AEW RESEARCH

U.S. Economic & Property Market Perspective

Q2 2022

AEW

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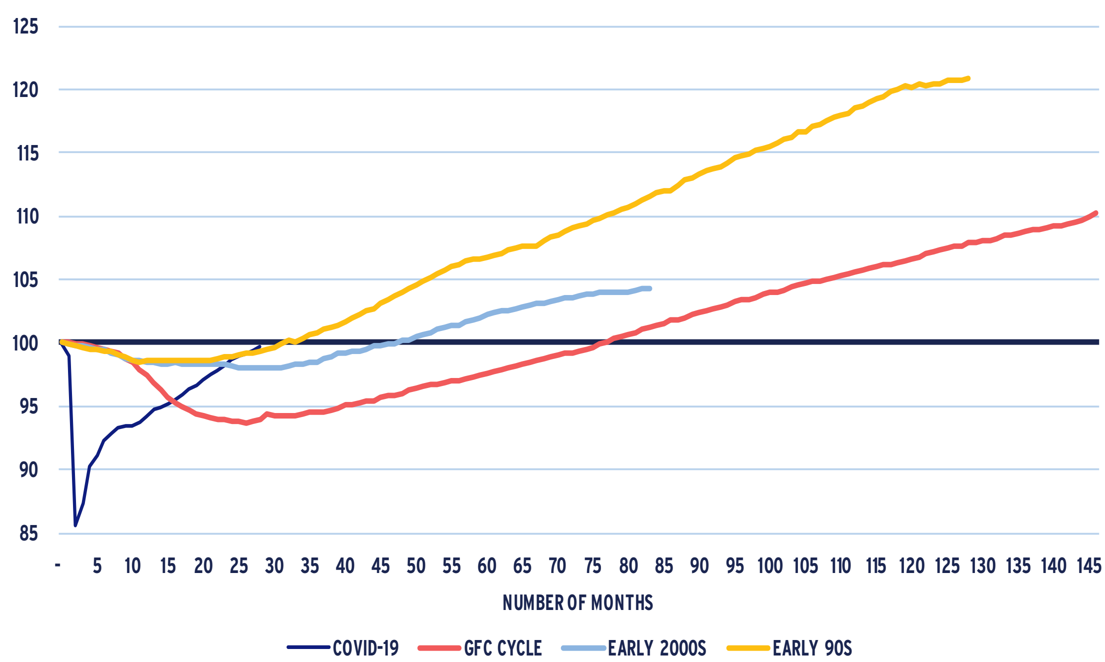
Prepared by AEW Research, August 2022

U.S Economic and Property Market Outlook

"History Doesn't Repeat Itself, But It Often Rhymes" *-Mark Twain*

The U.S. economy contracted slightly during the first half of 2022 with real GDP declining at an annual rate of -1.25% over the first two quarters. In aggregate, inflation adjusted GDP now stands -0.6% below the year-end 2021 level but still 2.5% above the prior pre-pandemic peak (2019 Q4) and 14% above the pandemic low (2020 Q2). While the ultimate assessment of whether this contraction constitutes an official recession will not likely be decided for some time by the National Bureau of Economic Research (NBER), such assessments are semantic distinctions. In practical terms, U.S. households and businesses are clearly struggling today, with persistent elevated inflation stemming, at least initially, from fiscal and monetary policy specifically designed to support and accelerate aggregate demand during the pandemic period and its aftermath. In broad terms, these policies were successful. The U.S. economy has returned to full employment faster than during any of the three prior economic downturns (see Figure 1).

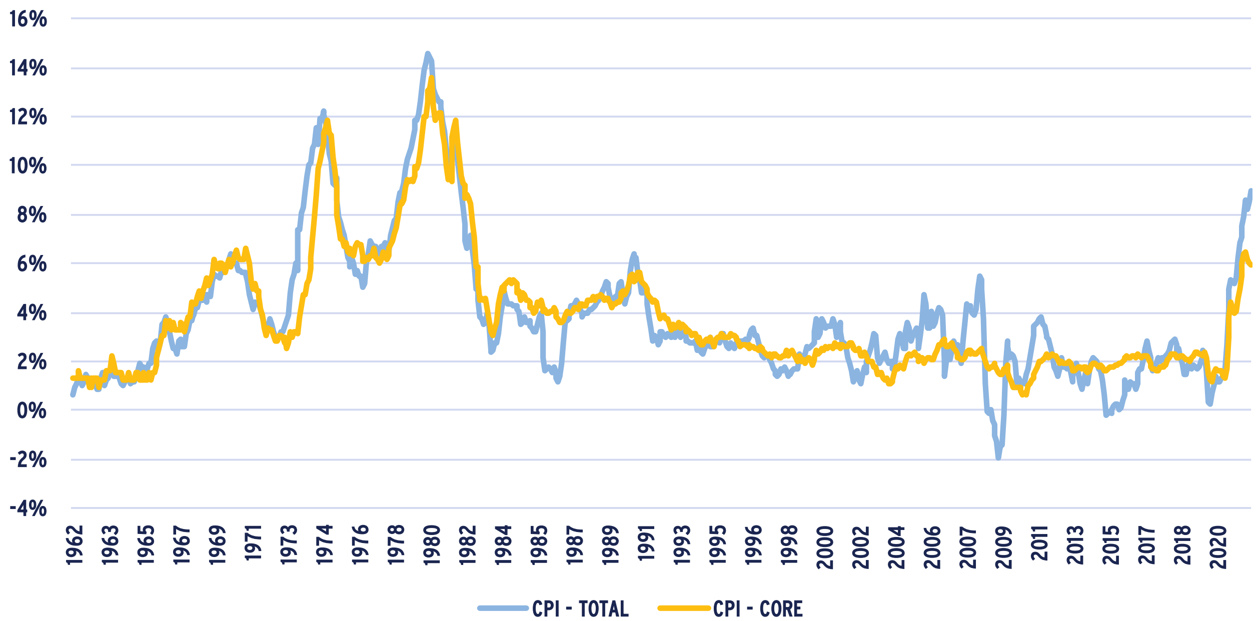
FIGURE 1
U.S. TOTAL EMPLOYMENT INDEXED TO 100 AT BEGINNING OF ECONOMIC DOWNTURN



Source: Bureau of Labor Statistics, as of June 2022

While there are myriad positive economic, social political and property market follow-on effects of returning to full employment quickly, these policies did come with a cost. Across the economy, demand accelerated more quickly than supply could respond, triggering higher and longer lasting than expected price inflation. The mismatch between post-COVID lockdown demand side and supply side re-starting has also been compounded by deleterious impacts of the war in Ukraine on global energy and food markets as well other inflationary consequences of follow-on lockdowns and other production bottlenecks in key supply areas such as China. Most importantly, broad elevated inflation has yet to show signs of abating despite some evidence of price pressures beginning to ease in various parts of the economy such as gasoline, copper and lumber as well some global measures of shipping costs and port backlogs.

