INTRODUCTION:
SMART INVESTMENT, SUSTAINABLE RETURNS

Since California gained statehood in the late 1800s, Los Angeles (LA) has grown rapidly into the United States’ second largest city and one of the world’s most populous metropolitan areas. In recent years, it has continued to evolve and redefine itself as truly global destination, fueled in large part by the on-going growth of its major industries and investment portals: film, technology, infrastructure and tourism.

Situated on a coastal plain in the warm climate of Southern California, Los Angeles is a sprawling metropolis with a multicultural and young population representative of demographic trends occurring across the US. Indicative of its diversity, Los Angeles County has the largest Latino population in the nation, and nearly 40% of the city’s residents were born outside the US.

The city’s economy has been on an upward trajectory for the last five to seven years, which has resulted in significant increases in residential and commercial property values, both for sale and rental. Last year, median home prices in Los Angeles surpassed 2007 to 2008 pre-recession highs, and they continue to rise at a rate of 5% to 10% every year.

Numerous multibillion-dollar landmark developments are underway across the city, including the Korean Airlines Building, the Waldorf Astoria Beverly Hills Hotel, the expansion of the Purple and Expo Metro lines, the LA Rams football stadium, and the University of Southern California’s University Village. Construction over the next three to four years does not show signs of slowing. Furthermore, if LA—currently a final candidate for the 2024 Olympics—is selected as the host city, construction and real estate activity could potentially catapult to even higher levels.

Despite strong economic drivers and a prosperous real estate development market, LA poses several challenges and risks to investors. For example, even the large investments in infrastructure and transportation have not resolved all of LA’s gridlock traffic issues, and the city’s freeways remain the most congested in the country. These impairments pose logistical concerns for new construction and also place a premium on investment locations accessible to targeted clientele and user groups. Additionally, the project approval and building process can be a complex endeavor for even the most seasoned veteran. To address these challenges, in addition to many others, prospective developers and investors need to be equipped with local knowledge and experience to avoid exposure to artificially inflated market conditions.

Arcadis has compiled the following guide to investing in Los Angeles. Our goal is to provide an overview of the city’s investment landscape, offer insight for investors new and old, and identify the key opportunities and challenges to generating returns.
Whether you’re considering investing in LA for the first time or are a seasoned expert looking to achieve greater value from your investments, think of Arcadis as your guide. We know how to deliver remarkable outcomes from investment in built assets.

READ ON IF YOU’RE WONDERING…

HOW DOES THE LAND MARKET WORK?

WHAT ARE THE OPTIONS FOR LAND USE?

HOW DOES THE PLANNING PROCESS WORK?
WHAT ARE THE MAJOR DEVELOPMENT COST DRIVERS?

HOW SHOULD WE SELECT A PROJECT TEAM?

WHAT ARE THE MAIN RISKS ASSOCIATED WITH DEVELOPMENT IN LA?
POLITICS:

- Property taxes and other administrative fees and fines fund the majority of the LA city budget.

- The outcome of the presidential election of November 2016 is impacting LA’s city government. The mayor is focused on protecting city residents and securing Federal funding for infrastructure projects as well as homelessness, green space, climate change and education programs. Current LA government staff are working with the new administration to discuss the path forward.

- The city is composed of 15 city districts, each with a single member City Council representative. A centralized Planning Department is responsible for zoning, master planning and special use permits across the city.

- LA maintains a long-term plan through the year 2035, which includes an overall city plan and 35 specific area plans.

- LA has a large amount of federal, state, and local public capital directed towards transit and infrastructure improvements, such as roads, light rail, sidewalks and waterway adjacent upgrades.
ECONOMIC:

- LA is the second largest city in the US with nearly four million residents and is part of the larger Los Angeles County area with a population of more than 10 million. It is second only to New York City in terms of total contributions to GDP (approximately $800 million in 2014).
- The municipality has a projected total budget of nearly $9 billion for 2016 to 2017, a large portion of which is dedicated to capital projects and transit upgrades.
- Los Angeles County is an economic hub for the US. It is home to the largest workforce (4.6 million) in the country and also has the largest county economy in the nation ($640 billion). More than 244,000 businesses are located in Los Angeles County, and the city is home to six companies on the Fortune 500 listing.
- LA is also the largest customs district in the US. Over 40% of all waterborne goods entering and exiting the country pass through the Port of Los Angeles located south of Los Angeles Downtown. Each day, more than $1 billion in cargo comes through the port, which is the largest American port in terms of volume and 18th in the world.
- Los Angeles Airport (LAX), which serves as a gateway to Asia, Latin America and Europe, is located within LA and is the seventh busiest airport in the world based on passenger traffic.
- Los Angeles City and County maintain a diverse and robust business economy. Leading sectors include Logistics & Trade, Biotech/Health Sciences, Creative, Tech, and Manufacturing. LA is considered a world leader for the entertainment industry, fashion, clean tech and aerospace.
- Los Angeles County is the largest manufacturing center in the US. It is home to the largest workforce in the US, particularly for trade workers, engineers, and PhDs.
- Los Angeles County is the leading American county for foreign direct investment by Foreign Owned Enterprises.
SOCIAL:

- LA is one of the most diverse cities in the US. Nearly 40% of residents were born outside the US. People of Hispanic and Asian descent together make up more than half of all residents. The city is often considered the 21st century American city because of its diversity and rich multicultural heritage.

- LA is home to two of the world’s top universities (UCLA and USC) and there are more than 100 colleges and universities in Los Angeles County, including top ranking California Institute of Technology (Caltech).

- LA is a top tourist destination for the US and the world. In 2015, it achieved a record level of tourism at more than 45 million visitors for the year.

