potloc

The future of Canadian shopping centers.

Introduction.

Canadians malls, while in better shape than their American counterparts, are facing headwinds. Traditional anchor tenants such as Sears and Target have closed down in recent years, consumers are increasingly opting for online shopping, and a decrease in car ownership are just a few of the issues real estate operators have to deal with to keep their shopping malls alive.

The old tactics of increasing parking space, securing anchor tenants and flashy franchises are no longer at the core of staying relevant and attractive. Consumer behaviour has shifted dramatically and adapting to that evolution has become a matter of survival.

Canadian mall owners took notice and they are aiming to redefine the mall experience. Rather than merely being a place people go to shop, malls are striving to be a place where people go to enjoy themselves. High-end dining, indoor entertainment and investing in technologies that allow them to better understand and serve their audience, are just a few examples of how they're doing it.

Despite the turmoil, Canadian malls are not going away. They're just going to look a lot different from the teenage hang-outs of the pre-internet era.

In this white paper, we explore some of the tactics mall operators in North America are implementing to face these challenges. Curious? Read on!

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Shoppertainment.

One of the main problems shopping malls had to face in the wake of the mobile phone and the online shopper, is that they lost their biggest appeal: Convenience. Why go to a shopping mall if you can order the exact same thing on your phone? No driving, no lines, no crowds and no hassle. The mall shopper's experience became stale and boring. And "boring", is the worst thing you can possibly experience if you are Millennial or Gen-Z.

The solution? The shopping mall had to become an entertainment destination in itself. And Canadian operators have not ignored the call for more vivid, colourful and sensory experiences. The equation is crystal clear: more time spent in the mall translates to additional purchases, better conversion rates, and repeat business.

The show must go on

Some are likening the new mall experience to a playground or theme park that meets consumers' sensory needs and that cannot be replicated online. A prime example of this is Cirque du Soleil. They recently announced they are launching family entertainment centers in malls across Canada in partnership with real estate company Ivanhoé Cambridge.

When it comes to shopping, Millennials represent a huge target market, making up approximately 26 percent of the Canadian population, or about 9 million people. Their shopping journey is highly technology-based. Online shopping plays a part in this, but their decision-making as consumers is also heavily-based on social media hype or popularity. Malls can leverage this by offering an all-in-one approach that offers hype, convenience, new experiences and highly instagrammable moments. How? →

> Consumers expect more — they desire more than mere shopping. They want a unique experience. Those who strive to provide that kind of environment offer an exclusive shopping offering, high-end entertainment and haute cuisine.

Make it pop!

Moving away from anchor tenants and dedicating that space to pop-up shops that provide products trending on social media is a great start. Pop-ups enable malls to generate excitement with consistent new offerings rather than locking companies into leases. With the right offerings, tactics like these can lead to long lines of consumers, eagerly waiting to purchase. A great example of this is CONCEPT, a 3,600 square foot multi-tenant space devoted to pop-ups created by Toronto's Yorkdale Center.

Co-work to the rescue

To make the best use of all their space, malls are now extending their offerings to include co-working spaces. In Mississauga, the Mindshare Workspace is a 4,000 square-foot flexible workspace for startups and local businesses. A developer approached the Mindshare founder and there are plans to create more workspaces in other malls across Canada.

Bon appétit!

Shopping is one major aspect, however opportunities to keep people in the mall to continue socializing after they have finished shopping also need to be tapped into. As malls are turning into entertainment centers, the traditional food court is getting a makeover. Malls now strive to offer their customers a higher-quality food experience, with better restaurants establishing themselves in shopping centers.

Darryl Schmidt, vice-president of national leasing for Cadillac Fairview, notes that fine dining is increasingly being offered in Canadian malls:

> *In the last three years, we've increased the amount of premium, casual restaurants in our shopping centers by 35 percent and that's going to continue. That's not a fad. That's a trend. We're going to continue to increase the amount of dining options, both on a fast food basis with food halls and with premium casual restaurants.*
>
> – Darryl Schmidt

20%

The total real estate space dedicated to food & beverage by 2025 in the global market.

Source: International Council of Shopping Centers.

Specialization.

Canadians malls are extending their recreational offerings and finding innovative ways to attract and retain shoppers. Yet, the gap between high and low performers is still widening. Successful venues such as Yorkdale in Toronto welcome up to 18 million savvy consumers each year while other malls are being abandoned. So what is happening? In one word: specialization.

The one-size fits all department store strategy is no longer relevant as the middle class explodes into many different consumer cohorts with different needs and purchasing behaviours.

