

Coronavirus: impact of the crisis on East Sussex commercial property

Second report: July 2020

1. This second report draws on seven telephone discussions of varying durations (and thus detail) with the following categories of commercial property professionals: partners in two chartered surveying practices (a large practice covering Sussex and Surrey; the other primarily operating in Wealden); the landlord of a large diversified farm in rural Rother; two very experienced commercial developers with strategic business parks in East Sussex; a partner in a large commercial law practice, and the manager of a large managed-workspace facility with both office and workshop space in the west of the County. It is hoped that the wide scope of these discussions presents a picture of sufficient granularity to be useful to partners.
2. The main interviews took place between the 8th and 20th July 2020 – with several follow-ups to elicit additional information. The potential stages in the crisis we've mapped out are: *not enough information to say/steep decline/levelling out/starting to get better/good as it's going to get/back to previous norms*. The majority view is that the property industry is in the 'starting to get better' stage of the crisis but others were taking a more cautious approach with two (one developer and one agent) commenting that there's 'not enough information to say' and the diversified farmer reporting things were 'levelling out' – with impact on commercial property almost at its lowest point. He also added the rider that we are not through the crisis yet and predicts a delayed effect with some businesses that have struggled through so far needing additional support to survive on the way back out of the crisis. This however, is an improvement on the situation described in the previous report where consultees were unanimous in the view that there was *not information to say* what stage had been reached in the crisis. In short, there now appears to be some appreciation of a so-called 'new normal'.
3. One of the developers suggested that that the situation was 'improving' for 90% of his tenants because they now have an opportunity to trade and, as a result, his business park is now much busier, but has not yet reached the previous high. He comments that, for businesses that are not performing, the crisis will either hasten their demise or (through forcing them to make the necessary efficiencies to survive) would make them ultimately perform better in the future.
4. From the agents' perspective, one said that the next quarter – perhaps the next two – will be most interesting in terms of confirming where we are in the crisis. The outlook seems much more positive with businesses in the main 'trading better than initial forecasts might have suggested'. The main threat is another lockdown.
5. This agent reported that the pattern of demand remains the same as pre-Covid conditions (although not quite back at the same level) with warehouse/industrial in high demand although the market may well soften in the coming months as some existing businesses vacate their premises.
6. The other agent's experience is not dissimilar in that overall levels of enquiries are down – the phone is quieter than usual – but those enquiries that are received are serious and good quality and the practice is busy. Counter-intuitively, it is retail that is the busiest with

instructions from tenants who have given up during (but not because of) the crisis. Warehouse and industrial premises are also in strong demand, for which there are shortages previously noted in the June report. It should be stated, however, that the areas where the two agents canvassed here operate have at least some new business space available.

7. It is clear that landlords just don't want motor trade and there are a lot of enquiries in this category. This is a conclusion that chimed with the lawyer's comments on the lack of space availability particularly for 'dirty or noisy' industrial uses.
8. The commercial legal practice we canvassed has been, after a slow start in the early lockdown period, very busy indeed. This has resulted in all staff in the department having high workloads – none have been on the furlough scheme – with those solicitors dealing with residential having ridiculously high levels of work. The partner we spoke to stated that residential instructions are up over the last couple of weeks to a level even beyond that of last year: 'it is as if buyers are now making up for lost time'. It must be supposed that the temporary reduced rates for stamp duty will further feed this frenzy. He has had an influx of instructions for business units (industrial and warehouse) and deals have continued to be done over the period of lockdown. There has been some activity in retail, even in those sectors (such as beauty) which government restrictions at the time prevented from opening.
9. By contrast, he reports the office market is very quiet (no deals reported) and the hotel sector is depressed. Both agents also confirmed that the office market is considered very tough at the moment for obvious reasons, although one said that this has just accelerated an existing trend.
10. Conversely, the business centre manager reported that she is now receiving enquiries as normal – or perhaps at a level that is a little higher than before the pandemic. She explained that the cyclical pattern of enquiries that repeats throughout the year is unchanged, although it damped down a little during the lockdown. She noted – as is often the case with these facilities – that if she has workspace space available, the demand will be for offices and vice-versa!
11. One chartered surveying practice confirmed that the situation still pertains, as outlined in the last report, where larger companies are reported to be more reluctant to commit to investment. The situation has evolved from the June report in that the previous uncertainty caused by the unknown future operational requirements for coronavirus has been factored in to decision-making because it's now thought that social distancing will remain de rigour. The uncertainties now surround large exporting companies which are exercised by the increasing possibility of a no-deal Brexit.
12. The impact of coronavirus on the market – with premises left vacant because of an inability of businesses terminally affected by the lockdown to pay rent – was not clear at the June 24th Quarter Day. This did not have huge implications because fixed staff costs continue to be mitigated through continuation of the furlough scheme until 31st October. The ban on evictions, which has been extended to at least the end of September, also meant that no enforcement action could be taken against landlords not paying rent. The next pressure point will be September 29th Quarter Day when tenants will be expected to pay rent in advance and support measures end.
13. None of those canvassed reported significantly increased vacancies as a result of coronavirus. One agent reports a marginal increase in vacant premises, but nothing in reality has changed

as the 50,000 ft² Connect 27 development has reached practical completion and is on the market – thus increasing supply and affecting data that his practice collects. The diversified farmer has 100% occupancy. The other agent who operates in Wealden reports a rise in vacant premises but this is not linked to coronavirus as these are changes that were happening anyway.

