Commercial Real Estate Market Insights Report

September 2024

National Association of REALTORS®
Research Group

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Commercial Real Estate in August

An Overview

By the end of the summer, the economy displayed increasing signs that the cooling effects of high interest rates were no longer needed. Inflation is approaching the 2% average target, while the labor market continues to slow down, growing at a slower pace than the previous months. With markets already responding to the anticipated rate cut from the Federal Reserve, commercial real estate is also experiencing the effects. Demand for office space has improved, but additional supply has kept office vacancy rates at record highs. The retail sector remained tight due to limited new supply, while the industrial vacancy rate has steadily increased over the past couple of years, further decelerating rent growth for industrial spaces. Nevertheless, the multifamily sector continues to experience a robust rebound, with demand approaching the record-high levels seen in 2021.

Below is a summary of the performance of each major commercial real estate sector as of the end of the summer:

Although net absorption for the **office** sector remains in negative territory, demand for office space has improved. The surplus of unoccupied office space has dropped from nearly 59 million square feet a year ago to 35 million square feet in August 2024. Approximately half of the metro areas across the country saw an improvement in office net absorption compared to last year. Major markets such as the Texas Triangle – Austin, Houston, and Dallas – along with Philadelphia, Sacramento, San Diego, and Tampa successfully shifted net absorption into positive territory this year. However, the national office vacancy rate remained at record highs, with further increases in inventory recorded in August.

Even though mortgage rates eased in August, the **multifamily** sector thrived as housing affordability strained. Net absorption doubled compared to the previous year, exceeding 530,000 units. However, despite this robust demand for rental units, elevated completions and units under construction have kept the multifamily vacancy rate near 8%, with rent growth holding steady at around 1% over the past year. Looking ahead, rent growth could increase next year as the pace of new deliveries is expected to slow.

Retail space remains at historically tight levels, with less than 5% available retail space for lease for over two years. Demand continues to rise, further straining the market due to limited new supply. In the past 12 months, net deliveries totaled just over 33 million square feet – less than half the 10-year average. The sector's fundamentals are expected to remain tight with fewer retail spaces under construction and robust consumer spending.

The **industrial** sector continued to lose momentum in August. Net absorption was nearly 70 percentage points lower than a year ago, while rent growth decelerated significantly, dropping to 3.2% from 8.0%. With additional new supply, the vacancy rate rose 6.6% from 5.1%. However, further declines in inflation and interest rates in the coming months may boost demand for goods. This usually creates a ripple effect, increasing the need for industrial spaces to manage production, storage, and distribution.

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Economy

Job growth (August 2024 compared to March 2020): 5.4%
Inflation (August 2024): 2.5%
Gross Domestic Product (GDP) Q2 2024: 3.0%

Both of the primary factors influencing the Fed's upcoming policy decisions showed further signs of easing at the end of the summer. Inflation fell to 2.5%, approaching the 2% average target. Meanwhile, job creation remained below the average level of the past 12 months. Thus, the economy indicates that it may no longer need the cooling effects of high interest rates.

Job growth continued to ease in August

In August, the market added 142,000 new jobs, which was 30% below the average monthly gain of 202,000 over the past 12 months. Even though the unemployment rate fell to 4.2%, it remained higher than a year ago.

Specifically, the total number of job positions increased to 159.1 million in August. In the first eight months of the year, the economy had welcomed about 1.8 million new jobs. Since the onset of the pandemic in March 2020, the U.S. has successfully generated over 8.2 million jobs.

