

APPENDIX: D

REAL ESTATE MARKET ANALYSIS

ECONOMIC DEVELOPMENT STRATEGY CITY OF NEWTON, MASSACHUSETTS

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Prepared for:

City of Newton
1000 Commonwealth Avenue
Newton, MA 02459



120 West Avenue, Suite 303
Saratoga Springs, NY 12866

518.899.2608

www.camoinassociates.com

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EXECUTIVE SUMMARY

As part of the initial research to create an economic development strategy for the City of Newton, Camoin Associates conducted a real estate market analysis to determine development opportunities for different use types throughout the city. These use types include office space, lab space, medical office, industrial, retail, hotel, and residential. This information will be used to ensure economic development strategies are grounded in market realities. Market opportunities are summarized in Table 1.

Table 1: Newton Market Opportunity Summary

Newton Market Opportunity Summary	
Use Type	Opportunity
Office	Significant vacancies and a lack of Class A sites limit demand for new development, but opportunities exist to reposition and amenitize current inventory.
Lab	Robust growth and soaring rents in Cambridge/Boston life sciences sector presents an opportunity to create a lab space node in Newton.
Medical Office	An aging population and shifting trends in health care delivery means strong demand for medical office space into the future.
Industrial	Land availability constraints and high land costs limit potential for comparatively low-value industrial development.
Retail	High incomes and significant spending leakage are an opportunity for new retail development in the city, but rising rents are squeezing out existing mom-and-pop shops.
Hotel	Sluggish commercial development in Newton and increased room supply in nearby suburbs limits potential, but differentiated boutique hotels could be viable.
Residential	Urgent need for multifamily/affordable units to house the talent required to attract commercial development.

INTRODUCTION

As part of the initial research to create an economic development strategy for the City of Newton, Camoin Associates conducted a real estate market analysis to determine development opportunities for different use types throughout the city. These use types include office space, lab space, medical office, industrial, retail, hotel, and residential. This information will be used to ensure economic development strategies are grounded in market realities. A discussion of market trends and development potential for each use type follows.

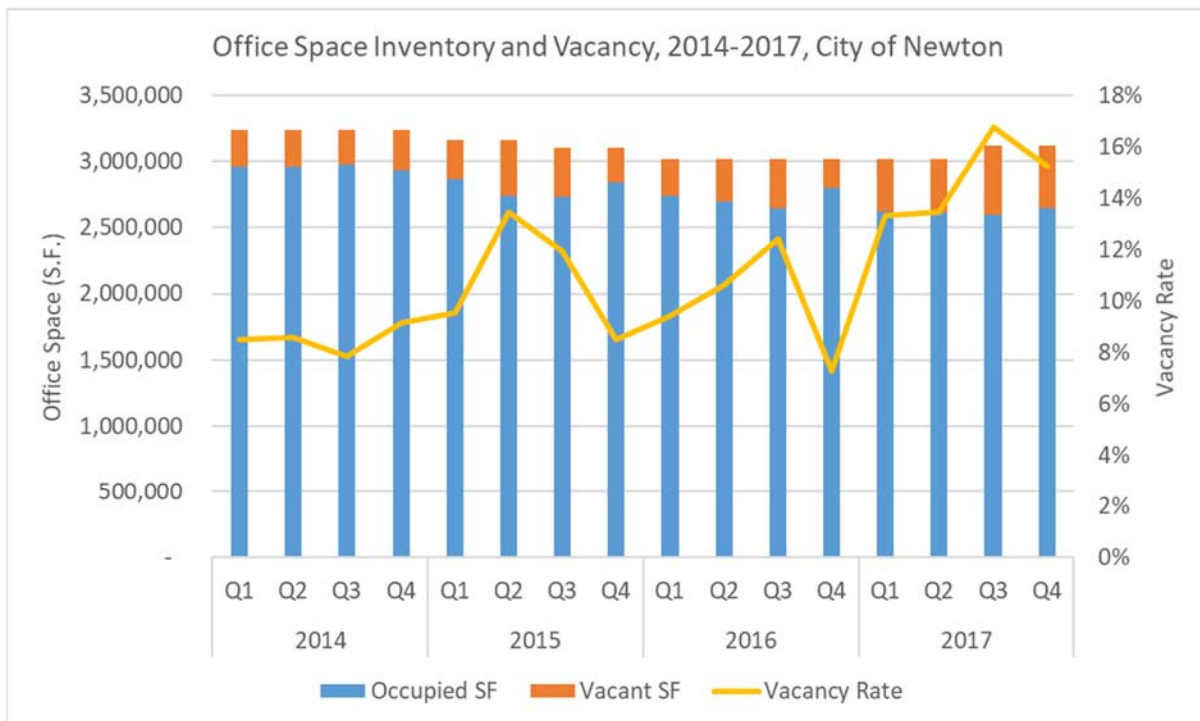
OFFICE

As the Boston economy booms, the regional office market has benefited from significant tenant demand, especially among innovation, technology, and life sciences companies. The metro’s ability to attract and retain talent has led to supply challenges, particularly in the Boston core and Cambridge. Locations with amenities and transit access continue to perform the best in terms of occupancy and command the highest rents.

Urbanization trends, however, are a challenge for some suburban markets, which have experienced elevated vacancy rates. Large blocks of space are becoming increasingly limited in Boston and Cambridge, putting upward pressure on rents, and creating opportunities for suburban locations to lure larger tenants with more competitive pricing. Suburban office offerings that are mixed-use and transit-oriented will have the most success attracting tenants. The repositioning of aging properties in transit-oriented locations has become a salient trend in the suburbs, as speculative new-build is unlikely in the near term due to ample vacancies and high construction costs. The addition of amenities such as gyms, food service, conference space, game rooms, and outdoor space has taken hold as a way to make use of unproductive space and add value to aging office properties.

Another notable trend is the “urban outpost” model, by which traditionally suburban tenants have multiple locations in order to retain their existing suburban-oriented workforce while simultaneously accessing downtown talent.

Figure 1: Office Space Inventory and Vacancy, City of Newton



Data Source: JLL

Newton Office Space Inventory

The commercial office space inventory in Newton has remained relatively flat over the past four years, dipping slightly from 3.2 million square feet in 2014 Q1 to 3.1 million square feet to 2017 Q4. Meanwhile, office vacancies have risen considerably from 8.5% to 15.2%. Note, however, that the newly renovated and delivered 2 Wells Avenue building accounts for 102,000 square feet of the vacant space. Excluding this building, the vacancy rate in Newton is 12.4%. Vacancy trends over the past several years are shown in Figure 1.

