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COMMERCIAL REAL ESTATE'S CHANGING LOCAL LANDSCAPE

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COLDWELL BANKER COMMERCIAL SUNCOAST
Bright Ideas. Brighter Solutions.

Commercial real estate is one topic in which nearly everyone has an interest. People want to know what's being built near their homes, schools and workplaces. They also want to know where commercial developments will be built next, how they'll affect traffic flow, and if they'll have any effect on their own real estate interests. On the following pages, five individuals who know our region well offer their insights on market trends today and what the future may hold.

How would you describe the current state of our region's commercial real estate market?

STEVE ANDERSON: I believe the commercial real estate market in our region is strong. We have development happening in many areas of the county, and I love to see new lights coming on in every part of town. I think that's an indicator of the health of our region – seeing all parts of our county with some kind of development activity.

JOHN CHESHIRE: I believe New Hanover County and the surrounding counties are in a positive trend of growth, but nowhere near where we were prior to 2009. Prior to the recession, the economy was strong, our clients had money to spend, banks were lending, and buildings were being built.

After 2009, there was a drastic change in the market. The residential and commercial markets were hit hard. Banks were not lending money to small and large businesses alike, for fear of another recession. People of all walks of life were being laid off and competition was as strong as ever in all job markets, especially in the commercial building industry.

Now it seems that the public market has rebounded well. The passing of the New Hanover County Schools bond referendum in 2014 and the positive outlook for the Brunswick County Schools ballot in 2016 has and will increase labor, material and the subcontractor markets, and that brings with it more work for our neighboring counties. As for the private market, I think we are seeing job growth in the commercial markets

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RICHARD COLLIER
McKim & Creed, Inc.

by way of banks being more lenient in lending, and with private opportunity funds lending as well toward new construction.

RICHARD COLLIER: Our commercial real estate market is expanding as a result of continued housing market growth, transportation improvements and a healthy economy. This area is being recognized as much more of a primary residential location, rather than a second home market. We are no longer simply a destination; we are a place where people want to live, raise their families and retire.

KEN DULL: In a word, I would say that it is fair. Commercial development always lags behind residential, which seems to be doing well right now. I expect the commercial real estate market to continue being fair or better.

There are good spots – the Mayfaire area seems to be doing the best. The rest of the town is yet to be seen. Ask me that question again next year.

GRAYSON POWELL: The current commercial real estate market is very strong across almost all sectors. Investors are increasingly interested in commercial real estate in Greater Wilmington and that is having a positive impact. Office inventories are tightening and that is also having a positive impact on rental rates. We do have a few geographic areas in the office market that are lagging behind the rest, but overall, the market is strong and continues to strengthen.

What is the most interesting trend you see in a particular segment of the market?

CHESHIRE: To me the most interesting trend not only in our local market, but in markets throughout the southeastern United States, would be what I call the "grocery store wars."

Growing up in North Carolina, my family shopped at Harris Teeter, Food Lion and Lowes Foods. Now we are seeing the push from Publix, Whole Foods, Trader Joe's, Fresh Market and European chains like Aldi and Lidl all establishing their footprint here in the southeast as well.

With the steady growth of our population in residential and commercial multifamily construction, the need for convenience seems to be a driving force for these "grocery store wars." It seems shoppers would rather drive a mile or two for a discount special on produce and then drive to another chain for a discount on meats. One could speculate that it's all about the deals, saving money and store location convenience.

This push has created a great opportunity for job creation in regard to short- and long-term employment. This is not just limited to the new construction. The older and well established chains seem to be forced to renovate, expand and offer fresh new looks and styles to keep up with the times and growing market.

COLLIER: One of the most interesting trends is the senior housing market. In response to the aging baby boomers, there are many more options now than just the traditional "nursing home" that many of our grandparents lived in. Today, seniors want to live in age-qualified residential communities or high-end, high-level independent living properties. And the commercial market responds to that. Developers understand that people don't want to get in their cars and drive 10 miles to go to the drugstore. They want to walk across the street or down the stairs, so it's important for commercial facilities to be proximate to these new senior housing areas. The commercial real estate market is responding to the decisions of our aging populations.

