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Luxury malls ride out changing US shopping habits

Anna Nicolaou in New York

Sometimes, Kevin does not see a single person for three hours straight.

So, when a customer walks into the Michael Kors store in the Westchester Mall, tucked in a wealthy suburb 30 miles north of New York City, the young sales worker dashes up excitedly to greet her.

The store has made more money than last year, he says, but the number of visitors to the mall has dropped since he began working there two years ago.

“There’s just a lot fewer people walking through,” Kevin says. “It’s quiet here, mostly Westchester housewives or private school girls who come after school, and it definitely feels less busy than a few years ago.”

The rise of online shopping, combined with a lacklustre US economy, has hit the great American mall hard. Once a staple of American culture in the 1980s and 1990s, retail foot traffic during the November-December holiday season halved from nearly 35bn in 2010 to 17.6bn in 2013, according to ShopperTrak.

But look behind the headline numbers, and it becomes clear that not all malls are equal. Since 2007, the asset value of luxury, or so-called “A+” malls like the Westchester, has nearly doubled. The values of lower-tier “C” and “D” malls were slightly negative, according to Green Street Advisors, a real estate consultancy.

This divergence explains US mall owner Simon Property’s hostile $22.4bn bid for Macerich, a smaller rival, last week.

Although it is just a quarter of Simon’s size in both enterprise value and rental income, Macerich has restructured itself around luxury malls by selling off underperforming property — and booking more than $1bn in pre-tax profit last year in the process.

Macerich said it made 85 per cent of its 2014 operating income from what it calls "super zip codes" — where the median household income hovers around $120,000 and more than two-thirds of adults have a university degree. This is up from 66 per cent three years earlier.

When we do well, we do really well

- Sales worker in Michael Kors store, Westchester Mall

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Simon's bid is a "battle to own the best, most high-end malls in the country", says David Auerbach, a Reit trader at Esposito Securities.

Macerich, which did not respond to requests for comment, has said it would review what it described as an "unsolicited, conditional" proposal from Simon, which is at a 30 per cent premium to Macerich's undisturbed share price.

The imperative of owning luxury properties is apparent at the Galleria, a "C" ranked mall less than a kilometre from the Westchester.

The dimly lit, gritty complex, anchored by Sears and Old Navy, stands in stark contrast to the carpeted, shiny corridors of its posh rival.

A square foot of retail space at the Galleria generates just $310 a year, compared with $1,085 at the Westchester Mall. Employees at American Eagle, Old Navy and Aéropostale say the mall is less busy than a year ago and shoppers seem to spend less money.

Across the US, "C" and "D" malls make up about a third of the some 1,100 malls by number, but only 5 per cent by value. In the next decade, some 15 per cent of US malls will fail or be converted to non-retail property, according to Green Street Advisors, most of which would be lower-tier malls.

Much of this divergence is due to rising US income inequality, which has "affected everything in malls", says Howard Davidowitz, chairman of Davidowitz & Associates, an investment bank.

Luxury and lower-tier malls are hurt by online shopping in different ways.

"Luxury malls are golden, but the question is, where does the middle class shop? Cheaper alternatives, Walmart, TJMaxx and online deals, they're off the mall," he says.

The Westchester, for example, is home to jewellery and accessories stores such as Tiffany, Louis Vuitton and Dooney & Bourke. People buying an expensive watch, for example, are more likely to want to visit the store and see the product, says Simeon Siegel, research director at Nomura.

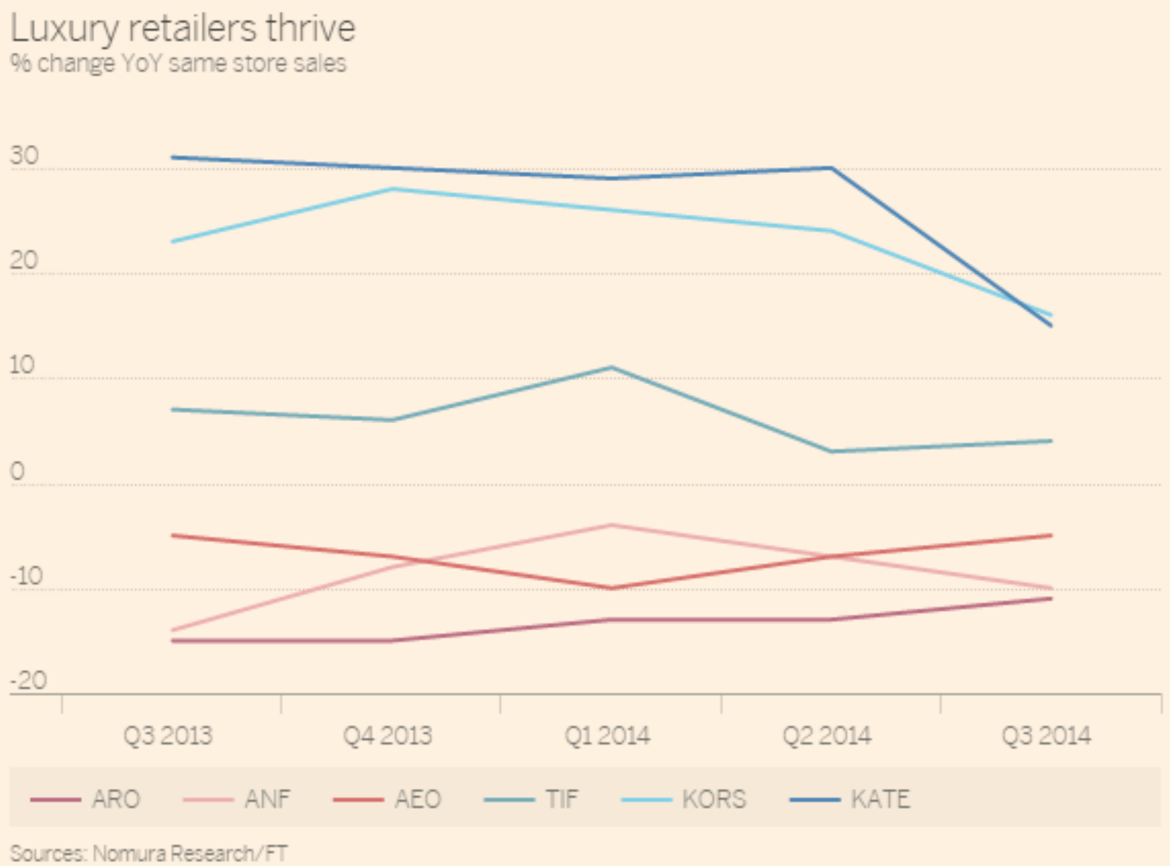
For the teen clothing brands at the Galleria such as Aéropostale and Old Navy, by contrast, there is much less reason not to shop online.

Wealthy Americans are also simply spending more as the economy recovers. Same-store sales at luxury brands — including Michael Kors — have grown by double digits in the past few years.

Abercrombie & Fitch's US same-store sales fell 10 per cent for the November through January period, while Aéropostale's dropped 9 per cent. Same-store sales at traditional "mall stores" such as Express and Ann Taylor have declined for three consecutive quarters.

For stores like Michael Kors, strong demand from the wealthy will probably shield it from the threat of ecommerce and drop in overall traffic, say analysts.

"I don't know why it is [that fewer people are visiting the mall]," Kevin says. "But don't get me wrong — when we do well, we do really well."



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