KEEPING OUT OF THE MIDDLE

Many believe the retail market is not bottoming out, so much as its middle is shrinking. California's shopping center owners and tenants are attempting to differentiate and move out of what was once considered the comfort zone.

By Nellie Day

Being in the middle seems to arouse an emotional response from many people. Some prefer to blend in with the crowd, neither being too high or too low on any given measurement scale. Others want to stand out, creating personalities and characters that display notoriety or infamy and make them outliers in one direction or another.

Many traditional malls, tenants and property owners enjoyed decades situated within this cushy zone, never needing to be the top sales producer or nicest establishment. None of that mattered. Location was what mattered. Being the closest mall with a JC Penney or neighborhood center with an Albertson's almost guaranteed a monopoly on the surrounding trade area. And if the customers didn't like it, what were they going to do? Were they really going to drive two districts over just to frequent the same stores? Or were they going to simply stop shopping altogether, just hoping toilet paper would magically appear at their front door?

Oh, how times have changed.

KTGY recreated the 758,504-square-foot Shops at Montebello for Simon to create a new experience for shoppers.

CULPRITS OF CHANGE

"There's no doubt the retail landscape is changing," says Christopher Thornberg, founding partner in Los Angeles-based Beacon Economics. "Anybody who pretends otherwise is just ridiculous. We live in a new world. The idea is you have substantial changes in the underlying dynamics of an industry, and that leads to changes regarding how things are done."

And change, things have. California lost more than 7,000 retail jobs during the first half of 2017. Many of these losses were due to the 76 store closures that occurred over that same time period in the state, according to the Employment Development Department. This number was up 15 percent compared to 2016 when California saw 66 stores shutter. These job and store losses were felt as Bebe, Gymboree, American Apparel, Sport Chalet and Sports Authority closed up shop throughout the state and, sometimes, the nation.

Then you have Limited Stores Co., which filed for bankruptcy earlier this year, announcing it will close 250 stores nationwide. Payless ShoeSource followed suit in April, announcing it would close about 400 stores, 50 of which are in California. One-time mall staple JC Penney closed 138 stores at the end of summer. The list can — and does — go on and on. From Sears and Kmart to

Forever21's F21 Red concept store has big expansion plans to capture consumers who want to spend less.

Westfield invested $1 billion to recreate Century City, a plan devised to keep the center at the top of the charts.

Office Depot, Abercrombie & Fitch, BCBG, h.h. Gregg, Aeropostale and Pier 1 Imports, retailers of all sizes and in all categories appear to be dropping like flies.

Garrick Brown, vice president of retail research for the Americas in Cushman & Wakefield's Sacramento office, cautions, however, that things aren't always as they appear. He believes a little perspective is in order before we reach for the panic button and start polishing our truck driving skills before applying to Amazon.

"Anyone who says the sky is falling is missing the boat," he says. "Online shopping gets all the press — and it's definitely the biggest cause of closures — but not every retailer that's going down is going down because of that."

Brown cites a variety of reasons for this shakeup, including shifting consumer patterns brought on by Millennials, a race to bottom-of-the-barrel pricing with discount stores that are stealing market share, debt hanging over the heads of retailers like Toys "R" Us and Borders and just too many cooks in the kitchen.

"Pure and simple, we were over-retailed," he states. "No other country even came close. We have about 13 billion square feet of retail real estate and 360 million residents. That comes out to a lot of retail square footage per person. We're twice as retailed as Canada and the United Kingdom. All we needed was some sort of disruptive force and the market was going to be vulnerable. This turned out to be a monstrous disruptive force."

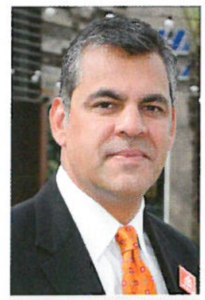
This monster is, of course, ecommerce. Though the advent of online shopping has been a "monstrous disruptive force," like Brown, Thornberg urges people to choose perspective over panic before letting these figures get too far into their heads.

"It's not as if somehow non-store competition didn't exist before," Thornberg notes. "It's just that the internet is making it more intense than it used to be. Customers have two options: I can sit at my desk and buy something or I can sit in your plaza and buy something. What are you going to do to shift that balance to you? To make people want to make the effort to go to your establishment? That's how you're going to win."

Brown believes stand-out quality, not quantity, will be more important than ever going forward as retailers shutter their shops and give back more space.


Christopher Thornberg
Founding Partner
Beacon Economics

"The middle has eroded in retail," he says. "The flipside to all these closures is that if you're an Abercrombie & Fitch or a Burberry that's going from 1,200 units to 600 units, the weird irony is that the stores you keep open are more important than ever before."


