retailthinktank
KPMG | Ipsos

2013-2014

annual review

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About the Retail Think Tank

Creation of the Retail Think Tank...

The Retail Think Tank (RTT) was conceived and created in 2006 by Helen Dickinson (former Head of Retail at KPMG LLP) and Tim Denison of Ipsos Retail Performance (Ipsos) to provide an authoritative, credible and trusted window on what is really happening in retail and to develop thought leadership on the key areas influencing the future of retailing in the UK. The intended audience for the outputs of the RTT is primarily retailers as well as anyone with an interest in all aspects of retail and retailing.

KPMG cutting through complexity

Ipsos

Who are we?

Nick Bubb (Retail Consultant to Zeus Capital)

Dr Tim Denison (Ipsos Retail Performance)

Martin Hayward (Founder of Hayward Strategy and Futures)

Richard Lowe (Barclays)

David McCorquodale (KPMG)

Vicky Redwood (Capital Economics – Left July 2013)

Neil Saunders (Conlumino)

Mark Teale (CBRE)

James Knightley (ING – Joined the RTT Dec 2013)

What do we do?

Our primary objective is to give a balanced, considered and unbiased view of the true state of the health of the retail sector. We aim to provide an authoritative, credible and trusted window on what is really happening in retail.

We assess the 'Health' of the UK retail sector

- Traditionally it has proved incredibly difficult to get a true view of the state of affairs with different sets of statistics due to:
  - sheer volume of data; and
  - large variation in how it is generated and then interpreted
- Since inception, the RTT's activity includes:
  - a retrospective look at the past quarter - looking ahead to the next three months
  - taking into account the three key drivers of retail health: Demand; Margins; and Costs
- The Retail Health Index (RHI) outputs provide analysis and a visual snapshot of how health is changing on a quarter-by-quarter basis covering the past six years

We write White Papers

- Thought leadership on the key areas influencing the future of retailing in the UK
- Issued quarterly throughout the year
- Highlighting issues and investigating areas of topical relevance to retailers
- The 2013 White Papers are included in this review and we have previously covered topics including:
  - the impact of inflation on retail health and strategy
  - like for like sales and whether they are still a useful measure of retail performance
  - is weather just another excuse of retailers' poor business models and risk management?

Where to obtain further information?

www.retailthinktank.co.uk

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contents

After eight quarters of retail health on a downward trajectory, 2013 started as the previous year had ended, with more high street casualties including Blockbuster, HMV and Republic. The threat of a triple dip recession hung heavily in the air, the inflation picture was deteriorating once more and consumer confidence remained buried in the deep trench in which it had sat for 12 months.

2013 retail health index review

Quite unexpectedly, however, demand, and with it retail sales, began to improve in Quarter 1. The food sector was the star performer of the quarter, despite the horse meat contamination scandal rocking consumer trust in supermarket product quality and sourcing. The convenience formats traded particularly well over the long winter and inclement conditions. Elsewhere sales were heavily promotion-led, a scene that endured for the best part of the year in the non-food sector. The uptick in demand was strong enough to stop the decline in retail health and for the Retail Think Tank to register a 1 point improvement to its Retail Health Index (RHI), moving it off its nadir score of 76.

The positivity rolled through into Quarter 2. Monthly sales figures painted a confounding picture to RTT members, particularly as the economy still appeared to be bumping along a corrugated bottom and real earnings carried on shrinking thanks to rising inflation. Retail sales saw growth at levels beyond those of previous quarters, reflecting sustained employment growth and consumers' inclination to spend, given access to easier borrowing and an absence of incentive to save. Many retailers continued to feel pressure to promote sales and discount in order to nurture demand. The food sector, in particular, remained extremely competitive with many of the major grocery stores set on discounting to claim market share. And because of the lengthy wintery weather conditions, the clothing market was concertinaed into a very short season. Overall, stronger demand outweighed any weakness in margins and led to the RHI gaining another point in Quarter 2, moving to 78.

By the middle of the year the indications were that retailing was finally entering calmer waters; RTT members deemed that conditions had steadied rather than have picked up discernibly. It was too early though to talk of the beginning of a robust retail recovery, but the signs were there that things were edging upwards and a healthier state of play was returning. The Retail Think Tank noted a marked mood shift in the commercial retail property market compared to the year start.

Though still southern and London-centric, some of the large shopping schemes that had been shelved following the onset of the recession returned to the viability table. News that the UK had not, in fact, even suffered a double dip recession, that GDP bounced back strongly in Quarter 2, that employment figures continued to impress and that signs of recovery in the housing market were appearing all helped bolster consumer confidence. This change in sentiment, accompanied by the enduring warm weather and sporting successes also contributed to the release of some pent up demand throughout July and August which boosted food sales and the Summer clothing season.

The combination of stronger demand and holding less stock enabled retailers to sell more through at less discounted prices, putting gross margins under less pressure than they had been in the first half of the year. For the first time in three years, two of the three key drivers of retail health – demand and margins – turned positive in Quarter 3 and the RHI notched up another point to 79, its highest level since Quarter 3 2011. Costs remained a concern for retail health in the Autumn, however. Although online sales continued to show relatively strong growth, members were conscious that the associated incremental transport costs and logistical challenges of fulfilment represented a growing burden, though the popularity of click-and-collect helped mitigate some of these costs.

Expectations for Quarter 4 were that the health of the sector would improve still further. Economic conditions were generally on the rise, some semblance of stability had returned to the sector and there was a sense that employees had become less nervous at losing their jobs and had become more comfortable at spending again. October's news of double digit hikes in energy prices was unwelcome, however, and served to emphasise the vulnerability of the consumer spending upturn.

In the event Quarter 4 became a mild disappointment and the RHI remained flat at 79. RTT members conceded that Christmas spending levels had been tempered by the ongoing fall in disposable income levels. Slower than expected demand in the middle weeks of December had put intense pressure on retailers to discount, which in turn squeezed margins for those that crumbled early. Furthermore, the caution that consumers exercised with their household budgets led to competition intensifying in food retailing and discounters gain valuable market share. The winners over the festive season were those non-food retailers that were able to offer a seamless multi-channel operation, enabling people to shop at their convenience, and those that refused to discount too early or too heavily.

2013 was the year of a consumer confidence comeback when retail health moved back into a state of gradual growth.

prospects for 2014

View of members

Richard Lowe

Head of Retail and Wholesale, Barclays

Richard Lowe has been a corporate banker for over 30 years, and has provided advisory and specialist banking services to retailers and wholesalers in the UK and Ireland for the past 16 years.

As Head of Retail and Wholesale at Barclays he and his dedicated London team of relationship directors, together with the pan UK & Ireland relationship directors are responsible for thousands of clients ranging from boutique fashion houses and high street booksellers to department stores, all with turnovers in excess of £5m. Additionally, retailers and wholesalers are offered access to the products and expertise of the other businesses in the Barclays Group including the Investment Bank and the Wealth & Investment Services division.

Richard is a regular commentator in the national, regional and trade media on retail trends and industry issues as well as retail sales figures. Away from the office he is an avid reader and when time allows he is also a motor racing enthusiast. He is married with two children and lives in Hertfordshire.

Expectations are that the British high street is in for a successful Christmas but, once the festive tunes have faded and the sales rails have been cleared what will 2014 have in store for retailers?

The sector is on a positive path and while there will, undoubtedly be a few kinks along the way retailers can take comfort from improved growth numbers and a cautiously confident consumer as a sense of balance slowly returns to the UK economy. Across the channel, the Eurozone's problems have remained manageable or, at least, stayed out of the headlines and, consequently, out of British consumers' minds.

With the economic stage set, omni-channel strategies will continue to dominate the boardroom agendas of Britain's retailers. I expect to see a renewed focus on the logistics of the last mile which is becoming increasingly important as consumers push for greater convenience. Service offerings such as click & collect will also continue to rise in popularity and sit well with sector strategies as they allow retailers to maximise value from their existing store infrastructure and cost base. As a result, rationalisation and investment in stores and staff to support these offerings will be important throughout 2014.

While domestic growth will continue to be the mainstay of retail revenues, retailers will also continue to eye consumers further afield to boost sales whether it is from purchases made online or tourist spend in physical stores in our larger towns and cities or those with visitor attractions. In 2012 it was estimated that foreign visitors spent a staggering £4.5bn whilst visiting the UK so plans to relax visa rules for Chinese visitors, who already add some £300m alone to the British economy, should also help boost till receipts further.

The past few years have not been easy for retailers, and despite the air of uncertainty which continues to linger around the wider economy, the general feeling is that the sun is starting to rise. This should provide the fillip the high street is looking for 2014. As a result, Barclays remains a committed supporter of the sector.

Mark Teale

Head of Retail Research, CBRE

Mark Teale joined CBRE (Hillier Parker) in 1986. Initially setting up a retail project consultancy team, Mark was appointed Head of Retail Research in 1989. Mark's research team specialises in retail property related consumer market research and forecasting but covers all aspects of retail research including information development for market analysis systems, shopping development viability studies, store location analysis and benchmarking.

Mark was responsible for establishing the industry's first shopping centre trading audits for rent review purposes. Mark also pioneered The National Survey of Local Shopping Patterns (NSLSP) survey, the largest continuous household survey programme of shopping destination preferences undertaken in the retail industry. The NSLSP survey is widely used by leading store groups for locational analysis purposes and by property/planning organisations for impact forecasting. Mark is now primarily concerned with the development of local forecasting and benchmarking applications and related retail property market measurement applications.

More of the same, yet again!

Economic sentiment improved significantly during 2013. The general expectation is that we are going to see (relatively) strong Christmas trading, at least in London and the South East. There is little sign of a sustained upturn in retail market prospects setting in during 2014 however, not least because of continuing deflationary pressures in tandem with equally persistent cost inflation. Whatever the Christmas outturn, retail sector profits will continue to be squeezed in 2014.

Retail expansion activity levels flat-lined in 2013 with openings – in branch number terms but not floorspace – pretty well matched by closures. Retail floorspace levels continued to increase though due, in large part, to expansion activity in grocery and discount sectors. It has tended to be large floorplate stores that have been the most active expanders during the downturn (grocers, pound shops, discounters generally etc). Large store market share gains, in conjunction with internet sales growth, have inevitably left weaker secondary high streets pock-marked with vacancies but without interrupting net shop space growth elsewhere, predominantly in grocery markets.

It is often forgotten in this respect that a single superstore can have net sales space equivalent of 70 or more high street unit shops. Vacancies are meanwhile heavily concentrated in the small-unit secondary high street shopping stock. Cumulatively, this vacant stock accounts for a tiny percentage of overall shop space (however newsworthy a 14% vacancy rate might appear). And that is the heart of the perennial 'high street problem': a chronic supply/demand mismatch. The market is awash with small unit shopping that is no longer viable for mainstream retailing purposes while there is a permanent shortage of high productivity shopping stock that meets modern retailer size and locational requirements. There is no magic planning wand that can render obsolete tertiary and poor secondary high street shopping productive so do not expect the flurry of 'saving the high street' reports to have much impact on failing high streets; without fundamental changes in regulatory controls and town centre management the problems are irresolvable.

Speculative development activity remains stuck at rock bottom levels. Primary stock availability continues to dwindle. A primary supply famine is setting in once again. Because of obvious primary stock shortages, a small number of large shopping centre schemes are now finally being stirred into life but it will take a very major – and sustained – improvement in underlying economic activity to see pipeline levels begin to lift significantly. Only London is bucking the trend. The boom conditions experienced in Central London look set to continue during 2014. The problem for Central London, as always, is a chronic lack of supply. Plus ça change.

Dr Tim Denison

Director of Retail Intelligence, Ipsos Retail Performance

Dr Tim Denison, BSc MSc PhD MCIM, is Director of Retail Intelligence at Ipsos Retail Performance, the UK's market leader in performance improvement systems for retailers. He is also a regular commentator, broadcaster and conference speaker on retail matters, particularly those related to behavioural issues.

Tim is Director of Retail Intelligence at Ipsos Retail Performance, part of Ipsos, the third largest market research company in the world. Ipsos Retail Performance is a specialist retail business unit, that uses technology to monitor retail footfall, shopper behaviour and capture retail trends. Tim set up its analytics and consulting services when the company was established in 1995. He is regularly invited by national and international media to comment on shopping behaviour in his capacity as a retail psychologist.

Trained formally as a social scientist and marketer, Tim has written over 50 papers, reports and publications on consumer behaviour. Before joining Ipsos Retail Performance he worked at Cranfield School of Management specialised in retail and branding issues and consulting on key research and policy initiatives on behalf of organisations such as the European Commission, the Department of Trade and Industry, BP and BT.

2014 – a smart, new world

The health of the retail sector in 2014 will be led by demand-side issues. Will consumer confidence continue to recover? If it does, we can expect those in a position to do so to spend a little more and save a little less, as they have in the second half of 2013 which helped to inject some momentum into retail sales. More fundamental and more universal is what happens to real earnings. Inflation peaked in June 2013 at 2.9% and has been heading towards the Bank of England's target ever since. In contrast wage awards have remained doggedly low, tracking at about half the level of inflation. Public and private sector productivity needs to improve before we can expect to see significant real earnings growth, and for that to happen businesses need to re-discover the confidence and preparedness to invest. This will be a slow process and one that is unlikely to gain great traction in 2014. Consequently, at best we can only expect wage awards to converge towards inflation rates and the decline in spending power to abate. With a fair wind, subdued growth in demand will edge up the health of the retail sector in 2014.

