SPECIAL REPORT

Marcus & Millichap

FOREVER 21 BANKRUPTCY

OCTOBER 2019

Retail Redesign Still a Work in Progress as Former Fast-Fashion Leader Files for Bankruptcy

Some retailers still acclimating to modern consumers. The retail sector's transformation continues to leave behind companies that fail to adapt, including Forever 21. Overexpansion, a high-inventory business model and slowed mall traffic overwhelmed the fast-fashion heavyweight, leading to a recent filing for Chapter 11 bankruptcy and the announcement of 178 store closings — about a third of its U.S. brick-and-mortar portfolio. These closings could help the retailer recalibrate its operations to a more modern retail concept, striking a balance between physical and online footprints. Though Forever 21's undoing was widely anticipated by many mall and shopping center owners, it does place additional pressure on landlords already battling defunct storefronts. Backfilling these soon-to-be empty retail locations with more sustainable tenants will be key for owners moving forward, especially with risks of a softening economic outlook rising. Tenant mixes have become more crucial amid the evolving retail sector, increasingly impacting investment appeal and underwriting feasibility.

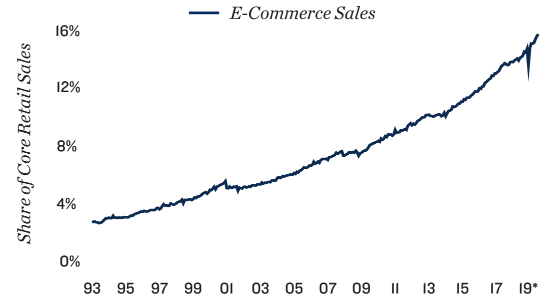
Retail reinvention continues to provide investors with new opportunities. Forever 21's closures will affect a wide range of investors as its locations can be found in regional malls and shopping centers. While the company's average store size is 38,000 square feet, some locations cover more than 100,000 square feet, potentially creating a more challenging task of backfilling the unused space. Retail owners faced with retenanting defunct Sears and Toys R Us stores have become creative when finding new occupants, adding entertainment-oriented retailers, dividing the space into multiple blocks or converting the space use to office or industrial depending on the dynamics of the property. Those attempting to retenant Forever 21 stores may mimic some of these concepts, exploring ideas that will boost the long-term viability of their assets.

Markets With Largest Forever 21 Footprints

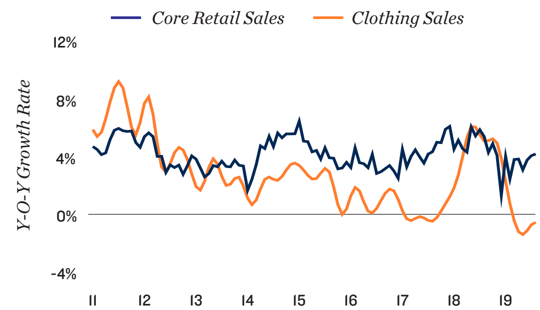
Metro	Estimated Total Square Footage	Store Closings
Los Angeles	454,000	16
New York City	398,000	16
Washington, D.C.	234,000	7
San Francisco	179,000	5
Chicago	148,000	7
Philadelphia	117,000	5
Seattle-Tacoma	115,000	5
Dallas/Fort Worth	98,000	4
U.S. Total	**6,764,000***	**178**

** Based on the 178 planned closures in the U.S. at an average store size of 38,000 square feet*

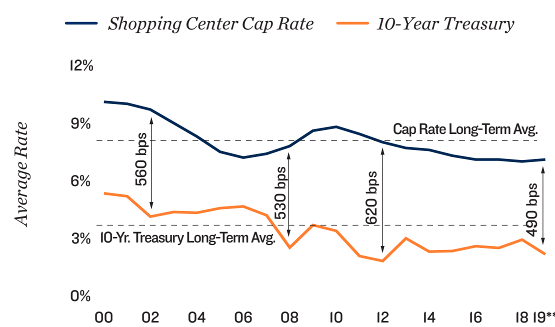
Online Shopping Continues to Grow Yet Remains Small Part of Total Spending



