

# Quarterly Market TRENDS

Commercial Real Estate Market Trends and Transaction Analysis • **THIRD QUARTER** • [www.ccim.com](http://www.ccim.com)

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**NATIONAL  
ASSOCIATION of  
REALTORS®**

*Produced by CCIM Institute,  
an affiliate of the  
National Association of Realtors®*

# Quarterly Market TRENDS



## *November 2014* FOREWORD

Dear CCIM Institute members,

Welcome to the third-quarter 2014 edition of CCIM Institute's Quarterly Market Trends. The report provides timely insight into major commercial real estate indicators for core income-producing properties. It is produced by the National Association of Realtors® in conjunction with and for members of the CCIM Institute, the premier provider of commercial real estate education.

The third-quarter 2014 report features commentary from Lawrence Yun, Ph.D., NAR chief economist, and George Ratiu, director of NAR's quantitative and commercial research. It also includes market analysis and data collected from CCIM members that illustrate regional economic and transactional trends across the U.S. I'd like to thank the CCIM members who participated in the survey and shared insights on their local markets.

I hope that the information provided in CCIM's Quarterly Market Trends report provides both economic and commercial real estate market information that will assist you in your business strategies in 2014 and beyond.

Help CCIM make this report even more valuable by participating in the next QMT survey. Watch your email for details.

Sincerely,

Karl Landreneau, CCIM  
2014 CCIM Institute President

klandreneau@latterblum.com

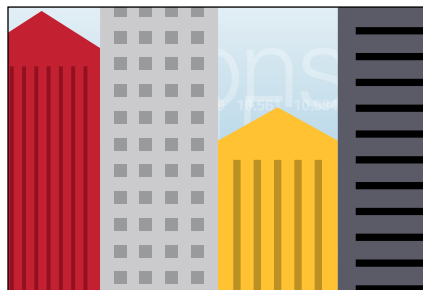


# Quarterly Market TRENDS



## *Table of* CONTENTS

CCIM Transaction Survey Highlights . . . . .	4
Commercial Property Sector Analysis . . . . .	5
Commercial Real Estate Market Update . . . . .	9
Commercial Real Estate Forecast . . . . .	13
U.S. Economic Overview . . . . .	14
U.S. Metropolitan Economic Outlook . . . . .	19
Sponsors . . . . .	22
Contributors . . . . .	23

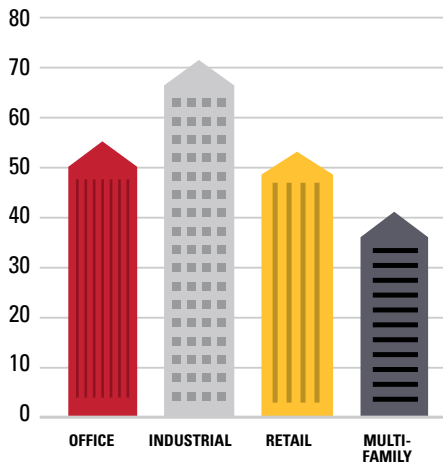


## CCIM Transaction Survey HIGHLIGHTS

With rising deals and investor confidence, CCIM members provided insights into their markets in an August/September 2014 survey.

### GREATEST DEAL FLOW INCREASE: INDUSTRIAL

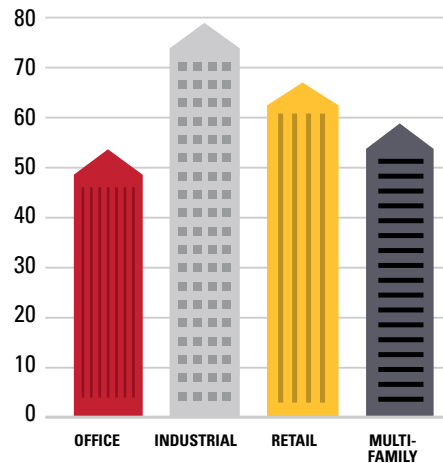
3Q14 YOY % BY SECTOR



Industrial deal flow saw the biggest increase with **71%** of respondents reporting year-over-year **GAINS**.

### BUYER INQUIRIES FOR INDUSTRIAL PROPERTIES INCREASE

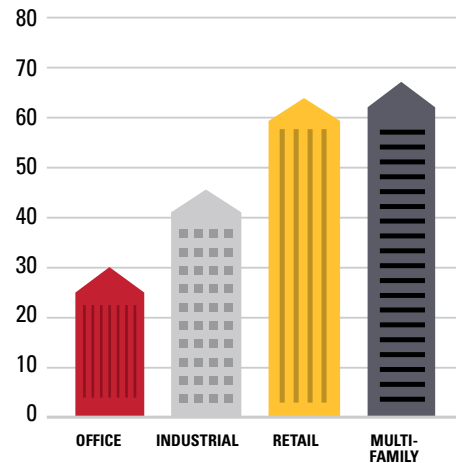
3Q14 YOY % BY SECTOR



Approximately **79%** of respondents said they received **MORE SERIOUS INQUIRIES** from buyers in 3Q14.

### MULTIFAMILY PROPERTY PRICES SEE BIGGEST GAINS

3Q14 YOY % BY SECTOR



Multifamily property **PRICES ROSE** in 3Q14 for more than **68%** of respondents.

In 3Q14, **52% OF CCIM MEMBERS INDICATED MORE DEALS** compared to same period last year.

More than **60% OF RESPONDENTS HAD MORE INQUIRIES RELATED TO BUYING**, while 11% reported more inquiries related to selling.

Property prices rose somewhat from the same period last year with **47% REPORTING HIGHER PRICES**, and 33% of respondents reporting prices similar year over year.

The **CAP RATE GAP BETWEEN BUYERS AND SELLERS NARROWED** in 3Q14, according to 44% of CCIM members who responded, and remained flat for another 44% percent of respondents.

Rents increased, with **51%** of CCIMs who responded indicating **HIGHER RENTS YEAR OVER YEAR**; 35% of respondents indicated similar rents year-over-year.

Approximately **48%** of responding practitioners indicated that **CAP RATES REMAINED IN LINE** with last year; 44% dealt with lower rates in 3Q14.

About **53%** of respondents expect **RENTS AND PRICES TO MOVE TOGETHER** in the next two to three years, 18% said rent growth will outpace price growth, and 29% indicated the opposite, with prices expected to outperform rents.

**49%** of members considered that **TREASURY YIELDS WILL REMAIN**

**ABOUT THE SAME**; 22% of respondents indicated that Treasury yields will rise, but will only minimally impact cap rates due to the current spreads; 12% of CCIMs considered that Treasury yields will rise and force cap rates upward.

About **33%** of respondents said the saw **MEANINGFUL IMPROVEMENT IN CREDIT AVAILABILITY** in 3Q14; 56% reported marginal improvement.

According to **54%** of CCIMs who responded, **CREDIT CONDITIONS WILL IMPROVE** over the next two to three years, while 40% consider the current tightness to be the new normal.

