

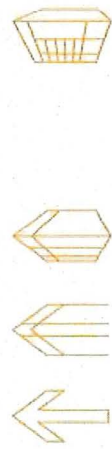
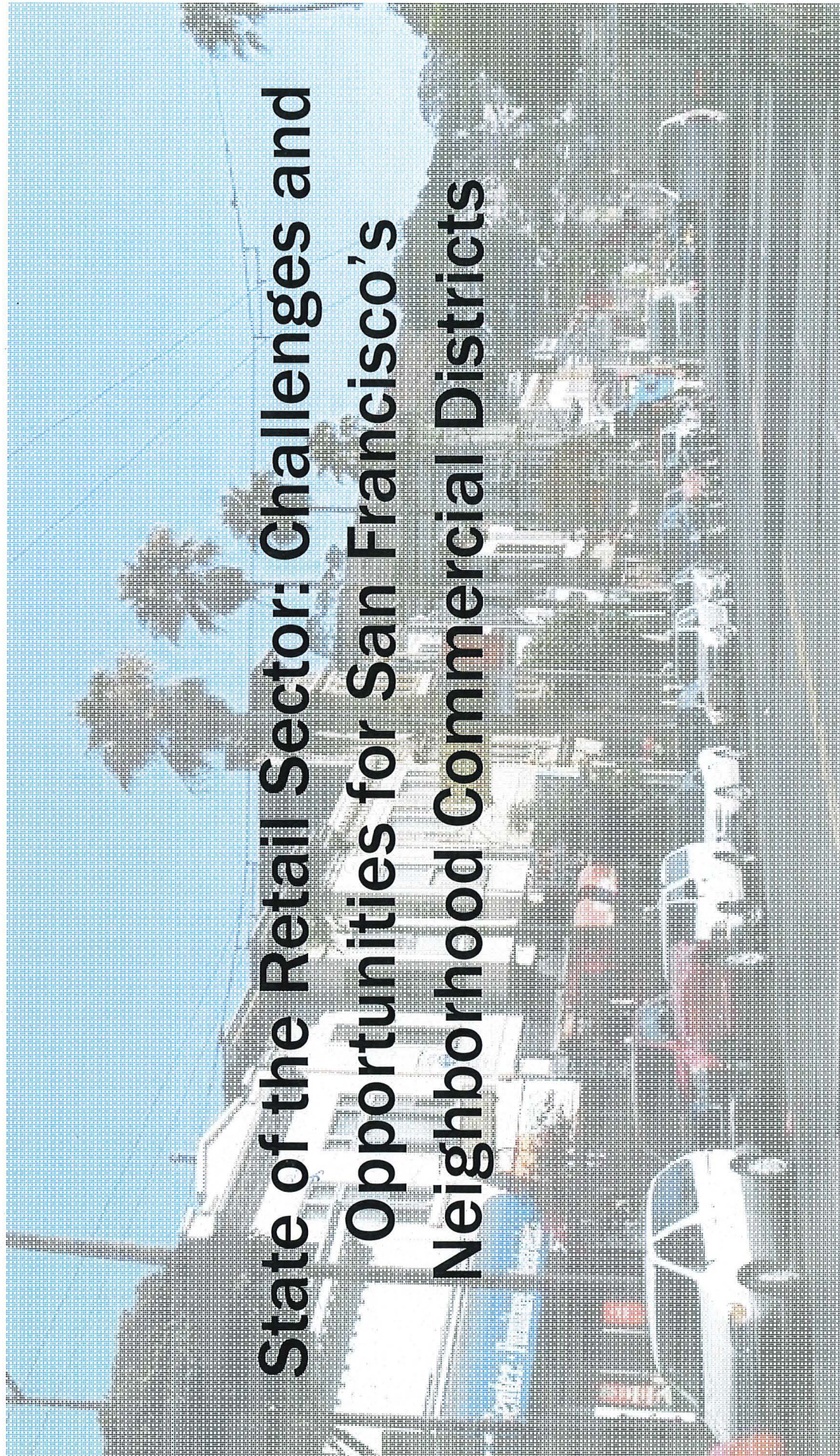


Informational Hearings Neighborhood Retail Study & Strategies for Storefront Vacancies

Land Use & Transportation Committee
February 5, 2018

Land Use 2/5/18

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



STRATEGICECONOMICS

Presentation to the San Francisco Board of Supervisors Land Use Committee

February 5, 2018

Introduction

Study overview

- **Strategic Economics prepared a series of related issue briefs for the San Francisco Office of Economic and Workforce Development (OEWD):**
 - Issue Brief 1: National Retail Industry Trends and Implications for San Francisco
 - Issue Brief 2: What Makes a Successful San Francisco NCD?
 - Issue Brief 3: Costs and Challenges of Doing Business in San Francisco
- **Study does not provide specific policy and program recommendations, but is intended to inform future recommendations by departments and policy makers.**

Introduction

Focus of the study: retail, restaurant, nightlife and entertainment, personal services industries

- **Retail Sales Establishments:** Brick-and-mortar and online stores selling physical products (such as groceries, clothing, sports equipment, toys, etc.).
- **Restaurants:** Establishments serving food and/or beverages for consumption on the premises (or in some cases for take-out), generally including cafés and bars as well as fine dining, casual, and other restaurants.
- **Nightlife and Entertainment:** Restaurants, bars, clubs, theaters, and other venues open during evening hours.
- **Personal Services & Fitness:** Establishments providing personal services to the general public, such as hair salons, nail salons, barber shops, gyms or other fitness centers, etc.

