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By Steve Bergsman

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# How to Make Lemonade From Lemons

## With The Real Estate Market Turning Up a Lot of Lemons, It's Time to Lemon-Aid Your Clients

What's that old cliché? "When life gives you lemons, make lemonade?" Well, for the past five years, it wasn't life but the economy that has given the commercial real estate market nothing but lemons.

And how do you get rid of all those lemons, i.e., vacant buildings? The simple answer is, you guessed it, lemon-aid.

Sounds easy, but it's not. When you have vast square footage of empty space in a poor economy, it takes a lot of work and re-focusing of your skill sets to get deals done. It takes commitment, marketing skills, flexibility, and straight-talk with clients. On top of that, it sometimes takes a bit of luck.

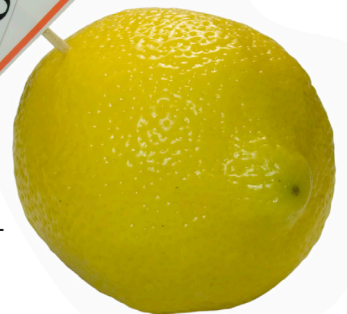
According to **Greg Gunn, SIOR**, senior vice president with Coldwell Banker Commercial NRT in Salt Lake City, UT, if you are representing a landlord, the three things to do in a market awash with lemons are:

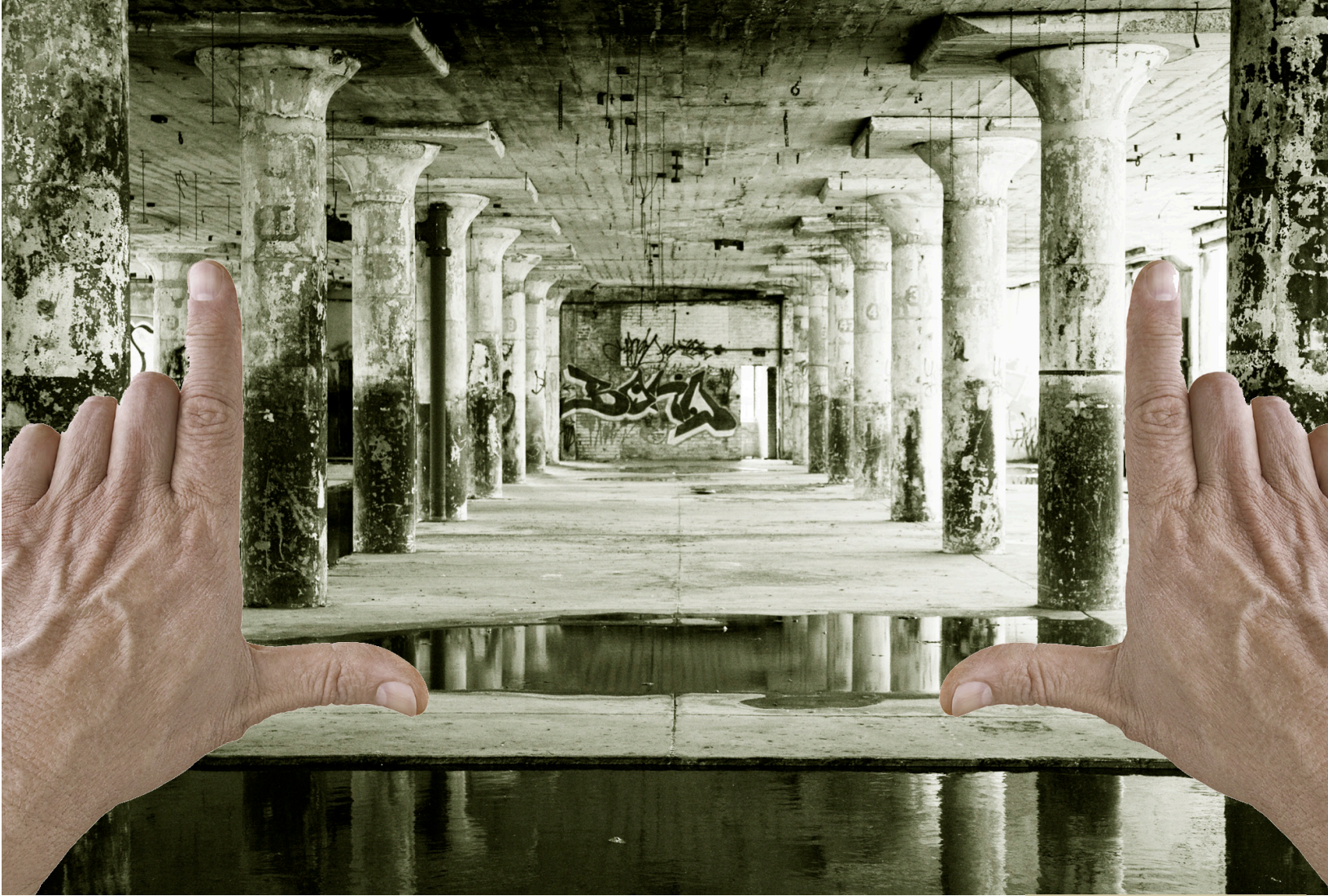
- Remind your clients that markets are cyclical. A bad market is going to come around eventually and you can't take the loss of income or rejections associated with it personally otherwise it will overwhelm you psychologically.
- Warn the client that concessions will have to be made. The broker needs to get comps, have a heart-to-heart with the client, and make sure the client gets a reality check in regard to the market.

