

LOW INVENTORY

JUST ONE FACTOR FUELING BTS DEVELOPMENT

By Curt Hefner, SIOR

For the last seven years, industrial real estate users gravitated towards the abundance of vacant buildings created by the “Great Recession.” As the market has recovered, that abundance of vacant buildings has quickly turned into downright scarcity. The lack of quality space has led many users to look at an option that they would have never considered in 2010, a build-to-suit (BTS). The current market forces have created a surge in BTS development and we believe that this will not be a short-term trend. Everyone from the largest e-commerce users to regional companies are finding value in BTS solutions for their distribution needs.

For the brokerage community, understanding the BTS process is essential to ensuring client satisfaction. The key is to set clear expectations for your client and surround yourself with an experienced and capable team. Ground up construction is inherently more complicated than leasing or purchasing an existing building, but there are a number of ways to streamline the process and mitigate risk.

HOW MARKET FORCES FUELED THE GROWTH OF BTS

A lack of existing product is not the only factor contributing to the increase in BTS activity. First, industrial users have increasingly specialized requirements for their facilities. Whether it is clear height, trailer parking, outside storage or security requirements, the standard speculative building or 10 year old facility does not meet their demands. Secondly, the speculative development community is concentrating on the “big box” distribution product. Most spec buildings are at least 400,000 square feet in any market that I travel to and most are over 600,000 square feet. The majority of tenants, who occupy less than 200,000 square feet, are being ignored by the new developments and their options are very limited.

ADVANTAGES AND DISADVANTAGES OF BTS

There are numerous benefits that industrial users find in BTS facilities: building specifications, location, expansion capability, single tenant occupancy, and additional security.

First and foremost, a user can get exactly what they need where they need it. Because the building is custom built to their specifications, they can ensure it satisfies all their requirements for an efficient operation. Many companies have similar space needs in multiple markets and can benefit from developing standardized facility designs. Having standardized facilities can help improve consistency across the supply chain, improve employee safety and minimize interruptions during the move in process. Being able to select an optimal location allows users to save on transportation costs, improve proximity to major customers or suppliers, and take advantage of local incentives.

A BTS facility also allows the client to have greater control of their future and their environment. A high percentage of the facilities that we have built incorporate some additional land designed for future expansion. Unlike a one-time right of first refusal offered in an existing building, expansion land cannot be leased out from under the client. That land is exclusively at the user’s disposal and can be utilized at their discretion. The other issue that is becoming more important to users is site and product security. In addition to the traditional list of security concerns, many governmental programs like Foreign Trade Zone (FTZ) and Customs-Trade Partnership Against Terrorism (C-TPAT) have strict security requirements for compliance. A single tenant building offers the highest level of security and the easiest path to compliance.

COMMON MISCONCEPTIONS

There are two excuses that we consistently hear as to why clients shy away from build to suit: the cost of building new and the time and effort it takes to build.

There is no getting around the timing issue. If a user needs to occupy a building in 30 or 90 days, a BTS is not an option. However, we find that perception is much worse than reality and most users do have the time to pursue a BTS facility. The lack of existing product currently available in the market has forced users to focus on looking for new space 12 to 18 months before their lease expiration. With rare exception, that is plenty of time to design and construct a new building.

Cost is the other issue that is frequently brought up, but we really only find that to be the case when you compare a brand new BTS facility with a 20 year old Class B or C facility. Almost every market across the country has experienced a dramatic rise in rental rates as vacancy rates continue to fall. As new speculative developments begin to deliver in the major distribution markets, the quoted rental rates are at an all-time high. This has virtually eliminated any cost premium for a BTS solution. In addition, the cost equation isn't just about what you pay; it's about what you get for your money. There is a value to all of the advantages mentioned earlier in this article.

The bottom line is that cost is no longer the deciding factor. Often the decision comes down to timing and appropriateness. The client must determine whether they are willing to plan ahead to get what they want or if they're willing to make compromises to get something last minute.

Once the decision is made to pursue a BTS, turning to a company with experience and resources is vital to the success of the project. Experienced BTS developers understand the nuances of the process and can help you and your client avoid common pitfalls. They can guide the project through the complexities of site selection, governmental agencies and even outspoken neighbors. They can help you set expectations for your client, eliminate surprises, mitigate risk and deliver on what was

promised. Happy clients make happy SIORs and partnering with the right developer will dramatically increase the probability that your client will think of you as a BTS Rock Star at the end of the day.

Inventory is one of the reasons why BTS is growing in favor. However, a well-run BTS project can deliver several other advantages for your clients.



ABOUT THE AUTHOR: CURT HEFNER, SIOR, is Senior Vice President of Investments of Becknell Industrial. He is responsible for business development focused on new build-to-suit development opportunities across the U.S. Hefner works closely with the brokerage community, clients and corporate facility managers to identify client needs and coordinate resources, from site selection and design to final delivery of the facility.