

## Vacancy gloom lifts a bit by year's end

Commercial Real Estate **RICHARD METCALF** Of the Journal

A dark and cloudy year for the Albuquerque metro's office real estate market had a silver lining.

The office market ended 2009 with more space filling up than going empty, according to the latest Office Trends Report by Grubb & Ellis New Mexico. Among the 62 metros tracked by Chicago-based Grubb & Ellis, Albuquerque was one of only eight with a positive absorption of office space last year.

Keys to the positive absorption were the openings of Hewlett-Packard's 218,000-square-foot service and sales center in Rio Rancho and the 112,000-square-foot second phase of Fidelity Investments' office building at the Mesa del Sol master-planned community.

"Without (those two deals), the total amount of space absorbed for the year would be a negative 271,000 square feet of space while the vacancy rate would be 44 basis points higher," the new report says.

Ultimately, however, the office vacancy rate still jumped from 13.1 percent at the end of 2008 to 16 percent at the end of 2009. Last year ended with the highest office vacancy rate since the first quarter of 2004, when it peaked at 17 percent, according to Grubb & Ellis.

From a broader perspective, Albuquerque's office market isn't doing too badly. The average office vacancy rate nationwide increased from 14.8 percent at the end of 2008 to 17.4 percent at the end of 2009. Phoenix had the highest vacancy rate in the country at 26.6 percent at the end of the year.

Last year's increase in vacancy rate does not necessarily contradict a net absorption of space. The two don't always go hand in hand.

In terms of square footage, the HP and Fidelity deals accounted for threequarters of all office activity in what will go down as a really slow year in commercial real estate, said Ken Schaefer, director of brokerage services at Grubb & Ellis. In other words, the size of the two deals outweighed the sum of all the smaller spaces going empty during the year.

In fact, the largest single vacancy in 2009 occurred when HP vacated 72,000 square feet of temporary space in the Jefferson corridor. The Palo Alto, Calif.-based company's new building more than made for the vacancy.

The foremost contributing factor to the increase in vacancy rate was the opening of several new but largely empty office buildings. Alameda Office Complex at Hope Plaza and Office Suites at Fountain Hills, both on the West Side, and the Aperture Center at Mesa del Sol opened last year with a total of more than 100,000 square feet of vacant space, Schaefer noted.

Newer, largely empty buildings have another impact on the overall office market. Because of the costs associated with newer buildings – construction, land, government fees – their asking lease rates are almost always at or near the top end of the office market. Those comparatively high lease rates pull up the average asking rates for the entire office market, Schaefer said.

The average asking lease rate for space in a Class B office building actually increased by about 4 percent in the past year, from \$17.30 a square foot at the end of 2008 to \$17.96 at the end of 2009, according to Grubb & Ellis. The local increase bucked the national trend, which saw an average decrease of 4.6 percent in asking lease rates for Class B space around the country.

Class B space makes up two-thirds of Albuquerque's office market. A Class B building typically has a wide range of tenants and looks pretty good. Rents are in the middle of an office market's high-to-low range.

The increase in average asking lease rate also points to landlords trying to hold the line on rents in order to cover costs, said Scott Throckmorton of Argus Investment Realty.

"A component of the asking rate is operating expenses," he said. "Taxes went up in the past year. Utility bills are going up. Labor costs are going up."

Both Schaefer and Throckmorton said the increase in average asking lease rate is more of an illusion than a reality. Effective lease rates, or what space actually rents for, are dropping sharply here as they are all over the country, Schaefer said.

"It's like when you're buying a car, no one pays the sticker price," he said.

A precipitous drop in lease rates appears to be coming. Last week, Forest City Covington dropped its asking lease rate at the Aperture Center from \$23 a square foot to \$19.50, full service. The discount is good for leases of five years or more that are signed by June 1.

In light of the recession, budget-minded companies looking for space tend to set \$20 a square foot as a cutoff point for rent, explained Terri Dettweiler of CB Richard Ellis, who is marketing the space for Forest City. At the Aperture Center's former rate, she added, "We don't even make the short list."

The move comes two months after the biggest owner of office properties in Albuquerque, BGK Group of Santa Fe, dropped the asking rates on more than half of its 20 local office properties by 20 percent or more. BGK's local portfolio consists of Class B buildings or better.

As another example, the Office Suites at Fountain Hills at 8700 Education Place NW was marketed last April at an asking lease rate of \$24 a square foot, full service. The property is currently on the market at an asking lease rate of \$17.50 a square foot, plus expenses.

Looking at the major submarkets for office space in the metro, Downtown ended 2009 with the same vacancy rate of about 18 percent that it seems to have year in, year out. Throckmorton said, "Downtown will always be stable in that 18-20 percent rate, while other submarkets go up and down."

Uptown lost about 100,000 square feet of occupied space in the past year, sending its vacancy rate from 8.5 percent at the end of 2008 to 14.2 percent at the end of 2009. Locally owned Heritage Home Healthcare vacated 23,000 square feet in Uptown for a larger space that it purchased in the North I-25 submarket.

Most of the remaining space vacated in Uptown stemmed from consolidations that resulted from the merger of financial services firms Morgan Stanley and Smith Barney, and Verizon Wireless' purchase of Alltel a year ago, Throckmorton said. The consolidations are an example of how corporate movements at the national, even international level effect the local market.

The metro's biggest submarket for office space, the North I-25 area with more than 3.2 million square feet, saw its vacancy rate go up from 13.3 percent at the end of 2008 to 17.4 percent at the end of 2009. The main reason for the increase was HP's departure to Rio Rancho.

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**JOURNAL FILE** The stylish, 78,000-square-foot Aperture Center at Mesa del Sol has dropped its asking lease rate for office space from \$23 a square foot to \$19.50 a square foot.





**JOURNAL FILE** The final phase of the 217,842-square-foot Fidelity Investments building at Mesa del Sol, shown here, helped tip the metro's office market into positive territory in 2009.