DULL: It would be hard for me not to say new multifamily housing and the resurgence in this area. It is an interesting trend and it's hard not to notice it. Some people use the word apartments, but it's really multifamily. On Kerr Avenue, it's all those duplexes they built. Multifamily could also be senior living. There are two new senior living facilities on Eastwood Road.

This is a trend everywhere. I think the whole world is downsizing, from college students to working professional without children to empty nesters and seniors.

There also seems to be a splash of new grocery store chains and stores. You're not seeing existing franchises, like Harris Teeter and Lowes Foods, building many new stores. You're seeing new brands coming to town in a market where the population is not growing that much. I think that's interesting because you tend to ask, do we really need it?

POWELL: We have started to see an increase in lease-back sales where the owner of a commercial property sells the property, but then immediately leases it back from the new owner for the original owner's continued use. There is a large volume of investors in our market looking for commercial property to purchase, so this has become more and more attractive to property owners. By selling and leasing their property back, business owners are able to free up capital to pursue other investment options, such as second locations or new equipment.

STEVE ANDERSON: We have a niche here in our market that we focused on about 16 years ago when we started creating commercial condominiums. The commercial condominium market for our group is stronger now than ever.

Back during the recession, our condominium product worked so well because banks still had an appetite for owner-occupied units. As the economy has improved, our ratio of owner-occupied clients wanting to purchase instead of leasing has gone up tremendously. For example, at the Offices At Airlie, our most recent commercial condominium office development, five out of the six units are owner occupied. That's a trend I see continuing.

How does the Wilmington region grow thoughtfully by balancing the need for new commercial and residential development with maintaining the lifestyle we enjoy?

COLLIER: Wilmington has a great blend of commercial and residential growth. Firms like McKim & Creed are fortunate to collaborate with competent and talented city and county staff who understand the importance of well-thought-out development and are focused on building communities, not just subdivisions. RiverLights is an excellent example of development that is enhancing our entire area with not just housing, but with a marina, boardwalk, live-work opportunities and miles of trails.

Another example is the extension of trail systems and parks in the region. By making it easier to get from point A to point B without having to depend on

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a car, we are promoting the enjoyable, healthy lifestyle that brought many of us to the area in the first place. The Wilmington region is growing and developing in a smart, thoughtful way.

DULL: I spent six years on the New Hanover County Planning Board and six years on the Wilmington Planning Commission. My experience has shown me that you've always got to find common ground among stakeholders, and that means nobody needs to be taking extreme positions. I think extreme positions hurt everybody.

If we weren't able to find common ground over the last 50 years, if we had just stopped development, if our forefathers said, "Now that I'm here, let's not let the town grow anymore," then chances are that most of us wouldn't be here right now.

On any kind of planning decision, my first thought is, "Will this provide my children with a potential job and will this also protect the lifestyle that I've enjoyed?" I want to be able to answer "yes" to both of those questions.

POWELL: Zoning laws and regulations are in place that ensure that new commercial and residential development is done in a thoughtful manner that protects the interests of all parties in our community. Both the city and county are in the process of drafting comprehensive plans that will update these regulations. The trick is to maintain balance – both for the business community and for residents – and to make sure the regulatory process doesn't overreach and become so onerous that it stifles thoughtful and balanced economic development all together.

What are the best signs you have seen in our commercial real estate market since the Great Recession?

DULL: The best sign I've seen is that the private sector has more consumer confidence for the first time in about eight years. We're seeing new projects, and people are hiring, at least for some positions. People who had business plans before the Great Recession are now feeling confident enough to act on them.

The stabilization of rent rates in the commercial markets is another sign. They've been very low for quite some time, and that hurts everything – it hurts values, it hurts lending abilities, and it hurts the tax base, quite honestly.

POWELL: Lending institutions have stricter guidelines and investors are much more careful about the deals they make. I haven't seen the feeding frenzy that I saw in 2007. There is a lot of activity in the market, but there is a lot more study done in the due diligence phase, which is a good thing. Some of this study is due to the demands that the banks are making, but a lot of it is buyers being more cautious.

This is where a good commercial broker can be a real asset by helping the buyer thoroughly analyze the opportunity rather than just working to close the deal. We pride ourselves in bringing the experience and expertise to the process to help clients determine what is best for them to meet their short- and long-term goals, not what will get them into a deal the fastest.

