



MID-YEAR 2016

The Innovation Issue

New Horizons

**Futurists Roundtable:
What's Next for Real Estate**

**Cutting-Edge Projects
From Around the U.S.**

Get Ready for Gen Z

Survival of the Fittest

How commercial real estate will evolve

By Amanda Marsh

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With urbanization, technology and demographic shifts transforming commercial real estate faster than ever, the industry is poised to look drastically different within the next decade. Four thought leaders share their perspectives on where it's headed.

CPE-MHN: To what extent will larger cities continue to draw investment, development and population during the next five to 10 years?

LINNEMAN: The central core cities will do quite well. I wrote my thesis in 1976, when Baby Boomers were young and deferring marriage and childbirth. My thesis said that cities would revitalize, and that happened—even in places like New York City and Cleveland, which were bankrupt and where things were pretty dramatic. Today, there are more Millennials than Boomers, and they're getting married and having children even later. This means the urbanization trend will last a little longer. And as long as there's population, investment will come.

STEINER: Around the world, the percentage of urban population versus suburban population has surpassed 50 percent. But to be successful, these environments must include a strong mix of uses including retail, restaurants, entertainment, residential and office, with great access to transit. Boomers are moving back to downtowns for the same exact reasons that Millennials want to be there: walkability, ease of access and a sense of place and community.

CURRAN: There is clearly a trend toward urban living that has accelerated in the past decade as the oldest Millennials have entered adulthood—and there is another wave of Millennials that will come of age in the next decade.

KELLY: Twenty-four-hour cities have proven (to have) superior investment returns over time. And 18-hour cities are moving up the scale in returns, especially for multifamily. These are places like Houston, Austin, Nashville and Seattle—they're desirable, walkable, and as a result, capital magnets. If you're not a 24-hour city already, it's expensive to become one. You have to invest a lot of money in infrastructure, commit to high-quality services and grow your tax structure. There are very few places that have the

appetite to increase their tax revenues, but cities that don't are in a race to the bottom.

CPE-MHN: How about the suburbs?

CURRAN: We are already seeing the urbanization of the suburbs—nodes of retail and businesses that are clustered in areas that are within walking distance of homes. You used to have to get in your car to go anywhere in the suburbs. That is starting to change in some areas.

STEINER: We will continue to see planners and developers focusing on projects that create town or village centers or hubs where people can gather. Performance will be driven by the developer's ability to curate the right mix of uses as well as their ability to effectively integrate into the greater community.

KELLY: The configuration places need to have if they are to grow in a healthy way: well accommodated to transit, walk-to-work housing and attractive education, from the K-12 to the university level. If you don't have these, your viability for growth in the future goes down.

LINNEMAN: Selected suburbs are actually growing faster than some cities. If you look at Bureau of Labor Statistics data, suburbs are still growing, but not at the pace of 20 or 30 years ago. But the pace of Millennials going into suburbs is greater than the pace of Millennials going into the cities. However, both are seeing increases in population; it's not a rob-Peter-to-pay-Paul situation.

KELLY: We have 320 million people in our country, and that will grow to 400 million by 2050. They're going to spread out around the country, and not just the cities.

LINNEMAN: The headline of Millennials moving to the city is actually a bit overhyped. There is a reality that will hit them when they have children: Living on the fifth floor of a five-story walkup

on top of a bar won't be as enjoyable. We'll see more Millennials move to the suburbs as their children hit school years.

CPE-MHN: What major changes are on the way for the commercial real estate sector?

LINNEMAN: We're still trying to figure out what Millennials will do and where they will stay permanently. Developers are building apartments and cool office space for them, but will they want that when they're 40?

CURRAN: Work spaces will continue to evolve to meet the changing ways we do business. Although large corporate offices will not go away, I expect we will see a reduction in the number of people who choose to work from a home office. The develop-

ment of co-working space is accelerating, and developers are toying with co-living spaces now.

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CPE-MHN: What are you expecting in regard to the role of technology in commercial real estate?

STEINER: People talk about smart building technology being a disruptor, but it's a normal progression, and things are only going to get better. We'll see an evolution, not a revolution.

LINNEMAN: History has had nothing but technological advances, yet we use more space than we used to—we have bigger buildings, and more of them, because of technology. Skeptics have said it would decrease real estate usage. In reality, what it's done is changed the way we use real estate but not reduced the overall demand for real estate.

