UK Commercial – Q2 2020

SPOTLIGHT
Savills Research

The initial impact of Covid-19 on the retail and leisure market

savills

- Essential retail by assest class
- Foostore performance
- Convenience store resiliance
- Insolvency activity

> “Savills Research estimates that in the week following the beginning of the restrictions 73% of retail and leisure operators from across the whole of the UK were classified as ‘non-essential’ and were required to shut.”

Government imposed business and venue closures

A Cabinet Office mandate determines which retail and leisure operators must close and which can continue trading

In the weeks following the government imposed strict social distancing measures and with the majority of the UK’s public urged to stay at home, what was the immediate impact on the nations retail and leisure industry? Did some sectors show more resilience than others? Does this continue to be the case as some retailers begin to re-open stores?

In this report we look at what type of retail locations had the highest proportion of essential retailers after the government imposed sanctions, and which therefore experienced the lowest trade and rental shock in the month following. We also examine whether out of town supermarkets are the biggest winners (or the smallest losers) in the immediate aftermath, as well as the strength of small format convenience stores in serving the needs of the consumer during the pandemic.

On the 23rd March the government stepped up its measures to prevent the spread of coronavirus and ordered that a large number of businesses and venues throughout the UK closed and remain so until further notice.

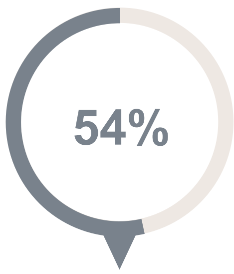
This had a dramatic effect on the nations retail and leisure industry with shops, restaurants, pubs, bars, hotels and cinemas all shutting their doors overnight alongside other institutions and places of public assembly such as libraries, community centres, places of worship, museums and outdoor recreation space.

Despite these stringent new restrictions the government made a number of important exceptions and issued a list of ‘essential retailers’ that were allowed to stay open in order to keep the public healthy, fed and properly sheltered, as well as keep the country’s key workers mobile and able to get to their place of work.

These essential retailers included supermarkets and other food shops, food delivery and takeaway services, pharmacies and chemists, opticians, off-licences, corner shops and newsagents, petrol stations, bicycle shops, home and hardware stores, launderettes and dry cleaners, car garages and MOT services, vehicle rental services, veterinary surgeries and pet shops, post offices and banks and building societies.

More and more businesses look set to re-open in the coming weeks, albeit not necessarily at their full capacity as social distancing measures are put in place that restrict the typical flow of consumer trade. However in the month immediately following the government sanctioned closures and with the essential retailers in mind, what was the actual impact of Covid-19 on the UK retail and leisure market? How much of our retail landscape remained open? Conversely, how much of it closed? How did this vary across different asset classes and how has this manifested in the recent insolvency activity we have seen as a result of the pandemic? This report will crunch the numbers and provide some clarity on the situation the UK’s retail and leisure industry found itself in at the end of March, the basis from which we are currently witnessing the early shoots of trade reactivity.

A quarter of all UK floorspace remained open via the out of town retail market



More than half of all retail floorspace left open and trading was in the out of town retail sector

Source: Savills Research

27%

of the UK retail and leisure market was eligible to remain open in the weeks following March 23rd

31%

of out-of-town units remained open in that market in the weeks following March 23rd

19%

of high street units remained open in that market in the weeks following March 23rd

16%

of shopping centre units remained open in that market in the weeks following March 23rd

The essential retail market

The proportion of retailers left open for trade and the variation across different asset classes

Savills Research estimates that in the week following the beginning of the restrictions 73% of retail and leisure operators from across the whole of the UK were classified as 'non-essential' and were required to shut. Conversely only 27% of the UK retail and leisure market was therefore eligible to stay open which resulted in an uneven spread of trade across different asset classes. Figure 1b highlights that a third of these essential retailers were on the high street, whilst three fifths consisted of individual standalone shops or small shopping parades. On a unit basis out of town retail and shopping parks accounted for only 6% of what was left open, with shopping centres being the hardest hit accounting for only 2% of essential retail operations.

As a proportion of the whole of the UK retail and leisure market the figures looked bleak. Only 9% of UK retail was left open via the high street, 16% across individual shops and parades, only 2% for out of town assets and less than half a percent for shopping centres (figure 1a).

