



European High Streets

December 2023



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Key takeaways

- Retailers continue to consolidate, focusing on fewer, but bigger and strategically located, flagship stores.
- Income streams for quality assets are stable, or stabilising, as prime rents have rebased substantially.
- An omni-channel approach is crucial for retailers with online now seen as less of a threat as footfall to physical stores rises in parallel with a slowdown in online spend.
- The Eurozone economic recovery has been delayed to the latter half of 2024 as monetary tightening filters down through the economy.
- Inflation is past its peak and is trending down but the situation for households remains challenging. There are however signs of improvement.

Drivers of retail



Tourism: the return

It is said that people have short memories, and this seems to be the case in terms of the resumption of travelling in the wake of a pan-regional or global events such as SARS in 2002/3 and COVID-19 in 2020.

This is good news for the retail sector as tourism is an important indicator of the health of our international high streets. Travel, both domestic and international across Europe, had been steadily picking up since the dip experienced in 2009 following the Global Financial Crisis, although incomparable to the 65% fall seen in 2020 as governments around the world locked down their economies

“The resurgence of Europe’s luxury high streets is gathering momentum, supported by a solid rise in tourist numbers and spend, whilst in parallel, the growth in online retail has slowed and is no longer seen as the intense threat to physical stores as it once was.”

Joanna Tano, Head of Research, Europe

and confined large swathes of the population to their homes as they tried to curb the spread of COVID-19.

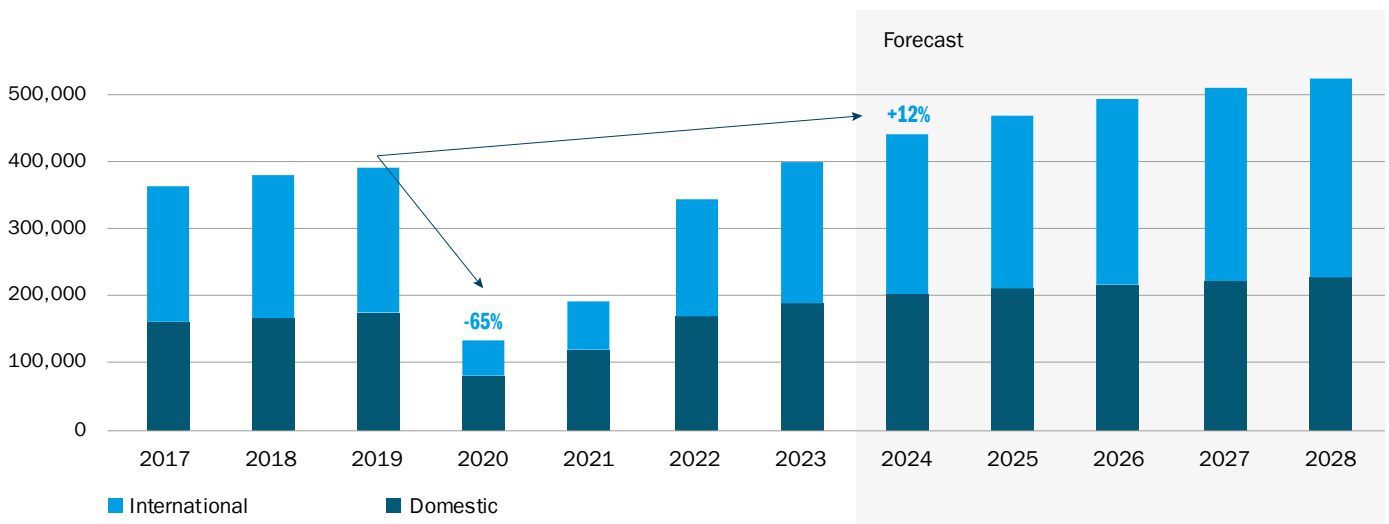
This was undeniably not good for physical retail. High streets suffered immensely as units were forced to close their doors for an undefined period, and footfall dwindled to zero. But as history seems to repeat itself, once economies opened again, travel rebounded with a speed some thought unimaginable and footfall numbers to Europe’s high streets followed suit and picked up. The number of nights spent in tourist accommodation by the end of 2023 are forecast to be back to pre-COVID levels and anticipated to be approximately 12% higher when comparing 2024 to 2019.

