

Interpretation

This report presents the findings of empirical analysis of secondary market performance to glean how its investment profile — the trends, participants, and points of inflexion — is differentiated from primary markets. Differences are apparent when contrasting primary and secondary markets as well as between secondary markets. In a few cases, these observations point to clear investment strategy implications. In most cases, they are instead suggestive of opportunities and risks for investors and lenders.

As an overview of the secondary market investment landscape, the scope of this report is ambitious. The causal drivers of commercial real estate market performance at every level will command the attention of our industry's academic and practitioner researchers far into the future. Rather than attempt to isolate causality, the empirical analysis and results presented here are both descriptive and interpretive. They survey patterns of market performance and relationships that can inform investors' evaluation of market opportunities in secondary markets.

A Distinctive Investment Landscape in Secondary Markets.

Conditions are ripe for a shift in focus to commercial real estate's secondary markets. Bolstered by the potential for more stable national economic trends, buyers' improving tolerance for risk-taking, and a widening disparity in yields across primary and secondary markets, investors are broadening their sights.

Apart from their rankings on the commercial real estate investment hierarchy, secondary markets present investors with distinct opportunities and risks. The assumptions underpinning investment strategy along the coasts are not completely portable as buyers and lenders migrate to areas of lower liquidity — secondary markets are not business as usual on a smaller scale.

Differences between primary and secondary markets — and across the diverse array of secondary markets themselves — extend well beyond a tally of each metro area's inventory of commercial properties. For an investor making a first foray into secondary markets, the landscape of market participants, properties and linkages to the real economy will be less familiar. Secondary markets also present unique issues related to the timing of property acquisitions and dispositions and the dependence of investors on the availability of financing to support a critical mass of activity.

For investors motivated by a secondary market's long-term prospects for appreciation, several factors may be important. Markets with a high concentration of skilled workers, and a track record of innovation, rank high on the list, as do supply-constrained markets. A cautionary note accompanies that endorsement. If those skilled workers are all busy doing the same thing, a downturn in a market fueled by a single knowledge industry can be particularly difficult. The notion of a creative class driving a market's long-term growth does not preclude volatility over the business cycle.

This report explores practical issues facing secondary market investors and their implications for the timing of investments and market and asset selection. Secondary market investment opportunities present unique risks. As the economy expands and the distance from the financial crisis widens, understanding secondary markets' performance patterns and their risk-return tradeoffs becomes an increasingly important task for investors, lenders and policymakers.