



# VIEWPOINT 2022

**COMMERCIAL REAL ESTATE  
TRENDS REPORT**

An Integra Realty Resources Publication





## ABOUT VIEWPOINT

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# COMPREHENSIVE COMMERCIAL REAL ESTATE MARKET RESEARCH, VALUATION AND ADVISORY SERVICES

## ABOUT IRR

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Every IRR office is supervised by one of our more than 165 MAI-designated professionals, industry leaders who have over 25 years, on average, of experience in their local markets. Having more MAI-designated experts than any other firm is just one testament to the high levels of training and experience which we put at our clients' disposal: as of January 2022, IRR's senior management team also includes: 16 FRICS; 9 MRICS; 16 CREs; 25 SRAs; 18 CCIMs; 6 ASAs.

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# CEO'S LETTER

*Anthony M. Graziano, MAI, CRE*



*Dear Viewpoint Reader:*

Thank you for your interest in Integra's 29th year publishing *Viewpoint*. Whether you're a first-time reader, or a returning student of real estate history, we thank you for joining us for another edition. We hope this year's edition embodies the spirit of *Viewpoint*; to capture the moment and discuss the inflection points in the market while providing relevant market data that has contextual relevance in comparing U.S. real estate markets.

I wrote with enthusiasm in the fourth quarter of 2020, recognizing vaccines might soon arrive, and acknowledging the efforts of Americans to rally following our period of isolation. I challenged the market to "catch the sword" that was falling towards us, knowing we could be scathed but hoping to stave off worldwide economic catastrophe...and rally we did. By Q1 2021, all sectors of the U.S. economy went into overdrive; workers and employers adjusted to new workplace challenges; our healthcare system delivered immense benefits; and consumer spending (often labelled "revenge spending") rocketed back.

This also translated into spiking demand for goods and services. The return to school, increased leisure travel, and a return to near normalcy had many beginning to discuss "post-pandemic" effects. It is significant that we declare we are not post-pandemic just yet. This is the crossroads of 2022 that we discuss at more length in this edition of *Viewpoint*.

Theories of inflation abound. The concern over inflationary effects on housing, wages, food, and energy could all translate into a necessary increase in wages. Nearly all businesses will feel the effects of these cost increases to deliver goods and services profitably. Inflation will also change the risk premiums for real estate investment which could force many to mis-price risk at the crossroads.

There is no shortage of risk factors. The Omicron variant has already supplanted Delta as the dominant mutation of COVID-19, and vaccine uptake appears to have plateaued in the U.S. at roughly 70%. Our nation is in a state of internal conflict over social equity, future climate

commitments, housing affordability, and the potential for winter pandemic outbreaks. The "Great Resignation" is upon us with a record 39 million workers who quit their jobs during the first three quarters of 2021. The coming year will most certainly reveal the market value of labor.

The fundamentals of real estate are well established. The market's behavior (residential and commercial) in 2021 was driven by plentiful capital availability. It's probably time to tap the brakes, or at least take our foot off the accelerator. How reliable is it to record an asset trade at a 3% capitalization rate when the buyer expects to increase rents 20% in the coming 6 months? Did they really buy on a 3 cap? How aggressive the market is with growth assumptions (and how right or wrong they turn out to be) will determine the fate of recent trades. What we need in 2022 is discipline, market research, and better perspective around the conditions of 2021 so they are not misinterpreted as long-term circumstance.

The only constant is change, and the world is changing quickly. There will be more focus on ESG investment in capital allocations and a new process for measuring the capital landscape. There will be transformative infrastructure investments that will change local markets for better or for worse. And if 2021 taught us anything, there will be continued major shifts in the employment base. In 2022, these employment shifts will be largely driven by the ability to recruit and retain talent. Everything is going to continue to get more expensive in 2022, including debt.

And yet, we would do well to be thankful. We head into these conditions with strong balance sheets and good prospects. We survived and thrived under a radical worldwide pandemic, that for all its future uncertainty, is almost certainly going to improve as natural and booster immunity expands worldwide.

Welcome to the crossroads. Our challenge for 2022 is to forge ahead confidently...but not recklessly.



# ECONOMIC TRENDS

*The perilous, twisting road travelled by Americans in the past two years brings us to a critical crossroads in 2022. That crossroads involves a convergence of complex economic and social issues that include rising inflation, undersupply of housing and disruption in the workplace – all with COVID-19 continuing to overshadow the marketplace.*

*Despite the “pandemic fatigue” that may be creeping into the market, now is not the time for indifference or disengagement. At the crossroads, indifference only puts the choice into the hands of others. Integra’s national survey amply shows a wide range of real estate choices that are sensitive to pricing parameters, appetite for risk/return, and geographic preferences.*

## COVID-19



## Effects of the virus continue to impact behavior and the global economy

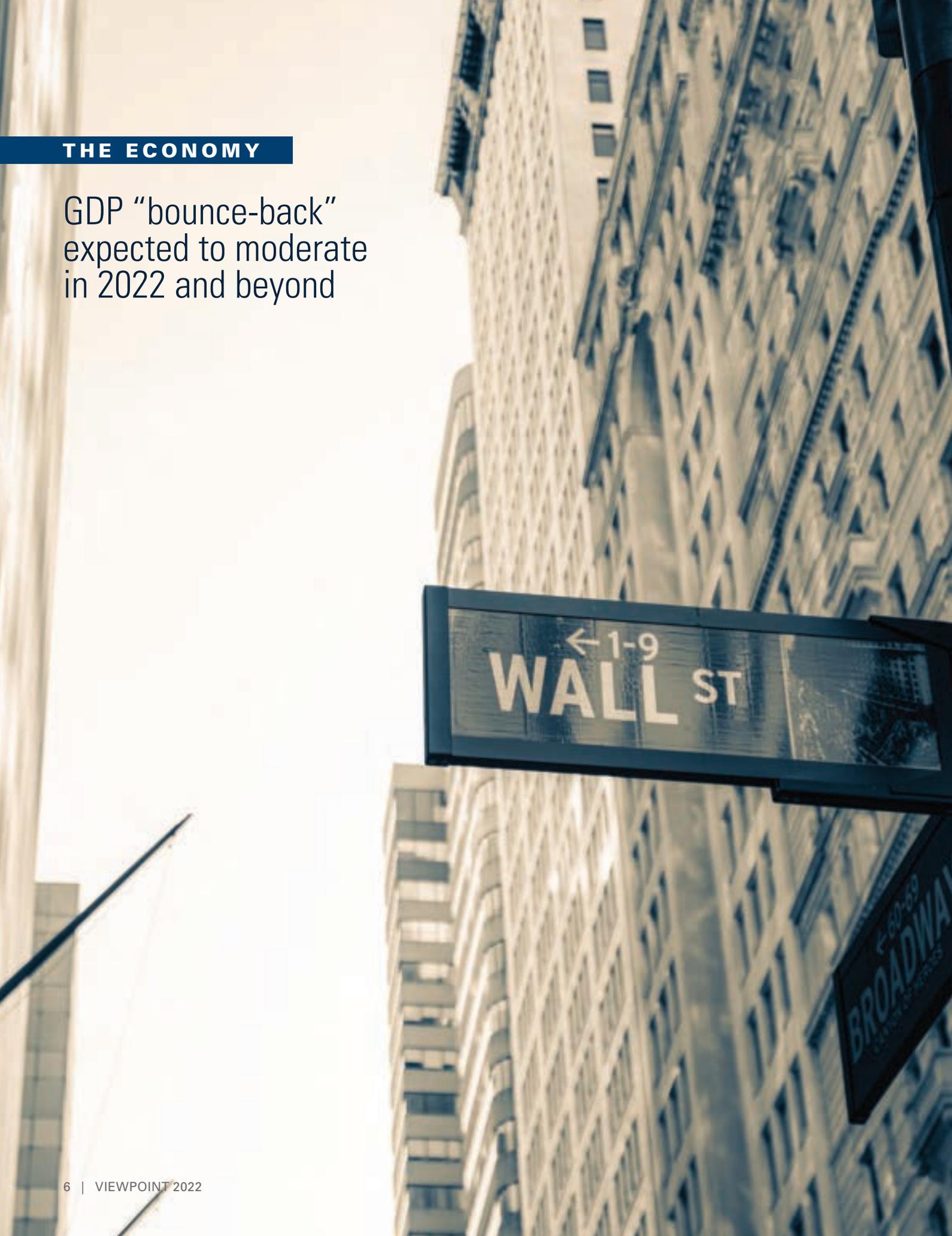
In the first quarter of 2022, we will mark the second anniversary of the arrival of COVID-19 into the United States. Despite the historically swift development and deployment of powerful vaccines, the Coronavirus has not been vanquished and is still the single most significant economic problem facing the nation. As of this writing, there have been more than 800,000 deaths from the virus, and the 7-day moving average of newly reported deaths remains above 1,200 per day in late December. Without some dramatic, and as yet unforeseen turnaround, the year 2022 will see the American death toll climb above 1 million. Surges in the virus trigger behavioral adjustments in the workforce, often puzzling regulatory responses at federal, state, and local levels, and uncertainty amongst business leaders seeking to plan for a volatile future.

The year 2022 will see the American death toll climb above one million.

The global nature of this disease is a critical factor in both its intractability and its economic impact. Many nations that are key trading partners with the U.S. have infection rates that are far above the United States. Such nations include major European economies – Germany, the Netherlands, and the U.K. Bottlenecks in supply chains are affecting global vaccine distribution, in addition to the well-documented impacts of supply chain disruption on inflation in the U.S. and abroad (e.g., port restrictions in China’s Pearl River delta, congestion at the L.A./Long Beach port, and rising commodity prices in food and metals related to production shortages).

The ripple effects of COVID-19 continue to be pervasive and significant. And, sadly, that will be the case for some time to come.

Crystal balls remain cloudy on the macro-economy, but the sun appears to be breaking through.

A low-angle, upward-looking photograph of a tall, classical-style skyscraper with many windows. In the foreground, a black street sign is visible, featuring a white arrow pointing left, the number '1-9', and the text 'WALL ST'. Another sign for 'BROADWAY' is partially visible below it. The sky is a pale, clear blue.

## THE ECONOMY

GDP “bounce-back”  
expected to moderate  
in 2022 and beyond

The refrain “when will we get back to normal?” received a partial answer in the third quarter of 2021. The advance report on Gross Domestic Product (GDP) showed that the output of goods and services in the United States grew 2.0 to 2.3%. That was a mere fraction of the bounce-back third quarter 2020 figure of 33.8%. It also was a notable slowdown from the intervening three quarters, which had growth rates of 4.5%, 6.3%, and 6.7%, respectively. Nevertheless, 2% growth was common pre-pandemic and represents the consensus forecast for the balance of the 2020s.

What has been going on, and what does it portend for 2022 and beyond? Any risk of a double-dip recession was forestalled when the \$1.9 trillion American Rescue Plan (ARP) squeaked through a partisan Congress in March by votes of 219-212 in the House and 50-49 in the Senate. Key to the effectiveness was its speed in execution, its specific targets in mitigating the economic effects of the COVID-19 disruption, and its breadth in providing income support across the American population. The major elements of ARP are:

- \$656 billion in Direct Financial Assistance, including direct stimulus checks, expanded unemployment benefits, and tax credits such as the Child Care and Earned Income provisions.

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- \$362 billion in assistance to state and local governments, which helped reduce the negative ripple effects of layoffs among the over 19 million workers on state and local payrolls.

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- \$212 billion in direct education and related assistance aimed at providing the physical and technological investments needed in K-12 classrooms.

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- \$86 billion for community healthcare support aimed at improving rural services, expanding COVID-19 testing, and “aftereffect” mitigation that include mental health issues and suicide prevention.

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**Two percent growth was common pre-pandemic and represents the consensus forecast for the balance of the 2020s.**

These major components of ARP are in great measure responsible for the strength of the economic performance registered in the first half of 2021. They also stand as stark reminders of how vulnerable the U.S. economy was early in the year.

In contrast, there is good economic momentum heading into 2022. Although the nation is not fully back in employment, GDP has exceeded expectations in returning to its pre-pandemic level. There has been encouraging balance in growth, with gains in personal consumption expenditures and domestic private investment both clocking in at about 7%. Government outlays have appeared fairly flat – despite the fiscal stimulus – because of the peculiarities of budget accounting. And our trade balance deteriorated in a year of massive importing.

All told, most sectors of the economy should experience further expansion in the coming year. The key points of friction for most households now seem to be rising consumer price inflation and a frustration with the availability of desired goods. This is a good example of how economic statistics often do not match with what individuals are experiencing – a real and important dissociation.

One effect of that is the tepid reading of consumer confidence from the Conference Board and the University of Michigan surveys, especially regarding expectations. The Purchasing Managers Index of business confidence, meanwhile, anticipates an expanding economy in the year ahead, with about equal optimism amongst goods-producers and services-producers.

As usual, crystal balls remain cloudy on the macro-economy. But the sun appears to be breaking through the clouds.

**Any risk of a double-dip recession was forestalled when Congress passed the \$1.9 trillion American Rescue Plan (ARP).**

## EMPLOYMENT

# Disruption caused by COVID-19 is transforming how and where people work



Right off the bat, one thing that economists have gotten right in their prognostications about the “post-pandemic market” is that the jobs numbers would not recover as quickly as the GDP figures. Projections that it might take until 2024, or even mid-decade, for employment to regain its pre-COVID peak now seem unduly pessimistic. As of November 2021, the U.S. is still 4.2 million jobs shy of where we were before the pandemic. And, even with millions of jobs added since the second quarter 2020 trough, we are roughly 8.5 million jobs below where we were pointed as a trajectory if the coronavirus disruption had not swept in.

But it is not mere numbers that describe the employment crossroad we stand at as 2022 begins. It is more and more apparent that we are at a moment of qualitative change in the world of work. Both blue collar

and white collar jobs were so profoundly disrupted by COVID-19 that it seems inevitable the future will hold substantive change in the way work is performed. This means that real estate, where the jobs are done, will be changing substantively as well.

Much attention has been paid to the question of remote vs. back-to-the office trends. All indications point to a “both/and” rather than an “either/or” resolution. Moreover, the solutions of 2022 are highly likely to morph in 2023 and beyond. Two key factors still evolving are the presumed shift from pandemic to “endemic” COVID-19, and the impacts of competition on businesses weighting in-person work over Zoom work, or vice versa.

For workers with options, we should not underestimate the degree to which anxiety over health risk will shape the pace of office utilization, as well as the way that

businesses and real estate property managers will need to adapt to office workers' expectations. Let's be clear about the radical change that COVID-19 has brought. It is the workers who are in the driver's seat, not employers and not governments. Most office workers are both pragmatic and fairly evidence-based. If vaccinations continue to make inroads on illness, anxiety will abate and the "new normal" will emerge more quickly. If, on the other hand, we find COVID-19 deaths increasing from today's 807,000 to 1 million or more during 2022, expect white-collar workers to be slow to return to their offices.

The Bureau of Labor Statistics JOLTS (Job Openings and Labor Turnover) report released in November starkly illustrates this point. The report shows 10.4 million job openings overall, of which 1.8 million are in professional and business services, and another 1 million in predominantly office-using fields like finance, information, and entertainment. So far, so good in terms of future employment growth. However, some 4.4 million Americans voluntarily quit their jobs, and of these, more than 1 million were in office-dominant job sectors. Workers are being picky, and fully understand that a 4.2 percent unemployment rate enables them to be more selective in their job searches.

**The U.S. is roughly 8.5 million jobs below where we were pointed as a trajectory prior to the pandemic.**

## The Great Resignation: Some 4.4 million Americans have voluntarily quit their jobs.

It is not just a white-collar phenomenon. About 3.2 million private sector job openings exist in manufacturing, trade and transportation, hotels and restaurants, and personal services. Voluntary separations (quits) totaled 2.4 million in the JOLTS report, meaning that the blue-collar jobs in those sectors will show net improvement only very slowly. Furthermore, the traumatic disruption of COVID-19 in hospitals and schools will make hiring in healthcare and education difficult in the foreseeable future.

All this paints a picture of slow employment growth, even in an economy on the mend. More importantly, there are qualitative changes afoot which appear to be altering the character of work for many. The architectural and design firm, Gensler, cites worker expectations for jobsite autonomy, privacy, flexibility, and wellness support. The Harvard Business Review (HBR) reports a widening gap between the job environment that employees want and the ones their employers offer. HBR surveying identifies four key foundations for blue collar and white collar employee recruitment and retention alike: value, purpose, certainty, and belonging. During this period of "The Great Resignation" these qualitative factors will define the job numbers.

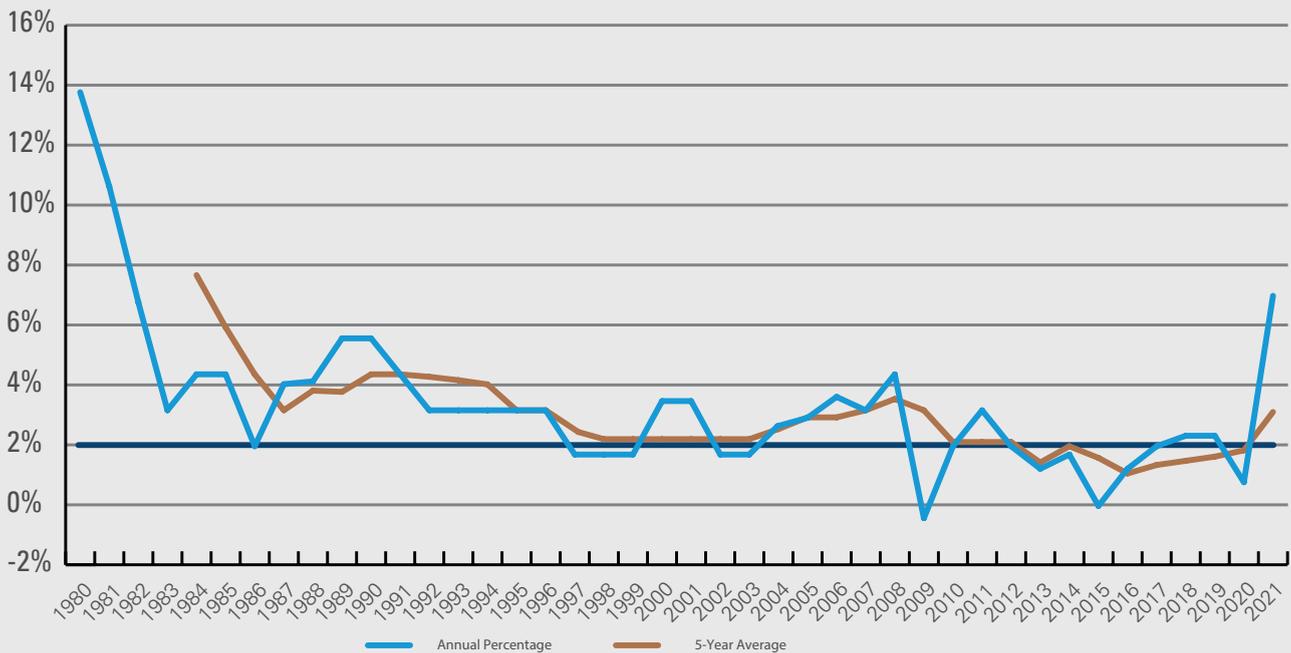




## INFLATION

Although not a root economic problem, rising cost pressures pose potential risks

CONSUMER PRICE INFLATION: 1980 - 2021



Economists John Maynard Keynes and Friedrich Hayek are often reflexively set in opposition in our ideologically purist politics. But they were united in the knowledge of the corrosive effects of runaway inflation. Keynes accurately predicted the inflationary pressures triggered by the 1919 Treaty of Versailles, while Hayek was earning his doctorate in Vienna during the midst of that intense upward price spiral.

