RENOVATION & INNOVATION
IN OLDER STRIP SHOPPING CENTERS

by

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Renovation and Innovation in Older Strip Shopping Centers

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ABSTRACT

Perhaps one of the most underutilized and ubiquitous real estate assets in America today is the strip shopping center or strip. These small centers, typically under 100,000 sq. feet in size, were largely developed in the 1940s and 1950s. Often the developers were home builders who had moved to the suburbs to provide for the housing needs of our returning veterans.

Originally intended as grocery and personal service centers, these centers suffered as new community centers of 200-300 thousand square feet soon appeared, only to be followed by regional malls that often exceeded one million square feet of retail space.

Of late, there has been a renewed interest in the strip, owning to demographic changes within our society and structural changes within the retailing industry. This paper examines the evolution of the strip center and looks at some of the methods that savvy developers are using to create interest, value and amenity in these valuable commercial properties.
RENOVATION & INNOVATION 
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This thesis will examine the redevelopment potential and profit opportunities available in older strip shopping centers. The work presented is not site specific, but rather focuses on strip centers as a rather ubiquitous and often underutilized source of development potential. I have generally limited these discussions to strips of 100,000 sq. ft. or less, although many of the rehabilitation concepts would apply equally well to much larger regional centers.

When I began this thesis, I frankly thought that I had stumbled upon an overlooked area of real estate potential. However, given the amount of printed material published on the subject, and the large numbers of developers who have undertaken center redevelopment, I now realize that I am scarcely pioneering.

As my personal background in the development business has been confined to residential land subdivision, I felt it necessary to begin at the beginning with a strict set of working definitions as to the types of retailing facilities
and their relative rankings in terms of both sales generated and the relative quantity of stock (square feet) in existence. Also, in order to understand the "vintage" of these older strips, and the retailing and regulatory environment in which they were constructed, I have included a short history of constructed retailing facilities. To those readers experienced in retailing, these two introductory sections may be superfluous.

What I would like to accomplish via this writing is a thoughtful look at what others have done to rejuvenate older centers, express some thoughts on the peculiarities of this type of investment, and present some hypothetical conjuncturing about theme centers that may correspond well to emerging demographic and retailing trends. It is my hope that by assembling these many thoughts on strip center redevelopment, I may have produced a good primer for the inexperienced developer contemplating the acquisition of an underutilized strip.
In order to gain some perspective on the historical context and business climate in which older strip shopping centers were developed, it is necessary to supply a brief overview of retail development. The same forces that produced the strip shopping center may be in part responsible for their resurgence.

The American shopping center industry did not begin in America. The tradition of a central marketplace where people assemble to conduct commerce has existed for centuries. In colonial America, the major seaports—among them, Boston, New York, and Philadelphia—served as the major trading centers as they stood as the most convenient locations for shipping and receiving goods from other countries. As the colonists spread inland, it was primarily water access that determined a city's ultimate potential as a center of commerce and industry. Water access was the key to goods transport and was therefore crucial to commercial development.

Concurrent with the growth of major commercial ports, small towns in the Midwest and West emulated the "town square" concept already well proven in the New England...
States. Here the townspeople would gather to buy and sell all manner of merchandise from the public square areas. These later developed into the downtown districts that are common today. The public squares also served important social and civic goals, as they contained the town meeting halls, schools and churches.

Two important themes that continue to dominate retailing can be shown to have their roots in these earliest of colonial times. First, major trading centers tend to be concentrated in areas that are most accessible to both people and transportation. The factors of location and trading areas continue to be two of the most important determinants of retailing success or failure. They are also two of the primary factors in the resurgence of strip centers as viable retailing facilities.

The second theme that emerged from colonial times is the idea that the center was provided to serve all of a buyer's shopping needs. Separate markets for food, clothing, and hard goods were all found at the village center. There were also important social and community needs being met, although "fulfilling the need for social interaction" probably never occurred on anyone's shopping list. The desire for one-stop convenience retailing was later met by the regional mall but strip centers are again capitalizing on their particular brand of convenience amenities.
During the later 1800s, the Industrial Revolution first took hold of the nation and brought about permanent changes to the working life, economic means and consumption habits of the American public. New more efficient means of production emerged making available greatly increased quantities of consumables and the economic means to afford them.

Coupled with the new methods of production came new means of distribution. Most significant of these to retailing was the widespread use of the automobile in the 1900s. The family automobile allowed new freedom of travel, and was a significant contributor to the rise of the regional mall. As a result, a distinguishing feature of most shopping centers is the availability of free, convenient, and plentiful on-site parking.

The most significant events effecting retailing in the 20th century were the explosive population growth that occurred following the end of WW II, and the related demographic changes that occurred following the rebirth of the "American Dream". The dream— the dream of owning a home—had previously been unattainable by many Americans. The government moved aggressively to stimulate housing production with a host of federally sponsored programs. For war veterans, there were mortgage loans backed by Veteran Administration guarantees. The Federal Housing
Administration (FHA) was established. President Eisenhower initiated the interstate highway program that made it easier for suburbanites to commute to and from the city. There were also federal programs to aid suburban communities in educational programs and in sanitation services. Along with a simple desire of many people to leave the problems and congestion of the city behind, these factors combined to produce a mass exodus from the cities to the suburbs.

Shopping center developers followed the population into the suburbs. They began by building strips, small neighborhood centers that typically contained from ten to twelve tenants. The stores were often designed (or if you prefer, not designed) in the long straight lines common in the tract housing developments being built around the strips. Often the centers were located on the fringe areas of large scale residential development, and not in the traditional central business district.

Not surprisingly, grocery stores were among the first tenants to move from the downtowns into the new suburban strip centers. These grocery stores established themselves as the early anchors, that is the major tenant in these neighborhood centers, and the tenant most desired by a developer to ensure a viable project. These centers were focused around the resident population and their immediate
buying needs. Food, drugs and services were the original function of these early centers.

Before 1950, department stores activities in the suburbs were almost non-existent. By the mid-1960s over one half of all department store sales were in suburban shopping centers.

Gradually shopping centers became larger. Innovation and expansion came quickly with a handful of developers establishing early dominance in developing large malls. The first enclosed shopping mall opened in the mid-1950s, but it was during the 1960s when the mall became commonplace. The mall became more than a retailing center, it soon became a social gathering place. Many malls have been credited with the demise of suburban downtowns; they are the modern, suburban American answer to the town square. Public, one-stop, temperature controlled shopping with convenient free parking. What better?

Bigger, not better. The super regional mall emerged in the 1970s. With upwards of two million square feet of retail space these behemoths appeared in many metropolitan areas of the country. The seventies were generally profitable years for developers as old fixed rate mortgages were being played off against rampid inflation and significant increases in overage rents, again inflation driven.
The single greatest constant in real estate is change. With the 1980s, several significant changes took place that have altered the climate for developing retail facilities. Consumers saw their disposable income decrease as the costs for housing, food, clothing, health care and transportation all increased. As a consequence the public grew far more discerning about how much it bought and how much it spent. Interest rates increased to record highs inhibiting new construction. Inflation was brought under control faster and to a larger extent than many would have thought possible. Regulatory and environmental protection obstacles, coupled with community pressures, severely inhibited the production of new centers. Site acquisition and assembly for the few remaining areas with retail potential often proved impossible.

Finally, many shopping center developers had optimistically depended on the baby boom generation to supply new demand for marginal center locations. The baby boom generation has matured to a large extent, and many have chosen to have smaller families, later in life, or to have no children at all. The one person household is no longer an anomaly. The population that was to support the grand scale, suburban shopping center developments, in sum, never came to be. All these factors have had major impacts on the
shopping center industry.

The 1980s will be remembered as a time when large regional shopping centers lost their appeal as the darlings of the development industry; as a time when tenants at shopping centers began to demand smaller spaces; as a time when "middle markets" and "food courts" dominated the developers literature, and as a time when older centers got a much closer look from developers seeking to realize new investment opportunities in the shopping center industry.

As an aside, it is interesting to note that the Boston area has a rather unique history of being in the forefront of new trends in commercial development. One of the first regional centers in the nation, Shopper's World, was constructed in Framingham in 1951. Two of the earliest enclosed malls were developed here—in Peabody along Route 128 north of Boston and in Braintree to the south. In 1971 another precedent was set when Liberty Tree Mall in Danvers became the first regional center to be located next to another shopping center. The Rouse Company's rehabilitation on Boston's waterfront and its use of food as the main attraction represent another retailing innovation. Most recently, we have Copley Place, a major retail experience incorporated into a mixed use, air rights development.

1 Boston Metropolitan Area, Development Markets, Leggat, McCall & Werner, Inc. 1984
CHAPTER TWO
INDUSTRY DEFINITIONS & STATISTICS

Before beginning a detailed look at strip center opportunities, I thought that it would be useful to gather some industry statistics on both the stock and the retailing performance of the various center types currently in existance. In particular, I was interested in both the numbers and GLA (gross leasable area) of each type center and their sales performance based on dollars per square foot of GLA. Although this thesis is focused on strip center rehabilitation, the quantity of new space being developed would be an indication of the health of strip centers as retail properties and might also provide some insight as to the competitive pressures facing rehabilitated properties.

The bulk of these statistics were contained in the 1984 Biennial Census of the Shopping Center Industry as contained in the trade magazine Shopping Center World. Census figures reflect shopping center space that was opened or scheduled to be open by the end of 1984.

