



nerej

Bright spots, hiccups and trends within the 2021 commercial real estate market - by Webster Collins

January 29, 2021 - Spotlights

Webster Collins

CBRE

At CBRE's annual kick off "town hall" meeting to discuss Boston's commercial real estate market as the new year began, we were on Zoom instead of the Intercontinental Hotel ballroom, and the focus was primarily internal and Covid-19. The leader was Spencer Levy, chairman of Americas Research at CBRE. His overall prediction for 2021 is that pricing will return for "best in class assets" to 2019 levels. Best in class assets by far are life science buildings and industrial markets which finished 2020 on a high note.

This article summarizes the CBRE town hall meeting as well as the expected turnaround times as published by such sources as PwC's Q4 2020 Real Estate Investor Survey.

Basic Economies

The basic economy is sound. Goldman Sachs is projecting a 6% GDP growth rate for 2021. The key quote from the meeting is:

"The amount of pent-up demand in the consumer is much greater than you realize for two reasons:

1) Just math – savings rates in the US are at levels we haven't seen in decades. The consumer has money to spend.

2) Psychological means – the consumer wants to spend."

At the same time, there have been big hits in the market. The weak areas which will lag behind market recovery are multi-tenanted office buildings, retail and hotels. Office buildings need to be re-tenanted; retail and hotels lag the market because many are going out of business. Mention was made that in retail some tenants went out of business even before they could pay their first month's rent.

Full-service restaurant rents have fallen by 50% and are likely “never to return to pre-Covid levels.” Outdoor shopping will remain dominant over enclosed malls. Office rent softened approximately 5%-10% in suburban markets and in secondary markets 20%-30%. There were a lot of bankruptcies in 2020 with more to come.

According to PwC’s Real Estate Investor Survey’s real estate barometer, for Boston the projections are a mild recession for office in 2021 and 2022 with a recovery in 2023. For industrial, a flat market is projected in 2021 and expansion into 2022 and 2023. For the multi-family markets, PwC projects recession in 2021 and 2022 with recovery in 2023. PwC projects retail recession conditions holding through 2023.

New to the Market

Remote working is new to the market. In various office building studies pre-Covid, 90% of tenant spaces were occupied by users at any point in time. Projections are that for high-rise Boston towers, the market will remain strong at the same time, CBRE’s December 2020 office market survey showed an occupancy rate of only of 5.1%.

In the city of Boston’s 83 million s/f of office, 25%± is Class B or C space. Most of these buildings are typically old and approximately 50% of this space is occupied by small tenants. A number of buildings have leases to flex space providers -- companies who master lease space and then like WeWorks, sublease to industrial users. The financial strength of the master lease tenant will govern this market. I recently inspected an older office property with a rent roll in hand for each subtenant. Each tenant space was leased yet when inspected was totally empty and abandoned in place. The tenants had vacated and were likely in a work-from-home mode.

The key issue is that remote working is expected to become a trend and will have its own separate impact on the older property market within Boston. Over the past 50 years the Boston office market has been through five cycles. At the end of each cycle, rents, while dipping in recession, have risen to higher levels than ever previously achieved. With remote working, what is apparent is that a two-tier office market may develop: a large-tenant market with corporate uses and a completely separate small-tenant market with a different rent level. CBRE’s Downtown class B/C market asking rents for Q4 2020 were \$68.23 per s/f. I have recently seen small tenants’ lease renewals at \$43.00 per s/f and in one instance, an accepted rent at \$37.50 per s/f, 16% below what the landlord had hoped to achieve.

Conclusion

The consensus at the CBRE town hall meeting was that Boston will rebound faster than any other city in its competitive set. Change in real estate markets is continuous. Boston is what is known as a 24-hour city with the depth and capacity to carry through and in my opinion will remain one of the best places in which to invest in the United States.

Webster Collins, MAI, CRE, FRICS is an executive vice president within Valuation and Advisory Services Leadership Team of CBRE/New England, Boston.

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