FIGURE 2
YEAR-OVER-YEAR PERCENT CHANGE IN CONSUMER PRICE INDEX (CPI)

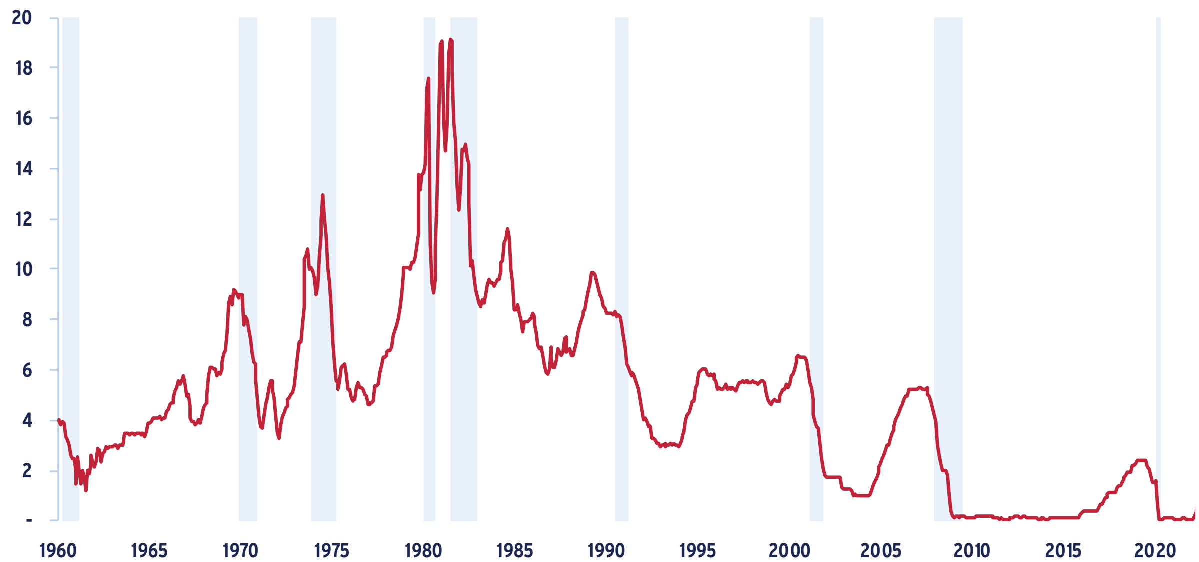


Source: Federal Reserve

The Federal Reserve has responded to higher and more persistent inflation by accelerating the pace at which overnight member bank borrowing costs will rise while also beginning the longer-term process of shrinking its balance sheet and slowing money supply growth[1], all with the goal of slowing aggregate demand and inflationary pressures. While the tools of modern monetary policy have evolved considerably since the financial crisis, they remain quite blunt and history shows that most, but not all, Fed tightening cycles have ended in recession (see Figure 3). As such, many asset markets globally have endured significant re-pricing as investors recalibrate their outlook for future earnings in the face of rising likelihood of recession as well as higher capital costs.

[1]A process referred to as quantitative tightening (QT), the undoing of so-called quantitative easing (QE).

FIGURE 3
FEDERAL FUNDS RATE AND PRIOR RECESSIONS



Source: Federal Reserve, NBER

U.S. Commercial Property

Against this backdrop of broad risk asset re-pricing, U.S. commercial property continues to post positive, albeit moderating, performance. For its part, the unleveraged NCREIF Property Index (NPI), again led by the industrial and apartment property sectors, recorded a second-quarter total return of 3.23% following the first-quarter return of 5.33%. For its part, the broad open-ended core fund index (ODCE) posted a second-quarter total return of 4.77%, also down from a first-quarter mark of 7.37%.

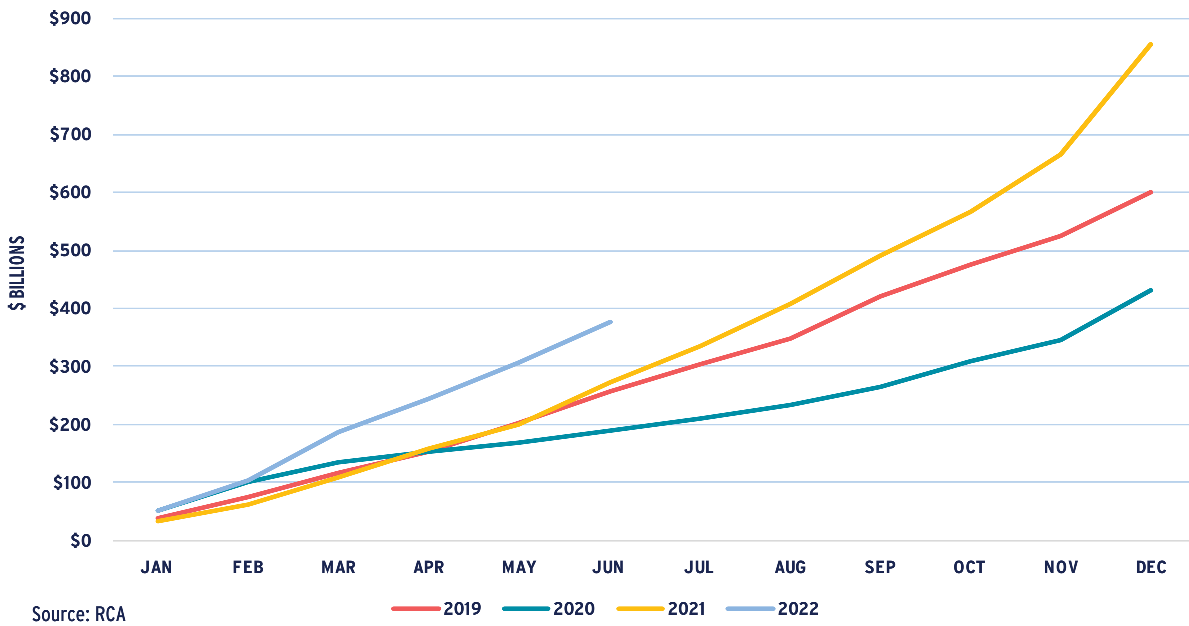
TABLE 1
TOTAL RETURN

	2022 Q2	2022 Q1	1 YEAR
NCREIF PROPERTY INDEX (NPI)	3.23%	5.33%	21.45%
NCREIF FUND INDEX - ODCE	4.77%	7.37%	29.51%
NAREIT EQUITY REIT INDEX	-14.68%	-5.26%	-5.89%
S&P 500 INDEX	-16.10%	-4.60%	-10.61%
NPI - PROPERTY SECTORS			
APARTMENT	3.86%	5.25%	24.40%
HOTEL	1.80%	1.76%	10.39%
INDUSTRIAL	5.86%	10.96%	47.67%
OFFICE	0.58%	1.60%	5.85%
RETAIL	1.68%	2.26%	3.97%

