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Photo courtesy of Arthur Levy

Retail Growth Explodes in Metro Denver

Kimberly D. Campbell

Is there a better time to be a consumer in Colorado than right now? Spurred by a well-educated workforce, diverse employment base, business-friendly environment, and robust housing market, new-to-market retailers are flocking to the greater Denver area. Both Scandinavian furniture retailer IKEA and Swedish apparel retailer H&M entered the market in 2011. Last year, J. Crew Group, Inc. brought its fashion-forward collegiate Madewell brand to Denver and opened a third location last summer in Boulder at Twenty Ninth Street. This year, outdoor outfitter Cabela's bookended the market with new prototype stores in Thornton and Lone Tree. Limited Brands opened their first stand-alone PINK concept at FlatIron Crossing, and book and tech reseller 2nd & Charles found its first Front Range home at FlatIron Crossing in a recycled Border's location. Trader Joe's will show Coloradans some love when they open stores in Denver and Boulder on Valentine's Day 2014. They have also announced a site in Fort Collins.

Denver and Boulder have been havens to healthy restaurant fare, prompting expansion from regional concept True Food Kitchen, which opened in the Cherry Creek North district, and vegan fast casual chain Native Foods Café, which opened at Twenty Ninth Street. Chicago-based Protein Bar will open three locations in 2014, including one at Twenty Ninth Street.

The healthy eating and farm-to-table trend is also evident in the grocery sector and has created opportunities for shopping center owners to fill vacancies. Boulder boutique grocer Lucky Markets expanded into Longmont last August, Whole Foods has announced a new Longmont location at the former Twin Peaks Mall, and even Walmart has entered the fray with their Neighborhood Market concept tailored specifically to Boulder consumers, revitalizing space at Diagonal Plaza.

Encouraged by rising home sales and new home development (approximately 2,000 new home units are in process in the City and County of Broomfield alone), Houston-based home décor superstore Garden Ridge recently opened in a former Broomfield Target

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Consumer Ratings: Fact or Fiction

From the Editor

The retail sector in Colorado accounts for more than 1 out of every 10 employees in the state of Colorado, and impacts every business and citizen directly or indirectly. The sector is a catalyst for the exchange of goods, facilitating the purchase of everything from cars to corn. The retail sector is rapidly transforming, with the use of information technology broadening the sales landscape to include e-commerce; educating consumers on products, prices, and quality; and informing sellers about their customers using sophisticated analytics.

Retail sales in Colorado have fully rebounded from the recession, and retail employment is projected to reach a new peak in 2014. This issue provides insight into some of the specific subsectors and growth within the retail industry, and discusses some of the dynamic changes within the industry ranging from information to delivery.

Please contact me at 303-492-1147 with questions or comments.

Richard Wobbekind

Bart de Langhe, a marketing professor at the University of Colorado Boulder, sat down with Brian Lewandowski, research associate with the Business Research Division, to discuss what online product ratings reveal about product quality.

Bart de Langhe

Q: Over the years, how has online retailing changed consumer behavior?

A: Consumers have a desire for instant gratification and that is exactly what online retailers such as Amazon.com provide. Yes, most often consumers need to wait a few days for their package to arrive but the transaction can be completed immediately, 7 days a week, 24 hours a day. This implies that the consumer has full control over the timing of the transaction. Moreover, based on product ratings that are posted online, prospective consumers believe they have close to perfect information about product quality. This reassures them that there is no need to postpone their purchase and that it is OK to buy that product now.

Q: Do you believe that online reports and websites give an accurate indication of product quality?

A: In general, consumers tend to believe the information given in these reports. They trust these ratings as much as recommendations from family and friends. However, there are several reasons why consumers should be cautious when using these ratings. First, businesses are well aware of the effects of online ratings on sales. Research shows that a one-star increase in a restaurant's rating on Yelp.com leads to a sales increase of 5–9% and a 19% increase in the likelihood of selling out tables during rush hour. This creates a strong incentive for managers to post positive fake reviews for their own offerings and negative fake reviews for the offerings of competitors. Recent academic research suggests that 5–10% of reviews are fake. Second, there is a silent majority of consumers who feel indifferent about a product and do not feel the urge to rate products online. There is also a vocal minority of consumers who absolutely love or hate a product. The opinion of these consumers is overrepresented online. Third, there are strong herding effects. The first rating for a product is crucial to success as other raters are influenced by it. Finally, in my own research with Philip Fernbach and Donald Lichtenstein, we have directly compared online ratings from Amazon.com with a more objective measure of quality and found that the relationship is weak at best.

