

MEMORANDUM

TO: City Council

FROM: Alfred D. Lott, ICMA-CM, CPM
City Manager

SUBJECT: *Status Report* DATE: February 18, 2021

Status Report

1. Impact of COVID-19 On Retail Real Estate

The International Council of Shopping Centers (ICSC) Research Office released a report today called The Impact of COVID-19 on the Evolving Use of Retail Real Estate. According to the report:

American retailers and commercial real estate companies express strong confidence that shoppers will visit stores in greater numbers in 2021 — a sign of resilience in an industry beset by the COVID-19 pandemic. After a year in which nearly every aspect of the store and shopping center experience has been modified to adhere to social distancing and other health precautions, retail executives and shopping center operators assert that the crisis is driving a wave of innovation that positions the industry to absorb future shocks. To handle the sudden surge in click-and-collect shopping as cities locked down in 2020, parking lots became hubs for curbside pickup. As the economy reopened, stores reconfigured their layouts to keep shoppers and employees safe. While the industry looks ahead to the future, retailers and commercial real estate firms say they will make targeted investments in digital marketing and online storefronts to keep up with the convergence of online and physical retail.

The results from ICSC's survey of retail and commercial real estate leaders illustrate how the adoption of technology, shifts in merchandising and operational strategies, and safety precautions put in place during the pandemic will evolve in 2021 and beyond. The research shows that an aggressive omnichannel approach anchored by a store network helped retailers manage through the pandemic. It also shows that to remain relevant and keep customers coming back to stores and centers, retailers and center operators alike need to continue to innovate and give consumers a taste of the future.

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The Impact of COVID-19 on the Evolving Use of Retail Real Estate

Introduction

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Results from this survey of retail and CRE leaders illustrate how the adoption of technology, shifts in merchandising and operational strategies, and safety precautions put in place during the pandemic will evolve in 2021 and beyond. Our research affirms that an aggressive omnichannel approach anchored by a store network helped retailers manage through the pandemic. It also affirms that in order to remain relevant and keep customers coming back to stores and centers, retailers and center operators alike need to continue to innovate and give consumers a taste of the future.

Objective, Methodology and Respondent Profile

From October 29 to November 10, 2020, an ICSC survey conducted by OnResearch, a market and consumer insights firm, polled U.S. real estate industry leaders – comprising 277 executives retailer companies and 107 representatives from commercial real estate (CRE) companies. The survey examined the actions brick-and-mortar locations were taking in response to the COVID-19 pandemic; assessed how retailers and CRE companies had adopted or changed technology, merchandising, and logistics in response to COVID-19; and explored how these businesses planned to operate in the post-pandemic period.

The online survey employed a quota sample to ensure a minimum number of respondents across various sizes and regions. Survey respondents comprised senior director-level roles and above among retail respondents, and property manager-level roles and above in the CRE sector.

Survey participants included independent retailers with annual revenue under \$45 million (small retailers), retailers with revenue from \$45 million to \$3 billion (mid-sized retailers), and large chains with revenue over \$3 billion (large retailers). Among CRE companies, participants included firms with gross leasable area (GLA) under 6 million square feet (small CRE) and CRE companies with GLA over 6 million square feet (large CRE).

Section 1: Safety and Operations

Consumers and government officials have made safety a priority during the pandemic and retailers and CREs have responded. Some of the most visible changes to the shopping experience since early 2020 have occurred outside stores, as customers are being asked to stand in line or mask up. Though regulations vary widely by

location and retailer, implementing coronavirus-related precautions have become standard industry procedure. Twenty-eight states have some type of [OSHA-approved coronavirus plan](#) in place, emphasizing the magnitude of the crisis for workplaces such as retail outlets.

In our survey, the three most common safety precautions taken by both retailers and CRE companies included complimentary hand sanitizer, free masks, and temperature screening upon entering stores. Additionally, retailers implemented maximum capacity limits (36% of respondents), while CREs focused on sanitizing properties (40%).

Small CRE operators say they plan to continue focusing safety resources on social distancing among shoppers and employees, with 79% of respondents saying they will likely leave plexiglass barriers installed for the next 12 months. The smaller centers are planning shortened hours of operation, with 76% favoring truncated hours compared to just 53% of large CRE firms that reported limiting hours.

