ICSC
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Canadian Shopping Centres Steadily Evolve

Industry retains balance in adjusting to broad demographic and technological trends

Abstract: *This article is a follow-up to an* Industry Insights *article on Canadian trends published December 20, 2017. It reviews the major trends affecting retailers and shopping centres in the nation in the past year. It is based on interviews with John Crombie (ICSC Provincial Chair for Ontario, Canada); Robert Boyle (Senior Director, Retail Research, Ivanhoé Cambridge Inc.); and Maureen Atkinson (Senior Partner, Research Insights, J.C. Williams Group).*

Although stability is a hallmark of the Canadian shopping centre industry, landlords and tenants have been propelled forward by broad-based change. Consumers, already empowered by their sheer numbers, are exerting additional influence through technology. The results can be seen in everything from how centres have been leased to how they are preparing for a sustainable future.

1. Demographics

Age, racial and ethnic influences

Projections call for more Canadians entering their peak spending years between 35 to 54 starting in 2020—a shift from the last 10 years, when there were more people leaving than entering that age cohort. (See Chart 1.) That differs from the United States, where the reversal occurred five years ago.

Although Millennials have been much discussed in the business media, generalizations about them should be kept to a minimum because of their wide age range. While most members of this age group have entered the workforce, some are still in post-secondary school and, therefore, not spending as much.

Even so, Millennials, through sheer numbers, are already making their presence felt through their influence on the shopping centre industry, including through:

- greater interest in food and beverage (F&B) offerings;
- greater use of mobile devices/shopping assistants;
- greater interest in "seamless" digital-physical channels; and

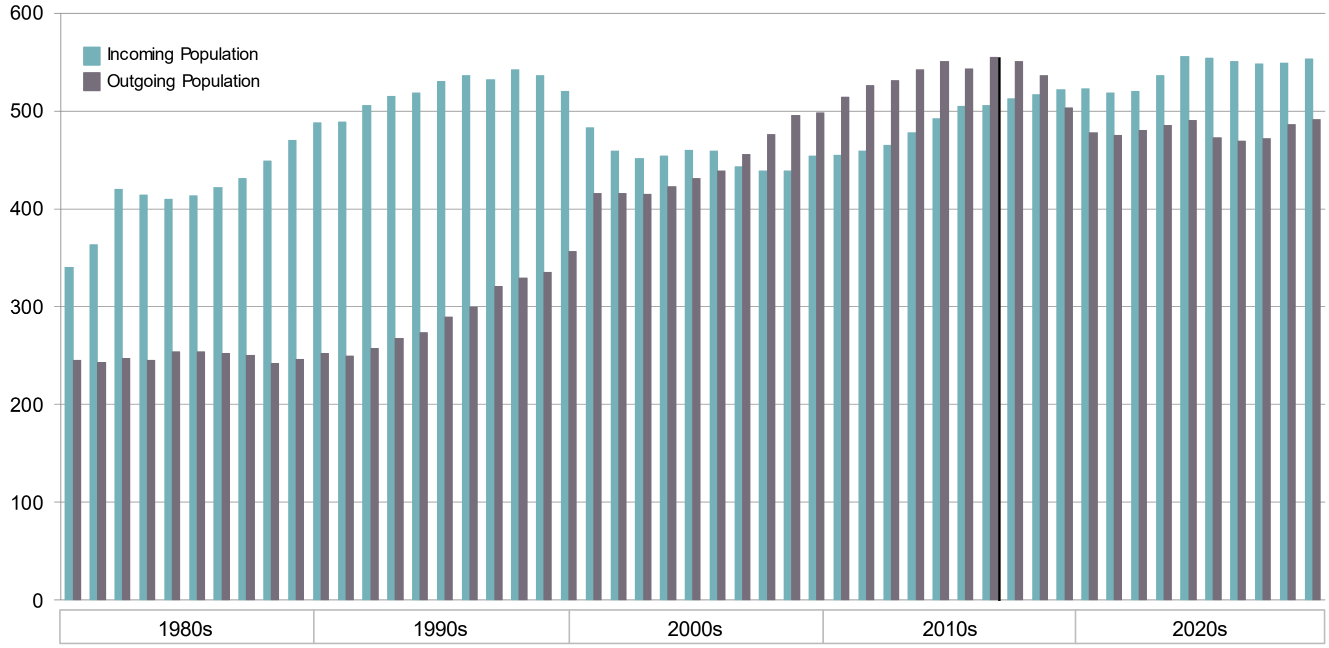
Lessons Learned

Though rarely shifting to rapid acceleration, the Canadian shopping centre industry has been marked by continual, consistent advances:

