Best practices in site selection

An introduction for real estate decision makers

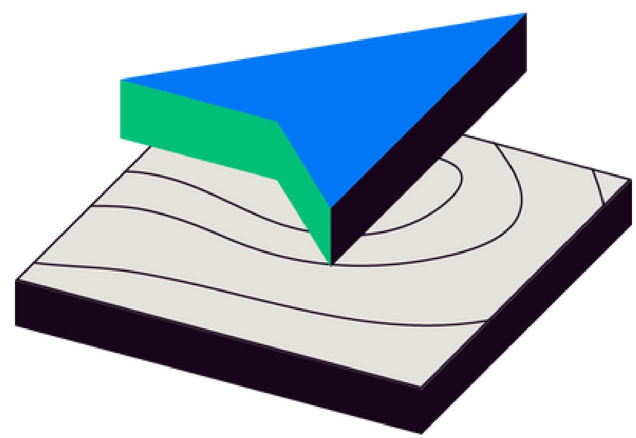
Kalibrate

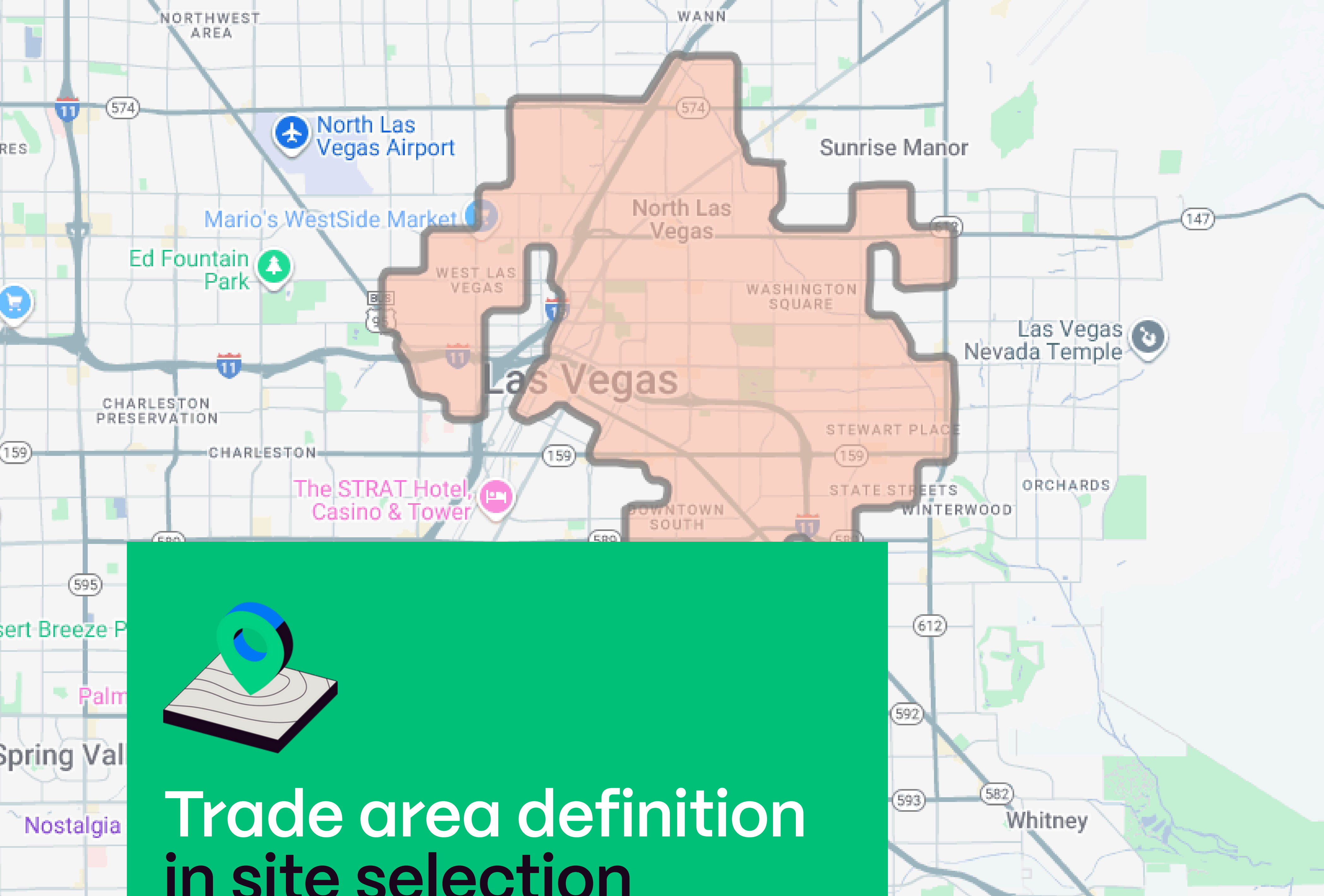
Introduction

Site selection is a skill real estate professionals perfect over the course of their careers.

