Q4 2019
Retail First Glance

Pre-Release Analysis of Fourth Quarter 2019 Moody's Analytics REIS Findings in the Retail Sector

RETAIL NUMBERS START TO TURN NEGATIVE

As major department and other stores have closed over the last two years, many have anticipated reports of soaring vacancy rates and plummeting rents. Yet the data has shown otherwise, defying the anecdotal reports of a retail apocalypse. This is largely due to new tenants occupying the vacated space including trampoline parks, fitness companies, new grocery stores and other users.

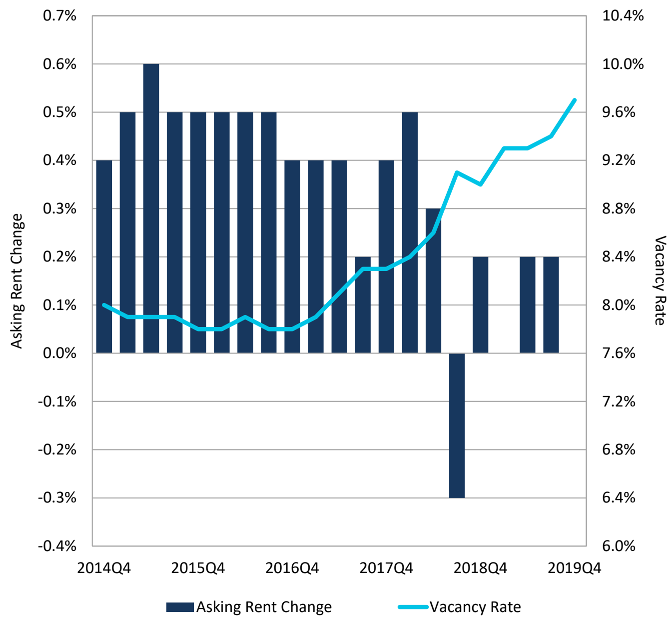
The year-end 2019 REIS data, however, indicates that the balance between stores closing and tenants leasing new space started to tip toward added vacancy: net absorption for neighborhood and community shopping centers was negative 3,000 SF, and the mall vacancy rate increased 0.3%. The REIS inventory shows 16 Kmart closings in the fourth quarter in 13 separate metros. At the same time rent growth for retail was 0.1% in the quarter – the lowest since 2012 – and the average mall rent was unchanged. Given these numbers, one cannot help but wonder if this was the start of the retail downturn or was it simply one weak quarter.

NEIGHBORHOOD AND COMMUNITY SHOPPING CENTERS

Not since the second quarter of 2018 has the neighborhood and community shopping sector incurred negative net absorption. Still, with the 16 Kmart closings totaling negative net absorption of 1.48 million SF, the final net of a mere -3,000 SF shows that new tenancy nearly offset the Kmart closings – a story we have repeated most quarters. The REIS internal leasing tracking shows new occupants in these centers include fitness centers, grocery stores, home furnishing stores and trampoline parks.

Despite the decline in occupancy in the fourth quarter, the vacancy rate rose only 10 basis points to 10.2% as new supply was tepid, as well. The vacancy rate also stood 10.2% a year ago.

REGIONAL AND SUPER REGIONAL MALL VACANCY AND RENT TRENDS



As mentioned in previous quarters, the national numbers conceal a wide gap between metros with positive absorption and those with negative: 35 metros saw negative net absorption in the fourth quarter, up from 33 last quarter. For the year, 26 metros show negative net absorption, and 32 metros have a higher vacancy rate as some added more inventory than was absorbed.

Construction in the neighborhood and community shopping center space was 732,000 SF, down from 1.4 million SF added in the third quarter. In the fourth quarter of 2018, construction was 2.8 million SF. These lower numbers reflect the caution from both developers and lenders that most metros are still over-retailed. In 2019, only 5.4 million SF was added to inventory, which was 46% lower than the 10.0 million SF added in the 2018. Only 6 metros saw new construction in the quarter led by Houston, Columbus, Birmingham, Denver and Greensboro/Winston-Salem.