Rich malls, poor malls

Since 2012, retail sales in North America have been climbing — both online and in-store. In absolute terms, the growth of physical retail (brick and mortar) contributes to half of the market's entire growth.

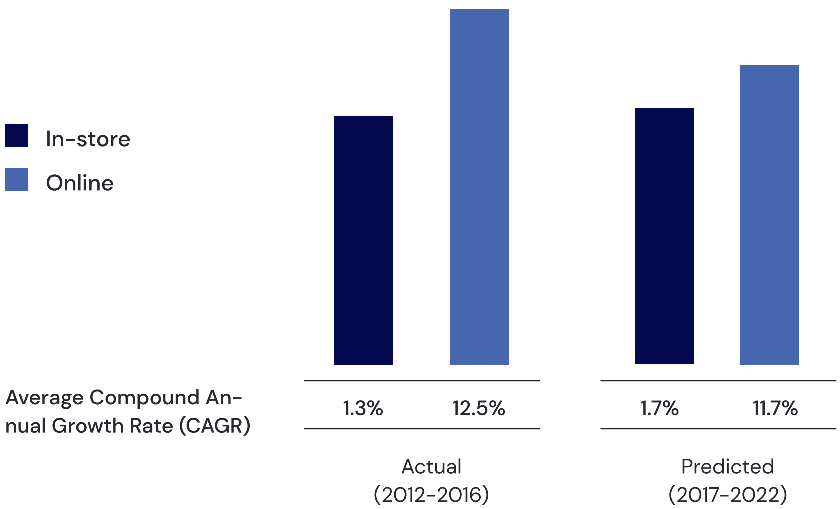
That's one of the interesting facts that emerges from The Great Retail Bifurcation, a Deloitte study that cross-references American macroeconomic data and consumer socio-demographic profiles to decipher the trends that are going beyond this e-commerce vs. brick and mortar battle.

Thus, if all of the economic indicators are increasing, the true riddle of today's market is this: how did retail get its floundering reputation in a time when its ground is clearly so prolific?

If we check under the hood, part of the explanation resides in the massive disparities between consumers. In the United States, the 1% received 82% of the wealth generated in 2017. Over the last decade, 80% of consumers have watched their economic situations deteriorate, causing irrevocable changes to their consumer habits. Shopping habits are intrinsically linked to income brackets and retail has been shifting as a reaction to America's economic situation. Deloitte's analysis separates retailers into three categories to glean a more detailed understanding of this phenomenon.

First, discount stores that base their market value in low, attractive prices. Second, more "balanced" retailers that rely on promotions, product variety and shopper experience. Third, retailers that offer differentiated high value-added products. According to Deloitte, the rupture between weak and strong revenues can be found among retailers.

Channel growth: Annual average sales growth



Source: IBIS World and Deloitte Insights

If we look at retail sales according to economic status, the richest are making their profile group skyrocket. On the other end of the spectrum, smaller income and middle-class households are rushing to discount stores to compensate for their loss of buying power, leaving our second category of retailers without a solid clientele reference point. If understanding the consumer is the key to gaining footing in this industry, the companies that neglected this are paying the price. Consumer research should therefore be implemented as standard practice within the industry (more on that topic in chapter 5.)

Today's constant access to technology is transforming the habits and needs of consumers. Comparing products and prices is easier than ever before, and flow of access has opened the door to new competitors on the market.

> In a market where offering a personalized shopping experience fosters customer loyalty, retailers cannot forgo understanding their clientele. Retail is exploding into smaller, niche markets where each type of client brings their own set of unique expectations, so consumer research is essential to understand the split.

40.8%

In Canada, the 20% richest segment of the population held more than 40.8% of total incomes.

Source: World Bank

46.6%

In the United States, the 20% richest segment of the population held more than 46.6% of total income.

Source: World Bank

Yorkdale shopping center: finding your niche

Amidst all the upheaval in consumer demand, some shopping malls in Canada are adapting to the changes surrounding them by becoming specialized. A select few, like the Yorkdale Shopping Center, are reaping major benefits.

What exactly is happening to the profit margins of shopping malls in Canada? Several factors play a part, including the rise of ecommerce, evolving consumer tastes, and the Millennial generation, who bring their own unique spending habits.

