

# UK Retail Warehousing



# Consumer trends

Retail sales remain elevated compared to pre-COVID levels, despite consumer concerns over inflation and supply chain shortages.

After six months of post-lockdown improvement, the UK's consumer sentiment began to be hindered by anticipated rising living costs amidst headlines of fuel shortages, supply chain disruption and surging energy bills. Subsequently, GfK's overall consumer confidence index currently stands at -14 having dropped by 7 points from July, its highest point this year. Despite the month-on-month declines we witnessed until November, when we saw a very slight improvement, this is still largely in line with the 2019 monthly average of -12.6.

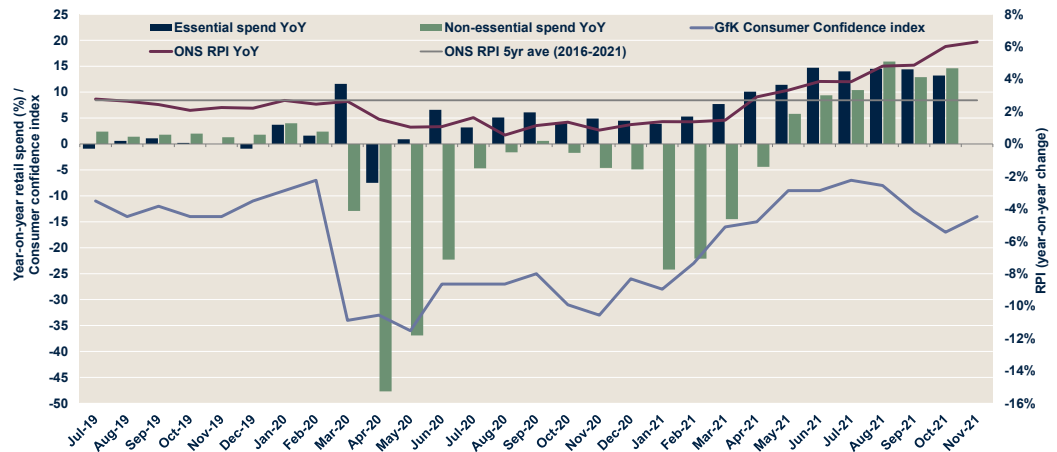
Meanwhile, the major purchase index dropped three points to -6, as high inflation begins to take its toll on spending habits. The ONS Retail Price Index (RPI) reported a 6.3% year-on-year rise in November 2021, the highest growth recorded since November 2011. This heightened inflation is expected to be temporary, in line with disruption to supply chain and staffing shortages, however, Oxford Economics are currently forecasting that year-on-year UK RPI levels will remain above 3% until at least Q2 2023.

## Retail spend remains elevated, despite rising consumer caution

Non-essential retail spend has seen positive growth since May, coinciding with the end of lockdown restrictions earlier in the year. In September, it grew +12.9% compared to equivalent 2019 levels, however this represented a smaller growth than the +15.8% recorded in August, according to Barclaycard data. While still inherently positive, the month-on-month softening in growth in September looked to highlight the early beginnings of consumer concerns over shortages and pricing hikes. This reduction in discretionary spending however, seemed short lived. October saw some improvement in non-essential spend, back up at 14.6% growth compared to 2019. With pent-up demand following nearly two years of heightened savings, consumers are perhaps once again choosing to spend more on non-essential items. It remains to be seen if the fears over inflation, energy prices, shortages and supply chain issues will outweigh this trend.

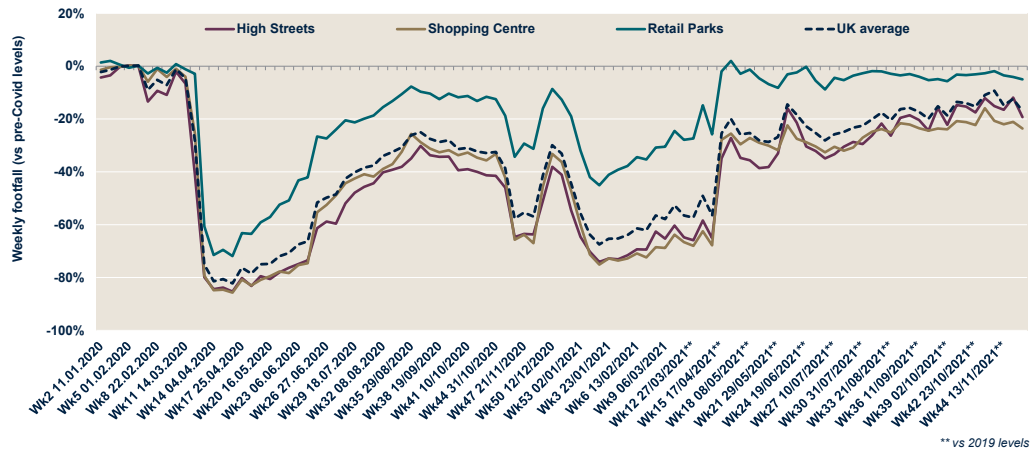
With such concerns comes the inevitable growth in consumer spend on essential items, with fuel and supermarket spend reporting +11.1% and +14.7% respectively in September, compared to the same month in 2019. However, growth in October slowed a little as concern over these matters softened, at least in the short term.

**Figure 1: UK consumer spend growth despite hindered consumer confidence** as rising inflation and supply chain shortages dampen consumer sentiment.



Source: Savills Research; Barclaycard; ONS; Oxford Economics; GfK

**Figure 2: UK weekly footfall by retail sector** highlight how retail parks continue to be far more resilient, with levels just 5% below the equivalent week in 2019.



