

Quick Stats

	Change from	
	Q2 08	Q3 07
Consumer Sentiment	↓	↓
Retailer Sentiment	↓	↓

Hot Topics

- The turmoil in the global financial markets is now shifting from Wall Street to "Main Street" and as a result consumer confidence is being affected.
- Despite demand for prime units remaining robust, rental growth is now slowing in many European markets.
- Retailers are now beginning to scrutinise expansion plans, however, many remain active across Europe.

OVERVIEW

The turmoil in the global financial markets is now having a clear impact on wider economic prospects, as the focus shifts from Wall Street to "Main Street". Of particular concern for the retail sector is the potential impact on consumer spending, which on average makes up over half of European economic activity and has been one of the key drivers of growth in Europe.

In Central and Eastern Europe (CEE), where consumer spending has accounted for an even higher proportion of recent growth, initial hopes that the economy would be relatively unaffected have proved unfounded.

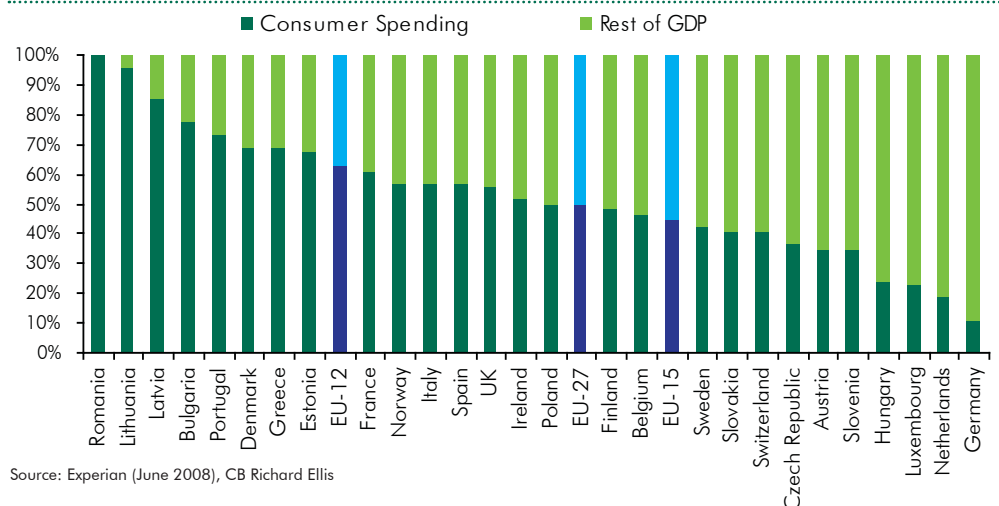
The main fear is that the wider economic slowdown will translate most quickly and directly into reduced retail sales. As disposable incomes come under pressure and cheap mortgages and credit cards are withdrawn, consumers will be forced to reduce the "discretionary" components of their expenditure. Given that their spending on housing, travel, education and food are largely fixed, it is the non-essential clothing, household goods and leisure sectors that will be the first to see any impact.

Although the full impact of reduced consumer spending has not yet been seen, it is already noticeable that some retailers are beginning to slow their expansion programme. Signs of stress amongst retailers are currently being seen in weaker sales performance rather than store closures or corporate collapses. However, some retailers in the UK are already asking to pay rent monthly rather than quarterly to help improve cashflow.

At the same time, many retailers are continuing to see sales growth, albeit at a slower rate than in the recent past. While luxury brands such as the LVMH group and Burberry are reporting growth, many of the discount retailers such as Primark, Lidl and Aldi are actually seeing sales soar, as they attract increasingly price conscious consumers.

Going forward, it will be those retailers who have a particular point of differentiation within their market – either on product or price - who are likely to succeed despite tougher market conditions. Indeed, many such retailers are continuing with their expansion plans, seeing the current market as an opportunity to grow their market share.

