

Market Strategies: Plumbing the Depths of Micro Markets

“We never know the worth of water ‘til the well is dry.”
– English Proverb

By Patrick Duffy

During the recent housing boom, market feasibility studies were fairly simple to produce: gauge the price points and absorption of the closest competitors, compare against the local resale market, ensure there wasn't some unknown project about to start across the street and call the client with the good news. Even when builders or lenders wanted more in-depth analyses – such as data on countywide employment and demographic trends or local school quality information – the rising tide could easily paper over a few inconvenient details in favor of a green light.

Now those days are a fairly distant memory, replaced by what should have been requested all along – namely comprehensive feasibility studies which analyze not just the active and proposed competitors, but whether the entire pool of interested and qualified buyers within the immediate area is large enough to accommodate the latest entrant. To be useful, they must adequately answer the questions of who are these people, what do they want, what can they afford – whether to buy or to rent – and how can a builder motivate them to move?

Enter the ‘micro market’ analysis. Long used by other industries and larger homebuilders to comb through and target certain demo- and psychographic populations, until recently the focus on selling to a certain type of buyer *who also lives in a certain area* has been mostly the exclusive domain of your friendly neighborhood resale agent. You can toss out their calendars and notepads from your mailbox and smirk at their bus bench advertising all

you want, but when people decide to buy a home, they usually ask for a reference to a trusted advisor – and certainly someone who specializes in specific areas.

Today's market studies should be just as knowledgeable on the micro markets as the best local agent, yet at the same time provide an objectivity that can only come with a disinterested third party. Several times I've seen developers of mixed-use communities rely completely on the advice of commercial brokers for retail or office uses and only seek a third-party opinion for residential components, which can be quite problematic for lenders who may not buy into the unaudited argument that “everyone who's anyone will want to be a part of this really cool retail center!” At the same time, their expertise on specific micro markets can add both flavor and dimension to analyses that risk myopia from the unknowingly misinformed eye.

And of course there's the spectre of emotion – the kind that accompanies hopeful homebuyers falling in love with a specific list-

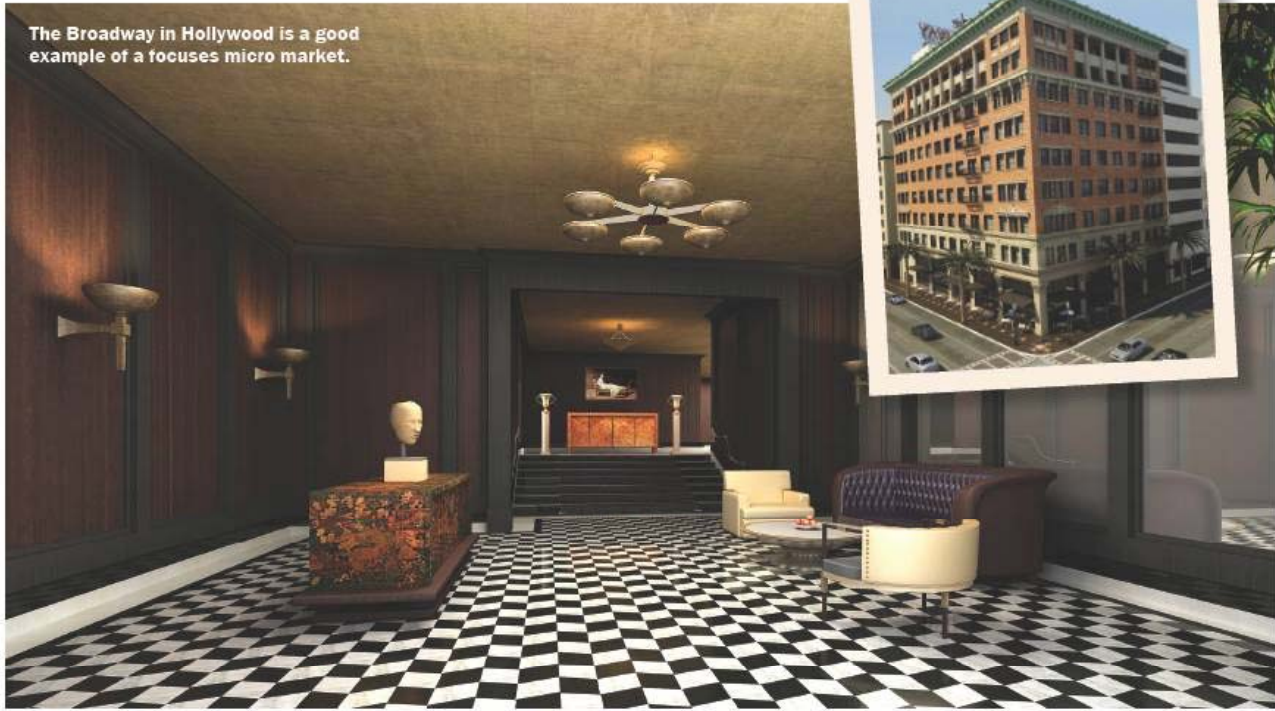
ing, and developers who are often no different with their own projects. A few months ago we received a call from a builder who wanted to price his new lofts in the San Fernando Valley at the same price for which he successfully sold similar units in a much more exclusive area of Los Angeles south of Hollywood near Hancock Park. When we tried to explain to him the importance of considering micro markets (especially for infill projects) – and that the two sites were completely different and would not get the same price – he steadfastly defended his position, claiming that the high ceilings, granite countertops and stainless steel appliance packages would somehow mask the view of the Hollywood Freeway just outside the windows, and that this project could compete not only with Hancock Park but also Hollywood and downtown Los Angeles. When we tried to explain – gently, this time – that adding in other micro markets to make a project pencil was both unethical and an almost-certain path to bankruptcy, he said he'd take his business elsewhere.