Domestic tourists initially led the recovery, but 2023 saw a tipping point as international tourists in overnight stays accounted for a higher proportion. This is a trend that we expect to see continue going forward. The change is boosted by strong inter-regional demand, travel postponed by the pandemic, US travellers benefitting from a strong dollar and the re-opening of China. The reversal of China’s zero-COVID policy saw Chinese tourists returning to European high streets sooner than expected boosting overall spend figures.



102 avenue des Champs-Élysées, Paris

Chart 1 - Overnight visits in paid accommodation in Europe (000s)



Source: Oxford Economics, November 2023

► Key takeaway:

Tourist numbers are on the rise and back to pre-pandemic levels with overnight stays in 2024 expected to be approximately 12% above 2019



Online and physical retail: working in tandem

Consumers accelerated their online spend during the COVID-19 pandemic, but there were already signs of rising online spend in the run up to the pandemic as structural global trends continued to play out.

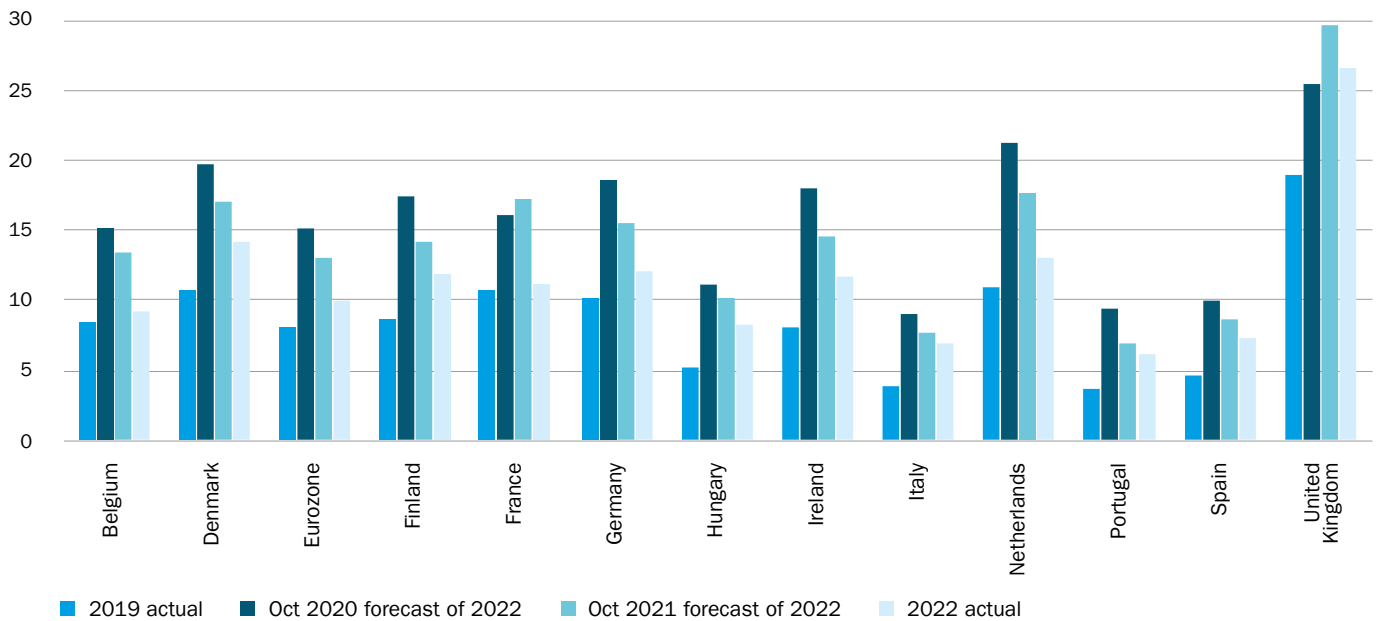
Along with the increase we saw a rising number of headlines on the disastrous and long-lasting impact that e-commerce would have on physical real estate and in particular, the retail sector and high streets. It is fair to say that the actual online numbers refute this, and forecasts were perhaps over ambitious in terms of the amount of spend that would shift permanently to online. Online shopping levels did indeed rise dramatically during the pandemic as the opportunity to visit physical stores was withdrawn, but since the re-opening of economies, online spend has seen volumes decline and whilst they are sitting marginally above pre-pandemic levels, they are generally still below the pandemic – see chart 2.

