Research bulletin

Unlocking Town Centre Retail Developments

The crisis faced by many town centres and **how to revive them, has been extensively debated over recent months.** The Portas Review made a series of sensible recommendations, most of which have been adopted by ministers.

However, in our view, these palliative measures do not address the reasons why so many town centres are failing to achieve the meaningful new development and investment needed to secure their future.

May 2012

> Local authorities should undertake an assessment of need to expand town centres to ensure a sufficient supply of suitable sites...only if suitable sites are not available should out of centre sites be considered
>
> NPPF

> Unlike Mary Portas, I don't think we can continue to try to muddle through supporting the traditional high street model......right diagnosis, wrong prescription
>
> Phil Wrigley, Chairman of Majestic Wine

> I believe that our high streets can be lively, dynamic, exciting and social places
>
> Mary Portas Review

gva.co.uk

Introduction

The crisis faced by many town centres and **how to revive them, has been extensively debated over recent months.** The Portas Review made a series of sensible recommendations, most of which have been adopted by ministers. **However, in our view, these palliative measures do not address the reasons why so many town centres are failing to achieve** the meaningful new development and investment needed to secure their future.

In the 2000s a record amount of new town centre retail development was undertaken, stimulated by a buoyant economy, strong occupier demand and rising rents and capital values. The development pipeline has now effectively come to a halt and, with it, the catalyst for new investment in town centres. 2012 will be the first year since BCSC records began in 1983 that no significant new centre has opened. A few new schemes are underway and more are planned, but far fewer than occurred a decade ago. Many schemes that were in the pipeline have now stalled.

GVA has undertaken a survey of local authorities which found that around a third do not have any significant development planned (of 5,000 sq.m gross or more). Of those which do have plans in the pipeline, just over a quarter are progressing as originally planned. The rest have been delayed (c. 30%), temporarily halted (c.20%) permanently stalled (8%) or are still at the concept/master planning stage (c.13%).

There are some obvious reasons for this. Town centre retail rental and capital values are in many towns much lower than they were just a few years ago, threatening viability; development finance is very difficult to obtain and occupier demand has noticeably changed. The economic outlook is weak, retail spending has suffered and increasing amounts of spending are undertaken via the internet rather than in physical shops. The harsh reality is that we have too many shops – so why is the lack of pipeline a problem?

While overall space requirements may be shrinking, the major multipliers generally require fewer, larger shops in a limited number of large centres. In many towns, the space that is readily available does not meet retailers' requirements. Without new developments, or qualitative improvements to the existing stock, many locations will struggle to compete in the future. The lack of viable town centre options will in turn create more pressure for retailers to develop their 'clicks and mortar' strategy on line and out of town.

Of course the future of the high street depends on more than just the major multiples. Other Portas initiatives may go some way to alleviating some of the pressures facing town centres. Diversification, markets, and niche/independent retailers all have a key role to play. But without significant new investment, many centres face the prospect of a spiral of decline.

This paper examines the problems facing town centres, and the particular obstacles to new development and how these can be overcome. We highlight the need to identify and actively promote new schemes, where appropriate and the need to ensure that developments are realistic, viable and deliverable. We recognise that new development will not be the answer for many towns, and there is no 'one size fits all solution'.

We hope that **this paper will contribute to the debate, and help to unlock much needed new investment** in our town centres

The challenges facing town centres

The retail sector has undergone fundamental changes in recent years and **today's market is very different from 5 years ago** when spending was booming and development activity was buoyant.

The current difficult market conditions have effectively halted the development pipeline, which in the absence of public sector funding has left many towns less able to respond to the structural problems they face. The slowdown in retail spending, caused by the severe recession, is compounding the effects of long term, fundamental shifts in how and where we shop. This has 'greatly exacerbated what had become a downward spiral for many high streets'. Many towns are being left with a surplus of secondary space which is not fit for purpose (BIS Understanding High Street Performance, December 2011).

With weak spending, the competition for sales is fierce and town centres have been losing sales to out-of-centre locations, and the internet. The UK is now Europe's leading e-retail economy (The Guardian, 28th April 2012). According to ONS the internet now accounts for 10.7% of sales by value, and in volume terms, non-store sales (which are predominantly via the internet) represent c.12% of total sales. Experian forecast this will rise to 15% by 2018, but no one can predict the level at which its growth will top out.