Source: NCREIF

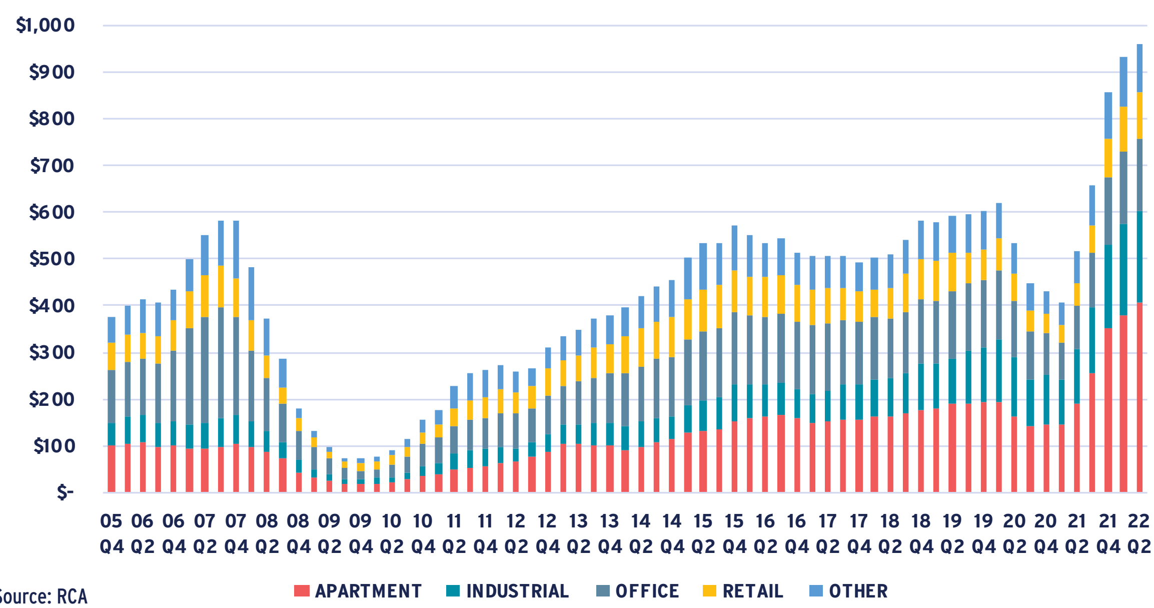
While not yet reflected in reported data, there are signs that property investor sentiment and capital pacing is slowing and that the market has entered a new period of price discovery for this cycle. Anecdotally, most major money center banks have recently slowed or stopped new lending activity, largely in response to external capital reserve requirements or internal allocation issues. In some cases, lender capital pacing during the first half of 2022 has already exceeded all of 2021 and there is little business case pressure to continue. Indeed, this is affirmed by the first half aggregate property transaction volume data highlighted in Figures 4 and 5, with total volume during the first six months of this year well ahead of the pacing of 2021 and 2019 (pre-COVID). More significantly, when viewed on a trailing four quarter basis, U.S. total property transaction volume is nearing an all-time peak of $1 trillion, far in excess of prior peaks in 2007 and 2019.

FIGURE 4
TOTAL COMMERCIAL PROPERTY TRANSACTION VOLUME BY YEAR



Source: RCA

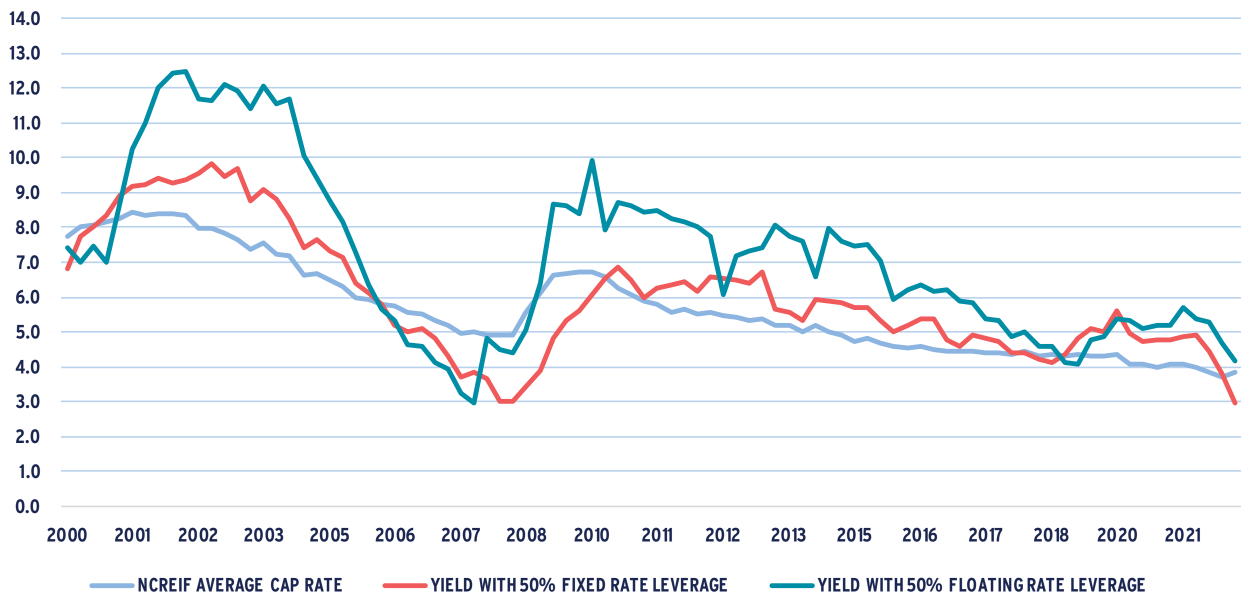
FIGURE 5
TOTAL COMMERCIAL PROPERTY TRANSACTION VOLUME BY SECTOR OVER PRIOR FOUR QUARTERS



Source: RCA

The combination of lender pullback and higher borrowing costs is quickly eroding the availability and the yield accretion of financial leverage, effectively pushing highly leveraged investors to the transaction market sidelines. As shown in Figure 6, the cost of most fixed-rate borrowing is already well above the average NPI property yield (cap rate), which stood at 3.8% as of the second quarter, and most floating-rate leverage is quickly moving in the same direction.

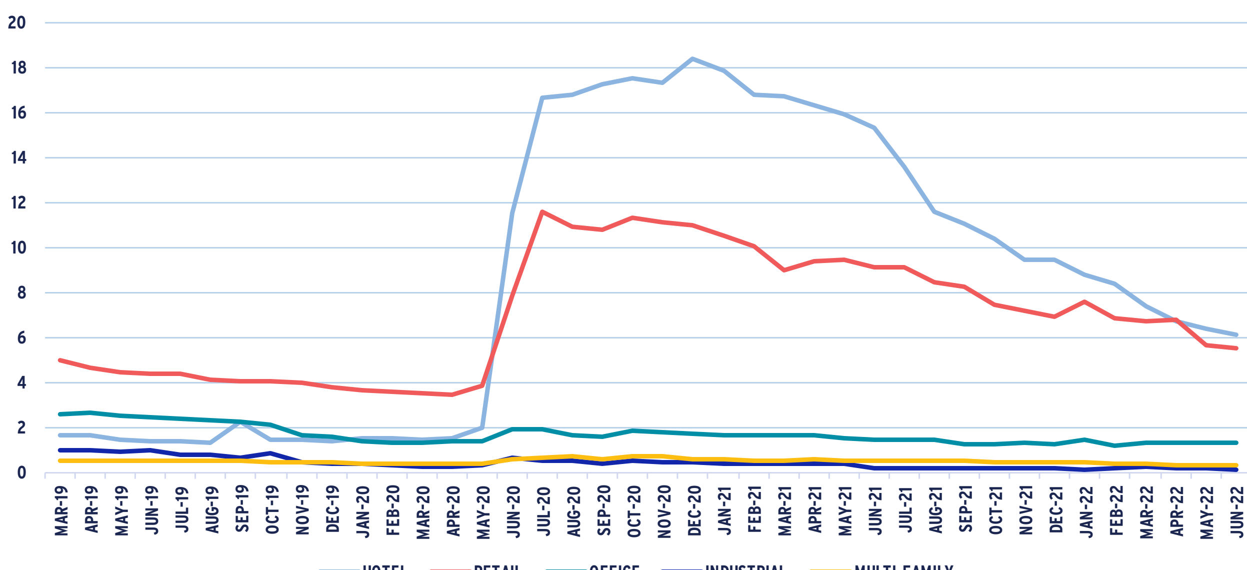
FIGURE 6
IMPACT OF LEVERAGE ON PROPERTY YIELDS (%)



