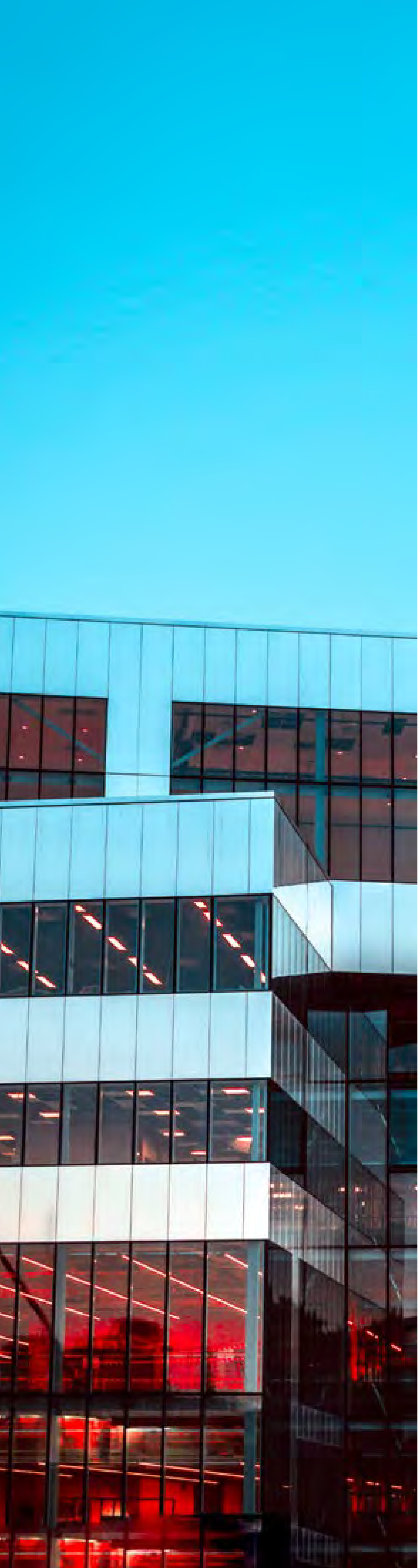
CREXI

National Trends Report

Q1 2023



INTRODUCTION

The first quarter of 2023 presented an uncertain start to the year, as occurrences in the financial sector and macroeconomic factors sent a cascade of concerns throughout the broader United States economy. Despite somewhat steady property valuations, some of this concern fell onto the shoulders of commercial real estate, pausing deal activity and requiring investors to more heavily scrutinize each acquisition before taking action.

The cost of capital increased again resulting from increased interest rates, and we're just starting to see the financial pressure cracks from the Fed's aggressive anti-inflationary measures and the evaporation of stimulus measures. However, real estate fundamentals in many sectors and markets remain solid. These times of uncertainty and ongoing talk of a recession may unearth long-term, value-add opportunities for watchful commercial real estate stakeholders.

Comprehensive, data-powered information is an essential tool in investor and broker arsenals. We aim to provide the most valuable insights and trends to shed light on the undercurrents of commercial real estate activity, with an eye toward the sector's future. Our quarterly overview report dives into transaction and leasing activity on Crexi throughout Q1 2023, considering quarterly metrics and year-over-year data, so that CRE stakeholders can approach any coming storm with the most informed strategies possible.

WHAT HAPPENED IN Q1 2023

Bank failures caused concern as broader economic implications are still being assessed.

In March, the closures of high-profile regional banks, including Silicon Valley Bank and Signature Bank, triggered alarm throughout various financial sectors. The factors surrounding these failures are highly complex, but one of the broader implications is that capital providers are scrutinizing commercial real estate more closely.

The closures of these banks have triggered a need to examine and potentially tighten lending requirements, which, combined with rising interest rates, could result in a slowing velocity of investment activity in the space. Regional banks house as much as 70% of commercial real estate's $2.9 trillion in loans. As some of this property debt comes due by the end of 2025 or sooner – particularly on assets such as long-vacant offices and larger malls – some banks may have to sell portfolios at a loss.