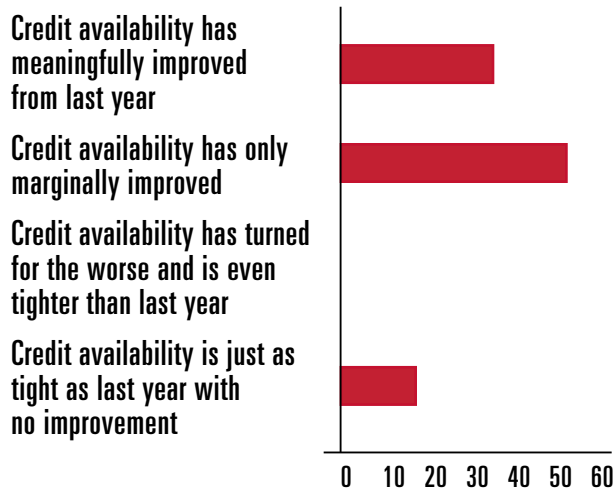
## Commercial Property SECTOR ANALYSIS

### NATIONAL OFFICE MARKETS

Office trends improved in 3Q14:

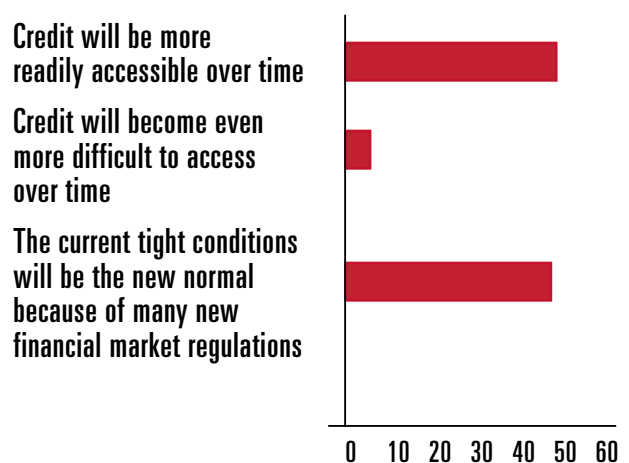
- Deal flow was higher for 55 percent of CCIM member respondents (compared with 50 percent in 2Q14).
- Property prices were higher for 30 percent, while 50 percent found them to be flat.
- Cap rates were even for 58 percent of respondents, and lower for 28 percent.
- Rental income was flat for 40 percent of respondents; higher for 48 percent.
- 53 percent of respondents had more serious buying inquiries (compared with 54 percent in 2Q14).

#### FINANCE TRENDS (YoY) / Office Properties %



Source: CCIM Institute, National Association of Realtors®

#### FINANCE OUTLOOK / Office Properties %



Source: CCIM Institute, National Association of Realtors®

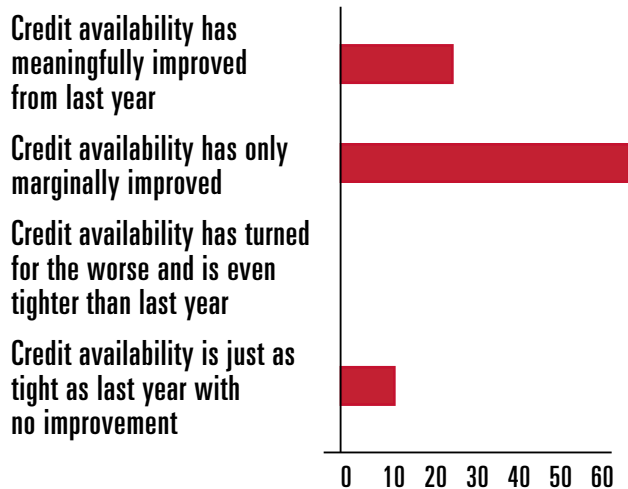
## Commercial Property SECTOR ANALYSIS

### NATIONAL INDUSTRIAL MARKETS

The industrial sector recorded moderate improvements during 3Q14:

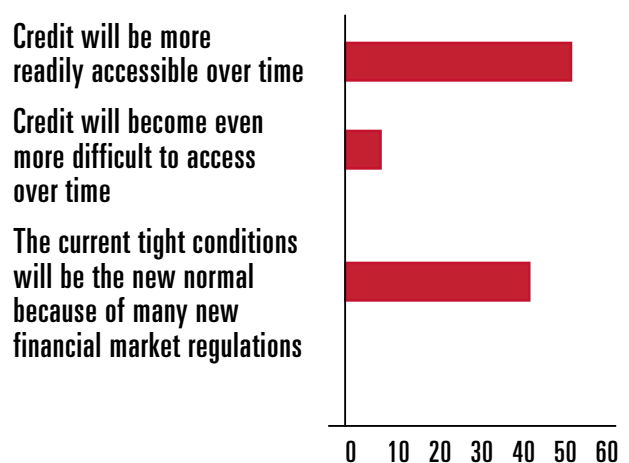
- Industrial deal flow was higher year over year for 71 percent of respondents (vs. 70 percent in 2Q14).
- Prices were even for 42 percent of respondents, and higher for 46 percent.
- Cap rates were flat for 46 percent, while 42 percent reported lower cap rates YOY.
- 62 percent of CCIM members reported higher rents.
- About 79 percent of respondents reported more buying inquiries in 3Q14.

#### FINANCE TRENDS (YoY) / Industrial Properties %



Source: CCIM Institute, National Association of Realtors®

#### FINANCE OUTLOOK / Industrial Properties %



Source: CCIM Institute, National Association of Realtors®

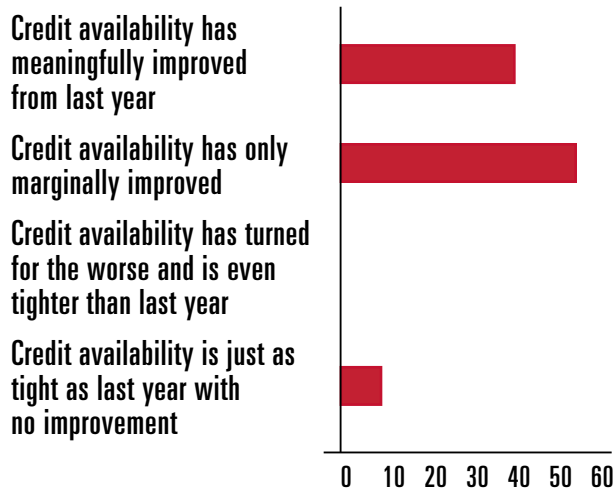
## Commercial Property SECTOR ANALYSIS

### NATIONAL RETAIL MARKETS

With rising consumer spending, the retail sector recorded positive trends in 3Q14:

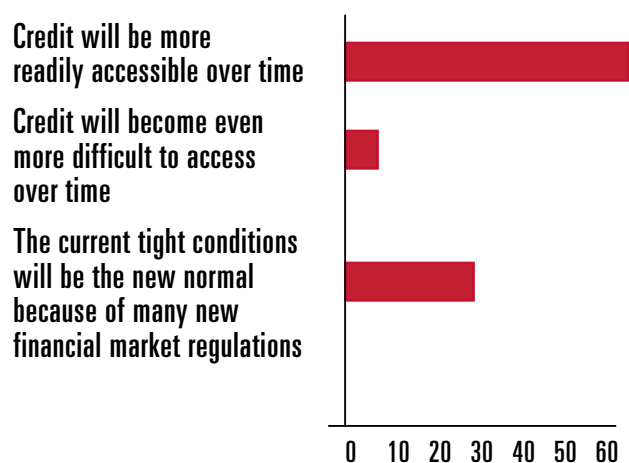
- Retail deals increased for 53 percent of respondents (compared with 59 percent in 2Q14).
- Prices were unchanged for 21 percent of respondents, and higher for 62 percent.
- Cap rates were the same for 41 percent of CCIMs, and lower for 56 percent.
- Rental income rose for 56 percent of CCIM members (vs. 53 percent in 2Q14).
- Respondents reported 67 percent more buying inquiries during 3Q14.

