



# State of the Retail Sector: Challenges and Opportunities for San Francisco's Neighborhood Commercial Districts

# Introduction

## Concerns motivating the San Francisco study

- **How are national trends in the retail, restaurant, and personal services industries affecting businesses in San Francisco's Neighborhood Commercial Districts (NCDs)?**
- **What local challenges do San Francisco businesses face?** E.g., changing customer base, employee recruitment and retention, real estate conditions.
- **What characteristics do successful NCDs share?**
- **How might businesses and NCDs need to adapt to remain successful given national trends?**

Retail Apocalypse? The Sky Isn't Falling -- The Sector Is Just Evolving

 **Greg Maloney**, CONTRIBUTOR  
*I write on the confluence of shopping centers, economic development, and urban planning.*  
[FULL BIO](#)  
Opinions expressed by Forbes Contributors are their own.

### America's 'Retail Apocalypse' Is Really Just Beginning

By Matt Townsend, Jenny Sumane, Emma Orr and Christopher Cannon  
November 8, 2017

 **WIKIPEDIA**  
The Free Encyclopedia

Article talk Read Edit

### Retail apocalypse

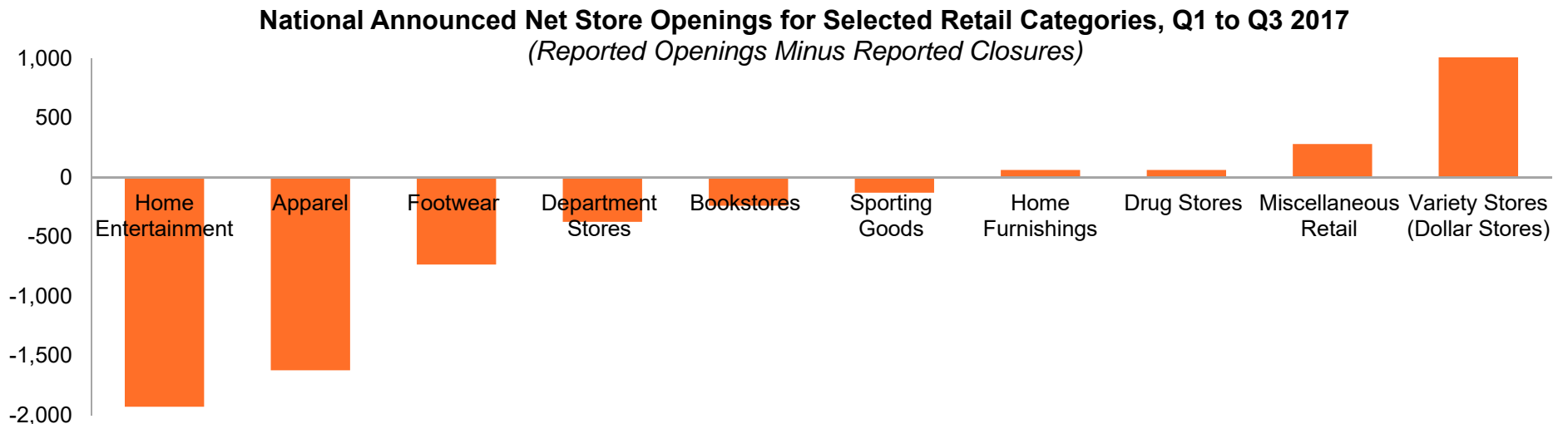
From Wikipedia, the free encyclopedia

The retail apocalypse refers to the closing of a large number of American retail stores beginning in 2016.<sup>[1]</sup> Over 4,000 physical stores are affected as American consumers shift their purchasing habits due to various factors, including the rise of e-commerce.<sup>[1]</sup>

# National Trends

## Expanding and contracting retailers

- **Major retailers are closing stores in record numbers**, reflecting a national oversupply of retail space, increased competition with online sales, and (for some retail chains) debt obligations associated with leveraged buyouts.



Note: Only categories for which data are available are shown. Different sources vary in reported numbers.  
Source: ICSC and PNC Real Estate, 2017, from Bloomberg's 2017 article, "America's Retail Apocalypse is Really Just Beginning"

