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 another quarter of positive growth notwithstanding the uniquely challenging operating environment.

- Trading density growth (sales per square meter; annualised), came in at +6.1% year on year (y/y) to December 2019 in current price terms – stable on the revised +6.1% recorded for the year to September 2019.

- The 6.1% y/y increase in trading density was a function of a positive 6.9% sales growth & a 0.8% increase in the amount of reported trading area (i.e. a dilutionary impact).

- The sales growth figure of 6.9% was higher than StatsSA’s nominal retail sales growth of 3.8% y/y for the year ending December 2019, highlighting the relative defensiveness of malls, especially in a recessionary environment.

- The trade in large format centres has stagnated while the smaller retail formats have accelerated. The positive performance of the Neighbourhood retail segment in particular has been noteworthy.

- However, this outperformance needs to be viewed in context as the neighbourhood retail segment underperformed the other segments from 2013 to mid-2016. The recent growth has brought the neighbourhood centre segment back in line with the other retail segments rather than outpacing them.

- Close to half of the segment’s recent growth has been driven by the Food category (7.1% out of 15.2%).

- Retailer’s cost of occupancy, defined as the ratio of gross rental to sales, continued its upward trend. An increase of 10bp y/y to December 2019 brings the ratio to 8.0% across the 100+ measured centres.

- On a segment level, Super Regional centre’s cost of occupancy is currently at an all-time high and significantly higher than the other segments.

- The average vacancy rate of the 100+ shopping centres forming part of the MSCI Retail Trading Density Index was recorded at 4.6% at December 2019, 20bps up on the previous quarter.

- On a segment level, the lowest rate of vacancy is in the Regional shopping centre segment at 3.2%. This may seem surprising, bearing in mind that this segment has see the lowest level of ATD growth. However, keeping the vacancy rate down has come at a cost as gross rental has only increased by 3.5% suggesting negative reversions on renewal and re-letting.
Headline Performance

South African shopping centre trading performance as measured by the MSCI South Africa Quarterly Retail Trading Density Index, recorded another quarter of positive growth notwithstanding the uniquely challenging operating environment.

Trading density growth (sales per square meter; annualised), came in at +6.1% year on year (y/y) to December 2019 in current price terms—stable on the revised +6.1% recorded for the year to September 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 just shy of 5 million square meters.

The 6.1% y/y increase in trading density was a function of a positive 6.9% sales growth & a 0.8% increase in the amount of reported trading area (i.e. a dilutionary impact).

The sales growth figure of 6.9% was higher than StatsSA’s nominal retail sales growth of 3.8% y/y for the year ending December 2019 (annual growth of Jan-Dec ’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 malls, especially in a recessionary environment.

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**Fig 1: Trading density growth – MSCI South Africa Retail Trading Density Index**

Annualised sales/sqm growth; Current price terms; y/y

- 2007 Q4: 3.7%
- 2011 Q4: 3.8%
- 2013 Q2: 6.6%
- 2016 Q2: 7.5%
- 2019 Q4: 6.1%
- 2017 Q4: -2.6%

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
- 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 +6.1% comprised a 6.9% growth in sales while reported trading area was up 0.8% (i.e. a dilutionary impact). Looking at it from another perspective, trading density growth was a function of spend per head increasing by 1.5% while aggregate footcount/sqm grew by 4.5% (Fig 3).

Footcount – expressed per square meter – has now ticked up every month since April 2019 and encouragingly, grew at its fastest rate since December 2012 (Fig 4). Of concern though will be the fact that Spend per Head growth dipped into the low single digits at 1.5% y/y. So, shoppers are starting to visit malls more frequently but critically are not maintaining their spend per visit - possibly spreading out roughly the same level of spend over more trips.

Over the long term, the growth in the amount spent per visitor has been the primary driver of trading density growth and a further decline in this figure may see overall trading density decline impacting tenant’s cost of occupancy and consequently landlord’s net income growth.

**Fig 3: Trading density growth attribution – December 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>+6.1%</td>
</tr>
<tr>
<td>Impact of change in trading area</td>
<td>-0.8%</td>
</tr>
<tr>
<td>Sales growth</td>
<td>+6.9%</td>
</tr>
<tr>
<td>Footcount growth/m²</td>
<td>+4.5%</td>
</tr>
<tr>
<td>Spend per Head growth</td>
<td>+1.5%</td>
</tr>
</tbody>
</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.

**Fig 4: More feet through the door, but spend per visit flat**

Trading density growth requires growth in both components

![Graph showing trading density growth](image)

Source: MSCI Real Estate
Sales Performance

The South African economy remains in a perilous state. Business confidence plunged to its lowest level in more than two decades in the first quarter of 2020 and could weaken even further as the full effect of the coronavirus and oil price crash filters through to the domestic and global economy. Retail sales growth is weighed down by weak consumer confidence, muted demand, high rates of unemployment and load-shedding.

Despite these headwinds, 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. Overall, the trading density for December 2019 increased by 6.1% versus December of 2018 which translates to a 2% growth when adjusted for inflation.

However, looking only at the headline figures in isolation can be deceiving. At an aggregate level, annualised trading density growth has been mainly driven by the smaller retail formats (Fig 5) which have benefitted as shoppers favour convenience centres for an increasing proportion of their spend.