Number of Jobs

March 2020	**150.9 million**
August 2023	**156.4 million**
August 2024	**159.1 million**

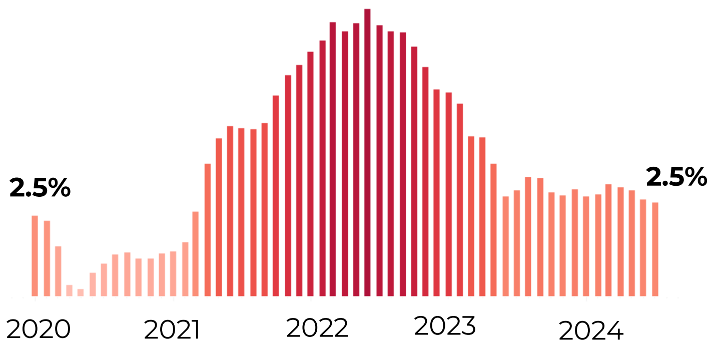
Source: NAR analysis of U.S Bureau of Labor Statistics data

Inflation fell to 2.5% in August

Inflation decreased further to 2.5% in August, the lowest seen since February 2021. Although inflation hasn't yet reached the Fed's 2% target, it has shown consistent signs of easing, which will allow the Fed to cut rates multiple times in the remainder of the year and the year ahead.

Meanwhile, data from the private sector suggests that rent growth, which usually represents the 40% of the CPI basket, will decelerate further in the coming months. This will help to bring down further the inflation rate.

Inflation



Source: NAR analysis of U.S Bureau of Labor Statistics data

Interest rate remained unchanged

The Federal Reserve kept unchanged its interest rates at 5.5% in August. However, with slower inflation and job creation, the Federal Reserve is expected to begin reducing interest rates in their coming meeting in September. While interest rates set the foundation for borrowing costs, these lower interest rates are expected to stimulate investment activity in commercial real estate.

The economy grew faster in Q2 2024

Surprisingly, the economy grew at a 3.0% pace in Q2 2024, faster than a 1.6% increase in the first quarter. The growth of the economy picked up in the second quarter as cooling inflation and a strong labor market allowed consumers to keep spending despite high interest rates. Compared to other countries, the U.S. economy continues to outperform.

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Commercial Real Estate Lending

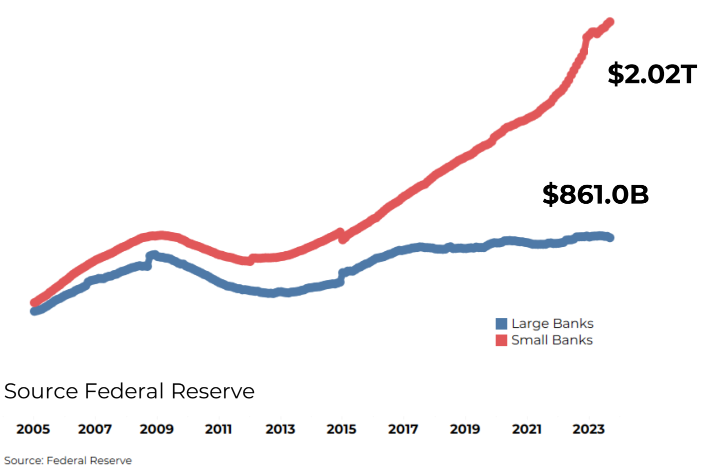
CRE loans (August 2024): $3.00 trillion
Delinquency rate of CRE loans (Q2 2024): 1.42%

CRE debt held steady at $3.0 trillion in August

The volume of CRE loans remained at $3.0 trillion in August. While the markets expect the Fed to begin cutting its interest rates, these anticipated lower interest rates have impacted CRE investment activity as well.

By bank size, within large domestically chartered banks, the volume of CRE loans fell further to $861.0 million from $886.2 a year earlier. Nevertheless, the CRE loans of small domestically chartered banks continued to grow in August, rising 4% compared to a year ago.