Our survey also revealed that independent retailers are using signage and crowd management measures

to a greater extent than their larger retail counterparts. For instance, while 58% of independent retailers say they intend to manage lines outside their storefronts in the coming year, just 35% of the large retailers intend to continue doing the same.



Store layouts allowing for social distancing will continue to predominate inside stores, though retailers of different sizes indicate they'll take different approaches to creating space between shoppers. Independent retailers were more than three times as likely as larger chains to say they plan to continue using one-way movement in stores (47% vs. 13%). By contrast, two-thirds of the largest retailers intend to stick with redesigned floorplans, compared to only 37% of smaller independent retailers. Take a trip to the national grocery chain or pharmacy in your area and you will likely see this already in play.

The safety precautions put in place to allow for safer trips to shopping centers have required new expenditures and created a host of new operational challenges. Among CRE respondents, for instance, 72% saw increases in their operational costs due to the implementation of new cleaning procedures, new signage and other protective measures. The same share of CRE firms said COVID-19 had compelled them to eliminate touchpoints, while half of these companies made changes so shoppers could drop in and complete their purchases quickly.

Many of these changes are in response to consumers becoming more purposeful with each trip in an effort to reduce dwell time and potential exposure to the virus. However, many may be here to stay. Over the course of the pandemic, ICSC has conducted a regular survey of 1,000 consumers gauging their sentiment on topics such as the economy, spending, and shopping and dining habits. Consistently, an overwhelming number (most recently 70%) indicated they would like to see the current safety protocols extended beyond the pandemic. Historically, cleaning equipment and crews remained behind the scenes, with clean up taking place when customers were gone for the day; but, today, many retailers and centers are putting cleaning efforts front and center to demonstrate that safety is a priority.

Continuing Safety Precautions Over the Next 12 Months



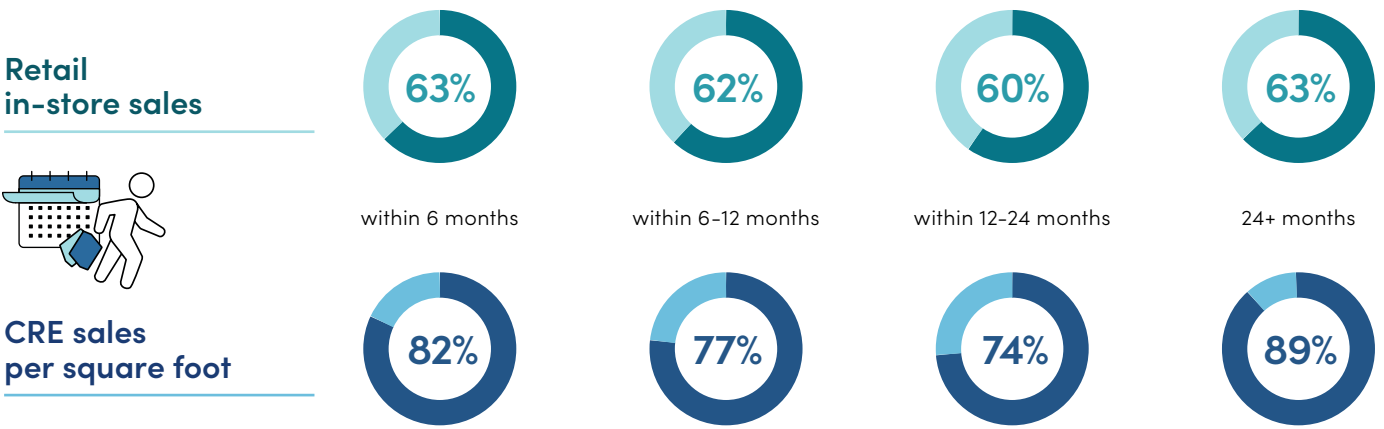
Section 2: Business Metrics – Resilience and Optimism

U.S. unemployment in 2020 hit a high of 14.7%, the highest rate in the history of the data. Visitors to retail real estate properties dipped from a high point in February – at the start of the crisis – to April when lockdowns were in full swing. Mandatory closures of nonessential businesses, as well as general safety concerns, kept many shoppers at home during the early days of the pandemic, and in certain areas of the country, throughout the year.

