Routledge Companion to Real Estate Development

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Retail market analysis for development projects

Publication details
https://www.routledgehandbooks.com/doi/10.4324/9781315690889.ch8

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Published online on: 10 Aug 2017

How to cite :- Petros Sivitanides. 10 Aug 2017, Retail market analysis for development projects from: Routledge Companion to Real Estate Development Routledge
Accessed on: 01 Jan 2024
https://www.routledgehandbooks.com/doi/10.4324/9781315690889.ch8

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Retail market analysis for development projects
Coping with new frontiers in retailing

Petros Sivitanides

Abstract
The successful development of a retail scheme in today’s competitive and ever-changing retail marketplace presents a formidable challenge to real estate entrepreneurs. Market analysis is one of the most crucial stages in designing a retail development scheme that will successfully cope with the new challenges of today’s retail marketplace. Within this context, this chapter discusses first the new frontiers in retailing as well as their implications in terms of planning new retail development projects and assessing their market potential. It then proceeds with the discussion of the four basic stages of a typical market analysis for a retail development project, while pointing out in each stage the relevance of the new trends in retailing. The first stage focuses on the different methodologies for defining the project’s trade area, while the second stage focuses on the analysis of competing retail developments, which needs to take into account features that make them more attractive in the new retailing environment. In the third and fourth stages the focus shifts on consumer shopping patterns and the estimation of the project’s sales potential and supportable square footage, with special emphasis on assessing as accurately as possible potential in-store sales as opposed to online sales.

Introduction
Over the last decade, the retailing landscape has been undergoing significant structural changes as a result of the rapidly growing use of the internet and mobile devices by consumers and businesses alike around the globe. These structural changes include the steadily and rapidly rising share of retail sales captured online; the emergence and implementation of multi-channel strategies that integrate e-commerce with physical store space; and the changing role of the physical store to better complement the online shopping experience (Piotrowitz and Cuthbertson, 2014; Platt Retail Institute, 2014). In addition to these developments, the consumer base has been undergoing significant structural changes in its composition and characteristics that have direct implications on shopping demands and preferences (Platt Retail Institute, 2014). These new frontiers in retailing have important implications in terms of optimizing the design and assessing the potential of a retail development project in today’s
environment. Thus, when carrying out market studies for retail development projects the implications of these trends need to be appropriately taken into account when quantifying demand for the specific project and assessing the competition.

Data from the USA confirms the rapid growth of online sales over the period 2000–2014. Online sales in the United States grew from about $5 billion in 2000 (representing 0.9 percent of total retail sales) to $299 billion in 2014 representing 6.4 percent of total retail sales. No arguments have been presented in the literature as to why this consistent and rapid growth of e-commerce’s share should cease. On the contrary, the continued rise of this share seems unavoidable due to the rising percentage of the population that gains daily access to the internet worldwide; the vastly superior capabilities that the internet provides in terms of price comparison and product assortment; and the evolving e-commerce technologies that continue to upgrade and enrich the internet shopping experience.

As e-commerce continues to grow, many retailers are led in the adoption of multi-channel strategies integrating management of customers, pricing, and retail mix across online and offline sales channels (Verhoef, Kannan, and Inman, 2015). The need for such an integration is reflected in the rising popularity of click and collect. Click and collect allows consumers to take full advantage of the superior capabilities provided by the internet in terms of price and product search, and at the same time gain possession of the product quickly by picking it up from their closest store (Piotrowitz and Cuthbertson, 2014).

The seamless integration of online with in-store shopping is changing the role of the physical store, not only as the point at which consumers can have a three-dimensional interaction with the product, or pick it up after ordering it on the internet, but also as the point that integrates all channels of interface with the customer. According to Piotrowitz and Cuthbertson (2014) the new role of physical stores will also be characterized by increasing in-store technologies, such as interactive screens and augmented reality, as well as appropriate store layout design to organically incorporate them in the store functioning and customer shopping experience.

Another important dimension of the new frontiers in retailing is the changing structure of the consumer base. This new structure is characterized by a basic dichotomy in the consumer makeup, consisting of the aging baby-boomers with high buying power, and a new internet-addicted generation, born between the early 1980s and early 2000s and referred to as “Generation Y” or the “Millennials,” with considerably smaller buying power (Platt Retail Institute, 2014). The other major characteristic of the changing consumer base is the increasing multiculturalism and diversity, manifested in an increasing number of diverse consumer groups seeking specialization, customization and niche interest products and services (Platt Retail Institute, 2014).

