



Tom Palmer's Journal

Tom Palmer, a former reporter and editor for The Boston Globe, contributes a news journal to McDermottVentures.com about development-related events in Boston and the region. The journal appears frequently. Tom is an independent communications consultant.

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Just as the Boston area's real estate picture was beginning to turn around, the global recession hit, and the office market in the suburbs is being hit hard. Even in prime areas, like the Central 128/MassPike submarket, a vacancy rate of 7.6 percent in the first quarter of 2006 has leapt to 17.2 percent in the quarter just completed. Even the tenants looking are seeking less space, and, "This has put quite a squeeze on the landlords," said Adam Meixner of Boston Realty Advisors. ... *Also a ribbon-cutting at the Richard E. Griffin Academic Center on Huntington Avenue, Rating the Raters, MassDevelopment Brownfields, Nonantum Road, and WriteBoston ...*

Boston Realty Advisors, a leasing and investment sales company, presented a market briefing today for a few dozen area business people at the Wellesley Country club. It's the first of several the company plans, perhaps a couple a year.

The market in the nine communities at the intersection of those two highways consists of 842 A, B, and C quality buildings, with a total of about 34 million square feet. That's a substantial portion of the entire suburban office market of Boston, and a little over half of the size of the downtown market.

The first quarter of the year is usually the slowest -- "Being in 20-degree weather just ain't that fun," said Meixner -- but 17-percent-plus is serious. There's about 5.8 million square feet of space on the market.

The absorption rate is negative 502,696, the firm's figures show -- compared to a small but at least positive absorption for 2006 of 47,575 square feet.

Activity is of course off too. First-quarter transactions in 2006 numbered 110 and averaged 7,500 square feet. This quarter: 82, averaging 3,305.

Rents for A buildings were \$35-\$44 a square foot only a year ago; now they're \$24-\$32. B and C buildings' rents have taken a hit too, but, "The buildings that have been hit the hardest are really the Class A," said Meixner. "Class C has really been affected the least," in part because rents were already low.

Boston Realty Advisors' advice if your lease expires within 12 months is to study the market carefully and compare before you sign.

It's important to focus on rents and tenant improvements or concessions, obviously, but don't forget to look at base-year taxes and operating expenses, Meixner said. Tenants are often responsible for increases in those costs, so be aware which year is the base. Meixner is associate director for commercial brokerage at BRA.

About half of landlords will offer extensions at a locked-in rate, the other half at "market rate" if the extension is exercised, he said. Boston Realty Advisors usually offers 95 percent of market, in consideration of the security that an extension brings the landlord.

Most leases are 3-5 years, but medical leases are typically 10 to 15.

If you have more than a year to go on your lease and need to expand, it may be profitable to do it within the landlord's portfolio rather than moving. If your business is steady, look to "blend and extend," at a lower rent rate. If your business needs relief, try to work out a sublease or other arrangement with the landlord.

Boston Realty Advisors said don't go the way Sleepy's reportedly did recently -- just sending out letters saying it was unilaterally lowering the rent called for in its contracts. "A lot of these landlords are going to be going after them legally."

If you sublease space, "You're going to take a big hit," Meixner said. Say you're paying \$20; you'll probably get \$11 or \$12. And make sure your lease says you can sublease -- sometimes the landlord gets to fill direct space first, if he or she has any.

The outlook? "This will continue to be a tenant-driven market for the next two years," Meixner said. Rents will decline for

the next 12 months, he predicted. There will be no increase for 24. "At best they'll just level off."

With rents at 66 percent of what they were a year ago, "It's just unheard of for a market to turn around as quickly as this has.

Jeremy Freid of Boston Realty Advisors talked about the sales market, which reflects the leasing market. In the last seven months of 2006 there were 63 transactions in this submarket; in the last six months, there have been 20 of any size at all.

"There's a huge valuation problem," said Freid. "Buyers are on the sidelines. Sales are frozen because of the bid-to-ask spread."

