

The year of 2008 was a transitional year towards what is becoming the most tenant-favorable market since the commercial real estate recession of 1991-1995. In Q4 2008, we saw availability rates continue to raise throughout the suburban San Diego office submarkets, as well as continued softening in biotechnology and industrial real estate. In the extreme, Governor Park closed the year at 57% availability, which in our 20-year history as a firm operating in San Diego, is the highest availability rate in history in any submarket. Aggregate sublease space is now at 6,000,000 square feet, the highest level since 2001, leading to intense competition for landlords trying to lease direct space, or otherwise renew tenants. The Irving Hughes quarterly commercial real estate market dashboard detailing these trends may be viewed at [IH\\_Suburban\\_Market\\_Dashboard\\_Q4\\_2008.pdf](http://IH_Suburban_Market_Dashboard_Q4_2008.pdf).

In 2008, landlords struggled to keep a floor on asking rental rates by offering free rent, moving allowances and turnkey tenant improvements. These tactics enabled landlords to hold their asking rents, but actual results were discounted off of face rates from 15% - 20% in Q4. That discounting will continue, but 2009 is the year in which certain landlords will break ranks and lower their asking prices in order to compete. In 2009, we expect availability rates to increase marginally, as tenants react to the recession and the capital markets crisis by generally downsizing when their leases expire. The average tenant will downsize 10%-20% when their 2009 lease expires, which will have a net effect of increasing overall availability rates by as much as 3%-4% in most submarkets in San Diego County by the end of the year.

In Sorrento Mesa and Carlsbad, which have been soft markets for three years, we are completing leases at terms and conditions, including rental rates, tenant improvement allowances and other concessions, at the lowest levels in almost 15 years, inclusive of both sublease and direct space. Del Mar Heights is also feeling the pain as law firms are generally frozen, technology companies are leaving for cheaper submarkets, and the financial services sector of hedge funds and advisory firms have been substantially downsized.

Savvy San Diego County landlords have finally come to the realization that they can no longer play the capital markets game of buying low and selling high, and the debt and equity markets for commercial real estate have evaporated. We have already seen some foreclosures of commercial real estate assets, and we have to do more due diligence than ever on specific landlords to ensure their ability fund tenant improvements. This crisis for landlords will likely last at least three years, and possibly as long as five years. While most institutional landlords will endure and hold on to their positions, many landlords that have loans coming due in 2009 and 2010 will not be able to refinance. Those owners will find their asset value is now 30%-40% less than when they bought it back in the 2004-2006 hyper-inflated market and will face foreclosure.

Tenants with leases expiring in 2009 and 2010 should be consulting with us now to develop strategies of how to exploit this soft market condition. San Diego companies that are looking to reduce their overall corporate expenses are hitting the leasing market in a great window to reduce their real estate cost structure. Some tenants may be tempted to do direct renewals with their landlords, as landlords are going to proactively come to tenants with what appear to be fair deals. However, the best way to achieve the most favorable terms is to go to the market first to evaluate subleases, as well as to see what other landlords are willing to do to win your business. Irving Hughes has completed thousands of lease restructurings; renewals and relocations during our 20-year history, and new landlords are generally more aggressive to win a new tenant than the existing landlord is to keep them. Notwithstanding, any renewal negotiation can be optimized without leverage, information and the real-live threat that the tenant has a viable option to move to.

**For help with your next moving decision please contact:**

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**<http://www.ATELCommunications.com/movingHelp.aspx>**

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