Photos courtesy of TCA

The Broadway in Hollywood is a good example of a focuses micro market.

Photos courtesy of KQR Development



The lofts, now under construction, are currently being offered for rent. More recently, our consulting group was asked by a developer to analyze the potential pricing and absorption for new condominiums and/or apartments that would be part of a large mixed-use residential and retail center called *Paseo Plaza* on the east end of a rapidly redeveloping Hollywood. While at first glance (and at first drive around the immediate neighborhood) it was challenging to picture a gleaming new center in this most transitory of neighborhoods off of Santa Monica Blvd. near the Hollywood Freeway. However, the same conclusions could have been drawn from a very successful downtown Hollywood or a sketchy Wilshire & Vermont intersection just a few years ago.

Due to fairly rapid absorption rates for the apartments and brand-name retail tenants (not to mention saving the venerable Schwab's Drug Store) at the mixed-use *Sunset & Vine*, when this four-acre parcel opened in 2004 it provided an immediate launching point for other redevelopment efforts in all four directions from that famous intersection. Thanks in part to its success, just up the street at Selma and Vine TCA Architects has completed its design for a two-acre, mixed-use project to

be constructed by the usually upscale apartment builder Camden Development (and which, suitably enough, will be anchored by a Whole Foods market). Over in Koreatown at the *Wilshire & Vermont Station Apartments*, the MTA worked with Urban Partners to leverage this Red Line subway stop into 450 units opening in 2007 that command rents more in line with Wilshire Blvd.'s Miracle Mile than the immediate neighborhood.

In other words, casting a net for a market study isn't just about geographic proximity; more than anything, it should center on analyzing similar developments in which potential buyers and renters are choosing to live. The fact is that pent-up demand for new housing alternatives in the huge swath of land extending from the Pacific Ocean to downtown Los Angeles and from Interstate 10 to the Hollywood Hills, made defining the micro market for *Paseo Plaza* a bit tricky, so input from local brokers was crucial. Consequently, by basing it more on demographics and future land use patterns than geography alone, the competitive net extended west and south of Hollywood to capture the type of resident willing to overlook a neighborhood not yet gentrifying but wanting the associated advan-

tages – such as mass transit, entertainment options, or a short commute – of urban living. Most importantly, with two distinct product lines chasing different buyer segments, nearly 400,000 square feet of planned retail space and plenty of security measures, such a large development will undoubtedly create its own ambience and jumpstart surrounding redevelopment efforts by virtue of its size alone – theories that have already been well documented in practice at both *Sunset & Vine* and *Wilshire & Vermont*.

After all, no one said micro markets and their developments had to be small – just *focused*.



Patrick Duffy is a Principal with Los Angeles-based *MetroIntelligence Real Estate Advisors* (www.metrointel.com) and authors the *Housing Chronicles* blog (www.housingchronicles.com). He can be reached at pduffy@metrointel.com.

