Briefing note
Restaurant expansion in shopping centres: path to success or a wrong turn?

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People are eating away from home with increasing regularity. Many shopping centres are responding to this appetite for eating out with a larger restaurant offering, killing two birds with one stone. They are replacing unproductive retail space and positioning themselves as leisure destinations. Is this a promising strategy?

Eating at home? Get out of here!

Germans are not exactly renowned in other countries for their culinary culture. A few figures demonstrate why. The average German consumes more than 45 kg of frozen food per year. Almost a tenth of this is attributable to frozen pizza. However, there is one particularly striking trend. While retail sales of frozen pizza have increased by “just” 13% over the last five years, eating-out sales for the same product have risen by more than 60%. However, it is not only pizzas that are being consumed away from home with greater regularity in Germany. Overall household expenditure on eating out has risen by more than a fifth over the last five years (see Graph 1).

Shopping centres are responding with an increasing restaurant offering

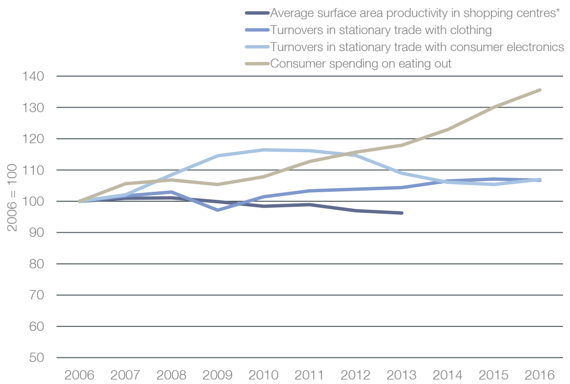
The appetite for eating out has come just at the right time for shopping centre managers, offering them the opportunity to compensate for the diminishing magnetic effect of former anchor tenants, such as clothing department stores and consumer electronics stores (see Graph 1) by expanding their restaurant offering. Restaurants also play an important role in centre managers’ endeavours to stage shopping as an experience in order to provide differentiation from online retail. Indeed, restaurant space in shopping centres has already been growing for some time, doubling to almost 8% of total lettable area over the last 10 years in Germany. The current model for a contemporary shopping centre entails a much higher percentage. The proportion of restaurant space in the MyZeil in Frankfurt, for example, will increase to 15% (from less than 5% previously) following the current modernisation, while the refurbishment of Hamburg’s Europa-Passage will take the restaurant offering to 20% (previously 13%). Similar plans have been announced for many other shopping centres.

Substituting retail space with restaurants with no loss of sales appears unrealistic

The strategy of replacing space with declining productivity (e.g. clothing and consumer electronics retail) with uses having increasing attraction appears logical at first glance. Whether rental income is generated via sales of clothing or food ultimately makes little difference. This is all the more true if not only the space but also sales can be substituted one for one. The idea that every shopping centre will achieve this, however, appears questionable. In the long run, consumers will not spend less money on jeans and televisions and instead have this at their disposal for burgers and pizzas. They will simply buy their jeans less often in shopping centres than previously and instead shop via Zalando et al. From a consumer's perspective, therefore, shopping centre restaurant sales represent additional outgoings that they must be willing and able to pay. If we assume that the proportion of restaurant space in German shopping centres will increase to 15%, this would translate into sales of approximately €3.4bn per year* that would have to be generated going forward in addition to the current sales of approximately €4bn from shopping centre restaurants. Based upon the

GRAPH 1

Consumer spending on eating out bustles off center-productivity



Source: GCSC, Federal Statistical Office / * data only available until 2013 average growth rate in eating-out expenditure over the last five years, this level would not be achieved until 2033. In view of the very good economic growth and relatively high population growth in recent years, this may already be an optimistic scenario.

Other retail formats are also expanding their restaurant offering

Consequently, centre managers will either require a large amount patience, which they may not be able to afford faced with declining sales from a number of their tenants, or they must succeed in attracting a significantly higher proportion of those eating out into their shopping centres. To date, shopping centres are likely to have accounted for only around 5% of overall expenditure on eating out. With revenues of almost €80bn in this sector each year, a modest expansion in market share would suffice for shopping centres to generate the required €3.4bn at least a few years ahead of schedule. However, since the trend towards an increased restaurant offering is not only evident in shopping centres but also in other retail formats, such as retail parks, as well as in prime locations, centre managers may struggle to achieve such expansion. Furthermore, the stores themselves are increasingly entering the food and beverage sector, which is completely excluded from any floor area statistics. More and more retailers are providing seated areas within their stores where they can serve their customers drinks, snacks and sometimes hot meals. In shopping centres, these are competing for the same custom as the in-house food courts.

Adaptation more promising than expansion

Our verdict is that the above-average growth in consumer spending on eating out relative to retail expenditure combined with stagnating or even declining revenues in several in-store retail segments offers shopping centres an opportunity to maintain, or ideally increase, visitor frequency and sales. However, this ‘reinforcement’ should not be equated with an increase in space. Even today, there is much to suggest that the supply of restaurants is growing ahead of demand. Should this remain the case, then the logical consequence is consolidation. Against this background, whether an increased restaurant offering is worthwhile for all shopping centres is questionable, especially since fit-out costs for restaurant space are relatively high. What may be the path to success for certain shopping centres is likely to be a wrong turn for the sector in its entirety. Consequently, we consider the adaptation of restaurant offerings in shopping centres according to their target groups in order to increase or stabilise the productivity of space, rather than simply “filling” space with weak sales, to be the more promising approach. Furthermore, depending on the location and structure of a property, it may be sensible to enhance the attractiveness of the shopping centre via alternative uses such as co-working spaces or libraries.

*Assumption: average rent for restaurant operators in shopping centres is €30 per sq m/month and is paid from 10% of turnover

Savills Germany

Please contact us for further information

Marcus Lemli
CEO Germany
+49 (0) 69 273 000 12
mlemli@savills.de

Karsten Nemecek
Corp. Finance - Valuation
+49 (0) 30 726 165 138
knemecek@savills.de

Draženko Grahovac
Corp. Finance - Valuation
+49 (0) 30 726 165 140
dgrahovac@savills.de

Jörg Krechky
Retail Investment
+49 (0) 40 309 977 144
jkrechky@savills.de

Thomas Pasiecznik
Retail Agency
+49 (0) 211 22 962 260
tpasiecznik@savills.de

Matthias Pink
Research
+49 (0) 30 726 165 134
mpink@savills.de

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