ADAPTING TO THE FUTURE

CREATIVE REUSE RISES AS BIG APPLE EXHAUSTS LAND, PROPERTIES

BY KAITLYN MITCHELL

As the supply of land dwindles in New York, adaptive reuse is becoming an increasingly important strategy for commercial real estate owners. "Even with the proliferation of glass towers, I see masonry, large windows and detailed interiors as the most desirable for [owners and tenants]," according to Ari Aufgang, principal of Suffern, N.Y.-based Aufgang Architects. "It's something we try to exploit when we can and also employ on new buildings."

The firm, which works with property owners throughout the New York metro areas, is seeing the most interest in adaptive reuse in TriBeCa and DUMBO – two areas with a substantial number of the former warehouses and factories that fit the bill for today's tenants. "We've worked on the conversion of former Brillo factory, which presents certain challenges," Aufgang said.

The former Brillo factory, located at 200 Water Street, was converted into 15 condos of varying sizes. The property benefited from 14-foot ceilings and 10-foot windows but was also very deep. "You don't want living space to be more than 30 feet from the windows," Aufgang said. The owner obtained permission from the Landmarks Preservation Commission to remove thirty feet from the back of the building and replace the space with two new floors on the top. "We built the addition back 15 feet and on the back, the floors overhung on top. It's all glass and the units have skyline views of Manhattan," he added.

Part of adaptive reuse is making do with what's available, particularly in places like Downtown submarket. Many of the buildings there have small windows that look out over small courtyards. "It's not nice to have small windows that look over small courtyards. It's about having living rooms facing the street and bathrooms and kitchens in the center," Aufgang added.

The strategy goes beyond the apartment sector, with older buildings with flexible zoning are being evaluated as either creative office space or light industrial and last mile distribution warehouses. "There's a battle going on to see the highest and best use for properties," a local player told *REFI*. "Both uses can work and be profitable, but buyers and sellers don't know which way to go. A year ago, it was more about creative office space – now, there is much more interest in light industrial and distribution adaptive re-use."

The types of investors that are pursuing adaptive re-use deals are mostly local New York groups that are teaming up with institutional capital. "I'm not seeing any groups from the outside doing adaptive re-use. It's mostly local experts with offices in Manhattan who are trying to put together deals," a broker said. "Many of the local owners here in New York haven't been able to buy in the last couple of years because prices have been too high, so they are looking in the boroughs."

Local stalwarts involved in adaptive re-use projects include Tishman Speyer, TH Real Estate, SL Green, Related Companies, and Vornado Realty Trust. "New York City's stock is old – in Midtown East, the average age of a building is more than half a century," said Giacomo Barbieri, head of the New York region at TH Real Estate, the real estate investment arm of TIAA. "Bringing real estate to its highest and best use has always been a part of the game. We're engaged in repositioning, converting, and changing uses of various properties, including converting old manufacturing warehouses to office and other uses. Demand for high quality real estate is strong but it's most important to stay and ahead of the curve because by the time you read it in a research report, it's too late. [Developers and investors] must be at the forefront of the emerging trends, or the relevancy of the conversion may be impacted."

The cost of rehabbing a property can be as expensive as ground-up construction, noted Jonathan Kalikow, president of Gamma Real Estate.

"I do expect to see more adaptive re-use deals done in some A-plus areas," said Kalikow. Gamma is lending to adaptive re-use deals outside of New York City, including the Railway Exchange in St. Louis Missouri, and 925 Euclid in Cleveland. "When a historic tax credit element is associated with a building, it can be converted into multifamily apartments and offices – a lot of these older buildings are centrally located in cities," he added. "This is becoming a bigger part of our lending activity – buildings that are on the national registry and have not undergone any renovation in years become a terrific asset once the work is done."

Two examples of adaptive re-use deals in Long Island City are being spearheaded by Metropolitan Realty Associates. LIC's office and retail growth is being complemented by 23,000 residential units in the pipeline as well as 4,900 new hotel rooms, according to the Long Island City Partnership. Industrial space remains scarce, as the vacancy rate for industrial properties hit a two-decade low at the end of 2016. Several buildings with the potential for adaptive re-use are also for sale in the Bronx – these include old-fashioned manufacturing industrial companies that are either moving or closing, local pros told *REFI*.

Along with its joint venture partner TIAA Global Asset Management, Metropolitan acquired HUB LIC in Long Island City for $89m in August 2016. The four-story, 326,000 square foot commercial building is located at 47-25 34th Street in Queens' Long Island City submarket. The property is 48% leased to tenants including POLO Ralph Lauren, TEC Systems, Eleni's Bakery, Charles Gracie, and Richelieu. The property has 16 to 21 foot ceilings, a floor-to-ceiling window line, a 7,000-square-foot pitched skylight in the center of the second floor and skylights throughout the third floor.

MRA also acquired the former Matsil Bros. building in LIC with equity partner TH Real Estate for $55m in March 2017. The three-story, 246,000 square foot property built in 1946 is located at 48-49 35th Street in Queens and last traded hands nearly 40 years ago. It is 79% leased, with international shipping company AirSea Packing as the largest tenant occupying 100,000 square feet. The property has a 17,500 square foot unit available on the ground floor with two loading docks and a 40,000 square foot unit occupying the entire third floor with a loading dock and a freight car.