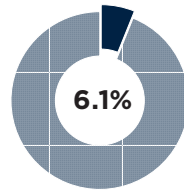
Source: Springboard

The leisure sector continued to improve by the end of Q3, with pubs, bars and clubs reporting +43.5% spend growth against 2019 levels, while the entertainment segment reported its strongest growth for over two years, of +28.0%. This has been driven by a return to events, gigs and cinema releases, along with a return to post-work socialising.

Clothing spend softened slightly on a month-on-month basis, albeit still reporting double-digit growth of +10.1% compared to September 2019. Footfall recovery across Q3 2021 has supported significant improvement to in-store sales for some retailers. Next announced that retail stores serviced 44% of sales in September 2021, settling between the 34% recorded in March 2021, and the 55% share reported pre-COVID. Meanwhile, Inditex suggests store sales are largely returning to 'normal' levels, as of H2 2021.

According to Springboard footfall on retail parks remains well ahead of the UK average at only 5% below 2019 levels in the week beginning the 13th of November. Clearly the ability to social distance across large retail parks has been an important factor in the public's consciousness and remains so, owing to its drive-to convenience, outdoor setting and therefore perceived COVID-safety.

Looking ahead, the headwinds currently facing retailers could become more acute as we head towards the Christmas period. Supply chain issues could both restrict stock levels and cause further price inflation, particularly during the heightened Christmas period, while difficulties staffing the busy period could further limit operations. This has the potential to apply significant pressure on margins for some retailers during the period which ordinarily has great bearing on annual reporting figures.



Despite some creep, vacancy remains low in the sector, particularly compared to other retail asset classes.

## Occupational market

The strong occupational story continues in the retail warehouse market but despite the positivity, the sector must not be complacent about the important ESG targets it must meet, that are rapidly becoming an increasing consideration for both landlords and occupiers alike.

From an occupational standpoint our in-house position on the strength of the sector remains a positive one and hasn't changed for some time. Even before the onset of the global pandemic we were singing the praises of the sector in response to its positive occupational performance, comparative to other parts of the retail market, and indeed commercial property as a whole. It will be no secret to anyone that has subscribed to this report over the last few years that the fundamentals of the sector that saw it evolve in the first place – more space at lower rents than those found on the high street – is why we believe retail warehousing has consistently proven itself to be much more resilient to external market pressures than is true of other asset classes. These include, but are not limited to, the pre-pandemic growth of online retail, the structural change and re-basing of rents as well as the retail and leisure insolvency activity we have seen over the last few years. If you couple that resilience with the sectors positive performance indicators - including above average acquisition activity, above average footfall performance, comparatively low vacancy rate, click-and-collect growth driving additional sales, retailer performance and growing consumer spend - the sector has been well placed to cope and in some cases even thrive, in what has been a period of unprecedented challenge to retailer performance during the COVID crisis.

The latest swathe of statistics do nothing to dampen our positive outlook. Vacancy in the sector remains stable at 6.1%. This does represent a creep of 0.6% since this time last year, however half of that (0.3% of the market as a whole) was as a result of the failure of Arcadia at the end of 2020 which resulted in overnight voids of 77 units or 1.1m sqft of fashion space across the Outfit, TopShop, TopMan, Burton, Dorothy Perkins and Miss Selfridge brands.

Nevertheless, vacancy in the sector certainly remains robust in comparison to other retail asset classes. LDC currently forecast vacancy for the whole retail and leisure sector at 14.8%, with shopping centres at 18.0% and the high street at 11.9%. The loss of the Arcadia brands at the end of 2020, as well as the disappearance of Debenhams department stores around the same time, have had a far bigger impact on the high street and shopping centre markets than is true out of town.

### No major insolvency activity in 2021 helps to keep vacancy stable in the market

The retail warehouse sectors ability to maintain a consistently low void rate is fundamentally down to two important factors. Firstly, a lack of any significant insolvency activity in the market has helped keep voids low. 2021 has seen no major brands with a significant out of town focus pass through a CVA, administration or liquidation. This of course hasn't been exclusive to retail warehousing. On June 16 2021 the government announced an extension of the existing moratorium on landlord action for rent arrears under the Coronavirus Act, from 30 June 2021 (when it was due to expire) to 25 March 2022. The extended moratorium restricts the ability of commercial landlords both to forfeit leases for non-payment of rent and to seize goods in payment of rent arrears under the Commercial Rent Arrears Recovery (CRAR) procedure. The end of the eviction moratorium in March 2022 however, could pose as a potentially significant moment in the retail sector as a whole. While many retailers who relied on the moratorium may have had significant time to recover revenue and trade profitably again, its end could prove to be a catalyst for retail vacancy for those unable to pick up trade over the next six months. Local Data Company is therefore forecasting that UK retail vacancy will rise to 16.5% by H1 2022, up 0.7 percentage points from the 15.8%

reported in H1 2021. It is our view however, that should we see a flurry of insolvency activity post Q1 2022, the out of town sector is much better placed to weather the storm, as it did before the moratorium was put in place.

The fact that retail warehousing was comparatively less affected by retailer failures than is true of other retail segments last year, was largely due to their lower exposure to mid-market fashion operators which accounted for as much as 57% of units to pass through an insolvency process in 2020. As previously eluded to, the Arcadia and Debenhams administrations led to the largest proportion of closures in both the in-town and out-of-town markets. However, of Arcadia's c.6m sq ft of retail space, the out-of-town market accounts for only 18%, predominately through their 'Outfit' brand, going some way to explaining the difference in fortunes between the two asset classes.

The recent trading performance of the retail warehouse sectors most prominent brands, coupled with their continued appetite for further expansion, suggests even when the moratorium ends, a flurry of insolvency activity in the retail warehouse sector is, at least in our view, unlikely. The basket of retailers most prominent in the sector has arguably never been as strong in terms of their covenant strength which brings us to the second point on why the retail warehouse sector maintains a consistently low void rate.

