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End of year outlook - Boston industrial real estate market report - by David Skinner

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Boston industrial real estate is as hot as it has ever been and there are few signs of slowing down. While we may hear conflicting reports about the health of the U.S. economy as a whole, the specific factors that contribute to the Boston market would point to at least a few more interesting years in the favor of property owners, sellers and landlords alike. Sale prices are strong, leasing rates are on the rise, and investors are taking more and more risks because the potential downside is insignificant. The absorption rates due to new user types and adaptive reuse maintain a declining supply and expanding demand. Each indicator points to healthy demand for industrial moving forward.

Sales both in total deal volume and price per square foot have risen nearly every single year in the Boston market since 2014. Last year was highest of the last six and 2019 will likely surpass all of those still. Many local Boston-based companies who have historically leased rather than purchased properties are now flush with cash and are looking to deploy those resources in stable assets, which then drives up the pricing.

Rental rates have also continued to climb, growing a steady 7% year-over-year but climbed even above 8% in the second quarter in 2019. Most of the rental rate increases have come from inside Rte.128 because of the decreased supply in that sector. What has neither been leased nor developed is seeing sharper increases than 8% because of the last-mile proximity to Boston and the rise of logistics costs. This forces delivery companies to pay more rent for the benefit of the location.

Numerous transactions have been completed below a 6% cap rate on industrial sites which is a fairly new phenomenon in Boston. Of the four major property types (multifamily, office, industrial, and retail) values of industrial have appreciated most aggressively and have outpaced the national average by over 2%. This is one of the reasons to be bullish on the Boston industrial market, namely that as values appreciate due to lack of availability, the market fundamentals point to an above-average increase in value. Many investors have made gambles on sites by purchasing

vacant sites on spec, confident that the tenants exist in the market and it is only a matter of time before they sign leases.

Pausing quickly to survey the landscape of industrial development, it is important to note that since 2010 over 20 million s/f of industrial space has been removed from the marketplace due to adaptive reuse or been taken offline for other reasons. The demand for biotech, lab, flex, and office space has also invaded historically industrial areas. This 20 million s/f deficit is being replaced by less than two million s/f of new development. Manufacturers and distributors are moving to Rte. 128, I-495, and even as far out as Worcester and Providence to find price-competitive space at their required volumes.

The I-495 beltway is home to many large construction projects that have been delivered in 2019 or are set to be delivered in 2020. Some have been leased, but many will be delivered vacant, also another sign of the prospective health of the marketplace. The 'Boroughs submarket is one that offered cost-effective land a few years ago that has since been purchased and built upon and has only grown more attractive to investors and users alike.

Everybody has an opinion on how the world economy is going to continue to rise or fall. If anybody knew the definitive answer to that question, none of us would need to work. That said, T. Boone Pickens was once quoted saying that if you study the market fundamentals of any industry, and those fundamentals tell you something other than what the rest of the world is saying, follow the fundamentals. We can easily observe the duplicitous nature of interest rates especially in a presidential election cycle, but the job growth inside Rte. 128, the burgeoning demand for e-commerce distribution space, and the sale of large industrial parcels for residential redevelopment points to a direction of positive growth for Boston for the foreseeable future. In markets like this, tenants and buyers would be remiss to be picky on available space because sellers and landlords are heavily benefiting from the trends as we see them unfolding.

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