

How To Take Advantage Of The Best Commercial Real Estate Market For Tenants In The Last 20 Years

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THERE IS A CLEAR UPSIDE TO TODAY'S DOWN ECONOMY. COMMERCIAL TENANTS SHOULD BE ABLE TO SECURE LOWER RENTS AND BETTER LEASES THAN THEY HAVE IN YEARS.

Whether renewing a lease, seeking to renegotiate an existing lease or moving into a new space with a new landlord, the environment is right to gain lower rents, better terms, more concessions, and reduce overhead significantly.

To achieve these savings, you must handle negotiations smartly. You must do proper due diligence and negotiate firmly in order to gain the upper hand from landlords.

If a tenant new to a building gets a better deal than an existing tenant gets on a renewal, the renewing tenant left a lot of money on the table. As surprising as it may sound, renewing tenants routinely get shabbier treatment than new tenants.

Why?

A typical commercial landlord reaches out to its tenants approximately one to two years before the lease expiration date to renew the lease at a moderate increase, citing inflation, higher taxes and costs as standard policies. The landlord positions itself as compassionate, asking for only a moderate increase, giving the impression it has the upper hand and the tenants must agree to their terms.

Don't be fooled. Saying that space should be renewed at \$50 per square foot because the lease you signed ten years ago topped out at \$48 is as absurd as saying that AOL is worth

\$100 per share now because when you last bought it ten years ago you paid \$95.

Landlords rent to the market whether you are renewing a lease in your current building or moving from A to B. And now more than ever, tenants hold the power in these negotiations. The key is to understand how and why tenants have leverage and to then use this leverage effectively to secure a fair deal.

Here are some basic facts you need to know:

Fact one:

Landlords need to keep their buildings occupied. Day to day cash flow pays the bills and net operating income (rents minus expenses) determines what the building is worth whether an owner is selling or refinancing.

In today's economy, keeping tenants is more difficult than ever before. Companies going out of business or downsizing means they need less office space. This has forced commercial vacancy rates higher. For example, in Manhattan commercial vacancy rates have reached 10% Downtown and 14% Midtown.

Fact two:

Small companies matter. In major markets such as New York City, the average space user rents 5,000 square feet and the vast majority of

tenants rent spaces that are under 10,000 square feet. A common misconception is that landlords don't really care unless you are a large tenant. This is not true. These under 10,000 square foot tenants are the life blood of landlords. Mark Holiday, the CFO of SL Green, the largest owner of commercial real estate in NYC, has said publicly that as a landlord, his number one priority is retaining existing tenants of all sizes.

Fact three:

Losing an existing tenant is expensive. Landlords lose what amounts to approximately 18 months of rental income if a tenant (regardless of size) vacates its space. This is based on downtime, marketing costs, free rent to a new tenant, the cost of building out space and credit risk.

Really understanding how much money is on the table for landlords is crucial to tenants. This knowledge gives tenants power and leverage. Landlords need to keep buildings occupied at any reasonable cost, so tenants can and should demand – and get – better terms.

Fact four:

Getting a new tenant is expensive. New tenants typically receive several months or more free rent plus free build-outs by landlords eager for them to fill empty space. Smart tenants translate these costs into a specific dollar amount which is then used as the guideline for what a lease should cost whether in your current building or in a different building.

Once tenants clearly understand these basic facts they can truly capitalize on the fact that commercial rents have dropped over 40% in the last 18 months.

That said, tenants hate to move and landlords know this. So, convincing a landlord that you will move if you do not get the right deal is essential.

How do you do it?

If your lease is due to expire within one to two years, don't take your current landlord's lease renewal offer no matter how sweet it first appears. If your landlord keeps the rent stable or reduces it slightly and also offers to repaint and re-carpet your offices, interpret it as a signal there is a much better deal to be obtained. In most cases, a landlord's first offer is nowhere near its bottom line.

You or your intermediary must go through the process of looking at other space options in order to understand the market and secure the best deal. You must create doubt to entice the landlord to offer you terms to keep you. And, you might even find better space elsewhere.

The lease negotiation process is part dance and part dog fight. The right intermediary between you and the landlord makes it easier to leverage your power in the negotiation which will save you money now and for a long time to come. We're in the best commercial real estate market for tenants in the last 20 years. Take advantage of it.

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