EUROPEAN
RETAIL MARKET 2023

savills

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European Retail Market | **2023**

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Economic & Consumer Landscape

Tightening consumer finances dampened retail sales in 2023, but stronger performance forecast for 2024

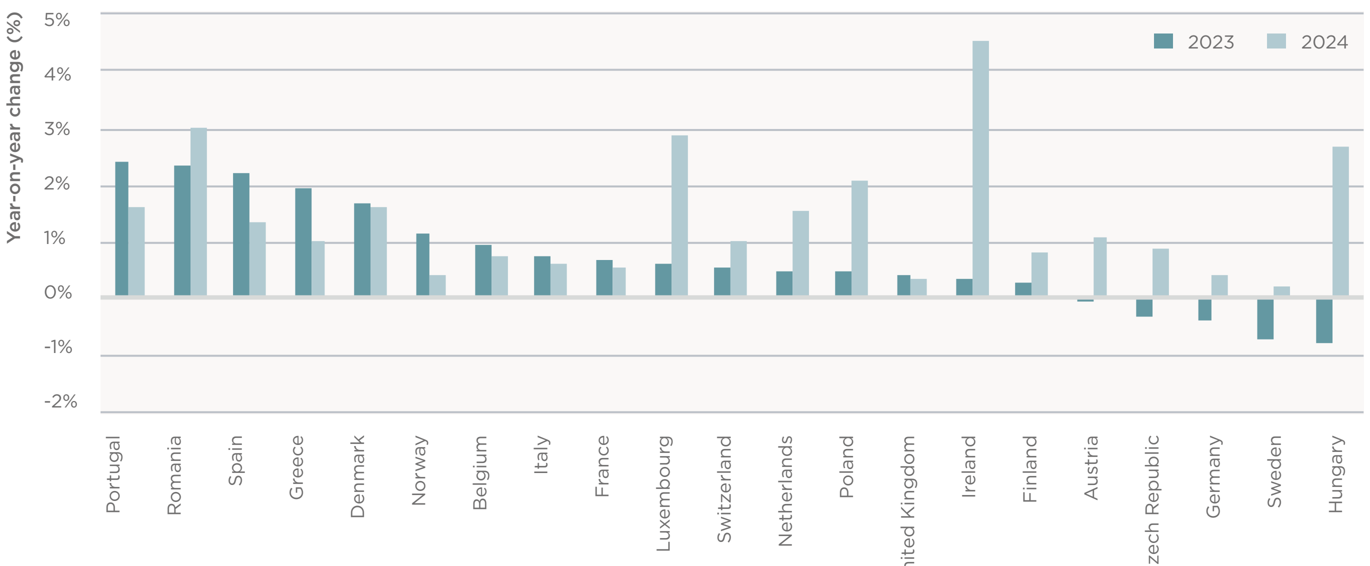
With the weight of inflation, consumer confidence well below its long-term average, and an increase in interest rates in most European markets, consumers are restricting spend in some areas as their disposable income is squeezed. As a result, total retail sales for Europe are forecast to marginally decline by -0.1% in real terms in 2023. But, while macro-economic headwinds have been particularly acute this year, conditions look set to improve.

Firstly, the recession in Europe looks set to be avoided this year with 0.5% GDP growth forecast, accelerating to 0.9% in 2024. The strength of the labour market has also helped to sustain the European economy, with unemployment at record lows; the EU unemployment rate is expected to hit 6% in 2023, down 20 basis points (bps) year-on-year, the lowest unemployment rate seen since the Global Financial Crisis (GFC). Finally, fiscal tightening has eased headline inflation across Europe, with CPI forecast to be 4.9% in the EU-27 in 2023, down from 9.2% in 2022.

These evolving market conditions indicate an improved retail sales outlook for the coming year, particularly as the squeeze on real disposable incomes dissipates, with forecasts for European spend in 2024 pointing to a rebound with growth of 3.7% (real terms).

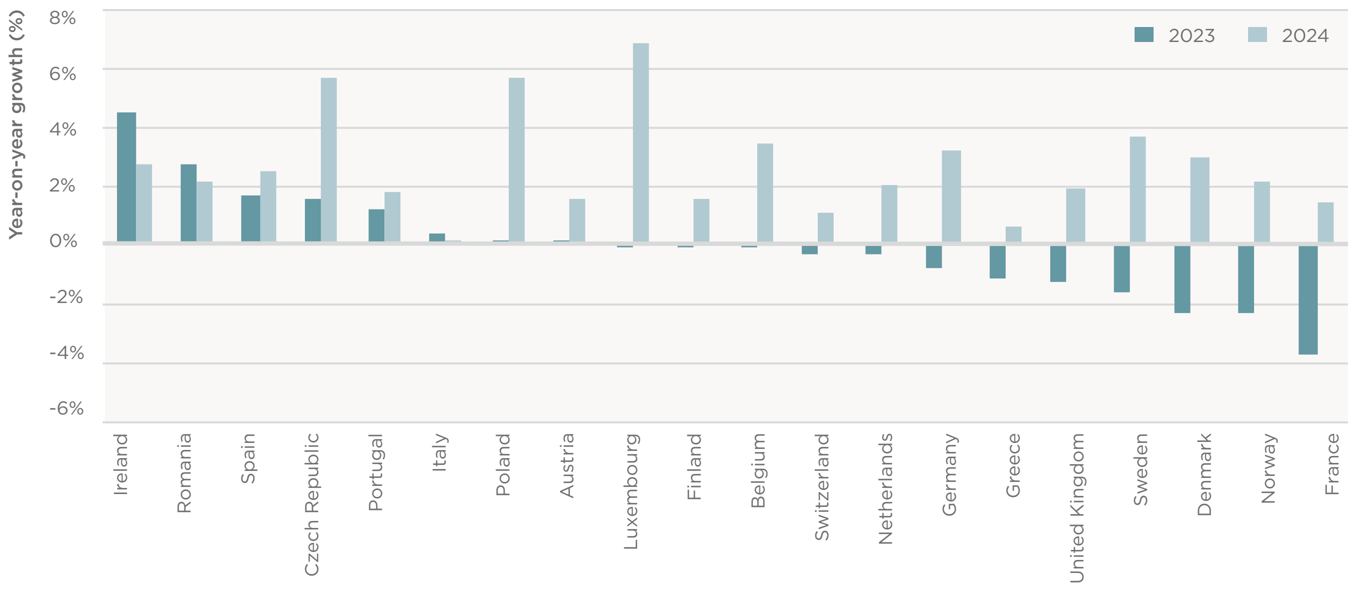
But some markets bucked the wider European trend of weaker retail sales this year. Ireland is expecting year-end sales growth to hit 4.6%, with a further 2.8% growth in 2024. The Southern European markets of Spain, Portugal and Italy are also expected to report positive growth by the year end of 1.7%, 1.2% and 0.4%, largely the result of lower inflation and returning tourism boosting sales, particularly in the luxury market. A stronger rebound in performance for Spain and Portugal is forecast for next year.

Annual GDP growth



Source: Oxford Economics

Annual retail sales growth



Source: Oxford Economics

Consumers spending priorities evolve

While total retail sales have been under downward pressure this year, this has not been reflected across all parts of the retail market. Tightening consumer finances have buoyed discount and convenience-driven retail spend, as consumers look to make savings on everyday items and head for cheaper retail options.

Recent spend on fashion has also been impacted by the evolving consumer environment, with the sub-market projected to increase by only 0.2% this year, despite recovering to its pre-pandemic levels in 2021. However, waning headwinds to consumers' discretionary spend in 2024 suggests fashion spend will strengthen with a growth of 3.7% forecast.

But again, headline performance only tells part of the fashion spend story. The mid-market has been more exposed to this year's 'squeeze'. Mass or value fashion has, on the whole, continued to perform well albeit with slower growth rates than seen in 2022. For example, Primark reported year-end sales in September up 17%, with Zara also posting a 13% year-on-year growth for the first half of 2023.

This relatively strong performance has also been mirrored at the premium and luxury end, with Bain-Altagamma forecasting that personal luxury goods spend in Europe in 2023 was 8.1% above that seen in 2019, with forecasts to 2030 suggesting a further 33% increase. This has been helped by not only the resumption in international tourism, but also accrued pandemic savings that, despite a de-winding from their pandemic highs, remain above pre-pandemic levels. According to the European Central Bank (ECB), overnight household deposits in September 2023 were still 22% above equivalent 2019 levels, albeit down from the 36% differential reported at the start of the year.

The prioritisation of spend in the luxury part of the market by certain consumers is also being seen in the 'experiential' space. Leisure and food and beverage (F&B) sectors continue to be resilient across many markets, with spend within the sector accounting for 54% of total European retail sales to date, unchanged from its 2022 share, with this share to increase to 55% in 2024. We have seen a similar trend when it comes to leisure travel within Europe due to many households looking to reduce spend elsewhere in order to protect holiday trips and spend.