**New Flannels store at Cyfarthfa Shopping Park, Merthyr Tydfil**





**832**

stores let up to the beginning of November 2021, already at the decade average and in advance of the 701 let the previous year.

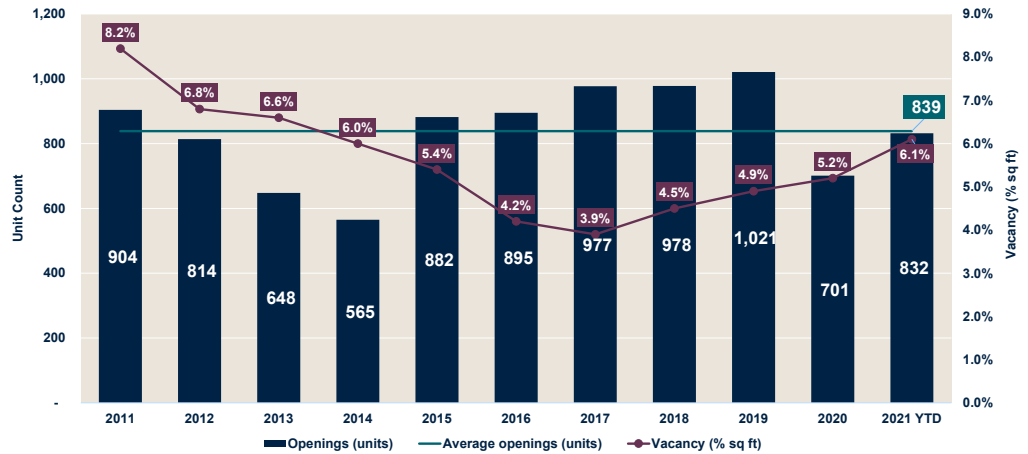
**New store openings for 2021 will finish above the decade average, helping to keep voids below the wider retail average**

Figure 3 highlights how new store openings in the sector are getting back to pre-pandemic levels having all but reached the decade average with 832 new openings by the beginning of November. With two months of the year to go and the inevitable flurry of deals toward the end of the calendar year, the sector will undoubtedly see the number of new opening get close to 1000 units, as it did in the three years prior to the onset of the pandemic. As figure 3 elegantly demonstrates this should therefore have a positive downward influence on the current vacancy rate over the next twelve months, typically and unsurprisingly previous years have demonstrated a strong correlation with high numbers of store openings and low vacancy in the sector.

In terms of the brands it is of course the value oriented operators that continue to top the charts of the most acquisitive retail and leisure brands (figure 4). Overall value orientated operators account for a third of all new openings so far in 2021. Of the top 20 brands highlighted in figure 4, value retailers account for two thirds (66%) in terms of new units and 80% in terms of new space. Lidl, Aldi, Home Bargains, B&M, Iceland/The Food Warehouse, Farmfoods and The Range all examples of value orientated retailers that have been the most acquisitive over the last 3 years. Lidl of course remain top of the leader board both in terms of the number of new units and additional space. So far this year they have acquired as many as 53 new units, equating to 908,400 sq ft of additional floorspace, with an average store size of 19,700 sq ft. Aldi are not far behind with 41 new stores, equating to 685,200 of additional floorspace, with an average store size of 19,000 sq ft. With both operators stating they are each looking for around 50 stores each per annum for the next 3 years at least, the growth pattern of the discount grocers in particular looks set to continue.

This strong pattern of portfolio growth for a number of retail operators is no accident as ultimately the fundamentals of the sector remain strong, attractive to both the consumer and occupiers alike. Convenience, free car

**Figure 3: New store openings** will exceed the decade average in 2021, after last year's inevitable but not disastrous pandemic related dip



Source: Savills Research

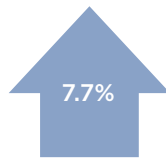
**Figure 4: Top 20 most acquisitive retail and leisure operators** by (a) number of units and (b) floorspace (sq ft) (November 2021)

(a) ranked by units					(b) ranked by sq ft				
Rank	Operator	Units	Total Floorspace	Average Unit Size	Rank	Operator	Units	Total Floorspace	Average Unit Size
1	Lidl	53	908,400	19,700	1	Lidl	53	908,400	19,700
2	Aldi	41	685,200	19,000	2	Sports Direct	23	779,700	46,000
3	Home Bargains	30	598,200	20,600	3	B&M	27	689,700	27,400
4	B&M	27	689,700	27,400	4	Aldi	41	685,200	19,000
5	Sports Direct	23	779,700	46,000	5	Home Bargains	30	598,200	20,600
6	Starbucks	20	35,200	2,000	6	M&S	6	257,200	48,900
7	Costa Coffee	19	31,900	1,900	7	The Range	9	221,200	32,700
8	Gourmet4	18	69,000	4,100	8	Everlast Fitness Club	7	180,800	25,800
9	Greggs	16	24,500	1,700	9	Iceland	13	171,000	12,800
10	Pure Gym	14	139,900	10,000	10	Next	5	169,100	30,400
11	Tim Hortons	14	47,900	3,400	11	Pure Gym	14	139,900	10,000
12	Co-operative Food	13	50,800	4,300	12	Farmfoods	11	117,400	10,700
13	Iceland	13	171,000	12,800	13	JD Gyms	5	114,200	22,800
14	TheGym	11	109,500	10,000	14	TheGym	11	109,500	10,000
15	Farmfoods	11	117,400	10,700	15	JD Sports	9	105,200	11,700
16	JD Sports	9	105,200	11,700	16	Poundland	9	103,600	11,500
17	Bensons For Beds	9	102,100	11,300	17	Bensons For Beds	9	102,100	11,300
18	Five Guys	9	25,800	3,400	18	CS Lounge Suites	7	94,900	13,600
19	The Range	9	221,200	32,700	19	Cineworld	1	89,700	89,700
20	Poundland	9	103,600	11,500	20	Tesco	4	73,500	34,900

Source: Savills Research

parking, ease for click & collect fulfilment, lower service charge, good size and layout of units, sustained footfall from foodstore anchors in particular and of course more competitive rents all help to drive the above average acquisition activity we have seen both pre and post lockdown. It is also why Savills have seen a number of traditionally high street retailers such as Holland & Barrett begin to take space in the out of town market also.





