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Construction costs climb in some markets, slower in others

August 21, 2014 - Retail

Developers are keeping a watchful eye on construction costs, which have slid upward the past few years, and have spiked dramatically in some markets, though in others not so much.

Some developers are blaming the rising cost of materials, while others curse a jump in labor costs.

"Construction costs, which were rising at a pace of 15 percent annually for the last two years, are jumping very quickly," said Stephen Coslik, chairman of Fort Worth, Texas-based The Woodmont Co. "In a 90-day period this year, we saw a 40% increase in steel prices."

It's a problem, Coslik adds, because "rents have gone up, but are not keeping pace with materials and land cost increases. Years ago, we used to try to build a 12% return on costs, now you work to get a 9% to 10% return and even that's damn tough."

But not everyone everywhere is fretting about construction costs. Over in the Gulf South, the worry is more about labor costs than the rising price of materials. "The primary materials for retail development are steel, asphalt and concrete and while there have been continual upticks in pricing I've not seen any big jumps recently," said Townsend Underhill, senior vice president of development at Covington, La.-based Stirling Properties. "Prices have just been creeping up since last year."

This isn't to say construction costs in the Gulf Coast haven't skyrocketed. They have, but it's mostly to due to labor, Underhill maintains, adding he doesn't know if the problem is endemic to the country as a whole or just specific to the Gulf Coast. "The big issue," Underhill said, "is a rare phenomenon of general contractors outnumbering the sub-contractors by two-to-one or three-to-one in the Gulf South. This is an inverse relationship and it is not healthy for the construction economy."

Tim Grogan, editor of the Engineering News-Record, which tracks construction expenses for the building trades, finds all this talk of quickly rising construction costs perplexing. The News-Record reports that union labor costs are rising a moderate 2-4 percent annually.

As for material costs, prices jumped but that was a few years ago and have since settled back to absorbable increases. "We might have hit double digits five years ago. Today everything is ranging around a 4% increase," Underhill said, adding that he doesn't measure specific project types, i.e., shopping centers, that might make the cost very different. "Some costs pop up, other things go down, but overall we have been seeing modest inflation rates for construction."

As for materials, the News-Record reports the Producer Price Index for Cement in June was up 5.6% over a year ago. Structural steel costs increased 4.6% this year, but were down 2.9% in 2013 and down 9.3% in 2012. That was after swelling over 14% in 2011. Steel prices are expected to rise 3% in 2015. Meanwhile lumber prices took a big spike when housing started making a comeback, but then housing stalled. Lumber prices jumped 15% in 2013 and 13% the year before. This year lumber prices are heading upward at a 6% pace.

"Prices were depressed through the recession," Grogan said. "With demand prices popped back up, but the recession wasn't strong enough to support long-term gains. The rate of escalation has slowed."

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