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Is High Tech Moving Out?

THE "RIGHT" SMALL CITIES CAN ATTRACT TECH COMPANIES

By Steve Lewis | Sponsored By SIOR Foundation

Recent articles have touted the proposition that Silicon Valley is no longer the mecca for high-tech companies that it once was. A number of smaller, less costly cities are succeeding in luring tech companies away from such major hubs.

"Ironically, tools created in Silicon Valley (such as Slack) have made it easier for people to work remotely and for companies to start up outside urban areas where the cost of living is significantly lower," writes Inc.'s, Marc Emmer. "According to PitchBook, less expensive alternative cities like Seattle and San Diego feature venture capitalist investments of over a $1 billion [*sic*] a year."

Emmer continues: "The Economist reports that a median-priced home in the San Francisco Bay Area costs $940,000—more than four times the national average. Forty-six percent of Bay Area residents plan to leave 'in the next few years.'"

"Google employees aren't the only ones walking away from elite tech headquarters," crows the headline of a CNBC report. "Silicon Valley is not about to lose its dominant position as the home of billion-dollar technology start-ups and hub for top talent, but there are a growing number of reasons why more workers and new companies are choosing other cities, far from San Francisco, Boston and New York, to call home. Several quality-of-life considerations come into play, from housing costs and transportation ease, to education opportunities."

"When I read out the 16 leading 'smart' cities, the top ones are expensive, but are the others?" challenges Daniel Levison, principal of CommissionTrac in Atlanta. "[In terms of expense and cost of living,] Dallas is not outrageous; and places like Denver, Charlotte, and Austin are being sought out; Chattanooga is also not expensive; and look at Augusta—it's exploding in high-tech."

There are a number of factors a company must consider when moving outside these larger cities. "If companies are unable to find the kinds of workers they need, they are not going to move to that city—it's that plain and simple," adds Grant Pruitt, SIOR, president and managing director of Whitebox Real Estate in Dallas. "Typically, labor is a company's highest expense, and

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especially in tech, labor is usually the greatest driver of real estate decisions. I recently had a real estate director from a very large publicly traded tech company from California tell me that the cost of the prime real estate space they had in San Francisco could be attributed to about 5 percent of the cost of an employee there. They cannot find enough engineers, so they are competing via the office environment to create a better workplace than the corporate competitors down the street. They are pushing the limits in terms of finishes, wellness, and amenities to attract these people. If the people are not available, the companies will not go there."

It Depends On What "Small" Is

Pruitt is quick to point out, however, that size and cost alone will not attract these types of companies. "It depends what you quantify as 'small,'" he explains. "There has to be a draw or a reason, and that reason is typically education. Pittsburgh is a smaller city that comes to mind. Carnegie Mellon and the University of Pittsburgh are a very large reason for this. Austin is in a similar place in that it has the University of Texas among others, and it has a rich technology legacy."

Past a certain point, however, a city will be too small to support relocation, Pruitt continues. "I'm in Dallas, Texas. We have some 209,600 jobs in the tech sector; that is almost the population of Houston and Austin combined. Dallas has a very large tech presence and more than five major universities (45 universities and colleges in totality). It also has a great legacy of tech (Texas Instruments, EDS, Perot Systems). Only 6-8 percent of the Dallas economy is in the tech space. The tech talent pool is larger than a small city, just because there are more people."

Still, in his article, Emmer cited the following "tech hubs" as "thriving": Portland, Ore.; Seattle; Austin, Texas; Washington, D.C.; Detroit; Charlotte and Raleigh-Durham, N.C.; Huntsville, Ala.; Grand Rapids, Mich.; and Orlando, Fla.—not all areas teeming with people.

Chris Falk, SIOR, principal and executive vice president at Newmark Grubb ACRES in Clearfield, Utah, says that "overall, the majority of tenants look for a downtown hub," but in some cases employees can be attracted to locations outside the heart of "smart" cities.

"Developers, computer engineers—that crowd likes the higher end mixed use or downtown living," he asserts. "What I have seen in the last 12-18 months has been several national and some international companies reaching out to me in this area." However, he adds, the hottest area, "Silicon Slopes," is slightly outside of downtown.

"As an employer, you may not want to compete specifically for that talent and instead offer a little different type of work environment," he explains. "For employees, they can drive to work or ski in the mountains in 20 minutes or less."

As part of an employer's competitive analysis, he continues, they may determine that if they can offer a little better or higher variable or lower cost of living, the employee can buy a house. Typically, of course, the real estate will be a little cheaper; there would also be free surface parking.

Co-working a Fit for Smaller Markets

Levison says that for the smaller markets, co-working facilities can help draw these companies because professional and tech related companies seem to enjoy the environment. Of course, we're not talking about "Amazon's" here, but there are still many companies like these in need of space, he points out.

"We're about to raise money for four new locations—in Greenville, S.C., Birmingham and Huntsville, Ala., and Chattanooga, Tenn.," he shares. "I'm not going to the Charlottes and Nashville's and Raleigh's."

With the ability to work remotely, he continues, tech companies "will be looking at cities where the costs are lower and the pace more subdued." Cities like Knoxville, Tenn., Asheville, N.C., and Columbus, Ga. are on his radar for that reason.

Not that he's only working with small companies. "We work with Verizon, and one of the things they like about co-working is going to sites where they need to be for two months, or six months," he shares. "These are secondary or tertiary cities."

As new techs and startups grow, he continues, "you'll see some of these secondary cities growing too." For example, he points out, Huntsville, Ala. now has fiber running throughout the city. "This gives tech companies a level of confidence the internet will not go down; when you are not on fiber you will not get a master service agreement (MSA) which guarantees certain speeds of delivery," he says. "There have been more multi-family permits filed there than in any city in the Southeast."

While Levison admits you "probably will not get a company on the list of top Fortune 500 companies to go to Chattanooga, you could probably go on NASDAQ and find that middle tranche—$20 million or $30 million. Then it's all about lifestyle and cost of living, so go after the right group."

Another advantage, he says, is that "you get smaller, more nimble businesses; [but] that doesn't mean they are not stable." Still, he concedes, in bigger cities you'll find a larger amount of quality workers—assuming large numbers are what you need.

Watch Your Sites

It's important to remember, says Pruitt, that regardless of whether your market is a large or small city, the three principal factors of real estate (location, location, location) still apply. "The issue that SIORs need to be aware of is poor site selection and demographics research," he says. "Not being in the right area, the right location, the right building, the right environment, can kill the company. If they can't recruit and retain, the company will cease to survive."

How can these problems be avoided? "It comes down to doing your homework," says Pruitt. "Everyone is looking for alternate locations, but they are not always there. The way I have seen this overcome, though, is if the company or multiple companies create their own ecosystem. They can master plan this and invest in it to pull it off. It takes money and commitment.

"As it relates to the oversaturation," he continues, "that is owner-specific. Many tech companies are more or less still startups that may not have been in business very long. There are not a lot of assets to securitize a lease. There are some tricks to help securitize it, but this takes some planning and negotiating."

But whatever the market, he adds, "the companies have to be in places that can draw the workers and support the job requirements. Also, the employees typically want to live in these cities. Cities need a nice young neighborhood for these young, typically millennial, employees that offer the live-work-play environment."

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