# CityNorth Retail Economic Analysis

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## *Overview*

CityNorth is a proposed 6-million square foot mixed use development to be located near the loop 101 near 56th Street and Tatum proposed by Thomas J. Klutznick and Company.

The City of Phoenix entered into a development agreement with Klutznick including a payment of half city sales tax income for a period of 11 years and 3 months or $97.4 million whichever occurs first for use of parking facilities provided by the developer at the site.

Regardless of the semantic used to frame the development agreement, the economic notions underlying it have little to do with parking, but with subsidizing the retail development component of the site.

Keyser Marston Associates, Inc. provided a developer estimated feasibility gap of $117 million for the entire project, of which the feasibility gap was $3 million for in-line retail, $131 million for Anchor retail, totaling $134 million. The rest of the project, the developer projected as having a $17 million dollar feasibility surplus. [2] Keyser Marston created its own projections and found an overall feasibility gap of $25 million, with in-line retail providing a $47 million surplus, but anchor retail generating a $115 million gap, yielding a total retail shortfall of $68 million.[3]

Hence, the presumed weakness in the project was retail, and specifically anchor retail, which generates the justification for a city subsidy. This report does not evaluate the accuracy of this feasibility gap, but examines the economic impact of the retail focus relative to economic development goals one might presume the city has, while also evaluating the accuracy of gross economic impact estimates provided to the city

[1] Information for affiliation purposes only. Analysis does not reflect the position of the School of Letters and Sciences or Arizona State University.
[2] Do note that feasibility is not the same as profitability; rather feasibility assumes a required rate of return, so a feasibility gap or surplus, simply means the revenue generated would create a lower or higher rate of return than the developer has targeted.
[3] Keyser Marston Associates, Inc. Review of the CityNorth Project, February 9, 2007, see summary tables 1 and 2.

including the difference between gross impacts and net impacts. In addition, it examines the wage-base of high-end retail illustrating that these jobs do not offer a wage premium over other kinds of private employment in Phoenix and to the extent that they do this finding is mitigated by a documented tendency of such retailers to engage in employment practices which fail to employ Hispanic and African-American workers. As such, on the basis of job-quality and economic opportunity, a city subsidy seems unwarranted, especially given that income levels in the Phoenix metro level continue to lag behind other growth cities: Austin, Atlanta, Denver, Portland, and Seattle, as emphasized in a recent *Arizona Republic* Sunday feature.[4]

## *Economics of Shopping Centers*

CityNorth will join the nearby Desert Ridge Marketplace to create a regional shopping draw, as Desert Ridge targets more budget-oriented shoppers relative to the opulent emphasis of CityNorth.

Reviewing the project summary from the developer in the Keyser Marston report one finds differential rents for in-line retailers and anchors. The anchors, Nordstroms, who has already signed on, Bloomingdales, who appears to have agreed as well[5], along with projected stores, Macy's, and Neiman Marcus, pay $2.32 per square foot annually, while the in-line retailers pay $54.26, more than twenty-times more.[6]

Meanwhile projected sales per square foot (annually) are $375 for the anchors compared to $580 for the in-line retailers with restaurants weighing in at $750, yielding collective sales of $531 per square foot.[7]

Yeats, Charles and Jones provide a basic overview of the economics of shopping malls in their article "Anchors and Externalities." General features are that malls need anchors to attract customers who then frequent the in-line retailers, free parking to make them accessible to customers, stores placed in relation to each other so as to enable customers to comparison shop and shop for a wide variety of goods, and chain stores due to their better known product relative to locally owned businesses.[8]

As a consequence of the ability of anchors to draw customers, they note that "it is not unknown for anchors to be charged lease rates per square foot as little as 5 to 10 percent of those of non-anchors."[9] In the case of CityNorth, the expected lease rate is even lower at 4.3 percent. However, their study found that in-line retailers near an anchor under renovation lost about 12 percent of business, implying a vibrant anchor might contribute

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[4] Graham, Chad, "Ariz.'s Choice: Lead or fall behind," *Arizona Republic*, October 28, 2007, pp. A24-A26.
[5] Sagon, Erica.,"Phoenix to get state's first Bloomingdale's" Arizona Republic, October 27, 2007, http://www.azcentral.com/news/articles/1027bloomingdales1027.html.
[6] Tunstall, Richard, Principal, Market Analysis and Research, Peachtree City, GA, memo to Mr. John Gagnier, Thomas J. Klutznick Company, November 10, 2006.
[7] Tunstall, Richard, Principal
[8] Yeats, Maurice, Andy Charles, and Ken Jones (2001), Anchors and Externalities, *Canadian Journal of Regional Science*, volume 24, no. 3, pp. 465-484.
[9] Yeats et al, p. 469.

a similar amount of business suggesting that the lease discounts offered in the marketplace are not matched well by existing underlying economic fundamentals.

Intriguingly, some new regional malls in the area may be moving away from the multi-anchor approach, which increases the space rented at higher amount relative to low-rent space. Westcor's San Tan Village, a regional mall in the Phoenix suburb of Gilbert, opened this month with just one anchor, Dillards.[10]

## *Gross Economic Impact of Retail at CityNorth*

Thomas J. Klutznick Company contracted with Elliot D. Pollack and Company to provide an economic impact evaluation of CityNorth. These estimates are gross impacts that make two assumptions. First, all of the economic transactions that would take place at CityNorth are new transactions to Maricopa County and would not occur otherwise. Tourists who stay in the hotel would have never arrived, and shoppers would not have spent their money elsewhere, and businesses operating out of offices would not otherwise exist in the county. Second, gross impacts assume the proper means of comparison is of the CityNorth complex to an empty lot, presuming that in the absence of this proposal nothing would occur on the property.

Clearly both assumptions are false. While this area is growing with new people, retail does follow rooftops, and some kind of land use would develop on this property. Likewise, tourists would still arrive, businesses would still exist and shoppers will shop elsewhere. But developing an accurate net economic impact which takes into account these factors is challenging, compared to estimating the economic transactions that will take place at a particular project.

Thus, the gross economic impact vastly overstates the net economic impact of the project, but we can't readily determine by how much.

In this case, however, even the gross economic impact is inaccurate.

Pollack and Company used the industry standard Minnesota IMPLAN software device to estimate economic multiplier impacts which include the direct impact (payment to employees and local suppliers), the indirect impact (how suppliers in light of heightened business then hire workers, expand, and purchase added materials locally), and induced impact (how employees in spending their money locally create additional impacts). Again these are gross impacts. However, inexplicably, though Pollack and Company correctly estimate that total retail sales generated will be $672 million annually ($531 sales per square foot times 1,265,000 square feet of retail space), the direct annual economic impact for retail is placed at nearly twice that amount subsequently at $1.1 billion. Direct economic impacts can't exceed the revenue the businesses take in.

