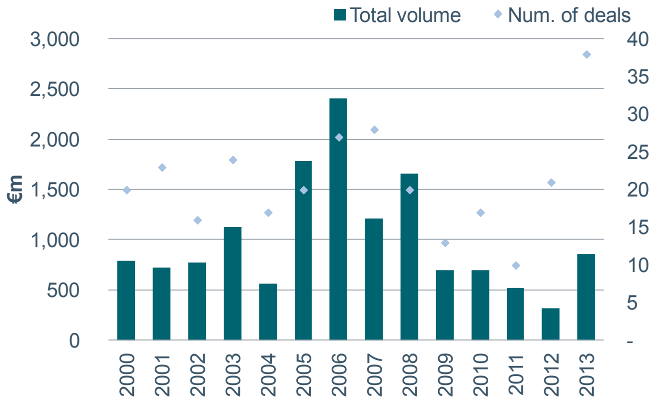
Market report
Spain Retail

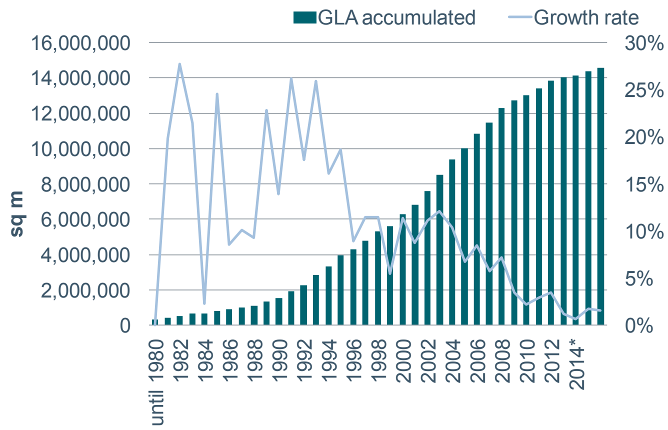
February 2014

GRAPH 1
Retail investment volume and number of deals*



Source: Savills / *excluding bank braches

GRAPH 2
GLA accumulated and growth rate



Source: AECC / Savills / *forecasts

SUMMARY

Investment volume tripled compared to 2012

■ Hardly more than 160,000 sq m of GLA came onto the market in 2013, which is 60% less than the same figure in 2012, which was a year when various large and very large projects were delivered.

■ The amount of new space in the pipeline over the next two years stands at just over 300,000 sq m. As is becoming the norm, these are just initial estimates, as the number of new projects that will come on to the market will very much depend on how the economy fares and the availability of finance.

■ The main retailers in the market continue to be actively expanding, but these expansion plans are always accompanied by an in-depth study of the potential business that can be carried out in the new points of sale.

■ In addition, various international brands are actively searching for retail units in order to open in Spain.

■ The general decline in sales continues to favour additional rent reductions for existing leases, mainly via rent reviews and temporary rental discounts.

■ Prime shopping centres that are performing well, have reached stable rents for new leases and in some cases are even seeing an increase in rents.

■ After thee years of free fall, the annual investment volume increased significantly. The slightly more than €850m, almost tripled the previous year's investment volume. Thanks to international funds, investor activity has picked up again and traditional properties have returned to being the most in demand product, knocking retail units off the top spot that it had held for several years.

Economic situation

After a period of recession, the Spanish economy is currently at a turning point. According to the latest GDP data published by INE (National Statistics Institute), Q3 saw a 0.1% quarter-on-quarter increase, which is the first positive figure for the past nine consecutive quarters, which would technically mean we are out of the recession. Despite all of the above, and despite the fact that the last quarter of the year will continue to increase, the overall annual figure will continue to be negative.

The weak employment market is showing some positive signs. According to the latest Q3 data from the Economically Active Population Survey (Encuesta de Población Activa - EPA), the employment fell at a rate of 2.7% y-o-y, compared to 4.7% in the same period in 2012. On the other hand, at the end of the year, the Public Employment Service (Servicio Público de Empleo Estatal - SEPE) registered 147,385 fewer unemployed people, which is the first decrease since the start of the crisis.

The Consumer Confidence Index has continued to increase since May 2013, with a slight relapse in October, but then continued to trend upwards. In addition, retail sales have also started to pick up. September saw a y-o-y increase of 2.2%, which was due to the significant drop in the same figure in 2012, due to the hike in taxes. Retail sales growth continued in October and November (+2%).