- Tourists account for an estimated $20 billion in direct spend for the city’s economy.

- LA is the lead American candidate for the 2024 Olympic Games and is making a significant investment to secure the event.

- LA is widely considered the entertainment capital of the world and is recognized for its celebrity residents, professional sports teams (Lakers, Clippers, Dodgers and newly acquired Rams) dining and nightlife.

TECHNOLOGY:

- LA has emerged in the last few years as a world hub for the technology sector. The western part of the city is densely populated with tech firms and is commonly known as Silicon Beach.

- LA is a leader in the clean technology sector and lays claim to numerous innovative companies making advancements in alternative power sources, sustainable material design and manufacturing, and water treatment.

- The aerospace and defense industries in LA have been a cornerstone of the city and country’s economy over the last half-century. In addition to traditional firms like Lockheed and Northrup Grumman, startup firms like SpaceX and Virgin Galactic have recently established a strong presence in the area and are advancing industry technologies at a rapid rate.

- An initiative called “CityLinkLA” is currently running parallel to Google’s Fiber upgrade initiative for the city and will bring gigabit speed internet access to all of LA.

- Two sectors highlighted for growth in the city’s long-term plans are technology and creative, which are supported by tax incentives and funding of support services.
LEGAL:

- LA maintains a mature and clearly structured legal system that provides equal coverage and accessibility for foreign and domestic parties. Because of these traits, the legal system is an appealing environment to investors who want to limit the legal risk exposure for their investments.
- The majority of businesses require a Business Tax Registration Certificate, provided by the Office of Finance. Certain operations also require a special use permit, such as food services.
- Companies are eligible to obtain a variety of corporate ownership structures, such as Limited Liability Corporation, S Corporations, C Corporations, etc. Each structure offers specific tax and management implications.

ENVIRONMENT:

- In April 2015, LA released its first sustainable city plan, called pLAn, which provides a roadmap for economic, environmental, and physical transformation through 2035. Focus initiatives include increased water conservation, the promotion of energy efficiency and solar energy, and plans to address LA’s housing shortage.
- The UCLA Institute for Environment and Science rated LA’s overall environment as a C+ because of water shortages, air pollution and ecosystem health.
- Because the city has suffered a regional drought over the past two years, it encourages water sustainability as a significant design consideration for new developments.
• LA is making significant progress toward improving its environmental health. It has become the leading American city for installed solar power; it has the highest recycling rate of any large American city; it is projecting to add more green jobs than any other American city by 2017; and it is committed to being the first large American city to achieve zero waste by 2025.

• LA Mayor Eric Garcetti co-created a Mayor’s National Climate Action Agenda as a leading force in implementing climate change policy.

• Currently, the largest infrastructure program in the US is underway to address the city’s infrastructure and transit issues. The program includes a massive expansion of the Los Angeles Metro, which will include the first metro line to connect downtown LA with the city’s western beaches.
### Figure 1: City Comparison

<table>
<thead>
<tr>
<th>INDICATOR</th>
<th>LOS ANGELES</th>
<th>NEW YORK</th>
<th>DUBAI</th>
<th>SHANGHAI</th>
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<tbody>
<tr>
<td><strong>GDP growth</strong></td>
<td>3.3%</td>
<td>1.9%</td>
<td>4.5%</td>
<td>6.7%</td>
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<tr>
<td><strong>Population (2014)</strong></td>
<td>13m</td>
<td>18m</td>
<td>2.5m</td>
<td>24m (end 2015)</td>
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<tr>
<td><strong>GDP/capita</strong></td>
<td>$69,692</td>
<td>$89,611</td>
<td>$32,800</td>
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<td><strong>City size</strong></td>
<td>1,302km²</td>
<td>789 km²</td>
<td>4,114 km²</td>
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<tr>
<td><strong>Population density</strong></td>
<td>3,198/km²</td>
<td>27,812/km²</td>
<td>408/km²</td>
<td>3,410 /km²</td>
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<tr>
<td><strong>Unemployment</strong></td>
<td>7.5%</td>
<td>6.1%</td>
<td>0.3%</td>
<td>4.2%</td>
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*Greater Los Angeles area*
<table>
<thead>
<tr>
<th>CRITERIA</th>
<th>INDICATOR</th>
<th>LOS ANGELES</th>
<th>COMPARISON CITIES</th>
</tr>
</thead>
<tbody>
<tr>
<td>Competitiveness</td>
<td>Power City Index (Mori Memorial Foundation)</td>
<td>14&lt;sup&gt;th&lt;/sup&gt;</td>
<td>Dubai n/a New York 2&lt;sup&gt;nd&lt;/sup&gt; Shanghai 17&lt;sup&gt;th&lt;/sup&gt;</td>
</tr>
<tr>
<td>Financial Power</td>
<td>Financial Centres index (Z/Yen)</td>
<td>29&lt;sup&gt;th&lt;/sup&gt;</td>
<td>Dubai 13&lt;sup&gt;th&lt;/sup&gt; New York 2&lt;sup&gt;nd&lt;/sup&gt; Shanghai 16&lt;sup&gt;th&lt;/sup&gt;</td>
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<tr>
<td>Global Engagement</td>
<td>Global Cities Index (AT Kearney)</td>
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<td>Dubai 28&lt;sup&gt;th&lt;/sup&gt; New York 2&lt;sup&gt;nd&lt;/sup&gt; Shanghai 20&lt;sup&gt;th&lt;/sup&gt;</td>
</tr>
<tr>
<td>Sustainability</td>
<td>Sustainable Cities Index (Arcadis)</td>
<td>50/100</td>
<td>Dubai 52/100 New York 26/100 Shanghai 74/100</td>
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<tr>
<td>Real Estate</td>
<td>Jll Global 300 Commercial Attraction Index</td>
<td>5&lt;sup&gt;th&lt;/sup&gt;</td>
<td>Dubai 33&lt;sup&gt;rd&lt;/sup&gt; New York 2&lt;sup&gt;nd&lt;/sup&gt; Shanghai 8&lt;sup&gt;th&lt;/sup&gt;</td>
</tr>
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<td>Tourism</td>
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<td>Dubai 9&lt;sup&gt;th&lt;/sup&gt; New York 2&lt;sup&gt;nd&lt;/sup&gt; Shanghai n/a</td>
</tr>
</tbody>
</table>

