

**February 2007 Newsletter****By Jake Adler-Partner**


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## Washington DC Metro Land: Is There Really a Shortage?

There has been a lot of talk recently about the shortage of land available for development in the Washington DC Metro area and as such it will have an upward effect on rents for the future. Are more companies and people moving in and helping to drive this demand? Are corporations leasing more space to expand? How will BRAC (Base Realignment and Closure) affect the area from Washington DC to North of Baltimore in and around the Aberdeen Proving Grounds?

We'll start with the hot topic of BRAC. It is estimated that anywhere from 40,000 to 60,000 new residents and jobs will be created in Maryland over the next few years. The biggest question is where are these people going to come from? Will they be moving from out of state? Or, will local residents change jobs and work for government contractors? The unemployment rate in Maryland at the end of 2006 was 3.8%, and below 3% in Montgomery County, so in terms of growth from existing residents, either local businesses will lose talent to these contractors or these contractors will have vacant positions (assuming they want to house these employees here in Maryland).

According to CoreNet Global's *Corporate Real Estate 2010: Enabling Work in a Networked World*, the goal of corporate real estate directors will be to reduce the amount of traditional office space that corporations occupy by offering more flex time and telecommuting. Many firms recently interviewed have acknowledged that they have already taken steps and are on track to meet this goal.

*(CoreNet Global is the world's premier association for corporate real estate and related professionals. It is run by and for corporate real estate directors).*

This is in stark contrast to what many institutional investors are saying and doing. Many of these investors have been purchasing office buildings at extremely high prices and low cap rates with the assumption that office rents will increase down the road and their return on investment will then rise. No one can say if this is right or wrong but Corporate America is singing a different tune. Also, let's not forget that more and more support functions at many of these corporations will be outsourced overseas to lower costs thus many of these firms will not need as much space as they have now.

In terms of land development, it is correct that many jurisdictions have put a hold on development, but let's not forget the projects put on hold are not the owner occupied buildings, meaning a company is constructing a building to occupy on their own. Municipalities want to listen to their constituents' complains about development but they do not want to lose substantial jobs.

As was with the rise and fall of the tech firms in the late 1990's and early 2000's, investors are flocking to the 'hot market' which is real estate right now. Many technology companies crashed, it is anticipated that many of the recent real estate developments and purchases will as well. Just like plenty of technology firms survived, many landlords will survive and will come out ahead, but the big question is how many will lose their shirts?

At the end of the day, there is a shortage of land in the true sense, but is there really demand coming to fill the gaps many of these developers and investors are hoping for? More importantly, do companies really have to be in the high rent areas? Some do, or think they do, but most times companies can move to a cheaper location and remain competitive.

Construction costs have gone up and many investors of late feel they will be able to obtain future rental increases with their spaces. How long will construction costs remain high? Many believe that costs will continue to remain high due to heavy demand from China and India. Remember, those nations are also building office buildings to house workers, probably from US firms looking to outsource work!

New construction will almost always be more expensive, so don't be surprised if firms start opening offices in some of the depressed office markets across the country, from Northern New Jersey to Denver, Colorado and all the cities in between. Firms can lease cheaper office space and pull from a cheaper labor pool, as well as placate legislators by not moving support jobs overseas.

In the end, don't believe all the hype you hear and read and don't think that times will always be good. Things change. Terrorists attack. Money dries up. People wise up to their poor investment judgment. It's the circle of life and things always come back to where they originated.

There is a business motto that rings so true in this heated commercial real estate environment and it is "***Bad business decisions are often made in good times***". Keep your powder dry!

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