> **We're long-term confident in commercial real estate, especially in an ecosystem where data and access are increasingly available to industry stakeholders. Information will be key to timing market turns, and those who are best prepared to make opportunistic decisions are the ones most likely to yield strong ROI after weathering a down cycle."**
>
> *- Mike DeGiorgio, CEO, Crexi*

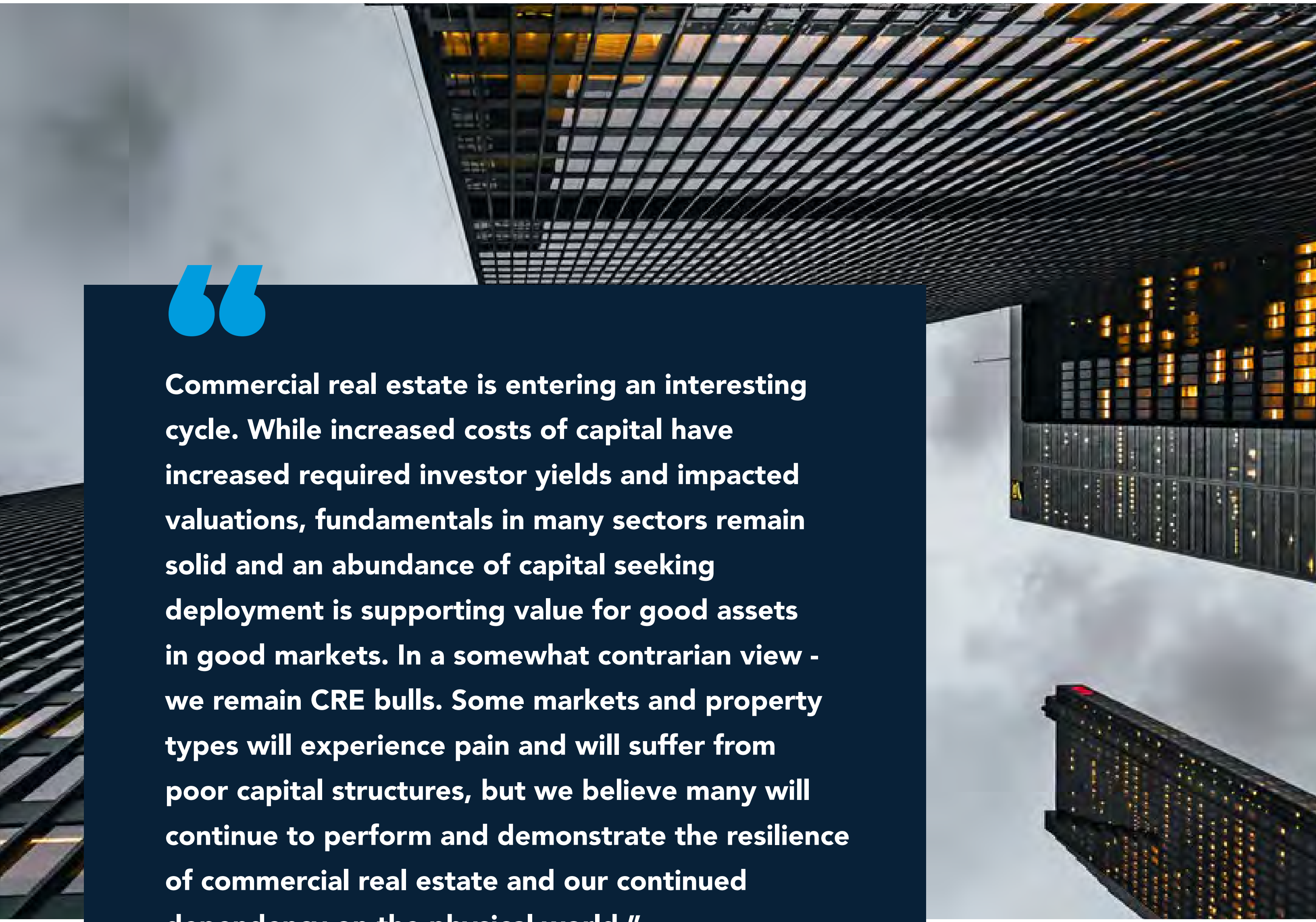
We do not consider these banking issues as cause for alarm bells, as the industry spans many sub-sectors with solid fundamentals that vary from market to market. Multifamily housing, for example, has consistently been in high demand due to housing shortages in recent years, and retail has proven remarkably resilient.

