

Real Estate Matters

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Investing in commercial real estate offers many benefits and could serve to diversify an investment portfolio that is based solely on stocks and bonds. While commercial real estate typically describes all income-producing real estate such as commercial, industrial, retail, and multi-family residential, our focus in this article will be on commercial and industrial properties.

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The Benefits of Investing in Commercial and Industrial Real Estate

By: Mike Lorelli – Senior Vice President – Commercial Asset Management, High Associates Ltd.



Secrets of Success in Property Management

By: Brad Mowbray – Senior Vice President & Managing Director – Residential Division, High Associates Ltd.

There are numerous benefits that a property owner gains from having a professional property management company overseeing the daily operation of its apartment communities. While there are added costs for this service (3-4 percent of effective gross income), the benefits significantly outweigh the expense and help drive positive returns for owners.

An essential role of a property manager is risk mitigation and protection from legal issues with residents while ensuring compliance with current local, state, and federal laws. Navigating the complexities of fair housing laws, the eviction process, and other legal matters can be daunting for property owners. Seemingly innocuous mistakes, such as a delay in repairs or asking the wrong questions during a property tour, could lead to substantial fines,

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President's Message

I am excited to announce the launch of a new series in our newsletter, dedicated to exploring the transformative impact of artificial intelligence (AI)



on the real estate industry. As technology continues to advance at an unprecedented pace, AI is poised to revolutionize the way we buy, sell, and manage properties, bringing unparalleled efficiency, insight, and opportunity to every segment of the market.

In this series, we will delve into the

various ways AI is reshaping the real estate landscape. From predictive analytics in property valuation to AI-driven customer service to intelligent investment strategies, each issue will feature an article that highlights the latest advancements and their practical applications in our industry.

I encourage you to dive into these insightful articles and explore the exciting possibilities that AI brings to our industry. Embracing these technological advancements will undoubtedly shape the future of real estate, and I am confident that our newsletter will serve as a valuable resource in keeping you informed about the latest developments.

In this issue, we'll be kicking off the series with a deep dive into how artificial intelligence is transforming the retail real estate market, enhancing everything from sentiment analysis to customer experience.

Thank you for your continued support and engagement. Together, let's embrace the future of real estate, focusing on how AI can enhance the way we do business.

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Secrets of Success in Property Management continued from page 1

lawsuits, and other legal challenges. An experienced property manager will stay on top of ever-changing regulations and will possess the knowledge to handle legal issues effectively.

In addition to the peace of mind provided by property management's involvement, excellent customer service is what helps differentiate one community from another. Property management companies can respond quickly to tenant complaints, facilitate timely repairs, and provide excellent customer service, all of which are factors that contribute to greater resident satisfaction and retention. Happy residents are more likely to renew their leases, reducing turnover costs and minimizing the hassle of having someone vacate the property. Historically, 45-50 percent of residents will choose to move when their lease term is completed at an average cost to the owner of approximately \$3K per moveout, including cleaning,



“Good quality management ensures that properties are well-maintained, tenants are happy, and investment yields are maximized.”

painting, carpet replacement, repairs, and vacancy time. Outstanding customer service is the single best way to minimize resident turnover.

Property managers also host community events where residents can gather and create new relationships with their neighbors, which helps foster a sense of belonging among residents – and their pets. When residents can forge quality friendships within the community, they are more likely to stay in their apartments longer and enjoy where they live even more. The financial impact is measurable, but the positive reviews also make it more desirable for prospective residents to want to move into the community.

Good quality management ensures that properties are well-maintained, tenants are happy, and investment yields are maximized. This gives property owners the peace of mind of knowing that their investment is in good hands.



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The Benefits of Investing in Commercial and Industrial Real Estate continued from page 1

Before making a direct investment in real estate, it is important to understand the market where the investment is located, including competitive properties, rents, occupancy, and the area's general economic health. An investor should also understand the costs of ownership. Unlike stocks, real estate is an active investment and may require additional capital investment over the hold period.