Source: American Council of Life Insurers (ACLI), NCREIF

Thus far, property markets operating metrics, as evidenced by borrower delinquency, has remained quite strong. During the peak of COVID, certain property sectors such as hotels, segments of the retail market and some apartment properties did experience significant disruptions to property income severe enough to impact loan payments, but those impacts peaked during the latter half of 2020 and have been diminishing steadily
(see Figure 7).

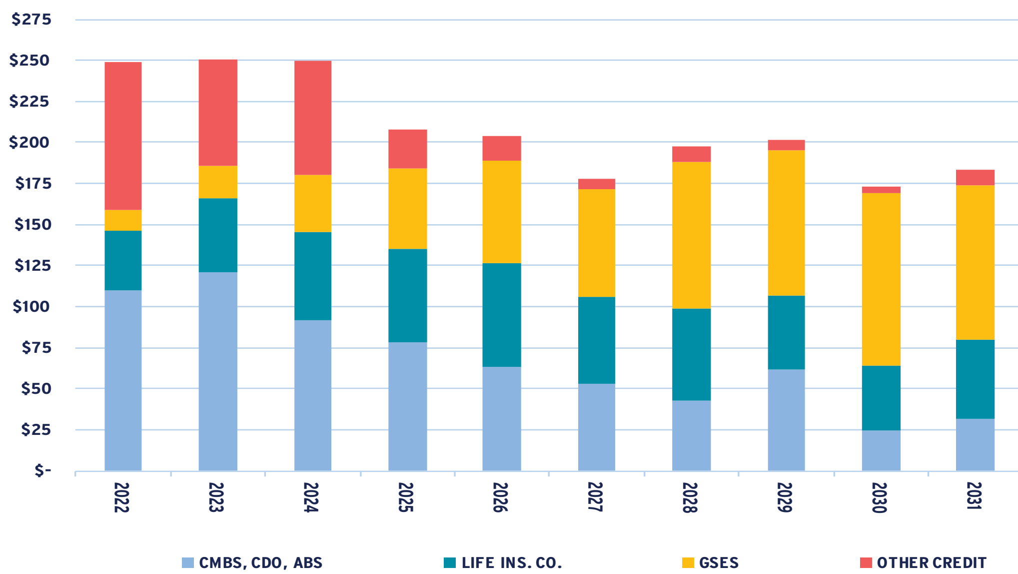
FIGURE 7
NCREIF PROPERTY INDEX (NPI) FOUR-QUARTER TOTAL RETURN BY PROPERTY TYPE



Source: Fitch

Greater recession risks will, of course, lead to greater risk of future operating performance downside. So far, except for the office market broadly, occupancy and rental rates have been improving as peak COVID effects on property markets fade. For their part, certain office properties and markets are experiencing unique challenges related to the now higher share of office-using employees now working somewhere other than their employers' office space. We do not expect this effect to lead to a significant near-term increase in office property operating defaults as most office tenants continue to honor their leases and most office property owners continue to service their debt. We do, however, anticipate the likelihood of higher levels of maturity defaults as loans mature into a market with fewer active lenders and more stringent underwriting assumptions regarding future structural vacancy and rental rates.

FIGURE 8
COMMERCIAL MORTGAGE LOAN MATURITIES BY YEAR AND TYPE OF ORIGINATOR



Source: Mortgage Bankers Association

Conclusion

Commercial real estate is both a financial and a physical asset. As a financial asset, it represents a claim on current and future income generated by property but this income, in turn, flows from its role as a physical asset. Property operating metrics such as occupancy and rental rates are ultimately a function of the health of a property's tenants and the economy they serve. Buoyed by unprecedented fiscal and monetary stimulus during the pandemic and its aftermath, U.S. commercial property has largely performed well and its value, similarly buoyed by extremely low interest rates and heightened financial liquidity, has soared. The future path for the broader economy is clearly less buoyant as the pandemic stimulus dissipates and decisionmakers across the economy contend, at least for some time, with higher prices, less predictable supply chains and greater volatility. All of this will ultimately impact property operating metrics.

Property's value as a financial asset reflects both the incomes it generates as well as the value that investors attach to such income streams. Investors in real-time auction markets such as equities and fixed income have, in recent months, re-priced those assets, sometimes significantly. Property largely still trades in a private, appraisal-based market that typically lags such events, often by as much as a year or more. So far, private market commercial property in aggregate has shown little or no re-pricing, but we must assume that there will eventually be some and we will likely point back to the end of the second quarter of 2022 as the inflection point of valuations for this cycle. The answers to the questions of how much and how fast are elusive. As Yogi Berra famously observed, "it's tough to make predictions, especially about the future."

Office

The office market continued to face headwinds through mid-year with elevated vacancies and ongoing demand challenges. However, a lack of employed people in office-using jobs is not primary among them. Office-using jobs currently stand ~3% above 2019 levels, besting the broader economy, which is achieving parity with pre-pandemic levels. Rather, the biggest challenge remains the shifting dynamics associated with remote working that are causing companies to reevaluate the type, location and aggregate need for office space. A return to full in-office workweeks appears notably less likely for most companies (although outside of the U.S. that is less the case) with a more structural shift underway. This is not to say all office-oriented jobs will be afforded this luxury or all employers will embrace it. The attributes of a hybrid model benefit both the employer in the form of reduced costs and the employee with lifestyle flexibility. There are also counter arguments - loss of work culture, less collaboration, lower productivity - all of which are difficult to measure. Still, companies have managed through the past 2+ years under varying degrees of remote work and have been successful, which does not go unnoticed. In aggregate, the tide continues to point toward the need for less versus more space.