National Trends

The national retail industry is undergoing a major restructuring

- **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.
- **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.
- **However, while many types of stores are struggling, discount retailers continue to open new locations.** 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

Increasing influence of e-commerce

- **Online sales are driving retail sales growth, and expanding into new categories.** Nationally, online retailers accounted for 40 percent of retail sales growth between 2014 and 2016, with growth in categories including apparel, office supplies, sporting goods, toys, and groceries.
- **National retail employment remains flat, while e-commerce employment is growing.** Employment attributed directly to e-commerce has doubled in the last five years.
- **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

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 9th 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's many competitive advantages for retail and restaurants have somewhat insulated the City's retail from national trends.** These include:
 - Strong local economy.
 - A culture that values shopping local and eating out.
 - Significant regional and international tourism.
 - The attractive environment offered by many NCDs.
 - Limited number of malls and a large number of independent businesses.
- **However, after many years of growth, San Francisco's retail sector appears to be slowing.**
 - Sales tax revenues slowed between 2015 and 2016.
 - NCD rents have reportedly plateaued, and vacancies in some NCDs are increasing.
 - Retail employment is growing, but relatively slowly compared to incomes and the rest of the economy.
 - Business owners report increased competition with e-commerce and in more categories (e.g., groceries, clothing, personal care goods).
 - Fewer traditional retailers are seeking space; increased interest from other uses.

Challenges for San Francisco Businesses

In addition to national trends, San Francisco retailers also face more local challenges

- **Employee recruitment and retention challenges**
- **High labor costs**
- **High rents**
- **Land use regulations and permitting requirements**
- **Loss of long-time customers**
- **Public realm (streets and public spaces) challenges**

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 (e.g., selling products online, developing a stronger social media presence, offering classes and events)
 - Reduce costs (e.g., adopting less labor-intensive business models, making do with less space)
 - Diversify revenue streams (e.g., expanding inventories, serving food or alcohol, subleasing space to other retailers)
- **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.**

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.

Conclusions & Implications

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.**

Conclusions & Implications

Conclusion #1: To thrive in a more challenging business environment, retailers need to embrace new technologies. For example, this includes online sales, social media, and app-based delivery services.

Implications

- Businesses may benefit from **technical and financial support** in expanding their online presence, adjusting their inventories for a changing customer base, etc.
- **Curb management policies may need to be revisited to maintain customer access**, effectively manage competing transportation needs (pedestrians, bicyclists, delivery vehicles, TNCs, and parking), and support a pedestrian-friendly environment, while enabling new businesses to take advantage of emerging delivery technologies.

Conclusions & Implications

Conclusion #2: Retailers need to be flexible and creative to provide customers with a more interesting experience. For example, by offering classes and workshops, hosting events, and serving food and beverages, to draw shoppers into stores.

Implications

- **Land use policies may need to be modified to provide retailers more flexibility,** for example in experimenting with combining uses and expanding services (e.g., serving food and beverages or incorporating “maker” or PDR space).

Conclusions & Implications

Conclusion #3: Diversifying the mix of uses in an NCD can help retailers expand their customer base. The components of a healthy mix vary by district, but typically include some combination of the following:

- **Anchor businesses** that drive foot traffic to the district, including to other businesses in the same commercial district. Examples include full-service grocery stores, general merchandise stores, other larger stores (many of which are formula retail) or a cluster of related retail stores or restaurants.
- **Restaurants, nightlife, and entertainment** that complement retail sales and services by providing destinations and gathering spaces for potential customers.
- **Personal services & fitness centers** that provide needed services and also help draw foot traffic.
- **Professional services** that provide needed services in an office-like setting directly to the general public.
- **Office & housing uses** that may not directly serve the general public, but help generate foot traffic and demand for retail.

Conclusions & Implications

Conclusion #3, Continued: Diversifying the mix of uses in an NCD can help retailers expand their customer base.

Implications

- New ground floor retail should **include a range of storefront sizes** and storefronts should be **designed to maximize marketability and be adaptable** to the needs of a diverse set of retailers, restaurants, etc.
- **Office and housing uses** that may not be open to the general public could be located **above the ground floor, or on the ground floor in weaker market locations** (e.g., at the periphery of an NCD).
- **Limiting ground floor retail requirements** for new development to the strongest locations for retail could help reduce potential vacancies.

Conclusions & Implications

Conclusion #4: By offering an attractive, fun shopping and dining experience, NCDs can help retailers continue to draw foot traffic.

Implications

- **Continuing to maintain and enhance the public realm** is critical.
- **Celebrating local historic and cultural assets** can contribute to a unique and interesting environment.
- **High-capacity district management organizations** can help districts create a great experience for residents and visitors.

