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Another Victim of the Bubble: Office Building Prices Decline

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The tech wreck is crunching the price of office buildings.

In suburban Denver's high-tech corridor, Merrill Lynch & Co. has on the block a sparkling, but empty, office campus for $53 million, or $125 a square foot -- way below what it would cost to replace it.

The New York financial-services giant vacated the 66-acre campus in Meridian, Colo., in June. So far, though, no takers -- even at that bargain price. A Merrill spokeswoman declines to comment.

The asking price, along with a few recent sales, has local brokers wondering where the bottom is. "We've been asking ourselves that for two years," says Peter Savoie, a broker in the Denver office of Cushman & Wakefield Inc., the New York real-estate services firm.

Office buildings in the hardest-hit markets are going for bargain-basement prices as beleaguered tech companies and other owners are selling off their once-crowded, now-empty campuses. For the brave few willing to wade into the most distressed markets, a few properties are going for deep discounts to replacement costs -- a big benchmark that signals that new development won't be economical anytime soon. The reason: buildings bought below replacement cost can be rented at cheaper rates than any new development.

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TODAY'S NEWS

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The ultralow prices may also be a sign that strapped corporate owners have stopped holding out for a rebound and are waving the white flag, says Brett R. Wilkerson, a director of Property & Portfolio Research Inc., a Boston real-estate research firm.

"There are alternate opinions out there about the future, and those with pessimistic expectations may be taking their losses," he says.

In suburban Boston, faltering telecom and Internet companies concentrated along famed tech corridor Route 128 and further west and north have left vacancies in some areas near 30%, local brokers say. That hurt struggling telecom-equipment maker Lucent Technologies Inc. when it sold a 500,000-square-foot complex in Marlboro this summer for $27.5 million, or about $55 a foot, a very low price.

Discount Property

Some recent office-property sales in troubled technology markets.

Owner	**Location**	**Buyer**	**Total Price** (in millions)	**Price Paid Per Sq. Ft.**
Lucent	Milpitas, Calif.	Westbrook Partners	$47	$135
Merrill Lynch	Meridian, Colo.	On the market	$53	$125*
Nortel	Santa Clara, Calif.	South Bay/Pacific Coast	$24	$65
Rhythm Netconnections	Englewood, Colo.	South Metro Fire Rescue	$5	$55
Lucent	Marlboro, Mass.	Gillespie & Co.	$28	$55

Sources: Real-estate brokers; the companies

**Asking price*

The price is about half of replacement cost and an even bigger discount to what the building would have fetched three years ago during market peaks, says Lisa Campoli, a senior managing director in the Boston office of Insignia/ESG, a New York real-estate services firm that wasn't involved in the sale.

The buyers were a group of local investors led by Gillespie & Co., of Concord, Mass. Ian Gillespie, a Gillespie principal, acknowledges that market demand is currently nil and unlikely to pick up anytime soon. But at this price, he adds, he isn't worried. "We can not lease a lick of space for five years and still make a ton of money," Mr. Gillespie says.

In a statement, Lucent, based in Murray Hill, N.J., said it was pleased with the outcome of the Marlboro sale and another one, which were "designed to reduce our overall cost structure and to make the most efficient use of our capital."

Back in the late 1980s and early 1990s, large chunks of the nation's office stock changed hands, after a huge amount of oversupply hit a sharp slowdown in demand for office space. Highly leveraged real-estate developers and speculators couldn't meet debt payments, and littered the landscape with foreclosures, see-through buildings and real-estate bankruptcies.

This time, the sellers have so far been mainly cash-strapped technology companies and other corporate users trying to get real estate off their balance sheets. But real-estate investors have watched nervously as the national office vacancy rate has jumped to 15.7% as of the third quarter, from recent lows of 7.9% in December 2000, and is expected to top 16% next year, according to Reis Inc., a New York real-estate research firm. That's not that far from a 1991 peak of 19.3%.

Ms. Campoli says that real-estate companies these days are better capitalized and have so far weathered the downturn without a serious threat to their ability to meet debt payments. But further deterioration could unleash a wave of selling by major property owners.

Now, bargain prices in tech markets and a general softening elsewhere have begun to drag down office-building prices generally. Nationally, the average price of office buildings in central business districts slipped 5.5% to $206.77 per square foot at the end of the second quarter, from their recent peak of $218.07 in the fourth quarter of 2000, according to National Real Estate Index, a San Francisco-based research firm.

And in the most-distressed markets, vulture investors are starting to swoop, tempted by motivated sellers.

In Santa Clara, Calif., the heart of Silicon Valley, local investors South Bay Development Co., based in Campbell, Calif., and San Francisco-based Pacific Coast Capital Partners LLC in August bought a 359,000-square-foot campus on 16 acres for $23.8 million. The $65-a-square-foot deal raised eyebrows because it was much less than what the seller, another struggling telecom giant, Nortel Networks Corp., Brampton, Ontario, was seeking just this summer and a third of what it might have fetched at the market's peak, according to local brokers.

Mark Regoli, executive vice president of South Bay, says his company bought the building with the understanding that it might not be able to lease it for three years.

A Nortel spokesman says the sale was part of the company's consolidation plan. "We're very happy with the outcome," he says.

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