CION INVESTMENTS

A Guide to Commercial Real Estate

When it comes to real estate investing, commercial real estate is probably the most well-known and traditional way to get into the game.

But what is “commercial” real estate? The asset class is confusing because it includes categories that span a wide variety of usage. Office buildings, retail stores and multi-family housing all fall into the commercial bucket.

And commercial real estate is growing despite the headwinds (more on this later). In fact, U.S. commercial real estate investment volume increased by 45% year-over-year in Q1 2022 to $150 billion.[1]

In this primer, we’re going to dive into the 101 of commercial real estate.

WHAT CLASSIFIES AS COMMERCIAL REAL ESTATE?

Like its cousin, residential real estate, commercial real estate has a number of different categories and ways to access the asset class. Investors are looking to generate income, portfolio diversification, and capital gains from the asset(s).

When it comes to asset categories, there are four common ones:

OFFICES

Office real state, the asset category that probably comes to mind when you think commercial, is defined as properties with at least 75% of the space built for offices. These buildings are often in larger metropolitan areas and typically include long-term leases from major corporations.

MULTIFAMILY

Whether it’s a stand-alone apartment building, or a development with multiple buildings, multifamily has seen strong growth over the past few years. A multifamily dwelling is defined as two or more units having shared “physical” elements, like walls, AC units, and more.

RETAIL

Whether you’re walking into the mall, a grocery store, your local CVS, or a big-box store, retail commercial real estate can be classified as buildings designed to cater to businesses that sell consumer goods and services.

HOSPITALITY

Hotels, motels, inns – hospitality commercial real estate includes structures that are built for short-term stays.

WHAT'S DRIVING COMMERCIAL REAL ESTATE TRENDS?

The last few years have been rocky for the commercial real estate market as the pandemic shifted long-established consumer dynamics and business and personal travel was curtailed. Remote work, shopping online, and moving out of big cities meant commercial real estate got hit hard in 2020-21. But those dynamics may be shifting back in its favor.

According to Moody's Analytics, multifamily vacancies hit 4.7% in the third quarter of 2021 – which are pre-pandemic levels. And while e-commerce is eating the world, it's domination may have been overblown according to J.P. Morgan, as people still want to eat out and shop in public.

The key thematic areas shaping commercial real estate into the future include things like updating building infrastructure, amenities, technology, and affordability. While people want better infrastructure and technology, this impacts the affordability of commercial real estate, and with real estate costs rising in general, this means the verdict is still out for certain categories within commercial real estate.

HOW DO YOU GET STARTED?

Similar to other types of real estate, there are generally two ways to get involved:

DIRECT INVESTING

This is essentially purchasing a property outright or joining with others to purchase a property or properties in a partnership framework. Investing directly has the potential for rental income and capital appreciation.

INDIRECT INVESTING

Usually in the form of a REIT – A Real Estate Investment Trust. A REIT is a vehicle that owns, operates, or finances real estate or real estate-related assets. REITs combine the capital of numerous investors, allowing for lower investment minimums.

WHAT ARE THE RISKS?

Any investor should carefully consider the risks associated with investing, whether the strategy suits your investment requirements, and whether you have sufficient resources to bear any losses which may result from an investment. There are a few risks common to real estate:

- **Market Risk** – The strategy is subject to normal market fluctuations and the risks associated with investing in markets. Therefore, the value of your investment and the income from it may rise as well as fall, and you may not get back the amount originally invested.
- **Property Risk** – Property is a specialized sector that may be less liquid and produce more volatile performance than an investment in other investment sectors. The value of capital and income will fluctuate as property values and rental income rise and fall. The valuation of property is generally a matter of valuers' opinion rather than fact. The amount raised when a property is sold may be less than the valuation.
- **Liquidity Risk** – Any investment may make investments or hold positions in markets that are volatile, and which may become illiquid. Timely and cost-efficient sale of positions can be impaired by decreased demand and/or increased price volatility.

Commercial real estate can potentially provide income and portfolio diversification away from equity and bond markets. It's important to consider the risk when investing in alternatives, and speaking to a financial professional may be advisable.

Footnote

1. CBRE: U.S. Capital Markets, Q1 2022

The information contained within is for educational and information purposes ONLY. It is not intended nor should be considered an invitation, inducement to buy or sell any security or a solicitation to buy or sell any security. The information is not designed to be taken as advice or a recommendation for any specific investment product, strategy, plan feature or other purpose in any jurisdiction, nor is it a commitment from us or any of our subsidiaries to participate in any of the transactions mentioned herein. Any commentary provided is the sole opinion of the author and should not be considered a personal recommendation. This is also not intended to be a forecast of future events nor is this a guarantee of any future result. Both past performance and yields are not reliable indicators of current and future results. Information contained herein was obtained from third party sources we believe to be reliable; however this is not to be construed as a guarantee to their accuracy or completeness. Observations and views contained in this report may change at any time without notice and with no obligation to update.

All investments carry a certain degree of risk, including possible loss of principal and there is no assurance that an investment will provide positive performance over any period of time. There are specific risks associated with investing in various types of financial assets and in different countries. The information contained within should not be a person's sole basis for making an investment decision. One should consult a financial professional before making any investment decision. Investors should ensure that they obtain all available relevant information before making any investment. Financial professionals should consider the suitability of the manager, strategy and program for their clients on an initial and ongoing basis.