

## Maine Spotlight

# The unique state of the commercial real estate market: New construction has come back strong



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We've been through several cycles in the commercial real estate market since I started back in 2005. The robust and bullish market through 2007 with moderate vacancies and active buyers and sellers, the down market triggered by the Great Recession, and then the very active market that followed, with clients taking advantage of high vacancy rates, discounted valuations, and repositioning opportunities.

*The overall economy is strong, and the current commercial real estate investors and speculative developers are in a great position moving forward. As we saw in the early 2000's, construction firms and sub's will grow in numbers and size to take advantage of the bullish redevelopment and new development market, and although there will be a delay due to planning and approvals for new projects, this will allow for lease rates to increase while construction costs begin to flatline a bit. I expect there to be a significant increase in speculative and owner-user developments in the pipeline by the end of 2017, and as a result we will move towards a more balanced market for tenants, landlords, buyers and sellers going into 2018.*

After six straight years of dropping vacancies, we have entered a new phase in our industry. New construction has come back strong, particularly in the housing and industrial markets, and as a broker, the new challenge is a very low inventory in all sectors. This has slowed transactions for two obvious reasons: There is less available on the market for buyers and tenants to consider, and less motivation for potential sellers due to a lack of repositioning and exchange opportunities.

With such low vacancy rates, sales prices and lease rates are on the rise. We have also seen several successful speculative new construction projects, as well as successful speculative pur-

chases of vacant or partially vacant buildings.

The biggest obstacle I see at this point is that lease rates are not rising at the same rate as construction costs. The recession played a role in this. Several general contractors/design build firms and subcontractors closed their doors, and others became more lean and less top heavy. Additionally, there is a lack of qualified workers due to low unemployment rates. Combine the thinning of the construction workforce with the boom in apartment and condominium construction, and it paints a picture as to why construction costs have gone up at a faster pace than lease and sale rates. A moderate increase in material costs has certainly also played a role, but more than anything we are seeing less aggressive pricing from contractors due to an already steady workload. The pendulum will swing and lease rates are bound to reach a point to support new construction, but until they do, we face limited inventory and a more challenging brokerage environment. Redevelopment of antiquated buildings, speculative industrial development, land purchases, and under the radar pocket sales seem to be the trend for at least the remainder of 2017.

In 2016 I was confident that we would see increase in supply and inventory due to repurposing and renovation of antiquated buildings, speculative new construction, and land purchases from owner-users looking to build due to limited existing options. In hindsight, I think I was off by at least a year. Vacancy rates have continued to drop, and lease rates have not gone up as quickly as I expected. Combined with the more dramatic increase in construction costs, this has slowed the new supply of inventory.

It's important to note that this issue is not economy related. The overall economy is strong, and the current commercial real estate investors and speculative developers are in a great position moving forward. As we saw in the early 2000's, construction firms and sub's will grow in numbers and size to take advantage of the bullish redevelopment and new development market, and although there will be a delay due to planning and approvals for new projects, this will allow for lease rates to increase while construction costs begin to flatline a bit. I expect there to be a significant increase in speculative and owner-user developments in the pipeline by the end of 2017, and as a result we will move towards a more balanced market for tenants, landlords, buyers and sellers going into 2018.



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- SALE INCLUDES EXTENSIVE LIST OF EQUIPMENT

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#### LEASED



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