*refer to inside back cover for source, definitions and notes.
MARKET DYNAMICS:

LOS ANGELES MARKET DYNAMICS

LA’s property market has been in an upward cycle for nearly seven years. Prices are reaching record highs for the US, including a median home price of nearly $700,000 and an average cost per square foot of $553. The average cost per square foot increased nearly 10% from May of 2015, a particularly robust growth year, to May of 2016.

Property values have more than doubled for residential units over the past five years. Like New York and San Francisco, LA has experienced significant growth driven in large part by the technology sector. This has contributed to the success of high-end developers, who look for notable projects with record-setting sales prices to take advantage of the luxury real estate market.

As of June 2016, the median rent for a two-bedroom property in LA surpassed $3,000. This represents record highs for the market and places LA among the top five highest priced rental markets in the US.

While the volume of residential sales has been slowing since June 2016 (down 30% from last year), foreclosures are close to an all-time low, and vacant properties only account for about 7% of all homes. Some areas, such as the western portions of the city, are highly sought after and offer minimal supply, which causes quick sales cycles and increasing values.

These neighborhoods are receiving additional boosts from infrastructure investments such as the Metro expansions, which will improve residents’ commutes across the city.

In addition to the residential sector growth, commercial and retail lease rates have been on an upward trend since the last recession. Yearly increases have been 2% to 5% for lease rates over the past few years. Another indicator of the hot property market in LA for commercial space is the city’s rising hotel rates. The average hotel price per night in LA is nearly $200—a 10% increase from the last year.
Average residential housing prices have increased over 7% over the past year.
**MARKET DYNAMICS:**

**WHAT YOU NEED TO KNOW**

**MARKET:**

- LA is a relatively fast-growing city; in 2015 its population grew by 1.3%, which equated to nearly 50,000 new people moving into the city. Much of the city’s recent growth can be attributed to a younger demographic enticed by the urban environment.

- LA has benefitted from record amounts of foreign investment entering the city. In 2015, China invested over $15 billion into the LA market and with over $5 billion invested by March, is on pace to surpass that amount in 2016.

- In recent years, the primary focus areas for foreign investors in LA have been telecoms, technology, and real estate.

- Despite a vibrant construction sector, a strong surplus of skilled trade workers maintains a stable market for construction costs.

- LA’s construction labor force is organized within trade unions that must be utilized on the majority of construction projects.

- LA’s ports provide direct access to materials and products necessary for construction (without the added transportation costs associated with cross-continental shipment after port entry).

- Construction prices are competitive and market conditions are stable, enabling construction clients to secure good value. Investors can also count on commitment from the local government and its partners when initiating projects.

- After a period of urban blight from the 1970s to the mid-2000s, LA is currently redeveloping its downtown district. It is rapidly changing into a vibrant city center with a mix of large-scale construction projects, high-density residential, and the repurposing of industrial space to commercial and mixed-use space.
RESIDENTIAL:

- Housing prices in LA rose approximately 7% from June 2015 to June 2016, and rents have risen approximately 4% for that same period.
- LA has some of the highest housing prices and rents in the US, after San Francisco and New York.
- There are more than 1.4 million housing units in LA, and nearly 60% are occupied by renters.
- In 2015, 81,000 homes were sold in Los Angeles County. For comparison, 2003 represented the record high year for the county at 125,000 home sales. Since the recession of 2007 to 2008, sales volume has hovered around 70,000 to 80,000 per year.
- For the past three years, nearly all sub-sectors of the housing market, including single family, multifamily and apartment, have experienced growth.
- Because of the housing shortage in prime areas of LA, increased competition often results in multiple offers on a single property.
- Los Angeles County is home to more than 40,000 college students living in campus housing with an upward trend projected for the future. Areas near major university campuses experience lower vacancy rates and higher rents when compared with the overall market.

OFFICES:

- Rental rates for offices have increased 5% over the past year, an average cost of $2.92 GSF per month.
- In 2016, the office vacancy rate in LA is around 14%, which represents a reduction of 1% from the same time last year.
- The market maintains a strong net absorption of available space (nearly double the 10-year average). The West Los Angeles area accounts for most of this figure.
- In 2016, over 2.3 million square feet of office space is under construction in the Greater Los Angeles area. Hollywood accounts for more than 25% of that figure and is the leading area for new office construction in the market.
- As demand for modern office accommodation increases, LA is experiencing an over-supply of office space. High vacancy rates mainly affect older commercial properties located outside of core office locations.
- In the past year, mega commercial transactions occurred in almost every submarket. The largest transaction occurred in Downtown Los Angeles with the sale of a $313.6 million office building to a Germany-based investment fund. The property traded for approximately $450 per square foot.
- Office demand is projected to increase over the next year, which will reduce vacancy rates. Market sales professionals project that lease rates will expand by 2.4% by mid 2017.
RETAIL AND HOSPITALITY:

- The LA retail market is experiencing one of the highest positive absorption levels of the major American markets.
- The area’s vacancy rate for retail dipped to 4.5% in 2016. The asking rental rate was up to $2.26 per square foot (triple net lease: lessee pays taxes, insurances, and maintenance).
- In the Los Angeles Basin, a total of 1.28 million square feet of retail is currently under construction. Many notable fashion retailers are picking up iconic properties in the Melrose and Hollywood areas.
- The Greater Los Angeles Area (including Los Angeles County, Ventura County and Orange County) is composed of 472 million square feet of multi-tenant shopping centers and single tenant properties. It is the leading region in the US for retail.
- The LA market attracts a mix of high-end and affordable retailers due to a diverse market with mixed product demands. High median incomes and a growing population make the areas ideal for retailers.

