Geomarketing

EUROPEAN RETAIL IN 2019

GfK study on key retail indicators: 2018 review and 2019 forecast

EDITORIAL

Dear reader,

Should I stay or should I go? The Brits answered this question originally posed by the Clash with a "go" in 2016. But almost three years after the referendum on the EU withdrawal, it turns out that there are various possibilities for what this "go" could mean. These include a so-called "no-deal Brexit," Theresa May's long-negotiated withdrawal agreement and a customs union.

Critics of Brexit are calling for another referendum on the final Brexit deal, with the explicit aim of having the public vote again on whether to stay in the EU.

The political uncertainty surrounding this historical event makes it impossible at the time of the editorial deadline to predict whether and when the United Kingdom will leave the EU. But there is no doubt that the outcome of the Brexit drama will have a major impact on the development of retail in the United Kingdom. However, in our special chapter on the country, we evaluate other trends such as the so-called "trading-up" phenomenon currently in evidence.

Our study offers a detailed assessment of the technical consumer goods segment and reveals how "click-and-mortar" retailers are catching up with online-only retailers in Europe.

From a pan-European perspective, the study also discusses key retail benchmarks such as retail turnover, sales area provision and the distribution of purchasing power. Whether you're an investor, project developer or retailer, our insights offer valuable support for your decision-making.

Kind regards,

Dr. Johannes Schamel
Study lead
Geomarketing, GfK

Impressum

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Contents

PURCHASING POWER IN 2018

More robust purchasing power gains* than in previous years

+3.0%

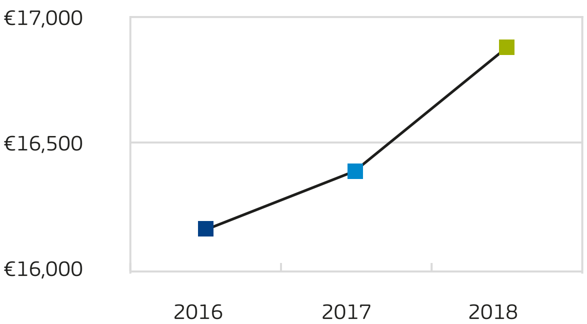
more per capita purchasing power in the EU-28

For more than 30 years, the key goal of the European Union's cohesion policy has been the dismantling of regional and international economic disparities among the member states. The EU is closer than ever to achieving this goal with respect to per capita purchasing power, at least at the national level.

The ten EU nations with the highest per capita purchasing power gains this past year all have below-average purchasing power and were admitted into the EU as part of or after the eastward enlargement. Increasingly tight job markets in these nations have led to sizeable pay increases. For example, citizens of the growth forerunners Latvia and the Czech Republic have €8,030 (+10.3%) and €9,492 (+9.3%) at their annual disposal, respectively. This moves them closer to the European average of €16,878 (+3.0%), although continued progression in that direction is likely to require the ongoing support of the European Union.

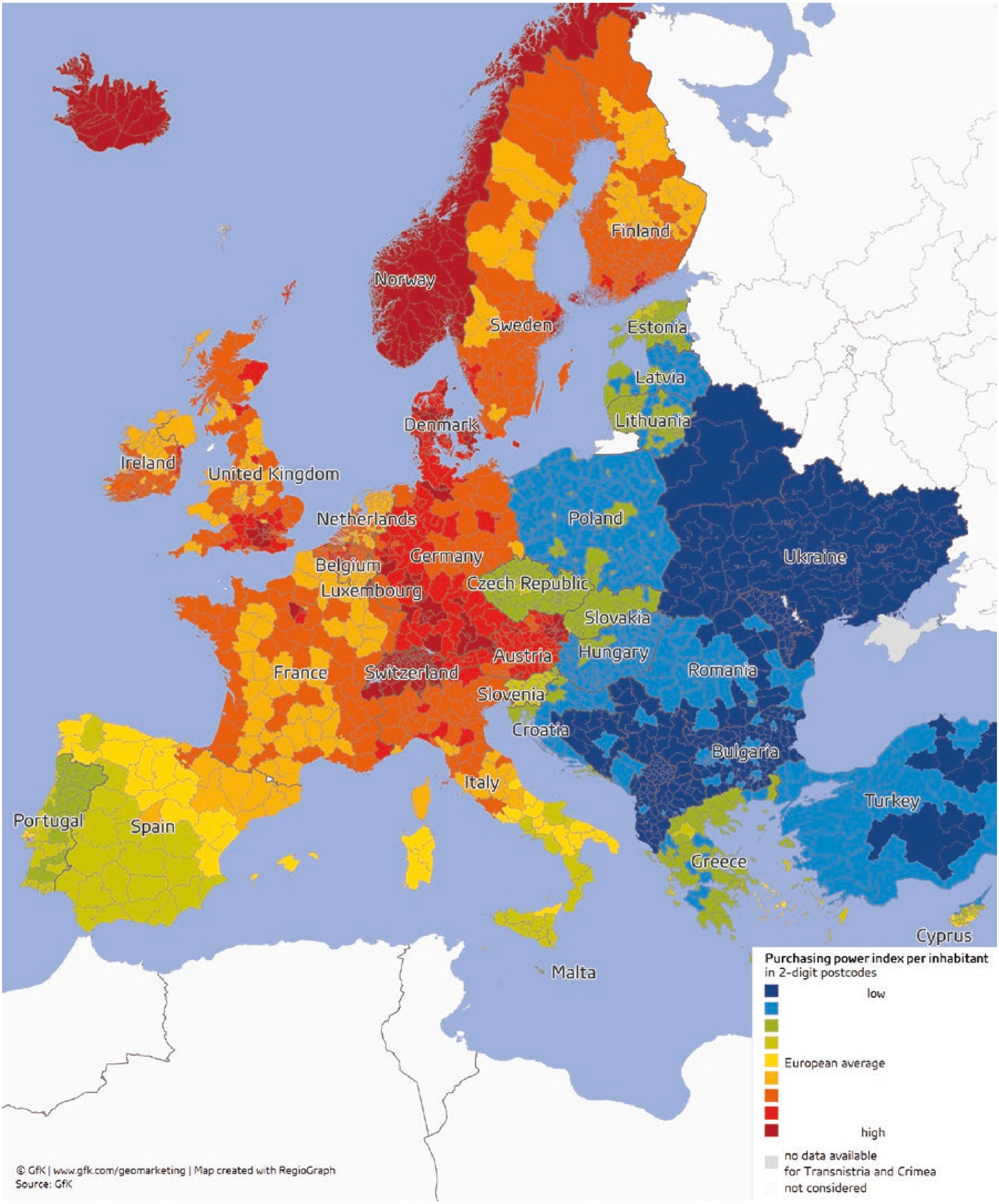
Poland also achieved substantial purchasing power gains in 2018 (+7.7%), but the gap between wealthy and poor regions is noticeably more pronounced. Among Poland's 380 districts, inhabitants of the least affluent district Przysuski (€4,295) have less than one-third of the money available to inhabitants of the wealthiest district Warszawa (€13,535).

Per capita purchasing power (EU-28)



*Purchasing power corresponds to the population's disposable income, including government subsidies such as pension payments, unemployment assistance and child benefit. The population uses its purchasing power to cover expenses related to food, accommodation, services, vacations, insurance, private pension plans and retail purchases. Purchasing power is a prognosis and is provided in nominal euro values. Comparison figures from previous years are based on revised values.

GfK Purchasing Power Europe, 2018



BRICK-AND-MORTAR RETAIL TURNOVER IN 2018

Minimal gains in real terms among large western European markets

The Italian government coalition consisting of the Five Star Movement and Lega Nord issued a decree for the introduction of a poverty relief scheme known as “citizens’ income” at the beginning of 2019. This was preceded by an at-times intense dispute with Brussels, which was concerned about negative consequences to Italy’s creditworthiness stemming from its large public debt and credit-financed reform.

Even so, the reform in question should at least have a positive impact on retail over the short term. This silver lining is urgently needed, because Italy’s brick-and-mortar retail underwent a nominal turnover decline of -0.2%* in 2018.

The other large western European markets of Spain, the United Kingdom and Germany experienced only nominal turnover gains in brick-and-mortar retail. Only in France with growth of 3.6% were these gains high enough to result in notable turnover increases in real terms. For the EU-28 as a whole, the nominal turnover growth of +1.9% hovers around the level of inflation.

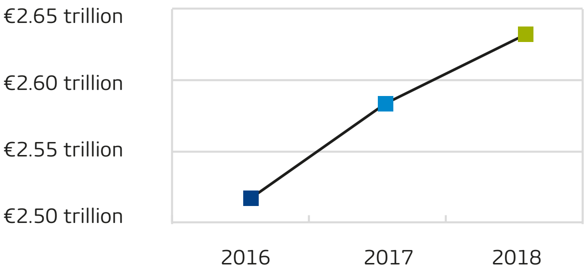
*All rates are based on nominal values, meaning they have not been adjusted for inflation.

