Net Takeaways with Feller, Harf, and Team

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October 2024

Big Picture Takeaways

- **Inventory Imbalance: $24 Billion Today vs $9 Billion 24 Months Ago**
  With transaction volume stifled by higher rates, on-market inventory has surged, creating a significant imbalance that needs to be carefully managed by sellers in order to capture upcoming market opportunities.
- **Implied Interest Rates: Rates Today in the 6.10% Range vs. 7% for Much of the Year**
  While the Fed has initiated rate cuts, implied rates still reflect a cautious market. The extent to which these cuts lower borrowing costs for real estate investors will be key to unlocking deal flow.
- **July/August Transactional Activity Likely Bottomed**
  While the summer season is always the nadir of market activity, the summer of 2024 is likely to go down as the low point of closed transactions for the past decade. We believe that between pent up demand, and lower rates, deal-making will substantially increase into Q4 and 2025.
- **Market Engagement Increasing**
  Buyer and broker interest was markedly higher in September, with more phone calls, emails and OM downloads. Whether this translates into actual deals under LOIs is still an open question and will depend on realistic pricing and whether capital sources support renewed enthusiasm.

Market Commentary:

If there was a singular potential turning point after 24 months of a subdued NNN market, it would be the Federal Reserve's much-anticipated 50 basis point rate cut, bringing the target rate to 5%. Following nearly three years of tightening monetary policy to curb post-pandemic inflation, recent inflation data and softening jobs numbers have finally given the Fed the confidence to begin a return toward more normalized levels.

Within hours of the Fed's announcement, market speculation surged, with many hopeful that cap rates would soon fall sharply in response. However, we urge caution. While lower rates will certainly help the market, they are not a panacea. The last few years of elevated interest rates have severely diminished transaction activity, shrinking 1031 exchange capital by nearly 80% compared to the prior decade's average. This has resulted in a substantial increase in on-market inventory, with single-tenant retail properties rising from $9 billion in June 2022 to over $24 billion by June 2024.

Lower rates will drive positive momentum, but we don't expect a reversal in the upward trend of cap rates. The real effect will be an increase in transactional activity—likely up 20% year-over-year for Q4. Market participants should strategically position their on-market inventory to capture this resurgence in deal-making while being cautious not to price themselves out of potential opportunities.

OH WHAT A DIFFERENCE TWO YEARS MAKES...

Q2 2022 Q2 2024

CAP RATE CHANGE FOR NNN TENANTS: Q2 2022 VS Q4 2024