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Market gets tighter for 1st-class office space

A Philadelphia real estate broker recently contacted Bill Gladstone looking for luxury office space in downtown Harrisburg.

Gladstone, a broker with The Bill Gladstone Group of NAI/CIR, had bad news for the company that was conducting a search for a law firm. All Gladstone had available was Class B+ office space, which doesn't have all the amenities of top-shelf office space such as floor-to-ceiling windows and elegant lobbies.

"If your business depends on downtown, you will make due until you find what you want," Gladstone said.

His experience isn't unique.

A lack of available luxury office space -- known as Class A space -- in downtown Harrisburg is sending potential tenants to the suburbs, commercial real estate observers say. The city's downtown core averages a vacancy rate of 2 percent or less for luxury space, which is considered extremely tight.

"In recent weeks, users have considered the suburban markets after tours of the downtown business district have left them with underwhelming options," said Thomas T. Posavec, vice president of Landmark Commercial Realty Inc. in Wormleysburg.

Posavec does a quarterly report on trends in the area market for office space.

"The market has done so well that what [prospective tenants] are left with are the crumbs and not the cream," he said.

That leaves possible tenants with the option of leasing less-desirable office space just to be downtown or looking elsewhere. Lately, Posavec sees renters locating a few minutes away from downtown, either elsewhere in the city or in suburban areas such as the West Shore and near Interstate 83 on the East Shore.

Instead of paying \$16.50 per square foot to lease Class B space downtown, they might decide to drive a short distance and get Class B+ or Class A- space for the same price.

Posavec said the city has vacant lots where new Class A office space can be built.

And buildings for sale are commanding a good price, he added, such as a Class B+ office building at 321 N. Front St. that sold for about \$520,000 in 2006 and is now on the market for more than \$800,000.

"We're seeing some serious appreciation downtown, but there's a point where the market is going to resist," Posavec said.

Gladstone said that while Class A space in the city is tight, demand isn't strong enough to push developers to build more. Land in the suburbs for a building might cost \$150,000 to \$200,000 an acre, but the same acre in the city runs \$750,000 up to \$2 million.

"Demand is there but not in the same quantity" as in 2005, when the 18-story Market Square Plaza opened and put about 125,000 square feet of new Class A space on the market. The building is now fully leased, but "that didn't happen in one year," Gladstone said.

The tight downtown market is contributing to the gradual expansion of the core downtown market to **midtown**, as well as commercial projects being developed on Cameron Street.

Harrisburg developers Powers & Associates is adding nearly 50,000 square feet of Class A office space as part of an office-retail complex in **midtown**. The building will be across from the former Evangelical Press building at Third and Reily streets that Powers is redeveloping into the **midtown** campus of Harrisburg Area Community College.

Powers is asking \$19.49 to \$22.49 per square foot. Tom Powers, president of the firm, expects some of the office space will go to institutional users with relationships to HACC, while the rest will be professional office firms. He expects the building to be fully leased by the time it is ready for occupancy in late 2008.

Another 105,000 square feet of Class A space will go on the market at Capitol View Commerce Center at 1000 N. Cameron St. The space is listed during construction for \$13.75 per square foot, including utilities.

Greg Rothman, president and CEO of RSR Realtors, said RSR has letters of intent from lease prospects for 30,000 square feet.

Property Management Inc. of Lemoyne manages Market Square Plaza as part of PMI's total inventory of about 240,000 square feet of downtown Class A office space.

Eric Kunkle, vice president of PMI, said the company has no Class A space available in the core downtown. He doesn't know of anyone with downtown luxury space to lease.

PMI's closest luxury space is on the East Shore off Union Deposit Road. The availability of downtown space managed by PMI is limited to Class B and Class B+, and even that is 92 percent occupied.

Kunkle said Mayor Stephen R. Reed's Southern Gateway project, which would use street improvements to extend downtown to underutilized land at the southern end of center city, would open more luxury space near downtown.

The proposed new federal courthouse also will "shake up" the office market, but the impact can't be clearly assessed until a final location is determined, Kunkle said.

The government is looking at two sites, one on Third Street and one on Second Street, for the courthouse.

Outside the city, the availability of office space is generally good. If anything, Kunkle said, available space on the West Shore exceeds demand, while the East Shore inventory is somewhat less.

Other than downtown Class A space, Gladstone sees little demand for new office space in the area. He expects an overall weakening in the area office market because the region has a lot of available space to absorb.

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