ValTrends
1Q 2023 Report

Since 1931, the most trusted investment analysis in the commercial real estate industry.

Capital Dislocation

SitusAMC

In first quarter 2023, the 10-year Treasury rate was up 165 bps year-over-year (YoY) following ten consecutive Fed funds rate increases. This has resulted in ***capital dislocation*** *as sharp declines in transaction volume leads to lack of clarity on property values. Negative leverage is a concern given the high cost of capital and investors are increasingly willing to walk away from a property with debt. Capital generally remains on the sidelines as market uncertainty is causing pause in investors' willingness to participate in the markets.*

Investor preference for the commercial real estate (CRE) asset class dropped for the fifth consecutive quarter to a record low, blaming the short-term economic uncertainty and declining CRE values for the decrease. This uncertainty has propelled investors' recommendation to hold CRE. The recommendation to hold increased from 80% to 91% in first quarter. It was the highest hold endorsement since RERC began collecting these data in 1996 and about double the level seen during the Global Financial Crisis (GFC). Investors were least likely to recommend buying; preference for the strategy fell 6 percentage points QoQ to 3%. The recommendation to sell fell QoQ from 11% to 6%. The recommendation to buy and sell were at record lows and about 20 percentage points and 10 percentage points below GFC levels.

Amid the capital markets upheaval, the availability of capital dropped for the sixth consecutive quarter to the lowest level since the GFC. Underwriting standards were rated as the most restrictive since the GFC. Investors note that the high interest rates, uncertain economic outlook, challenges in the banking sector and volatility of CRE pricing are making lenders extremely selective and equity capital will likely be difficult to obtain until the market has a better understanding of the new normal in the financial and capital markets.

First quarter spreads between RERC real estate yields and the 10-year Treasury and corporate bonds were among the narrowest since the GFC. The first quarter CRE yield over 10-year Treasury spread was almost 180 bps below the long-term average (LTA). First quarter real estate yield spreads over Moody's Baa and Moody's Aaa spreads were 150 bps and 110 bps below the LTA.

Transaction volume slowed again in first quarter with substantial quarterly declines across all major property types, except for retail. First quarter overall CRE transaction volume, as measured by MSCI Real Assets, was $85 billion, the weakest first quarter since 2014 and down 77% from the peak in fourth quarter 2021. The National All-Property RCA CPPI, a gauge of property prices, was down 5.1% in first quarter, the largest quarterly decline in prices since the GFC. Prices were down almost 10% from their peak in second quarter 2022. NCREIF NPI overall CRE total returns improved 170 bps QoQ, but remained in negative territory. First quarter returns were the second lowest since the GFC and capital appreciation has been negative for three consecutive quarters. One-year trailing total returns were -1.6%, down 720 bps QoQ. It was the first time one-year trailing returns were negative since the GFC.

The office segment continues to be the least favored sector by investors. Not a surprise given that more than half of companies with U.S. offices plan to shrink their footprint over the next three years. Demand for office space remains weak with the occupancy rate decreasing 20 bps to a record low in first quarter, according to Reis. The ongoing decline in office occupancy is noteworthy given the continued growth in employment, notwithstanding high profile tech layoffs. Tenant renewals and re-leasing will continue to be an issue along with declining net operating incomes (NOIs) and increasing tenant improvement (TI) costs, according to investors. Market sentiment has weakened and perceived recession fears place upward pressure on investors required returns. With remote and hybrid work continuing for the foreseeable future, there is limited demand, especially for CBD offices.

01

CAPITAL MARKET VALTRENDS

Capital Dislocation Persists in First Quarter

Economy & Financial Markets

GDP slowed to an annual rate of 1.3% in the first quarter of 2023 (second estimate), down from fourth quarter's rate of 2.6%. The deceleration in first quarter was primarily attributable to reductions in private inventory investment and nonresidential fixed investment.

The labor market continues to be robust. In May, the economy added 339,000 jobs, near the monthly average of the year prior. The unemployment rate rose 30 bps to 3.7%, the highest since October 2022, but still historically low. The labor force participation rate was steady at 62.6%, up 20 bps from the beginning of the year, but 70 bps below the pre-pandemic rate. Wage growth slowed, easing inflation fears.

Inflation continues to cool from last year's fervent pace. The consumer price index (CPI) slowed throughout first quarter from 6.3% in January to 5.0% in March. April's rate was 4.9%, the lowest since April 2021. Core CPI, which excludes food and energy, was 5.5% in January and February. Core CPI ticked up to 5.6% in March, but returned to 5.5% in April, the lowest since December 2021. Core personal consumption expenditures (PCE), the Fed's preferred inflation measure, slowed from 4.7% in January to 4.6% in March. However, it ticked back up in April to 4.7%.

In May, the Fed raised rates for the tenth consecutive time since March

CRE & Investment Alternatives

	YTD[6]	1-Year Trailing	3-Year Trailing	5-Year Trailing	10-Year Trailing	15-Year Trailing
NPI[1]	-1.8%	-1.6%	7.2%	6.7%	8.3%	6.3%
NFI-ODCE[1]	-3.4%	-3.9%	7.5%	6.6%	8.5%	5.0%
NAREIT Index (All Equity REITs)[2]	1.7%	-19.4%	10.2%	6.3%	6.5%	6.7%
Consumer Price Index[3]	0.2%	5.8%	5.2%	3.9%	2.6%	2.3%
Dow Jones Industrial Average[2]	0.9%	-2.0%	17.3%	9.0%	11.1%	9.6%
Nasdaq Composite[4]	16.8%	-14.1%	16.6%	11.6%	14.1%	11.8%
NYSE Composite[4]	1.3%	-7.8%	14.3%	4.3%	5.4%	3.8%
S&P 500[2]	7.5%	-7.7%	18.6%	11.2%	12.2%	10.1%

	1Q 2023	1Q 2022	1Q 2020	1Q 2018	1Q 2013	1Q 2008
10-Year Treasury Bond[5]	3.6%	1.9%	1.4%	2.8%	2.0%	3.7%

[1]NCREIF NPI is a property-level (unleveraged) total return index, gross of fees; NCREIF NFI-ODCE is a fund-level (leveraged equity) total return index, net of fees.
[2]Based on total return index, and includes the dividend yield.
[3]Based on the published data from the Bureau of Labor Statistics (seasonally adjusted).
[4]Based on price index, and does not include the dividend yield.
[5]Based on average quarterly T-bond rates.
[6]Year-to-date (YTD) averages are not compounded annually except for CPI and NAREIT.
Sources BLS, Federal Reserve Board, S&P, Dow Jones, NCREIF, NAREIT, compiled by SitusAMC Insights, 1Q 2023.

