Franklin L. Burns School of Real Estate & Construction Management
UNIVERSITY OF DENVER

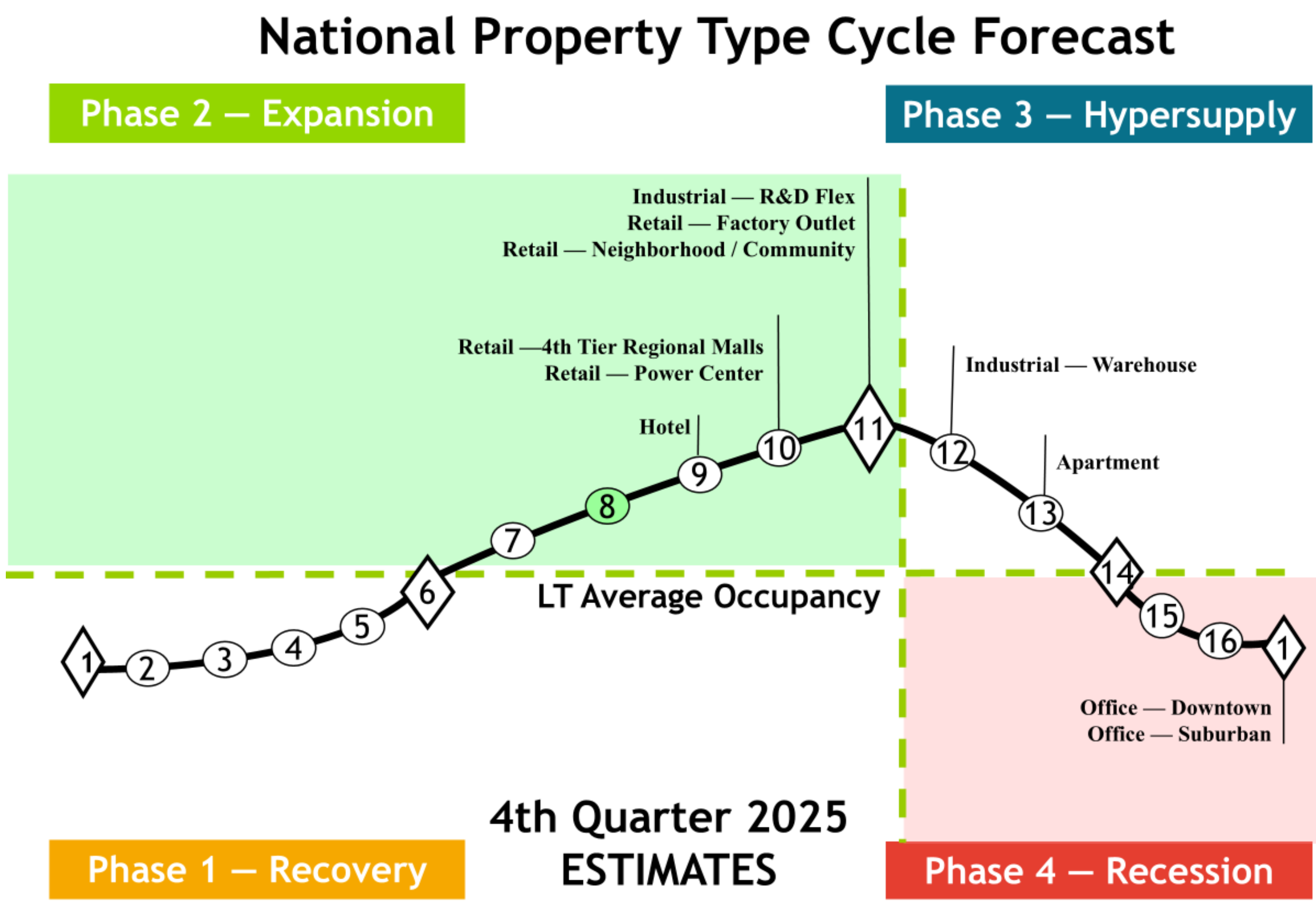
SHARING CONNEXION

MUELLER
REAL ESTATE MARKET CYCLE FORECAST

Fourth Quarter 2025 Estimates – February 2025

On one hand the economy is expected to slow, due to tariffs keeping inflation from declining, and interest rates high. On the other hand, if reshoring of manufacturing begins employment growth and spending could surge. If people go back to their offices, the post-Covid slowdown in downtown commerce could disappear and cities experience a resurgence. Construction activity should be high as the rebuilding from hurricanes, floods and fires begins – this should add to GDP growth in a significant way and at the same time restrain any potential for overbuilding in the commercial property sector. If the Trump administration can move the country in a new direction, 2026 could be a boom year.

Office occupancies are forecast to **be flat** in 4Q25, with rents to be **increasing 1.9%** quarter-over-quarter.
Industrial occupancies are forecast to **be flat** in 4Q25, with rents **increasing 3.4%** quarter-over-quarter.
Apartment occupancies are forecast to **be flat** in 4Q25, with rents **increasing 3.6%** quarter-over-quarter.
Retail occupancies are forecast to **increase 0.1** in 4Q25, with rents **increasing 1.5%** quarter-over-quarter.
Hotel occupancies are forecast to **be flat** in 4Q25, with RevPAR **increasing 0.5%** quarter-over-quarter.



