

From Outcasts To Anchor Tenants: The Rise of Fitness Options In Shopping Centers



MARKET COMMENTARY

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Large Gyms And Boutique Fitness Brands Are Increasing Traffic Within Shopping Centers and Malls Once Maligned, The Fitness Industry Has Experienced Explosive Growth Over The Past Decade

Several Trends Have Converged To Fuel The Growth Of The U.S. Fitness Industry

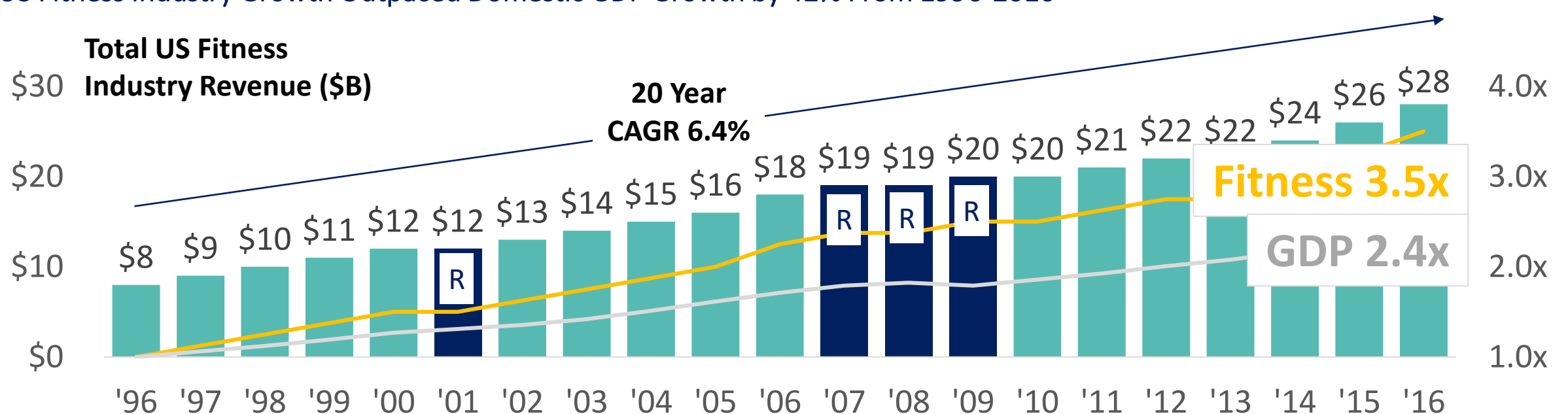
Last June, LBX acquired a shopping center in Orlando, FL that is co-anchored by YouFit, a health club chain with over 100 locations. The primary benefit of this kind of tenant is clear: it brings foot traffic from the local community to our center at all hours. Twenty years ago, this kind of retail use was often considered an eyesore, but the fitness industry has evolved. Large chains like LA Fitness and Planet Fitness, as well as boutique studios like Orangetheory and Pure Barre, have proliferated in shopping centers around the country. Since 1996, the fitness category has grown 3.5x versus GDP of 2.4x (42% higher), with sustained growth through recessions (Piper Jaffray). Today, more than 57 million people belong to a health club (19.3% of the US population) and memberships have risen by 26% since 2009, according to IHRSA (the fitness industry trade group). Fitness tenants are now commonplace for several reasons, including:

U.S. Fitness Industry – By The Numbers

- 57 MM** U.S. Health Club Members
- +26%** Increase in Memberships Since 2009
- +42%** Industry Growth vs. GDP Growth

- **Retailers Have Closed Stores:** As traditional retailers close thousands of stores, big box space is freed up for different uses. While boutique fitness chains generally occupy smaller footprints (10,000 SF or less), major players can often step right into all or part of a vacated box and occupy space ranging from 20,000 SF on average (Planet Fitness) to 114,000 SF on average (Lifetime Fitness).
- **Fitness Chains Have Broad Institutional Backing:** At least 15 private equity backed fitness operators are competing for market share and Planet Fitness and LA Fitness are both public traded companies. This, coupled with low cost financing, has spurred significant expansion by leading fitness concepts.
- **Non-Traditional Retail Uses Have Demonstrated An Ability To Drive Foot Traffic:** In last month's research piece we highlighted [Retail-tainment](#) and the impact of non-traditional uses like trampoline parks on shopping centers. Fitness chains offer a more conventional use that attracts shoppers.
- **Consumers Are Becoming More Health-Conscious:** There is a growing focus on preventative healthcare in response to rising healthcare costs, and consumers are more educated about the costs of living an unhealthy life.
- **The Changing Consumer:** The appeal of live-work-play environments means that shoppers now consolidate their trips, combining workouts with grocery or salon trips is now the norm. Also, the industry is increasingly segmented, with boutiques and high-value/low-price fitness chains exhibiting the strongest growth over the past several years.

