Space shortage emboldens landlords

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BY ALLISON LAMPERT, THE GAZETTE MAY 10, 2011

A panoramic view of McGill College Ave. in Montreal.
Photograph by: Allen McInnis, The Gazette

MONTREAL - Tenants aren't yet wooing office building landlords with baskets of fine wine and vacations on pricey yachts.

But the space shortage in many of Montreal's premium downtown office buildings is starting to embolden landlords, who are commanding slightly higher rents and offering tenants fewer incentives to sign deals than even a few years ago, brokers and landlords say.

"Now a landlord is going to be a lot more confident in maintaining his position than he was two years ago," said René Arsenault, vice-president, Quebec region, for Toronto-based CREIT Management Ltd., which manages 1010 Sherbrooke St. W.

"Today we've turned offers down, whereas two years ago we may have been more flexible."

Jim Beckerleg, president and CEO of Homburg Canada REIT, which owns Alexis Nihon Plaza, said landlords are less willing to negotiate in what he called a more balanced downtown office market: "There is firming in the market, although I think it's slow in coming."

At the end of the first quarter, there were only eight Montreal Class A buildings with more than 35,000 square feet of available contiguous space, an Avison Young report published Monday said. The availability rate for space in Class A office buildings is around eight per cent.

"Tenants are not particularly grovelling ... but it's a bit shocking when you're a larger tenant and that's all the choice you have," said Bruce Cowper, senior vice-president and principal at Avison Young Quebec.

“Companies are now starting to look way in advance of when their lease expires.”

Arsenault said he’s seeing more interest from prospective tenants.

According to Altus Insite, the availability rate at 1010 Sherbrooke St. W. is a minuscule 2.1 per cent.

“Two to three years ago, you’d have five tenants going through a building, where two are interested and one is very interested,” Arsenault said.

“Today you have six people going through and three are very interested.”

The space crunch is the result of the improved economy and the absence of new construction in the downtown core. Earlier this month, Kevric Real Estate Corp. announced the first privately funded construction of downtown office space in 20 years.

Some landlords are already raising their net effective rents, the amount of rent after deductions for maintenance and repairs and any tenant allowances.

What’s more, it’s harder for large tenants to secure sweet deals from landlords. Today a tenant would get maybe three to six months’ free rent, whereas during the recession, some could get up to a year’s free rent on a 10-year lease, said Louis Burgos, branch manager for Cushman & Wakefield’s Montreal offices.

“The difference between then and now is that the magnitude of the inducements has diminished, because there are not as many landlords sitting with huge vacancies,” Cowper agreed.

But with 230,000-square feet of office space to be delivered by Kevric in 2013, and with another potential tower to be announced this year, some observers are urging tenants to wait.

“I think tenants should be wary of perhaps overpaying at the moment, given the lack of space that we’re presently seeing in downtown Montreal,” said William Jegher, vice-president for Ernst & Young Real Estate Transaction Advisory Services in Montreal,

“Depending on their lease expiration dates, if they could perhaps hold off on securing new space until some of the new construction hits the market, I think they’d be in a much better position to get existing vacant spaces for a lower price.”

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