Excluding Community and Neighbourhood centres drops the overall growth to 2.1% which is about half of the current consumer price inflation rate. The three larger retail formats haven't seen their sales per square meter grow faster than inflation since 2016. Regional shopping centres, in particular, are still having a tough time of it and only grinded out a 0.8% growth (-3% after inflation). Regional centres (GLA of 50-100k sqm) rarely dominate their catchment areas anymore (especially those in metro areas) and compete against smaller, convenience centres and larger malls with more tenants and longer trading hours.

Among the five largest merchandise categories, Electronics stores continue to perform well with an annualised trading density growth of 9.3% for the year ended December 2019. The Food Service category (comprising restaurants, fast food and the like) and Department Stores also reported ATD growths in excess of 6.8% y/y.

Fig 5: Above-inflation growth in smaller format centres, larger malls underperforming

<table>
<thead>
<tr>
<th>Segment</th>
<th>Annualised Trading Density Growth %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Super Regional</td>
<td>2.83%</td>
</tr>
<tr>
<td>Regional</td>
<td>0.72%</td>
</tr>
<tr>
<td>Small Regional</td>
<td>2.80%</td>
</tr>
<tr>
<td>Community</td>
<td>5.41%</td>
</tr>
<tr>
<td>Neighbourhood</td>
<td>17.16%</td>
</tr>
</tbody>
</table>

Source: MSCI Real Estate
Food has driven neighbourhood centre performance

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 December 2019, the segment recorded a year on year growth of 17.2%.

However, this outperformance needs to be viewed in context as the neighborhood retail segment underperformed the other segments from 2013 to mid-2016. 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 (7.1% out of 17.2%). As at December 2019, the Food category contributes 48.2% of Neighborhood centres’ total sales underlining its importance to the segment’s fortunes – especially considering that it occupies ‘only’ 30.8% of GLA while paying 22.7% of total gross rental.

An important point to make is that the improved trading density growth of Food retailers has been mainly landlord-driven via active management and right-sizing, rather than consumer driven via an increased spend.

From late 2012 to the end of 2019, the average Food Retailer’s store area declined by 17.8%, while the average turnover per store declined by a lower 6.3%.

Fig 6: Comparing November to October – across segments & merchandise categories
% difference in monthly trading density
Retailer cost of Occupancy

Retailer's cost of occupancy, defined as the ratio of gross rental to sales, continued its upward trend as rental growth marginally outpaced sales growth. An increase of 10bp y/y to December 2019 brings the ratio to 8.0% across the 100+ measured centres.

On a segment level, Super Regional centre's cost of occupancy is currently at an all-time high and significantly higher than the other segments. While Super Regional centres attract more shoppers and spend, its current cost of occupancy may see retailers becoming more selective in their approach to the segment. Should they be present in all Super Regional centres? If so, should they be more flexible about their store size and trading model? Does the increased costs of occupancy necessitate greater investment in their online capability to complement their physical footprint?

As at December 2019, Super Regional tenants pay R11.57 towards their gross rental for every R100 in sales, followed by the Regional and Small Regional segments at R9.11 and R8.66 respectively (Fig 7).

The Super Regional and Small Regional segments in particular has seen a significant increase in tenant occupancy costs since 2016.

Neighbourhood retail was the only segment that saw its cost of occupancy improve on a year over year basis – a 20bp improvement to 5.3%. Cost of occupancy in the smaller retail formats remain significantly lower than that of larger malls and are now well below 2016 levels as a result of an improved occupancy rate and inflation-plus sales growth.

Fig 7: Rent to Sales ratio flat overall, but up sharply in large malls

Source: NQG Retail Estate

Change in Gross Rent to Sales ratio- December 2019
12 month change (percentage points)
Retail Vacancy Rates

The average vacancy rate of the 100+ shopping centres forming part of the MSCI Retail Trading Density Index was recorded at 4.6% at December 2019, 20bps up on the previous quarter.

On a segment level, the lowest rate of vacancy is in the Regional shopping centre segment at 3.2%. This may seem surprising, bearing in mind that this segment has seen the lowest level of ATD growth. However, keeping the vacancy rate down has come at a cost as gross rental has only increased by 3.5% suggesting negative reversions on renewal and re-letting.

The Community centre segment is next lowest at 3.8%, although vacancy in the segment has slowly trended higher (Fig 8).

It’s important to maintain a sense of scale when comparing the different retail segments. A vacancy rate of 5% in a typical Super Regional Centre equates to around 6,000sqm of empty store space while 5% for a Neighbourhood centre means a not insignificant, but possibly more manageable 500sqm.

Given the challenging operating environment, filling 6,000sqm of Super Regional space is no small order – given that most major retailers will already command a presence in malls of that size as well as heightened cautiousness relating to store expansion and a declining pool of smaller-format tenants.

Since mid-2018, the vacancy rate of the Super Regional segments is down 90bps while that of the Small Regional segment is up 130bps.

In the context of a 40,000sqm Small Regional centre, 110bps works out to 520sqm of additional vacancy compared to a year ago, resulting in additional costs relating to reinstatement and TI, letting and administration as well as lost rental within, and possibly beyond the initial beneficial occupation periods.

Fig 8: Super Regional vacancy rate down since mid-2018, other segments up

![Vacancy Rate Graph]

Source: MSCI Real Estate
RESULTS FOR THE QUARTER ENDED DECEMBER 2019.
MARCH 2020

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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