Real Estate Forecast 2010

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One thing is certain: the commercial real estate forecast for 2010 remains uncertain.

Many real estate professionals and experts continue to predict that commercial real estate values, deals, and prospects for 2010 will probably get worse before they get better. Michael Kurtzon, a member of Dykema's Real Estate Group and a recent panelist at the Illinois Real Estate Journal's 8th Annual Commercial Real Estate Forecast Conference in Chicago, Illinois, noted, "Until the underlying reasons for the lack of liquidity in the capital markets are addressed and credit again becomes available, we will continue to spend most of our time dealing with troubled assets in short-term loan extensions, workouts where possible, and foreclosures. When no one can agree on the value of a project, or even how to value it, making a deal is a daunting challenge."

Unlike in 2009, there is a bright spot: declines in values will not likely drop as fast or as severely as they did in 2009, and increased rents will help to offset the overall property declines in 2010. Credit availability is still the big unknown that will be the driving force in determining how quickly these commercial sectors will bounce back. Despite the uncertainty, reports suggest there are signs of hope. According to Grubb & Ellis, we can expect the four core property types to recover in the following sequence: multi housing, industrial, retail, and office. The forecast for each of these sectors as reported by the latest Commercial Real Estate Outlook published by the National Association of Realtors ("NAR Report"), Finch Ratings, and Grubb & Ellis is briefly summarized below:

Multi Housing: We can expect a stable outlook for multifamily REITs in 2010, with access to attractive, low-cost financing from Fannie Mae and Freddie Mac (Fitch Ratings, 2010 Outlook Report). Further, apartments are forecasted to benefit from the return of homeownership rates to "pre-bubble" levels (Grubb & Ellis 2010 Forecast Report), and multifamily vacancy rates will likely remain steady, from 7.3 percent in the third quarter of 2009 to 7.4 percent in the third quarter of this year (NAR Report).

Industrial: Of the four core property sectors, industrial depends the least on job creation, which will benefit this sector as unemployment levels remain high (Grubb & Ellis 2010 Forecast Report). The Fitch Ratings, 2010 Outlook Report predicts a negative outlook for industrial REITS, with above-average leverage and slow economic recovery reducing overall productivity and the need for space. According to the NAR Report, vacancy rates will rise from 13.5 percent in the third quarter of 2009 to 15.4 percent in the third quarter of 2010, but industrial rent will fall, as net absorption tracked in 58 markets is predicted to go from negative 298.7 million square feet in 2009 to negative 140.5 million square feet in 2010.

Retail: Retail vacancy rates are predicted by the NAR Report to rise from 12.2 percent in the third quarter of 2009 to 13.0 percent in the third quarter of 2010. Similar to the trend for the industrial market, however, the NAR Report predicts that the average retail rents will decline, with net absorption of retail space (tracked in 53 markets) increasing from negative 21.9 million square feet in 2009 to negative 4.7 million square feet in 2010. Fitch Ratings predicts a negative outlook for retail REITS, with additional store closures. Retail sales are predicted to be flat to up slightly from 2009, and according to Fitch Ratings, this means soft consumer demand as a result of high unemployment rates (among other things). Grubb & Ellis reports that retail's recovery will be slowed as a result of consumer conservatism and attention to value, particularly the increase in the saving rate of consumers from near zero in recent years back to around 5 percent or more.

Office: This sector appears to fare the worst among commercial real estate watchers, with unemployment being the pivotal factor. Grubb & Ellis forecasts the office market will not return to health until employers begin hiring again—a broad-based resumption of hiring is not expected to begin before the second half of next year. According to the NAR Report, office sector vacancy rates are expected to rise from 16.1 percent in the third quarter of 2009 to 18.5 percent in the third quarter of 2010, again due to continual job losses. Similarly, unemployment is the cause of the poor health of office REITs, which are not expected to improve until we see a reduction in unemployment levels.

Overall, real estate watchers are predicting a fall in prices but are saying they do not have much further to fall nor will they fall as quickly as they did last year.

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