

Competitive landscape in commercial real estate

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Home » Property Types » Retail » Clash of the Titans: Regional Mall REITs Fight for Limited Outlet Development Opportunities Clash of the Titans: Regional Mall REITs Fight for Limited Outlet Development Opportunities May 9, 2012 12: 54 PM, By Elaine Misonzhnik, Senior Associate Editor In the fall of 2010 executives with Taubman Centers Inc. , a Bloomfield Hills, Mich. -based regional mall REIT, began talking about the REIT's new avenue for growth: outlet centers. Article Tools ? Latest News

More Latest News Taubman had recently completed the conversion of its Great Lakes Crossing property in Auburn Hills, Mich. , a 1. 35-million-sq. -ft. enclosed regional mall, into Great Lakes Crossing Outlets. Taubman was able to sign up many tenants that were not present elsewhere in Michigan, including Bass Pro Shops Outdoor World, Disney Store Outlet and Rainforest Cafe. Great Lakes Crossing Outlets was attracting both local shoppers and Canadians from across the Detroit River. As a result, the center's sales per sq. ft. umbers rose significantly, company officials said during earnings calls. The success in Auburn Hills helped convince Taubman's management to capitalize on additional outlet center opportunities. Besides, in a market saturated with fortress malls and lifestyle centers, outlet centers represented one of the last opportunities for ground-up construction. Robert S. Taubman, the REIT's chairman, president and CEO, laid out a goal of developing from five to 10 outlet centers in the p of a decade. Among the first such undertakings Taubman pursued was a site in Manvel, Texas, near Houston.

The site seemed a good fit for Taubman's target outlet center sales level of at least \$400 per sq. ft. The median household income in Manvel is \$65, 864 a year, more than \$15, 000 higher than the median household income for

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the state as a whole. In addition, the town's proximity to Houston would give Taubman access to 2 million potential shoppers. Taubman's Texas ambitions, however, did not pan out. Both Tanger Factory Outlet Centers, a Greensboro, N. C. -based REIT that specializes in outlet center development, and Simon Property

Group, the largest retail landlord in the country in both the regional mall and outlet center arenas, had laid claims to outlet center development sites in nearby Texas City, just 22 miles away. According to brokers familiar with the market, the greater Houston area could not support two, let alone three, outlet centers. In June 2011, Simon and Tanger took a decisive step to win the market by announcing that they would partner to build a 350, 000-sq. -ft. joint development in Texas City under Tanger's brand name. It marked the first joint venture development partnership in Tanger's history.

Ultimately, the two firms decided to work together on one large outlet center rather than spend money fighting each other, says Michael Rodenas, principal with Rodenas Consulting, a national consulting firm that specializes in shopping centers and malls. As a result, Taubman quietly retreated from the market. In July 2011, while discussing the company's earnings for the second quarter, Robert Taubman admitted to analysts that outlets constitute " a very competitive space. It's a very competitive world out there in development generally. " He reiterated the company's commitment to investing in outlet centers both in U.

S. and in Asia, but refused to discuss the Texas project. The Houston saga wasn't the only time Taubman and Simon came to loggerheads in the outlet space. In early April, Simon and Taubman each issued press releases about <https://assignbuster.com/competitive-landscape-in-commercial-real-estate/>

competing outlet center projects in Chesterfield, Mo. , another market where trade area demographics seem to dictate that only one outlet development can succeed. On Apr. 3, Simon revealed that Saks Fifth Avenue OFF 5th agreed to anchor its St. Louis Premium Outlets, an outlet center slated to contain at least 350, 000 sq. ft. of space. (St.

Louis Premium Outlets is a product of a joint venture between Simon, Woodmont Outlets and EWB Development LLC, all experienced outlet center developers.) Two days later, Taubman announced it broke ground for Taubman Prestige Outlets Chesterfield, a 450, 000-sq. -ft. center. Taubman's press release noted that it had firm commitments from a number of tenants, but did not identify any retailers by name. It is likely that only one of those two centers will get built in Chesterfield. " We've said publicly, I think, Simon has said publicly that there is only going to be one project built in St.

Louis," Robert Taubman said during the firm's first quarter earnings call. " We are way ahead, on a much better site with much better access, much better visibility. ... So to us it's very clear as to which project is going to be built. " Most industry sources, however, are putting their money on Simon because of the firm's size, its existing network of relationships in the outlet center industry and the fact that it has already bagged a major tenant. The large regional mall players, including Simon, Taubman, Macerich Co. CBL & Associates Properties and others, have all made overtures to enter the outlet space. But with limited opportunities for development and an existing group of experienced landlords already competing there, these battles—competing press releases, wars of words and unconventional partnerships— are likely to continue to play out repeatedly throughout the country. CBL & Associates

recently invested in The Outlet Shoppes in El Paso (Texas). Last spring, both Simon and Tanger announced outlet center projects in the town of Halton Hills, a suburb of Toronto.

