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## Bad Retail Climate Lets Strong Chains Expand At Discount

### Rents Down, Vacancies Up

With malls losing tenants, dollar stores add sites, often in better locales

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Retailers live and die by two sets of numbers: sales per square foot and rent per square foot.

With sales sluggish or worse and mall vacancies soaring, retailers are now asking landlords to slash rents. That's been a boon to those chains healthy enough to expand.

"The power is shifting from the landlord to the tenant," said Mitch Kaiser, an analyst with Piper Jaffray.

He estimates that store rents have fallen by 10%-20% in the last nine months.

"All retailers are trying or have tried to go to their landlords to either reduce occupancy costs or to try to terminate leases. The landlords are getting barraged," said Ivan Friedman, CEO of RCS Real Estate Advisors in New York City. RCS represents tenants in talks with landlords.

"It is a buying opportunity if you have the money to expand," he said.

### Price Right For Dollar Stores

Among those taking advantage of the new rents are off-price discounters whose sales have held up well as consumers seek bargains.

"The dollar stores are picking up leases for \$2-\$5 a square foot that would not have been available for less than \$10," Friedman noted.

It's not just that rents are cheap. Chains with the cash to finance growth internally can move into better strip malls and shopping centers.

The off-price retailers "have a lot more choice on where to go and what to pay," said Michael Burden, a principal with Excess Space Retail Services, a private firm in Lake Success, New York, that also represents tenants.

This doesn't mean high-end malls, where they would seem out of place.

"If they could be on 5th Avenue it wouldn't do them any good," said Burden. But they can "move up a little bit." Instead of leasing in an older strip mall, they might move in to a new or refurbished mall.

Family Dollar (FDO), Dollar General, Dollar Tree (DLTR), Big Lots (BIG) and 99 Cents Only (NDN) are likely to benefit from plunging rents, Kaiser said. He was recently at a real estate conference and noticed landlords swarming around discounters' booths. Little wonder: Shopping centers and malls are suffering a pandemic of store closings. The retail vacancy rate soared to a longtime high of 9% in Q1, reports **Marcus & Millichap Research.**

The National Association of Realtors predicts the retail vacancy rate will rise to 15.8% in 2010.



Big Lots plans to open 45 stores this year. The chain benefits from sinking rents and an abundance of expansion sites, said Tim Johnson, vice president of strategic planning and investor relations. Until recently, he added, Big Lots had only limited presence in the Northeast because of "prohibitive" rents. "Now we're seeing more opportunities," said Johnson.

Big Lots expects to open 10 to 15 stores in the Northeast, up sharply from the recent pace of three to five annual openings. Big Lots has also been able to win better terms from landlords on older leases up for renewal. "We have received some sort of concession on all 250 lease renewals," said Johnson.

Indianapolis-based electronics retailer HHGregg (HGG) has "a big opportunity" to grow its "footprint," said Kaiser. The chain plans to add 16-18 stores by April 2010 to its base of 111 stores. Lower rents and overall landlord "flexibility" have helped, chief operating officer Dennis May told analysts on

June 2.

Citi Trends (CTRN), an apparel chain that caters to African-Americans, is another growth candidate, says JPMorgan analyst Evren Kopelman. The Savannah, Ga.-based retailer had 365 stores at the end of April, mostly in southern cities. But with no debt, a fair amount of cash and rock-bottom opening costs, Citi Trends can double its store base over five or six years, Kopelman reckons. "They will definitely benefit from lower leasing rates," she said.

Two others poised to benefit are Coach (COH) and Ross Stores (ROST), she adds. Both chains have "strong" balance sheets. The lower rents should let Citi Trends, Coach and Ross expand profit margins.

### No End In Sight?

Some industry insiders believe that rents could fall much further as more retailers file for bankruptcy. To this point, many have been hesitant to file for Chapter 11 because there is no easy exit. With no credit for debtor-in-possession financing, firms like Circuit City and Linens 'n Things that have filed have had little choice but to liquidate eventually.

So a thaw in credit markets could have the ironic effect of unleashing a flood of retail bankruptcies. With credit available, struggling chains would gamble on going bankrupt and restructuring with new debt. But this would likely involve numerous store closings, further swelling vacancies and pressuring rents.

One company able to negotiate lower rents and emerge from bankruptcy is Buffet's Inc. By reworking 177 leases, the restaurant chain will save \$24 million in coming years, said Bill Sullivan, a partner with Huntley, Mulaney, Spargo & Sullivan, which helped Buffet's in talks.

But many that file for bankruptcy are forced to liquidate. This can create great cut-rate leasing opportunities for others. The defunct West Coast retailer Mervyn's was able to auction off its leases because they were at below-market rents. Kohl's (KSS) and Forever 21 picked up 46 leases for just over \$6 million. Friedman estimates that the leases were worth at least \$20 million.

For some, at least, the deflation of commercial real estate is a breath of fresh air.