

BANKER & TRADESMAN

THE REAL ESTATE, BANKING AND COMMERCIAL WEEKLY FOR MASSACHUSETTS

A PUBLICATION OF THE WARREN GROUP

FOCUS ON MID-YEAR ROUNDUP

Commercial Real Estate Monthly

JUNE 30, 2003

Banker & Tradesman Special Section

SECTION B

B8

Banker & Tradesman • Commercial Real Estate

JUNE 30, 2003

► BOSTON RATES

Within Stone's Throw of City Waterfront Market Mix Valued

By Lisa DonFrancesco



The basic theory of supply and demand continues to impose its rule over the Downtown Boston office space market. Simply put, there continues to be far fewer tenants willing and able to lease office space than the amount of space available.

As a result, tenants are often able to negotiate rental rates that are 10 to 15 percent below asking rates, and are frequently able to combine this with very favorable inducement and concession packages. The bottom line is that tenants have maximum leverage in virtually every lease negotiation, including lease renewals with their current landlord.

The market is skewed in favor of tenants because of several combined market factors that are now nearly approaching three-year trends. The unsettling local economy, high unemployment rate, and numerous companies restructuring and cutting jobs have contributed to total vacancy rates that continue to climb.

LISA DONFRANCESCO is a vice president at the Codman Co., a real estate services company based in Boston.

Total availability in the Boston market, not including shadow or excess space that is not being marketed for sublease, is beyond 17 percent.

Office rental rates are decreasing, although at a slower pace than previous years. And new construction and newly renovated buildings continue to add to the over-supply of space. Demand remains sluggish and the outlook for negative net leasing absorption is expected to continue through year-end 2004.

Tenants have reacted by looking to restructure existing leases and by entering the market for new space much earlier than in previous years. Nevertheless, in anticipation of further market reaction, many leasing decisions are being delayed.

However, there are pockets of opportunities and signs of optimism for landlords. Once known as the Fort Point Channel and Seaport District office markets, the newly combined area has been renamed The South Boston Waterfront District. The district, which includes office space primarily between Summer and Congress streets and stretches from the Fort Point Channel to The World Trade Center, has a total supply of approximately 3.7 million square feet. It is comprised of 2.7 million square feet of new construction and rehabbed space and 1 million square feet of non-rehabbed space.

While statistics such as its vacancy rate – the district's rate is currently approaching 14 percent – suggest that it is experi-

Continued on Next Page



303 Congress Street, Boston



22 Boston Wharf Road, Boston

Within Stone's Throw of City Waterfront Market Mix Valued

Continued from Previous Page
encing similar challenges as its neighboring downtown districts, a closer look reveals some surprising details. The rehabbed space market and the non-rehabbed space market are performing very differently from one another.

The non-rehabbed, under \$20 per-square-foot space, is beating to a different drummer. This market segment is showing little signs of the local economy's stagnant growth and lack of demand for space. In fact, the transaction volume in this segment has been up and relatively active over the past year.

Who are the tenants that tour the space and look to make their best deal? Much like any office market, tenants tend to come from nearby and similar class buildings, and with this segment of the market, tenants are mainly entrepreneurial in nature. More importantly, leases are also being transacted in number with tenants who are looking for value and identity. With its newly and soon-to-be complete developments, including the convention

center, Massachusetts Turnpike Extension, Fan Pier and improved subway and water transportation to the area, the value of an under \$20 per-square-foot rental rate is thought to be greater than other similarly priced space opportunities in other downtown districts.

Also, like the downtown market, the South Boston Waterfront District is headed

towards becoming a 24/7 neighborhood. With all that has come to the area and all that is slated for development, rental rates have held over previous years. The market segment's vacancy rate, while it hit a low during the dot-com era, is currently in the low single digits.

Also, this property type has built-in natural insulators that keep it healthy, such as its limited supply of non-rehabbed space – none, of course, is being developed. In fact, Boston Wharf Co.'s sale of its A Street buildings to Beacon Capital in 2000 removed approximately 800,000 square feet of space of its under \$20 per-square-foot market. The buildings are currently being redeveloped and the mixed-use complex will include components of artist lofts, movie cinema and retail.

This under \$20 per-square-foot market segment compares and contrasts with some of its neighboring buildings – the second segment of the South Boston Waterfront District office market. The second segment, specifically the \$25-plus per-square-foot market comprised of new construction and rehabbed office space, is performing similar to the districts that it competes with – South Station, North Station and the Financial District.

Two newly constructed mid-rise buildings in the South Boston Waterfront District, namely 22 Boston Wharf Road and 303 Congress St., are feeling the effects of the tenant market. Activity in this segment of the market is slow, which

is partly explained by its physical distance outside the central business district and its comparative shortage of area amenities.

Boston Wharf Co. is the district's largest commercial landlord and owns approximately 2 million square feet of renovated and newly constructed space. The company has curtailed any additional plans for new construction or redevelopment beyond its 300 A St. project, which is scheduled to be delivered this summer, until the face of the market changes.

Thomson Financial, Boston Wharf Co.'s largest tenant, began placing space on the market for sublease about one year ago. Thompson Financial continues to market over 50,000 square feet of sublease space. Another significant indicator of this market segment is the World Trade Center Complex, which is comprised of approximately 1 million square feet of existing office space in its East and West towers. There is approximately 170,000 square feet of office space currently available. The third office tower in the complex, World Trade Center South, is slated for completion in 2006. When complete, the tower will drop another 420,000 square feet of office space into the South Boston Waterfront District office space market.

Despite the many new developments and renovations that are coming to the area, conditions suggest that the \$25-plus per-square-foot market segment in the South Boston Waterfront District office space market may be in second position to recover, after the Financial District. ■