Commercial Real Estate Debt for Small and Large Banks (August 2024)

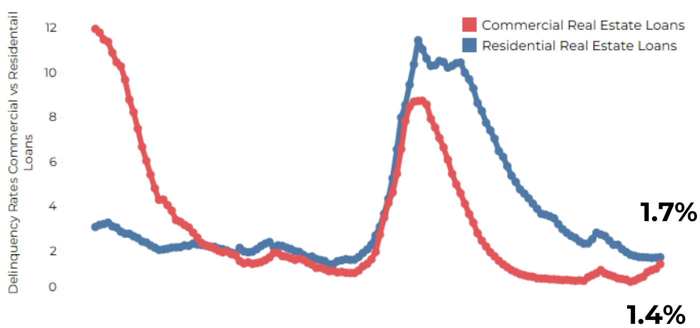


Source Federal Reserve

CRE delinquency rates significantly increased in Q2 2024

The Federal Reserve also provides data on delinquency rates for both commercial real estate (CRE) and residential loans. According to the latest data, delinquency rates for commercial loans significantly rose in Q2 2024. However, these loans maintained lower delinquency rates compared to residential loans. Specifically, the CRE delinquency rate was 0.85% in Q2 2023, and currently, it stands at 1.42%. Nonetheless, when delving into historical records, the delinquency rate for CRE loans consistently stays historically low, below 3.5%.

Delinquency rates Commercial vs Residential loans (Q2 2024)

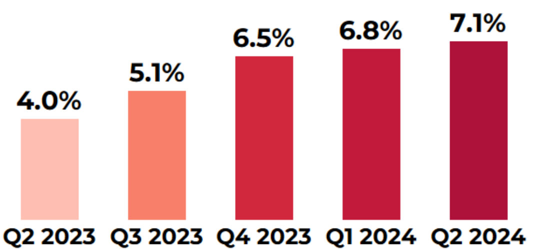


Source Federal Reserve

Office delinquency rates rose again in Q2 2024

According to the Mortgage Bankers Association, 7.1% of the balance of office property loan balances were 30 days or more days delinquent during the second quarter of the year, surpassing those of loans backed by retail and hotel properties. This is an increase from the 6.8% recorded at the end of the first quarter, and a substantial jump from the 4.0% reported a year ago (Q2 2023). While the number of vacant office spaces continues to increase, concerns grow regarding the health of these commercial loans. Given that delinquent loans backed by office properties represent nearly 30% of the Commercial Mortgage-Backed Securities (CMBS) outstanding, the condition of these office loans has a large impact on the outlook of this sector.

Delinquency rates for loans backed by office properties (Q2 2024)



Source Mortgage Bankers Association (MBA)

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Office

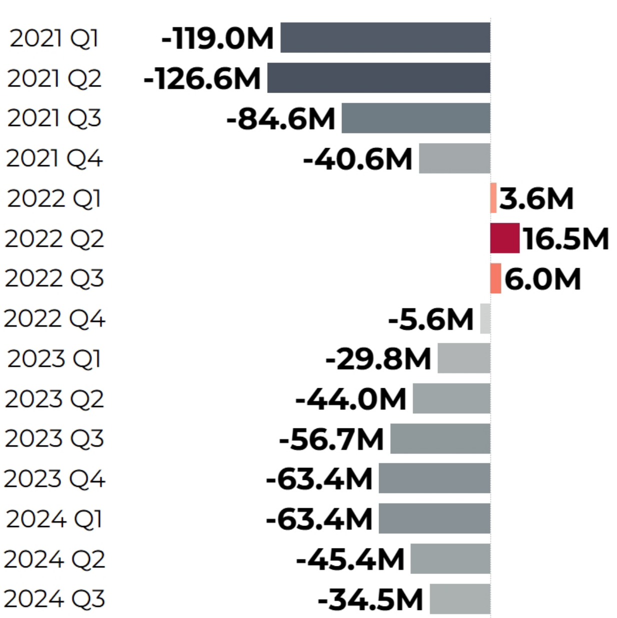
Net absorption in the last 12 months: -34.5 million sq.ft.
Rent growth in the last 12 months: 0.9%
Cap rate: 8.8%

Despite negative absorption affecting all office classes, Class A spaces are the hardest hit, with vacancy rates rising by 1% over the past year to 20.2%. In contrast, Class B office spaces have seen less negative absorption for the fourth consecutive quarter, with a vacancy rate of 12.4%, well below the national average of 13.8%. Class C spaces have the lowest vacancy rate at 5.1% as companies focus on cost-cutting amid economic challenges. Reflecting these trends, annual office deliveries have decreased by 52% compared to last year, contributing to a modest rent growth of 0.1%, now at 0.9%.

