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C&P

Retail Property Briefing 20

December 04

Left & Front Cover:
Kidderminster - Weavers Wharf, Development, Agency and Funding Advice

BCSC 2004 Gold Award Winner

Sevenoaks: Blighs Meadow
Asset management, buy-in and re-letting to Marks & Spencer on behalf of Sevenoaks (Blighs Meadow) Ltd.

Solihull: Touchwood
Acquisition on behalf of Fopp Ltd.

Index

Market overview

Graham Chase FRICS FCI Arb

Poole: Comet and Staples - Fleets Lane
Investment Acquisition on behalf of ISIS Property Asset Management Plc.

London: Leicester Square
Aquisition on behalf of Done Bros.

From our market perspective the two sectors that created the most interest over the past twelve months have been retail investment and planning.

As we predicted last year, investment in all forms of retail property has grown but even we did not foresee how strong the growth would be. Between the finishing of our last report in November 2003 and February 2004, institutions allocated well over £2 billion for retail property purchases. The move was driven by actuarial sentiment firmly attaching itself to real estate and bricks and mortar against little confidence in stock markets and an expensive bond market with meagre return. With a significant excess of demand against supply, particularly for the relatively rare commodity of retail warehousing, the net result has been a fall in equivalent yields for prime stock of between 50 and 100 basis points.

As to planning, we reported our concerns on an over-burdened and failing infrastructure, since which time matters have gone from bad to worse. The planning inspectorate now accepts that they cannot cope and consequently hearing and decision dates are continuing to move out. Local Planning Authorities do their best with a growing workload but this is against the background of greater consideration required on each application and a lack of qualified staff. With the new Planning and Compulsory Purchase Act now almost upon us, it's as if the system has ground to a halt. The new Act looks more like a complete rewrite rather than an upgrade, incorporating a new tier of regional planning which can only add to the consultation process and burden on the system. In the circumstances the next 12 months are unlikely to produce any improvement in terms of speed, certainty and quality of decision making.

In considering the market generally, the strong housing sector of last year has now evaporated with pundits predicting price falls between 10 and 20% against the peak. The underlying problem relates to debt and unsustainable lifestyles. Total household debt now exceeds £1,000 billion with over 20% classified as unsecured.

On the commercial loan front, Bank of England figures show lending continuing to rise with over £110 billion out and total potential commitments now exceeding £130 billion. The rate of increase has, however, slowed and against the increase in commercial property values over the past 12 months it could be argued the sector is under-capitalised in terms of its debt.

On the other hand the USA is, according to some observers, technically bankrupt, with their debt making the UK look frugal by comparison. Other world threats to the UK economy are obvious and include an unstable Middle East, high oil prices and rising energy costs coupled with deflation in a number of commodity markets.

To date UK Plc has demonstrated a surprising strength and ability to continue growth despite a challenging world economy. Recent rises in the London Stock Market maintain this status and this strength will need to continue over the next twelve months if a sudden correction is to be avoided.

Retail expenditure has been fairly steady over the past 12 months but anecdotal evidence from retailers suggests the party is over with a wet summer hitting many fashion traders and the months of October and November proving nothing short of disastrous. As ever, retailers are looking to Christmas to bail them out - no wonder the decorations and seasonal sales began even earlier this year in the first week of November.

All the above points to a strain on the retail occupational market and a question as to how well consumer expenditure will hold up. The good news is that despite the problems of Marks & Spencer, many high street retailers have tremendous confidence, with Next, Debenhams and Bhs showing strong growth. The retail warehouse market is likely to see some casualties in the near future (Courts is the first example) but there are growing concepts who will fill any voids that are created, coupled with a serious lack of supply of good quality space.

We anticipate total returns from retail property to continue at their current double-digit high levels for the next 18 months, fuelled principally by recent yield falls and previous rental growth, which will take this period of time to feed into the system. The decisions that will be made by retailers and investors in the late spring of 2005 will be the key datum point and likely to shape the next cycle of the retail property market.

Town planning

Delay

- The most significant theme in the planning arena over the past year has been one of delay.

PPS6

- PPS6 was issued for consultation in December 2003 and representations were invited by March 2004. The draft introduced several sensible new elements of policy and, to practitioners at least, implied that the extremes of PPG6 (as clarified on various occasions) were recognised by the government as being in need of review. Perhaps it was of some concern to the government that national planning policy was being added to without any consultation, which is of course contrary to the government's own advice regarding the weight to be given to policy.
- Nevertheless, as at October 2004, PPS6 is yet to be published and we are informed will not be published until the new year. Since the ODPM has been quick to criticise planning authorities for delay, there must be a sound case for the ODPM to get its own house in order.

Inquiries

- Other ODPM inspired delays occur regularly in the arena of Call-In Inquiries and subsequent decision making. Development and investment is clearly recognised as crucial to the country's economic welfare, yet major delays to decision making are being caused by the ODPM's dictat requiring Call-In Inquiries, not to mention the time taken to issue the post-Inquiry decision.
- Our own experience of this is more than frustrating. Having negotiated a Certificate of Lawfulness for a retail use of three former car showrooms in the West Midlands, and also negotiated with the planning authority to achieve the grant of planning permission for redevelopment of the site for less retail floorspace with conditions to allow bulky goods retailing only, the proposed development was called in for a public inquiry. The Inquiry took some eight months to arrange. Nearly five months after the Inquiry the decision was still not issued by the ODPM.
- For a government which, on the face of it, wants to encourage investment, these delays are more than disappointing. It also reveals an overzealous interference with the decision making role of planning authorities.
- In this regard, it is high time that the role of the Minister's Planning Policies Division is made more accountable and transparent. Who are they? What background in planning and development matters do they have? Are they really sufficiently experienced in development and planning matters to overrule the expert opinions of qualified and experienced inspectors?
- We believe that all retail development practitioners should be given more information on the Planning Policies Division, and a greater effort made by the ODPM to speed up his own decision making.
- In Best Value terms, the ODPM would be unlikely to secure more than one star (out of three).