Survey respondents confirmed the drop, with many of the retailers reporting greater decreases than increases in daily visitors and in-store sales because of the crisis. Among CRE respondents, the picture is mixed: A larger share said sales per square foot were up compared to those that reported declines. While 42% of CRE operators saw increases in visitors, 43% said that shopping center visits were down because of COVID-19. These results are not surprising when factoring in the role of essential retailers, such as grocers and pharmacies, in the pandemic as well as basket-size increases due to less frequent consumer visits.

Even with the drop in visits, there remains optimism for the future. Shopping center operators anticipate that properties will deliver better results across several business metrics over the next 12 months. This forecast includes 77% of CRE firms that expect higher sales per square foot, compared to just 5% of CREs that anticipate sales figures to fall. Eight in ten CREs predict an increase in the number of shoppers per day, and three out of four CRE respondents predict longer dwell times by shoppers.

Expectations of Sales Metrics to Increase



Additionally, 60% of respondents said they anticipate foot traffic to return to pre-COVID levels at their shopping centers within 12 months of containment of the virus. About a quarter of respondents believe shoppers will return to pre-COVID levels even sooner – within six months. The positive outlook for the year ahead isn't limited to landlords. According to our recent 2021 Consumer Outlook Survey, more than half of consumers (54%) expect to resume pre-pandemic behaviors once it is safe to do so.

Retailers were equally optimistic about shoppers returning to their stores in the next 12 months. Across all sizes in the segment, 55% of respondents expected their in-store traffic to return within 12 months. In a less optimistic outlook than CRE firms, only 15% of retailers believe that the volume of shoppers will return to pre-COVID levels within six months. Bottom line, most of our survey respondents believe people are eager to get out of their houses; however, retailers are less optimistic than their CRE counterparts.

The Consumer Outlook Survey also found that 43% of respondents said that within a year they would resume visits to malls at the same pace as pre-COVID levels, and 42% said they would visit brick-and-mortar retailers on a regular basis again.

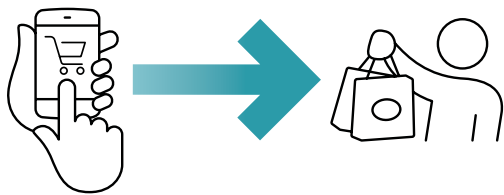
It is clear that even with fewer store visits in the future, retailers are counting on the trend of larger basket sizes to continue. Half of retailers anticipate that in-store revenue will account for more or significantly more of their total sales revenue in the coming year. Smaller independent retailers were less optimistic about the short-term future, however. Sixty-five percent of consumers indicated that, in 2021, they will try to make more purchases from small/local businesses, which could result in strong sales.

Section 3: Digital Strategy and Investments

There is little doubt that the pandemic has dramatically accelerated consumer adoption of online shopping, and for some retailers, it condensed years of operational and digital transformation planning into a matter of months. Many of the changes have been made to enhance the online shopping experience for consumers while

also allowing for sales to continue amidst mandated closures and ongoing safety concerns.

Expected Increases in Click and Collect Will Drive Retailer Actions Over the Next 12 Months



- 62%** # of online orders fulfilled at brick-and-mortar stores
- 61%** % of floor space for stocking/warehousing and distributing online orders
- 63%** % of parking lot space being used for online order fulfillment
- 61%** Staffing specifically to accommodate online order fulfillment
- 61%** Retail warehousing/stocking capacity

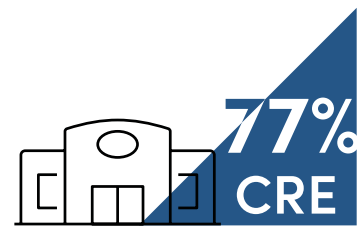
Meeting the increased demand in online ordering requires infrastructure – something 40% of retailers identified as being one of their greatest operational challenges during the pandemic. The outcome of those struggles is that 70% of all retailers are making investments in their digital storefronts a priority. Although consumers have come to expect, and demand, an online purchasing option, smaller brands report that physical stores still capture the majority of their sales. In fact, in-store sales comprise 56% of their overall revenue, whereas large retailers see the majority of revenue (57%) originate online.

