



BULL REALTY NATIONAL NET LEASE SURVEY - AUGUST 2017

By Nancy Miller, CCIM/MBA, President - National Net Lease Group, Bull Realty, Inc.

Email: NMiller@BullRealty.com

The Bull Realty National Net Lease Investment Group completed a survey of single tenant net lease (STNL) owners, developers and brokers. The survey was sent to over 4,000 individuals in early August of 2017. The objective was to gain a better understanding of investor preferences and their STNL goals in the next 12 months. The survey investigated the following areas:

- The key factors investors consider when buying a STNL investment.
- Investor perceptions of interest rate and CAP rate trends over the next 12 months.
- The most important reason for their decision to buy, for those planning to buy STNL properties in the next 12 months.
- The MOST and LEAST favored types of tenants that STNL investors are seeking.
- Preferred locations for purchasing STNL investments.
- How investors “source” or find investment properties.

The respondents were a mix of investors, developers, lenders and real estate brokers as following:

Investors	67%
Real Estate Brokers	13%
Lenders	11%
Developers	9%

TOPLINE FINDINGS:

» Investors top considerations when buying STNL investment properties:

1. Quality of the tenant (including a strong tenant guarantee) - 62.5%
2. Sufficient remaining lease term - 54%
3. Quality of the underlying real estate - 52%

» Investor perceptions of interest rate and CAP rate trends in the next 12 months?

1. CAP rates will rise - 56%
2. Interest rates will rise - 70%

» The greatest motivators to buying STNL properties in the next 12 months:

1. When they find “the right property” - 50%
2. Plan 1031 exchange - 8.5%
3. Want to lock in interest rates now - 4%
4. They are not planning to purchase a property - 23%

BULL REALTY NATIONAL NET LEASE SURVEY - AUGUST 2017

» MOST and LEAST Favored tenant types:

1. **Most** favored tenant types:
 - › Dollar stores - 50%
 - › Medical/health - 48%
 - › Fast food (QSR) - 37%

2. **Least** favored tenant types:
 - › Special Use - 27%
 - › Casual dining - 17%
 - › General retail - 11%
 - › Auto/tire - 11%
 - › Industrial - 11%

» Preferred regions to buy STNL properties:

1. The Southeast - 71%
2. States with no state income tax - 42%

» Sources of Buying/Finding STNL properties:

1. Work through brokers - 51%
2. Use a combination of brokers and the internet - 34%
3. Return to the prior sellers, particularly to developers - 9%

DETAILED FINDINGS:

Let's take a closer look at the survey categories and hear what respondents say!

1. KEY FACTORS considered AS MOST IMPORTANT when selecting a STNL investment?

10 factors were ranked ordered by importance from MOST to LEAST important. The tabulation below represents the highest percentage of respondents choosing what they thought to be the top three factors they consider when selecting a STNL investment:

1. QUALITY of tenant (strong tenant guarantee)	20.8%	6. PRICE (regardless of CAP rate)	6.3%
2. Remaining LEASE TERM (more being better)	18%	7. NEW or RECENT construction	5.6%
3. QUALITY of underlying real estate	17.4%	8. RENT/SF is at or below market)	4.9%
4. CAP Rate (the higher the better)	11.1%	9. Leases have PERIODIC rent increases	4.1%
5. NNN investments only	11.1%	10. NN preferred to improve the CAP rate	1%

BULL REALTY NATIONAL NET LEASE SURVEY - AUGUST 2017

Quality of tenant and remaining lease term are also factors that drive the investment cost higher. A strong guarantor is likely to command a lower CAP rate, regardless of lease term, providing that the underlying real estate is easy to re-purpose. Respondents seem to indicate that higher CAP rates and NNN leases are important factors as well, but not as important as the top 3 factors.

The following responses reflect the single MOST important factor chosen as the **first choice** by respondents is as follows. This demonstrates the overall importance of QUALITY of tenant, remaining lease term and quality of the underlying real estate in a STNL investment selection.

1. QUALITY of tenant (strong tenant guarantee)	33%	6. CAP Rate (the higher the better)	6%
2. NNN only	21%	7. Price (regardless of CAP rate)	2%
3. Remaining LEASE TERM (more being better)	19%	8. NN preferred to improve the CAP rate	0%
4. QUALITY of underlying real estate	10%	9. Leases have PERIODIC rent increases	0%
5. NEW or RECENT construction	8%	10. RENT/SF is at or below market)	0%

2. Interest Rate and CAP Rate Expectations for the next 12 months

Next, respondents were asked what interest rates and CAP rates would do in the next 12 months.

	CAP Rates	Interest Rates
Likely to stay the same	24%	20%
Likely to increase	56%	70%
Likely to decrease	7%	0%
I do not know what will happen	13%	10%

The results show that majority of respondents think that both CAP rates and interest rates will increase over the next 12 months, with a stronger sense of this regarding interest rates. Historically, as interest rates rise, CAP rates will also rise, but lag somewhat behind them. Sellers and investors remain concerned about the spread between interest rates and CAP rates to keep the yield attractive enough for investors.