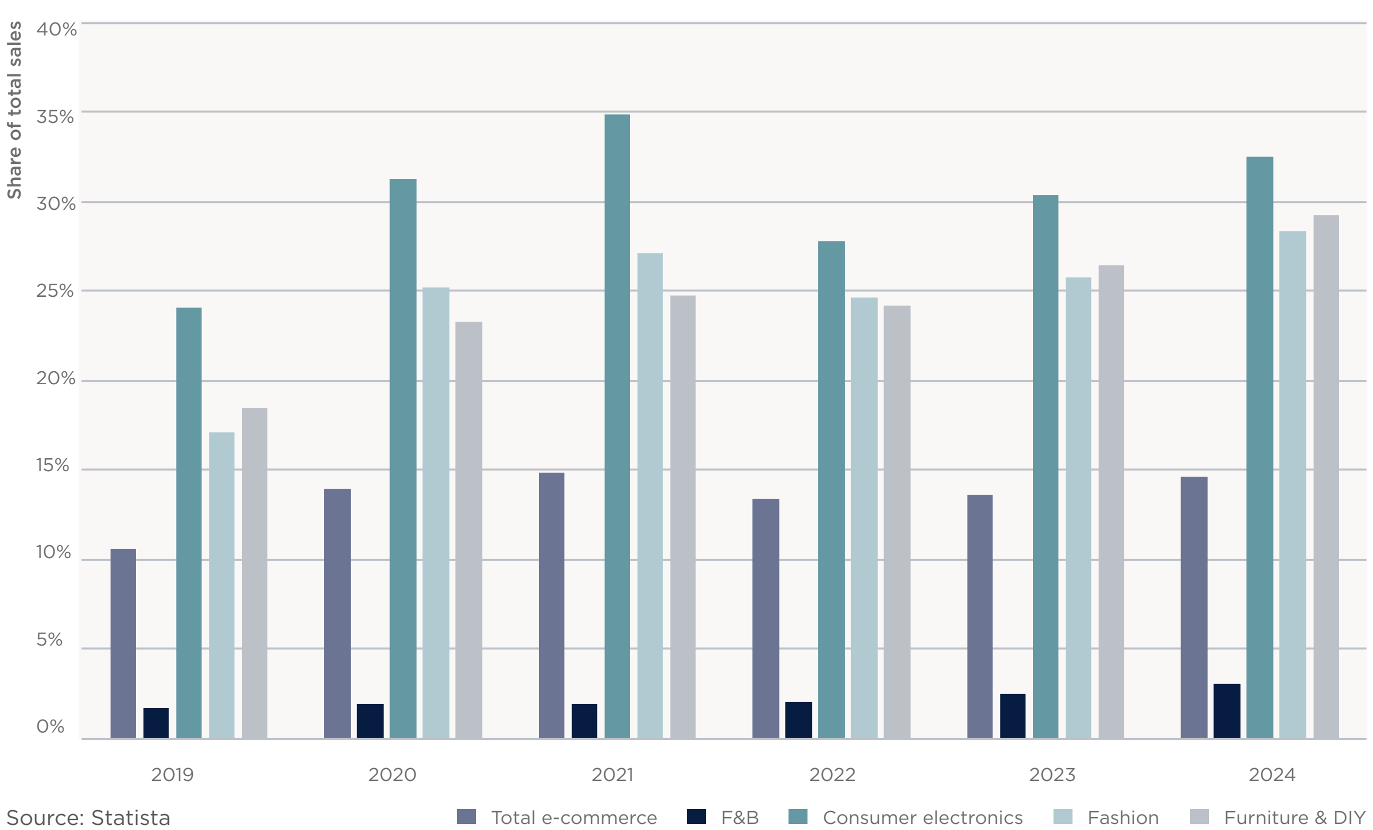
Omni-channel strategies mean physical stores are being increasingly prioritised

The share of e-commerce in Europe is predicted to grow to 15% in 2024 from 14% in 2023; 28.4% of fashion spend in Europe is forecast to be online in 2024, up from 17.1% in 2019. However, there are parts of the retail market where the rate of penetration is much higher or much lower.

While the rise of online has had a significant structural impact, its read-through to occupational markets varies across different geographies. For example, in Southern Europe, where the online penetration rate is relatively lower, its impact has been less pronounced, with overall vacancy rates remaining relatively low, though they are on the increase for secondary and tertiary retail locations.

Since the pandemic, evolving omnichannel strategies – where e-commerce complements physical store performance and visa-versa – is resulting in prioritisation of store portfolios by retailers. This is manifesting through upsizing in key markets and targeted expansion, and has been exacerbated by the rise in online customer acquisition costs and those associated with online deliveries/returns. What has not changed post-pandemic, is the fact that prime and super convenient retail locations are benefitting from this strategy.

Share of European online sales



Source: Statista

Prime High Street

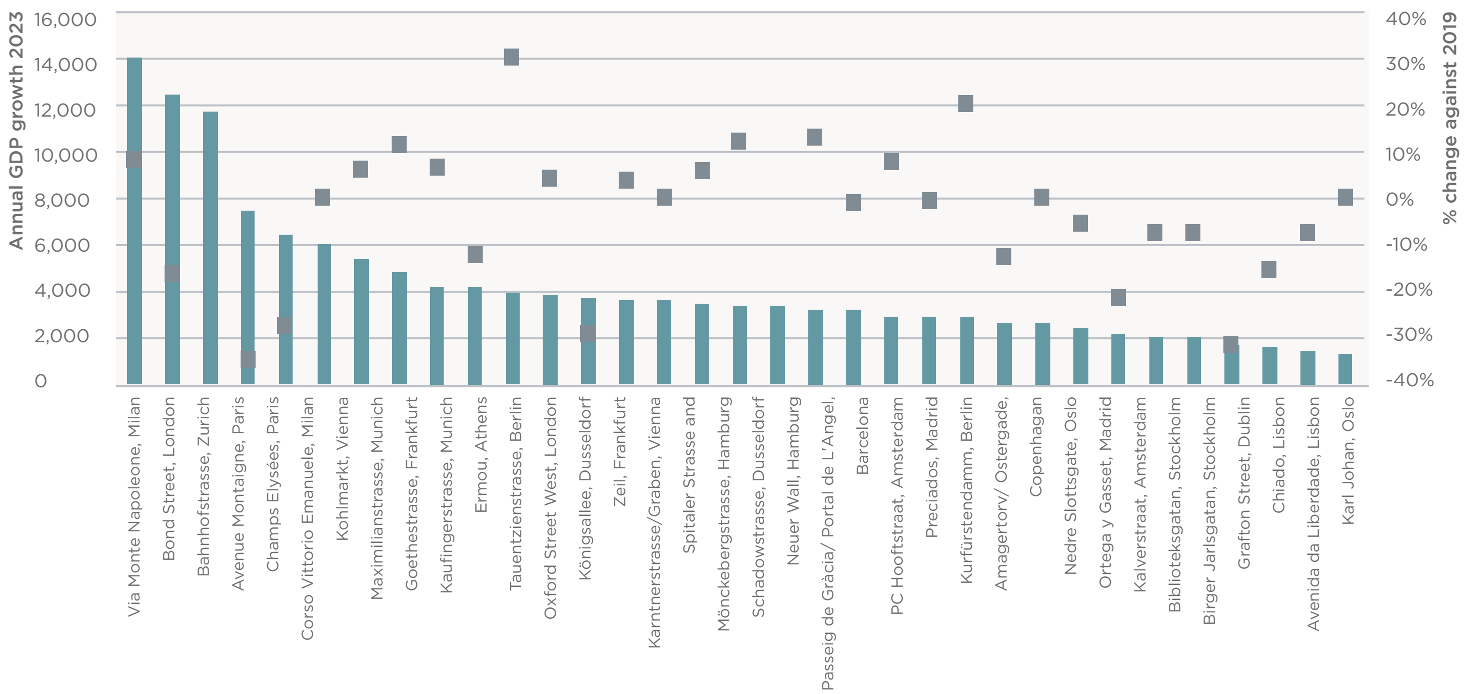
Milan's Via Monte Napoleone tops the ranking as Europe's most expensive retail street

Milan's major luxury street, Via Monte Napoleone, now outranks London's luxury Bond Street as the most expensive retail street in Europe with prime rents of €14,000 per sqm per annum, 7.7% higher than where they were pre-pandemic. A number of other luxury streets have also seen an improvement in rents or, at the very least, were able to minimise pandemic declines and have started to recover. For instance, across the 16 luxury streets we track in Europe, average prime rents as of Q3 2023 are only 2.0% below where they were in Q4 2019, having increased by 1.2% on the pandemic lows seen in late 2021.

Perhaps of most interest is the fact that much of this growth and resilience has been driven by smaller luxury streets beyond the big luxury capitals of Milan, Paris and London, with average rents 1.0% ahead of 2019. This resilience has been supported by more restrained availability, but also the fact that many of these smaller markets are predominately driven by domestic spend. In contrast, the premier luxury streets in London and Paris were more exposed to the absence of international visitors, a key driver of performance in both cases.

The recovery in international travel is supporting an acceleration in the recovery of Bond Street and Avenue Montaigne. Bond Street, for example, has seen vacancy reduce by 721 bps on its 2021 pandemic vacancy high of 13.6%; rents are up 14.3% over the same period.

Prime high street rents



Source: Savills

Smaller affluent cities moving up the agenda for luxury brands

The localisation of luxury spend during the pandemic – online or through department stores – has provided many luxury brands with greater insight into where their customers live, and is also helping to identify markets that were perhaps relatively underserved. This, combined with an evolving strategy by some luxury brands to understand both where their consumers live and where they holiday, is generating new requirements across a range of smaller affluent European cities, as well as a desire by some brands to upsize existing stores in key markets. All of this is then being exacerbated by the general shift away from wholesale towards own-brand stores, which is also feeding into store strategies. Ultimately, helping to drive down vacancy and place further upward pressure on rents on prime luxury streets.

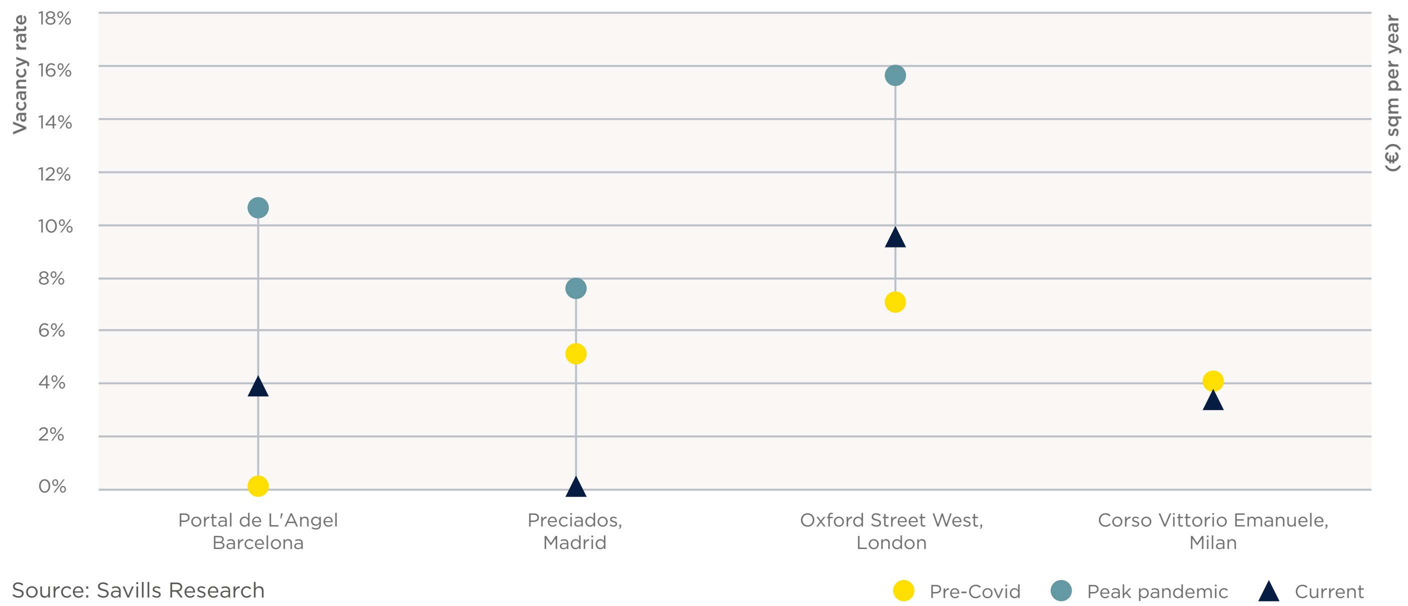
Recovery on Europe's prime mass market streets starts to pick up pace

The impacts of the pandemic were perhaps the most profound and drawn out on Europe's major mass market streets, locations that were already facing challenges due to growing online spend and reduced occupier demand for large flagship units. For example, vacancy pre-pandemic on London's Oxford Street (western end) had climbed 543bps over the course of 2019.

