



# One of Nation's Largest Office Developers Braces as Demand for Space Slows

Boston Properties Says Companies 'Much More Cautious' in Committing to Long-Term Leases



Boston Properties expanded its portfolio in Seattle after finalizing a deal in May to acquire the downtown Madison Centre tower for \$730 million. (CoStar/Anthony Harle)

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CoStar News

July 27, 2022 | 3:05 P.M.

On the heels of its strongest leasing quarter since the onset of the pandemic, one of the nation's largest developers and office landlords is preparing for a downturn in demand as companies respond to mounting economic uncertainty by pulling back on long-term financial commitments.

Boston Properties said it signed more than 1.9 million square feet of leases across its portfolio in the second quarter, more than 160% of the leasing volume it reported in the first quarter and 140% higher than the developer's 10-year historical average for the period. CEO Owen Thomas said the leasing activity was a result of the return of in-person work as well as the ongoing flight to high-quality office space by companies.

Still, the landlord is braced for "headwinds" as economic conditions in the country and around the world worsen.

"The economic environment will have several impacts, and even though leasing activity has been very strong over the last few quarters, we anticipate headwinds, at least in the short term," Thomas told investors on the developer's earnings call Tuesday. "Business leaders are generally more reticent to make large capital allocation decisions such as a lease in an uncertain economic environment. We can't predict the depth or length of an economic slowdown, but we're positioning [Boston Properties] for relative success regardless of the economic trajectory."

In the face of inflation, rising capital costs, a tightened financing environment and soaring construction expenses, Boston Properties said it would continue to pursue its \$2.6 billion development pipeline but would be more selective about what it adds to it moving forward. The developer has already locked in its anticipated costs for the 11 office, life science and residential projects it has underway across the country, which will collectively add about 4.2 million square feet to its portfolio.

The developer has signed leases for about 1.1 million square feet of the non-residential projects in development.

The company, which touts itself as the largest publicly traded U.S. developer and office owner, reported revenue rose 8% to about \$774 million from the year-earlier period in the quarter ended June 30. Net income climbed to \$223 million from the year-earlier \$111.7 million.

## 'Less Urgency,' But Bright Spots

While Boston Properties tightens its belt in anticipation of an economic slowdown, it is trying to market space to companies doing the exact same thing.

Company President Doug Linde said conversations the developer has had with tenants have shifted in recent months from the return-to-work and space utilization to the pace of job growth or headcount reductions as actions such as the Federal Reserve's rate increases ripple through the economy.

"New lease transactions continue to move toward completion, and what's more telling is that none of our active lease negotiations have been scrapped," Linde said. "However, companies are much more cautious about what they're doing. There is less urgency to make new commitments since everyone is factoring in the impacts of a slowdown, their business performance and the reduced demand for space."

Even so, the landlord said a renewed push to get employees back to physical office space could help offset any abbreviated dips in leasing momentum and push occupancy rates across the company's office portfolio even higher.

The average vacancy rate across Boston Properties' office and life science portfolio was 10.5% as of June 30, down from 11.2% at year-end 2021. The national office vacancy rate now averages about 12.4%, according to CoStar data, a figure that has climbed over the past several months as demand for office space weakens.

Linde said that while the availability rate for office space across the country "continues to be very elevated," Boston Properties' portfolio of high-quality space has provided a crucial buffer for the landlord. The company's leasing volume over the past several quarters has subsequently risen, resulting in more than 6.3 million square feet of leases signed over the past year.

Another 975,000 square feet of deals have been signed but not yet included in Boston Properties' occupancy figures, and the developer said it is in negotiations with potential tenants for yet another 1.3 million square feet of space.

"We continue to feel really good about our portfolio position in each market," Linde said of improving office occupancy rates in cities such as San Francisco, Seattle, Boston and Los Angeles. "The high end, premier space is where the market holds up really well."

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