Implications of new frontiers for retail market analysis and shopping center design

The new frontiers in retailing have important implications in terms of planning new retail developments and assessing their viability. First of all, the increasing market share of internet retailing at the expense of bricks-and-mortar retailing, points to the risk of diminishing demand for store space in retail developments (Henderson Research, 2013). According to Platt Retail Institute (2014) there have been estimates that by 2025 40–70 percent of retail transactions might take place online. On the other hand, Damesick (2001) and Hortacsu and Syverson (2015) suggest that the rise of the internet shopping may not necessarily result in the demise of the physical store, but in a “bricks-and-clicks” hybrid retailing format. Along the same lines, AT
Kearney (2014) suggests that the two channels may end up complementing each other with e-commerce “specializing in product search and discovery” and physical stores in product testing, purchase, and return. Although there are varying opinions in terms of the size of the negative effect of the internet on demand for physical store space, this debate underscores the importance of a thorough market analysis for retail development projects, and the accurate assessment of the online and in-store shopping patterns of the consumer groups within the project’s trade area.

The rise of internet retailing has important implications in terms of designing an appealing and attractive retail development concept and tenant mix. In particular, the fierce competition from the internet points to the need for transforming the shopping center from mostly a shopping destination to a destination of “meaningful lifestyle experiences – fun family destinations where all age groups can spend quality free time together” (Evans, 2014, p.37). Such transformation requires a considerable increase of the non-retail tenants and specifically food and beverages, leisure, entertainment, and services in order to provide a pleasant three-dimensional experience that cannot be replicated in the two-dimensional electronic space. According to Evans (2014), the optimal level of the leisure component is 25 percent of the tenant mix and he predicts that leading shopping centers will increase their leisure component to such levels in the short term.

Another implication of the recent trends in retailing in terms of tenant mix is the importance for new retail developments to include technology-savvy tenants that have embraced the new technologies and offer a seamless integration of physical and electronic space. The inclusion of such tenants will reduce the longer-term risk of the development, as they are more likely to withstand the challenges of the new environment and provide the shopping center owner with a more stable cash flow in the long term. Furthermore, the development will be more attractive as the consumers will be able to enjoy an integrated online and in-store shopping experience.

The new demographic frontiers also have important market analysis implications as they call for in-depth consumer research, so as to accurately identify the diverse consumer groups that compose the project’s clientele and thoroughly map their shopping habits, both online and offline, as well as their leisure, entertainment, and other preferences. Such an analysis will provide a solid basis not only for designing an appealing tenant mix so as to best serve the project’s clientele, and strengthen its “destination” character, but also for accurately assessing the supportable square footage for the different lines of trade that will be included in the project. Within this context, the analysis of consumer profiles and their shopping patterns in the development’s trade area is of crucial importance in evaluating and refining the project concept so as to successfully cope with the new frontiers in retailing.

**Market analysis for retail development projects**

The market analysis process for evaluating a retail development concept focuses on the analysis of demand for the goods and services that are expected to be traded at the project and the analysis of the competition. The new trends in retailing discussed earlier are relevant in the analysis of both the demand and the supply side of the market. In order to properly analyze these two aspects for a particular development, the project’s trade area needs to be defined first. Thus, the market analysis process includes four basic stages for estimating the project’s supportable square footage in different product lines. The first stage includes the preliminary definition of the project’s trade area and the second the refinement of its boundaries through the detailed analysis of the competition. The third and fourth stages include the analysis of the shopping patterns of the consumers residing within the trade area and the quantification of the project’s potential sales and supportable square footage in the different product lines expected.
to be traded at the center. These four stages along with the relevant analytical implications of new frontiers in retailing, wherever applicable, are discussed below.

