New Hampshire's office and industrial markets, while different, will show similar trends in 2011

January 27, 2011 - Spotlights

The office and industrial real estate markets in New Hampshire are different products, but the 2011 trends for both are similar.

The New Hampshire office and industrial markets will continue to resemble a "shell game" heading into 2011, with rental rate reductions leveling off and leasing incentives lessening.

Over the past two years landlords used generous incentives such as shorter lease-terms, delivering "turnkey" space with little or no up-front tenant contributions, free rent and low lease rates to retain and attract tenants to their buildings. Toward the end of 2010, landlords seemed to push back slightly, resisting the level of lease incentives offered since fourth quarter 2008.

An uptick in activity has most landlords looking forward to easing the deal making that favored the tenant during the recent recession. A majority of the leasing activity in 2010 consisted of tenant relocations to similar or smaller leased spaces. This trend was a result of tenants benefitting from landlord incentives mentioned above, which allowed users to upgrade the quality of their space or remain in similar space at a lower overall cost.

Expect similar office leasing activityâ€"tenants moving from one location to anotherâ€"to carry forward through 2011, with some positive absorption occurring in the fourth quarter. The Manchester submarket's Class A office space is a great example of this; leases were executed but the vacancy rate has had little to no fluctuation since first quarter 2009. Similarly, New Hampshire's office vacancy rate was increased a mere .5% as of the close of 2010. A slight gain in tenant demand will be the trend in the office market statewide, as some business sectors realize a slight increase in office requirement needs for the first time in over two years.

Office leasing continues to outpace sales throughout all submarkets. New construction is rare, in New Hampshire unless it is owner-occupant driven or medical office. There is, however, an increase in the inventory through redevelopment of existing facilities. Mill renovations to Class A mill space is a good example of this.

The industrial market continues to show more activity than the office market, but not enough to register actual growth in the six New Hampshire submarkets over the last few months of 2010. This should continue in 2011. The New Hampshire industrial vacancy rate was 13.3% at the close of 2010. A majority of the activity in 2010 involved users looking for smaller amounts of spaceâ€"under 25,000 s/f. This activity has created a shortage for stand alone 10,000 to 30,000 s/f industrial/flex facilities. Several factors that contribute to this shortage are overall flat industrial growth, the aging of existing product base and historically low lease rates (making it difficult to financially justify building new product for lease).

Slow growth to flat absorption, with a couple of notable exceptions, in the industrial sector will remain a trend for the first two quarters and perhaps for all of 2011. Lease rates will likely remain low in 2011. Low rental rates, coupled with low demand, has created little impetus for new construction in the New Hampshire submarkets. However, two areas that do bear watching are the user/owner 20,000 to 30,000 s/f industrial flex market and the 50,000 s/f industrial/warehouse market. There are more buyers for the former, and tenants for the latter, than currently available product in many of the submarkets we track.

Tenants and buyers are looking for facilities with high bay space, high tech data capability and convenient access to highways, among other things. However, the current available inventory cannot meet this demand. While such supply/demand situations should trigger construction, tenants and users/owners will likely look for other alternatives. Depressed lease rates make it difficult to justify the cost of bringing new space to marketâ€”for lease or for purchase. Instead, tenants and users/buyers in 2011 will continue to "make do" by renovating existing, aging product to meet current needs. It will take a stronger, more sustained recovery to create the confidence required to bring on new construction by owners and landlords and lenders.

Meanwhile, expect the office market in New Hampshire to return to a slightly more level playing field between landlord and tenant in 2011. Rental rates will begin to level off, and may even begin to increase by fourth quarter 2011, likely making this the final opportunity for tenants to take advantage of depressed lease rates. The industrial market 2011 vacancy rates are not expected to see a significant change. Expect vacancies to remain stubborn, tracking in the same range as in 2010. Thus, the office and industrial markets, while vastly different products, will show similar trends in 2011.

Robert Rohrer, Jr. is the managing director of transaction services for Grubb & Ellis|Northern New England, Bedford, N.H.