Consumer Spending Growth as % of GDP Growth, 2004-2008



Source: Experian (June 2008), CB Richard Ellis

RETAIL ECONOMICS

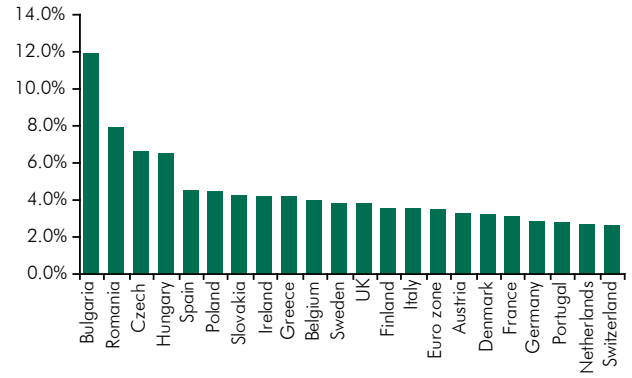
During the first half of the year there was significant debate about whether inflationary pressures were the major threat to economic growth, and whether this justified further increases in interest rates. However, it is now apparent that recession is the real threat. Although inflation remains well above the ECB and Bank of England target level of 2%, it is expected that this has now peaked. As the economy begins to slow, inflation will fall as a consequence.

Whilst the inflationary threat may be moderating, a wide range of other factors are combining to reduce consumer's confidence and thus their spending plans. This is summarised on page 7 using the Misery Index, which charts the combined impact of inflation, interest rates and unemployment on consumption activity. Consumer confidence has fallen steeply since mid-2007 and is now well below its long term average. Media coverage of an impending "global recession" does little to encourage people to spend. Consumers remain nervous about the prospect of limited income growth at best, and at worst the possibility of unemployment. They also need to pay back any existing mortgage and credit card debt which has built up over the last few years. Overall, consumers "wealth" is also likely to be declining, not only as a result of falling house prices but also in terms of savings held in the form of equities and bonds.

Whilst there has been much comment on the US housing market, it is also the case that the housing market in much of Europe became even more overheated. Mortgage debt has risen sharply in many countries over the last ten years. The European consumer is therefore far more exposed to the rising cost of mortgages than in the past. This is particularly an issue for those who are seeing their mortgage payments reset to 'market' levels after an initial discount period. Falling house prices mean that, for some, they are now in position of 'negative equity'.

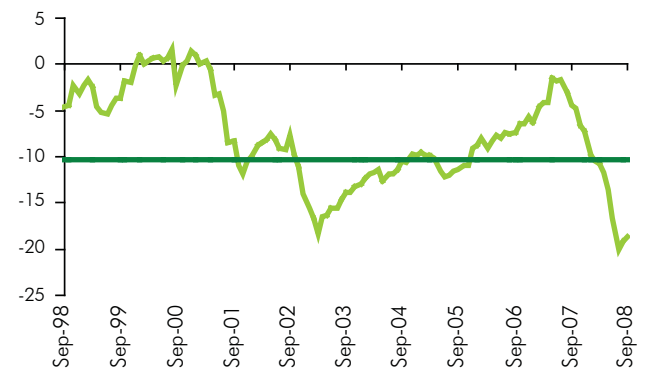
In the short term, the prospects for many retailers appear weak – although thus far reported retail sales remain fairly flat across many of the main European markets including UK, Germany and France. Overall retailer confidence is suffering, but as the crucial Christmas trading period approaches the impact on retailers or markets will not necessarily be uniform. Whilst some will suffer, others who have a particular point of differentiation within their segment stand to benefit. This includes some of the budget retailers who will appeal to the cost conscious, but also the luxury brands for whom general trends in spending are less relevant.