**Stage 1: Preliminary definition of the boundaries of the development’s trade area**

A retail project’s market or trade area is the area encompassing all locations from which the majority of its clientele is drawn. For this reason, it is important to define the geographical boundaries of the project’s trade area before proceeding to the analysis of consumer demand and the competition. At this stage the new trends in retailing are not relevant, as a typical methodology for the preliminary definition of a project’s trade area is based on reasonable maximum driving times that consumers are willing to drive depending on the typology of the retail cluster under consideration. In estimating driving times to the site under consideration the analyst needs to take into account road access, speeds, and the configuration of the area’s transportation network, as well as public transportation routes. The driving time norms typically used in the industry for the different types of retail clusters are 15 minutes for a neighborhood center, 30 minutes for a community center, 45 minutes for a regional center, and 60 minutes for a super-regional center (Schmitz and Brett, 2001).

A more simplistic approach for defining the project’s trade area is the concentric ring approach, which defines the boundaries of the development’s primary trade area as a circle with a radius that varies depending on the type of the development considered. According to Schmitz and Brett (2001), the industry norm with respect to the length of this radius, measured in straight distances, is one and a half miles for a neighborhood shopping center, three to five miles for a community center and eight to 12 miles for a regional mall. The major pitfall of this approach though is that it ignores the uneven accessibility patterns as determined by the area’s topographical characteristics and the existing transportation and public transit network.

A more complicated approach for a preliminary definition of the project’s trade area is the “near twin” or “analog” approach, according to which the geographic capture of existing similar retail developments is used to guide the determination of the geographic capture of the planned development (Fanning, Grissom, and Pearson, 1994). “Near twin” developments are selected on the basis of their similarity to the planned development in terms of several factors, including development type and size, tenant mix, layout, and physical design, surrounding streets, location with respect to downtown and other competing retail clusters, access and distance to sources of demand, and volume of traffic on adjacent streets for stop–off business. Once the “near twin” development is identified, information is collected regarding consumer shopping patterns, such as frequency of visits by type of consumer and by location, in order to provide the basis for identifying the spatial extent of the project’s area of influence and the delineation of the development’s primary, secondary, and tertiary trade areas. This approach is expensive to implement though and may not be feasible or lead to inaccurate definition of the project’s trade area and its potential clientele, if true “near twin” developments cannot be found.

Once the boundaries of the trade area have been defined through any of the above approaches, they can be adjusted to account for the effect of competing developments using the simple gravity approach introduced by Reilly (1929). This approach can be used to estimate how far the planned project’s attraction extends, given its characteristics and distance from a specific competitor and the characteristics of the competitor. According to the modified gravity model presented by Converse (1949), the distance to the boundary of the trade area of center $j$ (TAB) with respect to competing center $k$, depends on the distance between the two centers ($d$) and the relative attractiveness of the two centers, measured typically by their size ($S_j$, $S_k$) or other attributes (see Figure 8.1).
This technique can better account for multiple project characteristics in addition to size, if $S_i$ and $S_j$ are replaced by indices that are based on a comparative scoring system of the different characteristics (including size) of the planned project and its competitors. For example, the Total Amenity Indices that can be developed using the Competitive Differentials Technique (which is discussed in a subsequent section) can be used instead of $S$ in order to better reflect the attractiveness of center $j$ vis-à-vis center $k$.

The boundaries of the trade area should also be adjusted taking into account any socio-economic and cultural/ethnic barriers that may have an effect on visitation rates from particular population groups. For example, Hardin and Carr (2006) have found that higher income households may not patronize community centers in areas with high concentrations of households on public assistance even if they are the closest ones to their location. A final adjustment will be needed in order to align the boundaries of the development’s trade area with the geographic boundaries of area definitions for which secondary population and income data is available, such as counties, census tracts, zip codes, or blocks. For example, if a census tract is used, Carn et al. (1988) suggest that it can be included in the trade area if more than 50% of its geographic area is contained within the line representing the maximum driving time from which customers can be drawn to the development under consideration. Carn et al. (1988) suggest that blocks may be used for neighborhood shopping centers, census tracts or zip codes for community shopping centers, and counties for regional shopping centers.

The most advanced and accurate approach in determining a retail development’s trade area is the advanced probabilistic approach, which estimates econometrically the project’s capture rates from the homogeneous residential zones that are within reasonable driving distances. These capture rates can then be used for more accurately defining the development’s trade area by including all the residential zones with a minimum capture rate. However, its application requires a preliminary definition of the development’s trade area using the techniques just discussed. This approach is discussed further in the section focusing on the estimation of the planned development’s sales potential.