The closure of all but essential retailers due to Covid-19 is one of the most significant changes within the UK retail market in living memory. There is no denying that having only a quarter of the UK's shops deemed as essential and able to trade by the end of Q1 was devastating for the country's retail and leisure economy. On the surface it seems that the high street showed slightly more resilience than both retail warehousing and shopping centres in this initial phase, however context is everything; as a proportion of their respective markets out of town fared better with just under a third of all units remaining open in that market. High streets and shopping centres both had less than a fifth of their respective markets still trading (figure 2).

The early resilience in the out of town market is demonstrated further when analysing the figures by floorspace instead of by unit. Of those retailers deemed as essential, high streets accounted for a similar proportion by floorspace as they did by unit at just over a third (38%). Retail warehousing however accounted for more than half of all retail space open and trading at 54%, undoubtedly as a result of the larger format retailers considered essential, particularly foodstore operators, that typically take more space in the out of town retail market (figure 3b).

As a proportion the UK's entire retail and leisure footprint again the retail warehousing market came out on top. A quarter of all UK floorspace remained open via out of town, 17% across high streets and as little as 2% for shopping centres (figure 3a).

Analysing each market separately (figure 4) highlights how as much 61% of retail warehousing floorspace was designated as essential, whilst for high streets it was just under a third and shopping centres a quarter of their total UK floorspace.

Figure 1: Essential retailers by asset class as a proportion of (a) all UK retail and (b) essential UK retail only (by unit, as of March 23rd)

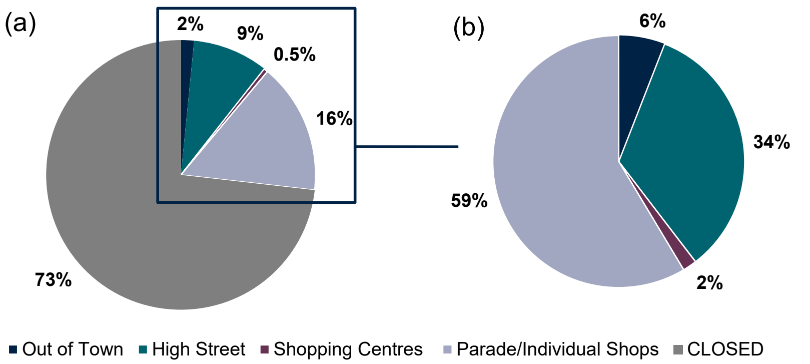


Figure 2: Proportion of each market that is deemed essential (by unit, as of March 23rd)

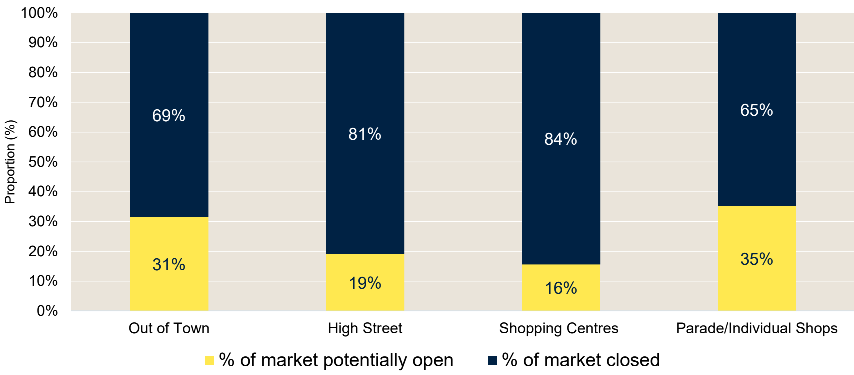


Figure 3: Essential retailers by asset class as a proportion of (a) all UK retail and (b) essential UK retail only (by sqft, as of March 23rd)