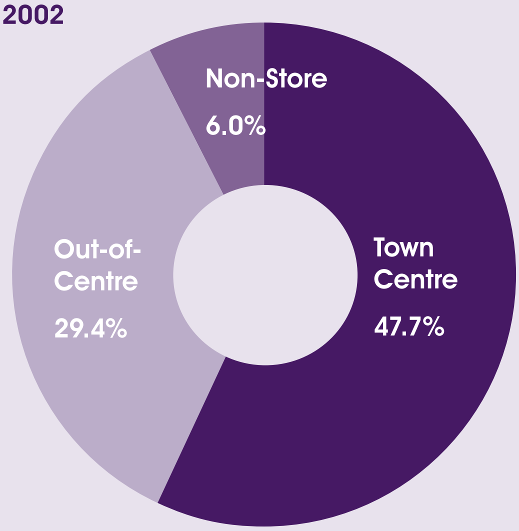
Town centre spending has dropped from almost half of total spending to just under 40% over the last decade. This trend is set to continue, and the impacts have been felt most by middle ranking and smaller towns, as noted by the BIS report. Town centre floorspace and unit numbers fell by circa 14% over the last decade, mainly between 2007-12. In contrast, out of centre floorspace grew by over 23% over the same period (Verdict 2012). Town centre floorspace as a proportion of total floorspace has reduced from 55% to 48% (2002-12). The focus of development activity is increasingly outside town centres, despite the 'pro-town' centre planning policies in place since the mid 1990s. Recent figures from Trevor Wood show some 10m sqm of retail park space was built last year, up from 9.9m sqm in 2010. This is occurring at a time when figures from the Local Data Company show 14.6% of high street shops are vacant.

Presently there is little town centre development activity to counter balance this, leaving town centres unable to respond to the threat from other retail channels. Recent research by the BCSC found that that 2012 will be the first year in three decades that no significant new town centre scheme will open. The pipeline for 2013 and 2014 remains subdued. Looking ahead the report shows around 1.5m sqm of shopping centre floorspace in the pipeline for 2015-2019, although 40% of this will be extensions to/ reconfiguration of existing floorspace.

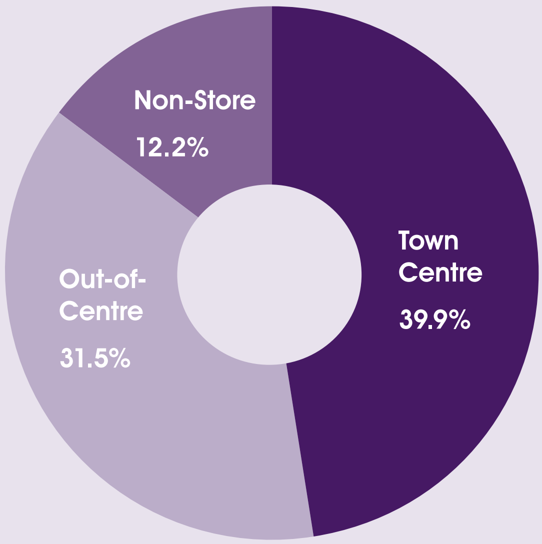
The notable exception is schemes anchored by foodstores. GVA's survey evidence shows that of the schemes which are progressing, (either with an original or a delayed opening date) almost three-quarters are anchored by foodstores.

Share of retail spending by location (Verdict Research, 2012)

2002



2012(e)



This represents a key opportunity, particularly for small and mid sized centres which are being left behind in the ongoing polarisation of comparison retail activity.

Of course, it would be naïve to expect to reverse the structural changes taking place in the retail sector. Not all centres can support new development. But where the stalled town centre development pipeline is unable to respond to retailers' requirements, it inevitably deflects retailer demand to more efficient, cheaper out of centre options. This further erodes demand in the centre, and so the process continues.

