



# SUMMER 2022 MARKET UPDATE



Greater Richmond  
Commercial Real Estate

## As lease terms shorten, the value of properties becomes more uncertain.

If the pandemic has infused business with any one idea, it's flexibility. Companies need to be flexible to get work done. Employees want flexibility to work but also be safe and manage personal and family obligations.

Flexibility has largely come down to space and, uncertainty. When executives aren't sure what normal will look like in where employees work, they can't tell how much office space they need. While some sectors of commercial real estate are stable in terms of tenants, others are a question. That's leading to some pushing for shorter term leases ironically, both by tenants and some owners as well as headaches for underwriting as the predictability of tenancy is up in the air.

The impact short-term leases could have on overall markets depends on their number, and that's tough to estimate, as it can vary greatly by location and type. Visual Lease is a proptech company that tracks several hundreds of thousands of leases in its systems. CEO Marc Betesh says that, first, it's still early to see what's happening, as given average lease turnovers of about five years, only roughly 20% of them have been at a natural point of renegotiation.

"Because of the instability of the market generally, the pandemic and new variants and all of the things that are happening, you probably have a bell curve of reactions," Betesh says. But there will be an inclination among many to look at their options. "When people don't know, they hedge. They take the safest, more conservative route."

"Most average rent rolls have decreased from 12 months to 18 months for an office building," says Transwestern associate Erik Coglianesse.

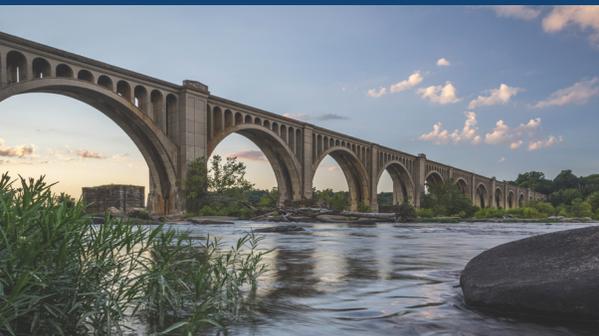
"Specific to the office, we've seen a lot of short-term deals signed," Eric Enloe, head of commercial valuation for JLL's valuation and advisory services platform in Chicago, tells GlobeSt.com. "The reality is large firms, Fortune 1000 companies, private companies, they don't know what their space needs are, Everybody has been hoping they'd get clarity as time went on. Even today, people have still not figured out what their design needs are and what their work from home versus work in office plan is. Most companies haven't figured this out yet. So, they sign a two-year deal, one-year deal, six-month deal."

Besides the tenants, many landlords have been wary of longer leases. "The owners didn't want to lock in low prices [during the impact of pandemic conditions on prices] for a long lease," says Toni Jordan, president of the central PA division at Univest Bank and Trust Co.

The dynamic of asking for shorter leases has been largely a function of timing, Jordan adds. "As leases were rolling off, they were inclined to do shorter terms," he says. "As bankers, we look at a building a client owns. We were in touch with all of those clients. 'What's going on with all of your tenants? Are you being asked to offer concessions?' Ninety percent said they weren't asked to offer concessions or rewrite leases. I see that as evidence that [the tenants are] financially healthy and able to pay rent if they're dark or partially dark."

One sector that Transwestern has found largely ignored short-term leases have, surprisingly;

## Short-Term Leases Complicate Underwriting



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been Class B and C buildings with small tenants using anywhere from 500 to 3,000 sq. ft. "These are small companies that rely on being in the office and some of the employees may not have space to work in the house from," says Coglianese. "Those buildings have done extremely well during the pandemic."

For property owners that go this route, there are financial implications. Those with long-term lease single-tenants are in good shape. "That market is vibrant," says Enloe. "It can be a Fortune 500 company that's viewed as a very secure investment. That's trading at levels that are higher than pre pandemic."

Multi-tenant office buildings are entirely different stories. "We've seen WALT [weighted average lease terms for entire properties] continue to diminish across office product," says Coglianese. "Underwriting and valuation of properties are seeing an impact. Risk profile is increasing for the building as the terms are decreasing. Even in a normal market, it would have an impact on value and buyer underwriting. More so now because there's a question of what tenants will do."

"Some [tenants] are going to take more, some are going to take less, and some are going to take the same," Enloe says. "If you're thinking of buying a multi-tenant office building, you're trying to figure out what the tenants will do in the future." Guess wrong and you could lose big, which is why Enloe says that lenders are charging more in such situations. "Because these corporations have not figured out their real estate strategy yet, it's causing these short-term leases that are harder to underwrite."

