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# Business Review's 2010 Ann Arbor area Commercial Real Estate Roundtable

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What's there to say about commercial real estate in Ann Arbor at the start of 2010?

I posed that question to many of the leading regional industry experts as 2009 drew to a close, in anticipation of my annual roundtable discussion focusing on what kinds of real estate changes we can expect to see that will affect owners, brokers, tenants - and ultimately, the health of the business community.

Vacancy rates, development pace, lending patterns and building values all are changing rapidly across the nation, and all are likely to affect Ann Arbor, too.

My first commercial real estate roundtable launched Ann Arbor Business Review in January 2003, and I've done it every year since. This year, many participants said we're in a bit of a holding pattern: We know it could get worse, but hope to keep hold of the existing, perhaps tenuous, stability.

So instead of gathering participants in person for an open discussion now, I asked each a set of standing questions to define the start of the year. We'll follow up by midyear to track changes and effects of some of the conditions - like the tight lending - that some say could be starting to improve.

What follows are their responses, offering a guide to what our local experts see coming this year and beyond as the nation braces for changes in this sector.

## When you look back on 2009, how will you describe it?



**Rob Aldrich, [MAV Development](#), Ann Arbor:**

Generally flat demand for office space with most activity coming from renewals within the Ann Arbor market. (There was) very little demand coming from outside of the market. The capital shortage has affected entire market more than many expected.



**David Hamilton, [Swisher Commercial](#), Ann Arbor:**

"By most reports, the 'recovery' seems to be under way. We saw some evidence of this at the end of 2009, and if it continues into 2010 and beyond, we will be able to confirm 2009 as the beginning of the recovery. We would hope to be able to say 2009 was the peak year at an overall vacancy rate of 17.62 percent since Swisher Commercial began the reports

in 1993."



**Patrich Jett, [Grubb & Ellis](#) agent, Southfield:**

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“2009 was the year that the housing market and automotive industry collapsed creating a challenging economic environment in Michigan. It is also the first year in which Michigan took significant steps to retool its economy in the production and manufacturing of clean energy and advanced automotive electrification.”

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**Bill Kinley, Phoenix Contractors, Ypsilanti:**

“It was a challenge. The tenants with leases that were renewed were looking for consideration, and we’ve given them consideration. So far we’ve held onto all tenants who wanted us to look at leases.”

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**Cam McCausland, director Colliers International, Southfield:**

“Brutal, stagnate for the first six months of the year. Not only did user activity dry up but also lending came to a complete stop, which has contributed to inactivity.”



**Ted McMullen, McMullen Co., Ann Arbor:**

“The same way many probably celebrated New Year’s Eve: glad that 2009 is over. It was a very challenging year but also nice to see how well the stock market did, especially in the latter part of the year, while the rest of the economy was in the tank.”



**Ed Shaffran, the Shaffran Cos., Ann Arbor:**

“Having gone through four-six cycles ... it’s just another notch on the belt of experience. By global comparison, I’m glad we are in Ann Arbor.”



**Neal Warling, Bluestone Realty Advisors, Ann Arbor:**

“The year that never was. 2009 was perhaps the most uneventful year in commercial real estate in the area, characterized by many companies continuing to contract and very few expanding in the face of economic uncertainty.”



**Jim Chaconas, Colliers International, Ann Arbor:**

Ugly.

**What are you projecting in the regional commercial real estate market in 2010?**

**Rob Aldrich:** Prices will continue to decline with few buyers and limited capital (debt) sources. Development will be non-existent due to lack of demand and capital.

**David Hamilton:** A slow recovery in the commercial sector. It may not come soon enough or fast enough for some companies who are struggling now, so there could be more losses in jobs and mortgage foreclosures before it is over. Vacant land is dead. Industrial and warehouse vacancy may yet increase in the near term before the 'recovery' is felt.

**Patrich Jett:** Low activity and neutral price change. I believe we have seen a small correction in Ann Arbor to reflect market conditions, but overall, the Ann Arbor region has weathered the storm quite well (as it has diversified from the rest of the southeast Michigan economy). However, the recession will keep activity very low as employers remain cautious and look for long-term direction.

**Bill Kinley:** The further you move away from Ann Arbor and Ypsilanti, it gets a little slower. To the east, it's going to be very slow for the foreseeable future.

**Cam McCausland:** Slight improvement, but that is relative to next to nothing from an activity standpoint. Pricing will be under pressure, landlords will be struggling with incentives to be competitive.

**Ted McMullen:** For the first half, even worse than 2009 - few will be looking, some smaller leases will get done, no blockbusters, and some leases will even get executed at rates that are reset to lower levels. However, the bottom is near and the second half of 2010 could bring an upward turn as smart money returns and these investors will be buying properties at historic lows.