However, recovery in these locations is starting to pick up pace. Based on a select number of markets where we have historical vacancy trends, the vacancy rate has compressed by an average of 639bps since their pandemic peak and are now on average only 64bps above where they were in 2019. Madrid's Preciados vacancy is zero, in Q1 2020, it was at 5.0%. This squeeze on vacancy is starting to generate upward pressure on rents in some markets, albeit largely confined to those smaller markets with tighter levels of supply. Beyond London, Paris and Milan, the prime mass market streets across Europe have seen average rental growth of 2.2% since 2021.

As with the luxury streets, it's been those more 'expensive' mass market streets where international footfall constitutes a larger component of spend that continue to lag, with Champs Elysées in Paris and Oxford Street (west) in London being prime examples of this. Vacancy ranges from 9-12% with prime rents are at least 25% below where they were in 2019 on both streets, but these locations are both undergoing significant change via major redevelopments and enhancement of their public realm. Changes that will ultimately enhance their appeal to visitors, and in turn brands, as evidenced by recent leasing activity.

Vacancy trends across select prime mass market high streets



Source: Savills Research

What's driving occupier demand on these prime high footfall high streets?

Firstly, occupier demand for prime high streets across Europe has seen a strong bounce post the pandemic. And in some markets, such as southern Europe, demand is perhaps stronger than what was seen in 2019. There are some concerns around the strength of consumer spending going into 2024, which is generating headwinds in some markets such as Germany and the Nordics. But in most cases, brands are taking a longer-term view buoyed by strong balance sheets alongside rebased rents and improved availability in target markets.

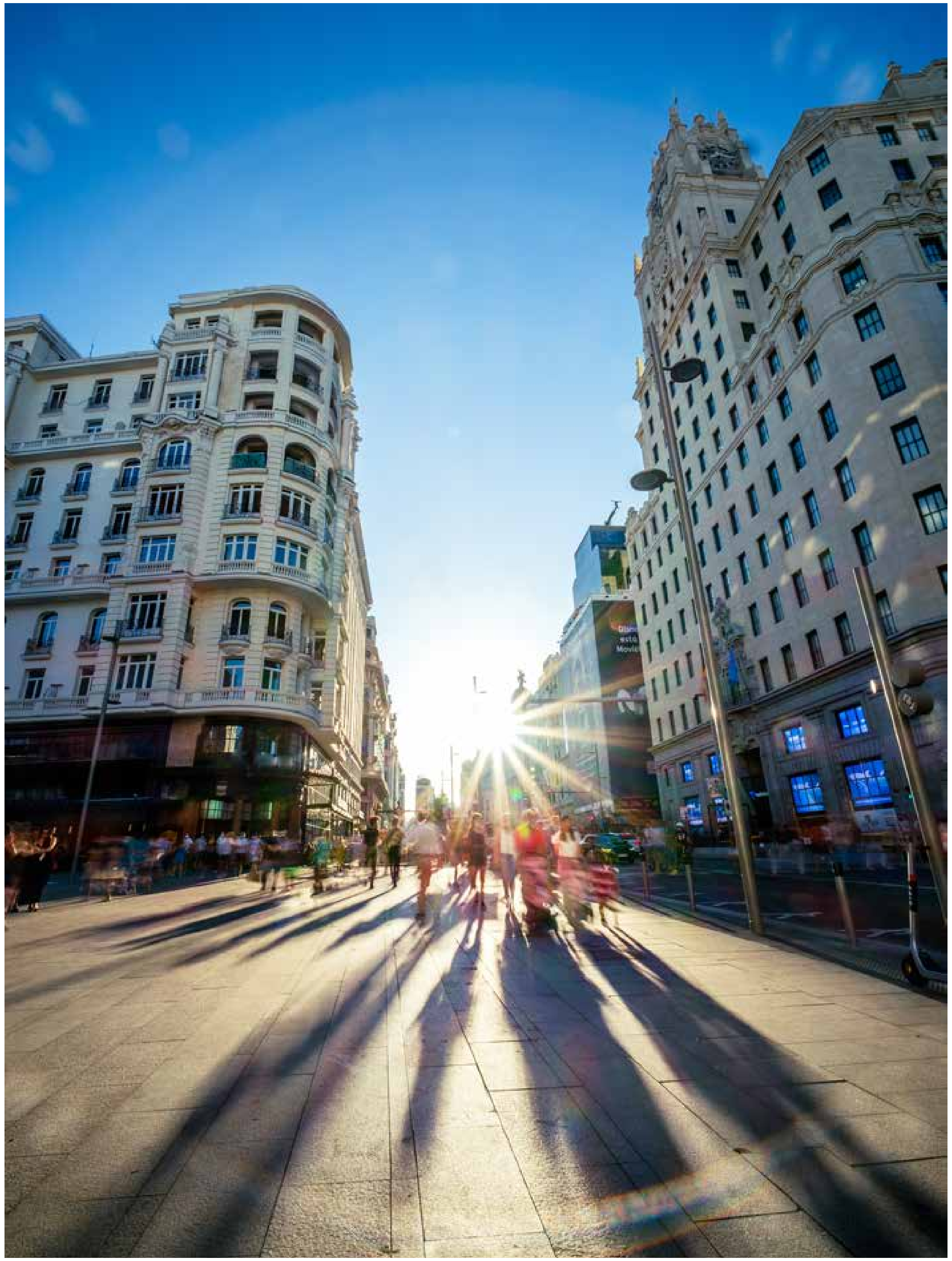
What is perhaps different post-pandemic is the focus by some occupiers on city-centre locations. There is a definite appetite from brands to be in city centres to enhance their visibility to a greater number of customers, with a view to drive sales. Even with the entrenchment of agile working, prime high streets across Europe can deliver on this visibility and for a range of cities we track, prime segments on key mass market high streets can have an average monthly footfall of above 860,000. On Champs Elysées, a unit on its prime pitch could see footfall as high as 1.5 million per month.

When it comes to who has and will be driving this demand going forward, the profile of occupiers and their specific requirements is perhaps the most diverse than we have ever seen (see page xx for more detail). Even for the major fashion groups and their stable of brands, such as Zara and H&M, their occupational demands vary from market to market, ranging from upsizing flagships to rolling out new smaller concept stores in order to enhance their ability to secure new sites and grow their footprint.

Current vacancy

Preciados, Madrid	0%	MASS MARKET
Monte Napoleone, Milan	0%	LUXURY
Biblioteksgatan, Stockholm	0%	MIXED: LUXURY & MASS
Part of Birger Jarlsgatan	0%	LUXURY MARKET
PC Hooftstraat, Amsterdam	1.2%	LUXURY MARKET
Nedre Slottsgate & Karl Johan, Oslo	2%	MIXED: LUXURY & MASS
Vittorio Emanuele, Milan	3.3%	MASS MARKET
Portal de L'Angel, Barcelona	3.8%	MASS MARKET
Avenue Montaigne, Paris	3.8%	LUXURY
Grafton Street, Dublin	4.4%	MIXED: LUXURY & MASS
Passeig de Gracia, Barcelona	4.9%	MIXED: LUXURY & MASS
Kalverstraat, Amsterdram	6.1%	MASS MARKET
Bond Street, London	6.4%	LUXURY
Oxford Street, London	9.4%	MASS MARKET
Oretage y Gasset, Madrid	9.8%	LUXURY
Champs Elysees, Paris	12.2%	MIXED: LUXURY & MASS

Source: Savills



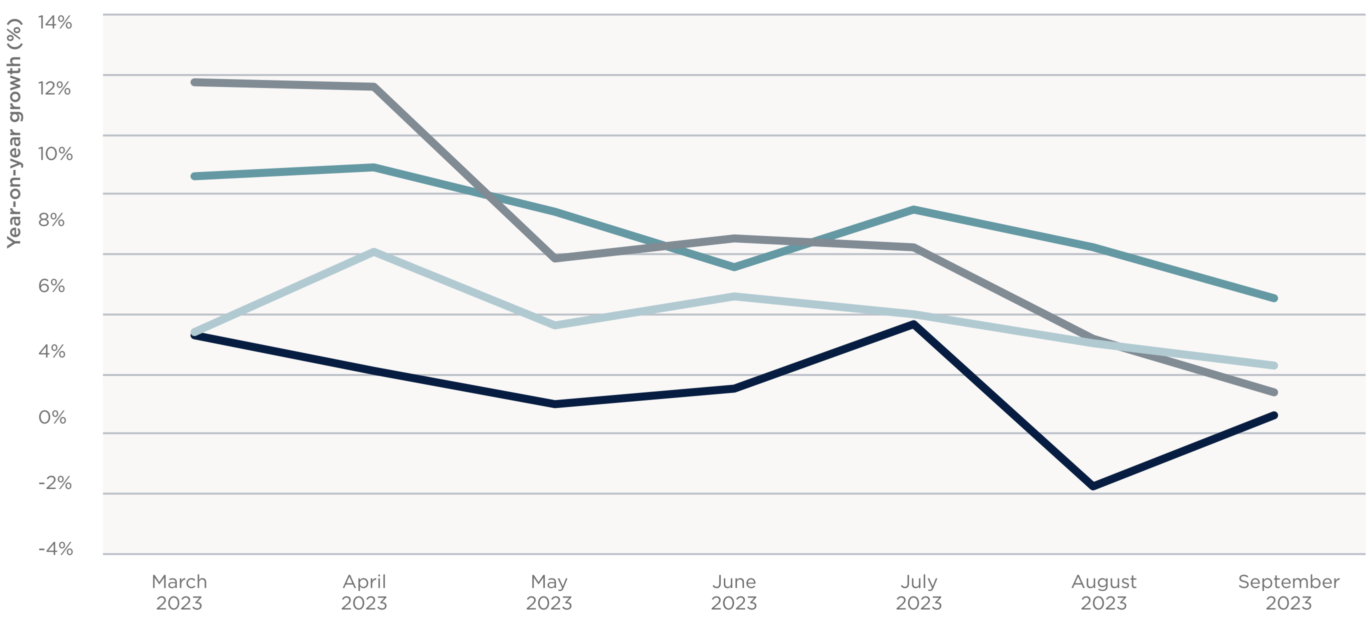
Shopping Centres

Footfall recovery may be lagging, but basket spend on the up

Shopping centre (SC) footfall is yet to recover to pre-pandemic levels, with several markets showing -15-20% down on levels recorded in January 2020. However, basket values have increased in most countries we monitor; this is largely an inflationary impact rather than an increase in purchasing sentiment, but it does point to more purpose-driven consumerism.