[10] Van den Berg, David, "San Tan Village layout called standard for future centers," *Arizona Republic*, Business Section, October 23, 2008, http://www.azcentral.com/business/articles/1023biz-santan1023.html.

In addition, if one reviews the tutorial for the IMPLAN program, it clearly states that one must deduct the cost of goods sold (as goods aren't produced locally) from gross retail sales before calculating the indirect and induced impacts.[11] As retailers here will typically run margins of about 40 percent (margin is the remainder after the cost of goods sold is deducted), the direct economic impact then should be approximately 40 percent of $672 million.[12]

In Table 1, I present the corrected gross retail economic impact numbers from what appears in the Pollack and Company generated table in CityNorth: Draft Impact Analysis and Infrastructure Summary, December 8, 2006.[13]

Table 1

INCORRECT from Table 5 Annual (Gross) Economic Impact from Retail Operations
CityNorth
Maricopa County (2006 dollars)

| | Jobs | Wages | Output |
|---|---|---|---|
| Direct | 3,163 | $ 73,813,000 | *$1,098,786,000* |
| *Indirect* | *2,885* | *$ 165,202,000* | *$ 519,116,000* |
| *Induced* | *3,660* | *$ 143,294,000* | *$ 358,393,000* |
| **Total** | ***9,708*** | ***$ 382,309,000*** | ***$1,976,295,000*** |

CORRECTED

| | Jobs | Wages | Output |
|---|---|---|---|
| Direct | 3,163 | $ 73,813,000 | $ 268,835,296 |
| Indirect | 706 | $ 40,419,271 | $ 127,009,903 |
| Induced | 895 | $ 35,059,133 | $ 87,686,491 |
| **Total** | **4,764** | **$ 149,291,404** | **$ 483,531,690** |
| **% Less** | **51%** | **61%** | **76%** |

Source: Table 5 "Annual Economic Impact Operations City North Maricopa County," page 13 of CityNorth: Draft Impact Analysis and Infrastructure Summary, December 8, 2006 and calculations of the author.

[11] "IMPLAN Workshop Tutorials And Case Studies," see Case Study Exercise 2B: Impact of the Retail Development Component, pp. 91-93, accessible at http://www.implan.com/library/pdf_files/workshoptutorials_092007.pdf

[12] For Nordstrom and Neiman Marcus, 35 percent is roughly their gross margin. See Neiman Marcus' Form 10-K filing with the Securities and Exchange Commission, p. 29 accessible via http://phx.corporate-ir.net/phoenix.zhtml?c=118113&p=irol-sec. For Nordstom see their Financial 2006 which starts with their Form 10-K filing with the Securities and Exchange Commission, pp. 12-13 accessible via http://about.nordstrom.com/annual_report/2006/pdf/financials2006.pdf. However, their accounting procedures include costs of occupancy (rent and utilities) as part of the costs of goods sold, so I have made the margin higher to compensate.

[13] See Table 1 "Assumptions of Analysis City North" on p. 9 for correct retail calculations and Table 5 "Annual Economic Impact from Operations CityNorth Maricopa County (2006 dollars)" on p. 13 for the table with erroneous calculations.

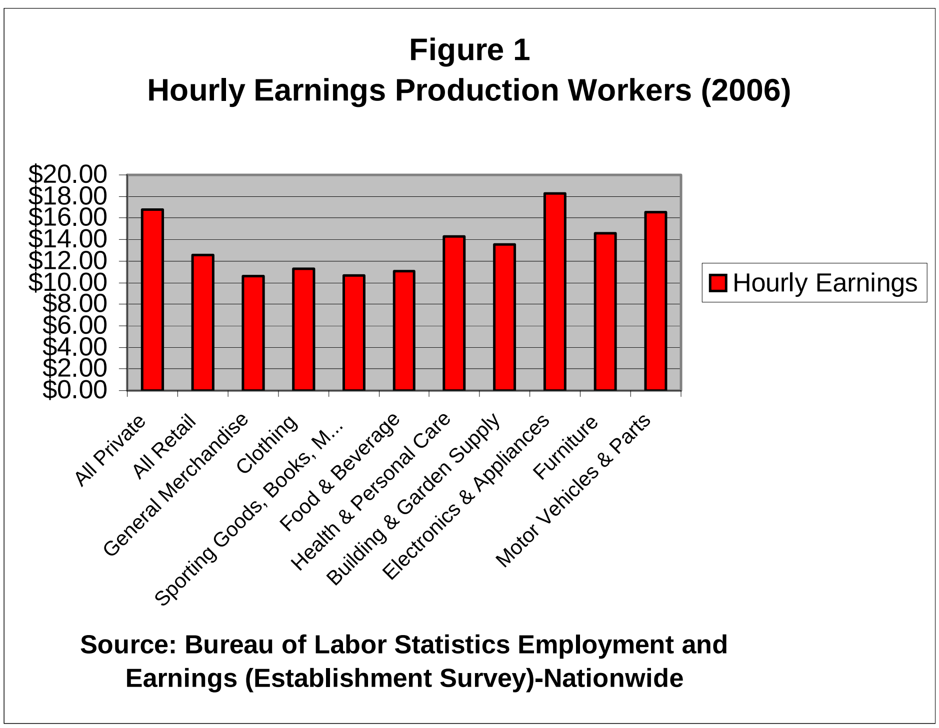
## *Compensation of Retail Workers*

### Government Data

Overall, compared to other workers in the private sector, retail sector workers earn considerably less, but pay rates vary considerably within sectors of the industry. The IMPLAN estimates above indicate an average annual pay for the 3,163 workers of $23,336. This figure is consistent with other measures, including those for high-end retailers, and significantly below average pay in the private sector.

The Bureau of Labor Statistics collects two sets of data. One is based on an establishment survey that focuses on production workers and excludes more supervisory and higher level employees, so is good for examining lower to middle end jobs, such as retail. The other examines all employees covered by unemployment insurance and tends to be more comprehensive.

The establishment survey collects data for various sectors of the retail industry, but doesn't make some of the most pertinent ones available even at a national level, such as "Department Stores, not Discount," a category that includes a wide-range of department stores from Sears to Nordstrom. Whereas, discount department stores includes companies like Wal-Mart and Target. However, the Bureau of Labor Statistics only releases data in the combined category of "General Merchandise Stores," which combines these two and also includes warehouse stores and supercenters.[14] For purposes of comparison, other retail sectors have been included.




Earnings are for Production workers which are defined in the establishment survey as including working supervisors and all nonsupervisor workers which in the retail context includes virtually all workers at any given store site, but not those in a corporate

[14] NAICS Codes (industry codes as of 2002), http://www.census.gov/epcd/naics02/naicod02.htm.