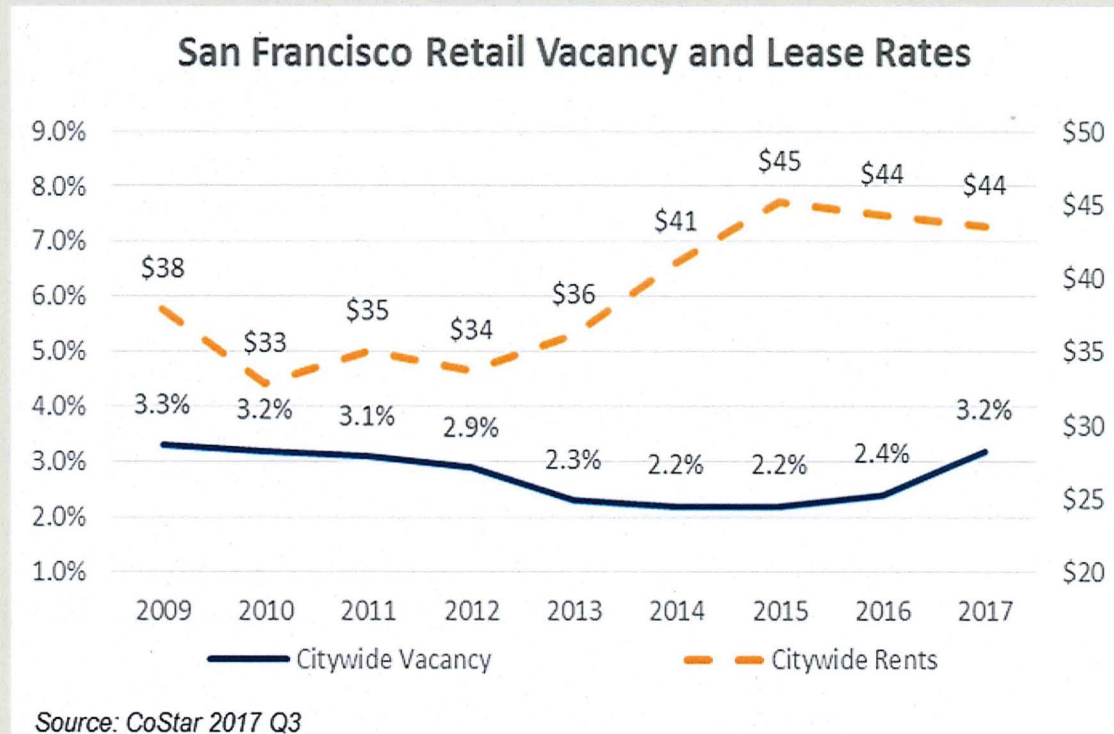
How does OEWD define “vacancy”?

A vacant storefront is:

- Empty with no identified future occupant
- Under construction, or
- Occupied with a non-commercial use

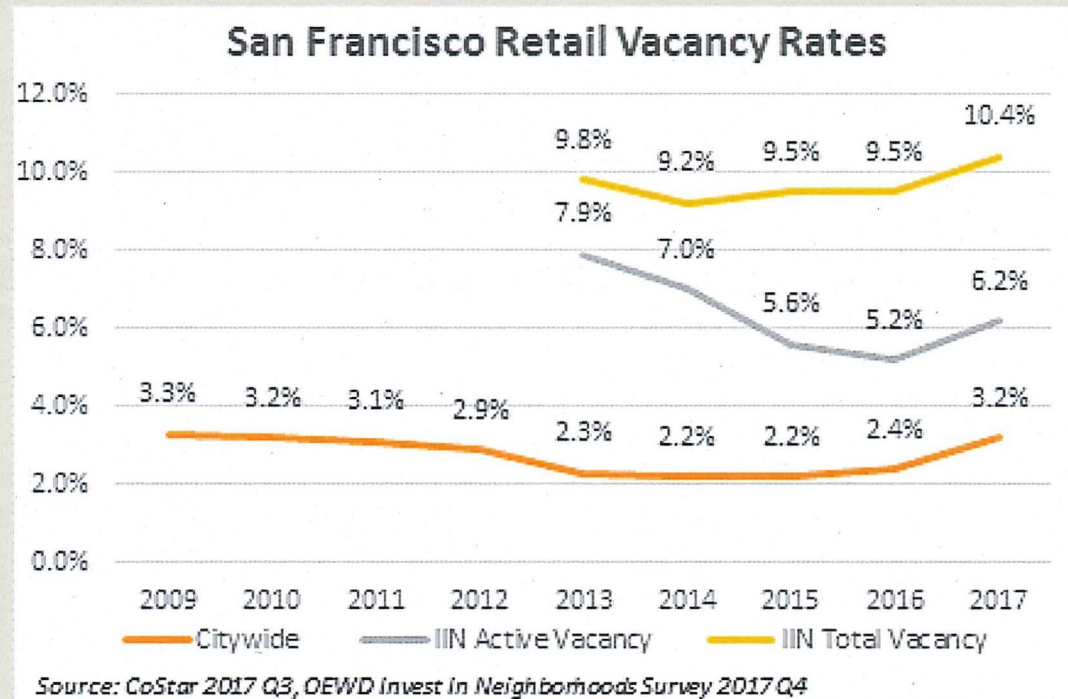
What is “healthy” vacancy?

- 5%-10% vacancy is the target range
- OEWD is concerned when vacancies are too high, as well as too low
- San Francisco maintained low vacancy rates through the last recession
- Overall low vacancy rates has put upward pressure on lease rates