#### FINANCE TRENDS (YoY) / Retail %



Source: CCIM Institute, National Association of Realtors®

#### FINANCE OUTLOOK / Retail %



Source: CCIM Institute, National Association of Realtors®

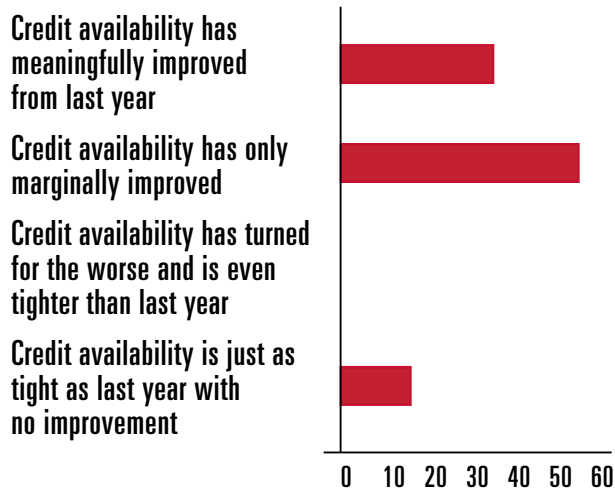
## Commercial Property SECTOR ANALYSIS

### NATIONAL MULTIFAMILY MARKETS

As more supply entered the market, trends for apartment properties moderated:

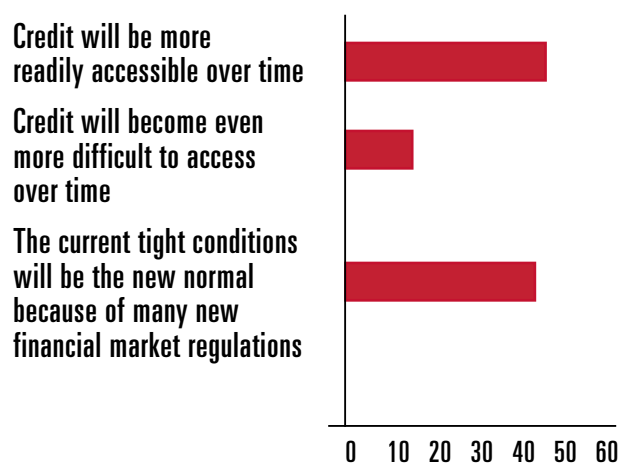
- 41 percent of respondents reported more deals YOY (vs. 46 percent in 2Q14).
- Prices were higher for 68 percent of respondents (vs. 69 percent in 2Q14).
- Cap rates were flat for 32 percent of respondents and lower for 68 percent.
- Rental income rose for 45 percent of respondents (vs. 56 percent in 2Q14).
- 59 percent of respondents reported more serious buying inquiries.

#### FINANCE TRENDS (YoY) / Multifamily %



Source: CCIM Institute, National Association of Realtors®

#### FINANCE OUTLOOK / Multifamily %



Source: CCIM Institute, National Association of Realtors®



## Commercial Real Estate Market UPDATE

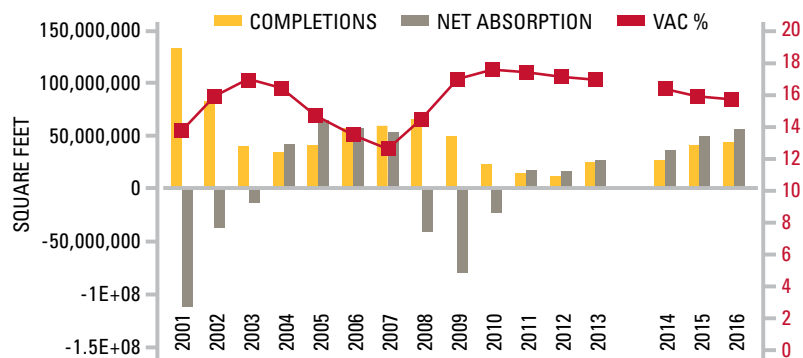
### OFFICE

With employment figures showing gains, especially for professional and business services, office fundamentals witnessed broader strengthening across U.S. markets in 2Q14. Fifty-one metro markets out of 82 posted improving absorption over the period, while 69 metros saw rising effective rents, according to Reis. However, at the national level, the vacancy rate was flat, due to an influx of new supply. During 2Q14, 4.33 million square feet of new office space entered the market and net absorption totaled 2.97 million sf. It seems that companies—even though hiring—are placing employees in existing space, without expanding their footprints.

A sign that fundamentals are continuing to improve, the steepest vacancy declines occurred in markets outside the tech and energy sectors. Washington, D.C., recorded the lowest vacancy rate in 2Q14 at 9.5 percent, with New York a close second. In terms of rent growth, technology and energy remain the best bets—Houston; San Jose, Calif.; San Francisco; Dallas; and New York are top picks.

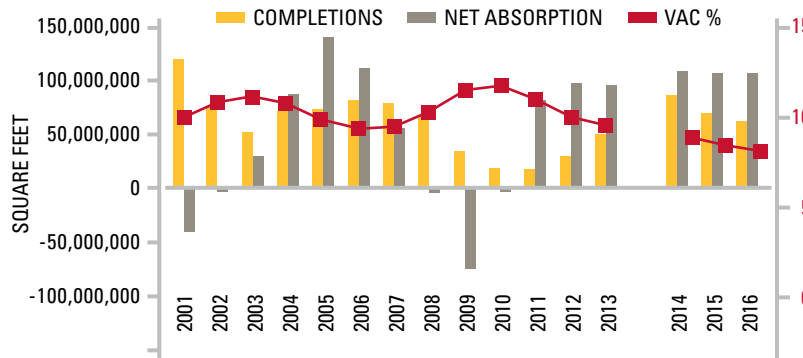
Asking rents for office space advanced 0.7 percent in 2Q14, to \$29.5 per square foot, according to Reis. Effective rents rose by an equal 0.7 percent during the period, aver-

### U.S. OFFICE FUNDAMENTALS



Sources: National Association of Realtors® / Reis, Inc.

### U.S. INDUSTRIAL FUNDAMENTALS



Sources: National Association of Realtors® / Reis, Inc.

aging about \$23.8 psf. Asking rents are projected to grow a total of 2.8 percent by year-end.

### INDUSTRIAL

Riding the rising wave of stronger second quarter economic activity, the industrial sector posted strong fundamentals during the period. With brisk international trade and

rising manufacturing, demand for warehouse and distribution centers was especially strong. For the quarter, net absorption totaled 21.5 million sf, according to Reis. New supply also picked up speed, adding 13.1 million sf to existing inventory. As a result, national vacancy rates declined 50 basis points YOY.