2022. The pace of rate hikes slowed to 25 bps for each of the three decisions made in 2023. The federal funds rate was up 425 bps in May from a year prior and the highest rate since July 2007. The 10-year Treasury rate reached a 2023 peak of 4.1% in early March, about 20 bps below 2022's peak, but still among the highest rates since 2008. The average rate for April declined to 3.5%, but ticked up in May, ending the month at 3.6%. The Fed signaled it may pause interest rate increases at its June meeting.

Despite several bank failures, turbulence in crypto and ongoing uncertainty about a possible recession, stocks proved hardy, with the Dow, S&P 500 and Nasdaq notching gains of about 0.4%, 7% and 17%, in first quarter 2023, respectively. Gains were not steady; the indexes rose in January, but fell in February and early March – first due to fears that the Fed would keep interest rates higher for longer than anticipated and again after the collapse of Silicon Valley and Signature Banks. Stocks rose again in March and April after the Fed softened its stance on ongoing rate increases and better-than-expected corporate profits in April led to gains of 1.5% (S&P 500), 2.5% (Dow) and 0.4% (Nasdaq). Stock markets were mixed in May, even as the U.S. faced a potential debt default, with the Dow down 3.5% and the S&P 500 up 0.2%. May was a good month for the Nasdaq, rising almost 6%, over market enthusiasm about artificial intelligence.

Legislation suspending the debt ceiling for two years takes pressure off the bond and stock markets, as well as potential damage to economic growth resulting from a federal default.

Spreads between RERC real estate yields and the 10-year Treasury and corporate bonds expanded QoQ, with an increase in real estate yields and a decrease in bonds. Despite the increases, spreads were among the narrowest since the GFC.

The first quarter CRE yield over 10-year Treasury spread was almost 180 bps below the long-term average (LTA). First quarter real estate yield spreads over Moody's Baa and Moody's Aaa spreads were 150 bps and 110 bps below the LTA.

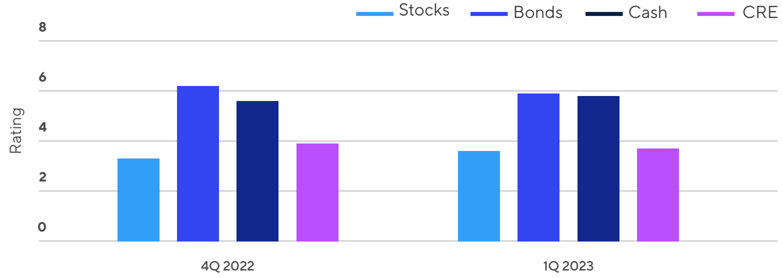
CRE & Investment Alternatives

With widespread uncertainty and interest rates hovering around 13-year highs, cash and bonds earned the top ratings for referred asset classes. Institutional investor preference for bonds had a slight edge over cash in first quarter.

The rating for bonds was the second highest since 2007, when RERC began collecting these data. Investors note that the relatively high interest rates that can be earned on short-term investment vehicles are very attractive in this period of uncertainty. Though the preference for cash was considerably higher than the LTA, ratings were well below what was seen in the early part of the pandemic and during the GFC. Still, many investors are concerned about macroeconomic risks and volatility in the stock market and thus prefer the risk-free returns on

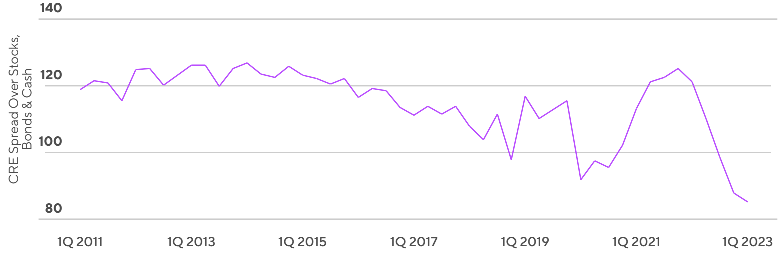
> "Cash talks, everybody else walks."
>
> - EAST REGION RESPONDENT`

Ratings of Investment Alternatives



Ratings are based on a scale of 1 to 10, with 10 being excellent.
Sources: RERC, SitusAMC Insights, 1Q 2023.

CRE Attractiveness Index[1]



[1]The RERC Attractiveness Index shows CRE investors' changing preferences for CRE over the traditional asset classes. The baseline of 100 indicates that investors feel traditional assets and cash, on average, are as attractive as CRE. Sources: RERC, SitusAMC Insights, 1Q 2023.

cash holdings.

The preference for CRE dropped for the fifth consecutive quarter to a record low. Investors blame the short-term economic uncertainty and declining CRE values for the decreased preference for the asset class. Stocks were the least preferred among the asset classes, with a slightly lower rating than CRE, citing market volatility as the culprit.