Owning either commercial or industrial real estate offers many benefits. First, unlike residential properties, lease terms tend to be longer, typically three to 10 years or more. This provides an investor with a longer, uninterrupted income stream and potentially less turnover and vacancy loss than a residential investment. Buildings and/or tenant suites are also more customized for the business and its operations, resulting in less turnover than other types of real estate. The lease structure for office and industrial real estate is typically triple net meaning that most of the cost of ownership is passed back to the tenant. Expenses such as taxes, insurance, maintenance, and repairs would be reimbursed by the tenant. Structural issues such as roof replacement or parts of the building envelope typically remain the investor's responsibility.

Real estate investment serves well as a diversification to a stock portfolio since it helps mitigate risk against stock market volatility and serves as a hedge against inflation. Most commercial and industrial leases have annual escalators, which can increase the investor's income to offset inflation. Rising rental rates also offer the potential for real estate appreciation, assuming capitalization rates remain steady. This appreciation will increase the investor's overall return when the property is sold.

The final benefit of owning investment real estate is the tax benefits derived from ownership. The most well-known benefit is depreciation, which allows investors to depreciate the acquisition of the building based on a set schedule. Additionally, there are options for accelerated depreciation and cost segmentation, providing faster opportunities for depreciation based on the useful life of certain building systems or elements. Mortgage interest expense is also deductible, and depending on the investment, there could be tax credits or incentives based on the property's location, energy enhancements, and other government initiatives. Finally, there is a tax benefit for like-kind exchanges, commonly referred to as a 1031 exchange. If successful, an investor can defer capital gains associated with the sale of a property if invested in another commercial property within the defined period of time. To fully understand all the potential tax benefits of an investment, it's advisable to consult an accountant or a tax professional.

Investing in commercial and industrial real estate can be challenging for many investors due to the substantial initial investment and the ongoing capital requirements. Additionally, the lack of liquidity associated with this type of investment



may deter some potential investors. If this is your situation, but you like all the other benefits of owning real estate, then investing in a real estate investment trust (REIT) may be a good option to explore. They offer liquidity and the ability to invest with a relatively small amount of capital. According to the National Association of Real Estate Investment Trusts (NAREIT), the average annual returns from REIT investments, considering both income and appreciation, range from 8 to 12 percent over the long term. These returns will vary based on the asset type, geographic footprint, and the current economic cycle. As with any investment, research should be done before investing in a REIT. When evaluating REITs, key factors to consider include historic return performance; markets invested in; types of assets included in holdings; performance of their portfolio such as occupancy, tenant mix, and lease rates; dividend payment policy; quality of management team; and performance to peer REITs.

Whether investing directly in real estate or through REITs, real estate can serve as a valuable addition to a stock portfolio, helping to diversify and mitigate risk while potentially enhancing overall returns.

If you are interested in an individual property, you should consider selecting a buyer agent to represent your interests before entering into a real estate transaction. A qualified agent should have strong local market knowledge regarding lease rates, cap rates, vacancy ratios, and product demand for the specific asset class. Whether you are buying or selling, High Associates Ltd. provides comprehensive representation services supported by a wealth of experience in real estate development, leasing, property management, and sales negotiations.



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Creating a Family-Friendly Environment in Your Hotel

By: David Aungst – President, High Hotels Ltd.

Family travel continues to be a key driver in the hospitality industry. In the May edition of LODGING magazine, Booking.com shared that family travel was poised to increase in summer 2024 when it reported “searches for accommodations by families for the summer travel season are already seeing an 8 percent increase as compared to last year, while flight searches globally are seeing an increase of 21 percent. These figures underscore an interest in travel this summer, as families look to make the most of the warmer months ahead. Almost two-thirds (62 percent) of families rank spending quality time as the main motivator for traveling this year, followed by finding the time to properly relax (58 percent) and discovering new places (48 percent).” Further, as millennials continue to grow their families, research has shown that they are deeply interested in unique experiences when they travel.

Both owners and operators have the opportunity to increase hotel revenue by attracting families.

