ROUNDTABLE

New How: Perspectives

Delivering the town of tomorrow

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SHOOSMITHS

Introduction

We all need our town centres. But more than that, we need our town centres to work better for us.

As consumers grow increasingly comfortable with online shopping, the realisation that our towns are over-reliant on retail is being played out at a national level. No longer can we expect empty retail units to be snapped up by new tenants in a matter of weeks. The office market faces similar challenges, with office workers now demanding greater flexibility and a blending of time spent between office and home, causing office occupiers to assess how they use their space and how much space they need. And what about residential? Much has been said about the pandemic prompting a 'race for space', but will urban living be key to bringing footfall back into our town centres?

Social behaviours have changed, and our town centres need to change with them, or risk being left behind. Greater flexibility and more variety of uses are needed but, with so many stakeholders involved, delivering a joined-up vision for a town centre is not easy to achieve. Issues around funding, shifts in yields, disparate ownership and an inherently slow-moving system are challenges that need to be overcome. But one thing is for sure, the town of tomorrow needs to be led by the consumer. Only through developing urban neighbourhoods which better reflect the needs of the modern consumer and throwing aside dated concepts of what worked in the past, will we see the true revival of our town centres.

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Shoosmiths recently hosted a roundtable debate with various stakeholders to discuss these issues and more, analysing what is really required to deliver the town of tomorrow. The participants were:

- **Stephen Martin**, Senior Estate Manager – Boots
- **Neil Hockin**, Director & Head of Shopping Centre Leasing – Lunson Mitchenall
- **Michael Whitney**, Head of Development – Ellandi
- **Stuart Heslop**, Managing Director, Real Estate Finance, Scotland & North England and UK Housing Finance – RBS
- **Scott Cardwell**, Assistant Director for Development - Doncaster Metropolitan Borough Council
- **Ian Fletcher**, Director of Policy (Real Estate) – British Property Federation
- **Stephanie Smith**, Director - Portfolio Operations, Europe – Invesco
- **Janette Speed**, Partner & Head of Real Estate (Scotland) – Shoosmiths
- **Chair: Nathan Rees**, Partner – Shoosmiths

Do our town centres have a bright future and how do they need to change?

Ian Fletcher – On the retail side, clearly there has been an evolution of the sector over the last decade or so: more mixed-use, retreat of goods retailing and multiples, more independents etc. The independents and leisure, in particular, have been hit hard by the pandemic but I predict that they will bounce back strongly. People want to get out and they want to shop locally, and there will be lots of entrepreneurs wanting to start up new businesses on the high street.

For the property sector, the big challenge has always been around how to attract investment into high streets. We have put forward proposals, such as town centre investment zones, but the fragmented ownership of a town centre and the small unit sizes makes it difficult for the larger players in the market to be able to find the sufficient scale of investment opportunity.

On the policy side, various pots of capital are being thrown at local authorities, such as the towns fund, levelling up fund, high street fund etc, however there is a concern that local authorities – who have no shortage of vision – lack resource and so will struggle to find time to submit competitive bids for this money. We've welcomed the new class E and the flexibility between different commercial uses that brings, however our members have been concerned with the government's new permitted development right allowing commercial to convert to residential in a non-planned way. I'm not against residential in our town centres and high streets but, if it's not planned, it tends to impact badly on placemaking, retail frontage and the like.

The elephant in the room, though, is around business rates and hopefully we'll see more direction from government on that. Levelling up is really important for town centres; those town centres that struggle often tend to do so because there isn't the wealth and income in the local area, so levelling up is really important to the town centre agenda.

Finally, if retail is in evolution then offices is in revolution. In 1981, 1.5% of the population worked mainly from home. In January 2020, it was 5.7%. And then in the last year, we've seen 40-50% of office workers working from home. That is a huge revolution that we can't turn the clock back on. So, what does that mean for the sector? Our members are saying that they'll be using offices in different ways, that there'll be a flight to quality and that people will want less but better space. There may be moves to more serviced office space that is closer to home, rather than in big city centres, and there will be greater demand for flexibility. In short, there is a huge amount of change going on in this area.

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What needs to happen to ensure our future towns create more diverse centres which can better serve their communities?

