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WWD

May 13, 2015

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While facing challenges from Internet and mobile commerce, shopping center developers are looking for innovation and experiential retail as they head into the International Council of Shopping Centers annual conference next week. Additionally, pockets of retail — from the overall travel sector to neighborhoods in Paris and Los Angeles — are percolating with new activity and restoration.

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Onward, Upward

Retail development is headed to new heights — in both construction and rent — as retailers strive to innovate to keep shoppers coming in.

By **SHARON EDELSON**

THINGS ARE LOOKING UP FOR THE shopping center industry – literally. With a dearth of available land for new ground-up projects, developers such as Howard Hughes Corp., are thinking vertical. "We have almost 50 million square feet of vertical entitlements," said chairman and chief executive officer David Weinreb, calling the company's Ward Village Gateway project in Honolulu "a master plan village in the sky.

Shopping center owners and developers tend to have a glass half-full mentality, which allows them to think big and see complex projects through the endless government approvals process. But with the International Council of Shopping Centers' ReCon conference in Las Vegas, May 17-20, along with the requisite glad-handing and deal making, there could be issues clouding the glass, including rising interest rates, sharply escalating asking rents on major retail thoroughfares, the fate of C and D malls, and the long-term implications of the 800 pound gorilla in the room that is Internet and mobile shopping.

"It seems like there's a lot of focus on consolidation," said International Council of Shopping Centers president Michael Kerchaval. "It's not about building. It's very challenging to get growth. They'll get it through acquisitions and consolidation and partnerships."

Shopping centers are treating lemons – the result of a bigger than usual crop of bankruptcies, downsizings and liquidations – like fresh meat. Don Ghermezian, president of Triple Five Group, said, "We start marketing spaces, going behind the scenes when we sense weakness. What you're finding is retailers that overexpanded are scaling back."

The retail industry is nothing if not Darwinian. "Clearly, on the specialty side of the business we lost retailers," said David Simon, chairman and ceo of Simon Property Group. "The ones going away are weaker. There's a whole host of stronger ones in the pipeline that we expect to add excitement to our properties."

Simon's strategy for recapturing space includes a joint venture with Sears Holding Co. Other retailers could "take advantage of their inherent real estate value," said Richard Sokolov, president of Simon. "If they're thoughtful about how they want to take advantage of the real estate, I'm sure there's value to be made for their shareholders."

Still more bankruptcies are expected this year. "It's difficult for teen retailers," said a shopping center executive. "You have one bad season and it's very difficult to convince kids that you're cool. Abercrombie & Fitch went from doing $1,800 in sales per square foot to $400 per square foot to $200 per square foot. It's been an incredible descent."

"Very quietly, every big box user is considering what it can do," Kerchaval said. "Stores are recognizing they don't need as much selling space. They can convert some space to distribution for omni-channel fulfillment or consolidate even farther. You're seeing these conversations running the gamut of retailers."

Similar conversations are taking place between retailers and owners of urban property. "We had Diesel as a tenant at 685 Fifth Avenue and the corner of 54th Street," said Joseph Sitt, chairman and ceo of Thor Equities. "I gave them money to buy them out. Richmont signed a deal for all of its brands for just above $4,000 per square foot. So many retailers want Fifth Avenue. There's an intensity from Asia."

There are concerns that rising rents and diminishing supply could rupture the real estate bubble. "Rents have escalated very quickly over the last few years," said Jedd Nero, principal and executive managing director of retail services at Avison Young. "There comes a point where retailers can't make a profit. This is really starting to be apparent. Landlords don't really want to understand that. It's very hard to justify the rents."

But Robin Abrams, executive vice president of Lansco Corp., said prices are beginning to ease. "Retailers held back. A lot of them were looking, but the pricing was overly aggressive. We're starting to see prices leveling off and landlords are more flexible in order to now execute deals," she said, noting that 650 Fifth Avenue, the Juicy flagship, and No. 636, the Faconnable store, are both on the market.

