LOCATE EAST SUSSEX

Coronavirus: impact of the crisis on East Sussex commercial property

Third report: September 2020

1. The interviews were conducted between the 9th and 16th September. As August is generally seen as a quiet month in the commercial property market the decision was taken to default to September (there is no August report).

2. For the first time the interviews included a partner who heads up the retail and leisure department of a large chartered surveying practice, providing specialist information for that sector. A managing agent with a portfolio of about 30+ commercial premises in Wealden, and partners in two chartered surveying practices were also interviewed. They took place before the recent spike in coronavirus infections which may well be affecting perceptions going forward, especially as previous respondents have said that the prospect of another lockdown would be very disruptive.

3. Asked 'where are we in the crisis?' it became clear from responses that there is a fragmented market and the impact is (property) sector specific. With different commercial property sectors faring better than others, perceptions vary according to respondents' involvement in a specialist property area. That being said, the majority view from this round of interviews is that as yet 'there is not enough information to say' with the uncertainties affecting retail, leisure and offices – and the impending discontinuation of the government's furlough scheme – affecting perceptions of most respondents. However, all agreed that the market for 'sheds' (warehouse and industrial) is strong.

4. One of the agents, an industrial specialist, suggests that in his sector the impact of coronavirus has ceased to be an issue and essentially business is 'back to previous norms'. Having (in his words) 'got through Covid', a bigger worry now for medium-sized companies is the implications of a no-deal Brexit. This is freezing decision-making on property moves as these companies now consider how to deal with international supply-chain uncertainties. This is what he has hitherto been reporting in relation to some large companies i.e. iro 100,000+ ft^2, which he says have now dealt with the situation by taking premises in mainland Europe. Smaller companies continue, as before, to get on with trading 'in the moment'.

5. In retail the current position is that there is are two main, highly differentiated markets: the prime market has gone, with national occupiers 'retreating into their shells' whereas the secondary and tertiary retail markets have been 'going strong' throughout the crisis. The dynamics of the two sectors are quite different as we shall see.

6. The prime retail market, essentially national occupiers in main high-street locations, has faded and the A3/A4 market is also really suffering. This prime market is now characterised by occupiers on turnover based rents, with incentive packages from landlords having gone up to include 12-18 months rent-free contributions on 5-year leases. Some 50%-60% of new tenants prefer capital contributions for shop-fitting out works, rather than rent-free packages. This helps with cash flow and ensures that occupiers are not eating up funding put aside for contingencies. It is predicted that prime retail will get worse over the coming months.

7. In contrast, the secondary and tertiary retail markets have been performing strongly throughout the crisis and in fact, the agent we interviewed has not lost any deals over this period. Rents are essentially where they were pre-Covid and local A3 and A4 also remains strong.

8. The government's Changes to the Use Classes Order in England (from September 2020) has been generally positive, and examples were given of planning use changes to enable childcare facilities (formerly D1). This makes things more flexible for businesses as there is not a 12 week wait to get planning (or not) which can be difficult when certainty is required and, in these conditions, there is a commercial imperative to move quickly.

9. Vacant premises are up in number but not as much as might have been imagined would be the case. It is predicted that prime locations will see more availability until landlords fully understand the 'new norm' and the importance of incentives. However, the situation in Sussex is not like London where huge swathes of property is vacant. In local communities, the secondary and tertiary market has been buoyed by office workers staying at home and using local stores. Food retail remains heavily contested by national operators as this sector has remained relatively unscathed by the crisis but also smaller stores like Londis have entered the frame.

10. Patterns of demand have changed in that good enquiries, with the strong covenants that landlords expect, are down.

11. Net take-up is up and the secondary and tertiary segments of (for example) Eastbourne retail is very busy and letting much better post Covid-19 than before the pandemic started! The explanation is that the Business Rates Retail Discount has been increased by government to 100% and relief extended to include occupied retail, leisure and hospitality properties in the year 2020/21 (there is no rateable value limit). This, coupled with rent-free periods of about 3 months in secondary or tertiary means that occupiers can effectively set up their businesses without two of the main fixed property costs. The other reason why the tertiary market is unaffected is that redundancy payments are being spent on setting up businesses (as shopkeepers).

12. The property lawyer interviewed in July also pointed to activity in retail, even in those sectors (such as beauty) which government restrictions at the time prevented from opening.

13. All respondents agreed that the office sector is the weakest and its prospects are unknown. It has suffered the largest increase in vacant premises with companies, in the words of one surveyor: 'dumping office space'. However, one of the agents predicts a resurgence in 2021. He considers that when the weather breaks, the prospect of another year of home working will be considerably less appealing.

14. Reaction from agents who commented to the government's Changes to the Use Classes Order in England (from September 2020) has been generally positive, with the greater flexibility helping the high-street to evolve.

15. Interestingly, commenting on changes in patterns of demand, one agent said that, in normal times, the summer holiday period in July and August is usually very quiet, with the market waiting for September and October to wake up again. This year, the reverse has been true as the market has been sitting on its hands, looking for reassurance in what the future holds

with furlough ending shortly and Brexit related uncertainties. This is not thought to be a universal view.

16. Another commented that the industrial/warehouse market is essentially back to the normal levels that would be expected for September pre-Covid. Other factors contributing to this demand are leisure uses (gyms, childcare etc) in industrial/warehouse premises that have been enabled by the new planning regulations, and also companies supplementing or moving out of traditional retail into internet sales which has translated into demand for warehousing to fulfil online orders. The need to socially distance in the workplace has increased demand for larger premises.

17. The retail specialist said that the number of vacant premises is up – but not as much as might have been imagined. In local communities, the secondary and tertiary market has been buoyed by office workers staying at home and using local stores, together with the Business Rates Retail Discount. Food retail remains heavily contested by national operators and small local food stores have prospered.

18. Changes in leasehold terms as a result of the crisis include shorter, more flexible leases, and some occupiers are demanding break-clauses linked to another Covid lockdown – which landlords are resisting. There was unanimity that rents are unchanged although the retail specialist pointed to a market which was characterised by incentives in the form of rent-free periods or capital contributions.

19. There were various views as to the likelihood of rent being paid on time for the September Quarter Day (29th), which again varied according to the market segment respondents operate in. One agent predicted more business casualties but the agent specialising in industrial/warehouse was not concerned. The retail specialist said that landlords are expecting tenants to pay rent as they now have a period of trading under their belts since non-essential businesses ended the lockdown phase on the 15th June and he predicts 60%-70% of rents will be paid on the due date this Quarter. The local managing agent is cautiously optimistic that payment will be 100% in September. It appears that occupiers are now paying monthly rather than quarterly in advance to mitigate the effects of reduced cashflow.

20. There is evidence that the development market is unfreezing with some interest in East Sussex sites from external development companies.

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