

Construction Outlook: Panel Expects Big Declines For All Sectors
Greater Phoenix Blue Chip
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The reality of the extent of the downturn in the residential housing market has clearly set in with the *Greater Phoenix Blue Chip Real Estate* panel. The panel now expects a decline in single family permits of more than 43% to a level of about 17,600 permits in 2008. This is a decline of about 72% from the peak in 2005 making it one of the most severe housing cycles on record. To give some perspective to the 72% decline from the peak to the current expected level, the peak to trough decline in the 2001 recession was a very modest 4%. From the peak in 1986 to the trough in 1990, the decline was about 54% for single-family housing and from the peak in 1978 to the trough in 1981, the decline was about 63%. The early 1960's downturn saw a decline of 74%.

The *Blue Chip* panel does expect a recovery next year, however, to approximately 22,300 housing units, a 26% increase. Even if that increase occurs, it would still make 2009 the weakest year (with the exception of 2008) since 1992.

Apartment permits are also expected to decline to just under 5,000 units, a decline of 25% from the 6,600 units of last year. Multifamily units are expected to decline another 13% in 2009 because absorption for apartments is expected to approximate zero this year and only 2,800 next year. Vacancy rates are likely to increase to more than 9% in both years. This situation can only occur if population flows have slowed dramatically which appears to be the case.

As expected, given the current set of economic conditions, the outlook for commercial construction is less than sanguine. Office construction is expected to be approximately 3.6 million square feet this year, but only 710,000 square feet are expected to be absorbed. This could push year-end vacancy rates to close to 17%. In 2009, only about 1.7 million square feet of space is expected to be added to the market while 1.2

million square feet should be absorbed. This would push vacancy rates to the 18% level, the highest on record since 2003.

Retail construction is also expected to slow dramatically from 11 million square feet last year to a little over 7 million square feet this year and 4.3 million square feet next. Absorption is also expected to slow dramatically from 9.4 million square feet last year to 5.0 million square feet this year and less than 4.0 million square feet next. As a result, vacancy rates are expected to jump to 9.2% in retail by the end of 2009.

Construction of industrial space is also expected to slow dramatically and vacancy rates will hit double-digit levels. Construction, which was more than 13 million square feet in 2007, is estimated to drop to about 7.3 million square feet this year and 5.7 million square feet next, while absorption slows from more than 8 million square feet last year to less than 2 million square feet this year and about 3 million square feet next. Vacancy rates should end the year at more than 11%. Given present trends in the economy, these projections could easily prove to be optimistic.

Overall, the construction outlook is ugly. No significant improvement is expected in single family activity and commercial activity is expected to slow.