Neil Hockin – There is no 'one sizes fits all' solution. All of us and national and local government need to start thinking on a more localised basis. Different towns, cities and villages need to achieve different things and different catchment populations have their own thought processes. One of the things that concerns me about some of the central government funding is that it will dissipate out but get spent on very generic solutions. We have to think about what the local consumers want as we will have to drag them away from their computers and give them a really compelling story to get them back into the town centre. For me, that sits somewhere between the public sector and private sector in terms of driving investment back into towns. Most retailers tend to follow the money. So, a lot of the shopping centres we have let have first had anchor tenants because other retailers then follow. That world has changed completely, and we now need to put consumers back into town centres first through adding alternative uses such as doctors' surgeries, medical facilities, libraries etc. Retailers will then follow.

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Scott Cardwell – On the funding issue, central government is spraying cash at local authorities at the moment for use on high streets and town centres, but it is in multiples forms. It gives no real opportunity for local authorities, which are essentially place-shaping organisations, to do tailored programmes to regenerate their town centres. Some of the funding streams have been great, but they require you to deliver the outputs that have been dictated. However, what's appropriate for Doncaster might not be the same as for Edinburgh or anywhere else. A move from central government to a larger, longer-term pot of money that allows for tailored use by individual local authorities would be more beneficial.

In Doncaster, all of our regeneration projects in recent years have been around trying to diversify the town's offer. It's about trying to do more things around the leisure and creative industries, and we've invested in things such as new theatres, new cinemas, new libraries etc. It's been less about going purely down the retail route, which we've left to the private sector. Our biggest challenge is to diversify the town and make sure it is able to give consumers a vibrant experience.

We are, however, starting to see some green shoots from central government around attaching weight to the creative and leisure industries, but there is still a real lag. A lot of these funding schemes are still all about GVA uplift and jobs. We need to create towns that feel vibrant but also look vibrant and, at the moment, public realm doesn't score high on some of the funding streams. But if you create a nice place, people will want to come and spend time there, and investors will come in off the back of that. So, I'd like to see a bit more foresight in terms of reshaping our centres, shrinking existing retail and putting in parks and spaces that will create growth corridors for investors to come in behind.

What would attract investors and occupiers to a scheme which has a broader placemaking focus and what issues would need to be overcome?

Stephanie Smith – One of the important things to recognise whenever you are looking at a scheme, whether it's a placemaking scheme or an individual building as part of a greater community, is to really think about the demographic and the commitment you are making to that area. When engaging on a new project, a main focus for us is to align ourselves with high quality developers who are prepared to 'think outside of the box' and work with us to think more about where we should be going with our developments, pushing past the basics and looking to improve with each step. It is not just in the UK, either - we've recently launched two buildings within a greater placemaking scheme in Copenhagen where there has been an incredible intent to build a viable community. The overall estate offers a kindergarten, community garden, well thought through commercial businesses, grocery stores and other great features which help create neighbourhood.

At times, there is perhaps a hunger to get places done and to just think about that asset, but where it can fall short is in working with planning departments where they say, for example, that you need to have a commercial unit in a particular spot but that you are limited to 0.4 parking spaces per tenant. The conundrum is how are you supposed to attract a commercial tenant if you don't have sufficient parking for the residents, let alone the commercial space? In certain central locations, parking may be less of an issue and, from an ESG perspective, that is something we need to consider. However, if you are in a zone with a high commutability rating, then you still need to account for that. That is where we need to get more aligned with the planning departments and get them to realise that we are trying to build something, and maybe the answer is to meet halfway. Ultimately, you are trying to get commitment and longevity, otherwise you're just going to have another vacant store front. An empty store front in a neighbourhood which already had a barren high street will be even more of an eyesore and potentially impact letting up processes. I do think there is a huge amount of potential if looked at with flexibility, reality of practice, an eye on the full vision of the area and the needs of the demographic profile.

> **"You've got to look at the destination type and be realistic about its purpose and what a destination is there to do.**

Stephen Martin – You've got to look at the destination type and be realistic about its purpose and what a destination is there to do, and there are all sorts of factors which come into that, such as heritage for example. As a retailer, Boots is perhaps different to most other retailers in that we are present in pretty much every destination type, but from a more general retail point of view, it is always about investment. There will be some retailers who think primarily about returns but there will be others who want a blend that with more of a customer satisfaction element. But one thing that is consistent across all of them is cost and budget, and no retailer likes unexpected costs coming through. So, it's really about trying to control those cost elements and trying to take that risk away.

