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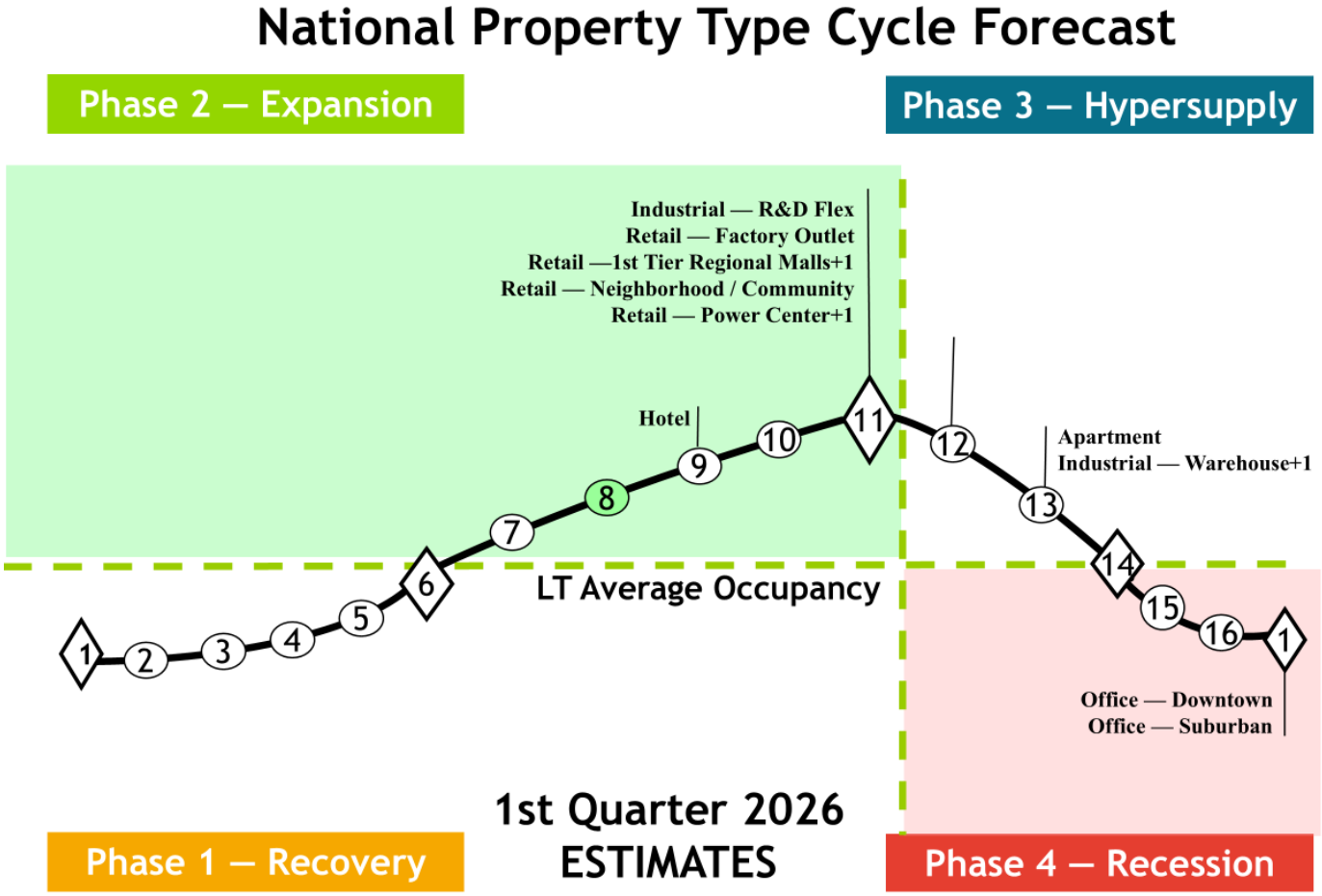
MUELLER
REAL ESTATE MARKET CYCLE FORECAST

First Quarter 2026 Estimates – May 2026

2025 should see some GDP growth from the promised government fiscal stimulus and extended tax cuts. We estimate that this should help to keep the moderate employment growth continuing through the rest of 2025. Remember, employment growth is the #1 cause of increased demand for all property types. However, goods price increases from tariffs may slow consumer spending and GDP growth. These uncertainties make business leaders pause on both business expansion and hiring. Remember, uncertainty is the #1 cause of indecision. Real estate markets are estimated to be mostly in equilibrium in 2026.

