ZRP | ZIFF REAL ESTATE PARTNERS

Retail Update
July 2024

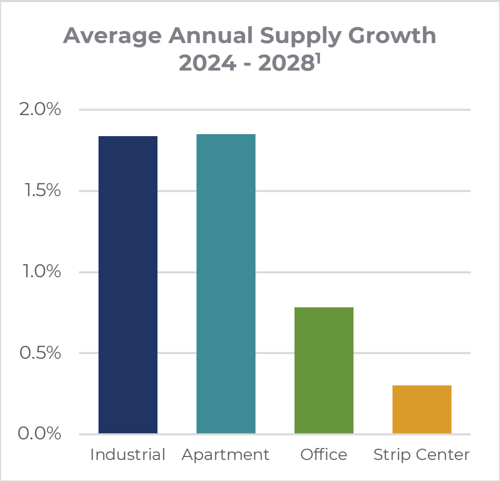
COMPELLING OPPORTUNITY IN STRIP RETAIL CENTERS

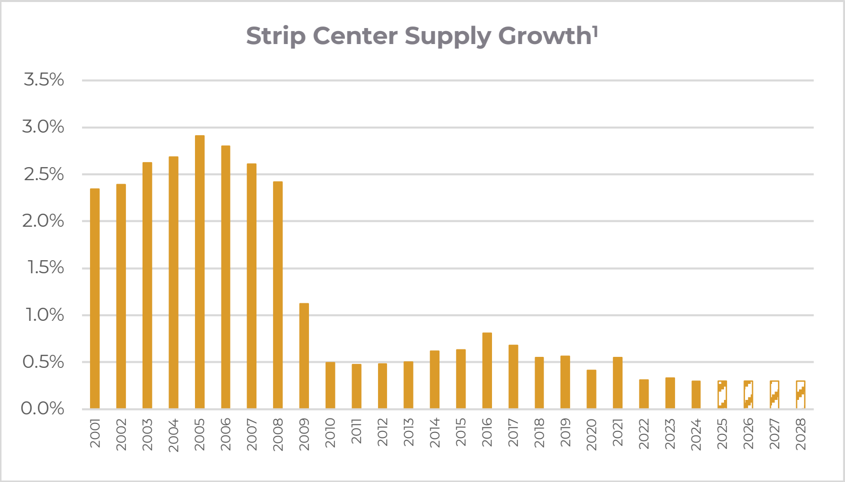
At ZRP, we have invested in commercial retail properties (primarily strip centers) for 32 years and produced attractive returns driven by our value-add strategy that utilizes in-house leasing and property management teams.

While our retail investment strategy hasn't changed, market fundamentals and the investment opportunity for strip retail have, and in a very positive way. **For the first time in our history, we are seeing a material undersupply of strip retail space which, coupled with robust demand from tenants, is producing high occupancy and strong rent growth.** This undersupply is expected to persist, making this an opportune time to increase exposure to this asset type.

Our investment thesis is underpinned by five key fundamental factors:

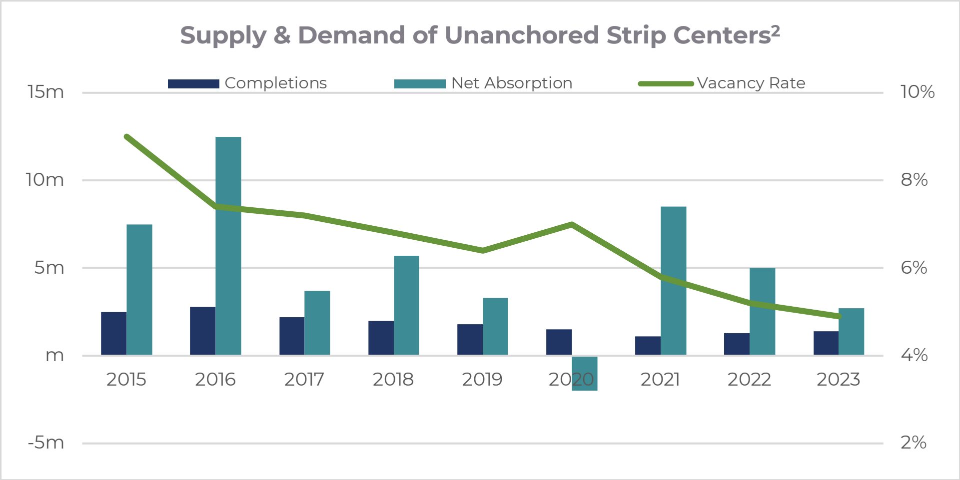
1. **Limited New Construction:** New construction of strip centers has stagnated at low levels for the past decade. Industry forecasts for new construction predict similarly low levels of new supply for the next four years, with industrial, multifamily, and office all expected to see greater annual supply growth than strip centers.



