

RETAIL INDEX

ANNOUNCING NEW DISCOUNTS

Total returns for the retail sector slipped into negative territory in fourth quarter 2018, weighed down by -1.60% appreciation return for the sector, as cautious sentiment for retail and negative headlines for department store anchors continued unabated. Countering conventional wisdom, in-store retail sales grew at a healthy rate, helped along by fiscal stimulus, rising 5.7% year-over-year over third quarter 2018. But with e-commerce sales increasing 11.0% year-on-year over the same period, two factors - the shifting channels for sales and the mismatch between America's retail footprint and today's retail demand - are driving sharp differentiation in performance at retail properties. In aggregate the appreciation indices for regional and super-regional shopping mall subtypes were marked down by -2.47% and -2.52%, respectively, in the fourth quarter, the steepest declines among retail subtypes. However, this masks the widening spread in both cap rates and NOI growth between high-productivity and low-productivity malls. Meanwhile neighborhood center appreciation declined to -0.23%, while single-tenant retail was the only retail subtype to avoid value markdowns in the fourth quarter, at 0.22% appreciation. The sector's quarterly total return of -0.43% was retail's first negative quarterly return since the end of the GFC in fourth quarter 2009, and marks the first quarter for any NPI sector with a negative return since the cycle began.

Vacancy at NPI-owned retail properties actually improved over the year to fourth quarter 2018 and ended the year at 6.92%, twenty basis points below the sector's five-year average. NOI growth of 2.18% in fourth quarter 2018 also improved from its year-ago mark, although in-store sales growth is increasingly challenging for owners to translate into higher rents. Given the converse strength of the industrial sector, where NOI growth hit 9.61% in the fourth quarter, the retail sector's current cap rates increased to 5.27%, wider than the industrial sector for the third consecutive quarter.

Amid the headwinds, retail properties selling out of the NCREIF Property Index dropped to a multi-year low in 2018, with 39 properties trading out of the index, half of the five-year average and apart from the GFC in 2008 and 2009, the lowest pace for retail properties sold out of the NPI in 20 years. The aggregate outbound sales volume of \$1.2 billion over 2018 also declined from an average of \$3.3 billion over 2014 through 2017, a fall that is unique to the retail sector and reflects its challenges and weak investor sentiment.

Retail owners are responding by reinvesting capital where warranted, to reinvent their properties for an era with greater demand for vibrant mixed-use retail assets. Among the 62 super-regional malls within the NPI, totaling 60 million square feet, capital expenditure per square foot has increased from roughly \$8.50 in 2014 to nearly \$14 in 2018, led by tenant improvements and building improvements and expansions. Equating to more than 30% of NOI, these increasing capex projects demonstrate the race to orient malls towards a modern, multi-use and omnichannel-focused retail business model.

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RETAIL TOTAL RETURNS

	Total NPI	Total Retail	East	Midwest	South	West
4th Q 2018	1.37	-0.43	-0.71	-1.49	-0.73	0.15
3rd Q 2018	1.67	0.56	0.28	-0.22	0.63	0.90
One Year	6.72	2.18	0.42	0.18	1.84	4.03
Three Years	7.21	5.59	4.28	4.06	5.94	6.67
Five Years	9.33	8.95	7.78	7.61	9.69	9.66
Ten Years	7.49	8.24	7.48	7.24	8.81	8.69
Twenty Years	8.98	10.01	9.64	8.64	9.88	10.91

RETAIL INCOME RETURNS

	Total NPI	Total Retail	East	Midwest	South	West
4th Q 2018	1.11	1.16	1.20	1.13	1.20	1.12
3rd Q 2018	1.11	1.13	1.18	1.13	1.17	1.07
One Year	4.56	4.66	4.77	4.66	4.82	4.49
Three Years	4.67	4.74	4.83	4.79	4.82	4.60
Five Years	4.88	4.99	5.07	5.09	5.10	4.83
Ten Years	5.48	5.73	5.75	5.90	5.87	5.54
Twenty Years	6.39	6.62	6.66	6.73	6.68	6.52

RETAIL APPRECIATION RETURNS

	Total NPI	Total Retail	East	Midwest	South	West
4th Q 2018	0.26	-1.60	-1.91	-2.62	-1.94	-0.97
3rd Q 2018	0.56	-0.57	-0.90	-1.35	-0.54	-0.18
One Year	2.08	-2.40	-4.20	-4.33	-2.88	-0.44
Three Years	2.46	0.83	-0.54	-0.71	1.09	2.01
Five Years	4.30	3.82	2.61	2.43	4.43	4.66
Ten Years	1.92	2.41	1.67	1.29	2.81	3.03
Twenty Years	2.47	3.23	2.85	1.83	3.05	4.19

RETAIL INDEX—QUARTILE RANGE OF RETURNS

