
2 Market for retail tenancy leases

This chapter examines the scope and nature of the retail tenancy market to provide some context for the assessment of potential constraints on the efficient operation of the market and possibilities for change.

Section 2.1 discusses the range of premises and businesses that are included in the market in relation to the type of goods and services retailed, and the size, experience and resources of market participants. Section 2.2 considers the availability and use of retail space for different types of premises. Ownership and management of retail space and the businesses that use the space are also discussed. Finally, section 2.3 reports on how these differences relate to current vacancy rates and the ability of businesses to enter or leave different parts of the retail tenancy market.

2.1 Scope of the market

Businesses operating from retail premises

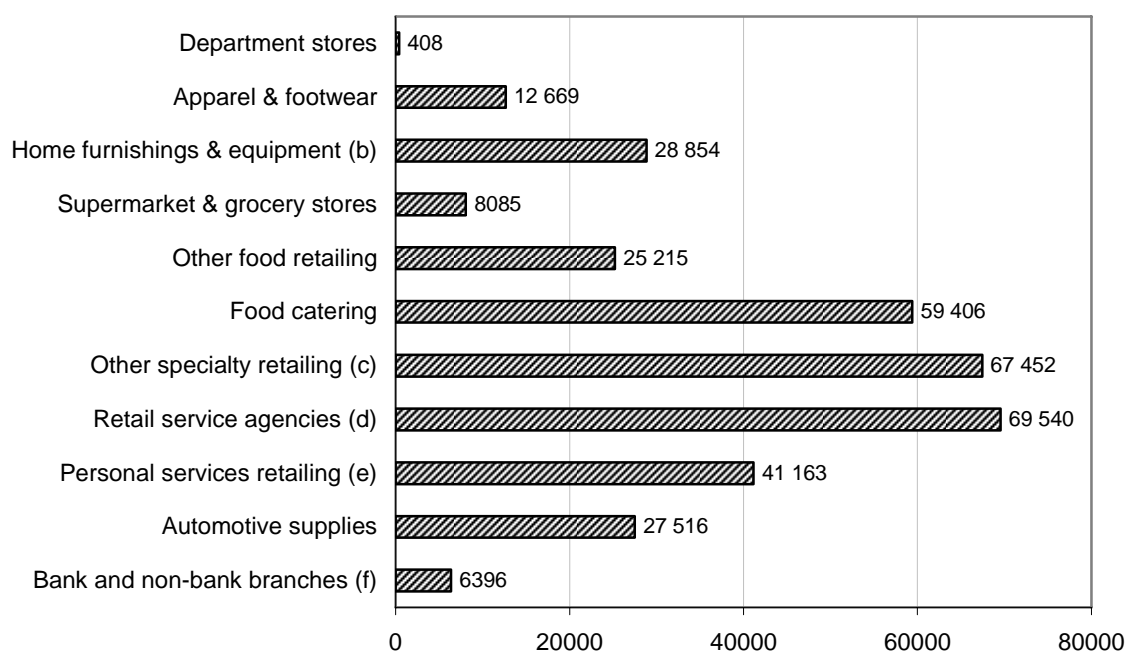
The market for retail tenancies exists to provide space for the provision of all manner of final goods and services in a retail format to the general public, including individual household and business customers.¹ Retail space may be owned by the retailer, but usually is provided by landlords in many formats including stand-alone premises, neighbourhood shops and large shopping centres.

There may be up to 350 000 businesses currently operating from retail premises including department stores, supermarkets, specialty retailers, retail service providers, and branches of banks and non-bank financial institutions (figure 2.1). The most prevalent activities of businesses operating from retail space are food catering (such as cafes and restaurants), ‘other’ specialties (such as recorded music, leisure products and books and stationery) and retail service establishments (such as

¹ The concept of ‘retail’ used here is broader than the concept of ‘retail trade’ adopted by the Australian Bureau of Statistics (ABS). The ABS (2006) defines retail trade to cover the provision of *goods* without ‘significant transformation’ to the general public. The broader concept adopted in this inquiry focuses on retail space used in the provision of *goods and services* to the general public in a retail format (such as a shop or store) and encompasses both traditional ‘retailers’ and also ‘non-retailers’ who operate from retail space.

travel agents, post offices and real estate agents). Together these three groups account for over half of all businesses operating from retail space.

Figure 2.1 Businesses using retail space in Australia, June 2006
Number^a



^a A business is defined by the ABS to include both entities that are registered as an Australian Business Unit and larger more complex entities that the ABS defines as a 'business' on the basis of their 'type of activity'. Because businesses may operate from more than one location (that is 'establishments') they may have more than one retail tenancy. ^b Includes fabric and soft good retailing, furniture, floor coverings, domestic hardware and houseware and domestic appliance retailing. ^c Includes retailing of recorded music, leisure products, books and stationery, photographic equipment, marine equipment, pharmaceutical and cosmetics, antiques and used goods, garden equipment, flowers, jewellery, retailing nec. and household equipment repairs. ^d Includes agencies for travel, post, telecommunication, real estate and insurance. ^e Includes optometry and optical dispensing, lotteries, video hire outlets, personal and household goods hiring, laundries and drycleaners, film processing, hairdressing and beauty salons, and personal services nec. ^f Refers to the number of branches, as reported by the Reserve Bank of Australia, rather than the number of businesses published by the ABS.

Sources: ABS (*Counts of Australian businesses, including entries and exits, June 2003 to June 2006*, Cat. no. 8165.0, Canberra); Reserve Bank of Australia (2007).

Of the businesses that use retail space, a proportion own the premises from which they operate and therefore do not have a lease. For other businesses, the size, location and its ownership structure (such as a public company) will determine whether they are required to enter into a lease that is regulated by relevant State or Territory retail tenancy legislation or enter into a commercial lease (Minter Ellison 2006). For example, leases of some larger furniture stores and hardware stores may not be within the jurisdiction of retail tenancy legislation because the floor area exceeds a legislated cut-off size (typically 1000 square metres). Similarly, a branch of a bank can be required to have a retail tenancy lease if located in a shopping centre, but a commercial lease if located elsewhere.

There are estimated to be around 290 000 retail tenancy leases in Australia (table 2.1), with an estimated 58 000 new (or renegotiated) leases each year. Just under 20 per cent of leases are for retail space located within shopping centres (box 2.1).

Table 2.1 Estimated number of leases by State, 2006-07

<i>Jurisdiction</i>	<i>Number of leases under tenancy regulation</i>
	<i>'000</i>
New South Wales	97
Victoria	72
Queensland	52
South Australia	20
Western Australia	35
Tasmania	6
Northern Territory	3
Australian Capital Territory	6
Australia	290

Source: Productivity Commission estimates, see box 2.1.

FINDING

There are an estimated 290 000 retail tenancy leases in Australia. Just under 20 per cent of these are for businesses located within shopping centres.

Box 2.1 **Estimating the number of leases for retail space**

There are no consistent statistics on the number of leases for retail space across Australia. However, the number of businesses using retail space in Australia (350 000) potentially stands as an upper limit to the number of leases. Some of these businesses are owner-occupiers and therefore do not have leases. Further, a subset of these will be larger businesses that may have a commercial rather than retail lease.

Some information is available on leases held by smaller businesses that use retail space. In Victoria, leases for retail space under the *Retail Leases Act 2003* are required to be notified to the Office of the Victorian Small Business Commissioner when the lease is established or renewed. In recent years, the number of notified leases has been around 14 500 each year. Assuming an average lease term of five years, this suggests that there are around 72 500 leases regulated under retail tenancy legislation in Victoria. Given that Victoria's share of the Australian economy (as measured by gross state product) was around 25 per cent in 2006-07, and extrapolating to a national basis, this suggests there could be close to 290 000 leases regulated by retail tenancy legislation across Australia. The number of leases under retail tenancy legislation in other jurisdictions can be similarly estimated from each State's share of the national economy.