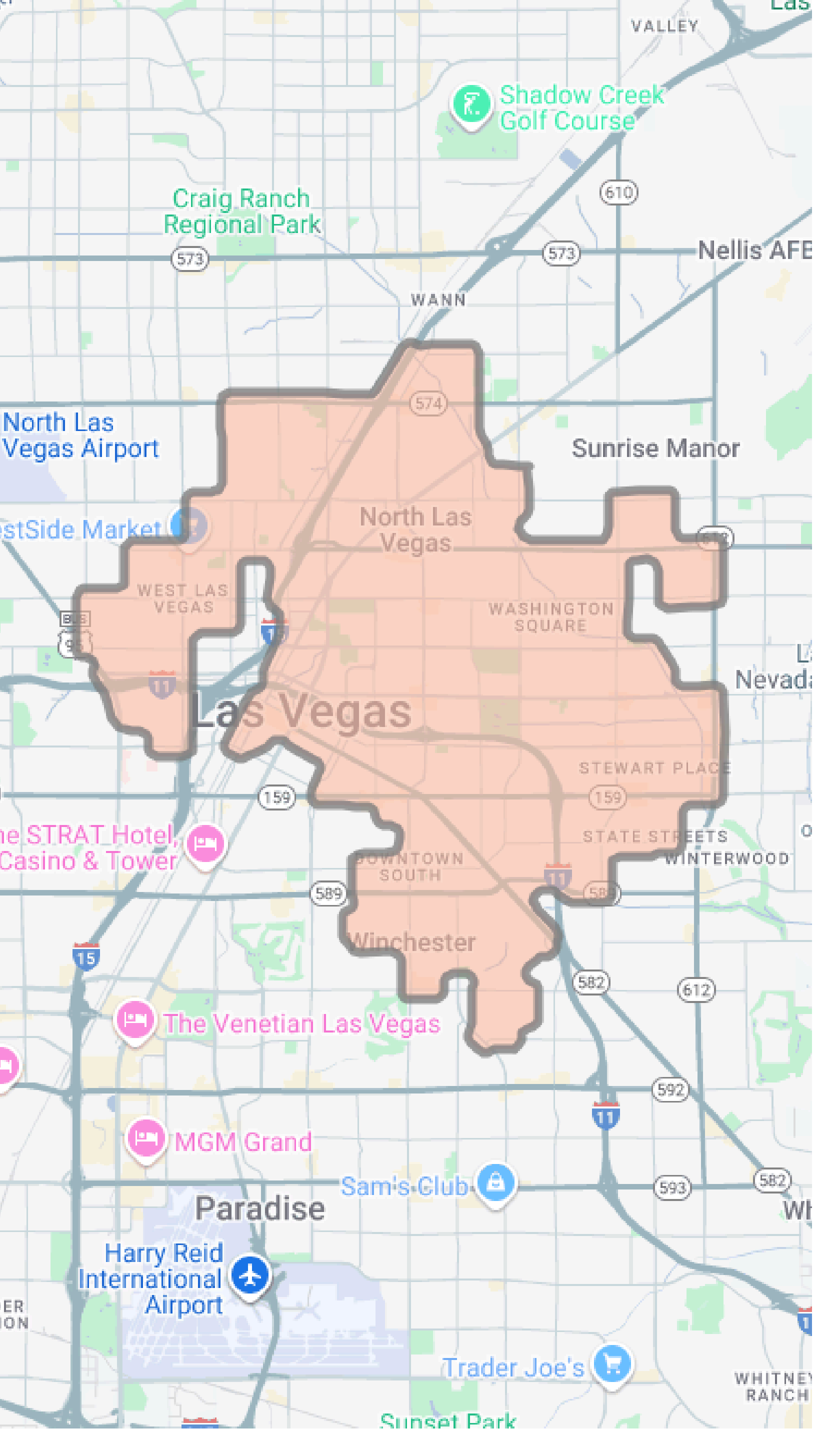
Through our experience working with leading multi-unit brands, we have identified best practice approaches to data and insight that deliver the greatest levels of certainty when creating a location strategy.

The principles covered in this report focus on the importance of accurately defining trade areas, how site and situational characteristics should be considered, and methods for quantifying competitive impacts, to remove the guesswork from the site selection process





Trade area definition in site selection



The importance of trade area definition

What is a trade area and why are they so important to site selection decisions?

A trade area in its simplest definition is the geographic area from which the vast majority of revenue (or customers) originates. It is not at all unusual for retailers, restaurants, and healthcare providers to serve multiple disparate trade areas depending on the trip origin or destination associated with each customer.

