WHERE CAN WE EXPECT COMMERCIAL REAL ESTATE TO GO IN THE NEXT 5 YEARS?

By Rose Morrison, Writer & Managing Editor, Renovated

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Commercial real estate experienced unforeseen setbacks during the coronavirus pandemic in 2020 and 2021. For a while, a stream of variants and uncertainty surrounding the future of office-based work and rents resulted in unfavorable forecasts for retail and corporate real estate markets.

However, there's a glimmer of hope as the United States continues combatting the virus with widespread vaccinations and health safety measures, allowing Americans to return to a pre-pandemic level of normalcy with confidence.

Corporate America is currently opening its doors and dusting off its cubicles. Retail stores have also reopened, once fearful e-commerce would forever transform the brick-and-mortar livelihoods that are the backbone of vibrant communities. The future of multifamily real estate is also looking up.

Although the commercial real estate market is anything but certain, trends seem to be moving upward positively. Here are five possible outcomes to look for in commercial real estate in the next five years.

1. AN UPTICK IN OFFICES LEASES

At the beginning of the pandemic, businesses had to transition to remote work – an experiment that proved surprisingly successful and profitable. However, as CEOs seek a return to the office, they're now grappling with decreasing employee retention as demands for greater flexibility and livable wages increase.

Since spring 2021, all sectors have felt the effects of the Great Resignation. In March 2022, about 44% of the workforce sought new jobs offering higher pay, better benefits, and ongoing remote work.

Yet, companies and employees are compromising on hybrid work, even using remote workdays as a recruitment and retention tool. Additionally, employers are investing in attractive facilities and amenity upgrades to draw employees back to the office.

Employee preferences are undoubtedly changing the workplace – but they haven't shuttered doors indefinitely. According to the National Association of Realtors (NAR), office occupancy increased by 84% in the first quarter of 2022, particularly in major metropolitan areas and technology hubs.

In the Mid Atlantic Real Estate (MARE) Journal's May 2022 edition, Philadelphia, Pennsylvania's commercial business district (CBD) leasing market is also reportedly holding steady, despite occupancies below the pre-pandemic average of 30% – however, signs of activity look promising.

Executive VP of WCRE I CORFAC International, Todd C. Monahan, states that demand for new leasing opportunities in Philadelphia is increasing with over a million square feet of CBD offices in play. As for current tenants that allow their contracts to expire, the city has witnessed several of those offices convert to life science laboratories or find additional solutions and uses for the space.

The future of hybrid working models certainly puts the office sector on shaky ground. If employees spend approximately 3.5 days at the office, projections indicate a potential 9% decrease in office demand.

Nevertheless, while it's still early to tell if the demand for remote work will supersede office culture, commercial building leases will likely continue to rise.

2. RETURN OF RETAIL

Retail stores and restaurants felt some of the largest pangs of pandemic pain during nationwide shutdowns in 2020 and 2021. With more people staying at home and utilizing e-commerce services, several brick-and-mortar locations closed or filed for bankruptcy, while others were able to scale back and reopen.

Originally, global investment banking company UBS forecasted 80,000 shop closures by 2026 – a calculation more likely to fall around 40,000 to 50,000, thanks to inflation and retail sales growth. Nevertheless, forecasts suggest that clothing, accessories, consumer electronics, and furniture chains will experience the most closures.

Traditional shopping malls anchored by department stores are also at higher risk following the pandemic, as more people prefer quick trips for the mere essentials. However, this presents commercial real estate investment opportunities to revitalize grocery-anchored shopping centers that could potentially enhance retail success.

In the past, grocery stores proved themselves capable of withstanding recession – people must eat regardless of economic conditions. Yet, even as e-commerce grocery sales surged by 9.7% from 2019 to 2020, grocery properties also proved to be pandemic-resistant.

Studies indicate that people visit their grocery store about 1.5 times per week, which could increase foot traffic to attached or nearby shops and eateries. Since big-name grocery stores also tend to boast credibility amongst consumers, people may be more inclined to combine their errands and leisure shopping in one convenient location.

3. MULTIFAMILY RECOVERY

Multifamily real estate has made the most headwind in pandemic recovery, although this largely depends on several factors, including city, sub-market, and neighborhoods.

According to Fannie Mae, projections for U.S. multifamily vacancy rates will remain relatively flat at 5% in 2022, with upward trends in 2023 and 2024. This is attributed to greater inventory next year and climbing employment, raising the demand for housing.

The Federal Housing Finance Agency capped 2022's multifamily loan purchases at $78 billion, approximately 11.4% higher than in 2021. Despite positive indications for growth, investors must consider affordability.

Multifamily real estate has already encountered a significant uptick in rents. Across the U.S., rents rose an average of 11.3% in early 2022 due to the supply-demand shortage. However, employment wages will need to keep up with increasing rent costs.

Regardless of current challenges, investors could potentially do very well in 2022's apartment real estate market.

The National Association of Home Builders (NAHB) anticipates a 6.4% boost in multifamily properties throughout the year – even as developers and builders face ongoing building materials and labor shortages.

4. UPGRADED RENTALS

Whether companies choose to bring their employees back full-time, implement a hybrid workweek, or allow them to telecommute indefinitely, remote work is here to stay in some capacity.

As such, the new at-home workforce has transformed multifamily demand. For better workflow, renters are now upgrading their dwellings to two-bedroom apartments to create an office space.

In the National Multifamily Housing Council's (NMHC) 2022 NMHC/Grace Hill Renter Preferences Survey Report, a snapshot suggests that the future is remote, flexible, smart, and connected. Therefore, commercial real estate investors should focus on building and upgrading multifamily properties with the following survey responses in mind:

- About 35% of respondents desired a shared workspace in their multifamily communities.
- Interest in townhomes and single-family home rentals is 23% and 19%, respectively.
- Two-thirds of renters are looking for flexible space in their units and homes.
- About 70% of renters demand smart technology features or wouldn't sign a rental agreement for a unit lacking them.
- None out of 10 renters require strong internet connectivity if they're going to rent a unit.

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Upgraded multifamily properties with renter preference considerations should continue to entice potential tenants. Adding modern design touches, enhancing on-site amenities, and integrating innovative technology can also justify higher rents.

5. BOOST IN PROPTECH

Property technology – simply referred to as proptech – saw tremendous growth in 2021. Throughout 2022, continuous development is favorable for real estate tech investments, particularly in construction, mergers and acquisitions, and the Gen-Z renter experience.

In fact, a Deloitte Center for Financial Services survey reveals that over three-fourths of commercial real estate investors intend to expand partnerships or invest with proptech companies in 2022.

According to Crunchbase, proptech and real estate firms raised $21 billion in 2021 to optimize embedded finance, remodeling software, and project management software. Additionally, Gen-Z renters seek innovation that enables the virtual space to tour units, sign rental contracts, and pay rent.

Commercial stakeholders are especially interested in digital integrative financing, management, and analytics solutions to improve investment participation. This will likely drive proptech backing even more.

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Although uncertainty still surrounds pandemic recovery, the commercial real estate market is trending upwards – with all signs pointing in the right direction.

Consumers and renters have undoubtedly modified behaviors that subsequently altered the commercial landscape. A seemingly surefire way for commercial investors to maximize real estate opportunities is to adapt to people's demands, from upgrading multifamily properties to accounting for the "convenience first" attitude in consumer shopping.

Rose Morrison is a residential and commercial real estate writer and the managing editor of Renovated. To see more of her work visit:: https://renovated.com/

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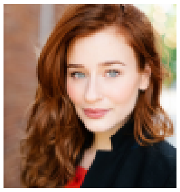

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