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## Is Now a Good Time To Buy? Leasing versus owning in a soft market

By John Schnoebelen  
Broker Associate, RB Murray Company

Not surprisingly, "Should we lease or buy" is often one of the first questions businesses ask brokers when searching for commercial property. In light of the current bear market conditions, businesses may be more inclined to consider purchasing under the guise of "getting a better deal" than that offered during a bull market. This may or may not be the case depending on the property's location, forecasted growth in the area, as well as the current owner's exit strategy.

Though market conditions are important, equally important is the stage of the business: cash flow needs, type and size of space, trade area, franchise value, growth objectives, and ability to obtain financing, to name a few.

### Advantages of Owning

Certainly, appreciation is a benefit that owners realize in addition to control over rent prices. Locking in a fixed mortgage enables owners to control expenses long term. In fact, control is often cited as a reason why businesses decide to purchase. Owners have the freedom to operate the facility as they see fit and to "avoid the boot" by landlords who may elect not to renew a lease.

Income potential is another advantage of ownership. Owners may use rent money from excess space to pay down their mortgage, fund their primary business or invest in other ventures. Owners also reap the benefits of any improvements made to the property whether they are made by themselves or by renters.

From a tax standpoint, owners are able to deduct the mortgage interest, property taxes, and depreciation. Businesses should consult with their tax advisor on additional cost-recovery opportunities that may result from commercial property ownership.

With all this said, it generally makes the most sense to buy when a business is in a mature phase. Space needs are established, growth trends have leveled out and a larger cash reserve has been established.

### Advantages of Leasing

Flexibility is the name of the game when it comes to leasing space. Businesses that are still exploring their space and location needs can make an average three-year commitment, after which time they are free to renew or move. Typically, a one-month deposit upfront is the bulk of the investment beyond monthly rent whereas purchases often require a 20% down payment. Renting also means less

responsibility with much of the maintenance burden resting on the owner's shoulders. Renters are able to wholly focus on their core business and utilize capital to invest in business growth.

Renters also benefit from a tax standpoint since lease payments are fully tax-deductible. If the lessee pays operating expenses in addition to rent, they are deductible as well.

Overall, leasing makes a lot of sense for startups or rapidly expanding (or contracting) businesses. In fact, some small or marginally profitable businesses may not qualify for mortgage financing, thereby making leasing the only solution. Sometimes a lease with an option buy at a designated time in the future can be an option, allowing a renter to lock in a desirable location while providing a grace period for reserving cash to fund the future purchase.

### What The Market Is Saying

According to a recent article in \*Financial Week, U.S. commercial real prices did decline in June for the fourth straight month. The article quotes Lawrence Longua, a professor at the REIT Center at the NYU Institute of Real Estate. "Right now debt is expensive and it's not available. No one knows what real estate is worth, so people are only selling when they are compelled to sell."

With that being said, this is a good time for qualified buyers to take advantage of good, low rates and motivated sellers. In contrast, tenants can take advantage of the soft market and high inventory by negotiating rent rates and out clauses that maximize their flexibility.

John Schnoebelen, Broker Associate, RB Murray Company. John can be reached at (417) 881-0600 or john@rbmurray.com

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\*Financial Week, August 19, 2008 "Commercial Property Prices Fall For Fourth Straight Month," by Beth Braverman