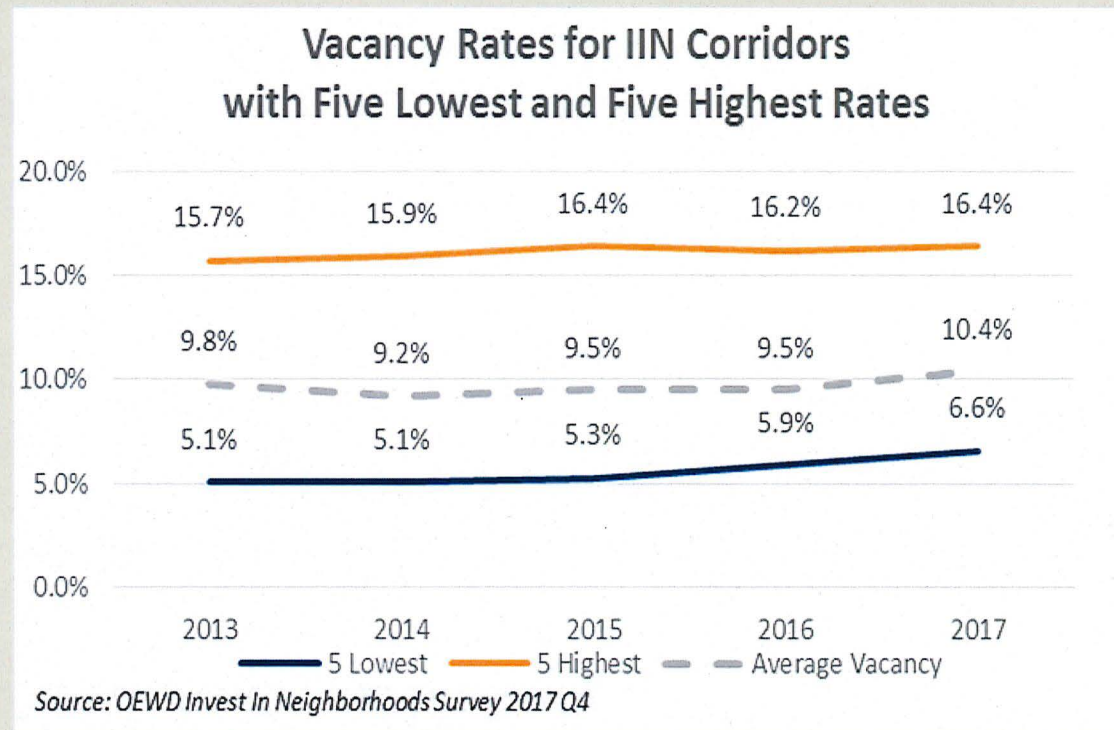
Citywide and Corridor Retail Vacancy

- Retail vacancy rate in SF as of 2017 Q3 is 3.2%
- IIN corridors surveyed had an average Q4 vacancy rate of 6.2%
- Higher than the city average, but within the “target” range
- Including inactive vacancies, the rate goes up to 10.4%

