August 15, 2016

Are Foreign Investors Moving to the Sidelines?

Foreign investment in U.S. commercial real estate properties hit a record high of $92.4 billion last year, and many predicted that momentum to continue in 2016 as foreign investors looked for a safe haven for their capital. Instead, foreign investment has taken a sharp drop. "The expectation going into the year was one that the trend and flow of capital would be there, and potentially increase in 2016, despite the dramatic jump in foreign capital that was invested in the U.S. last year," says Riaz Cassum, a senior managing director at HFF, a provider of capital markets transaction services, in Boston. In fact, a 2016 report from the Association of Foreign Investors in Real Estate (AFIRE) found that nearly one third of its members planned to maintain or increase their investment in U.S. commercial properties this year. Yet during the first half of the year, cross-border transactions totaled $23.1 billion—down 47 percent compared to the $43.3 billion in closed transactions that occurred in the first half of 2015, according to New York City-based research firm Real Capital Analytics (RCA). There are a multitude of factors contributing to the slowdown, ranging from general market volatility to specific issues that are impeding capital flows from some countries or regions specifically. "It is a little difficult to put your finger on one particular thing, because there is not one particular thing causing this slowdown. It is a combination of events," says Cassum. Notably, new government restrictions in China have made it more difficult for both institutions and private investors to get capital out of that country. Chinese investment won't be shut off completely, but the restrictions have definitely slowed momentum for what had been the single fastest growing source of foreign capital into the U.S., notes Cassum. Slumping oil prices continue to impact Middle Eastern sovereign funds, and the recession in Brazil has also diminished investment capital coming out of that country. Canadians continue to be active, but are more cautious due to the perception that the real estate cycle is moving into a later stage. Foreign investment activity is clearly down compared to last year, but it may not be as big of a drop as the numbers suggest, says Zeb Bradford, chief investment officer at Seattle-based Metzler Real Estate, an investment advisor that specializes in representing foreign investors in the U.S. real estate market. Metzler Real Estate is the North American affiliate of B. Metzler seel. Sohn & Co. KGaA, the oldest private bank in Germany. The figures were somewhat inflated last year due to some large portfolio sales. That being said, there is a bit of a pause in the market that is due in part to pricing. Prices that had been on the rise for the past five years may have hit a peak around mid-2015, says Bradford. "I think pricing has taken a bit of a pause for most assets, and because of that, I think sellers also have taken a pause to understand where pricing is and either reset their expectations or their desire to hold for a bit longer," he notes. For example, Metzler assisted its client Union Investment Real Estate GmbH with the April acquisition of Boston's 101 Seaport Boulevard. Union, which is one of Germany's largest asset managers, acquired the 17-story office tower for $452 million or a record $1,027 per sq. ft. Despite the slow start, foreign transactions could accelerate in the second half of the year. The Brexit vote and continued uncertainty in Europe are expected to funnel more investment capital towards the United States. Investors are concerned about the short-term outlook for real estate in European markets, and they are also looking for alternatives given the fact that many countries now have flat or negative bank rates across Europe. China is in the midst of an economic slowdown and Japan doesn't have strong economic growth. So even though the U.S. may be moving towards the end of a cycle, economic growth is still positive and there are still good fundamentals in real estate, says Bradford. Historically, about 10 percent of the capital coming into the market has been from foreign sources, and foreign capital represents an even larger component of the market for class-A properties in major metros at 20 to 25 percent, says Bradford. "Foreign capital has always been a very important component of the U.S. real estate capital markets," he says. "But I think it is becoming a larger and larger player in the market, and I think that will continue." **(National Real Estate Investor/Beth Mattson Teig)**

...

Forget the Canal—Inland Ports Show Impressive Growth

Supply chain experts agree that the massive, long-awaited Panama Canal expansion opening in late June, while interesting, is not likely to impact industrial activity in the short-term. However, the often-forgotten U.S. inland ports have been quietly tearing up records for expansion and growing at nearly twice the national rate for industrial properties. Inland ports have been the fastest growing markets for industrial demand, says Dwight Hotchkiss, national director of industrial for real estate services firm Colliers. About half of the 77 million sq. ft. of industrial space absorbed in the second quarter was located in the inland port markets, and the average asking rent for distribution facilities in these markets is at an all-time high of $5.66 per sq. ft., he says. "The inland ports are not as sexy as the seaports, and don't get the same attention, but they're also growing at a fast rate. Retailers need the inland ports to help satisfy the massive ecommerce demand today," Hotchkiss notes. An inland port is comprised of two main criteria, according to a recent CBRE study: Direct connection to a major seaport via Class I rail, and major transportation infrastructure, in the form of rail (usually), interstate highway or inland waterway. Many markets considered inland ports also have access to large population centers within 300 miles, a strong industrial inventory, large labor pools and economic development policies such as Free Trade Zones and tax incentives. The top five inland ports in the country in terms of industrial size include Dallas/Ft. Worth, Atlanta, Houston and the Inland Empire, according to David Egan, Americas head of industrial research for CBRE, but Chicago dwarfs them all at more than 1.2 billion sq. ft. The Chicago area is the largest point of origin for rail-to-truck intermodal shipments in the U.S., and almost half of all shipments flow through the market. That amount of activity doesn't get the same attention as East or West Coast ports, Egan notes, but an inland port like Chicago is significantly important to the nation's supply chain. "Seaports are a distinct place, whereas an inland port like Chicago is more of an idea, a collection of places," he says. "But I think how we think of goods moving through the country has changed, from paying attention to the point of entry to now looking at the supply chain as a whole. Everything is competing with e-commerce, down to the kind of bread you buy on the shelf of the Whole Foods store. The way inventory is carried to all these large population centers is typically through the middle of the country." The Chicago port boasts a total of 18 intermodal, train-to-truck terminals, moving enough freight to rank it the second largest port behind Los Angeles/Long Beach. Much of the freight flows through the country's largest intermodal terminal, the CenterPoint Intermodal Center, located on 6,500 acres at the intersection of interstates 80 and 55 in Elwood and Joliet, Ill. The property includes 15 million sq. ft. of distribution space, and has absorbed one million sq. ft. on average annually since it opened in 2002. The market is also supported by five other interstate highways, six Class I railroads, O'Hare International Airport and multiple water terminals serving the Great Lakes and Illinois waterways. Just in Chicago, inbound truck and rail shipments are projected to grow by more than 50 percent in the next 24 years, Egan says, and outbound rail shipments are expected to increase by almost 150 percent. The top 12 inland ports are already growing fast, expanding their base of industrial properties by 2.7 percent in the first quarter and outpacing the national average growth rate of 1.6 percent. The Inland Empire has grown by 4.3 percent since last year, and Atlanta and Dallas/Ft. Worth increased in size by 3.6 percent. "It's absolutely astonishing, the amount of space being leased in the inland port markets," Egan notes. "We would expect by now, seven years after the recession, to start seeing some drop-off, but we don't see any reason that growth with slow down. With the rapid growth of e-commerce, I don't see that we're even near the finish line. I'd say we're just a couple steps from the starting line." **(National Real Estate Investor/Robert Carr)**