There are also many potential opportunities to acquire well-positioned assets at a discount, so the time to shore up capital and relationships with lenders is now. Opportunities such as office conversions and mixed or adaptive-use redevelopments are hot topics in a post-pandemic landscape, with plenty of room for savvy investors to participate.

Rising interest rates strained CRE activity, but Fed hikes seem to be nearing their peak.

The Fed continued increasing interest rates in Q1 to a range of 4.75-5% in late March, with officials forecasting one more rate increase this year. Policymakers continued to focus on managing inflation and maintaining hiring levels but indicated their concern with overdoing rate hikes in the wake of banking distress. Economic signs indicate a likely slowdown in hikes soon: March's job report saw unemployment rates continue to shrink but at a lesser velocity, showing signs of a slightly leveling labor market.

The impact of rising rates on commercial real estate deal velocity continued through the first quarter, slowing valuation growth and lengthening the deal-making process, especially as lenders started buckling down on deploying capital. Many economists have asked the Fed to adjust their rate-hiking strategies in the wake of the banking events, and there's hope that more moderate holding or even decreases in rates will be forthcoming.



"Commercial real estate is entering an interesting cycle. While increased costs of capital have increased required investor yields and impacted valuations, fundamentals in many sectors remain solid and an abundance of capital seeking deployment is supporting value for good assets in good markets. In a somewhat contrarian view - we remain CRE bulls. Some markets and property types will experience pain and will suffer from poor capital structures, but we believe many will continue to perform and demonstrate the resilience of commercial real estate and our continued dependency on the physical world."

- Eli Randel, COO, Crexi

Tighter lending underwriting practices constricted commercial activity, so stakeholders got creative.

Because of the high cost of capital and a potential clamp down on lending practices, it's more important than ever for CRE stakeholders to conduct thorough due diligence and get their ducks in a row when sourcing funding. Even without additional rate hikes, a wall of refinancing will likely [drive lending rates] to as high as 4.5% higher than many existing mortgages.

Making friends with your lenders and financial teams is essential, as forbearance and workouts can be crucial steps in many investors' arsenals. Meet with your core team consistently and [keep conversations flowing]. Some investors are also exploring [creative financing solutions] as alternative strategies to keep deals moving and ensure more solid equity footing. While much of this is pressuring valuations, many commercial real estate subsectors and market fundamentals remain strong and will still serve as a valuable, long-term financial vehicle.

COMMERCIAL REAL ESTATE NATIONAL SALES TRENDS

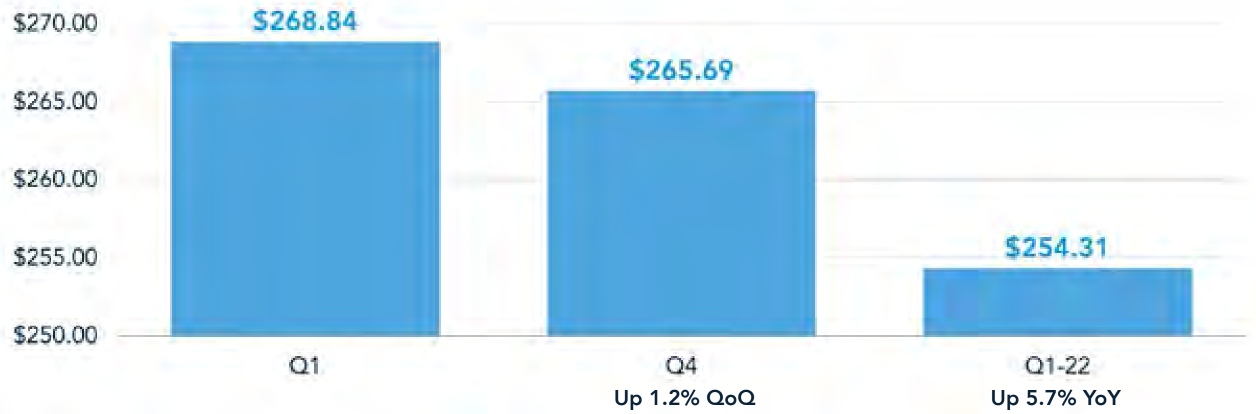
On Crexi's platform, overall average valuations and investor activity rose in early 2023, but fewer assets closed than in the previous quarter. Investors eagerly sought commercial property on our platform, with stunning gains in searches, reaching out to sellers, and indicating motivated interest in acquiring assets.

