



Outlook

ORANGE COUNTY
GROWTH MANAGEMENT DEPARTMENT

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Orange County Retail: ups and downs, challenges and opportunities

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Introduction

According to the Florida Retail Federation, the retail sector is Florida's second largest employer, generating 1 of every 5 jobs in the state. It annually contributes \$20 billion in wages and \$13.4 billion in sales taxes. In the Metro Orlando area, the retail & trade industry accounts for 10.9% (or 119,300 positions) of the employment sector, more than any other except leisure and hospitality (18.1%) and professional and business services (17.8%) (Agency for Workforce Innovation, September 2008). Given the importance of the retail sector, it is necessary to determine impacts of the current economic conditions on one of the state and county's major employment providers.

So, what is going on with retail? Generally speaking, economic uncertainty makes consumers save more and spend less. The banks, in contrast, are less willing to give and/or extend credit and loans to businesses. The consumer spending slump and tightening credit markets are causing an increasing wave of bankruptcies within the retail sector. According to Michael Dudley, these "store closings are expected to remake suburban malls and downtown shopping districts in Florida and all across the country" (Planetizen, February 16, 2009). The current downturn in retail affects many – employees lose jobs, shoppers can no longer buy from their favorite stores, malls and shopping centers lose their tenants, and commercial landlords must reduce their rents.

The results? More business closures, declines in sale tax revenues, and the ever-increasing number of empty buildings and store fronts.

Is it really that bad out there?

Here are just few major retailers that closed their doors or downsized in 2008: *Linens' n Things* closed 500 stores in 47 states; *Circuit*

City is shutting down their 567 remaining locations; discount clothing chain *Goody's* announced it would liquidate its nearly 300 remaining stores; *Starbucks* will close 300 underperforming stores around the world (in addition to the 600 U.S. stores it begun closing in 2008); *Foot Locker* said it would close 140 stores, *Ann Taylor* is scheduled to close 117, and the jeweler *Zales* will close 100. What makes the situation worse is that now even retailers that have not experienced a downturn are eliminating an estimated 10 to 15% of their lowest-performing stores. In Orange County, almost 385 retail positions are scheduled to be eliminated in the next two months (FL WARN notices, March 2009). Overall, many retailers – from *Home Depot* to *New York and Co.* – have been shuttering stores.

According to Colliers Arnold's Central Florida Retail Market research for the first quarter of 2008, the Orlando Market, which includes Orange, Lake, Seminole and Osceola Counties, had more than 3.9 million square feet of vacant retail space. This represents a 6.3% vacancy rate, an increase from 4.6% in 2007. It should be noted that, by industry standards, a 5% vacancy rate is considered to be "good." Higher vacancy rates can affect nearby property values. Closed stores might also affect an overall shopping centers' synergy as shopping centers might not look successful having several stores closed, and stores that are still open would not benefit from higher traffic previously associated with now closed stores. Research also shows that the Central Florida regional malls' average vacancy rate rose from 5.8% in 2007 to 7.1% in 2008. Vacancy rates in Central Florida are expected to spike in 2009, reaching 17.3% by the middle of 2009, according to Property & Portfolio Research, Inc., a Boston-based property research and portfolio strategy firm. That figure includes information on neighborhood shopping centers, community centers, power centers,



regional malls and lifestyle centers larger than 30,000 square feet.

Figures 1 and 2 provide a comprehensive breakdown of vacancy retails by retail submarkets in Orange County. **Figure 1** shows that the Downtown Orlando submarket has a vacancy rate significantly higher than any other submarkets in the County – 23.3%, which could be explained by large numbers of newly built retail and office space and nearly vacant new residential towers built in the last two to three years.

The East Orange County and Apopka submarkets have the second and third highest vacancy rates in the County, with vacancy at 9% and 8%, respectively. The Millenia submarket has the lowest vacancy rate at 0.7%, while maintaining the second highest lease rate of \$32.67 per square feet. This popularity could be explained, in part, by its convenient location between tourist centers and Downtown Orlando, resulting in high consumer traffic generation rates. Among all fifteen Orange County submarkets, the average vacancy rate for the first quarter of 2008 was 6.74% (5.56% excluding Downtown Orlando), with an average lease rate of \$20.95 per square feet of space.