Source: Mueller, 2025

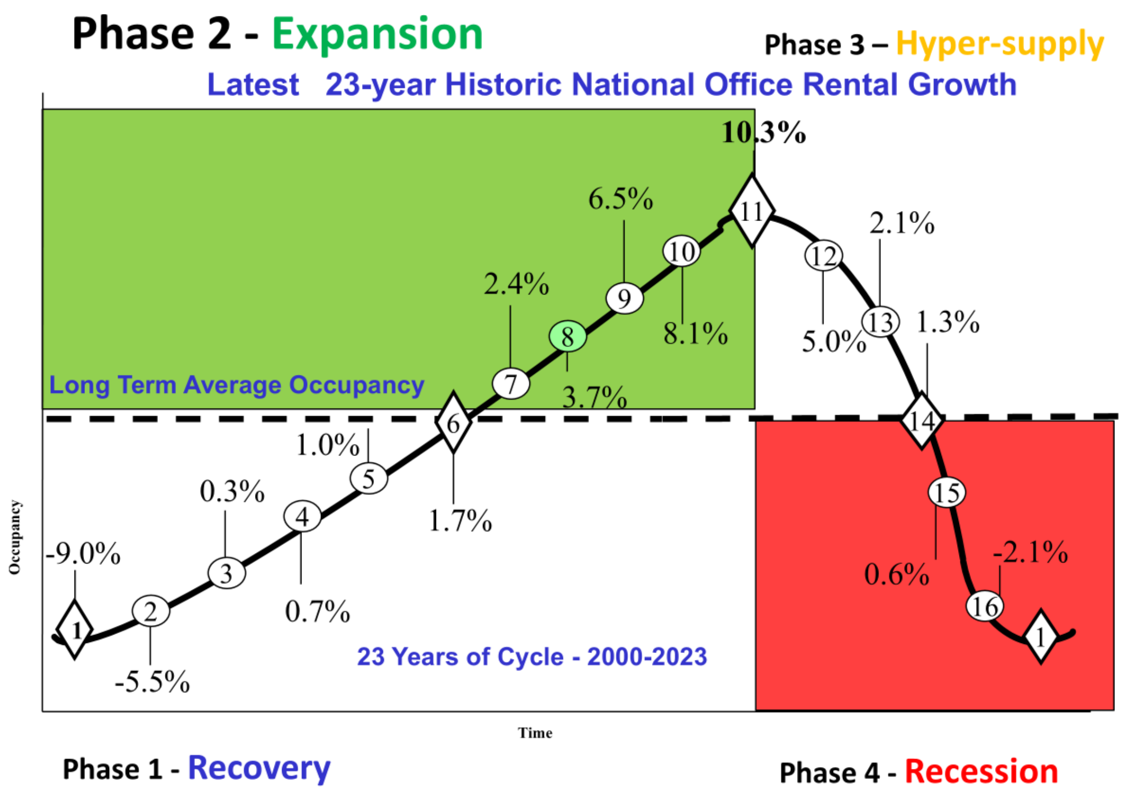
The National Property Type Cycle Locations graph shows relative positions of the sub-property types.

Glenn Mueller, Ph.D.– *Professor Emeritus*– Denver University www.du.edu/burns-school - **glenn.mueller@du.edu**
Director - **Sharing Connexion** –www.sharingconnexion.org– **glenn.mueller@sharingconnexion.org**

Franklin L. Burns School of Real Estate & Construction Management
UNIVERSITY OF DENVER

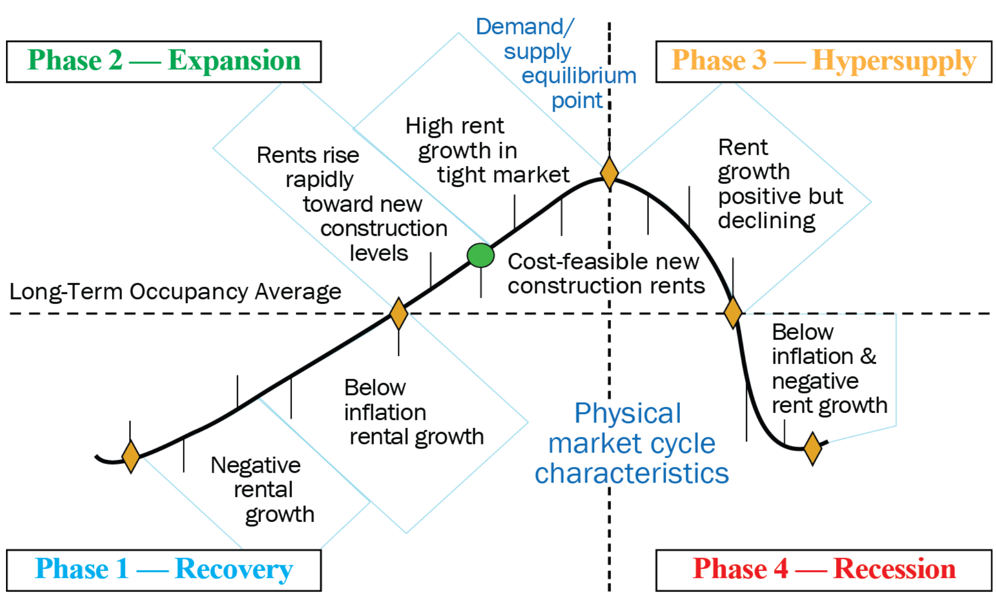
SHARING CONNEXION

The **Cycle Forecast** analyzes occupancy movements in five property types in more than 50 Metropolitan Statistical Areas (MSAs). The market cycle analysis should enhance investment-decision capabilities for investors and operators. The four property type cycle charts summarize almost 300 individual models that analyze occupancy levels and rental growth rates to provide the foundation for long-term investment success. Commercial real estate markets are cyclical due to the lagged relationship between demand and supply for physical space. Long-term occupancy average is different for each market & each property type. ***Long-term occupancy averages*** (points #6 & #14) are a key factor determining rental growth rates that drive income affecting commercial real estate returns.