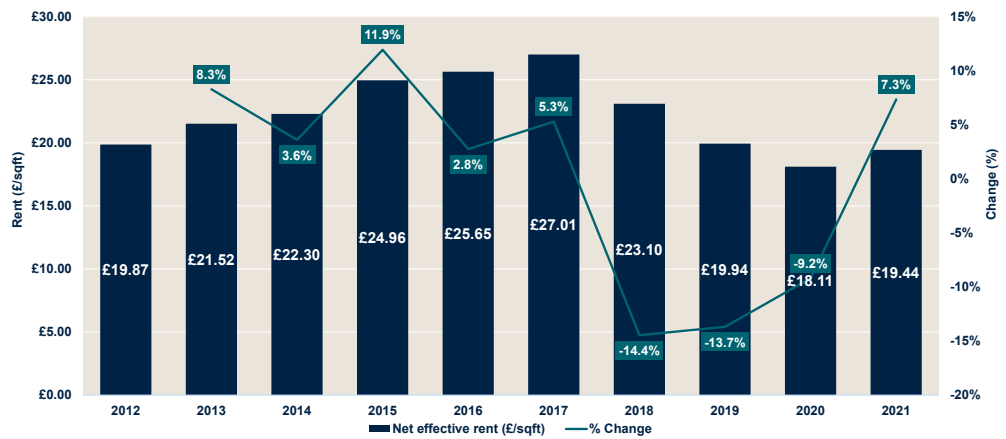
**+7.7%**  
improvement on the average rent achieved, for Savills 2021 open market lettings and regears

**2021 sees average rents improve on Savills open market lettings and regears**

Undoubtedly, retailer acquisitions have in part been driven by the structural change in rent we have seen in retail over the last few years, where the most active brands, particularly the discount operators, have been keen to take space on more affordable terms. 2017 was the last time we saw positive rental growth in the retail warehouse market. Data from all Savills open market lettings and regears saw net effective rents fall by a third on average across the market since the onset of the decline, from £27 per sq ft in 2017, to £18 per sq ft by the end of last year (figure 5). However, as we have discussed in previous issues of this Spotlight, the retail warehouse market has increasingly shown itself to be more resilient than other asset classes when it comes to rental decline. Significantly, for the retail warehouse sector, declines in net effective rents have been slowing year on year since 2017. In fact Savills new lettings and regears for this year, up to the end of Q3, have actually seen their average net effective rents increase to £19.44 per sq ft, a 7.7% improvement on the deals that were done in 2020 (figure 5). The evidence therefore suggests we are perhaps on the precipice of recovery in rental terms, as it seemed we were back in March 2020, before the impact of the pandemic delayed proceedings and the inevitable questions of further rental decline and even operator survival began to emerge.

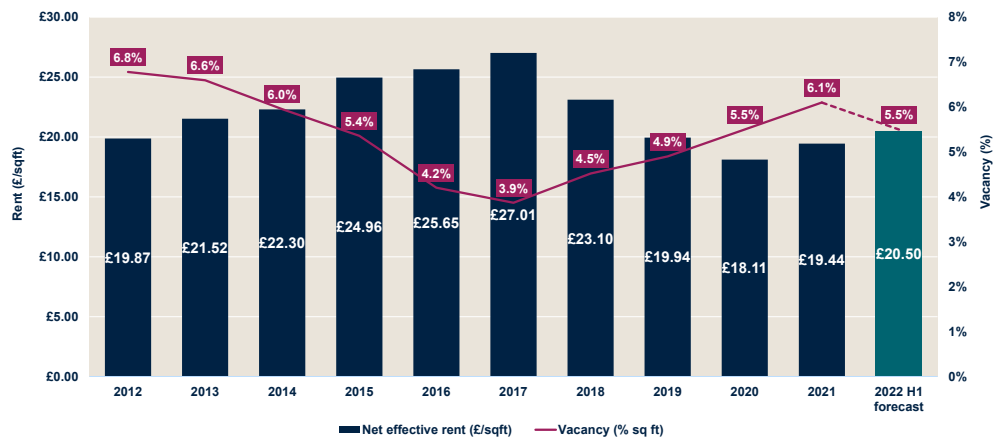
There is now real optimism surrounding the potential for rental growth in the near future, supported by the consideration that only 26% of tenants across retail and shopping parks have a lease expiry sometime in the next 3 years. The evidence suggests we are close to the end of the lease expiry cliff in the retail warehouse sector, having renegotiated most of the large, arguably unsustainable, rental agreements that were signed 10 to 15 years ago. As much as three quarters of the out-of-town market has already been re-based in terms of rents, much further along in the process of dealing with rental encumbrance it would seem, than is true of shopping centres or high streets. Figure 6 makes the point that historically when vacancy/supply in the market has been at its lowest, that is when net effective rents

**Figure 5: Net effective rents on Savills new lettings and regears up to the end of Q3 2021**, have seen a 7.7% improvement on average, on the deals that were done in 2020



Source: Savills Research

**Figure 6: Historically when supply has been at its lowest in the market rents have started to climb**



Source: Savills Research

have reached their highest. As the value orientated retailers snap up the best of the Arcadia stores and the current vacancy begins to fall, the sector could be forgiven for assuming rents may begin to creep northward at a similar rate.

