Banking on the Fed: What December's Interest Rate Hike Means for Texas

For the first time since June 2006, the Federal Reserve board voted to raise its key rate by a quarter-point to a range of .25 percent to .5 percent. The announcement made on Dec. 16 is something the Fed has hinted at since March, causing months of speculation about the impact of an increase.

BY BRANDI SMITH

"Nearly seven years ago, the Fed put its benchmark interest rate close to zero as a way to prop up the economy," said John T. Fenoglio, CBRE Capital Markets' Houston-based executive vice president.

In fact, Fed staff concluded that the equilibrium real interest rate, which is the rate adjusted for inflation, had dipped into negative territory following the financial crisis. Only recently has it risen to zero. In the most basic terms, that means the economy was so weak that interest rates had to be lower than inflation to incentivize households and businesses to spend and borrow.

"The reason they haven't raised it before when they thought they would is just that it seems that any time there's some growth in the economy, it seems measured," said an experienced lender in the Texas market.

Positive economic news of late, including low unemployment numbers and higher wages, helped push the board toward its decision. Inflation was also an important factor, as it had reached the central bank's 2 percent target.

Because the hike has been anticipated for months, it's unlikely to have a significant impact on the commercial real estate industry here in Texas, though it will certainly be a topic of discussion.

"I think it's just been such a long time since we actually had to make that at the forefront of how we made decisions," said the Texas lender. "It hasn't been at the forefront of anyone's mind. It's been part of the decision, but not the leading top decision."

"Rates are near to historical lows and most forecasters do not see them increasing to levels that would harm or curtail Texas real estate prices," Fenoglio said.

However, the Fed's next moves will be watched closely as the frequency and intensity of any future hikes could significantly slow down market and economic performance.

"If we got into a scenario where the rates were being raised every time the Fed met, and they were taking a pretty good clip up, then that would move further up their list of things they wanted to consider," the Texas lender advised, speculating whether developers would want to move forward with long-term projects.

The situation really all depends on how the economy shakes up and adapts with this and any future hikes.

"If interest rates increase measurably in the long run, we could see price declines but we could also see higher rents and pricing would remain unchanged and possibly go higher if rent increases exceed interest rate and cap rate increases," said Fenoglio.

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In truth, only time will tell how individual markets react to the change in the long term.

Said Fenoglio: "It's anybody's guess."