People talk about 'the road to recovery' with an expectation that retailing will return to the halcyon days of post-millennium. In truth of course, the future will inevitably be different from anything that has gone before it. We can expect more change than we have seen in recent years– changes in public policies affecting retailing, changes in how retailers connect with their customers and changes to shoppers' behaviour and attitudes. The need is no longer one of battening down hatches; it's time for action.

I have no doubt that this will be an exciting year, driven by the rapid development of the digital age. We can expect retailers in 2014 to move beyond a promotion-led strategy towards more creative practices. Participating in and facilitating connected customer communities is one obvious path that is being trod. The ability to develop more targeted approaches and personalised offerings that augment desirability, relevance, affordability and motivation and embrace technological innovation provides routes that leading retailers are beginning to explore, conscious that investment will need to be just as important a part of 2014 success as cost control.

David McCorquodale
Head of Retail, KPMG

David McCorquodale is UK Head of Retail at KPMG and is responsible for leading and developing the firm's retail practice in the UK. An experienced M&A practitioner, he is regularly quoted in the trade and national media on retail sales trends and other key issues affecting the sector.

David has been with KPMG since 1984 and is one of the founders of KPMG's corporate finance business, advising listed and private companies on divestitures, acquisitions and fund raisings. He also leads KPMG's European retail transactions and restructuring practice and has advised on numerous high profile retail transactions, including the sales of Card Factory, Dreams, Peacocks, Blacks Leisure and JJB Sports.

KPMG is an associate member of the British Retail Consortium (BRC) and David works closely with the BRC in a number of areas including the analysis, sponsorship and administration of the BRC-KPMG Retail Sales Monitor.

Recession over, investment resumes

2013 has seen a return to growth - hard fought, hard earned and sometimes fragile: but growth.

We've seen an end to the cold recession but not witnessed the quick thaw that has followed previous downturns. Consumers may have a little more confidence with greater job security and better economic news but, with wage rate inflation still lagging general inflation and utility costs increasing, that confidence has not yet turned into cash.

I see further growth in 2014 in the retail sector but recovering from a deep, long, global recession is not the only challenge facing retailers. The sector must respond to the seismic shift caused by the internet that has changed its face forever, commoditising the sector. Returning to old pre-recession ways is not an option now.

The recovery in 2014 will not simply resurrect the pre-recession consumer – instead, the thaw will reveal many consumers with real financial pressures who don't see a way out. Those with jobs and cash have got used to value and will stick with that rather than trade up just because they can. All consumers now want a bargain but also demand best in class service in a multi-channel environment. Price matching may not be enough to win the sale – differentiation around delivery service or collection ease is also a key component.

For five years now, some retailers have simply battened down the hatches to survive. Others have fought on many fronts to change, adapt and invest for growth. It is not too late to join the investment race but for those who can't get out of survival mode, survival itself will become much harder.

The winners of 2014 will be those who have invested and who continue to invest in the future of their business. The priority investment areas for 2014 include: systems to link their many channels; robust and short supply lines; information that allows them to merchandise rather than simply buy stock; data analytics to trail their customers through their digital exhaust and personalise their promotions; delivery services and international markets. We may not have drones and robots yet but it's clear that those who invest are opening their minds to such things.

Stock markets have been good for retailers in 2013 and they will be open for new entrants in 2014. Many IPOs are being lined up. Some, but not all, will succeed. However, all eyes will be on successful debuts from those from a PE backed environment as a poor trading update from one may well close the door on others. Debt markets have also eased for retailers and I expect this to continue as the year unfolds.

I look forward with confidence to another year of change from a very dynamic sector; fortune will favour those who invest decisively.

Nick Bubb
Retail Consultant to Zeus Capital

Nick Bubb has been a leading retailing analyst for over 30 years. He retired from the City last year, having worked at a number of different stockbroking firms and investment banks (including Morgan Stanley, Société Générale and Arden), but he is still a well-known commentator on UK retailing in the press and works as an independent retailing analyst and consultant.

Nick was rated No 1 in the 'Institutional Investor' magazine 1988 poll of Stores Sector analysts. Nick has been ranked in Retail Week's 'Top 100' list of the most influential people in retailing. Nick graduated from Christ Church, Oxford (MA in Philosophy, Politics and Economics). He is married, with two children, and lives in Richmond in Surrey, where he spends much of his spare time gardening, reading and watching cricket and horse-racing.

The outlook for 2014: Food bad, Non-Food good?

Economists will look back on 2013 as the year that the economic recovery started, but it hasn't felt like a recovery for many in the country, particularly those living outside London.

With some help from his new best friend at the Bank of England, who seems absolutely determined to keep interest and mortgage rates as low as possible, the Chancellor of the Exchequer appears to have engineered a good old-fashioned pre-Election recovery, with GDP forecasts picking up nicely.

But the recovery is, literally, coming off a low base after the 2008 financial slump and it is very much a wealth/London housing market-driven affair (additionally boosted by the bounceback in activity in the City and the financial services sector), as exemplified by the apparent prosperity of the John Lewis Partnership customer base. Improved job security has helped boost the overall consumer confidence surveys, but many of those jobs are part-time and so household incomes are not keeping pace with inflation, which is why Tesco and others have been saying that the mass-market is a much tougher place.

For food retailers in general, let alone Tesco in particular, 2013 has been a disappointing year, despite a period of strong demand in the summer. Since then LFL sales have been flat and the astonishing rise of the discounters like Aldi and Lidl shows that many households are still keen to economise. With Waitrose and M&S Food continuing to do well at the premium end of the market, there is no end in sight for the squeeze on the middle ground. This may yet bring more casualties in senior management if investors in the City lose patience, but Morrison's will attempt to square the circle with the launch of their Fresh Food focused approach to online grocery retailing in January, which seems well conceived.

In non-food retailing, 2013 has seen further amazing growth in both sales of tablet PC's and the usage of such "mobile devices" for online shopping, which continues to revolutionise the industry. Retailers of consumer electronics have done very well and there are more gadgets in the pipeline, including "smart" watches and glasses, together with another World Cup spike in TV sales, but there is some evidence that the sheer bulk of consumer spending in the general area of electricals has diverted money from other retail sectors, including clothing.

For 2014, the recovery in housing market activity should stimulate more spending on household goods, after a period of suppressed replacement demand. But the timing of such spending will, as ever, be partly determined by the vagaries of the Great British Weather, which in 2013 saw a cold/late spring followed by a summer heatwave...

Martin Hayward

Founder, Hayward Strategy and Futures

Martin is the founder of Hayward Strategy and Futures, providing strategic marketing advice to the Loyalty, Retail, Insight, Financial Services, Telecoms, Media and Consumer Goods industries.

An acknowledged thought leader in the future of customer data, insight, loyalty and marketing, Martin was previously Director of Strategy and Futures for dunnhumby, at the heart of the development of the innovative use of detailed customer data for marketing and communications. His previous position was as Executive Chairman of The Henley Centre, WPP's leading Strategic Marketing Consultancy.

Prior to joining The Henley Centre, Martin was the founding Managing Director of BBH Futures, the strategic consultancy arm of the Bartle Bogle Hegarty Advertising Group. He was also Head of the Marketing Services Department for Mercury Communications, during which time Mercury was voted Brand of the Year.

If ever there was a year to get the temperature of the economy right, then next year will be it. The UK needs a Goldilocks economy, not too hot but not too cold.

The balancing act will be tricky for the governor and the government, as many of the challenges of an accelerating economy are already beginning to manifest themselves. On the one hand it's already being asked if we are merely creating a mini credit fuelled boom, driven by house prices and reduced consumer saving. Equally there are questions about the continuing reluctance of government and business to invest that may hold back growth.

The UK retail sector is clearly very dependent on how well this balance between consumer and industry led growth plays out.

At the heart of the consumer response will be where interest rates go. If they stay low, we will see continued consumer confidence albeit with risks of another bubble. But if they go up too quickly, it could choke the momentum underway. Real incomes are unlikely to rise significantly for most households in 2014, so confidence in the future will be the catalyst for releasing consumer spending.

Overall, as long as the policy makers play their hand correctly, it is likely that the gradual improvement in consumer confidence seen over the last few months will continue over the next year. This combined with a recovered housing market will drive more big ticket purchases, but longer term payment and credit plans may become more popular again. This could be the golden year of the DFS model.

On the channels front, we shall begin to see the seamless integration of on-line and off-line really come to the mass market, which should enhance the in-store experience, and bring greater convenience to shoppers. The challenge for retailers will be to understand the changing journey that shoppers are undertaking, and to not use this as an opportunity to reduce staffing costs, but to use their staff in different ways to deepen customer engagement and satisfaction. There will also be an interesting challenge to use the new tools such as location based services and targeted promotions selectively to avoid 'offer anarchy' and a descent into purely price driven purchasing. Rather ironically, in a digital age, the in-store experience could well be the element that allows a price premium to be maintained.

James Knightley
Senior UK Economist, ING

James Knightley is a senior global economist at ING with particular focus on the UK and US economies. James has written extensively on the pressures facing both the household and corporate sectors since the start of the global financial crisis and during his time there the ING economics team has consistently ranked highly in surveys of forecasting accuracy.

He is frequently quoted in the UK and international press and appears regularly on television and radio. James joined ING as a graduate trainee in 1998 after studying at Durham University.

2014: Feeling the recovery

2013 saw a remarkable turnaround in the economy's fortunes. At the start of the year there were fears of a "triple dip" recession, but in the end the UK is likely to have grown by close to 2%. 2014 looks set to be even better with growth of 3% looking achievable.

Business confidence has rebounded sharply and we suspect that after several years of retrenchment, firms are going to be moving into a more expansive mode. UK businesses are cash rich so we suspect the one area of real weakness over the past five years – investment spending – will be a major driver of economic activity. We are also increasingly upbeat on the UK's largest trade partner, the Eurozone, so exports should also perform better. Nonetheless, the UK's longer term recovery will not be guaranteed unless the household sector responds more positively.

Consumer confidence has risen markedly over the past 12 months, reflecting the strengthening jobs market. However, the majority of households have not been feeling this improvement in their pockets. Wage growth has failed to keep pace with the cost of living for over four years, meaning a significant erosion in spending power. As a result, we have seen households dipping into their savings to fund spending growth.

Households should begin to feel the recovery in 2014. As the economy gains momentum, productivity should rise, which will boost corporate profitability and make it more likely that businesses offer their workers a greater share of the rewards from the recovery. Consequently, we suspect wages will rise faster than price inflation this year, thereby boosting spending power and the prospects for the retail sector.

One potential issue that could worry the high street is that the Bank of England may be the first major central bank to raise interest rates given the strengthening economy. However, the BoE is now looking at "macro prudential" policies to specifically target certain "hot" areas of the economy, such as restricting credit to the housing market. Such action will help limit the scale and pace of any interest rate rises.

Neil Saunders
Managing Director of Conlumino

Neil is Managing Director of Conlumino, a research agency specialising in retail and consumer research. In this role he heads up client projects working with retail and consumer related companies to help develop, evolve and implement business strategies.

Prior to Conlumino, Neil worked at Verdict for over ten years where, before the company's acquisition, he was a board director with responsibility for Consulting, Corporate Development and Planning. Latterly, he was Consulting Director and responsible for all bespoke and consulting projects.

Before Verdict, Neil worked for the John Lewis Partnership where he was involved, among other things, in the planning and relocation of new stores, the development of the John Lewis website and the creation of technical and information systems. Neil serves as a non-executive director of the train operating company First Great Western and is a Visiting Fellow at the School of Management, University of Surrey.

There is little doubt that 2014 starts on a more optimistic note than 2013. The economy is back in growth, consumers are more confident, and retailers are more optimistic about the future.

However, as well as the differences, so many things are the same: inflation remains fairly entrenched, household incomes are under pressure, and the economy is still fragile. The end result is that 2014 will be a better year for retail, but only by a matter of degree.

While the improved economic outlook will deliver more growth for the sector, it is important to remember that some of the present pressures are caused by structural, rather than cyclical, factors. These will continue to exert a challenging influence regardless of the prevailing economic conditions. Foremost among these are the issues of overcapacity and the closely allied problem of channel shift.

As a very mature sector, retail in the UK is highly competitive and, arguably, we have too much capacity relative to demand. From the consumer point of view this is a positive as such a competitive dynamic improves standards and reduces prices. However, from the retailer point of view it places pressure on margins and, potentially, means that not all 'retail mouths' can be adequately fed. Consequently it creates an environment of winners and losers; a trend that will continue to prevail over the course of 2014.

Closely related to the overcapacity issue is the ongoing channel shift which will see online take an ever greater share of retail spend. Although it is important not to exaggerate the influence of online – it will not destroy all high streets, for example – it is vital that legacy retailers reassess their routes to market and store portfolios in light of this shift in the way people shop. For many, 2014 will be a year of putting their retail houses in order.