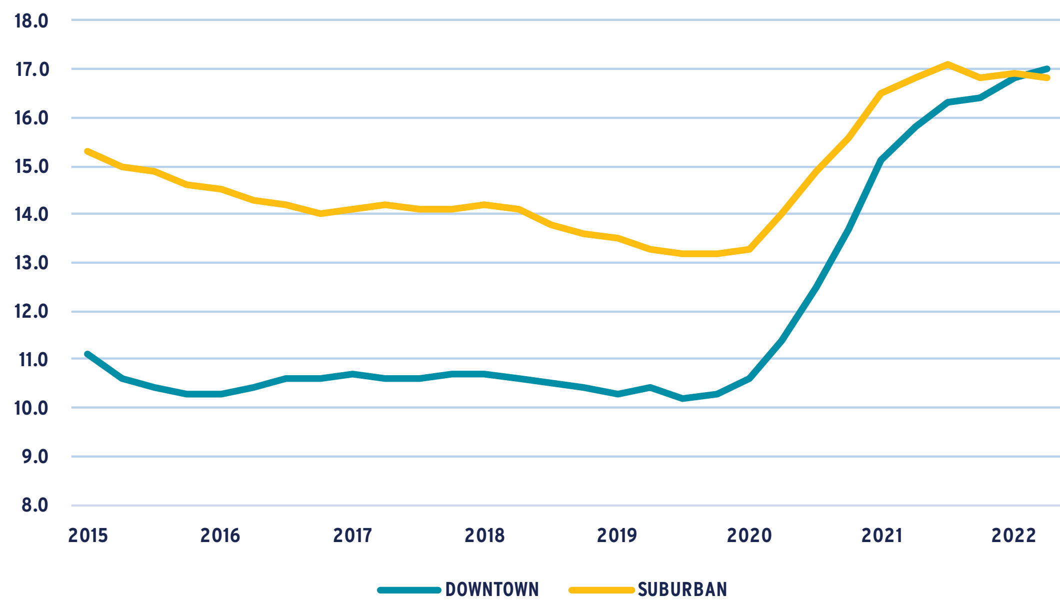
Office market vacancies inched up 10 bps to 16.9% for the quarter bringing the first half increase to 30 bps, continuing the pattern of rising rates albeit at a slower pace than 2021. The issues have been more pronounced in downtown markets, which averaged 10.3% prior to the pandemic but reached 17.0% in the second quarter, eclipsing suburban rates (16.8%) that stood at 13.2% in 2019. While every effort is being made to put the pandemic behind us, the evolution of new variants has weighed on employers' ability to fully implement return-to-work policies that will ultimately shape longer-term space needs. Office utilization (physical occupancy) has plateaued in the low-to-mid 40% range while other real-time metrics (restaurant reservations, travel, event attendance, etc.) across the broader economy have returned closer to pre-pandemic levels. Something more than just health-related issues are clearly at work when it comes to office use.

Leasing velocity has improved significantly but remains at 70% of pre-COVID levels. That said, velocity was sufficiently strong to generate 6.2 million square feet (msf) of positive net absorption for the quarter following the 1.1 msf recorded to start the year based on CBRE-EA's figures. Looking behind the scenes much of this gain was matched by an increase in sublease space suggesting the underlying demand dynamics are still in flux. A total of 6.8 msf of sublease space was added to the market in the first half of 2022. All told, sublease space now accounts for 2.1% of the 16.9% total office vacancy rate. In the Class A market, sublease space accounts for 2.4% of the 17.5% vacancy rate despite the flight to quality trends. More broadly, office tenants continue to take a measured approach to adjusting their space needs as the return-to-work dynamics continue to evolve with many companies choosing short-term lease extensions (1-2 years). For those making a more definitive decision, the dynamics appear to be more skewed to reducing or reconfiguring space at renewal or upgrading to better space with a move.

At the metro level, Houston and Dallas top the list in terms of vacancy rates at 25.6% and 22.8%, respectively, along with Portland (20.5%), Chicago (20.0%), Minneapolis (20.0%) and Nashville (19.2%). Portland and Nashville have seen some of the largest increases in vacancies over the past year. San Francisco, Seattle and Manhattan are also seeing notable increases. Markets with some of the tightest vacancies include West Palm Beach (10.1%), Orlando (11.1%), Raleigh (11.4%), Boston (11.8%), San Diego (13.7%) and Miami (14.7%), which are all benefitting from their high migration or life science exposures. Except for San Diego (+20 bps), each of these markets saw vacancies fall with Miami and Raleigh dropping 100 and 90 bps, respectively.

Overall, AEW Research reaffirms its belief that many companies will embrace a more fully integrated hybrid work model that will translate into a reduction in aggregate demand. That said, it will take time to play out as firms assess the impact of the shifting work model on productivity, profitability and the ability to retain talent. We are seeing this translate into a skewed demand for quality space and location premiums. It will be interesting to see the dynamic unfold over the next couple of quarters as economic conditions adjust and the FOMC continues to attack inflationary pressures.

OFFICE MARKET VACANCY RATES: DOWNTOWN VS SUBURBAN



Source: CBRE-EA

OFFICE	
Vacancy Rate	16.9%
12-Month Historical Trend	
Vacancy Change	↑
Rent	↓
Absorption	↑
Completions	↓
Cap Rates	↔
Transaction Volume	↓

Source: CBRE-EA, RCA and NCREIF

Apartment

According to CBRE-EA preliminary data, apartment market vacancies increased to 3.1% in the second quarter of 2022, up 80 basis points (bps) quarter over quarter (QOQ) but down 100 bps year over year (YOY). Vacancies while up in the quarter remain exceptionally low. Indeed, vacancies are roughly 200 bps below the market's 15-year historical average of 5.0% (2007-2021).

The uptick in vacancy was driven by the return of nearly 39,000 units to the market and the completion of roughly 79,000 units. Over the past year, however, over 475,000 units were absorbed, more than 2.5 times the historical average. Construction activity remains robust but is well short of demand with one-year completions of 307,000 units. With strong demand and exceptionally low vacancies, effective rents advanced 14.6% on a YOY-basis in the second quarter. This follows growth of 15.3% and 13.4% YOY in the previous two quarters, respectively. Overall, since the 2020 Q4 COVID low, rents have increased by 19.1% and are 13.3% above their pre-COVID peak.

By market, the Sunbelt markets, which outperformed during COVID and subsequent recovery, showed the largest increases in vacancy. West Palm Beach, Tucson, Phoenix, Las Vegas, Jacksonville, Houston, Fort Lauderdale, Atlanta, Tampa, Raleigh, Fort Worth, Dallas, San Antonio, Richmond, Austin, Memphis, Greensboro and Charlotte all reported a QOQ uptick in vacancies of 100+ bps. Meanwhile, markets that were harder hit during COVID and lagged in the recovery showed more steady performance. Indeed, New York, San Jose, Minneapolis, Boston, Philadelphia, Chicago, Seattle, San Diego, Orange County, San Francisco and Los Angeles posted an increase in vacancies of between 10 bps and 60 bps on the quarter. The performance was similar on a YOY basis, with the markets hit harder by COVID outperforming the Sunbelt (see chart).