Based on figure 2.1, about 192 000 of the 290 000 leases across Australia would be held by firms retailing goods and 98 000 by firms providing retail services. This is broadly consistent with the estimate of the Shopping Centre Council of Australia of around 180 000 to 200 000 'retailers' with retail leases (submission no. 83, p. 10).

Almost 60 000 businesses (or just under 20 per cent) that use retail space are estimated to be located within shopping centres, as defined by the Property Council of Australia (PCA). The remainder are located in retail strips and stand-alone retail premises such as bulky good sites and direct factory outlet sites. This is consistent with the Shopping Centre Council of Australia estimate that shopping centres make up only 19 per cent of all retail locations (submission no. 83, p. 10).

Based on the Victorian small business numbers and extrapolating nationally, the number of new leases negotiated each year is estimated to be around 58 000.

Sources: Office of the Victorian Small Business Commissioner (2007); ABS (*Australian National Accounts: State Accounts*, Cat. no. 5220.0, Canberra); Productivity Commission estimates.

Participants in the retail tenancy market

Businesses participating in the retail tenancy market are diverse in terms of size, experience and resources. Ownership and management of both lessors and lessees can span sole ownership by an individual with minimal education and experience, to small syndicates of informed professionals, to large multinational corporations with extensive experience and resources. The interaction of businesses in the market for retail tenancies is illustrated in box 2.2.

While relative size is often the focus of perceived concerns in the relationship between landlord and tenants in the retail tenancy market, there are many other influences including business experience and acumen, information and understanding, due diligence on their own behalf and the use of specialist advice. In addition to these influences, the relationship is influenced by general market conditions including the level of consumer demand and consumer preferences for particular products and shopping formats, and the supply, format and location of available space.

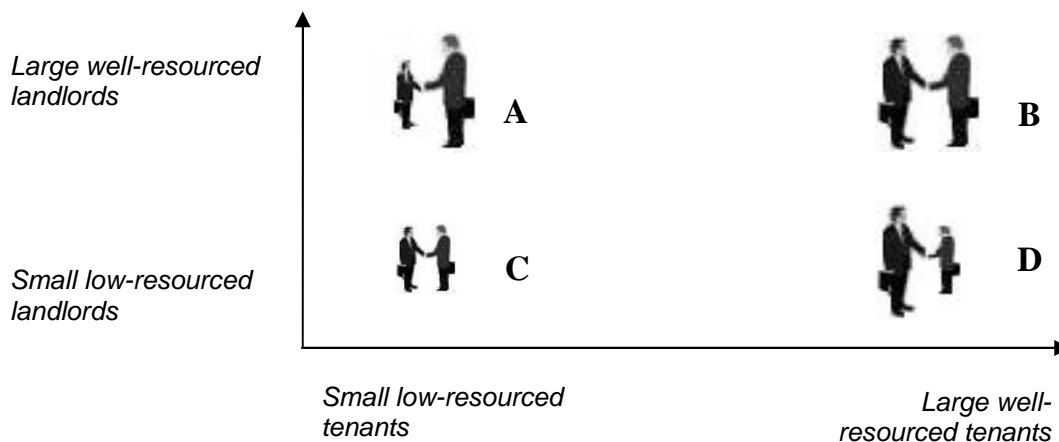
Changes in retail formats

The market for retail tenancies is complex and dynamic (box 2.3). The traditional form of retailing based on retail strips or high street shopping has gradually moved towards greater concentrations of shopping under single ownership (as in supermarkets and departments stores) and single management (as in shopping centres). The grouping of small retailers within shopping centres with a single and often ‘large’ landlord has become more commonplace since the 1950s and 1960s. Nevertheless, while this concentration has been occurring in one part of the market, other shopping formats (such as ‘bulky good’, ‘direct factory outlet’ and internet shopping) have also emerged.

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The retail tenancy market comprises a wide range of businesses that vary in terms of the format of retail space provided, goods or services retailed, their size, experience and resources.

Box 2.2 Interaction of businesses in the retail tenancy market



- Case A represents relatively 'small' tenants operating in a competitive/atomistic market, located in retail premises operated by a 'large' landlord. While the individual tenant may have virtually no influence on the shopping environment or the way it is managed, the tenant can choose whether or not to pursue such a tenancy under the conditions offered. Tenants can also inform themselves of the implications of a lease through their own business acumen, information and understanding and due diligence, and through specialist advice. Some tenants may have trading skills or product lines highly sought after by centre managers and therefore may have some strength in negotiations with a landlord.
- Case B represents large tenants interacting with large, well-resourced landlords. Both have the means and experience to look after their own interests.
- Case C represents small low-resourced landlords interacting with small low-resourced tenants. Each is on a roughly equal footing in terms of size, although both groups may need to seek advice on the implications of lease obligations, complex legislation and documentation. The negotiating position of each will also be influenced by market conditions and the business acumen and knowledge of individual traders.
- Case D represents large tenants interacting with relatively small landlords. This situation may occur, for example, in smaller centres or in country areas, but is not very common because of the substantial investment required to provide retail space for larger tenants. The landlord's negotiating position will be heavily influenced by market conditions and the attractiveness of the property on offer relative to other available retail space.

Although there are invariably some tensions in situations B, C and D, it is the perceived bargaining imbalance in case A that has formed the basis for government intervention in the retail tenancy market. Indeed, most retail tenancy legislation has been introduced to deal with case A, though it also applies to case C which is, in fact, much more common. Cases B and D, with large tenants are generally excluded in the coverage of tenancy legislation, on the basis of either floor space used or turnover.

Box 2.3 **The changing face of retailing**

The traditional layout of retail space in many countries, including Australia, has been town centres with streets lined with retailers. In such a setting, there are potentially many owners of retail space and a large number of tenants. In Australia, a trend from this so-called 'shopping strip' or 'high street' arrangement to arcades and department stores began in the late nineteenth century. This was facilitated by the supply of adjacent retail space with the same owner and the capacity to construct larger stores.

'Chain stores', characterised by a single owner (often a corporation) with a number of similar stores in separate locations or markets, emerged gradually in the early 1900s, and proliferated from the 1950s with an expansion of shopping into suburbs and regional centres. 'Shopping centres' offering retailing and public facilities in an enclosed space with car parking, emerged in the 1950s and 1960s with urban expansion, increased use of cars, and consumer demands for 'one-stop' shopping in a comfortable and accessible environment. Scarcity of city-centre land and the increased scope that shopping centres (often multi-storey) provide to co-locate a large number and variety of retail outlets, gave further impetus to the growth in shopping centres. With this expansion, tenancy models of a single landlord with many tenants became more commonplace.

Nevertheless, other retail store-based formats have also experienced substantial growth, including: 'direct factory' outlets which spread in popularity and number during the 1970s and 1980s; 'bulky good' outlets which have enjoyed rapid growth in recent times; outdoor coffee/food retailing in shopping strips, promenades and other locations; boutique/trendy clothes stores in high profile shopping strips; and convenience stores (often in association with petrol retailing).

There has also been a growth in non-store formats such as street markets and electronic retailing. Shopping centres and department stores have responded to this growth by including speciality areas within their centres and stores and, in some cases, offering internet purchasing.

Despite very strong growth in non-store retailing in recent years (off a small base), store-based retailing remains overwhelmingly the dominant form of retailing. For example, store-based retail sales represented an estimated 96.5 per cent of total retail sales of merchandised goods in Australia in 2005.

Sources: Kingston (1994); DEH (2001); Euromonitor International (2006); submission no. 112, p. 5.

