RESEARCH
Retail Trends Report
Key Research Findings

South African shopping centre trading performance as measured by the MSCI South Africa Quarterly Retail Trading Density Index, recorded its best year-on-year growth since December 2016. Trading density growth (sales per square meter; annualised), came in at +5.7% year on year (y/y) to June 2019 in current price terms—up from +3.2% recorded for the year to March 2019.

The index is based on data collected by MSCI Real Estate’s Retail Performance Benchmarking Service which quantifies sales performance as well as other key retail performance metrics across 24 merchandise categories in more than 100 retail centres, covering in excess of 4 million square meters.

The 5.7% y/y increase in trading density was a function of a positive 6.3% sales growth & a 0.6% increase in the amount of reported trading area (i.e. a dilutionary impact). The above-inflation sales growth is particularly encouraging given the macroeconomic backdrop and a continuation of this trend will be positive for occupancy rates and occupancy cost ratios.

Trading density growth for the year ended June 2019 was a function of spend per head increasing by 4.2% while aggregate footcount/sqm grew by 1.4%. It marks the first period of positive footcount per square meter growth since September 2016.

From mid-2016 to 2019Q1, negative footcount growth detracted from trading density growth suggesting that consumers were visiting malls less frequently even though their spend per visit kept pace with inflation. Growth in shopper numbers is an important element of trading density growth and will play an important role in supporting ATD growth for the balance of 2019 as we approach Black Friday and then head into the Festive Season.

South African household expenditure continue to be constrained by consumer and administered price increases as well as higher income tax and additional levies such as the carbon fuel levy that’s added 9 & 10c/l to petrol and diesel respectively.

Despite increasing at an aggregate level, annualised trading density growth has been mainly driven by the smaller retail formats.

The Super Regional shopping centre segment saw its annualised trading density growth rebound after fears that it was running out of runway during the previous quarter.

Mid-tier centres also saw their trading density growth increase on the quarter before but remain in the low single digits (negative when viewed in inflation adjusted terms). These ‘mid-sized’ centres often don’t dominate their catchment area amid a need to balance convenience, experiential and comparative shopping elements.

Among the five largest merchandise categories, Department Stores outperformed with an annualised trading density growth of 7.5% for the year ended June 2019. The Food category (mostly comprising Grocery/Supermarket tenants) and Electronics also reported ATD growths in excess of 6% y/y.

Retailer’s cost of occupancy, as measured by the ratio of gross rental to sales, continued its upward trend with a 10bp y/y increase to June 2019. This was the result of a 6.3% growth in overall sales and a 5.9% y/y increase in aggregate gross rental.

On a segment level, Super Regional centre’s cost of occupancy remain significantly higher than the other segments. As at June 2019, Super Regional tenants pay R11.30 towards their gross rental for every R100 in sales, followed by the Regional and Small Regional segments at R9.00 and R8.60 respectively.

The vacancy rate of the 100+ shopping centres forming part of the MSCI Retail Trading Density Index was recorded at 4.3% at June 2019, above the long term average of 2.9%.

On a segment level, the highest vacancy rates are in the Neighbourhood and Super Regional retail segments at 5.3% and 4.7% respectively. However, these two have been the only segments to have recorded improvements in their occupancy rates since the start of 2018.
Headline Performance

South African shopping centre trading performance as measured by the MSCI South Africa Quarterly Retail Trading Density Index, recorded its best year-on-year growth since December 2016. Trading density growth (sales per square meter; annualised), came in at +5.7% year on year (y/y) to June 2019 in current price terms—up from +3.2% recorded for the year to March 2019 (Fig 1).

The index is based on data collected by MSCI Real Estate’s Retail Performance Benchmarking Service which quantifies sales performance as well as other key retail performance metrics across 24 merchandise categories in more than 100 retail centres, covering in excess of 4 million square meters.

The 5.7% y/y increase in trading density was a function of a positive 6.3% sales growth & a 0.6% increase in the amount of reported trading area (i.e. a dilutionary impact). The above-inflation sales growth is particularly encouraging given the macroeconomic backdrop and a continuation of this trend will be positive for occupancy rates and occupancy cost ratios.

The sales growth figure of 6.3% was higher than StatsSA’s nominal retail sales growth of 3.7% y/y for the year ending June 2019 (annual growth of Jun ’18-Jun ’19 on the same period a year before). This continues the trend of mall-based retailers outperforming the broader market and highlights the relative defensiveness of shopping centres in a challenging operating environment.