ANDERSON: The best signs I've seen are concrete trucks and dump trucks on the road heading in every direction. We didn't see that a few years ago. We have development downtown, in midtown and continued development in the Mayfaire and Landfall area. I am encouraged to see development happening all across our county. If my competition is doing well that means I'm doing well.

The fact that banks are aggressively competing again for business is another sign that the commercial real estate market is improving. During the slowdown, it was really only the bank you had a relationship with who was able to look closely at a deal.

COLLIER: Wilmington is now viewed as a champion market, and nationally acclaimed businesses like Publix and international companies such as Lidl are coming to Wilmington because they recognize that we are a growing market. Semi big-box stores that would normally gravitate toward Raleigh and Charlotte are now considering Wilmington as a viable market. That is a very positive sign of confidence. Right after the Great Recession, banks were afraid to lend, developers were afraid to build and businesses were afraid to expand. Now, developers are asking where they can go that is upcoming and booming and hot. And the answer is Wilmington.

"My experience has shown me that you've always got to find common ground among stakeholders, and that means nobody needs to be taking extreme positions."

KEN DULL
McKinley Building Corporation

What are your biggest concerns around construction and commercial development in our region?

POWELL: We don't like sprawl and, unfortunately, we don't like height. Most of the city and county limits building heights to 45 feet. To mitigate sprawl, buildings need to be built higher.

The projection being made by the Plan NHC (future land use plan) is that the county will grow by more than 100,000 people by 2040. If we continue to require low building heights and smaller buildings to accommodate this growth, more land will be required for development, and this will put greater pressure on the little land that we have available. Smaller buildings mean less green space and more sprawl, neither of which is good for our community.

COLLIER: We need to promote controlled, smart growth, and not overbuild. Also, we need to continually upgrade our roadway and utility capacities as we continue to grow.

CHESHIRE: With our local market and regional markets on a positive trend upward since the recession, one could see that the biggest concern around construction and commercial development would have to be the availability of a talented subcontractor workforce.

The high volume of projects in pre-construction and construction has made it harder to find qualified, available and competitive contractors in our sub markets.

DULL: My biggest concern is that we must be careful that outsiders don't perceive us as being closed for business. Sometimes the loud few speak instead of the silent majority, and perception becomes reality. If everything we are doing becomes a fight, then the potential job creators are going to skip over our area and go somewhere that is a quicker point from A to B. If we're OK with being a retirement and vacation destination, if that's what we want to be, then that's the perception that we need. If we're open for business, we've got to let people know.

I think we need to understand that we're not in the 1960s anymore, when we were building chemical plants and dumping sewage in the river. We've all come a long way. There are state and federal regulations to protect the environment that are built-in now. We pay regulators every day to be watching and to make sure we are doing things right.

What is the next "hot spot" for commercial development in our region?

ANDERSON: I see commercial office and retail growth starting to really heat up in the Oleander/Military Cutoff corridor. We have developed more than 210,000-square feet of class A office space in the Mayfaire area in the past eight years. We have another 120,000 square feet that we are beginning to market here at The Offices At Mayfaire IV, V and VI. We're going to have developed more than 330,000 square feet of Class A office space in this zip code.

I think what's encouraging is that you continue to see signs of change as you drive on Military Cutoff to Oleander Drive. You have Wilmington Tire and Auto, a brand new store.

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There's a new barbecue restaurant in the old Flip's Barbeque House. I hear that plans have been submitted for a new animal hospital on the same side of the street, just up from there. At the Newbers Refrigeration site, we project building 70,000 square feet of new office and retail condominiums. We are seeing tremendous redevelopment and new development just within that 1.5 mile corridor. I think that similar projects could work their way down Oleander Drive.

CHESHIRE: As far as New Hanover County's next "hot spot" for commercial development is concerned, it looks as if apartments, retail and the grocery boom are dictating the need for what little land is left to be developed.

I believe the two hot spots that are currently being developed in New Hanover County are our northern downtown waterfront and the midtown area of Barclay West off of Independence Boulevard and 17th Street Extension. Both of these hot spots will encompass apartments, destination retail, restaurants and grocery.

