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## Los Angeles Market Creative Office Trends and Workplace Strategy

**CBRE**

Summer 2013

## INTRODUCTION

Companies across all industries – from media and technology to financial services and law firms – are continually seeking a competitive advantage by creating workplace strategies that optimize efficiency, collaboration and creativity. Organizations have acknowledged the fundamental role of the workplace in the competitive business environment, but they are now paying closer attention to the design of the physical workplace and its effects on employee creativity, increased efficiency and overall performance.

Many studies have explored the link between the physical environment and innovative thought. The outcome of these studies suggests that when seeking a place to think and work creatively, individuals will consistently choose spaces that are more dynamic and conducive to social interaction and collaboration – these spaces are defined as creative spaces. Creative spaces are often distinguished by designs that include work environments full of visual detail with extended views throughout the workplace. The designs use more natural materials and elements such as exposed ceilings and duct work, large windows and skylights, open kitchens and polished concrete floors.

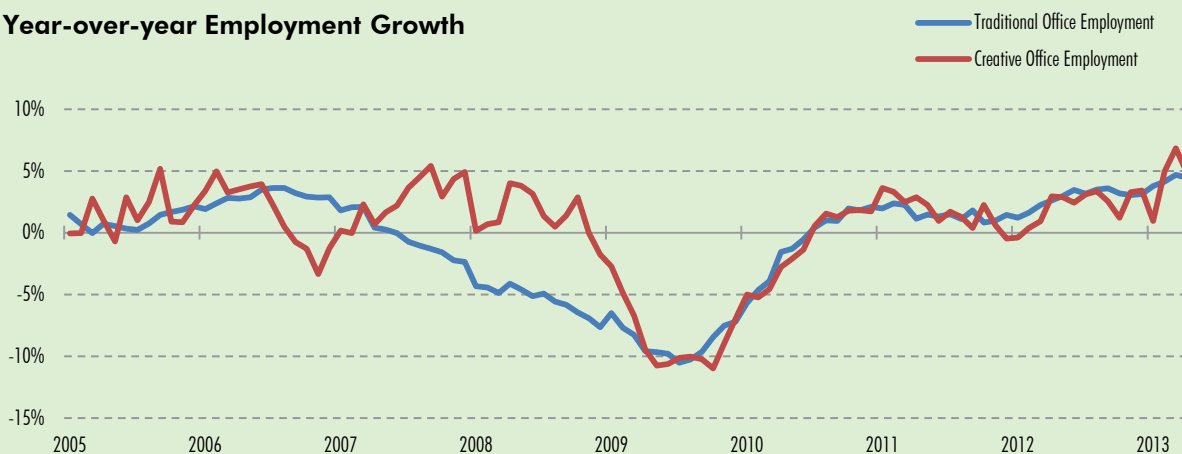
Creative space has long been reserved for companies like entertainment and media firms, ad agencies, architects, technology and other industries that rely on the creative class of workers as their core competency. Demand for this type of space surged in the late 1990’s during the dot-com boom as tech companies created work environments filled with collaborative workstations, shared office space and creative outlets for their ultra-creative workforce. Now, demand for creative space is surging once again as the working environment is more global, more mobile and more diverse than ever before.

The burgeoning demand for creative space has now extended into the more traditional office environment as many real estate companies, financial firms, law firms and other traditional office tenants have joined the fray. Many of these firms are serious about developing a creative workplace strategy by eliminating the traditional cube environment and executive offices in favor of highly-functional shared workplaces. These strategies focus on space optimization, increased collaboration, enhanced culture, employee wellness, and the ability to attract, engage and retain top talent.

## EMPLOYMENT TRENDS – CREATIVE OFFICE OUTPACING THE MARKET

In April 2013, non-farm employment in Los Angeles County grew to approximately 2.9 million jobs. Of the total, roughly 350,000 jobs were in the creative industry sector. Although the entertainment industry employs the greatest number of creative office workers at nearly 40%, jobs are diversified and extend into many industries such as entertainment, media, high tech, advertising, fashion, architecture and software. These jobs account for more than 35% of the total office-using jobs in Los Angeles County, having a significant impact on the health of the office market throughout the region. Compared to last year, creative office employment grew by 4.8% in April, led by the entertainment industry which grew by approximately 6.9%.

