RESEARCH

SHOPPING CENTRES
INVESTMENT QUARTERLY **Q4 2016**

Outlook

2016 – A Year to Forget

2016 saw the lowest transaction volumes since 2009, down 28% compared to 2015. These bare stats become worse when one considers that of the £3.05bn transacted, just four deals comprised over half of the total (£1.6bn), these being: Merry Hill (50%), Grand Central Birmingham, Liverpool One (35%) and the development commitment at St James Edinburgh.

A major factor in the low transactional volumes has been the Brexit vote, with concerns over the outcome contributing to low volumes during the first half of the year and most investors taking a cautious ‘wait and see’ approach in the second half of the year.

2017 Themes

With a similar political backdrop likely in the early part of the year, 2017 is likely to start much as 2016 ends, with economic uncertainty suffocating investment volumes. Where schemes are offered to the market it is likely to be done quietly and to a targeted audience.

As the year progresses we anticipate more liquidity with valuations re-aligning and vendors being more willing to accept the revised levels of market pricing.

We do anticipate that as next year progresses, we will start to see an improvement in global demand for prime assets, this having waned in 2016.

The general divergence between “the best” schemes and “the rest” will continue, and the more experienced and active asset managers are likely to fare better than those whose resources are limited or stretched.

Retail Sales Growth Accelerates in Q4

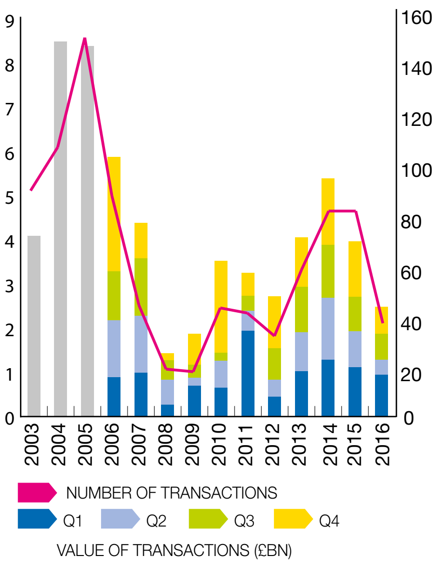
Consumer demand remains supportive of occupier markets, contrary to widespread expectations. Indeed, retail sales growth has accelerated since the Referendum vote, with rolling 3 month volumes and values up 5.7% and 4.2% respectively in October, according to the ONS.

The BRC reported a relatively solid set of figures for November (+1.3% overall, +0.6% like-for-like) and retailers seem well set for a positive outturn in December, particularly in the context of a soft comparable last year.

FIGURE 1

Shopping centre transactions

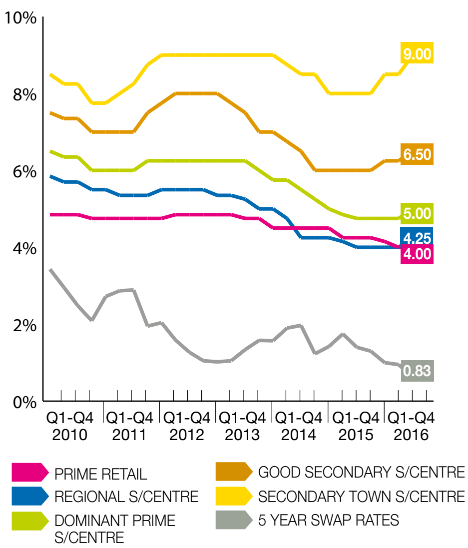
(LHS – Value of transactions, £bn)
(RHS – Number of transactions)



Source: Knight Frank LLP

FIGURE 2

Retail & shopping centre equivalent yields Q1 2010 - Q4 2016



Source: Knight Frank LLP

Q4 2016 shopping centres transactions

Shopping centre	Status	Purchaser	Vendor	Price (£m)	NIY %
Intu, Bromley (85%)	Sold	LaSalle Investment Management	Intu / Aviva	£236m	6.00%
The Mall, Camberley	Sold	Surrey County Council	Capital & Regional	£86m	5.90%
Observatory & Queensmere, Slough	Sold	ADIA / Catalyst	Golfrate / Criterion Capitol	£130m	5.00%
Southside, Wandsworth (50%)	Under Offer	Invesco	Delancey	£147.5m	4.50%