Tanger has since moved its project further away and will build it as an outlet addition to Heartland Town Centre, one of Canada's largest power centers. Simon, meanwhile, started construction on its original site in Halton Hills in April. And in the Chicago area, Macerich and AWE Talisman have announced plans to build a \$200 million, 528, 000-sq. -ft. outlet center in Rosemont while Craig Realty Group, a privately held outlet center developer, has ambitions to develop Chicagoland Outlets at Country Club Hills, a 408, 500-sq. -ft. project.

Simon Property Group declined to comment for this article. Tanger, Taubman, Macerich and Craig Realty Group, meanwhile, did not respond to calls for comments. "The problem is—as we saw when developers started to roll out lifestyle centers—that everyone goes after the same markets," says Jeff Green, president of Jeff Green Partners, a Phoenix-based consulting firm. "And many times the newer folks to the outlet industry are going to find that it's a much harder industry to get into when there are relationships that have been in place for so many years." In certain isolated instances, such as the one near Houston, two big developers might form joint ventures because one of them holds a better site while the other wields more power with retailers. Such examples, however, will be few and far between, according to Richard Hauer, managing director of business restructuring services at BDO, a New York City-based consulting firm. "Let me put it this way: Neither Simon nor Taubman is going to build a second-rate outlet mall," he says. "So if the first

guy can get Coach and Polo and Saks and a few of those names that every outlet mall really wants, you'll see the other guy back down. Mass appeal. The reasons the outlet sector has suddenly become overcrowded are easy to trace. During the downturn, outlet center sales rose while mall sales fell or remained flat because shoppers were suddenly attracted to outlets' value proposition. What's more, as these centers moved closer to urban areas and proved that they can work in close proximity to regional malls, the number of markets that could support new projects increased. With limited opportunity for growth elsewhere, regional mall REITs began to focus on the outlet sector.

Real estate owners that want to gain market share in a new property segment typically have two avenues for growth: either through acquisition of multiple assets or another operating company or through development. But when Simon bought Prime Outlets Inc. in 2010 it snapped up the last big privately-held outlet center operator in the market. Today, "no private guy controls 20 or 30 centers that could be sold," says Gerard Mason, executive managing director with Savills LLC. What's more, there is a wide spread on yields between development and investment.

For instance, CBL & Associates, a Chattanooga, Tenn. -based REIT, recently invested more than \$108 million to provide financing for two outlet centers developed by Horizon Group Properties, a Rosemont, Ill. -based outlet center developer. (CBL has also partnered with Horizon on groundup projects in Oklahoma City and Woodstock, Ga.) But CBL CEO Stephen Lebovitz admits that development projects offer double-digit returns while investing in existing centers brings returns in the 8 percent range. I would expect that

our growth will be mainly through new development,” he says. At the same time, Lebovitz notes that the number of markets in the U. S. that would meet CBL’s development criteria, including a trade area of approximately a million people, a sizeable tourist base and lack of existing competition, is limited. One high-ranking industry source says that for developers targeting outlet center sales on par with Simon’s levels, which average about \$550 per sq. ft. , there are maybe 10 untapped markets left that fit the necessary trade area characteristics.

For developers targeting Tanger’s sales levels, which currently average \$371 per sq. ft. , there are about 40 untapped markets. “ But there aren’t 100,” the anonymous source notes. By the end of the 2012, there will be 187 outlet centers containing 71 million sq. ft. , according to Value Retail News, a publication that covers the outlet industry. Linda Humphers, editor-in-chief of Value Retail News, estimates that in the long term, the country may be able to support another 250 centers, but that would include conversions.

Occasionally, a developer will be able to find a site in an offbeat location that nobody else has thought about, says Gerard Mason. But for the most part, all the REITs are looking at the same markets, and in many cases, at the same piece of land. “ There is clearly room for growth in the sector—every major metro area can certainly support outlet retail,” says Michael P. Glimcher, CEO of Glimcher Realty Trust, a Columbus, Ohio-based regional mall REIT that also owns outlet centers in Elizabeth, N. J. and Auburn, Wash. I just think the reality is there are a lot of people in that category and only a small percentage of what’s being announced will actually get built,” Glimcher says.

Bloodless war When it comes to handling competition on new developments

the big retail REITs have acquired a reputation for being ruthless, employing tactics such as funding community opposition groups to derail each others' projects, says Patrick Fox, president of Saint Consulting Group, a firm that specializes in zoning and land-use battles. These are mature markets, they are largely over-built and the battle for market share is tremendous," he notes. But unlike large regional malls that tend to be located in major urban areas, outlet centers don't normally inspire the same kind of opposition from local residents, according to James Schutter, senior managing director with Newmark Knight Frank Retail, a retail real estate services firm. In fact, many communities want to see outlet centers built because of the tremendous amount of sales tax revenue they bring in. The real battle in outlets' case is for tenant commitments.