### Year-over-year Employment Growth



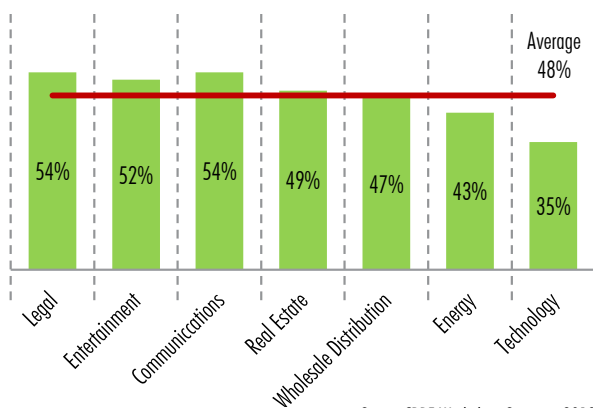
Source: CA Employment Development Department & CBRE Research & Consulting, July 2013.

## DRIVERS OF CHANGE

Traditional space configurations are being underutilized and are often inefficient for today's modern workforce. Recent 2013 figures from CBRE's Workplace Strategy group provide a deeper understanding of current space use. On average, office space is only occupied roughly 48% of the time. These figures vary depending on the type of organization and their departmental focus, but this trend is relatively consistent across traditional industry sectors and across business service lines. Additionally, the nature of the work during occupancy is spent primarily on the computer or on the phone, activities that can be completed in any environment.

These utilization metrics can begin to help a firm properly identify and analyze their optimum workplace requirements. While there is not a one-size fits all approach, companies today are looking to reinvest capital into technology and a more modern environment that incorporates various elements of creative office space. Design features typically include open seating, collaborative workspaces, focus rooms, learning corners and socialization areas.

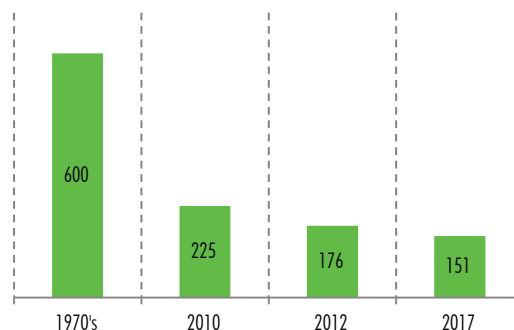
**Figure 1: Seat Utilization by Industry**



Source: CBRE Workplace Strategy, 2013.

However, truly creative spaces also reinvent paradigms of employee adjacency, develop a unique brand identity and find ways to create inside-out work environments. Companies are looking to create something unique, a lifestyle within their workplace that reflects their firm's culture and their employees' personalities. These spaces are designed with a commitment to sustainability as companies want their space to be environmentally friendly. Technology also plays a large role in creative

**Figure 2: Office Space Per Worker (per sq. ft.)**



Source: CoreNet Global, 2012.

office space as the designs typically find new and innovative ways to use evolving technology.

Many of these firms are also reducing their overall footprint while providing greater efficiencies and increased employee performance. In a 2012 report published by CoreNet Global, the average allocation of office space per person in North America will experience a significant fall within the next five years. According to the report, the average sq. ft. per worker for all companies in 2017 will fall to approximately 150 sq. ft., compared to 225 sq. ft. in 2010 and 600 sq. ft. in the 1970's. At least 40% of the 465 companies responding to this survey indicated they expect to reach this all-time low benchmark of office space per worker.

Generational diversity in today's workforce, which has been infused over the past decade with younger workers, is also playing a key role in the evolving workplace. The overall demographic shift is moving away from the Baby Boomers (born 1946-1964), who are transitioning into retirement to the Millennials (born 1982-2004) who will soon become our next generation workforce. This massive shift is changing the way work gets done as this new generation of worker brings a different mindset with expectations for a unique work environment. The younger workforce is drawn to a more creative and collaborative workplace within districts that have redeeming qualities and include desirable lifestyle amenities and services.

Another driver for change was the economic recession in 2009. During the downturn, there was an immediate need for companies to build a smaller but smarter office in a troubled economy. Since 2010, the demand for creative office environments experienced a noticeable acceleration period as tenants began to renew their



**CASE STUDY – GENSLER**

**Assignment**

The Los Angeles office of Gensler operated in their Santa Monica location for more than 15 years. However, their space was very outdated and their rent obligation was significantly above market value.

**Challenge**

The biggest obstacle in their search was reaching an internal consensus on where the firm should be located. Many within the company wanted to be in downtown Los Angeles, while others wished to remain in West Los Angeles.

**Results**

Gensler was introduced to over 20 viable options ranging from Venice to downtown Los Angeles and ultimately chose the “jewel box” in downtown Los Angeles. The unique structure of the building allowed the firm to design creative office space unparalleled in the downtown marketplace. Gensler received a 3-year reprieve from the City of Los Angeles for gross receipts tax, which equaled more than \$1 million in savings. In addition, the landlord provided an above market \$75 dollar per sq. ft. tenant improvement allowance on core and shell and matched the estimated parking costs of West Los Angeles.



