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Downtown Portland office market update - opportunities for either other office users or residential development - by Kristie Russell

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Kristie Russell

Over the past year, the downtown Portland office market has undergone noticeable changes due to the evolving dynamics of the business environment and changing work patterns. One of the most significant shifts has been the increase in the office vacancy rate, rising by 2.8% year-over-year and reaching 11.4% by the end of the first quarter of 2024.

This area has seen the vacancy rate climb over the last couple of years, some of which is due to a hybrid work schedule. This hybrid schedule has raised questions for some companies, pondering the effectiveness of employees if they aren't collaborating in person. Mainebiz released a survey in the first quarter of 2024 asking people, "Has the growth of remote work in recent years hurt the ability of your business to innovate?" The responses were almost even. 57% of the respondents chose "no," adding that either, there has been no loss of innovation or – just the opposite – that the arrangement has created a more innovative environment. If more businesses decide to use a hybrid or full work-from-home model, downtown may continue to see downsizing or closures, creating quite a few opportunities for either other office users or residential redevelopment.

Class A properties have been particularly affected by this hybrid model. Over the last year, the vacancy rate for this sector surged by 4.8%, finishing the first quarter at 14.7%. A large portion of this shift was due to Maine Street Design vacating 511 Congress St. at the beginning of this year and Emburse, an international expense management company, leaving 320 Cumberland Ave. at the beginning of the second quarter of 2023. It is worth noting that last summer, 511 Congress St. received approvals to convert the 10-story office tower into a total of 107 housing units. Until the project moves forward, the office space is still being marketed.

Another significant trend in the downtown class A sector is the growing availability of sublease space. Since the start of 2020, there has been a gradual increase in sublease availabilities, driven by companies scaling back their office space requirements as remote work and flexible schedules become more prevalent. Over the past 12 months, this trend has intensified with the number of companies downsizing their office footprints. As a result, the amount of sublease space has risen by 3.3%. This uptick in sublease availability not only contributes to the overall increase in office vacancy rates, but also adds to the competitive landscape for landlords and property owners, as they seek to attract and retain tenants in a challenging market.

On the lease rate front, downtown Portland has witnessed a general decline across all office categories. The average asking rate dropped by 3.7% ($0.87 per s/f) year-over-year, finishing the first quarter at $22.84 modified gross. The most significant drops were observed in class A and class B office spaces, with both categories experiencing rental rates dropping by more than 5%.

Interestingly, the rental rates for class A properties were impacted the most by the sublease rate rather than the direct lease rate. There was a substantial 16.7% drop in the sublease rate for class A spaces over the past year, even with more than a 3% bump in available space. A large amount of the drop was due to leases being signed at 12 Mountfort St. This space hit the market at the beginning of 2023 after Covetrus' new facility was completed. However, with the changing business environment, the company no longer needed the entire building. At the beginning of this year, more than half of the space was leased including a 23,230 s/f sublease to OnPoint Health Data and VETRO FiberMap subleasing 5,830 s/f.

The downtown Portland office market is still navigating through a period of change with rising vacancy rates, increased sublease availability, and declining rental rates across all categories. The challenges faced by class A office properties may cause landlords to adapt to these evolving trends and seize opportunities to effectively traverse the downtown office landscape. This could lead to more landlords and sublessors dropping asking rates or offering other concessions, such as free rent built into the lease or higher tenant improvement allowances. It may also lead more well-established landlords to residential conversions of their vacant office buildings. As the market continues to evolve, proactive strategies and adaptability will be key for both landlords and tenants in this dynamic environment.

Kristie Russell is a research manager | New Hampshire and Maine, with Colliers, Manchester, NH.