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RESEARCH

Retail Trends REPORT

IPD

An MSCI Brand

Report compiled by IPD

Q2 2014:
KEY FINDINGS

- For the year ending June 2014, the centres in the IPD Retail sample recorded a year-on-year increase of 4.6% in annualised trading density (sales per square meter). In real terms (inflation-adjusted) this translates into marginally negative growth.

- Vacancy levels have been steadily rising over the past 5 years but remains below 3% in centres larger than 25,00sqm. However, smaller centres have seen vacancy rates rise significantly over the past 6 months. Neighborhood centres have been particularly hard hit over the past 6 months.

- Gross rentals continue to grow faster than sales which have seen retailers' cost of occupancy increase. Cost of occupancy is currently the highest in the 10 year history of the series and is almost exclusively driven by higher administered costs.

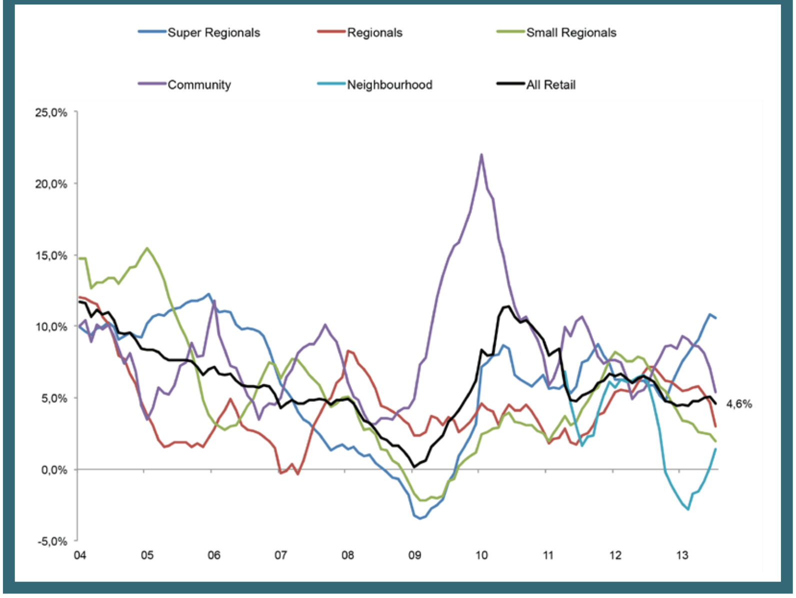
- Footcounts recorded during the quarter ending June were unchanged compared to a year before, symptomatic of the currently tough trading environment. In conjunction with a higher nominal trading density, this has resulted in a higher spend per head compared to a year before.

SALES PERFORMANCE

For the year ending June 2014, the centres in the IPD Retail sample recorded a year-on-year increase of 4.6% in annualised trading density (sales per square meter). In real terms (inflation-adjusted) this translates into marginally negative growth.

While Super Regional centres keep powering along at ~10% y/y, all other retail segments recorded nominal growth of sub-5%. Regional and Community shopping centres, in particular, experienced a sharp slowdown in growth during the last quarter. Neighbourhood shopping centres are still the worst performing segment at 1.3% y/y, despite returning its first positive quarter of growth since Q3 2013. (Figure 1)

FIGURE 1:
ANNUALISED TRADING DENSITY GROWTH
YEAR ON YEAR TO JUNE 2014



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T: 011 883 0679 F: 011 883 0684 Email: marketingmanager@sapoa.org.za Web: www.sapoa.org.za

Larger shopping centres have outperformed over the past 10 years -aided by nodal dominance, a larger variety of categories & tenants and a larger boost from seasonal trade.

Super Regional trade has traditionally been thought of as more defensive and stable through the economic cycle. However, analysis of the IPD Retail dataset suggests that this might not be the case.

Over the past 10 years, Super Regional trading performance wasn't more defensive relative to other retail segments when measuring the spread between median and lower quartile real trading density levels.

In other words, in difficult economic times, Super Regional sale volumes didn't hold up significantly better than other retail segments.

However, in good economic times, when the macroeconomic environment is supportive of increasing consumer spending growth, Super Regional centres seem to benefit more than other retail segments (Figure 2).