Q: What specifically do you mean by a weak relationship between consumer ratings and "objective quality"?

A: Let me give you an example. I was recently looking to buy a booster seat for my daughter and as many consumers do, I went to Amazon.com. Two car seats grabbed my attention. One had a high price ($299) and a high rating (4.64), the other a substantially lower price ($50) but also a much lower rating (3.76). Now, I am also a subscriber to *Consumer Reports*. Experts from *Consumer Reports* had tested these two car seats on crash protection and ease of use, arguably the two dimensions that young parents care most about. It turns out that experts gave the less expensive car seat with the lower rating on Amazon the highest quality rating. They rated the expensive one, on the other hand, as second-worst. This led us to do a more systematic analysis of many brands across different product categories. We found that on average when one brand is rated higher than another brand on Amazon.com, more than 40% of the time the other brand is better quality.

Q: What is reflected in online ratings then?

A: Online ratings are heavily influenced by marketing variables. These are variables that are not intrinsic to the product, like price or brand name. Although consumers believe that more expensive products get lower ratings, price actually has a positive effect on ratings. This means that on sites like Amazon, consumers tend to rate expensive products better. This effect can probably be traced to a cognitive process that psychologists refer to as "motivated reasoning." When people pay a high price to acquire a product, they have a tendency to engage in an internal justification process: "I paid a high price, so I must really like this product." We have done many studies in our lab showing that consumers are unable to form unbiased evaluations of product quality, even after experience with the product.

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RETAIL GROWTH EXPLODES, CONTINUED FROM PAGE 1

location. Conn's, Inc., a regional specialty retailer of electronics, and furniture, lawn and garden products, is slated to open its first Colorado store in 2014 in a former HomeBase location in Arvada. Conn's has also leased a 246,000-square-foot distribution center near Aurora with plans to open up to eight more stores in the region.

In this environment of high demand for retail space and scarcity in some pockets of the market like Boulder, shopping center owners are afforded opportunities to add value to their real estate, converting former big box space to other uses, replacing underperformers and right-sizing retailers who desire more or less space. For example, at FlatIron Crossing last year, Eddie Bauer relocated, downsized, and built its new prototype, giving Macerich the opportunity to create 18,000 contiguous square feet for consumer darling H&M. A former Border's location at Twenty Ninth Street was split into two spaces and is now home to SA Elite, Sports Authority's high-end apparel and shoe brand, and office space for high-tech company Ligit Networks, Inc.

Photos courtesy of David Budd

The strength of the local retail real estate sector is evidenced by vacancy and rental rates: in Q3 2013 Denver's retail vacancy rate was 7.6% and Boulder's was a mere 5.7%. Average retail rent in Denver increased 0.45% over last year, to $15.60 per square foot NNN (triple net: base rent plus pro rata share of common area maintenance, real estate taxes, and insurance). Fueled by high demand, Boulder commands some of the highest rents in the metro area, at $19.50 per square foot NNN on average (CBRE Denver Retail MarketView Q3 2013).

This landlord's market is also resulting in significant investment by both private developers and municipalities. Two current examples of large redevelopment projects are Foothills Mall in Fort Collins and Twin Peaks Mall in Longmont. Alberta Development Partners plans to spend $313 million on Foothills Mall, which will include 658,000 square feet of retail space and about 500 apartments. It is hoped that the City of Fort Collins will vote to approve a $53 million financing agreement in December. NewMark Merrill plans an $80 million redevelopment of Twin Peaks Mall with a contribution of $27.5 million in municipal bonding for infrastructure from the City of Longmont. Litigation with Dillard's has slowed the project, which is expected to house Sam's Club, Whole Foods, and a renovated movie theater.

