The Weekly Take

Don’t Look Back: What’s Ahead for Commercial Real Estate

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RIchard Barkham
From a macroeconomics perspective, the 1970s was characterized by a series of supply shocks and demand not very well managed. So you had inflation. What have we got now? We’ve got negative supply shocks and we've got demand, not very well-managed, pumped up by pandemic stimulus. So we’ve got inflation. I think the parallels with the 1970s are pretty profound, actually.

Spencer Levy
Last week, CBRE presented one of our signature events of the year, the unveiling of our comprehensive update on our Outlook for the Year in Progress, moderated by CBRE’s Head of Global Thought Leadership, Julie Whelan, the panel featured CBRE research leaders and sector experts from around the world. In a year marked by shifting uncertainty and tight credit conditions, CBRE is offering timely insights and analysis on the global economy and current trends in commercial real estate. On this episode, we are joined by one of the headliners from that event, CBRE’s Global Chief Economist Richard Barkham, for a deeper dive into some of the most thought provoking ideas.

RIchard Barkham
Hi Spence. Thanks for having me on the show.

Spencer Levy
Coming up, we break down CBRE’s midyear real estate market outlook and shed light on what may be on the horizon for the rest of the year ahead. I'm Spencer Levy, and that's right now on The Weekly Take.

Spencer Levy
Welcome to The Weekly Take. And Richard, I don't have to tell you it's been a year of change, but I want to start by quoting Julie’s set up of the panel discussion.

Julie Whelan
As we started 2023, uncertainty was looming in our global economy and our commercial real estate markets were already feeling the effects. Consensus was the global markets would be operating in a weak economic environment as central banks continued to fight inflation. Now we find ourselves at midyear. So much uncertainty remains, but we have more answers than we did six months ago, which of course means a new set of questions. Inflation is trending in the right direction, but will there even be a recession? Will it have a global impact? Commercial real estate capital markets have slowed, but fundamentals have remained strong in so many sectors. Which ones could surprise on the upside?

Spencer Levy

Richard, bring us up to date on the guesswork. We've been through a lot since the start of the year when many, if not most economists, predicted a recession of varying degrees. What have we learned so far this year? Richard?

RIchard Barkham
Well, the main thing we've learned, Spence, is that the economy is not behaving quite how we thought it would be. There's been a lot of change, a structural change, pandemic related change and interest rates of the highest level in 40 years. But they're not having this depressing impact on the economy that many economists thought that they would have. And we've all been working very hard to try and understand why the US economy has been so resilient.

Spencer Levy
Well, let's talk about that for a second, Richard. If you recall a year and a half ago, both you and I would say on stage the magic word transient. And of course, it wasn't transient inflation. It lasted much longer, much higher than we thought. Now, a lot of the naysayers are saying the opposite, longer higher. But that's not being proven out by some of the headline inflation numbers. And, the U.S. economy keeps chugging along. What do you think?

RIchard Barkham
I think we might well have been a little bit too pessimistic this year, Spence. But that word transitory has many meanings. Because that trend, inflation, being longer than we thought it was going to be. I think we all thought it would become endemic, and I think we all thought the Fed is going to have to crush the economy to get rid of it. But as it happens, it's turned out to be transitory, just a longer transition period. So it's coming down quite nicely now. So there is a degree of optimism. The path to a soft landing has emerged. I think there will have to be some weakening of the economy in the labor markets. And I think the Fed will keep interest rates high until that happens. We are still reasonably optimistic that this isn't going to be a deep recession, it's probably going to be a mild recession, maybe just a period of stagnation. But I think for long term sustainable levels of inflation, there are going to be a couple of quarters that will show mild negative growth. And whereas before we thought that would be Q3 and Q4 in 2023, like most others, we're now seeing it in Q4 2023 and Q1 of 2024. We've pushed it out a little bit, but it's still there in our thinking.

Spencer Levy
Is the labor market too tight? Or what, in fact, is causing wages to increase if we're at the same basic level of unemployment we were pre-pandemic?

