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WESTERN REAL ESTATE BUSINESS®

Connecting Real Estate in the West

Tiffany and Co. used Valentine's Day as the ideal time to launch its first pop-up at Caruso's the Grove in Los Angeles.

WHEN RETAIL IS YOUR 'SPECIALTY'

The retail industry has seen an uptick in specialty leasing activity as tenants require new space, and previously online-only companies wade into brick-and-mortar.

By Nellie Day

The success of today's shopping centers lies in the experience. There is much focus nowadays on the in-line tenants, in addition to a center's special events and social spaces. This leaves out what has become an increasingly large piece of the puzzle, however. Specialty leasing used to be confined to pretzel vendors and acne medication kiosks, but that is no more.

Today, specialty leasing involves so much more as brands and shopping center owners have embraced the notion that consumers thrive on new, novel and, oftentimes, temporary. *WREB* spoke to three specialty leasing experts — a property manager, specialty leasing broker and a company that brings temporary activations to life — to get the latest on this ever-evolving category.

see SPECIALTY RETAIL, page 36

MULTIFAMILY CONSTRUCTION IS A BALANCING ACT IN TODAY'S ECONOMY

The multifamily market in the West has many pros — but it also has many cons as investors, lenders and contractors work to get projects done.

By Nellie Day

Eden Housing and Alameda Point Partners are constructing the 60-unit Alameda Point Senior Apartments at Alameda Point, a creative reuse project just south of Oakland, Calif.

The world seems to work most efficiently when balance and moderation are in effect. This strategy is particularly true of today's multifamily development pipeline out West. The current market is all about supply and demand, ensuring that resources aren't spread too thin and weighing priorities, which tend to create an imbalance between the haves and the have nots.

"Notwithstanding the pickup in activity we had in 2018 and notwithstanding the fact that Millennials are still looking at apartments as opposed to single-family homes, we view multifamily housing as one of the more vulnerable parts of the construction industry right now," said Robert Murray, chief economist at Dodge Data & Analytics, during a presentation at Le Meridien Perimeter in Atlanta in June.

The broad issues impacting the nation's multifamily construction industry include trade tensions with China, a tight labor market, economic uncertainty, a $1 trillion deficit that may limit government spending and the increasing costs of materials. The Producer Price Index for construction materials jumped 6.4 percent last year,

see MULTIFAMILY, page 37

INSIDE THIS ISSUE

CRE BEGINS TO COME AROUND ON TECHNOLOGY

The commercial real estate industry is good at many things, but remaining on par with the latest technological advancements hasn't been one of them. Thankfully, however, the industry is beginning to play catch up as it embraces what this new digital and automated world has to offer.

IT'S TIME FOR CRE TO CATCH-UP WITH NEW TECHNOLOGIES

By Bruce Greenfield, Principal, Architects Orange in Orange, Calif.

Greenfield

The past three decades have been marked by staggering changes in technology that have dramatically impacted nearly every aspect of our personal and work lives. These changes have set new expectations for speed, convenience, increased productivity and better communication. From finance to agriculture, manufacturing to media, global industries have evolved and learned to leverage technology to better serve their businesses.

Yet, commercial real estate continues to lag behind. Our industry isn't quite taking advantage of all the benefits technology has to offer to expedite project timelines, reduce costs and promote greater partnerships between project team members. Now is the time for the industry to jump on the bandwagon and get brought up to speed on how best to leverage forward-thinking innovations.

Below are two examples of technologies that have great potential to meet the expectations of both development partners and end users.

Virtual Reality: A Next-Level Communications Tool

Virtual reality (VR) has been around for a few decades, but it's only recently made its way into commercial real estate. Several obstacles are delaying its widespread adoption. These include hardware costs, training requirements and — the greatest challenge — a lack of understanding about its benefits for all project partners, including developers, architects, builders and beyond.

VR enables users to visualize a project like never before. Architectural drawings and models often lack the capacity to convey what it would be like to actually walk through and experience a space. This is where VR steps in to place a user right there, in the middle of a space. If a picture is worth a thousand words, virtual reality is worth a thousand pictures.