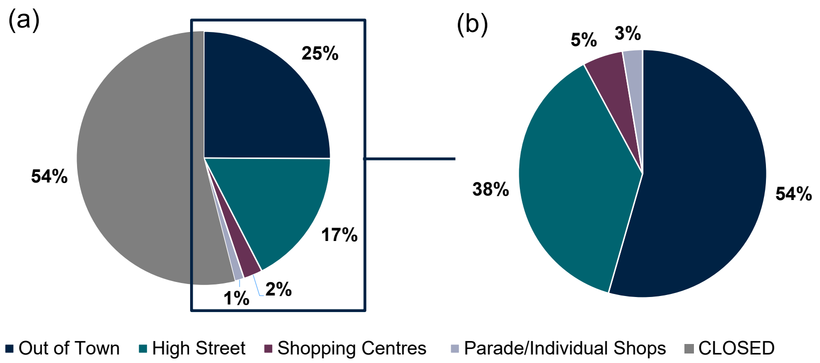
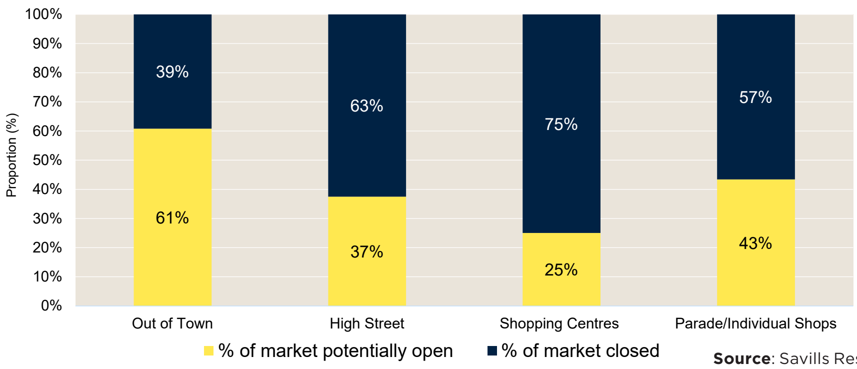


Figure 4: Proportion of each market that is deemed essential (by sqft, as of March 23rd)



Source: Savills Research

DIY essential retailing issues

Not all essential retailers had the capacity to stay open at the beginning of lockdown

The practicalities of remaining open and keeping both staff and public safe from the virus proved difficult for some retailers, with the essential retailers in the bulky goods sector the most prominent example. DIY, home and hardware shops as well as equipment, plant and tool hire outlets were all included on the government's essential retailers list. What supermarket operators are to feeding the UK, home repair and maintenance retailers are to keeping people properly sheltered.

As a result most DIY and home improvement stores remained open for trade immediately after the measures were imposed, with sales in stores actually accelerating as people faced the prospect of increased time at home. Kingfisher (owner of Screwfix and B&Q) reported that sales increased by 38% in the third week of March compared with the same period in 2019.

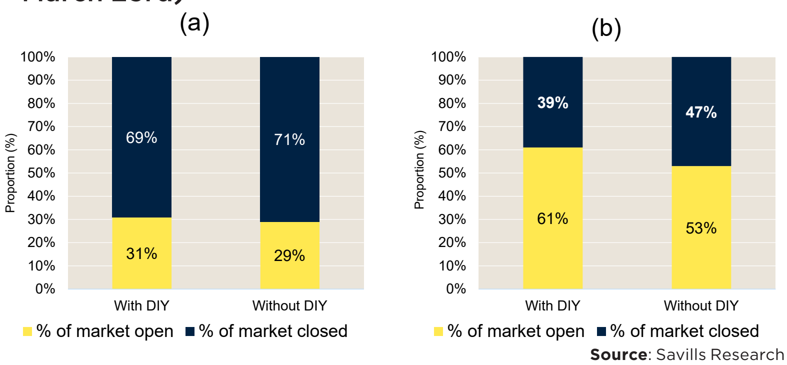
However, the difficulties faced by these retailers in their stores soon became apparent. DIY retailers typically occupy large stores and with staff levels inevitably dropping as a result of the virus, many operators struggled to maintain sufficient staff numbers on the shop floor.

Furthermore the sheer scope of goods DIY and hardware stores sell meant that many of their products fell outside of the 'essential' category meaning stores faced the prospect of having to rope off sections deemed to be selling 'non-essential' items such as bathrooms and kitchens. It's therefore perhaps unsurprising that in light of these factors, a number of major DIY and hardware stores took the decision to close, despite receiving government approval to remain open.