For example, most trade areas associated with retailers are residence-centric; that is, most retail shopping trips originate from each customer's place of residence. Conversely, restaurants almost always serve multiple trade areas which typically reflect not only customers residing in the vicinity of a restaurant, but also customers working or shopping near the restaurant.

What factors define trade areas?

The trade area definition hierarchy of sophistication:

BEST

Uniquely modeled and defined trade areas for an individual location

BETTER

Concentric **drive-time ring(s)** around the location

GOOD

Concentric **mile ring(s)** around the location

It is important to not rely on generalizations to approximate a trade area.

Retailers should consider numerous factors such as drive-time, the presence or absence of other units in the same brand, and urbanicity.

They should also look at barriers that would impede access to a location — natural barriers like rivers or lakes, or non-natural barriers like a major highway.

Ultimately, the significance of these factors is implicit in the actual sales or customer distributions associated with each location.

Based on rigorous analysis of individual existing locations, we can quantify the extent to which each of these factors "matter".

If you have a location that is situated in a suburban area on the periphery of a major metro area, we'll very often see the sales density (and trade area) for that location extend 20–30 minutes into the country, but only 10 minutes back into the city. That's difficult to account for with concentric ring methodologies, and a big part of why retailers should follow the data and take the more rigorous approach.

How are trade areas used in practice?

Trade definition is a vital step when generating a forecast for any location.

It is critical to understand that not all consumers patronize a brand in the same way. Consumers who reside or work locally are those that have a convenient opportunity to utilize a brand's services. Their convenience-driven visits are foundational to customer profiling, predicting future sales, and estimating cannibalization, and it is these consumers upon which trade area extents should be based.

Consumers coming from some larger distance — travelers from out of town, visitors to a nearby attraction — defy those patterns of convenience.

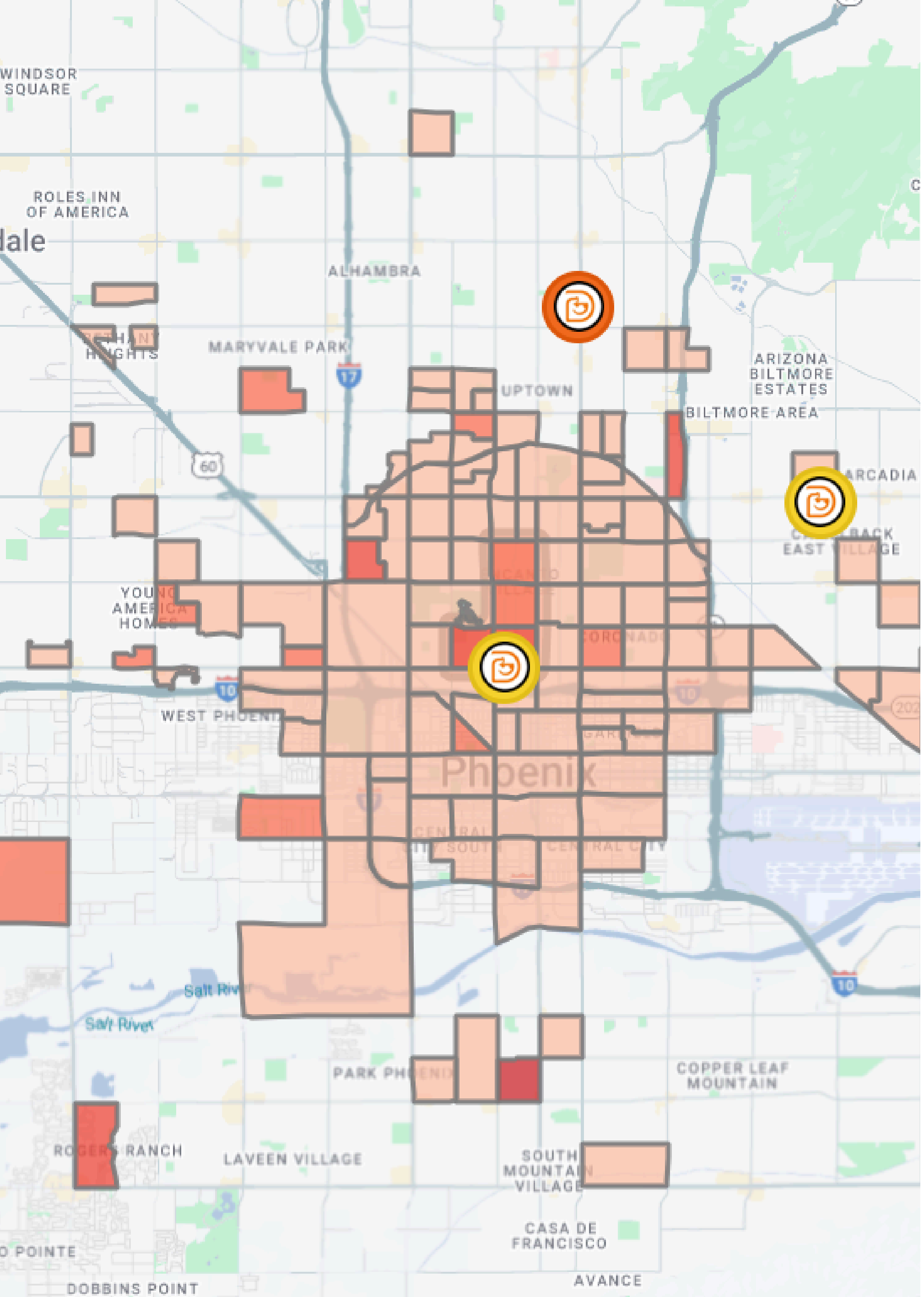
So, the trade area can be used as a “line of demarcation” to isolate individuals that patronize a location based on convenience versus those that had something else draw them to the area.