Coming out of Covid, we need to get a full twelve months of trading behind us, as that will be a really important year for the industry to understand what the start of the new future looks like, with base trends to work from. Because, at the moment no one really knows.

From a leasing point of view, rating has to change, and I don't think anyone can argue differently. Lease structures work well, to a point, between turnover or traditional lease type, but I think it is going to take time for retailers to rebalance the shift toward turnover and establish confidence to understand what works best for them. Again, different destination types will vary the preferred rent basis. I appreciate that I'm assuming a very broad brush, but I don't believe that the property industry respects what turnover rents could actually achieve. Landlords often quote leases being X% turnover but to me that's missing the point. A landlord and a tenant would need to share and understand the revenue potential and set a percentage against that figure whilst a minimum guaranteed rent should be linked to footfall. It's then the retailer's issue if they can't maximise the trading opportunity and the landlord's problem if they can't deliver customers, but I fully appreciate this is not a model that would work everywhere.

Ultimately, retailers want a level of certainty so if you take the 54-act element away, how do you maintain certainty for retailers and give landlords flexibility as well, particularly where there's a high level of initial capital investment?

> Town and city centres require constant investment to make them relevant.

Michael Whitney – Rents and lease terms are what they are. Whether you switch to a turnover rent or have a more traditional rental product, the rent being produced is still the same. The big question is around yields and where yields go. At the moment, you have some town centres and shopping centres that are actually trading well, but their values are being reduced because of people's perception of yields in the market. So, if we take Stratford, for example, that is still trading well and turning over a lot of income because it is a community-based shopping centre, so there are banks in there, food stores, cafes, a bit of everything. It is a place that people around Stratford will go and visit. Now, if you look at that on a pure valuation perspective, the valuer is going to hit that shopping centre regardless of the fact that its turnover is doing well (taking Covid out of the situation). So, for investors, we are beholden to that yield movement. Valuers are knocking values regardless of what the underlying asset is actually doing, and that's what is causing a bit of hesitation in the whole retail market. Not all retail is struggling, some sites are doing really well and you'd think that those asset classes would be good for investment but, because of the wider yield markets, it is causing a problem from an investment perspective, which goes back to the point around local authorities getting money in to help drive regeneration and bring other use classes in. A knock-on effect of that though, is that some long-term investment funds can't invest in all of those use classes, as they can't get the critical mass they want or the size of investment they need. To do that, they'd need to diversify the uses and they can't always do that within their funds.

Neil Hockin – Town and city centres require constant investment to make them relevant and this is particularly pertinent now as we seek to encourage shoppers back on to our high streets. Retail and leisure landlords are under enormous pressure with over £8 billion of unpaid rent as a result of the government moratorium on the capacity for landlords to pursue tenants for unpaid rent. They have also been hit by CVAs, yield movement and changing deal structures. The investment market for town centre retail property is slow, and the next tranche of purchasers are likely to be opportunist investors with a shorter hold window.

Whilst mixed-used regeneration is a longer-term option, investment from the commercial sector into retail is likely to be limited and local authorities and landlords are going to have to work together to provide a compelling offer for their consumers.

Michael Whitney – I agree. That is the issue that is compounding the change of the high street. There are high streets out there that are over-subscribed to retail, and which need to bring in other uses. But where it has worked well is in those towns which have found an ability to adapt between the day and the night and also between the seasons. Creating flexible neighbourhoods which means you have people there at different times of the day. One of my biggest bugbears about a lot of town centres is that they are like defensive castles, flanked on either side by a big car park and with shops in the middle. We need to break that up and create more connectivity through town centres, allowing more uses to naturally blend into that. If you provide the flexibility in that space – and the new class E helps with this – it then allows the right type of fit for a town centre.

From a funder perspective, what will make our town centres investable again?

Stuart Heslop – When you look through the various asset classes, leisure has been hit the hardest and arguably will come back the quickest. Retail has been going through a correction for a number of years and clearly this pandemic has accelerated that. It has become about destination shopping, and some of that will be in towns, some in cities and some in shopping centres, as the big well-known shopping centres will remain strong. We have undoubtedly seen yields shift in that space, part of which is down to investor sentiment and part down to centres that are over-rented. So, you are going to see a correction in value in even the best centres, with some of the lower-performing centres having seen a significant drop in value which is damaging for both equity and debt.