There seemed therefore to be a disparity between what was considered as essential and allowed to continue trading and what actually remained open after lockdown. Removing the biggest retail warehousing DIY operators from our calculations sees the proportion of essential retailers represented by the out of town market remain at 6% by unit but, perhaps more importantly, fall from 54% to 47% by sqft, owing to the scale of their store formats. In terms of the out of town market in isolation, without B&Q, Homebase and Wickes the proportion of retail warehousing that was allowed to trade versus what actually remained open falls from 31% to 29% by unit and 61% to 53% by sqft (figure 5).

However, even without the main DIY operators the out of town sector still displayed a greater degree of robustness compared to high street and shopping centres. In reality the degree of resilience this sector has shown lies somewhere

Figure 5: Proportion of the out of town market open with or without DIY (a) by unit and (b) by sqft, (as of March 23rd)



Source: Savills Research

between the proportion of retailers deemed as essential in the sector, following the closures, and the proportion who actually chose to stay open immediately after the government issued their advice.

This is evidenced in the fact some of the major DIY operators began reopening their stores in the last week of April, having had time to better equip themselves to cope with staffing and store configuration issues, as well as devise a strategy to meet with the unprecedented demand they saw shift to their online platforms immediately after their closures. B&Q had to temporarily shut down its website in the first week of April, whereas Wickes and Homebase customers were faced with lengthy virtual queues after their stores initially closed.

All of B&Q's 288 UK stores are now open to the public, albeit with strict social distancing measures in place. Since closing stores in March the retailer has made a staged return to trade, initially trialling their newly adopted safety procedures in 14 of their stores and subsequently rolling those measures out further, opening a total of 155 stores by the end of April. The desire to quickly implement measures that facilitate the reopening of stores, even if that means they won't be able to operate at their full capacity, highlights the importance of the store to sufficiently satisfy the consumer demand in this sector. The social distancing controls they have adopted are similar to supermarkets and limit the number of customers in store at any one time. Measures include two metre floor markers throughout stores, Perspex screens at checkouts and only accepting contact-less payments to avoid staff handling cash. Homebase have adopted a similar approach, opening 20 of their stores on April 25th in the first phase of their reopening strategy and opening a further 50 stores a few days later. By May 2nd Homebase had reopened all 164 of its stores.

Wickes have been slower to react having only reopened 6 stores by April 30th and all with reduced trading hours. They will need to follow suit and roll out further store openings in order to remain competitive. The nationwide store closures imposed on 23rd March have had a significant impact on sales at its parent company Travis Perkins Group with revenue in the first three weeks of April just one-third of what it was in the same period last year. Wickes however has proven slightly more resilient within the Group, owing to the increased demand as consumers looked to make home improvements whilst in lockdown. Online sales of paint, paintbrushes and paint rollers at Wickes increased dramatically in the third week of March by 180%, 238% and 193% respectively. Weekly sales of flooring and tiles at Wickes also close to doubled. Nevertheless, with only 6 stores trading and serving customers predominantly through non-contact channels will have significantly reduced their sales overall. Wickes branches are still being used as fulfilment centres for their online delivery and click-and-collect orders, however with B&Q and Homebase, having fully reopened their store networks, albeit with social distancing measures, Wickes is likely to see a slowdown in their online sales as customers migrate to physical stores for immediate fulfilment.

At B&Q's re-opened stores, customers can purchase any products that are available for takeaway in store on the day. This is significant as the retailer therefore does not have to categorise products based on what is truly essential and what is not. However, services such as kitchen and bathroom design, paint mixing, timber cutting and key cutting are not available for the time being.

Interestingly plants are available to buy online and collect via the contact-free click-and-collect service, or indeed at the re-opened stores that have a range of self-service plants. B&Q point to the importance of gardening to their customers wellbeing but have also recognised the scale of the challenge Covid-19 presents for some of their suppliers. Plant growers have complained that they are being forced to discard vast stocks of unsold stock. The Horticultural Trade Association has warned that £200m worth of plants will have to be destroyed if the lockdown continued into June without such invention.

What the DIY sector has taught us is not only was it not possible for all retailers that qualified as essential to initially continue trading but also as more and more stores re-open the cost and practical implications of social distancing measures can further squeeze retailers margins and ultimately affect their ability to pay their occupancy costs.

> "Research from Kanter suggests that the amount families spend on a shopping basket has reached a record high, with the £26.02 being spent per supermarket visit, £7 higher than this time last year."

Out of town foodstore trading

Are supermarkets the biggest winners (or the smallest losers)?

