The 2025 Boston Area Real Estate Development Outlook – *Featuring opinions from Doug Manz, Board President of the NAIOP MA and Partner and Chief Investment Officer of the HYM Investment Group and Adelaide Grady, Board Member of the NAIOP MA and Partner and Senior Vice President of Leggat McCall Properties.*

By Jaron J. Frieden – Director, The Vertex Companies, LLC, December 11, 2024

As 2024 sunsets and we await the sunrise of 2025, what can the development community reasonably expect given the change in political leadership and the litany of twists and turns that our economy has endured since 2020, when the world seemingly changed forever? I have been working at the Vertex Companies, LLC (VERTEX) since 1996 and, like most reading this article, have seen several real estate cycles. It has been crucial, particularly during times of uncertainty, to work as a trusted development team member to strategize and execute on environmental, construction and engineering challenges on some of the largest developments in Boston. We are always interested to talk with our clients to understand their strategy, business challenges, and their outlooks, as it makes us a better consultant. This article will feature some of our observations, but more importantly, the perspectives of two prominent developers in the Boston area, Doug Manz, President of the NAIOP Boston Chapter and Partner and Chief Investment Officer of the HYM Investment Group as well as Adelaide Grady, Partner and Senior Vice President of Leggat McCall Properties.

Like most real estate cycles, toward the end of the last real estate run, every development and acquisition deal appeared to fit into a very large box. Then that box began to shrink rapidly, and most deals that progressed required some serious strategy and creative thinking to execute. Although client sentiment is on the rise for 2025, creativity and sticking to sound investment principals seems to be the go forward plan. Market trends locally have certainly been shifting and developers need to continuously adapt, according to Mr. Manz, "*HYM sees the greatest areas of opportunity to be in rental housing, seniors housing and office to residential conversions. We think there are opportunities in distressed assets and have consistently been seeing more of those. Additionally, the Commonwealth's MBTA Communities Act as of right zoned land is creating new opportunities, and we are seeing that cities with struggling commercial properties (office and retail) are more willing to find ways to repurpose those. There is very little activity in office or life science due to oversupply.*" Ms. Grady adds "*The millennials who drove demand for highly amenitized, Class A buildings when they were in their 20s are now in their 30s and ready to move up to more space, direct outdoor access, and natural surroundings. While the big guys will continue to deliver high density product in large-scale developments in margin plays, there will be opportunity for* *value creators to deliver a more boutique, private space-forward product catering to a more discerning renter-by-choice (or renter-by-force due to lack of homes on the market)*.

The Federal Open Market Committee meetings, once watched and discussed by the few, have now drawn the interest of many. Interest rates have become a regular topic of conversation as we chat waiting for participants scrambling from other calls to join our respective Zoom or Teams project meetings. Ms. Grady indicates that *"2025 will continue the trend of interest rate challenges, particularly rates that are benchmarked to long-term rates, which were deflated through the 20-teens because of quantitative easing. Short-term rates may reverse their downward trend if the next administration's inflationary tariff plans are implemented, since the Fed has only a blunt instrument to combat it: the fed funds rate. In an imaginary world where rates are not a factor, our region's supply and demand imbalance in rental housing would continue to drive up rents, particularly in the inner suburbs and outer urban areas. However, the 20-25% value adjustment in multifamily real estate that occurred in mid-late 2022, when cap rates adjusted from 4% to 5% for stabilized product, can't be overcome with the kind of rent growth the market has seen since then. Low-basis product will continue to be what pencils, as investor return expectations will remain high as long as strong risk-adjusted returns continue to be available in other investment types."* Mr. Manz suggests that "*It is hard for us to judge at this point in time what effect the new Presidential administration will have on interest rates, inflation and new policies in 2025. With that said, we do anticipate interest rates to continue to come down, though likely not to pre-2022 rates, and we expect inflation to moderate, both of which are positive for real estate development. The demand for new housing in Massachusetts, particularly Greater Boston, exists, and if the cost for capital comes down that will help to get new buildings in the ground."*

Affordable housing demand continues to dominate politics and news cycles. Figuring out the answer was once akin to solving a Rubic's Cube and is now as complicated as mining cryptocurrency. According to Ms. Grady, "*The issue is more about how to afford producing these units than it is about demand for the units, as the demand is basically insatiable. The increasing percentages required to be incorporated into projects is contributing to the general infeasibility of most urban multifamily development projects today. In the suburbs, the issue is mitigated somewhat by the strong increase in area median incomes over the recent inflation years, which has driven up the 80% AMI rents such that value diminution of affordable units isn't as substantial as it has been in previous years. In Boston and other cities with 20% inclusionary requirements, the spread between the inclusionary rents and market rents is wide, rendering these projects infeasible. As the saying goes, 20% of zero is zero; we need to find other solutions to the housing affordability problem than burdening new* *housing development with the policy failures of the past."* According to Mr. Manz, "*We believe the demand for affordable housing must be met through the material increase in production of housing in general. Across all of our projects, we comply with each community's affordable and inclusionary housing regulations. We're very concerned that some communities are seeking percentages of affordable housing that make projects wholly unable to finance and build. We are looking at creative ways to team up with M/WBE's who specialize in affordable housing for projects next to or near our developments, as creating 20% affordable on site does not pencil out."*

