

COLD SHOULDER

RETAILERS ARE FAVORING URBAN CORES FOR EXPANSION AND SHUNNING SECONDARY MARKETS

By Steve McLinden

AS U.S. RETAILERS RETRENCH, they are digging into familiar turf. For that small number of national tenants still able to expand during this downturn, almost all of the leasing action is taking place in the major market areas, site-selection experts say.

"The deals that are getting done are in the more densely populated urban areas," said Joseph French, national director of retail at Sperry Van Ness. Not only are secondary and tertiary sites off the table for most retailers, French says, so are some of the more challenging urban redevelopment parcels. Many retailers grew from concerned to frightened this fall, and retail developers are seeing a marked increase in the number of tenants backing out of deals, he says.

Still, retailers are not utterly abandoning long-term growth plans for diverse markets, French says. "Thus far retailers have told me they have simply pushed their plans back," he said. Chains planning to open 20 stores in each of the next two years, for instance, could opt to open only five next year and then roll the balance of postponed openings over to the following year's schedule, French says.

Less retail expansion into smaller markets "has as much to do with concepts limiting growth dramatically or abandoning growth altogether," said Joe Brady, managing director

of retail outsourcing services at Jones Lang LaSalle. "Concepts are growing, if they are growing, in more in-fill areas rather than the suburban-ring fringes." That fringe growth came to a screeching halt when anchors such as Target and Wal-Mart began pushing openings from 2009 to 2010 and 2011, says French.

Sitehawk Retail Real Estate, an affiliate of ChainLinks Retail Advisors, has witnessed a pullback in retail expansion plans for 2009. "National retailers are being extremely selective, and they are finding themselves in the driver's seat when negotiating deals," said Mark Perlstein, the firm's principal. Sitehawk is fielding more requests than ever for in-depth site demographics and competitive analyses, he says.

Local leasing agents have had little success trying to persuade national retailers to come Texas' oil-wealthy Midland-Odessa area, which, as a tertiary market, is off the radar screen of many large national retailers, says Roy Allen, general manager of Music City Mall, in Odessa. That market's population of 260,000 is hungry for new retail and supported the existing chains this year with double-digit sales, says Allen.

Under current conditions, retailers are looking only at the best real estate and shopping centers, which are mostly in the major markets, says Ivan Friedman, who heads New York City-based RCS Real Estate Advisors.

"They have capital issues and have to be very

selective on new sites," Friedman said. After October's stock market drop, most retailers that had been mapping out growth plans for several years stopped looking ahead over six months, he says. "They simply aren't able to look too far out with the uncertainties of the economy and Christmas."

Because of this widespread apprehension, some RCS retail clients that were previously told their leases would not be renewed after Jan. 31, 2009, are seeing landlords reapproach with offers of two- and three-year extensions, says Friedman.

Retail analyst Bill Dreher, of Deutsche Bank Securities, notes in a report that many retail chains made ambitious store plans when consumption was unusually robust and that it has become clear that those expectations were inflated. Since then, the cutback announcements have been manifold. Starbucks is in the process of shutting down about 600 U.S. stores by early 2009. Ann Taylor, Foot Locker and Zales will each close between 100 and 150 stores. Charming Shoppes, owner of Fashion Bug and Lane Bryant, says it will shut 150 stores. Pacific Sunwear is closing down its 153-store Demo concept, and Wilson the Leather Experts is darkening about 150 stores. ICSC projections say 5,770 stores will close in the U.S. by year-end 2008.

Some major retailers are even forsaking large metropolitan sites that have been in

their pipelines for years. Home Depot, which said nearly a decade ago that it would anchor the long-planned East River Plaza shopping center, in New York City's East Harlem, has withdrawn from the yet-to-open project and is now attempting to sublet the 110,000-square-foot space it leased in 2006. Home Depot said in May that it would forgo 50 U.S. stores it had in the new-store pipeline and would close 15 others. The chain is posting a \$400 million charge for financial obligations associated with the canceled stores.

Citing what it calls a squeeze play on consumers, Kohl's, one of the industry's healthiest retailers, scaled back its expansion plans this year to about 70 from 90. Though the company has identified 400 sites in markets of varying size for potential stores, it says that kind of growth may not happen until 2014.

"A big problem right now is getting anyone to make a decision on future expansion," said retail consultant Jeff Green, head of Mill Valley, Calif.-based Jeff Green Partners. Many of today's store closings are the result of retailers' excessive penetration of markets, he says. "Wall Street is killing retailers on cannibalization and same-store sales decreases," Green said. Gap

and Chico's, both of which sustained double-digit same-store sales declines this fall, and then suffered commensurate drops in share value, are examples, he says.

But smaller markets may yet get their national concepts in the near future, says Green. Retailers questioning whether they have too many stores in highly competitive markets are likely to look closer at the secondary and tertiary ones as the path of least resistance, he says. Apart from the economy, a general unwillingness to tailor store formats to smaller markets is holding some retailers back.

"While many retailers have found their stock prototypes to be too big to be successful in smaller markets, they still, for some reason, remain averse to creating smaller prototypes that stand a better chance of adapting to them," Green said. He points to Apple, which generated a nation-leading \$4,500 in sales per square foot in 2007, versus Best Buy, which pulled in \$930 per square foot, according to Bernstein Research.

Lower-tier markets allow a chain greater penetration combined with minimal sales cannibalization, says Perlstein. "Plus, you will

also typically have lower overall occupancy costs in secondary and tertiary markets compared to major metropolitan areas," he said. The downsides are smaller daytime populations, slower merchandise turnover and reduced sales volume.

While some retailers are scaling back, "others are realizing that if they have the money, it's a great buyer's market and they want to take advantage of the opportunity at this point in the cycle," said Charles Wetzel, COO of Fort Worth, Texas-based Buxton Co., which specializes in site selection for major retailers. "But retailers are going to be extremely careful over the next few years with credit markets like they are. We are going to see them focus more on existing customer bases.

"We are seeing a large new crop of retailers coming up that have smaller footprints but have a strong concept." Retailers that are able to grow are still looking for the biggest potential markets, he says, and this does not necessarily exclude smaller trade areas. "Our clients are simply telling us they are looking for the best location in the right market." **SCT**