However, the disparity between the number of actions leading up to purchase and the actual volume of closed assets belies how much more stringent underwriting and due diligence requirements have slowed sale velocity. Investors were still seeking to trade but generally paused their deal-making activity as a natural byproduct of more extended discovery periods, lending crunches, and a general caution awaiting the unfolding of a potential recession.

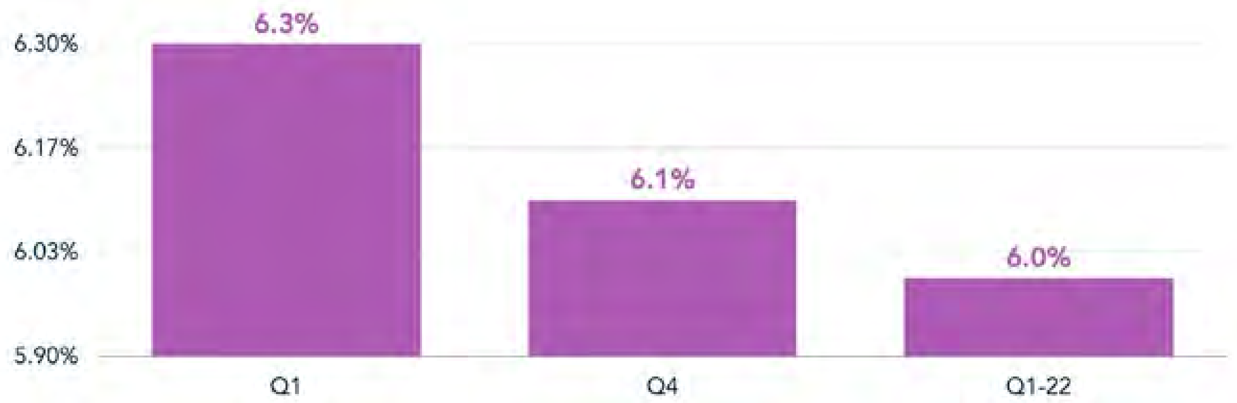
From an investment philosophy perspective, commercial real estate remains a strong hedge amid other short-term economic uncertainties. Not all asset classes are weathering current economic uncertainty well, with offices most impacted by a climate of rising rates, stricter lending practices, and investor fears. However, other asset classes, such as multifamily and warehouses, buoyed the overall commercial real estate sector to higher average valuations in Q1 as investor interest continued to pour in.

What the Data Says

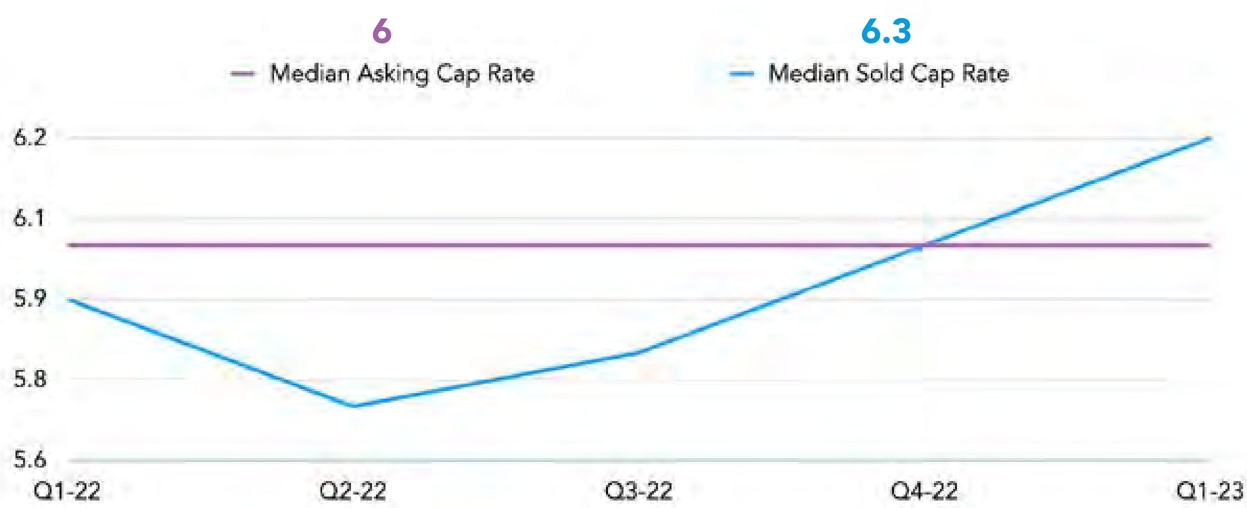
Average Asking Price per SF and Changes Over Time



