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“The book-ends of demographics (Boomers and Millennials) will dictate the direction of real estate in the US and abroad” IRV

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## Introduction

By Lance W. Doré, FRICS, MAI

Like Lemmings to the Sea – whether this is Fact or Fiction, Myth or Reality – the markets are in a state of automation. But what lurks around the corner is the big question.

Markets are strong across all property types, but are they really? Are some fundamentals being overlooked that might lead to the next recession?

This is the Lemming Dilemma – is everyone jumping off the cliff playing follow the leader, or are there really legs in the current recovery that will sustain the markets for a while longer?

There are hints of fractures in the global market that, taken individually, do not portray any impending adjustments, but taken collectively may be a harbinger of doubt.

Brexit has occurred. There is a sense in the UK that they are better off without the anchor of the other EU countries.

The US elected Trump with a Brexit synonymous “me first” platform.

Puerto Rico is bankrupt.

PIIGS is still slowly recovering – and this is in a good global economy. What happens to PIIGS if there is a dip? Greece is still faltering. Portugal, Spain, Ireland and Italy are holding their own – for now. Are we heading to FIG (France, Italy and Greece) as the anchor holding down Europe? Will Spain Exit the EU?

The US is the preferred investment country to mitigate investor risk. Asian countries are strong and Latin countries are stable. The Lemmings march on.

## Looking Around

According to Real Capital Analytics (RCA) global transactions of commercial property totaled US\$1.3 trillion in 2016, down 4 percent from 2015.

Transaction volumes were hindered by the uncertainty resulting from the Brexit referendum, the US presidential election campaign, and the lack of divestiture of assets.

Germany was the transaction leader in 2016 (at US\$60.2 billion) which surpassed UK (US\$59.9 billion) as the top transaction market in Europe.

New York (US\$17.77 billion) overtook London (US\$17.71 billion) as the top overall destination for cross-border capital and China became the largest market in Asia Pacific for income-producing asset with US\$36.6 billion.

Asia Pacific investment totaled US\$584 billion in 2016, which was 15 percent higher than 2015.

Investment in Japan (US\$29.2 billion) and Australia (US\$23.5 billion) in 2016 followed China in investment volumes.

According to the **Situs RERC 2017**, Europe's economy is stable, but likely in the late stage of the real estate cycle. CRE growth is expected to slow with opportunities in secondary and tertiary markets. Expect some clarity or volatility as elections occur in the Netherlands, France, and Germany. The results of the French election were a stabilizing factor when Macron was elected who favored the EU and majority in the Parliament. This bellwether implies stability.

Continued political instability will test the investment markets.

According to **PwC** and **ULI**, the global cities for real estate investment for 2017 are:

Canada	Europe	Asia Pacific
Montreal	Berlin	Bangalore
Toronto	Copenhagen	Bangkok
Vancouver	Dublin	Guangzhou
	Frankfurt	Ho Chi Minh City
United States	Hamburg	Jakarta
Austin	Lisbon	Manila
Charlotte	Lyon	Mumbai
Dallas/Fort Worth	Madrid	Shanghai
Los Angeles	Munich	Shenzhen
Nashville	Stockholm	Sydney
Orange County		
Portland (Or)		
Raleigh/Durham		
San Francisco		
Seattle		

Of interest in the list of top cities is the focus on urban centers with a high concentration of technology and finance with available public transportation and services. These will be the marching orders for future real estate investment.

There is a continued defining and influencing of the ongoing revitalization and expansion of live/work/play environments with both “Baby Boomers” and “Millennials” competing in the same sectors. This includes urban residential (apartment and condominiums) and discretionary travel (hotels).

“A global drift to domestic agendas was seen both as having the potential to kick start stalled economies but also risks upsetting finely balanced interdependencies between countries and regions.” **Emerging Trends in Real Estate | PwC & ULI**



## Looking Forward

**Game Changers – 2017** include the impact of AV (Autonomous Vehicles) and Drones. How does this impact real estate?

The consensus is that AV will directly impact three main areas of real estate investment and development; 1) less parking will be required for most new built projects. This will increase density when land does not have to be set aside for cars; 2) person centric will be the new model for planned development and mixed-use projects. In the past, especially in the United States, most development was car centric. This shift in development priorities will reshape the real estate landscape and put pressure on how architects, urban planners and developers plan for the future with AV's; 3) Infrastructure shifts from private to public. Private use of public streets will shift to public transportation for private use. This has been evident in other countries where public transportation has been entrenched in major cities around the globe including; New York, Berlin, Zurich, London, Paris, Tokyo, Singapore and

Seoul. But this final push of AV's may finally dislodge the real estate industry to adapt to an entirely new technology.

Drones may not have the same impact on real estate as AV's – but the industrial sector of real estate will likely gain traction as a result. The mantra will be distribution, distribution, distribution. The elements of real estate that can accommodate the requirements for "the last mile" will likely gain a significant advantage in the future.