So, the coming year will bring some respite to the retail sector and it will bring with it much better prospects. However, any retailers hoping for an 'easy ride' will likely be disappointed.

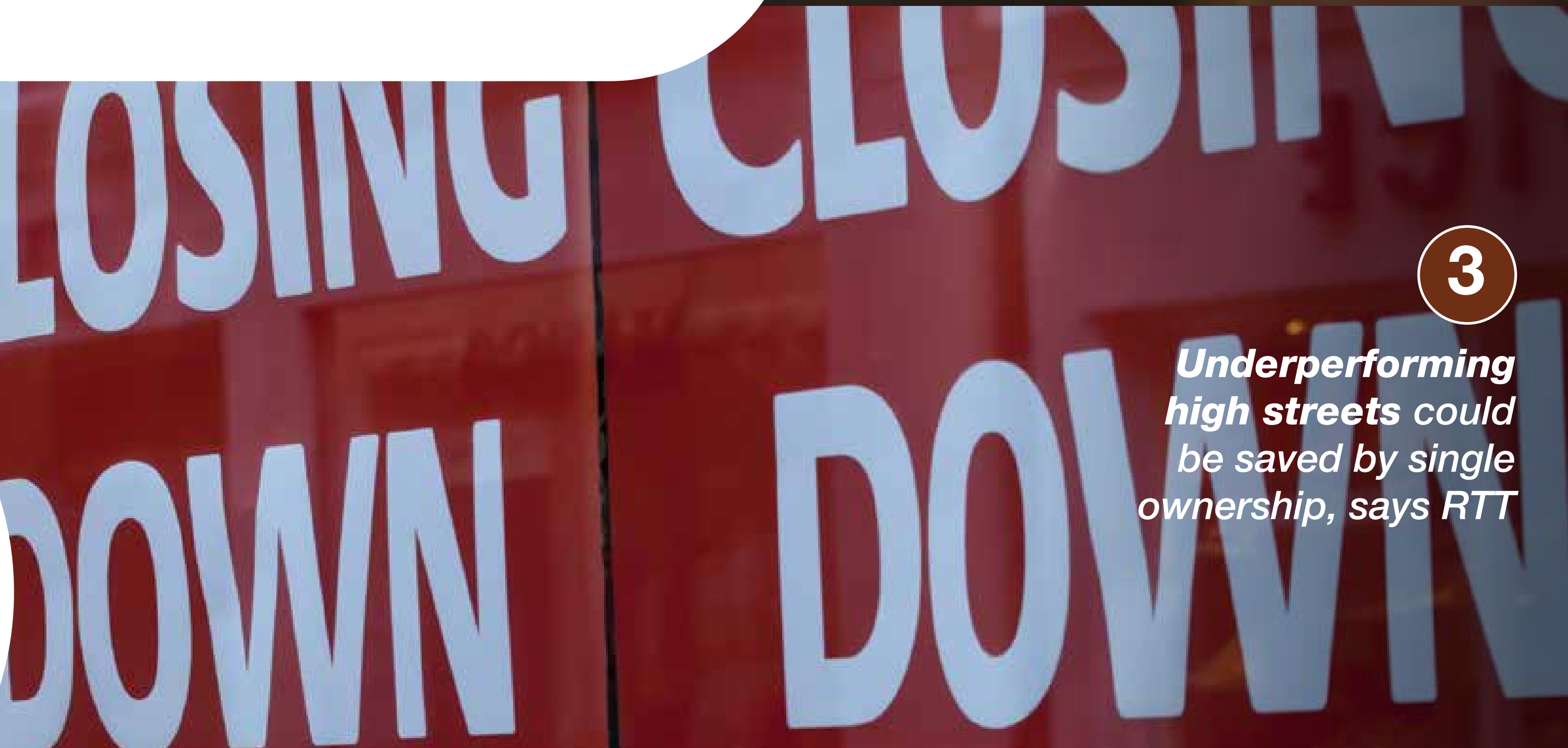
white papers

1

*Life after the **food contamination** crisis*

2

*How will **demographic trends** in the UK affect the retail sector?*



3

***Underperforming high streets** could be saved by single ownership, says RTT*

1

life after the food contamination crisis

– how closely should retailers vet their suppliers' sourcing? Where does the ultimate responsibility for consumer safety lie?

Part I:
Executive Summary

The contamination of the beef supply chain with horse meat is a stark illustration of the risk of supply chain failure and should serve as a wakeup call for all retailers, not just those in the food sector.

The KPMG/Ipsos Retail Think Tank ('the RTT') met in April to consider the implications of the horse meat contamination scandal for the retail industry and to ask how closely should retailers vet their suppliers' sourcing? Where does the ultimate responsibility for consumer safety lie?

The horse meat scandal:
This isn't a safety issue, it's one of trust

As Nick Bubb, Retail Analyst, notes, **"It's a funny kind of food "crisis" when nobody dies or is even reported unwell after eating the affected products".** Despite the fact that testing has confirmed that the risk to consumers' health is extremely low, the recent horse meat contamination saga has captured the nation's imagination through the media coverage and sparked widespread fears about the vulnerability of UK food supply chains.

Richard Lowe, Head of Retail and Wholesale at Barclays, says: **"This is not only an emotional issue but one of trust too. Consumers rightly expect a certain standard, and when those retailers they choose to shop with fall short, there is a clear expectation that these businesses need to address the root causes of these issues as soon as possible. In this case, we saw many retailers respond quickly and provide their customers with updates, whether by email or in store, and they are working to restore that trust, particularly around the security of the supply chain."**

The RTT agree that retailers need to urgently rebuild consumer trust in their products and the security of their supply chains.

Neil Saunders, Managing Director at Conlumino, says: **"This wasn't really about safety. The problem was people had been mis-sold something, and felt misled. The adulteration of meat left many consumers highly uncertain about what they are eating; if products contain extraneous horse meat, they ask, what else might be hiding within?"**

"This erosion of confidence has serious implications for both the retail and food processing industries. Consumers have already reacted swiftly, ditching brands and products tainted by the scandal, with many rediscovering the local butchers they once abandoned in favour of the big supermarket chains. As new developments come to light, we should expect to see habits change still further."

Cause and effect:
The crisis is a consequence of behaviours within the industry

The RTT believes that the food contamination crisis is linked to the pressure on retailers to cut costs and deliver the cheapest possible product, leading to complex, opaque, supply chains.

The RTT notes that this move to slash costs has been partly driven by consumer demand and shopping behaviour. As economic hardships hit consumers' pockets, many sought to make savings in their weekly shop, choosing the cheapest possible product. This led retailers to compete vigorously against each other on price.

Martin Hayward, Founder of Hayward Strategy and Futures, said: **"There has been a relentless pressure to focus on price at the expense of quality at the lower end of the retailing market. It is perhaps unrealistic for consumers to expect to be able to eat or dress themselves so cheaply, but they have been led to believe it is possible by purveyors of 'value' products in the food and clothing chains. For these value propositions to be maintained, there is great pressure on the retailers to source cheaper ingredients and products, inevitably leading them to less controlled markets and suppliers around the world with concomitant cheaper labour costs."**

The RTT notes that improving the traceability of food could add exponentially to the overall cost of the product, and it was doubtful that this price would be swallowed by the consumer.

David McCorquodale, UK Head of Retail at KPMG, says: **"The crisis won't have a bearing on the cost of food. Low cost food is here to stay. However, it's surprising how far food chains stretch across the globe, especially as these chains are for established products, so they really should be as short, and as efficient, as possible."**

However, the scandal has prompted a degree of switching behaviour. Tim Denison, Director of Retail Intelligence at Ipsos notes that the value grocers like Tesco and Aldi have lost market share in the short term as consumers changed their buying habits and shopped at places like Morrisons and Marks and Spencer's, who are seen as trusted sources.

In the long term it is unlikely that all consumers will stop buying low cost, processed food. As Nick Bubb, retail analyst, explains: **"In the past, the impact of food scandals has always been short-lived, so it will be interesting to see how long this market share shift to quality operators will last, or whether it simply reflects the relative affluence of their customer demographic."**

The RTT also believes that the crisis could have been caused by a breakdown in relationships between retailers and suppliers. The crisis has shifted the balance of power away from retailers to those companies that supply them, and highlights the importance of having better quality suppliers. **"If retailers squeeze their suppliers too far on input pricing then suppliers will find ways to get some money back by cutting quality"**, explains Nick Bubb.

"The best supplier relationships are built on long-term partnerships and shared interests in a fair distribution of risk and reward."

Finding a solution:

Complex and opaque supply chains need to be tackled

The RTT says that for some retailers supply chain complexity has reached unprecedented levels. In recent years, financial pressures have driven many companies to cut costs as much as possible and take greater risks in their supply chains, often without undertaking a full assessment of what these risks really entail. This drive to cut costs through the supply chain can have unintended consequences. As buyers cut costs, suppliers are forced to reduce controls to protect margins, increasing the risk of supply chain failure.

The RTT believes retailers have a duty to assure their supply chain for their end consumers, place renewed focus on supplier risk management and ensure the necessary checks and controls are in place.

The Group advises retailers to shorten their supply chains to improve visibility of the end to end process. **"The food contamination crisis has shown how hard it can be to keep a close eye on every stage of the supply chain",** says Vicky Redwood, Chief UK Economist at Capital Economics. **"This has arguably become more difficult with the proliferation of outsourcing to far-flung countries in order to take advantage of cheaper material and production costs overseas. This should prompt a wider rethink of supply chains and encourage retailers to reduce the length and complexity to increase provenance."**

Tim Denison of Ipsos adds: **"A more elegant solution could actually introduce cost reductions. Simplifying chains to fewer players, building stronger end-to-end supply relationships and establishing shared responsibilities to deliver traceable food that ends up on the consumer's table brings with it a sense of back to old fashioned basics; and what's wrong with that? This can mean a return to local sourcing, for processed as well as primary foodstuffs, something in which shoppers have new found interest. Waitrose is already going down this path. Its ready meals are predominantly own-brand from authenticated direct sources and those that aren't come from smaller UK suppliers, with simpler supply chains."**

The Group suggests that retailers try to take steps to develop stronger collaboration with suppliers in order to strengthen relationships with them and build trust. This could take the form of putting in place long term contracts with suppliers. Such a collaborative approach could ensure that risks are reduced and governance is better.

However, the RTT acknowledges that the elimination of risk is impossible, and external factors like natural disasters or being targeted by fraudsters will always be possibilities retailers must plan for. Mark Teale, Head of Retail Research at CBRE says: **"With thousands and thousands of food lines, it is simply not possible to guarantee that the food chain will not be contaminated. A bit like drugs testing in sports, spot checks as a deterrent are the best you can do. Much more than that and the process becomes so onerous that it becomes counter-productive. At the end of the day, as with so many other things, you have to rely largely on trust. There will always be rogue manufacturers."**

Some cross contamination will always exist – labelling isn't the silver bullet

The RTT believes that labelling products with further disclaimers is not the answer to this crisis.

"Yes, retailers could simply make their product descriptions more vague', says Vicky Redwood of Capital Economics, **"but obviously this would compromise consumers' perceptions of the quality of the products and could dent consumer demand. Retailers may do better to appeal to consumers by improving – and advertising – the guaranteed provenance of their products."**

The RTT notes that eliminating cross contamination is nigh on impossible, because very few processing plants are dedicated to producing just one product, and may have different types of meat flowing down their lines and through their machines. This means that from product to product, a minor level of contamination will always exist. The RTT concludes that labelling should not list the other products being made in the same plant, nor attempt to detail the permutations of possible cross contamination.

"This would lead to longer and longer disclaimers, like medicines," says Mark Teale of CBRE. **"It's easy to overreact and label extensively and pass the buck onto your suppliers but in reality risk has to be solved with better trust between the retailer and the supply chain."**

The RTT believes that increased regulation would not increase safety, but would give consumers a false sense of security. David McCorquodale of KPMG says: **"Retailers need to look at their own corporate governance and check their controls. Their reputation is on the line and they will care more about protecting it than an inspector from a regulator. After all these scandals cost them money and hit their profitability. Labelling should be about safety and warning people with allergies if the product might not be suitable for them. Instead of increasing labelling, retailers should be encouraged to spend their time better assessing the risks in their supply chain and repairing any weaknesses."**

The RTT instead suggest that current regulation, such as the Trade Descriptions Act, should be vigorously, and publicly, enforced to deter fraudsters targeting food chains.

Conclusions:
life after the horse meat contamination crisis

It's six weeks on from the scandal and it's foot on the ball time. The RTT concludes that while retailers have reacted swiftly to remove the products from the shelves and begin testing, a cohesive strategy outlining steps the industry needs to take to shore up the safety of the supply chains is needed.

The RTT agrees that retailers are ultimately responsible for what they stock on their shelves and sell to consumers. While the horsemeat contamination was caused at a supply level, retailers still have a responsibility to assess the risks in their supply chain, and put appropriate controls in place.

There will be debate around how far the industry will push on the issue of controls and how far regulators will pull.