Inflation 2008



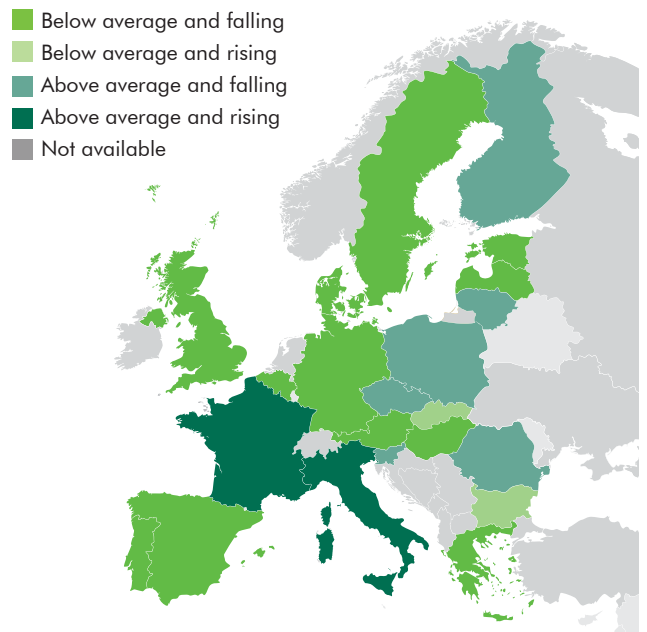
Source: Consensus (October 2008)

Consumer Confidence, September 2008



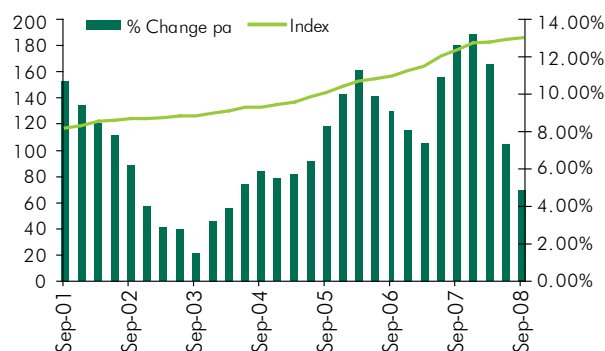
Source: Eurostat

Retailer Confidence, September 2008



Source: Eurostat

EU-27 Retail Rent Index, Q3 2008

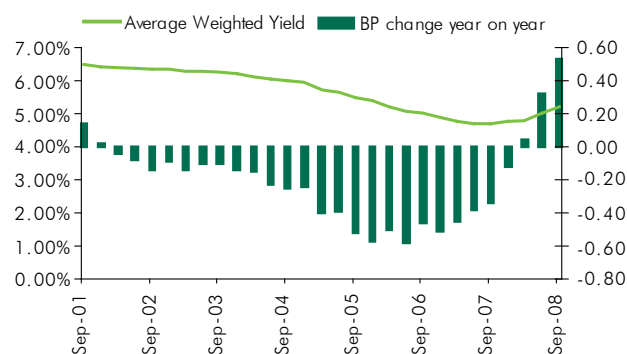


Source: CB Richard Ellis

EU-27 Retail Rent Index

	Q4 2007	Q1 2008	Q2 2008	Q3 2008
Index (Q1 2000 = 100)	182	183	185	186
Quarter-on-Quarter (% change)	2.6%	0.8%	0.9%	0.5%
Year-on-Year (% change)	13.2%	11.6%	7.3%	4.9%

EU-27 Retail Yield Index, Q3 2008



Source: CB Richard Ellis

EU-27 Retail Rent Index

	Q4 2007	Q1 2008	Q2 2008	Q3 2008
Index (Q1 2000 = 100)	76	76	80	83
Average Weighted Yield	4.77%	4.80%	5.03%	5.22%
Quarter-on-Quarter (bp change)	8	3	23	19
Year-on-Year (bp change)	-2	1	5	8

RETAIL PROPERTY MARKET

The EU-27 Retail Rent Index remained virtually static this quarter, with growth of 0.5% from Q2, as a result of a somewhat less active occupier market. Rental growth has slowed across much of Europe, especially compared to the first half of 2007 when quarterly rental growth peaked at 5%. However, there were still small upward movements in rent in some markets including Vienna, Athens and - most notably - in London, where rents show no indication of a slow down, increasing over 7% quarter-on-quarter, and over 11% annually. Elsewhere, rents generally remained stable during the quarter.

