

Q4 2022 Cap rate report

U.S. Capital Markets Net Lease Group

The Net Lease sector rounded out 2022 in a very steady fashion, quite the opposite of other sectors, even though interest rates have continued to trickle upward as the Federal Reserve hopes to taper inflation numbers. Across the different Net Lease sectors, cap rates generally increased between Q3 and Q4, averaging a 37.9 bps upward change. While this may seem troubling for investors, in the face of rising global tension, rising interest rates, and other macroeconomic headwinds, this increase pales in comparison with other sectors such as office.

With smaller price points making turbulent debt markets irrelevant in a lot of cases, private and institutional buyers have flocked to Net lease assets as a hedge against inflation, and unpredictable stock markets. This can be illustrated when comparing the rise in 10-year Treasury yields and cap rates of single tenant net lease assets. What is particularly interesting is the stark contrast in deal volume between Q3 and Q4. In Q3, we tracked 342 deals, compared to 762 in Q4. This is a

testament to the resilience of the sector in the face of macroeconomic headwinds, to not only see more than double the volume of transactions, but to see cap rates virtually unchanged, with some sectors such as Medical, seeing a decrease in average cap rate. What is unsurprising here is the average remaining term increasing by almost four years between Q3 and Q4, a sign that while the sector is resilient to economic turbulence, it is not immune and the few extra years on a lease give investors the confidence they need to transact.

The 762 deals observed in Q4 2022 had an average cap rate of 5.65% across all tracked sectors, with an average remaining term of 12 years.

Of course, a closer look at the performance of specific sectors reveals much more complex and nuanced market conditions. Of particular interest were the Convenience Store (C-Store), Pharmacy, and Quick-Service Restaurant (QSR) sectors.



**Average
Cap Rate**
5.65%



**Average
Lease Term
Remaining**
12.0

Sectors in brief

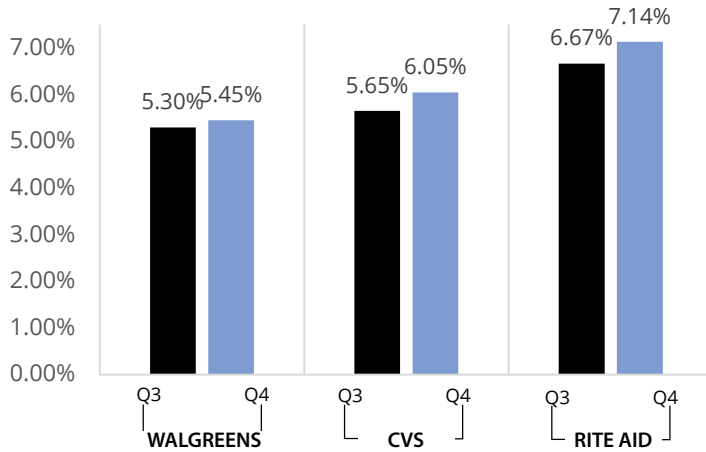
Sectors	Q3 2022					Q4 2022					Avg Cap Rates (bps)	Lease Years (Rem)
	Avg Cap Rate	Low	High	Avg Lease Yrs	Sample Size	Avg Cap Rate	Low	High	Avg Lease Yrs	Sample Size		
Automotive	5.35%	4.35%	7.50%	5.1	20	5.79%	3.90%	7.85%	14.9	77	43.7	9.9
C-Store	4.48%	3.40%	7.25%	13.7	48	5.08%	4.10%	7.24%	13.9	71	59.7	0.1
QSR	4.67%	3.00%	6.75%	12.4	100	4.98%	3.25%	7.64%	14.2	189	31.8	2.1
Dollar Store	5.50%	4.50%	7.50%	9.5	33	6.15%	4.80%	9.00%	10.0	106	65.1	0.4
Casual Dining	5.51%	4.00%	9.29%	8.6	27	5.81%	3.75%	8.22%	13.2	90	30.6	4.6
Medical	6.09%	5.00%	7.89%	9.9	10	5.93%	2.00%	8.73%	7.8	37	(25.6)	(2.1)
Other Retail	5.58%	4.00%	10.00%	5.6	22	5.84%	3.39%	8.50%	14.1	114	26.6	8.5
Pharmacy	5.60%	4.00%	13.00%	15.2	69	5.42%	3.73%	8.15%	12.0	49	22.9	(3.2)
Bank	4.81%	3.50%	7.00%	1.5	8	5.22%	4.50%	11.67%	6.1	17	115.8	4.7
Educational	6.17%	4.50%	7.00%	0.8	5	6.26%	5.06%	8.00%	13.9	12	8.7	13.1
Average	5.38%			8.2		5.65%			12.0		37.9	3.8
Sample Size						342					762	