US Fitness Industry Growth Outpaced Domestic GDP Growth by 42% From 1996-2016



Source: Piper Jaffray

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Fitness Industry Overview: The Largest Players Continue To Expand

As noted, the fitness industry has been growing steadily for the past quarter of a century. Between 1996 and 2017, it grew at an annual rate of 6.4% and health club memberships among Americans aged 15 and older increased annually by 4%, sustaining growth through two recessions. Between 2011 and 2017 the industry grew annually at 5.6%, to \$28 billion in annual revenues, and revenues are projected to increase 2% to 3% per year between 2018 and 2021 (source: CreditIntell). Fitness boutiques and low-cost operators have increased competition over the past several years. Between 2011 and 2017 fitness locations in the U.S. increased at a 5-year CAGR of 5.1% while average memberships per location declined 1.8% between 2012 and 2017. Annual fitness spend per member (other than membership) is now \$490, and has seen an uptick over the past five years, from a 2.2% annual growth rate to 3.5%. Health clubs attracted more than 70 million consumers in 2017, a record-high since the International Health, Racquet & Sportsclub Association (“IHRSA”) began tracking health club consumer statistics in 1987. The number of individual members totaled 60.9 million, up 6.3% from 57.3 million in 2016. Of the 298.3 million Americans age 6 and older, 20.3% were health club members in 2016. The total number of health club visits has also increased, amounting to 5.9 billion visits in 2017, up from 4.3 billion in 2008.

Club Industry’s Ten Largest Fitness Chains (By Revenue)

Rank	Company	2017 Revenue (Millions)	Revenue Change from 2016 ¹	Founded	# Sites in 2017	# of States Operate In 2017	# Memberships in 2017
1	LA Fitness (Irvine, CA) www.lafitness.com • Multipurpose clubs	2,100 ***	5.7%****	1984	705 (O)	NA	NA
2	Life Time (Chanhassen, MN) www.lifetimefitness.com • Fitness, family recreation and spa destination multipurpose clubs	1,550*	5%*	1992	NA	NA	NA
3	24 Hour Fitness (San Ramon, CA) www.24hourfitness.com • Multipurpose health club company	1,441	1.5%	1983	433 (O)	13	3,540,000
4	Equinox Holdings (Equinox, Blink, SoulCycle, Pure Yoga) (New York, NY) www.equinox.com • Equinox Holdings includes Equinox, Blink, Pure Yoga and SoulCycle brands	1,300***	19%****	1991	91 (O)	NA	NA
5	ClubCorp (Dallas, TX) www.clubcorp.com • Membership-based operator of private golf and country clubs, and business, sports and alumni clubs	1,190	1.9%	1957	192 (O) / 12 (M)	27	173,130
6	Planet Fitness (Hampton, NH) www.planetfitness.com • Low-priced judgment-free gym	430	14.0%	1992	1518 (F)	48	NA
7	Town Sports International Holdings (New York, NY) www.mysportsclubs.com • Fitness-only clubs under the brands New York Sports Clubs, Boston Sports Clubs, Philadelphia Sports Clubs and Washington Sports Clubs	403	1.5%	1973	165 (O)	NA	NA
8	The Bay Club Co. (San Francisco, CA) www.bayclubs.com • Operator of active lifestyle campuses	235	4.0%	1977	24 (O)	1	58,543
9	Capital Fitness Inc. dba Xsport (Big Rock, IL) www.xsportfitness.com • Operator of multipurpose health clubs and express models	195	2.0%	1997	39 (O)	3	346,000
10	Crunch (New York, NY) www.crunch.com • Health club operator and franchisor	173	8.0%	1989	58 (O) / 177 (F) / 4 (L)	24	1,095,000

Key: 1 = Increases may reflect revenue growth through acquisition or new club openings. * = Revenue derived from various financial & industry sources. ** = Estimated revenue based on revenue increase company predicted when submitting 2017 Top 100 form. *** = Revenue is last 12 months ending 09/30/2017. **** = Percent increase compares full 2016 revenue estimate to LTM 09/30/2017 revenue. (A) = Acquire. (B) = Build. NA = Not available. (O) = Owned/Leased. (M) = Managed. (F) = Franchised. (L) = Licensed.

Charting The Rise Of The Boutiques and High Value/Low Price Fitness Chains

While the largest chains (by revenue) are LA Fitness, Life Time, and 24 Hour Fitness, the boutique segment such as Orangetheory and high-value/low-price chains (including Planet Fitness, which IPOed in 2015, Crunch and Town Sports), grew store count rapidly over the past decade. As of 2016, for example, high-value/low-price (“HVLP”) and boutique fitness chains accounted for 40% of the top 15 fitness chains, up from 13%+ in 2009. Growth in both segments has been rapid but they cater to different clientele. Whereas boutique studios, which typically feature a pay-as-you-go model that can top \$30/session, market a high-end studio experience to those looking to stay in shape, the HVLP segment is decidedly off-price. Chains like Planet Fitness enable customers to sign up for \$10/month – people sign up and do not feel like they need to visit the gym regularly in order for the price to make economic sense. This arguably makes the HVLP more recession-proof.

