United States Retail Outlook

Q3 2023

Limited supply a drag on leasing activity

JLL SEE A BRIGHTER WAY

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Executive summary

- Despite the headwinds presented by high interest rates and concerns over inflation, retail sales continue to see month-over-month gains heading into the holiday season. Sales rose for the sixth straight month, increasing 0.7% from August.
- Demand remains on par with levels seen during the first half of the year. The primary constraint on leasing activity is the lack of available space in desirable locations. Retailers are also facing higher operating costs, a dearth of labor and higher interest rates.
- Retail real estate is experiencing a significant shortage of available space, due to limited new deliveries and 145 million square feet demolished in the last five years. The availability rate is nearly 200 basis points below its historical average of 6.8%.
- Outside of entity-level transactions the capital markets were relatively consistent with Q2. Preliminary estimates of transaction volume (excluding entity-level) were roughly $9.9 billion, a slight decrease over the previous quarter and a 40% decrease over Q3 2022.
- Some traditional mall tenants have announced plans to relocate some of their mall stores to open-air neighborhood and community centers with higher foot traffic.
- New power center deliveries are still considerably lower than they were 15 years ago, during the great recession. Q3 2023 deliveries were less than 5% of their Q3 2008 levels, which is why vacancy is some 100 basis points below what it was and why rent gains, while moderate, remain steady.

Economic and retail RE fundamentals

U.S. retail economy trends

Inflation

3.7% ↑

While the consumer price index growth has moderated to 3.7% above year-ago levels, the cumulative jump in prices since 2019 paint a clear picture: it takes more money to buy the same things now. This impacts lower-income shoppers significantly more than those earning more money.

Consumer sentiment

63.0 pts ↓

Consumer confidence fell 5.1 points from September to October, thanks to growing consumer concerns over inflation. However, overall sentiment remains comfortably above what it was in September of 2022, when inflationary growth was markedly steeper.

Retail sales

0.7% ↑

Retail sales grew for the sixth straight month in September, jumping 0.7% over August and 3.8% year-over-year. While most of this growth can be attributed to inflation, categories that showed particular strength included auto dealerships, F&B places and miscellaneous retailers.

Retail fundamental statistics Q3 2023

Fundamentals	General retail	Malls	Power centers	Neighborhood and community	Strip centers	Total retail
Inventory	6,470,520,261	910,494,494	799,759,285	2,981,669,141	706,491,027	11,973,152,202
Vacancy	2.5%	9.1%	4.3%	6.0%	4.7%	4.2%
Net absorption	8,434,857	(434,694)	235,521	1,478,262	518,412	10,474,337
Net deliveries	5,365,351	194,870	444,984	1,044,393	349,486	7,421,783
Under construction	42,781,436	3,339,962	1,826,431	8,003,646	2,922,429	60,084,408
Market rent	$23.62	$32.94	$26.21	$23.60	$22.40	$24.48

Retail supply and demand at odds

U.S. retail RE fundamentals snapshot

1

Demand

Demand remains on par with levels seen during the first half of the year. The primary constraint on leasing activity is the lack of available space in desirable locations. Retailers are also facing higher operating costs, a dearth of labor and higher interest rates.

2

Rents

While rent growth is moderating from the highs seen in 2022, market rents are still increasing, buoyed by the scarcity of desirable space in strong markets.

3

Supply

Retail construction activity remains at a minimum due to soaring costs. As a result, retail availability is nearly 200 basis points below its historical average of 6.8%. The lack of desirable supply is expected to persist given low construction starts and a modest but steady demolishment of obsolete retail space.

4

Capital markets

Outside of entity-level transactions the capital markets were relatively consistent with Q2. Preliminary estimates of transaction volume (excluding entity-level) were roughly $9.9 billion, a slight decrease over the previous quarter and a 40% decrease over Q3 2022.

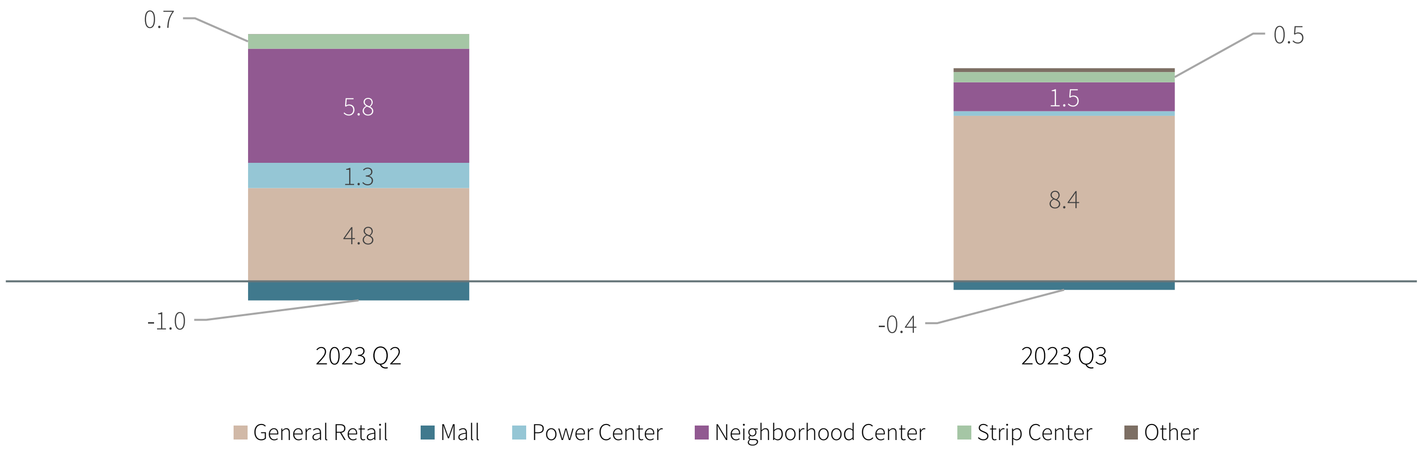
Demand shifts to freestanding retail space