Source: Mueller, Real Estate Finance 1998 Source: Mueller, 2024

Rental growth rates can be characterized in different parts of the market cycle, as shown below.



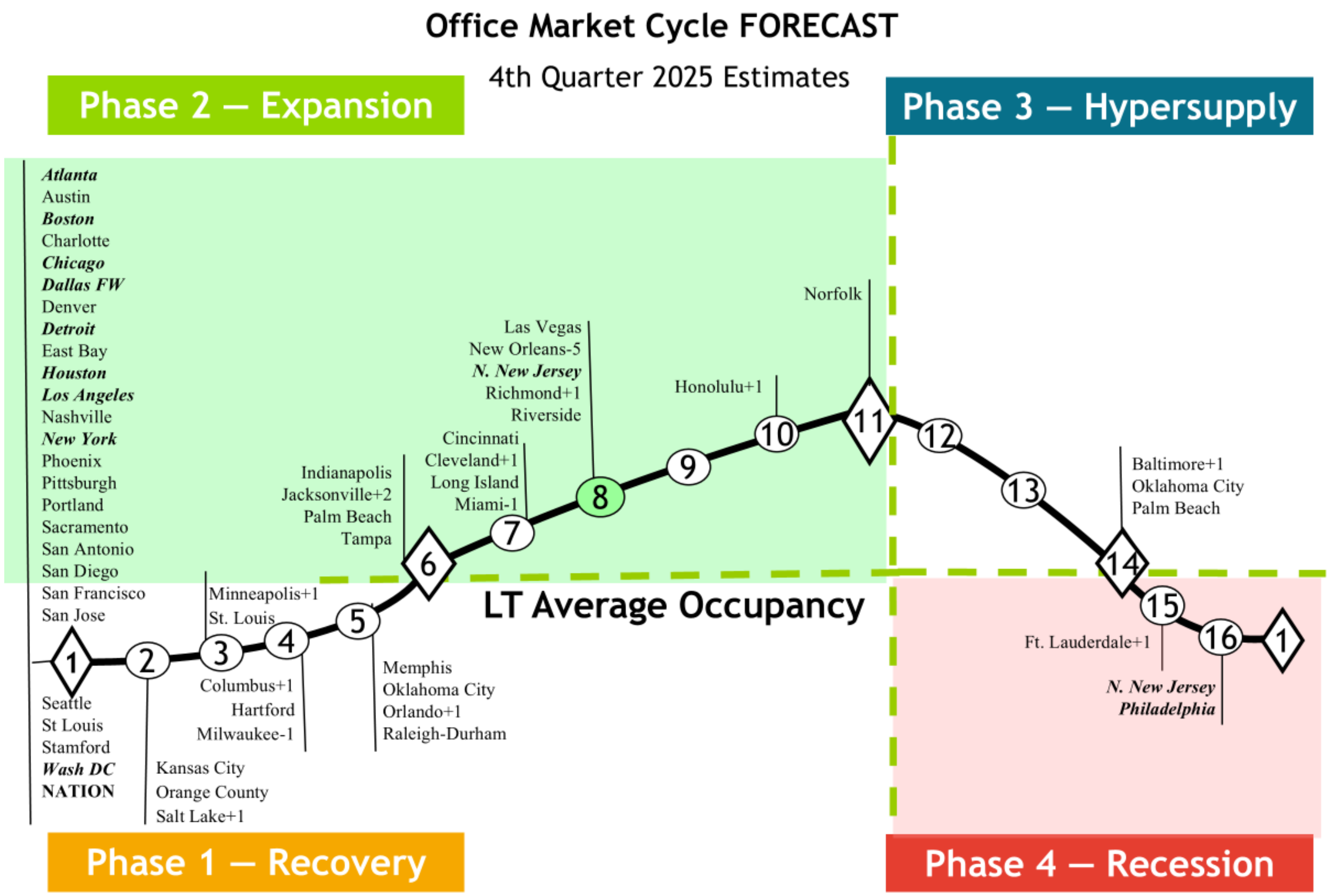
Source: Mueller, Real Estate Finance, 1998.

Franklin L. Burns School of Real Estate & Construction Management
UNIVERSITY OF DENVER

SHARING CONNEXION

OFFICE FORECAST

Office occupancies are forecast to **be flat** in 4Q25 and be **down -0.2%** year-over-year. Return to office is expected to accelerate with many major employers like Amazon requiring increased office attendance in 2025, artificial intelligence (AI) firms expanding, healthcare expansion, and the Trump administration requiring Federal workers back to office (yet at the same time laying off more Federal office staff). Most expiring leases are expected to renew at a 15 to 25% lower amount of square footage, as landlords right-size their office needs. New supply coming online should slow substantially in 2025 to less than 100 million square feet of completions, the lowest since 2012 - allowing occupancies to improve. However (while never exercised historically) all federal leases have a mandatory yearly cancellation cause. It has also been announced that the government may sell their own buildings, creating additional empty supply. We expect the market bifurcation to continue where premium class A space is in high demand with limited new supply causing high rent growth, while lower class space has increasing occupancy drops. We expect the national average office asking rents to **increase 1.9%** in 4Q25 and be **up 2.6%** year-over-year, with effective rents forecast to drop even faster.