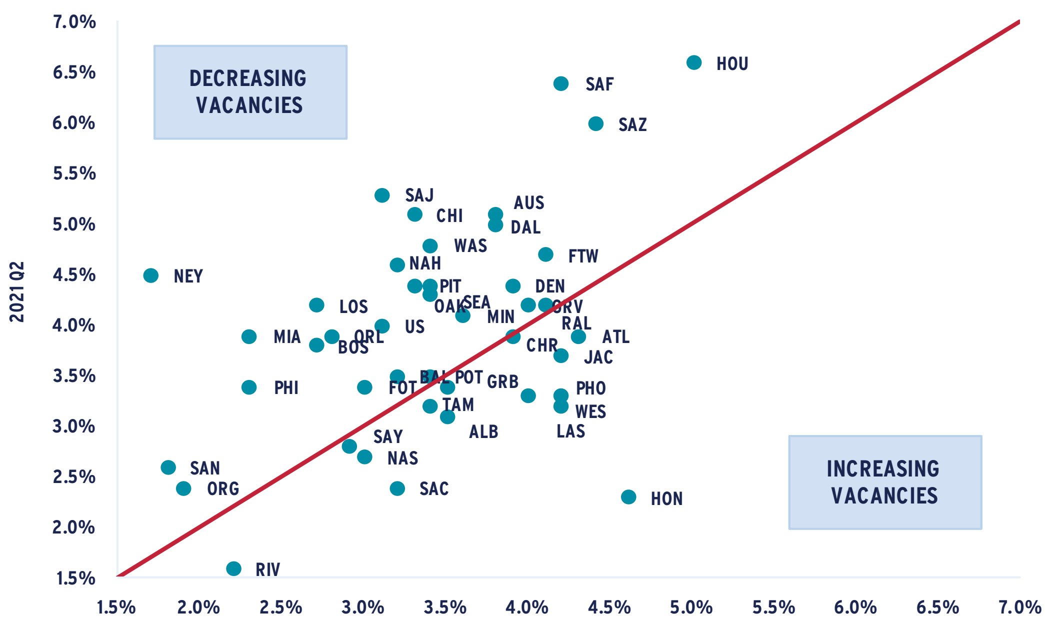
Despite the increase in vacancies, it is important to note that all markets remain exceptionally tight with nearly all reporting vacancies well below historical averages. 2022 Q2 vacancies by market were 100+ bps below the historical average in all markets with the exception of Oakland (-80 bps), Long Island (-50 bps), Minneapolis (-40 bps) and San Francisco where vacancies were equal to the market's 15-year historical average. Not surprisingly, Sunbelt markets showed a disproportionately large gap between current vacancies and historical vacancies, with vacancies that were generally 180+ bps below their historical average.

Reflecting the still solid market conditions, rent growth remained robust. West Palm Beach, which experienced the largest quarterly gain in vacancy, posted a 26.2% YOY increase in effective rent, the largest gain among all markets. Further, Sunbelt markets dominated in terms of rent performance with the top 10 largest YOY rent gains being reported in the Sunbelt (West Palm Beach, Fort Lauderdale, Orlando, Tampa, Miami, Nashville, Raleigh, Jacksonville and Phoenix). Further, rents in all markets, except for San Jose (-0.3%) and San Francisco (-7.1%), have well surpassed their prior peak. Again, Sunbelt markets have exhibited the largest growth with rents generally 25% to 38% above their prior peak.

Given the run up in rents, affordability is a concern. Indeed, income growth has lagged far behind both rent growth and home price appreciation. In many Sunbelt markets, the rent-to-income ratio is now over 30%. In West Palm Beach, the average rent to median household income is now 39%, up from 30% in late 2019. This means the median household would not qualify for the average rent in the metro area today, while they qualified a mere two years ago. Additionally, Miami, which was unaffordable in 2019 with a rent-to-income ratio of 36.6%, has the highest rent-to-income ratio today at 41.7%, surpassing New York's 41.5%. Meanwhile, the housing affordability index (HAI), which measures the ability of the median household to afford the median single-family home, has declined across all markets. Austin, Phoenix, Atlanta, Raleigh, Tampa, Charlotte, Las Vegas, Orange County, Salt Lake City and Nashville have all reported a decline in the HAI of over 40%; Riverside, Cincinnati, San Jose, New York, West Palm Beach, Seattle, Sacramento, Miami, Jacksonville, Fort Lauderdale, Orlando, Portland, and Oakland followed with a decline between 37% and 40%, outpacing the national decline of 36%.

With rising mortgage rates and the risk of recession increasing, the potential for a correction in the housing market has also increased. Sunbelt markets are at a greater risk given their outsized increase in home prices and drop off in affordability. A correction in the housing market would likely moderate apartment rent growth, as apartment rent growth typically lags home price appreciation (or depreciation) by 12-18 months. Moreover, greater economic uncertainty is also likely to weigh on household formation and subsequently apartment demand. Indeed, leasing traffic has slowed in many apartment markets in recent weeks. That said, a housing market correction would likely yield greater apartment demand, both creating renters by need (through increased foreclosures) and renters by choice (those waiting for the housing market to stabilize). This would work to shore up demand for apartments and subsequently rents, perhaps limiting any potential correction in apartment rents. Overall, it appears the market is headed for a period of moderation, both in terms of demand and rent growth. The outsized gains of late are likely to temper going forward. In sum, AEW expects the market will remain healthy and allow for continued, albeit more moderate, rent growth in the coming quarters.

YEAR-OVER-YEAR VACANCY COMPARISON



Source: CBRE-EA

APARTMENT	
Vacancy Rate	3.1%
12-Month Historical Trend	
Vacancy Change	↓
Rent	↑
Absorption	↓
Completions	↑
Cap Rates	↔
Transaction Volume	↑

Source: CBRE-EA, RCA and NCREIF

Industrial

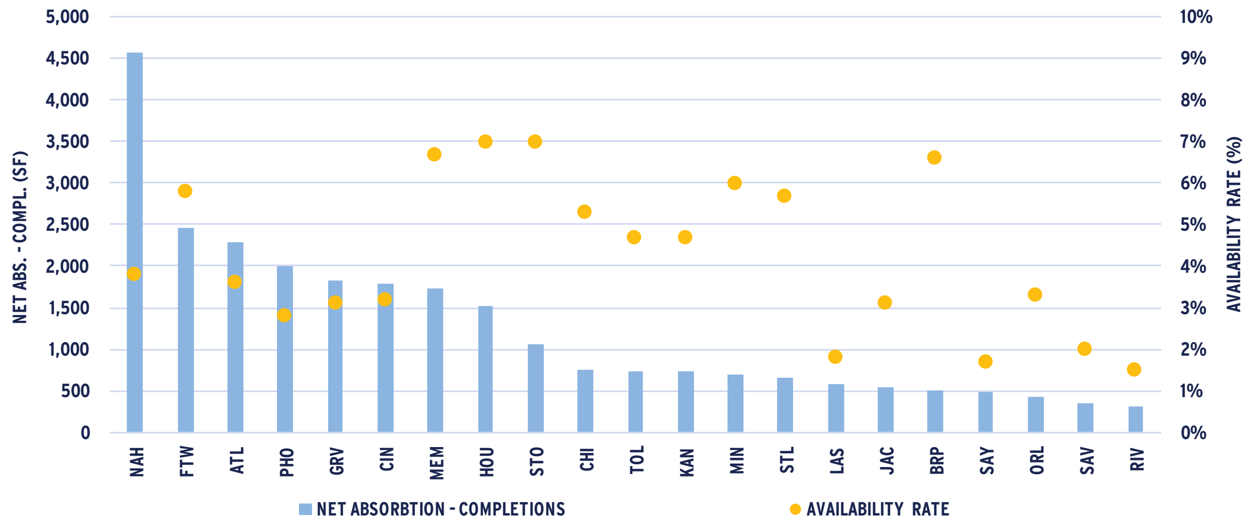
In the second quarter of 2022, the industrial property sector remained incredibly healthy, maintaining its record low availability rate of 4.6%. Availability in the quarter was on par with 2022 Q1 but was an improvement of 100 basis points (bps) from the prior year. Availability stands 460 bps below its historical average of 9.2% (tracked since 1989 Q1). This quarter, 64.6 million square feet (msf) of completions just eclipsed the healthy net absorption of 60.2 msf. Net absorption was down significantly from the 127.7 msf quarterly average seen over the previous year; given the low availability rate, however, the slowdown in demand may be due to the lack of available space to lease, particularly in the tighter markets. Additionally, new completions were down 19.1% in the second quarter compared with the 77.0 msf average deliveries seen over the previous four quarters.

