

## Forecast calls for balanced US retail sector as market dynamics shift

*Years of limited construction offset supply additions from store closings*

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The U.S. retail market entered the final quarter of 2025 on firmer footing, following a turbulent first half of the year marked by elevated store closings and more space added than newly occupied.

However, market dynamics have improved thanks to demand for retail space turning positive in the third quarter and a slowing number of store closures. With new supply barely registering, the U.S. retail property sector is expected to remain balanced, with vacancy expected to rise only slightly over the coming quarters before easing toward 4.3% by the end of 2027.

This revised forecast is consistent with our previous outlook for the third quarter that similarly projected the national retail vacancy rate to peak under 4.4% in the second half of 2026.

Underpinning this stable outlook was the return of demand for additional store space in the third quarter. After two consecutive quarters of falling demand, retailers resumed their quest for space in the third quarter, as the pace of store closings slowed and backfill demand surged, resulting in a net increase in retail occupancy of 4.8 million square feet.

Strong demand to backfill recent closures helped push the net change in retail occupancy positive in the third quarter. This former Party City in the 380 Towne Crossing shopping center in McKinney, Texas, was available for three months before it was leased by Western apparel retailer Cavendars. (CoStar)

However, despite being very low by historical standards, the amount of new retail space added to the market still exceeded net absorption, a measure of the net change in occupancy, by 3.1 million square feet, causing the national vacancy rate to edge up to 4.3% in the third quarter.

Overall, retailers vacated 3% less space than in the prior quarter, as the pace of retailer move-outs moderated after the bankruptcy-driven closures involving major chains, such as Rite Aid, CVS, and Joann, wound down. Although receding, store closures are still expected to remain elevated over the coming quarters. They will continue to weigh on net absorption despite strong demand to backfill the space left behind by recently closed retailers. As

such, net absorption is expected to average just 3.8 million square feet per quarter in 2026, well below the prior five-year average of 9.8 million square feet per quarter.

Nevertheless, the latest forecast predicts a modest increase in retail vacancy of just seven basis points between now and the end of 2026, thanks to the near-historically low level of space availability, steady backfill demand, and minimal new supply in the development pipeline.

Retail construction starts have fallen to multi-decade lows, driven by sharply increased costs and the significant gap between current market rents and those required to support new development. As a result, construction activity is expected to remain subdued for the foreseeable future. This lack of new supply, combined with a reacceleration in retail sales growth expected in 2027 and 2028, underpins our outlook that the U.S. retail property sector will remain balanced over the mid-term, with the national vacancy rate holding within a tight range of around 4.3%.

The forecast carries both downside and upside risks, though the balance currently tilts to the downside. Significant uncertainty remains around the impact of shifting tariffs on an already cost-conscious consumer. While suppliers and retailers have largely absorbed these costs to date, many have signaled that price increases are imminent.

With consumers already showing signs of spending fatigue, tariff-related price hikes could further strain household budgets and curb discretionary spending, cooling demand for retail space. Additional downside risks include a softer labor market, resulting in slower wage growth and lower-than-expected population gains due to stricter immigration enforcement.