CLUTTONS

UK retail market monitor

Quarter four – 2020

Cluttons market monitors track investment and occupier activity across the UK office, retail and industrial sectors. This edition offers a brief update on the UK retail market and presents headline figures on central London, the South East and the rest of the UK. We hope you find it informative.

In this report

SUMMARY OF RECENT ACTIVITY	IMPLICATIONS
Across the whole of the UK's retail landscape there are very few signs that the problems of the last few years are near being resolved. In some parts of the market take-up improved in Q4, but the long-term direction of travel suggests demand for retail space will continue to fall away.	The economic background is not auspicious for traditional retail businesses trading form the UK's High Streets. Non-food store sales collapse with the announcement of every lockdown. Retailers will be hoping that the successful roll-out of vaccinations will allow a return to some sort of normality.
The other side to weak demand is increasing levels of supply. The development pipeline has responded. Construction activity is at low levels. The limited amount of construction being undertaken is targeted specifically at the supermarket sector. Aldi and Lidl appear to be aggressively expanding capacity and market share.	The UK already had too many shops before the arrival of Covid-19. Lockdowns have accelerated the established trend. It is likely that the stock of shops will need to shrink by 30% or more. As things stand, the fragmented ownership of the UK's town centres prevents the necessary large-scale re-development or re-purposing.
Rental values continue to decrease but a rapid adjustment to the prevailing market conditions is delayed by leasing structures; in particular, upwards only rent review clauses. Business rates represent another obstacle to a regeneration of physical retailing. The cap on rates recently announced is seen as inadequate for large retail businesses seeking to re-structure.	There will be a gradual adjustment to turnover rents that more closely align the interests of asset owners and occupiers. The objections that have been raised, like the problem of accounting for click and collect, are not insurmountable. Business rates are going to remain for some time. They are after all an efficient way of raising tax revenue. A revaluation that recognises "true" retail rental values may be a solution.
Deflating rental values and the failure of large scale national multiple retailers will have dissuaded investors from considering investing in the sector. There is some indication that private property companies in particular see some value in retail warehousing trading at yields of 10% or more. Expect to see a more diverse range of investors including Local Authorities and Housing Associations.	Retail Parks add value to the property portfolios of major retailers such as Marks & Spencer and Next through increased sales. The case for them is even stronger if customers continue to shy away from public transport. Investment demand also comes from residential and logistics developers who are attracted to large sites located on the periphery of the UK's towns and cities.
Weak investor sentiment is causing yields to rise. In the last 12 months Shopping Centre capital values have decreased 30% and Retail Park values are down by 16%. Values have even been falling in central London. In Q4 MSCI recorded Mayfair retail values falling at an annualised rate of 26%.	At some point falling capital values and rising yields are likely to represent an opportunity for investors. But we have not reached that point yet. Funds that have a large weighting in retail are faced with the difficult decision of whether to switch out of the sector and crystallise significant losses.