According to the Office for National Statistics UK retail sales declined 5.1% in March from February, the largest drop since the agency started collecting the data in 1996. Non-food store sales were particularly badly hit , down 19.4% month on month. The sharpest decline however was in clothing which saw a decrease of 34.8% in the same period. Given the lockdown was imposed toward the end of March, another large decline in overall retail sales is set to be reported for April.

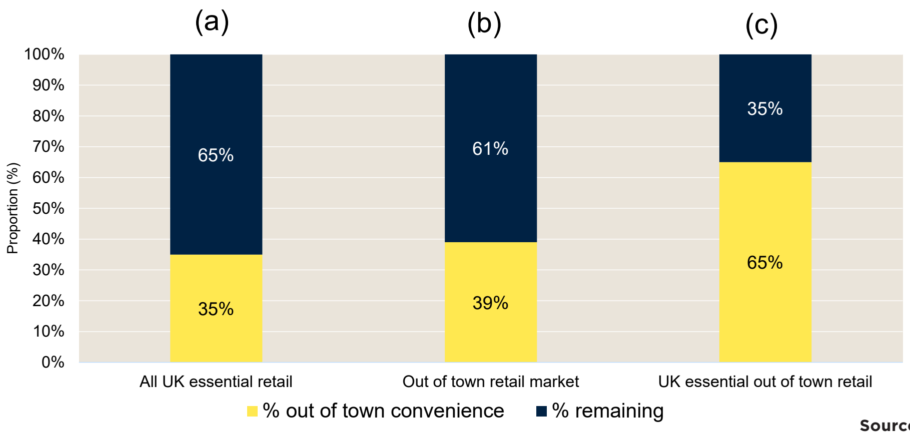
However, food sales and online-only firms were the only areas to see growth. Supermarkets and other food stores recorded a 10.4% increase in sales, while alcohol sales jumped 31.4%. Out of town convenience retail has remained open and trading throughout accounting for more than a third (35%) of the essential retailers permitted to trade immediately following the government sanctions (figure 6a). As a proportion of retail warehousing in isolation, the supermarkets left trading accounted for 39% of the out of town retail markets overall floorspace (figure 6b) and just under two thirds of what was deemed as essential in that sector (figure 6c).

The 'essential' status of large foodstore operators not only reflected well proportionally, in what was left open and trading in the UK retail market at the end of March. Consumer habits in the month following also changed in response to lockdown restrictions which have also seemingly favoured the industry. Research from Kanter suggests that the amount families spend on a shopping basket has reached a record high, with the £26.02 being spent per supermarket visit, £7 higher than this time last year.

The surge in spending has been accompanied by a fall in the number of shopping trips customers are making, as they contend with lockdown measures and queues to enter supermarkets. Consumers are food shopping less frequently but spending more when they do, whilst relying on local convenience stores for more frequent, small, additional top-up purchases to supplement their grocery shop. The rise in grocery spending has reflected well across the UK's major supermarket brands. In the three weeks to April 19th Sainsbury's sales grew by 8.4%, Tesco's were up 7.2% while Morrisons and Asda had rises of 4.3% and 3.5%, respectively. Both the Co-op's and Ocado's sales rose by a fifth in the same period.

It is not all good news for supermarkets however. Some foodstore operators have reported that the implementation of social distancing measures is now starting to temper both their in-store sales and profit margins as they are simply unable to serve the same volume of consumers as before. Furthermore, they have had to increase staff levels in order to implement such social distancing measures. Anecdotal reports suggest that one value grocer has seen a recent 40% decline in in-store sales due to social distancing rules. Although it seems supermarket operators were initially the biggest winners with large sales increases during the panic buying phase, as the situation progresses and social distancing measures become more commonplace they too may feel the squeeze on their ability to turn a profit, suggesting thus far they are perhaps the retail industry's smallest loser instead of its biggest winner.