RIchard Barkham
Very interesting question, I think. Well, you will remember that pre-pandemic, 2019, interest rates were going up to try and slow the economy down. So the fact that we've got back to that pre-pandemic level of unemployment, we're still in a position in 2019 where rates would have to be elevated. Now, they may not need to be elevated to where they are now. In fact, we expect them to come down in 2024. But they still need to be at a level that eases the demand for labor relative to supply. And that transition to a more balanced labor market is still to happen and rates need to achieve that.

Spencer Levy

Well, let's transition this just a touch to real estate, and I want to go back to the CHIPS Act and the Inflation Reduction Act, both massive fiscal stimulus, much of which hasn't happened yet, will happen over time, but nevertheless, it will bring some manufacturing back to the United States, which we are already seeing. How does the boom in manufacturing impact the real estate industry in industrial or perhaps other asset types?

RIchard Barkham
The normal pattern, I think, in a recessionary period is for construction costs to fall, and that is one of the factors that is good for real estate because it means that developers, their projects begin to pencil. But I think we're not seeing quite the reduction in construction costs that we would because a lot of that construction resource is going into building structures for that manufacturing revival. So that's an odd thing that's happening that we wouldn't have expected. I think the fact that construction is strong is one of the factors that's making the US economy more resilient. And it might well be feeding into a process where interest rates can't quite come down as quickly and you can't have everything in the economy. If we have a resilient economy, we're not going to have interest rates coming down quite as quickly. So those are the two factors, I think, that have most impact on real estate.

Spencer Levy
What I've been hearing from my clients on the construction cost front is similar to what you said. They say that we have seen a flattening, not a lowering, but a flattening. To your point, from a macro standpoint, the manufacturing is diverting resources, keeping wages and/or construction costs high. But overall, would you agree that we're beginning to see at least a flattening in construction costs, if not a decline?

RIchard Barkham
Oh, absolutely. And the fact that commodities are weakening in terms of price is very, very helpful. But this is not the drop in construction cost that you would normally associate with a high interest rate period. And in the longer term, you could argue that it's good for real estate because the less real estate you create, the more it keeps vacancy at lower levels and it sustains rents and sustains value. So, some sort of check on new construction, arguably, in the longer term, is quite good.

Spencer Levy
And for the record, Richard, our house view has been to expect a mild recession. But we're also not saying the dangers are over. What are those dangers and what should we expect over the next year?

RIchard Barkham
I mean, the dangers come, obviously, out of elevated interest rates. We're probably about at the peak of the rate cycle now. We may yet have one more rate rise in the United States, and one more rate rise in Europe. The economy's changed quite a lot. And so nobody quite understands the way in which interest rates are going to affect the economy in terms of the extent and the time period. So I think whilst we're not overly pessimistic, I think we still should expect those interest rates to suppress economic activity, both consumer spending and investment for at least the next 6 to 12 months. That's what gives us that weakness in Q4 and Q1. That's the classical pattern. It hasn't quite happened, as in classical economics yet, but that's why we're cautious on the future.

Spencer Levy

Now, let's get the perspective of some of our sector specialists, starting with the capital markets. Here's Julie Whelan with Darin Mellott, CBRE Vice President of Capital Markets Research.

Julie Whelan
Now, these interest rate hikes have also brought the banking sector into the spotlight, especially small banks. The topic of debt defaults in commercial real estate is under a lot of scrutiny. Darin, I know you just wrote a great paper on this. Is this a global topic? Is it isolated to the US? Is it as big a problem as headlines will lead us to believe?