Neither economist would ignore our present run of rising prices, but they likely would have a common voice in putting our current situation into perspective. Both great thinkers would see that today's inflation is a mere epiphenomenon, not a root economic problem. Insightful thinkers keep our expectations in bounds during times of fear and times of euphoria.

Normally, we think of two fundamental inflationary tendencies: cost-push inflation and demand-pull inflation. In America, our most severe experience of inflation in the past century has been the cost-push inflation of the OPEC era where rising energy prices led to a systemic price-wage spiral. Demand-pull inflation, most famously summarized by Milton Friedman's aphorism about "too much money chasing too few goods", has lived on as a catch-phrase but has rarely been an accurate description of economic conditions. (The exceptions being periods when foreign policy exigencies flooded the domestic economy with cash.)

Demand-pull inflation, to be frank, is visible in the intervention programs enacted in 2020 and 2021 to keep incomes on-stream even as employment struggled to rebound. The support of consumer spending was not a "bug" but a "feature" of the \$1.9 trillion American Rescue Plan Act, flowing money quickly and broadly across the population in a severely dislocated market.

However, this stimulus fell directly over the income-inequality divide that separates Americans as systemically as the Continental Divide. Economically, the lowest income cohorts have a substantially higher "marginal propensity to consume", while wealthier households have a greater "marginal propensity to save." American households do, as a group, have much more money at their disposal than the employment numbers would suggest. Still, the demand-pull effect is just a fraction of the 6.8% CPI annualized increase, as cost-push inflation generates the rest. Most of the published commentary has done little, if anything, to measure and unpack the relative

power of these two root causes. And it is rare to find anyone acknowledging the global extent of inflation in nations far from U.S. domestic stimulus spending.

Where we are finding inflation is in asset prices: both in the stock market and in the housing markets, where the marginal propensity to save has greater impact. The debate about inflation will not go away in 2022, but inflation hawks will almost certainly fail to distinguish between directing spending toward consumers and toward investors. While neither Keynes nor Hayek would see this as a moment to panic, both would know risk when they see it. Both the housing market and the stock market are now priced in such a way that risk of a correction is inadequately reflected. When that risk is effectuated, there will assuredly be pain.



Stimulus fell directly over the income-inequality divide that separates Americans as systemically as the Continental Divide.

## HOUSING

# Price increases, limited supply create headwinds for homebuyers



During second quarter 2021, the median price of a home jumped 20% year-over-year. This is a dramatic example of asset inflation in the COVID-19 era, but it also builds upon housing pressures well underway prior to the pandemic.

As in other areas of the economy, price inflation in the single-family home market has had both cost-push and demand-pull inflationary forces at work. On the cost side, materials and labor shortages have been powerful. The National Association of Homebuilders (NAHB) noted a 19.4% increase in the Producer Price Index for residential construction input, a more than ten-fold increase compared with 2015-2020. This is due to supply chain disruption that has affected lumber, gypsum board, wire, and other home components.

Over the longer term, the shortage of construction labor will persist. The short-run view is actually positive as the housing surge has sparked a mini-building boom. Residential construction employment was up 6.3% year-over-year as of October 2021, and residential specialty contracting jobs are up 3.3%. But this disguises the larger picture: housing construction employment is down 13.4% (137,000 jobs) from its prior peak, with residential contracting trades similarly down 11.9% (244,300 jobs). We continue to systematically under-produce housing, with supply-side shortages exacerbating inflationary pressure and pricing many homebuyers out of the market.

For those with financial capacity, buying a house has become a fierce bidding competition. That financial capacity was bolstered by direct grants and expanded unemployment relief in the 2020 CARES Act and the

2021 American Rescue Plan that sent the savings rate soaring to an average of 16.3% in 2020 and a slightly lower 13.1% in the first nine months of 2021. Both levels are significantly higher compared to the average savings rate of 7.2% from 2010-2019.

Moreover, interest rates have remained at stunningly low levels. Freddie Mac reported an average of 2.98% for 30-year fixed-rate mortgages from January through early November 2021 after averaging 3.11% during 2020. By comparison, such mortgages carried an average interest rate of 4.09% from 2010-2019. Net residential mortgage borrowing hit \$945.6 billion (at a seasonally adjusted annual rate) in mid-2021, compared with \$321.6 billion in 2018 and \$307.7 billion in 2019.

Such economic incentives enabled the homeownership rate to spike to 67.9% in the second quarter of 2020 before retreating to 65.3% in the third quarter of 2021. The low rates coupled with high levels of spending also tightened the residential sales market to a mere 2.4-month supply of homes for sale as of September 2021 – down from 4.0 months in 2018 and 3.9 months in 2019, and a far cry from the 9.4 months of inventory available in 2010 following the Great Recession.

Imbalances in the for-sale market set the stage for volatility, not only in single-family sector in 2022, but also in the surging multifamily sector. Complicating the picture is the lifting of eviction moratoria in both the ownership and rental housing sectors. The hangover of the COVID-19 induced stresses will be with us for a while, and we can expect the news media to be focusing on this story in the year ahead.

## CAPITAL MARKETS

Liquidity supports a rebound in transaction volume, but rate risk will be an issue to watch in 2022

For most of the past decade, real estate commentary has comforted readers with the observation that the market has been enjoying an abundance of both equity and debt capital. For the most part, that observation has been correct.

Let's take today's temperature. Some key data points that show robust deal flow and increases in valuation are:

- As of mid-2021, the size of the NCREIF Property Index portfolio amounted to \$785 billion, up from \$539 billion just four years ago.

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- Deal volume tracked by Real Capital Analytics (RCA) was \$523.8 billion year-to-date as of October 2021, up 70% from the previous year and on track to match, or even surpass pre-pandemic transaction totals.

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- RCA's national commercial property price index (CPPI) was up 15.9% year-over-year as of October 2021.

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- The value of the NAREIT Equity stock index stood at 15,877 as of the third quarter 2021, having rebounded from its March 2020 low when COVID-19 first hit and now up 50% since 2017.

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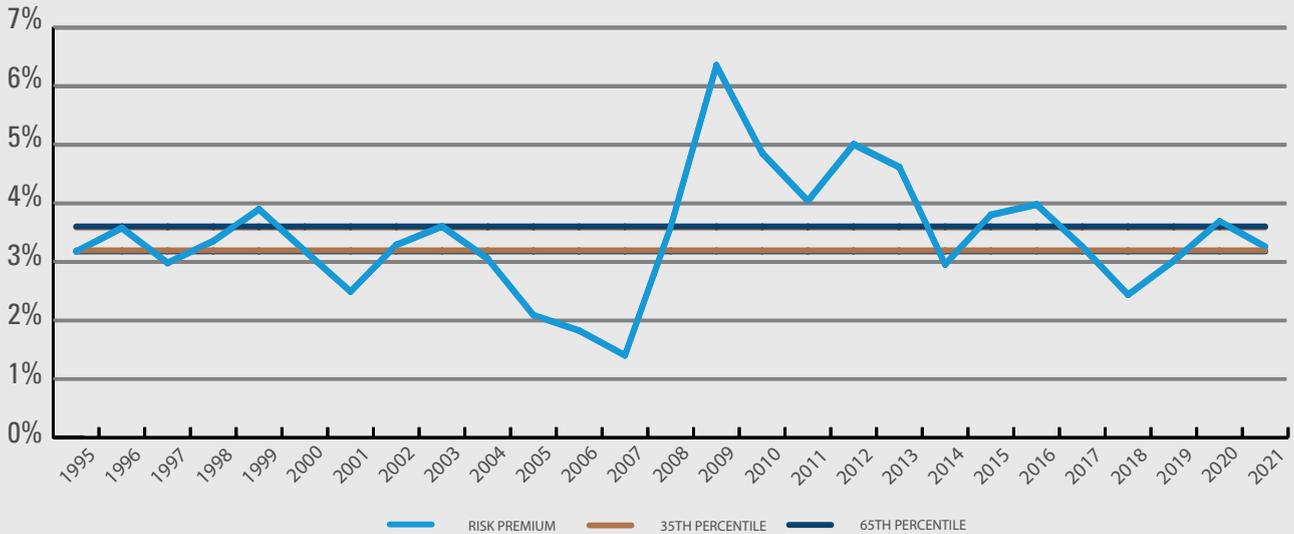
- Commercial mortgage loans outstanding, as tallied by the Federal Reserve's Z.1 report stood at \$3.1 trillion, of which \$1.9 trillion was held by banks, \$450 billion by insurers, \$385 billion by asset-backed securities, and \$207 billion by REITs.

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- Trepp's Quarterly Data Review for fall 2021 noted that private-label CMBS issuance doubled in the third quarter, bringing the year-to-date volume to nearly \$68 billion, up 65% from the same point in 2020.

The graphs for many real estate capital market measures have been taking the worrisome "hockey stick" shape in the COVID-19 recovery period. That's dangerous on two fronts. First, real estate investors are as prone to euphoria as any other market sector, and, unfortunately, the memories of the Great Recession have been fading over time. A second related concern is that in extrapolating recent conditions into the future, there is a real potential for underpricing risk.

## RISK PREMIUM IN MORTGAGE RATE - ALL ASSETS



As the accompanying graph shows, the risk premium in life-insurer mortgage rates has been quite thin – below the red line marking the 35th percentile of historical spreads – for most of the past four years. The jump in risk premiums in 2020 reflects the descent of the risk-free Treasury benchmark to approximately 0.5%. However, rates have moved moderately upward in

2021, and most Fed watchers expected further tightening of rates in 2022. Lenders were slow to react 15 years ago, and rate risk may re-emerge if a deep pool of capital seeking mortgage product again decides to seek market share, rather than pursue strategic safety in a more volatile capital market.

## ABUNDANT CAPITAL SUPPORTING MARKETS



**INFRASTRUCTURE**

Spending bill will bring needed improvement to country's infrastructure and create important multiplier effect for real estate

The coming year marks a crossroads in a very tangible sense, including substantive action on America's huge shortfall in achieving a "state of good repair" in the country's infrastructure based on an evaluation by the American Society of Civil Engineers (ASCE). The good news is that, even prior to the passage of the bipartisan

Infrastructure Bill in November 2021, some progress was being measured. ASCE's overall grade for 2021 was "C-minus". That was by no means a great score, but it is the first time in 20 years that the grade climbed above a "D".

**PRIORITIES: INFRASTRUCTURE BILL AMOUNTS AND ASCE SCORES**

INFRASTRUCTURE CATEGORY	AMOUNT IN LEGISLATION PASSED	AMERICAN SOCIETY OF CIVIL ENGINEERS 2021 REPORT CARD
ROADS AND BRIDGES	\$110 BILLION	ROADS: D; BRIDGES: C
RAIL: PASSENGER AND FREIGHT	\$66 BILLION	RAIL: B
BROADBAND	\$65 BILLION	NOT RATED
POWER GRID	\$65 BILLION	ENERGY GENERATION AND TRANSMISSION: C-
CLEAN WATER	\$55 BILLION	DRINKING WATER: C-
CLIMATE RESILIENCE	\$50 BILLION	LEVEES: D; STORMWATER: D; DAMS: D
PUBLIC TRANSIT	\$39 BILLION	BUS AND COMMUTER RAIL: D-
AIRPORTS	\$25 BILLION	AVIATION: D+
SUPERFUND/BROWNFIELDS	\$21 BILLION	HAZARDOUS WASTE: D+
PORTS	\$17 BILLION	PORTS: B-
ELECTRIC VEHICLE CHARGING	\$7.5 BILLION	NOT RATED

Several key observations can be made. First is that the breadth of the legislation passed in late 2021 is aligned with the wide-ranging needs for reaching a state of good repair. Most categories are in terrible shape. The amount of investment needed to get our infrastructure to a “good” grade is more than \$5 trillion. So, \$1 trillion invested over 10 years makes a dent, but it is not a full solution. Nevertheless, it is a step along the right road.

The second note is that the fiscal measure of the legislation counts its costs in expenditures but is not a measure of its value. The value of an investment in infrastructure comes in its multiplier effect across the economy. The inefficiencies and lost productivity related to congestion and the disruptive impacts of failures in systems such as power, water, and the transport of goods, weakens our economic multiplier.

On average, if an infrastructure marginal increase of \$100 billion per year bolsters output more than its outlay – and \$100 billion is 0.5% of our \$20 trillion GDP – the cost/benefit of the bill is positive. Or, we could look at the costs we would face if no action had been taken, which the ASCE has estimated as \$10 trillion in lost GDP through 2039.

A third observation is that, thankfully, the infrastructure investment is not merely a backward looking “repair” expenditure. Spending categories such as broadband

improvement and electric vehicle charging stations are crucial needs as this economy evolves technologically and functionally. This is a plan about the future. Isn't that what planning is supposed to be about?

Lastly, what stake does real estate have in improved infrastructure? Speed and reliability are needed in all our business functions. Getting workers to and from the job. Getting materials to industrial users and to builders. Getting goods to consumers. Getting travelers to their destinations. Providing the essential power and communication needed to households, whether owners or renters. Mitigating the downside of climate-related costs, including insurance, that currently burden property owners. Real estate has particular reason to cheer that, at the crossroads, America has taken an important step in the right direction.



The amount of investment needed to get our infrastructure to a “good” grade is more than \$5 trillion.

# PROPERTY REPORTS

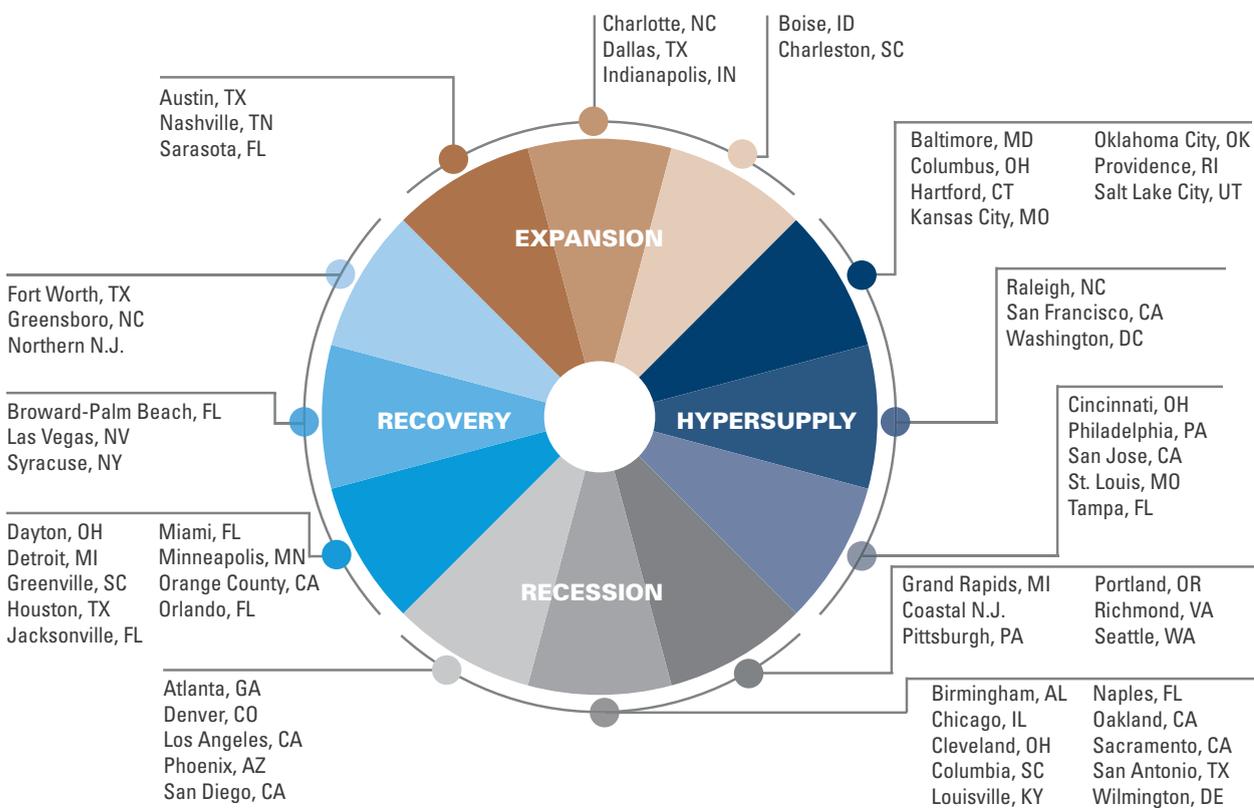


*Despite a strong rebound in economic growth and commercial real estate transaction volume in 2021, the high tide is not lifting all boats equally. Industrial and multifamily continue to lead in property performance and cap rate compression, while waters remain choppy for office, retail, and hospitality.*

## OFFICE

# Wide spread on bid/ask prices constrains transaction volume

### OFFICE MARKET CYCLE



#### EXPANSION

Decreasing Vacancy Rates  
Moderate/High New Construction  
High Absorption  
Moderate/High Employment Growth  
Med/High Rental Rate Growth