Eastern Europe presents a different picture. Despite substantially declining populations, both Bulgaria (+7.7%) and Romania (+7.1%) continue to be the European forerunners along with the Czech Republic when it comes to growth rates in brick-and-mortar retail. Hungary (+5.3%) and Poland (+5.9%) were not able to achieve last year’s growth rates, but this is partly due to exchange rate effects.

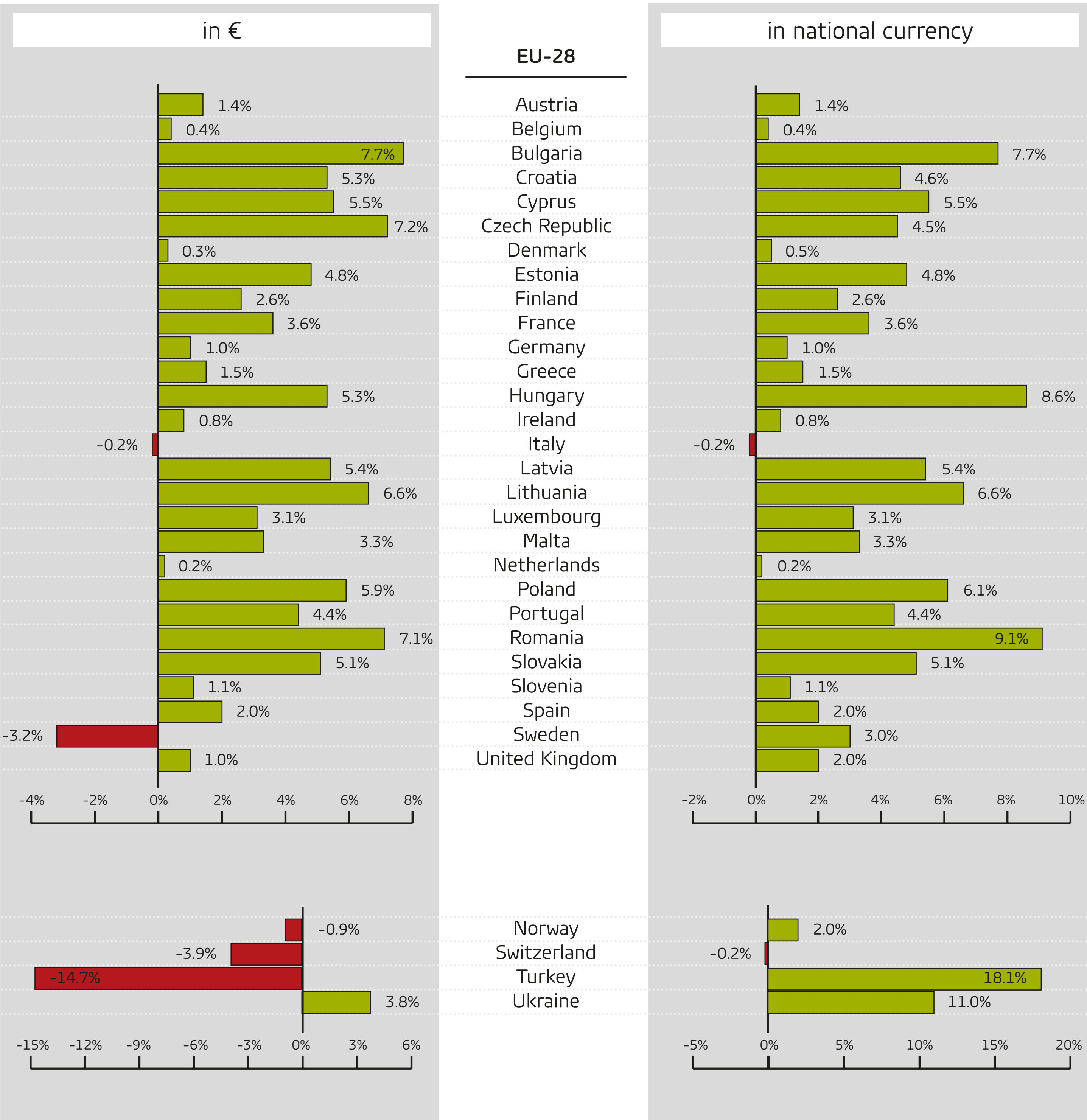
+1.9%

brick-and-mortar turnover in the EU-28

Brick-and-mortar retail turnover (EU-28)



2018 turnover growth in brick-and-mortar retail as a %



source: GfK

PROGNOSIS FOR BRICK-AND-MORTAR RETAIL TURNOVER IN 2019

Online retail dampens growth prospects for brick-and-mortar retail

+2.0%

forecasted brick-and-mortar turnover growth in the EU-27 (excludes the UK)

The majority of European consumers are currently subjected to opposing forces. On the one hand, this consists of uncertainty over Brexit, trade conflicts and weaker growth prospects in important export markets such as China. But on the other hand, consumers have a more robust labor market, higher wage increases and moderate prices for crude oil. This means that the purchasing power gains in real terms enjoyed by citizens in the majority of EU countries tend to go toward savings rather than retail purchases given the dampened consumer climate.

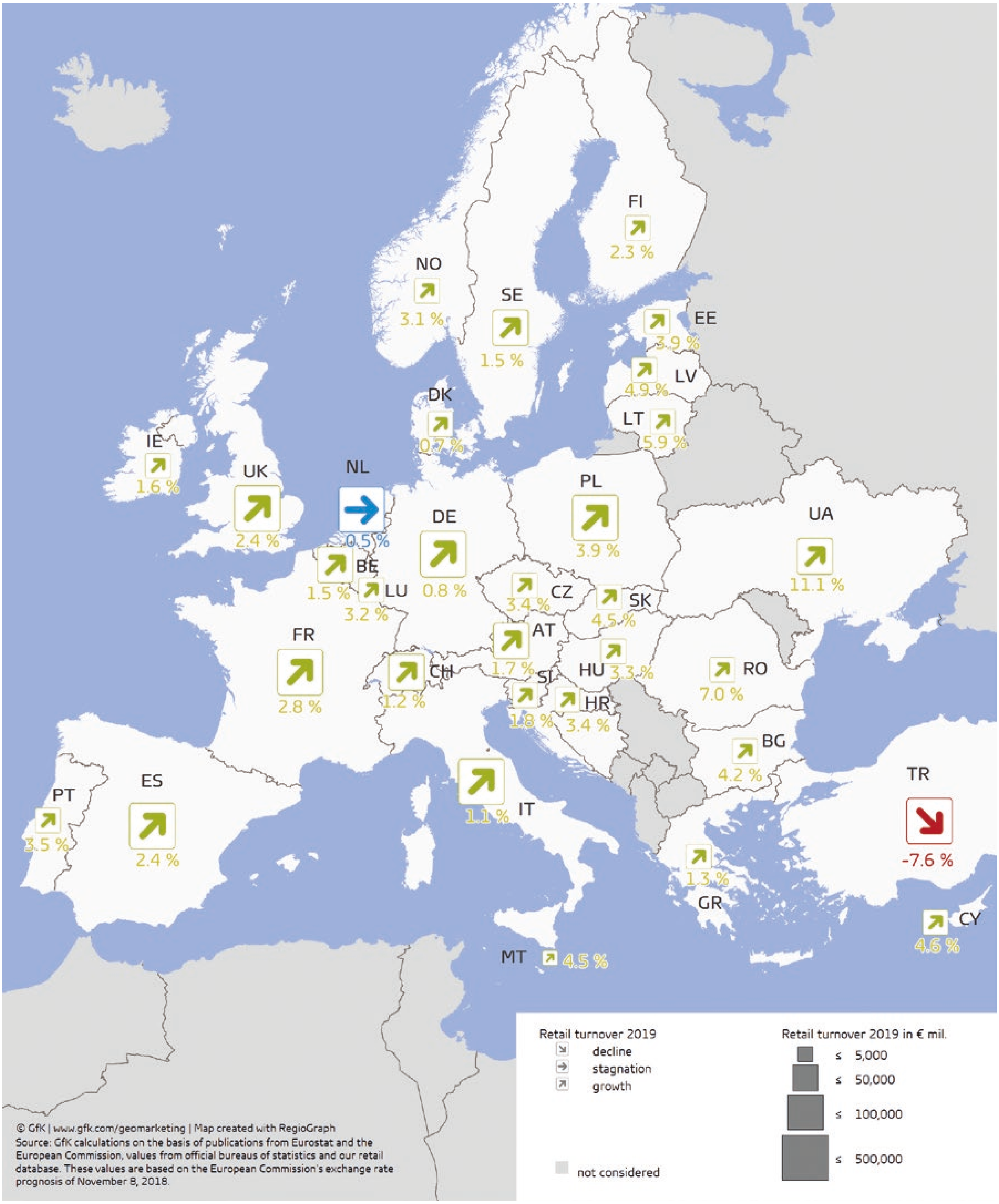
In light of the continued dynamic growth in online retail, we anticipate nominal turnover growth of +2.0% for the EU-27 nations, a figure that is only slightly above the rate of inflation.