Newton is part of the Route 128/Mass Pike submarket, as tracked by commercial brokerages. According to JLL, office inventory in the city represents about 15% of all submarket space, and Newton's vacancy rate is on par with that of the submarket as a whole, about 15.0%. This compares to 17.8% in the Boston suburbs overall, 8.9% in central Boston, and 5.7% in Cambridge.

Vacancy rates for Class A are higher in Newton than for space overall, at 17.0% (excluding 2 Wells Ave). Class A vacancy rates are also higher in many of the comparison markets, though Newton has the highest spread in vacancy between Class A and Class B/C properties. Class A space also comprises a significantly lower share of all office space in Newton as compared to other markets. Only a third of office space in Newton is considered Class A by commercial brokerages, compared to 61% in the metro overall, and 63% in both the Rt. 128/Mass Pike submarket and Boston suburbs overall.

Rents in Newton and Rt. 128/Mass Pike submarket are about average when considering the Boston metro as a whole. Class A rents in Newton are around \$38 per square foot, considerably higher than more distant submarkets along I-495 where rents are just over \$20 per square foot, but considerably lower than rents in central Boston and Cambridge where average rents are upwards of \$60 per square foot.

Table 2: Office Statistics, 2017 Q4

Office Statistics, 2017 Q4						
Market	Class A Space			All Classes of Space		
	Inventory (SF)	Vacancy Rate	Rent per SF	Inventory (SF)	Vacancy Rate	Rent per SF
Newton*	1,063,631	17.0%	\$ 38.24	3,124,724	12.4%	\$ 34.07
Rt. 128/Mass Pike Submarket	13,201,608	16.5%	\$ 40.19	20,793,230	15.0%	\$ 37.68
All Boston Suburbs	57,212,727	17.6%	\$ 28.71	90,979,957	17.8%	\$ 25.59
Central Boston	37,955,708	9.5%	\$ 61.06	66,370,589	8.9%	\$ 57.68
Cambridge	7,544,118	6.3%	\$ 69.44	10,107,067	5.7%	\$ 63.60
Boston Metro	102,712,553	13.8%	\$ 40.11	167,457,613	13.6%	\$ 36.44

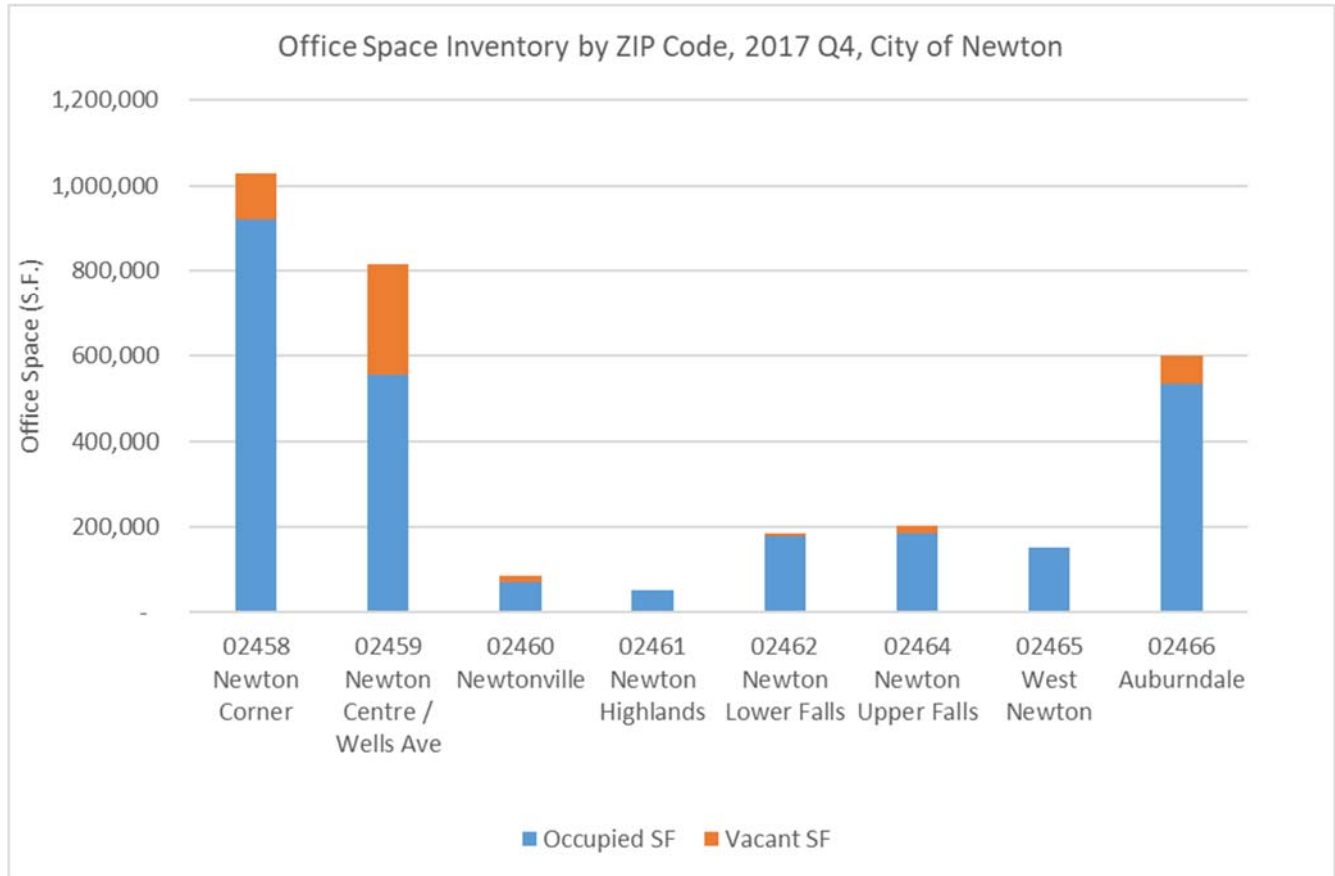
*Vacancy rates adjusted to exclude 2 Wells Avenue. Including 2 Wells Ave, Class A office vacancy rate is 23.1% and overall office vacancy is 15.2%.

Note: Vacancy rate includes both direct and indirect vacancies. Rents reflect direct asking rents.