Before looking at the statistics, we might do well to define explicitly the center types. The second issue of the "Shopping Center Development Handbook" published in 1985 by the Urban Land Institute was my reference for definitions and factual matters relating to Center development.
Individual retail stores can be categorized on several different levels; on the basis of merchandise carried, on the basis of functions performed or services rendered, on the basis of ownership (independent, local branch, national chain), or on the basis of location. Shopping centers however are usually described by only three principal categories—neighborhood, community and regional. Each category usually implies a clear and distinct function, trade area and tenant mix.

A neighborhood center provides for the sale of convenience goods (food, drugs and sundries) and personal services (laundry, dry cleaning, barbering, etc.). A supermarket has traditionally been the anchor tenant for such a center but now super-drug national chains are often assuming this role. As geographical convenience is the most important factor in determining a shopper's choice of supermarkets, the neighborhood center normally serves a trade area population of 3,000 to 40,000 within a five minute drive of the center. Typical centers average 50,000 to 60,000 s.f. of GLA, although the range of center sizes is from 30,000 to over 100,000 s.f.

The community center is the "in between" center. Some neighborhood centers have the ability to grow into community centers just as some community centers have the ability to grow into regional centers. The typical community center has
150,000 s.f. but may range from 100,000 to 300,000 s.f. Initially, the community center contained both a supermarket and a junior department store, variety store or discount department store. It provided the shopper with a wider range of soft lines (clothing) and hard lines (hardware and appliances). The typical anchor tenant in community center is no longer the junior department store, but is more commonly an off-price discounter, hardware/building/home improvement store, furniture warehouse, catalog store or other strong specialty store. The community center serves a population trading area of 40,000 to 150,000 within a ten to twenty minute drive of the center.

The regional center contains at least two full line department stores and average almost 500,000 s.f. Regional centers serve a target population of at least 150,000 who travel up to 30 minutes to arrive at the center. More recently, the industry has seen the rise of the super-regional, defined as a center containing three or more full line department stores often exceeding one million s.f. Sites for regional and super-regional centers vary dramatically—from ten acres for a multi-level urban center to over 100 acres for a single level super regional center.

Where does the strip center fit within the context of these definitions? Nowhere. The convenience center and the strip commercial development "do not easily fit within the
definition of shopping centers." (Shopping Center Development Handbook, ULI, 1985).

The ULI handbook does discuss two other forms of retail development, the convenience center and strip commercial. The convenience center is seen as the substitute for the mom and pop grocery store. These centers often combine a national chain (Seven Eleven, White Hen Pantry, etc.) with one or two other convenient uses, a dry cleaners, a barber or similiar service intensive provider.

Strip commercial development, as distinguished from the "strip shopping center" (a physical description of a center with a linear configuration) is defined by ULI as

"a string of commercially zoned lots developed independently or a string of retail commercial stores on a single site where there is no anchor tenant and no central management, and where tenant mix results from leasing to available tenants with good credit, not from planning and executing a leasing program. While not condemning such retail development patterns out of hand, this handbook views such development as less likely to experience long term success, to give concern to the needs of the consumer, and to be an asset to the community it serves."2

From the tone of this quotation, it appears that nobody likes a strip center developer. Not even other developers.

Fortunately, Shopping Center world chooses to collect data based on GLA, not shopping center categories as defined

2 Shopping Center Development Handbook, Second Edition
by the ULI. For the purposes of this thesis, we will assume that retail developments less than 100,000 s.f. are generally large neighborhood strip centers or convenience centers to which the process of rehabilitation described in this paper is applicable.

What is the relative distribution of center sizes throughout the United States? Do the large surburban malls do all the business with the community centers and strip centers picking up the scraps? Is anyone still building strips? By massaging the Shopping Center World statistics some interesting trends emerge.

As you would expect, the total number of centers under 100,000 feet is large; 64% of all centers are between 10,000 and 100,000 s.f. What is surprising is that these smaller centers make up 28% of the total GLA and contribute 30.5% of the total retail sales. The figures for the six New England States, (Maine, New Hampshire, Vermont, Massachusetts, Rhode Island, and Connecticut) are even more heavily weighted toward the small center. Here 31.2% of the total GLA can be found in the small center, accounting for 36.9% of the total retail sales. The figures on the following page graphically illustrate the huge inventory of small centers that exist in New England and their relative strength of sales in the competitive retail market.
DISTRIBUTION OF N.E. CENTERS BY GLA
ALL FIGURES IN ,000 FEET GLA

SALES VOLUME BY CENTER SIZE
SIX NEW ENGLAND STATES

On a national basis, these figures translate into per square foot volumes for the small centers that exceed all other size categories, as is depicted graphically below. (Importantly, the data base excludes department store sales from the larger center sizes as these are reported separately. The average sales volume in these stores is much higher and would distort all other statistics. The average Merlins Store does $295. per s.f., Marshall's averages $250.

**AVERAGE SALES VOLUMES**

<table>
<thead>
<tr>
<th>CENTER SIZE (.000 sf GLA)</th>
<th>10-100</th>
<th>100-200</th>
<th>200-400</th>
<th>400-800</th>
<th>800-1MM</th>
<th>1MM +</th>
</tr>
</thead>
<tbody>
<tr>
<td>AVERAGE SALES $ PER SF GLA</td>
<td>160</td>
<td>150</td>
<td>140</td>
<td>130</td>
<td>120</td>
<td>110</td>
</tr>
</tbody>
</table>

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3 Kilmartin & Britton, respectively. 1984 International Council of Shopping Centers Annual Convention, cassette recording, "Let's Start at the Top: Chief Executives Examine their Retail Strategies." ICSC, Atlanta, GA.
One of the major themes influencing the rehabilitation of older centers is the environmental, regulatory and political hurdles that have become commonplace in the production of new centers. Couple these constraints to production with the lack of available sites in the areas with population densities great enough to support a major center and you get a major force for small center rehabilitation & reinvestment. If this premise is correct, new centers should almost always be created at the 100,000 sf and smaller range. This is exactly what I found in the New England States in the period 1983-1985.
The time lag between permitting and construction accounts for the two new malls in the one million plus range. Although these malls will continue to be developed, the explosive growth phase of regional and super-regionals is clearly on the wane. Interestingly, rehabilitation of these centers built in the early 1960s is a well established trend in the industry and could well be the subject of a subsequent thesis (by others).

The conclusions of all these statistics when applied to small center rehabilitation are obvious:

* small centers of 10,000 to 100,000 square feet are the most numerous both in terms of absolute numbers and in total GLA

* small centers continue to produce sales volumes that are at least equal to sales produced in similar stores found in larger community, regional or super-regional malls

* small center development and construction will probably dominate the new product placed in service over the next few years owning to the site assembly and permitting complications accompanying the production of larger centers.

Having looked at the historical background and some center statistics, we now take a look at the economic forces driving the developer toward small center rehabilitation.
Without question, the dominant trend today in shopping center development is the resurgence of the strip shopping center. The strip has made a dramatic comeback in the last three years, bringing with it dramatically improved aesthetics and marketing savvy.

John M. Stone writing in National Real Estate Investor
May 1985

This chapter will examine some of the economic, demographic, and development considerations that are driving the renewed interest in rehabilitating older strip centers.

DEMOGRAPHIC CHANGES

It is tempting to say that the lack of available sites and excessive government and environmental regulation are the primary forces restricting mall development and therefore underlying strip center rehabilitation. While these are certainly contributing factors, the real forces are the demographic & structural changes occurring in our society.

Demographic studies are sophisticated people inventories. The retail developer is concerned with where, how many, how old and how much? Significantly, the first three inventory items are changing; the fourth, disposable income, is generally acknowledged to be unpredictable over the long run.

Where is not a static statistic. In the past, the
mobility of the population has been a strong factor in the
development of new retail centers. Americans are moving
less. The decline in mobility has a variety of probable
causes including the rise of the two-jobholder family, the
rising cost of housing, the continued increase in
homeownership and the pattern of overhousing in the purchase
of the first home (thus decreasing the need for the family to
move when a couple has children). The combined effect of
these changes are to produce a generally more stable retail
market in existing known, geographic areas.

In the past, older neighborhoods tended to decline as
people aged. Today more and more younger families are
purchasing and improving existing houses in older
neighborhoods. (Gentrification is not limited to the South
End of Boston.) The effect of this change has not been lost
on developers.

How many? Fewer than expected. The United States
appears to be headed on a path to zero population growth.
The U.S. Census Bureau currently predicts a population
peak in the year of 2050 at 309 million. The projected
population growth rate for the rest of the eighties is less
than one percent. The number of families with three or more
children declined by 39 percent between 1970 and 1981. The
fastest growing segment of the housing market is the single
person household; four out of every 10 fall into this
category. The implications to the retail developer are clear. Developers can no longer rely on rapidly increasing population densities to support new facilities in secondary locations, nor will population densities likely increase dramatically in existing population centers as family size trends down.

How old? Different age distributions produce differing demands of retail facilities that in turn produce alternate patterns of retail consumption. For the strip center redeveloper the opportunities lie in sensitivity to these subtle, slowly evolving neighborhood changes. The number of adults between 35 and 44 will increase by 12 million over the next decade. The design and merchandising of existing centers can be expected to reflect the changing consumer preferences of a maturing population, which will generally be affluent and at the peak of its earning power.

Similarly, the retired and elderly population are asserting their influence in the retail market. As a group, they are healthier, more active, and more independent. The average income for this group grew 25% faster than for all U.S. households between 1970 and 1980. Over the decade of the eighties they will also become 25% more numerous, 6.3 million by 1990 or almost 13% of the population. Well located centers that respond to the shopping and community needs of this market segment will be in demand in the 1990s.
How much (disposable income)? Anyone's guess over the long term. Other non-retailing factor prices for housing, fuel, and transportation are important factors. One certainty is that the growth of the single-person household and the two-income household will have significant influences over what the population considers value.

