MARKET REPORT

Marcus & Millichap

RETAIL
Jacksonville Metro Area

Q3/19

Strong Income Growth Attracts Buyers to Low-Cost Acquisitions Along the Coast

Impressive household growth and rising incomes continue to generate retail demand in the metro. Over the past five years, the Jacksonville metro has had the third largest household growth rate compared with Florida's other major metros. Additionally, employment has contributed more than 100,000 positions over the same time period. In 2019, jobs are projected to grow by 1.5 percent, or by 11,000 new positions, as the median household income lifts 6.2 percent to $67,769 per year. These strong demographic shifts will continue to support consumer discretionary spending at local stores, keeping tenant demand for retail space robust and allowing the metro vacancy to drop under 5 percent.

Regional economic momentum coupled with expansion capability spur coastal retail construction. Construction has been prominent in the northern St. John's County submarket, east of St. John's river, as the Beachwalk and Durbin Pavilion developments bring near 700,000 square feet of new retail space. Pent-up demand for big boxes remains steady as Home Depot and Bass Pro Shops move into northern St. John's County. The eastern Nassau County submarket will receive new midsize retail construction, including Aldi and Tractor Supply Co. Metrowide, properties are being absorbed quickly, contracting vacancy. Affordable construction and leasing costs within high income areas of the metro attract local and national retailers looking for sites where they can grow long term.

Retail 2019 Outlook

1.8 MILLION SQ. FT.
will be completed

CONSTRUCTION:
Construction will outpace the prior year's 960,000 square feet by year end. The northern St. John's County submarket and eastern Nassau County submarket will receive the most inventory.

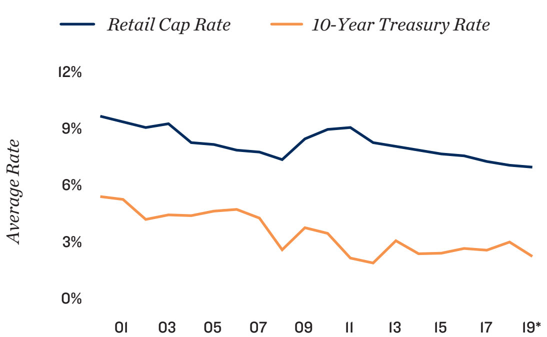
40 BASIS POINT
decrease in vacancy

VACANCY:
Absorption outpaces supply for the seventh consecutive year, tightening vacancy to 4.6 percent, building on last year's 50-basis-point decline.

2.9% INCREASE
in asking rents

RENT:
The average asking rent will grow to $15.40 per square foot in 2019. This will be the third year in a row with a positive increase in rent.

Local Retail Yield Trends



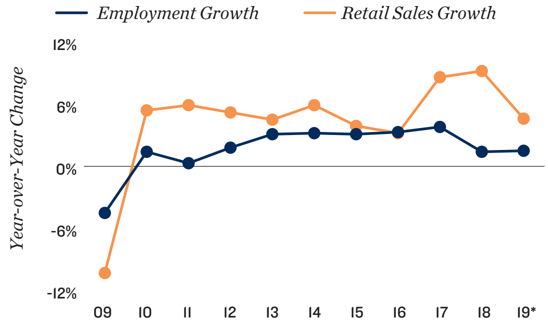
** Cap rates trailing 12 months through 2Q19; 10-year Treasury up to June 30*

Sources: CoStar Group, Inc.; Real Capital Analytics

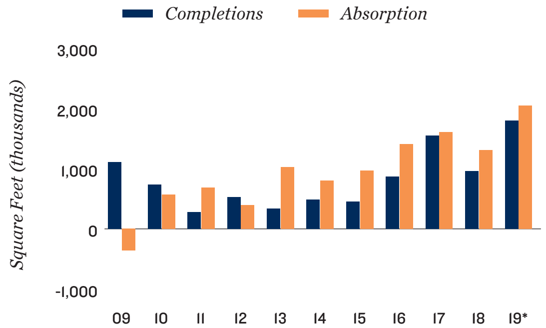
Investment Trends

- Transaction velocity increased over the past four quarters compared with the previous annual period by 15 percent. Trades for both multi-tenant and single-tenant properties contributed to this increase.
- Out-of-market buyers will continue to be active players in Jacksonville. Over the past year, investors from neighboring Georgia, Texas and other major markets in Florida have been active.
- Drugstores and fast-food establishments traded with cap rates in the mid-5 percent range as fast-casual restaurants changed hands in the high-5 percent area. Auto repair and daycare center single-tenant assets provided the highest first-year yields in the high-6 to low-8 percent range.
- Sales remain prominent in within a 5-mile radius of the city of Jacksonville, along the St. John's River. Big-box retail in the outlying suburbs of the city of Jacksonville also shows positive growth. Two former Kmart buildings sold within the past 12-month period to be transformed into alternative uses.