You can't look at CAP rates, because there may be no significant income growth. You can't look at comparable sales, because there haven't been any in most cases. Replacement cost "is probably the only really accurate way to figure out what a property is worth in this economy."

When things shake loose, though, there will be opportunities. The FDIC's PPIP, public-private partnership purchase arrangement is one. Buying distressed properties for pennies on the dollar, or investing in vulture funds, is another. Some talks on Moody Street properties in Waltham are a recent bright spot, Freid said. "We're getting there. We're on a path."

The third panelist today was Peter Covo, who practices law in the Law Offices of Peter Covo in Wellesley. Usually, landlords "stick to the four corners of their lease," he said, and some still will. But more will be flexible these days, rather than risk empty space.

Covo advised putting flexibility into any lease you sign, and looking ahead with contingencies specifically written in -- not just a "we'll work it out" oral agreement. "Always think of what-if scenarios for your business."

"Be accurate and specific," he said. "Get these terms in there. What happens in terms of default?" (Require two notices from the landlord and the ability to catch up, or "cure," if you're late; don't find yourself out of your lease because you missed a payment.)

Tenants can be responsible for injuries and liability that happen in properties even if the conditions were pre-existing, so, again, Covo said, watch the language. And some of the properties are going to have problems, too. "At 12 bucks a foot, don't expect International Place." He said he never advises using a standard lease.

Covo said make sure you have the right to look at the audit of expenses kept by the landlord, and ask for it annually even if you don't plan to study it, so you'll know where you stand. "Landlords hate it," but it can pay off.

"There's no standard way to calculate expenses," he said.

Finally, he said, "If you're a significant tenant, always consider the option to buy. The landlord may be in trouble."



Adam Meixner of Boston Realty Advisors

Room With a View

It was 10 years ago when the Massachusetts College of Pharmacy and Health Sciences bought a gas station on a little, 7,500-square-foot, wedge-shaped piece of land at 670 Huntington Ave.

Today college officials joined Mayor Tom Menino and other pols and cut a ribbon on the six-story Richard E. Griffin Academic Center, a \$35 million academic building where students can study and enjoy views of downtown (and even the tops of the Harbor Islands) from the top floor.

There are 50,000 square feet of interactive classrooms, faculty and staff offices, simulation labs, a technology center, and a 250-seat auditorium.

Designed by Perkins + Will and built by Bond, with interiors by Kris Stoller Interior Design, the handsome new building with the sharp edge facing downtown was named after 1971 grad and pharmacist Richard Griffin, whose father also was in the business.

Menino noted the college is Boston's oldest institution of higher education, at 185 years, and said it has graduated more pharmacists than any other school in the world.

College president Charles F. Monahan Jr., credited as the visionary responsible for this and other expansions, said, "Welcome to Mission Hill. I'm part of the neighborhood." When the college bought this land, it also bought two row houses at 700 Huntington Ave. and turned them into the president's residence.

"This is a partnership between a college and a neighborhood," Monahan said. The neighborhood had its say, though, and the building is not as tall as it might have been.

"This new academic center gives the college the ability to expand," said Griffin.



New Richard E. Griffin Academic Center



President Monahan and Connie Kastelnik of CK Communication

Rating the Raters

"A large part of the credit crisis happening in the United States is driven by the credit-rating crisis," said Effi Benmelech, assistant professor of economics at Harvard University. "In summary, they have failed in rating or grading complex assets."

Benmelech, who formerly worked for the Israeli ministry of finance, spoke recently to a group gathered at Harvard by the Rappaport Institute for Greater Boston and the Taubman Center for State and Local Government.

Ratings to the complex instruments that are at the heart of our current financial troubles are assigned by Standard & Poors, Moody's, and Fitch. "Many investors relied heavily on their ratings," Benmelech said.

Funds of loans and debt known as "collateralized loan obligations" or "collateralized debt obligations" -- CLOs and CDOs - were gathered into so-called special purpose vehicles, managed and rated before being sold in portfolios.