From there, the possibilities and benefits of VR in commercial real estate are nearly boundless. Some advantages are obvious, like the ability to offer virtual property tours. This practice is spreading widely across the office and retail sectors, allowing potential tenants to view spaces on their quest for a lease. Tenants searching for non-local leasing opportunities can narrow their choices down to a few preferred properties to visit in-person. Architects are also starting to use VR to walk clients through projects, allowing them to better envision what the final product will look and feel like. This proves invaluable when making key design decisions and providing feedback.

VR also removes physical and spatial boundaries, offering better ways to collaborate and solve problems faster and more efficiently. Picture this: all project partners are holding a meeting directly in the VR model to make changes to design and discuss construction progress in real time. Some VR software can even let users write notes on the walls directly inside the model. With this, you eliminate the delays involved in visiting a site, traveling across the country to meet in person, or realizing there are potential structural, mechanical and architectural conflicts. For example, a contractor doing a VR walk-through on a recent project noticed a duct was protruding from the ceiling. This is a fairly mild fix prior to construction, but one that would likely not have been caught without VR and could have caused major delays in the field.

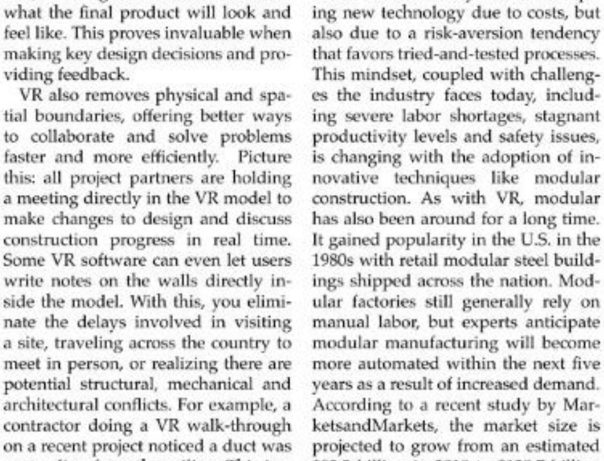
VR can also be used as a powerful ally in communication, particularly when it comes to presenting projects to council members, planning commissioners and neighbors. It has proven very effective in clarifying questions by bringing to life abstract concepts and renderings laid on paper. It also helps to inspire and generate excitement for projects.

Automation of Modular Construction Factories

The construction industry as a whole is notoriously slow at adopting new technology due to costs, but also due to a risk-aversion tendency that favors tried-and-tested processes. This mindset, coupled with challenges the industry faces today, including severe labor shortages, stagnant productivity levels and safety issues, is changing with the adoption of innovative techniques like modular construction. As with VR, modular has also been around for a long time. It gained popularity in the U.S. in the 1980s with retail modular steel buildings shipped across the nation. Modular factories still generally rely on manual labor, but experts anticipate modular manufacturing will become more automated within the next five years as a result of increased demand. According to a recent study by MarketsandMarkets, the market size is projected to grow from an estimated $92.2 billion in 2018 to $129.7 billion by 2023.

By automating modular construction factories, modular companies are able to improve key benefits that already set this technique apart from conventional on-site construction. Benefits include consistency, reliability and time efficiency. In fact, modular can currently reduce construction time by an average of six months. This enables contractors to lay down foundation while units are simultaneously being built off-site, shielding the project from potential delays. From there, it takes another one or two months to stack and then another four to six months to finish the facades and corridors. The construction schedule can be further shortened by accelerating the pace and volume of units produced through automation. Another anticipated benefit of automation is that modular will become much less expensive than conventional site-built construction, which is currently not always the case.

The screen above shows what a VR participant is viewing in real time.



VR tools can allow anyone, anywhere to tour a project that has yet to be built. This can be used as a power marketing or collaboration tool, as project managers weigh in on construction and design.

New sectors, such as hospitality and multifamily, are also dipping their toes into modular and finding it much to their liking. For example, Architects Orange recently completed the first modular Marriott Courtyard hotel in Los Angeles County. The construction of the hotel, which combines a 221-room Courtyard by Marriott and a 133-suite TownePlace Suites by Marriott, took about one year to complete, shaving an estimated six months off the project timeline.