Industrial fundamentals showed positive performance across a wide

## Commercial Real Estate Market UPDATE

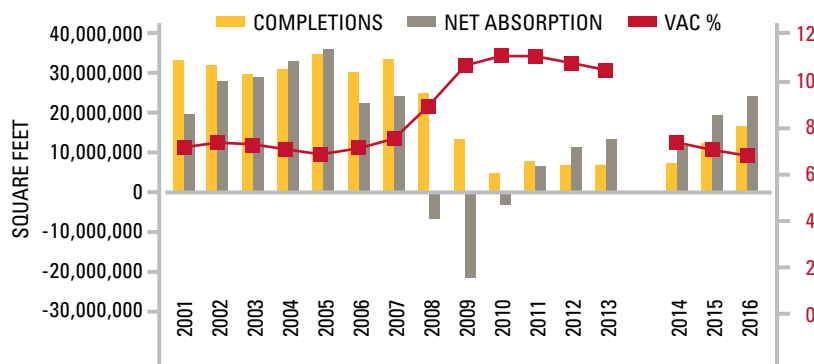
geographic range. Of the 47 metro markets tracked by Reis, 37 recorded improved absorption figures, 32 posted gains in occupancy and 46 had higher effective rents. Boston was the only market where effective rents remained flat. East Coast distribution centers had a particularly upbeat second quarter, delivering accelerating absorption, particularly Baltimore, Richmond, Va.; Raleigh-Durham, N.C.; and Palm Beach, Fla..

National asking rents for industrial spaces rose 0.4 percent, while effective rents gained 0.6 percent. Asking industrial rents are expected to increase 2.1 percent on a yearly basis by the end of 2014. Rents were strongest for large warehouse and distribution markets. Houston; San Bernardino/Riverside, Calif.; Kansas City; Chicago; Fort Worth, Texas; Memphis, Tenn.; and Atlanta all recorded rent growth in excess of 3.0 percent during 2Q14. In the flex/R&D space, West Coast markets were top performers, led by San Francisco, Los Angeles; San Bernardino/Riverside; Seattle; Orange County, Calif.; and San Jose.

### RETAIL

Increased consumer spending translated into an uptick in demand for retail spaces during 2Q14. Retail net absorption totaled 2.5 million sf, according to Reis. This was a notice-

### U.S. RETAIL FUNDAMENTALS



Sources: National Association of Realtors® / Reis, Inc.

### INCREASED CONSUMER SPENDING TRANSLATED INTO AN UPTICK IN DEMAND FOR RETAIL SPACE.

able improvement from 1Q14's dismal 771,000 sf, but below the same quarter in 2013. Across the U.S., 50 markets out of 80 tracked by Reis displayed stronger absorption figures. New completions also picked up from the glacial first quarter pace, bringing 1.4 million sf of retail space to market.

The retail vacancy rate declined 10 basis points. Markets with the lowest estimated vacancies for 3Q14 include San Francisco (3.5 percent), Fairfield County, N.Y.; (3.9 percent), San Jose (4.6 percent), Long Island, N.Y. (5.2

percent), and Orange County (5.3 percent).

Asking and effective rents rose by an equal 0.5 percent over the second quarter, to an average of \$19.5 and \$17.0 psf, respectively. Of the 80 metros analyzed by Reis, 63 posted higher effective rents. The projection for 2014 calls for retail rents to advance 2.0 percent.

### MULTIFAMILY

With improving employment figures, apartment demand continued growing in the second quarter. Net absorption totaled 35,539 units, according to Reis. Completions of new apartment units picked up pace from the first quarter, rising to a total of 34,431 units in the second quarter. New supply is expected to accelerate in the latter half of 2014, adding upward pressure on vacancies. The

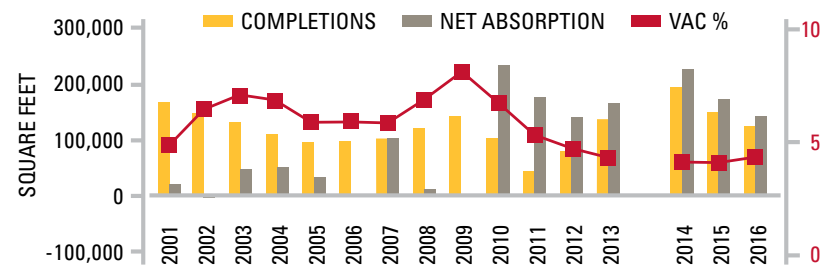
## Commercial Real Estate Market UPDATE

national vacancy rate remained unchanged. After a strong rebound and fast pace during the past five years, apartment fundamentals seem to be slowing down a bit. However, the performance of the sector is expected to remain comparatively strong going forward.

Absorption was positive in all 82 metro markets cataloged by Reis. New Haven, Conn., remained the tightest apartment market, with a vacancy rate of 2.2 percent during 2Q14. The second quarter witnessed relatively sharp declines in vacancies in a number of smaller markets. Columbia, S.C., and Tucson, Ariz., posted quarter-over-quarter vacancy declines of 50 basis points and 40 basis points, respectively. Rochester, Minn.; Richmond; New Orleans; Colorado Springs, Colo.; and Albuquerque, N.M., recorded availability compressions of 30 basis points on a quarterly basis.

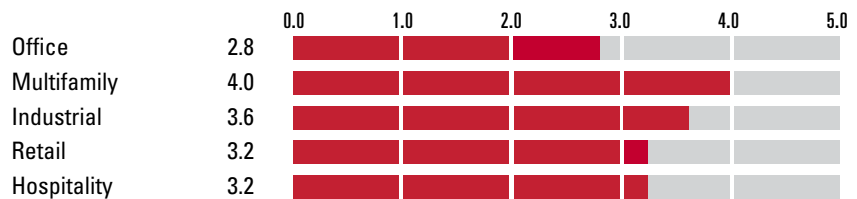
Apartment asking rents moved in line with historical trends. In the first quarter, asking rents advanced by 0.8 percent, while effective rents rose 0.9 percent, according to Reis. National effective rents were \$1,100 in the second quarter, with New York continuing as the most expensive market, with an effective monthly rent of \$3,100. Asking apartment rents are expected to rise at a 4.0 percent yearly rate during 2014.

### U.S. MULTIFAMILY FUNDAMENTALS



Sources: National Association of Realtors® / Reis, Inc.

### INVESTMENT CONDITIONS



Based on an August/September 2014 CCIM transaction survey.

### INVESTMENT VALUE VS. PRICE RATIO



Based on an August/September 2014 CCIM transaction survey.



## Commercial Real Estate Market UPDATE

### INVESTMENTS

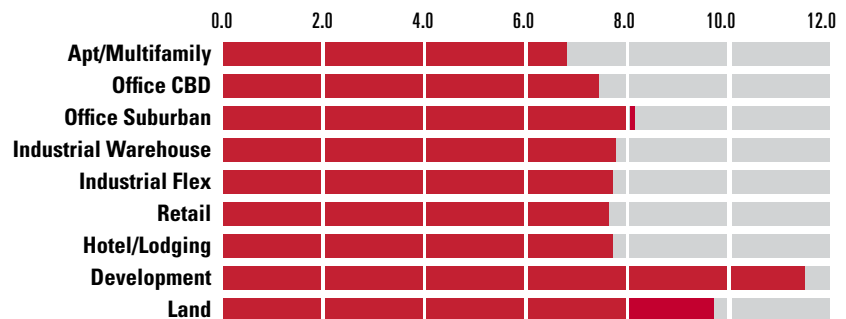
Sales of properties rose 7.0 percent on a yearly basis in 2Q14, down slightly from first quarter's 11.0 percent, according to the National Association of Realtors® 2Q14 Commercial Real Estate Market report. Prices for Realtor® commercial transactions advanced 3.0 percent YOY. A noticeable shortage of inventory remained the main concern during the second quarter, putting upward pressure on prices.

Cap rate compression eased in the second quarter, declining 34 basis points from a year ago. National cap rates averaged 8.3 percent in 2Q14, according to NAR. Hotels posted the lowest average cap rates at 8.0 percent, followed by apartments at 8.1 percent. Office and retail cap rates averaged 8.9 percent and 8.2 percent, respectively. Industrial properties posted cap rates of 8.4 percent.

