Revenue Share Rent of different retail formats

May 2010

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INDIAN RETAIL & REAL ESTATE PERFORMANCE

How much do different Indian Retailers pay mall owners as Revenue Share Rent?

May 2010

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INTRODUCTION

In most established international markets, retail tenants do not pay a fixed rent to mall owners or landlords. The most common best practice followed globally is turnover rent, or as we call it in India – revenue share rent.

When organizations such as Propzone (then ICS Broll) and Asipac tried to introduce this concept back in 2004, most retailers resisted. In fact, some leading retailers even threatened that they would stop dealing with Propzone and Asipac. However, by the year 2006, because rental asks from developers and landlords started shooting through the roof, some of the larger or more established players started to come around to the fact that this globally accepted best practice was the true way to establish a healthy win-all partnership between the owner and occupant.

The drive towards revenue share got a major push during the 15 month recession period in 2008-09, as retailers thought this was the best way for them to reduce risk. Finally, this globally prevalent best practice became an accepted norm in India as well. As they say, all's well that end's well.

So what is this revenue share or turnover rent model? Although there are multiple types of arrangements in the revenue share model, the most common one is where the retailer pays the owner or landlord a percentage of its sales turnover or revenue (less VAT or Entertainment Tax or Service Tax or other similar tax), or a Minimum Guaranteed rent (referred to as MG, but also called Base Rent in some markets), whichever is higher.

Other models include a Provisional Rent ("PR") instead of a minimum guaranteed rent, where the starting Provisional Rent is usually higher than what the MG would have been, and is reset every year, based on the previous year's actual achieved revenue share rent. This model, while reducing the retailer's risk during slowdowns or recession, greatly improve the owner's cash flow and also protect the owner from unnecessary rent reductions during a downturn. One could also build-in a minimum guarantee clause within the PR model, where the MG could be at least 75% of the previous year's PR.

Many other permutations and combinations of the revenue share model can be negotiated.

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The exact percentage to be paid by a retailer depends on the nature of the retailer's business, their anticipated trading density and gross margins in that category. Prevalent percentages in India range from as low as 1.5% to as high as 30%. Sometimes, the negotiated percentage figure depends on the location of a mall, its size, the developer's past record, the importance of the particular retailer for a particular mall and finally, both parties' negotiation skills.

There are also complex arrangements of revenue share, such as variable percentages depending on time (i.e., different for the first year, the second year and from the third year onwards) or based on volume (i.e., the revenue share percentage either increases or decreases when the retailer's turnover crosses a threshold). Established mall owners with a good track record may also insert clauses which protect them from comparative under performance by the retailer.

Under the fixed rent model, the owner is not much concerned about how the individual retailer is performing within the mall. This puts the parties on opposite sides. On the other hand, in the revenue share model, the rental revenue of the owner is directly dependant on the sales revenue of the retailer. Thus, it is in the interest of the owner to increase footfalls and conversions with better mall management and marketing. Therefore, the relationship between the parties changes to a true partnership. Clearly, no one can dispute that the revenue share model is a win-win model.

But how are mall owners to decide the percentage of revenue share? This study hopes to demystify that question. The data presented in this study, along with the conclusions, will help retail property owners and developers to do research-led decision making in the selection and placement of retail stores in shopping centres (malls) and in freezing that magic figure of % revenue share, in order to achieve a sustainable relationship.

This study is the fourth in a series of research-led studies that Asipac has planned on Indian retail in general and retail real estate in particular. Two of our past studies were published in multiple publications, including daily newspapers, business dailies, business magazines and industry magazines. We hope that the findings of this study will help faster deal closures and bring greater transparency into the system.

The data is presented in a fairly simple format. Numbers pertaining to trading density are given in Rupees psfpm (per square foot per month).

METHODOLOGY

The data for this study was collected by Asipac consultants through direct contact with senior management executives of more than 80 retail formats currently active in India spread over the last 18 months.

While the trading density data pertains to both, shopping centres (malls), as well as high streets or main streets in the Top 20 cities of India, the revenue share percentages are applicable only for shopping centres.

Asipac senior management verified the data by cross-checking almost 40% of the figures and we are reasonably satisfied with the accuracy and reliability of the figures presented.

It has to be kept in mind that the ATDs and Effective Revenue Share Rent (ERR) is a national average, and can greatly vary from city to city, location to location (within a city) and the location of the store (including floor) within a mall.

Before final publication, the report was sent for review to some of India's top retailers. By and large, these highly respected industry professionals agree with the accuracy of the data. Some of their comments/remarks form a part of this final report.