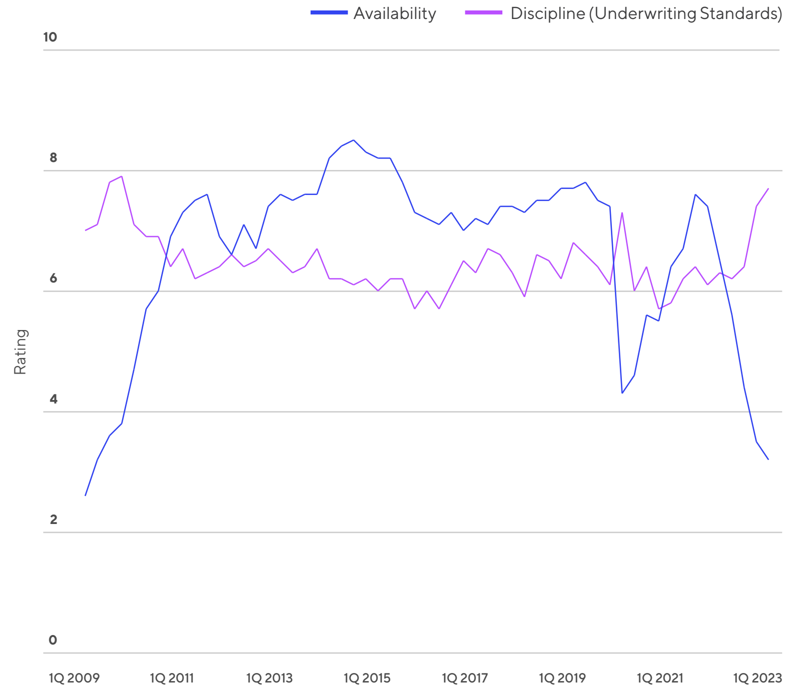
Availability & Discipline of Capital

Though the 10-year Treasury rate declined about 20 bps QoQ, first quarter interest rates were among the highest since 2010. Amid the capital markets upheaval, the availability of capital (equity and debt combined) dropped for the sixth consecutive quarter to the lowest level since the GFC. With a significant quarterly jump, underwriting standards were rated as the most restrictive since the GFC. Investors remark that the high interest rates, uncertain economic outlook, challenges in the banking sector and volatility of CRE pricing are making lenders gun shy about new commitments.

Equity capital availability remained the same QoQ at the lowest level since at least 2014 when RERC began collecting data on debt and equity capital separately. Debt availability declined substantially QoQ reaching a record low. Discipline of both debt and equity capital became more restrictive in first quarter, reaching record tight ratings. Investors remark that the availability of deal funds will likely decline as general market volatility

> "Lenders have pulled in their welcome mats."
>
> - EAST REGION INVESTOR

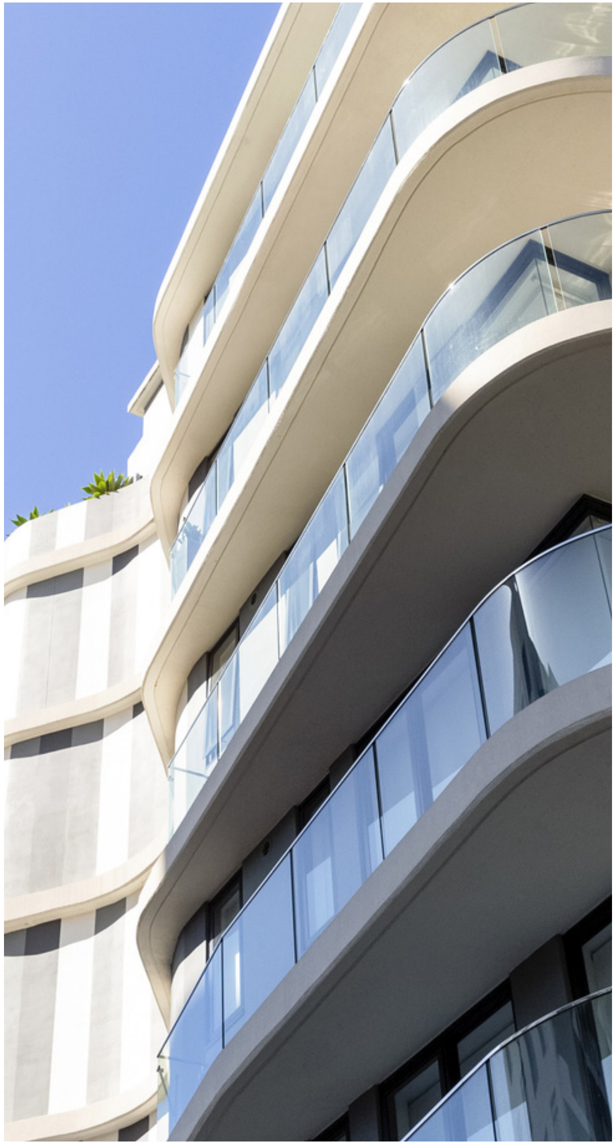
Historical Availability & Discipline of Capital – Equity & Debt Combined



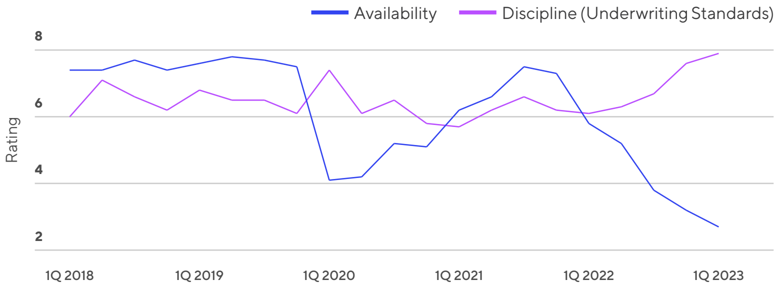
Ratings are based on scale of 1 to 10, with 10 being excellent.
Sources: RERC, SitusAMC Insights, 1Q 2023.

continues to increase. Also, the rise in the federal funds and interest rates combined with concerns about bank liquidity are causing lenders to reduce activity and causing debt costs to rise.

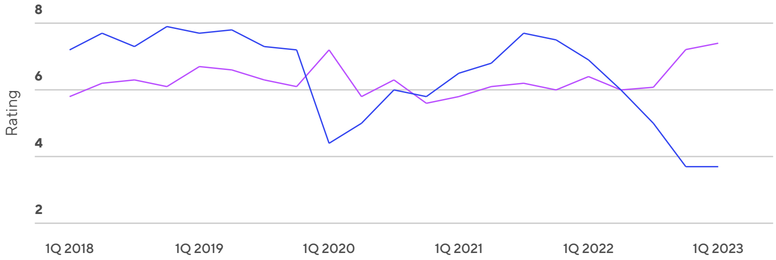
Concerns about a potential recession has many lenders pulling back; investors note that it has become very difficult to secure debt, and that debt is expensive. Also, underwriting standards are getting tougher with the rising cost of capital so investors are having to provide more equity and returns are dropping. Lenders are hyper-focused on the credit worthiness and liquidity of borrowers, debt service coverage ratios and the quality of assets.



Historical Availability & Discipline of Capital – Debt



Historical Availability & Discipline of Capital – Equity



Ratings are based on scale of 1 to 10, with 10 being excellent.
Sources: RERC, SitusAMC Insights, 1Q 2023.