Online is no longer seen as the intense threat to physical stores as it once was. The lines are more blurred, and the high street is far from dead. Perhaps a better descriptor is alive and well. As economies reopened consumers voted with their feet, returning to physical stores, prompting a gradual but steady decline in online retail spending in most European countries. In addition, a growing number of pure play brands are seeing the intrinsic value in physical real estate and are opening stores, and this shift is likely to continue over the coming months and years. There is a greater understanding of multichannel retailing and the co-dependencies of online and store-based retailing at work today. Building an efficient



71-73 avenue des Champs-Elysées, Paris

Chart 2 - Percentage of online spend (2019 & 2022 actual versus 2022 forecasts from October 2020 and October 2021)



Source: Property Market Analysis, October 2023



multichannel operating model should be at the heart of any retailer's transition to the 'new normal' marketplace.

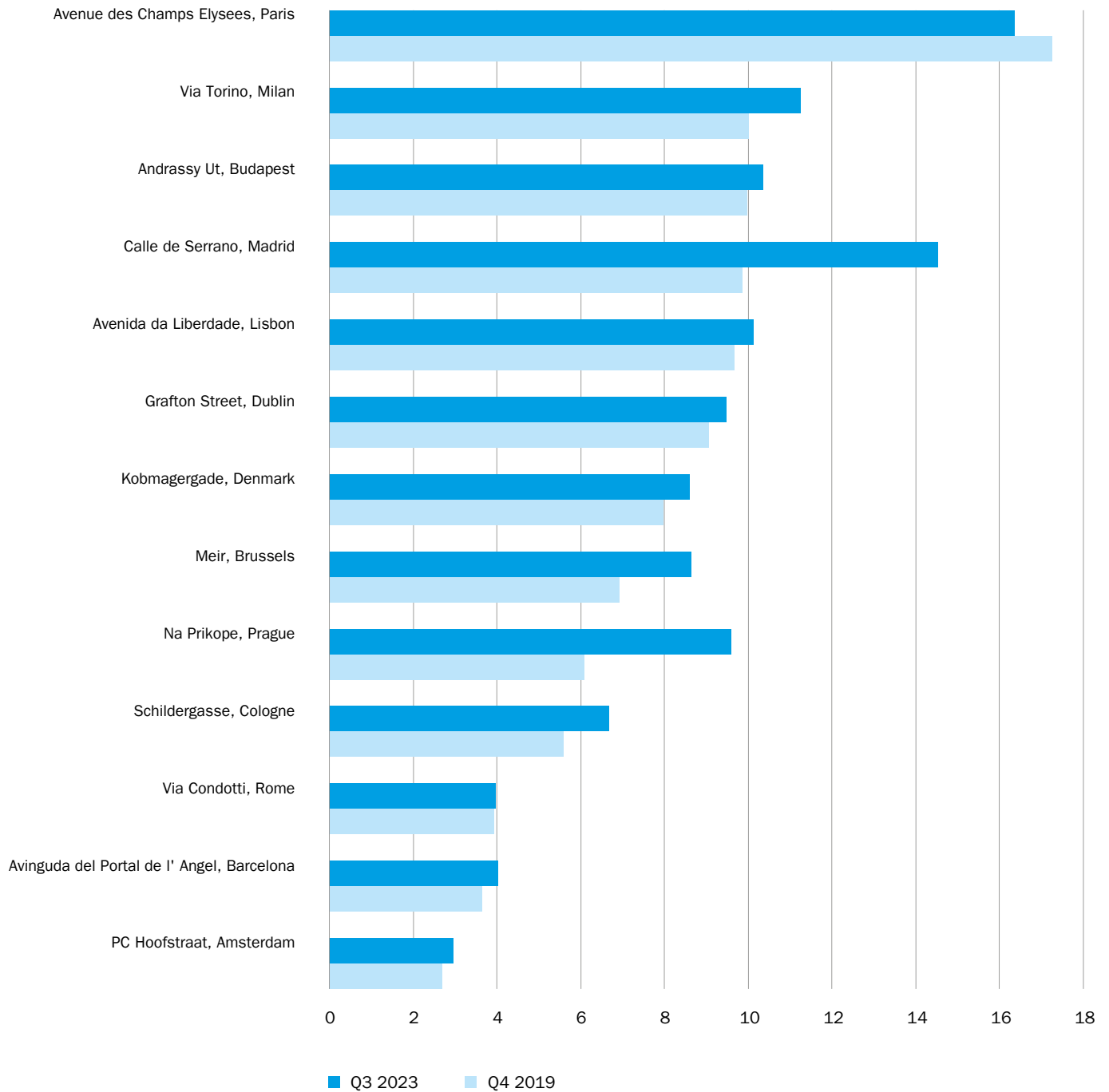
Bricks and mortar appear to drive higher conversion spending rates as brands tap into the experience offered by their in-store staff who can provide a more personal and customised service. Consumers can try before they buy, benefitting both the consumer and the retailer as it reduces the need for returns. As fulfilment costs rise, historically borne by the retailer, we are seeing more and more retailers introducing return fees for items being sent back to fulfilment centres whilst offering free returns to physical stores with the parallel aim of increasing footfall numbers and encouraging additional purchases whilst in store, driving higher turnover volumes. The importance of having a quality omni-channel approach where the online and physical worlds work in tandem to create the best consumer experience possible is clear.

