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# THE HIGH STREETS HIT NEW HIGHS

Increased consumer spending and greater international competition push retail rents in some Manhattan submarkets to record levels.

By Jaime Lackey

New York City ranks as one of the top retail markets in the world. Competition is so fierce for spots on Fifth Avenue that it had ranked the most expensive retail destination in the world for a decade — until Causeway Bay in Hong Kong pushed Fifth Avenue down to second place in last year's annual ranking by Cushman & Wakefield.

"In terms of global branding, New York City is one of the most important locations for retailers. In the context of global high streets, we're on par with — or have surpassed — London, Paris, Tokyo, Hong Kong and Shanghai," says Gene Spiegelman, executive vice president with Cushman & Wakefield.

And retailers aren't just focused on Fifth Avenue. Last summer, Cushman & Wakefield reported that New York held four spots on the list of top 10 retail markets in the world, including Fifth Avenue, which averaged rents of $2,500 per square foot at that time; Times Square, with rents of $2,100 per square foot; East 57th Street, with rents of $1,100 per square foot; and Madison Avenue, with rents of $1,100 per square foot.

Spiegelman predicts that Fifth Avenue will again outrank all other retail rents in the world this year. "And I believe Times Square has the potential to rank second this year," he says. "Just think about how many eyes see a store in the historical area of Times Square."

Some markets in Manhattan — namely, Fifth Avenue, Times Square, and SoHo — have exceeded their high watermarks in terms of average asking rents, says Ariel Schuster, executive vice president with RKF. He notes that the market hit bottom in 2009 and that it has taken four years of slow and steady growth to reach pre-recession rents.

Now the question is: how long will the growth continue? "If greater absorption pushes rents higher, what will be the demand at the higher rents?" Spiegelman asks. "We'll begin to see a trend in 2014. That is when we'll find out if we have a trend line that indicates continued growth or if we've hit a ceiling. Granted, it would still be a very high ceiling."

## The Strength of NYC

Manhattan is a unique market, Schuster says. "Many tenants are here for the branding, and it is typically the first stop for European retailers and other international tenants that want a U.S. presence."

While the U.S. has long been a targeted market for major retailers globally, the global economic situation may create even more interest. "As much as our economy as been in a recession, the European economy has been worse. Consumers there are not spending money and European retailers are coming here," says Chase Welles, partner with SCG Retail, a division of The Shopping Center Group that focuses on urban retail.

"The added international competition pushes rents higher," Welles notes.

Manhattan also attracts many tourists — which in turn attracts many re-

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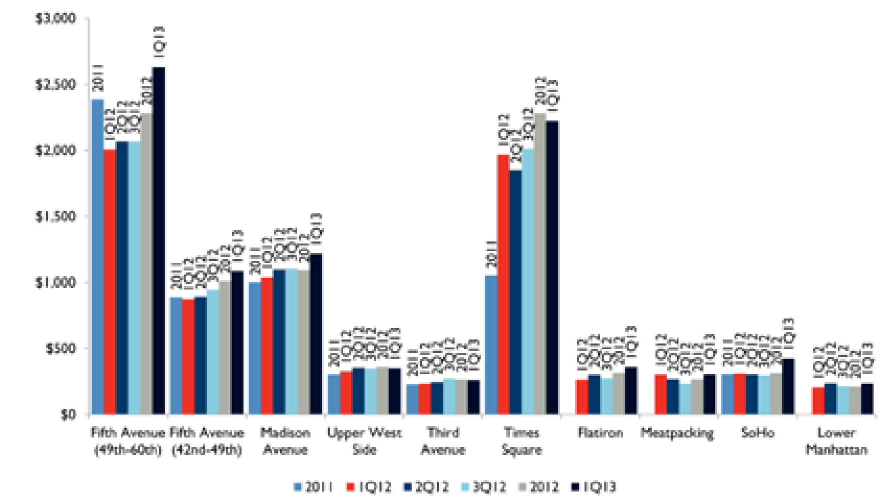
### Manhattan Retail by Submarket

Average Ground Floor Asking Rent 4Q11 - 1Q13




Please Note: As of 1Q12, the asking rents and availability rate of the Times Square submarket include the Bowtie region only. No 2011 data available for Flatiron, Meatpacking, & Lower Manhattan.