It is therefore Savills view, judging by the number of units in the market already under offer, that the vacancy rate will fall to around 5.8% by the end of Q1 2022, and further still to 5.5% by the end of H1, particularly with a number of longer term voids, where alterations have taken longer than usual to pass through the planning process, also coming back on to the market. Analysis of the deals Savills has in the pipeline suggest this will take the average net effective rent to nearer £20.50 per sq ft on new open market lettings and regears.

Rental growth is obviously an important

consideration for the market in terms of measuring its performance, although as we know, since the onset of COVID-19, rent payments on existing leases have helped illuminate the strength of the sectors position versus other asset classes. With much more of the retail warehouse sector considered to be 'essential' during the height of the pandemic, retail warehousing performed better than most other retail asset classes. In September last year 53% of retail park rent payments were being met on Savills managed schemes, compared to only 28% for shopping centres. The most recent statistics on the 2021 September collection date, highlight tenant payments have significantly improved in the sector, retail parks rents now at 76% payment, whereas shopping centres remain much lower at 51%.

**The grocery sector leads the way in last mile fulfilment and omni-channel retail provision**

One trend that has taken a foothold in recent years is retailers recognising that retail warehousing is a strong option in their 'last mile' customer fulfilment requirements. As a result the sector has begun to see much more interest from investors, many exploring the sector for the first time, who typically have had portfolios much more weighted toward logistics than they have been towards retail.

Grocery is the sector where the 'last mile' fulfilment has gained the most traction over the last 18 months. The COVID-19 pandemic dramatically changed the online grocery landscape by turbo-charging demand throughout the UK and propelling online sales to 15% of the market. Operators responded impressively in increasing home delivery capacity from 1.8 million deliveries per week to 3.7 million deliveries per week, driving five years of growth in online grocery in the first five months of the pandemic.

Meeting consumer demand with the significant rise in online grocery sales however, was only actually achievable due to the network of stores already in place for those operators with an online purchasing and delivery platform. The extensive and widespread store networks of operators such as Tesco, Sainsbury's, Morrisons, Asda and Waitrose is what puts them close to their customers and enables them to get their products, particularly those that need to be temperature-controlled, on our doorsteps quickly and easily. According to Atrato Capital, Tesco increased their online weekly delivery slot capacity by 150% from 600,000 orders pre-COVID, to over 1.5m orders per week post COVID. Asda (89%), Sainsbury's (126%) and Waitrose (167%) also all more than doubled their respective capacity.

This increased online penetration has had the added bonus of transforming the profitability of omni-channel grocery fulfilment, Pre-COVID, online sales were considered to be costly and structurally less profitable than physical in-store sales however, the near doubling in online grocery penetration has materially improved delivery densities which has, in turn, nearly halved delivery costs from omni-channel stores. Given the dominant driver of grocery home delivery fulfilment costs are wrapped up in delivery, more so than picking and packing, this new-found efficiency gain has transformed online profitability to the point whereby online sales are close to profit margin parity with physical in-store transactions, achieving a seamless integration for the operator between online and offline channels. This new normal underpins the importance of having the right stores in the right location to be successful and empowers the operator to be truly blind to channel. Future grocery strategy can therefore be focussed purely customer focused, agnostic to where the sale takes place – in store, online with delivery or click and collect. This has huge advantages for the retail warehouse sector as they are best placed in all three fulfilment options.

As a result, interest has therefore begun to return to out-of-town supermarkets with the largest floor-plates, as

operators look to combine a traditional customer facing foodstore with a semi-automated picking centres. Located at the back of the brick-and-mortar store they typically require a footprint of approximately 10,000 to 15,000 sqft, allowing operators to enhance capacity and productivity. Furthermore, adding online fulfilment operations to a supermarket creates a much better in-store experience, for the customer it creates a virtuous circle with greater numbers of staff on the shop floor, increased product turnover, leading to a bigger and better range and fresher product on the shelves

For the retailer converting a supermarket to also operate as a last mile fulfilment centre, requires minimal capital expenditure, largely because they can be supplied by its pre-existing centralised distribution centres. Tesco have recently alluded to 'owning the last mile' in this way, as a means to scale up deliveries without heavy capital expenditure. They have pointed out that in-store micro-fulfilment centres can be installed in just a few months at a much lower capital cost, as opposed to up to two years for a large automated warehouse.

Sainsbury's decision to close its 'dark store' in Bromley-by-Bow in London would suggest online fulfilment is better served from trading stores. By March next year, more than 20 stores in and around the capital are expected to expand their online packing capabilities, enabling Sainsbury's to deliver thousands more orders each week. Asda have also announced plans to shut two of its online warehouses, switching from its dark stores in Dartford, Kent, and Heston, west London, to picking grocery orders from the shelves of local stores.

The advantage for the retail warehouse sector is that it is not just supermarket operators that have begun to recognise the importance of their out-of-town store network in fulfilling online consumer demand. For Kingfisher (including B&Q and Screwfix), growing online sales is a key strategic priority, with investment in the channel allowing them to respond quickly and effectively to changing consumer behaviour during COVID-19. Online sales rose 158% during FY2020/21, driven by strong growth in click-and-collect (+226%) which now accounts for 78% of group online sales, up 16ppts on last year. In other words, more than three quarters of their online sales require their network of stores for fulfilment, which of course has the added bonus of driving additional consumer sales to the store at the point it is collected.

