



January 2019

ACTIVATING GROUND FLOORS

IN DOWNTOWN SEATTLE'S BUILDINGS

ACKNOWLEDGMENTS

Amazon.com

Hudson Pacific Properties

Skanska

Talon Private Capital, LLC

Washington Holdings

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INTRODUCTION

To vie for the influx of new employers in downtown Seattle's competitive office market, office buildings must increasingly offer great amenities. On the ground floor, the most successful office buildings include amenities that contribute to a vibrant city center such as retail storefronts, cafes, restaurants, and informal meeting spaces. Owners of existing office buildings are catching on, converting traditional office lobbies (and in some occasions, banks) into active and inviting hangout spaces.

In 2018, the Downtown Seattle Association (DSA) launched a research effort to better understand the motivations behind developers and property owners who convert existing ground-floor spaces and to encourage others to make similar changes. DSA and ECONorthwest interviewed five property owners and developers in downtown Seattle who have either repositioned ground-floor retail space into active uses or constructed new office buildings that respond to this trend.

This report is intended as a resource for developers and property owners considering the addition of ground-floor amenities. Drawing from **five case studies**, it details **key lessons**, a potential **investment process**, and **key players** in ground-floor activation in downtown Seattle.

KEY LESSONS LEARNED FROM THIS RESEARCH

1. Investments can unlock building and neighborhood value
2. Ground-floor retail is an amenity for office tenants
3. Design decisions support ground-floor success
4. Focused attention is required to curate the appropriate tenant mix
5. Successful ground-floor activation requires patience, commitment, and partnerships



400 Fairview



8th + Olive

CASE STUDY OVERVIEW

These case studies provided the basis for DSA's research into ground-floor activation in downtown Seattle.

8TH + OLIVE

Developer: Talon Private Capital, LLC

Location: 720 Olive Way

Year Built: 1981

Year Renovated: 2015

Floors: 20

Office SF: 285,675 SF

Retail SF: 15,035 SF

The rapid redevelopment of South Lake Union and the northward growth of downtown created an opportunity to turn a value property into a signature office project that could thrive in the competitive office leasing environment. Talon Private Capital invested over \$12 million of capital into the building's renovation.



400 FAIRVIEW

Developer: Skanska

Location: 400 Fairview

Year Built: 2015

Floors: 14

Office SF: 320,000 SF

Retail SF: 18,000 SF

400 Fairview is a LEED Platinum (targeted) project in Seattle's South Lake Union neighborhood that serves as a new destination in a developing neighborhood with restaurants and retail spaces. This building sold in summer 2018 for \$991/sf, second only to the region's record sale price of \$992/sf set months earlier.

411 FIRST

Developer: Hudson Pacific Properties

Location: 411 First Ave. S.

Year Built: 1906

Year Renovated: 2013

Floors: 7

Office SF: 143,117 SF

Retail SF: 15,788 SF

411 First is a part of three adjacent, Class A office buildings offering street-level retail. Hudson Pacific acquired the building in 2014 to capitalize on the renovated building's close proximity to the future Seattle Festival Pier and Pioneer Square, which has become a growing hub for media and creative sectors.



DOPPLER + DAY ONE

Developer: Amazon.com

Location: 2021/2121 Seventh Ave.

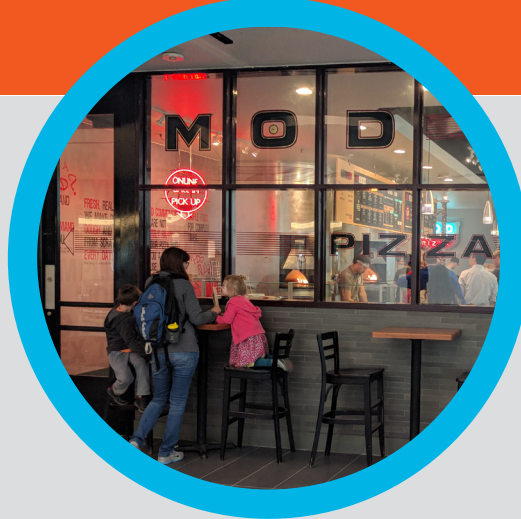
Year Built: 2016/2017

Floors: 37/37

Office SF: 1,000,000 SF/991,000 SF

Retail SF: 20,000 SF/9,000 SF

Amazon's Doppler and Day One buildings are part of a three-tower complex at the heart of a growing Amazon campus in the Denny Triangle. Amazon staff used ground-floor spaces to create a vibrant, urban setting, reflect Amazon's mission and values, and establish a culture that encouraged employees and neighbors to spend time in their neighborhood.



