A Colorado Real Estate Journal Publication

February 2024

RETAIL PROPERTIES *Quarterly*

What to watch: Shopping center management

Several retail shopping center landlord representatives recently got together at a networking event and we inevitably got to talking about the latest trends, challenges and innovations in the industry. There is always a great wealth of information shared at these events, but three concepts kept emerging in the discussion that seemed to be a big focus for shopping center owners and property managers in 2024: enhancing security measures affordably, complying with existing and planning for future environmental legislation and innovating lease negotiation structures.

■ **Implementing cost-effective security measures to address property crime.** A significant concern for landlords and property managers continues to be the high incidence of property crimes at retail shopping centers, an issue that not only affects the safety and well-being of tenants and shoppers but also impacts the financial health of retail spaces. While a representative of the Downtown Denver Partnership noted that the three-year average for property crime is down more than 40% from its post-COVID peak in the city, that trend seems to be lagging in many suburbs, and most landlords cited continued issues and costs related to vagrancy and crime as a major ongoing concern going into 2024.

Ross Carpenter
Director of leasing, NewMark Merrill Companies Inc.

An individual with knowledge of Belmar shopping center in Lakewood, for instance, noted the center is now spending roughly $900,000 per year on private security at the site, in addition to signing a free temporary lease agreement with the police department to increase the police presence and deter crime at the center.

Most of the landlord representatives noted that they have experienced a significant rise in break-ins, theft of copper pipes and wiring, and tenant closures directly or indirectly related to these issues in the post-COVID era. On-site security staff play an important role, but the group underscored the importance of finding more cost-effective solutions given that the burden of increased security is most often borne by shopping center tenants. We have been testing a variety of AI-powered interactive camera solutions from several vendors as a way to supplement existing security measures. An on-the-ground security presence is critical in some cases, but we have found that these monitored camera systems are often able to provide better petty crime deterrence at a small fraction of the cost of on-site security. The key for landlords will be finding a balanced approach, leveraging guards and technology to create safer retail environments while managing costs efficiently.

Please see Carpenter, Page 15

INSIDE

Carpenter

Continued from Page 1

■ **Navigating upcoming environmental legislation.** Another focal point of the discussion was the challenge of complying with upcoming and often nebulous municipal and state environmental legislation, notably the Energize Denver ordinance and Colorado's Benchmarking and Building Performance Standards statute (HB 21-1286). The BPS program generally requires retail (and other commercial buildings) larger than 50,000 square feet to reduce their greenhouse gas emissions from the 2021 benchmark by 7% in 2026, and 20% by 2030. The regulation is nuanced and complex, and the compliance details are still being crafted.

Most thoughtful landlords and property managers are proactively working with consultants, vendors and attorneys to craft multiyear strategies to meet these new guidelines. These strategies are not only about meeting the legal requirements for compliance but also about enhancing the energy efficiency of buildings, thereby offering utility expense savings to tenants and contributing to a reduction in the Colorado retail sector's carbon footprint. With an estimated 300 million sf of retail space in Colorado, the potential environmental benefit of these efforts can be substantial, but it may also pose a significant risk to landlords and retailers who don't proactively address the possible capital investment required in new roofing, HVAC and lighting systems necessary to meet the benchmark requirements in their buildings.

■ **Simplifying lease negotiation with fixed CAM.** The process of negotiating retail leases has become increasingly lengthy, complex and costly due to growing tenant demands and evolving market dynamics. In response, some landlords in Colorado are pioneering a shift from a long negotiation about what is included in the tenant-reimbursed common area maintenance charges toward a fixed CAM escalation structure to streamline lease negotiations and reduce associated costs. While this model promises to save time in the leasing phase and potentially reduce negotiation-related costs, it also poses risks for landlords. The representatives implementing this fixed CAM model stressed the importance of careful consideration and implementation of these structures to avoid creating financial liabilities in the face of potential inflation. This emerging trend reflects a broader industry movement toward simplifying and standardizing lease terms, in an effort to make the negotiation process more efficient and transparent for all parties involved.

The collective wisdom shared among this networking group underscores the multifaceted nature of managing retail real estate in an era marked by rapid change. By adopting innovative solutions in security, environmental compliance and lease negotiations, landlords and property managers are navigating these challenges with a strategic eye toward the future, setting new standards for the sustainable and efficient management of retail spaces. ▲

rcarpenter@nmc-mountainstates.com

Flint

Continued from Page 4

metro average. Rising rents have the potential to be alleviated by upcoming construction projects, mostly taking place where the space is in suburban markets.

All in all, the retail real estate market in Colorado has absorbed each lesson taught by every recent downturn, and shows us that it can consistently come back stronger than ever. Through each cycle, brick and mortar retail stores have proved to be essential, due to the transformation the stores can undertake. The demand for physical retail space remains high, proven by the occupancy throughout the whole metro area.

With the combination of economic momentum and expectation of a few decreases in national interest rate, we hope to see what seems to be the continued growth of high activity in the Colorado retail market. ▲

cameron.flint@cbre.com

Balafas

Continued from Page 8

about 5% to 6% of retail space is open, but this percentage lowers to 2% when competing for the most sought-after trade areas. In third-quarter 2023, average asking rent in metro Denver increased to $19.90 per sf.

Nationally, CoStar Group notes particular strength in convenience centers where average asking rents reached a record-high $20.37 per sf in the third quarter, a 17.3% increase compared with the same period in 2019. The rate of available space in strip centers fell to 5.3%, representing the tightest level of supply on record.