By contrast, we expect positive growth for Spain: At the beginning of 2019, the minimum wage was increased by +22%, which will directly and indirectly benefit 2.5 million people according to the Spanish government. With this in mind, we predict nominal turnover growth of +2.4% for the Iberian nation. Given the expected inflation rate of +1.2%, this should equate to a turnover increase in real terms for brick-and-mortar retail.

France also experienced a meaningful development at the beginning of the year. The tax system was finally changed from an annual collection for the expired calendar year to a monthly deduction at source taken from income. This could negatively affect consumer mood. But due to a fiscal stimulus effect coming into play in 2019, we expect that turnover in brick-and-mortar retail will increase by +2.8% despite the growing savings trend.

Romania (+7.0%) and Lithuania (+5.9%) are anticipated to have the highest growth rates among the EU nations. In the Baltic state, rising incomes and tax relief in the current year are leading to strong growth in disposable income.

Forecasted brick-and-mortar retail turnover for 2019



RETAIL SHARE OF PRIVATE CONSUMPTION IN 2018

Revised numbers show declining share in 2018

Metropolises and densely populated areas offer substantial benefits to many companies delivering knowledge-intensive services. Easy access to universities, institutions and customers facilitates the transmission of tacit knowledge. Specialized labor markets cannot simply be replicated in rural regions without further measures. As a result, urban economies in many European nations have grown in significance compared to rural areas, which has consequences for intraregional migration.

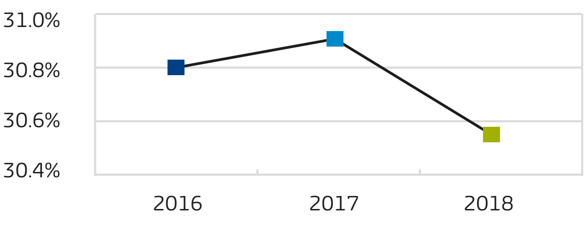
This influx into regions with already tight housing markets as well as rental and real estate prices that have grown in past years generally require consumers to spend a higher share of their income on housing. Along with other factors, this development could be a causative force behind the long-term trend toward a declining share of brick-and-mortar retail turnover in overall consumer expenditures. In 2018, this share sank by 0.4% to 30.5%.

Particularly in the Scandinavian countries as well as in Austria, Germany and Switzerland, brick-and-mortar retail has declined in relative importance in recent years with respect to overall consumer expenditures. By contrast, brick-and-mortar retail turnover generally experienced more robust growth in Portugal and Hungary than was the case for total consumer expenditures. This also led to the current situation in Hungary, where inhabitants devote more than half of their consumer expenditures to brick-and-mortar retail purchases (50.3%), which is the highest figure in the European Union. The comparatively weak status of online retail could be playing a role with respect to this phenomenon.

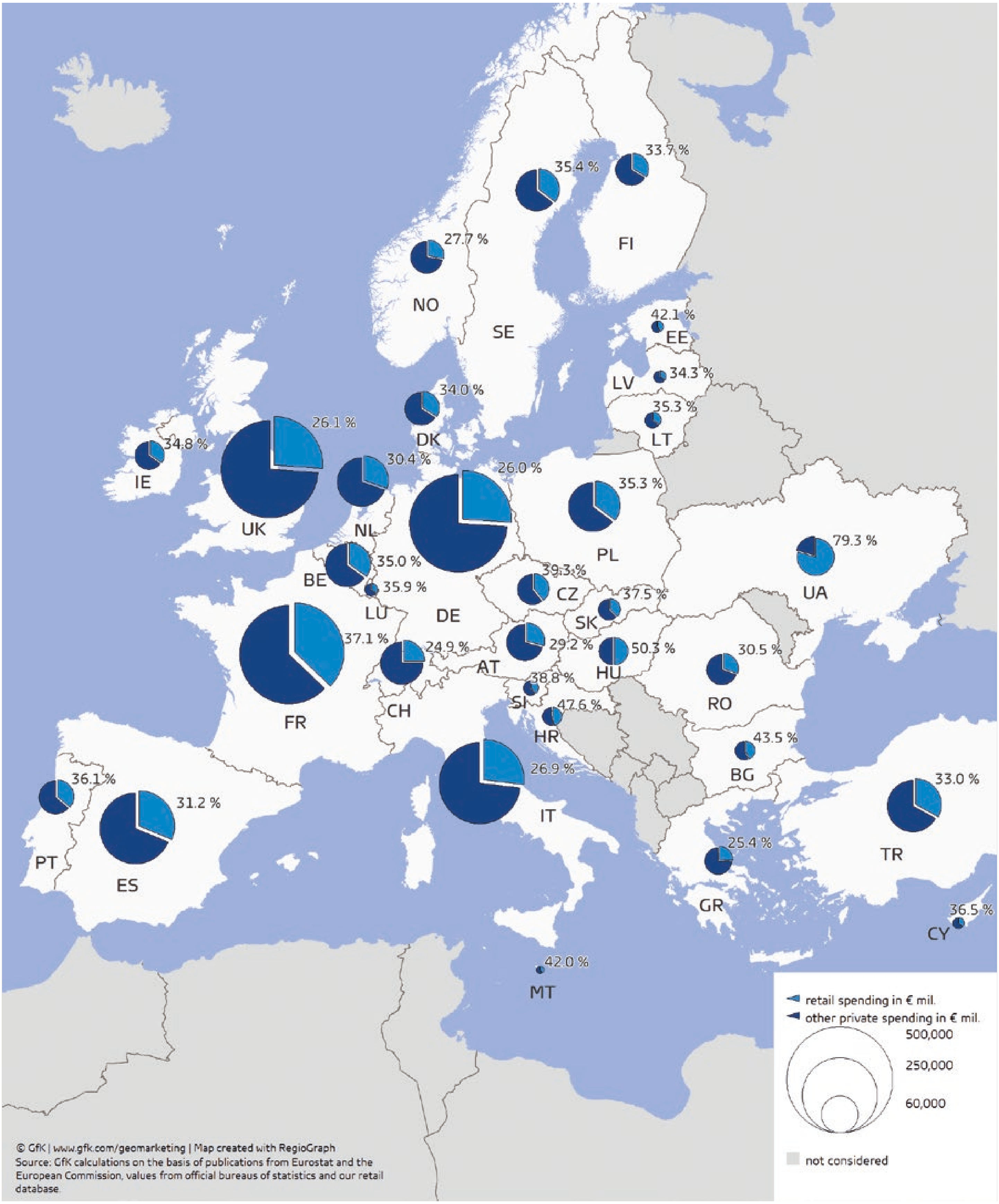
30.5%

retail share of private consumption (EU-28)

Retail share of private consumption as a % (EU-28)



Retail share of private consumption in 2018



Source: GfK calculations on the basis of publications from Eurostat and the European Commission, values from official bureaus of statistics and our retail database.

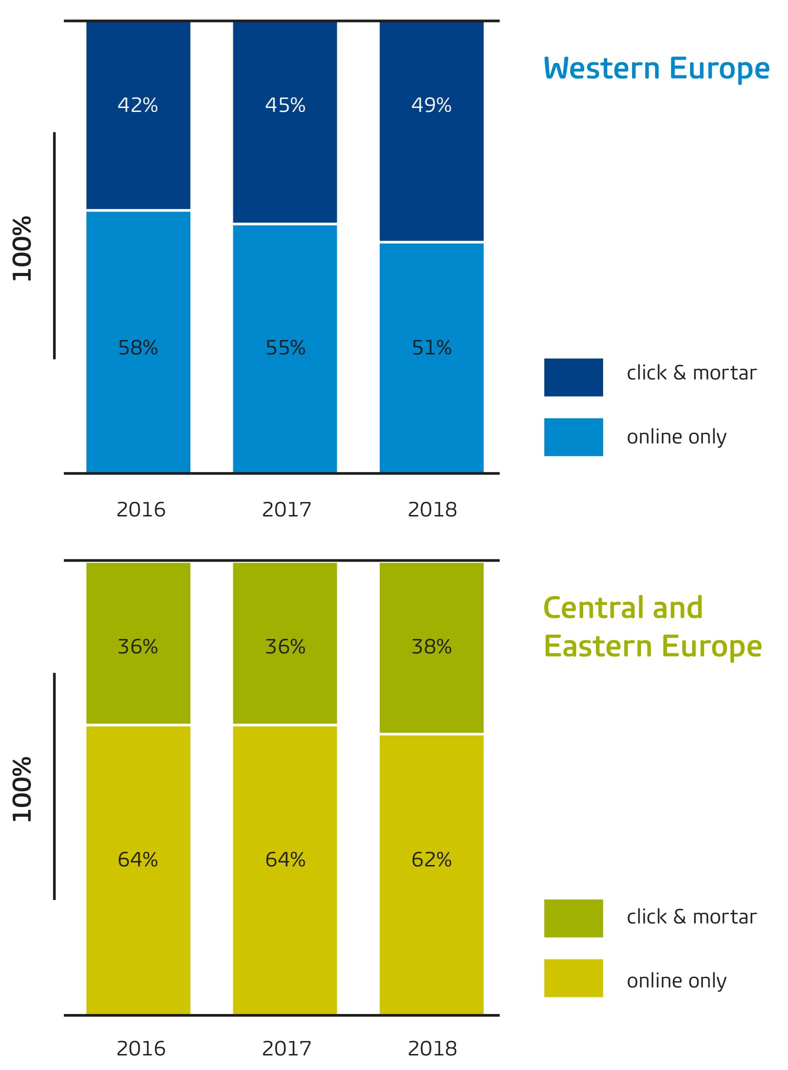
RETAIL OF TECHNICAL CONSUMER GOODS

Multi-channel retailers catching up with online-only retailers

According to the press, Amazon secured a property in London in February in order to open the first Amazon Go shop on European soil. Cameras and sensors capture consumers' every move in these cash register-free stores and automatically monitor the goods that consumers put into their shopping baskets. This allows customers to exit the business without having to scan their chosen products. Amazon is also experimenting with digital enhancements to traditional brick-and-mortar concepts. For example, Amazon's 4-star shop that opened in New York in the fall of 2018 contains only products that were given at least a four-star rating by online customers.