…

California's Tax, Regulatory Policies Causing Businesses to Flee (and it's about to get worse)

California's tax and regulatory policies have made the cost of doing business more expensive than other states and prompted about 10,000 companies over the last eight years to leave the state or shift or curtail operations to reduce costs, according to a report from Spectrum Location Solutions. The Irvine-based company, which helps companies find places to locate their operations, issued a report titled " California Business Departures: An Eight-Year Review 2008-2015," which provides details about such events by company name, ranks the popularity of destination states and cities, and outlines the difficulties of doing business in the Golden State. The study found at least 1,687 California disinvestment events occurred from 2008 through 2015, but the report said that number is understated since it reflects only those that became public knowledge, such as through company announcements or regulatory reports. Spectrum President Joseph Vranich, who authored the study, said at least five events fail to become public knowledge for every one that does. "Thus it is reasonable to conclude that a minimum of 10,000 California divestment events have occurred during that period," Vranich said. California disinvestment events are defined as companies that:

1.Relocate entire offices and facilities to an out-of-state location

2.Remain in the state but expand elsewhere with facilities that heretofore were built in California

3.Close completely with production moving to competitors in dispersed locations

4.Shift work to a foreign nation through offshoring, outsourcing or relocation

5.Cancel a project after it has been announced, or

6.Perform a "U-Turn" – which means considering a California location but rejecting it after studies favor a location outside of the state's borders.

The report said the top 15 California counties with the most events were:

1. Los Angeles
2. Orange
3. Santa Clara
4. San Francisco
5. San Diego
6. Alameda
7. San Mateo
8. Ventura
9. (tie) Sacramento
9. (tie) San Bernardino
11. Riverside
12. (tie) Contra Costa
12. (tie) Santa Barbara
14. San Joaquin
15. Stanislaus.

Vranich said Los Angeles has the worst ranking in part because it has so many businesses, but also because doing business is costlier in Los Angeles than in just about any other California location outside of the San Francisco Bay Area. The top 10 states that benefited from the California disinvestments were Texas, followed by Nevada, Arizona, Colorado, Washington, Oregon, North Carolina, Georgia, Florida, and Utah, which tied with Virginia. Texas was the top destination for California companies each year during the eight-year study period. The out-of-state metropolitan areas that benefited included:

1. Austin-Round Rock-San Marcos
2. Dallas-Fort Worth-Arlington
3. Phoenix-Mesa-Scottsdale
4. Reno-Sparks
5. Las Vegas-Paradise
6. (tie) Denver-Aurora-Lakewood
6. (tie) Portland-Vancouver-Hillsboro

8. Seattle-Tacoma-Bellevue

9. Atlanta-Sandy Springs-Marietta

10. Salt Lake City-Ogden-Clearfield.

The report notes that California does offer a variety of incentive programs to lure businesses, many of which are administered through the Governor's Office of Business and Economic Development. Some of those incentives include tax incentives for aerospace companies, California Film Commission incentives, employment training panel incentives, and California Energy Commission incentives. But the study also notes California' business environment could worsen as the state is considering imposing a broad set of taxes on businesses in 2016 and 2017, including higher fuel and motor vehicle taxes, and tax increases on business properties. "The proposals, if enacted, will worsen California's business environment, so much so that a result may be an increasing number of businesses leaving California for greener domestic or international pastures," Vranich said. **(LA Biz)**

...

	CURRENT	**1 MONTH PRIOR**	**1 YEAR PRIOR**
FED TARGET RATE	.50	.50	.25
3 MONTH LIBOR	.82	.67	.31
PRIME RATE	3.50	3.50	3.25
10 YEAR TREASURY	1.51	1.47	2.17
30 YEAR TREASURY	2.23	2.17	2.84