

Real Estate Journal

THE LARGEST BUSINESS PUBLICATION OF ITS KIND IN THE NATION

Suburban office market continues to pick up momentum: Leasing activity to be strong

gh Garry Holmes



R.W. Holmes Realty Co.

cj Craig Johnston



R.W. Holmes Realty Co.

The Boston suburban office market has experienced twelve 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. For 2006, the trend is a modest increase in rental rates coupled with a modest decline in vacancy. The combined availability rate for the 78.6 million s/f suburban office market now stands at 19.2%.

The Framingham/Natick area continues to be the strongest submarket with a combined availability of 9.1% while the I-495 North market continues to lag behind at 28.4%. The Central 128 corridor continues to be the "hot spot" with the availability rate declining to 15.2% (a sharp contrast to the 27% availability posted in 2003). More importantly as rents for trophy properties along Central 128 approach \$40 per s/f, rents for class B buildings have appreciated 10% this year.

The I-495/Mass Pike office market had limited success for 2005, but is starting to show signs of improvement as the availability rate declined slightly to 25.2%. Southborough and Westborough have benefited directly from the scarcity of options in Natick and Framingham as evidenced by Iron

Mountain leasing 82,000 s/f at 120 Turnpike Rd. in Southborough, Middlesex Savings Bank's 80,000 s/f acquisition of 120 Flanders Rd., and Bose's expansion into 180,000 s/f at 9 Technology Dr. in Westborough. 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: Totten Pond Office

Center in Waltham to BPG Properties for \$44.98 million; University Office Park in Waltham to NPV/Direct Invest for \$39 million; National Amusements acquisition of 846 University Ave. in Norwood for \$9.4 million; 3 Com Campus in Marlborough to an affiliate of Eaton Vance for \$135 million; 2200 West Park Drive in Westborough to Everest Partners for \$10.4 million; 144 Turnpike Rd. in Southborough to Colony Realty for \$18.1 million; 50 Speen St. in Framingham to Bulfinch Group for \$3.7M; 372 Washington St. in Wellesley to Alevizos Group for 10.3 million; and Crosby Corporate Center in Bedford to RREEF for \$70.7 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 called Reservoir Woods - a 448,000 s/f campus with three tenants presently committed to leasing 227,320 s/f. Also in Waltham, Duffy Associates is building a 142,000 s/f building on Waverly Oaks while Boston Properties will be coming out of the ground soon with 250,000 s/f on Prospect Hill (a site that can ultimately handle up to 600,000 s/f). Carruth Capital cleared 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 is building a first class 50,000 s/f office building in Southborough. Over the next 6-12 months, we expect several more de-

velopers to start focusing on new construction.

According to a recent article in the Boston Globe - "Employment in professional and business services, comprising a variety of tech firms, has grown a healthy 2% in the last year, twice the rate of overall employment growth in Mass., according to the state department of Workforce Development. Makers of technology products are bucking the trend of job losses in manufacturing and adding jobs - more than 3,000 in the last year. Massachusetts tech exports are surging; foreign sales of semiconductor manufacturing and testing equipment nearly doubled in the past year".

The Globe article supports our viewpoint, that leasing activity continues to pick up momentum. 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 has been 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 are demonstrating rental appreciation especially within the core submarkets.

Garry Holmes, SIOR is president and Craig Johnston is senior vice president of R. W. Holmes Realty Co.,