

Turkey: Modernizing through Mall Development

BY MARC LOUARGAND, PH.D., CRE®, FRICS

TURKEY IS A NATION THAT—BOTH LITERALLY AND FIGURATIVELY—has one foot in Europe and the other in Asia. More specifically, Turkey straddles the boundary between Europe and the Middle East. The contrasts between Turkey and Europe in terms of lifestyle, education and affluence are growing dimmer while their respective economies converge. Turkey is an emerging economy that has arrived. A nation of more than 70 million, it has a diversified economy and a young workforce unburdened by a large dependent populace, unlike many European countries. Yet Turkey also represents the ancient ways of the nomad, the souk and the bazaar. In the past five decades Turkey's population has shifted from 40 percent in provincial centers and sub-centers to 76 percent, a pace of urbanization matched only by China. During that period the economy has grown at a rapid pace and diversified dramatically. How does the culture evolve to keep up with such rapid change? A key element in the transition is the shopping mall and modern retail systems. This article describes the current state of retailing in Turkey, the forces at work transforming Turkish society and their integral relationship.

TURKISH ECONOMY

While the Ottoman Empire had been in decline for nearly a century of its 700-year history, its dissolution at the end of World War I marked an end to a religious and feudal state. In less than a century, the modern state envisioned by Mustapha Kemal Ataturk has emerged as a modern and thriving economy. Turkey's gross domestic product of €536 billion places it as the 17th-largest economy in the world out of 181 nations ranked by the International Monetary Fund. As a full member of the European Union (EU) it would represent about five percent of European output today and be tied with the Netherlands as the

sixth-largest member economy. The Organization for Economic Cooperation and Development (OECD) reports that Turkey's real GDP grew by 8.7 percent in 2010 and is forecast to grow by 6.7 percent per year on average from 2011 to 2017. It is expected to be the fastest-growing economy in the 34 OECD member countries. In "The World in 2050," PricewaterhouseCoopers forecast that the Turkish economy will grow at an average rate of 5.1 percent in U.S. dollar terms for an extended period.

About the Author



Marc A. Louargand, Ph.D., CRE®, FRICS, is an internationally known economist and investment expert and has been active in real estate and institutional investment for more than forty years. He is a principal at Saltash Partners LLC, a private equity investment firm he founded in 2007. Louargand was a co-founder of Cornerstone Real Estate Advisers where he was chief investment strategist until his retirement in 2007. In addition he was a professor of finance and economics at California State University at Northridge, University of Massachusetts and Massachusetts Institute of Technology. He has been editor or editorial board member of the Journal of Real Estate Portfolio Management, Journal of Real Estate Research, Journal of Real Estate Literature, Journal of Corporate Real Estate, Real Estate Issues and Briefings in Real Estate Finance (UK). Louargand is the past president of the American Real Estate Society and one of its Distinguished Fellows. He is also a Fellow of the Homer Hoyt Institute and the Royal Institution of Chartered Surveyors. He is a board or advisory board member of The Counselors of Real Estate®, The Counselors of Real Estate Foundation, the American Real Estate Society, the James R. Webb Foundation of ARES, the Angel Investor Forum of Connecticut, Doran Capital Partners (Korea) and Sustainable Real Estate Solutions, Inc. Louargand holds a master's degree in business administration and a doctorate degree from UCLA's Anderson School, and a bachelor of arts degree from the University of California at Santa Barbara.

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The Turkish economy is one of the most successful of the 20th century. While retaining part of its labor force in traditional agricultural roles, exports from the automotive and electronic industries now surpass Turkey's traditional textile exports. Full accession to the EU is still in question but may occur at some time in the coming years. Accession to the euro zone would likely increase tourism and trade significantly.