### OUTLOOK THROUGH YEAR-END

Commercial real estate fundamentals are projected to continue on a positive path for the remainder of the year. Office vacancy rates are forecast to remain unchanged over the coming year, despite higher employment, as new inventory enters the market. Growing trade is poised to accelerate trends in the industrial sector, with strong absorption driving vacancy contractions. Retail spaces will continue to benefit from steady consumer spending. Even with slowing fundamentals, the multifamily sector is expected to perform well through year-end.

### NATIONAL AVERAGE CAP RATES (%)



Source: CCIM Institute, National Association of Realtors®

### NATIONAL CAP RATES BY REGION

	CANADA & MEXICO	EAST	MIDWEST	OTHER	SOUTH	WEST
Apartment Cap Rate	5.0%	6.8%	7.8%	6.4%	7.2%	5.7%
Office CBD Cap Rate	5.0	6.9	8.6	6.8	7.8	6.8
Office Suburban Cap Rate	6.0	7.4	8.9	7.4	8.4	7.5
Warehouse Cap Rate	7.0	7.9	8.1	7.6	8.3	7.0
Flex Cap Rate	-	8.0	8.4	7.5	8.3	7.1
Retail Cap Rate	6.0	6.8	8.5	6.5	7.7	6.9
Hotel Cap Rate	-	7.7	9.4	7.9	7.9	6.8
Development Cap Rate	-	9.8	12.3	8.7	11.9	13.7
Land Cap Rate	-	12.5	12.7	11.0	8.4	7.5

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## Commercial Real Estate FORECAST

Due to a number of factors, the U.S. economy is expected to perform at a quicker pace during the remainder of 2014. However, the pace of growth remains muted, tempering expectations for commercial real estate. Absorption is projected to continue growing, leading to declining vacancies across most property types. The forecast below projects conditions for the commercial sector through 2015.

### Commercial Real Estate / FORECAST THROUGH 2015

	2014 III	2014 IV	2015 I	2015 II	2015 III	2015 IV	2016 I	2014	2015	2016
<b>OFFICE</b>										
Vacancy Rate	15.70%	15.70%	15.90%	15.80%	15.70%	15.70%	15.70%	16.20%	15.80%	15.60%
Net Absorption (‘000 sq. ft.)	12,094	10,995	12,163	12,669	14,190	11,656	13,315	36,192	50,678	57,782
Completions (‘000 sq. ft.)	6,185	6,352	10,010	11,978	9,774	10,037	10,625	26,450	41,799	44,862
Inventory (‘000,000 sq. ft.)	4,099	4,105	4,115	4,127	4,137	4,147	4,158	4,105	4,147	4,192
Rent Growth	0.60%	0.60%	0.70%	0.80%	0.80%	0.90%	0.80%	2.60%	3.20%	3.60%
<b>INDUSTRIAL</b>										
Vacancy Rate	8.90%	8.80%	8.70%	8.50%	8.50%	8.40%	8.30%	8.90%	8.50%	8.10%
Net Absorption (‘000 sq. ft.)	27,971	24,744	18,891	26,237	31,484	28,336	18,908	107,580	104,948	105,044
Completions (‘000 sq. ft.)	16,953	16,133	14,439	21,314	19,939	13,063	12,961	83,424	68,755	61,720
Inventory (‘000,000 sq. ft.)	8,452	8,468	8,482	8,504	8,524	8,537	8,550	8,468	8,537	8,598
Rent Growth	0.60%	0.70%	0.60%	0.70%	0.70%	0.80%	0.70%	2.40%	2.80%	2.90%
<b>RETAIL</b>										
Vacancy Rate	9.80%	9.70%	9.80%	9.70%	9.60%	9.60%	9.60%	9.80%	9.70%	9.40%
Net Absorption (‘000 sq. ft.)	4,030	3,918	5,215	4,442	3,567	6,089	6,565	11,214	19,314	24,313
Completions (‘000 sq. ft.)	1,827	2,028	3,062	2,673	3,062	3,399	4,271	7,275	12,196	16,342
Inventory (‘000,000 sq. ft.)	2,033	2,035	2,036	2,039	2,042	2,046	2,050	2,035	2,046	2,062
Rent Growth	0.60%	0.60%	0.50%	0.60%	0.60%	0.70%	0.60%	2.00%	2.40%	3.00%
<b>MULTIFAMILY</b>										
Vacancy Rate	4.10%	4.00%	4.00%	4.00%	4.00%	4.00%	4.10%	4.00%	4.00%	4.20%
Net Absorption (Units)	67,429	63,595	43,399	39,969	38,106	48,590	35,778	223,421	170,065	140,128
Completions (Units)	49,475	47,123	29,143	38,899	37,843	40,576	26,257	191,481	146,461	122,381
Inventory (Units in millions)	10	10.1	10.1	10.1	10.1	10.2	10.2	10.1	10.2	10.3
Rent Growth	1.00%	1.00%	1.00%	1.00%	1.00%	0.90%	1.10%	4.00%	3.90%	3.50%

Sources: National Association of Realtors® / Reis, Inc.

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## U.S. Economic OVERVIEW

### U.S. ECONOMIC OUTLOOK / Actual and Forecasted

	2013 Q3	2013 Q4	2014 Q1	2014 Q2	2014 Q3	2014 Q4	2014 Q1	2015 Q2	2015 Q3	2015 Q4	2012	ANNUAL		
	History				Forecast*						History		Forecast*	
GDP g.r. (%)	4.5	3.5	-2.1	4	3.7	2.9	2.6	2.8	2.8	2.8	2.8	1.9	1.8	2.8
Non-farm Payroll Employment, g.r. (%)	1.6	1.8	1.5	2.2	2	2	1.8	1.9	1.9	1.9	1.7	1.7	1.9	1.9
Consumer prices, g.r. (%)	2.2	1.1	1.9	3	1.8	2.8	3	3.3	3.3	3.3	2.1	1.4	2.4	3.2
Unemployment rate (%)	7.2	7	6.7	6.2	6.1	6	5.9	5.8	5.8	5.8	8.1	7.4	6.3	5.8
30-Year Government Bond Yield (%)	2.9	2.8	2.8	2.6	2.5	2.7	2.9	3.3	3.5	3.7	2.9	3.4	2.7	3.4
30-Year-Fixed Mortgage Rate (%)	4.4	4.3	4.4	4.2	4.1	4.3	4.6	5	5.2	5.4	3.7	4.0	4.3	5.1
Consumer Confidence (1985=100)	81	74	80	83	90	90	91	91	90	90	67	73	86	91

\*National Association of REALTORS® Forecast as of September 2014

Although the U.S. economy's recovery from the Great Recession has been painful and slow, the country should see increased economic growth, additional jobs, and reasonable interest rates for the next 18 months. Lower than normal growth and high unemployment have been gradually receding, and the second half of 2014 is expected to show significant improvement over previous months. Projections indicate that 2015 should achieve almost normal economic growth.

#### ECONOMIC OUTLOOK: 2014-2015

The recovery from the Great Recession is now past its fifth year. The economic challenges appear to have left decision makers somewhat

hesitant, distrustful, and uneasy about the economic outlook:

- Consumer confidence has been slow to recover.
- At 67 months into the current expansion, the August unemployment rate was 6.1 percent. At a comparable time in the expansion of 1991-2001, the rate was 5.2 percent; the comparable rate for the 2001-07 expansion was 4.6 percent. The projected 5.8 percent unemployment rate is higher than would normally be expected.
- Partial employment recovery: Job additions averaged 215,000 for the first eight months of the year. In order to allow for new entrants to the workforce, the economy needs to add approx-

imately 125,000 additional jobs per month. At the current rate of job creation, the economy may not achieve full employment for another two years. The growth of part-time employment may be indicative of a lingering lack of confidence by employers in terms of the economic outlook.

