WHAT TO EXPECT IN 20

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BY GEOFFREY KASSELMAN, SIOR

Regardless of where you fit into the commercial real estate ecosystem, or what asset class(es) you work with, one thing is for sure: 2020 will be a year to remember!

We are in the midst of extended—if not unprecedented—cycle run-time, yet with potentially more room to run. The cost of, and access to, quality low-cost capital remains the rule rather than the exception, as does the ability to exit to an active secondary market. Corporate profits and consumer confidence remain relatively strong, if not solid enough to continue to drive demand. Additionally, domestic economic indicators like unemployment rate, inflation, interest rates, and GDP are all aligned enough to support continued real estate activity in 2020.

Layered on top of such dynamics are relentless innovation and its impact on key variables like supply chain, retail, food and beverage, automation, IoT, and energy, among other notable pivot points.

With these variables and key drivers in mind, here are six focal points to track in 2020:

Economics: As large employers hedge against late-cycle concerns and automation begins to really matter, watch for unemployment to bottom out and start to creep back up; it should end the year at near-historic lows, yet the trend bears tracking. Expect interest rates to stay within 250 basis points of where they are, which may be a double-edged sword—low capital costs are important for stimulating continued market activity, but in the event the economy cools quickly or unexpectedly, there is no downward mobility as economic stimulus. And because consumer confidence is 70% of GDP, 2020 will largely hinge on whether this spigot continues to flow, or not. It's likely that consumer confidence erodes enough by the end of 2020 to be adversely impactful in concert with other key variables.

Global Dynamics: Import and export activity tends to scale with our largest trading partners: China and the European Union (EU). China is likely to have an inopportune stretch, driven by a bubble economy that was already showing signs of bursting, extended-term tariffs, and now the Novel Coronavirus has all but shut China down (and rightfully so). The EU just lost the United Kingdom (UK) to Brexit and most observers expect both the UK and the EU to have an off-year—or two. Such dynamics do not bode well for any kind of economic record-setting in 2020. Additionally, there is a bona fide geo-political movement across the globe towards conservative nationalism which, in turn, is reshaping alliances and trading patterns and cannot be fully discounted in its impact on the world economy. Consequently, the trend towards more nimble and diverse supply chain dynamics will continue with additional re-shoring activity this year.

Real Estate Deal Activity: Since most real estate transactions that will occur the first half of this year were conceived and funded in 2019, these first two quarters in particular should be strong, perhaps enough so to carry the 2020 annual metrics to yet another relatively well-performing year. That said, as the U.S. presidential election takes center stage, and the full effect of some of the previous outlined dynamics are realized, expect transaction activity in the second half of 2020 to be slowed or delayed, with fewer new project starts carrying into 2021. As such activity wanes and more under construction inventory (speculative) space comes in line in 2020, supply will catch up to demand, resulting in flattening rents. Also watch for increased corporate surplus and sale-leaseback activity, the continued decline of the office square foot/person metric, and shorter-term space commitments, even at a cost premium. Likewise, 2020 will see the return of large-scale suburban office leases as cost-conscious employers seek lower operating costs while also tweaking their recruiting and retention strategies with on-site amenities and ultra-flexibility. To that point, don't be surprised to see a significant corporate user strike up a multi-market deal with WeWork where the corporate user gains functional, furnished flexibility with a vibe at a relative value, while WeWork and its landlords gain a sigh of relief and much-needed stability.

Technology: Scaled disruption will make notable strides in 2020, through a variety of internal and client-facing proptech, constructiontech, and energytech products and services. Watch for aggressive funding, surprising new partnerships, more Internet-of-Things (IoT), and a move towards further automation. Blockchain-driven activity for smart contracts, data monetization, property tokenization and transparent supply chain will gain speed in 2020, while AI will continue to work in the background, 24/7/365, while we eat, play, work, and sleep. Accordingly, expect significant AI news for the real estate sector this year. Commercial-grade electric vehicles (EVs) will hit the market in 2020 while limited-scale drone deliveries and air taxi service will commence by the end of the year as well. Both additive manufacturing (3D printing) and modular construction may also make significant strides in 2020 as additional commercial-grade capacity comes online and mainstream use-cases become more widely known and understood.

Mergers & Acquisitions (M&A): As real estate operators move to improve shareholder value, achieve greater scale, improve efficiencies, extend geographic reach, and enhance branding—while also taking capacity out of the market—there is an inevitability to some significant M&A activity in 2020. Expect to see at least two larger commercial real estate firms come together this year while firms like Prologis and Blackstone will continue to pick up other operators where and when it makes sense (note: Simon Property has just announced a $3.6B acquisition of Taubman in the retail sector). Many sellers know that peak valuations are here and the urgency to transact may be elevated as a result.

Intangibles: The science and data are overwhelming, and the debate is over: climate change is real and teetering on being irreversible. Nothing could be as disruptive or impactful on property dynamics everywhere as chaos caused by climate change. Reducing carbon emissions is therefore everyone's priority, so a move to alternative energy sources is already well-underway. The holdback seems to be in commercially scalable battery storage. In this regard, with over $250 million of invested capital, expect a major battery storage breakthrough in 2020. In certain geographies, pivotal market movers such as real estate tax changes, legalized cannabis, and transit-oriented development (TOD) could be real game-changers. And we can never lose sight of cybersecurity. There will be at least a few bombshell breaches again in 2020.

In summary, 2020 promises to be a year of success, concern, exponential progress, and change—which is the new normal. Here's to another great year wherever you are, but do not take your eye off the ball even for one second, or risk missing out on something truly notable.

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