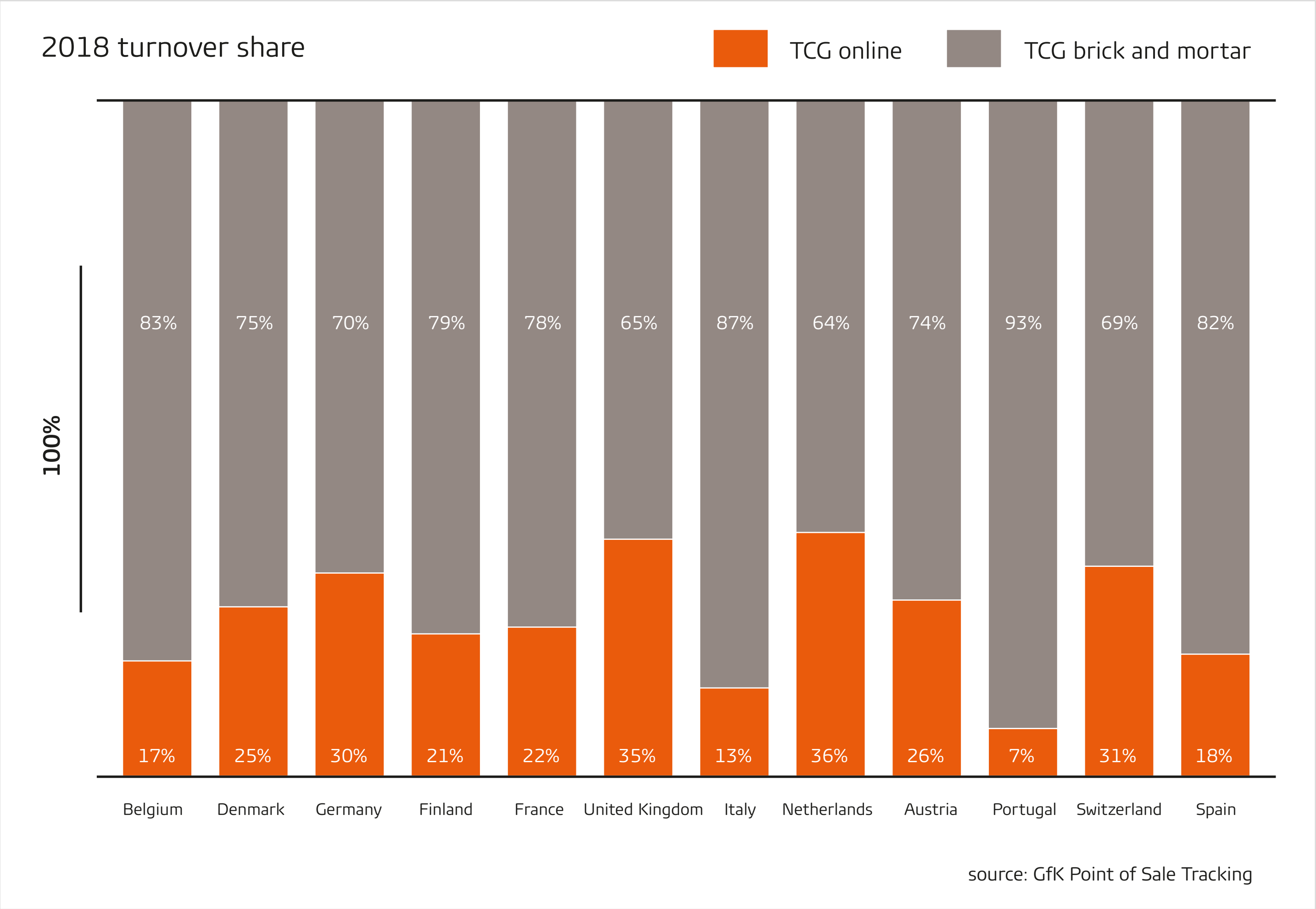
Amazon's strategic decision to further develop itself into an omni-channel player underscores the evolutionary path already followed many times by former brick-and-mortar retailers and that seems to have paid off. In 2018, online shops of traditional brick-and-mortar retailers in the technical consumer goods (TCG) segment in Western Europe* had turnover growth of +24%, which is six times the growth experienced by online-only retailers (+4%), as demonstrated by GfK Point of Sale Tracking data. The digital channel alone of multi-channel businesses (click & mortar) has a 49% share of the total online turnover in this segment. In Central and Eastern Europe**, online-only retailers have a market share of 62% , out-performing the online turnover of multi-channel companies (38%), although the latter had higher growth rates in 2018 (+17% to +27%).

Share of online turnover by sales channel



source: GfK Point of Sale Tracking

*includes the states of Austria, Belgium, Denmark, Finland, France, Germany, United Kingdom, Greece, Ireland, Italy, Luxembourg, Netherlands, Norway, Portugal, Spain, Sweden and Switzerland
**includes the states of Croatia, Czech Republic, Hungary, Poland, Romania, Serbia, Slovakia and Slovenia



But the boundary between online and brick-and-mortar retail is blurring noticeably due to the smartphone. Twenty-eight percent of online customers indicated that they made at least one purchase from their smartphones from the online store of a competitor while they were physically present in a brick-and-mortar retail business (source: GfK Consumer Life Study 2018).

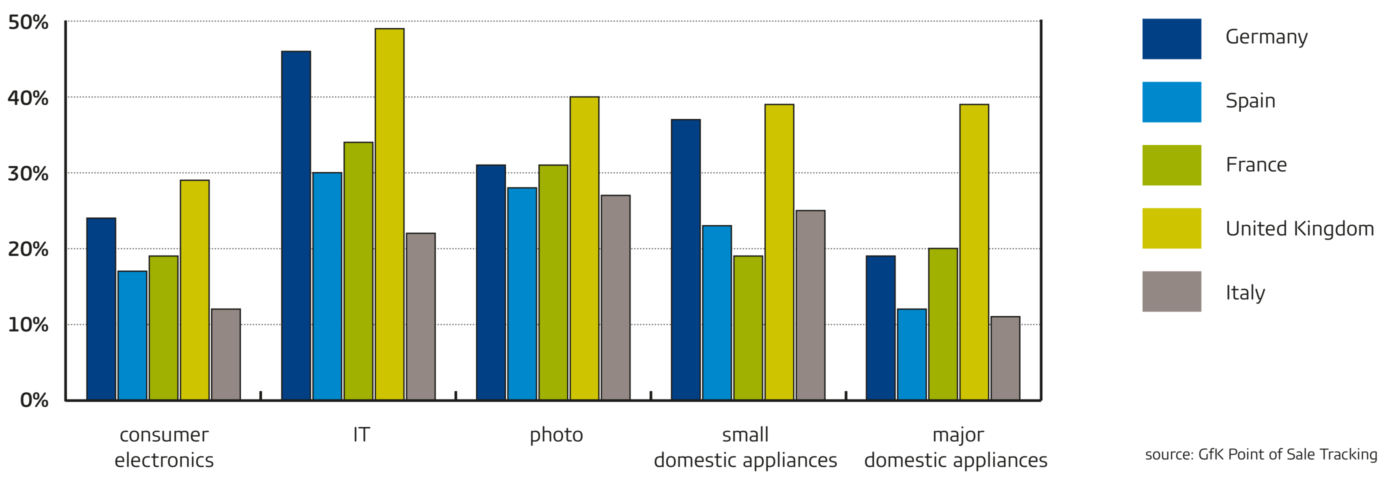
Taking into the account the individual components of omni-channel trade, the technical consumer goods segment in Western Europe unsurprisingly increased its market share from 19% in 2014 to 26% in 2018, which was to the benefit of online turnover. There are enormous differences among the considered countries in this regard. The Dutch (36%) and the Brits (35%) spent more than one-third of their expenditures in the online TCG segment, while Italians spent only 13% and the Portuguese just 7%.