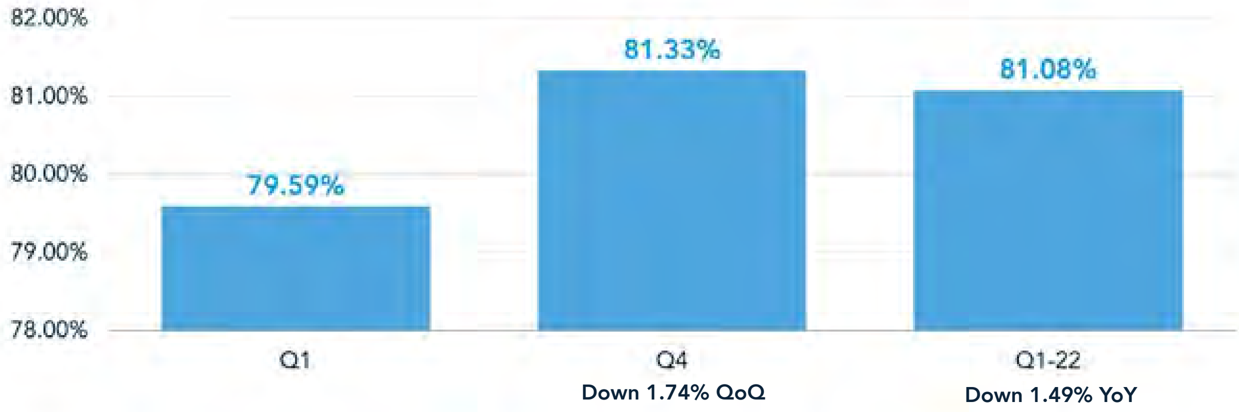
Median Sold Cap Rates



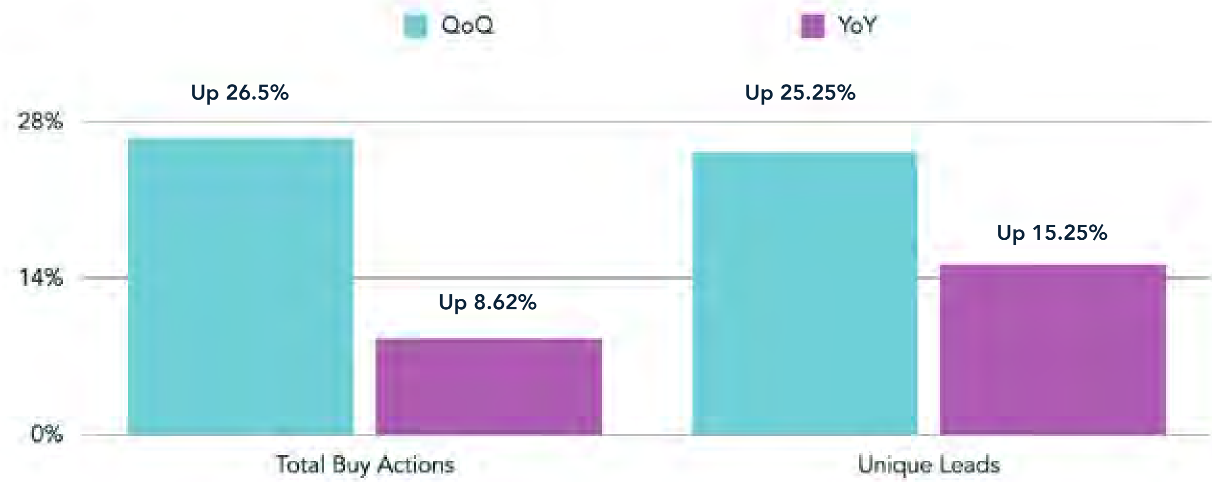
Median Asking vs. Sold Cap Rate Over Time