Where will population growth occur in the 1980s? Suburbs and small cities will continue to capture the major share of population growth throughout the 1980s and will outpace both the central cities and the rural areas. Migration to the Sunbelt will continue, but not in the record numbers seen in the recent past. Nonmetropolitan growth represents a major new force in U.S. population distribution that will provide the largest source of opportunities for new retail facilities.

Shopping Center Development Handbook, Chapter 8, Future Trends, the Urban Land Institute, 1984.
All these trends can be used to support the thesis that well located existing strip centers may make for better performing real estate assets than new centers located in outlying areas. The changing demographics also point to some of the major value-creation opportunities, namely retenanting to suit the needs of a maturing population with different shopping needs.

**SUPPLY CONSTRAINTS ON AVAILABLE SITES**

I think what you've heard today from these panelists will be the major trend for the next decade: the renewed emphasis on small center and community center redevelopment as the opportunity for mall development decreases. You've got more and more of these fine retailers looking to expand and one of the only opportunities for expansion will be the production of smaller neighborhood and community centers and their helping to foster that.

1984 Annual Convention
International Council of Shopping Centers
from cassette recordings
New Anchors in Small Centers,
What Are They Doing There?

The lack of good available sites can be traced to the slower spread of suburbanization and to increased growth, land use and environmental controls.

Historically, retail developers could look at an area map, tick off the direction of residential growth, and start to buy up property. Neighborhood and community center
shopping developers who ventured with homebuilders into an area found themselves sitting on significant value as density filled in around them. Far greater fortunes befell the early mall developers who acquired the sites created at the interchanges of highways created by the Federal Interstate Highway System. As the federal highway system nears completion, and suburban growth is retarded due to the demographic changes discussed earlier, the good center locations in built-up areas are almost exhausted.

With the increased sophistication of the retailers themselves, many developers now prefer to follow the market rather than speculate on future growth. Often the national retailers will know the characteristics of their target market (size, income, age bracket, etc.) and will dictate the communities in which they will locate to the developer.

The lack of sites manifests itself in many different ways. Site costs that at one time prohibited development such as steep terrain, excessive ledge, even sites with an existing user, are now beginning to prove feasible.

The impact of the Wetlands Protection Acts and related environmental legislation have made some sites unbuildable although the weight of this legislation has not fallen any more heavily on shopping centers than it has on other land uses. Environmental regulation has added greatly to the cost
and time factors associated with the production of new centers.

There does appear to be growing support for more comprehensive impact assessment analysis for suburban centers, as they often become the hub of larger nodes of commercial activity.

New retail development almost always entails the problems of site assemblege, high site development costs, environmental review and potential community and businessmen opposition. The creation of space to compete with the existing merchants is seldom received with enthusiasm.

Contrast this with the retail redeveloper. His site is assembled and transferred to him at closing. If the center is in trouble, he will be welcomed by both business interests and residents for the improvements to the asset and the shopping choices. And beyond construction and signage permits, no other regulatory or environmental permits are usually involved.

FINANCING

There are two significant financing considerations that favor rehabilitation of strip centers over new center construction.

First, it is easier to syndicate an existing center that is being rehabilitated and has a track record than it is to
build a speculative center as a syndicator.

Second, in this climate of lender participation via convertible or participating mortgages, it is easier to keep your own deal if you have a proven income generator. It may even be possible to have an earn-out clause that will finance the rehabilitation via increases in the center's rent roll.

CONSTRUCTION COSTS

As many of these distressed centers are sold on the basis of capitalized cash flows, it may sometimes be possible to acquire centers for less money than it would cost to reproduce the bricks and mortar. Assuming that the distressed center is bought at discount, and that rehabilitation costs are controlled, the developer may find himself able to offer space at rentals that are significantly more competitive than new product.

If the center is not distressed, the developer may find himself in a strong position to negotiate with the tenants as to the apportionment of some rehabilitation work, such as parking lot resurfacing, new signage, etc. into the common area or maintenance account.

If the center is bought at a deep discount from replacement cost, the developer may be able to qualify for the Historic Rehabilitation Tax Credit. Center
rehabilitation costs must meet or exceed fifty percent of building acquisition costs for this credit to apply.

The tax credit available is significant. For structures 30 yrs old, a tax credit equal to 15% of the rehabilitation costs is available; if the structure is 40 yrs old, a 20% credit applies.

Some site improvements do not apply as rehabilitation expenditures. Also, the initial allocation of acquisition cost between land, improvements, and building must be credible in the view of the Internal Revenue Service. Proper tax advice is essential in order to structure the credit to withstand IRS scrutiny.

The Rehabilitation credit available to developers may be short lived. It is expected to change significantly under the proposed tax law changes being promulgated by the Regan Administration.
Strip centers have never been known for their architectural grandeur. A major challenge facing the redeveloper of the typical strip is how to add physical improvements to the center that enhance value and create better retailing environments. In addition, there is the issue of when to stop; properties can be over-improved beyond the expenditure level justified by the anticipated cash flows. In a well managed program, the level of expenditures will be preset at center acquisition; the developer's objective becomes obtaining the "most bang for the buck."

This chapter will look at individual components of the typical strip center; the configuration, parking & vehicle access, signage & imageability, site improvements and store fronts. To do this in a generic way is useful, as site specific details would tend to divert attention from the central theme of value creation in retailing via constructed improvements. Lastly I will explore some of the particular construction & management issues that are unique to center rehabilitation work.
CONFIGURATION & ENCLOSURE

The strip was named for its linear configuration. Most strip centers parallel existing highways or through streets. The parking lot extends between the stores and the street. A canopy typically extends over a pedestrian walkway that parallels the front of the stores. Deliveries are made via a service alley that parallels the rear of the stores. The length should not exceed a convenient walking distance.

The strip becomes an "L" when it is located at the intersection of two streets. This design also works well on a deep lot.
When the site is large a "U" or dumbbell shape is often found. The dumbbell layout places two anchor tenants on either end of a rectangular shaped center, with the smaller tenants between them, thus encouraging shoppers to notice the smaller stores on their route between anchors.
Many of the architectural and site design features that make strip centers so predictable and non-descript are the same features that retailers desire most. Both the strip and the "L" provide retailers with the maximum vehicular site exposure to passing motorists. The mansard roof, so common in strip centers, provides the vertical height and projection for a sign band visible from the street. The metal canopy encourages pedestrian traffic and window shopping along the front of the stores. And the asphalt parking in front, encourages frequent shopping visits.

Mall like enclosures for small strip centers are probably ill advised. One of the major attractions of the strip is the opportunity for the shopper to make quick, one stop shopping trips. A mall enclosure necessarily limits entry to a few distinct points. Further, mall maintenance expenses are significant and difficult to amortize over the small number of tenants in a typical strip. Even more damaging to the retailers is the loss of individuality that comes from not having an identifiable street presence. As we will see in later chapters, this is the reason often quoted by retailers for preferring the smaller strips over the regional malls.

For these same reasons, it is also inadvisable to provide permanent, enclosed protection in the area that is currently the metal canopied shoppers walkway. The walk from the auto
to the canopy will usually be as great as the distance travelled beneath.

Developer's seldom enclose either linear or "L" shaped strip centers. Site constraints and the loss of tenant identity behind exterior walls are the primary reasons for not enclosing small centers. However in larger community centers, enclosure may be used as a defensive move aimed at protecting the investment of the original center from regional center competition.
FACADES AND STOREFRONTS

Although enclosure usually doesn't make economic sense, exposure certainly does. One method often used by strip redevelopers is to open up the stub ends of existing strips to provide more linear feet of storefront. This is particularly true in the case of strips that are satellite locations drawing from existing community or regional centers. The ends of strips are ideal locations to add density in these situations. Adding building density to an existing center is one of the primary methods of center revitalization.

One of the best ways to enliven a center and add some architectural distinction is to add some relief and variety to the storefronts and pedestrian walkways. Nothing is more representative of the small strip than 250 linear feet of aluminium storefront, set with precise linearity, and located just on the edge of an eight foot poured in place sidewalk. Although it is impractical to change elevations (finish floor elevations inside the stores, handicap considerations, and material handling complications limit this) it is possible to add significant visual interest and consumer appeal by selectively varying the horizontal alignment. To borrow a phrase from a distinguished MIT professor and retail consultant, "create a (mini) discovery network." 5

The concept of varying horizontal alignment is common to

5 Prof Michael Buckley, Design for Development, Fall 84
retail mall redevelopers. In Atlanta, the Rouse Company used the redefinition of tenant lease lines inside the mall to eliminate the "bowling alley look" when creating Outlet Square from the former Shoppers Mall.

The visual variety can easily be extended to the walking surface itself. Occasional splashes of color and texture, provided by brick pavers or textured concrete, add interest. The redefinition of the storefronts may create natural seating or planting areas. Knee walls help distinguish the space. The canopy can take interesting forms and angles, even canterlevering out over the traffic lane to highlight an entrance and mark a drop-off point.