#### HYPERSUPPLY

Increasing Vacancy Rates  
Moderate/High New Construction  
Low/Negative Absorption  
Moderate/Low Employment Growth  
Med/Low Rental Rate Growth

#### RECESSION

Increasing Vacancy Rates  
Moderate/Low New Construction  
Low Absorption  
Low/Negative Employment Growth  
Low/Neg Rental Rate Growth

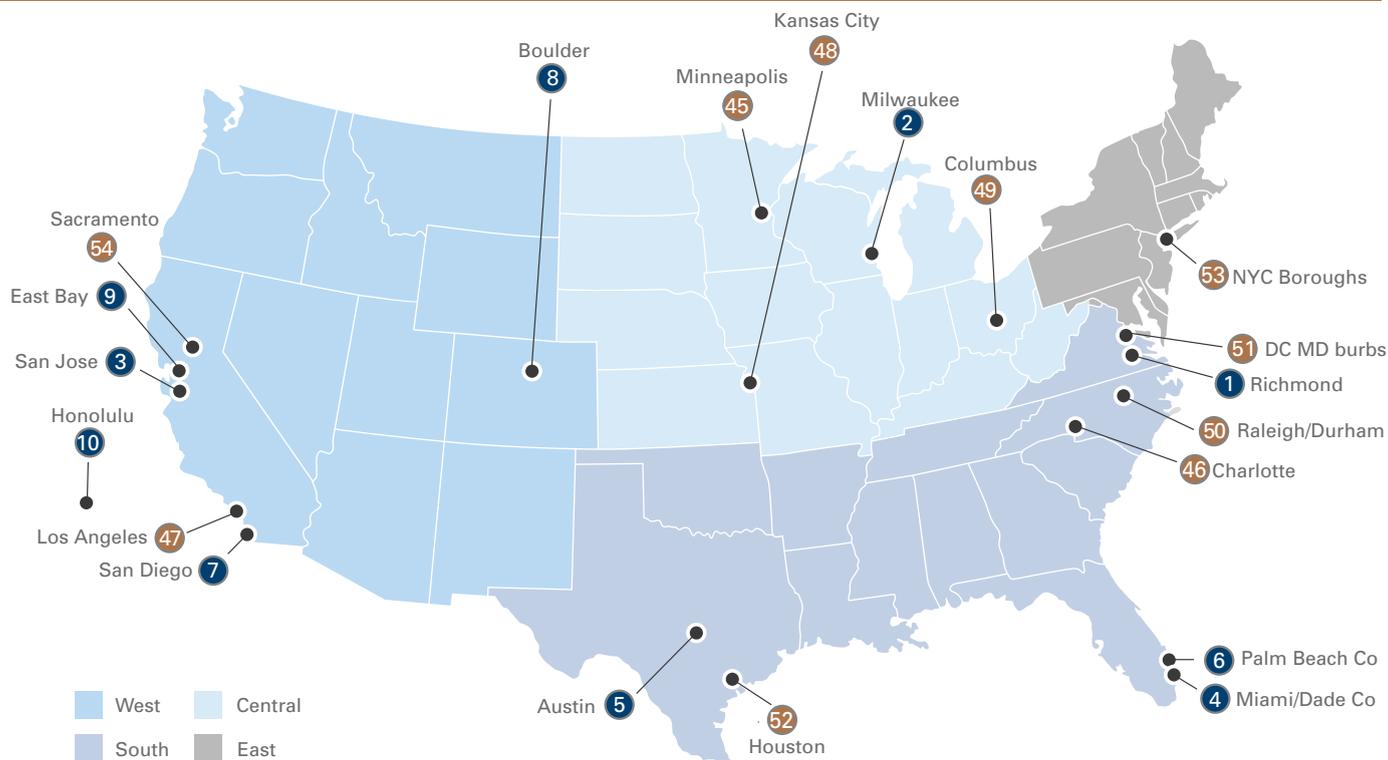
#### RECOVERY

Decreasing Vacancy Rates  
Low New Construction  
Moderate Absorption  
Low/Moderate Employment Growth  
Neg/Low Rental Rate Growth

Chasm of viewpoints on work-from-home vs return-to-work translates into divided expectations for office space occupancy, rents, and ultimately, office building values.

Behavioral economists have identified a powerful effect influencing buying and selling behavior, and the impact on market pricing. They call it the “Anchoring Effect”. In brief, this effect says that when market participants receive what they deem a signal of a market evaluation referent, this signal takes on a life of its own. The result is an anchoring of individual evaluations, which may be above or below the referent, but which center on it.

TOP MARKETS BY OFFICE TRANSACTION VOLUME BASED ON YOY PERCENTAGE CHANGE



**Bulls (Top 10)**

2021 Rank	City	YOY Change	Total 4Q20-3Q21	Vol. Rank*
1	Richmond	629.2%	\$875 M	29
2	Milwaukee	255.6%	\$672 M	34
3	San Jose	181.5%	\$7,120 M	3
4	Miami/Dade Co	176.1%	\$1,977 M	21
5	Austin	165.8%	\$2,828 M	12
6	Palm Beach Co	160.5%	\$1,581 M	23
7	San Diego	149.1%	\$3,353 M	9
8	Boulder	136.5%	\$551 M	40
9	East Bay	135.8%	\$2,492 M	14
10	Honolulu	121.1%	\$314 M	51

**Bears (Bottom 10)**

2021 Rank	City	YOY Change	Total 4Q20-3Q21	Vol. Rank*
45	Minneapolis	-17.8%	\$960 M	26
46	Charlotte	-17.8%	\$2,260 M	18
47	Los Angeles	-19.3%	\$4,066 M	7
48	Kansas City	-21.5%	\$435 M	44
49	Columbus	-26.1%	\$407 M	46
50	Raleigh/Durham	-27.4%	\$1,379 M	24
51	DC MD burbs	-28.6%	\$893 M	28
52	Houston	-45.0%	\$1,675 M	22
53	NYC Boroughs	-45.2%	\$701 M	33
54	Sacramento	-46.6%	\$648 M	36

\* Volume Ranking is based on the overall transaction volume among 54 markets nationally

In 2021, we find much evidence of the persistent power of anchoring in U.S. office markets, and this anchoring phenomenon can be expected to retain its force in 2022.

In its October 2021 review of trends in office markets, Real Capital Analytics (RCA) notes that even with a smart rebound from the depressed levels of 2020, the past year was falling shy of pre-pandemic transaction volume. RCA commented that “buyers and sellers are simply too far apart on expectations” to agree on appropriate price. Capital market specialists have long referred to this as the bid/ask spread, and they see the widening or compression of the spread as an indicator of market liquidity. So, with a wide spread on expectations, it is no surprise to find transaction volume somewhat constrained.

What is the measure of that constraint? Between 2015 and 2019, the annual transaction volume for office properties averaged \$142 billion. Over the first three quarters of 2021, that volume was just \$95 billion and chances of getting close to the pre-pandemic average seemed slim.

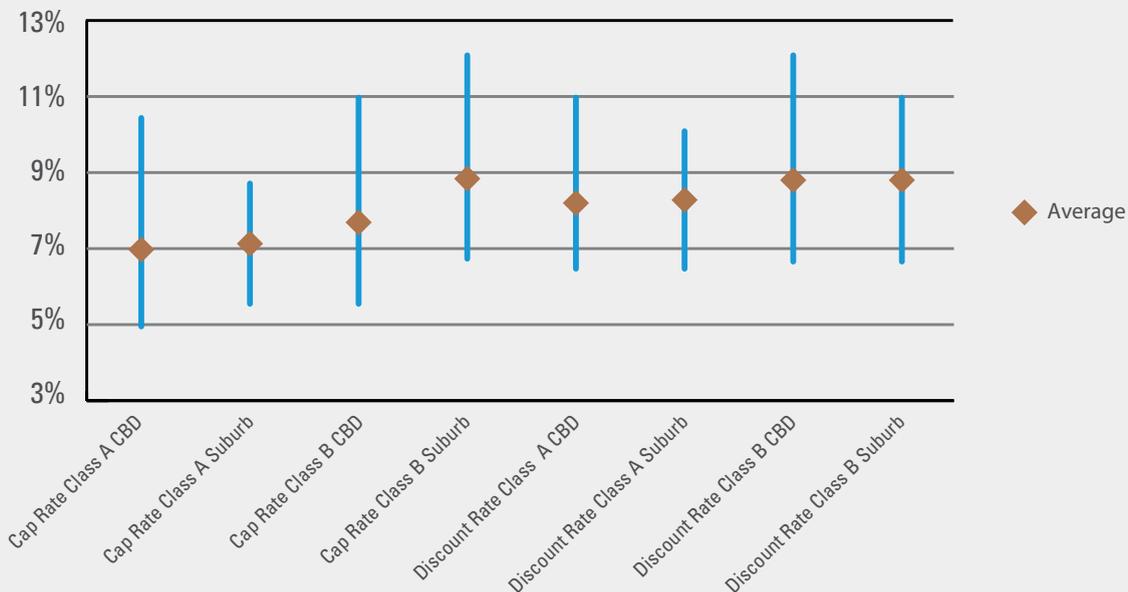
The Anchoring Effect can shed light on why sales volume has been constrained. There is a chasm

between those who expect the work-from-home (WFH) motif that marked the world of office work after the onset of COVID-19 to be the basic template of white-collar employment, and those who anticipate that, in-person office work will return to dominance. At this point, no one seems to believe this is an either/or proposition. Some form of hybrid work management seems more likely, but there is still deep disagreement on where the relative weighting of working styles will fall. And that chasm translates into divided expectations for office space occupancy, rents, and ultimately, office building values.

What are the anchoring signals? Let’s start with density. Lower density suburban office investment outstripped the higher density CBD towers by more

IRR’s survey data on pricing parameters shows only a narrow gap, on average, between office and suburban cap rates, once analyzed by class of property.

### CAP RATES & DISCOUNT RATES - BY CLASS



than 2-to-1 for the first three quarters of 2021. It is true that IRR's survey data on pricing parameters shows only a narrow gap, on average, between office and suburban cap rates, once analyzed by class of property. For Class A offices, there is just a 19 basis point spread between CBD and suburban assets, and a mere 10 basis point difference in discount rates applied to cash flow projections. For Class B assets, similarly, a slim delta of 11 basis points in going-in cap rates exists on average, and an even tighter 6 basis points in the discount rate separates CBD and suburban offices.

But averages can be deceiving, as the "high/low/average" chart drawn from the survey table on page 20 shows. Statistics are always abstractions, and groupings of numbers can provide overall clarity while disguising important differences in the granular data. Take, for example, the range from high-to-low in the cap rates and discount rates displayed. The market is telling us of an anchoring impression of relatively lower risk at the lower end of the ranges but is warning of greater uncertainty at the upper range. More generally, it is saying that the perceived range of risk is more homogeneous across suburban markets than in downtowns.

An examination of just which markets are at the high and low ends suggests where buyers and sellers detect current and post-pandemic advantage (and disadvantage). To take the good news first, cap rates for Class A downtown offices in the 5.0-5.5% range tell us of the positive outlook on the West Coast (L.A., San Francisco, San Jose, Seattle), in key Southeastern cities (Atlanta and Charlotte), and even in Chicago. Interestingly, many of these same cities also post the lowest suburban cap rates. This suggests that overall metropolitan economic vitality trumps the density factor in the outlook for the major West Coast cities, as well as for markets like Charlotte, Dallas, and Denver. And there is considerable consistency in the outlook for reliability of office

income for most of the above-cited markets, as indicated by the associated discount rates applied to cash flows. That's what anchoring looks like.

Unfortunately, a similar pattern can be seen, both for downtown and suburban offices in evaluations of greater risk. The Midwestern markets in Ohio, smaller New England metros like Hartford and Providence, and even Florida markets including Orlando and Jacksonville, display higher than average cap rates and discount rates both for their CBDs and suburbs. This list of more risky markets includes some Southeastern metros as well: Greensboro, N.C., Greenville, S.C., and even the Atlanta suburbs.

The anchoring phenomenon is a critical variable to consider when anticipating which markets are likely to enjoy positive movement on the market cycle wheel in 2022, and which are probably going to be held in place in the coming year.

REGIONAL RATES COMPARISON – OFFICE					
	CAP RATE	DISCOUNT RATE	MARKET RENT (\$/SF)	VACANCY RATE	4Q '20 - 4Q '21 CAP RATE △
<b>SOUTH REGION</b>					
CBD Class A	6.72%	8.01%	\$27.17	17.50%	▼ 14 bps
Suburban Class A	7.10%	8.25%			▼ 13 bps
CBD Class B	7.40%	8.63%			▼ 36 bps
Suburban Class B	7.62%	8.77%	\$19.89	20.71%	▼ 35 bps
<b>EAST REGION</b>					
CBD Class A	7.61%	8.83%	\$38.90	14.45%	▲ 48 bps
Suburban Class A	7.68%	8.96%			▲ 24 bps
CBD Class B	8.47%	9.56%	\$27.45	17.34%	▲ 47 bps
Suburban Class B	8.39%	9.55%			▲ 6 bps
<b>CENTRAL REGION</b>					
CBD Class A	8.00%	9.23%	\$24.87	18.59%	▲ 13 bps
Suburban Class A	7.90%	9.00%			▲ 8 bps
CBD Class B	8.71%	9.79%	\$18.37	22.59%	▲ 10 bps
Suburban Class B	8.65%	9.67%			▲ 4 bps
<b>WEST REGION</b>					
CBD Class A	5.98%	7.40%	\$39.76	16.22%	▼ 2 bps
Suburban Class A	6.25%	7.59%			▼ 5 bps
CBD Class B	6.48%	7.81%	\$28.64	19.65%	0 bps
Suburban Class B	6.75%	7.98%			▼ 4 bps
<b>NATIONAL AVERAGES/SPREADS</b>					
CBD Class A	6.97%	8.27%	\$31.70	16.85%	▲ 4 bps
Suburban Class A	7.16%	8.37%			▼ 2 bps
CBD Class B	7.64%	8.84%	\$22.94	20.20%	▼ 5 bps
Suburban Class B	7.75%	8.90%			▼ 14 bps

## MULTIFAMILY

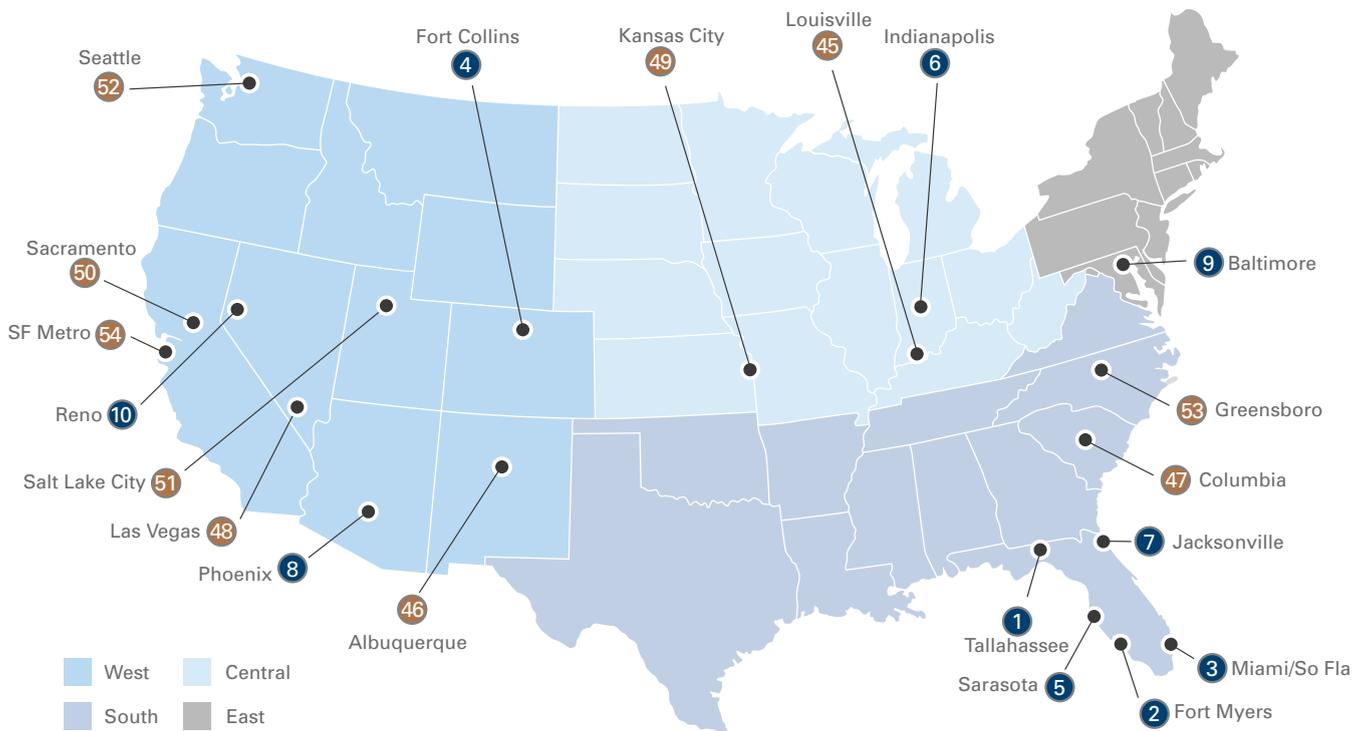
Investors continue to scour the country for available for-sale assets

In physics, the formula for momentum is “mass x velocity.” Multifamily real estate is barreling into 2022 with enormous momentum by all available measures. As far as “mass” is concerned, transaction volume in the apartment sector had surpassed all prior annual records based on year-to-date October 2021 numbers tracked by Real Capital Analytics (RCA). The speed of the multifamily surge has been something to behold, as investment year-over-year was up 96% and the

acceleration of investment has been the swiftest for any period since RCA started monitoring the industry two decades ago.

Multifamily capital flows were, by and large, rational and disciplined even in such an overheated market environment.