Another practical benefit of accurately defined trade areas for existing units is that it provides an easy-to-use visual tool that market planners can use to identify infill opportunities and to visually approximate the impact from new unit openings.

Understanding the trade area extents of existing units and how they vary by market size, urbanicity, location type (mall/off-mall), prototype, etc. provides a means by which one can estimate the trade area extent(s) of future locations. Having defined trade areas for an existing database of units, one of the first models we develop is a model that accurately predicts these known trade areas' extents.

Knowing that we can accurately model the extents of existing trade areas provides us confidence that we can accurately predict what the trade areas for future units will be.

Why accurately defining trade areas matters



An over-defined or under-defined trade area means you are not accurately capturing a location's potential.

The gold standard approach considers both the characteristics of the location and the characteristics of surrounding neighborhoods when estimating trade area extent because this is likely to provide the most accurate results.

However, flexibility is important here — there are always going to be unique situations when applying a model, and being able to adjust on the fly for local market conditions is part of how we've built our forecasting platform.

And with mobility data, it's possible to study the sales distributions and trade areas for competitors or shopping centers near a unit under consideration to serve as a point of validation against the trade area you define.

Site and situational characteristics in site selection

The importance of site and situational characteristics

How do the physical characteristics associated with a location influence underlying demand?

There are three primary considerations in assessing the viability of proposed locations regardless of the industry evaluated: the underlying demand for the product or service, the existing supply of competitive operators who are serving that demand, and the quality of the specific site location. Site characteristics refer to the last of these considerations.

In addition to the physical attributes of a site, its situation or positioning vis a vis complimentary retailers/restaurants/service providers, other traffic generators, and pockets of potential customers should be considered.

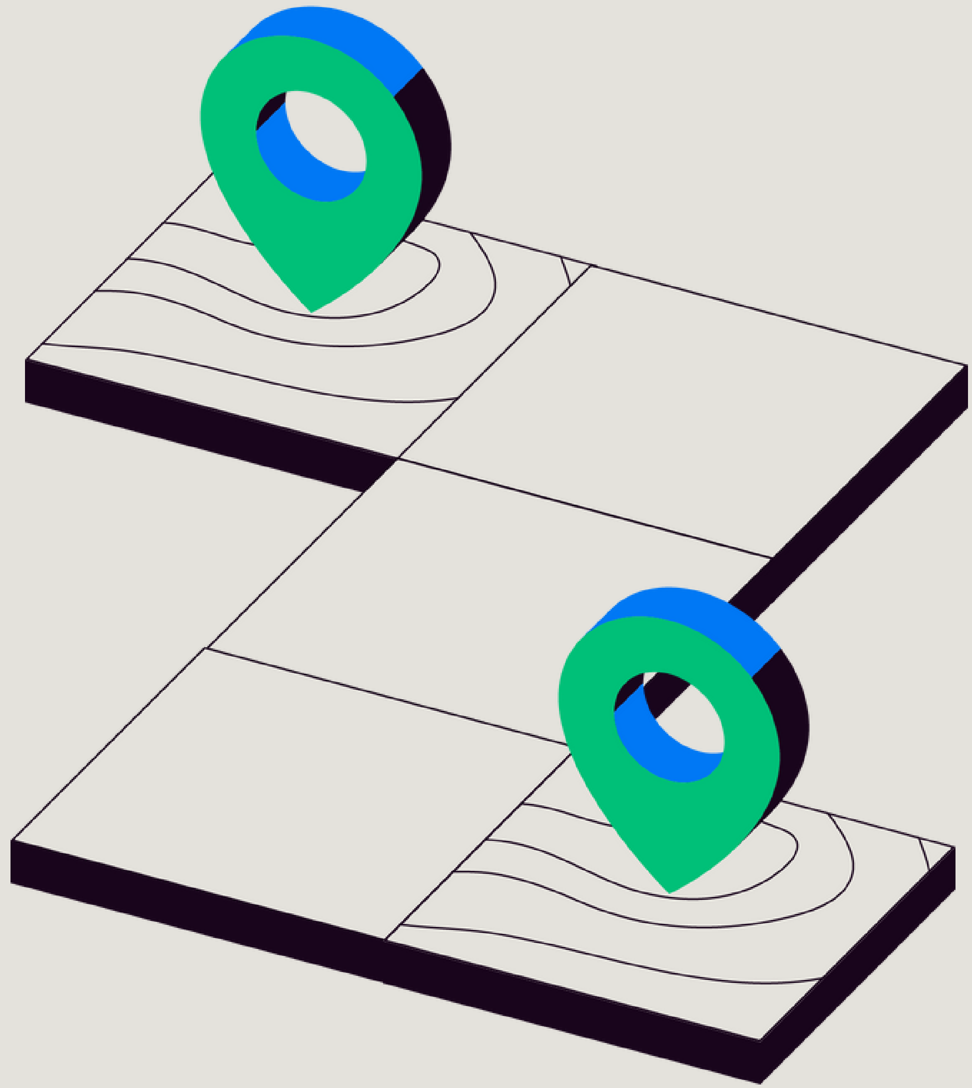
These are commonly referred to as situational characteristics and include factors such as co-tenancy, proximity to regional hubs, access to Interstates and highways, proximity to worker and "daytime" population concentrations, traffic counts/flow, and the "going home versus going to work" side of the road.