"The general impending improvement in mid-term macroeconomic forecasts is a positive sign, but we must wait and see if this will then filter down to the domestic economies, which are the ones to underpin increasing consumption"

Gema de la Fuente, Savills Research

Footfall

According to the latest footfall index published by Experian, a marked drop in footfall in shopping centres continues. 2013 saw a year-on-year change of -3.71%, the third sharpest correction in history.

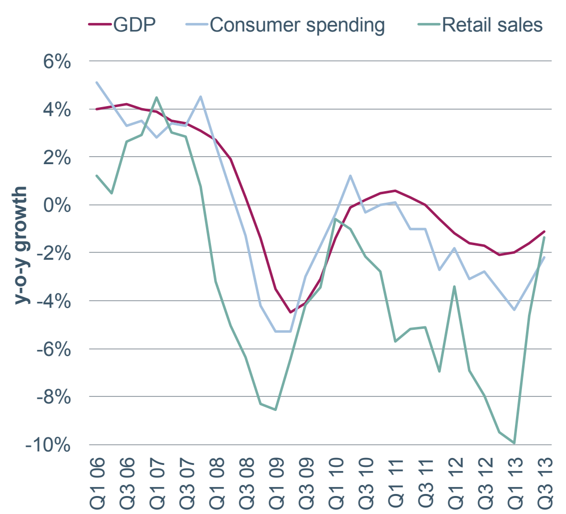
Since the beginning of 2013, monthly indexes have remained below 2012 figures, with the greatest declines taking place in April, with a drop of 6.6%. The smallest corrections took place in February and March, both of which were below 1%, coinciding with the sales over the winter period.

New measures

With the aim of incentivising retail sales and increasing employment in the sector, in July 2012 a law was passed that increased the minimum number of bank holidays that stores over 300 sq m could open - from eight to ten. It also established that towns with over 200,000 inhabitants that registered over 1,000,000 overnight stays in hotels each year, and/or received 400,000 cruise passengers should, at the very least, be designated a major tourist destination. 14 cities have met the criterion set out by the government, of which three already had non-restrictive retail opening hours, due to them already being major tourist destinations. Palma de Mallorca, Santa Cruz de Tenerife and Madrid. The latter opted for complete flexibility to operate at any hour, which will allow Makro to open its new centre in the south of the city (Paseo Imperial) 24/7. The company

GRAPH 3

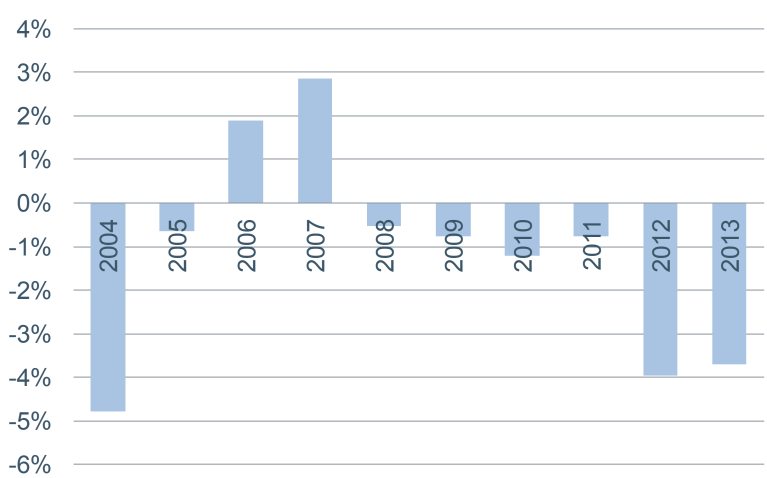
Economic indicators



Source: INE

GRAPH 4

Footfall index y-o-y variation



Source: Experian

confirmed that it will apply its new opening hours over December and the beginning of January, except for Christmas Eve and New Year's Eve.

The other cities (Alicante, Barcelona, Bilbao, Cartagena, Cordoba, Granada, Malaga, Las Palmas, Seville, Valencia and Zaragoza) have not all been as enthusiastic about the new regulation. Various groups within the sector believe that the measure clearly favours large retailers, as opposed to small neighbourhood retailers and various town's local governments have fixed a blanket or partial veto on the regulation. On the other hand, the areas that do not meet the required objectives set out by the government, can request to be declared tourist areas, in order to then be able to extend their retail opening hours. According to data provided by the Secretary of State for Commerce, after the National Retail Conference in September 2013, there were 694 areas that were already declared as major tourist destinations, which were spread over 526 towns.

According to data published in the latest report by Globe Shopper Index Europe, Madrid is the second largest shopping destination in Europe, ahead of cities such as Paris, Berlin and Barcelona, with only London ahead of it. One of the most highly valued aspects was the opening hours, particularly on Sundays.

