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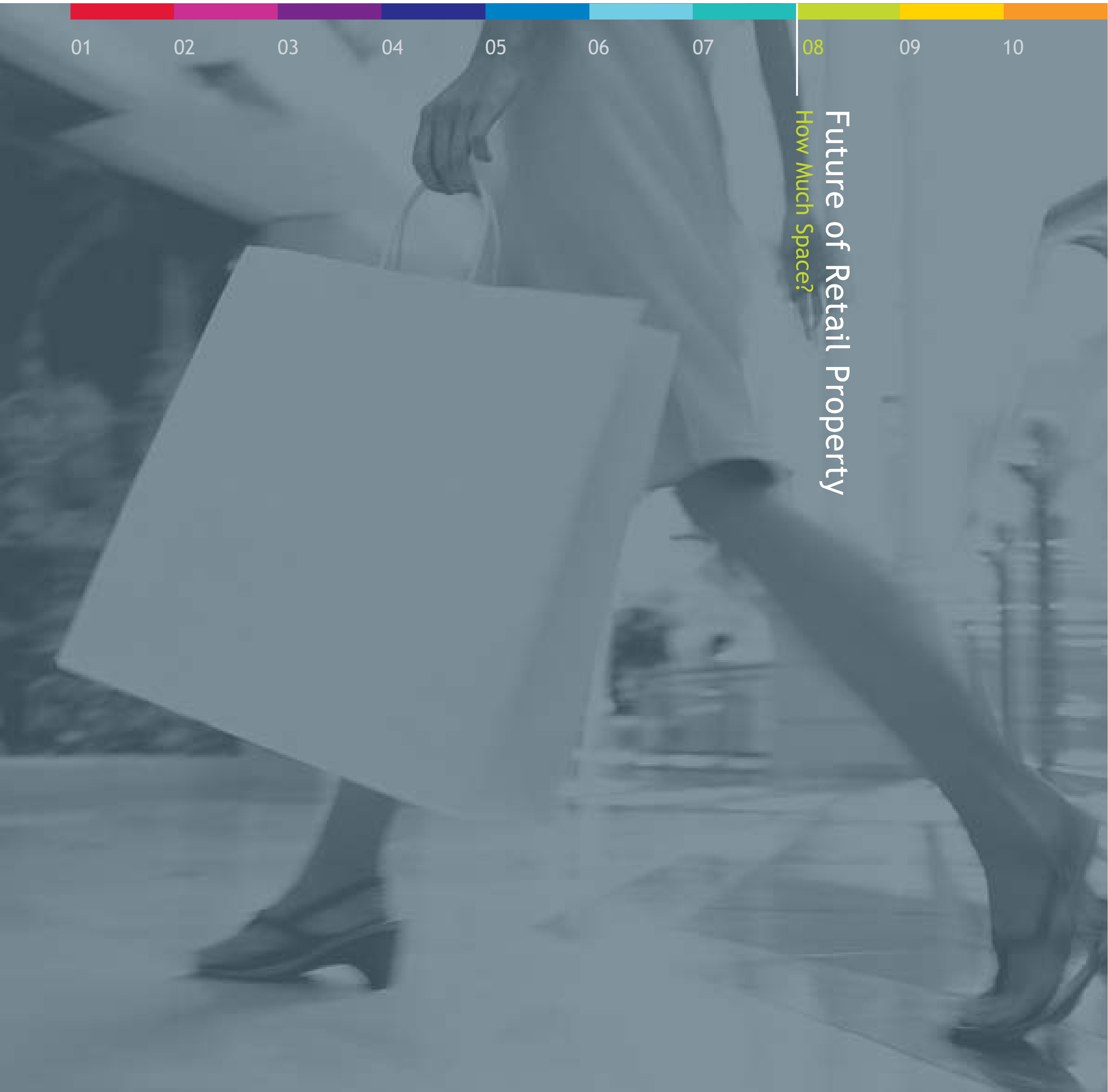
SHAPING RETAIL PROPERTY

Future of Retail Property

How Much Space?



The predicted slowdown in sales growth, the expansion of internet shopping and the potential for increases in sales per square metre are factors likely to impact on the need for additional retail floorspace over the next decade.

At the same time, in some areas more retail space will be required – but in which regions and in what timescales?

We are delighted to present this informative piece of research which examines the varied factors affecting patterns of growth in retail space over the next ten years.

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How Much Space?

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Introduction

This report examines the future requirements for retail space, particularly for the type of non-food stores commonly found in shopping centres.

The demand for shopping space originates from consumers' need to buy retail goods from shops. The first two sections explore the likely future for in-store spending on retail goods. Section one focuses on those economic factors that determine how much individuals and households spend, and what proportion of this expenditure is on retail goods.