And this is not just theory. Footfall numbers have increased over the past twelve months in all the top 205 European high street locations. And by the end of Q3 2023, footfall levels were back

to, or above, pre-COVID levels in a significant proportion of shopping streets in Europe's capital and strong Tier I cities – as illustrated in chart 3.

Public investment is also playing its part in reinvigorating city centres and high streets, making them more attractive and appealing and thus driving higher levels of footfall. Every location is different, and each has its own story to tell. And here we see more coordinated strategies involving multiple relevant stakeholders from local authorities, landlords, tenants, and developers working together to create long-lasting regeneration projects. One example is the "Re-enchanting" of the Champs Élysées in Paris. In January 2021 the mayor of Paris, Anne Hidalgo, announced a long-awaited development of the avenue and surrounding area, initially costing at €250 million and first unveiled by local community leaders and businesses in 2019. The plan includes transforming the 1.9-kilometre avenue into extraordinary gardens, reducing traffic, and utilising the pavements for more food and beverage offerings.

Chart 3 – Footfall figures pre versus post pandemic (in millions)



Source: CBRE Calibrate, December 2023

➤ Key takeaway:

Online is no longer seen as the intense threat to physical stores as it once was, the lines are more blurred

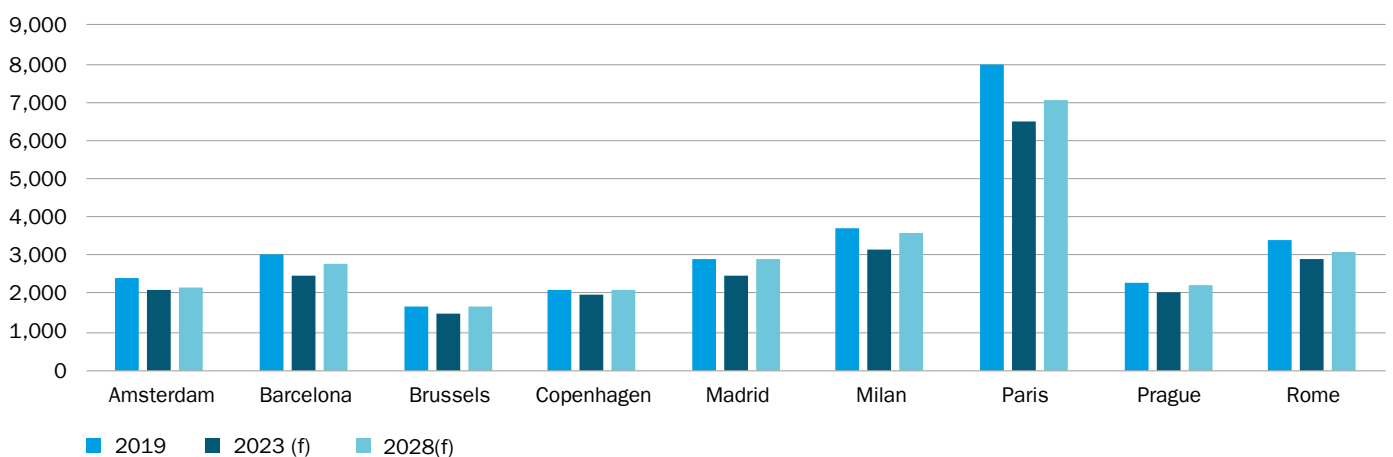
Drivers of retail real estate



Occupier market: rents have rebased enough to stimulate activity

Navigating the retail landscape is not without its challenges for occupiers. High street activity saw a revival as markets emerged from an almost standstill during the pandemic as consumers were allowed back onto high streets and into physical stores.

