



ADVANTAGES OF LEASING COMMERCIAL SPACE

Leasing rather than owning commercial real estate gives business owners flexibility, liquidity, and someone else to worry about repairs and maintenance.

Flexibility

Flexibility from leasing commercial real estate can be beneficial in two ways. First, leasing allows a business owner to grow or shrink the footprint as the business changes. If a business is growing and the landlord is unable to accommodate that growth, the tenant can move, sub lease the existing space or work with the landlord to turn back the space. This is much more challenging when a business owns its own real estate and needs to sell property in order to grow. Selling real estate takes much more time and risk associated with values that may not be where they need to be at the time of the sale. The same issues apply when a company is downsizing, in which case if the business owns its own space, it will need to sell, or sub divide and lease a portion of the space. Thus, becoming a landlord and shifting focus from core business operations.

Secondly, in addition to a business growing and shrinking, leasing provides flexibility when a company starts to consider an exit strategy. The sale of a business often requires some or all of the business to relocate. If the business owns its own real estate, the decision to sell at an optimum time might be impacted by the real estate market. Real estate values are volatile and there are many factors combined that determine the assessment of the property. Depending on the timing, the worth of the property may remain stagnant, or drop in value at a time when a business owner can least afford to incur a loss.

Liquidity

For many business owners, preserving cash for operations is often the primary reason leasing is more appealing than owning. Buying commercial real estate usually requires a large amount of cash up front to fund the equity and closing costs. While there are government sponsored programs such as the SBA that can offer loans with as little as 10% down, most commercial loans require 25% or more in upfront equity. That coupled with closing costs compromised of points, legal fees, title insurance, environmental studies, appraisals, and more, results in a large cash commitment that will be tied up for many years by the owner.

In addition to cash up front, real estate requires ongoing capital improvements such as replacement of roofs, HVAC systems, lighting upgrades, etc. Business owners have to chose where to deploy their cash, which is a scarce resource especially for early stage businesses. Tying up cash in real estate in lieu of

investing it into the R&D, personnel, operations or marketing is a decision that many business owners choose not to do. When leasing, a business will typically limit its cash commitment to a security deposit and leasehold improvements, significantly less than the upfront cash required when owning. An additional benefit of leasing allows ownership to leverage their credit for operating the business rather than real estate.

Repairs & Maintenance

While leasing space requires the business owner to find a responsible landlord who has an excellent track record for repairs and maintenance, remodeling and capital upgrades, once they find a reputable landlord, the headaches and costs of property management are with someone else. Real estate requires day-to-day repairs and maintenance, as well as long-term capital improvements. A business owner managing day-to-day repairs and maintenance of a building will inevitably compromise time invested into the business. This is especially important for small and startup companies who need to focus as much management time on growth as possible.

Capital projects consume even more management time. Time away from the business is time away from growing a business. Many landlords have strong relationships with trades, such as architects, and engineers that allow them to manage repairs and maintenance and capital projects in a time and cost efficient manner. In some circumstances, landlords have onsite management and staff to provide quick responsive service to the tenants and their guests. This is especially beneficial in New England where a sudden snowstorm can shut down business operations if not addressed in a timely manner.

Leasing commercial real estate makes sense for early stage and many established businesses. There are a lot of variables to consider when leasing rather than buying. Flexibility, liquidity, and repair and maintenance are just some of the issues for a business to consider when making a decision. There are also many aspects that center on financial, tax, and personal issues. Business owners should be sure to invest enough time to perform a cash flow analysis when choosing between leasing and purchasing space. They should also discuss both alternatives with an accountant and/or financial planner in order to make the best-educated decision as to which opportunity better suits the business at hand.

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