Net absorption totaled 10.4 million square feet in the third quarter, declining 10.2% from the prior quarter. The proportion of space taken by each retail property type also shifted radically between the second and third quarter.

General/freestanding retail absorption doubled from the previous quarter, while power center absorption fell nearly nine percentage points. Smaller shopping center absorption in the third quarter was less than a third of its level in the previous quarter.

Tenants who have been most active in expansions include discounters and QSRs. In fact, F&B tenants accounted for almost 20% of all leasing activity in the last year. Fitness and experiential tenants continue to take significant big-box space. Experiential retailers account for roughly 15% of all leasing activity in the past year, buoyed by demand from tenants like Planet Fitness and Urban Air.

Net absorption by retail property type



Source: CoStar

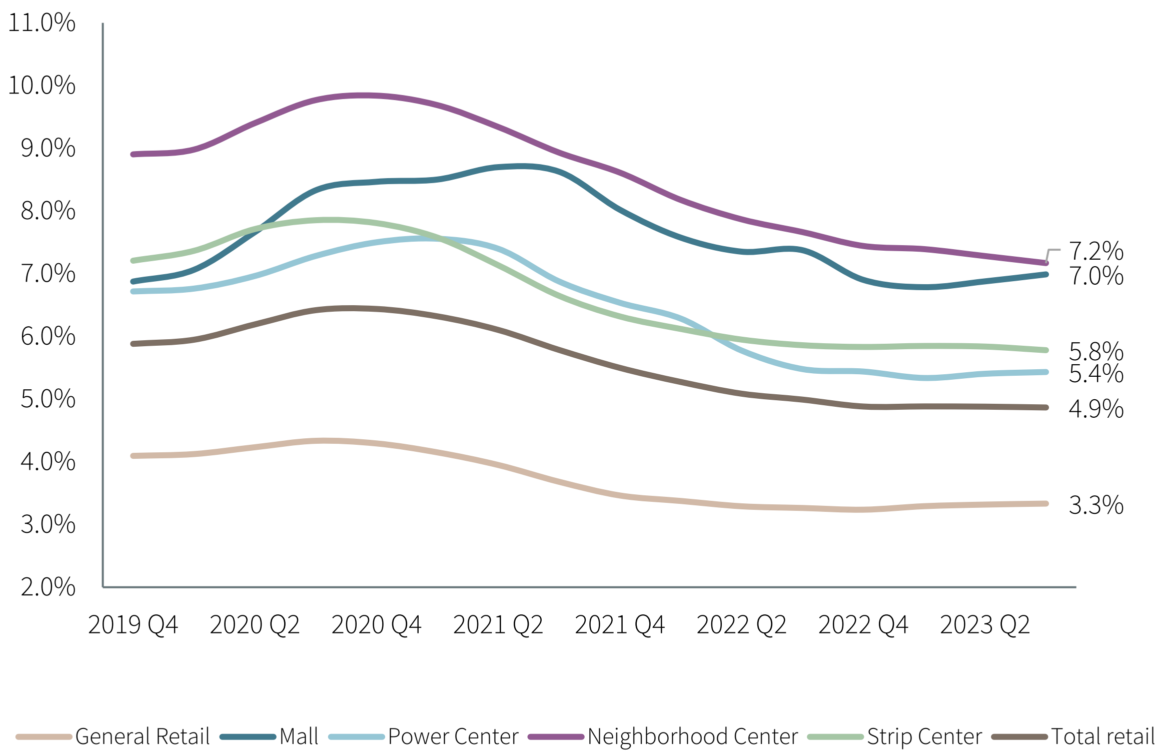
Retail supply and demand at odds

Retail real estate is experiencing a significant shortage of available space, due to limited new deliveries and 145 million square feet demolished in the last five years. The availability rate is nearly 200 basis points below its historical average of 6.8%. Particularly scarce are mid-sized boxes and outparcels in the top Sun Belt markets.

With desirable space in strong markets so scarce, leased space as a proportion of available square footage is more than 100 basis points above historical averages at 8%.