- ***Millennials***, through sheer numbers, are already influencing the shopping centre industry by their greater interest in food and beverage (F&B) / service offerings, use of mobile devices/shopping assistants, interest in "seamless" digital-physical channels, and use of the walkable "live-play-work" environments found in mixed-use centres.
- While vitally interested in ***mixed-use projects***, developers, unlike those in the United States, tend to be more constrained by a web of zoning restrictions.
- ***Top pension funds*** not only continue to own most major malls in the nation, but continue to reinvest in existing assets to enhance the offering and experience.
- To fill space and inject excitement into centres, landlords are introducing a host of ***new experience- and entertainment-based tenants***, including luxury cinemas, entertainment centres, and non-retail amenities/services such as performing arts, rock-climbing lessons and gyms.
- ***Food halls*** have tended to work best in urban, higher-income, health-conscious areas.
- ***Store openings*** have proceeded incrementally, marked by caution about the economy and NAFTA negotiations with the United States, while landlords have been prepared for a while to absorb the impact of any store closings.
- Interest in ***cannabis retailers*** has been inhibited by provinces' different sales regulations.
- ***International retailers*** *coming to Canada* in 2018 largely engaged in one- or two-store openings rather than more intense expansion.
- ***Pop-ups*** tend to be well-known brands and often occur seasonally.
- Though ***retailers' transition to omni-channel strategies*** is not proceeding at the pace maintained by the U.S. and U.K., it is still advancing, especially through "click-to-brick" openings and the practice of "click-and-collect."
- Integrated building energy management is one of the more common ***environmental initiatives***, as it dovetails with centres' desire to drive down electrical costs, improve net operating income and maintain their commitment to sustainability.

Chart 1

Canadian Consumers' Peak Spending Years (35-54 Years Old), 1980-2030



Sources: Euromonitor International, ICSC Research

- greater use of the walkable "live-play-work" environments found in mixed-use centres.

Millennials and Gen Xers are also not investing in the housing market the way prior generations did. Instead of large homes, their expenditures are being directed toward condominiums, or even experiences. Instead of spending on decks or fences, they might do so on home furnishings, in-home "smart" technologies (e.g., Alexa) or other less-expensive options.

Different racial and ethnic groups—notably, the Chinese and South Asian communities—are also impacting centre development and marketing, in addition to consumer spending. A major influence is not just family but multi-generational. Various Asian-oriented shopping centres/malls in suburbs of Toronto, Vancouver and Calgary cater to many of these consumers. Older men represent a particularly sizable part of this group, with F&B a major part of their expenditures. These groups, along with many others, are heavily represented in Toronto and Vancouver, and to a somewhat lesser extent, Calgary and Edmonton.

2. Real Estate/Property Considerations

Mixed-Use, Weighing Different Property Types

In Canada, as in the United States, landlords remain vitally interested in mixed-use development. But unlike their southern neighbors, Canadian developers tend to be more constrained by a web of zoning restrictions. Moreover, with few tenants in excess of the 100,000-square-foot footprints associated with many big-box anchors, landlords are forced to split the space. In those cases, gyms come closest to filling the space.

Other major property types—office, hotel, residential and entertainment—have attracted interest from developers as space alternatives. In the past, for example, potential office tenants sometimes kept their distance. But now, with the rise of the time-pressed consumer, it makes more sense to locate office spaces near or in shopping centres.[1]

In terms of residential space, Canadian Baby Boomers, while downsizing, are tending to stay close to where they already are—either in smaller communities around the urban core, or in urban centres themselves, making condominiums a particularly compatible accommodation type. (In Ontario, for instance, "Green Belt" restrictions passed in 2005 have increased the level of densification, which is more cost-effective for municipalities.)

In this environment, landlords are looking to opportunities to maximize space value. One company that has launched particularly aggressive plans to do so is RioCan, which has set up a new unit, RioCan Living™, which seeks to convert retail centres into mixed-use developments.[2]

Entertainment has come into the spotlight, too, especially through The Rec Room, a chain of restaurants owned by Cineplex Entertainment. This "Eats and Entertainment" concept offers dining experiences with live entertainment and amusement gaming. In the last couple of years, locations have opened in downtown Toronto, as well as in malls or mixed-use centres in West Edmonton Mall, Calgary's Deerfoot City, and Masonville Place (London, ON). Two more are planned in 2019: Square One, Mississauga, ON, and The Amazing Brentwood complex in Burnaby.[3]

[1] Logistical considerations also may enter into office location decisions. Four areas in Toronto, for instance, are expected to experience major growth in the next 25 years due to major infrastructure investment by the provincial government: East Harbour, Vaughan Metropolitan Centre, the Pearson Transit Centre and the Hurontario Light-Rail Transit corridor. See "Four Growing Commercial Hubs in Toronto," *www.Reminetwork.com*, November 28, 2017.

