



Chicago's normally bustling Michigan Avenue was empty on Friday, March 20, 2020, as businesses shut their doors amid the spread of the new coronavirus. (Jennifer Waters/CoStar)

## As Cities Go Dark, Tenants Gain Upper Hand in Office Space Negotiations

Pandemic Slows  
Demand, Pushes  
Landlords  
to Close Deals Quickly,  
With Concessions

**As the U.S. commercial real estate market reckons with the rapid spread of the new coronavirus, office brokers and analysts are bracing themselves for a market that favors tenants when, just days ago, the nation was broadly experiencing one of the strongest demand benefiting landlords.**

For proof, look no further than a deal closed in the past week by Coy Davidson, a senior vice president in brokerage Colliers' office group in Houston. Davidson, who was prohibited from naming the landlord and tenant by a nondisclosure agreement, said the office tenant — a health care company looking to lease 8,000 square feet — and the property owner of a "very expensive space" in a "high-profile building" were negotiating back-and-forth over price, "and, all of the sudden, the world started changing."

At the beginning of last week, when markets fell and local businesses began shutting their doors, the landlord quickly agreed to sign the tenant at a roughly 10% discounted rent rate, Davidson said.

*"Why wouldn't they?" Davidson said. "Landlords are going to be smart. Leasing activity is just going to come to a trickle, and we don't know if that's going to [last] a month or three months."*

The anxieties come as the U.S. stock market veers wildly as nearly every nonessential business in the nation — such as bars, restaurants and retailers — moves to temporarily shut their doors to mitigate the spread of the virus, which has so far infected more than 330,000 people globally. The closings have sparked widespread layoffs and many companies are holding off on making any new leasing decisions, putting landlords back on their heels.

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*"It is absolutely a tenant's market right now," Mike Petrivelli, market analyst with CoStar in Denver, said in a phone interview. "Everyone seems to be piling up their cash reserves because of the uncertainty moving forward, so you're going to see some office concessions."*

The speed at which the market shifted from a landlord's market to a tenant's market can hardly be overstated. The sudden coronavirus collapse of U.S. office demand comes after it set a post-recession record last year, according to CoStar's most recent report on the matter.

More than 2 million jobs were added in 2019, and rents were on pace to rise steadily by around 1% annually over the next few years. Nationally, vacancy had held at 9.7% throughout 2019, and a slew of companies — including Amazon, Apple and the international law firm Skadden Arps — planning to move into millions of square feet of office space in 2020 were projected to further strengthen national office absorption, too.

In recent days, though, mass job losses and an uncertain market environment has paralyzed businesses. Economists and analysts are painting a dire picture of the economy over the next few months. The Federal Reserve Bank of St. Louis President James Bullard even estimates that the national unemployment rate could pass 30%, a level higher than that seen even in the Great Depression.

That's left landlords eager to ink deals that will keep office space off the market and rent payments rolling in.

### 'Landlords are getting nervous'

Davidson and Petrivelli spoke of an office market that's evolving not because of some known, impending event, but of the huge degree of unknowns in the air.

Financial forecasters can make market predictions based on national or global reactions to era-defining events — such as the 9/11 attacks, for example — but the unprecedented nature of the new coronavirus' rapid spread around the world is translating to uncertainty in the commercial real estate market.

*"Things are going to come to a standstill for a while," Davidson said.*

Davidson closed three (3) deals this week, he said. Under normal circumstances, those deals would've still closed this week, but the landlords involved showed a new urgency to put pen to paper.

*"I could tell the landlords are getting nervous, because they were like, 'Where's the lease? Where's the lease?'" Davidson said.*

Landlord uncertainty isn't just limited to the office market. Retailers, already facing challenges from the growing e-commerce industry, is going to be further strained as more people opt to stay indoors. The Texas Restaurant Association, a trade group, expects between 25% and 30% of restaurants to close permanently as result of these virus restrictions affecting about 600,000 industry jobs, according to CoStar's most recent report on the retail sector.

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*"The harsh new reality of these closures is that thousands of jobs, households and retail leases are now in jeopardy," the report states.*

Slowdowns in Houston are inevitably tied to the price of oil, too. The price of U.S. crude posted its largest weekly price drop in 29 years, The Wall Street Journal reports. It ended the week of March 20 with a 29% price dip.

With a number of cities implementing shelter-in-place orders — as of the time of publication, California, New York and Illinois were among the states ordering residents to not leave their homes — deal flow may soon halt altogether. But for deals that do close in the coming weeks, as well as those that close in the weeks and months after the crisis, it's likely that the proverbial ball will remain in tenants' courts.

*"I'm sure they'll get creative with lease terms in terms of length, duration and stipulations," Petrivelli said of office landlords in a phone interview.*

As of late Monday, the World Health Organization reported more than 330,000 confirmed cases of the coronavirus and more than 14,000 deaths in 189 countries or territories. In the United States, there have been more than 31,000 confirmed cases with 402 deaths.

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