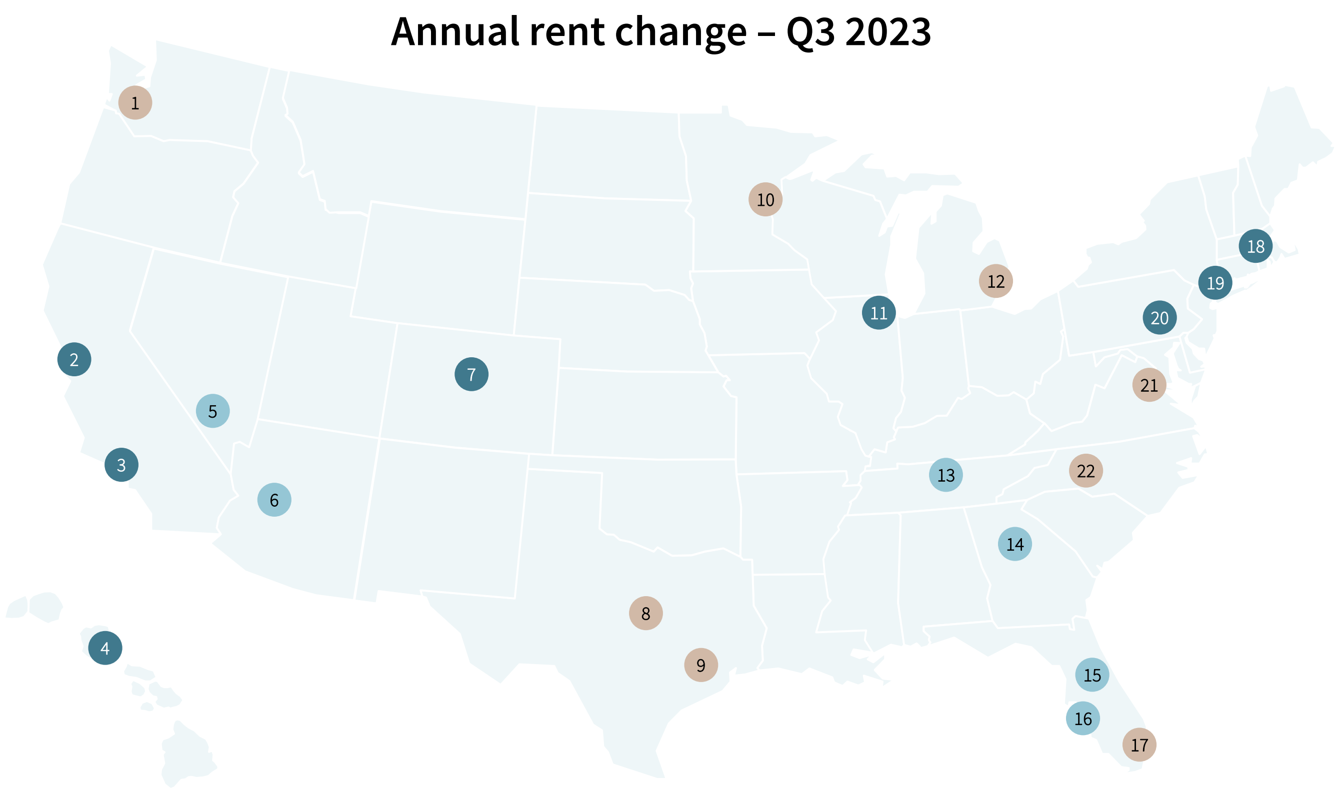
With deliveries remaining near record lows – falling 30.4% from the previous quarter – retail vacancy stayed at 4.2%. Rents continue to rise, although growth is slowing. On a positive front, all major markets are seeing rent growth, although the strongest growth remains concentrated in the Sunbelt.

Retail availability rate by retail property type



Source: CoStar

Major metros see positive rent growth with strongest in Sunbelt markets



1	Seattle	4.7%	12	Detroit	3.5%
2	San Francisco	1.1%	13	Nashville	6.5%
3	Los Angeles	0.6%	14	Atlanta	6.1%
4	Honolulu	0.9%	15	Orlando	7.7%
5	Las Vegas	8.9%	16	Tampa	8.2%
6	Phoenix	9.7%	17	Miami	4.5%
7	Denver	0.8%	18	Boston	0.5%
8	Dallas	4.6%	19	New York	2.0%
9	Houston	4.1%	20	Philadelphia	2.3%
10	Minneapolis	4.5%	21	Washington, D.C.	4.0%
11	Chicago	1.2%	22	Charlotte	5.3%