The post-Covid bounce-back in footfall seen in 2022 has slowed through the course of 2023 as the cost-of-living crisis has unfolded, yet growth remains in positive territory, albeit marginal in most markets. Spain and Portugal have bucked the trend, with year-on-year growth in footfall above 4% throughout the year. Visitors are a key factor here, accounting for more than 10% of turnover in schemes in tourist hotspots. Meanwhile, secondary shopping centres across Europe show signs of struggling to remain relevant, accelerating the polarisation between strong and weak assets and is reflected in a variation in vacancy and rental tone.

Annual shopping centre footfall growth



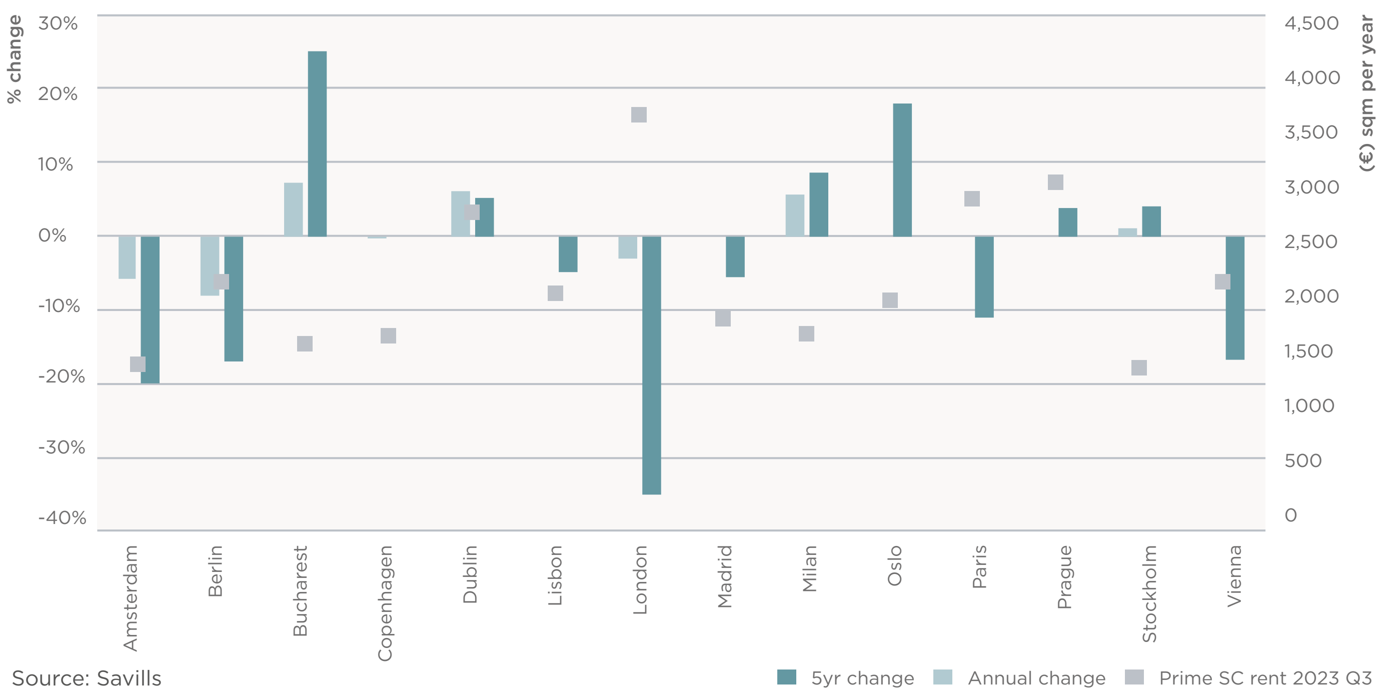
Source: Savills

Rental changes: rebasing, adjustment & growth

The shopping centre rental picture highlights three themes that dictate the variations in different markets: rebasing, adjustment and growth.

Cities that have seen significant rebasing of prime rents over the last five years include Amsterdam, Berlin, London, Paris and Vienna, where rents have fallen 10-35%. This brings the rents of prime shopping centres in these cities down towards the benchmark average of €1,205 sqm in Q3 2023. This rebasing was being seen prior to the pandemic across a number of markets due to growing impact of online spend on retailer's store strategies, which was then exacerbated by the pandemic.

Prime shopping centre rents



Source: Savills

A second group of cities, including Lisbon and Madrid, have seen a 5-10% fall in rental values in the last five years. With no further fall in the last 12 months, this could indicate that the adjustment in rents has been sufficient. Whether adjustment or rebasing, the rental levels now seen in these cities' shopping centres are likely to make them look more affordable and attractive to tenants.

Cities that have continued to exceed expectations in rental growth given the economic backdrop include Dublin and Milan, with around 5% growth in the last year. Bucharest has seen 5% growth consistently each year since 2018, with prime shopping centre rents now exceeding those recorded in Amsterdam and Stockholm. In Oslo, rents have increased by 18% over the past five years.

The flight to quality by occupiers widening the gap between prime and secondary

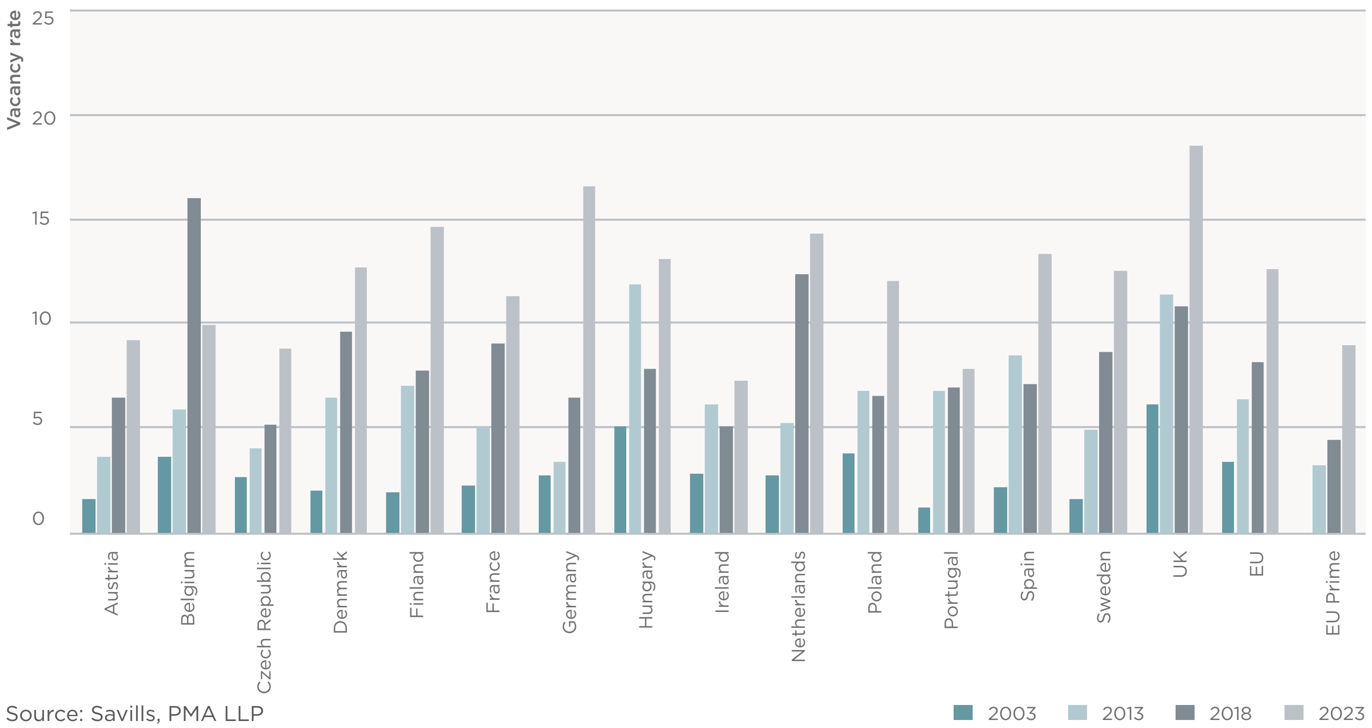
Shopping centre stock in both the Netherlands and Sweden are some of the highest in Europe on a per capita basis (0.3 sqm/0.5 sqm per capita), which may go some way to explaining the adjustment to rents seen in these countries. There is a loose correlation that more shopping centre supply tends to result in higher void rates and rental decline.

Irrespective of relative supply levels in each country, the long-term picture across Europe shows an increase in empty shops, with some schemes and retail brands struggling to keep pace with evolving consumer demand or are eclipsed by the growth of out-of-town retail formats and e-commerce. Twenty years ago, the average shopping centre vacancy rate in Europe was below 3%, but it doubles a decade later, with the UK being the only market with vacancy above 10%. In 2018, three more countries had seen vacancies in their largest cities reach double figures. By 2023, only three countries remain below 10%, with Germany, Netherlands, Finland and the UK now having voids above 15%. While these vacancy rates are reflective of total stock, a flight to quality means that vacancy for prime shopping centres is much lower.

The upward pressure in vacancy seen across the wider market is causing occupational and investment stress in markets with more mature provisions. This has been reflected in asset revaluations and the need for significant redevelopment; in recent years, a number of UK shopping centre assets have fallen in value by as much as 80% for the least relevant schemes. Value degradation for the most relevant, prime and dominant assets has been much less significant, in the region of 25%. Other European countries are also showing signs that stranded assets are a real proposition. However, the risk of empty shops still provides challenges to emerging markets where the rate of development has the potential to quickly saturate local markets and re-designate 'prime' supply. Hungary, for instance, has the highest growth in shopping centre rents in our benchmark, below average retail provision, and yet shopping centre vacancy is above the European average.