Ken Hira
Executive Vice President
Kosmont Companies

Brands like Abercrombie, which would be considered a mid-level retailer, and Burberry, more of a high-fashion house, must differentiate themselves on experience and high-quality merchandise if they're to capture the top spenders and what is left of the disappearing middle class.


Garrick Brown
Vice President of Retail Research for the Americas
Cushman & Wakefield

"The retail industry is having the same problem as the middle class," Brown explains. "The middle class is being squeezed. Some are moving up the ladder, and some went backwards. The people at the top are spending more, the people at the bottom are very price sensitive."

This is where dollar stores, online shopping and fast-fashion retailers like Forever 21 can really swoop in. The Los Angeles-based women's, men's and kid's clothing and accessories retailer is already known for its low prices, but its F21 Red concept takes this value even further. With that in mind, it's no surprise to learn F21 Red will open more than 40 new stores by the end of 2017. The chain already boasts eight stores in California, with the newest one being a 20,706-square-foot location at 3535 Sports Arena Blvd. in San Diego that offers t-shirts for $3.90 and camisoles for $1.90.

"We are excited to be growing F21 Red's presence in 2017," says Linda Chang, vice president of merchandising at Forever 21. "F21 Red expansion represents an important and exciting opportunity for our growth plan, and will allow us to bring a wide variety of product at competitive prices to new regional areas for our increasing customer base."

Vintage Real Estate worked with KTGY to redevelop SouthBay Pavilion in Carson.

HARBINGERS OF CHANGE

Naturally, not all retailers can compete with an outlet that sells tank tops for less than the price of a venti pumpkin spice latte at Starbucks. This is why the focus on the surviving stores is so important. That focus begins with the store's location, proving that not everything we knew about retail has changed.

"What's essentially happened is just like everything else where the middle has eroded, in the mall and shopping center worlds, we're seeing a huge gap between performing assets and underperforming assets," Brown says. "The strong has gotten stronger, the weak has gotten weaker. You still want to be in the best locations and shopping centers."

Thornberg considers centers like Caruso's the Grove in Los Angeles and the Americana at Brand in Glendale to be a few examples of California's best in class. This is due to a very fundamental reason — one that is critical for shopping centers to survive in the age of Amazon.

"What you're seeing out there today is how these guys respond to changes in underlying dynamics," he says. "They're figuring out what to do when the Sears and Macy's leave. The Grove and Americana are packed to the brim with people. They're doing fantastic because they offer lots of restaurants and fun retail in the midst of an environment that people like to be in. When you scratch away at the surface, what everyone recognizes is that destination retail supported by sectors that don't compete with the internet are doing great."

The question of what to do when that big box anchor leaves can be a large one, but it can also be an opportunity. Simon Perkowitz, a principal at KTGY Architecture + Planning in Irvine, believes no idea is too far-fetched to consider when it comes to repurposing a large space. Instead, he adheres to the approach of leaving no consideration unturned, even if that means the use is no longer pure-play retail.

"What you do with a vacant big box is a very complex decision," he says. "There are many paths that lead to failure and very few that lead to success. Do you tear down the building and build something from the ground up or repurpose it to give it a new life? Do you divide up the retail space to accommodate multiple tenants, or push out beyond the walls to create a multi-use environment that might include residential, hotel, shopping, dining and/or office uses?"

PEAK PERFORMANCE

Brown likes the idea of adding entertainment- and service-based tenants like Punch Bowl Social, Lucky Strike and Dave & Busters to centers. He has a word of caution for these companies, however, before they let their popularity with landlords go to their heads.

"Even though concepts like these will be welcomed with open arms by shopping center owners that are hurting and need to plug in someone like you, you still want to be in those trophy centers yourself," he says. "You can't just stick with malls and you should stay away from neighborhood centers. It comes down to quality. Quality centers will be fine. You're going to pay for it and you're going to get lower returns, but these will be your bullet-resistant properties even as closures peak over the next year."

At Nordstrom's new Century City store, there are several showplaces within the store, including this Givenchy handbag boutique.

And Brown sees quite the peak. He estimates the nation will experience 9,000 store closures by the end of this year, a 125 percent increase over 2016. Brown believes next year's number may be closer to 13,000, likely due to one very large player.

"At least one major department store chain will go down next year," he predicts. "It will trigger a round of strategic closures like we've never seen before."


Designed to entertain and enlighten the senses: the men's department at Nordstrom in Century City doesn't look like your typical department store.

The ripple effect of that could trigger co-tenancy clauses, which issue "get out of jail free cards" to tenants that may have been looking for one, Brown says.

"There may be 700 malls with players like Victoria's Secret and Gap that want to close stores and get out of their leases, and they just may have found a way," he continues.

As the traditional retail landscape further contracts, Brown believes a focus on other issues will be key.

