

# THE REAL DEAL

Commercial market report: Landlords dangle record amounts of free rent  
*Manhattan's office leasing market fails to keep momentum from previous months*

*By Adam Pincus*

The amount of free rent that landlords are offering to entice reluctant tenants to sign contracts has hit record levels in the current downturn, despite the fact that asking rents have started to stabilize in parts of the Manhattan leasing market.

In the third quarter, two Midtown leases were signed with 17 and 18 months of free rent -- double the average of eight and a half months, figures from the most recent report from commercial services firm CB Richard Ellis showed.

Some industry professionals said even longer rent-free periods were being negotiated.

Real estate attorney Jonathan Adelsberg, a partner with Herrick, Feinstein and co-chair of its commercial leasing department, said that while contracts with one year of free rent have become common during the downturn, in the last four months he's started seeing some deals with two years of free rent also being negotiated.

"For some landlords it may be advantageous to give more free rent [but] with a higher rent [per square foot]," he said.

The free rent was just one element of a soft Manhattan leasing market that saw a 1 percent decline in September asking rents. Those rents fell to \$50.78 from \$51.28 per square foot the month earlier, the CBRE data shows. Average asking rents are now down 29 percent from the peak of \$71.92 per square foot in July 2008.

The market was unable to keep up the momentum of August on several fronts. The volume of leasing declined by 19 percent in September, to 1.46 million square feet, from the month earlier. For the year, leasing volume dropped 21 percent, to 11.4 million square feet, CBRE data revealed.

Throughout Manhattan, the percentage of space available for leasing within the next 12 months, known as the availability rate, climbed to 14.2 percent in September from 14 percent the previous month, the figures said.

But at the same time, some parts of the market showed strength, and industry experts expressed very different viewpoints on the varied landscape.

Stephen Gordon, a senior managing director at PBS Real Estate, was skeptical that leases

Manhattan office stats		
Manhattan	Availability rate	Average asking rent
Sep '09	14.2%	\$50.78
Aug '09	14.0%	\$51.28
Midtown		
Sep '09	14.9%	\$57.88
Aug '09	14.8%	\$57.94
Midtown South		
Sep '09	14.8%	\$42.45
Aug '09	14.3%	\$42.68
Downtown		
Sep '09	11.8%	\$39.54
Aug '09	11.4%	\$40.20

Source:CBRichardEllis

with 24 months of free rent were actually being signed.

"I don't think that's out there," he said. But he saw an increase in activity, if not an increase in contracts signed.

"I've seen a greater return of the market to its typical velocity," he said. "[But] there are still outsize concession packages available from credit REITs [real estate investment trusts] and other stable owners."

On a positive note for landlords, four submarkets in Midtown showed increases in asking rents, including Park Avenue, which saw a \$0.28 per square foot jump, to \$64.08. It was the first time any Midtown submarket had seen an increase in asking rents since May, CBRE statistics showed.

Jay Smith, president of commercial brokerage Jay G. Smith, said asking rents in some Midtown buildings were rising, but that it was temporary.

"Now you have a flood of activity and landlords started raising their asking prices. When the smoke clears, there will be a lull again ... and then the prices will start coming down a little bit," he said.

Herrick, Feinstein's Adelsberg said he has not seen "any increases in rent," a fact he ties to weak employment levels.

The overall Manhattan office vacancy rate -- now at 11.1 percent, as measured by commercial services firm Cushman & Wakefield -- could climb to 16.3 percent if an additional 98,000 office workers lose their jobs, on top of the 74,000 jobs that have been shed through the third quarter.

But in a more moderate projection, the vacancy rate would rise only to 12.9 percent if an additional 21,000 jobs are lost, Cushman & Wakefield data showed.

"Until I see some actual hiring and expansion, I don't see rents going up," said tenant and landlord representative broker Grant Greenspan, a principal with the Kaufman Organization, and head of its leasing division.

## **Midtown**

Average asking rents and leasing activity slid modestly in September. Rents fell to \$57.88 from \$57.94 per square foot in the month earlier, and leasing velocity slipped to 1.15 million from 1.19 million square feet the month earlier, CBRE data showed.

The availability rate rose from 14.8 to 14.9 percent in September.

Michael Dubin, president of tenant and owner representative leasing services at landlord Savitt Partners, said the period of uncertainty in pricing had largely passed, but not to the

advantage of the landlord. He said there is a much smaller gap between what a landlord expects in rent and what a tenant is now willing to pay than there was just a few months ago.

But while activity has stepped up, "It hasn't increased to the point where I can sit back and say, 'Look Mr. Tenant, this is what we are offering; if you don't like it, that's okay.' Landlords aren't there yet," he said.

Cushman & Wakefield projects Class A office rents in Midtown will fall a bit further this year from \$67.64 per square foot, and remain flat at about \$63.50 per square foot from 2010 to 2012, before rising again in 2013.

The Park Avenue submarket fell the most in the city from September 2008 to 2009, falling 33.2 percent, from an asking rent of \$108.24 to \$72.33 per square foot, Cushman data showed.

### **Midtown South**

More square feet were signed in September than in August in Midtown South, the only market to see an improvement in Manhattan. Leasing velocity pushed up slightly, from 180,000 square feet in August to 210,000 square feet in September, the CBRE statistics showed.

But by other measurements, the market further weakened. The availability rate rose to 14.8 percent in September from 14.3 percent the month earlier, and average asking rents fell to \$42.45 per square foot in September from \$42.68 per square foot, CBRE data showed.

The availability rate in the Flatiron District, which has been rising all year, hit 19.7 percent in September, still the highest of any submarket in the city.

The tightest sector of Midtown South was Union Square, with an availability rate of 9.1 percent.

### **Downtown**

Leasing activity dropped sharply in September to 100,000 square feet leased, from 430,000 square feet leased the month before, the CBRE report said.

The lower activity pushed up the availability rate, which rose to 11.8 percent from 11.4 percent the month earlier, which is the lowest of the three Manhattan markets.

During the same period, average asking rents declined to \$39.54 from \$40.20 per square foot, CBRE reported.

Robert Goodman, senior managing director at FirstService Williams and a specialist on

the Downtown market, predicted trouble ahead for the area.

"I see more of a black cloud" hovering over Downtown because of large blocks of unneeded space that financial services firms have yet to put on the market, Goodman said.

But for "smaller and midsize users, if a landlord can come to the table quickly and assertively with [tenant improvements] and a reasonable amount of free rent, they will be able to secure a tenant," he said.

The World Financial District saw the largest submarket decline in asking rents Downtown compared with a year ago, Cushman statistics revealed.

The average price per square foot fell 23 percent, to \$47.53 in September 2009, from the same time the year before.