Retail Market Commentary

1.1. Headlines

- **Economic impact:** In September, the Bank of England said that it expected CPI to exceed 4% by the end of the year and admitted the economy is not growing as fast as it had expected but is still expected to register strong GDP growth this year of 6.6% after a 9.9% contraction in 2020.
- **Consumer spending:** Consumer spending is expected to be the main driver of this year's economic rebound. The release of pent-up demand and the rapid vaccine rollout is forecast to drive the strongest growth in spending since 1988.
- **Occupational market:** the retail occupational market has stabilised. The grocery, homeware, value, Bulky Goods and DIY sectors have outperformed other segments over the previous 12 months, driven by growth in online sales during enforced lockdowns.
- **Investment market:** There is a recovery in investment activity linked to occupational resilience. There is strong demand for food stores and retail warehouses with a value/convenience offer or strong alternative use potential. Shopping centres volumes have rebounded and exceeded the total amount of stock traded in 2020 with £850m havingxx transacted by Q3 2021.
- **Lending market:** There is increased availability of debt in the market to underwrite out of town retail assets, with strong fundamentals and food stores. Loan to Value covenants are still at a conservation 50% - 55%. Many banks have expanded their restructuring teams and we envisage an increase in distressed retail sales in 2021, particularly in the shopping centre market as in the case of NatWest's Project Mercatus.

1.2. Economic Impact

- **Promising GDP growth predicted for Q3:** Gross Domestic Product (GDP) grew by 4.8% in Q2, after falling by -1.6% in Q1. This left the economy 4.4% smaller than it was pre-Covid. However, GDP figures for July disappointed expectations, with the economy growing by just 0.1% over the month. Survey data points to underlying demand remaining strong, with recent forecasts predicting Q3 GDP coming in around 2.2%, which remains strong by historical standards.
- **Business Surveys indicate strong bounce-back:** The latest CIPS/Markit PMIs indicate the economy has seen a strong pick-up in activity since last year. June's composite PMI of 64.2 saw a rebound after dropping to 4.06 in January 2020. However, this was revised down to 54.8 in August 2021, signaling a slower speed of recovery across the private sector economy.
- **Inflation rises:** The consumer prices index rose by 3% in the 12 months to August 2021, up from 2.1% in the 12 months to July. However, the recent increase in demand for energy, labor and transport, coupled with a restricted supply chain, has led economists to believe that central banks will raise interest rates if inflation continues to rise.
- **UK Government announces funding for UK High Streets:** The government has unveiled a Future High Street Fund of up to £830m which will be invested in 72 areas across England. The aim is to transform high streets into vibrant hubs for future generations and to protect and create thousands of jobs, as well as helping areas to recover from the pandemic while also driving long term growth.

1.3. General Retail Overview

- **ESG has become the top priority for banking and investor clients alike:** It is anticipated that changes will be made to the EPC framework on which much of the UK legislation relating to sustainability is based upon. The next major MEES milestone is in 2027, where the minimum standard will be raised to a C from F&G and again in 2030 from C to B.

- **Rent collections statistics:** Data from REMark (which covers around 125,000 leases and £2.3 billion of rent and £364 million in service charge) for the September quarter showed that the overall average rent collection increased to 57.4%, the highest rent collection rate on due date in the past 18 months.

- **Footfall:** The latest Springboard UK footfall tracker show High Street and Shopping Centre footfall still materially lower than pre pandemic levels compared to retail parks which are close to or have exceeded 2019 levels in many cases:

	All Retail	High Street	Shopping Centres	Retail Parks
Week on week	-4.2%	-2.2%	-7.7%	-4.7%
2021 vs 2020	+14.6%	+20.7%	+10.8%	+5.7%
2021 vs 2019	-17.3%	-20.4%	-23.5%	-4.0%

- **Retail category performance:** Underperforming categories include fast fashion, food & beverage, travel and leisure. More resilient categories include discounters, DIY, sports, health & beauty, homeware, children's wear and supermarkets. Those businesses with a strong online platform and resilient supply chain have outperformed as well as those to have benefitted from 'essential' status.