- The economy has started to show some signs of acceleration, with the GDP growth rate in recent years having been disappointingly low. The projected 2.8 percent growth rate for 2015 will be better than experienced in the past two years, but still below 3.0 percent.

The economy is expected to grow at a yearly rate of approximately 2.8 percent in 2015, compared to 1.8 percent in 2014; with 10-year



## U.S. Economic OVERVIEW

government bonds at 3.4 percent, compared to 2.7 percent in 2014; and unemployment at 5.8 percent, compared to 6.3 percent in 2014.

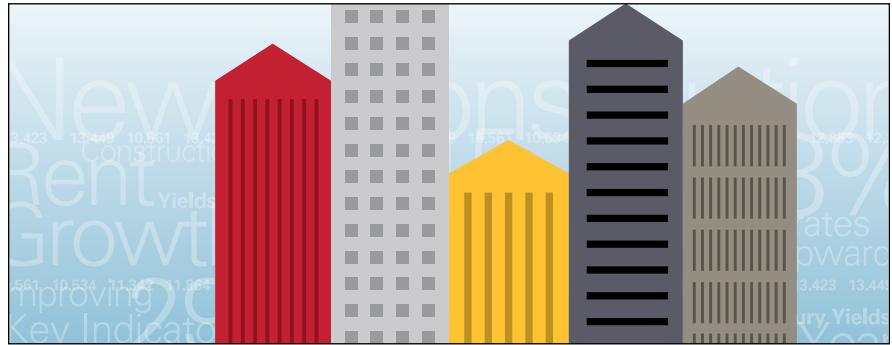
### GDP BY ECONOMIC SECTOR

A review of GDP by sector provides insight on the positive and negative features underlying current economic conditions. The downside risks of a no-growth economy or a recession in the near future appear to be minimal based on current trends in the data relative to previous economic conditions. Using the standard macroeconomic formula for GDP, the analysis of the specific components provides insight on the future course of the economy:

$$\text{GDP} = (\text{Consumption}) + (\text{Investment}) + (\text{Government Expenditures}) + (\text{Exports}) - (\text{Imports})$$

### CONSUMPTION

Personal consumption expenditures generally comprise approximately 67 percent of GDP. Any change in consumption will have a substantial impact on GDP levels. Starting with the beginning of the Great Recession, the growth of consumption lagged relative to previous trends. If consumption had continued to increase at previous rates after the Great Recession, personal consumption expenditures would have been



\$12.2 trillion rather than the actual \$10.9 trillion.

A number of factors have been cited as contributing to decreased consumption:

- Economic slowdown – standard economic theory identifies the circular flows of economic activity in determining GDP levels. Declining GDP can lead to declining consumption, which can lead to declining GDP and so forth on an ongoing basis.
- Household income – both median and average household income have declined in recent years.
- Decreased wealth – wealth has been increasingly concentrated in upper brackets, with the wealth distribution becoming increasingly unequal.
- Unemployment – levels have remained relatively high.
- Family formation – decreased family formation appears to have negatively impacted consumption.

Looking forward, there are a number of positive factors suggesting that the outlook for increased personal consumption expenditures is positive: Consumer confidence has been increasing, there has been additional job creation, household assets have recovered, and consumers have reduced debt loads. Therefore, an expectation of continued increases in personal consumption expenditures appears to be reasonable.

### PRIVATE DOMESTIC INVESTMENT

The major investment components comprising the GDP can be summarized as residential, non-residential, and changes in business inventories. Gross private domestic investment is approximately 17.0 percent of the GDP. Residential housing investment comprises 4.0 percent of GDP, with non-residential and inventory investment at approximately 13.0 percent.

- Residential investment/construction - in recent years, decreases in residential construction have had

## U.S. Economic OVERVIEW

a major negative impact on the economy. Housing starts declined from 2.2 million in 2005 to under 500,000 in 2009. A normal expectation for housing starts is approximately 1.5 million units per year. Currently, housing starts have rebounded to approximately 950,000 units per year.

- Tight credit conditions – tighter credit has had negative effects on builders, particularly small builders, who have traditionally produced half of the supply of new construction.
- Housing outlook – the outlook for 2014 housing starts is 1.041 million units, followed by 1.290 million units in 2015. This seems to be a reasonable expectation. The decline of housing starts during the Great Recession created a housing deficit relative to what would have normally been expected. In addition, housing starts are currently lower than they were in 2000, but there are an approximately 13 million additional households. Accordingly, residential construction appears likely to increase in the foreseeable future.



### THE MAJOR DRIVERS OF COMMERCIAL CONSTRUCTION ARE EMPLOYMENT ADDITIONS AND THE GDP.

#### BUSINESS INVESTMENT, PRIVATE NON RESIDENTIAL FIXED INVESTMENT

Business investment, including inventory changes, typically accounts for 13.0 percent to 15.0 percent of GDP and declined significantly during the Great Recession. The impact on the economy from non-residential fixed investment is now positive. Overall, the investment outlook supports continued economic expansion. Commercial construction, one of the components of business investment, is on the upswing. The major drivers of commercial construction are employment additions and the GDP. Accordingly, increased commercial construction appears to be likely.

#### GOVERNMENT EXPENDITURES

Government expenditures should continue to have an upward, favorable impact on the GDP. With an increased focus on efficiency and constrained by revenues government

expenditures declined during the Great Recession. Federal government expenditures impacting the GDP are now on an upward trend. State and local governments continue to expand their expenditures; income from tax revenues is increasing, and there is an increased desire for social amenities. Accordingly, there does not appear to be much downward expectation for government spending.

#### NET EXPORTS

The U.S. exports approximately \$2.3 trillion and imports approximately \$2.9 trillion of goods and services on a yearly basis: A total of \$5.2 trillion and 30 percent of GDP. The resulting net trade deficit actually impacting the GDP has been in the neighborhood of \$500 billion yearly. A trade deficit has a negative/downward impact on the economy.

The net deficit has currently narrowed somewhat from 2008, becoming less of a drag on the economy. However, the outlook for the net trade deficit in the next year will largely depend on the strength of the economies of the U.S. trading partners. As the U.S. economy continues to expand a higher level of imports appears to be likely. Recessions facing some trading partners could decrease the level of U.S. exports, worsening the trade deficit and its impact on the



## *U.S. Economic* OVERVIEW

GDP. For example, a slowdown in the European economies would have a negative impact, although the level of the impact would be in the low billions (not trillions) range.

Foreign recessions can impact the U.S. economy through decreased U.S. exports. The global economic environment remains mixed, but the broad picture points to an acceleration of economies into 2015 in many countries.

### **ECONOMIC OUTLOOK: UNCERTAINTIES AND FORECASTING**

The examination of the assumptions underlying an economic projection can identify factors creating forecast risks, i.e., over or under estimation relative to the actual outcome. Any economic forecast is based on an understanding of the economy and a variety of assumptions which may or may not be accurate—political or other circumstances may unexpectedly change.

