

Market in Minutes

Retail investment in Europe rebounds

November 2018

Consumer confidence is elevated

■ Consumer confidence in Europe is elevated with the indicator well above its long term average. This reflects the positive sentiment created by strong labour market and low interest rates. Private consumption is forecast to rise by 1.5% this year and 1.6% next year.

Rebound of investment activity

■ Retail investment achieved a healthy turnover of €21bn over the first three quarters of the year, with an overall increase of 8% yoy. This is still 23% below the current cycle peak at 2015. Activity was driven by some sizeable portfolio deals across markets.

■ Retail investment increased by 23% in France and 15% in Germany, while significant rises were noted in the non-core markets of Belgium (229%), Italy (52%), Poland (80%).

■ Germany has overtaken UK as the largest investment market accounting for 24% of the activity compared to the

UK, which has dropped from 24% last year to 19% in the first three quarters of 2018. Poland and Italy increased their shares from 6% to 10%.

Large portfolio transactions boost volumes

■ There were 59 portfolio deals in the first three quarters of the year, down from 103 last year, but still above the long term average (10-year) of 40 portfolio deal pa. Once again the majority of the transactions took place in Germany, with 15 portfolio deals, followed by 12 in Spain.

■ About one third of the deals were retail warehousing and retail park portfolios, with ten in Germany and four in Sweden. 11 involved the transaction of supermarket/hypermarket portfolios, mainly in Germany and Italy and another four deals in Germany can be attributed to the restructuring of the department store sector. Consolidation and sale and leaseback deals were also behind the drivers of some of these larger transactions.

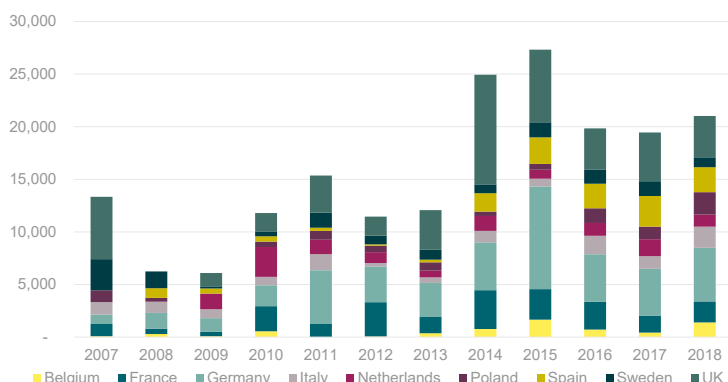
■ Despite the lower number of portfolio deals the total volume was 24% above last year, reflecting the larger size of portfolios transacted. The average size of deal was €124m, double last year's size. In Poland, Germany, Italy and Spain, some of the largest portfolio deals were recorded.

Non-core markets still catching up

■ Investment in shopping centres (SC) increased by 11% yoy though it is still 40% down from the high levels of 2014. This result was driven by the non-core markets which are still catching up with the cycle: in Italy, the total SC turnover increased by 158% yoy in the first quarters of the year at almost €1.2bn and Poland saw a 82% rise yoy at €2.1bn. In Belgium also an impressive €1bn SC transaction turnover was achieved.

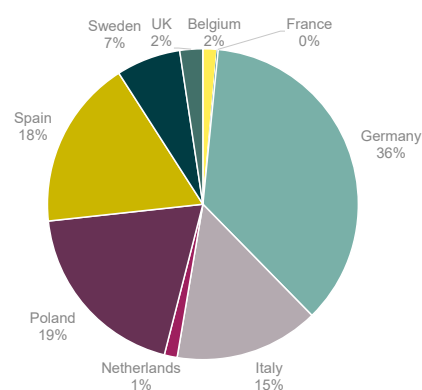
■ Availability of opportunities, relatively attractive pricing and in the case of Poland the dominance of shopping centres as the main retail and leisure destination for the consumer were the

GRAPH 1
Retail investment in Europe Q1-Q3 8% higher than last year



Graph source: Savills

GRAPH 2
Portfolio deals per country (volume) in Q1-Q3 2018



Graph source: Savills

→ main reasons behind these trends. Poland has become the largest shopping centre investment market in our survey area overtaking the UK and Germany and capturing 23% of the total.

The share of retail warehouses normalises

■ Over the past five years retail warehouses/parks increased significantly their share of total retail investment activity, from an average of 10% pa between 2007-2012 to 30%. In the first three quarters of 2018 their share has fallen back to 27% as the market is drying up from prime product and repositioning opportunities, which have driven activity previously.

■ Total turnover in the Q1-Q3 2018 was down 24% yoy to €5.7bn. Highest drop was noted in Spain (-64%) due to a record year in 2017. On the other hand Poland, Belgium and Italy have more than tripled their investment volumes, although Poland and Belgium shares are small 1% and 3% respectively.

■ The largest market was still the UK with €2.5bn turnover accounting for 43% of the total, followed by Germany, which captured another third of the market and exceeding €1.9bn.

Prime high street as a defensive choice

■ The role of high street transactions has been notable in a number of markets, such as France, where they account for over 50% of the total, as well as Spain and the Netherlands, at

about 30%, while in Italy and Belgium the capture about one fifth of the total.

■ Overall, quality high street units in shopping streets with strong footfall and rising tourist numbers are highly sought after by investors, considered to be a defensive choice against the disruption caused by online retailing to secondary retail destinations.

Yields compressing

■ The average achieved yield has been compressing since 2014. Over the past four quarters the average achieved yield moved in by 40bps to 6.5% (yield evidence for about 30% of our deals, excluding high street). 54% of the deals achieved a yield below average, compared to 48% last year, reflecting investor focus on prime product.

e-commerce deterred some investors from increasing their exposure in the sector. Nevertheless this same reason makes both landlords and tenants of physical retail to rethink their strategies and become more proactive.

