2010 Market Forecast

Blue skies ahead ... eventually

My market forecast covers the core industrial area of Denver comprising the central and northeast submarkets. This area contains roughly 112 million square feet of all varieties of industrial space, from manufacturing to showroom, but mainly warehouse/distribution and, therefore, represents a good picture of our industrial market.

We are currently in a slow recovery mode from the deepest recession in my 30-year commercial real estate career but we've seen this story before:

April 2008. We had sustained a decade of growth and prosperity. Nothing but blue sky with predictable absorption and a vacancy rate of 6.8 percent. Some 1.3 million sf of Class A space is under construction.

September 2008. I am on a golf vacation in Oregon (just helping the economy) while the market crashes. The industrial market seizes up along with commercial lending.

December 2008. The vacancy rate jumps to 8 percent. All new construction projects are put on hold. Miraculously, absorption remains steady with leases being negotiated on virtually all remaining Class A inventory!

June 2009. Vacancy rates rise to 8.5 percent. Leasing has continued at a slow pace. There are virtually no sales. Construction has stopped. General malaise sets in.

December 2009. Vacancy stands at 9.5 percent, the highest in 18 years. Class A vacancy makes up less than 1 percent of the availability, the lowest in 18 years. There is no new construction on the horizon and tenants have done a good job of flight to quality.

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What does it mean? Where will the tenants go?

Based on the other three recession recoveries I've survived, I would suggest the following moving forward through 2010:

■ **Absorption and vacancy.** The vacancy rate already has begun its descent. Large chunks of Class B space already have been taken during the first quarter. We will start to see competition for good, functional space by midsummer followed by slight rent growth.

The first signs of life will start during the third and fourth quarters of 2010 as users start scouting around for build-to-suit land after finding much to their surprise that there are no suitable large blocks of space for their operations.

■ **Construction.** The first signs of life will start during the third and fourth quarters of 2010 as users start scouting around for build-to-suit land after finding much to their surprise that there are no suitable large blocks of space for their operations.

■ **Lenders.** They will remain MIA because their MAIs (appraisers) will be reluctant to support the values. This will remain an obstacle until early 2011, when there is suitable evidence that a rental premium can be achieved for the scarce commodity of new, functional space. Then the rush to lend will happen again, perhaps a bit more tempered than the last expansion.

■ **Tenants.** They better have concluded their blend-and-extend negotiations with their landlords because rents are going up and landlords will be angry. There will be a disbelief that the market has firmed and they will be finding competition for quality space.

■ **Land.** Look for a bleak 2010 and a brisk 2011.

So these are the trends you can count on, but the ride will be bumpy. We will show great signs of recovery, momentum, rent growth, absorption and elation and then we will be *crushed, humbled and fooled* in unpredictable doses and this wash and rinse cycle will continue several times until mid-2011, when the blue skies return and we selectively forget our last cycle and proceed on another 10-year run.▲