*Source: Cushman & Wakefield*

# NET LEASE TURNS UP THE HEAT

Net-leased properties are a hot commodity due to dwindling supply and high demand.

By Coleman Wood

The net-lease sector finds itself in an interesting place. On one hand, many brokers say a lack of high-quality supply is the biggest issue facing the sector. On the other hand, investors are having no problem finding deals.

Many brokerage firms finished 2012 with big increases in net-lease transaction activity. Real Capital Analytics reported year-over-year sales increases in nine of the past 10 quarters. However, with little new construction on the horizon, 2013 may see more investors competing for fewer deals.

The current net-lease market reads like a textbook example of a supply-demand imbalance. Investors abound, and they are armed with historically cheap debt and the promise of healthy returns.

"The problem is that there isn't nearly enough supply on the market to meet the demand," says Winston Orzechowski, research director for Reston, Va.-based Calkain Cos., which specializes in net-lease investments.

The reasons for this situation are threefold. First, the relative security of net-lease properties has made them a hot investment. According to Calkain, the average capitalization rate for net-lease retail properties has trended

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tailers. In 2012, 52 million tourists visited New York City, a new record and an increase of 2.1 percent over tourism numbers posted in 2011, according to the office of New York City Mayor Michael Bloomberg. In 2012, New York City welcomed an estimated 41 million domestic visitors and 11 million international visitors, which generated an estimated $55.3 billion in economic impact to the city's economy, including direct spending of $36.9 billion.

The local population is also a desirable demographic for retailers. "Manhattan is home to affluent, high-spending customers and we have a low square footage of retail per capita," says Spiegelman.

All of these factors play into the formula that has allowed rents to continue increasing.

"With average rents nearing $2,700 per square foot, Fifth Avenue is the leader by far — in terms of price per square foot, though not volume of transactions," says Michael Hofmann, senior managing director with Cassidy Turley. "Some of these retailers will spend a lot of money to get in front of people on Fifth Avenue, Madison Avenue or Times Square."

He continues, "Madison Avenue was hard hit [by the recession]. Rents dropped nearly 50 percent. But they've recovered quickly, with today's rents 30 percent higher than this time last year. Today asking rents — and some closing rents — are back up to $900 to

# Retail Markets to Watch in NYC

New York City is a patchwork of submarkets, each with its own retail character — and its unique business drivers. Tourists and international retailers may be driving record-high rents on the High Streets, but retail brokers predict opportunities worth watching in quite a few other markets.

## Financial District

With the development of the World Trade Center, Brookfield Place (formerly known as the World Financial Center) and the new transportation hub — all of which will bring a total of 550,000 square feet of retail space to the market — "downtown is really coming around," says Michael Hofmann of Cassidy Turley.

Approximately 365,000 square feet of retail and restaurant space at the World Trade Center and WTC Transportation Hub will open in spring 2015. The project, a joint venture between Westfield and the Port Authority of New York and New Jersey, will be known as Westfield World Trade Center.

The September 11 attacks split downtown New York City and eliminated the mega mall that had resided under the World Trade Center.

"As the World Trade Center is being rebuilt and marketed, you can see the Financial District becoming a more integrated market," Hofmann says. "Although retailers took a wait-and-see approach to the Financial District, the area is gaining momentum now."

Today, more than 1.2 million residents live within 15 minutes of the site, and approximately 500,000 commuters work in the area each weekday. Both the daytime and residential populations will grow rapidly as office buildings are completed and old office properties are converted to condos and apartments.

"Of course the World Trade Center is creating a lot of buzz downtown," says Chase Welles of SCG Retail. "Long-term, Wall Street will change dramatically."

