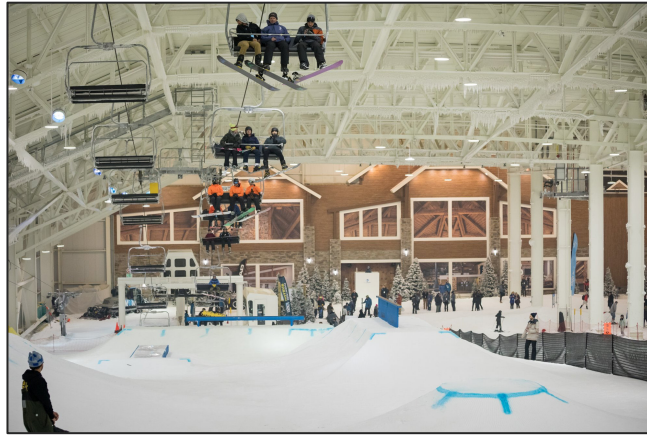


Location, Location, Experience Creation:

The Market Dynamics and Financial Impacts of
Experiential Retail

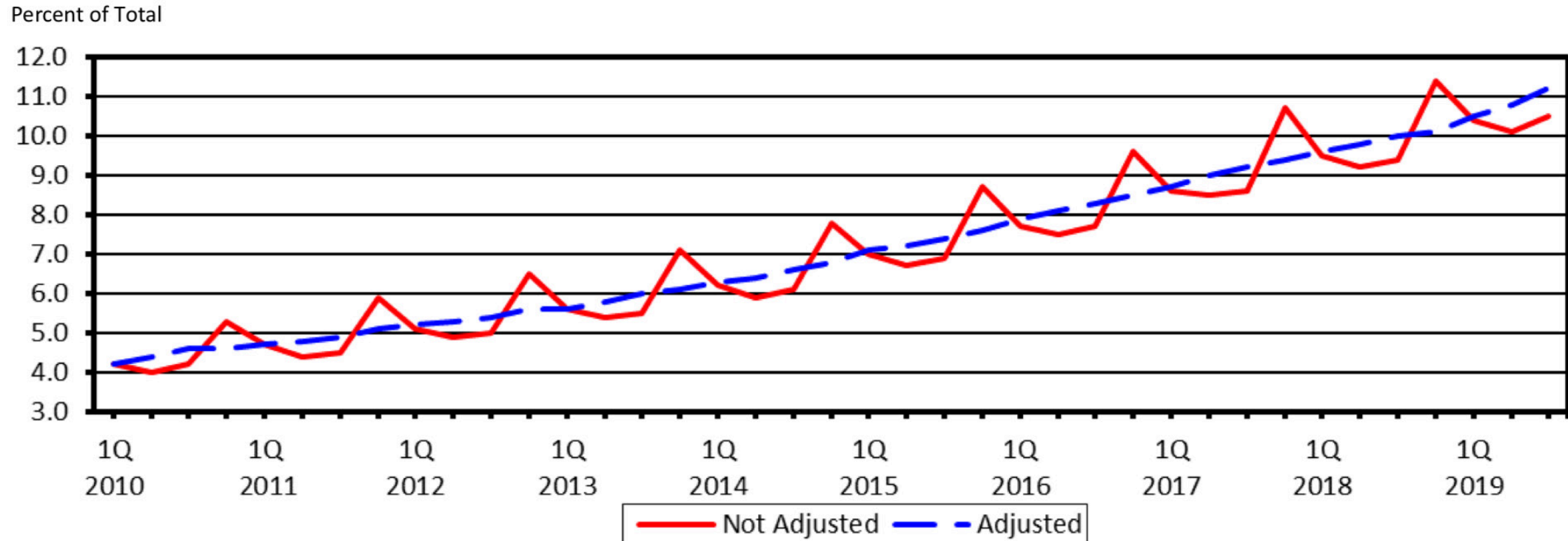
Austin Fields
Dr. Andrea Chegut

What's in Common?



Background: The “Retail Apocalypse”

Estimated Quarterly U.S. Retail E-commerce Sales as a Percent of Total Quarterly Retail Sales