David McCorquodale of KPMG believes it is essential that the industry is on the front foot: **"Retailers need to lead the debate and take decisive action as an industry on labelling and managing supply chain risk or they will be frogmarched down the wrong path by regulators."**

Neil Saunders of Conlumino adds that it is in retailers' financial interests to tackle the problem head on: **"If retailers see the effect on their bottom line they will take action. The market is self correcting. They fear losing share and so they will look at solutions, including those retailers unaffected this time."**

Part II:

In detail – Individual views of the RTT members

Nick Bubb, Retail Analyst:

It's a funny kind of food "crisis" when nobody dies or is even reported unwell after eating the affected products, but the recent horse meat scandal has caused some interesting shifts in consumer perceptions of supermarkets and in the balance of power between suppliers and retailers.

One message from the recent scandal was that "you get what you pay for", with the problems concentrated at the bottom/cheap end of the market for meat products. The better quality supermarkets like Sainsbury's, Waitrose and M&S seem to have done well out of their focus on food provenance, as has Morrison's, with its control of its own supply chain. In the past, the impact of food scandals has always been short-lived, so it will be interesting to see how long this market share shift to quality operators will last, or whether it simply reflects the relative affluence of their customer demographic.

Another message, however, from the recent horse meat scandal was that if retailers squeeze their suppliers too far on input pricing then suppliers will find ways to get some money back by cutting quality, so supermarkets shouldn't get too hypocritical and affect to be shocked at what some of their more shady suppliers have been up to. The best supplier relationships are built on long-term partnerships and shared interests in a fair distribution of risk and reward. In the same way, clothing retailers should be careful that the arbitrary imposition of retrospective discounts to payment terms doesn't result in a similar lowering of quality standards by clothing suppliers...

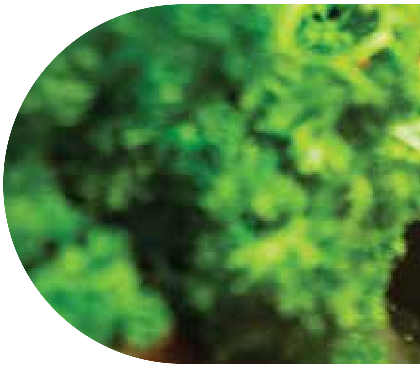
Richard Lowe, Head of Retail and Wholesale at Barclays:

Since the horse meat scandal broke, I suspect many of us have shared the same niggling doubts as to whether we too are among the millions of unwitting victims of horse-gate. One thing which is in no doubt is the need for retailers to overhaul their supply chains in its wake and, to the industry's credit many have already made public pledges to do so.

As the final link in the supply chain, retailers should be vetting their suppliers' sourcing vigorously to ensure the provenance of all their products. Some have already taken steps to shorten their supply chains, or brought them closer to the UK so that in future they can confidently confirm the origin of the goods sold in their stores. The bond between the consumer and retailer is crucial and the horse meat scandal has highlighted the damage which can be caused to retailers when supply chains aren't rigorously managed.

As to where the responsibility for consumer safety lies - this has not been about consumer safety per se. To date there is no evidence to suggest eating horse meat is unsafe. However, unlike many European countries, eating horse meat remains a taboo subject at British dining tables. Therefore, as the last link in the chain, retailers are ultimately responsible for what they stock on their shelves and for easing consumer concerns as to where it has come from.

This is not to say consumers are to be absolved of responsibility. With household budgets under significant pressure there is a natural inclination for shoppers to trim costs wherever possible. While food is not a luxury item it now accounts for more than 40 per cent of all retail spend according to the Office for National Statistics and is, therefore, an obvious target for thriftiness. Consumers are rightly outraged at the horse meat scandal but, will they be willing to pay more at the checkout for their shopping in these straightened times – only time will tell.



Neil Saunders, Managing Director at Conlumino:

The essence of the horse meat crisis is one of trust. The adulteration of meat has left many consumers highly uncertain about what they are eating; if products contain extraneous horse meat, they ask, what else might be hiding within?

This erosion of confidence has serious implications for both the retail and food processing industries. Consumers have already reacted swiftly, ditching brands and products tainted by the scandal, with many rediscovering the local butchers they once abandoned in favour of the big supermarket chains. As new developments come to light, we should expect to see habits change still further.

Retailers will be thankful for the fact that the crisis is of such scope and scale that blame has been dispersed over a wide area with no one in particular in the crosshairs. However, this does not mean that it is a non-issue; consumers expect action to be taken and for someone to take responsibility to ensure that problems are remedied. As the final link in the supply chain, retailers must bear the ultimate responsibility for what is sold. Most have done just that; there has been very little ducking and diving within the industry.

However, this sense of responsibility must also extend to actions. The pressure retailers exert to trim every possible cost is enormous and the whole supply chain from farm to fork is now so tight that it was probably only a matter of time before a crisis arose. In other words, this is more than an accident; it is a direct consequence of the behaviours within the industry. That's what needs to change.

However, there is arguably another actor who is also liable: the consumer. Buying food is not discretionary; it's something we all need to do, and do regularly. As such, it accounts for a very large proportion of all that we spend on retail. If we can reduce the amount we spend during our weekly grocery shop then we have more scope to buy other more exciting consumer goods; so, many of us happily laden up our trolleys with value ready meals and cheap cuts of meat in order than we can shave a bit off our bill. How many of us, though, really thought about that 99p ready meal and asked "is this really too good to be true?" The answer is not nearly enough of us.

None of this is to excuse retailers or manufacturers, but it does open up an important question about the current realism in terms of economics within the food industry. Part of solving this matter and guaranteeing, as far as possible, food which is free from contaminants has to be the acceptance of higher prices. Notably, when we talk about higher prices we are not talking about massive hikes but a few pence here and there. Certainly, that's unwelcome in the current economic environment but it is a necessary price to pay.

Will consumers wear it? Their reaction to horse meat suggests that they probably might. The fact that many are already buying more expensive foods or using butchers which charge a little more suggests there has been a subtle shift in attitude. Will retailers wear it? Arguably they should; being the cheapest at all costs may well bring some short term market share gains, but if it ultimately undermines long term confidence in the brand it becomes something of an own goal.

The bottom line is that when it comes to food prices the old farming adage is as true now as it ever was: you reap what you sow.

Vicky Redwood, Chief UK Economist at Capital Economics:

Of course no retailer would want to deceive consumers deliberately (we hope!). However, the food contamination crisis has shown how hard it can be to keep a close eye on every stage of the supply chain. This has arguably become more difficult with the proliferation of outsourcing to far-flung countries in order to take advantage of cheaper material and production costs overseas. Food contamination is just one example – the use of child labour is another recent example.

It is retailers' responsibility to sell consumers the goods consumers are told they are buying. Of course, this is of most importance when questions of consumer safety are at stake. The food contamination crisis is slightly different in that horse meat itself is not dangerous. But of course, the question is, if horse meat can get into food products unknowingly, what else can? Indeed, one supermarket recently had to withdraw food for being contaminated with veterinary medicine.

So how will, and should retailers, respond? They could of course simply make their product descriptions more vague. Take peanuts. Rather than making 100% sure that peanuts are not included in products, retailers usually just write "may contain peanuts" on the packaging to shift the responsibility to the consumer. So maybe we will now see more "meat lasagne" rather than "beef lasagne"! But obviously this would compromise consumers' perceptions of the quality of the products and could dent consumer demand. And appetite for ethical products has been growing, suggesting that retailers may do better to appeal to consumers by improving – and advertising – the guaranteed provenance of their products.

Accordingly, retailers will have no choice but to take more care in controlling the supply chain, and facing up to the fact that cheap outsourcing may not be the free lunch it may have appeared to be in the past – reducing costs without much extra expense. In the extreme, all of this could mean bringing back production to where it can be more closely supervised - which would involve higher costs for consumers.

Mark Teale, Head of Retail Research at CBRE:

The only obvious way of improving food vetting is to increase the level of third-party testing. In practice the range of packaged/processed mass-market food products is so large that across-the-board testing is simply a non-starter. At best, testing will continue to be limited to areas where there is a suspicion of adulteration or where adulteration has occurred in the past.

At the end of the day, as the retailer is the point of sale, it is the retailers' responsibility to ensure consumer safety. In practice, with thousands and thousands of food lines, it is simply not possible to guarantee that the food chain will not be contaminated. The same is true in non-food markets. It is not possible to guarantee that all goods supplied meet the manufacturing/employment age/conditions criteria that we consider essential. A bit like drugs testing in sports, spot checks as a deterrent are the best you can do. Much more than that and the process becomes so onerous that it becomes counter-productive. At the end of the day, as with so many other things, you have to rely largely on trust. There will always be rogue manufacturers.

Scandals will continue to occur, like the horse meat contamination (and salmonella in eggs incidentally: in the UK many years ago and much more recently in the US), but there is little evidence that contamination is a significant issue with processed food per se: health risks attaching to processed food generally (sugar, salt obesity etc) are clearly a much bigger issue than the periodic contamination found in individual food lines.

Martin Hayward, Founder of Hayward Strategy and Futures:

There is no doubt that consumers have been shocked to find that products they have been buying do not contain what the packet says they do.

At the heart of the matter lies the perceived relentless pressure to focus on price at the expense of quality at the lower end of the retailing market.

It is perhaps unrealistic for consumers to expect to be able to eat or dress themselves so cheaply, but they have been led to believe it is possible by purveyors of 'Value' products in the food and clothing chains.

For these value propositions to be maintained, there is great pressure on the retailers to source cheaper ingredients and products, inevitably leading them to less controlled markets and suppliers around the world with concomitant cheaper labour costs.

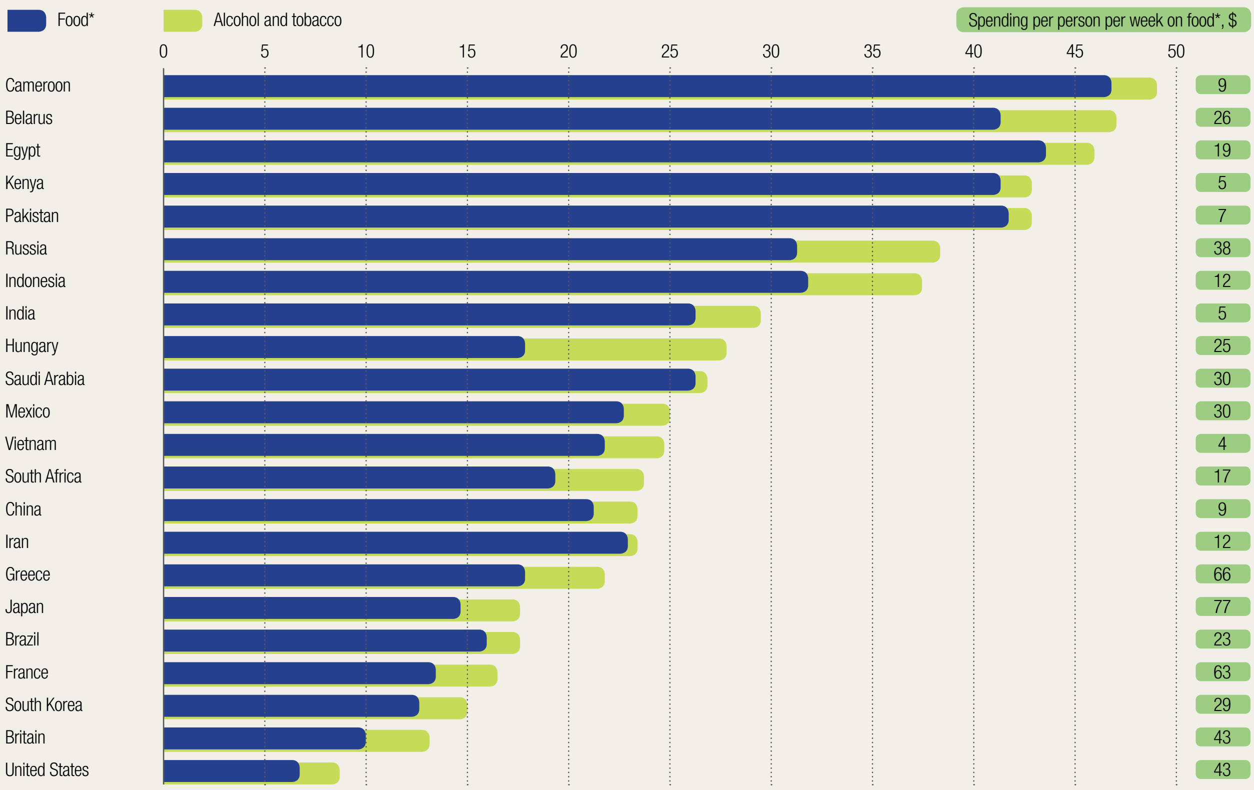
Food costs actually represent a small proportion of household expenditure compared to historically, and to continue to aim to reduce it further has led to the complex and hard to regulate sourcing policies uncovered by the recent contaminations. (The richest countries also spend the smallest percentage of income on food).

It has been rather bewildering, but certainly good news for UK farmers and consumers, to see some retailers suddenly discovering a passion for UK sourced product, not perhaps because they believe it is right because they would surely have done it years ago if that were true, but because they feel have to.

In a recessionary environment, it is harder than ever to put ethics and provenance ahead of price, but the performance of those food retailers who have adopted this position, goes some way to show that the consumer perhaps has a better understanding of the trade-offs involved than they are given credit for.

