

A HELPING HAND IN HARD TIMES LANDLORDS FIND WAYS TO HELP TENANTS COPE WITH A TOUGH ECONOMY.

By Joel Groover

On these rainy days for the U.S. economy, retail landlords are doing whatever they can to stay dry. When Americans began receiving those tax-rebate checks in their mailboxes this spring, some people did exactly what the architects of this government “economic stimulus” plan had hoped: They took their windfalls shopping. And when they got there, they found the malls eager to help.

“We’ve been doing a ‘Stretch Your Rebate Further’ promotion at 25 of our malls,” said Brooke Houghton, vice president of public relations at Jones Lang LaSalle. “If you spend \$200, you then get a \$20 mall gift card. It helps the consumer, but it also draws them back so they can spend that gift card at another point.”

At The Shops at Atlas Park, in Glendale, N.Y., meanwhile, the cash giveaways were downright theatrical. On April 14 mall owner Damon Hemmerdinger walked up to shopper Cynthia Lewis and handed the 43-year-old mother of three \$1,000—in cash. Hemmerdinger’s costumed companions were dressed as Lady Liberty and Uncle Sam.

These are just two examples of the ways shopping center owners and managers are fighting the economic slowdown. Some are focused on strategies to help struggling tenants stay afloat. Hemmerdinger, for one, seeks to buoy consumer confidence, cheer up tenants and drive mall traffic by countering what he sees as excessive pessimism about the economy. His commitment, in fact, goes well past handing out 60,000 “I Support the Economy” stickers this spring; he also gave away \$20,000 of his personal savings to shoppers at Atlas Park.

“I decided to take the most constructive step I could think of to inspire people to change their point of view on the economic future,” Hemmerdinger said. “People have been saying things won’t get better until the election in November. That will be a self-fulfilling prophecy if we all believe it.”

This is not to dismiss the seriousness of the challenges some retailers and landlords face. By all accounts, sluggish sales and

tight credit have contributed to a rash of store closings and retailer bankruptcies this year, particularly among home furnishings chains and others that rely on discretionary income. The list of hard-hit retailers thus far includes Ann Taylor, Circuit City, Linens ‘n Things and Sharper Image. ICSC predicts that 5,770 stores will close this year, up 25 percent from last year.

“What we thought might be a 20 percent increase in business this year may end up being upwards of 40 percent,” said Michael Wiener, president and CEO of Excess Space Retail Services, a consulting and advisory firm focused on real estate disposition and lease restructuring for the retailer side. “I’ve never seen this many retailers at one moment talking about closing stores.”

For shopping center owners, of course, these trends translate into unpaid rents and greater risk of vacancies. The rate of vacancies at neighborhood and community shopping centers rose 20 basis points to 7.7 percent during the first quarter, writes Sam Chandan, chief economist at Reis, a New York City-based research firm, in a report. This is the highest level since 1996 and 100 basis points above the low of 6.7 percent in the second quarter of 2005. Moreover, the gap between list rents and what landlords actually receive for retail spaces widened during the first quarter of this year, to nearly 10 percent, the highest since 1989, Chandan says.

Vacancy rates at regional malls, which typically lag those of smaller centers, increased by 10 basis points to 5.9 percent, their highest since the fourth quarter of 2002, Chandan says. “A small number of national brands have closed in the first quarter,” he wrote. “There is significant risk of other, larger retailers shuttering [at regional malls] over the next year.”

In such an environment, owners and managers should work especially hard to support struggling tenants, says John Bemis, executive vice president and leasing director of Jones Lang LaSalle’s retail group, in Atlanta. Just as promotions can be tailored to help jewelry retailers for Valentine’s Day, similarly customized programs

are possible to help those retail categories hit hardest by a slowdown, Bemis says. The Shopping Center Group, an Atlanta-based retail real estate brokerage firm, is using precisely this strategy when it organizes large tent sales for its furniture retailers. "These are commingled events where, instead of the furniture guys doing their own solo event, they're leveraging everybody in the center," said John Sebring, a property management director in the firm's Georgia division. "They wouldn't do that in the past."