**Stage 2: Analysis of the site/project and its competition**

The analysis of the competition is very important in further refining the trade area boundaries using the gravity model discussed earlier. Furthermore, the analysis of all competing projects is crucial in accurately assessing the sales potential of the project under consideration in today’s highly competitive environment. The new frontiers in retailing are quite relevant in analyzing the strength of the competition in terms of four aspects. These new-frontier aspects include the availability of the necessary technological infrastructure so as to allow wireless internet access at any point of the center; the extent to which the tenant mix includes strong entertainment, leisure, and service components that reinforce the center’s destination character;
the variety of product assortment and the extent to which it appeals to a multicultural consumer base; and the resilience of the specific tenants of the center to internet penetration, which will depend on the types of goods they sell and the degree of integration of the physical and electronic shopping experience. Given the new trends in retailing, these factors can play a key role in determining the attractiveness of the project under consideration against the competing projects.

The analysis at this stage focuses both on location and project characteristics. In analyzing the location attributes of the competing projects, special attention needs to be given to the particular access to the site from the nearest major thoroughfare, as well as its broader access to consumers by car and public transportation; the attractiveness of the project’s immediate environment; and the demographics and income characteristics of nearby residential neighborhoods. In analyzing the characteristics of competing projects the focus is on the main factors that affect their drawing power, including those relating to the new frontiers in retailing. These characteristics include, but are not limited to, the building-to-land area as a measure of the project’s building density; the total Gross Leasing Area (GLA), which is an important center size indicator; GLA by major categories of retail goods, services, leisure, and entertainment, which provides the broader tenant mix of the development and can help assess its strength as a destination character; number of stores in different product lines as a measure of product mix, which was found to be one of the most important factors in affecting shopping center choice by millennials (Larsen, Selton, and Wright, 2015); technological infrastructure and access to the internet; landscaping, design, aesthetics, and appeal of internal layout; and parking availability.

Beyond the above, a detailed analysis of each competing project’s tenant roster is required in order to better understand and evaluate the attractiveness of its detailed tenant mix and assess the variety and quality of the goods and services offered. Detailed tenant analysis identifies among others, anchor and non-anchor tenants, goods/services sold by each store, brand reputation, the particular providers of non-retail services, such as leisure, entertainment and other services, and the square footage occupied by each use and individual tenants. As indicated earlier, an important dimension of the tenant profile that has to be examined from a new-frontiers perspective is the extent to which they have integrated successfully in-store and offline shopping channels with online shopping channels.

Finally, information on the performance of competing centers such as rental rates and other tenant charges, visitation rates, sales per square foot, and occupancy rates can help not only better assess the strength of competing projects but also assess the potential performance of the project under consideration in terms of these indicators, taking into account its characteristics. However, performance measures and rental rate paid by each tenant or detailed categories of tenants, apply only to existing operating projects and it may be difficult to obtain, as they represent confidential information that the owners of competing projects are reluctant to share.

Once the detailed attributes of the planned project and competing developments are systematically and comprehensively listed they have to be analyzed in order to identify the project’s strengths and weaknesses and assess its competitive position in attracting consumers. This comparative analysis can be carried out through the Competitive Differentials Technique, which is a non-econometric approach and does not require significant additional information beyond the information on the characteristics of the competing projects. This technique is discussed by Clapp (1987) and provides a reasonable methodology for quantifying the multidimensional differences between the planned development and the competing projects. The major issue in using this approach is that it cannot quantify scientifically the different weights assigned by consumers to the different center characteristics when making their
shopping/patronage decisions. However, this may be a serious shortcoming in light of the rising importance of a handful of new-frontier related factors discussed earlier.

The differential effect of the various project characteristics on its attractiveness can be more accurately assessed using the econometric approach in which information on consumer shopping trips to and purchases at competing developments, in combination with information on the characteristics of these developments, is used to quantify the effect of the latter on the former (Weisbrod, Parcels, and Kern, 1984; DiPasquale and Wheaton, 1996). This methodology is discussed further in the estimation of the project’s sales potential using the probabilistic approach. From a new-frontiers perspective, the use of this approach can provide a more accurate assessment of the attractiveness of the project under consideration against its competition.