Clothing Sales Falling Behind Overall Growth



Shopping Center Cap Rate Trends



** Through August*
*** Through 2Q*
Core retail sales exclude auto and gasoline sales.
Sources: Marcus & Millichap Research Services; CoStar Group, Inc.; Real Capital Analytics; U.S. Census Bureau

Few Retailers to Blame for Store Closures; Omnichannel Concept Expanding as Retailers Become More Dynamic

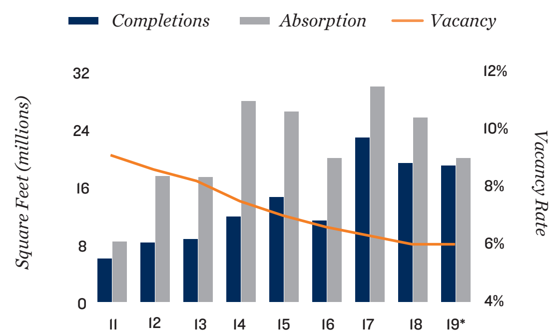
Growing pains to benefit retail sector's long-term outlook. With store closings on track to hit a record high and surpass 12,000 locations in 2019, the common perception of physical retail remains clouded despite the sector boasting some of its healthiest performance metrics in more than a decade. The majority of closures stem from just a handful of retailers who failed to adapt with the changing landscape. Of the nearly 8,600 stores that have closed in 2019, roughly 70 percent of them can be traced to 10 retailers, most notably Payless ShoeSource, Gymboree, Dressbarn and Fred's. Several relatively stable retailers like Family Dollar and Walgreens also closed some doors; however, these closures were a product of business model optimization rather than weak firmwide financial metrics. Though the wave of store closings suggests the sector remains in a transformative stage, the outlook continues to improve as retailers explore ways to keep stride with evolving consumers.

Retailers find common ground amid sector evolution. The ominchannel retail concept continues to gain prominence as physical retailers develop stronger online capabilities and digitally native companies set up brick-and-mortar stores. Retail has evolved past the idea that either in-store or online will survive, ultimately strengthening the sector as retailers build more sustainable business models. Sector heavyweights including Target and Walmart have effectively adopted the omnichannel concept by adding robust digital infrastructure to supplement their large physical footprints. In contrast, internet brands like Bonobos, UNTUCKit and Warby Parker are building out their physical framework through aggressive expansion plans, while tech powerhouses Amazon, Apple and Microsoft continue to bolster store counts as well. In-store pickup and home delivery services have been popularized by the blending of physical and online retail, offering consumers a variety of shopping channels.

Evolving consumers prompt retailers to realign strategies. While performance by retailer has varied over the past several years, many companies have come to realize they're overstored. The rise of e-commerce and shift to a more digitally driven environment is prompting many retailers to rethink their selling platforms. Companies are reevaluating their brick-and-mortar portfolios, shuttering excess locations that weigh on the bottom line. This has supported trimmed employee counts while retaining the most productive workers to streamline operations and boost the companies' overall efficiency. Despite these cuts, retailers still recognize the imminent need for physical retail as brick-and-mortar locations can build trust and engagement with customers, offering them a place to test new products, ask questions and return merchandise purchased online. When a retailer opens a physical store within a market, web traffic increases by an average of 37 percent in that area, reemphasizing the value of real world engagement.

2018 Net Store Growth

Shopping Center Supply and Demand



* Completions and absorption trailing 12 months through 2Q; vacancy 2Q

National Retail Group

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Sources: Marcus & Millichap Research Services; BDO; Coresight Research; CoStar Group, Inc.; Creditntell; ICSC; Moody's Analytics; Real Capital Analytics; U.S. Census Bureau