Getting the measure of Europe's retail destinations

Redevco's latest City Attractiveness Model, which lists 200 European cities according to risk, highlights that soft factors, such as historical points of interest, are now playing a greater role in the rankings.

Location risk has risen up the agenda for investors into Europe in the past few years and many factors need to be juggled to determine whether a particular city should be a target. Retail property management company Redevco has taken its decision process to another level by developing its City Attractiveness Model, devised through a combination of hard facts and knowledge from Redevco's teams in each country (see box).

The annually-updated model is now in its fourth iteration and as it has been honed over the years it has started to throw up some interesting results – both in terms of what makes a city an investment hotspot and what makes a city a no-go area.

Starting with the top of the list, it is perhaps unsurprising that the most highly rated cities have remained more or less unchanged each year, explains Marrit Laning, Redevco's head of research and strategy. "For the last four years, the top 25 has been stable because they are all strong cities," she says. "They score so highly in fundamentals as well as soft factors. Further down, some cities have improved their positions as their economic situations improve, for example Spain was bad a couple of years ago but as we're seeing a recovery so some cities are improving their positions, such as Bilbao."

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Marrit Laning, Redevco

Fundamental shifts

While some fundamentals such as low yields, low vacancy and high rents are keeping the top 25 in their strong positions, it is the cities further down the list that are most positively affected by the fundamentals of rental growth and retail sales levels.

"Since the volumes of retail sales are particularly low in developing countries in the fringes of Europe compared to Western European countries, growth kicks in at higher rates," explains Laning. "Examples of this are found in Spain, Poland and Turkey. In Spain the economic crisis hit hard and is now bouncing back. Poland's economic growth is caused by an uplift in consumer spending power. This is caused by lower cost of living, an increase in labour market conditions and cheaper credit loan conditions. In Turkey the outlook is good due to private consumption booms due to low oil prices and monetary easing measures."

While the fundamentals of a city are important, Laning says the most interesting outcome of creating the model is the discovery of the importance of soft factors, such as the number of historical points of interest a city has, or the concentration of creative workers.

"When we started using the City Attractiveness Model we were actually quite surprised by the real impact of soft factors and how they are growing in importance," she explains. "If you think about shopping, you don't have to go to a store any more. If you go you want to see other things, be surprised, meet people and so on. This is where soft factors come in. They are even more important than we thought when we started, and we have raised them in importance as we have evolved the model."

Soft factors are increasingly driving the fundamentals, she says: "Rental value change in cities with a high number of historical points of interest is stronger than in cities with a low number of historical points of interest. In addition, the yield level compression is also stronger in cities with a higher number of historical points of interest. This stresses the importance of tourist retail spend as input for rental growth."

While highlighting Europe's strongest cities, Redevco's City Attractiveness Model also highlights the weakest. Though the company is naturally unwilling to release the full rankings, Laning says that only those cities that fall into the categories 'excellent', 'very good' and 'good' are deemed to be investment grade. For the cities nearest the bottom of the list, the future of retail property doesn't look too rosy.

"As you go down the list, cities are more susceptible to change," says Laning. "If you look at property performance and capital value growth there's an increasing polarisation. 'Excellent' cities have generated excellent capital value growth, but the top and bottom cities are getting further apart (see Figure 1). Some cities are struggling to maintain their relevance to the consumer."

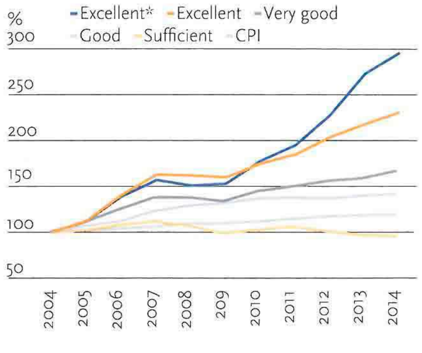
Online retail impact

The impact of online retail, which Laning believes is set to continue to increase as innovations are introduced to ease logistics, is one reason cities are losing their relevance to the consumer. As a result, some areas of Europe are experiencing high, and rising, vacancy rates, which is one of the model's indicators. Redevco has vacancy figures for around half of the cities analysed, of which about 40% are showing deteriorating vacancy rates.

"If you take into account that the ones we have figures for tend to be the better performing ones as they're more transparent, this suggests that about half the retail landscape is suffering from deteriorating vacancy," says Laning.