HALLMARKS OF A GROWING MODERN ECONOMY

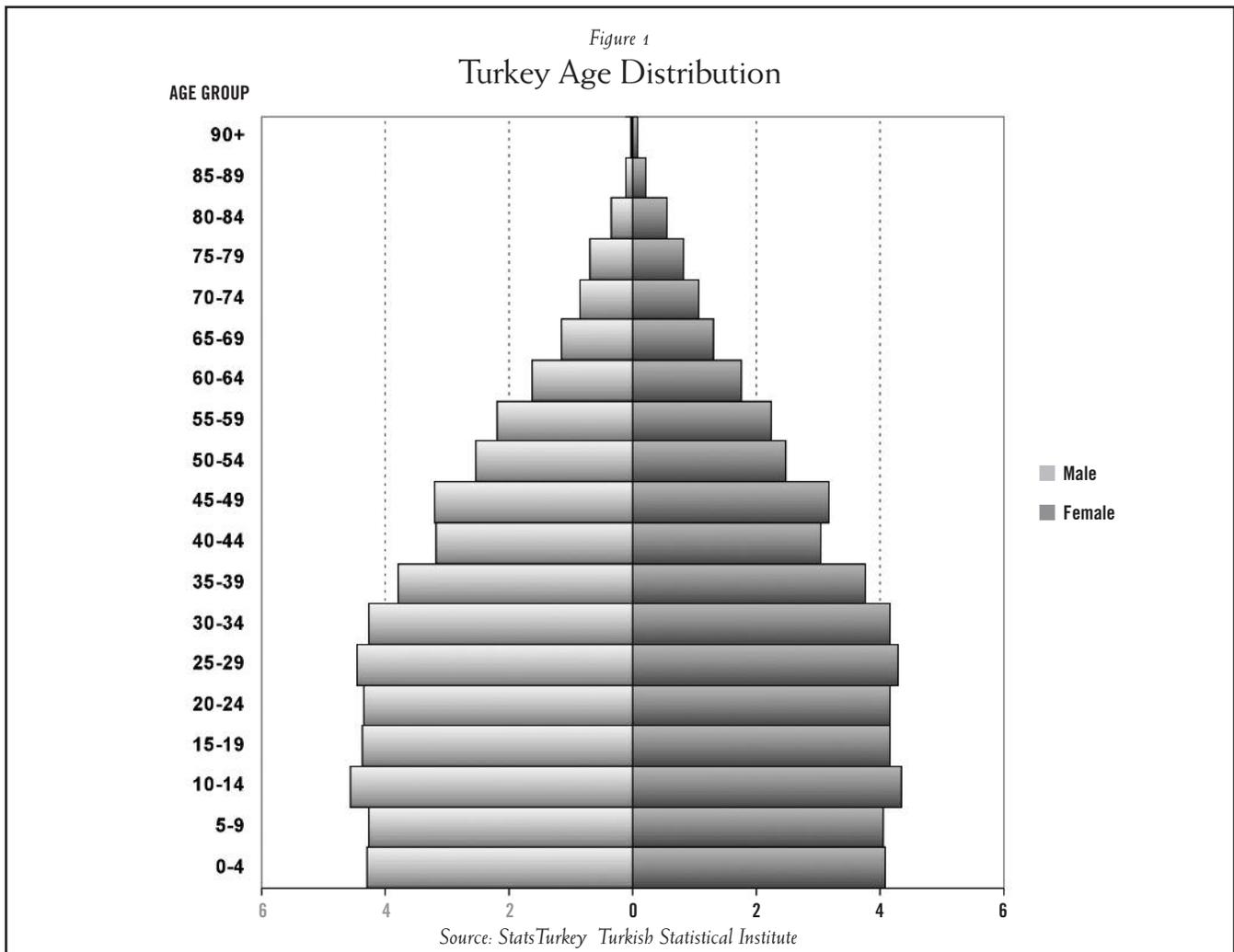
Rapid growth brings cultural and social change as well as economic. The rise of the mall in Turkey is both a function and a result of those changes. Changes include urbanization and suburbanization, female labor force entry, increased income, globalization of attitudes and tastes, homogenization of taste through television and Internet access, and shifting socialization to leisure time from the traditional workplace. The modern mall is a key element in these changes.

Suburbanization

Turkey has become an urbanized country much like the rest of the developed world. In 2010 the government estimated that more than 76 percent of the population lived in an urban setting (district and province centers). Urbanization has been rapid, as it was estimated at 40 percent in 1960. This urbanization has created cities with substantial suburban surrounds. Suburbanization led to increased automobile use and provided fertile ground for the development of the modern shopping mall.

Demographics

Turkey's population is young. Sixty-seven percent of the population is between 15 and 64 years of age and the median age is 29. More than 25 percent are below the age of 14 (see Figure 1).