**+180%**  
increase in  
online grocery  
demand (since  
the onset of  
COVID-19)

**80%**  
of all UK online  
orders fulfilled via  
omni-channel stores

**100%**  
online margins  
now at near  
parity with  
instore sales

**30mins**  
average drivetime  
to customers - key  
to lowering  
fulfilment costs

Source: Savills Atrato Capital



👉 **The stamp duty land tax holiday introduced by the government in July 2020, ran until September of this year and with it saw a meteoric rise in the number of people moving home...which translated to positive sales growth in household goods sales** 👈

**The unprecedented increase in housing transactions has resulted in positive sales growth for many bulky goods operators**

Another feather in the cap for retail warehousing, from an occupational standpoint, has to be the relationship between residential transactions and the positive sales growth for the sectors traditional bulky goods and DIY operators. The stamp duty land tax holiday introduced by the government in July 2020, ran until September of this year and with it saw meteoric rise in the number of people moving home. Figure 1 shows a very clear spike in the total value of housing market transactions, which translated to positive sales growth in household goods sales (which includes furniture, lighting, electrical household appliances, hardware, paint, glass, music and video recordings and equipment). This result can be seen in the individual performance of some of the more prominent retail warehouse operators. Dunelm have seen total revenue growth of 26%, Topps Tiles revenue like-for-like sales increase of 20%, and DFS revenue growth of 47%, each in their last full year performance results. In H1, B&Q have seen UK and Ireland sales increase by 30% whereas Wickes has seen like-for-like group revenue increase by 33% (according to GlobalData).

Since the onset of the pandemic, even those consumers that haven't moved house have been spending more enthusiastically in the bulky goods/

DIY sectors, driven largely by pent-up demand following nearly two years of heightened savings. With people spending increasing amounts of time at home, many indeed working from home for large periods, many have been choosing to invest in and improve upon their surroundings, particularly those that have saved money they would have typically spent on holidays for example. Many furniture operators lost sales in lockdown this year but have since seen strong recovery since their stores have reopened. Whilst it is possible buy a sofa online, many consumers simply want to check the look and feel of it first before such a large purchase. Showroom retailing in this is an important factor in out of town retailing and why the sector remains more defensive to e-commerce than other parts of retail.

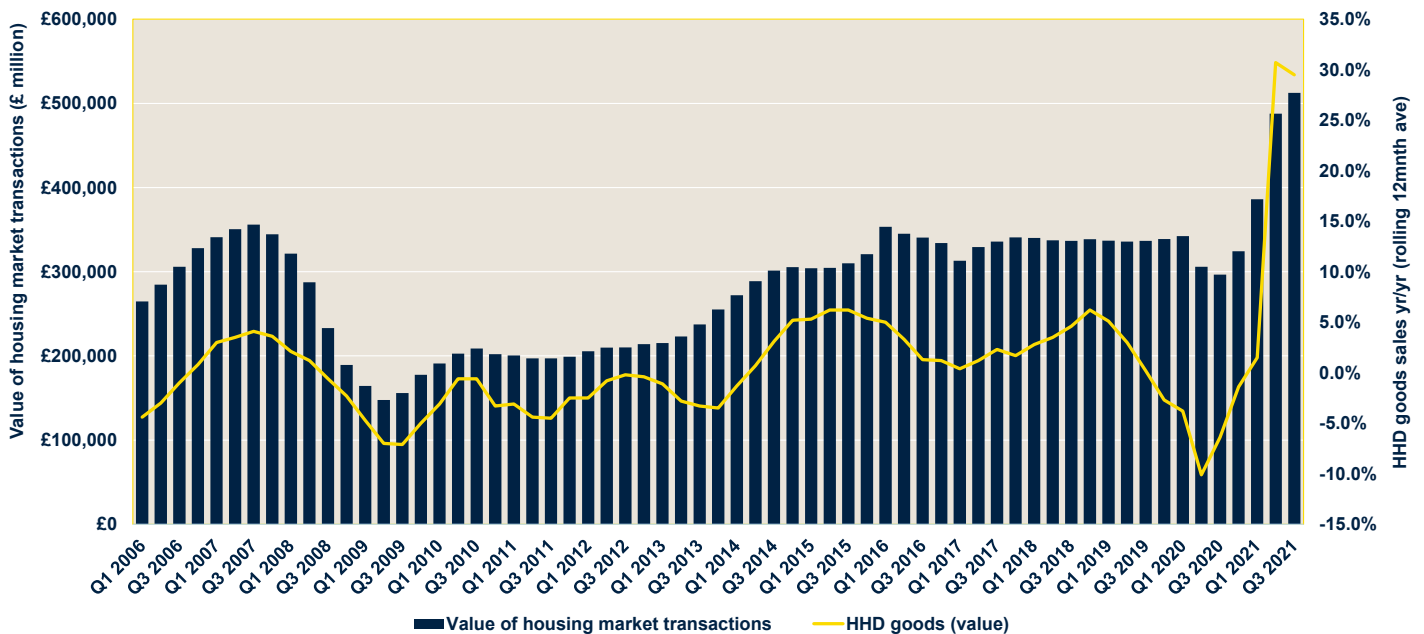


**+29.7%**  
H1 FY2021/22  
(end July)  
UK & Ireland  
sales



**+26.3%**  
FY2020/21  
(end June)  
total sales  
growth

**Figure 7: Value of UK housing market transactions versus household goods sales (by value)**



Source: Savills Research, HMRC. Land Registry. Registers of Scotland, Northern Ireland Department of Finance. Bank of England (MLAR), ONS; GfK

“ By 2023, all retail property must have an EPC grade of at least an E, which means that as it stands 185 million sq ft of retail outlets may be un-lettable in just over a year ”

**Retail warehousing and ESG – targeting an environmentally sustainable future**

Despite the positivity surrounding the retail warehouse sector it is not without its challenges. Environmental, Social and Governance (ESG) targets are rapidly becoming an increasing consideration for both landlords and occupiers, not just in the out of town market, but across all commercial assets and indeed property in general.

