Challenges and Opportunities Facing the Future of our Cities

BY GEORGE T. VALLONE, CRE

I MET MY BUSINESS PARTNER DAN GANS IN 1972 when we were both freshman at Gettysburg College. One year after graduating, we decided to start a development business together. After studying the entire New York Metropolitan area for three years as we completed our post-graduate studies, we came to the conclusion that Hoboken would be the best place to start.

The selection criteria that we used in deciding where to start our redevelopment business mirrors the criteria that developers around the world consider in their site selection process. It's no secret that the primary driver of value in real estate is directly linked to location. Lifestyle and housing preference decisions follow a selection process which drives market demand. Consequently, understanding those market preferences leads directly to the highest value locations.

We elected to begin our career in the city of Hoboken, New Jersey. In our specific case we picked Hoboken because of its location on the Hudson River directly across from Manhattan Island in New York City, and it met all of our other selection criteria. It had a large inventory of 100 to 150 year-old, very well-built brownstones and brick row houses. These buildings were in disrepair and were available at very low prices due to the evaporation of middle class workers whose port related and manufacturing employers in these industries closed down and moved elsewhere. The middle class simply moved out leaving many homes for sale with few buyers. These buildings were well-suited for high-end renovation and sale as condominiums. Additionally, Hoboken and Jersey City were transit rich locations. They both had mass transit access to one of the largest employment centers in the country (New York City) via subway, bus and ferries. It also had automobile access into Midtown and downtown Manhattan through the Lincoln and Holland Tunnels. Both cities also had significant employment generators within their borders as they were home to several academic institutions, hospitals, and hundreds of small commercial, retail and dining and drinking establishments.

We purchased a four-story, brick row house as our first development project on Third Street in Hoboken in 1979. We picked it because the price was a very reasonable $20,000, it was two blocks from Washington Avenue (Hoboken's Main Street) and it was a five minute walk to the PATH transportation center. In one year, we completely renovated it and

About the Author

George T. Vallone, CRE, *is President of The Hoboken Brownstone Company (HBCo) — a multi-faceted real estate development firm active along New Jersey's Hudson River "Gold Coast." Mr. Vallone is President of the New Jersey Builder's Association (NJBA) and Chairmen of NJBA's Mixed-Use Developers Affiliate ("MXD"). The members of MXD are responsible for the construction of more than 75 percent of all rental housing built in N.J. For 10 years he served as President and Vice Chairman of the Board of Our House, Inc., a non-profit group that builds, owns and operates over 30 group homes and provides job training for 120 developmentally disabled adults and individuals with mental health, substance abuse and criminal backgrounds. He also served on the Board of YCS — Youth Counseling Services, Inc. — a $70M non-profit whose mission is to serve children at risk all over N.J.*

Mr. Vallone possesses a BA in Accounting from Gettysburg College and an MBA in International Finance from Fordham University. He has been a licensed N.J. Real Estate Broker and is a Counselor of Real Estate. He has guest lectured at NYU, MIT, and taught a Real Estate Finance and Risk Management course at the Rutgers Graduate School of Business, the N.J. Redevelopment Agency's Edison Institute, the Rutgers Cook College Continuing Education Series, and at the N.J. Bar Association's Institute for Continuing Legal Education. He also lectures extensively around the country on numerous real estate topics involving creative finance, joint venturing with land owners, structured seller financed land development, risk management, green building, and brownfield redevelopment topics.

converted it into four condominiums.

We sold the upper three units and kept the ground floor unit for the two of us to live in and for our first office. We continued with larger and larger projects including the construction of a 100 unit high-rise condominium in 1985 simultaneous with the restoration of an adjacent 1905 bank building which was listed on the National Historic Register, earning us a 25 percent tax credit which helped to shelter the condominiums profits.

To keep with large scale projects, we became involved with brownfield redevelopment on the Hoboken waterfront and downtown Jersey City. Brownfield redevelopment involves cleaning up contaminated industrial sites and repurposing them into mixed-use developments such as: multifamily, retail, parking and parks.

In the late 70s, 80s and 90s our condominium buyers were the "Baby Boomers," referred to back then as "Yuppies" — Young Upwardly-mobile Professionals, and their children, referred to as "Gen X." As the Boomers moved into their late 20s and early 30s they began forming families and many left our market in search of the suburban lifestyle: a single-family house with a yard, two-car garages and a swing set. A generation later, that same demand for the urban lifestyle is being driven by the Gen X and the Millennial generations. Further fueling demand for housing in redeveloping urban areas is the fact that over the last 10 years the middle aged Baby Boomers, who are en-mass becoming empty-nesters, are retiring and returning to the urban lifestyle of their Yuppie youth. Empty nesters are now combining with Gen X and the Millennials to fuel the demand for luxury rental apartments and condominiums on the New Jersey side of the Hudson River. The exact same housing trend is being seen energizing many older neighborhoods and industrial areas along the Brooklyn and Queens waterfronts on the East River side of Manhattan. Nationally, the Baby Boomers, Gen X and Millennials are a 215,000,000 strong market (67 percent of the 319 million U.S. population). The percentage of this market that prefers a place to live where job centers, culture, active and passive recreation, dining, drinking and shopping are all interwoven in pedestrian friendly neighborhoods that are accessible to regional mass transit is clearly up-trending. This mega-trend toward urban living is happening all over the United States and in many of the world's post-industrial waterfront cities.

