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THE RETAIL CONTINUUM:

Staying Ahead of the Curve in Today's Market

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While bankruptcies have increased in a slower market, quality space still commands a premium. The current market has brought both pros and cons for the retail industry. As long as buyers remain—and tenants are allowed to remain in their stores—there can be real reasons for optimism in this sector. Spence Mehl explains…

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While lately it seems as if doom-and-gloom economic headlines have ranged from grim to grimmer, the direct impact of the subprime mortgage crisis and subsequent credit crunch on retail's bottom line has been somewhat less dramatic. The industry as a whole has thus far proven to be quite resilient, especially considering the overall economic context.

That said, there have been noticeable changes. The sluggish real estate market has inevitably begun to exert somewhat of a slowing effect on retail growth. In addition, rising prices in staple necessities such as food and gasoline have contributed to an overall cost-of-living increase that has taken a toll.

The net result is that, fundamentally, there are fewer overall dollars available for American consumers to spend. The statistics reflect that reality—with retail growth slowing and softening markets contributing to overall square footage numbers that are at their lowest levels in quite some time.

A UBS-International Council of Shopping Centers survey of 43 prominent retailers reported a same-store sales average gain of just 2.1% in 2007, and early results from this year have been even more anemic. Sectors that have been hit particularly hard include areas such as furniture, luxury items and some apparel.

While 2008 promises to be a challenge for some…the long-term future looks bright for those who are able to meet that challenge with creativity, flexibility, insight and innovation.

With store closings currently outpacing openings and more on the horizon, the situation seems likely to get somewhat worse before it gets better. Retail bankruptcies are on the rise, including some very prominent names in American retail. With the majority of those bankruptcies going right to liquidation, store counts are dropping.

But the news is not all bad. In fact, there are a number of real reasons for optimism. There are still buyers out there, and across the board we are seeing a renewed appreciation for quality.

Compared to some slices of the national economic pie, retail has held its own, and for new stores in quality locations, rental prices have not appreciably fallen off. People are understandably cautious and more likely to wait for prime opportunities, but there are buyers, and there is a lot of development and investment money still out there.

The "flight to quality" phenomenon is a natural and healthy development in a free market, and the Darwinian nature of the commercial marketplace will ultimately reward quality and demand a realistic reassessment of marginal spaces. With retailers consolidating in good markets and fleeing from bad ones, the "A" locations are going to continue to do just fine. It is those "C" malls and developments (generally those with sales of $225/square foot or less) that are going to struggle.

On the growth and development side of the coin, this all adds up to *opportunities*. There are bargains to be had and, with prices beginning to fall, landlords are generally more willing to work to keep tenants in place than they were 12-18 months ago.

Keeping occupancy numbers as high as possible becomes even more of a priority during periods of uncertainty, and, with "lease-up" times growing longer and overall cycles slowing down, landlords and tenants alike will need to continue to engage in creative and productive negotiations to derive maximum value from less expensive space. Because while 2008 promises to be a challenge for some, with continued slow growth and consolidation likely, the long-term future looks bright for those who are able to meet that challenge with creativity, flexibility, insight and innovation. abfj

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