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Anchors away! - Retail

Real estate experts say market should move full steam ahead into economic recovery

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IBJ Graphic/Jo Payton

Captains of Indianapolis' real estate ships charted waters carefully in 2003, trying to steer clear of hull-splintering obstacles such as high vacancy rates, slow leasing activity and business owners who are still tightening down the hatches.

Some had an easier time of it than others. Office brokers and developers struggled to right their ship as large amounts of sublease space continued to buoy suburban vacancy rates. Retailers had mostly smooth sailing, but dark clouds are gathering on the horizon for the city's grocery stores, which deftly maneuver through a sea of competitors. And wind continued to fill industrial's sails with major leases such as the 1.1

million-square-foot deal signed by Case New Holland in Lebanon, although older industrial buildings still need to pick up speed.

Plainfield, Avon and Brownsburg were some of the most popular destinations for industrial and retail cruises, but Clay Terrace in Carmel and the Michigan Road/West 86th Street area in Indianapolis promise to steal away some retail visitors as new developments come online.

And downtown, the Market Square area looms on the horizon as a fleet of developers and observers wait to see how the ripples of that redevelopment will affect them. In the meantime, new restaurants and retailers will continue to dock ship downtown.

IBJ invited 12 of the city's top office, industrial and retail brokers and developers to open their captain's logs and review the past year's journey. They mused on near-shipwrecks and record-time voyages, and took out their spyglasses to look forward into the coming year.

To the sailors' delight, most saw red skies as the sun set on 2003.

Participants: Brian A. Epstein, president, **Urban Space Commercial Properties**; Mark Perlstein, partner, The Linder Co.; Rick Sutton, senior associate, CB Richard Ellis; Stephen P. Zinkan, partner, Flynn & Zinkan Realty



Epstein

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IBJ: What do you think was the most significant event or trend in the Indianapolis retail market in 2003?

SUTTON: To me, it is the ongoing question mark about groceries. For consumers in this market for as far back as I can remember, it has been a good market. You get good buys, but with Wal-Mart's decision to come in with Neighborhood Markets, and all the existing players, and Costco bringing probably 80,000 to 100,000 feet of grocery space to the market, it just seems to be the 800-pound gorilla in the room that attracts questions and comments.

EPSTEIN: From the deals I have been working on over the past year, one of the trends in the restaurant sector would be the immense difficulties the independent restaurants of this city have had. I see that trend kind of carrying through with the downturn in the economy and the difficulty in getting money from the banks, in the restaurant sector at least.

PERLSTEIN: Sak's entering Indianapolis is probably a very, very important announcement for the city. The joint venture announcement between Simon [Property Group Inc.] and Lauth [Property Group Inc.] on Clay Terrace was a very interesting event. I think they have hurdles to overcome and I think they will overcome them. I think the project will be successful. Also, what has happened on the 96th Street corridor in the past year and a half to two years is almost beyond belief. Lastly, probably on a micro

level, I think the closing of Atlas Supermarket meant a lot to a lot of people. I think it is going to be interesting to see what happens to that project.



IBJ Photo/Robin Jerstad
Perlstein

ZINKAN: The redevelopment in 2003, whether it was the Greenwood Park Mall, which is a sparkling gem on the south side, the redevelopment of the northeast corner at 82nd and Allisonville Road, or what Target is doing in Nora, is significant because I think they represent great properties that have some type of functional or economic obsolescence, yet are great locations.

IBJ: What do you think is driving retail development or redevelopment right now?

SUTTON: It is no one thing. I think the grocery repositioning is going to be important for a long time. That is going to be a really difficult thing for us to predict and for other developers and brokers to react to. The grocers are constantly rethinking their positions.

ZINKAN: I think those dynamics are no different from any other retailers. You have a retailer wanting to increase sales either through new store openings or increasing same-store sales against a very competitive environment and constraints on the supply side. We are blessed to do some Kroger work, and they are doing excellent in this market. To compete globally against a non-union grocer such as Wal-Mart, they have to level the playing field in terms of labor and other costs. They dropped their cost on a gross margin basis probably 5 to 6 percent about a year ago, which put further pressure on Marsh. Although we don't do any Marsh work, they are a great hometown favorite. But when you look at their access to capital versus a major player such as Wal-Mart or Kroger, I see that as being an impediment in moving forward for the hometown folks.