Source: Mueller, 2025

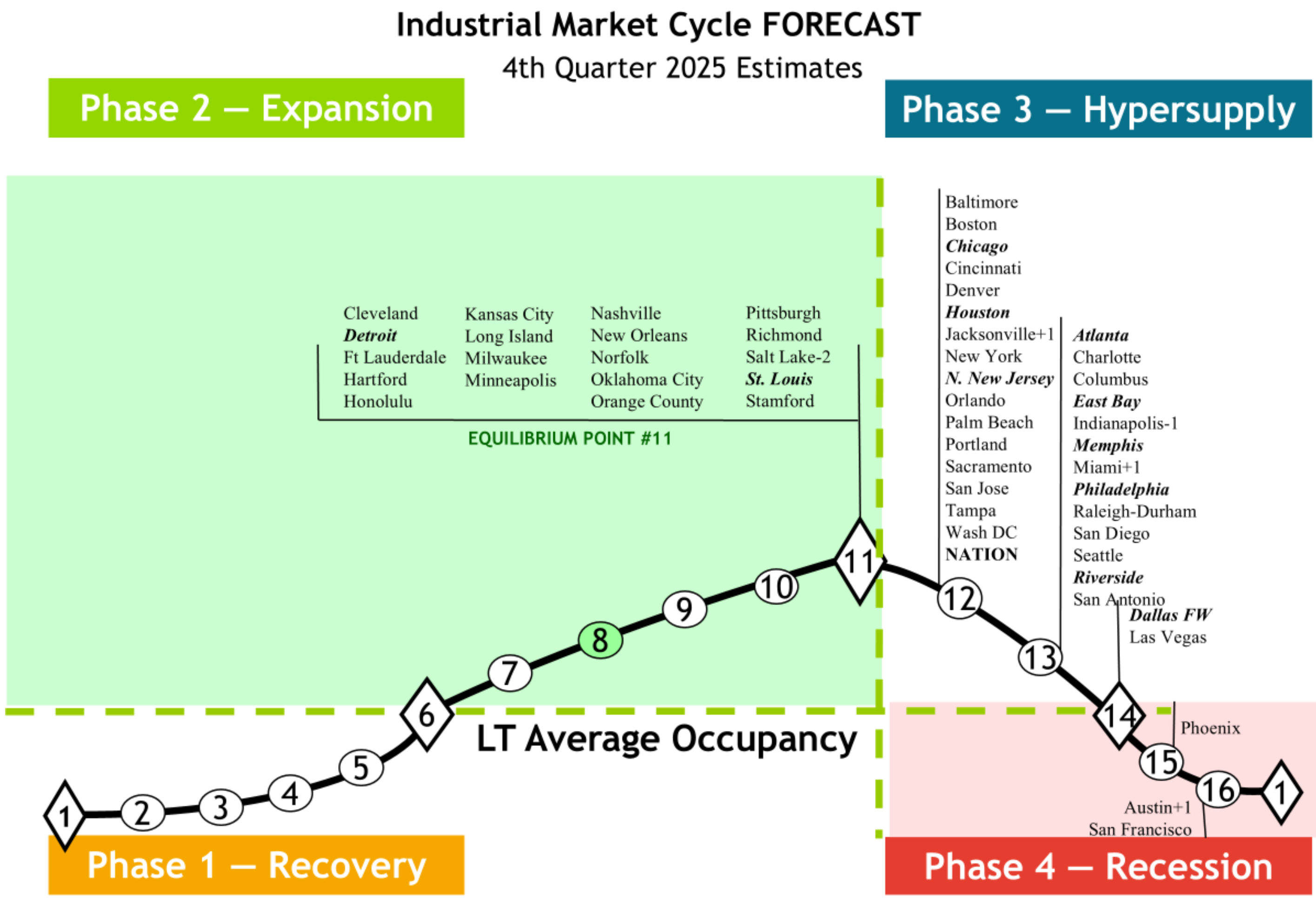
Note: The **11-largest office markets make up 50%** of the total square footage of office space that we monitor. Thus, the 11-largest office markets are in ***bold italics*** to help distinguish how the weighted national average is affected.

Markets do not always go through smooth forward-cycle movements and can regress or move backward in their cycle position when occupancy levels reverse their usual direction. This can happen when the marginal rate of change in demand increases (or declines) faster than originally estimated or if supply growth is stronger (or weaker) than originally estimated.

Franklin L. Burns School of Real Estate
& Construction Management
UNIVERSITY OF DENVER

INDUSTRIAL FORECAST

The national industrial occupancy growth is forecast to be **flat** in 4Q25 and be **up 0.2%** year-over-year. Industrial demand is somewhat of a jump ball in 2025, as tariffs slow imports and the demand for storing goods in the short term, but may increase demand if manufacturing is reshored, causing a jump in the need for goods & parts storage. If that happens it would be late in the year at best. Supply growth should slow more by 3Q25 allowing occupancies to turn the corner and increase in the second half of the year. Large bulk warehouses still have some downside due to oversupply, while the small bay R&D industrial market has had little new development, thus occupancy remains at pre-pandemic record highs. While market-asking rents are expected to have small increases, many existing leases will be renewed at more than 40% higher mark-to-market rates than when they were signed 5 to 10 years ago. We expect the national average asking rents to **increase 3.4%** in 4Q25 and be **up 5.5%** year-over-year.



Source: Mueller, 2025

Note: The **12-largest industrial markets make up 50%** of the total square footage of industrial space that we monitor. Thus, the 12-largest industrial markets are in ***bold italics*** to help distinguish how the weighted national average is affected.