Office occupancies are forecast to **be flat** in 1Q26, with rents **increasing 0.2%** quarter-over-quarter.
Industrial occupancies are forecast to **be flat** in 1Q26, with rents **increasing 0.7%** quarter-over-quarter.
Apartment occupancies are forecast to **be flat** in 1Q26, with rents **increasing 0.7%** quarter-over-quarter.
Retail occupancies are forecast to **be flat** in 1Q26, with rents **increasing 0.4%** quarter-over-quarter.
Hotel occupancies are forecast to **decrease -0.1%** in 1Q26, with RevPAR **increasing 0.1%** quarter-over-quarter.



Source: Mueller, 2025

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

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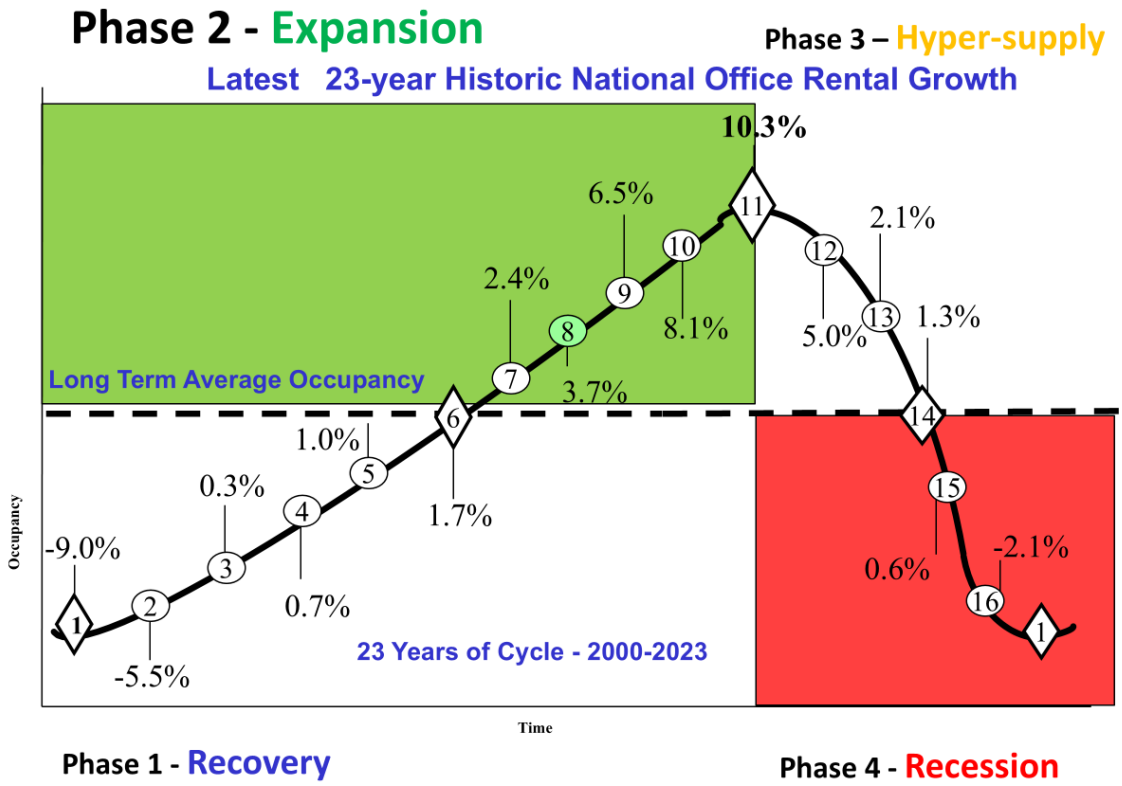
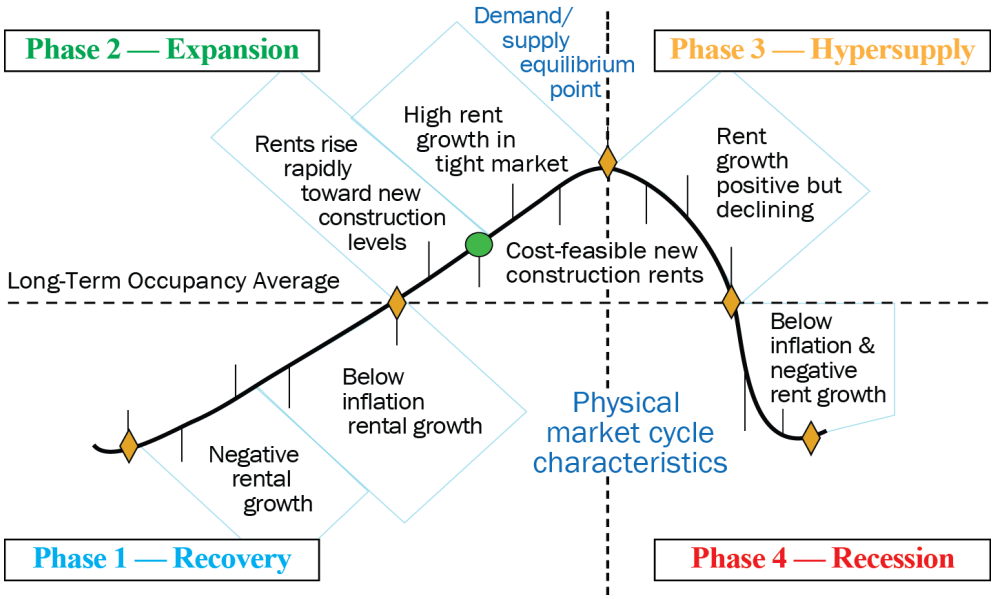
The **Cycle Forecast** analyzes occupancy movements in five property types in more than 50 Metropolitan Statistical Areas (MSAs). The market cycle analysis should enhance investment-decision capabilities for investors and operators. The four property type cycle charts summarize almost 300 individual 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.

