NAI Fennelly Sees Service, Business, Legal Office Sectors Overtaking Pharma In Central NJ

FEBRUARY 5, 2018 | BY STEVE LUBETKIN

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Gerard (Jerry) Fennelly, president of NAI Fennelly, Princeton, NJ

PRINCETON, NJ—Pharmaceutical firms and the life sciences sector have been driving significant activity in the Princeton/Central New Jersey submarket for several years, but the market has slowed down considerably since 2016, and the service/business/legal sector have overtaken health sciences as the fastest expanding office sector, according to new research by **NAI Fennelly**, which has offices in Hamilton and Princeton.

In its just-published January 2018 Princeton Office Space Report, **NAI Fennelly** says net absorption of Princeton, NJ, office space was 768,532 square feet in 2017, off nearly 24 percent off from growth of 1.015 million square feet in 2016. 2016 was an exceptional year for the Princeton market, the first time since 2008 in which there was over one million feet of positive net absorption, **NAI Fennelly** says.

The average per-transaction growth declined year-over-year, from 5,050 square feet in 2016 to 3,694 square feet 2017. That's the first time the average transaction dipped below 4,000 square feet since 2010, the firm says.

Pharmaceutical and bio companies, led by foreign-based companies, represented 20.8 percent of the growth in Princeton's office/lab market. Two of the biggest deals of the year, in fact, involved companies headquartered in India. **Aurobindo** had a new 567,000-square-foot building delivered in East Windsor (Exit 8 NJ Turnpike) that is a blend of office, lab, drug manufacturing and drug storage, while **Eywa Pharma**, also from India, leased 62,000 square feet at **Cedar Brook** in Cranbury for drug manufacturing.

Bristol Myers Squibb made several adjustments to its real estate portfolio, including shedding lab space locally and adding space in Cambridge, MA. However, the biggest deal was the completion of a new 600,000-square-foot office building in Lawrenceville – or about two miles from the company's headquarters in the greater Princeton metro market.

The greatest amount of office expansion last year came from the service/business/legal sector, with 324,577 square feet, overtaking pharma as the expansion leader for 2017.

In terms of vacancy rates and rental rates, the downtown Princeton submarket, which is both small and unique, had the lowest vacancy rate of 6.1 percent and a wide range on rents, from $30 to $45 per-square-foot. The Route 1 submarket, which has about 40 percent of the overall supply and 54 percent of total demand from Princeton's 25 million-square-foot office market, ended last year with a vacancy rate of 21.47 percent and rents between $22 and $37 per square-foot. Class A rents have increased 5 percent during the recent 24 months.

The Cranbury submarket, with its overall access to the New Jersey Turnpike and proximity to New York or South Jersey, had a vacancy rate of 21.1 percent at the end of last year, most of it in biology lab space. Cranbury rents have a similar range depending on whether the space is lab or office space, from $19 to $30 per foot. The vacancy rate for the Ewing/Lawrenceville (located at the crossroads of NJ 295 and Route 1) submarket ended up slighter higher for the year, at 10.61 percent, in part because five tenants moved from Princeton Pike and Lenox Drive into corporate (office) purchased facilities.

Also, **GS1** built its own free-standing office building at Route 31 and 295. Those departures were somewhat offset by the 88,000 square feet **Billtrust** leased at **1009 Lenox Drive**, a move the automated accounts receivable and payments company made to reduce commute times for its employees, many of which come from Pennsylvania and South Jersey.

There were 20 sales transaction of office properties totaling $82 million. Of those, 14 of the sales were owner/occupier, an unusually high number compared with many US submarkets. Yet they were among the smaller buildings as "user sales" only accounted for $23.3 million of the total volume for the year.

Many of those user sale acquisitions were from buyers exiting New York and moving from leased buildings where rents are going up. Most of the owner/occupier purchases featured low capitalization rates of around four percent.

Capitalization rates usually reflect the going-in or first-year yield and the level of risk associated with an investment sale. By comparison, the six investor sales had cap rates from 7.8 percent to 9.2 percent, the latter of which involved the $12 million sale of a four-story, 111,300-square-foot office building located at **3 Independence Way** in South Brunswick, part of the **Mack-Cali** office portfolio.

Over the next 12 months, **NAI Fennelly** says Princeton should continue to experience an average growth of 800,000 square feet in office expansion (gross absorption/actual leases), offset by an estimated 250,000 square feet in consolidation and relocation movements. Like 2017, leasing activity should be somewhat balanced between class A, B and C office properties.

International and incubator pharmaceutical companies will continue to be attracted to Princeton's office/laboratory property markets in part because the cost of living for executive level and staff positions is much more affordable than other life science centers in the US, including Boston, San Diego, San Francisco and Palo Alto, CA. Princeton also offers central proximity to over 80 million people within a five-hour drive and excellent rail service throughout the Northeast.