

Retailers Grow Without Adding Stores

By Steve McLinden

Few new shopping centers are going up in the U.S., and yet Wall Street remains hungry for growth. The retailer response is to expand “in place”: to reshape their spaces and fine-tune their brands, in the hope of squeezing more from existing footage. From Macy’s \$400 million remake of its New York City store in Herald Square to a wholesale recasting of some 3,000 Army and Air Force PX stores nationwide, retailers are aggressively reinventing their images.

At least 8,000 U.S. stores under the Jones Lang LaSalle retail umbrella are undergoing some kind of renovation program, says Steve Jones, managing director of the Jones Lang LaSalle multisite retail program. “In fact, there is a backlog of several years,” said Jones. “Retailers are busy seeking out a new brand identity and figuring ways to carry that over to the store level and their products and fixtures.” New-store growth has slowed, so retailers know they need to increase same-store sales, he says. “They’re looking at how to increase revenue and are doing minor and major renovations ranging from new paint to new fixtures to new equipment to entirely new departments. They want to give the customers a whole new look and feel.” The national slowdown in new construction has given retailers an opportunity to re-examine the in-store presentations they may have neglected when they were busy opening new units, says Jones.

Driven by improvements, annual retail construction spending rose from \$40.9 billion in 2010 to an estimated \$42.03 billion last year, with projections of an increase to \$46.2 billion this year and to \$53 billion next year, according to Reed Construction Data. Though sales results depend on many factors, merchants can realize sales growth of at least 6 percent on such projects, and in some cases much more, Jones says.

In the case of the 3,100 Army & Air Force Exchange Service department stores, systemwide rebranding and remerchandising helped boost sales by upwards of 200

percent in most locations, according to Jones Lang LaSalle. Jones Lang LaSalle and consultants came up with a new logo, remarketed the stores as “The Exchange,” conceived a V-shaped store layout and reorganized the sales floors. These stores were losing business to off-base big boxes and other private stores before the overhaul.

Fast-food restaurants are on the move too. Arby’s boosted sales at some 70 restaurants it renovated, all of them over 20 years old. Jones Lang LaSalle assisted with the new look, which includes fresh signage, brighter interiors and kitchen upgrades.

In many cases department store retailers are initiating their renovation strategies at flagship stores. In November Macy’s announced a four-year, \$400 million overhaul and expansion of its Herald Square store. A reconfiguration of office and storage space will add 100,000 square feet of floor space for a total of 1.2 million square feet. The shoe department will be the world’s largest, offering up to 300,000 pairs, according to Macy’s. The redesign is to incorporate new technology interactive store directories. Ultimately, the store will boast 22 restaurants and food-service stations. “Like other department stores, Macy’s is trying to make their real estate more productive while creating the right customer experience and aggressively moving into the digital space,” said consultant Wendy Liebmann, CEO of New York City-based WSL Strategic Retail. “Retailers are being forced to think about productivity. They’ve come to recognize that opening more stores isn’t the route to growth and profitability.”

As of last December, Macy’s is operating roughly 850 stores (including Bloomingdale’s), the same number it was operating in 2007. Last year the chain remodeled its Water Tower Place Macy’s store, in Chicago, and its New York City Bloomingdale’s flagship store. The reported price tag on that revamp of the 520,000-square-foot New York Bloomingdale’s is \$50 million.

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SHOPPING CENTERS TODAY

Department stores typically postponed renovations through the first few years of the recession, Liebmann says, but they are now making up for lost time. Sak's Fifth Avenue completed a comprehensive flagship store renovation in 2010, JCPenney has revamped its various prototypes, and Barneys New York, Lord & Taylor, Nordstrom and others are reassessing their real estate, she says. Kohl's remodeled 100 stores last year, up 18 percent from the number of remodels the year before.

"Retailers want to remain relevant in the eyes of the customer and send a message that they are cutting edge, and there's no better way to signal that than a renovation," said Kenneth Katz, a principal of Baker Katz, a Houston retail brokerage. "We're seeing it across the board in all product types. It is a great opportunity to make a statement." Best Buy, for one, is spending a lot on renovations while also trimming its prototype size, he says.

Many retailers that expanded robustly last decade often found that they failed to generate enough additional revenue to justify the effort, says Jeff Green, who heads an eponymous retail consulting firm in Phoenix. "So now they really want to drive their sales per square foot in smaller or existing locations," Green said.

While large retailers try to get more out of existing boxes, some regional retailers are pondering the store-expansion opportunities afforded by the large number of small-space vacancies in most markets, says Mike Schmid, who heads the research and geographic-information-systems departments at Fort Worth, Texas-based Buxton. "They are looking for locations, but they are taking the opportunity to better understand who their customers are first," said Schmid.

In the Philadelphia area smaller apparel retailers are growing into new locations rather than renovate the existing ones, says Douglas Green, a principal of Michael Salove Co., a real estate brokerage and advisory firm in Philadelphia. "There is a more disciplined approach to expanding than four or five years ago," he said. "Deals have to fit into a tighter box. The local supply of shopping centers has dwindled to a point where we are on the

precipice of new construction here."

Grocery chains have spent the past four years improving existing stores instead of building new ones, and they remain on that path, says Chris Wilson, president of Los Angeles-based Wilson Commercial Real Estate. "The recession more or less defined and refined that objective," Wilson said. The strategy carries forward to some retail REITs as well, Wilson says. "We do leasing for Regency Centers, and they've also been concentrating on getting greater value out of their existing portfolio."

Some remodeling has been executed with an eye toward saving energy. Two 14,000-square-foot Nike Factory stores — one in Louisville, Ky., and the other in Des Moines, Iowa — were remodeled late last year to achieve LEED (Leadership in Energy and Environmental Design) Gold certification. Before they reinvest wholeheartedly in existing stores, large tenants typically seek a commensurate financial commitment from landlords, says Jones. "They're looking at the lease to determine the remaining terms and making sure they're there at the appropriate price point and that the owner is upgrading the center along with them," he said. "It's an opportunity for renegotiation."

Store renovation is still a relative bargain for U.S. retailers, Jones says, but that may be changing. "This is still an opportune time to renovate, with construction prices remaining low," he said, "but with improving conditions, that's bound to get more expensive."