

DUTCH RETAIL MARKET CONTAINS HIDDEN GEMS

The Dutch retail market is becoming increasingly polarised but a selective approach to investments and active asset management can pay off

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Dutch retail real estate has traditionally generated strong returns, averaging more than 9% over the past few decades and outperforming both the residential and office sectors. But the market is changing and a clear division between ‘good’ and ‘bad’ real estate is emerging, making a selective approach to investments crucial.

The complex Dutch retail market has some unique characteristics. It can be divided into three distinct types made up of eight different retail segments (see illustration below). More than a third of the country’s retail stock is found in city centre shopping areas, while ancilliary city shopping streets and smaller, district and neighbourhood shopping centres account for around 14% of the total.

In other countries, large shopping centres in peripheral locations (such as supermarkets) account for a much higher proportion of the total retail stock. In the Netherlands, out-of-town retail parks, including

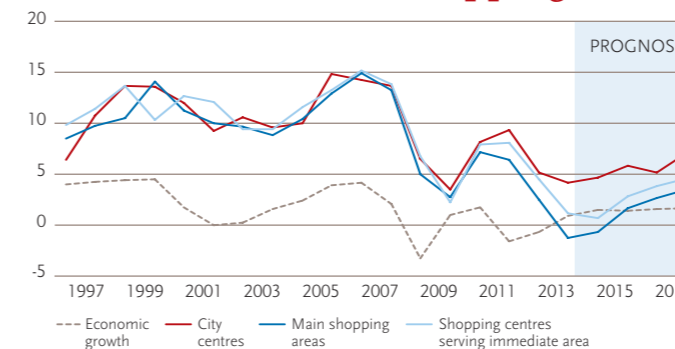
garden centres and DIY stores, make up just 16% of the total (see graphic below, facing page). Each of these three retail types has been affected in different ways by current retail developments, such as urbanisation and depopulation in parts of the Netherlands, the rise of online shopping and urban planning regulations.

Nevertheless, in Bouwinvest’s opinion, 2016 is likely to be a good time to enter the retail real estate market, from both a historical and an international perspective. Despite the difficulties there are still gems to be found and the Dutch market offers attractive returns – if you know where to look. Occupancy rates are likely to remain high in city centre shopping areas and in small district and neighbourhood shopping centres providing daily needs. Bouwinvest focuses on these two segments which, together, generate an attractive return. Local knowledge, driving a selective and active approach to asset management, is the key.

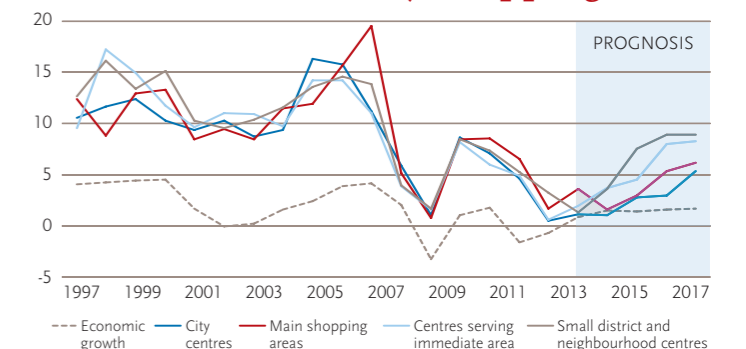
Retail segment definitions

RETAIL AREA	RETAIL SEGMENT	DEFINITION
Central shopping areas	<ul style="list-style-type: none"> City centres Main shopping areas Shopping centres serving immediate area 	<ul style="list-style-type: none"> City centres of 17 largest Dutch cities (more than 400 shops) Largest shopping areas in mid-size and small cities (between 100 – 400 shops) Centres of small and large towns (up to 100 shops)
Ancillary shopping areas	<ul style="list-style-type: none"> Borough centres City centre shopping street Large district centres Small district and neighbourhood centres 	<ul style="list-style-type: none"> Supplementary to central shopping areas (more than 50 shops). E.g. Amsterdam Osdorppelein. Ancillary shopping streets in larger cities, non-planned developments (> 50 shops) Supplementary to central shopping area (25 – 50 shops) Specific ancillary function with supermarket and 5 to 25 shops.
Other shopping areas	<ul style="list-style-type: none"> Large-scale concentrations (retail warehouses) 	<ul style="list-style-type: none"> More than five shops with floor space greater than 500 m², with more than 50% selling larger goods: furnishings, plants, DIY, etc.

