Welcome to Walkable Suburbia

Here's how savvy developers are turning old-school office parks into vibrant, mixed-use villages.

MARCH 2014 | BY BRAD BROBERG

Traditional suburban office parks are gray flannel suits in a skinny jeans world. Faced with adapting to change or becoming obsolete, the bland, old-school behemoths are increasingly getting mixed-use makeovers. The result is rave reviews along with a healthy stream of new occupants.

Originally built exclusively for business, office parks are evolving into vibrant villages as investors and developers strive to improve performance and add value through redevelopment. The result is a re-envisioned suburbia where people can dine, shop, and live—all within walking distance of work.

The move toward makeovers is the product of a triple whammy that hit the suburban office market during and after the Great Recession. First came the waves of layoffs that led to permanent corporate downsizing. Next came a shift to more open floor plans in offices requiring less square footage. The clincher is the perspective of a new generation of young professionals in their 20s and early 30s—the millennials—who have no interest in working in the same dull McOffice Park that their parents did.

It all adds up to an excess of suburban office inventory that is pushing developers to hit the reset button because employers no longer have the space needs they once did. "There's definitely too much suburban office right now—substantially too much," says Dane Anderson, CCIM, director of appraisal and litigation services with Real Estate Research Corp. in West Des Moines, Iowa. The nationwide vacancy rate for suburban office space was 16 percent as of the fourth quarter of 2013, according to the commercial real estate services firm Newmark Grubb Knight Frank. If over-supply is the problem, mixed-use makeovers are a potential solution in places where job growth is strong and there's also high demand for multifamily and retail.

Helping Workers Feel at Home

To recruit and retain top talent, employers are eager to give millennials what they want: a walkable live-work-play environment. And suburban office parks can capitalize by giving employers what they seek: diversified environments where offices are surrounded by dining, entertainment, shopping, and housing. “It’s the new norm,” says Anjee Solanki, national director of retail services with Colliers International in San Francisco. “People are expecting it.”

That’s the vision Advance Realty and CrossHarbor Capital Partners LLC have for a vacated biotech campus in Bridgewater, N.J., which they bought for $45 million last year from a global pharmaceutical company. After getting a “good deal” on the campus, they hope to begin redevelopment sometime this year, says Peter Cocoziello, president and CEO of Advance Realty.

The campus, renamed the New Jersey Center of Excellence, contains 1.2 million square feet of offices and labs on 110 acres. While most of the office and lab space will remain, the new owners plan to demolish some of it to make way for multifamily housing (apartments, townhomes, and condos are all being considered), retail, and a hotel, as well as a new corporate headquarters building for an unspecified occupant. When redevelopment is complete, the overall footprint will grow to between 1.5 million and 1.7 million square feet, Cocoziello says.

The new owners found takers for 360,000 square feet of office and lab space in the first few months after buying the mothballed campus. A central location and state-of-the-art labs are big carrots for tenants, but so is the pending addition of apartments, retail, and a hotel.

Advance Realty typically holds properties for a period of time while they gain value, Cocoziello said. Current rents at the New Jersey Center of Excellence vary from $20 to $35 per square foot. “As I keep building out the product, I should be able to get better pricing,” he says.

Retrofitting for the Times Continental Park in El Segundo, Calif., has already traveled the path the New Jersey Center of Excellence is on. The 86-acre office complex once teemed with workers from the aerospace industry, but when defense spending began to shrink in the 1990s, the buildings began to empty. “We had to rethink what to do with the property,” says Alex Rose, senior vice president of Continental Development Corp.

Most of the buildings had been occupied by single large tenants. Continental Development steadily began retrofitting the buildings to fit multiple tenants. Then it began adding restaurants, shopping, hotels, fitness centers, and a movie theater—all served by a light rail stop. “Once you get the cycle going, it feeds on itself,” Rose says. With 3 million square feet of mixed-use space and an office vacancy rate below 5 percent, Continental Park found the right strategy to turn things around. “By taking a mixed-use approach, we think we did a good job of listening to our market,” Rose says. “We’ve been able to keep our rents up, keep occupancy up, and attract tenants that perhaps our competition can’t.”

Invesco Real Estate and SSV Properties of Ontario, Calif., bought four office buildings in Continental Park totaling 540,000 square feet for an undisclosed amount last year. One was fully leased, but the new owners are spending an estimated $75 million to convert the other three to open floor plans that support workplace collaboration.