A large proportion of the commercial stock in the UK requires further investment to become environmentally sustainable. Currently, British shops emit over 8 MtCO<sub>2</sub>e more than the emissions targets derived from current Building Regulations. In order for retail property to become carbon neutral, ambitious targets have been set to decrease carbon footprints through the Minimum Energy Efficiency Standards (MEES). By 2023, all retail property must have an EPC grade of at least E, which means that as it stands 185 million sq ft of retail outlets may be un-lettable in just over a year. To meet the minimum B grade standards being considered for 2030, 1.4 billion sq ft (83% of stock) will need to be improved. This will come at a considerable cost and in many cases may not be economically viable.

That said, the majority of commercial property is owned by either corporate or institutional investors with their own ESG targets already in

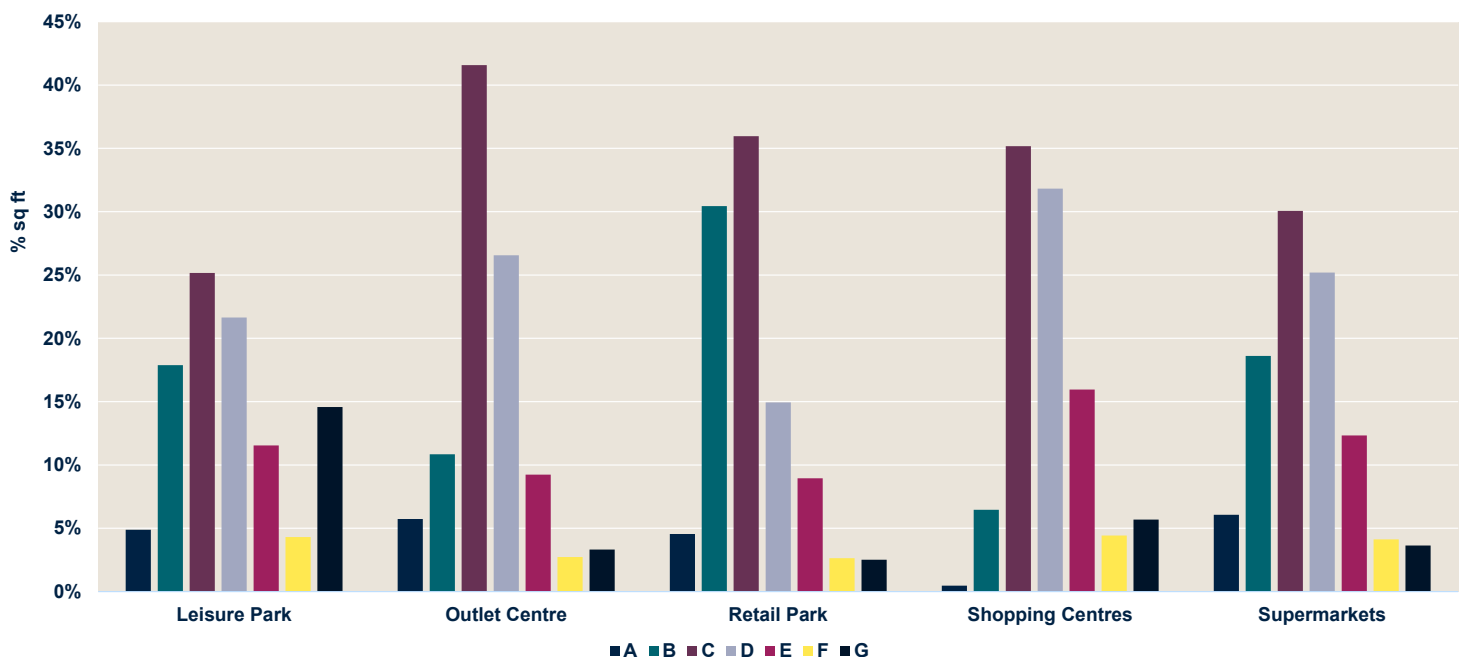
place. As such many have already begun to make the changes that are needed to be in line with or, in some cases ahead of legislative changes. Investors in commercial property are of course used to factoring in the costs of obsolescence to ensure that their asset remains lettable at the best market rates in the future and so the retail market could be considered to be ahead of the curve versus the residential property sector for example.

The good news for the retail warehouse sector is the vast majority of retail park space is currently classed as B (30%) C (36%) and D (15%) which means less 6% of its floorspace is ranked as F or G in terms of its EPC efficiency rating (figure 8). This represents less than 5% of 85 million sq ft of retail outlets currently in need of an upgrade ahead of the minimum grade E target looming large on the horizon. Nevertheless, in real terms that does mean nearly 9 million sq ft of retail park floorspace is in need of some immediate attention if it is to remain lettable beyond 2023, so there is still some work to do for a number of landlords over the next 12 months. That said, there is also a strong correlation between the worst performing assets and high retail vacancy rates, which begs the question in some instances whether bringing some shops up to grade will actually be worth the investment.

Looking ahead, for large institutional landlords, their ESG obligations and lettable space will be key drivers in reducing outlet emissions even further. The size of their individual investments and access to capital will increase viability. However, most retail property emissions are not associated with shopping centres, retail parks and large high street blocks, which only account for around 25% of retail property emissions. Small shops are more difficult to retrofit, or are much older and so it is those outside of both key ownerships and core trading locations that are likely to require more government intervention, policy and support to drive the change.