In any extensive study of this nature, there are bound to be errors & omissions. If anyone reading this report comes across any such errors or omissions, we will be happy to receive your comments on research@asipac.com and will incorporate necessary corrections after verifying its/their accuracy.

NOTE:

1) The first Table (divided into Pg.7 & 8) is the data sorted by the Average Trading Density and the second Table (divided into Pg.9 & 10) is the same data, but sorted by the Average Revenue Share Rent, in order to give a better comparison.
2) In Cinema, the Revenue Share Percentage could vary substantially in situations of Entertainment Tax exemption.
3) Since the sitting area in Food Court is paid by Mall owner, the Effective Revenue Share Rent (ERR) of FCC Operators may be divided by five, to enable accurate comparison with other retail formats.

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IMPLICATIONS / OUTCOME

This study was undertaken in order to achieve the following objectives:

1) To understand the concept of the revenue share model.

2) To understand retailer's rental affordability in absolute terms.

3) To help retail property owners, especially shopping centre developers or owners, now make informed and research-based decisions, especially on selecting the right retailers (or retail formats) and on deciding the revenue share percentage to be charged.

ACKNOWLEDGMENTS
We wish to acknowledge the contributions of all the retailers, mall owners, mall managers and leasing professionals with other firms who have cooperated in sharing data with us.

ABBREVIATIONS

PPP – per capita GDP

EBO – Exclusive Brand Outlet

MBO – Multi Brand Outlet

psfpm – Indian Rupees Per Square Foot Per Month

ATD – Average Trading Density

RS% - Revenue Share Percentage

ERR – Effective Revenue Share Rent in Indian Rupees Per Square Foot of Carpet Area Per Month

FCC – Food Court Counter

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Revenue Share Ratios of Different Retail Formats in Indian Malls

Notes: All Revenue Share %s exclude CAM, the ATD is on carpet area; all numbers are indicative and vary from location to location, property to property, store sizes, location within mall, etc.

Retail Format	Example of Retailer/Brand	Average Trading Density (psfpm)	Revenue Share Range (%)	Avg Revenue Share %	Average Rent on carpet area (psfpm)
Food Court Counter Operators	Several Local & National Players	Rs. 3,500	20.00 to 30.00%	25.00%	Rs. 875.00
FECs	Amoeba, Time Zone, Orama, Fun City, Blu-O	Rs. 250	13.50 to 27.50%	20.00%	Rs. 50.00
Beauty Salons, Hairdresser	L'oreal, Lakme, YLG, Several Local Brands	Rs. 600	15.00 to 23.00%	18.50%	Rs. 111.00
Ice Cream, Juices	Walls, NZ Naturals, Booster Juice, Baskin Robbins	Rs. 750	15.00 to 22.00%	18.00%	Rs. 135.00
Cafes	Café Coffee Day, Barista, Coffee World, Costa Coffee	Rs. 600	12.50 to 23.00%	17.50%	Rs. 105.00
Western Fashion - International	Tommy, Benetton, Alcott, Celio, Lerros, OVS	Rs. 850	12.00 to 18.0%	15.00%	Rs. 127.50
Leather Bags & Accessories	Hidesign, Calonge, Esbeda, Holii, Blue & Blues	Rs. 1,700	12.00 to 17.00%	14.50%	Rs. 246.50
Western Fashion - National	Madura, Indus League, Zodiac, Provogue, Arvind	Rs. 900	11.00 to 16.00%	14.00%	Rs. 126.00
Denim Apparel	Levis, Lee, Wrangler, Pepe	Rs. 1,500	11.00 to 16.00%	13.50%	Rs. 202.50
Multiplex	PVR, Inox, Cinepolis, Big, Fun	Rs. 300	11.00 to 16.00%	13.50%	Rs. 40.50
Fashion Accessories - Men	Neckties & More, Addons, Tie Rack London	Rs. 1,650	12.00 to 15.00%	13.00%	Rs. 214.50
Restaurants (Formal or Fine Dining)	BJN Group, Mainland China, Great Kabab Factory	Rs. 750	11.00 to 17.50%	13.00%	Rs. 97.50
Eyewear	Vision Express, Foresight, Sunglass Hut, Himalaya	Rs. 1,250	10.00 to 14.00%	12.50%	Rs. 156.25
Restaurants (Casual Dining)	Rajdhani, Several Local Brands	Rs. 1,025	10.00 to 14.00%	12.00%	Rs. 123.00
Sports Lifestyle EBOs	Adidas, Nike, Reebok, Puma	Rs. 1,350	10.50 to 13.50%	12.00%	Rs. 162.00
Footwear	Metro, Mochi, Bata, Regal, Rocia, Aldo	Rs. 1,650	9.00 to 15.00%	11.50%	Rs. 189.75
Ethnic Fashion - New Gen	Biba, Jashn, W, Global Desi, Satya Paul, Soch	Rs. 1,600	10.00 to 13.50%	11.00%	Rs. 176.00
Gift Shops	Archies, Hallmark, Gift Express, Nik Nish	Rs. 1,400	9.50 to 12.50%	11.00%	Rs. 154.00
Sports MBOs	RSH, Planet Sports	Rs. 850	9.50 to 12.50%	11.00%	Rs. 93.50
Pens & Personal Accessories	William Penn, Editions	Rs. 2,250	9.00 to 12.00%	10.00%	Rs. 225.00
Ethnic Fashion - South Traditional (Vanilla)	Kalanjali, Vijaylakshmi, Neerus, Nalli, Pothy	Rs. 2,200	8.00 to 11.50%	9.50%	Rs. 209.00