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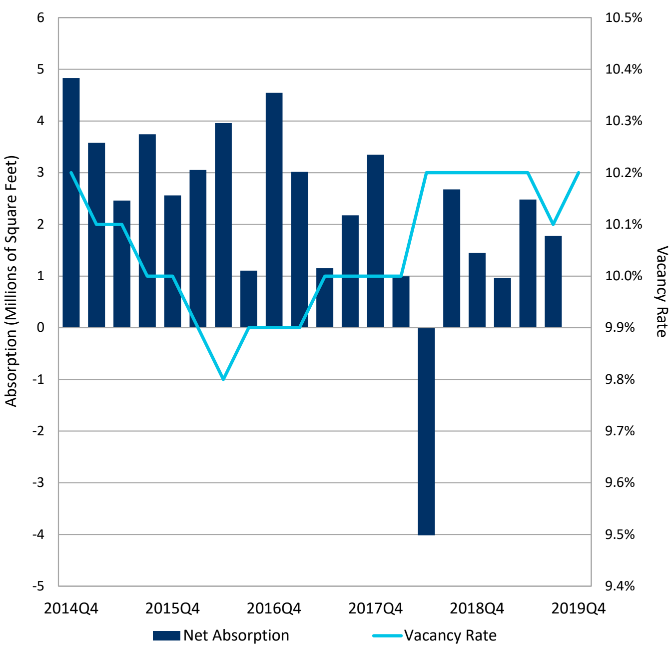
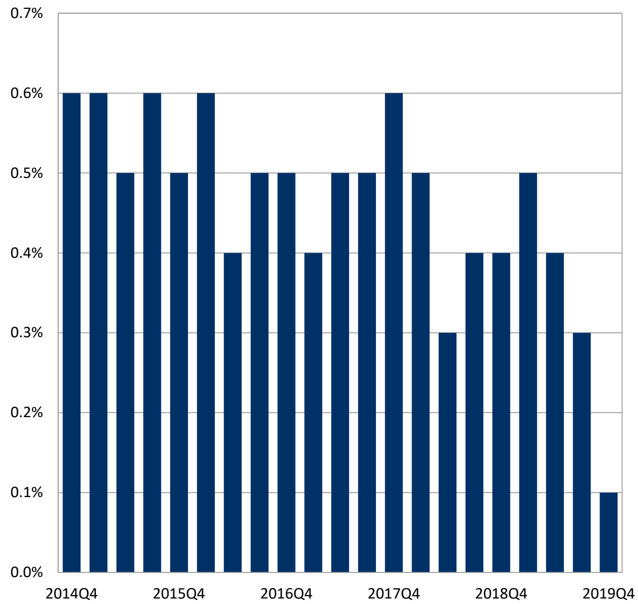
The average neighborhood and community shopping center asking and effective rent increased 0.1% in the fourth quarter. At $21.48 per SF (asking) and $18.82 per SF (effective), the average asking and effective rents have increased 1.2% and 1.3%, respectively, since the fourth quarter of 2018, well below the rate of inflation. The low but positive rent growth seems surprising given the uncertainty surrounding the retail sector, but the average growth rates represent a net of all the

NEIGHBORHOOD AND COMMUNITY SHOPPING CENTER NET ABSORPTION AND VACANCY



NEIGHBORHOOD AND COMMUNITY SHOPPING EFFECTIVE RENT GROWTH



REGIONAL MALLS

At 9.7%, the national mall vacancy rate is the highest in ten years. The average rent, however, was unchanged in the fourth quarter at $43.53 per SF. The average mall rent has grown 0.4% over the year and 2.7% cumulatively over the last three years. Still, anecdotal reports have been dire, far more so than these numbers. Many Macy's and other large department stores are owner-occupied and are often not included in the REIS mall inventory. Still other malls have sold large anchor spaces to developers, converted spaces to self storage, or leased the space to a trampoline park or entertainment company. These new uses for big box spaces have kept rents from falling dramatically.