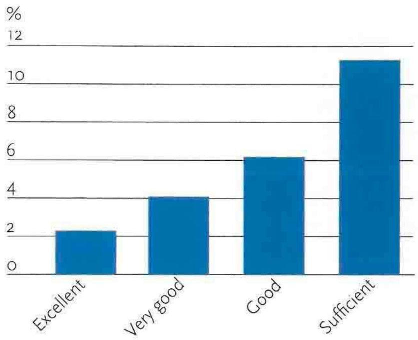
Generally, there is too much space available, she says. Last year Redevco calculated store densities and sales per square metre on a country level, based on data from Euromonitor International. Assuming that in 2000 store densities were healthy, it calculated what the store densities should be according to the economic cycle. The firm found that there is currently a lot of

Fig 1: Capital value growth index by city quality grade, 2004-2014
Top and bottom cities are getting further apart



Source: Redevco

Fig 2: Average vacancy rates by city quality grade 2014
Poorer areas experience higher vacancy rates



Source: Redevco

higher skilled workforce. We have to assume that immigrants will be integrated into a country's workforce and add to it, which could lead to higher retail spend."

Overall, Laning is confident the model equips Redevco well to make informed decisions. Judging by the cities at the top of the list, investments are likely to be made within the seven countries where it currently has teams on the ground. Although some less established cities feature high up the list, Laning says it still takes more than this for money to be committed.

"In areas such as Spain, Poland or Turkey that are less developed in terms of sales per capita, we see that the population will mature and grow as the middle class grows," she says. "At the same time we need a level of prosperity for positive movement to start, and it's not there yet in all areas. Our regulatory framework means we need to make safe investments and some areas pose a risk still and there are other factors we need to take account of, such as liquidity or the ease of operating in the area."

Redevco is currently focusing on the top 200 cities as defined by its model and, as Laning says, believes there are plenty of investment opportunities without the need to look further afield. As the property cycle moves along, however, and competition for assets increases, it may yet broaden its horizons further.

occupied selling space which is not profitable – perhaps 20-25% of operational stores. Laning is keen to emphasise that this is already an old number and certain retail digital leaders are closing more stores than they are opening, and being more profitable by doing so.

"This doesn't mean there's too much retail space everywhere – some cities that are performing particularly well have a shortage and prime areas are getting bigger," she adds. "Consumers are getting choosier about where and how they shop, concentrating spending in fewer areas, but in those areas footfall is increasing. Retailers are looking at adjacent areas in the same city, such as Le Marais in Paris, Fuencarral in Madrid or Rokin and Nieuwendijk in Amsterdam."

While the combination of fundamental and soft factors provides a firm base on which Redevco can determine a location's risks, certain factors cannot be easily predicted. One example is the current influx of refugees and migrants into Europe. Demographics and population growth are key factors in the model and can raise or lower a city's position.

"Some areas are already seeing a growing population, but that might not be people who are able to spend," says Laning. "That would cause a negative impact on the model, but it's very difficult to predict this population growth. It could also have a positive impact, where immigration is of a

HOW THE CITY ATTRACTIVENESS MODEL WORKS

The City Attractiveness Model ranks 800 cities in 25 European countries, using 19 indicators derived from 39 sources. The indictors, which Laning describes as a mixture of fundamentals and soft factors, are grouped into four categories, which are weighted to calculate a city's score. The categories comprise:

- **Population: pollution size, catchment area, future population growth;**
- **Economy: economic structure retail sales per capita, retail sales development, employment growth, unemployment, household disposable income;**
- **Property market: yield level, rental level, vacancy, share of international retailers, development pipeline, deal flow;**
- **City quality: tourism, creative professionals, historic points of interest, average age.**

Redevco's country teams then add their local knowledge and cities are ranked into five quality baskets from "excellent" to "poor".

TOP 25 CITIES

Top 25 has been table in past four years

1. London	10. Copenhagen	19. Frankfurt
2. Paris	11. Manchester	20. Stuttgart
3. Munich	12. Madrid	21. Dusseldorf
4. Berlin	13. Oslo	22. Glasgow
5. Hamburg	14. Barcelona	23. Edinburgh
6. Vienna	15. Rome	24. Dublin
7. Stockholm	16. Zurich	25. Istanbul
8. Milan	17. Cologne	
9. Amsterdam	18. Prague	