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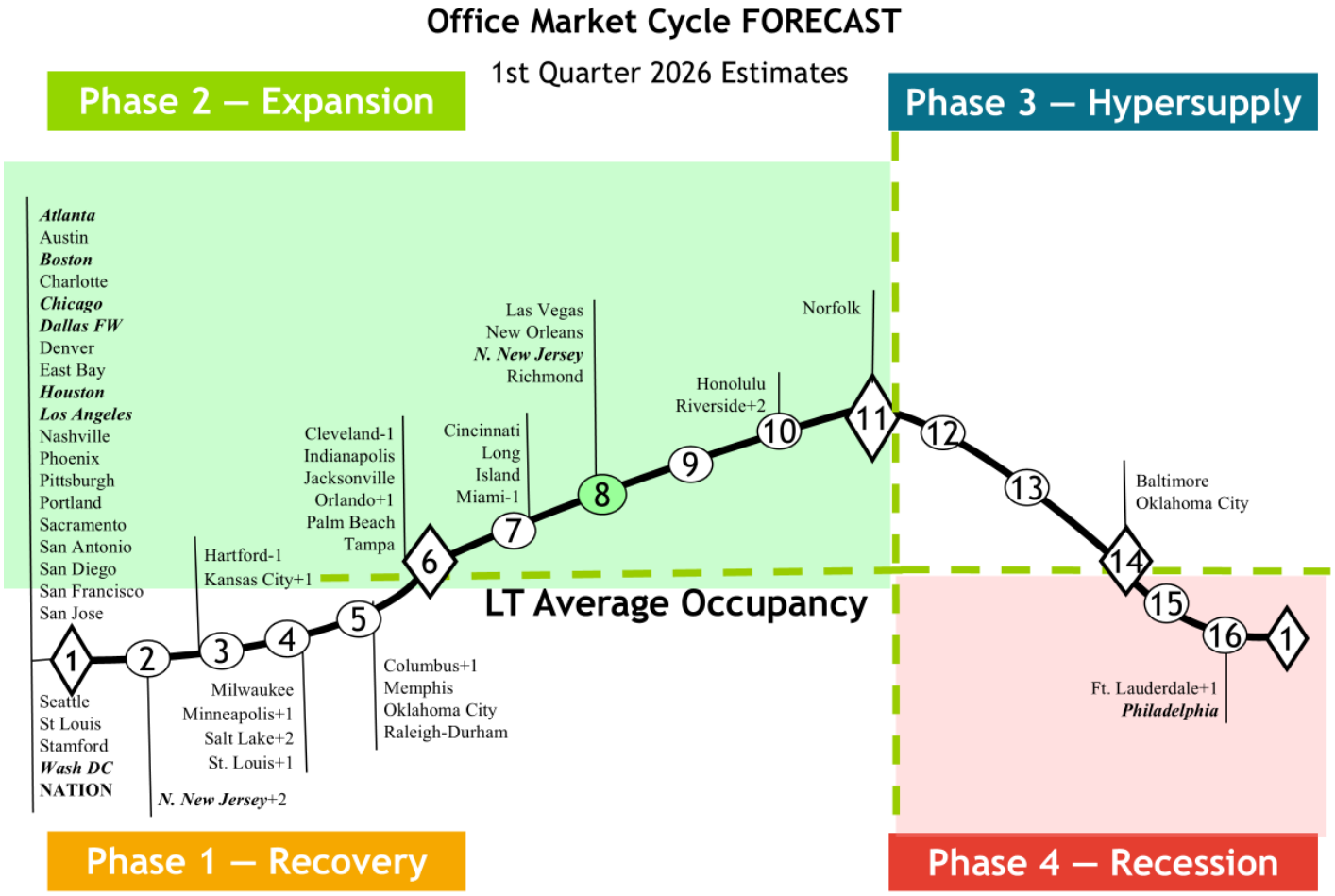
OFFICE FORECAST