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Planning advice to Land Securities Plc.

Vacuum

- Elsewhere in the planning world, new planning and compulsory purchase legislation was introduced to speed up the system. From our discussions with planning authorities, it seems that its introduction has caused delay in many planning measures coming forward, and in some cases even a planning policy vacuum.
- In last year's end of year round-up, we commented on the need for more resources to be allocated to council planning departments, so as to enable them to attract more staff and reduce delays. This observation is now being reinforced by similar calls from all over the property development industry but appears to be falling on deaf ears.
- Perhaps next year the development industry will be recognised as fundamental to the UK Plc's well-being and positively encouraged. For the moment, development and developers are increasingly viewed by the Government as a source of tax income, in one form or another, hence "affordable" housing policy and hence the review of the Section 106 Agreements.

Mezzanines

- Many out-of-town retailers have been using a mezzanine as part of their fitting-out to increase the storage or sales area of their unit. New planning legislation will stop that ability 'as of right'.
- The draft order has not been issued yet but effectively the law will change overnight. One day it will be lawful to erect a mezzanine the next day it will not - unless the order is complied with.
- Each landlord or tenant will have to make a planning application for any increase over the ground floor area. It may be that a percentage of the ground floor area will be allowed within the order.
- Interregnum period means that a property being marketed in 2004 which has the ability for a mezzanine now, may not in 2005 when the order is made and when the tenant wants possession. Some landlords and tenants are 'building' in advance of the legislation.
- This will affect retailers with existing stores who are upgrading their offer by the use of mezzanines e.g Homebase, Halfords, JJB Sports.
- Mezzanine trading will continue to be a part of the market but LPA's will have more control. It will be seen as a way of restricting more out-of-centre development, but the forward-thinking authorities may find that they can use it in a positive way. As retail demand increases they should accept that first floor trading can soak some of that up and avoid the need for more development.
- Landlords and retailers will need to work together to promote their arguments and accept that when making an application to 'extend' the LPA may impose conditions.

In-town retail

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Market Overview

- Market relatively stable over the past twelve months. Expansion by a number of retailers on a selective basis, very low vacancy rates but equally only a limited supply of new quality product.
- Whilst some retailers continue to prosper such as Next, Arcadia, Bhs and Tesco, others, all previous market leaders, such as Marks & Spencer, W H Smith and Sainsburys are really struggling to find their way through the cutthroat retail market.
- Prime pitch still sought after with strong competition.
- Successive increases in interest rate this year have started to show a reversal in the housing market particularly in the southeast. The impact on the retail sector is now being felt.
- Retailers continue to see costs rise through SDLT, DDA requirements and rating revaluation together with the threat of 'BIDS'.
- The grey pound – becoming more important to the retail industry that has always coveted the 15-35 year old fashion market. Over 55's are a growing and increasingly important market.
- Last year we commented on the level of private equity deals and whilst this has slowed slightly, this method of financing and buy out is likely to remain popular for at least the next few years.
- Pressure from supermarkets to come back into town centres due to the planning regime. In London the requirement for additional residential units has produced 'living above the shop' once again. This market will continue to grow, even given resistance from local residents.

Major Stories / Trends

- Philip Green fails in his attempts to take over Marks & Spencer however, his friend Stuart Rose has taken up the challenge. Will the New Year see a renewed bid? October trading figures suggest a difficult future. Get ready for sale and leasebacks as a way of boosting returns and investment.
- Despite concerns about retail expenditure following the blip in July/August, receiverships over the last twelve months appear to have been thin on the ground. BDO Stoy Hayward report the lowest number of retail failures since 1993. Our Price and Cromwells, however, did bite the dust.
- For once the public had more sympathy than usual when retailers complained following a particularly wet easter and summer that caused a blip in sales. Boots half-year profits fell by 48% with the poor weather partially to blame.
- Perhaps the most notable seller of property on the high street has been Dixons who placed some 120 units on the market. JD Sports, Adams and Virgin have also undertaken substantial disposal programmes as they rationalise their portfolios.
- One of the more competitive markets for expansion is that of bookmakers and betting shops. All the major operators - Coral, Done Brothers, Ladbrokes, William Hill and Paddy Power are going "head to head" competing for space since the introduction of "fixed odds" betting terminals. All operators have seen large rises in profits.

Other Issues

- Stamp Duty Land Tax has now been in operation for just over one year. Whilst this does not appear to have had a major impact on the market the trend to shorter leases continues, perhaps pushed a little harder by this legislation. A few retailers have noted that this has increased their start up costs – again coming straight off the bottom line. Another clever stealth tax introduced in a strong market but the burden may prove unacceptable in a weakening economy.
- The Disability Discrimination Act came into effect on 1 October 2004, however, the property industry still does not seem to have a clear idea of the exact implications. Developers and occupiers have seen costs increase in order to provide buildings that comply with the legislation.
- The rating revaluation will take effect from April 2005. It is estimated that rateable values will increase by over 25% and hence retailers will be hit with another increase in their occupational property costs that they cannot control.
- Given the rise in costs associated with the above factors there is concern that the retail market, whilst stable, is finely balanced and could deteriorate if there are further interest rate rises.