Another new factor in the sector has seen the end of sales periods, in favour of continually offering promotions and discounts. It is still early days in terms of gauging whether this has been a success, but it is clear that this measure offers more opportunities to the consumer to benefit from discounts and have a positive impact on sales figures. In any case, the word 'sales' continues to have a psychological impact on boosting consumption.

Special mid-season promotions are now standard practice for the majority of chains operating in Spain and there are ever more brands that incorporate and link various offer formats. One of the latest arrivals is 'Black Friday', which in the USA officially kicks off the Christmas season with significant discounts. Various retailers in Spain launched special promotions for this day and others even extended it in to the weekend. Some of which discounted selected articles in stores and online and others solely focused on e-commerce. Fnac, El Corte Inglés, Media Markt, Zara Home, Oysho, Massimo Dutti, Apple and Amazon were just some of the names that signed up for this initiative.

Sales and turnover

According to data provided by the Spanish Shopping Centre Association (AECC), shopping centre turnover in Spain fell by 2.4% in 2012 compared to 2011. Forecasts of average household spending published by INE also show clear signs of contraction in family spending, with a variation of -4.5% y-o-y, reaching 12% when compared to the same figure in 2007.

Despite the unfavourable market situation, the National Association of Large Distribution Companies (ANGED) expects that there has been an increase in Christmas shopping that will allow this sector to end the year with an increase in turnover for the first time since the crisis began. In this respect, 2012 was heavily influenced by the VAT increase in September and the cancellation of civil servants' extra pay, which negatively affected not only the turnover of ANGED members, but the retail sector as a whole.

Expansion plans

Despite this unfavourable environment, operators are sticking to their expansion plans, consolidating their presence in strong markets and streamlining growth in the best shopping centres in their catchment areas. In terms of sectors, fashion brands clearly dominate the market, accounting for 40% of new openings or extensions, followed by the restaurant sector with 18%. In third place are cosmetics and personal care retailers. There has hardly been any change between the percentage of new openings this year and last year, but we would highlight that sports brands (in fourth position), as in 2012, slightly increased their activity.

The big fashion players continue to jostle for position in an ever more competitive market. The top spot that used to be held by Inditex, has now been taken on by other brands that are looking to significantly increase their sales network. Shana and its new line, Double Agent, accounted for 13.25% of new fashion store openings, followed by the Inditex Group, with just over 12%. H&M and Primark were also very active and are in third and fourth place with 6.6% and 5.15% respectively.

Low cost brands offering fashion and new trends at very low prices are clearly on the up and Inditex is aware of this. Lefties accounted for close to 44% of all of Inditex's new stores.

Holea, Carrefour Property's new shopping centre in Huelva was the largest space to come on to the market (33,000 sq m). Fashion has been the driving force, with 42% of all stores opened, followed by the specialist store category (telephones, opticians, hairdressers, amongst others) with 40%. Among the fashion brands were the regulars: Inditex, H&M, Mango and Primark. Since its entry in to the Spanish market in 2006, Primark has not stopped growing and plans to continue to expand over the coming year.

In terms of launching new business lines, as well as expansion and growth, we would highlight Mango's frenetic activity. For some months now, Mango Kids and Mango Sports & Intimate lines have been available in many of the Catalan brand's stores and 2014 will see the launch of 'Violeta', which will be the brand's specialist plus size line. It is expected to launch in mid-January, with clothes for Spring/Summer 2014. The collection will be available in some Mango stores, although the idea is for the brand to have its own individual stores. In addition, the collection will be available on the online store two days before it hits the stores. Rebels, which is another fashion brand for 14 to 22 year olds, will postpone its launch, due to the managing director leaving the project.

Toys"R"Us has also extended its business with the launch of a new range of sports equipment for children, named 'Future Champions' and another children's decoration range. Stores in Alcorcón (Parque Oeste) and Torrejón de Ardoz (Parque Corredor), have been the ones chosen in Spain to test out a European strategy which has also been launched in France, Germany and the United Kingdom.

Decathlon is also testing out new growth concepts. The Spanish subsidiary has opened stores that are predominantly focused on fashion. The new chain is known as 'Lots of Colors' and now has four stores in Madrid, three in high street retail units and one in the Islazul shopping centre.

