



Mixed-Use Center Conversions, Part II: Achieving Optimal Market Position

Case Studies Show Why Each Project Requires Unique Synergy—and the Patience To See a Complex Process to Completion

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Abstract: A previous article, “Mixed-Use: The Economics of Place-Making,”¹ addressed how residential uses work with the retail and services model in shopping centers. The four brief case studies in this article demonstrate in practice the process required to transform regional malls or department stores into mixed-use centers.

How To Tell If a Mall Is Struggling

The signs of a struggling mall are readily apparent, including:

- Numerous vacant spaces, particularly in the zone around a department store in decline;
- An outdated food court filled with substandard restaurant proprietors;
- A physical space showing signs of aging due to deferred maintenance of the building and parking fields.

Consequently, a number of tenants pay little, if any, rent. Moreover, a shift toward value in consumer spending patterns, preferences and tastes is indicated by newer power centers, grocery-anchored community centers and lifestyle centers which further dilute consumer spending potential for retailers at a regional mall.

Mall owners faced with such declining centers and more competitive environments need to evaluate the highest and best uses of the property. By necessity, this includes a thorough evaluation that curates a more selective modern blend of retailers, restaurants, entertainment and services unique to the local market.

At street level, a mixed-use redevelopment is a dynamic mix of these selected uses that attract and support viable non-retail uses, such as a limited-service hotel, medical office and residential

housing. Such specialization enhances the center’s differentiation from the rest of the market, and it is this dynamic that adds value to the property and increases returns to the owners-investors.

The conversion process, however, requires market intelligence, strategic planning and patient capital. “Patient capital” will be discussed shortly for a particular project, but it is best to discuss the other two concepts in a general manner at this point.

Market intelligence means understanding the underlying reasons for changes occurring in the local retail market. This requires quantifying those changes relative to new retail opportunities. For example:

- How many retail square feet are supportable?
- What type of retail (e.g., off-price, big box, specialty, etc.) is viable?
- Who are the market-viable retailers, restaurants, or entertainment uses, their footprint size and estimated sales volumes?

That market intelligence must be part of an actionable *strategic plan*. For example, the quantification of the local market, including the viable retailers and their sales volumes, becomes a leasing tool, as well as the basis for a project pro-forma analysis.

A closer look at some regional mall-to-mixed-use redevelopment projects underscores these points.

Lessons Learned

The conversion from a regional mall to a mixed-use center that enhances the local market and community is complex, requiring:

- The *need for different forms of patient capital*: professional, financial, political, and social.
- *Protecting, stabilizing and growing the asset base* from where it is today.
- *Maintaining the support for existing tenants* (e.g., through short-term renewals).
- *Building a long-term leasing and asset uses master plan* that moves the regional mall toward optimal market position as a mixed-use center.

This process does not occur overnight—which is why some conversions may not occur as quickly as department store closings.

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¹ Jerry Hoffman, “Mixed-Use: The Economics of Place-Making,” *Industry Insights: Industry Sector Series* (ICSC), February 20, 2018.

Case Study

Ballston Quarter, Arlington, VA

Forest City's conversion of Ballston Common Mall, a 590,000-square-foot regional mall, into a four-level mixed-use development started with a proposal in 2013. Renamed the Ballston Quarter (see the Figure 1 rendering), it is located four miles from downtown Washington, DC, close to two Metro stations, Arlington National Cemetery and Pentagon City, and a 15-minute drive to Tysons Corner.

Macy's has anchored this part of Arlington since the early 1950s. Other tenants include a Hecht's furniture gallery, a 12-screen Regal cinema with stadium seating, and a sport & health club.

Approximately 310,000-square-feet of the mall is under renovation. Delivering over 400-apartment homes in a 22-story high-rise in late 2018, Ballston Quarter will be integrated into this mixed-use space referred to as Arlington's "new downtown."

This property is located in a vibrant economic hub, the Rosslyn-Ballston Corridor, which is dense with office, commercial and residential properties. It is also surrounded by some of the most affluent suburban neighborhoods of D.C., with average household incomes from \$181,000 to above \$250,000 close to the Ballston Common Mall. Residents are well-educated with sophisticated tastes and lifestyles.

Ballston Quarter is a response to strong demand for housing in the Ballston-Arlington market. The quick apartment lease-up velocity in this market is attributable to high-income renters.² This is especially the case among the household segments of 20-to-34-year-olds (i.e., young professionals) and empty-nesters. Approximately 532 new apartment units were delivered over the previous 12-month period (November 2016 to November 2017), and net absorption was 551 units. Due to the appeal of this dynamic mixed-use market, there is a reported 25 percent rent premium, thus attracting new residential development.³

This development will also appeal to a uniquely curated mix of retail tenants, restaurants and perhaps a specialty grocer. The opportunity exists for a tenant mix that would keep the daytime population in the area longer after work, while activating the area at night and on weekends by both residents and visitors. [Bethesda Row](#) and the newer [Pike & Rose](#) development are good analogs for the Ballston Quarter project.

