NAIOP
COMMERCIAL REAL ESTATE DEVELOPMENT ASSOCIATION

CAPITAL AND CREDIT AVAILABILITY

KEY POINTS

- Commercial real estate is an important driver of economic growth, contributing $2.5 trillion to U.S. gross domestic product, $881.4 billion in personal earnings, and supporting 15 million jobs, according to the 2024 NAIOP Research Foundation report.
- Adequate capital and credit are critical for properly functioning and efficient real estate markets, but credit availability for commercial real estate has become severely constrained.
- Banks are the largest source of financing for commercial real estate. But high interest rates, reduced property valuations, and an uncertain regulatory environment have contributed to reduced lending from banks.
- Federal Reserve regulations that unduly restrict the ability of banks to provide credit will exacerbate an already challenging economic environment for commercial real estate owners needing to refinance maturing debt.
- The economic impact will be felt by local communities, which rely heavily on property taxes as a source of revenue.
- Congress must exercise strong oversight over banking regulators to ensure that adequate credit is available to commercial real estate and the broader economy.

OUR POSITION

Credit availability for commercial real estate has become severely constrained, creating potential risks for the U.S. economy. Congress must exercise strong oversight of the Federal Reserve and other federal financial regulatory agencies to ensure that adequate credit is available for commercial real estate. Clear justification must exist for regulatory actions that increase capital requirements on banks and further limit their ability to lend.

Bank lending to commercial real estate is at historically low levels and trillions of dollars in maturing debt are coming due in the next few years. Major causes include rapid and steep interest rate increases that have raised borrowing costs, and remote work patterns that have increased vacancy levels and reduced the value of office properties. Of note:

- The Fed raised interest rates 11 consecutive times between March 2022 and July 2023. Interest rates rose from nearly zero in 2022 to over 5% a year later.
- Approximately 19.6% of office space in major U.S. cities was not leased at the end of 2023, an increase from 18.8% the prior year, the highest vacancy rate since 1979, according to Moody's Analytics.
- According to a report by the McKinsey Global Institute, the predicted loss in office property values in major global cities will be $800 billion by 2030, with an average loss of 26% from 2019 through 2030.

Commercial real estate loans exceed $6 trillion, with banks holding over 50%, according to the Financial Stability Oversight Council. The bulk of these loans were initiated at base interest rates near zero, but the current baseline federal funds rates are 5.25% to 5.50%. In the next two years, more than $1 trillion in commercial real estate debt will need to be refinanced at higher borrowing costs.

Regulatory uncertainty is creating additional obstacles. Banks have been under pressure from federal oversight agencies to reduce their portfolio of commercial real estate loans. Now, the Fed is moving to implement regulations proposed by the Basel Committee on Banking Supervision that would increase the capital requirements for banks with assets of $100 billion or more by an average of 16%, and 19% for larger banks. Increasing capital requirements on banks reduces their ability to provide credit.

Further restricting credit availability will increase defaults on maturing debt and hamper construction for multifamily and affordable housing, industrial, and other property types. The impact on many cities and localities of depressed commercial real estate markets will be profound. Local governments collected $581 billion in property taxes in 2020, or 30% of local general revenue according to the Urban Institute.

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