Although the outlet industry doesn't have anchors in the same sense that the regional mall industry does, there are certain key stores that are necessary to attract shoppers and that the rest of outlet retailers follow, notes Hauer. These include Saks Fifth Avenue OFF 5th, Coach and Polo, as well as Neiman Marcus Last Call and Nordstrom Rack. About a decade ago, Hauer tried to develop an outlet center near Syracuse, N. Y. When he started negotiating with potential tenants the answer was " if you can get Polo, we'll sign. Otherwise, we are not interested. "

When there are two developers competing to build a center in a market that can support only one project it becomes a race to be the first to announce leases with major tenants. The developers try to convince expanding retailers that their center is the one that's going to happen by putting out announcements about land permits and ground-breakings. Ultimately,

however, it's the line-up of tenants that determines whose center gets built. " Developers announce that they will put together a mall [all the time], they don't always make it happen," says Schutter. If you've got this tenant and this tenant and this tenant coming, the other guys in the marketplace say, ' Let's go into this project. '" " A ground-breaking is not as strong as being able to announce a strong anchor tenant," Fox adds. So how do those key retailers decide who to go with when the choice is between Simon and Tanger, or Simon and Taubman or Macerich and Craig Realty Group? After Taubman converted its Great Lakes Crossing project into an outlet center, sales rose significantly.

Having the best site certainly makes a difference, which is why Simon may be willing to partner with Tanger if Tanger has secured a better location, according to Michael Rodenas. When the projects are in the same trade area, the choice might come down to seemingly small differences like which side of the highway the center will be located on or which zip codes in a given area are missing from the retailer's customer base. But in the outlet industry, having existing relationships with a potential landlord is also very important, according to Hauer, Green,

Lebovitz and others. And in this, Simon, which controls the largest mall portfolio and the largest outlet center portfolio in the country, has a tremendous advantage. That might not come into play as much in the Simon/Tanger relationship because the two REITs specialize in slightly different projects, but it will likely loom large in any battle between Simon and other regional mall REITs. " If you [as a tenant] get Simon angry with you on the outlet side, they can be angry with you on the traditional retail

side also,” says Green. Let’s just say that in that case the developer has a large hammer, a larger hammer than any mall-only developer would have. ” That’s why most retail industry insiders feel that while Taubman and the other regional mall REITs will eventually be able to build a handful of outlet centers, they will not be able to break into the business in the big way they had imagined. “ The outlet mall industry is kind of a closed world,” says Schutter. Sidebar: Eastern Promises While U. S. retail REIT executives try to build up their outlet portfolios at home, most of them realize that growth opportunities here are limited.

So in recent months they’ve been announcing outlet center projects elsewhere in the world, including Canada, Brazil, Japan, China, South Korea and Malaysia. In April, Simon signed a deal with BR Malls Participacoes S. A. to develop outlet centers in Brazil, with the first project scheduled to be built in Sao Paulo by 2013 and started construction on Phase I of Shisui Premium Outlets, a 234, 000-sq. -ft. outlet center in Shisui, Japan. Both Simon and Tanger have been working on outlet centers in Canada, including Simon’s 500, 000-sq. ft. Toronto Premium Outlets in Halton Hills and Tanger’s 312, 000-sq. -ft. outlet addition to Heartland Town Centre in Mississauga. And Taubman executives have told analysts they are looking to build outlet centers in Asia, where Taubman already has offices in Hong Kong and Seoul, South Korea. “ In the U. S. , you are not going to see outlet centers double in number,” says Gerard Mason, executive managing director with Savills LLC, a global real estate services firm. “ That’s why Simon is in Brazil and China.

In Brazil they might be able to do 15 outlet centers because their middle class is just emerging and they need shopping centers. ” —E. M. Sidebar:

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Mini-Malls With the increase in outlet centers' popularity, the concept has evolved to represent something different than a small collection of factory stores in the middle of nowhere. In the 1980s and 1990s, the rule of thumb was that an outlet center had to be located at least 70 miles away from the closest phone line, jokes one broker. Today, if a shopper goes to Central New Jersey, " you have the Freehold Raceway Mall [a 1. -million-sq. -ft. superregional center] and then 10 to 15 minutes away, there is an outlet mall," according to Richard Hauer. Today's outlet centers have grown larger, sometimes containing up to 450, 000 sq. ft. or 500, 000 sq. ft. of space, whereas the outlet centers of yesterday tended to average 150, 000 sq. ft. The tenant line-up has changed from manufacturers to big retail chains, many of which, including Nordstrom, Neiman Marcus, Saks Fifth Avenue, Bloomingdales, Gap, J. Crew and Aeropostale, have established off-price and outlet divisions.

Plus, outlet centers now feature mall-like amenities, such as foodcourts, restaurants and movie theaters, because people are staying on the properties longer than they used to, notes Michael Rodenas. And when CBL & Associates Properties and Horizon Group Properties were working on the plan for The Outlet Shoppes at Oklahoma City, a 350, 000-sq. -ft. center that opened last summer, CBL marked land around the property for the addition of restaurants and hotel facilities. " We feel it adds critical mass," says Stephen Lebovitz. —E. M.