

Real Estate Journal

THE LARGEST BUSINESS PUBLICATION OF ITS KIND IN THE NATION

Suburban office market posts positive gains for 2005; leasing activity strong as we begin 2006

gh Garry Holmes



R.W. Holmes Realty Co.

cj Craig Johnston



R.W. Holmes Realty Co.

The Boston suburban office market has experienced nine consecutive quarters of positive net absorption. 2005 proved to be a pivotal turn around for the suburbs with 2.2 million s/f of net absorption. The combined availability rate for the 78.6 million s/f market has declined to 23.1%.

The Framingham/Natick area continues to be the strongest submarket with a combined availability of 8.6% while the I-495 North market continues to lag behind at 30.4%. The Central 128 corridor exhibited the greatest improvement, with the availability rate declining to 18.3% (a sharp contrast to the 27% availability a couple of years ago). More importantly, first class rents for trophy properties along Central 128, now achieve rents between \$32 - \$34 per s/f.

The I-495/Mass Pike office market had limited success for 2005 and still posts a hefty availability rate of 28.1%. Southborough and parts of Westborough have benefited directly from the scarcity of options in Wellesley/Natick/Framingham; however, communities directly along I-495 are facing limited demand with most of the requirements for space below 5,000 s/f.

One of the biggest challenges for

property owners these days (outside of finding tenants) is coping with the substantial increase in construction prices. What would previously cost \$15-\$18 per s/f for building out second generation space is now at \$22-\$25 per s/f, while space in shell condition is averaging \$38-\$40 per s/f. With rental rates for class "B" properties averaging \$17 per s/f (of which \$7.50 per s/f on average goes toward operating expenses and real estate taxes) property owners cannot make sense out of a lot of deals unless they are fortunate to find a tenant with minimal build out needs.

A decrease in vacancy, along with rental appreciation is resulting in substantial investor interest in Suburban office properties. Some recent investor activity includes: 293 Boston Post Rd., Marlborough, 199,005 s/f class "A" office building selling to Lincoln Properties Co. for \$17.6 million; 377 Simarano Dr., Marlborough, 156,630 s/f sold to Spear St. Capital for \$25.5 million; and One Research Dr., Westborough, 283,261 s/f office building selling to KBS Realty Advisors for \$55.5 million. Looking at the Central 128 market we see investors such as The Davis Cos. acquiring 1210, 1220 and 1230 Washington St. in

Newton, 89,525 s/f, from Berwind Properties for \$16,508,625; Transwestern Investments purchasing 313 Washington St., Newton, a 84,860 s/f office building for \$12.6 million; TA Associates selling 100, 200 and 300 Fifth Ave. in Prospect Hill Office Park in Waltham for \$62.3 million to Broadway Real Estate Partners; Boston Properties acquiring Prospect Place (296,399 s/f) from TA Associates for \$63.1 million; Paradigm Properties buying 101 Walnut street in Watertown, a 100% occupied 94,000 s/f office building for \$20.15 million.

The Andover area witnessed several noteworthy deals with J.P. Morgan structuring a joint venture deal with Brickstone Properties for Minuteman Park; Transwestern acquiring Brickstone Square (\$77 million); and New Boston Fund purchasing New England Business Center for \$34 million.

As core submarkets move through the recovery cycle and into the expansion cycle (the stage where rental rates reach a level to justify new construction) we are experiencing a few developers testing the waters such as: The Davis Cos. redeveloping the former Polaroid site in Waltham, now the Reservoir Woods, a 448,000 s/f office and research campus, with three tenants presently committed to leasing 227,320 s/f. Carruth Capital is clearing a site at the entrance to Westborough Office Park, for a large campus user for up to 750,000 s/f; and Capital Group Properties in the final permitting process to build a first class 50,000 s/f office building in Southborough. In 2006, we expect a

few more developers to start focusing on new construction.

The Mass. economy is "running out of gas and is slowing to a virtual standstill" according to the Benchmarks Bulletin issued in early January by the University of Mass. Donahue Institute and the Federal Reserve Bank of Boston. Real gross state product growth in the third quarter slowed to an annual rate of 1.6%, compared to a national growth rate of 4.1%, the report indicated. The State's economy under pressure from the cost of living, outsourcing and competition in the technology sector, is expected to grow at an annualized rate of only 0.3% over the next six months, according to the report.

From our viewpoint, activity from companies looking to lease space is strong, as we begin 2006. There continues to be an up tick in venture capital funding with expansion from our traditional software, high tech and service industries. There are a number of companies looking for space in the suburbs which is being driven by expansion needs. Job creation will certainly be moderate for 2006. However, we are still forecasting 2 + million s/f of positive net absorption for the suburbs. In addition, class "A" properties will continue to experience 15-20% rental growth in and around the Central 128 corridor, while rents for the class "B" product will remain flat with the exception of a few core submarkets.

Garry Holmes, SIOR is president and Craig Johnston is senior vice president, R. W. Holmes Realty Co., Inc., in Natick, Mass.