Fig 1: Trading density growth –MSCI South Africa Retail Trading Density Index
Annualised sales/sqm growth; Current price terms; y/y

Source: MSCI Real Estate
Key economic drivers for the retail sector

Fig 2: Retail sector – macroeconomic fundamentals
2003 up to & including latest available

- **Real GDP Growth**
  - Real GDP growth q/q SAAR
  - Real GDP growth y/y

- **Consumer Price Inflation (Core)**
  - Excl. food, non-alcoholic beverages and petrol

- **Final consumption expenditure by households**

- **Ratio of debt-service cost to disposable income**

*Source: StatsSA; South African Reserve Bank*
Drivers of trading density growth

As alluded to earlier in the report, trading density growth of +5.7% comprised a 6.3% growth in sales while reported trading area was up 0.6% (i.e. a dilutionary impact). Looking at it from another perspective, trading density growth was a function of spend per head increasing by 4.2% while aggregate footcount/sqm grew by 1.4%. It marks the first period of positive footcount per square meter growth since September 2016 (Fig 3).

From mid-2016 to 2019Q1, negative footcount growth detracted from trading density growth suggesting that consumers were visiting malls less frequently even though their spend per visit kept pace with inflation.

Growth in shopper numbers is an important element of trading density growth and will play an important role in supporting ATD growth for the balance of 2019 as we approach Black Friday and then head into the Festive Season. Over the long term, the growth in the amount spent per visitor has been the primary driver of trading density growth (Fig 4 below). Since 2006, trading density growth has averaged +5.1% comprising a spend per head growth of 5.9% while the growth of footcount per square meter had a dilutionary effect of -0.8%.

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**Fig 3: Trading density growth attribution – June 2019**

Weighted contribution to Trading Density Growth

<table>
<thead>
<tr>
<th>Component</th>
<th>Contribution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trading density growth</td>
<td>+5.7%</td>
</tr>
<tr>
<td>Impact of change in trading area</td>
<td>-0.6%</td>
</tr>
<tr>
<td>Sales growth</td>
<td>+6.3%</td>
</tr>
<tr>
<td>Footcount growth/sqm</td>
<td>+1.4%</td>
</tr>
<tr>
<td>Spend per Head growth</td>
<td>+4.2%</td>
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</table>

Source: MSCI Real Estate; Note: numbers may not add up due to rounding. This graphic illustrates the weighted contribution to Trading Density Growth of changes in Sales, Trading Area, Number of Shoppers and Spend per Head.

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**Fig 4: Trading Density Growth mainly driven by spend per head growth over longer term**

Weighted contribution to Trading Density Growth

Measure Names
- Footcount growth/sqm
- Spend per head growth
- ATD Growth

Sources: MSCI Real Estate
Sales Performance

South African household expenditure continue to be constrained by consumer and administered price increases as well as higher income tax and additional levies such as the carbon fuel levy that’s added 9 & 10c/l to petrol and diesel respectively. The 2019 budget also saw no changes made to the personal income tax tables and brackets which would likely have resulted in many individuals moving into higher tax brackets as a result. Despite these factors, annualised trading density growth as measured by the MSCI South Africa Quarterly Retail Trading Density Index, has now been positive since the second quarter of 2018 and crucially, has continued to accelerate.

As with most performance indexes, it is important to look beyond the headline figures and dig into sector level trends which are often more revealing. Despite increasing at an aggregate level, annualised trading density growth has been mainly driven by the smaller retail formats (Fig 5). The neighbourhood retail segment in particular has been showing strong growth in its trading density over the past two quarters (we explain the drivers of this in the next section).

The Super Regional shopping centre segment saw its annualised trading density growth rebound after fears that it was running out of runway during the previous quarter. The mid-tier segment (Small Regional and Regional centres) also saw its trading density growth increase on the quarter before but remain in the low single digits (negative when viewed in inflation adjusted terms). These ‘mid-sized’ centres often don’t dominate their catchment area amid a need to balance convenience, experiential and comparative shopping elements.

Among the five largest merchandise categories, Department Stores outperformed with an annualised trading density growth of 7.5% for the year ended June 2019. The Food category (mostly comprising Grocery/Supermarket tenants) and Electronics also reported ATD growths in excess of 6% y/y.

**Fig 5: Growth in large format centres low but improving - Smaller retail formats accelerate**

*Source: MSCI Real Estate*
What’s behind the increase in Neighbourhood trading density growth?

As illustrated in Figure 5, the trade in large format centres has stagnated while the smaller retail formats have accelerated. The positive performance of the Neighborhood retail segment in particular has been noteworthy. For the year ended June 2019, the segment recorded a year on year growth of 15.7%.

However, this outperformance needs to be viewed in context as the neighborhood retail segment has been underperforming since 2012. The recent growth has brought the neighborhood centre segment back in line with the other retail segments rather than outpacing them.

