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Industrial Property Squeeze Play

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Why is it that in 2007 popularly sized industrial buildings in the boroughs of New York City are beginning to sell in excess of $300.00 per square foot? More importantly, how will this phenomenon affect the future of New York City?

To start at the beginning, one needs to first look at the unfolding dynamics of rapid demographic change. Bricks and mortar, in and of themselves, have no intrinsic value but that which is imparted to them by the market's desire to obtain and utilize them. This market is made up of a burgeoning, young group of 20 to 30 year old professionals who are increasingly courted by city based businesses offering the dream of a creative urban lifestyle.

This demographic shift has fueled the rebirth of new neighborhoods, such as the meat packing district on West 14th Street, but more significantly, has forged an unstoppable impetus for the conversion of outlying industrial neighborhoods to residential use.

When a public need coincides with tremendous profit potential, politicians take note and public policy changes soon thereafter. The result? Great swathes of Queens and Brooklyn having their exclusive industrial blocks re-zoned to allow for residential mixed use development. Better than winning the lottery, owners of factories and warehouses, simply by the stroke of a pen, have had their net worth increased tenfold. The results are there to see by taking a quick drive through Greenpoint, Williamsburg, or Long Island City.

Now we have the direct cause for that popularly sized industrial building fetching over $300.00 psf. But the chain of causal effects does not stop there. Imagine yourself owning a property across the street from a newly minted residential zone. If only the zoning line could be changed, millions would drop into your bank account. You're not alone in suffering from this seemingly arbitrary re-districting. Our politicians, vigilantly willing to right wrongs and help the oppressed, have created a buffer district named an "Ombudsman" area. These buffer areas would permit, on a case-by-case basis, a change from industrial to residential usage.

This then has become the final causal factor in creating the $300.00 per square foot industrial property. While clearly pure demand from relocating businesses out of a newly minted residential neighborhood would cause price appreciation, the well founded anticipation that one's industrial property will eventually be zoned residential, provides the real price kicker.

What does this mean for New York? Clearly, an accelerating cycle of de-industrialization will result in the cost to operate a factory to become prohibitive as its profit potential as a development site continues to escalate. An excellent example of which would be Pfizer's recently announced closing of its flagship 660,000 sq. ft., 155 year old factory in Bushwick, Brooklyn. If the production of a high-value "intellectual product such as pharmaceuticals doesn't make sense in light of rising industrial property values, does the manufacturer of widgets stand a chance?

The snowball affect of de-industrialization is also helped along by the shortening of the length of the lease offered by property owners. This only makes sense with the possibility of a 3-year window, in which industrially zoned property could be rezoned; then, should a landlord be tied up with a 5 or 10 year industrial lease. This increasingly common lease term demand has already begun chilling the relocation of new industrial firms to the Brooklyn and Queens areas, as well as the expansion of existing ones.

As this marriage between demographic change and real estate development continues, New York City will witness costly pressures on its public educational system and its infrastructure. New school construction, significant curriculum changes, bridge and road widening, subway extensions, and intermodal rail to highway freight mega projects will all be required rather quickly.

A good example of such a massive civic undertaking is the proposed multi-billion dollar Cross Harbor Project, which will provide a rail tunnel connecting Jersey City to an intermodal freight transfer yard in the heart of Maspeth, Queens. A 20 year project, its future is hanging on the analysis of whether the flooding of Maspeth, the geographic center of New York, with fully loaded rail cars, will actually reduce inter-city traffic or increase it.

What all this portends for New York City is that no taxing method or traffic control technique will be considered off limits. Will we see E-Z Pass zoned districts in Manhattan? Probably. Some form of personal property tax as in Connecticut? Probably. Special use district real estate tax add-ons? Probably. Increase in personal income tax? Probably. Continuation of draconian traffic fines and ticketing? Probably. Increase in property transfer taxes and filing fees? Probably. A dynamic, creative and enlivening urban environment offering unparallel city life? Probably. The possibility of finding an industrial building for under $300 per square foot? Probably not.

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