Let's not argue its importance. The canopy, walkways, and storefronts are what Mr. and Mrs. Shopper can see and touch and what gives them their feelings about our centers. Our canopies can bore them and even turn them off or they can give them that warm, fuzzy feeling that makes them come back for more. 7

The question is how to prioritize construction expenditures so as to create warm fuzzies without taking all of the developers cool greenies. Lonnie Peterson, AIA, says put the developer's money where the public will see and feel it most."For example a textured walkway or nice knee wall are

6 "Outlet Conversion Restores Excitement at Run-Down Atlanta Mall," Shopping Center World, Jan. 84
7 Glenn D. Hettinger, "Mall Construction" SCW June 84
more important than expensive glazed roof tile." The roof tile is seen from a distance and nobody cares if it is authentic Lowicki clay tile at about $1,000. per square or a much more economical concrete Spanish tile at about $300. per hundred sq. ft.

"If a client insists on a very basic canopy and only has $10,000. for pizazz, at least buy landscaping. If he has nothing extra to spend, at least force his tenants to comply with the architect's signage criteria. These two components can make a cheap canopy or ruin an expensive one."

PARKING & VEHICLE ACCESS

Perhaps the greatest single source for value creation inside an existing center is the opportunity to provide additional GLA. This can be done by acquiring adjacent parcels, by additions to the existing strip on an underutilized site, by kiosks located in the parking lot or by selling off or leasing pad locations at the perimeter of the site. All of these options usually involve changes to the existing parking and vehicular circulation systems.

The ease of access and interior circulation is of prime importance to the consumer. Given that his stay at the

8 ibid. pp. 18
center is limited, a large part of the consumer's impression will be formed while accessing, parking and departing from the center. Any change in these systems to accommodate added density must be regarded in light of the total impact on the center's accessibility.

Having said that, where do we go to generate density? The parking lot of course. Many of these older centers were built in the era when "plentiful free parking" was almost axiomatic. Consequently the centers are almost always over subscribed when it comes to actual parking required. This is not to say that they are in excess of the locality's specifications for parking required. Many of these local standards were developed lacking proper data collection and are particularly conservative as to the number of spaces required.

This conservatism extended to industry publications. In 1963 the Urban Land Institute promulgated a guideline of 5.5 spaces per 1000 sq. ft. GLA. The table below is the parking index as drawn from the 1984 Dollars & Cents of Shopping Centers (1984, ULI). Clearly 5.5 remains the standard.

<table>
<thead>
<tr>
<th>Type of Center</th>
<th>Number in Sample</th>
<th>Median</th>
<th>Lower Decile</th>
<th>Upper Decile</th>
</tr>
</thead>
<tbody>
<tr>
<td>Super Regional</td>
<td>90</td>
<td>5.66</td>
<td>-1.60</td>
<td>6.89</td>
</tr>
<tr>
<td>Regional</td>
<td>101</td>
<td>5.72</td>
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<td>Community</td>
<td>244</td>
<td>5.59</td>
<td>-1.26</td>
<td>8.52</td>
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<tr>
<td>Neighborhood</td>
<td>340</td>
<td>5.52</td>
<td>3.76</td>
<td>8.96</td>
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</tbody>
</table>

PARKING INDEX IN U.S. SHOPPING CENTERS
In 1981, ULI published the results of a major study of the parking requirements for shopping centers. The primary goal of this study was to establish parking standards for shopping centers in the United States and Canada, based upon observations of transportation activity at existing centers. These recommendations could then be applied to the planning of new centers or the expansion of existing centers.

Their study recommendations are summarized below:

* 4.0 spaces per 1,000 square feet of gross leasable area for centers having a GLA of 25,000 to 400,000 square feet

* from 4.0 to 5.0 in a linear progression, with an average of 4.5 spaces per 1,000 square feet of GLA for centers having from 400,000 to 600,000 square feet GLA

* 5.0 spaces per 1,000 square feet GLA for centers larger than 600,000 square feet GLA

The provision of parking spaces per the U.L.I. guidelines will provide for the centers total needs during all but 19 busiest hours of the more than 3,000 hours during which the center is open annually. During 19 hours of each year, which are distributed over the ten busiest shopping days, some patrons will not be able to find parking spaces when they first enter the lot. If the center is able to provide (or enforce) off site employee parking during these

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Parking Requirements for Shopping Centers, ULI, 1982.
peak days, total parking requirements can be reduced by 15%.

The ULI study focused upon four variables related to parking demand: center size, retail uses, non-retail uses, and method of travel to the center. Only food service had a measurable effect on required parking of the retail uses studied. ULI recommends that a center with between 25,000 and 100,000 square feet of total GLA will require an additional 10 spaces per 1,000 square feet of food service area. Centers between 100,000 and 200,000 need only provide six spaces per 1,000 square feet of food service GLA, and centers above 200,000 require no additional spaces.

Non-retail uses were also studied. Office use which amounts to over 10% of total GLA, and cinemas at smaller centers, were found to require additional spaces.

When less than 75% of the center's customers arrive by private car, parking requirements can be further reduced. The ULI completed detailed case studies on 15 centers and found 91% of the customers arrived by automobile, 4% walk, 3% take the bus or other public transportation, and 2% bicycle or skateboard or whatever. Very few centers will have less than 75% of their customers arriving by car.

Clearly the largest single determinate of parking requirements is center size. But why do small centers require less spaces, proportionately, than larger centers?
Because their retail peaks are lower. Recall that the ULI analysis is based on providing parking based on the 20th busiest parking hour. This is analogous to the power company dilemma as to providing incremental generating capacity to meet the once a year spike in power demand caused by all the air conditioning load on the hottest day of summer at 3:00 in the afternoon. Power companies often elect "brown outs" rather than provide the generating capacity required to meet these peaks in demand. The ULI suggests a similar "let them wait for a space" solution during those few hours after Thanksgiving and those few hours before Christmas when demand is heaviest.

For the small center, the Christmas rush presents less of a spike in demand. The graph below depicts % of annual sales by month for neighborhood, community and regional centers.

![MONTHLY SHOPPING SALES VARIATIONS FOR NEIGHBORHOOD, COMMUNITY & REGIONALS](image)

10 Ibid. pp 47.
Notice from the previous page that while region1 and community centers complete 16.6 and 15.3 percent of their annual sales during December, a neighborhood center, typically a small strip, completes only 14%. The variation in month to month sales volume is far less for strips than for other center types because the centers are often more oriented toward service than retailing.

The ULI study also speaks to the impact of downsizing of actual automobile dimensions and the impact of smaller cars on parking layouts. They suggest that the current stall dimensions of 8.5 or 9 feet by 18 feet can be reduced to 7.5 feet by 15 in light of today's smaller cars. The figure below represents a self-enforcing plan for comingled small and large car parking that produces density improvements of 28%.
What is the significance of all these parking ratios and automobile size considerations? Revenue. By thoughtful use of the ULI guidelines, a retail developer can often add GLA to an existing center without purchasing additional land. Density additions and retenanting are the two strongest methods available for increasing cash flow from an existing center.

There are a few cautions appropriate here. The ULI guidelines were developed by an industry organization for use by developers. They will not necessarily be accepted by local authorities as the definitive word on parking by local regulatory bodies. Also, the tenant deserves to be well represented in any discussion of parking density. Many national changes have internal requirements for parking densities that will not be compromised. Unleased and non-leasable density additions do nothing for a revenue stream.

SITE IMPROVEMENTS

By far the most visible and dramatic site improvement that can happen at a strip center is the addition of a well planned and executed program of landscaping. The shopper and community support that generate from landscape improvements cannot be underestimated.

There are however, two components of cost that must be recognized by developers contemplating landscape
improvements. First costs, those associated with design and construction, are always considered. A single red maple of sufficient caliber and height to make an impact, may cost over a thousand dollars. Advances in large tree transplant make possible the immediate look of an established, mature landscaped plan.

More significant than first costs are the costs of maintenance that will continue as a line item expense on all property records for years to come. In the particular case of small strip centers, these costs can be particularly burdensome as they must be amortized over a smaller GLA, both as first costs to the developer, and later as part of the common area maintenance (CAM) assessed to each tenant.

A landscape plan should respect the existing signage and flexibility required in tenant configuration. Plantings that restrict access to the storefronts or that have the potential (either on installation or as trees mature) to block the signband should be avoided. An often overlooked area for landscape is the rear of the strip parallel to the service way. These plantings can pay big dividends if the abutters are single family residences, as is so often the case in neighborhood strips.

Often landscaped traffic islands are used to "break up the sea of asphalt" that exist in front of the stores. These can be very effective visually but they have corollary
effects on parking lot sweeping, snow plowing and removal and plant maintenance that are not insignificant. The middle of a large parking lot is as inhospitable to most plants as it is to most people. Pollutant effects of automobile exhaust and salt from ice control, wind effects, dead loads over roots and severe temperatures are all concerns when selecting plant materials for parking lot islands.

Beyond landscaping, parking lot lighting is perhaps the most effective site improvement. The security afforded by this improvement is particularly important to working women, who have been shown to do much of their convenience type shopping in the evenings. Also parking lot lighting can help in establishing center presence by illuminating building facades from the street. Advances in high pressure sodium and halogen lighting systems have greatly reduced the number of stanchions required and operating costs of parking lot lighting. For strip centers with shallow lots, it is often possible to eliminate stanchions entirely by roof mounting of fixtures.

SIGNAGE & IMAGE

The importance of image in attraction to major regional centers is well studied and widely acknowledged. In the

absence of specific regression analysis, we are left to empirical formulations as to what attributes of strip centers are effective in leaving the best possible image with consumers.

Some of the impressions left by a center relate more to the retailing environment than to the physical plant. Quality and variety of the stores, sales personnel, the general price level, the merchandise assortment and promotional activities are components of image not easily tied to the actual bricks and mortar.