We currently are working with developers in pre-construction on the Pier 33 Apartments and are under construction on the BlackFinn and Vida Restaurants on what was previously a brownfield site on the waterfront adjacent to the Wilmington Convention Center. Also, Clancy & Theys is currently breaking ground for construction on retail outparcels at the Pointe at Barclay West, which until recently was one of the last undeveloped hot spot tracks of land left in New Hanover County.

COLLIER: There are several "hot spots" for commercial development in our region, including the southern portion of New Hanover County, the U.S. 17 South corridor toward Leland, the southwestern side of Pender County (particularly the U.S. 17 corridor), and the eastern portion of Pender (again, along the U.S. 17 corridor), which includes the mixed-use community known as Blake Farm. Some of these areas include properties that were being developed before the recession, and commercial interests and developers are looking at them again. Extending water and sewer service along the U.S. 421 corridor will also be an incentive for commercial development.

DULL: I think it is downtown. It's not hot yet, but if it keeps trending like it is, if all the projects happen that are on the books, it is on the verge of being the new hot spot. And that is great. Having a strong downtown is a great selling tool for business.

"I haven't seen the feeding frenzy that I saw in 2007. There is a lot of activity in the market, but there is a lot more study done in the due diligence phase, which is a good thing."

GRAYSON POWELL
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POWELL: With the onset of RiverLights in the western part of the county and the creation of both commercial and residential properties in midtown, we see that entire swath of New Hanover County really taking off. Just like Mayfaire has evolved into its own anchor development, we see that happening in RiverLights and in the 17th Street/ Independence Boulevard area with Barclay. And of course, once sewer goes into the U.S. 421 area, that area will hopefully become a hub for new business and industrial development, both of which are sorely needed in New Hanover County.

How do you advise companies that are looking at upsizing or downsizing a commercial space?

DULL: My advice would be to make sure you've thought through your business plan for the next five years, and then the next 10 years, before deciding if upsizing or downsizing makes sense.

POWELL: Take the time to do the proper due diligence on your specific space needs, both now and five years to 10 years from now, before determining how much space you need. A good commercial broker has the experience and knowledge to assist in this process, and this step should never be skipped. An objective third-party can help a business owner do an unbiased analysis that can ultimately save considerable time and money for that owner.

ANDERSON: Relocating your company can be an exciting time. It can also be a stressful time trying to gauge how much more space or less space you need.

Ninety-five percent of my client base, over all of my office development career, has come to us for upsizing. That was even true during the downturn in the economy. In advising them, the first thing I do is introduce them to my architect and builder. We offer to do an office space plan for them on a no-fee basis for the first plan. Quickly, they can see if the space will meet their current and future needs.

I encourage them to look at their business model before making a decision. I've had clients take more space than they need in the short-term and then lease it out on a three-or five-year lease. They then have the option to take their own space and enlarge it when they are ready. What better way to grow than to own contiguous space? That way they own their own growth.

What are the most common mistakes people make when buying, leasing or building commercial property?

COLLIER: In terms of development, one of the most common mistakes is insufficient due diligence, such as soil testing, the presence of underground infrastructure, etc. Unchecked environmental or infrastructure aspects may negatively impact development costs.

DULL: I always tell people that they need to know what their five- to 10-year strategy is. If you are going to buy or build, then what does that exit strategy or growth strategy look like when the business owner is ready to do something else? Are you going to be at your location forever, or in 10 years are you going to do something else with that business? Have you built something that will be obsolete or that nobody else can use? You need to ask yourself those questions.

ANDERSON: They fail to plan for growth within their office or retail needs. They don't take the time to plan down the road. I find that they will focus way too much on current needs and not forecast for the future.

POWELL: Too many times companies buy or lease less space than they should. They consider the short-term position of what they need now instead of planning for growth. You need to think about where you want to be in two, five or 10 years and make sure you have the options available that will let you meet your future goals.

What is the top thing our leaders can do to help create new jobs in our region?

DULL: Allow commercial growth in the "right" areas. Commercial development is such a broad term and covers so many things. There is a right place for grocery stores, there is a right place for shopping centers, there is a right place for office buildings, and there is a right place for manufacturing and industry. We need to be sure that we allow those "right" places to exist and coexist with everything else.