Spending on food and drink

Selected countries, 2011, % of total household spending



Source: US Department of Agriculture

* Includes non-alcoholic beverages

Tim Denison, Director of Retail Intelligence at Ipsos:

It's easy to overplay the "horse meat" scandal. The fact is we have a good track record on food quality matters in this country; certainly compared to the likes of China, for example, whence I have recently returned amidst reports of another break out of bird 'flu in poultry and a boat of contaminated dead pigs found floating down the Yangtze.

Let's be clear. The weakness that the recent saga exposes is not about the two ends of the supply chain - the farmer and retailer, it is all about the filling in the middle of the sandwich – the processors, food manufacturers and packagers.

Some argue that food quality standards became compromised when an EU directive scrapped daily abattoir inspections in 2006. I'm not interested in blame, but solutions. The current European legislation requires companies to have proven traceability of content and origin back to the previous stage in the food chain. This dictat is fallible, as some retailers have recently experienced to the detriment of their market share. The system neither provides end-to-end proof of authenticity and source origin, nor any requirement for physical inspection: it purely hangs on a paper-based trail of documentation.

In these times of austerity, when the financial strain on the chain is ever tightening, the quest for cheaper sources often leads companies to explore overseas supplies, involving passage through more pairs of hands, weakening traceability and risking product substitution.

The solution is less obvious. End-to-end traceability is technically possible, but it would involve significant cost to a market already under severe cost pressure. The expense would not be so much in the electronic tagging of the produce itself, but in the data management system and its integration into existing supply chain systems such as warehousing. A cheaper option, though still costly, is testing for product contamination, which, to its credit, Sainsbury's introduced at its expense a decade ago with DNA sampling. It is testament to the solution that Sainsbury's has emerged unscathed from recent events.

A more eloquent solution though could actually introduce cost reductions. Simplifying chains to fewer players, building stronger end-to-end supply relationships and establishing shared responsibilities to deliver traceable food that ends up on the consumer's table brings with it a sense of back to old fashioned basics; and what's wrong with that? This can mean a return to local sourcing, for processed as well as primary foodstuffs, something in which shoppers have new found interest. Waitrose is already going down this path. Its ready meals are predominantly own-brand from authenticated direct sources and those that aren't come from smaller UK suppliers, with simpler supply chains.

End-to-end traceability in the food industry is inevitable one day, I'm sure. It works splendidly in the motor manufacturing industry, increasing safety through enabling targeting product recalls and reducing costs. But its time in the food sector is not yet. Some retailers are already showing perfectly well how to be responsible and responsive to quality management without introducing unjustifiable additional cost. It's now down to the others to step up to the mark and strengthen their means of authentication of source of origin and so improve the appeal of their "sandwich filling".

David McCorquodale, UK Head of Retail at KPMG:

At first it was headline grabbing, press inflamed horror. How am I eating horse meat? What's a Cypriot middle-man doing in the supply chain? What else can there be in a beef lasagne? Who can I trust anymore? Not one of the retailers could stand tall in the immediate aftermath and say they were unaffected. It was clear that something was amiss and, whilst fraudulent practices may have been around, the episode has exposed too many risks in long and complex global supply chains. Change is needed.

The industry, retailers and manufacturers and regulators alike, coped well in the immediate aftermath, with good cooperation and swift testing, with the 1% threshold holding up adequately. However, the retailer, being the main party at the apex of consumer trust and brand reputation, needs to drive that change. It is the retailer after all who establishes the 'deal' with the consumer through the 'contract' on the label and who takes the consumer's cash.

The complexity of the food supply chain came as a surprise to the public. From farm to fork there has been a lack of consistency in the way produce has been monitored, creating black holes in the supply chain that enable unscrupulous or desperate parties to cut corners or sabotage products. From conception to consumption there can be more than 450 critical steps as produce finds its way from field or sea via the abattoir, dairy and storage silo, through the processing plant to the packaging facility and the supermarket shelf. Along this chain, managers have to assess and control risk.

Change is inevitable. Supply chains must be shortened to reduce risk, which may bring more processing back to the UK. Greater collaboration and perhaps even longer term contracts between retailer, manufacturer and farmer may emerge to enable investment and guarantee availability. Regulation is inevitable and the food industry must participate in this. The dairy industry has demonstrated the advantages of consolidation, and the meat industry may have to follow suit even if this clashes with the desire for smaller, identifiable local farmers. Whilst costs associated with compliance and assurance will increase, I suspect this will not be passed to the consumer. Efficiency and security will need to fund themselves.

Lessons can be learned from other industries. The pharmaceutical and automotive industries are best in class for traceability and risk control. Imagine the uproar if a brake pad had the rubber equivalent of horse meat in it on a motor car! Key for the consumer is trust and retailers need that to maintain reputation.

– 2/3rds of retail spending growth will come from shoppers aged 55 plus

– Ageing population will transform not only the face, but the role the high street plays in society

How will demographic trends in the UK affect the retail sector?

2

Part I:
Executive Summary

With a rapidly ageing population and migration trends changing the ethnic makeup of our cities and towns, UK shopping habits too are beginning to evolve and reflect these wider demographic changes.

The KPMG/Ipsos Retail Think Tank ('the RTT') met in July to consider the implications of these demographic shifts for retailers. Should retailers adapt to meet the population's changing needs?

David McCorquodale, UK Head of Retail at KPMG explains: **"The changing demographic profile of the UK is a major influence on consumer purchasing power, shopping behaviour and shopping preferences. The age structure, ethnicity, household composition and demographic distribution of the UK population are all undergoing significant change and its implications are important for retailers to understand and anticipate."**

Over the next ten years two-thirds of all retail spending growth will come from those aged 55 and over

Vicky Redwood, Chief UK Economist at Capital Economics, believes that the main challenge facing retailers will be to adapt to the UK's ageing population and get to grips with their specific tastes and demands. She says their influence will be significant: **"By 2030, the number aged 65 or older is projected to reach 15.5m, growing 43% on its level in 2012, compared to an expansion of only 13% in the population as a whole. While this group currently accounts for less than £1 in every £5 of total spending, this share might rise to £1 in every £4 within two decades."**

The rising influence of this group could see sales shift towards the categories and methods of shopping that they favour. Health, DIY and home maintenance retailers, which attract a large share of elderly households' budgets, should benefit from this change, whereas retailers selling clothing, beer and soft drinks, which are geared towards a more youthful market, could lose out.

An ageing population could also reshape the UK's high street. **"I expect not just the face but the role of the high street to evolve to meet the needs of this ageing population,"** says Richard Lowe, Head of Retail and Wholesale at Barclays. **"We have already begun to see some forward thinking town planners break with tradition and incorporate services and local amenities into the traditional high street. GP surgeries, libraries and other health services have begun to pop up in between convenience stores and chemists whereas traditionally they have been set back from the main thoroughfare. These act as a draw for the older generation who are less inclined and perhaps less able to travel for their groceries but still need to access essential local services. Transport, accessibility and local infrastructure will therefore become increasingly important."**

What does this mean to retailers? The Group believes that retailers must rethink store design, marketing and advertising campaigns to attract the grey pound and above all understand these are older consumers who still think of themselves as young consumers.

Neil Saunders, Managing Director of Conlumino, adds: **"The baby boomer generation has no intention of retiring quietly to a life of crochet and gentle gardening. They are down-ageing: acting younger, both physically and mentally. Understanding this is important because it's this older segment that's going to drive retail over the next ten years. An ageing population profile, helped by lower birth rates, longer life expectancy and the sheer size of the baby-boomer generation – many of whom are now retiring – are just three factors underpinning this trend. As a result, we estimate that over the next ten years almost two-thirds of all retail spending growth will come from those aged over 55."**

Retailers must also remember that not all baby boomers are awash with disposable income. Independent retail analyst Nick Bubb says: **"Conventional wisdom paints a rosy picture of a growing number of affluent retired couples with plenty of time and money to spend, but the reality for many is rather different. With ultra-low interest rates and annuity rates, pension income is under considerable pressure, forcing many older consumers back onto the part-time job market to supplement their financial resources. And one painful consequence of people living longer is that many older consumers have the cost of looking after their own parents to consider. And their own children may not find it easy to get full-time jobs in a continuing climate of financial austerity."**

The importance of the social aspect of shopping to this age group should also not be underestimated. Martin Hayward, Founder of Hayward Strategy and Futures, says: "**I have often asked 'Why do pensioners go shopping on Saturdays?' Clogging up the stores with their silly trolleys when they could easily go on Wednesday morning when there's nobody else about. They do it because that's when everyone else goes shopping, because the buzz of the market place is central to our human needs to forage and interact."**

The rise of **Generation Y**

The rising influence of so-called "Generation Y", who are generally considered to be the under 30 to 35s is also having a major impact on retailers and their future strategy.

"This group is overtaking the baby boom generation in terms of their size", says Vicky Redwood of Capital Economics. **"Not only does this group desire different products from previous generations, but it has different ways of shopping and different attitudes to brands. Obviously the changes already underway – such as multichannel retailing – will particularly appeal to this generation."**

David McCorquodale of KPMG added: "**The number of children aged 16 and under is projected to increase by 12% to 13 million by 2035 benefiting the infant and children's sector."**

This means a difficult balancing act for retailers. Whilst tackling the demands of the baby boomers, retailers must look at the other end of the age spectrum and work out how to attract the interest, and spending power, of the younger generation.

Shift in Britain's multicultural make up

The RTT believes that those retailers that successfully understand and target the shifting cultural makeup of Britain will outperform those using antiquated research and customer stereotypes.

Understanding migration trends is of utmost importance for those retailers operating in London. Figures from the Office for National Statistics show that in the year to 30 June 2012 a third of migrants entering the UK headed to the capital city, demonstrating the city's rapidly changing ethnic profile.

"Traditional social and racial stereotyping still prevails in most marketing studies, but half the babies born in London are now to non-indigenous UK mothers, so marketing and advertising campaigns need to adjust to the fact that the target market is changing, just as many supermarkets now sell Polish and Asian specialty foods," says Nick Bubb. **"As our big shopping centres embrace a "wifi" world they will also need to weigh up the kind of shops and facilities that a less young and a less "English" population will need in the next decade."**

Whilst a rise in ethnic communities, particularly in urban areas, is leading to increasing diversification, this differs from region to region and retailers must consider regional demographics when allocating products across their store networks. **"There is no "one size fits all solution" here"**, warns David McCorquodale of KPMG.

The modern approach to property

While demographic shifts happen very slowly, shopping patterns are constantly changing due to development activity. **"The development of new shopping space – shopping centres, retail parks, factory outlets, retail parks, superstores et al – has had a major impact on where consumers choose to shop, regardless of demographics, and will continue to so in the future. What age change is doing however is strengthening demand for both improved shopping environments and better service/accessibility: older shoppers are far more demanding than the young,"** says Mark Teale, Head of Retail Research, at CBRE.

"The last 20 years has seen a steady reduction in non-food chain size as retailers have sought to concentrate their retailing activities in larger branches in dominant markets. This relentless network contraction has left a long tail of obsolete small-unit High Street shops in its wake. Half the population now shop for comparison goods in just ninety or so major trading locations nationally, down from over 200 in 1971. This steady market concentration has gone hand-in-hand with the homogenisation of offers in large dominant centres simply because mass market non-food retailers are all chasing space in the same places."

And this trend for smaller, more strategic, property portfolios looks set to continue. **"Retailers (particularly fashion retailers) are now reporting plans to further top-slice consumer markets, concentrating networks in just 150 or so of the largest centres, instead of following the traditional route of aiming for deep local market penetration via many hundreds of branches. 'Click and collect' activity is doing the same,"** reveals Teale.

But this trend is not being followed by convenience goods retailers. Grocers are following a completely different strategy, consolidating network penetration by opening large numbers of small convenience goods branches, as well as superstores, increasing rather than reducing branch network sizes. Adapting merchandise offers to meet gradual demographic change is a lot easier than keeping step with underlying shopping pattern change.

Technology will continue to play a pivotal role

Technology will continue to play a pivotal role in shaping the way consumers shop and how retailers can communicate and market to them. **"In some ways, the boom in the take-up of smartphone and tablet device technology (and the related explosion in the power of social networking) is a bigger influence on the pattern of retail spending than demographic change",** says Nick Bubb.

However, retailers must also be careful not to alienate certain demographics through an over reliance on technology. Martin Hayward of Hayward Strategy and Futures says: **"There is potential for many older consumers to be disenfranchised by a rapid rush towards new technology in retail by some players, without clear thought as to the needs of those who choose, or are unable, to embrace it.**

"Retailers must ask themselves to assess both the efficiency and the effectiveness of new technologies in the value chain if they are to enjoy the many benefits that it can bring. A good example is self-scanning technology in convenience stores - many love it, yet many, particularly older consumers, hate it. The answer has to be therefore to offer both options, not to insist on consumers using technology if they don't want to."

Conclusions:
How will demographic trends in the UK affect the retail sector?

The RTT believes that retailers will need to work much harder to understand customers and target ranges and products much more sensitively. That means greater segmentation, much better use of tools like sub-branding and much more clarity in offers on shop floors and websites. Over the next ten years, this fragmentation of consumer types will most likely mean that personalisation becomes an increasingly important watchword.