- Retailers in Central London claim congestion charge resulted in reduced turnover.
- The Planning & Compulsory Purchase Act 2004 should help to speed up the development process due to less onerous reasons for securing an order, although we have doubts that the additional compensation payments will result in faster settlements with parties being acquired.
- 'BIDs' being trialled in some areas eg. Piccadilly and Kingston add to occupational costs.

Development Pipeline

- There is still a lack of available quality stock on the high street and as we reported last year, vacancy rates continue to be generally very low. Only a few new shopping centres opened during 2004 including Pescod Square, Boston; Water Gardens, Harlow; Whitefriars, Canterbury (phase 2). Retailers have therefore had few opportunities to expand into new markets.
- 2005 will again see limited new scheme openings so the immediate pressure on retailers will continue next year forcing them to consider extensions, refurbishments and alterations to existing stock and also expanding out-of-town.
- This pressure should be alleviated from 2006 onwards when a number of major schemes are scheduled to open in Belfast, Bradford, Bristol, Chester, Derby, Exeter, Leicester, Liverpool, Nottingham, Enfield, Sheffield, Norwich, Portsmouth, Plymouth etc. This perhaps reflects the impact of the Government's planning regime in recent years focusing on regenerating town centres.
- It is hoped that when this new space hits the market, the retailers will absorb it readily. We can't afford another 1992 with too much space at the wrong time in the economic cycle.

Department/ Variety Stores

- John Lewis is expanding with new stores opening in Cambridge, Cardiff, Leicester, Liverpool, Portsmouth, Sheffield and Northern Ireland.
- Following last year's leveraged buy out Debenhams continues to expand across the UK and has just introduced a trial for a small store of between 12,000 and 20,000 sq ft and will consider towns with 60,000 population. This year Debenhams reported an increase of 119% on pre-tax profits.
- Bhs is also considering small store formats and this trend may open up opportunities for development in smaller towns as it seeks to increase its sales densities.
- Allders continues to struggle and it will be interesting to see where its future lies if sold by Minerva.
- House of Fraser appears to have had mixed trading although they are trying to upgrade their store portfolio with 20% new space being added with new stores at Croydon and Maidstone.
- TJ Hughes, following the MBO from JJB, is back on the expansion trail looking to take its 38-store portfolio up to 50.
- Next continues to consider larger store formats and opened a 150,000 sq ft store in Manchester.
- As retailers expand their trading formats in the form of larger stores they are seeking to benefit from paying effectively lower rental rates per square foot. With increased competition, however, rental levels are rising in this sector for the better towns and locations.

Company Purchases

- Private Equity continues to be attracted to the retail sector - Ethel Austin has been sold to Amro Capital. USC the fashionable menswear chain acquired by West CoastCapital. Austin Reed has been bought by Dawnay Day. Robert Dyas was also sold to Change Capital back in March. Hobbs has gone to 3i. Bridgepoint Capital bought Faith Shoes.
- Borders bought Paperchase, a chain of 61 shops
- Unwins off licence goes to French wine company, Castel.
- Early Learning Centre bought the upmarket Daisy & Tom chain.
- Moss Bros continues to be stalked as a potential takeover target.
- Sports World takes Cromwells out of Administration.
- Permira withdrew their bid for WH Smith in July mainly on the back of potential pension provision although results have since declined further with a reported loss of £135 million.
- Clinton Cards buy Birthdays.
- Baugur close in on Big Food Group.

London: Oxford Street
Assignment to Subway on behalf of Budgens Stores Ltd.

Horsham: Carfax
Acquisition for Cook (Trading) Ltd.

Expanding Retailers

- Despite the caution there appear to be more retailers wishing to expand than for many years, perhaps representing a particular point in the cycle.
- MacKays are seeking another 50 shops on top of the existing chain of 260.
- George seeks further stores following the success of their early openings.
- TK-Maxx opened their first home store in Edinburgh of 10,000 sq ft with more to follow.
- Monsoon seeks to open childrenswear shops and is piloting a menswear offer in 12 shops.
- Gamestation, owned by Blockbuster, expanding aggressively and take 6,000 sq ft in Birmingham.
- Halfords introduce a new smaller store format for suburban and town centre locations of between 4,000 and 6,000 sq ft.
- Matalan continues to seek stores in-town but few agreed to date.
- Music Zone, Fopp and HMV continue to expand across the country as does their DVD competitor, Silverscreen.
- Other acquisitive retailers include Peacocks, Primark, Savers, Sportsworld, Ted Baker, Warren James Jewellers, Caffé Nero, Costa Coffee, Deichmann Shoes (in-town format), Dixons Xcel, Dominos Pizza, Dreams Beds, Eat, Faith Shoes, Farm Foods, Fat Face, Fragrance Shop, Games Workshop, Greggs Bakers, Johnsons Dry Cleaners, Maplin Electronics, Lush Cosmetics, O2, H&M Hennes, Cotswold Outdoor and Krispy Kreme.