Also, know what the majority of the people want and not just the loud few. Again, what does Wilmington look like for my children? Will they be able to come back and get a good job and enjoy a good lifestyle? I think that's the first question our leaders should ask every time.

POWELL: Put a great amount of thought and work into our new zoning regulations that would negate the need for New Hanover County's special use permit that was passed in 2011. Companies that are searching for new locations focus on places where the zoning laws are clear and unambiguous

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and do not involve a great deal of risk. They want to know how their business is going to fit into the new location (and proceed through the regulatory process) before they ever visit the areas they are considering. Site locators working for prospective companies look for reasons to eliminate a site. If we are giving prospective companies the impression that our decision process is subjective (as it is for many companies under the special use permit), we'll be off the list before they even conduct a site visit.

COLLIER: Continue with expansion of utilities capabilities and transportation networks. Expanding the Port of Wilmington to a deepwater port would increase opportunities for industrial manufacturing shipping, which would help create more jobs in the region. Reevaluating incentives for the film industry would bring back some of the jobs that have been recently lost in this area.

From the standpoint of commercial development, the North Carolina Department of Commerce's Certified Sites Program makes it easier for industries to locate qualified sites throughout the state. Through the program, sites are inventoried and pre-qualified to ensure they meet a consistent set of due diligence standards. This official process enables businesses to be up and running more quickly, thereby initiating new jobs sooner. McKim & Creed has extensive experience with the Certified Sites Program and works with businesses and industries to locate qualified sites as quickly as possible.

What are the transportation issues you would like to see addressed to assist with growth in the area?

POWELL: A supplementary route to divert truck traffic directly to the ports instead of routing them down Front Street would be welcome. The conversion of rail traffic around the city instead of through it also has a great deal of merit and will hopefully get some traction once the feasibility study is done. We also need to come to some sort of consensus on the treatment of Independence Boulevard to create another north/south corridor through the community as well.

COLLIER: As an engineer, land planner, and vice chair of the City of Wilmington Planning Commission, the top transportation issues I see concern relieving pressure on our roadways. Specifically, areas such as South Market Street, I-140 to Military Cutoff, and Independence Boulevard to MLK experience very heavy traffic. Completing the connection between I-140 and U.S. 17 and continuing to expand the airport and associated services will help alleviate transportation issues, and amenities like the Cross-City Trail provide safe pathways for people to walk, run and bike to their destination, rather than driving. McKim & Creed is helping with the issues by providing transportation surveying, subsurface utility engineering, full-service engineering, land planning and landscape architecture, and construction observation services for projects throughout this area.

DULL: To start with, we need more transportation dollars. When you look at a city like Charleston, S.C., they've been able to do it all. They have a great lifestyle in the city and region. They have great beaches. They have preserved their environment. They have a vibrant downtown. A lot of that is possible because of a great transportation system, including a great port, and that port was the driver of Charleston to be what it is.

We can provide the same lifestyle here, but what we don't have is the transportation infrastructure. When you think about it, it's kind of crazy that you have to wait to get in to Wilmington when a ship is coming through. Charleston figured out how to make that work. They've got tons of great software companies, but they have manufacturing too, like at Boeing.

Some people may not like it, but I think the port in Brunswick County would have been great for our long-term viability and the lifestyle we enjoy.

With future development, what opportunities do you see for redevelopment and infill?

ANDERSON: The Military Cutoff/Landfall/Oleander Drive corridor is going to see a lot of redevelopment and infill. For example, start at the traffic light at Military Cutoff and Wrightsville Avenue where we developed The Offices At Airlie – that vacant corner had been held by the same family for many decades. Even with all the new construction at Mayfaire/Landfall, we were sold out at The Offices At Airlie when we were only 60 percent through construction. That's a great sign that there is still a need for Class A office space on that end of town.

I also think it's going to be a natural progression for us to continue to see growth as we've seen in the Bradley Creek/Seagate community. We could have commercial growth continue down the Oleander Drive corridor.

POWELL: I would love to see our downtown area attract a good mix of local and national retailers like you see in Charleston, S.C. Our downtown area is such an asset and a more balanced mix of retailers would go a long way toward generating additional traffic into the area. And we need to attract more industry and manufacturing into our community. We have areas specifically zoned for industrial use and we should welcome companies for that use if they meet all state and federal regulations. U.S. 421 also presents an excellent opportunity to offer some new, shovel-ready industrial sites once water and sewer is installed.