- Advise your client to lead in bad times, not follow the market down. This one is the hardest to accomplish. If concessions are coming, get to your existing tenants early and make deals, because if you wait, the competition will get to lower rent levels, first, by enticing your tenants away.

The last suggestion is very difficult for landlords to get a handle on, Gunn cautions. "If you say to the landlord you have two choices: stay as is, or offer a rent reduction in exchange for a new five-year lease, the landlord will often say something to the effect of, 'What? Are you crazy? I don't make money at lower rent..!' But, six months or a year later, the landlord's building is 50 percent vacant and he says, 'OK, I'll drop rent and offer concessions.' By then, the income is lost and is troubled. You have to lead the market down."

If there was a fourth recommendation, it would be to make sure the landlords understand the competitive position of their buildings vis-à-vis the other structures in the market. This is important because more often than not the land-





lords might have to spend a buck if they want to get back one-hundred bucks.

“For brokers, it’s tough to convince property owners to do repairs and clean up the property,” notes **Gregory Wernisch, SIOR, CCIM**, a vice president with CTK Chicago Partners in Des Plaines, IL, “I strongly suggest you have a list of things that need to be done.”

Wernisch took a foreclosure assignment in Franklin Park, IL, for a bank. The building was 14,700-square-feet and had been used as a machine shop. It was a mess.

“We had a three-page list of things that had to be done along with photos,” says Wernisch. When the list was accomplished, the building sold.

Another time, Wernisch became the third broker on a building in Evanston, IL. It was another case where the structure was in bad shape with vegetation growing out of the rain gutters, filthy carpets and an out-building damaged when hit by a truck. The owner took Wernisch’s list to heart and the building was eventually sold to professional photography studio.

“The landlords don’t always listen and we’ll take the assignment even if they don’t,” says Wernisch,

“but we try to tell them it will take them spending \$10 to make a \$1,000 or \$200 to make \$200,000.”

Four solid recommendations make for a good package. Down in Louisville, KY, **Jeff Dreher, SIOR, MBA**, a sales associate at Commercial Kentucky/Cushman & Wakefield Alliance, put together his own list of *articulos quatro*. First and foremost is making sure the landlord understands the strengths and weaknesses of the property, and then secondly, if the property is weak in certain aspects compared to the competition, the pricing has to take that into consideration.