[2] "RioCan Launches New Residential Brand RioCan Living," *www.RioCan.com*, March 5, 2018 press release.

[3] "Letter to Shareholders," *Cineplex Inc. 2017 Annual Report*, February 21, 2018.

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Chart 2A
Pension Funds' Share of Gross Leasable Area (GLA), 100 Largest Malls

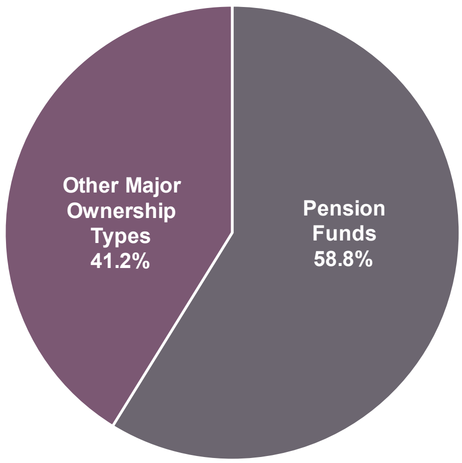
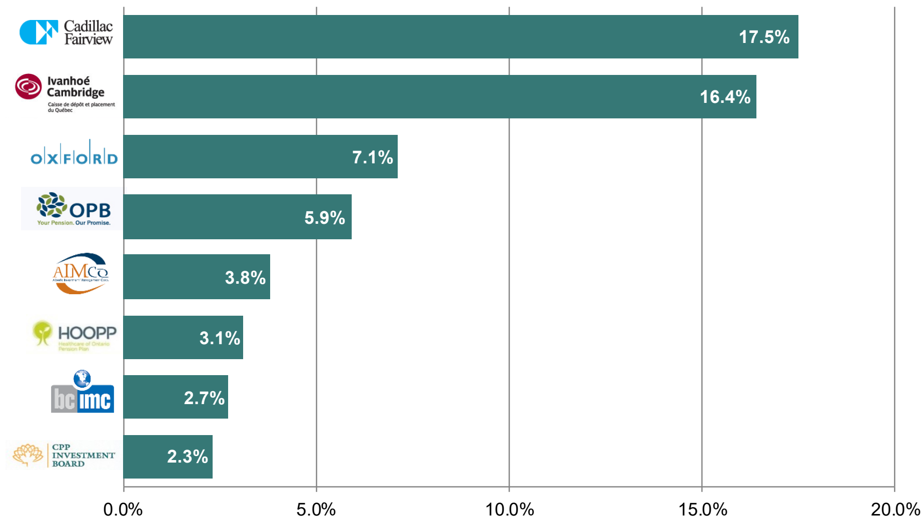


Chart 2B
Breakdown by Individual Pension Funds' Share of GLA, 100 Largest Malls



Source: Ivanhoé Cambridge Retail Research; figures current as of Q3 2018.

Institutional Ownership of Major Malls: Most Significant Effects

Most major Canadian malls continue to be owned by pension funds. In fact, the top pension funds continue to reinvest in existing assets to enhance the offering and experience. Approximately three-fifths (58.8%) of gross leasable area (GLA) in the nation's 100 largest malls are owned by pension funds, as seen in Charts 2a and 2b. Their attitude might be best summarized as "Be the best and sell the rest"—i.e., occupy the best real estate with the biggest size in the biggest markets. That may mean selling properties in secondary or tertiary markets.

With this concentration of the most sales-productive malls comes a high barrier to entry into particular markets, and considerable stability. Mall landlords tend to view their properties as long-term investments.

Experience and entertainment

Increasingly, Canadian landlords view experience-and entertainment-based tenants as a means of filling space and injecting excitement into centres.

Although cinemas have long been a part of Canadian malls, landlords are introducing a new wrinkle into this experience with luxury cinemas. A new five-screen premium movie theatre from Landmark Cinemas will open at CF Market Mall in Calgary by the spring of 2019. The cinema, which will feature digital projection and recliner seating, marks a departure from recent theatre development in the nation, which tended to emphasize larger footprints.[4]

The first Cirque du Soleil family entertainment centre in Canada, CREACTIVE, will open at Vaughan Mills in 2019. The recreational activities at this venture will include bungee jumping, wire and trampolines, mask design, juggling, circus track activities, dance and more.[5]

Shopping centres are also adding non-retail amenities/services such as performing arts, rock-climbing lessons and gyms. (In the case of gyms, the sizable population of Baby Boomers has sparked interest in exercise and associated health and wellness activities.) In addition, some malls have accommodated cooking exhibitions by local or celebrity chefs, notably at two Oxford Properties centres in Ontario: Upper Canada Mall (Newmarket) and Square One.

