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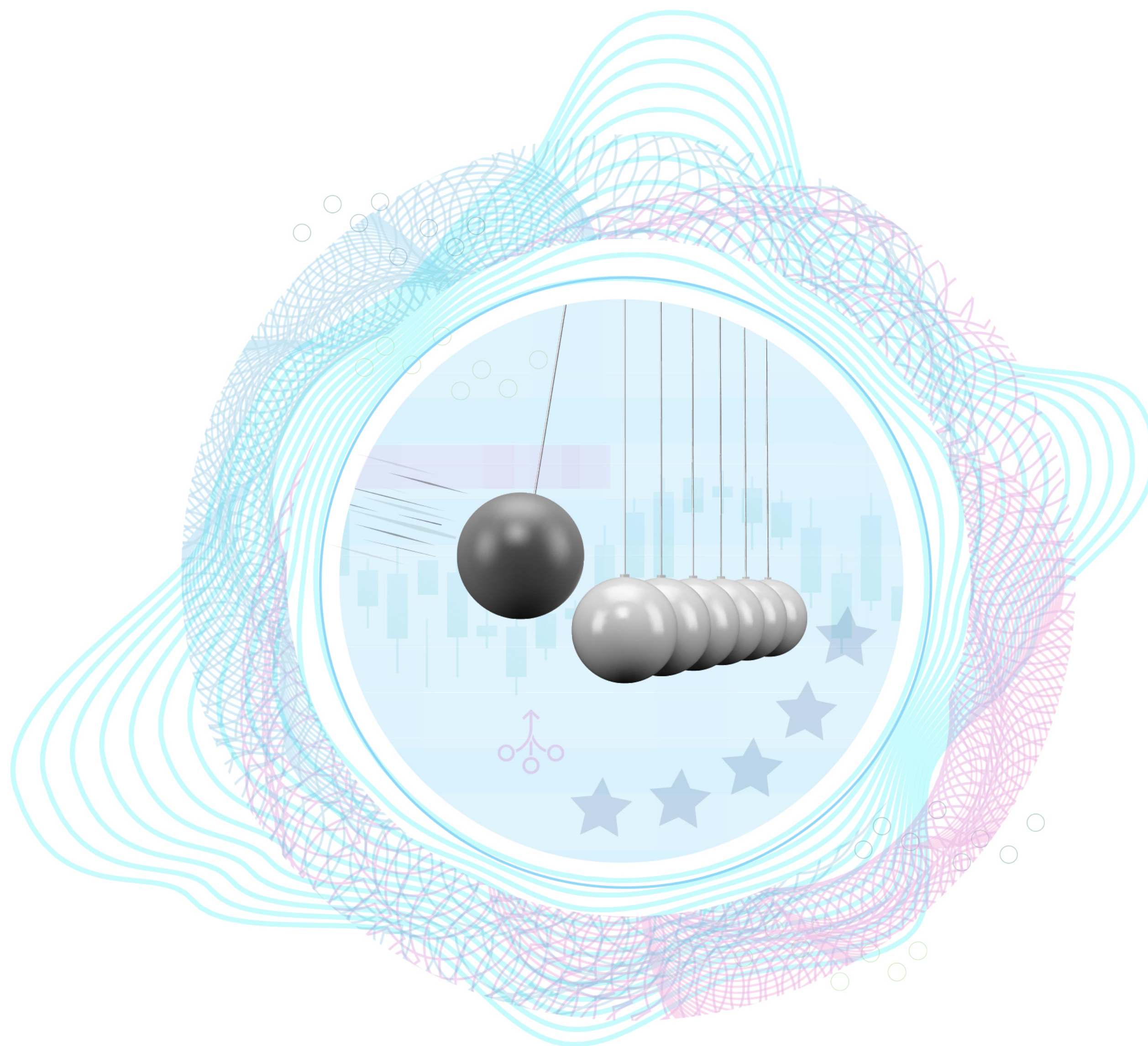

2022 real estate M&A outlook

Momentum continues, but sector matters

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Overview and outlook

The pandemic has reshaped and reprioritized where and how people live, work, and play, and their choices are exerting major influence on commercial real estate (CRE) industry mergers and acquisitions (M&A) activity. Performance measures across the industry make one thing abundantly clear: sector matters.

2021 was a banner year for the industrial sector, with demand for properties supporting the digital economy driving robust transaction volume and premium pricing. The residential sector continued its run as a strong and stable investment class, buoyed by a competitive homebuying market and increasing consumer interest in single-home rental properties. The hotel and leisure sector saw early activity, slowed a bit amid COVID-19 virus resurgences, then picked back up through the 2021 holidays and into 2022—showing promising signs of recovery after two challenging years. Office sector M&A was down across the board due to increased uncertainty about when—or if—occupancy levels will return to pre-pandemic levels; meanwhile, many employees continued to enjoy the flexibility of work-from-home arrangements. Finally, 2021 was a mixed bag for retail: M&A activity was better than Q2-Q4 2020; however, consumers' preference for online shopping, increasing vacancy rates, declining rent collections, and higher operating costs continued to weigh heavily on the sector.

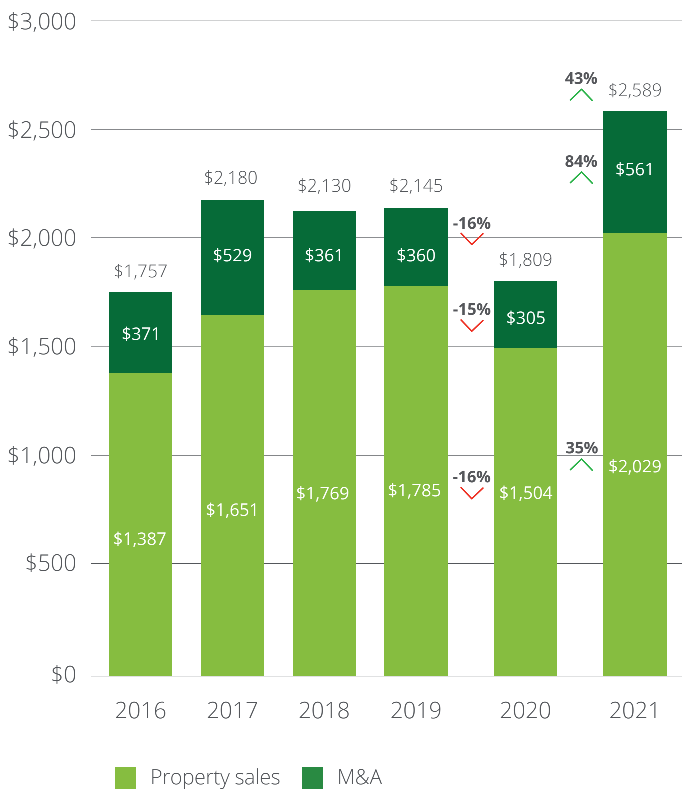
This report reviews 2021 CRE M&A activity from broad industry and sector-specific perspectives, looks ahead to 2022, and explores global and US-specific trends and drivers to help CRE owners and investors plan their M&A strategy as they position to adapt and grow in the future.