FIGURE 2 A:
REAL ANNUALISED TRADING DENSITY
LONG TERM DISPERSION IN REAL ANNUALISED TRADING DENSITY

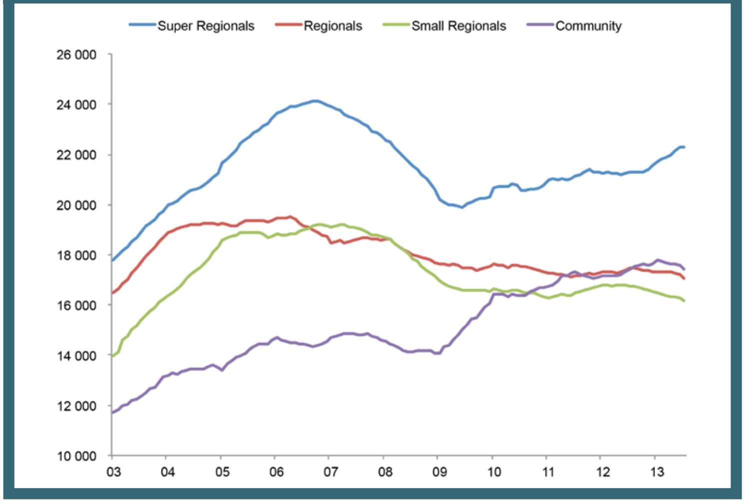
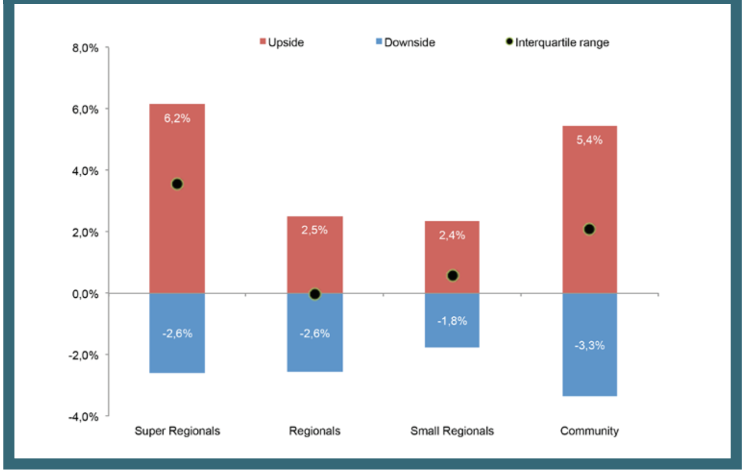
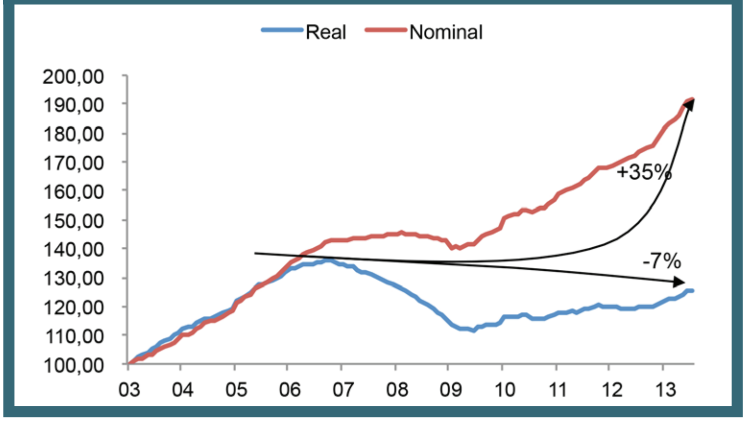


FIGURE 2 B:
10 YEAR SPREAD OF REAL ANNUALISED TRADING DENSITY
SUPER REGIONAL CENTRES OUTPERFORMED IN UPCYCLE



In nominal terms, the Super Regional trading density is currently 35% higher than it was at the height of the consumer cycle in 2007. However, this needs to be put into perspective, as in real terms; trading densities are currently 8% lower than it was in 2007. This means that on average, retailers are selling a lower volume of product compared to the height of the consumer boom. This could negatively impact retail margins and landlord's potential for rental upside through potential retailer price markdowns and higher inventory holdings costs.

FIGURE 3:
SUPER REGIONAL TRADING DENSITY - REAL VS. NOMINAL
INDEXED - 2003=100



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The outperformance of Community centres could be seen as somewhat surprising but the reason could be two fold. Firstly, a certain degree of outperformance can be attributed to the currently tough economic environment where a combination of high fuel prices and less disposable income could mean that consumers are choosing to shop closer to home. An additional advantage of Community centres in the current environment is that parking charges are lower relative to larger centres.

Secondly, a relative overweight position in outperforming categories also contributed positively to the trading performance of Community centres. The categories responsible for the majority of the growth were Apparel and Sporting Goods/Wear. Both of these categories have delivered above average trading density growth over the last year which has underpinned Community centre performance.

These two merchandise categories also seems to be one of the factors behind the relative underperformance of Neighbourhood centres relative to Community centres since the Community retail centre segment has a 20% exposure to these two categories while that of Neighborhood centres is significantly lower at 7%.

Another factor potentially contributing to the underperformance of Neighborhood centres in the current consumer environment is a less diverse tenant mix across fewer merchandise categories with almost half of lettable area attributed to food retailers and food service outlets.