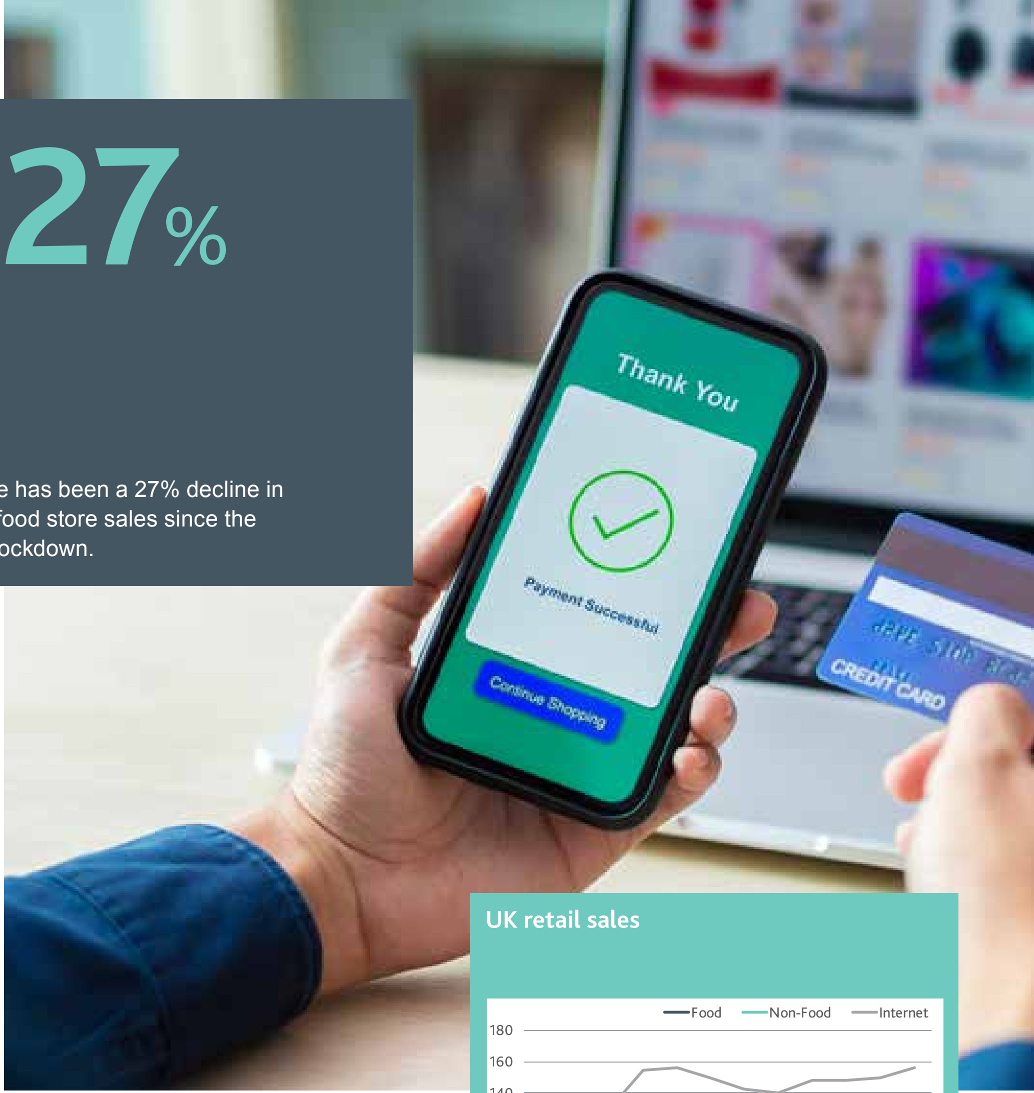
Internet sales are 56% higher than they were in February 2020. Non-food store sales are 27% lower than at the start of the pandemic. Traditional retailers are continuing to grow their online presence and shrink their bricks and mortar portfolios. Consequently, many towns have too much retail space relative to their consumer base. Debenhams in Wandsworth has been taken on by the trampoline company, Gravity and John Lewis are considering converting half their Oxford Street store to offices. But business rates continue to obstruct re-structuring of retail businesses.

We are now comfortably into the third month of Lockdown 3.0 and its impact on the retail economy is by now well understood. The first lockdown created a wave of panic buying of toilet rolls and pasta. Since then, food sales have remained reasonably stable. At the end of January, they were just 5% above their level in February 2020. Office workers are still required to work from home and only travel when absolutely essential. White vans delivering internet purchases to households make up much of the traffic on residential streets. Internet sales have kicked on again in Lockdowns 2.0 and 3.0 and are 56% higher than they were in February last. All of which means that non-food store sales are 27% lower than at the start of the pandemic (see chart opposite).

There are some surprising and not so surprising numbers behind these headlines. Quite intuitively, in a pandemic, dispensing chemists have increased sales by 44%. Sales of clothing are down 47%; households only need so many sets of pyjamas and track suits. Restaurants, pubs, clubs and bars may be closed but there are indications household bubbles are socialising at home. Sales of beer, wines and spirits are up 19%. Music sales that grew 8% in the five years ending in February 2020 have now grown 7% in the last 11 months.

Since travel restrictions were first imposed in March last year there have been very many articles, academic papers and webinars discussing the impact of working from home on the future demand for office space. The assumption was that employees were being supplied with wi-fi, routers, computers, screens, web cams, laptops and printers to equip the home office. But this may not be the case. Counter intuitively, sales of computers and telecoms equipment have fallen 47% since the first lockdown started.