Darin Mellott
Well, it is primarily a US problem and it stems from issues in the office sector, and that's where challenges in the office sector are most pronounced. So that's where I'll focus my comments. But there's no doubt that we're going to see a significant amount of distress, particularly in office, as I mentioned, during the coming quarters. Now, let's put this into a bit of perspective. US banks have about $1.7 trillion in exposure to CRE. However, office debt only accounts for about 340 billion of that. So, again, perspective is everything. This is about a percent and a half of the banking systems' total assets. Also, during the global financial crisis, as you mentioned, some people wonder about wider implications. This was a global financial crisis driven by residential real estate, which in 2007, made up 20% of bank assets, compared with commercial real estate accounting for closer to 10% of bank assets today, with much more conservatively underwritten loans. Still, we think losses could be substantial. US banks could see up to $60 billion in losses over the next several years, with the office accounting for roughly 26 billion of that. Again, for context, that's equivalent to roughly three and a half percent to seven and a half percent of total exposure. In the context of total banking assets, losses are within a few tenths of a percentage point of the total.

Spencer Levy
So, Richard, what do you think about the potential for greater bank losses, more bank consolidation, more bad loans, not only hitting the market but also gumming up the works, so to speak, for the bank's ability to lend?

RIchard Barkham
I think you've got to separate out the smaller and regional banks from the larger banks. The banks do have to book losses. I think there will be consolidation and I think that will take place over the next 12 to 18 months. But it's nowhere near as severe as the great financial crisis or the savings and loans crisis. But I think the small banks, the regional banks, have been quite an important part of lending to real estate over the last ten years. So I think there will be some sluggishness on their part as they seek to absorb the losses, losses particularly coming in the value loss from the office sector. But it's just, I think, not big enough to be a total block on lending to real estate.

Spencer Levy
A comment that I heard recently at the Real Estate Roundtable was that, this came from a major lender, that because we don't know what the risk free rate is, meaning that they don't know when the Fed's going to stop, they can't lend yet, or they don't feel comfortable getting into the market yet. And that's why I think the single most important day in the next six months is what has been called on Wall Street, the pivot or the pivot party. When the Fed finally says either they're done or better yet, actually drops rates a bit. So when is that going to happen, Richard?
RIchard Barkham

I think it's going to happen at the end of the year. Although you're quite right. I mean, the two big uncertainties that the economy and particularly the estate capital markets have had to face is both inflation, which is a slippery fish to forecast at the best time, and then the Fed's reaction to inflation. Now we're beginning to get a handle on inflation. It's coming down into the zone where we can see where it's going and we're comfortable with. We're still not completely certain how the Fed will react. Will it be content with inflation, just whatever it says, getting below 3%, or is it actually going to drive inflation down to 2%? But we think that if the Fed can get inflation in the two, two and a half percent range, which it will do by the end of the year, then I think it'll call a halt to interest rate rises. And then, because the economy won't be in full recession, likely to be a mild recession, it won't be a normal, you know, rates dropping off a cliff type of environment, but it will be a top of the rate cycle and we will be looking at the slow decline of rates through 2024. So as you point out, that would be enormously beneficial to capital markets participants who can then start to price deals and move ahead. We know that there is an enormous desire for people to move ahead because, apart from in the office sector, real estate fundamentals are pretty good at the moment.

Spencer Levy
Well, this is a perfect time then to transition into the specific asset types. Richard, let's turn to one that's been at the very core of perhaps the biggest real estate or even cultural change we're seeing around the business world. I'm talking about office. Workplace. Here's Julie with Jessica Morin, head of CBRE Americas Office Research, along with Ada Choi, her counterpart in Asia Pacific.

Julie Whelan
One thing I want to pick apart for our listeners is how much office fundamentals are struggling from the secular impacts of hybrid work that we just talked about versus that layered effect of the economic cycle. So, Jessica, I know you've done some work on this lately. Let's start with you.

Jessica Morin
Sure. So in the US, demand measured by tenants in the market has remained pretty stable so far this year, but office leasing activity has not yet stabilized. So what that tells me is that tenants are really deferring these leasing decisions until there's a greater degree of economic clarity. And so this mix of the economic uncertainty plus the hybrid work makes it difficult to discern which is the primary cause of reduced demand. But because we saw leasing activity exceed pre-pandemic levels for several months in 2021, before that economic uncertainty set in late last year, it's likely that the cyclical events here are the bigger factors. So, once we have economic stabilization, we can really expect to see a rebound in tenant and leasing activity. And then on top of that, construction completions also peaked in 2021, and they're likely to stay low for the foreseeable future. So that's also going to support market fundamentals once we see demand pick up in late 2024. And then talking to my colleagues in Europe, it's a similar story. Both factors are impacting the market. But economic challenges especially are impacting weak leasing activity in Europe so far this year. And so volume is down there by about 20% compared to where it was in the first half of 2022. And it's going to be the second half before we see any material signs of improvement there.