3.1% - 6.0% < 3.0% > 6.0%

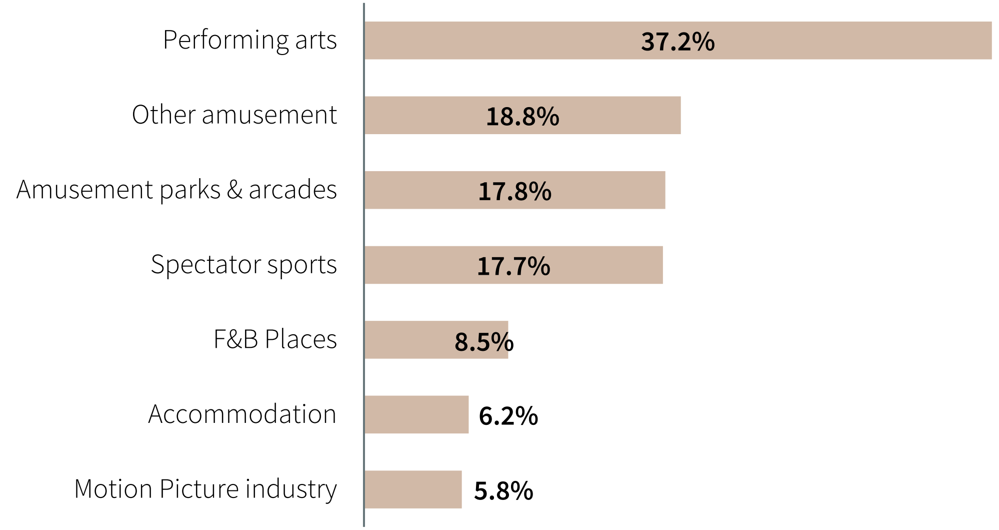
Source: CoStar

Consumers focus on fun

Spending on experiences sees continued growth

As we approach the 2023 holiday season, the gradual shift to normalcy and return to experiences continues. Third-quarter spending on performing arts soared 37.2% year-over-year. Amusement parks, arcades and spectator sports all saw double-digit growth. Fun is in again.

Y/Y change in sales Q322 – Q323



Source: U.S. Census Bureau

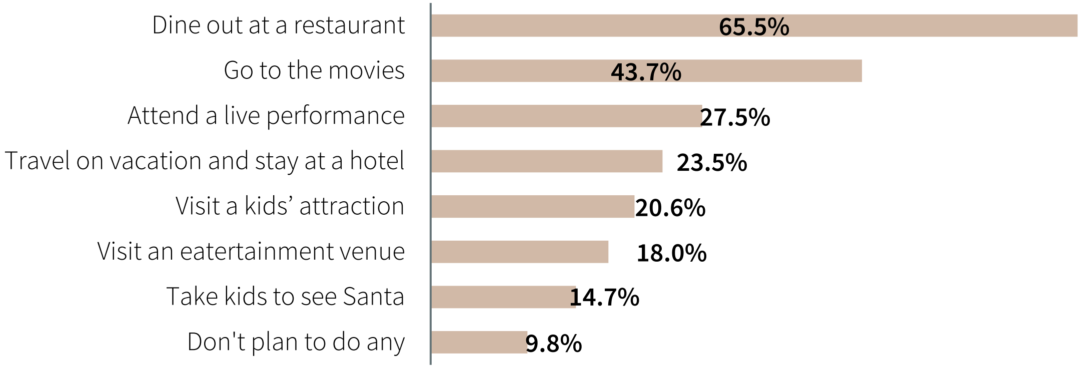
Consumers budget big on fun for the holidays

Consumers' gradual move away from goods spending towards services and experiences is in full effect for the holidays, with shoppers planning to spend a healthy $958 per person this holiday season – 22.8% of which will used for holiday entertainment and experiences.

Planned spending on physical goods – gifts and other holiday merchandise – is down some 13.8% from 2022, decreasing from an average of $868 per person last year to $748 per person this year. However, with the addition of the new spending component of experience in this year's survey, consumers' overall holiday budgets exceed 2022.

More than 90% of respondents surveyed plan to participate in at least one holiday-related experience. And they're doing so more than they did in 2022. Almost two-thirds of respondents plan to dine out, while close to half will go to the movies – almost twice as much as last year.