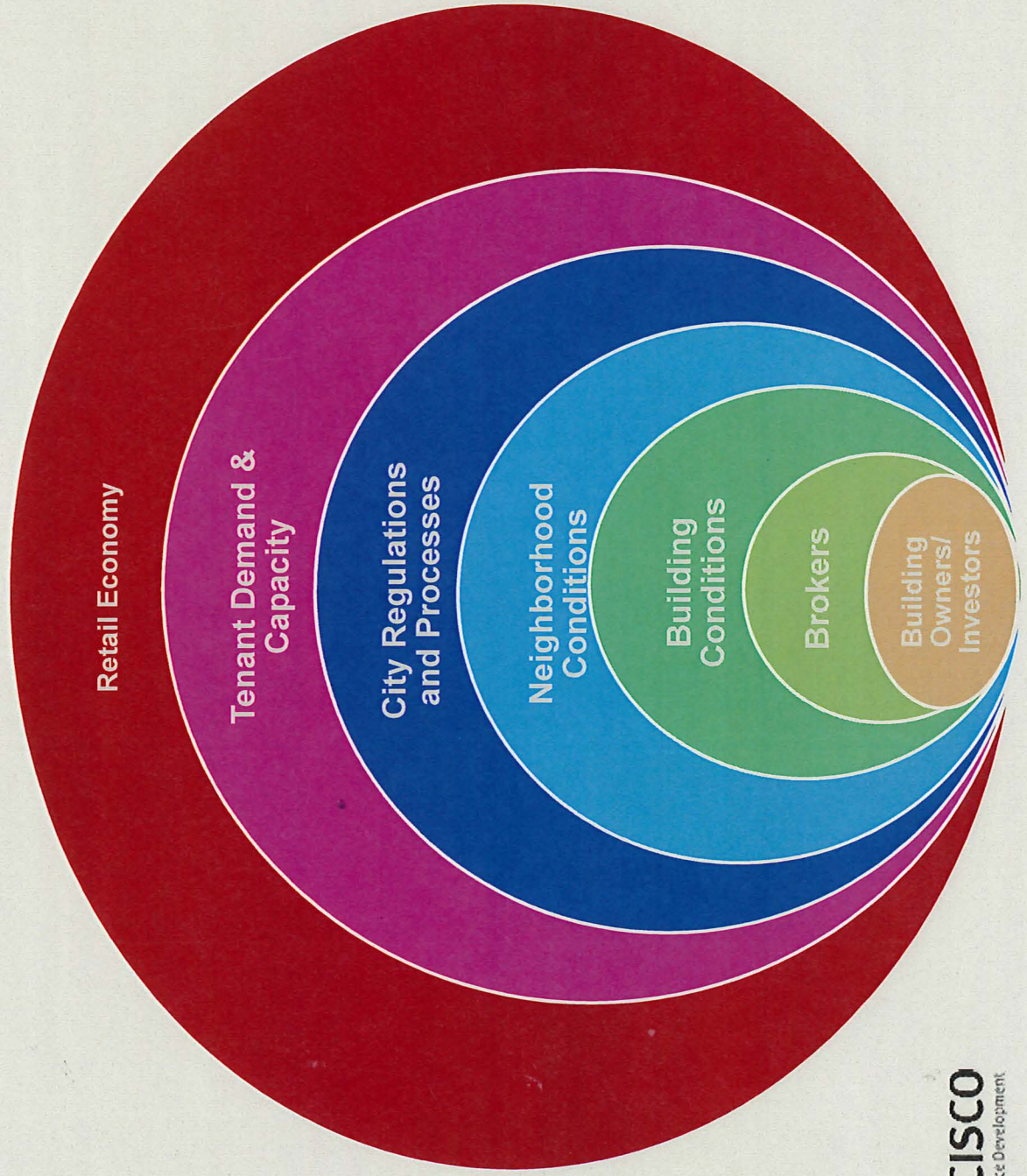


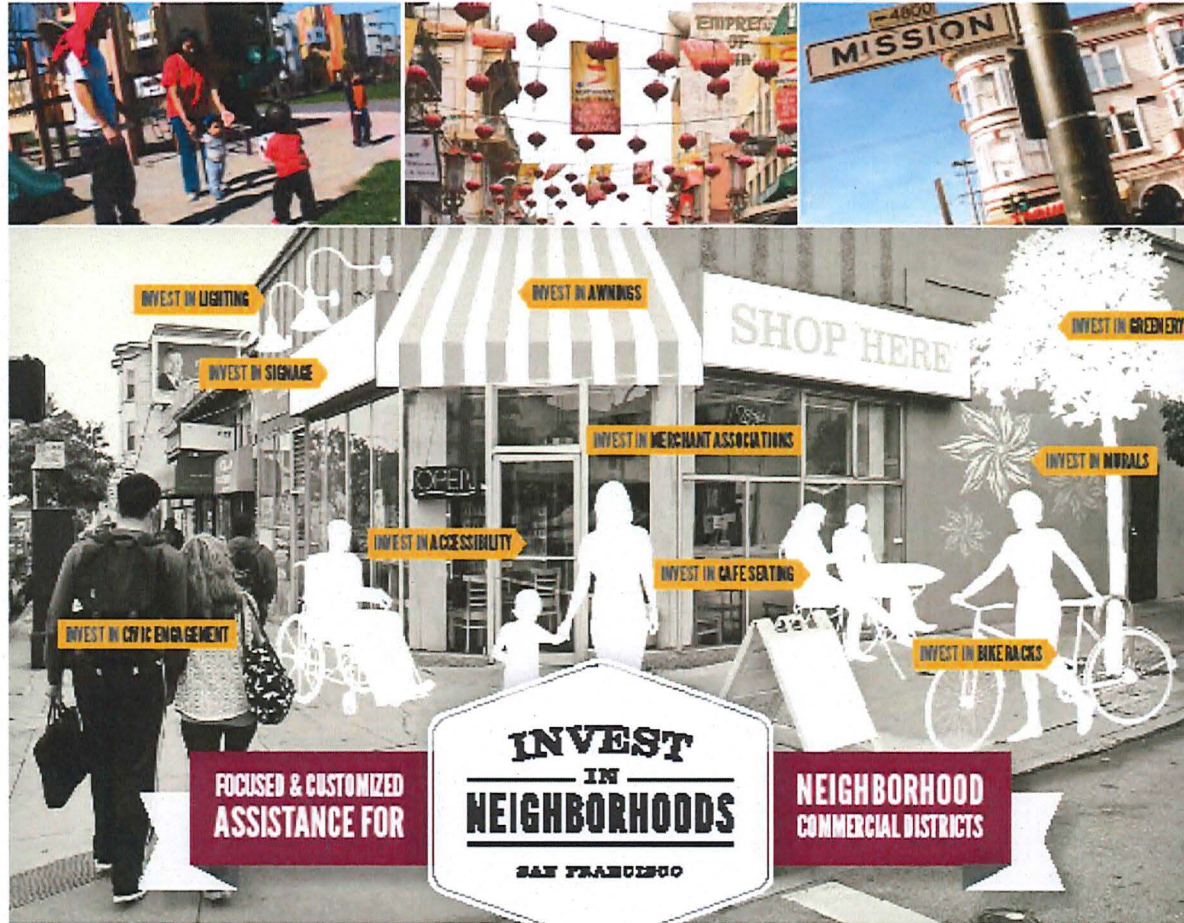
5 Lowest and Highest Neighborhood Vacancy Rates

- Five highest vacancy rate corridors averaged 16.4% in 2017
- Five lowest vacancy rate corridors averaged 6.6% in 2017
- 1/3 of NCDs saw vacancy rate increases of at least 2% since 2015



Factors Contributing to Vacancies





San Francisco's neighborhood commercial districts will be economically thriving, safe, resilient, sustainable, and meet the needs of local residents.

OEWD Programs and Services

Commercial District Planning & Management

- **Economic Development Plans**
- **Community Benefit Districts**
- **Merchant Association and Nonprofit Capacity Building**
- **Cultural District Planning**
- **District Marketing Assistance**
- **Public Realm Enhancements**

OEWD Programs and Services

Business Strengthening and Retention

- **Jobs Squad**
- **Small Business Technical Assistance and Consulting**
- **ADA Program**
- **Construction Mitigation and Disaster Recovery Assistance**
- **Business Retention and Relocation**
- **Small Business Loan Programs**
- **SF Shines Façade Improvement Program**

OEWD Programs and Services

Business Attraction

- **Target Business Attraction**
- **Small Business Loan Programs**
- **SF Shines Façade Improvement Program**
- **Small Business Acceleration Program**