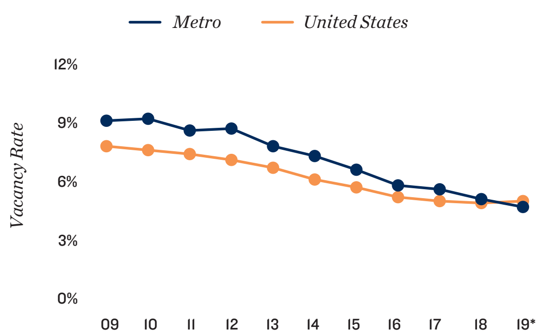
Employment vs. Retail Sales Trends



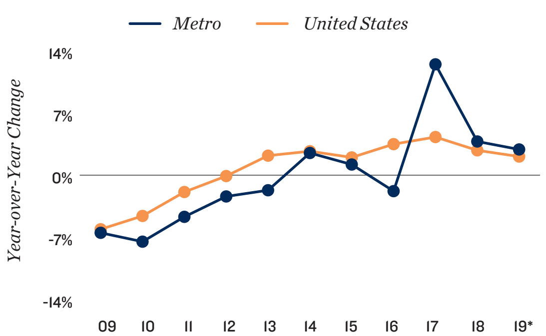
Retail Completions



Vacancy Rate Trends



Asking Rent Trends



*Forecast

Sources: CoStar Group, Inc.; Real Capital Analytics

2Q19 – 12-Month Trend

EMPLOYMENT

1.9% decrease in total employment Y-O-Y

- Over the past year ending June, 13,200 positions were created in the metro, nearly half the amount of employees added one year earlier. The leisure and hospitality sector led job growth, bringing 4,900 new payrolls.
- The unemployment rate has hovered below the 4 percent mark for the past eight consecutive quarters. A smaller pool of applicants has made it more difficult to fill available positions.

CONSTRUCTION

1.1 million square feet completed Y-O-Y

- Construction levels are down from the previous four quarters' 1.5 million square feet.
- Developers have focused their attention in the Southside submarket and in St. Johns County, delivering 802,000 square feet in the past 12-month period. The Beachwalk and Durbin Pavilion developments will deliver the most inventory, totaling nearly 700,000 square feet of retail space.

VACANCY

70 basis point decrease in vacancy Y-O-Y

- Since June of 2018, slightly over 1.5 million square feet of retail space has been absorbed, reducing the vacancy to 4.5 percent matching the prior period's basis point decline.
- Multi-tenant vacancy dropped 120 basis points to 6.0 percent during the same period. The Riverside submarket had the largest drop in retail vacancy, declining 260 basis points to 3.9 percent.

RENT

3.1% increase in the average asking rent Y-O-Y

- Over the past four quarters, the average asking rent in the market has increased 3.1 percent to $15.01 per square foot, building on the prior period's 9.4 percent surge.
- Multi-tenant buildings continue to post strong rent growth, expanding 4.7 percent to $14.07 per square foot during the past 12-month period.

Demographic Highlights

2019 Job Growth*

Metro 1.5%

U.S. Average 1.3%

Five-Year Population Growth**

109,014 *or* 1.4% *Annual Growth*

U.S. 0.6% *Annual Growth*

Five-Year Household Growth**

56,500 *or* 1.9% *Annual Growth*

U.S. 1.0% *Annual Growth*

2Q19 Median Household Income

Metro $65,517

U.S. Median $64,784

2Q19 Retail Sales per Month

$4,200 *Per Household*

U.S. $4,017

$1,626 *Per Person*

U.S. $1,550

Retail Sales Forecast**

Metro 24.7%

U.S. 17.0%

** Forecast ** 2018-2023*

SUBMARKET TRENDS

Lowest Vacancy Rates 2Q19**

Submarket	Vacancy Rate	Y-O-Y Basis Point Change	Average Asking Rent	Y-O-Y % Change
Butler/Baymeadows	2.3%	-10	$16.64	-9.4%
St. Johns County	3.2%	-60	$18.76	5.7%
Arlington	3.9%	-380	$12.33	22.9%
Beaches	3.9%	50	$17.36	-14.1%
Riverside	3.9%	-260	$17.14	13.2%
Southside	4.1%	-80	$14.81	-6.6%
Nassau County	4.2%	0	$13.48	-4.5%
Orange Park/Clay County	5.1%	-90	$12.56	-1.0%
Mandarin	5.3%	210	$16.11	10.9%
Northwest Jacksonville	8.2%	450	$10.00	-8.5%
Metro Area	**4.5%**	**-70**	**$15.01**	**-3.1%**

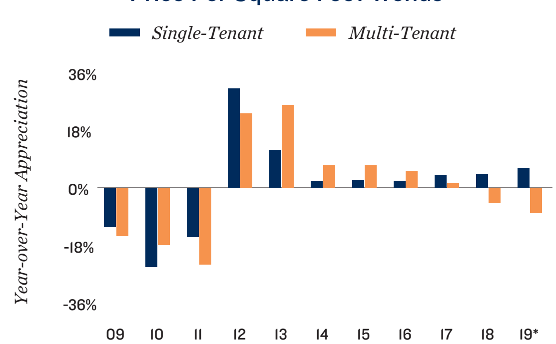
*** Includes submarkets with more than 3.4 million square feet of inventory*