Defining Experience

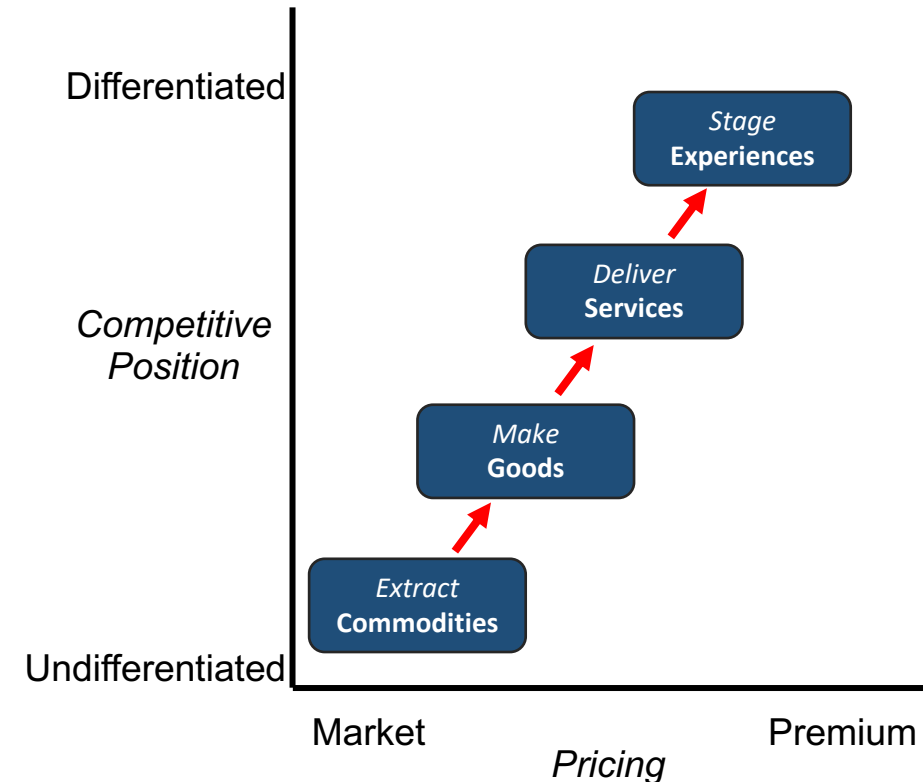
Memorability + Personalization → Differentiation

- Themed
- Harmonize Cues
- Memorabilia
- Engage Senses

JLL's Dimensions of Retail Experience

- Intuitive
- Human
- Meaningful
- Immersive
- Accessible
- Personalized

The Progression of Economic Value



Defining an “Experiential” Metric

Experiential Retail Identification Rubrics

SUFFICIENT CONDITIONS	Weak	Strong
Artistic Installations	YES	YES
Customization (Apparel/Accessories)	YES	YES
Customization (Food/Beverage)	YES	NO
Customization (Hair/Nails/Skin)	YES	YES
Customization (Household goods)	YES	NO
Entertainment	YES	YES
Events	YES	YES
Experiential Grocer	YES	NO
Fitness Classes	YES	YES
Memorabilia	YES	YES
Mixed Program	YES	YES
Spa Program	YES	YES
Technology Integration	YES	NO
Leases	76	62
Buildings	71	58

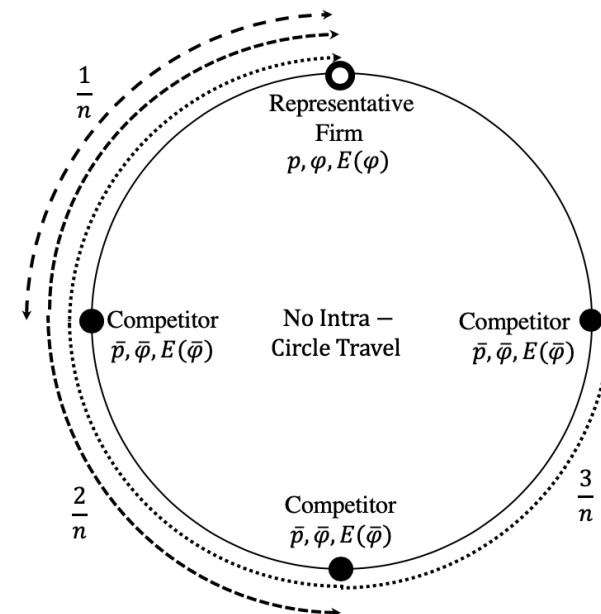
Case Study: Museum of Ice Cream



Theoretical Framework

- Firms invest in experience to drive eWOM, which determines brand awareness
- Experience augments consumer utility. Consumers prefer firms offering better experiences, all else being equal
- Experience and consumers' preferences for e-commerce determine a firm's resistance to e-commerce competition

Model Overview



$$\pi(p, \phi) = \underbrace{(p - c)}_{\text{Firm Profits}} \times \underbrace{\beta(E(\phi))}_{\text{Markup}} \times \underbrace{\left(\frac{\delta\phi(\bar{p} - E(\bar{\phi}) - p + E(\phi))}{t} + \frac{\delta\phi}{n\bar{\phi}} \right)}_{\text{Demand Loss Due to Online Competition}} - \underbrace{F}_{\text{Fixed Costs}} - \underbrace{\omega(E(\phi))}_{\text{Experience Costs}}$$

