

## **For owners of commercial real estate, patience and endurance needed are the traits most needed**

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The foliage tells us that fall is in full stride. Many companies are, or just have, completed their budgets for 2010. In virtually all cases, they are budgeting 2010 to be no better than 2009. I cannot disagree with their logic. 2009 has been a long slog and 2010 will be more of the same. So folks are hunkered down and simply trying to wait this one out.

The best description I have heard is from Rich Karlgaard, the Forbes columnist who suggests we will have a "VW" recovery. It will be a slow jobless process. The "VW" refers to some sector or individual company success. But overall the economic tides will not raise all boats. There is too much debt to be restructured, the consumer is hunkered down, the banks and other financial firms are a mixed report. Some are doing OK, on the mend, but several hundred banks are iffy. Manufacturing is still reeling. No one wants to be a doom and gloomer but the US is not going to lead the global economy out of this recession. Neither is Europe. The hope is that China, India and the Far East will be the little engine that can.

The Obama administration appears to have gotten distracted with the aggressive health care plan proposal and schedule. While the economy has stabilized, more or less, the predicted recovery beginning in Q-4 has not appeared yet.

What does all this mean for commercial real estate? The bottom line is that it takes jobs to fill space. Office vacancies are up and still rising. Retail is frozen and the latest data indicate a flat Christmas season. Restaurant sales are down. Hotel occupancies are down significantly. Warehousing is more or less steady, so far. But manufacturing is continuing a steady downward spiral. The US good producing sector lost another 116,000 jobs in September. Defense, which has been a bright spot, is now mixed. Given the stimulus spending and huge increases in debt, long term capital intensive defense projects are being delayed and/or cut back. War material for Iraq and Afghanistan is steady, but the troop levels are about 100,000+ in each theater. That is a lot of bullets and other ordinance, but not enough to ignite the manufacturing sector. That is not to say that the makers of drones, predators and road side bomb jammers are not flat out, but those are small niches and do not represent tens of thousands of jobs.

In New Hampshire we see vacancies in all categories of space. We see tenants renewing for less space and short terms. Until confidence returns along with a sustained recovery, real estate will languish. The gap between "bid and ask", what landlords are offering versus what tenants are will to pay, is large and getting larger each month. It is a tenant's market. Concessions are essential to keep and to capture tenants. The stress point is the caliber and financial strength of the tenant. Landlords do not want to risk significant fit up dollars, free rent and other concessions unless they can be confident that the prospective tenant will survive these concessions and then prosper.

Speaking of tenant fit up, a number of landlords do not have the cash on hand and their lines of

credit have been lowered due to the drop in real estate values. On a recent 16,000 s/f office requirement, we issued 15 RFPs. Seven landlords declined to respond as the fit up package was about \$400,000 or \$25 per s/f. But 8 landlords did propose and ultimately the tenant was able to secure an attractive rent, significant beneficial occupancy and above standard fit up.

How long will the correction go on? It is anyone's guess, but it will be several years at least. In the interim, tenants will need space and landlords will need tenants, so the mating dances will continue. Keep in mind that there is something on the order of \$3 trillion of excess liquidity that needs to be squeezed from the US economy. Consumers are saving (or paying down debt) and not spending. The consumer represented 70%± of the economy in 2007. Much of that was driven by refinancing of their homes and using home equity lines of credit as an ATM. Not now. Home values have softened and lenders are tightening credit lines so the consumer is on the side line for the foreseeable future. For owners of commercial real estate, patience and endurance are the traits most needed for the next year or two.

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