2.2 Provision and use of retail space

In 2005-06, it is estimated that there were around 45 million square metres of retail space in Australia, up from an estimated 33 million square metres in 1991-92 (figure 2.2). The Shopping Centre Council of Australia (SCCA) estimated that a further 1.1 million square metres of retail space was under construction around

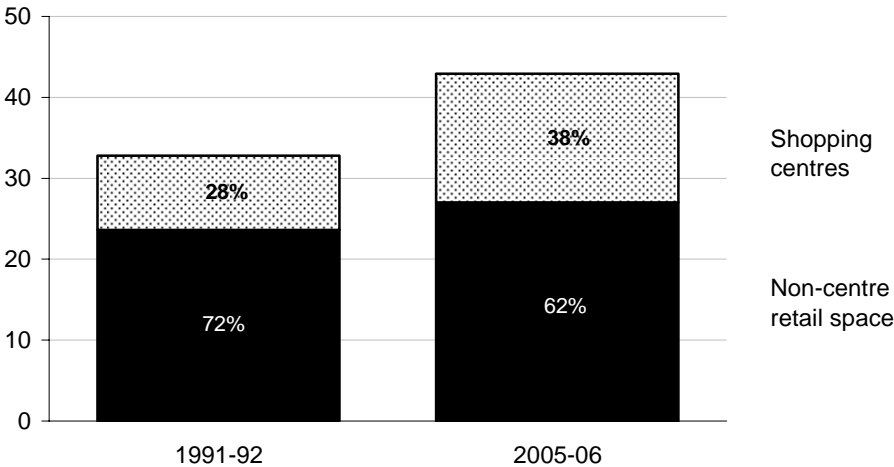
Australia in early 2007 (submission no. 83, p. 51). Most retail space is located outside of shopping centres in retail strips or, increasingly, in stand-alone premises such as ‘bulky goods’ sites and ‘direct factory outlets’. The Bulky Goods Retailers Association submitted that the increase in floor space of Australia’s key bulky goods retailers over the period from 2004 to 2007, exceeds that typically contained in five regional shopping centres (submission no. 126). Jones Lang LaSalle (2005) similarly estimated that bulky goods was likely to account for about 40 per cent of new retail space supply in 2005-06.

Reflecting above average growth in shopping centres as a major retail format, the contribution of shopping centres to total retail space increased from 28 per cent in the early 1990s to 38 per cent in 2005-06. Shopping centres also accounted for around 40 per cent of the value of all sales by retail businesses in 2005-06 (submission no. 83, p. 2). However, not all of these retail sales or retail space relate to businesses with retail leases — as discussed in section 2.1, many businesses in centres operate with a commercial lease and are not covered by the retail tenancy legislation. Nevertheless, the majority of submissions received in this inquiry relate to shopping centre tenancies.

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While most retailing occurs outside of shopping centres, centres nevertheless represent a growing share of the total market. Within the non-centre retail market, stand-alone bulky goods sites and direct factory outlets are increasing in importance relative to retail strips.

Figure 2.2 Retail space in Australia, 1991-92 and 2005-06
Per cent of total retail space provided



Sources: Submission no. 83, p. 13; PCA (2006).

Shopping centres

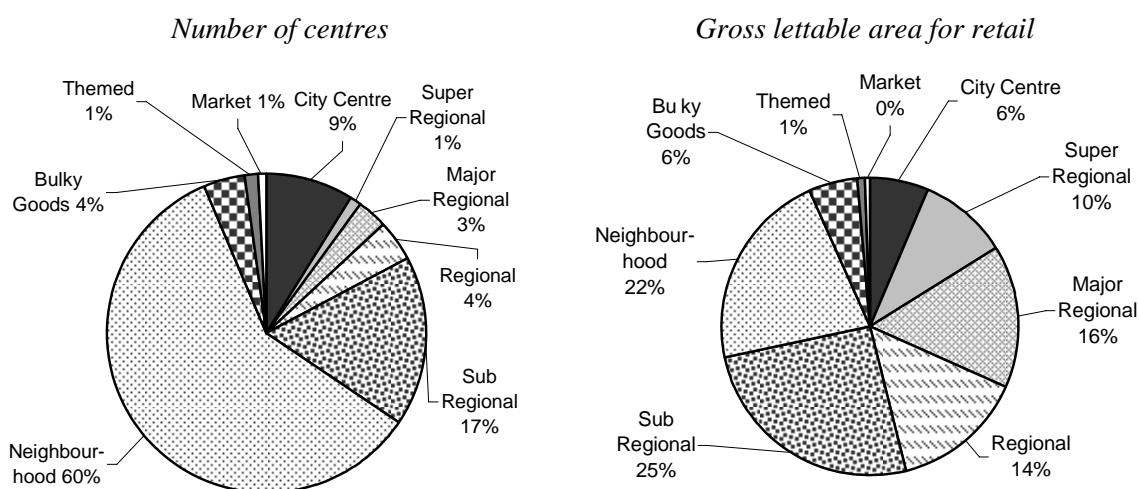
A broad perspective

Australia currently has some 1360 shopping centres, with around 16 million square metres of retail floor space operating in various types of centres (box 2.4).

While over half of Australia's shopping centres (60 per cent) are neighbourhood centres, they account for less than one quarter of retail space (figure 2.3). On the other hand, regional shopping centres (including regional and super, major and sub regional centres), account for one quarter of the number of centres, but provide 65 per cent of retail space in shopping centres or 25 per cent of all retail space. The largest shopping centres — super regional centres — while accounting for only 1 per cent of the number of centres, contribute 10 per cent of shopping centre lettable space — 4 per cent of all retail space.

The mix of centres offering retail space has varied over time. Urbis JHD (2007a) observed that, over the past decade, regional centres have declined in terms of their share of retail centre floor space while sub-regional centres and supermarket based centres have expanded. The SCCA submitted that this is likely to be due to several factors (submission no. 83). First, with the construction of new centres largely limited to those regional areas that have rapidly expanding populations, existing sub-regional and neighbourhood centres have been refurbished and extended. Second, the number of available anchor tenants in Australia is relatively low, restricting opportunities for the establishment of new shopping centres, as currently conceived.

Figure 2.3 Predominance of types of shopping centres in Australia, 2006



Source: PCA (2006).

Box 2.4 What is a shopping centre?

A shopping centre is a retail concentration in an enclosed space with some common public facilities. Shopping centres are differentiated according to the physical size of the retail concentration and the number and type of tenants. The following types of shopping centres are defined by the PCA (2006):

City Centre: an arcade or mall development, owned by one company, firm or person and promoted as an entity within a major Central Business District (CBD). Total retail gross lettable area (GLA) exceeds 1000 square metres and the centre is typically dominated by specialty shops and has a frontage onto a mall or major road.

Super regional centre: a major shopping centre aimed at one-stop shopping for all needs. Total retail GLA exceeds 85 000 square metres and the centre typically includes several comprehensive department stores, supermarkets, and around 250 specialty shops, in addition to a range of entertainment and leisure attractions.

Major regional centre: a major shopping centre incorporating at least one comprehensive department store, several discount department stores and supermarkets and around 150 specialty shops, in addition to some entertainment and leisure attractions. Total retail GLA generally ranges from 50 000 to 85 000 square metres.

Regional centre: a retail centre with an extensive coverage of retail needs. Total retail GLA generally ranges from 30 000 to 50 000 square metres and the centre typically includes a comprehensive department store, discount department store, supermarket and at least 100 specialty shops.

Subregional centre: a shopping centre that is typically dominated by at least one discount department store or major supermarket, but also includes 40 or more specialty shops. Total retail GLA is typically 10 000 to 30 000 square metres.

Neighbourhood centre: a local shopping centre comprising a supermarket and up to 35 specialty shops. These centres are typically located in residential areas and cater for basic day-to-day retail needs. Total retail GLA is usually less than 10 000 square metres.

Bulky goods centre: a medium to large shopping centre that is dominated by bulky goods retailers (furniture, white goods and other homewares), but may contain a small number of specialty shops. These centres are typically purpose-built and are located adjacent to large regional centres or in non-traditional retail locations.

Themed centre: a specialty shopping centre, located primarily in resort areas to cater for tourist needs.

