

Q&A



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Urban Retail: Assessing the Damage

The financial crisis continues to reverberate throughout the world's economy. Against this backdrop, we sat down with Madison Retail Group's New York Principal, Stephen Stephanou and Madison Marquette's San Francisco-based Director of Investments, Chad Eisenbud to get their thoughts on how America's major urban centers are faring.

Q: How is the financial crisis impacting major urban centers in the U.S.?

CE: In San Francisco, the giant financial firms control 4.2 million square feet of office space in and around the city. We expect to lose about 500,000 square feet from consolidation by companies such as AIG, Wachovia, Washington Mutual, Lehman Brothers and Merrill Lynch. Wells Fargo, however, is now a national retail banking powerhouse because of the Wachovia acquisition and that designation will only increase the city's reputation as a dominant financial center.

Seattle too will suffer from the loss of Washington Mutual — especially since they had recently constructed a large downtown headquarters building. The company employed 4,300 people in the area.

SS: The financial crisis has been a devastating blow to Manhattan. The loss of tens of thousands of jobs and a growing sense of uncertainty has created a cloud over the city that won't soon dissipate. That said, New York is a very resilient city and remains an enormous economic engine. Although government intervention will funnel a great deal of money to Washington, D.C., New York City is still the financial capital of the world.

What has kept the city on steady footing in the past year has been foreign tourism encouraged by a weak dollar. However, this safety net is now in doubt because of the global nature of the financial crisis and the gradual recovery of the dollar.

CE: Although the financial crisis will most directly impact the downtown in commercial real estate, the housing bust and related development fallout is being most acutely felt in emerging submarkets. In San Francisco, some outlying exurban areas have seen home prices fall as much as 50% in the last year.



New York, New York



San Francisco, California

SS: Another major fallout of the tough economic climate is the tightening of business travel budgets. Many restaurants and hotels in Manhattan are now struggling because of it.

Q: What is happening to urban retail rents?

SS: We are definitely witnessing a rise in vacancies and a pullback from national retailers. Some are even pulling back from done deals. For their part, landlords with strong financials are refusing to lower rents because that would lower overall property valuations. This stalemate will continue until a clearer picture emerges of when the economy will turn around.

Most of the deals getting done now are sub-leases. These deals are particularly difficult to close because of the resistance from landlords and because most retailers have scrapped expansion plans.

CE: San Francisco's Union Square is starting to see some vacancies, but overall the rental rates for retail have remained strong. We still see tremendous opportunity for developers who can acquire large parcels in San Francisco's in-fill locations.

Q: Are certain retailers doing better than others?

CE: Most agree that value-oriented retailers are benefiting from the lean economic times. Many of these retailers are taking advantage of developers who are desperate to have them. Target is a standout and

one that continues to aggressively seek new store opportunities in good markets.

SS: It used to be thought that luxury retail was immune from downturns. That may be true in some instances, but overall we are seeing luxury consumers willing to compromise higher quality products for basic goods and services. Anecdotally, I am hearing from restaurants that while food sales are down, alcohol sales are way up.

Q: Will urban revitalization be halted by the slowdown?

SS: There is no doubt that emerging neighborhoods will not evolve as quickly as they did two or three years ago. However, the fundamental demand for more convenient, urban living will continue to drive redevelopment.

CE: Housing is the key driver in most emerging neighborhoods and right now the financing environment is such that the young professionals who traditionally live in these areas are having trouble getting a mortgage.

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