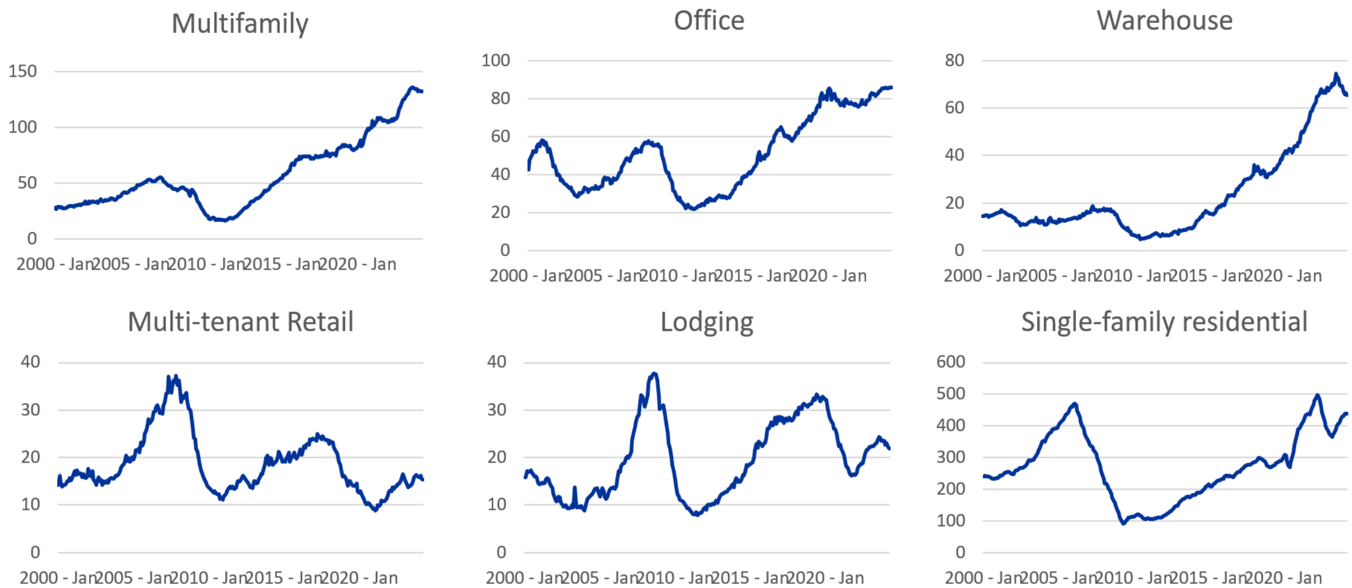
Chart of the Week – June 28, 2024
Value of Private Construction Put-in-place
($billions, SAAR)



Source: US Census Bureau

Physicists have protons, neutrons, and electrons. Biologists have DNA and RNA. And economists have supply and demand -- the building blocks upon which most of our understanding of markets rest.

In commercial real estate (CRE), demand is driven by a variety of economic, demographic, and other factors that occasionally ebb but generally flow – increasing the overall need for CRE space but with periods of pullback or consolidation.

Supply is driven by developers seeing opportunities to deliver space whose costs to build are less than the value that property will command given expected market incomes and valuations. When the cost to deliver is less than market value, project development flows.

The level of private construction put-in-place for different property types is like tree rings showing periods and conditions that brought developers forward. This week's Chart of the Week highlights trends in the value of private construction put-in-place as it pertains to the different property types using data from the U.S. Census Bureau.

For multifamily and industrial/warehouse, mismatches between supply and demand meant rapid increases in rents, incomes, and values. Low interest rates, cap rates and values then drew developers in droves – pushing the value of construction put in place to record levels.

Conversely, construction of retail and lodging properties grew prior to the pandemic but shifted downward when shutdowns and other social and government responses immediately and dramatically hampered those property types.

With hindsight, the level of construction of office properties perhaps seems curious. But office properties – and their loans – performed well during the early days of the pandemic as companies continued to pay rent even when not using their space and then migrated to the highest quality (newest) space when renewing leases.

Census data on building starts shows that multifamily developers have already adjusted their new construction activity downward in response to interest rate, cap rate, and supply/demand conditions. The same is certainly true for other property types as well.

In the dance of supply and demand, demand generally takes the lead but – as in any great dance pair – the follower, in this case supply, determines the degree to which the pair stay in sync.

- Jamie Woodwell (jwoodwell@mba.org)