“The owner has to understand the reality of the property and the market,” Dreher says. “You need to be realistic and if the owner can’t handle the message, then this is one you might want to pass on because if the property has challenges you have to make sure everyone is coming in with the same game plan.”



“... in a market that is all lemons, the real key is to be flexible and creative.”

## Contributing SIORs



**Greg Gunn, SIOR**



**Jeff Dreher, SIOR, MBA**



**Gregory Wernisch, SIOR, CCIM**

## Contributing SIORs



Dan Doherty, SIOR



Kevin Geenty, SIOR



Sheldon Gross, SIOR, CRE



Stan Kurzweil, SIOR



David Zimmer, SIOR, FRICS

The third item on Dreher's list is making sure the property is offering the proper incentives to offset any weaknesses. And, finally, number four is to "expand" your own sales force by engaging the local broker community: take them to lunch, have them tour the building, show-off the main benefits of the building, and dispense marketing pieces on a regular basis.

**Stan Kurzweil, SIOR**, an office specialist with Cassidy Turley in Somerset, NJ, expanded his sales force in a sense, by participating in the local events, which is really part of a wider marketing plan.

"You have to differentiate your listing and yourself from the others," says Kurzweil. "Instead of relying on e-mails, I personally call on other brokers and go to all the open houses so I can interact and find out what's going on. It's helpful and they often return the favor."

Since Kurzweil is a proponent of strong marketing techniques, one of the first things he does with a new client is draw up a marketing plan with a budget.

"I had a major Fortune 500 company as a client," he recalls. "They had 60,000 square feet of office space that needed to be filled. There were difficulties in that it was in a big complex that had a lot of extra office space and it was for a short-term sublease."

Kurzweil's solution was to "market the heck out of it," including a big open house. The budget was not cheap but it was worth it because Kurzweil did two deals to fill the space. The client spent thousands and ended up saving millions by doing the deals.

In U.S. metros that remain in deep recession, the whole commercial real estate market is just one big lemon and it takes major adjustments to the usual game plans to be successful.

For **Dan Doherty, SIOR**, a senior vice president with Doherty Industrial Group, business in Las Vegas, NV, is a gamble that didn't pay off for a lot of real estate investors – almost 16 million square feet of industrial space sitting empty.

After four years in purgatory, Doherty has a few recommendations – the magic number *four* to be exact. First, he says you need to be a specialist's specialist. "You have to decide what kind of product you want to work with because the general practitioner guys are struggling," says Doherty. "Even within industrial, you have to decide what kind of product you're going to go after."

Secondly, most of the work these days is with REOs and short sales, which means dealing with banks and the banks' overseers. "Pricing is the key, especially because there are FDIC regulations involved," Doherty continues. "Banks typically can not list a property below appraisal price so we try to interface with the appraisers to make sure they have all the relevant market information. We

want the appraisals to be at market, not 25 percent above market."

Thirdly, and this harkens back to comments by other SIORs, you have to make your building competitive, which means investing money in clean-up, repair, and graffiti removal.

And finally, banks move slowly, and in commercial real estate, time kills deals, so you have to work closely with the banks to set up procedures and facilitate quick decision-making.

Generally, to be successful in a market that is all lemons, the real key is to be flexible and creative. There are always new realities and difficult conditions in a weak economy, and those who survive and out-perform the market are always adjusting, because yesterday's benchmarks won't be relevant tomorrow.

**Kevin Geenty, SIOR**, vice president of the The Geenty Group Realtors in Branford, CT, is both a broker and a landlord and knows the value of adjustment to economic realities from both sides of the property equation.

"Business conditions in Connecticut have forced area landlords to consider lease terms and conditions that they would not necessarily consider in better times," he remarks. "For example, landlords who want income to replace vacancy are spending more of their own money doing tenant fix-ups. The equivalent of four-to-six-months rental is commonly being spent to secure a three-to-five-year tenant. I'm doing it and I'm encouraging clients to do it as well."