■ This year's activity has been underpinned by the need for adjustment to an era where the role of physical retailing is changing: consolidation, sale and leasebacks, repositioning of existing retail schemes, the emergence of new concepts and the repricing of secondary assets have offered new opportunities to investors.

■ So far this year's turnover is still 38% above the 10-year average, so despite this year's rebound it may need to normalise further, under the pressure of

“Retailers and landlords are adjusting to the changing role of physical retailing. This brings new investment opportunities in the market” Oliver Fraser Looen, Savills retail investment

■ Based on the available evidence the lowest average yield was achieved in France (6.1%), followed by the UK (6.2%).

Outlook - towards a hybrid asset?

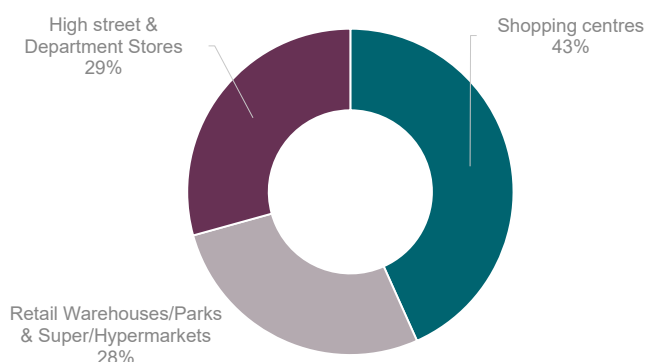
■ The rebound of the retail sector may have come as a surprise following two years of falling investment activity, as the disruption caused by the rise of

the rising share of online sales. At the same time, some of the existing retail formats may convert to service the rising property needs of e-commerce. The demand for click and collect points, local fulfillment centres and urban warehouses for last mile delivery, can potentially lead to a hybrid type of asset, which serves logistics needs but is strongly linked to retail fundamentals. The convergence of retail and logistics yields is a first indication of this possibility. Historically industrial yields were on average 160bps above shopping centres. This gap has halved to 80bps in Q3 18.

■ Average prime shopping centre yields have stabilised to 4.5%, while they continue to compress for the rest of the sectors. The average achievable prime yield for retail warehouses/parks was at 4.9%, 50bps below last year and for high street units at 3.2%, 20bps lower yoy. We expect this inward yield shift to slow down over the next year.

■ In the following section we discuss the rising importance of sales and leaseback in this year's activity and the reasons behind it.

GRAPH 3 **Retail investment by type** Shopping centres still capture the highest share of the activity



Graph source: Savills, Note: No HS deals included for UK and DE

Retail sale and leasebacks

Back on the rise

Activity in the retail sales and leaseback segment is continuing. Approximately €1.4bn of retail properties were sold and leased back (SLB) over the course of the past 12 months, according to Real Capital Analytics.

During the first three quarters of the year, retail SLB amounted to approximately €1.2m. This is four times the amount sold and leased-back during the same period last year and 31% above the average of the past five Q1-Q3s. Retail SLB currently accounts for 4.1% of the total retail investment volume.

More than half of the retail SLB was concentrated in Spain (55%). Netherlands (13%), France (11%) and Italy (10%) also accounted for a third of the total retail SLB volume recorded since the beginning of the year. These are mature markets where retail ownership still offers opportunities for investors. The activity was mainly driven by fashion and supermarket retailers.

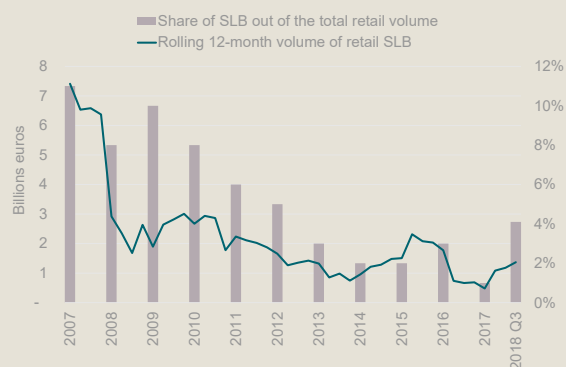
Based on pending transactions and an increasing number of discussions around the subject, we can expect more of this type of deal during the remainder of the year and in 2019.

In this challenging landscape, retailers need to rationalise and consolidate their units. Sale and leaseback transactions are a great financial opportunity for retailers seeking to raise capital to reinject in their core business.

From an investor's perspective, as long as the retailer offers a strong covenant and retail units are in prime locations, it is an alternative opportunity to source property and to invest large amounts of capital, which in return will provide secure income streams.

GRAPH 4

Retail sale and leaseback deals four times up compared to last year



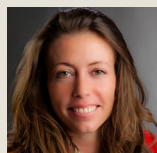
Graph source: RCA

Date	Name of property / Portfolio	Type of retailer	N. of properties	Country
Q4 18	El Corte Inglés	Department store	1	Spain
Q3 18	El Corte Inglés	Department store	2	Spain
Q3 18	De Mandemakers Groep	Home furnishing	3	Netherlands
Q3 18	Casino	Super/hypermarket	1	France
Q2 18	Stradivarius	Fashion	4	Spain
Q1 18	Eroski	Super/hypermarket	6	Spain
Q1 18	Tigos	Super/hypermarket	8	Italy
Q1 18	Zara	Fashion	14	Spain
Q1 18	Coop	Super/hypermarket	29	Italy
Q1 18	Casino	Super/hypermarket	1	France
Q1 18	Ermenegildo Zegna	Fashion	1	France
Q4 17	Albert Heijn	Super/hypermarket	15	Netherlands

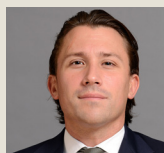
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