

# METRO BOSTON R&D MARKET

## Second Quarter 2001 Report

### Asking Rents Firm Amidst Tech Slump

Buoyed by demand from office space users as a cost-effective alternative, asking net rents for R&D space are remaining firm in most submarkets of Metropolitan Boston. This situation attests to the increased diversity of the metropolitan economy. In spite of a staggering reversal of fortune by telecom firms and a general slump in the high tech sector, demand remains active for R&D facilities.

Biotechnology firms are presently leading the way, as their drive to capitalize on the region's scientific brain trust is prompting the construction of additional lab/R&D facilities throughout eastern Massachusetts. From Cambridge to Worcester, from Andover to Norwell, new biotech facilities are underway. While the market for IPOs and secondary offerings may not be strong, biotech firms are having little difficulty attracting venture capital or the interest of deep-pocket, global pharmaceutical corporations, many with their own biotech divisions.



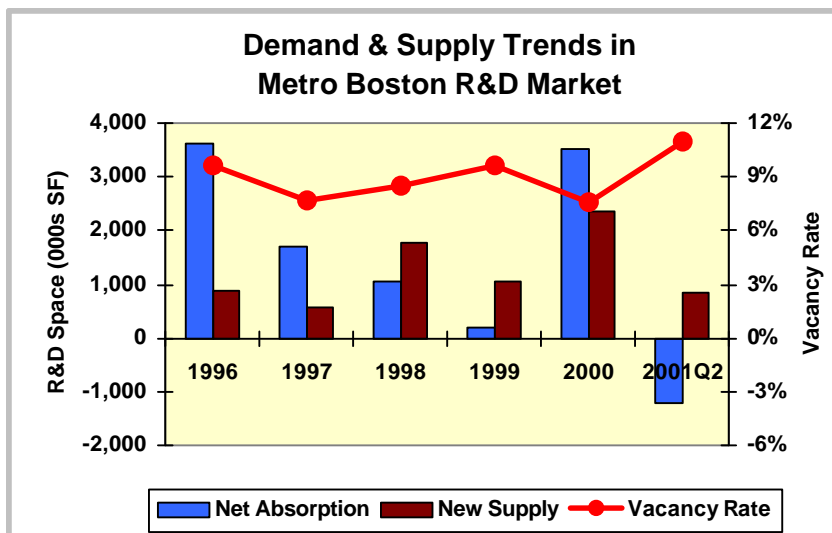
*Applied Materials is rumored to be the most likely occupant of the former Osram Sylvania facility at 75 Sylvan St. in Danvers following its conversion to high-tech R&D space by Gilbane/College St.*

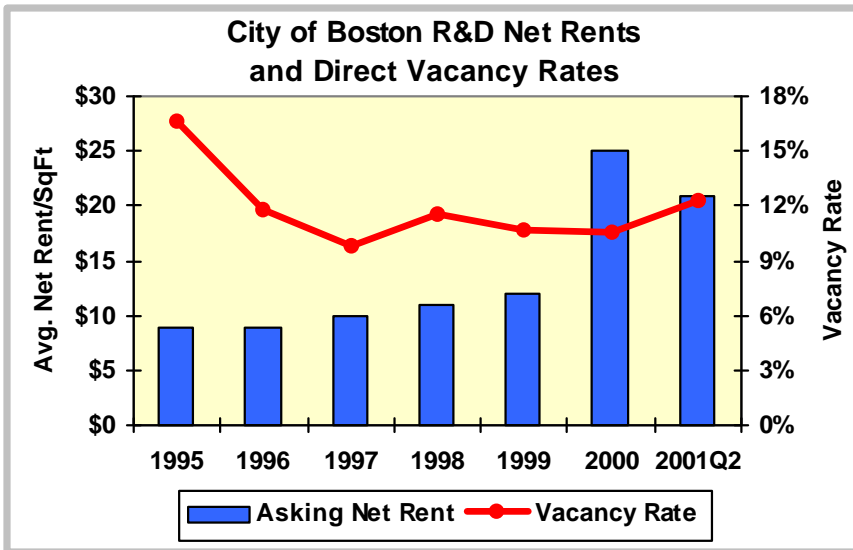
While end-user demand for semiconductor chips may have plummeted (temporarily), the demand for new technologies has not. In the Route 128 North R&D submarket, Applied Materials may be soon moving local operations into a new facility, perhaps at 75 Sylvan Street in Danvers.