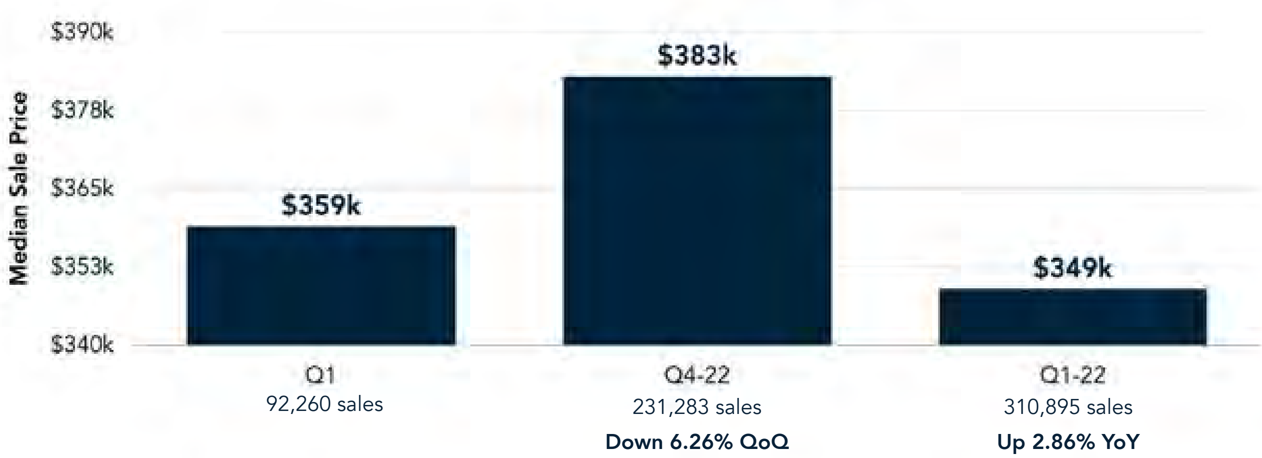
Average Occupancy and Changes Over Time



Buyer Activity, Leads and Changes Over Time



Transaction Volume, Median Sold Pricing, and Changes Over Time



Key Insights

We observed noticeable surges in investment activity in the first quarter, with buyer activity and unique leads up over 26% and 25%, respectively, across sectors. Offer movement dipped, showing how tighter lending practices have stymied investor intent to acquire assets and complicated access to capital. Establishing good terms with lending and financial partners or exploring alternative capital sources will be essential for investors as banks sort through the fallout of current banking crises.

Regional Trends

Cities with Highest Asking Price per SF in Q1

City	Price per SF	Cap Rate
Santa Barbara	$743.25	4.55%
New York	$683.91	4.47%
San Jose	$557.14	5.44%
San Francisco	$556.00	5.01%
Boston	$550.89	6.21%
Miami	$479.73	4.93%
Nashville	$479.73	5.7%
San Diego	$458.02	3.86%
Raleigh	$451.58	4.52%
Austin	$446.37	5.87%

Cities with Most Pricing Growth in Q1

City	Price per SF	% change QoQ
Buffalo	$159.41	53.10%
Providence	$247.76	41.13%
Sacramento	$297.52	31.15%
Boston	$550.89	29.97%
Riverside	$439.86	27.89%
Louisville	$211.94	27.59%
Chicago	$252.17	27.18%
Nashville	$479.73	26.10%
Birmingham	$289.93	22.61%
Kansas City	$211.02	21.19%

