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Are strong fundamentals enough to spur speculative industrial development in southern N.H.? - by Mike Harrington

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The Southern New Hampshire industrial markets continue to experience strong fundamentals, with overall vacancy rates hovering around 5.6% and lease rates ranging from $6 to $7.80 per s/f, NNN with year over year projected rental growth rates of 2.5% to 3%. (The higher end of the range for specialty industrial flex space.) It's projected that this trend will continue as the market struggles to justify bringing new speculative industrial products into the market, thereby limiting supply despite the increase in demand.

The Southern New Hampshire industrial market is following a national trend. According to CoStar, leasing activity of industrial space in 2018 occurred at a record pace totaling one billion s/f of leasing. One driver of this activity continues to be the online model of shopping which is driving demand for warehouse distribution space, a trend predicted to be a key driver of activity into the future as consumer goods continue to be purchased in greater volume online. CoStar reports national vacancy rates of 5%, slightly below New Hampshire's vacancy, with year over year rent growth predicted to increase 5% as demand continues to outpace supply.

I was recently completing some research for a client and was reminded that the last large speculative industrial project developed in Manchester was a 225,000 s/f warehouse distribution facility at 1070 Holt Ave. built by Danais Realty Group in 2007, which was quickly preleased while the building was under construction and has been occupied ever since. I spoke to Dick Danais, Danais Realty Group, who continues to be an active owner/investor of industrial properties in this market, who confirms that demand for warehouse distribution space continues to be strong. They recently purchased a vacant 100,000 s/f former BJ Warehouse building in Hooksett, currently under agreement to a national distribution company who will lease and occupy the entire building once renovations are complete. As a side note, there were three national companies competing to lease the same space, all with 100,000 s/f requirements.

I highlight this to demonstrate that even with considerable tail winds from a strong consumer driven economy that has rebounded from the Great Recession over these past six years, coupled with corporate and personal tax incentives and historically low interest rates, market rents for new industrial projects have not yet caught up with the costs to purchase land and construction to justify speculative development in Southern New Hampshire.

At some point in the future this is predicted to turn, as demand for industrial space in Southern New Hampshire continues to increase, and as rents continue to rise as projected over the next few years. When that eventuality draws near there are several properties either currently available for purchase or on the sidelines ready for development that will be first to capture these requirements. Examples of these include: John Flatley Co. has one million s/f of industrial space ready to be built in Merrimack at the Merrimack Commerce Center. There are 34 acres of approved land located at Exit 4 off Rte. 101, Raymond known as Granite Meadows that can accommodate up to 300,000 s/f of high bay distribution space available for sale. Garrison Glen Corporate Park in Exeter has a few lots available for sale with approvals to build high bay warehouse space. And there are several lots available at the Londonderry Industrial Park adjacent to the Manchester-Boston Regional Airport available for ground lease and purchase. All of these are excellent examples of properties well positioned to absorb supply as rents increase or as user demand dictates.

In the meantime, what do you do if you're a tenant that has outgrown its current facility and the lack of expansion space is preventing your company from growing? It's recommended that you start your search well in advance of your lease expiration, thereby allowing you sufficient time to actively search the market for appropriate space. Once you've found the right building be prepared to commit to space quickly and be proactive. This includes drafting a letter of intent to lease versus requesting a proposal to lease from the landlord. This is an important technicality that sometimes does not get used or is overlooked in the negotiation process and it could mean the difference between winning or losing your space to another tenant.

A strong leasing market implies a strong subleasing market, which is good news for a tenant. Subleasing your existing space will allow you to move sooner and will minimize your lease obligation to your current landlord. Another tactic is to consider actively working with a developer who has the ability to purchase land, build a building and lease it back to you at a negotiated rate. This usually requires a long-term commitment, but it may be necessary if appropriate space is not readily available in the market.

In summary, it's predicted that there will continue to be a shortage of industrial space especially within the warehouse distribution sector, rates will continue to increase year over year and vacancy rates will continue to trend below historical averages. At some point in the future, the economics of this trend will be strong enough to trigger and support the development of new industrial space similar to what was built in 2007 at 1070 Holt Ave. The question is not "if," but "when," and that will be determined by the market.

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