"Assets of varying quality were combined, some of them with junk credit ratings, and used as collateral for tranches of varying quality typically From AAA through BBB-BB," he said.

With AAA-rated ones, the risk of default in the next year was considered almost nonexistent. Not so with the other pieces.

Moody's, around since 1909, and Fitch are the younger of the rating agencies. Standard & Poors has been doing business in some form since the 1860s. "We can trust it -- that was the notion," said Benmelech.

The notable past failure for the agencies was with East Asian banks, when they were criticized for lagging behind the market.

This time the rating agencies more or less had guidebooks for creating the securities that are in trouble, he said. They said, "Here's how you do it."

"There's no one particular agency we can blame more than another," he said.

Benmelech studied upgrades and downgrades of the dominant structured finance products on the market since the early 1980s: CDOs, CLOs, residential mortgage-backed securities. While the world, or most of it, still thought everything was as secure as it had ever been, in fact the number of downgrades was growing fast. (He plotted upgrades of one ratings notch, downgrades of two.)

A year ago there had been about 10,000 downgrades of the ratings of these products. Today there have been about 40,000, or 25-30 percent of all those issued. Most of the products are issued by US financial institutions, but they're sold around the world. Some are not registered in the United States. From 10 to 15 percent are not issued in US dollars.

"Is this normal?" Benmelech wanted to know, of the number of downgrades. They had increased in the 2002-03 recession too.

So he looked at the ratings of normal securities, the downgrading and upgrading of corporate bonds, for comparison.

Downgrades did increase in the 2000-02 period, to about 5,000. But they increased very little in the 2007-08 period, where those other products were looking shakier (to those who followed the ratings closely).

"Since 2006, there have been many more downgrades, not just one notch but as many as six," he said. "Like going from [ratings of] the US to Slovenia."

The most downgraded products lately were CDOs and RMBS instruments. Those are home-equity loans and securitizations ultimately backed by mortgages. The collateral for a CDO is a pool of RMBS's, he said.

"These are very complex. It's almost impossible to find them," he said, which is making the process of unwinding the instruments, putting a value (lack of value?) on them, and marketing them so difficult. "Eventually you want to know, 'Where is my mortgage?'"

One recent index showed the price of an A tranche of debt at 22 cents on the dollar.

New numbers were due soon, Benmelech said, but in early February crisis-related writedowns of loans totaled about \$520 billion, broken down like this: Insurers and asset managers \$116 billion, North American Banks \$209 billion, European banks \$171 billion, Asian and other banks \$23 billion.

CDOs represented \$2 billion, or about half of that total.

Relevant issues for future consideration or reform, Benmelech said, include the fee issue (possible conflict of interest, because ratings agencies are paid by the companies whose products they rate), high barriers to entry for anyone seeking to compete in the ratings industry, separating the actual business of ratings analysis from the marketing and promotion of ratings companies, structure of fees charged (up front vs. the life of the transaction), the role of ratings agencies as architects of these complex products, and finally, as he put it, "the use of black boxes."

Ratings agencies claim transparency, but he was skeptical. "This is alchemy," he said.

"The products are so complicated that probably even people at Moody's and Standard & Poors didn't understand it."

Though the next crisis will probably come in some other, unforeseen financial area, he said one lesson is, "We shouldn't trust black boxes very much."

We missed another recent talk, also sponsored by the Rappaport institute, which was held along with the release of a new policy brief called, "Silver Bullet or Trojan Horse? The Effects of Inclusionary Zoning on Local Housing Markets in Greater Boston," based on work that Jenny Schuetz, Rachel Meltzer, and Vicki Been, have done at NYU's Furman Center for Real Estate and Urban Policy.

