GVA James Barr

Research report

Scottish Retail Trends

September 2015

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Introduction

GVA James Barr are pleased to publish the sixth edition of our retail bulletin covering the latest indicators and emerging trends that are affecting the health and viability of Scotland's towns and wider retail sector.

We are reporting at a time of increasing positivity within the commercial property sector following the doldrums of recession, and starting to witness a slow but steady economic recovery that is now trickling down beyond Scotland's main cities to the other larger towns and satellite locations. This improvement has been borne out in a number of the findings of this year's publication.

Continued Recovery

The outlook for the Scottish economy is positive with healthy economic growth, estimated at 2.8% pa during 2014 set to continue, albeit at a more moderate pace of 2.1% in 2015. Employment growth has been strong and the unemployment rate has fallen to 5.9% (February-April), down from a peak of 8.6% in 2011, and wage growth is finally outpacing inflation. This is providing a real boost to household incomes and consumer spending which is positive news for the retail sector.

Retailers are reporting mixed trading performances, with some continuing to rationalise portfolios, whilst others are still expanding, particularly at the premium and value ends of the spectrum. Demand for retail property remains strong for prime locations, both in terms of the strongest/largest towns and the prime pitches within town centres.

Where supply is constrained retailers are increasingly considering areas previously thought of as fringe or peripheral. Town centres are also seeing more alternative uses filling voids, with leisure and other service/community uses helping to underpin centres. It is important that appropriate planning policies are in place to support these processes, and enable centres to adapt in order to remain vital and viable.

Retail property performance indicators

Rents

Average high street retail rental values in Scotland fell by more than 20% from 2007 to mid-2014, according to the IPD Monthly Index. However, rents are now starting to rise again, and as at May 2015 rental values are 1.1% higher than their low point in June 2014. The rate of growth has accelerated sharply in recent months. Taking just the three months to May, Scottish town centre average rental values rose by 0.5%, an annual equivalent of 1.9%.

We expect rental growth to increase gradually as rising wages, healthy employment growth and rising house prices impact positively on retail sales and shop vacancy rates edge downwards.

Yields

Demand for UK commercial property continues to be extremely buoyant from both domestic and overseas buyers, and this has resulted in strong downward pressure to property yields across the UK (the lower percentage yields reflecting higher levels of capital invested in assets). The Scottish retail sector as a whole has seen average high street retail yields tighten, with a fall of nearly 35 basis