The most significant increases in vacant office spaces are in major tech hubs like San Francisco, Houston, Dallas-Fort Worth, Washington, DC, and Denver, CO, largely due to companies and workers relocating to regions with lower operational costs.

On the other hand, the top-performing markets in this sector, such as Wilmington, NC, Myrtle Beach, SC, and Savannah, GA, boast vacancy rates below 2%.

Net Absorption 12 Mo in sq. ft



Top 10 areas with the largest vacancy rates

	2024 Q3	2023 Q3
San Francisco, CA	22.52%	20.36%
Houston, TX	18.61%	18.54%
Dallas-Fort Worth, TX	18.15%	17.60%
Washington, DC	17.23%	16.08%
Denver, CO	17.02%	15.92%
Phoenix, AZ	16.84%	15.63%
Atlanta, GA	16.53%	15.79%
Austin, TX	16.50%	15.89%
Chicago, IL	16.25%	16.12%
Los Angeles, CA	16.11%	15.00%

Top 10 areas with the lowest vacancy rates

	2024 Q3	2023 Q3
Wilmington, NC	1.31%	1.91%
Myrtle Beach, SC	1.82%	2.21%
Savannah, GA	1.86%	1.73%
Davenport, IA	1.92%	2.18%
Hickory, NC	1.98%	2.17%
Huntington, WV	2.04%	1.86%
Asheville, NC	2.21%	2.50%
Olympia, WA	2.32%	2.38%
Salisbury, MD	2.48%	2.69%
Pensacola, FL	2.60%	1.92%

Source: NAR analysis of CoStar data

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Multifamily

Absorption of units in the last 12 months: 534,668 units
Rent growth in the last 12 months: 1.2%
Cap rate: 6.1%

As the third quarter of 2024 progresses, the multifamily housing market adjusts to an increased trend of renting due to high interest rates making homeownership less attainable. A 115% rise in 12-month absorption now totals nearly 535,000 units. Deliveries have increased by 21% over the past year, while units under construction have decreased by 34%.

Class A multifamily properties have seen their vacancy rate rise by 0.7% over the past year, reaching 10.7%, the highest among multifamily categories. These properties have experienced an annual rent growth of 0.5%. Meanwhile, Class B properties, traditionally marked by lower absorption rates, are witnessing increased demand for the fifth consecutive quarter. With a lower vacancy rate of 8.7%, Class B properties have achieved a 1.1% rent growth over the past year. This trend highlights the financial pressures many are facing, pushing more people toward affordable housing as inflation remains above the 2% target.

While rent growth is sluggish nationwide, some Sun Belt metro areas are seeing a decline due to an oversupply of properties, with Fort Myers, FL, Austin, TX, and Naples, FL, witnessing rent decreases of over 4%. On the other hand, Lancaster, PA, Evansville, IN, and Rockford, IL are bucking this trend, with rent increases exceeding 5%, significantly above the national average of 1.2%.

In major urban areas like Dallas-Fort Worth, TX, and New York, NY, more than 24,000 multifamily units were absorbed over the year ending in August. This surge in demand underscores the strong performance of the rental market in these high-cost regions.

Top 10 areas with the strongest 12-month absorption

	2024 Q3	2023 Q3
Dallas-Fort Worth, TX	25,648	8,910
New York, NY	24,102	18,887
Houston, TX	18,452	8,598
Phoenix, AZ	18,319	8,888
Austin, TX	18,171	7,068
Atlanta, GA	18,002	3,429
Washington, DC	16,231	9,116
Orlando, FL	14,232	4,718
Seattle, WA	11,932	5,569
Nashville, TN	11,764	5,697