Owners

For owners, creating a family-friendly environment ideally begins in the project’s design phase. From selecting a brand to determining room layouts, amenities such as indoor pools or playgrounds, and technologies such as the number of data ports, wireless hotspots, and internet speeds, owners must consider market dynamics and demand generators. All these decisions have implications related to cost per square foot and room counts, but they are crucial for attracting family-oriented travelers. The hospitality landscape is dotted with brands that cater to families, from the Cartoon Network Hotel in Lancaster to Great Wolf Lodge and a variety of other resorts and specialty hotels that span the United States.

Existing hotels can also be repositioned to attract more families through renovations. For example, at High Hotels, we utilized



renovations to create a family-friendly environment at our York Home2 Suites by converting rooms with a single king bed to two double queen beds. Similarly, at our TownePlace Suites in Mechanicsburg, PA, we replaced uncomfortable sofa beds with trundle beds to make them more appealing to families.

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Operators

While owners deploy significant capital to position their hotels, operators can creatively make hotels inviting to families. For hotels with restaurants and food offerings, operators should offer a variety of menu options that cater to all age groups. For hotels with more limited food and beverage offerings or more restrictive franchise requirements, operators should encourage their staff to engage with families in simple but effective ways, such as having crayons and coloring pages for breakfast, board games for rainy days, easy driving instructions to family-friendly

venues, and gift shops stocked with snacks for families on the go.

Beyond these offerings, hotel staff should ask questions about the reasons for travel when guests arrive. When they discover it is Johnny's or Sally's birthday, they should have birthday cards signed by staff or balloons ready or inquire about purchasing a small cake or cupcakes to help celebrate the occasion.

Operators can also create family-friendly hotels by allowing the local community to rent their meeting rooms or swimming pools for birthday parties during off-peak times.

At High Hotels, we look for opportunities to spread joy through hospitality. Creating lasting memories does not need to be expensive or cumbersome, but it does require thoughtfulness and creativity.



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First Impressions: The Importance of Good Property Maintenance

By: Kim Long – Director of Real Estate Operations, High Associates Ltd.

Everybody appreciates a well-maintained property. Property maintenance, an essential aspect of both real estate ownership and property management, refers to activities undertaken to ensure buildings and their utility systems are safe, habitable, and in good optimum working order. Small, neglected repairs may become costly over time if ignored. Below are some of the reasons why good property maintenance is so important.

Air Filter Replacement. HVAC air filters should be changed or cleaned once every three months. If the air filter becomes too dirty, it creates poor air quality and makes the unit work harder. Worse yet, neglecting this task for too long could cause the unit to stop working, forcing an entire system replacement.

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Property Inspections. Regular inspections are a fundamental part of good property maintenance in order to identify potential issues and address them promptly. Routine checks and servicing can identify potential problems early and prevent minor issues from escalating into costly repairs.

Outside Maintenance. It's crucial to prioritize the maintenance of your property's landscaping and outdoor areas. Well-kept outdoor spaces help create an inviting and visually appealing environment for tenants, thus boosting overall satisfaction of existing tenants and attracting new ones.

Value Preservation. Well-maintained properties retain their value and appeal over time. This is particularly important for those looking to sell or lease their properties, as it can directly impact the property's marketability and price.

Safety and Compliance. Regular maintenance ensures that properties adhere to safety standards, reducing the risk of accidents and legal liabilities. It also ensures compliance with local building codes and regulations, which can prevent fines and other legal issues.

Efficiency and Sustainability. Adequately maintaining systems like heating, cooling, and plumbing increases their efficiency, leading to lower utility bills and a smaller environmental footprint. It also extends the lifespan of these systems, further contributing to sustainability efforts.

In conclusion, maintaining a property is essential for preserving its value, ensuring the safety and well-being of its occupants, and minimizing costly repairs in the long run. It is not only a wise investment but also a crucial responsibility for ensuring the longevity and sustainability of the property.