**TOP MARKETS BY MULTIFAMILY TRANSACTION VOLUME BASED ON YOY PERCENTAGE CHANGE**



**Bulls (Top 10)**

2021 Rank	City	YOY Change	Total 4Q20-3Q21	Vol. Rank*
1	Tallahassee	255.9%	\$790 M	45
2	Fort Myers	231.5%	\$673 M	49
3	Miami/So Fla	188.5%	\$8,128 M	8
4	Fort Collins	171.0%	\$805 M	44
5	Sarasota	169.5%	\$814 M	43
6	Indianapolis	163.1%	\$1,939 M	28
7	Jacksonville	161.5%	\$2,594 M	25
8	Phoenix	159.5%	\$13,198 M	5
9	Baltimore	158.6%	\$3,175 M	23
10	Reno	156.4%	\$777 M	46

**Bears (Bottom 10)**

2021 Rank	City	YOY Change	Total 4Q20-3Q21	Vol. Rank*
45	Louisville	32.6%	\$642 M	51
46	Albuquerque	32.0%	\$643 M	50
47	Columbia	31.3%	\$595 M	53
48	Las Vegas	20.9%	\$2,799 M	24
49	Kansas City	19.3%	\$1,280 M	33
50	Sacramento	18.1%	\$1,646 M	29
51	Salt Lake City	15.2%	\$1,328 M	31
52	Seattle	7.7%	\$5,859 M	11
53	Greensboro	5.6%	\$855 M	42
54	SF Metro	-34.4%	\$4,243 M	18

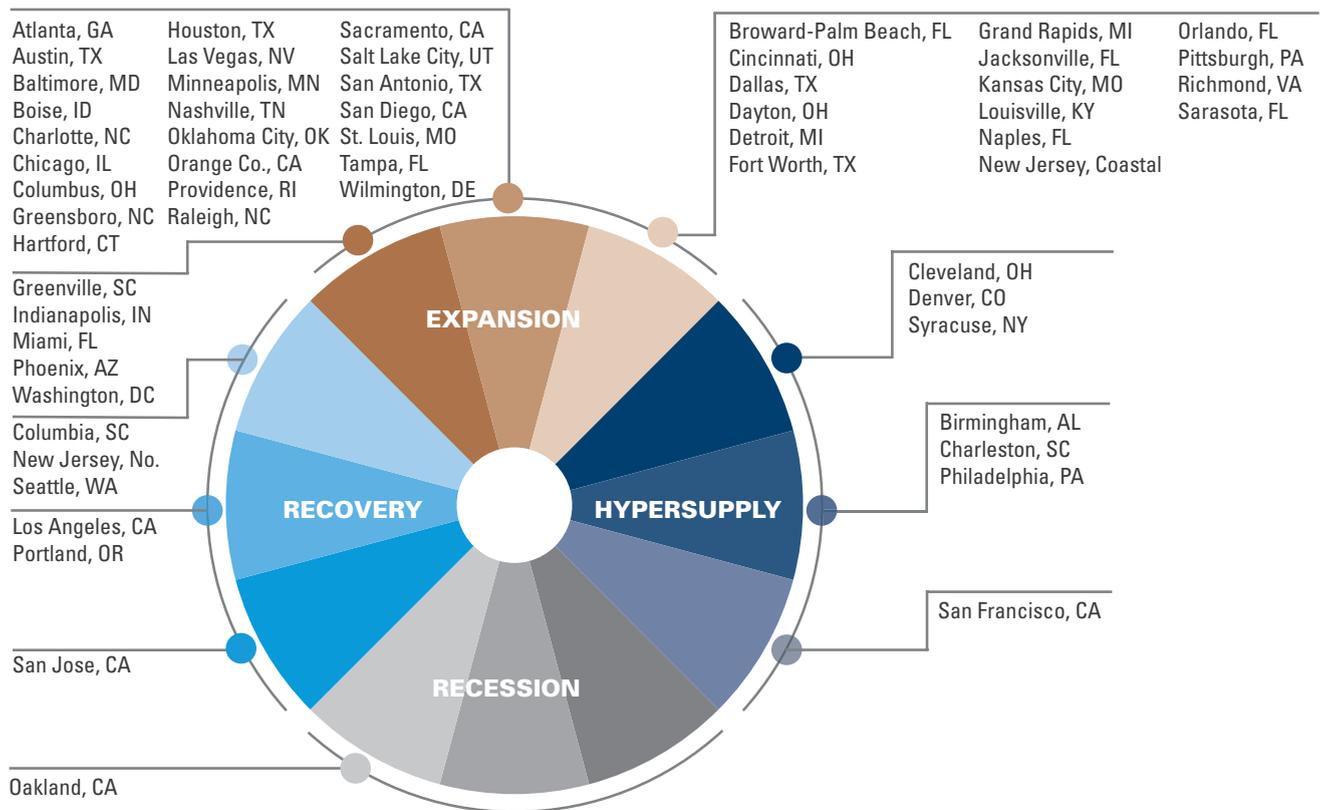
\* Volume Ranking is based on the overall transaction volume among 54 markets nationally

All of this is context for the stunning story emerging from IRR's Q4 2021 *Viewpoint Survey*. Under the pressure of capital seeking quality assets, cap rates and discount rates declined almost across the board. The only exception was the already sky-high priced urban assets along the East Coast. Nationwide, Class A CBD apartment properties commanded sub-5% first-year cap rates, and the expectation that values would hold over time found confirmation in a residual cap rate of just 5.5%. Multifamily also generated the lowest discount rate of any of the asset categories surveyed at 6.5%. The discount rate is an indicator of the expected reliability of the income stream over time. All systems read "go" heading into 2022.

The initial household diaspora from city centers to

suburbs and exurbs in 2020 ran out of steam in 2021. This is unsurprising from our perspective. First of all, there has been a long-term deceleration of household migration in the U.S. dating back to the mid-1980s. This demographic pattern is one, but not the only factor in the much-discussed urban renaissance and the rise of the 24-hour city. Skeptics had been awaiting the end of the downtown revival and quickly jumped on the first evidence of the relocation of affluent urban professionals seeking to avoid the coronavirus threat. Suburban revivalists took every opportunity to trumpet this in the media and made the all-too-frequent mistake of extrapolating a short-run change into a long-term forecast. Based upon the investment spreads favoring urban apartments in 2021, it does not look like multifamily buyers hopped uncritically on the bandwagon.

### MULTIFAMILY MARKET CYCLE



#### EXPANSION

Decreasing Vacancy Rates  
 Moderate/High New Construction  
 High Absorption  
 Moderate/High Employment Growth  
 Med/High Rental Rate Growth

#### HYPERSUPPLY

Increasing Vacancy Rates  
 Moderate/High New Construction  
 Low/Negative Absorption  
 Moderate/Low Employment Growth  
 Med/Low Rental Rate Growth

#### RECESSION

Increasing Vacancy Rates  
 Moderate/Low New Construction  
 Low Absorption  
 Low/Negative Employment Growth  
 Low/Neg Rental Rate Growth

#### RECOVERY

Decreasing Vacancy Rates  
 Low New Construction  
 Moderate Absorption  
 Low/Moderate Employment Growth  
 Neg/Low Rental Rate Growth

That said, investors scoured the country for assets and often found the most available product was the suburban garden complex. Looking to put capital to work in this sector wherever possible, buyers bid cap rates down and dramatically compressed spreads. Both Class A and Class B suburban properties saw their cap rates drop more than 50 basis points year-over-year -- reaching the point where they were just 17 basis points higher than Class A high- and mid-rise buildings in city centers, and a skinny 11 basis points higher for Class B multifamily assets in the suburbs. True, the cap rate spread compression reflected sharply tighter vacancy rates in the suburbs, whose competitive position was enhanced by more affordable rents. This was an important advantage in the uncertain economy of the COVID-19 disruption.

Multifamily capital flows were, by and large, rational and disciplined even in such an overheated market environment. Comparatively little money flowed toward markets classified in the Recession or Hypersupply segments of our cycle wheel. But metros in the Recovery segment saw tens of billions of dollars invested, especially in places like Los Angeles, Phoenix, Seattle, and Washington DC. Even more capital was committed in major markets in the Expansion category, principally in the Southeast and Southwest regions. Atlanta, Austin, Dallas, and Houston each captured \$5 billion or more over the first 10 months of 2021, which was distributed nicely between suburban and urban assets. A cluster of more mid-sized markets in Expansion likewise acted as capital magnets, each receiving between \$3 billion and \$5 billion in multifamily acquisitions. Such metros included Charlotte, Raleigh, Nashville, Orlando, and Tampa in the Southeast, while San Antonio, San Diego, and Las Vegas also enjoyed similar deal volumes.

Developers, naturally, responded to the environment of ample capital and strong rental housing demand by increasing production. Construction data from the Census Bureau shows year-over-year completions up 14.1% as of August 2021, and bigger leaps in permitting activity at 52.7% and multifamily starts at 60.1% in the same time frame. This is all the more

notable because residential construction was subject to the disruption of materials supplies and shortage of labor constraining the economy as a whole. Of course, this means the cost of new production is increasing, illustrating another way in which inflation is being felt in the real estate sector.

The multifamily industry is buoyed by ample debt capital and a strong pool of equity. Mortgage Banker Association data shows mortgage commitments rising from all sources: banks, life insurance companies, the GSEs, and private-label security issuers. Delinquencies on multifamily debt have been modest – certainly lower than for hotel and retail mortgages. And as of November 2021, 30+ day delinquencies on multifamily CMBS debt was just 1.9%, according to Trepp’s analysis.

All told, for the rental apartment industry in 2022, the theme music sounds like “seldom is heard a discouraging word.” Or, in the words of Damon Runyon, “The race is not always to the swift, nor the battle to the strong – but that’s the way to bet.”

REGIONAL RATES COMPARISON - MULTIFAMILY

	CAP RATE	DISCOUNT RATE	MARKET RENT (\$/SF)	VACANCY RATE	4Q '20 - 4Q '21 CAP RATE ▲
<b>SOUTH REGION</b>					
Urban Class A	4.65%	6.22%			▼ 72 bps
Suburban Class A	4.92%	6.44%	\$1,457.38	5.87%	▼ 72 bps
Urban Class B	5.51%	6.97%			▼ 62 bps
Suburban Class B	5.74%	7.17%	\$993.38	4.20%	▼ 70 bps
<b>EAST REGION</b>					
Urban Class A	5.48%	6.78%			▼ 10 bps
Suburban Class A	5.54%	6.89%	\$2,048.80	6.52%	▼ 26 bps
Urban Class B	6.05%	7.35%			▼ 17 bps
Suburban Class B	6.04%	7.40%	\$1,403.20	3.38%	▼ 30 bps
<b>CENTRAL REGION</b>					
Urban Class A	5.44%	7.29%			▼ 50 bps
Suburban Class A	5.39%	7.20%	\$1,392.18	5.90%	▼ 63 bps
Urban Class B	6.24%	8.02%			▼ 55 bps
Suburban Class B	6.17%	7.85%	\$892.55	3.44%	▼ 58 bps
<b>WEST REGION</b>					
Urban Class A	4.38%	6.04%			▼ 33 bps
Suburban Class A	4.71%	6.43%	\$2,251.23	6.00%	▼ 30 bps
Urban Class B	4.87%	6.46%			▼ 23 bps
Suburban Class B	5.11%	6.80%	\$1,565.31	3.23%	▼ 34 bps
<b>NATIONAL AVERAGES/SPREADS</b>					
Urban Class A	4.90%	6.50%			▼ 48 bps
Suburban Class A	5.07%	6.67%	\$1,724.91	6.02%	▼ 53 bps
Urban Class B	5.62%	7.15%			▼ 44 bps
Suburban Class B	5.73%	7.26%	\$1,173.10	3.69%	▼ 54 bps



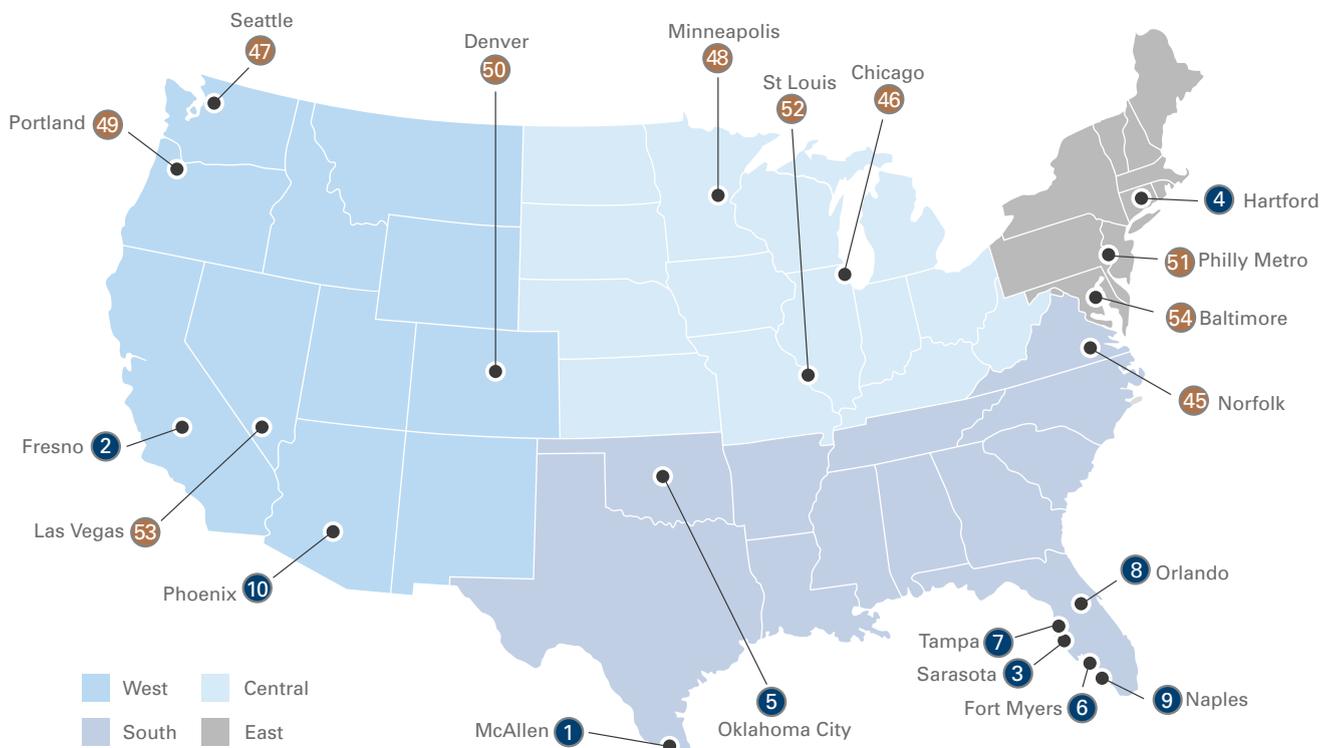
**RETAIL**

Despite challenges,  
glimmer of optimism  
emerges

The songwriter and author Richard Fariña, a Brooklyn-born talent of Cuban and Irish extraction, published his novel *Been Down So Long It Seems Like Up to Me* in 1966. The book title might serve as an epigram to a review and outlook of the retail real estate sector in this third decade of the 21st century. The travails of malls and shopping centers have been a steady motif of Cassandra-like pronouncements for decades now.

Take, for instance, the comments in *Emerging Trends in Real Estate 2000* by PwC and Lend Lease published more than 20 years ago: “There is too much retail. That’s been the problem for the past decade, and Internet retailing will just add to the available retailing channels... From 20 to 30% of existing retail is redundant. We are really ‘under-demolished’.”

**TOP MARKETS BY RETAIL TRANSACTION VOLUME BASED ON YOY PERCENTAGE CHANGE**



**Bulls (Top 10)**

2021 Rank	City	YOY Change	Total 4Q20-3Q21	Vol. Rank*
1	McAllen	977.8%	\$194 M	47
2	Fresno	151.1%	\$221 M	44
3	Sarasota	150.4%	\$298 M	35
4	Hartford	149.0%	\$239 M	43
5	Oklahoma City	147.7%	\$161 M	52
6	Fort Myers	141.6%	\$244 M	42
7	Tampa	141.0%	\$906 M	16
8	Orlando	116.7%	\$936 M	14
9	Naples	115.5%	\$153 M	53
10	Phoenix	105.6%	\$1,881 M	7

**Bears (Bottom 10)**

2021 Rank	City	YOY Change	Total 4Q20-3Q21	Vol. Rank*
45	Norfolk	-10.0%	\$190 M	48
46	Chicago	-11.9%	\$1,825 M	8
47	Seattle	-15.0%	\$1,019 M	13
48	Minneapolis	-17.4%	\$570 M	23
49	Portland	-19.6%	\$271 M	39
50	Denver	-20.6%	\$931 M	15
51	Philly Metro	-21.6%	\$646 M	19
52	St Louis	-31.7%	\$282 M	37
53	Las Vegas	-33.9%	\$718 M	18
54	Baltimore	-36.2%	\$284 M	36

\* Volume Ranking is based on the overall transaction volume among 54 markets nationally

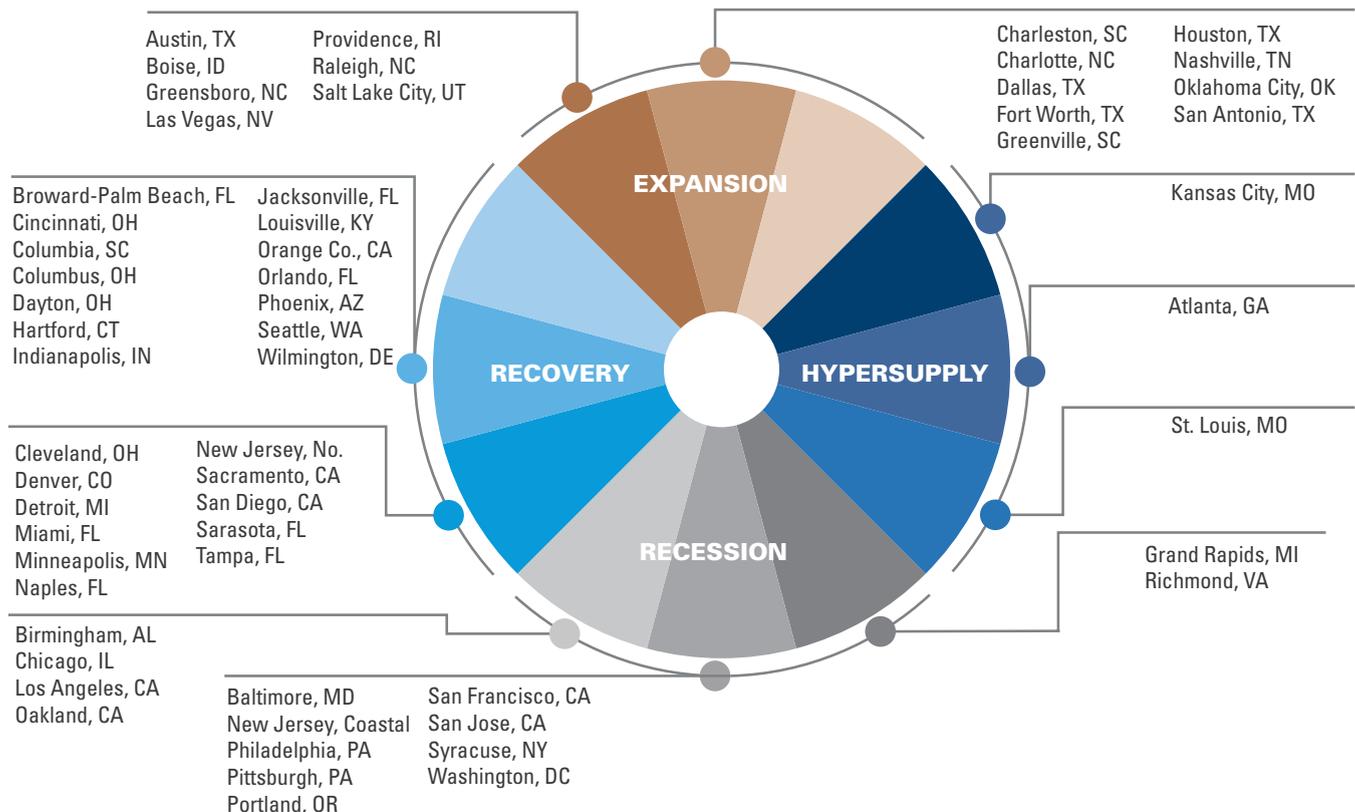
## One-fourth of American retail property markets are in the Recession phase compared to half in the 2020 survey.