The Ballston Quarter-Ballston Common Mall mixed-use project is an example of how Forest City is rethinking the regional mall relative to dynamics of the local marketplace in a Tier 1 market.



Case Study

University Mall, South Burlington, VT

Ballston Quarter also reveals that the opportunities for regional mall redevelopment into a mixed-use project are uniquely local, not formulaic. How does that work when the regional mall has gone into foreclosure?

University Mall, located in the Tier 3 market of Burlington, VT, is one example. The attempt to transform it into a mixed-use center, which stalled last year, demonstrates that such projects may take time and encounter difficulties before proceeding.

Such obstacles also vividly illustrate the need for different forms of *patient capital* and the areas in which they apply, including:

- *Professional*: Management, leasing, marketing and operations;
- *Financial*: Owners, lenders and investors;
- *Political*: Planning, zoning, and entitlement; and
- *Social*: Consumers, neighborhoods, and media.

Built in 1978, this 693,000-square-foot enclosed regional mall is anchored by JCPenney, Sears and Kohl's. The mall was renovated in 2005 and foreclosed in 2016.⁴ Coupled with substandard net operating income associated with low-performing existing retailers, there is strong retail competition less than three miles away: Burlington Town Center.

Furthermore, Bon-Ton was due to vacate its 60,000-square-foot space in January 2018. This is one of the 42 stores being closed as part of Bon-Ton's Chapter 11 bankruptcy. In its place will be a new Target store, the first in the state of Vermont, that is scheduled to open in October 2018.⁵

This situation raises several investment issues:

- *What are the highest-and-best uses for this property?* For example, if residential uses are supportable, then what are the product

² 2017 CoStar Group.

³ *Ibid.*

⁴ Dan D'Ambrosio, "[University Mall Falls Into Foreclosure](#)," *Burlington Free Press*, July 21, 2016.

⁵ "[The Bon-Ton Stores, Inc. Announces Closing of Its Bon-Ton Store in South Burlington, Vermont](#)," October 18, 2017 company press release; "[KeyPoint Partners Procures Target's First Vermont Store](#)," *Boston Real Estate Time*, November 15, 2017.

Case Study

University Mall, South Burlington, VT (continued)

types (e.g., apartment rentals, townhomes, condominiums, etc.)? To whom do those product types appeal?

- *What is the estimated rent revenue and net operating income from new residential development?* What is the market timing for that development?
- *Can the property be acquired for a price that justifies the capital requirements* to convert from a regional mall to a mixed-use development?

Despite the center's recent financial problems, University Mall remains a prime piece of real estate at the center of the South Burlington trade area, between the Burlington International Airport and the University of Vermont. Conversion to mixed uses permits the property ownership to incorporate a residential component that best fits the market opportunities. This is underscored by Target's decision to move into the vacated Bon-Ton space. Target's arrival will capture consumer market share for the retailer. Moreover, the smaller-format Target lends itself to a mixed-use development that is made dense with residential housing formats (i.e., apartments, townhouses, senior housing, etc.).

Using PRIZM[®] Premier 2017, a lifestyle segmentation system by Claritas, Map 1 illustrates that the University Mall property is positioned along a key demographic boundary. That is, the trade area has two dominant life-stage groups:

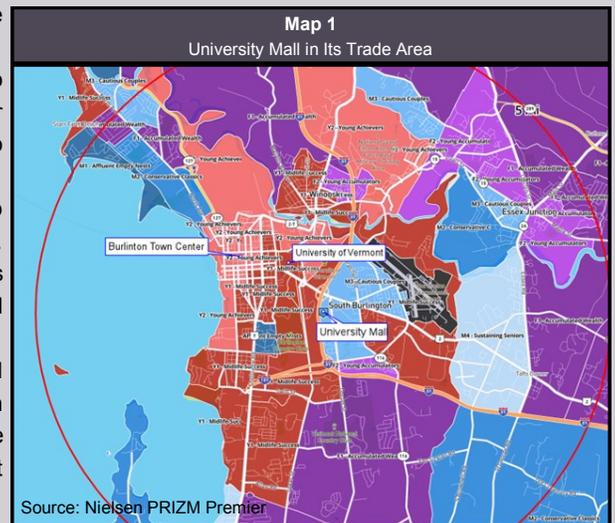
- *Young Achievers*, a cohort of approximately 25-44-year olds that are college-educated and upscale professionals; and
- *Accumulated Wealth*, an older group comprising 55-to-74 year olds, which includes empty-nesters and retirees.

Retail may not be the main use of the University Mall property, as has been recognized by its ownership.⁶ In addition to apartments, the Burlington market may also have a strong demand for senior housing product, such as independent and assisted-living units (e.g., continuing care communities with different levels of services to meet the needs of an aging population).

Additional nearby medical-office and medical care clinics may be needed to support residents in these properties. Moreover, as the population lives longer and enjoys a more active lifestyle, these new communities will need to integrate entertainment venues, restaurants and other social gathering places.