Figure 6: Out of town convenience as a proportion of (a) essential UK retail, (b) the out of town retail market and (c) essential retail in the out of town market (by sqft, as of March 23rd)



Source: Savills Research

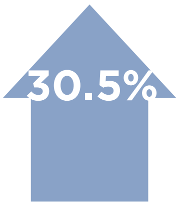
5.1%
decline in total UK retail sales

10.4%
increase in supermarket and other foodstore sales

34.8%
decrease in clothing and footwear sales

19.4%
decline in non-food store sales

In March from February (ONS)



Spending growth in local independent retailers between the last week pre-lockdown and the first week after the measures were announced (Barclaycard)

Small shops and convenience store resilience

The role of small format convenience chains and independents retailers

The role of small suburban convenience stores and independent shops, whether standalone or on small shopping parades, has become increasingly prominent since the government measures were introduced. My personal spend in my neighbourhood 'Nisa Local' convenience store has increased dramatically in the last month, from the odd pint of milk approximately once a fortnight to a far more substantial weekly spend on several bottles of wine to get me through the weekends online quiz activities.

This shift in personal behavior begins to make sense when it becomes clear that more than half (59%) of all retail units that were classed as essential following lockdown were small individual convenience based shops, including convenience stores and corner shops, newsagents, takeaways, pharmacies, off-licences , butchers, bakers and green grocers (figure 1b). This equates to 16% of the UK retail and leisure market as a whole (figure 1a), the best represented asset class following the government impositions on the basis of the number of units open and trading.

Where for out of town essential retailers, particularly supermarkets, the proportion of floorspace is much more significant, it is the opposite for small local convenience based retail operators. For supermarket operators the amount of space they occupy is much more important as it allows a large number of consumers access to a wide variety of groceries all at once. Convenience retailers however accounted for less than 3% of retail floorspace considered essential at the end of March. Convenience based operators are by their very nature about just that, convenience. They allow consumers to make smaller and more frequent, essential, 'top-up' purchases in smaller units close to their homes.

In an attempt therefore to reduce the risk of social contact, potentially long queues and making any unnecessary journeys, it seems we have become much more reliant on what is local to us in additional to our larger less frequent supermarket shop . Looking solely at independent retail operators across the UK it is again the convenience sector, small individual suburban shops and parades, where proportionally essential retailers became the most prominent accounting for 56% of units that were allowed to remain open.

In fact spending in this asset class, that includes local independent bakeries, butchers, grocers and takeaway outlets, has increased by a third compared to this time last year. Data from Barclaycard, which tracks almost half of all card transactions, shows that spending in local independent retailers rose by 30.5% in between the last week pre-lockdown and the first week after the measures were announced, compared to the same period in 2019.

UK retail market variation

Disparity in the exposure to essential retail goods and services

The towns and cities with the lowest percentage of essential stores that remained open after the lockdown were largely in the tourist and coastal locations particularly in southern England. Figure 7 highlights the eighteen markets where the penetration of essential retail after March 23rd was less than 20%. Of these Torquay, Falmouth, Brixham, Littlehampton, Faversham, Whitby, Formby and Llandudno are all retail centres located on the coast.

Conversely Luton, Coventry, Barnsley, West Bromwich, Doncaster, Wolverhampton, Rotherham, Ilford, Peterborough and Croydon are the ten largest markets where a third or more of their provision was classed as essential immediately after the government sanctions. This is largely because these towns/cities have a higher density of convenience retail accounting for more than 10% of all retail units and between a third and two fifths of what was left open in their respective markets.

Figure 7: UK retail markets with less than 20% of essential retail and leisure provision (as of March 23rd)

Source: Savills Research

Retailer insolvency activity

How have government closures manifested in the most recent administration

The Centre for Retail Research (CRR) estimates we will see more than 20,000 permanent store closures this year, an increase on the 16,000 we saw in 2019, which will have the potential to trigger nearly 250,000 job losses as a result of the financial reckoning faced by the retail sector as a result of Covid-19. A number of retailers have evidently witnessed a dramatic decline in their turnovers of up to 100 per cent, since March 23rd when the government ordered all non-essential stores to be closed during the pandemic. Despite government intervention measures put in place to support businesses, a series of measures including loans, grants, business rates holidays and a furloughing scheme, retailers are asking the government to support a "furloughed space grant scheme" where the state would cover the fixed costs of businesses that have experienced dramatic falls in turnover.

In mid-April a number of the UK's biggest retailers wrote to Chancellor Rishi Sunak warning that many currently viable businesses will undoubtedly need to file for administration, leading to substantial job losses, if the government does not do more to support the struggling retail and leisure sector, particularly with their rent payments. The British Retail Consortium and the British Property Federation have outlined that commercial tenants and landlords propose the government should introduce a scheme of rental support for the space that has in effect been furloughed, in the same way staff have been.