Even as we enter 2022, it is hard to find real estate professionals who would strenuously disagree with such an assessment. But *Viewpoint* this year provides an occasion to look up, at least somewhat. Where a year ago we reported that more than half of U.S. retail markets were mired in the Recession phase of the cycle, this issue can announce that that dire situation has been cut in half. As we analyze conditions, just

25% of American retail property markets are in a Recessionary trough. A remarkable 42% can be said to be in Recovery, and a further 27% in Expansion with 5% in the development-positive Hypersupply phase.

It seems startling, but let's look at the details. Investors, seem skeptical of any claim of light on the retail horizon. Real Capital Analytics (RCA) transaction volume in 2021 (year-to-date through October) was just \$51 billion, less than half of the industrial sector and about one-fourth of the multifamily total. Consequently, in RCA's metrics, retail cap rates have remained elevated even as warehouse/distribution and residential apartment cap rates have declined.

### RETAIL MARKET CYCLE



#### EXPANSION

Decreasing Vacancy Rates  
 Moderate/High New Construction  
 High Absorption  
 Moderate/High Employment Growth  
 Med/High Rental Rate Growth

#### HYPERSUPPLY

Increasing Vacancy Rates  
 Moderate/High New Construction  
 Low/Negative Absorption  
 Moderate/Low Employment Growth  
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#### RECESSION

Increasing Vacancy Rates  
 Moderate/Low New Construction  
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#### RECOVERY

Decreasing Vacancy Rates  
 Low New Construction  
 Moderate Absorption  
 Low/Moderate Employment Growth  
 Neg/Low Rental Rate Growth

IRR’s survey reinforces RCA’s findings. Going-in cap rates, discount rates, and reversionary cap rates for both Class A regional malls and community shopping centers are higher, on average, than the investment rates for CBD office, industrial, and multifamily. Interestingly, the retail property rates are similar to suburban office rates across the board. However, it is worth noting a couple of distinctions. First, the retail property type is predominantly suburban. And next, when taken together, the data appears to suggest a jaundiced view of a purported re-blossoming of suburbs as a post-pandemic phenomenon. Finally, the absence of Class B retail from the analysis should not be considered accidental: there has been very little investor appetite for older or poorly positioned retail property, much of which is falling to the residual value of the land it sits upon or is primed for adaptive reuse.

Even with this caveat there is a real glimmer of optimism to be found in the data. In all regions of the country, retail cap rates have declined between eight and 50 basis points year-over-year (2020 – 2021). All regions but the East see discount rates falling between 10 and 48 basis points. While data on market rents and vacancy are mixed, at least the trends are no longer entirely dour. Perhaps this augurs a 2022 opportunity for selective contrarian investors to step in with acquisition capital when competitive pressures are limited.

What are the markets that seem to be making a positive cyclical move?

Fifteen metros have evolved from a Recession classification to Recovery. Some may be surprises, others not. Improvements in market fundamentals have bolstered a number of Midwest cities: Columbus, Indianapolis, and Detroit among them. South Florida is marking steps forward on both the Atlantic and Gulf Coasts in Miami, Broward/Palm Beach, Naples, and Sarasota. Hartford, Northern New Jersey, and Wilmington have moved into the positive phase of the property cycle. And conditions are also brightening in dynamic Western metros including Denver, Phoenix, Seattle, Sacramento, and San Diego.

Furthermore, five of the markets with maturing Expansions should be noted as newly arrived in this category for

*Viewpoint 2022.* The strong GDP growth in 2021 has prompted a surge in energy demand that has not only raised gas prices at the pump but invigorated the Houston economy. Phoenix and Salt Lake City are also in Expansion mode. Salt Lake’s metro population has continued to grow about 1.1% per year, even through the pandemic, while metro Phoenix is sustaining demographic growth at about 2 percent per year. Providence, meanwhile, has successfully stemmed the economic decline that shrunk its consumer base and is now capitalizing on its recovering housing market, in concert with its vital educational and cultural resources. Greensboro, meanwhile, finds its pool of household income steadily increasing, with recent demographic change following the trendline of the past 10 years, adding about 5,000 residents annually.

All in all, the challenges facing the retail sector should not be dismissed. It is not at all clear that a sustained positive turnaround can be announced. However it is a maxim that no one should do research unless willing to be surprised. And even if the retail property sector is still “down” on a relative basis, we find credible evidence that “looking up” is at least one way to characterize the *Viewpoint* for 2022.

**In all regions of the country, retail cap rates have declined between eight and 50 basis points.**

REGIONAL RATES COMPARISON - RETAIL					
	CAP RATE	DISCOUNT RATE	MARKET RENT (\$/SF)	VACANCY RATE	4Q '20 - 4Q '21 CAP RATE ▲
<b>SOUTH REGION</b>					
Community Retail	6.97%	8.29%	\$18.66	10.55%	▼ 23 bps
Neighborhood Retail	6.83%	8.14%	\$17.01	11.51%	▼ 40 bps
<b>EAST REGION</b>					
Community Retail	7.20%	8.65%	\$18.66	10.55%	▼ 50 bps
Neighborhood Retail	7.52%	9.05%	\$17.01	11.51%	▼ 38 bps
<b>CENTRAL REGION</b>					
Community Retail	7.40%	8.38%	\$18.66	10.55%	▼ 26 bps
Neighborhood Retail	7.65%	8.37%	\$17.01	11.51%	▼ 37 bps
<b>WEST REGION</b>					
Community Retail	6.23%	7.64%	\$18.66	10.55%	▼ 8 bps
Neighborhood Retail	6.20%	7.80%	\$17.01	11.51%	▼ 25 bps
<b>NATIONAL AVERAGES/ SPREADS</b>					
Community Retail	6.92%	8.21%	\$21.65	10.31%	▼ 25 bps
Neighborhood Retail	6.96%	8.26%	\$19.44	10.69%	▼ 35 bps



## INDUSTRIAL

# Unprecedented demand continues to fuel industrial expansion

It was Shakespeare who wrote in his 1591 play *Henry VI*, “Ill blows the wind that profits nobody.” This was shortly after one of England’s periodic outbreaks of the bubonic plague (1585-1587). As we navigate through the COVID-19 pandemic, the Bard’s words resonate as they often do, with contemporary meaning.

The performance of industrial markets, by their point in the real estate cycle, depicts how the disruption of the American economy since the spring of 2020 has indeed brought profit to at least one commercial property sector. Our survey this year finds 90% of industrial in the Expansion phase of the cycle, 7% in Recovery, and just 3% in Hypersupply. Notably, not a single industrial market is rated as being in Recession. By far, this is the strongest profile of the major property types, even ahead of the solid multifamily sector.

A year ago, *Viewpoint* underscored the nation’s vulnerability to stresses stemming from the “just-in-time” inventory management approach, which had not yet fomented the supply-chain crisis that became headline news as 2021 developed. But the expanding dependence on e-commerce, pandemic-exacerbated labor shortages in manufacturing abroad and distribution at home, and the risk of a single unobtainable part to bring an entire assembly process to a halt, has now been the subject of investigation in pretty much every serious journalism medium.

The pressure of relative scarcity has not stalled out demand for warehousing and distribution real estate from either the user or investor. On the contrary, it has inspired a seemingly national spirit of FOMO (Fear of Missing Out). Since the summer of 2021, it seems, consumers have been inundated with warnings that shortages were likely to lead to disappointments when the holiday shopping season came around. Coupled with the price increases that are triggered when the supply and demand curves are misaligned, the result has been a feverish rush for maximum throughput in the goods sector of the economy.

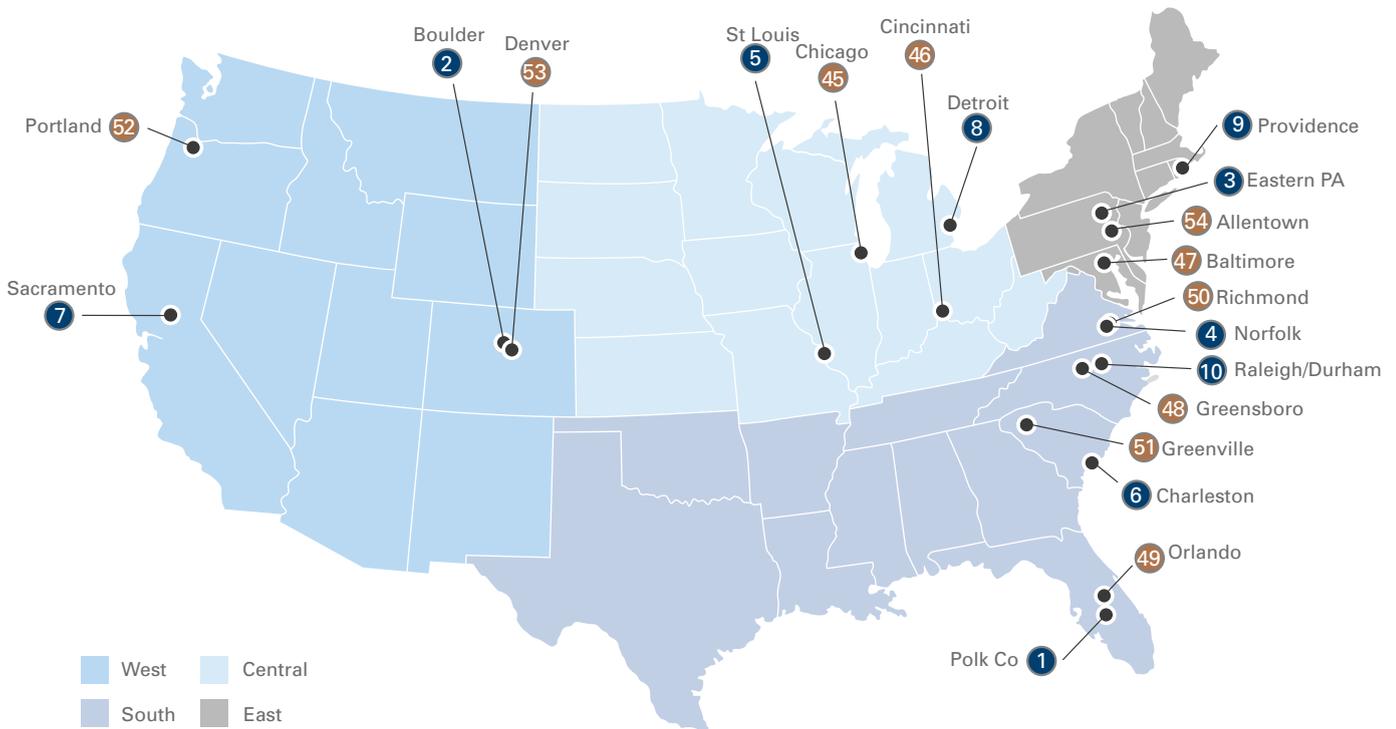
Transaction data from Real Capital Analytics (RCA) displays the consequently rising volume of investment, descending capitalization rates,

and steeply rising prices for industrial property assets. As the pie chart depicting regional investment volume on page 33 shows, every region of the country was sharing in the over \$107 billion of industrial transactions recorded year-to-date through October 2021. Private equity led the parade of buyers, representing 44% of dollar volume, followed by institutional capital at 29.4%. Cross-border investors were reasonably active with a 12.6% market share, which was about double the purchase total of REITs.

Investors are responding to unprecedented demand signals from space users. Vacancies have continued a

Net absorption tracked by national brokerages reached record territory during 2021, with the potential to exceed 400 million square feet by year's end.

**TOP MARKETS BY INDUSTRIAL TRANSACTION VOLUME BASED ON YOY PERCENTAGE CHANGE**



**Bulls (Top 10)**

2021 Rank	City	YOY Change	Total 4Q20-3Q21	Vol. Rank*
1	Polk Co	508.8%	\$1,035 M	31
2	Boulder	355.8%	\$629 M	45
3	Eastern PA	299.1%	\$467 M	50
4	Norfolk	286.4%	\$425 M	51
5	St Louis	218.5%	\$1,777 M	17
6	Charleston	192.0%	\$473 M	49
7	Sacramento	180.3%	\$1,197 M	27
8	Detroit	180.0%	\$910 M	34
9	Providence	167.6%	\$546 M	48
10	Raleigh/Durham	141.5%	\$1,541 M	20

**Bears (Bottom 10)**

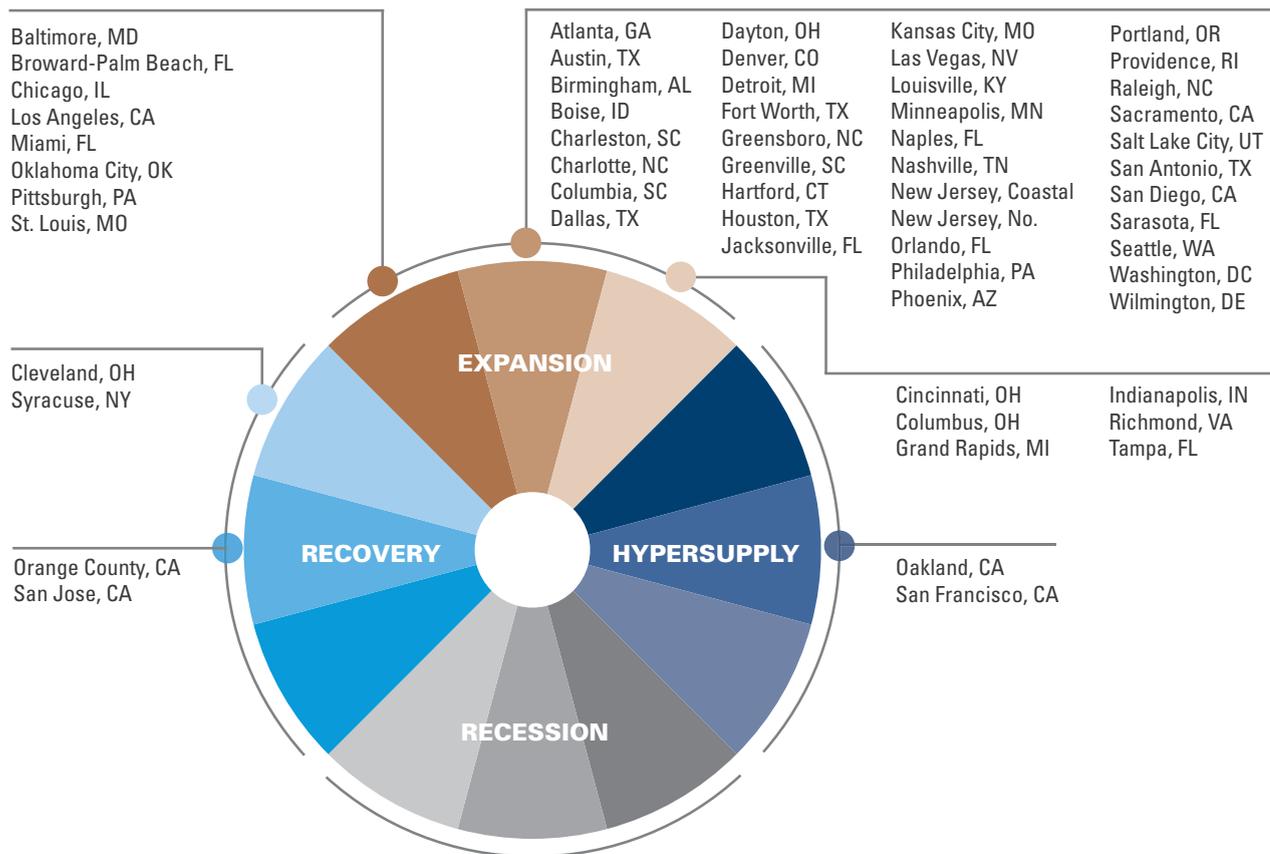
2021 Rank	City	YOY Change	Total 4Q20-3Q21	Vol. Rank*
45	Chicago	-4.9%	\$5,964 M	5
46	Cincinnati	-4.9%	\$762 M	38
47	Baltimore	-5.5%	\$1,503 M	21
48	Greensboro	-5.7%	\$763 M	37
49	Orlando	-6.4%	\$985 M	32
50	Richmond	-11.3%	\$574 M	47
51	Greenville	-14.3%	\$657 M	44
52	Portland	-19.6%	\$918 M	33
53	Denver	-24.0%	\$1,449 M	23
54	Allentown	-75.5%	\$600 M	46

\* Volume Ranking is based on the overall transaction volume among 54 markets nationally

decade-long downward trend and now stand below 5%. Net absorption tracked by national brokerages reached record territory during 2021, with the potential to exceed 400 million square feet by year's end. Expectations for further expansion in 2022 are high, backed by anticipation that consumption will remain strong and supply chain disruptions will ease somewhat. However, there is a shadow side to such robust conditions: price pressures are increasing at nearly every step from producer to end-user. As such, cost-push inflation is very much the economic environment for this sector.