- **UK moratorium on evictions:** The UK Government has confirmed an additional 9 month extension to the moratorium on evictions, until 25 March 2022. Fears that rent collection rates would suffer because of this further delay appear to have been overblown as rent collection rates improved at the June quarter.

- **Business Rates review:** The Government has confirmed that the final report of the fundamental review of business rates will now be published in Autumn 2021, when it is hoped there will be more economic certainty.

- **Business Rates holidays ends in England:** Businesses in England will start to pay a reduced business rates bill now that the tax break has ended. The UK government applied a full discount for firms from 1st April to 30th June, with a 66% discount rate after that date, meaning bills will now start to be paid again.

- **Current leasing trends:** the JLL retail agency team continue to agree new lettings, demonstrating that there is tenant demand for the better schemes. We are seeking an increasing number of tenants seeking to switch to a turnover based leases structure, although mid-market fashion operators are driving adoption and we are seeking much less of a change for retail parks.

1.4.2 Retail Warehouses

- **Size of the market:** According to Trevor Wood Associates the UK retail warehouse market reached 196m sqft in 2020, across 953 retail parks and 123 shopping parks. The retail warehouse vacancy rate rose to 8.4% at the end of Q2 2021, reflecting a small increase from 8.2% in December 2020. This compares to the 10 year average of 7.4%.

- **Demand from acquisitive retailers:** The JLL Retail Agency team have tracked current requirements for new stores totaling some 5m sqft which would take the vacancy rate well below the 10 year average, if translated into net absorption.

- **New supply is constrained:** On average less than 2m sqft of new stock has been developed and added to the market over the last ten years and this figure is lower over the last three years which has created the conditions for a more balanced supply demand dynamic as some stock is repurposed.
- **Retail parks are fundamentally more convenient:** Retail parks typically benefit from accessible locations, free parking, large stores with greater choice for consumers and more recently a perceived safer environment to shop. Those retail parks with a higher proportion of 'essential retailers' have also benefitted from higher footfall during the pandemic.
- **Rent collections statistics:** Retail rent collection stats for September 2021 averaged around 60.0% according to Remit Consulting, which is the highest level since March 2020. Retail parks have typically benefitted from a higher proportion of 'essential retailers' and have seen higher collection rates as a result with some investors reporting upwards of 80% during the pandemic.
- **Retail category performance:** The pandemic exposed 'non-essential' retailers, particularly those without a strong online offer and the food & beverage, leisure and hospitality sectors. Resilient sectors to have emerged include groceries, discounters, DIY, homeware, Bulky Goods and sportswear although we have seen a recover in the Food and Beverage and Leisure sectors since restrictions were lifted in the Spring.

1.4.3 Supermarkets

- **Supermarkets double rate of store growth:** The number of UK supermarket stores grew by twice as much last year as in 2019, with the total number of grocery stores in the UK up 1.4% in 2020, up from 0.7% in 2019. Supermarkets have been the undisputed winners in the pandemic but as the country recovers, there are signs they are beginning to be viewed less favorably, particularly compared to retail warehousing due to high costs and a fiercely competitive marketplace.
- **UK grocery sales:** Against a backdrop of rebounding footfall UK grocery sales have dipped by 1.9% during the 12 weeks to 5th September 2021, though shoppers spent £3bn more on grocers than they did during the same period of 2019. Total till sales bounced back to a growth of 1.1% in the most recent four weeks as physical stores benefitted from and 10% slump in online grocery sales. The population returning to dining out more regularly has been responsible for this trend.
- **Online sales decline for the first time:** According to Kantar at least 55% of shoppers now say they feel safe when making trips to a retailer. The number of people choosing to buy groceries online fell by 81,000 in July compared with the same four weeks last year. As the nation returned to shops, workplaces and restaurants over the summer months, digital baskets shrunk by 8% to an average of £80 per shop, the lowest since February 2020. As a result, year-on-year sales growth for online groceries has dropped for the first time ever, falling by 2.6%. The channel currently accounts for 13.3% of the total market.
- **There was increased investor appetite for food stores during the pandemic:** owing to their perceived security of income and often indexed rent the sector recorded the highest investment volumes of the retail subsectors in 2020 with £1.8bn transacted and prime yields below their pre pandemic levels.