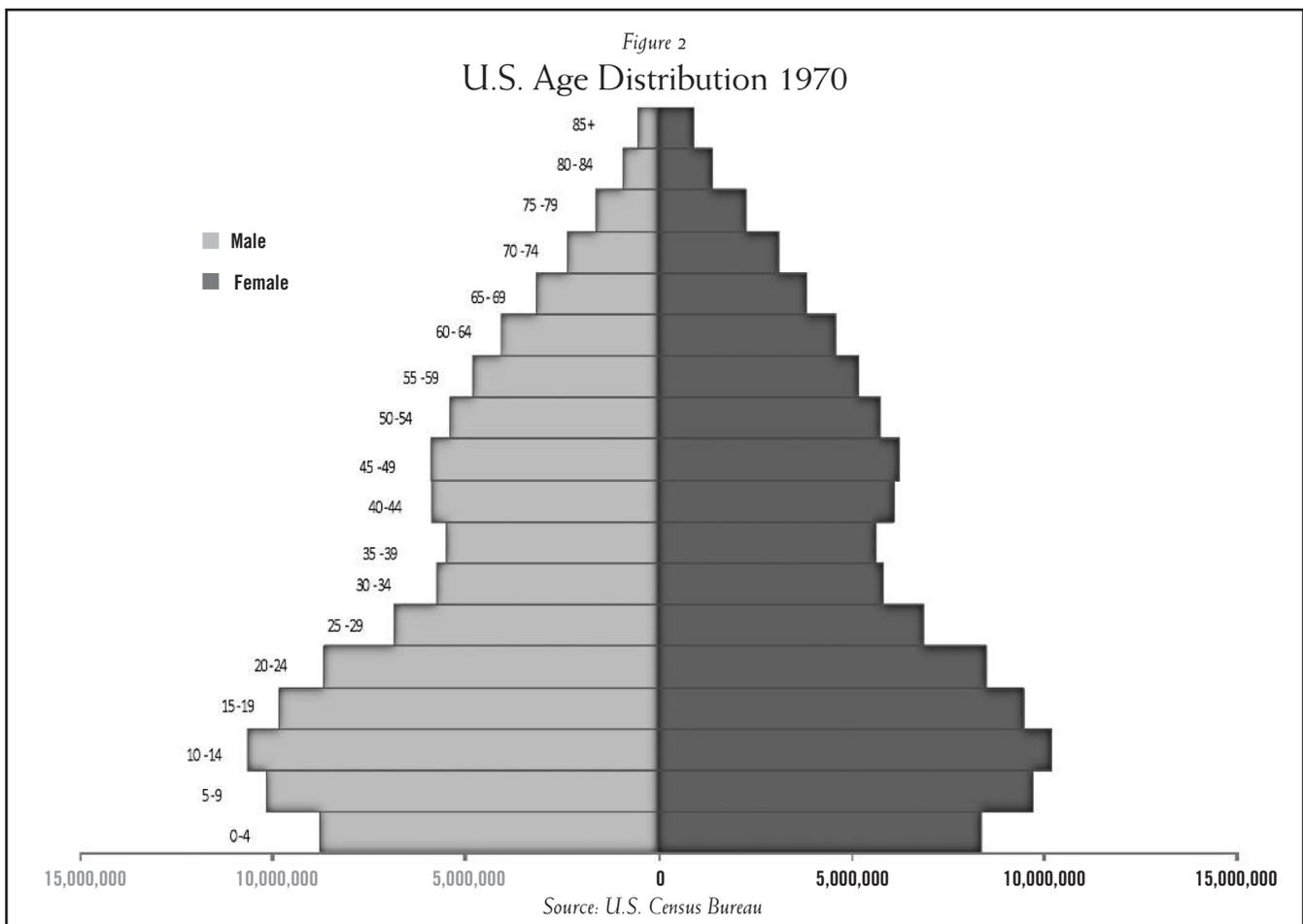


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Perhaps the best way to grasp the impact of the age distribution is to contemplate Figure 2, which shows the U.S. age distribution in 1970 when the bulk of the baby boomers were in their teens and twenties. One benefit of Turkey's youth is that it will have the world's second-fastest labor force growth rate in the next few decades, trailing only India. Additionally, the small ranks of the elderly means that Turkish workers will not have a large dependent population to support, so rising earnings will likely translate into rising retail sales. A third benefit of a youth-centric population is openness to change and new ideas, which will hasten the transition from traditional Middle Eastern retail models to modern western ones.

education have participation rates of 85 percent male and 72 percent female. This bodes well for labor force growth, considering the country's large youth cohort, growing population and increasing female education. Under these circumstances the labor force can grow significantly faster than the population, creating growth in prosperity. A food and beverage industry report by Deloitte for the prime ministry of Turkey observes:

Through the widespread presence of modern MGR [mass grocery retail] outlets and rising disposable incomes, consumption patterns have been shifting to packaged and processed foods, such as ready-to-eat meals and frozen foods. Additionally, the increases in the number of females in full-time employment have supported the



Female Labor Force Entry

Turkey's labor force comprises a wide range of skills and education. Those in the labor force who have less than a high school education have participation rates of 69 percent male and 23 percent female. Those with higher

trend towards packaged, frozen and ready food. Therefore, considering that Turkey still has the lowest per capita consumption of packaged food in Europe, there is considerable potential in the aforementioned sub-sectors.