In the short-term, though, downtown has taken a beating, says David Firestein, also with SCG Retail. "Retailers have not recovered from Hurricane Sandy, but recovery is months — not years — away. Second Avenue is also down on its luck because streets have been ripped up and doorways blocked to accommodate construction on the transportation hub. The market will come back when the subway project is complete."

## The Meatpacking District

"We are looking at a change in the profile of tenants in the Meatpacking District," reports Gene Spiegelman of Cushman & Wakefield.

He notes that Stella McCartney and Alexander McQueen are both leaving the submarket, while Sephora, Anthropologie and Levi's have moved into the market.

Alexander McQueen has just signed a lease on Madison Avenue on the Upper East Side; Stella McCartney is moving to SoHo. "I believe they are both moving to be closer to where they believe their core customer is," Spiegelman explains. "There is a changing vibe in the Meatpacking District. Their core customer is not as prevalent in current traffic patterns as in the past."

The Whitney Museum, which will open in 2015 on Gansevoort Street, will continue to change the neighborhood. The new building will include approximately 50,000 square feet of gallery space and 13,000 square feet of rooftop exhibition space.

"This is definitely a market in transition. What will be the trend line in terms of [retail] pricing here?" Spiegelman wonders.

## The Bowery

"The Bowery is one of the hottest markets in Manhattan," according to Ariel Schuster of RKF. "It is the new Meatpacking District."

He says, "Twenty-five years ago, SoHo was the up-and-coming market. Ten years ago, it was the Meatpacking District. Over the last 18 months, the Bowery has moved into position as the up-and-coming market to watch."

New tenants in the market include Anthropologie, Patagonia Surf and Intermix, as well as high-end French clothing store A.P.C.

"We are seeing many historically SoHo retailers move to the Bowery or open new stores here," Schuster says.

*Courtesy PANYNJ and Westfield*

The retail component at the World Trade Center will be known as Westfield World Trade Center; it represents a $1.22 billion joint venture between Westfield and the Port Authority of New York and New Jersey.

"There are also a lot of national tenants that want to grow beyond malls that are looking for urban locations and seek space in the Bowery, which attracts both New Yorkers and tourists."

## The Flatiron District

The Flatiron District, from 15th Street up to 25th Street, is another market to watch. This area, which includes lower Fifth Avenue, is a leader in the emergence of key apparel retailers, says Spiegelman.

He notes that Eataly has helped the Flatiron District become a tourist destination. Eataly is a unique mix of Italian restaurants and markets; each restaurant purchases fresh ingredients from the markets within the building. Eataly was founded by Oscar Farinetti in Italy in 2007. He collaborated with Mario Batali, Joe Bastianich, Lidia Matticchio Bastianich, Adam Saper and Alex Saper to bring the concept to the U.S. (The New York location of Eataly is the concept's first U.S. location. There are several locations in Italy and Japan; a second U.S. location will open this year in Chicago.)

"We will continue to see the Flatiron District rise and demand will remain aggressive," Spiegelman predicts.

## Hudson Yards

"Hudson Yards will have a dramatic effect on the far west side of the city," says Kelly Gedinsky of Winick Realty Group. "Essentially, we are adding an entire new market to the retail landscape."

Spiegelman agrees: "From a retail perspective, Hudson Yards will be a major emerging market over the next decade."

The Hudson Yards area is zoned for approximately 26 million square feet of new office development, 20,000 units of housing (almost 5,000 units will be affordable units), 2 million square feet of retail, and 3 million square feet of hotel space.

"With all of the residential space that will be constructed will come the need for retail to service the new residents," Gedinsky notes.

The workday traffic will be a boon to retail too. For starters, Coach will anchor the first office tower, after purchasing 600,000 square feet of space in the 47-story building that Related Cos. will develop. L'Oréal will occupy 402,000 square feet at the building for its U.S. headquarters.

Additionally, the 7 MTA subway line will be extended from its current terminus at Times Square to a new terminal station at 34th Street and 11th Avenue.