Retailers Disposing

- As expanding retailers search hard to satisfy requirements, there are also those who are taking the opportunity of divesting themselves of surplus or non performing outlets.
- Dixons rationalise and place over 120 stores on the market.
- Adams selling out of high rented stores to pursue concession opportunities.
- Country Casuals are seeking to drop their name.
- Deichmann Shoes have been selling out of some of their early stores.
- Gymboree are pulling out of UK.
- JD Sports has continued its rationalisation following the purchase of First Sport last year.
- Marks & Spencer closed its homestore in Newcastle.
- McDonalds continue to sell restaurants.
- Officers Club has been selling and buying larger stores as part of its re-focusing.
- Virgin similarly rationalise and acquire larger format stores.
- Clinton Cards have also been churning stock to get rid of older, weaker stores.

Other High Street Stories

- Laura Ashley admits that their fashion offer is not working and will commit greater resources to home furnishings.
- Waterstones acquire the former Tesco Metro on Oxford Street.
- Gap is still talking about bringing in other brands such as Old Navy and Banana Republic.
- Uniqlo re-launches in the UK market seeking selective locations in southeast England.
- Woolworths – whilst reducing the Big W out of town offer, is seeking 60 new locations in-town.
- Zara introduce boutique stores of down to 5,000 sq ft to provide greater opportunities for expansion in major markets.

Edge-of-town Development

- The award winning Weavers Wharf, Kidderminster opened fully in 2004 comprising a food store, leisure and retail warehousing plus retail shops linking with the High Street. This is a great example of urban regeneration working successfully.
- It extended the town centre and reduced leakage.
- Marks & Spencer, Next and New Look relocated to larger units within the town centre environment.
- Difficulties of land assembly, planning, CPO, contamination and a long lead-in period means viability is difficult to achieve. Partnership and strong support of the local authority is needed.

Sevenoaks: Blighs Meadow
Letting to Monsoon on behalf of Sevenoaks (Blighs Meadow) Ltd.

In-town/shopping centre investment

Yields Bottoming Out?

- Yields remain historically low as a result of continuing strong demand for the sector and (despite recent rises) historically low borrowing rates. Signs of both high street and shopping centre yields 'bottoming out'.
- Substantial amount of shopping centre stock on the market. Mostly secondary, with some notable exceptions. Partly the normal 'pre-Christmas' rush, but could also be vendors calling the peak of the market?
- Realisation that future capital growth may be reliant on more than just favourable yield shifts. An end to 'quick-fire' trading and a return to market fundamentals?

Yield Convergence

- Continued compression of secondary yields producing an exceptionally narrow gap between prime and secondary (1.0% - 1.5%). Prime cheap or secondary over-priced?

Borrowing Environment

- General consensus that interest rates may peak sooner (and lower) than originally expected, due to signs of slowing down in the economy and housing market. Swap rates reacting favourably. Borrowing conditions remain good although many banks have tightened up on borrowing criteria.

Funds vs Property Companies

- Institutional investors over the previous twelve months have been in the ascendancy due to their cash position and substantial funds to spend in the sector. Leveraged property companies have had difficulty competing in low yield environment. Institutions remain on the whole net investors in the high street and shopping centre sectors; many with pressing requirements for stock. Notable examples: ING, Scottish Widows, Standard Life, Insight, F&C.

Sector Comparisons

- Along with retail warehousing, the high street and shopping centre sectors remain the most competitive in terms of yield. Many ' would be' investors sidelined and redirected into the office and industrial sectors in search of higher returns.

Stock Supply

- A fundamental lack of new development opportunities turning developers into asset managers.

Lease Length

- Legislation continuing to loom over lease length. Much debate over possible consequences (most expected to be negative) and the justification for legislation in a free market. Except in exceptional circumstances (25 years +) a heated investment market masking much of the differentiation in value resulting from varying lease length. Long leases (25 years +) highly valued and benefiting from an element of 'scarcity'

REITS/PIFS

- Much excitement in Q1 2004 over potential legislation on REITS. Disappointment with timescale and uncertainty over suggested restrictions on reinvestment and redevelopment results but debate rumbles on.

Influence of Private Buyers

- Private buyers, or syndicates of private equity, responsible for much market activity. Irish, Danish and Middle Eastern buyers especially notable. Almost no upper limit on (typical) lot size. For smaller lots, private buyers remain especially visible in the auction markets.

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Sale of Portfolio of 14 shops for Aberdeen & Highland Estates.

Lancaster: St Nicholas Arcades Shopping Centre acquired for Ediston Properties

Shop and Shopping Centre Yields

- Prime high street shops: 4.5% - 5.25%
- Secondary shops: 6.0% - 7.0%
- Prime shopping centres: 5.0% - 6.0%
- Second tier shopping centres: 6.0% - 7.0%
- Auction market (small lot sizes) 5.0%

The Year Ahead

- Base rate appears to be peaking at 4.75%. Demand for retail investments remaining strong, provided institutions remain net (and heavy) investors in the sector. Yield stability but 'bottom' of cycle reached. Some stock 'sticking' given overpricing (and keenness to sell into the top of the market). Increased emphasis on 'asset management' since rapidly falling yields will no longer be the primary contributor to annual returns. If yields do rise it will not be a large hike given low base rate. Secondary yields might be under pressure if the market cools and the yield gap between prime and secondary is forced wider than the current narrow dividing line.

