Manhattan's building boom a quandary for aging office complex

NEW YORK | BY HERBERT LASH

A new skyline rising across Manhattan poses a challenge for the owners of the city's aging office buildings as they face expensive overhauls in order to compete against a wave of amenity-rich towers nearing completion.

Manhattan has the oldest office infrastructure in the world, and record levels of available space by 2017 will test the moxie of landlords who are losing top tenants to the new buildings mostly going up in Lower Manhattan and on the West Side.

Firms such as Time Warner Inc, News Corp, L'Oreal and Conde Nast, among others, already have moved or agreed to relocate either downtown at the developing new World Trade Center complex, or the West Side's new Hudson Yards district.

By the end of the decade, about 18 million square feet of new office space will be built in the biggest building spree that New York has seen in more than three decades. While just 4 percent of the city's entire office space, even owners of prime Class A space need to ensure they can retain or sign the best tenants.

By late next year, big blocks of space will open up, adding pressure to a market with nine or 10 buildings, largely in Midtown, that realtor Savills Studley says already are struggling with "empty building syndrome" - tenant vacancy rates of 75 percent or higher.

"Unless there is some big wellspring in demand and unless there's a bounce-back in the core tenants - the financial and legal sector - we don't see where the demand is going to come from," said Keith DeCoster, director of U.S. real estate analytics at Studley, a unit of Savills Plc.

To nab tenants, some landlords are getting creative with renovations, and some even had to wait years to empty a building of tenants that had long-term, staggered leases.

Developer L&L Holding Co LLC waited a decade for leases to expire last year so it could "re-imagine the geometry" of a 1953 building at 390 Madison Avenue once occupied by United Nations offices, said L&L co-founder and chief executive David Levinson.

When finished in 2017, the building just north of Grand Central Terminal, could help spur renewal of a largely nondescript stretch of Midtown, a long-time office district where the average building age is 75 years.

Three million pounds of steel and concrete will be gutted from the 24-story building's base

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and eight new floors will be added on top.

MAKEOVER

The makeover aims to compete with newer structures and overcome a zoning hurdle: a completely demolished structure would have had to be smaller in size. By retaining most of the structure, only 18 percent will be dismantled, the new building will have the same square footage as the original.

The new design includes a three-story atrium, an open-air deck, the gutting of four floors to allow for two new ones that are double-height and a new corner at 46th Street inspired by Alice Tully Hall at Lincoln Center. Sunlight is maximized with floor-to-ceiling, energy-efficient glass exteriors throughout.

"You're going to definitely see more of this," Levinson said. "If the owners don't do it, their buildings are going to be what we call commodity buildings, and they're going to rise and fall based on when the tide comes in."

Levinson declined to say how much the makeover will cost. The New York Post said the building's acquisition and renovation might approach $1 billion.

Another pressure point for landlords is space per worker has been cut in half since the 1980s. When law firm Skadden Arps moves to 1 Manhattan West in five years, it will reduce its footprint to 550,000 square feet from more than 800,000, Studley's DeCoster said.

The departure of Skadden Arps and Conde Nast from 4 Times Square from a building that debuted to much fanfare just 16 years ago has led owners the Durst Organization to plan $80 million to $100 million in renovations, said Tom Bow, who is in charge of leasing at Durst.

Amenities will be anchored by an existing Frank Gehry-designed cafeteria and will include new private dining, a conference room and possibly a gym, Bow said.

Renters may lease less space than the past as they shed boardrooms or other areas no longer used daily, and opt to rent communal areas provided in the re-designed building, he said.

The challenges for these structures have emerged even though Manhattan real estate remains strong because of heavy appetite from foreign investors and well known companies such as Facebook and Twitter. The availability rate is just 4.2 percent in Midtown South, Studley says.

Many expect the new space to be absorbed as the building boom is less speculative than three decades ago, when large buildings were built without tenants lined up.

"You cannot equate the next cycle with the downturn of the late '80s, early '90s," said Michael Cohen, president of the tri-state New York area at Colliers International.

"But you can say the math simply argues that the new construction being done...is going to leave in its wake increasing inventory in other parts of town," Cohen said. (Reporting by Herbert Lash; editing by Grant McCool)