Rate Cuts May Not Be Enough to Drive CRE Prices Higher

The level of interest rates may no longer be the one-factor model for CRE prices

By Philippa Maister

CRE owners are likely to focus on net income preservation instead of interest rates in the coming year, according to CoStar Group’s January real estate update.

While high interest rates and speculation about whether/when the Fed will lower them have dominated the capital markets for months, CoStar expects they will not play as significant a role in the months ahead.

This view flies somewhat in the face of the ongoing demands from CRE investors for interest rates to be lowered to encourage deal-making and development. It comes even as markets speculate that the Fed appears set to start cutting rates in March. Right now, the market is pricing in six 25-basis-point rate cuts next year to a range of 3.75% to 4%, or a reduction of about 150 basis points from its current range of 5.25% to 5.5%, according to CoStar. The Federal Open Markets Committee expects a cut in the mid-to-upper 4% range by year end.

CRE prices were depressed because of high interest rates, a boom in post-Covid supply and a weak office market, CoStar noted. But lower rates alone may not boost prices as much as had been hoped. “As absorption continues to cool in tandem with a steady supply of new deliveries in 2024 and 2025, the level of interest rates may no longer be the one-factor model for commercial real estate prices that they have been,” CoStar noted.

CoStar called the anticipated interest rate cuts a welcome reprieve. The question now is whether they will be enough to drive up CRE prices and unstick the market.