Chart 4 - Prime high street rents (€ per sq.m per year)



Source: Property Market Analysis, October 2023

48 rue François 1er, Paris



But inflation has eroded households' purchasing power and squeezed retailer margins. Having said that, those retailers that are well capitalised have been able to look beyond the current market conditions and are best placed to execute on strategic plans, even if they have been scaled back. Although, with margins squeezed as rapid inflation rises took their toll, and despite recent falls, retailers are conscious of where and how to deploy capital. There will be increased focus on store performance with retailers trying to maximise the value of their real estate assets.

The pandemic created opportunities for retailers – the availability of units increased, and rental levels declined. Some retailers took advantage of this and accelerated their strategies to right-size store networks, consolidating into fewer overall, but with bigger more strategically located flagship stores achieving a more sustainable rental base. This contrasted with having multiple small units, which could potentially dilute sales. Practically, these larger spaces allow brands to house their full product range whilst allowing customers to experience the brand before making any purchases. Premium and luxury brands were the most active occupiers in 2023 while innovative and mass-market brands continued to open state-of-the-art stores aimed at delivering an enhanced customer experience.

These post-pandemic opportunities are now almost absent across many primary European high street markets as supply comes under renewed downward pressure and demand for quality space on prime, high footfall streets picks up. Plus, there is increasing evidence that international brands in particular, are agreeing to longer

leases to secure the right unit on the right street. This squeezes their competition and facilitates them being able to strategically dominate certain locations. Rents have been pushed upwards in parallel with this trend. But it is not until mid-2024 that positive growth will likely be more evident with rents now having rebased to, arguably, more sustainable levels. Along with positive rental growth, retailers are positioning themselves for when consumer confidence returns and flows into retail sales. Some retailers have taken the opportunity to pivot towards onboarding technology to support changing consumer behaviour throughout the customer journey from beginning to end.

► Key takeaway:

Retailer strategies will continue to focus on securing the right space and delivering a customer experience

Investment market: high streets have repriced enough to offer select opportunities

The first nine months of 2023 recorded an investment volume of €120 billion across all sectors in Europe.

There has also been a rebalancing between sectors – retail was the second most traded sector in the year to September 2023 after offices with approximately €22.0 billion exchanging hands, equivalent to a 19% market share. Looking at the retail sector in more detail, high streets were the second most active segment across 2023 to Q3 whereby €5.0 billion was invested, equating to 23% of the retail volume. This was significantly ahead of retail warehouses accounting for a 19% share. Shopping centres were the most active sector in 2023 so far, not unsurprisingly given the typically larger lot sizes compared to high street shops and boosted by an active third quarter.

The hesitancy amongst investors seen during the second half of 2022 rolled over into 2023 but is expected to ease as 2024 unfolds as the market starts to unlock with inflation falling and greater clarity on the path of interest rates. While no country has been immune to the slowdown in investor activity it has

