GLOBAL SHOPPING CENTER INDUSTRY UPDATE
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Thank you very much.

I'm happy to be able to say that the economic recovery, if a consensus view of economists is to be believed, is now turning into a durable one and will deliver the U.S. 3%-plus growth in GDP for the next few years.

And although it may sometimes appear fitful and uneven, the recovery in our own industry is improving in step with that of the broader economy.

The unemployment rate nationwide has been falling in recent months and was back down to 9.0% in January, still very high but well off the 10 percent-plus peak of late 2009.

Job growth has been picking up at the same time and a little over 400,000 jobs have been created in the economy since October. It's not much but at least it's a start.

Although there are good signs in the economy, the pace of the recovery is frustratingly slow for many in our industry. Consumers have had enough of frugality and are starting to spend again but many are still very financially constrained and value-oriented.

This is prolonging a period of fierce competition among retailers at the lower- and middle-ends of the market, particularly in sectors like groceries and discount general merchandise. Pricing power is limited in these sectors. Where wholesale costs have increased retailers have had a difficult time passing these costs on to consumers. Where wholesale product costs are falling, the retailer must immediately reinvest the decline in lower prices to remain competitive.

Having said that, the recovery in the upscale sector that my company serves has been outstanding, with the affluent customer having now returned and the aspirational consumer on the way back.

According to the latest Census Bureau data, non-auto retail sales increased by 5.4% in January of this year compared with January a year ago. That followed 5.8% growth for 2010 as a whole, much of which was back-loaded into the latter part of the year.

Growth in 2010 was a huge improvement over the 5.2% sales decline of 2009.

In malls, the latest issue of the ICSC U.S. Mall Performance report showed that for 2010 mall sales per square foot nationwide were up 5.6% over 2009. Average productivity across the mall industry is now almost back to 2008 levels.

Particularly noteworthy has been the performance in malls of the home entertainment and electronics category which reached sales per square foot of $1,144 last year, representing a growth rate of 36% over 2009. This is rather startling testimony to the emergence of digital products not just as a dominant functional item in the household but also an important fashion item among the nation's consumers.

However, traditional fashion in the sense of clothing and accessories, jewelry and personal care are also recovering.

Mall apparel sales per square foot increased 3.3% in 2010 according to ICSC.

Women's accessories and specialties, women's shoes, men's apparel and athletic shoes enjoyed the strongest productivity gains.

Women's ready-to-wear and family apparel are still experiencing only modest growth.

While overall fundamentals in the discretionary sector in which malls operate continue to improve, things are tighter in the supermarket and discount businesses that anchor most of our small centers.

Supermarket sales increased by a mediocre 1.8% nationwide last year. Preliminary indications are that they had a better January but structurally this is becoming an incredibly competitive sector. Drug stores, dollar stores and other non-supermarket formats are now all in the food-selling business along with supercenters, warehouse clubs and other formats.

Looking ahead, a consensus forecast by the Philadelphia Federal Reserve drawing on 43 professional forecasters, including ICSC's Mike Niemira, is increasingly optimistic about the economy's prospects both this year and for the next several years. The Consensus forecast is for a growth rate of 3.2% this year and 3%+ growth for each year through 2014, which is well above the long-term benchmark of 2.5%.

However it is clear that this will not be a consumer-led recovery but consumer spending is expected nonetheless to grow strongly partly as a result of pent-up demand from the long recession.

State and local government budget cutbacks will be a constraint on growth, especially in state capitals. And if the federal deficit reaches $1.5 trillion this year as expected, interest rates may well be on the way up.

Elsewhere in the developed world, as in the U.S., growth has been measured rather than explosive.

In the Europe retail sales growth averaged 2.0% in 2010. Results there have been weighed down heavily by Ireland, Greece, Spain, Italy and Portugal, where fiscal strains and austerity measures have combined to create a stiff headwind for consumer spending.

However, the United Kingdom, France and Germany have experienced a fairly steady recovery.

In emerging markets the situation has been even more positive.

In South America, Brazil's consumers were on a tear last year with retail sales growing by 14.5% nominally and 10.9% in volume terms. This made 2010 the best year for growth in Brazil since 2001.

Like Brazil, Chile also has a dynamic retail industry with sales growth of more than 15% in 2010. Chile not only has a vibrant and resilient consumer culture that keeps sales ticking away at home, but also represents an important source of new retailers and development expertise for its neighbors in the region.

Meanwhile, in Asia, growth is also generally impressive. Mainland China and Hong Kong both achieved sales growth above 18% in 2010, Korea just under 10%, and Singapore almost 7%.

An exception is Japan, where things have begun to slide into negative growth again after some positive trends emerged in mid-year.

In an environment where growth is slow in the U.S., Europe and Japan, and rapid in emerging markets, the current general pattern of retailer store expansion across the globe is easy to understand.

