

Commercial Real Estate Activity: “Increased in Most Districts”

June 1, 2016

The Beige Book report for June, which summarizes comments received from businesses and other contacts outside the Federal Reserve, suggested that economic growth during the most recent period was “modest,” with an uptick in the number of Districts seeing slower or marginal growth. Nonetheless, commercial real estate activity “increased in most Districts,” with **greater space absorption in Atlanta and Kansas City**. **Dallas** reported **healthy demand for office space**. A **decline in vacancy rates and a rise in rents** were noted in **Chicago and Minneapolis**, while contacts in **San Francisco** said **demand for commercial real estate expanded further**, particularly in urban areas with robust technology and health care industries.

Construction and real estate activity generally expanded too, with most Districts reporting an overall positive outlook (especially **Philadelphia, Richmond, and Minneapolis**.) Strong project pipelines were reported in **Cleveland**, and some contractors in **Atlanta** noted **one- to two-year backlogs**. An **uptick in industrial construction** was cited in **St. Louis**, while activity was varied across markets in **Boston**. **Multifamily construction continued to grow in many Districts**, including **New York, St. Louis, and Dallas**, but a slowing was noted in **Atlanta**. In **San Francisco**, construction of multifamily units continued to outpace single-family units. In **Boston**, apartment construction remained very active, but **related lending slowed among smaller banks**.

Economic Growth Characterization by District

	April Beige Book Report (through April 7, 2016)	June Beige Book Report (through May 23, 2016)
“Moderate” Growth:	Chicago, Minneapolis, San Francisco	San Francisco
“Modest” Growth:	Cleveland, New York, Philadelphia, St. Louis	Atlanta , Cleveland, Philadelphia, St. Louis, Minneapolis
“Other” (positive)	Boston (“rising sales and revenues”) Kansas City (“increased slightly”) Richmond (“strengthened”)	Boston (“generally improving”) Richmond (“continued to expand”)
“Other” (neutral/negative)	Atlanta (“unchanged”) Dallas (“flat to up slightly”)	Chicago & Kansas City (“pace of growth slowed”) Dallas (“activity grew marginally”) New York (“generally flat”)

Source: Federal Reserve **Bold** = change from prior report.

WAGES/EMPLOYMENT: Employment grew modestly since the last report, but **tight labor markets were widely noted in most Districts**. Demand for labor rose moderately in **Richmond**, and contacts noted continued difficulty finding workers in numerous occupations. In **Boston**, **staffing industry contacts observed robust labor demand**, particularly for specialized workers in high-skill fields. Contacts in **Atlanta** and Richmond said **high-skill workers in high-demand fields continued to be hard to find, and low-skill jobs were also becoming harder to fill**. In **New York**, employment grew modestly, and manufacturing and services firms planned to add jobs in the months ahead. **Soft labor markets were reported in energy sectors in Cleveland, Atlanta, Minneapolis, Kansas City, and Dallas**.

Wages grew modestly, with increases concentrated in areas of labor tightness. Higher wages were reported for entry-level and lower-skill positions in **Richmond and Atlanta**. In **San Francisco**, **minimum wage increases** pushed up wages for low-skilled workers, with diminishing effects up the pay scale. **Atlanta, St. Louis, and San Francisco** reported **wage pressure for certain high-skilled employees**. In **New York**, a sizable share of service-sector contacts reported higher wages. Wage pressure was minimal in the **Dallas** District, due in part to **compensation at energy services firms that was steady to lower for staff that have been retained**.

Below, we detail specific comments by District on commercial real estate.

Heidi Learner, Chief Economist
hlearner@savills-studley.com 212-326-8648



District	Comments on Commercial Real Estate
Atlanta	“Commercial real estate contacts continued to report improvement in demand resulting in increased absorption and rent growth across property types , but cautioned that the rate of improvement varied by metropolitan area, submarket, and property type . Most commercial contractors indicated that the pace of nonresidential construction activity had increased from one year ago, with many reporting backlogs of one to two years. Amid ongoing concern regarding the overbuilding of apartments , reports from District multifamily contacts suggested that there has been some pullback in the pace of construction. Looking forward, most commercial real estate contacts expect the pace of nonresidential construction activity to increase slightly over the next quarter . However, expectations for the pace of multifamily construction activity are mixed.”
Boston	“Contacts report that commercial real estate leasing activity is steady or improving across the First District... Boston's office leasing environment remains strong, yielding further declines in vacancy rates, although tenants appear reluctant to commit to new leases on the most expensive spaces ...Investment sales are steady in Boston, Portland, and Hartford, although the bidding environment remains less exuberant in Boston than it was a year ago ...Office construction continues to increase in Boston but remains below normal relative to fundamentals...Apartment construction remains very active in Boston. However, contacts say lending for apartment construction is slowing among the region's smaller banks as they seek to stay within their own pre-set limits on that sector's loan allocation. Contacts across the District are mostly optimistic that commercial real estate activity will hold steady or improve in coming months, although one Boston contact notes the risk of a modest slowdown in office leasing .”
Chicago	“ Demand for nonresidential construction was little changed overall , but one contact did note an increase in industrial construction. Commercial real estate activity rose modestly, with contacts reporting gains in both the for-sale and for-lease markets, particularly in urban areas . Activity was distributed across segments, but was particularly strong for retail. Rents edged up, vacancy rates decreased somewhat, and the availability of sublease space was little changed.”
Dallas	“ Demand for office space was healthy in Austin and Dallas-Fort Worth, but deteriorated in Houston where sublease space continued to rise, putting pressure on office rents . Industrial leasing was generally active and vacancies were tight. In Houston, however, the picture was mixed as the market benefitted from ongoing petrochemical expansions and solid demand from retailers and third party logistics firms, but experienced an increase in industrial sublease space in the first quarter partly due to weakness in oil and gas-related manufacturing.”
New York	“Commercial real estate markets have been mostly stable thus far in the second quarter . In Manhattan, office availability rates edged up, and asking rents were flat, though still up moderately from a year ago . Across the rest of the New York City metro area, however, office availability rates edged down and asking rents climbed. In upstate New York, availability rates were steady to down slightly, and asking rents were little changed. Industrial markets continued to tighten across the District , with asking rents continuing to climb and vacancy rates edging down to multi-year lows.”
Philadelphia	“Nonresidential real estate contacts, predominately in the Greater Philadelphia area, reported little change in the ongoing modest gains in construction activity and in leasing activity . A developer noted that office projects have been in greater demand for over a year, while industrial/warehouse buildings have remained strong for many years. One contact indicated that existing tenants have been opting to expand at an increased rate; another noted that demand for relocation to downtown space has grown from outside firms .”
Richmond	“On the commercial side, leasing activity increased moderately overall . A commercial real estate development company in Richmond reported a very active market for retail and grocery stores. In Washington, a contact noted that limited available office space for rent was pulling vacancy rates down...rental rates and vacancy rates varied across submarkets and locales. With respect to commercial construction, increased activity was reported in Charleston, South Carolina, Charlotte, Richmond, Washington and Baltimore .”
San Francisco	“Real estate market activity grew at a robust pace across most of the District...growth in the construction of multifamily units continued to outpace that for single-family units. Contacts reported construction lead times of up to six months for multifamily projects in some urban areas constrained by shortages of skilled labor and building materials . Building permits for all types of residential construction picked up in most parts of the District. Demand for commercial real estate expanded further, most notably in urban areas with robust technology and health-care services industries . Contacts in states that have legalized sales of cannabis products noted a pickup in demand for retail storefront property.”