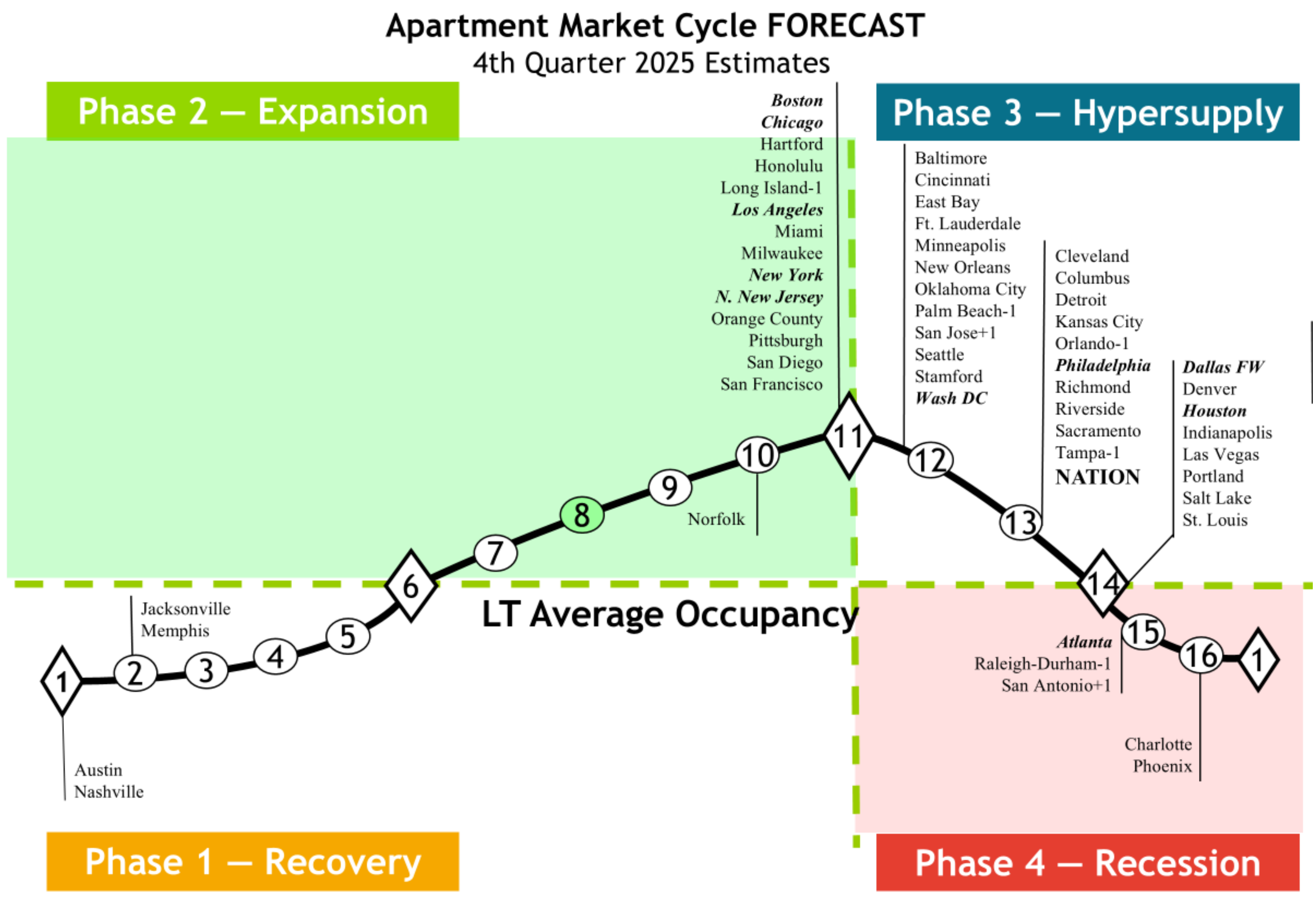
Markets do not always go through smooth forward-cycle movements and can regress or move backward in their cycle position when occupancy levels reverse their usual direction. This can happen when the marginal rate of change in demand increases (or declines) faster than originally estimated or if supply growth is stronger (or weaker) than originally estimated.

Franklin L. Burns School of Real Estate & Construction Management
UNIVERSITY OF DENVER

SHARING CONNEXION

APARTMENT FORECAST

Apartment occupancies are forecast to **be flat** in 4Q25 and be **up 0.3%** year-over-year. Positive job growth is expected to allow the strong demand experienced in 2024 to continue in 2025 at over 500,000 units. Supply is forecast to moderate to about 350,000 units (an almost 50% decline from 2024). More demand than supply translates to a positive net absorption for the year and improving occupancy. Most new supply is in the downtown Class A category where rent growth should be low, however, while the affordable, work force and low-income housing segments should continue with high occupancies and stronger than national average rent growth. We forecast the national average apartment rental rate to be **up 3.6%** in 4Q25 and **increase 7.5%** year-over-year.



Source: Mueller, 2025

Note: **The 10-largest apartment markets make up 50%** of the total square footage of apartment space that we monitor. Thus, the 10-largest apartment markets are in ***bold italics*** to help distinguish how the weighted national average is affected.