IBJ Photo/Robin Jerstad
Sutton

PERLSTEIN: What is also driving retail development now for every retailer is convenience: creating one-stop shopping as much as possible. The other area that is driving it is the demand for retailers to back-fill markets to gain market share. You are going to see Bed Bath & Beyond attempting to get locations where Linens n Things is getting locations; the same with Circuit City and Best Buy. There is no question low interest rates right now are driving more development.

EPSTEIN: One of the trends we are obviously going to get into a little more in the next year and a half with Clay Terrace opening up is a whole new genre of retailers we don't have in this market. Around the country, I am

seeing other lifestyle centers with retailers like Sur la Table and Crate and Barrel. There is a whole laundry list of retailers that I was never really familiar with until I went to some of these lifestyle centers.

IBJ: Speaking of lifestyle centers, Clay Terrace could open in late 2004, Premiere Properties is planning one in Plainfield, and Ameriplex is looking at creating something like that at the new Six Points Road interchange. What effect does that have on retail in other locations as you lease or develop?

SUTTON: Whenever you do that kind of center--in the neighborhood of 250,000 square feet--new tenants are important. But it will pull dollars from someplace else. So it will have an effect down the line on something else. If you live much below 40th Street on the north side and much above a certain point on the south side, you have to travel a long way to find any retail.

That is a disturbing development, but we are not going to change it. Retail is following homes and green space. The more that happens, I wonder about what is left behind, and the boxes that are left.



Zinkan

IBJ Photo/Robin Jerstad

PERLSTEIN: When Clay Terrace opens next year, it will have a definite effect on sales at any of the upper end retail projects on the north side of the city, including the Fashion Mall, Merchant's Square, and Village Park. But I think they will pick back up. They will take a hit initially. I think when Plainfield's development opens it is going to be interesting to see the impact. It brings up the point, what will be left for the Ameriplex development once Plainfield opens? That is going to be very interesting for that project.

SUTTON: I don't think people have begun to understand yet what the redevelopment of the airport is going to do. They are moving a freaking interstate. It is going to bring a whole lot of ripple effect. A big economic development project like that throws off a lot of need for retail.

IBJ: In the past few years we have seen some new national retailing names come into the market. Do you think we will continue to see that next year?

PERLSTEIN: Our market is only large enough to support so much new retail. We are not Chicago. Chicago gets concepts we are not getting yet. We are much slower from that standpoint. There have been rumblings of some retailers such as Ikea starting to look at this market. I don't believe they'll be ready for five or 10 years to come to this city.

ZINKAN: Underneath all retail is new household formation and job creation, which

supports the ability of folks to purchase homes, and, unfortunately, I think there's a struggle with that. If there is no new rooftop formation, we are not going to have new center development.

SUTTON: Gurus call this the jobless recovery. If you don't have existing homes increasing incomes or new homes to add to incomes, I don't know how people afford the Ikeas of the world. Those folks know how to research markets. They look very hard. I hope there are some new names, but maybe not for a year or so yet. We are still recovering from a really, really tough economy.

EPSTEIN: In the next 12 to 16 months you will see some new restaurant concepts in town. The Clay Terrace project is going to bring four or five new names to the market that we don't currently have. I am working personally on three or four new concepts to bring downtown. We're trying to bring things that aren't a rehash of another steakhouse or another Italian place. They are out there. It is just a matter of convincing them about the viability of downtown and the Indianapolis market.

IBJ: Do you think that we will start to see other kinds of retail development downtown, not just in restaurants?

PERLSTEIN: You will continue to see retail development along the Massachusetts Avenue corridor. We have had a project there that we have been working on. We have created a wonderful mix with Elements, Starbucks, Silver in the City, Three Dog Bakery, Splurge--a woman's apparel store--and now we are working with a gourmet food store to round out the tenant mix there. You are going to continue to see growth in the Fountain Square area. You are going to continue to also see growth near the IUPUI campus with what is happening with Clarian and its expansion.

There is going to have to be additional retail to support that area, as well as continued redevelopment within the heart of the central business corridor downtown. Not to mention, everyone is waiting to see what happens with Market Square. It is going to be very exciting to see who lands that project and the type of retail it will include.