Market: a covered centre of at least 5000 square metres dominated by food retailing with at least 50 stalls or outlets. It may operate on a permanent or irregular basis.

Outlet centre: a medium to large sized shopping centre which generally comprises specialty shops selling stock at discounted prices.

Source: PCA (2006).

Regional differences

As well as being variable over time, there are marked differences in the mix of shopping centres providing retail space across jurisdictions (figure 2.4). For example, in States and Territories with less concentrated populations, most retail space is located in neighbourhood shopping centres. On the other hand, the relative importance of super regional, major and regional centres tends to be greatest in the more populous jurisdictions — New South Wales, Victoria and Queensland — and in the Australian Capital Territory.

Ownership and management of retail space

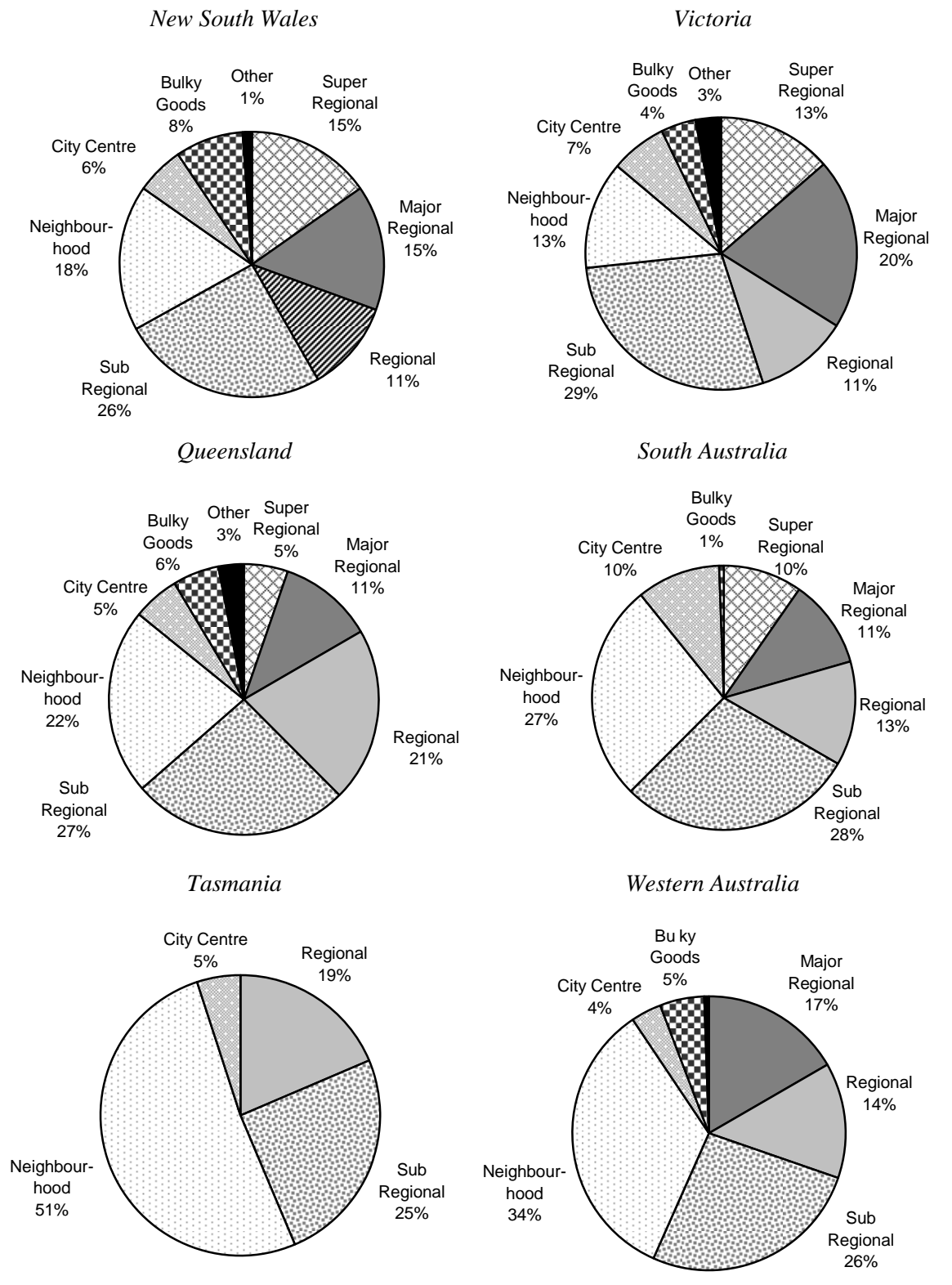
Who owns retail space in the strips and other non-centre locations?

The ownership of retail space in shopping strips, stand-alone bulky goods stores, direct factory outlets and other non-centre formats is widely dispersed and involves firms of all sizes and levels of skill, from small family investor/operators to large corporations. With respect to retail shopping strips, the National Retail Association note that:

... the majority of retail premises in Australia are in ‘main street’ locations, with widely dispersed property ownerships, and generally substantially lower sales and rentals. (submission no. 47, p. 6)

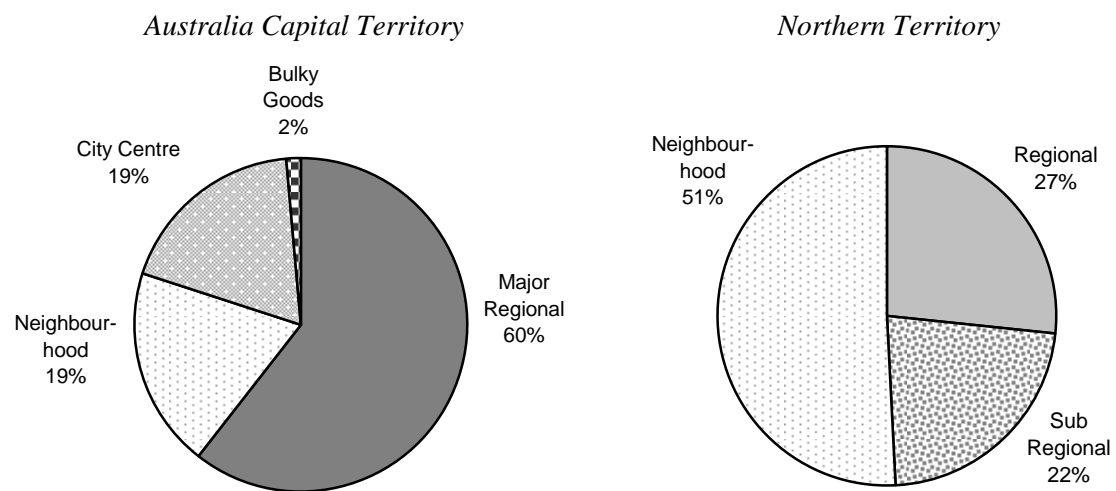
The relationship between landlord and tenant in these cases may be defined more by local market conditions and expectations than by the relative size, resources or experience of either party. There is often a large number of landlords competing for tenants within a given area.