Country-specific characteristics are also apparent with regard to individual product groups. For example, the United Kingdom's share of online turnover for electrical household appliances is 39%, which is higher than the total share of technical consumer goods as a whole. By contrast, this value is below the respective national average for technical consumer goods in the other four large European markets of Spain (12%), Italy (11%), Germany (19%) and France (20%). Compared to the United Kingdom, built-in appliances play a significantly larger role in the aforementioned countries, with the result that assembly and installation services boost brick-and-mortar retail in these nations.

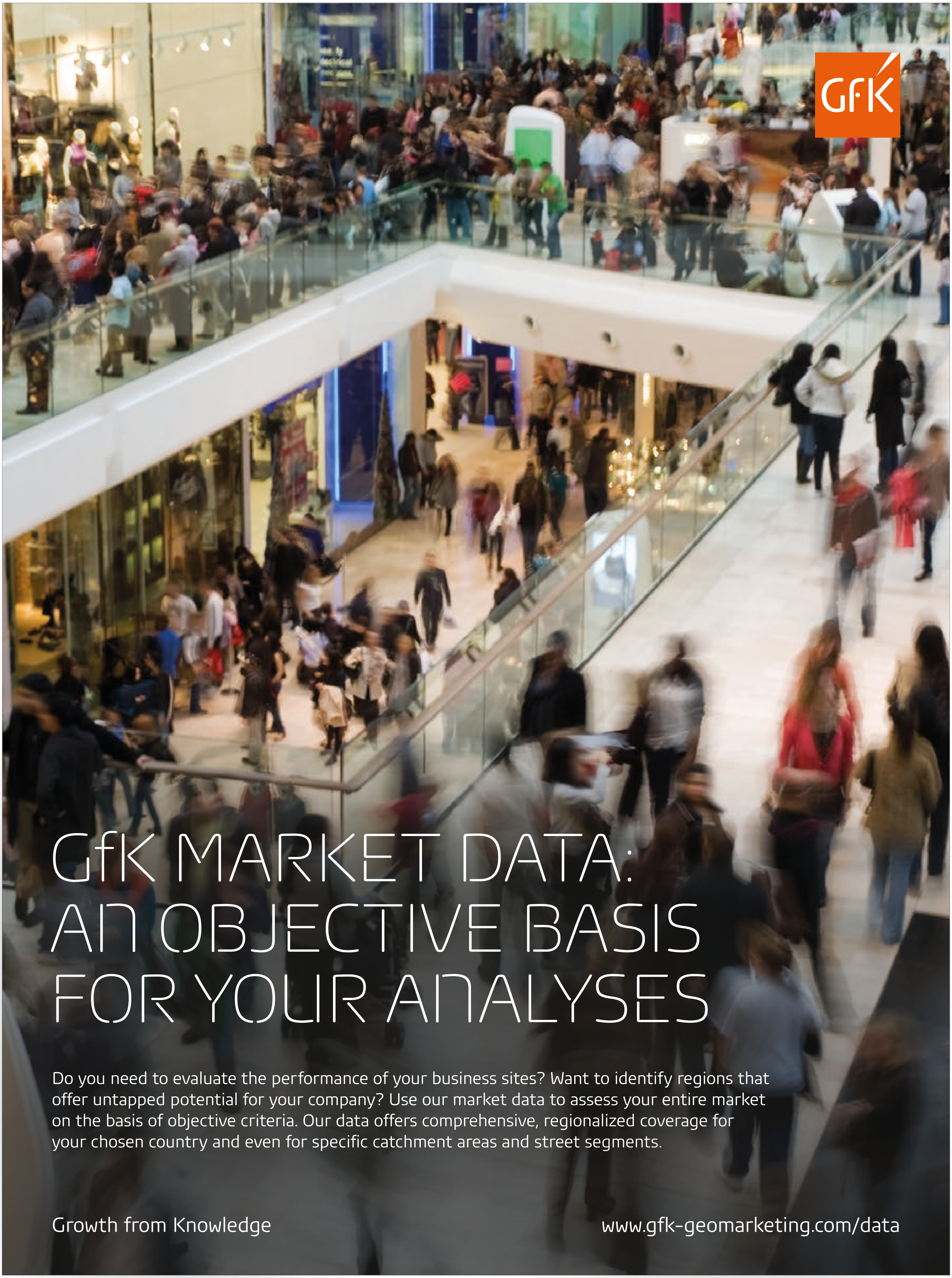
39%

online turnover share for electrical household appliances in the UK

Online turnover share of total 2018 turnover



source: GfK Point of Sale Tracking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CONSUMER PRICE TRENDS FROM 2018 TO 2019

Moderate inflation despite zero-rate policy

Prices in the EU continue to develop moderately. While the inflation rate of 1.9% in 2018 is the highest since 2012, it is still just below the 2.0% goal considered ideal for the economy.

Within the EU, consumers in the Baltic states (+2.5% to +3.4%) and especially in Romania (+4.1%) and Hungary (+2.9%) had to reach deeper into their pockets for purchases in 2018. Among the most populous nations, the United Kingdom continued to have a comparatively high inflation rate of +2.5% in 2018, followed by France (+2.1%) and Germany (+1.9%). Similar to the previous year, crisis-ridden Italy experienced an inflation rate of +1.2% in 2018.

But sinking energy prices beginning already at the end of 2018 suggest that the EU's inflation rate will fall again. Along with continuing trade disputes with the USA, the weakening European economy at the beginning of 2019 is dampening the mood of economists. As a result, a lower 2019 inflation rate of 1.6 percent is expected for the European Union. This translates once again to a moderate difference between nominal turnover and turnover in real terms for European retail. The European Central Bank reacted to this development by announcing that it wants to increase the sustained record low base interest rate of 0% no earlier than 2020.

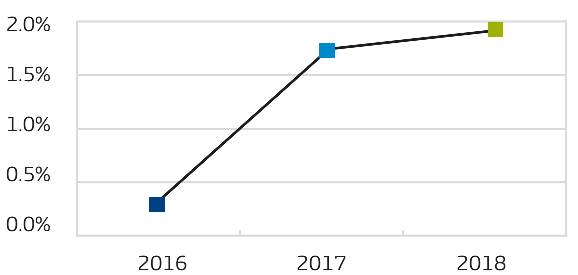
+1.6%

expected inflation in 2019 (EU-27)

Significantly lower inflation rates compared to the previous year are primarily expected for the largest three economies in the European Union. While an increase of +1.4% is anticipated for France and Germany in 2019, a price rise of +1.8% is expected for the United Kingdom.

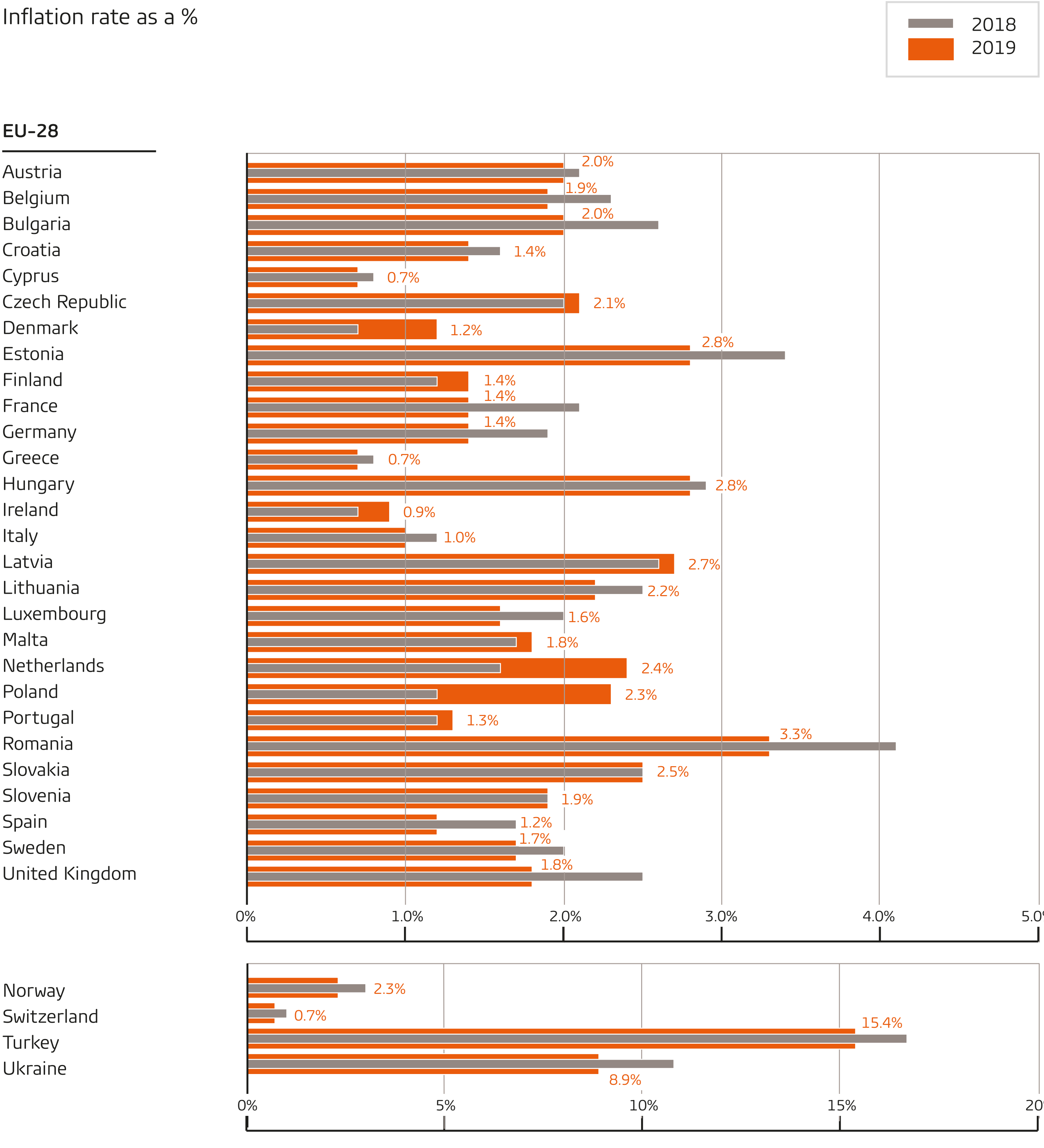
Beyond the EU, Turkey's 2018 inflation rate of +16.7% attracted attention. The unchecked plunge in value of the lira led to a 15-year high in the inflation rate in the fall of 2018. Despite the increase in the base interest rate by Turkey's Central Bank, which helped to lower inflation, high price increases are also anticipated for Turkey in 2019.