Which of the following do you plan to do at least once this holiday season



Source: JLL Holiday Shopping Survey 2023

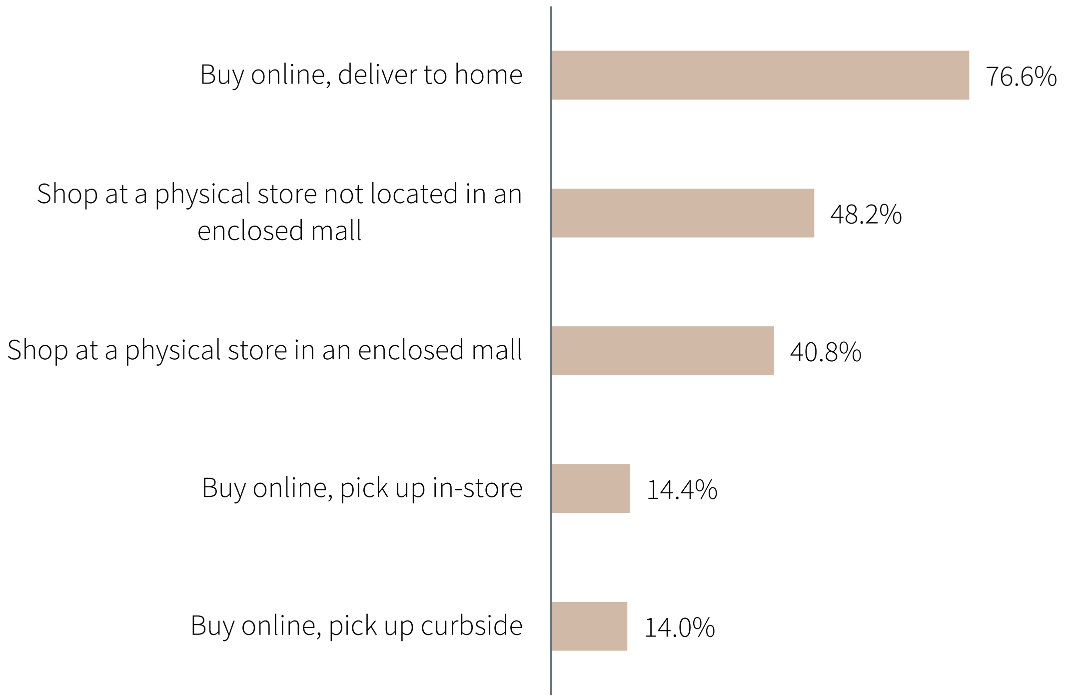
Americans will shop across channels

Most consumers will interact with the physical retail store in some way this holiday, either by shopping in a mall, in an open-air center or picking up curbside or in-store. In comparison, more than three-fourths will order online for home delivery.

Consumers will not limit themselves to one channel. Approximately 57% of shoppers will use two or more channels to cross off their holiday lists.

For instance, roughly 48% of shoppers who order online for home delivery will also visit an open-air center and 41% will head to the mall. Holiday shoppers visiting malls are also likely to shop at open-air centers. Curbside and BOPIS shoppers will order online for home pick up and more than half will head to also shop inside a physical store at a mall or open-air center.

% of Americans who shopped via a particular channel



Source: JLL Holiday Shopping Survey 2023

M&A transactions buoy retail capital markets activity

Retail sees strong M&A activity in third quarter

The retail capital markets in the third quarter were largely marked by M&A transactions, including the announcement of Kimco's acquisition of RPT Realty. Entity-level transaction volume in the third quarter was comprised of Global Net Lease's (GNL) $3.9 billion acquisition of The Necessity Retail REIT (RTL) and Regency Centers' (REG) $1.4 billion acquisition of Urstadt Biddle (UBP).

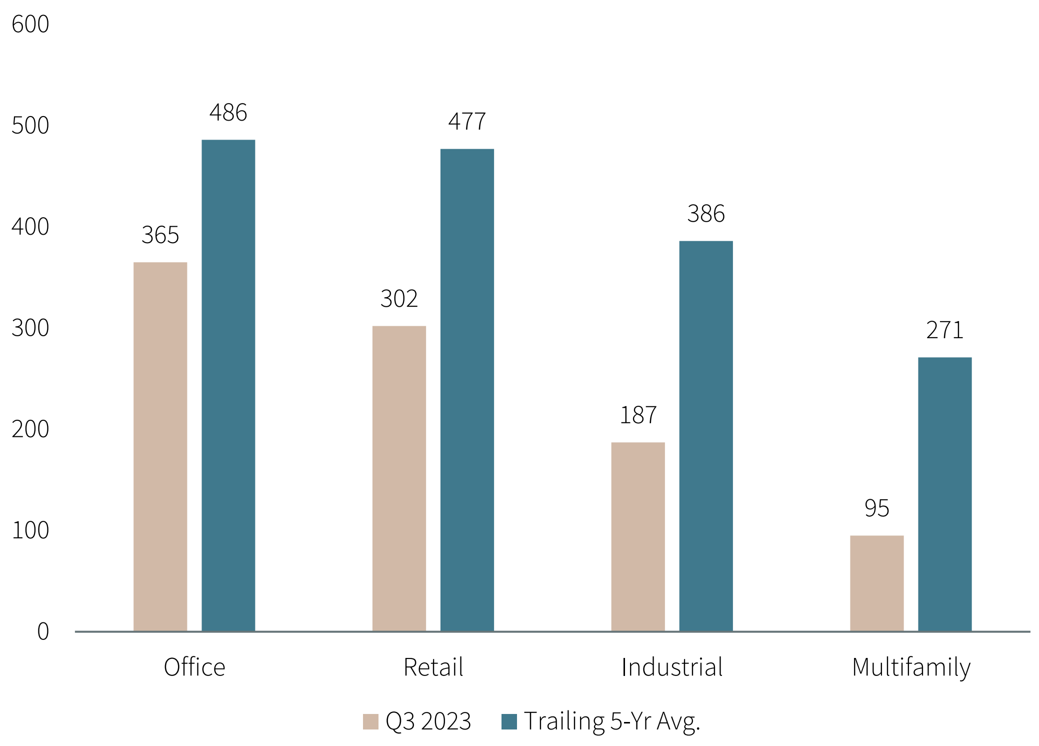
The former of the two transactions was larger both in volume and quantity of assets trading hands, with roughly 649 assets totaling just over 22 million square feet, while the latter consisted of 77 properties and 5.3 million square feet. Both deals were all-stock transactions, and each represented a 35% premium to the target company's market value.

Retail transaction volume on par with previous quarter

Outside of entity-level transactions, retail capital markets performance was relatively consistent with the second quarter. Preliminary estimates of transaction volume (excluding entity-level) were roughly $9.9 billion, a slight decrease over the previous quarter and a 40% decrease over Q3 2022. Traditional gateway markets were the most liquid in the third quarter with New York, Los Angeles, and DC leading the pack. Regional transaction volume trends, however, remained unchanged with the Southeast and West Coast claiming nearly half of all sales.