Office occupancies are forecast to **be flat** in 1Q26 and be **down -0.3%** year-over-year. We expect the uncertainty of tariffs and government layoffs to lead employers to pause on employee expansion through most of the rest of the year. The good news is that new supply completions should be slowing throughout the rest of the year, thus occupancy levels should not decline by any significant percentage. We do not know if office-to-apartment conversions can have a meaningful impact on supply reduction at this point. We expect many firms to keep the current office space level they have, in anticipation of more in-office work, but the bifurcation of strong demand for premium Class A space versus declining demand for all other office space levels creates a have/have not environment. We expect the national average office asking rents to **increase 0.2%** in 1Q26 and be **up 1.1%** year-over-year, with effective rents forecast to decline.



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.

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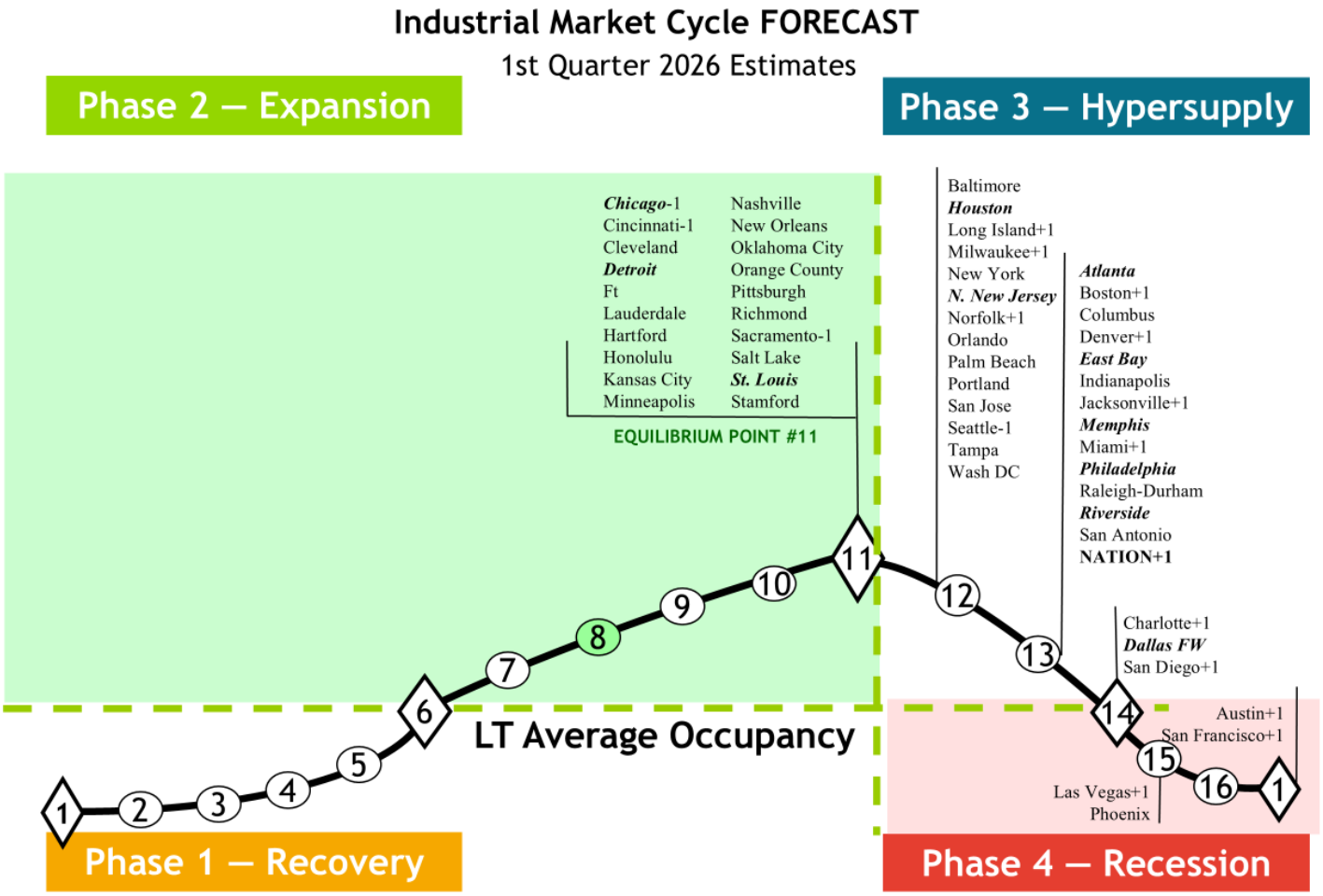
INDUSTRIAL FORECAST