East 57th Street between Fifth and Madison Avenues, once the most expensive retail thoroughfare in the U.S., "is in huge transition," Abrams said. "The stretch between Fifth Avenue and Madison which was considered prime. Now it's not as strong a retail corridor as those avenues." Niketown's site at 6 East 57th Street is on the market as is Geoxx's store at 575 Madison Avenue at 57th Street.

Amid the changes, longtime 57th Avenue denizens Chanel and Dior are said to be looking for new digs. "It will be interesting to see what the new owners of the Crown Building do," Abrams said, referring to General Growth Properties and partner Jeff Sutton's $1.75 billion purchase of the building's retail component, which set a record. The owners are looking to expand the retail square footage and experts estimated asking rent of $3,500 per square foot.

"A lot of great retailers on Fifth Avenue and in Times Square are looking for lots of traffic, but can't afford the rents. I don't believe those rents are at all sustainable," said Ghermezian, whose company is planning a Miami Dream "down the road." Casualties of the high occupancy costs include Toys 'R' Us, which is leaving its prominent Times Square flagship. F.A.O. Schwartz will close its store at 767 Fifth Avenue and 58th Street.

Isaac Chera, a principal at Crown Acquisitions, which owns property in Manhattan and Brooklyn, said, "Rents have increased because foot traffic and business is there. The Internet is a big part of it. It gives retailers coverage and gives them the global prices that they look for. The folks that are doing the business, such as Apple and Zara, can afford to pay for it. It's about their ability to business to capture that traffic."

Some malls are treating fast-fashion giants such as Uniqlo and H&M as "mini anchors." The latter is expanding its COS and & Other Stories brands. "L Brands is now looking for locations for White Barn," Sokolov said. "Victoria's Secret is still expanding, and [sub-brand] Pink is still growing."

Sokolov also cited Hanna Andersson, a former

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– DAVID SIMON, SIMON PROPERTY GROUP

catalogue for clothing made from natural and/or organic fibers, and Altar'd States, a fashion brand with a wholesome backstory, and the mission statement "...we stand out for good to glorify God."

"There are now aggressive brick-and-mortar expansions in the 'feel and look good' category, including Soul Cycle, Blue Mercury, Athleta and Lululemon," said Peter Ripka, cofounder of Ripco Real Estate. "Deals in all these categories will be pushed forward at the convention."

Greg Miles, chief operating officer of Westfield Corp., agreed. "Health and beauty is still very much a growing category," he said. "Major cosmetics brands are doing more standalone stones. Kiko Milano and Aesop are finding a niche."

"Web-only companies looking for physical space is another growth opportunity we're pursuing," Sokolov said. "All of the companies start with tests."

"The market is active, space is tight and rents have gone up in all forms of retail real estate – regional malls shopping centers and urban areas," Ripka said, adding that reasons include the fact that "the better retailers have learned how to benefit from e-commerce overall and not fear it."

E- and m-commerce retailers are smarter about opening stores than their brick and mortar predecessors. "They have more knowledge of where their customers are than 30 years ago," Miles said. "I don't think you'll see many retailers create networks like the Gap." Bonobos and Warby Parker are in Westwood centers, and Nasty Gal "is looking to open more stores as well. We'll see a continued roll out but in a much more measured way."

"Technology forces retailers to be creative," Nero said. "For example, it's enabling customization of everything from clothing to shoes. Shoppers want stuff that isn't just off the rack. Three-D printing is also going to bring people into the stores. Instead of the Gaps of the world sitting back and living off the success of years ago" retailers are being forced to innovate.

"We're exited about our same day delivery service," said Ghermezian, adding that it's offered at the company's gargantuan Mall of America and Mall of West Edmonton. The long-awaited American Dream will have an IT budget in the "tens of millions," he said.

Westfield on May 28 will launch Bespoke, an environment in downtown San Francisco replete with event and technology demo space that will encourage collaboration with start-ups and makers and will host fashion runway shows and hackathons under its dome. "It's where people can test and trial and innovate," Miles said.