The importance of co-tenancy

Co-tenants are among the most important situational characteristics

Generally, retailers should seek locations in a retail node that attracts "like" types of consumers, thereby enabling your site to capitalize on the synergy created by other proximate retailers.

The same would be true of restaurants. High-end, white tablecloth restaurants will typically avoid a development that is anchored by a discount retailer or whose food service tenants are predominantly QSR-centric.



How importance varies by operator

The weight decision makers should place on site and situational characteristics depends on concept.

For some operators such as gas stations, quick-service restaurants (QSRs), coffee shops, and convenience stores, site and situational characteristics are very important.

For example, with fuel and convenience retailers, the corner on which they are positioned makes a significant difference for the consumer.

As a rule, the more frequently you patronize the operator, the more important site characteristics are.

Conversely, if a retailer is a destination retailer such as IKEA, Costco, or Sam's Club, the fact that it might take consumers an extra 30 seconds to cut across traffic to get into their parking lot is not that big of a deal.

Proximity to regional accessibility rather than what corner they are located on is far more important for more destination-oriented concepts.

For healthcare providers, characteristics can matter even less. Admittedly, a good site can help accelerate the acceptance of a greenfield health care practice in a new market. However, for an established practice, the characteristics associated with the office location are negligible.

While the site and situational characteristics generally matter most for convenience-based retailers, they do matter for all brick-and-mortar locations, even some destination-oriented retailers — it's just a matter of degree.

Occasionally, site characteristics don't seem to matter much at all due to a unique and strongly destination-oriented concept. Such retailers can take significantly compromised locations such as sites in predominantly industrial areas.

However, the moment a competitor "clones" the concept, site characteristics suddenly start to matter a lot. If these competitors deploy in areas with a more desirable location, site and situational characteristics became a much more significant consideration concerning the selection of future sites

How site and situational characteristics support effective forecasting modeling

Like trade areas, site and situational characteristics are critical to understanding a location's potential.

You cannot accurately evaluate the revenue potential of a prospective site without incorporating the influence of its site and situational characteristics. Just like you can't evaluate the validity of a site without understanding the demographic make-up of the trade area or the intensity of competition.

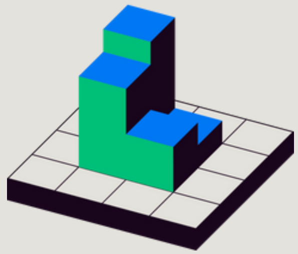
This is what makes predictive analytics truly a challenge — how to simultaneously consider interdependent factors which collectively contribute to the site's ultimate performance.

The following factors are vital for most clients we serve:

What is the geographic extent of the trade area each site will serve and what is the revenue potential implicit in the composition of trade area consumers?

What is the quality of the site and situational characteristics unique to each location under consideration and does it inhibit or enable me to capture my fair share of those dollars?

How intense is the competitive environment, and how are these competitors distributed throughout the trade area?



KEY INSIGHT

Failing to account for the impact characteristics have on projected performance, because they are difficult to quantify, is not an option.