¹ Other retail includes retailers who don't otherwise neatly fit into one of the above categories such as grocery stores, cellular stores, mattress stores, and fitness centers.

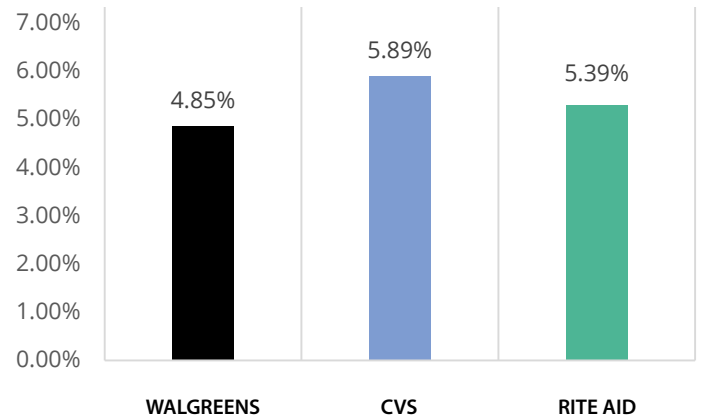
Markets in depth: Pharmacy

The Pharmacy sector, unlike the aforementioned sectors, saw depressed sale volume between Q3 and Q4 2022, registering 49 transactions in Q4, down from 69 in Q3. In this vein, the average term remaining captured on executed sales was down to 12 years in Q4 2022, compared to 15.2 years in Q3 2022. When looking at cap rates, Q4 2022 registered a median cap rate of 5.42%, we elected to use this figure rather than the average due to a high skew. That said, it would be unfair to compare to Q3 figured, but for the record, the average cap rate in Q3 2022 was 5.6%.

