@@HADDOW'S REAL NEWS

QUARTERLY MARKET INSIGHTS

FOURTH QUARTER 2017

THE GREATER RISK

The mature phase of a real estate cycle usually breeds excesses that tilt the market toward oversupply. When good times roll, the result is often irrational exuberance and lack of restraint. An abrupt transition can then occur, particularly if there is a demand contraction.

We are in the ninth year of an economic expansion that lifted a depressed real estate market and has set it afire. The beauty of this cycle is that it has been driven by real demand, while the supply side has been reasonably in check. Clearly, apartment and industrial development have soared, but so has absorption. The office and hotel sectors have expanded only modestly, but rent and room rate growth have been solid. The retail market faces unique challenges from e-commerce, yet two shopping centers have recently sold at prices in excess of $600 per square foot. Atlanta's single-family housing market has bounced back but is not experiencing the rampant development of past cycles. Most importantly, the capital markets have exercised restraint.

The greater risk of undoing today's good times is not the actions of local market participants so much as external forces. Three things stand out. First, the stock market's fantastic run has provided newfound wealth, some of which could produce an undue stimulus to the real estate sector. The Dow Jones Industrial Average has advanced 30 percent in just the past year, which could lead some investors to hedge their bets by diversifying some assets into real estate, particularly given meager bond yields. Second, the Trump administration's efforts to deregulate industry and reduce taxes could unduly stimulate the economy, producing near-term benefits but long-term consequences. Remember what happened after the Glass-Steagall Act was repealed in 1999. And third, a heightened risk of military conflict is a growing threat to our prosperity.

In short, things are certainly good right now, but change is the one constant in real estate. Factors beyond our control sometimes redirect the economy, most notably the Arab Oil Embargo of 1973. The savings and loan meltdown, dotcom bust, and sub-prime mortgage crisis were more of our own making. When things seem too good to be true, like the stock market's surge, it often proves out. Hopefully, we have learned from the past and will watch for excesses and aberrant behavior that might turn the tide.

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CONTINUED

FOURTH QUARTER 2017

THE SURGING LOFT OFFICE MARKET

Loft office is no longer a niche product in Atlanta, having evolved into a significant asset class that is now outperforming traditional office. Some simple statistics from Colliers International highlight this fact: rents at loft office projects grew 62.4 percent from 3Q2013 to 2Q2017, compared to rent growth of 22.4 percent for Class A office buildings in metro Atlanta. Even more dramatic is absorption. In the first half of 2017, loft office accounted for 16 percent of total office absorption, despite only comprising two percent of total supply. Recent investment sales activity provides further validation of the product's appeal. Origin Investments, a private equity firm from Chicago, recently purchased Puritan Mill and Ellsworth Office Lofts, and Preferred Apartment Communities reportedly has Armour Yards under contract for around $350 per square foot.

RECENT ENGAGEMENTS

A local real estate operator hired our firm **to analyze the future investment potential of a shopping center** the group owns in Savannah. Due to the changing dynamics in the retail industry and the nature of the businesses located in the shopping center, the owner wanted objective advice regarding the optimal investment strategy moving forward. We analyzed the current potential value of the shopping center, prospects for vacant suites, long-term viability of the anchor tenants, and redevelopment potential of the site.

In 2016, we were hired by two families that owned adjoining income-producing properties in the urban core. We weighed the income stream against the merits of potential redevelopment of both properties in order **to help formulate the optimal investment strategy** for each family. In Spring 2017, we were hired by both families to market the properties for sale. Two of the three parcels sold at or above the recommended pricing, while the third property is still being marketed for sale.

A family that owns one of the largest remaining undeveloped residential tracts (263 acres) in Cobb County engaged our firm **to evaluate the property's highest and best use** and to formulate a game plan. We worked in conjunction with a land planner to fully understand the property's unique physical attributes. Several concept plans were prepared for the property to understand the economic implications of different development scenarios, and an investment strategy was recommended.

To monitor key economic and housing indicators, please visit our website. As always, your thoughts and feedback are encouraged.

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