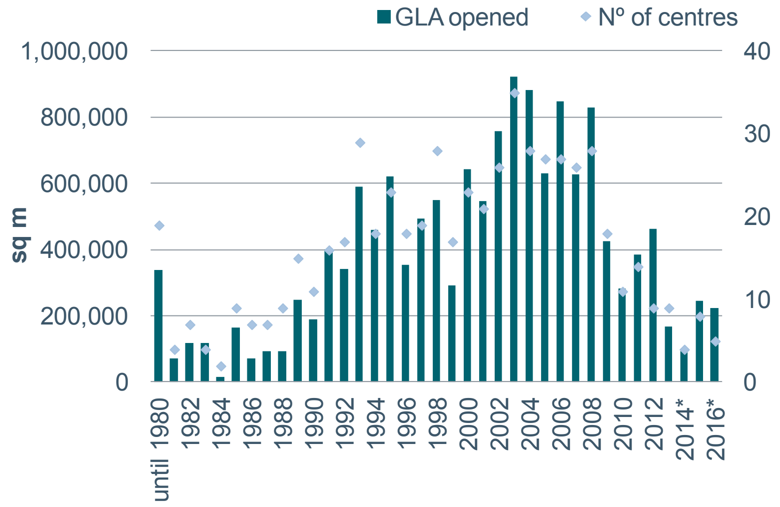
New retailers

The confidence in a mid-term economic recovery means that new retailers are looking to move in to the market. The brands Brooks Brothers, 7 For All Mankind, Stella McCartney, Coach, Fifth & Pacific and Moncler have opened stores on the main high streets of Madrid and Barcelona. Some of them had already carried out a trial period with their own stores in outlet centres such as La Roca Village (Barcelona) and Las Rozas Village (Madrid).

Another form of entering the Spanish market is via online retail. The Swedish group H&M already opted for this strategy with one of its young fashion brands, Weekday, for which it is now actively looking for bricks and mortar stores. It recently announced that the Spanish market is one of the 18 European countries in which it will launch the online store for its youngest fashion brand, Cheap Monday, which up until now has been limited to a few articles of clothing that were only available on the Asos platform.
Uniqlo, known as the Japanese Zara, is looking ever more closely at entering the Spanish market. It already has an online store for the whole of Europe, in Britain, but has expanded the number of countries that it delivers to: as well as Spain, France, Germany, Italy and Ireland. In addition to this, they are also negotiating the opening of a new store in Barcelona.
Finally we would mention the creation of a new brand in the homewares sector. Casa Bianca has been started by an ex-director from Mango. The online store is already operational, but the company is also studying the opening of a bricks and mortar store in Barcelona next spring, as well as pop-up stores in locations in Majorca and Formentera, due to their high numbers of tourists.

GRAPH 6

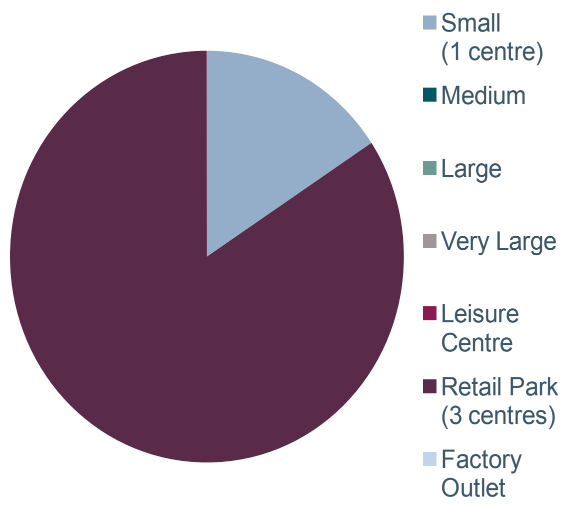
Openings by year (GLA and number of centres)



Source: AECC / Savills / *forecasts

GRAPH 5

New GLA by type of scheme (2014)



Source: Savills

Online retail

Online retail continues to be an ever more promising alternative in order to access end users and an easy way of entering new markets. According to the 2012 B2C e-commerce study carried out by the National Telecommunications Observatory and Information Society (Observatorio Nacional de Telecommunicaciones y la Sociedad de la Información - ONTI) the volume of business generated by the consumer e-commerce channel, reached €12,383 billion in 2012, which is 13.4% more than the same figure registered the year before. Despite this increase, the volume of business is along way off the results registered in Europe. A document published by the European Statistics Office, Eurostat, recently confirmed that only 43% of Spaniards buy online, whilst the European average is 60%. A comparison with the most active countries, such as the United Kingdom with 82% or Denmark and Sweden with 79%, reveals that Spain still has a long way to go in terms of e-commerce. One of the reasons for the above is probably cultural, given that the Spanish society is very much a street based society, which favours purchasing in high street stores. But one must also take in to consideration the lack of confidence in buying online and the lack of brands omni-channel retailing.