This willingness to work together highlights a more cooperative and humble attitude among retailers since the downturn, and this holds true even for some traditionally recalcitrant national and super-regional chains, says Sebring. As a result, tenants may now be willing to contribute more money, time and effort to ads and events spearheaded by the landlord. The positive response of tenants to Hemmerdinger's campaign, for which California Pizza Kitchen chipped in \$2,500, helped lift spirits as well as traffic at Atlas Park. "Every single store, including nationals you wouldn't expect to do this, has stickers at the cash registers to give to customers," Hemmerdinger said. "They have their employees wearing the stickers. There has been a real positive impact."

Landlords can help tenants in less-visible ways as well, says Sebring. The Shopping Center Group is working with its landlords to slash the cost of operations-related goods and services. The sluggish economy actually makes it easier to get better pricing for the landlord through rebidding on such things as insurance. "I've never spent so much time on making sure we have the single best pricing on everything," Sebring said. "Our leases allow us to pass a lot of these operating expenses through [to tenants], and if those expenses are reduced, it is a good thing for all the retailers."

And landlords can tinker with the tenant mix itself, says Jonathan Dubovsky, leasing director of Shopping Center Group's Georgia division. One approach is to eschew troubled categories and sign shorter-term leases with necessity-focused retailers, Dubovsky says. When the market rebounds and those leases expire, the landlord can revisit the role in the overall mix of tenants that rely on shoppers' discretionary income, such as fashion or home furnishings chains.

"It's a way of putting retailers in there to weather the storm and get cash flow going," Dubovsky said. "Unless warranted by the tenant, you don't put a lot of tenant allowance or improvement dollars into the center. You try to minimize what the landlord is taking out of pocket."

Of course, with regard to helping retailers, all these strategies remain on this side of what every landlord considers a last resort: outright rent relief. No doubt about it, though, more and more retailers are indeed turning to their landlords and asking for a break, says Ivan Friedman, president and CEO of RCS Real Estate Advisors, a New York City-based retail real estate advisory firm that represents retailers in such negotiations. "Even the healthy retailers are very active in looking at their portfolios and addressing underperforming locations," Friedman said. "We are going to landlords and saying, 'This

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Unpleasant as it may be for the landlord, rent relief is sometimes the only option. The incentives to keep stores open, even at a lower rental rate, are many, Friedman says. The need for cash flow is one. "I call it 'some rent instead of no rent,'" Friedman said. Another incentive is the painful cost of replacing retailers that fit the tenant mix and are, in rosier times, popular with

shoppers, says Dubovsky. "In some cases, it can be significantly more expensive to replace those tenants than to keep them in the center [during a slowdown]," he said. These expenses, incidentally, rise during a downturn. Landlords that once could replace tenants within three to six months now expect the process to take between one year and 18 months, Friedman says. Smart tenants who have chosen to expand in this environment already are using their newfound leverage to demand better terms, including more money for store build-out, he says.

Yet another concern, particularly for landlords who own properties that rarely reach 100 percent occupancy, is avoiding a vacancy level that undermines the welfare of all the tenants. "As a rule of thumb, landlords don't want to be less than 90 percent open and occupied for a mature center, and, certainly, if it gets to less than 80 percent,

that would be worrisome,” said Lary P. Hanshaw, president and CEO of Oakland, Calif.–based Metropolis Retail, an advisory firm for retailers.

In deciding whether to reduce the rent or allow termination of a lease, landlords must analyze the overall market, the center’s competitive position and the tenant’s current health and future prospects, Hanshaw says. If the landlord does decide to offer relief, certain approaches can be mutually beneficial. “We’ve looked at situations where we will convert [from base rent] to a straight percentage rent,” Hanshaw said. “That way if sales go up, the landlord benefits from that. If you hit a certain sales level, which will differ by center, [the retailer] pays back the accrued credit received to date.”

Developers nervous about occupancies at a new project set to open could use rent relief as a bargaining chip. “They can say to the retailer, ‘Well, if you open in this location, then as a quid pro quo we will give you rent relief in these other centers,’” Hanshaw said. “That seems to satisfy both parties.”

Whatever strategies landlords adopt to assist their tenants during this challenging time, though, they should keep in mind that this cycle, like the boom that preceded it, is temporary, Bemis says. Owners must never allow shoppers to forget about their centers and stores. “In a slow time, you can’t slash your sales and marketing budget,” Bemis said. “This is just a cycle. Following these cycles is always a period of pent-up demand. ... Once we get back on track to where we need to be, consumers and retailers alike will be clamoring for product.” ■
