The impact of the rate hike on the retail sector

Although the upper end of the consumer bracket is safe from the interest rate hike announced last week, middle-income consumers already under financial pressure will feel the pinch of the hike...

Last week, South African Reserve Bank Governor, Lesetja Kganyago, announced that the bank will increase the repo rate by 25 base points to 6.0% per annum with effect from 24 July, 2015. Prime rate is now 9.50% and this means those with loans will pay more on monthly instalments.

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Preston Gaddy, Divisional Director for Strategic Retail Leasing of Broll Property Group said that the rate hike is not helping the financial situation of many households whose disposable income is still under pressure.

"The increase in home loan repayments, vehicle financing and other HP agreements will mean that there will be less in the wallet for discretionary purchases."

However, Gaddy pointed out, the upper end of the consumer bracket will not necessarily feel the pinch, but middle-income consumers will as they have been feeling the effects of stagnant economic growth for the past two to three years now.

Furthermore, he said that the purchase of items that are deemed to be luxuries will be put on hold for now while retailers of large ticket items, such as appliances and electronics, are likely to feel the impact the most.

Those retailers serving the high-end consumer, the likes of Woolworths, will still post moderate growth as this end of the scale is least likely to be affected by the recent interest rate hikes, according to Gaddy.

Meanwhile, value fashion retailers such as Mr Price, Pep, Ackermans, Jam and PQ will also continue to be the destination of choice among the middle-income consumers.

Gaddy notes that fashion as well as homeware/furniture retailers that rely on credit purchases are in for a challenging 18 months ahead.

"It will be interesting to see whether hardware and home improvement retailers, who have had fairly decent growth over the past two to three quarters, will continue to post growth, given that consumers may look at home improvement and renovation as opposed to acquiring new homes," said Gaddy.

Sector growth projections

Gaddy said that we are likely to see overall retail sales growth ranging from 2% to 2.75% for the remainder of 2015 and this trend will continue through to 2016.

He explained that given the stagnation with respect to real retail sales growth, retailers will be cautious to opening new stores and with the current over-supply, it is certainly a 'tenant market' and landlords will need to be continually 'creative' in securing new tenants.

"The cautious approach by national retailers will mean further pressure on centre vacancies, but not across all centre classifications. For example, national retailers will be scrutinising renewal terms far more stringently and landlords need to be prepared to offer either flat escalations or, in some cases, rental reversions."

New retail developments planned for 2016 openings will face challenges in ensuring these centres open fully let, or are still offering the same overall return as initially projected due to current economic conditions, he said.

Inside shopping centres

According to Gaddy, large and super regional shopping centres should, by all accounts, be able to weather the storm with respect to increasing vacancies and rental growth. The diverse range of tenants, coupled with a leisure/lifestyle offering in these centres, will continue to draw consumers to their doors.

"While footfalls don't always translate to turnover, the wide assortment of tenants (value, semi-luxury, mid-range, discount, food and entertainment) will still lure cash-strapped consumers to this asset class although year-on-year growth may be muted."

Similarly, he said that convenience centres should also be able to survive the impact, but we may see further delinquencies in the 'independent' sector. Grocery anchors along with certain franchised food service outlets who are the mainstay of convenience/neighbourhood centres are not likely to feel a major downturn as people still need to eat. Recent economic data pointing to the fact that food inflation has remained relatively stable bodes well for this sector.

Community and small regional centres, mostly in metropolitan areas, could see added pressure on vacancies and rental growth - this is where national retailers may ponder a little longer on whether they will, in fact, be renewing leases. Marginal stores with higher than average rent-to-turnover ratios may see closures/non-renewals and landlords may also have to bear the brunt of flat escalations in order to retain certain tenants.

Interestingly, retail trading in rural markets will be less affected as many of these consumers do not have financial commitments, such as paying off of home loans and cars for example.

"Retailers would prefer to focus their energies on better performing stores, which are more often located at large and super regional centres as their conversion ratios are far better at these stores."

He added that these centres typically see higher footfalls/m² of GLA and the converse of this is the fact that grocery anchors, in most cases, do not perform as well at the larger retail centres.