

***Introduction to Commercial  
Property Markets***

RE 619  
Urban Land Development  
Dr. Longhofer

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***Boring Administrative Stuff***

- The syllabus is available on the course web site
  - <http://webs.wichita.edu/longhofer/re690.htm>
- Please update your e-mail forwarding and phone number on MyWSU
  - <http://mywsu.wichita.edu/cp/home/loginf>




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***Real Estate Markets***

- To understand how real estate values are determined, it is important to recognize that real estate transactions actually occur in two distinct but interrelated markets
  - In *real estate space markets* households and businesses buy and lease land and buildings in which they will live and work
  - In *real estate asset markets*, investors buy and sell the rights to future cash flows that real estate will generate from the users in the space market
- Rents and prices for real estate are influenced by factors in both of these markets

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***Real Estate Space Markets***

- There are a number of fundamental physical and economic characteristics of real estate that cause real estate space markets to differ from most other product markets
  - These characteristics ultimately affect how existing space is used and whether new space is developed
- By far the most important characteristic of real estate is its *fixed location*
  - Most every important characteristic of real estate derives from its fixed location
  - As a result, *all real estate markets are local*

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***Real Estate Space Markets***

- Because real estate cannot be moved, each parcel of real estate is *unique*
  - Only one piece of land occupies the confluence of the Big and Little Arkansas Rivers
  - A commercial office building in downtown Wichita is different from an identical building in downtown Manhattan
  - As a result, real estate in a particular area for a particular use is scarce despite an abundance of land
  - In addition, searching for real estate and gathering information about it is costly

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***Real Estate Space Markets***

- Finally, the fixed location of real estate also means that land uses are *interdependent*
  - Spillover effects are common in real estate
- These characteristics imply that it is misleading to talk about a single “real estate space market”
- Instead, space markets are segmented by
  - Geographic location
  - Property type
  - Use of the property or quality within a type

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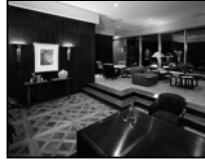
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### ***Commercial Office Markets***

- *Class A* office buildings command the highest rents because of high quality, excellent amenities, and prestigious tenants and location



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### ***Commercial Office Markets***

- *Class B* office buildings are generally high-quality buildings that don't have certain amenities or otherwise lack the "wow" factor



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### ***Commercial Office Markets***

- *Class C* buildings still offer cost-effective, usable space, but may have significant functional obsolescence or be in less-desirable locations



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***Commercial Office Properties***

- IREM lists 12 fundamental criteria for classifying office buildings:
  - Location
  - Ease of access
  - Prestige
  - Appearance
  - Lobby
  - Elevators
  - Corridors
  - Office interiors
  - Tenant services
  - Mechanical systems
  - Management
  - Tenant mix

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***Retail Space Markets***

- Retail properties are segmented by quality or class as well as geographic location
- Shopping centers are also often categorized by their size or intended market area

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***Retail Properties***

Shopping Center Type	Size in Sq. Ft.	Anchor Tenant	Market Area Population
Neighborhood center	30,000 – 100,000	Supermarket or drugstore	1,000 – 2,500
Community center	100,000 – 300,000	Junior or variety department stores	40,000 – 150,000
Regional center	300,000 – 750,000	One or more full-line department stores	150,000 or more

Source: *Shopping Center Development Handbook*, ULI

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### ***Retail Space Markets***

- *Neighborhood centers* are generally small, strip centers that serve a close-by resident population (5- to 10-minute drive)
  - Often “anchored” by a large grocery chain or drugstore



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### ***Retail Space Markets***

- *Community centers* are essentially larger versions of neighborhood centers that serve a larger market area (10- to 15-minute drive)



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### ***Retail Space Markets***

- *Regional and super-regional centers* are large, often enclosed, centers with one or more major department stores as anchor tenants



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### ***Retail Space Markets***