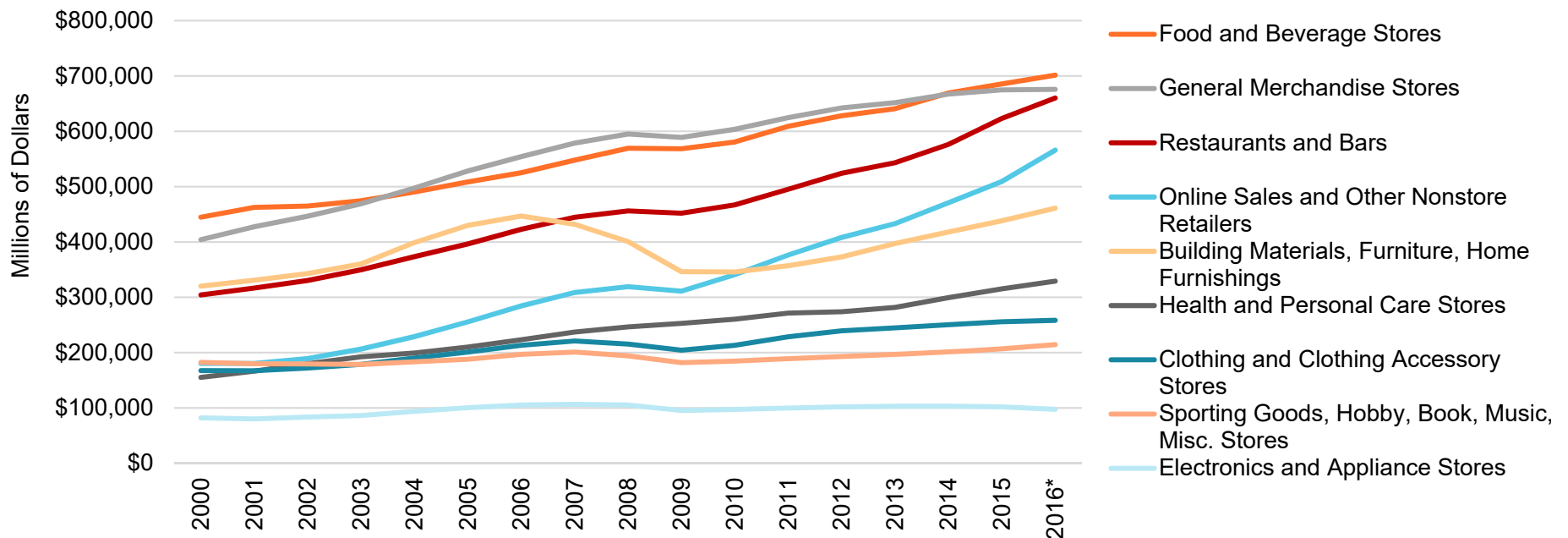
- **Discount stores are seeing continued growth, while luxury brands are struggling.** Discount retailers are adding stores, including discount clothing stores (TJ Maxx, Marshalls), discount grocery stores (Grocery Outlet, Trader Joes), warehouse and general merchandise stores (Costco, Target), and dollar stores.

# National Trends

## Restructuring of the national retail, restaurant, and personal services industries

- Nationally, growth in retail and restaurant sales is concentrated in a few categories** including online sales, food and beverage stores, restaurants and bars, building materials and home furnishings, and health and personal care stores.

**Estimated Annual Sales of U.S. Retail Firms by Type of Business: 2000-2016**  
(in Millions of Dollars, not Adjusted for Inflation)



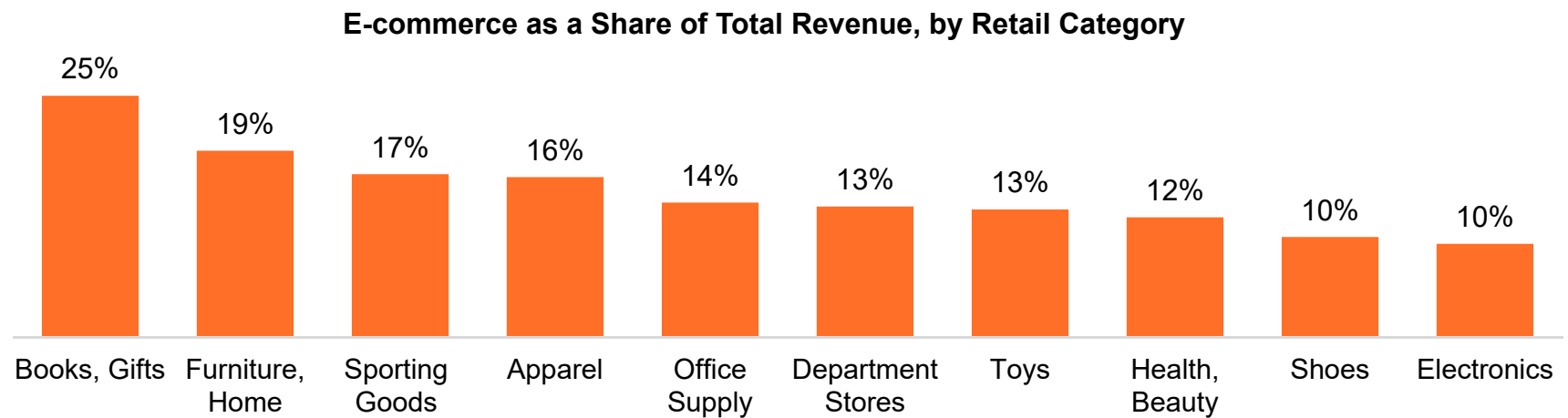
Based on monthly sales for 2016; annual 2016 estimates have not yet been released.

