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Investor Appetite for Retail Real Estate Is Heating Up Again

Institutional buyers are snapping up grocery stores, pharmacies and other recession-resilient stores

By *Kate King* Follow

Dec. 19, 2023 9:00 am ET

Institutional buyers are still approaching retail with caution, sticking to safe assets and largely avoiding enclosed malls. PHOTO: AARONP/BAUER-GRIFFIN/GC IMAGES/GETTY IMAGES

Big investment firms that have shunned retail real estate for years are giving the sector a fresh look, the latest sign that this long beleaguered property type is on the mend.

Institutional buyers are snapping up grocery stores, pharmacies and other recession-resilient stores. Retail's strong performance in recent years has also increased the sector's appeal as remote work depresses demand for office buildings.

"We think there's going to be probably a lot more money that's going to look at retail," said Steve Plenge, chief executive of Pacific Retail Capital Partners, which buys, develops and manages retail properties.

Private-equity funds, in particular, are showing more interest as industrial and multifamily real estate has gotten more expensive, Plenge said.

Overall commercial-property sales, including retail, have slowed significantly since the Federal Reserve began increasing rates last year. And family offices, wealthy individuals and small private-investment firms are still dominating acquisitions, with these private investors snapping up $1 billion more retail assets than they sold in the third quarter, according to data firm MSCI Real Assets.

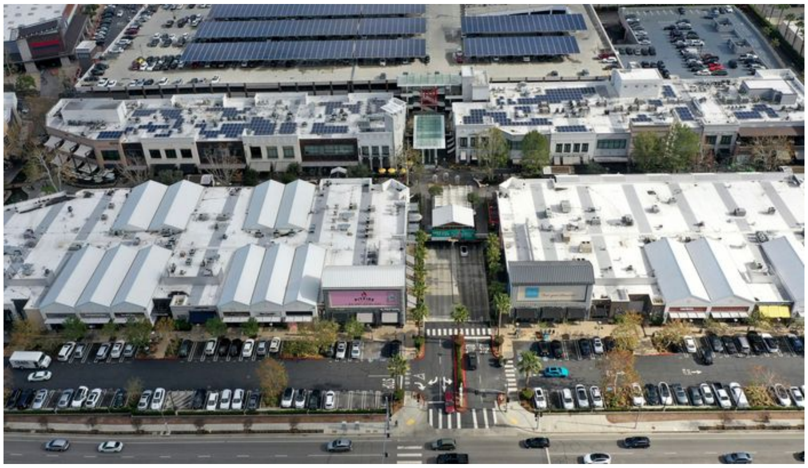
"The institutional buyers were a bit gun-shy about retail for a while," said Jim Costello, chief economist for MSCI Real Assets, adding that the declining value of many enclosed malls soured many bigger investors on retail entirely. "It got painted with a broad brush."

Institutional investors and real-estate investment trusts, or REITs, are still net sellers of retail, although the pace of dispositions has slowed over the past year. Retail owners and analysts said they expect to see more institutional capital flowing to the sector in 2024, especially amid expectations that the Fed will begin lowering rates next year.

New York-based investment-management firm Blue Owl Capital ranks as the biggest institutional buyer of retail so far in 2023, according to MSCI Real Assets. The firm has acquired between $1.5 billion and $2.3 billion in retail properties annually since 2020.

Blue Owl largely buys retail it considers resilient to both online shopping and economic downturns, such as free-standing grocery stores, pharmacies, gas stations, convenience stores and auto-part retailers, said Marc Zahr, who heads the firm's real-estate platform.

"We think those types of retail assets generally hold up well and there's multiple buyers that are interested in those assets regardless of the market environment," he said.



Shoppers have flocked back to bricks-and-mortar stores since the pandemic, easing fears that e-commerce would eclipse in-person purchases. PHOTO: DEAN MUSGROVE/ASSOCIATED PRESS

Chicago-based private-equity firm Temerity Strategic Partners, or TSP, has also jumped in. It partnered this month with private retail real-estate company DLC to fund up to $2 billion in retail acquisitions over the next three years.

Multifamily and industrial prices are so high right now that buyers need to raise rent before they can start profiting from their purchases. But "you can buy open-air retail today with an immediate return on your purchase price in excess of your cost of debt," said TSP CEO Bruce Cohen.

Cohen, who has been investing in commercial real estate for three decades, co-founded TSP in 2022 with partner Jeff Citrin and spent the last year meeting with more than 300 real-estate operators across the country as they considered where to invest.

"We were a bit surprised to discover how strong we found retail's fundamentals," he said.

Shoppers have flocked back to bricks-and-mortar stores since the pandemic, easing fears that e-commerce would eclipse in-person purchases.

Retailers, meanwhile, weathered the upheaval of 2020 with relatively few bankruptcies as consumer spending remained resilient. Stores vacated by companies that did go under, notably Bed Bath & Beyond, have been quickly snapped up by new tenants.

Perhaps most important, very little new retail has been built over the last dozen years, which has helped keep vacancy low while pushing up rent prices.

High construction costs and interest rates will likely discourage new retail development for the foreseeable future, said Adam Ifshin, CEO of DLC, which recently bought four open-air shopping centers in Colorado, New Jersey, Arizona and Ohio for a total $100 million.

REITs have been growing through mergers this year. Kimco Realty said in August that it would acquire fellow open-air shopping center owner RPT Realty. That same month, retail landlord Regency Centers completed an acquisition of Urstadt Biddle Properties in an all-stock transaction.

Institutional buyers are still approaching retail with caution, sticking to safe assets and largely avoiding enclosed malls. Kairos Investment Management CEO Carl Chang, who owns primarily grocery-anchored and convenience retail, has been impressed by the strength of dine-in restaurants since the pandemic. But he believes a correction is coming next year if the economy falters.

“I think we’ll finally begin to see the higher interest-rate environment slow down consumer spending,” Chang said.