REIMAGINING RETAIL SPACE. FOOD FOR THOUGHT FOR PHYSICAL RETAILERS

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How much space do shoppers really need?

Covid-19 has put many of the trends currently affecting the business world into fast forward. Not only has it rapidly made new ways of working mainstream, such as remote working, it has given massive extra impetus to the spread of e-commerce. This has had a major knock-on effect on the amount of space now required for office, residential and retail purposes.

These recent developments tie in with a number of larger-scale trends. The rise of mega-cities and increasing density of living mean that less and less space is available overall, and human impact on the environment is growing inexorably. A recent trend has emerged towards smaller living spaces and the phenomenon of "tiny houses". Shared office spaces are increasingly popular. Disruptive hotel concepts are appearing, with less individual space but increased shared space for urban travelers. Changes are also underway on our roads, with mobility concepts based on sharing rather than owning, reducing the number of vehicles and hence the amount of space needed for them.

What does this changing world mean for physical retail – traditional bricks-and-mortar stores? In the past, retailers followed a simple formula: Increase your retail space and your top line goes up. But today, with the amount of retail space needed rapidly shrinking, physical retailers must develop alternative strategies for using floor space that has become surplus to requirements.

In this paper we take a high-level look at how these macro-level developments challenge traditional retail models on the ground. We investigate the options available to physical retailers. How can empty retail space be reimagined? And what shift of mindset is required in order for physical retail to remain relevant in the coming decades?

The future of physical shopping

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The Covid-19 lockdown has provided a major boost to online shopping. In Germany, for example, interest in purchasing products across categories online has risen significantly. Experts expect that these new digital behaviors will in part persist after the crisis subsides. Thus, while online grocery shopping is likely to fall back from its pandemic highs, categories such as electronics and books will rise to new levels. According to the Sweden-based Institute of Retail Economics, German consumers plan to permanently reduce their trips to stationary retail outlets by 24.7 percent, for example, continuing a trend towards declining footfall figures in inner cities that has been noted since as early as 2015, well before the current pandemic.

Slowing demand for stationary shopping goes hand-in-hand with weaker demand for retail space, especially large bricks-and-mortar stores. In response, many retail chains are considering giving up their current outlets. Cologne-based market research institute IFH, in cooperation with German business newspaper *Handelsblatt,* forecasts that the number of retail stores in Germany will fall from 363,000 in 2017 to 274,000 in 2023. Weaker demand for space, combined with growing availability, will result in excess capacity – in other words, retail floor space that needs to be filled.

Empty retail spaces are likely to emerge not only in Germany, but across Europe. Real-estate service and investment company CBRE expects total retail space requirements in the United Kingdom to fall by up to 16 percent between 2021 and 2025, for example. Clothing and footwear are forecast to see the largest decline in space requirements, at 35 percent, followed by electricals, at 19 percent. Rhodri Davies, head of United Kingdom Retail at CBRE, describes the situation as follows: "Retailers are becoming increasingly efficient in their use of space, meaning they can use less space to achieve the same level of retail sales. We have seen significant changes in our sector over the past 12 months and we will see more as retailers continue to adapt and evolve."

Reimagining empty retail space

Falling demand for physical retail space presents landlords, tenants and urban planners with a pressing question: How to fill empty retail space in cities? The overarching goal remains to improve footfall and average basket size. The obvious solution, therefore, is to retain the current retail space and enrich it with new retail concepts, such as "retailtainment", tutorial corners, micro-spaces, pop-up stores and the like. However, this approach will not work in every case. Decision-makers have two further options at their disposal: To combine the retail space with a non-retail element, such as a gym or gastronomic offering; or to replace the retail space completely, for example, with housing. We examine each of these options in turn below.

Option 1: Retain and enrich existing retail space

Despite the rise of digital shopping, physical stores remain a key pillar in the customer journey. Younger consumers – Gen Z and Millennials, in particular – greatly value physical retail and use it as a forum for both socializing and product discovery. However, as consumers become more demanding in their shopping habits, businesses need to reinvent their in-store concepts and floor division. Below, we outline a number of concepts for improving the retail space strategy and use of floor space.

Retailtainment, also known as "experiential marketing", is one way to rise to the challenge. It is no longer enough for retailers to provide efficient service and a wide variety of products, they must now also create an experience that customers cannot buy. Creating one-of-a-kind experiences supports brand-building goals, strengthens company-consumer relations and solidifies customers' loyalty to the brand. Gentle Monster is a good example of how this works in practice. The sunglasses brand is known for its unusual store installations, creating a unique theme expressed through unique "sculptured landscapes".