Cities with Highest Cap Rates in Q1

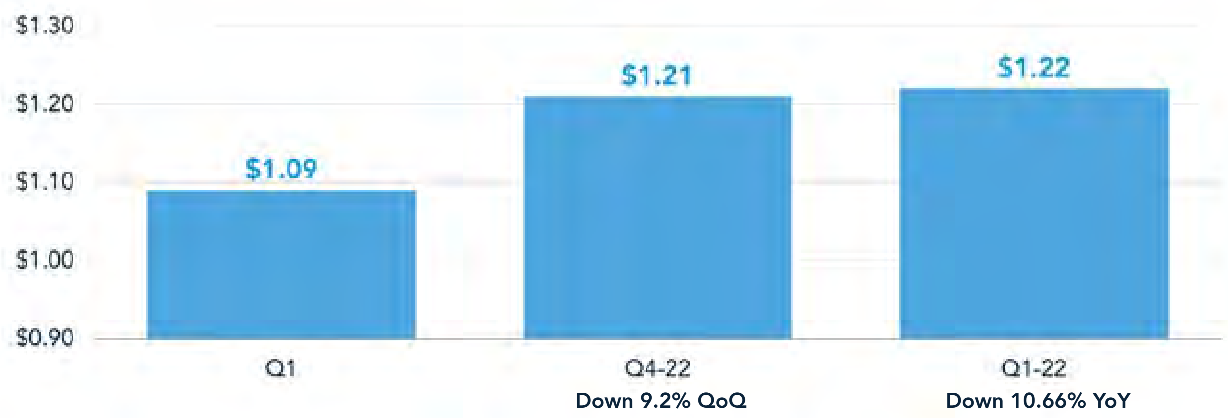
City	Cap Rate
Cleveland	9.27%
Milwaukee	9.24%
New Orleans	8.43%
Detroit	7.83%
Cincinnati	7.78%
Kansas City	7.49%
St. Louis	7.45%
Indianapolis	7.22%
Memphis	6.80%
Buffalo	6.77%

COMMERCIAL REAL ESTATE NATIONAL LEASING TRENDS

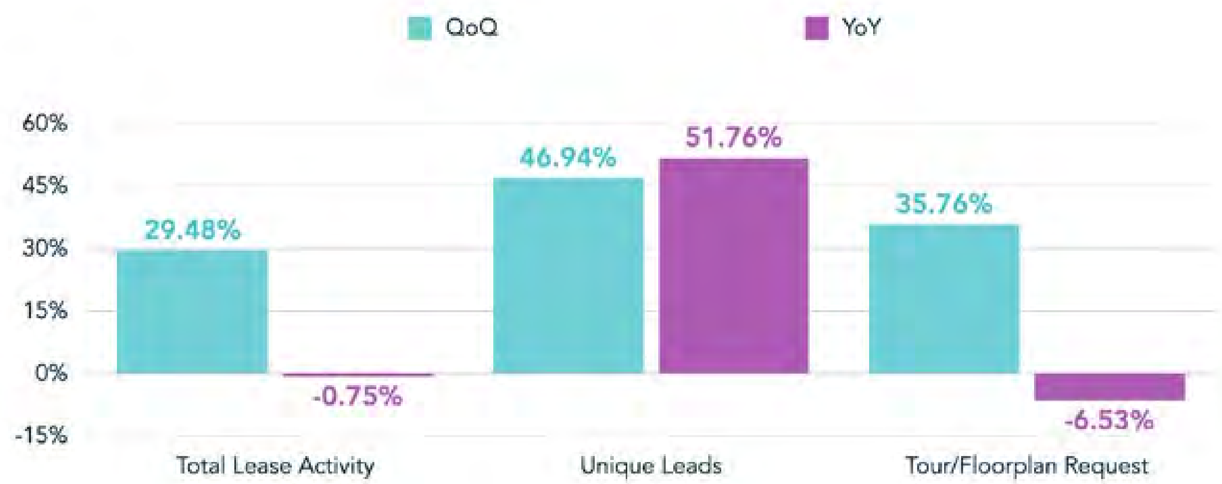
For-lease assets on Crexi experienced harsher weather conditions than their sales counterparts, with asking rates trending down across most asset classes. Interestingly, the number of people searching for leasing space displayed remarkable gains. This is likely due to many people coming up on expiring terms, either staying to negotiate their leases or searching for new spaces. But despite increased demand, economic concerns are pausing the signing of contracts, and more and more vacant space in competition is driving down tenant revenue.