One major finding: "While zoning codes in more than half of Greater Boston's cities and towns include some form of inclusionary zoning (IZ), these provisions appear to have produced relatively few units of affordable housing and may have put some upward pressure on housing prices in communities that have adopted them. In contrast, more stringent and widespread IZ provisions in the San Francisco Bay area and counties surrounding Washington, D.C., appear to have been more effective in producing affordable housing. However, due to limitations in the data, we cannot directly compare how IZ provisions have impacted permitting and prices in those two regions."

Thank's to the institute's David Luberoff for passing along that summary, and for all the good recent panels and seminars.

Brownfields

MassDevelopment has announced that four municipally owned properties have been selected for low-cost loans of up to \$2 million under its Brownfields Priority Project Program, known as "P-cubed."

They're located in Boston, Chelmsford, New Bedford and Springfield.

According to a press release, the program was created in August 2006 and designates high-impact parcels to attract developer interest in reuse that would be viable but for environmental contamination. The selected communities are eligible for up to \$2 million in low-cost, flexible brownfields remediation funding, \$1.5 million more than the \$500,000 available under standard program rules.

"The priority project designation is intended to support communities as they remediate and reposition properties to attract investment from private developers," Bob Culver, president and chief executive, said in the release. "The redevelopment of these high impact sites can lead to the revitalization of entire districts, and new economic opportunities across the region. I hope that those not chosen for priority status come back to us to learn about other financing options available through the Brownfields Redevelopment Fund."

The locations include the Modern Electroplating site in Dudley Square in Boston, the Silicon Transistor Corp. site in Chelmsford, the Dartmouth Finishing Co. site in the South End of New Bedford, and the Indian Motorcycle site and other land in Springfield.

Slowing the Speedway

Stimulus money coming at a serendipitous time may allow for long-awaited improvements on narrow, always exciting Nonantum Road, reports our friend and public citizen John McQueen, who attended a recent Department of Conservation and Recreation meeting on an evening when we were double-booked. Thanks to John for this report:

Courtesy of the Federal Economic Stimulus Package, major rehabilitation and improvements seem finally to be on the way to help make the historic but famously treacherous Nonantum Road safer for vehicular and non-motorized transportation as well as to make its surrounding Charles River Basin parkland area more scenic and environmentally friendly.

For years, the unforgiving recipe of this extremely narrow four-lane, severely potholed, nearly-blind entry, no-shoulder parkway...that each day is an unrestrained "speedway" for lane-weaving drivers has made the mere 8700-foot stretch of Nonantum Road one of The Commonwealth's deadliest, registering four fatal auto accidents within only the past three years.

The good news about the improvement project was announced and the new designs were discussed at a public meeting that was sponsored by the DCR, currently the state's steward for parkland-abutting roadways and bridges...on March 12 at the spiffy new Community Rowing Inc. facility.

The meeting was well-attended with a productive and largely positive atmosphere. DCR Director of Public Outreach Anne Fiesinger coordinated attendees, who were a mix of concerned residents, advocacy groups, and elected officials, including Rep. J. Hecht; Rep. K. Honan; Rep. P. Koutoujian; Boston Councilor M. Ciomo; Watertown Councilors M. Devaney, V. Piccirilli, M. Sederis; Newton Aldermen A. Ciccone and S. Lennon, plus staff members of Sen. Tolman and Congressman Markey.

DCR Deputy Commissioner Jack Murray opened the meeting by announcing that the \$6 million award from the "shovel ready" stimulus funds will cover the project cost and will allow the long-planned but continually underfunded project to proceed, putting it on a fast track with a use-it-or-lose-it contract award date of July 2. Murray and DCR Project Manager Rick Corsi recapped the history and existing conditions on Nonantum Road and the geographic scope of the project (i.e., from Galen Street intersection to the North Beacon Street intersection) for which Fay, Spofford & Thorndike will be the managing engineers.