Both sectors lend themselves to modular, as well as volumetric modular, where the appeal lies in the repeatability of units and design with entire units built and finished in the factory. In addition, these sectors already naturally follow modular patterns by stacking a single type of room or unit through several floors to optimize construction efficiency. Recent technological advancements are also enabling modular stacking to unprecedented heights, making it adequate for high-density, high-rise buildings.

VR and modular are only two examples of a myriad of promising technologies that have the potential to solve real challenges in the industry. This includes increased productivity, as well as addressing the needs and demands of consumers. To stay relevant and competitive in today's market, it's time for CRE leadership to trade their wait-and-see attitude for a more assertive adoption of new technology.

THE TECHNOLOGY EFFECT AFFECTS ALL AREAS OF THE ECONOMY, CRE

By Julie Melander, 2019 Chair, The Counselors of Real Estate

Melander

The Counselors of Real Estate identifies the current and emerging issues expected to have the most significant impact on real estate annually. Several topics are discussed, debated and voted on, culminating in the 2019-2020 Top 10 Issues Affecting Real Estate. U.S. infrastructure, housing in America, and weather- and climate-related risks are the leading concerns this year, according to the 1,100-member organization.

While technology ranks No. 4 on the list, many of the issues are interrelated and, thus, influence one another. Technology is going to drive capital markets, the use of space, leasing, brokerage, valuation and building operations. It may also make the actual location of a business less important.

It's no surprise the Technology Effect is a top 10, as it impacts nearly every area of our lives. The business of commercial real estate is no exception. Real estate has had somewhat of a different technology adoption path compared to other industries due to the bifurcation between the back-office technology and the front-of-house technology in buildings. This bifurcation became noticeable because back-office solutions and systems are generally in-step with tech advances in other industries, while buildings and the technologies that run them have been at least a decade behind when it comes to employing current-day tech.

While leveraging many IT attributes, the buildings themselves used a different type of tech called operational technology (OT), which was somewhat left behind. The OT building control systems, such as HVAC, elevator, lighting and parking, function and depend on computer servers, operating systems, protocols, local area networking (LAN) and remote Internet access. Those responsible for designing, installing and maintaining them for the past 40 years have neither IT nor cybersecurity skills. Thus, in addition to the bifurcation issue, there is a systemic risk that the entire building control system's value chain does not have IT skill sets, which has operational risk implications.

Notwithstanding those risks, all the back-office and building technologies are now beset by new technology leveraging the Internet of Things (IoT), big data, analytics, digital twin, artificial intelligence (AI) and blockchain. These are all moving faster than the industry can assimilate them. As a result, we see a wide variety of solution types, adoption rates, vendors and results.

Preparing For The Future

If this makes your head hurt, it's just getting started. The industry is moving into overdrive with increased intensity on occupant experience where all of this comes together in near real time. It involves tracking people and reacting with environmental conditions, amenities and responsive services, as well as dynamic billing or allocation. All of this requires integration and automation like never before.

The solution to all this is simpler than it sounds. Like we saw with smartphones and tablets, the more technology advances, the simpler it can be to have experiences and get results. Since no one expects real estate executives to be MIT technologists, our industry should not approach them this way. Instead, we should take a step back and rely on the fact that there is ample technology to support our most inventive desires for efficiency, experience and risk management. The real estate industry can start creating next-generation use-cases in real estate terms and not tech terms. Some large organizations have even disseminated RFPs with only use cases as the criteria, allowing the industry to determine how to respond, partner and fulfill the requirements.

In more general terms, organizations need to staff and organize around the realities of technology, including the speed of change, which is equally bringing risk and opportunity. It's important to measure twice and cut once. Underlying all of this is a need for new levels of cybersecurity that not only address data and hacking, but also the fragmented OT systems and contractors. The greatest risk is not adapting or changing quickly enough. This would be a competitive miscalculation, an impending operational risk or, more likely, both.

Technology enables shifts in consumer behavior. This includes the advent of ecommerce, which has impacted industrial real estate positively and retail somewhat negatively. Tech companies are the dynamic drivers of economic growth, leading to highly selective criteria for office locations. Emerging technologies could further impact supply chains via automated vehicles; warehouse space demand via robotics; delivery of medical services via seniors housing and medical office; data proliferation via data centers; and property security and marketing.

