MARKET REPORT

Marcus & Millichap

RETAIL

Chicago Metro Area

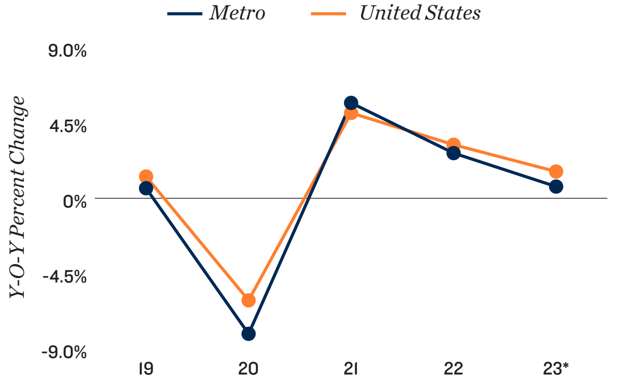
2Q/23

Floor Plan Needs Alter Retail Landscape, While Big-Box Challenges Weigh on Multi-Tenant Performance

Loop-adjacent markets benefit from shift in retailer preferences. In an attempt to capture more foot traffic, area retailers are adapting to omni-channel business models, vacating larger stores in favor of smaller floor plans in affluent suburban neighborhoods. Abercrombie & Fitch and Bloomingdale's are recent brands to adapt this model locally, introducing boutique-sized stores in Loop-adjacent neighborhoods. While this trend will adversely impact fundamentals in areas of store closings, the shift will aid retail performance in submarkets like Lincoln Park, Lincoln Square, Logan Square and the Gold Coast. Each entered the second quarter with vacancy rates well below their pre-pandemic benchmarks, and helped metrowide absorption exceed completions for the third consecutive year in 2023.

Market positioned to withstand near-term, big-box closures. Economic headwinds, such as supply chain challenges during a historic inflationary period, are prompting some large retailers to close local operations this year. Notable exits by Walmart and Bed Bath & Beyond headline these big-box exits. Predominantly located within shopping centers, these closures will reduce near-term multi-tenant absorption; although, consistent tenant demand should help backfill some newly-vacated space. Since 2017, the segment's vacancy rate has held between 7 and 8 percent every year, aside from 2019 when multi-tenant availability dipped to 6.2 percent. Steinhafels, a regional furniture store, recently leased a former Bed Bath & Beyond in Vernon Hills, exemplifying existing demand for these large spaces.

Employment Trends



* Forecast

Sources: BLS; CoStar Group, Inc.

Retail 2023 Outlook

35,000 JOBS *will be created*

EMPLOYMENT:

Staff additions this year will be enough to outpace the rate from 2019. Still, a notable pullback in the pace of hiring persists through the remainder of 2023 as total employment growth drops below 1 percent.

750,000 SQ. FT. *will be completed*

CONSTRUCTION:

Developers add less than 1 million square feet of inventory for the first time since at least 2007. This year, completions are predominantly single-tenant spaces and are well-distributed across the metro.

10 BASIS POINT *decrease in vacancy*

VACANCY:

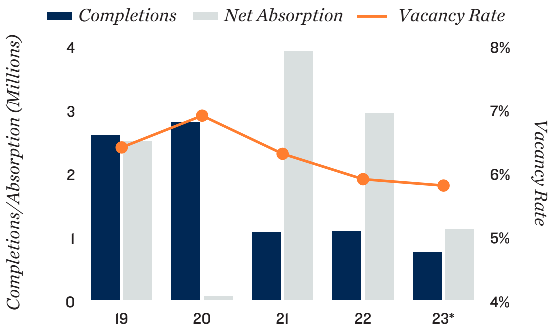
Following the 20-basis-point cut over the first three months of the year, Chicago's vacancy rate will lift to 5.8 percent by December. Still, this will mark the metro's third consecutive year of vacancy compression.

3.0% INCREASE *in asking rent*

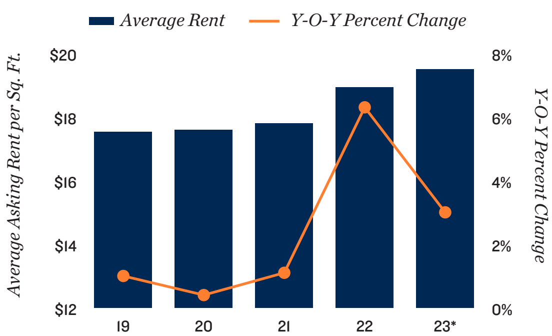
RENT:

The metro's lowest year-end vacancy on record will support a historically above-average rate of rent growth, bringing Chicago's mean rate to $19.50 per square foot by year-end.

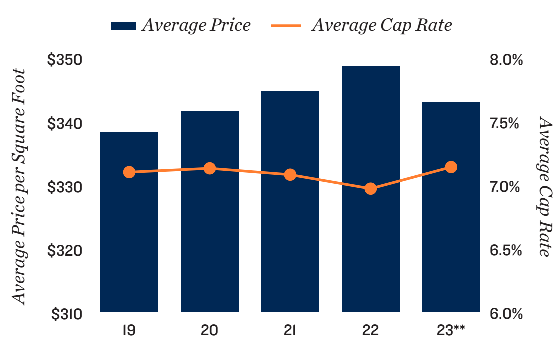
Supply and Demand



Rent Trends



Sales Trends



** Forecast ** Through 1Q*

Sources: CoStar Group, Inc.; Real Capital Analytics

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Price: $250

1Q 2023 - 12-Month Period

CONSTRUCTION

1,015,000 sq. ft. completed

- Developers added less than 100,000 square feet of retail space during the first three months of 2023. This was the smallest quarterly delivery slate on record and resulted in an annual inventory growth rate of 0.2 percent.
- Supply additions near Oak Brook and Naperville accounted for 20 percent of deliveries over the recent yearlong period ending in March.

VACANCY

60 basis point decrease in vacancy Y-O-Y

- Vacancy compression over the prior four quarters resulted in the rate reducing to 5.7 percent in March, Chicago's lowest mark since at least 2007.
- The single-tenant segment recorded net absorption of more than 3.5 million square feet over the 12-month period ending in March, bringing the retail subtype's vacancy rate to 5.3 percent entering the second quarter.

RENT

5.9% increase in the average asking rent Y-O-Y

- Historically tight vacancy raised tenant competition for available space, boosting Chicago's average asking rate to $19.50 per square foot in March.
- A number of sizable multi-tenant exits in desirable downtown locations, commanding above-market-average rents, add to the segment's available space and helped raise its mean marketed rate 13.3 percent.

Investment Highlights

- Transaction velocity dropped nearly 50 percent over the first three months of 2023, compared to the prior two-year quarterly average. Notable hikes in the Federal Reserve's lending rate, combined with mounting economic pressures, contributed to this notable decline in local activity. The Fed's tapering pace of rate hikes, along with improved local retail asset performance, may raise trading velocity in the latter half of 2023.
- Despite deal flow reaching a decade-long low in early 2023, investors are still finding opportunities in well-performing areas. Logan Square and surrounding northwest portions of Chicago proper recorded a large amount of trade volume in the opening months of 2023 amid local vacancies under their 2019 figures. Elsewhere, strong leasing trends and rent growth in the Oak Brook and Naperville areas helped the submarket account for more than 20 percent of metro deal flow in the first quarter.
- GIC's acquisition of STORE Capital and its significant Chicago portfolio in the first quarter reflects long-term institutional confidence that may carry over into the private investor pool, given strong local fundamentals.