

Houston's retail market seeks balance between bricks and clicks

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Retail Trends

Commentary by Hal P. Colbert, Senior Vice President

The advent of the internet and online shopping created rhetoric about the end of brick and mortar retail and the retail apocalypse was just around the corner as brick and mortar retail's end was near.

Now years after these predictions, studies show that brick and mortar isn't going away anytime soon. True, some retailers who either couldn't or didn't adapt have failed and fallen by the wayside. Thus bringing us to a new phase of retail where retailers have right-sized, adapted and are thriving, proving that the hysteria over "clicks" will kill "bricks" has not been a valid conclusion; however, the jury remains out as we live in a continually evolving world and the end is not yet in sight.

There have been several studies recently that have all come to the same conclusion, that clicks drive bricks and vice versa. According to a recent ICSC study of over 9,000 adults in 9 countries statistically showing that across all age categories (millennials, Generation X and baby boomers) clicks benefit bricks and sales increase in clicks when a physical store is nearby. ICSC calls this the Halo Effect whereby an impression created in one area affects another. 55% of the global study group thinks a nearby physical store is important to them when making online purchases as they generate brand awareness and trust. The study also found that opening a new store boosts online traffic while store closings decrease online traffic. The industry refers to the modern approach to retail marketing as Omni-Channel. The concept is to catch the consumer's attention in as many ways as possible, leveraging the daily habits of consumers including social media, online shopping, and physical stores to stay in front of consumers and increase brand engagement. It is not an either/or strategy, but rather an all of the above. Case in point of traditional web-only retailers opening physical stores here in Houston are Amazon, Indochina, Untuckit opening in the Galleria Mall and Warby Parkers new store in Highland Village.

Market Indicators Relative to prior period	Annual Change	Quarterly Change	Quarterly Forecast*
VACANCY	↑	↑	↑
NET ABSORPTION	↓	—	↓
NEW CONSTRUCTION	↑	↑	—
UNDER CONSTRUCTION	↓	↓	—

*Projected

Summary Statistics Houston Retail Market	Q1 2018	Q4 2018	Q1 2019
Vacancy Rate	5.2%	5.3%	5.4%
Net Absorption (SF) (million square feet)	0.9M	0.4M	0.4M
New Construction (SF) (million square feet)	0.6M	0.4M	0.7M
Under Construction (SF) (million square feet)	3.2M	1.1M	0.5M
Asking Rents Per Square Foot Per Year			
Average NNN	\$15.46	\$15.91	\$16.17
Neighborhood Centers	\$14.65	\$15.00	\$15.39
Strip Centers	\$19.10	\$19.59	\$19.52

The above asking rents are an average of all property types and classes that are currently listed with an asking rate. This average does not include properties that are fully leased or that do not list an asking rate. Please see page 2 of this report for an expanded discussion of retail rental rates.

Retail Trends - continued

Research further shows that people who order online and pick up in-store will purchase more items when picking up their online purchase. Today, online sales account for only 12% of total retail sales. That number will grow over time and the retailers who embrace the all of the above strategy will be the winners in the new retail reality.

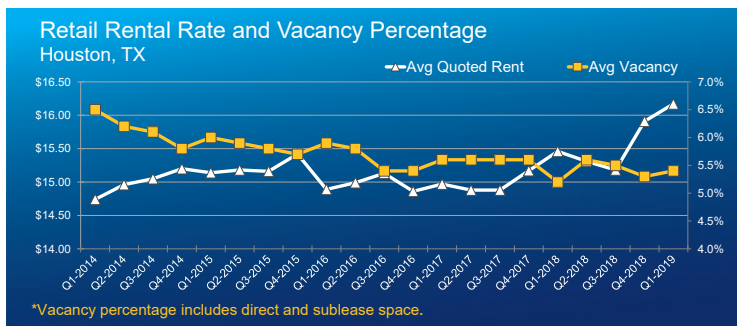
The retail industry is reinventing itself and it isn't just bricks or clicks, but about developing a strategy that works for a shopper using internet connected technology that changes the way they shop, and creative retailers are using the new technologies to innovate and attempt to stay ahead of the curve. So now retailers are going from a clicks to bricks mentality and brick and mortar stores are still as relevant as ever. A new trend is developing as retailers reinvent and seek that balance between clicks and bricks.