Figure 1: Average rental growth value – Scottish high street retail

Source: IPD Monthly Index

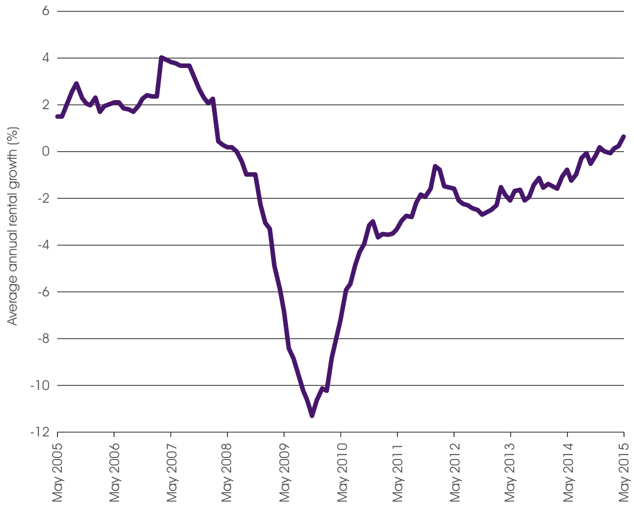


Figure 2: Scottish high street retail yields

Source: Nationwide

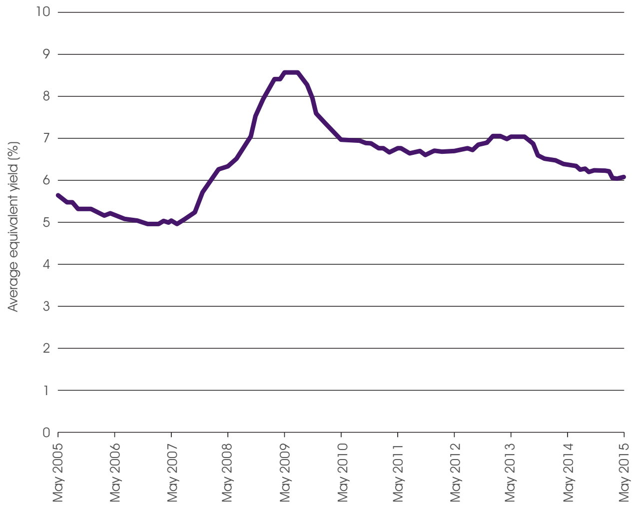


Figure 3: Floorspace composition

Source: GOAD

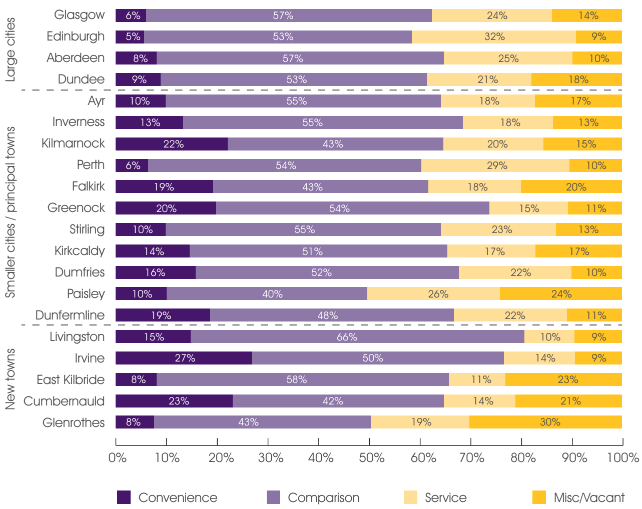
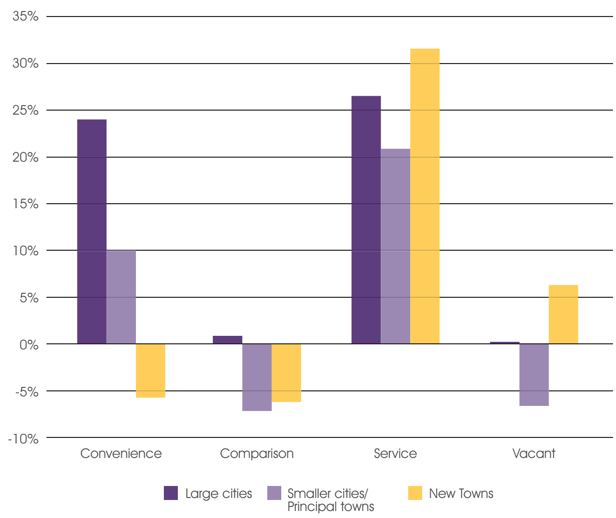


Figure 4: Overall change in floorspace composition 2008 - 2014

Source: GOAD



points over the last year and by 100 basis points over the last two years, to 6.1% as at May 2015 (IPD Monthly Index).

The outlook for the next 12 months remains positive and we see no reason for the international inflow of capital into the UK market to slow. 10-year gilt yields remain close to historic lows at below 2% (as of early May), so the gap with property yields remains wide, and high street retail capital values in Scotland are still more than 35% below their 2007 peak (IPD Monthly index). This, combined with an improving rental growth outlook, means that we see potential for further downward yield movement this year.

Floorspace Analysis

The floorspace composition of the centres monitored in this publication, based on GOAD data, is set out above. This information is a useful tool to assess macro changes within each centre, in terms of their overall composition and importantly, to compare the vacancy rates within each town and city.

Figure 3 shows that on average the main 4 largest cities have the lowest share of convenience floorspace (c.7%) and higher shares of comparison and service floorspace (c.55% and 26% on average respectively). In the smaller cities / principal and new towns, there is a much higher share of convenience floorspace (averaging 14% - 16%).

We have analysed the change in floorspace over time by comparing GOAD data from 2008 with the data for each centre from 2014. Figure 4 shows the broad trends across the cities, principal towns and new towns.

During the tougher economic conditions of the last few years, it is noticeable that there has been significant growth in service floorspace (which includes restaurants, cafes, bars, etc) across all centres. This supports the clear trends that non-retail /service space has become increasingly important within town centres since the recession. This is an essential 'real-visit' trend which augurs well for footfall vitality in our centres and helps fight back against virtual retail from home. The coffee shop boom cannot be found online!

Convenience floorspace has also increased within the cities and principal towns, in part reflecting supermarket-led developments, but also the trend in the grocery sector of the 'big 4' chasing market share by opening local/express stores within centres. In contrast comparison floorspace has seen little growth within the cities (with the exception of Aberdeen), reflecting the constrained development activity and has contracted within the principal and new towns overall.