If I could simplify this pattern to just four succinct points they would be:

First, retailers that are saturated in mature domestic markets with their traditional formats are turning to much more flexible and unconventional configurations to enable them to take advantage of the remaining untapped real estate opportunities at home.

Copy-and-pasting might still work in Windows but it won't anymore for retail formats. Wal-Mart, is a classic example. Saturated with its supercenter format in the U.S., it is experimenting with a variety of smaller options that will bring it closer to its customers wherever they happen to be.

Second, I would say that retailers in mature markets are looking to start up operations as quickly as is practical in emerging markets to take advantage of phenomenal growth of spending power, increasing local political support, and improving infrastructure in many overseas markets.

Retailers no longer battle so much against "psychic distance" as they once did. Many are undeterred by differences in culture, geography or market maturity.

Third, European and Japanese retail chains are beginning to take advantage of the vast untapped opportunity for them in the U.S., and vice versa.

And fourth, local chains that were in positions of competitive strength before the recession have been opportunistically expanding into space that their weaker peers have vacated. At the same time, smaller retailers that previously had limited access to prime shopping center space are now finding dream opportunities opening up for them in the best centers.

For us in the U.S. the net result of all this is that even when the recovery is in full flight we are still likely to be operating in a very different and in some ways more challenging environment than we were in the go-go days before the recession.

In fashion and home electronics, many of the dominant retail chains that formed the backbone of US shopping center tenancies for many years are going to be adding just a tiny fraction of the number of domestic stores that they opened in the past.

In some cases, such as the Gap chain, they will actually reduce their total U.S. retail space while expanding aggressively abroad.

Recent domestic store closings by Abercrombie & Fitch, while at the same time announcing the impending opening of flagship stores in Paris, Madrid, Dusseldorf, Brussels, Dublin and Singapore, suggest that they too are operating in the same manner.

In some respects this process of international store expansion is being made less risky by the internet. Retailers are using their websites as much for market research as they are for selling product. By interacting with overseas consumers on their e-commerce sites they can better understand these consumers and gather intelligence on geographic locations before investing in physical stores. Where the internet goes, stores inevitably follow.

However, expansion is not always through directly owned and operated stores. Credible franchisees and licensees who can competently manage fashion brands are now prominent in most emerging markets. Many U.S. and European retailers are now using local "brand managers," because they remain in control over their brand, image, and inventory while avoiding direct financial risk.

This works well for the retailers until they are ready to take on the financial responsibility and create the internal infrastructure to manage far flung divisions themselves.

I don't see this international expansion trend, with the UAE, Russia, Latin America and Asia being the primary beneficiaries, changing soon.

In effect, retailers are simply doing what stock market investors have long believed in and practiced – holding a diversified asset portfolio. By having store fleets in both developed and emerging markets retailers are reducing their dependency on a single region, allowing them to benefit from a strong upswing in one market understanding that it will shift back and forth over time.

As I mentioned earlier, retailers in the U.S. are working hard at adapting themselves to a more diverse range of real estate opportunities than they had a few years ago when they were in full expansion mode. Likewise, retailers expanding abroad are incubating formats that are better tailored to new international markets. They recognize that growth prospects in emerging markets particularly will depend upon their ability to break out of the one-size-fits-all mentality, and make their customary formats more adaptable to local conditions.

Levi’s and interestingly Hermes are even creating separate brands for the Chinese market. Levi’s, which is of the most recognized international brands itself, launched dENiZEN last summer with a big fashion show in Shanghai. They plan to make it available in China, Korea, and Singapore but not in the U.S. Levi’s expects to roll out 50 stores in Asia by the end of this year.

Department stores are also on the move. Upscale retailers such as Bloomingdale’s in the U.S. and Harvey Nichols in the U.K. are offering fresh alternatives to mall developers with scaled down concepts that appeal to a narrower customer profile and are perhaps more customized to local tastes. This enables them to operate into smaller spaces than the customary 100,000 to 200,000 square foot department store box.

Department stores are also experimenting in other ways including creating outlet divisions, or sub-leasing space in their boxes to fast fashion retailers as a way to draw younger customers.

For example, the Sears department store at South Coast Plaza in Orange County, California, one of the top-performing shopping centers in the U.S., is sub-leasing 43,000 square foot of its own space to Forever 21, making the latter effectively a shopping center co-anchor within the same store.

Thousands of miles away in Tokyo's Ginza district, the Matsuzakaya department store has also leased parts of its first five floors to Forever 21, totaling about 40,000 square foot. The gamble is that the Forever 21 will help to attract the 20- and 30-year olds that the department store itself now struggles to draw.

So not surprisingly the retail world continues to evolve as retailers attempt to maximize the value of their space.