1.4.4 Shopping Centres

- **Retail sales grow:** Household spending increased by 15.4% in the year to August 2021, according to Barclaycard. However, separate figures from the British Retail Consortium show that the spending boom has begun to slow, with sales rising by 3% in August, compared with the 6.9% three-month average and 3.9% growth during the same month last year.

- **Store closures continue:** Research has revealed that over 8,700 chain stores closed in the first six months of 2021, against 3,488 store openings over the same period. While this results in a net decline of 5,251 outlets, this is 750 less than this time last year.
- **Rent collections statistics:** Data from REMark (which covers around 125,000 leases and £2.3 billion of rent and £364 million in service charge) for the September quarter showed that the overall rent collection increased to 57.4%, the highest rent collection rate at the due date since before the pandemic. Retail rent recorded a marked improvement with 59.8% of rent collected by the due date compared to 50.8% in March 2021. Retail service charge collection improved from 42.5% to 52.1% at the due date.
- **Uplift in shopping centre transactions in 2021:** In 2020, shopping centres transacted a totaled £350m, a 72% decline on 2019 levels. However, the investment market has experienced an uplift in transaction volumes this year, with £850m traded from January to September 2021. JLL predict volumes to reach in excess of £1bn by year end which would be in line with 2018/19 levels but still some way off the 10 year average of £3bn.
- **M&G's two prominent shopping centres are under offer:** the Galleries Shopping Centre, Washington and Cwmbran Shopping Centre are reportedly under offer to LCP properties at a combined price of £140m, a discount of £29m from the asking price and reflecting a NIY of c.10%. CBRE are acting for M&G on the sale of the 750,000 sq ft Washington scheme and the 840,000 sq ft Cwmbran centre, which reportedly received multiple bids. The deal reflects the returning investor appetite for core retail assets.

1.4.5 Leisure

- **Leisure Rent Collection:** Data from REMark (which covers around 125,000 leases and £2.3 billion of rent and £364 million in service charge) for the September quarter showed that the overall rent collection for the leisure sector reached 34.3%, the highest rent collection rate at the due date since before the pandemic. Retail rent recorded a market improvement with 59.8% of rent collected by the due date compared to 50.8% in March 2021. Retail service charge collection improved from 42.5% to 52.1% at the due date.
- **UK dining out market to make full recovery in 2022:** The UK dining out market is expected to grow by 33.4% in 2021, to £63.6bn. By the end of 2022, the market is set to be worth £91.9bn, exceeding its pre-pandemic value of £91.3bn. The total dining out market declined by 47.8% to just £47.7bn in 2020, with just 11 weeks of normal trading.
- **Cinemas showing encouraging signs of recovery:** Annual admission were down 75% on 2019, equating to £44m, however, since the easing of lockdown restrictions, the early green shoots of recovery experienced in July 2020 have returned and are showing signs of positive momentum. The UK Cinema Association saw total box office takings reach £10.9m in the last week of September 2021, it's best performance since February last year.
- **Changing consumer patterns are now emerging in the leisure sector:** Customers are seeking experiences rather than transactions. Leisure has become an excellent way to drive customer engagement and diversify the income profile away from traditional retail. We are witnessing the breadth of leisure offer increasing to include trampoline parks, Escape Rooms, or branded attractions like Lego, SeaLife Centres or Nickelodeon alongside the more established competitive socialising concepts of crazy golf, axe throwing and of course, ten pin bowling.
- **Green shoots appears for UK Leisure in different sectors:** The UK leisure market was hit harder than most other sub-sectors during the pandemic. However, due to the easing of lockdown restrictions, the sector is now experiencing green shoots; an encouraging sign for investors actively seeking to capitalise on the recovery of assets within the retail market.

- **Repurposing agenda gathers pace:** Following Landsec/Invesco's plans to develop the 70,000 sq ft Wandsworth former Debenhams store into an amusement centre, US based Reef technology has reportedly signed an agreement with Capital & Regional to find new uses for parts of the landlord's schemes in Luton and London. Reef typically finds alternate uses for under-utilised car parks and shopping centres, turning them into urban farms, fulfillment centres and neighborhood kitchens.