CRE Returns, Volume & Pricing

Returns

NCREIF NPI overall CRE total returns improved 170 bps QoQ, but remained in negative territory. First quarter returns were the second lowest since the GFC. Income returns topped 1.0% for the first time since fourth quarter 2021. First quarter marked three consecutive quarters of negative appreciation. One-year trailing total returns were -1.6%, down 720 bps QoQ; it was the first time one-year trailing returns were negative since the GFC.

Hotel had the strongest first quarter returns among the main property types at 2.3%, despite slowing 110 bps. Hotel and retail were the only two property types with positive returns in first quarter. However, hotel has not been able to claw back its pandemic losses despite two years of positive growth. One-year trailing returns were over 10.5%, the top performing segment by far and among the highest in seven years and 470 bps higher than the LTA.

Retail had the second highest returns in first quarter, rising 110 bps QoQ, according to NCREIF. Retail and industrial were the only two property types with an increase in returns in the first quarter. Though total returns were nearly 150 bps lower than the LTA, income returns were the highest in eight years. One-year trailing returns were 1.0%, the lowest in nearly two years and almost 780 bps below the LTA. Regional and super regional malls performed the best among the retail subtypes, at 0.8% and 0.9%, respectively. Single tenant was the worst performing retail subtype at -1.8%.

Industrial returns improved from their weak fourth quarter performance by over 270 bps. Nevertheless, returns were second worst since the GFC after the fourth quarter's drop, declining 0.8%. One-year trailing returns were 2.4%, a record low since the GFC. Still, the one-year trailing return was strong enough to place second among the major property types. All industrial subtypes experienced a quarterly increase in total returns except for manufacturing. R&D was the best performing industrial subtype in first quarter at 1.0%. Flex was the worst performing subtype at -1.1%.

Apartment total returns were -2.1% in first quarter, a decline of 110 bps QoQ. It was the second lowest quarterly return since the GFC, trailing only last quarter's return. One-year trailing returns were negative for the first time since the GFC at -0.4%. Among the apartment subtypes, low-rise was the top performing in first quarter despite having a negative return of 1.6%. Garden apartments were the best performing subtype on a one-year trailing basis; high-rise apartments were the worst performing, with a total return of -1.7%.

Surprisingly, office total returns, as measured by the NPI, increased by over 70 bps QoQ and income returns were the highest in nearly five years. However, the first quarter total return was still the worst among the property segments at -4.1%. It was the second lowest return for the segment since the onset of the GFC, trailing only the previous quarter's abysmal return. Office was also the worst performing sector on a one-year trailing basis at -8.8%, the lowest one-year trailing return since 2010. CBD office performed worse than suburban office in first quarter, but both subtypes were strongly negative at -5.0% and -3.0%, respectively.

Volume

Deal activity slowed again in first quarter with substantial QoQ declines in transaction volume across all major property types, except for retail. First quarter overall CRE transaction volume, as measured by MSCI Real Assets, was $85 billion, the weakest first quarter since 2014, but well above the activity seen during the GFC. Volume has declined steadily for three consecutive quarters and is currently down 77% from the peak in fourth quarter 2021. However, first quarter 2023 volume was on par with the first quarter LTA (between 2001 and 2023). Individual transactions comprised the bulk of transactions in first quarter at 76%, compared to the LTA of 72%. At less than 14%, the proportion of transaction volume from portfolio sales has declined for the last three quarters to the lowest since 2003.

Apartments accounted for the greatest share of deal volume in first quarter at 30%; however, it was the lowest percentage since 2015. Volume declined by almost 52% QoQ to about $25.5 billion. It was the lowest quarterly deal volume since second quarter 2020 and down about 85% since the peak in fourth quarter 2021. Still, first quarter's deal volume was about 6% higher than first quarter LTAs.

Industrial was the second most active segment (22% of total volume), transacting $18.5 billion in first quarter. Volume declined by more than half QoQ and is down about 76% from its fourth quarter 2021 peak. Despite the recent sharp declines, first quarter deal volume was over 43% higher than first quarter LTAs.

Retail deal activity was roughly the same QoQ at almost $17 billion and comprised 20% of total volume, the highest percentage since 2014. This dovetails with the heightened investor interest for the segment as seen in our institutional survey data. First quarter volume was down 55% from its fourth quarter 2021 peak. However, first quarter activity was over 26% above first quarter LTAs.

The office segment continues to fall out of favor with transaction volume less than $11 billion in first quarter. This too, mirrors our investor survey showing it by far the least favored segment. Volume the lowest since the GFC following a 68% quarterly decline. First quarter deal volume was more than 52% below first quarter LTAs. Office comprised less than 13% of total deal volume in first quarter, the lowest percentage on record, far below the average of 36% it garnered during its dominating status before the GFC.

Hotel volume declined by more than half QoQ to about $5.9 billion (7% of total volume). It was the slowest quarter since the end of 2020 and over 17% below first quarter LTAs.

Pricing

Higher interest rates and substantial declines in investor interest continued to take a toll on pricing for all property segments, except industrial, in the first quarter. The National All-Property RCA CPPI, a gauge of property prices, was down 5.1% in first quarter, the largest quarterly decline in prices since the GFC and down almost 10% from their peak in second quarter 2022. However, because of the sharp run-up in prices over the last couple of years, overall CRE market pricing is up almost 20% since the pandemic began. Though industrial was the only segment without large declines in prices first quarter, the most recent monthly data showed prices stepping down by 3.3% between March and April.

Industrial prices fared best among the property types in first quarter, remaining roughly the same QoQ. Following the huge run-up in prices in 2021 and 2022, industrial prices are still 51% above pre-pandemic levels and down just 0.1% from their 2022 peak.

Office prices continued to fall from their second quarter 2022 peak in the first quarter, down 6.6%. Office prices declined 3.1% QoQ, the largest decrease since the GFC. Still, first quarter prices were 12% above pre-pandemic levels.

Retail prices declined 3.7% QoQ, the largest quarterly decline since the GFC. Retail prices peaked in second quarter 2022 and have since fallen by 7.6%. However, retail prices were up over 13% in the first quarter from pre-pandemic levels.