While the demand for urban life is growing, urban brownfield redevelopment certainly has its many challenges and problems.

One of the major challenges of urban redevelopment results generally from problems caused by a policy clash between legislators passing unprioritized legislation which promotes well intended but conflicting objectives. An example of such conflicting objectives would be incentivizing urban redevelopment versus creating jobs for unionized construction workers. Both of these policies have a high priority which forces legislators to try and accomplish both and use legislation to connect them. In New Jersey, local financing subsidies like real estate tax abatements and PILOTS (Payments in Lieu of Taxes), which have the intention of fostering redevelopment of former industrial areas, typically come with a prevailing wage (union) requirement, thus diluting the beneficial impact of the incentive by about 30 percent to those who use it and sometimes discourage potential new entrants to the market. Similarly, New Jersey's Brownfield Reimbursement Program, whose objective is to incentivize the remediation and redevelopment of historically environmentally impacted industrial property, also comes with the prevailing wage requirement. By failing to prioritize policies and using legislation to attempt to accomplish conflicting objectives, you end up achieving less of both of the objectives.

Another significant challenge urban redevelopment faces is the availability of affordable workforce housing in up-and-coming neighborhoods. As redevelopment in our inner cities accelerates and existing property values escalate, the incentive for the private sector to preserve affordable housing diminishes.

Affordable housing policies often clash with redevelopment policy when the cost of building new affordable housing is placed on the development community without an offsetting compensating incentive like density bonuses, property tax relief or expedited approvals and permitting. Another challenge that is bias is often referred to as the "NIMBY" (Not In My Back Yard) mentality. This bias is well documented in suburban and rural communities: it is now beginning to show up in urban areas where residents of "high-end neighborhoods" do not want to preserve the existing affordable housing stock or admit new affordable housing into their midst because that will introduce a "bad element" of the population into their otherwise upscale neighborhoods.

Producing new affordable housing traditionally has only been accomplished through government incentives, like low-cost financing, vouchers (like the HUD Section 8 voucher program), and 4 percent and 9 percent Low Income Housing Tax Credits which are in short supply. Additionally, some become an annuitized and increasing burden on the private tax-paying sector over time.

Land use policies in America's oldest cities evolved over the last hundred and fifty years. Originally they were designed to be more and more restrictive in order to solve (control) the many major problems that became endemic in many of the northern cities, as their populations began to explode after the Civil War. The original well-intended purpose of land use laws was to reduce density to solve the horrific conditions in cities caused by overcrowding and the consequent problems of fires from unsafe construction practices, sanitation, crime, and the industrial pollution caused by the necessity of factories being located next to where people lived. For the most part, over the last 50 years, these health and safety conditions no longer exist. The solutions to these historic problems; however, have not caused a commensurate change in land use policy. Those now-outdated restrictions should be reduced and growth and densities encouraged in appropriate locations. With modern sewer, water and mass-transit systems in urban areas and the increasing deindustrialization of our cities as we move from a manufacturing to an information based economy; cities should be allowed to grow without these outdated restrictions. In fact, the most successful cities have their employment buildings in close proximity to where people live. Walkability to mass transit and jobs is the new amenity.

Exacerbating the problem of efficient land use in New Jersey is that zoning is done at the local rather than the municipal level. "Home rule," as the locals like to call it, has resulted in 537 municipalities each deciding how much and where they will allow growth to occur with absolutely no concern about the effect of this growth, or lack thereof, on neighboring municipalities or the regional economy. This bottom-up planning model creates an imbalance between the social benefit of growth and the private costs that growth sometimes imposes. The solution is top-down planning where long-term growth can be anticipated, future infrastructure requirements can be budgeted and planned for, and the creation of low density low-cost affordable housing and public open spaces can be balanced and offset by high-density high-cost housing. Resistance to top-down planning is also often exacerbated by urban landowners attempting to preserve local zoning power to artificially inflate the value of their assets by restricting the supply of additional product on the market.