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Conditions in the Bazaar

The traditional bazaar, while colorful, does not suit the modern lifestyle evolving in Turkey. Increasing independence of women is particularly at odds with tradition. The bazaar may be less attractive to women shoppers on grounds of efficiency, safety, cost and convenience in comparison to a modern enclosed mall. While the bazaar is an ancient and enduring tradition, modern retail is new to Turkey and appears to be gaining ground quickly in terms of shoppers' preference.

Efficiency of Traditional Retail

Retail in Turkey has traditionally been the province of the bazaar and the bakkal. Bakkal are generally small shops, often specializing in one or more products. In some respects they continue to serve some of the needs that a convenience store serves in the U.S. They may be open late and may be an integral part of a neighborhood. But like much traditional retail, they are not efficient and are unable to drive price and volume in the manner of modern retail. There are conflicting views in Turkey about the viability of the bazaar and the bakkal. It is likely that they will endure but retain an ever-smaller share of retail volume as more modern retail is developed and the population becomes more affluent. (Even in Singapore, which has the third-highest GDP per capita, there remain traditional retail venues despite the presence of massive amounts of modern retail.) Traditional retail outlets are often staffed only by family members. They typically buy in relatively small quantities and the pace of business may not be the equivalent of the modern shopping mall.

Modern Food Retailing

The grocery store and hypermarket were the first evidences of modern retail in Turkey and comprise about half of the stock of anchor tenants in malls. Major firms include domestic operators, joint ventures between Turkish and offshore firms, and foreign retailers who have acquired Turkish operators. The French retail giant Carrefour entered into a joint venture with Sabanci in 1996 creating Carrefour SA. In 2003, British retailer Tesco

acquired local firm Kipa to form Tesco Kipa. The largest operator is a Turkish firm established in the 1950s—Migros. Thus the grocery landscape is evolving into a pattern much like that of the U.S. with domestic and offshore ownership and with a bias toward traditional domestic branding.

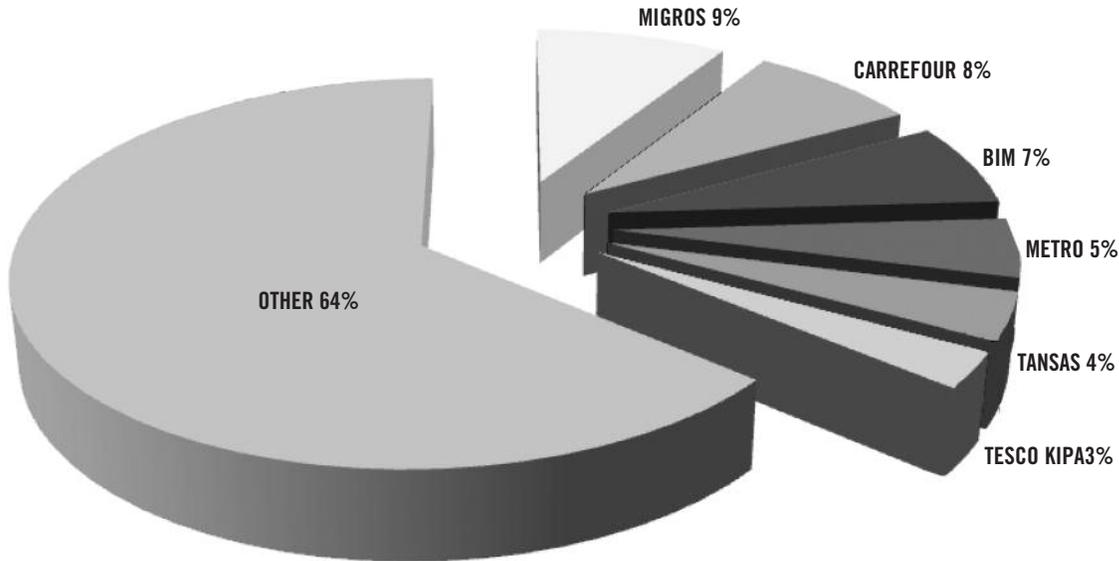
The McKinsey Global Institute published a study in 2003 that analyzed the barriers to modernization and productivity in Turkey's economy. The analysis included a focus on what are classified as fast-moving consumer goods (usually defined as consumer nondurables and semi-durables, i.e., the goods found in a hypermarket).