Ada Choi
Well, I think in Asia-Pacific, I would say that the office performance is largely outfactored by the economic cycle and the supply peak that pushes frequency to 20 years high.

Recovery in mainland China is weaker than expected, while supply is really high, resulting in further decline in rents.

Spencer Levy
Your thoughts, Richard? Are the changes in workplace around the world cyclical to the economy or something more profound?

RIchard Barkham
Cyclical or structural? Well, it's actually both, Spence. Most people at the moment are focusing on the structural shift, which is that we've got an increase in remote working, and some of that is not going away. But we're also at a cyclical downturn, as well. And I think people are reading too much cyclical into the structural downshift. So I do think as the economy transitions and we get into the next growth cycle, and as the labor market rebalances, then I do think we will see an upswing in the office sector as we have done in every cycle for the last 40 years. So that's my view. I think there is a reason why we have this great big office economy and it tends to be clustered. It's because, and you've spoken about this, you know, if not once, a hundred times. You know, there is something productive about people working together. And it's not surprising to me that productivity in the US economy is flatlining at the moment. At the same time, as you've got relatively low levels of office utilization. So I think companies will want to restore their productivity growth and they'll do that through collaboration, not quite as much as it was prior to the pandemic, but more than it is now. And one thing I would say is, just from an economics perspective, the resilience of labor markets, the presence of these high interest rates, has been somewhat surprising to us. What I think companies are doing, and you've heard the term labor hoarding, what remote working I think allows companies to do is to hoard labor but still cut costs on the footprint. So I think that's what they're doing and it's probably, you know, it's overshot. Companies will need to rebuild their physical footprints and it may take a year, may take two years. But the occupied stock of offices is at a cyclical and structural low, and I think it will bounce back.

Spencer Levy
So where do you stand on the reversion to the mean versus the secular shift that we're seeing in occupier office occupancy and their footprint.

RIchard Barkham
In an era of digital economy growth and just huge investment in artificial intelligence, you're a brave man if you ignore the structural shift. But I don't know, I think, more of a reversion to the mean. And I think once we get through the disruption, the lingering disruption from stimulus, from pandemic, from technical change, I think we will probably be surprised at how much reversion to the mean that we actually get. It's been delayed, but that's where I would put my money.

Spencer Levy
Well, Richard, another hard hit sector, at least during the pandemic, was hotels. Here's Julie with Rachael Rothman, CBRE’s head of Hotel Research and Data Analytics, to shed some light on the sector.

Julie Whelan
Does the slowdown in global growth that we've discussed change your outlook for the rest of this year and into next?

Rachael Rothman
Well, if we could just set the table for a minute and take a quick walk around the globe and talk about what's happened in the first half of the year. In the US, we've seen room revenues up about 5%. In Europe, they're up 20, and in Asia-Pac, over 50. As you mentioned, this growth has been fueled by work flexibility, improvement in group business in the US, Americans' strong desire to travel abroad, particularly to Europe, and the reopening of China and Japan. We do expect growth to slow as we move into the back half of 2023 and 2024, of course, given the strong trends year to date. In addition, it can take time to add back long haul flights. And there has been some friction in the visa process. But as that eases, we do expect trends to resume.

Spencer Levy
I also want to bring in another sector that's on the rebound post-pandemic. That is multifamily. Back to Julie now with Matt Vance, CBRE’s America's head of Multifamily Research.

Julie Whelan
Over the last year, the conversation around multifamily has been focused on softer demand and a lot of development, which can usually create an imbalance in the market. But with interest rates that have risen and therefore the cost of mortgages being more expensive, do you expect this to actually drive an uptick in multifamily demand?

