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Play *to* Win

The Real Estate Game
Renew vs Relocate



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A good coach makes sure that the team takes the field with every position covered, prepared for the challenges ahead, and conditioned to the play the entire game.

You shouldn't step onto the field without a great coach, just like you shouldn't go to court without the best representation. Commercial Real Estate is no different. With a Colliers advisor on your team, you will have a coach who will use extensive knowledge of market dynamics and a thorough understanding of your company's future business plans to develop a real estate strategy that allows us to stand shoulder-to-shoulder on the front line to advance key strategic business objectives. So whether the call is to renew or to relocate, Colliers will create a comprehensive plan that ensures a win.



It's all about the game plan...

Tenants who negotiate their own renewals gain some concessions, though they have little insight into their true value or how much more they might have gained. The brokerage professional can balance the negotiation on behalf of the tenant. In comparison to the landlord's strong field position, the tenant is undermined by attempting to renew a lease directly without an experienced coach.

Watch out for the win/win

Consider this play: Company RED's current facilities are adequate for the next five to seven years. It can choose to renew in place or relocate to comparable space. The company's real estate team leader goes out to market and examines comps, both for relocation and as a benchmark to judge the current landlord's lease renewal offer. Using the price per square foot of comparable space to establish the average, company RED calculates that the current landlord very likely will lease at a lower rate based on savings in the costs of a work letter, free rent, and possible market risk incurred in finding a replacement tenant. It seems like a fair assumption. But the landlord offers a new lease at a rent higher than average. The assumption is that the current tenant can move, but new space will cost the tenant even more than the rate offered when they factor in cost of moving, technology, new furnishings, build-out, lost productivity, and all the stress generated by the move. In the landlord's mind, the above average offer saves company RED in real costs, so everyone comes out ahead.

The Instant Replay

Let's take a look at that win/win and break it down. When you look closer, you see that the landlord is working the game from both benches, and wins by avoiding costs incurred to secure a new tenant (work letter, downtime, marketing costs). The Landlord the wins again, every month, when they collect company RED's premium lease rate, and all without risk or adding any value to the tenant.

When did we lose the ball?



1

Fumble 1: Assuming that a lease renewal was just a straightforward administrative matter, because there was no operational need to relocate.

Not having to address the operational, logistical, and cost issues associated with a move, managers typically feel that they have come out ahead of the game. Also missed is the opportunity to huddle up and assess whether or not the current space:

- Upholds & enhances our brand
- Facilitates & fosters our corporate culture
- Invigorates & supports our people
- Addresses & solves key business issues
- Enhances & stimulates innovation

2

Fumble 2: Stepping on the field without a clear strategy.

Since company RED did not see the lease renewal as an opportunity to gain a competitive edge, it did not commit adequate resources to the transaction. By underestimating the magnitude of the economic benefits that could be extracted from a routine renewal, company RED missed out on a major fiscal opportunity.

3

Fumble 3: Not understanding the economics from the landlord's perspective.

Landlord's determine their required economics based on numerous factors, including:

- Asset cost basis
- Required returns to debt & equity capital
- Effect of current economic conditions on real estate market activity
- Unique features of the market segment
- Tenant mix
- Competitive position in the specific market segment
- Rental rates & lease terms across the landlord's portfolio

Additionally, there was a over-dependence on a "good" relationship with the landlord. Given the business dynamics and possible repercussions in that assumption, did company RED understand:

- The nature of the game it was engaged in with the landlord?
- That there was even a game and that it was a player
- Just how much was at stake based on the outcome?

4

Fumble 4: Even knowing the game has started, company RED did not know the rules, strategy, or tactics.

Company RED may be a standout in their particular sport, but they could be rookies when they step onto the landlord's turf.



Landlords play the game with a loaded bench.

Lease renewals are not conducted on a level playing field. The landlord is in the real estate business and the tenant is not. This sounds obvious, but it has important underlying significance for the real estate decision maker. With an organized, extensive, and sophisticated information network to gather market intelligence and other data, the executive has developed the means to use this information in creating value for the company.

The landlord's chief survival skill is the ability to collect information in an unstructured environment. They know from a variety of inside sources when a tenant is considering moving out, and know from real estate market sources whether a tenant is scouting relocation alternatives.

