

# Commercial Real Estate Trends & Outlook

January 2021

National Association of REALTORS® Research Group



NATIONAL  
ASSOCIATION OF  
REALTORS®

# COMMERCIAL REAL ESTATE TRENDS & OUTLOOK

## January 2021 Report

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This report is based on information collected from NAR's 2020 Q4 Commercial Real Estate Quarterly Market Survey of its members who are primarily engaged in commercial transactions. The 2020 Q4 Commercial Real Estate Quarterly Market Survey of REALTORS® reveals that the commercial real estate market continues to recover, but sales, leasing, and construction activity remain below year-ago levels. The recovery also remains uneven, with stronger investor interest for land, multifamily, and industrial properties than for hotels, retail, and office properties. REALTORS® are typically engaged in the small commercial market (properties valued at less than \$2.5 million).

On a year-over-year basis, sales declined by 1% in the fourth quarter of 2020 (5% in the second quarter). Leasing volume fell by 1% (4% in the second quarter). Construction activity among REALTORS® was down by 3% (6% in the second quarter). The risk spread (cap rates less 10-year T-bond) remains elevated at 6% compared to 4% prior to the pandemic.

For the first quarter of 2021, REALTORS® expect an increase in sales of land (5% y/y), industrial (3% y/y) and multifamily (2% y/y) properties. Regarding the land market, the properties with the strongest expected increase in sales are residential land (7% y/y), industrial land (5% y/y), and ranch lands (5% y/y).

REALTORS® expect vacancy rates to hover at about 5% among multifamily and industrial properties, at 10% for retail properties, at 12% for office properties, and 50% for hotel/hospitality properties.

REALTORS® expect commercial prices to increase in 2021 Q1 for multifamily properties (+1% y/y), industrial (2% y/y), and land assets (3% y/y), and to decrease in the office market (-3% y/y), retail (-6% y/y), and hotel/hospitality (-6% y/y).

Enjoy reading the latest issue!

# 1 | COMMERCIAL SALES

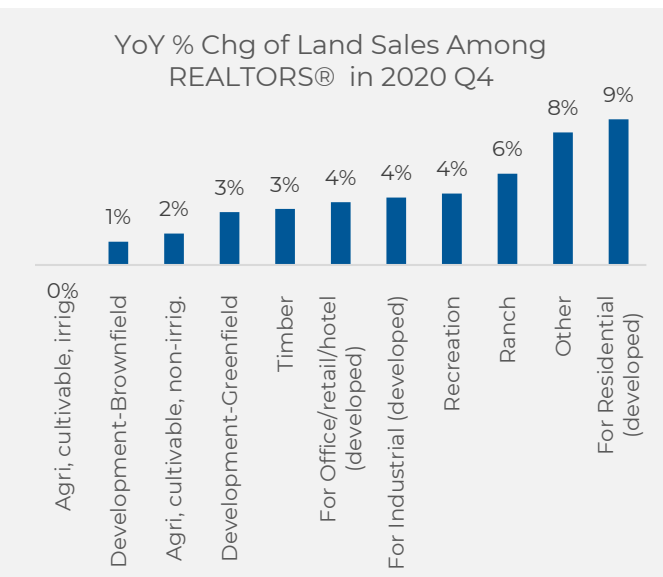
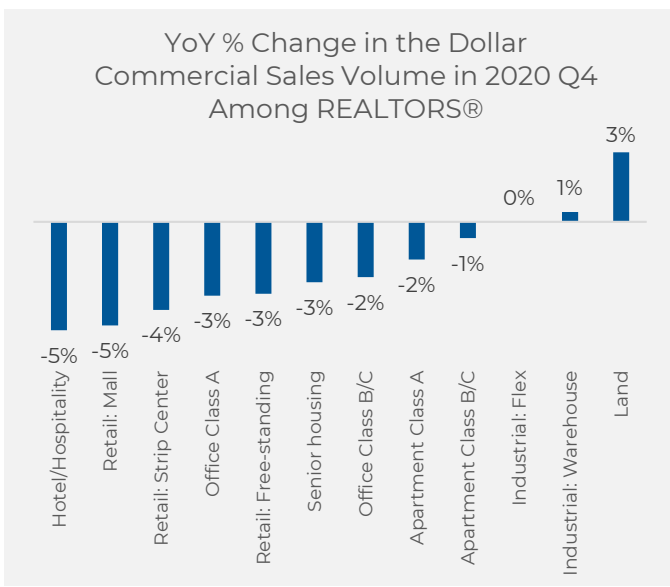
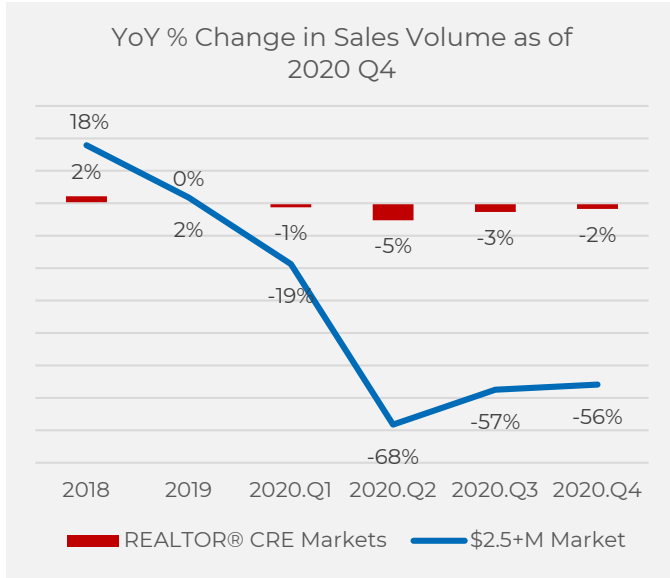
## REALTORS®' Commercial Sales Declined in 2020 Q4, Except for Land and Industrial Acquisitions

In NAR's Commercial Real Estate Quarterly Market Survey, REALTORS® reported that their sales transactions volume in the fourth quarter contracted on average by 2% year-over-year. However, this rate of decline is smaller than the 5% decline in the second quarter when the economy practically shut down. NAR commercial members' transactions are typically below \$2.5 million (small commercial market).