The nuance evidenced points to a trend that we are seeing unfold in almost all European markets and explains why we can record – at the same time in general terms – high rental growth and high voids in the same cities. This is the 'flight to quality' (F2Q), which is polarising the best and worst locations. F2Q sees additional demand for retail schemes in locations with the right offer in the right place and often creates an undersupply in the best pitches. However, it is clear from the limited pipeline of new shopping centre schemes across the block that investors are focussing primarily on repositioning, repurposing or redevelopment opportunities. More detail on this evolving trend can be found on page 28.

Average shopping centre vacancy rates



Source: Savills, PMA LLP

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Retail Parks

Rising footfall and falling vacancy; retail parks continue to out perform

The challenges to consumer spend and subsequent stronger performance in the discount and value retail segment has proved beneficial to retail parks. The convenience of these locations to consumers, particularly in those markets where agile working has become the norm post pandemic, has also come into play. This is evidenced by the fact that the most profitable retail parks are typically anchored by food stores, spend at which is often insulated by macro-economic headwinds as it is an essential spend category. It is also a retail sector where the online penetration rate is much lower compared to other parts of the market.

Consequently, retailers with a focus on essential product categories and value have continued to drive footfall to retail park's across Europe. UK footfall levels remain at parity with those seen pre-Covid, peaking over Easter weekend at 4.5% above the levels seen at the same time in 2019.

The strength of performance and subsequent growth ambitions of retail park operators has resulted in a decline in voids across Europe, with the UK dipping as low as 4.4% this year. However, if the available space that is no longer fit for purpose and needs to be repurposed is excluded, the vacancy rate is actually closer to 2.1% or just 81,700 sqm of available space – less than two years of supply. It is a similar picture across most of Europe and is reflected in the strength of rental growth over the last five years.

Dublin, Vienna, Amsterdam and Lisbon have all seen significant growth of 14% or more in prime rents over the last five years. In the case of Dublin, Vienna and Amsterdam, this is largely a consequence of low voids, exacerbated by a restriction in new stock. For Lisbon, it is more reflective of a market that is still emerging and gaining in popularity with consumers and occupiers alike. From a retailer's standpoint, retail parks offer competitive cost-effective operations, including lower rent and service charges than other retail formats.

There is still a positive story for those markets where rental growth has been absent over the last 12 months, or where we have seen rental declines, particularly when benchmarked against other retail segments. For example, prime retail park rents in London are down a total of 6% over the last five years; in contrast, prime rents on London's Oxford Street are down 40% over the same period. This highlights the relative resilience of the former particularly in light of recent events.

A restricted development pipeline will help to drive further rental growth

Retail park stock across Europe is projected to total 42.7 million sqm by the end of 2023. Stock has expanded by an average annual rate of 12% over the last five years, but this expansion has been slowing, with a 2% increase recorded for 2023. Despite the incremental increase in supply across the continent, various markets are at varying evolutionary stages.

Sweden (0.33 sqm), UK (0.16 sqm), Netherlands (0.14 sqm), Austria (0.14 sqm) and Ireland (0.14 sqm) all have the highest retail warehouse supply on a per capita basis – above the European average at 0.10 sqm per person. Both annual and five year growth in supply in these more mature markets has been subdued. But this is not reflective of weak demand as evidenced by the strength of rental growth in some of these markets; Dublin has seen prime retail park rents increase almost 15% over the last five years. Rather, the restrictive development pipeline is a response to a combination of reasons.

Firstly, the demand for large plots has proved difficult to satisfy when development space is at a premium and is often competing with the ambitions of the residential or logistics property market. Furthermore, build costs have also proved to be prohibitive across a number of these more mature markets, and as a result, many retail park developments are now for smaller schemes. The 3.4% growth in UK stock over the last five years has almost exclusively be through the expansion of existing schemes, allowing landlords to drive greater value from their existing portfolios.

New high growth, under-supplied markets, emerging

Portugal, Finland, and Denmark comprise a group that epitomises emerging markets, with the lowest overall stock levels in Europe and below-average supply per capita. This relative under-supply on a per capita basis presents an interesting development and investment opportunity, one that is starting to be realised when considering historical trends. For example, expansion over the last five years in these markets has been in excess of 15% when compared to 2018, albeit this does reflect growth off a low base.

Poland has been one of the fastest growing markets in stock terms having seen growth of 84% over the last five years. As a result, it is relatively well supplied in terms of total quantum of stock, coming second to Spain with 2.4 million sqm of stock. However, Poland continues to have one of the lowest densities of retail park stock per capita at 0.06 sqm. The more mature markets of the UK, Netherlands, Sweden, Austria and Ireland have more than doubled this, with stock per capita averaging 0.18 sqm. While a further 900,000 sqm of new space is expected to be delivered by 2026/2027 into Poland, helped in part by the relative ease developers can source suitable out-of-town locations, it will only have an incremental impact on per capita supply increasing it to 0.08 sqm per capita.

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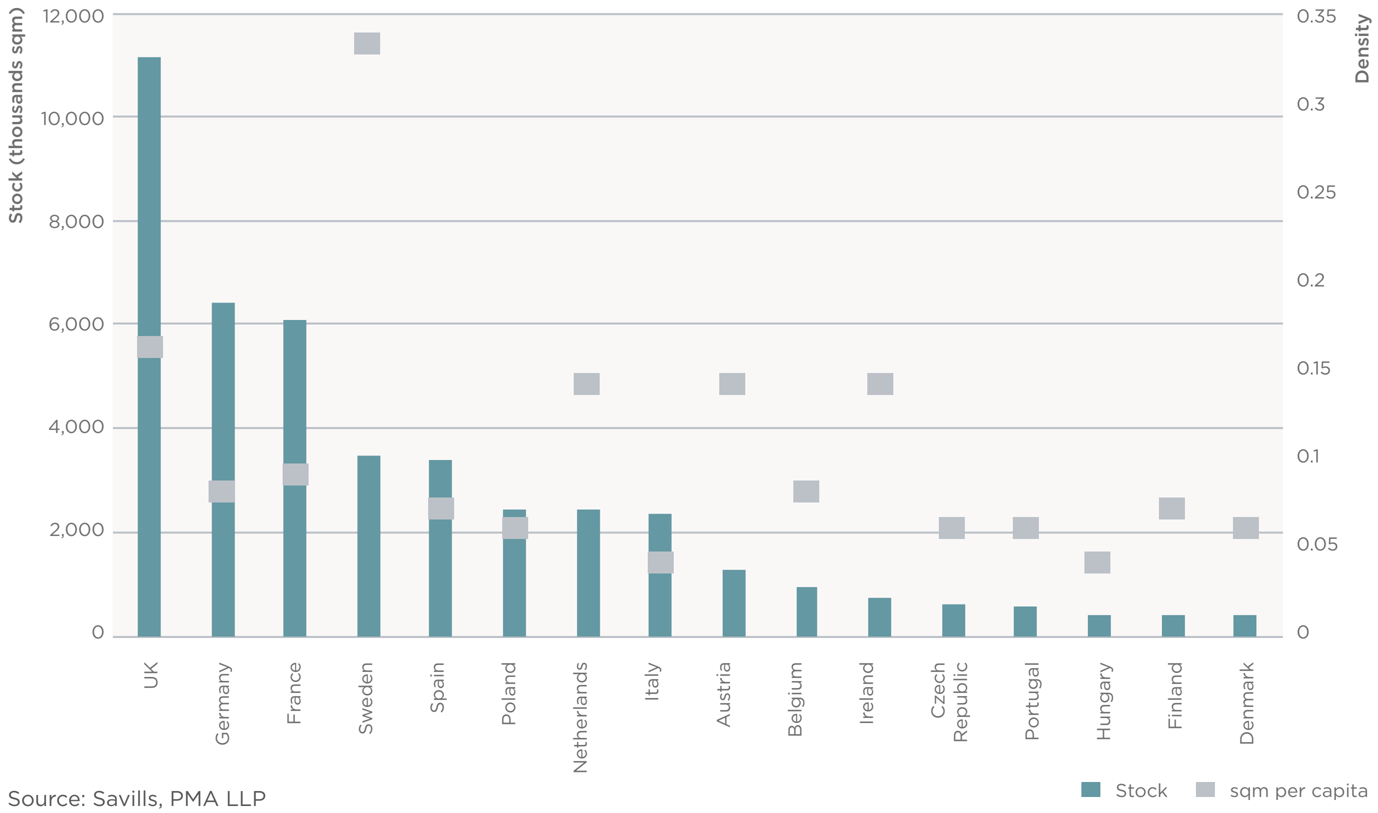
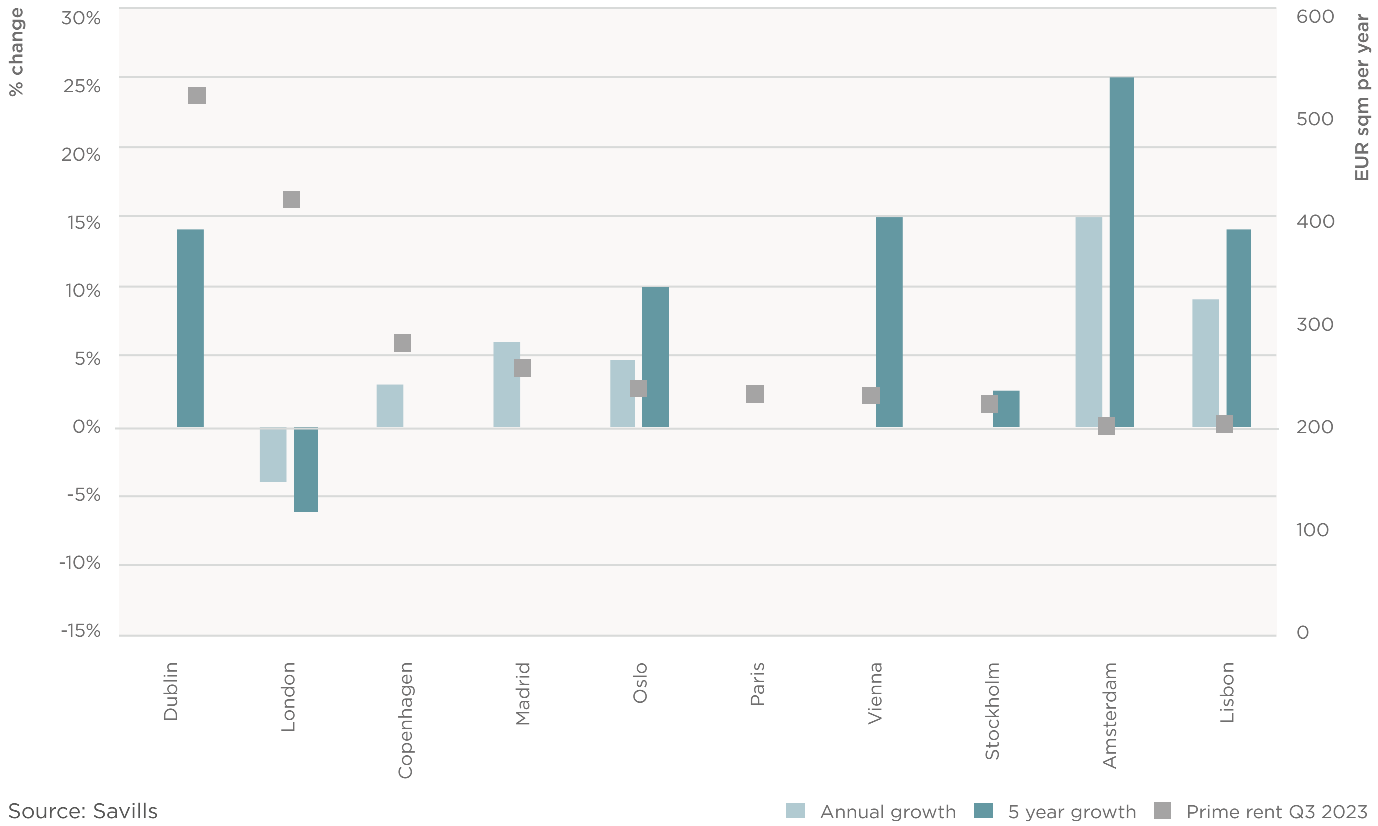
Retail warehouse stock



