

From the San Francisco Business Times:

<http://www.bizjournals.com/sanfrancisco/stories/2008/02/25/focus1.html>

Condos go shopping

Premium content from San Francisco Business Times - by Sara Wykes

Date: Sunday, February 24, 2008, 9:00pm PST

Richard and Janet Tarlov were veterans of the upscale food business when they wrote a business plan for the first grocery store of their very own. Seasoned at some of the country's top gourmet markets, including Dean & DeLuca and Balducci's in Manhattan and the [Oakville Grocery](#) in Napa, they had learned a thing or two -- especially about real estate.

"We knew from lots of experience at different stores over the years that the ultimate success of the business frequently depended on owning the property," said Richard Tarlov. "I've seen many have to pack it in before their ideal exit because of leases. You have plenty to worry about in this business aside from whether you're going to have a giant rent increase or the failure to add another option."

Traditionally, business owners wanting a hedge against exactly that sort of uncertainty bought a building. But commercial real estate prices make that nearly impossible for a small business owner just about anywhere in the Bay Area.

The Tarlovs did the next best thing -- something that many now see as actually a better thing -- they bought a retail condo.

The Tarlovs, who opened the Canyon Market in San Francisco's Glen Park neighborhood a year ago, have plenty of company.

The Bay Area's commercial real estate market is humming nicely with retail condo sales. It's a business choice that's appealed to developers and investment companies, too, in urban and suburban settings.

San Francisco's densely urban core offers special opportunities in parts of town where residential is making an appearance in the form of hundreds of luxury living spaces stacked in highrises, energizing dozens of moribund blocks into emerging neighborhoods. South Beach and Mission Bay are two hot spots where interest is intense.

Counter intuition

The evolution of retail condos is a bit illogical. The size of the spaces -- generally between 1,000 square feet and 5,000 square feet -- is best suited for independents, entrepreneurial sorts who might once have seen a mortgage as far too long a commitment, something that could render them stuck in a location that's not working out, with foreclosure as a possibility. But even for beginning ventures up against high failure rates, the allure of equity instead of money disappearing in rent can overcome all those fears.

What surprised Polaris' Chris Foley is "high net-worth people you would think are only ever going to buy (a building) ... are looking seriously at commercial condos because they couldn't buy the building where they wanted it to be."

Another retail condo buyer segment, said Erika Elliott of Cornish & Carey, is established retailers or commercial businesses with the wherewithal to buy "because they have to be in that space and there was no option to lease."

Cost benefit

The cost of borrowing is also proving influential. Interest rates are low -- and the Small Business Administration's 504 loan program a real boon. The 504 funding is designed for property acquisition and requires only 10 percent down. The SBA will loan a business up to \$2 million.

Nationwide, said SBA spokesman Bob Borden, 504 loans last year represented \$4 billion out of a total of \$20 billion for all SBA loans. "They've been on an upward trend," Borden said, "and are becoming a large part of our portfolio."

While most of the retail condo market's square footage is east of the Mississippi and heavily concentrated in New York City, one of the most successful projects in California is the 300,000 square feet of retail and wholesale condos that anchor one section of the Los Angeles Fashion District.

In the South Bay, Milpitas officials are glowing with a San Jose developer's plans for 135,000 square feet of retail condos on a 16.4-acre property at the prime intersection of Interstate 880 and Highway 237. Again, potential customers are right at hand. The development will also include 375 luxury residential condos.

Indeed, a big chunk of the retail condo market is showing up in projects that combine residential, office and retail and sometimes even public spaces.

Canyon Market is part of a three-story building that includes a public library on the second floor and offices on the third. San Francisco city officials see these sorts of blended functions as powerful community building. And it's hard to argue with the nearness of a customer base.

"The actual clients for the retailer are located right above or within a half block vicinity," said Catherine House at [CB Richard Ellis](#). "There is a lot of demand for vacant spaces."

Purchase prices for retail condos in the city are running around \$500 per square foot, she said. The demographics for the buyers of the new residential condos are also attractive -- lots of young couples without kids and downsized baby boomers who are clearly not living on fixed incomes.

Retail condo buyers, House said, represent a varied landscape -- restaurants, home decor, wine bars, coffee cafes and service business that include optometrists, dentists and spas.

Things to ponder

Business condos certainly come with their own set of potential problems -- just as with residential condos, retail condo owners are part of an owners association and must agree on marketing decisions, which might include who they allow to buy in the building and other provisions. But there are no laws for a neighbor's dog to soil and no one will complain about late night piano practicing.

Some developers and management companies are being as cautious as little old ladies crossing a busy street -- building in soundproofing, extra ventilation and thicker walls and flooring to buffer upstairs tenants from restaurants. One Florida mixed-use project, next to a busy port, is requiring that residents to agree not to sue over noise.