Despite natural disasters and the recent antics of our politicians in Washington, retail sales continue to grow: up 4.2% year-to-date nationally in October (U.S. Department of Commerce data). (While Colorado sales data are not available beyond Q2, local sales have trended higher than national sales.) Our shopping and dining choices are plentiful in the metro-Denver and Boulder markets. As long as consumer confidence continues to be strong, fueling retail sales growth, we can expect a continued retail real estate boom and more choices for local consumers.

Kimberly D. Campbell is Senior Manager, Property Management for Macerich, a Santa Monica-based public Real Estate Investment Trust (REIT). She is responsible for the operations of FlatIron Crossing in Broomfield and Twenty Ninth Street in Boulder. She may be reached at kim.campbell@macerich.com.

Technology and the Relocalization of Food Retail

Chad Arnold

Chad Arnold

Online retail growth continues thrive in the United States. Forrester Research has reported that e-commerce growth is outpacing total retail sales growth by more than 10% and that 46% of total U.S. retail sales were either transacted directly or influenced by Internet research on PCs, smartphones, and tablets. This technology-driven growth can be seen in both sales data and in consumer purchasing behavior influenced by technology and the 150 million (47.3%) of the country's population who will be regular mobile Internet users by the end of 2013 ("US Cross-Channel Retail Sales to Reach $1.8 Trillion by 2017," Forrester Research, October 29, 2013). While this shift to e-commerce has created significant disruption in most every major retail sector, one industry has lagged behind: food.

Historically speaking, food was an inherently local activity. Growers only produced what they could sell from a small shop, near where the food was crafted, and they spoke to their customers every day. Food that was grown or picked nearby had the best flavor, the most nutrients, and an assurance of safety provided by the grower directly to the consumer. As farming, retailing, and distribution became more consolidated, retail grocery has turned into a global business with national sales exceeding $602 billion in 2012. This consolidation drove selection up and prices down, and led to a focus on processed and shelf-stable products on the shelves, shifting the American diet. It also had the unintended consequence of separating the farmer/producer and the "eater." Small family farms began to disappear, reports of environmental issues began to increase, and the health of Americans decreased. These issues have created a demand for change in retail food

and Colorado's leadership in natural and organic food has thrived, along with a reemphasis on fresh, artisan, and local offerings.

While the food supply chain is now a very global enterprise, the dominance of the brick and mortar channel and the inherent efficiencies in local/regional supply chains continue to drive regionality in the retail food sector. In fact, food and beverage stores in Colorado recorded $15.2 billion, or 9.3% of all retail sales in the state (Colorado Retail Sales and Sales Tax Summaries, Calendar Year City and County Summaries, 2000—Current, Colorado Department of Revenue). While the development of e-commerce in other sectors has led to geographic consolidation, online grocery shopping may be a unique opportunity to leverage the inherent value and quality in local sourcing and distribution, thereby strengthening Colorado's position and the local economy.

As technology begins to play a larger role in the retail food business, new approaches and models are beginning to take shape. For models that specialize on fresh products, such as Door To Door Organics,

Photos courtesy of Door to Door Organics local sourcing is a priority. New technology empowers procurement and sourcing, enabling a high level of product tracking and a new frontier in product information, which helps consumers make more informed decisions. This model also creates a more direct marketing channel for producers and reduces transaction costs, thus enabling smaller, local farmers and producers to reach a larger audience. In turn, this strengthens local access and local demand, creating a virtuous cycle for the local economy.

Other approaches work, too. Alfalfa's, a small Boulder-based retailer, is driving local engagement through their social media efforts. Whole Foods drives a highly decentralized approach and is using its web presence to profile local producers through video and provide local sourcing maps.

Large traditional food retailers have also begun to embrace a more multichannel approach that includes e-commerce, and many of these efforts are leading with a natural, organic, and local approach. Safeway's online service, which has garnered the most headway among the traditional retailers, has developed a 3.2% share of the home delivery market according to market research firm IBISWorld, but it has limited presence in Colorado. Walmart is piloting its Walmart To Go e-commerce and delivery in the Denver area, while Kroger's HomeShop service delivers throughout Colorado. Finally, Amazon Fresh is now expanding service from its base in Seattle to Los Angeles and the San Francisco Bay Area, with rumors of a presence in Colorado.