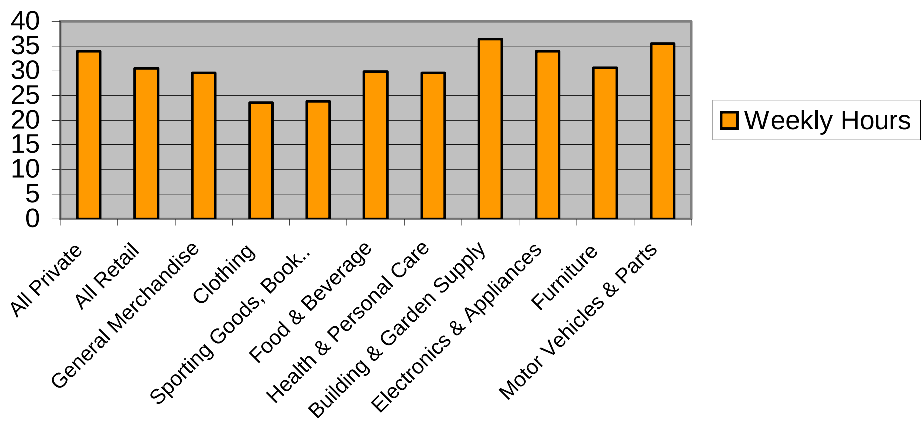
office. Supervisors need to be sufficiently close to production and/or on the floor to count.

Payroll information includes regular pay divided by hours worked to create an overall wage. It should include commissions based on sales as that is normally a regular added component of pay, but it does not include bonuses that might be contingent on a store's annual performance or health or retirement benefits provided by the employer. Payroll data is before tax deductions.[15]

This data gives us an initial benchmark for what retail jobs at CityNorth might pay.

Figures 1 and 2 illustrate that General Merchandise stores on average pay less than other retail outlets and offer fewer hours, yielding lower overall weekly pay. Combining hours and pay, the overall private sector production workers earn $30,000 a year. Retail by contrast typically pays only $20,000 a year.[16] The only retail sectors that are equivalent or outperform the overall private market are Electronics and Appliances and Motor Vehicles and Parts.

**Figure 2**
**Weekly Hours Production Workers (2006)**




**Source: Bureau of Labor Statistics Employment and Earnings (Establishment Survey)-Nationwide**

Arizona State University's W.P. Carey School of Business has developed an index of job quality in Arizona that uses the other measure which comes from the Bureau of Labor Statistics, the Census of Employment and Wages. This data set has the advantage of enabling us to focus on just Arizona as W.P. Carey's study does or even Maricopa County, and even restrict data to the category "Department Stores, not Discount."

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[15] Technical Notes to Establishment Survey Data Published in Employment and Earnings, http://www.bls.gov/web/cestn1.htm.
[16] Calculations: All Private Production Workers=$16.76/hr x 33.9 hrs./week x 52 weeks=$29,545. All Retail Production Workers=$12.58 hour x 30.5 hrs./week x 52 weeks = $19,852.

The W.P. Carey study examines relative pay of the entire Arizona labor market with retail being one of those sectors.[17] Using data from the Census of Employment and Wages, monetary compensation of all covered (for unemployment insurance) workers is pooled and divided by weeks to get a weekly wage or accumulated over the year to determine average annual compensation. It does not provide a measure of hours, just employees, so there is no measure of hourly earnings as with the data set in Figures 1 and 2.

Although unemployment insurance covers workers looking for full-time employment, unemployment insurance taxes usually extend to those who also work part-time as the Bureau of Labor Statistics notes the survey covers 96 percent of total wage and salary jobs. Typically in the retail context workers may put in 25 to 40 hours weekly, where hours worked is often determined more by the employer than the employee due to fluctuations in product demand in a given time period.

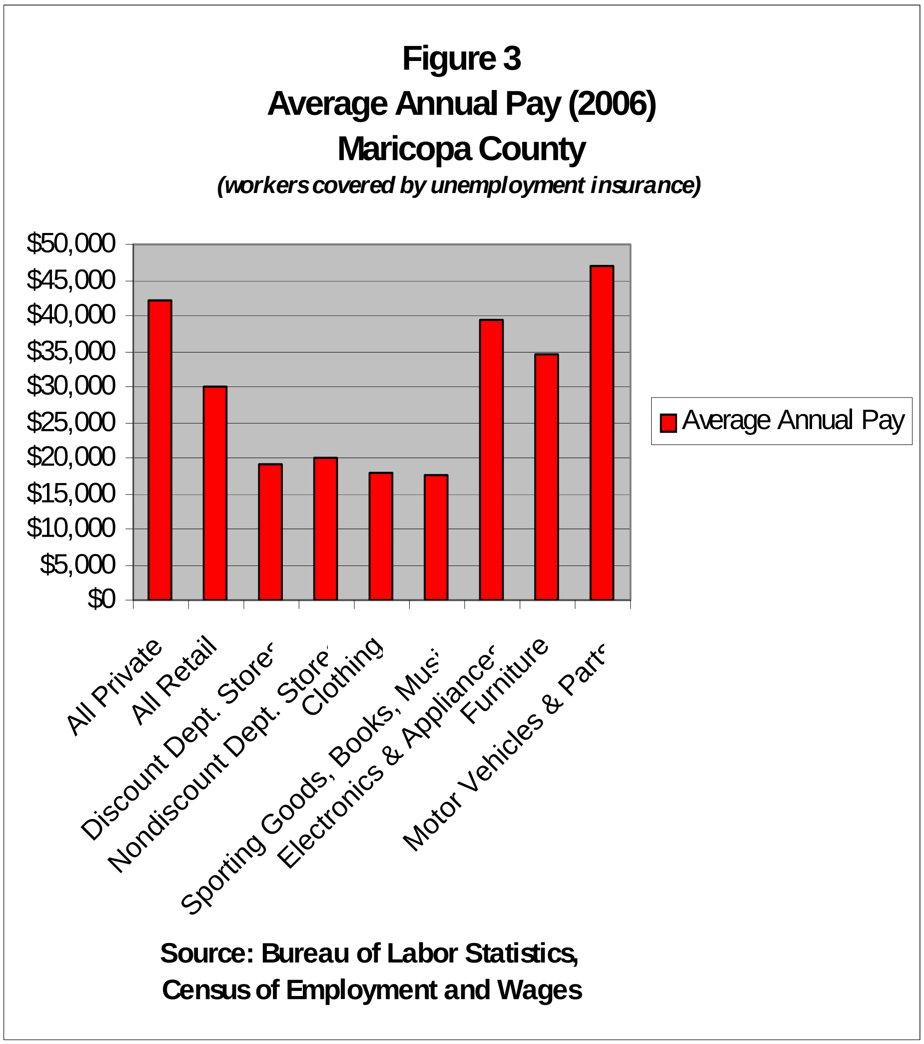


Figure 3 indicates using this more inclusive measure of workers which includes most part-time workers (except some seasonally employed) that overall retail sector pay ($29,917) is roughly 70

[17] Rex, Tom, "Job Quality in 2004 and The Change Between 2001 and 2004," March 2006, Productivity and Prosperity Project (P3), L. William Seidman Research Institute, W. P. Carey School of Business, Arizona State University.

percent of the private sector average ($42,107) and the kinds of stores frequently locating in malls: clothing, sporting goods, books, music, department stores (not discount) all pay closer to half the overall average private sector annual pay. These results are in-line with the IMPLAN estimated annual pay of $23,336 in the developer's report cited earlier.

