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This spring should be a great time to be looking for office space or real estate capital

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As we emerge from one of the snowiest winters on record, New Englanders look forward to the warmer months with typical reservations.

The region is still trying to absorb the latest exodus of another corporate headquarters, as Gillette's new Ohio-based parent is likely to shed many executive jobs in this market. Coming on the heals of John Hancock's sale to Manulife, this latest takeover will put additional stress on the local office market. While office owners cannot be overly pleased with this news, downward pressure on office rents should make Boston more competitive and hopefully lead to additional job growth.

Not all corporate sales to outside companies lead to a reduction in local investment. BankNorth's recent sale to Canada's Toronto Dominion Bank looks like it will have the reverse effect. The bank, headquartered in Portland, Maine, expanded significantly into the Massachusetts market over the last several years with acquisitions of several lenders including Metro West Bank and AndoverBanc. Now, with the larger pocketbook of its new parent, BankNorth has announced it is paying around $100 million over the next 20 years to re-flag the former Fleet Center as "TD BankNorth Garden".

Real estate remains on most investors A-List. Almost defying the upward trend in interest rates, cap rates for commercial properties continue to either fall or remain near record low levels. The investors come from a broad range: pension funds, REITS, private partnerships and more recently, hedge funds from both domestic and international locals. Outside of regional malls in weak markets and offices in challenging areas, almost every asset class is enjoying unprecedented attention. Sales at these high prices, coupled with investor return requirements is driving more borrowers to seek higher leverage via "stretch – bridge loans" or mezzanine loans which can move debt to 90% LTV and beyond. In addition, many of these borrowers are looking for little or no amortization in order to allow some cash flow to the investors.

Interest rates continue to click northward as US Treasury yields have grown over 50bps (1/2%) so far this year. Perhaps more interesting is the fact that the yield curve has flattened substantially as the difference between yields of the 5 to 30 year T's has compressed from about 100bps (1%) to about 70 bps (.7%). This type of event historically indicates investors are seeing mixed signals in the market. While the Fed has indicated they plan to continue gradual rate increases, the market appears to believe there is no dramatic upward pressure on rates.

The year 2004 saw record loan activity on a national level. The Mortgage Bankers Association convention in San Diego was one of the best attended in recent years. CMBS activity is off to a big start with two very large ($1.5 billion) securitizations already completed this year verses only one for the same period last year. All these trends point to the fact that it is a great time to be a borrower.

Some real estate bears are predicting a massive market correction, including a full re-pricing of the residential sector, which has seen record appreciation. Others see a threat of a return to the "real estate winter" of the early 1990s. While any comparison to that destructive period is sure to win headlines and gain attention, the critical difference between the current cycle and the one from 15 years ago is the strong liquidity in today's market. The liquidity in the marketplace will continue to grow as more pension funds; endowments and foundations increase their allocation to real estate asset classes. With liquidity, comes efficiency, which will minimize the historic cycles that had been experienced in real estate investment and development of the past.

Liquidity is further enhanced by a very healthy banking industry. Much of the "risk investment" today, especially in higher leverage situations, is being conducted by non-bank institutions. This would seem to be a proper allocation as these investors are often better equipped to address workouts and at a minimum are not abusing Federally insured deposits.

In summary, this spring should be a great time to be looking for office space or real estate capital. Despite all the talk about an overheated market and higher rates, the real estate market should continue to offer a stabilized investment alternative for the foreseeable future.

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