Top 10 areas with steepest 12 Mo rent declines

	2024 Q3	2023 Q3
Fort Myers, FL	-5.67%	0.28%
Austin, TX	-4.46%	-3.65%
Naples, FL	-4.03%	-0.24%
Raleigh, NC	-2.70%	-1.72%
Sarasota, FL	-2.57%	-1.59%
Jacksonville, FL	-2.25%	-1.22%
Huntsville, AL	-2.20%	-1.10%
Killeen, TX	-2.16%	2.84%
Phoenix, AZ	-1.83%	-1.99%
Atlanta, GA	-1.77%	-2.43%

Source: NAR analysis of CoStar data

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Retail

Net absorption in the last 12 months: 33.3 million sq. ft.
Rent growth in the last 12 months: 2.3%
Cap rate: 6.9%

Tightening conditions in the retail sector continue to suppress leasing activity and net absorption. Specifically, net absorption is nearly 40% lower than a year ago. Despite growing demand for retail space, limited new supply has kept the availability rate at a record low.

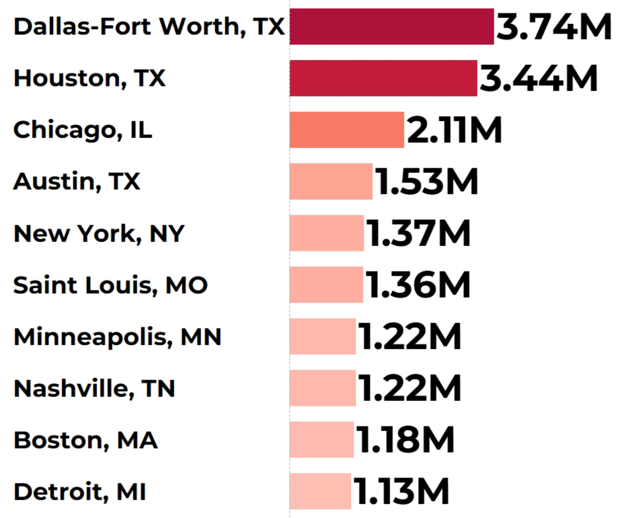
By category, general retail spaces and neighborhood centers have been significant contributors, accounting for approximately 83% of the positive net absorption as of August 2024. In contrast, malls saw a vacancy of 1.9 million square feet, raising their vacancy rate to a record high of 8.7%

The overall retail vacancy rate has remained at a record low of 4.1% for the 7th consecutive quarter, with deliveries only slightly surpassing absorption.

General Retail maintains the lowest vacancy rate at 2.5%. Neighborhood Centers and Power Centers recorded the highest rent increases, at 3.4% and 3.2%, respectively.

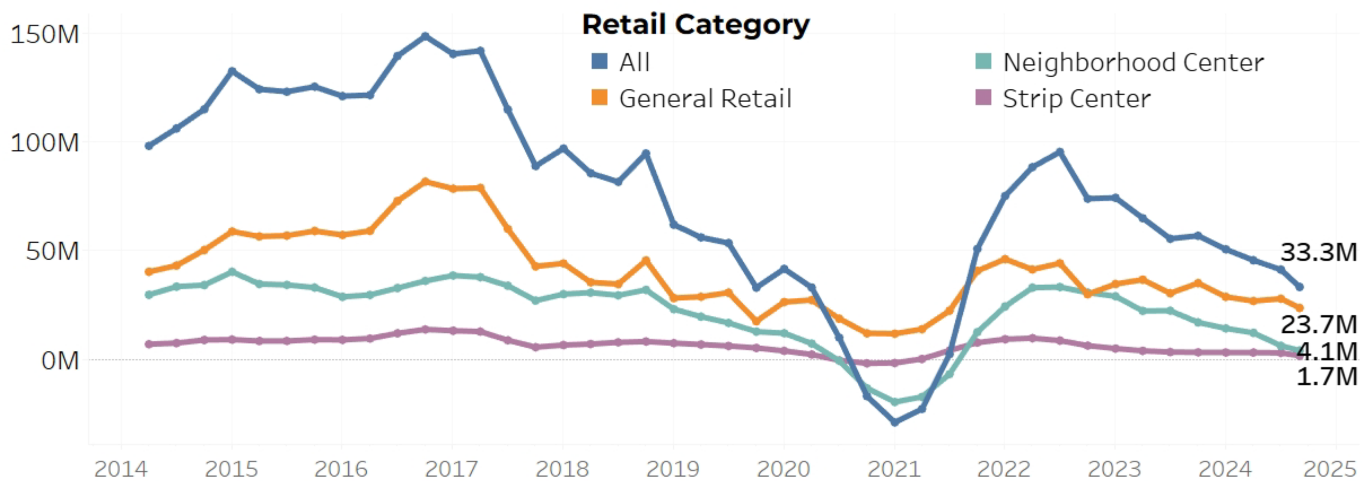
In August, Salt Lake City, UT, and Raleigh, NC, experienced the highest year-over-year rent growth at 8.9% and 7.2%, respectively. On the flipside, Pittsburgh, PA, and San Francisco, CA, had rent declines more than 2%.