The Higher Institute for the Development of the Internet (Instituto Superior para el Desarrollo de Internet - ISDI) indicates that Spain is one of the countries with the highest adoption of smartphones and the consumer is using electronic devices more and more to search, compare and purchase products.

According to data from the Online

Business School, in 2012 mobile-commerce in Spain billed a total of 2.5 billion euros. Only 6% of Spaniards with smartphones made purchases via their phone, which is a long way off the 43% in South Korea, 30% in the USA and 26% in the United Kingdom.
Mobile phones will change the way we buy and retailers should adapt to this new digital environment. Factors such as 'showrooming' (checking out products in the bricks and mortar store and then subsequently purchasing online at a lower price), scanning QR codes, gamification and geolocation tools are now a reality that should be taken seriously.

"Various international operators are preparing to enter the Spanish market, due to the improved mid-term economic outlook. Some have been waiting for years for the right moment. Others have pre-tested the market via their online store" Gema de la Fuente, Savills Research

Current supply and developments in 2013

Total supply of retail space in Spain has now reached 14.8 million sq m. This figure includes shopping centres, outlet centres, leisure centres and retail parks, but excludes high street retail units and retail warehouses constructed around a retail area in out-of-town locations.

Retail density per 1,000 inhabitants stands at 313 sq m. This figure has grown at a more moderate rate over the past few years, due to the drop in construction of retail properties.

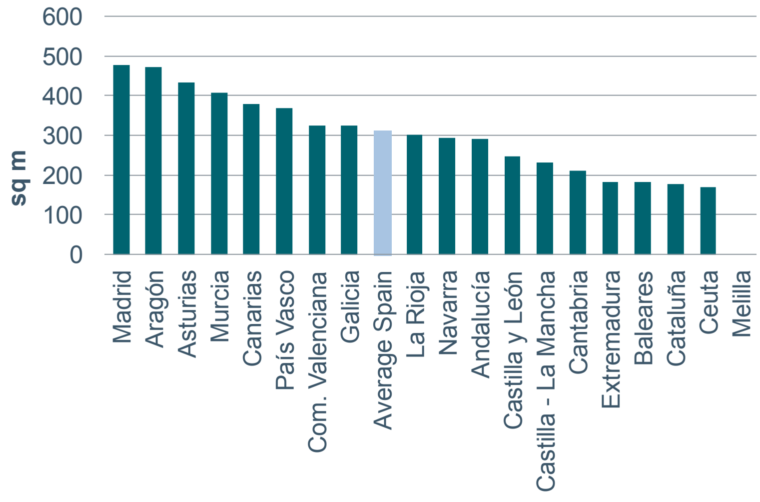
Of the barely more than 160,000 sq m of new space that was in the pipeline for 2013, 91% was already open in November. In terms of size, we would highlight the previously mentioned 33,000 sq m Holea shopping centre, which was developed by Carrefour Property, as a complementary property to its Carrefour hypermarket.

But the volume of new retail space has significantly decreased from the circa 460,000 sq m opened over 2012, when multiple projects under the categories of large or very large shopping centres where delivered. 92% of new space which came on to the market in 2012 was for properties over 50,000 sq m. In terms of volume, we would highlight the 118,000 sq m shopping arcade at Puerto Venecia in Zaragoza, which completed a 200,000 sq m retail complex. The 80,000 sq m La Zenia Boulevard retail complex in Alicante, which comprises a retail park and shopping centre and the 65,500 sq m Río Shopping in Arroyo de la Encomienda in Valladolid, which is the second complex constructed by Inter Ikea Centre Group in Spain.

Thus, the total number of openings in 2013 compared to 2012 has reduced by 60%, although nationally speaking, the distribution of retail space has barely changed. Madrid, Andalusia and the Comunidad Valenciana continue to lead the regional rankings for retail space. Between the three of them, they account for 50% of all retail space.

GRAPH 7

Commercial density by region (sq m/1,000 inhab.)



Source: Savills

Future developments

The amount of new space in the pipeline over the next 24 months stands at just over 300,000 sq m. These are just initial estimates, as the number of deals signed will very much depend on changes in the economic climate and the availability of finance.

After the record levels of new developments recorded in 2008, with almost one million square metres opened, the average volume stands at around 400,000 sq m. 2013 has seen a marked decline compared to 2012, when various mega-projects came on to the market, which significantly increased the average area per project.