Online order fulfillment wasn't only a solution to help get products into the hands of consumers, respondents specifically noted that it also elevated the importance of the relationship between stores and shopping centers and fulfilling online orders. Three in four respondents said the pandemic demonstrated the increasing role of shopping centers in fulfilling online orders, while the same share said

the crisis made them aware of the degree to which online orders could drive store success. Undoubtedly, this is a trend that will continue post-pandemic.

Another key area of focus is fulfillment – the process of acquiring, warehousing, and readying merchandise for pickup or delivery. Lockdowns in the early weeks of the pandemic spurred massive growth in online shopping – which surged more than 30% between the first and second quarters of 2020 – dramatically transforming

Online Order Fulfillment Will Be Essential to Ensuring Physical Stores Remain Financially Viable Post-COVID



fulfillment operations. For retailers this often meant pulling inventory from a store to fulfill click-and-collect orders from the 34% of consumers taking advantage of the option each month. The impact on CREs was dedicating space for consumers to pick up their purchases while observing health and safety protocols.

Our study found that two in three retailers (66%) across all sizes expanded the number of stores offering in-store fulfillment of online purchases in response to COVID-19. The smallest retailers made the biggest adjustments — 73% added click-and-collect options at stores — as rising demand for e-commerce hit Main Street and provided a lifeline to struggling businesses. In looking ahead, a third of retailers recognize that a primary draw to physical locations will continue to be the ability of consumers to make online purchases they can then pick up at the store.

Executing the logistical challenges of getting orders out of warehouses or stores and into the hands and personal vehicles of shoppers has spurred other changes as well. Pickup locations stretched beyond the store and into the parking lot where curbside pickup became a staple. In fact, three in four CRE firms reported using their parking lots to accommodate online order fulfillment and 56% said they are currently using at least half of their parking space for curbside pickup of online orders. The dedication of this space is unlikely to change in the future as consumers have not only come to expect this convenience, but 41% plan to continue using it post-pandemic.

As previously noted, nearly half (47%) of retailers have made technology and digital infrastructure investment their top priority since the onset of the pandemic. With those investments now underway, retailers of all sizes are looking to shift their focus to future marketing efforts.

More than half (56%) of retailers expect to prioritize digital over in-store investments as part of their marketing outlays in the year ahead. Among large retailers, 78% say their marketing campaigns will focus on their efforts to enhance the digital customer experience, as well as growing online sales, brand positioning and ensuring customers are aware of the health and safety protocols that have been implemented. While CRE firms are less focused on the online sales channel, their focus will also include health and safety measures as well as ways to help drive foot traffic to pre-pandemic levels.

Conclusion

As the cases of COVID-19 have risen and fallen across the country so too has the percentage of people who are comfortable following their typical daily routines. In our October 2020 consumer survey, 46% of respondents said they were engaging in a “normal” level of outside-of-home activity. That percentage is sure to rise as the virus subsides and consumers feel safe spending more time away from home. The extraordinary challenges that retailers and CRE companies have faced throughout the pandemic have placed tremendous strain on the teams that keep stores, shopping centers, and e-commerce operations running. We are wholeheartedly appreciative of the commitments to customer and employee safety as the emergency around the pandemic evolves.

The public should feel assured, whether they choose small, independent retailers or do their shopping at larger centers, that the efforts to keep people safe are being implemented in accordance with the most accurate public health guidance — from displaying signage promoting good safety practices and creating one-way movement through stores to designing floorplans to allow for social distancing

The pandemic has accelerated the adoption of industry trends such as click-and-collect shopping, that were already underway before the crisis. Now, there’s even greater integration between digital and physical channels and more investment in infrastructure and operations that offer greater flexibility and convenience to the customer. Our survey demonstrates that stores will continue to account for growth and remain essential to the shopping experience; however, that experience will likely look and feel quite different.

The long-term strength of the CRE industry is critical to communities across the country. Retailers have demonstrated throughout this crisis that they are capable of meeting demand, both online and in person. We are excited to see how the industry will continue to change and innovate during these challenging times.

ICSC is the preeminent membership organization serving retail and real estate professionals. Our members believe ICSC's unparalleled programs and services are the most efficient and effective way to develop relationships, facilitate transactions, share insights and shape public policy and perception.