Source: Savills, PMA LLP

Prime retail warehouse rents



Source: Savills

Occupier Trends

What are the new and most expansive segments and brands to watch?

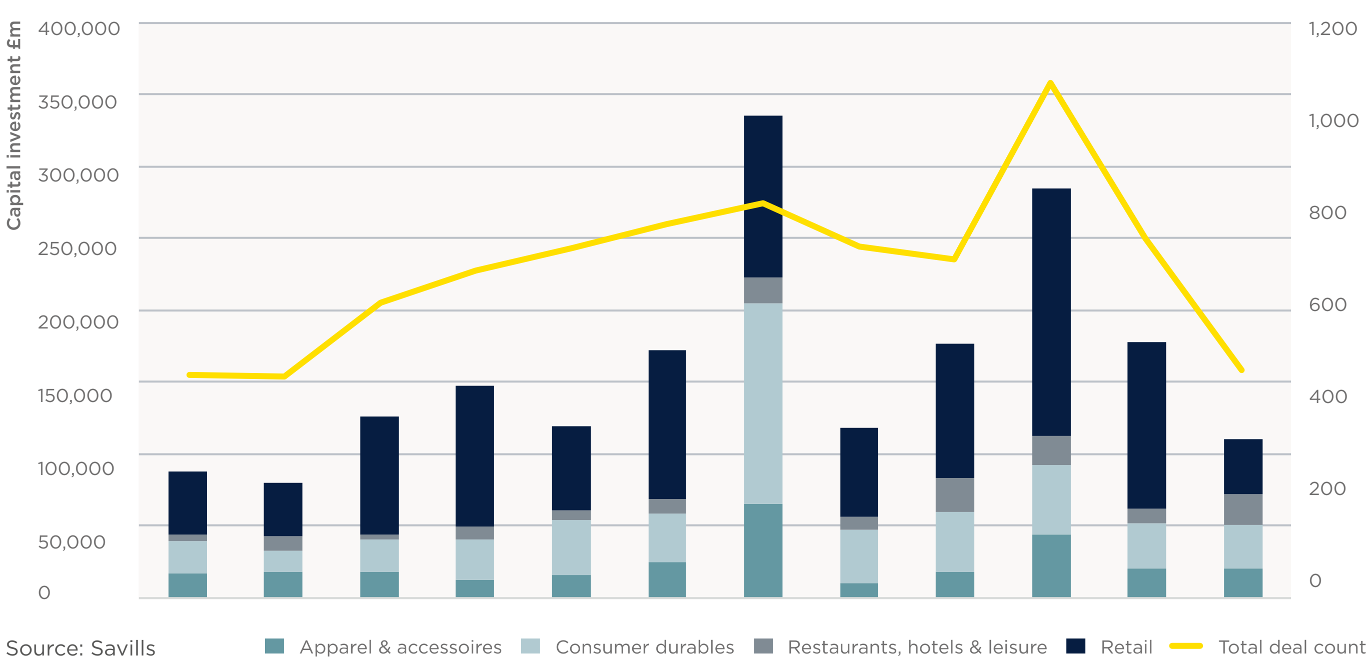
Despite the pandemic and the shift of retail spend online, investment into retailers and their associated brand industries (apparel, consumer durables, restaurant and leisure) has been on an upwards trend. Investment over the last 18months has slowed but 2021 was a new three year peak totalling £284bn globally, with retail companies receiving 61% of this investment.

But, does this tell us anything about future expansion into physical space?

Typically, fresh investment often translates into new space requirements, albeit this will be dependent on the types of companies receiving investment. In the case of recent trends, the bulk of activity has been focused on verticals related to E-Commerce with some of the largest growth seen for verticals covering supply chain technology (+150% 3yr CAGR) and mobility technology (+152% 3yr CAGR). There has also been increased investment into companies that are more likely to take physical space. Beauty, for example, has seen cumulative investment expand 79% per annum over the last three years. Wellness-focused companies have seen inflows increase by 60% per annum on the same basis. Likewise, restaurants, leisure and hotels have seen a 17% increase per annum, with significant growth in E-Sports (+80% per annum) and Gaming (+71% per annum) concepts.

These recent investment trends are already starting to feed through to space requirements, some of which are explored in more detail opposite.

Global capital investment into Apparel, Consumer Durables, Restaurant, Leisure and retail companies & brands



Source: Savills

Most expansive segments and market hotspots

ATHLEISURE

London & Southern Europe

Hotspots: Premium and high footfall high streets

Brands: On/ Alo Yoga/ Fabletics/ Vuori

EV BRANDS

Northern Europe

Hotspots: High footfall high streets & major destination shopping centres

Brands: NIO/ Zeekr/ Geely Group

BEAUTY

London & Paris

Hotspots: Premium and high footfall high streets

Brands: Diptyque/ Aesop/ Byredo/ Sephora/ Kiko Milano

FUNITURE & HOME

Southern Europe

Hotspots: Premium and High footfall high streets; major regional destination shopping centres

Brands: H&M Home/ Zara Home/ Ikea/ Bolia

F&B

Hotspots: Premium and high footfall high streets

Brands: Big Mamma Group

BIG BOX | IMMERSIVE

Hotspots: High footfall high streets & major destination shopping centres

Brands: Culture Spaces/ Museum of Illusions/ Moca Museum

VALUE RETAILERS

Germany, Southern Europe, Central Europe

Hotspots: Retail parks

Brands: Lidl/ Aldi/ Home Bargains/ Pepco Group/ Mercadona

COMPETITIVE SOCIALISING

Germany, Southern Europe, Central Europe

Hotspots: High footfall high streets and shopping centres & major European cities

Brands: Lane 7, F1, Activate

Retail Investment

Investment activity remains relatively resilient

European retail investments over the first nine months of the year totalled €17.7bn, which was 34% below the five-year average for the period. Whilst volumes were down, activity fared better than other European asset classes; multifamily and office investment over the same period was down -57% and -53%, respectively, against their five-year average. Nearly all countries saw retail volumes down against their five-year average bar Ireland (+69%), the Czech Republic (+54%) and the UK (+13%). As a result of robust activity in the UK, the core markets (UK, Germany and France), captured 71% of this retail activity.

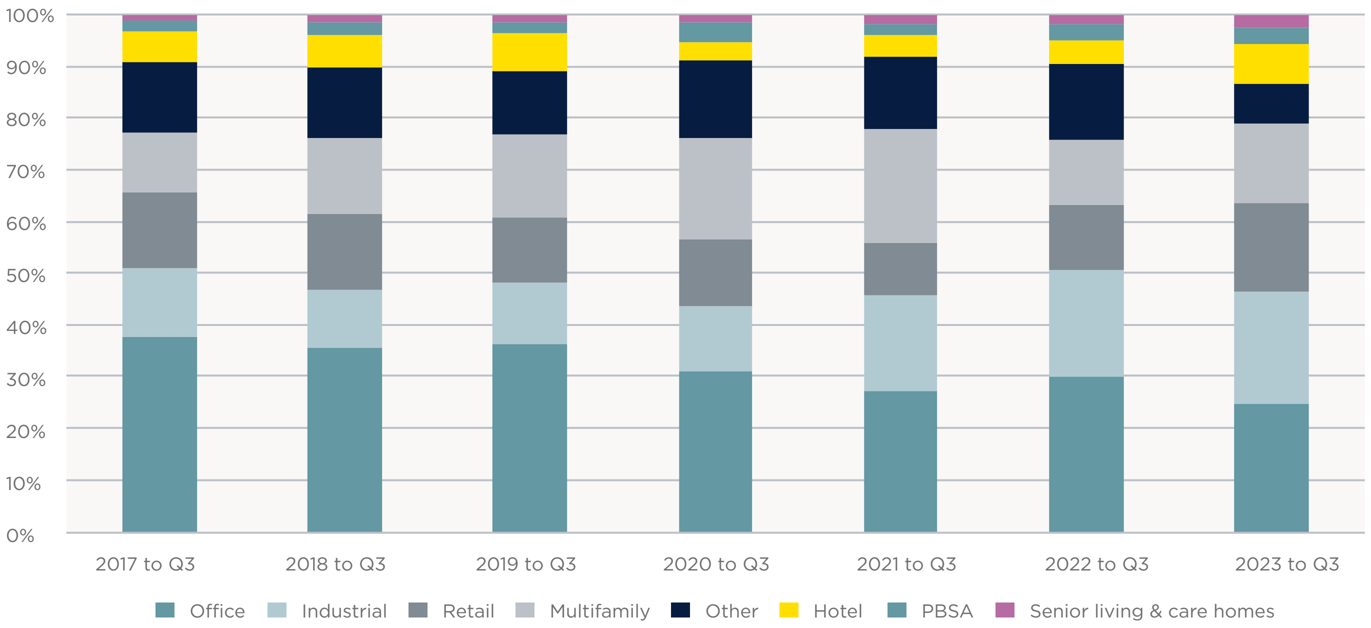
The relatively shallower declines in volumes against other segments meant retail accounted for 17% of total European investment volumes, its largest share since 2016. Compared to the past five-year average, retail volumes declined in nearly all countries except Ireland (+69%), the Czech Republic (+54%) and the UK (+13%).