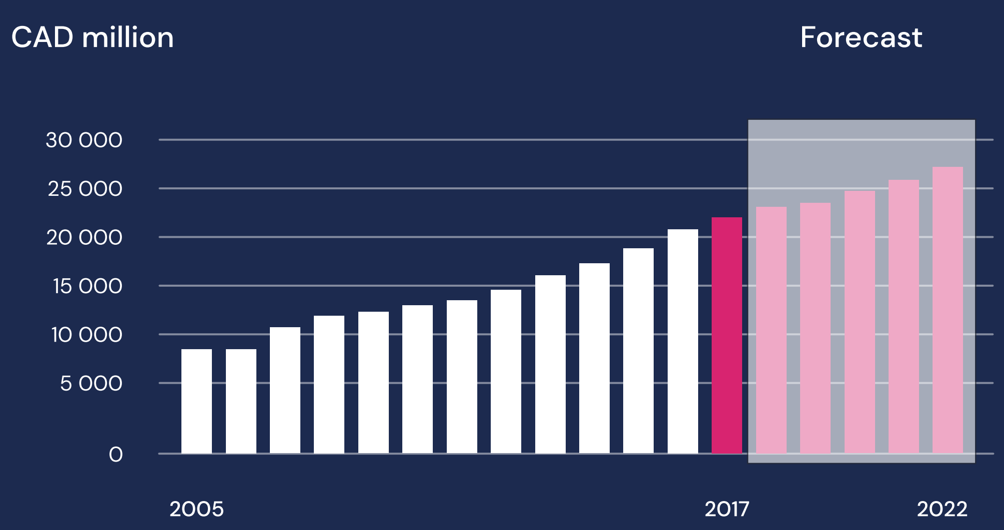
As per the Huffington Post, the rise of specialty retailers — like stand-alone stores for brands such as Hunter Boot Ltd and Canada Goose — and discount stores, including Walmart and Dollarama, are also luring shoppers away from former Canadian mall staples like Sears.

Finally, the Millennials on which malls so desperately depend aren't driving cars as much as their parents did, which reduces their mobility. They also prefer to spend money on experiences, like travelling, rather than on material things.

The result is that the savviest mall operators have been forced to change strategies and reinvent their spaces.

Yorkdale Shopping Center has been a model example in that regard. According to the Globe and Mail, the North York mall lists annual sales figures of $1.6-billion, generated by 18 million visitors.

Sales of luxury goods (Retail Value RSP)



Sales of luxury goods reached 21 861 million canadian dollars in Canada with a 70% increase between 2010 and 2017. Sales of luxury goods are expected to reach 25 000 million by 2020.

