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Advance in Office and Industrial Markets Softens in Third Quarter of 2016

December, 2016—WASHINGTON, DC — Members of the Society of Industrial and Office REALTORS® (SIOR) participated in the Commercial Real Estate Index survey, supplying their knowledge of the industrial and office market conditions in the United States for the second quarter of 2016. The responses, given by 210 SIOR members, compiled by SIOR in association with the National Association of REALTORS® (NAR), present an accurate depiction of the current industry for the end of 2016.

Office and industrial markets dropped in the third quarter; with the SIOR Commercial Real Estate Index decreased 4.1 points moving from 123.1 to 119, keeping the CREI over what is considered the balanced market threshold at 100 points. The SIOR Index measures ten variables pertinent to the performance of U.S. industrial and office markets (see methodology).

Leasing: 54 percent of respondents felt that leasing activity in their market is higher than historic levels; 24 percent found leasing in line with averages, while 23 percent found leasing below normal.

Rents: 6 percent of respondents felt that asking rents are below where they were one year ago (4 percent last qtr.); 59 percent feel that asking rents are in line with long-term averages; 34 percent reported rents above historical trend.

Vacancies: 10 percent of respondents thought that vacancy rates are higher than a year ago; 18 percent contend they are the same and 71 percent say they are lower (68 percent last quarter).

Subleasing availability: 9 percent felt that there is ample sublease space available, compared with 4 percent last quarter; 61 percent considered subleasing to have a small influence on the market.

In terms of tenant concessions—23 percent felt that tenants were benefiting from moderate concessions to deep discounts to rents (20 percent last qtr.); 32 percent of respondents found a market in normal negotiating balance; 45 percent thought the market favored the landlord.

Construction activity: 41 percent indicated rising new construction; 18 percent found development close to historical averages; 21 percent of respondents indicated levels lower than normal, and 20 percent mentioned that there is no new commercial construction in their market.

In terms of development acquisitions—it was a buyer's market according to 14 percent of respondents (13 percent last qtr.); 34 percent found it a balanced market, while 52 percent experienced a seller's market (56 percent last quarter).

On the investment side, prices were below replacement costs in 39 percent of the markets, compared with 35 percent last quarter; prices were above costs in 40 percent of the markets.

Local economies—12 percent of respondents feel that their local economy is slowing or contracting, compared with the 11 percent from last quarter. Meanwhile, 52 percent considered that the local economy is strong and improving (55 percent last quarter).

National economic impact—15 percent of respondents felt that the national economy is having a negative impact on their local market (19 percent last qtr.); 37 percent felt that the national economy was having a positive impact on their markets.

When asked about the outlook for the next three months—8 percent indicated that business was going to be down from current levels, 36 percent of respondents felt the market will be maintaining the current level during the next three months, and 56 percent pointed to expected improvement in the market.

Methodology

The SIOR Commercial Real Estate Index is constructed as a "diffusion index," a very common and familiar indexing technique for economic measures. Other examples of diffusion indexes include the Index of Leading Economic Indicators, the Consumer Confidence Index, and the Institute of Supply Management's Purchasing Managers' Index. In the SIOR Commercial Real Estate Index, a value of 100 represents a well-balanced market for industrial and office property. Values significantly lower than 100 indicate weak market conditions; values significantly higher than 100 indicate strong market conditions. The theoretical limits of this Index are a low of zero, and a high of 200, though it is unlikely that such limits would be approached as long as the property markets are operating efficiently.

The Index is based on a survey questionnaire with ten topics. The topics covered are (1) recent leasing activity; (2) trends in asking rents; (3) trends in vacancy rates; (4) subleasing conditions; (5) levels of concession packages in leases; (6) development activity; (7) site acquisition activity; (8) investment pricing levels; (9) the impact of the local economy on the property market; and, (10) the effect of the national economy on the property market. Survey respondents are given five choices. For each topic, five choices are provided, corresponding to conditions that are very weak, moderately weak, well-balanced, moderately strong, or very strong.

For each question, answers are tallied and the percentage of responses for each of the five choices is calculated. If survey panelists indicate "very weak" conditions (the "a" choices in the questionnaire), the answer is assigned 0 (zero) points; "moderately weak" ("b" answers) earn 5 points; an indication of "market balance" ("c") receives 10 points; "moderately strong" indications ("d") score 15 points; and "very strong" ("e") responses receive a maximum 20 points. Thus a score of 10 for a given question can be earned if responses are evenly distributed across all five choices, if all responses were "c", or if the answers form a "bell-shaped curve" centered around the "c" choice. The total index value is derived by summing the scores for all ten questions. Index values for each of the two property types are similarly calculated.

The survey was developed by Hugh F. Kelly, CRE, clinical professor at New York University, who worked with SIOR on research projects since 1989.

Headquartered in Washington, D.C., the Society of Industrial and Office Realtors® (www.sior.com) is a global professional organization that certifies commercial real estate service providers with the exclusive SIOR designation. Individuals who earn their SIOR adhere to the highest levels of accountability and ethical standards. Only the industry's top professionals qualify for the SIOR. Today, there are 3,100 SIOR members in 650 markets in 34 countries.

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