### **THE UNCERTAINTIES**

Although foreign economies are generally in an expanding mode, there appear increasingly to be political risks in Eastern Europe, the Middle East, and Asia. Disturbances that decrease international trade will clearly have a negative impact on the U.S. economy. Despite exten-

sive discussions of foreign affairs in the media, the actual prediction of impacts is virtually impossible.

The Federal Reserve has kept the current levels of interest rate artificially low, reportedly in order to stimulate the economy and achieve a lower unemployment rate. Interest rates impact the economy, but at this time the size and timing of

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### **FOREIGN RECESSIONS CAN IMPACT THE U.S. ECONOMY THROUGH DECREASED U.S. EXPORTS.**

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any interest rate change is essentially unpredictable: Higher interest rates would probably slow growth; conversely, lower interest rates appear conducive to more rapid expansion. The media are filled with speculations about the timing of potential changes in interest rates, events impossible to predict.

Low interest rates are irrelevant if qualified borrowers are unable to obtain as much credit as is appropriate. As a result of the Great Recession, financial institutions tightened credit to an unreasonably

stringent degree. For example, NAR has estimated that home sales could rise by 10 percent if normal credit requirements were in place. A loosening of credit should have a positive effect on the forecast.

Although currently recovering, new-home construction has lagged following the Great Recession. Both interest rates and credit availability appear to have had a major impact on new construction. Construction trends can be volatile and could have an upward impact on the forecast if credit became more readily available.

Student debt is currently in excess of \$1 trillion. The average amount owed per borrower grew at 7 percent a year between 2004 and 2012, according to the Postsecondary National Policy Institute. Student debt levels may be negatively impacting home ownership. However, student debt levels do not appear likely to impact the economic projections over the time period 2014-2015.

Household formation is an important economic driver: The formation of new households generally means an additional need for space, home furnishings, etc. A decrease in household formation appears to have coincided with the Great Recession. To the degree that this trend changes in the next several years, the change is likely to be upwards, given the maturation of Generation Y.

## U.S. Economic OVERVIEW

Data indicate an increasing concentration in income and wealth compared to a decade ago. The Federal Reserve's Survey of Consumer Finances for 2013 has reported that over the 2010-13 time period, the median value of real family income fell by 5 percent, while the mean income increased by 4 percent. Decreased purchasing power coupled with limited income expectations by the bottom 60 percent of the population may be holding the economy to a lower expansion path.

Finally, job uncertainties are a major factor. Unemployed, underemployed, and missing-from-the-labor-force workers have continued to be a problem during the recent economic expansion. Unemployment levels have been high relative to previous experience, part-time work by workers who would like full time jobs has grown substantially, and a number of workers have simply dropped out of the labor force. A significant change in any of these factors would be an upscale risk to the forecast: More people working would almost certainly mean a higher level of GDP.

A variety of reasons for the sluggish labor market have been hypothesized, including continued obsolescence of smoke-stack industries, and a lack of trained workers. Lack of demand is another factor: To some degree the relatively high levels of unemploy-

### ECONOMIC CLIMATE BY REGION

	CANADA & MEXICO	EAST	MIDWEST	OTHER	SOUTH	WEST
The regional economic climate is booming	-	23.5%	5.7%	7.7%	31.1%	18.8%
The regional economic climate is level	100.0	29.4	28.6	30.8	15.6	18.8
The regional economic climate is moderately positive	-	41.2	45.7	53.8	48.9	50.0
The regional economic climate is stagnant	-	-	-	7.7	-	6.3
The regional economic climate is weak	-	5.9	20.0	-	4.4	6.3

*Based on an August/September 2014 CCIM transaction survey.*

### ECONOMIC RATE

		0.0	1.0	2.0	3.0	4.0	5.0
REGIONAL Average	3.7						
NATIONAL Average	3.1						

*Based on an August/September 2014 CCIM transaction survey.*

ment have been a function of the recession. This can be confirmed simply by noting that an expanding economy has accompanied some degree of job growth. Risk aversion is another factor: Some economic commentators have noted that businesses developed a degree of risk aversion during the Great Recession by not hiring workers even when there were openings and clear needs.

All of the risk factors mentioned are essentially unpredictable with any degree of accuracy on a consistent basis—so the forecast is based on “best guesses” about uncertain exogenous factors. If the economy were to

catch a break, for example, a decrease in international tensions leading to higher export levels or the Millennial generation suddenly moving towards increased household formation, then there could be a substantial upward impetus to the economy.

### CONCLUDING THOUGHTS

In examining all of the potential risks affecting the forecast, it appears that there is more upscale potential than negative potential to the economic outlook. Accordingly, an expansion in the neighborhood of 2.8 percent GDP growth in 2015 appears to be a reasonable forecast.

## U.S. Metropolitan ECONOMIC OUTLOOK

The leading market index uses an array of factors to assess the relative health of an individual market. The factors include job creation, unemployment claims, bankruptcy filings, and permits for construction. The first two factors provide an indication of potential business expansion/contraction as well as of labor market health and a leading

indicator of multifamily rental growth. Bankruptcy filings allude to the health of the business environment, while the permits data point to business plans and have an indirect impact on inventories.

The leading indicator is weighted based on both the current measure

as well as its recent trend or lagged measures. These weighted measures are then added to create a score. This score is then ranked relative to a fixed scale where a measure of 85 or better indicates a robust market, 75 to 85 a strong market, 65 to 75 an average market, and a score below 65 coincides with a weak market.

### LEADING INDICATOR INDEX

CITY	STATE	SCORE	LEADING INDICATOR	BANKRUPTCY FILINGS (2014 vs. 2013)*	UNEMPLOYMENT CLAIMS (2014 vs. 2013)**	UNEMPLOYMENT RATE as of JUL 2014	EMPLOYMENT (APR 2014 vs. APR 2013)**	TOTAL PERMITS (2014 vs. 2013)**
Phoenix	AZ	B	81.25	-12%	-1%	6.0%	2.7%	10%
Tucson	AZ	C	71.88	-12%	-1%	6.2%	2.5%	-10%
Los Angeles	CA	C	68.75	-28%	8%	7.3%	1.8%	0%
San Bernardino/Riverside	CA	C	71.88	-28%	8%	8.3%	3.2%	57%
Sacramento	CA	C	68.75	-28%	8%	6.9%	2.7%	49%
San Diego	CA	B	75.00	-28%	8%	6.0%	2.8%	10%
San Francisco	CA	B	75.00	-28%	8%	5.1%	2.8%	-8%
San Jose	CA	B	81.25	-28%	8%	5.4%	2.8%	20%
Colorado Springs	CO	B	84.38	-16%	-8%	6.5%	0.4%	18%
Denver	CO	A	90.63	-16%	-8%	5.1%	2.8%	9%
Hartford	CT	C	65.63	-5%	-10%	6.5%	0.6%	-12%
Washington	DC	B	81.25	-1%	0%	5.0%	0.6%	4%
Jacksonville	FL	D	62.50	-7%	-3%	5.9%	2.8%	-10%
Miami	FL	C	68.75	-7%	-3%	6.0%	3.3%	-1%
Orlando	FL	C	68.75	-7%	-3%	5.8%	3.5%	-3%
Tampa-St. Petersburg	FL	C	65.63	-7%	-3%	6.2%	1.7%	-13%
Atlanta	GA	C	68.75	-10%	-13%	7.4%	2.8%	19%
Chicago	IL	D	62.50	-9%	-12%	6.6%	1.0%	44%
Indianapolis	IN	B	78.13	-11%	-18%	5.3%	2.6%	34%
Lexington	KY	C	68.75	-5%	-13%	6.3%	1.3%	1%
Louisville	KY	C	68.75	-5%	-13%	6.8%	2.2%	15%

