# Stability Starts to Emerge in Commercial Real Estate

**However, that doesn't mean conditions like interest rates are getting easier.**

By Erik Sherman

The commercial real estate industry has been trying to sort out, and lobby for, where things are going. Goldman Sachs said office markets, maybe the most rattled part of CRE, have bottomed. Price increases could also indicate the start of a bottom according to a CoStar report. Then again, private CRE funds are facing pressure from investors and Federal Reserve Chair Jerome Powell recently said the central bank is in no hurry to raise rates.

A recent take by S&P Global Ratings tries to work out some of the conflicts in views and conditions. Start with the negative side. Interest rates remain high compared to those since the Global Financial Crisis, making refinancing harder. Complicating that issue are lower asset valuations and debt service coverage ratios that have increased, so lenders face more risk.

S&P says all this will continue until the Fed starts cutting rates, and the firm doesn't expect that to start happening until December 2024. Even if that happens, cuts will likely be a quarter percentage point at a time at a pace to see how the changes affect the economy. Some sources have told GlobeSt.com over the last half year that a 25-or-50-basis-point isn't likely to be a big motivation to investors.

At the same time, S&P says that stability has started to emerge in CRE markets. Even as they maintain 24% of REITs as having a negative outlook, that has more to do with the office sector. Bad enough, but not fundamental issues with REITs themselves. There have also been better performance and stronger balance sheets in healthcare- and retail-centric REITs. Outside of office, REIT net operating income has slowed but still positive. Their rating distributions approach 60% BBB or higher, meaning institutional grade. Two-thirds of them have a stable outlook and another 8% are positive.

Single-family housing has seen challenges. However, residential property demand has been "resilient" and homebuilders' sales and margins have stayed relatively strong even as mortgage rates are close to 7%. Multifamily has also seen strain with increased inventory and slowing rent growth. That could become a problem for lenders, who increased exposure to multifamily to offset problems with office. The two property types make up about 60% of lenders' portfolios, so could provide problems. At the same time, lenders build credit loss reserves and they will probably "remain selective with originations and focus on preserving liquidity."

In addition, sales and leasing activity has begun to stabilize and property management companies see "steady performance." And then, 83% of building materials businesses are stable with an additional 10% positive.

Overall, while many conditions are challenging, the overall look across different aspects of CRE are stabilizing, meaning better prospects in the future.