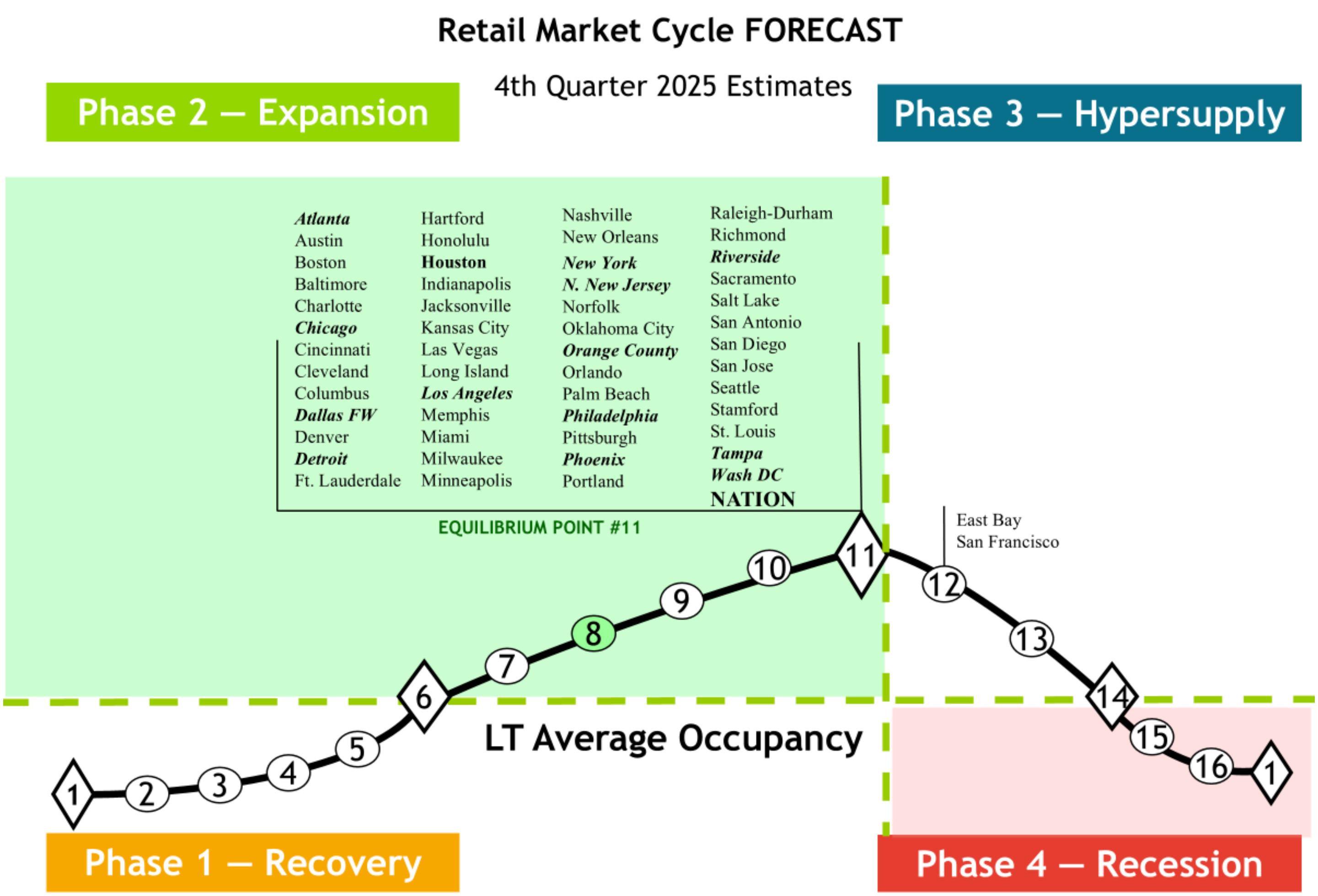
Markets do not always go through smooth forward-cycle movements and can regress or move backward in their cycle position when occupancy levels reverse their usual direction. This can happen when the marginal rate of change in demand increases (or declines) faster than originally estimated or if supply growth is stronger (or weaker) than originally estimated.

Franklin L. Burns School of Real Estate & Construction Management
UNIVERSITY OF DENVER

SHARING CONNEXION

RETAIL FORECAST

Retail occupancy is forecast to **increase 0.1%** in 4Q25 and **be flat** year-over-year maintaining its peak/equilibrium level. The low new home sales in the US created a major demand slowdown in the home goods retail sector, causing over 8,000 retail store closures. The largest number were with Walgreens, Advance Auto and Family Dollar. There are also many retail bankruptcies in progress such as Big Lots, Party City and Conn's. Fortunately, there is enough demand to absorb this space in the market. However, retailers may be more cautious in expansions, as they expect tariff induced price increases. Supply is forecast to continue its 10-year low growth rate, as construction and financing costs make feasibility difficult. We forecast the national average retail asking rental rates to **increase** 1.5% in 4Q25 and be **up 4.3%** year-over-year.



Source: Mueller, 2025

Note: The **15-largest retail markets make up 50%** of the total square footage of retail space that we monitor. Thus, the 15-largest retail markets are in ***bold italics*** to help distinguish how the weighted national average is affected.

