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The central Route 495 corridor has options for tenants seeking value with office tenancy

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The central Rte. 495 corridor is a market in a state of transition. Over the past 18 months, we have seen a shift in the ownership profile of the rentable office inventory, a marked increase in average asking rents, a flight-to-quality run on Class A product, and a widening in the variety of options available to tenants in the market. Towns with historically high vacancy are seeing accelerating absorption patterns. While variation in rents by town is diminishing, asking rents on individual properties within towns are showing a widening disparity based on ownership and purchase date.

The west Rte. 495 submarket, Franklin in the south up to Bolton in the north, has long been considered a value with properties renting for 20-30% less than equivalent product in suburban submarkets geographically closer to Boston. While this competitive advantage still remains true in a relative sense, the absolute affordability of the market is changing. According to market statistics from Grubb & Ellis research, Class A asking rents in the west Rte. 495 submarket rose past the $20 per s/f gross mark in the first quarter of 2007. This market had been recording lease transactions in Class A space from the mid-to-high teens on a per s/f, gross basis for the past four years.

Rising average rents are one measure that can demonstrate the rising cost of occupancy in the area, but they do not show the whole picture. The rental appreciation in the market has largely been the result of a handful of properties and office parks raising rents, by 25-30% in some cases. During this time, the submarket has not experienced the level of increase in tenant demand equivalent to the spike in asking rents. Rather than market fundamentals driving rental appreciation, the current increases are a result of new ownership in the market and repositioning of assets.

One such example is the Marlborough Technology Park at 100-700 Nickerson Rd. This property was purchased by Normandy Real Estate Partners from Morgan Stanley as part of the Glenborough portfolio sale in 2006. Another example is the Westborough Office Park, purchased by BPG Properties in September. While an increase in demand has not yet materialized across the submarket as a whole, certain parts are seeing a spill-over of activity from the Framingham/Natick market. The town of Southborough has experienced growth as tenants seek out more options than the tight inner suburban markets can provide. Faced with an 8.2% vacancy rate in Framingham and Natick, office tenants have recently expanded their surveys to include quality space along Rte. 495. In the past 18 months, Southborough has recorded higher volumes of leasing activity with small-to-midsize tenants, resulting in nearly 100,000 s/f of positive net absorption in office tenancy. This figure represents 13% of the entire office inventory in Southborough, with the effect that vacancy has fallen 13% points to 16.1% at the end of the third quarter.

In addition to the limited availability of space in these areas, it is important to note what little vacancy remains exists primarily within the Class B office product inventory. For tenants seeking Class A office space, options in these towns becomes even more limited. The same dynamic carries through the entire west Rte. 495. Though vacancy is greater in the rest of the submarket, it is certainly true that Class A product is receiving substantially more interest from prospective tenants than Class B product.

While the preceding facts describe a market in which negotiating power is moving to landlords, there are still deals to be had for tenants in the market and many space options within the submarket remain available. Tenants will have to start rent negotiations at a higher point than two years ago, but there is room to negotiate on concessions. Landlords are currently conducting negotiations from a variety of positions, ranging from aggressive to accommodating, depending upon the asset's ownership type and tenant roster.

Tenant options in the submarket continue to expand through speculative construction projects. Capital Group Properties is developing a Class A building in Southborough at 134 Turnpike Rd. This property will have the same look and feel as the buildings at 132 and 136 Turnpike Rd. Also in development is a high-end flex property at 417 South St. in Marlborough. This building is going up spec as a LEED Silver certified building with high end energy efficiency.

Symbolic of the newfound tenant interest in the west Rte. 495 submarket, IBM recently announced a 490,000 s/f lease signing at 550 King St. in Littleton to consolidate operations in the area. This property was originally developed by Digital Equipment, and subsequently housed HP prior to IBM's arrival. Given the unique size and building requirements, the Rte. 495 belt was arguably the only place such a tenant could satisfactorily consolidate their operations. The deal does not represent a net positive absorption of 490,000 s/f since IBM will be closing up operations at other sites in the submarket, which will free up additional options for interested tenants, including 93,000 s/f in Westborough.

In conclusion, the central Rte. 495 corridor is a dynamic office submarket. Changing ownership patterns and leasing benchmarks can cause confusion to tenants seeking to place themselves in the best possible location to serve their business needs. Options still exist for tenants seeking value with office tenancy. What is required is knowledge of the current market landscape and the ability to navigate through the submarket in order to locate the best possible deal.

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