Sources: U.S. Census Bureau, 2015 Annual Retail Trade Survey (released March 6, 2017) and Annual Revision of Monthly Retail and Food Services: Sales and Inventories—January 1992 Through March 2017; Strategic Economics, 2017.

# National Trends

## Increasing influence of e-commerce

- **Online sales are driving retail growth, and expanding into new categories.** Nationally, non-store retailers accounted for 40 percent of retail sales growth between 2014 and 2016.
- **At the same time, technology is allowing retailers, restaurant owners, and service providers to integrate brick-and-mortar and online sales strategies.** Including online sales, app-based delivery services, and online reservation services.



# National Trends

## Employment & real estate impacts of e-commerce

- **E-commerce employment is growing, as overall retail employment remains flat.** In the last five years, national employment attributed directly to e-commerce has doubled – even without accounting for associated increases in warehousing and logistics jobs.
- **While there is a national oversupply of traditional retail space, demand for “last mile” distribution space is growing.** This includes warehouses located within close proximity to major population centers (e.g., five to seven miles), as well as lockers and other types of small-scale distribution and fulfillment facilities.



Source: Flickr Commercial Use Photographs; see footnotes for citation.



# National Trends

## Growing importance of offering an “experience”

- **Americans are increasingly spending their money on experiences – such as dining, personal services, and fitness – rather than objects.** Increased spending on food away from home, health and wellness, and travel.
- **Retail stores are experimenting with new strategies to capitalize on increasing demand for experiences.** For example, by serving food and drinks, offering classes or events, and expanding opportunities for customers to interact with products before purchasing.

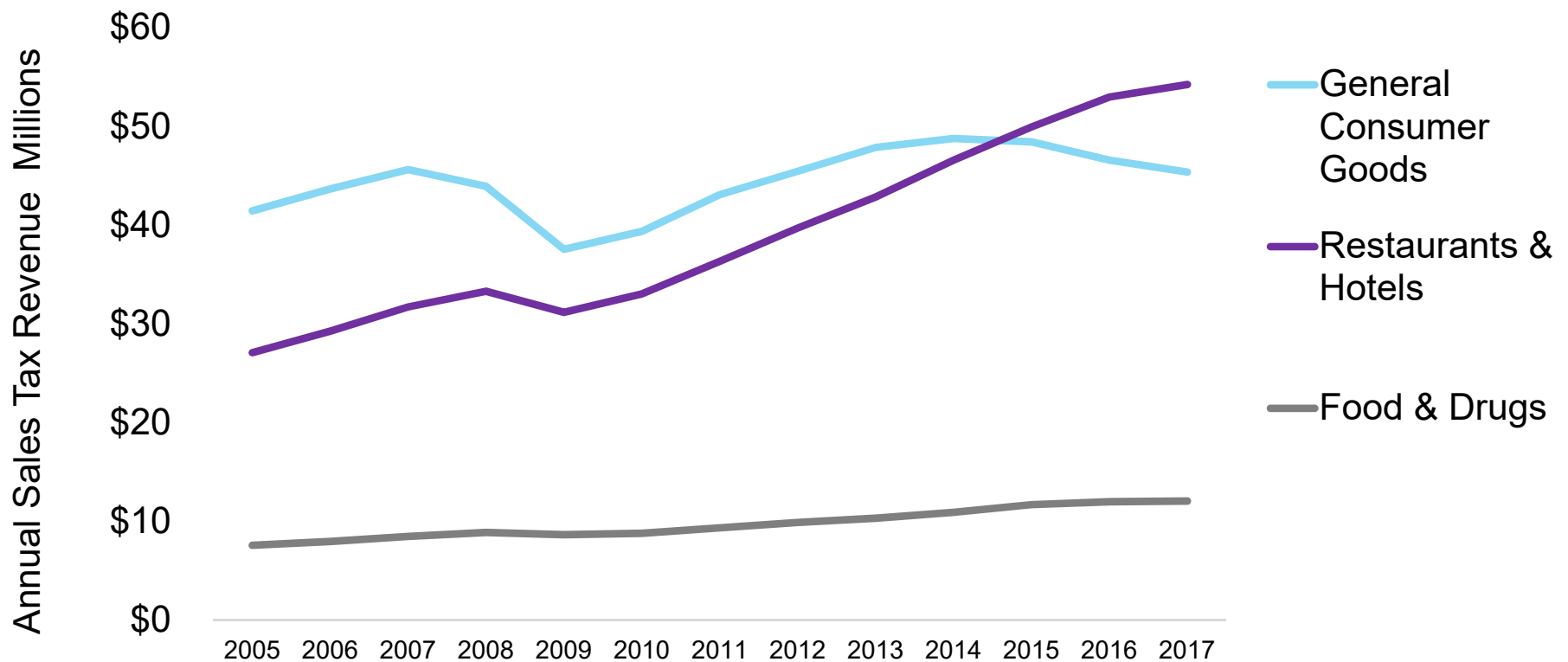


Source: Bird & Beckett, 2015 (left); San Franpsycho 9<sup>th</sup> Avenue, Yelp; 2017 (right)