Existing Tools: Planning Department

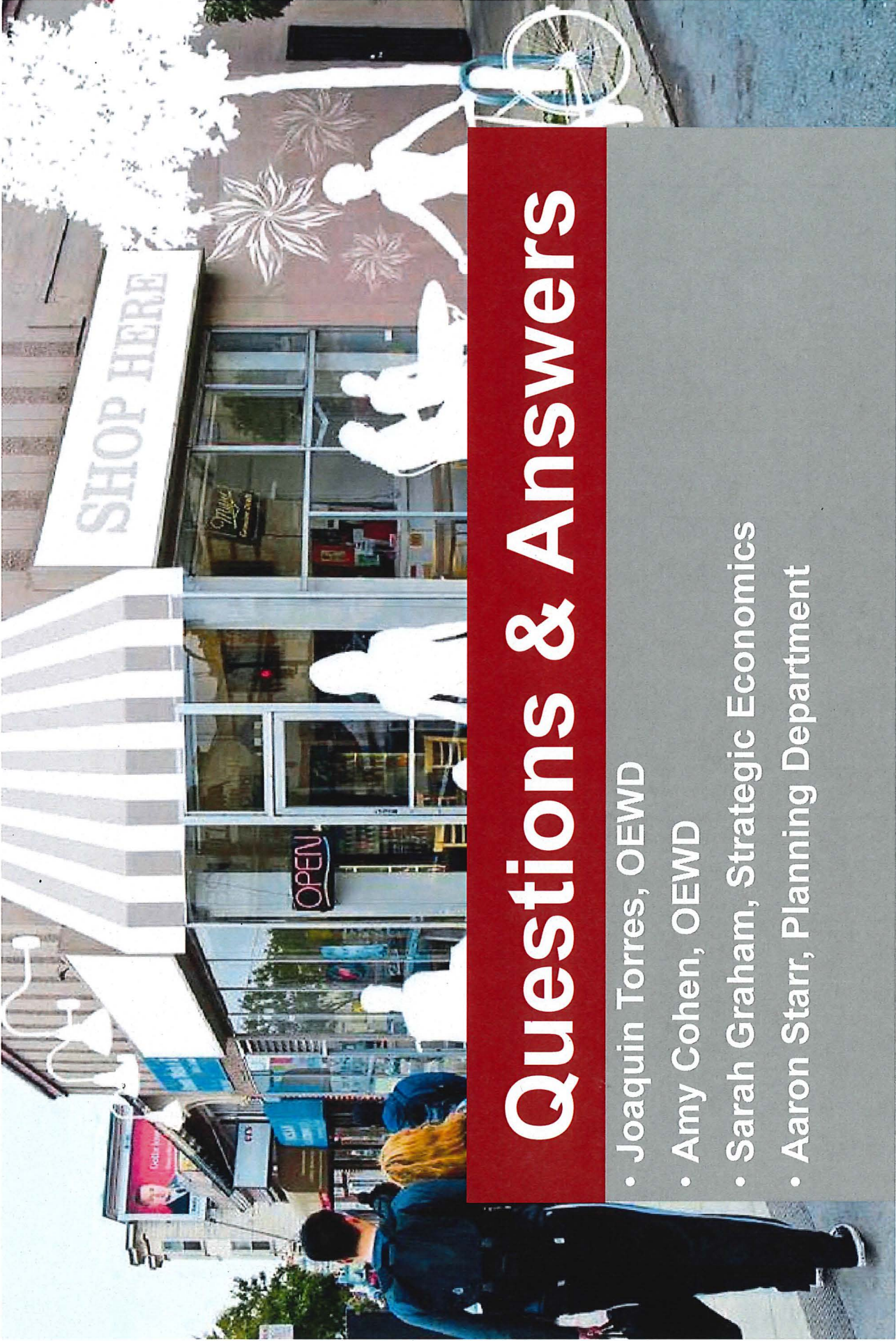
- **Individually Named NC Districts**
- **Vertical Zoning Controls**
- **Formula Retail Controls**
- **Use Permit Approval Process**
 - Principally Permitted
 - Conditional Use Authorization (PC §303)
 - Discretionary Review
 - Neighborhood Notification (PC §312)
- **Storefront Development Regulations**
 - Design Guidelines (Existing and Pending)
 - Street Frontage and Transparency Requirements (PC §145.1)
 - Non-Residential Use Size Limits (PC §121.2)
 - Active Commercial Use Requirements (PC §145.4)
 - Ground Floor 5' Height Bonus (PC §263.2)
- **Historic Preservation Review**
- **Accessory Use Controls**

Policy and Program Changes for Consideration

- **Small business technical assistance programs**
- **Neighborhood commercial district management programs**
- **Storefront development regulations & design guidelines**
 - **Ensure retail marketability and pedestrian experience**
 - **Promote activation for non-retail uses**
- **Use controls**
 - **Create flexibility in targeted areas with vacancy concerns**
 - **Reduce barriers to combining multiple uses within one storefront**
- **Curb management policy**
- **Enforcement**
 - **Update DBI Enforcement Program**

Next Steps

- 1. Gather feedback on retail study and recommendations**
 - Retail Study Public Hearings BOS (2/5/18)
 - SBC Hearing (2/12/18)
 - Planning Commission Hearing (2/22/18)
- 2. OEWD identify & implement business technical assistance program modifications**
- 3. Planning Department to review the retail study and hearing information to develop recommendations for the 2/22 planning commission**
- 4. DBI identify & implement Vacancy Enforcement program modifications (DBI)**



Questions & Answers

- Joaquin Torres, OEWD
- Amy Cohen, OEWD
- Sarah Graham, Strategic Economics
- Aaron Starr, Planning Department

PREVENTING AND FILLING COMMERCIAL VACANCIES IN SAN FRANCISCO

Policy Analysis Report to Supervisor Yee (issued January 16, 2018)

Presentation to:

LAND USE & TRANSPORTATION COMMITTEE

BOARD OF SUPERVISORS

CITY AND COUNTY OF SAN FRANCISCO

February 5, 2018

Budget and Legislative Analyst

Land Use 2/5/18

Commercial vacancies causes and effects

Causes:

- Normal turnover (typically, under a year).
- Non-leasable buildings (e.g., non-conforming uses, Building Code compliance issues).
- Owner lack of information about and tools to help find a new tenant.
- Speculation to obtain higher rents or sale prices in the future.
- Absentee landlords: Property owners may live or operate outside of the local area and may not be motivated to fill the vacancy in a prompt timeframe.
- Neighborhood conditions makes property unattractive to a new tenant.
- City regulations and zoning.
- Disputes among partnership or family ownership.
- Landlords not willing to improve the property to make it more marketable.
- Landlords waiting for a particular type of tenant (e.g., national firm able to pay higher rent).