STATISTICS BY METRO

Although 31 metros saw a quarterly increase in vacancy, most were less than 1.0%. These were mainly due to negative net absorption as mentioned above. Metros with the largest increase in vacancy for the quarter include Syracuse, Columbia, Pittsburgh, Long Island, Charlotte and Norfolk. All had a vacancy rate increase of 0.5% to 1.6%. Metros with the biggest drop in vacancy include Albuquerque, Tacoma, Fairfield county, Salt Lake City and St. Louis. These metros saw vacancy rate declines of 0.4% to 0.5%.

Similarly, the number of metros that posted a rent decline in the quarter increased to 31 from 15 in the previous quarter. Metros with the sharpest effective rent decline include Chattanooga, Fairfield County, Central New Jersey, Greensboro/Winston-Salem and Dayton which had rent

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declines of 0.7% to 1.0%. The metros with the highest rent growth were Seattle, Hartford, Tacoma, Birmingham and Palm Beach that each had rent growth of 0.8% to 1.1% in the quarter. For the year, eight metros show a rent decline, up from two metros in the third quarter. Metros that saw the strongest rent growth in the year were Nashville, Seattle, Raleigh-Durham, Sacramento and Salt Lake City.

OTHER RETAIL MEASURES

The retail sector ended the year on a positive note, adding 42,800 jobs in the fourth quarter. That said, retail shed a net 34,000 jobs in all of 2019. Clothing and accessory stores saw the biggest loss in the year with 40,000 fewer jobs (-2.9%), followed by department stores with 25,000 lost jobs. Grocery stores added 37,000 jobs in 2019. Dwarfing these gains, restaurants added 290,000 jobs in 2019, a growth rate of 2.4%. Also, fitness and recreation companies added 23,000 jobs (3.6%) and sports teams and personal services added 25,300 jobs (1.7%).

The metro retail employment statistics are somewhat consistent with the occupancy statistics in that 57 metros shows a year-over-year loss in retail jobs as of November. Those that lost the most jobs include Columbus, Tucson, New Haven, Cleveland and Las Vegas. Those that added the most retail jobs in 2019 include Charleston, Colorado Springs, Columbia, Knoxville and Greensboro/Winston-Salem. Only 60 of the 80 metros tracked by Reis | Moody's Analytics have a reported restaurant employment number. Of these, 10 show a year-over-year loss in restaurant jobs, but many show strong restaurant gains including Suburban Virginia, Tacoma, Milwaukee, Salt Lake City, Dallas and New Orleans.

The Census statistics on retail sales shows a mixed picture as e-commerce sales grew nearly 13% in 2019 over the same period in 2018 (January through October). Yet declines were significant in sporting goods stores (-2.8%), electronics (-4%) and department stores (-4.9%). Health and drug stores (+3.4%) along with grocery stores (+3.0%) show healthy gains in 2019, as do restaurants with sales growth of 4.3%. In sum, the aggregate real-estate-using retail sales (that nets out e-commerce, gasoline and automobile sales but adds restaurant sales) shows a year-over-year gain of 2.1% which is consistent with the positive occupancy growth. In fact, real-estate-using retail sales has grown consistently over the last few years, and this does not include sales for fitness companies or personal services like salons or dry cleaners.

RETAIL OUTLOOK

The retail sector had its weakest quarter in nearly two years as net absorption was negative due to significant closings of Kmart stores. In addition to the 16 Kmart closings mentioned above in primary metros, another ten Kmart stores in tertiary markets closed yielding 1 million SF of negative net absorption. Yet despite this heavy blow, the vacancy rate was flat for neighborhood and community shopping centers.

