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Not a large wave of sublease space hitting the market, this is a good sign for two reasons...

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Grubb & Ellis Company, a leading real estate services and investment firm, today said that the Boston office market contracted by 1.3 million s/f of space and that overall office vacancy rates increased 60 basis points to 12.9% at the end of the first quarter of 2009, according to the company's Boston Office Market Trends report.

"Despite the Boston area's diversified corporate base and its historic role as an incubator for startup companies, we're up against the same negative economic forces as the rest of the nation," said Steve Brodsky, executive vice president and managing director of Grubb & Ellis, Boston. "Companies are looking at their real estate obligations as they seek to reduce their overhead costs, so landlords are feeling pressure to lower asking rates and increase concessions. For tenants in a position to renegotiate, move or grow, it's a great time to find excellent space at attractive rates."

According to the report, the 1.3 million s/f of negative absorption is a distinct break from 2008, which saw an average positive absorption of 678,000 s/f per quarter. The market contraction and freeze in the national credit markets have posed problems for planned construction throughout the Boston metropolitan region as many new projects were put on hold due to difficulty in securing financing.

Also of note is the slowdown in the office investment market, which saw transactions totaling just $76.1 million in total consideration in the first quarter of 2009 after the market posted $172 million in the fourth quarter of 2008. Both represent a significant drop off from 2007, when investment sales totaled $1.2 billion in the fourth quarter alone. In fact, just three transactions of $5 million or greater in value closed during the first quarter of 2009.

The national recession is causing tenants to look at real estate as a way to cut operational costs, resulting in the execution of short-term leases, downsizing renewals and shopping the market for less expensive space, pushing down asking rents and forcing landlords to become more competitive. Class A asking rents in the CBD fell to $60.68 per s/f and $28.65 in the suburbs, dropping from $64.83 and $29.46, respectively, from the fourth quarter of 2008.

Although the volume of sublease space continues to rise, the report concluded there is a silver lining - unlike past recessions, there has not been a large wave of sublease space hitting the market all at once. Less than 300,000 s/f of the CBD's 1.4 million s/f of available sublease space was added in the first quarter, while the suburbs stayed flat from the prior quarter with 3.5 million s/f. According to Grubb & Ellis researchers, this is a good sign for two reasons: first, it means that companies have not over-committed to space, and second, it shows that Boston is still maintaining a competitive market in terms of availability.

One troubling sign of tough economic times has been the Cambridge market, which in the past has played host to numerous biotech and startup technology firms. As many of the smaller companies closed down operations that could not withstand the recession, the lab market lost 84,000 s/f of space, sending vacancy up to 15.2% from 2008's average of 12.7%.

Overall, the Boston office market will continue to contract in the coming quarters as tenants consolidate and startup companies falter when they see less support than they have in the past. As a result, vacancy is expected to rise, and there will be pressure on landlords to further reduce rental rates and increase incentives, creating excellent opportunities for tenants. On the investment side, Grubb & Ellis researchers expect to see some over-leveraged towers go back to the lender, providing ample choices for opportunistic investors looking for deals.

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