Bleaker on Broadway: The Contractual Origins of High-Rent Urban Blight

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Abstract

We document the rise of storefront vacancies in prime retail locations, a phenomenon we refer to as high-rent blight, in America's largest and most expensive urban retail market: Manhattan. We identify a little-known contracting feature between retail landlord and their bankers that generates vacancies in the downstream market for retail space. Specifically, widespread covenants in commercial mortgage agreements impose rent floors for any new leases landlords may sign with tenants, short-circuiting the price mechanism in times of low demand for retail space. Quasi-experimental estimates suggest that binding rent floors imposed by mortgage covenants substantially reduce the probability of occupancy. We microfound this contracting feature as the solution to a moral hazard problem between landlords and banks. We show that while rent floor covenants increase vacancies, their absence reduces credit supply to landlords.