Spending on retail does not have to take place through shops, which have always had competition from other outlets such as market stalls and mail order. Now it is internet retailing, or e-tailing, that is in the news and there is a widespread concern that booming internet sales might take a substantial chunk of retail spending away from traditional shops. Section two tries to quantify the growth of the internet shopping phenomenon and speculates about what share of the retail market the internet might eventually account for.

The opening sections give a view of how much additional spending is likely to go through shop tills between now and 2015. But translating increased spending into an increased need for shopping space is not straightforward. The complex relationship between the two means a 10% increase in spending is unlikely to equate to a 10% increase in the amount of retail space.

Sales per square metre (also described as sales densities) vary for a number of reasons. Different shop types have different sales per square metre. Food shops, for example, tend to have higher sales densities than non-food shops. Also, successful shops will have higher sales per square metre than failing shops. There are also national characteristics with shops in the USA, for example, tending to have more room and lower sales densities than similar outlets in the UK.

The main concern here, however, is if and how sales per square metre can change over time. If these can increase without any adverse effects from overcrowding, then a 10% increase in spending will mean that an increase of less than 10% is needed to service the extra spending. There is a tendency for sales per square metre to increase year-on-year, especially for non-food stores, and section three looks at how this can happen and what the trends in the future are likely to be.

In section four, the report estimates the future need for additional shopping space and assesses the particular requirements arising from the split between food and non-food items. Increasingly, food stores also sell non-food items and the expansion of non-food sales by supermarkets and hypermarkets has resulted in less spending in non-food outlets. Yet it is non-food (or comparison) shops that form the great majority of shopping centre tenants. The amount of space supermarkets and hypermarkets use for selling non-food items in the future is another key consideration in planning future space requirements for comparison retailing.

According to CBRE there are currently 7,840,000 square metres of new non-food space in the pipeline, equivalent to about 14% of the existing stock.

Section four asks if future spending levels will be sufficient to make use of the additional shopping space. This section examines the likely regional balance between additional retail spending and new shopping space in the pipeline. This section also considers different scenarios to assess plausible but extreme cases relating to projected requirements. The scenarios cover increases in spending, the growth of the internet, the potential increase in sales densities and the amount of non-food sales made through supermarkets and hypermarkets.

The final scenario looks at the implications of a radical change to the planning regime in the UK. British planning policy has wavered between the restrictive and not-so-restrictive but it has never been as liberal as in the USA. This scenario looks at the impact of introducing a US-style planning regime allowing US-scale sales densities. Such a move would have been considered completely implausible until recently and it is still highly unlikely. Nonetheless, some of the ideas from the recent *Barker Review* relative to the economic effects of land use planning could be seen as pointing in the direction of US-style planning so the scenario is an interesting one to consider.

The demand for shopping space originates from consumers' need to buy retail goods from shops.

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Section 1
Executive Summary

Summary and conclusions

The future for retail spending

Spending on retail goods has boomed over the past decade or so, particularly spending on non-food or so-called comparison goods.

In part this has been due to a generally benign economic climate. Total household incomes and all the goods (e.g. clothes, electrical appliances) and services (e.g. meals out, holidays) bought by UK households have also seen strong growth. Increased spending on comparison goods has been helped by cheaper prices, a result of the introduction of new technology and the flood of cheap imports from China and other parts of the Far East.

The next ten years are likely to see comparison goods volume growth slowing down for a number of reasons:

a. The upsurge in borrowing and run down of savings seen over the past ten years is unlikely to be sustainable. Consumer indebtedness, compared to income, has reached new highs leaving many consumers increasingly uncomfortable with the size of their borrowings.

b. The surge in house prices relative to incomes, which has permitted 'equity withdrawal' to finance consumer spending, cannot persist at the same rate as it has done over the past decade.

c. Low high street prices caused by the flood of goods imported from the Far East are coming to an end. China is now a much more developed economy seeking to raise living standards rather than to export at any cost, and there is even the possibility of the revaluation of the Chinese currency, the renminbi, which would hold back any further falls in imported goods prices.

All of this adds up to a forecast annual average increase in the volume of spending on comparison goods of 4.3% a year between 2006 and 2015.

As well as being much less than the average annual increase of 7.4% recorded over the last decade this is also less than the 40-year average of 4.9% often used in retail planning enquiries.

The pension crisis could result in even lower rates of spending growth but a combination of better state provision, the spread of low cost schemes and, especially, later retirement will probably stave off a crisis.