"Nowadays there's no such thing as an 'average consumer'; there is no universal," says Neil Saunders of Conlumino. **"What we have instead is a mosaic of minorities: lots of different tribes of people, with many people often belonging to more than one tribe. And for retailers and marketers making assumptions about a person from their looks, gender or age can be extremely dangerous. Reaching a mass market is much more difficult because there is no mass, homogenized market to reach."**

However, retailers have time on their side to plan for, and adapt to, the changing face of Britain. Demographic change happens slowly and can be anticipated, analysed and understood. This is a fundamental difference between it and the other challenges facing retailers in a competitive market place, which happen much faster, for example the effect on shopping behaviour caused by new technology. These can mean significant capital expenditure is suddenly required, which can catch businesses out.

Richard Lowe of Barclays says: **"The implications of an ageing population are clear for all to see, so provided the sector continues to evolve in line with these shifting demographics and consumer spending patterns, retailers won't find themselves asking where all their customers have gone in years to come."**

David McCorquodale of KPMG says: **"In summary, the evolution in demographics impacts product, space, offering and packaging and those retailers who monitor trends and adapt their offering will be best placed to benefit from the changes."**

The RTT warns that traditional retailing and its hard learned values still have a central role to play and social interaction in stores and good quality customer service will remain important. Martin Hayward of Hayward Strategy and Futures: **"There can be a tendency in society at large and the retail sector as well, to chase the novel at the expense of the proven, the new at the expense of the old. As has been said many times, there is also a natural inclination to initially over-estimate the impact of new technology, yet to underestimate it in the longer term."**

"Efficiency should always be sought in retail, but your older shoppers and maybe your younger ones as well will still value the human touch. Remove it at your peril."

Part II:

In detail – Individual views of the RTT members

Vicky Redwood, Chief UK Economist, Capital Economics

The main challenge for retailers will be adapting to the ageing population. By 2030, the number aged 65 or older is projected to reach 15.5m, growing by 43% on its level in 2012, compared to an expansion of only 13% in the population as a whole. While this group currently accounts for less than £1 in every £5 of total spending, this share might rise to £1 in every £4 within two decades.

Health, DIY and home maintenance, which attract a large share of elderly households' budgets, should benefit from this change. Clothing, beer and soft drinks, which are geared towards a more youthful market, could lose out. All retailers will have to make changes, though. Store design, marketing and advertising will all have to be rethought to make the high street more appealing to an older demographic. Above all, there will be the challenge of appealing to older consumers who still think of themselves as young consumers.

At the same time, retailers will also need to appeal to so-called "generation y" – generally considered to be the under 30 to 35s. These are overtaking the baby boom generation in terms of their size. Not only does this group desire different products from previous generations, but it has different ways of shopping and different attitudes to brands. Obviously the changes already underway – such as multichannel retailing – will particularly appeal to this generation.

The third challenge will be reacting to the more multicultural nature of the population. 15% of the UK population was not born in the UK. Even if the government succeeds in slowing net migration, births to immigrant mothers are rising. The most successful retailers could be those managing to blend the general and multicultural markets.

The general rise in the birth rate in recent years – after a period of decline – will open up further opportunities for retailers in the baby and children markets. And finally, the rise in female participation in the labour market probably has further to go, given female participation in the UK is still lower than in some other developed economies. Retailers will therefore have to respond to this rise in women's disposable incomes.

Neil Saunders, Managing Director, Conlumino

Understanding shoppers is not easy.

Fifty or so years ago it was much easier to categorize people – mainly because things were much more uniform and people behaved according to accepted norms and traditional stereotypes. These days, consumers misbehave and do completely unexpected things.

Yesterday, people acted their age. The aged grew old gracefully. Many of the older generation of today, those who are 75 or over, still conform to this norm. But the baby boomer generation has no intention of retiring quietly to a life of crochet and gentle gardening. They are down-ageing: acting younger, both physically and mentally.

Understanding this is important because it's this older segment that's going to drive retail over the next ten years. An ageing population profile, helped by lower birth rates, longer life expectancy and the sheer size of the baby-boomer generation – many of whom are now retiring – are just three factors underpinning this trend. As a result, we estimate that over the next ten years almost two-thirds of all retail spending growth will come from those aged over 55.

It's not just age that's more complex either. The same goes for lifestage. People no longer follow predictable patterns. We have a diversity of household types and of family structures. Income and social class is also much more complex. Yesterday it was very easy to predict where people would shop based on their class and income. Today, the old rules don't apply: consumers are shopping at both premium and value ends of the market irrespective of income or social background.

Gender too has changed. Females are now more empowered that they used to be and men, especially younger men, are much more interested in retail sectors that were traditionally the province of women - as the rapid growth of men's personal care attests.

So nowadays there's no such thing as an 'average consumer'; there is no universal. What we have instead is a mosaic of minorities: lots of different tribes of people, with many people often belonging to more than one tribe. And for retailers and marketers making assumptions about a person from their looks, gender or age can be extremely dangerous. Reaching a mass market is much more difficult because there is no mass, homogenized market to reach.

The upshot of all of this is that retailers need to work much harder to understand customers and, in so doing, they probably need to target ranges and products much more sensitively. That means greater segmentation, much better use of tools like sub-branding and much more clarity in offers on shop floors and websites. Over the next ten years, this fragmentation of consumer types will most likely mean that personalisation becomes an increasingly important watchword.

Ultimately, those that succeed will be the ones closest and most responsive to their customers.

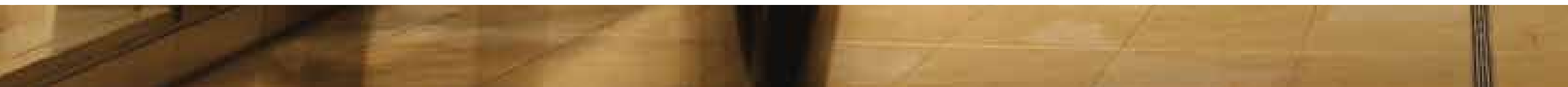
Richard Lowe, Head of Retail and Wholesale, Barclays Retail & Wholesale

There is no denying that the population is growing older; the Department of Health expects the number of people aged 65 and over to grow by 51 per cent by 2030, and those aged over 85 to rise even more steeply, by 101 per cent. This certainly creates a challenge for retailers but, as these figures show demographic shifts take decades to emerge, not seasons so the sector has time to adjust to Britain's ageing population.

That said, retailers should not ignore this issue as understanding how the market is changing today will be essential in the long term. The older generations are expanding in numbers, creating a large consumer audience but, while their needs may differ from younger consumers they are just as likely to be using technology in similar ways, particularly as new technologies and mobile devices become more user-friendly and intuitive.

What this points to is the increasingly important role retail formats will play and the need for retailers to focus on and develop their multi-channel offerings. Channels such as click and collect and e-commerce with home delivery neatly provide an alternative way of shopping for the older, often less mobile consumer. Similarly, I also expect not just the face but the role of the high street to evolve to meet the needs of this ageing population. We have already begun to see some forward thinking town planners break with tradition and incorporate services and local amenities into the traditional high street. GP surgeries, libraries and other health services have begun to pop up in between convenience stores and chemists whereas traditionally they have been set back from the main thoroughfare. These act as a draw for the older generation who are less inclined and perhaps less able to travel for their groceries but still need to access essential local services. Transport, accessibility and local infrastructure will therefore become increasingly important.

The implications of an ageing population are clear for all to see, so provided the sector continues to evolve in line with these shifting demographics and consumer spending patterns, retailers won't find themselves asking where all their customers have gone in years to come.



David McCorquodale,
UK Head of Retail, KPMG

The changing demographic profile of the UK is a major influence on consumer purchasing power, shopping behaviour and shopping preferences. The age structure, ethnicity, household composition and demographic distribution of the UK population are all undergoing significant change and its implications are important for retailers to understand and anticipate.

The UK population is growing and projected to rise to 73.2 million in 2035, creating new market demand and a growing market place. The ageing population and changing ethnic make-up of the UK are two of the most influential demographic forces shaping the UK retail market.

Over the next 10 years, 37% of the UK population will be over 50. Capital Economics predicts that the over 65's will account for £1 in every £4 of retail expenditure. The labour market is also changing significantly. The number of people who are working aged 65 and over has doubled in the past two decades, coining the term 'Silver Sloggers'. Older consumers will unquestionably be different from today with marked differences in lifestyle, attitude and preferences.

The way people shop will continue to evolve. Online shopping is becoming more widespread amongst the older population. Shopping facilities that assist mobility and convenience will continue to grow, as will delivery services. Retailers should consider revisiting their store layout, space allocation and product apportionment and packaging.

The financial and time demands being placed on the middle generation is growing, due to a growing number of dependent children staying at home for longer and a rise in the elderly being cared for at home. This is placing a further squeeze on disposable income and a growing demand for convenience led retail solutions.

The profligate spending youth market is shrinking and the proportion of 15-29 years olds is forecast to decline to 17%. However, the number of children aged 16 and under is projected to increase by 12% to 13 million by 2035 benefiting the infant and children's sector.

Similarly, there is predicted to be more but smaller households. The number of one-person households in England is forecast to increase, single parent households are forecast to continue to rise, whilst the number of one-child households is growing and now account for 47%, increasing demand for smaller pack sizes and increasing the spend per child.

Net migration has become the primary driver of demographic change in the UK. Growing ethnic diversification is leading to further internationalization of demand and a rise in ethnic communities, particularly in urban areas. However, change is not being felt uniformly and differs by region. This forces retailers to consider regional demographics when allocating products.

In summary, evolution in demographics impacts product, space, offering and packaging and those retailers who monitor trends and adapt their offering will be best placed to benefit from the changes.

Mark Teale, Head of Retail Research, CBRE

Retail markets are constantly adapting to economic and regulatory change; to cultural and social change and to seasonal demand variations. Demographic trends change too but at a snail's pace in comparison to the main retail sector drivers and in ways that are highly uneven geographically. For example, population growth is apt to occur much faster in the south than the north; populations are apt to cluster by income and, in the case of migrants, often by nationality too. And age/life-stage/employment prospects also impact upon where we choose to live. These factors all affect local per capita spending levels and goods purchasing proclivities locally to some degree. But there are many other factors in play, not least shopping pattern change caused by development activity, which also impact local consumer spending: factors that have a far greater effect on the retail sector over time than demographic trends per se.

For example, the last 20 years or so has seen a steady reduction in non-food chain size as retailers have sought to concentrate their retailing activities in larger branches in dominant markets. Continuing network contraction has left a long tail of obsolete small-unit High Street shopping in its wake. Half the population now shop for comparison goods in just ninety or so major trading locations nationally, down from over 200 in 1971. This steady market concentration has gone hand-in-hand with the homogenisation of offers in large dominant centres simply because mass market non-food retailers are all chasing space in the same places.

Although in part a recessionary gambit, the number of retailers (particularly fashion retailers) now reporting plans to further top-slice consumer markets, concentrating networks in just 150 or so of the largest centres, instead of following the traditional route of aiming for deep local market penetration via many hundreds of branches, has given market concentration a further boost. 'Click and collect' activity is doing the same. Grocers meanwhile are following a completely different strategy, consolidating network penetration by opening large numbers of small convenience goods branches, significantly increasing branch network sizes. So although trends like population ageing and the relatively high rates of inward migration from EU countries (largely affecting London and the south) will impact the retail sector, they are not key sector drivers. Other far more important factors are in play.

Nick Bubb, Retail Analyst

Conventional wisdom paints a rosy picture of a growing number of affluent retired couples with plenty of time and money to spend, but the reality for many is rather different. With ultra-low interest rates and annuity rates, pension income is under considerable pressure, forcing many older consumers back onto the part-time job market to supplement their financial resources. And one painful consequence of people living longer is that many older consumers have the cost of looking after their own parents to consider. And their own children may not find it easy to get full-time jobs in a continuing climate of financial austerity.

> And older consumers are not necessarily the most IT-savvy people around, at a time when retailing is moving rapidly online, although the fastest-growing part of the online market is the fabled "silver surfers".

In some ways, the boom in the take-up of smartphone and tablet device technology (and the related explosion in the power of social networking) is a bigger influence on the pattern of retail spending than demographic change. And, in turn, the shifting ethnic mix of our increasingly multi-cultural society may also be now as important a factor as pure demographics.

Traditional social and racial stereotyping still prevails in most marketing studies, but half the babies born in London are now to non-indigenous UK mothers, so marketing and advertising campaigns need to adjust to the fact that the target market is changing, just as many supermarkets now sell Polish and Asian specialty foods. The influence of the UK's shifting ethnic mix on markets like fashion is less clear, with the assumption being that "global" brands and styles will dominate. But as our big shopping centres embrace a "wifi" world they will also need to weigh up the kind of shops and facilities that a less young and a less "English" population will need in the next decade.

Martin Hayward, Founder of Hayward Strategy and Futures

There can be a tendency in society at large and the retail sector as well, to chase the novel at the expense of the proven, the new at the expense of the old. As has been said many times, there is also a natural inclination to initially over-estimate the impact of new technology, yet to underestimate it in the longer term.