Top 15 Fitness Chains By Store Count, 2009 vs. 2016

2009			2016			Growth
1	Snap Fitness	1,012	1	Anytime Fitness	3,443	259%
2	Anytime Fitness	959	2	Snap Fitness	1,911	89%
3	24 Hour Fitness	425	3	Planet Fitness	1,303	320%
4	Powerhouse Gyms	327	4	LA Fitness	689	113%
5	LA Fitness	324	5	Orangetheory	570	N/A
6	Planet Fitness	310	6	9Round	449	N/A
7	EXOS	203	7	EXOS	439	116%
8	Town Sports	158	8	24 Hour Fitness	425	0%
9	ClubCorp	154	9	Pure Barre	400	2757%
10	Plus One	112	10	Powerhouse Gyms	315	-4%
11	Life Time Fitness	85	11	Plus One	300	168%
12	Club One	83	12	ClubCorp	206	34%
13	American Leisure Corp	68	13	Equinox	200	300%
14	Lifestyle Family Fitness	55	14	Crunch	175	821%
15	Equinox	50	15 (T)	CorePower Yoga	150	355%
			15 (T)	Town Sports	150	-5%
19	CorePower Yoga	33				
30	Pure Barre	14				

Source: Piper Jaffray

Legend

- High Value/Low Price
- Boutique Studio

As The Industry Expands, Understanding Both The Benefits And Risks Of Fitness Tenants Is Imperative

As mentioned, landlords have increasingly turned to fitness tenants to fill vacant space, in large part because they drive traffic. There are other benefits to having a fitness chain in your shopping center, including the following:

- **Fitness buildouts are generally expensive, which tends to make them “sticky” tenants:** In most markets, low-priced clubs cost between \$30-60/SF, larger boxes and franchises cost \$40-60/SF, and higher end clubs cost more than \$75/SF to build out. The significant upfront investment that fitness chains tend to make in their stores mitigates the risk that stronger operators will eventually leave the center.
- **At the high end, fitness centers are transforming into space with multiple uses:** Higher end centers often feature high quality food and drink options, complementary daycare, wi-fi, and exercise docking stations for laptops. Fancier gyms attract wealthier consumers and health club goers are well-monied compared to national averages. For instance, more than 40% of health-club members reported household incomes exceeding \$100,000 in 2016, according to IHRSA, compared with 26% of the overall population.
- **At the low end, fitness centers dovetail with off-price and budget trends:** Following the Great Recession, millions of workers shifted to part-time and contract work, asset prices increased at a faster rate than wages, healthcare and education costs rose, and budgeting became the norm. Off-price and discount retailers have proliferated since, and budget gyms like Planet Fitness mesh well with other budget retailers.

Despite the sector’s expansion, there are several risks to consider when adding a fitness use to your center, including:

- **Parking:** Gymgoers are notorious for monopolizing parking spaces at shopping centers, particularly during peak hours.
- **Lease Restrictions:** Many leases in power centers (e.g, from grocers and tenants like Ross and TJX) restrict fitness centers.
- **Market Saturation:** Competition in the fitness sector is intense with options ranging from gyms to boutique fitness studios that typically specialize in classes, typically with a pay-as-you-go pricing structure. At some point the relentless growth of gyms will slow and some will fail.
- **Excess Leverage:** As the chart below suggests, fitness chains – in particular 24 Hour Fitness – are highly leveraged. While debt has fueled the sector’s expansion, an economic slowdown or rising interest rates could impact chains at the corporate level.
- **Franchisees:** Chains that rely on a franchising model by nature are relying on individuals to expand their brand. The business acumen of these individuals can vary widely.

Fitness Buildouts Often Require Significant A TI Allowance



Source: Planet Fitness

Interest Coverage Averages 3.2x Across The Largest Chains, But Overleverage Tied To Rapid Expansion Could Be A Concern

Fitness Chain	Store Size (SF)	Sales Per Store (\$000s)	Sales Per Square Foot \$/SF	Rent Per Square Foot \$/SF	Occupancy Cost (%)	EBITDA (\$000s)	Total Debt (\$000s)	Debt to EBITDA (0.0x)	Interest Coverage (0.0x)
Planet Fitness	20,000	\$1,752	\$81.24	\$15.85	19.5%	\$184,700	\$703,761	3.8x	5.2x
LA Fitness	40,000	\$3,111	\$76.98	\$18.06	23.5%	\$296,296	\$1,600,000	5.4x	1.9x
Gold's Gym	35,000	\$2,585	\$71.06	\$22.40	31.5%	\$348,264	NA	NA	NA
Lifetime Fitness	114,000	\$12,453	\$106.19	\$19.00	17.9%	\$430,725	\$1,970,516	4.6x	3.5x
24 Hour Fitness	35,000	\$3,441	\$97.75	\$30.00	30.7%	\$210,938	\$1,350,000	6.4x	1.0x
Equinox	40,000	\$5,614	\$128.16	\$19.50	15.2%	\$199,200	\$996,000	5.0x	2.9x
Town Sports	38,000	\$2,641	\$67.34	\$22.16	32.9%	\$56,144	\$196,029	3.5x	4.5x
Average	46,000	\$4,514	\$89.82	\$21.00	24.5%	\$246,610	\$1,136,051	4.8x	3.2x

Source: CreditIntell