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Greater Springfield experiences a year of relatively strong performance

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Once again sitting down to write about Colebrook's Annual Office Survey of Greater Springfield, I am assaulted by intrusive sports analogies and dÃ©jÃ vu. Nearing the end of a decade-presidential election where a Massachusetts governor (this time two) gets national play in the media, looming state fiscal crisis, banking and financial institutions in extremis, feds looking to re-regulate, Celtics are World Champions and, as was true in so many decades of my life, the Red Sox lose a big series in Game 7.

Why then does it seem so different from 1988? To begin with no one seemed particularly upset by the Sox withdrawal after the ACLS. With the drought sated in 2004 and 2007, has a new rationality imbued the nation? Can we better appreciate great effort in the face of key injuries and real team effort (vs. the '86 roster = number of cabs philosophy)?

This is typically the time of year that two of the most respected professional organizations in commercial real estate (the Urban Land Institute and the Counselors of Real Estate) hold annual meetings to assess the state of the real estate markets and try to understand the metrics of economic influences that will affect the future of the industry. It will surprise no reader that the state of the economy was of overriding concern in both these meetings. The word "unprecedented" was in constant use describing conditions affecting real estate and the economy in general.

While the decline in equity markets have dominated the popular press (how our 401(k)s have become 200.5(k)s), the real core disruption began in 2007 and continues in the capital markets where loans happen. The size of the fixed and variable rate capital markets dwarfs the amount of equity in the world's stock markets by an exponential amount (many trillions). The sub-prime crisis has been broadly described and it has been largely perceived by the public as a housing phenomenon when in fact it has deeply lacerated the arterials of funds that drive every part of the industrial world's economies. In one memorable week in October, Interbank Overnight Loans virtually dried up. When banks are unwilling or unable to lend to one another overnight, what chance has a normal borrower who needs funds to operate his business or finance a new building. I guess we all know the answer. After we have wrung hands over how bad the metrics are, the question quickly becomes "How long until the recovery?"

The tools available to government in times of recession include 1) lowering interest rates 2) devaluing currency 3) cutting taxes 4) recapitalizing banks 5) creating stimulus expenditures to jump start spending. Clearly each of these has already been used. We will have to see what a new administration and the new cooperation of central banks bring to the fire.

Commercial real estate, particularly the office category, is both a lagging indicator and a residual of other economic activity (particularly employment). Torto Wheaton Research, one of the most highly respected sources of econometric modeling as it pertains to real estate, points to a very worrying trend of job loss, nationally. The optimistic projection of national job loss is through the projected nadir in 2010 is 1.4 million jobs, the pessimistic view climbs to 4.1 million positions victim to the recession. This result would eclipse recessions of 1974 and 1983 by significant margins. Since office and industrial vacancy track those events closely, there is ample evidence for concern. Our colleagues in Boston report rents softening in the financial district as well as most sectors and the prognosis of the market fundamentals in the face of announced consolidation and job loss in the financial sector

How do these performance trends and influences pertain to the market that most concerns us, greater Springfield? Interestingly, we have just experienced a year of fairly strong performance. Colebrook considers the total inventory of office space in greater Springfield as just over 6 million s/f of which a little over a third is Class A with about half the Class A inventory in the Springfield CBD.

We estimate total market vacancy to be 15.53% with Class A vacancy 13.36%. We believe the market as a whole absorbed some 82,000 s/f. Most of that absorption occurred in the Class A inventory, with both suburban and CBD building posting gains. Not surprisingly, in a market with relatively little in-migration most of this new demand came from internal growth and somewhat at the expense of Class B inventory. For a more complete analysis of these metrics and trends, please see our soon to be published Real Estate Analysis available from Colebrook Realty Services or through our website at www.ColebrookRealty.com.

Once again we are in the position of trying to explain the apparent divergence of the metrics of greater Springfield's office market from that of our larger and better known neighbors as well as national trends. The explanation may be as simple as a theory of smaller markets that might hold they are more isolated from metropolitan centers than those involved in traditional economic development might wish. Indeed looking into the numbers that underlie our good performance we are in what seems like a perpetual "tenant's market" in which Class A rents yield net present values that are a fraction of replacement costs. This is particularly true in the CBD, but also has been a damper on new suburban development. A look at coming events include the addition of the former Federal Courthouse building with 128,000 s/f of effective new supply to the market as well as at least one larger financial services space now empty and at end of term. The market has a way of humbling its participants. As John Maynard Keynes said "..markets can stay irrational longer that you can stay liquid...". Humility remains the watchword here, but we are always prepared for an opportunity.

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