Figure 2.4 Retail space by type of shopping centre and jurisdiction, 2006
 Proportion of total gross lettable area for retail



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Table 2.4 (continued)



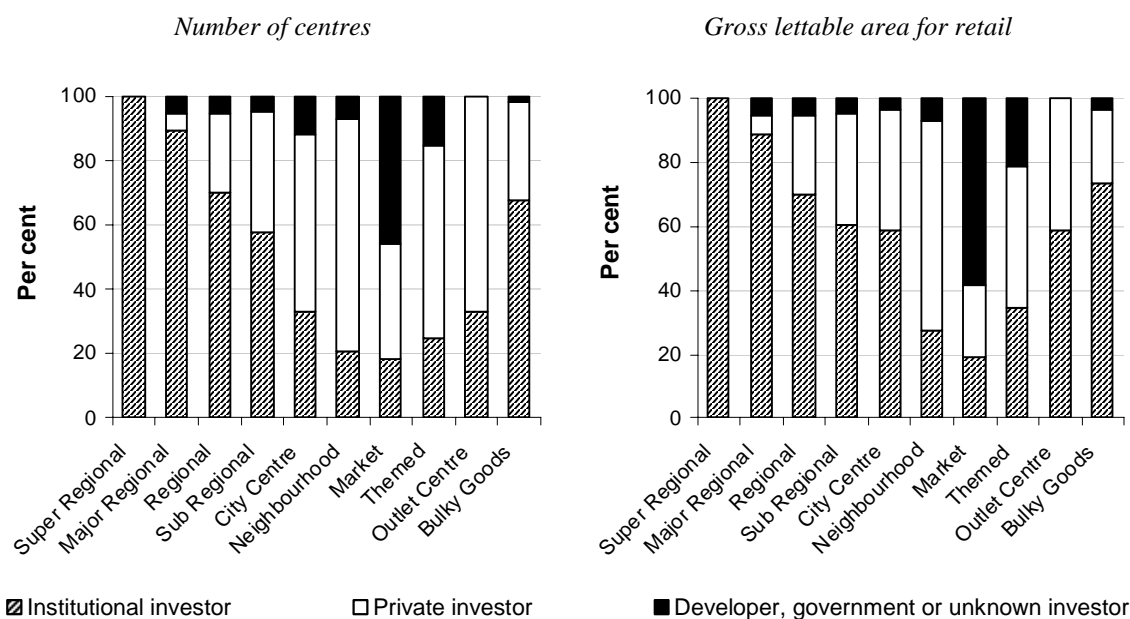
Source: PCA (2006).

Who owns the shopping centres?

The ownership structure of Australia's shopping centres is complex. The SCCA estimates that there are in excess of 500 separate owners of shopping centres around Australia (submission no. 83, p. 11). An estimated 63 per cent of all retail space in centres is owned by institutional or company investors, 31 per cent by private investors/owner occupiers, with the remainder owned by other parties, including developers and governments.

The prevalence of institutional and company investors as landlords for retail tenants is much higher in larger shopping centres — the super and major regional centres and the bulky goods and outlet centres (figure 2.2). Ownership of the larger aggregations of retail space is concentrated in the hands of a small number of large companies or investment funds. For example, 6 companies/funds own 85 per cent of the retail space in Australia's 15 super-regional centres. In this context, the Westfield Group is the largest shopping centre owner in Australia, with a financial interest in 44 centres, covering over 3.3 million square metres of leasable area and almost 10 000 retail outlets in 2006 (submission no. 85, p. 4).

Figure 2.5 Shopping centre owners by type of centre, 2006



Source: PCA (2006).

In contrast, the neighbourhood, city centre and themed centres are more likely to be owned by private investors, while the market centres are largely owned by developers, government or other investors. Each of the 31 market and themed shopping centres in Australia has a different owner.

On another level, the ‘owners’ of many of Australia’s shopping centres (particularly the larger centres) can be considered to be the millions of individuals who indirectly invest in shopping centres via numerous trusts and funds, or own shares in public companies that directly invest in centres. The predominance of property trusts and funds as owners of retail space has expanded in recent years with the growth in superannuation funds. This has financial benefits for centres in terms of an increased capacity to raise capital for centre expansion and redevelopment (box 2.1). As a consequence, many companies now own shopping centres via funds and trusts rather than through more direct ownership arrangements. For example, unlisted and listed property trusts purchased over two-thirds of all retail properties sold in 2006 (SCCA 2007). One of Australia’s largest wholesale funds managers is Queensland Investment Corporation (QIC), with ten Australian superannuation funds (representing 4.2 million individual investors) investing in its ‘Property’ or ‘Shopping Centre Funds’ (submission no. 46, p. 1). Similarly, Westfield point out that it has 131 000 security holders — 75 per cent of whom are institutional investors, with the remaining 25 per cent comprising individuals, companies or privately managed superannuation funds (submission no. 85, p. 4).

Box 2.5 Investment in shopping centres

With opportunities to construct new shopping centres largely confined to new growth areas and land releases, most additions to retail supply in recent years have been in the form of extensions and refurbishments to existing centres. Frank Knight observed:

Refurbishment and reconfiguration together with active management continues to be a crucial requirement for owners of secondary centres wishing to remain competitive. (submission no. 79, p. 10)

The SCCA reports that, at any given time, the equivalent of up to 10 per cent of a property's value could be expended annually on maintenance or upgrades (SCCA 2003). Indeed, the larger shopping centre owners report continuing expansion and redevelopment of their centres. GPT Group reports current and planned developments of \$1.5 billion (compared with a retail portfolio in Australia of \$3.5 billion at the end of 2006) (GPT 2006). Similarly, Centro Properties Group completed developments of \$426 million in 2006 and has a further \$362 million of developments that are either underway or have received board approval (Centro 2006). The total value of the Centro retail investment portfolio in Australia was \$3.1 billion at the end of 2006. Further, the Coles Group invests over \$400 million each year in new and replacement stores, refurbishments and shopping centre acquisitions and developments (submission no. 48).

The timing, nature and extent of investment in retail space may be affected by the scope for the centre owner to pass on redevelopment costs to tenants. Under State and Territory retail tenancy legislation, capital expenditure generally cannot be charged to tenants, but repairs and maintenance of existing structures and equipment can be. Additional costs associated with refurbishment that shopping centre owners incur include compensation payments to tenants who are either relocated or otherwise adversely affected during refurbishment.

Concentration of 'ownership' in shopping centres varies widely between jurisdictions. Tasmania, the Australian Capital Territory and the Northern Territory have the highest share of gross lettable area for retail space owned (and managed) by a single company (table 2.2). At most, around 30 per cent of centre retail space in a state is held by a single business — this level of concentration of ownership is not considered to be especially high.

It would be expected that in smaller regional communities which have less demand for, and supply of retail space, that ownership of that space could be highly concentrated. However, concentration of ownership of retail space within a localised region does not necessarily equate to market dominance in the control of retail space. A retail area with highly concentrated ownership may effectively be in competition with other providers of retail space if potential tenants are able to move to other sites and customers are willing and able to travel between retail locations.

There is some evidence that customers are willing to travel for some distance to undertake their shopping, expanding the potential for competition between retail locations. For example, around 80 per cent of households in Melbourne and the Australian Capital Territory travel up to 15 minutes (by any transport means) from their home in order to undertake their main household shopping for food and groceries (ABS 1994 and ABS 1997a). In regional Victoria and Tasmania, households generally travel for a slightly longer period to undertake household grocery shopping (ABS 1997b). Households may be willing to travel even further when shopping for large non-consumables or specialty items.

The potential for competition between providers of retail space within a region is evidenced by PCA data for two larger regional communities. In far north Queensland (around Cairns), the largest two shopping centre owners each have 22 per cent of total centre retail space, with the remaining 56 per cent of space distributed between 13 owners. In the Central Western region of New South Wales (around Dubbo and Bathurst), 63 per cent of centre retail space is distributed fairly evenly between five owners, with the remainder of centre space held by a further five owners.

The managers of retail space

Many retail tenants have little contact with the ‘owner’ of the premises — negotiations and practical operation of the lease are typically handled by a manager under delegation from the owner. This distinction between owner and manager introduces a crucial third party to retail tenancy operations.

The type of retail manager is typically aligned with the type of space leased. For example, space in a retail strip, if not managed by the owner/investor, is more likely to be managed by a local real estate firm than by a larger corporation. In contrast, shopping centres that are owned by large corporations or institutions tend to be either managed internally by a related entity, or else by separate specialist corporations or institutions engaged as managers. Available information indicates that the largest four managers of shopping centre retail space collectively manage 36 per cent of gross lettable space in centres across Australia (table 2.2).