The national industrial occupancy growth is forecast to be **flat** in 1Q26 and be **down -0.4%** year over year. We do not know which way demand might go in 2025, as tariffs pushing up prices, slows demand for industrial spaces,. Both higher daily goods prices, and low new home sales reduce all home good and furniture demand. On the other hand, if tax cut extensions are successful and the tariff negotiations conclude (as they seem to be with China and Britan so far) then demand could be positive for the year. We expect the national average asking rents to **increase 0.7%** in 1Q26 and be **up 2.9%** 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.

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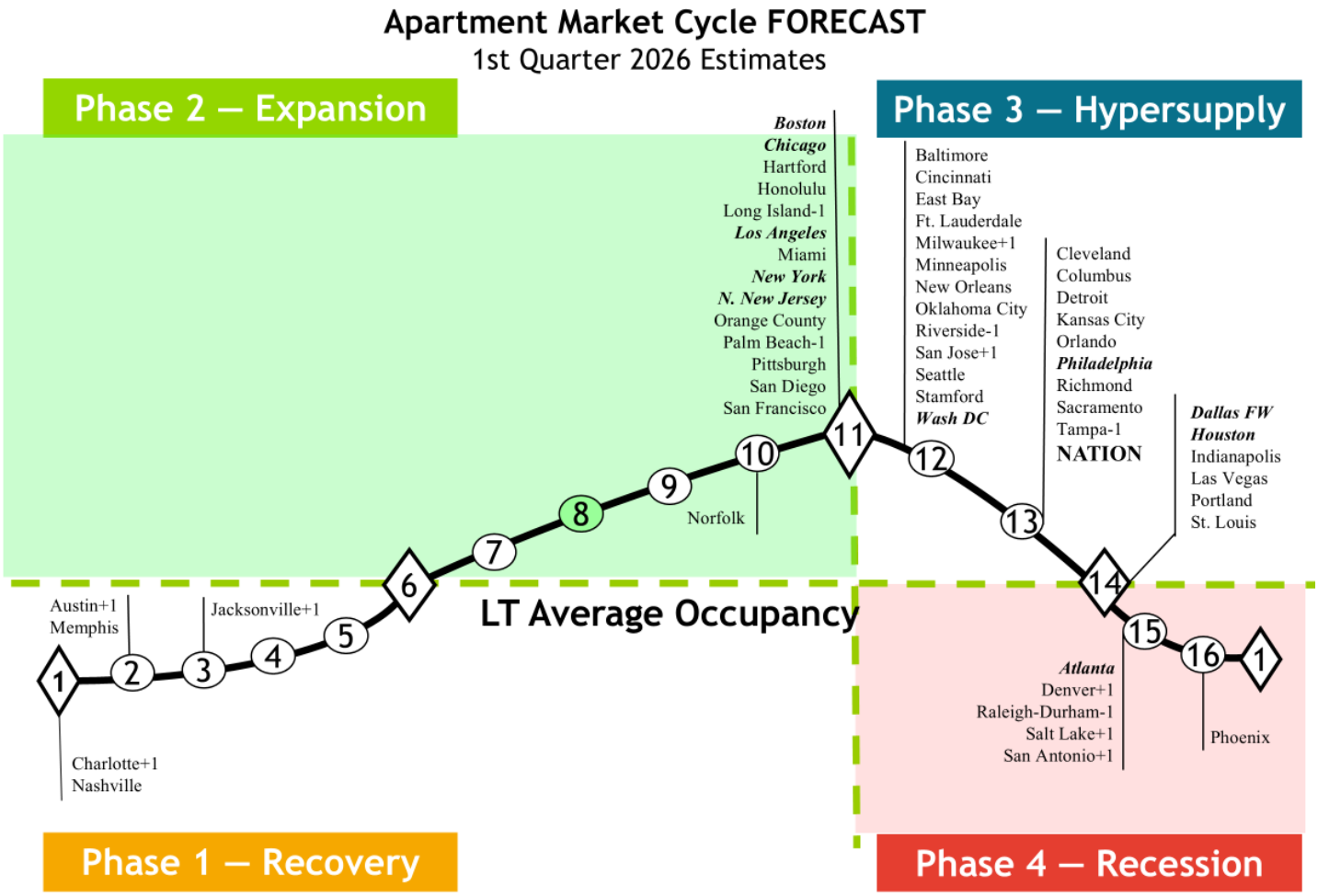
APARTMENT FORECAST