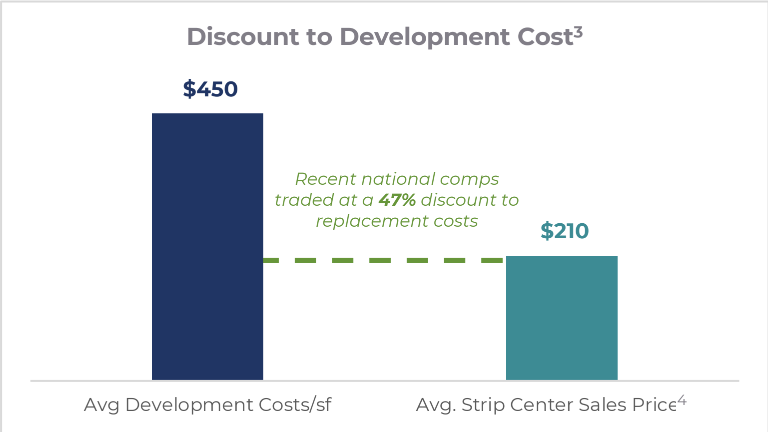


[1]Green Street Strip Center Insights "Drawing the Line – Where and When New Developments Pencil". July 2024.

2. **Stable and Growing Demand:** Demand for strip center retail space continues to grow for several reasons. First, as e-commerce grew over the last decade, strip center tenants evolved away from selling physical goods to providing necessity-based services that consumers need locally. Over 50% of tenants in ZRP's retail centers are now service providers (dentists, vets & doggy daycare, yoga studios, restaurants, and nail & hair salons). Second, despite rapid e-commerce growth many digital-first brands are turning to brick-and-mortar stores to facilitate an immersive brand experience and reach consumer segments they are missing in ecommerce channels, with notable store footprint expansions from direct to consumer ("DTC") brands like Allbirds, Warby Parker, Buck Mason, and Marine Layer. Coupled with many years of undersupply, these demand tailwinds have driven vacancies to record lows, producing double-digit rent growth for renewals and new leases.