Recently, in the fourth quarter of 2021, the industrial sector reported the highest level of quarterly completions seen in over two decades, with 100.2 msf delivered (only surpassed by the 104.8 msf of completions in 2000 Q4). However, even with the considerable completions of 311.4 msf over the last year, ample demand of 450.9 msf surpassed the new supply. Demand of late has been noteworthy, with 509.3 msf absorbed on annual basis in 2021, the highest level of annual demand in the sector's history. With the Q2 availability rate maintaining its historic low, completions trending downwards from their recent peak and solid demand, rents have been driven upward. This quarter, the CBRE-EA rent index reached a new record high of $9.33, up 12.0% year over year.

In terms of performance on a metro level, while supply pipelines have been active, the 2022 Q2 net absorption still surpassed new completions in dozens of metros. Of the 69 markets tracked by CBRE-EA, 37 reported levels of demand that outpaced completions. In the set that reported demand outpacing supply, the gap between demand and supply averaged 780,000 sf. The largest gap was in Nashville, where net absorption exceeded completions by 4.6 msf. Per CoStar, Nashville's industrial market has been boosted by its central geographic location, which has attracted e-commerce and third-party logistics firms.

Decreases in industrial availability have been widespread across most metros. Only 24 of the 69 markets tracked by CBRE-EA reported increases to availability year to date (YTD). Of the set of 40 markets that reported a decrease in availability so far this year, the average improvement was roughly 80 bps. Some of the industrial markets with the most noted YTD changes include Nashville (-240 bps), Manhattan (-190 bps), Charleston (-170 bps) and Wilmington (-170 bps). Several markets reported exceptionally tight 2022 Q2 availability rates, such as Riverside (1.5%), Charleston (1.7%), Salt Lake City (1.7%), Las Vegas (1.8%), Savannah (2.0%) and Albuquerque (2.0%).
While the industrial sector is currently reporting impressive fundamentals, there are several headwinds related to challenges in the broader economy. Per the Federal Reserve's Beige Book released in June 2022, consumer confidence has started to take a hit. Households and businesses are dealing with rising interest rates, breakneck inflation, labor market difficulties and supply chain disruptions. The shortages of labor and material have caused delays in industrial construction. With reduced disposable income, customers are beginning to reduce their purchasing, which may abate the noted rise in e-commerce sales. Across several major markets, while industrial activity is currently strong, the sector has begun to show some deceleration in leasing from the highs seen during the peak of the pandemic. Per CBRE, construction costs for the industrial sector have increased by 10-20% due to the rising cost of labor and per CoStar, the sector's largest tenant, Amazon, is slowing its expansion. These challenges are likely to moderate industrial market fundamentals in the short term.

2022 Q2 - GAPS IN SUPPLY AND DEMAND



Source: CBRE-EA

INDUSTRIAL	
Availability Rate	4.6%
12-Month Historical Trend	
Availability Change	↓
Rent	↑
Absorption	↑
Completions	↔
Cap Rates	↓
Transaction Volume	↑

Source: CBRE-EA, RCA and NCREIF

Retail

At the midway point of 2022, the retail sector has continued to see improvement from pandemic-related lows, with fundamentals bolstered by the minimal levels of new supply. Per CBRE-EA, as of the second quarter of 2022, total retail availability stood at 5.1%, down 20 basis points (bps) from the prior quarter and down 110 bps year over year (YOY). Impressively, this is a historical low for total retail availability. This quarter, 19.9 million square feet (msf) of space were absorbed, while just 3.6 msf were completed. This is the lowest level of completions seen in a single quarter in the sector's history, a sharp drop from the 13.4 msf of new deliveries seen each quarter on average over the last decade. The contraction in new supply has been met with solid net absorption, improving the availability rate and total retail fundamentals. While the sector reported two quarters of negative net absorption in 2020 Q2 and Q3, in the 7 quarters since, net absorption has been positive and totaled 166.9 msf, surpassing the 51.0 msf delivered since the pandemic's peak. Limited completions and tightening availability have driven up rents, setting record highs for gross asking rent ($19.93/sf), net asking rent ($20.52/sf), and EA asking rent ($22.39/sf).

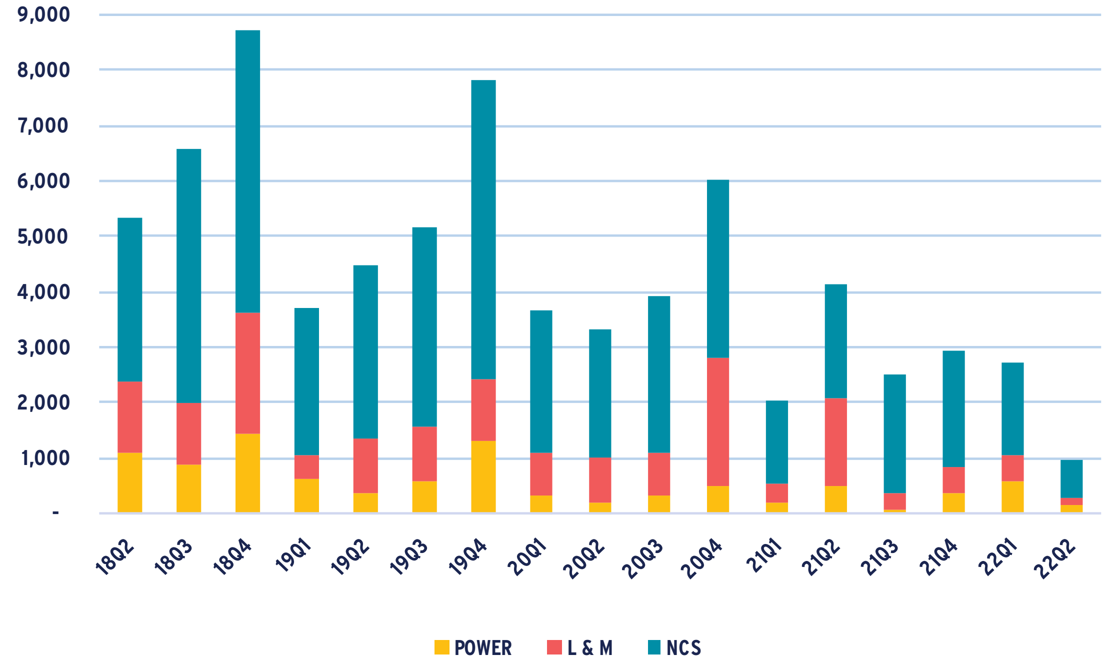
The neighborhood, community, and strip center (NCSC) subtype is now fully recovered. As of 2022 Q2, availability was 7.3%, down 30 bps on the quarter and 150 bps on the year. This is the tightest availability rate in the subtype's history. As seen with total retail, completions slowed to a crawl, with just 662,000 sf delivered, a considerable reduction compared with the 3.9 msf average quarterly completions seen over the last decade. Net absorption remained solid this quarter at 9.7 msf. Of the 64 markets tracked by CBRE-EA, the year-to-date (YTD) availability rate increased in just four markets: Honolulu (90 bps), Louisville (40 bps), Ventura (10 bps) and San Jose (10 bps). The 57 markets that reported a YTD improvement in availability averaged an 80-bps tightening, with the largest improvements seen in Westchester (-280 bps), Albuquerque (-230 bps), Tucson (-150 bps) and Austin (-140 bps).