The opposite is therefore true for the retail warehouse sector where, owing to the nature of its construction, it is in theory at least, much easier to implement the physical changes needed to be compliant. Large units with flat roofs provide plenty of opportunity for photovoltaics (PV) or ‘solar panel’ installation/upgrades, whereas large car-parks offer electric vehicle (EV) charging provision opportunities much more easily, for example. It is therefore little surprise that the average unit size of A-rated retail property is five times as large as G-rated properties, highlighting how well placed the retail warehouse sector already is, to implement change going forward.

**Figure 8: EPC grade by retail asset type (% of floorspace)**



Source: Savills Research

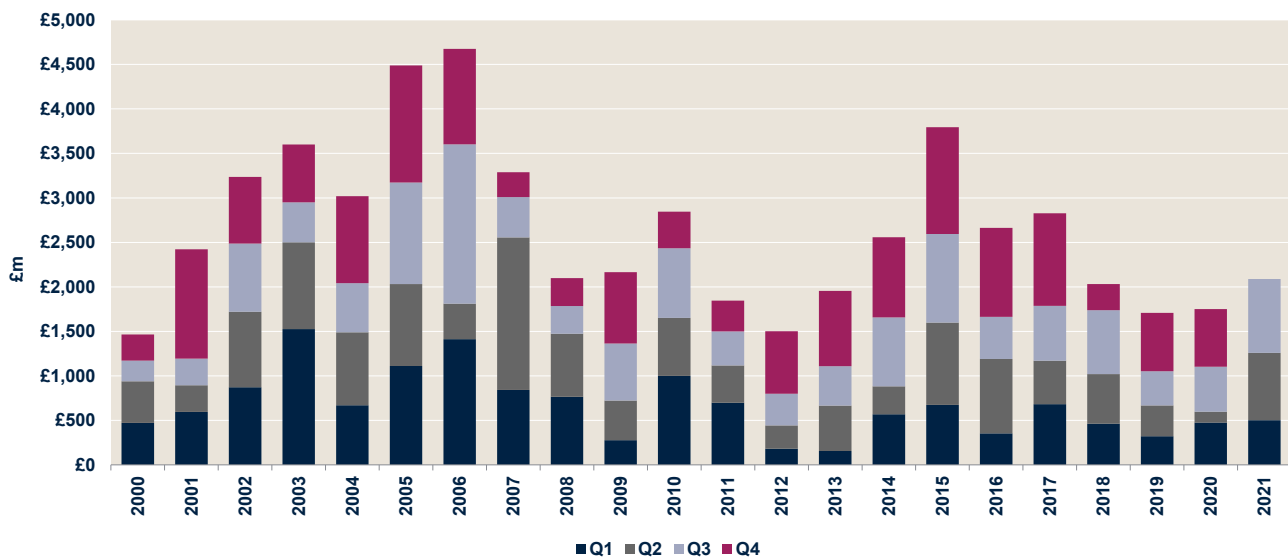


“ With a turnover of £2.6bn for the 11 months to the end of November 2021, there is no doubt that this year will be the most active retail warehouse investment market since 2015 ”

# Investment market

Investment market – Volumes boom and prime yields fall in 2021. Will this momentum be sustained into 2022?

**Figure 9: UK retail warehouse investment volumes**



Source: Savills Research

With a turnover of £2.6bn for the 11 months to the end of November 2021, there is no doubt that this year will be the most active retail warehouse investment market since 2015. Putting this in the context of other asset classes, the 75% year-on-year increase in transactional volumes this year is second only to the 109% increase in industrial/logistics investment activity.

While the overall make-up of the buyer pool has been fairly heavily biased towards opportunistic and private equity in the first half of this year, it is also notable that as the year progressed some more traditional retail park owners were active, with both Threadneedle and British Land in the top ten of the most active purchasers in 2021.

The reasons why retail warehousing has seen such a strong recovery in investor interest have been well rehearsed in this Spotlight in the past, but one recent change that we have noted is that debt has become easier to obtain over the last few months (admittedly from a position of being unobtainable earlier this year!). While the terms on offer are generally pretty cautious, at around 50% LTV, this change does point to 2022 having

the potential to be a more liquid investment market than 2021.

Downward pressure on prime pricing has continued during the second half of 2021, and prime Restricted and Open A1 parks have seen a full 100bps downward shift in yields this year. Prime restricted yields are now broadly in line with their ten year average at 5.75%, but Open A1 parks at 5.50% are still 25bps above average. While the differential between the two groups has closed over the course of 2021, and is perhaps justifiable given caution around fashion retailing in particular, we believe that the rising weight of money targeted at retail warehousing in general will close this gap further in 2022.

The bulk of investment activity this year has remained towards the more opportunistically priced end of the spectrum. However, even the average yield achieved has hardened this year from 7.77% in the first six months of 2021 to 7.10% in the second half.

Looking ahead to 2022, while some commentators are suggesting that the surge in activity in the retail warehouse investment

market will accelerate, we remain a little more cautious. There will be both push and pull factors in play, and these will mean the transactional volumes might not be significantly higher in 2022 than 2021. Private equity buyers, unless their ethos is more Core+ than Value-add, are likely to be seduced to other higher yielding parts of the retail market next year, though their withdrawal will to a degree be compensated by a steady return of domestic and European institutional buyers in the market.

Institutional buyers will be more focused on the prime end of the market, comforted by the strengthening rental growth prospects, and this should put further downward pressure on prime yields in 2022. However, PE buyers are likely to be taking a hard look at what the prospects for real capital value growth will be over the next five years, and this will be another factor that might reduce their activity in this sector next year.



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