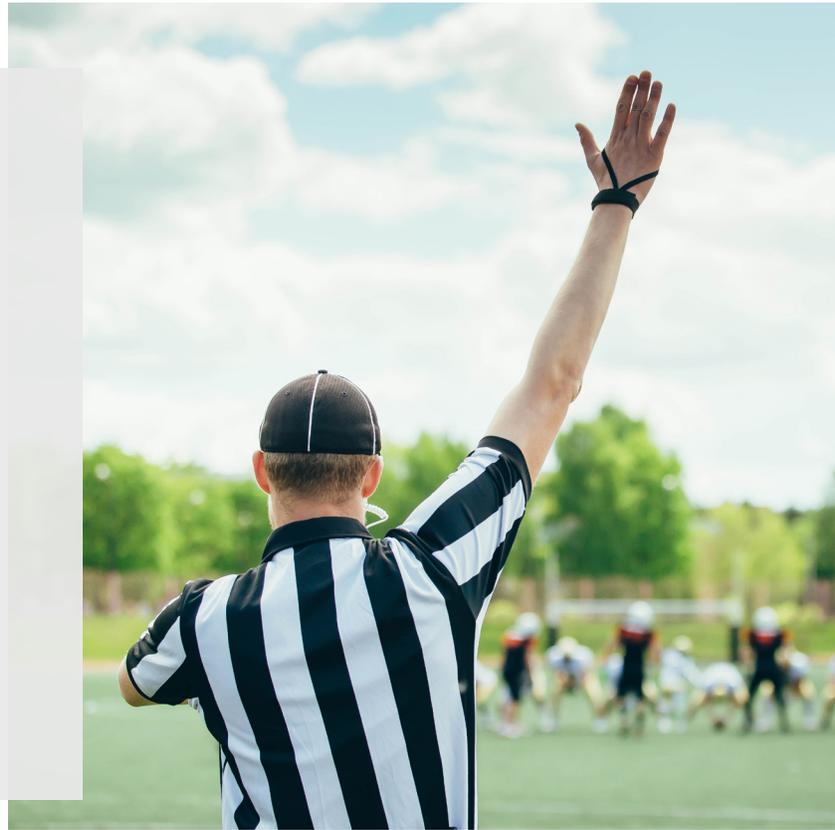
Since the landlord plays the game every day and the tenant only place once every five to ten years, or even longer, the landlord already knows every move in the game. The landlord already knows the unrepresented tenant's playbook – the moves and bluffs, the review and approval processes, and the timelines. Because the landlord has superior information and understands the game's strategy and tactics, they usually take an unbeatable lead from the beginning. In convincing the tenant that scoring based on their cost of relocating and not on the landlord's cost of finding a new tenant/tenants to replace lost income, the landlord loads the bench and moves into position for the win.

The good news is that tenants can win the renewal game. While the landlord has clear advantages, the important fact is that lease expiration and relocation expose the landlord to both significant lease-up costs and market risk. The tenant who understands this and builds a team that knows how to take advantage and play to that weakness can capture what otherwise would be a major windfall for the landlord.

Game Changers

In the renewal game, a tenant's chances of winning are enhanced by effective coaching in the form of a professional real estate advisor. Colliers International provides winning strategies for clients across Texas and around the world. Some tenants lower their odds of a win by taking the field without a full roster.

Here are some assumptions that lead to losing strategies and some defensive plays to counter them:



We have no interest in relocating & plan to simply renew, so we won't need Colliers' services

- Our role is not only to find space. Rather, our prime objective is to drive the most aggressive economic and non-economic leasehold terms regardless of a renewal or of a relocation.
- The moment a tenant requests a proposal to renew without a real estate advisor, the landlord achieves the upper hand in negotiations.

We have a good relationship with the landlord/landlord representative

- The landlord's objective is to maximize profits and shift economic and non-economic risk to the tenant.
- The landlord's advisor has a fiduciary obligation to achieve the best deal for the landlord and does not represent the best interests of the renewing tenant.
- The landlord is in the business and yet they still rely upon professional representation.
- The financial implications of a lease are significant, a similar strategy of professional representation should be employed by the tenant.

We are getting a good deal. The landlord lowered our rent & we are saving money

- A "good deal" can only be benchmarked against relocation alternatives that have been brought to full economic and non-economic maturity.
- Setting up competition for your tenancy in a methodical process is needed to create the benchmark of a "good deal".
- Landlords do not give their best deals. Strategy and leverage define market reality.

Engaging colliers for a lease renewal will cost us money and diminish our savings

- Brokerage fees are not added to your real estate expense. They are already embedded and don't disappear or reduce in the absence of representation.
- The landlord's advisors receive a larger fee should the client not engage representation.
- The landlord's advisor has the incentive to discourage the use of a tenant rep, resulting in a deal favorable to the landlord and the landlord's representative.

Strategy & Tactics for the Game

The first reality that the tenant must accept is that gaining maximum value from a lease renewal is not necessarily quicker or easier than finding, negotiating, and moving into a new space. Depending on the company's needs and objectives, it may involve all the costs and logistics of a move. The key difference is who pays for achieving those objectives, and who resolves the issues (qualitative, environmental, operational, etc.) through the renewal.

The renewal strategy objective is to shift the market risk to the landlord. The tenant's strategy must be to throw the landlord into the market in search of a tenant, and not allow the landlord to push the tenant out of bounds and into the market. For the landlord to have the perception that they are in the market and at risk, they must be convinced that they have lost the advantage and that there is a high probability of losing the existing tenant. Until that happens, the landlord will gamble on playing a familiar game where they have developed a very high skill level.

For the tenant to win, they must be willing to enter into a process that requires commitment, confidentiality, and above all, credibility.
The essential components of a successful renewal strategy include:

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Stopping the clock:

Landlords know how much time it takes many companies to make decisions and how readily they defer action. The pregame must begin early enough to convince the landlord that there is in fact enough time on the clock to make both the decision and the move. For projects of any significance, the process should begin at least two years prior to lease expiration. For larger projects, even more time is required.