Vacancy rates

In many centres, comparison of the latest GOAD figures with those from last year's publication shows a reduction in the proportion of floorspace which is vacant. The centres with the biggest improvements are Dumfries and Dunfermline, where the vacancy rate has fallen by 6 percentage points. Stirling and Cumbernauld have seen the vacancy rate improve by 3 percentage points, whilst Inverness, Kilmarnock, and Irvine have seen more moderate reduction of 1-2 percentage points.

A marginal vacancy increase of c.1% was seen in Glasgow, Edinburgh and Dundee, with a static vacancy rate in Aberdeen. Across the centres monitored, Edinburgh, Inverness, Dumfries and Irvine have the lowest proportion of floorspace vacant at 8%, closely followed by Aberdeen and Livingston, with 9%.

In many of the Scottish cities and towns recent improvements in the vacancy rate means they are now well below the Scottish average. In fact the overall average vacancy rate across the centres monitored has improved over the last 12 - 18 months, bringing it in line with the average vacancy rate from 2008 (c.14%).

VenueScore Rankings

Figure 5 sets out the latest VenueScore rankings from the Javelin Group, and highlights how these have changed over the last five years. These rankings reflect the retail offer of each venue and their relative consumer appeal. Centres which appear above the line are those which have improved their ranking position, whereas those which are below it have seen their ranking position fall.

Outside London, Glasgow maintains its position as the top ranked retail destination in the UK, a position the city has consistently held over the last five years. The picture for other centres is mixed with some centres slipping down the rankings, whilst others have seen their retail offer/appeal and hence their rank improve.

Edinburgh has slipped six places over the last five years to number 10 in the rankings, although this is likely to be partially reflective of improvements in other major centres such as Leeds, Liverpool, Birmingham and Cardiff, that have all benefitted from major new schemes/refurbishments over this period. This trend highlights the importance of the Edinburgh St James project to the city centre, as originally identified by the Edinburgh Area Retail Needs Study (EARNS) back in 2005, as being a vital component for improving the city centre's retail performance. GVA's planning team has been involved throughout the complex process of securing the necessary permissions for this scheme. Most commentators agree it will arrest this decline and return Scotland's capital as one of the most attractive and successful shopping destinations in the UK. It is estimated that Edinburgh St. James will bring an annual added trade benefit of £251m to the city centre. Edinburgh St. James has benefitted from the Scottish Government's Growth Accelerator Model funding (a form of TIF).

Both Aberdeen and Dundee have seen their rank position improve, up to 12 for Aberdeen (with the opening of Union Square) and to 50 for Dundee. Some of the other centres with a notable improvement in their rank include Ayr, Inverness, Kilmarnock, Dumfries and Livingston.

Centres which have seen the biggest fall in rank include Falkirk, Paisley, Dunfermline and East Kilbride. The perhaps reflects a lack of investment in these towns and competition from elsewhere, (enabling other centres to improve over them) along with typically higher than average vacancy rates.

Retail Pipeline

GVA James Barr's planning team's unique research considers the scale and form of new retail floorspace that is emerging through Scotland's planning system. We collate information from each of the country's 32 planning authorities and 2 national parks on all the Proposal of Application Notices (PANS), planning applications and planning permissions that they have processed in the past year to gain an understanding of the country's retail planning pipeline.

In terms of overall floorspace, the research has identified that total floorspace within the pipeline has dropped by some 171,000 sqm to 1.04m sqm, from 1.2m sqm last year. This represents the lowest level of retail floorspace in the Scottish planning system since our research began in 2009. Figure 6 breaks these figures down between the various application stages; applications, consents and floorspace under construction.

Figure 5: VenueScore ranking

Source: The Javelin Group

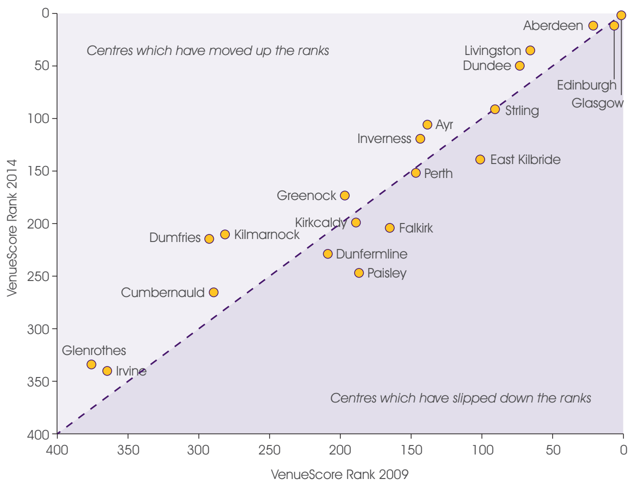


Figure 6: Total floorspace volumes (2009 - 2015)

