

SWFL Office Market 2010

By Mark Alexander, CCIM

The reason you can buy or rent such great deals today in SWFL is because the office vacancy is so high. The average office vacancy for SWFL right now is 17% but averages can be misleading. You really need to dig down to the actual class of space and its particular location to check the vacancy for that specific area to gain useable knowledge. For example, at the end of 2009 Lee County showed 19% vacancy for Class A space, 18% vacancy in Class B space and 12% vacancy in Class C space. But Charlotte County showed 53% vacancy for Class A, 22% vacancy for Class B and just 11% vacancy for Class C space. Collier County showed 26% vacancy for Class A, 16% vacancy for Class B and 10% vacancy for Class C. I should point out that an ideal balanced market is where owners and tenants do not have leverage over each other. This balanced market occurs when office vacancy factors reach the 8% to 10% range. An "Owner's Market" exists when you have vacancy factors between 0% and 7%. A "Tenant's Market" exists when you have vacancy factors of 11% or higher. We are solidly in a "Tenant's Market" right now with varying degrees of distress based on class of space and county.

Unfortunately, office vacancy is due to go even higher by the end of 2010. When we finally stop losing jobs in SWFL, we will stop losing demand for office space. Demand for office space is measured by calculating annual absorption. The SW Florida office market had negative absorption of 540,000 square feet in 2009. This means tenants who occupied 540,000 sf of space in 2008, moved out and left their space vacant in 2009. If the average tenant size in SWFL had 2,000sf, then this is the equivalent of 272 tenants in SWFL giving up their office space for vacant in 2009.

During the recession of 1991 to 1992, tenants were focused on survival like they are today. As their leases came up for renewal in the early 90's, we witnessed tenants dropping down a Class of space seeking lower rent in an effort to keep their businesses alive. But we see a different trend in today's recession. We have not seen tenants move to lower classes of Space at the end of 2009. Annual office absorption is a good indicator of what tenants are doing. SWFL saw

Class A space reach positive absorption of 5,100 sf at the end of 2009. This means Class A tenants who pay the highest rent in the SWFL have weathered this economic storm the best so far. We lost no tenants from class A space and actually gained a few new Class A tenants by the end of 2009. One reason for this phenomenon is that some sellers (especially banks with foreclosed office product) are discounting their vacant class A office space which has become attractive to tenants who decide to buy instead of continuing to rent. Class B space lost 264,000 square feet of space in 2009. Where did these Class B tenants go? Did they move down to Class C space as was typical during the early 90's? The answer is "no" when you realize that Class C space lost 281,000 sf of space itself. So Class B and Class C tenants simply moved out while Class A tenants stayed where they were as the most stable segment of the office market.

It seems we can't depend any longer on stable population growth to bring us positive absorption of office space like we enjoyed over the past three decades. So we have a lot riding on the preferences of the huge baby boomer market retiring over the next decade. Hopefully they will still like the warm sun, the white sand, the boating, the fishing and golfing...as much as the many who retired before them. This brutal winter weather up north should get more than a few boomers dreaming fondly of our swaying palm trees.

Many seem to think this is the worse office market we have ever endured...but it is not. SWFL had a higher vacancy (21%) in 1991 which was caused mainly by overbuilding back then. Today's office market (at 17% vacancy) feels worse emotionally because we have lost so many jobs in addition to healthy overbuilding of our office market. Since 2005 we have built 4.8 million SF of new office space in SWFL during a time span when our demand for office space was quickly diminishing. Fortunately there are only 230,000 SF of new office deliveries scheduled for 2010. Most economists predict positive job growth by the end of 2011 or beginning of 2012 so that is when positive office absorption should resume. Until then, it is a great time to buy or rent at the bottom of the market.

When is next Boom?

It took 14 years from our worst office market in 1991 to reach our best office market in 2005. If history were to repeat, SWFL office market

would see its next peak in 2024. But a different picture emerges when you look at the study completed by economist Fred Foldvary of Santa Clara University. Mr. Foldvary researched the real estate cycles in America over the past two centuries. He found that 18 years was the most common time period between troughs to peaks for real estate market cycles....except for one glaring exception. After the great depression...it took 44 years to reach the next market peak. So anywhere between 14 and 44 years from now...southwest Florida should peak again for office sellers and Landlords with a smoking hot year. But if you are a tenant looking for favorable (i.e. low rent) renewal terms...or if you are a buyer looking for an office to buy cheap and occupy...2010 is your peak year.

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