



Rapidly increasing construction costs concern contractors, developers

By **ERIK PISOR**, The Daily Transcript

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Whether it's industrial, commercial or residential construction, a common obstacle any developer or contractor must spar with is construction cost increases, which were the topic of discussion for one panel during a recent **Burnham Moores Center for Real Estate conference at the University of San Diego.**

"With 80 percent of our costs (labor, material, equipment and land) increasing rapidly, this is a timely discussion," said Dennis Cruzan, founder of Cruzan|Monroe, a real estate investment and development company.

While the price of land has risen -- a 400 percent jump for commercial land in the past 10 years, according to the Urban Land Institute -- the largest concern among contractors and developers appears to be construction material price increases.

In previous years, labor constituted 50 percent of construction costs -- excluding the purchasing of land and equipment -- and materials represented the other 50 percent, according to Matthew Reno, founder of Reno Contracting Inc.

"Now you see that material is 60 percent to 70 percent of the cost of construction," Reno said, adding that economic factors such as natural disasters can result in specific locations requiring more construction materials in order to rebuild. "The costs we're seeing today are really driven by supply and demand."

Giving an outside-the-county perspective, David Allred, executive vice president of the Douglas Allred Co., an industrial developer, said he has seen construction material increases of 15 percent to 20 percent in Phoenix and Orange County, where the company focuses its development activities. Surges in steel and concrete prices made the company's costs increase from \$28 to \$32 a square foot to \$55 per square foot.

The cost of concrete likely will continue to increase, since the majority of it used in the Southwestern U.S. comes from Cemex in Mexico, the world's third-largest producer. Allred said the current cost of concrete per yard is cheaper in California than Mexico. However, Cemex already has announced California will soon pay the same figure per yard as builders in Mexico, which requires developers and contractors to plan ahead when laying out a project.

"It's really important for us to work for a seasoned developer that has a good historical background in terms of their yields and what the land prices are," Reno said, adding that it's also vital to formulate a good team consisting of a developer, contractor and architect.

In response to past material increases, Allred Co. resolved to start development projects in inland markets such as Arizona, where land was cheaper and building costs and rent were similar to San Diego's.

"You go to a different market and you're able to maintain a higher yield and your costs into the project are the same," Allred said.

Besides construction cost increases and permit fees paid by builders, certain city traffic mitigation fees can also affect the overall price tag of a project. Reno said traffic mitigation fees typically add \$500,000 to a large industrial project, but now he's seeing those fees increase to as much as \$800,000 a project.

"The municipalities are looking to the private sector to finance public projects. ... People are OK with that, but it's the process that we have to go through," Reno said.

Allred said a recent project it undertook in Lake Forest, Calif., required the company to pay \$10 per square foot in traffic mitigation fees; however, in Phoenix the company pays less than 50 cents per square foot.

These fees and other cost increases are passed on to the homebuyer who or business that occupies the building. Combine this with the already high sales price here, and it becomes clear why some businesses are moving their operations out of the county.

According to Allred, big businesses are looking for a more economical alternative in terms of location, such as Imperial County where land and housing for employees are less expensive.

A cheaper alternative is something businesses shouldn't expect in San Diego County in upcoming years. Reno predicts a 0.5 percent increase per month in construction costs depending on product type. This would equate to an overall increase of 9 percent in 2006.

"Those things are very hard to predict," Reno said. "(But) I don't see anything in the foreseeable future (that would drive costs down)."