Table 2.2 Shopping centre owners and managers by jurisdiction, 2006
Top 4 owners and managers, in terms of quantity of gross lettable retail space^a

	<i>Owners</i>	<i>% total retail GLA</i>	<i>Managers</i>	<i>% total retail GLA</i>
New South Wales	Westfield group	18	Westfield group	21
	Centro group	7	Centro group	7
	AMP group	6	AMP group	7
	Stockland group	5	Stockland group	6
Victoria	Colonial group	16	Gandel Retail Management	16
	Centro group	13	Centro group	13
	Westfield group	9	Westfield group	11
	GPT group	9	GPT group	8
Queensland	Yu Feng Group	11	Retail First	12
	Westfield group	7	Gandel Retail Management	8
	Centro group	7	Centro Properties group	7
	Stockland group	6	Westfield group	6
South Australia	Colonial group	15	Westfield group	20
	Centro group	12	Savills	16
	Australian Prime Property Fund Retail	10	Gandel Retail Management	15
	Westfield group	5	Centro Properties group	12
Western Australia	Centro group	14	Savills	13
	Westfield group	10	Centro Properties group	11
	Perron Investments	4	Westfield group	8
	Macquarie	4	Jones Lang LaSalle	8
Tasmania	Centro group	30	Centro group	30
	Colonial group	19	Gandel Retail Management	19
	Northgate Property Syndicate	12	Jones Lang LaSalle	15
	Glenorchy Plaza	5	Burgess Rawson	8
Northern Territory	GPT group	27	GPT group	27
	Joondanna Investments	13	Joondanna Investments	13
	Jape Nominees	12	Jape Nominees	12
	Yeperenye	6	LJ Hooker Group	9
Australian Capital Territory	Westfield group	31	Westfield group	41
	Leda group	20	Leda group	20
	QIC group	18	QIC group	18
	Christodoulou	3	Savills	4
Australia	Westfield group	11	Westfield group	14
	Centro group	9	Centro group	9
	Colonial group	7	Gandel Retail Management	8
	GPT group	5	AMP group	5

^a The GLA of retail space for centres that are jointly owned is allocated equally between owners. Owners and managers are grouped for presentation purposes on the basis of organisation name.

Source: PCA (2006).

With the growth in shopping centres as a major retail format over recent decades, there has been a fundamental shift in the way in which much of Australia's retail space is managed. In retail strips, there tends to be little intervention by the landlord's managers in the operation of the retail business utilising that space. In contrast, retail tenants in shopping centres (particularly specialty retail tenants in the larger centres) operate in a micro-managed environment. For these tenants, not only is the provision of retail space managed, but typically their lease provides for the centre manager to exercise some control over the commercial operation of the retail business itself.

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Concentration of ownership and management is not especially high at a State, Territory or regional level, although localised dominance of particular owners and managers may be more apparent in smaller communities.

Use of retail space

Businesses that use retail space are typically categorised by their physical size and type of activity and, in shopping centres, their potential for drawing large numbers of customers into a retail area. Broadly, tenants are described as being either a 'major' tenant or a 'specialty' tenant in a shopping location.

Major tenants

Major tenants are larger-sized retailers that attract significant numbers of customers to a shopping area and include supermarkets, department and variety stores. Major tenants operate in either retail strips or centres. In shopping centres, the largest of the major tenants are referred to as 'anchor tenants'. Anchor tenants typically occupy about 75 per cent of the available tenancy space in shopping centres and are seen to be an essential base around which the centre is developed. As noted by Stockland:

... anchor tenants are of paramount importance to the development and sustainability of shopping centres. In essence, a shopping centre is built around anchor tenants. (submission no. 88, p. 15)

In 2006, there were about 2300 major tenants in Australia's shopping centres. Up to 80 per cent of foot traffic in a shopping centre is estimated to be made up of customers who have come to the centre to shop at a department store or discount department store (SCISR 1997, p. 18).

The length of leases for major tenants ranges up to 40 years, although shorter terms, for example 15 to 25 years, are common. For example, the Coles Group submitted that leases and options for its stores can extend out to 40 years (submission no. 48). The longer duration leases provide stability in use of the relevant retail space to other retailers dependent on the foot traffic generated and to investors.

In Australia, there are only a small number of potential anchor tenants for shopping centres (submission no. 83) — only two major chains of department stores (Myer and David Jones) and three major chains of discount department stores (Big W, KMart and Target). This provides these tenants with a strong bargaining position in centre development, negotiation of their own tenancy conditions and conditions in the remainder of the centre in which they are located (especially when KMart and Target are owned by the same parent organisation). In particular, the anchor tenants can have some sway in determining the mix and location of smaller retailers within the shopping centre (SCISR 1997 p. 18).

Typically, leases of major tenants for retail space are not covered by State or Territory retail tenancy legislation, although coverage varies according to store size and corporate status of the business (for example, whether or not the business is a publically listed company).

Specialty tenants

A specialty tenant is a ‘non-major’ tenant that typically occupies less than 400 square metres and specialises in a narrow range of merchandise with an emphasis on product knowledge and customer service (PCA 2006). Specialty tenants provide a shopping region with product and service variety, and ‘character’. The nature of specialty retailers in a region often reflects the socio-economic status of the expected customer base, but can, in turn, influence the type of customers attracted to a shopping area.

The total number of specialty tenants is estimated at around 290 000 businesses in 2006 (table 2.1). Of these, about 57 000 specialty tenants, including retail trade and retail service businesses (such as travel agents, banks, Medicare and post offices) are located within Australia’s shopping centres (table 2.3). Specialty tenants occupy about 42 per cent of retail space in centres across Australia, although there is some variability between states. The proportion of centre space used by specialty retailers is, on average, significantly lower in Tasmania and the Northern Territory than elsewhere in Australia.

The amount of available retail tenancy space occupied by specialty shops also varies considerably between types of shopping centres. In the larger centres, specialty shops typically occupy about 35 to 40 per cent of the gross lettable area

for retail (figure 2.6). In the smaller centres, the share of total retail space occupied by specialty shops is much higher — up to 90 per cent in themed centres. The Commission found this pattern to be largely consistent across States and Territories, within each particular category of shopping centre.

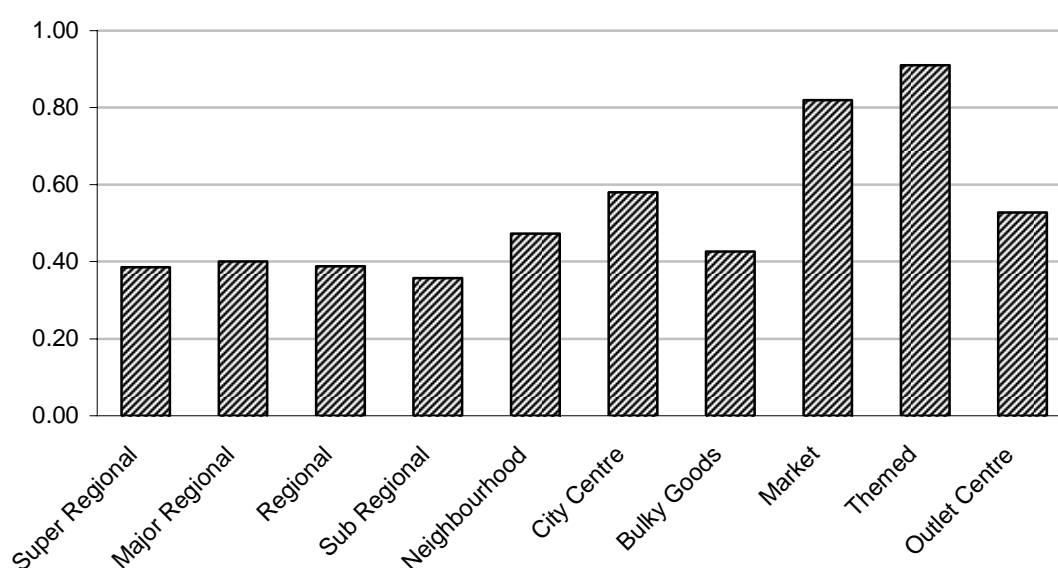
Table 2.3 Specialty retailers in shopping centres by State, 2006

	<i>Centres</i>	<i>Specialty retailers</i>	<i>Total retail gross lettable area</i>	<i>Proportion of State retail gross lettable area occupied by specialty retailers</i>
	No	No.	'000 sq metres	%
New South Wales	394	18 591	5 223	42
Victoria	196	11 786	3 090	41
Queensland	298	13 173	3 698	44
South Australia	137	4 389	1 301	41
Western Australia	279	7 289	1 958	44
Tasmania	23	481	162	32
Northern Territory	20	483	170	32
Australian Capital Territory	17	1 122	313	42
Total	1 364	57 314	15 915	42

Source: PCA (2006).