Pricing for retail assets was unable to avoid the impact of an 85 basis-point increase in the 10-Year Treasury, with cap rates increasing nearly 30 bps quarter-over-quarter. Unanchored strip centers were the most aggressively priced multi-tenant retail sub-type with an average cap rate of 7.1%, followed by grocery-anchored at 7.2%. Retail is still highly attractive on a relative basis compared to the other asset classes, with an average spread of 300 bps over the 10-yr (versus 185 bps for industrial and 95 bps for multifamily). We may see this pricing spread moderate as institutional investors and REITs begin to re-enter the market in a meaningful way over the next few quarters. For the time being, however, retail investors will continue to see accretive risk-adjusted returns.

Cap rate spread vs 10-yr US treasury (bps)



Source: JLL Research, Bloomberg Finance, LLP

Retail property subtype performance

Retail property definitions

Retail subtype	Definition	Examples
General retail	Consists of single-tenant freestanding general-purpose commercial buildings with parking	Drug stores, some groceries, streetfront urban retail stores
Malls	Includes Lifestyle Centers, Regional Malls and Super Regional Malls	Primarily anchored by mass merchants, fashion and department stores
Power centers	Consists of several freestanding anchors with minimal small tenants. 250-000 – 600,000 s.f.	Primarily anchored by big box tenants and discount supercenters
Shopping centers	Includes Community Centers, Neighborhood Centers and Strip Centers	Primarily anchored by groceries and local services
Specialty center	Consists of the combined retail center types of Airport retail, Outlet center and Theme/Festival center	Primarily anchored by manufacturers' and retailers' outlets
Total retail	All retail building types in both single-tenant and multi-tenant buildings, including owner-occupied buildings	All retail

Malls

Malls still seeing negative net absorption

Mall net absorption was negative again at -0.4 million square feet, although ameliorated somewhat from the previous quarter. Vacancy increased 10 basis points to 9.1%.

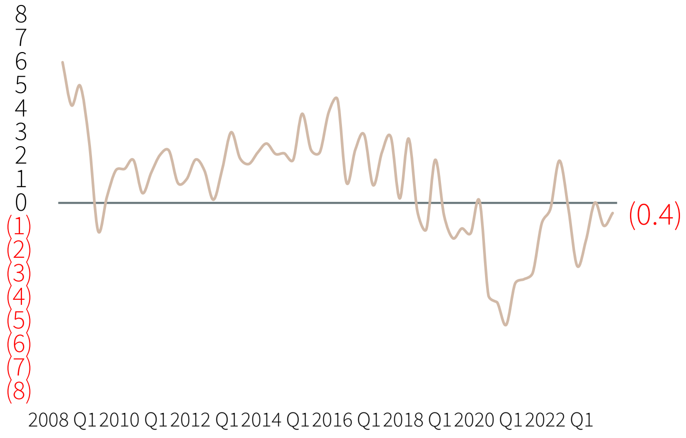
Phoenix topped major markets for year-to-date net absorption at 0.7 million square feet, including move-ins from tenants like Picklemall, Dick's Sporting Goods and Italian restaurant, Élephante. Miami and Chicago had the next highest absorption of 0.3 million and 0.2 million square feet, respectively.

Sun Belt markets are seeing above-average year-over-year mall rent growth, particularly, Atlanta, Tampa and Phoenix.

Mall fundamentals		
Q3 2023 net absorption	-0.4 million s.f.	⬆
Vacancy	9.1%	⬆
NNN rent	$32.94	⬆
Under construction	3.3 million s.f.	⬆
Deliveries	0.2 million s.f.	⬇

Source: CoStar
National index markets

Mall net absorption negative in Q3



Source: CoStar

Class A malls and lifestyle centers enjoy low vacancy

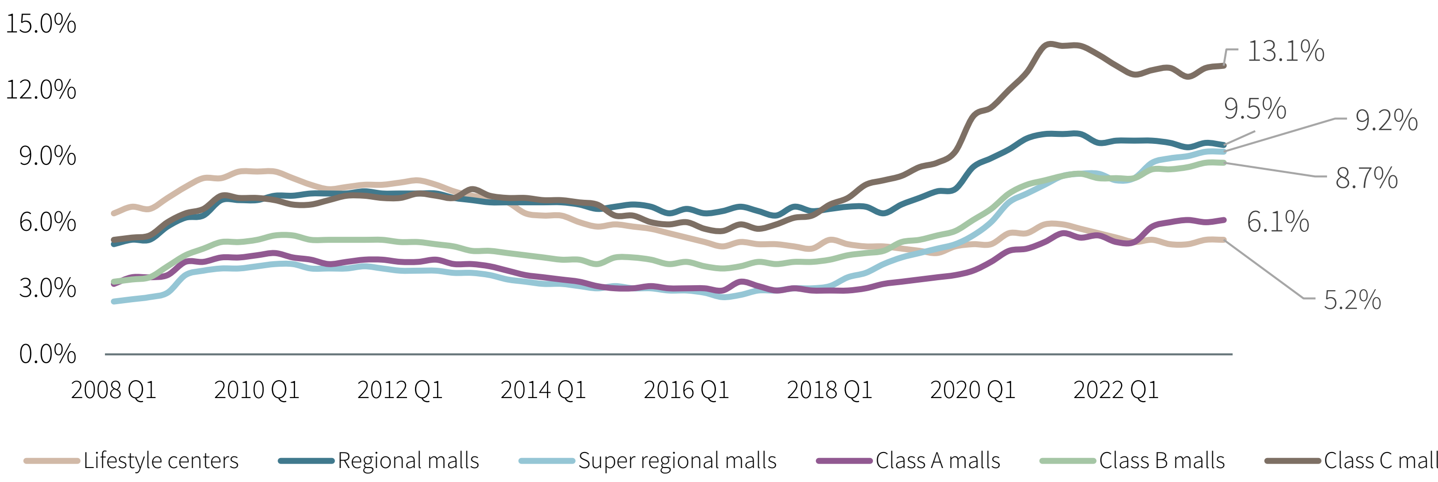
Mall vacancy is at the highest level it's been for over 15 years, but it really started to escalate in 2020 during the pandemic lockdowns.

