Major Southern California office owner shifts San Diego strategy as investors retreat from US downtowns

Irvine Co. looks to capitalize on shift to suburbs

By Lou Hirsh

One of California's largest office owners is cutting back on its holdings in downtown San Diego, joining a host of landlords responding to nationwide struggles for big-city central business districts in recent years.

Irvine Co., a dominant Southern California office landlord with properties across the country, recently offloaded its second office tower in downtown San Diego for well below its prior cost.

Property records indicate Irvine sold 101 W. Broadway for $43.9 million, less than one-third the price of $148.5 million that the firm paid for the 452,436-square-foot tower in 2005. The sale closed at the end of November, about two months after Irvine sold the second-tallest tower in downtown San Diego for just under $45.7 million, a 66% discount from its 2003 sale price.

Irvine has yet another downtown office tower on the market; a sale of all three would cut in half the six towers that for decades represented the largest collection of such properties owned by one firm in the city.

The sales mark a rare shift in the decades-long buy and hold strategy for the largest office owner in San Diego. The 160-year-old company is now looking outside the downtown core to the region's second-largest office neighborhood — University Town Center — that has benefited from mixed-use diversification in recent years.

The company is "conducting a long-term strategic review that we anticipate will include the sale of certain downtown San Diego office properties and reinvestment in others," Irvine said in a statement.

The Newport Beach-based owner isn't the only one shifting its geographic and property type focus in the wake of the pandemic that upended downtowns across the country, due to the high concentration of downtown office space.

From 2020 through the first half of 2024, the U.S. office market retracted by nearly 200 million square feet in negative absorption, the net change in occupancy. That retrenchment hit downtown areas harder than their urban and suburban office peers.

Downtown San Diego's office vacancy rate of 31% is more than triple the 10% level in nearby University Town Center, or UTC, named for its proximity to the University of California, San Diego in nearby La Jolla.

Struggles for San Diego's downtown mean UTC's status as the second-largest office neighborhood

could change significantly in the next few years. Irvine and local commercial brokers said a major catalyst is a community plan update approved by the city earlier this year for UTC.

Mixed-use shift

Irvine already owns nearly 40% of the existing office inventory in UTC, according to CoStar data. The firm's development focus is going to be more on mixed use in nature rather than traditional office, as remote-work trends in the wake of the pandemic have prompted some companies to cut back on their office use.

“Guided by the city’s vision and our experience creating world-class mixed-use districts, we are beginning our master planning to create quality housing connected to office campuses, retail, transit and open spaces,” Irvine said in a statement.

City officials and local brokers have said multiple regional and national developers are expected to put forward plans in the coming years for mixed-use developments in UTC that will likely include office, retail and multifamily elements to "take advantage of one of San Diego’s strongest employment and housing nodes," according to Joshua Ohl, senior director of market analytics for CoStar Group in San Diego.

San Diego Mayor Todd Gloria signed into law an updated community plan for the UTC neighborhood, replacing a blueprint that was established in 1987. The city now seeks to add 29,000 housing units to UTC, which would nearly double the neighborhood’s population to around 130,000 over the next 25 years.

The plan also seeks to add 72,000 new jobs to what is already a bustling business hub, by attracting new commercial projects to the area. Plans come as San Diego like many cities is looking to boost the housing supply in response to chronic statewide problems with affordability, while also getting polluting vehicles off roads and encouraging development of pedestrian-friendly mixed-use projects.

“The community plan update could provide momentum for investors," Ohl said, adding that the shift to UTC comes "as office demand downtown has fallen and apartment buildings are selling below construction costs."

Downtown deals

Irvine Co. counts a 129 million-square-foot office portfolio in California, Chicago and New York; it also develops and owns retail, hospitality and housing throughout California.

The firm self-finances the bulk of its investments and developments, and has historically not faced substantial financial struggles.

In September, Irvine signaled a shift for San Diego's real estate market when it sold the 34-story Symphony Towers to Formosa Ltd. for just under $45.7 million, or about $84 per square foot,

according to public filings. That's a steep discount from the $134 million, or $246 per square foot, that Irvine paid in March 2003 for the downtown San Diego tower.

The firm then tapped brokerage Eastdil Secured to market for sale two other downtown San Diego towers that are each more than 40 years old, at 101 W. Broadway and 225 Broadway.

It purchased both towers in a 2005 portfolio deal totaling $265 million, and offloaded the larger 101 W. Broadway tower just before Thanksgiving for roughly $97 per square foot, based on the property's transfer tax listed in a public deed filing. Records indicate the buyer is a private joint venture involving Stockton Blvd. Partners and Saca Properties.