The dollar sales volume for properties or portfolios of at least \$2.5 million (middle to large commercial market) contracted 56% year-over-year in the fourth quarter, according to Real Capital Analytics.

By property type, REALTORS® reported the largest declines in sales/acquisitions in the hotel/hospitality market (-5%), retail malls (-5%), and retail strip centers (-4%).

The largest increase in sales acquisitions was for land, with sales volume up by 3% year-over-year.



Among land transactions, the largest gains were in sales of recreational land (e.g. for camping), ranches, and residential land. This could be related to increased interest for land outside urban centers in the wake of the COVID-19 pandemic.

# 1 | COMMERCIAL SALES

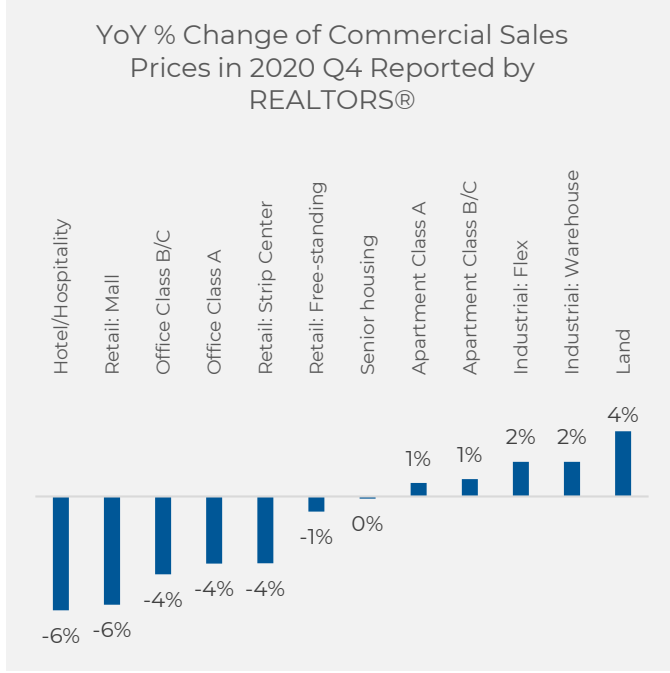
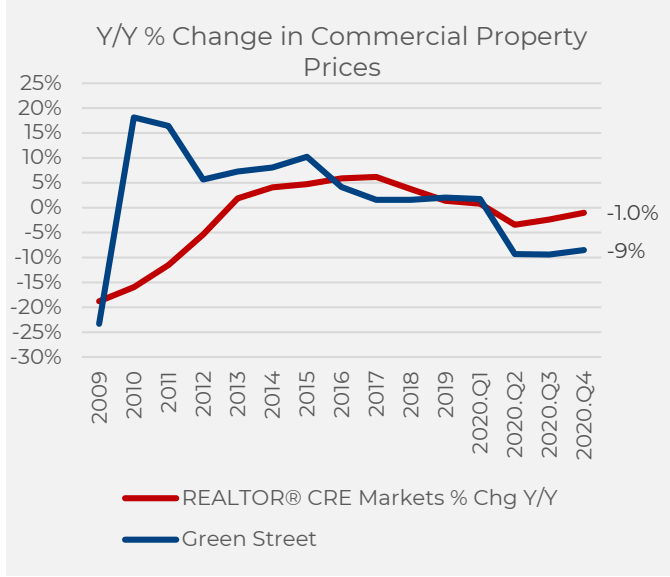
## Commercial Prices Decreased Except for Multifamily, Industrial, and Land Assets

REALTORS® reported that commercial sales prices in their markets were down on average by 1% in the fourth quarter on a year-over-year basis. By type of property, REALTORS® reported the largest decline in property value for hotels/hospitality (-6%) and retail malls (-6%), followed by office buildings (-4%).

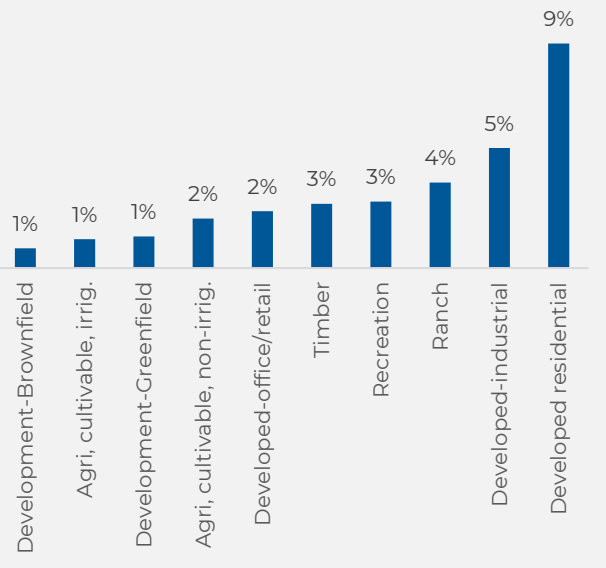
On the other hand, REALTORS® reported higher property values for apartments (1%), industrial assets (2%), and land (4%).