CURRAN: We will need to approach technology upfront and holistically or we will lose our ability to compete. But certainly we can expect technology to become more integrated into our working and living spaces. It will also be interesting to see how artificial intelligence develops in the coming years and the impact it will have.

KELLY: We have to remember that technology is an ally, not the enemy. There's a long history of technology heralding the so-called death of distance, including the telegraph, telephone, fax machine and Internet. All these advances actually helped cities concentrate and grow.

KELLY: Commercial real estate has enormous flexibility—when properties reach their economic utility, their uses can change.

STEINER: Both office and multifamily are moving in closer to hubs so that they are more connected to their surrounding communities. This allows them to integrate with other uses and really enhances the mixed-use environment. We'll also see much less single-family residential as demographics continue to change. As for shopping center development, you don't have to look too far to see how the Internet is affecting the sector.

CPE-MHN: What should the industry expect when things start to slow down next time? How well are the industry's main business lines preparing?

KELLY: Anyone who forgets that real estate is cyclical is going to set themselves up for disaster.

CURRAN: We have been experiencing a slow and prolonged recovery, which is allowing the industry's main business lines to make thoughtful investment decisions. It is difficult to be entirely prepared for something you have no control over timing-wise. But

CPE-MHN: How would you characterize the industry's efforts to recruit and retain the best possible professionals?

LINNEMAN: Wharton's Zell-Lurie Real Estate Center—the system I was part of—and UC Berkeley's Fisher Center for Real Estate & Urban Economics have created programs that other universities are now using to raise talent levels in the industry. Real estate has done a better job than any other industry at upping their game in terms of training, and we're well positioned to recruit talent due to the efforts of these schools more than a quarter century ago.

KELLY: If you're growing your economy and wealth, you have

impact on the buildings' insulation and consumption levels.

CURRAN: Urban storm water runoff needs to be a critical focus in the development industry, as it is the greatest source of water pollution.

KELLY: I spoke in Strasbourg before COP 21 and discussed sustainability from the real estate perspective, including New York City's PlaNYC program for 2030, which includes 248 individual sustainability programs. People in Europe asked me, "How can we afford all of this?" I told them, "When you're a city with \$20 billion in real estate taxes, you can do this kind of planning and

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to look at how to take entry-level jobs and make them something other than dead-end. And commercial real estate is in an excellent position to be a leader rather than a follower. As we have more office, apartment, retail and industrial buildings, how can we turn entry-level jobs into careers?

CPE-MHN: Is it still possible to move up the ladder?

KELLY: It can be done—one of my students at NYU started off as a laborer carrying bricks in a Utah housing development, and now he's an executive for a major trade association. A hotel developer told me about one of his managers who started off as a valet parker. In my own case, I started in real estate relatively late, at age 29, and was sent on a three-day temp assignment to Landauer Associates to do copying and filing. I left the company 22 years later as its chief economist. There are tens of thousands of opportunities to do this, and we need to focus on them.

CPE-MHN: The industry is embracing sustainability on multiple fronts these days. What do you think is ahead?

LINNEMAN: It has to make the bottom line better. Those technologies will get adopted; everything else will just get lip service.

STEINER: Office and mixed-use developers are taking more advantage of the weather, such as collecting rainwater to retain hydrocarbons and using filtered outside air. It has had a great

implement it." Sustainability is important on all fronts, but more affordable when you have good value in your real estate base.

CPE-MHN: What is the single biggest challenge facing commercial real estate in the next 10 years?

CURRAN: Infrastructure, infrastructure, infrastructure. Both cities and suburbs that are not adequately prepared with public transit to link employment centers to residential neighborhoods will suffer. Other infrastructure like adequate power—particularly with the increased needs due to the expansion and integration of technology—will also be critical.

LINNEMAN: In the long term, real estate is about housing economic growth. And this growth is increasingly challenged by an ever weakening societal commitment to educational excellence.

STEINER: Retail is undergoing a huge transformation. Twelve percent of sales are online, and that number will jump to 20 percent in the next 10 years. People are also eating less and buying less. In the hotel sector, Internet reservation systems are making the bigger brands nervous, because boutique brands can do just as well as flagged brands.

KELLY: Financial amnesia is a recurrent cause of financial euphoria. We need to learn the hard lessons of past failures. We also need to focus on innovations that are going to last. Identifying them, though, is a big challenge. 