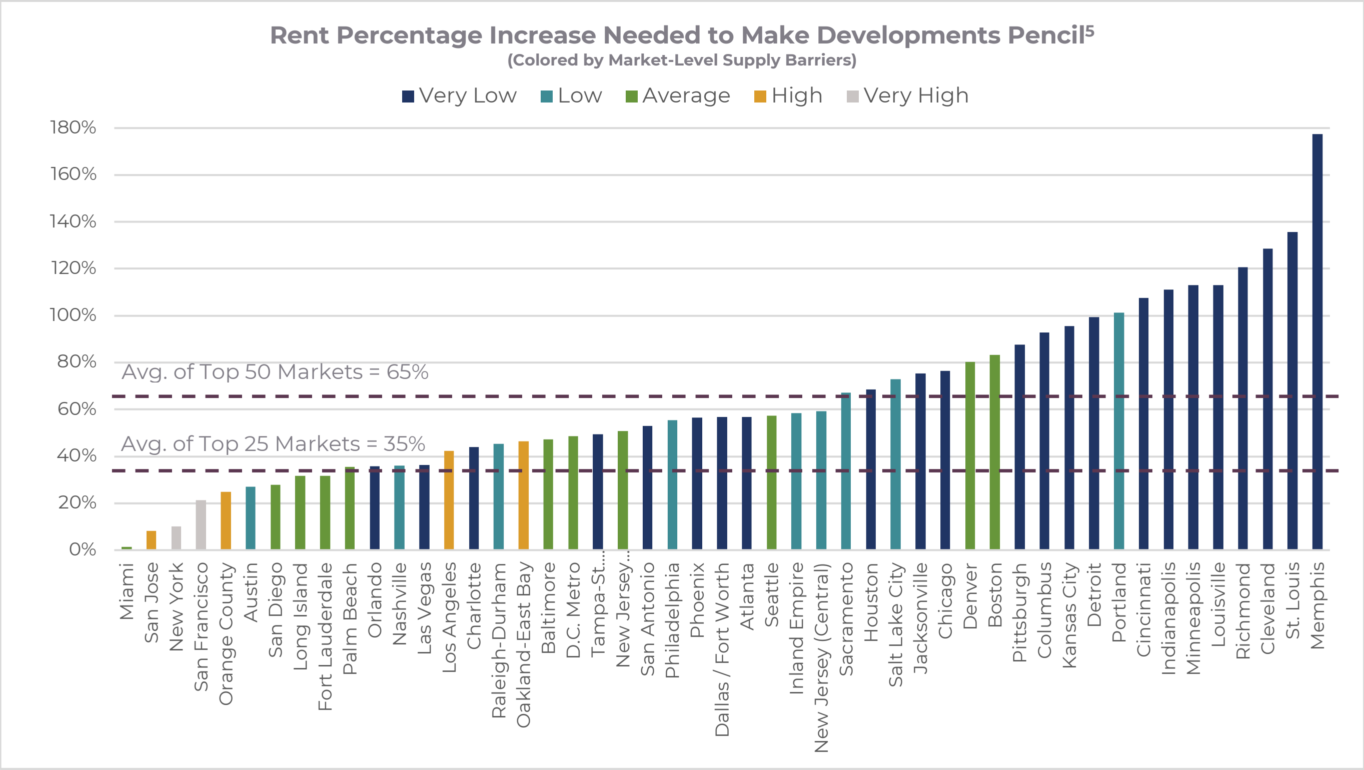


3. **Elevated Development Cost:** While this level of undersupply is usually met with new construction, the current costs of land, impact fees, material & labor costs, and other development fees make it prohibitively expensive to build profitable new retail centers at current rents. Additionally, the current capital market conditions and rate environment add financing challenges to new development. The graph below illustrates the significant purchase discount for existing centers compared to the cost of new builds.



[2]Marcus & Millichap "Strip Centers' Unique Service Offerings Stand Out in Current Retail Landscape". April 2024.
[3]Green Street Strip Center Insights "Drawing the Line – Where and When New Developments Pencil". July 2024.
[4]Based on Green Street's Sales Comps database. Average price per square foot for all neighborhood, community and power center transactions year-to-date.

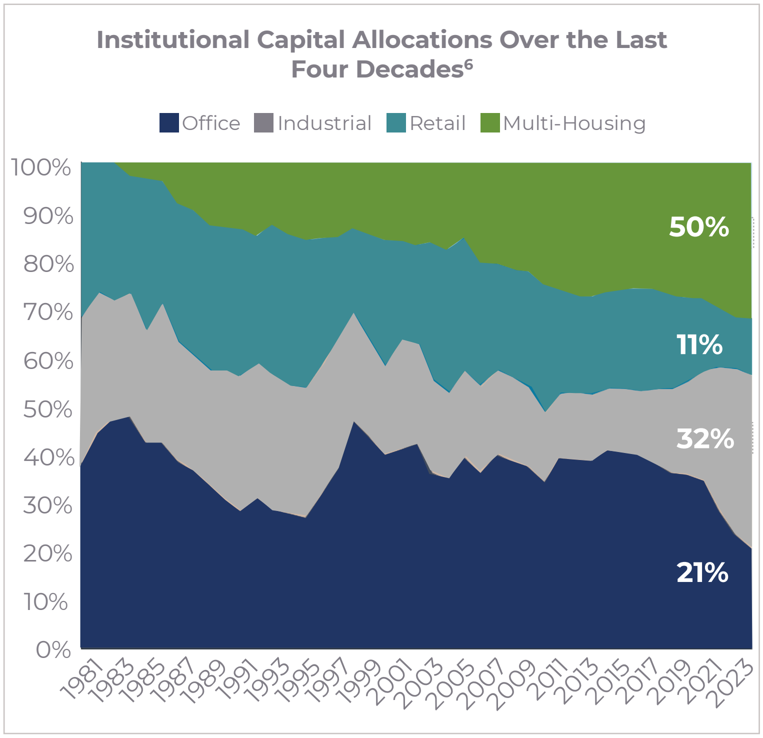
Furthermore, the next graph shows how much rents would need to increase in order to turn a profit on new retail construction across various markets. As you can see, in ZRP's core sunbelt markets, existing rents would need to climb by 35-80%, creating a significant barrier to new supply. This level of rent growth will take time, reinforcing forecasts of minimal new supply for the foreseeable future. In the meantime, we expect rent growth to continue to materially outpace inflation.

