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The trifecta driving Midwest corporate real estate investment

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The Chicago real estate market endured a bruising slowdown after the 2008 recession, and lagged behind its coastal counterparts in its recovery. Finally, though, the market is back on its feet and poised for growth. While the period from 2008 to 2013 was defined primarily by cutting costs and increasing efficiency—often by moving production overseas or to Mexico—this trend is beginning to reverse.

A combination of energy and transportation costs, manufacturing innovation, and the emerging demands of e-commerce are driving the Midwest's real estate growth, and providing clues to its future.

1. The Transportation Tipping Point

The Midwest's attractive energy rates are a key element of the market's recovery. The lure of cheaper resources abroad is waning in favor of proximity to large population centers and affordable transportation costs.

Transportation costs in the Midwest are becoming nationally competitive: diesel fuel prices have declined 2.6% since August of 2013 compared to a national average of 1.5%, while the cost of electricity also remains below average, according to the BLS. With six of the nation's seven largest rail lines passing through Chicago, the UPS worldwide air hub in Louisville and the FedEx "SuperHub" in Memphis, regional firms are granted access to both local and international markets.

Taken together, businesses that choose to double down on the Heartland not only reap the benefits of lower transportation expenses, but also quicker entry into population centers.

2. The Digital Manufacturing Drive

Technology advancements and the gradual uptick in firms moving operations back to the U.S. will also play a large part in fueling Chicago area investment. To take advantage of new processes like additive manufacturing (commonly known as 3D printing), many firms are choosing to reshore in Chicago, near major population centers and a forthcoming digital manufacturing hub.

The Digital Manufacturing and Design Innovation Institute, announced in February, promises to serve as a guiding force in the Chicago real estate market. The digital manufacturing hub will attempt to reduce development costs while spurring activity in the industrial sector through government, academic and private sector partnerships. Already the project has attracted a host of companies (from Boeing to Procter & Gamble), and investments from many more that anticipate increased activity in the Midwest market.

While the Institute is outfitted to support manufacturing operations, it is more than likely that new ventures and spinoff companies generated by the initiative will require additional facilities.

3. The Brick-and-Mortar Side of E-commerce

Despite their propensity to displace retail outlets, e-commerce giants are absorbing industrial real estate at an astonishing rate. Everything from warehouses to server banks require storage close to the markets they serve. Its central location and access to population centers makes the Midwest a natural destination for e-commerce retailers looking to expand (see, for example, Amazon's not one but two distribution centers in Wisconsin.)

The proliferation of same-day shipping promotions is another notable influencer, magnifying the importance of developing distribution facilities near population hubs. While perhaps not all of the Midwest will see retail-driven industrial real estate demand (offerings like same-day shipping require a critical mass before they make financial sense), those closest to its big cities are positioned to take advantage of impressive growth, creating a hub-and-spoke effect. Amazon's forthcoming 1.1 million and 500,000 square foot Kenosha distribution centers, for example, are likely to spur smaller, satellite fulfillment facilities in nearby urban areas (including Chicago and Milwaukee.)

Even where same-day shipping is off the table, the Midwest remains an attractive market for e-commerce firms. The region's highly developed intermodal capabilities provide national reach at extremely competitive rates. A central location with a broad, efficient transportation network offers significant advantages over a swath of local hubs, making the Midwest a supply chain destination for players in the e-commerce space.

Flexible Development

Overall, the most prominent forces influencing Midwest industrial real estate are those seeking to take advantage of the market's flexibility. Whether it's an established e-commerce company or a manufacturing startup, the availability of well-developed transportation options and affordable energy rates places the Chicago market high on any firm's list. On the flip side, e-commerce and manufacturing businesses will play a large role in determining future real estate investment in the region. Those properties best suited to fulfill the needs of these core industries (e.g., warehouses, data centers, fulfillment hubs) are likely to command high valuations and guide future development efforts.

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