Kroger-Albertsons Merger Could Shake Up Supermarket Real Estate in California

Reduction in Store Count Could Open High-Traffic Locations to New Competitors

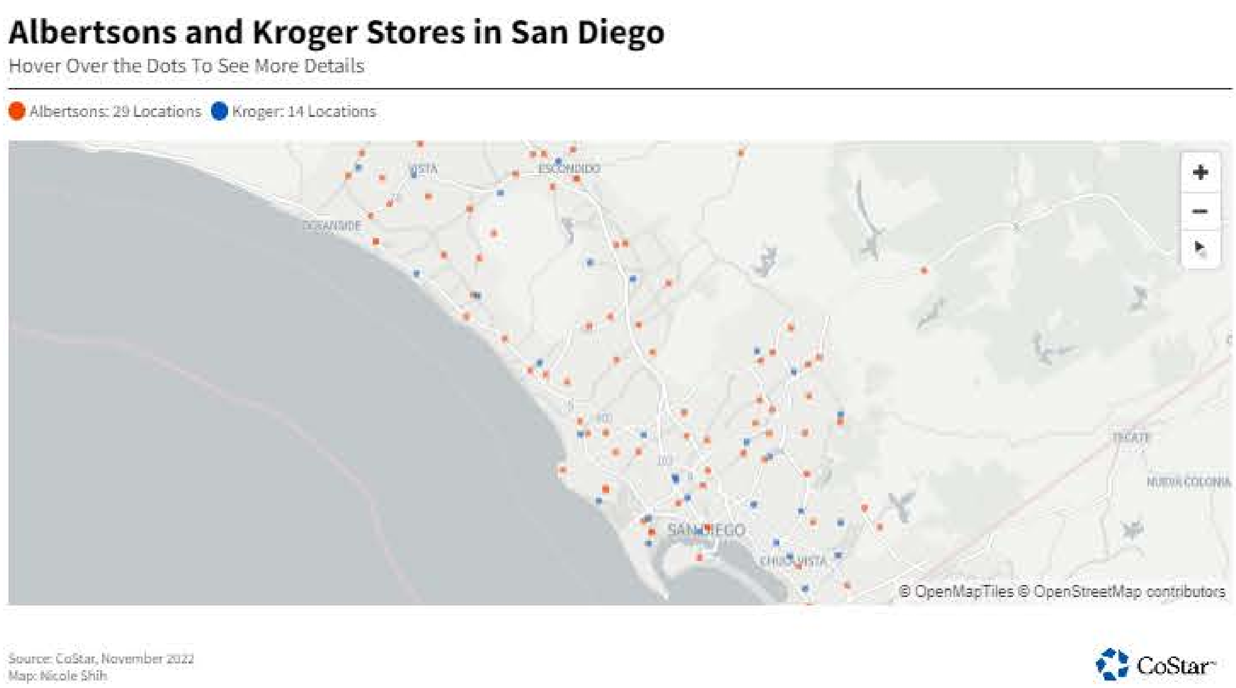
By Lou Hirsh

The proposed $24.6 billion acquisition-merger between supermarket giants Kroger and Albertsons could result in a national wave of store closures and selloffs as the grocers look to head off regulatory concerns about competitive balance. The shakeouts could be most pronounced in California, home to three brands in the deal with long histories and large footprints.

CoStar and company data show Kroger and Albertsons combined operate more than 1,000 stores in California, including multiple brands among the 667 Albertsons-owned locations and 356 Kroger-owned stores. A key issue in a merger review could be service overlaps in Southern California between Kroger-owned Ralphs and Albertsons-owned Vons, both with centurylong histories and multigenerational customer loyalties in the region.

“There are many places, like in San Diego, where you have a Ralphs and a Vons anchoring centers at the same intersection,” said Steve Avoyer, president of San Diego-based Flocke & Avoyer Commercial Real Estate, which handles leasing and management at more than 100 Southern California shopping centers. “There are changes that are going to happen, whether it’s closings or selloffs, and they’re not going to be able to avoid that in all those places.”

The two companies together currently operate nearly 5,000 stores, more than 2,000 fuel centers, 66 distribution centers and 52 manufacturing plants nationwide.



Location maps compiled by CoStar News show that overlap is likely to be limited in Northern California, where Kroger has traditionally had a minimal presence. There is considerably more overlap between Ralphs and Vons or Ralphs and Albertsons in Southern California, especially in Los Angeles and San Diego.