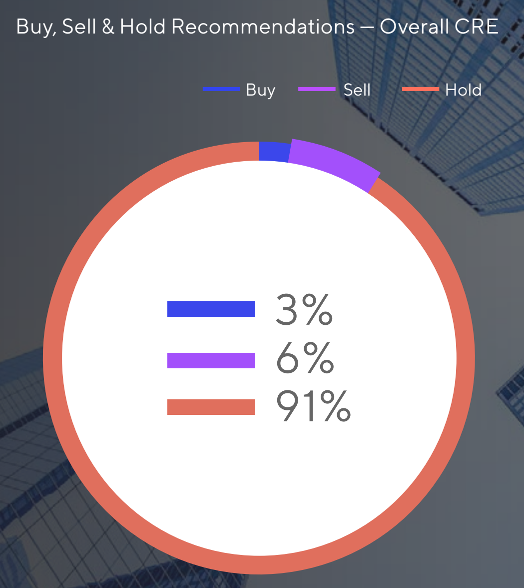
Apartment prices fell by 6.8% QoQ, a record quarterly decline. First quarter prices were down 13% from their second quarter 2022 peak. The drop in prices corresponded with particularly weak first-quarter fundamentals data. Despite the sharp decrease, apartment prices are more than 25% above their pre-pandemic levels due to the tremendous price growth in 2021 and 2022.

RERC Buy, Sell or Hold

Uncertainty in the financial markets and lack of pricing transparency helped propel investors' preferences to hold CRE. The recommendation to hold increased from 80% to 91% in first quarter. It was the highest hold endorsement since RERC began collecting these data in 1996 and about double the level seen during the GFC. Investors were least likely to recommend buying; preference for the strategy fell 6 percentage points QoQ to 3%. The recommendation to sell dropped QoQ from 11% to 6%. The recommendation to buy and sell were at record lows and about 20 percentage points and 10 percentage points below GFC levels, respectively.

Investors recommended holding for the overwhelming majority of property types: R&D, flex, regional mall, power center, neighborhood and community retail, apartment and hotel. Investors were bearish on CBD and suburban office, with a recommendation to sell and more bullish on warehouse, with a recommendation to buy. The alternative property types all garnered a hold rating: student housing, affordable housing, senior housing, medical office, self-storage and data centers.

> "Rising interest rates make holding an attractive alternative in this environment."
>
> -INSTITUTIONAL RESPONDENT



Percentage of total respondents recommending buy, sell or hold.
Sources: RERC, SitusAMC Insights, 1Q 2023.

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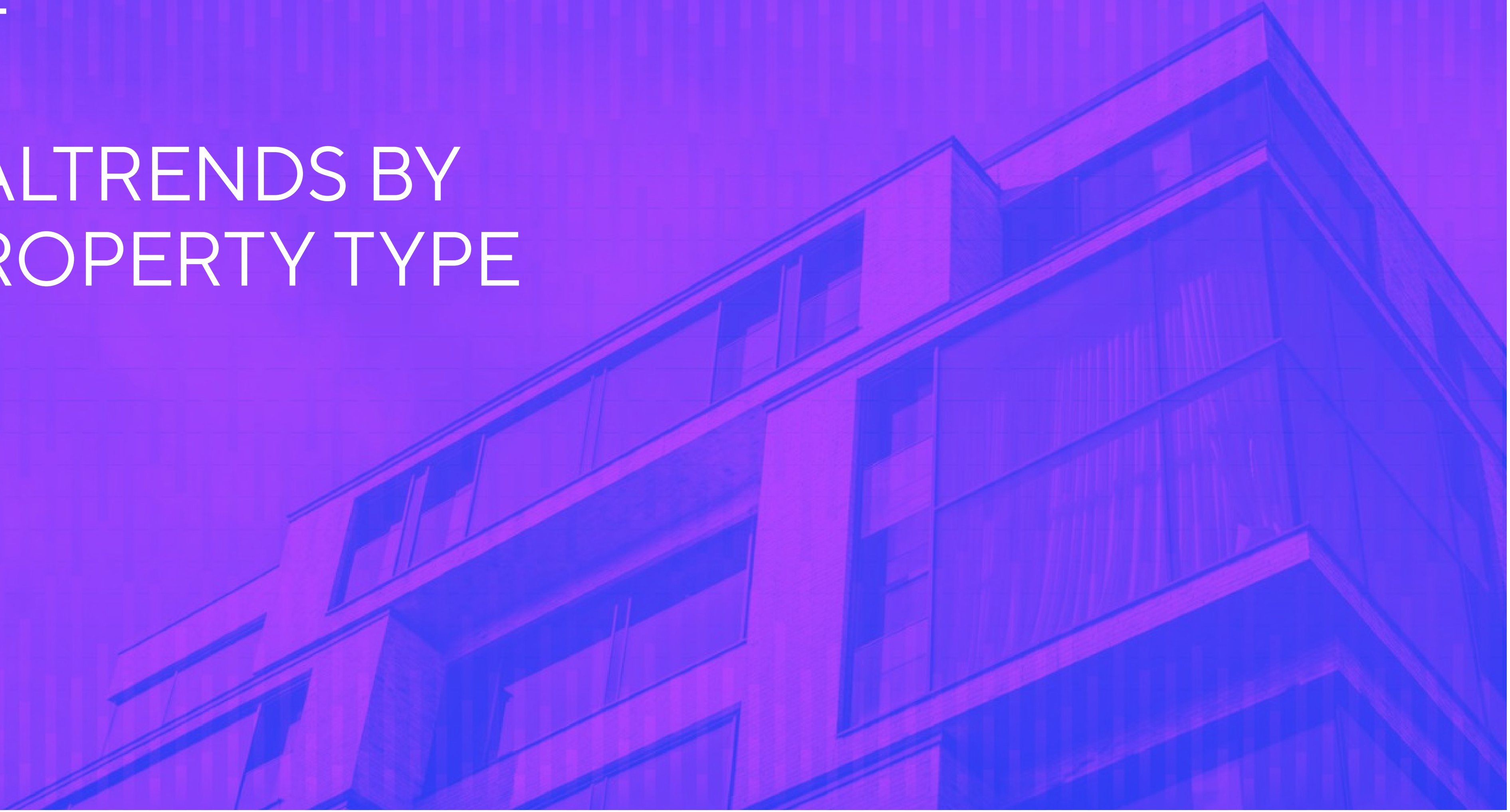
VALTRENDS BY PROPERTY TYPE



Cost of Capital Puts Continued Pressure on Values

RERC Perceived Return Relative to Risk

Investors’ perceptions of returns relative to risk for the overall CRE market and each of the property segments deteriorated substantially in the first quarter; neither overall CRE nor any of the property types were considered as having higher returns relative to risk. The overall CRE market was deemed the riskiest relative to returns since at least 2007, when RERC began collecting these data. According to investors, overall pricing levels have been high so near-term downward adjustments could be material.