Apartment occupancies are forecast to **be flat** in 1Q26 and be **up 0.1%** year-over-year. Demand prospects look good for 2025 as Generation Z kids come out of school and get their first job, in addition many baby boomers are now entering their time to sell their house and go back to a rental unit, with no hassles and more social interaction opportunities. The supply pipeline is expected to slow to less than 80,000 units over the next 3 quarters, thus allowing for positive absorption to restart and occupancies to turn positive by year end. Affordable and workforce housing should , as always, to be in high demand, keeping occupancies in this sub-property type very high. We forecast the national average apartment rental rate to be **up 0.7%** in 1Q26 and **increase 2.7%** 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.

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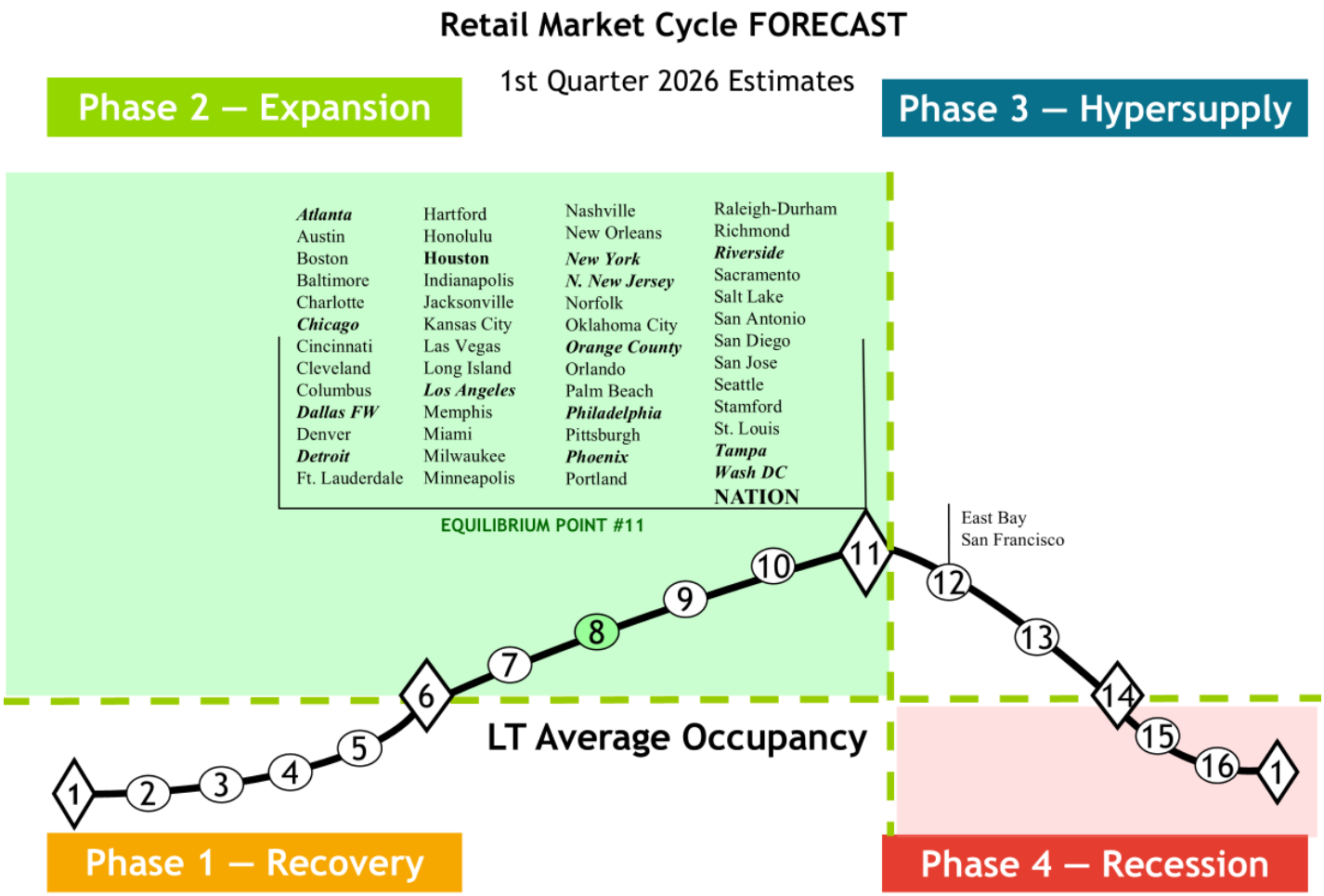
RETAIL FORECAST

