In the Marketplace

Why Commercial Real Estate in Maine is a Good (Great) Investment!

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"As prices for residential real estate throughout Maine and New England have either fallen or held steady over the past several years, commercial real estate, especially in the retail, office and development sectors continues to thrive. Those of us who sell or lease commercial/investment real estate in Maine, are often asked the questions "How is the market?", "Are you seeing a slowdown/softening of the market?", "How have the interest rates affected sales?" and so on. The truth of the matter is that commercial real estate in Maine, especially in Southern Maine, remains a good (great) investment for any and all who have chosen that route over the last 15+ years. I personally started selling commercial real estate in Portland in 1991. For the purposes of this article, I have chosen to highlight a number of different office and retail properties that have changed hands at least twice over the course of the last 10-15 years. These particular properties involved some fitup and investment by the owners, but relatively small in comparison to the gains that they realized by leasing up their properties and then eventually putting them back on the market. Some of these properties, I am aware of personally because I was involved in the sales and/or leasing. Some of them, I am just aware of from being in the marketplace and had no broker involvement on my part whatsoever. Typically, the owners realized a significant profit, even after considering their fitup costs, brokerage commissions, capital improvements and other costs associated with owning commercial real estate.

Some examples of sales:

- An approximate 25,000 SF Class B retail/office building in South Portland, Maine, was purchased by a client of mine in 1993, as a distressed property for $215,000. My client put quite a bit of tenant fitup into the space (in the vicinity of around $200,000); we leased up any remaining vacancies, with a combination of short term and long term in leases. He sold the building in 2000 for $1,200,000.00. That same building was sold again 2003 for $1,340,000.
- An approximate 95,000 SF retail center in South Portland was purchased in 1997 for $5,000,000. The owners were able to secure some long term credit tenants for the property; did a modest amount of fitup which the Landlord paid for and quite a lot of fitup paid for by the Tenants. This same property was sold in 2003, approximately 6 years later for $8,850,000.
- A Class A- office building of approximately 21,000 SF located on Commercial Street in Portland, was sold in 1991 for $1,100,000 and was re-sold in 2004 for $2,450,000.
- An example of a smaller multi use property on Washington Avenue in Portland, sold last year for $420,000.00. That property was sold twice before in 1995 for $60,000 and then again in 2001 for $150,000, with relatively minor investment by any of the owners into improving the property.

The selling price of a commercial property is typically determined by the value of the leases that are

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currently in place, as well as assigning a value to any vacant space. In the case where an owner/ user is the purchaser, the pricing may be determined based more on comparable selling prices per square foot, then in utilizing an income approach. Although we are not typically appraisers, commercial brokers are often given the task of determining the purchase price through an analysis and a Broker's Opinion of Value. Oftentimes, Buyers are looking to make a purchase based on a certain Capitalization Rate. A Capitalization Rate or Cap Rate is a ratio used to estimate the value of income producing properties.

The Cap Rate is determined by taking the Net Operating Income (NOI) and dividing it by the sales price. Quite simply, the Seller is trying to get the highest price for the property and sell at the lowest cap rate possible. The buyer is trying to purchase the property at the lowest prices possible which translates into a higher cap rate. The question is then, what makes these prices set forth above as examples, achievable by the Owners? What happens from the time they purchase a building and when they sell it for a profit? Usually, it is a function of the leasing of the building, typically handled by their broker. The Owner has been able to secure good tenants at increasingly higher lease rates which increases the NOI and thus increases the Selling Price. In addition, Buyers expectations for Cap Rates have been reduced over the past 5-10 years. That has come about as a result of credit-worthy tenants, strong long term leases, less risk, well positioned buildings, as well as comparable sales from the marketplace.

For this article, I have not included any properties which would be classified as development projects in which clients have purchased the land, taken it through the approval process, constructed it and then leased to tenants. Typically, because the risk is greater in that type of scenario, the reward can be greater as well. Real Estate development can have greater rewards but truthfully can often be daunting to those investors that haven't gone through that process.