"Those properties will have to be reinvented as something else," he says. "They could still be retail, but they won't be super-regional malls. A 1-million-square-foot super regional mall will come back as a 400,000-square-foot lifestyle center with office and medical uses. It will be rebirthed as mixed-use with a retail component."

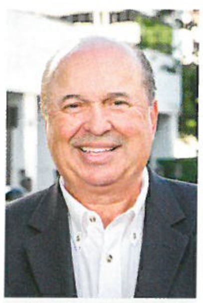
Ken Hira, executive vice president of Kosmont Companies in Manhattan Beach, believes a variety of uses will be necessary to not only fill these vacancies, but provide shoppers with an incentive to leave their homes.

"The California shopping center should be thought of as a 'blended-use' opportunity site that can be repurposed with food, fitness and entertainment, along with residential, office and hospitality uses," he says. "Google and Amazon also embrace the brick-and-mortar formats — target them as next-generation retailers and/or last-mile 'click and collect' options."

This was part of Westfield's strategy when it invested $1 billion to position Westfield Century City as its flagship property for the next generation of shoppers. The 1.3-million-square-foot center features internet-proof concepts like Equinox gym; medical uses like UCLA Health Clinic; a variety of food offerings like the first West Coast Eataly; a 1,100-square-foot pop-up space for revolving concepts; partnerships with the Annenberg Center for Photography and the Los Angeles County Museum of Art; shop-in-shop experiences like the Nordstrom x Nike sneaker boutique and SPACE inside the new three-level, 154,000-square-foot Nordstrom; and brick-and-mortar spaces for ecommerce companies like Amazon Books, Bonobos and Warby Parker.

Brown asserts Westfield Century City was a stand-out in Los Angeles, seemingly operating at the top of its game, before it decided on this massive undertaking. However, its latest efforts will ensure this property remains at the top, rather than blending into the middle of the pack.

"Westfield Century City is a top five mall per square foot," he says. "It has been in the past five to six years. But they still spent all this money on renovation. They realized they were dominant already, but they said 'we want to have unquestionable dominance.'"



Simon Perkowitz
Principal
KTGY Architecture + Planning

Even if you don't have an extra $1 billion lying around, Brown believes reinvestment and reinvention are the keys to success for shopping center owners all over the state. Perkowitz has seen this first-hand as KTGY has been called upon to makeover centers throughout the Southland. This includes Vintage Real Estate's 1.1.-million-square-foot Southbay Pavilion in Carson and Simon's 758,504-square-foot the Shops at Montebello in Montebello. Both assets were enclosed malls in need of something fresh.

"KTGY used textured walls, up-lighting and clean, open storefronts to create a contemporary space that feels up-tempo and is easy to navigate when it reimagined Southbay Pavilion," he says. "The Shops at Montebello needed a facelift. The façade renovation brings an inviting and contemporary aesthetic to the center with enhanced entryways, landscaping and signage. The outdoor seating and extensive glazing activate and enliven the once-enclosed mall."

The exterior of the new Westfield Century City in Los Angeles.

The centers also focused on adding new tenants, while honoring their current tenants throughout the reinvention process. Southbay Pavilion's new look attracted the attention of F21 Red, which opened a new 17,000-square-foot store at the center. KTGY assisted the center with store branding for new retailers to the site. This included large, contemporary letters and clean lines to create visibility for the F21 Red store from both the curb and inside the enclosed retail center. The exterior entry design incorporated stone veneers, metal louvers and wood siding. New flooring and restroom updates that made them more comfortable and accommodating also helped Southbay Pavilion nab ever-important food outposts, including Wing Stop and Chile Verde Mexican Food.

The food court was similarly redesigned at the Shops at Montebello, which improved connectivity between the mall and the food service and dining areas. Simon also renovated H&M's space, which included the interior demolition of existing smaller multi-tenant suites to create a 3,285-square-foot expansion. This provided H&M with a new space totaling 21,579 square feet.

Perkowitz acknowledges it is a very crucial time for shopping center owners as they make decisions about the future of their centers based on all the change taking place nowadays. He also believes, however, that this is a great time for, well, greatness.

"I think that the adage of 'when one door closes, another one opens' is very fitting here," he says. "There are always opportunities for those who are willing to see how the retail landscape is changing and are willing to evolve with it — and even better for those who can anticipate it."

Even if you can't anticipate all the changes set to grasp the retail industry, Brown believes you should approach the upcoming year with an open mind — and perhaps an open wallet.

"You should have a willingness to explore new strategies," he says. "Everything from grocers to discount to expanding food and entertainment options. Definitely don't shy on upgrading. Create better experiences for your consumers. You have to give them a reason to come to your center today. It's not like the old days were you could have 1,600 malls across America that are very cookie cutter. You must differentiate. That's part of the new retail world."

Welcome to the new world. **CC**