Figure 2.6 Floor space in shopping centres held by specialty retailers in Australia, 2006

Proportion of total gross lettable area for retail in shopping centres



Data source: PCA (2006).

While many specialty retailers rely on foot traffic (passing trade) for commercial success, some specialty tenants are a destination for customers — either because of a differentiated product, their own marketing efforts, their reputation or that of their franchisor. Examples include bank and post office outlets, pharmacies, some hairdressers, sports stores, high-fashion and specialty book stores. Other factors being equal, the more differentiated the product that a retailer has for sale (compared with other potential retailers in the area), the more choice that the retailer is likely to have in where to locate and in the terms and conditions of their lease.

Ownership of businesses that use retail space

Ownership of major stores is typically confined to companies and organisations that have resources sufficient to maintain and manage a large retail outlet. In contrast, many specialty retail businesses in Australia are owned by ‘independent’ retailers either as a small company, partnership or sole trader. For example, within shopping centres alone, available estimates suggest some 47 per cent of all specialty stores are owned and operated by independent retailers (Euromonitor International 2006).

Despite separate ownership, many specialty retailers are part of a national chain or larger franchise arrangement. For example, Colonial First State Property Management states that in its portfolio of centres, approximately 80 per cent of leases involve tenants that are part of a national chain (submission no. 78, p. 6). Similarly, Stockland reports that almost 60 per cent of its retail tenants are multi-store ‘chain’ retail tenants (submission no. 88, p. 4). In fact, the majority of franchising in Australia takes place in the retail non-food industry (Griffith University 2006). For the specialty retail tenant, the existence of a franchise arrangement often influences the landlord-tenant relationship, depending on the nature of the franchise, and the franchisor’s relationship and negotiating position with the landlord.

A small proportion of businesses that use retail space are outlets for a local, State or Commonwealth government agency and may be owned by an individual lessee or the larger agency. For example, many licensed post offices are separate small businesses that operate under a franchise arrangement and it is the responsibility of the licensee to negotiate for retail space (submission no. 10).

2.3 Market entry, exit and vacancies

The operation of the retail tenancy market in Australia is influenced by the availability of vacant retail space and the ease with which businesses enter and exit the market.

Market entry and exit

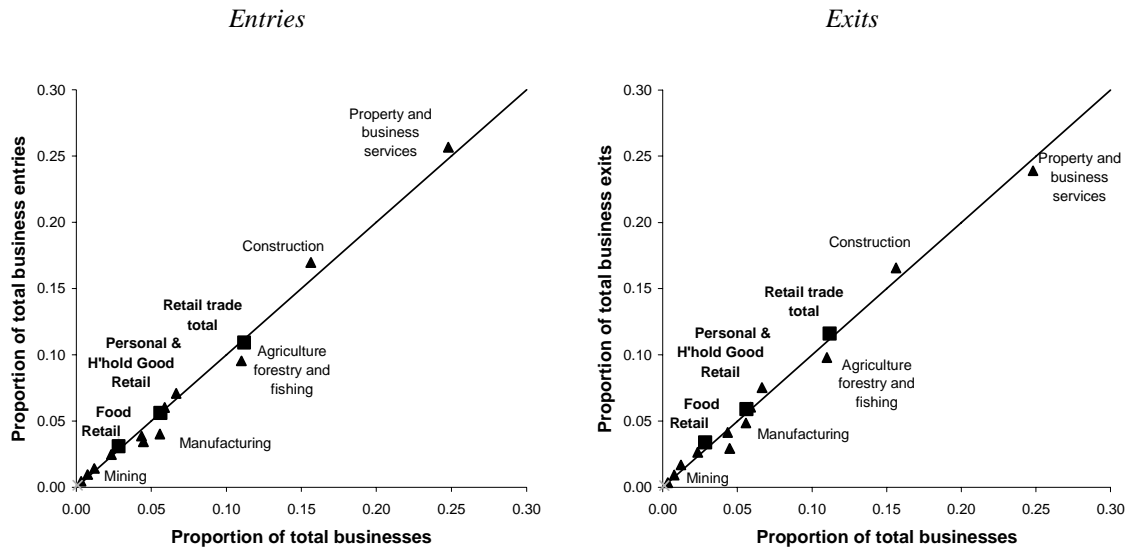
The entry and exit of firms in an industry is a natural outcome of a functioning market and has significant positive effects on efficiency of the market (Bickerdyke, Lattimore and Madge 2000). New businesses can offer innovative products and services, while exiting businesses can free up labour and resources for more productive uses. Nevertheless, this churning of businesses may involve costs, particularly when there are significant fixed cost items, such as store fitouts.

Rates of entry and exit would be expected to vary significantly between activities, with differences in barriers to firm movement and set-up costs. For example, in an activity with relatively low set-up costs — as might be the case for some of the personal and household goods retailers (such as clothing shops) — the number of firms undertaking the activity and the entry and exit rates could be expected to be relatively high compared with those in other activities that have more substantial set-up costs (such as food retailing). That is, entry and exit rates would be expected to be proportional to the stock of businesses, unless there was a systematic problem with the market in which a particular activity operates, or the activity was going through a transition.

Data on the number of businesses and exit and entry rates show that for retail businesses, entry and exit rates are in line with the relative share of retail businesses in the Australian economy (figure 2.7). This is the case for all industry categories examined. This suggests that there is no systematic industry-wide feature of retailing that consistently leads to higher than average business failure.

Entry and exit of businesses in the retail and services sectors have been broadly comparable in recent years (table 2.4). Around 16 per cent of all retail and services businesses leave the industry each year. There is, however, some variation between different retailing activities. For example, there is slightly more movement (or churning) of businesses into and out of food retailing than other forms of retailing, implying slightly lower survival rates than average. The incidence of entries and exits is likely to vary with broad economic conditions, although such variation is not particularly evident in the available data.

Figure 2.7 Business entry and exit rates, 2005-06
Proportion of total operating businesses by industry category



^a A business entry is recorded for a business which has newly registered for an ABN and which has a GST role allocated. A business exit is recorded for a business for which the ABN has been cancelled and/or which has ceased to remit GST for 5 consecutive quarters or for which the GST role has been cancelled.

Data source: ABS (*Counts of Australian businesses, including entries and exits, June 2003 to June 2006, Cat. no. 8165.0, Canberra*).

