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## **Market perseveres through economic & global challenges - by Pete Hayes, Matt Fair, and Steve Flachbart**

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Living with uncertainty has become a new normal. As consumers and companies begin to see a world that's not dominated by the pandemic, they continue to deal with supply shocks, high inflation, and global economic uncertainty due to war abroad. This hasn't stopped several commercial real estate sectors from thriving both nationally and locally in Rhode Island. Investors are still flush with capital and continue to pursue deals across all sectors, but especially medical, multifamily and industrial. We expect these sectors to remain strong because of their competitive advantages and significant entry barriers. Commercial real estate is traditionally a good hedge against inflation, while low interest rates have provided inexpensive borrowing options.

The availability in industrial space was limited before the pandemic, and the increased needs of e-commerce, manufacturing and distribution have further tightened market vacancy. The largest issue for industrial remains the lack of quality supply on the market for either lease or sale. This has provided the opportunity for new development projects to gain traction. North Point Development is pursuing a 500,000 s/f high-bay warehouse and distribution center in close proximity to I-95 and TF Green Airport. Another one million s/f facility has been proposed at a peat mining site located at 295 George Washington Hwy. in Smithfield. The development would be expected to create 500 new jobs in Smithfield.

Medical demand has remained strong and buildings with long-term leases in place have continued to garner significant interest, highlighted by Evergreen Medical Properties and Bain Capital's acquisition of 15 buildings in a multi-market portfolio totaling 570,000 s/f. \$120 million of that investment were allocated to buildings located in Rhode Island. Regarding new development, Providence Community Health Centers recently opened a 27,000 s/f medical facility at 31 Atwood Ave. in Olneyville. PCHC Atwood expects to see 14,000 patients annually at the new location.

As single-family home sales have continued to race higher, investor confidence in multifamily investments has been robust, with increased interest in urban living as the pandemic's impact decreases. The Foundry sold 433 luxury units at the Promenade Apartments for \$105 million. Brown University paid \$75 million for the newly constructed, 174-unit River House apartment complex on the Providence River near Point and Eddy Sts. Avalon Bay sold 50 Park Row adjacent to the Providence train station to Hines for \$75 million. The demand for urban living expands beyond the Central Business District, which is shown by the Rising Sun Mill's recent \$27 million sale for 135 loft apartments in Olneyville.

The lack of necessary housing has continued to push new multifamily developments forward, and the I-195 District land continues to produce great opportunities. Exeter Property Group is scheduled to complete its \$90 million development called Emblem 125 on Parcel 28 at the corner of Clifford and Chestnut Sts. The development will have 248 apartments and roughly 20,000 s/f of ground floor retail on 1.25 acres. Parcel 6, which is at the corner of Point St. and South Main St. in Fox Point, will be completed this August by D+P Real Estate and Truth Box, Inc. with 60 new residential units and 23,000 s/f of commercial space. New projects are also slated to start soon, highlighted by Pennrose building 130 residential units towards the end of this year on Parcel 9 in Fox Point, and the very recent selection of Urbanica beating out the competition for Parcel 2. The site will be a six-story, 135,000 s/f apartment complex featuring 194 units. It's located along the Providence River between South Water and South Main Sts. across from the new pedestrian bridge.

The weakest sector has been multi-tenant office leasing, which investors have avoided. While the asset class has had soft market performance and vacancy rates have increased, it is important to note that the bottom has not fallen out. Overall Rhode Island office availability is currently 12% compared to being under 9% at the end of 2018. Office leases typically have been long-term, multi-year deals, which has provided some stability for landlords. Even though much of the office space is being underutilized, most tenants have continued to pay their rent. Sublease space

continues to play a minor role compared to larger markets with an availability rate under 1%.

Initially during the pandemic, office leasing was completely stagnant, tenants were focused on short-term renewals in place. They didn't know how big they wanted their office to be, how many people would be working from home permanently or via flex time, or if their layouts would be changing to incorporate social distancing.

We still have not seen any specific trend dominate. Companies have closed, merged offices or downsized, which explains the increase in vacancy, but pandemic fatigue and the need to address short-term lease renewals has created an increase in market velocity. Companies that feel productivity has remained steady during the pandemic are pursuing a reduction in their footprint, due to incorporating a hybrid work environment. Layouts largely seem to remain consistent with a company's pre-pandemic culture, and there has not been a significant push going back to private offices. Rental rates and concessions which have experienced minimal change over the past couple years will be an area to watch throughout 2022, as landlords begin to compete for a more active tenant base.

In addition, there has been a flight to quality trend. While the market vacancy has increased overall, the class A Providence market has fared better, going from 8.7% at the end of 2018 to about 9.5% at the end of 2021. This is partially because of the initial long-term leases and a strong, credit tenant base, but tenants are also currently pursuing higher quality, wanting class A standards for HVAC and cleaning.

An example of the flight to quality trend is Wexford's continued investment in the Innovation District with its \$15 million redevelopment at Davol Sq. The project has garnered significant interest and had a positive absorption in 2021. The complex has been completely renovated, and it is one of the best stories in Providence. The unique property offers both office and retail opportunities and is a great example of combining the high ceiling, brick and beam loft style of Davol Sq.'s history with modern, high-end finishes.

The past 24 months have been a challenging time for everyone, and business was forced to adapt. Commercial real estate values were pushed to new heights and certain market segments have thrived. Macro-economic pressures will continue to play a significant role as businesses deal with high inflation, supply shortages, a declining pandemic and war abroad. These challenges should continue steady investor demand for medical, industrial and multi-family properties both nationally and in Rhode Island.

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