Parking Facilities: A Tight Space for Investment

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Parking represents a highly desired asset class in an evolving $30 billion industry[1]. To satisfy significant investor requests (both debt and equity), broker requests and appraiser requests for overall rate support for this asset class, JNL Parking and Parking Property Advisors partnered with Situs RERC to publish an inaugural analysis of parking facility capitalization (cap) rates for second quarter 2016.

Situs RERC, JNL Parking and Parking Property Advisors surveyed parking owners, investors, advisors, brokers, and appraisers across four regions of the U.S. These experts provided cap rates for parking facilities, as well as insight into the factors which determine both cap rates and the value of parking assets. In addition, information regarding parking investment conditions (e.g., risks to parking facilities, the current investment environment) was gathered.

Historically, the prevailing general market assumption has been that overall cap rates for parking facilities were higher than most other real estate asset classes due to the limited availability of parking assets and the traditional lack of long-term parking leases. However, those involved in the day-to-day parking business know that investor appetite is much greater than the overall market perception. In fact, quality parking investments rarely even get exposed to the open market because most parking assets are purchased off market. This lack of market exposure, as well as very few independent (stand-alone) parking facility transactions, were the impetus for conducting an investor survey to help gather cap rates for parking facilities.

It should be noted that parking facilities include both surface parking lots as well as parking garages. However, because surface lots are more adaptive, many investors often report cap rates based on the assumption that the space will eventually be repurposed. The end result is that parking facility cap rates primarily relate to parking structures/garages.

Survey results are depicted for separate seller and buyer perceptions (see table below), no distinction was made between first-, second- or third-tier markets for this asset class. Sellers were more aggressive and optimistic than buyers. The average

Parking Facility Capitalization Rates[1]

	Seller	Buyer
National		
Range (%)[2]	4.5 - 10.0	5.0 - 10.0
Average (%)[2]	6.3	7.0
West Region		
Range (%)[2]	4.5 - 8.5	5.0 - 9.0
Average (%)[2]	6.4	6.9
Midwest Region		
Range (%)[2]	5.0 - 10.0	5.5 - 10.0
Average (%)[2]	6.7	7.2
South Region		
Range (%)[2]	4.5 - 8.0	5.0 - 10.0
Average (%)[2]	6.0	6.9
East Region		
Range (%)[2]	5.0 - 8.0	5.0 - 10.0
Average (%)[2]	6.1	6.9

[1] This survey was conducted in first half 2016 and reflects estimated capitalization rates for this period.
[2] Ranges and other data reflect the central tendencies of respondents: unusually high and low responses have been eliminated.
Sources: Situs RERC, JNL Parking, Parking Property Advisors, 1H 2016.

[1] Source: International Parking Institute, "2013 Emerging Trends in Parking," May 2013.

cap rate was calculated nationally and for each region (i.e., East, Midwest, South, and West). Additional analyses were conducted using descriptive statistic methods (e.g., percent of totals, counts, ranges).

On a national basis, cap rates ranged from 4.5 percent to 10.0 percent, with average rates of 6.3 percent (seller response) and 7.0 (buyer response). These rates compare favorably to other asset classes. Among the four regions, the lowest rates were reflective of parking facilities in the South and the highest rates were reflective of parking facilities in the Midwest.

The overwhelming majority of participants (78 percent) indicated that the current parking market environment is strong. Interestingly, most parking assets were purchased with significant leverage; 84 percent of parking facility acquisitions were purchased with 50 percent or more in leverage. Only 16 percent of parking facilities are purchased with a majority in cash.

Parking facilities represent a valuable asset class with overall strong investor interest. From a cap rate standpoint, parking facilities compare favorably to other asset classes. Further analysis of parking facility sales is difficult due to insufficient reliable operating data, but with few market transactions, this data has been historically difficult to obtain. By introducing this survey, we are able to provide invaluable information on parking facility cap rates.

If you work with parking facilities and are willing to provide investment data, please email **surveys@rerc.com** with your interest in participating in our survey or visit **www.parkingcaprates.com** for direct access.

Current Market Environment is Strong[1]

	National
Strongly Agree	32%
Agree	46%
Neither Agree Nor Disagree	20%
Disagree	2%
Strongly Disagree	0%

[1] Respondents' reactions to the statement "Current market environment is strong."
Sources: Situs RERC, JNL Parking, Parking Property Advisors, 1H 2016.