Source: GVA James Barr

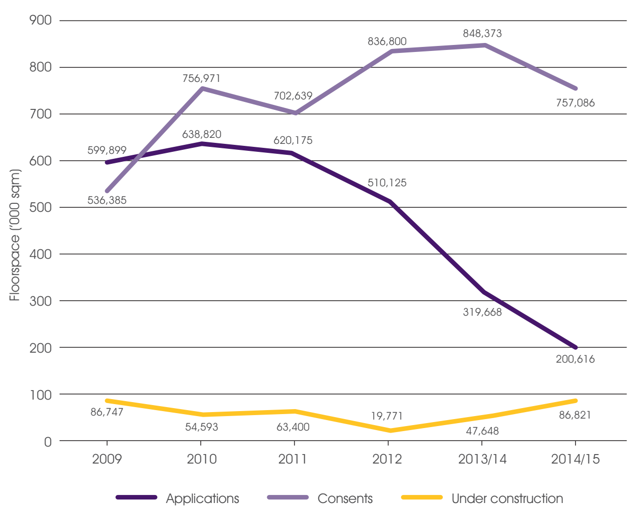


Figure 7: Stage in planning process (% of floorspace)

Source: GVA James Barr

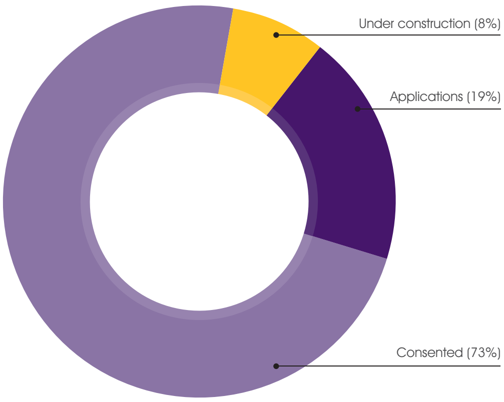
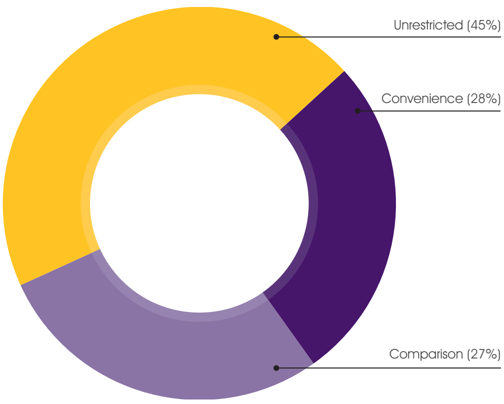


Figure 7: Retail floorspace type

Source: GVA James Barr



The graph indicates a significant reduction this year in terms of floorspace at application stage, which is now less than a third of the amount of floorspace that was at the same stage in the system between 2009-11. The research also identified a drop in retail floorspace with planning permission, the first decline in consented space since 2011.

One explanation for the first trend could be due to changes in the convenience retail market with the major supermarket 'race for space' effectively halted. Changing market conditions and increased pressure and competition from discounters are forcing the big four operators to consolidate space and review business operations to try and bring space back to profitability. Initiatives currently being trialled include sub-letting space to other comparison retailers or to expand the catering and leisure offerings in stores to improve customer dwell-time.

A further finding of the research is the notable increase in the delivery of new retail floorspace. Figures for this year indicate that 86,821 sqm of new space is under construction, which is the highest level since 2009. Retail space under construction now accounts for 8% of the total floorspace in the system. The implementation of a number of larger scale retail schemes have played an important part in this growth. This includes the Buchanan Galleries extension in Glasgow, which at the time of writing has detailed planning permission and construction was due to commence July 2015. However, due to the programmed works to the adjacent Queen Street Station and Glasgow –Edinburgh rail electrification the project has experienced a delay, further indicating the additional challenges that come with development in city and town centres. GVA James Barr have been involved in the planning of this development for more than 10 years and in the successful implementation of the country's first Tax Increment Financing (TIF) scheme.

In terms of the type of the floorspace within the planning pipeline the research indicates that the majority of this is unrestricted (45%), with convenience and comparison space at 28% and 27% respectively. Compared with past findings, this marks a considerable increase in unrestricted space within the pipeline. This is perhaps indicative of the increasing need for developers to seek flexibility in the form of new shopping space they are proposing in order to maximise the opportunities for securing future occupation. It could also reflect the ever-evolving product ranges sold by modern retailers, which no longer fall easily within the traditional sub-sectors of food (convenience) and non-food (comparison).