Stage 3: Shopping pattern analysis

Given that the new frontiers of retailing have to do with how the consumers interface with electronic and in-store shopping, their basic demographic structures, and their cultural diversity, this stage is of critical importance in accurately assessing the project’s potential sales and planned tenant mix. The third stage focuses on the consumer groups within the planned development’s trade area and involves primary research that aims at better understanding their characteristics, their shopping choices and spending patterns. The information on consumer characteristics and preferences will help in determining the most suitable tenant mix for the particular type of development and improving the project’s rating against the competition based on actual consumer preferences. The information on consumer spending patterns will provide the foundation for estimating the project’s sales potential by analyzing how consumer patronage preferences are influenced by consumer characteristics and retail cluster characteristics.

The information collected in this stage focuses specifically on consumer profiling within the project’s trade area in order to identify key characteristics such as age, income, household size, education, and ethnicity/culture (Sivitanidou, 2011; ICSC, 2005). This information will allow the segmentation of the population residing within the project’s trade area into distinct age and ethnic groups, and better identify their shopping, leisure, and entertainment preferences, as well as their spending patterns in different product lines both in physical stores and on the internet. The information that it is typically collected at this stage via the consumer survey is described in more detail in Table 8.1. If the consumer survey is carried out systematically to include samples from all residential zones within the development’s trade area, it can allow for the estimation of the project’s capture rate through advanced probabilistic modeling, which is discussed in the next section.

Stage 4: Estimating the project’s sales potential and supportable square footage

The main objective of the fourth stage is to derive estimates of the project’s sales potential and supportable square footage as a means of evaluating the feasibility and viability of the development concept under consideration. The key figure that is needed in order to estimate the development’s sales potential is its capture rate or market share, that is, the percentage of the trade area’s sales that the project will capture. One approach suggested by Fanning et al. (1994) for estimating the project’s capture rate is using the industry standard capture rate for the primary trade area, which is 70–80 percent, and adjusting it accordingly depending on the strength of the project’s location vis-à-vis the location of the major citywide retail clusters. If the location is among the strongest ones then the industry standard capture rate can be applied
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Table 8.1 Information collected for shopping pattern analysis

| a | Detailed demographics of the population residing in the different homogeneous residential zones that compose the project’s trade area including age, income, education level, ethnicity and household size |
| b | The different types of purchases made by each socioeconomic group and the specific retail clusters that are chosen for each type of purchase |
| c | The characteristics of all shopping trips made by the consumers, including travel mode, travel cost and time, as well as motivations for each trip, such as shopping, entertainment, leisure or other |
| d | The frequency of visits to the competing retail clusters by type of purchases |
| e | The amount spent on different types of purchases of goods and services in the different competing projects |
| f | Online purchases in terms of amounts and different product/service lines, as well as intentions in terms of future online purchases versus in-store visitations and purchases by line of trade |

to the project, otherwise it should be adjusted downwards depending on how weak the project location is compared to the strongest ones. According to Sivitanidou (2011), the project’s competitive position index, derived through the competitive differentials technique, is a more comprehensive and appropriate measure of the project’s relevant attractiveness as it takes into account not only its location but many other project characteristics including those that would make it more competitive in the new retailing environment. As such, the competitive position index is a more appropriate weight for adjusting the industry standard capture rate, as opposed to a location rating.

In terms of coping with the new frontiers in retailing, the most accurate approach for estimating the project’s capture rate and sales potential is the advanced probabilistic approach. This approach is more accurate in terms of assessing the implications of new frontiers in retailing because it can take into account the demographic and diversity/cultural characteristics of the particular consumer groups that reside within the project’s trade area as well as their in-store and online shopping patterns and shopping preferences. Empirical evidence has shown that differences in certain consumer characteristics are associated with different in-store and online shopping patterns. For example, Li, Kuo and Russel (2006) confirmed that higher income and educational levels are associated with higher online purchases while no statistically significant effect of age was found.

The information on consumer characteristics and their shopping patterns is collected in the third stage through consumer surveys in the different homogeneous residential zones that compose the project’s trade area. This information, along with information on the major characteristics of competing developments, can be used to estimate econometrically the probability that a consumer residing in a specific residential zone \( k \) and belonging to a particular consumer group \( y \), will choose to visit the planned development for satisfying its shopping needs for line of trade \( i \). This probability can be used as the capture rate \( (CR_{yi}) \) of the project for the specific zone \( k \), consumer group \( y \) and line of trade \( i \) and represents the percentage of sales that is expected to be captured from each residential zone in the development’s trade area. For a detailed discussion of this methodology see Weisbrod, Parcels and Kern (1984), and DiPasquale and Wheaton (1996).