Signage, layout, ease of mobility, availability and ease of parking, comfort areas and building architecture are all components of image that relate back to the facility.

Sign bands and signs beneath the canopy marking store entrances should conform to some standard architectural controls as to materials, illumination, and size. The combined effect of a good signage program will be to convey information effectively while giving the shopper a sense of place and a deliberate, but subtle impression of order and organization.

Many retailers have their own signage and graphic identities that do not fit well into a developer inspired signage program. Also the cost of recreating signage is substantial and will not be welcomed by existing tenants. Many communities have developed their own sign standards and
permitting procedures for new signs. Individual permits for all strip mall signage can be a logistical & regulatory nightmare. Finally, many sign types have a substantial lead time and must be ordered well in advance of other construction items.

A signage & graphic consultant paired with a good architect make an effective team in center rehabilitation.

What about the other building & design aspects of center image. The best advice I have read comes from Neal Freeman, Vice President of Watkins Associates Developers in Atlanta.

We've had the most problems when we didn't tell our architect what we wanted. You have to share your market research with your architect. Tell him who's going to shop there. I insist on a site inspection. Sometimes we'll want to give a youthful feeling to an older buying public. Another time we are after a hi-tech or a conservative or an earthy feeling. Whatever feeling we want has to be communicated to the architect.12

Image has implications beyond the successful leasing or releasing of the strip. As much of the centers inflation protection and future cash flows will come from percentage rents, the shopper appeal of the strip created should be a primary concern of the developer. Additionally, for the developer that intends to be a continuing presence in the

12 "If Informed, Architects Can Make Developer's and Manager's Dreams a Low Cost and Eye Appealing Reality, op cit, pp 18.
commercial leasing business, past projects are a continuing source of pride, or embarrassment, that help shape the opinion of leasing agents, tenants, and community power structures.

CONSTRUCTION CONTRACTING CONSIDERATIONS

The reconstruction of a strip mall is a significant contracting and coordination effort worthy of management attention. These projects are almost always undertaken with the existing center tenants still in place. Existing conditions, multiple contractors, tenant concerns with business continuity, and the problems usually associated with the construction renovation process combine to produce a comparatively small but highly complex undertaking.

There are three peculiarities to strip mall reconstruction that deserve special notice and attention from the developer. The first management question that deserves attention is the construction permitting process. The key is how many projects do we have, from a municipal inspector's point of view. Some building inspectors will consider each individual store's fit-up as a separate job. This makes for a permitting and inspection nightmare as incremental inspections are required at each phase of the work, and the paperwork and plan submission load is multiplied by the number of stores. A more reasonable solution is to consider the strip as a single
entity for reconstruction, (some communities refer to this as a planned unit development or PUD) and allow for a consolidated permitting and inspection process.

Other permitting crisis occur when developers fail to pull the necessary demolition permits well in advance of construction, or wrongly assume the permits will be obtained by the contractor. The topic of signage permits has been discussed earlier and should be an agenda item with municipal officials early in the process. Often even the change of a single sign will require a permit. Discuss with the tenants who will pay for temporary signage during construction.

Equally as important are the items of work that do not require a permit. Establish which building details and areas must be brought to current building standards and which do not. Permits pulled often serve as the basis for future real estate valuations so it is wise to keep their dollar value as low as practical.

Contractor selection is the second big concern. Beyond the normal concerns of union vs. non-union and competitive bid vs. negotiated price, there is the issue of contractor capability. Developers make money by signing leases and placating tenants, not fighting change orders with untrustworthy contractors. Look for sufficient depth of resources as many tenant fit-ups are done on a fast track, multiple shift basis. Prior experience in both
rehabilitation projects and specialty retail is the ultimate combination for a strip center contractor. Check references.

Finally, just like good tomatoes, there is a season for retail rehabilitation. As some 31% of the business is transacted between Halloween and Christmas, stay away from rehabilitation that will disrupt this peak retailing season. New tenants will want to be in place in August/September to take advantage of back-to-school and related seasonal sales. If possible, begin rehabilitation work in January or February and work toward completion by fall.

There is a real issue of cost vs. time in strip rehabilitation. Rents and credibility both are lost when schedules are not met.

Be aware of phrases like "match existing" on architectural drawings. How do you match 20 year old, partially discolored tile? Phrases like that show a lack of knowledge of existing conditions and should immediately be brought to the architect's attention.

In some extremely depressed centers, it may make economic and sociological sense to close the center entirely during renovation. This adds an air of anticipation to the "grand reopening" and may help to shed a negative perception of a former depressed or unsafe center.
CONSTRUCTION COSTS

Along with the management issues, are the construction cost considerations of the various work items associated with center rehabilitation.

In general, these small strips are perhaps the simplest form of constructed facility, more easily compared with open warehousing than any other construction type. Typically one story with steel frame and joist construction, block exterior walls and aluminium storefronts, these buildings are being produced new today in the twenty to thirty dollar per sq. ft. range.

For the strip center rehabilitator, roofs, parking lots and facades represent the most likely areas of expenditure. Many of these centers were constructed with flat, asphalt built-up roofs that have reached the end on their useful life. New roofing costs vary widely with the condition of the existing roof and flashing, with roof size, and with the number of roof penetrations. Rehabilitation and replacement methods are numerous but will generally run from $1 to $3 per square foot. Newer centers are being constructed with one piece rubber membrane roofs or with the new standing seam metal roofs available from the pre-manufactured building suppliers. Both of these roofing systems offer longer life and better service than built-up roofs and at closely comparable first costs.
Parking lot reconstruction is very much a site specific call and varies from minimal crack sealing to complete removal, new base and drainage construction, and new paved surfacing. Consultant advice is a good idea when evaluating contractor proposed replacement options.

Store fronts and facades are major expense items that cannot be overlooked. To generate a new storefront in an existing block wall will cost approximately $300 per linear foot. Drywall or dry-vit sign bands and facades constructed over metal studs average around $15 per square foot.

Often this space is delivered to retail tenants in new centers without a floor and with mechanical and electrical services just stubbed inside the exterior wall. The redeveloper can supply a better quality space, including vinyl floor and suspended acoustical ceiling, for minimal cost, usually less than $2 per square foot.

All of the construction costs associated with rehabilitation are negotiable with the tenants depending on the relative bargaining power of the owner and the desirability of the center.
CHAPTER FIVE
THE DEVELOPER'S ROLE: CREATING VALUE IN EXISTING CENTERS

An existing, well tenanted strip center of 40,000 to 100,000 sq. ft. GLA bought as a passive, buy-hold income producing property can be a good real estate investment. If the tenant list is strong, and the center is well located, strip centers provide risk diversification and steady cash flows. Supply constraints such as zoning and site availability limit competitive pressures. Lease devices can be used to protect against inflation and against increases in operating expenses and taxes.

But the purchaser of such a center is more properly characterized as a passive real estate investor than a true developer. This chapter will examine the various strategies used by developers to "create" value in acquired strips. The power to create value can produce returns, both over time and at disposition, that are several times the 8-12% typical investor return.

THE POWER OF CAP RATES

At the risk of being repetitive, there are only three types of returns available to real estate: cash flow, tax benefits and gain on sale. For commercial real estate, gain on sale will be tied primarily to cash flow generated from the property and certain other macro-economic conditions over
which the developer has very little control. Similarly, as real buildings depreciate on the order of 1/2 to 2% per year, depreciation becomes a fictitious deduction based on tax policy again outside the developer's control.

Cash flows then become the instrument for creating value whether the developer is a buy-hold or develop to sell entity. With capitalization rates for shopping centers as low as 8%, one dollar in increased rental translates into $12.50 capital appreciation. There is great economic power and profit potential here. If in a typical 50,000 sq. ft. center, rents can be increased by only $1, the value of the center has increased some 500,000 based on a very obtainable 10% cap.

The balance of this chapter will be methods to "up the rent" and live well.

DENSITY ADDITIONS

One good way to up the rent is to rent more. In the previous chapter we spoke of finding density opportunities by looking at parking ratios. If we can find a center with absolutely no vacant land, but with a 5.5 car per 1000 sf parking density, we may get rich.

The advantage of non-site specific research like this is that it is difficult to get mired down in details. A fictitious example follows:
EXAMPLE: PARKING LOT DENSITY ADDITION

EXISTING STRIP CENTER 40,000 GLA
LAND AREA RQD TO SUPPORT PKNG 77,000 s.f.
(based on 5.5 spaces per 1,000
GLA @ 350 sf per space)
TOTAL LAND AREA AVAILABLE
(excludes rear service alley) 117,000 s.f.

EXPANSION POTENTIAL CALCULATION
(based on revised parking ratio of 4.0/1000 GLA)

Expansion Potential = \frac{\text{Total land area}}{\text{Parking lot factor}} - \text{GLA Existing}

Expansion = \frac{117,000}{(1000 + (4*350))} - 40,000
= 8750 \text{ s.f. GLA}

SERVICE ALLEY

EXISTING 40,000 GLA
ADDITION *
8,750 GLA *

Formerly 220 spaces
With additional GLA & new ratio
of 4.0/1000, 195 spaces

lot boundary

MAIN STREET, USA

56
If we use the previous example and assume a $9. rental and construction cost of 35.00 per sf, our developer has increased his rent role 78,500 for a one time capital cost of 306,250, a 25% return. Further, when capped at 10%, the developer has increased the value of his center some 785,000 and profited by almost $480,000.

