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The changes in trends are directly correlated with interest rates, workforce location and inventory - by Kevin Casey and Christina Rouse

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Punxsutawney Phil predicted an early spring in store for us this year. Spring brings new life and new energy as it is a time for growth and development. We are hoping Punxsutawney Phil is right for both the weather and the commercial real estate market. We do expect an uptick in activity as the weather warms, but transaction sizes could be much smaller than years past. The changes in trends are directly correlated with interest rates, workforce locations and inventory needed. There are users in the market, but the inventory is not matching their needs. We are nearly at the tipping point of ground-up construction over renovation.

Converting costs versus building costs are nearly at their tipping point depending on how the project is funded. For financed users it still makes sense to convert over build, the ground-up construction just isn't penciling out. We've seen that recently with Parcels 8 & 8A in the I-195 district. Pricing is staying consistent prior to the interest rate hike, and we've not seen the adjustments needed to factor in the higher borrowing rates. With rumors of a decrease, the tone of the market will be set by how the Fed adjusts its rates in the coming months.

Nonfinance construction is occurring, car dealerships are a good example of this. As we have come out of the pandemic vehicle inventory is building back up to pre-COVID numbers and in doing so has driven the need for dealership developments required by the vendors. Land developments that have also continued to thrive are car washes.

0 Comstock Pkwy. in Cranston is a 17-acre shovel ready site with plans for a 200,0000 s/f warehouse and an additional 70,000 s/f warehouse, but without a significant tenant the banks are unable to fund projects on a “spec” build. An anchor tenant or two would likely allow for an equity construction loan to be assigned to the property. The issue is, are the users able to wait for the construction to occur.

One of the trends that we have been seeing and continues to linger is longer transaction timelines, in both sales and leasing. The delays are sometimes due to lead time for materials, appraisal lead times, environmental requirements, backed up court systems, and with delays comes higher overall costs associated with the transaction. The biggest impact on the timeline are the decision makers taking longer to execute on their decisions. Understandably, they are trying to anticipate the next eight to ten years for their businesses after going through such a flux in the last four. There are more items that decision makers now have to factor into their business real estate in order to meet their retention and growth goals.

The big news story for commercial real estate continues to revolve around the office market. On the office leasing side, lease terms are returning to a five-year average, compared to the trend in 2021 of two-year renewals. It seems we have shaken the “kick the can down the road” mentality and users are making more meaningful moves for their office spaces. The leases that were renegotiated during the pandemic are now coming to term and many businesses that are continuing with the work-from-home model do not need as much office space as they did in March of 2020. The reduction in square footage needs seem to be trending at about 50% of the previous leasing cycle. Quality buildings in submarkets such as Lincoln and Warwick are experiencing a boom in need. Multi tenanted office buildings that are able to meet square footage needs in the 1,000 to 3,500 range have fared extremely well in the current market. The narrative that offices are empty and struggling is confined to the downtown areas that were previously highly tenanted, with most of the buildings having been constructed post 1990 being excluded.

The future of our spring and summer markets is unfortunately not up to Punxsutawney Phil, and we shift our attention to the Fed in hopes that hotter markets are on their way. The investment and conversion markets depend on financed users to be active in the market and with current rates, it just is not penciling out. If we reach that tipping point and the balance shifts towards ground-up construction projects, we anticipate being able to attract potential users who are in the market but unable to commit due to unforeseen timelines for conversion customizations.

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