ONE + TWO UNION SQUARE

Developer: Washington Holdings

Location: 600 University St./601 Union St.

Year Built: 1981/1989

Year Renovated: 2017/Currently

Floors: 36/56

Office SF: 680,000 SF/1,132,000 SF

Retail SF: 40,000 SF

These two class A buildings in downtown Seattle share three levels of urban retail, an outdoor courtyard, and an underground pedestrian concourse. Washington Holdings renovated the buildings to promote a mix of destination uses as well as amenities for tenants, and to make visionary capital improvements.



One + Two
Union Square



KEY LESSON #1

Investments Can Unlock Building and Neighborhood Value

Attractive, active lobby and/or retail spaces are a desirable amenity for office tenants who need space to meet with clients, collaborate with teammates, find a respite from their normal work environment, or to recharge with food and drinks.

Lobby renovations result in an amenity that creates an economic premium.

First, they help office buildings achieve rents at the higher end of the spectrum. Second, they can help buildings keep pace in the marketplace through stronger absorption rates, better occupancy, and higher tenant re-lease rates.

Flexible retail spaces can evolve over time as the neighborhood changes.

By building flexibility into first floor renovation projects, developers ensure that those spaces can be used in a variety of ways over time.

Retail needs a neighborhood to succeed.

Retail success depends on the surrounding neighborhood, which is beyond the control of an individual developer. A few thousand square feet of retail space in one building is not enough to create the kind of busy neighborhood residents and office workers want. Therefore, the City of Seattle, DSA, and its partners should provide technical and other assistance to encourage a critical mass of active ground floor spaces.



Doppler +
Day One



KEY LESSON IN ACTION



8th + Olive

Both food retailers, Mr. West and Juicy Cafe, have performed much better than expected. 8th and Olive was sold in 2017, returning a 26 percent internal rate of return and 200 percent to equity investors.



400 Fairview

The renovation created a new center of gravity in South Lake Union with the creation of a market that nearby development projects have marketed as an amenity.



411 First

The attractive location provided an opportunity for more competitive office rents by targeting investment on the ground-floor. Since Hudson Pacific owns over 800,000 square feet of space in its adjacent holdings, the renovation approach focused on the retail and tenant amenity mix as part of building and district development.



Doppler + Day One

One of Amazon's development goals is to build community through design. By prioritizing independent businesses and custom design, Amazon is helping to create a new urban neighborhood that feels welcoming and vibrant, and integrates their offices into the city.



KEY LESSON #2

Ground-Floor Retail Is an Amenity for Office Tenants

In the past few years, building owner/operators have attracted retail businesses to serve as an amenity that helps secure higher lease rates from the office tenants and residents above. This is a departure from traditional retail leases that exist to generate the highest revenue possible to the building owner. Retail rates for buildings in the case studies reflect this new reality.

Many owner/operators consider renovations as a defensive move.

Office tenants see ground-floor amenities as the new norm. In some cases, tenants will explicitly pay more for these amenities. Other times, amenities contribute to tenant lease-up or retention rates.

“Next generation work spaces” demand retail as part of the amenity package.

Integration of retail makes the building more attractive and improves competitiveness for office leases. It is critical to activate lobby and entry spaces.



One + Two
Union Square



KEY LESSON IN ACTION



8th + Olive

Renovations aimed at creative office tenants included a new building conference facility, fitness center, coffee shop, and bike storage. New creative office space tenants were willing to pay a 25 percent premium in rent for on-site amenities.



400 Fairview

400 Fairview hosts a healthy variety of office tenants ranging from high fashion to technology. Because of the ground-floor retail, Skanska believes that the office spaces leased up faster than similar buildings and reports there was a \$1.50 to \$2.50 increase in rents for office space. Shared amenities like bathrooms, seating, and display areas for the flower shop made the leases affordable for small retail businesses.



411 First

Hudson Pacific focused on making office leases competitive rather than generating incremental revenue from retail, creating a symbiotic relationship between the two. The company finds that the impact of high-quality ground-floor space benefits both occupancy and lease rates.



Doppler + Day One

After locating its headquarters in a neighborhood that, at the time, lacked amenities, Amazon took proactive steps to create food and service opportunities for employees and visitors.