Source: JLL

Newton’s 3.1 million+ square feet of office space is concentrated in three ZIP codes: 02458 (Newton Corner) with 33% of all space, 02459 (Newton Centre/Wells Ave) with 26%, and 02466 (Auburndale) with 19%. See Figure 2 for the distribution of the city’s office space by ZIP code.

Figure 2: Office Space Inventory by ZIP Code



Rt. 128/Mass Pike Submarket Development Pipeline

Within the Rt. 128/Mass Pike submarket,¹ major recent deliveries include 89 A Street in Needham Crossing, which has been fully leased to Shark Ninja and Steward Health. Bose has leased 100,000 square feet of space at 80 Guest Street, part of the Boston Landing development in Boston’s Allston/Brighton neighborhood featuring nearly 2 million square feet of mixed-use development, a state-of-the-art practice facility for the Boston Bruins, and a new commuter rail station providing access to South Station in downtown Boston. Other developments include POST, a 430,000-square-foot development at the Rt.128/Rt. 2 in Waltham, expected to attract a variety of innovation companies. Needham has recently approved a tax break allowing NBCUniversal to build a new regional headquarters in Needham Crossing.

¹ The Rt. 128/Mass Pike submarket is defined to include the following communities: Newton, Watertown, Waltham, Weston, Wellesley, Needham, Brookline, and Allston/Brighton (part of the City of Boston).

Office Space Demand Projection

To estimate future demand for office space in Newton, we analyzed job projections data for the City of Newton, the Rt. 128/Mass Pike submarket, and the Boston MSA. Table 3 shows the projected increase in employment by industry sector over the next ten years (2017-2027), with sectors that typically utilize office space highlighted in orange.² Collectively, office-utilizing industries in Newton are expected to add about 1,600 jobs, growing slightly slower than the economy overall. According to these projections, Newton will account for a growing share of office jobs of the Rt. 128/Mass Pike submarket, with 30% of the 5,300 new submarket office jobs expected to be located in Newton. Currently, Newton represents about 22% of office jobs in the submarket. The Boston MSA as a whole will add nearly 65,000 office jobs by 2027, of which Newton will account for about 2.5%, consistent with the city's current share of office jobs in the region.

Table 3: Projected Employment Growth in Office-Utilizing Industries, Newton

Projected Employment Growth in Office-Utilizing Industries, Newton					
NAICS	Description	2017 Jobs	2027 Jobs	2017 - 2027 Change	2017 - 2027 % Change
11	Agriculture, Forestry, Fishing and Hunting	68	82	14	21%
21	Mining, Quarrying, and Oil and Gas Extraction	<10	<10	Insf. Data	Insf. Data
22	Utilities	0	0	0	0%
23	Construction	1,536	1,795	259	17%
31	Manufacturing	457	420	(37)	(8%)
42	Wholesale Trade	1,316	930	(386)	(29%)
44	Retail Trade	5,347	5,159	(188)	(4%)
48	Transportation and Warehousing	600	755	155	26%
51	Information	2,335	2,382	47	2%
52	Finance and Insurance	2,387	2,313	(74)	(3%)
53	Real Estate and Rental and Leasing	2,821	3,148	327	12%
54	Professional, Scientific, and Technical Services	7,008	7,739	731	10%
55	Management of Companies and Enterprises	740	774	34	5%
56	Administrative and Support and Waste Management and Remediation Services	4,535	4,685	150	3%
61	Educational Services	21,350	23,345	1,995	9%
62	Health Care and Social Assistance	13,062	15,974	2,912	22%
71	Arts, Entertainment, and Recreation	3,412	3,826	414	12%
72	Accommodation and Food Services	3,678	3,924	246	7%
81	Other Services (except Public Administration)	3,849	4,417	568	15%
90	Government	4,997	5,138	141	3%
99	Unclassified Industry	0	0	0	0%
	Total for Office-Utilizing Industries	25,852	27,448	1,596	6%
	Total	79,506	86,816	7,310	9%

Source: EMSI, Camoin Associates

² This analysis defines office-utilizing sectors to include: Information; Finance and Insurance; Professional, Scientific, and Technical Services; Management of Companies and Enterprises; Administrative and Support; Other Services; and Government. Medical office space users, which are considered in the analysis of medical office building demand, are excluded. Educational Services, which occupy office space in part, are also excluded.

Assuming 175 rentable square feet of office space per job,³ about 280,000 square feet of office space will be required in Newton to accommodate future office jobs. In the Rt. 128/Mass Pike as a whole, about 924,000 SF will be needed and in the Boston MSA, 11.3 million SF.

Table 4: Projected Office Space Demand, 2107-2027

Projected Office Space Demand, 2017-2027							
Region	2017 Total Jobs	Share of MSA Jobs	2017 Office Jobs	Share of MSA Office Jobs	Projected Office Job Growth, 2017-2027	Share of Projected MSA Office Job Growth	New Office Space Demand* (SF)
Newton	79,506	2.7%	25,852	2.2%	1,596	2.5%	279,328
Rt. 128/Mass Pike Submarket	294,753	10.1%	119,849	10.0%	5,279	8.2%	923,770
Boston MSA	2,905,879	100.0%	1,199,385	100.0%	64,718	100.0%	11,325,606

*Assumes 175 SF of space per office job

Source: EMSI, Camoin Associates

While regional and local job growth will be strong, the glut of office space in the region means that even if no new office space is built, there would still be substantial office vacancies. In Newton, new office-utilizing jobs would fill about 60% of existing vacant space, leaving another 200,000 SF still vacant. In the submarket, only 40% of existing vacancies could be absorbed by projected job growth. See Table 5.

Table 5: Future Supply and Demand of Office Space

Future Supply and Demand of Office Space (SF)			
Region	New Office Space Demand (2027)	Existing Vacant Office Space (2017)	Remaining Vacant Office Space in 2027*
Newton	279,328	476,420	197,092
Rt. 128/Mass Pike Submarket	923,770	2,178,265	1,254,496
Boston MSA	11,325,606	14,174,332	2,848,726

*Assumes no construction of new office space

Source: EMSI, JLL, Camoin Associates

This analysis, of course, assumes that existing space will meet the needs of future office users, and is not to say that no new office space will be developed in Newton. In particular, potential large space users will find it challenging to locate acceptable existing space in the city, requiring new-build projects. In addition, dated and obsolete space may be removed from the city's office inventory, prompting the construction of space to satisfy some level of replacement demand. However, on a macro level, the abundance of vacant space in the market will mean that property owners will need to invest in their existing properties, undertaking renovations and adding amenities, in order to compete for a limited number of new tenants.