Non-store sales and the rise of the internet

Not all retail spending takes place through shops. In the past, mail order, door-to-door and street markets sales have all flourished independently. More recently there has been a spectacular expansion of internet shopping allowing retailers to sell directly from the warehouse in higher volumes than ever before.

In the next decade, online sales will grow as both consumers and retailers take advantage of the internet. The market shares of comparison goods and convenience goods accounted for by the internet and other forms of non-store retailing are expected to rise to 12.4% and 6.5% of total non-store sales. This assumes growth for both is still rapid, but slower than that seen between 2000 and 2005.

The increase in internet shopping will mean that the annual average growth in in-store sales of comparison goods will be 3.6% a year rather than the 4.3% growth of all (in-store and non-store) spending on comparison goods.

Sales per square metre

Increases in spending can be met by an increase in sales per square metre as well as by new space.

Different shops have different sales per square metre, with food shops tending to have higher rates than non-food shops. Successful shops will have higher sales per square metre than failing shops.

What matters here is the potential for sales per square metre to change over time. The evidence is that sales per square metre, adjusted for inflation, have seen quite rapid increases in the past, particularly between 2000 and 2005.

Some of this was due to the introduction of Sunday trading and some was associated with the spending boom. However, these rapid increases are not sustainable. Sales per square metre for comparison goods are expected to increase by 2.2% per year over the next decade. This is considerably below the 2.9% estimate for the period between 1987 and 2005.

The onset of 24-hour trading could increase sales per square metre much further, but its widespread adoption is unlikely in the next decade.

Summary and conclusions

The amount of potential new space in the development pipeline is considerable and will be enough to provide for practically all of the projected sales growth over the next decade.

How much retail space

Given the projections of in-store retail spending, the likely changes in sales per square metre, and taking into account comparison goods selling space in supermarkets and hypermarkets, it is possible to estimate future retail space needs.

The proportion of convenience store space given over to selling comparison goods rather than to traditional convenience goods such as food is projected to increase to 25% by 2015 up from 21% in 2005. Without the increase in comparison goods sales there would be barely any need for additional convenience store space over the next decade.

The calculations show a need for 6,090,000 square metres of additional (gross) comparison store space in England and Wales between 2006 and 2015. This is an increase of approximately 10% on the 2005 stock.

This estimate does not take into account the existing development pipeline or any demolition that will take place as a result of new development. Estimates from CBRE show a total of 7,840,000 square metres of potential new comparison space in the development pipeline. Even allowing for possible demolitions needed to make way for the new developments, on the basis of projected increases in spending by 2015, there is little scope for many additional schemes over and above what is in the current pipeline. Adding in demolitions gives an additional development requirement of just 484,000 square metres – which is little more than three big shopping centres.

Estimates based on BCSC's pipeline data indicate that there may be substantial regional variation. The development pipeline looks to be inadequate to meet needs in the south of England while there appears to be a possible excess of developments in the North West.

Scenario analysis

Both high and low scenarios were tested for all of the key forecasts (spending growth, internet sales, growth in sales per square metre and comparison goods sales in supermarkets and hypermarkets).

The low cases had a marked impact, particularly for spending growth, growth in sales per square metre and increased non-food sales by convenience stores. Each of these would cut net additional space requirements by more than half, before any consideration of the existing pipeline. If more than one of them were to occur there would be no need for additional space, even before taking the pipeline into account.

A move to a more liberal planning regime that led to sales per square metre approaching US levels would provide a major boost to retail floorspace demand, so much so that the implied increase in the demand for space could not possibly be built within a ten-year period.

Such a change is unlikely and would be counter to the Government's sustainability policies. Nonetheless, some of the ideas from the recent *Barker Review* relative to the economic effects of land use planning could be seen as pointing in the direction of US-style planning. This scenario illustrates the order of magnitude of such space implications.

Conclusions

A slowdown in sales growth, the expansion of internet shopping and the potential for increases in sales per square metre are all contributing towards limiting the future need for additional comparison floorspace.

At the same time the amount of potential new space in the development pipeline is considerable and will be enough to provide for practically all of the projected sales growth over the next decade. Allowing for the existing pipeline, projected spending growth would justify little more than three big new shopping centres.

There are significant regional differences. There appears to be a lack of new developments in the pipeline in the south of England relative to likely sales growth. Other areas, particularly the North West, could actually have a surplus of new developments although they may be justifiable on regeneration grounds rather than simply to provide for future spending increases.

All of the calculations assume that the UK's high sales per square metre are maintained and, indeed, that they will rise further. A change to a more liberal planning regime that permitted more developments and lower sales per square metre would create a development boom but is unlikely given current policies on sustainability.

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