

DOWNTOWN SHOPPING CENTERS – A MARKETING IMPACT ANALYSIS



Cities can achieve more for existing retail if they consider a well-integrated center rather than preventing it or leaving it potentially untapped by restricting size or parking, according to a study by Rainer P. Lademann. His research provides the first extensive, detailed findings on a controversial topic.

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1. STARTING POINTS

Since shopping centers are hardly ever built in non-integrated locations anymore, but predominantly in downtown areas, a controversial discussion has flared up about their effects on and ability to integrate into grown existing structures. While fears of losing the historical Central European urban structures prevail, supporters point out the high level of customer acceptance and the economic sustainability of centers.

The controversy is largely a result of the knowledge deficit about the marketing effect of downtown shopping centers. So far, the search for generalized studies that systematically quantify the effects has been in vain. Nevertheless, since 2006 a growing number of publications have come out that categorically reject center developments or, in favor of supposedly city-friendly management, make restrictive regulations on building permits, for instance concerning size, store mix, or parking capacity. Treatment without a reliable diagnosis is, however, neither a sustainable foundation for rational urban planning policy, nor for prosperous retail development.

2. DEMAND FOR ADEQUATE EPISTEMOLOGICAL PERSPECTIVE

The review of previous research and case studies on the effects of shopping centers showed that the knowledge deficit has two causes. Shopping center opponents in particular regard changes in retail after a center development compared to the previously existing situation as effects of the center. Furthermore, primarily methods like one-time surveys and footfall measurements or vacancy surveys are used in such a comparison reduced to two points in time, and these do not accommodate the complexity of spatial economic links. Both the simple pre/post comparison and purely descriptive methods impede the discovery of causal relationships.

Explaining and predicting the results of center developments is complex, because retail development in a market-based system with decentralized decision-making takes place between all participants, private and public. First and foremost, municipalities, investors, retailers, and customers react to each other, which is why shopping center developments and their consequences are to be analyzed over time, i.e. dynamically. For this reason it is invalid to draw conclusions about the effects of a center from simple pre/post comparisons. In order to do justice to the causality of center effects, it is necessary to evaluate how retail would have developed without a center development (zero alternative), in addition to a project forecast.

For example, an analysis of relevant official statistics on retail operations with ranges of goods typical of downtown areas showed an annual shop fluctuation of up to 14%. This inherent dynamic of use is to be differentiated from the center effects.

The development of the market after centers are built depends upon whether and how the participants react to each other for both the planned project and the zero alternative. One of the unresolved questions is, therefore, why retailers in some cities react to a center development with extensive adjustment measures (marketing and investments), whereas in others they accelerate their market exit through resignation. Lastly, the development of retail is overlaid with inherent change in forms of business as well as with numerous overall or regional economic factors that cannot be attributed to a center development.

3. SIGNIFICANT ADVANTAGES IN TURNOVER AND RENT COMPARED TO ZERO ALTERNATIVE

In response to this, a center database was developed that includes almost all new openings of downtown centers between the years 1990 and 2008 with data on residents, purchasing power, and rent as well as regional economic information (97 of 106), which allowed a series of different studies.

The rents also served as indicators for the development of turnover. Initially the course of average rents showed that they had been declining for 15 years in downtown areas before a center was built, only to increase again in the 15 years after the center opened. This indicates that center developments were predominantly opened in cities with declining appeal and thus were not the cause of the observed drop in rent.

Because other influences could have also played a role over such long periods of observation, an integrated longitudinal (19 years) and cross-sectional analysis (97 centers) was conducted (panel regression) for the period from 1990 to 2008 with which the development of rents could be explained since the reunification. In order to isolate the influence of other factors of the center impact, numerous potential variables were investigated to test their explanatory power for the development of

rents. In the end, the development of rents was best explained by including the following as variables: the size of the city, the population growth, and the influence of the existing rent levels typical for the time series on the rent development. Because time series data, including rents, is often influenced by an overlapping trend, a trend variable was also factored in. This captures, for example, effects of decentralization trends through expansion, inflation, or long-term location factors. Including the variables used for the center development, the regression model explains over 98% of the rent fluctuations in 1a or prime locations and over 90% in the 1b locations (second-highest category).

RESULTS:

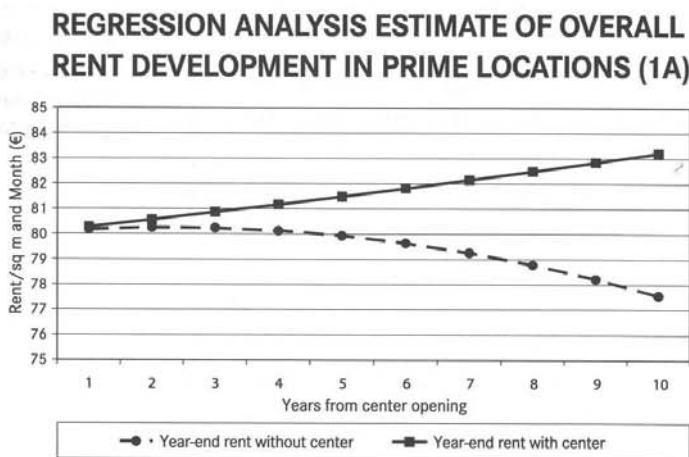
- A center development in prime locations effectuates a significant, not random, reversal of a previously negative trend in rents. The trend reversal is stronger than the earlier negative trend, resulting in an overall increase in rents.