³ A 2010 report from the U.S. General Services Administration, "Workspace Utilization and Allocation Benchmark," found average rentable office space per employee to be 230 square feet. As a result of efforts to implement more efficient design standards, the typical office standard has declined from around 250 square feet per workstation in the early 2000s to around 190 square feet or less. In addition, a trend toward less personal workspace in favor of larger group space, as well as an increase in teleworking will likely contribute to continued declines in office space per employee. This analysis conservatively assumes 175 square feet per job.

Sites with Office Development Potential

A significant challenge for office space development in Newton is the lack of Class A sites within the city. While the city is physically proximate to downtown Boston, Rt. 128, and the Mass Pike, there are few sites with direct access to transportation infrastructure that Class A tenants require. For example, while much of Needham Street and Wells Avenue Business Park—together comprising the Newton portion of the N² Innovation District—are less than a mile from Rt. 128 onramps and offramps, developers perceive these locations as inferior to the Needham Crossing area, which is directly adjacent to the highway. Moreover, congestion along Needham Street and the traffic bottleneck at the entrance to Wells Avenue work against the desirability of these locations.

The quirky path of Newton's western municipal boundary along the Charles River means that many prime sites with direct access to Rt. 128 fall just outside the city limits in neighboring Needham, Wellesley, or Weston. An exception is the Exit 21/22 interchange area where Rt. 128 crosses Washington Street (Rt. 16) and Grove Street. In particular, the Riverside T station site was identified as a key opportunity property for Class A office development given its accessibility via both automobile and public transit.

Certain areas along Washington Street, including Newton Corner, Newtonville, and West Newton may have some Class A office potential, but are limited by a number of factors. Full direct access via the Mass Pike is present only at highly congested Newton Corner. West Newton is only directly accessible via a partial interchange to/from the east. Commuter rail access should be stressed as an important asset along this corridor, though infrequent service limits its usefulness. In addition, parking along Washington Street is very limited and parcels are highly fragmented, making lot assembly for a sizable project limited.

Nonantum stands out as a potential opportunity area and has existing office development comprising the Charles River Mill District. Further redevelopment of industrial properties is possible in this area, which is proximate to restaurants and other amenities on Watertown Street and in Watertown Square in neighboring Watertown, as well as the Charles River Greenway trail. However, a lack of direct public transit and Mass Pike access are limiting factors to Nonantum's development potential as a Class A office location.

Route 9 also presents some level of office development opportunity, particularly along the stretch with transit access (Newton Highlands and Eliot T stops) and the Chestnut Hill retail area, which offers amenities for office workers that can potentially be integrated. While Route 9 is a major thoroughfare, these sites are likely too far from interstate access for significant Class A development. Moreover, assembling sizeable lots will be a significant challenge all along Route 9. Still, there is likely some potential for small- to mid-scale infill commercial development.

LAB

Greater Boston has the highest concentration of life science researchers in the US. Kendall Square and MIT in Cambridge are the epicenter of life science research activity in the region, and supply of lab space is extremely constrained, with rents surpassing \$75 per square foot. As a result, lab space development has been spilling out of the Kendall Square area into West Cambridge, Boston's Seaport District, and Longwood Medical Area. Outside of the urban core, inner-ring suburbs are becoming increasingly attractive as a "release valve" for more lab space. Bedford, Lexington, Waltham, and Watertown have also seen significant lab space development, with rents in these communities averaging \$43 per square foot. The suburban development pipeline is growing, fueling the evolution of a suburban cluster of life science companies. Unlike in the office market, extremely constrained supply in the lab market has spurred speculative suburban development projects.⁴

There is currently no significant lab space in Newton as tracked by commercial brokerages, a fact confirmed by interviews with lab space developers. Newton is not "front of mind" when it comes to suburban lab space development chiefly because there is no existing cluster of major lab space users in the city. Lab tenants tend to want to locate near other lab space users for both practical and psychological reasons. Not only do they want to be around similar companies in an area that is perceived as a hub for life sciences activity, but the ability to expand into nearby space or sublet unneeded space minimizes risk. Being the only life sciences company in a given location is not optimal for most. While the suburbs to the north of Newton along Rt. 128 are increasingly perceived as a bioscience node, this activity has yet to spread southward.

From purely a locational perspective, Newton could be a viable place for lab space given its proximity to both Cambridge and the Rt. 128 suburbs with existing space. In addition, Boston College is currently undertaking construction of the new Schiller Institute for Integrated Science and Society, which will include laboratory and office space and may present an opportunity for synergies with other lab users. However, the nature of Newton's building stock and limited developable sites presents challenges for any developer interested in creating a sizeable lab node in the city. A minimum of 100,000 SF of lab space would be needed to anchor a potential node, with sites available nearby for additional future development.

In terms of building requirements, lab space requires stronger floor loading relative to office (100 pounds per square foot compared to 70 for office), 13.5- to 14-foot ceilings to run duct work, ventilation with a high air-change rate, good power distribution, and access to wastewater treatment infrastructure. In lab buildings, lower-story space is more valuable as regulations allow for fewer chemicals to be stored on higher stories. Single-story manufacturing buildings tend to be prime candidates for conversion to lab space as they already have or can be retrofitted to have these features.

A potential lab developer in Newton would need to know that the approvals process will be predictable and not overly onerous. Cambridge, Lexington, and Watertown were mentioned in interviews as municipalities with straightforward and predictable processes, and they have seen significant lab space development activity as a result. Designating certain area(s) in Newton where lab space development is permitted by right or with minimal effort would communicate to prospective developers that undertaking a lab project would be welcomed. The most desirable locations for lab space in Newton are similar to prime office space locations: sizable sites that can accommodate substantial development footprints and that offer good access to Rt. 128, the Mass Pike, and public transit.

⁴ JLL. Boston Life Sciences Outlook 2017.

MEDICAL OFFICE

Despite uncertainty in the healthcare industry with the continued speculation around the future of the Affordable Care Act (ACA), nationally the aging population and increasing number of people that are insured are driving an increase in demand. In response, the healthcare industry continues to grow and medical office building (MOB) vacancy rates have fallen. These trends are mirrored locally, where medical office space shows strong potential.

Medical office buildings are trending towards flexible space (flex space) and multi-specialty offices. This allows for the incorporation of a range of medical technology and equipment used in procedures and appointments. Additionally, the amount of technological equipment being used in procedures and appointments has been increasing, further adding to the demand for efficient space. Flex space allows for adaptability as technology changes or the needs of patients change.