The Hartman Group reports that 75% of consumers are now shopping online and 54% are using social media to discover new foods and share their food experiences. Forrester Research estimates that $15.4 billion was spent for food and beverages online in 2013. While online penetration in food retail is only around 1.2%, trial is growing, with Internet Retailer reporting that 12% of Internet users say they've bought grocery items online. Predictions about the growth in online food retail range from an annual growth rate of 10% to achieving a 17% share of the marketplace by 2023.

Colorado is well-positioned to take a leadership roll in this growing segment. Colorado is often rated as the fittest state in the nation. It has a long history of leadership in the retail food industry in everything from natural and organic retail, to consumer packaged goods, as well as farming and ranching. Colorado companies, such as Door to Door Organics, are bringing together food and technology to improve the consumer experience online, with products and services that drive engagement with food, highlighting quality and ultimately a more regional awareness. As the transition to online food occurs, driven by fresh artisan products, it brings with it a push for relocalization. If fresh,

high-quality food helps to lead the transition to online grocery, more economic activity is bound to stay at least within a region, if not within an individual state like Colorado.

Chad Arnold (Leeds School of Business MBA, 2007) is the president and CEO of Door to Door Organics, a Louisville, Colorado-based online grocer that partners with local farmers and artisan producers to deliver organic produce and natural groceries to homes, offices, and schools throughout Colorado and nine additional states. Under Arnold's leadership, Door to Door Organics has expanded operations to Illinois, Kansas/Missouri, Michigan, and Pennsylvania. In 2012, the company received a $3.25 million Series A round investment from Greenmont Capital and was awarded "Company of the Year" by Naturally Boulder.

A Summary of the Colorado Retail Industry

Rick Brubaker and Samuel McMeley

The Colorado retail industry has continued its moderate gains in both total retail sales and employment in 2013. The growth experienced this year was driven mostly by strong retail performance in Colorado's metropolitan areas, where retail numbers increased 4% from last year. In 2013, the retail trade sector recorded some of the largest employment growth in Colorado. The retail industry offers employment options from entry-level positions to upper-tier managerial positions. In 2013, the industry proved to be resilient during times of difficulty with regional preliminary numbers showing a much quicker recovery from the September flooding than expected. In 2014, statewide retail is expected to continue its growth, mostly from strong automobile sales and large retail chains opening new branches across the state. Newly legalized marijuana retail storefronts might add jobs and further growth to Colorado's retail industry, along with up to $67 million in tax revenues from Proposition AA, a ballot measure recently approved by Colorado voters in 2013 to provide additional taxation on retail marijuana sales. Retail marijuana's true impact on the Colorado retail industry remains largely speculative as the industry is in its infancy stages.