The W.P. Carey research study of job quality created an index relative to the portion of jobs in particular sectors using all of retail as a category. If retail jobs increased as a portion of all jobs in Arizona, then Arizona's job quality declined. Hence, city subsidies of projects designed to provide retail jobs would be seen through this measure as eroding the overall job quality index. Of the 20 industry sectors identified, retail ranked as the third lowest wage sector.[18]

## Developer Provided Estimates

The CityNorth developer contracted with Elliot Pollack and Company, who used the Minnesota IMPLAN economic impact estimation tool. Though the gross retail economic impact was flawed, we can use the corrected figures from Table 1 as a means of assessing the structure of the retail jobs. Simply dividing wages by jobs among the direct impact yields $23,336. However, we're also interested in the degree to which the higher end retail stores at CityNorth might differ from the industry average. Every five years the Bureau of the Census conducts an economic census of businesses throughout the country. Our most recent results are from 2002, as 2007 will not be conducted until the end of this year. Table 2 compares the IMPLAN estimates with some of the results from the 2002 census. The IMPLAN figures are in 2006 dollars and the Census 2002 dollars. I have not adjusted to consistent dollars, as the proper price adjustment is difficult to discern. Though the consumer price index increases about 3 percent annually, apparel overall has declined.[19] That does not mean that specialty apparel, like the increasingly popular designer jeans, which might be featured at CityNorth, have declined in price—they probably have not.

Table 2

| | Retail IMPLAN-CityNorth | All Retail Phoenix Metro | non-Discount Department. Stores Phoenix Metro |
|---|---|---|---|
| Sales (thousands) | $ 672,088 | $ 38,501,066 | $ 1,151,749 |
| Wages (thousands) | $ 73,813 | $ 4,133,930 | $ 144,394 |
| Employees | 3,163 | 174,829 | 8,453 |
| Pay per Employee | $ 23,336 | $ 23,646 | $ 17,082 |
| Wages as % of Sales | 11.0% | 10.7% | 12.5% |

Sources: Thomas J. Klutznick Company, CityNorth: Draft Impact Analysis Summary, December 8, 2006, Table 1 Assumptions of Analysis City North, p. 9, and Table 5 Annual Economic Impact from Operations CityNorth Maricopa County, p. 13
2002 Economic Census, Bureau of Labor Statistics, Sector 44: Retail Trade: Geographic Area Series: Summary Statistics: 2002 for Phoenix-Mesa-Scottsdale MSA.

[18] Rex, Tom, "Job Quality in 2004 and The Change Between 2001 and 2004," p. 9.
[19] Bureau of Labor Statistics, Consumer Price Index Summary, September 2007, http://www.bls.gov/news.release/cpi.nr0.htm.

What stands out in Table 2 is that while the IMPLAN estimated jobs may pay more overall than the non-Discount Department Store sector, the developer's estimates of retail job quality at CityNorth is indistinguishable from the retail sector as a whole for the Phoenix metropolitan area. Low pay is a result of two factors that one cannot distinguish with this data, lower hourly pay suggested by the data provided in figure 1 and the frequent use of part-time workers in retail settings.

## Store-Based Data: In-line Retail

CityNorth will largely feature retailers who pay in this range. In-line retailers have not yet been identified except for a few restaurants, but the business model for the kinds of retailers likely to fill the space is well-documented as based on part-time sales workers, who usually don't stay on the job long. Across the retail industry, turnover among hourly workers (as opposed to salaried) is nearly 80 percent (on average 4 of 5 employed leave during a year).[20] Turnover among the higher paid salaried retail workers is substantially lower, but most in-line retailers will have overall employee turnover rates between 50 and 67 percent, and some even higher.

As two quick illustrations consider two companies likely to be included at CityNorth, Abercrombie & Fitch and at least one of Limited Brands: Victoria's Secret, Bath & Body Works, C.O. Bigelow, The White Barn Candle Co., Henri Bendel and La Senza. Abercrombie & Fitch report average sales per square foot of $500 for 2006 (p.26), yet as of March 23, 2007 Abercrombie & Fitch had 86,400 sales associates (which they term "models" in house) of which 77,900 were part-time (p.7).[21] Likewise, though Limited Brands reported sales per square foot of $731 for Victoria's Secret, $697 for Bath & Body Works, and collectively $352 for their apparel brands (p. 18), they reported employing on February 3, 2007, 125,500 associates of which 105,100 were part-time. (p. 4).[22] One former student (had in class in 2006) I interviewed who had worked briefly a few years ago at Abercrombie noted the pay level was less than a dollar above minimum wage with no commission, but employees received a 30 percent discount on the trendy merchandise.[23] This experience is quite common. Part-time work primarily attracts teenagers and those going to college, as characterized by high employee turnover, and the companies typically provide little or no benefits beyond an employee discount. Hence, in-line retail, with few exceptions, will not generate quality jobs.

## Store-Based Data: Anchors

The anchor stores will be among the best retail employers at CityNorth, as high-end retailers potentially pay substantially more due to the more expensive nature of their

[20] Carla Joinson "The Cost of Doing Business? - employee turnover and retention in the retail sector," *HR Magazine*, December 1999, FindArticles.com, October 16, 2007, http://findarticles.com/p/articles/mi_m3495/is_13_44/ai_58738503.

[21] Abercrombie & Fitch Form 10-K Filing with the U.S. Securities and Exchange Commission, filed March 30, 2007, pp. 7 and 26, accessible through SEC filings link at http://www.abercrombie.com/anf/lifestyles/html/investor_left.html.

[22] Limited Brands Form 10-K Filing with the U.S. Securities and Exchange Commission, filed April 3, 2007, pp. 4 and 18, accessible through SEC filings link at http://www.limitedbrands.com/investor/financial_performance/sec_filings.jsp.