INDUSTRIAL AND LOGISTICS:

- Strong market demand over the past few years has led to an all-time low industrial property vacancy rate of 1.1%–the result of a .5% reduction in 2016.
- The year-over-year increase on lease rates (Q2 2015 to Q2 2016) is 7.5%, bringing the average asking lease rate to $0.72 square feet at the end of Q2 2016.
- Limited supply and continued demand is driving the long-term rise in industrial rents.
- Development activity in the Greater Los Angeles Area has increased over the past two years, and 39% of projects in the construction pipeline are pre-leased.
- With supply levels at historic lows across the region, Class A buildings and buildings with high clear heights remain in demand. As a result, prospective tenants have shown increased interest in Class B product, which has in turn led to upward pressure on rents and further-restricted supply.

The Greater Los Angeles Area has attracted the highest volume of retail space in the US due to a strong consumer market and diverse product appetite.

Industrial vacancy is near 1% for the LA region.
Recent upward market trends have returned generous gains for investors and developers, but the market still poses significant challenges to those looking to invest. Navigating LA’s politics, regulations, and market conditions requires a keen understanding of local drivers.

Because it is an appealing target market internationally, LA is on the receiving end of numerous billion-dollar development projects sponsored by foreign investment groups and companies. China, Europe, and the Middle East are all heavily active in the market. Although new construction (greenfield) is well balanced with investment into existing properties, the state of California has the highest number of foreign greenfield projects in the US.
Construction Management firms are widely used in the market and can serve in an “agent” or “at-risk” capacity.
INVESTORS/DEVELOPERS:

- A variety of commercial and residential developers are active in the market, ranging from Real Estate Investments Trusts (REITs) to private equity players and joint venture partners. The region’s principal investors are regional investment firms that have accumulated funds targeting the market.

- Historically, LA’s commercial market has been dominated by regional firms. Since 2005, the top commercial developers by square feet have nearly all been based in Southern California. Watson Land Co., based in Carson, California, has been the leading developer over the past decade with more than 22 million square feet of developed real estate. The regional trend is rapidly eroding, however, as some of the world’s largest developers, like China’s Wanda Group and Gemdale Corporation, have moved into the market.

- Local companies, such as the Irvine Company, have largely dominated the residential sector; however, Greenland USA (the American arm of a Chinese development company) currently is setting records with one of the largest mixed-use projects in US.

- Joint ventures and public-private partnerships have become more prevalent in recent years, particularly as the size and complexity of projects increase.

CONTRACTORS:

- LA is home to operating bases for a mix of firms, including local contractors, large American firms, and international engineer procure construct (EPC) firms. Notable companies with local presence include Turner Construction, Clark Construction, Tutor Perini, and Skanska USA.

- Los Angeles County is the headquarters location for some of the world’s largest EPC firms, including: Parsons Corporation, AECOM (and formerly URS), Fluor Corporation (formerly headquartered in Santa Ana).

- Due to the growing number of large infrastructure and commercial projects in the region, various international construction and engineering firms have increased market presence over the past few years.

- Most contracting firms have rebounded post-recession and are achieving profit margins on par or in excess of the pre-2007 levels. Generally speaking, local contractors have an optimistic outlook for the future and a strong backlog of secured projects for the next few years.

- Subcontractors are increasingly working in direct connection with owners, rather than through general contractors. Due to alternative delivery structures, such as alliance and integrated project delivery, owners are finding advantages in procuring subcontractor services directly.
CONSULTANTS:

• Owners typically engage a construction consultant (i.e. construction manager or project manager) for projects that involve multiple disciplines and team coordination. Project managers have overall responsibility to the owner for all aspects of the project, including design, construction and closeout. Although the terms “project manager” and “construction manager” are sometimes used synonymously, project managers are technically defined as having management responsibility for the entire project’s success, while construction managers are only responsible for construction-related activities.

• The contract structure of project managers and construction managers will define the level of risk and exposure that an owner maintains. If these services contract directly with other trades and services, then they typically hold the project risk. If these services are only acting as advisors to the owner, then the owner typically retains the risk.

• Architects generally are responsible for leading the overall concept planning and design, as well as city planning and permit approval. They can coordinate directly with specialty subcontractors for the detailed and technical design work. In LA, general contractors are responsible for actually pulling the construction permit and leading discussions with the city agencies for any post-approval changes supported by the architect. Detailed design work is typically performed in-house by an architect’s staff engineers or would be subcontracted to a specialty engineering firm if in-depth technical expertise is required.

• Structural and building services engineers work closely with the architect but are procured directly by the client in some cases.

• A contract manager is often engaged on larger projects. They are responsible for identifying commercial, contractual and legal risks during the execution of a contract; monitoring the contractual agreements; and supporting the project team to develop contractual awareness. Most project and construction management firms have contract managers on staff. Some owners prefer an internal or independent contract management function to limit potential conflicts. Contract managers often report directly to a project or construction manager because they are a performing function that contributes to the overall scope.