At present, despite the long anticipated and signposted ageing of the population, there is potential for many older consumers to be disenfranchised by a rapid rush towards new technology in retail by some players, without clear thought as to the needs of those who choose, or are unable, to embrace it.

Retailers must ask themselves to assess both the efficiency and the effectiveness of new technologies in the value chain if they are to enjoy the many benefits that it can bring. A good example is self-scanning technology in convenience stores - many love it, yet many, particularly older consumers, hate it. The answer has to be therefore to offer both options, not to insist on consumers using technology if they don't want to.

The human interaction in shopping is crucial to consumer satisfaction, and we must acknowledge that we have yet to fully understand the impact that remote and technology driven interactions will have on satisfaction.

Will we tire of an endless stream of on-line offers, literally faceless transactions and conversations, or will we simply adapt to this new world order over time?

There is much talk of digital natives versus digital immigrants, with many citing that the younger generation are growing up in this digital world and will know and demand no different, whereas those over 35 are looking in on a world they'll never fully understand. Or will the younger generation tire of remote and online interactions and begin to search out the human face of retail again?

I have often asked Why do pensioners go shopping on Saturdays? Clogging up the stores with their silly trolleys when they could easily go on Wednesday morning when there's nobody else about. They do it because that's when everyone else goes shopping, because the buzz of the market place is central to our human needs to forage and interact.

Efficiency should always be sought in retail, but your older shoppers and maybe your younger ones as well will still value the human touch. Remove it at your peril.

3

Underperforming high streets could be saved by single ownership, says RTT

– Single ownership could rescue many high streets that are currently locked in a spiral of decline

– Experienced asset managers hold the key to revitalising high streets

– Compulsory purchase orders may often be necessary to effect beneficial mix change

– Use and access controls (including decisions on the scale of parking provision required) need to be vested in asset managers too

– Managing high streets as single shopping centre assets could attract very substantial funds from turnaround players, private equity and foreign investors

Part I:

Executive Summary

Much has been said about the death of the high street and the subject has spawned numerous reports with government and retail experts putting forward a plethora of palliative proposals. But serious solutions to the deeply rooted high street problems have yet to emerge. This is surprising as high streets are, in effect, just shopping centres. Commercially managed shopping centres continue to operate successfully despite the long-run downturn. If the political will was there, implementing solutions would be expected to be quite straightforward. So what is wrong with the 'high street'?

The KPMG-Ipsos Retail Think Tank ('the RTT') met in October to discuss the key issues facing the high street and to consider the steps needed to revitalise failing high streets.

Why has it come to this?

Seismic changes have rocked the retail landscape over the last 50 years, from rapid growth in car ownership and out of town shopping developments to the internet. And now we are beset by the longest run economic downturn in a generation: a recession that has caused structural damage to retail markets and accelerated high street decline. Underlying everything is the long-run migration of chain operators from small markets to large that has left a trail of obsolete shopping in its wake.

Nick Bubb, independent Retail Analyst, says: **"In any recession there is the inevitable shake out of those weaker retailers. However, ordinarily new retailers eventually replace those who have left, and the high street would recover. This recession has been so deep, and so long, that the tide has not come in and this second wave of retailers has not arrived, leaving washed up shops and widespread structural problems in the high street."**

David McCorquodale, Head of Retail at KPMG, notes that: **"UK high streets have divided into a two tiered environment of the thriving and the merely surviving. Some, like Bond Street and Buchanan Street with their eclectic mix of shops and strong community programmes, are prospering whilst others are blighted by vacancies as retailers flee the confines of their slowly dilapidating surrounds in favour of a modern purpose built shopping centre with ample parking - and bypasses that take passing traffic away from town centres."**

The average UK high street now consists of a patchwork of unit shops owned and managed by individual landlords, leasing their units on the terms that best suit them and their business. Securing and maximising revenue must of course be their top priority, and it is unlikely the average single unit landlord will turn away a secure tenant because their use doesn't complement the overall retail mix.

This is one of the key problems facing the high street according to the RTT. The mix and type of retailers on the high street need to be proactively managed to create a vibrant centre, but multiple ownerships often make this impossible.

In certain extreme examples where high streets have become severely dilapidated, are riddled with vacant units and are not delivering for their local community, the RTT believes the only way to overcome this problem is for properties to be brought under single ownership so that the high street can be actively managed as an entity in the same way as a purpose-built shopping centre.

Single ownership can deliver the substantial, and radical, change necessary to rescue many currently moribund high streets. Indeed, it is lack of high street mix control (commonly in tandem with poor accessibility due to inadequate parking provision and shopper-unfriendly parking controls) that has resulted in mainstream investors progressively turning their backs on the high street in favour of modern purpose-built shopping centres. Investor flight has compounded the high street problem by draining stock-renewal cash away.

Fixing the mix

Mark Teale, Head of Retail Research at CBRE says: **"A lot of high streets have nothing intrinsically wrong with them as shopping vehicles, subject to inadequate parking provision and unit size distribution problems being addressed. It is the absence of mix control, due to multi-ownership, that is the real bugbear. Mixes are not self sustaining: they need continuous work for high streets (or shopping centres) to be sustained as shopping attractions. A lot of currently failing high streets would be fine if only they were managed in the same way as purpose built shopping centres."**

But multi-ownership is also damaging the high street. Individual owners are understandably apt to go for the highest rent possible, paying little regard to how their lettings impact the wide tenant mix. This approach is in stark contrast to the attitude of a shopping centre owner who is commonly prepared to take a hit on rents if it means securing a tenant whose business will strengthen the mix, enhancing the value of the overall asset.

Everything comes back to ownership. Without single ownership there is no mix control. And without mix control, and control over accessibility (including parking provision), it is all but impossible to reverse high street decline.

However politically unpalatable it might initially appear, a lot of high streets would be far better off under the control of professional shopping centre asset managers than a plethora of individual owners. Achieving that requires an extension of compulsory purchase powers together with the vesting of use and access/parking controls in the hands of asset managers, as occurs with purpose-built shopping centres.

Neil Saunders, Managing Director of Conlumino says: **"A single owner would take greater care of the environment around the high street and it would be in their interest to organise targeted events which would benefit the local community and encourage them to visit, a bit like the initiatives we see in shopping centres. They could also buy and control local car parking and remove charges which are dissuading visitors. By owning the retail environment they could make commercial decisions to suit the local market and make the high street as successful as possible."**

The issue of parking also needs to be addressed. Mark Teale of CBRE says: **"Accessibility is important. Parking provision needs to be brought up to the levels necessary to serve the shopping offer present. Rationing parking to generate parking revenues for local authorities is pernicious from the shopping perspective because it deters shoppers, undermining high street prosperity. The milking of town centre visitors to generate parking revenue is like a hotel owner charging guests to use the lifts or stairs to get to their rooms. Parking is just part of the accessibility arrangements, not a business end in itself. The long-run failure to invest in town centre parking has inevitably resulted in many high streets becoming hopelessly uncompetitive compared with modern customer friendly purpose-built shopping facilities."**

Address regulation that's no longer fit for purpose

Mark Teale of CBRE says: **"The sort of short-term high street fixes we have seen bandied about over the last three to four years can only fail because they address superficial symptoms (vacancies or current rating anomalies) not the underlying reason for high street decline at individual town level. Much of the decline is self-inflicted due to inappropriate planning controls and counter-productive central and local government taxation activities."**

"Some high streets can be radically improved simply by bringing them under single management, as long as the shopping stock is still viable. Other high streets, for stock obsolescence reasons, are no longer viable for shopping, whatever you do. The UK is littered with small-scale Victorian and Edwardian unit shopping, originally developed prior to the car as walk-in shopping for local residents that has been redundant for years. Given a great deal of it was originally carved out of residential stock there is an implicit hint regarding a viable alternative use for much surplus stock."

"Creating a sustainable town-centre mix however needs a very clear strategic goal for all the commercial/residential uses present, not an anarchic free-for-all where everything is left to the whims of individual owners. Planning type use controls are useless here it needs cohesive estate-management to sort the high street mess out. Bringing stock under single-ownership can be win-win for everybody the community gets better shopping; shop occupiers make more money; the shopping stock appreciates in value sustaining stock renewal; investors get higher returns and the local authority gets greater rating income. It needs however the political will to relinquish control to asset managers."

Neil Saunders of Conlumino, says:

"We need to remove regulation and let market forces shape the high street. The current regulation in force was designed for a post war Britain when retail was very local, very fragmented and before chain retailers even existed."

Richard Lowe, Head of Retail and Wholesale at Barclays believes high streets would benefit if more businesses were encouraged to return to town centres. **"A high street relies on a buoyant local economy and what better way to drawing in hundreds, if not thousands, of workers from the suburbs and beyond than by incentivising businesses across all industries to relocate to our city and town centres,"** says Lowe.

"We have already begun to see some forward thinking town planners break with tradition and incorporate services and local amenities into the traditional high street. GP surgeries, libraries and other health services have begun to pop up in between convenience stores and chemists whereas traditionally they have been set back from the main thoroughfare. Employers could help boost numbers further if the right incentives were introduced."

A new investment opportunity

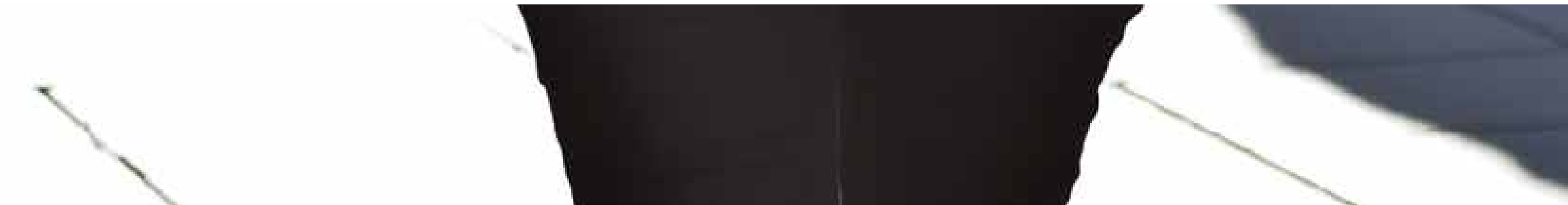
The RTT believes that introducing cohesive asset management to currently multi-owned high streets would restore the attraction of high streets to investors. **"You only have to look at Marylebone High Street, Regent Street, Sloane Street, and Mount Street et al to see the potency of single ownership asset management at street level. However, in most high streets, bringing stock under single management can only be achieved by compulsory purchase. There are examples – such as Queensway – where investors have painstakingly purchased multi-owned stock but the process is simply too time consuming to be used in most high streets"**, says Mark Teale of CBRE.

"The approach would also provide the opportunity for high street planners to jump ahead of shopping centres by creating connected communities via the powers of the internet in much the way Bill Grimsey described in his review," comments Tim Denison, Director of Retail Intelligence at Ipsos Retail Performance.

Overstocked and overtaxed

The RTT agrees with the point made by many commentators regarding unviable shopping stock in many locations. On the one hand the UK has a huge surplus of redundant tertiary shopping and, on the other, a chronic shortage of larger high-productivity unit stock in primary high-volume shopping destinations: on a per capita basis, less than a third of US levels. Clearing redundant stock needs a major shift in central and local government attitudes regarding use controls and business rates.

The need to overhaul the business rate system was seen as particularly urgent by the RTT. Tim Denison of Ipsos says: **"Rates are a totally rigid cost which have far outpaced rents and driven many smaller operators out of business entirely. Bringing forward the next revaluation is not the solution. We need more radical re-thinking on a fair and just means to raise sufficient funds to be in a position to re-engineer and re-energise the high street."**



Conclusions:
Underperforming high streets could be saved by single ownership

The bringing together of the high street under single ownership is a radical approach and isn't suitable for all high streets. However, the RTT believes it could help rescue some of those marooned in secondary and tertiary locations which investors have previously shunned. There is a lot of good high street shop property out there that just needs commonsense management.

The RTT advocates that some test bed sites are used to determine whether such a radical approach may work and to shake down and resolve the teething issues.

David McCorquodale of KPMG says: **"Now is the time for action and for commitment from the Government to act on the reviews and industry feedback they have been given. This is not an issue that can be punted into the long grass and forgotten about."**

"The potential long term solutions must involve active asset management by experts in the retail industry, who know the local market and can look at the high street commercially and make the changes needed to secure its future prosperity."

Martin Hayward, Founder of Hayward Strategy and Futures says: **"The economics of retail have changed forever and the economics of town centre management need to catch up. Without customers there will be no shops, and with no shops there will be no revenue from rent, rates, parking or otherwise."**

Richard Lowe of Barclays concludes: **"Despite the media headlines the high street will continue to play an important role in our communities, however it must evolve to meet their changing needs. This will only happen with the sustained support from central and local Government, retailers and the local communities themselves."**

Part II:

In detail – Individual views of the RTT members

Nick Bubb, Independent Retail Analyst

A review into why there have been so many reviews of the high street would probably conclude that neither Mary Portas nor Bill Grimsey were ideal choices to front up high-profile investigations into the state of the high street, although both made contributions to the debate.