Ignoring site characteristics brings risk

Gathering site and situational characteristics is challenging, but it should never be ignored

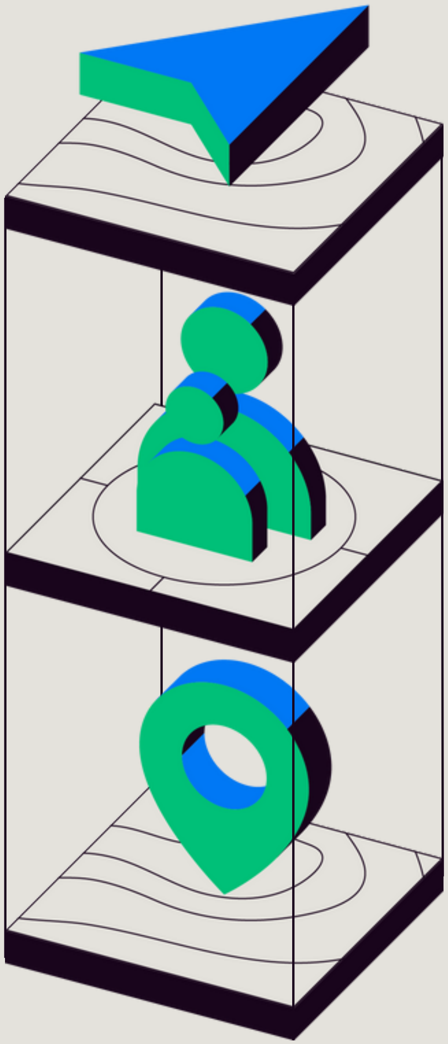
While many datasets are available at the census block group or consumer household level, there is no third-party compiler of site characteristics for individual tenants that can be licensed — the data must be collected.

Site characteristics also include a mix of objective ("what is the speed limit in front of the store") and subjective ("how visible is the store to passing motorists") data. Due to these difficulties, some analytics companies ignore their influence when developing models.

The inherent difficulties associated with collecting site characteristics data are irrelevant. If site characteristics have an impact on unit performance, they need to be considered.

Anyone who has ever been involved in the site selection process intuitively recognizes how strongly site and situational characteristics can influence unit performance, regardless of the sales potential and competitive environment inherent in the site's trade area.

Competitor impacts in site selection



How does competition influence forecasting model development?

Kalibrate’s forecasting models are trusted by some of the most sophisticated real estate teams in the world. Here’s our take.

Most operators have a pretty good handle on who their primary competitors are, or at least have a good hypothesis of the brand(s) that they directly compete with. Our goal is to first align on the consideration set that will be evaluated from a competitive standpoint.

The objective, outsider's perspective that we bring to this process enables us to make recommendations regarding specific operators for inclusion in the analysis that our client might never have otherwise considered.

We then work through our analyses to establish which of these competing brands ultimately impact their bottom line, proving or disproving their pre-existing hypothesis regarding perceived competitive operators.

Beyond the core trade area

The next element of our approach focuses on the larger trade area that our clients and their competitors serve.

We first seek to define whether specific competitors are what we classify as "impacting", an example is that both you and your competitor(s) are located 5 minutes away from the consumers that both have the opportunity to serve in different parts of the trade area. There is no locational convenience for the consumer in an impacting scenario.

We then work to determine whether any competitor(s) are considered to be "intercepting". A great example of this is when the consumer has to drive past a competitor to reach your front door.

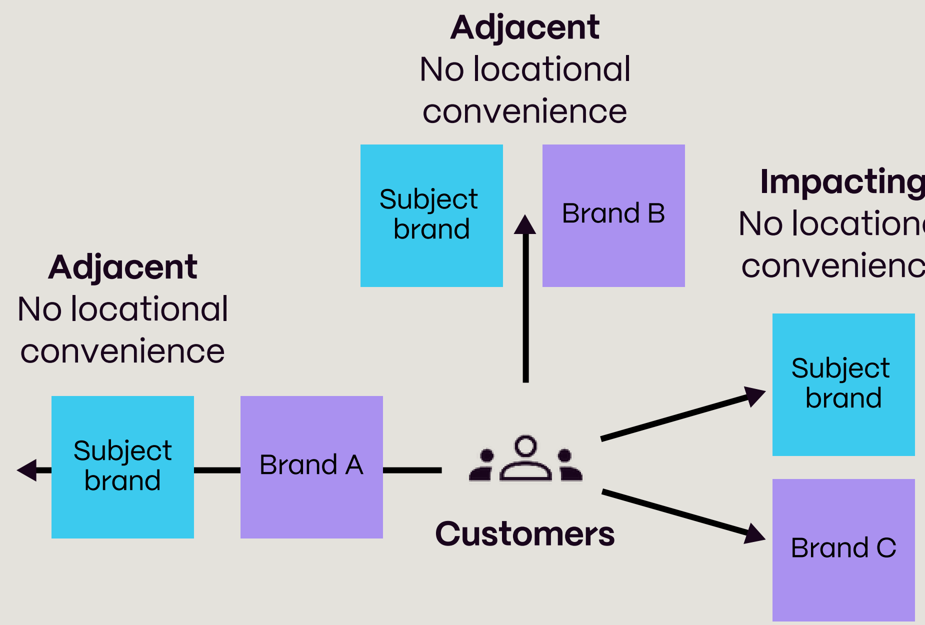
When explaining the importance and relevance of various competitors to our clients, we explain that "we look at the world through the lens of the consumer, and in doing so work to account for the competitive influence experienced by consumers rather than focusing on the perceived impact to your stores."

