RESEARCH

Q1 2012 SHOPPING CENTRE

Investment quarterly

Knight Frank

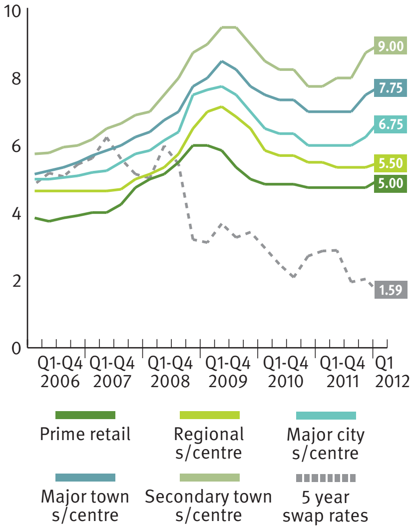
Outlook

- While the economic outlook appears to be more stable, Q1 2012 recorded much lower levels of transactions than a year ago as investors remained cautious. Pricing remains key, with investors now increasingly pricing in potential retailer failures, demanding rental guarantees on certain income streams and, in some cases, excluding risky income from their analysis.
- As a result, shopping centre yields are generally under outward pressure, particularly at the secondary end of the market. In relation to prime schemes, much will depend on the outcomes of the on-going sales of Meadowhall and Basingstoke. Many retailers are still experiencing tough trading conditions and continue to seek opportunities to re-base rents – which will inevitably affect values.
- While the UK Economic outlook has improved slightly, recent retail sales growth has remained weak and driven by the internet which continues to take an increasing share of total spend. Indeed, in addition to the difficult economic backdrop, the retail sector continues to undergo significant structural change, with many retailers expected to further reduce their store portfolios going forward.
- Nevertheless, demand exists for the right product across the quality spectrum, provided realistic pricing is adopted. We are also noticing more enquiries from overseas sources for quality schemes.

Figure 2

Retail & shopping centre equivalent yields

Q1 2006 - Q1 2012

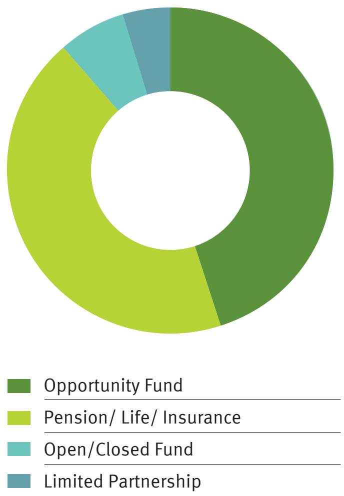


Source: Knight Frank LLP

Figure 1

Who's buying?

Q1 2012



Source: Knight Frank LLP

Q1 shopping centres sold and under offer

Shopping centre	Status	Purchaser	Vendor	Price (£m)	NIY %
Royal Victoria, Friary Mall, Castlecourt	Sold	Hermes	Westfield	190.0	N/A
Ocean Terminal, Edinburgh	Sold	Resolution	Forth Ports	90.0	7.50
St John's Centre, Liverpool	Sold	InfraRed Capital Partners	Land Securities	76.5	8.50
Marriots Walk, Witney	Sold	RREEF	Kandahar/LBG	28.1	6.04
St Andrews Square, Droitwich	Sold	Salmon Harvester	LBG	19.8	7.50