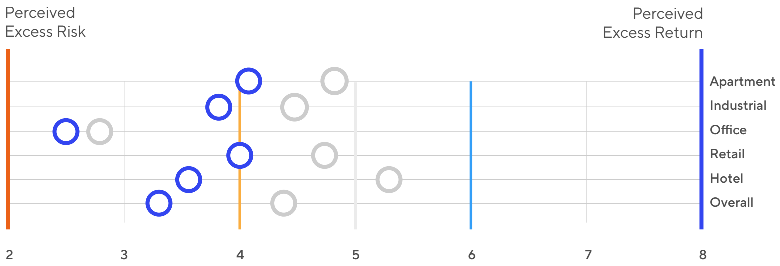
Investors perceive the office segment as the riskiest relative to return among the property types and the first quarter rating was the lowest in history. Investors believe that office space will continue to be retrenching as remote and hybrid work reduces office space usage in coming years.

Though declining substantially QoQ, apartment garnered the highest rating among the property types in first quarter. However, first quarter’s rating was the lowest since the onset of the pandemic as space market conditions showed a marked downshift from the robust conditions of recent years.

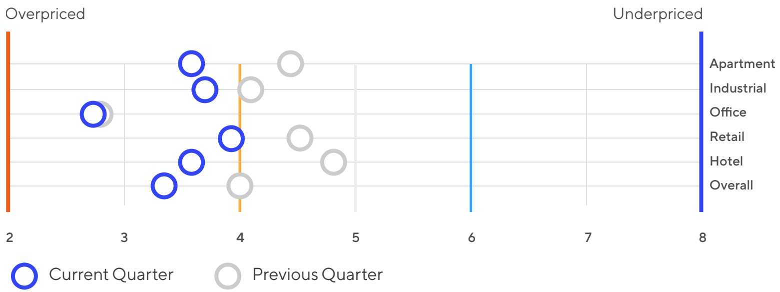
Industrial earned the second highest rating among the property segments, despite a sizeable drop QoQ to a record low for the segment. Since industrial has typically traded at lower cap rates, the segment is at higher risk for negative leverage scenarios due to higher interest rates.

Retail and hotel were rated the lowest since the end of 2020. Hotel’s quarterly drop was the largest among the property types. Ongoing macroeconomic concerns are fueling perceptions of risk for hotel and retail.

RERC Perceived Return Relative to Risk



RERC Relative Value Sentiment



Ratings are based on a scale of 1 to 10, with 10 indicating that return far exceeds risk or value far exceeds price. Sources: RERC, SitusAMC Insights, 1Q 2023.

RERC Relative Value Sentiment

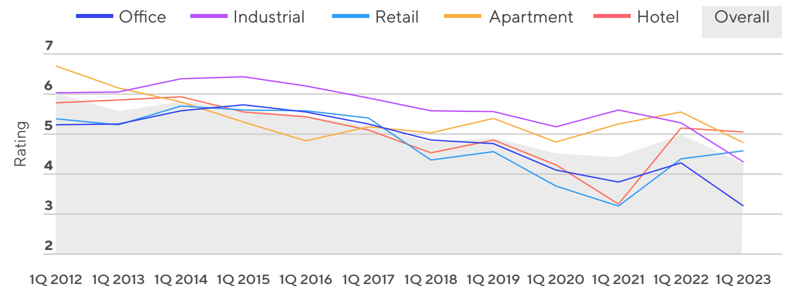
Relative value sentiment declined QoQ for overall CRE and all the property types. Investors note that until there is a better understanding of the new normal in financial markets, all sectors are facing repricing.

The overall CRE market, office, industrial and apartment segments were rated the most overpriced in history. However, investors expressed that a lack of pricing transparency made it difficult to determine fair pricing. Office, unsurprisingly, garnered the lowest rating among the property types. Urban office pricing, in particular, is becoming less affordable and feasible with market demand shrinking, according to investors.

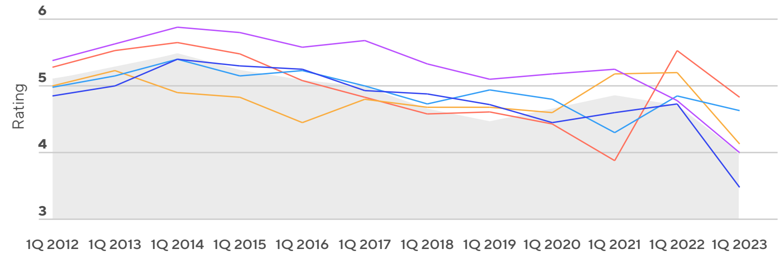
Retail had the highest rating among the property types in first quarter, despite a substantial QoQ drop. Investors indicate that the position of retail assets in the repricing cycle compared to other asset classes makes the segment more favorable. However, retail was deemed as the most overpriced since the onset of the pandemic and on par with the ratings seen during the GFC.

Hotel had the largest quarterly decline in ratings among the property segments; investors indicated that hotel was the most overpriced since the onset of the pandemic. Investors note that business travel has yet to return to pre-pandemic levels and there is a potential for oversupply.

RERC Perceived Return Relative to Risk — Average Annual Ratings



RERC Relative Value Sentiment — Average Annual Ratings



Ratings are based on a scale of 1 to 10, with 10 indicating that return far exceeds risk or value far exceeds price. Data represent four quarter moving averages. Sources: RERC, SitusAMC Insights, 1Q 2023.

SitusAMC Office Insights

Demand for office space remains weak with the occupancy rate decreasing 20 bps to a record low in first quarter, according to Reis. The ongoing decline in office occupancy is noteworthy given the continued growth in employment, notwithstanding high profile tech layoffs. Additionally, net absorption continued to be negative for the fourth consecutive quarter. Net absorption was on par with the levels seen during the first year of the pandemic, but is substantially lower than the levels during the GFC.

Surprisingly, effective rents increased 0.2% QoQ, marking the seventh consecutive quarter of modest gains. Rents are now above their pre-pandemic high. Completions fell by 18% QoQ to the lowest level in a decade.

Occupancy rates reached record lows for both Class A and Class BC after dropping 30 bps and 10 bps, respectively. The overall Class A occupancy rate was 220 bps higher than the Class BC rate in first quarter.