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An increasing number of companies are offering **tutorial corners** in a dedicated area of their stores, as a venue for live tutorials, workshops and advanced product advice. This approach is in line with the concept of showcasing the brand and bringing the brand values to consumers. It not only adds an additional service layer to the company's offering, but also facilitates the customer relationship with a person-to-person approach. Perfumery chain Douglas, for example, incorporates a beauty spa into each of its new flagship stores, offering everything from facials and makeup tutorials to a hairdressing salon. Similarly, Apple's Genius Bar offers branded technical support, not only giving the brand a personality but also providing customers with access to Apple devotees who are deeply knowledgeable about the company's products and fully support its philosophy.

Micro-spaces are a way for retailers to make their physical retail space sustainable long term. The idea is that not every town or city needs a large-scale, experience-heavy format. By combining smaller spaces that focus on services with rich flagship experiences, retailers can create an offering that serves customers' needs on a day-to-day basis. One of the best examples is Swedish furniture and homeware giant IKEA, which has downsized its large-scale, out-of-town stores to reach city-dwelling audiences. Starting with London, the firm's "Planning Studio" model lets customers design their perfect IKEA spaces and purchase products that are then delivered directly to their homes. The company plans to expand this model to New York this year, adapting each studio in line with local demand. Other retailers opening smaller-format stores include John Lewis, Nike, Arc'teryx and many others.

Pop-up stores and **shop-in-shops** (in-store concessions) create a healthy churn of independent retailers relevant to the local communities that they serve. Brands operating pop-up stores also benefit from seeing how customers respond to them, which can then guide their thinking on new products and services. Pop-ups boost the idea of exclusivity – a feeling increasingly popular for many customers. Louis Vuitton, for example, created a pop-up store in New York featuring its Fall 2019 men's collection. The store had a striking color scheme: It was painted inside and out in a bright neon green. This color scheme was continued along the street, with objects such as a fire hydrant and bicycle painted the same color to catch potential customers' attention.

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Portfolio holders and investors are increasingly looking at repurposing or repositioning properties with large surface areas in city-center locations. Properties with large surface areas and good delivery facilities, such as department stores, offer the potential for urban logistics or **warehousing** on floors that are no longer required for retail – a blending of retail and last-mile logistics. Leveraging the trend for quick commerce, retailers with large stores can potentially partition an inefficiently used area of their store and transform it into a commissioning space for deliveries with a short lead time. This not only builds a new and innovative sales channel, it also uses the space more productively.

Expansion into **adjacent retail categories** can inject new life into spaces and attract new groups of customers. For instance, CBRE reports that grocery-anchored retail, which was already experiencing strong investor demand before the pandemic, has enhanced its appeal during the crisis, and retail investors who previously had no exposure to this sub-segment are now expanding into it.

E-commerce players are also investing in bricks-and-mortar stores, pop-ups, events and other physical retail strategies. Amazon, MADE, Glossier, Casper, Zalando, Shopify and many others have made the move into the stationary retail space area, filling unused spaces in department stores and along main streets. These brands have a strong appeal, particularly with younger generations that can potentially be attracted back into the city. Similarly, in 2019, Facebook opened a pop-up café in London offering free beverages to anyone who agreed to a privacy checkup – a smart response to criticism of the company's record on privacy issues.

Option 2: Combine retail space with a non-retail element

The second option for retailers and urban planners is to give over some of the retail space to other methods of driving footfall, such as gyms, co-working spaces, gastronomic facilities, health centers and educational institutes. As more and more people move to densely populated urban areas, so demand increases for local, walkable downtown centers where consumers live and work. These spaces can offer integrated shopping and entertainment experiences, lifestyle accommodation and access to all the necessities. Mixed-used department stores can cater to specific interests. For example, the Life Time Center in Boston has become a successful health and fitness-focused center. Similarly, the new shopping mall from Viva City in Dubai will be dedicated exclusively to sports, both in terms of its retail offering and its entertainment facilities. The Sport Society will occupy three entire floors, featuring different sports events and activities within this space.

Option 3: Replace retail space completely

In some cases, retail spaces will need to be completely replaced by other types of business. This is especially true for town and city main streets in Germany, which have seen a stark decline in footfall over recent years. This is the result not just of digital shopping but also the lack of the distinctive retail features on which local communities once prided themselves. Urban planners can counter this development by repurposing old retail spaces, turning them into alternative types of offering that are more relevant for local communities.

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One potential new use for former retail space is **services.** This simple solution involves creating a concentration of service providers in streets that were formerly dominated by retail. An innovative approach here is to establish a mix of service providers, from healthcare providers to bars and restaurants. The conversion of retail to service facilities is already common practice in some parts of the world and can often be achieved even without local authorities becoming involved.

Alternatively, some types of former retail stores can be converted into apartments or residential housing, promoting **inner-city living.** This also boosts footfall and increases the use of the retail outlets that remain, as new residents demand various products and services on their doorstep.

Another option is to use former retail space for **urban manufacturing,** in line with growing consumer demand for locally produced goods. Small, city-based manufacturers often produce high-quality, design-oriented products, from lifestyle objects to clothing and furniture. They act as pioneers, reclaiming urban spaces as production locations and creating a win-win-win situation for themselves, their customers and the city as a whole. Neighborhoods can subsequently experience an overall economic upswing, making it even easier for the manufacturers to operate sustainably and increasing their attractiveness for skilled workers and customers. Manufacturers also benefit by being located close to other companies, allowing them to build new, interdisciplinary partnerships. New York offers many good examples of urban manufacturing: The city is focusing on local ties, using the "Made in NYC" label to promote small urban manufacturers – 6,000 of them in total, creating employment for around 81,000 people.

Boosting customer satisfaction and financial return

As we have seen, landlords, tenants and urban planners have a range of tools at their disposal to ensure that physical retail remains relevant in the coming decades and, where this is impossible, to repurpose unneeded retail space. When implemented correctly, these measures can yield a wide array of benefits, from reduced operating costs in the case of downsizing to diversified revenue streams in the case of mixed-use properties. Often, retailers' actions will be geared towards enhancing the brand and shopping experience for customers, and boosting the customer engagement rate. Elsewhere, their focus will be on making the retail space more relevant – for example, by creating themed department stores – or transferring positive brand equity by featuring digital brands in a larger store, say.

Underlying this process of refocusing should be a shift in mindset. Rather than looking at surface-area productivity as a key metric, businesses should expand their vision to include areas of their stores that do not generate revenue directly, but rather boost marketing and brand-building. The key lies in ceasing to think about the store and starting to focus on the space instead. Dalziel & Pow's Paul West believes that, in the future, this space will do a lot more than selling: "The space of the future will have a range of jobs to do – from instant fulfilment and convenience to full experience, education and community."

In conclusion, we suggest a number of critical questions that decision-makers should consider before launching any space improvement projects. These questions can also underpin their medium-term strategic decisions and help them formulate a vision for the future.

Q: How much space do we need?
Retailers should critically challenge each square meter in the store, assigning clear targets – whether sales targets or marketing targets – to different floor areas. We recommend using different surface area productivity rates and average store sizes depending on the purpose of the store (brand-building or sales?), the retailer's price level (entry level or luxury?) and the industry in question (for example, automotive or food?).

Q: How can we increase footfall?
It is essential for retailers to attract the right audience to their stores and increase footfall per square meter. Players can take various actions here, from improving sales-generating areas to creating new areas, such as product experience areas, design installations or spaces offering product-related services.

Q: How should we organize closures, rightsizing and refitting?
Best-practice transformation projects begin with a rightsizing exercise, analyzing the location of the store, the type of neighborhood, current and expected footfall, and defining the purpose of the store. In the case of refitting projects, a clear timeline with strict deadlines is needed in order to limit store revenue loss during the refitting period.

Q: How can we finance the transformation?
Ideally, transformations lead to rental cost reductions and a sales uplift, thereby quickly paying for themselves and buffering the financing costs. In some cases, however, the investment may not yield a direct financial return but instead make a positive contribution to the brand. This would be the case, for example, if the store is turned into a brand museum.

Q: What action must we take right now?
To optimize sales floors and leverage existing potential in terms of customer experience, retailers must act early and act fast. When reimagining retail space, the sooner retailers start the process the better. The time for action is now!

Further reading

STORES, REINVENTED
➔ rb.digital/Stores_reinvented

HOW HEALTH AND SUSTAINABILITY TRENDS ARE DRIVING CHANGES IN CUSTOMER BEHAVIOUR
➔ rb.digital/Health_and_sustainability_trends

CONSUMER BEHAVIOR PATTERNS WON'T GO BACK TO "NORMAL"
➔ rb.digital/Consumer_behavior_patterns

DATA MANAGEMENT IN RETAIL HOLDS ENORMOUS VALUE POTENTIAL
➔ rb.digital/Data_management_in_retail

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