For the 90% of markets IRR classifies in the Expansion phase, rent growth has been exceptional. Double-digit percentage increases in rent, for instance, have been measured in Baltimore, Columbus, Los Angeles, Miami, Northern New Jersey, Sacramento, Salt Lake City, and Washington DC. There are severe shortages of very large distribution properties, which is creating a major squeeze for the nearly 30% of the leasing market represented by logistics firms. The COVID-19 boost in e-commerce demand now has the online sale of goods accounting for nearly 20% of retail sales, resulting in more goods flowing direct to consumers.

## INDUSTRIAL MARKET CYCLE



### EXPANSION

Decreasing Vacancy Rates  
Moderate/High New Construction  
High Absorption  
Moderate/High Employment Growth  
Med/High Rental Rate Growth

### HYPERSUPPLY

Increasing Vacancy Rates  
Moderate/High New Construction  
Low/Negative Absorption  
Moderate/Low Employment Growth  
Med/Low Rental Rate Growth

### RECESSION

Increasing Vacancy Rates  
Moderate/Low New Construction  
Low Absorption  
Low/Negative Employment Growth  
Low/Neg Rental Rate Growth

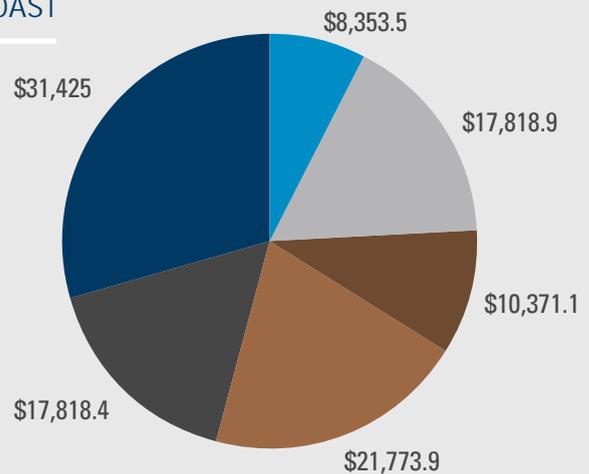
### RECOVERY

Decreasing Vacancy Rates  
Low New Construction  
Moderate Absorption  
Low/Moderate Employment Growth  
Neg/Low Rental Rate Growth

## INDUSTRIAL INVESTMENT: BUYERS ACTIVE COAST TO COAST

SALES VOLUME IN MILLIONS

- Mid-Atlantic
- Midwest
- Northeast
- Southeast
- Southwest
- West



With such sunny prospects, it is worth pausing a moment to (perhaps) curb our enthusiasm. The attitude of “what could possibly go wrong?” is very often the precursor to rude shocks. Real estate veterans are rightfully leery of “hockey stick growth” graphs, and that is the shape of many industrial market indicators. So, what are the potential warning signals to watch out for?

First of all, it is vital to keep in mind that this is anything but a normal real estate cycle, even if it seems an extreme one. We are still coping with a disruption, which is a form of discontinuous change. The boost to household incomes we saw in 2020 and 2021 through direct payments to millions of American households will not be replicated in 2022.

Second, the Federal Reserve is signaling that it will tap the brakes on growth next year in response to the 2021 inflation evidence. We should never forget the maxim of the former Fed Chair William McChesney Martin, who described the Fed’s role as “taking away the punch bowl once the party gets going.”

Third, the pandemic certainly spiked e-commerce demand, and it is reasonable to anticipate that households have greatly satisfied pent-up demand,

especially for consumer durables. Deceleration in online shopping growth would not be a surprise.

These cautionary notes are not intended to diminish the remarkable run of success in the industrial sector. But wise managers know the efficacy of contingency planning in advance of slowdowns. After all, we cannot expect that we will be seeing the number of industrial markets in Recession to remain at “zero” indefinitely.

### REGIONAL RATES COMPARISON - INDUSTRIAL

	CAP RATE	DISCOUNT RATE	MARKET RENT (\$/SF)	VACANCY RATE	4Q '20 - 4Q '21 CAP RATE ▲
<b>SOUTH REGION</b>					
Flex Industrial	6.76%	7.97%	\$9.01	7.83%	▼ 74 bps
Industrial	6.04%	7.29%	\$5.36	8.50%	▼ 71 bps
<b>EAST REGION</b>					
Flex Industrial	6.60%	7.78%	\$10.02	10.12%	▼ 34 bps
Industrial	6.29%	7.50%	\$7.23	6.03%	▲ 8 bps
<b>CENTRAL REGION</b>					
Flex Industrial	7.58%	8.54%	\$7.64	10.43%	▼ 22 bps
Industrial	6.78%	7.96%	\$4.49	8.17%	▼ 30 bps
<b>WEST REGION</b>					
Flex Industrial	5.71%	7.21%	\$12.93	7.47%	▼ 48 bps
Industrial	5.16%	6.71%	\$7.54	6.31%	▼ 48 bps
<b>NATIONAL AVERAGES/SPREADS</b>					
Flex Industrial	6.65%	7.87%	\$9.88	8.59%	▼ 52 bps
Industrial	6.03%	7.32%	\$6.01	7.51%	▼ 45 bps

**HOSPITALITY**

Two steps forward,  
and one step back



It is no secret that the hospitality market experienced true carnage in 2020 due to the onset of the global COVID-19 pandemic. CV-19 put many hotels and restaurants out of business, and the entire hotel industry is still struggling. Hundreds of thousands of hotel employees lost their jobs, and now the U.S. lodging industry is dealing with a huge labor shortage as former employees have left the industry for higher paying jobs. Further disruption emerged due to extensive supply chain shortages.

Fast forward into the first half of 2021. The lodging market experienced gains in ADR and occupancy, due primarily to a strong return of leisure travelers, which yielded summer occupancy levels beyond earlier expectations at U.S. hotels. Luxury and upscale hotels did not fare as well. Demand ebbed as students returned to school after a year of home-schooling, just as the CV-Delta variant swept the country and the world. This variant threatened the “return to the office” and business travel/group meeting plans of many firms. Clearly, the hotel market cannot reach any true level of stabilization or recovery until convention and business travel and international travelers return.

Now, in fourth quarter 2021, the Omicron variant threatens any return to profitability, potentially reversing the gains achieved during the first half of 2021. Earlier projections anticipated a return to pre-pandemic levels and market stabilization by 2023. However, there is now concern that the market may not fully stabilize and allow a return to profitability until 2025. Statistics can be misleading.

STR and Tourism Economics, CoStar’s analytic company, reported that RevPAR on a nominal basis is projected to be fully recovered in 2023. This top-line recovery is based on improved RevPAR projections that are largely due to ADR gains. STR/TE officials clearly indicate, however, that statistical RevPAR gains were due in part to strong demand and also to revenue management controls and inflation. This top line recovery does not mean a return to profitability. STR/TE reported that when adjusted for inflation, RevPAR will likely remain below 2019 levels until at least 2025. While demand and ADR may recover by 2023, the underlying question is: When will profitability return?

According to the latest edition of CBRE’s Hotel Horizons, all 65 major U.S. lodging markets were expected to achieve RevPAR gains in 2021. Larger

markets will see greater percentage gains in RevPAR (46.8%) during the year compared to the smaller markets (36.3%); truthfully, because they suffered more in 2020. The magnitude of the difference in RevPAR growth becomes even more exaggerated in 2022. CBRE is forecasting a RevPAR increase of 34.3% for the 65 markets during the year, while the markets outside this 65-city universe are anticipated to see their RevPAR levels drop 6.2%. This decline is mostly attributable to the loss of the price premiums currently obtained by hotels in remote and rural locations and by management pushing ADR over occupancy. The underlying reality in this projection is that, despite the strong RevPAR growth rate, by year-end 2022 the \$86.65 RevPAR achieved by the major market properties will still lag their 2019 RevPAR levels by 18.8%. The gap will be even greater in the nation’s 25 largest hotel markets, where the RevPAR deficit is projected to be 21.4%. For comparative purposes, the entire U.S. lodging industry is forecast to achieve a 2022 RevPAR that is 18.3% below 2019 levels.

Almost all experts offering their projections, including hotel investors and brokerage companies, are using calendar year 2019 as the benchmark for market comparison, as that was the last full year of data prior to the onset of the pandemic. While the hotel market has certainly improved during 2021, and it is projected to continue to improve during 2022, CoStar analytics reported that “beneath the surface of national averages hide the most uneven recovery in the history of the hospitality industry”. STR/TE reports that RevPAR is down by 20% in 2021 when compared to the same point in 2019. Most of the largest U.S. markets have performed worse than the U.S. average because these markets depend on business travelers, conventioners, and international guests who have not materialized in 2021, and these segments may not fare much better in 2022. The markets that have come close to 2019 levels are primarily popular beach areas that benefitted from pent-up demand from leisure travelers.

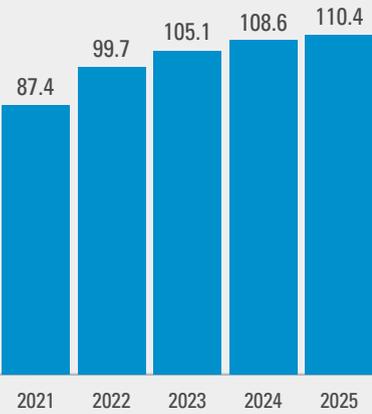
**STR/TE reported that when adjusted for inflation, RevPAR will likely remain below 2019 levels until at least 2025.**

STR/TE is forecasting 2022 occupancy at 63.4% (+1.1%), ADR at \$130 (+1.06%), and RevPAR at \$82.00 (+1.17%). Leisure demand is expected to boost performance in resort and remote areas; thereby skewing market statistics and the prognostication of a full recovery. The fact is that the threat of continued market disruption from the COVID pandemic can and may likely cause even the best projections for the hospitality market in the near-term future to be nothing more than hope and speculation.

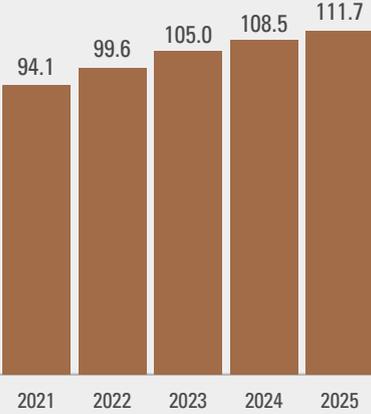
Most of the largest U.S. markets have performed worse than the U.S. average because these markets depend on business travelers, conventioners, and international guests.

DEMAND AND ADR NEAR FULL RECOVERY IN 2022 WITH REVPAR FULLY RECOVERING IN 2023. U.S. KPIS, INDEXED TO 2019

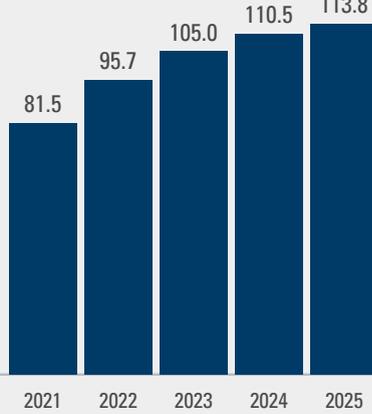
DEMAND INDEX



ADR INDEX



REVPAR INDEX





**INVESTOR RATES TABLE**  
INTEGRA REALTY RESOURCES CAPITALIZATION RATES  
DISCOUNT RATES AND REVERSION RATES

**2022**

# 2022 INVESTOR RATES TABLE

INTEGRA REALTY RESOURCES CAPITALIZATION RATES  
DISCOUNT RATES AND REVERSION RATES

## EAST REGION

BALTIMORE, MD  
HARTFORD, CT  
NEW JERSEY, COASTAL  
NEW JERSEY, NO  
PHILADELPHIA, PA  
PITTSBURGH, PA  
PROVIDENCE, RI  
SYRACUSE, NY  
WASHINGTON, DC  
WILMINGTON, DE

## SOUTH REGION

ATLANTA, GA  
AUSTIN, TX  
BIRMINGHAM, AL  
BROWARD-PALM BEACH, FL  
CHARLESTON, SC  
CHARLOTTE, NC  
COLUMBIA, SC  
DALLAS, TX  
FORT WORTH, TX  
GREENSBORO, NC  
GREENVILLE, SC  
HOUSTON, TX  
JACKSONVILLE, FL  
MIAMI, FL  
NAPLES, FL  
NASHVILLE, TN  
OKLAHOMA CITY, OK  
ORLANDO, FL  
RALEIGH, NC  
RICHMOND, VA  
SAN ANTONIO, TX  
SARASOTA, FL  
TAMPA, FL

## CENTRAL REGION

CHICAGO, IL  
CINCINNATI, OH  
CLEVELAND, OH  
COLUMBUS, OH  
DAYTON, OH  
DETROIT, MI  
GRAND RAPIDS, MI  
INDIANAPOLIS, IN  
KANSAS CITY, MO  
LOUISVILLE, KY  
MINNEAPOLIS, MN  
ST. LOUIS, MO

## WEST REGION

BOISE, ID  
DENVER, CO  
LAS VEGAS, NV  
LOS ANGELES, CA  
OAKLAND, CA  
ORANGE COUNTY, CA  
PHOENIX, AZ  
PORTLAND, OR  
SACRAMENTO, CA  
SALT LAKE CITY, UT  
SAN DIEGO, CA  
SAN FRANCISCO, CA  
SAN JOSE, CA  
SEATTLE, WA

AVERAGES

CLASS A GOING IN CAPITALIZATION RATES (%)									CLASS B GOING-IN CAPITALIZATION RATES (%)			
CBD OFFICE	SUBURBAN OFFICE	INDUSTRIAL	FLEX INDUSTRIAL	URBAN MULTIFAMILY	SUBURBAN MULTIFAMILY	REGIONAL MALL RETAIL	COMMUNITY RETAIL CENTER	NEIGHBORHOOD RETAIL	CBD OFFICE	SUBURBAN OFFICE	URBAN MULTIFAMILY	SUBURBAN MULTIFAMILY
7.25	7.75	5.50	6.00	5.50	6.00	8.50	7.00	7.25	9.00	8.50	7.00	6.50
8.25	8.50	7.50	7.75	5.50	5.50	9.00	7.50	8.00	8.50	8.75	6.00	6.25
7.25	5.65	6.50	5.50	5.60	7.50	7.50	7.50	7.75	7.65	5.75	5.85	5.85
6.00	6.50	4.25	5.25	5.00	5.00	9.00	6.00	6.00	8.00	8.25	5.50	5.50
7.50	7.50	5.50	6.00	5.50	5.25	7.25	6.75	7.00	8.00	8.00	6.25	6.00
8.00	7.50	7.25	6.50	6.00	6.25	8.75	8.25	8.00	9.00	8.75	6.25	6.75
8.50	8.75	7.25	7.50	5.25	5.75	8.00	7.50	7.75	8.75	9.00	6.00	6.25
8.00	8.00	8.50	8.50	5.75	5.50	8.00	8.00	9.50	9.00	8.50	6.25	6.00
6.50	7.50	5.50	6.00	4.75	5.00	7.00	6.25	6.50	7.00	8.50	5.00	5.25
8.50	7.50	6.00	6.00	6.00	5.50	7.75	7.25	7.50	9.00	8.00	6.50	6.00
5.25	6.75	5.50	7.25	4.25	5.25	6.00	6.25	6.75	5.75	7.25	5.50	6.50
6.60	7.00	6.20	6.70	4.90	4.90	7.10	7.40	6.80	7.90	8.20	7.20	7.20
7.00	7.00	5.75	7.50	4.75	4.75	7.50	7.50	6.50	7.25	7.25	5.75	5.75
6.25	6.75	6.00	6.00	4.25	4.25	6.00	6.00	6.25	6.75	7.25	4.50	4.50
6.50	7.50	7.25	7.50	3.50	3.85	7.50	7.00	7.25	7.00	8.00	5.00	5.25
5.00	5.50	4.20	5.00	4.00	4.50	7.00	6.75	6.50	6.50	7.25	5.00	5.75
7.00	7.25	6.00	7.00	5.50	6.00	7.00	7.75	7.00	7.50	8.00	5.75	6.25
6.00	6.50	6.00	7.00	4.75	5.75	8.00	6.25	6.50	7.50	7.00	5.00	6.25
6.70	6.26	6.50	7.00	4.75	5.00	9.00	6.00	6.00	6.90	6.60	5.00	5.25
7.50	7.75	5.00	7.50	5.00	5.00	8.00	7.00	6.75	8.50	8.75	7.00	7.50
7.00	7.75	5.50	6.50	5.75	6.00	7.00	7.50	6.25	7.50	8.00	6.00	6.25
6.90	7.20	6.60	7.10	5.40	5.40	7.30	7.10	7.00	7.90	8.20	6.50	6.50
8.50	7.75	4.75	6.25	4.50	4.25		8.00	7.00	9.00	8.00	4.75	
5.75	6.50	5.50	5.50	4.00	4.00	6.25	5.75	5.75	6.00	7.50	4.25	4.25
7.25	6.75	6.75	6.75	5.50	6.75	6.75	7.00	7.00	7.50	7.50	6.75	6.00
6.50	7.50	6.25	6.00	4.25	4.25	8.75	7.50	7.50	6.50	7.50	5.00	5.00
6.75	7.25	7.75	8.25	6.00	6.50		7.25	7.50	7.75	8.00	6.50	7.25
8.50	8.00	4.75	6.25	4.50	4.00		7.00	6.50	9.00	8.00	4.75	4.75
6.50	7.25	5.75	5.75	4.00	4.25	7.25	7.00	7.25	7.25	7.50	4.75	5.00
6.75	7.25	5.75	7.00	5.00	5.25	7.75	7.75	7.75	8.00	8.00	6.25	6.00
7.00	7.25	7.00	7.25	4.50	4.50	7.50	7.00	7.00	7.50	7.75	5.25	5.25
6.50	7.25	7.25	7.25	5.75	5.75	6.75	6.75	7.00	6.50	6.50	6.00	6.00
7.25	7.50	7.00	7.25	4.00	4.25		7.00	7.25	7.50	7.25	4.50	4.75
5.50	7.50	5.00	8.25	4.50	5.00	7.00	7.50	8.00	6.25	8.50	5.25	5.75
8.25	8.75	7.25	7.75	6.00	6.25	8.50	8.00	7.75	9.50	9.75	7.00	7.00
8.00	8.75	7.00	7.75	6.25	6.50	8.10	7.85	7.65	8.00	9.00	7.25	7.50
8.00	8.25	6.75	7.75	4.50	4.25	8.25	7.50	7.25	8.75	8.75	4.75	4.50
10.50	8.50	8.50	8.75	7.75	6.75	8.00	8.25	8.50	11.00	9.25	8.50	7.75
8.25	8.00	8.00	8.00	5.00	4.75	6.25	6.50	7.00	8.75	8.50	5.50	5.00
7.25	8.00	8.00	7.75	4.50	4.75	7.50	7.75	8.25	7.75	8.50	4.75	5.50
8.00	7.75	5.50	7.00	5.00	5.00	6.00	7.00	7.50	8.50	8.25	5.50	5.75
7.50	7.75	7.00	7.75	5.75	5.75	7.00	7.25	7.75	8.25	8.50	6.50	6.50
8.75	7.75	6.65	7.15	6.25	5.70		7.75	7.95	9.75	8.75	7.85	6.50
7.00	6.50	4.50	5.50	4.00	4.50	6.50	6.00	6.50	8.00	7.75	5.00	5.50
9.00	7.25	7.25	7.50	5.75	5.50	7.50	7.50	7.75	10.00	8.25	7.00	6.75
6.25	6.50	6.00	6.00	4.50	5.00	6.25	6.50	6.75	6.50	6.75	5.00	5.50
6.00	6.00	5.00	5.50	4.50	4.75	7.75	7.50	7.00	7.00	7.50	4.75	4.75
7.00	7.50	5.25	5.50	4.50	4.50	7.50	7.25	7.00	7.00	7.50	4.75	4.75
5.50	5.75	4.75	5.50	3.75	4.75	5.50	5.50	5.25	5.75	6.00	4.00	5.00
6.00	6.25	4.50	5.50	5.00	6.00	6.00	6.00	6.25	6.50	6.75	5.75	6.25
6.50	6.25	4.25	4.75		4.00	5.00	5.90	5.00	6.50	6.50	4.25	
6.50	6.50	5.00	6.00	4.25	4.25	7.00	6.50	6.50	7.00	7.00	4.75	4.75
6.00	6.25	5.75	6.75	4.50	5.50		6.75	6.50	6.75	6.75	5.75	6.25
6.25	6.75	6.00	6.25	5.50	5.75	6.50	6.50	6.75	6.75	7.25	5.75	6.25
6.00	6.50	5.00	5.00	3.75	4.25	7.50	6.50	7.00	6.50	6.75	4.50	4.75
6.50	6.25	5.50	5.50	4.00	4.00	6.50	5.75	5.75	6.75	6.50	4.50	4.50
5.25	5.75	5.25	5.00	4.25	4.25	4.75	4.75	4.75	5.50	6.00	4.50	4.50
5.50	5.50	5.75	6.00	4.00	4.00	6.50	5.25	5.50	6.00	6.50	4.50	4.50
5.00	5.75	4.25	6.75	4.50	5.00	5.50	6.50	6.75	6.25	6.75	4.75	5.50
6.97	7.16	6.03	6.65	4.90	5.07	7.21	6.92	6.96	7.64	7.75	5.62	5.73