3. Single Most Important Motivator for Investor Buying in the Next 12 Months

This question is not based on the property characteristics or the tenant type, but rather on what is triggering a buying decision. They will purchase:

1. When they find "the right property".	50%
2. If doing an IRS 1031 exchange.	8.5%
3. To lock in interest rates now.	4%
4. NOT planning to purchase a property.	23%

BULL REALTY NATIONAL NET LEASE SURVEY - AUGUST 2017

4. FAVORED TENANTS...

From a list of 8 tenant categories, respondents were asked to rank their choice of preferred tenants. The choices included fast food (QSR), dollar stores, auto/tire related, casual dining, medical/health related, general retail, industrial, and special use/other.

The favored tenant preferences are as follows:

Tenant Type	MOST Preferred Tenant Types
1. Dollar stores	50%
2. Medical/health related	48%
3. Fast food (QSR)	37%
4. Auto/Tire	26%
5. Casual dining	13%
6. General retail	13%
7. Industrial	9%

Top Preferred Tenants: Dollar stores offer long lease terms, have available new construction and are a financially strong, publicly traded company. While medical/health related tenants (Fresenius, Aspen Dental, urgent care, etc.) are also in the Top 2, they have a higher price point, less availability of location and lower CAP rates. However, due to the generally higher barriers to entry and building costs, this type of tenant is less likely to relocate. Looking down the preferred list, it is no surprise that QSR's are also in the top 3 favored type tenants. They generally have favorable real estate, ease of re-purposing and more frequent rent increases than favorites #1 and #2. However, QSR's have more franchise operators, which increase the investment risk in the minds of investors.

The least favored tenant preferences are as follows:

Tenant Type	LEAST Preferred Tenant Types
1. Specialty/Other	27%
2. Casual dining (least favorite)	18%
3. General retail and Industrial	11%
4. Auto/tire related	11%
5. Industrial	11%
6. Dollar stores	9%
7. Fast food (QSR)	8%
8. Medical/health related	3%

Looking at the **LEAST favored tenant types** (the bottom 3), it is no surprise that the casual dining space (O'Charlie's, Chiles, Applebee's, Ruby Tuesdays, etc.) has the least popularity. These restaurants are struggling to re-define and re-invent themselves and attract more Millennials.

BULL REALTY NATIONAL NET LEASE SURVEY - AUGUST 2017

5. Preferred Regions to Purchase STNL Properties

Respondents had the option of choosing multiple responses showing their preferences in regions that they will consider buying. The distribution of regional preference is below:

Southeast - 71%
States with no state income tax - 42%
Midwest - 21%
Southwest - 20%
Rocky Mountain Region - 12%
Northeast - 11%
West Coast - 11%
Pacific Northwest - 11%

The Southeast and states with no state income tax are preferred by STNL buyers.

6. How do investors find STNL properties?

Respondents indicated that 51% of them use brokers as a primary way to identify properties while along with personal search (internet, etc.) is done by 34% and 9% go back to the sellers that they previously purchased from.

7. Sources of Buying/Finding STNL properties

The high demand and limited supply of quality STNL properties in the current environment requires investors to be work hard to find properties meeting their criteria. Respondents were asked how they “source” or search for STNL properties.

1. Work through brokers - 51%
2. Use a combination of brokers and the internet - 34%
3. Return to the prior sellers, particularly to developers - 9%



BULL REALTY NATIONAL NET LEASE SURVEY - AUGUST 2017

CONCLUSION:

Key factors when purchasing a STNL property? Study findings reveal that respondents prefer purchasing STNL properties that have strong tenant guarantees, sufficient remaining lease term and possess underlying quality real estate. Surprisingly, CAP rates and price were less of a priority leading to the conclusion that STNL investors are looking at long term, stable investment properties.

What about interest rates and CAP rates? Most respondents forecast that they will rise in the next 12 months. When will investors buy? 50% of respondents say that they will buy when they see the right property. This speaks to the patience STNL investors show.

Preferred tenant types. STNL investors, given the choice of many different tenant types, had the strongest preference for dollar stores, medical/health related and fast food (QSR). The LEAST favored tenant types included specialty STNL and casual dining.

Where do STNL investors prefer to buy? The clear majority prefer either the Southeast or states with no state income tax, followed by the Midwest. Ultimately, due to limited supply, investors are likely to consider most areas of the country if they meet their preferred investment characteristics.

How do STNL investors source (find) properties? The majority of respondents reported that they work through brokers and do some internet research on their own. Given the aforementioned issue of supply, coupled with the concern for quality, investors find that full time real estate professionals have a greater awareness of on and off market investment opportunities.

For additional questions or comments, please contact Nancy Miller, President – National Net Lease Group, Bull Realty, Inc. 404-876-1640, ext 118 or NMiller@BullRealty.com.