[23] This was when the minimum wage in Arizona was $5.15 an hour.

merchandise, their economies of scale, and the correlated business model based on customer service. Ferreting out the upscale department stores targeted for CityNorth is more difficult, however, due to the proprietary nature of corporate pay levels.

The CityNorth Updated Sales Projections from Richard Tunstall, Principal of Market Analysis and Research, indicate that the four anticipated anchors are Bloomingdale's, Macy's, Neiman Marcus, and Nordstrom, of which Nordstrom and Bloomingdale's appear to have officially signed on to the project so far.[24]

Wal-Mart's average employee pay of $9.70 an hour was disclosed in 2001 in a sex discrimination lawsuit with more than half the workers earning $9.00 an hour or less.[25] If Wal-Mart's pay has since kept up with general increases in the retail sector, we'd expect the current Wal-Mart average to be roughly the $10.61 an hour for production workers in the general merchandise sector. If upscale retailers pay more, how much more? And equally relevant, how does whom they employ change?

Two of the retailers, Nordstrom and Neiman Marcus, are owned by companies for which these stores are their primary business. Hence, corporate filings enable us to examine them in the absence of other public measures. Macy's and Bloomingdale's are both owned by Federated Department Stores, which earlier this year renamed itself Macy's Inc. Macy's, Inc./Federated in 2005 purchased May Department Stores and over the last couple years has been renaming many of these former regional stores Macy's. Hence, names like Hecht's, Feline's, and Marshall Field's have disappeared and been replaced by Macy's.[26] Public filings will primarily illustrate the business model for Macy's as opposed to Bloomingdale's, since Macy's stores are far more numerous. Elsewhere in the public domain we do find ample evidence of what pay levels are at Macy's and limited evidence for Bloomingdale's. Overall, it appears that Macy's does not pay much better than Wal-Mart. Although the other three do, only Neiman Marcus pays at a level comparable to the average private annual pay found elsewhere in Maricopa County.

## Macy's

Macy's is the least upscale of the four and appears to offer pay levels that are not significantly higher than Wal-Mart. Macy's pay information generally becomes public in the context of labor disputes. Hence, these are unionized stores which likely biases wage levels beyond what we might see in Arizona. In 2006, a labor dispute in New York City included four stores, among them the famous flagship store; employees primarily disputed the health care coverage.

Public records reveal that Federated was pushing to increase its already high employee health care costs on to employees. CBS news characterized as increasing the cost

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[24] Tunstall, Richard, Principal.

[25] Dupe, Arinjadrit and Ken Jacobs, "Hidden Cost of Wal-Mart Jobs: Use of Safety Net Programs by Wal-Mart Workers in California," University of California Berkeley Labor Center. August 2, 2004.

[26] Federated and May Announce Merger; $17 billion transaction to create value for customers, shareholders, February 28, 2005, http://phx.corporate-ir.net/phoenix.zhtml?c=84477&p=irol-newsArticle&ID=679294&highlight=.

sharing to 60 percent on employees from 50 percent. While other sources focused on deductibles and noted that individual deductibles would be $1500 and $3000 for a family. Given that typical wages at Macy's were reported as $11 an hour and a full-time worker might make $20,000 (35 hours a week), this represents a significant portion of earnings, not to mention any additional cost sharing that occurs after the deductible is met.[27]

Workers do earn commissions at Macy's, but commissions appear to be based on meeting a minimum sales quota that workers indicate can often only be reached during sales. Those quotas appear to be $2,000 in gross sales per week. Macy's workers have also complained about requirements to get one to two additional Macy's credit card accounts each week to avoid disciplinary actions, including possible firing. Workers say that regular customers are a main source of business, so opportunities are limited.

<u>Maximum</u> pay levels revealed at a web site from Washington state were:[28]
Sitting Room $9.00
Processors $10.65
Commissions Associate $12.40
Sales Support $12.73
Cosmetics $14.35

Commissions might be possible in some cases, but again appear to be an erratic source of added pay.

Thus, overall Macy's does not appear to be an overly generous employer offering high quality jobs to match its higher end reputation.

## Bloomingdale's

An Equal Employment Opportunities Commission study describes Bloomingdale's as follows:

> Bloomingdale's serves high-income customers. Only 20 percent of its workers are part-time, turnover is low, wages are above average for Federated stores, and a significant amount of money is spent on recruiting polished workers with good "people skills" mostly young white women attending college.[29]

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[27] "Strike Threat Rumbling At Macy's: Health Care Costs Wages Big Issues at NYC Stores," CBS News, February 21, 2006, http://www.cbsnews.com/stories/2006/02/21/business/main1331691.shtml, Har-el, Lori, "Macy's Employees Protest Merit Wage Increases," The Epoch Times, February 28, 2006, http://en.epochtimes.com/news/6-2-28/38782.html, and Harrigan, Susan, "NYC, Westchester store employees reach no resolution in talks on costs of health care and wage hike criteria," Newsday, February 21, 2006, republished at Retail, Wholesale and Department Store Union, UFCW, http://www.rwdsu.info/en/archives/2006/02/nyc_westchester.html.

[28] "Tacoma Macy's Vice-President Carol Lorton Ducks 2006 Pierce County 'Grinch of the Year' Award," Washington State Jobs with Justice, http://www.wsjwj.org/news_2006/grinch_pierce07.asp.

[29] "High End Department Stores, Their Access To And Use Of Diverse Labor Markets: Summary Report," U.S. Equal Employment Opportunity Commission, 2004, http://www.eeoc.gov/stats/reports/departmentstores/summary.html.

A 2004 union contract on line through Cornell University revealed more information regarding pay levels, though perhaps upwardly biased relative to Arizona due to union representation.[30]

It indicates that the starting wage can be no lower than $8 an hour. It specifies a series of hourly raises of about 40 cents per hour for those not working on straight commission that, relative to an employee earning $10 an hour (approximate Wal-Mart average), is approximately 4 percent per year with larger increases dependent on store performance benchmarks.

Sales associates working full-time are expected to open one new charge account per week (like Macy's). The contract also illustrates an example pay scheme for associates in the fur department. The fur department is not representative of the entire store. In this case the typical pay for four individuals singled out is about $20 an hour, creating a base pay of $40,000. On top of that is a commission tied to sales goal and additional service payment (for years at the company), creating annual pay of nearly $70,000. Intriguingly these named employees were also given a severance package offer equal to the base pay as alternative. Collectively, it suggests a very special case that one should be careful in terms of interpreting broader implications.

The furniture memo within the contract indicates that employees will be paid $20 an hour base and service to the store added compensation (which is likely contingent on meeting sale quotas) ranges from $6,000 to $10,000.