Given the economic challenges, it is more important than ever that there is strong collaboration between public and private entities to achieve common goals. Public-Private Partnership development projects (P3) may potentially offer a solution that works for both the private and public sector. According to Mr. Manz, "*Partnerships with cities, states, and universities are critically important and create an ability to make land developable. Numbers are very tight and challenging currently in real estate development, and partnering with a city or State through land grants or programs can help make projects pencil out where otherwise it would not be possible."* Ms. Grady provides a unique perspective, *"As a party to a major public-private partnership for the redevelopment of the Bunker Hill Housing development in Charlestown, I see the success of these projects as being highly dependent upon the collaborative spirit of the partnership. True collaboration that builds trust between the parties takes dedication, transparency, and collective purpose. And while these are usually very long roads, they can result in truly transformative projects that leverage the private sector to achieve public policy goals. This type of P3 project is rare; if more municipalities and public agencies were to approach housing and revitalization initiatives in this way, as opposed to piling on public benefit demands through the zoning and entitlement process, I am certain better outcomes for public entities and developers alike could be achieved. Separately, we will likely see more P3 student housing projects that use partnership for the purpose of financial engineering and dedicated demand, but these will likely be accomplished by national student housing players."*

While VERTEX's Project Advisory and Owner's Project Management practice area demand has unsurprisingly softened with fewer construction starts, VERTEX's Construction Claims, Disputes and Forensics consulting practice area has seen tremendous growth from distressed construction projects. Some general contractors have run into labor, schedule and cost control issues that have resulted in delay and construction defect claims. In some cases, there have been bond defaults which have required VERTEX to complete the projects on behalf of the surety company. Distressed real estate matters are on the rise as well. If buildings sit vacant, modifications to life safety systems may provide cost savings and there can be indoor air quality issues or other matters to contend with before they can be occupied safely.

VERTEX has also seen a rise in claim and litigation matters where expert services are needed on behalf of the developers and/or general contractor defense teams regarding condominium board Statute of Repose construction claims. Mr. Manz is aware of this trend as it affects HYM's investment strategies *"We are seeing that more people would like to buy than rent, but in Massachusetts we lack sufficient for sale and ownership production, and we don't think that's changing any time soon. It's more difficult to build a large scale for sale projects than it has been for rental housing. An area we are trying to think about more is how to bring more for sale product to the market, but there is limited interest from equity partners and a higher risk associated with it, particularly given the 6-year Statute of Limitations on Construction Defects."* Mr. Manz adds, *"We are looking at distressed assets, where we can acquire things below value and potential value add type of acquisitions. We are always looking for opportunities for ground-up development in transit-orient locations, as we see that's where the strongest demand is."*

In this time of uncertainty, one thing is for certain, most of us have been through numerous real estate cycles that present unique challenges and have the experience to navigate these choppy seas until conditions improve. We will strategize and critically think about the financial, construction, engineering, and environmental challenges on each deal while we climb out of the proverbial box and build a new one as we progress into the next upward trend. We collectively thank NAIOP for providing the leadership and platform for us to collaborate, learn and influence positive outcomes for the future of our communities, businesses and careers.

ABOUT THE AUTHOR AND CONTRIBUTORS

Jaron Frieden, Director, The Vertex Companies, LLC | Jaron Frieden has worked at VERTEX since 1996 and is the Director of Growth Strategy. In this position, Mr. Frieden works closely with the Chief Revenue Officer, focusing on growth strategy including organic and acquisitive growth for all of VERTEX's Practice Areas including Compliance & Regulatory, Forensics, and Project Advisory business sectors. Due to VERTEX's diverse service offerings, Mr. Frieden educates clients and colleagues on the benefits of maximizing our Environmental, Construction Management, Engineering, Litigation Support and Insurance Services and is well versed in the execution of those services. As with all of the senior leadership at VERTEX, Mr. Frieden continues to stay involved in complex projects to ensure their delivery and that

VERTEX's clients are delighted, not just satisfied, with our strategic and value add consulting services.

Doug Manz, Board President of the NAIOP MA and Partner and Chief Investment Officer of the HYM Investment Group | Douglas J. Manz is a Partner and the Chief Investment Officer at The HYM Investment Group, LLC. Mr. Manz is responsible for leading HYM's development teams in the advancement of over twenty (20) million square feet of mixed-use development in Greater Boston, including Bulfinch Crossing (Government Center Garage Redevelopment) and Suffolk Downs.

In 2019, Mr. Manz was appointed to and currently serves on the NAIOP Massachusetts Board of Directors, NAIOP's Government Affairs Committee, A Better City's Land Use and Development Advisory Committee and is also a member of ULI. In 2013, Mr. Manz was appointed to and served on the City of Cambridge Transportation Advisory Committee for four years. Mr. Manz is a graduate of Cornell University and the Harvard University School of Design.

Adelaide Grady, Board Member of the NAIOP MA and Partner and Senior Vice President of Leggat McCall Properties | As a Senior Vice President, Addie is responsible for the firm's multifamily and mixed-use investments. Over the course of her career, she has been responsible for nearly $1B in multifamily ground-up development activity in the Boston market, performing all aspects of the development process including sourcing, permitting, financing, design and construction oversight, marketing and leasing oversight, and disposition. Addie is a graduate of the University of Michigan and Brown University.

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