McKinsey's focus on retail included the opinion that: "When Turkish policymakers address the barriers to productivity central to the fast-moving consumer goods (FMCG) retail sector, they will be tackling the two most important factors affecting productivity in the economy overall and, potentially, they will be stimulating a ripple effect that should catalyze improvements in a broader slice of GDP. FMCG retail is a large and rapidly growing sector, with a pivotal role as the final link in a long value chain going back to agriculture."

In the eight years since, modern retail has taken a substantial leap forward. Food sales are generally estimated at 50 percent of total retail. The modern retail component of that has risen from 20 to 60 percent of sales since the 2003 McKinsey report. While growth has been rapid, there is still a substantial opportunity for extended growth from both market penetration and increasing affluence. Taken together, the major chain grocery retailers had a bit less than 40 percent market share at last measure. Migros, the largest, had a nine percent share in 2008 and others trailed that. Sixty-four percent of the mass grocery retail market is potentially available to modern tenants. During 2009, MGR consumption fell back a bit in response to the financial crisis, so these shares are probably close to the current status of the market, which rebounded in 2010 to previous levels, with substantial growth expected in 2011 and beyond.

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Figure 3
Mass Grocery Retail Market Share 2008



Source: Business Monitor International; Deloitte

Figure 4

Beymen Department Store Brands
(Sample)

Alexander Wang	Halston
Armani Collezioni	Jil Sander
Balenciaga	Jimmy Choo
Balmain	Marc Jacobs
Bottega Veneta	Michael Kors
Brooks Brothers	New Balance
Canali	Nike
Church's	Nina Ricci
Diane VonFurstenberg	Prada
Dior	Red Wing
Dolce & Gabbana	Stella McCartney
D-Squared	Timex
Ermenegildo Zegna	Tom Ford
Givenchy	Tory Burch
Gucci	Valentino

Source: Beymen Stores

Global Brand Awareness

While Turkey has successful homegrown retailers, global brands are a major factor in the marketplace. While a combination of some sort is a major theme in the food market, soft and hard goods with familiar names are widely seen. Figure 4 lists a sample of brands carried by Beymen Department Stores, a Turkish retailer of long

standing. The brands represent designers and manufacturers from Europe, North America and Asia. Turkey is estimated to have 25 million Internet users, a critical mass of eyes on the world that will serve to spread brand awareness and demand to its residents.

Changing Household Composition

The transition from an agricultural and nomadic economy in the past hundred years has changed the nature of the family in Turkey as it has in many societies. In an agricultural setting, children have positive economic value as they can work the fields. In an urban mixed economy, they are cost centers, requiring education, food, clothing and shelter. As educational levels rise they require these things for even longer periods of time. Throughout the world, economic emergence is accompanied by lower fertility rates and smaller household sizes. One beneficial result is that rising incomes are more available for discretionary consumption than would be the case with large families. Between 1978 and 1998, Turkish households changed dramatically. The extended family household shrank from 20 percent of households to 10 percent while nuclear family households rose from 62 percent to 72 percent, and single adult households rose from three to five percent of total households.

Turkey's urbanization is recent and modern, including modern-sized, multi-family residential units that also

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encourage smaller households. Since 1990, the divorce rate has tripled and since 2000, the rate of divorce in marriages of long duration has quadrupled according to Statistics Turkey. This appears to indicate that Turkish household characteristics are rapidly assuming western form, another sign that rising affluence is fueling the growth of smaller households. Despite these changes, Turkey still has relatively large household size compared to other emerged economies, and especially so relative to euro zone nations. Thus, it is reasonable to expect the Turkish household size to continue to shrink, creating increasing demand for retail services as the ratio of households to population rises.

Increased Educational Attainment

Turkey's youth are attending college in greater numbers. Recent estimates are that 13 percent of high school graduates attend college, on a par with Sweden, Norway, Mexico and Austria. These data do not include those who enroll in college some years later. By contrast, the U.S. enrolls 41 percent of its high school graduates in college. Greece has the highest attainment at 68 percent. Again, these disparities indicate that the in-place trend is likely to continue with ever-increasing numbers of young people attending college and expecting growing affluence in their adulthood.