Collectively, fur and furniture are likely more privileged sectors within the store, so may not be representative of the whole—but in general it appears Bloomingdale's pays between $8 and $20 an hour with added commissions and service payments in the context of being unionized—and it is likely typical Bloomingdale's employees are paid fairly well relative to the rest of the retail sector and department stores in particular, but less than the average private sector pay in Maricopa County. Bloomingdale's average pay may be most comparable to Nordstrom.

## Neiman Marcus and Nordstrom

No clear information could be found regarding compensation at Neiman Marcus, other than Neiman Marcus appears to employ most sales associates on a strict commission basis.[31] Given that Neiman Marcus, of the four department stores, appears to be the most geared to extremely high-end customers, this should not be too surprising. Based on an EEOC study quoting a 2002 trade article from *Women's Wear*, "Neiman's average customer is 43 and earns approximately $200,000." The EEOC study also did a price comparison of web sites from a number of retailers and rated Neiman Marcus most

[30] Bloomingdale's and Retail, Wholesale and Department Store Union (RWDSU), Local 3 (1996), Cornell Industrial Labor Relations School, contract effective date March 1, 2004 through March 1, 2008, http://digitalcommons.ilr.cornell.edu/cgi/viewcontent.cgi?article=1454&context=blscontracts.

[31] See for instance, Dukcevich, Davide, "Neiman Marcus Sows Seeds For A Turnaround," September 10, 2002, Forbes.com, http://www.forbes.com/2002/09/10/0910neiman.html.

expensive with its five most expensive items in each of handbags, shoes and apparel selling for above or close to $1,000.[32]

Neiman Marcus' business model put forth in a form to the Securities and Exchange Commission suggests a staffing and compensation emphasis similar to Nordstrom as each rely on an approximately 36 percent margin on sales (cost of goods sold is 64 percent) with Selling, General and Administrative (SG&A) expenses at 25 percent.[33] Labor costs are a substantial element of SG&A.

Nordstrom has a solid reputation as a customer service focused retailer that is good to work for. In fact, unlike other retailers, including the ones noted above here, Nordstrom is usually singled out for its corporate culture where associates are given far more independent decision making.[34] Salaries are generally good for retail, though difficult to pin down. Nordstrom has historically started employees off at a higher wage than Macy's or Bloomingdale's according to one author. So in the mid-1990's while employees started at $6 to $7 an hour at the former two, at Nordstrom they started at $9.50 an hour. Nordstrom expects much of employees, so turnover is primarily generated by new employees.[35]

Sales per square foot for higher-end department stores drives pay levels, since it is the basis of company revenues that can compensate employees. Peck et al. claim in their 1999 book that in 1990 Nordstrom's Sales Associates earned twice the industry average, $23,000 to $26,000 and that Nordstrom had twice the sales per square foot of stores, $380 compared to $194 the industry norm where Bloomingdale's and Macy's largely stood.[36]

Table 3
Nordstrom sales per square foot

| 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|---|---|---|---|---|
| $377 | $385 | $362 | $340 | $341 | $319 | $317 | $325 | $347 | $369 | $393 |

Source: Nordstom, Financials 2006, Form 10-K filing with the Securities and Exchange Commission, pages 12-13 accessible via http://about.nordstrom.com/annual_report/2006/pdf/financials2006.pdf.

These numbers appear to be correct, but Nordstrom of 1990 does not appear to be the Nordstrom of today, because sales per square feet never kept up. As Table 3 illustrates, Nordstrom's sales stagnated in the 1990's then fell significantly. Not until 2006 has the

[32] "High End Department Stores: Their Access To And Use Of Diverse Labor Markets: Technical Report U.S. Equal Employment Opportunity Commission, 2004, http://www.eeoc.gov/stats/reports/departmentstores/technical.html.
[33]Neiman Marcus, United States Security and Exchange Commission, Form 10-K, for year ending June 29, 2006, p. 29. http://nypl.brand.edgar-online.com/EFX_dll/EDGARpro.dll?FetchFilingHTML1?SessionID=mFVhj7y2l3gcCGx&ID=4673483.
[34] See for instance, Spector, Robert, 1996, *The Nordstrom Way: The Inside Story of America's #1 Customer Service Company*, Wiley, excerpts accessible at http://www.robertspector.com/book_nordstrom_excerpt.cfm.
[35] Peck, Helen, Martin Christopher, Moira Clark, and Adrian Payne, 1999, *Relationship Marketing for Competitive Advantage*, Elsevier, see chapter 5.
[36] Peck, Helen et al., pp. 379-381 (google searches enable you to read these pages online).

store eclipsed that mark. Consequently, pay at Nordstrom's has not changed much in that time period. Table 6 uses Nordstrom's financial data to estimate that current average full-time pay at Nordstrom is roughly $29,500, a significant drop from 1990 when inflation adjusted.

Corporations file 10-K forms with the United States Securities and Exchange Commission. In the case of Nordstrom and Neiman Marcus, their department stores are by far the primary business. Labor costs are never clearly specified in company financial statements. However, they are a part of SG&A: Selling, General and Administrative expenses. A simplified comparison of Wal-Mart and Nordstrom, Home Depot and Lowe's is noted below in Table 4.

Table 4

| | WMT | NORD | HD | LOWES |
|---|---|---|---|---|
| **Revenue** | **100%** | **100%** | **100%** | **100%** |
| **COGS** | **76%** | **64%** | **67%** | **66%** |
| **Gross Margin** | **24%** | **36%** | **33%** | **34%** |
| **R&D** | **0%** | **0%** | **0%** | **0%** |
| **SGA** | **18%** | **28%** | **23%** | **23%** |
| **Expenses** | **18%** | **28%** | **23%** | **23%** |
| **Op Profit** | **6%** | **8%** | **11%** | **11%** |

Source: Tillet, Charlie, "Building Financial Projections" Powerpoint, January 23, 2007, Massachusetts Institute of Technology, http://entrepreneurship.mit.edu/15975/Presentations/Session3_Tillett_2007.ppt.

From revenue one deducts the Cost of Goods Sold (COGS), leaving the gross margin (recall the 40 percent margin used earlier in this analysis). The cost of goods sold typically includes the cost of merchandise, shoplifting/employee theft losses, freight, and distribution costs. Often store occupancy costs (rent, fees for maintenance of common areas, and property taxes, store maintenance and utilities) are also grouped here. Sales, General, and Administrative expenses include all labor costs including fringe benefits as well as transaction fees on credit cards, marketing, legal, accounting, information systems, and corporate office expenses. [37]

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[37] Summary borrowed from Dick's Sporting Goods, 10-K filing with U.S. Securities and Exchange Commission, March 31, 2005, Annual Report, http://biz.yahoo.com/e/050331/dks10-k_a.html.

