Commercial Real Estate Index tracks wide span of activity

by: Stan Austin, TEN editor

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The regional indicator reflects local developments and offers early insight into what might be on the horizon.

Seeing local news reports about office construction projects or driving past signs advertising vacant space provide only a glimpse of what is happening in the vast world of commercial real estate.

The CRE sector touches a wide span of activity that can provide insight into many economic trends such as community banking, construction activity, employment forecasts, infrastructure investment and land development. Activities in these areas and others have always been vital to understanding a region's economic condition but tracking them can be difficult to accomplish all at once. Besides the need to monitor conditions for various property types and local markets, many developments only become evident after some time has passed.

To present a more comprehensive measure with minimal lag, the Bank launched the KC Fed CRE Index in February. The index, which will be updated quarterly, was developed by Vice President, Economist and Denver Branch Executive Nick Sly and Research Associate Bethany Greene. In an *Economic Review* article introducing the index, Sly and Greene explained that the new tool "encompasses a broad range of related economic activities and financial considerations based on timely survey responses received from market participants across the Tenth Federal Reserve District."

The KC Fed CRE Index data for the first quarter of 2024, the *Economic Review* article, a "CRE 101" fact sheet, and related resources are available on the Bank's website. The new index joins the Bank's suite of regional economic indicators. Those products include the Agricultural Credit Survey, the Community Banking Bulletin, the Manufacturing Survey and Tenth District Beige Book reports.

What the index tracks and how

The KC Fed CRE Index synthesizes a broad set of conditions into a simple tracker that reflects local developments and provides early insight into developments that might be on the horizon. A positive value in the index indicates that CRE conditions are stronger than the long-run average, while a negative value signifies that activity is below the long-run average. The current release describes conditions for the previous quarter.

“It’s one simple number that describes conditions relative to historical norms,” Sly said. “That makes it very easy to understand a diverse and complex market.”

The index is based on information received from contacts spanning Colorado, Kansas, Nebraska, Oklahoma, Wyoming, western Missouri and northern New Mexico. The measure incorporates related economic activities and financial considerations across a variety of commercial property types, including retail properties, hotels, office buildings, multifamily housing and industrial space. Further, the index accounts for subsegments of each property type.

The index summarizes information about several aspects of regional CRE markets:

- Prices for existing CRE space
- Availability of existing CRE space
- New construction and development of CRE space
- New construction costs and materials prices for CRE space
- Financial conditions

Why the CRE Index matters

Sly said that business, community and policymaking leaders can look to the index for insight into key areas such as construction employment and CRE loan performance—important in a region where community banks have a strong presence and often have extensive commercial real estate lending portfolios. Commercial real estate also is closely watched because the sector is sensitive to changes in interest rates.

He added that the Kansas City Fed has a long history of broadly monitoring CRE trends across its footprint and that the KC Fed CRE Index advances that analysis by using a network of contacts to help identify factors in commercial real estate activity that might differ from one business cycle to another.

“Commercial real estate has many property types and looks very different across geographies,” Sly said. “You can go one mile down the road and see two very different outlooks for activity. There are so many market types and so many market segments that can all move in different directions. You have to talk to a lot of people and have broad engagement in order to track those market conditions.”

Regional focus

While the CRE is broad in its makeup and reach, the index reflects the regional economic landscape rather than be shaped by national factors.

"The need for industrial space versus office space, for example, depends entirely on the makeup of the regional economy," Sly and Green stated in their article. "Likewise, proximity to airports or travel destinations motivates investments in hotels and retail, while population density and the pace of regional development drive demand for multifamily housing separate from national trends."

Sly added that with the KC Fed CRE index, "People get to see what's happening in their market, whereas as a lot of the national headlines are about what's happening in big cities outside the Tenth District. It really is a regional tool."

Looking ahead

Sly and Greene noted that going forward the index could be helpful as leaders across the region face "structural shifts" that are unfolding in the CRE sector:

"Workplace habits have changed, altering the use of office and retail spaces and the geography of economic activity within cities. Supply chains for many industries are being reforged, altering the needs for warehouses and industrial space across locations. The KC Fed CRE Index may be a useful tool for tracking these developments in a timely manner and delineating the drivers of CRE activity amid these structural shifts."

Follow the KC Fed CRE Index and sign up for alerts.