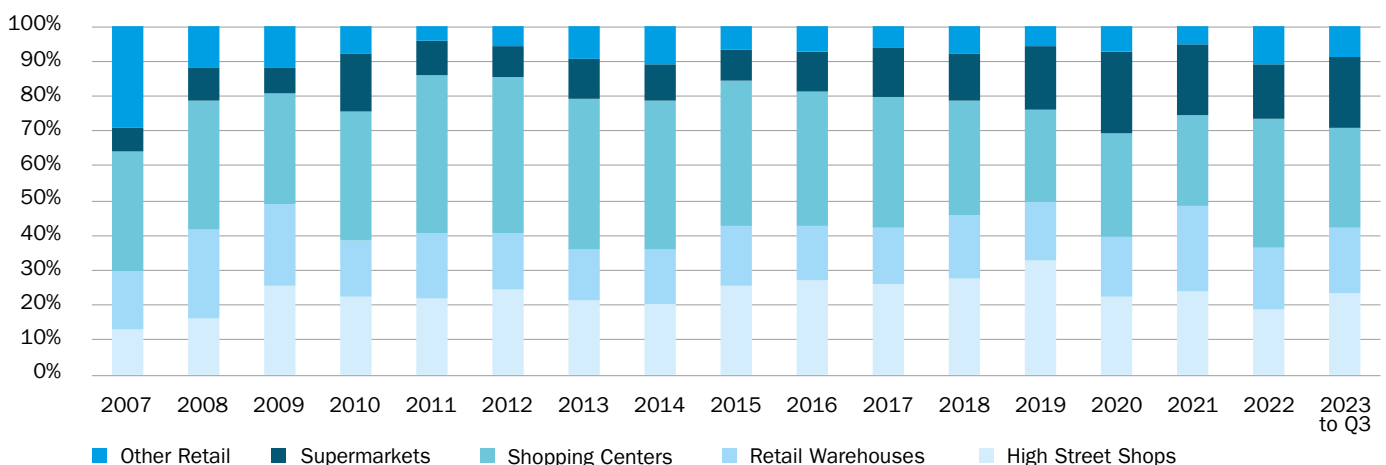
varied by country. Investors maintained confidence in the core European markets with Germany, the UK and France accounting for 78% of activity across the first nine months of 2023.

There is some dry powder waiting to be invested when signs of more stability emerge, and higher investment activity should follow relatively quickly after that, although the speed will be determined by how much stock is released to the market for sale. While some investors have paused acquisitions until there is more clarity, parts of the retail sector such as high streets have already seen significant repricing driven by structural trends that were in play well before the pandemic. And so, any outward movement in yields over the next three to six months will be less severe than for other sectors such as offices or logistics. This could be particularly evident in logistics where yields have compressed sharply over the last few years. It is fair to say that even though consumer confidence in many economies is at record lows, retail prices have corrected to such an extent that much of the bad news is already priced in. This in turn offers renewed opportunities to investors, some of whom believe that quality retail assets are now attractively priced and could offer solid returns, but stock selection is key – see chart 6.

Key takeaway:

Retail has already seen significant repricing with some good quality assets attractively priced, but stock selection is key

Chart 5 – European retail investment volumes by asset type



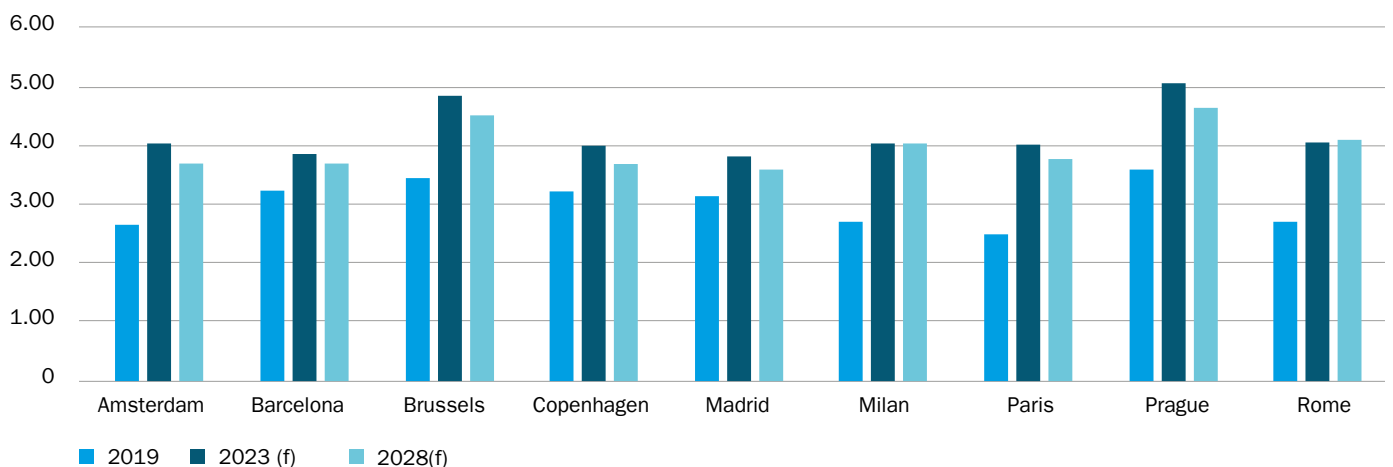
Source: Real Capital Analytics (MSCI), Q3 2023

“The occupiers’ market has been incredibly resilient this year, buoyed by the dynamism of major international brands, particularly in the sportswear and luxury sectors.”

