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2012 commercial real estate forecast: Cloudy with a good chance of...

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As we begin the New Year a variety of headlines have attempted to put the commercial real estate market into perspective: "Slow Growth in 2012", "Office Construction Makes a Comeback", "More Good Times Ahead for Multifamily in 2012", "Tough Times on The South Shore for Office". But regardless of the caption, what has become very clear is that it's a mixed forecast for the commercial real estate market depending on not only the property type and its class but the segment of the market. The good news is that 2011 generally appears to be a turning point year and did bring about a modestly improved overall commercial real estate market with the multifamily sector coming out a winner.

A new perception about home ownership and tight mortgage underwriting requirements drove the demand toward renting apartments, decreasing the national average vacancy rate to 5.6%, according to The National Association of Realtors. The New England markets of Boston, Hartford and Providence fared much better than the national average, at 3.9%, 3.1% and 4.5%, respectively. 2012 will continue to bring a further decline in apartment vacancies while demand and rents will continue to rise well above the average 5% rent increase seen in 2011. As this demand for apartments continues, the rental supply will become more limited and new construction will follow. This trend has begun in South Boston's Waterfront District with more than 1700 residential units proposed for construction by various developers. Strong demand has also reached further than the Boston metro area with new apartment complexes being built on the South and North Shores as well as the Metro West. As employment improves, the market will see better than average growth in supply and rental rates.

The Mass. office market, rated as one of the most improved, continued to make a comeback in 2011. Greater Boston led the recovery with rising average rents to almost \$46 per s/f, an increase of new office space construction and an average vacancy rate of 15.4% vs. the national average of 16.2%. The remainder of New England, especially the Providence market saw modest gains in occupancy. The exception was in a few submarkets which actually saw a rise in vacancy. This was mainly concentrated on the South Shore of Mass. where vacancy hit 20%.

Office rental rates in 2011 remained level for the first time in 3 years. Rental concessions were minimal in 2011 and will fade in 2012, but rents will not start rising until 2013 when it is forecasted that employment conditions will support sustainable economic growth.

In Mass., some biotechnology companies started construction of new office buildings, most notably Vertex Pharmaceuticals at Fan Pier in the expanding South Boston Waterfront area and rumored State Street Corp.'s move to the Seaport District. Overall new construction of office buildings will remain minimal and submarket specific. As jobs are continually added to the economy throughout 2012 and into 2013, companies will begin to expand, prompting office construction and increased

rents to make a comeback.

Another winner was the retail market, with Mass. at an average 10% vacancy and Greater Boston at an approximate 6.9% Vacancy far outpacing the national average of approximately 13%. The rest of New England didn't do quite as well, with the greater Providence market hovering slightly below the national average at 12.5%. With a better than forecasted December sales number, returning to 2007 levels, the retail market will continue to improve. Growth in employment, more shoppers, greater demand for space and little if any new supply will contribute to a further decline in vacancy for 2012 and in 2013 we will see a slight rise in rents.

Finally, the New England industrial market worsened in 2011 caused mainly by corporate consolidations and relocations. The Mass. average vacancy rate of 19% exceeded the national average of 12.3% and average asking lease rates slipped.

The manufacturing sector's vacancy rate at 20.8% primarily was contributed to the rise in the vacancy rate with negative absorption in 2011. The warehouse sector and flex market both had positive absorption producing a reduction in vacancy rates. Warehouse ended the year at 16.9% and the flex market was at 16.8%.

It is forecasted for 2012 that the industrial market will improve slightly and asking lease rates will stabilize, especially as manufacturing continues to expand. New England's, especially in Mass., high-tech, bio tech and pharmaceuticals production output expanded throughout 2011 and is expected to continue in that direction through 2012. Flex space vacancy will continue to improve as the tech companies begin to expand once again.

Overall the New England commercial real estate market improves in 2012 with vacancy being reduced and rental rates stabilizing and increasing. The Boston market in particular remains in the national top 10 overall best markets and according to the ULI is #5 in the top 20 markets for investment and development.

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