**Ed Shaffran:** Pretty much of the same as 2009 - continued contraction, such as the downsizing of firms' space needs.

**Neal Warling:** Slight improvement with a few bright spots. Regionally, things will continue to settle out as a result of the restructuring of the automotive industry. We should see an uptick in properties going back to the lenders. Buildings financed with non-recourse loans and either appraising too low on loan renewals or those simply having no tenants or too few tenants will be given back.

**Jim Chaconas:** It's not going to be as bad as 2009, but until they get the financing situation straightened out, it's going to be tough.

## **What should the average person be learning from today's commercial real estate market?**

**Rob Aldrich:** Leverage is a great concept but there is risk in paying back debt.

**David Hamilton:** Leverage is a wonderful thing when the market is booming, but properties that were highly leveraged in the last five years may be underwater now. There are bargains for cash buyers as banks and investors discount values to clear their books. Those who were conservative are now in a stronger position.

**Patrich Jett:** There is no guarantee in real estate. Research and knowledge can reduce risk and exposure. There is opportunity in every market, take advantage of it. Fear and greed also can affect markets in very dramatic ways.

**Bill Kinley:** There have been very positive discussions about buying local. The retailers

and restaurants that focus on their local clientele seem to be the strongest, and I think that support is needed.

**Cam McCausland:** Buy low and sell high. Owners who paid top dollar for property (primarily because money was available) are going to struggle to make economics work in a poor market.

**Ted McMullen:** Play everything conservative. For owners, work hard on the basics, keep your properties well-maintained and really listen to your tenant's needs. Do everything possible not to sell at this time. For buyers, think of worst-case scenarios with today's loan-to-value financing, rent projections, rainy day reserves, etc. The purchase of real estate should be looked at with the long-term mindset. People who have followed these practices in the past have been able to weather the storm.

**Ed Shaffran:** Excessive leverage is a perilous zeal.

**Neal Warling:** For lessees: good things come to those who wait. For lessors: part of something is better than all of nothing. For buyers: cash is king. For sellers: good things come to those who wait, but they may come too late.

**Jim Chaconas:** It's the old adage. For years in both residential and commercial, agents would just answer the phone. ... Today it's got to be a constant, daily grind (to succeed).

## What indicators will tell us that recovery is in sight?

**Rob Aldrich:** Positive employment growth.

**David Hamilton:** Right now the majority of our business is people moving around and/or downsizing. We need to see expansion and companies moving into our market. We need to see job creation and not job losses.

**Patrich Jett:** Liquidity and job creation will be required for sustained recovery in the economy and commercial real estate market. Once public access to capital is readily available, I believe we will see an accelerated recovery.

**Bill Kinley:** Our measure, as people who are renting space, is the amount of interest when a space becomes vacant...It's slower re-renting right now.

**Cam McCausland:** Job growth. As discussed before, it is the only factor that matters. Without it, there is no need for real estate.

**Ted McMullen:** When employment increases, the lending climate improves and there are lowered business taxes. These will stimulate expansion and relocation, but it all starts when corporate decision makers 'get off the fence' and make decisions regarding the growth of their businesses. This is when the phones will start ringing again.

**Ed Shaffran:** Jobs.

**Neal Warling:** I think that recovery is already in sight, as indicated in a fairly sharp increase in leasing activity over the past month or two. I think the key phrase, though, is 'in sight', as it certainly isn't upon us yet.

**Jim Chaconas:** The vacancy factor. When we see absorption, that will tell us that business is turning around.

## What's your best advice for sellers in today's market?

**Rob Aldrich:** Don't sell unless you absolutely have to.

**David Hamilton:** We have advised many sellers to hold if they can. If they have to sell, there will be less value than three years ago and three years from now. Seller financing is an advantage where a seller is able to offer it. Make sure you are making your real estate decisions based on the facts. Get advice from a commercial realtor who is an expert in the selling your of particular type of property.

**Patrich Jett:** Take what you can, when you can, if it makes economic sense; it may be a while before you have another opportunity in front of you.

**Bill Kinley:** Unless it was a (lender-)forced sale, I wouldn't put something up for sale.

**Cam McCausland:** Hold on, if you can. Pricing is going to have downward pressure for the foreseeable future.

**Ted McMullen:** If you have a choice, don't sell now. Otherwise, expect 50-70 percent of your asking price, depending upon how realistic it was in the first place.

**Ed Shaffran:** Unless you absolutely have to, hold.

**Neal Warling:** Don't.

**Jim Chaconas:** The person who's working for you had better be marketing your property. If there's a needle in the haystack, they'd better know it's there.