The power center subtype has also seen conditions improve, with a Q2 availability rate of 5.6%, down 50 bps on the quarter and 170 bps on the year. This is the lowest availability rate for the subtype in over five years and is 90 bps below the historical average of 6.5%. This quarter, 3.0 msf of net absorption outpaced completions of 149,000 sf. Improvements were seen across markets but were not as widespread as in the NCSC subtype; 12 markets reported YTD increases in availability. However, the markets that did improve were better off by a considerable amount. The 47 markets that reported an improvement of availability YTD averaged a 120-bps decrease, with the largest improvements seen in Honolulu (-440 bps), San Francisco (-370 bps), Jacksonville (-320 bps) and Chicago (-280 bps). In fact, 23 markets reported an improvement YTD of 100 or more basis points.

Even the recently challenged lifestyle & mall (L&M) subtype appears to be stabilizing. Second-quarter availability stood at 6.1%, on par with the prior quarter and down 50 bps YOY. This quarter, there was negative net absorption of 251,000 sf with 149,000 sf of completions. This is the lowest level of deliveries in the subtype's history. Rents are still recovering, with the EA asking rent of $34.17/sf just 1.0% below its 2019 Q1 peak of $34.50/sf. When looking at L&M performance by market, there was a wide range in fundamentals. Jacksonville has the highest availability rate in the nation at 20.8%, up 610 bps YTD. Of the 64 tracked markets, 18 reported increases in availability this year. However, some markets saw dramatic improvements; of the 42 markets that have had tightening availability rates so far this year, the average decrease was 170 bps. This was partially driven by big changes in a few markets. Albuquerque reported a Q2 availability rate of 1.2%, down 15.2 percentage points YTD. Other markets with large improvements include Cincinnati (-1,210 bps), Birmingham (-570 bps), Tulsa (-520 bps) and San Francisco (-350 bps). Per GreenStreet, mall performance has continued to depend on the mall's quality; Class A malls are seeing successful performance, while malls rated B- or below are struggling to maintain adequate levels of foot traffic.

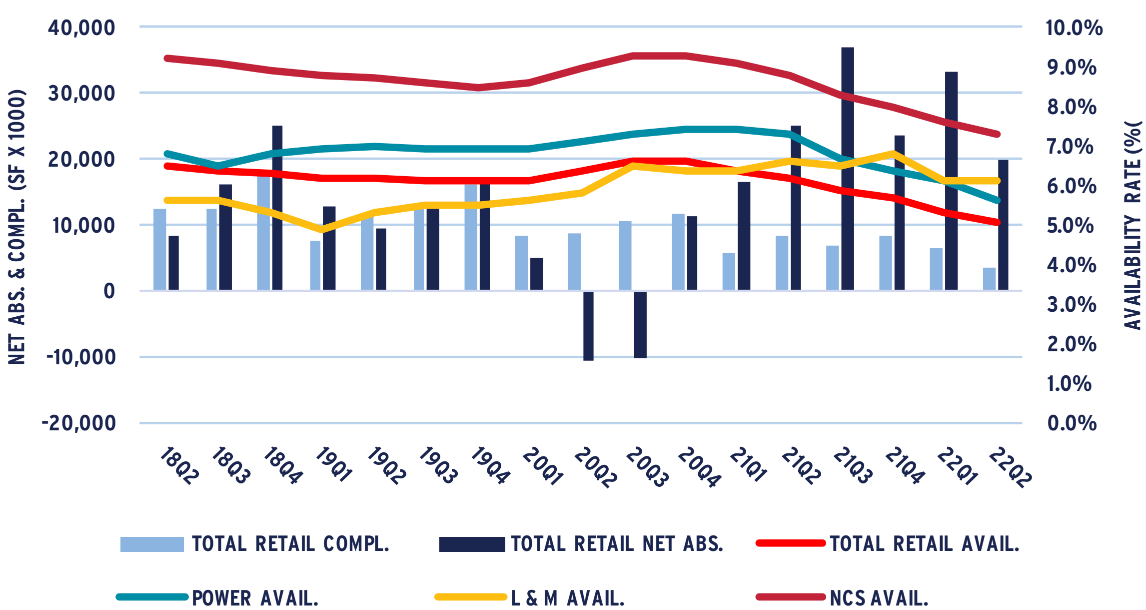
While fundamentals are solid across total retail and the major subtypes, there are some headwinds that should be monitored going forward. During the pandemic, many households had their cash flows boosted by transfer payments and stimulus checks. At this point, that additional spending power has run out. Additionally, higher inflation is also putting pressure on consumers to reduce their spending. Per the Bureau of Labor Statistics, as of June 2022, the Consumer Price Index was up 9.1% YOY, the largest 12-month increase in 40 years. Energy-related categories, like spending on gas, were up 41.6% while grocery spending was up 12.2%. Given the higher cost of goods and services, consumers will have less disposable income available for shopping, driving down retail sales, which could ultimately influence the sector's currently stable conditions. Thus, moving forward, challenges to consumer spending remain a concern for the sector.

QUARTERLY COMPLETIONS



Source: CBRE-EA

RETAIL SECTOR FUNDAMENTALS



Source: CBRE-EA

RETAIL	N&C SHOPPING CENTERS	LIFESTYLE & MALL	POWER CENTER
Availability Rate	7.3%	6.1%	5.6%
12-Month Historical Trend			
Availability Change	↓	↓	↓
Rent	↑	↔	↑
Absorption	↔	↔	↑
Completions	↓	↓	↓
Cap Rates	↔	↑	↓
Transaction Volume	↑	↑	↑

Source: CBRE-EA, RCA and NCREIF