2006 **retail**

L.I. retail forecast: Prepare buyers to put more equity into their purchases due to thin profit margins

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10, 9, 8, 7, 6 could either be the anticipated countdown of a NASA shuttle or the final landing of Nassau County capitalization rates. While real estate brokerage is not rocket science, in today's seller's market, a successful broker should add "detective" to his résumé, as listings have become far and few between. Without partnerships dissolving or owners retiring, island-wide commercial brokers agree that the majority of their time is spent romancing sellers, rather than cultivating new buyers.

Specializing in the sale of income-producing properties for the past two decades my partner, Dale Staudigel and I were asked to shed some light on the pulse of the retail market on Long Island from a broker's perspective. While many potential investors sit on the side lines today waiting for rates to rise and the sky to fall, the majority of our investors have not skipped a beat in their pursuit of adding more bricks to their portfolios.

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While the 80/20 rule still holds true that 20% of all investors purchase 80% of properties, today's savvy retail buyer has had to adapt to a supply-constrained market where double digit returns can only be realized over longer time horizons. With capital pouring into real estate due to the heartburn of the Dow (the Dow Jones industrial average has gained just shy of 1% since January 2005), this perfect storm of a seller's market shows little signs of derailing in the first quarter of 2006.

Roy Fedeleman, a principal planner at Suffolk County Planning Department, confirms that indeed today's vacancy factor in Suffolk County for community, neighborhood, and retail strip centers is down to 7.8% from 12% in 2001, but he also points out non-retail service-type tenants lease 33% of all storefronts, compared to 25% in1988.

It's true that more listings came on the market this past quarter which is often the first hint of market psychology shifting, and cap rates rising, but in actuality cash yields continue to float in the 6%-6.75% range for community and neighborhood shopping centers. Of course this overstated rate of return (6%-6.75%) exists only on paper. The reality is a management number (typically 4%-5% of the gross income), a 4% vacancy factor prescribed by lenders, and a reserve for deferred maintenance are expenses that were previously factored in only two years ago by sellers. Today, owners have removed these fundamental expenses from their proformas, inflating their bottom line, and creating unrealistic price points.

Nevertheless buyers outnumber sellers in all asset categories as 1031 money from high net worth individuals and investment groups alike continue to keep sellers in the driver's seat and make retail a safe haven for smart money.

Hopefully, in 2006, through our efforts to contain inflation, interest rates and rising taxes, we can arrive at market normalization, and the only bubble bursting will be from the sound of champagne corks popping.