## And what about advice for tenants?

**Rob Aldrich:** Be mindful of the capital foundation and financial strength of your landlord.

**David Hamilton:** Tenants are already asking for discounts, free rent, or leasehold improvements. If your company is strong, this may be the time to negotiate for a long-term lease at today's lower rates, if they can find a landlord willing.

**Patrich Jett:** Timing the market is not a strategy; pulling the trigger and taking advantage of an aggressive market while you can is. This will also reduce your exposure to change and risk. An early renewal is a great way to save money on real estate costs and most landlords are happy to reduce rent to extend a term.

**Bill Kinley:** If they are having financial problems, they should talk to their landlords.

**Cam McCausland:** If possible, go out and make a new deal. Everything is on sale, take advantage.

**Ted McMullen:** Do what you need to do to hang in there, because good times are in front of us. I really believe at the end of this recession/depression there is a boom waiting for us. In the meantime, shop the market and stick to the good owners and managers.

**Ed Shaffran:** Investigate your options. Landlords/owners might be willing to make some concessions today in exchange for a new longer-term lease.

**Neal Warling:** There is no better time to go shopping.

**Jim Chaconas:** If you can lock in a deal, do it now. If you're going to renegotiate, do it now.

## Just how tight is lending right now?

**Rob Aldrich:** Debt sources are scarce. The little money that is out there is looking at 65 + percent loan-to-value ratios on stabilized properties.

**David Hamilton:** It works for the owner-occupant as there is Small Business Association coverage that limits the bank's exposure. For investors it is difficult to find, and the down payments are much higher making the investment less attractive. For developers there is very little if any. Seller financing is an advantage.

**Patrich Jett:** Too tight. At some point the pressure needs to be released, or the economy will deteriorate further. It is not acceptable for banks and lending institutions to dictate the future of good business owners and real estate investors.

**Bill Kinley:** It appears to still be quite tight. We haven't gone out to borrow, but we've had some prospective tenants look for startup lending, and that's very, very hard to do.

**Cam McCausland:** As tight as it gets. There is no lending at reasonable terms.

**Ted McMullen:** With a good project, good credit and good equity, reasonable lending is available, especially from small banks that have been smart in the past, enabling them to be aggressive now.

**Ed Shaffran:** Individuals or entities with good credit and a good track record will continue to be in the driver's seat. 'Fogging a mirror' is no longer the sole qualification for a loan nowadays.

**Neal Warling:** Still extremely tight, unless you are an owner/user and can take advantage of Small Business Association programs.

**Jim Chaconas:** Very tight. The conduit market is gone. One thing we're seeing, though, is banks renegotiating deals instead of foreclosing on them. ... Still, financing demands higher equity today.

## How will your business change in 2010?

**Rob Aldrich:** Very little. We will continue to focus on tenant service and maintaining our properties at the highest level in the market. We will continue to seek acquisition and development opportunities in Ann Arbor and western (primarily Colorado) markets.

**David Hamilton:** Like many others, we had already 'right-sized' to keep pace with the declining market. Swisher Commercial is looking forward to an uptick in business, but we expect another tough year before we get there. Most importantly, we are here in our 40th year to give our clients the expert advice on the local commercial market they need the most in 2010 and beyond.

**Patrich Jett:** Same business model, same value: focus on great clients and provide them with the highest quality real estate consulting service. However, I would like the pleasure to focus on a few new job creation projects in the region. That would make

2010 great.

**Bill Kinley:** We're going to do more marketing. Our new Web site went live last week.

**Cam McCausland:** Continue to gain market share, brokerage companies will consolidate, less providers in the market. We can have good activity going up or down, we cannot have inactive markets.

**Ted McMullen:** Our business will not change one bit, and we will continue our same philosophy: maintenance updates come first, tenant requests are a close second and hard work by every employee is continued.

**Ed Shaffran:** Minimally, if any. Continue to focus on servicing tenants needs. Some capital projects may get scaled back or delayed, however, it is important to keep up with building maintenance and repair issues.

**Neal Warling:** I have never gone into a year with more uncertainty or trepidation that I will be going into 2010. Market forces will determine our business, and we will have to be more 'light on our feet' than ever before in reacting to opportunities that present themselves. I do believe that more (banks') real estate-owned properties will come available in 2010, which will continue to create some downward pressure on rental rates and sale prices, as banks and other lending institutions rid themselves of non-performing assets. This will force the owners of certain competing assets to adjust their pricing quickly so as not to lose leasing or sale opportunities.

**Jim Chaconas:** We'll shift more toward the Internet. And I'm starting my own website. You've got to be able to find people better, so we're investing in new ways of marketing. One example is how we're bringing the online virtual tour (found in residential listings) to commercial real estate.

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