The close proximity of major competitors Varian and Axcelis reinforces the perception that the talent pool in this field has a sizeable concentration on Boston's North Shore.

Not to be overlooked is demand for R&D space from emerging growth high-tech companies. Firms with new technologies under development (in contrast to a dot-com enterprise with a new business model) are receiving venture capital and funding from strategic partners. Many of these firms are located close to the homes of founders along the Route 128 Corridor or near affordable housing for recent college grads, typically along the Interstate 495 Loop.

Investor demand for R&D space remains selective, with sale/leaseback transactions involving credit-rated tenants being the most popular. Owner-occupant demand has also driven prices higher in recent years.





## Boston R&D Adjusts to Life After Telecom

It was great while it lasted. The rise and fall of the telecom hotel sector illustrates the opportunities and pitfalls associated with accommodating explosive space demand by firms in an emerging growth industry. High market rents were an attractive lure motivating developers to seize upon opportunities to redevelop functionally obsolete industrial buildings near fiber optic corridors.

No sooner than some of these projects had broken ground, however, the telecom sector faced a crippling capital crunch as investors fled from a perceived tidal wave of oversupply. The world's migration to cyberspace was not happening as quickly as had been forecast by Wall Street. Overcapacity meant inevitable price slashing. Preleased space was suddenly available again, with few takers in sight.

As a consequence, asking rents for R&D space in the City of Boston are down 15% to 20% from peak levels in 2000. That's good news to space

users which were shocked last year when asking rents doubled. Rents are still well above 1999 levels and reflect the continuing strong demand for office/R&D space in Boston.

Cabot, Cabot & Forbes is pursuing a variety of R&D space users for its redevelopment of the former Casey & Hayes warehouse in Boston's Brighton neighborhood. Originally

intended to be a giant telecom hotel adjacent to the fiber optic corridor running along the Mass Pike, the developer is now capitalizing on the site's proximity to a future campus envisioned by Harvard University.

Across town, biotechnology firms are also being courted by Boston University as its BioSquare campus is gradually expanded. Adjacent to Boston Medical Center and to Interstate 93, this location represents a farsighted vision to redevelop a former industrial and warehouse district into a vibrant source of high-tech employment.

On a smaller scale, individual properties in industrial/R&D districts adjacent to downtown Boston continue to be gradually upgraded to more of an office use. This trend has played a major role in the upward movement of R&D rents in recent years. It is also a trend that is likely to continue as what constitutes R&D work today is often best accomplished in space that combines first-class office space with state-of-the-art lab facilities.



*Following the cancellation last December of a 15-year lease agreement with Globix Corp. for a telecom hotel at 176 Lincoln St. in Brighton, developer Cabot, Cabot & Forbes is now seeking biotech firms.*

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# Cambridge Counts on Life Sciences to Keep Growing

As discussed in NAI Hunneman's mid-year report on the biotechnology industry, Cambridge continues to be a sizzling hot location for biotechnology companies. University Park at M.I.T. is a beehive of research activity and new construction. Lab space requirements are changing so swiftly these days that companies are finding it essential to frequently upgrade their laboratory facilities. Failure to do so is expensive as world-class scientists and researchers are in high demand by nearby competitors.

The robust growth of (Wyeth) Genetics Institute, Inc. demonstrates that not all demand is driven by biotech share prices. Genetics Institute is a subsidiary of American Home Products Corporation, the financially strong pharmaceuticals and consumer health care products company (e.g., Centrum, Advil, Chap Stick) with annual sales near \$13 billion. In addition to the recent addition of 200,000 SF of state-of-the-art office/R&D space at its Cambridgepark Drive enclave, Genetics Institute also



**Genetics Institute, Inc. continues to expand its West Cambridge "campus" near Alewife Station with the completion of a 200,000 SF mid-rise office/lab/research facility at 200 Cambridgepark Drive.**