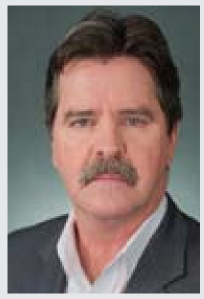
## Columbus Circle

The biggest news in New York retail is that Nordstrom plans to open a 285,000-square-foot store at 225 West 57th Street, between Broadway and Seventh Avenue, in 2018. The seven-story department store will be located at the base of a mixed-use tower developed by Extell Development Company.

"I am curious to see how the southern part of Columbus Circle will change," Spiegelman says. "What types of retailers will jump into this market in anticipation of Nordstrom opening?" — *Jaime Lackey*

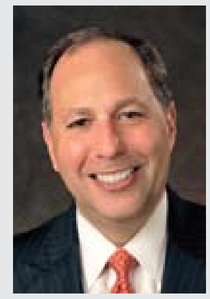
David Firestein,
managing partner,
SCG Retail

Kelly Gedinsky,
broker,
Winick Realty Group



Michael Hofmann
senior managing partner,
Cassidy Turley

Ariel Schuster,
executive vice president,
RKF



Gene Spiegelman,
executive vice president,
Cushman & Wakefield

Chase Welles,
partner,
SCG Retail

$1,200 per square foot."

As for Times Square, "It never lost its base and has continued to grow. Today, rents at Times Square are $2,000 per square foot, and SoHo's highest rents — located on Broadway — are approaching the $1,000-per-square-foot range," Hofmann says. "The East Side didn't fall as far but hasn't yet come back to pre-recession levels. Lower East Side is just starting to come back."

The makeup of some markets is changing, though. And the new dynamics may have a greater long-term impact on retail rents than the recession. For example, Hofmann notes, "The Upper East Side has practically become a mall. A few years ago, national retailers rushed in to replace local tenants, but these stores just aren't profitable for the chains and they are now moving out of the market, leaving many spaces available."

According to Spiegelman, Broadway, the Upper West Side and the Financial District are all coming back to or exceeding pre-recession levels. "On the East Side, in the mid-20s, rents are in the mid-$200 range, while availability is down to 8 or 9 percent," he adds.

According to Cushman & Wakefield, the overall availability rate in Manhattan is 9 percent, which is slightly below the national average. Cushman & Wakefield includes occupied space that can be delivered within 12 months in its availability rate. "True vacancy is probably 5 or 6 percent and even lower in some markets," Spiegelman says.

He adds, "Availability is actually up a little on Fifth Avenue and SoHo. Because investors are becoming quite aggressive, more owners are putting properties on the market, so availability is up even though vacancy is down. We'll have to watch to see how successful these plays are — what the taking rents will be."

Although luxury brands are driving the record-breaking rents, rental rates are up across all categories of retail space in most markets.

And where rents are too much of a stretch for retailers, we see expanding boundaries of submarkets, such as SoHo. "Just like Broadway became very commercial with high rents and tenants expanding to side streets in a way that expanded the market, traffic in SoHo is shifting and the boundaries of the market are growing as retailers sign side street leases to accommodate SoHo stores," says Kelly Gedinsky, a broker with Winick Realty Group.

David Firestein, managing partner of SCG Retail, agrees. "Rents are very strong in SoHo and the Meatpacking District, and along Bleecker, Madison and Fifth Avenue. These addresses are expensive. Retailers that cannot afford these rents move to other submarkets or do one-off deals just off the main streets. The food tenants are particularly attracted to this type of play," says Firestein.

For example, Starbucks couldn't justify the rent on Fifth Avenue or Madison in the upper 50s, so the company opened a location on 58th, the connecting side street, two doors down from UGG on the Madison corner. Apple anchors the Fifth Avenue corner of 58th Street. Before the rents skyrocketed, Starbucks would have occupied one of those corners.

## Branding vs. Profit

Which retailers pay the high rents — and are they doing so because the numbers work or are they taking a loss for the brand value of having a High Street location?

Jewelry and cosmetics have the margins to make money even at the highest rents, Hofmann says.

Spiegelman adds, "Some apparel retailers do $1,000 to $2,000 per square foot in sales."