However, occupancy losses have been worse for Class A offices during the pandemic, with Class A down 300 bps compared to 120 bps for Class BC, despite the “flight to quality”.

Asking rents rose 0.4% for both Class A and Class BC office in first quarter; both asset classes had rent growth above their quarterly LTAs. Rents have surpassed their pre-pandemic highs by 2.1% and 1.1% for Class A and Class BC, respectively.

More than half of companies with U.S. offices plan to shrink their footprint over the next three years, with larger firms being the major drivers of this downsizing. The survey of executives also found that 32% plan to relocate their offices to better space and 40% would use the office market downturn to renegotiate their existing leases.

SitusAMC notes that office values are down considerably, with the market anticipating further declines. Stabilized occupancy has become the true differentiator of office values; about 25% of the value decline is specifically due to stabilized occupancy change. There have been large value declines in CBD gateway markets and to a lesser extent, suburban sun belt markets. There has also been a de-risking of cash flows, rate expansion and continued upward pressure on TI costs and leasing commissions.

Investors participating in our quarterly survey indicated that tenant renewals and re-leasing will continue to be an issue along with declining NOIs and increasing TIs. Market sentiment has weakened and perceived recession fears place upward pressure on investors required returns. With remote and hybrid work continuing for the foreseeable future, there is limited demand, especially for CBD offices.

SitusAMC Industrial Insights

Warehouse occupancy ticked down 10 bps QoQ, per Reis. Despite the slight decrease, the occupancy rate remains near the highest level on record. Net absorption remained positive in first quarter, as it has since the GFC. However, absorption has slowed by more than 85% since the record set in third quarter 2022. First quarter absorption was about half its LTA.

Warehouse effective rents grew 1.5% in first quarter, the slowest pace in nearly two years, but still 60 bps above the LTA. Rents were 39% above pre-pandemic levels. Rent growth should continue to be relatively strong amid constrained supply. First quarter completions fell by 57% QoQ, the lowest level in four years.

Favorable supply and demand dynamics in the niche industrial outdoor storage (IOS) segment should lead to strong rent growth and risk-adjusted returns, especially for infill locations, according to Green Street. Proximity to seaports, airports or highways boosts a property's attractiveness. New supply of IOS is near zero.

According to investors in our quarterly survey, industrial appears to have the most stable fundamentals. Rent growth remains strong with very little new supply. Additionally, there is not as big of a gap between buyers and sellers as it is easier to project cash flows. Market sentiment on self-storage is the best among the industrial subtypes, as it often weathers downturns better and has a broad base of options for buyers.

SitusAMC is seeing strong demand for assets that have a mark-to-market opportunity in the near term. Rental growth has been solid in many markets across the country, especially infill locations. This strong rent growth has helped offset some material cap rate expansion. Given inflationary pressures, especially the cost of materials and labor, future supply is expected to be tight. However, the segment will likely see continued write-downs because of the variance between contract and market rents.

NPI Total Return	-0.8%
Warehouse Occupancy Change	-10 bps QoQ
Warehouse Effective Rent Growth Change	+1.5%

"Best combination of near-term and long-term outlook and potential."

-INSTITUTIONAL RESPONDENT

Sources: NCREIF, Reis, SitusAMC Insights, 1Q 2023.

SitusAMC Retail Insights

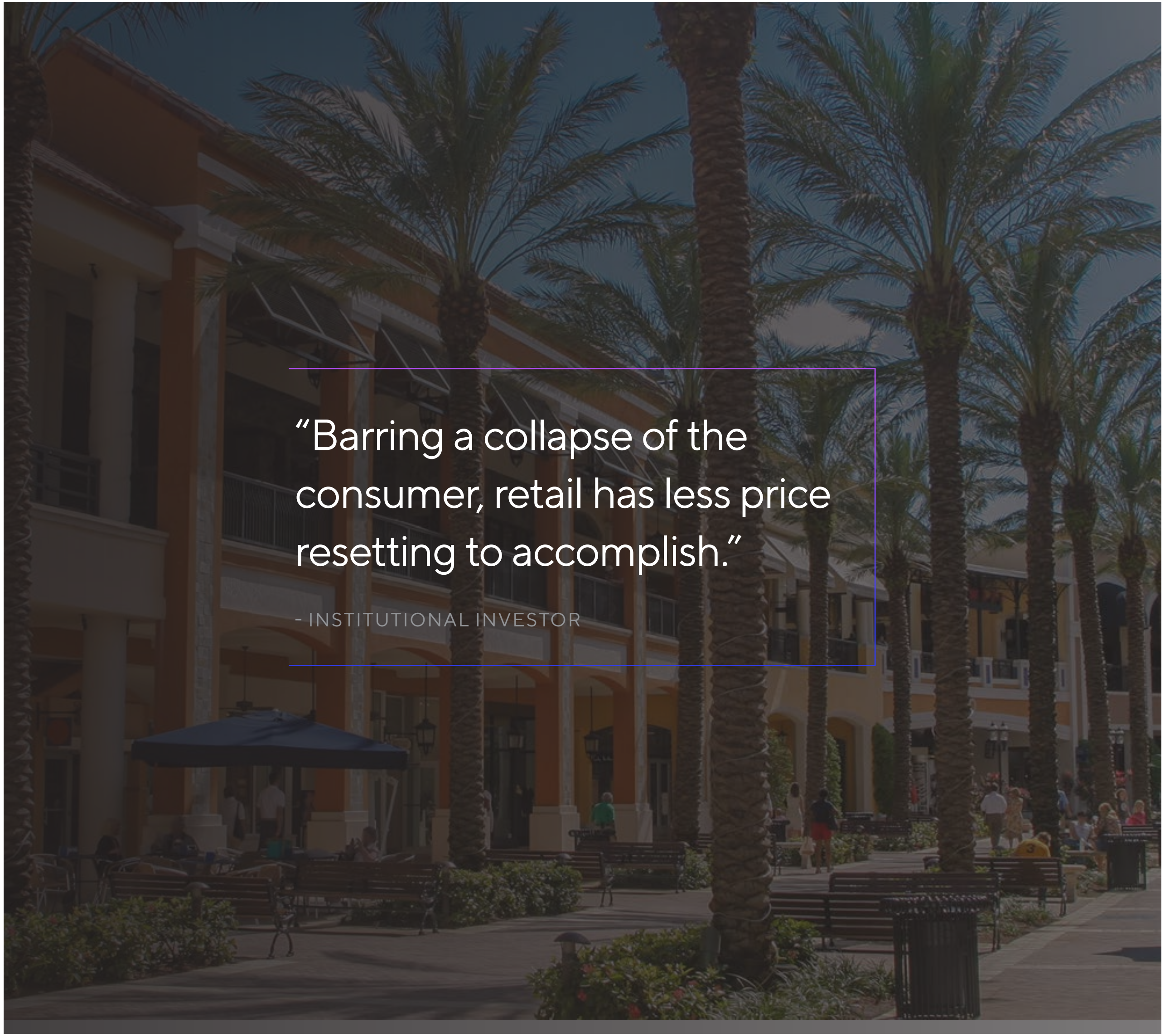
Retail's occupancy rate remained the same in first quarter, but it is still 10 bps lower than the pre-pandemic rate, according to Reis. Net absorption cooled substantially in the first quarter but remained positive. It was the lowest level of absorption in two years.

