

Spotlight European Shopping Centres Investment benchmark

November 2013

Consumers' optimism to drive an upturn?

After five years in the crisis Europe seems to be about to turn a corner. Recent indicators point to an economic upswing; in the second quarter of the year GDP rose by 0.3% both in the EU27 and in the Eurozone, thus ending six consecutive quarters of contraction - the longest recession in the Eurozone's history. Germany and France led the rebound, growing by 0.7% and 0.5% respectively. Meanwhile, persistent weakness in peripheral countries remained although at a lesser extent. Spain contracted 0.1% over the previous quarter and Italy dropped by 0.2%.

This follows some improvement in industrial production recorded in June and boosted economic and consumer sentiment. According to the European commission in August consumer

confidence continued its upward trend that started in December 2012 and increased by 1.8 points. Consumers' opinions on the future financial situation of their households and on their savings over the next 12 months also brightened. Yet the weakness of the labour market continues to weigh on consumer spending. The unemployment rate in July was unchanged at 12.1% at record high level despite the second consecutive drop in the number of unemployed.

Retail trade confidence also increased substantially (+3.3) as managers were more positive about the future business situation and their volume of stocks improved markedly. In the last European shopping centre opinion survey, the ICSC also reported a high Euro-Shop Index figure thanks to strong shopping centre sales and good occupancy and footfall performances.

Summary

■ This report presents the results of our second shopping centre (SC) investment benchmark which analyses the market size, retail prospects, the market stability and the potential return across 16 European countries.

■ Germany ranks number one as a core destination for shopping centre investment, followed closely by the UK, France, Norway and Sweden.

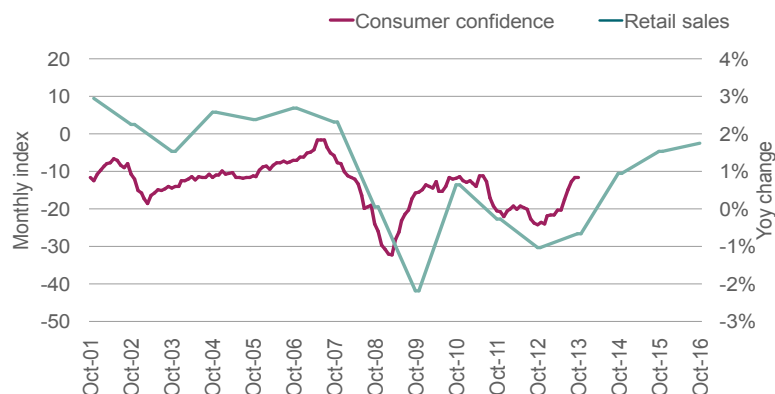
■ Romania, Poland, Hungary, the Czech Republic and Austria have made the top five ranking of opportunistic destinations.

■ Consumer confidence is growing in all areas surveyed helping to spur on a positive outlook for the retail trade.

■ Investor focus on the prime segment of the market has materialised by an overall inward yield shift. The average prime shopping centre yield in the surveyed area moved in by 15 bps between Q3 2012 and Q3 2013 and stands at 6.30%.

■ From next year the prime yield gap between Core and non-Core countries could start slowly narrowing as investment activity is expected to broaden to the whole of Europe.

GRAPH 1
Consumer confidence vs retail sales



Graph source: European Commission, Oxford Economics



"We expect the non-core countries to grow on investor radar seeking prime opportunities, which have become rare and "high-priced" in core countries." Lydia Brissy, Savills

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Retail investments

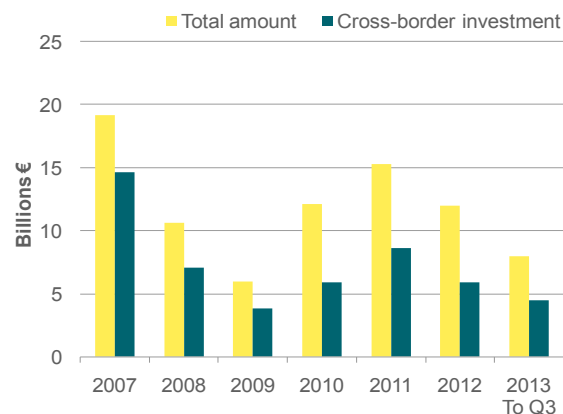
After a weak start during the first half of the year, investment activity in the retail segment and particularly in shopping centres improved significantly. According to Real Capital Analytics in Q3 the shopping centre investment volume in the 16 countries covered in this report doubled compared to the previous quarter and reached €3.8 bn. This brings the volume invested since to the beginning of the year to nearly €8 bn, a similar level to that of last year during the same period.