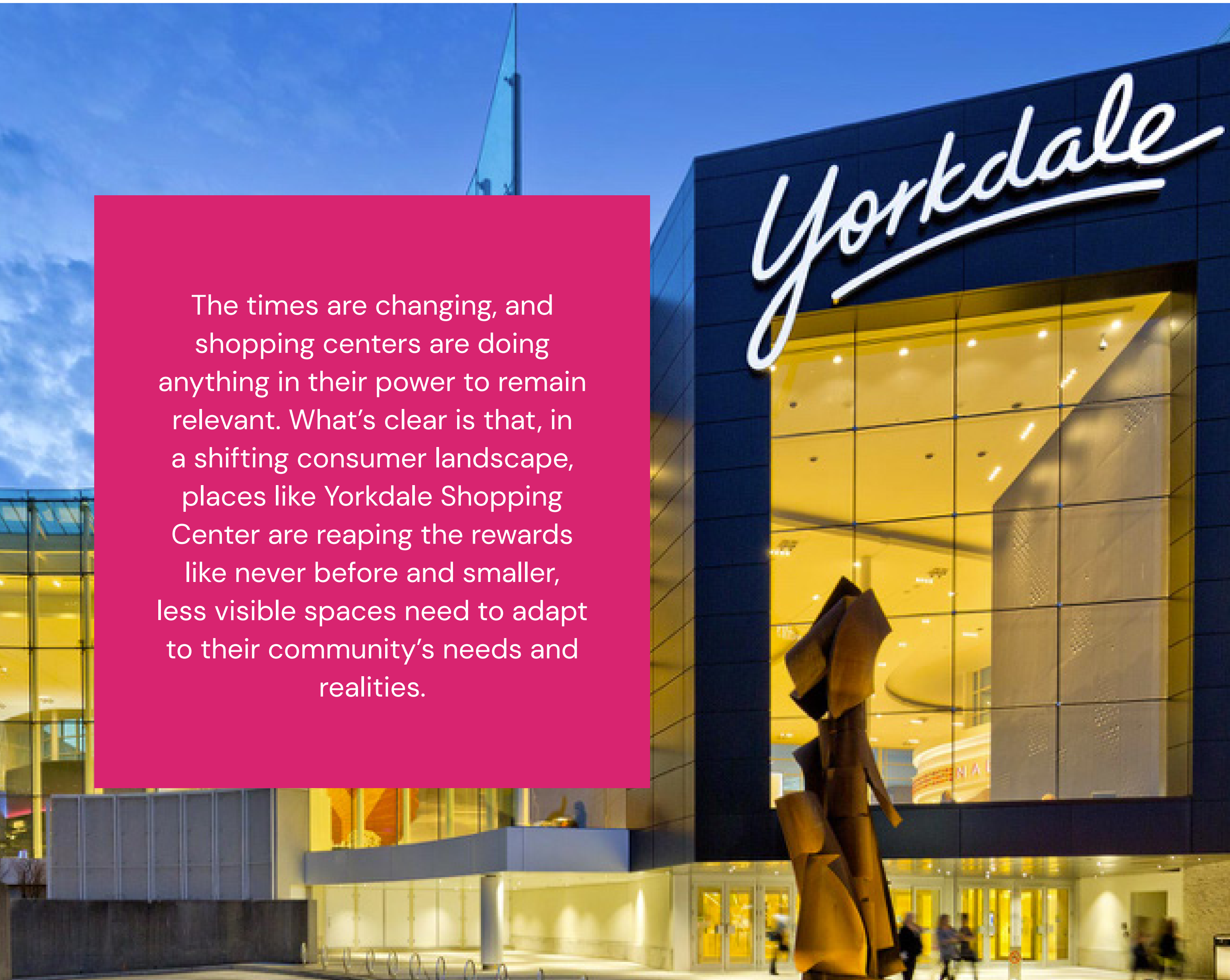
Source : Euromonitor

As Toronto's upper class population grows, along with it comes a larger demand for high-end fashion, beauty, tech, and housewares. But Yorkdale doesn't just use luxury brands to entice new generations of shoppers. As the Huffington Post explains, they doubled down on food offerings that draw in shoppers and keep them inside longer, bringing in a Jamie Oliver restaurant and, more recently, Canada's first Cheesecake Factory.

It's all paying dividends, too: Yorkdale leads Canada's malls in sales per square footage, according to the Retail Council of Canada.

Clearly, this can't be replicated across Canada. A mall in Moose Jaw, Saskatchewan simply isn't blessed with the same foot traffic that Yorkdale attracts every day.

Armin Begic, director of the retail business group and market research firm NPD Group, told Huffington Post that malls in smaller cities will replace large anchors with multiple, smaller tenants featuring the type of experiences their customers want. An example of this type of creative retailer could be Indigo Books & Music Inc., with its cafes, book clubs and children's toy areas.



The times are changing, and shopping centers are doing anything in their power to remain relevant. What's clear is that, in a shifting consumer landscape, places like Yorkdale Shopping Center are reaping the rewards like never before and smaller, less visible spaces need to adapt to their community's needs and realities.

74,000

The number of retail stores and services housed inside Canadian shopping malls

Source: Ryerson University's Center for the Study of Commercial Activity

Malls within malls: RAAS

A unique retail concept that involves creating a mini-mall within a larger shopping center is preparing to expand to other venues following its successful debut at the West Edmonton Mall, where Retail as a Service (RAAS) concept was launched last fall.

The concept follows the format of the "Souk", the millennia-old public markets that you can find in places like Morocco or Turkey, where each vendor has a "stall" –maximizing the use of the space and introducing more variety. The West Edmonton Mall did this by allocating just over 5,000 square feet to a minimum of 20 local retailers, with the capacity to hold as many as 30.

Michael Kehoe, an Alberta-based retail specialist with Fairfield Commercial Real Estate in Calgary, said the RAAS project is a great incubator for startup retail entrepreneurs and established retail brands that wish to set up pop-ups to test drive specific merchandise lines in a new market.

"The concept is transferable to other shopping centers or non-retail venues. RAAS is a throwback to the great Souks of the Middle East that were the world's first shopping centers, some dating back over 1,500 years," said Kehoe.

> *Many retailers that get their start in locations such as the RAAS — where store sizes are small, rents are often affordable and lease terms likely flexible — go on to lease brick and mortar stores and become long-term shopping center tenants.*
>
> \- Michael Kehoe

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Thinking outside the floorplan.

Innovative ideas are popping up everywhere to optimize the retail space malls previously filled with fast food chains and department stores.

Today, when a mall manager tries to make the most out of their expensive retail space, they go beyond the obvious: they turn to micro-stores, residential units, entertainment venues and ephemeral stores.