Responding to **the challenges**

We have highlighted the challenges facing town centres **but how should they respond ?**

A series of measures to address high street decline were put forward by the Portas Review. These include initiatives to drive footfall and make better use of obsolete space. Other ideas, such as traffic calming; designating a BID; or providing a market may all help centres to adapt and respond to some of the challenges facing them.

In some towns; the market will no longer support previous, ambitious plans. In others, it may support scaled back or phased new development. And in some case, the fundamentals may still be right, but innovative financial measures, such as TIF may be required. The key issue when considering new, or stalled schemes, is understanding which circumstances apply in each case.

These issues can be presented as a pathway to unlocking development potential, as follows:

Assessing market potential:

Can demand be identified – does any opportunity exist?

Where an opportunity exists –

Is this clearly articulated / defined?

Delivery:

How should the site be delivered?

Investment:

If all the fundamentals are in place, how do you unlock funding?

Step 1: Assessing the market potential

With the growth of internet sales and with many leases up for renewal in the next five years, retailers are looking to consolidate store portfolios and dispose of less profitable stores. This presents challenges and opportunities.

A decade ago a retailer looking to expand across the UK would probably set their sights on 300-500 locations. The power of e-commerce is such that this number of locations is no longer necessary. Retailers are now looking for representation focussed on key target areas, generally within the top 100 locations. This new model greatly reduces the operating costs for retailers, but accelerates the migration of retailing towards the bigger centres, where larger footprint stores can be accommodated.

In many towns these requirements simply cannot be met without significant redevelopment of the existing stock. Where retailers cannot see this happening they are looking at out-of-centre sites to fulfil requirements.

Within these broader trends, there are still significant 'gaps' in retailers' networks, and priority requirements for some towns/catchments still remain unmet. The presence of an affluent and growing catchment may also trigger retailers' requirements for smaller centres. However, the main driver is consolidation, and the demand for larger, more efficient units which are accessible to existing core catchments. If these conditions exist, there is an opportunity for new development.

Some towns are simply over-shopped, and/or unlikely to capture the interest of the major multiples. In these cases, LPAs may need to put plans in place to consolidate the retail core of the town centre, and allow more A2 and A3 uses and/or change of use to leisure, residential and community uses. In some towns there may be market potential to support limited redevelopment and provide qualitative improvements, and to target niche/specialist sectors. But in each case the market potential and deliverability will need careful consideration.

Where there is localised growth in population and expenditure this may create market potential to support new development to increase the quantity and quality of the retail stock. New urban extensions, for example, may trigger retailer demand. There is also evident growth in certain key locations, e.g. Central London, triggered by population and spending growth and major infrastructure projects.

But every case requires careful analysis and a clear view of what is planned in competing towns. Many town centre planning strategies are based on forecast spending growth and theoretical capacity projections. Such analysis may give an indication of where market conditions may support new development. However, this needs to be supported by a clearly defined and realistic market proposition.

> "'Capacity' forecasts need to be supported by a clearly defined, realistic market proposition. Where this cannot be identified, major new retail led redevelopment is not a realistic option"

Step 2: Framing the development opportunity

The next, and critical, step is to frame the market potential into a deliverable opportunity.

If the market opportunity is clearly defined, the key requirements will be clear. This may be for key anchor(s) not present in the town, or for relocations to enable existing retailers to meet their requirements. Local authorities may need to accept that new development can lead to short term impacts on other parts of the centre, and develop a co-ordinated strategy for dealing with these.

Retailers requirements will determine the size/number of units which are supportable, the level of new parking, and the need for effective linkages into the primary shopping area (PSA). These need to be translated into an opportunity which is suitable, viable and available.

Key considerations may include:

- Is there a suitable opportunity? Size, accessibility, prominence and linkages with the PSA
- Key land ownerships and owners aspirations. What factors may give rise to an opportunity, and is CPO available?
- How will commercial and design/conservation conflicts be reconciled? How does the local planning authority (LPA) intend to resolve these?
- Is development viable? What are the site assembly costs? Construction costs? Other exceptionals?
- Is there sufficient political and officer commitment to the development and expertise to deliver it? Town centre development can be complex and time consuming.

