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Spring 2020 overview - The industrial real estate market meets the COVID-19 threat - by David Skinner

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Two weeks ago we heard about some illnesses being passed around China and South Korea. One week ago we were seeing some international travel restrictions. This week has seen a majority of people working from home, and now other parts of the country like San Francisco are in the middle of mandatory 14-day lockdown. According to CNN, mayor Bill de Blasio has intimated that New York City should prepare for a similar order in the near future. At the time of this writing, things are moving fast.

How does this impact industrial real estate in Q1 2020? Maybe it means that the highest and best use for land sites in Boston are not residential developments, but rather for all the toilet paper manufacturers! Just kidding. But the 2020 outlook has changed overnight in the blink of an eye.

Boston mayor Marty Walsh was the first in America to order all construction work in the city to stop because of the COVID-19 threat which impacts any contractor or supplier who is involved with the myriad projects in the city. Many towns around the 128 and 495 suburbs are considering similar moratoriums.

Cash-heavy building and contractor supply houses will be more likely to weather the storm than those who are more highly leveraged, and the local companies with one or two locations will have a much more difficult time than the larger brands with a regional or national presence. A shutdown for a few weeks will be a workable challenge, but if the outbreak continues with containment procedures lasting through the summer, the consequences will be much more serious. The most serious effects are being felt by companies who need to send their employees home with limited productivity but also continue paying them their wages.

Importers and wholesalers who bring in product from anywhere outside the United States are going to continue to struggle due to tariffs and ever-thinning margins, especially those who import goods from parts of the world that have the most reported cases of COVID-19.

Other industrial sectors that are being affected by the outbreak are any that facilitate rentals for weddings or graduations, which are being pushed out until Q3 2020. A few notable groups in this sector have temporarily laid off up to 63% of their hourly workforce with full intent to hire them back. This is what could likely fuel a tremendous finish to the year when the cancelled events come roaring back with fullforce.

The question every landlord is thinking right now is how they will continue to get paid if their tenants will not make the monthly obligations. Insurance companies will likely see an increase of lawsuits with regard to “force majeure” or “acts of God” clauses in contracts. Hotels, airlines, and any other type of travel-based companies are feeling the pressure of cancellations and will see these same types of clauses get exercised. Many companies who have been forced to close their doors will likely not receive any aid, so there may be an increased level of vacancy on the market in Q’s 1, 2, and 3.

Speculative construction projects also have slowed because developers are awaiting the longevity of this crisis before jumping into further debt on each project. As one prominent landlord of 100,000 s/f of manufacturing/distribution space in the inner city aptly stated, “The American economy is going to contract in the short term because of the upheaval in workforce and supply chain, and it will continue on for a while until we have the situation under control.”

However, there are numerous shining stars in the horizon. Amazon’s recent 10-year lease of 100,000 s/f in Wilmington, Mass. which includes 600 parking spaces coupled with their aggressive recruitment of over 100,000 more employees is a prototypical example of the type of industry that will continue to flourish amidst the distressed marketplace. Similarly, businesses in the repair rather than replacement business will also continue to do well. Continue to look to warehouse/distribution centers, third party logistics (3PL), and grocery to absorb more space even in the downturn.

Sales and leasing transactions have not stopped, but speculative buyers and private equity (PE) fund managers have become more cautious because of the lack of clarity with regard to how long the various forms of containment proceedings will continue on. Some of these groups have put a complete moratorium on all acquisitions for the next 4-6 weeks until there is more clarity and definition in tenant interest and leasing activity.

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