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Office-Leasing Rebound Could Be Deceiving

Tenants Signing Commitments Often Take Less Space, Give Less Room to Each Employee

By ANTON TROIANOVSKI

Even as the office market enjoys a rebound of leasing activity, some businesses are giving landlords the shivers by figuring out how to use less space per employee.

Companies that sat on the sidelines during the darkest days of the economic downturn are increasingly making leasing commitments. In the 12 months that ended June 30, office tenants signed 161.3 million square feet in leases nationwide, according to Studley, a commercial real-estate brokerage firm. That is a 5.7% increase over the 12-month period ended in March.



Mark Ovaska for The Wall Street Journal

Deloitte asked for tax breaks to support a consolidation of offices at 4 World Financial Center, Merrill Lynch's previous location.

But in many cases, tenants are taking less space than they had before—both because they have fewer employees and because they are able to use space more efficiently. In New York, for example, three of the five largest deals of the second quarter involved tenants either taking the same amount of space or less.

"Until tenants shift into expansion mode ... the market will be engaged in a process of musical chairs," states Studley's second-quarter report on New York.

The trend bodes poorly for an office market struggling with a national vacancy rate of 17.4%, the highest since 1993, according to real-estate research firm Reis Inc.

Concerns are particularly acute for the hundreds of office properties that are in precarious financial condition because they are worth less than the mortgages that were made during the boom years. They need to fill space to boost rental revenue—and values.

"People should temper their expectations about how quickly office space will be leased up," said Victor Calanog, research director for Reis. "Where there are leases being signed, companies are trying to be efficient with the space they're using."

Businesses aren't expanding as much partly because they are uncertain about the strength of the economic recovery. They also are figuring out how to use less space per employee by setting up more-collaborative work environments.

Law firms are increasing the number of attorneys assigned to a single secretary while eliminating libraries and filing areas. Corporations moving into new offices often are asking architects for open floor-plans and fewer offices. The White House is asking federal agencies to look for ways to consolidate offices and cut the amount of space they use.



NRG Energy Inc.

NRG Energy is cutting office space in Houston by moving into an open-plan work space modeled on its Princeton, N.J., headquarters, above.

In Houston, [NRG Energy Inc.](#) is moving out of 260,000 square feet across two buildings into less than 220,000 square feet of office space in a new property, Houston Pavilions.

The New Jersey-based power company's employees will work in a space with no enclosed offices, reducing the amount of space per employee the company needs to pay for, and, executives say, helping people work more efficiently.

"You get efficiency from a real-estate standpoint, but you gain even more efficiency from the way people interact or share information," Denise Wilson, NRG's chief administrative officer, says.

Law firms have been among the most aggressive in reducing their space. Law firm Baker & McKenzie recently signed a lease to move its offices into 237,000 square feet down the street from its current home in Chicago's East Loop, allowing it to reduce space per attorney to about 700 square feet from 1,000 square feet, according to [Jones Lang LaSalle Inc.](#)'s Bill Rogers, who brokered the deal.

Landlords have taken note. [Boston Properties](#) President Doug Linde said in a conference call with analysts last month that law firms were looking to reduce their overall footprint by 10% to 15%—both because they no longer need many spread-out

conference and file rooms and because they have yet to rehire laid-off employees. "We have seen a clear change," Mr. Linde said, according to a transcript.

More efficient use of space could help reduce office demand even when the economy recovers—adding to the hesitation that most real-estate developers feel about investing in new buildings.



The trend "is an impediment for new construction," says Richard LeFrak, head of LeFrak Organization, a large private developer in New York. "We have all this supply from within. You have to be cautious now."

In New York, accounting giant Deloitte recently asked the city for \$11 million in tax breaks that would support a consolidation of its New York offices at 4 World Financial Center in downtown Manhattan. Under the lease deal, which isn't final, Deloitte—which now occupies some 934,000 square feet of office space in the city—would eventually move those operations into just 390,000 square feet at 4 World Financial Center, with options to expand to 630,000 square feet.

Deloitte would spend more than \$90 million on building and fitting out the space with a new, more efficient design, according to its application for the tax breaks. A Deloitte spokesman declined to comment on the design plans.

The federal government also is looking for more efficient office space. President Barack Obama in June sent a memo to federal agency heads urging them to squeeze \$3 billion in costs out of their real-estate portfolios by the end of the 2012 fiscal year by, among other things, consolidating into unused office space and increasing the number of people who can work in an office. Past efforts at cutting the government's real-estate footprint, Mr. Obama wrote, "did not emphasize making more efficient use of existing assets."

Interior architects and furniture designers are taking advantage of the movement by working with companies that want to squeeze more people into less space and create more collaborative work environments. Andrew Garnar-Wortzel, a principal at architecture firm Gensler, said flexible workbenches that allow different numbers of people to occupy the same work space are increasingly common.

In the financial sector, Mr. Garnar-Wortzel said, many companies are trying to reduce their footprint to 200 square feet a person or less. Ten years ago, on the other hand, financial firms were looking to reduce their space from 300 square feet to 250 square feet a person, he said.

Pittsburgh-based banking giant [PNC Financial Services Group Inc.](#), for example, found itself with more than 300 square feet a person after its merger with Cleveland bank National City Corp. in late 2008. It recently put in place new guidelines that call for about 180 square feet an employee in new offices, according to the company's director of corporate real estate, Gary Saulson.

Write to Anton Troianovski at anton.troianovski@wsj.com

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