Retail warehouse sector

Market Issues

Development

Limited New Schemes

- Market has not entirely dried up with new "shopping parks" taking the design and marketplace forward in 2004 at Bournemouth Castlepoint and Beckton: Gallions Reach.
- Developers have not given up where they believe there is strong demand and a good planning argument.

Extension/Rebuilding/Refurbishment/Asset Management

- Parks are being considered for extension where possible. The planning arguments may be a little easier than on new schemes.
- Taunton Priory Fields Retail Park has been knocked down and rebuilt. All tenants were prepared to close down and reopen in the new scheme comprising exactly the same total square footage.
- Regeneration of "old" schemes through investment in them by landlords. Retailers do not like 'tired' retail environments. Good design aids competitiveness.
- Failure of Courts will provide some opportunities.

Development Manager

- Our landlord clients have been outsourcing the "development" and project management role to market specialists e.g. Redbourn at Taunton and Poole and Chinacorp at Scarborough.
- Their expertise and market knowledge enables the owner to benefit from the ability to bring forward change in a specialist area while leaving themselves free of the time consuming process of project control. The client makes quick informed decisions and knows the "developer" will progress it.

Company Changes

Consolidation, sales and cash injections

- Trend in corporate break ups a feature e.g. Homestyle in 2004 following Kingfisher in 2003.
- Exception is GUS with its purchase of Homebase, with profit enhancement potential.
- Halfords bought out from Boots, restructured, new products introduced and successfully floated within two years.
- In contrast Focus Wickes has been changing internally for years but announced in December a corporate sale of the Wickes business to Travis Perkins and further review of the Focus business.
- Companies that have been bought out, bought in or simply sold as a whole or in part this year include Pets at Home, Rosebys, American Golf, Land of Leather, Furnitureland, DFS and Maplin Electronics.
- Such retailers may be floated in the future after changes are made.
- Lack of new entrants (other than those expanding from the high street) but the fascias often hide management changes and new requirements reflecting a dynamic and evolving market.

Professional

Mezzanines

- Valuers will be on the look-out for market evidence that suggests there is a rental differential between units that have a mezzanine and ones (perhaps on the same park) that do not following the new legislation. Each case will have to be judged on merit.

Lease Renewals

- Due to the inception of the retail warehouse market in the late 1970's/early 1980's and the prevalence of 25 year terms, lease renewals only now coming into play.
- Landlord and tenant often "re-gearing" in advance rather than waiting for lease renewal in 5 to 10 years time. New occupational terms agreed to reflect current market. It often allows a capital injection from the landlord to pay a premium to secure the tenant on a longer lease and make physical improvements.
- Possible impact of SDLT may deter this.

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Rent Reviews General

- Concept of pitch. Landlords and tenants looking for evidence of different areas of a retail park trading better than others and commanding a higher rent. Pitch can change with a new retailer opening e.g. Next.
- Where lettings not available to confirm rental levels other techniques may have to be adopted.
- Turnover can be turned into evidence and argued at review but only as a comparison in the growth of different centres.
- Affordability arguments carry little weight in terms of identifying rental levels.
- Argument continues about single letting providing the best evidence on a scheme e.g. Sports World outbidding competitors at tender.
- May only be one tenant e.g. B&Q. Hypothetical tenant will pay no more than is needed but the willing lessor does not have to let to the one tenant if not profitable.

Treatment of Incentives

- Question as to length of term for amortisation of incentives and methodology e.g straight line or DCF. Retail warehouse market is probably former.
- Incentives must be analysed on a case by case basis. If a premium is one that would have been paid by the market as a whole, and can attach itself to the hypothetical tenant as a payment in lieu of rent, then it should be amortised.

Arbitration

- Not enough qualified Arbitrators to overcome problems of conflicts/involvement in a small market.
- Some Arbitrators taking too long to issue awards.
- Some protagonists using and abusing the Arbitration process by exertion of pressure, delaying tactics, and failure to comply with RICS Guidance Notes.
- Some Expert Witnesses still failing to produce "honest" opinions of value. RICS Practice Statement has no teeth.

The Occupiers

- The market remains strong in most of the sectors although there continues to be discussion about which retailers are successfully competing in the key areas of electrical and furniture. There is good news from some retailers who have struggled in the past e.g Mothercare, and more high street retailers are looking at the shopping parks.

DIY Sector

- B&Q
  - 35 years old.
  - Mini Warehouse format expanding by refitting existing stores of over 35,000 sq ft, new development up to 60,000 sq ft and extensions of existing stores e.g. Eastleigh.
  - Continued arguments at planning inquiries about the larger Warehouse format but the mini Warehouse is drawing a similar customer without the full range.
- Focus/Wickes
  - Wickes Extra open their fifth store in Maidstone.
  - Wickes open three stores in the last financial year with new owner Travis Perkins wanting to continue expansion.
  - Focus expansion in smaller towns.
- **Homebase**
  - GUS making changes to grow the business.
  - Continued mezzanine expansion.
  - Concentrating on smaller town footprint to compete with Focus but still looking for larger stores up to 60,000 sq ft.
- **Glyn Webb**
  - Actively refurbishing existing portfolio and ready to expand.

Taunton: Priory Fields
Agency, Planning and Investment advice to AXA REIM and Redbourn.

Sheffield: Crystal Peaks
Lettings on behalf of Hermes Property Asset Management

Electrical Sector

- The race for space slowed markedly at the beginning of the year as retailers took stock in a competitive trading environment and property requirements continue to change.