➤ *Prolonged vacancies or abandonments can lead to blight, loss of community-serving small businesses, and weaker neighborhood economies.*

The City's commercial & abandoned building vacancy ordinances

Ordinance	Requirements	Fees
Vacant or Abandoned Building Ordinance (2009, Building Code 103A.4)	Owners of vacant or abandoned residential or commercial buildings must register with Department of Building Inspection (DBI) after 30 days of vacancy.* Failure to comply can result in penalties.	\$711 annual fee due with registration.
Vacant Commercial Storefront Ordinance (2014, Building Code 103A.5)	Owners of vacant commercial storefronts must register with Department of Building Inspection (DBI) after 30 days of vacancy.* Failure to comply can result in penalties.	\$711 annual fee but not until storefront has been vacant 270 days.

**Excludes buildings and storefronts under permit, awaiting permit, not classified as blighted and being marketed for sale or lease.*



OEWD programs & services addressing commercial vacancies

Aimed at preventing commercial vacancies:

- Jobs Squad**
- Business Retention and Relocation**
- ADA Outreach**
- Small Business Technical Assistance**
- Business Corridor Management**
- Small Business Revolving Loan Fund**
- Emerging Business Loan Fund**
- SF Shines**

Aimed at existing commercial vacancies:

- Targeted Business Attraction**
- The Small Business Acceleration Program**
- Non-Retail Activation of Vacant Storefronts**

How many buildings & commercial storefronts are vacant or abandoned?

Citywide information not available from City or private sector measuring commercial vacancies & abandonments.

Source	Measure	Limitation	Vacancy rate/amount reported
Private real estate companies	Commercial vacancies	Generally downtown office, selected neighborhoods.	Varies
City Controller	Commercial vacancies	Downtown only	8.2% (Q4 2016)
Office of Economic & Workforce Development	Commercial storefront vacancies	Not Citywide: 24 commercial corridors only.	5% for corridors tracked (FY '16)
U.S. Postal Service	Commercial addresses with stopped mail service 90+ days	Includes commercial spaces not covered by ordinances.	7.4% 3,448 addresses (2016)

Apparent low compliance with commercial vacancy ordinances

Vacant or Abandoned Buildings and Storefronts on DBI Registries, 2013-2016

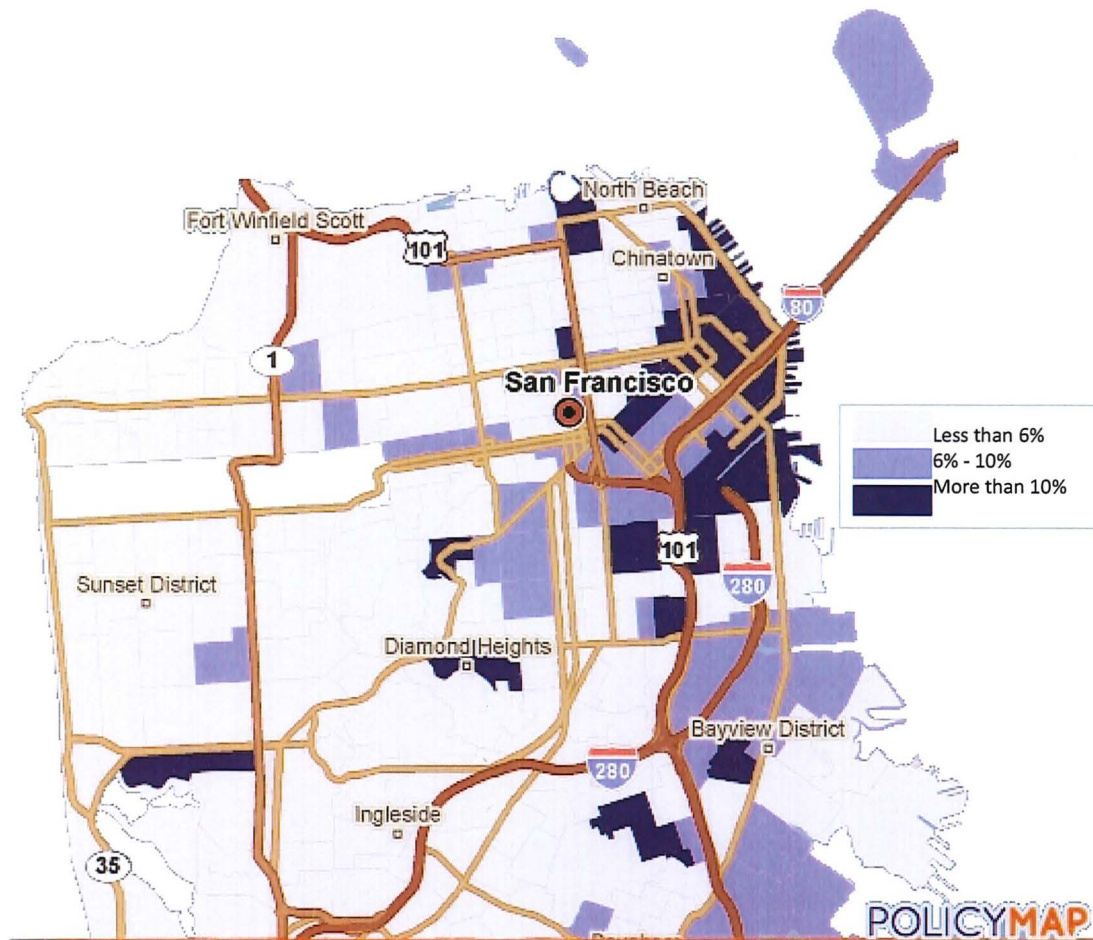
Type	2013	2014	2015	2016
Total buildings (residential & commercial)	224	267	243	220
Commercial buildings only	38	32	30	28
Commercial storefronts	-	-	38	25

Source: Vacant Building Registry, Vacant Commercial Storefront Registry. Department of Building Inspection.