REALTORS® reported higher prices for all types of land, with the largest price increase in ranch land, industrial, and residential land, an indication of the strong demand for land outside urban areas since the COVID-19 pandemic.

According to Green Street's appraisal-based commercial property price index of REIT-owned unleveraged commercial properties, commercial prices were down 9% year-over-year in the fourth quarter.



YoY % Change in Land Prices in 2020 Q4



# 1 | COMMERCIAL SALES

## Risk Premium (Cap Rate Less 10-year T-Bond) Trending Down But Still Elevated vs. Pre-Pandemic Level

The risk premium has slightly trended down to 6% in the fourth quarter, but the risk premium is still elevated compared to the 4.5% risk premium prior to the pandemic. The risk premium (going-in cap rate less 10-year T-bond) started rising in 2018 (recall talk of recession, US-China trade war) through the second quarter of 2020, at 6.2%.

REALTORS® reported Apartment class A acquisitions had the lowest going-in cap rate (or lowest risk) among commercial assets, at 5.4%.

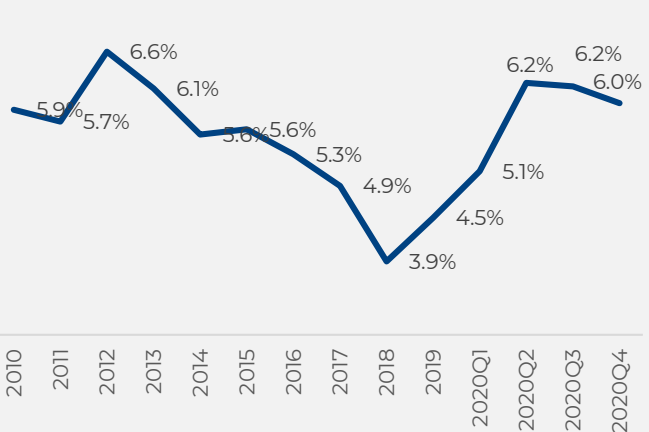
Hotel/hospitality, retail, and office Class B had going-in cap rates of over 7%.

## Cap Rates in 2020 Q4

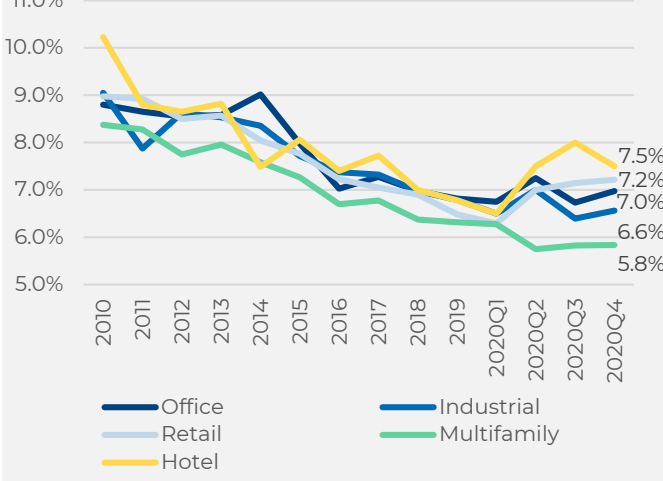
Office: Class A	6.5
Office: Class B/C	7.5
Industrial: Warehouse	6.5
Industrial: Flex	6.7
Retail: Strip center	7.0
Retail: Mall	7.4
Retail: Free-standing	6.9
Apartment: Class A	5.4
Apartment: Class B/C	6.2
Hotel/Hospitality	7.5
Senior housing	6.4
Land	6.5

Source: 2020 Q4 NAR CRE Market Survey

Risk Premium Starting to Trend Down  
(Going-in Cap Rate Reported by REALTORS® Less 10-Year T-Bond)