It is quite common for real estate teams to lose sight of the fact that the competitive environment can vary significantly within a given trade area, depending on where you are positioned directionally. That is a paramount concern that we have to control for in our modeling.

Operators tend to think in terms of "who's right next to me?" or "how many competitors are within five miles or 10 minutes", when, in reality, your competition could be positioned to the east of your location and the consumer base is located to the west of you.

Our approach is to take into account where customers are coming from relative to where the competition is. Locational convenience is key!

One additional element worth calling out regarding competition — the more analogous a competitor's offering is to yours, the more competitive they are likely to be with you. What clients often overlook is that there is perhaps no greater competitor than another of their existing locations, what we refer to as "sister" locations.



How does regionality impact competitor selection?

Competitor brands may have differing impacts on performance in different markets. We call this regionality.

Generally speaking, retailers with a national presence have greater brand equity and thus are more competitive as a whole, but ignoring performance variances between both geographic regions and markets can lead to site forecasts that overstate or understate the potential of a proposed location.

A great example of a regional competitor is Fuzzy's Tacos, based in Dallas Fort Worth, like one our our US offices. They are a strong competitor throughout Texas in the fast-casual sector but are not as competitive in the Southeast.

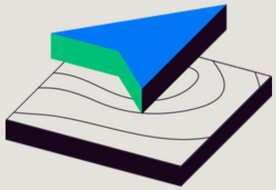
Are there varying degrees of competitors?

A major challenge in many operators is isolating the impact of an individual brand as a competitor.

Using the QSR space as an example — there is no way to know the real impact of McDonald's on Chick-Fil-A on a national scale because there is such significant variance on a market-by-market basis, not to mention the interplay of all other QSRs within a given market (some of whom are national in scale while others are local/regional operators). Each competitive situation is unique.

Therefore, a statistical correlation in the analysis is used to ensure that we are directionally accounting for the impact of competition.

When looking across the entire network of a client's locations, our goal is to help clients understand the degree to which any competitive scenario appears to be favorable or unfavorable to their performance.



KEY INSIGHT

When clients realize why adjacent competition often aligns with higher sales, we know they are in the proper analytical mindset for site forecasting.

Don’t make assumptions about your competition.

Sometimes where the competition is located is more important than who the competitor is.

It is also worth noting that when we are quantifying the factors that impact performance as part of our larger modeling effort, competition alone is not the sole factor that causes individual locations to perform poorly.

Most operators come into a modeling exercise with the expectation that measuring competition is a straightforward, black-and-white proposition.

While Kalibrate provide our clients with meaningful insights through our work, an equally important outcome from our work is when clients gain an appreciation for the complexities involved in determining how best to account for competition during a site evaluation.

When clients realize why adjacent competition often aligns with higher store sales performance, we know they are in the proper analytical mindset for site forecasting.

What about complementary competition?

Some competition actually helps your sales potential – but it trends higher in certain situations.

It's the clustering effect, or what we refer to as "complementary competition".

For example, consumers often like to visit numerous retailers when shopping for apparel, and therefore might prefer to go to lifestyle centers and super-regional malls where concentrations of clothing stores exist.

The gravitational pull for consumers is greater when numerous choices for a similar offering exist in proximate fashion to one another.

This phenomenon exists in numerous sectors — from "restaurant rows" and competing car manufacturers that position dealerships near one another to healthcare providers that co-exist in medical office buildings (MOBs) and larger healthcare districts.

Any other impacts to consider?

Some sectors should look at market-level saturation to inform their strategy.