Since Q4 2019, Class B and C mall vacancy have jumped over 300 basis points each, while Class A vacancy rose 270 bps. In contrast, lifestyle center vacancy has only increased 30 basis points during the same period, while super regional malls saw vacancy surge over 400 basis points.

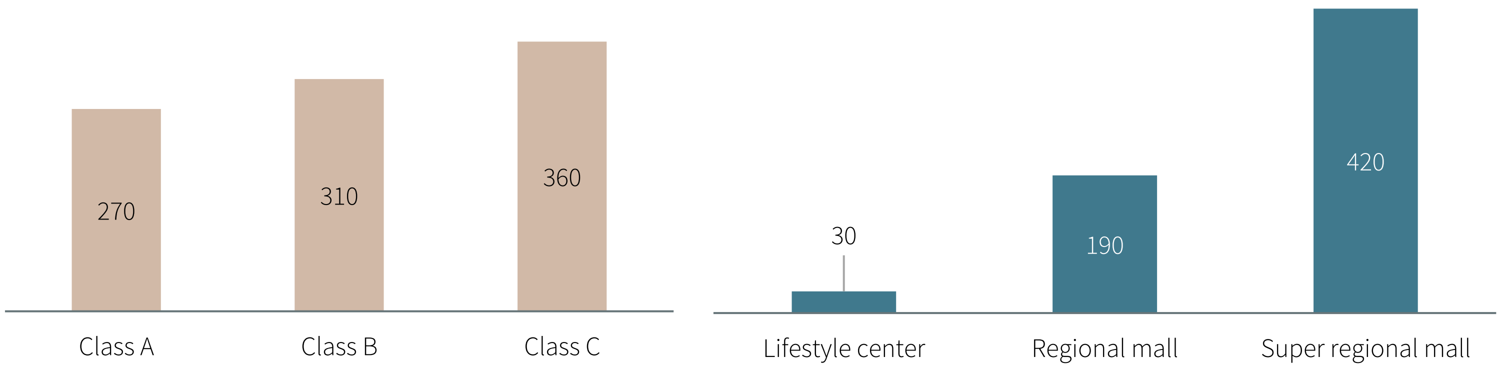
Much of this can be attributed to the swathe of bankruptcy-related closures that took place since 2020, including:

- Apparel retailers like Ascena Retail (1,600 closures), Tailored Brands (500) and Christopher & Banks (450)
- Department stores like JC Penney (242) and Neiman Marcus (24)
- Health tenants like GNC (1,200) and Jenny Craig (623)

Class A malls and lifestyle centers have significantly lower vacancies



Change in vacancy from Q4 2019 – Q3 2023 (in bps)



Source: CoStar

Malls see shift in tenant mix

Some traditional mall tenants have announced plans to relocate some of their mall stores to open-air neighborhood and community centers with higher foot traffic.

- Foot Locker announced it is closing 400 of its mall locations while simultaneously opening 300 off-mall locations
- Bath & Body Works plans to shutter 50 mall-based stores and open 90 non-mall locations.
- Macy's plans to open 30 smaller stores – roughly one-fifth the size of its traditional stores – in strip centers over the next two years. The convenience and higher traffic of these open-air centers boost store performance.

So, who's moving into malls? Notable mall move-ins came from apparel & accessories stores, fitness tenants and health/medical. Experiential tenants like Round1 and Picklemall are also targeting malls.

Q3 2023 mall move-in highlights			
	Lifestyle centers	Regional malls	Super regional malls
Big-box tenants	H&M, Planet Fitness, Warby Parker, Planet Fitness	Dunham's Sports, Old Navy, Regency Furniture Showrooms	Life Time Fitness, Round1, REI, Picklemall
Smaller tenants	Nike, Crumbl Cookies, Sephora, Yoga Six	Sunglass Hut, J. Crew, Cellairis, Aesop	Express, Puma, Sur la Table, StretchLab

Source: CoStar

Power centers

Power center demand sees lull in Q3

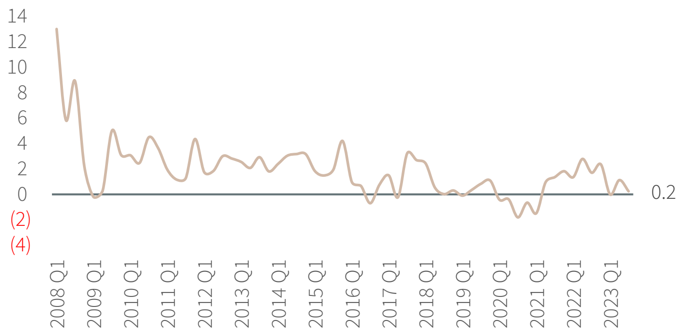
Power center absorption was minimal during the quarter, at 0.2 million square feet – an 81.7% reduction from the prior quarter. Deliveries, on the other hand rose by nearly 0.5 million square feet during the quarter, which pushed vacancy up slightly to 4.3%.