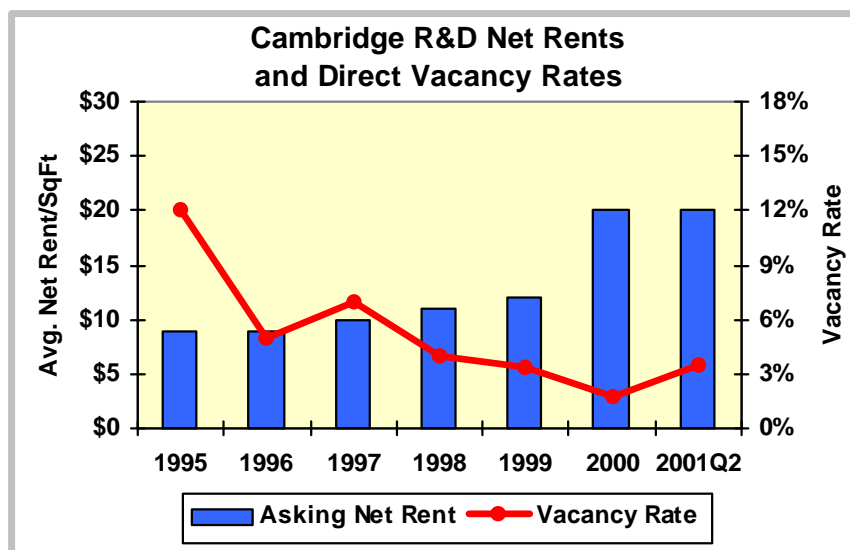
recently renovated and expanded its 500,000 SF R&D and manufacturing campus in Andover.

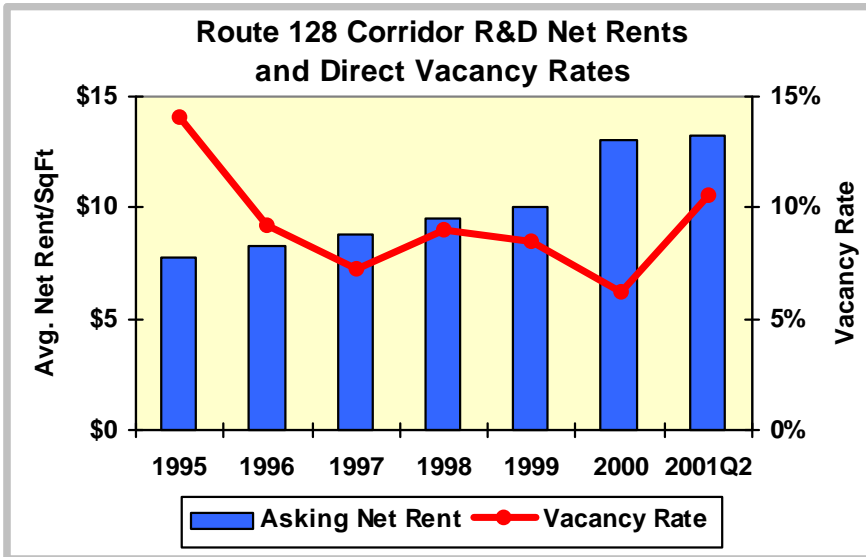
Amgen, the world's largest biotechnology company (as measured by market cap), now has a massive new facility coming on-line in Kendall Square. A stone's throw away, major local employer Biogen recently expanded at Cambridge Center. Also nearby are projects under construction for Millennium Pharmaceuticals and Alkermes.

This massive source of demand for office/R&D space has also caught the attention of office building owners and developers of projects originally slated to be telecom hotels. With over 500,000 SF of R&D space under development, telecom hotel developers in Cambridge are very fortunate to be located in the Kendall Square neighborhood. Demand from biotech companies running out of space may come to the rescue of these well-located projects.

While the looming temporary oversupply of R&D space in Cambridge has resulted in asking net rents remaining flat during the first half of 2001, there is little risk of a substantial decline in average R&D rents in this submarket. Research activities associated with Harvard University and M.I.T. are not limited to the biotechnology field and demand for R&D space will continue to grow in the years ahead.