Overall Pharmacy Cap Rates



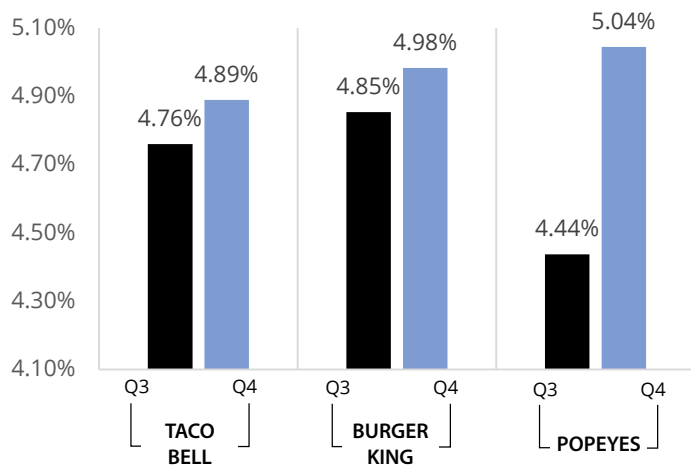
Pharmacy Cap Rates w/ 10+ Years



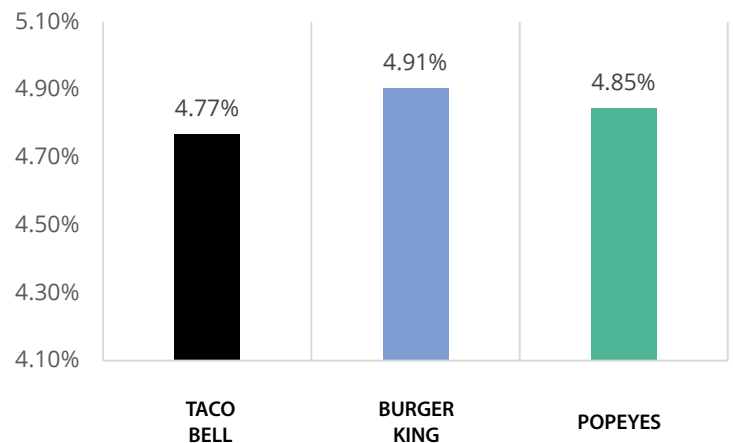
Markets in depth: QSR

Quick Service Restaurants, or QSRs, represent the highest transaction volume of any of the tracked sectors, registering an astonishing 189 transactions in Q4 2022, this is compared to 100 in Q3 2022. Over the timeframe, average cap rates trended upward roughly 30 bps, landing at an average of 4.98% which also happens to be the lowest average of any of the tracked sectors. The sector also saw a pretty drastic increase on the average term remaining of executed deals, landing at an average of 14.2 years remaining, compared to 12.4 years remaining in Q3 2022 deals. As new players in the market continue to gain market share, it will be interesting to monitor this sector over the coming quarters.

Overall QSR Cap Rates



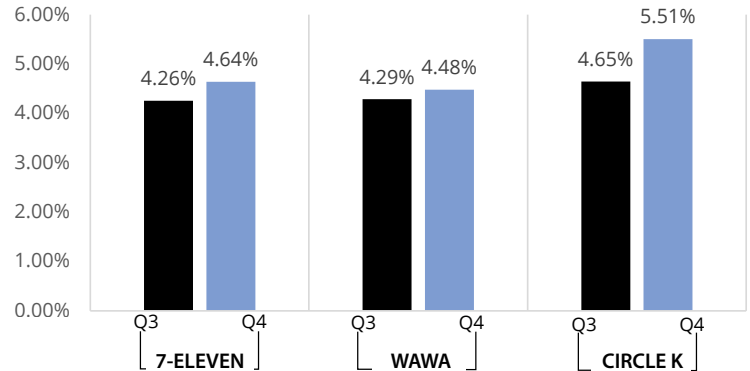
QSR Cap Rates w/ 10+ Years



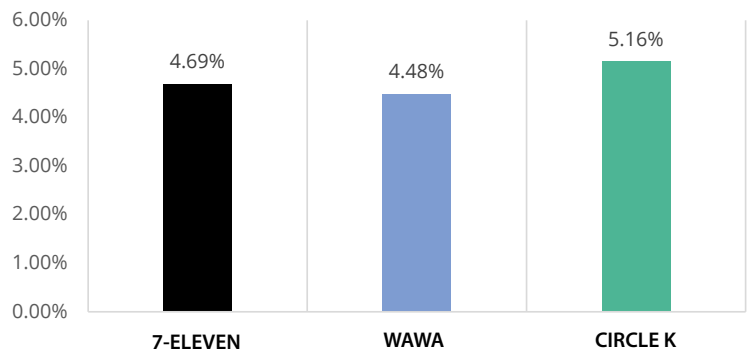
Markets in depth: C-Store

Investment volumes and cap rates have been steady in the C-Store sector nationally. Over the last Quarter months cap rates have come in at 5.08% for the C-Store sector, about 50 basis points lower than the average for single tenant net lease (STNL) transactions. We should note that the business terms of deals are typically agreed upon 60-90 days prior to a deal closing; so, a deal that closes today is an indicator of market conditions 60-90 days in the past. Also observed in the C-Store sector was a slight increase QoQ in term remaining, registering 13.9 years vs. 13.7 years in Q3 2022. Most notable in the C-Store segment of the market is the rise in transaction volume between Q3 and Q4, registering 71 deals in Q4 vs. 48 in Q3.

