Silent mall departures signal new risk for retail

By Robin Driver - January 12, 2018

Despite a strong holiday performance for retail, malls will continue to struggle this year, according to a white paper published by Green Street Analysts. Stealthy in-line store pull-outs and intensified competition to attract new retailers are just some of the problems facing retail real estate companies in 2018, which must diversify their offer and focus their investments on consumer experience to survive.

The report, written by Green Street President Jim Sullivan and Senior Associate Otto Aletter, analyzed 2017 tenant turnover in 950 malls in the United States in order to determine their trajectories, and highlighted some potentially worrying trends.

In addition to announced widespread department store closures, the report found that around half of the top 25 national retail tenants were exiting malls without making any public announcement, often by simply not renewing expiring leases.

This trend was identified as “a significant risk to the sector”, as the retailers in question – among whom figure Hallmark, Claire’s, Mens Wearhouse, Kenneth Cole and The Body Shop – are largely in-line tenants which, despite having an exaggerated effect on a mall’s net operating income, tend to slip under the media’s radar as it focuses on the big closures of anchor tenants.

The report explains, “Although department store struggles have dominated headlines, they provide only a small portion of a mall’s net operating income (NOI) because many anchor tenants own their stores or pay little-to-no rent. In-line tenants, therefore, have an outsized impact on mall NOI, and their performance offers a preferred indicator of mall health.”

In spite of this, some retailers are continuing to expand their brick-and-mortar footprint: Sullivan and Aletter cite companies aiming to increase their brand offerings, or e-commerce brands looking to adopt an omnichannel model, such as Fabletics, Suitsupply and Bonobo.

However, just as malls are having to fight to maintain their existing in-line tenants, they will also face stiff competition in attracting new tenants among expanding and emerging retailers.

The report notes, “while there are new emerging brands who are expanding their brick-and-mortar locations within malls, they are being more discerning about mall quality and ownership, and they are opening stores at a slower pace,” concluding “Landlords now must work harder at building relationships with more selective tenants, with something much more than a commercial real estate lease.”
each tenant representing a smaller proportion of overall demand.”

Reporting for Forbes, Pamela N. Danzinger stated that malls would have to radically rethink their strategy over the coming year, claiming that “Their primary job is not about real estate any longer, but transforming their business model to one focused on attracting shoppers so that they can then attract tenants, not the reverse as in the past.”

The trend for experiential retail and shopping destinations continues to grow, as traditional retailers face up to formidable online competitors. Against e-commerce giants such as Amazon, retailers have adopted a wide range of strategies, including opening pop-ups and hosting in-store events in a bid to increase foot fall at brick-and-mortar stores.

Among successful strategies adopted by malls, Danzinger pointed out the transformation of spaces into offices, gyms, theaters, and residential facilities, underlining a general trend to focus more on consumer experience and create community-based environments. She also emphasised the importance of foregrounding experience, rather than stores and products, in mall marketing.

Indeed, with analysts claiming that malls are now paying the price for overbuilding, many retail real estate companies are having to make large investments to accommodate the seismic shifts taking place in the industry and protect their assets.

A study published by Jones Lang LaSalle last year, for example, revealed that $8 billion dollars had been spent to revitalize 90 US mall properties, with the majority of funds going towards developing secondary-use spaces.

Elsewhere, Franco-Dutch group Unibail-Rodamco acquired Sydney, Australia-based Westfield Malls, which operates 33 retail centers in the US, in a $16 billion-dollar deal in December. In a release published at the time, the company stated that the acquisition was part of Unibail's strategy to focus its energies on high-end "destination" malls in landmark locations.

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