Annual growth in the index has also slowed, although rents are still 4.9% higher than a year ago. Activity from retailers remains focused on key cities and prime locations, with those who are still expanding remaining focused on their longer term strategic objectives - which tend to involve entry into strategically important markets and expanding market share. While demand for prime pitches is expected to remain robust it is the secondary locations which are expected to experience more challenging times, both in terms of retailer demand and trading performance.

In the investment market, the CB Richard Ellis EU-27 Retail Yield Index increased for the fourth quarter running, with the Average Prime Yield rising 19 basis points quarter-on-quarter to 5.2%. This is an increase of over 50 basis points from its historic low point in Q3 2007.

Despite relatively stable occupier demand, it was many of Europe's leading retail cities such as London, Paris, Berlin and Milan that saw some of the strongest outward movement in yields over the quarter; in all of the above, yields rose by between 25 and 50 basis points. Concerns over the prospects for Irish retail, as the country became the first in Europe to enter recession officially, resulted in an outward yield movement of 75 basis points over the quarter; yields have now risen by 200 basis points in the last year.

Elsewhere, prime yields in the best locations have generally remained stable, although yields on secondary retail stock have seen more rapid adjustments. It is also expected that different retail formats will fare differently during a period of slower economic growth. Just as dominant retailers will benefit at the expense of weaker players, so dominant locations and formats should outperform. In the Shopping Centre sector this might suggest that larger centres will perform better than smaller centres, but this will certainly not always be the case. Many smaller centres with strong local catchments are proving more resilient than their larger competitors.

EUROPEAN OCCUPIER MARKET

The "internationalisation" of retail has been a hot topic in recent years, and despite (or in some cases because of) tougher economic conditions in domestic markets, many are still looking to expand into new markets. In recent years the UK, Spain and Ireland having been amongst the biggest beneficiaries of this trend, with the arrival of numerous retailers from other countries. However, these are also the markets which have been hardest hit by the credit crunch, largely due to high levels of personal debt and exposure to an overheated housing market. Retailers remain confident about these markets longer term, although short term demand for units is likely to moderate. However, many see current market as a time of opportunity, with retailers such as Next, Tous, Bestseller group and H&M looking to expand in both Western and Eastern Europe. Some are more bullish than others, and private companies are generally better placed than listed companies who are subject to the more negative sentiment currently prevailing in the equity market. Value retailers such as Primark, Lidl and Aldi have seen strong trading activity as a result of more price conscious consumers. At the other end of the market, high-end retailers are also continuing to trade well as the spending of top end consumers is less closely tied to the fortunes of the economy as a whole.

UK

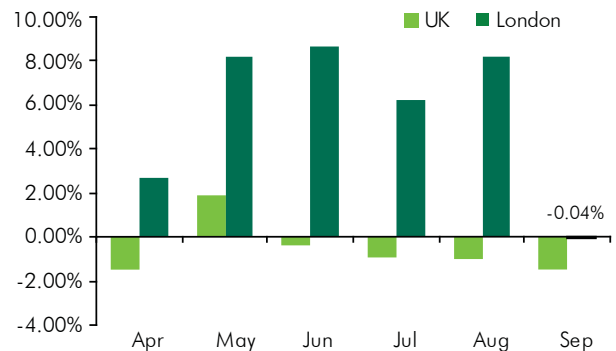
The upheaval in the financial markets continues to impact the UK economy and consumer confidence remains greatly affected. Central London remains somewhat resilient to the downturn, especially as tourists take advantage of the weak pound. However, many domestic retailers are beginning to suffer as a result of the economic crisis. Leading chains such as Marks and Spencer and John Lewis – traditional indicators of the UK market as a whole - have been reporting falls in like-for-like sales. Cross border retailers remain active, especially in London. Tous has recently opened its first UK store and others coming to the market soon include National Geographic, Hollister and Fnac.