As a result, gigantic venues are no longer attractive, while highly flexible and specialized tenants are filling up vacancies. In other words, small is beautiful.

Honey I shrunk the store!

More square footage no longer means more sales, as many big box retailers have shut down and many shoppers prefer the convenience of online shopping. Meanwhile, commercial rents have increased both in the US and Canada, especially within desirable postal codes. As a result, retailers are increasingly maximizing their square footage and implementing “smaller is better” strategies, while mall operators are building out spaces to accommodate them.

Downsizing vs rightsizing

“Downsizing” and “rightsizing” are two terms with similar meanings, yet they often translate very differently within the context of the retail sector.

Downsizing mostly refers to planned shutdowns of retail locations and laying off a substantial number of employees. The primary motive is to reduce labour and operating costs and therefore comes with a negative connotation.

$1,257

The average sales per square feet in the 10 most productive Canadian shopping centers.

Source: Retail Council of Canada

On the other hand, rightsizing is a more positive concept. Rightsizing occurs when a company restructures its human resources to align with company goals and strategies. This may include a combination of department and position cuts to make room for a more efficient use of a store's existing square footage, based on customer demand and preferences.

US-based department store chain Kohl's recently adopted a rightsizing strategy with encouraging results. Kohl's has shrunk hundreds of stores in its fleet of 1,160 locations from 90,000 square feet to about 60,000. Furthermore, the company is developing an even smaller 35,000 square foot store model at 12 locations hoping to reach new markets, including downtown locations.

This rightsizing strategy aims to maintain brand presence, improve inventory management through "unsexy but essential technologies" and help support e-commerce activities, given that many shoppers prefer to pick up orders in-store (online shopping represents 18% of the company sales as of April 2018). During the holiday quarter, Kohl's sales rose 6.3%, aided by a 7% drop in inventory.

Canadian malls will survive

According to a report released by Colliers, it's not all doom and gloom for Canadian shopping centers. In fact, the disappearance of anchor tenants like Sears and Target from prime locations across Canada has been (or will be) replaced with several retail chains such as Nordstrom, La Maison Simons and Saks Fifth Avenue.

Meanwhile, retail sales are still growing. The Colliers report said total national retail sales in 2017 amounted to $588.83 billion, 6.46% increase from 2016.

The opportunity of zombie shopping malls

Reviving a shopping mall that is losing momentum is difficult and risky business. When you lose giants like Sears, JCPenny or Target and grass is growing between the cracks in the parking lot, it doesn't look good. On the other hand, huge parcels of land, strategically located near major roadways, provide undeniable advantages.

Some struggling shopping centers are converted into warehouses for Amazon, university campuses, office buildings, hospital centers, or churches. "I predict that three quarters of them will be converted according to lifestyle," said Ben Conwell, a retail expert at Cushman & Wakefield, an American commercial real estate broker.

In fact, reviving a dead mall is more like avant-garde urbanism.

Live in it!

"You don't drive there, you live there!" read a headline in the Globe and Mail, reporting on the redevelopment of the Honeydale Mall in Toronto. Soon, there will be several condo towers, green spaces and new businesses along the streets.

"Cities are gradually moving from an automobile-dominated culture to mobility-based on a mix of means of transportation," said Brent Toderian, President of the Canadian Institute of Planners.

Shopping centers surrounded by a sea of asphalt will be converted into urban green spaces, where public transport, walking, cycling and self-driving shuttles have replaced automobiles, which have been relegated, at worst, to underground parking lots.

Even better, hotels and theatres are joining the ranks in shopping centers, as demonstrated (successfully) at the DIX30, in Brossard, which will soon become the Montreal South Shore lightrail terminal for the Réseau Express Métropolitain managed by the Caisse de dépôt et placement du Québec.

In Vancouver, 14 new 44-storey towers are being constructed in the skyline of the Oakridge Center, featuring green roofs, 2,600 apartments, 500,000 square feet of office space, one million square feet of pedestrian street shopping, and 10 acres of green space. Sales now total $1,600 per square foot, the second highest in the country, according to its promoters.

0,1%

Between 2012 and 2017, department store revenue fell by an annualized rate of 0.1% to $28.1 billion.

Source: IBISWorld

Cities are gradually moving from an automobile-dominated culture to mobility-based on a mix of means of transportation.

– Brent Toderian

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Understanding the community.

Amazon's vision "to be Earth's most customer-centric company" had a huge impact on the retail industry as a whole as they focused their attention towards the communities they serve. It single-handedly made customer centricity a top priority for many retailers.