Food: consumer expectations and tastes

More and more, food has become elevated in importance and consumer expectations. Food halls have attracted particular interest for their ability to add local flair and seasonal flavoring. At the same time, centre owners are reluctant to launch a building spree for this type of development lest it subtract from what has made it so different and unique. Food halls tend to work best in urban, higher-income, health-conscious areas, such as Assembly Chef's Hall, which opened at Oxford Properties' 111 Richmond Street West in Toronto a year ago. In addition, the British media company Time Out will open its gourmet food hall Time Out Market at Centre Eaton de Montreal in late 2019.[6]

As F&B tenants become more common, some landlords have looked to single operators of food halls such as Mercantino's that can control pricing and offerings. If operators see a sales shift for particular concepts, they can follow the trends and adjust quickly. This ensures that the hottest concepts enter the tenant mix quickly; that concepts losing favor are kept to a minimum; and that food offerings can be customized to the season.

Other centre visitors still prefer fast, cheap food. For this latter group, an alternative might be food courts with additional, healthier options.

Canadian ***groceries*** also represent an essential part of the Canadian food environment. Competition and consolidation were

[4] Mario Toneguzzi, "Cadillac Fairview Partners with Landmark Cinemas: Announces Premium CF Market Mall Theatre," *Retail Insider*, January 29, 2018.
[5] "The First CREACTIVE in Canada To Open at Vaughan Mills in 2019," www.invanhoecambridge.com, June 21, 2018 press release.
[6] Tim Forster, "Mega Food Hall Time Out Market Is Coming to Montreal," *Eater Montreal*, May 30, 2018; "The New Centre Eaton de Montreal is Under Way," *www.centreeatondemontreal.com* (Undated press release).

the hallmarks of this landscape even before Loblaws' takeover of Shoppers Drug Mart and Amazon's acquisition of Whole Foods, and they remain so after Sobeys' recent buyout of Farm Boy. The situation is further complicated by the fact that Canadian e-commerce capabilities have not measured up to those of other major countries. However, the nation's supermarket operators, if past performance is any indicator, should react rapidly to challenges to retain their loyal shoppers.

3. Retail

Store openings and closings

Store openings in Canada have proceeded incrementally, marked by caution about the economy and NAFTA negotiations with the United States. Although service and entertainment tenants continue to be sought after, other more unusual retail tenant types (aside from those in food halls, already discussed) are helping landlords maintain occupancy rates.

Toronto-based mattress maker Endy has followed the lead of firms like glasses retailer Clearly, suit maker Indochino, and clothing retailer Frank and Oak in opening physical locations after starting as online-only ventures.[7] More such companies are expected to appear in shopping centres as these "Internet first" retailers realize the brand awareness that accrues from brick-and-mortar.

In the wake of legalization of marijuana in October 2018, intense curiosity has also spread about ***"cannabis retailers."*** The one inhibiting factor at the moment concerns each province's different sales regulations. The appetite for these shops can be seen especially in one province, Alberta, where physical stores are run privately rather than by the government. Nineteen stores opened there in the first day of legalized sales. Within a year, the provincial government expects 250 stores to open.[8] These retailers are relatively new with unproven potential, so the consumer response to them is unknown at this point.

In addition, ***dollar stores*** have been extremely active. The company implementing the most aggressive expansion strategy is Dollarama, which now operates 1,000 stores across the country.

As for store closings, they generally do not have the same kind of widespread impact as in the United States. They may not have even the same kind of impact that they have had in Canada itself in the recent past. Closures at long-ailing Sears Canada, for example, have not produced the same shock as Target Canada's 2015 shutdown of all its 133 stores, after only 26 months in the market. In fact, landlords have often been glad to have the Sears Canada spaces back, as they had not generated as much traffic lately.

Hence, the long-term decline of Sears Canada has also led Canadian landlords to anticipate its vacancies. It is unlikely that a single major big-box retailer will fill all the space. Older stores, dating as far back as the 1960s, may be demolished or redeveloped. Other options include a combination of F&B, entertainment, and smaller in-line tenants. In any case, landlords will likely devise market-specific solutions.

Currently, mall landlords are watching The Bay to see if it can stave off the fate of Target Canada and Sears Canada. But challenges elsewhere in the Canadian retail sector are not as stiff as for department stores. For instance, no major Canadian apparel retailer declared bankruptcy in the first eight months of 2018.