Firm Profits Markup Demand Loss Due to Online Competition Representative Firm Demand Without Online Competition Fixed Costs Experience Costs

Theoretical Results

- **Proposition 1:** As consumers' preferences for e-commerce increase for a given experience, firms provide more experience, brand awareness increases, some firms exit, and pricing power increases¹
- **Proposition 2:** As experience-to-eWOM conversion efficiency increases, firms provide less experience, brand awareness increases, some firms exit, and pricing power increases
- **Proposition 3:** As fixed costs decrease, firms provide less experience, brand awareness declines, some firms enter, and pricing power declines
- **Proposition 4:** As the magnitude of negative rent discrimination by experience increases, firms provide less experience, brand awareness declines, firms enter the market, and pricing power declines

1) Pricing power is the mark up over marginal production cost.

Empirical Strategy

- We study **166** retail leases executed in **2019** across **New York City**
- We compare **effective rents, tenant concessions, and lease terms** between “experiential” and “non-experiential” tenants
- Augmenting the CompStak data, we collect various proxies for experience
 - Yelp ratings
 - Google Places ratings
 - The Weak and Strong rubrics

Empirical Results

- Experiential tenants, measured by all proxies, command **no statistically significant effective rent or free rent differentials**, conditional on lease characteristics, location fixed effects, time fixed effects, and industry fixed effects
- Experiential tenants, measured by both of rubrics, are associated with an approximate **\$13 PSF TI premium**, conditional on lease characteristics, location fixed effects, time fixed effects, and industry fixed effects
- Experiential tenants, measured by our weak definition, are associated with **17 additional months of lease term**, conditional on lease characteristics, location fixed effects, time fixed effects, and industry fixed effects

Contributions

- Shifting consumer preferences → vacancies/bankruptcies + experience creation
 - As landlords' rewarding experience creation ↑, experience creation ↓
- Preliminary evidence does not support experiential rent discrimination
 - BUT, experiential tenants receive additional TI allowances and longer lease terms (≈zero-interest loan)



Appendix

Rent Discrimination: Yelp Rating

Dependent Variable: Logarithm of Effective Rent				
VARIABLES	(1) Lease Cond.	(2) +Loc. FE	(3) +Time FE	(4) +Ind. FE
Yelp Rating	-0.181** (0.066)	-0.107* (0.057)	-0.096* (0.054)	-0.035 (0.080)
ln(Transaction Size)	-0.245** (0.089)	-0.227*** (0.064)	-0.216*** (0.057)	-0.167** (0.071)
Lease Term (Months)	-0.001 (0.001)	0.001 (0.001)	0.001 (0.001)	0.002 (0.001)
Free Rent (Months)	0.071 (0.042)	0.009 (0.024)	-0.005 (0.022)	-0.024 (0.024)
TI (\$ PSF)	0.003 (0.002)	0.004*** (0.001)	0.004*** (0.001)	0.004*** (0.001)
Sublease (1=YES)	0.420*** (0.133)	0.210* (0.104)	0.150 (0.106)	0.177 (0.191)
Building Renovated (1=YES)	0.543** (0.201)	0.249* (0.131)	0.252* (0.129)	0.145 (0.120)
Location FE	NO	YES	YES	YES
Time FE	NO	NO	YES	YES
Industry FE	NO	NO	NO	YES
Constant	7.192*** (0.631)	5.850*** (0.380)	5.688*** (0.319)	4.760*** (0.494)
Observations	166	166	166	166
R-squared	0.192	0.662	0.671	0.733
F Adj R2	0.156	0.584	0.583	0.617

Notes: This table documents the effect of building and lease characteristics on effective rent per square foot. Location fixed effects are measured at the submarket level. Time fixed effects are measured by lease-commencement quarter dummies. Industry fixed effects are at the NAICS three-digit level. The base case is a tenant that is located on Park Avenue, commences in 2019:Q1, and is in the Food Services and Drinking Places subsector. Standard errors are clustered by submarket and execution year. *** p<0.01, ** p<0.05, * p<0.1.

Rent Discrimination: Weak Def.