"What we're not seeing [at high valuations are] multi-tenant office buildings and short-term leases," says Enloe. The problem is not blanket unwillingness to underwrite deals but difficulty in forecasting rents and cash flow, meaning risk is difficult to estimate.

"Does it hurt your valuation? Absolutely," Coglianese says. The working rule of thumb used to be that 75% of tenants would renew for terms of five, seven, or ten years. That's greatly changed. Currently, Transwestern's clients have seen 60% of their tenants sign short-term deals of 12 to 24 months, with many of those "possibly downsizing," according to Coglianese. Then there is the 35% signing new leases in the five- to ten-year range.

"The length of the lease was really saved by the [tenant improvement, or TI allowance] because construction costs have increased significantly," Coglianese says. "They're moving or downsizing in their existing building. They're getting a new TI package because they want their space to be really special." The only way to make things affordable is to amortize TI over a longer term. "Landlords say, 'Sure, higher TI, but a longer-term lease. And if the tenant doesn't agree, they amortize the TI numbers over a shorter period, which greatly increases the cost of the space.'"

As a result, owners of multi-tenant office properties are often keeping them off the market unless they have to list them for sale. "That's the reality," Enloe says. "The projects getting listed that are multi-tenant

offices it could be the timing of the fund they're in and need to do redemptions and need to sell it for that reason."

The assumption is that next year might bring a stronger economy and, hopefully, lesser problems with Covid-19 and its variants. "Most of them would rather take the chance of waiting it out, seeing what happens with the pandemic, betting on office space that the employers will start to value having employees in the office and creating the company culture and people would return to the office again positively impacting their cash flows and values," Coglianese adds. "Most of these properties are still cash flowing. Have we seen vacancies increase? Sure. But it's not enough that [some] people aren't servicing their debt." Most still can and they've been able to "renew a fair amount of their tenants."

But that has its own risk, especially if new pandemic variants like omicron have additional impacts on societies and business. If enough companies continue their real estate needs, or enough time passes so that tenants can't keep waiting for things to improve, the strategy won't last forever.

"For tenants, the things they need to be concerned about and balance is Covid safety protocols and saving money by downsizing or leaving the office space versus company culture and a sense belonging where people are excited to go to work," Coglianese says. "For landlords, they're probably concerned about media and the perception of the office space and so many people are perceived as leaving the office space. That's a concerning figure for an owner. A question for them is what are you going to do to change that? We've seen a flight to quality. The best amenified buildings, best locations are getting tenants."

Then comes the potential reckoning time. As the months pass, more and more leases will come up for renewal, all facing the potential issue that has dogged businesses and real estate since 2020. Each new variant and additional questions of what measures might be necessary to keep people safe increases the amount of uncertainty for what steps companies will take and what their space needs will be.

A lease comes up for renewal. Even the most financially steady company that had been keeping hold of long-term leases as a hedge against changing practices versus the need to create company culture will begin to ask if there is easy additional profit to be made from reconsidering the amount of leased space on hand. Perhaps flex space might be the answer, as JLL has predicted 30% of all office space globally to be flexible over the next decade.

A rush to expand flex space could keep a lid on pricing, making the approach even more fiscally interesting to companies trying, as always, to improve their balance sheet. If that happens, underwriters might see a more definite and predictable movement away from the need for as much space, reducing demand on traditional office space and providing the rationale to lower valuations.

**Source:** Short-Term Leases Complicate Underwriting | Erik Sherman | GlobeSt. Real Estate Forum | January/February, 2022

## SOLD/LEASED IN Q2 2022

### Recently Sold:

- 5,000 SF of office space at 2550 Professional Road in Richmond for \$695,000. Lebs Breeden represented the seller.
- 4,603 SF of restaurant space at 119 N 18th Street in Richmond \$800,000. Bill Phillips represented the seller.
- 2,934 SF of office space at 531 S Sycamore Street in Petersburg for \$192,000. Todd Buttner represented the buyer.
- 1,462 SF of retail space at 802 E Nine Mile Road in Highland Springs for \$175,000. Robert Brown represented the seller.