REALTORS® Commercial Capitalization Rates



# 2 | COMMERCIAL LEASING

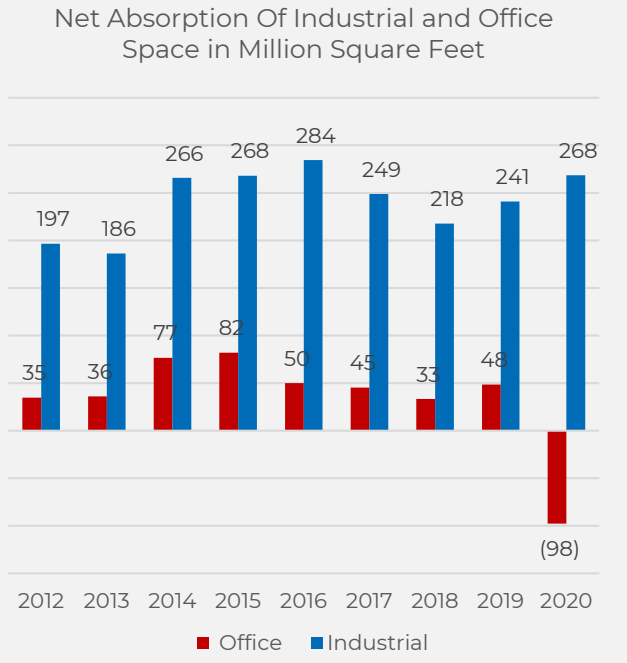
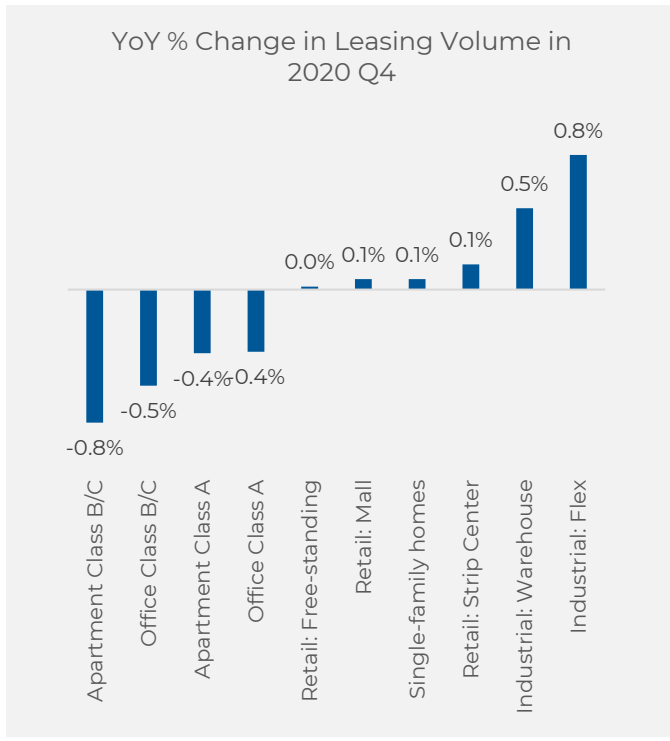
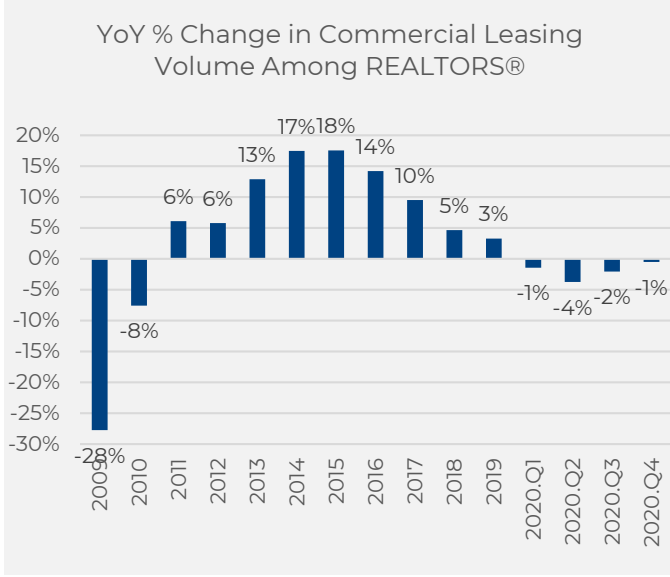
## REALTORS® Leasing Activity Decreased Except in Industrial Buildings

REALTORS® who responded to the survey reported that their leasing volume (renewals and new leases) declined on average by 1% in the fourth quarter from one year ago. However, this is a smaller decline compared to the 4% decline in the second quarter.

With one in five workers still working from home, according to Bureau of Labor Statistics data, REALTORS® reported a decline in leasing transactions for apartments (-1%) and office buildings (-1%).

On the other hand, leasing transactions for industrial properties increased (1%). The demand for industrial space is associated with the acceleration on e-commerce sales, spurring the demand for warehousing and distribution space.

In 2020, on a net basis, 98 million of square feet of office space was vacated, a third of which was in the Northeast. However, the loss in office space was offset by the net gain of 268 million of industrial space, about 45% of which is in the South region.



-97,648,067 Office	268,448,152 Industrial
-30,761,426 Northeast	46,410,590 Northeast
-7,880,078 Midwest	51,002,048 Midwest
-22,087,673 South	119,253,007 South
-36,918,890 West	51,782,507 West

Source: Cushman and Wakefield

# 2 | COMMERCIAL LEASING

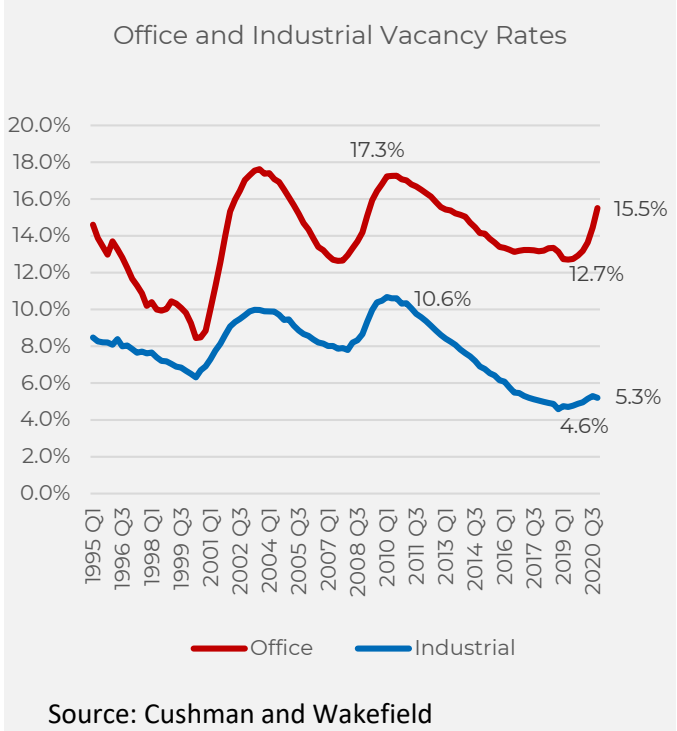
## Vacancy Rates Continue to Trend Upwards, But Apartment Rental Vacancy Remains Tight

With the loss in office occupancy, office vacancy rates have increased to 15.5%, about 3 percentage points higher than in the second quarter. However, the vacancy rate is still below the 17% rate during the Great Recession. Industrial vacancy rates have also increased slightly to 5.3%.

