There's a lot of work to do for REITs in 2017. There are opportunities to be found—but they won't necessarily come easy, or without accompanying challenges. So say senior officers of real estate investment trusts (REITs) surveyed recently by KeyBank Real Estate Capital.

We solicited their views on opportunities and risks that may affect their business in the coming year. Survey participants are keeping an eye on several issues that could pose threats to performance, but overall the picture they paint is one of cautious optimism.

Respondent firms represent a cross-section of the REIT sector. More than 70% of responses came from REITs that are publicly traded, and 16% have investment-grade ratings, while the others are not rated. All participants own and control at least $500 million in assets, and more than half have portfolios totaling in excess of $2 billion in assets.

The survey included REITs that invest in every major property type and additional property types, such as student housing, self-storage, data centers, manufactured housing, and healthcare. Many firms reported investment in multiple property types.

The greatest number of responses came from REITs that invest in retail properties, followed by healthcare and hotels.

When asked about their level of optimism or pessimism on the fortunes of the market this year, 63% said they are somewhat optimistic and 6% said they are very optimistic. All other respondents said they are neither particularly optimistic nor pessimistic overall. It's a good sign for the market that there is no single issue causing all REIT executives to lose sleep; although there are plenty of challenges ahead, the consensus forecast is partly sunny rather than partly cloudy.
The number-one challenge for nearly a third of respondents is the intense competition for acquisitions that has characterized the commercial real estate market for several years. This might be viewed as a good problem to have, because it’s an indication that investors continue to believe in the sector.

However, too much money chasing acquisitions creates the risk that prices may outpace fundamentals like occupancy and rent growth. One-quarter of REITs view market fundamentals as the biggest concern to watch, and 6% are worried about a real estate or financial bubble in the near future.

More good news for the sector is that only about 12% of REIT executives view rising interest rates as the biggest threat to the sector. Historically, REIT stock performance has suffered when investors are concerned about interest rates, and the survey was conducted just days before the U.S. Federal Reserve approved a one-quarter-point increase in its target funds rate—the first such increase in a decade. The Fed’s move was widely anticipated, so it’s gratifying to note that very few REIT executives expect the rate increase to dramatically affect their business.

The 23% who cited “other” may have no single overriding concern, or may be focused on issues specific to their property type; for instance, retail REIT executives could be worried about the rise of online shopping, while leaders of office REITs may be watching the shift in tenant demand away from traditional CBDs.
Approximately 69% predict that market fundamentals in 2017 will perform about the same as 2016. Another 19% see the market improving, while only 6% believe it will deteriorate.

Half of REIT executives see their acquisition volume holding steady over the next 12 months, and another 19% expect volume to increase by 5% or less. A quarter of respondents are planning to acquire more, with 12.5% looking for volume to increase 5-10% and an equal number aiming higher than 10%.

The majority of surveyed REITs—56%—anticipate no change in their disposition volume in 2017 compared to 2016. About one-third expect to increase dispositions to some degree, while 13% said they will sell less this year than last.

More than 37% of REITs expect to increase their development pipeline in 2017, although most executives predict only a modest uptick. Less than 13% see development slowing down, but within that smaller group deal flow is expected to drop by more than 10%. Half of all respondents anticipate no change in their pace of development; not surprising, since many REITs don’t engage in development.
REIT executives aired their concerns in their responses to the question, “What keeps you up at night?” There was no one issue that emerged as a major threat to the sector; rather, executives’ fears often reflected their own market position or property focus. For example, some respondents discussed the uncertainty of healthcare reform and fluctuations in government reimbursement levels—issues that are important to healthcare and seniors housing properties but not to most other property types.

A retail-oriented REIT executive expressed concern over the fast-paced change in customer demand and performance standards. Other issues that some executives are watching carefully include stock price changes, government regulation, the state of the economy, and interest rates.

REIT leaders tend to view lenders as solution providers rather than simply capital providers. More than 40% said they would like to see their financial partners offer more ideas for equity, debt, and M&A opportunities. In terms of the overall REIT market, 45% foresee lenders becoming more aggressive than last year, while 22% predicted lenders will be less aggressive and 30% see little change in the coming years.

The bottom line: a REIT’s ability to rise to these challenges, and recognize complex opportunities, will define whether the future is sunny or cloudy in 2017.

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