FRANCE

Despite the fall in consumer confidence in Europe, the French retail market has remained more stable than people may expect. Retail sales were robust up until the end of August, growing 3% year on year. Similarly the French National Council of Shopping Centres reported footfall remaining fairly stable throughout the year, an important indicator that consumers still appear willing to spend. International retailers remain the most active, with demand focused around Paris and the major regional cities. A notable event for the Paris retail market this quarter was the Swedish retailer H&M finally obtaining planning approval to open on the Champs Elysées. The street has been the subject of discussions and regulations restricting the over representation of fashion brands beyond a certain floor size. Retailers such as Abercrombie and Fitch and Dolce and Gabanna seeking to locate on the street have previously been refused planning permission. However, it is anticipated that the overruling in favour of H&M will invite appeals from these and other retailers.

UK vs London Retail Sales, April - September 2008

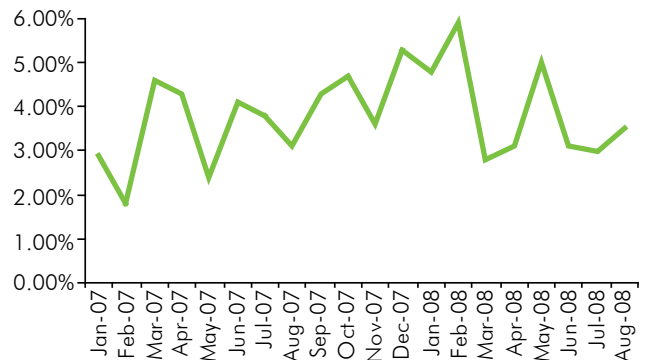
% growth, year on year



Source: British Retail Consortium

Retail Sales Growth, France

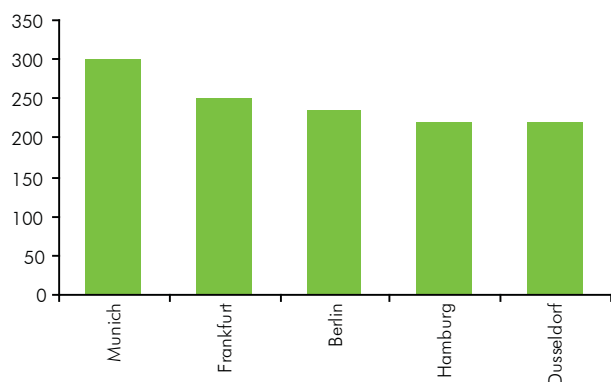
% growth, year on year



Source: Eurostat

Prime Retail Rents, Germany, Q3 2008

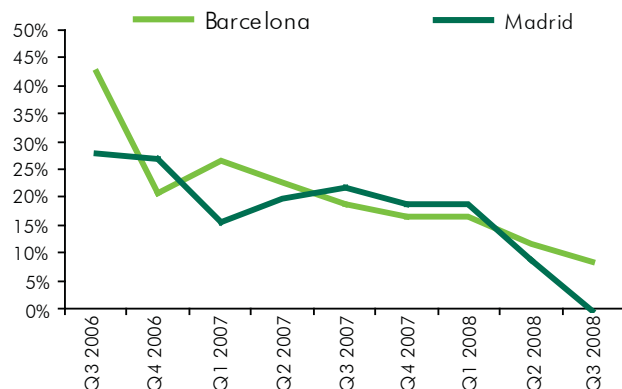
€/sq m/month



Source: CB Richard Ellis

Spanish High Street Rental Growth

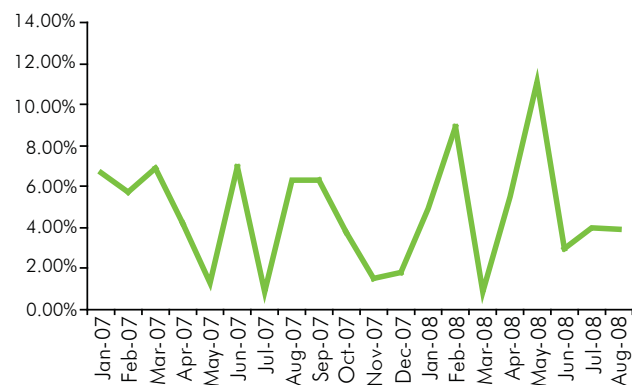
% growth, year on year



Source: CB Richard Ellis

Retail Sales Growth, Belgium

% growth, year on year



Source: Eurostat

GERMANY

Consumer confidence remains close to its long term average. Therefore, whilst some decline is expected, consumer spending and retail sales are not expected to fall as sharply as in other parts of Europe. Germany still remains a potential target for many international retailers, and with some retailers closing stores (SinnLeffers, Wehmeyer and Hertie) others see an opportunity to take market share. Primark has now signed for its first store on the outskirts of Bremen, and other new retailers in the market include Hackett, Ben Sherman and Yamamay. Rents in many of the key cities appear to have peaked. Payments of key money to secure prime units has been a notable trend in recent years, but this is expected to be a lot less common in future as overall levels of demand start to decline.

SPAIN

