

20 FAST FACTS FOR THE BIG PICTURE

the BRIEFING



Tom McNearney, Transwestern chief investment officer, examines economic data, news reports and industry trends to determine the near- and long-term impact on commercial real estate investment and development.

APRIL 2017

ECONOMIC SNAPSHOT

Of the many tax changes under discussion, six measures pose material implications for commercial real estate. If passed, these options would:

- Reduce the top corporate tax rate from 35% to 20%
- Allow immediate, full deduction of capital investment expenditures
- Eliminate interest deductibility on future loans
- Allow net operating losses to carry forward indefinitely
- Eliminate 1031 exchanges
- Tax carried interest on capital gains as ordinary income

Elimination of interest deductibility is a particular concern for investors, although a reduced corporate tax rate could mute its impact. Yet it is difficult to imagine that President Trump, the all-time black belt in commercial real estate borrowing, would eliminate interest deductibility. Despite the endless number of prognosticators, it is impossible to predict what this new administration will accomplish.

Even as waning confidence in the political system feeds uncertainty, economic confidence is rising amid ebbing volatility. As expected, rising employment and wage growth combined to drive a 3.9% increase in personal consumption, or consumer spending on goods and services. That purchasing activity helped to drive up inflation and manufacturing, with U.S. factories stepping up output each of the past six months through February. Corporate profits have also improved and are expected to surprise on the upside for the first quarter.

Studies suggest that commercial real estate outperforms other asset classes in a rising-interest-rate environment, particularly when markets avoid overbuilding, so look for continued good performance in 2017.

20 FAST FACTS

- 1** Total retail sales, or the dollar value of merchandise sold nationwide, increased 5.6% year-over-year in 2016 and online sales climbed 12%, reflecting job and wage growth.
- 2** Italy downgraded to BBB credit by DBRS, having already lost single-A ratings with Moody's, Standard & Poor's and Fitch.
- 3** The Dallas area added 95,300 jobs in 2016 to top the nation with 3.9% growth, more than double second-place New York's 1.5% rate with 100,400 new jobs.
- 4** The Eurozone's 15th consecutive GDP gain, at 1.8% in the fourth quarter, rivals the U.S.'s 1.9%. Year over year, the Eurozone actually edges out the U.S., 1.7% to 1.6%.
- 5** Household debt rose by \$226B in the fourth quarter, just \$99B short of the \$12.7T peak in third quarter 2008.
- 6** U.S. auto debt hit a record \$1.16T in the fourth quarter, or \$6,100 per licensed driver. Subprime borrowers tapped \$244B for cars in the past two years, the most since 2006 - 2007.
- 7** Several CMBS deals have effectively accommodated the new 5% risk retention rules, supporting all three structures: Horizontal, vertical and L-shaped.

CIVILIAN UNEMPLOYMENT RATE

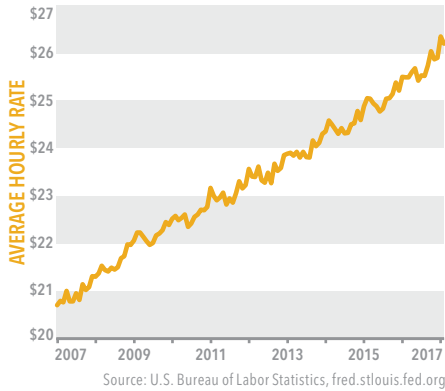
FEBRUARY 2007 – FEBRUARY 2017



Source: U.S. Bureau of Labor Statistics, fred.stlouis.fed.org

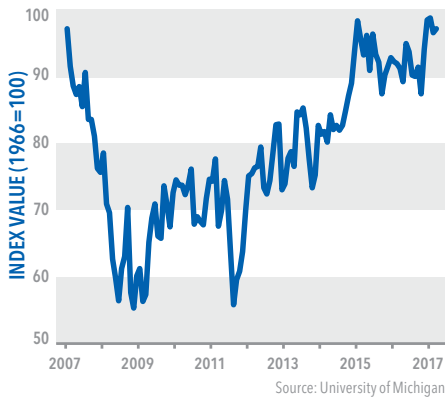
HOURLY EARNINGS

FEBRUARY 2007 – FEBRUARY 2017



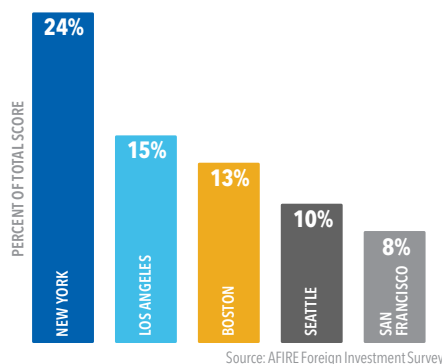
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JANUARY 2007 – MARCH 2017



TOP FIVE U.S. CITIES FOR FOREIGN REAL ESTATE INVESTMENT

2017



- 8 Existing home sales slowed to an annualized rate of 5.48M units in February after January's decade-topping 5.69M, squeezed by 21 months of diminishing inventory. February outpaced year-ago sales by 5.4%, and a 3.8-month supply of unsold homes will likely drive further price increases.
- 9 Overall, America's infrastructure scored a D+ in the American Society of Civil Engineers' 2017 Report Card, which rates the physical condition and needed investments by infrastructure category.
- 10 CRE private equity fundraising reached \$108B in 2016, with the 10 largest funds comprising 36% of the total.
- 11 Blackstone Group raised \$1.54B on its Invitation Homes public offering, assembled by spending more than \$108B on foreclosed homes to become rentals. Invitation Homes has 48,431 houses in 13 markets, vying with rental home rivals American Homes 4 Rent and Colony Starwood Homes.
- 12 The Moody's/RCA Commercial Property Price Indices have more than doubled since 2009 and stand 23% above the pre-crisis level. Federal Reserve officials are following apartment towers as a potential asset-price bubble.
- 13 Some 95% of surveyed Association of Foreign Investors in Real Estate members plan to maintain or increase their commercial real estate holdings in 2017. Washington, D.C., has fallen from 8th to 15th place as a preferred city for investment, while industrial is the favored property type.
- 14 Real Capital Analytics tracked \$489B in commercial real estate sales in 2016, down 11% from a year ago; volume dropped 20% during the fourth quarter/election season.
- 15 A new study by MIT and Boston University professors suggests that robots are winning the race for U.S. jobs, replacing 670,000 manufacturing workers since 1990.
- 16 Former Treasury Secretary Larry Summers said job destruction caused by technology is something we have been living with for two generations. He predicts that by mid-century, at any given moment 25% of men aged 25 to 54 will not be working.
- 17 The day the Federal Reserve announced a 25 basis-point rate increase, the 10-year note rate fell to 2.5%.
- 18 Mezzanine lenders expect a strong year from a \$109B wave of CMBS loans maturing this year amid a pull-back from banks and conduit lenders.
- 19 Moody's rates 19 retailers – or 13.5% of the retailers it covers – as a speculative or poor credit risk, vs. 5.6% in 2011 and 16% in 2009, during the Great Recession.
- 20 The Consumer Price Index climbed 2.5% in January from a year earlier, the largest year-over-year pricing increase since March 2012, but slowed its climb in February.