- Currys /PC World
  - Footprint changes while assessing new opportunities carefully.
  - Seeking to change standard lease terms with shorter lease length and fixed rental uplifts.
  - PC World expansion-minded and relocating off high rented parks.

- Comet
  - Kesa pleased with progress.
  - Quick turnaround of property deals when right opportunity.

- Powerhouse
  - Continued company changes.
  - Forecast profit in 2007.

- Miller Brothers
  - Rationalising space.

- Maplin Electronics
  - Maplin sold in August to Montague Private Equity.
  - First new style superstore opened in Blackpool

Furniture /Home Furnishings and Carpets

- A mixed year highlighted by the failure of the UK arm of the Courts business in December.

- IKEA
  - 13th store opening in Edmonton, London in February 2005.
  - Croydon is open until midnight.
  - Stockport planning refusal to be appealed.
  - Latest application made in Doncaster.

- ILVA
  - Dominant furniture offer provides competition from Danish retailer with first opening in Manchester in 2005 of 120,000 sq ft on two floors.

- Marks & Spencer Lifestore
  - Opened in February at Gateshead, trading queried in May, out-of-town concept abandoned by Stuart Rose in July and planned closure early in 2005.

- DFS Chairman Lord Kirkham announced he has bought back his "old" company in November after six months tough negotiations with shareholders.

- Furnitureland's business was bought by SB Capital in February.

- Courts administrators could not sell the business. SB Capital selling the stock and are to reopen 14 stores as Furnitureland.

- Land of Leather sold 50% of the business to SB Capital in July.

- Habitat expanding slowly and opened in Leeds in November.

- MFI's distribution problems intensified financial concerns.
  - Rumour of takeover.

- ScS's profits improve and new expansion programme is announced.

- Kingdom of Leather rebranding as Natuzzi.

- Rosebys /Homestyle
  - Rosebys Group grew by company acquisition and changed its name to Homestyle but seems destined to end up as individual fascias again.
  - Management buyout by Rosebys completed in April.
  - Homestyle fend for themselves and seek to turnaround Harveys
  - Homestyle quickly put bed businesses on the market.

Bracknell: Investment sale on behalf of Brookhouse Group

Grimsby: Victoria Retail Park
Rent reviews and asset management for Belgrave Land. New letting agreed to Sports World

Northampton: St Peters Way Retail Park
Rent reviews and Asset management for ING Real Estate Investment Management. Surrender of Aldi lease and new letting to Home Bargains who opened 1st November 2004.

- Carpetright continue to be the market leader. Allied Carpets are looking at smaller towns and smaller units to expand into new markets. Storey Carpets are expanding out of region.
- Dunelm gearing for flotation?
- Dreams and Paul Simon's continued fast expansion.
- Furniture Village reported better trading with other furniture retailers having problems.

Sports /Fashion

- The last 12 months has seen increased pressure for high street retailers to expand their existing operation out-of-town and for new ones to join it. Next have been the market leaders opening 31 stores in 2004 and expect a similar number to open in 2005.
- JJB have mixed trading reviews but continue the health club format with shop above.
- Sports Soccer changed its name to Sports World and confirmed strong expansion.
- Blacks open first out-of-town store in Northampton.
- Decathlon to open its sixth store in Thurrock.
- Matalan's growth stalled but it remains a successful business and is considering smaller stores.
- TK Maxx opened first TK Maxx Home (no clothing) as trial operation.
- Arcadia highlight out-of-town as the way forward.
- George trialling first retail warehouses in The Fort Manchester with more potentially to follow.
- Brantano's good profits back expansion.
- Marks & Spencer's new boss likes the look of the store at Speke – will this lead to more retail warehouses?

Commentary on other Retailers

- Boots the Chemists opened its 100th store in October in Crayford.
- Asda opened its first non-food only store branded Asda Living on Walsall Crown Retail Park in October.
- Halfords successfully floated in June with continuing broadening of the product range. September trading announcement shows the improvement.
- Pets at Home were sold in July and confirmed requirement in smaller stores of about 4,000 sq ft.
- Argos continue to report excellent trading.
- Staples dominate the office supplies market after their bid for Office World in April was cleared for completion in August leading to limited disposals.
- Big W downsizing programme continues.
- Mothercare are back on the expansion trail.
- Littlewoods announce out-of-town stores for the Index fascia.
- Hobbycraft sign up for two new stores.
- The Range has taken on larger units rejected by other retailers and show that a department store approach can work in the right location.
- Borders latest opening at Leeds, Birstall.

New Retailers, New Formats and Concepts

- Emergence of 'trade park' operators into secondary retail warehousing.
- Established retailers introducing new formats such as TK Maxx Home, George and Asda Living.
- 'New' retailers such as Hennes, Waterstones, Beaverbrooks, Virgin and H. Samuel will only consider 'fashion parks' like Glasgow Fort.

Poole: The Commerce Centre
Rent reviews and Asset management on behalf of Land Securities.