In the immediate - the landmarks for 2017 that will have the highest impact on real estate include 1) uncertain economic growth in Asia, 2) Geopolitical uncertainty in Europe, and 3) Construction Costs increases. There are other flags waving - such as access to affordable capital and supply | demand imbalances, but the combined impact on current investment guidelines continues to be a flight to quality in a time of some unknowns. This is not the same as a downcycle but simply prudence in a changing market.

**What is likely?** Commercial real estate markets will maintain strong fundamentals in 2017, but at peaks that may not be sustainable. The opinion of the market participants is that the market is *fully-priced* and commercial real estate growth (if any) will be more measured in 2017 and could be flat.

Commercial real estate will likely serve as a hedge against rising inflation, however interest rates will increase and investors should be cautious and monitor their portfolios and lease positions. The signs of unknowns will increase risk with a corresponding decrease in values.

Overall, look for an uneven landscape in transaction volume that will vary with geography and property type. The best bets for property type are those that meet the demanding demographics – this includes apartments, entry level housing, industrial and hotels. Watch for office to reposition due to the "share space" and beware of retail, especially with big box orientation.

"Elevated uncertainty through much of the year, real estate capital flows have slowed, investment volume has pulled back and investment performance has cooled.

Encouragingly, financial markets appear to be adjusting and signs of distress are minimal." **PGIM Real Estate 2017**



## Highlights: Cities to Watch | Mexico

According to AFIRE (Association of Foreign Investors in Real Estate) The top five global cities for real estate investment are 1) **New York**, 2) **Berlin**, 3) **London**, 4) **Los Angeles**, and 5) **San Francisco**. These rankings reflect a mix a safety and growth.

According to the same study (AFIRE), the top five emerging countries are 1) **China**, 2) **Mexico**, 3) **Brazil**, 4) **India** and 5) **Chile**. These ranking reflect the top location for emerging real estate acquisitions. Like any emerging market the opportunity is greater than the risk.

The top gateway cities reflecting access to imports/exports and infrastructure include.

**Manhattan, NY** – has seen a resurgence in construction with rapid growth in TAMI (Tech, Advertising, Media and Information).

**Singapore** –strong diversification in healthcare, education, aerospace and biotech.

**London, UK** – re-invention of financial hubs for the EU's.

**Hong Kong, China** – repositioning into office for multi-national users and;

**Paris, France** –also reinventing itself and may be an alternative to EU financial centers.

Watch the trends in these core cities along with Vancouver, Toronto, Sydney, Mumbai, Dubai, Munich and Madrid.

### Highlight Mexico

Mexico's Commercial Real Estate has been enjoying impressive growth during the past 6 years. The Industrial, Office and Retail sectors have posted relevant gains, especially since the creation of the FIBRAS and other forms of Real Estate Investment Trusts.

The World Economic Forum established that Mexico ranks 68th out of 144 with respect to the Competitiveness and Infrastructure Index. This is typical for gateway and emerging cities to invest for the future in highways, railway, water ports and airports.

There is a new resurgence in Mexico, Central and South America countries.



## Headquarters

The Hub  
1010 University Ave.,  
Ste. C207  
San Diego, CA 92103

PHONE:  
(619) 933-5040

MOBILE:  
(619) 933-9450

E-MAIL:  
[info@irvaluation.com](mailto:info@irvaluation.com)

## IRV De México

3723 Birch Street, Ste. 7  
Newport Beach, CA 92660

U.S. PHONE:  
(949) 336-6688

MEXICO PHONE:  
(52.55) 1167-8213

E-MAIL:  
[info@irvaluation.com](mailto:info@irvaluation.com)



## We're on the Web!

See us at:  
[www.irvaluation.com](http://www.irvaluation.com)

## About the Authors



**Lance W. Doré, FRICS, MAI**  
Founding Partner / President  
International Realty Valuation, Inc.  
[ldore@irvaluation.com](mailto:ldore@irvaluation.com)

As a Founding Partner and President of International Realty Valuation, Inc., Lance W. Doré manages the operations of the firm. He is actively engaged in a myriad of valuation assignments involving a wide variety of properties, with special expertise in the valuation of energy facilities, conservation land, open space/ ranches, and litigation support to public and private clients.



**Oscar Franck Terrazas, FRICS**  
RICS Registered Valuer  
Founding Partner / Vice-President  
International Realty Valuation, Inc.  
[ofranck@irvaluation.com](mailto:ofranck@irvaluation.com)

As a Founding Partner & Vice President of International Realty Valuation, Inc., Oscar is responsible for all operations in México and Latin-America. He is actively engaged in real estate valuation and counseling and has performed valuations of numerous properties, with specialized experience in large portfolios.



**Hiroyuki Isobe, CRE, FRICS**  
RICS Registered Valuer  
Founding Partner  
International Realty Valuation, Inc.  
[hisobe@irvaluation.com](mailto:hisobe@irvaluation.com)

Hiroyuki is a founding partner of International Realty Valuation, Inc., and is responsible for all operations in Japan. He has been actively engaged in real estate valuation since 1978, and has served as a consultant on numerous city planning projects, feasibility studies, and market researches on behalf of the public sector and private developers.

## About IRV, Inc.

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