Five Key Indicators For The CRE Market

lending pandemic CRE

Summary: CRE lenders have a lot to manage these days. We provide you with five key indicators to help.

According to one study, sarcasm promotes creative thinking. So, what are you waiting for?

These days, however, it will take more than creative thinking to stay on top of the CRE market. KPMG reports that 68% of corporate CEOs expect to reduce their office space. In addition, new firms created during the pandemic have been designed around a remote workforce with a smaller physical footprint. Meanwhile, small businesses are still struggling as forbearances are coming to an end, creating further pressure on landlord cash flow.

Eric Rosengren, president and CEO of the Federal Reserve Bank of Boston, raised this very issue as a point of concern in September. CRE landlords will soon know for certain how many tenants renew and how many don't. Given these trends and barring any new tenants, vacancies are expected to increase.

To add to this situation, we have heard there are sophisticated CRE borrowers with loans coming due in the next six months who are selectively deciding to strategically default now. The thought is that they believe they will be later forgiven due to the unprecedented nature of the pandemic.

We wanted to share five market indicators to help you manage your CRE portfolio through these challenging times. Remember that your geographic area and community are unique and not all of these may apply.

1. **New virus outbreaks and hot spots.** It is likely these numbers will increase as we approach the winter months. Notice how this may further impact occupancy rates as workers may be sent home or told to continue working from home; companies may become more and more acclimated to a remote workforce.
2. **Unemployment.** Look at unemployment and expected job cuts for your communities. Some areas are doing better than others; it is unclear where the total employee headcount will land.
3. **Transition from urban to suburban.** With the flight of many from urban to suburban areas, there may still be opportunities for suburban CRE. Companies could find gathering in the suburbs part of the "new normal" and travel by car safer than mass transit.
4. **Municipal, state, and other government bankruptcies.** State and local tax revenues account for about 9% of GDP. Some municipalities' revenue relies more heavily on sales taxes, such as from their local restaurants. The Brookings Institution forecasts that state and local government revenue will decrease by $155B in 2020 or 5.5%. Those states, municipalities, and near government agencies that are ill-prepared may falter.
5. **Hospitality and travel.** The daily numbers have ticked up for air travel from a low of 85K in April to around 984K in September. Yet, the airlines need at least 1.6MM daily travelers to break even. Full-service hospitality properties typically require a higher level of occupancy to break even, compared to limited-service hospitality properties. As an indicator of the travel and entertainment segment, the continuing uncertainty around air travel could further impact hospitality.

There is a lot to manage with your portfolio during the pandemic. In simple terms, keep talking to your borrowers and following the key indicators that affect our industry. We will continue to help you with the latter.

COVID-19 IMPACTING YOUR RESERVE

The continuing uncertainty due to COVID-19 makes preparing for year-end and 2021 challenging. Our complimentary report, which has been updated to reflect the most current forecasts, can help. The Q3 report is now available. Simply download Reserve Insights: COVID-19 today.