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Retail Format	Example of Retailer/Brand	Average Trading Density (psfpm)	Revenue Share Range (%)	Avg Revenue Share %	Average Rent on carpet area (psfpm)
Bookstores	Crossword, Oxford	Rs. 850	7.00 to 11.00%	9.00%	Rs. 76.50
Health & Beauty	Health & Glow, New U	Rs. 2,400	7.00 to 10.00%	8.50%	Rs. 204.00
Leisure Megastores	Reliance Timeout, Landmark, Odyssey	Rs. 625	6.50 to 9.50%	8.00%	Rs. 50.00
Watches MBOs	World of Titan, Helios, Ethos, Time Factory, Zimson	Rs. 2,100	7.00 to 9.00%	8.00%	Rs. 168.00
Small Dept Stores - 10,000 to 25,000 sft	Westside, Reliance Trends, Pantaloon, Marks & Spencer	Rs. 700	7.50 to 9.50%	8.00%	Rs. 56.00
Office Supply & Equipment	Staples, Office Depot	Rs. 900	6.00 to 8.50%	7.25%	Rs. 65.25
Quick Service Restaurants*	McDonald's Pizza Hut, KFC, Taco Bell, Nirulas	Rs. 1,500	5.50 to 8.50%	7.00%	Rs. 105.00
Large Department Stores >30,000 sft	Lifestyle, Shopper's Stop, Central	Rs. 800	6.50 to 8.00%	7.00%	Rs. 56.00
Watches EBOs	Omega, Rado, Tissot, Swatch	Rs. 2,500	6.00 to 8.00%	7.00%	Rs. 175.00
Furniture Megastores	Home Centre, @Home, Reliance Living, Home Town	Rs. 550	5.50 to 8.00%	7.00%	Rs. 38.50
Ethnic Fashion - South Traditional (ANCHOR)	RMKV, Kalanjali, Nalli, Pothy	Rs. 1,750	4.50 to 7.50%	5.50%	Rs. 96.25
Pharmacy	Guardian, Trust, Manipal C&C, Apollo, Reliagare	Rs. 1,800	3.75 to 5.00%	4.25%	Rs. 76.50
Grocery Stores	Food Bazaar, More, Reliance Fresh, Spencers Daily	Rs. 1,500	4.00 to 4.75%	4.25%	Rs. 63.75
Supermarkets - 10,000 to 35,000 sft	Spar Supermarket, More Megastore, Total, Spencers Super	Rs. 1,200	3.00 to 4.50%	3.75%	Rs. 45.00
Jewellery - Fashion	Nirvana, Several Local Brands	Rs. 4,000	3.25 to 4.25%	3.50%	Rs. 140.00
Hypermarkets >35,000 sft	Spar Hypermarket, Hypercity, Star Bazaar, Big Bazaar, Walmart	Rs. 1,150	2.50 to 4.00%	3.50%	Rs. 40.25
Electronics Specialty	Apple, Sony, Bose, LG, Samsung	Rs. 4,500	2.50 to 3.75%	3.00%	Rs. 135.00
Electronics Megastores	Croma, Reliance Digital, X-Cite, E-Zone, Local Retailers	Rs. 2,250	2.75 to 3.50%	3.00%	Rs. 67.50
Mobile Boutique	The Mobile Store, Univercell, One Mobile, Axiom Telecom	Rs. 6,500	2.00 to 2.40%	2.10%	Rs. 136.50
Jewellery - Gold & Diamond	Tanishq, Reliance Jewels, Gili, Local Brands	Rs. 8,500	1.50 to 2.00%	1.75%	Rs. 148.75

* 1.00 to 2.00% higher in Food Courts

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* 1.00 to 2.00% higher in Food Courts

SUMMARY & CONCLUSIONS

Our findings can be summarized and analyzed as follows:

1) As we had already concluded in the findings of our Trading Density Study, the organized retail industry in India is now quite evolved, with more than 450 established retailers (including foreign retailers) across 33 formats or categories.