Activity revival in the sector is first due to increased cross-border inflows (+7% since the beginning of the year compared to the same period last year). Cross border investments accounted for nearly 70% of the total shopping centre investment volume. Secondly, it is attributed to the recent renewed investor interest for non-core countries, particularly in Poland, Spain and Italy where prime assets are available on the investment market as opposed to core countries. The UK

and Germany still account for 60% of the SC investments recorded since the beginning of 2013.

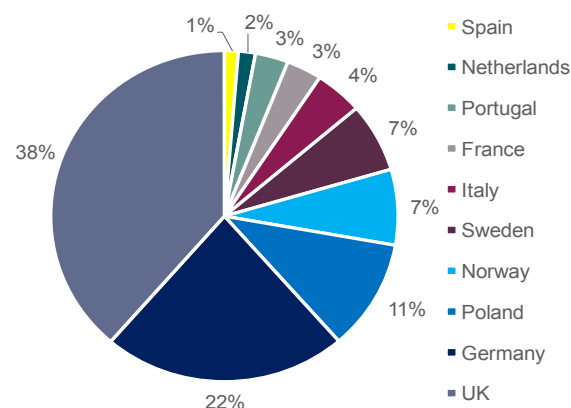
Investors' focus on the prime segment of the market has materialised by an overall inward yield shift. The average prime shopping centre yield in the surveyed area moved in by 15 bps between Q3 2012 and 2013 and stands at 6.3%. The other main contrast with last year is that this trend has affected nearly all locations covered in the report with the exception of Budapest, Milan and Lisbon (+25 bps) while Vienna, Berlin, Amsterdam, Oslo, Warsaw, Madrid and Stockholm remained stable. As a consequence the average yields gap between Core and non-Core countries tends to stabilise and reached 150 bps compared to 151 last year suggesting the gradual re-widening of the prime shopping centre market to non-core destinations.

GRAPH 2
SC investment volume Increasing cross-border investments



Graph source: RCA

GRAPH 3
SC investment volume in 2013 (to Q3)
UK and Germany accounting for 60%

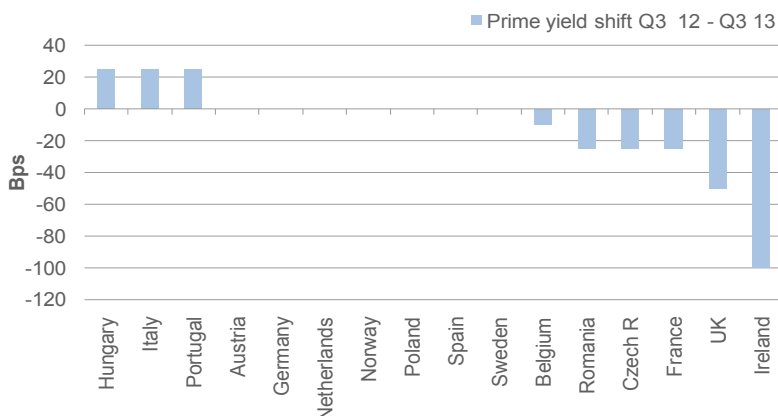


Graph source: RCA

“2014 will be an exciting year as investors have to deploy capital. There will be a strong debate amongst investors as to whether to invest in secondary product in core countries or core schemes in secondary countries.” Oliver Fraser Loonen, Savills European

