HOW LEASE ENGINE PROVIDES LEASING PROFESSIONALS THE ADVANTAGE BY HELPING LANDLORDS PROFIT

A Case Study in Why Broker Net Effective Rents are Meaningless

To start, lets begin with a basic leasing example. This is essentially your leasing budget to re-tenant what we will call a single-tenant building. In this particular example, with the exception of leasing commissions, your working capital account as "Landlord" has exactly $80.00 PSF remaining for Tenant Improvements – that's it. To summarize, your bank account balance less leasing commissions is $8,000,000 (or $80 in Tenant Improvements x 100,000 sf).

Landlord Example	
Perspective:	LANDLORD
Lease Start:	09/15/18
Lease Term:	10.0
Lease End:	09/14/28
Market Start Rent:	$24.00
Rent Increases:	1.50%
Rent Increment (Yr):	1.0
Rentable SF:	100,000
Tenant Improvements $/PSF:	$80.00
Leasing Commissions (Months 1-60):	5.00%
Leasing Commissions (Months 61 +):	2.50%
Discount Rate	10.0%

Within a week of closing on your single-tenant building, a Tenant approaches you through a Broker and would like to lease the space. However; the Tenant requires $150.00 PSF in Tenant Improvements – Not $80.00 PSF. What do you do?

The old-time Broker says "no problem, I have a spreadsheet that will compute Net Effective Rent ("NER"), which will easily determine where you need to be in terms of rent". The Broker uses his old rule-of-thumb calculation and arrives at $30.79 PSF in Starting Rent.

It is precisely at this moment that you as Landlord identify two fundamental problems with this method, one (1) where does the additional $70.00 PSF come from, and two (2) what is the Cost of

Capital required to sign this lease? By simply raising Starting Rent to $30.79 PSF, your Landlord bank account doesn't automatically fund itself with the additional $7,000,000 required to sign the lease – it must be borrowed. This is the logical conundrum of what we now know as Broker Net Effective Rent. It not only makes no sense in pricing leases (as in this example), but also has no premise in the broader property markets where Landlords must always weigh the cost of borrowing with their ability to profit.

Now, let's look at direct comparison between Broker Net Effective Rent and the Common Net Effective Rent which we will call "Net Effective Rent - Standard" recommended by one of North Americas largest consortiums of property investors, comprised of institutional public and private investment companies, Real Estate Investment Trusts, life insurance companies and pension funds.

The key difference between the two Net Effective Rents should be self-evident – one includes the time-value-of-money "cost of borrowing" (in either debt/equity or WACC), and the other ignores it completely.

From our example above the differences to the Landlord could not be clearer.

	Net Effective Rents Are Not Equal When It Comes to Profit	
	Net Effective Rent - Broker Example (Broker Computation)	**Net Effective Rent - Standard** (Investor Computation)
Annual - Starting Rent $PSF	**$30.79**	**$34.94**
Annual - Starting Rent	**$3,079,200**	**$3,494,200**
Loss in Rent Year-1	**($415,000)**	**$0**
Total Rent over Lease Term	**$32,955,821**	**$37,397,450**
Loss in Rent over Lease Term	**($4,441,629)**	**$0**
Net Present Value	**$4,698,164**	**$7,353,206**
Loss in Value over 10-Years	**($2,655,043)**	**$0**

For a tutorial on how to use the Lease Optimizer Technology built-into Lease Engine, please see the following pdf: TUTORIAL: HOW TO OPTIMIZE A COMMERCIAL PROPERTY LEASE

For a detailed discussion on the Net Effective Rent – Standard used within the F9Analytics Technology and recommended by the Appraisal Institute and one of North Americas largest commercial property investment consortiums; including REITs, Pensions Funds, and the largest private and public investment companies, please see the following pdf: REALPAC/ AIC - Common Net Effective Rent