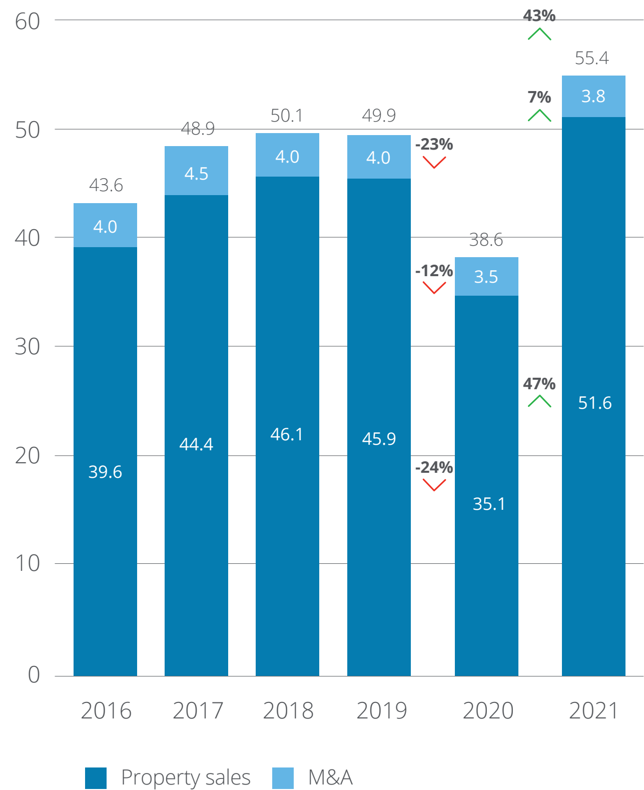
2021 in review

2021 was a big year for real estate M&A activity. Not only did global CRE transaction volume and value across regions and buyer types rebound from 2020's depressed levels, 2021 property sales and M&A totals exceeded those of pre-pandemic 2019 (figure 1).[1]

Figure 1. Global 2021 CRE sales and M&A volume

Property sales and M&A both set records





Source: Refinitiv, Real Capital Analytics

All global regions realized an annual dollar volume gain from 2020, although the Americas substantially increased its 2021 share of total (37%) to the highest level since 2007 (44%).[2] The United States posted a record $809 billion in 2021 commercial property sales, nearly double 2020's total.[3] APAC, despite still leading in absolute dollar volume as it has for 12 of the last 15 years, saw a large annual drop-off in investment share, going from 54% of total in 2020 to only 43% in 2021, its lowest share since 2015.[4] The top 2021 global and US CRE transactions ranged in value from $5.8 billion to $25.9 billion (table 1).[5]

Table 1. Top 5 2021 real estate M&A deals

Top 8 global transactions

Date announced	Acquirer	Acquirer nation	Target	Target nation	Target subsector	Value ($B)
11/29/21	Redefine Properties Ltd	South Africa	EPP NV	Netherlands	REITs	25.9
05/24/21	Vonovia SE	Germany	Deutsche Wohnen SE	Germany	Management & Development	18.4
04/29/21	*Realty Income Corp*	*United States*	*VEREIT Inc*	*United States*	*REITs*	*16.4*
11/15/21	*Investor Group*[1]	*United States*	*CyrusOne Inc*	*United States*	*REITs*	*14.7*
08/04/21	*Vici Properties Inc*	*United States*	*MGM Growth Properties LLC*	*United States*	*REITs*	*14.6*
09/26/21	Heimstaden Bostad AB	Sweden	Akelius GmbH-Residential Property	Germany	Residential	10.7
01/04/21	Brookfield Asset Management	Canada	Brookfield Property Partners LP	Bermuda	Non-residential	6.5
10/12/21	Fastighets AB Balder	Sweden	Entra ASA	Norway	Non-residential	5.8

Top 5 US transactions

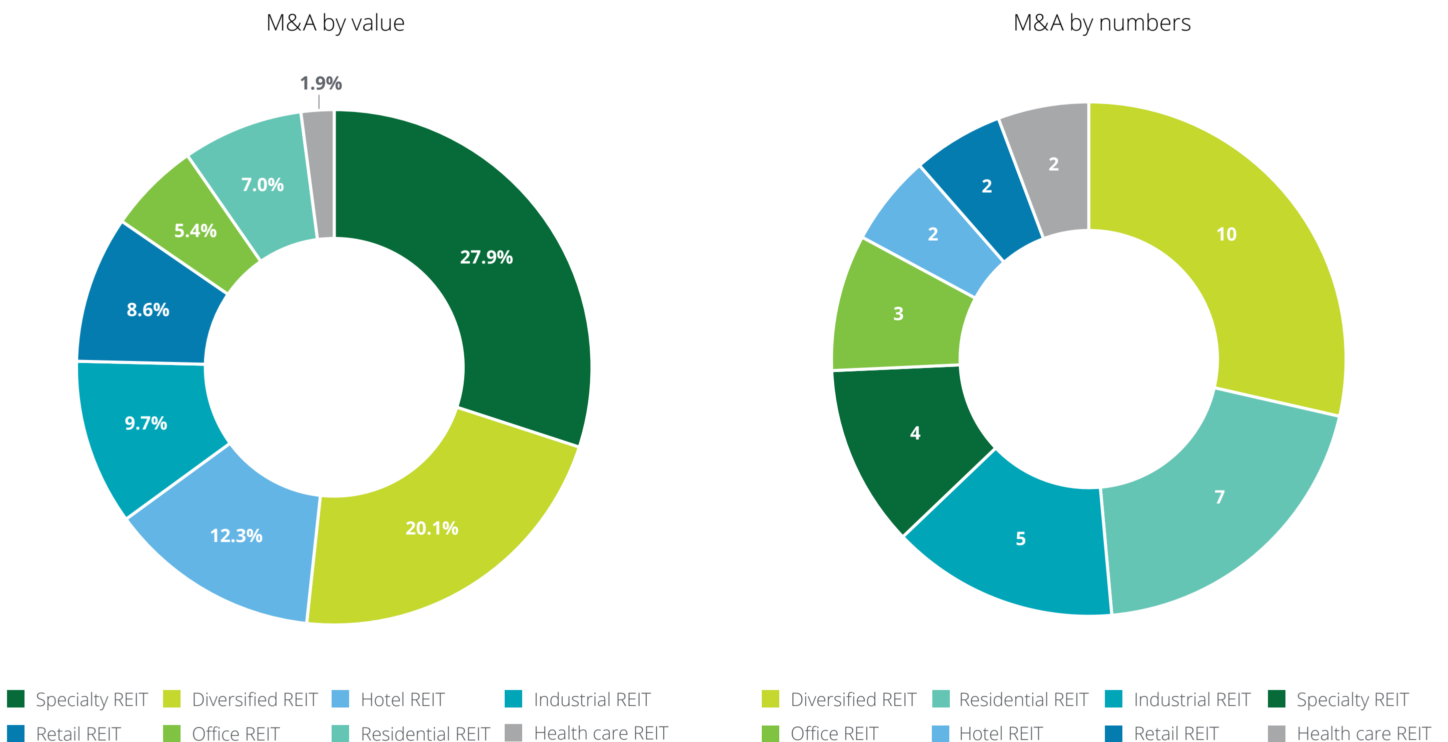
Date announced	Acquirer	Acquirer nation	Target	Target subsector	Value ($B)
04/29/21	Realty Income Corp	United States	VEREIT Inc	REITs	16.4
11/15/21	Investor Group[1]	United States	CyrusOne Inc	REITs	14.7
08/04/21	Vici Properties Inc	United States	MGM Growth Properties LLC	REITs	14.6
3/26/2021	BowX Acquisition Corp[2]	United States	WeWork Cos Inc	Non-residential	14.6
11/15/2021	Appleseed Merger Sub LLC[3]	United States	CoreSite Realty Group	Non-residential	14.6

[1] Composed of KKR and Infrastructure Partners LLC.
[2] BowX is a special purpose acquistion company (SPAC).
[3] American Tower is the parent company of Appleseed Merger Sub LLC.

Real Estate Investment Trusts (REITs), a primary contributor to CRE M&A, had an active year, especially in specialty or alternative asset classes such as data centers, cell towers, and net lease properties (figure 2).

Figure 2. Non-core* subsectors led 2021 REIT M&A activity by value

Residential and Industrial saw upbeat activity by numbers



*Non-core references "specialty" or alternative asset classes: data centers, cell towers, net lease, etc.

Note: Includes M&A transactions announced and completed in 2021 by Equity REITs globally. Only includes transactions with full acquisition and/or majority stake purchased.

Source: REFINITIV, S&P Global Market Intelligence

CRE M&A activity gained momentum as the year progressed, fueled—in part—by pent-up demand from 2020's pandemic-disrupted dealmaking. Yet, the news in 2021 was not universally positive: each sector had a different story to tell. Industrial and residential extended their run of stellar performance with a steady cadence of larger deals and higher price tags.

Office sector M&A reflected ongoing uncertainty about tenants' use of leased space amid shifting employee workplace preferences. The hard-hit retail and hotel/leisure sectors were more focused on weathering the effects of pandemic-related financial and operating challenges.

Industrial: Stellar sector performance

The industrial sector had another standout year in 2021, posting strong transaction volume and capitalization (cap) rates, with new construction and urban infill assets trading at a premium. Industrial REITs, which have taken advantage of their ability to lever at very low interest rates over the past five years, continued to generate healthy returns.

