

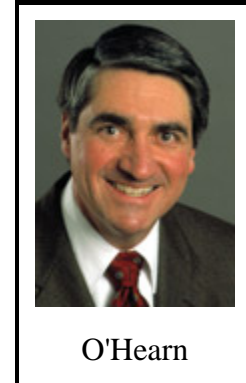
WHEN THE WHEELS COME OFF

After the sea change in Detroit, what should western cities, owners do with shuttered automobile dealerships?

Ned O'Hearn

With seismic rumblings from cracks in the nation's banking industry still being felt throughout commercial real estate, the shuttering of a vast number of big automobile dealerships is adding more woes to the West's troubled economy. Cities and investors hit hardest by the aftershocks are those clawing to preserve the traditional linear "motor mile" — dealership upon dealership along once-busy urban thoroughfares.

The impacts and challenges are widespread. Municipalities are losing bundles of much-needed sales tax revenue. Owners are left with shallow asphalt-fronted properties and hard-to-convert showroom space. Would-be developers are hamstrung by cities fiercely reluctant to rezone tax-producing commercial land. Brokers are vying to peddle properties in markets where product scarcity is hardly a viable selling point.



These once prosperous retail stretches were initially victimized in the mid-1990s by the appearance, then proliferation of mega auto malls. Scrambling for sales tax dollars, some municipalities used vacant land and ample slush funds to lure a new breed of auto mall developer, which then pirated dealerships from companion cities. Many cities withstood the initial onslaught — sort of — peppering dealerships with incentives to stay while appealing to community pride. Dealerships have traditionally been known for their civic spirit, from posting banners at local charity events to brandishing their names across little league uniforms.

The new wave of location-indiscriminate dealership closings — impacting the pirates as well as the pirated — can be traced to shifting product preferences based partly on the going price of gasoline, sharply reduced consumer spending in a staggering economy and, most recently, draconian manufacturer restructuring programs.

The aftershocks of the closings are most discernibly being felt in statehouses and city halls where legislators, city councils and finance directors are struggling to balance budgets. "The loss of so many dealerships has had severe detrimental impacts on our budget," laments Scottsdale, Arizona, mayor Jim Lane. He isn't alone. "Losing three dealerships erased over \$600,000 in sales tax revenue," adds Jeff Collier, Whittier, California's Community Development Director. "They represented critical sources of revenue and were integral parts of the local business community."

Similar consequences are reported throughout California. Auto-related sales taxes in Poway, located northeast of San Diego, once covered 11 percent of the operating budget. "We lost two of our nine dealerships in May 2008 without notice, and a Chevy operator has subsequently gone bankrupt," notes Dene Fuentes, director of redevelopment

services. “The sales tax implications are significant, as has been the visible toll of having three vacant dealerships on our commercial corridor.”

Besides trimming budgets with chain-saw precision, city officials are vigorously — and sometimes creatively — trying to retain the dealerships they still have. Whittier, for example, has temporarily slashed zoning application and building permit fees by 50 percent. “The intent,” says Collier, “is to urge owners to make improvements deferred because of limited funds.” The city has also reduced banner permit fees and slackened restrictions on banner usage, which should please dealership owners typically fond of ostentatious displays.

Its most controversial move was allowing used-car sales on existing dealership sites for a fixed 2-year period. “The city viewed this as an opportunity to help long-standing auto dealers, providing them an interim revenue stream while transitioning their property to a new use,” explains Collier.

Not many prideful cities suffocating financially from the loss of new car dealerships are anxious to pursue that course, even temporarily. Some, like San Jose, California, are content to wait out the storm, anticipating the appearance of sparkling replacement dealerships. “We’ve experienced a 30 percent drop in auto-related sales tax receipts,” observes Nanci Klein, the city’s director of corporate outreach. “But we maintain a strong critical mass of dealers. We can be patient.”

San Jose and Poway might enjoy characteristics conducive to the return of new car dealerships, but such optimism isn’t widespread. “Like the department store on Main Street, high-end dealerships on Motor Miles simply won’t be coming back,” asserts Aaron Gruen, a principal consultant at Gruen & Gruen + Associates. “Those sales taxes are gone for good.”