For perspective, new power center deliveries are still considerably lower than they were 15 years ago, during the great recession. Q3 2023 deliveries were less than 5% of their Q3 2008 levels, which is why vacancy is some 100 basis points below what it was and why rent gains, while moderate, remain steady.

Power center fundamentals		
Q3 2023 net absorption	0.2 million s.f.	↓
Vacancy	4.3%	↑
NNN rent	$26.21	↑
Under construction	1.8 million s.f.	↑
Deliveries	0.4 million s.f.	↑

Source: CoStar
National index markets

Power center net absorption modest



Source: CoStar

Discount big boxes open in power centers

Mass merchandisers like Target and Walmart and off-price retailers like Marshalls and TJ Maxx continue to take a lot of power center space. Other move-ins are coming from wholesalers, fitness centers and home improvement retailers.

Q3 2023 power center move-in highlights

	Lifestyle centers
Discounters	Five Below, Burlington, Kohl's, Ross Dress for Less, TJ Maxx
Apparel & accessories	Nike, Rack Room Shoes, Boot Barn, Sunglass Hut, Old Navy
Fitness/Wellness	Planet Fitness, Ace Pickleball Club, Crunch Fitness
F&B	Crumbl Cookies, Subway, Starbucks, Longhorn Steakhouse, Taco Bell
Cosmetic/Beauty	Sephora, ULTA, Bath & Body Works, Hand & Stone
Home furnishings	The Container Store, HomeGoods, Ashley Homestore, RH

Source: CoStar

Shopping centers

Shopping center demand pulls back

Shopping center absorption fell 69.5% from the prior quarter. Overall, there were fewer move-ins during the quarter. While all smaller shopping center types saw lower move-ins, neighborhood centers saw the largest decrease in absorption.

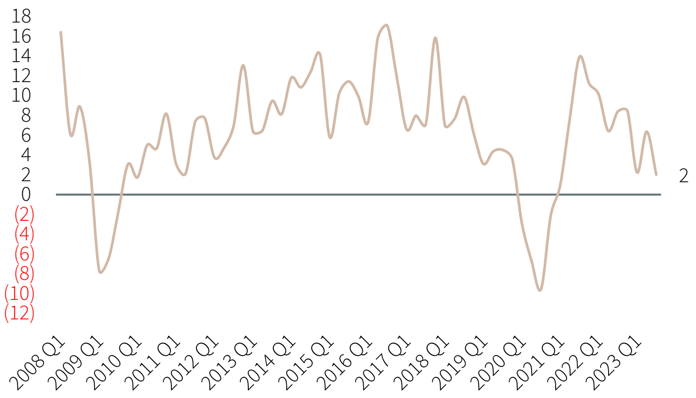
The strongest demand came from Philadelphia with net absorption of 0.9 million square feet for the third quarter. Orlando open-air demand was also robust at over 0.5 million square feet.

Space delivered fell slightly during the quarter, which kept vacancy at 5.3%.

Shopping center fundamentals		
Q3 2023 net absorption	2.0 million s.f.	↓
Vacancy	5.3%	→
NNN rent	$23.00	↑
Under construction	10.9 million s.f.	↓
Deliveries	1.4 million s.f.	↓

Source: CoStar
National index markets

Shopping center net absorption moderates



Source: CoStar

Discounters and fitness top open-air center move-ins

Community centers derived most of its demand from discounters during the quarter, including Five Below, Ross Dress for Less and pOpshelf. Other move-ins came from fitness centers like Planet Fitness, home furnishings retailers and F&B tenants like Subway and Crumbl Cookies. Neighborhood center demand consisted primarily of dollar stores and mass merchandisers; groceries, including ALDI and Publix7; and, fitness tenants like Planet Fitness and StretchLab. QSRs were very active in strip centers as were health/medical tenants and non-retail tenants.

Q3 2023 shopping center move-in highlights

	Neighborhood centers	Community centers	Strip centers
Big-box tenants	Kroger, Kohl's, Target, Flagship Cinemas, ALDI	Sprouts Farmers Market, HomeSense, Planet Fitness, pOpshelf	Hobby Lobby, Sprouts Farmers Market, CVS, Walgreens
Smaller tenants	X-Golf, StretchLab, Club Pilates, Play it Again Sports	Crumbl Cookies, Banfield Pet Hospital, Plato's Closet, Orangetheory Fitness	Dunkin, Verizon, Quest Diagnostics, U-Haul

Source: CoStar

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