Total returns central shopping areas



Total returns ancillary shopping areas



SOURCE: MSCI, OXFORD ECONOMICS, COMPILED BY BOUWINVEST RESEARCH (2015)

NEW BUILD ADDS VALUE IN RETAIL HOT SPOTS

Bouwinvest research shows new-build projects do add value in the strongest shopping areas. For example, the Bouwinvest Retail Fund is the largest investor in new retail in Amsterdam and has just completed a key city centre redevelopment project with C&A and Primark as anchor tenants. Until 2006/2007, the Netherlands maintained a healthy demand and supply ratio. In 2006, however, the government relaxed the rules, placing more responsibility for retail planning with local authorities. As a result, councils embarked on a large number of ambitious retail developments without any regional coordination. One of the effects was to end limits on peripheral developments, leading to further saturation of the market and a rise in the total retail stock of some 16%. The result has been rising vacancy rates, which by early 2015, had reached more than 7% of total retail space.

The rise of online shopping has created additional problems, although the impact depends on the type of retail development and the product. Despite the general decline in consumer spending, the share of ‘online purchases’ in total retail has risen sharply in recent decades. In 2014, online travel, ticket, food and clothing sales accounted for more than 11% of total Dutch retail sales, putting the Netherlands at the forefront in Europe.

Bouwinvest expects declining demand for physical retail real estate, combined with the still growing supply, will widen the divide in the retail market in the years ahead. What is good will become better and what is bad will become worse. The rise in online shopping is unlikely to have a significant impact on city centre shopping areas that offer the ‘fun-factor’ and they will continue to deliver strong returns. In addition to a complementary retail stock, the big cities such as Amsterdam, Rotterdam and Maastricht also have good bar and restaurant facilities and cultural attractions, providing a complete package for a day out. Smaller and medium sized cities are more vulnerable to the impact of online shopping than big cit-

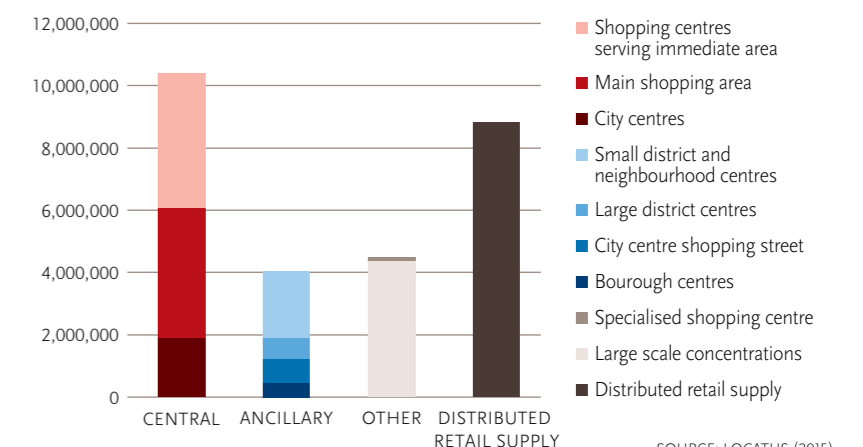
ies because they may lack these facilities.

While city centre developments benefit from the ‘experience’ factor, district and neighbourhood shopping centres with a focus on daily needs win favour for being convenient. The strong and stable turnover in the food segment continues to boost such ancilliary shopping areas’ performance, with returns averaging 6.7% in 2014. In particular, complementary specialty shops, such as bakeries and quality butchers, which offer consumers a wider selection, greater service and quality are helping keep both occupancy and lease rates at a healthy level.

