

Macy's closure to complicate mortgage concerns for CityPlace West Palm Beach

The **Related Cos.** was already facing a considerable challenge at its CityPlace urban retail center in West Palm Beach to restructure its \$150 million mortgage and the recently announced closure of its Macy's could make the situation even tougher.

Macy's is the largest tenant at CityPlace with 110,000 square feet of the 698,472-square-foot center, according to Trepp LLC, which monitors securitized mortgages. The retailer announced that it **would close the store by the end of 2017**. It has 72 employees.



The prospects for finding another tenant to fill 110,000 square feet aren't many, said **Katy Welsh**, a Colliers International South Florida retail broker in West Palm Beach. Most big-box retailers suffered a sharp decrease in sales during the holiday season. A sports retailer, like Dick's Sporting Goods, might be interested in the location, but that would probably require subdividing the space and finding a second tenant, she said.

“We have been in talks with Macy's about their plans to close their store at CityPlace, as a part of a broader initiative to close a portion of their stores around the country,” CityPlace's management stated. “Our goal is to not only bring a dynamic new use to this important location, but also ensure that the job base and

economic contributions to the city and region are preserved or enhanced.”

The Related Cos. is owned by **Stephen Ross**, the billionaire proprietor of the **Miami Dolphins**. It developed the complex at 700 S. Rosemary Avenue in 2000 with a ground lease from the city.

In February 2016, the \$150 million mortgage on CityPlace – broken down into a \$100 million “A note” and a \$50 million “B note” – was **placed into special servicing** by its commercial mortgage-backed securities (CMBS) trust for “imminent default,” according to **Trepp LLC**. The borrower missed several payments from March through September 2016, but made a payment in October and was 30 days past due for a payment as of late November, according to Trepp LLC.

The property was appraised at \$108.2 million in July 2016, according to Trepp. That’s significantly below its \$150 million mortgage. Its last appraisal was for \$143 million in 2011.

The borrower’s 2016 budget for CityPlace called for \$5.8 million of net operating income on revenue of \$22.7 million, according to Trepp. It was 94 percent occupied as of July 2016, up from 89 percent in October 2015.

The November report from Trepp said the **Related Cos.** made a loan modification proposal for CityPlace that the special servicer, C-III Asset Management, is reviewing it. The lender has not filed litigation against the borrower.

The Related Cos. is the best possible operator for CityPlace and no lender could do a better job managing the property, said **Ezra Katz**, CEO of Miami-based real estate firm **Aztec Group**. It would be better for the lender to work out its differences with the Related Cos. and let the developer solve the problem. Katz would expect the Related Cos. to stick with CityPlace, even if the prospects for making a profit are dim, because Ross’ company has a strong reputation to uphold.

The Related Cos. might have to put more capital into the property to position the Macy’s space for a new tenant, Katz added. That’s complicated by the fact that CityPlace appraised for less than the mortgage. The investors in the CMBS with the most risky position in this loan should write it off immediately, Katz said.

“This has the makings of a much bigger problem if it’s not handled correctly, particularly because of Macy’s decision to vacate,” Katz said.

The \$100 million “A note” carries a 6.27 percent interest rate but the \$50 million “B note” carries no interest. That loan was split in two and modified in 2012 after a previous stint in special servicing.

Under that modification deal, the interest rate on the “A note” jumped from 2.88 percent to 6.27 percent in January 2015, which significantly increased the monthly payments.

Both notes mature on Dec. 15, 2018, so a maturity extension might be in order too.

One of the biggest problems with the CityPlace mortgage are the expectations for the property when it was made in 2006. Back then, the property had net operating income of \$9.3 million but the loan was underwritten assuming its net operating income would climb to \$12.3 million thanks to higher rents so it could support higher mortgage payments, according to Trepp. CityPlace hasn't come close to those numbers.

It's not immediately clear what financial impact the Macy's closure would have on CityPlace. Trepp found that the lease doesn't mature until January 2026, but that document doesn't say whether Macy's would have to continue paying the lease should it close the store.

The closure of Macy's shouldn't hurt business at the other CityPlace retailers because they didn't have much cross traffic with the department store, said **Neil Merin**, chairman of West Palm Beach-based brokerage NAI/Merin Hunter Codman.

CityPlace was one of the first open-air retail centers in Florida when it was developed in 2000, starting what has become a trend in the state, Merin said. The Macy's was smaller than the typical department store because the idea was to focus on a mix of smaller retailers there, he said.

Most people who drive to CityPlace from the suburbs already live near a Macy's, so that's not what draws them to the property, Merin said.

“I enjoyed going there and it was convenient to go grab something,” said Welsh, a downtown West Palm Beach resident. “It will be missed. Obviously, they didn't have the sales they needed.”

CityPlace has shifted strategies several times. It started with a focus on national-brand retail, then added more furniture stores, but the housing recession hurt furniture sales. Then competition from the new Palm Beach Outlets just north of downtown drew many shoppers away from CityPlace.

“I like CityPlace a lot, however, many of the stores in CityPlace struggle,” Welsh said. “A lot of the stores moved out and went to the outlet mall.”

More recently, CityPlace has focused on entertainment with a movie theater, bowling, restaurants and a nightclub, Welsh said.

Related Cos. is building a larger store for Restoration Hardware in the median of Okeechobee Boulevard at CityPlace, although that property is not part of the CMBS loan. Welsh noted that the Restoration Hardware would include a restaurant, keeping with CityPlace's entertainment theme.

Losing Macy's could be an opportunity for the Related Cos. to reposition its space, Merin said. It could break it up for smaller tenants, create a collaborative workspace for a firm such as WeWork, or tear in down in favor of an apartment building or an office building, he said. All of those users are in more demand than big box retail.

The good news is downtown West Palm Beach's population has continued growing and there are a handful of residential towers under construction. Welsh said the city's demographics should be attractive to retailers to fill Macy's old space.