Clacton: Brook Retail Park
Letting and funding of new 67,000 sq ft retail Park

Market Overview

- Most retail parks are undergoing reassessment. Changing retail parks or "asset management" continues to be main source of opportunities.
- In some towns retail parks show a tiered market: prime, secondary and even tertiary e.g. Cardiff. Asset management seeks to rebalance the market.
- Retailers continue to assess their best size, mainly by downsizing e.g. MFI, Matalan, Staples.
- Effect of new planning restrictions on mezzanines not yet known.
- Furniture, carpet and electrical retailers targeted by landlords to relocate off open A1 retail parks as they secure interest from the likes of TK Maxx and Sports World e.g. Canterbury, Stour Retail Park.
- Evidence of more flexible lease negotiations with lease lengths falling and average lease lengths at 17/18 years (Source: King Sturge) Tenant requirements for longer leases mirrors position of landlords unlike certain high street circumstances. Currys successfully agreeing 15 year leases with both rent reviews "geared" only to percentage annual uplifts as an example of flexibility.

Government Policy – Arguments For A Strong Retail Warehousing Sector

- The basic principles for the effective display and sale of bulky goods remain sound as a retailing format.
- Arguments against are covered by a perceived threat to the town centre and land usage, which is valid where uncontrolled open A1 uses provide significant competition.
- By contrast bulky goods out of town centre are complementary to the town centre and reduce leakage to other retail centres.
- Far-seeing Local Authorities have used planning controls to enable bulky goods to be sold in retail warehouses while restrictive user policies have maintained and improved the high street offer.
- The growth of this 'new' market over the last 20 years is often ignored due to a focus on the detail of each park or retailer. Retail warehousing has added to consumer choice in a town.
- It has done this largely by providing units which help retailers reduce costs that are passed on to the public and provide increasingly good facilities in the best locations. The market has moved on and will continue to do so. Government and others must recognise the true merits of this type of retailing.
- Local Authorities are improving their understanding, but the Property Industry needs to work harder to promote how retail warehousing works and its wider impact on communities and commercial activity in a centre.

Disaggregation

- Over the last seven years or so there has been a growing argument that some retail formats could be 'disaggregated' e.g B&Q should have 10 small stores in a city rather than in their tried and tested format delivering goods at a significantly lower price under one roof.
- Hours of time have been spent arguing over it but it appears that the Draft PPS6 will accept the retailers' argument.

Retail warehouse investment

Overview

- Retail warehousing continues to be one of the strongest sub-sectors within the UK property market with unsatisfied demand from funds, property companies and private investors. Considerable funds allocated for purchases by Pension Funds in October 2003 still not allocated.

- Yields have continued to fall fuelled by greater institutional demand, lack of buying opportunities (continuing restrictive planning regime for new out of town retail development), the continued relative low cost of debt finance and weaker performance in other asset classes.

- Record low yields paid for a Shopping Park (Legal & General in London Colney – 4.40% approx) and new Bulky Goods park (High Wycombe –BP Pension Fund at 5.00%). Rumoured to be around fifteen bids reflecting weight of money and demand for good quality stock.

- Strong demand continues from the smaller in-house funds and private investors for good quality, well-let properties where the attraction is relatively long leases secured on good covenants. Security of income is arguably the main driver and location is becoming a secondary issue for some investors.

- Opportunities for property companies are still limited helping to suppress yields even further. For example LxB's purchase of Skimped Hill Retail Park in Bracknell, rumoured to be at 4.00% equivalent yield although purchaser had potential deals lined up at rents well above vendor's ERVs.

- Demand for more secondary retail warehouse investments has increased due to lack of buying opportunities generally. In yield terms the gap between prime and secondary has continued to close.

- Evidence of some investors (mainly property companies) 'turning' properties to take advantage of the continuing downward yield shift e.g. Resolution at Harlow – The Water Gardens and Grosvenor Hill at Llantrissant.

- Also lower yields are encouraging longer term holders to sell although for some funds especially problem is where to reinvest the money.

- Swap rates still remain relatively low resulting in funds and property companies having to remain competitive on the small to medium lot sizes where the debt buyers are still able to pay keen yields.

- Indirect investment continues to allow smaller players to gain exposure to the larger prime open A1 shopping parks e.g. Hercules Unit Trust (Pillar) and bulky goods parks e.g. The Junction Limited Partnership (Capital & Regional and Morley) and the Henderson Unit Trust. Investors include Local Authorities and smaller Corporate Pension Funds.

Outlook

- Yields could now stabilise on prime retail parks and London Colney and High Wycombe may well represent a peak in the market. These particular investments did provide almost unique opportunities to purchase new, prime schemes (open A1 and bulky goods respectively), in the South East, both with strong growth prospects.

- In the final quarter of 2004 there has been a relative 'flood' of retail warehouse parks on to the market including five at around or in excess of £50 million lot size. Does this represent the peak of a market cycle?

- Yields on secondary schemes with restricted planning permissions may soften if occupational demand becomes weaker and more property comes on to the market as investors seek to try and cash in on the strong market. This could be the sectors achilles heel. If the heat does come off the market it will be the secondary schemes with weaker tenant demand and less growth potential which will see the highest yield rise adjustment.

Mark Powell BA(Hons) MRICS   Abigail Nash   Tim Bevan-Thomas FRICS Dip IPF

Chorley: B&Q - North Street
Investment Acquisition on behalf of Prudential Property Investment Managers Ltd.

Yields (Equivalent)	2004	2003
• Prime open A1 shopping parks	4.75 – 5.00%	5.25 - 5.50%
• Open A1 non-food retail parks	5.00 – 5.50%	5.75 - 6.00%
• Prime bulky goods parks	5.25 – 6.00%	6.00 - 6.50%
• Prime standalone units	5.50 – 6.00%	6.00 - 6.50%
• Secondary parks and standalone units	6.50 – 7.25%	6.75 - 7.50%
• First generation schemes	7.25 – 8.00%	7.50 - 9.00%
• Food supermarkets	5.00 – 5.75%	5.00 - 6.25%

Dunstable: White Lion Retail Park.
Investment Acquisition on behalf of Universities Superannuation Scheme.