In terms of future projects, Cruce de Caminos should be highlighted, a 45,000 sq m retail complex in Sagunto (Valencia), that will be developed by Grupo Lar in association with Rockspring and Wit Retail. It will feature a shopping centre with a supermarket, a shopping arcade and several retail warehouse units, which will aim to become the best in the area. Decathlon and AKI DIY have already confirmed that they will form part of the tenant mix. The scheme's opening is expected by the end of 2015.

The 43,000 sq m Avenida M-40 shopping centre in Leganés (Madrid), will be fully refurbished in order to differentiate it from its many other competitors in its catchment area (Parquesur, Islazul and Plaza Nueva). The owner plans to reopen the centre over 2015.

At 40,000 sq m, the Jaén Plaza retail complex, in Jaén (Andalucía) is the third largest project. Developed by Grupo Alvores it will feature a retail park and a shopping arcade with specialized operators in fashion, household, food and leisure. Its opening is expected for the second quarter of 2014.

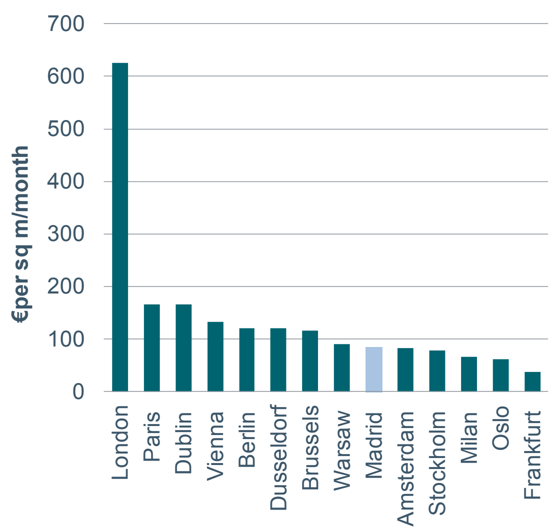
Differenciation

The market is generally cautious with regard to developing new complexes, primarily due to the ever present instability of Spain's main socio-economic indicators and the difficulty of acquiring financing. Given the need to attract more customers to the numerous shopping complexes, many owners have opted to both redesign and alter the retail or leisure offer in their shopping centres in a bid to improve the shopping experience, in order to make them stand out from the other shopping centres.

Muelle Uno (Málaga) is looking to improve thanks to the boost it will receive from the future development of the El Cubo cultural centre, which is an off shoot of the Pompidou Centre in Paris. This has meant that retailers are now showing more interest in taking space in the shopping centre.

GRAPH 8

Prime shopping rents in Europe



Source: Savills

Rents

The general decline in sales has increased operators' rent cover ratios once again, and is favouring further rental adjustments for existing leases, mainly via reviews and temporary rental discounts. Generally speaking, owners are very receptive, and they want to avoid increasing vacancy rates in their shopping centres, but rental adjustments will once again depend on different factors, such as the centre's specific circumstances or the retailer's relationship with the owner. I.e., whether or not the retailer has stores in several of the owner's shopping centres.

The idiosyncrasies of each centre will also determine rental levels in the new leases. Prime shopping centres, with high occupancy rates and high retailer demand, are even seeing rents increase slightly. The same can be said of consolidated centres, which are situated in secondary locations, but which are the leading centre in their direct catchment area. On the other hand, assets in provinces or towns suffering from oversupply and high unemployment rates are trying to attract new retailers via lower rents or incentives, which range from fit-out contributions, stepped rents and turnover rents, etc. We have even seen some centres financing small retailers to help them set up their business.

Based on in-house data, the average rent for leases signed between 2012 and the first few months of 2013 stands at €19.5 per sq m/month, which equates to a 12% decrease compared to the same figure in 2011. Moreover, the average rental level of centres registered in our database in 2012-2013 (which may contain data from previous years) has been slightly higher, reaching €20.2 per sq m/month, and clearly demonstrates the rental decline compared to the levels registered between 2008 and 2011, at €24.25 per sq m/month.

If we use retail units of between 100 and 200 sq m as a benchmark to analyse achievable rents in prime shopping centres, the average rent for new leases remains in the region of €90 per sq m/month. A low vacancy rate and the attractiveness of entering a dominant shopping centre in its direct catchment area are some of the reasons why rents are stable in the best shopping centres.

Prime rents in shopping centres in Spain are 35% below the European average, where the maximum rent was registered in the UK, at close to €610 per sq m/month. The national retail parks figure is in line with the European average, at around €16 per sq m/month, with the UK once again registering the highest figure, at almost €31 per sq m/month.