What the Data Says

Average Asking Rate per SF per Month and Changes Over Time



Lease Activity, Unique Leads, Tour/Floor Plan Requests, and Changes Over Time



Key Insights

Retail assets were largely responsible for the decrease in overall asking rents. The sector experienced an 18% drop in average asking rents for Q1-added listings, which paralleled a 20% increase in overall available inventory. This has had little impact on retail valuations, according to data from the sales side of our platform, which posted no change in pricing from the previous quarter. Consumers continued to spend in Q1, though there are some signs that a 6% consumer pricing index increase in February and a slowing in consumer expenditure in specific sectors revealed that rate hikes were working as intended to slow inflation.

Otherwise, other sectors posted little-to-no change in asking rates while demand galloped ahead, coming out of the slow Q4 holiday season. Tenant activity surged by nearly 30% in the first quarter of 2023, indicating a renewed sense of urgency for capturing space and locking in contracts before any potential rate increases. This shuffling of space also appeared in falling occupancy rates, which dipped below 80% (79.6%) in Q1 for the first time since Q1-2021. While some have left behind vacant offices, more of these departing tenants aren't departing the market altogether. Many are seeking better opportunities to consolidate operational costs and weather potential economic storms.

Regional Trends

Cities with Highest Average Asking Rents in Q1

City	Monthly Rate per SF	% Change QoQ
Birmingham	$1.59	12.92%
Providence	$1.58	-2.03%
Richmond	$1.56	11.95%
Cleveland	$1.52	29.97%
Raleigh	$1.49	-8.88%
Seattle	$1.49	0.25%
Memphis	$1.48	42.77%
Santa Barbara	$1.45	-1.37%
Orlando	$1.42	15.70%
Tampa	$1.41	-11.55%

Cities with Highest Rent Growth in Q1

City	Monthly Rate per SF	% Change QoQ
Memphis	$1.48	42.77%
Cleveland	$1.52	29.97%
Oklahoma City	$1.30	20.18%
Riverside	$1.09	17.33%
Orlando	$1.42	15.70%
Los Angele	$1.08	15.44%
Birmingham	$1.59	12.92%
Richmond	$1.56	11.95%
Denver	$1.34	9.37%
St. Louis	$1.25	8.64%

FINAL THOUGHTS

While elements of Q1's commercial real estate performance concern some, there is the longer-term success of the sector to consider when evaluating the asset class' health. Only minute dips in CRE valuations and healthy signs of investment and tenant activity indicate there's no less demand for the sector, simply that complications make transparency and proactive relationships between broker, investor, lender, and all parties more crucial than ever. Commercial real estate remains, as ever, an inherent long-hold investment vehicle, and we're long-term bullish on the sector yielding healthy ROI for those who stick to their guns. By keeping an eye overhead and watching for the best opportunities to appear, fortune may very well favor the bold.

METRICS AND METHODOLOGY

This article relies on data from [Crexi's marketplace](). In particular, to ascertain timely and representative trends in seller sentiment, this article focuses on offering metrics, such as average asking price per square foot, cap rate, and monthly rents, in addition to listed occupancy, tenancy, and square footage. Using these listing-based metrics and changes therein, we can use seller expectations at the time of listing to approximate overall valuation trends.

While these data aggregations may broadly reflect prevailing market conditions, it is essential to note that variations can also be affected by inventory changes, asset size, etc. We pair these data points with internal data from Crexi buyers on search trends and acquisition-related actions performed on Crexi to provide a holistic understanding of where both sides of commercial real estate are headed.

DISCLAIMER

TERMS

Occupancy: The percentage of occupied square feet in a building.

Absorption: A measurement of the net change of the supply of commercial space in a given real estate market over a specific period of time. Total absorption is new square footage leased by tenants minus vacated square footage vacated by tenants and made available on the CRE market.

Asking Price per Square Foot: The asking price per square foot of a building for sale.

Asking Rate per Square Foot: The landlord's asking rent rate per square foot for a building or market.

Asset Type: Also called "Asset Class" or "Property Type," one of four main categories in commercial real estate: retail, industrial, multifamily, and office. Also can refer to smaller categories including land, hospitality, etc.

Asking Cap Rate: Net Operating Income divided by the Asking Price.

Vacancy Rate: The rate of vacancy in the listed property.

Buyer Activity: Acquisition-related actions taken by users on Crexi sales property pages.

Buyer Searches: Internal site searches taken by users on Crexi sales or lease.

Lease Activity: Leasing related actions taken by users on Crexi lease property pages.

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