The Government's planning policy has consistently entreated local authorities to take a proactive approach to promote new development and resolve these and other issues. The fact that over 30% of Councils we surveyed have no plans, suggest this message is not being applied consistently.

The NPPF makes clear that where there is market demand, and the LPA cannot clearly identify suitable, viable and available town centre opportunities, it will be legitimate to consider out of centre alternatives.

Whether or not they are enshrined in the existing local development framework (LDF) or a new style 'local plan', local authorities cannot expect to progress town centre development aspirations to the delivery stage if they do not have a clearly defined opportunity, and the political will and resolve to safeguard and pursue it.

Step 3: Delivery

Where an opportunity is identified, what are the key steps towards delivery?

Planning and development briefs

The production of site-specific planning and/or development briefs can serve to promote town centre development by distilling policy parameters in the context of market realities and the broader aspirations of local decision makers. This provides visibility and certainty to the development industry, de-risking the planning process and removing barriers to investment. Such briefs effectively 'bridge the gap between the development plan and a planning application'.

> "Briefs that are formally adopted by Local Planning Authorities **carry significant material weight.** However, if the development fundamentals are sound, unadopted briefs still provide sufficient guidance and certainty to promote development; **particularly when the site comprises public sector land ownership**"

At a time when competition for investment and development is fierce between town centres, it is critical that briefs are kept simple, well structured, commercially realistic and (within reason) flexible to fluid market trends. In cases where underlying development and delivery issues are more complex (e.g. sites in multiple ownership), more comprehensive briefs may be required.

Given town centre development is often complex, such plans can be vital both in unpicking key issues and optimising the development opportunity. When produced in partnership with the private sector, they also perform the vital function of aligning public and private sector interests.

Viability/delivery considerations

Critically in a constrained market, the development opportunity should be underpinned by a sound assessment of viability and delivery issues. This exercise distils key constraints and reviews options to resolve these, and should provide a pathway to development. This process should also manage stakeholder expectations, including potential S106 and Community Infrastructure Levy (CIL) obligations.

The assessment needs to review in some detail the development's financial profile throughout the delivery cycle; from pre-planning through to construction, completion and onward into the property lifecycle. By its nature, town centre development is resource intensive for prolonged periods before substantive income is received; this cashflow profile weighs heavily on underlying feasibility. At a time when development finance is so heavily constrained, the importance of rebalancing cashflow through innovative methods is magnified.

A common solution is to break a large scheme down in to feasible chunks, leveraging off enabling development wherever appropriate. In the case of town centres, the early phases may not be the most valuable. It may be a key scheme anchor such as a major retail or leisure attraction to attract footfall. In some cases direct public sector intervention may be required (see later).

Local authority intervention – use of CPO, assets, disposal and procurement routes

Increasingly the emphasis is on key stakeholders to provide a clear pathway to delivery, particularly where public sector intervention is considered necessary, or where public sector land/equity is required. Setting a pathway may include addressing procurement and/or State Aid issues, alongside more fundamental principles of delivery to help to provide certainty to private sector stakeholders.

A key issue is deciding the role local authorities should play in promoting development, including: the selection and potential assembly of sites; using public sector assets and/or funding; investing directly, controlling development by way of agreement; and potentially taking on a direct procurement role. These may all be considered as part of a comprehensive town centre delivery plan.

Deciding upon direct intervention is a complex area of delivery and one that requires careful consideration of development, legal and financial parameters by a multi-disciplinary team. Key questions include; whether an OJEU process will be necessary; and if so which route is most appropriate; what will be the impact on private sector interest; and what are the timescale and cost implications for public and private sector?

The private sector has become increasingly unreceptive to high risk and lengthy OJEU procurement processes (in particular Competitive Dialogue) since the property downturn in 2007. In cases of marginal viability and/or delivery these perceptions are magnified. Town centre or retail-led schemes are often complex and marginal, meaning that a flexible, open and drawn out procurement process is required to allow for scheme refinement and negotiation – precisely what the private sector may resist.