As we continue to track new leases in our inventory, our data shows that grocery stores, home and houseware stores and fitness centers continue to lease space as well as trampoline parks, but fewer than in the past. Thus, the fourth quarter could mark the turning point when the sector truly started a downturn, or it may have suffered one weak quarter. Consumption growth

Fourth Quarter 2019 Market Performance

Improving Fundamentals / Flat or Declining Fundamentals

	Absorption	Occupancy	Effective Rent
Q4 2019	45+ / 35	31 ↑ / 49	48 ↑ / 32
Q3 2019	48 + / 32	36 ↑ / 44	58 ↑ / 22
Q2 2019	54 + / 26	35 ↑ / 45	61 ↑ / 19
Q1 2019	41 + / 39	36 ↑ / 44	61 ↑ / 19
Q4 2018	47 + / 33	33 ↑ / 47	62 ↑ / 18

Figures are based on 80 metro markets

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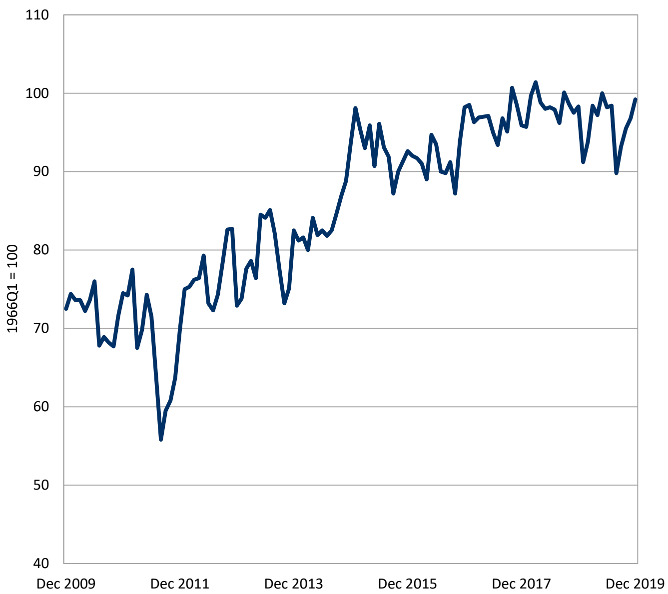
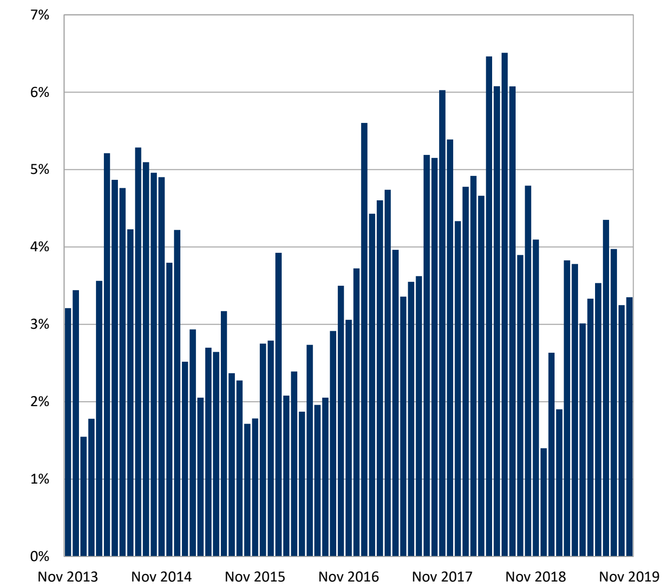
remains healthy, but it is hard to ignore the acceleration in e-commerce sales. Our outlook is less favorable than it has been, but we foresee only slow-moving changes to the vacancy rate and rents over the next year.

UNIVERSITY OF MICHIGAN CONSUMER SENTIMENT SURVEY



Source: FRED, University of Michigan

12-MONTH CHANGE IN RETAIL AND FOOD SERVICE SALES



Source: U.S. Census Bureau

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