But the health of the industry ultimately depends, of course, on an appropriate match between supply and demand. In the U.S. there are currently only a couple of fashion regional malls under construction and my company is developing one of them, so I am very aware of the current market conditions. Limiting new supply will give us the opportunity to fill some of the empty space that was left from the combination of the explosive growth in the construction of new retail space in the mid-2000's and the subsequent decline in the U.S. economy.

But hope springs eternal. I am already aware that companies are working on new projects to fill pockets of demand as markets continue to evolve. However I do not foresee substantial growth in new retail projects in the U.S. for a long time.

Fortunately, the very slender pipeline of new development has kept supply in check and helped avoid a glut of space that could have had disastrous consequences over the past couple of years.

According to Costar Realty Information retail openings amounted to less than 50 million square feet in 2010, which was a record low. We figure that new shopping center supply represented only about 0.5% of the existing inventory last year.

Very few large centers are in the pipeline and the number of new starts for grocery-anchored neighborhood centers will also remain subdued for reasons that I've already mentioned -- increasing out-of-center competition from big box retailers in the grocery business and also from non-traditional grocery retailers like drug stores and dollar stores.

Stronger demand from consumers and the lack of new supply means that the pick-up in leasing that we've observed for some months is translating into occupancy growth. This trend should continue and drive vacancy rates down for several years, since it will be some time before retail development once again delivers significant new supply to the marketplace.

Some one said, and it's been repeated often since, that you should never let a good recession go to waste. I think we in the shopping center industry have made the most of ours because the adversity has made us creative and innovative.

We are on a continuous learning curve to keep our properties in step with consumers. For example, we've learned that we needed to increase the number and quality of food retail experiences in our centers.

We are focusing more on merchandise and services that keep people entertained and connected.

We are delivering for our shoppers continuous improvements in the sense of place provided in our shopping environments.

Now we are being asked new questions, and face new challenges and opportunities, that we will have to meet effectively if we are to remain the number one distribution channel for goods and services.

A genuine technology revolution is occurring in the industry that goes beyond shoppers sitting at home using their computers to buy merchandise on the internet.

Retailers are now harnessing technologies to cut expenses improve operating efficiency and increase the number of touch-points they have with their customers.

This includes going after their customers more aggressively via mobile marketing programs, mobile commerce, social media, and even high-tech vending machines that can be moved around from location to location depending on where the traffic happens to be.

Technology is making the relationship between physical and virtual space more intricate and complicated and in some sense less transparent to the shopping center operator.

For example, mobile marketing programs enable the retailer to communicate with customers anytime, anywhere, to market to them on a personalized basis and to sell to them on their smart phones. This sounds like a threat to real estate.

But when backed by location-aware technologies of the type now being tested by Macy's, Best Buy and American Eagle Outfitters, the likely result will be to draw customers to physical stores more frequently and sell more out of these stores.

There is also a potential for shopping center operators to use the same location-aware technologies to help customers make more informed shopping decisions across the whole shopping center.

Many retailers are currently in the process of either planning or implementing systems to better integrate their online and physical real estate platforms. This gives the retailer better transparency into its inventory across both the store portfolio and the warehouses that service stores and online customers.

You may have heard of J.C. Penney's "findmore" kiosks in the home, women's, men's and footwear departments of some of its department stores. Customers use touch-screens to access the entire retailer inventory and arrange to have items shipped to a home address or to the store for pick-up, either at no charge. The customer pays then and there or prints out a bill that is added to in-store purchases when the customer pays at the checkout.

Retailers such as Wal-Mart here in the U.S. and Tesco and House of Fraser in the U.K. are experimenting with pick-up counters or drive-through pick-up windows in their stores so that consumers can order merchandise online and pick up at the store.

Integration of store and warehouse inventory systems means that merchandise ordered by a customer for store pick-up need not even necessarily be housed at the store itself, but can be shipped from the warehouse to the store on demand. This means the stores themselves need not be as large.

As the interaction between customer, physical space and virtual space melds together it will be a challenge for shopping center operators to stay on top of this to ensure first of all that they are getting value for all real estate-based sales, and secondly that they are harnessing the technology themselves to make shopping centers the first place consumers choose to shop.

If consumers are relying on digital devices to deliver their product information and make better shopping choices once they are at the shopping center, the center itself will have to wirelessly support this.

If retailers have drive-through windows, they may affect the way stores are configured and how they interface with the rest of the shopping center. These issues and others will all need to be thought through as technology evolves.

We in the industry need to be mindful that in this technology-driven world, a shopping center can no longer even rely as much on being a house full of great stores to be competitive. It becomes increasingly important to become more than that.

For a stable and prosperous future, we need to continue to elevate our centers from being need-based merchandise fulfillment resources into vibrant environments where people come to reconnect with the social aspects of the personalities, hang out with their friends and share experiences together while being entertained by the environment and the stores within it.

If we give them such an environment, a lot of their shopping will get done at the same time, no matter how many alternative channels are open to them.

Thank you very much.