Retail occupancy is forecast to **be flat** in 1Q26 and **be flat** year-over-year maintaining its peak/equilibrium occupancy level. We expect the substantial demand for new space to continue throughout 2025/6 and vacant space with good location to re-lease quickly. The limited new supply should be more expense, thus continuing to put a cap on new development. Bankruptcies of some national chains and more move-outs in lower performing locations are the only headwinds in 2025/6. Assuming the economy stabilizes in the second half of 2026, retail should be in a good position to maintain its peak/equilibrium location in the cycle. We forecast the national average retail asking rental rates to **increase** 1.5% in 1Q26 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.

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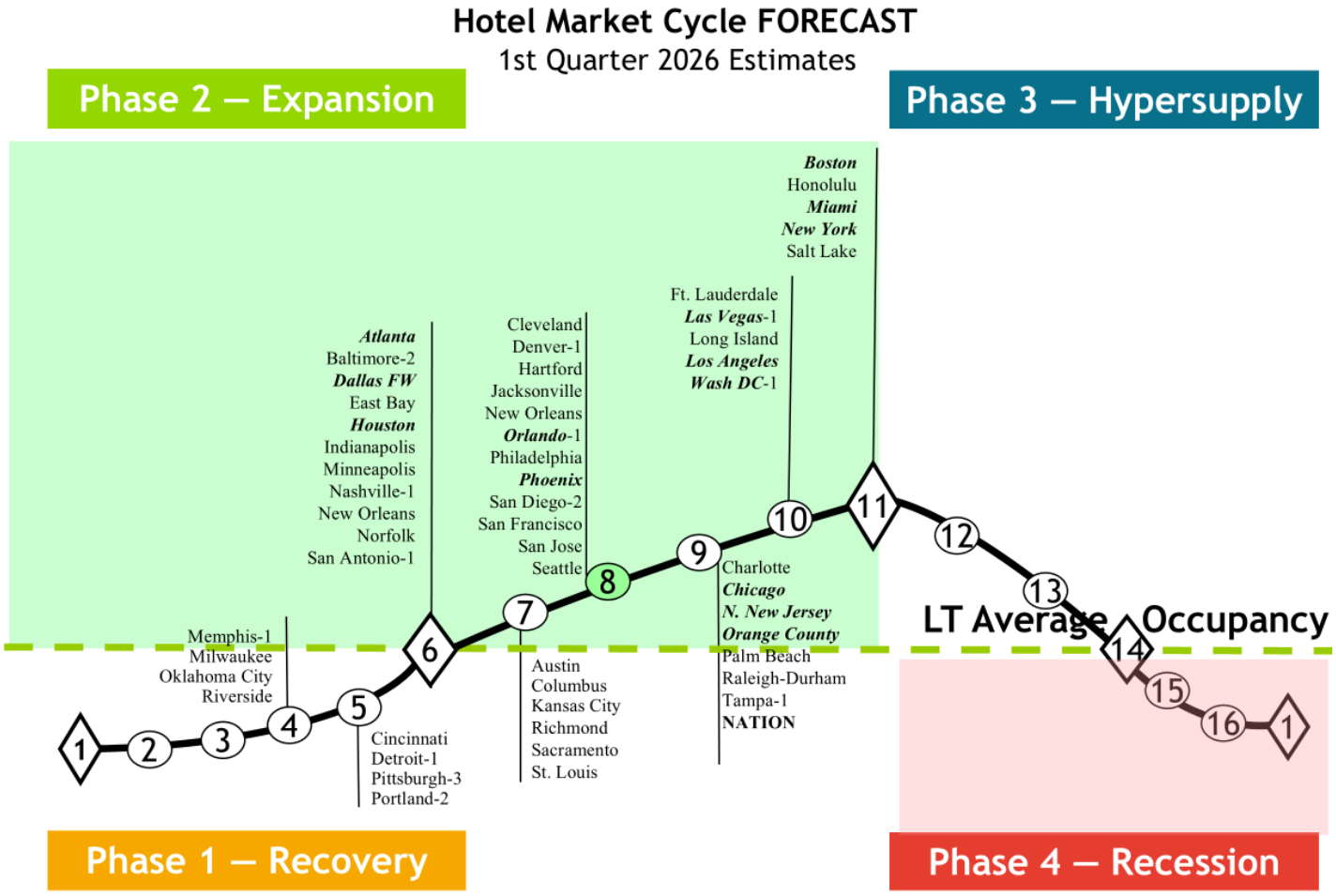
HOTEL FORECAST