Assia Amore,
European Fund Manager



Chart 6 - Prime high street yields (%)



Source: Property Market Analysis, October 2023



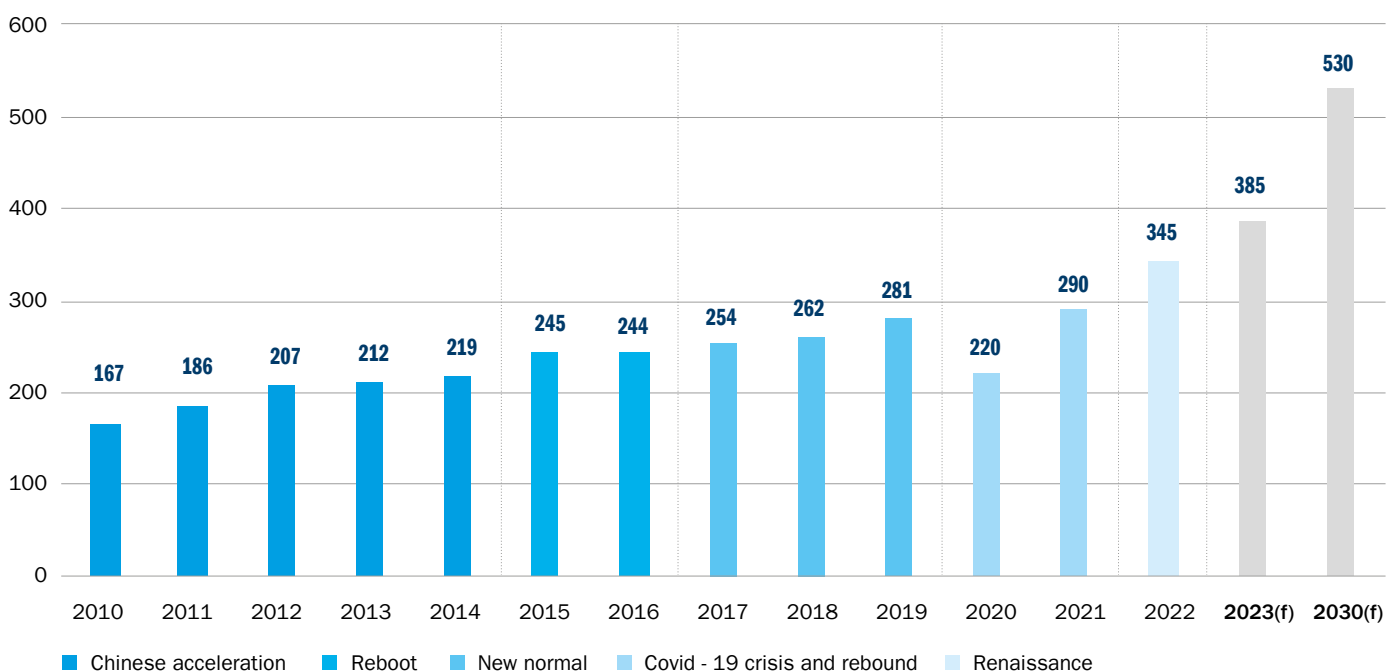
Spotlight on luxury



The Renaissance of the luxury retail sector

The luxury retail sector has shown its resilience and strength over the past few years. Retail generally slowed down in 2020, an inevitable consequence of the COVID-19 pandemic, as global economies were closed down, and consumers paused for thought.

Chart 7 - Global personal luxury goods market (€ billion)



Source: Source: Bain & Company, www.chanel.com; www.richemont.com; www.lvmh.fr; www.kering.com



But the subsequent rebound has been nothing short of outstanding with the global personal luxury goods market growing by 32% in 2021 year-on-year (Bain & Company). And this is despite current headwinds such as inflationary pressures and the wider economic slowdown, reflected in a general squeeze on household incomes and subdued GDP growth. The resilience of the global retail sector is shown in the subsequent 19% year-on-year increase that followed in 2022 with global turnover in the luxury goods market reaching €345 billion.