Technology is evolving at a faster pace and affects all facets of our lives, how we work, how we shop and how we live. Service and goods providers who adapt and embrace this changing world will succeed, while those who don't will become a spot in history. The one constant obviously is change.

Vacancy & Availability

Houston's average retail vacancy rate rose only 10 basis points between quarters from 5.3% in Q4 2018 to 5.4%. At the end of the first quarter, Houston had 15.6M SF of vacant retail space on the market. Among the major property types, single-tenant retail and lifestyle centers had the lowest vacancy rate of 1.5%, followed by theme/entertainment at 1.6%, and malls at 3.2%. Outlet centers have the highest vacancy rate of 12.4%, followed by neighborhood centers with a vacancy rate of 8.6% and then strip centers at 8.2%.

Twenty-one buildings delivered in Q1 2019 adding 0.7M SF to Houston's retail inventory. Approximately 74% of the new inventory delivered pre-leased. There is currently 1.0M SF of retail space under construction of which 66% is pre-leased. The majority of the projects under construction are located in the outlying suburban submarkets adjacent to rapidly growing residential developments. There are several H-E-B grocery stores under construction. A Costco Wholesale and a Home Source are underway in Cypress, TX. Some of the strip centers currently under construction include Riverstone Place, Parkway Marketplace and Lyric Market Food Hall.



Job Growth & Unemployment

(not seasonally adjusted)

UNEMPLOYMENT	2/18	2/19
HOUSTON	4.7%	4.2%
TEXAS	4.1%	3.9%
U.S.	4.4%	4.1%

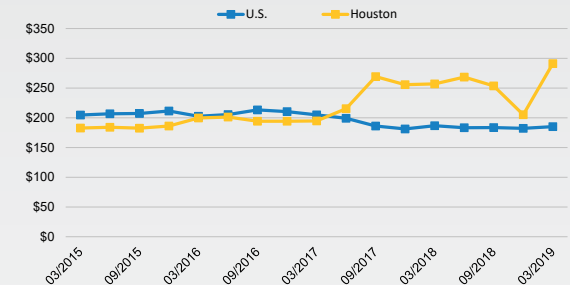
JOB GROWTH	Annual Change	# of Jobs Added
HOUSTON	2.4%	72.6K
TEXAS	2.2%	273.2K
U.S.	1.7%	2.5M

Sales Activity

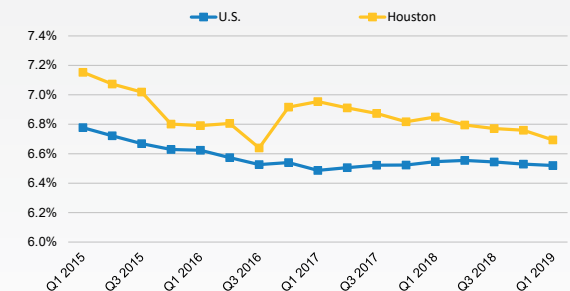
Source: Real Capital Analytics

	Q1 2019
NO. OF PROPERTIES:	30
TOTAL SF:	0.9M
AVERAGE \$/SF:	\$291
AVERAGE CAP RATE:	6.8%

Average Price Per SF



Average CAP Rate



Rental Rates

According to CoStar, our data provider, Houston's citywide average quoted retail rental rate for all property types increased by almost 2.0% between quarters from \$15.91 per SF NNN in Q4 2018 to \$16.17 per SF NNN. These average rental rates are typically much lower than actual deal rates since they include all retail property types and classes, the majority of those properties are not well leased and are listed with discounted asking rates. According to Colliers' internal data, Class A in-line retail rental rates can vary widely from \$30.00 to \$85.00 per SF, depending on location and property type.