Many retailers believe the three month moratorium against eviction for non-payment of rents proposed by the government is not enough to help them survive. Many state they are unable to take advantage of business interruption loans because lenders are reluctant to lend to shops and that even full use of these loans would only support their businesses for a matter of weeks or months.

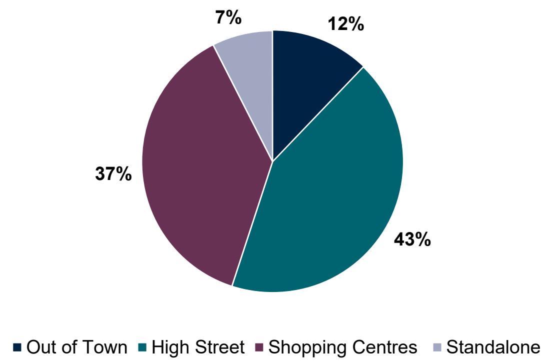
With little or no turnover from trading, ongoing payment of property costs will become increasingly more difficult for retailers which could lead to further collapses. This in turn will have a serious knock-on impact on landlords, including UK pension funds, listed companies and private investors.

In the last six months we have indeed seen a number of high profile retailer and leisure operators file for administration. Clintons and Bon Marche did so toward the end of 2019 whilst Debenhams filed for administration in early April, just before the Covid-19 outbreak, for a second time in a year.

Laura Ashley was the first high street casualty since the beginning of the pandemic, while department store chain Oasis and Warehouse, owned by Aurora Fashions became the latest retailer to file for administration. Other high profile retailers that have also recently deployed the rescue procedure, whereby a moratorium on legal action against the company by creditors is imposed allowing the company breathing space to reorganise its financial affairs, include Cath Kidston, Carluccio's, Chiquitos and Brighthouse. Both Laura Ashley and Cath Kidston have since found buyers for their brands but their physical stores are all set to close.

The resilience out of town assets have shown to non-essential closures at the outset of the pandemic, certainly in relation to high streets and shopping centres, is echoed when collectively analysing the portfolio spread of the operators currently under administration. More than 1,500 units have a question mark over their future, belonging to one of the retailers that have filed for administration in the last 6 months. Out of town assets are responsible for only 12% of these whereas high streets and shopping centres however have far greater exposure accounting for 43% and 37% respectively (figure 8)

Figure 8: Units under administration by asset class



Source: Savills Research

The early signs of a return to trading...?

High streets saw footfall decline 41.8% in March compared with the previous year, whereas shopping centres have been harder hit by the lockdown, reporting a 43.6% decline in footfall for the month. Retail parks however showed comparatively more resilience with a footfall decrease of 23.5% in March, a result which is reflective of the proportion of retail that was categorised as essential and how that manifested itself across different asset classes.

What is clear is that any resilience that has been demonstrated since the government imposed closures, whether that be by asset class, sector or individual retailer, has merely highlighted those areas of the industry that have perhaps suffered comparatively less as opposed to displaying any significant victory.

How quickly businesses can open and how quickly they can return to something resembling normal operations will determine who survives and who doesn't. The government seem set on phasing the re-opening of stores with a number of fast-food restaurants leading the first wave of businesses to resume operations in order to support those who may soon find themselves back in the office in some capacity. However, despite their advice for operators that offer takeaway services, guidance to be issued by the Department for Business, Energy and Industrial Strategy (BEIS) on the reopening of retailers, shopping centres, hotels, factories and offices, are clear that there are currently no foreseeable plans to reopen restaurants and bars to in-dining customers.

Nevertheless, BEIS does outline how non-essential retailers will be expected to implement new social distancing measures when they are allowed to reopen. These include limitations on the number of customers allowed in a store at any one time, using outdoor space for queueing, using screens to separate people, the provision of sanitation stations, one-way flow systems, staggering of employees' arrival and departure times and offering cashless payments and refunds to consumers. It remains to be seen how different retail centres will fare with these restrictions in place. However, the out of town retail sector may continue to show a degree of resilience as they are better configured to cope with some of the more difficult measures, particularly those that require people to maintain a physical distance, on account of their large store formats and car parking space.

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