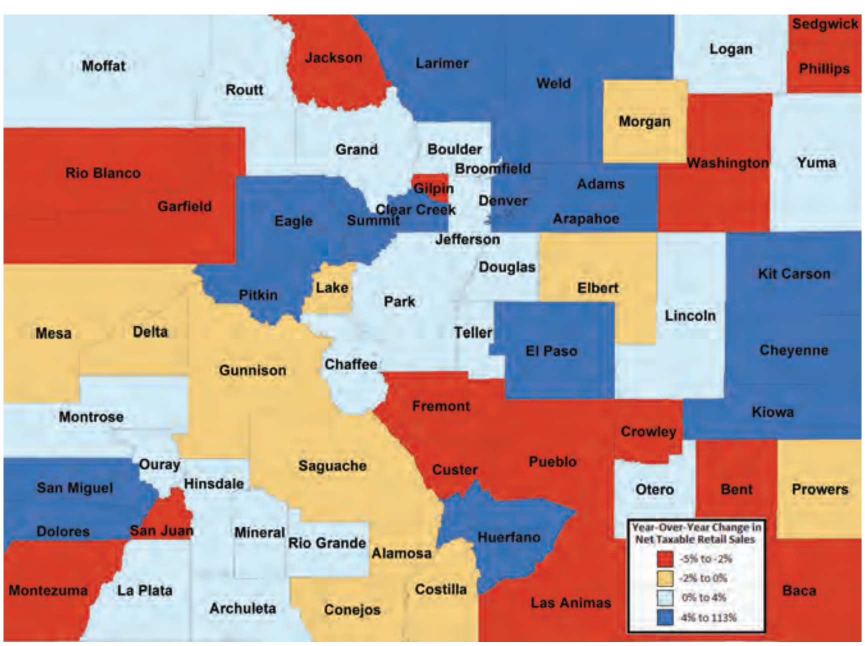
National retail sales increased 0.2% in August 2013 and 4.7% year-over-year. There was, however, a 5.1% monthly decline in unit sales of cars and trucks. Slow wage growth and continued high unemployment remain a constraint on consumer spending. Despite the slow national retail growth pattern, the retail sector in Colorado has continued its trend of moderate growth throughout 2013 with a 2.6% overall increase in employment since August 2012. The retail sector has experienced the fourth-largest employment growth of any sector in Colorado; it currently employs 249,000 people, or approximately 10.5% of Colorado's total workforce. This jump was largely centered in Denver but gains were also experienced in other metropolitan statistical areas (MSAs), notably Colorado Springs, Greeley, and Fort Collins-Loveland. Since August, Colorado has shown a statewide 5.4% increase in retail sales and a 4.3% increase in both state net taxable sales and state net sales tax revenue compared to the same period in 2012. The largest areas of growth within the retail sector for 2013 have been sporting goods and building materials.

These gains are centered exclusively in metropolitan areas. The rural counties of Colorado have experienced a 1% drop in year-to-date retail sales, net taxable sales, and net sales tax revenue when compared to the same period last year. On the contrary, Colorado's urban counties show a 4% year-to-date increase in retail sales in August, along with a 6% year-to-date jump in net taxable sales and net sales tax revenue. These changes occurred even when population differences were controlled for. Given that rural population increased by 2% in 2013 and urban population increased by 1%, the gain in retail sales cannot be accounted for by population change.

The worst of the September flooding occurred in the Front Range region of Colorado, specifically the areas around Boulder County. Catastrophe risk modeling performed by EQECAT estimates the total costs of the damages from the flooding in the state will exceed $2 billion. Retail expectations in the post-flood climate of these regions foresaw retail businesses suffering, perhaps even failing due to property damage and loss of business. However, this was not the case. Most businesses that took an initial hit the week after the flood showed remarkable resilience according to California-based retail analysis firm RetailNext. During that first week, shopper traffic in chain apparel and department stores was indeed 4% lower than the national average, but this drop was more than offset by shopper traffic rising 7% above the national average in the second week. Similarly, consumers spent 3% less than the national average in the first week after the flooding but during the following week Colorado consumers' spending was 4% higher than the national average. An exception to this back-and-forth trend can be found in hardware stores, which saw a constant increase in sales during the entire flood period.

Strong 2013 automobile sales point toward continued employment growth in the retail sector throughout 2014. New auto sales in the state saw

NET TAXABLE CHANGE IN RETAIL SALES IN RURAL COUNTIES VS. MSAs YEAR-OVER-YEAR CHANGE



4.5% year-over-year growth in the month of September according to a report by the Colorado Automobile Dealers Association. This is a continuation of the overall year-over-year growth of 12.5% observed in 2013 year-to-date. Colorado's year-over-year automobile sales exceed the national year-over-year sales of 11.2% in 2013 year-to-date, and as of September 30, a total of 130,166 new vehicles have been registered in Colorado. Blue Chip Economic Indicators forecasted in October a five-year average of 16.4 million units being sold in 2014–19 nationwide. The brand Dodge experienced a 51% increase in new unit sales in Colorado this year, the single-largest gain of the 25 automotive companies that saw increases in unit sales in 2013. As consumer confidence increases, households are more likely to make large purchases, meaning that the automotive industry can reasonably hope for continued growth. It is possible that auto sales in Colorado will be bolstered by people replacing vehicles damaged in the floods; however, because the extent of auto damages from the floods is unclear, the assumption cannot be backed with any certainty.