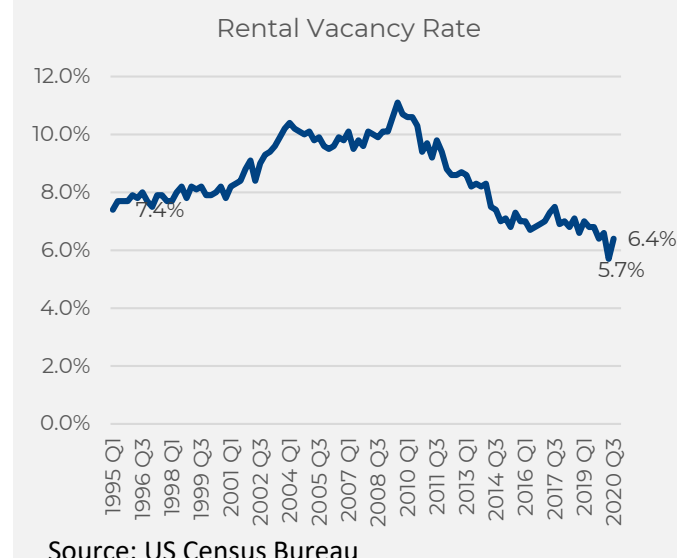
The rental vacancy rate for apartments slightly increased to 6.4% in the third quarter, but this is still a low rate relative to the historical vacancy rate of about 8% and is just about half the level during the Great Recession. Low rental vacancy rates will tend to support rent growth and increase the rate of return on apartment investments.

### Decline in the Average Office Space?

One major question about the impact of the pandemic is whether the office footprint will decrease (due to working from home) or increase (more space per person for social distancing). Sixty-nine percent of REALTORS® reported seeing “more” short-terms leases of less than two years in the latest 2020 Q4 survey.

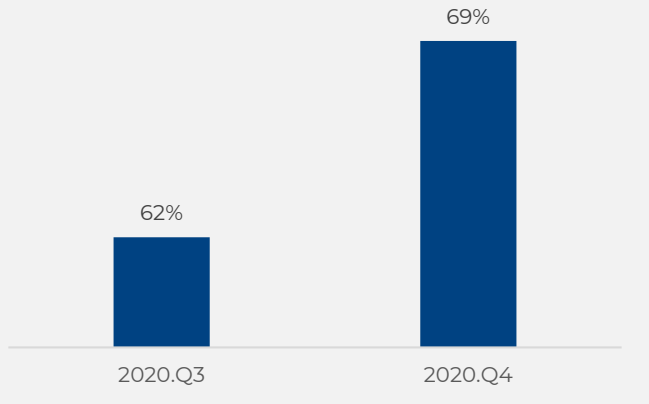


Source: Cushman and Wakefield



Source: US Census Bureau

Percent of REALTOR® respondents who reported "More" companies leasing smaller square footage due to working from home relative to January 2020





# 2 | COMMERCIAL LEASING

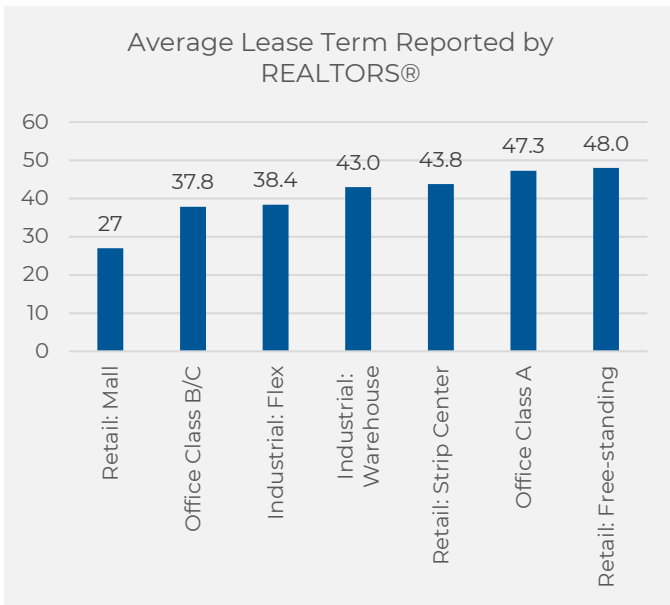
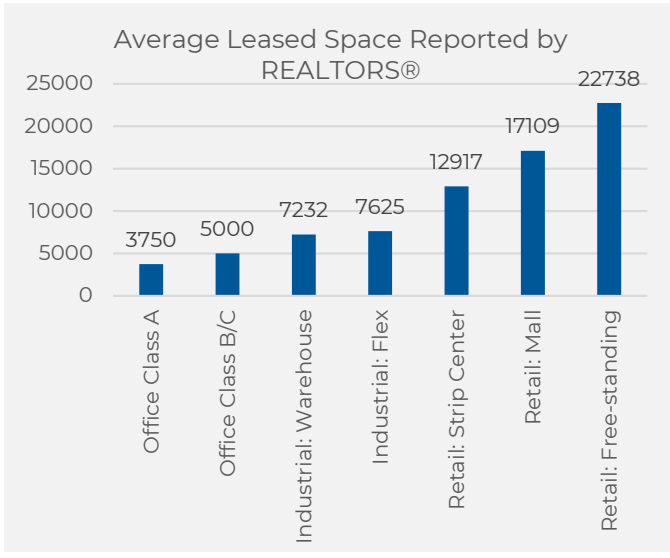
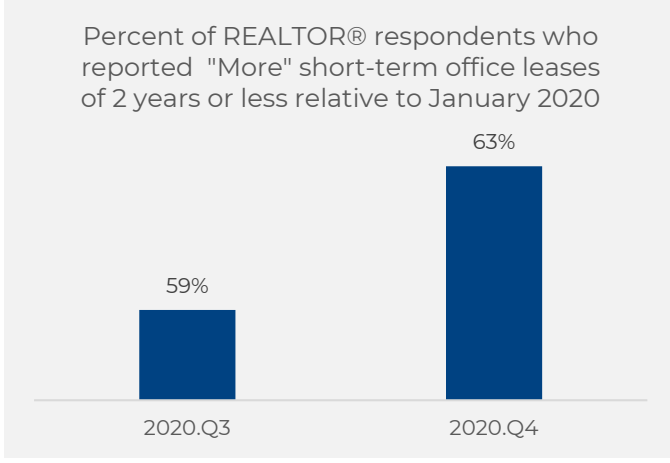
## Average Lease Terms of Occupiers