Matt Vance
Well, Julie, the multifamily sector nearly rebalanced itself this year already. US renter demand came back very strong in the second quarter, just as we've been projecting. It almost even kept pace with near-record supply. This is really important because vacancy only moved up another ten basis points. It returned to its long run trend of 5%. Now, the single family market, on the other hand, is not balanced at all. We estimate there's a shortage of around 3.1 million homes nationally. And because of this market tightness, prices are up. All right. And when you combine that with higher mortgage rates, buying a home has become extremely difficult for many. So I don't know, to answer your question, Julie, that this will cause enough of an uptick in demand to overcome some of the things that are or will be weighing negatively on new apartment leasing, things like a slowing economy, slowing job growth and other economic turbulence. But it is absolutely helping to preserve existing demand and existing occupancies. And this is something property owners are very focused on right now, is that preservation of existing occupancy.

Julie Whelan
Yeah, it's easier to keep an existing customer than to get a new one, right? So, what are your expectations for the rest of the year moving into next year?

Matt Vance
Absolutely. The same story that I just described applies throughout much of the world, as central banks have grappled with inflation and raised interest rates and the cost of buying homes. It's keeping renters renting for longer virtually everywhere.

Spencer Levy
Okay, Richard. Hotels and multifamily. Why are we optimistic about those sectors in ways that we might not be when it comes to office?

RIchard Barkham
Let's go to the second one first, multifamily. It’s not just a problem in the United States, it's throughout the developed world. We do not build enough houses. We're absolutely short of houses. So, that makes owner occupation expensive. It's particularly expensive at a time of high interest rates. So as people become a little bit more confident about the economy not going into recession, then you're going to see the rebound in terms of leasing in multifamily and second quarter leasing bounced back pretty strongly. So, in multifamily, it's about, primarily, shortage of houses. It's also about city living and smaller households, as well. On the travel side of things, the demographics that like to travel, the 55 plus and then the 25 to 35 age groups. Over the last ten years, demographics just swelled in size. So demographically, you have really strong demand for hotels and leisure and travel. And don't forget, people are looking at this travel boom as something of a pandemic bounce back. But don't forget that the ten years before the pandemic, 2009 to 2019, that was an era of relatively low growth and low income growth. So I think we're seeing a reaction not just to the pandemic, but the relatively weak growth in living standards that we actually saw in the decade before.

Spencer Levy
So, Richard, let's dig a little bit deeper into multifamily. What are we saying to clients today about luxury versus the other types of multifamily, and how they should be playing in those sectors moving forward, both from an investment and a construction standpoint?

RIchard Barkham
I mean, first and foremost, there's not enough housing. That would be true in all sectors, both at the affordable level and also at the luxury level. So I think investors can feel reasonably confident. There has been a focus of supply, I think recently, in the luxury sector. But I don't really have a sense that that is a sector that's oversupplied. In fact, I just came back from a trip to New York and the leasing market in New York, which has quite a high proportion of luxury multifamily, extremely strong. People still want to live in cities. They may not want to work there at the moment, but they still want to live there. So I think investors can invest with confidence in the luxury sector. If we go back to affordable, the really interesting thing about affordable is, for all that you are catering for folks who may not be in the highest paying employment, when you actually have rents that are below the median or affordable, people tend not to give them up. The rate of default is very low. The cash flow stability in affordable housing is remarkably strong.

Spencer Levy
The other thing about affordable is that they typically have inflation adjusted rents when dealing with capital A affordable. The biggest challenge with capital A affordable isn't that most people agree we should build more of it. There's simply not enough LIHTC out there, low income housing tax credits, to be able to make the math work so that the construction of a low income housing tax credit project equals that of market rate housing.

RIchard Barkham
I wouldn't disagree with you, Spencer. I think you can probably accept a lower return on affordable because the risk is lower. The risk adjusted return I think would be the same. But the stability in affordable housing is just remarkable.