Once the capture rate for each line of trade \( i \), residential zone \( k \) and demographic group \( y \) \( (CR_{yi}) \) is estimated, then the project’s total potential sales by line of trade \( i \) \( (SP) \) can be estimated using the formula shown in Figure 8.2.
Special caution is needed in applying the formula in order to ensure that the income measure used and the percentage of income spent on a particular line of trade \( e_y \) are consistent. Such percentages can be calculated from information that is collected from the detailed consumer survey in the analysis of the shopping patterns in the development’s trade area. In cases where a consumer survey is not carried out, such percentages can be obtained from detailed consumer expenditure reports that are usually provided by the national statistical service. In the USA, such information is provided by the Bureau of Labor Statistics (BLS). If this data is used for estimating \( e_y \), then the income measure that needs to be used in order to carry out the calculation is income before taxes because that is the income measure used by BLS in its cross-tabulations of expenditures in different product lines by age and income groups.

It should be noted that the consumer expenditure reports published by the BLS do not separate the spending for purchases in physical stores and purchases on the internet. Thus, if \( e_y \) is derived using the BLS data it will refer to both in-store and online purchases by households. However, in terms of assessing the supportable square footage in a planned development, the analyst needs to estimate the area’s potential sales in physical stores. That is the reason for taking into account in the formula the percentage of purchases carried out online \( (o_y) \). In cases where a detailed consumer survey in the project’s trade area has been carried out, this percentage should be available from the data collected through the survey. If a survey has not been carried out, an overall national percentage by line of trade can be used, based on the data provided by the Annual Retail Trade reports published by the Bureau of the Census. However, in such a case, the analyst needs to critically evaluate whether there is any strong rationale that would justify a significant deviation of the online purchases of the particular population within the development’s trade area from the national average and accordingly adjust the figure used for \( o_y \).

Once potential sales in each line of trade are estimated, then the analyst can estimate the supportable square footage by dividing these figures by the sales per square foot for the respective line of trade. Data for sales per square foot by line of trade and type of shopping center can be obtained from industry organizations, such as the International Council of Shopping Centers.

In sum, in order to accurately assess the project’s true sales potential and viability of proposed tenant mix, the estimation of the project’s sales potential and supportable square footage needs...
to explicitly take into account the online and in-store spending patterns of the consumers within the project's trade area. This is the most important analytical implication of the new frontiers in retailing, which retail property developers and their analysts should by no means ignore.

Conclusion

In this chapter we have discussed the new frontiers in retailing as well as the four basic stages of retail market analysis and the relevance of these new frontiers in each stage. The new frontiers in retailing are highlighted by the consistent and rapid rise of e-commerce’s share in total retail sales and the resultant competition with bricks-and-mortar retailing; the increasing use of multi-channel strategies by leading retailers; the changing role of the physical store so as to complement the online shopping experience; and the changing consumer base, with significant implications in terms of shopping preferences and spending patterns. These new frontiers in retailing have clear implications in terms of assessing the potential performance and viability of a retail development project in this new environment. A basic component of such an assessment is the market study.

The new-frontier aspects are not relevant in the first of the four basic stages of a retail market study but they are quite relevant in the other three. In particular, in the first stage, which is the preliminary definition of the project’s trade area, the new-frontier aspects are not relevant as the preliminary borders of the trade area are defined mainly on the basis of a maximum driving time. However, in evaluating in the second stage – the project against the competition – project attributes pertaining to the new frontiers in retailing must be taken into account along with other location and project characteristics in order to correctly evaluate project attractiveness in this new retailing regime. The third stage focuses on detailed analysis of consumer characteristics and shopping patterns within the project’s trade area. This stage is the most critical in understanding the implications of new-frontier aspects on the particular project by assessing the online and in-store spending patterns, as well as the shopping/leisure/entertainment preferences of its potential clientele. Within this context, the consumer survey of shopping preferences and spending patterns within the project’s trade area becomes one of the most critical components of the retail market study in the new retailing environment. The consumer survey and analysis carried out in the third stage provide a solid basis for estimating in the fourth stage the development’s true sales potential and supportable square footage by line of trade in a way that takes into account all crucial new-frontier aspects.

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