Equally the Restricted OJEU procedure, which can be executed in a matter of months, may not afford the design or negotiation freedom required when scheme specifications are fluid (for example if the scheme promoter wants to allow the developer to evolve their own scheme once selected). Whilst a range of options are available should an OJEU process be considered necessary; the characteristics of the scheme will often dictate that only a few options are suitable, after which it is usually a decision for the contracting authority, in light of legal and commercial property advice, to balance risk and reward in choosing the correct procurement.

> "Throughout the evaluation of delivery routes, issues and options should be assessed against the overriding objectives of the scheme promoter(s), placed in the context of scheme dynamics (physical, economic etc) and legal parameters"

The plan may also determine that compulsory purchases are required to enable delivery, and in that way the plan provides a key part of the evidence base necessary to embark on such a process.

Step 4: Funding

Continuing uncertainties about the economic outlook and occupier demand have put a premium on risk aversion. Investors are now principally concerned with income security, length of lease and covenant strength.

The current market conditions favour stronger towns with tenants that are multiples rather than independents, and long leases without break clauses (preferably with index linked rental uplifts rather than open market rent reviews). Smaller schemes in weaker towns, with low occupier demand from multiples, are more difficult to develop.

There is less availability of development finance from the banks, since the credit crunch, and the subsequent economic recession. Over-lending on property prior to 2007 has been followed by de-leveraging and little new bank lending on investment property – particularly new development due to the higher risks involved. This situation is unlikely to improve significantly for the foreseeable future and compounds the viability problems referred to, particularly for town centre development.

In these circumstances, it is self evident that where there is no occupier demand, or clearly defined, viable opportunity, it will not be possible to secure funding for new development.

In the recent GVA survey, where town centre retail development had stalled or been delayed the key problems stated by local authorities were development viability (45%), site assembly (28%), development financing and/or long term funding (27%) and weak occupier demand (23%).

However, where viable opportunities exist, with a clear delivery pathway, local authorities can play a key role to unlock them, using their assets, powers and covenant strength.

- Local authorities can use their sites to enter into joint ventures with private sector developers, which will give the local authority greater control over the type of retail development and tenant mix provided in the town centre. This also enables the local authority to use future profits to cross-subsidise schemes that are less profitable. Joint Ventures or Local Asset Backed Vehicles (LABV) have seen increased popularity with local authorities as they restructure their own assets and use them to stimulate development.
- Taking head-leases over new or existing retail space either to secure a greater diversity of retail tenants, whose financial strength may not be suitable to investors and funds (e.g. creating market areas, antique malls and art galleries), or to unlock funding. The local authority, in discussion with the landlord, would source tenants who would provide a greater shopping experience for the consumer. The local authority would take the risk on the tenant defaulting on the lease payment.

"In the recent GVA survey, where town centre retail development had stalled or been delayed the key problems stated by local authorities were development viability (45%), site assembly (28%), development financing and/or long term funding (27%) and weak occupier demand (23%)"

> Funding from future business rates can be used not only for development infrastructure but also for public realm and to increase the shopping experience/environment.
>
> The combination of business rates retention and TIF structures will give local authorities greater ability to support retail development. Under current government proposals these benefits will be available to local authorities in 2013

- Encouraging the use of Business Improvement Districts (BIDs) to improve public realm and diversity of tenants (including informal market areas and attractions). BIDs can also be used in combination with local authority head-leases/pre-lets to provide a buffer fund to encourage smaller tenants and provide a greater retail diversity.

  While not a direct means of development funding, a BID may help to establish improved conditions for attracting further investment.

- Purchasing poorly-performing, existing retail properties to provide a greater mix of tenants or incorporate these properties into a wider regeneration objective.

  As the owner of the retail property, the local authority will be able to directly influence the retail mix and provide funding to kick-start development. Once these properties have been re-let and have a stabilised income they can be sold into the investor market returning the funding to the local authority.

- Providing business rate relief and de minimis funding (e.g. rent reductions) to small occupiers, or grants to occupiers. This will enable smaller tenants and start-up retailers to establish themselves without the full initial financial burden. This intervention would be for a short period of time (e.g. 3-5 years depending on location). This would provide a greater diversity of shops and hence increase the shopping experience for the consumer.