Today, the best performers understand that acquiring new customers is five times more expensive than keeping existing ones. As a result, shopping centers are trying harder than ever to understand their clients and delight them in every possible way. The industry has taken many different paths to reach this goal.

The data driven shopping center

Mall owners that outperform the competition understand that they have to measure everything they can about their shoppers as knowing the community they serve is essential to their survival.

Measuring foot traffic and sales per square foot isn't enough anymore. Today, as consumers no longer need to visit a shopping mall, it is the work of the mall operator to know as much about their shoppers as Amazon knows about theirs. And this understanding shouldn't be limited to existing customers, but also non-shoppers that belong to the community the shopping mall serves. Tailoring experiences with them in mind, is a great way to convert them.

Just like retailers, malls are investing in rewards programs, indoor navigation apps and other systems to gather data about their shoppers, from traffic flow to customer feedback. Those investments are paying off. According to a Deloitte Digital survey, retailers that are investing the most in data aggregation and analysis have seen a revenue increase of more than 10% in the past fiscal year.

Surveying the community that lives, works, plays and transits around your shopping mall location is essential to tailor the experience for them while increasing your revenue and generating loyalty.

Combining this approach with external surveys that are able to measure not only shoppers, but also non-shoppers and the community surrounding the property as a whole, is a great way to pinpoint what consumers want and how to attract new business.

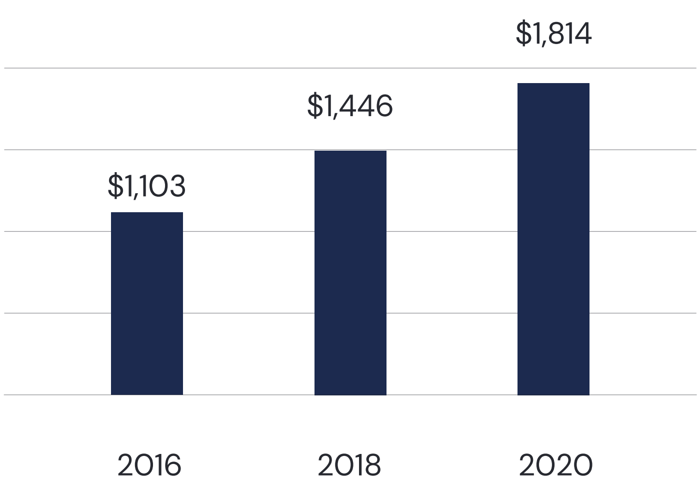
Unified systems

Westfield was one of the first large mall operator to invest massively in big data. In 2012, it set up Westfield Labs, an innovation lab that developed a comprehensive solution to track client traffic flow and purchases across all the retailers in its malls, and share the collected data with them.

Pooling the data collected by mall operators and retailers alike allows shopping centers to deliver a better experience to shoppers across their entire journey. It helps them make better decisions in terms of to whom they rent out their retail space, what stores should be where, and so on. Furthermore, such a system allows malls to improve the customer experience of their shoppers, by offering useful services, such as digital receipts, across all their retailers.

Canada's big data services market, 2016 - 2020 ($ millions)

1.1 Billion



In 2016, Canada's big data service market generated $1.1 billion in revenues. The market size is expected to increase by 65% before 2020.

Source : ICTC INDUSTRY CANADA (2015)

$1.25 billion

The expected size of the global chatbot market by 2025 with an annual growth rate of 25%.

