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Outsource Me

By Corey Bialow

May 1, 2006 12:00 PM

Outsourcing has landed.

National retail chains are hiring outside consultants and brokers to provide the services typically performed by internal real estate managers. It's even becoming commonplace to see a consulting company or so-called "master real estate broker" manage a retailer's entire growth.

Primarily, new high-growth national retail chains such as T-Mobile, The Vitamin Shoppe, Starbucks, Trader Joe's, Baja Fresh, etc. account for the shift toward outsourcing.

Small local retailers are embarking on regional or national rollouts as soon as they achieve even a moderate level of success within their local markets. And, for this, they increasingly are turning to outside firms to shoulder their expansion programs.

In the past, large retailers (Gap, Toys 'R'Us, Kmart, etc.) were most aggressive in implementing a national expansion plan. Doing so typically meant building an internal real estate department with regional offices throughout the country. A department would have a full staff of experienced leasing managers overseen by a senior-level executive. The cost of operating and maintaining these departments can become a significant line item in any growth retailer's G&A.

Money in the pocket

An outside consulting firm replaces that layer of personnel, field offices and overall training to yield significant savings for its client.

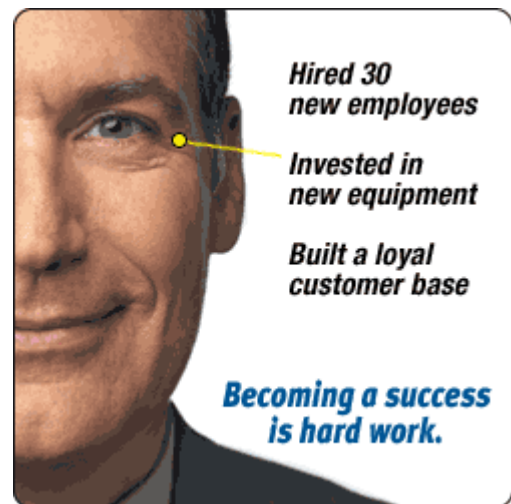
There are two ways that retailers have structured hiring outside consultants. In most instances the landlord is responsible for payment of a brokerage commission, which becomes the sole compensation to the outside consultant or broker.

In rare instances, such as with transactions inside the regional malls, the retailer typically compensates the broker from its end. The concept of brokerage fees being paid is not new; what has changed is the fee structure.

The development community has embraced the idea of paying larger brokerage fees (usually percentage based) because of the number of retailers that now have exclusive representation.

The larger sized boxes and aggressively growing retail chains can often get an outside consultant or master broker to take an assignment on a no-fee basis to the retailer and accept the brokerage fee as their total compensation.

This scenario is more common with non-mall retailers as most major mall owners are not inclined to pay brokerage



fees. In this instance a flat fee per transaction or a monthly retainer are common methods of payment by the retailer.

This results in cost savings over time, compared with traditional methods of payment for internal employees whose compensation is fixed regardless of annual fluctuations that may occur within a company's growth strategy.

A flexible alternative

Outsourcing also provides flexibility for companies that often see tremendous swings in their growth patterns. It is extremely difficult for most retail chains to project a growth budget beyond a two- or three-year window. Internal variables include sales, profits, mergers and acquisitions, while outside a company, availabilities in the marketplace, rent fluctuations and competition could accelerate or halt an expansion program.

Such dramatic shifts, which usually take place with little advance notice, can create long periods when internal real estate department are either understaffed or overstaffed.

The greatest competitive advantage of outsourcing is that retailers can leverage a consultant's knowledge, experience and relationships within the real estate community. This is especially true for smaller chains looking to expand into new markets where they may be virtually unknown entities.

The marketplace is controlled increasingly by a small group of large companies. The top 10 retail real estate firms in the U.S. own or control more than 1 billion square feet of retail space.

As public sector and private equity markets take advantage of historically low interest rates, an unprecedented rise in acquisitions and mergers in the shopping center industry will only serve to strengthen this consolidation.

Therefore, it has become more important than ever to have existing relationships with the largest retail developers, owners and management companies to successfully execute a national expansion program.

A retailer with no presence in a market and no brand awareness can instantly gain credibility by hiring the right broker or consultant that already has these relationships in place.

Master of all trades

There are many retail consulting companies that are able to provide additional services beyond that of a typical local broker.

Consultants can assist with all phases of a project: site selection, market analysis, lease negotiations, store planning/design, permitting and construction. During high-growth periods, many retailers will also temporarily utilize consultants for lease renewals, relocations, dispositions and facilities management according a fee-based structure.

Outsourcing a retailer's real estate needs does not always involve replacing an internal real estate team. Many national retail chains have embraced the "master broker" who can work alongside the vice president or the director of real estate.

One of the most difficult aspects of running a real estate department is selecting a local brokerage firm that suits one's needs, and then motivating the broker to work on a specific account.

A top broker in a particular geographic region will be in high demand from many competing retailers.

By bringing multiple customers to the table, a master broker is able to leverage its own business dealings with the top brokerage firms in each retail market.

Competitive advantage and better service ultimately flows down to the retail chain that hires that master broker.

Katz & Associates is a national consulting firm that only had about 5 or 6 clients 10 years ago; Now it has more than 50 retail clients.

The master broker also provides an internal real estate executive with a single point of contact rather than having to be in touch with dozens of regional brokers.

Retailers such as new venture capital startups that lack the internal strength of a full real estate department will emulate other chains such as Barnes & Noble, Circuit City, PetSmart, Hollywood Video, Starbucks and Cheesecake Factory. that have successfully relied on outside real estate consultants and master brokers.

For all these reasons, I believe the trend toward outsourcing will continue to grow for some time to come.

Bialow is founder and CEO of Bialow Real Estate, LLC. He was real estate vice president for The Vitamin Shoppe.

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