14. The business centre was kept open throughout the lockdown period although centre staff essentially worked from home. There were some losses of tenants in early March although this was not down to coronavirus as the manager had advanced warning that they were going to leave anyway. The direct impact of coronavirus is that some wanted to downsize to reduce costs and some upsized as they needed bigger premises to socially distance. In terms of occupancy, the centre was 99.9% full in 2019 (one unit available) and during lockdown this went down only to 85%. Now it is back to the late 80% - early 90%.
15. It appears that tenants are split into various camps as to whether they pay or withhold rent. From a commercial lawyer's perspective who represents both landlords and tenants, it seems that plenty of (mostly) smaller, tenants are not paying rent and he is aware that some landlords have (inadvisably) threatened legal action, which has only served to worsen relationships at a time when there has been a moratorium on evictions, so there is little that can be done through legal channels. Taking legal proceedings would normally be at the top of their list of remedies, it is now at the bottom! This is also why most tenants in trouble are not handing their keys back at this stage. He said that a more conciliatory approach better serves their interests, potentially paying dividends in the future. His assessment is that about 40% of payments were late at the last Quarter Day (24th June). Many of those tenants will have had the cash available to pay but are withholding rent, playing safe by banking it as a contingency for an uncertain future.
16. It was reported that some tenants were looking for help in terms of rental holidays. Some landlords have offered help: indeed, one landlord contacted all his tenants to unilaterally halve rents over that period and wouldn't need paying back (even though it seemed that one tenant wanted more!).
17. Landlords have reported taking various measures to mitigate the difficulties tenants are experiencing. One of those canvassed, who has developed out and manages a strategic business park, says that he has accommodated tenants by delaying payments in some cases. Some tenants were paying monthly not quarterly in advance and in other cases deferred payments were added onto future instalments. None of these businesses had gone under so far (although tenants keep their cards close to their chests).
18. This experience is borne out by the diversified farmer who went around all his tenants early on to see if were coping with the crisis. The great majority have got through so far, although a third of his tenants have not paid rent on time. All of these businesses are quite small and flexible, have taken advantage of the furlough scheme, and continue to operate. Only one of his tenants, who couldn't trade owing to government restrictions, is not in a position to pay rent so instead has spent the time improving his property in lieu of rent. Such flexibility on both sides is necessary in this situation. It should be said that his industrial tenants are reasonably busy with businesses doing quite well but not 'rock solid'. For example, the woodworking businesses have found difficulty in getting a supply of raw materials. Only a couple of his tenants still have to pay business rates, and he made the comment that the relief should also apply to them.

19. Landlords who have had to carry a lot of debt as a result of the crisis face pressure from their lenders and one agent made the point that, at some point, those tenants who owe rent will have to pay it back. The diversified farmer noted ruefully that, with some rents 2-3 months late, his cash flow is not brilliant.
20. One agent said that retail occupiers are capitalising on incentives such as lower rents or rent-free periods, which accelerates a trend that existed before coronavirus, however, other commercial rental levels are unaffected. He went on to say that coronavirus had only affected lease terms to the extent that shorter leases were more common as businesses wanted maximum flexibility but, again, coronavirus has only accelerated existing trends. The other agent that operates predominately in Wealden reported that he is seeing some flexibility in new leases as a result of coronavirus. One of the innovations has been break-clauses that are triggered by lockdown. The lawyer said that a few tenants are having a go at negotiating coronavirus terms, such as a rent-free period on new leases or lease renewal.
21. One of the developers told us that he is being more selective than hitherto about tenants taking space at his business parks. He is receiving a good volume of enquiries but has to feel confident that they will fit in (no messy car-related uses allowed) and that any tenant will be able to meet the not-inconsiderable financial commitment required to lease a unit; he therefore scrutinises businesses closely to ensure that they can pay.
22. The June report stated that commercial development was on hold but the situation now appears to have evolved to some degree, with some evidence that business confidence is sufficient for new schemes to be considered and existing schemes to be finished. For example, one developer is cautiously undertaking works to make the final phase of his site ready for development, although he would need to feel more confident to start erection of the new buildings. His rationale is that no-one has any idea what will happen in the property market for the 'next two or three months' as a second spike of coronavirus and a no-deal Brexit are two unknowns. The diversified farmer still has planning permission to develop more floorspace but has not yet got the business confidence to build this out.
23. In last month's report one of the agents suggested that if commuters can't or won't go into London by public transport, they will want local offices to go to rather than suffer the inconveniences of working from home. The diversified farmer echoed this thought and pointed to a potential for large companies to set up satellite offices in rural or small-town settings where, instead of travelling to London, commuters can instead travel to their place by car or bicycle and benefit from a pleasant environment, easier parking as well as shorter journey times (providing of course that there is a cluster of employees that live in the area). We know that satellite offices are one option being considered by large London-based employers that are reconsidering their property strategy in the light of the coronavirus crisis.
24. Whilst this would seem to provide an opportunity for business centres to respond by providing commuters with flexible office space, the business centre manager interviewed said that her client base is unchanged although enquiries about virtual offices might have picked up a little more due to coronavirus.
25. As an interesting aside, one of the agents acting for some of the big occupiers in Crawley was asked how recent announcements about job losses there will impact on the East Sussex commercial property market (through making competing space available). Whilst much of this is confidential, he said that these announcements affecting airside operations should not necessarily be conflated with commercial property in the town, where positive development

deals are still being done. The bottom line is that events in Crawley will, in his view, have zero impact on East Sussex's commercial property market.

Michael Cogswell
Locate East Sussex
24th July 2020