**525 S Flower Street**  
Downtown Los Angeles

**Date Completed**  
February 2011

**Landlord**  
Thomas Properties

**Quick Facts**  
47,162 SF Relocation

10-year and 15-year lease terms signed in the early 2000’s. In many cases, these companies either downsized their space needs while keeping the same staffing levels, or remained in the same amount of space with future plans to increase staffing levels.

**A GROWING TREND**

The trend toward a more efficient use of space is expected to gain further velocity in the foreseeable future in Los Angeles as the total volume of tenant lease expirations will increase by approximately 10% each year for the next three years. Many of these companies have engaged in their search for a more creative work environment, while the more strategic and forward-thinking companies have already made the transition.

In CBRE’s most recent “Tenants in the Market” report for West Los Angeles and Downtown Los Angeles, more than 35% of the combined 114 companies over 10,000 sq. ft. have expressed the desire to either locate in a pure creative office building or within an alternative creative space configuration in a traditional office building. These companies represent various industries, including media, entertainment, technology, advertising, apparel, furniture, architecture and construction.

With this shift in demand, the vacancy rate within buildings with existing creative build-out in core creative office markets remains tight, while the vacancy rate in traditional office buildings continues to stay elevated. This is especially true in Silicon Beach, which includes a

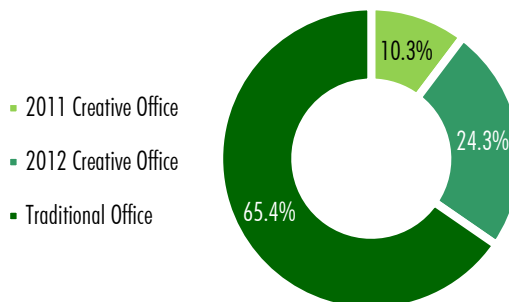
3-mile stretch from Santa Monica to Venice Beach and is home to hundreds of technology startups and incubators.

In Santa Monica for example, with elevated lease rates and a dwindling supply of vacant space, many users are expanding their geographies and looking to adjacent submarkets like Playa Vista, Culver City and Hollywood for their creative space needs. Playa Vista in particular has experienced increased demand as key occupiers with recently signed leases include YouTube, EA Sports and TMZ. Additionally, both Riot Games and Red Bull are actively looking to leave Santa Monica for new space in Playa Vista.

**RESHAPING DOWNTOWN**

Since 2011, many office tenants have started to convert cube environments within a traditional high-rise office building into an alternative creative office space configuration within a similar high-rise building.

**Figure 3: 2011-2012 DTLA Transactions**



Source: CBRE Research & Consulting, 2013.

In 2011, approximately 10% of the new direct Class A transactions in Downtown Los Angeles were these types of space conversions. This figure increased to 24% in 2012 and is expected to see further increases in 2013 as more tenants make the move to creative space.

There have already been a handful of occupiers who have transitioned to a more creative office environment in Downtown Los Angeles. In 2010, Gensler Architects relocated from Santa Monica and leased more than 37,000 sq. ft. in the Jewel Box building in the heart of the Central Business District. This signified the beginning of the creative office movement in Downtown Los Angeles and opened the door for others to follow.

The fashion and apparel design industry is a significant and growing creative office occupier in Los Angeles. In fact, the largest creative office user in Downtown, VF Contemporary Brands, recently relocated from Vernon to the Arts District in 2012 and is occupying approximately 82,000 sq. ft. in Alameda Square. They expressed the desire to create a fashion hub where technology, art, fashion and creative users come together. Additionally, NastyGal, an online vintage clothing store, grew organically during the past seven years from a very small studio in Northern California to 50,000 sq. ft. of creative office build-out in Downtown Los Angeles in 2011.

Emerging creative markets, like Downtown Los Angeles, are also in the early stages of redevelopment and adaptive reuse. Many landlords, especially in South Park and the Arts District, are openly discussing their plans to convert older and functionally obsolete office and industrial properties into a more creative environment, as the space is considered a more viable option for most of these properties.

### The Desmond

- 425 West 11th
- 78,000 sq. ft.
- Lincoln Property Group
- South Park District
- \$9 million renovation
- 2014 completion



A prime example of this is the conversion of the Desmond, located in the South Park district. Built in 1916, the building was once a large sales center for Willy's-Overland Motor Company before Desmond's Department store purchased the building and turned it into their Los Angeles warehouse. However, the building has long been vacant and now Lincoln Property Group is looking to capitalize on the growing demand for creative office space as they plan to convert the property into a mixed-use project with approximately 78,000 sq. ft. of creative office space, ground-floor retail and a rooftop bar.