CLASS A DISCOUNT RATES (%)									CLASS B DISCOUNT RATES (%)			
CBD OFFICE	SUBURBAN OFFICE	INDUSTRIAL	FLEX INDUSTRIAL	URBAN MULTIFAMILY	SUBURBAN MULTIFAMILY	REGIONAL MALL RETAIL	COMMUNITY RETAIL CENTER	NEIGHBORHOOD RETAIL	CBD OFFICE	SUBURBAN OFFICE	URBAN MULTIFAMILY	SUBURBAN MULTIFAMILY
8.75	9.25	6.75	7.25	7.00	7.75	8.50	8.25	9.25	10.50	10.00	8.50	8.50
9.25	9.75	8.75	9.00	6.50	6.50	9.25	8.75	9.00	9.50	10.00	7.00	7.25
8.60	7.00	7.50	7.00	7.10	8.50	8.50	7.75		8.95	7.25	7.25	
7.50	8.25	5.25	6.00	6.00	6.00	9.00	8.00	8.00	8.75	9.25	6.50	6.50
9.00	9.00	7.00	7.50	7.50	7.25	8.75	8.50	9.00	9.50	9.50	8.00	7.75
8.50	8.00	8.25	7.75	6.50	6.75	9.50	9.75	10.25	9.50	9.25	6.75	7.50
9.50	9.75	8.25	8.50	6.25	6.75	9.25	8.75	9.00	9.75	10.00	7.00	7.25
9.00	9.00	9.50	9.50	6.75	6.50	10.00	9.50	10.50	9.50	9.50	7.25	7.00
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10.00	9.50	7.50	7.50	8.25	8.00	9.25	8.75	9.75	10.50	10.00	9.00	8.50
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8.00	8.50	7.00	8.25	6.50	6.75	9.25	9.25	9.25	9.50	9.50	7.75	7.50
8.25	8.50	8.25	8.75	5.75	5.75	8.00	7.75	7.75	8.75	9.00	6.50	6.50



# SPECIALTY REPORTS



**AUTO DEALERSHIPS**

# Limited inventory fuels pent-up demand

**Automotive Dealership Trends**

Automotive dealerships have changed greatly since their inception. The first dealerships were primarily small businesses in central locations. As automobiles became more affordable, dealerships transformed from small buildings to large sites that could accommodate more product lines and keep a larger inventory of vehicles. Dealerships began to relocate into suburban areas where land was cheaper and more plentiful. As a result, auto malls became more attractive to dealers. The synergy created by the variety of dealerships is now viewed as a benefit that typically outweighs any negatives associated with competition. The number of new car dealerships has declined as auto malls increased in popularity. However, the number of new car dealerships has remained relatively stable since 2015.

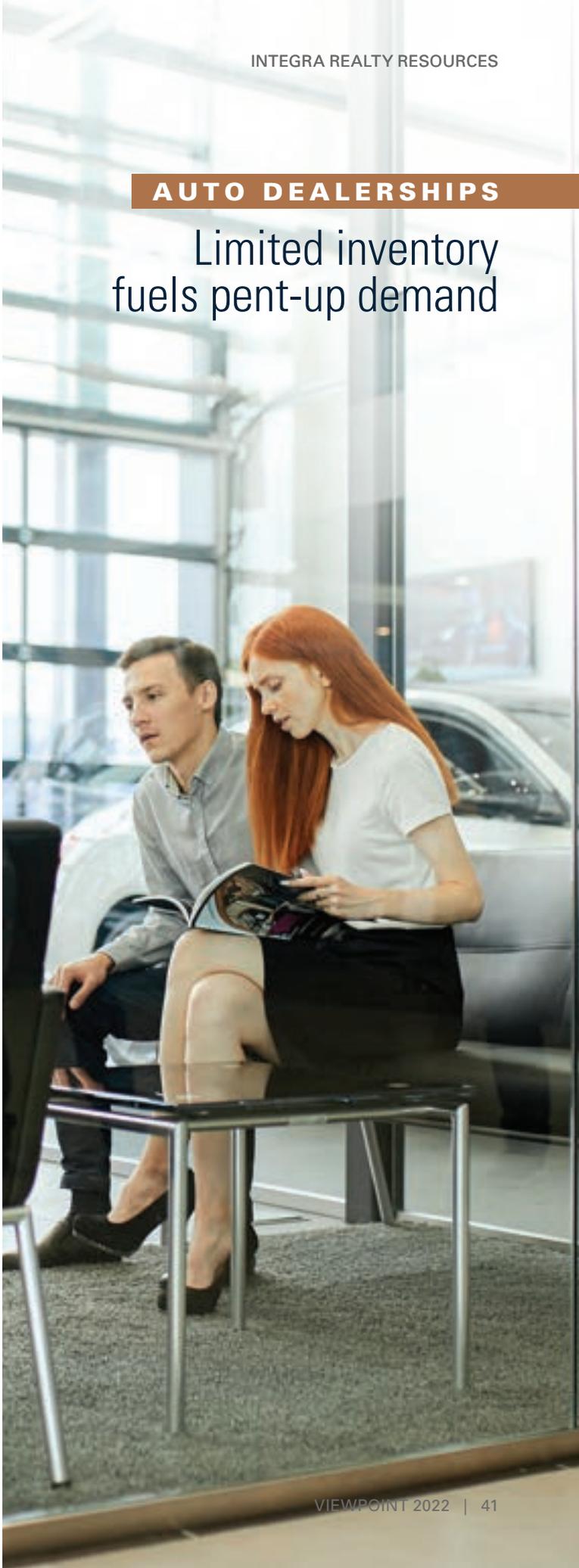
**Dealership Sales and Profits**

Automotive dealerships have three main centers of profit: new car sales, used car sales, and vehicle service and parts retailing.

From 2011 through 2015, the percentage of total sales attributed to new car sales steadily increased, likely due to the growing buying power of shoppers. Beginning in 2016, dealers began looking for ways to augment profits from used car, service, and parts sales, particularly as the internet has provided more options to potential buyers. A consistent upward trend in used car sales has been seen since that time. The ongoing COVID-19 pandemic has accelerated the pace of used car sales as manufacturing delays have severely limited new inventory. Dealers overwhelmingly report high profits in the current environment, fueled by the lack of negotiating power for buyers due to severe inventory shortages. Industry leaders report that demand is significantly outpacing supply, and growing pent-up demand is further fueling higher profits on fewer sales.

**Vehicle Sales Trends**

The United States automobile market has historically been a very cyclical industry. New vehicle sales climbed to a record high in 2016, reaching 17.5 million. Sales then stabilized before declining sharply in 2020 as a result of the COVID-19 pandemic. The current shortage of microchips continues to drive lower total sales, though it also provides higher profits for dealers. Additionally, low interest rates and high



trade-in values have helped mitigate any dissuasion of potential buyers due to lack of dealer incentives and high prices. It is anticipated that manufacturing constraints will slowly improve in the next year, though inventory levels will remain tight due to pent-up demand.

### Dealership Marketability Trends

Historically, dealerships were owned and/or operated primarily by local groups. However, this trend is moving toward regional and national automotive groups. In recent years, large national corporations and dealership groups have seen rises in dealership profits and in dealership real estate, and have been acquiring smaller franchises. AutoNation is the largest automotive group in the country, operating 235 franchises in 16 states as of year-end 2020. Berkshire Hathaway acquired Van Tuyl Group in 2015 and now owns 100 franchises in 10 states. In late 2015, Soros Fund Management invested in McLarty Automotive Group, a growing group which began with eight dealerships and has since grown to 37 dealerships with the backing of the Soros group.

Most recently, the Larry H. Miller Group announced the sale of its 64 dealerships to Asbury Automotive Group. This represents one of the largest acquisitions seen in decades, between the sixth-largest group and the eighth-largest group in the nation. Lithia Motors, the third-largest group, is likewise focused on expansion, with a recently announced goal of reaching \$50 billion in revenue in five years through acquisitions. Industry insiders expect more mega-deals in the coming years as larger groups are able to streamline operations and function more efficiently. Favorable financing conditions also contribute to the recent increase in sale activity.

### Dealership Real Estate Trends

The overwhelming majority of new car dealership facilities are transferred as part of a larger sale of the franchise. The general feeling among market participants in the auto industry is that dealership franchises are currently being priced at record levels and pricing continues to increase. The price allocated to the real estate as part of the going concern acquisition appears to generally follow the same trend, though it is frequently constrained by the slower appreciation of underlying land value. Moving forward, real estate value trends are anticipated to continue an upward trend as transactional activity has accelerated.

### Industry Trends

Industry concerns include tariff and regulation issues, as well as a general fulfillment of demand for automobiles, particularly considering the ongoing microchip shortage. Also, manufacturers continue to pressure franchise owners to upgrade facilities. This is occurring in both small and large markets. However, small markets in particular are experiencing challenges in rapidly rising upgrade costs, as well as higher competition from large ownership groups and internet sales. Still, prospects for the industry are generally positive with innovative design and technology and lack of inventory driving demand higher.

Moving forward, real estate value trends are anticipated to continue an upward trend as transactional activity has accelerated.

### AUTOMOTIVE DEALER SALES BREAKDOWN

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021*
New Car Sales	54%	56%	57%	58%	58%	58%	58%	57%	56%	55%	55%
Used Car Sales	32%	32%	31%	31%	30%	30%	30%	31%	32%	33%	35%
Service/Parts	13%	12%	12%	11%	11%	12%	12%	12%	12%	12%	11%
<b>TOTAL</b>	<b>100%</b>										

**GOLF COURSES**

Did COVID-19 save golf?  
Demand is on the rise as  
both golfers and investors  
return to the links

Golf rounds played in 2020 increased by 13.9% over 2019 levels, and on course participation increased by some 500,000 golfers, according to NGF and Golf Datatech

Did COVID-19 save golf? That statement may seem a bit hyperbolic, but there are some elements of truth in it. In order to assess the effect the pandemic had on the industry, it is important to first understand the pre-existing underlying fundamentals of the industry.

To begin, every market functions based on supply vs demand. In a perfect world, the two are in equilibrium, with a sufficient amount of supply available to satisfy the available demand. But markets are imperfect and fluid, and fluctuations in supply vs demand over time result in changes in volume and pricing. In the case of golf, new golf course development (supply) exploded from the late 1980s through 2005. According to the National Golf Foundation (NGF), more than 4,500 new 18-hole equivalent courses opened during this timeframe, the majority of which were new, primarily upper tier, courses developed in conjunction with residential subdivisions.

However, golf participation during this timeframe was relatively stagnant, generally fluctuating between 23.8 and 24.8 million golfers. And thus, with the substantial increase in course supply relative to stagnant demand, the result was that the volume of golf rounds remained essentially unchanged but was being spread across an increasing number of facilities.

As a result of the increase in competition, predictably, golf courses began discounting fees to attract play, which only served to lower top line revenue without drawing new players to the sport. As this reality became evident, the pace of new development began to slow as financing for new projects became increasingly difficult to secure in light of the changing financial landscape.

And then came the recession. As the economy cratered in 2008 and into 2009, an already challenging operating landscape became ever more difficult to navigate, and slowly but surely, courses began to close. Over 1,600 courses closed permanently from 2010 through 2020, which eased the course oversupply somewhat, but certainly not to equilibrium.

This brings us back to the pandemic and its effect on golf. With the onset of the pandemic in March 2020, and subsequent mandated shutdowns during the first wave, many courses nationwide were closed for a period of two to three months. However, upon reopening, the popularity of golf surged as it was viewed as a safe outdoors recreational activity. Despite the forced closure of courses during the

shutdown, rounds played in 2020 increased by 13.9% over 2019 levels, and on course participation increased by some 500,000 golfers, according to NGF and Golf Datatech. In 2021, rounds played year-to-date through September also increased over pre-2020 levels, albeit at a lower rate.

Is this increase in demand sustainable, or is it a blip that will level off as the pandemic subsides? While no one can answer that question to this point in time, signs are pointing to a renewed interest in golf, over and above just being a safe outdoor activity.

One factor is the development of “off-course” facilities utilizing golf course simulators, which allow for someone to play golf, but not on a “green grass” course. These off-course venues have successfully married golf with a casual and fun entertainment venue, allowing non-golfers to experience golf in a more accessible (and less intimidating) format. TopGolf is the leader in the space with over 60 facilities, but other operators such as Drive Shack are entering the field, as are small independent entrepreneurs.

Another factor is changing demographics. Many Baby Boomers, who had delayed retirement, decided that it was time to retire during the pandemic, and are playing golf in increasing numbers. Millennials, a group that had largely avoided golf because it was viewed as too time consuming and stodgy, are now turning to golf, partly aided by their exposure to the sport at off-course facilities. An increasing number of minorities and women are taking up the game. And lastly, COVID introduced a whole new generation to the sport with families hitting the links together, and parents who signed their kids up for safe, socially-distanced junior golf summer programs.

But how are these improving fundamentals influencing golf investment? Jeff Woolson, Managing Director with CBRE’s Golf & Resort Properties division, indicates that they are seeing an increase in the listing/sale of profitable golf courses. Profitable properties have sold on a 6x to 10x multiple of EBITDA (or a 10% to 14% cap rate). In comparison, unprofitable courses have sold on a GRM basis, generally ranging from 1.0x to 1.5x and less than 1.0x for lower revenue courses.

Chris Charnas, Principal with Links Capital Advisors, indicates that he is seeing new buyers starting to enter the market, drawn by the improving returns, and that investors who were used to low multiples and limited competition will have to adjust to a new transaction reality in 2022.

The future of golf appears to be bright, with renewed interest from both participants and investors. Headwinds remain, including an ongoing lack of financing, as well as the potential for increased labor costs as wages continue to increase. However, it appears that golf may have turned the corner towards a return to supply and demand equilibrium.

Profitable golf courses have sold on a 6x to 10x multiple, or a 10% to 14% cap rate.

## SENIOR HOUSING

Rebound in occupancies provides tailwind for NOI growth



Like many other real estate sectors, senior housing was hammered from several directions following the outbreak of the pandemic. Most obviously, occupancy levels fell. Staffing, the costliest expense, also is experiencing large increases. Lower occupancy and revenue, and higher operating expenses, in many markets have offset the

benefits lower interest rates are having on value. But wait, the baby boomers are coming. The average age of entrance into senior housing is in the low 80s, which means the oldest boomers are less than five years away from hitting the entry doors of senior housing.