Offices also has a sense of becoming a destination market as well. The death of the office is over-played and there is certainly a demand for people to get back to the office. The most attractive office settings will be London and the big six cities. If I reflect back to the start of the Covid crisis, I had in mind that business parks would be the place to go as you could drive there in your own car and be socially distanced when you got there, but the younger demographic don't necessarily have cars. They are reliant on public transport so they will always want to go back into their town and city centres and modern office settings.

This then requires occupiers to be more fleet of foot on their lease terms and more flexible, in all settings from retail to leisure to office. So, unless you are having a building developed for you and you need to sign up to a fifteen-year lease in order to get someone to build it, then ten years with a five-year break will become common. That is actually more difficult to lend against. So, everything becomes location-specific, because if you are the investor or the lender, you want to be confident that, when you come to the five-year break and the tenant wants to depart, then someone else will come straight into that building. If you look at retail and leisure, even a long lease doesn't give you confidence. It's the location that is important now because retail and leisure operators are so susceptible to changing consumer habits.

Only once retailers and leisure operators begin to trade properly again will we see whether people flock back to the shops or not, and that takes a bit of time to assess. But we need some stability to give lenders confidence.

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Much has been written about the repurposing of retail to residential in town centres, but how can this be done in a seamless and organic way?

Janette Speed – The residential market over the last year has actually been really busy in Scotland, particularly with government-backed funds that are looking to roll out mid-market rent properties across the central belt. Student accommodation providers are active in rolling out BTR schemes in city centres, and co-living projects are also growing, which is an interesting area of the market. But it is clear that we have a demographic issue across the UK that demands attention, with the younger generation looking for affordable housing post-university, as well as the ageing population looking to downsize or move into care, but there is nowhere for them to go. We need to look at that, and merge and introduce all of these different strands into the urban landscape. I suspect it will take twenty years for this to play out, but the political imperative is such that it won't disappear off the agenda.

> **As more people look for lifestyle and flexibility, it is becoming more about subscription living with a variety of services from which the residents can benefit.**

Stephanie Smith – There is clearly a housing shortage and a need for mid-market housing, but with a residential scheme it is about what you make of it and identifying the local needs. Regardless of whether it is a "purpose built" or an office or retail conversion, the building(s) need to add value into the neighbourhood and suit the local needs. While 'build to rent' is on the rise, there is still a stigma on renting and we have to change this perception that renting is a secondary thought or only for millennials. In reality, as more people look for lifestyle and flexibility, it is becoming more about subscription living with a variety of services from which the residents can benefit. We track demographics closely to determine trends and quickly found our BTR communities have a wide variety of residents, from retirees and families to professionals. Whether our residents are leaving school, starting a family or retiring, by building these homes we are making a commitment to adapting as people's lives change, and we are shaping neighbourhood dynamics. That is where it is important to consider all facets of your building, from thinking about the amenity balance or weighing out options for the commercial space on the ground floor and filling with an occupant who offers an attractive service which enhances the "lifestyle factor", supplementing the overall neighbourhood offering. We also carefully consider design both in amenity and even home touches, i.e. better storage or creating office nooks for residents who are going into the office less. These trends rose in the US a while back with the multi-family market where it was important to adapt homes to the changing needs of residents, and it is the same now. For example, in one of our schemes we may have an accountant in the commercial space next door to a food shop and a bakery or a salon, offering an array of services in one area. It is really looking at your resident profile, along with the local neighbourhood, and engaging with them on what services would build value.

In conclusion, what do you see as the biggest threat, and the biggest opportunity, for the future of our towns?