Table 2.4 Entry and exit of all retail businesses, 2003-04 to 2005-06
Per cent of businesses operating at start of each year

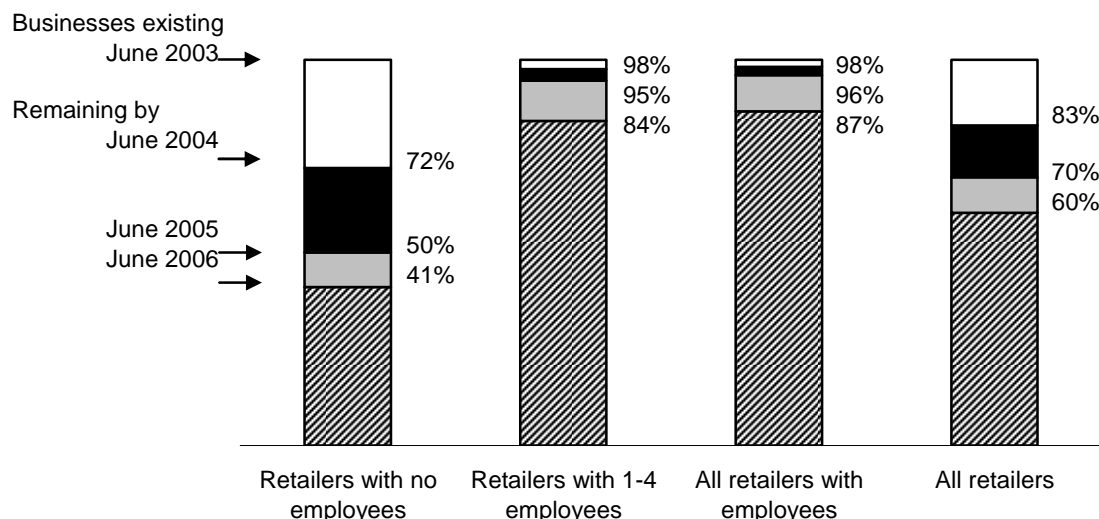
	2003-04		2004-05		2005-06	
	Entry rate	Exit rate	Entry rate	Exit rate	Entry rate	Exit rate
Food retailing	22	19	20	20	18	18
Personal & household goods retailing	18	16	18	17	16	16
All retailing^a	18	16	18	17	16	16
All service industries	17	15	17	15	16	15

^a Includes businesses in food retailing, personal and household goods retailing, and motor vehicle retailing and services.

Sources: ABS (*Counts of Australian businesses, including entries and exits, June 2003 to June 2006, Cat. no. 8165.0, Canberra*); Reserve Bank of Australia (2007).

Across retail trade businesses of differing sizes (as measured by the number of employees), survival varies substantially (figure 2.8). For example, over the period 2003-04 to 2005-06, exit rates were substantially higher for those retailers that had no employees (ABS 2007a). Retailers in this category include small specialty shops operated by the owner.

Figure 2.8 Survival of retail trade businesses by size, 2003-04 to 2005-06^{ab}
 Proportion of businesses in 2003-04 remaining in 2005-06



^a A business 'survivor' is a business which was actively trading at the start of 2003-04 and continued to be trading at the end of 2005-06. ^b Includes businesses in food retailing and personal and household goods retailing, but excludes those in motor vehicle retailing and services.

Data sources: ABS 2007a (*Counts of Australian businesses, including entries and exits, June 2003 to June 2006*, Cat. no. 8165.0, Canberra); Reserve Bank of Australia (2007).

Within shopping centres, the SCCA submitted that just over 85 per cent of retailers that were in a sample of centres in 2003 were still located in those centres in 2004 (submission no. 83, p. 57). This suggests an exit rate for those retailers of around 15 per cent — in line with the annual average rate of exit across all retail trade and service establishments (table 2.4). Furthermore, it is likely that only some of these exits represent business *failure*. In a study of small business failure in Australian shopping centres, Watson and Everett (1996) found that annual failure rates varied from less than 1 per cent when 'bankruptcy' was the definition of failure used, up to 9 per cent when failure was defined broadly as a 'discontinuance of ownership' (which may reflect a departure from business due to retirement or ill-health). Failure rates of around 4 per cent were attributed to a failure to 'make a go of it' or 'discontinuance of business'. At a broad level then, it is not apparent that the survival of Australian retailers, and hence churning of retail tenancies, is significantly different in shopping centres compared with elsewhere.²

The stability of tenants is generally higher in the larger regional shopping centres (around 90 per cent per year) than in smaller centres (around 82 per cent per year)

² In comparison, Cox and Vos (2005) reported that in New Zealand, small business failure rates are lower in managed shopping centres than in unmanaged centres. However, this difference was found to only be significant for a very broad failure category — a failure to 'make a go of it'.

(submission no. 83, p. 57). Reported renewal rates of leases also indicate that there is some variability in the stability of tenancies between different centres. For example, Westfield reported that 75 per cent of its five year leases for specialty shops that fell due in 2006 were renewed (submission no. 85, p. 5), while Centro reported that 81 per cent of specialty leases that fell due in 2006 were renewed (Centro 2006). Colonial First State Property management reported that 70 per cent of leases that expired in 2006 were renewed (submission no. 78, p. 4). These estimates are a broad indicator of the movement of small businesses in shopping centres but may under-estimate the extent of change in business ownership. For example, where leases are held by franchisors rather than the franchisees, a change in the franchisee may not be reflected by a lower lease renewal rate.

FINDING

Entry and exit of retail businesses is not exceptional compared to other service activities. The survival of retail businesses in shopping centres is in line with survival rates of retail businesses elsewhere.

Vacancies in retail space

The ease with which a potential tenant is able to find suitable premises from which to conduct business and lease terms depends on available vacancies, and the location and condition of the vacant space.

Vacancy rates for retail space vary substantially between locations (table 2.5). In general, vacancy rates in retail strips and neighbourhood centres appear to be higher than vacancy rates in the major city CBDs and larger shopping centres — making it potentially harder for a retailer to find space in such a location. In addition, the availability of space can vary significantly between regions, indicating the difficulty in generalising about the market from characteristics of an individual area or region. For example, in 2006, the vacancy rate for prime space in retail strips in the Sydney metropolitan area was over twice that for Melbourne.

Table 2.5 Vacancy rates by location, 2006 and 2007^a
Shopping centres and selected non-shopping centre locations

	<i>Per cent</i>
<i>Shopping centres</i>	
All shopping centres	1.2
Regional centres	0.9
Sub-regional centres	1.0
Neighbourhood centres	3.1
<i>Selected non-centre locations</i>	
Sydney CBD	1.6
Sydney metropolitan prime retail strips	5.9
Melbourne CBD	0.7
Melbourne metropolitan prime retail strips	1.8
Adelaide prime retail strips	2.1
Brisbane CBD (specialty stores)	2.3

^a Vacancy rates for shopping centres are averages for 2006. Rates for non-centre locations are the average rates prevailing in the December quarter of 2006 in Sydney and Melbourne, the June quarter of 2007 in Brisbane, and the September quarter of 2007 in Adelaide.

Sources: Submission no. 83, p. 52; CB Richard Ellis (2007a, 2007b, 2007c and 2007d).

While retail space available for rent is an important influence on the functioning of the market, other factors are also significant, including:

- condition of premises and ease of access to potential customers;
- landlord's requirements for tenancy mix or type of service, particularly in shopping centres;
- the demographic characteristics of people living in the areas surrounding vacant retail space and expected changes;
- the relative importance of business reputation and passing trade (foot traffic) to the business model of the retailer; and
- industry-specific factors that may restrict the use of retail space such as geographical-based location arrangements for newsagents (submission no. 51), location requirements for Licensed Post Offices (submission no. 10), and the regulation of pharmacies (submission no. 109).

2.4 Summing up

The retail tenancy market in Australia comprises a range of businesses that vary substantially in terms of the type of goods or services provided, ownership structure and the size, experience and resources that they bring to their operation. While most retailing occurs outside of shopping centres in retail strips and increasingly in stand-

alone bulky goods sites and direct factory outlets, shopping centres as a group are an important and growing share of the retail tenancy market. The vast majority of submissions received in this inquiry related to shopping centre tenancies.

The survival of retailing businesses (and correspondingly, the churning of retail tenancies) varies substantially with business size and type, although there is no significant difference in business survival for those located in shopping centres compared with elsewhere. Vacancies for retail space, however, do appear to vary according to location with more retail space available in shopping strips and the smaller neighbourhood centres than in major city CBDs or larger shopping centres. This makes it more costly for a retailer to find and retain space in such sought-after locations.