COLLIER: There are huge opportunities associated with the large commercial properties that were built in the 1980s and 1990s and are now sitting dormant. These facilities can be upgraded to meet current standards, while underutilized properties can be reconfigured for mixed use.

A great example of an underutilized property getting a new life is the Water Street Parking Deck. McKim & Creed is working with East West Partners and the City of Wilmington on the public/private revitalization of this key downtown property, which will provide residential units, space for retail businesses, parking and more connectivity to other areas of downtown. In addition, downtown is rife with opportunities for urban infill development that could bring more residents, businesses and retail tenants to the area.

DULL: I think it's going to be a naturally occurring thing. The highest best use sometimes changes. In the city, you're pretty much at that point where most new development is going to be redevelopment. That will be the case in most of the city limits.

CHESHIRE: With future development in New Hanover County, one would have to consider that redevelopment of existing built-upon land is the most logical and potential opportunity for commercial growth. With the exception of a few large family landholders and individuals who still own tracts, New Hanover County infill land seems to be about 90 percent built out. It appears that either teardown and build-back or renovation will be our only option.

On the redevelopment side, I like how developers are looking to brownfield sites, or even better, renovation and restoration of our historic buildings. I personally love the idea of young entrepreneurs heading downtown and using the existing historic buildings to revitalize and rejuvenate our waterfront and streets.

There has been a surge of construction of apartment communities in our region. Do you see this as a problem? What do you see happening in this segment of the market in the next five to 10 years?

CHESHIRE: I do not foresee at this time any current problems with the surge of construction of apartment communities in our region. In fact, speaking as a previous apartment renter, one could look at these apartment communities as a positive in many regards. For the young working professional, they are a way to have affordable housing and easy upkeep, and typically the bundling of apartment utility packages helps maintain your balance sheet.

In the short and long term, apartment construction has and will create jobs

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for our market. In the short term, our labor, material and supplier forces are being put to work, allowing for local and surrounding markets to grow. In the long term, the job opportunities will be created for the management and maintenance side.

In the next five to 10 years, one could speculate that we will see a steady decline of apartment construction in fear of being overbuilt. However, the opportunity funds and strong equity groups could still see a profit in certain markets with apartment construction.

COLLIER: At colleges and universities, dormitory life has completely shifted, resulting in more and more apartment communities. Student housing is a market all its own. The student of today wants his or her own bedroom and bathroom, and companies in the business of developing student housing recognize the hot markets like Wilmington. The demand for multifamily housing is very high, and most complexes are pre-leased/pre-sold before the first shovel is put in the ground. In the future, developers will need to differentiate their properties from the competition to capture interest. It's not enough to build a nice apartment with a pool. Today's renters expect high-end finishes, outdoor activity spaces, and smart home technologies.

"The Military Cutoff/Landfall/ Oleander Drive corridor is going to see a lot of redevelopment and infill."

STEVE ANDERSON
The Offices at Mayfaire IV, V, VI LLC

POWELL: The new apartments going up in our community are meeting a significant need among college students, millennials and empty nesters who prefer to rent rather than to own. Since the recession, there has been a shift among a portion of these population segments toward renting versus buying. Time will tell if this demand continues in the long-term, but we do see some evidence of a fundamental shift in attitudes toward renting. I don't think the apartment inventory is overbuilt yet, but I think that we will need to keep a close eye on it to ensure we don't overbuild to meet the demand.

DULL: I'm OK with it and there's no doubt that McKinley Building Corporation benefits from it. I think what you are seeing is a new mindset of people after the Great Recession. They don't believe that homeownership is the golden egg that everybody grew up thinking it was. Think about it: The older generation used to work one job, buy a house, retire after 30 years and that house was paid for. The new model is that the average college graduate is going to work five different jobs in three different cities. They like the freedom and flexibility of being mobile. That's a new mindset and I think it is here to stay for at least a generation.

I think we'll see this trend lasting at least five years, but it will depend on how quickly the market becomes saturated. Jobs are a factor too. If there aren't new jobs, you'll hit that saturation point because you won't be creating that market for new residents.

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