Inflation rate* as a % (EU-28)



* To ensure comparability between the countries under review, these figures refer to general inflation (including services, transport, etc.).

Inflation rate as a %



source: European Commission and International Monetary Fund

SALES AREA PROVISION IN 2018

Population growth and sales area development maintain a balance

For a long time, Europe-wide growth in sales area provision was a given. It now seems that an apex has been reached. While the total sales area provision for all considered countries also increased in 2018, this happened at a significantly lower level than in previous years. In 2018, the EU-wide* growth in sales area provision was counterbalanced by population growth. As such, the per capita sales area provision remains at the previous year's value of 1.13m².

This is due to multiple factors. The number of new retail projects declined again in 2018. Even in countries with substantial development in recent years, the focus has shifted to optimizations and revitalizations of existing retail real estate. The increasing transformation of classic shopping real estate and locations into so-called lifestyle hubs is also playing a role. Alongside dedicated retail space, more room is being devoted to gastronomy, entertainment, education and health offerings in European cites and shopping centers.

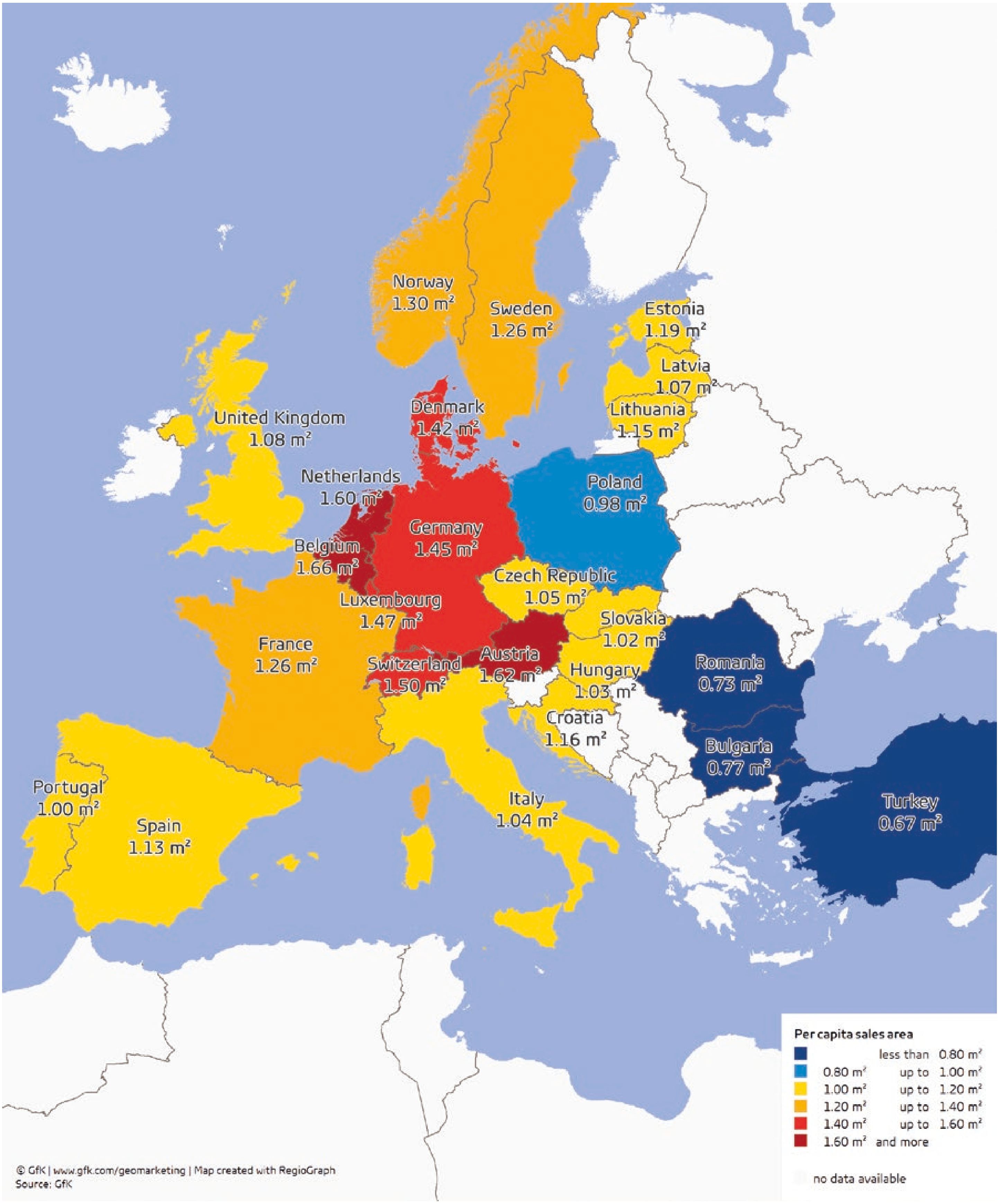
*excludes consideration of the countries of Cyprus, Finland, Greece, Ireland, Malta and Slovenia

The competition for the approval of European consumers has left some notable victims from the supply side in its wake. Amidst the uncertainties in the British market resulting from the Brexit negotiations, some well-known retailers such as HMV announced closures in 2018, generating headlines. Britain's per capita sales area provision decreased from 1.09m² to 1.08m². As seen through the branch network optimizations by Marks & Spencer, Debenhams and Tesco, new usages are increasingly sought after for many retail spaces in 2019/2020, particularly in areas away from the top locations.

Among the top-three countries in terms of per capita sales area provision are the Benelux nations of Belgium (1.66m²) and the Netherlands (1.60m²) as well as Austria (1.62m²), although the latter was the only country in 2018 among those considered for which total sales area declined (-2.0%).

In terms of 2018 sales area provision, Croatia (1.16m² per capita; +2.8%) as well as Bulgaria (0.77m² per capita; +1.7%) and Romania (0.73m² per capita; +1.7%) were able to gain ground, although the two latter continue to be at the bottom of the EU rankings.

Sales area provision in 2018



SALES AREA PRODUCTIVITY IN 2018

Even in the age of omni-channel retail in which the boundaries between online and brick-and-mortar retail are increasingly fluid, sales area productivity (gross turnover per m² of sales area) remains an important benchmark for evaluating the performance of retail locations and comparing the retail scene from country to country.

While online retail has been the clear winner in recent years, brick-and-mortar retail is by no means static. Customers increasingly expect brick-and-mortar retail to enhance its offering with some elements of online retail. The same is true for online retail, but in reverse. From both the perspective of retail and landlords, the sales area productivity of a given location continues to be a decisive benchmark for estimating turnover potential on the one hand and leasing options on the other.