Figure 1. Retail Statistics: Central Florida Submarkets

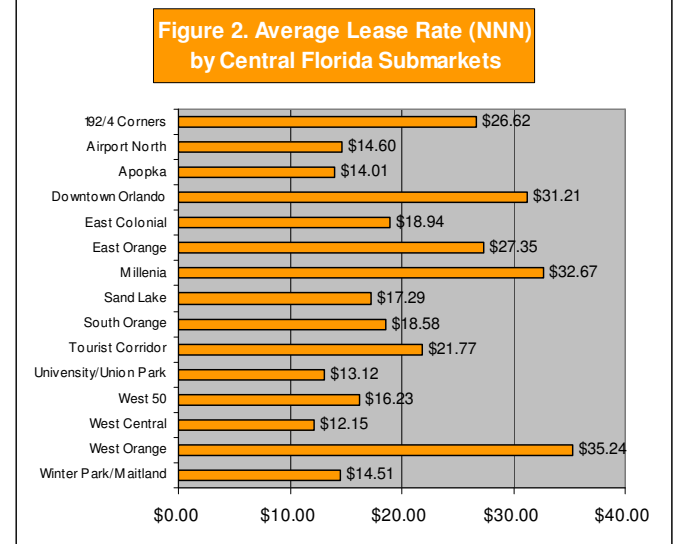
Submarket	Vacant Sq. Ft.	Vacancy Rate	Average Rate
192/4 Corners	34,508	5.8%	\$26.62
Airport North	205,283	4.7%	\$14.60
Apopka	130,641	8.0%	\$14.01
Downtown Orlando	208,185	23.3%	\$31.21
East Colonial	204,931	7.5%	\$18.94
East Orange	210,176	9%	\$27.35
Millenia	15,099	0.7%	\$32.67
Sand Lake	71,110	1.7%	\$17.29
South Orange	291,316	13%	\$18.58
Tourist Corridor	334,937	4.1%	\$21.77
Univensity/Union Park	163,019	6.9%	\$13.12
West 50	312,951	7.1%	\$16.23
West Central	157,258	4.1%	\$12.15
West Orange	69,942	1.9%	\$35.24
Winter Park/Maitland	52,935	3.3%	\$14.51

Source: Colliers Arnold, Market Research, First Quarter, 2008

Note 1: Figures include retail shopping center space of 15,000 sq. ft. and greater.

Note2: Overall vacancy figures include direct and sublet space.

Note3: Triple Net (NNN) refers to a rental type in which the lessee is required to pay for its share of the property's taxes, insurance and operating expenses (in addition to rent payments).



It should be noted that the data used in **Figures 1 and 2** is from the first quarter of 2008, and the current economic uncertainty may have altered conditions since that time. With more companies going out of business and downsizing, vacancy rates may have increased, while average rates could have decreased. However, until new data are available, these changes are almost impossible to quantify, except on an anecdotal basis. **Figure 3** represents a more recent perspective on the vacancy rate in Orlando area done by the Metro Orlando Economic Development Commission (EDC).

As **Figure 3** indicates, the retail vacancy rate has been going up, which might eventually cause the asking price per square foot to go down.

This dynamic, almost unheard of in a strong economy, might become a new reality for owners of local shopping centers and malls. In this new reality, the most viable option for landlords likely will be to try to hold on to existing tenants. This change in the landlord-tenant relationship is one of several major challenges in the retail sector.

Figure 3. Retail Statistics: Orlando

	2005	2006	2007	2008
Vacancy Rate	8.90%	8.50%	9.00%	9.40%
Annual Asking Rent (\$/sq.ft.)	17.42	18.3	18.85	19.51
Total Retail Completions (sq.ft)	2,090	1,300	3,500	2,800
Household Income (\$)	48,643	52,803	53,291	54,545

Source: Metro Orlando Economic Development Commission, February 2009

Different retail climate

In this tough economic climate, worried consumers have swapped “wants” for “needs.” According to the *New York* magazine, in market-research terms, purchases fall into two categories: staple and discretionary. “In more favorable economic times, the consumer usually begins purchasing those items that they would like but do not necessarily require. These items are classified as discretionary. During economic periods of contraction, consumers often forego their discretionary purchases and focus on those items they need but do not necessarily want. These items are classified as staples.” (Donald Dony, 2008). In the past decade or so, consumers have had needs and the wants, mixed up. Now, that distinction is being reestablished, and forcefully.

High fuel and grocery prices and rising unemployment on top of the housing crisis are making it more difficult for consumers to look beyond necessity products and services (staple items). This means that there are potentially some hard times ahead for specialty retailers (selling discretionary items) that thrived during the long economic expansion—retailers of jewelry, home electronics, clothing, and other high-end products. However, some chains continue to expand, offering opportunity for retail real estate owners to fill space—as long as it is in markets where money is being spent. Among those expanding are *Publix Super Markets*, *Rue 21*, and *Ulta* cosmetic stores.

For retailers, sales slowdown and tighter lending terms may lead to a continuing number of bankruptcies. Because retailers rely on a broad network of suppliers, their bankruptcies are rippling across the economy. The cash-short chains are leaving behind tens of millions of dollars in unpaid bills to shipping companies, furniture manufacturers, mall owners and advertising agencies. Many are unlikely to be paid in full, spreading the economic concern to other industry sectors.