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AI Series: The Use of Artificial Intelligence in Retail

By: Scott Hess – Vice President of Information Services, High Company LLC and Powell Arms – Senior Vice President & Managing Director – Retail Division, High Associates Ltd.

Artificial intelligence (AI), more specifically Generative AI (GenAI), has garnered substantial attention and excitement in the past 18 months due to the introduction of products like ChatGPT, Gemini, Copilot, and DALL-E, among others. For the first time, AI is accessible and comprehensible to anyone with an internet connection and a web browser. Users can engage in text-based conversations, ask questions, stimulate creativity, and edit documents without the need for programming skills.

While AI might seem like a recent innovation, its roots trace back to 1956 when a small group of scientists conducted a summer research project at Dartmouth University on artificial intelligence. Today, AI is increasingly being integrated into businesses and demonstrating its impact across all industries. A recent article by PwC, “Sizing the Price,” suggests that global Gross Domestic Product (GDP) as a result of accelerating development and use of AI, will increase by 14% or over \$15 trillion by 2030. Currently, the GDP of China is ~18 trillion and the United States is ~27 trillion.

The challenge for many businesses is determining how best to leverage AI.

Background

Generative AI operates by predicting the next letter or word in text based on models trained on vast amounts of data, including publicly available information from the internet and other sources. What sets GenAI apart is its ability to generate responses to user queries in conversational language. It can assist with creative tasks (‘how should I launch a meeting with a fun fact about AI in retail’), editing text (‘create an executive summary of 500 words based on the text below’), and image generation, showcasing just a few of its practical applications.

Retail

A recent study by Gartner, a leading technology research and consulting firm, indicates that 40-50% of retailers are using AI today, which will continue to increase in the next few years. This adoption varies widely from large retailers like Home Depot and Walmart to regional and local retailers.

Retailers employ AI for sentiment analysis, providing insights into consumer behaviors, preferences, and trends by analyzing unstructured data from social media

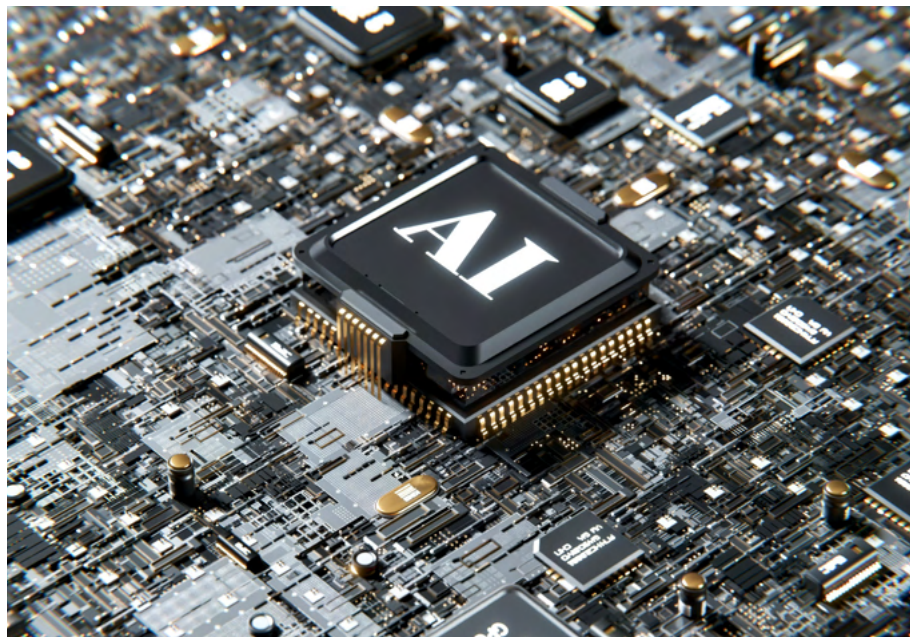
comments or website ratings. This information informs product development, customer service strategies, and more.