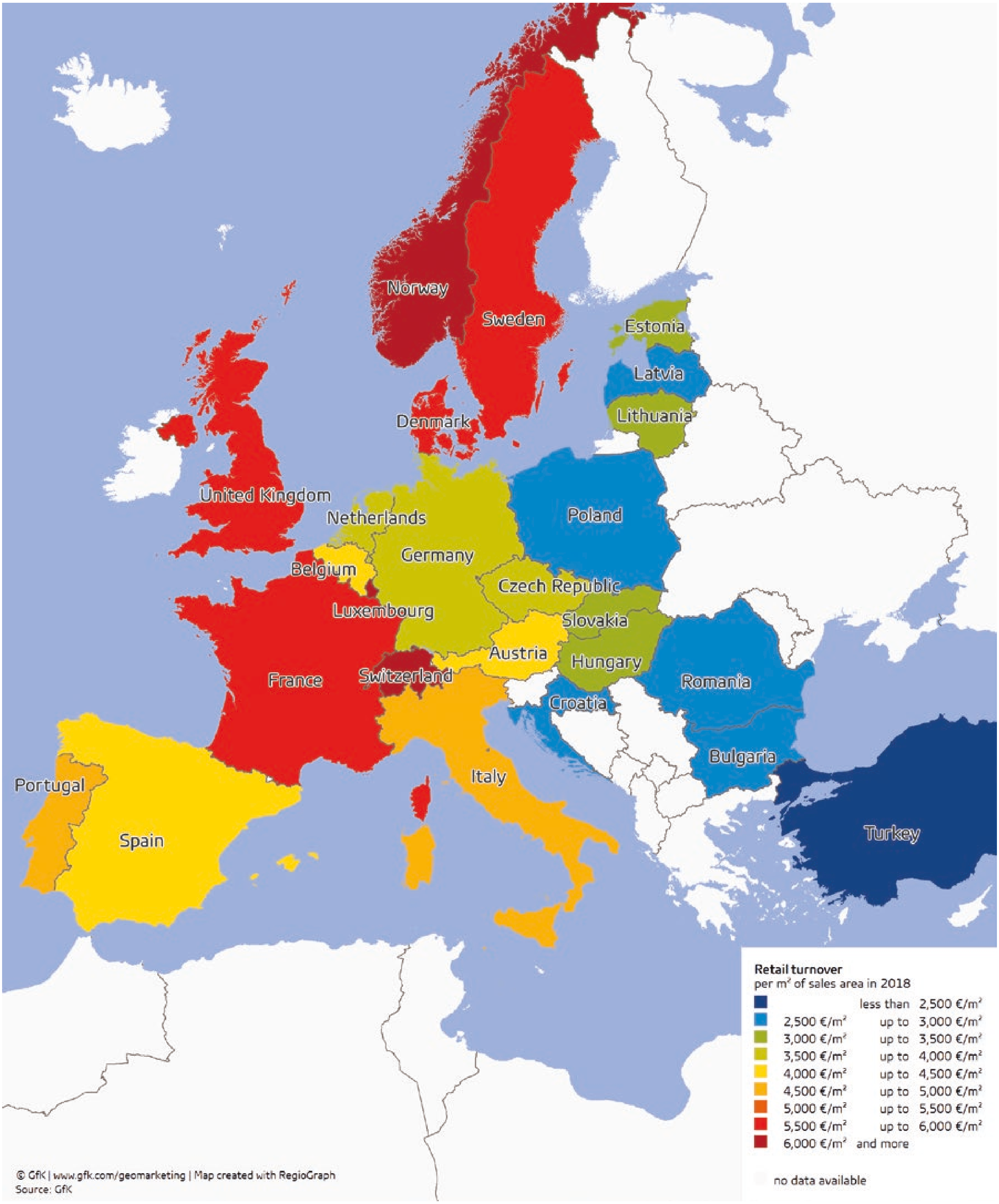
Europe-wide, there was no change to the top three nations compared to the previous year with respect to sales area productivity. The unchallenged forerunner continues to be Luxembourg (approximately €7,250/m²), which even experienced a slight increase (+1.40%) in sales area productivity in 2018. Second and third place are occupied by Norway (approximately €6,430/m²) and Switzerland (approximately €6,220/m²) respectively.

Thanks to strong turnover growth, sales area productivity in the Czech Republic grew substantially (approximately €3,510/m²), pulling just ahead of Germany (approximately €3,500/m²). Austria also enjoyed a rise in sales area productivity to approximately €4,090/m², which is a result of higher turnover and declining sales area.

As is the case for sales area provision, there continues to be a large range in sales area productivity values among the considered European countries. Turnover is significantly lower among retailers the further east and southeast that one goes in the EU. With approximately €2,680/m² to €2,760/m², Romania, Poland and Bulgaria have the lowest sales area productivity values in the EU. Even so, these countries are among those boasting the largest gains, with annual increases from +5.7% to +6.7%, which means they are slowly but surely closing the gap.

The devaluation of the Turkish lira is also apparent when assessing the sales area productivity results for retail in Turkey. After the economic difficulties of 2018, sales area productivity in Turkey dropped to approximately €2,350/m², the lowest value among all countries in the study.

Sales area productivity in 2018



SPECIAL FOCUS COUNTRY: UNITED KINGDOM

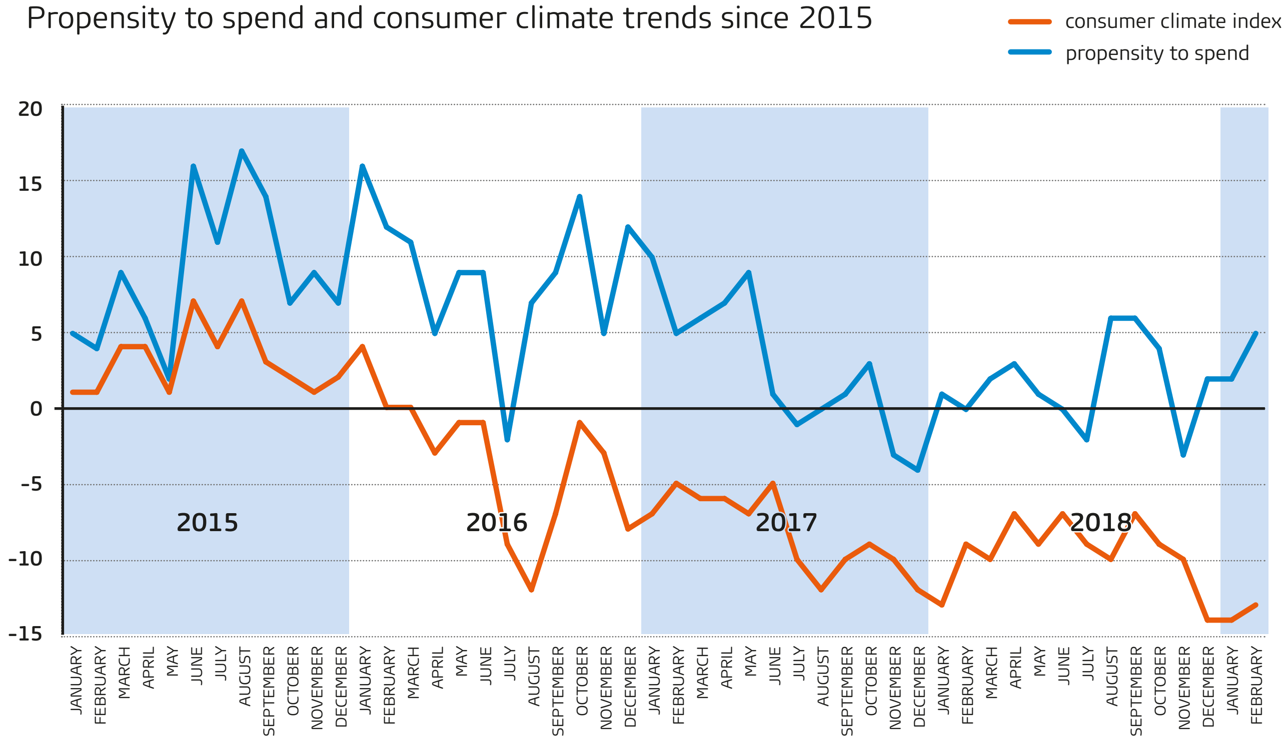
Turnover growth despite declining sales volume

It is impossible to say whether the United Kingdom will still be a part of the EU at the time of this publication, and if not, what the conditions of its withdrawal will be. The political uncertainty surrounding this historic event is simply too high. Taking this into consideration, the ensuing analysis has two goals: The first is a retrospective consideration of the impact of Brexit on consumers through an evaluation of the consumer climate. The second is an assessment of trends that should also hold true for the post-Brexit era based on what is currently known.