\* July 2013 through June 2014 vs. July 2012 through June 2013

\*\*August 2013 through July 2014 vs August 2012 through July 2013

\*\*\*September 2013 through August 2014 vs September 2012 through August 2014

# U.S. Metropolitan ECONOMIC OUTLOOK

## LEADING INDICATOR INDEX

CITY	STATE	SCORE	LEADING INDICATOR	BANKRUPTCY FILINGS (2014 vs. 2013)*	UNEMPLOYMENT CLAIMS (2014 vs. 2013)**	UNEMPLOYMENT RATE as of JUL 2014	EMPLOYMENT (APR 2014 vs. APR 2013)**	TOTAL PERMITS (2014 vs. 2013)**
New Orleans	LA	B	75.00	-2%	-22%	5.1%	2.7%	-5%
Boston	MA	A	90.63	-19%	-9%	5.0%	2.2%	3%
Baltimore	MD	C	71.88	-5%	-16%	6.2%	2.6%	-11%
Detroit	MI	C	71.88	-15%	-10%	8.7%	1.0%	18%
Minneapolis	MN	B	78.13	-13%	-7%	4.2%	2.8%	-3%
St. Louis	MO	C	71.88	-18%	-6%	6.8%	1.8%	7%
Kansas City	MO	C	65.63	-18%	-6%	6.2%	1.3%	20%
Greensboro/Winston-Salem	NC	B	78.13	-12%	-50%	6.6%	1.6%	30%
Raleigh-Durham	NC	B	84.38	-12%	-50%	5.1%	4.9%	-18%
Charlotte	NC	B	81.25	-12%	-50%	6.3%	3.0%	17%
Omaha	NE	B	78.13	-13%	-13%	3.9%	0.7%	-15%
Albuquerque	NM	C	68.75	-13%	-8%	6.8%	-0.1%	10%
Las Vegas	NV	B	81.25	-21%	-16%	7.7%	3.3%	11%
Buffalo	NY	B	78.13	-10%	-12%	6.1%	0.9%	5%
New York	NY	C	71.88	-10%	-12%	6.6%	1.8%	43%
Cleveland	OH	C	71.88	-12%	-16%	6.9%	1.5%	17%
Columbus	OH	B	84.38	-12%	-16%	4.5%	0.7%	6%
Cincinnati	OH	B	75.00	-12%	-16%	5.2%	1.9%	0%
Oklahoma City	OK	B	78.13	-10%	-14%	4.4%	3.5%	9%
Tulsa	OK	B	75.00	-10%	-14%	4.7%	1.7%	-2%
Portland	OR	C	71.88	-6%	-12%	6.1%	3.2%	7%
Pittsburgh	PA	C	68.75	-6%	-9%	5.3%	1.2%	-10%
Philadelphia	PA	C	71.88	-6%	-9%	6.0%	1.3%	29%
Providence	RI	B	78.13	-10%	-9%	7.6%	1.9%	11%
Charleston	SC	B	81.25	-1%	-17%	4.8%	0.8%	11%
Columbia	SC	C	68.75	-1%	-17%	5.2%	0.7%	-2%
Greenville	SC	B	75.00	-1%	-17%	4.8%	1.9%	44%
Knoxville	TN	C	71.88	-6%	-15%	5.9%	3.5%	31%
Nashville	TN	B	78.13	-6%	-15%	5.6%	2.8%	24%
Chattanooga	TN	C	65.63	-6%	-15%	6.7%	1.9%	47%
Memphis	TN	C	71.88	-6%	-15%	8.1%	1.6%	8%
Austin	TX	A	90.63	-11%	-5%	4.1%	3.9%	7%

\* July 2013 through June 2014 vs. July 2012 through June 2013

\*\*August 2013 through July 2014 vs August 2012 through July 2013

\*\*\*September 2013 through August 2014 vs September 2012 through August 2014

# U.S. Metropolitan ECONOMIC OUTLOOK

## LEADING INDICATOR INDEX

CITY	STATE	SCORE	LEADING INDICATOR	BANKRUPTCY FILINGS (2014 vs. 2013)*	UNEMPLOYMENT CLAIMS (2014 vs. 2013)**	UNEMPLOYMENT RATE as of JUL 2014	EMPLOYMENT (APR 2014 vs. APR 2013)**	TOTAL PERMITS (2014 vs. 2013)**
Dallas	TX	A	90.63	-11%	-5%	5.0%	3.8%	18%
Houston	TX	A	87.50	-11%	-5%	5.0%	3.9%	16%
San Antonio	TX	A	90.63	-11%	-5%	4.6%	2.4%	11%
Salt Lake City	UT	B	84.38	-8%	-12%	3.4%	2.9%	28%
Richmond	VA	B	84.38	-8%	-12%	5.5%	2.0%	3%
Seattle	WA	A	90.63	-14%	-8%	4.7%	3.1%	17%
Milwaukee	WI	C	71.88	-8%	-13%	6.2%	2.5%	12%
Birmingham	AL	C	71.88	-6%	-15%	6.0%	1.2%	21%
Little Rock	AR	C	71.88	-7%	-11%	5.6%	1.6%	-40%
New Haven	CT	C	71.88	-5%	-10%	6.7%	2.2%	40%
Wichita	KS	C	71.88	-7%	-11%	5.6%	0.9%	4%
Rochester	NY	B	81.25	-10%	-12%	5.9%	1.1%	6%
Syracuse	NY	C	71.88	-10%	-12%	6.2%	-0.6%	12%
Dayton	OH	B	75.00	-12%	-16%	5.5%	0.2%	-27%
Ventura County	CA	B	78.13	-28%	8%	6.4%	1.9%	8%
Westchester	NY	C	71.88	-10%	-12%	5.5%	-0.1%	-9%
Norfolk/Hampton Roads	VA	B	75.00	-8%	-12%	5.7%	0.4%	-20%
Tacoma	WA	B	78.13	-14%	-8%	6.2%	1.7%	17%
Orange County	CA	D	62.50	-28%	8%	5.7%	-0.6%	40%
Palm Beach	FL	B	75.00	-7%	-3%	5.9%	3.4%	3%
Fairfield County	CT	C	71.88	-5%	-10%	6.2%	1.1%	25%
Fort Lauderdale	FL	C	71.88	-7%	-3%	5.2%	3.1%	-1%
Fort Worth	TX	A	87.50	-11%	-5%	4.9%	3.0%	18%
Long Island	NY	B	81.25	-10%	-12%	5.0%	1.0%	43%
Northern New Jersey	NJ	C	68.75	-3%	-18%	6.3%	1.5%	33%
Oakland-East Bay	CA	C	71.88	-28%	8%	5.8%	2.3%	-8%
Suburban Maryland	MD	B	81.25	-5%	-16%	4.7%	0.2%	4%
Suburban Virginia	VA	B	84.38	-8%	-12%	4.1%	1.0%	4%
Durham	NC	A	90.63	-12%	-50%	5.0%	1.8%	22%
Raleigh-Cary	NC	B	84.38	-12%	-50%	5.1%	4.9%	-18%
Central New Jersey	NJ	C	65.63	-3%	-18%	6.4%	0.8%	22%

\* July 2013 through June 2014 vs. July 2012 through June 2013

\*\*August 2013 through July 2014 vs August 2012 through July 2013

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