Properties focused on supporting the last-mile needs of the burgeoning digital economy were in greatest demand. Consumers' move to an online, "everything right now" purchasing model relies less on brick-and-mortar retail stores and more on "near-urban" distribution properties—both traditional and specialized cold storage warehouses—close to the end user for quick order delivery to their homes. In a representative deal, Industrial Logistics Property Trust (ILPT) announced its purchase of Monmouth Real Estate Investment Corp, which specializes in single-tenant, net-leased industrial properties, for $4 billion.[6]

Data centers to support increasing digitization and cloud computing use were also prime acquisition targets in 2021. Three large data center deals in 2021 highlighted the digital economy's growing impact on industrial sector M&A: KKR and Global Infrastructure Partners (GIP) announced the acquisition of data center REIT CyrusOne Inc.[7] Blackstone funds acquired QTS Realty Trust,[8] and American Tower acquired CoreSite Realty Corporation.[9] The Cyrus One and CoreSite deals were among the year's top five US CRE transactions in value.

The US office sector in 2021 found itself sitting in the uncomfortable gray area of "what's to come?"

Office: The big question mark

With the exception of continued demand for specialized medical office and lab space, office sector M&A activity was down across the board in 2021. There was, however, one noteworthy announced deal: Pacific Investment Management Company (PIMCO)-managed funds' $3.9 billion acquisition of REIT Columbia Property Trust, which owns, operates, and develops properties in major US cities including New York, San Francisco, Washington, DC, and Boston.[10]

The US office sector in 2021 found itself sitting in the uncomfortable gray area of "what's to come?" after the spread of COVID-19 variants extended companies' remote work policies, which led to an estimated 14 million to 23 million Americans relocating from the coasts and Midwest to the South and Southwest,[11] many trading large city, central business district (CBD) living for less expensive metro and suburban areas. While office vacancy was on the rise in general, the rate of increase in downtown office vacancy outpaced that of suburban office.[12] With CBD recovery lagging, many property owners, operators, and tenants are questioning how once fully occupied office space should and will be used in the future, and formulating strategies for current assets and leases.

Survey after survey reveals that, post-pandemic, employees want to continue to have flexibility and work from home at least part of the time.[13] In response, some tenants may decide to downsize to the amount and type of space they need. They could start consolidating or hoteling; convert individual offices into places for people to collaborate and work together; or lease less space in a nicer building. But while these companies may enjoy the relative cost benefits of a smaller office footprint (albeit there also is a cost for hybrid technology), it comes with a potential trade-off—a diluted corporate culture and diminished feeling of community that is created by having the organization's members together in one place.

For a variety of reasons, the vast majority of occupiers have yet to make any moves. They may be locked into long-term leases, enjoying cost savings from lower occupancy needs and related support costs or not sure whether or not things will snap back to a pre-pandemic state. A continued surplus of subleased space may entice some of them to take advantage of favorable market conditions[14] and renegotiate lease terms. Office REITs, landlords, and management agencies will need to pay close attention to tenant-related trends and, potentially, be prepared to offer incentives and/or make concessions to retain them.

Residential: US Sunbelt shines

The residential sector is hot—and not just because demand for single- and multi-family properties is up in Sunbelt states including Arizona, Nevada, and Florida. More than 6 million homes were sold in the United States in 2021, despite sky-high prices in many markets.[15] Entering 2022, continued elevated pricing, and limited supply—the total inventory of homes is less than half of that available pre-pandemic—are creating challenges for prospective first-time homeowners.[16] The competitive homebuying market is also increasing consumer demand for rental properties and driving up rental rates—positive news for owners and operators.

Multi-family residential as an investment class has been a strong and stable performer for a number of years. Now, single-family rentals (SFRs) are emerging as the new face of rental housing[17] and an attractive residential investment class. Deal examples include Independence Realty Trust's acquisition of Steadfast Apartment REIT for $4 billion[18] and Blackstone's announced acquisitions of Home Partners of America for $6 billion[19] and Bluerock Residential Growth REIT for $3.6 billion.[20] Prospective renters—especially those raising families or looking to take advantage of remote working arrangements to leave expensive, large-city living behind—are attracted to single-family homes versus standard apartment units because a home is generally larger, located in more affordable secondary cities and suburbs, and offers access to outdoor space and kid-friendly amenities.

Even some homebuilders are carving out portfolio space for "build-to-rent" assets. While the segment currently comprises only about 5% of homes built,[21] both demand and prices are rising. Renewal rates are often higher for SFRs, and rent increases have consistently outpaced those of conventional apartments—in some neighborhoods, from 6% to more than 11%.[22] With millennial homeownership rates trailing previous generations—18% of recently surveyed millennials say they want to rent forever,[23]—the demand for single- and multi-family rental properties should continue to drive the residential sector.

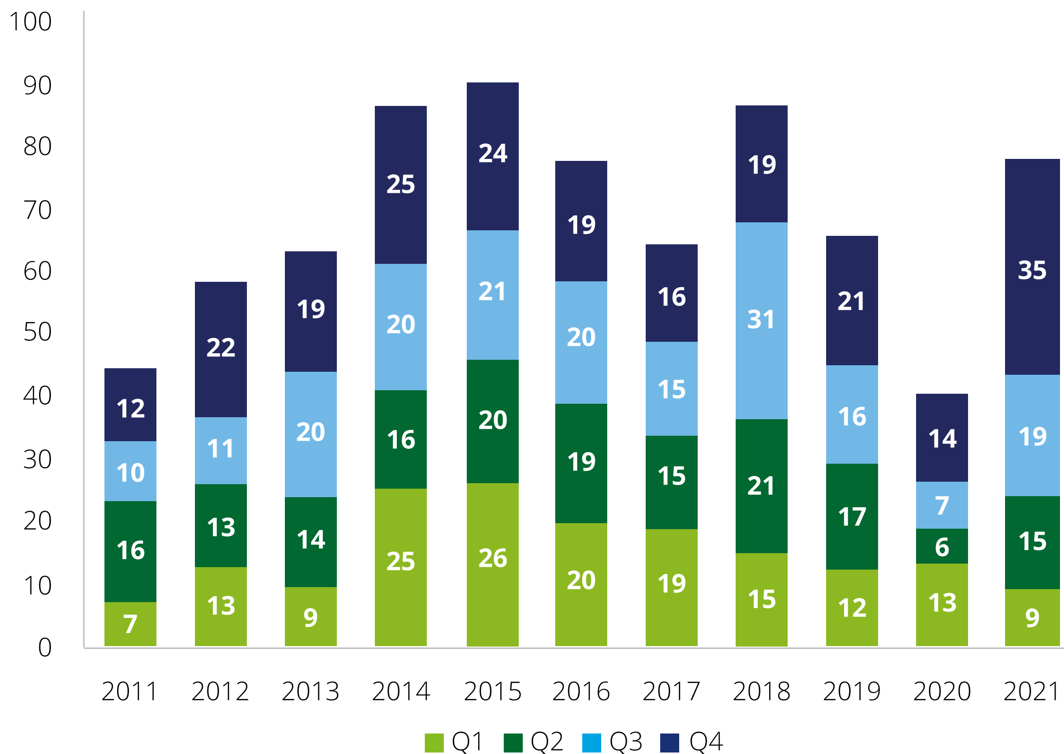
Retail: Rethink and reset

Many traditional retailers were already feeling the effects of consumers' growing preference for online shopping when a second year of pandemic-related closures and restrictions exacerbated softening operating fundamentals—increasing vacancy rates, declining rent collections, and higher costs from additional health and safety measures—and accelerated the sector's downward slide. A key takeaway from the pandemic is that consumers have reset their level of reliance on technology and digital platforms, and have tried and adopted new, innovative ways to shop. And even though consumers in Deloitte's 2021 back-to-school spending and holiday retail surveys indicated that they feel more comfortable returning to stores, their preference for online channels remains higher than before the pandemic.[24]

In both property sales and the M&A space, 2021 retail real estate transaction activity was a tale of two halves. The first half of the year was comparable to the second half of 2020, which likely had much to do with slow vaccine rollout, safety concerns, e-retail growth, and travel restrictions. The second half of 2021 was a different story: a modest rebound in the third quarter was followed by an exponential fourth-quarter rise of $35 billion.[25] Volumes across all CRE sectors jumped in Q4, so this is likely optimism across the CRE industry, and not solely for retail.