A deeper analysis of the neighborhood retail segment reveals that close to half of the segment’s recent growth has been driven by the Food category (7.4% out of 15.3%). As at June 2019, the Food category contributes 49.7% of Neighborhood centres’ total sales underlining its importance to the segment’s fortunes – especially considering that it occupies ‘only’ 32% of GLA while paying 23% of total gross rental.

An important point to make is that the improved trading density growth has been mainly landlord-driven via active management and right-sizing, rather than consumer driven via an increased spend. For the year to June 2019, neighbourhood centre based food retailers grew their sales by 3.6% but it was an 11.3% reduction in the average store size which was the major driver of the increase trading density growth.
Retailer cost of Occupancy

Retailer’s cost of occupancy, as measured by the ratio of gross rental to sales, continued its upward trend with a 10bp y/y increase to June 2019. This was the result of a 6.3% growth in overall sales and a 5.9% y/y increase in aggregate gross rental.

On a segment level, Super Regional centre’s cost of occupancy remain significantly higher than the other segments. As at June 2019, Super Regional tenants pay R11.30 towards their gross rental for every R100 in sales, followed by the Regional and Small Regional segments at R9.00 and R8.60 respectively.

The Super Regional segment also saw the largest year on year increase in its gross rent to sales ratio of 20bps – i.e. an extra 20 cents of gross rental per R100 of sales.

Neighbourhood retail was the only segment that saw its cost of occupancy improve on a year over year basis – a 10bp improvement to 5.4%. Cost of occupancy in the smaller retail formats remain significantly lower given the higher weighting towards their anchor tenants.

The three large format retail segments have seen pronounced increases in their cost of occupancy since the start of 2016 as sales growth have struggled to keep up with the rental growth (Figure 6).

While cost of occupancy in the three larger retail formats are at all time highs, that of the Community & Neighbourhood centre segments remain well below 2016 levels with the improvement driven by a rise in occupancy levels.

**Fig 7: Since 2016… Rent to Sales ratio up sharply in large format retail**

Cost of Occupancy up 150bps since 2016
Gross rental has grown faster than Sales

<table>
<thead>
<tr>
<th>centre’s &gt; 25k sqm</th>
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<tbody>
<tr>
<td>Gross Rental growth</td>
</tr>
<tr>
<td>Sales Growth</td>
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<table>
<thead>
<tr>
<th>Year</th>
<th>Gross Rent to Sales ratio</th>
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</thead>
<tbody>
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<td>2012</td>
<td>10.2%</td>
</tr>
<tr>
<td>2013</td>
<td>9.3%</td>
</tr>
<tr>
<td>2014</td>
<td>9.4%</td>
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<tr>
<td>2018</td>
<td>9.8%</td>
</tr>
<tr>
<td>2019</td>
<td>9.9%</td>
</tr>
</tbody>
</table>

Source: MSCI Real Estate
**Retail Vacancy Rates**

The vacancy rate of the 100+ shopping centres forming part of the MSCI Retail Trading Density Index was recorded at 4.3% at June 2019, above the long term average of 2.9%.

On a segment level, the highest vacancy rates are in the Neighbourhood and Super Regional shopping centre segments at 5.3% and 4.7% respectively. However, these two have been the only segments to have recorded improvements in their occupancy rates since the start of 2018 (Fig 8). On a year-on-year basis, the Super Regional segment has recorded a 110bp improvement in its vacancy rate to end the period at 4.7%.

Similar to previous cycles, the vacancy rate of mid-tier segment are currently lagging the Super Regional segment. Since the start of 2018, the Small Regional and Regional segments are up 90bps and 60bps respectively. In the context of a 50,000sqm centre, 90bps works out to 450sqm of additional vacancy compared to 18 months ago, resulting in additional costs relating to tenant installation, letting and administration as well as lost rental within, and possibly beyond the initial beneficial occupation periods.
**RESULTS FOR THE QUARTER ENDED JUNE 2019. SEPTEMBER 2019**

**About the Sample**

The IPD Retail sample consists of around 100 shopping centres across all geographies & centre types owned by listed real estate investment trusts, life & pension funds as well as private property funds.

The full quarterly results from 2003 onwards are available for 24 merchandise categories across 5 retail formats – from super regional down to neighbourhood centres. To subscribe to this quarterly publication please contact realestate@msci.com

**SHOPPING CENTRE DEFINITION TYPES**

- **Super Regional shopping centre**: > 100,000sqm
- **Regional shopping centre**: 50,000-100,000sqm
- **Small Regional shopping centre**: 25,000-50,000sqm
- **Community shopping centre**: 12,000-25,000sqm
- **Neighbourhood shopping centre**: 5,000-12,000sqm
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