Retailer cost of occupancy

Retailer's cost of occupancy, measured as gross rental as a % of sales, continued to increase over the past year and at June 2014 stood at 7.7% - up from 7.2% a year ago as gross rentals continue to increase at a faster rate than sales. (Figures 3 & 4) At the height of the recession, this ratio was recorded at 6.6% which emphasises the impact of rising administered prices.

The impact of rising tenant operating costs have been most pronounced in Community & Neighborhood centres where gross rent to sales ratios in these segments are currently significantly higher than 2009 levels.

Super Regional Centres is the only segment which currently has a lower gross rent to sales ratio compared to the highs of 2010, underlining its defensiveness in the current consumer environment.

The pace at which administered prices have been increasing is underlined by the difference in growth rate between base and gross rental. The divergence between gross and base rental has been especially pronounced over the last year which saw gross rentals grow at above 15% while base rentals have been increasing at between 7 & 9% (Figure 5)

FIGURE 4:
RETAILER COST OF OCCUPANCY
GROSS RENTAL AS A % OF SALES

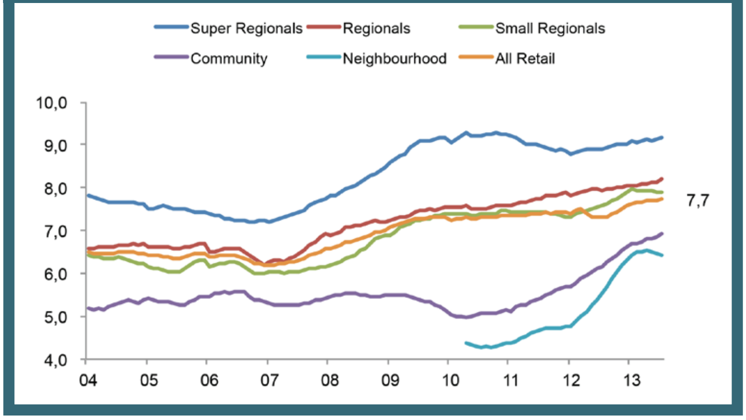
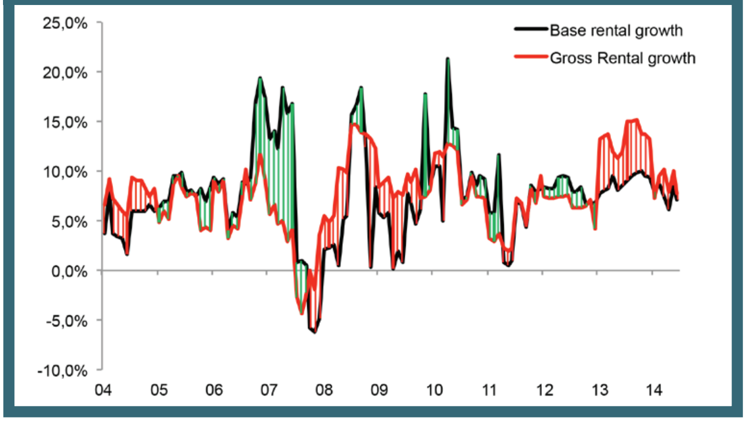


FIGURE 5:
GROSS RENTALS INCREASING FASTER THAN BASE RENTAL



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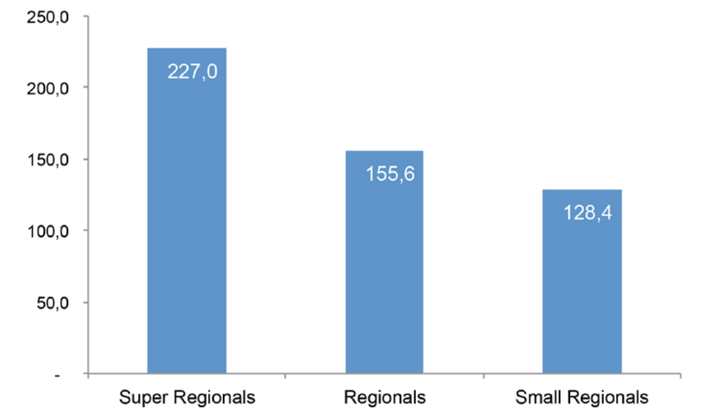
Retail vacancy rates

Vacancy levels have been steadily rising over the past 5 years but remains below 3% in centres larger than 25,00sqm. However, smaller centres have seen vacancy rates rise significantly over the past 6 months as illustrated by Figure 7 below. Neighborhood centres have been particularly hard hit with vacancies rising to above 10%. Community centre occupancy rates have also come under pressure with vacancies increasing from below 2% in the third quarter of 2013 to above 5% as at June 2014.