CAPITAL FLOWS TO NEIGHBOURHOOD CENTRES

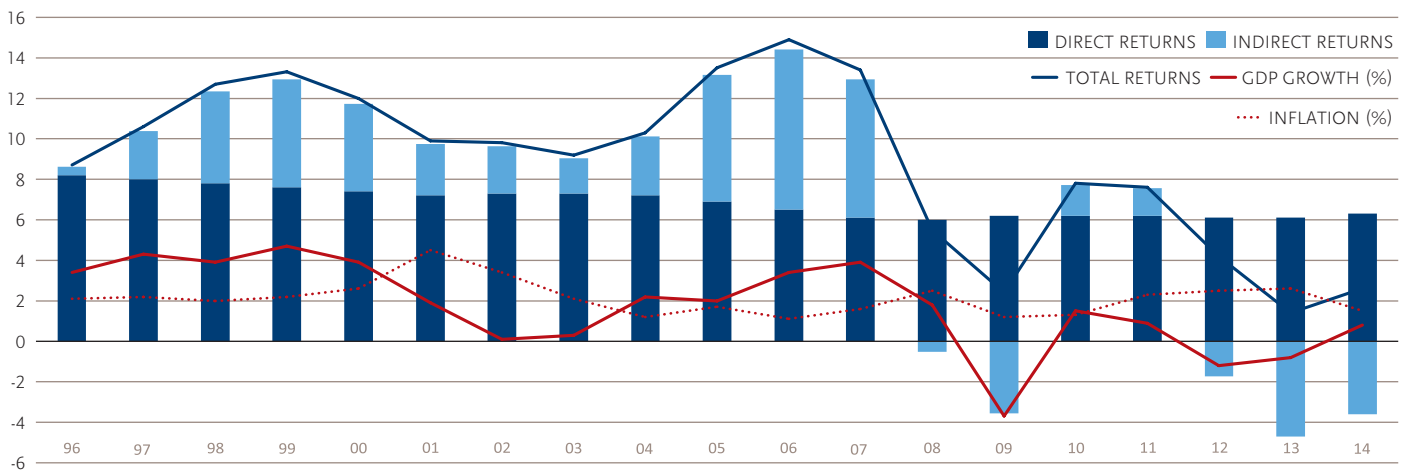
Neighbourhood centres are attracting considerable capital with their traditionally high yield gaps. The risk of vacancy is relatively limited and, thanks to the ongoing recovery of the economy, there is a chance of value growth in the medium term. However, retail areas with a relatively large proportion of shops for non-daily

Retail stock (m² GLA) per segment



SOURCE: LOCATUS (2015)

Returns Dutch retail estate, GDP growth and inflation (1996-2014, %)



SOURCE: MSCI, OXFORD ECONOMICS, COMPILED BY BOUWINVEST RESEARCH (2015)

essentials are finding it more difficult to keep occupancy rates at a healthy level.

Peripheral shopping areas (referred to as 'other shopping areas' in the definitions box) have a more volatile character than ancillary shopping areas and economic upturns and downturns have more impact. The retail stock is largely focused on non-daily needs and organised around a theme, such as home furnishings or DIY. The positive economic outlook supports peripheral shopping areas. However, this retail segment is also vulnerable to the impact of online shopping and any new-build retail supply. The Netherlands only has room for a limited number of peripheral shopping areas, as the catchment area has to extend across regions to have sufficient mass. In addition to economic growth, returns are highly dependent on planning management at a provincial and national level. Bouwinvest sees the lack of planning as a major risk.

ECONOMIC GROWTH WILL BOOST RETAIL VALUE

Now that the economy is picking up again, value growth in Dutch retail is also expected to be positive. The consensus is that we will see steady economic growth of

around 1.5% to 2.0% per annum over the next few years. Consumer confidence and spending are on the rise again and economic growth forecasts are being adjusted upwards (see graphic above).

This means 2016 looks like a good time to enter key sectors in Dutch retail real estate market: small district and neighbourhood shopping centres and the city centres segment. From a historical and an international perspective, the risk premium for the best retail real estate is fairly high, largely due to the sharp drop in long-term interest rates. On top of this, there has so far been no comparable drop in the prime net initial yields in the Netherlands, unlike in a large number of real estate markets worldwide.

Dutch regions with a healthy economic and demographic outlook are seeing growth. Central shopping areas in large cities are embracing omni-channelling and offer consumers extra experience when compared to online shopping. Small district and neighbourhood shopping areas are performing relatively well because of their focus on daily necessities. At the same time, shopping centres in areas where the population is declining and economy is lagging behind offer little added value compared to online shopping and central shopping areas, making them particularly vulnerable. This polarisation makes a selective approach and active asset management crucial to ensure attractive returns on retail investments.

Company profile

The Bouwinvest Retail Fund's investment strategy has two key strands: prime high street locations in the largest Dutch cities and district shopping centres that consumers use for convenience purchases. This combined 'experience and convenience' approach has generated consistently higher investment returns than the benchmark IPD's Dutch all-property index.

For more information go to <http://www.bouwinvest.nl/en/funds/retail-fund/>



Download the most recent Retail White Paper: Attractive Return in an increasingly polarised Dutch retail market