### Alameda Square

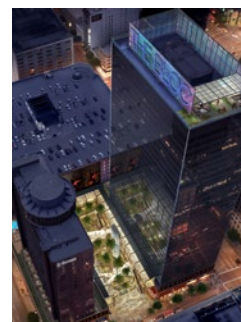
- 7th & Alameda
- 1.4 million sq. ft.
- EVOQ Properties
- Arts District
- \$78 million renovation
- 4 buildings on 32 acres



EVOQ Properties recently secured \$78 million in financing to renovate Alameda Square, one of Downtown's historical manufacturing and distribution centers. The campus is located in the Arts District and is comprised of four buildings totaling 1.4 million sq. ft. and includes creative office, retail and light manufacturing space. Their vision is to create Southern California's premier fashion apparel hub and to build a prominent creative office campus in Downtown Los Angeles.

### The Bloc

- 7th & Flower
- 1.8 million sq. ft.
- Ratkovich Company
- Financial District
- \$160 million renovation
- 2015 completion



The Bloc will be the largest renovation project in Downtown, with the conversion of the former Macy's Plaza, a 1.8 million sq. ft. mixed-use facility in the Financial District. The Ratkovich Company recently purchased the property and plans to begin a \$160

million renovation project to create a centerpiece for downtown retail and to develop a true live, work, play environment. They plan to reposition the 700,000 sq. ft. office tower into a dynamic creative office building in order to attract tenants interested in a more dynamic work environment.

### IMPACT ON REAL ESTATE

The demand for creative office space is also having a significant effect on the investment market as investors are recognizing the influence of creative office tenants and the value of the properties. These properties are generating higher lease rates, sometimes between 10% and 20% depending on the property, location and tenant mix – thus yielding higher value on a per sq. ft. basis.

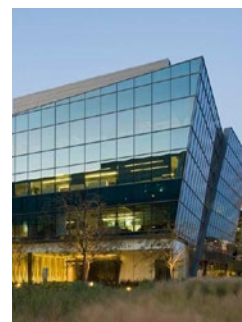
Overall, office market fundamentals are lukewarm across Los Angeles County with a Q1 2013 overall vacancy of 16.8% and relatively flat tenant demand. However, as you head west, the vacancy rates begin to decrease to 14.8% in the greater West Los Angeles submarket and 10.0% in Santa Monica. The primary reasons for stronger market fundamentals on the Westside include location, the make-up of tenants and creative office demand.

The Westside, especially Santa Monica and Playa Vista, is currently experiencing the highest levels of demand from both tenants and investors in Los Angeles. Many media, entertainment and technology firms are creating synergies due to the close proximity to one another. These companies are the predominant users of creative office space and current demand has helped solidify West Los Angeles as one of the more desirable markets on the West Coast for both occupier and investors.

According to transaction data collected by Real Capital Analytics, total sales volume in Los Angeles for the previous 12-month period ended Q1 2013 reached \$4.8 billion with an average price of approximately \$238 per sq. ft. Over that same time period, pricing on the Westside averaged more than \$400 per sq. ft. Recent trades for core creative office properties have been in excess of \$600 per sq. ft., illustrating the premium pricing for creative office buildings located within core creative markets like Santa Monica and Playa Vista.

### Campus at Playa Vista

- 12015-12045 Waterfront Dr
- 325,000 sq. ft.
- Hines Global REIT
- \$218 million
- \$671 per sq. ft.
- 4 buildings on 64 acres



The Campus at Playa Vista was an attractive purchase for Hines Global REIT due to the strong tenancy of tech companies, new construction and the expected long-term health of the West Los Angeles market. The property is approximately 97% leased and includes tenants: Belkin International, University of Southern California Institute for Creative Technology, ICANN and Facebook.

### Santa Monica Clock Tower

- 221-225 Santa Monica Blvd
- 54,000 sq. ft.
- Sorgente Group America
- \$34.3 million
- \$642 per sq. ft.
- 12 stories built in 1929



The Clock Tower is another example of Westside creative office space commanding premium rents and premium pricing. The creative office building is located at the epicenter of Silicon Beach and is one of the most well-known buildings in the region. Tenants include TrueCar, LivingSocial and Famigli Di Vendetta. Sorgente Group plans to conserve the cultural landmark and further insure the tower remains a prominent icon in Santa Monica.

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