Shifts in retail habits dent US asset values

Shopping centres

Cheaper rents and lower footfall could mean trouble for investors in American retail properties, reports *Daniel Thomas*

Starbucks chairman Howard Schultz painted a worrying picture last month of the "abundance of empty storefronts" spreading across US cities, even in what he described as "prime A1 locations".

Worrying, that is, for the property owners who now face a structural shift in demand for shops in malls and retail precincts. For Mr Schultz, who has 14,000 US outlets, it means lower rents to come for his popular café chain.

In a memo to staff that has been seen by the FT, he said the coffee chain was "at a major inflection point" where landlords across the country would be forced "sooner than later" to lower rents "as a result of the acute shift (consumer behaviour) away from traditional brick and mortar retailing to ecommerce".

He pointed to "an ever-shrinking list of potential tenants to fill the empty store fronts within their [landlords'] retail portfolio that will blanket the country", and not "a cyclical change in our occupancy expenses, but a permanent lowering of the cost of our real estate".

All this spells more damage to come for the US retail property sector, which has already experienced a wave of bankruptcies and restructurings that have hit demand for new stores.

Investor sentiment about the sector is reflected in the wave of investors selling the shares of listed shop owners "short", in the expectation that they will fall.

Short demand for the top US retail Reits — real estate investment trusts that own retail properties — is more than 8 per cent, according to IHS Markit. In companies such as CBL & Associates, Pennsylvania Reit and Tanger Factory Outlet Centers, more than a fifth of shares have been borrowed to sell short.

According to consultancy CBRE, US retail property was among the only major asset classes to see a fall in value last year owing to fears that internet-based retailers were taking market share.

The shift from physical retailing to ecommerce is not the only problem facing the sector, according to some analysts. Mike Prew, an analyst at Jefferies, says that Reits investing in malls have "deeper problems" than the shift towards online sales and saturation in the mid-range casual dining market.

"Retailers are adjusting to e-tailing but the baby boomers are decluttering while their offspring, the anxious Generation Y or 'Boomer Echos', are looking for authenticity and 'slow' instead of 'fast' fashion."

Analysts and agents describe a polarising of the US retail property market, as the best located centres continue to prosper but ones in less affluent areas struggle.

The economic backdrop is at least supportive, with consumer confidence high in the US on the back of President Donald Trump's tax reforms.

Starbucks' Howard Schultz argues US cities will be hit by an 'abundance of empty storefronts'

Agents say that the fate of the retail property sector is largely in the hands of its owners. CBRE reports that owners of less attractive malls are devising new features to attract consumers such as pop-up shops, short-term leases and co-working spaces.

Likewise, consultancy Jones Lang LaSalle says that retailers are "adapting and re-evaluating" their physical retailing space in response to ecommerce pressures. Property owners, too, are investing "to create attractive mixed-use destinations for a new kind of consumer".