- *Freestanding retail* stores are single tenant buildings
  - *Category killer* stores like Wal-Mart and Home Depot are frequently structured as freestanding retail buildings
  - Major shopping centers often have freestanding retail stores located on *pad* sites on the periphery of the lot
- *Specialty shopping centers* are characterized by a dominant image or theme
  - Old Town
- *Lifestyle centers*

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### ***Industrial Space Markets***

- Industrial properties include
  - Warehouses and distribution
  - Light manufacturing and flex space
  - Heavy, specialized factories



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### ***Industrial Properties***

- Although industrial properties are also classified by quality, they are more typically characterized by building type
  - Bulk warehouse
  - Office/warehouse
  - R&D
  - Office/tech
  - Light manufacturing and “flex” space
  - Traditional industrial (plants & factories)

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### *Residential Space Markets*

- Single-family residential may be either owner-occupied or renter-occupied



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### *Residential Space Markets*

- Similarly, multi-family residential properties include apartments, condominiums, and coops



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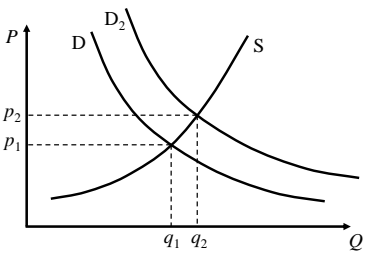
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### *Classical Model of Supply and Demand*



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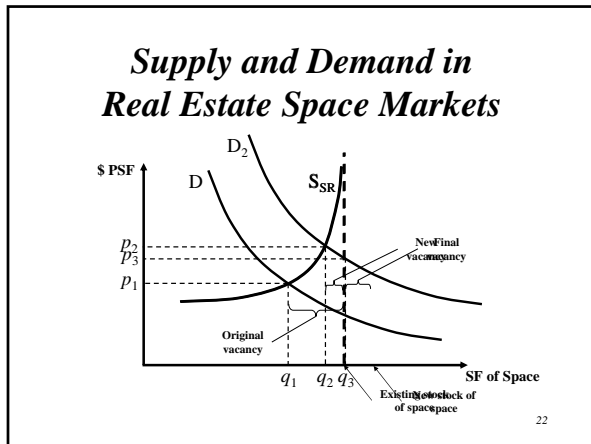
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### *Summary: Market Response to an Increase in Demand*

- Intensity of use of existing properties will increase, lowering vacancy rates
- Prices and rents of existing properties will rise
- If the change is perceived as long term or permanent, new development and conversion of property from other uses will increase the supply
- Rents will fall, but remain higher than they were originally; vacancy rates will fall to a “normal” level

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### *Real Estate Asset Markets*

- Individuals and institutions often acquire real estate because of the cash flows it generates, not because they want to occupy the space
  - Investment opportunities in real estate include income properties, REITs, mortgage loans, and mortgage-backed securities
- As an investment, real estate must compete with other capital market assets
  - Real estate is attractive as an investment if, on a risk-adjusted basis, its expected return is greater than what the investor could earn elsewhere

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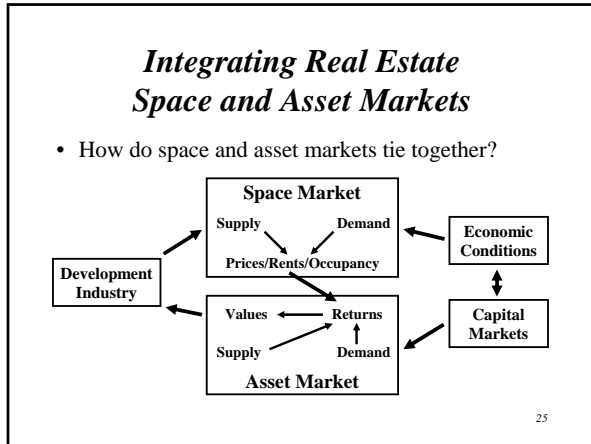
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