Effective rents have grown for eight consecutive quarters and are just 0.3% shy of their pre-pandemic levels. Completions fell 80% QoQ to a record low, which will likely support further rent growth.

Data from Open Table show that the number of dine-in restaurant bookings has returned to pre-pandemic levels. The data vary widely by market. The number of in-restaurant diners increased from 2019 in several sun belt metros like Miami (up 50%), Austin (up 23%), and Phoenix (up 13%). In-restaurant diners have not returned to pre-pandemic levels in the major markets, with San Francisco down 45% since 2019, New York down 30%, and Los Angeles down 10%.

Because retail took most of its valuation hits earlier in the pandemic, SitusAMC is seeing less of a boomerang effect than other segments; however, valuations have been flat to down. There has been decent market rent growth and positive lease trade-outs. SitusAMC anticipates some further rate movements, with implied cap rates moving slightly upward. The capital markets are at play in retail. Top-quality mall and grocery-anchored retail are securing financing in the mid-5% range. This is beginning to serve as a floor for where retail valuations need to peg.

Investors are seeing strong supply fundamentals and well-located, and needs-based retail is providing a good risk-adjusted return. Unless a recession severely disrupts consumer spending, the retail sector will likely be ahead of other sectors in terms of value declines. Investors are most bullish on neighborhood centers, particularly those that are grocery anchored. However, there are concerns that brick-and-mortar retail stores will continue to be downsized due to growth in internet sales.



SitusAMC Apartment Insights

Apartment demand continues to cool from its fervent pace in 2021 and 2022. Per Reis, apartment occupancy declined 20 bps QoQ, the largest decrease since the end of 2020. Net absorption was negative in first quarter for the first time since the GFC.

Lower supply may offset the decline in demand. Completions fell for the third consecutive quarter to the lowest level in 11 years. Effective rents declined 1.0%, the first decrease in two years. However, rents are still about 20% higher than those pre-pandemic.

Occupancy rates declined by 10 bps QoQ for Class A apartments reaching pre-pandemic levels. Class BC apartment occupancy increased 30 bps QoQ, but remain 30 bps lower than the pre-pandemic rate. Interestingly, Class A occupancy rates have generally declined over the past year, while Class BC rates have generally risen. Affordability may have driven tenants to lower cost properties.

Asking rents declined at a quicker pace QoQ for Class A than Class BC at -1.1% and -0.6%, respectively. First quarter was the first time in two years that either apartment tier had negative rent growth. Class A completions were down 42% QoQ to the lowest level since the GFC.

SitusAMC notes that many of the assets that have seen larger value declines this quarter may not have been written down as much in previous quarters; assets that have already taken large hits over the past few quarters are more likely to see flat values. Generally speaking, most values are down about 8% to 12% from their peak in second quarter 2022. SitusAMC is seeing rent deceleration though QoQ and YoY trade-outs are positive. Most markets are now at inflationary rent growth, except those in supply-constrained markets.

NPI Total Return	-2.1%
Occupancy Change	-20 bps QoQ
Effective Rent Growth Change	-1.0%

> "Still rent growth and better financing abilities."
>
> -INSTITUTIONAL RESPONDENT

Sources: NCREIF, Reis, SitusAMC Insights, 1Q 2023.

SitusAMC Hotel Insights

Seasonally adjusted hotel occupancy experienced a resurgence in first quarter, increasing almost 800 bps, according to Reis. The current occupancy rate is 140 bps higher than the LTA, but remains about 500 bps below the pre-pandemic high. Hotel occupancy data has been extremely volatile since the onset of the pandemic, but Reis forecasts the occupancy rate to increase through the rest of 2023, surpassing pre-pandemic levels by year-end.

Seasonally adjusted room rates and RevPAR also experienced large jumps in first quarter. Room rates increased 10.3% QoQ to reach new highs and RevPAR rose nearly 27% QoQ. Room rates and RevPAR are up 20% and 11% from pre-pandemic highs, respectively.

Upper-tier hotel occupancy surged 1150 bps QoQ; lower-tier hotel occupancy grew a respectable 520 bps. Both upper-tier and lower-tier hotel occupancy remains below pre-pandemic levels by 3.1% and 6.2%, respectively. First quarter upper-tier occupancy was 70 bps above its LTA.

Room rates increased 5.4% QoQ for upper-tier hotels and 13.7% for lower-tier hotels. Upper-tier hotel room rates are 17.4% higher and lower-tier hotels are 18.3% higher than pre-pandemic levels. RevPAR growth in first quarter was substantial for both hotel tiers. Upper-tier hotel RevPAR increased 26.4% QoQ and was over 12% higher than pre-pandemic levels. Lower-tier RevPAR improved 25.4% and was over 6% higher than pre-pandemic levels.

New York City tourism is forecast to grow to 63.3 million visitors in 2023, up from 56.7 million in 2022, and surpass 2019 levels by 2024, according to a New York City Tourism + Conventions March 2023 Outlook Report. Domestic travel is expected to reach 98.5% of the 2019 benchmark in 2023; international visitation is expected to reach 92%.

Investors from our quarterly survey indicate that hotel fundamentals are continuing to rebound from the COVID-19 years. Despite the ADR and occupancy growth coming out of COVID-19, pricing was not pushed upward as it was in other segments. Still, investors note that there are many hotel sales will be distressed, but can offer long-term gains.

ValTrends by SitusAMC

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