Notice that the value created does not flow exclusively from the "free land" but from the strength of the rental rate being capped so low. The implications to development are that it is often economic to buy adjoining parcels for use as parking areas to add building density and grow the rents.

What if local zoning or site constraints limit center expansion via parking density reductions or reconfiguring the existing lot? Are there other ways to increase GLA?

One possible solution is a parking lot kiosk. In this area we are all accustomed to the blue and yellow Fotomat store in its stand alone little traffic island. In the midwest this concept has been carried much further by developers seeking to add GLA to existing center locations.

There are many possible service and retail tenants who need a presence but not necessarily much space. Instant banking machines, mini-serve post offices, insurance claim adjusters, small food service vendors, and dry cleaners drop off centers come quickly to mind. These tenants can survive and prosper in 200-400 sf and are willing to pay higher than
standard rentals for the opportunity. Additionally these tenants are difficult to locate in a conventional strip as they do not need the 35-60 foot depth of store common in strips. A cluster kiosk of 5-6 of these tenants located on a drive-up pad location in the parking lot is a good solution.

As Greg Rice, Director of Leasing for the Meredith Organization explains, "A mini-kiosk can quickly help to revitalize a center and bring in five stores that you couldn't ordinarily accommodate in the strip." His firm has developed a patented five store mini-kiosk in which all stores are both drive-up and pedestrian accessible via a central treed atrium. Each store is 375 sq. ft. and is an ideal location for a florist, locksmith, printing shop, deli, pet supply, or similar high accessibility, small space user.

Another way to add density is to lease or sell off pad sites within the center to retailers who insist on the individual identification offered by the freestanding location. Retail tenants and food service outlets cite the opportunity for individual design and signage, the need for drive-through retailing, and the opportunity for outdoor sales (as in the case of a garden center or service station) as particular advantages of pad sites. For the small strip center, fast food outlets such as McDonalds or Arby's can

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13 *Rehab of a Center II, 1/2 Empty or 1/2 Full, 1984 ICSC Convention, Case tape recording*
generate traffic and interest for the strip.

Some cautions are appropriate for the developer planning pad sales. Although individual identity is desirable, very bold or extremely flamboyant architecture can detract from a center and lose a communities accumulated good will. Consider this exchange from the ISCS program on strip rehabilitation:

That was Golden Skillet Chicken... that was their pilot unit. We had a lot of discussion in the office about allowing a tenant to have that big sign there. It looks like a big frying pan sticking out in front. The city council has never forgiven us for allowing that bright orange roof; they think we ruined the look of the center. I don't think so. I think the tenant is entitled to some identity. I don't think its obnoxious; its distinctive.

Rehabilitation of the Crystal Shopping Center

Design reviews and plan approval can limit the chance of this embarrassment. One other aside on design. While pad chains like to enhance their own visibility, center developers also want to make sure those buildings don't obscure any part of their own center. Some developers place a high priority on the amount of ground given to the pad tenant, leasing just the amount necessary to put the building on the pad, making it almost impossible for the tenant to ever increase the size of the store. Most developers allow only a one story structure on pad sites.

Common area maintenance charges must be negotiated with

the pad tenants. Although these will typically not include some maintenance items unique to the strip, an allocation for charges would be appropriate if parking or promotion is shared for the center.

RETTANTING & RELEASING

If the goal of the developer is value creation via cash flow increases, an easy solution is to rewrite the leases at higher rates. Unfortunately, (or fortunately if you are the holder of a favorable lease) a lease is a property right that passes with the property to the next owner.

Only when viewed as an encumberance on the property can an existing lease be properly evaluated. A lease that offers no inflation protection or operating expense adjustment over a long term will eat away at future cash flow and diminish the value of the center. Similiarly, a well drafted lease to a credit worthy tenant creates economic worth more directly than physical, brick & mortar renovations. Buying out bad leases and recasting good ones is a strong value creation device.

The lease provisions of a commercial/retail lease are both numerous and complicated enough to qualify as a separate thesis unto themselves. For the purposes of this paper, I chose to look at only the economic consequences of current leasing activities. Who are the typical tenants in a
neighborhood strip center and how do the rents vary between different tenant types? What are the range of rents? And where are the operating receipts generated and operating expenses incurred? The data in the table below lists the twenty tenants most frequently found in U.S. neighborhood shopping centers.

### High Sales Volume Tenants in U.S. Neighborhood Shopping Centers

<table>
<thead>
<tr>
<th>Tenant Classification</th>
<th>Median Sales Volume per Tenant Square Foot GLA</th>
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</thead>
<tbody>
<tr>
<td>Supermarket</td>
<td>$271.46</td>
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<tr>
<td>Credit jewelry</td>
<td>185.70</td>
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<tr>
<td>Liquor and wine</td>
<td>177.89</td>
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<tr>
<td>Cameras</td>
<td>155.95</td>
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<tr>
<td>Convenience market</td>
<td>152.96</td>
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<tr>
<td>Fast food/carryout</td>
<td>150.59</td>
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<tr>
<td>Computer/calculator (retail)</td>
<td>142.85</td>
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<tr>
<td>Doughnut shop</td>
<td>141.49</td>
</tr>
<tr>
<td>Film processing store</td>
<td>137.15</td>
</tr>
<tr>
<td>Records and tapes</td>
<td>133.74</td>
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### Low Sales Volume Tenants in U.S. Neighborhood Shopping Centers

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<thead>
<tr>
<th>Tenant Classification</th>
<th>Median Sales Volume per Tenant Square Foot GLA</th>
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</thead>
<tbody>
<tr>
<td>Bowling alley</td>
<td>$ 21.03</td>
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<tr>
<td>Arcade, amusement</td>
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<tr>
<td>Laundry</td>
<td>34.91</td>
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<tr>
<td>Cinemas</td>
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<tr>
<td>Discount department store</td>
<td>48.88</td>
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<tr>
<td>Bath shop</td>
<td>48.96</td>
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<tr>
<td>Plant store</td>
<td>49.00</td>
</tr>
<tr>
<td>Health spa/figure salon</td>
<td>49.92</td>
</tr>
<tr>
<td>Variety store</td>
<td>50.53</td>
</tr>
<tr>
<td>Music studio and dance</td>
<td>51.03</td>
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</table>

### High Total Rent Tenants in U.S. Neighborhood Shopping Centers

<table>
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<tr>
<th>Tenant Classification</th>
<th>Median Total Rent per Tenant Square Foot GLA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Luggage and leather</td>
<td>$12.45</td>
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<tr>
<td>Athletic footwear</td>
<td>11.00</td>
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<tr>
<td>Automatic teller machine</td>
<td>10.35</td>
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<tr>
<td>Film processing store</td>
<td>10.07</td>
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<tr>
<td>Eyeglasses—optician</td>
<td>10.00</td>
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<tr>
<td>Contemporary home accessories</td>
<td>9.28</td>
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<tr>
<td>Candy and nuts</td>
<td>9.22</td>
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<tr>
<td>Wine and cheese</td>
<td>9.22</td>
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<tr>
<td>Decorative accessories</td>
<td>9.00</td>
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<tr>
<td>Fast food/carryout</td>
<td>9.00</td>
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### Low Total Rent Tenants in U.S. Neighborhood Shopping Centers

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<tr>
<th>Tenant Classification</th>
<th>Median Total Rent per Tenant Square Foot GLA</th>
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<tr>
<td>Bowling alley</td>
<td>$ 1.95</td>
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<td>Warehouse</td>
<td>2.05</td>
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<td>Variety store</td>
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<td>Discount department store</td>
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<tr>
<td>Junior department store</td>
<td>3.00</td>
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<tr>
<td>Showroom/catalog store</td>
<td>3.08</td>
</tr>
<tr>
<td>Community hall</td>
<td>3.26</td>
</tr>
<tr>
<td>Super drug (over 10,000 sq. ft.)</td>
<td>3.32</td>
</tr>
<tr>
<td>Supermarket</td>
<td>3.44</td>
</tr>
<tr>
<td>Hardware</td>
<td>3.60</td>
</tr>
</tbody>
</table>

---

15 Shopping Center Development Handbook, ULI, 1985
The importance of positioning your center correctly in the market cannot be over stated. The previous table reflects what is, the next chapter of this report speaks to what might be, i.e. innovative approaches to strip center retenanting.

Knowing who is there is not nearly as interesting as knowing who should be there. The tables below give some statistical background on rents and sales volume by tenant type for U.S. Neighborhood Centers.