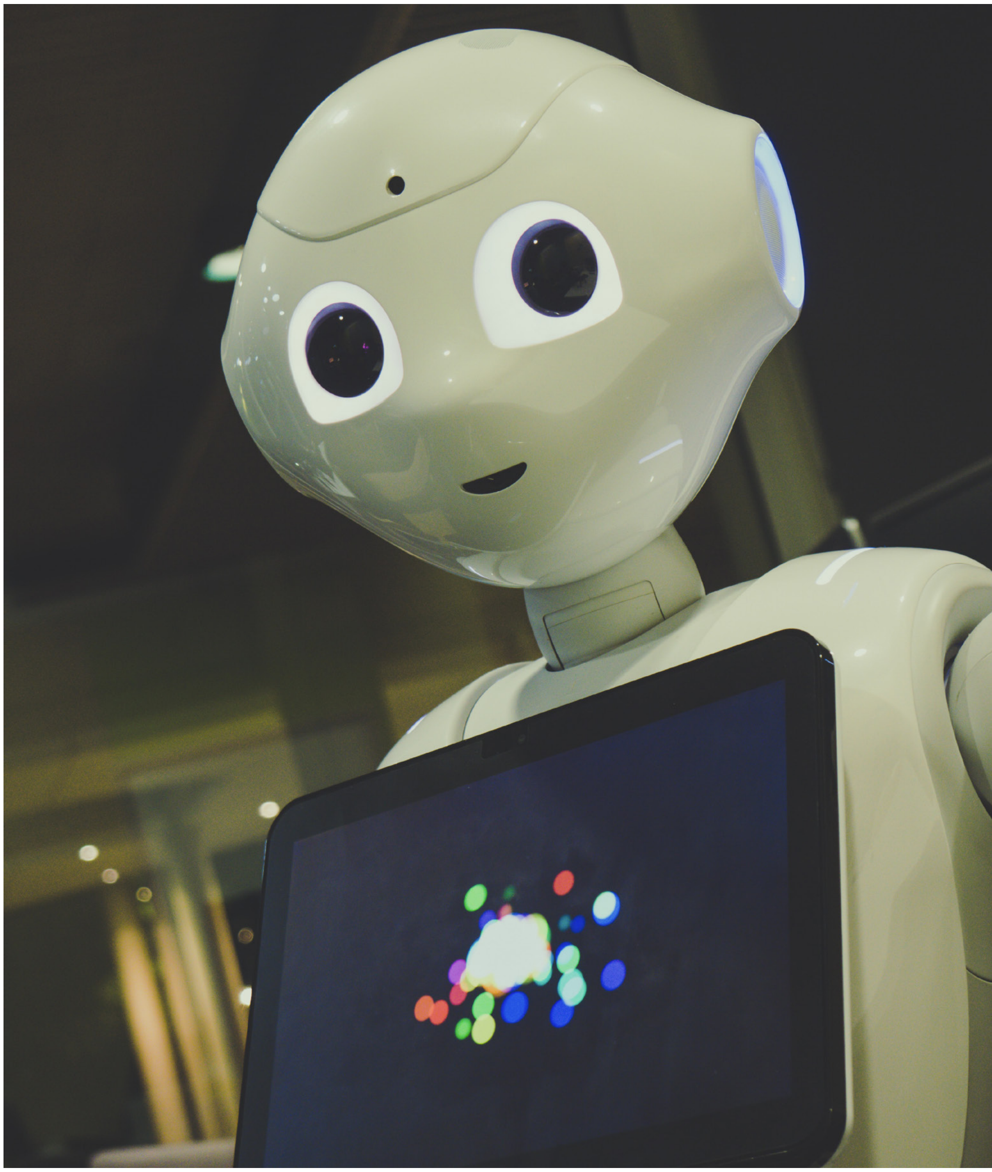
Source: Grand View Research, Inc

Talk to a robot

Digital conversational agents, commonly referred to as "chatbots," are becoming more and more common in malls. These chatbots allow malls to leverage data to provide a better customer experience and collect customer feedback.

The Mall of America in Minnesota (the biggest shopping center in the United States, and one of Potloc's customers) has recently launched a conversational agent initiative. In December 2017, the mall introduced a new app designed by Satisfi Labs. It is available via the Mall of America website, mobile app, Facebook page, and Amazon Alexa.

Additionally, three semi-humanoid Pepper robots conceived by SoftBank Robotics are on hand to guide lost shoppers to their desired store or attraction; and can even provide suggestions.



Indoor navigation

While mall operators need data to understand the traffic flow of shoppers within their space, shoppers often struggle to find specific retailers once inside a mall. Needless to say, that is a business opportunity in itself. According to a report from Markets and Markets, the indoor location market could be worth $41 billion by 2022.

Many current systems utilize WiFi or Bluetooth beacons installed around a given location, which can communicate through a user's phone and offer real-time directions similar to GPS.

The trend hasn't fallen into deaf ears. Microsoft launched an app called Path Guide that helps users find a place or room inside a shopping mall, even if GPS is not available. And Toronto-based Mapstead developed an app that works even without WiFi, Bluetooth or an internet connection.

Lost shoppers equals frustrated ones. Mall operators must keep in mind that the consumer experience should be as pleasant and seamless as possible. Indoor navigation is one of the elements in that equation and –as it evolves– it'll become a great tool to measure and drive foot traffic.