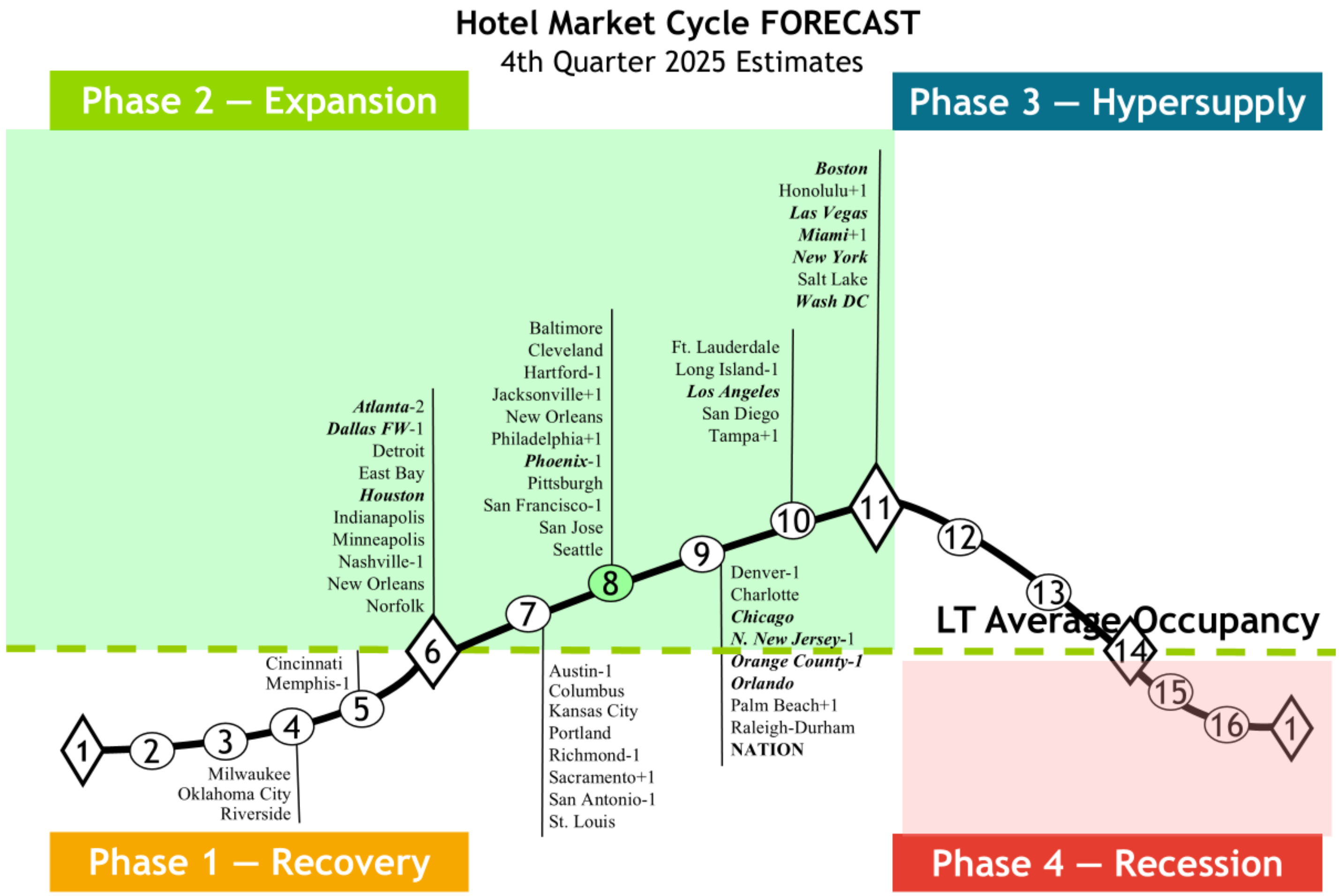
Markets do not always go through smooth forward-cycle movements and can regress or move backward in their cycle position when occupancy levels reverse their usual direction. This can happen when the marginal rate of change in demand increases (or declines) faster than originally estimated or if supply growth is stronger (or weaker) than originally estimated.

Franklin L. Burns School of Real Estate
& Construction Management
UNIVERSITY OF DENVER

SHARING CONNEXION

HOTEL FORECAST

Hotel occupancies are forecast to **be flat** in 4Q25 and **be flat** year-over-year. Many expect a reversal of fortune in 2025 as major city demand rebounds from back-to-office initiatives, while resort properties. (except luxury and upscale hotels) experience a decline as consumers have less money to travel, due to higher tariff and inflation induced living costs. With current high construction costs we expect lower new supply of about 150,000 units per year in 2025, thus helping to maintain the current occupancy levels. We expect the national average Revenue Per Available Room (RevPAR) growth to be **up 0.5%** for 4Q25 and **up 1.8%** year-over-year.



Source: Mueller, 2025

Note: The <u>14-largest hotel markets make up 50%</u> of the total square footage of retail space we monitor. Thus, the 14-largest hotel markets are in ***<u>bold italic</u>*** type to help distinguish how the weighted national average is affected.

Markets that have moved since the previous quarter are now shown with a + or - symbol next to the market name and the number of positions the market has moved is also shown, i.e., +1, +2 or -1, -2. Markets do not always go through smooth forward-cycle movements and can regress or move backward in their cycle position when occupancy levels reverse their usual direction. This can happen when the marginal rate of change in demand increases (or declines) faster than originally estimated or if supply growth is stronger (or weaker) than originally estimated.

Franklin L. Burns School of Real Estate & Construction Management
UNIVERSITY OF DENVER

