

Rough road to recovery

by Brian Brus

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Stephen Blank with the Urban Land Institute.
(Maïke Sabolich)

OKLAHOMA CITY – Real estate developers in Oklahoma and nationwide can take some comfort in the apparent trend of economic stabilization, Urban Land Institute fellow Stephen Blank said, but demand hasn't matched available capital yet.

So be patient and build liquidity, he told attendees at the Commercial Real Estate Council's annual forecast conference in downtown Oklahoma City.

"For 2012, the industry will face a continuation of what amounts to be a long grind, where returns for the best properties level off, and commodity real estate continues in a limbo-like world of nonrecovery," he said. "We have been saying for several years that this recovery would not be easy, and in fact, it looks more like an endurance contest."

Blank visited from New Jersey, where he works as a researcher on the popular Emerging Trends industry forecast report series. His presentation was succeeded by Mark Beffort, president and CEO of Grubb & Ellis Levy Beffort, who shared his ideas on the local market.

Both men said Oklahoma City is on the cusp of national recognition, and the only reason to fall short of the top market lists is a matter of perception. Neither Beffort nor Blank offered any ideas on how to break through.

The current economic recovery isn't following the model of typical past recoveries in the United States, as more businesses are finding ways to use less space and reduce their overhead, Blank said. Investment capital hasn't been making its way into real estate, except for the multi-unit housing apartment sector. And related to that, Blank said he expects that once home sales start to pick up, the trend will be for houses to be turned into rental units.

"For real estate investors, it means declining return expectations," he said. "How much you make going forward will depend on when, and where, you've invested. If you invested in 2009 and 2010, when we said you should have, in the prime gateway markets, where we said you should have, it's time to take some chips off the table. More recent investments, in core-style properties in the best markets, may be able to provide decent, income-oriented returns, but not much more. We don't see much in the way of appreciation in 2012, or 2013 for that matter.

"Legacy, opportunistic investments, where investors overleveraged, will be wiped out; it's just a matter of time before lenders, and borrowers, start to take their losses," he said.

Blank said that while interest rates are still being held low, now is a good time to lock in long-term debt of about 10 years. On the other hand, developers are going to prefer occupancy contracts of less than 10 years to allow flexibility as the market strengthens.

Because investors are starting to look for better yields in secondary markets, now would be a good time for Oklahoma City to play up its economic strengths such as its low unemployment rate compared with the national average.

"The reality is, too much capital is chasing too little product, and is getting frustrated," Blank said. "Our core real estate markets really can't satisfy potential capital demand, and when too much capital overshoots the asset class, problems follow. That's what we saw four years ago, and we're seeing signs of it today in the gateway markets."

In terms of emerging markets or interests, Blank and Beffort both said cities with greater walkability ratings are drawing more development attention lately, and Oklahoma City is encouraged to continue improving its mass transit systems as well.

Beffort said Oklahoma City's downtown properties continue to draw business occupants from the suburbs and low office vacancy rates will reflect that. He said residential properties are still being leased rather than bought outright, which reflects a delay in changing culture and perspective.

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