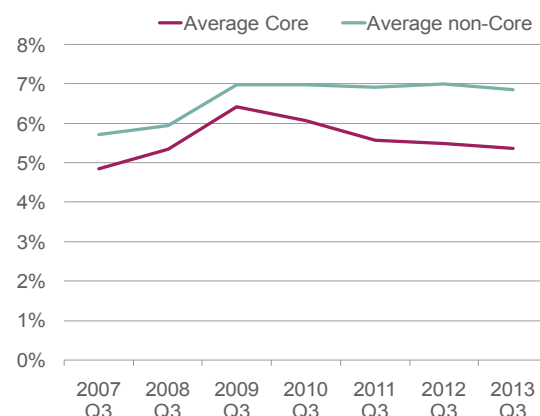
Investment

GRAPH 4
Prime shopping centre yield shift Strong appetite for prime assets led to an overall inward yield shift



Graph source: Savills

GRAPH 5
Average prime yields The gap between Core and non-Core countries stabilising



Graph source: Savills

Ranking results

Top five core destinations

■ **Germany** remains the safest country in Europe to invest in shopping centres still thanks to strong economic fundamentals. Although the country steps back from the 5th to the 6th position in terms of consumer spending per inhabitants it remains the biggest consumer spending market in Europe with a low unemployment rate, the 3rd lowest after Norway and Austria, one position better than last year. Bond yield is also the lowest across the covered countries. Yet the volume invested in shopping centres since the beginning of 2013 is significantly lower than during the same period last year. This results from a lack of prime opportunities available on the market, which has forced investors to seek other types of retail properties. Indeed, most prime shopping centres changed ownership in the past 2-3 years.

■ With the 2nd largest consumer spending volume, the 2nd highest consumer spending per inhabitant and the 3rd largest volume of shopping centre sales, the **UK** still stands out as second in our ranking results. The UK has been the best performing country in terms of investment activity and accounted for nearly 38% of all shopping centre transactions recorded in 2013 (to Q3) in the surveyed area. Further stratification of retail centres by trading performance has resulted in disposals providing the market with investment opportunities. Consequently, the prime shopping centre yield hardened by 50 bps between Q3 2012 and Q3 2013 and stands at 5% which remains attractive compared to France (4.75%) and Germany (4.9%) on top of the fact that the UK is a non-euro alternative to investors looking to avoid exposure to the Eurozone.

■ Market stability, consumer size and volume of shopping centre sales (the biggest within the surveyed area), remain the key components to attract shopping centre investors in **France** which kept the 3rd position in our ranking. Even so shopping centre

“Some CEE countries will offer good investment potential thanks to strong retail sales prospects and increasing development activity. Whereas some peripheral countries will offer opportunities arising from distressed sales.” Lydia Brissy, Savills

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investments decreased significantly during the first three quarters of the year. Strong investment activity recorded during 2010 and 2012, notably in 2010 has brought about a scarcity of prime shopping centre opportunity in the French market. Additionally, the prime yield, which stands at 4.75% has become the lowest in the surveyed area following an inward shift of 25 bps during Q3 2012 and Q3 2013.

■ **Norway** remains on the 4th line of our top five core destinations. Not only is Norway the best performing western European countries amongst the EU27 in terms of GDP growth, but the unemployment rate is still the lowest across Europe and Norwegians are still the biggest consumers compared to the 15 other nationalities. Strong economic fundamentals, good rental growth (+9.3% pa over the past five years) and attractive prime yield that currently stands at 5.5% have raised investors' appetite. Shopping centre investment since the beginning of the year nearly tripled compared to the same period last year. Cross-border investments also doubled over the considered period.

■ **Sweden** kept its 5th position in our top five results in spite of a weaker position in terms of employment and consumer spending per inhabitant, but Swedish nationals remain the 4th biggest consumers amongst the 16 countries covered. The investment volume recorded between January and September fell by nearly 24% compared to the same period in 2012. This can be attributed to the exceptionally strong investment activity in the sector last year. Yet the volume of investments is the 5th biggest after the UK, Germany, Poland and Norway.

METHODOLOGY

This research covers 16 European countries including Austria, Belgium, Czech R., France, Germany, Hungary, Ireland, Italy, Netherlands, Norway, Poland, Portugal, Romania, Spain, Sweden and the UK. It benchmarks shopping centre investment opportunities at country level based on four main market features: market size, retail prospects, market stability and potential return. Market criteria and data used for this analysis are weighted according to investment strategies, from core to opportunistic investments. Market size, economic stability and sustained consumer spending have been put at the forefront to define core destinations. Consumer spending, retail growth prospects and development potential are the criteria standing out to define opportunistic destinations.