Why has investment proved to be relatively more resilient?

It's a combination of factors. Higher yields, particularly in light of higher debt costs, and weaker investor confidence in other asset classes have all come into play.

The sector had already seen strong repricing over the past five years (+150 bps on average across Europe), meaning it had become highly attractive to investors seeking yield. This appeal has been further intensified in the current high financing cost environment, with pockets of liquidity emerging. These include assets offering defensive qualities, divestments from investors looking to raise capital and secondary assets with active asset management, redevelopment, or repurposing angles. Investment volumes have also proved to be relatively more resilient in response to investors growing diversification strategies and, more recently, weaker confidence in the office sector, particularly in light of its much tighter, or even negative, spread to debt costs.

Share of retail investment



Source: Savills

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However, banks and lenders remain cautious about the sector, with a reduced appetite to participate in potentially high-risk transactions. This is reflected in the decline in the number of large, high-leverage deals that once fuelled market growth and were relatively common in the retail sector. We have seen a number of large portfolios across Europe fail to attract buyers due to lenders' reluctance to finance these substantial transactions. Collaborative efforts have emerged as a prudent strategy for adapting to these evolving dynamics. In some countries, financial institutions and buyers are increasingly opting for joint venture arrangements to mitigate the associated risks in these sizable deals.

Acquisitions by occupiers accounting for a larger share

One notable emerging trend of the last 12 months has been the increasing number of retailers opting to purchase the buildings they rent. They accounted for more than 10.3% of total retail investment. This is an increase on their 6.7% share recorded for the same period in 2022 and significantly up on the 1-2% share seen over the preceding five years.

The most active in this group have been the supermarkets. The likes of Sainsbury's, Aldi, Lidl, Tesco, Coop, and Edeka, sitting on fairly major cash reserves, are capitalising on the downward pressure on capital values. This approach offers retailers greater independence from rental dependencies: a prudent move for both retailers' stability and long-term profitability.

Robust investor appetite for retail parks and grocery stores

Unsurprisingly, considering the strength of its occupational market, retail parks have been the most resilient part of the retail investment market, recording the lowest annual decline in investment volumes (-26%).

Strong activity was recorded in Italy, thanks to a few portfolio deals, including the joint acquisition by Polis Fondi and LeadCrest Capital Partners of Technomat properties (five properties) for €70bn. There has also been strong activity in CEE countries, notably Austria, Czech Republic and Poland. That said, most of the retail park investment activity seen to date in 2023 was concentrated in the UK, a reflection of the fact that it is a more mature asset class in that market. This meant the UK accounted for 45% of European retail park investment volumes.

Grocery store investment, including supermarkets and hypermarkets, remained relatively unchanged, accounting for approximately 19% of all year-to-date retail investment volumes. Strong activity was recorded in the UK, mainly due to two large occupier acquisitions by Sainsbury's in January and March for €960 million and €867 million, respectively.

The more subdued activity in the grocery market in 2023 is a reflection of a lack of opportunities rather than a lack of investor appetite, which is very focused on assets occupied by discount and value-orientated brands. Big US REITs such as LCN and Realty are notably very active in that space, particularly across the larger lot sizes. At the smaller end of the spectrum, there is a much wider investor pool, which has helped to generate downward pressure on prime yields.

Luxury high-street opportunities drive high-street investment

Overall, investors' appetite for luxury high streets is somehow mitigated by the fact that there were not enough price corrections. However, high-street investments accounted for 28% of the total retail volume transacted in the first nine months of 2023, in line with the five-year average of 27% but up on the 19% share recorded last year. This relative resilience has been driven by a small number of trophy assets signed in Paris, London and key German cities, including the Louis Vuitton Flagship on 101 Champs Elysées bought by LVMH from Gecina for €770m. As evidenced in this deal, and similar to that seen in the grocery market, luxury brands have become increasingly acquisitive both as a way to ensure occupational security and reduce exposure to future rental increases but also as a means to deploy capital reserves.

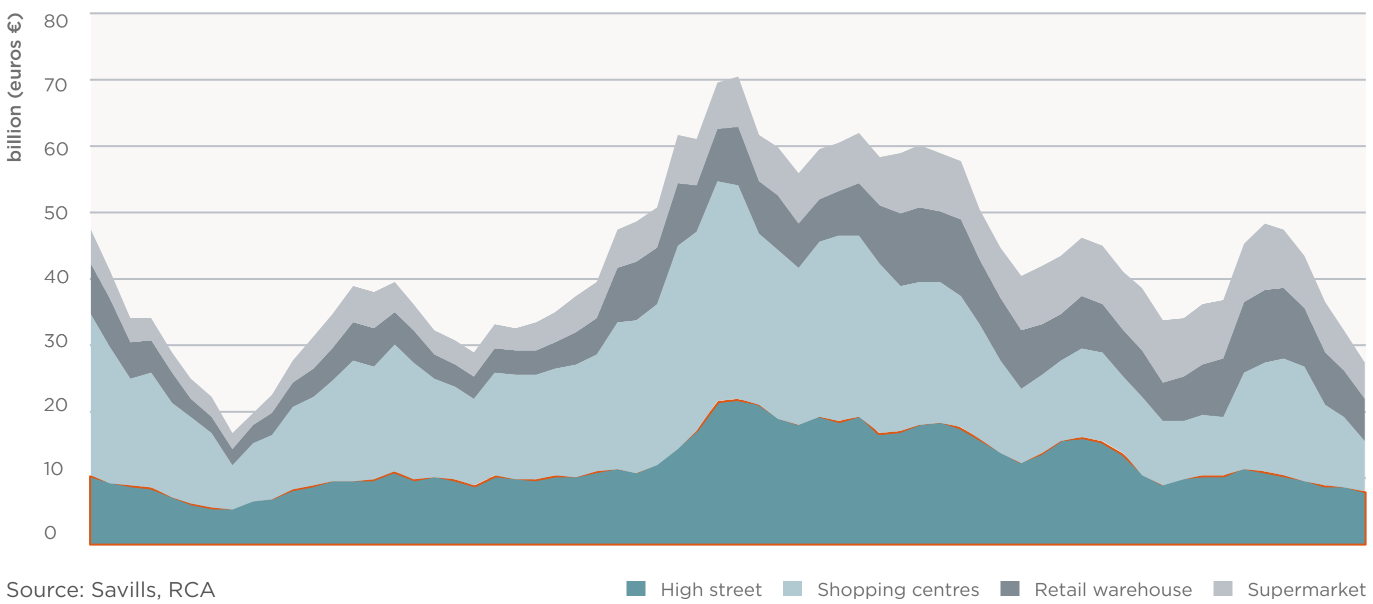
Shopping centre investment has been most exposed to rising debt costs

Despite a slight rebound in shopping centre investment activity during the first half of the year, volumes contracted in the third quarter, meaning that year-to-date volumes as of September were down by nearly 49% year-on-year. Despite this decline, shopping centre investment still accounted for a sizeable share of total volumes at 27%, albeit below its historical five-year average share of 33%.

France grabbed the largest market share of shopping centre investment (33%). Notable French transactions include the acquisition by Ingka group (IKEA) of the "Italy portfolio", two shopping centres based in the Paris 13th district from Hammerson for €550m. Passy Plaza in Paris 16th district was bought by AEW Ciloger from Generali Re Investment BV for €130m, and a five-factory outlet portfolio (Marque Avenue) was bought by Mata Capital for €200bn.

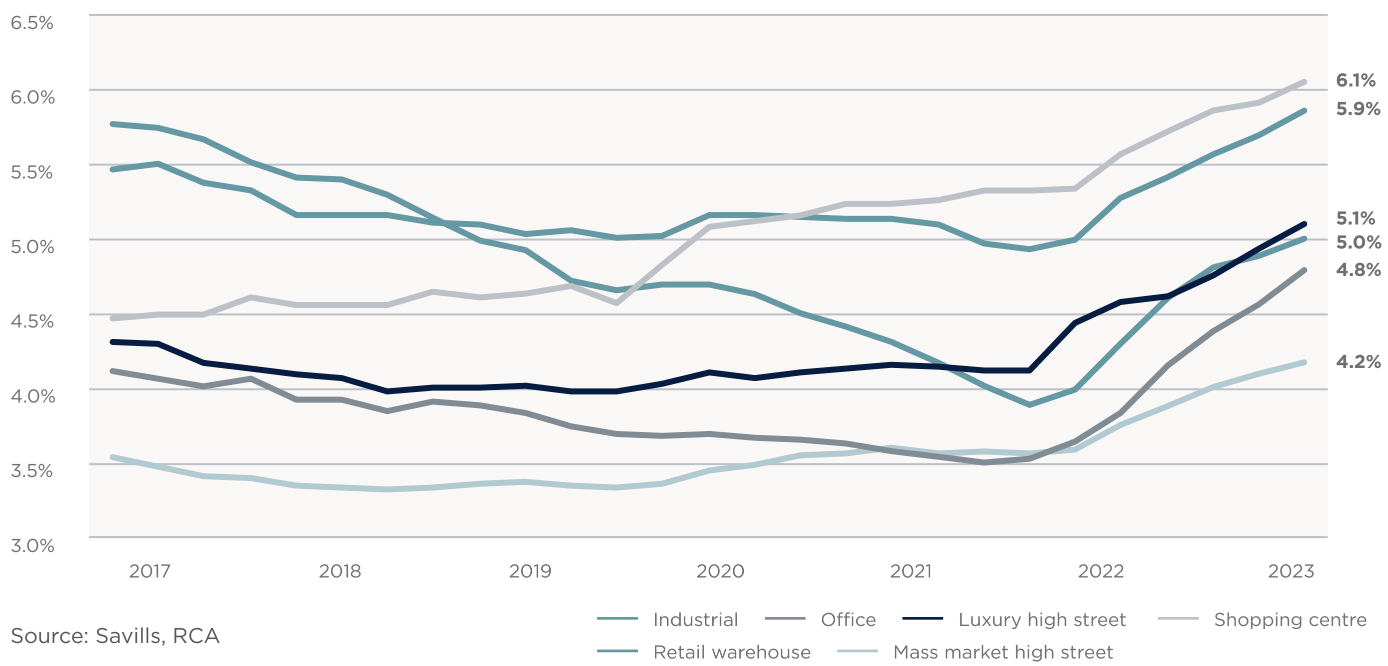
Generally, shopping centre deals take longer to close due to asset-level complexity and the need to finalise business plans, which, in many cases, have a number of moving parts. In March, Generali and ECE completed the acquisition of the Pep shopping centre in Munich, a deal that was initially agreed upon in late 2022. Apart from the super prime assets, shopping centres generally attract value-add investors seeking opportunities to lease or repurpose. Factory outlet centres, which are a strongly performing subsector and offer transparency on tenant trade, remain on the investor radar. However, these types of investment opportunities are relatively rare.