Spencer Levy
The mid-year outlook also addressed global trends in industrial and retail, and we discussed those in one breath because of one thing: fundamentals. Industrial stayed strong even at the depth of the pandemic. Asset types like warehouses and data centers

proving essential to the changing economic landscape. And while retail may have endured some pain, it rebounded with strong fundamentals, too. Here again is Julie with America's head of Retail Research, Brandon Isner.

Julie Whelan
Brandon, as I mentioned, retail also has decent fundamentals, but for very different reasons than industrial, and it's a little bit of a mixed story. So limited development and strong post-COVID consumer rebound has created resiliency behind retail. But do we expect that this is going to change given the state of the economy, and what's happening globally with this?

Brandon Isner
Well, Julie, that's a good question. I would say yes, but you're right that retail is a bit of a mixed bag globally, as it's so dependent upon the consumer. In Europe, retail sales volumes have been on a mild downward trend as real incomes have been squeezed due to inflation, but they remain about 2% above pre-pandemic levels. So that's fairly solid. The U.K. is essentially in line with their pre-pandemic levels. Consumer confidence remains challenged, but footfall at CBRE managed retail properties across Europe continues to improve. In the Asia-Pacific region, core inflation has decelerated in China. It's accelerated in Japan. Spending is continued, particularly with urban households. But, it looks as if any further spending will be, could be tapping into savings as savings rates have been declining. We're already seeing a leveling of, you know, level off of spending in June, but tours for available retail spaces are at a high level, which is leading to generally strong leasing activity. And then we come to the US, which is a little bit more confusing. Core inflation is decelerated. Consumer confidence has begun to rebound slightly, but remains well below long term averages. And some segments of retail are starting to see some cracks with year over year decline in sales for retailers such as home and garden retailers, department stores, electronics and apparel. Additionally, student loans, coming back into play in September, could mute retail spending this holiday season. Yet, the restaurant industry remains very strong, which is a sign of continued discretionary spending. On the real estate side, US retail remains at a very low availability rate of just 4.8%. That all said, despite retail having good fundamentals, it's difficult for retail developers to justify breaking ground on large projects because construction costs remain so high.

Spencer Levy
What do you think about retail, Richard?

RIchard Barkham
I think one of the facts that people miss sometimes is that retailers themselves have got better over the last ten years. They were caught a little bit flat footed by Internet sales. And towards the end of the 2010’s were struggling, particularly the department store format. But over the course of the last five years, many of them have gone through bankruptcy and restructuring. But I would say the retail sector has changed and is much more effective. Really knows its customer. Really slick brick strategies combined with click strategies, and just better engagement with the consumer. So I think part of the retail revival is limited supply. Partly, I just think it's, retailers have got better. They've raised their game, and it's more fun, more enjoyable to shop there. And of course, a third factor would be with, recently, with people spending more time at home. It's kind of been more money in the suburbs, and that's gone into some of the open air retail that you tend to see there, as well. So there are some other factors, but supply shortage is chief among them all.

Spencer Levy
Well we've had many great retailers on this show and they're all saying the same thing, that retail, for the best retail spots in the best locations, they're extremely tight. In fact, when Bed, Bath and Beyond had its bankruptcy, that actually opened up space that they needed. So retail is in a place that I frankly have not seen it maybe ever in my career, but certainly not in the last 20 years. And it bodes well for the future. But speaking of the future and the present, let's now switch to industrial. Where are we with industrial today, Richard?

RIchard Barkham
Well, I think some of us were a little bit worried that quite a big supply pipeline had built up, particularly in the United States, around industrial. But now we've seen the rate of new starts dropping off and I don't think it will take long for the 500 million or so square feet of new space to be absorbed over the course of the next 12 months. I think industrial is par excellence, as you've always already alluded to it. The sector that's going to be driven by the digital economy, and whatever analysis we do, whatever we say about macroeconomics, all you can see is the digital economy getting a bigger part of the overall economy over the next three, five and ten years. So in the United States, it may be a quarter or two of excessive completions over net absorption, but won't last. Longer term, very strong tailwinds.

