

Urban Development

Turning Sows' Ears Into Silk Purses Takes Careful Planning

By JOHN R. DONALDSON

NOR the least of the challenges faced by those who live in sunny Southern California is the cost of renting a roof over one's head. A recent study published by the USC Lusk Center for Real Estate predicts that rents in Los Angeles County will rise 8.2% over the next two years, making what is already one of the nation's most expensive rental markets that much less affordable. The study goes on to say that the pace of new multifamily construction continues to fall behind demand to the degree that it would take an additional 500,000 new apartments to meet current demand.

There are multiple reasons for this dislocated rental market. Certainly, the recession of 2008 impacted development of new multifamily product, while job losses and foreclosures played havoc with homeownership. While job growth continues to improve, many potential buyers still cannot qualify for mortgages, particularly as home prices escalate. This has put added pressure on the rental market. Additionally, many millennials simply prefer the flexibility of renting rather than owning. Also, California has some of the nation's most draconian environmental and land use laws which, when combined with the scarcity of city planning department personnel, makes entitling new multifamily projects both time consuming and expensive, further increasing rental rates.

Seizing Opportunity

Beginning in 2009, investors both private and institutional began to purchase existing multifamily assets, emphasizing class "A" product. Developers also focused on the upper end of the market, although the majority of renters could not afford the tariff. Other, more savvy investors began to look closely at "B" and "C" product, with an eye to rehabilitating these outdated buildings through cost efficient renovation. Since Los Angeles is one of the nation's most densely populated urban areas, there are many well located, but badly neglected, under-occupied properties that could be redeveloped. This is particularly relevant as we focus more and more on developing transit-oriented, mixed-use multifamily projects in these high density areas.

An important calculation should determine how much the current rents are below market and

how much they might be increased once the renovation is completed. Also important is the extent to which earthquake retrofitting will be necessary to secure the structural integrity of the property. Currently, the City of Los Angeles is beginning to study the number of so-called "soft-story" apartment buildings which it will require be seismically strengthened. Soft-story buildings are defined as being no more than three stories built over ground level with expansive openings containing car ports, parking garages or retail stores with extensive glass windows. According to a 2011 Caltech study, there are over 20,000 of these structures in the city. Our firm has been involved in the seismic retrofitting of dozens of these properties over several years.

Focusing the Work

Once the decision has been made to move forward with the restoration project, it's important to understand the challenges that are likely to impact the process. Having renovated over 10,000 apartment homes in the last 20 years, we're very aware of the problems that often present themselves. By far, the most significant is engineering. In most cases, these older structures do not meet current building codes and the cost to bring them into compliance can be significant. This is particularly true when it comes to electrical and plumbing systems. Another major concern is undertaking the reconstruction while the building is occupied. This requires careful planning and coordination on the part of the management and the construction teams in order to disrupt the lives of the tenants as little as possible. Meeting the federal and state requirements for disability access can also be a challenge.

Adding Sizzle to the Steak

While updating the engineering, utilities and safety systems in these classic buildings takes priority, it doesn't necessarily attract tenants. In our experience, the ambience of a project is of major importance. Attention should be paid to exterior renovation, including new stucco overlays with integral colors, contemporary exterior doors and windows, and even railings and decking. Well-tended landscaping and new signage will also add to the curbside appeal.

The common areas of apartment complexes are always a major focus. This is particularly true if the

property is likely to attract younger tenants who enjoy socializing. Ideally, depending on the size of the property, attention should be focused on the development of a clubhouse, business center and fitness center, and an outdoor deck with a pool, spa and BBQ area.

The apartment homes themselves do not need to be large, but should be well accessorized. In today's competitive market, the inclusion of washers and dryers in each unit is extremely important. Kitchens need to incorporate stainless steel appliances and stone countertops, and buildings should have central heating and air conditioning. Ceilings should be smooth lath and plaster, eliminating the so-called "cottage cheese" effect so popular in the 1960s and 1970s. Finally, the homes should be pre-wired for Internet and cable access.

Parking and security are two other aspects of project revitalization which take priority. In the case of parking, it should be covered and secured if at all possible. The need for security in the urban environment is always front and center. Most recently, we've been installing cameras in the entries, lobbies, clubhouses and fitness centers. Additionally, swipe card systems have been added to allow tenant access to these common areas. While this process permits after hours access, it also provides a record on who has been utilizing the facilities and when. The cards can be deprogrammed after a tenant leaves the property.

Finally, we live in an age of new technology and tenants expect this to be available to them in and around their homes. So, in addition to pre-wiring all apartments for Internet and cable access, Wi-Fi should be available throughout the property. Most recently, electric car charging stations and bicycle racks are being required by city staff during the planning process.

With careful budgeting and planning, a seemingly obsolete multifamily property can be turned from a sow's ear into a silk purse!

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