While retail Q4 2021 performance was an anomaly, it also sent a potentially strong signal of increasing retail sector momentum. In fact, its $35 billion in property sales activity was the biggest single quarter in the last 20 years.[26] That one quarter also accounted for just under half (44%) of 2021's total of $78 billion (figure 3). Still, this follows nearly two full years of retail volume declines and stagnant pricing growth. For comparison, compounded annual dollar-per-square-foot growth was 12% for industrial and 11% for multi-family residential over the past two years; retail dollar-per-square-foot growth has been 0% since 2019.[27]

Figure 3. Retail property sales volume ($ billion)



Source: Real Capital Analytics

Similar to the recent past, all retail assets did not fare equally in 2021. Class B and C indoor malls continued to struggle. The recent activity surge is being driven by grocery-anchored retail centers and stand-alone, single-tenant (often upscale) retail. 2021 had several large retail REIT merger announcements[28] and completions. Topping the list was Realty Income Corporation's $16.4 billion acquisition of VEREIT.[29] (While VEREIT is considered a "diversified" REIT, it does contain a large proportion of retail assets.) Kimco Realty Corporation acquired Weingarten Realty Investors, a grocery-anchored Sunbelt shopping center owner, manager, and developer,[30] for $5.6 billion.[31] And Kite Realty Group Trust acquired open-air and mixed-use shopping center owner and operator Retail Properties of America, Inc. for $4.5 billion.[32]

Retailers, more than ever, should consider rethinking and resetting their in-store and digital strategies and investments to support both traditional shopping patterns and omnichannel fulfillment activities.[33] For example, recent consumer data suggests that consumers are rethinking priorities, with one-third of consumers saying they are spending more on experiences than possessions compared to a year ago.[34] Retail properties that can offer consumers a single-destination, activity-based day of shopping, dining, and entertainment should benefit from this shift. Brookfield Properties, for example, developed a blueprint to upgrade and redesign many of its existing retail assets with experiential retail.[35]

The role of the brick-and-mortar store isn't going away, but it's changing. Recovery, even for well-functioning Class A malls, will likely take time and require significant capital. As has been the case for several years, we expect capital-rich REITs and private equity (PE) firms to take the lead as they look for opportunities to further improve well-functioning Class A properties and revive and/or repurpose Class B and C malls; for example, by converting some to distribution centers and other non-retail uses.[36]

Hotel and leisure: Poised for a comeback

Longtime property owners and operators have learned that macro events, such as the economic recession and the current global pandemic, typically have a deeper negative impact on hospitality assets. In addition, there are cycles for hospitality assets based on travel and consumer behaviors, both personal and business. So, citing historic downturn and recovery trends and anticipating that consumers may pull the trigger on delayed leisure travel (business travel is likely to take longer to revive), some hotel/hospitality companies, casino operators, and private equity real estate (PERE) firms took advantage of growth opportunities in 2021 to acquire some marquee assets in desirable markets.

Many of the year's casino deals continued the industry trend of separating real estate assets from operations. Gaming REIT Vici Properties announced its purchase of MGM Growth Properties for $17.2 billion. Vici will acquire 15 entertainment properties in the deal, potentially making it the largest property owner on the Las Vegas Strip.[37] Hyatt Hotels doubled its global resorts footprint with its $2.7 billion acquisition of Apple Leisure Group, a leading luxury resort-management services, travel, and hospitality group, from affiliates of each of KKR and KSL Capital Partners.[38]

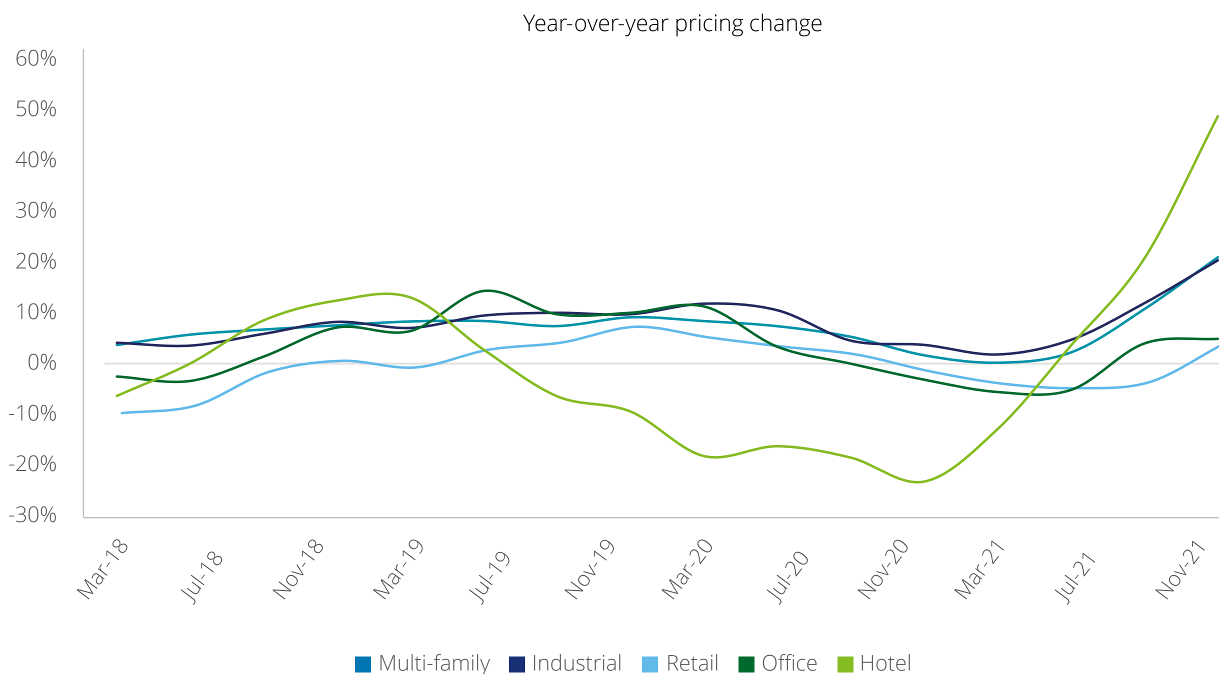
After a nearly yearlong pursuit, casino operator Crown Resorts agreed to PE giant Blackstone's $6.4 billion takeover bid.[39]

And Hard Rock International announced its acquisition of The Mirage Hotel and Casino from MGM Resorts for $1.1 billion. Hard Rock plans to build a guitar-shaped hotel on the property while rebranding the original Mirage hotel tower.[40]

With lending tight for new-construction projects and reduced income driving more efficient and less costly brand options, brand conversion deals gained in popularity during the pandemic.[41] Boston-based Sonesta International Hotels Corporation grew its 80-hotel portfolio to around 1,200 franchised and managed hotels with the March 2021 closing of its $90 million acquisition of RHL Corporation, parent company of Red Lion Hotels.[42] Sonesta also launched a platform that will enable the company to franchise four of its brands in the United States.[43] These and other deals drove up hotel pricing in 2021 (figure 4); however, it's an increase on a substantial drop-off, so the hotels that are trading are pricing similarly to pre-pandemic levels. We expect some variability in pricing for the sector given the deal volume might remain low for a few quarters.

