Commercial RealEstate Direct

Monday, July 21, 2025

Cap Rates for Small-Cap Properties Decline in 2Q, Indicating Stabilization

Capitalization rates for small-cap properties, meaning those having fewer than 50,000 square feet or between five and 50 apartment units, declined across the board in the second quarter, according to Boxwood Means.

That might be another indication that property markets are indeed stabilizing.

It started in last year's third quarter, when the headline National Council of Real Estate Investment Fiduciaries, or NCREIF, Property Index showed a positive return for the first time in nearly two years. It's posted positive returns quarterly since then.

Meanwhile, the NCREIF ODCE index, which tracks 25 open-ended funds that own U.S. commercial real estate, has posted positive returns for four straight quarters. For the second quarter, it recorded a 1.03% return, before fees, and 0.81% return, after fees.

The funds the index tracks hold $206.32 billion of assets. It is up 3.54% for the latest 12 months. That prompted Principal Asset Management's real estate research and strategy group to argue that commercial real estate "appears firmer than it has in the last three years."

Indeed, lending markets appear to be wide open and CMBS spreads, which provide insight into investor appetite for real estate credit, have continued to tighten. And investment managers are sitting on nearly $400 billion of dry powder, or capital they've raised that's yet to be invested.

Boxwood Means noted that cap rates for multifamily properties have declined by 30 basis points from their peak in mid-2022, to 6%. Rates for the three other major property types tracked by the Stamford, Conn., valuation and consulting company each fell by 20 bps, with industrial down to 6.1%, office to 6.3%, and retail to 6.3%.

Meanwhile, sales activity in the small-cap sector increased in the latest quarter by 13.6% from a year ago to $137.3 billion. While volumes remain well behind the mid-2022 peaks, when roughly $200 billion of small-cap properties changed hands quarterly, they're now more inline with the quarterly numbers registered before 2021, when super-low interest rates supercharged transaction activity.

The improved sales volumes show that the decline in cap rates wasn't necessarily the result of selection bias, when only the best-performing properties would change hands.

Boxwood Means recorded $55.2 billion of small-cap retail sales during the second quarter; $34 billion of industrial deals; $33.6 billion of office transactions; and $14.6 billion of multifamily sales. While those numbers were down from 1% to 2.4% compared to the first quarter, they were up 12.4% to 14.8% on a year-over-year basis.

The company highlighted the 14.1% increase in office sales from a year ago, noting that sales activity likely was driven by demand from opportunistic investors and sellers willing to adjust their pricing.

It noted that the small-cap market, like its large-cap counterpart, likely is past its cyclical bottom and that the bid-ask spread—the gap between the prices that sellers aim for and those that investors bid—that had stifled deal activity for so long appears to have narrowed substantially.

It said that the small-cap market might be past its repricing stage and transaction activity should remain disciplined, noting that it's unlikely to see the massive sales volumes of mid-2022.