FIGURE 6:
SPEND PER HEAD - JUNE 2014



Footcount & spend per head

Footcounts recorded during the quarter ending June were unchanged compared to a year before, symptomatic of the currently tough trading environment. In conjunction with a higher nominal trading density, this has resulted in a higher spend per head compared to a year before.

The increased spend per head could be attributed to shoppers visiting centres less often but lumping purchases together in order to save on associated travel and parking costs.

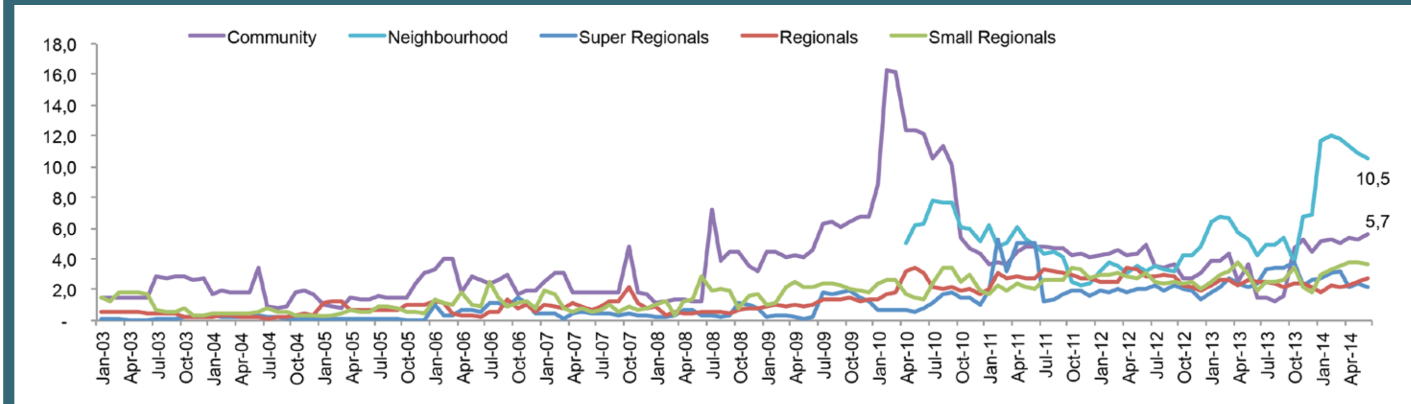
All centres larger than 25,000sqm has experienced a rebound in foot traffic since the recession of 2009. However, current levels of foot traffic per sqm is still significantly off the highs of 2004 when real economic growth was above 4%

The average spend per head across all centre types increased by 6.8 % for the year ending June 2014. The largest increase in the amount spent per visit was recorded for Super Regional centres at 12.6%. Small Regional centres recorded an increased spend per head of 8.5% while Regional centres recorded a negative growth of -1.9% y/y. (Figure 6) Annualised spend per head for all centres larger than 25,000sqm currently averages R170/visit.

Super Regional centres average an annualized R227/visit while Regionals and Small Regionals average R156 and R128/visit respectively.

Of the three larger retail formats, Super Regional centres is the only segment where real spend per head is currently above 2007 levels–largely as a result of a lower footcount, as opposed to a higher trading density. Real spend per head in Regional and Small Regional centres are currently 9% and 11% off their highs, respectively.

FIGURE 7:
VACANCY RATES PER RETAIL SEGMENT - JUNE 2014



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Merchandise category trends

The dislocation in the performance of the various merchandise categories continues. Categories that have outperformed include mostly non-durable and semi-durable goods while retailers selling durable goods and big ticket items count among those that have lagged.

Among the larger merchandise categories that have performed well are Sporting & Outdoor goods, Unisex Wear, Mini Department Stores, Food Service and Women's Wear.

Categories that have lagged include home furnishings, travel stores, toy stores and department stores.

A critical takeout from the current research is that category performance has not been consistent across the different retail segments.

As an example, Home Furnishings, has been an underperforming category over the last year or two but there's been a clear difference between the performance of outlets in the different retail formats. Furniture stores in Super Regional centres grew their trading density at above 10% for the year ending June while stores in Neighborhood and Community centres saw density going backwards. This potentially talks to the greater variety of outlets in the larger malls, catering to a broader demographic. The implication of this for landlords is that tenant selection might prove more crucial than category weighting – particularly in a portfolio containing centres of various sizes and target markets.

This trend is reversed in other categories where the convenience & value-orientated tenant mix of smaller retail centres are finding resonance with consumers in the current macroeconomic environment.

SHOPPING CENTRE TYPE DEFINITIONS

	TOTAL RENTABLE AREA
Super Regional Shopping Centre	> 100,000 m^2
Regional Shopping Centre	50,000 - 100,000 m^2
Small Regional Shopping Centre	25,000 - 50,000 m^2
Community Shopping Centre	12,000 - 25,000 m^2
Neighborhood Shopping Centre	5,000 - 12,000 m^2

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