EPSTEIN: It will be interesting to see what happens with Washington Street. That is kind of the one area that is sitting idle, and I think something will happen in the next year or so once the Market Square project is announced.

IBJ: Other than downtown, where are some hot spots for retail development?

EPSTEIN: Michigan Road and the northwest quadrant seem to be pretty hot. Rick has got a great project there, Duke has got a great project there, Kite has two sites in the area.

SUTTON: And we are all chasing the same people. There is enough critical mass there that we will all do well I think. Avon, Plainfield and Brownsburg continue to just expand beyond anyone's predictions.

PERLSTEIN: I think you will see some interesting things happen on the east side of town. I think Simon has been quietly working to retrofit [Washington Square] mall, which over the past years has had some significant vacancy problems. The Pendleton Pike corridor is quite incredible. Another area is going to be up at 146th and Hazel Dell Road. Hazel Dell Crossing is going to have 300,000 feet of retail that Skinner and Broadbent [Co.] is working on. I think that in itself is going to be a phenomenal development over the next three to five years. The Trader's Pointe project that Kite is doing is going to be very exciting. It wouldn't surprise me if they come out of the ground next fall 100 percent leased.

IBJ: You mentioned the east side. The city has announced tax abatements for some of the empty big boxes on the east side. Will that have an impact as far as trying to get retailers in there?

ZINKAN: I don't think a lot of people realize that Washington Street, unlike other major arterials, is one of the few routes--short of I-70--to get from here to Greenfield, which is vibrant. In the afternoons, you are looking at 40,000 to 60,000 cars. It is almost gridlocked. Unfortunately, I think what you are talking about are those economically obsolete large structures for which there is a limited demand. I don't think they are going to exist as they are currently configured today. I think the demand is there in terms of the passing traffic. How you capture that traffic is the \$64,000 question.

IBJ: On the other side of town, a slightly different program with the same aims was announced for the Lafayette Square area. That program, instead of giving tax abatements, would give money to someone interested in developing or redeveloping the site. What are the prospects there?

EPSTEIN: The west side is more of a challenge than the east. Like the east side, there is a lot of traffic going by those sites, but you have newer developments further west, in Plainfield and Avon and Brownsburg, that are pulling away those customers. You don't necessarily have that on the east side.

SUTTON: I can track almost 700,000 square feet of vacant big-box space in the Lafayette Square submarket that has been vacant three to four years or longer. That is not a trend, that's an existing fact. The city is trying, but spread over that whole submarket, that is not enough money. Until Simon [Property Group Inc.] decides how they are going to revitalize the mall, everything sort of spills out from that.

ZINKAN: The differences between Lafayette Square and East Washington Street are you have a substantially different traffic pattern. I have different routes and more means for accessing the west side than I do the east side. Secondly, if I am living in Avon, do I want to go to 38th and Lafayette Road on a Saturday night to see a movie or to eat dinner? Or do I want to stay out in my neck of the woods? Whatever economic

incentives you offer, it is structurally and fundamentally different in terms of demand.

IBJ: What are your predictions for the retail sector in 2004?

PERLSTEIN: Plainfield, Clay Terrace, Fashion Mall, Washington Square Mall and Trader's Pointe are going to be the highlights for retail development. You will see continual expansion of restaurants and banks. Bank expansion is beyond belief in this market right now. It will continue to be that way for several years to come. You will continue to see the repositioning of the drugstores. Although that has slowed down a bit, anywhere where there is a drugstore that is not meeting the requirements of what they need today, or not allowing them to have the drivethrough capabilities, they are going to do everything they can to reposition. Osco is not active--it is going to be CVS and Walgreen's fighting that battle. Lastly, you will continue to see co-branding of retail concepts, whether they are in grocery stores, Meijer, Costco, or even restaurants themselves such as KFC and A&W.

EPSTEIN: In the coming year, I see downtown being a big area of change with the Market Square project. Clay Terrace is going to be a great project for Indianapolis. It will be interesting to see how that does, and I think it will do well. I think the mix that they are going to have there will bring shoppers from a long distance, and their trade area is going to be substantially larger than most of the other malls in our market.

ZINKAN: We've had 13,000 to 15,000 new residential building permits each for the last few years. So long as we have cheap interest rates and we have jobs that can support the mortgages, you have new neighborhood retail, and I think the challenge will be the existing redevelopment.

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