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Boston's brain power attracts companies looking for talent, which in turn creates high demand for real estate

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"Fracking" of natural gas and oil is helping to boost the national economy, but another kind of power - brain power - is having an even more dramatic impact on the Massachusetts economy.

With 35 colleges and universities in the Boston area, including Harvard and MIT, the city leads the country in its ability to attract companies looking for talent. It's a key reason that Massachusetts is seeing demand and pricing increase rapidly in both commercial and residential real estate, even as the real estate industry continues to flat line in most of the country.

Likewise, new construction is slow in most regions, yet Massachusetts has billions of dollars of construction under way. Cranes will be plentiful on the Boston skyline this spring and summer.

We initially noted the promise of the Seaport District, but now the commercial construction boom has spread throughout the Boston area and beyond. Existing development has benefited, too, as rents for class B commercial space in the Boston market are up about 50% this year. Moody's even noted in November that values of commercial real estate have returned to within 1% of their previous peak.

Impact of Fracking

Some other parts of the country are also booming, such as the Dakotas and Pennsylvania, because of the use of hydraulic fracturing technology, commonly called fracking, to extract natural gas and oil.

While fracking is not taking place in Massachusetts - and is unlikely to take place in the foreseeable future - the state will benefit from lower energy prices, which will make manufacturing more competitive throughout the country.

Opposition to fracking in Massachusetts is already taking place and Vermont recently became the first state to make it illegal, but it doesn't matter much, as natural resources are not an economic driver for the state. A relatively small amount of shale oil has been identified in western Massachusetts by a U.S. Geological Survey, but the amount is small compared with deposits in other parts of the country.

Overall, fracking is having such a profound effect, it is shrinking the U.S. petroleum trade deficit. The deficit today is less than half of what it was in 2008 and, with \$90 billion in projects under development for 2013, the infrastructure for oil and gas will soon be enhanced to the point where many expect the U.S. will become a net energy exporter.

Potential Impact of Taxes

Fortunately, Massachusetts can depend on its brain power instead. It is virtually unregulated and does no damage to the environment, so higher education can continue to boost the Boston economy as long as its colleges and universities remain world class.

Higher education accounts for a significant percentage of jobs and new construction in and around

the city, but the industry's most important contribution is its product - an educated workforce. Harvard University and MIT, in particular, are driving development of a thriving biotechnology industry in Cambridge, where eight projects account for \$2 billion in new investment.

With so much new construction on the books, nothing could slow down the Massachusetts economy short-term, but that doesn't mean that political forces won't try.

While spring brings optimism, this year it may also bring another tax increase, as governor Deval Patrick is seeking a \$1.9 billion tax hike, including an increase in the sales tax from 5.25% to 6.25%. That would come on top of the recent federal tax increase. The expiration of Bush-era tax cuts resulted in a payroll tax increase that takes an additional 2% of income for most Americans, while wealthy taxpayers are shouldering far higher taxes, including an income tax rate of up to 39.6%.

In addition, both parties are locked in battle over sequestration, which will be followed by a battle over the federal debt ceiling.

This lack of resolution may help advance political agendas, but it creates uncertainty, which stalls business decisions. American businesses have been sitting on trillions of dollars in cash, waiting for direction based on the perceived impact of decisions in Washington. When decisions are not made, the money remains idle. Putting that money to use would boost the economy.

Such issues aside, spring is coming and it will be a busy and productive one for Boston's real estate industry, thanks in large part to Boston's "brain power."

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