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CORE PROPERTY VALUATIONS IN A SHIFTING MARKET CYCLE

INSIGHTS

Author : Patrick T. Craig, MAI, MRICS
Managing Director, Real Estate

The commercial real estate landscape is experiencing a fundamental recalibration. The dialogue has shifted decisively from cyclical adjustment to structural transformation. Core property values are no longer governed solely by traditional capitalization rate movements and macroeconomic headwinds; they are being redefined by profound divergences across asset quality, technological obsolescence, and capital access.

1. The Macro-Valuation Divergence: Core vs. Secondary Capitalization Rates

The post-peak interest rate environment has forced a rigorous re-examination of yield requirements across core asset classes. While headline inflation has shown signs of stabilization, the cost of capital remains structurally higher than the ultra-low regime of the previous decade.

The Flight to Quality: True core assets—those boasting prime locations, institutional-grade sponsorship, and superior sustainability metrics—continue to command resilient pricing, albeit with recalibrated yield expectations. Cap rate expansion has been highly bifurcated.

Secondary and Tertiary Compression: Properties lacking modern building systems or energy efficiency face widening yield spreads. Institutional capital is heavily penalizing assets that lack the flexibility to adapt to modern tenant demands, leading to uncurable functional obsolescence in lagging formats.

2. Sector-Specific Core Valuations: Office, Retail, Industrial, and Multifamily

Evaluating core property values requires distinct, asset-class-specific underwriting lenses as structural and operational shifts play out across primary sectors.

Office: The bifurcation within the office sector is extreme. While commodity and poorly amenitized suburban or secondary urban stock suffer from debilitating occupancy losses and severe valuation markdowns, prime trophy assets with state-of-the-art ESG compliance, touchless access, and robust tenant amenity packages are stabilizing. However, elevated tenant improvement (TI) allowances and leasing commissions continue to weigh heavily on net cash flows and overall valuation metrics.

Retail: Core retail has demonstrated surprising resilience, anchored by disciplined new supply and strong performance in necessity-based grocery-anchored centers and high-foot-traffic urban high street locations.

Underwriting focuses heavily on retailer sales-per-square-foot metrics and omnichannel fulfillment compatibility, with institutional capital favoring centers that serve as local distribution or pickup nodes.

Industrial: Following a period of hyper-growth, the industrial sector has transitioned into a more normalized, highly selective valuation environment. Demand remains solid for well-located logistics facilities near major transit corridors, but investors are increasingly scrutinizing clear heights, truck court depths, and power supply adequacy. Functional obsolescence is beginning to penalize older, multi-story, or functionally constrained warehouse stock.

Multifamily: Core multifamily pricing continues to navigate the crosswinds of robust underlying demographic demand against a wave of new supply deliveries in select sunbelt and coastal submarkets. Valuation models are highly sensitive to localized supply pipelines, escalating insurance and property tax expenses, and shifting rent-growth assumptions. Well-located, institutional-grade assets with proven resident retention remain favored safe havens.

3. Income Approach Realities: Revenue Sustainability vs. Expense Pressures

Valuation models under the Income Approach are under intense scrutiny as expense inflation meets pricing power limitations.

Operating Expense Inflation: Insurance, real estate taxes, and specialized maintenance costs have escalated significantly. In many markets, revenue growth has not kept pace with these operational creep factors, compressing net margins.

Lease Structures and Credit Quality: Shorter lease terms and tenants' demands for operational flexibility mean that underwriting must carefully distinguish between real estate value and Business Enterprise Value (BEV), particularly in operation-intensive properties. Institutional investors are placing a premium on long-term, high-credit tenancy that can withstand macroeconomic volatility.

4. Strategic Implications for Real Estate Valuation

For investors and fiduciaries preparing for Q4 portfolio marks and 2027 deployment strategies, the takeaway is clear: standardized index assumptions are no longer sufficient.

Accurate appraisal work requires granular, asset-level analysis that accounts for localized supply-demand dynamics, replacement cost realities, and specialized technological utility. As we look ahead, bridging the gap between historical comparable sales and forward-looking operational realities will define successful valuation practice and portfolio outperformance.

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