Gruen also doesn’t regard struggling municipalities as innocent victims of shifting economic winds. “Not only did they contribute to oversupply by freely subsidizing enterprises such as movie theater complexes and auto malls, but their regulatory rules and restrictions have hampered business success and are now constricting redevelopment initiatives.” He cites Scottsdale’s deep setback and landscaping requirements as but one example. “The dealers, of course, would like those trees to die so passersby could see their cars!”

Mike Pacheco, real estate director for The Van Tuyl Group, the nation’s largest privately-owned dealership group, heartily agrees. “The recession is simply the straw that broke the camel’s back,” he asserts, noting that some dealership sites have been doomed for years due to shifting demographics and brand preferences. “The downturn merely accelerated the inevitable.”

Not to say the recession hasn’t had its impact. “New car sales in the Phoenix market are down 50 percent,” reports Pacheco. “Nationally, we’ve been compelled to eliminate up to 2,000 jobs, mostly commissioned personnel. We’ve also modified our marketing and

networking programs and instituted an aggressive cost-awareness program. You count paper clips in tough times.”

Tough times don't necessarily translate into dealership site fire sales. Van Tuyl voluntarily closed two dealerships earlier this year in San Juan Capistrano, California. “There's value in these sites in a recovered market,” says Pacheco. “They really aren't suitable for a big box user, but a mini-box might work, and would come closest to letting us recapture our investment.”

That brings up the size issue. Older dealership sites are typically three to five acres in size, but feature more frontage and less depth. “The old sites zig when they need to zag,” quips Pacheco. “Without additional land assembly, many uses are eliminated, including big boxes.”

Land prices are another impediment to creative reuse. In the hierarchy of spending power, no one could outbid an investor with a dealership use. The high price paid, coupled with years of collecting above-market rents, provides little incentive for all but distressed owners to sell or re-lease for less income.

Gruen doesn't envision municipalities playing the overseer's role in the recovery process. “What they can do,” Gruen suggests, “is create an environment for success. With small lines at permit counters, cities now have time to rethink their redevelopment strategies, focusing on complementary and compatible uses.”

Gruen sees Scottsdale's McDowell Road Motor Mile as a case in point. “Let's face it, the famed motor mile is one long, dull corridor — multiple big dealership sites interspersed with numerous small lots.” The departure or closing of several dealerships has the city — and property owners — scrambling for redevelopment ideas. Gruen suggests encouraging a variety of interesting nodes at critical intersections with appropriate linkages. “But higher density alone isn't a solution to the land cost issue,” Gruen warns. “Decked parking costs, for example, can easily offset rent gains associated with bigger, taller buildings.”

One of those owners is Virginia Korte, a high-profile local who has served as head of Scottsdale's Chamber of Commerce. “We must look at creative reuses, something sustainable that will also enhance the community.” Yet, Korte can't envision unguided market forces getting that job done. “It's going to take proactive government participation — removing regulatory obstacles, providing incentives and linking into light rail.”

In Whittier, land-use gaps created by the departure of dealerships provide an opportunity for retailers. “We have buying power in the heart of our city, but retailers have been pushed to the outskirts by site scarcity,” Collier observes. Korte sees few such opportunities for her family's site or other dealership landowners. “The retail market is already fully absorbed,” she says. “We have to think bigger.”

Brokers spend less time thinking big and more time focused on land fundamentals. “Dealership sites with strong retail characteristics will eventually find a re-use,” insists Tony Villasenor of Voit Real Estate Services in San Diego. “This means flat land, good frontage, high visibility, strong signage and easy access.” He notes though that buyers aren’t standing in line. “Asking prices are absolutely too high for today’s market,” he says, adding that owners are understandably reluctant to approve tenants offering one-third of what the auto dealers paid in rent. He’s also quick to point out that few deals will be made until the current lending freeze thaws considerably. “Even if a site is perfect for a hotel,” he says, “there’s zero opportunity to get a loan.”

Deals can be made, however, when the owner is willing to concede on price. “A property on the 50-yard line might trade at a discount today, but it will trade,” suggests Grant Traub, a senior broker with Colliers International in Las Vegas. “At the end of the day, the quality sites will move and the others will sit.” That might be true, but, throughout the West, there are plenty of owners and municipalities hoping to beat those odds.

Ned O’Hearn is manager, client services, for Boulders Realty Advisors in Scottsdale, Arizona. www.bouldersrealtyadvisors.com