GlobeSt.com Commercial Real Estate News and Property Resource Print Now

NET LEASE FOCUS Last updated: April 23, 2009 12:02pm

Investors Still Have Appetite For Grocers

By Michelle Napoli

Grocery stores are among the more popular net lease retail investments these days. Sales of single-tenant grocery store properties were down 17% in 2008, according to the recent Single-Tenant Outlook retail report from the research services team of Marcus & Millichap Real Estate Investment Services Inc. While a decline, that figure is not nearly as steep as the overall decline in commercial real estate transactions last year, or in the broader net lease marketplace for that matter.

"Today the more popular net lease investment is the fast food category, and then I would say the grocery stores--depending on where they're located and their sales--are also appealing," says Edward B. Hanley, president of Irvine, CA-based Hanley Investment Group Real Estate Advisors.

Hanley recently represented both the seller, developer MV Investors Inc., and the buyer, Los Angeles-based limited partnership Downtown Gateway, of a Fresh & Easy Neighborhood Market store in Loma Linda, CA. The winning bid among six offers for the newly built 15,000-square-foot property was a purchase price of almost $2.87 million, representing a 6.6% cap rate.

A high traffic count location at a signalized intersection in an affluent residential neighborhood was significant in getting the investor comfortable with a "new tenant that has a pretty good story to tell but is unproven," Hanley says. "The market is such today that investors are going back to the fundamentals of commercial real estate--the viability of the tenant, the location, and then the rental rates."

According to the Marcus & Millichap report, the median cap rate for grocery stores was 7.3% in the fourth quarter of 2008, a 20 basis point increase from a year earlier and the media price fell by 10% to $183 a square foot. "Over the past year, Fresh & Easy stores in Arizona and Southern California have traded at approximately $250 per square foot and with average cap rates in the high-5% to low-6% range," the report states.

Fresh & Easy, a US concept from the British company Tesco, is an example of a growing trend of grocery retailers pursuing smaller store formats. Others include Jewel-Osco's Urban Fresh, Safeway's Market concept and Wal-Mart's Neighborhood Market stores. Marcus & Millichap notes that "while grocers cite increasing costs as one reason for smaller store formats, some of the new concepts are in response to the ongoing expansion" of the Fresh & Easy stores, which now number about 100 in the western part of the country. Hanley says he sees a desire to tap into the consumer base of high population, high barriers-to-entry infill locations as a significant driver of the trend.

According to Fresh & Easy's website, recent new store openings include a third location in the Bakersfield, CA market in February, a location in Gilbert, AZ in March and a Pedley, CA store earlier this month. Another in Corona, CA was scheduled to open April 22.

Tuesday Tesco reported that while its 2008 US sales included like-for-like growth of 30%, it suffered trading losses for the year that were higher than previously expected, "reflecting the more challenging trading environment in the Western states and our decision not to open stores in Northern California for the time being. Sales overall were lower than anticipated at the time of last year's preliminary results, as a consequence of our previously announced decision to maintain, rather than accelerate, our rate of new store expansion during the second half given the severity of the economic downturn in some geographic markets in the Western US," Tesco reports.

"I think it's going to be a few years before we see the final results of the mid- and small-size formats," says Hanley of the smaller grocer format concepts. "They're trying to follow the Trader Joe's success. It's a different product, but it's the same size."