SALES TRENDS

Low Cost and Strong Yields Keep Investors Scouring for Assets in Jacksonville

- **Multi-Tenant:** Transaction volume has remain steady within the past 12-month period compared with the previous period, holding average cap rates in the mid- to high- 7 percent range. The average price per square foot dropped 7.9 percent to $187.
- **Single-Tenant:** Average prices continue to strengthen among the metro, keeping cap rates in the low-6 percent area. The average price per square foot has increased 6.2 percent to $385 per square foot.
- **Outlook:** Investors searching the Southeast scour Jacksonville as it has the lowest entry-level cost compared with the major metros in Florida and Atlanta, with an average price per square foot of $305.

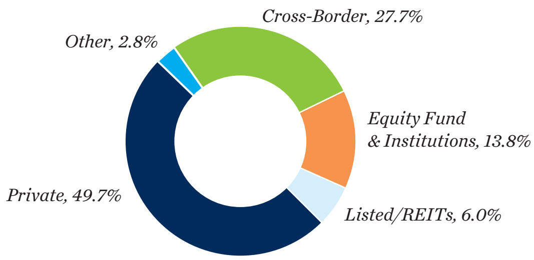
Price Per Square Foot Trends



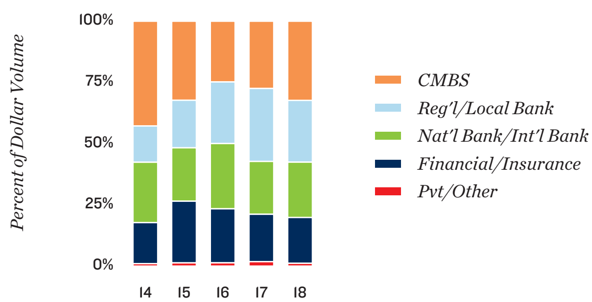
** Trailing 12 months through 2Q19 over previous time period*

Pricing trend sources: CoStar Group, Inc.; Real Capital Analytics

2Q19* Retail Acquisitions By Buyer Type



Retail Mortgage Originations By Lender



** Trailing 12 months through 2Q19*
Include sales $2.5 million and greater
Sources: CoStar Group, Inc.; Real Capital Analytics

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Price: $250

CAPITAL MARKETS

By DAVID G. SHILLINGTON, President, Marcus & Millichap Capital Corporation

- **Fed trying to extend economic runway but hitting headwinds.** The Federal Reserve's decisive action, including their rate drop in July, will support the economic growth cycle, but may be outweighed by the escalating trade war. Uncertainty and caution increased following August 1 announcement that additional tariffs would be levied, sparking a flight to safety and the recent inversion of the 10-year and two-year Treasurys. Though the Fed's 25-basis-point reduction of the overnight rate and early end to quantitative tightening could pose some inflation risk, the Fed has communicated a willingness to let the economy "run hot" in an effort to spur growth. Should core inflation rises above 2 percent, it will not be seen as an immediate risk Falling interest rates, a byproduct of the trade war and the Fed's efforts to boost the economy, will bolster leveraged yields for investors. With the yiel on the 10-year Treasury now down 70 basis points from the cycle peak last October and at their lowest level since 2016, investment options that may not have penciled even 30 days ago have been reinvigorated. This should help moderate the buyer/seller expectation gap that had widened earlier in the year.
- **Lenders shift focus to tenant blends as transforming sector opens new doors.** The evolving nature of the retail sector is providing opportunities for investors and giving underwriters more confidence in the long-term outlook of retail. Lending habits remain relatively conservative; however, a wide range of financing is available for strong proposals. Underwriters are beginning to focus more on tenant mixes while emphasizing the inclusion c tenants with sustainable business models before they sponsor a deal. Activ lenders include local, regional and national banks, insurance companies, debt funds and CMBS lenders. Net-leased assets and premier, mixed-use structures remain the most desirable asset types. Meanwhile, outlying malls and non-credit tenants will be heavily scrutinized and underwritten in a very conservative manner. Loan to Value (LTV) ratios are in the 60% to 70% range with typical debt service coverage (DSC) ratios above 1.30x depending on borrower, asset and location factors. Mezzanine and bridge loan structures have been more frequently used in this environment, with owners financing capital improvements at higher leverage ratios on short-term debt before seeking long-term financing options once their operations have been stabilized.

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Sources: Marcus & Millichap Research Services; Bureau of Labor Statistics; CoStar Group, Inc.; Experian; Moody's Analytics; Real Capital Analytics; TWR/Dodge Pipeline; U.S. Census Bureau