Another major question about the impact of the pandemic is on the length of the lease. Economic uncertainty will tend to lower the lease term, while greater certainty on the economic outlook will tend to increase the average lease term because long term leases (greater than two years) are cheaper. Lease terms among all occupiers will also tend to increase if the mix of occupiers shift towards those who anticipate being in the business for a number of years.

With the cases of COVID-19 infections still rising and nearly 25% of the workforce still working from home, 63% of REALTORS® reported that they are observing an increase in short-term office leases of two years or less compared to the pre-pandemic period.

REALTORS® reported that, on average, the office lease term among occupiers was 38 months (Class B/C) to 47 months (Class A). The average lease term of occupiers of office class A buildings seemed to have increased, to 47 months. As discussed previously, there's been a huge loss in office space occupancy, so the remaining tenants are likely those with long-term leases of about 47 months on average.

With the adverse effect of pandemic on the retail sector, the shortest lease terms were leases for malls, with the average lease term at just slightly over 2 years.





# 3 | CONSTRUCTION

## REALTORS® Construction Activity Declined Except for Apartment and Industrial Properties

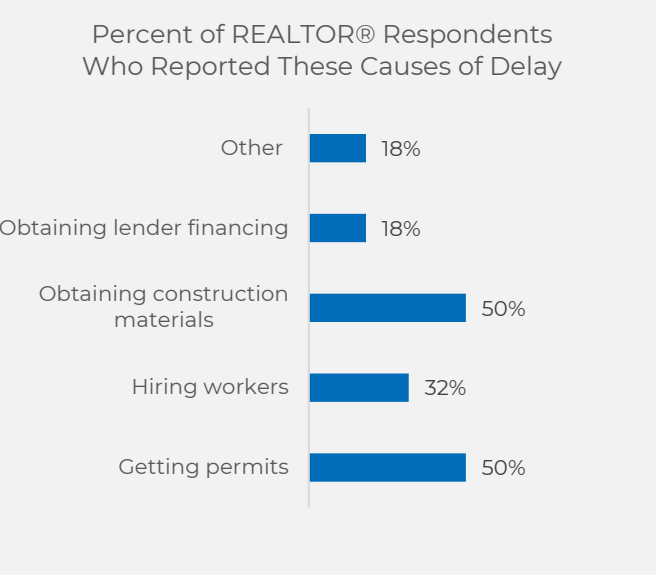
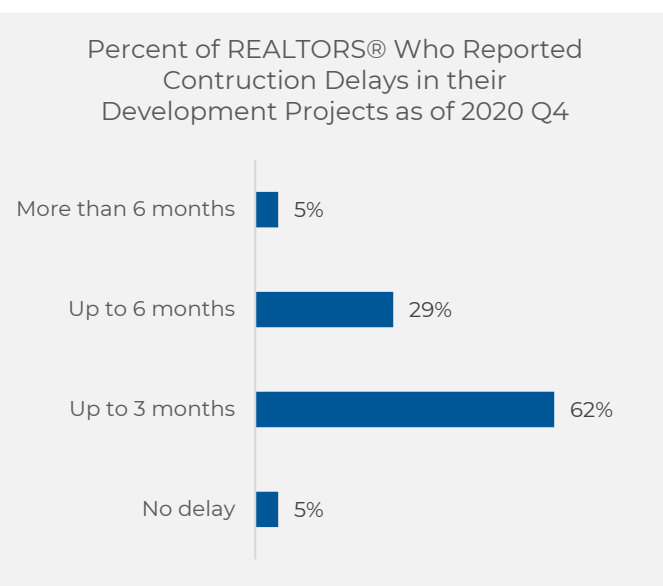
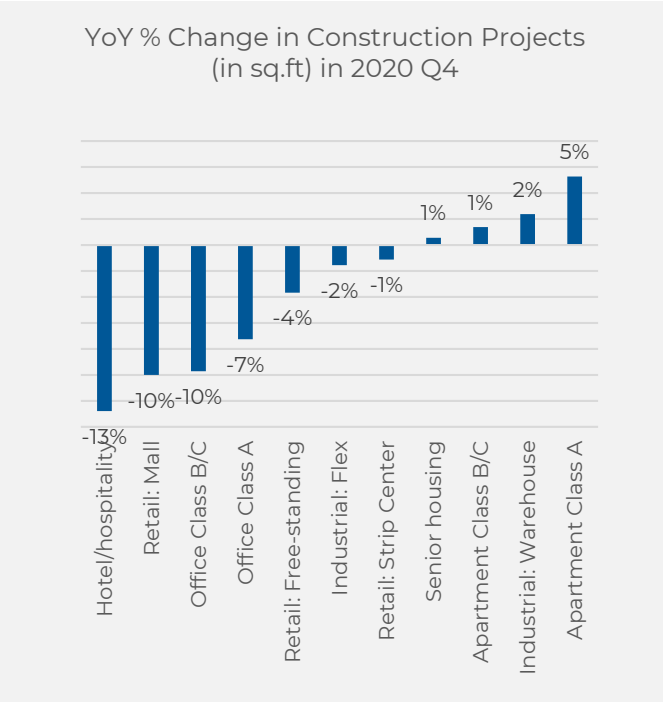
REALTORS® reported on average a 3% year-over-year decline in construction activity (in square feet) in their markets in 2020 Q4. In the second quarter, construction was down by 6%.

