

The Net Takeaways

January 2019

Bold Predictions for 2019



Dear Clients -

With 2019 now upon us, we hope that you had an extraordinarily enjoyable holiday season with friends and family. In this edition of Net Takeaways, we explore some of the trends and dynamics which we believe will have real impacts on the Net Lease industry this year and make some prognostications for what we believe will be ahead. Thus, without further ado, our bold predictions for 2019:

Equity market & recessionary pressures increase demand for Net Lease assets and transactional volume grows by 15%

- With the recent volatility in global equity markets, including the NASDAQ's nearly 25% decline over the last three months, it seems clear investors believe the bloom is off the near decade-long rally in the stock markets
- With global growth slowing, vast political uncertainty, and potential recessionary pressures on the horizon, 2019 is shaping up to be a year in which investors seek safe haven in more stable asset classes
- The 10 Year Treasury in the last 90 days has moved from 3.25% to 2.75% as investors have moved vast sums of capital from equity to bond markets
- In an environment of equity uncertainty and cheap debt, we believe investors will find Net Lease assets more attractive than in 2017/2018, rallying the amount of transactional activity in the sector

Conventional financing will not be more expensive than 5.40%

- As noted above, the movement of the 10 Year Treasury has already made debt much cheaper than in Q3 2018
- While loan spreads are slightly elevated compared to 90 days ago, investors are still able to achieve roughly 220bps over the benchmark, and an all-in coupon of roughly 5% or better for conventional financing (65% LTV, 10-year term, 30-year amortization)
- With the economic pressures noted above, we do not believe the market is likely to see more than 30bps of upward movement in interest rates in 2019, keeping financing costs at attractive levels for investors
- 5% coupon rates for financing, projects to roughly 6.80% loan constants, and important line of demarcation for cap rates (cap rates below the loan constant result in negative leverage, which investors typically avoid in earnest)

Prevailing cap rates will increase no more than 25 basis points

- In tandem, the two above forces will result in a Net Lease market that slows the upward movement of cap rates that have been seen over the past couple of years
- We predict that prevailing cap rates for all segments of the Net Lease industry will increase no more than 25bps, with industrial increasing no more than 10bps

We welcome the opportunity to discuss with you in further detail and look forward to working with you in 2019!

Brad Feller
Managing Director
bfeller@stanjohnsonco.com

Isaiah Harf
Director
iharf@stanjohnsonco.com

Andy Gatchell
Associate Director
agatchell@stanjohnsonco.com

Blaise Bennett
Associate
bbennett@stanjohnsonco.com

Mark Lovering
Associate
mlovering@stanjohnsonco.com

Rachel Walz
Associate
rwalz@stanjohnsonco.com

Stan Johnson Company
303 East Wacker Drive | Suite 1111
Chicago, IL 60601