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Rents rising, more space available than ever, so what gives?

Austin Business Journal - by [Russell Young](#) Contributing writer

Business owners are wondering if and when to pull-the-trigger on expansion.

Central Texas remains one of the strongest regions in the country bucking job and economic growth numbers. Despite this, there's a tangible uneasiness about the local versus national economic picture.

In the span of two short years, slightly more than three million square feet of office real estate will pour into Austin. Recent reports show that substantially less office space was absorbed in the last quarter of 2007, raising questions about the consequences of even more space on the market, and what the implications of that may mean.

In 2003, when market rates were 35 to 100 percent lower, many businesses signed up for five year leases. Now, those businesses are facing a harsh new reality. The cost of new construction and investors' drive for returns on their purchases has made rents go way up on a percentage basis. This rise in cost may seem counterintuitive because absorption has stagnated in 2007. In the last quarter of 2007, some researchers show only 65,950 square feet was absorbed across town, down nearly 75 percent from last year.

Why are businesses not absorbing more space? Rising rates is one reason. Not only are companies facing increased rental rates, they also have the cost of relocation and potential build-out. For now, there's little financial advantage to make any unnecessary moves. A general uneasiness about the economy, the rise in rates in the face of lower absorption and the onslaught of space are putting businesses in a holding pattern.

There are strategic moves and opportunities available for both renewing and relocating companies. For renewing companies, executives should realize that landlords are keenly aware of the new space coming onto the market. For them, it's new competition for tenants. Keeping tenants is generally less expensive for a landlord than replacing them. With the time lapse between the market and the economy, businesses will likely find points of leverage and concessions to be gained by staying put.

Businesses looking for new space will likely find landlords pushing for high rates, but may be willing to offer key types of concessions, including free rent, expansion and/or contraction rights, and other "non-economic" concessions. These concessions can provide tenants with real asset-value and allow them to benefit in other ways from the higher per-square-foot price tag.

For landlords, rent is the hot-button issue because it's the core of how they assess the value of their building. As we move into 2008, at a cap rate of 7.5 percent, every dollar of rent paid by a tenant equals a 13.3-times multiple in value for the building owner.

Tenants need to evaluate the long-term implications of their office space in relation to their business model. Leasing simply based on price-per-square-foot negates other key strategic concessions that provide value. As always, businesses need think about the worst- and best-case scenario as we head into an election year and potentially slower economic times. As the year progresses, rates are likely to soften and concessions will be more prevalent. Third and fourth quarter will be a key turning point.

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