### Recently Leased:

- 7,611 SF of office space at 1603 Santa Rosa Road. Bill Phillips represented the tenant.
- 5,590 SF of flex space 1521 Brook Road in Richmond. Lebs Breeden represented the landlord.
- 5,903 SF of retail space at 480 Winter Place Way in Midlothian. Bill Phillips represented the tenant.
- 2,400SF of retail space at 308 W. Broad Street in Richmond. Rob Brown represented the tenant.
- 2,382 SF of retail space at 5114 Richmond Henrico Turnpike in Richmond. Todd Buttner represented the landlord.
- 1,758 SF of office space at 2727 Enterprise Parkway in Richmond. Bill Phillips represented the landlord.
- 1,555 SF of office space at 2923 Polo Parkway in Midlothian. Todd Buttner represented the tenant.

See all our listings at:  
[JoynerCommercial.net/Property-Search](https://JoynerCommercial.net/Property-Search)

# What's New in RVA



## 'The Lake' in Chesterfield

A water-centric mixed-use development years in the making appears primed to get a boost from Chesterfield County.

The development is currently expected to cost \$323 million and would rise at 13400 Genito Road, and 2500, 2601 and 2991 Genito Place.

The development is expected to have 250,000 square feet of office, retail, entertainment and restaurant uses, though a specific breakdown hasn't yet been determined, Burkhart said. A 170-bed hotel is planned.



## Riverfront Amphitheater Planned

The centuries-old stonework at Historic Tredegar could soon form the framework for Richmond's version of Red Rocks.

The outdoor venue, which would host concerts as well as community events, would be fitted between Tredegar and the filled-in portion of the Kanawha Canal, which follows a curve in the hillside that forms an amphitheater-shaped footprint.



## "Project Rocky"

A massive e-commerce fulfillment center, similar to Amazon's robotics facility near Richmond Raceway, is in the works for a site in northeastern Goochland County about two miles west of Wyndham and Short Pump.

The center would be built off a 650,000-square-foot footprint, the same footprint as the raceway facility, which Amazon refers to as its RIC4 fulfillment center.

Source: Richmond BizSense | 2022

## FEATURED PROPERTIES



Land | For Sale

### KENTUCKY SPRINGS RD & HALEY DR

\$225,000 | 0.42 ACRES  
Lebs Breenen | (804) 536-3933  
3.316 acres of land fronting on Haley Drive and the corner of Kentucky Springs Road. Property is zoned C-2 for widespread commercial uses.



Retail | For Sale

### 921 HULL ST

\$1,200,000 | 4,662 SF  
Susan Haas, MURP | (804) 349-5788  
Renovated, one-story 4,662 SF brick storefront retail/office space is located in RVA'S fastest growing residential neighborhood.



Land | For Sale

### 12009 CHURCH ROAD

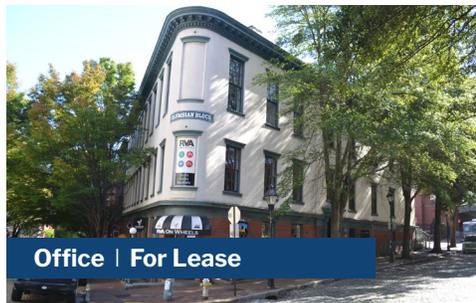
\$900,000 | 1.57 ACRES  
Sean Yoon | 804.355.4000  
1.57 Acres, zoned as A-1, is rare property is suitable for a skilled nursing facility, daycare center or multifamily units. Situated in densely populated Tuckahoe Farms.



Office | For Lease

### 2821 N PARHAM ROAD

NEGOTIABLE | 1,500 - 3,500 SF  
Todd Buttner | (410) 382-7109  
This two-story, 21,776± SF medical office building is located in the heart of Henrico County and right across the newly renovated J.R. Tucker High School.



Office | For Lease

### 1301 E CARY STREET

\$15.00 / SF | 2,914 SF  
Bill Phillips, CCIM | (804) 967-2739  
Creative office space located on the basement level of the Columbian Block in Historic Shockoe Slip adjacent to The Martin Agency.



Retail | For Sale

### 3318 JEFFERSON DAVIS HIGHWAY

\$895,950 | 2400 SF  
Newton Carroll | 804.967.2624  
Outstanding opportunity to own a thriving business that has been at this location for over 50 yrs. Location and VPD make this a very profitable investment opportunity.



2727 ENTERPRISE PARKWAY  
RICHMOND, VA 23294

Phone: 804-270-9440  
JoynerCommercial.net

