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National Office Report

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Office Conversions Have Appeal, But Challenges Abound

- As the office industry struggles to adjust to a new paradigm in the waning stages of the COVID-19 pandemic, interest in the conversion of underperforming assets is beginning to grow.
- Lab space is in high demand, with mRNA technology unlocking the door for researchers to study treatments for everything from HIV to heart disease to cancer. These researchers will need new lab space, much more than is currently available, and conversions will be part of the supply response. Leasing volumes are down across the board in office, with the exception of life sciences. A recent report from Newmark stated that new lab space in prime markets leases at a 20-40% premium over general office.
- Interest in conversions is sparking transaction activity. The \$1.2 billion purchase of 401 Park in Boston, the largest sale of the year, was made with intent to convert the building into lab space. In the Bay Area, Longfellow Real Estate Partners spent \$178 million on the San Mateo Bay Center, with an eye towards life science repositioning.
- For most offices, however, conversions into life science space may be unfeasible. The biomedical and life science industries are clustered in a few markets. Cushman & Wakefield reported that nearly three-quarters of all North American investment in life science firms is concentrated in Boston, the San Francisco Bay Area, San Diego, New York City and New Jersey. While growing demand for lab space may create opportunities in new markets, for now conversion opportunities will remain highly clustered. Outside of geographic challenges, life science buildings typically require large floor plates and high ceilings, eliminating most towers as a possibility. Additionally, zoning may create a roadblock.
- Conversions into multifamily are gaining interest from both owners and elected officials looking to increase housing supply. As an example that may serve as a template if successful, the New York state legislature recently passed a bill that allows New York's Housing Trust Fund Corporation to purchase vacant hotel and office buildings and convert them into affordable housing. Converting a building into an apartment does not have as many constraints as life sciences, but still comes with its own unique set of challenges. If floor plates are too large, apartments may not be able to get natural light or proper ventilation. As with life science conversions, zoning may also be an issue.