Mary Portas may be nostalgic for a time when butchers, bakers and greengrocers ruled the high street, but her vision of the importance of local community received shamefully little support from the Government. Bill Grimsey took a more hard-headed approach, rightly focused on the importance of business rates reform, but his report was rushed and his idea of a turnover tax on big retailers was not well thought through.

The background problem is, of course, that untrammelled expansion by online retailers, out-of-town retailers and big supermarkets has taken a lot of consumer spending away from town centres, leading to a polarisation of "the high street" between prime shopping streets/ regional shopping malls and secondary/tertiary shopping locations and it is the latter where the problem of empty units and "too many" charity shops and pound shops is most prevalent.

If the Government really wanted to reverse the shift in consumer shopping behaviour that has decimated many small towns and high streets then it would be looking at a tax on out-of-town car parking or a tax on online shopping, to make it more expensive to neglect high street shops or to at least level the playing field with the high street.

If the political will is not there to actively discourage online shopping or out-of-town shopping by the feckless consumer, then, as Bill Grimsey identified, the question arises of who will pay for local councils to restructure the weaker high streets. Some of these do have a future of a different kind (a sunlit vista of thriving cafes, farmer's markets and art galleries and online parcel pick-up points?), even if the scope for conversion to residential usage is limited.

If nobody is willing, in these times of economic austerity, to fund a restructuring of the weaker high streets or actively incentivise high street shopping, then it is very difficult to see much changing in the situation, although there is surely still room for a more coordinated effort to improve the public face of, and encourage more professionalism in, the fast-growing charity shop sector.

Tim Denison, Director of Retail Intelligence at Ipsos

I, like many, welcome the recent contribution that the Grimsey report makes to the debate about how to resolve the ills of the high street, not least because it is grounded on evidence-based analysis, something that was sorely missing in the Portas review.

To my mind his top-line conclusions settle in the right space:

- the future of the high street requires some conversion out of retail, creating multi-use spaces that re-introduce and connect living, breathing and working communities to town centres;
- the means of achieving this is through root and branch changes to the business framework that plans and "manages" them;
- high street planning should embrace the power of digital as part of its makeover.

Investment, of course, is at the heart of the matter. The proposed levy on national retail and leisure chains to amass a development pot seems unfair and implausible. The elephant in the room is the business rate tax mechanism which is simply no longer fit for purpose as the principal on-going funding generator. Bringing forward the next revaluation is not the solution. We need more radical re-thinking on a fair and just means to raise sufficient funds to be in a position to re-engineer and re-energise the high street. Perhaps introducing footfall as a unit of high street activity has a role to play here.

The need for Government action to facilitate change and encourage investment is clear, however, the speed with which it can make decisions and enable any grandiose plan to progress is a worry. In the meantime there is a responsibility on local authorities to seriously question how they can work differently to prevent the hearts being taken out of their town centres. As we have proposed before in the Retail Think Tank, a good starting point is for local authorities to tackle empty, obsolete property through a change-of-use process. Store closures on high streets are much about long term structural changes to the sector, so facilitating change-of-use programmes is a necessity.

I will finish where I started. Planning is at the centre of Grimsey's recommendations.

Whilst his report is constructed from evidence-based analysis, most of the facts are sourced through private enterprises rather than public authorities because they do not exist within. For high street planning to be anything other than piecemeal in the future, we need to have access to more retail data publicly about the mix of usage and sales performance so that planners and managers alike can measure their success.

Richard Lowe, Head of Retail and Wholesale at Barclays

The pace of technological change has resulted in a natural reduction in the size of store portfolios and an increase in the number of empty retail units on our high streets. Despite the media headlines the high street will continue to play an important role in our communities, however, it must evolve to meet the changing needs of communities. This can only happen with sustained support from central and local government, retailers and the local communities themselves.

The issues at the heart of the problem are extensive, ranging from business rates and petrol prices to infrastructure and simply selling the right product mix at the right price. For example, the increasing price of parking and petrol means that popping to the shops for a few groceries can be a costly experience so it is no surprise that many consumers have been driven out of our town centres to retail developments which offer free parking. Reducing parking costs or, even better, offering free parking for an hour could act as a stimulant and draw shoppers back to the high street.

Private sector employers across all industries could also help our high streets by locating more jobs in and around town centres. A high street relies on a buoyant local economy and what better way to drawing in hundreds, if not thousands, of workers from the suburbs and beyond than by incentivising businesses to relocate to our city and town centres. We have already begun to see some forward thinking town planners break with tradition and incorporate services and local amenities into the traditional high street. GP surgeries, libraries and other health services have begun to pop up in between convenience stores and chemists whereas traditionally they have been set back from the main thoroughfare. Employers could help boost numbers further if the right incentives were introduced.

So while Mary Portas and Bill Grimsey lock horns over how to revive the fortunes of the great British high street one thing everyone agrees on it that short-term retail friendly fixes are not going to save our shopping parades but, long-term and sustained planning will.

David McCorquodale,
UK Head of Retail, KPMG

UK high streets have divided into a two tiered environment of the thriving and the merely surviving. Some, like Bond Street and Buchanan Street with their eclectic mix of shops and strong community programmes, are prospering whilst others are blighted by vacancies as retailers flee the confines of their slowly dilapidating surrounds in favour of a modern purpose built shopping centre with ample parking – and bypasses that take passing traffic away from town centres.

For years the evolution of the high street was natural as increased car ownership and town centre congestion drove retailers to seek new frontiers. The pace of evolution was glacial and, in an environment of ever-increasing consumerism, it was argued that 'pedestrianised' high streets would bring independent stores and boutiques to life.

However, developments in the last five years accelerated the pace, and altered the direction, of change. A perfect storm of the deepest, longest recession ever, coupled with the seismic shift brought about by the internet has rapidly changed consumer behaviour. Consumer hardship coupled with digital commoditisation of the retail sector has driven massive structural change. Against this backdrop, an archaic property and rating system hasn't allowed retailers to cut their property costs in line with their falling markets.

The result? Consumers flew to value; the collapse of Woolworths made way for growth of value retailers in lower cost locations. Fashion brands re-appraised the optimal size of their UK estate down from around 250 to 60 stores and a great website. Penetration of online shopping damaged store profitability, leading to closures and failures. Local councils, suffering spending freezes, sought to raise funds from car parking. Together, these actions combined to impact detrimentally town centres in areas of consumer hardship or in close proximity to successful out of town shopping malls. However, the internet age now puts the consumer in control of how and where he/she shops.

Looking forward, the internet and car ownership are here to stay. The economy will recover and consumer spending will increase again. Evolutionary development will continue – already the grocers are returning with a convenience offering. However, tomorrow's cyber consumer will determine where and how they want to shop. I expect to see the social evolution of high streets return in time with a mixture of residential and leisure mixing with retail. Why shouldn't joiners, designers and dentists fill the vacancies and leisure units like nurseries, day care centres etc use the space? If consumer behaviour determines that retail turns its back, rents will come down and councils must work with landlords to drive the necessary changes to recreate a social hub – this must also involve the motor car too though!

There is no quick fix to this tale of two high streets – the evolutionary glacier will wind its way.

Neil Saunders, Managing Director of Conlumino

If the rise of online has done anything it has reshaped where we shop, including how we use our high streets. On its own the online dynamic was always sufficient to cause significant disruption to the established order but the recent downturn has had the effect of amplifying and accelerating the trends already prevalent in UK retail.

The fundamental issue facing high streets is that, following the pre-recession boom years, retail now finds itself with overcapacity. This is one of the reasons why so much space has become unprofitable and has closed. In a sense retail is rebalancing supply relative to demand. As harsh as it may be, this is not necessarily a trend we should try to buck as it's merely a function of natural market dynamics.

That said, there are a number of factors which are unhelpful to high streets, which are not necessarily part of the natural dynamic of change. The first of these is the punitively high level of business rates. These are set outside of market forces and have been damaging to many retailers and therefore to high street vitality. If high streets are to be given a fighting chance, this burden needs to be reduced or, better still, removed. The second issue is parking charges and restrictions, especially those set by local authorities. Again, many of these are not subject to proper market forces and, as such, dampen footfall from high streets.

Regardless of the causes of decline, the impact of changing habits is not even across all high streets. Those locations which are bearing the brunt are typically smaller, more secondary town centres – particularly in the north – which are experiencing high vacancy rates, as already under pressure discretionary demand is drawn elsewhere. Difficulties in these locations have been compounded by high profile retail casualties of large multiple retailers which would previously have been key footfall drivers.

Nonetheless, while the more general picture for high streets is uncertain, strong locations, offering varied retail mix in addition to leisure and food service, have actually continued to prosper. The situation on the ground, then, is both polarised and complex, which renders 'one size fits all' solutions – as often heralded by various reviews – rather inappropriate.

Mark Teale, Head of Retail Research at CBRE

What we are seeing playing out on the high street is nothing new. It is just that longstanding high street fault-lines have been brought into unusually sharp relief due to the longevity of the current downturn. Unlike the short-sharp recessions of the past (which also saw vacancies proliferate), we are now six years down the line with no hint yet of an end to the seemingly inexorable income squeeze (or the recessionary vacancy problem), the longest in living memory and the reason why high street attrition has proved both so pronounced and now appears so intractable.

The underlying problems however remain the same as they have always been. It is not the economic downturn that is the issue or online shopping or our archaic golden-goose killing rating system. Nor is it inept planning controls or money-grubbing local authorities abusing parking controls to milk shoppers: albeit all play a part in undermining the productivity of high streets. It is stock obsolescence and multi-ownership that are the real villains of the piece.

The more modern shop space that we have added; the more shopping centres and retail parks and superstores and outlet centres that we have built the more chain operators have migrated from small shops in small trading locations to larger, higher productivity, modern shop space in bigger markets. This long run migration (it started in the 1960s) has left a trail of redundant small-scale tertiary/poor secondary high street shopping in its wake.

There is no magic planning wand that can render unviable shop property productive. Short of subsidy, Canute like attempts by central and/or local government to sustain obsolete stock in shopping use is as doomed to failure today as it was 30-40 years ago. Belatedly the Government (but not yet many local authorities) has recognised this, proposing allowing some of the huge surplus of tertiary small-scale unit shopping to change use to residential, whence a lot of it came. There are however many high streets where the problem is multi-ownership, not stock obsolescence and/or accessibility problems.

Self-sustaining high street mixes built around local walk-in shopping ended with chain retailing. Mix control and accessibility is everything in retailing now. Balanced mix-uses attractive to shoppers rarely happen organically and, when they do, are rarely sustained. The free-for-all of mixed-ownership almost always results in the entry of occupiers that undermine mixes; it can often take just a handful of inappropriate occupiers to tip otherwise attractive shopping destinations into a spiral of decline. The UK is littered with high streets with hopelessly damaged mixes.

Bolt on the widespread abuse of parking controls by local authorities, with an eye to revenue raising rather than accessibility improvement (lack of parking investment and inflated parking charges/fines renders many high streets both hopelessly uncompetitive and hostile to shoppers); use controls that suited 1950s shopping but not modern shopping needs and a hopelessly-flawed rating system than can and does force healthy retailers out of business, and it is unsurprising that so many high streets are now in difficulty. And, as the problems are for the most part self-inflicted and resolvable, it is a tragedy.

An obvious solution (albeit politically unpalatable), is to bring failing high streets under single ownership, managing them commercially as shopping vehicles. But first it needs local authorities to be taken out of the loop, vesting use controls and parking in asset managers instead. Doing so would allow the common-sense mix controls used in shopping centres to be applied in high streets as well, free of the conflicted central and local government revenue raising goals that cause so much damage in shopping areas. The potency of high street mix management can be seen all over Central London in areas owned by landed estates and commercial estates: it just needs Government to have the political will to act.

Martin Hayward, Founder of Hayward Strategy and Futures

Both Portas and Grimsey have, in their own way, brought to life the changing role of the high street in modern life. At the heart of both their analyses lies an acknowledgement that shoppers used to need high streets, but now have to be encouraged to want them.

It is now perfectly feasible, if rather depressing, to sit at home and order almost all of one's requirements online, frequently for a cheaper price than would be possible on the high street itself. In this environment, we have to acknowledge that the high street has to add new attributes to its appeal in order to justify the time that a visit can take up.

These new attributes will need to reflect both the need to make a high street visit a more enjoyable and social activity but also to maximise the ease with which it can be accessed. The former will change the profile of the high street towards a much greater mix of services and building uses and the latter will require a major re-think of traffic and parking policies that can currently deter the quick visit.

To enable this transition to occur will require much greater foresight and simple common-sense from central and local government. The economics of retail have changed forever, and the economics of town-centre management need to catch-up. Without customers there will be no shops, and with no shops there will be no revenue from rent, rates, parking or otherwise.

A pre-occupation with pedestrianisation, and futile attempts to stop the use of cars (over 400,000 new cars were sold in the UK in the last month alone) seem to be at the heart of so many high street plans. It makes no sense that it's more convenient to order online and have goods delivered than it is to nip into the local high street for a quick shop. Humans are social animals, they love the buzz of the market place, people watching and the serendipity of browsing they just don't have the time or the patience to be managed around the one-way system and into the multi-storey to find it.


HIGH STREET

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