However, the redevelopment project has stalled and is now in receivership by LNR Property. This property is now being managed before it goes on sale. Meanwhile, the City of Burlington is supporting a \$300-million project across the street. CityCenter, anticipated as the new downtown for the city, will include apartments above ground-level stores and restaurants.⁷

University Mall could have stalled because of the existing reciprocal easement agreement among property owners, an extended financial situation on the property limiting the capacity to support the mall-to-mixed-use conversion. These conversions require access to deep pockets and to patient capital.



Case Study

Phipps Plaza, Buckhead, Atlanta, GA

Deep pockets and patient capital lay the foundation of Simon Property Group's transformation of Phipps Plaza from a conventional three-anchor shopping mall to a dense, urban mixed-use village in the Buckhead neighborhood of Atlanta, GA.

Phipps Plaza has served as one of the most affluent markets of Atlanta since 1968. This premier upscale regional mall, with over 800,000-square-feet of gross leasable area, and anchored by Nordstrom and Saks Fifth Avenue:

- Completed a major exterior renovation in 2016;
- Added a 166-key AC Hotel by Marriott to the parking lots on the east side of the property in 2016; and,
- Domain at Phipps Plaza, located adjacent to the AC Hotel, has absorbed nearly 250 of the 319 luxury residential units since opening in Q1 2017.

And Simon Property Group has plans for even more densification of Phipps Plaza. A \$200 million-plus project scheduled to open in phases through 2020 includes a 150-key Nobu hotel and restaurant, a 12-story office building and a 90,000-square-foot Life Time[®] Athletic fitness center. Belk is scheduled to close its 170,000-square-foot store, and that property will be incorporated into the overall mixed-use development.

More than a conversion into a mixed-use center, Phipps Plaza is being transformed into a sophisticated urban village reminiscent of European cities.

⁶ Phillip Tortora, "[University Mall Owner Pitches Mixed-Use Redevelopment](#)," *Burlington Free Press*, January 19, 2016.

⁷ Molly Walsh, "[Malls: Vermont's Largest Retail Complex Faces an Uncertain Future](#)," *Seven Days*, December 20, 2017.

Case Study

Ponce City Market, Atlanta, GA

Jamestown—already well-known for developing elsewhere in the U.S. retail-food emporiums such as New York’s Chelsea Markets—has also created a European-style village in Atlanta, GA, known as Ponce City Market. This is an adaptive reuse of a former Sears, Roebuck & Co. store and distribution center located in the Old Fourth Ward, northeast of downtown Atlanta and near the Jimmy Carter Presidential Library.

Ponce City Market embodies a more organic form of an urban village. The uses are well integrated, and the tenant mix is curated to create a unique place-based experience. Ponce City Market includes:

- Over 230,000-square-feet of retail with tenants such as West Elm, Anthropologie, Williams-Sonoma, and Rejuvenation;
- An innovative Central Food Hall;
- 258 residential units known as The Flat; and,
- Offices that have tenants like Techstars, a start-up accelerator program, and Industrious, a flexible office space for growing startups and small businesses.
- A creative use of its rooftop for entertainment purposes (e.g., mini-golf, a beer garden, slides, and rental space for weddings).

There are other innovative, adaptive reuse projects such as the Helms Bakery District in Los Angeles, Union Market in DC, and the former Coca-Cola bottling plant in Indianapolis (now under construction). These are different from the mall-to-mixed-use conversion projects; however, there are fundamentally similar issues at play, such as that:

- Adaptive reuse relates either to an old building or an aging mall;
- Uses are built-to-the-market dynamics; and,
- Breadth and depth of financial and political capital are needed to ensure long-term viability.

Conclusion

These brief examples illustrate that regional mall-to-mixed-use center conversions mirror the fundamental economics of the local marketplace; this is not a formulaic model equally applied across markets. However, this is increasingly being done in the United States and represents a clear trend. Residential uses, in particular, offer a lifestyle amenity to a more modern and uniquely curated retail, restaurant and entertainment tenant mix. And that mix is a rich amenity to the residential properties. This synergistic dynamic

can also achieve rent premiums for both the retail and the residential properties.

The conversion process, however, requires extensive market intelligence, strategic planning and patient capital. Often these market and project analytics are used in obtaining financing backing of a redevelopment plan. This is one reason why conversions are not happening as quickly as the closing of anchor department stores. To make strategic moves requires time—not to mention agile coordination of multiple processes.



Jerry Hoffman, Owner and President of Hoffman Strategy Group, is an economist with over 25 years of extensive experience in economic and market analysis that provides insights for all pieces of mixed-use projects. Core project specialties include urban retail corridors, infill, and suburban mixed-use, as well as shopping center re-purposing and redevelopment, entertainment district development, university-led development, and adaptive reuse of property. For additional information, visit hoffmanstrategygroup.com or contact Mr. Hoffman at jerry@hoffmanstrategy.com.

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