The Spanish economy has slowed considerably after an extended period outperforming its EU counterparts. Two of the pillars of Spain's growth, consumer spending and job creation, have deteriorated considerably and consumer confidence is currently at its lowest levels since the early 1990s. Retail sales have understandably been affected, particularly during the second half of 2007 and into 2008. National retailers in particular have begun to review expansion plans. Nevertheless, there is still interest from international retailers to either gain a foothold in the market or expand upon existing market share. Sonae Distribuição remains active with both Sportzone and Worten embarking on national expansion while other retailers, such as the Italian cosmetics brand Kiko, continue to roll out their brand across the country. As retail activity has slowed, tenants have become more selective. As such, rental growth has begun to decelerate and retailers have greater scope to negotiate better conditions.

BELGIUM

Although consumer sentiment in Belgium is being adversely affected by negative reports in the media, many consumers remain cash rich and spending does not appear to have suffered significantly. Take-up remains strong across the market with many retailers still willing to take space in prime locations. However, demand for secondary locations, and in smaller towns, has now started to suffer as a result of more cautious expansion plans. International retailers such as New Look and Camaieu are currently two of the most active retailers in the market. Most notably Camaieu recently acquired eight units from Etam, which has now begun to consolidate its store network across Belgium. While demand has previously resulted in upward pressure on rents, rental growth is now beginning to stagnate.

COUNTRY BY COUNTRY ANALYSIS

Demand has remained robust for prime high street stock in **Austria's** capital Vienna, especially from international retailers. American Apparel has now opened its first store in Austria located near the museum district. As units remains scarce, rents are coming under some upward pressure. Prime rents have been increasing by 2% quarter on quarter.

Consumer confidence has begun to suffer in the **Danish** retail market, and as a consequence retail sales are beginning to slow. While the trend has been less prominent in Copenhagen, there has been a slight increase in the amount of vacant units. While rents remain stable in the market it is anticipated that weaker market conditions in the future will result in subdued demand from retailers, may mean that rents begin to weaken.

Demand from international retailers in the **Greek** market is beginning to become intense. Retailers such as H&M and various Inditex brands are notably active. As Shopping Centre stock remains limited demand remains focused on key high street locations. In turn rental growth remains strong, especially in Athens, where rents have increased around 10% year on year. Development activity remains focused in the Athens region, with around three new centres anticipated to open during the final quarter of 2008. As demand remains strong, these centres are leasing well.