Institutional investment demand remains strong as well, as shown by M.I.T.'s on-going acquisition and redevelopment of multiple properties for office/lab/research uses.





## Route 128 Corridor Copes with Tech Sector Downturn

R&D facilities along the Route 128 Corridor are almost always in demand by some type of space user or a developer. For many high technology firms, R&D buildings provide for cost-effective office space in prime locations while also accommodating lab facilities, assembly, and storage spaces.

Telecom firms made their mark along Route 128 during the past two years. Internet service provider PSINet paid around \$155 per square foot for 55 Middlesex Turnpike in Bedford, MA last year, about 50% more than the seller had paid for the property the previous year. Now operating under bankruptcy court protection, the market waits to see what PSINet might do next with this prime facility.

Further out along the Route 3 Northwest Corridor, Nortel Networks acquired 129 Concord Avenue in Billerica from Nordic Properties last year, paying about twice the amount the seller paid to acquire the property just a few months earlier. More than

twice that amount was spent renovating the property into an exceptional, state-of-the-art office/R&D facility with clean room production/lab space. Now Nortel Networks is reportedly preparing to sell that facility without having occupied it.

While the slump in the high-tech sector has not been limited to telecom firms, their troubles have been the

most severe, save for dot-com enterprises that ran totally out of capital. High-tech equipment designers and manufacturers are coping with temporary cutbacks in demand from their customers. Same goes for many computer software companies.

The long-term outlook for the high-tech sector along the Route 128 Corridor, in general, remains bright. One of the most highly-skilled R&D workforces in the nation resides in the pleasant communities along this corridor. In addition, many of the finest residential neighborhoods for executives, entrepreneurs, and venture capitalists are located nearby. Aside from growing traffic congestion, the Route 128 Corridor will continue to be very popular with companies requiring R&D space in strategic proximity to key human capital resources.

Investor demand is strong and diverse, with R&D properties along the Route 128 Corridor and Route 3 Northwest Corridor being viewed as strategic long-term investments with valuable upgrading potential.



*Completed early this year, 20 Dan Road, Canton, is a 104,000 SF flex building constructed by Conroy Development. A similarly-sized flex building nextdoor at 10 Dan Road was completed last fall.*

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# Interstate 495 Loop Remains Popular

With new construction of R&D space along the Interstate 495 Loop kept to a reasonable level during the 1990s, the outer ring of Metropolitan Boston is much better positioned to absorb space that is becoming available as major high-tech corporations consolidate their operations and locations. The "build it en masse and they will come" mentality of the 1980s has been replaced by an incrementalist approach to development of R&D space.

Build-to-suit projects have also played a major role in expanding the inventory of R&D space along the Interstate 495 Loop. EMC Corp.'s new 200,000 SF office/lab/R&D mid-rise facility across from its large manufacturing complex at 50 Constitution Boulevard in Franklin, MA is a case in point. The functional layout of this new facility is geared to meet specific needs of the owner and is not typical of a speculative property. However, the building's attractive design, amenities, and convenient location also make the property highly marketable to future users, providing EMC Corp. with a valuable asset.



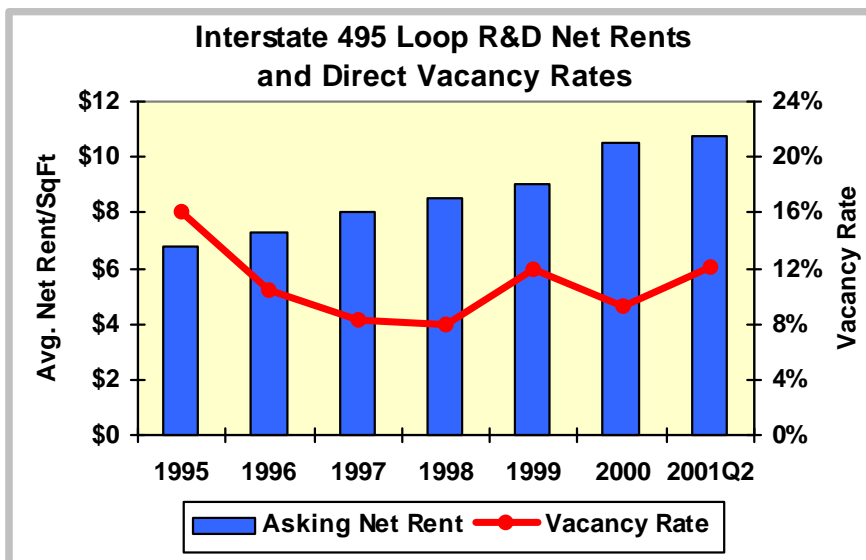
*Recently completed Building 7 at 101 Billerica Ave. in North Billerica is leased to Kaye Instruments, a subsidiary of Spirent PLC. This business park has expanded considerably in recent years, confirming demand for R&D (flex) space in an attractively landscaped setting.*