Criteria	Data	Source
Market size	Consumer spending in €m	Oxford Economics
	Consumer spending / inhabitants	Oxford Economics
	Shopping centre sales	ICSC / Savills
Retail prospects	Consumer spending prospects	Oxford Economics
	Retail sales prospects	Oxford Economics
	SC stock per inhabitant	Savills
Market stability	GDP stability	Oxford Economics / Savills
	Unemployment	Oxford Economics
	Bond yield	Oxford Economics
Potential return	Annualised 5-year rental growth	Savills
	Annualised 5-year total return	IPD
	Capital growth	IPD

Note: The views expressed herein are based on macro level statistics and do not take into consideration regional specificities or shopping centre standards. Certain data in this research paper were supplied by external sources and are believed to be reliable as of the date presented. Information presented herein is for discussion and illustrative purposes only and is not a recommendation or an offer or solicitation to buy or sell any properties. The information contained herein is subject to change without notice.

Ranking results

Top five opportunistic destinations

■ **Romania** came at the top of the five opportunistic destinations. This is mainly due to strong economic prospects. GDP is expected to grow by 1.8% at year-end, making it the best performing country within the surveyed area. Consumer spending and retail sales are also expected to show the fastest growth in the next five year with 2.7% and 2.9% pa on average. Additionally, the unemployment rate which currently stands at 7.1% is the top five lowest of all the countries analysed and the lowest within the CEE region. The shopping centre density remains the lowest across the 16 countries and demand for retail development is strong. Prime shopping centres, particularly located in Bucharest are attracting both domestic and international investors notably US value-add funds. Consequently the prime shopping yield moved in by 25 bps between Q3 2012 and Q3 2013. However, with the prime yield currently standing at 8.5% Romania is one the most attractive countries in terms of pricing within the surveyed area and also within the CEE region.

■ Although the **Polish** economy, which was the fastest growing in the past three years, is slowing down with GDP growth expected to be at 0.9% in 2013, it is still positive and above the European average. Additionally over the next five years consumer spending and retail sales should increase by 2.7% pa on average, the second best level of growth after Romania. However, due to the deterioration of the economy the labour market is weakening and the unemployment rate remains high (10.7%). The prime shopping centre yield stands at 5.75%. Shopping centre investment activity surged during the third quarter of the year thanks to the sale of the Silesia City Center bought by Allianz and the Bank of China. Although development activity is picking up, shrinking availability in the prime segment may curb the investment market in 2014.

■ Forecast for consumer spending and retail sales in **Hungary** until 2017 are respectively 1.3% and 1.1% pa on average, which is above the European average. The shopping centre density per inhabitant remains the second lowest across the 16 countries, which provide large potential for development and investment opportunities. Until now, the economic crisis and the tight financing conditions have not allowed development activity to pick up. The prime yield, which currently stands at 8.0% is the second most attractive in terms of pricing.

■ GDP growth in the **Czech R.** is expected to be below the European average, -1.0% at the end of the year but from 2014 the country should recover faster than all other 16 countries (same as Norway) with +2.2% expected at year-end. Over the next year consumer spending should grow on average by 2.1% pa the 6th best position in the surveyed area and retail sales by 2.5% pa, the 4th best percentage. The unemployment rate currently at 7.50% is relatively low. Shopping centre investments have been relatively limited since 2011 when the best volume of shopping centre investments had been recorded since 2006. But development activity is growing again with shopping centres on developers' radar.

■ **Austria** remains on the last position our top five opportunistic destinations. The current spending per inhabitant is amongst the fourth highest of the survey area and consumer spending is expected to rise by 1.3% pa on average until 2017, just in line with the European average. The Austrian population still benefit from a very low unemployment rate at 5.1%, the lowest rate after Norway. Shopping centre density per inhabitant remains limited, the 5th lowest of the surveyed countries, providing good development and investment opportunities. The average annual rental growth over the past five years (2.2%) and the average annual IPD retail return (6.1%) are both within the top three of the surveyed countries.