KEY LESSON #3

Design Decisions Support Ground-Floor Success

Successful ground-floor building activation projects prioritize increased light, openness, and street-level activation. Both new and existing building construction require resources dedicated to building open and high-finish spaces, along with tenant improvement allowances.

The design must ensure that the building effectively activates the street.

This can mean reconfiguring the “front” of the building to better orient to the pedestrian environment. Ground-floor retail within a building/hall can activate passive common areas by allowing for retailers to “spill out” into shared spaces for seating, bathrooms, and utility spaces.

Multifamily residential amenities and leasing offices should be on the first floor.

Fitness centers, business centers, and the property management office all add to the appearance of an “activated” ground-floor, even if use is restricted to building residents and potential residents.

Site features like plazas, patios, and public art offer ground-floor retailers the opportunity to cultivate a memorable customer experience.



411 First



KEY LESSON IN ACTION



One + Two Union Square

The lobby renovation project at Two Union Square added 6,500 square feet of lounge, retail kiosks, and common area that were taken from leasable space.



8th + Olive

To update the building, the construction team created an atrium by punching out the heavy brick frame. In addition, the team reoriented the front of the building to reclaim parts of the existing plaza.



400 Fairview

At 400 Fairview, the building design places the amenities and elevator at the edge of the building, providing a more open, bright, and flexible feel to the space, allowing retailers to spill into the common areas. Elevated photovoltaic panels created a covered space to host the rooftop bar. To keep this space designated as outdoor space, the “windows” are on sliding rail guards.



411 First

The brick and beam buildings were renovated to allow for large floor plates, expansive ceiling heights, and historic and modern architectural elements.



Doppler + Day One

During project design, Amazon outlined high-level priorities to encourage retail through activation of the street level, create opportunities for serendipitous encounters, and provide outdoor gathering spaces that are open to the public.



KEY LESSON #4

Focused Attention Is Required to Curate Tenant Mix

While high-quality, ground-floor tenants can help to create a brand for the building and stabilize occupancy, it takes time and resources to find the best fit.

Prioritize retail experience over revenue.

Retail is not part of the revenue model, instead, it is an amenity to set the tone for the building and attract tenants. Some owner/operators make concessions for an especially compelling retailer, such as providing up-front capital. Owners/managers with a portfolio of buildings can use their flexibility to make a deal that works for both parties.

Finding the right tenants is difficult, but rewarding.

Finding high-quality food/beverage and retail firms requires a strong commitment to their success. The first retailers are most important, as they establish credibility. Savvy owners/managers seek out tenants by finding successful small business owners who might be looking to expand, or by backing a popular chef or bartender who is ready to strike out on their own. Small, local retailers take more effort for recruitment, space buildout, and lease negotiation.

Maximize activation.

Development teams look for a mix of retailers and services that are open during various times of the day and days of the week to ensure that the building has continuous activation. While street facing retail can thrive off of outdoor pedestrian traffic, internal retailers must often survive on workday lunch traffic.



One + Two
Union Square



KEY LESSON IN ACTION



One + Two Union Square

Washington Holdings chose tenants with a proven concept. Adding Evergreen's (a salad chain) and Cortina (a destination restaurant by a locally celebrated chef) brought in outside customer traffic. These tenant spaces were able to command higher rents upon lease renewal, once the ground floor was fully occupied.



8th + Olive

To keep the lobby activated, the management team chose one tenant that would be open at minimum for breakfast and lunch (Juicy Café), and another that would be open for lunch and dinner (Mr. West). A mix of percentage and traditional retail leases allowed Talon Private Capital to attract high-quality tenants while making the financial structure work.



400 Fairview

Skanska wanted complementary food, retail, and service uses that were not already in the neighborhood, could activate the lobby and the street at different hours of the day, and meet the needs of both tenants and visitors. Skanska worked closely with all retailer on business strategy, planning, and collective marketing.



411 First

Hudson Pacific curated a mix of restaurants, retail, and cafés, such as Ill Terrazzo Carmine, General Porpoise Doughnuts, Flora and Henri, and Browne Family Vineyards to attract diverse pedestrian clientele.



Doppler + Day One

Most current leases are with food/beverage retailers, which the neighborhood lacked when the towers were initially built. Future towers will focus on attracting more service-based tenants. Amazon has implemented lower percentage lease structures that reset after time with more traditional lease terms. Amazon also uses concessions and lease flexibility to attract the right tenant(s).