- Providing debt funding to developers for retail developments that are having difficulty in securing debt finance from banks. Local Authorities, the Homes and Communities Agency (HCA) and central government are providing and implementing debt and equity funding to assist development where funding is not currently being provided by the private sector. These loans are structured similar to bank loans and will need to be State Aid compliant.

- Using Tax Increment Finance (TIF) or business rates retention to provide funding for retail developments, which are either less viable due to high infrastructure costs or contain unprofitable elements. Local Authorities will have greater control over their business rates income in the future, particularly relating to increased business rates due to new development (retail, commercial, industrial).

Conclusions

There are significant challenges facing the UK's town centres arising out of the economic downturn and long term structural change. The traditional role of town centres is changing forever. For some, a diminished retail function is inevitable. All centres need to adopt and evolve, and need investment to do so.

To date much of the response to these challenges has been palliative. The Portas review identifies a range of measures, but misses the point that the development pipeline which underpins private sector investment in town centres has ground to a halt.

The Government has restated the longstanding 'town centres first' planning policy, but the clear focus of development activity remains out of centre, to complement on-line sales growth. Unless there is a pipeline of suitable, viable and available town centre opportunities, and the Government enforces its policies, this trend will accelerate.

There is a legacy of stalled schemes. Many have no prospect of delivery. Others need a radical rethink. In the current economic conditions, it is not feasible or appropriate to attempt to subsidise fundamentally unviable town centre development, or to unnecessarily curtail retailers space requirements. However, given the critical importance of new investment in our town centres, it is vital that existing and new opportunities are re-evaluated.

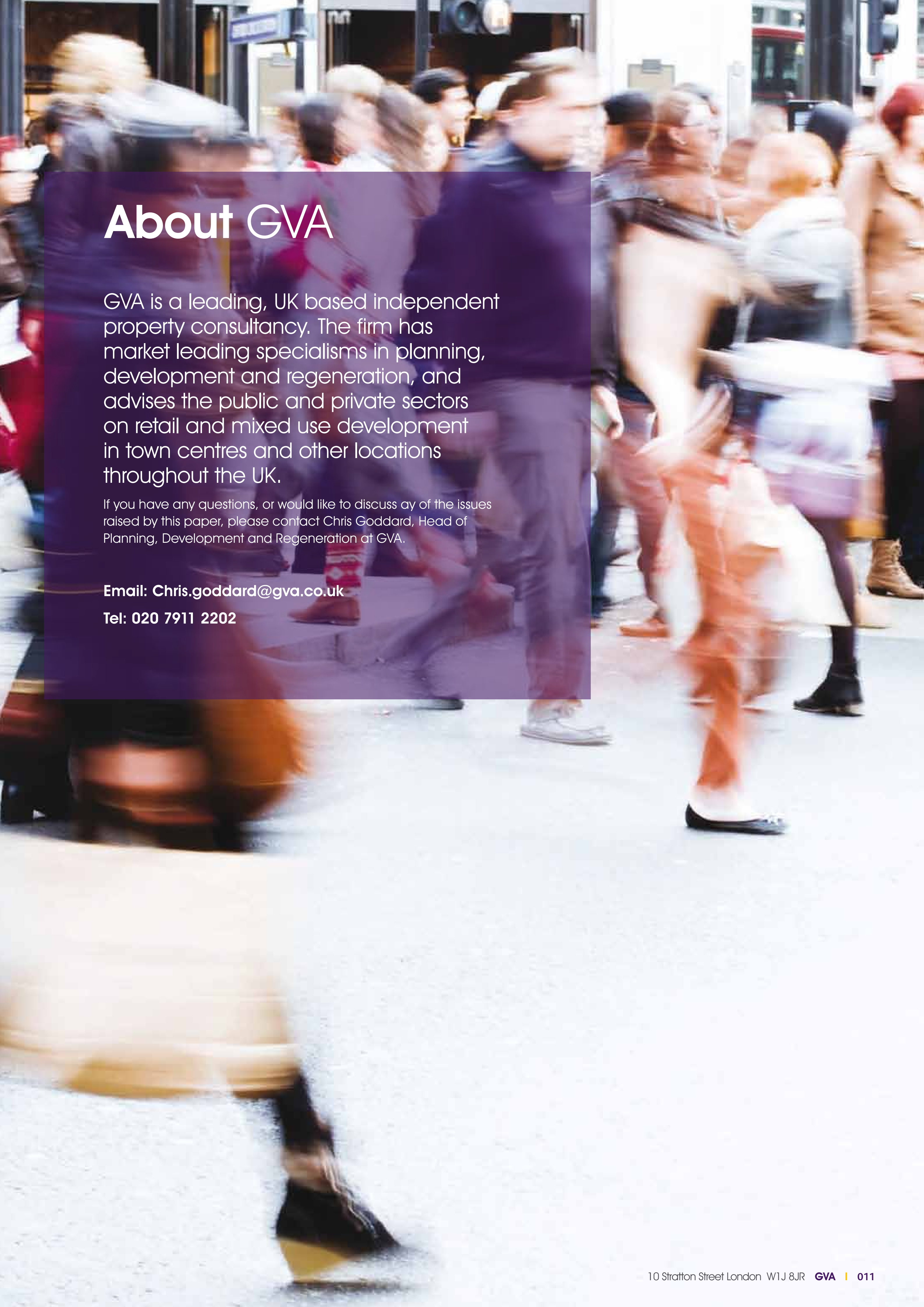
> "There must be clear evidence of market demand. This needs to recognise the ongoing market consolidation, and retailers requirements. There will be winners and losers out of this process, and local authorities will need to make difficult decisions about their priorities. Unless there is a clear market opportunity, new town centre development will not be deliverable"