AI can analyze existing in-store video systems to assist a retailer’s staff in responding promptly when attention is needed. For instance, if checkout queues become too lengthy, staff can be alerted to open additional checkout lines. Similarly, if a customer waits an excessive amount of time for assistance at areas like the deli or butcher counter, staff can be notified. Additionally, AI can analyze customer shopping paths to identify bottlenecks caused by layout and floor displays, helping to optimize a more natural and efficient flow within the store.

GenAI also enhances consumer engagement by enabling conversational searches via chatbots. Consumers can pose questions to find products tailored to their needs, bypassing traditional filter-based searches. Retailers can optimize product or service descriptions using GenAI. It can create alternative descriptions or make suggestions that resonate more effectively with their target market.

GenAI is also being used to improve consumer engagement. Retailers are using these tools to develop consumer or segment-specific marketing campaigns, brainstorm creative ways to market to consumers, develop interesting social media posts, and generate new images that resonate with a target market.

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Considerations

Despite its promise, it is crucial to recognize that AI, particularly GenAI, is still in its early stages of maturity. Organizations must assess potential risks before implementing these tools.

Generative AI operates based on available data, which users may not always be aware of or define properly. For instance, sensitive information like social security or payroll details stored on insecure shared drives could inadvertently be accessed by AI if proper security measures are not in place.

The reliance on publicly available data sources can also introduce biases or copyright issues. Data might be skewed towards specific demographics, leading to biased outcomes. Moreover, using copyrighted data without proper attribution can result in legal complications and financial liabilities.



Lastly, while AI can produce complex answers, they may not always be accurate. Human oversight is essential to interpret context, understand intent, and ensure the generated responses align with organizational goals.

Conclusion

The coming years will witness a surge in AI adoption, with potentially significant impacts across all industries. As these technologies evolve, it is crucial for organizations to understand their implications on employees, customers, and overall business operations. A well-informed understanding of both the benefits and risks associated with AI will empower business leaders to make informed decisions and navigate this transformative landscape effectively.



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The Future of Real Estate Commissions

By: Bill Boben – Senior Vice President – Sales and Leasing, High Associates Ltd.

The landscape of real estate commissions is undergoing significant scrutiny due to antitrust allegations in the single family space, and the subsequent settlement with the National Association of Realtors (NAR). On March 15, 2024, a settlement between NAR and the Plaintiffs was announced with a penalty of \$418 million payable over several years and a requirement for NAR to change several rules. This landmark case, now under re-examination by the Court of Appeals for the District of Columbia, signals a potential reshaping of how commissions are structured, directly impacting both buyers and sellers across residential and commercial markets.

Traditionally, real estate commissions are perceived as being paid by the sellers; however, this cost indirectly affects the buyers as the commissions are embedded in the home prices.

This traditional framework has been challenged by arguments suggesting that such structures unfairly burden first-time homebuyers and veterans. The counter argument is that the funds provided by the buyer and accepted by the seller in exchange for the property are what cover the real estate commission for both the seller's and buyer's agents in the majority of single family home sale transactions today, leading to a fairer transaction where both parties are represented.

The recent legal changes signifies a pivotal moment for the industry. This reevaluation could lead to lower, more transparent commission structures in the future, potentially increasing accessibility to home buying, particularly for first-time buyers.

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Katie Johnson, NAR's Chief Legal Officer, suggests that there could be a shift towards more buyer-friendly practices in property purchases. According to www.realestatewatch.com, the average realtor fees in Pennsylvania are 5.48 percent of the sale price which includes a 2.81 percent listing agent commission and a 2.67 percent buyer's commission. Depending on the legal proceedings still in motion, we might see the development of different service-level menus and fees based on consumers' needs. Unlike residential sales, commercial real estate transactions offer more flexibility in commission schedules due to factors such as property size, diverse uses, institutional ownership, higher equity requirements, and less regulated lending standards.



As the industry changes, the key question is whether the forthcoming legal and structural adjustments will truly enhance the fairness and transparency of single family real estate transactions for consumers, or if they will merely establish a new standard with its own set of challenges. Both industry professionals and consumers alike await these outcomes with bated breath, recognizing that the implications will resonate well beyond the courtroom.



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