



CELEBRATING
55 YEARS

nerej

I may sound like a broken record, but the glass is still half full and not half empty!

July 23, 2008 - Spotlights

How did we get to mid year already? The first six months of 2008 have been hectic. We currently have more than a dozen lease transactions in the pipeline, but none of them are racing to the finish line. There is simply a great deal of angst, anxiety, and hesitation in the business sector. Some of this comes from first hand experience, some is the media and the press hyping doom and gloom and some is an underlying concern that things are going to get worse before they get better.

First hand experience starts with high energy and transportation costs. At home rising food costs are prominent. In the construction sector incredible increases in cement, steel, and asphalt costs, to name a few items, all attest to pending inflation pressures. In a flat global economy, inflation is a serious risk to businesses because they simply do not have enough clout to increase prices. This has not been a prominent concern over recent years because substantial improvements in productivity have helped offset increases in materials, services or labor. However, energy is a key component to everything in our 21st Century world. Oil at \$140+ per barrel is so significant that we are all going to be paying more to get to and from work and to get our jobs done at work. Incredibly, no one grasps where energy prices are going, when they may level out or if they may drop as they have several times over the past 30 years.

There are two key factors at play here. First, the tremendous increase in global demand for oil from China, India, Brazil and other developing countries. Second, oil producing countries are not acting in lock step with OPEC. Saudi Arabia is no longer the US's best friend and oil ministers are reconsidering how much elasticity there is in the global market. The theory has been that oil producing countries do not want prices to rise too high because high prices promote domestic production and alternative energy development. Yet suddenly oil is over \$140 per barrel and continues to climb. While we see this everyday in the media, it really has a delayed effect as much of our gasoline and other energy laden products are currently being produced from oil sourced and bought 1, 2, or 3 years ago. So, the real impacts are yet to come. Before actions by the US and the developed countries could in fact, influence the markets, but that is much less so today. Energy is and will continue to be a big deal. And with no clear indications of where we are headed it is a big drag on companies looking to expand, move or commit to additional lease term.

Beyond the huge increase in actual energy costs is the whole credit issue. When it costs \$50 or \$70 or \$100 to fill your gas tank, the tendency is to charge it rather than pay cash. But for homes and apartments heated with oil, credit terms are tightening and there is less ability to charge, pre buy or do level payments. For many homeowners it will be cash on the barrelhead to the tune of \$800 to \$900 per delivery!

For the service sector energy costs may not have a great deal of direct impacts. But employees are spending more of their paychecks and will be seeking pay increases to offset these rising expenses.

In addition there is stress in the financial services sector. Banks are squeezed for margins. Mortgage lenders are still under siege. Volatility of interest rates is a major concern as well. The brokerage houses are struggling with a cool market and the investment bankers are reeling from their aggressive plays in derivatives and hedge funds. So leasing activity there is on hold too. Locally, we are seeing some high tech and defense related companies expanding, but these are conservative efforts. The outcome of the presidential election could have significant impact on the defense sector. High Tech has pockets of brilliance but many of these firms are small and do not occupy large spaces. While that is the general rule, there are exceptions and there are some firms doing very nicely.

Of course manufacturing continues to shrink in the region. Again high energy costs, long transportation costs, and comparatively high labor costs make manufacturing a challenging proposition in the northeast.

So at mid year, what is the good news? Well, as of this writing the glass is still half full and not half empty. The underlying economy in southern and central New Hampshire is still bumping along. While we lament the out migration of our young college graduates, the offset is a more mature population including the soon to retire Baby Boomers and they have relatively high household net worth. So it is a curious time. If we can absorb these energy cost increases and the correction is short lived then we should regain some positive momentum. But there are so many factors that can sidetrack a quick recovery. The odds are that this correction will take longer than the last two. This is what is prompting firms to hunker down and make due with the space they have. With energy, operating costs and rising real estate taxes, occupancy costs are rising even if base rent is not. So conservatism will be the rule until some of these variables settle down and the path of the economy is more certain.

Bill Norton, CRE, FRICS, is president of Norton Asset Management, Manchester, N.H.

New England Real Estate Journal - 17 Accord Park Drive #207, Norwell MA 02061 - (781) 878-4540