The Investment market

The Spanish property market is attracting renewed interest from international funds. After years of following the market from a distance, international money has actively returned to the playing field.

Current market indicators have not shown significant signs of change, but a significant shift in market sentiment has been noted. With an economic recovery predicted for 2014, many institutional investors are of the opinion that this is the right time to invest in the Spanish market, primarily in Madrid and Barcelona. Consequently, American, French, British and German funds, together with money from Latin America, have moved in to Spain over 2013 in search of opportunities, complementing domestic investors that have dominated the market since 2008.

The commercial property investment market has reached approximately €2.5 billion, which is a 12% year-on-year increase. The outlook is positive for 2014, in a market that will continue to accommodate different investment strategies, both in terms of opportunistic, as well as core. Acquiring financing will continue to be difficult and as a result cash-buyers will continue to dominate the investment market.

Around €850m invested in retail almost tripled the previous year's investment figure and equates to 34% of the total investment volume in the commercial property market. We should point out that the retail market figure does not include the bank branch sub-market, which saw the completion of one of the largest transactions of the year: Fibra Uno, a Mexican fund, acquired 278 Banco Sabadell bank branches for approximately €300m , which Moor Park purchased as a sale & leaseback agreement two years ago.

Traditional retail product (shopping centres and retail warehousing) has regained prominence in the investment market, accounting for approximately 54% of the total transacted volume, although the high street sector, including retail properties, continues to be in the investor spotlight. In 2012, retail units accounted for almost 60% of the annual figure and these were predominantly acquired by private domestic investors. However 2013 saw several foreign investors actively participating in this sector, focusing on prime assets in Madrid and Barcelona's major retail areas. Hence Deka is the new owner of the Adolfo Domínguez store at Calle Serrano 5, GLL purchased the store occupied by BBVA at Paseo de Gracia 25, AXA Reim acquired at the end of the year two stores occupied by Tiffany and Escada at José Ortega y Gasset, known as the Golden Mile, and IBA Capital Partners, the most active investor of the year, purchased two El Corte Inglés stores (amongst other properties) in Plaza de Cataluña (Barcelona) and Preciados (Madrid).

As for the shopping centre market, foreign investors have taken control, completing various different types of deals, from opportunistic, such as the purchase of three shopping centres from the SEB portfolio by an international fund, to other core purchases. In October, British investor Intu Properties, in partnership with the Canada Pension Plan Investment Board, acquired the Parque Principado shopping centre (75,000 sq m) in Oviedo (Asturias), for €162m. The announcement of the purchase by these traditionally conservative investors came as a surprise to the market. However they stated their optimism over Spain's future, noting that there are opportunities available and that you can purchase large quality shopping centres at historically low prices.
The most in demand product, prime shopping centres, also happens to be the most scarce, and has resulted in specialist investors looking to consolidated centres in secondary cities (provincial capitals) as a good alternative.

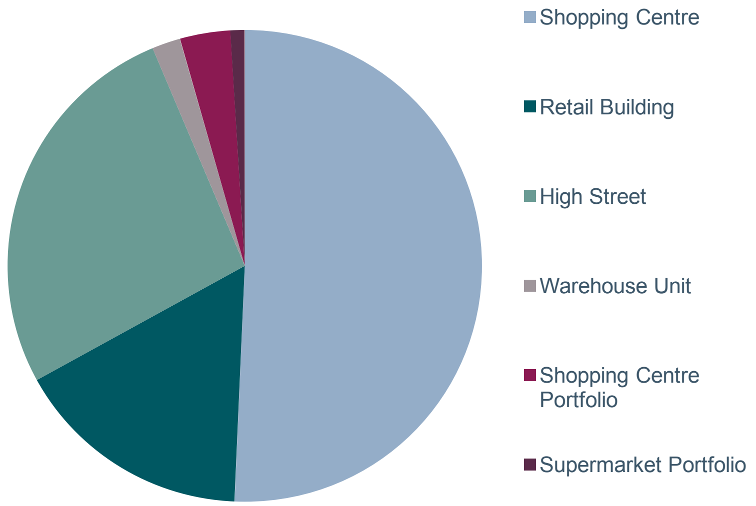
Yields

The change in sentiment by consumers, companies and the financial markets is paving the way for more pronounced investment activity. Spain is now on investors' radar, given that it is a developed country that has and continues to work its way out of the economic downturn in the shortest possible timeframe. Additionally investors can find interesting properties at lower prices than in London or Paris and which offer higher yields.

