

Analyzing the Risk/Rewards of D-I-Y Vs Teaming With Others in Mixed-Use

[By Don Briggs]

Mixed-use is the newest buzzword in real estate, but developers looking to build these projects should understand one basic underlying fact: combining different uses in one development is more complicated than simply stacking office or housing space over a store.

Developing mixed-use projects requires expertise in multiple formats: residential, retail, office, hotel and infrastructure, and only a few companies have the expertise to build all or most of these formats. In addition, the development process for these projects is longer, the construction more expensive and the prioritization and integration of uses more complex than building each individual element separately.



Pentagon Row in Arlington, Virginia, consists of 296,000 square feet of gross leasable area. It was built in 1999.

Mixed-use developers must carefully analyze the elements in each project and match them with their own capabilities, so that they can make the determination to bring in others or go it alone.

Having developed many mixed-use projects over the years, Federal Realty has learned to adapt its development models to suit each project. For decades, the company was an owner of neighborhood and community retail centers. In the early 1990s, it became involved with mixed-use through the development of Bethesda Row in Bethesda, Maryland. A strong move back to the urban core was taking hold in the country, as empty nesters no longer needed large homes and young professionals were seeking social interaction. The company began by integrating individual urban buildings and retail streets, but soon found that these projects were more complex than a typical suburban retail center. What we needed to do was to design our own street.

The Bethesda Row site is located near a Metro stop, with existing infrastructure - including a county-owned parking garage -- and it was also close to company headquarters in Rockville, Maryland. As a result, Federal Realty could build the project -- office space over ground-floor retail -- on its own.

That project was so successful that the company ventured into two more mixed-use complexes almost simultaneously, but approached them differently. For Pentagon Row in Arlington, Va., Federal Realty built the retail development and Post Properties built the residential portion. In contrast, the company decided to build Santana Row in San Jose, California, alone, learning a great deal about mixed-use development, risks and rewards, as part of the process.

Lessons Learned

Theoretically, developing in conjuncture with another group should mitigate financial risk, while adding expertise to a particular format. Post's experience in multi-family housing certainly helped Pentagon Row, which consists of more than 500 apartments above 296,000 square feet of retail.

But the development arrangement has to be structured properly. By being co-owners directing the general contractor, Federal Realty ended up sharing timing and cost risk from the other party's development. Pentagon Row has a solid yield now, but Federal Realty believes that the project taught them that one company should build the structure and deliver it to the other party.

Santana Row was an even greater lesson in the risk/reward relationship. The company's \$500