Executive boards of both companies have approved merger plans, and the chains are looking to complete the deal in 2024, if regulators approve the deal. In a bid to assuage concerns over competition, the two grocers have proposed placing between 100 and 375 stores, yet to be identified, into a spinoff company that would have its own traded stock and independent management.

Representatives of Kroger and Albertsons did not respond to requests from CoStar News to comment.

In a recent research note regarding the merger deal, retail analyst Scott Mushkin of R5 Capital noted there are several Western U.S. cities where high percentages of Kroger-owned stores are located within 3 miles of an Albertsons-owned store. San Diego has among the highest percentages at approximately 76.1%.

Mushkin noted that the proposed merger creates even higher service overlap percentages in the 3-mile radius in other Western regions, with Denver at approximately 90.5%, Las Vegas at 95.2%, Phoenix at 89.6%, Portland at 81.3% and Seattle at 87.4%.

Turnover Opportunity

Retail property landlords are preparing for changes ahead in California, and some tenant turnover could prove beneficial in the form of higher rents for spaces that otherwise have been occupied for years by the big supermarket chains under long-term leases.

“There’s a lot of demand out there from value-oriented and specialty grocers in these locations,” Stuart Tanz, CEO of San Diego-based Retail Opportunity Investments, a REIT that owns 93 grocery-anchored retail centers on the West Coast, said during an October earnings call with analysts. “So, if Albertsons and Kroger divest off some of these locations, we view this as a potential opportunity.”

Mike Moser, a partner at Solana Beach, California, brokerage firm Retail Insite, told CoStar News he has already “spoken to a few groups that are reviewing overlap and potential opportunities” for new locations in Southern California that are currently occupied by the merger-seeking supermarkets, though much depends on what locations and trade areas become available.

“I would assume that if the merger were to happen that there could be more forced closings or dispositions taking place here in California, given the market presence of both chains here,” Moser said. “If this were to happen it would open up the door for other chains to be able to expand into the market. This could be existing operators here already but not completely covering the market, or others from other regions.”

A merger-fueled shakeup could have unprecedented real estate consequences for two of the most popular grocery chains in Southern California. Kroger's primary footing in California consists of Ralphs, a mainstay in Southern California since its 1873 founding in downtown Los Angeles by brothers George and Walter Ralphs. Cincinnati-based Kroger in 1998 acquired Ralphs and its companion discount chain, Food 4 Less, which together total more than 270 stores.

Another regional mainstay is Vons, started in downtown L.A. in 1906 by Charles Von der Ahe and acquired in 1997 by what was then known as Safeway Inc., based in Pleasanton, California, and itself a decades-old mainstay of Northern California. Vons and its upscale companion brand, Pavilions, operate more than 200 stores.

Safeway, which included the flagship banner brand along with numerous others acquired over the prior 20 years, was purchased in 2015 by the private equity owner of Boise, Idaho-based Albertsons in what became the combined company now known as Albertsons Cos.

When federal regulators approved that earlier $9.2 billion merger, they required Albertsons and Safeway to first sell 168 stores to prevent unfair competition in 130 U.S. metropolitan areas. Post-merger, the combined company closed several other stores to eliminate duplication in neighborhoods where stores were deemed too close.

Avoyer noted that left the door open to numerous other grocery chains to establish or expand their Southern California footprints in attractive, high-traffic locations, including discount chain Smart & Final, specialty grocer Gelson's Markets and several regional grocers catering to the Asian and Hispanic communities.

He said that the same could result from a Kroger-Albertsons merger and that other chains that have been expanding for much of the past decade could also be seeking new location opportunities, including specialty grocer Trader Joe's and discount-focused Aldi.

Choice Locations

Avoyer noted, however, much depends on how many locations are ordered sold, where they are located and whether they are owned or leased by Kroger or Albertsons.

If some of the vacated spaces are owned by the grocers, as frequently is the case, the timetable for filling those spaces could be longer as the grocer may have different priorities, including filling the property with nongrocery tenants or just keeping it empty as long as possible to minimize neighborhood competition. Shopping center landlords may need to purchase those properties to gain faster access to them.

"Even if a lot of these spaces end up being closed, I can't imagine that a lot of them will stay empty for very long," Avoyer said. "It could really be an exciting time for some of these grocery companies and some of these landlords. You could be seeing a lot of dispositions, but you could also see a lot of other companies coming into these markets."

He noted that changes in store counts and locations could also affect logistics planning for a combined Kroger-Albertsons, including the possible closing or reconfiguration of distribution facilities. Company and public data show Kroger has two large California distribution centers, in Compton and Riverside near Los Angeles, while Albertsons has six in Los Angeles, Orange and San Joaquin counties.