# Impact of National Trends on San Francisco Retail

## San Francisco's retail is starting to feel the impact of these national challenges

### San Francisco Annual Retail Sales Tax Revenue by Category, 2005-2017



\*Note that because food for home consumption and prescription medications are not taxable, the taxable sales data shown here significantly underrepresent total (gross) sales at food and drug stores.

Sources: San Francisco Office of the Controller, 2018; Strategic Economics, 2018.



## Impact of National Trends on San Francisco Retail

### Demand for ground floor retail space in the NCDs appears to be slowing

- Real estate brokers report neighborhood retail **rents are plateauing**, after many years of growth.
- **Fewer traditional retailers are seeking space**, while there is increased interest from other potential tenants of ground floor commercial space (e.g., personal service, restaurants, medical services).
- Between 2015 and 2017, **a significant number** of the 24 NCDs for which OEWD survey vacancy data is available **experienced an increase in vacancy**. About one-third of these NCDs saw vacancies increase by at least 2%.

# Challenges for San Francisco Businesses

## High cost of doing business

- Employee recruitment and retention challenges
  - Low unemployment rates
  - High housing costs
  - Competition with other industries offering better compensation or more flexible hours.
- High labor costs
- High rents

## Land use regulations and permitting requirements

- The permitting process can add significant cost and time to the process of opening a new business.
- Some laws intended to protect traditional retail by limiting other uses may:
  - Limit retailer's flexibility to adapt to changing economic conditions.
  - Restrict complementary uses that could drive foot traffic to traditional retail.

# Challenges for San Francisco Businesses

## SF retailers face challenges adapting to a changing market

- Loss of long-time customer base due to demographic change.
- Increasing competition from other brick-and-mortar locations.
- Lack of technical expertise or financial resources to adopt new technologies, or invest in capital improvements or new inventory to appeal to a changing clientele.

## Businesses report public realm challenges

- Real and perceived issues around cleanliness, order, and safety, which may deter customers
- Long-term vacancies, which contribute to a sense of disinvestment

# Business Adaptations

## Rising costs and growing competition are prompting some businesses to adapt

- In response to national trends and local challenges, some businesses are adopting creative and varied strategies to survive. These strategies generally aim to:
  - Expand sales;
  - Reduce costs or pass costs on to customers; and/or
  - Diversify revenue streams.
- While adopting these types of strategies will help some businesses continue to thrive, change is challenging and some businesses will not be able to adapt to a changing market.
  - Policies and programs may support business owners by providing technical expertise or financial resources, but cannot force change on an unwilling business owner, or overcome fundamental challenges (e.g., lack of sufficient market demand for products or services).

## Successful Commercial Districts

### Retail businesses function as part of neighborhood commercial districts

- Most businesses rely on the spending power of households in the surrounding neighborhood (or trade area) to generate demand.
- Businesses also rely on each other, and on other uses in a district, to draw foot traffic.
- The quality of the pedestrian environment and of public spaces can help attract (or potentially drive away) potential customers.
- Cultural events, other special events, and public space programming can also help draw foot traffic.

# Successful Commercial Districts

## Key factors that contribute to successful commercial districts include:

- **Healthy business mix including:**
  - Anchors (or cluster of uses) that attract foot traffic
  - A diverse mix of retail and non-retail businesses, including restaurants, personal services, entertainment and nightlife
- **Appealing physical environment** including an attractive architectural character and street environment
- **Convenient, multi-modal access** including parking and curb space that is actively managed to balance the needs of different users.
- **Drivers of demand:** Local spending power, employment concentrations, medical/educational institutions, tourism.
- **High-capacity district management organizations** such as Community Benefit Districts, merchant associations, or Community Development Corporations.



# Conclusions

- 1. To thrive in a more challenging business environment, retailers need to embrace new technologies.**
- 2. Retailers need to be flexible and creative to provide customers with a more interesting experience.**
- 3. Diversifying the mix of uses in the NCDs can help retailers expand their customer base.**
- 4. By offering an attractive, fun shopping and dining experience, NCDs can help retailers continue to draw foot traffic.**