Finally, our analysis has again indicated that in Scotland Glasgow City Council and the City of Edinburgh Council continue to deal with the majority of new retail floorspace within the pipeline, with Renfrewshire (Braehead), North Lanarkshire, Fife and Aberdeenshire local authorities also featuring strongly.

Commentary

The research shows a clear trend of changes that respond to the economic upturn; some positives for larger centres but some lesser performances on other towns. The retail market continues to be highly dynamic and the emerging trends will present further challenges for all of Scotland's centres in the future. These trends include:

The future role of non-traditional town centres is a highly pertinent issue. Taking the Glasgow context as an example, both Silverburn and Braehead have current proposals that would take their comparison retail offer to well in excess of 1 million sq ft. This combination with their integral leisure offer of restaurants and cinemas makes them very attractive for consumers. These are either currently allocated as, or have been the subject of recent efforts to become, town centres within development plans. The question arises as to what the future scale and offer of such centres could be and what role they may play vis-à-vis Glasgow City Centre over the next 20 years. This underlines the importance of a strong strategic planning policy framework where the roles for each centre and their scope for growth is clearly defined and based on a robust evidence base. Recent legal judgements have endorsed the importance of the Strategic Development Plan in setting out the network of centres for our principal conurbations.

The continued rise of the discounters and on-line retail: While the 4 largest supermarket chains have entered a phase of revising their estate strategies, a number of the discount retailers (e.g. Aldi, Lidl, Homebargains) have continued along a path of increased presence and scale to meet the growing popularity of their offer. The demand from these operators has led to a large number of **retail park/ commercial centre** owners reinvigorating their asset management strategies to examine options to accommodate them. Retail parks in particular have suffered a loss of existing and prospective tenants as the number of bulky-goods retailers and the scale of floorspace requirements have contracted, in response to changing shopping patterns. The growth of online shopping for many bulky purchases has also been a significant factor. These major changes in the range of occupiers available present a number of challenges.

For retail parks the balance will be to prove the locational and use-mix credentials to justify status in the development plan as a recognised commercial centre, or even town centre, and to continue to attract the kinds of tenant that are still interested in the large format store with adjacent parking.

Retail 'need' or 'deficiency' is a particular issue that arises in many of the recent instructions this firm has been involved in for retail developers and investors. Scottish Planning Policy dictates that any proposal falling outwith an existing centre must show that a quantitative and qualitative deficiency is met by the retail floorspace proposed.

We believe that this position can however put Scotland at an economic disadvantage compared with other parts of the UK, where the retail 'deficiency' test no longer forms part of national policy. In our view the current tests can unfairly preserve the status quo position, over the benefits of improved choice for the consumer based on there being a lack of suitable capacity. There might be a case for a future SPP to embrace the approach as suggested in the draft SPP, to focus development plans and decisions on town centre impacts principally rather than the inflexible rigour of a test of deficiency. This concern is further compounded by the reality that few development plans are informed by up to date retail capacity assessments.

Traditional Centres – the high street: With the return of capital investment funding, and in Scotland some innovative Government financing moves to help public infrastructure costs through tax increment recovery, this bulletin's research has found evidence of the return of the larger central mixed use scheme and a clear move towards commitment on site for land assembly, site preparation and construction – all key factors that we have found lacking in our bulletins in the recent past. The Edinburgh St James redevelopment is now nearing site start, but this is a project in its ninth year of pre-planning; with the 100,000 sq m mixed use scheme running through its final detail approval and compulsory purchase, road stopping up etc procedures, before demolitions can commence the 4 year build programme.

As well as progress on larger central schemes, our research also finds evidence of increased vitality and viability in our high streets. The prime pitch frontages are now taking on a role beyond their function as shopping-only streets. Evidence points to the rise of the Class 3 uses across café, restaurant, bars etc. and other service uses. As the National Review of Town Centres (2013) found, their future success is important as they play a key role in the visitor's sense of belonging and community well–being. Scottish Government has previously issued additional policy guidance on town centre enhancement and with this we suggest there is still a key opportunity for those leading public sector efforts on town centre investment to promote viable central developments, prime pitch enhancements, land assembly, development finance and pro-active town centre plans in LDP Action Programmes.

Ensuring successful and sustainable high streets in Scotland will require close collaboration across the public sector, local businesses and catchment community. It will require innovative solutions, ensuring the appropriate blend of retail, leisure, work and public uses meeting the needs of different users. Scottish development plans continue to lead with a policy of control rather than a programme of facilitation. Many policies continue to discourage non-retail uses within centres unfairly, despite our research finding that it is these uses that are lifting levels of activity in high streets, reducing vacancy levels and improving the vitality of the smaller centres.

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