Nonantum Road was built in three segments from 1919 to 1935, an era of planning that predated the mixed urban transportation uses, safety and watershed considerations that are now 21st century priorities. Now, Nonantum Road serves as a comprehensive example of unsafe, obsolete design and of unattractive physical disintegration from neglect (broken travel lane pavement, curbs, retention walls, etc.). Despite being a prime route for pedestrians and bicycles, both commuter and recreational, these uses have no roadway space, scarce crosswalks, and are constrained within existing often-buckled, shared sidewalk path of only five to seven feet, with scant separation from the road's fast-moving traffic.

Fortunately, the dangerous inadequacies of Nonantum Road had already begun to be identified in a collaborative citizen-government process and addressed in the DCR Charles River Master Plan of April 2002 and the agency-commissioned June 2006 FST Traffic Study. The design presented in the March 12 meeting reflected refinements to the near-final reconfiguration plan that came out of the public meeting held last year on June 18.

Until the federal stimulus funds were awarded due to the sustained pleas from elected officials, the project (which made sense and was essentially ready-to-go since June) seemed destined to languish undone indefinitely due to tight state and federal budgets.

William Reed and John Michalak, project managers from FST, presented schematics of the new plan for Nonantum Road that constitutes a re-invention of the entire passageway; plus, they indicated that the prescribed DCR measures for minimizing noise and construction impact will be carefully followed (as they have succeeded in the Storrow Drive Tunnel/Longfellow Bridge repairs).

Catch basins and drainage will be reconstructed to protect river water quality and reduce roadway puddling. All surfaces will be rebuilt and repaved, not patched. To more appropriately control the flow of all traffic in this constrained footprint, the west-looking configuration will now be:

Three-foot shoulder, 11-foot travel lane, four-foot median, 11-foot travel lane, three-foot shoulder, guardrail, landscaped buffer, 10-foot shared-use lane. There will be new lights, and bikes as well as pedestrians will be accommodated.

Entry points to Nonantum Road will remove sight-blocking angles and become straight-facing. Left turns on to Maple Street and Water Street will be removed. To enhance pedestrian/bike access to the riverside, all crosswalks will be ADA-compliant, crosswalks will be added at Charlesbank, Maple and Water streets, and the pathway will be widened and protected.

The net effect of the almost counterintuitive change to two lanes from four lanes is to yield slower traffic yet a more consistent traffic flow that will be safer, more visible for motorists and non-motorists alike. Plus, the design is intended to not add congestion above current levels (now mostly a function of commuter-hour backups at the road's end point intersections of Galen Street in West and North Beacon Street in East).

Overall, comments on the new design and process were additive, constructive, often complimentary, and almost universally favorable. A number of commuter residents voiced some "show-me" skepticism about whether congestion will be same or less with fewer lanes, especially for those entering off Charlesbank. A representative from the Nonantum Yacht Club decried the current lack of speed enforcement along the road and indicated that sand used as winter weather measures ends up in the Charles River and reduces depths.

Also, it was suggested that left turns onto westbound Nonantum Road from Charlesbank and Maple should be removed from the designs, and that consideration be given to adding a traffic signal at the Charlesbank intersection. Additionally, there were suggestions that DCR find a way to expand the area of its project to include the entire North Beacon intersection so as to improve the dangerous crosswalk/curb/signal situation from right turning westbound cars.

Prior to advertising for construction bids in June '09, DCR and FST will hold another public meeting to in May, with the date to be announced later. At that meeting, the final design will be presented, and will address recent questions, suggestions, and concerns. Actual construction will begin in August 2009 and will continue for 18-24 months.

WriteBoston

Thursday evening, April 2, from 5:30 to 8 p.m., at the incomparable Boston Athenaeum, 10 1/2 Beacon St., there will be a fundraiser for WriteBoston, a new program focused on improving writing skills for students in the Boston public high schools.

Mayor Tom Menino will run the show, and tickets are available at \$250. For information on sponsorship opportunities, contact Betty Southwick at 617-541-2604, or see www.WriteBoston.org.

Prominent writers including The Boston Globe's Peter Canellos, Dennis Lehane, and Alice Hoffman will be present.