<table>
<thead>
<tr>
<th>Tenant Classification</th>
<th>Rank</th>
<th>Median GLA</th>
<th>Median Sales Volume per Square Foot GLA</th>
<th>Median Total Rent per Square Foot GLA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Food</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Supermarket</td>
<td>2</td>
<td>25,500</td>
<td>$271.46</td>
<td>$3.44</td>
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<tr>
<td>Food service</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Restaurant without liquor</td>
<td>8</td>
<td>2,250</td>
<td>105.32</td>
<td>6.93</td>
</tr>
<tr>
<td>Restaurant with liquor</td>
<td>4</td>
<td>3,200</td>
<td>117.05</td>
<td>8.00</td>
</tr>
<tr>
<td>Fast food/carryout</td>
<td>9</td>
<td>1,500</td>
<td>150.59</td>
<td>9.00</td>
</tr>
<tr>
<td>Clothing</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ladies specialty</td>
<td>17</td>
<td>1,440</td>
<td>112.54</td>
<td>7.37</td>
</tr>
<tr>
<td>Ladies ready-to-wear</td>
<td>10</td>
<td>1,700</td>
<td>103.15</td>
<td>7.00</td>
</tr>
<tr>
<td>Home appliances/music</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Radio, video, stereo</td>
<td>13</td>
<td>1,800</td>
<td>93.49</td>
<td>5.93</td>
</tr>
<tr>
<td>Gifts/specialty</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cards and gifts</td>
<td>14</td>
<td>2,250</td>
<td>71.75</td>
<td>7.00</td>
</tr>
<tr>
<td>Jewelry and cosmetics</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jewelry</td>
<td>19</td>
<td>1,000</td>
<td>128.20</td>
<td>7.79</td>
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<tr>
<td>Liquor</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Liquor and wine</td>
<td>16</td>
<td>2,450</td>
<td>177.89</td>
<td>6.00</td>
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<tr>
<td>Drugs</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Drug</td>
<td>12</td>
<td>5,800</td>
<td>113.60</td>
<td>3.84</td>
</tr>
<tr>
<td>Other retail</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other retail</td>
<td>5</td>
<td>1,320</td>
<td>77.14</td>
<td>6.75</td>
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<tr>
<td>Personal services</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Beauty</td>
<td>1</td>
<td>1,200</td>
<td>70.47</td>
<td>7.00</td>
</tr>
<tr>
<td>Barber</td>
<td>11</td>
<td>615</td>
<td>59.19</td>
<td>6.00</td>
</tr>
<tr>
<td>Cleaner and dyers</td>
<td>6</td>
<td>1,500</td>
<td>75.86</td>
<td>6.75</td>
</tr>
<tr>
<td>Financial</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Banks</td>
<td>18</td>
<td>3,188</td>
<td>—</td>
<td>6.65</td>
</tr>
<tr>
<td>Savings and loan</td>
<td>20</td>
<td>2,048</td>
<td>—</td>
<td>8.50</td>
</tr>
<tr>
<td>Real estate</td>
<td>15</td>
<td>1,200</td>
<td>—</td>
<td>7.73</td>
</tr>
<tr>
<td>Offices (other than financial)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Medical and dental</td>
<td>7</td>
<td>1,200</td>
<td>—</td>
<td>7.48</td>
</tr>
<tr>
<td>Other offices</td>
<td>3</td>
<td>1,135</td>
<td>—</td>
<td>6.81</td>
</tr>
</tbody>
</table>

62
Finally, the dispersion of shopping center receipts as a function of center age may give some indication of the upside potential available if older centers are substantially rehabilitated. The line graph below graphically illustrates the huge increment between older centers and newly leased product.

![Operating Results by Age Group](image)

**OPERATING RESULTS BY AGE GROUP**

**NEIGHBORHOOD SHOPPING CENTERS**

- □ receipts
- + expenses
- ◇ net income
The previous line graph dramatically illustrates the upside potential present in older neighborhood strip centers. A twenty year old center averages 38% lower rents and 46% less cash flow after operating expenses when compared to new product. Unfortunately, the data does not allow us to determine whether this is due to the existence of old leases, strip decay and vacancies or retail mismanagement. Whatever the reasons for older centers poor performance, the data suggests a significant rent gradient that is available for capture by the savvy developer.

The data on retenanting and releasing in this chapter presents a good summary of the existing tenancy of small centers; who the tenants are, typical rents for alternate tenant profiles, and the rent gradient that exists between older and newer centers. The following chapter will present various innovative thematic approaches used by developers to produce more interesting tenant mixes and to enliven centers that have lost their traditional service oriented consumers.

**MANAGEMENT & PROMOTION**

Yet another way to add value to an existing center is to simply bring increased management to bear on the physical asset and retailing program that currently exists.

The management of expenses incurred in center operation is a dollar for dollar pass through to existing tenants or
to the new owner depending on the relative split of common area maintenance between owner and tenant. Similarly, unrented stores that remain vacant too long between tenants are unnecessarily detracting from a center's performance.

I was surprised to see such a small total difference in operating expenses when centers of different ages were compared. Although the average mean operating expenses varied very little, the variation between the lower decile and upper decile inside each age category differed remarkably. The bar graph below represents the lower decile and upper decile range of operating results for centers twenty years old and older. Notice the range of magnitude in the various expenses and their effect on total operating expense.
Clearly the power of reducing operating expenses is far less of an income generator than increasing density or rewriting leases. This is particularly true when all CAM charges are passed through to the tenants. Still, it would seem reasonable that an incentive fee of 50% or more could be negotiated with the existing tenant on shared CAM savings, thus producing another source of increasing revenues for the developer.

As to promotional activities, the jury is still out. The data examined indicates that older centers pay from 3 to 17 cents per sf GLA for advertising & promotion, hardly overspending. Promoting a strip is difficult as the expense must be amortized over a small GLA and tenant roster. Also, the traditional strip has been heavily weighted toward the service industry, an area where impulse and destination shopping is far less prevalent, reducing the impact of advertising on sales. Also, centers vary widely on the source of operating receipts, with percentage rent often between 20 and 40% of base. Although increases in base are tied to center performance, a developer who is seeing very small upside in terms of percentage rent will show little interest in a heavy promotional budget, unless it is 105% passed through to the tenants.

If the center is given a new theme altogether, promotion may be the key to revitalization. If extensive physical
renovations are planned for the center, a complete promotional campaign should be developed consisting of preconstruction announcements, promotion during the renovation, promotion for the grand reopening, and the grand reopening. A well-executed promotional campaign, capitalizing on the excitement of the renovation, can actually increase sales during the construction period. Some developers include a grand reopening assessment in new leases negotiated.

To summarize, density additions, retenanting & releasing, and to a lesser extent, management and promotion are the primary "value added's" available to the strip center redeveloper to improve the economic performance of a center. The following chapter will present a brief overview of the various retail themes being used to create entirely new retailing concepts for these small centers.
CHAPTER SIX
THEMATIC STRIPS

In many locations the retailing strip center has been totally recycled from its former role as a convenience and service center to an entirely new identity as a theme retailing center. Outlet centers, fiesta centers, boutique centers, industrial shopping centers, professional & medical offices, entertainment centers, and condo-shopping centers are all innovative approaches currently being used to enliven existing strip centers.

OUTLET CENTERS

The outlet center, alternatately referred to as the off-price center, is one of the most popular trends in retail development today. The outlet concept has been found in 16 centers from 42,000 to 478,000 s.f. and is not unique to strip centers.

There is some confusion in the industry as to what constitutes an outlet center. "Outlet" used to mean a place selling one manufacturer's goods without a middleman, but this definition appears to be blurring. "Discount" suggests private branded merchandise. "Off-price" sometimes cannotes something of a lesser kind or quality.

― 16 "Big Developers and Major Retailers are Going Outlet", Shopping Center World, January 1984. ―
Whatever the strict definition, outlet centers are one solution for developers anxious to bring retailing back to strip centers. Developers agree that the two secrets to successful off-price centers are location and tenant selection.

The off-price center will generally have a larger market trading area for a well accessed center. A young growing market or a mature market not tied to a single industry are best, with incomes sufficient to encourage shopping. Interestingly, off-price merchandise tends to do best in affluent areas where people have more time to shop. A working person whose shopping is scheduled around work commitments has less time to hunt for value.

The same components that produce good tenant mix in a traditional center produce good tenancy in an outlet center. Just because the sign out front says off-price or factory-outlet will not bring shoppers running. Merchandise quality and selection, along with shopper defined measures of value, will determine long term success.

Finally, the off-price center is coming under strong competitive pressure as too many developers are remerchandising their centers as off-price. Further, some of the larger malls are allowing off-price retailers into their otherwise traditional tenant mix. Blending of off-price outlets into traditional malls is being met with less
resistance from traditional retailers than you would expect. Most retailers realize that shoppers are demanding off-price and they will leave the mall settings if off-pricing is only available elsewhere. A strip center that competes with a regional mall for the same shoppers has an uphill fight.

**FIESTA CENTERS**

There are some urban strips that are so well located that they deserve consideration as mini-Quincy Markets. These fiesta centers are really not strictly retailing centers but are rather social and entertainment environments in which retailing can comfortably take place. Often the primary source of revenue are the food courts, supplemented by numerous boutiques.

The physical configuration and lack of architectural distinction are the primary obstacles to renovating a strip into a fiesta center. To be successful, these centers must amaze and delight, and be a destination unto themselves. Uncommon locational characteristics and surrounding tourist attractions are necessary to support Fiesta Center Development.

**INDUSTRIAL SHOPPING CENTERS**

At the other end of the spectrum from fiesta centers is the industrial shopping center. These industrial shopping centers are appropriate for very delapidated strips that have
lost their retailing appeal. These centers, typically without anchors, bring together heavy commercial tenants into no-nonsense strips with storefront design, shared parking as well as manufacturing and warehousing facilities.

The typical tenant list for such a strip might include a cabinet maker, an electrician, an auto customizing shop, an appliance store, a wholesale plumbing supply store and a building contractor's office. Tenants that are normally excluded from traditional strip shopping centers are often the ultimate tenant for an industrial strip center.

One timely variation on the industrial strip center is the home improvement center. Tenants are grouped around the home renovation and furnishing theme to enhance the drawing power of the center and supply a shopping destination. Beyond the trades associated with homebuilding, this center might include a garden center, a do-it-yourself framing center, or a furniture warehouse type operation.

