



It isn't always 'location, location, location'

By JASON HUGHES

Monday, March 5, 2007

In a column some time back, I had occasion to quote a leading national real estate investment specialist as saying: "E-commerce is changing real estate's maxim from 'location, location, location' to 'location, price, service.'"

He's right, but the trend extends far beyond the needs of e-commerce office tenants. When you think about it, those three determinants of value apply universally throughout today's commercial real estate market.

Location, of course, continues to be the chief virtue in real estate. Few would argue that downtown San Diego and downtown Ramona compete for the same users or fetch the same leasing rates. But in today's competitive real estate market, location can become an exaggerated value if price and service factors are ignored.

Office space shoppers need to broaden their concept of what constitutes real value in office space. The typical tenant prospect being hustled about by the building-owner's leasing agent doesn't have the means to assess true value. The tenant looks out the window and sees a city or bay view. He or she is shown the convenient underground parking garage and is impressed the parking spots assigned to the space are close to the elevators. Ah, yes, the restrooms seem clean and tidy and the elevators are conveniently situated and appear to operate efficiently. Sure, there are a few maintenance problems that are immediately apparent, but, hey, the space is a little cheaper than what's available down the block, and the broker is quick to point out the great deli in the building lobby. And, it's downtown as well. Where do I sign?

This all-too-common approach is a good example of placing undue emphasis on location. Finding the best value in office space doesn't come as a result of taking a quick tour of all the available office spaces.

Determining real value takes professional insight into price and service factors -- things that are not readily apparent if location is considered as the primary value. This is a good place to say it isn't a matter of substituting the location factor for either price or service as singular alternatives. All three must always be included in any complete assessment of real estate value.

An example of a tenant looking for 5,000 square feet of office space can illustrate how location, price and service factors need to be equally considered.

Our tenant here has found two spaces, each the same size and within the same general location. One space is a dime per-square-foot cheaper. However, additional research reveals the building management does not have any reserve fund set up for deferred maintenance. The other space is in a building where such a fund is in place. The \$500 per-month premium for the "more expensive" space could easily be the bargain if there is considerable maintenance required over the period of our tenant's leasehold.

Now, let's extend our tenant example to take into account the service factor. Location factors in our example are relatively the same and even the leasing rate and reserve funds are equal. One of the buildings, however, doesn't have a management staff that is adept at keeping common areas and equipment up to par. That will be important the next time one of the elevators breaks down due to poor maintenance and our tenant is stuck between floors.

I can't leave this topic without talking more about location in the three-part equation. Location is often important in creating positive perceptions on the part of a tenant's employees.

I'll use downtown San Diego as the baseline. For example, while Sorrento Mesa may have larger building footprints and therefore typically more efficient layouts for technology users, downtown San Diego has many cultural benefits -- a great selection of fine restaurants, better access to public transportation, entertainment and the excitement of being in the bustle of a dynamic area. That creates more robust value.

For some office users, being able to walk up a downtown street to see an accountant, banker, attorney or other clients creates a positive synergy that the location factor solely provides. For others, proximity to areas of the county where many employees live is an important location value. Downtown is far closer and more accessible to the bedroom communities in South and East counties than Sorrento Mesa and other northern locales.

The point: All three value factors need to be weighed and taken into account if tenants are to find true value in today's commercial real estate market.

Hughes is a principal with Irving Hughes, San Diego's largest tenant representation company. E-mail: jasonh@sddt.com. Comments may be published as Letters to the Editor.