Absorption & Demand

Houston's retail market posted 0.4M SF of positive net absorption in the first quarter, a significant decrease from the 0.9M SF of positive net absorption posted in the same quarter of the previous year. Some of the positive absorption can be attributed to tenants that expanded into new locations. Among those tenants are Powerhouse Gym, Club Izel, HomeGoods, Melrose Apparel, Gift Baskets, Caliber Collision, Q Shop Bistro and Big City Wings.

Leasing Activity

Houston's retail leasing activity, which includes renewals, decreased over the quarter from 1.5M SF in Q4 2018 to 1.2M SF in Q1 2019. Some of the tenants that signed leases during the first quarter are listed in the table below.

Q1 2019 Select Retail Lease Transactions				
BUILDING NAME/ADDRESS	SUBMARKET	SF	TENANT	LEASE DATE
Baybrook Village	Southeast Outlier	46,000	Burlington ²	Feb-19
Market Square at Eldridge Parkway	Far West	27,100	PetSmart ²	Jan-19
Miracle Corners Shopping Center	Near Southeast	25,700	Crazy Boss ¹	Mar-19
White Oak Bayou Village	Near Northwest Oaks	24,300	American Freight & Furniture ¹	Mar-19
17955 North Freeway	Far North	20,100	Image Furniture ¹	Feb-19
Deerbrook Plaza Shopping Center	Spring Creek	15,300	Rainbow ¹	Jan-19
Steeplechase Plaza	Jersey Village	12,540	Kanga's Indoor Playcenter ^{1,3}	Mar-19

¹Direct/New

²Renewal/Extension

³Colliers International Transaction

Market Summary

Q1 2019 Retail Market Statistical Summary									
PROPERTY TYPE	RENTABLE AREA	DIRECT VACANT SF	DIRECT VACANCY RATE	SUBLET VACANT SF	SUBLET VACANCY RATE	TOTAL VACANT SF	TOTAL VACANCY RATE	4Q18 NET ABSORPTION	CLASS A RENTAL RATES (IN-LINE*)
Strip Centers (unanchored)	37,101,080	3,014,227	8.1%	19,481	0.1%	3,033,708	8.2%	(60,936)	\$27.00-\$45.00
Neighborhood Centers (one anchor)	70,815,229	5,968,570	8.4%	114,649	0.2%	6,083,219	8.6%	28,461	\$28.00-\$46.00
Community Centers (two anchors)	47,666,256	2,705,066	5.7%	76,725	0.2%	2,781,791	5.8%	247,443	\$28.00-\$45.00
Power Centers (three or > anchors)	28,922,276	1,636,588	5.7%	200	0.0%	1,636,788	5.7%	(24,523)	\$28.00-\$45.00
Lifestyle Centers	6,100,390	94,452	1.5%	-	0.0%	94,452	1.5%	18,714	\$40.00-\$85.00
Outlet Centers	1,393,543	172,266	12.4%	-	0.0%	172,266	12.4%	19,072	\$20.00-\$40.00
Theme/Entertainment	761,488	12,238	1.6%	-	0.0%	12,238	1.6%	3,100	\$25.00-\$35.00
Single-Tenant	73,403,177	1,017,855	1.4%	117,585	0.2%	1,135,440	1.5%	116,244	N/A
Malls	21,258,525	670,391	3.2%	12,397	0.1%	682,788	3.2%	8,689	N/A
GREATER HOUSTON	287,421,964	15,291,653	5.3%	341,037	0.1%	15,632,690	5.4%	356,264	