Overall C-Store Cap Rates



C-Store Cap Rates w/ 10+ Years

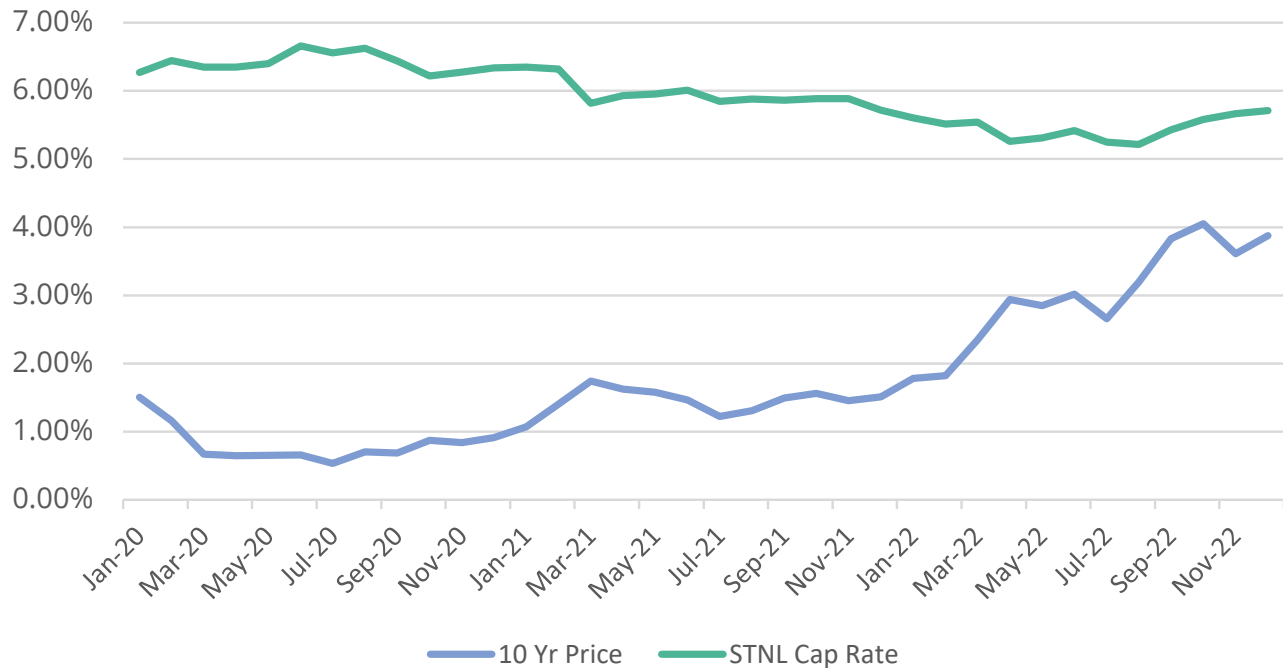


Brand by brand: Average cap rate changes

Tenants	Q3 2022 Avg Cap Rates	Q4 2022 Avg Cap Rates	Change in Avg Cap Rates (bps)
7-Eleven	4.26%	4.64%	38.5
AutoZone	5.40%	4.51%	-89.2
Burger King	4.85%	4.98%	12.9
Chick-Fil-A	3.59%	3.88%	29.3
CVS	5.65%	6.05%	39.2
Dollar General	5.41%	6.03%	62.5
Taco Bell	4.76%	4.89%	12.9
Walgreens	5.30%	5.45%	15.2
Wendy's	4.27%	4.99%	71.6

*All calculations are based upon available comps for each specific quarter with 10+ lease term remaining. The total number of sale comps for respective tenants in each quarter also varies significantly.

STNL Cap Rates vs. 10-year Treasury Rates



Conclusion

Despite all the indicators pointing toward a turbulent 2023, the net lease sector should remain as it generally has, resilient. The sheer uptick in transaction volume from Q3 to Q4 despite the rise in interest rates and mass layoffs in the tech sector illustrate this.

As institutional investors have generally put their pencils down on larger deals that require complex financing solutions, they still have capital to deploy, and the net lease sector will be an attractive place to diversify risk and place capital. Based on current conditions, the sector will remain favorable to private investors due to the low-price points offered, which as previously mentioned, render the cost of capital irrelevant.

Let's connect.

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Jonathan Hipp
Principal, Head of U.S. Net Lease Group
D 703 787 4725
C 571 926 2009
jonathan.hipp@avisonyoung.com

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