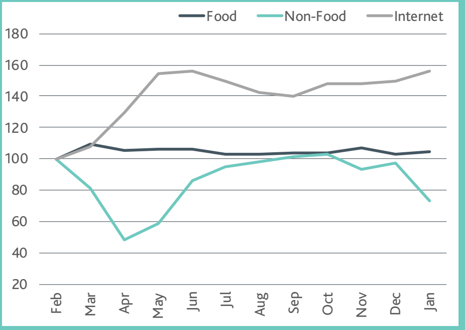
The UK's pre-eminent shopping location is starting loose its lustre. Debenhams, Topshop, and Gap stores on Oxford Street are closing. Meanwhile the former HMV and Forever 21 flagships remain empty, months after being vacated.



-27%

There has been a 27% decline in non-food store sales since the first lockdown.

UK retail sales



Source: Office for National Statistics

Traditional retailers are continuing to grow their online presence. At John Lewis online sales have grown to represent more than 60% of sales, from 40% before the pandemic. The retailer is committing £1bn over the next 5 years to accelerate its online business and transform its shops. The pre-pandemic delivery capacity at Waitrose was limited to 55,000 customers per week. That has now grown to 250,000 orders per week and the ambition is to grow capacity further.

Next sales from its stores in Q4 2020 fell 43% but its online sales grew 38%. The online business compensated for almost all sales lost in retail stores and total sales were down just 0.5%. Sales of loungewear and sportswear were a success but unsurprisingly adult clothing for work, parties and nights out did not sell well. Next reported that stores located in out-of-town retail parks continued to perform around 15% better than those in city centres and shopping centres. This trend is picked out in this report and represented by the stronger investment performance from Retail Parks.

Another hot pandemic discussion topic has been how to re-purpose the UK's high streets. Many towns have too much retail space relative to their consumer base. KPMG's January report entitled "The future of towns and cities post Covid-19" concluded that home working and online shopping could cost a further 400,000 retail jobs. Basingstoke, Bracknell and Guildford were considered to be three of the more vulnerable centres.

Debenhams, which fell into administration for the second time in April 2020, provides an illustration of just how re-purposing might work. In January, online fashion retailer Boohoo paid £55m for the Debenhams brand and website but not its stores. Meanwhile, the 80,000 sf former Debenhams in Wandsworth had been taken on by the trampoline company, Gravity. The store will now house an electric go-karting area, bowling lanes, pool, darts and crazy golf. And, Next will take over the beauty halls in five Debenhams stores in Hammerson owned shopping centres as it seeks to build its beauty brand.

Mike Ashley who bought House of Fraser from its administrators in 2018, is understood to have been negotiating to buy the other vacated Debenhams stores. However, these negotiations appear to have been jeopardised by the Chancellor's plans to limit business rate relief from July onwards for the tax year ending March 2022 with a £2 million cap.

Frasers Group which includes brands such as Sports Direct, Game and Evans Cycles, has taken clear exception at the £2m cap in particular, saying:

"The £2m rates cap on 'businesses' from July 2021 to March 2022, makes it a near worthless support package for large retailers ... [it] will make it nearly impossible to take on ex-Debenhams sites with the inherent jobs created. It will also mean we need to review our entire portfolio to ascertain stores that are unviable due to unrealistic business rates."

Real estate is forming a key part of John Lewis's future strategy. Last year, John Lewis announced the closure of eight stores in Birmingham, Croydon, Watford, Newbury, Swindon, Tamworth Heathrow Airport and St Pancras International. It is now reported to be considering further closures. There are also considerations to convert half of the flagship Oxford Street store into offices. In addition, Waitrose supermarket sites will have their suitability for residential development assessed.

It is clear the investment performance of shops, Shopping Centres and Retail Parks is not going to turn round any time soon. The accompanying report highlights shrinking take-up from occupiers and growing levels of availability. In these circumstances expect rental values to fall back and yields to soften further. Any upside is represented by Retail Parks which may offer opportunities for either residential development or re-purposing as logistics space.

-38%

Next's online sales grew by 38% in Q4 2020, but sales from its stores fell by 43% over the same period.

£55m

In January, online fashion retailer Boohoo paid £55m for the Debenhams brand without the stores.

Central London retail in figures

Central London

Opposite, recent quarterly activity in central London's retail markets is compared to activity last quarter, last year and to average levels. The outlook for rents and yields is summarised.