PROFESSIONAL & MEDICAL STRIPS

"On an average day at my podiatry center with my 15-foot front and two by four foot lit sign, and with twenty shoe stores sending me referrals, I'll make at least 1,000 people aware of my presence. This compares to maybe twenty five people at my other office in a professional building in nearby downtown where I'm on the second floor and have a one by ten inch sign, and get a few referrals from other doctors."17

17 "Shoppers Get Service at the Center as Professionals Move to the Malls"Shopping Center World, April 1983
Professional Offices are discovering strip retailing for much the same reason as Willie "that's where the money is" Sutton discovered banks: that's where the people is. Although rent for retail locations is typically higher than office locations, many professionals are beginning to consider retail sites for their offices. Many professional offices are finding that the convenience aspect of their service is as important to the consumer as the service itself. Sears has accelerated this trend by bringing investments, insurance, and health care professionals into their mall locations. Independent practitioners are being forced to compete on a convenience basis.

The movement of professionals into retail locations has its roots in 1977-78 when a series of federal and state court decisions established that these professional firms have the ethical right to advertise (and thus to try to do business on a commercial scale).

From a developer's point of view, the typical percentage rent clause is deemed fee splitting in the laws of most states and professional organizations and must be eliminated. Developers usually insist on base rentals that are four or five points higher than retail tenants, and usually insist on Consumer Price Index Linkages with frequent reviews.

The concept of grouped professional services wherein a cluster of professional offices is used (similar to a food
court) is being experimented with by some national developers. This is probably an inappropriate use in a small strip in that these services on their own do little to stimulate traffic, nor do there appear to be many linkages between competing services. Its hard to imagine a shopper seeing his lawyer about a divorce staying around for a quick root canal and some car insurance.

ENTERTAINMENT CENTERS

Theaters and bowling alleys don't lead the list of high rent payers but any rent is better than no rent. In over stored locations the entertainment center is a very creative and congruent use of an older strip center. The use mix in such a center might include a health club, bar & grill, night club or disco, theme restaurant, YMCA, video store or even a good restaurant. The center would necessarily do most of its business between noon and closing and the hours of operation might reflect this.

CONDO CENTERS

Condo housing. Condo Office Buildings. Condominium Warehouses. Can condo retail centers be far behind? In fact, they have been around for some time.

A 1982 article in Shopping Center World was entitled "Condominium Centers: Just a Fad or a Coming Fact?" Since I have found no further mention of the condo centers since
that article, I am assuming it was a fad since faded.

The single biggest hindrance to going condo with a strip would be the availability of merchant financing to acquire the store. The typical local tenant in a strip has a life expectancy of about six years. Who prequalifies the next buyer? The lenders are rightfully concerned that with the lack of a single entity responsible for, and with an economic stake in the performance of the retailing, the center may lose its tenant mix, commitment to maintenance, and ultimately its economic viability.

All the issues discussed in this paper deal with retailing as more than a collection of individual shops and shopkeepers. The condo concept has trouble dealing with these issues, even with carefully crafted condo-documents and restrictive covenants. Better to use the merchants as a source of funds in a Realty Trust and keep the center ownership in the hands of a single source than "go condo."

NOT A STRIP AT ALL: THE PODMALL

Although not specific to strip mall rehabilitation, I find the lessons learned from abandoned gas stations to be instructive when thinking about smaller strip centers. 18

In California, retail developers are acquiring these gas stations left behind by the 30 mpg subcompacts, and

18 "The revenge of the podmall", Forbes, 15 July 85
converting them into mini-retailing centers called podmalls. These centers typically contain four to six smaller stores and fifteen to twenty spaces. Often they are "anchored" by a convenience store but not always. There are some 2000 of them now!

The attraction for retail tenants is visibility, traffic count, and market area a.k.a. location. The typical podmall has a 100,000 population within two miles and a 45,000 cars per day passing by. This translates into developer rents of twice retail mall rates, often $3. per sq. ft. per month.

Perhaps podmall development will be "the most significant trend in retailing today" tomorrow.
CHAPTER SEVEN

"A DOLLAR BORROWED IS A DOLLAR EARNED"

FINANCING CONSIDERATIONS

The typical strip center is attractive as a real estate deal in today's market because it is one of the last remaining real estate ventures in which conventional lenders do not necessarily "take a piece." As these properties are often bought as passive investments, the equity required to meet the lender's debt coverage ratio's is often enough to provide the comfort level necessary to secure the loan.

Also these are existing income producing properties, not development deals. The value of bricks and mortar in place can be assessed and the financial history of the center can be established. The valuation required by the bank can be based upon an income approach, replacement cost, or comparable sales analysis. In any event, the objective of the developer using this conventional financing approach is to secure enough equity to provide the gap between asking price and the bank's comfort level in making the loan.

Some interesting peculiarities exist when the center is severely delapidated or when substantial rehabilitation expense is anticipated. In this situation, the purchase money mortgage is not sufficient as a stand alone mortgage
instrument as substantial expenditures have yet to be made on rehabilitation, tenant improvements, and leasing and other soft costs.

An interesting device developed by GE Credit Corporation is the earn out mortgage. The center is purchased based on cash flow or comparable sales basis with the money for renovation and tenant improvements advanced to the developer as the leases are signed. The mechanics of this mortgage arrangement are interesting as they allow the developer to see his funding grow as the value of his leases (and simultaneously the value of his center) grow. Typical earn out's advance about $8.00 in construction funding for each $1.00 in annual cash flow from base rent.

Owner financing for the first purchase money mortgage is common in these transactions. Many of these centers are old family trusts with substantial equity and very little in existing debt. An interesting play on owner financing is to purchase only one-half of an undivided interest in a property. This arrangement works particularly well in centers being purchased for rehabilitation. Often the existing owner is selling his center not on a cap rate based on today's earnings but rather on projected earnings after rehabilitation. In this scenario, conventional measures of return such as return on equity and free and clear return (i.e. non-leveraged) are not attractive to most investors.
In this scenario the buyer gets up front cash and the full purchase price based on a cash flow that has yet to be seen. The purchaser gets the operation of the center, a preferred return calculated to bring the return on his equity contribution to acceptable levels, and 1/2 of the added cash flows beyond that amount. In addition the buyer has locked in the purchase price of the center via an option that is tied to the here to fore unrealistic pricing set by the seller. Cash flows above the minimum preferred return required by the buyer are split 50-50.

There is an interesting wrinkle to releasing the rehabilitated strip center that bears directly on future financing. The major tenants in a rehabilitated strip will usually insist on a below normal base rent to minimize their risk in a non-proven location. Often this is acceptable to the developer desiring a name tenant and some leasing momentum. The developer often counters by obtaining a higher than average percentage rent from the tenant. Unfortunately, lenders are reluctant to consider percentage rents as part of the cash flow basis for mortgage refinancing.

As the typical strip redeveloper will wish to refinance his center in four to six years, the poor base rent presents

18 Lamm, Robert R. "Selling an Overpriced Shopping Center" Shopping Center World, December 84
an artificial cap on center performance. One way to eliminate this is to include a provision in the lease that converts the base rent in year four to ninety percent of the base rent in year three plus all percentage rent paid in that year. This is not an intimidating clause to the tenant, and it provides the developer with a higher cash flow on which to base his refinancing.

There is a school of thought espoused by some purchasers of shopping centers that suggests unleveraged, all cash purchases are the best form of acquisition, largely due to the simplicity of the transaction. This makes no sense to me. The interest write-off is lost, the power of leverage on futures evaporates, the number of deals that can be accomplished is limited and hence the risk is poorly distributed over a limited property portfolio. The power of all cash purchases continues to evade me.

19 Goodman, Gary. "When Shopping for Centers, Buy with Cash," Shopping Center World, Sept 84.
CHAPTER EIGHT
SUMMARY & CONCLUSIONS

I have tried to demonstrate through my research that small strip centers are not retailing or real estate dinosaurs, but viable real estate properties that offer significant opportunities for innovation and profit.

There was a surprising amount of printed material available on the rehabilitation of small strip centers. The economic potential and development opportunities presented by these small centers has not gone unnoticed. These are highly sought after properties in the development community and prices for these centers have been escalating rapidly.

Moreover, there are a number of players seeking small center opportunities. Individual investors, partnerships of professionals seeking shelter and inflation protection, syndicators, REITs, development companies doing exclusively retail projects and even the major national tenant chains have been active in purchasing centers.

These small centers offer some unique advantages over other buy-hold real estate opportunities. First, many of the sellers are family trusts that developed centers many years ago as part of larger residential projects. They are often being held at exceedingly low basis with little depreciation
shelter flowing from the property. These family trusts often lack the expertise and initiative to aggressively manage the center and maximize returns.

Also there is the anti-competitive aspect of owning prime retail space in well developed markets. For all the reasons listed earlier in Chapter Three, good retailing locations are very much supply constrained.

The inflation protection afforded by a well crafted percentage rent clause is not to be found in any other real estate property, except perhaps hotels. The percentage of sales clause over a pre-determined sales base provides a daily inflation adjustment to the strip center owner.

Management issues are far less intensive than with an office building or residential property. Recall that the tenant is entirely responsible for his own interior space, including floors, fixtures, HVAC, and finishes. There are usually no common interior spaces being maintained by the owners in these small strips. Tenant turnover is generally less, and there are outside professionals who specialize in retail brokerage and management.

The buildings themselves are models of simplicity with no elevators or other sophisticated mechanical equipment. Electrical systems are basic and telecommunications equipment is usually limited to public address systems and pay phones.
Finally, there is virtually no public sector involvement because these are existing properties not subject to the stringent environmental and civic reviews which accompany most new development projects.

Couple all these factors with the value creation opportunities described in Chapter Five and the economic power of these small strips can be fully appreciated.
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