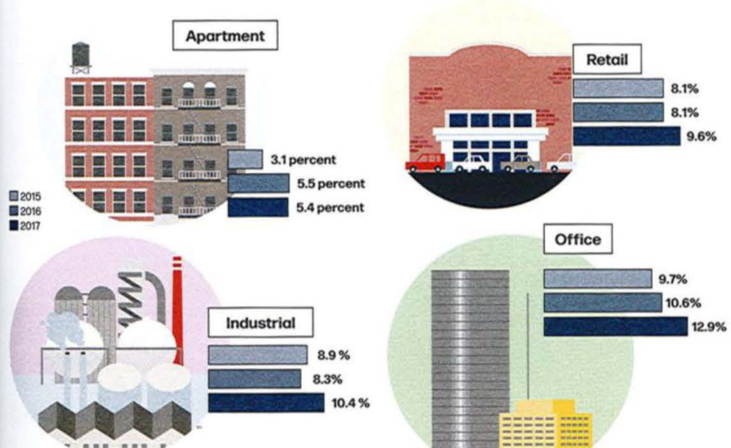
Howard Hughes is taking advantage of its vertical entitlements at its Seaport District project, where it plans to build a controversial 42-story residential tower. The company is rebuilding Pier 17 and constructing a four-story glass building with food and retail and entertainment on the roof.

Downtown Summerlin, Howard Hughes' "if you build it they will come" project in the desert, is nine miles from the Las Vegas Strip and part of a 25,000-acre master plan community that includes a 106-acre, 1.6 million-square-foot mixed use open air development with over 125 stores and restaurants that opened in the fall.

Weinreb said Hughes will pursue a similar strategy to find emerging talent for Summerlin as it did at the Seaport through its partnership with WWD, which identified up-and-comers through "The 10 of Tomorrow."

Brookfield Properties has a similar idea for Manhattan West, a seven million-square-foot development one block west of Penn Station and the proposed 7 subway train extension that sits at the gateway to the larger Hudson Yards project that Neiman Marcus will anchor. "We want to get that neighborhood feel," said Jerry Larkin, executive vice president and director of leasing. "We'll be looking for less of a mall tenant and more of a mom and pop retailer."

U.S. vacancy rates forecast for commercial property



SOURCE: STATISTA

Milan Galleria

COMMONLY REFERRED to as "the parlor of Milan" by the Milanese, the city's sumptuous Galleria Vittorio Emanuele II, one of the oldest shopping arcades in the world, has returned to its original grandeur, thanks to investments by Prada and Versace. The two fashion houses, along with the city government, injected more than 3 million euros, or $3.4 million, to finance the restoration work.

First completed in 1867, the Galleria Vittorio Emanuele, which was designed by architect Giuseppe Mengoni to connect Piazza Duomo with Piazza Scala, recently fell into a state of neglect, which was a poor match for the elegant and sophisticated allure of the several luxury stores present there, including Prada, Versace, Gucci, Louis Vuitton, Giorgio Armani, Tod's, Church's and Borsalino, among others.

Timing was also key: The decision to invest in restoring the galleria was spurred by the onset of Expo 2015.

Following a year of work – which was facilitated by an overhead traveling crane allowing teams to work during the day without obstructing regular store activity – the Galleria reflects a look more loyal to its original style. Sixteen teams – 12 working during the day and four at night – completed the project, which was mainly focused on cleaning and dusting the stone elements and restoring the plaster.

"The biggest challenge was to recognize the original parts," said architect Marco Sobrero, technical director for the restoration firm Gasparoli. Sobrero explained that many interventions have been made on the Galleria through the centuries. Two years after it was built, a violent hailstorm broke the glass ceiling, causing rain to pour into the Galleria and the chalk and plaster parts to disintegrate. In addition, bombs dropped during World War II damaged the site in 1943.

"We discovered that the original color was very different from the existing one," said Sobrero, pointing out that the current white tone, which was replaced by yellow before the restoration, was the hue originally chosen by Mengoni. – ALESSANDRA TURRA