In the past, personal guarantees were common in the Connecticut leasing business, but that doesn't work anymore. "In my business park, I have 19 tenants. Probably 16 have been there for more than two years and have no personal guarantees," Geenty says. Finally, he adds, it has become more common to do shorter leases.

Over in Kansas City, MO, **David Zimmer, SIOR, FRICS**, president of Zimmer Real Estate Services, says his company oversees a portfolio consisting of about 2 million square feet of B- and C-buildings that were constructed in 1960s and 1970s. The portfolio is running about 92 percent to 93 percent occupied.

"We upgraded the buildings to make them compete better and we strike quickly," he says. "We start negotiations early, not waiting for the RFP to come out. We will make proposals to companies right after they have seen our buildings and we set the bar where we want it to be, not where the competition is going."

Most importantly, Zimmer espouses flexibility. One of Zimmer's tenants was a logistics firm handling empty bottles for Proctor & Gamble and its space needs varied from month to month. Zimmer leased the tenant a 54,000-square-foot building with rent based on 30,000 square feet with additional billing based on additional usage.


He explains, "I come to the warehouse, and inspect it with the tenant. The tenant certifies the maximum square footage occupied for that month as it is up to his client's whim as to how many bottles will be in the warehouse each month. Yes, it's a little bit of a headache as far as I'm concerned, but they are in the building, paying rent, and have no desire to leave anytime soon."

This wasn't the first time Zimmer resorted to this flexible tactic. Another tenant is a logistics company handling the warehousing of Harley Davidson motorcycles. The company is in a 150,000 square foot building, but is only charged on 75,000 square feet. Then we charge them the delta between the minimum and maximum they occupy in a given month."

One of the most successful ways to make lemonade out of lemons is to change the use of a property, notes **Sheldon Gross, SIOR, CRE**, a principal with Sheldon Gross Realty Inc. in West Orange, NJ, "We had an old warehouse in Monmouth County and the warehouse market started to deteriorate. The building was right on a busy highway, so, using the foundation of the old structure we constructed a new office building and successfully leased it up."

Since then the market changed, with too much office and not enough industrial. "What we have started to do is get approvals to put industrial space behind some of our office buildings where we had a lot of property," he says. "The location was away from the highway and there had not been much interest in it. Now, with industrial space in demand, we are opening it all up to industrial and putting in a major road."

Gross observes, "The only way you are going to succeed in any kind of market is to be flexible because nothing stays the same. Change is constant."

It's a good adage from Gross but it faces competition from Geenty's summation: "The only way to make lemonade out of lemons is to fill the vacancies and get cash flow." 

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David DeVaney, SIOR, CCIM



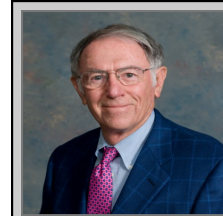
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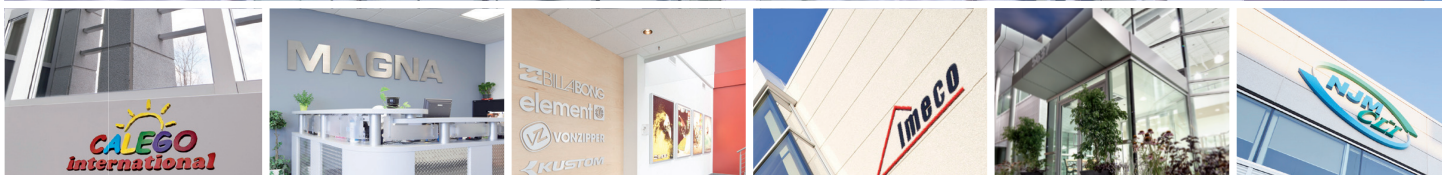
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