Figure 4. YoY pricing rebounds to end 2021

Property sales and M&A both set records



Source: Real Capital Analytics

2022 outlook

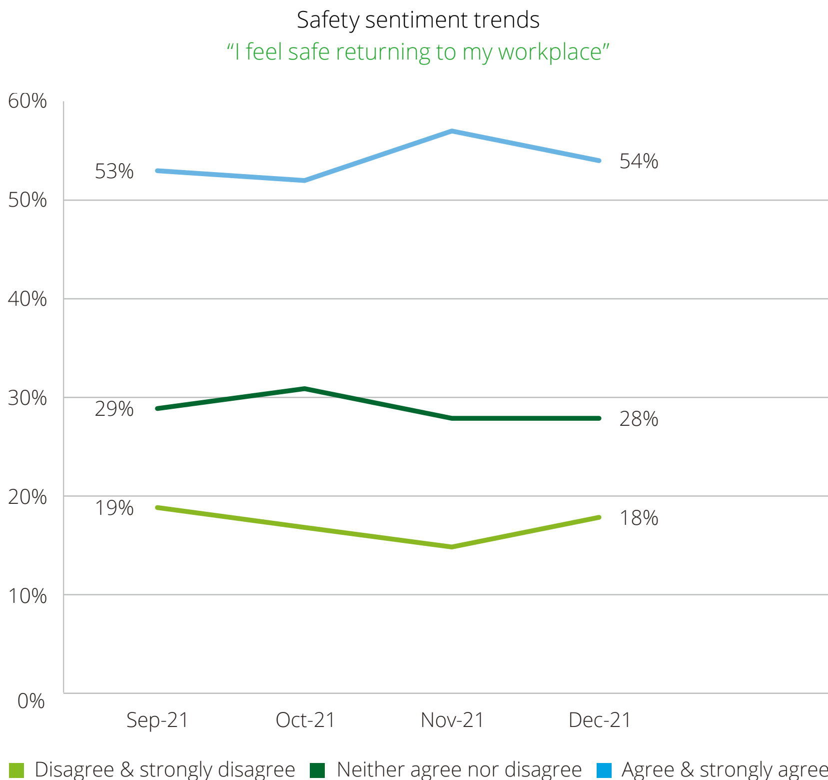
We expect to see continued high levels of CRE M&A activity in 2022, although it will likely be unevenly spread—the result of spillover from the 2021 sector story of "hot" versus "not." Pent-up demand, ready access to capital, a low-interest environment (at least for the near term), and abundant [PE/PERE] "dry powder" should have investors clamoring for properties in the hot industrial and residential sectors, despite their rich prices. Optimism appears to be growing for a moderate uptick in the office and hospitality sectors, and retail's surprising fourth-quarter performance may be an indicator of better times ahead. Potential headwinds include fierce competition for scarce assets, the impacts of rising inflation and interest rates on company valuations and deal financing, and impact of escalating geopolitical turmoil on the global economy.

From the standpoint of individual sectors, demand for **industrial** properties should continue in 2022—although potential buyers face dual challenges of high valuations and fierce competition. Current warehouse/distribution inventory is extremely limited—builders are having difficulty meeting demand amid the current e-commerce boom—which will likely contribute to sky-high prices. How will that supply-demand balance shake out?

From a digital economy perspective, there are many willing buyers for data centers and cell towers but fewer "able buyers" with the expertise to manage or even underwrite such complicated assets. We expect industrial M&A will have a fairly long run; however, high prices may reach a tipping point that prompts potential acquirers to look at other value-add investment opportunities.

"Will they, or won't they?" is the big question facing the **office** sector in 2022, and it is likely to have important implications for the year's M&A activity. We expect uncertainty will continue to drag on the sector until there is more clarity as to what the future of work will look like. Recent survey results show that slightly more than 50% of responding consumers agree that they feel safe to return to work, but nearly 20% disagree (figure 5).

Figure 5. Safety sentiment on return to workplace



Source: Deloitte Global State of the Consumer Tracker

A hybrid work model is likely to be predominant in the future, but much depends on geographic location (e,g., people on the East and West Coasts primarily working at home; and people in smaller cities dividing their time between home and office or fully back in the office). 2022 transaction activity, meanwhile, may remain on the slow side until deal teams can underwrite with more certainty. In addition, the continued surplus of subleased space could entice occupiers to try to take advantage of the favorable conditions[44] to renegotiate lease terms. REITs and landlords may continue to employ aggressive concession packages, particularly in urban gateway markets, to attract and retain tenants.[45]

Pricing pressure from increasing demand and inventory constraints, along with rising interest rates and inflationary pressures in the broader economy, could have a cooling effect on 2022 **residential** market M&A. Unless we see the current elevated pricing for desirable single- and multi-family assets level off to something more "normal," potential buyers may need to either pursue creative financing options or pass on deals if the value isn't there. In addition, a strong return-to-work rollout may keep people in major cities and temper migration to the suburbs.

Acquirers' appetite for grocery-anchored properties and upscale specialty retail should continue in 2022; however, a shakeout is likely for Class B and C indoor malls as more and more consumers opt to shop from the comfort of their homes. Aging properties' vacant square footage presents REITs and owner-operators with a strategic conundrum: Is it time to pivot to a new business model? Invest in a major makeover to create a high-profile retail and entertainment destination? Convert underperforming properties into last-mile distribution? Should they sell? Or is it time to shutter the stores and raze the buildings? For the past two years, predictions about the retail industry's future have seemed dire.[46] 2022 will present both new and familiar challenges, but it will likely offer opportunities to use strategic M&A to set the retail recovery in motion.

Finally, 2022 may be a turnaround year for the beleaguered hotel and leisure sector, as pandemic restrictions ease, people become more comfortable resuming normal activities, and travelers return to their favorite vacation destinations. Pent-up demand should boost hotel occupancy, with some sources projecting a return to pre-COVID-19 levels by 2023 or 2024.[47] This hospitality recovery will be leisure-led; the fate of downtown/CBD and convention hotel properties will likely remain in limbo as long as the resumption of business travel remains questionable.[48] The sector also has a major talent shortage: Millions of hospitality workers were laid off during the pandemic, pushing many of them to find new, often higher-paying jobs in other industries.[49] While US hotels were forecast to add around 200,000 direct operations jobs in 2021, that number is still about 500,000 below the industry's pre-pandemic level of 2.3 million employees.[50] Hospitality M&A could see an increase in 2022, with acquirers particularly interested in hotel, leisure, and gaming properties in traditional domestic vacation destinations such as Hawaii and Florida.

2022 real estate M&A trends and drivers

Realigning portfolios for greater value-generation

The pandemic's uneven impact across CRE sectors is prompting company leaders to emphasize and accelerate the process of realigning portfolio assets through organic and inorganic means[51] to hedge risks and generate greater value. While "core four" real estate (office, industrial, retail, and multi-family) remains the foundation of a diversified portfolio, institutional investors, REITs, and PE firms are increasingly funneling more of their investments into "alternative" assets such as data centers, cell towers, and movie studios—so much so that the alternative space has become more mainstream.

REITs tend to be identified with or locked into a certain asset class and, generally speaking, focus their M&A within that class. Realty Income Corp, a large public REIT, acquired VEREIT,[52] a Phoenix-based owner of offices, restaurants, stores, and other commercial properties to add scale, diversify into new growth areas, strengthen cash flow, and leverage financial and operational synergies. The companies also plan to spin off nearly all of their office properties[53] into a new, self-managed, publicly traded REIT,[54] with the main company focusing primarily on single-tenant net lease retail and industrial properties in the United States and United Kingdom.[55] In contrast, PE funds have more freedom to move among sectors when populating their portfolios. Over the past two years we have seen some PE firms move from general office and retail into formerly nontraditional sectors; KKR and Blackstone, for example, have made big M&A plays in the SFR, data center, and medical office/life sciences markets.

CRE investment options in 2022 are more varied than ever. A pricing gap between Class A and Class B and C space in second-tier metro office and retail properties may generate interest in lower-end assets. Last year's passage of the bipartisan $1 trillion Infrastructure Investment and Jobs Act (IIJA)[56] creates opportunities for new CRE development.[57] Booming e-commerce may be the impetus to convert unused retail space into storage and distribution facilities. Additionally, tired hotel brands that are losing marketplace appeal may need a new owner to drive a property reset. Investors' choices, as always, will depend on capital availability, return requirements, risk appetite, and—in the case of PE firms—if an asset is nearing the end of its hold period.