Dependent Variable: Logarithm of Effective Rent				
VARIABLES	(1) Lease Cond.	(2) +Loc. FE	(3) +Time FE	(4) +Ind. FE
Experiential (Weak)	-0.179 (0.120)	-0.206** (0.084)	-0.224** (0.086)	-0.173 (0.125)
ln(Transaction Size)	-0.184* (0.097)	-0.196** (0.071)	-0.181*** (0.065)	-0.168* (0.085)
Lease Term (Months)	-0.001 (0.002)	0.001 (0.001)	0.001 (0.001)	0.002 (0.001)
Free Rent (Months)	0.061 (0.045)	0.001 (0.020)	-0.015 (0.018)	-0.030* (0.018)
TI (\$ PSF)	0.004 (0.002)	0.005*** (0.001)	0.005*** (0.001)	0.004*** (0.001)
Sublease (1=YES)	0.583*** (0.171)	0.370** (0.135)	0.285** (0.118)	0.318 (0.224)
Building Renovated (1=YES)	0.563** (0.209)	0.242* (0.134)	0.241* (0.140)	0.156 (0.119)
Location FE	NO	YES	YES	YES
Time FE	NO	NO	YES	YES
Industry FE	NO	NO	NO	YES
Constant	6.138*** (0.585)	5.112*** (0.414)	4.996*** (0.376)	4.564*** (0.659)
Observations	166	166	166	166
R-squared	0.156	0.665	0.679	0.740
F Adj R2	0.119	0.587	0.592	0.626

Notes: This table documents the effect of building and lease characteristics on effective rent per square foot. Location fixed effects are measured at the submarket level. Time fixed effects are measured by lease-commencement quarter dummies. Industry fixed effects are at the NAICS three-digit level. The base case is a non-experiential tenant that is located on Park Avenue, commences in 2019:Q1, and is in the Food Services and Drinking Places subsector. Standard errors are clustered by submarket and execution year. *** p<0.01, ** p<0.05, * p<0.1.

Tenant Incentive Discrimination

Dependent Variables: TI and Free Rent				
VARIABLES	(1) TI	(2) TI	(3) Free Rent	(4) Free Rent
Experiential (Weak)	11.839** (5.475)		-0.190 (0.232)	
Experiential (Strong)		13.161** (5.534)		-0.100 (0.262)
ln(Effective Rent)	15.040*** (5.307)	13.976** (5.271)	-0.400 (0.248)	-0.377 (0.260)
ln(Transaction Size)	3.703 (2.900)	3.701 (3.136)	-0.163 (0.134)	-0.152 (0.136)
Lease Term (Months)	-0.051 (0.071)	-0.040 (0.070)	0.011** (0.005)	0.010** (0.005)
Free Rent (Months)	5.946*** (2.120)	5.840** (2.118)		
TI (\$ PSF)			0.023** (0.008)	0.022** (0.008)
Sublease (1=YES)	10.433 (16.084)	23.878 (15.421)	-2.896*** (0.841)	-3.103*** (0.869)
Building Renovated (1=YES)	5.608 (11.381)	6.248 (11.432)	0.096 (0.475)	0.081 (0.473)
Location FE	YES	YES	YES	YES
Time FE	YES	YES	YES	YES
Industry FE	YES	YES	YES	YES
Constant	-104.798** (47.666)	-100.598* (49.205)	4.701** (1.875)	4.576** (1.918)
Observations	166	166	166	166
R-squared	0.463	0.466	0.469	0.468
F Adj R2	0.230	0.234	0.239	0.237

Notes: This table documents the effect of building and lease characteristics on TI per square foot and free rent in months. Location fixed effects are measured at the submarket level. Time fixed effects are measured by lease-commencement quarter dummies. Industry fixed effects are at the NAICS three-digit level. The base case is a non-experiential tenant that is located on Park Avenue, commences in 2019:Q1, and is in the Food Services and Drinking Places subsector. Standard errors are clustered by submarket and execution year. *** p<0.01, ** p<0.05, * p<0.1.

Lease Term Discrimination

Dependent Variable: Lease Term		
VARIABLES	(1) Lease Term	(2) Lease Term
Experiential (Weak)	17.070** (6.934)	
Experiential (Strong)		9.475 (8.231)
ln(Effective Rent)	16.812 (13.022)	15.039 (14.343)
ln(Transaction Size)	21.731** (8.707)	21.204** (8.992)
Free Rent (Months)	6.864** (2.935)	6.854** (2.943)
TI (\$ PSF)	-0.125 (0.197)	-0.103 (0.195)
Sublease (1=YES)	-8.657 (25.755)	9.618 (30.352)
Building Renovated (1=YES)	-7.615 (17.268)	-6.448 (17.348)
Location FE	YES	YES
Time FE	YES	YES
Industry FE	YES	YES
Constant	-97.319 (110.609)	-87.639 (116.153)
Observations	166	166
R-squared	0.578	0.567
F Adj R2	0.394	0.379

Notes: This table documents the effect of building and lease characteristics on lease term in months. Location fixed effects are measured at the submarket level. Time fixed effects are measured by lease-commencement quarter dummies. Industry fixed effects are at the NAICS three-digit level. The base case is a non-experiential tenant that is located on Park Avenue, commences in 2019:Q1, and is in the Food Services and Drinking Places subsector. Standard errors are clustered by submarket and execution year. *** p<0.01, ** p<0.05, * p<0.1.