Top 10 areas with the strongest net absorption in the last 12 months



Moreover, Texas is excelling in retail real estate, with cities like Dallas-Fort Worth and Houston recording the highest year-over-year retail space absorption rates in the nation, surpassing 3 million sq. ft. as of August 2024.

Net Absorption 12 Mo by type (Q1 2014 – Q3 2024)



Source: NAR analysis of CoStar data

Industrial

Net absorption in the last 12 months: 105.2 million sq. ft.
Rent growth in the last 12 months: 3.2%
Cap rate: 7.3%

The industrial real estate market, which saw significant growth in 2022, is facing challenges due to an excess of available properties and lower demand. From August 2023 to August 2024, net absorption plummeted by 68%, reaching a 10-year low of 105.2 million square feet. Furthermore, property deliveries are outpacing absorption by 4 to 1, causing the vacancy rate to rise by 1.5% to 6.6%. Although rent growth has decelerated to 3.2%, it continues to outperform other sectors.

Logistics spaces continue to be the only industrial segment with positive absorption, accumulating nearly 111.4 million square feet over the past year ending in August. In contrast, Flex and Specialized spaces vacated 5.8 million and 0.4 million square feet, respectively. Logistics spaces also led in rent growth with a 3.5% increase, while Specialized spaces had a 2.7% rise, and Flex spaces grew by 2.8%.

Dallas-Fort Worth, TX, recorded the highest industrial space absorption in the last 12 months, followed by Houston, TX, and Phoenix, AZ, each absorbing over 13 million square feet by August 2024.

As the third quarter continues, Reno, NV, Greensboro, NC, and Los Angeles, CA, have fallen from the top 10 to the bottom 10 in industrial absorption over the past year. The strong demand from 2022 and early 2023 has diminished, resulting in slower rent growth. Despite this, Los Angeles and Reno maintain lower vacancy rates of 5.6% and 4.1%, below the national average of 6.6%.

Richmond, VA, Orlando, FL, and Columbus, OH, saw industrial rents rise by over 7% last year, driven by strong warehouse demand, reflecting the region's economic growth and competitiveness.

Top 10 areas with the strongest 12-month absorption

	2024 Q3	2023 Q3
Dallas-Fort Worth, TX	21.83M	37.15M
Houston, TX	19.40M	24.01M
Phoenix, AZ	13.79M	19.38M
Savannah, GA	10.94M	11.33M
Nashville, TN	7.94M	5.81M
Austin, TX	7.59M	3.70M
Chicago, IL	7.24M	25.95M
Philadelphia, PA	6.59M	7.14M
Minneapolis, MN	6.00M	3.86M

Top 10 areas with the weakest 12-month absorption

	2024 Q3	2023 Q3
Los Angeles, CA	-12.12M	-14.72M
Reno, NV	-4.68M	4.27M
Winston-Salem, NC	-2.86M	-0.14M
Harrisburg, PA	-2.79M	2.72M
Portland, OR	-2.42M	1.91M
San Diego, CA	-2.42M	-1.85M
Greensboro, NC	-2.28M	3.18M
New York, NY	-2.16M	-1.58M
Seattle, WA	-1.69M	0.50M
San Francisco, CA	-1.52M	-1.61M