Hotel occupancies are forecast to **be down -0.1** in 1Q26 and **be down -0.3%** year-over-year. Hotel demand should be very economy dependent in 2025, as trade and travel are dependent on economic growth. While increasing wages should translate into more recreational travel, higher product inflation could use up all the excess spending money. Higher interest rates and construction costs have put major restrictions on new supply, thus allowing the markets to be more in balance with low new supply. New hotel loans dropped to 1/3 of normal historic flow levels, and that is expected to continue in 2025/6. We expect the national average Revenue Per Available Room (RevPAR) growth to be **up 0.1%** for 1Q26 and **up 0.6%** year-over-year.



Source: Mueller, 2025

Note: The 14-largest hotel markets make up 50% of the total square footage of retail space we monitor. Thus, the 14-largest hotel markets are in ***bold italic*** 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.

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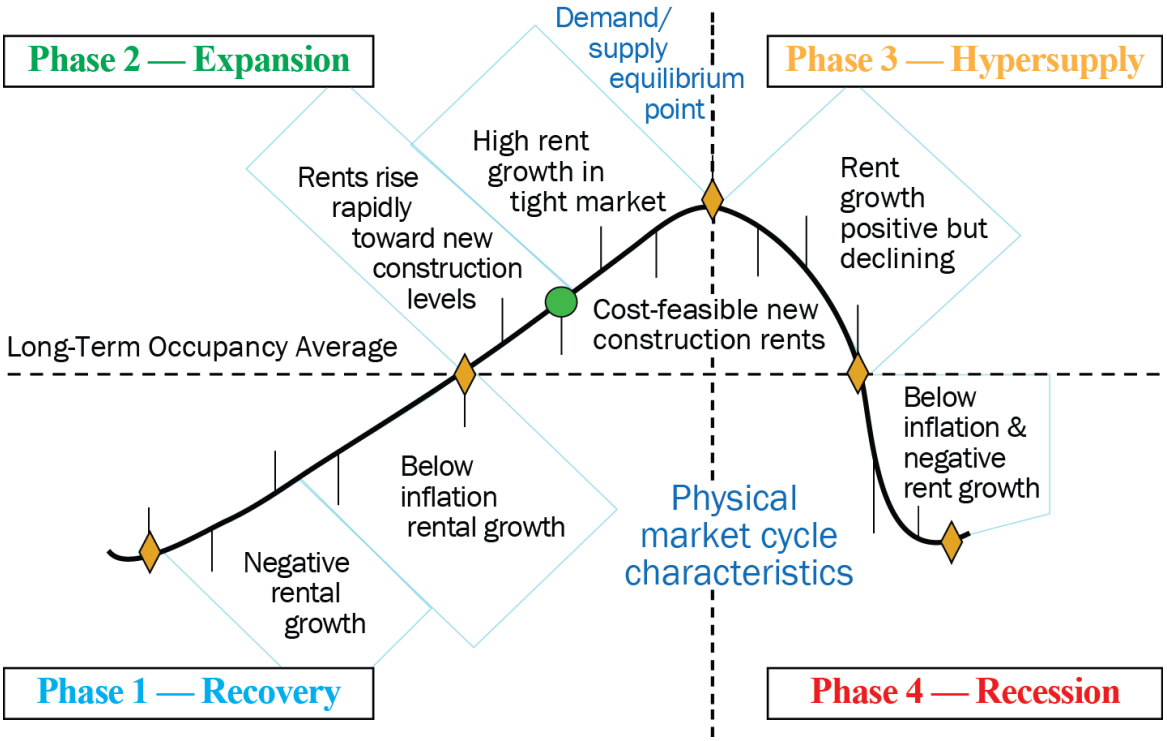
MARKET CYCLE ANALYSIS — Explanation

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.

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