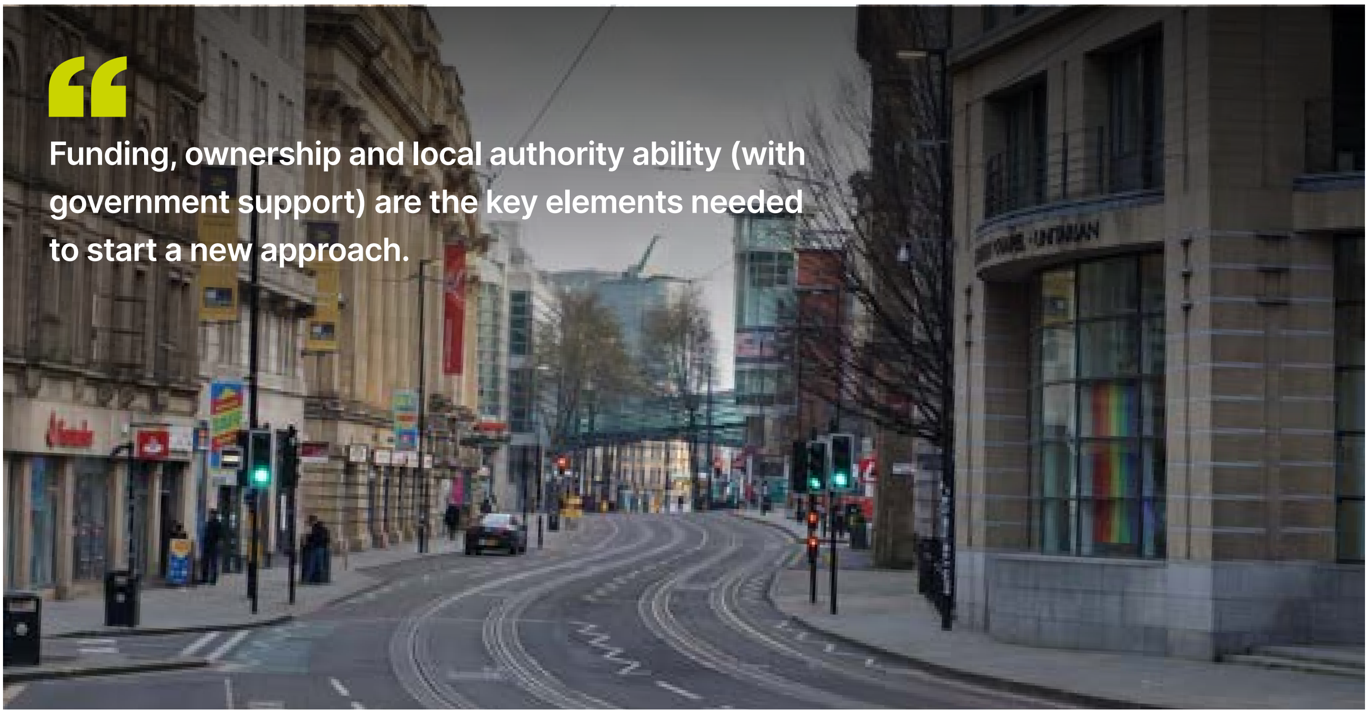
Stephen Martin – For me, it is about how all of this is harnessed, focused and delivered through what would inevitably be a long-term programme of many years. Funding, ownership and local authority ability (with government support) are the key elements needed to start a new approach. However, does the complexity of town centre interests mean that current participants are committed to making it happen, especially with the length of time needed to actually deliver results? Are LEP's working? For smaller towns, are the single/majority owners getting the support they need to deliver the towns of tomorrow? Is central government funding being put to effective use, and who actually controls and directs that local spend? This, to me, is the main body that has the power to shape all of this.

The last year has been monumental in terms of the speed and impact with which the government has brought changes to statute and, assuming this is a priority for government, could that momentum continue to deliver on the right priority solutions in a post-pandemic world?

In the property industry this year, we've seen some significant changes through lobbying government and hopefully that will at least be seen through to improving business rates liabilities too. Timing needs to be considered carefully for government to want (and be able) to listen at a time when there are many other national and international issues. There is no time like the present though, and we need to use those government ties in order to deliver the best local solutions.

Stuart Heslop - Key for me will be the issue of multiple ownership of high streets in towns and cities across the UK severely impeding the desire to move quickly. Getting owner groups together with master planners to determine what is viable in each of those individual towns in need of change is essential. That will require brave and open-minded owners, willing planners and engaged councils to work together to find the best solution and then, importantly, implementing it.

Funding will play its part with infrastructure funding from local and national government and residential-led development funding from mainstream banks. Leisure and retail occupiers will follow in order to create 24-hour economies with people living, working and spending their leisure time in well-designed and well-served towns.



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