Secondary And Tertiary Markets Are Taking The US Into Extra Innings

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Select tertiary markets are driving the economic expansion and will likely continue to do so for the balance of this year and well into 2019.

June marked the 9th year, or 108 months, of economic expansion in the U.S., the second longest in U.S. history. It has the potential of overcoming the longest period of growth in America (120 months from 1990 to 1999) if the current expansion makes it to July 2019.

Most of the recovery since the Great Recession wound down toward the end of 2009 and the early months of 2010 has occurred in primary markets and gateway cities, yet beginning a couple years ago investment and development capital was increasingly directed toward secondary markets – a trend that has become dominant in the current economy.

In fact, in ULI's 2018 Emerging Trends Report (Urban Land Institute) from the 78 U.S. markets surveyed, the top 20 were comprised of four of the top secondary markets, four markets that are adjacent to primary or gateway markets, ten secondary markets and just two primary markets. As one national office investor noted for the report, "Traditional gateway markets have gotten so competitive that we are looking at adjacent submarkets and the top secondary markets."

I would take it a step further and say that select tertiary markets are also driving the economic expansion and will likely continue to do so for the balance of this year and well into 2019.

By way of examples, I spoke with leaders from our firm in the secondary markets of Orlando, FL and Salt Lake City, as well as the tertiary markets of Central Wisconsin and Ocala, FL.

"The Orlando market was good in 2016 and probably the first "good" year since the recovery began, while 2017 was flat and the first half of 2018 has been on fire," according to **Robin Webb**, CCIM, CPM and Managing Director/Principal of **NAI Realvest** in Orlando.

He attributed high volumes in both sales and leasing activity to ongoing organic growth plus annual in-migration of 50,000 to 75,000 people, the strength of the Central Florida Research Park and phenomenal growth in the hospitality sector, only a portion of which is connected to Disney World, by the way.

"Multifamily rents are up 7 percent year-over-year, the unemployment rate is around 3 percent, industrial vacancy about 4 percent and the office vacancy rate just dipped below 7 percent, which is really remarkable considering that office vacancy was 16 percent in the depths of the recession," Webb said. Orlando ranked 16th overall on ULI's 2018 Markets to Watch (a section of the Emerging Trends Report) with an investment score of 3.49 (21st) and development score of 3.42 (11th). He said the most active buyers and developers – especially on land deals for multifamily, have been locals or outside firms that have been in the Orlando market for quite some time.

In June two office buildings with a combined occupancy rate of 85 percent sold for $39.19 million in Central Florida Research Park (CFRP), which is 1,027 acres, employees 10,000 people and is located adjacent to the University of Central Florida and 13 miles northeast of downtown Orlando. Banyan Street Capital and funds managed by Oaktree Capital Management L.P. sold the 244,549-square-foot (combined) buildings to TerraCap Management LLC for $160 per square foot.

"Our recovery started five or six years ago and was originally fueled by local investors that knew the intrinsic value of the market and had confidence in our community. However, as The San Francisco Bay Area tech economy boomed Salt Lake City became a direct beneficiary and as the expansion matured, we've seen a ton of outside investment money coming to our market," said **Marlon Hill**, Principal Broker/Managing Partner with **NAI Premier** in Utah.

He added that it is not only tech companies driving Salt Lake's growth.

"Businesses that come here invariably say in part it is because of the quality of life we have to offer, educated labor pool, good communities and schools and reasonably priced housing. I think you'll find combinations of these elements in all the secondary and tertiary markets that are doing well," Hill said.

ULI's 2018 Emerging Trends report ranks Salt Lake City third overall among the 78 markets surveyed and the number one investment market in the U.S. with a score of 3.79. In May Facebook announced it would build a $750 million data center spanning nearly one million square feet in Eagle Mountain, which is on the I-15 corridor 39 miles south of Salt Lake City. The social media giant also said it would spend at least $100 million to expand the city's infrastructure to accommodate the project.

Wisconsin made national news a year ago when Foxconn Technology Group announced it would build a $10 billion plant in southeastern Wisconsin to make display panels used in televisions and other products. The Milwaukee suburban cities of Racine and Kenosha – which already have a robust industrial market, are bound to be prime beneficiaries of the new 20 million-square-foot campus. According to published reports, the new Foxconn plant is expected to initially employ 3,000 and may create an additional 22,000 related jobs in the future.

In Appleton, Secura Insurance Co. is building a new 300,000-square-foot, $90 million headquarters office building on the west side of town, with plans to sell its current 190,000-square-foot facility while Gulfstream (based in Savannah, GA) recently announced that it would add about three hundred (mostly office) jobs in a deal featuring a ground lease at Appleton International Airport (ATW), and a build-to-suit for a 180,000-square-foot maintenance, repair and overhaul facility, according to **Mike Pfefferle,** President of **NAI Pfefferle** with offices in Appleton, Wausau and Green Bay.

Pfefferle added that U.S. Venture Inc., a local Fox Valley company, plans to break ground in downtown Appleton in 2019 to construct their corporate headquarters consisting of 200,000 square feet with a total value of approximately $50 million.

In Green Bay, Schreiber Foods recently built a new 250,000-square-foot headquarters while the Packers' have started leasing office space at its mixed-use, 45-acre development — Titletown District at Lambeau Field, and will soon introduce a residential component to the project. The famed football club has also partnered with Microsoft to roll out an incubator program called Titletown Tech. Last year the kitchen and bathroom plumbing behemoth Kohler Company opened a new hotel (Lodge Kohler) just yards from Lambeau Field in the heart of Titletown.

In addition, "Dollar General has grown throughout Wisconsin and the Midwest in rural cities over the past several years and will continue to evaluate opportunities in the area for future locations," says Pfefferle. He estimates that the retailer has built over 150 stores in small cities and towns in the state and adjacent states since 2004.

The economic expansion is even impacting Ocala, FL, a community of approximately 250,000 people in a rural area located along Interstate 75 in Central Florida and about 75 miles due east from Daytona Beach.

"We're essentially out of industrial inventory with most of it occupied by local businesses while in the last six months we have been getting calls from national companies for 3,000 square feet to 5,000 square feet of office space requirements, which we have not seen in years," said **Randy Buss,** CCIM with **NAI Heritage** in Ocala.

Ocala's office vacancy rate was 6.4 percent at the end of the first quarter this year and its industrial vacancy rate in the same quarter was 6.1 percent, according to CoStar. A new 150,000-square-foot industrial building was added to the market and another 450,000 square feet is under construction in the market, reports CoStar.

Tech's Big 5 (outside of Silicon Valley, San Francisco, LA's "Silicon Beach," New York's "Silicon Alley" and downtown Chicago)

While doing research for this article, we found data that demonstrates how significant the technology industry is to the U.S. economy and how it has spurred growth in some of the country's secondary markets. According to the U.S. Census Bureau and top MSA's in the U.S. (Metropolitan Statistical Areas – Population), in the 2000 survey Seattle ranked #19, Denver #25, Salt Lake City #46, Austin #48 and Raleigh #51. By 2017 (these are the Bureau's estimates and are unofficial), Seattle had moved up to #15, Denver to #19, Austin made the biggest jump to #31, Raleigh moved down eight notches to #43 and Salt Lake actually dropped back to #48. One suspects that Salt Lake City's "decline" was only because so many other markets got bigger-faster, such as Dallas/Ft. Worth and Fort Lauderdale.

Jay Olshonsky, FRICS, SIOR, is president of NAI Global. The views expressed in this column are the author's own and not that of ALM's Real Estate Media Group.