Measuring client satisfaction

On average, the industry's Net Promoter leader outgrows its competitors by a factor greater than two times. It's not surprising that the Net Promoter Score (NPS), a measurement of client satisfaction, has become a reference point for shopping centers, who are using various strategies to perform NPS surveys. Many of them employ their mailing list to survey their clients, using anything from their WiFi network to an indoor navigation app to retrieve their shoppers' email addresses. Other ways to perform NPS surveys is to have surveyors question shoppers as they exit the mall (intercepts), or to perform social media surveys with providers such as Potloc.

Choosing the right audience

NPS can be an excellent Swiss Army knife for the industry, capable of obtaining different information according to the surveyed population. Here are three audiences malls are targeting: shoppers that visited a mall over the course of the last 12 months, shoppers that are shopping at a competing mall, and specific population segments that are part of the mall's client base.

A competitive advantage

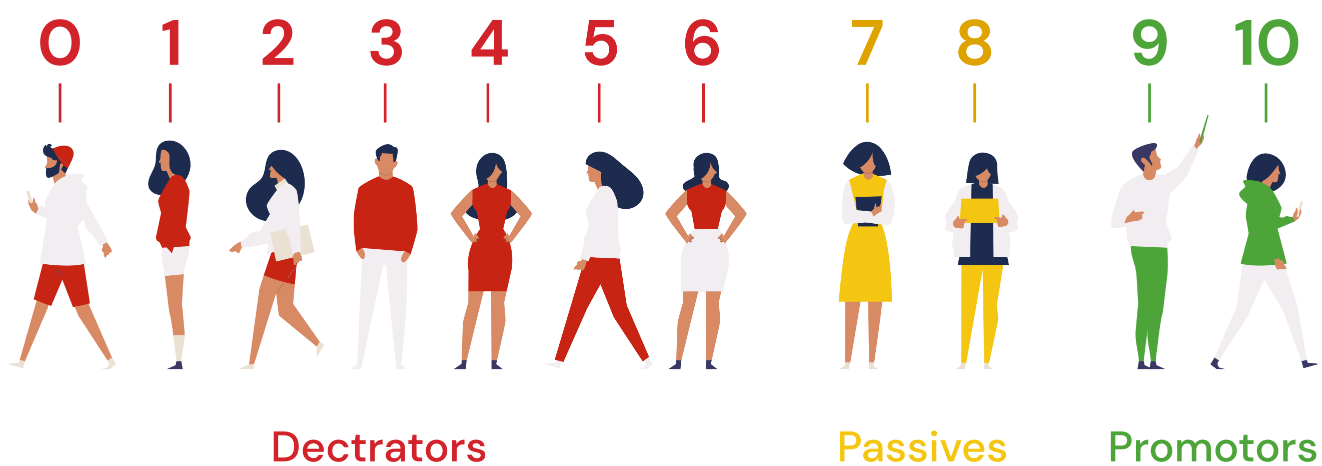
According to Bain & Company, NPS is an excellent indicator of potential growth. We've seen it happen: the business with the best NPS in their respective industry grows twice as quickly as their closest competitors. Based on this argument alone, brands have become increasingly interested in NPS. Furthermore, if your shopping center receives a high score, it can add value to your recruitment process when searching for quality tenants.

How to calculate the Net Promoter Score (NPS)

A company’s NPS is obtained by asking its customers one simple, effective question:

“On a scale of 0 to 10, what is the likelihood that you would recommend Company X to a friend or co-worker? ”.

Those surveyed are then sorted as detractors, passives and promoters based on their responses.



The NPS is calculated by using the difference between the promoters and the detractors:

NPS = % OF PROMOTERS — % OF DETRACTORS

Going beyond your shoppers

Competitive opportunities are also presented in the form of non-shoppers and mall operators should not neglect them when surveying their community. Understanding why a segment of your audience is not visiting your shopping mall or why they are choosing a competitor is crucial to optimize the customer experience.

With the right strategy, those not currently shopping at your center could become customers and even ambassadors. All it takes is understanding what they want and tailoring the experience for them. This applies to all consumers around the community you serve and this is where hyper-targeted consumer research comes into play.

Did you enjoy this WhitePaper?

At Potloc, we reinvented consumer research by placing consumers at the heart of the process, so you can understand their shopping habits and needs.

If you want to see how we do it, visit us at Potloc.com

About Potloc

Potloc conducts thousands of geo-targeted surveys using social networks, completely reinventing consumer research for retail and commercial real estate. We are driven to give people a voice in their communities and empower the businesses that serve them with valuable insights. Hundreds of businesses use Potloc to understand their consumer base and solve strategic challenges. Headquartered in Montreal and founded in 2014, Potloc has grown to nearly 60 employees, with global offices in Canada and Europe. Check us out at Potloc.com