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Market Focus - Office Leasing:

DC Office Landlords provide Greater Lease Concessions



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MARKET CONDITIONS IN THE DC METRO AREA continue to favor tenants. Vacancy rates continue to rise due to more Class A office space coming online and decreased demand by the federal government for leased space as a result of sequestration and budget cuts. In addition, tenants' use of office space has become more efficient, thereby further reducing demand for office assets.

According to a recent survey published by the CBRE, the Washington, DC office market saw a 30 basis points increase in vacancy rates in the second quarter of 2014. To attract tenants in this competitive environment, landlords are increasing the concessions provided to potential tenants. Some of the most common types of landlord concessions are as follows.

- **Rent Abatement** - One of the most commonly used type of lease concession is rent abatement. Although Landlords typically are reluctant to lower base rent since such a reduction will reduce their property's net operating income and value, in order to keep vacancy rates in-check, landlords are more willing to provide prospective tenants with a limited period of free rent. Tenants benefit from rent abatement by having a reduced *effective* rent rate over the full term of the lease while landlords gain by preserving their property value by keeping the annual base rent stated in their leases at a higher level
- **Lease Buyout** - Although not a common concession, some landlords have chosen to attract tenants by agreeing to buyout a tenant's current lease in another building. One of the most prominent examples of this type of concession was Vornado Realty Trust's buying out of the remainder of Cooley LLP's lease at the building on 777 6th Street, NW in order to attract the law firm to Vornado's Warner Building.



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- **Increased Improvement Allowance** - Another important type of lease concession is an increased tenant improvement allowance. By providing tenants with more upfront money to build-out their space, landlords are able to attract tenants to their building while also keeping base rent high. According to a recent quote by Savis-Studley's Tom Fulcher in the Washington Business Journal, the norm five years ago for tenant improvement allowances was \$60 per square foot. Today, it is not unusual to see tenant improvement allowances in the range of \$90 to \$110 per square foot.
- **Enhanced Parking Rights** - A less common concession offered by landlords is enhanced parking rights. This type of concession is frequently provided in the form of free or reduced cost parking, an increase in the number of tenant allocated spaces, the ability to have reserved spaces and/or more advantageously located spaces. Together with other lease concessions, enhanced parking rights can be an important part of an effective concessions package.

Conclusion - As vacancy rates rise and demand slackens for Class A office space, landlords must be proactive in order to preserve the value of their buildings. Lease concessions are an effective way for landlord's to address these challenges.



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