# The Pinkard Fund

## Investor Update July 2015

### Market Update For Q2 2015

What a difference 90 days, good weather and some positive job growth can do for the real estate market. The second quarter marked the first time in a few quarters that the office market showed positive absorption, at least DC and Northern Virginia did. A number of the online publications are calling this a market turn and suggesting that it is no longer a tenant's market. As one who is leasing a couple of buildings right now I beg to differ. The tenant brokers are still asking for the moon and the stars and the shirt off your back. What is significant, however is the increase in tenant activity (inquiries and tours) that is taking place. The combination of the reported turn in the market and the increased level of tenant activity will push tenants to move more quickly over the next year. Over the past two years there has been little incentive for tenants to act. Why sign a lease today when you can get a better deal tomorrow? But as the market bottoms and turns, tenant brokers will advise their clients to sign up now because they will not get better terms tomorrow. This leads to faster absorption, and ultimately, a landlord's market.

One sign that this may be taking place is that while lease terms have been really brutal for landlords, they haven't gotten much worse over the last 18 months. In fact, rental rates have gone up slightly in certain sub markets over that time period while concessions have remained high but stable. This is what happens at the bottom of the market when there is little new space delivered and the amount of A quality space slowly gets leased.

The apartment market is a whole other story. The supply of new apartments that delivered in 2014 and which are expected to deliver in 2015 and 2016 is unprecedented. At the same time over the last two years absorption of apartment units has been double the 10 year average. It is not unusual for absorption to spike when there is lots of supply, but market observers have been surprised at the resilience of this market. There is no question that the popularity of the urban life style among millennials and others has led to a secular change in the balance between single family homes and apartment living. The real question is how deep is this market? As far as rental rates are concerned they have generally remained flat rather than gone down as predicted. The key is to deliver the right product in the right market and stay away from commodity buildings which have suffered in a very competitive landscape.

What strikes us is how the office and apartment markets are in such different places. The office market presents a great timing opportunity with challenging current fundamentals, while the apartment market presents a timing challenge (late in the cycle), yet solid long term potential.