Rolling past 12-month retail investment volume



Source: Savills, RCA

European prime average yields



Source: Savills, RCA

Upward pressure on yields continues, albeit the pace of softening is slowing

While the acceleration in debt costs in the latter part of 2022 and into early 2023 generated significant upward pressure on prime retail yields, this has been less pronounced than in other sectors where the starting yield was much keener. Since Q2 2022, for example, prime industrial yields have softened by 101 bps to average 5.00%, with office yields out by 116 bps to 4.80%. In contrast, prime retail yields across Europe have softened by an average of 71 bps over the same period to reach 5.30%.

There are also some early signs that yields are starting to stabilise. September 2022 saw the largest single outward shift in yields, with European retail reporting a quarterly softening of 20bps on a median basis. European Industrial yields over that same period softened by 31bps. Since then, we have seen consistent quarterly increases in yields, albeit the rate of this decompression has slowed, with Q2 2023 average retail yields moving out by 11 bps quarter-on-quarter, down on the 14bps softening reported the previous two quarters. The latest quarter did see a small acceleration in decompression to 15bps, but we are of the view that this will be a relatively isolated occurrence considering expectations that the current rate-rising cycle has peaked.

In Q3 2023, the European average prime retail warehouse yield stood at 5.9%, marking a 59 bps increase compared to the same period last year. The European average prime shopping centre yield was at 6.1%, reflecting an annual increase of 49 bps. Luxury high street yields were at 4.2% on average across Europe, 42 bps up on the same quarter last year and mass-market high street yields moved out by 53 bps annually to 5.1% in Q3 2023.

Going forward, with the deteriorating economic sentiment steering investors towards super-prime assets and restraining investment opportunities, we expect further yield expansion across Europe until mid-next year, yet at a slower pace than that recorded over the past nine months.

Repurposing & Sustainability

Diversification is happening and often under the radar

Repurposing is materialising across Europe, but only at scale in markets where there is an excess supply or significant retail failures.

Consumers have returned from the pandemic with a higher expectation for what will drive their footfall. Hence, the focus is on convenience-based and experiential retail and leisure formats, while the average mid-market schemes increasingly struggle to remain relevant and compete. Many retailers are consolidating their businesses, reassessing store numbers and reducing overheads amid significant cost inflation, which is hitting margins as well as consumer sentiment. Department stores have been affected particularly badly in recent years, and there are examples of repurposing projects within this subsector across the continent. The administration of Debenhams in the UK in 2021 left 126 units vacant, which have been re-occupied by retailers such as Marks and Spencer, The Range, TK Maxx in some locations, and repurposed for alternative uses such as cinemas, training centres and hotels in other locations.

In 2019, Canadian department store brand Hudson Bay closed 15 stores in the Netherlands. In 2020, Debenhams and Topshop went into liquidation following the fate of several other high-profile brands in large store formats in the UK, which is anticipated to result in 25% excess retail stock, of which 40% of vacant units are already redundant. It is estimated that 75% of shopping centres in Germany need to be repositioned or converted. In 2023, in Germany, Galeria Karstadt Kaufhof has closed 52 stores, the majority of which are being considered for redevelopment as there are not enough alternative retail occupiers leasing large units.

Retail repurposing was already starting to happen in several countries before COVID-19 as part of longer-term structural changes to the consumer-retailer dynamic. But there is no doubt that the pandemic accelerated these trends into focus. We saw the increased reliance on convenience and amenity, the importance of health and wellbeing, and an appetite for leisure experiences and F&B, with these trends persisting into 2023 despite consumer inflationary concerns.

European Retail Market | 2023

Blended consumer uses are reviving spaces, but sticking to leisure where possible

The range of uses being considered for redundant retail space is varied, and while most notable when accounting for larger stores or SC blocks, small-scale adjustments to tenant line-ups mean that many schemes are evolving into more blended and relevant propositions.

La Vie shopping centre in Porto is undergoing a retail-to-office conversion, with phase 1 already complete and operating.

Clerys Department store in Dublin has been converted to provide a blend of retail, office, leisure and F&B to reinvigorate a key city high street.

X-Madrid has seen a struggling traditional big-box leisure scheme transformed into an experiential leisure and retail destination. 47,000m2, including surfing, scuba diving, event space, cinema, gaming and leisure retail, plus a wide range of F&B.

Maj, Prague sees a department store repurposed to create a new 17,000m2 shopping centre, which shows that repositioning is about creating relevant spaces and not just conversion away from retail.

Schemes across Portugal, Germany, Poland, the UK and Sweden have seen an increase in alternative consumer uses, such as medical uses and veterinary services, taking single stores or upper floors of SCs. This represents an important diversification away from pure retail while extending hours of operation and creating additional footfall drivers.

What about markets where repurposing is not currently a consideration, where the void rates are low and where there is a pipeline of new retail development? The key question is whether future developments will address the macro trends being felt in more congested markets by building more flexible agile places with a more blended offer or continue to develop 'retail only' developments. The clear message to the market is that the future of retail is in adopting the right balance of mixed consumer uses if they are to be future proof, particularly on locations off the prime pitch.

An imbalanced transition towards sustainability measures

SCs are moving towards investing in energy efficiency initiatives with lots of activity across Europe. The cost of energy and extreme weather events has created a greater sense of urgency. Spain and Portugal are arguably ahead of the curve. A Portuguese study examining sustainability practices in shopping centres, states that 85% of operators have good management practices, in line with the UN's sustainable development goals, and 57% already produce photovoltaic energy or are developing projects in this area. The average recycling rate in the industry is 53%, and half of the SCs are BREEAM, LEED or WELL certified. Spain has 100 BREEAM-certified SCs and 50 more in the pipeline.

Across the rest of Europe, the cost of implementing measures and applying for certification has resulted in a lower take-up. The UK has some of the highest SC provision in Europe (over 800 schemes), but only a handful of BREEAM building certificates and BREEAM in use is yet to reach double figures. While SCs across Europe are implementing a range of efficiency measures, overall, the changes are not sufficiently rapid to meet carbon targets. With investors increasingly seeking green assets (often as a result of fund criteria), schemes that fail to install adequate measures are likely to find declining investment interest and risk becoming obsolete.

There is a close synergy between optimising space through repurposing underutilised retail space and undertaking sustainability measures simultaneously. Refurbishing buildings provides an opportunity to implement greener infrastructure while bringing in more meaningful uses, extends the life of the buildings and can reduce embodied carbon. Investor sentiment is increasingly drawn to redevelopment opportunities where they can add value and meet net-zero targets.

Savills Outlook

What does the next 12 months have in store?

Consumer Landscape:

Consumer landscape Headwinds to retail spend to dissipate and stronger growth to emerge, supporting stronger trade performance

- Retail sales in Europe forecast to increase 3.7% in real terms in 2024, supported by real disposable incomes moving back into positive territory as inflation continues to slow.
- All major European markets are forecast to see retail sales growth next year, with the growth markets of 2023 (Ireland, Spain, Portugal) continuing to report growth in excess of 2%.
- The evolution of consumer spending habits and the prioritisation of experience spend is expected to continue, feeding positively into F&B and leisure spend.

Retail Parks:

Space is at a premium in all but emerging markets, which will lead to further rental growth

- Occupational demand to continue into 2024. For those markets where availability remains significantly constrained, but where spend performance is strong, competitive tension will materialise generating upward pressure on rents.
- Stock expansion to continue, led by those emerging markets that have the lowest per capita stock and have seen some of the highest expansion to date. These include Portugal, Finland, Denmark and Poland.

Prime High Streets:

Momentum builds with major mass market streets accelerating their recovery

- Vacancy will continue to be squeezed, with rental growth to continue. This is likely to be confined to markets beyond Germany and the Nordics over the next six months.
- London's Oxford Street and Paris' Champs Elysées will continue its recovery trajectory with availability constraints to intensify in the latter part of 2024. Its rental recovery likely to be more protracted and extend into 2025.
- Luxury demand for new sites in major cities to slow, in line with the current normalisation in trade. Hotspots of activity will materialise as new best-in-class opportunities in key streets, such as Bond Street and Champs Elysées, are delivered.
- Strong appetite for smaller affluent markets by luxury brands will continue with a growing interest in resort markets.
- Demand on major high footfall mass market streets to further diversify; F&B and leisure will become more pronounced with new entrants from Asia Pacific targeting flagship opportunities in London, Paris and Milan.

European Retail Market | 2023

Shopping Centres:

Vacancy rates expected to reach double figures in most markets, but prime assets continue to be more defensible

- The polarisation between prime and secondary assets to continue to widen. Beyond prime destination shopping centres, vacancy is likely to get a little higher before it starts to recover in late 2024. For secondary and tertiary schemes, further challenges await, with vacancy rates continuing to track upwards through 2024, particularly if there is a significant alternative supply.
- Vacancy trends will dictate rental performance, which we expect will remain flat for prime assets over the course of 2024 with upward pressure on rents to emerge in 2025.
- Landlords to increasingly look to introduce a more dynamic and leisure-orientated offer into their schemes in order to increase footfall, dwell time and ultimately retail spend.
- Investor sentiment should improve in 2024, with assets in some markets likely to look good value, particularly if there is a compelling redevelopment angle.

Investment:

Retail's relatively higher yields will continue to attract investor interest, with the focus on more defensible assets such as retail parks and supermarkets

- Prime yields are stabilising, with further outward shifts anticipated to be minimal and restricted to the first half of 2024.
- The continued repricing of retail assets, particularly in relation to other real estate asset classes, will intensify investor appetite.
- Investment activity has bottomed out, with volumes likely to increase over the next 12 months. This resurgence is anticipated to be most prominent in countries where significant price corrections have occurred.
- The expected decline in central bank rates in the latter part of 2024 and into 2025 will provide a boost to investment activity. This will generate downward pressure on prime yields in some parts of the market.
- Grocery stores, supermarkets and retail parks will continue to capture most of investors' appetite for retail assets. High street investments will remain restrained by the lack of opportunities on the market rather than a lack of appetite.

Savills Research
We're a dedicated team with an unrivalled reputation for producing well-informed and accurate analysis, research and commentary across all sectors of the UK property market.

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