Consumer mood changeable after major referendum dip

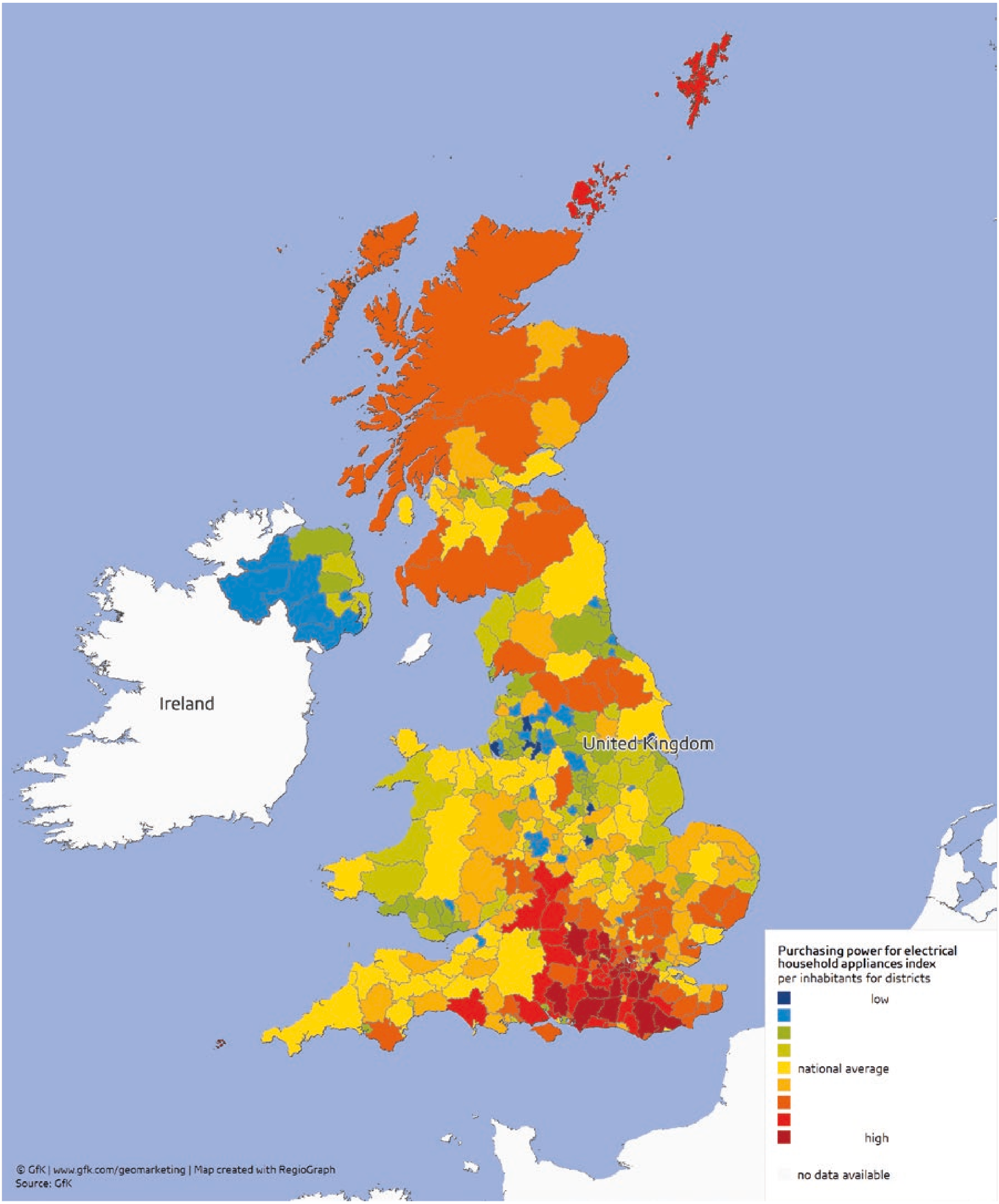
Amidst the increased risk of an unregulated Brexit in the first months of this year, British consumers were surprisingly stoic with regard to their propensity to spend. In February of this year, the propensity to spend index even climbed slightly by +5 index points compared to the end of 2018. At -13 index points, the more broadly defined consumer climate index is also stable, but at a significantly lower level. Immediately following the Brexit referendum in July 2016, both indices reacted strongly to the changed situation and dropped substantially, with the consumer climate index undergoing the largest decline in 26 years. The indices recovered slightly thanks to subsiding media coverage in the second half of 2016. But the announcements of price increases from manufacturers and retailers (necessary due to the weakening British pound) dampened consumer mood again over the course of 2017.

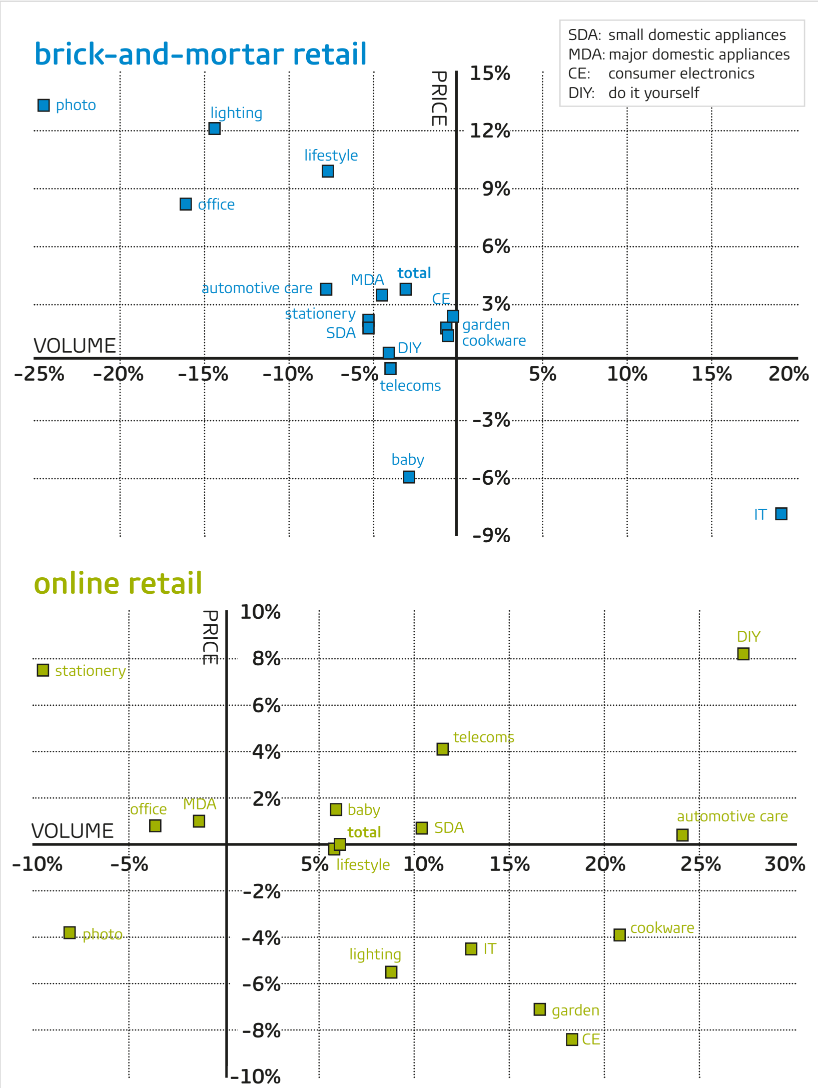
Propensity to spend and consumer climate trends since 2015



source: GfK

Purchasing power for electrical household appliances, United Kingdom 2018





source: GfK Point of Sale Tracking

Turnover gains despite declining sales volume thanks to trading up

Retail price increases as a reaction to the changed conditions also continued in 2018 and were a reason why the average price of durable consumer goods increased on average by +6.3% (both online and offline). A second major development is the so-called trading-up phenomenon - i.e., the purchase of higher value goods in the same product group. This has been a long-standing trend and a sign of an increasing quality-oriented focus among consumers. For example, televisions with 70 inch screens or larger as well as televisions with OLED technology are the fastest growing segments. Among small electrical appliances, the robust sales of high-priced brands such as Dyson are bringing the British market into the growth zone. According to GfK Point of Sale Tracking data, brick-and-mortar retail was able to achieve nominal turnover growth of +2.5% last year in the durable consumer goods segment despite a decline of -3.1% in sales volume.

Online retail growing more strongly than in Germany

A large portion of the retail growth for technical consumer goods was due to online retail, which profited more substantially from this segment (+9.1%) than was the case for brick-and-mortar retail (+2.5%). Consequently, online retail further expanded its turnover share to 35% – an increase of +10% over a span of five years. As such, the online retail of technical consumer goods has developed more dynamically in the United Kingdom than in Germany, where this segment's market share in the same time frame increased from 26% to 30%.

Substantially above-average spending on electrical household appliances in Northern Ireland

During the withdrawal negotiations, the Brits made it clear that they did not want an EU boundary between Northern Ireland and the rest of the United Kingdom, as some observers had requested. However, from a retail perspective, there is already a divide between Northern Ireland and Great Britain in terms of spending on electrical household appliances. Northern Ireland has an average per capita purchasing power index of 80.5. This equates to €183 per person, which is around 20% less than what is spent on electrical household appliances in brick-and-mortar retail by the average Brit and approximately one-third less than what an average London resident spends (€287).

This range is significantly broader at the level of the UK's 394 districts. For example, inhabitants of Kensington and Chelsea spend €517 per person on this product group in brick-and-mortar retail outlets, which is almost four times the amount that inhabitants of Nottingham spend (€132). However, this discrepancy is less than the purchasing power differences between these two regions. Concerning the latter, the value for Kensington and Chelsea (index 324) exceeds the value for Nottingham (index 66) by almost five times.

Making the right decisions for the future is challenging amidst constant change in the retail sector. Project developers, investors and retailers must continually respond to consumers' evolving needs and expectations.

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