Continental Park’s mixed-use environment was a key factor in the decision to buy the buildings as a long-term investment, said Peter Cassiano, director of acquisitions for Invesco. “The way officing is going right now, folks want the [mixed-use] environment and amenities,” he says.

Garrick Brown, director of research with Cassidy Turley in Sacramento, Calif., is bullish on mixed-use makeovers. “There are plenty of markets where this would solve an awful lot of problems—especially if you can incorporate multifamily in the mix, because that’s where the strongest demand is,” Brown says. “The only reason we haven’t seen more [mixed-use redevelopment] is cost.”

Many underperforming office parks can’t afford mixed-use makeovers because the owners don’t have the capital. They don’t have the capital because the property is underperforming. The only escape from this Catch-22 is acquisition by new owners with deeper pockets, Brown says.

Investing for the Long Haul

Synergy Business Park in Brentwood, Tenn., wasn’t necessarily underperforming when Boyle Investment Co. bought it for $62.8 million in 2012 with an eye on giving it a mixed-use makeover and holding it as a long-term investment. The 500,000-square-foot complex—since renamed CityPark—was at 90 percent occupancy at the time of the sale and climbed to 96 percent occupancy with a bump in rents before the makeover even began earlier this year. “It wasn’t an issue of needing to redevelop the property due to increased vacancy and declining rents, but more an issue of us wanting to enhance the property ... so that it adds value and succeeds both now and 30 years from now,” says Shelby Larkin, a Boyle spokeswoman.

Boyle got good value by purchasing the property in a downturn, Larkin says. Construction is underway on 40,000 square feet of retail and restaurant space, a 126-room Hilton Garden Inn, and a one-acre park—all within a stroll of a 300-unit upscale apartment complex another developer is building nearby. “There really won’t be anything like it in Brentwood,” Larkin says.

North Carolina's iconic Research Triangle Park will start construction later this year on the first of three planned mixed-use clusters. Phase one consists of 1,000 apartment units, 200,000 square feet of retail, and 700,000 square feet of new office and research space.

The triangle in Research Triangle Park refers to three surrounding universities: the University of North Carolina in Chapel Hill, North Carolina State University in Raleigh, and Duke University in Durham. The vast park, founded in 1959 and now home to 170 companies with more than 38,000 employees, created an identity for the region as a center for innovation, but the park is a laggard when it comes to urban amenities. "Research Triangle Park is 7,000 acres—that's half of the size of Manhattan—and you can't buy a latte anywhere," says Bob Geolas, president and CEO of the Research Triangle Foundation, which manages the campus. "We want to make sure the park stays at the forefront. If the park was viewed as a dinosaur, that would impact the Research Triangle brand."

The overall vacancy rate in the 21 million square foot park is 3.34 percent, but most buildings are owner-occupied. The vacancy rate is 18.9 percent in the 4.3 million square feet of space that is under lease. Lee Clyburn, sior, principal with Avison Young, a commercial real estate firm in Raleigh, N.C., says adding a live-work-play flavor should help Research Triangle Park improve occupancy. "I think adding amenities to the park will help all of us attract more tenants and lease more space out there," Clyburn says.

Transportation Game Changers

Some suburban office parks are better positioned for redevelopment than others. The presence of transit options and support from local government for any needed zoning changes are game changers. Redevelopment was a nonstarter in Tysons Corner, Va., until the Washington, D.C., Metro decided to extend light rail service to the unincorporated suburb—four new stations will open this spring—and Fairfax County approved greater density.

With 26 million square feet of office space and a workforce of 110,000 people, Tysons Corner is a "tremendous employment and economic engine," says Eric Maggio, vice president and chief financial officer at CityLine Partners, a leading developer and owner of office and commercial property in Tysons Corner. "The problem is it's just a collection of office parks and a large shopping center. It's not a livable place."

CityLine is in the opening stages of a sweeping live-work-play makeover that could total up to 8.5 million square feet of residential, retail, and office space over the next decade and beyond. Construction is underway on 1,575 apartment units. "You can continue to operate old office parks, but you're chasing falling revenue," Maggio says. "Corporations are no longer in the mode of wanting office buildings where all their employees have to drive to work."