Across the Boston region, medical office space vacancies are considerably lower than those of general office space, 6.1%⁵ versus 13.6%. Average gross rents are also lower at \$25 per square foot versus \$35 per square foot, as general office users are typically willing to pay for more prime locations. MOB rent growth in the Boston metro, however, topped 17% between 2017 to 2018 indicating strong demand and constrained supply. Low MOB vacancy, high rent growth, and favorable demographic trends point to opportunities for medical office space development into the future.

Medical Office Space Demand Projection

An examination of regional employment trends in ambulatory care and outpatient services suggests demand for over 5 million SF of new medical office space in the Boston metro by 2027, of which roughly 233,000 SF would be needed in Newton. (Refer to Table 6.) The pace of job growth in ambulatory health is expected to far exceed that of the economy overall, 24% for ambulatory health versus 9% economy wide. This translates into accelerating demand for suitable medical office space.

Table 6: Projected Demand for Medical Office Space

Projected Demand for Medical Office Space					
Region	Ambulatory Health Care Jobs*				New Medical Office Space Demand** (SF)
	2017	2027	2017-2027 Change	2017-2027 % Change	
Newton	3,847	4,780	933	24%	233,250
Rt. 128/Mass Pike Submarket	11,524	13,804	2,280	20%	570,000
Boston MSA	105,834	126,258	20,424	19%	5,106,000

*NAICS 621, excluding Home Health Care Services

**Assumes 250 SF per job

Source: EMSI, Camoin Associates

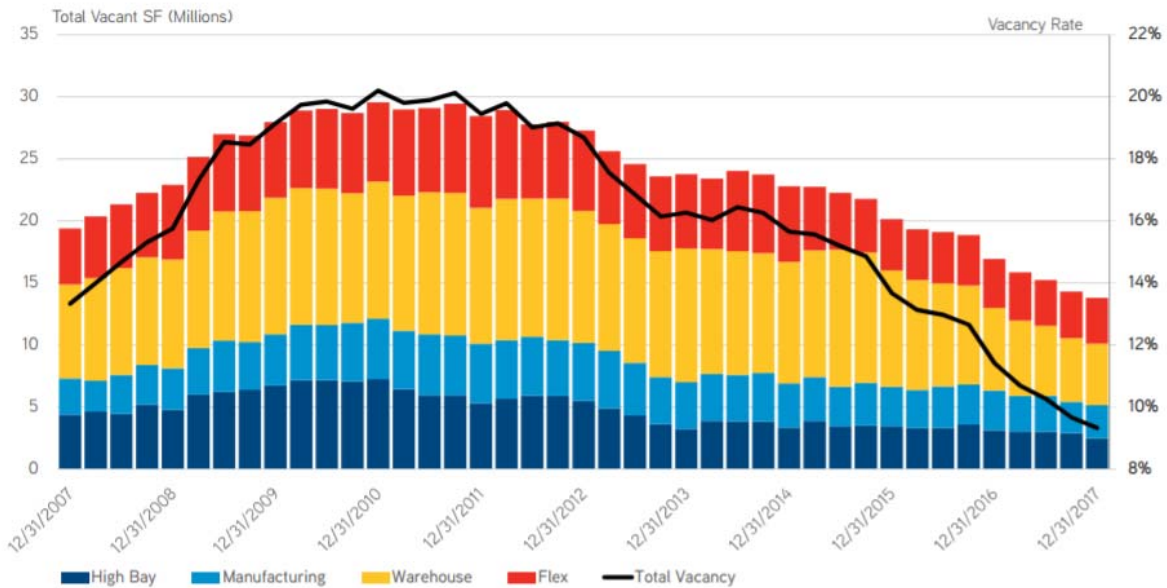
⁵ 2018 Healthcare Marketplace. U.S. Research Report. Colliers.

INDUSTRIAL

The Boston industrial market remains on a hot streak, with absorption of nearly three million square feet of space in 2017 and downward trending vacancies. According to Colliers, market-wide industrial vacancy stands at 9.3%, down 2.1 percentage points year-over-year. As a result, rents are rising rapidly, surpassing \$7.00 (NNN) on average for the first time, a 13.9% increase over last year. While the development pipeline is significant, developers have shown restraint when it comes to spec construction, suggesting stable fundamentals into the future.⁶

Of the industrial product types (flex, manufacturing, warehouse/distribution), the latter has performed the best; the majority of industrial leases signed in Q4 2017 were for warehouse and distribution space. Positive absorption in this category more than compensated for slight negative absorption in the other industrial product types. According to JLL, heightened market activity in warehousing/distribution aligns with trends seen nationally as demand for last-mile distribution continues to rise, particularly in urban areas.⁷ Last-mile distribution refers to the capacity to deliver products ordered online to consumers' homes.

Figure 3: Vacancy by Space Type, Boston Metro, Q4 2017



Source: Colliers International

Newton has a small amount of commercially tracked industrial space, about 200,000 square feet, all of which is Class B and C space located in the Newton Corner/Nonantum area.⁸ This space accounts for just 6% of industrial space in the Rt. 128/Mass Pike submarket, compared to the city's 15% share of submarket office space. Despite the strength of the industrial market regionally, opportunities for industrial space development in Newton are limited due to land availability constraints, as well as high land costs that do not justify comparatively low-value types of development.

⁶ Colliers International. Greater Boston Industrial Viewpoint Q4 2017.

⁷ JLL. Boston Industrial Insight. Q4 2017.

⁸ Data provided by JLL

RETAIL

As online shopping volume continues to grow, retail disruption is happening quickly. Increasingly, virtual and physical presence are finding synergy rather than competition, and one of the major themes of 2017 was the rapid convergence of online and brick and mortar sales. A number of formerly online-only retailers are starting to see that a brick and mortar presence can be an integral part of their omni-channel and consumer experience.⁹

In order to maximize the benefits of this model, retailers have been working to reposition stores, close unproductive units and improve their mobile apps so that people can shop from their phones anywhere—even in the store itself. The omni-channel approach is also causing some retailers to rethink their footprint and number of locations in areas where the real estate is expensive. Many of these companies are choosing to have a single well-located store. Encouraging customers to shop online also means that retailers can keep less on-site storage, further reducing their footprints.