Austria and Poland, although ranked as 5th and 2nd respectively in our top five opportunistic destinations in terms of retail prospects and returns are much better placed in terms of market size and market stability than the other CEE countries which could position them as "core" destinations within Eastern Europe.

TABLE 1

Top five shopping centre deals - January to September 2013

Date	Country / City	Name	Buyer	Seller	Price in million
Q3 13	Poland / Katowice	Silesia City Center	Allianz / Bank of China	Immofinanz	€412
Q3 13	Germany / Munich	Hofstatt	Quantum Immobilien AG	LBB Immobilien	€400
Q3 13	Spain / Zaragoza	Puerto Venecia	Orion Capital Managers	British Land	€145
Q3 13	Aberdeen, Scotland / UK	Bon Accord and St Nicholas	F&C REIT	Land Securities / British Land	€227
Q3 13	Glasgow, Scotland / UK	St Enoch Centre	Blackstone / Sovereign Land	Ivanhoe Cambridge	€218

Table source: RCA, Savills

Conclusions and outlook

Overall, the recent positive shift in economic indicators and consumer confidence should slowly translate into increasing consumer spending. However substantial differences between countries will persist. Countries with good economic growth, high savings ratio and/or strong consumerism culture will lead the trend. At the other end of the spectrum over-indebted governments and weak labour markets will continue to drag on spending in the troubled fringe countries. Retail sales in the survey area are expected to continue to decrease until the end of 2013 (-0.4% yoy). From 2014 it should turn positive (+1.0% yoy) with only Italy (-0.8%), Spain (-0.4%), Portugal (-0.4%) and the Netherlands (-0.2%) still expected to record negative figures.

Investor appetite for quality shopping centres will continue, fuelled by brighter economic prospects. On one hand we expect non-core countries to grow on investor radar seeking prime opportunities which have become rare and "overpriced" in core countries. Some CEE countries will offer good

investment potential thanks to strong retail sales prospects and increasing development activity. Peripheral countries including notably Spain and Italy will offer attractively priced opportunities arising from distressed sales as suggest by the recent activity revival recorded in these two countries. On the other hand in core markets we expect the investment activity to be increasing restrained in the prime segment. It is likely that only one or two prime centres will be traded in each country, bought by global capital source at keen yields. This means that in core countries the investment market will head into secondary assets.

Strong competition for prime products will lead to further hardening of prime yields in most markets covered in the survey area. The current prime average yield remains 90 bps above the average recorded at the top of the cycle in Q2 2007 (5.4%). The prime yield gap between core and non-core countries will start slowly narrowing. Increasing demand for secondary assets in core countries will put inward pressure on secondary yields. ■

"We expect the recently improved market sentiment in Spain and Italy to lead to increased investment activity in 2014." Danny Kinnoch, Savills European Shopping Centre Investment

Market size

Rank	Country	Grade 2013*	yoy trend
1	UK	85.4	►
2	France	77.1	►
3	Germany	77.1	▲
4	Italy	66.7	►
5	Sweden	60.4	►

Market stability

Rank	Country	Grade 2013*	yoy trend
1	Austria	79.2	▲
2	Germany	77.1	▲
3	Netherlands	77.1	►
4	Norway	72.9	►
5	Belgium	62.5	▼

Retail prospect

Rank	Country	Grade 2013*	yoy trend
1	Romania	93.8	►
2	Poland	77.1	►
3	Czech R	66.7	▼
4	Hungary	62.5	▼
5	UK	56.3	▼

Potential return

Rank	Country	Grade 2013*	yoy trend
1	Austria	68.8	▲
2	Poland	64.6	►
3	Hungary	54.2	▼
4	Netherlands	54.2	▲
5	Portugal	54.2	►

Table source: Savills / * 1 = low - 100 = high

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Please contact us for further information



Nick Hart
Shopping Centre Investment
+44 (0) 20 7409 8837
nhart@savills.com



Danny Kinnoch
European Retail Investment
+44 (0) 207 409 8864
dpkinnoch@savills.com



Oliver Fraser Looen
European Retail Investment
+44 (0) 7807 999 582
oflooen@savills.com



Lydia Brissy
European Research
+33 (0)1 44 51 73 88
lbrissy@savills.com

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