Unfortunately, finding out how much payroll costs are as a percent of SG&A is not simple. Using three companies who have released it in different retail sectors: Radio Shack, Pier 1, and Costco, we can develop an estimate. None of these companies are likely to locate in CityNorth, but their figures are useful in determining an estimated cost basis for payroll expense in retail. Because of different business models, the focus is not on labor costs as a percent of sales, but labor costs as a percent of SG&A, which would have less variation. Because marketing costs can also vary across business models, when possible I have also calculated payroll costs as a percent of SG&A less marketing costs. Table 5 suggests that using 80 percent of SG&A less marketing expenses would be a reasonable high-end estimate of employee compensation including benefits for anchor retailers at CityNorth.

Table 5

| | Payroll / Payroll & Benefits as percent of SG&A[1] | Payroll/Payroll plus benefits as percent of SG&A less marketing |
|---|---|---|
| Costco (inc. benefits) | 70%[2] | n.a. |
| Pier 1 (inc. benefits) | 43% | 74% |
| RadioShack (excludes benefits) | 51% | n.a. |

[1]Radio Shack includes occupancy costs in SG&A. The rent cost was removed from SG&A before calculating the percent to make it more comparable.
[2]BJ's Wholesale Club in the same category reports 73-79% across different quarters.

Sources: Costco: Galanti, Richard, CFO, Costco F2Q06 (Quarter Ending February 12, 2006) Earnings Conference Call Transcript (COST) posted on: March 02, 2006 , http://seekingalpha.com/article/7335-costco-f2q06-quarter-ending-february-12-2006-earnings-conference-call-transcript-
Pier 1: Pier 1 Imports, Inc. Reports Second Quarter Financial Results, Sept. 20, 2007, http://www.pier1.com/SideMenu/IR/PressReleases/tabid/94/default.aspx?ReleaseID=1053709
RadioShack: Cocq, Matthieu. Franck Legoux, Patrick de Loe, Genki Oka, and Alexander Zorn
RadioShack: Turnaround Management Report, Arpil 24, 2006 http://www.turnaround.org/cmaextras/Paper--Radioshack.pdf

Building on prior research in this paper, Table 6 presents estimated annual pay including commissions and bonuses for full-time employees employed by Neiman Marcus, Nordstrom and Macy's, which also owns Bloomingdale's. I assume as the 2004 EEOC report stated for Bloomingdale's that all the stores employ only 20 percent part-time employees. I then presume that part-time employees work about 2/3 the hours of full-time employees to develop a measure of full-time equivalent employees. The results indicate that only Neiman Marcus at $40,071 comes close to the average annual pay in the private sector cited in Figure 3 at$42,107. But one should note that the $42,107 figure includes both full-time and part-time employees weighted equally. Had I done my calculation similarly, then Neiman Marcus' pay would be $37,426, a full $5,000 less.

Nordstrom and Macy's fare far worse with estimated full-time pay levels below $30,000. As these figures include upper management in corporate headquarters, they should be seen as potentially upwardly biased, though to the degree part-time employees are placed on lower pay scales compared to full-time employees, then this upward bias would be mitigated or eliminated.

Table 6

| (thousands) | Neiman Marcus 2006 | Nordstrom 2006 | Macy's 2006 |
|---|---|---|---|
| SG&A | 1,105,100 | 2,296,863 | 8,678,000 |
| marketing | -100,200 | -109,373 | -1,171,000 |
| marketing as % of SG&A | 9% | 5% | 13% |
| | | | |
| Total employee payroll & benefits (80% est.) [1] | 803,920 | 1,749,992 | 6,005,600 |
| Employees | 17.9 | 52.9 | 188.0 |
| Full-Time Employees (est.) [2] | 14.3 | 42.3 | 150.4 |
| **Full-Time Employee Pay[3]** | **$40,071** | **$29,516** | **$28,502** |

[1] Based on Table 5 assume as high-end estimate that payroll and benefits are 80 percent of SG&A after deducting marketing expenses.
[2] Based on EEOC report assume all merchants are like Bloomingdale's and have 80 percent full-time employees.
[3] I assume part-time employees work 2/3 the hours of full-time employees to calculate full-time equivalent (FTE). Total payroll and benefits are also divided by 1.2 to capture costs of mandated payroll taxes employer paid (FICA match, workers comp & unemployment insurance (9%) plus retirement, health, life and disability insurance (11%). Figures are based on compensation averages for Trade, Tranportation and Utilities by Bureau of Labor Statistics.

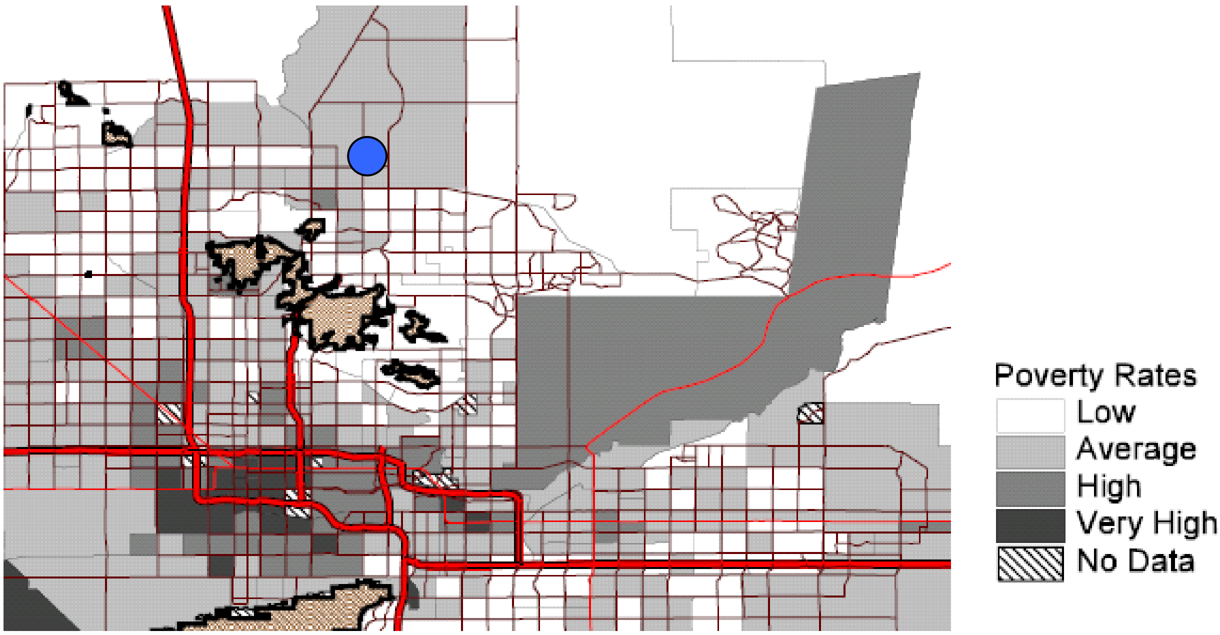
Source: See Neiman Marcus' Form 10-K filing with the Securities and Exchange Commission accessible via http://phx.corporate-ir.net/phoenix.zhtml?c=118113&p=irol-sec. For Nordstom see their Financial 2006 which starts with their Form 10-K filing with the Securities and Exchange Commission, accessible via http://about.nordstrom.com/annual_report/2006/pdf/financials2006.pdf. For Macy's Form 10-K filing with the Securities and Exchange Commission for April 4, 2007. Bureau of Labor Statistics, Table 6. Employer costs per hour worked for employee compensation and costs as a percent of total compensation: Private industry workers, by major industry group, June 2007, http://www.bls.gov/news.release/ecec.t06.htm