The move towards experiential retail has had the most influence on a reimagined tenant mix. The sectors that have seen the most growth in recent quarters are fitness, food, entertainment, and service. Gyms were historically viewed as undesirable users, to the point where many leases prohibited them, along with tenants like adult shops and gambling halls. However, the big box gym has now come to be seen as a desirable anchor that can drive traffic in non-peak hours and provide landlords with recognizable brand-name tenants with solid business models. The success of traditional big box gyms has spawned an explosion in recent years of boutique fitness studios. Yoga, Pilates, and spin studios were the trailblazers of this segments, while newcomers include dance workouts, personalized group training, and boxing.

Entertainment concepts are also backfilling a lot of second-generation box retail, after overcoming similar resistance as the fitness sector. Growth and evolution of traditional uses are also being seen here. Those properties with clear heights of at least 17' are ideal for trampoline parks, and tenants like Sky Zone, Launch, and Altitude have taken spaces anywhere from 20,000 to 40,000 square feet. Round1 features specialty arcade games, bowling, ping pong, and karaoke, and specialized concepts like axe-throwing, Top Golf, glow-in-the-dark mini golf and bowling, and indoor "micro" amusement parks have also been looking to grow their footprints in Massachusetts.

Much of the retail development currently in the pipeline in the Boston suburbs is planned as part of mixed-use development. Notable examples include grocery-anchored projects with high-end apartments or townhouses like the Merc in Waltham. Traditional enclosed malls are continuing to struggle, as consumers make their preferences for these mixed-use centers known. While the retail sector disruption remains ongoing, it does not necessarily mean death; it means evolution.

The core retail markets inside and along Route 128 have seen record-setting rents as of late, and are expected to remain steady. In this area, average rents of \$50-\$55 per square foot NNN¹⁰ for small shop space and \$25-\$30 per square foot NNN for larger spaces are common. For every operator that comes into this area aggressively but cannot sustain sales sufficient to cover high rents, there are strong tenants ready to backfill that space. Recent successful retail developments in Newton include The Street Chestnut Hill and Newton Nexus.

In non-core markets where tenant demand has cooled, there will be a continued effort by landlords, developers, and lenders to reposition and repurpose assets. Dated, lower quality, and less desirable properties will need to transition from traditional retail to a focus on experiential categories like fitness, food, and entertainment.

⁹ CBRE/New England 2018 Market Outlook

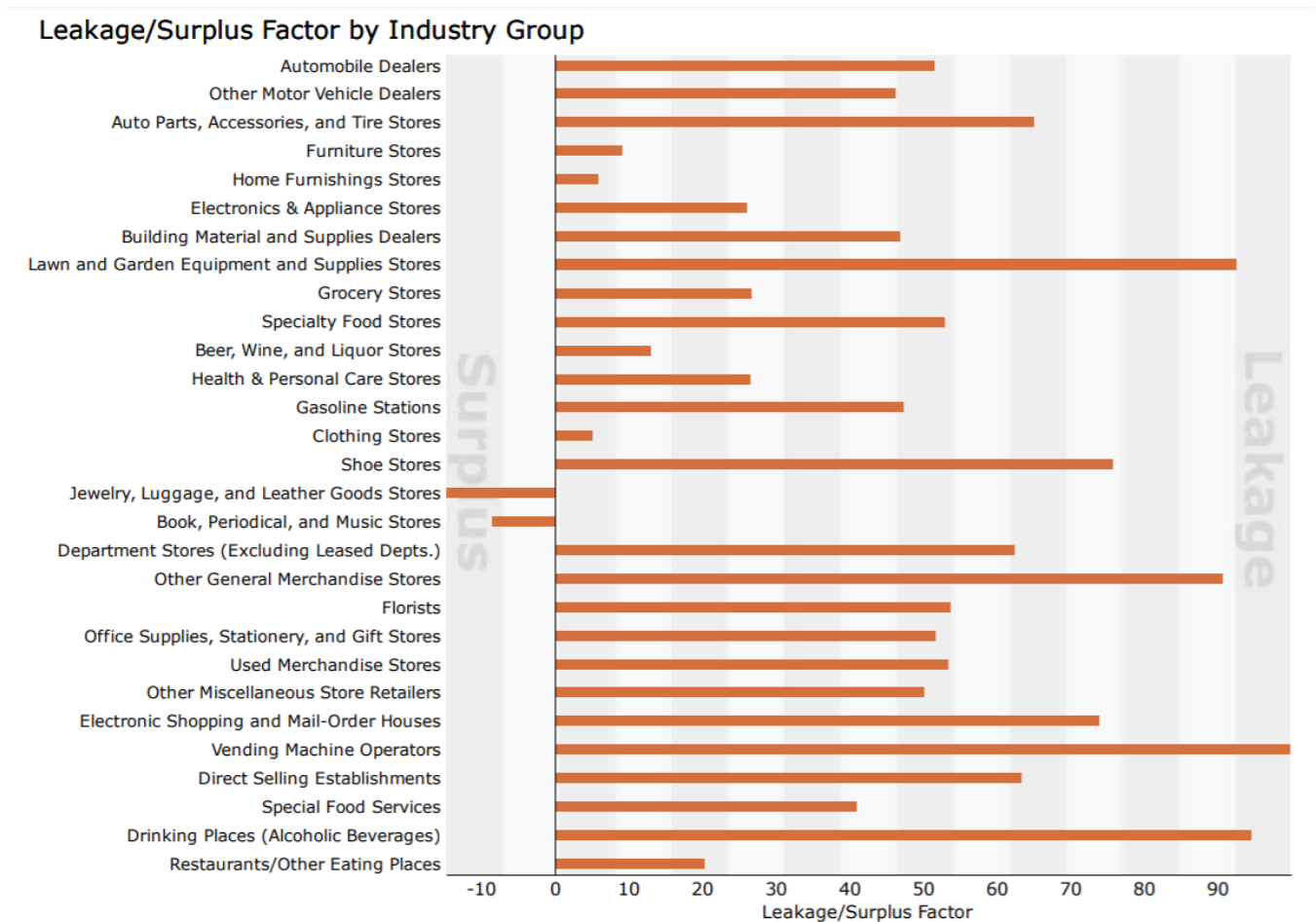
¹⁰ NNN, or "triple net," refers to a lease arrangement where the tenant is responsible for property taxes, maintenance, and insurance expenses, beyond the base rent amount

Retail Gap & Potential Analysis

In a retail gap analysis, the existing retail sales (“supply”) of trade area businesses are compared to the estimated retail spending of trade area residents (“demand”). For this analysis, the trade area is defined as the City of Newton. The difference between demand and supply is referred to as the retail gap. The retail gap can be positive or negative. Note that existing retail sales are specific to the defined trade area whereas retail spending is an estimate of gross spending by residents living in the trade area regardless of where the retail spending occurs.