Real estate divestiture is another important driver of portfolio diversification. Among industry respondents to the Deloitte 2022 M&A Trends Survey, 44% said they have divested assets within the last 12 months, and 50% said they were considering doing so.[58]

Finally, as explored in the Deloitte 2022 Commercial Real Estate Outlook, CRE leaders should look at their portfolio assets through an environmental, social, and governance (ESG) lens. To support the transition to a lower-carbon economy, property holders can collect and assess data on the environmental impacts of building operations, implement resource efficiencies, and partner with developers who use sustainable practices and materials.[59] In addition to helping combat climate change, such business practices may add portfolio value. Sixty percent of Deloitte survey respondents believe that ESG initiatives are driving new business opportunities for their organization, and half think these initiatives are giving them a competitive edge.[60]

Because real estate investments come with unique risks and considerations, organizations should be strategic and intentional when making CRE part of their growth strategies. Deal teams should use tenant/end-user data, predictive models, geospatial variables, and other advanced analytics to help accurately predict future property valuations and tenant viability and support their investment, development, leasing, and repurposing decisions.[61]

Opportunity area: Real Estate-as-a-Service (REaaS)

Real estate owners and operators can unlock new sources of value and revenue by providing REaaS, which combines strategy, technology, and data to deliver digital and physical services—not just space—to tenants and users. Leveraging advanced digital technologies, an REaaS model could combine and cross-leverage smart-building capabilities across systems, enabling a flexible yet comprehensive infrastructure supporting end-user requirements under one roof and enhancing the tenant experience. Respondents to a Deloitte 2021 global survey of 400 CRE senior executives cited sustainable and energy-efficient properties, dynamic building designs, and flexible leasing models as the most promising enhancements to impact the tenant experience (figure 6).[62]

Figure 6. Unlocking value with REaaS

Importance of each aspect, ranked

Most important 1 2 3 4 5 Least important

Enhancements	Industry subsector					
	Overall	Office	Retail	Industrial	Residential	Specialty residential	Hospitality
Sustainable/energy-efficient properties	1	2	2	3	1	1	4
Dynamic building designs, such as reconfigurable spaces	2	3	1	2	3	3	2
Flexible leasing models (i.e., revenue sharing, management contracts, etc.)	3	1	5	1	2	4	3
Additional amenities	4	4	2	5	5	5	5
Interactive mobile apps for communication and updates	5	5	4	4	4	2	1

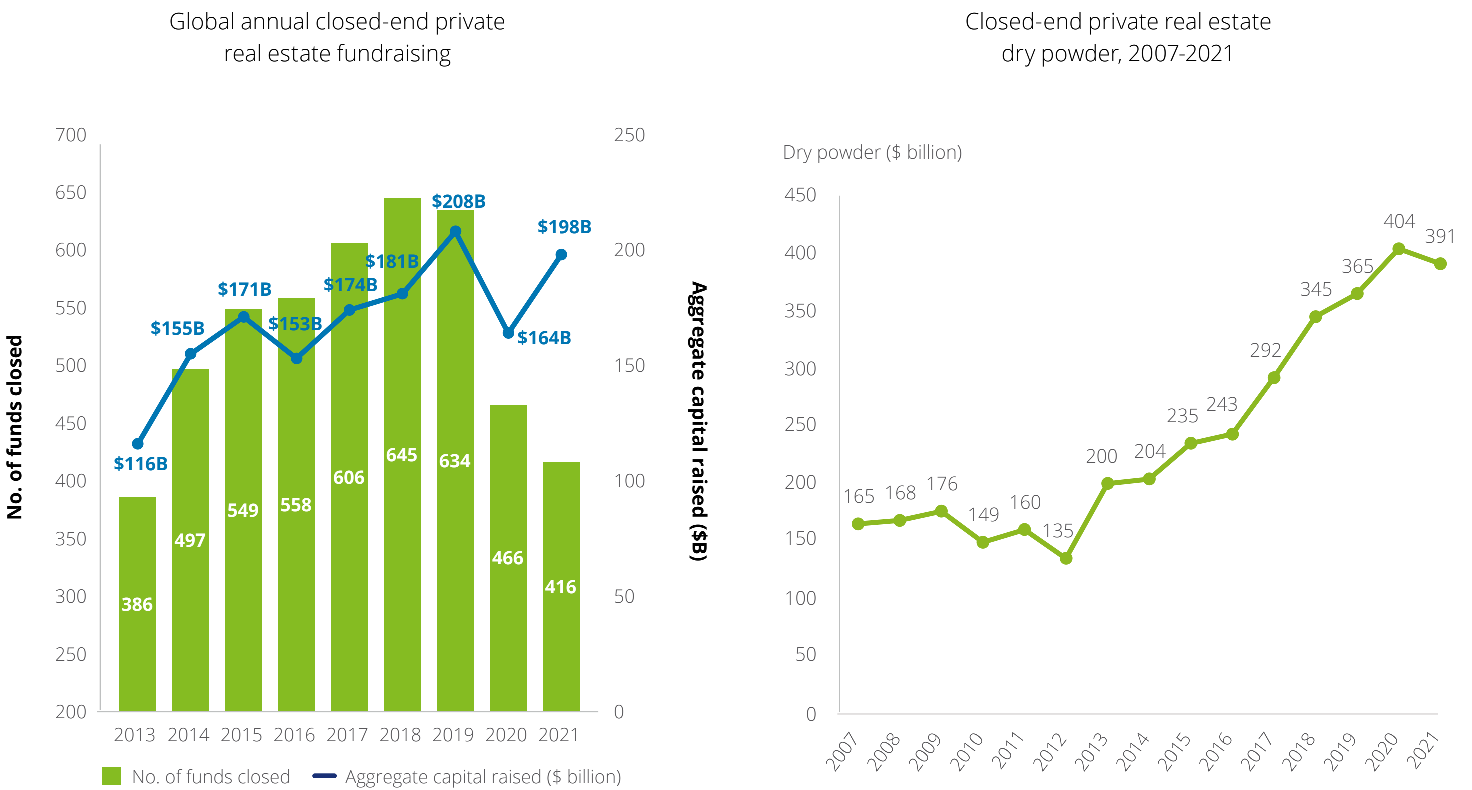
Source: Deloitte Center for Financial Services Global Outlook Survey 2021.

Enabled by an REaaS service model, property owners and operators can partner with tenants in new ways. Many retailers, in particular, are interested in REaaS because they see that as a way of offering differentiated services, including bars, restaurants, and other amenities, can enhance the retail experience, encourage people to visit their stores more frequently, stay longer, and spend more each visit.

Private equity firms continue their CRE buying spree

PERE 2021 fundraising may be below pre-pandemic highs and concentrated in fewer funds, but PE firms continue to hold tremendous reserves of "dry powder" to invest in commercial real estate (figure 7).

Figure 7. PERE fundraising below pre-pandemic highs, but plenty of dry powder to invest