Even where there is demand, there needs to be a clearly framed development opportunity, which is suitable, viable and potentially available. The LPA has a key role to identify and unlock opportunities, in partnership with the private sector. Where opportunities are identified, politicians and officers will need the long term commitment and expertise needed to safeguard and deliver them.

The public sector has a key role to play, translating the opportunity into reality, de-risking the planning process, considering viability/deliverability, procurement options and site assembly. More direct intervention, through asset rationalisation, taking head leases, providing direct funding and tax increment financing are all options to unlock new development, provided the fundamentals are sound.

New development is not a panacea for all the challenges facing our town centres. Nor are the range of other measures advocated in the Portas Review. There is no 'one size fits all' solution, and in reality the retail function of many traditional centres faces inevitable decline, whatever initiatives are applied.

However, there is much more that can and should be done where real opportunities still exist, given the political will and commitment, using the range of innovative mechanisms available. It is too early to write off our town centres as being in a 'death spiral', but for some that is a very real risk without urgent action.



About GVA

GVA is a leading, UK based independent property consultancy. The firm has market leading specialisms in planning, development and regeneration, and advises the public and private sectors on retail and mixed use development in town centres and other locations throughout the UK.

If you have any questions, or would like to discuss ay of the issues raised by this paper, please contact Chris Goddard, Head of Planning, Development and Regeneration at GVA.

Email: Chris.goddard@gva.co.uk

Tel: 020 7911 2202

London West End
10 Stratton Street
London W1J 8JR

London City
80 Cheapside
London EC2V 6EE

Belfast
Rose Building Third Floor
16 Howard Street
Belfast BT1 6PA

Birmingham
3 Brindleyplace
Birmingham B1 2JB

Bristol
St Catherine's Court
Berkeley Place
Bristol BS8 1BQ

Cardiff
One Kingsway
Cardiff CF10 3AN

Edinburgh
Quayside House
127 Fountainbridge
Edinburgh EH3 9QG

Glasgow
206 St Vincent Street
Glasgow G2 5SG

Leeds
City Point First Floor
29 King Street
Leeds LS1 2HL

Liverpool
Mercury Court
Tithebarn Street
Liverpool L2 2QP

Manchester
81 Fountain Street
Manchester M2 2EE

Newcastle
Central Square
Forth Street
Newcastle upon Tyne NE1 3PJ

Published by GVA
10 Stratton Street, London W1J 8JR

GVA is the trading name of GVA Grimley Limited and is a principal shareholder of GVA Worldwide, an independent partnership of property advisers operating globally
gvaworldwide.com

08449 02 03 04
gva.co.uk

08461