The largest decline in construction activity was in hotel/hospitality (-13%), followed by retail (-10%) and office (-10%).

REALTORS® reported that on average, construction activity increased in the fourth quarter compared to one year ago in Class A apartments (5%), followed by industrial warehouses (2%), and Class B/C apartments (1%) as well as senior housing (1%).

Nearly all respondents reported construction delays, with 62% reporting a delay of up to 6 months.

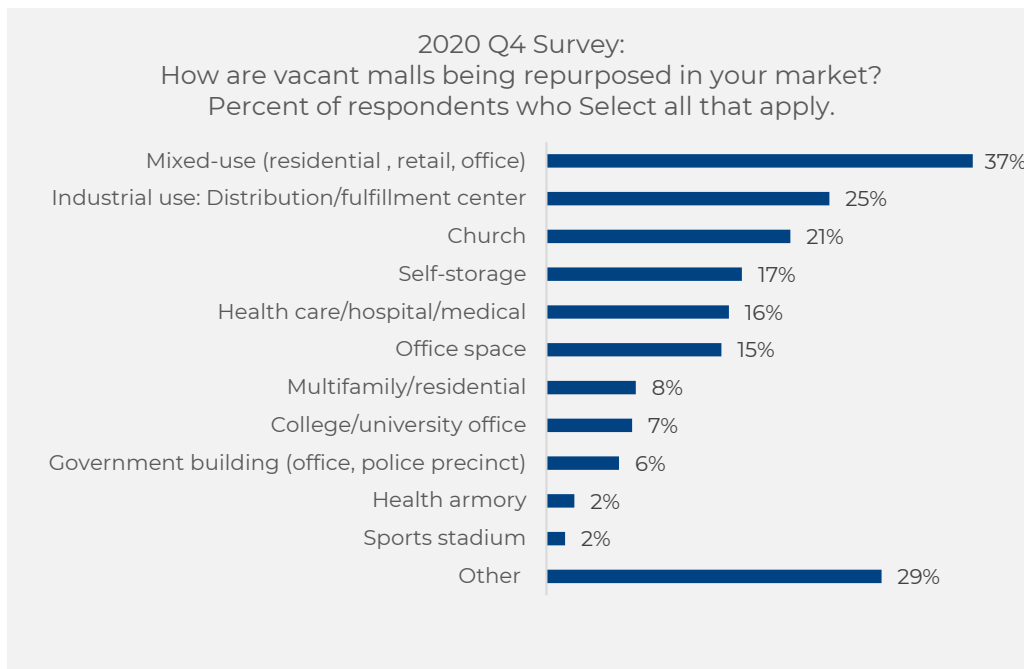
Obtaining construction materials and obtaining permits were cited by half of REALTOR® respondents as the causes of delay.



# 4 | IMPACT OF COVID-19 ON REAL ESTATE

What changes are you seeing in the following areas relative to January 2020 (pre-coronavirus condition)?	Percent of respondents who answered "More"	
	2020.Q3	2020.Q4
Tenants with missed, late, or partial office, retail, or industrial space rent payments	54%	59%
Tenants with missed, late, or partial multifamily residential rent payments	53%	63%
Repurposing of vacant malls	52%	53%
Working from home/alternating/staggered office work schedules	83%	85%
Headquarters with satellite offices	48%	51%
Sales or leasing transactions in suburban area vs. central business district	43%	46%
Demand for flexible/co-working office space from individuals (gig workers, independent contractors, etc.)	51%	48%
Demand for flexible/co-working office space from enterprise clients/large firms	43%	39%
Companies leasing or moving into offices with smaller square footage due to working from home	62%	69%
Short-term office leases or use service agreements (2 years or less )	59%	63%
Tenants with rent concessions	65%	65%
Co-tenancy clauses for retail properties	37%	38%
Investment in workspace redesigns to increase sanitation, hygiene, and social distancing (plexiglass, air filtration, etc.)	76%	81%
Companies that pay for expenses related to working -from-home (broadband internet, office supplies, etc.)	60%	68%
Offices being charged higher common area maintenance expenses related to safely and sanitation measures	42%	44%
Use of work data analytics to track mobility and use of office spaces	45%	46%
Companies that offer transportation services/shuttles for their workers	21%	20%
Companies obtaining business interruption insurance	50%	51%