There are a several key reasons behind this trend. One is that the impact of financial crises on consumers with a higher-than-average purchasing power tends to be more limited as they have a greater financial buffer. A second is the growing consumer base expected to expand from around 400 million people in 2022 to 500 million by 2030. Thirdly, companies which trade in luxury goods have spent time and money successfully developing their omni-channel platforms in recent years which has helped them to extend their distribution and reach higher numbers of consumers globally, boosting sales.

The profitability of some retailers has been slightly eroded by the modernisation of their infrastructure network. Stores have been right-sized, raw material cost have increased, and employee wages risen. They have nonetheless benefited from price inflation, a proportion of which they have passed on to their consumers, buffering their margins and the overall increase in the level of sales. The leader of luxury goods, LVMH, recorded a 23% increase in turnover in 2022 year-on-year. Over the same period Richemont reported a 19% rise, while Kering and Chanel reported increases of 15% and 10% respectively.

The strong performance in 2022 suggests that growth should stay healthy for the personal luxury goods market in the medium term. According to Bain & Company, the

strength of the market's fundamentals, combined with the emergence of new sources of profit based on technology, should boost the luxury market turnover to between €530 – €570 billion by 2030. This compares to €345 billion in 2022 and represents an increase of at least 50%. That said, this growth will not come without challenges, as luxury companies, historically anchored in high-quality products and genuine human commitment, must now tackle new challenges that include consumers increasingly demanding sustainability considerations are factored in across the supply chain and technological advances.

Luxury brands are also looking beyond their 'traditional' products and are enhancing and expanding their brands to include hotels and hospitality, offering a lifestyle choice to their customers. The product allows the brand to get closer to their target customers whilst the expansion into hospitality helps them to elevate their brand. For example, LVMH's Cheval Blanc Hotels or Christian Louboutin whop opened their first hotel in 2023 in Melides, Alentejo in Portugal.

► Key takeaway:

The resilience of the global retail sector is shown in the 19% year-on-year increase in 2022 with global turnover in the luxury goods market reaching €345 billion.

Our vision

A Q&A with Ian Kelley, Head of France, Benelux & Southern Europe



Q The Columbia Threadneedle Real Estate team in Paris manages approximately €2 billion worth of high street retail across Europe, consisting of over 50 properties, how do you see the current environment for high street retail markets?

“On the macroeconomic side, the recovery of international tourism has been a great support. In most of the cities in which we are invested, tourism is back to pre-COVID levels. Also, in these European capitals, markets are deep with high income local consumers able to acquire luxury and premium products and ready to pay more for what they desire. To give some perspective, the global luxury market is forecast to reach over €530 billion by 2030 – 2.5 times its size in 2020.

On the tenant side, international brands are ready to pay significant levels of rent for quality stores with high visibility and footfall. Despite the COVID impact and the growing e-commerce market share, the best high street retail pitches are recording prime rental growth, this is notably the case in Paris, Milan, and Rome. Nowadays, international retailers are developing less but are more selective, seeking better and/or bigger stores in the best locations.”

Q What is your strategy in terms of asset value creation?

“The key elements of value creation in high street retail assets revolve around two main themes. Firstly, retailers are willing to pay significant rents for a visible location with high footfall. We work proactively with retail specialists to achieve tenant rotation that captures market rent increases. Often, retailers are also open to renegotiating the terms of their leases to retain their current locations, in the context of refurbishing their store for example.

Secondly, the size and format of the stores must be efficient and determine the sales potential of the brands. This can also include acquiring adjoining stores to enlarge the size if it's too small or dividing a store if it's too large. Thus, all our refurbishment projects have the objective to optimise store layout, maximise the sales area and adapt, when necessary, the unit to a wide range of retailers.”

Q What is your outlook for 2024?

“Repricing combined with the potential easing of financing conditions should see attractive investment opportunities come to the market in 2024. Thus, softer pricing combined with the macro trends supporting rental growth will make the timing right for both new investments and new leasing deals.”



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