Rebuilding infrastructure is another challenge facing our older urban areas. Although much of the infrastructure that exists was capable of handling much larger populations from the peak industrial levels of our past, the infrastructure is aged. We still discover wood and brick sewers when we open up the streets for water, sewer and power connections, and we still have combined stormwater and sanitary flows running through the same pipes in most of our older cities. During recent severe storm events, most municipal sewage treatment facilities were overwhelmed by the surge of storm water which had nowhere to go so it backed up onto the streets causing widespread flooding. Major portions of Hoboken and downtown Jersey City were under four to five feet of water that caused hundreds of millions of dollars in property damage.

These combined systems are in need of redesign, separation and rebuilding. Financing the rebuilding of our infrastructure can be a very simple matter if the cities are willing to accept taller buildings and increased densities. By making additional density in taller buildings available in redevelopment areas for a price, infrastructure funding can be created quite literally from thin air. One of the density bonus plans we worked on in Jersey City, N.J., would have allowed 40+ story buildings instead of the 20 story buildings currently permitted and would have added 2,000 additional units to a neighborhood which, at an average market price for land per residential unit of $50,000, woulld have generated $100 million which could have been used for public purposes like infrastructure financing, affordable housing, open space, and mass transit improvements. Solutions like these exist but require political leadership.

Notwithstanding these challenges, there are far greater opportunities in redeveloping post-industrial cities like Hoboken and Jersey City.

Most of the local political and bureaucratic officials we deal with have a pro-development attitude. Developers who know how to work together with the community stakeholder groups and the city are in great demand. They know that working together during the planning process ensures faster approvals and projects that result in more profitability for the developer and more benefits for the host community. There are a significant number of large tracts of river front and river view property, originally all exclusively occupied by industry that became vacant and available for redevelopment. Active railroad right-of-ways that traversed and connected the cities from their waterfront factories and warehouses to their markets inland are now used by passenger rail. Sixteen years ago, New Jersey Transit invested $1.5 billion into the Hudson Bergen Light Rail Train (HBLRT) using the newer and less expensive light rail technologies. The HBLRT's 23 station stops running along 34 miles of the New Jersey Hudson River waterfront provide easy access for 54,000 people per day commuting up and down the Hudson River waterfront to local employment centers and for connecting to the ferry and PATH subway systems into Manhattan.[1] As a result of that infrastructure investment, private developers have constructed approximately $30 billion of private investment surrounding these station stops.

Another opportunity exists because of inactive and abandoned railroad right-of-ways being converted to linear parks that also function as pedestrian walkways and bike paths; i.e., "Rails to Trails." Rails to Trails projects like Manhattan's 1.5 mile long "High Line" have proven the popularity of these walkways and demonstrated the value-add benefits to adjacent property owners who now have high foot-traffic retail space on their upper floors which align with and have frontage along this linear park. On a larger scale, the "East Coast Greenway" is planned and sections are getting built that will ultimately take hikers and bikers on a 3,000 mile path along abandoned and repurposed railroad right of ways stretching all the way from Calais, Maine, on the Canadian border to Key West, Florida.[2]

In the very near future, we will begin to see a reduction in the traffic congestion in urban areas. This has long been an excuse to prevent more development. Already, disruptive transportation technologies like Uber, Lyft, Zipcars and Citi Bikes are dramatically reducing the need to own an automobile in urban areas. In the near future, driverless cars will take over our urban roadways. You will be able to order a car which will pick you up at your doorstep, take you to your destination, then come back and pick you up when you're finished and return you to your point of origin. No one will need to own a car anymore. This is why the big three automakers are paying very close attention to the Teslas and the Google self-propelled automobiles that are on the verge of widespread adoption. You can see a telltale sign of that attention as GM recently invested $500 million in Uber's competitor Lyft.[3] Parking lot and car-garage owners and automobile insurance companies will feel this disruption first. Parking lot and car-garage owners, whose facilities are typically located near employment centers or near transit portals to employment centers will be able to convert them to housing and greatly increase their value but the automobile insurance companies will not fare as well.

Our experience over 37 years of urban redevelopment has convinced us that although the challenges are great, the opportunities are even greater. The development community has always been vigilant in tracking demographic changes and their implications on the site selection process. Forward thinking developers realize the way to create successful developments is by focusing on the triple bottom line: societal, environmental and economic. In our role as real estate professionals, it is incumbent on us to continue to educate all of the disparate stakeholders within the legislative, policymaking, regulatory and development communities on the importance of harmony. By working together with our legislators to address the challenges of prioritizing redevelopment policy we can focus the power of public land use controls and incentives to create private sector financing for affordable housing, to rebuild our aging infrastructure, and to provide the necessary amenities for a quality urban lifestyle. Only though this type of political awareness and redirection will we create the best cities of the future. ■

ENDNOTES

1. See: *www.nytransit.com.*
2. See: *www.greenway.org.*
3. See: *https://www.bloomberg.com/news/articles/2016-01-04/gm-invests-500-million-in-lyft-to-bolster-alliance-against-ube*r. Accessed March 2, 2017.