One additional distraction, a benefit to some landlords and a challenge for others, is what LaSalvia describes in a Scotsman Guide article this month as "retail rent by vintage." In the majority of metros around the country, LaSalvia finds that there is a rent premium of 50% to 100% for properties built in the past decade.

■ **Landlords, rents affect independent retailers**. All of this leverage has downsides for retail variety, growth and support for independently owned businesses. In a New York Times interview, Stacy Mitchell, a co-executive director of the Institute for Local Self-Reliance, a nonprofit advocate for independent businesses, suggests that while national chains might be a safer financial choice when compared to independent entrepreneurs, leasing to the giants is shortsighted because it makes every city look the same. In New York, independent retailers have always been a draw for regional shoppers bound for city adventures. Several small retailers in the city are attempting to cope with significant rent increases by adding their own pop-up stores within their leased space and reaching out to shoppers at community events, among other tactics. Similarly, we may need to ask ourselves what type of legacy we leave behind for destination shopping areas like the Highlands, River North, South Broadway and, soon, Colfax.

■ **Big investors get into the game.** Institutional investors and private equity firms that once shunned retail based on their limited exposure to news about mall declines are now populating their portfolios with grocery stores, pharmacies and other recession- and online-resilient stores such as free-standing pharmacies, gas stations, convenience stores, and auto-part retailers, which may add to the inventory squeeze. Despite this, we believe there is still plenty of room for a variety of in-market retail real estate investors and landlords whose local knowledge and influence remain significant.

■ **Peering into crystal balls.** Moody's Analytics Senior Economist Ermengarde Jabir remains cautious to bullish on 2024's retail real estate outlook, particularly neighborhood retail in densely populated urban and suburban areas. While e-commerce continues to grow, it only makes up about 15% of all retail, and he posits that there's plenty of room for brick-and-mortar operators. According to Jabir, "Retail will emerge as a stalwart in 2024. The asset class is expected to experience steady performance, with unchanging (low) vacancy rates and moderately positive rent growth."

Unfortunately, we can't foresee how long retail real estate will remain a healthy business sector due to any number of larger economic factors:

- What will the Fed do with interest rates?
- Will giant investors and private equity firms cherry-pick the best properties, pushing out smaller developers/investors who are still motivated to grow?
- Will shoppers pull back because they've hit their credit limits or spent their remaining COVID-19 savings?
- How will the increasing costs of consumer goods further affect shopping preferences?
- When, and how quickly, will the retail construction pipeline move forward?
- Are investor-developers willing to rehab their older properties for repositioning?

We remain downright optimistic, bullish even, that retail real estate will continue on its profitability path for some time, considering the challenges of limited, new construction and the demand we're seeing for space overall. If your predictions differ, drop me a line so we can get smarter together. ▲

jbalafas@kentrogroup.com

Wright

Continued from Page 11

investment properties in Colorado and has received strong interest and feedback from the net lease community.

■ **Pro-business states.** Many STNL investors are seeking investments in pro-business states and markets. These investors are seeking favorable tax treatment and believe in the long-term prosperity of these markets. There are currently nine income tax-free states, including Texas, Tennessee, Florida, Wyoming and Washington, which are commanding premiums. Many investors are seeking properties in pro-business environments throughout the Southeast that have experienced robust recent population growth due to a lower cost of living and favorable business policies.

Moving forward, we anticipate STNL investors to continue to scrutinize and evaluate opportunities more thoroughly and to take advantage of their increased negotiating power. It's nearly impossible to find the perfect deal that checks every box, and investors typically must sacrifice something. Properties with attractive real estate fundamentals, long-term leases with strong rental increase schedules, and locations in pro-business growth markets will be at the forefront of investor demand and continue to receive premium pricing. ▲

Brandon@bouldergroup.com
Zach@bouldergroup.com

McNeely

Continued from Page 12

gain insights into challenges impacting your property:

☑ **Local partnerships.** Build positive relationships with local businesses, organizations, and government entities to contribute positively to the community and enhance an investment property's overall reputation.

☑ **Stay informed,** Be aware of any zoning changes, applications and permits, and pending development projects that may impact your community, the real estate market, and your commercial properties.

■ **Stay up to date: Laws and regulations, market trends.** Legislative changes and real estate industry trends can impact an investment property. As such, your property asset management strategy should include looking into developments regarding:

☑ Energy improvements. Stay compliant with energy requirements like LEED, indoor air quality and lighting standards for enhanced property efficiency.

☑ **Mechanical system upgrades.** Be aware of the push to eliminate gas furnaces, and explore alternatives and potential financial impacts on your investment returns.

☑ **Market trends.** Stay informed on general market trends and macroeconomic factors that may impact your real estate portfolio.

☑ **For Denver and Colorado owners in particular:** Stay informed about Colorado's new energy legislation, including Energize Denver, affecting building performance standards. Consult with your property manager to assess potential impacts. Also, the city of Denver's website provides Resources for Building Owners.

By diligently addressing the components outlined in this property asset management checklist to maximize value, owners can position their investments for success.

Proactive management strategies, coupled with an awareness of real estate market trends and tenant needs, will not only maximize property values but also contribute to sustained growth and increased net operating income. Staying ahead of the curve will be the key to long-term success in commercial real estate asset management. ▲

bryce@bluewestcapital.com