Despite its closures in the United States, Toys 'R' Us continues to operate in Canada, attracting cross-border traffic from Detroit, for instance, to its Windsor store.

International firms

Various news reports indicate that, instead of intense expansions, international retailers coming to Canada have tended to engage in one- or two-store openings that either test the waters or build carefully on an initial success.

One area of the world that has not contributed significantly to this foreign surge is the United States. The failures of Sears Canada and Target Canada may well have led some companies to reconsider an aggressive expansion of their own.

Instead, at least some of the slack has been taken up by retailers based in Asia (MUJI and Uniqlo, both from Japan), as well as Europe (Sephora, based in France).

As in the last few years, luxury retailers from abroad have continued to establish footholds, including Nordstrom Rack and the eyewear retailer Oliver Peoples. For the most part, these companies have opened a select few stores (e.g., in Toronto, Calgary, Edmonton and Vancouver) without plunging in deeper at this point.

The past year also proved very strong for tourism, not only from the U.S. but from Asia in general and South Korea in particular. The Canadian dollar has been low, helping to drive the sector, with luxury spending especially boosted. The guest services desk and some retailers at Yorkdale, Metropolis in Vancouver and Premium Outlet Collection Edmonton International Airport, for example, implemented Alipay, a mobile-based payment method used by Chinese consumers.[9] Initiatives such as this have helped make tourists 20 percent of that mall's consumer base.

Pop-Ups

Major landlords are looking at pop-ups as a means of injecting newness or excitement into selected mall tenants anywhere from a few days to several weeks. These are often well-known brands that open seasonally, such as in the summer. Still, they are not as commonly found as in the U.S.

In the last couple of years, pop-ups have included the Ikea Play Café in Toronto, La Maison Simons (in a partnership with Finnish fashion design house Marimekko), Hudson Bay's The Collections (a pop-up shop with 12 Canadian designers), Nordstrom's ¡Viva Mexico!, Holt Renfrew's Stone Island, House of Marley at Vaughan Mills, and at Toronto Eaton Centre, Google and Amazon.

E-commerce/Omni-Channel Considerations/Strategies

While Canadian shoppers are tech-savvy and quick to adopt new technology, their retailers have been slow to keep pace. At least part of this is a logistical challenge. With a sizable majority of the population living within 100 kilometres of the border with the U.S., that leaves a long, thin supply line thousands of miles long

[7] Peter Nowak, "URBAN HORIZONS: Online Merchants Venture Into the Real World, Changing the Retail Landscape," *The Globe and Mail* (Toronto), October 22, 2018.
[8] Josh Dehaas, "Provinces Raked in Revenue on Day One of Cannabis Sales," *www.ctvnews.ca*, October 18, 2018.
[9] Megan Harman, "'Golden Week' Campaign Uses AliPay App to Target Chinese Tourists," *Retail Insider*, September 30, 2018.

for transporting goods to retailers. Hence, servicing the e-commerce market is difficult.

Nevertheless, though the transition to omni-channel strategies is not proceeding at the pace maintained by the U.S. and U.K., it is still advancing. Previously "pure-play" (Internet-only) retailers continue to open physical locations, such as Toronto-based mattress maker Endy and Ottawa-based Shopify, which helps merchants set up their own e-commerce operations.

To one extent or another, retailers have been adopting different practices to move into the new omni-channel era, including opening warehouses near consumers, enhancing their ability to ship from stores and warehouses, and designating more staffers for social media, chat and e-mail. But the most widespread practice appears to be click-and-collect. It seems to be especially popular with Canadian grocers, such as Loblaws, which has now set aside space for lockers.

Environmental practices

Canadian landlords and their tenants are experimenting with a host of environmental initiatives, including, in Quebec, rooftop gardens (at IGA) and beehives (at Simons department store). Many consumers if asked, however, would be unaware of these efforts, except for recycling—perhaps because they are not readily noticeable to the public.

Companies' efforts to anticipate environmental needs may also be complicated by alterations in governmental policy. A change in parties in Ontario, for example, has resulted in the recent repeal of the Green Energy Act.

One powerful force for enhanced environmental practices may be pension funds. Across entire portfolios, these institutions want to ensure that proper "green" protocols are being followed. A major focus of their interest, integrated building energy management, dovetails with centres' desire to drive down electrical costs and improve net operating income.

Conclusion

While seldom shifting to rapid acceleration, the Canadian shopping centre industry has been marked by continual, consistent advances. Logistical and management structures are likely to continue to encourage gradual change while mitigating the urge to engage in greater risks.

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