When the demand (spending by trade area residents) for goods and services is greater than sales at trade area businesses, sales are said to “leak out” of the trade area creating a positive retail gap (i.e. sales leakage). Conversely, if the supply of goods sold (local trade area sales) exceeds trade area demand (spending by trade area residents), it is assumed that non-residents are coming into the trade area and spending money, creating a negative retail gap (i.e. sales surplus). Figure 4 illustrates the leakage and surplus factor by retail category for the city.¹¹ Almost every category shows sales leakage. This means that Newton residents are leaving the city to make many of their retail purchases.

Figure 4: Retail Leakage/Surplus Factor by Retail Category, City of Newton



Source: Esri

¹¹ The Leakage/Surplus Factor presents a snapshot of retail opportunity. This is a measure of the relationship between supply and demand that ranges from +100 (total leakage) to -100 (total surplus). A positive value represents 'leakage' of retail opportunity outside the trade area. A negative value represents a surplus of retail sales, a market where customers are drawn in from outside the trade area.

Sales leakage and sales surplus carry different implications. In many cases, sales leakage presents an opportunity to capture unmet demand in a trade area since a percentage of residential spending occurs outside the trade area. This demand can be met within the trade area by opening new businesses or expanding existing businesses within retail sectors that show sales leakage. However, not all retail categories that exhibit sales leakage within a particular trade area are a good fit for the region.

A sales surplus might exist for several reasons. For example, the region might be a popular shopping destination for tourists and other out-of-towners, or a cluster of competing businesses offering a similar product or service may be located within the trade area, creating a specialty cluster that draws in spending by households from outside the trade area. Alternatively, a sales surplus could be an indicator of market saturation.

Sales leakage of retail categories in Newton was compared to average sales of similar business in the Boston MSA. This allows us to identify which industries with sales leakage may have enough unmet demand to warrant opening a new store or expanding existing stores. Additionally, the amount of supportable square foot is provided based on average sales per square foot for each retail category.

Table 7 identifies the number of new businesses that theoretically, could be supported in Newton assuming:

1. 10% of the sales leakage is recaptured (this is typical among various retail categories), and
2. New businesses have sales comparable to the average sales of all Boston MSA businesses in the same retail category.

Table 7: Supportable Retail, City of Newton

Supportable Retail, City of Newton							
A	B	C	D	E	F	G	H
NAICS	Retail Category	Retail Gap	10% Leakage Recapture	Average Sales per Business	Supportable Businesses (D / E)	Average Sales per SF	Supportable SF (D / G)
7225	Restaurants/Other Eating Places	\$ 83,449,535	\$ 8,344,954	\$ 746,006	11	\$ 350	23,843
4451	Grocery Stores	\$ 161,505,222	\$ 16,150,522	\$ 4,707,055	3	\$ 500	32,301
4441	Bldg Material & Supplies Dealers	\$ 93,157,657	\$ 9,315,766	\$ 3,092,156	3	\$ 350	26,616
4539	Other Miscellaneous Store Retailers	\$ 31,093,473	\$ 3,109,347	\$ 845,926	3	\$ 300	10,364
4461	Health & Personal Care Stores	\$ 63,062,722	\$ 6,306,272	\$ 2,991,827	2	\$ 400	15,766
4529	Other General Merchandise Stores	\$ 78,144,980	\$ 7,814,498	\$ 3,628,365	2	\$ 500	15,629
4511	Sporting Goods & Hobby Stores	\$ 29,405,729	\$ 2,940,573	\$ 1,418,317	2	\$ 250	11,762
4413	Auto Parts, Accessories & Tire Stores	\$ 29,597,557	\$ 2,959,756	\$ 1,003,741	2	\$ 300	9,866
4532	Office Supplies, Stationery & Gift Stores	\$ 21,554,300	\$ 2,155,430	\$ 1,024,969	2	\$ 300	7,185
4521	Department Stores	\$ 161,061,631	\$ 16,106,163	\$ 15,157,405	1	\$ 250	64,425
4431	Electronics & Appliance Stores	\$ 42,772,212	\$ 4,277,221	\$ 2,147,270	1	\$ 500	8,554
4482	Shoe Stores	\$ 18,297,880	\$ 1,829,788	\$ 1,376,101	1	\$ 300	6,099
7224	Drinking Places - Alcoholic Beverages	\$ 14,855,317	\$ 1,485,532	\$ 891,610	1	\$ 250	5,942
4442	Lawn & Garden Equip & Supply Stores	\$ 11,912,228	\$ 1,191,223	\$ 730,531	1	\$ 250	4,765
4452	Specialty Food Stores	\$ 11,675,260	\$ 1,167,526	\$ 823,975	1	\$ 350	3,336
4531	Florists	\$ 5,989,460	\$ 598,946	\$ 316,614	1	\$ 200	2,995
4533	Used Merchandise Stores	\$ 5,428,955	\$ 542,896	\$ 297,355	1	\$ 200	2,714
	Total				38		252,163

Source: Esri, Camoin Associates

The retail gap analysis shows that a substantial amount of retail spending is “leaking” out of Newton, with some degree of leakage in almost every retail category. Assuming 10% retail leakage recapture, upwards of 250,000 square feet of net new retail could be supported in the city. In particular, department stores and grocery stores stand out in terms of supportable square feet. In addition, at least 11 new restaurants could be supported.



Retail Space Affordability

Newton is undoubtedly a desirable destination for retailers due to its relatively high population density and very high disposable incomes. This attractiveness, however, comes with its challenges. Strong retail demand in Newton has put upward pressure on rents, making it difficult for small mom-and-pop shops to stay in the city. Retail rents that easily top \$30 or \$35 per square foot NNN¹² are often unaffordable to smaller retailers who do not have the sales volume to cover space costs. Interviews with local shop owners revealed mounting concerns about a potential exodus of these stores to more affordable communities, and the impacts of these relocations on the character of Newton and its villages.

HOTEL

Consumer preferences within the hotel industry are expanding from traditional hotels that merely offer a place to rest your head at night to establishments that aid travelers in developing experiences. Some of this change is attributed to the influx of millennials who, in comparison to previous population cohorts, such as baby boomers or Gen X, travel more and are more passionate about travel. They value communal spaces, digital connectivity and local design touches to broaden their travel experience.