KEY LESSON #5

Successful Projects Take Time, Commitment, and Partnerships

While there is an economic upside to activating the ground floor, these projects require patience, investment dollars, and relationship building.

For many projects, success relies on long-term partnerships and collaboration with the community and local government.

- **Funding** — Funding in the form of storefront improvement grants or public-private partnerships for plazas or parks.
- **Visioning and programming assistance** — Some neighborhoods in a period of transition benefit from public-private collaboration to craft a shared vision for how a building can create value for tenants and neighbors.
- **Interim or community uses** — Some projects have found success in completing a simple build-out and donating leased space for a period of time to a community arts or service organization that will provide a positive appearance to potential tenants for the upper floors.
- **Regulatory flexibility** — Many projects work with local governments to allow for flexibility in parking requirements, ingress and egress requirements, floorplate dimensions, ventilation, and insulation.

Ground-floor projects can cause temporary but impactful disruptions to building operations.

During major remodels, building owners often close down spaces and reduce their rent rolls. Not all owners and operators can accommodate interruptions to building operations.



One + Two
Union Square



KEY LESSON IN ACTION



One + Two Union Square

Renovations required a capital contribution, meaning a potential pause on cash flow for a period of time during building renovation. To maintain design consistency, Washington Holdings hired the original architect, NBBJ, to update the building with new features that could evolve with tenants over time.



400 Fairview

To allow for natural light in the lobby and accommodate the site's changes in elevation, Skanska worked with City to reallocate FAR to other parts of the building.



411 First

Committed building ownership means that they could take a longer-term perspective in curating a neighborhood district.



Doppler + Day One

Amazon identified a need to program their hardscaped street and plaza spaces to provide more activation, interest, and energy. They worked closely with DSA and internal staff to activate outside spaces through outdoor concerts, buskers, and amenities such as seating and public art.



INVESTMENT PROCESS

As part of the interviews with downtown Seattle building owners, most talked about six key phases of the redevelopment process. Here is an overview of those steps.



1



1) Identify how potential investment can respond to market changes.

- New jobs have driven construction and redevelopment of downtown commercial spaces. Much of the growth is fueled by technology companies that compete fiercely for talented workers, workers who value the quality of their work environment.

Downtown Seattle added **76,000 jobs from 2010 to 2017, a 35% increase** in comparison to a 26% increase for all of Seattle. This makes up **64% of all jobs** gained in Seattle over that same period.

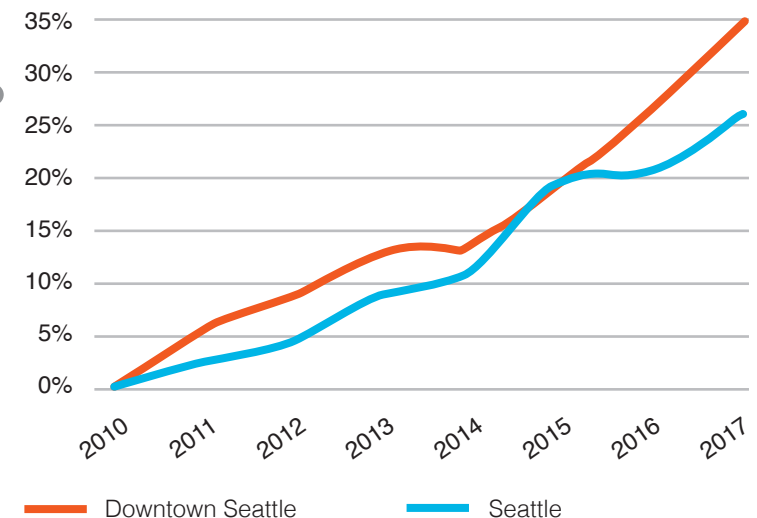
2) Engage with real estate advisors.

- Work with real estate professionals to identify the project's goal, value add, budget, and timeline.



2

Percentage Job Growth (cumulative), Downtown Seattle Compared to All of Seattle, 2010-2017



Example: To illustrate changes in cash flow through the course of a renovation project, ECONorthwest created a simple cash flow model of a 300,000 SF office building with Class B rents. The model compares a **status quo scenario** with a **lobby remodel scenario**.

3) Develop a financial plan.

- A financial plan can help an owner/operator determine the risks and potential rewards of an investment.