The lack of prime deals makes establishing yield levels complicated, and we have therefore maintained the theoretical level at 6.75% (net). The same is true of prime properties in retail parks and big box retail, which remains at 7.5%. The growing interest in consolidated shopping centres in secondary locations is hardening the yield in this asset class, which has adjusted from 2012's level by 25 basis points, to now stand at 7.75%.

GRAPH 9

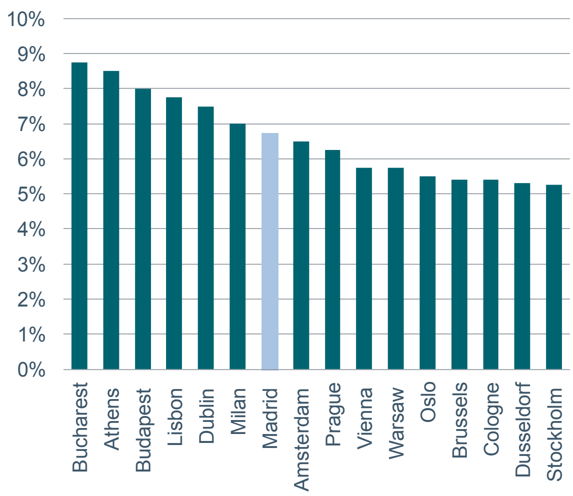
Investment volume by product (2013)*



Source: Savills / *excluding bank branches

GRAPH 10

Prime shopping centres yields in Europe

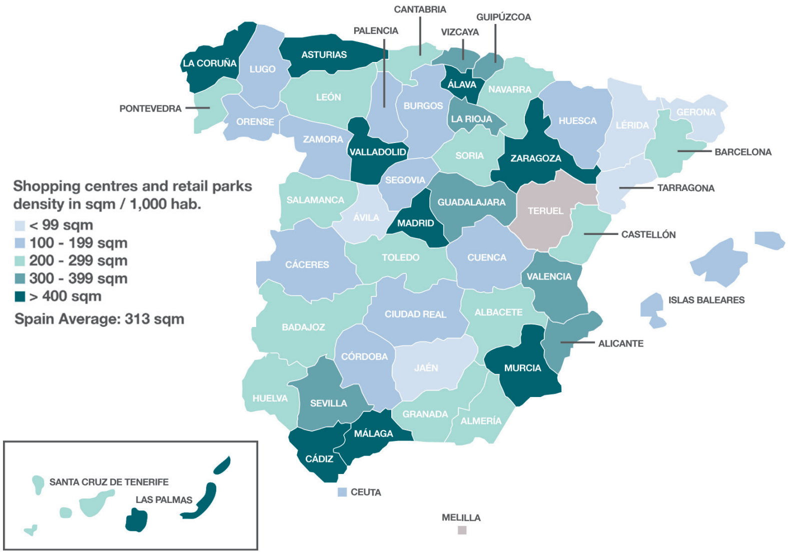


Source: Savills

MAP 1

Spanish retail market

Shopping centres, retail parks, outlet centres, leisure centres and hypermarkets



OUTLOOK

2014

■ Large retailers continue to expand, but as in previous years, they are looking at the business potential of these new stores with a magnifying glass. In some cases, the opening of new stores will be driven by a business reshuffle within a particular city that has various points of sale, always opting for the best locations, from which they hope to generate higher revenues.

■ The arrival of new brands on to the Spanish market is breathing new life in to the market. The American chain Urban Outfitters and the Japanese brand Uniqlo are some of the brands that are actively looking for retail space. Recently, the Dutch chain Hema indicated that it was looking to open stores in Spain and the United Kingdom over the first half of the year.

■ The investment market will continue to be active in 2014 and we believe that higher volumes of investment can be achieved as more product is coming onto the market. The most in demand products are prime shopping centres, but these are the most scarce, therefore secondary and consolidated shopping centres appear to be a good alternative.

■ Over the first half of the year, we expect to see various deals completed that were started over 2013. The portfolios of Klépierre and Vastned, Urbil and Parque Ceuta, would account for €500m, which would account for 65% of 2013's total annual volume.

■ Yield compression is expected for prime shopping centres, while prime retail parks remain stable..

Savills Team

For further information, please contact

Luis Espadas
Capital Markets
+34 91 310 10 16
lespadas@savills.es

Salvador González
Investment Retail
+34 91 310 10 16
sgonzalez@savills.es

Gema de la Fuente
Research
+34 91 310 10 16
gfuente@savills.es

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