• Asset and program management firms are often engaged by entities with large capital project portfolios. These firms are established as an outsourced extension of the organization to manage facilities, deliver projects, and oversee the construction and real estate portfolio. Typically, these firms have a deep pool of talent in the construction, engineering and facilities industries that the owner would struggle to recruit and hire directly.

Contractor margins have returned to pre-recession levels; however, components of profit are often tied to measurable performance bonuses to encourage behaviors.
PROCUREMENT CONSIDERATIONS:

- In LA, the two most common contracting strategies are design-bid-build and design-build. In the former, the owner procures design and construction services separately; in the latter, a single firm is responsible for both.

- The use of a construction manager is prevalent in the US construction industry, thus reducing some of the benefits of the design-build model. Construction managers are still used for the delivery of design-build projects but their scope of services is reduced to align with the internal coordination of the design-build entity.

- Although design-bid-build is still the most prevalent delivery strategy, owners are more willing to explore alternative structures like design-build or alliance.

- Construction management services can either be procured in an at-risk or agent capacity. At-risk construction managers will directly hold the contracts for general contractors and other vendors. Agent construction managers will be directly contracted to the owner but not directly to any of the other involved parties.

- For industrial and infrastructure projects, design-build is often preferred due to the technical complexity of the works and the need to gain efficiencies in schedule and coordination. The model enables efficiencies by linking design and construction under one firm.

- Increasingly, LA’s building projects are employing digital information models. Within integrated contracts, systems engineering is used to verify the client’s requirements during the design and construction of the project. Additionally, BIM (Building Information Modeling) is used to develop the design in more detail and to monitor the work, including deviations.
CONTRACT MODELS:

In the past two decades, alternative contract models have been developed to achieve greater efficiencies on projects. These models differ from one another largely in terms of the extent of influence the client can exercise over a project and the liability that is linked to that influence.

The three primary models currently available for use in the building sector include: the traditional model (design-bid-build); the construction manager model; the design-build (or engineer-procure-construct) model. Of these, the traditional model and construction manager model are the most commonly used.

1. The traditional model

Within the traditional model, the owner procures an architect and a general contractor. The architect designs and engineers the project, and when the design is complete, a contractor carries out the design. Both parties are directly contracted to the owner.

2. The construction manager model

The owner procures a construction manager to oversee both design and construction of a project. The construction manager either directly contracts these parties (in the at-risk model) or oversees contracts held by the owners (in the agent model). Both models add a layer of fiduciary control and management to the project.

All contract models have their own conditions with specific roles and liabilities for all involved parties. Contracts can be tailor-made, and clients have the opportunity to add specific preferences or conditions to their contracts, if desired.
Undertaking development activities in LA often requires an interface with city and state agencies, regulations and requirements due to the location and nature of the land. Adding additional complexity is the state of many available development opportunities, which involves the conversion of industrial or blighted sites to either commercial or residential use. These sites present numerous environmental challenges for owners, because they must bring the sites up to an acceptable standard per the US Environmental Protection Agency (EPA). Furthermore, sites in close proximity to the Pacific Ocean are often governed by Coastal Commission Board, as well as the City Government.

Typically, LA is favorable towards development, particularly in cases where there is the potential for high-density urban infill. LA aims to add 150,000 new houses by 2025 through the approval of these highly dense and transit-oriented developments under the pLAN initiative.
LAND CONSIDERATIONS:

- Most developments in LA take place on previously developed sites, which can create problems associated with existing structures and contamination. Many creative and tech companies seek to reuse existing buildings, rather than tear down and build new. Undeveloped greenfield land is extremely rare within the city proper. Since LA is well developed, utility and infrastructure accessibility to sites is not typically a concern.

- Available land is scarce in prime LA locations near to beaches, downtown or along transit routes. For this reason, land prices have been rapidly increasing over the past four to five years.

- By limiting changes to a building’s footprint and façade, developers can circumvent historical preservation requirements and city architect approvals.

- Developments aimed at providing a mixed-use function are often favored by the city, particularly if the development can convert a portion of the property into a public use function, like a park.

- Developers often like to use the city zoning and permitting to achieve increased densities or alternative designation for their parcels (i.e. residential or commercial instead of industrial) to achieve their project goals.

- Developments located within one of the city’s master plans receive quicker reviews and approvals because they are based on the city’s long-term vision for the area.

- To incentivize high profile businesses and developments, the city can serve as a partner to developers in numerous ways, including easing zoning restrictions, donating land for the development and providing tax incentives to the end user.

- For the development of large industrial, logistics or commercial sites, the city is stricter in their enforcement of existing zoning designation and allowable uses. The city attempts to protect the real estate interests of the surrounding businesses and homes by avoiding the introduction of a perceived public nuisance to the area. In some cases, the municipality can bring adverse possession proceedings against property owners located on or near a site needed for industrial use.
• Entitlements is the city’s approval process. It is what determines whether a parcel of land receives development rights based on its size, design, use, etc. Sites around LA are zoned to provide guidelines for the entitlements process. Modifications and/or change can be requested to a site’s zoning in order to entitle a different type of product.

• The large majority of real estate transactions in Los Angeles occur between private parties in a free market structure. Ownership transfers require city recording; however, approval is administrative in function.

• For potential land developments, developers often purchase an option to perform due diligence activities over several years on the property. This option usually gives the developer enough time to re-zone or entitle the property with the right to build their proposed project prior to fully closing on ownership transactions.