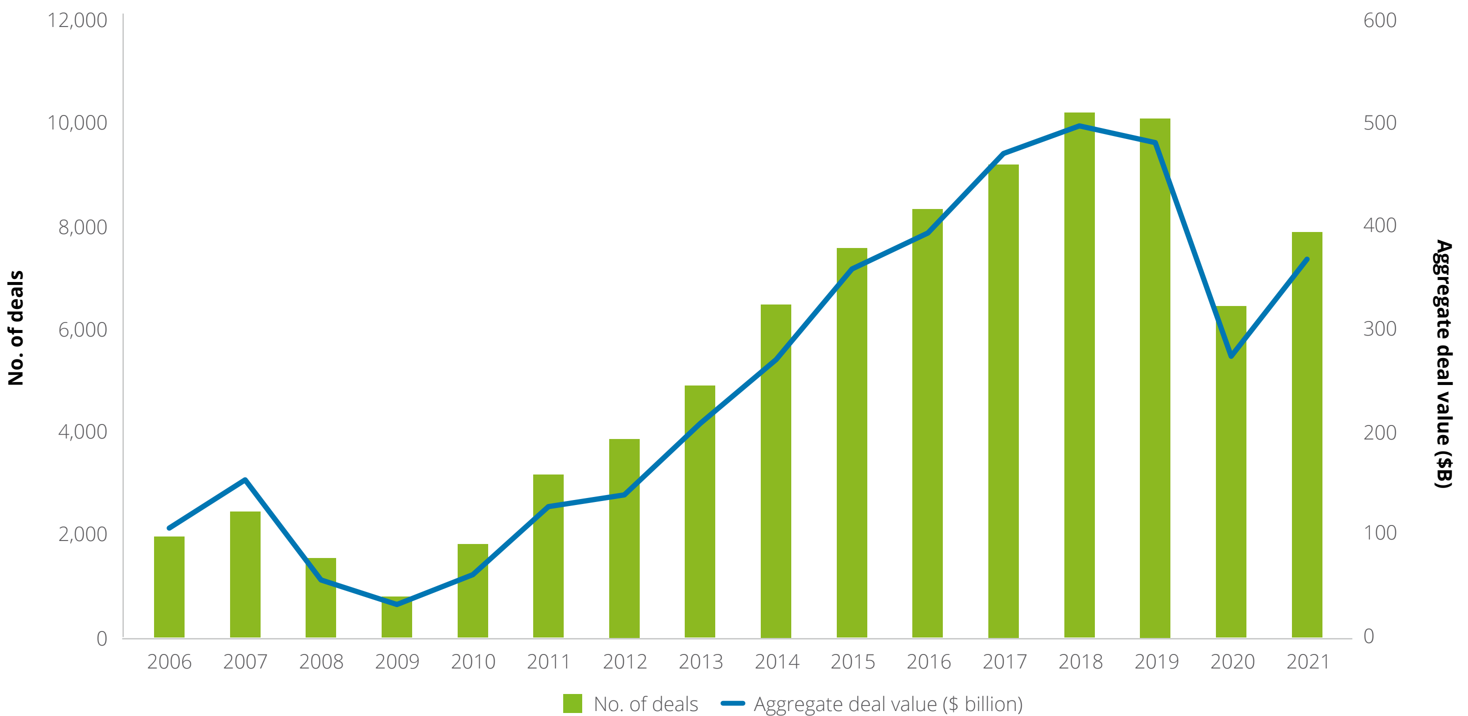


Source: Preqin Pro

Very low interest rates/yield from bonds and related instruments have driven many PE investors to real estate as a proxy for that asset class. PEs have also moved into open-ended, non-traded REITs—a major driver of CRE M&A activity—in addition to closed-end funds. Blackstone Real Estate Income Trust (BREIT) led 2021 non-traded REIT fundraising with $24.9 billion, followed by Starwood Capital with $6.3 billion.[63] And while the pandemic interrupted PE firms' multi-year buying spree in 2020, deal volume and value rebounded in 2021 (figure 8), building momentum for the coming year.

Figure 8. Private equity real estate activity

Yearly private equity real estate deals



Source: Preqin Pro

Among the major PE players, Blackstone funds have been incredibly busy of late, posting a laundry list of multibillion-dollar deals across the industrial, residential, and hotel and leisure sectors. Noteworthy 2021 announced and completed BREIT acquisitions include QTS Realty Trust (data center) for $10 billion,[64] WPT Industrial Trust (industrial REIT) for $3.1 billion,[65] and Home Partners of America (single-family homes for sale and rent) for $6 billion.[66]

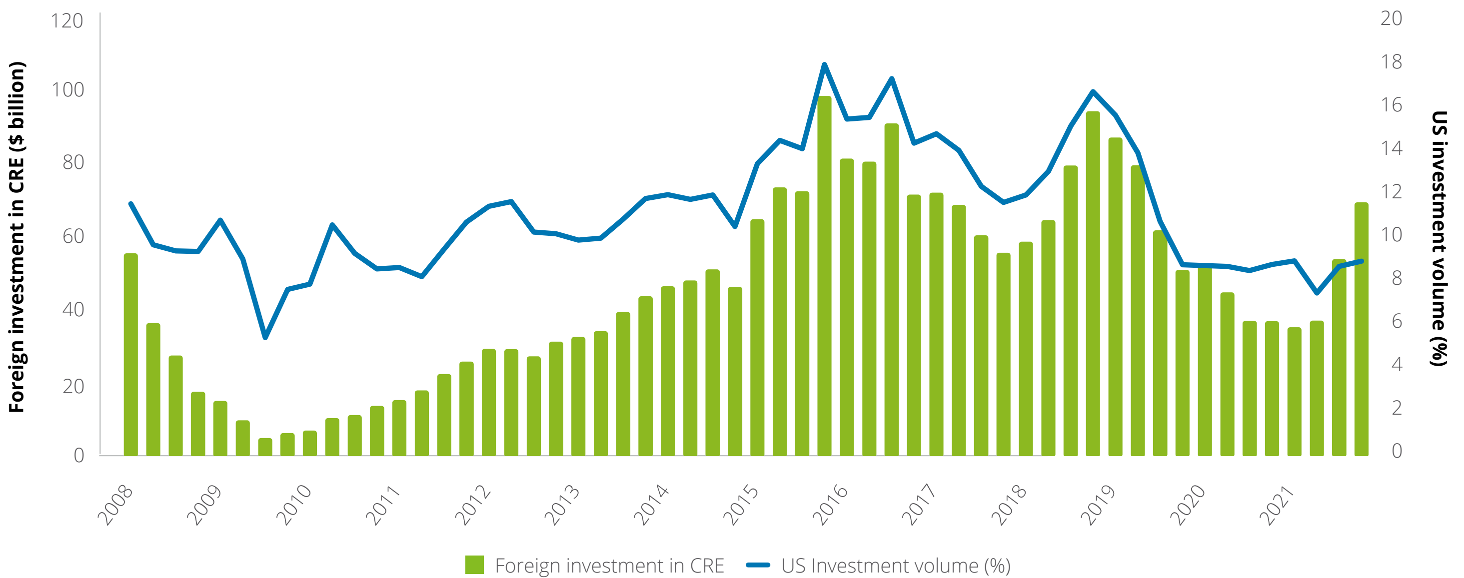
Closed-end fund Blackstone Real Estate Partners (BREP) acquisitions include Bluerock Residential (multi-family REIT) for $3.6 billion[67] and Extended Stay America and its paired-share REIT, ESH Hospitality, for $3.6 billion in a joint venture with Starwood Capital Group.[68]

Increasing appetite of foreign investors for US assets

COVID-19 variant uncertainty and travel restrictions contributed to middling foreign investment in US real estate in 2021, although interest from abroad began to show signs of life in the second half of the year, with a $53 billion gain contributing an overwhelming majority of 2021's $69 billion annual total.[69]

2021 foreign investment in US properties increased 90% from year-end 2020, and 37% from year-end 2019 (figure 9),[70] building momentum going into 2022.

Figure 9. Foreign investment in US CRE makes first notable move

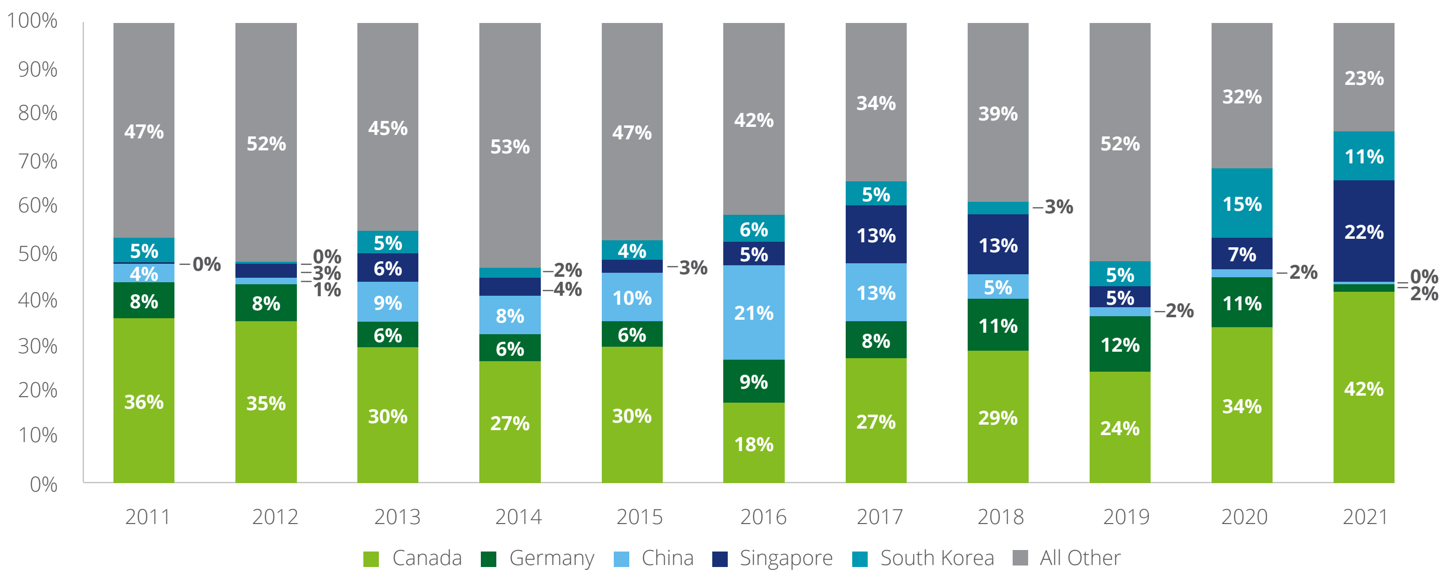


Note: Volume represented as four-quarter rolling average.
Source: Real Capital Analytics