- In 1b locations a center development considerably diminished the previous negative trend. This applied universally for smaller or larger cities, smaller or larger centers, and cities in eastern or western Germany.

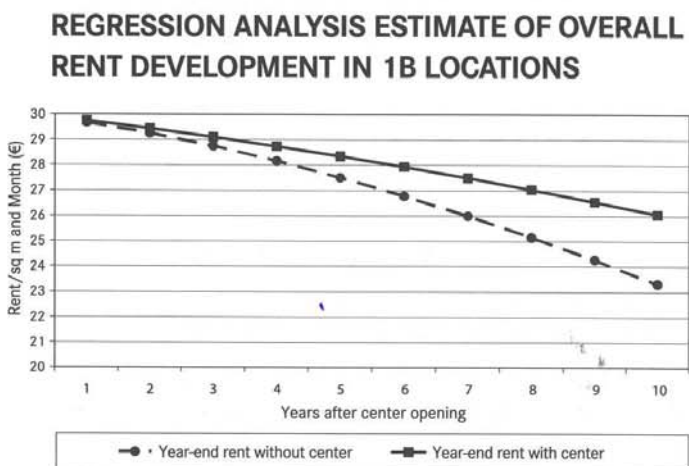
- Individual evaluations of prime locations (1a) according to center size showed that with larger centers and in larger cities the development of downtown centers had a more positive effect than smaller centers or in smaller cities.

- Even though the positive influence of a center development in prime locations in the new federal states was stronger than in western Germany, the considerably more negative trend in the east could not be fully compensated. In western Germany, on the other hand, the center developments significantly raised the rents in prime locations.

Consequently, center developments confirm the predictions of agglomeration theory and always cause an absolute and relative improvement to rent and turnover development of a city's downtown compared to a zero alternative. With-



SOURCE: OWN CALCULATIONS



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out center developments, rents in prime locations would be 7% lower within 10 years calculated without further changes of other factors (cf. figures).

The rent level in existing retail is also a good 9% higher in 1b locations compared to a zero alternative, whereby the decline in rent was considerably dampened. Therefore, center developments do not cause the observed erosion of rents, but rather mark the turning point from a downward to an upward movement.

In a further evaluation, the rent development was analyzed in a five-year period both before and after center opening. This includes center developments between 1976 and 2003 that were opened predominantly in western Germany for historical reasons. This analysis shows the following significant relationships:

- In the prime locations there were disproportionately high positive turnover and rent developments overall. Furthermore, significant or highly significant increases in turnover and rents were visible in existing retail with newer center developments, openings in the new federal states, in cities with less than 120,000 and more than 300,000 residents, with mid-sized (15,000 to less than 25,000 sq m of rental space) and large centers (over 25,000 sq m), as well as with centers with a high proportion of typical downtown product lines.
- In contrast, minor decreases in turnover and rent were observable for 1b locations in cities with populations from 120,000 to below 300,000.

These findings underscore that, with regard to the size of the city, relatively larger centers generally have more favorable effects on turnover and rent for existing retail than (too) small centers, which clearly lack the power to draw customers as, based on the city's market potential, the demand is already tied more to the downtown area. In addition, smaller cities profit more from a center development than mid-sized cities, one of the reasons for this being that the relative turnover supply effect through the higher proportion of centers in downtown retail is greater than in larger cities.

4. CHAMBERS OF INDUSTRY AND COMMERCE (IHKN) CONFIRM SUCCESS OF INTEGRATION

These findings were also confirmed through a parallel survey conducted by the author of the German Chambers of Industry and Commerce, which assessed the downtown development after centers were built in their chamber districts. Here it was shown that existing retail was predominantly able to profit from center developments, and negative effects (loss of turnover, vacancies) were mainly in scattered locations but hardly appeared in 1b locations. Participants in center developments were, therefore, generally successful in working out solutions that were advantageous to the city, existing retail, and investors and thus benefit the consumer. Failures in urban planning are the exception.

5. UNIVERSAL RECOMMENDATIONS FOR CENTER DEVELOPMENTS DAMAGE CITIES AND RETAIL

The results of the study underscore that cities achieve more for existing retail if they consider a well-integrated center rather than preventing it or leaving potential untapped by restricting size or parking. Along with the best possible network of walkways connected to the surrounding area, parking capacity should be established that also allows tie-in sales with the nearby retailers. Furthermore, this analysis shows that the positive effects for the municipality in which the center is built are more likely to come from centers that are large enough to exploit the market potential of a city, while (too) small centers by those standards can weaken the existing retail. For this reason, rigid limits are to be rejected for urban development, because they stand in the way of customized solutions for cities, which also benefit existing retail.

The study by Rainer P. Lademann can be purchased in German as a book for €39 from Göttinger Handelswissenschaftliche Schriften (GHS 2011, Band 77, ISBN 978-3925327-93-3) or by emailing info@dr-lademann-partner.de.



RAINER P. LADEMANN,

CEO of Hamburg based Lademann & Associates GmbH, is an economist focused on competition and spatial economics. His goal was to quantify selected marketing effects of downtown shopping centers beyond the individual case, thereby reducing a gap in research.