The potential sale of 225 Broadway would bring Irvine down to three downtown high-rises, including the 34-story One America Plaza, built in 1991 at 600 W. Broadway and still the San Diego region's tallest office building.

Like Los Angeles and other large cities nationwide, San Diego's older downtown office towers experienced rising vacancies and sublease opportunities well before the COVID-19 pandemic caused a sharp ramp-up in remote and hybrid work arrangements.

CoStar data shows downtown San Diego's office vacancy rate at 31.5%, close to a historic peak. Its availability rate, with space for sublease factored in, is 36.8%.

The same situation has been mirrored in multiple U.S. cities such as Los Angeles, San Francisco, St. Louis, Chicago, Cleveland, New York and Seattle, as owners sell off older towers in urban hubs at well below their previous deal prices. In some cases, like in downtown Los Angeles, towers have been sold by lenders or special servicers after property owners walked away from troubled loans.

Ohl noted that Irvine Co. is reported in local brokerage circles to be considering at least one more downtown tower sale as it looks to retain two in the neighborhood. The company declined to comment to CoStar News on further downtown sale plans.

"We are actively planning to reinvest in the greater San Diego metropolitan area and anticipate growth for the foreseeable future," Irvine said in an emailed statement.

Tale of two neighborhoods

Much of that growth is slated to occur in UTC, a market where office asking rents are among the highest in San Diego, though rent growth has slowed in the past year. Roughly 560,000 square feet of office space is underway, all of which is spoken for. Meanwhile, the apartment vacancy rate is down year over year to 4.4% from 4.8%, with rents up nearly 1% in the past year to $3,190 per month, among the highest in the county.

"UTC's status is firmly cemented as one of the most attractive submarkets in San Diego to both live and do business," according to a CoStar analysis.

Ariq Huda, vice president in the San Diego office of brokerage JLL, said the rise of UTC is in part the culmination of problems that have long plagued the downtown office district. Those include homelessness, crime and from a tenant perspective a shortage of convenient parking available at a feasible price for many types of businesses.

Also, many of downtown's office buildings are older, including some dating back 40 or more years that would be challenging to renovate with the sort of high-end amenities some companies demand. It hasn't helped that a number of the region's biggest job-creating industries, such as technology and life science, have long been migrating north to match where company executives and workers are residing, putting downtown at a disadvantage.

"The big employers already know to establish their operations to enable their workers to get to work in the quickest way possible, including shortening their commutes," said Huda, who primarily represents office tenants in the region.

Huda said downtown landlords could face mounting challenges in years ahead if the neighborhood's current drawbacks cannot be addressed. But UTC also has some challenges, including limited available land for new development, meaning much of the neighborhood's future projects will likely involve redeveloping or repurposing older properties to cluster housing, offices and retail.

Changing development focus

UTC's development since the mid-1970s has mostly played out through development of individual projects with just one type of component rather than mixed configurations.

That has gradually begun to change over the past decade. Mall operator Westfield invested about $1 billion in upgrades to its 40-year-old Westfield UTC mall, including redeveloping some retail buildings to include second-story offices now occupied by firms such as Amazon and CBRE. It has further mixed-use redevelopment planned for the UTC mall site that formerly housed Nordstrom.

Westfield also worked with nationwide developer Greystar to build a 23-story luxury apartment tower that opened in 2019 on land that once housed mall parking spaces. In 2021, regional transit officials completed a $2 billion extension of the light-rail San Diego trolley that brought full service to both University of California, San Diego and the nearby UTC neighborhood for the first time, with a terminus at the Westfield mall.

"The trolley extension is one of the biggest things that ever happened to UTC in terms of people wanting and gaining access to the neighborhood," said Ron Miller, senior vice president with brokerage Colliers International, who primarily represents office tenants throughout the San Diego region.

Unlike downtown, which has seen office rents decline as vacancies soar, Miller noted rents are holding steady in UTC as demand for space remains steady among technology, life science and financial service firms.

Located in what is known as the city's Golden Triangle, where state Route 52 crosses interstates 5 and 805, the enclave has become increasingly attractive to residents of northern San Diego, including corporate executives, and also commuters living in suburbs to the north, such as Carlsbad and Oceanside.

Downtown remains a big hub for the local tourism industry, with the San Diego Convention Center feeding steady year-round business into neighboring hotels. But Miller said downtown's current office trajectory will likely spur owners and developers to rethink their plans for big projects in the region as the center of business gravity shifts northward.

"The idea of the central business district is changing," Miller said. "The reality in San Diego at this point is that the true central business district is a place like UTC."