3

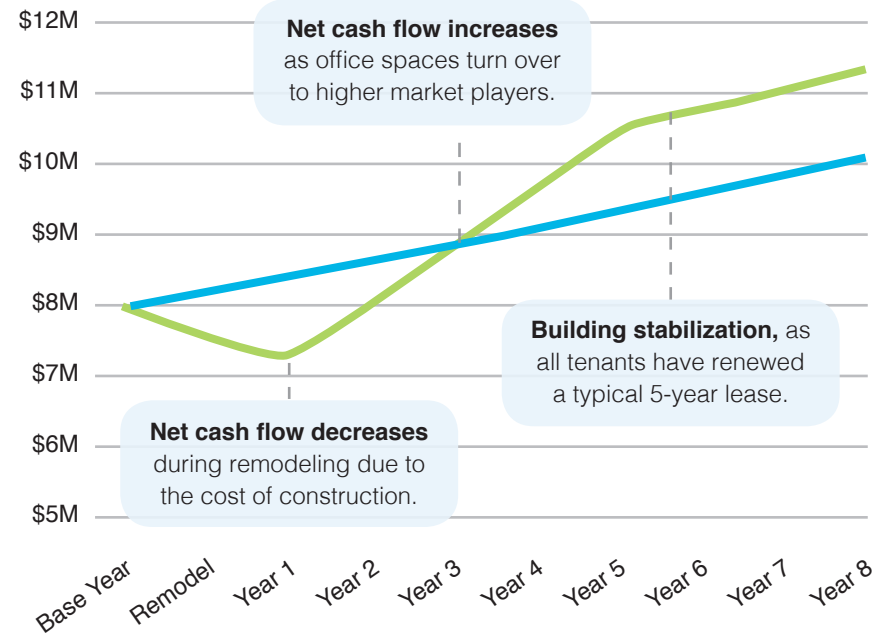
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4) Develop a tenancing plan.

- Work with existing retail and office tenants to determine future plans, solicit feedback on the potential tenant mix, and communicate changes.
- Using this information, identify ground-floor retail mix and develop a recruitment strategy.
- Develop a plan for office tenant conversion for the 2nd floor and above, including a plan to upgrade office finishes to achieve higher market rents.

Comparing “Status Quo” to a Lobby Remodel Scenario



The improvements drive a **3% increase** in the total ten-year net cash flow over the status quo scenario, resulting in a **23% increase** in building valuation.

- “Status quo” Scenario**
the owner/operator makes no changes to the building
- Lobby Remodel Scenario**
assumes an 18-month period of design and construction with a significant investment in the lobby

5



5) Determine design goals.

- Engage neighborhood stakeholders on how the building interfaces with the area’s urban design and streetscape.
- Articulate the purpose and ideal use of the space that invites and activates, including how the space compliments the desires of targeted office tenants.
- Engage architects to design the space.
- Work closely with lobby retail tenants on the configuration of tenant spaces and common area design.

6



6) Initiate permitting and construction.

- Lay out project requirements and steps to lead to construction (neighborhood outreach, permitting, regulations).
- Work with permitting agencies to seek any necessary design variances and other project approvals.
- Break ground! Work with construction project management to execute remodel.
- Mitigate impacts to existing retail tenants during project construction.

KEY ROLES

There are four key players in ground-floor activation in downtown Seattle.

Building Owner/ Property Manager

In commercial real estate, property owners have different expectations and goals. Downtown Seattle's property owners include individual "mom and pop" owners with a single building; family investors with larger portfolios; real estate developers who build, own, and sell their assets; and institutional investors who are investment managers with some portfolio in real estate assets.

Real Estate Advisor/ Developer

Most property owners that are not developers themselves will seek advisory services on lobby renovations. The advisor knows how to execute a real estate transaction but will bring a more strategic approach to helping owners achieve their goals.

Downtown Seattle Association

DSA cultivates downtown's vibrant retail experience through a comprehensive approach to business development services. In its capacity, DSA supports existing and emerging economic clusters through advocacy and coordination, provides business retention and development support services to existing building owners and tenants, and identifies desirable business types for specific geographic focus areas. DSA also leads studies to inform retail and storefront design in downtown.

City of Seattle

The City of Seattle facilitates the improvement of ground-floor spaces by setting long-term urban planning goals and handling land use entitlements and construction permits. Outside of the permitting process, the City sets design guidelines and code for ground-floor spaces.

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Interviews were conducted with representatives from Amazon.com, Hudson Pacific Properties, Skanska, Talon Private Capital, LLC and Washington Holdings



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