Supermarket and food superstores

Jo Dear   Graham Chase FRICS FCI Arb

The current restrictive planning regime has significantly reduced new development but activity is far from muted in this sector.

Morissons

- Morissons' acquisition of Safeway is having some impact. Although suffering a shaky start with not particularly encouraging trading figures, we expect this trend to be reversed as the refurbishment programme and the promotion of the strong Morrisons brand begins to accelerate.
- New store acquisitions are limited, but in a market where there are few planning permissions being granted for new stores the emphasis on refurbishment, upgrading and extensions, suggests that Morrisons' timing is about right.
- One side effect of Morrisons' purchase of Safeway is that a small number of redundant stores are beginning to find their way on to the market, but with the benefit of open A1 consents, alternative users are coming forward.

Tesco

- Tesco, with a turnover of £2 billion, produced record profits up by 27% in September and do not appear to be putting a foot wrong. Extensions of existing stores to create their large Extra format are improving the opportunities for the sale of non-food goods, maximising profit returns and sales densities. The smaller Metros are tapping markets close to their customers in built-up areas, which were abandoned a number of years ago by the foodstore operators. These new developments also provide excellent mixed use opportunities with residential "above the shop". By contrast expensive city centre locations have struggled to provide sufficient returns with some recent closures.

Asda

- Asda, in the number two spot, is moving forward with its concept where no food is sold, encouraged by its Wal Mart parent. The new Asda Living format opened its first store in October in Walsall, a direct result of the lack of opportunities for new food sites. The expansion of the stand-alone George brand is also likely to include retail warehouse units, with the first retail park store opening at the Fort Shopping Park in Manchester in October and comprising 15,500 sq ft.

Somerfield

- Somerfield have recovered winning back customers through their focus on high quality food and service, again exploiting local markets. This has led to their ground breaking deal to acquire 114 smaller type convenience stores from Morrisons for a total price of £260 million through two vehicles including a Joint Venture with Barclays Bank and Robert Tchenguiz.

Booths

- Another smaller group, Preston group Booths, aims to double turnover to £400 million from its current base of 26 stores.

Iceland

- Iceland are finding it hard to make ends meet as their customer base leaks to their stronger competitors. By contrast, discounters such as Netto, Lidl and Aldi continue to expand with Netto planning to expand their property portfolio by between 10 and 25 stores per year over the next few years. The sale of the business and a break-up of it's property assets looks imminent as we go to press.

Sainsburys

- Problems at Sainsburys continue. It reported pre-tax loss of £39m for six months to October 2004 and now only has the third best market share. The stock market, and indeed customers, will be watching carefully how the company performs over the next 12 months and rises to the challenge of stronger competition with new trading formats and expansion on existing sites. In this regard the 'central' format has not worked with a number now available on the market.

Waitrose

- Waitrose, following on from some group acquisitions from Safeway last year, continues to expand and is now moving into in the North of England for the first time. Waitrose has improved its food and home offer with the introduction of coffee shops, crèche and toys, thereby maintaining the emphasis on quality and service.

Marks & Spencer

- Even Marks & Spencer's food division is finding it difficult to move forward which is giving cause for concern, given that it was this area of Marks & Spencer trading which was providing the only good news when like-for-like sales of clothing and homeware continued to slide.

Property Market & Professional Side

A number of issues have either been clarified or are beginning to emerge as follows:

- Premium payments are becoming rarer as rents begin to rise. Where premiums are paid, provided it can be demonstrated that they are attached to the property and the hypothetical tenant would have paid the premium and does not represent a payment which would only be paid by a particular tenant, it is capable of being amortised. Equally there are a number of reasons why it may not be appropriate to do so and hence each case must be judged on its merits and care taken to understand precisely why the premium has been paid.
- Operators have become more flexible taking mezzanines, first floors and decked parking. This has been the case for the last 5/7 years. Rental rates being applied to these stores appear to be maintained even where the original criteria of ground level trading and surface car park providing a ratio of spaces of 1:100 of GIA are sacrificed. However, this is only for stores which improve their trade, even though the traditional criteria are weakened. In this respect the food sector has adapted to the new planning regime more quickly and effectively than most other sectors.
- Rental levels for the best food superstores outside of London are now set to breach the £20 per sq ft mark and in London there is evidence to suggest that rental levels now lie somewhere between £25 - £30 per sq ft for the best quality stores.
- The lack of open market lettings continues to hold back this sector in terms of assessing true market rents and whether they should be higher or lower than those figures currently being achieved at review. The position is unlikely to improve given that Morrisons prefer to hold their own freeholds, despite their new levels of debt, and Tesco have also indicated that freehold purchases are their preferred option. Nothing new here.
- The restrictive planning regime has reduced dramatically the number of new developments. Where they do arise, competition is so great that it is usually difficult for a developer to become involved in creating an open market letting on a lease, as the operators, as in the past, bid directly. The role for the developer is often reduced to simply that of a project manager.
- Benefits have also resulted from planning policy, as in some centres saturation of foodstores has been reached as demonstrated by the sell-offs by Morrisons. The stricter planning regime has underpinned property values in the sector and given greater security for the future for existing players. