Chorley Council

COUNCIL

TUESDAY, 24TH JULY 2018, 6.30 PM
COUNCIL CHAMBER, TOWN HALL, CHORLEY

I am now able to enclose, for consideration at the above meeting of the Council, the following reports that were unavailable when the agenda was published.

Agenda No	Item	
11	**MARKET WALK UPDATE** To receive and consider the report of the Director (Business, Development and Growth).	(Pages 3 - 12)
14	**TO CONSIDER THE NOTICES OF MOTION (IF ANY) GIVEN IN ACCORDANCE WITH COUNCIL PROCEDURE RULE 10**	(Pages 13 - 34)

GARY HALL
CHIEF EXECUTIVE

Electronic agendas sent to Members of the Council

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Meeting contact Ruth Rimmington on 01257 515118 or email ruth.rimmington@chorley.gov.uk

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Report of	Meeting	Date
Chief Executive (Introduced by Executive Member for Economic Development and Public Service Reform)	Full Council	24 July 2018

MARKET WALK UPDATE

PURPOSE OF REPORT

1. This report provides an update on the current status of the project and proposed phasing.

2. The report outlines the status of associated parking, public realm and enablement projects which are linked to the delivery of the project.

RECOMMENDATION(S)

3. That Council notes the schemes progress in line with the programme proposed in Appendix A to enable trading to commence for Christmas 2019.

EXECUTIVE SUMMARY OF REPORT

4. Council approved a report on Market Walk 23 January 2018 which authorised the Executive Leader, in consultation with the Executive Cabinet, to approve the final design based on Option 2 and to approve any alterations or amendments to the final design, for the delivery of Option 2, which are contained within the approved budget and cost model.

   Option 2: Commission a partial redesign of the layout, based on the building footprint from the original design to increase flexibility in lettings and then continue to build at the earliest opportunity.

5. On 23 January 2018 Council resolved to proceed without further delay, with the Market Walk Extension development based upon Option 2.

   This will include:

   a. The building of the retail and leisure units based upon a design that meets the needs of the tenants; and
   b. The delivery of the proposed parking solution; and
   c. The delivery of the Public Realm improvements.

Confidential report Please bold as appropriate	Yes	**No**

CORPORATE PRIORITIES

6. This report relates to the following Strategic Objectives:

Involving residents in improving their local		A strong local economy	X

area and equality of access for all			
Clean, safe and healthy communities		An ambitious council that does more to meet the needs of residents and the local area	X

BACKGROUND

7. On 23 January 2018 Council resolved to proceed without further delay, with the Market Walk Extension development based upon Option 2.

   This will include:

   a. The building of the retail and leisure units based upon a design that meets the needs of the tenants; and
   b. The delivery of the proposed parking solution; and
   c. The delivery of the Public Realm improvements.

8. The Council allocated the budget sum of £16,364,643 to deliver the Market Walk Extension and associated works.

CURRENT POSITION

9. Works to the main build were suspended in November 2017 after M&S failed to complete their Agreement for Lease due to re-profiling their store portfolio and re-appraising proposed store expansion plans.

10. Works are underway to extend the Cleveland street short stay car park by demolishing Oak House – this is due to be complete in early August.

11. Works are underway to create a decked car park expanding Friday Street long stay car park.

12. Works took place to create temporary short stay parking provision on the Flat Iron and tenant parking by Market Walk service yard 2.

13. Works are complete to create a council staff car park on Arley Street.

14. In addition to the above temporary parking arrangements have been put in place for market trader parking provision adjacent to Chorley Station and at the Swan with 2 Necks.

CURRENT LETTINGS POSITION

15. Unit 1 – 12,800 sq ft positive dialogue is ongoing with Marks & Spencer design team regarding a revised ground floor store.

16. Unit 2 – 3,900 sq ft letting agents in discussions with retail outlets

17. Unit 3 – 3,400 sq ft letting agents in negotiation with a high street restaurant chain

18. Unit 4 – 9,200 sq ft Heads of Terms been agreed with a high quality regional leisure/restaurant venue operator

19. Unit 5 – 2,000 sq ft letting agents in discussions with coffee outlets

20. Unit 6 – Reel cinema has signed an Agreement for Lease, have been informed of the current situation and confirmed their commitment to the scheme.

21. Unit 7 – 14,600 sq ft first floor accessed from 1,300 sq ft ground floor lobby letting agents in negotiation with a national gym chain.

22. Unit 8 – 3,300 sq ft Heads of Terms are agreed with Loungers and they have instructed their solicitors.

PROJECT PHASING

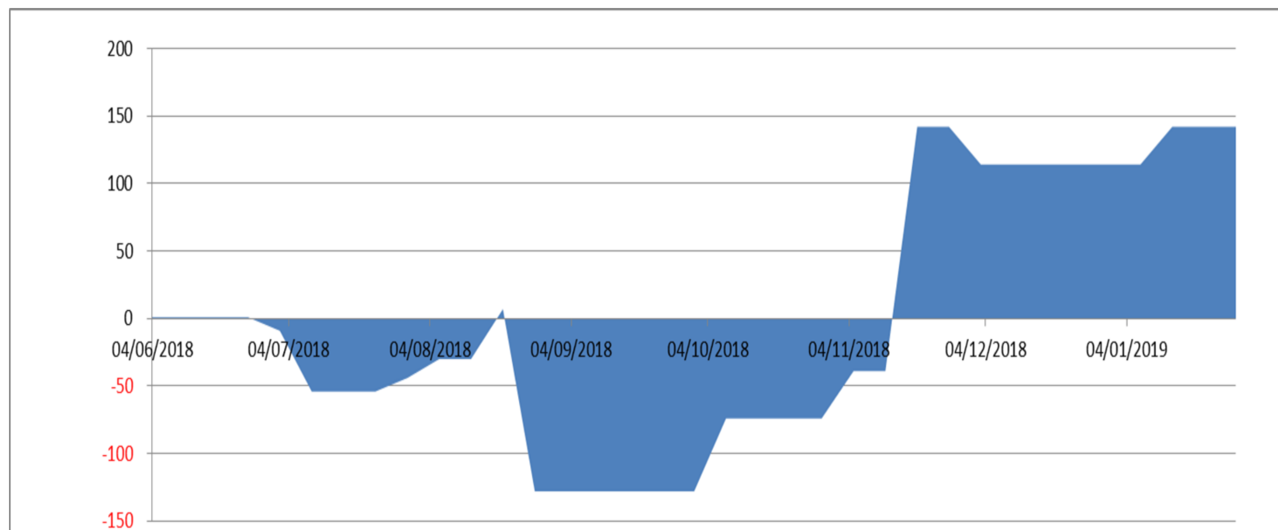
23. In order for the scheme to be open for trading in Christmas 2019 the phase 2 main build needs to commence prior to Christmas this year. Appendix A shows a phasing plan across all associated works in order to achieve this.

24. The key points from this programme are:
    a. Oak House complete in mid-August
    b. Friday Street car park ground floor released mid-October
    c. Friday Street full car park released mid-November
    d. Unit 8 site investigations and council network duct installation commence late August
    e. Clifford Street crossing works commence early September
    f. Brunswick Street improvements commence mid-September
    g. PALS monument works commence mid-September (in time for the centenary event on 11/11/2018)
    h. Phase 2 main build commence early October
    i. Union Street public realm improvements commence April 2019
    j. Tenant access for fit-out (practical completion) July 2019
    k. Scheme open for trading December 2019

PARKING

25. A major concern for existing businesses within the town centre has been the impact of lost parking spaces in close proximity to the retail core during phase 2 works.

26. The impact to parking across the town centre of the proposed phasing plan (Appendix A) is shown in the chart below:



27. The chart shows:
    a. That there are deficiencies of ~50 spaces through July & August until the Oak House spaces are completed.
    b. That there are deficiencies of ~125 spaces through September until the ground floor spaces of Friday Street are released.
    c. That there are deficiencies of ~75 spaces through October until the full Friday Street deck is completed.
    d. Once the deck is completed there will be a surplus of ~140 additional spaces compared to what was previously available on the Flat Iron
    e. By closing Oak House car park to accommodate the Christmas Ice Rink there will only be an additional ~115 spaces in December.

28. To mitigate the period where spaces are lost whilst phase 2 works re-commence, prior to the Friday Street car park being fully complete, it is proposed that a number of council staff will be instructed to park & ride through a shuttle bus service from Woodlands Road site each Tuesday when demand is highest. On the other days of the week there is envisaged to be enough surplus capacity at this time of year to suffice for the short period.

ASSOCIATED WORKS – PUBLIC REALM

29. The Chorley PALS memorial improvements now need completing in isolation in order to be ready for the centenary event on 11th November 2018.

30. The super-crossing on Clifford Street will be delivered prior to the Friday Street car park opening and under a traffic management plan keeping a lane flowing at all times apart from 2 overnight closures to resurface.

31. Brunswick Street improvement works will be carried out to improve pedestrian linkage through to Friday Street car park alongside the Clifford Street works.

FINANCIAL APPROVALS TO DATE

32. On 23 January 2018 a report to Full Council asked members to approve one of three options to be progressed with Eric Wright. Members approved the option to commission a partial redesign with an updated budget of up to £16.365m (excluding VAT) as detailed in Table 1 below.

33. **Table 1 Budget Approved in January 2018**

	Approved Budget
Development Cost	12,309,911
Total Development Budget	**12,309,911**
Parking Options	2,297,719
Enabling Costs	1,557,013
Brunswick Street	200,000
Total Approved Budget	**16,364,643**

34. Out of the overall approval in Table 1, approval was given to commit funds against a pre-construction service agreement (PCSA) to undertake the initial phases of work. These approvals totalled £2,735,226. The work done to date has been drawn down from the

development budget and is therefore absorbed in to the estimated costs provided by Eric Wright, as detailed the Costs section in Table 2 below.

COSTS

35. **Table 2 – Current Development and Parking Costs**

	Approved Budget	Current Forecast
Market Walk Extension - Main Build	12,309,911	12,306,677
Market Walk Extension - Enabling Costs	1,557,013	1,592,226
Total Development	**13,866,924**	**13,898,903**
Oak House Car Park	476,161	535,270
Friday Street Decked Parking	1,751,558	1,660,470
Arley Street Car Park	70,000	70,000
Brunswick Street Improvements	200,000	200,000
Total Parking Options	**2,497,719**	**2,465,740**
Grand Total	**16,364,643**	**16,364,643**

36. The costs detailed in Table 2 above for the Market Walk Extension main build are provisional, subject to a re-tendering exercise being carried out by Eric Wright. Eric Wright have been asked to keep costs within the overall budget, therefore wherever any element of the project is forecast to be over budget, the costs will be met through value engineering elsewhere.

37. Other maintenance works on-site such as temporary parking and the improvement to the PALS memorial will be funded through council maintenance budgets.

MAIN DEVELOPMENT - FINANCING

38. The annual borrowing cost for the development is dependent on the level of overage that the council wishes to commit to the project and therefore the level of risk the council wishes to take. There is an option to reduce borrowing costs by committing overage funds which have not yet been agreed by developers.

39. Table 3 below illustrates the annual cost of borrowing assuming the council takes the low risk approach to committing these funds. All subsequent income analysis assumes the higher cost of borrowing.

40. **Table 3 - Financing of the Development**

	Development
Borrowing	6,723,226
Overage	2,391,664
Developer Contributions	3,711,055
Capital receipts and reserves	1,072,958
Total Financing	**13,898,903**
Annual Cost of Borrowing	**239,150**

41. The net distributable income achieved by the extension factors in both the borrowing cost and rental income.

42. The estimated net distributable income on a fully let scheme is shown in Table 4 below. Assumptions for currently vacant units have been made based on ongoing discussions with interested parties and typical rental values per square foot. The value of incentives available has been capped at the level reported in July 2017.

43. **Table 4 – Net distributable income assuming full occupancy**

Fully Occupied	**Development**
Annual Cost of Borrowing - Development	239,150
Gross Rental Income	(935,135)
Cost of Incentives	235,681
Distributable Income (Surplus)/Deficit	**(460,304)**

44. Heads of Terms or advanced negotiations with Solicitors have been agreed with Reel, Marks & Spencer and Loungers. This represents lettings of 48.6% of floor space with 6 vacant units available for letting. If the scheme were to progress with the commitment of these three tenants the value of Net Distributable Income would be as shown in Table 5:

45. **Table 5 - Net distributable income with current lettings**

Current Agreed Lettings in Heads of Terms or in negotiation with Solicitors	**Development**
Annual Cost of Borrowing - Development	239,150
Gross Rental Income	(451,480)
Cost of Incentives	180,046
Distributable Income (Surplus)/Deficit	**(32,284)**

46. As the models show, the scheme will make a surplus with all current parties signed up.

47. The scheme will also attract additional income through the retained business rate scheme. It is not possible to quantify the exact amount as the rateable value is dependent on a number of factors. The government has committed to 75% retention by 2020/21 but the details of how the scheme will operate and how sums will be distributed between bodies are still unknown.

48. The valuation office provided an estimate of rateable values on the original scheme, which under current regulations, provided around £117k per annum in retained rates.

PARKING - FINANCING

49. Dependent on the chosen financing, the parking options required in the town centre would attract a borrowing cost, as detailed in Table 6 below, which could be met from any surplus achieved from the rental income. The borrowing has been assumed over a 30 year period:

Table 6 – Financing of the Parking Schemes

	Parking
Borrowing	1,879,890
Capital receipts and reserves	585,850
Total Financing	**2,465,740**
Annual Cost of Borrowing	**89,210**

50. There is a potential further receipt of overage dependent on the result of ongoing discussions with the developers.

51. As stated in the report to Council on 23rd January 2018 the council could expect approximately £5.2 million of overage. This is £2.8 million more than assumed in the financing figures above. If the full £5.2 million is received it could replace borrowing assumed to finance the parking schemes. This would eliminate the £89k borrowing costs outlined in Table 6 and result in the council receiving the surplus outlined in Table 5.

IMPLICATIONS OF REPORT

52. This report has implications in the following areas and the relevant Directors' comments are included:

Finance	X	Customer Services	
Human Resources		Equality and Diversity	
Legal	X	Integrated Impact Assessment required?	
No significant implications in this area		Policy and Communications	

COMMENTS OF THE STATUTORY FINANCE OFFICER

53. The report focuses on the cost to deliver the development and the financial return that it could generate. In terms of net distributable income there are two main factors, cost of borrowing and rental income.

54. The cost of borrowing is very important and the use of existing resources can be used to minimise the borrowing and therefore the ongoing cost to the council. Members will need to consider what level of existing resources they are willing to commit to the scheme, in particular the amount of overage that should be applied. The financial modelling has been carried out on the basis that £2.3 million overage will be used to fund the scheme. However, there is around £5.2 million that could be available if agreed by developers.

55. If all the interested parties sign up to the scheme, i.e. Reel, Marks and Spencer and Loungers then the development should yield a surplus even if all other units remain vacant. The period until completion of the development provides an opportunity to secure further lettings which further reduces the revenue risk.

56. The net distributable income stated within this report looks solely at the development and associated development works. If the development proceeds there will be additional costs to deliver a town centre parking solution. There is around £586k identified for parking at Oak House from the reverse premium and if the remainder were to be funded through borrowing there would be a further cost of around £89k per annum.

57. There are options to commit further overage or capital receipts to reduce the level of borrowing required. However even with the maximum level of borrowing the subsequent deficit would not impact significantly on the councils overall deficit position. The most advantageous method of financing the project will be agreed at the time.

58. It should also be noted that the some of the cost appraisals, including the main build, are estimated and we will not know the final costs until a further tendering exercise is undertaken. In addition allowances have been made for future lease negotiations but again we may need to vary these in any final agreements. However, any negotiations can only be agreed within the cost envelope agreed by Council and should any of these exceed the amounts agreed then Council will be asked to consider any such requests.

COMMENTS OF THE MONITORING OFFICER

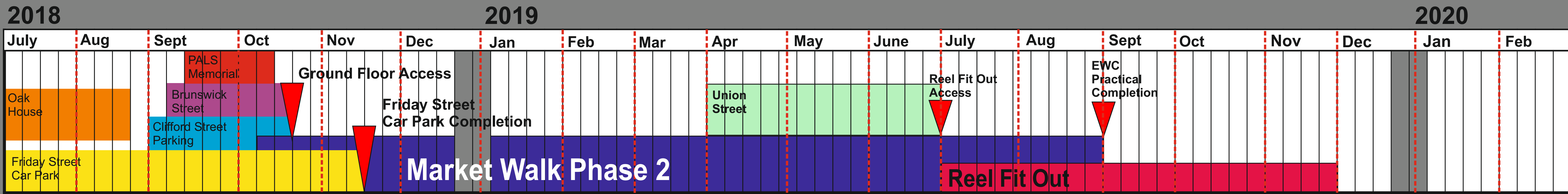
59. The project is being delivered in accordance with authorities granted.

GARY HALL
CHIEF EXECUTIVE

Background Papers			
Document	**Date**	**File**	**Place of Inspection**
Market Walk Update	23 January 2018	***	
Market Walk Extension – Award of Contract	25 July 2017	***	https://democracy.chorley.gov.uk/Extranet/ieListDocuments.aspx?CId=114&MId=5711&Ver=4&LO=1
Urgent Commissioning Works: Market Walk	30 August 2017	***	https://democracy.chorley.gov.uk/Extranet/documents/s78219/Urgent%20Commissioning%20Works%20Market%20Walk.pdf?LO=1
Urgent Commissioning Works: Market Walk	11 October 2017	***	https://democracy.chorley.gov.uk/Extranet/ieListDocuments.aspx?CId=112&MId=6215&Ver=4&LO=1
Market Walk Update	21 November 2017	***	https://democracy.chorley.gov.uk/documents/s80660/Market%20Walk%20Rpt.pdf

Report Author	Ext	Date	Doc ID
Mark Lester	5571	13 July 2018	***

Market Walk Chorley : Phasing : Option A



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Motion to Council.

Following the 2018 Report, *Living with the Normal*, produced by Deloitte Hoskins in which they give a stark warning of significant reductions in the valuation of shopping centre assets and a bleak outlook for those owning these assets. It is requested that the Council write to Deloitte's, as our original advisors on the scheme, requesting the following:

1 That the Council be provided with an up to date valuation of the current Market Walk.

2 That the Council are provided with forecasted projected income levels and property valuation for the existing Market Walk development based on 2020 and 2024.

3 That the Council are given similar projections and a comprehensive viability report before any decision to progress further with the development of phase 2 is considered.

Proposed by Cllr Alan Cullens

Seconded by Cllr Martin Boardman

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Deloitte.

Living with the New Normal
The clock is ticking for UK secondary shopping centres

Restructuring

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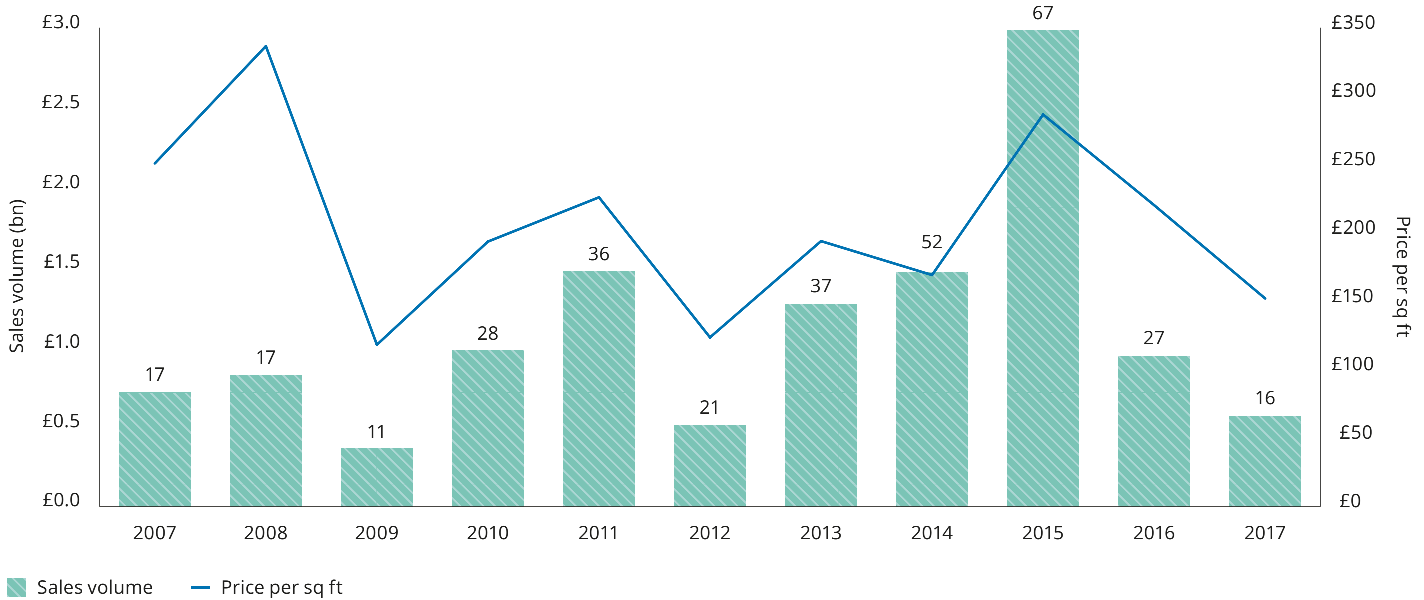
Living with the New Normal

The best things in life are worth waiting for, or so the maxim runs. However, the UK's shopping centre owners, and their lenders, should be careful. In many cases they are waiting for an upturn in fortunes that will never come: many centres are beset by flat or declining revenue, increasing costs and thinner margins, and a high risk that all attempts to reverse this will fail. This reflects not merely the particular problems of individual centres, but commercial problems for shopping centres as a whole.

Transaction volume by year
Label indicates no. of shopping centres transacted



Responding to these problems, owners and lenders must make a realistic appraisal of a centre's prospects, utilising all available asset management initiatives and exit routes. They need to do this now, before the deteriorating prospects of the country's schemes depress asset prices further – the average sales price per square foot has already plummeted from almost £300 in 2015 to little more than £150 in 2017. Optimists may regard this as an Uncertain Interlude, but we think owners and lenders must instead open their eyes and accept that there is a New Normal for the sector, which is much less benign than what they have been used to.

Having said this, a small group of super-prime sites – about 50 to 70 of the country's 1,400 or so shopping centres – are performing well. They attract the highest-quality anchor tenants because they have higher footfall, which makes the centres attractive to other high-quality tenants that can afford expensive rents. An example is the new John Lewis store that anchors the extension opened in March 2018 at Westfield London, the largest shopping centre in Europe. These super-prime sites usually have vacancy rates of zero, or close to it. Some prime centres outside this small circle are also performing well, supported by excellent anchor tenants and leisure facilities, such as cinemas and bowling alleys, which make them go-to "experience" destinations.

To a degree, the more poorly performing prime centres, together with many of the country's secondary and tertiary sites, are performing badly because others are doing well. The sector divides shopping centres into these different categories, based on a combination of size, sales/rental value per square foot, age and general attractiveness, because each category behaves differently. The super-prime centres are taking market share within the shopping centre universe away from smaller and less prestigious schemes.

Squeezed retailers, squeezed consumers

Shopping centres as a whole are suffering at the hands of e-tailers, and of out-of-town retail parks that boast the advantages of easy parking, ample space and, in many cases, proximity to a leisure offering.

Other supply and demand factors are affecting the UK retail landscape as a whole. Business rates and rents have risen in London and many other parts of the country. Wage bills have grown faster than usual, because of the 2016 introduction of the National Living Wage for people in their mid-twenties and above, and the introduction of the apprenticeship levy a year later. The fall in the pound since the 2016 vote for Brexit has raised the cost of many goods imported by retailers.

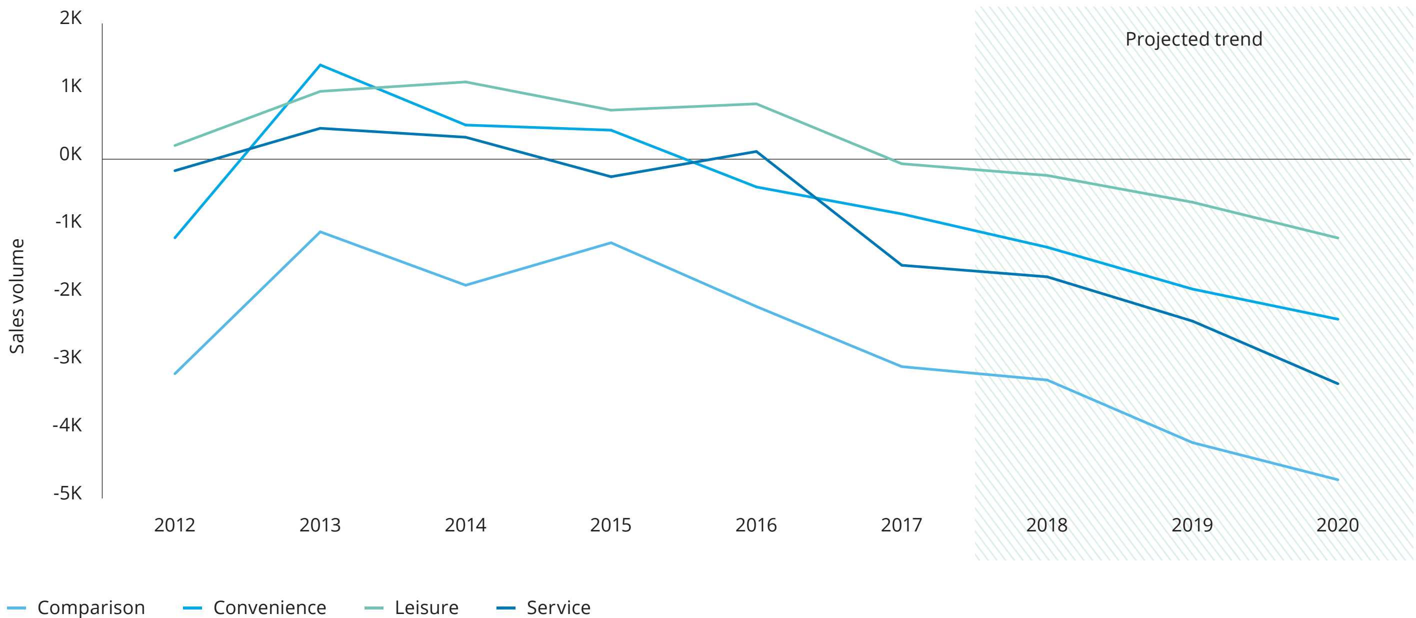
From a demand perspective retailers' revenues have also been hit, because the pound's fall has squeezed consumers too: depressing their real incomes by boosting consumer price inflation. In addition, the political uncertainty caused by Brexit has further weakened consumer sentiment, and a tightening of consumer credit is reducing their ability to spend. The challenge has been especially acute in casual dining, which in recent years has been used by asset managers to compensate for departing retail tenants. Belt-tightening in consumers is forcing restaurant closures in a sector that had rapidly over-expanded, often under private equity ownership.

Belt-tightening in consumers is forcing restaurant closures in a sector that had rapidly over-expanded.

Decline and fall

This general malaise in retail and casual dining has played out in a very different way in different types of shopping centres. Using Creditor Voluntary Arrangements (CVAs), companies have cut outlet numbers, usually by closing those located in secondary and tertiary centres while keeping outlets open in prime and super-prime sites.

Net store closures: actuals to 2017, and forecast 2018-2020



Comparison | Convenience | Leisure | Service

Shopping centre owners have responded creatively to their troubles, and some have succeeded in turning around their fortunes. But many have not, against the backdrop of widespread store closures in a troubled environment for consumer spending. Deloitte has analysed information on closures of all consumer-facing outlets from the Local Data Company – casting the net wide to include not only shops but also businesses such as restaurants, pubs, petrol stations and estate agents.

Our research finds that 429 more outlets opened than closed in 2014. But the following year saw 338 net closures, and by 2017 5,493 more outlets shut than opened. Based on the recent trend, Deloitte predicts that between 2018 and 2020 UK retail will see 27,000 net store closures.

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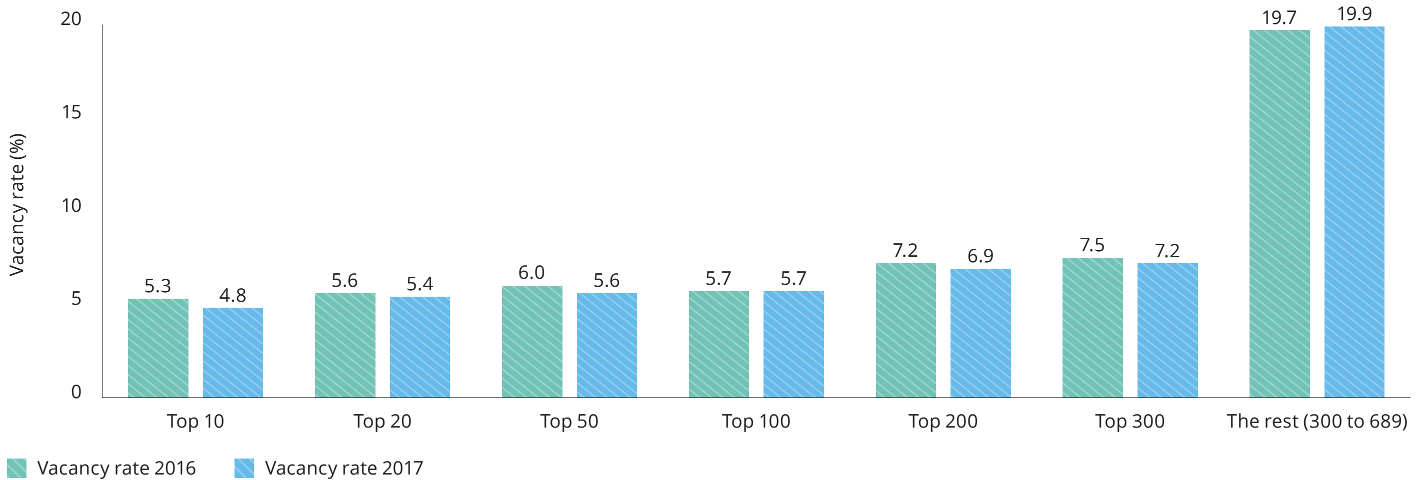
Shopping centre vacancy rate by Health Index rank across GB



Source: LDC

Because of these closures, we predict that average vacancy rates in secondary shopping centres will rise to more than 25% by 2020. Data from LDC's latest Retail and Leisure Trends report shows that according to their Health Index barometer, more than half of the 689 shopping centres included in their review already have vacancy rates of 19.9%. Back in 2017, the LDC reported an average vacancy rate of 12.6% across UK shopping centres. Some secondary and tertiary centres are already closing, as property companies streamline their portfolios.

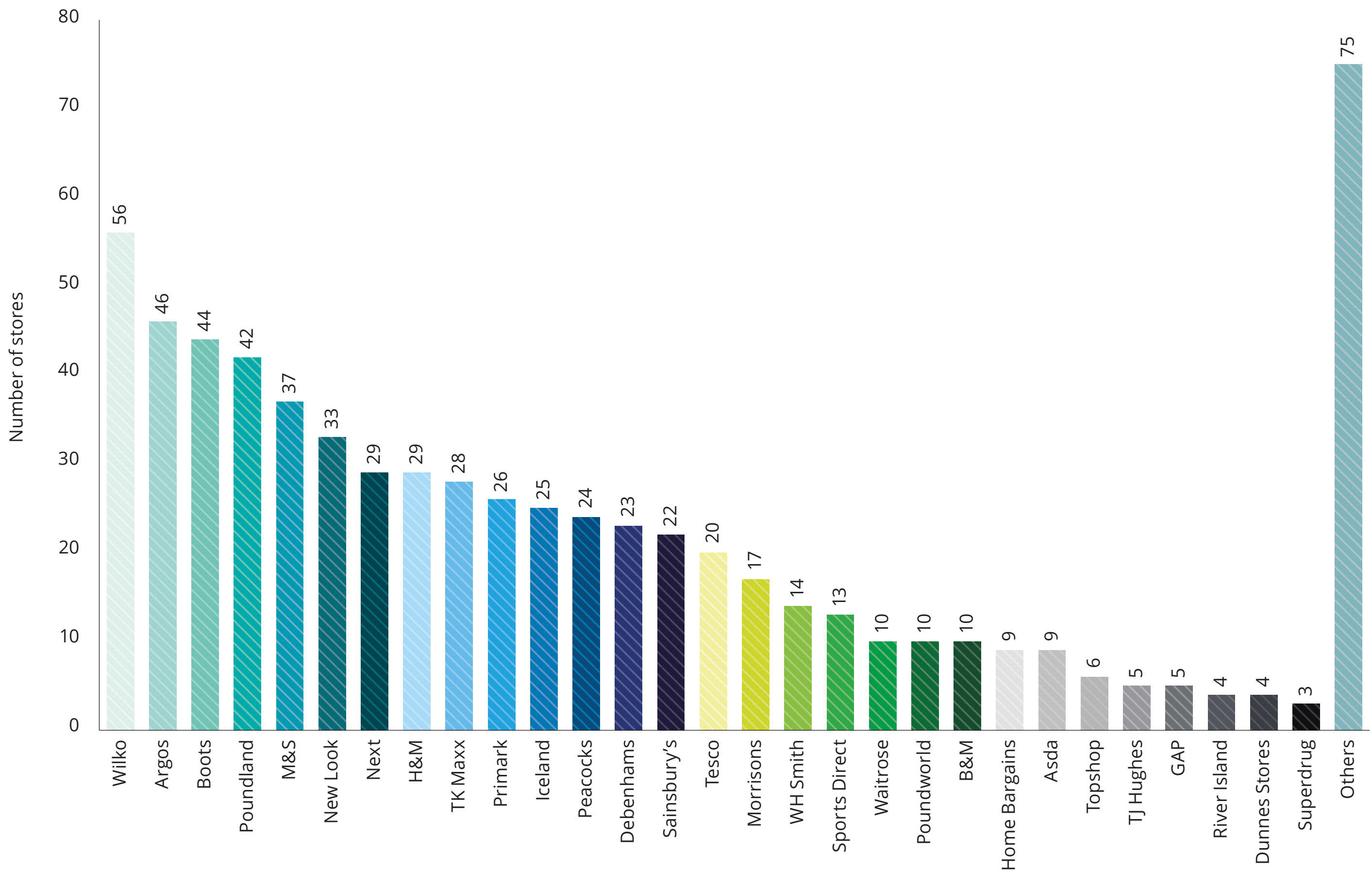
A specific problem lies with anchor tenants. Our analysis suggests that secondary and tertiary shopping centres are increasingly dependent on a dwindling pool of core anchor occupiers, many of whom are publicly reviewing their portfolio of stores.

Moreover, the sector is especially sensitive to the failure of large, multiple retailers. On top of this, it is suffering from the steady attrition of units, as occupiers across the spectrum of general retail face up to their own particular online disruptions by downsizing their portfolios – emptying the rental income bucket faster than hard-working asset managers and agents can refill it.

For owners and lenders assessing the risks to their assets, it helps to consider how the face of decline tends to look. First of all, a highly desirable anchor tenant, which brings in affluent customers, leaves because of disappointing local performance or corporate crisis: classic examples are H&M's recent round of closures, and the 2016 failure of BHS.

The space is filled by tenants, such as discount retailers, which sell lower margin goods and are less likely to attract shoppers who spend money on high-margin goods. Other tenants respond to the diminished commercial opportunities by exiting the centre. The owner tries to fill the vacated space with low-rental booths and even lower-rental market stalls, cheap gyms and other tenants that provide much lower income. After a few years the asset has a 40% vacancy rate, a string of charity shops paying no rent, a leaky roof without the rental income to mend it, and negative income because capital expenditure and operational costs are higher than rents.

Top "anchor" tenants in secondary shopping centres transacted 2007-2017

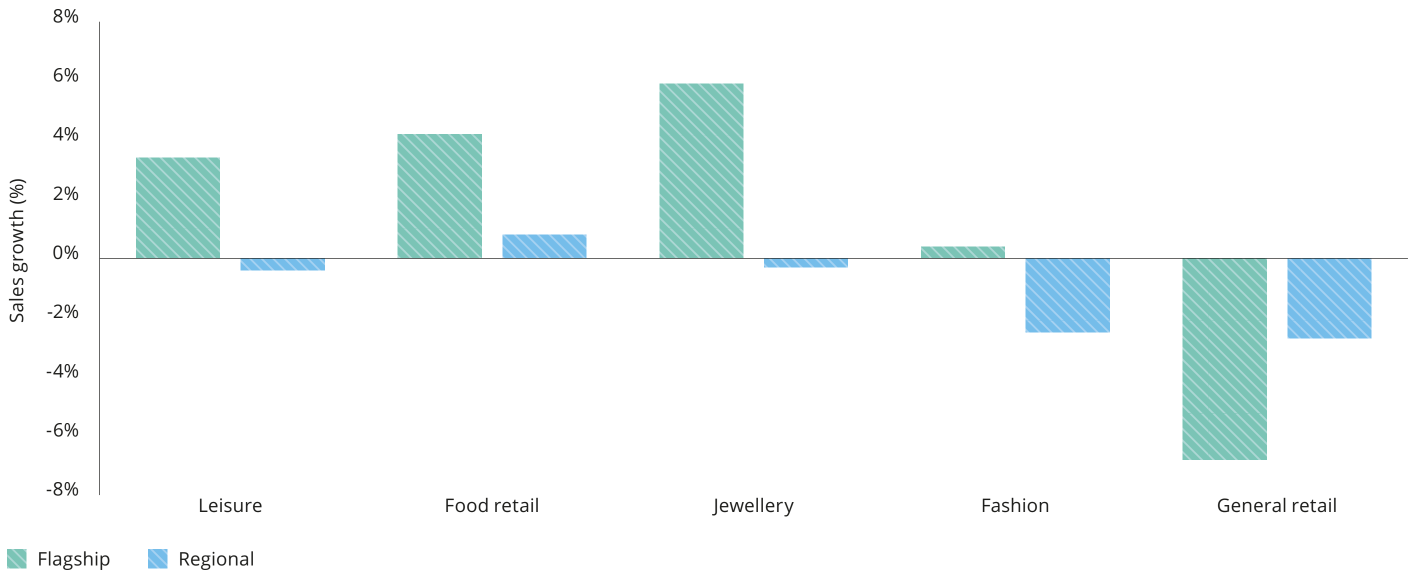


Six of the top eight "anchor" tenants have publically announced restructurings of their store portfolios resulting in a downsizing of their UK footprint. The restructurings range from a staggered exit from leases upon expiry to the more drastic use of CVAs where, in some cases, retailers are almost halving their store numbers.

Thinking widely and deeply
How should owners respond to this environment?

Owners need to evaluate the whole range of asset management strategies that can be applied to their particular shopping centre. These include an assessment of the additional operational and marketing costs, and above all the capital spending, that will be needed as part of any plan to rescue the asset from decline.

Speciality retail sales growth (full year 2017)



Source: Westfield 2017 financial results presentation

Installing a leisure facility, such as a cinema, may increase footfall (if the scheme allows), but possibly not enough to justify the large capital costs involved in remodeling the site. Taking on casual dining tenants may do little to increase footfall in an ageing centre that is an inherently unattractive place to spend time in. The very different contribution made by leisure to the health of different categories of shopping centre is shown by Westfield's breakdown of sales growth into flagship (prime) and regional (secondary) centres.

Doing this appraisal well requires a wide set of skills. These include not only financial analysis, surveying and asset management, but also people well-versed in development and planning.

Knowledge of development and planning is increasingly important because of the progressively more activist attitude of local councils towards shopping centre land. It is impossible to choose the best among all possible options, without knowing the council's overall strategy for its district. Factors include the desire for shopping facilities that bring commerce within its borders, and its needs for affordable and other residential housing. In the New Normal of hard times for shopping centres, knocking down the asset and using the space for housing may be an attractive exit route for owners, and a housing solution for local authorities.

But while in London and most of the south-east there is a housing shortage, many parts of the north of England and Scotland are suffering a surfeit. This may explain why there have been so many sales of shopping centres in the south of England recently – and at higher prices and lower yields – compared with the rest of the UK.

Lenders need to make the same all-encompassing appraisal as owners, to maximise the recovery of interest and principal.

It also pays both sides, quite literally, to create a cooperative rather than hostile environment for distressed properties. To understand why this matters, consider two scenarios.

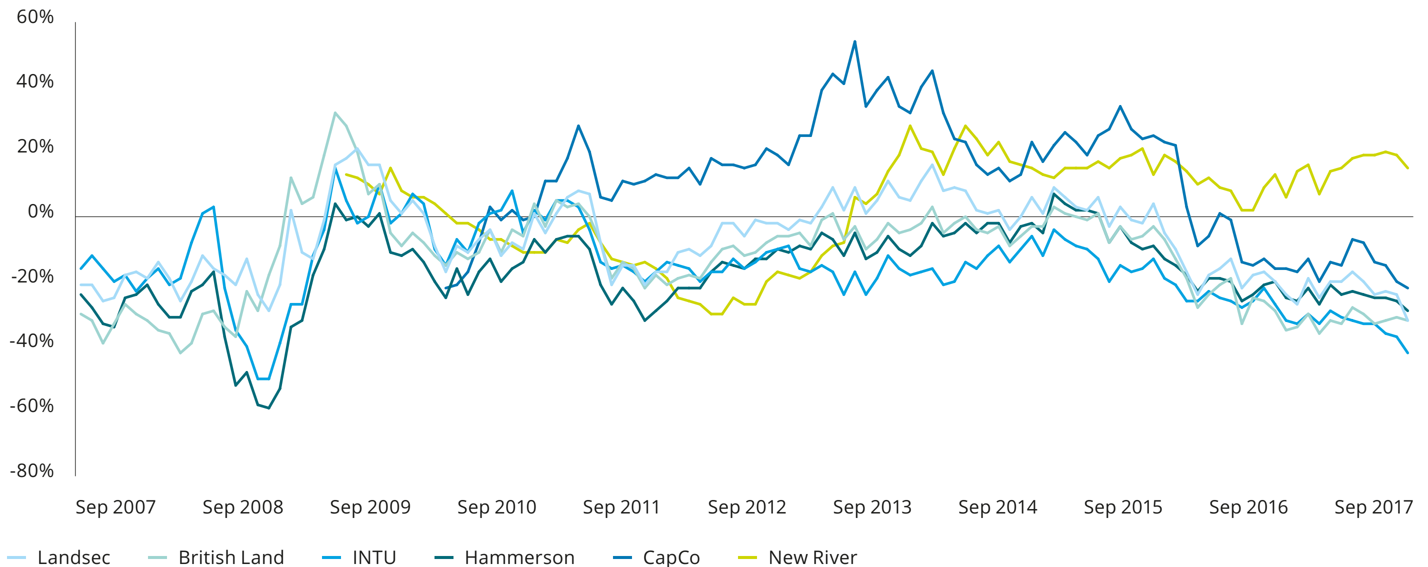
Scenario one is a hostile approach by the lender: enforcing the loan and taking control immediately, rather than trying to secure what it wants by seeking cooperation. The owner meets hostility with equal hostility, refusing to provide any information (such as tenancy schedules) that would help the lender work out a fair value for the centre to maximise the chance of a satisfactory sale.