Of the commercial storefronts:

- 16 on Haight and Polk Streets in 2016 (64%); 33/38 on 3rd Street, Mission Street, and Ocean Ave in 2015 (87%).
- None in Chinatown, Castro, Richmond, Central Mission, Financial District in 2016.
- Castro/Upper Market study: 53 vacant commercial storefronts (Hoodline, 3/17)

Distribution of 3,448 vacant commercial properties reported by U.S. Postal Service (Q4 2016)



Number of properties and fees collected for vacant or abandoned buildings or commercial storefronts, 2013-2016

Type	2013		2014		2015*		2016	
	Number	Fees	Number	Fees	Number	Fees	Number	Fees
Total Buildings (residential and commercial)	158	\$120,870	101	\$76,995	103	\$77,013	58	\$41,238
Commercial Buildings Only	32	\$24,480	20	\$15,300	17	\$12,465	7	\$4,977
Commercial Storefronts	-	-	-	-	5	\$3,555	5	\$3,555

Source: Vacant Building Registry, Vacant Commercial Storefront Registry. Department of Building Inspection.

*The annual fee was reduced in 2015 from \$765 to \$711.

Many cases are not abated or closed each year

Cases Closed or Abated, Vacant or Abandoned Buildings and Storefronts, 2013-2016

Commercial Buildings	2013	2014	2015	2016
Closed or abated	20	24	14	11
Closed	5	8	5	7
Abated, not closed	15	16	9	4
Not closed or abated	18	8	16	17
Registry Total	38	32	30	28
Commercial Storefronts				
	2013	2014	2015	2016
Closed or abated	-	-	18	14
Closed	-	-	10	3
Abated, not closed	-	-	8	11
Not closed or abated	-	-	20	11
Registry Total	-	-	38	25

Source: Vacant Building Registry, Vacant Commercial Storefront Registry. Department of Building Inspection.



Limitations: ordinance enforcement

- Assuming actual number of vacant and abandoned commercial buildings and storefronts is higher, owners not registering, in violation of ordinances.
- DBI does not pro-actively identify vacant or abandoned commercial properties:
 - most identified through citizen complaint,
 - other sources: owner self-reporting, City employee reporting.
- DBI does not monitor vacancies after they are reported & added to registries.
- Fee collection is low, resulting in limited resources for DBI's program.
- Registries not posted online.

Commercial vacancies a problem in other cities

City	Areas measured	Vacancy rate range	Notes	When
New York City	Retail corridors throughout city	5 – 20%	Higher vacancy rates in high rent areas (Madison Ave., SoHo, Columbus Ave.)	3/17
Chicago	Metro area	3.8 – 14.3% 10% overall	Rising costs affecting independent business's ability to remain open.	8/17
San Francisco	Commercial areas tracked by OEWD	1.3% - 16.9% (W. Portal – Visitacion Valley)		

Approaches to commercial & abandoned vacancies: other jurisdictions

City	Program	Details
Chicago	Economic Development programs for 8 distressed corridors	Neighborhood Opportunity Fund: contributions from downtown developers for density bonuses. Retail Thrive Zones: reduced property taxes, competitive grants.
	More stringent registration & fee program	Fees every 6 mos. (\$200 - \$2,000) Higher fees if vacancy not reported by owner or if cited for repeat building code violations.
Washington, D.C.	Supplemental property tax for vacant blighted buildings	5% tax on assessed value for vacant non-blighted; 10% for vacant, blighted. <i>Not applicable in California.</i>
Dallas & State of Michigan	Government acquisition of vacant properties	Land banks acquire, hold, manage & develop vacant & abandoned properties.
Seattle	Zoning code changes	Reducing properties zoned exclusively for retail. Reduction in areas zoned as neighborhood commercial. Removing some ground floor retail requirements for multi-story projects.

Zoning and planning changes to address commercial vacancies in SF

- Planning Commission considered, but denied, proposal allowing retail space to convert to office (Union Square: 222 Sutter, 3rd floor, 2017).
- Planning Commission: approved expanded definition of Neighborhood Commercial districts, making it easier to open childcare without conditional use permits (including ground floor retail). Approved by BOS July 2017.
- Proposals to require smaller ground floor retail spaces in Central SoMa, allowing for a mix of retail uses and types. (*Central SoMa Plan & Implementation Strategy*, SF Planning Dept. 2016)

Policy options

The Board of Supervisors could:

1. Enhance funding for the City's existing small business programs.
2. Request Planning Department and Planning Commission consider and report back on possible Zoning and Planning Code changes for more flexible use of commercial spaces
3. Suggest that DBI improve outreach on the Vacant & Abandoned Building and Commercial Storefront registration requirements and reduce barriers to reporting vacant & abandoned commercial properties by the public and City agencies.
4. Amend Ordinances to raise fees and penalties, particularly for non-registrants or properties with extended vacancies to serve as an incentive for property owners
5. Request that, in combination with improving identification, reporting, and monitoring of vacant properties, DBI leverage HUD data to identify areas that have high commercial vacancy rates and proactively track changes in those areas over time.
6. Request that DBI make Vacant Building and Commercial Storefront registries publicly available.



Questions and comments

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