Grocery chains that open new stores could add hundreds of jobs in Colorado in the coming years. Specialty grocery store chains, including Whole Foods, Trader Joe's, and Lucky's, are often anchors stores for shopping malls. Many of these chains are planning to open locations around the state, including Trader Joe's, which is opening four new locations in the state. Personal income rose a modest 3.3% year-over-year, which might lead to an increase in consumers frequenting specialty grocers.

The legalization of marijuana in 2012 by Amendment 64 has provoked discussion on how the retail marijuana industry will impact Colorado in 2014 and beyond. The effects of recreational marijuana sold at retail stores will largely depend on how the market reacts to the recent approval by Colorado voters of ballot measure Proposition AA. The proposition provides for an initial 15% excise tax and an additional 10% sales tax on retail marijuana sales. The additional taxation will raise an estimated $67 million during the first year for the state of Colorado according to the nonpartisan Colorado Legislative Council. Of the $67 million, around $27.5 million a year will be directed to the Public School Capital Construction Assistance Fund and the remaining amount will be allocated toward regulating the retail marijuana industry. Some cities will receive a portion of the sales tax. Despite raised prices from high taxation and regulation of their product, most prospective shop owners are in support of the measure as it offers a way for their business to be considered legitimate. Those opposed to the proposition argued, unsuccessfully, that higher taxes and regulation in the industry will turn consumers back to the black market or incentivize home-grown operations to escape the high taxes. The results of the 25% tax on retail marijuana in the state remain to be seen, and 2014 will prove to be an interesting year to monitor the subsector. The Marijuana Enforcement Division has received more than 100 retail recreational license applications as of November 2013, the majority of which have the intention of opening in early 2014. The initial retail stores that will open, along with those that will open in the future, are expected to add hundreds of jobs to the Colorado retail industry, although many of these jobs will be in Denver and other urban centers. Implications for employment growth for retail marijuana in the long term are very speculative as the future of the industry is uncertain.

In all, the Colorado retail industry has seen moderate gains in total employment as well as retail sales. Urban areas continue to be the backbone of the industry, providing most of the sector's employment growth. The industry displayed fortitude during the flooding in September, experiencing a net 3% increase in shopper volume and a net 1% increase in consumer increase in the week of and the week following the flood. Looking ahead to 2014, the retail industry in Colorado expects more growth from the automotive industry and employment increases from new specialty retail stores opening in the state. Finally, although the impact of the retail marijuana sector is uncertain, businesses that will begin opening in January may add hundreds of retail jobs in 2014.

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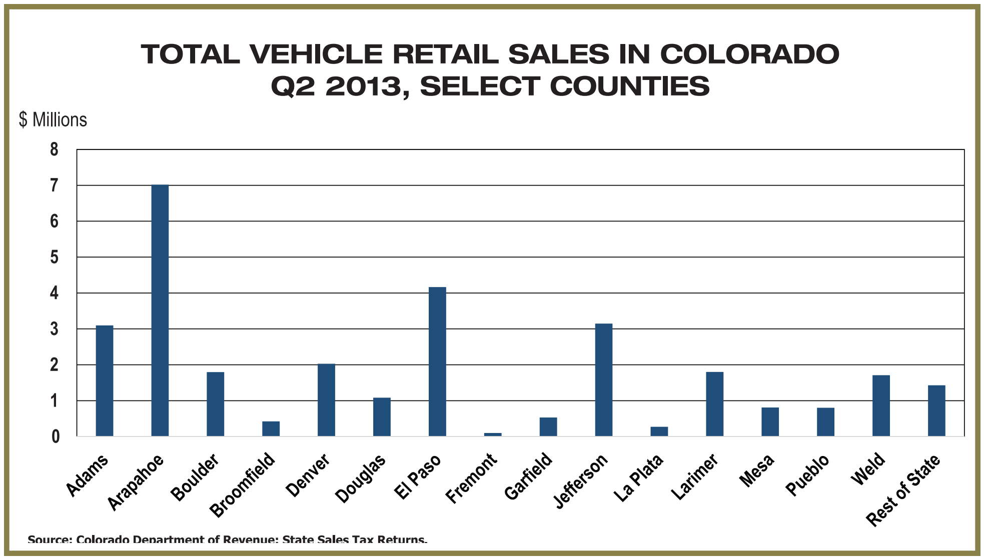

