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Is the 200,000 Square Foot Deal the new 800,000 Square Foot Transaction?

August 17, 2010 | Staff Writer | [PRINT ARTICLE](#) | [EMAIL THIS ARTICLE](#)

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The general populace in the US has become accustomed to such statements as '40 is the new 30' and 'Gray is the new Black'. Statements like these are no surprise as there is a constant need to recalibrate and re-adjust our direction based on current data.

In the Chicago-based industrial real estate universe where we prospect, developers, investors and brokers alike are regularly questioning the direction of the industry today. It seems that we are looking for a statement to define the current landscape and provide that solid direction. Although it may not be a certainty yet, based on the latest data available, one statement that deserves a further look would be "the 200,000-square-foot deal is the new 800,000-square-foot deal."



Infrastructure

In order to comprehend the nature of future deals, we need to quickly review Chicago's key components that allow us to complete transactions. Chicago's identity as the City of Big Shoulders has likely influenced the metro area's perceived reputation as a city of big industrial deals. In addition, Chicago's infrastructure platform lends itself to a wide variety of business opportunities. Chicago is the home to O'Hare International Airport, which is the 18th ranked cargo and 3rd busiest passenger airport in the world, placing it third overall behind Atlanta's Hartsfield and Beijing's Capital Airports respectively (Airports Council International).

Chicago is also the only city in North America where all six major Class I North American Railroads meet (US Dep. of Transportation). Oil pricing is the largest variable in transportation costs and is subject to a wide range of uncontrollable geo-political influences. This means rail will play an important role in the future of global transportation. As of 2009 Bill Gates controlled 34 million shares of the CN Rail, and Warren Buffet completed his acquisition of the BNSF.

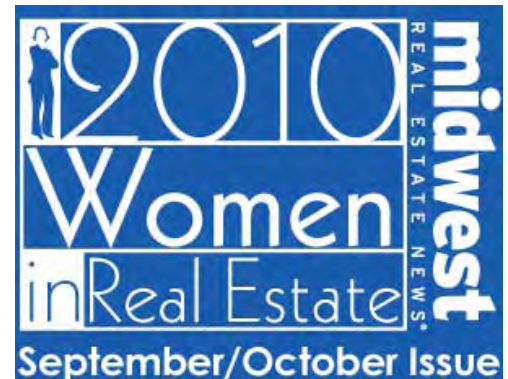
It is no surprise that two of the most visionary business minds in the world have concentrated their holdings in the rail industry. In addition to the six railroads, five federal highways intersect in the city of Chicago. Chicago's adjacency to the Great Lakes is another arrow in its quiver, solidifying its standing as a key cargo junction in America. More than 26 million tons of goods and natural resources travel through the Great Lakes' Port of Chicago annually (Illinois International Port District).

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Inventory

A location with this type of infrastructure in place lends itself to being a very attractive distribution hub. Nearly 1.2 billion square feet of industrial inventory exists in Chicago (CO-Star) which represents one of the largest industrial markets in the world. As a real estate community it might make sense to push the envelope to accommodate larger users. The only way to do this is to control land sites which enable developers to construct larger buildings. We will use 500,000 square feet as the definition of large buildings for the purpose of this dialogue. Accommodating these facilities forced developers to expand geographic boundaries. There was a time not that long ago when a map of the Chicago industrial submarket showed I-294 as its western boundary. Today, that same map stretches approximately 60 miles west of I-294 to the I-39 corridor.

Information

Recently, a colleague issued the statement that the 200,000-square-foot deal is equivalent to the 800,000-square-foot transaction of past glory days. On the surface this is an attractive statement given the nature of the economy and the current malaise of the real estate industry. Here in Chicago the numbers tell the tale. (Co-Star)

- Absorption –the change in total space occupied. Various research groups show negative absorption ranging from -30 million s.f. to -20 million since 2007
- Vacancy Rates have ranged from 9.5 to 12% since 2007
- Rent growth. None, however in some micro sub-markets rents have performed better throughout time
- 96% of deals done in Chicago since 2007 are <150k SF

Speculative Activity/Selected Lease Activity

Since 2004, 53 speculative buildings over 400,000 square feet have been constructed. Those buildings represent over 32 million square feet of inventory, approximately 2.5 percent of the entire market. Thirty Five of those 53 speculative buildings exceed 500,000 square feet. Since 2004 there have been approximately 30 new deals of more than 500,000 square feet completed in the metro area. The majority of the transactions were concentrated in consumer goods, the food industry and a variety of outsourced 3PL opportunities.

Of those deals approximately one-third were build-to-suits, with an additional third occurring in low second or high third generation buildings. Even with today's current market conditions, two of the rumored four deals greater than 500,000 square feet focused in the I-80 corridor are likely build-to-suits. Based on this data set I would conclude that large transactions lend themselves to specific build-to-suit opportunities, not speculative activity.

The Future

The current vacancy rate approaching 12.5 percent represents nearly 150 million square feet of vacant space. Of that vacant space 65 million square feet of it was built after 1980, with clear heights greater than 20'. A significant inventory of functional and relatively modern facilities exists, which effectively means no new speculative construction for the next 18-24 months. The majority of these buildings are multi-tenant in nature able to accommodate smaller users.

Deals less than 150,000 square feet dominate the Chicago market by a wide margin. Fuel costs, fluctuating supply chains, and relatively static population concentrations would indicate that speed to the consumer is the key factor in the distribution of goods. The way to accomplish this is by the utilization of smaller and more efficient distribution centers. There will always be large scale super regional distribution centers serving as statistical outliers. The 50,000 – 150,000-square-foot transaction is the engine behind Chicago's distribution dominance. Velocity has diminished, however the nature of the size and scope of successful transaction in Chicago should remain consistent.

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- April 2010 (99)
- March 2010 (1)
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