

Renaissance or rhetoric?

Is the downtown office market coming back? **Interviewed by Paul R. Harvey**

A business headline in the mid-1980s read, "Will the last tenant out of downtown please turn the lights out?" Unfortunately, the creative quip correctly foreshadowed the impending collapse of the downtown office market.

The 1980s concluded with tenants moving out of downtown to cheap alternatives in the suburbs — in concert with the opening of five new downtown high-rises and a horrid recession. The dust finally settled with a vacancy rate approaching 40 percent.

"The subsequent years have brought so much change — and so little change," says Craig Irving, a principal at Irving Hughes. "A thriving central business district is paramount to the economic, social and cultural fabric of our region."

Smart Business spoke with Irving about the current health of the downtown office market and where it's heading next.



Craig A. Irving
Principal
Irving Hughes

What is the current status of the downtown office market?

Downtown's share of the region's office market sits at about 15 percent. The current vacancy rate is approximately 16 percent, up from 11 percent a year ago. Factors involved in that increase include People First moving 100,000 feet of space to Texas and smaller tenants moving to the suburbs.

A suburban tenant of reasonable size occasionally moves into the 92101 ZIP Code. American Specialty Health took over the Paladion in the 1990s; Gray Cary later moved into 80,000 square feet; and Eset, a technology company, recently settled into 25,000 square feet. It's unfortunate there are not more.

How did the downtown office market reach its current state?

Following the mass exodus in the late 1980s, a major imbalance of office space occurred, with more than 97 percent of all new office space being built in the suburbs. Meanwhile, 70 percent of the office inventory downtown was showing its age. Of the 16 business clusters that drive the region's economy, (including wireless, communication, biotech and defense), only three (government, legal and financial) have a major

presence downtown. Further, of the 3 million square feet now under construction in the region, none are downtown. Organic growth of existing downtown tenants has for the last 20 years primarily fueled downtown's growth.

What factors drive tenants from the downtown market?

Beyond the major business sectors, most tenants are small business owners. After personnel costs, rent is their next-biggest expense. For example, when a small alw firm's lease is set to expire, the new landlord, who just paid an exorbitant price for the building, plans to raise rent by 40 percent. The tenant does the math and determines it'll either have to raise billing rates 20 percent to 25 percent or increase work hours by 120 to 125 percent. Neither is a good choice. The third option is to move the business to a location that will afford the company a par (or better) quality of life.

Downtown tenants are also subject to a lack of parking. Very few surface lots remain due to those lots now being filled with high-rise condo buildings. The remaining surface lots charge an arm and a leg and make it prohibitive for employers to offer parking benefits. This impacts employee morale, retention and recruiting efforts.

How does transportation come into play?

Many CEOs reside in Rancho Santa Fe, Del Mar and Fairbanks. The nightmare of the I-5/I-805 merge has influenced some to limit their office space search to anywhere north of the merge. Demographic studies of where all the employees live in the county should be evaluated and considered before eliminating certain geographic locations, but it is rarely part of the process.

Along the way, former city planners who forced developers of high-rise buildings to limit their parking to one space per 1,000 square feet also failed miserably to provide alternative means of transportation for commuters. Had those same planners imposed the same parking regulations on suburban developers, downtown would have held a major advantage because, as bad as it is, it is the hub of mass transit in the county.

How has this cycle forever changed the region?

In 1985, under great mayoral leadership from Pete Wilson, Ernie Hahn opened Horton Plaza. Some said this was a risky endeavor, but the Gaslamp District emerged as a fantastic destination for residents and visitors. Hotels sprung up and the convention center expanded, bringing millions of dollars to our region and billions of dollars invested into downtown's resurgence. Residential development exploded, and we now have a vibrant central business district.

What is the outlook for downtown?

The downtown office market will always be fickle, but its resurgence provides a glimmer of hope for the future. Meanwhile, South San Diego will continue to build housing for the work force of our county. Downtown is the central location; hopefully CEOs soon will let their workers exit downtown instead of continuing up the I-5 freeway — or better yet, let them take the trolley straight into downtown. Fewer cars on the roads would be great for everyone.

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