

Declining Manhattan retail rents:

The market is finding a new level

As of Q3 2017, retail rents in the Manhattan market continue to decline. The market is reckoning with the implications of an environment where pricing has been misaligned with current demand levels, as it adapts to the larger challenges of an evolving retail business model. While declining rent creates challenges for some landlords and investors, the downward adjustments are helping to stabilize the Manhattan retail landscape—and encouraging tenants to take advantage of a healthy New York City economy.

Between 2010 and 2014, retail rents surged in Manhattan, outpacing the growth in local spending. For available space along the main corridors tracked by CBRE, the average asking rent more than doubled on average, while the city's total retail sales (excluding online sales) grew at the much slower rate of 36% over the same period. This suggests that, for many retailers, rents surpassed the revenue that could be achieved from in-store sales.

250 210 200 74 162 Growth Index 150 145 136 100 Indicates spread at peak and Q3 2017 50 0 Q3 2015 Q3 2017 Q3 2016 NYC Total Retail Sales (excluding online) Manhattan Average Asking Rents

Figure 1: Manhattan Average Asking Retail Rents vs NYC Total Retail Sales Indexed

Source: CBRE Research, U.S. Census Bureau, Moody's Analytics.



Since peaking in 2014, however, the overall average asking rent among Manhattan's main corridors has decreased by 23%. This adjustment is bringing rent growth between 2010 and 2017 closer to the trajectory of retail sales growth, which has expanded steadily in recent years. These two trends together suggest that the market is coming closer to alignment between what tenants can afford to pay and the revenue they can achieve.

Figure 2: Average Asking Rents*

Neighborhood	Corridor Parameters	Q1 2010	Peak	% change from Q1 2010 to peak	Current Q3 2017	Current % from peak
Upper West Side	Broadway 72nd to 86th Streets	\$255	\$408	60%	\$295	(28%)
Upper East Side	Third Avenue 60th to 72nd Streets	\$255	\$372	46%	\$287	(23%)
Upper Madison Avenue	Madison Avenue 57th to 72nd Streets	\$807	\$1,771	119%	\$1,289	(27%)
Plaza District	Fifth Avenue 49th to 59th Streets	\$1,650	\$3,850	133%	\$3,412	(11%)
Grand Central	Fifth Avenue 42nd to 49th Streets	\$420	\$1,366	225%	\$1,023	(25%)
Times Square	Fifth to Seventh Avenues 42nd to 47th Streets	\$1,100**	\$2,413	119%	\$2,086	(14%)
Herald Square	34th Street Fifth to Seventh Avenues	\$446	\$988	121%	\$575	(42%)
Flatiron / Union Square	Fifth Avenue 14th to 23rd Streets	\$249	\$419	68%	\$406	(3%)
SoHo	Broadway Houston to Broome Streets	\$507	\$871	72%	\$607	(30%)
Downtown	Broadway Battery Park to Chambers Street	\$178	\$421	136%	\$414	(2%)

Notes: *Prices are in \$ per sq. ft., based on ground-floor direct space. **Q1 2011.

Nearly all of Manhattan's main shopping corridors have experienced meaningful declines in their average asking rents in recent years, although the degree of these decreases varies considerably. Some of the biggest declines have been seen among corridors where rents more than doubled in previous years, including Herald Square, Upper Madison Avenue and Grand Central, with rents contracting from peak levels by between 42% and 25%. Other corridors that recorded lesser increases are also seeing downward rent adjustments—including Broadway both in SoHo and on the Upper West Side, as well as Third Avenue on the Upper East Side—ranging from 30% to 23%.

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Source: CBRF Research.



Meanwhile, other locations have seen more modest downward adjustments. Upper Fifth Avenue in the Plaza District, which experienced a rent increase of 133% between 2010 and 2014, has seen its average asking rent drop only 11%, and remains the city's most expensive and coveted retail location. Times Square, which has been the beneficiary of the shift to experiential retailing concepts, has seen its average asking rent fall a relatively limited 14%, despite having risen 119% between 2010 and 2014.

In some corridors, average asking rents have remained fairly resilient against the trend. The Flatiron / Union Square section of Fifth Avenue has been the most stable in recent years, falling just 3% after climbing more than 68% earlier in the cycle—a modest increase compared to most of Manhattan's other shopping corridors. Downtown Broadway is perhaps the biggest outlier among recent trends. Rents continued to rise in this once under-performing corridor through Q2 2017, helped by the delivery of new, high-quality retail product as well as by strong growth in demand drivers.

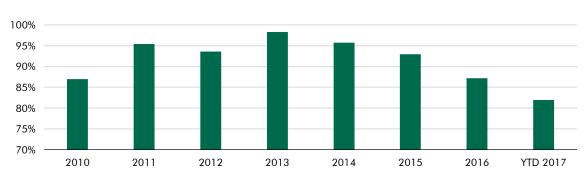


Figure 3: Taking Rent Index

Source: CBRE Research.

Studying asking rent tells only part of the story. Looking at taking rents today versus where they stood when rents were at their recent peaks provides additional insight. In the surging market of 2013 and 2014, the competitive environment left little room for negotiation: on average, the taking rent index ranged from 96% to 98%, and some leases closed at, or above, asking rent. By contrast, as the market has softened, not only have asking rents declined, but the taking rent index has fallen considerably: looking at completed transactions through Q3 2017, the average taking rent is just 82% of asking—the lowest percentage since 2010. Additionally, net effective rents have declined, as current deals include more generous landlord concession packages—in the form of tenant improvement allowances and free rent periods—than were offered in the peak market.

There are still examples of tenants bidding up rents to secure coveted spaces in high-traffic locations, particularly in the case of food service operators and experiential retailing concepts. Yet, in much of Manhattan, the overall trend has been a significant decline in both asking and taking rents to a level more in line with the revenue potential. While additional rental adjustment is possible and likely in some locations, it appears that the Manhattan retail market is approaching a new level.



VIEWPOINT NEW YORK CITY RETAIL

DEFINTIONS

Availability — Space that is actively marketed; includes spaces for immediate and future occupancy.

Asking rent — Average asking rent calculated using the straight line average for direct ground-floor spaces that have street frontage along one of the 16 corridors tracked by CBRE.

Taking rent index — Initial base taking rents as a percentage of asking rents.

SOURCES

¹ U.S. Census Bureau, Moody's Analytics

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