Take-up increased in Q4. Over the whole of 2020 take-up is 33% lower than 2019 and 24% below the 5-year average. Availability levels have increased, and rental values fallen back. Development completions are trending lower reflecting limited construction activity and poor occupier demand.

We expect very limited occupier demand to cause a continuing decline in rental values. Poor investment demand will allow yields to soften further.

Take-up ('000 sf)

Quarter	Year	Vs. 5-year quarterly average
+17%	-33%	-24%
Q4 : 102.9 k sf Q3 : 88.1 k sf	2020 : 333 k sf 2019 : 479.3 k sf	5-year quaterly average : 134.6 k sf

Costar asking rents (£ per sf)

Quarter	Year	Outlook
-2%	-3%	-5%
Q3 : -1% Q2 : -1%	2019 : 2% 2018 : 0%	2022 : -2% 2023 : 0%

Availability (m sf)

Quarter	Year	Vs. 5-year quarterly average
+38%	+69%	+104%
Q4 : 1.6 m sf Q3 : 1.1 m sf	2020 : 1.6 m sf 2019 : 0.9 m sf	5-year average : 0.8 m sf

Investment (£ bn)

Quarter	Year	Vs. 5-year quarterly average
+900%	-10%	+79%
Q4 : £310.0 m Q3 : £31.0 m	2020 : £342.7 m 2019 : £379.2 m	5-year quaterly average : £173.4 bn

MSCI yield on Central London shops

Quarter	Year	12 month outlook
+40 bps	+60 bps	+25 bps
Q4 : 4.1% Q3 : 3.7%	2020 : 4.1% 2019 : 3.5%	2022 : +12 bps 2023 : -12 bps

Note: Central London refers to Camden & Islington, Covent Garden & Soho, Chelsea, Kensington and Knightsbridge, Mayfair, Oxford Street west and north of Oxford Street.

Source: Cluttons, MSCI/EY, Property Data, Costar

South East retail in figures

South East retail

Opposite, recent quarterly activity in the South East's retail markets is compared to activity last quarter, last year and to average levels. The outlook for rents and yields is summarised.

Low take-up in Q3 decreased even further in Q4. Over the whole of 2020 take-up is 38% lower than 2019 and 76% below the 5-year average. Availability levels have increased, and rental values fallen back. Development completions have increased in the short term but are trending lower in the medium to long term.

We expect very limited occupier demand to cause a continuing decline in rental values. Poor investment demand will allow yields to soften further.

Take-up ('000 sf)

Quarter	Year	Vs. 5-year quarterly average
-40%	-38%	-76%
Q4 : 40.9 k sf Q3 : 68.8 k sf	2020 : 266.4 k sf 2019 : 428.4 k sf	5-year quaterly average : 169.5 k sf

Costar asking rents (£ per sf)

Quarter	Year	Outlook
-1%	-3%	-7%
Q3 : -1% Q2 : -1%	2019 : 2% 2018 : 0%	2022 : -4% 2023 : -3%

Availability (m sf)

Quarter	Year	Vs. 5-year quarterly average
+4%	+15%	+32%
Q4 : 1.2 m sf Q3 : 1.2 m sf	2020 : 1.2 m sf 2019 : 1.1 m sf	5-year average : 0.9 m sf

Investment (£ bn)

Quarter	Year	Vs. 5-year quarterly average
+379%	-46%	-68%
Q4 : £49.6 m Q3 : £10.4 m	2020 : £97.7 m 2019 : £180.32 m	5-year quaterly average : £155.9 bn

MSCI yield on South East shops

Quarter	Year	12 month outlook
+17 bps	+93 bps	+25 bps
Q4 : 7.0% Q3 : 6.9%	2020 : 7.0% 2019 : 6.1%	2022 : +12 bps 2023 : -12 bps

Note: South East refers to Brighton, Bromley, Kingston, Guildford, Milton Keynes, Oxford, Reading Canterbury, Southampton and Chelmsford.

Source: Cluttons, MSCI/EY, Property Data, Costar

UK regional centres retail in figures

UK regional centres

Opposite, recent quarterly activity in the UK's major regional centres is compared to activity last quarter, last year and to average levels. The outlook for rents and yields is summarised.

Take-up increased in Q4. Over the whole of 2020 take-up is 34% lower than 2019 and 54% below the 5-year average. Availability levels have increased, and rental values fallen back. There were no development completions of note in Q4, and completions are trending lower in the medium to long term.