Building a game strategy:

To avoid making an unfocused or unproductive threat to the landlord's income stream, the tenant should clearly define the objectives under a renewal. These can be defined in terms of rental rate, amenities, options, services, renovations/construction, signage, or any other components of value.

Playing a smart defense:

There are no "universal" landlords, no matter how similar they may seem to tenants. They vary greatly by types of investments, portfolios, personalities, financial and non-financial objectives, and risk profiles. An entrepreneurial developer has different objectives than a REIT or a pension fund. Foreign landlords have perspectives different from those of domestic landlords, even in the same line of business. Highly structured and joint venture landlords add another dimension of complexity. Buildings have different lease expiration schedules, debt structures, and equity maturities. Landlords have different hold periods and may have different perspectives on the relative importance of income versus asset value.

Using the counter play:

The landlord will not believe an eminent move if the motivation is not realistic and based on an unmet need. They must be convinced that the tenant seeks, and is intent on finding, something that a competing landlord can provide. This dissatisfaction has to be carefully crafted and developed or the landlord will see through it.

Playing to your strength:

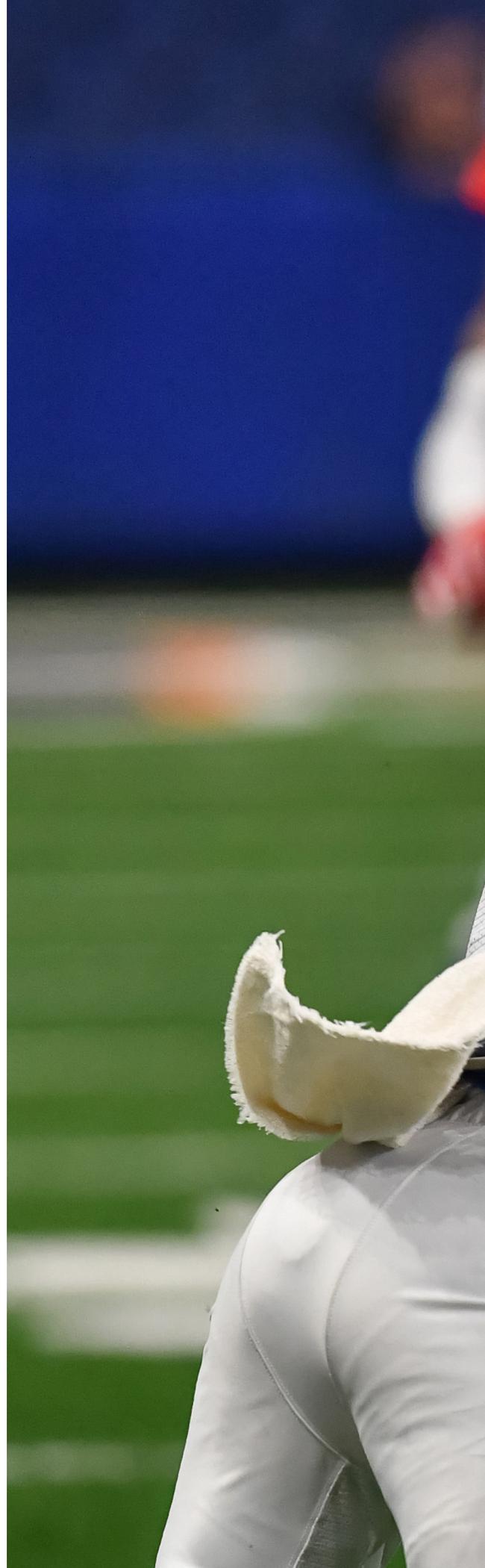
The tenant must develop alternatives and make sure that the landlord is aware that they are pursuing them. Landlords understand that corporate inertia works to their advantage - an aggressive market search by a seasoned real estate advisor from outside the company is strong evidence that the potential to move is real, primarily because it signals upper management's willingness to consider a wider range of alternatives.

Much of this awareness may sound as if it should be evident, but it rarely is, due to the inherent nature of the renewal environment. A company is more effective when acquiring space, which takes place in an environment much different from that of a lease renewal. In a new acquisition of space, the company's real estate executive enters the market with the full force of the company in play. The landlords usually have no long-term, intimate contact with the company hierarchy and will be forced to compete on price with other landlords.

In a large renewal environment, the smart landlord will have formed as many relationships as high in the company as possible to dilute the real estate executive's authority. The bottom line is, in these larger leases, the real estate executive may not get the company's full support in the renewal game that would normally be available in an acquisition situation - and the landlord knows this.

The Final Score

The importance of completing your roster with the strong support of a professional real estate advisor to plan and execute a real estate strategy cannot be overstated. A sophisticated advisor brings industry and market knowledge of the various players, market economics, key tactics, and critical vulnerabilities. Leveraging this knowledge and expertise can give you the “home field advantage” and ensure the likelihood of a winning result in every game.







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