ACQUISITION CONSIDERATIONS:
PLANNING CONSIDERATIONS:

- The planning system is highly complex, and developers in LA need to take account of zoning, master plans for the area, interaction with the Coastal Commission and/or the right-of-way for other utilities and agencies. Factors such as setbacks from property lot lines, open space conservations, preserved sightlines, traffic flow and much more must be considered.

- Although city permit and planning fees are not significant in relation to total construction costs, costs associated with consultants and land carry costs to process complex entitlements can become a significant project expense.

- There are numerous tax incentives available to developers for proposed developments, such as low-income housing tax incentives and redevelopment credits.

- Successful planning outcomes typically require consultation with a broad range of stakeholders, including planning departments and special interest groups dealing with conservation, business and community interests. Foreign parties involved often need assistance navigating this process.

- Special interest groups, elections and other interventions can influence the planning process. This means that a planning process can be delayed if a proposal has a large impact on an area or is developed in a historical or city center location.

- The Department of City Planning is charged with preparing, maintaining and implementing a General Plan for the development of the City of Los Angeles. The General Plan consists of the Framework Element, which provides overall guidance for the future of the city.

- The General Plan promotes residential and commercial growth along boulevards, corridors, and clustered development around high-activity centers and around transit hubs.

- It is comprised of 35 specific community plans that provide allowable land uses across the various communities.

- The planning department implements the General Plan by applying tools through the application of zoning regulations: traditional zoning, specific plans, overlay districts and special use permits.

WHAT IS LA’S TRANSIT-ORIENTED DEVELOPMENT PLAN?
In order to promote development and construction near modes of public transportation, LA has created focused “Transit Neighbourhood Plans” along five emerging transit corridors. These plans include land-use incentives for vibrant, transit-oriented development, attractive streetscapes, and new community amenities.

WHAT IS THE GENERAL PLAN?
California State Law requires every city and county to adopt a comprehensive General Plan to guide development. The document serves as the foundation for all land-use decisions and includes required Elements mandated by State law. Local governments may adopt additional optional Elements to address local priorities and planning goals.
1. Property Idea

2. B&S Department Reference

2A. Project Approved

2B

3. Planning Counter Reference

4. Decision/Public Hearing

5. Planning Staff Recommendations

6. Project Approval or Denial

1. The owner of a property identifies a development opportunity.

2. The owner contacts the Los Angeles Department of Building & Safety (LADBS) to check the zoning regulations on the property and to determine if the proposed project meets all zoning requirements.

2A. If it meets requirements, the applicant receives a “by right development” building permit and can commence the project with no further approvals or consultations.

2B. If the project fails to conform to zoning regulations or requires further planning approval, LADBS instructs the owner to apply to the Department of City Planning for necessary land use permits/entitlement.

3. At the Planning public counter, a planning official reviews the project and determines the type of land use permit (entitlement) required for approval. The owner then goes away with the appropriate application form and instructions for completion, and returns it to the public counter when complete.

4. For most applications, the entitlement process requires a public hearing. A notice is mailed to the relevant certified Neighborhood Council, and all other appropriate parties. At the public hearing, any individual or community group including the Council has the right to speak on the proposed project. Written comments are also accepted.

5. After considering all public testimony and planning staff recommendations, the city’s Planning department determines the outcome of project application. The application is either approved as is, approved with conditions, or denied. If there are no appeals, the decision is final. If the decision is appealed, it is subject to additional public hearings and determination by an appeal body before the decision is made final. As an entity of the City of Los Angeles Neighborhood Council cannot directly appeal a determination.

6. After an application receives approval (and subsequently the project gains entitlement), the owner must return to LADBS to obtain necessary building permits.
Construction costs in LA trend slightly above the US average (7% greater in 2015); however, when compared to the other top metros in the US (New York, Chicago and San Francisco), LA has the lowest construction costs. The city’s large labor pool helps to drive down costs relating to installation.

Construction costs in LA have risen 5 to 7% over the past five years based on the calculated composite price index for the city. Investors and developers need to consider the effect of these increases on the profitability of potential projects.
Construction activity in LA has surpassed the levels achieved before the 2007 recession. As the market has recovered, construction costs have been on the rise for more than five years. In some cases, the cost of materials has nearly doubled based on the premium paid for increased demand, although labor costs remain steady. As the construction industry grows as forecasted, construction material costs will likely continue to increase faster than inflation.

Across the city, numerous major projects are nearing ground-breaking. These projects are likely to keep the industry operating at full capacity for the next three to five years.

### Figure 4: Construction Costs Table

<table>
<thead>
<tr>
<th></th>
<th>LOS ANGELES</th>
<th>LONDON</th>
<th>DUBAI</th>
<th>SHANGHAI</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>US$ per m²</strong></td>
<td>MIN</td>
<td>MAX</td>
<td>MIN</td>
<td>MAX</td>
</tr>
<tr>
<td>High-rise prestige offices</td>
<td>4,450</td>
<td>4,900</td>
<td>3,890</td>
<td>4,970</td>
</tr>
<tr>
<td>Medium/high-rise offices, average standard</td>
<td>3,650</td>
<td>4,320</td>
<td>3,630</td>
<td>4,520</td>
</tr>
<tr>
<td>Out-of-town shopping center</td>
<td>2,490</td>
<td>3,120</td>
<td>2,470</td>
<td>3,630</td>
</tr>
<tr>
<td>Apartments - average size and quality</td>
<td>2,670</td>
<td>3,830</td>
<td>2,660</td>
<td>3,230</td>
</tr>
<tr>
<td>Apartments – high-rise private, luxury</td>
<td>4,010</td>
<td>5,120</td>
<td>4,190</td>
<td>5,890</td>
</tr>
<tr>
<td>5 star hotel</td>
<td>4,680</td>
<td>5,340</td>
<td>4,890</td>
<td>6,760</td>
</tr>
</tbody>
</table>

Construction costs in LA are the lowest among the top four largest American cities. 