We expect very limited occupier demand to cause a continuing decline in rental values. Poor investment demand will allow yields to soften further.

Take-up ('000 sf)

Quarter	Year	Vs. 5-year quarterly average
+20%	-34%	-54%
Q4 : 124.6 k sf Q3 : 104.1 k sf	2020 : 555.4 k sf 2019 : 839.1 k sf	5-year quaterly average : 271.5 k sf

Costar asking rents

Quarter	Year	Outlook
-3%	-1%	-7%
Q3 : -1% Q2 : +1%	2019 : +1% 2018 : -1%	2022 : -4% 2023 : -3%

Availability (m sf)

Quarter	Year	Vs. 5-year quarterly average
+2%	+38%	+26%
Q4 : 2.7 m sf Q3 : 2.6 m sf	2020 : 2.7 m sf 2019 : 1.9 m sf	5-year average : 2.1 m sf

Investment (£ bn)

Quarter	Year	Vs. 5-year quarterly average
-55%	-83%	-68%
Q4 : £24.4 m Q3 : £54.3 m	2020 : £175.6 m 2019 : £1,059.1 m	5-year quaterly average : £317.3 m

MSCI yield on Rest of UK shops

Quarter	Year	12 month outlook
+26 bps	+121 bps	+25 bps
Q4 : 8.2% Q3 : 7.9%	2020 : 8.2% 2019 : 7.0%	2022 : +12 bps 2023 : -12 bps

Note: 'UK regional centres' refers to Birmingham, Bristol, Edinburgh, Glasgow, Leeds, Manchester, Cardiff, Liverpool, Newcastle and Nottingham.

Source: Cluttons, MSCI/EY, Property Data, Costar

Retail parks & shopping centres in figures

UK regional centres

Opposite, recent quarterly activity in the UK's Shopping Centres and Retail Parks is compared to activity last quarter, last year and to average levels. The outlook for rents and yields is summarised.

Take-up increased in Q4. Over the whole of 2020 take-up is 47% lower than 2019 and 69% below the 5-year average. Availability levels have increased, and rental values fallen back. Development completions are lower across all time periods analysed.

We expect very limited occupier demand to cause a continuing decline in rental values. Poor investment demand will allow yields to soften further.

Take-up ('000 sf)

Quarter	Year	Vs. 5-year quarterly average
+21%	-47%	-69%
Q4 : 563.6 k sf Q3 : 464.7 k sf	2020 : 2593.5 k sf 2019 : 4915.0 k sf	5-year quaterly average : 1796.2 k sf

Costar asking rents (£ per sf)

Quarter	Year	Outlook
-2%	-5%	-3%
Q3 : -3% Q2 : 0%	2019 : -3% 2018 : -7%	2022 : -2% 2023 : -2%

Availability (m sf)

Quarter	Year	Vs. 5-year quarterly average
+1%	+14%	+8%
Q4 : 11.4 m sf Q3 : 11.4 m sf	2020 : 11.4 m sf 2019 : 10.1 m sf	5-year average : 10.6 m sf

Investment (£ bn)

Quarter	Year	Vs. 5-year quarterly average
-15%	-18%	-26%
Q4 : £387.3 m Q3 : £456.4 m	2020 : £1,067.5 m 2019 : £1,295.1 m	5-year quaterly average : £521.8 m

MSCI Shopping Centre yields

Quarter	Year	12 month outlook
+57 bps	+202 bps	+25 bps
Q4 : 9.3% Q3 : 8.8%	2020 : 9.3% 2019 : 7.3%	2022 : +25 bps 2023 : -12 bps

MSCI Retail Park yields

Quarter	Year	12 month outlook
-3 bps	+74 bps	+25 bps
Q4 : 7.6% Q3 : 7.6%	2020 : 7.6% 2019 : 6.8%	2022 : +25 bps 2023 : -12 bps

Source: Cluttons, MSCI/EY, Property Data, Costar

CLUTTONS

Cluttons LLP
2 Portman House
Portman Street
London W1H 6DU

T: 020 7408 1010
F: 020 7647 7177
cluttons.com

For further details contact
James Gray
Managing partner
T: 020 7647 7204
james.gray@cluttons.com

Sophy Moffat
Head of research
T: 07970 539 958
sophy.moffat@cluttons.com

2807 – 0321