The lender is also left with responsibility for managing the facility – a responsibility that will have to be passed on to an external management company. The paucity of data also increases the risk that a sale will fall through or that price chips – a whittling down of the sales price – will happen at the due diligence stage, when the buyer discovers nasty surprises. This is the "hard landing" scenario.

Transaction volume

Annual sales volume vs. yields achieved

In the above chart, each circle indicates the yield achieved for the centre transacted. The trend line indicates if yields are increasing or flat in the relevant region. The numbers on the bars indicate the number of transactions. The height of the bar indicates the total volume of all transactions in a year.



Source: Lazarus research

Scenario two occurs when the lender approaches the borrower peaceably, in the knowledge that, because of where the value breaks, it ultimately holds the power. The borrower provides all relevant data, and continues to manage the centre. In this atmosphere of collaboration, even if the lender eventually takes control of the asset, the former owner receives a management fee for continuing to run it. The process of selling the centre is made much easier, because of the ample information available to the buyer. This is the "soft landing" scenario.

During the last real estate downturn Deloitte was involved in many examples of distress within the secondary and tertiary shopping centre sector.

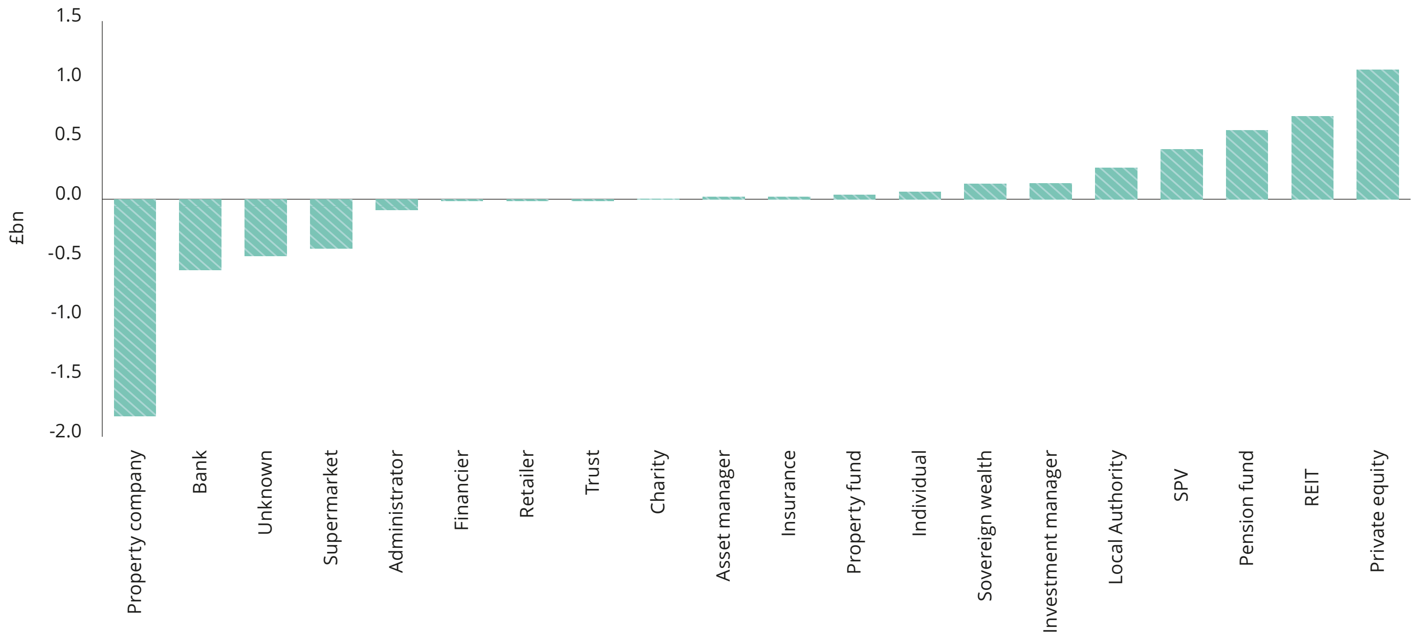
Key takeaways include (1) there needs to be a "gritty" and realistic approach to asset management, (2) a change to bring in specialist asset managers can provide real benefit, (3) be ready for a confrontational enforcement but co-operation with the borrower invariably delivers optimum returns and (4) access to up to date and accurate information is important to ensure financial valuation and forecast appraisals can be delivered swiftly to enable rapid decision making. Ultimately, asset owners must strike a careful balance. It is defeatist to assume that they can never turn around declining performance without uneconomic capital spending. But at the same time, they must be realistic about the prospects of their centre.

The pricing of Real Estate Investment Trusts in the public market suggests that many investors in property companies are already pricing in this downbeat assessment. Many REITs trade at a significant discount to NAV, revealing market scepticism about the long-term yield prospects of much shopping centre stock.

Failure to accept the New Normal

However, the evidence suggests that far from staring the New Normal square in the face, many owners are desperately trying to spy better times on the distant horizon. Owners have taken a number of asset disposals off the market after these failed to reach their asking price, and the number of schemes sold fell in 2017 to its lowest level since 2009. This suggests that many owners are not pricing their schemes realistically.

Net sales and purchase by entity type



Two recent examples illustrate this. Callendar Square centre in Falkirk, once valued at £26m in 2006, reportedly sold for £1m in October 2017. Abbeygate shopping centre in Nuneaton, once valued at £17m, sold for £4.3m in February 2018.

Understanding the New Normal should be a particular concern for the private equity firms that have snapped up so much shopping centre stock in recent years. Deloitte research shows that they have been net buyers of more than £1 billion-worth since 2007 – largely taking ownership from property companies, which have been net sellers of almost £2 billion.

Private equity firms have made these purchases in the hope of a sustained market recovery and improved occupier demand. But they have failed to find buyers for a number of their investments, with exit strategies frustrated by the market's perception that they are asking too much. A typical private equity response has been to refinance and wait for the market to improve. The flaw with this strategy is that, if current times prove to be the New Normal rather than an Uncertain Interlude before better times begin, the market will never improve markedly. This will leave private equity owners with a net internal rate of return that is very poor indeed.

It will leave yield-based investors such as REITs and pension funds, the second and third biggest net buyers, as owners of assets whose yields are gradually but in many cases inexorably trundling downwards.

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