Traditionally, foreign investors target Class A office properties in US gateway markets—New York City, Los Angeles, Washington, DC—because they're easy to manage, market themselves, and deliver high yields. However, we have been seeing an exodus from assets in such gateway markets to primary and secondary markets such as Seattle, Atlanta, and Austin. Also, recent indicators show that foreign investors are gravitating toward other asset types: Industrial grew from 15% to more than 30% of all foreign capital invested in US CRE since Q2 2020,[71] followed by multi-family at just under 30% of all 2021 capital invested.[72]

Among the contributors to 2021 US foreign investment, firms based in Canada had their most concentrated year in US real estate in over a decade, totaling 42% of transactions (figure 10).[73] And although Chinese capital was minimal for the third straight year, volume from other APAC countries soared, led primarily by Singapore, which has been uncharacteristically active over the past 12 months. Historically, Singapore accounts for approximately 6% of US foreign investment sources. In 2021 the country's investment share of total foreign investment was 23%, second behind Canada.[74] Singapore's surge is primarily attributable to two major institutional, high cash-on-hand funds, Mapletree and GIC, both of which are making forays into logistics and residential real estate.

Figure 10. Canadian investment peaks in 2021; Chinese capital absent for third straight year



Note: "All Other" refers to countries that historically have less than an average of 5% foreign investment share.

Percentages may not total 100% due to rounding.

Source: Real Capital Analytics

Between a record stockpile of dry powder globally, lower yields on CRE and traditional financial investments outside the United States, and geopolitical constraints, foreign companies will likely target US real estate in 2022 for many of the reasons they always have, and then some: ease of doing business, the wide range of asset types, and a bullish outlook on income growth, especially during periods of high inflation.

Potential impacts of higher inflation and interest rates on CRE M&A activity

We do not anticipate significant headwinds for 2022 CRE M&A arising specifically from accounting, regulatory, or tax influences, although some changes in focus among advisory and regulatory bodies (e.g., climate change; ESG issues) as well as the progression of (and increasing clarity around) certain country and global regulations and standards merit watching.

The combination of higher inflation and higher interest rates, however, has the potential to impact CRE company financials, operations, and M&A decisions in 2022. Inflation soared 7% in 2021, the largest 12-month increase since June 1982.[75] Real estate is often thought to be a "safe" investment and a hedge against inflation because it isn't subject to wild fluctuations[76] and investors generally are able to recoup higher leverage/interest costs by passing inflationary pressure on to tenants; for example, raising rents for residential properties, especially when occupancy rates are high and supply is limited. However, when costs are rising across the board but a company's earnings aren't rising commensurate to expenses, it may mean less available capital to apply against M&A. This can be especially troubling for the office and retail sectors, where new tenants may not be able or willing to accept rent increases on new leases or renewals.

For business leaders worried about what will happen with inflation, some economists expect that the current situation is transitory and likely to be quickly reversed,[77] perhaps within the next 12 to 18 months. If that does turn out to be the case, organizations can plan to simply manage a temporary shock while awaiting a return to normalcy.[78]

Added to inflationary concerns is the prospect of three or more increases in short-term interest rates in 2022, which US Federal Reserve Chair Powell alluded to at the Fed's December 2021 meeting.[79] The impacts of higher interest rates on CRE company financials and M&A activity can swing both ways: As interest rates rise so, too, will investment income, which increases cash flow that, potentially, can be applied to M&A. In another positive, higher interest rates typically increase company valuations, which can strengthen sellers' negotiating positions. Buyers, however, may not fare as well, as the cost of debt will go up and they will have to pay the price for those previously mentioned increased valuations. As mentioned earlier, real estate may also provide investors an inflation hedge, as rents and property values are highly correlated with rising consumer prices.[80]

Moving forward on 2022 real estate M&A opportunities

We expect CRE M&A to continue its momentum in 2022, although overhanging pandemic, economic, and geopolitical uncertainties may again influence sector-specific dealmaking. A large majority of CRE industry respondents to the Deloitte 2022 M&A Trends Survey (released in January) expressed positive opinions about the outlook for industry fundamentals over the next 12 months (figure 11), with nearly three-fourths (73%) anticipating increased transaction activity.[851]

Industrial and multi-family residential deal volume and value will likely continue to impress, as long as high prices and asset scarcity don't deter buyer enthusiasm. Sectors hit hard by the pandemic—office, retail, hospitality—may figure prominently in portfolio consolidations, diversifications, and conversions.

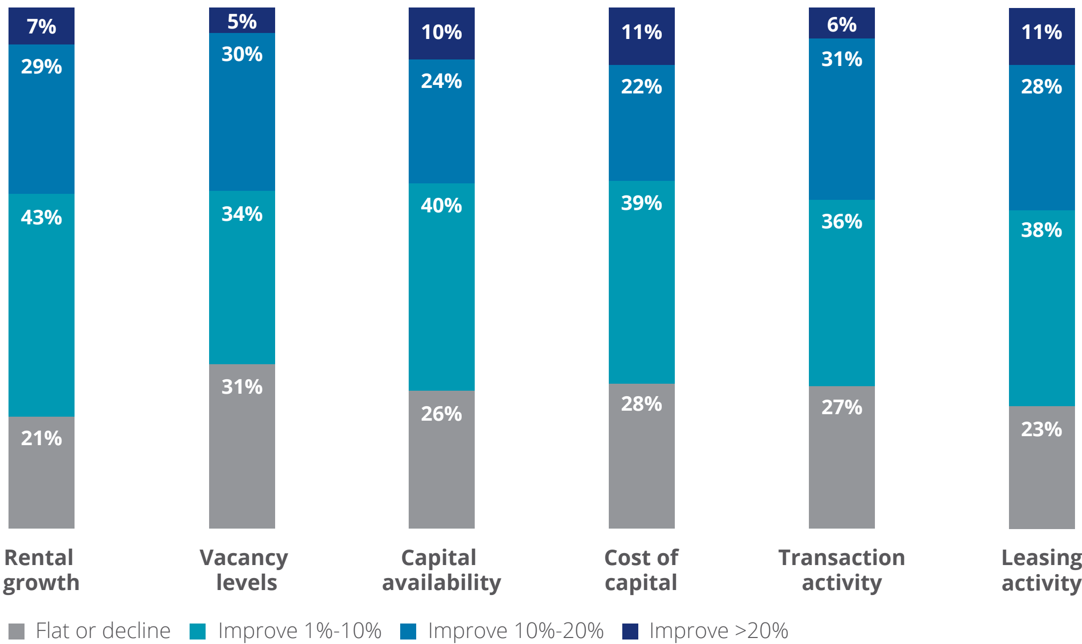
Deep-pocketed PERE firms will continue to look for buying opportunities among both premium and distressed properties. Foreign investors may add to their traditional (office) and alternative asset (industrial, multi-family) holdings.

As they formulate their 2022 M&A strategies, CRE leaders should remain alert to the impacts of higher inflation and higher interest rates. The ability to rapidly pivot and adapt in today's dynamic macroeconomic environment is an essential attribute of effective M&A deal teams. Finally, in anticipation of increased transaction activity, companies should consider expanding their finance department capabilities and systems to strengthen performance, improve access to capital markets,[82] and move M&A planning to action.

Figure 11. Generally positive outlook for 2022 CRE operating fundamentals

Respondents' opinions about the outlook for operating fundamentals are generally positive

Expected changes over the next 12 months



Note: Percentages may not total 100% due to rounding. A decline in vacancy level and cost of capital is noted as positive.

Source: Deloitte Center for Financial Services Global Outlook Survey 2021

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