2) There is no single rule to correlate the Average Trading Densities (ATD), Revenue Share percentages (RS%) and Effective Revenue Share Rents (ERR) between different formats. The RS% does not depend only on the ATD, but on the category's margins as well. For example, while the category "Jewellery – Gold & Diamond" has the highest ATD, it still does not yield the highest ERR to the mall owners. In fact, it is #19 in terms of ERR. On the other hand, while the category "Leather Bags and Accessories" is #12 by ATD, it is #2 in the ERR yield.

3) Hypermarkets as a category are the second last (#40) in the ERR yield based on the revenue share model, but they should be a preferred tenant, because they are one of the highest Footfall Frequency Drivers (FFD) and thus play the largest anchor role. Beauty Salons / Hairdressers are #29 by ERR yield but are also a high FFD.

4) Although Pens & Personal Accessories yield amongst the highest rents, you can't really fill up a mall with too many of such retailers – at best, there can be 2-3 stores in each of these categories.

5) Ethnic fashion stores have a >50% higher rental yield compared to western fashion stores, at least in South India.

6) Even anchor stores from traditional retailers such as RMKV, Nallis, etc. are giving more than 70% higher rental yields. The modern retail anchors need to wake up to this fact.

7) Categories such as Pharmacies, FECs and Multiplexes, even though they yield very low ERRs, are a must have in any mall.

SUMMARY & CONCLUSIONS (continued)

8) Furniture megastores in Indian malls are not doing well. In terms of rental yield, they are last on the list. There is no reason for malls to give them space, as they neither pay decent rents nor drive footfalls. Owners/managers of these categories are probably spending too much time on the sample bedrooms in their stores – wake up!

9) Even Leisure Megastores (such as Landmark, Reliance Timeout and Odyssey) need to wake up and improve their ATDs or start paying higher rents.

10) Small Department Stores such as Westside, Pantaloons and M&S are currently paying the same rent (ERR) as Large Department Stores such as Lifestyle, Shoppers Stop and Central. This is not fair to the mall owners, as the big brothers take much bigger spaces and drive greater footfalls. Therefore, if the ATDs of the smaller players is not going to improve, they must start paying a higher RS%.

11) Although the recession forced mall owners to accept the revenue share model up to a certain extent, there is still a long way to go, as many retailers are still not comfortable sharing accurate revenue data or their books of accounts, and mall owners do not trust the information provided.

12) Revenue Share is the way forward – as it is a win-win scenario, allowing mall owners to get a share of the retailers' growth, while making them share greater risk in times of downturn or if a mall is not managed well.

13) Fixed Rent tenancies in malls will be dead in the next 2-3 years. RIP.

Testimonials

"The report appears to be comprehensive and informative."

Ajay Baijal, CEO, Reliance Digital

"Good work. Very useful in setting rental expectations and establishing feasibility of a retail project. In Cinema, the % could vary substantially in situations of Entertainment Tax exemption, inefficient designs, or saturated markets with e-tax. Nonetheless, those are corner cases. Your analysis works well in mainstream situations. Keep up the good work."

Deepak Marda, Joint MD, Cinepolis India - the first international multiplex chain in India

"Asipac's revenue share study is a very interesting study which clearly articulates the win-win benefit of revenue share schemes. The data appears accurate and insightful and I hope developers continue to adopt this approach when letting retail space."

Martin Jones, Managing Director, Marks & Spencer (India)

"*I've gone through the study and greatly appreciate your efforts. I am sure that the industry will be happy to receive the report extremely positively, besides finding the contents meaningful."*

Manoj Motta, COO, Shopping Centres Association of India

"Thank you for sending me the Asipac study on revenue share rentals. As with your previous studies, this study is also very well researched and will definitely help the retail industry and property development. We have been following the revenue share model for over 30 years. 65% of our shops including high streets are on a pure revenue sharing model. In the past when we used to take stores in malls, the mall owners used to talk only of fixed rentals but in the last couple of years more than 50% of our mall shops have been on revenue sharing basis".

