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Institutional capital floods the market, driving up values

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Operations will remain tight in the urban core as retailers expand to premier locations in Central Boston, while stagnant building activity and an uptick in demand will allow operators to backfill under-utilized space in the suburbs. As businesses expand payrolls in the Financial District, residents will migrate toward major employment hubs and entertainment districts in surrounding areas. As a result, global and national retailers will expand or relocate from older centers in peripheral neighborhoods to newer, redeveloped infill properties in the Central Boston submarket. Prime shopping districts in Back Bay, including Newbury St., Commonwealth Ave., and Boylston St. will garner the most consideration this year as tenants lease quality, street-level store fronts with high visibility. As available space shrinks in the submarket, vacancy will drop to a metrowide best of 3.4% this year, giving owners enough leverage to raise rents to record highs. Meanwhile, muted construction and large lease signings will support positive net absorption in third-ring suburbs such as the South Bristol County and North/Merrimac River Valley submarkets, reducing vacancy an average of 100 basis points this year.

As the local economy recovers at a brisk pace, institutional capital will flood the metro as investors look for long term stability and passive income. In a flight to safety, REITs and foreign investors will acquire single-tenant properties net leased to a national chain for long-term revenue streams and capital preservation. These risk-averse buyers will take advantage of the low interest rates and expand their portfolios in premium locations inside of state Rte. 128, including Cambridge, Back Bay, and Beacon Hill where operations remain tight. As bidding intensifies, first-year returns will slightly compress in the second half, averaging in the low-7% range. In the multi-tenant arena, sales velocity will modestly pick up as local investors target strip centers with mom-and-pop tenants in Middlesex and Norfolk Counties for higher potential upside. Performing shopping centers with a strong grocery anchor will command yields in the mid- 8% range, while unanchored, in-line space will trade above 9%.

2011 ANNUAL RETAIL FORECAST

Employment: Boston will post some of the strongest employment gains in the U.S. this year as companies boost payrolls by 2%, or 49,000 new positions, the largest year-over-year increase since 2001. Last year, over 21,000 workers were added to the metro.

Construction: In 2011, 500,000 s/f will be delivered to Boston, expanding supply levels by 0.3%. In the preceding 12 months, over 1 million s/f came online.

Vacancy: As builders complete the least amount of new space on record this year, solid demand will continue to put downward pressure on vacancy rates in the second half. As a result, vacancy will contract 40 basis points in 2011 to 6.1% after retreating 70 basis points last year.

Rents: As tenant demand intensifies, owners will pad asking rents 1.3% this year to $21.35, while effective rents will jump 2.2% to $19.26 per s/f. In the prior 12 months, asking rents ebbed down

0.1%, and effective rents retreated 0.8%.