Q1 2019 Houston Retail Highlights

TOTAL RETAIL INVENTORY **287.4M SF**



95%
OCCUPANCY

LEASING ACTIVITY



20%
QUARTERLY

Q1 2019	1.2M SF
Q4 2018	1.5M SF
Q3 2018	1.3M SF
Q2 2018	1.5M SF
Q1 2018	1.7M SF

CURRENT

5.4%
VACANCY

0.4M SF
NET ABSORPTION



1.0M SF

FOR MORE INFORMATION

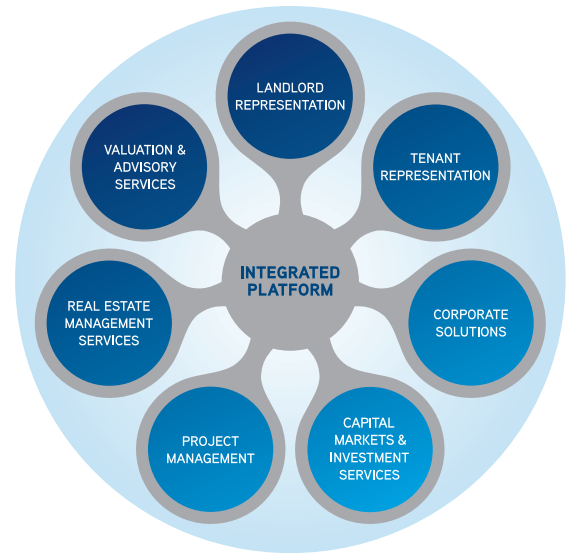
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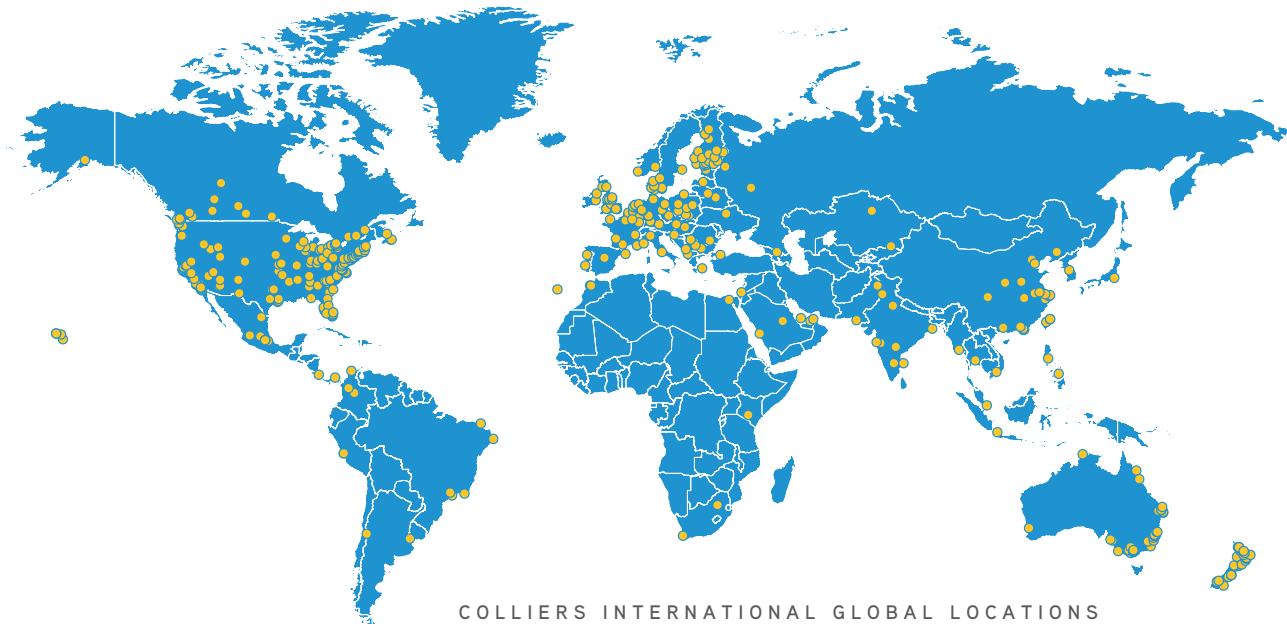
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COLLIERS INTERNATIONAL GLOBAL LOCATIONS



\$127B
TRANSACTION VALUE



2B
SF UNDER MANAGEMENT



\$3.3B
IN REVENUE



438
OFFICES



17,300
PROFESSIONALS



340
ACCREDITED MEMBERS



68
COUNTRIES