These estimates are roughly in-line with the pay of sales associates at Nordstrom from 1990, which Peck et al. claimed ranged from $23,000 to $26,000 for full-time work. As Nordstrom's sales per square foot have only increased 3 percent (nominally) since 1990 and benefit costs, if anything, have risen as a percent of total compensation, these estimates suggest sales associates receive nearly the same nominal pay (i.e., not adjusted for inflation). In inflation-adjusted dollars, full-time pay levels would have fallen significantly at Nordstrom since 1990 and appear to be about 70 percent of the average in the private sector in Maricopa County.

## Who will get hired?

The U.S. Equal Employment Opportunities Commission conducted a study of the relative availability of members of various ethnic groups in the labor markets of department stores and compared that to actual hires in a 2004 study. In that study they

Figure 4
METROPOLITAN PHOENIX POVERTY RATES, 1989
Percentage of Total Population




CityNorth approximate location.

Source: Calculated from 1990 Census data. Map on page 8 “Population Demographics In Metropolitan Phoenix” Prepared for the Morrison Institute for Public Policy School of Public Affairs College of Public Programs, Arizona State University As part of the Brookings Growth Case Study Tom R. Rex Center for Business Research L. William Seidman Research Institute College of Business Arizona State University, August 2000.

found high-end department stores in general had similar access to nonwhite workers including African-American and Hispanic as other department stores, but they found high-end department stores which they called Designer/Bridge and included Nordstrom, Neiman Marcus and Bloomingdale’s (not Macy’s) had an 80 percent likelihood to employ significantly fewer nonwhite workers than expected given overall labor supply. The model also held when testing for just African-Americans and just Hispanics. Macy’s was classified as a better/moderate department store. That category had only 25 percent of stores with low minority employment counts relative to their labor markets.[38]

It seems quite likely that CityNorth will also fail to employ sufficient African-Americans or Hispanics in its higher paying retail stores. Proximity will be one factor. While the Census Data for the map is dated (1990), this Arizona State Morrison Institute study’s map shown in Figure 4 illustrates the significant distance between where CityNorth is and where Phoenix’s areas of economic deprivation exist, which are also predominately Hispanic and African-American neighborhoods.

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[38] High End Department Stores: Their Access To And Use Of Diverse Labor Markets: Technical Report U.S. Equal Employment Opportunity Commission, 2004, http://www.eeoc.gov/stats/reports/departmentstores/technical.html.

As Figure 4 is particularly outdated with respect to the economic demographics in the census tracts within the approximately 50 square miles surrounding CityNorth, 2000 census tract data from those tracts closest to the proposed development were examined for the portion of minority population, median incomes, and portion of households with incomes below poverty. Table 7 compares this 50 square mile region with the city of Phoenix as a whole. Table 7 is also dated due to the continuing growth in that region. However, it more clearly indicates the degree to which that area is comparatively more

Table 7

| | % Hispanic | % African-American | poverty rate | median income |
|---|---|---|---|---|
| CityNorth Area | 7.5% | 1.4% | 3.7% | $65,739 |
| All Phoenix | 26.7% | 4.0% | 10.5% | $44,473 |

Source: Census 2000. CityNorth Area includes 7 census tracts in Phoenix 303.58, 303.33, 303.55, 303.56, 303.57, 303.30, 303.31 and 1 census tract in Scottsdale 2168.24.

affluent than the city of Phoenix and noticeably less ethnically diverse with about one-third the portion of Hispanics and African-Americans as the entire city of Phoenix. As such the labor market for retailers in CityNorth will generally provide less opportunities for minorities and those from lower incomes than is the case if it were located elsewhere in the city. Combined with the known propensity of Designer/Bridge retailers which includes Bloomingdale's, Neiman Marcus, and Nordstrom (the only three other department store retailers the EEOC placed in this category were Marshall Fields, Barneys, and Saks Fifth Avenue)[39] to fail to employ ethnic minorities relative to those minorities' proximity to the jobs suggests that subsidies by the city of Phoenix will be subsidizing anchor retailers who will tend to employ affluent white, non-Hispanic, members of the labor force, failing to meet economic development goals for the city's most at risk populations.

## *Conclusion*

This economic analysis has reviewed the gross economic impact of the proposed retail development at CityNorth. Gross economic impacts overstate actual impacts as they presume no economic activity would have occurred otherwise—e.g., that if you did not buy shoes at CityNorth you would not buy shoes at all. And it presumes that nothing would be built if CityNorth was not developed as proposed. In addition the estimates by Elliot Pollack and Company overstate the gross retail impact by 50 percent in terms of jobs and 75 percent in terms of economic output.

Job quality analysis illustrated that retail jobs pay significantly less than other jobs in the private sector, including other opportunities for production workers. In-line retailers at CityNorth will primarily employ part-time workers at low wages. More careful analysis of the four anticipated anchor stores illustrates that Macy's

[39] High End Department Stores: Their Access To And Use Of Diverse Labor Markets: Technical Report.

compensates employees little better than Wal-Mart. A typical full-time worker at Macy's can expect to bring home $20,000 based on labor dispute records, while facing an individual deductible for health insurance of $1,500 in addition to other cost sharing. Full-time workers at Nordstrom do earn more, but likely no more than 70 percent of average private sector annual pay in Maricopa County, leaving only Neiman Marcus as paying full-time employees comparable to the average annual private sector pay in Maricopa County, though even here when adjustments are made for part-time workers Neiman Marcus falls $5,000 below the county's average.

However, even these results are shaded by the documented history of higher-end retailers failing to employ as many minorities, especially Hispanics and African-Americans, relative to those minorities' proximity to their stores. Less prestigious department stores with similar minority labor market proximity to their stores do substantially better in employing them.

Collectively, it is hard to find an economic basis to justify a subsidy to the developer of nearly $100 million.

October 30, 2007