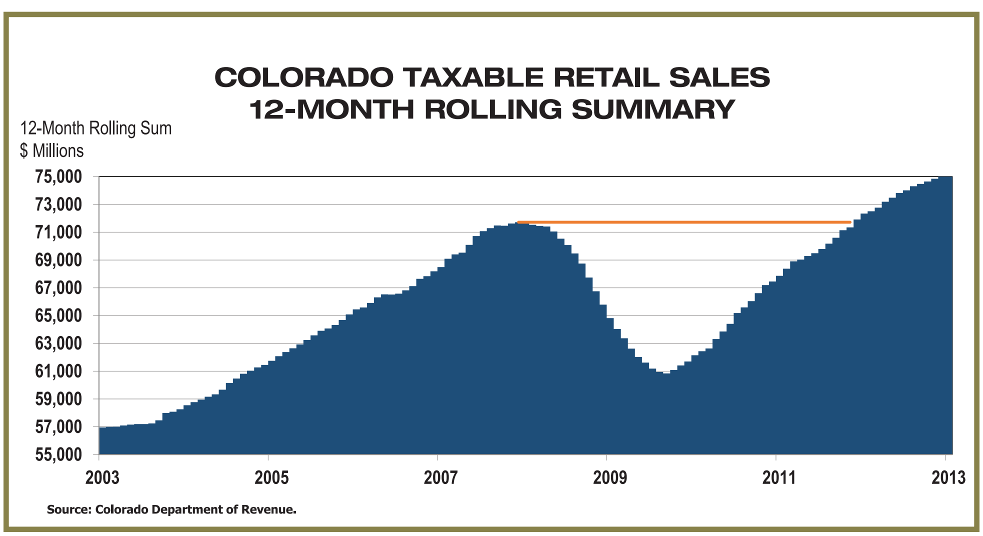

COLORADO BUSINESS REVIEW

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CONSUMER RATINGS, CONTINUED FROM PAGE 2

Q: Do consumer ratings give a better indication of product quality for some product categories than for others?

A: We are still looking into this. So far, we have mostly examined durable, functional product categories like air conditioners, cooking pans, or printers. From this analysis, we have found a weak relationship across the board. It is possible that online ratings are more informative when it comes to experiential purchases, like restaurants or hotels. Interestingly, recent academic research suggests that consumers value online ratings less for experiential purchases. This may be because consumers believe that they are unique when it comes to food and travel. Based on our research, I think we can safely conclude that consumers strongly believe that user ratings are a great indicator of product quality but that the predictive value is very weak.

Q: As we head into the holiday shopping season, what is some advice you can give buyers as they are looking to buy products online?

A: First, it is important to understand that online user ratings cannot be used as a substitute for more elaborate, expert tests of product quality. In fact, suppose you want to surprise a family member with a new coffeemaker. If your goal is to buy the coffeemaker that experts say is the best, you are much better off relying on price than online user ratings. The correlation between price and quality is almost twice that of the correlation between consumer ratings and quality. Second, it is important to be aware of some elementary statistics. Many products have been rated by only a few consumers and therefore the average consumer rating is not reliable. When interpreting consumer ratings, it is crucial to consider the number of consumers who have rated the product. A product has to be rated enough as larger samples tend to be more reliable. As a benchmark I would only trust consumer ratings that have been rated 100+ times, yet there are always exceptions to any rule.

Bart de Langhe is an assistant professor of marketing at the Leeds School of Business, University of Colorado Boulder. After obtaining a BA and MA in psychology from the Catholic University of Leuven (Belgium), he obtained a Ph.D. in marketing from Erasmus University (Netherlands). In 2009, he was a visiting scholar at the University of Chicago. His research examines the role of learning, memory, and cognition for consumer and managerial decision making. His work has been published in the *Journal of Consumer Research*, the *Journal of Marketing Research*, and *Organizational Behavior and Human Decision Processes*. Professor de Langhe teaches consumer and organizational buying behavior in the undergraduate program.