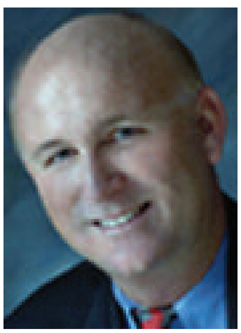
Lease Negotiations in a Down Market



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By Gregory P. Schenk, SIOR

In many areas around the country, the office market is experiencing its highest vacancy rate in years. What does this mean to brokers, tenants, and owners of commercial real estate? For brokers, it is a great time to brush up on skills in tenant representation to ensure that you are ready to help your clients realize the opportunities available to them.

When vacancies are high, the potential for greater savings for tenants increases. Opportunities include taking advantage of early lease renewals to relocation to space that is renting at below market rates. Commercial brokers, who solely represented landlords in the past, have seen that tenants have new opportunities to take advantage of changing market conditions to craft leases that are more favorable to them—with the help of a tenant rep broker and a good strategic plan that offers tenants increased savings. Savings can be achieved in areas such as discounted base rent, capping controllable operating expenses, generous build out allowances, free rent, and tax incentives.

Imperative to Know Your Market

Knowing the market, which includes knowing the landlords who can offer the best incentives, is imperative. Because build out expense has increased dramatically because of soaring costs for steel, cement, copper, and other building materials, knowing which buildings are ready to move into immediately and which ones need minor build out, is important and can help tenants save money. Agents need to study each building in the market area to determine which buildings can accommodate tenants with little improvements and which landlords/owners can and will cover the high cost of renovations.

The bottom line is that tenants have never had it so good! In many markets around the country, clients are experiencing savings of from 10 to 20 percent this past year; with no end in sight!

Getting the Best Deal When Negotiating a Lease

Landlords analyze potential leases on the following items: credit, amount of space available to lease, lease terms, and the cost to build out that space. What does the landlord/owner need to do in this down market? The landlord can begin by educating brokers and prospective tenants about their properties and the competitive edges that they offer. Are the buildings well managed, clean, well lit, secure, handicap accessible? Are the floor plans on CAD and easy to read? Is it easy to subdivide the space for various size requirements of tenants? Most cities have many tenants that have small space requirements and not as many that require larger office space, which again points to the importance of having space that can be subdivided. What kind of amenities does the building offer—shared conference rooms, Wi-Fi, plenty of parking for events, and cafes are among the most desired amenities.

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Evaluate Clients' Needs

It is always important to listen to clients' needs and goals to select a property that will best suit them. Easy-to-read floor plans and brochures are helpful to everyone in evaluating properties. Consider having an expert space planner work with the tenant to determine space needs.

Getting a floor plan priced out correctly and in a timely manner also is important. Knowing the permit process will help a great deal; many tenants procrastinate on relocation efforts and do not plan far enough in advance to allow for a thorough search and careful negotiations.

Lease negotiations in a down market are all about the credit of the tenant, learning about the tenant's short- and long-term goals, and educating them about the options and incentives available when the vacancy rates are high.

Brokers who are good at listening to their clients and who can put together a creative plan, will be successful in 2009 and beyond—even in a down market!

High Vacancy Benefit for Landlords

Even landlords can benefit to a certain extent in a high vacancy market. With a tenant who has good credit, landlords are able to refinance properties at low interest rates that are locked in for a longer period of time, or they can dispose of their higher-occupancy buildings to investors who are still looking for sound investment projects.