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Conversions Continue to Face Uphill Battle

- The potential for vacant office stock to become new housing has been a hot topic since early in the pandemic, when it first became clear that the relationship between the office and the worker would be forever altered. While conversions are now occurring in nearly every market, there is still a long way to go before they make a significant impact in the broader office and housing markets.
- These days, you don't need to look far to find an office being converted into housing. In Manhattan, the famed Flatiron building, which has been vacant since before the pandemic, will be converted into 40 luxury condos. Other major metros like Boston, Dallas, Washington, D.C., and Los Angeles have seen high levels of conversion activity, but conversions are underway in smaller metros, as well. In Charlotte, Duke Energy sold an 800,000-square-foot tower to MRP Realty, which will convert it into 450 apartments. In Milwaukee, developers purchased the struggling 100 East, a 35-story tower in downtown, with plans to convert it into 350 apartments.
- Many of the problems that have so far forestalled conversions remain prevalent. The large floor plates found in office towers present logistical challenges. The submarkets with the highest office vacancies are typically in CBDs, which lack access to necessities like grocery stores. Even a building perfectly suited for a conversion requires significant capital, meaning that interest rate increases and tight capital markets further limit the pool of opportunities. Unless the office sector sees unprecedented loss of value, conversions will require public support to thrive. The public sector can provide financing and incentives to help projects pencil out, and can also work with developers to smooth out issues like zoning and landmark preservation, a challenge for older properties such as the Flatiron Building.
- The White House made headlines recently by announcing a plan to help spur office conversions. While it is encouraging to see the highest levels of the federal government acknowledge the hurdles these projects face, the plan still comes up short on game-changing support from the public sector. The plan makes financing and other assistance available through a variety of sources—20 different programs across six agencies—but comes with no net new funding. There is potential for some programs to make a significant impact, like those offered by the Department of Transportation focused on transit-oriented development, but for now it is unclear how much impact the plan will have. Yardi Matrix will monitor the effect the plan has on conversions going forward.