With office rents having soared in recent years prior to giving back some of those gains this year, asking net rents for R&D space along the Interstate 495 Loop have also soared. It is not uncommon for R&D rents in recent leases to be above "replacement cost" equivalent levels. The result has been an unusual situation in which current cash flow-based property valuations are sometimes significantly higher than

replacement cost estimates. This has caused some institutional buyers to sit on the sidelines while providing a buying opportunity for owner-occupants and developers eyeing additional rent growth as existing leases expire.

As with any property type, location plays a key role in determining the desirability and value of R&D properties. Interstate 495 Loop submarkets are very appealing to high tech corporations wanting to offer employees closer proximity to affordable housing. As major corporations such as Cisco Systems and EMC Corp. expand along the Interstate 495 Loop in the years ahead, demand for nearby R&D space by partner and supplier firms will increase as well.

Proximity to major highway interchanges is especially important along the Interstate 495 Loop as employees may be coming from distant locations. While "the Boroughs" remain the most popular Interstate 495 submarket, demand is also strong in Andover, Westford, and Franklin.



# METROPOLITAN BOSTON R&D MARKET

## Conditions as of 2001Q2

R&D Submarket	Space Inventory	Vacant Space	Vacancy Rate	Average Net Rent
<b>City of Boston</b>	<b>5,432,759</b>	<b>668,773</b>	<b>12.3%</b>	<b>\$21.00</b>
<b>Cambridge</b>	<b>1,415,417</b>	<b>48,549</b>	<b>3.4%</b>	<b>\$20.00</b>
Route 128 North	11,693,451	1,093,338	9.4%	\$13.00
Route 128 Northwest	8,303,000	464,968	5.6%	\$14.00
Route 128 West	9,568,294	1,408,453	14.7%	\$15.00
Route 128 Southwest	4,321,737	501,321	11.6%	\$11.00
Route 128 South	2,614,495	366,814	14.0%	\$11.00
<b>Route 128 Loop</b>	<b>36,500,977</b>	<b>3,834,894</b>	<b>10.5%</b>	<b>\$13.25</b>
I-495 North	4,883,830	574,338	11.8%	\$10.00
I-495 Northwest	4,748,204	338,072	7.1%	\$11.00
I-495 West	7,565,377	1,059,153	14.0%	\$11.50
I-495 Southwest	1,808,710	141,984	7.9%	\$11.00
I-495 South	1,516,391	364,085	24.0%	\$10.00
<b>I-495 Loop</b>	<b>20,522,512</b>	<b>2,477,633</b>	<b>12.1%</b>	<b>\$10.75</b>
<b>Metropolitan Boston</b>	<b>63,871,665</b>	<b>7,029,848</b>	<b>11.0%</b>	<b>\$13.25</b>

This report was researched and authored by Daniel P. Guenther, SrVP / Director of Research, in collaboration with NAI Hunneman Commercial Company office, R&D, and industrial brokers, property managers, and project consultants as well as using property-level data provided by CoStar Realty Information Group. The views and opinions expressed are solely those of the authors and are not necessarily those of NAI Hunneman Commercial Company nor its employees. For additional copies of this report, please call your NAI Hunneman broker or Amy Szeto at (617) 457-3400. If you have questions regarding the data or analysis contained in this report, please call Dan Guenther at (617) 457-3369 or send an e-mail to [dan\\_guenther@naihunneman.com](mailto:dan_guenther@naihunneman.com).

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