The retail industry has capitalized on hotels with major retailers opening up branded hotels rich in experiences. This trend began over a decade ago when high-end fashion designers merged with hotels to create a completely shoppable hotels where hotel furnishings and décor are all available for purchase. Currently the high-end fashion hotel market includes rooms created by designers such as Versace, Fendi, Tommy Hilfiger, etc. in which customers can experience all senses of the brand in the highly curated spaces.

Williams-Sonoma plans to open branded hotels starting in late 2018 in Charlotte, North Carolina; Detroit, Michigan; Indianapolis, Indiana; Oakland, California; Minneapolis, Minnesota; Savannah, Georgia; and Portland, Maine. This expansion from home retailer to hotel curator allows the brand to connect with customers during out-of-town visits.¹³ West Elm, a Williams-Sonoma brand, aims to create hotels that reflect the mood of its host city while combining an opportunity for customers to interact with West Elm products in an intimate, non-manufactured setting.

Additionally, the hospitality industry has embraced the sharing economy through house sharing. Companies such as AirBnB, allow customers to gain access to entire homes, lofts, and even boats. These accommodations offer a local experience unparalleled to that of a traditional hotel and can sometimes be a fraction of the cost. Despite the increase in supply of accommodations due to house sharing and boutique hotels, the hotel market remains strong.

When perusing accommodations, hotel customers may choose one establishment over another based on available features and amenities. Connectivity is considered a highly sought after amenity, both in terms of shared space and technology. Guests want fast and free Wi-Fi along with charging ports in common areas. Hotels are incorporating communal spaces where both guests and residents can be brought together in a collective setting. In terms of business traveler connectivity, typically larger properties are associated with amenities such as conference rooms and event spaces giving large hotel corporations a competitive advantage in the business traveler market.

Other sought-after amenities include spas, restaurants, and bars. The latest hotel trends suggest there is a movement towards luxury amenities such as in-room purifiers, branded amenity products as well as music and

¹² Based on LoopNet property listings

¹³ <http://www.retaildive.com/news/are-hotels-the-new-frontier-in-experiential-retail/505878/>

entertainment. Additionally, there has been a shift towards sustainability within hotels with features such as high efficiency lighting, energy management sensors, and towel/linen reuse programs.¹⁴

Location of hotel and motel establishments is driven by an area’s attractions. Guests want to be where the action is, in close proximity, and ideally within walking distance of restaurants, shopping, and other recreational amenities. The industry also targets locations with emerging millennial populations as a signal of popular destination locations. In general, accessibility through robust transportation infrastructure as well as close proximity to employment centers, universities, and other visitor attractions is critical to success.

Greater Boston Hotel Trends

The Greater Boston hotel market has been historically strong, bolstered by strong business and leisure segments. In the Boston suburbs, demand has increased steadily since 2009 despite a slight dip in 2016. However, growth in supply continues to outpace demand, indicating the need for additional rooms will be limited over the short term.

New supply in the Newton area includes three hotels recently completed or under development in Waltham: a 138-room Hampton Inn, a 100-room Residence Inn, and a 90-room Fairfield Inn. Other nearby developments include a Residence Inn and a boutique-style Archer Hotel in Burlington, and a Courtyard Marriott in Westwood. Three major hotels currently exist in Newton, comprising 891 rooms:

- Hotel Indigo Boston–Newton Riverside – 191 rooms
- Boston Marriott Newton – 430 rooms
- Crowne Plaza Boston–Newton – 270 rooms

According to projections from Pinnacle Advisory Group, occupancy and revenue per annual room (RevPAR) in the Boston suburbs will decline slightly through 2018 despite an increase in average daily rates (ADR).¹⁵ See Table 8.

Table 8: Suburban Boston Hotel Performance Projections

Suburban Boston Hotel Performance Projections			
	2017	2018	Pct. Change
Occupancy	68.50%	67.00%	-2.2%
Average Daily Rate (ADR)	\$ 140.50	\$ 142.50	1.4%
Revenue per Available Room (RevPAR)	\$ 96.24	\$ 95.48	-0.8%

Source: Pinnacle Advisory Group

Sluggish office and lab space development in Newton compared to nearby suburbs will likely translate to somewhat flat demand for hotel rooms in the city over the short term, and therefore limited demand for any sizeable hotel development. However, the niche boutique hotel market may present opportunities if a substantially differentiated product can be offered that responds to trends in consumer preferences.

¹⁴ American Hotel & Lodging Association

¹⁵ 2018 Hotel Outlook. Pinnacle Advisory Group.

RESIDENTIAL

The City of Newton recently commissioned a Housing Needs Analysis that lays out strategies for addressing the city's current and projected housing needs. Key findings as presented in the Housing Needs Analysis include the following:¹⁶

- Newton's population is aging, and seniors will be a key driver of housing demand into the future.
- Newton is particularly attractive to families with school-age children, especially older-parent families, who seek to take advantage of the city's high-quality school system.
- The young adult population in the city, those between 25 and 45, has declined, and has done so at a faster rate than in the surrounding region.
- Housing diversity is limited, with multifamily units accounting for only 8% of the total housing stock.
- Approximately 31% of all new housing development since 2005 has been multifamily units, but this has not made a significant dent in the overall housing type and price mix.
- The relatively low level of development activity is not having a substantial impact on the variety of housing types or prices in the city. All new development since 2005 that was not accomplished through a public-private partnership has focused exclusively on the high-end market (200% of area median income and up).
- The Housing Needs Analysis cites a projection from MAPC of 1,900 new households in Newton between 2010 and 2030, based on a status quo population scenario. Between 2010 and 2017 the City gained approximately 1,100 households. This status quo scenario assumes the continuation of current rates of birth, death, migration, and housing occupancy.

The findings of the analysis point to an urgent need for significant multifamily housing construction in the city that can help to increase supply and stabilize soaring prices. Moreover, development of affordable multifamily housing is critical for general economic development within the city. As revealed in interviews with a variety of stakeholders, in order to successfully attract and retain large employers, the city will require a housing stock that is accessible to a diverse workforce, in terms of both age and income. Employers want access to talent, and if the talent cannot afford to live in Newton, business attraction efforts will continue to be hampered.

¹⁶ Housing Needs Analysis and Strategic Recommendations - City of Newton, Massachusetts. RKG Associates, Inc. June 2016.