Source: Knight Frank LLP

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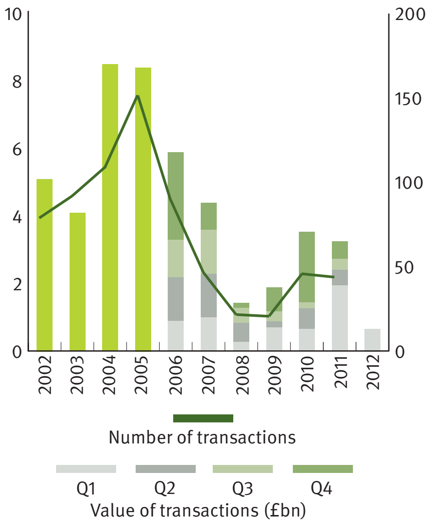
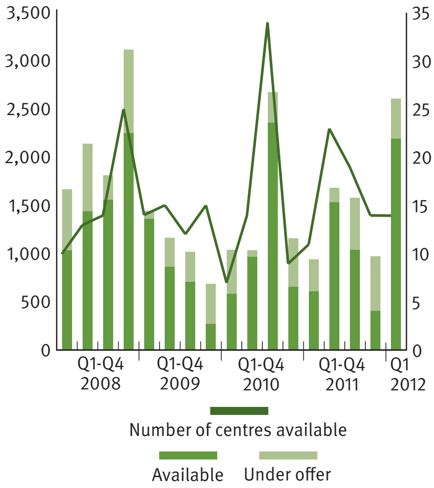
Figure 3
Shopping centre transactions
(LHS – Value of transactions, £bn)
(RHS – Number of transactions)



Source: Knight Frank LLP

Figure 4
Shopping centre availability
(LHS – Value of availability, £m)
(RHS – Number of centres available)



Source: Knight Frank LLP

Market commentary

- Concerns over the economy and the general health of the retail sector have led to reduced investment activity. Ten shopping centre assets were transacted during Q1 2012, with overall transaction values reaching £668.8m, compared with Q1 2011's £1.95bn. In addition, the cost and availability of finance remains a key issue, with debt on competitive terms generally available only for the better-let schemes.
- The largest deal of Q1 was Hermes' £190m acquisition of Westfield's 50% stakes in Royal Victoria Place, Tunbridge Wells, The Friary Centre, Guildford and Castle Court, Belfast. As a result of the deal, Hermes now owns the three schemes outright.
- Other key transactions which were agreed in late 2011 included the sale of Ocean Terminal in Edinburgh and St Johns Centre in Liverpool; both lot sizes were over £50m and had net initial yields of 7.50% and 8.5% respectively.
- The purchaser profile in Q1 was dominated by the opportunity funds which accounted for 45.1% of acquisitions by value, followed closely by pension/life/insurance funds which accounted for 43.6%. While the larger REITs/property companies remain active in the shopping centre market, they did not conclude any purchases in Q1.
- At the end of Q1, 14 assets with a combined quoted sale price of £2.19bn were available, compared with £400m worth of stock at the end of last year. The majority of this stock comprises secondary schemes and relatively small lot sizes. Nonetheless, one sizeable prime asset also came to market in Q1, namely the Meadowhall Centre in Sheffield for a quoted sale price of £1.68bn (100%).
- Four schemes with a combined value of c£300m were reported to be under offer at the end of Q1, namely The Mall in Norwich to Infrared, the Broadwalk Centre in Edgware to SWIP, the Kingfisher Centre in Redditch to Capital & Regional and Captain Cook Square in Middlesbrough to LaSalle Investment Management.
- Yields on all UK shopping centres remain vulnerable to a further outward shift and a difference of as much as 225 basis points now exists between prime schemes and good secondary stock. While buying opportunities for prime assets remain in short supply, debt-driven investors have been extremely cautious and have focused on stock with strong income profiles. The prime shopping centre yield stood at 5.50% at the end of March – a 15bps outward shift on December, while the yield for good secondary schemes was 7.75% – 25bps higher than three months earlier.
- Based on the latest IPD data (February), the rate of decline in shopping centre capital values accelerated to just over 1% between January and February on the back of falling rents and higher yields. Rents edged down by 0.25%, while the initial yield rose 8bps over the month to stand at 7.37% in February.
- Real growth in retail sales has been minimal for some time and sales volumes for February rose by just 1% year-on-year – driven by predominantly food stores. While the internet continued to surge ahead with annual sales growth of 9%, non-food sales growth was flat overall.

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