Percentage of Parking Facility Acquisitions Financed by Cash

Percentage Financed by Cash	Percentage of Total
<25%	59%
25 - 50%	25%
51 - 75%	7%
>75%	9%
Total	**100%**

Sources: Situs RERC, JNL Parking, Parking Property Advisors, 1H 2016.

SITUS RERC'S RISK-ADJUSTED RETURN ANALYSIS

Today's CRE investment environment is ripe with opportunities and risks. Although there are bright spots, as will be discussed in this analysis, many investors see economic risks looming in the not-too-distant future that could impact the stability of CRE. This perception is rightfully causing participants to think long-term.

Total returns are comprised of capital returns and income returns. Income return can be thought of as net operating income (NOI) received, while capital return can be thought of as appreciation/depreciation in value of the asset.

Situs RERC is pleased to introduce a new analysis for the current issue of the *Real Estate Report*: a capital return performance metric (see "Capital Return Performance" table below). Capital return performance compares the current quarter (i.e., quarterly and 1-year trailing) capital return to 10 years of historical NCREIF capital returns. The analysis seeks to provide historical context to the current capital return performance. We focus on capital return because there is a greater range of returns over the past 10 years versus income return, which is not as volatile. A higher outperformed percentage indicates the percentage of time the current capital return is outperformed by historical capital returns.

The second quarter 2016 quarterly capital return performance for all property types was 0.84 percent, the lowest since first quarter 2010. The income return component was stable in second quarter, but at 1.19 percent, remained among the lowest results in the history of the NPI going back to 1978.

On the individual property-type level, trailing 1-year capital return performance over the past 10 years has shown that CBD office property returns were greater than current returns three-fourths of the time. In addition, most property types have historically outperformed second quarter 2016 trailing 1-year capital returns, with the exception of the neighborhood/community retail, industrial R&D and industrial warehouse sectors, which have been outperformed only 26.83 percent, 31.71 percent and 34.15 percent of the time, respectively (i.e., these property types are performing well as compared to the past 10 years).

The second quarter 2016 risk-adjusted return (RAR) metric results are similar to those from the previous quarter but with minor downward movement, primarily due to a slight degradation to National Council of Real Estate Independent Fiduciaries (NCREIF) returns. The NCREIF 1-year trailing return for all property types fell 120 basis points to 10.64 percent (see 1-Year Trailing Returns - 2Q 2016 table). Similarly, the neighborhood/community retail sector fell to second place with a 1-year trailing return decline of 179 basis points. The only shift in the rankings in second quarter 2016 was in the top two property sectors, with the regional retail mall sector topping out the rankings with a RAR metric of 1.4. The RAR metric is a ratio of return divided by standard deviation. As shown in the 10-Year Returns - 2Q 2016 table, NCREIF 10-year returns continued to underperform the current trailing 1-year return results. This is good news, as we are still in positive territory since coming out of the recession in 2010.

Over the past three to six months, investor sentiment and data suggest that significant value increases and capital gains may have peaked in the major metros. This has caused many to think that the industry

Capital Return Performance - 2Q 2016

Property Type	Quarterly Return	Outperformed by Historical Returns[1]	Trailing 1-Year Return	Outperformed by Historical Returns[1]
Regional Mall	1.07%	53.66%	6.85%	56.10%
Neigh/Comm	1.37%	29.27%	6.99%	26.83%
Industrial - Whse	1.65%	41.46%	8.06%	34.15%
Power Center	0.54%	63.41%	4.06%	51.22%
All Property Types	0.84%	75.61%	5.56%	56.10%
Industrial - R&D	0.63%	63.41%	6.58%	31.71%
Apartment	0.73%	70.73%	4.87%	65.85%
Office - Suburban	0.28%	73.17%	3.98%	56.10%
Hotel	-0.81%	78.05%	1.36%	51.22%
Office - CBD	0.82%	75.61%	4.84%	75.61%

[1] Capital return performance compares the current quarter (i.e., quarterly or 1-year trailing) to 10 years of historical NCREIF returns and indicates the percent of periods the current return is outperformed by the historical returns.
Sources: Situs RERC, NCREIF, 2Q 2016.