Source: Knight Frank LLP

MARKET COMMENTARY

A Test of Mettle for Retail Occupiers

Next year is likely to prove to be something of a year of reckoning for retailers, who have to date been largely incubated from post-Brexit pressures. The challenges are likely to be margin/profit-related, as opposed to top-line/sales-driven. Indeed, we expect consumers to carry on spending and retail sales to hold up accordingly.

However, for many retailers, pressure will mount on the bottom line next year. This is only in part Brexit-linked, with issues such as the national living wage and business rates re-evaluation playing out independently of wider economic uncertainty. The issue of rising sourcing costs on the back of Sterling's weakness will come increasingly to the fore as existing currency hedges lapse.

There will inevitably be some occupier fall-out in the early part of 2017, but this is likely to be fairly minor in scale. The fact that most retailers have right-sized their portfolios and repaired their balance sheets over the last few years means we are unlikely to see a repeat of 2008.

South East Focus

Centres in London and the South East will continue to experience higher levels of investment demand than those in other parts of the country. Fringe-London demand is strong relative to the regions and with rents looking affordable against inflated Central London occupational costs, we do foresee medium term rental growth in and around the M25. Certainly vacancy rates in this area are likely to remain significantly lower than they are in comparable stock in the regions.

Councils very active but are they here to stay?

Local Authorities were key players in the market in 2016, transacting nine of the 40 schemes sold, or around 12.5% of total volumes by value. However, the government has confirmed plans to abolish the Public Works Loan Board, which may reduce the ability of Councils to borrow.

Until now, local authorities have been responsible for making their own borrowing decisions without government consent under the prudential regime, where any borrowing is automatically secured against authorities' revenues. However, whilst the process is currently under consultation, this lending power is likely to be transferred to the Treasury, which in turn is likely to mean that the ultimate function of the loans comes under increased scrutiny, which may reduce local authorities' ability to acquire property.

Debt Market

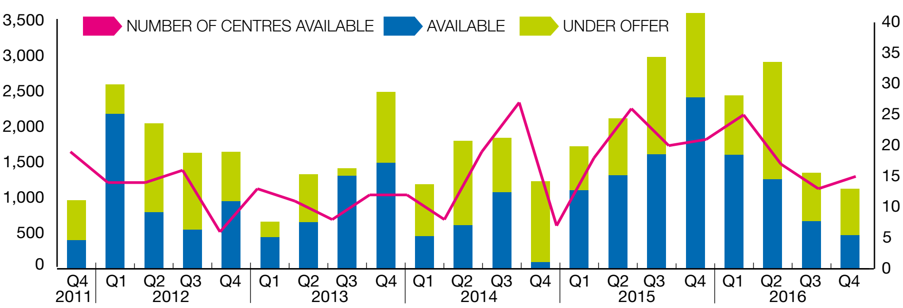
Senior debt remains generally available up to 60% LTV on an interest-only basis, and up to 65% with some amortisation, with best pricing achievable on property with long term sustainable rents. Schemes with short WAULTs are becoming more difficult to finance, and whilst credit departments are still receptive to new transactions, they are becoming more cautious. Regulatory costs are increasing, and generally we are seeing increased swap rates and upward pressure on loan margins, which start at c170 bps for investment finance.

Knight Frank advised the purchaser of Parkgate Shopping Centre, Shirley

- November 2016
- Long Leasehold
- Price: £16m
- Size - 195,000 sq ft
- Vendor – Helical Bar
- Purchaser - Moorgarth Properties Ltd
- NIY – 7.25%

FIGURE 3

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



Source: Knight Frank LLP

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