These stores can make the rents work — and each store's P&L is more important than ever since the recession.

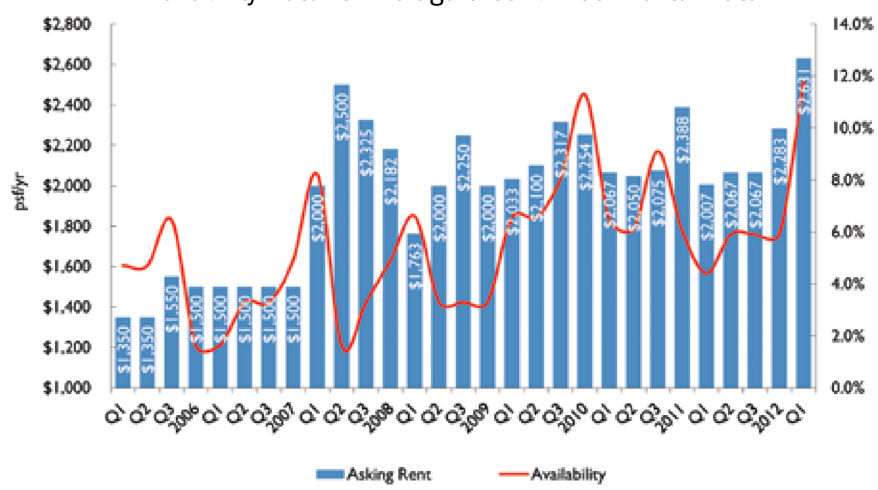
"Retailers do recognize the importance of being in Manhattan for branding purposes, but it is more and more difficult to reconcile doing a store with high occupancy costs in Manhattan if sales don't justify the rents," Spiegelman says.

Hofmann notes, "Generally, only the brands trying to get a foothold use location for branding. For most retailers, in-store sales must support the expense."

Firestein agrees: "An international retailer opening one U.S. store may choose location for branding purpos-

## Fifth Avenue Retail Market (49th - 60th)

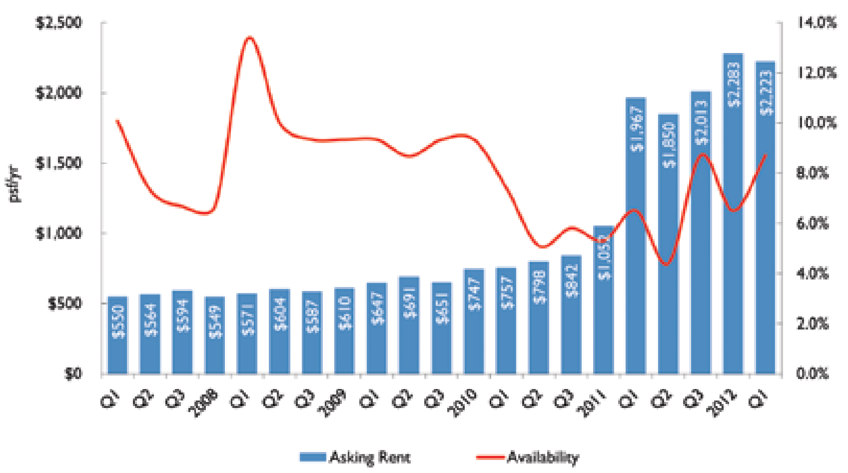
Availability Rate vs. Average Ground Floor Rental Rate