Increasing Affluence

As industry and services have replaced agriculture as the dominant forces in the economy, incomes have grown substantially. At the same time, the level of sophistication in industry has risen, creating more affluence for a portion of the population. As GDP per capita has reached double digits (approximately €10,250 on a purchasing power parity basis) the potential consumption mix has changed beyond subsistence goods to include western style goods. Turkey's GDP per capita has doubled in the past decade, growing at an average rate of 7.6 percent per year according to the CIA's *The World Factbook*. The Economist Intelligence Unit forecasts private consumption to grow at more than five percent per year through 2015. Consider that there is likely to be a continuing shift away from traditional retail during that time so that the growth in mall spending could be significantly higher than five percent per year.

New Patterns of Socializing

A big part of the mall's attraction is its use as a venue for socialization by the young. In "the rise of the shopping mall in Turkey: the use and appeal of a mall in Ankara,"

Professor Feyzan Erkip of Bilkent University in Ankara sampled shoppers over time at the Bilkent mall. The responses broke into patterns that would be very consistent with a similar study at a U.S. mall. Young people often came to the mall without shopping as did a smaller share of more mature people. The young saw crowded conditions as positive, indicating that they were there for socializing. Women felt more comfortable in the mall setting. Erkip writes: "Turkish people are looking for a new modernity in these global spaces through consumption and leisure patterns provided by a more 'civilized' space than the existing urban center and the street." A motivational survey had several overwhelmingly positive responses, including: "Shopping is convenient;" "It's a beautiful place;" "Like activities other than shopping;" "Came here for browsing;" "This place is secure;" and "Feel comfortable here." These responses reinforce the attractiveness of the mall relative to the traditional bazaar.

Density and Spread of Malls

PricewaterhouseCoopers (PwC) released "Glimmering Star – Impact of Retail Sector on Turkish Economy" in September 2010, estimating that the retail sector will grow to 304 malls totaling eight million square meters by the end of 2011. While the sector has shown very rapid growth, it has barely penetrated the market, especially outside of Istanbul. PwC's estimate translates to approximately 115 square meters of modern retail per 1,000 persons. The current density estimates range from between 200 square meters per 1,000 in the Istanbul market to less than 100 square meters per thousand in other parts of the country, according to Jones Lang LaSalle. By contrast, the International Council of Shopping Centers estimates that there are in excess of 660 million square meters of shopping centers in the U.S. which represent 47 percent of total retail space. That translates to approximately 2,100 square meters of shopping center space and 4,500 square meters of all retail per 1,000 people in the U.S. While one might argue that the U.S. has more than enough retail and that these data include a significant amount of obsolescent or redundant retail, it seems clear that Turkey's rapidly growing and modernizing populations can support substantially more than the current stock of modern retail space.

Mall Investment

Transactions data from Real Capital Analytics show that Turkey is developing as an investment market as well. Retail mall transactions since 2005 have included buyers Merrill Lynch JV Krea Real Estate, VastNed Retail NV

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(Netherlands), Citi Property Investors, Corio NV (Netherlands), LaSalle, and Commerz Grundbesitz Investmentgesellschaft (Germany), as well as entities domiciled in Turkey. Other property type purchasers have included Apollo and Blackstone. A sample of those properties most consistent with modern mall characteristics shows sale prices averaging €1,973 per square meter. These transactions were reported to have cap rates averaging 8.2 percent in a tight range from 7.8 to 9.0 percent. While not as deep as markets in the euro zone, the institutional property market in Turkey appears to be well on its way to robust development. Turkey has enjoyed foreign direct investment in excess of €60 billion in the past five years according to the United Nations. Both Goldman Sachs and Jones Lang LaSalle have published reports in 2010 indicating that they expect Turkey to be upgraded from its current rating of BB+ (Fitch) to BBB, which would make it investment grade and significantly increase its attractiveness for foreign direct investment. Should that occur, Turkish real estate would very likely be a focus of foreign investors.

CONCLUSION

At a time when the U.S. property market is facing a tough two or three years of recovery, Turkish retail may offer an attractive diversification opportunity for portfolios of high net worth and institutional investors. Turkey is forecast to have stronger economic growth, faster labor

force growth, shrinking household size, greater affluence and increasingly western tastes. The nascent level of the shopping mall promises significant market penetration opportunities for retailers and retail developers, with much less intense competition than what might be found in the U.S. or other venues. ■

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