



BENUZZI'S INDUSTRIAL GUIDE

Your BIG Chicago Area Industrial Real Estate Resource Guide

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Construction: A Chicago Market Overview

Compared to the last few years, 2015 is looking good from an economic standpoint. The US economy is experiencing solid growth, job gains are up, the dramatic price drop in oil has meant consumers have more cash to spend, and inflation is expected to stay low. As a result, manufacturers are looking to expand.

Mark Augustyn, Chief Operating Officer at Principle Construction, thinks this is a winning formula for the Design-Build construction business serving the industrial industry in the Chicago market. "There have been more permit starts and more buildings are under construction in 2015 than there were last year," he says. As a comparison, Principle's ground up, spring starts of 2015 have experienced more than a 50% increase over last year. Even more exciting is that the value of those projects is higher, reflecting a greater capital investment by our industry. Contract values for 2015 represent an increase of over 115% from the prior year. "We are on track for similar increases for summer and fall starts here at Principle as well. Not to mention, the pipeline of new prospects is still flowing strong, without any let up in sight."

It's no secret that the Great Recession took its toll on everyone from consumers, to manufacturers and developers. "Back in 2008, everyone hit the brakes on development and expanding their business. Financing tightened, speculative building virtually stopped. Some thought the business environment would get back to normal in one year, some thought longer, but everything was put on hold for over five years. Finally, the train is moving again and is quickly gaining speed," says Augustyn.

That train has already brought Chicago industrial vacancy rates lower than they were last year, prompting manufacturers to renew expansion plans. Where before they may have increased efficiencies within their existing footprint, now they have no other choice but to increase space. The fact that many firms looking for space all at the same time reflects the amount of pent up demand from companies who cautiously stayed put in recent years.

"Now that developers see vacancy rates falling, they're feeling more comfortable investing in speculative development," said Augustyn. But quality and speed is still an important factor. Business parks with proposed buildings on vacant land are harder to rent than available space in an existing building. Customers' timelines are often tight, with many needing to take occupancy in a few months. This makes existing space more attractive than proposed space.

Developers know this, which is one reason why speculative building activity has picked up. "Last year we saw just a few speculative buildings come out of the ground," he continued. "This year we are seeing a lot more from our developer customers. So, the outlook is much rosier," says Augustyn.

On the down side of all this increased demand is the adjustment we are all making to work capacity limitations. Our industry consolidated during the Great Recession. Staff levels were reduced in management, labor, manufacturing and government. Now, as the work load increases, every segment is adjusting to increased demand. Finding the right balance of increasing overhead, without sacrificing quality or long term profitability is the new challenge. "Surprisingly, we have

been told by several subcontractors that they are 'too busy' or have taken all the work they can handle for 2015 already. But capacity adjustments are being made. For example, the precast wall panel industry is bringing new casting beds on line and adjusting their labor commitments to ensure they can meet the current growth in demand."

Even local building departments are struggling to keep up. "Currently, one of our small TI projects is in its fifth week of permit review where last year we would have had it turned around by the municipality in the traditional two week time frame. There is only so much work a person can accomplish in a given day. The increased quantity of project inspections and new permit review demands on the municipal inspectors is exceeding their current capacity." Like everyone else, municipalities will be adjusting their staff levels to today's and tomorrow's projected work volume.

One would expect that a surge in development would lead to a dramatic increase in the cost of materials and labor. Augustyn says, "We track long lead item delivery times and subcontractor pricing in our market, and the data is telling us that costs have remained stable or are increasing at traditional rates." One exception: concrete, which has risen 12% in 2015 over 2014 pricing. Why? Augustyn thinks it's related to transportation issues and industry consolidation of cement and ready mix manufacturers.

The tell-tale signs of volatility are on the horizon though. Fewer and fewer vendors are willing to hold prices for

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extended periods and in some cases even honor quotes provided. Material suppliers are starting to send out notices of midyear price increases. Still stinging from the concrete shock of 2015/2014, with fresh memories of prior years' price shocks in steel, copper

and roof insulation, there is strong resistance to making long range price commitments. Fortunately, oil seems to be stable (at least as of today) and our domestic production capacity has dampened what used to be one of our most volatile commodities. "Along every step of the process, buyers of commodities continually push back against price increases.

We are always pressing for lower pricing, better quality and improved delivery. In general, the market has been responsive to those demands. What I can confidently predict is that there will be a lot more pushing from each side as everyone enjoys the increases in work."

Mark Augustyn is co-founder of Principle

Construction Corp., a design/build general contracting firm located in Rosemont, Illinois. As COO and Treasurer, Mark has the responsibility of overseeing and managing many of the companies' functions and providing overall leadership for the growth and development of the organization. Mark is a licensed Architect in Illinois and Wisconsin.