SHARING CONNEXION

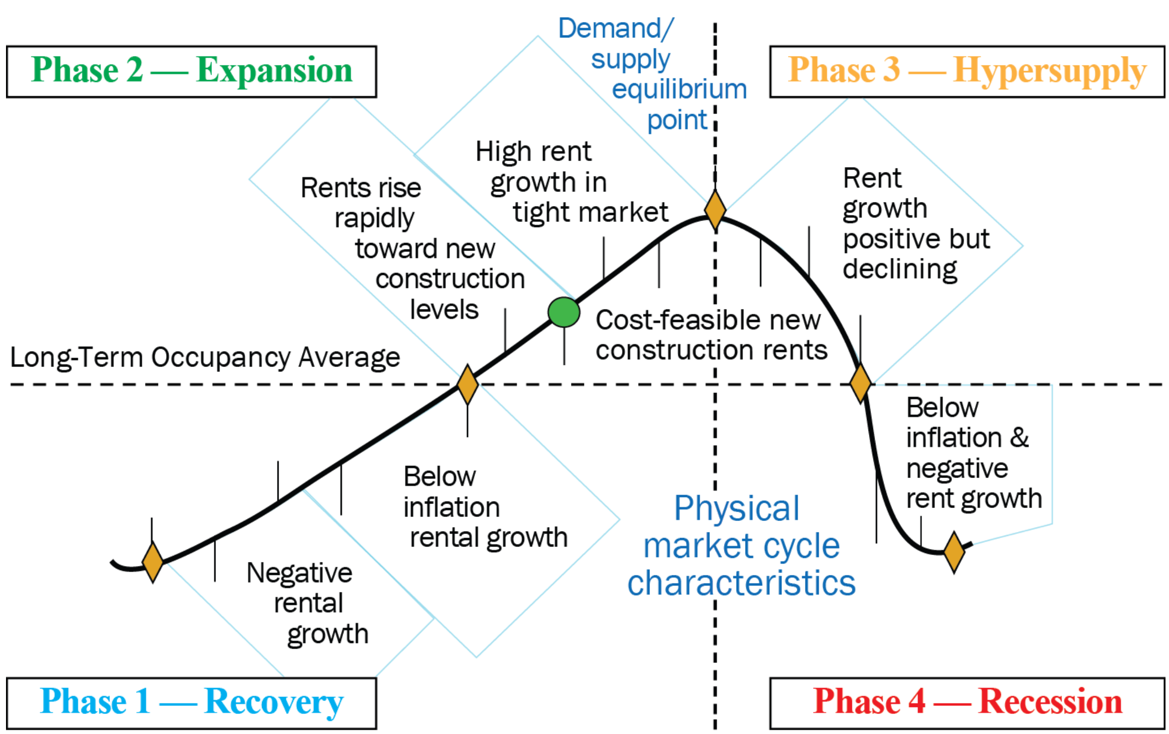
MARKET CYCLE ANALYSIS — Explanation

Supply and demand interaction is important to understand. Starting in Recovery Phase I at the bottom of a cycle (see chart below), the marketplace is in a state of oversupply from previous new construction or negative demand growth. At this bottom point, occupancy is at its trough. Typically, the market bottom occurs when the excess construction from the previous cycle stops. As the cycle bottom is passed, demand growth begins to slowly absorb the existing oversupply and supply growth is nonexistent or very low. As excess space is absorbed, vacancy rates fall, allowing rental rates in the market to stabilize and even begin to increase. As this recovery phase continues, positive expectations about the market allow landlords to increase rents at a slow pace (typically at or below inflation). Eventually, each local market reaches its ***long-term occupancy average*** whereby rental ***growth is equal to inflation***.

In Expansion Phase II, demand growth continues at increasing levels creating a need for additional space. As vacancy rates fall below the ***long-term occupancy average***, signaling that supply is tightening in the marketplace, rents begin to rise rapidly until they reach a "cost-feasible" level that allows new construction to commence. In this period of tight supply, rapid rental growth can be experienced, which some observers call "rent spikes." (Some developers may also begin speculative construction in anticipation of cost-feasible rents if they are able to obtain financing.) Once cost-feasible rents are achieved in the marketplace, demand growth is still ahead of supply growth — a lag in providing new space due to the time to construct. Long expansionary periods are possible and many historical real estate cycles show that the overall up-cycle is a slow, long-term uphill climb. As long as demand growth rates are higher than supply growth rates, vacancy rates should continue to fall. The cycle peak point is where demand and supply are growing at the same rate ***or equilibrium.*** Before equilibrium, demand grows faster than supply; after equilibrium, supply grows faster than demand.

Hypersupply Phase III of the real estate cycle commences after the peak/equilibrium point #11 — where demand growth equals supply growth. Most real estate participants do not recognize this peak/equilibrium's passing, as occupancy rates are at their highest and well above long-term averages, a strong and tight market. During Phase III, supply growth is higher than demand growth (hypersupply), causing vacancy rates to rise back toward the long-term occupancy average. While there is no painful oversupply during this period, new supply completions compete for tenants in the marketplace. As more space is delivered to the market, rental growth slows. Eventually, market participants realize that the market has turned down and commitments to new construction should slow or stop. If new supply grows faster than demand once the long-term occupancy average is passed, the market falls into Phase IV.

Recession Phase IV begins as the market moves past the long-term occupancy average with high supply growth and low or negative demand growth. The extent of the market down-cycle is determined by the difference (excess) between the market supply growth and demand growth. Massive oversupply, coupled with negative demand growth (that started when the market passed through long-term occupancy average in 1984), sent most U.S. office markets into the largest down-cycle ever experienced. During Phase IV, landlords realize that they could quickly lose market share if their rental rates are not competitive; they then lower rents to capture tenants, even if only to cover their buildings' fixed expenses. Market liquidity is also low or nonexistent in this phase, as the bid–ask to spread in property prices is too wide. The cycle eventually reaches bottom as new construction and completions cease, or as demand growth turns up and begins to grow at rates higher than that of new supply added to the marketplace.



Source: Mueller, Real Estate Finance, 1996.

Glenn R. Mueller, PhD – Professor Emeritus - https://daniels.du.edu/burns-school - glenn.mueller@du.edu
Director – www.Sharingconnexion.org – glenn.mueller@sharingconnexion.org