*refer to inside back cover for source, definitions and notes.*
When it comes to regulation, investors need to be aware of the contractual agreements, contract models and both national and local regulations that will impact their operations in LA. Within US law, various contract models are available.
CONTRACTUAL ARRANGEMENTS:

- US law governs the enforceability of construction contracts. It is partially based in case law, which assigns judgments based on preceding case judgments.
- Within the US, a variety of standard contract templates are used for development and construction agreements; however, contracting parties are free to modify at their discretion as long as provisions do not constitute an agreement to break the law.
- The American Institute of Architects (AIA) and Associated General Contractors of America (AGC) are two leading professional organizations that maintain construction project contract templates and forms for use.
- Agreements made with a local, state or federal agencies are required to follow public procurement requirements for the authority holding jurisdiction.
- Payment terms are governed by the contract documents, but typically business-to-business invoices must be paid within 30 days of issue if another term is not stipulated in the contract.

REGULATORY ISSUES:

Regulatory requirements associated with construction can emerge from a national agency or from a state or local level.

- Nearly all construction activity requires a building permit prior to beginning site activities. Limited exceptions to these requirements include emergency health and safety repairs and cosmetic modifications under a certain dollar threshold.
- The Building Department of Los Angeles is responsible for reviewing the proposed construction work and issuing a construction permit. Fees are borne by the owner, although occasionally the contractor will pay for fees under specific contracting models. The cost is based on a variety of factors, including the overall project cost.
- All technical rules for refurbishing, building, demolishing or occupying buildings are recorded in the LA building code guidelines. These technical regulations represent the minimum requirements for all structures in LA and relate to safety, health, usability, energy efficiency and the environment.
- The City’s planning commission is a municipal body that provides guidelines on the aesthetics or positioning of a structure in connection with overall entitlements and permit process.
- In specific cases, the municipality has the power to apply special building codes to a project. These codes relate to non-technical requirements of construction works and are applied, for example, when parking pressure is high and the developer must create parking spaces on the site. The regulations also relate to issues like contaminated soil and noise hindrance.
- For some areas within the city, archeological finds can impact regulations. If historic traces are found, a specialist team must be engaged by the owner to retrieve the traces and save historical materials. This intervention might result in delays to the progress of a development.
## Figure 5: Summary of Key Market Differences

<table>
<thead>
<tr>
<th>Markets</th>
<th>LOS ANGELES</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Low commercial vacancy and limited property supply has led to strong competition in prime locations. Many areas of the city are transforming through regulation changes and city planning.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Construction</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The construction market is becoming more competitive and projects are increasing in complexity. Reliable vendors and service providers are a necessity to succeed in the market.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Cost and Inflation</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The cost of construction materials continues to rise in the market as well as nationally. Some products carry a hefty premium and are in scarce supply.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Contracts</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Well-established contract sets are widely adopted across the industry. Traditional contracts are the preferred procurement route used to assure delivery quality, but use of alternative construction structures is increasing.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Building</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>LA building codes adhere to a high-quality standard relative to other regions across the globe. The city maintains a building code publication that is updated yearly with new requirements. City building inspectors have discretion as to the interpretation of various elements contained in building code requirements. A firm with extensive experience navigating all elements of the building code is recommended.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Planning</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Although the planning process is clearly defined, local politicking and insight is a key component for success. A project can take various routes through city planning, and an expert is needed to keep the endeavor on track.</td>
</tr>
<tr>
<td><strong>DUBAI</strong></td>
<td><strong>SHANGHAI</strong></td>
</tr>
<tr>
<td>-------------------------------------------------------------------------</td>
<td>------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>High levels of office availability exist, but the market is controlled. Inward investment is creating a safe haven in Dubai. Build-it-and-they-will-come policy is still fuelling development.</td>
<td>As a Tier 1 City, Shanghai still has a very active real estate market despite lower-tier cities showing signs of consolidation.</td>
</tr>
<tr>
<td>The construction market is growing at around 5% per annum through public and private sector investment. More investment is needed in roads and other infrastructure to enable new development in buildings.</td>
<td>The big local Chinese contractors dominate construction and claim a major share of the market.</td>
</tr>
<tr>
<td>Construction prices in Dubai increased by less than 1% in the past year. General inflation is at 4 to 5% according to the UAE National Bureau of Statistics.</td>
<td>The rate of growth in capital investment in China is slowing, which is creating some spare construction capacity; however, labor costs continue to increase and prices remain unchanged.</td>
</tr>
<tr>
<td>Contracts are generally FIFIC-based and well established. Design-Bid-Build is the predominant procurement route, and Design and Build is becoming more common.</td>
<td>Standard contract documentation is in place and widely adopted by major developers influenced by international cost managers.</td>
</tr>
<tr>
<td>Dubai Municipality sets the building code and construction specification requirements. These are subject to individual interpretation. Free Zones have independent Building Control authorities.</td>
<td>Standards are relatively high compared to lower-tier cities because of the internationalization of quality and influence from MNC developers. Compliant solutions are developed by Local Design Institutes (LDIs).</td>
</tr>
<tr>
<td>Dubai Municipality is the main authority for planning. Approval is based on political and technical factors. Rapid approvals and minimum red tape are common.</td>
<td>Shanghai Planning Bureau has ultimate authority on the shape and size of developments within the city. The approval process is rigorous.</td>
</tr>
</tbody>
</table>
ASK THE EXPERTS:
NAVIGATING LOS ANGELES' INVESTMENT CHALLENGES

CHALLENGES

WHAT ARE THE POSSIBLE RISKS WHEN INVESTING IN LA?