IRR performs senior housing and healthcare property valuation services nationally. In 2021 alone, we have appraised proposed and existing senior housing properties coast-to-coast – from Florida to Alaska and Maine to California (no trips to Hawaii this past year). We have seen a broad spectrum of conditions ranging from markets that were oversaturated before the pandemic to markets that have more demand than supply. It is not surprising to know that some markets with high development cost, or barriers to entry (land scarcity and extraordinarily high construction costs), have unmet need, and conversely, lower-entry-cost markets are frequently experiencing low occupancy and pricing pressures.

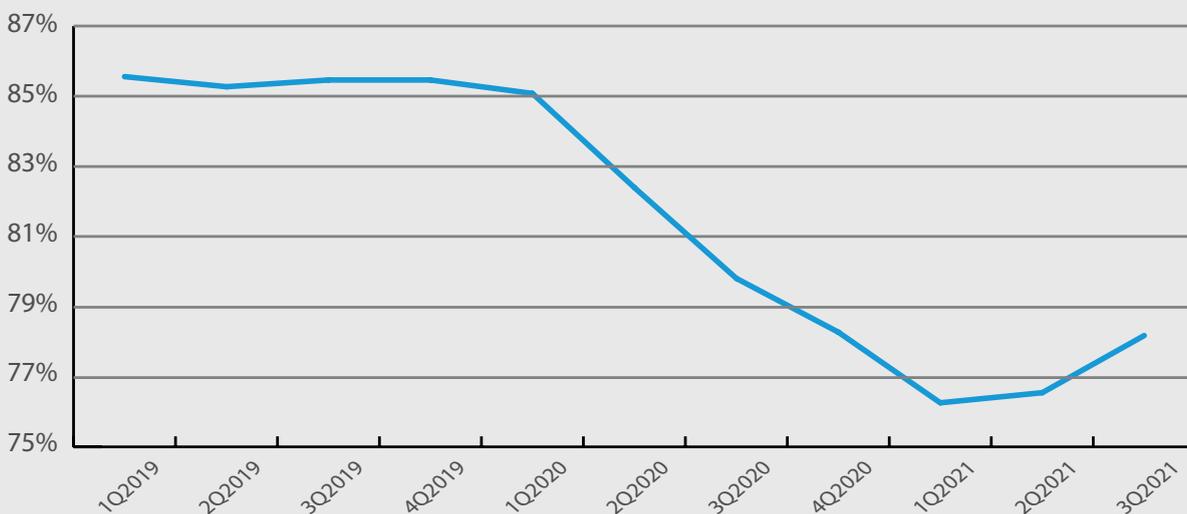
We are seeing a widening spread in capitalization rates in 2021, with several recently built and stabilized senior housing properties selling at rates under 5.0%. Keep in mind, when discussing capitalization rates, everyone should get on the same NOI definition page. Much like stocks, real estate investors are buying future earnings, and valuations are based on anticipated earnings. Therefore, NOI for stabilized properties, as developed for appraisal purposes, involves anticipated occupancy, revenue, and operating expenses over the coming 12 months rather than the trailing NOI. All of the expenses should be applied consistently in extracting capitalization

from market transactions and developing the NOI forecast for the property being valued. Using trailing NOI to develop a market capitalization and applying to a forecasted NOI for the subject property is a problem. Given that context for the NOI story, several sales of new, stabilized senior housing properties in suburban markets of “major-league cities” commanded sub-5.0% capitalization rates during 2021 from institutional-type buyers. Driving these lower capitalization rates are low mortgage rates and better-than-average prospects for demand growth – the Boomers are coming.

On the other hand, we are seeing more senior housing properties that were already suffering from extended absorption caused by market oversaturation get pushed into a corner because of the pandemic. The owners of most senior housing properties were able to obtain forgivable PPP loans and other stimulus, and many actually profited nicely.

The pandemic has certainly reduced the project demand growth rate for senior housing for years to come because of increased deaths, and frankly, the stigma that attached to skilled nursing in the early months of the pandemic. IRR expects over the next 12 months that seniors who were standing on the sidelines during the pandemic will start signing residency agreements at rates not seen previously,

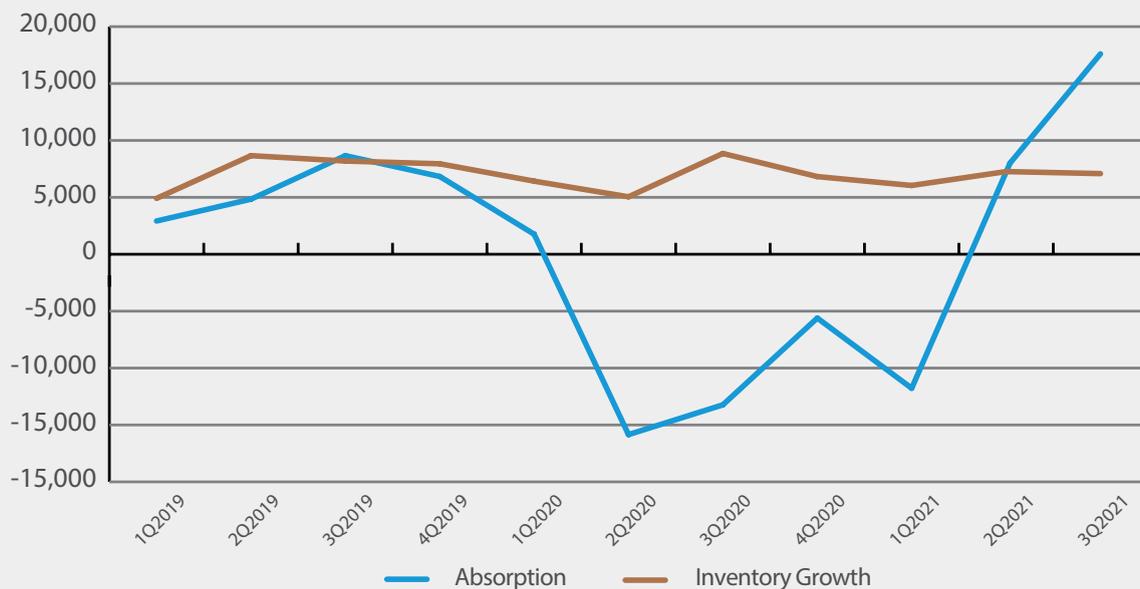
### SENIOR HOUSING OCCUPANCY TRENDS - PRIMARY AND SECONDARY MARKETS



resulting in extraordinarily strong absorption. Coupled with normal demand growth, occupancy levels and rate increases should exceed paces experienced between the recovery of the global financial crisis and the pandemic. Some of that revenue increase will be consumed by higher staff wages and other expense increases related to higher inflation. From a value standpoint, there also are indications that the Federal Reserve will begin moving interest rates higher in the coming year. Of course, higher interest rates can erode NOI gains through occupancy and rate increases.

Let’s take a closer look at supply and demand trends for senior housing, which includes independent living, assisted living, memory care, and CCRCs for primary and secondary markets, per NIC MAP Data Services. The supply within the primary markets includes 7,517 properties and 733,216 units as of 3Q 2021. As shown below, senior housing occupancy rates were declining even before the pandemic. The reason for that modest decline in 2019 was that inventory (supply) was growing faster than demand. In fact, the highest occupancy rate was achieved in the fourth quarter of 2014 at 90.0%.

### SENIOR HOUSING NET ABSORPTION & INVENTORY GROWTH



Between 1Q 2015 and 1Q 2020, inventory increased 23.7% (4.7% annually) and demand growth increased 18.0% (3.6% annually), according to NIC MAP Data Services. It also is important to note that inventory growth has been occurring unevenly throughout the country.

The pandemic has had a dramatic impact on occupancy levels. Measuring from the start of the pandemic in 1Q 2020 to the lowest point in 1Q 2021, the total number of occupied senior housing units declined 7.4%. Measuring by occupancy rate, which considers an increase in supply, the occupancy rate fell even further by 9.2%.

Now, what conclusions can be made for the coming year for senior housing? First, IRR expects the rebound in occupancy levels to be substantial in most markets that are not seeing large increases in supply. The increased

**IRR is forecasting that senior housing demand will increase sharply through 2023, with pent-up demand filling the void.**

move-ins, coupled with higher inflation, should be enough to push rents and service fees higher than seen in the past decade, if not longer. The rate increase may be easier to accept as future residents will be selling their homes at record price levels and tapping their assets in stock and bond portfolios that have experienced significant appreciation.

From a valuation standpoint, occupancy and revenues should see nice increases. Operating expenses are likely to increase beyond the 2.0 to 3.0% annual inflation levels that have been the norm for a number of years.

Nevertheless, NOI at most properties should increase. The big wild cards for valuation in 2022 will be interest rates and performance of the economy in general.

Several sales of new, stabilized senior housing properties in sub-urban markets of “major-league cities” commanded sub-5.0% capitalization rates during 2021 from institutional-type buyers.



## Economic Trends

Written By: Hugh F. Kelly, PhD, CRE

Consumer Price Inflation  
 Source: US Bureau of Labor Statistics

Risk Premium in Mortgage Rate – All Assets  
 Source: Hugh Kelly Real Estate Economics. Data: ACLI mortgage rates for office, apartments, industrials, and retail (weighted average) minus US Treasury rate for 7-year constant maturity securities

Abundant Capital Supporting Markets  
 Source: NCREIF Detailed Reports, Market Indexes Tables; Normalization to 1Q2017 by Hugh Kelly Real Estate Economics

ASCE Report Card  
 Source: Infrastructure Bill: www.whitehouse.gov; American Society of Civil Engineers 2021 Report Card

## Property Reports

### Office

Office Market Cycle  
 Source: Integra Realty Resources

Top Markets by Office Transaction Volume Based on YOY Percentage Change  
 Source: Real Capital Analytics

While Office Cap and Discount Rates Appear Tight, On Average, There is a Wider Spread for Downtown Assets than Suburban Properties  
 Source: Integra Realty Resources

Regional Rates Comparison  
 Source: Integra Realty Resources

### Multifamily

Top Markets by Multifamily Transaction Volume Based on YOY Percentage Change  
 Source: Real Capital Analytics

Market Cycle  
 Source: Integra Realty Resources

Regional Rates Comparison  
 Source: Integra Realty Resources

### Retail

Top Markets by Retail Transaction Volume Based on YOY Percentage Change  
 Source: Real Capital Analytics

Market Cycle  
 Source: Integra Realty Resources

Regional Rates Comparison  
 Source: Integra Realty Resources

## Industrial

Top Markets by Industrial Transaction Volume Based on YOY Percentage Change  
 Source: Real Capital Analytics

Market Cycle  
 Source: Integra Realty Resources

Industrial Investment: Buyers active coast to coast  
 Source: Real Capital Analytics, Industrial Trends Report, October 2021 year-to-date Sales Volume

Regional Rates Comparison  
 Source: Integra Realty Resources

## Hospitality

Written By: Jeff A. Greenwald, MAI, SRA, AI-GRS, ASA, FRICS, Senior Managing Director/Principal, IRR - San Diego

Demand and ADR Near Full Recovery in 2022 with Revpar Fully Recovering in 2023  
 Source: U.S KPIS, Indexed to 2019

## Specialty Reports

### Auto Dealerships

Written By: Daniel Kennard, Senior Analyst, IRR - Salt Lake City  
 Automotive Dealer Sales Breakdown  
 Source: NADA Industry Analysis Division

### Golf Courses

Written By: Cary A. Lannin, Director, IRR - Chicago

### Healthcare & Senior Housing

Written By: James K. Tellatin, MAI, National Practice Leader, IRR - Healthcare & Senior Housing

Senior Housing Occupancy Rate Trend, Primary and Secondary Markets, Q1 2019 - Q3 2021  
 Source: NIC MAP Data Services

Senior Housing Occupancy Net Absorption and Inventory Growth, Primary and Secondary Markets, Q1 2019 - Q3 2021  
 Source: NIC MAP Data Services

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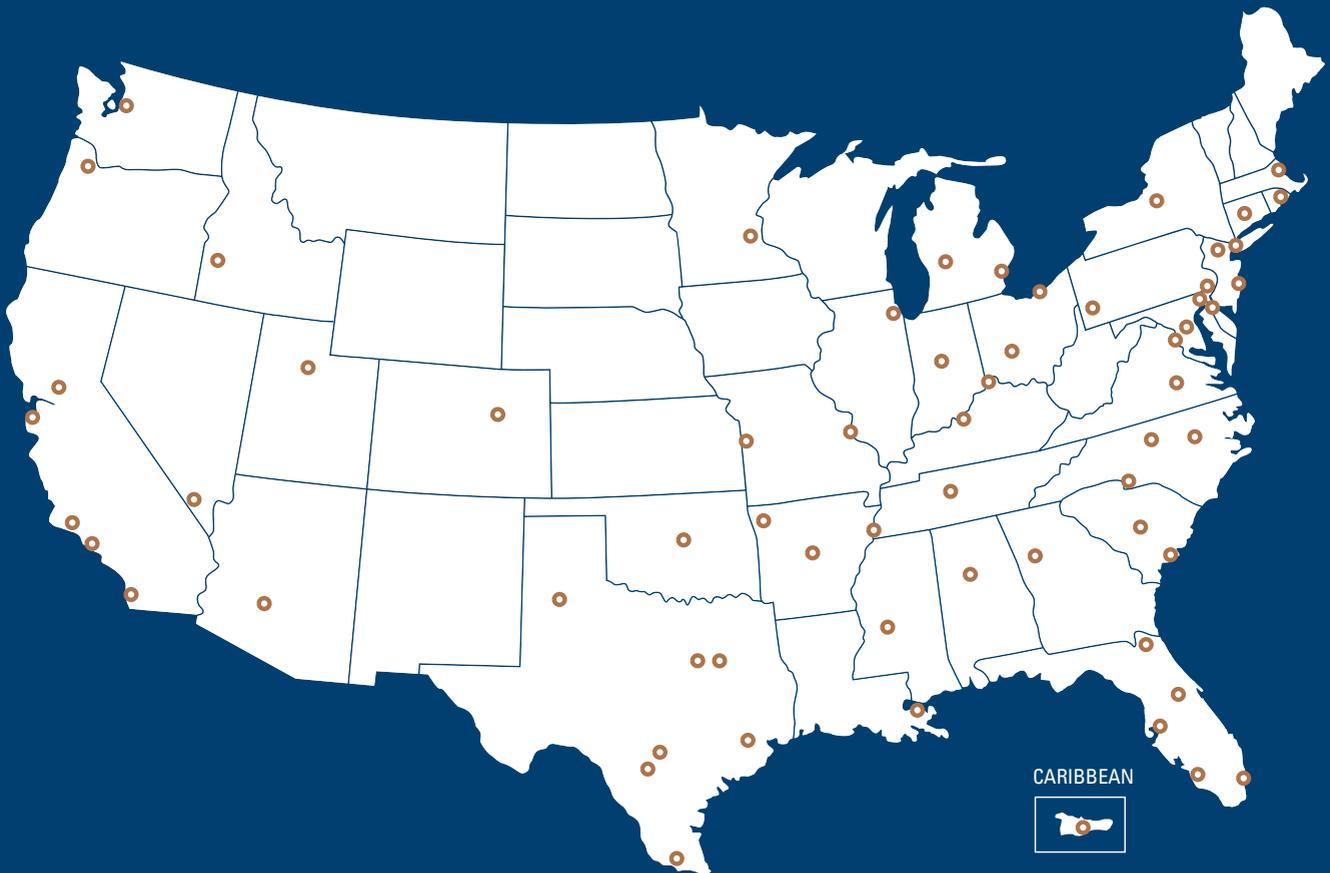
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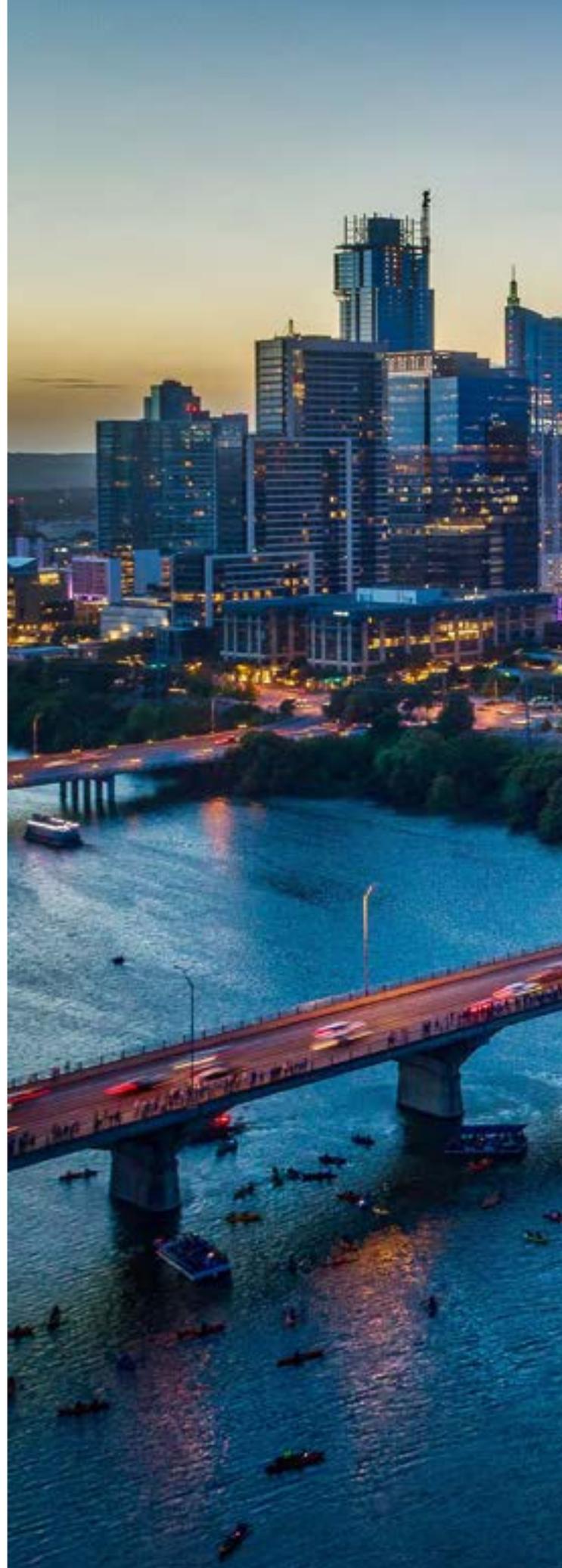
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