

Blend and Extend

BY BERT ROSENBLATT AND ANDREW STEIN

SO YOU SIGNED YOUR OFFICE LEASE AT THE TOP OF THE MARKET, YOU'RE PAYING A SMALL FORTUNE IN RENT, BUT YOUR SPACE IS ONLY WORTH A FRACTION OF WHAT YOU'RE PAYING. WHAT CAN YOU DO TO LESSEN YOUR FINANCIAL BURDEN? BLEND AND EXTEND...HERE'S HOW IT WORKS:

Let's say you're paying \$70 per square foot and you have two years left on your lease. But in today's market your space is worth \$50/sf. You're \$20/sf over market. You want some relief and you want it now. Here's an approach that works for many tenants:

You have two years left on your lease commitment. You are paying \$20/sf above the market for each of these years. That's \$40/sf in total over market (20 times 2). Now, if you extend your lease out an extra ten years and do it now, you tell the Landlord you want to create a blended rate of old and new. The way this works is you divide the \$40/sf that you are over market into the new ten year term. Or in other words divide 40 by 10 and you get 4.

If you did not have the old \$70/sf commitment you could make a deal at \$50/sf. But since the landlord is not going to just forgive that high rent, you will agree to blend in the overage and instead of paying \$50/sf you will pay \$54, but it will start immediately. This is a win-win for both Tenant and Landlord. For the Tenant it's a win because it lowers your immediate costs. That \$16/sf savings can go into your business or into your pocket.

For the Landlord, it's a win for two reasons. One, you have not forfeited any money – you've just re-structured when you'll get it. And two, you have secured a long-term lease with an existing tenant. This is extremely valuable to a Landlord because banks and other lending

institutions value buildings based on Net Operating Income over time. If a building has leases expiring in less than 5 years, banks are likely to discount that portion of the operating income. However, if a building has a tenant in place for ten years or more, lenders feel secure and buildings are valued at higher numbers.

Many Landlords make a lot of their money not through collecting rent or selling their buildings, but rather by re-financing the asset or modifying the loan agreements. The key for Landlords in doing this successfully is to have fully occupied buildings with long term leases.

Will Landlords always work with Tenants in this way? Of course not. But it is worth a shot because MANY will. Keep in mind this only works if there's a significant delta between what you are paying and what the market will bear. According to Co-Star Group (a national independent tracking agency) office rents in NYC have dropped 42% from the highs in 2007. However, in the past few quarters, rents have started to inch back up.

From a tenant perspective, this signals a time sensitive opportunity to lock in a great rate before the market fully recovers.

Bert Rosenblatt and Andrew Stein are principals of Vicus Partners, LLC and the ITRA affiliate for New York City – Downtown. Bert Rosenblatt can be reached at (212) 880-3747 ext. 6619 or at brosenblatt@vicuspartners.com. Andrew Stein can be reached at (212) 880-3747 ext. 6620, or at astein@vicuspartners.com