Escalating real estate values and premium property locations make LA a tempting locale for investors and developers. Although returns on investment can be lucrative, the city presents a challenging and competitive environment on multiple fronts. An investor needs to be well versed in city politics, and vendor and contract management, in addition to site selection and land acquisition. There is a risk that even a develop/investor with a Class-A site will not be able to navigate the city’s approval process for entitlements and permitting and will also not be able to form and manage the appropriate team to deliver the project on time and within budget.

Hiring an experienced project team can help avoid these numerous pitfalls of the LA market. From an experienced design team to a seasoned project manager, a key to success in this competitive landscape is to align your organization with individuals and entities that have a track record of success navigating the process. Additionally, ensuring your organization assembles the correct team and level of oversight and controls (appropriate to the selected project, contract and delivery strategies) is a key to success. If a firm does not have a strong presence in the market, accountability for overall project success needs to be outsourced and impartial checks and balances effectively integrated.
LA is a diverse and dynamic market with various investment opportunities. Investors should align performance goals and risk appetite with the various opportunities available in the market in order to make the most appropriate selection.

Our experts specialize in navigating investment challenges to maximize opportunities. Here are some of the questions our team is frequently asked and their advice on how to proceed.

OPPORTUNITIES

WHAT KIND OF PROPERTIES WOULD BE INTERESTING FOR ME TO INVEST IN?

LA offers countless opportunities for investment in the real estate market. The demand for all types of real estate product creates various scenarios in which a savvy investor can achieve success. The most important factor would be to align your investment with the market sector that best complements your business or investment fund’s overall goals and trajectory. While signature commercial buildings have the potential for monumental returns on investment and public notoriety, infrastructure projects or high-density infill could serve as a more reliable source of continued income.

An additional opportunity for investors in LA is redeveloping environmentally contaminated brownfield properties. By transforming these contaminated sites into useable properties, investors can add a good deal of value and maximize return on investments. In order to pursue these sites, investors would need to engage an authority in environmental services, such as Arcadis, prior to tackling such a monumental task.

The LA market is a dynamic, high-demand region that can appeal to a number of investors. The city’s location, infrastructure and population make the market an appealing investment for global firms.
CONCLUSIONS:

REALIZING LOS ANGELES’ REAL ESTATE POTENTIAL
LA today is undergoing a transformation into a global metropolis. Since emerging from the great recession the city has experienced a renaissance rivaled by few other cities. From infrastructure upgrades to economic sector booms to iconic development projects, LA’s urban revitalization provides appealing investment conditions for even the most risk-averse investors. All signs point to this opportunity only growing from here: the city has a vision to continue on its journey of transformation and further establish itself as one of the world’s great cities. Although conditions are favorable, investors must remain wary of the risks and challenges the dynamic environment presents. First-of-a-kind projects mixed with complex political and vendor challenges demand that developers bring experienced teams to execute proposed projects. Although market strength is aligned with achieving high returns, cost overruns and delays will quickly deplete margins.

In addressing these risks, investors and developers must partner with industry experts who have a proven track record of performance in the LA market. An experienced team can assist developers with navigating these pitfalls, anticipating unseen risks, and extracting the greatest value from a robust and exciting investment market.
Arcadis is the leading global design and consultancy firm for natural and built assets. Applying our deep market sector insights and collective design, consultancy, engineering, project and management services, we work in partnership with our clients to deliver exceptional and sustainable outcomes throughout the lifecycle of their natural and built assets.

As one of LA’s premier asset and program management firms, Arcadis has been a long-term partner to some of the city’s largest agencies for construction, facilities, and asset management. Notable public clients include Los Angeles Metro and Los Angeles Community Colleges District.

Arcadis has also partnered with various foreign investors to perform oversight and management of their investments and construction projects. As a multi-disciplined firm with deep experience in buildings (commercial and industrial), water infrastructure, and environmental services, Arcadis provides a single point of contact for all of an investor’s real estate, engineering and construction needs.

The Arcadis LA office is made up of professionals who are leaders in their respective fields. We are able to bring together multidisciplinary teams in order to meet our clients’ unique needs.

**Key Figures**

- 27,000 people globally
- €3 billion in revenues globally
- 6,300 people in North America
For more than five decades, Callison and RTKL have created some of the world’s most memorable and successful environments for developers, retailers, investors, institutions and public entities. In 2015, our two practices came together, expanding our sphere of influence and the depth and breadth of our resources. Our team is comprised of more than 2,000 creative, innovative professionals throughout the world who are committed to advancing our clients’ businesses and enhancing quality of life.

ABOUT CALLISONRTKL

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*FIGURE 2:
Criteria definitions:

Competitiveness – overall assessment of performance including the economy, R&D, culture and the environment based on published indices.


Sustainability – balanced assessment of economic, social and environmental sustainability based on published indices.

Real estate momentum – combines short-term market indicators describing demand for real estate with long-term measures of the attractiveness of a market based on innovation, education and so on.

Tourism – measures the number of tourists and their spending habits.

*FIGURE 5:
Notes:

– Costs are current in Autumn 2016 based on exchange rates on 10th October 2016

– Office costs include the developer’s finish but exclude the tenant’s fit-out

– Hotel costs include FF&E

– All costs exclude allowances for external works, professional and statutory fees and local sales taxes

– Rates are calculated on the basis of gross internal floor area.