Spencer Levy
Richard, I think your talk about the digital economy and AI is a perfect place to transition into data centers. Data centers have been a booming business and a very hot topic thanks to everything that we just discussed and other technological innovations across all sectors. But should we be cautious? Before you answer, Richard, Julie posed an important question to Gordon Dolven, Research Director for CBRE, America's Data Centers.

Julie Whelan
Data centers may rival industrial in terms of the asset that's in favor. So there have to be some challenges. What do you see as the biggest headwind that data centers actually have to battle against right now?

Gordon Dolven
Yeah. The biggest issue right now, Julie, is availability. So large corporations, if they're going from on premises to co-location, they're struggling to find a turnkey solution with one operator in one market. So we're seeing across the globe, a lot of occupiers having to segment out their requirement to different operators, to different regions, to different markets in order to fulfill the demand that they're seeking. On the power side, we still have some transmission and distribution delays and issues. But there are some bright spots that I do want to highlight as well, given that these headwinds are something that we can do something about. So, recent federal legislation provided $2.5 billion to modernize our electricity grids here in North America. And I'm really proud of the fact that in digital infrastructure, we're leading the way in terms of low carbon and renewable energy initiatives. So whether this is nuclear, wind, solar or hydropower, we are at the forefront of trying to bring on new renewable and low carbon energy solutions for the industry. And we look forward to monitoring that the rest of 2023.

Spencer Levy
From an economic perspective, what do you make of that? Is limited supply going to slow the power of data centers or will demand simply empower more development and growth in the sector?

RIchard Barkham
I would be of the latter camp. We've seen huge demand and the growth of AI is only adding mega demand on top of really strong demand. So, I think people will find a way of bringing that supply online. Now there are some checks on that, one of which we've already mentioned, which is the cost of construction; acts as a natural brake. And also power. I think getting the grid capable of supplying data centers with enough power remains a challenge that I think our sector, real estate, can manage on its own and needs a governmental response, a state government response, and that can be a bit sluggish. So I do see some checks on growth of data centers, but certainly not from a demand side.

Spencer Levy
What's interesting about data centers, and most people don't realize this, is that rents were actually going down in data centers till about three years ago and now they're finally on the upswing. I think they're going to be up swinging even more for the reasons you just laid out. Well, Richard, before we say goodbye to this annual summer reunion of ours, I'd love to pull our lens back to the global factors and macroeconomic trends and get your final thoughts. What are you most closely watching that our viewers should keep an eye on, also?

RIchard Barkham
Most closely, I'm watching the rate of wage growth in labor markets around the world. I would like to see that settle down below four and a half, closer to 3%. Then I will be happier about core inflation coming down. Watching labor markets is key to watching, to following interest rate, and that's key to macroeconomic forecasting. Of course, I'm also following the Arsenal Football Club, who have invested heavily in new talent over the course of the summer, and I would forecast a very good season for them in the English Premier League.

Spencer Levy
Well, I'm glad you brought that up because as you know, I live in Baltimore and our Baltimore Orioles are in first place in the toughest division in baseball. World Series contenders. So good luck to Arsenal, and good luck to the Baltimore Orioles, as well. Well on behalf of The Weekly Take, Richard, I want to thank you. Richard Barkham, CBRE's Global Chief Economist. Richard, always a pleasure and looking forward to the next time.

RIchard Barkham
Thank you for having me, Spence. Good luck.

Spencer Levy
And I'd also like to thank Julie Whelan, another regular on our show, and all the CBRE experts who spoke on the 2023 mid-year Real Estate Outlook presentation. For more, including other related content, check out The Weekly Take's website at CBRE.com/TheWeeklyTake. You can share the show, and don't forget to subscribe, rate, and review us wherever you listen. Also, a shout out to those of you who reached out via the Talk to Us button on our landing page. We've gotten some great notes from you, our listeners, and thank you for your feedback. Keep them coming. Hope you'll join us again next week as we continue to survey the economic landscape in the commercial real estate industry and beyond. Thanks again for joining us. I'm Spencer Levy. Be smart. Be safe. Be well. And go Arsenal and the Orioles.