Source: NAR Commercial Real Estate Quarterly Market Survey

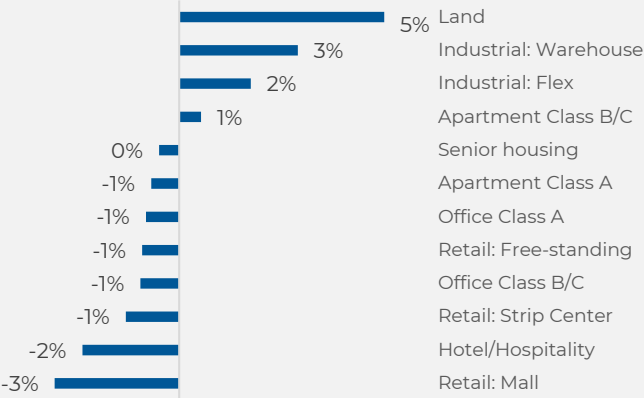


[Download the Case Studies on Repurposing Vacant Malls](#)

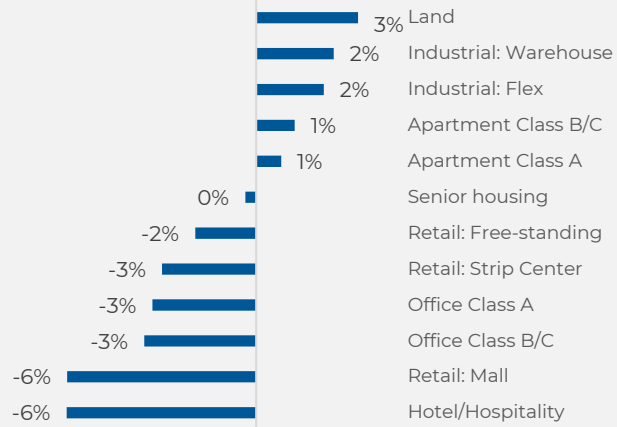
# 4 | COMMERCIAL OUTLOOK

## REALTORS® Expect Land, Industrial, and Apartment Properties Market to Perform Better than Office, Retail, and Hotel

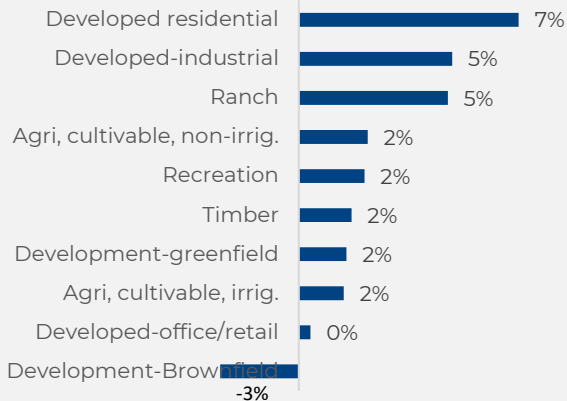
REALTORS® Outlook of the Dollar Commercial Sales Volume in 2021 Q1 Compared to 2020 Q1



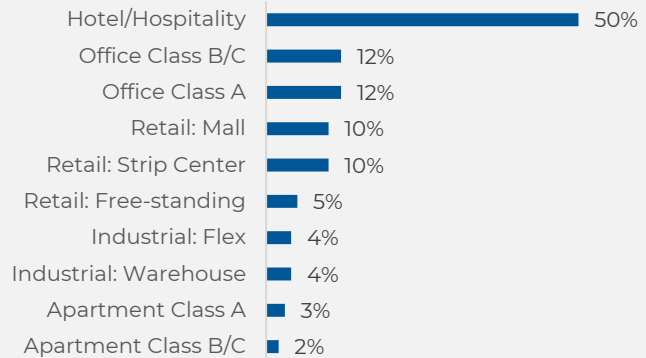
REALTORS® Outlook of Commercial Prices in 2021 Q1 Compared to 2020 Q1



REALTORS® Outlook of Land Sales in 2021 Q1 Compared to 2020 Q1



REALTORS® Outlook of Vacancy Rates in 2021 Q1



# COMMERCIAL REAL ESTATE TRENDS & OUTLOOK

## January 2021

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This report is based on information collected from NAR's 2020 Q4 Commercial Real Estate Quarterly Market Survey. The survey asks about the commercial transactions of REALTORS® and members of NAR' commercial affiliate organizations (CCIM, SIOR, RLI, IREM, and the Counselors of Real Estate) during the fourth quarter of 2020. The survey was sent to approximately 76,000 commercial REALTORS® and members of affiliate organizations during January 4-17, 2020, of which 969 provided answers to at least one question.

The NAR Research Group acknowledges the I/S/Cs for reaching out to their members to respond to the survey and developing the survey: Aubrie Kobernus, CEO, Realtors® Land Institute; Denise LeDuc-Froemming, CEO/EVP, IREM; Alexis Fermanis, Communications Director, SIOR; and Greg Fine, CEO/EVP, CCIM Institute. The Research Group also acknowledges Charlie Dawson, Vice-President, Engagement, and Rodney Gansho, Director of Engagement, in reaching out to CCIM, CRE, IREM, SIOR, and RLI designees to respond to the survey.

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Download report at: <https://www.nar.realtor/commercial-real-estate-market-survey>



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