

January 24, 2006

Dear _____:

In the last six months the midtown and midtown south office markets have gone through a shift in the relationship between supply and demand that can only be described as “classic.” After a long period in which the tenant had the whip hand, the vacancy rate has dropped since July of 2005 to the pre “bubble burst” levels of early 2000 while rents have risen 17 to 23%, depending on the building.

Rent as a percentage of operating expense has declined in recent years, but in the last six months this rise has reversed the trend. While, historically, increases of this magnitude peak and then fairly quickly retreat, there are good reasons to believe that this time round we aren't just looking at a “standard issue” cyclical swing. Tenants in New York City are, in fact, facing a fundamental shift in the cost of doing business.

To put it plainly, the underlying cost structure of creating and providing office space in Manhattan has drastically altered. In the last five years property taxes have gone up by \$5.00 and other costs of running a building by \$6.00 per square foot due, among other things, to dramatically more expensive energy and insurance. Meanwhile increased material, labor and other costs have driven the cost of construction up far ahead of inflation, so that where five years ago, a new tenant interior installation cost \$45.00 it would today cost \$60.00. When it comes to new construction, you can add in a dramatic rise in the price of land, making projects that would recently have made excellent economic sense quite impracticable now. It seems unlikely, then, that any meaningful pullback in rental rates is on the horizon.

One way that we at Edward Warren & Co. are dealing with these trying times for tenants is by bringing them quickly up to speed on what they need, so that when they see it they know to take it right away. Before going out and looking at the market, a tenant should (with, of course, a little help from their broker) do a space program and a location analysis. They should prepare a budget, too – not a wish list

disguised as a budget, but a real, realistic, one, taking into account the market, the type of space and the amenities needed.

Then, when they see the right thing, they should go for it. And when they've negotiated an acceptable deal, they should, as I think I've already said, take it right away. In a market like this extended thinking is the kiss of death. We have an over-analytical tenant that lost a series of transactions by sitting and staring at its choices for two or three weeks at a time. The result in one case was that the space was rented, in the next a bidding war erupted, and in the third, the landlord proceeded to pre-build the space to a plan the tenant could not use. This last space was one of the first we showed them, and while they were spending six weeks looking at alternatives (none of which represented an improvement on it), the landlord moved ahead and turned it into something that no longer worked. *In this market space gets rented in weeks, not months.*

If you need space or have other tenancy issues, do something about it now. These are trying times for tenants, but with the right help they don't have to be impossible. Give us a call.

Yours truly,

Tristram H. Pough
President