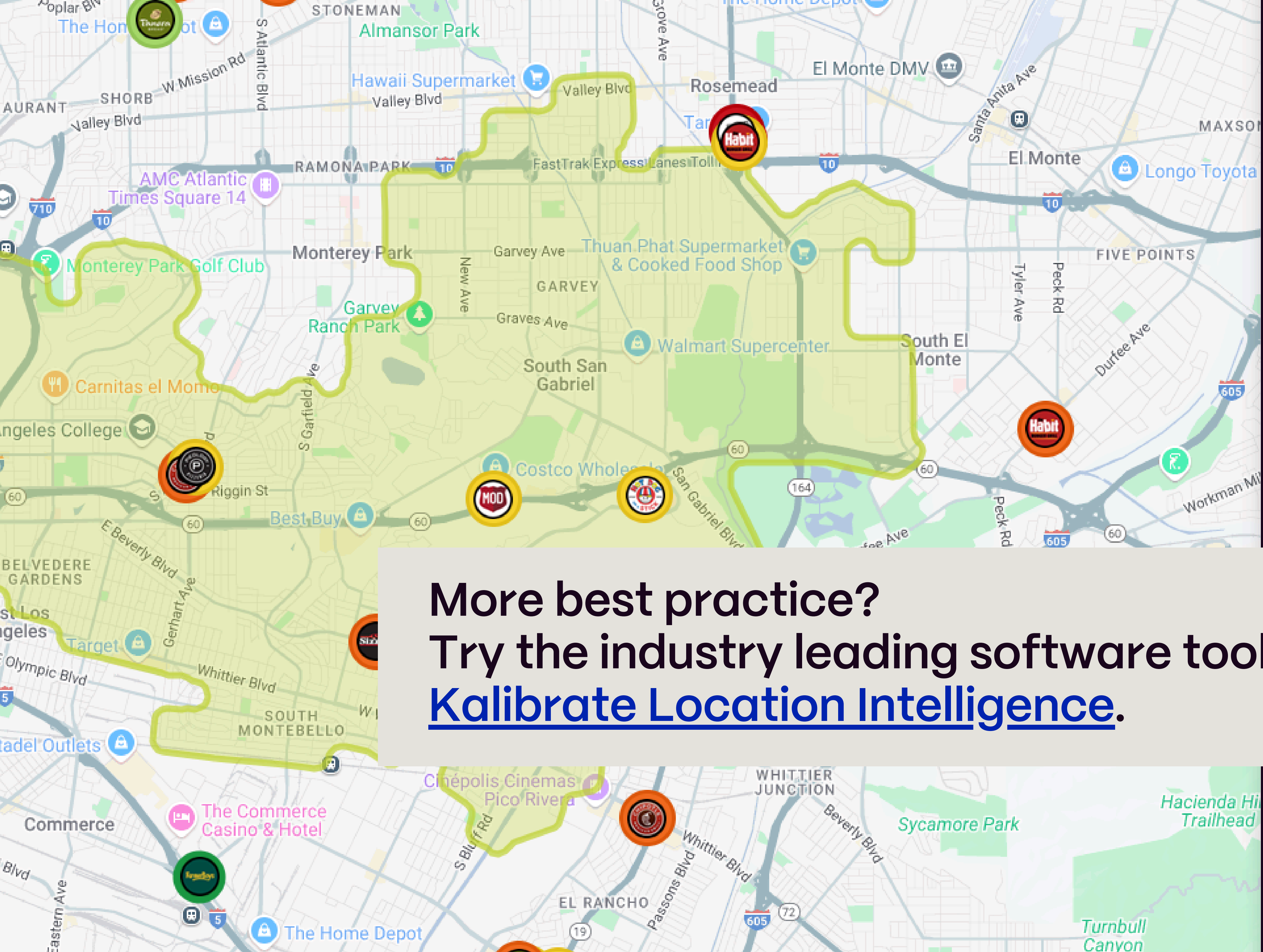
Simply put, market-level saturation consists of dividing total households by store count as a surrogate to gauge brand strength in a market.

A great example of the power of market-level saturation is Whataburger — both in their home market of San Antonio and throughout their home state of TX.

While McDonald's has 16x the number of locations nationally, Whataburger's market saturation exceeds that of McDonald's in the Corpus Christi market.

When comparing Whataburger's market saturation to the likes of Burger King (8x greater locations than Whataburger nationally) and Wendy's (~7x greater locations than Whataburger nationally), Whataburger's physical footprint exceeds these much larger operators in nearly every "home" market.

	Households per unit			
	Whataburger	McDonald's	Burger King	Wendy's
Dallas-Fort Worth	16,700	9,400	23,900	23,800
Houston	17,400	8,400	15,700	23,900
San Antonio	12,900	8,500	17,500	25,100
Harlingen-Brownsville	9,200	7,600	12,400	49,500
Austin	21,300	12,400	35,200	28,900
Corpus Christi	5,600	7,300	18,200	43,800
Tyler Longview	8,800	7,500	17,200	41,700



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Kalibrate

Kalibrate is a global location intelligence firm that specializes in supporting clients seeking actionable insights into questions relating to place, price, and promotion.

The company's customized analytics solutions consist of leading software platforms, consulting services, and proprietary datasets.

Headquartered in Manchester UK, Kalibrate actively serves companies across industries in over 70 countries through office locations in the USA, Canada, Japan, India, and Australia.

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