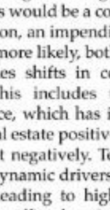
Technological advancements have a nexus to many of the selected issues in the Counselors of Real Estate's top 10 list. It's at the core of international trade issues, is a central driver in demand for the four primary real estate asset categories and is paramount to continued productivity gains.

Source: CBRE

Virtual kitchen map.

ORDER UP: RESTAURANTS SERVING UP TECH TO CUT COSTS, MEET DEMAND

By Dan Hunker, Research Analyst, CBRE



Hunker

If there's one thing Americans love to spend their hard-earned money on, it's dining out. U.S. consumers shelled out more than $1.5 trillion on food in 2018 — half of which was spent on restaurants.

For most of the early 2000s, the consumer price index for grocery items and for food and beverage (F&B) providers had pretty much stayed in tandem with one another. Ever since the recession, however, grocery expenditures have slowly dropped, leaving F&B spending to continue rising on its own. This widening gap is due to a number of factors. Namely, price deflation from farm-level goods for grocers and rising operating and labor costs for restaurants. According to CBRE Research's recent U.S. Food in Demand report, this chasm poses a risk for restaurants: if grocery items are cheaper than dining out, then what incentive is there for the consumer to forego the kitchen in favor of the dining room?

Creating a memorable experience for consumers is only one part of the equation. The other and, arguably, most important, is overall convenience. Since any conceivable item can be bought from the internet with a few simple keystrokes, restaurants big and small have been endeavoring to do the same with their own ordering apps. These apps allow customers to order and pay before arriving at the restaurant — thereby bypassing the line inside or at the drive-thru window. Combined with popular food ordering/delivery services like UberEats, DoorDash and Postmates, and it's easy to see that U.S. restaurants have been pulling in a sizeable amount of revenue from online ordering alone. This equated to roughly $30 billion, or 5 percent of total restaurant sales, in 2017.

While convenient for the consumer, this does, inevitably, place additional strain on food and beverage operators to keep up with a deluge of additional orders. There are some restaurant operators that have approached this problem with a unique solution: move online-fulfillment offsite. Located in the heart of Nashville, Chick-fil-A recently opened a 5,800-square-foot location to solely satisfy online and catering orders. Without a traditional dining room, more than two-thirds of the leased space is taken up by the kitchen — double the size of a typical Chick-fil-A kitchen — and reserved for only one purpose.

Other restaurants have taken a similar approach to dealing with online ordering, but in a more cost-effective manner. Chipotle, for instance, has no plans to open stand-alone online ordering facilities, but instead is looking to streamline the ordering process in their established retail locations. Dubbed "second make," a select few Chipotle locations will play host to computer-assisted assembly lines that help workers complete online orders faster and with much better precision than before.

Then there are virtual kitchens, an emerging, attractive cost-saving alternative to restaurants of any size. Like the commercial kitchens utilized by caterers and food trucks, virtual kitchens (VKs) can house dozens of varied restaurants at a fraction of the cost of a traditional retail space. Besides cost, VKs remove the burden of online fulfillment from regular restaurant locations and decongest parking lots and drive-thru lanes.

Online food ordering is looking to be a massive money maker for food and beverage operators in the years to come. Online food sales are expected to reach upward of $25 billion by the early 2020s. Morgan Stanley estimates sales in Southern California will reach nearly $220 billion for the whole U.S. in the same period. That isn't to say there won't be bumps along the way. Ordering apps reportedly take a 20 to 30 percent cut of each sale. With some small restaurants operating on razor-thin margins, this may be too high a price to pay.

Online shopping has come a long way since the dial-up days of the early 1990s. Back then, the idea of ordering food online was mocked as a languid act by maladjusted homebodies. Nowadays, it's hard to imagine a world in which food of any variety isn't available at one's fingertips at all hours of the day. As the pace of technological advancement quickens, we can only imagine what the future will bring for the food service industry. ■

GLA Historical Restaurant Vacancy Rate

Source: CBRE