Wider economic turmoil in the **Irish** market has now begun to affect retail sales, which have now fallen year on year. As a result of this, many national and UK retailers have scaled back expansion plans. However, there is still interest from retailers from continental Europe, as well as North America, with most notably the US retailer American Apparel announcing they are to open on Grafton Street. While there has been no clear decline in rents, it is now apparent that more incentives are on offer as a result of the current climate.

Despite consumer spending forecasts seeing a slowdown in 2008/9, retailer demand remains robust in the **Italian** retail market. However, demand remains focused on the 'fashion cities' of Milan and Rome. Rents remain broadly stable, and due to limited modern stock in both cities, under slight upward pressure. The development of new large shopping centres in regional cities is becoming a key trend. However, due to a relatively low existing provision of shopping centre stock, this is not expected to cause any threat of significant over supply in the short term.

While key cities across the **Netherlands** continue to see demand from retailers, this is concentrated in the prime locations. As a result prime rents in key locations remain stable, however, further rental growth is likely to be very limited. As in line with European trend, secondary locations are now facing tougher trading conditions.

Despite subdued economic growth forecasts for the **Portuguese** economy, the retail market is being affected in line with Europe as a whole, where prime locations continue to see robust demand, while secondary locations suffer. Vacancy remains low in prime locations, although rents are yet to come under any upward pressure as a result of this.

Demand from international retailers to enter the **Swiss** market continues to be high, despite Geneva and Zurich having some of the highest rents across Europe. Graff Jewels has now opened in Geneva, and discount retailers such as Aldi and Lidl continue to search for opportunities within the Geneva area.

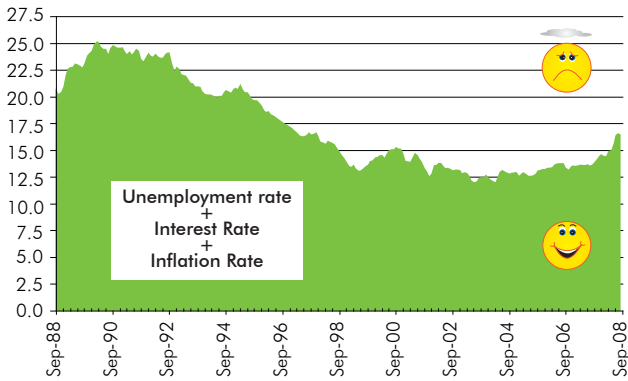
The **Hungarian** economy now faces a waiting game as hopes are pinned on the completion of the IMF/EBRD rescue package. However, some luxury retailers such as Gucci are still acquiring units as a part of their longer term strategic plans. In Budapest this is supporting the continued expansion and upgrade of Andr ssy  t, one of the most important retail destinations in the country.

The trend of retail development outside Warsaw has continued this quarter in **Poland**. Many regional cities are now becoming the focus for development, as Warsaw now has a relatively high stock per capita provision. Five centres opened in various regional cities during Q3 2008 with a further 300,000 sq m of stock planned to be delivered to the market before the end of the year. Rents remain stable throughout the country, but do vary significantly depending on the city and more specifically the centre.

Retailer activity in **Romania's** capital, Bucharest, saw some key tenant changes in the prime high street, Magheru Boulevard. Tom Tailor and Diverta have both now taken space, and there is further development happening in the street as a result of robust retailer demand. Rents are at present therefore continuing to see growth.

Russia continues to see a keen interest from many retailers, and demand continues to push up rents. There is a notable trend that interest is beginning to expand past the dominant regional cities, and into "smaller" cities (those with less than one million population).