*Source: Cushman & Wakefield*

## Times Square Retail Market

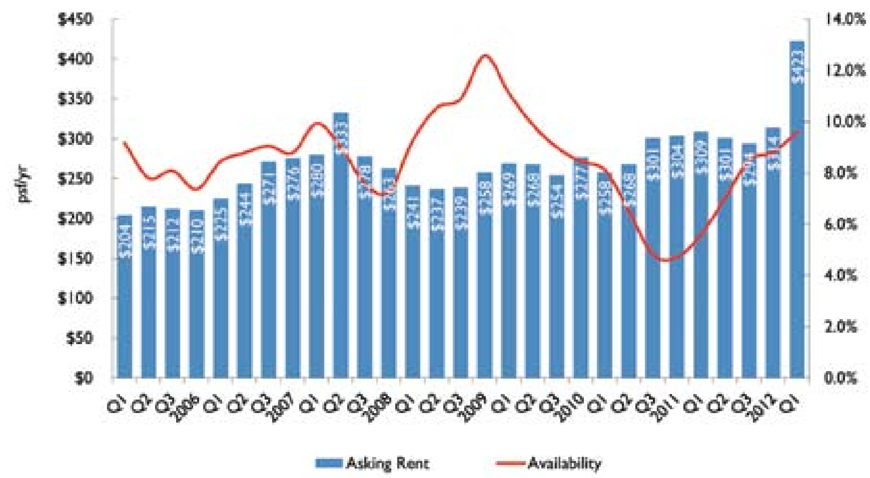
Availability Rate vs. Average Ground Floor Rental Rate




*Source: Cushman & Wakefield*

## SoHo Retail Market

Availability Rate vs. Average Ground Floor Rental Rate




*Source: Cushman & Wakefield*

es. But retailers rolling out multiple locations need their stores to make money."

And many retailers are willing to get creative to find space they can afford on the streets where they want to be.

"Often, retailers are willing to look at smaller stores or multilevel stores to blend the rental rate down," Firestein says. "It is harder to operate in a multilevel store but retailers are looking at the options."

As examples, Welles of SCG Retail, cites Whole Foods' successful two-story locations, like the one at Third & 87th, and he notes that Staples — which typically doesn't do multilevel stores in the suburbs — will consider them in the city because of the rents. Recent examples in New York City include stores at 43rd and Third and 39th and Fifth.

### Tenant Activity

While much of the retail industry worries about the negative impact Internet shopping can have on physical stores, Schuster notes that some successful e-commerce retailers see the benefit of bricks-and-mortar stores — at least in Manhattan.

For example Bonobos, which launched its website in 2007 with a focus on better-fitting men's pants, has opened a Bonobos Guideshop on 25th Street, one block from Fifth Avenue. This is an e-commerce showroom that offers one-on-one service to customers. The retailer opted for space on an office-level floor rather than a street-level storefront.



Warby Parker, which sells eyeglasses online, is another e-retailer that has found benefit in physical stores, with two locations in SoHo.

Retailers with existing stores in Manhattan are looking to make sure they have the best locations to connect with their customers.

Fashion designers Stella McCartney and Alexander McQueen are leaving the Meatpacking District. Stella McCartney is moving to SoHo, Alexander McQueen to Madison Avenue.

Swedish fast-fashion retailer H&M has signed a 57,000-square-foot lease at 589 Fifth Avenue; this will be the largest H&M store in the world. (There are rumors the company will vacate its store at 640 Fifth Avenue.) The company has also signed a lease at 4 Times Square for 42,500 square feet.

Apparel and accessories stores drive the most volume, according to Spiegelman. Some of today's lease transactions are also driven by drugstores, supermarkets and banks. The balance of leases are for food and restaurant tenants.

For example, Canada-based Joe Fresh, which offers affordable clothes for men, women and children, has four stores in Manhattan; Aritzia, a women's clothier also based in Canada, has opened stores in SoHo and on Fifth Avenue at 49th Street.

Welles, who exclusively represents Whole Foods in the metro area, says that Whole Foods deals last year included 125th Street in Harlem, Williamsburg in Brooklyn, and Third Avenue between 87th, and 88th on the Upper East Side.

Quick-service restaurants are very active, says Schuster. Among the most active are Pret A Manger, Chipotle and Potbelly Sandwich Shop.

Pharmacies are growing by leaps and bounds, says Hofmann.

"Drugstores are steady," Welles agrees. CVS/pharmacy has signed at Columbus Circle. Duane Reade (which merged with Walgreens but kept the popular Duane Reade brand name for New York City locations) is very active. ■