Source: NAR analysis of CoStar data

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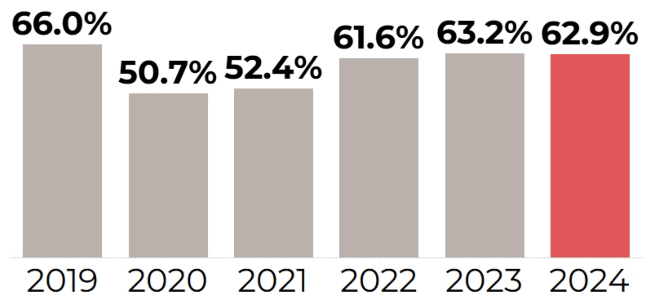
Hotel

Occupancy rate in the last 12 months: 62.9%
Average daily rate in the last 12 months: $158/room
Revenue per available room in the last 12 months: $99/room

As we continue into Q3 2024, the hospitality sector is maintaining stability. Hotel occupancy rates have leveled off at around 63%, remaining roughly 3% below pre-pandemic figures, which suggests that a complete recovery may be elusive due to the prevalence of remote work. Nevertheless, average daily rates and revenue per available room have now exceeded pre-pandemic benchmarks.

12-month Occupancy Rate in August



Specifically, in August 2024, the average daily rate (ADR) per room rose to $158/room, up 20% from August of 2019. The revenue per available room (RevPAR) also increased to $99/room, up 15% compared to the same period in 2019.

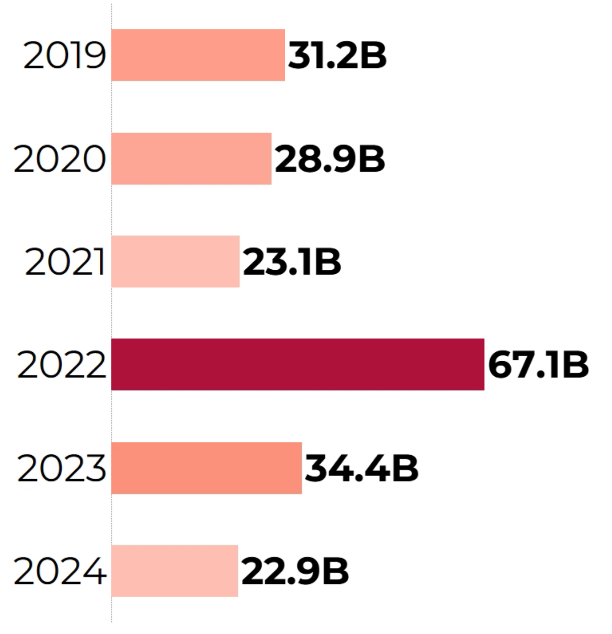
12-month ADR and RevPAR in August

	Average daily rate	Revenue per available room
2019	$131	$87
2020	$117	$59
2021	$113	$59
2022	$144	$88
2023	$154	$98
2024	$158	$99

ADR is the total revenue/number of rooms.
RevPAR is ADR x occupancy rate.

Sales acquisitions have declined since the last year. In August 2024, the 12-month sales volume dropped to $21.3 billion from $35.7 billion in the previous year.

12-month Sales Volume as of August



Source: NAR analysis of CoStar data

At the local level, the hospitality sector on Hawaii's Kauai Island is flourishing, with the Average Daily Rate (ADR) increasing by 59%, Revenue per Available Room (RevPAR) rising by 57% from pre-pandemic levels, and an impressive occupancy rate of 70%. Maui Island leads the nation with outstanding figures, with an ADR of $554 and a RevPAR of $367. Meanwhile, New York City holds the highest hotel occupancy rate at 83%.

Conversely, regions in California, especially San Francisco/San Mateo and San Jose/Santa Cruz, are still facing significant challenges, with RevPAR remaining 25% and 28% below pre-pandemic levels, respectively, indicating ongoing recovery difficulties.

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COMMERCIAL REAL ESTATE REPORT
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