EU-15 Misery Index

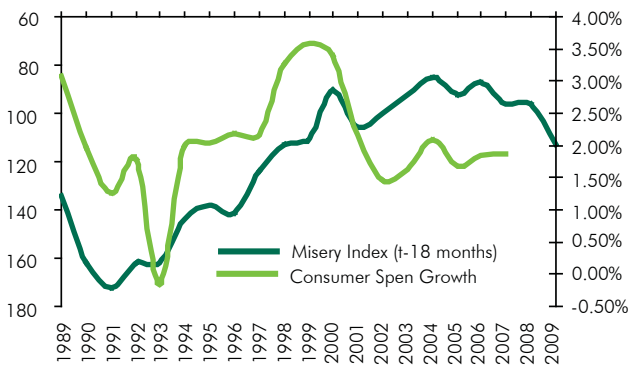


Source: Eurostat, CB Richard Ellis

CONSUMER SPENDING: THE MISERY INDEX

Consumer spending has been one of the key drivers of overall economic growth in Europe over the last few years. A key issue for European economic prospects – and for retailers in particular – is the outlook for consumer spending. Consumer confidence indicators, such as the Gfk survey shown on page 2, give us a snapshot of current sentiment but are not always a reliable indicator of medium term trends. However, it is possible to use a “Misery Index” to capture the underlying drivers of consumer behaviour and compile a better leading indicator of expenditure. The first Misery Index was developed by economist Arthur Okun in the mid 1970s. Over time the concept has evolved in a variety of ways, all of which are based on the premise that consumer willingness to spend is fundamentally driven by a few key economic variables. In order to calculate the CB Richard Ellis Index, our preferred composition of the Index is: **Unemployment Rate + Inflation Rate + Interest Rate**

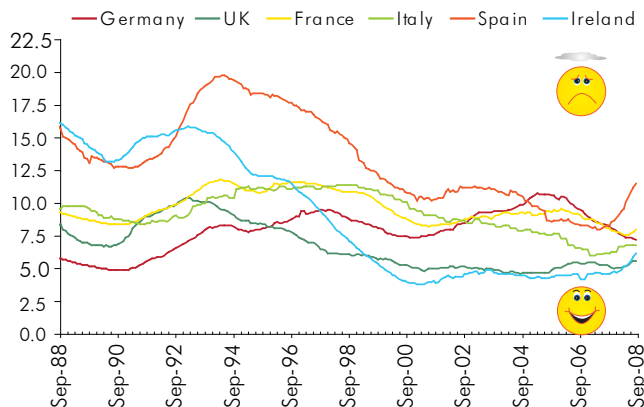
Misery Index (inverted) vs Consumer Spending Growth



Source: Eurostat, Experian, CB Richard Ellis

Whatever the actual rate of these variables, the higher they are the more miserable people feel, and the less likely they are to spend. Thus the threat of unemployment is likely to see consumers increase savings; the higher cost of goods (inflation) means less disposable income to spend on non-essential high street retail goods; and higher interest rates make it more expensive to borrow money, which reduces new expenditure on credit cards as well as absorbing a higher proportion of incomes in paying down existing debt.

Misery Index - Key Countries



Source: Eurostat, CB Richard Ellis

The EU-15 index has been rising quite sharply for the last twelve months. Even though it has not reached anything like the levels seen in the 1990s, it is the speed and direction of change which is notable. This is shown clearly when the change in the Index is compared directly with consumer spending growth. The increases already seen in the Index are therefore expected to have a dampening effect on spending over the coming 18 months. Even though interest rates and inflation will moderate during 2009, unemployment is set to rise and this will exert further downward pressure on consumer spending.

This suggests that the challenging environment for retailers is set to continue at least for 2009. It will therefore be those retailers who have a particular point of differentiation within their market – either based on product or price – who are likely to succeed despite tougher market conditions. Indeed, many such retailers are continuing with their expansion plans, taking advantage of current market conditions to grow their market share.

For more details about the construction and analysis of the CB Richard Ellis Misery Index, please see our EMEA ViewPoint on this subject.

CB Richard Ellis employs over 300 retail consultants in 36 countries across the EMEA (Europe, Middle East and Africa) region. The team provides expert, practical advice on all types of retail environment – from high street, to shopping centres, to out of town. Working with our network of research analysts, we are able to provide insight into retail market trends and consumer behaviour, as well as more conventional property market analysis.

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