Rafique Malik, Chairman, Metro Shoes & Mochi

"Asipac's revenue share study will help develop a framework for decision making for the mall owners as well as the tenants. What actually emerges is that it takes all kinds of tenants to make a mall and therefore it is important to get the tenant mix right for a mall to succeed! The challenge for the mall owner would be to realize that the revenues he will get from the various types of tenants is different but each one of them have a role to play to make the mall a success, pretty much like a product manager's or merchandiser's job, of balancing volume drivers & profit drivers in the product mix, while at the same time maximizing overall margins".

V.Govindraj, VP – Integrated Retail Services, Titan & Tanishq

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PRESS PAGE

The first-of-its-kind study of the revenue share rent paid by organized retail formats to mall owners, done by Bangalore-based retail real estate consultancy Asipac, will take the mystery away from landlord-tenant transactions in Indian malls, thus bringing about much needed transparency in the industry.

Asipac's study on the average trading density of modern retail formats, widely published earlier this year, had already set the path towards greater transparency in Indian retail real estate. That study was welcomed by a large cross-section of mall owners/developers as well as retailers, negating the myth that Indians do not want transparency.

"The revenue share study will help mall owners and developers understand the revenue share numbers and what they actually mean in terms of effective rental yield," said Asipac Chairman Amit Bagaria.

There is no single rule to correlate the Average Trading Densities (ATD), Revenue Share percentages (RS%) and Effective Revenue Share Rents (ERR) between different formats. The RS% does not depend only on the ATD, but on the category's margins as well. For example, while the category "Jewellery – Gold & Diamond" has the highest ATD, it still does not yield the highest ERR to the mall owners. In fact, it is #19 in terms of ERR. On the other hand, while the category "Leather Bags and Accessories" is #12 by ATD, it is #2 in the ERR yield.

The study finds that ethnic fashion stores have a >50% higher rental yield compared to western fashion stores, at least in South India. "Even anchor stores from traditional retailers such as RMKV, Nallis, etc. are giving more than 70% higher rental yields. The modern retail anchors need to wake up to this fact," Bagaria added.

According to Asipac, it is a myth that revenue share is a phenomenon of recession. In most established global markets, the most common best practice is turnover rent (called revenue share rent in India). When Propzone and Asipac tried to introduce this back in 2004, most retailers resisted. However, by 2006, because rentals started shooting through the roof, some larger retailers started to accept that this global best practice was the true way to establish a healthy win-all partnership between the owner and occupant. The drive towards revenue share only got a major push during the 15 month recession period in 2008-09.

ABOUT ASIPAC

Established in 1996, Asipac Group comprises India's most admired mall development consultant and letting managers, a multiple award wining real estate marketing consultant, a highly respected retail research & consulting firm and India's newest mall management company.

Our services include:

- Project Conception
- Comprehensive Mall Planning
- Design Process Management
- Letting and Lease Management
- Retail Research and Consulting
- Mall Marketing Consultancy
- Mall Management
- Rental Yield Maximization
- Conception of New Retail Formats
- Marketing Strategy, Ideas and Programs for RE Projects

In 14 years, we have provided high level strategic advice to RE developers on projects with a combined built-up area of 380 million square feet valued at more than US$24 billion.

In retail real estate, we have advised developers on retail / shopping centre projects of over 14 million square feet, including nine of the 25 largest malls in India. We have leased more than 6.8 million square feet of retail real estate across India in just four years.

Asipac undertakes strategic research on the retail as well as the retail real estate sectors. Our study of trading densities of modern retail formats was featured twice in The Economic Times and was cover story of Images Retail's February 2010 issue. Our study on India's largest malls featured in The Economic Times, The Times of India (twice), The New Indian Express, Business Today magazine and Shopping Centre News magazine.

We conceived and planned India's first luxury gated community, the first hotel condo, first affordable housing project below Rs.1 million post-2004, first 12 minute lifestyle suburb, first luxury lifestyle resort for seniors, first Brand Factory, largest enclosed mall, largest strip mall, and the World's first fashion-themed SEZ.

Asipac was voted at GIREM as **Best Marketing Firm 2008** competing against 3 IPCs and has won **3 Remmy Awards** from Times of India. One of our projects broke a **Guinness World Record™** and was a finalist in Mixed Use Project category of **Cityscape Asia 2008 RE Awards**. A project launch won a **Bronze at 2009 EEMAX Awards**. An unpublished campaign won **GOLD at the Big Bang Awards** of Ad Club, Bangalore.

With **215+ media articles** and **40+ TV features**, including **16 front page/cover stories**, our credentials are well known in Indian real estate.

SHAPING THOUGHT. BUILDING VALUE.

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