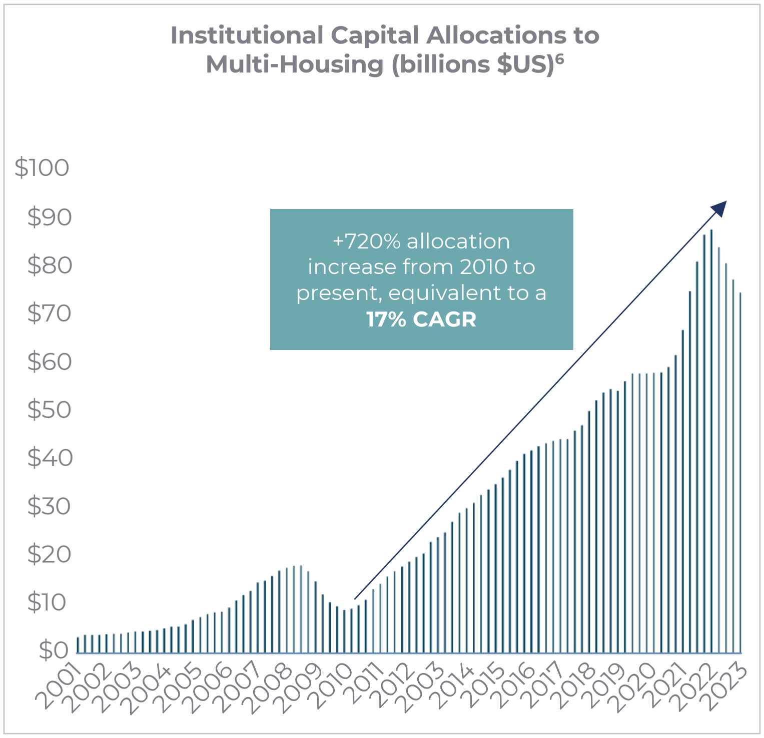


4. **Attractive Relative Value:** Despite these strong fundamentals, strip centers continue to trade relatively cheaply compared to sectors like multi-family and industrial. We are seeing the opportunity to acquire retail centers with below-market rents and the opportunity to drive NOI higher as rents are brought to current market levels at going in cap rates of 7%+. This compares to multi-family and industrial properties trading in the low 5% cap rate range, despite record new supply and softening rents, a direct contrast to the strip center opportunity as we see it today. In addition to the opportunity to add value through occupancy and rent growth, there may be an opportunity to increase property values should retail cap rates compress modestly towards the level of multi-family and industrial properties as institutional investors become more focused on the compelling opportunity in retail.

[5]Green Street Strip Center Insights "Drawing the Line – Where and When New Developments Pencil". July 2024

5. **Complex & Misunderstood Asset Class:** As shown below, large institutions have been increasing their allocations to multi-family and industrial for years, while investments in retail are at a 40-year low. These institutions are now actively seeking teams to deploy capital in strip retail, as they lack the in-house talent to lease and manage diversified pools of small business tenants, which comes with greater complexity than managing homogenous assets such as apartments and industrial. There are very few teams that match ZRP's vertically integrated capabilities and long-term track record, positioning ZRP well to take advantage of this opportunity.





In closing, we feel the risk-adjusted returns available in strip retail are compelling. The fundamental tailwinds of limited supply, rising demand, high occupancy, rent growth and possible cap rate compression provide downside protection and room for upside in our return forecasts for the next five years and beyond.

Our acquisition team is actively building a pipeline of potential investments, and we hope to present you with several opportunities in the coming months. As always, our internal partners will be among the largest investors and expect to commit 25% or more of the equity offered for each transaction.

In the meantime, we would be happy to schedule a call if you have questions or would like to speak further about our retail investment thesis.

Curt Schade & Tim Walter

[6] JLL "US Multi-Housing Capital Markets Overview." June 2024.

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