For landlords, businesses shutting down cause more closed doors and higher vacancy rates. Retailers’ store closings and curtailed growth plans are tipping the balance in the tenant’s direction for the first time in memory. Tenants have more leverage, and they can be more obstinate in negotiating favorable terms. Such change brings new and different opportunities to business owners looking to strengthen their positions in the market or to expand.

New opportunities

What are those opportunities? First of all, there are perks for retailers from landlords (Michael Ido, 2009, Anjali Fluker, 2008). To find new tenants and keep current ones, property owners are willing to “sweeten the deal”. Where conditions of contracts were previously given to retailers with virtually no right to negotiate, landlords are now ready to sign up for shorter lease terms, give away months of free rent and agree to restructured pricing with early discounts and rent increases over time.

The second big question is what will be done with the empty buildings? It may well be late 2010 before some proposed shopping center developments are back on track. The nationwide prediction is that up to 3,000 shopping centers, mostly smaller strip centers and some larger malls, will close in 2009. So what is to be done with all empty retail space, especially the vacant “big boxes” dotting the landscape with the liquidations of *Linens’ n Things* and *Circuit City*?

Some creative ideas for utilizing empty big boxes include (a) turning them into seasonal stores, such as those that sell Halloween or Christmas decorations; (b) using them for community purposes, such as community centers and alternative school sites, if operating funds are available; or (3) subdividing them into spaces smaller merchants would use. There can be many more ways to utilize empty spaces and prevent them from acquiring a negative appearance in the community.

For Orange County in particular, the presence of large empty retail spaces could be a great opportunity for implementing some of the smart growth principles conceptualized in the most recent update to the Orange County Comprehensive Policy Plan, which promote mixed-use infill and redevelopment projects. An overall desire to concentrate new development closer to existing urban centers of the County could be realized through development intensification (higher density and intensity) and a mix of uses on a property and reuse of existing structures (infill and redevelopment). Reuse of empty retail spaces in shopping plazas and strip centers could do just that and might eventually lead to higher intensity of existing development and creation of “activity centers” in the County. *Colliers Arnold Market Research Group* has also emphasized in their retail market overview that “infill projects will grow to become a popular development choice throughout Orlando as prime available retail land

diminishes" (Orlando, FL, Market Research, Retail, 1st Quarter, 2008).

The third opportunity is more of a mental shift for consumers. It is a chance for American society to rethink our way of living, which lately was mostly concentrated around spending and consumption. Current economic conditions force us to think more before we spend, to save more, and to distinguish our "wants" from our "needs." Lasting effects when the economy recovers are not clear, but collective evaluation of personal economic priorities may be beneficial in the long term.

This shift has already begun. *The New York Times* reported this February that "American consumers and businesses are embarking on an era of thrift as the recession deepens, saving more money as they cut purchases." The data indicate that Americans cut their spending for a sixth month in December 2008, as they worried about losing their jobs and earning less in a deteriorating economy. At the same time, the personal savings rate in the last three months of 2008 rose to its highest level in six years (3.6% in December). These reports highlight consumers' rational behavior in response to incentives and conditions of the current economic situation.

Conclusion

This analysis is, by no means, comprehensive, as it is almost impossible to predict what would happen in the near future to the county's, state's and national economy. The amount of data available is limited, and existing data is outdated very quickly. Therefore, it is important to monitor changes occurring in the retail sector of the local economy, in order to prepare for challenges the ever-changing economic conditions will bring. It is also necessary to analyze local markets more comprehensively by including data on office and industrial uses.

This article highlighted multiple store closings and other retailer challenges, consumer concerns, and issues with landlords and retail leasing, as well as changes in our behavior. But in reality, not all retailers are experiencing hard times. Wine bars, low-price eating establishments, and some grocery chains are doing extremely well. *Aldi* and *Publix Super Markets* are spotting opportunity in others' troubles by opening new stores and absorbing traffic previously generated by now closed retailers. Discount cosmetics superstore *Ulta* plans to add 75 stores to its 283 stores in 2009. *Rue 21*, a teen fashion chain, plans to add 1000 stores to its 300 stores. Startup Winter Garden

wine-tasting shop *Put a Cork in It* plans to open six to ten new locations.

What is clear is that local retail markets, along with office and industrial sectors of the economy, are laying the foundation for existing and future economic development in this volatile economy. This time in economic history is about surviving, and it would be the "survival of the fittest" which would reshape our retail landscape in the next few years. After all, Florida has eight of the top ten strongest markets in the Southeast, in terms of total consumer expenditures per household (Claritas, 2007). Over time, the strength of these economic fundamentals will emerge, and some retailers will benefit, while others will have to restructure and downsize to survive the storm.

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