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Commercial build-to-suit market forecast 2009: Strong market position will weather this cycle

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The financial chaos in 2008 has brought a large portion of the world's developed nations into uncharted economic territory. Those who did not understand how the global economy worked have received a lesson in Economics 101. The economy is based on credit and the confidence of the lending entity in the borrower's ability to repay the debt owed. Basic lending fundamentals were ignored for a significant period of time, and a culmination of deregulation and corporate greed created this perfect economic storm.

The state of the economy has negatively affected the attitude of board members charged with making corporate decisions to commit spending capital funds for new buildings. An additional deterrent to new building is the fact that financing is difficult at best, more expensive than in the past, and would require much larger equity participation at a time when cash is in short supply.

For the commercial build-to-suit market in Mass., N.H., and R.I., 2008 started out well, with seven projects under construction totaling 860,000 s/f. The project mix included two distribution projects totally 383,000 s/f, one flex renovation of 140,000 s/f, two office buildings totaling 184,000 s/f, and two manufacturing facilities of 158,000 s/f.

Second half 2008 activity dropped way off with one warehouse expansion, one manufacturing plant, and one corporate training center totaling 173,000 s/f combined.

Two major projects preparing for construction in early 2009 include Medline's ground-up 350,000 s/f medical supply distribution center on West St. in Mansfield, Mass. and Tyco Valves and Controls 118,000 s/f office and manufacturing renovation on Cabot Blvd. in Mansfield.

According to McGraw-Hill's Construction Outlook issued late last year, the level of construction starts was off 12% in 2008, with 2009 predicted to be off 7%. Applying the effect of the financial down-turn to the build-to-suit commercial building market here in New England, I would estimate that 2009 will be off by between 20 and 25% in new construction dollar volume from 2008. Financing will be available, but the sources may be local banks that know the business they are lending to versus the larger national banks and investment houses. As of this writing, the first half of the \$750-billion bail out package has had little effect on the economy. The money is not making it to Main St.

Construction costs for material and labor have become volatile. Subcontractors are feeling a sense of urgency when bidding any viable, shovel-ready project and, as a result, lower construction costs are benefiting building owners. Cost for construction has fallen 10 to 15% since Labor Day 2008. Steel cost per ton is falling as demand for steel worldwide has virtually collapsed. Gas as of this writing was at the high-\$30 per barrel range, a far cry from last summer's \$148 per barrel. This should help stabilize material and delivery costs. Subcontractors will continue to be aggressive in their bidding as competition heats up for the remaining work and fewer projects will break ground.

There will be some fallout of general contractors and subcontractors as the market volume declines. Design-builders and general contractors who operate based on good fundamentals with efficient overhead and a strong market position should be able to weather this cycle.

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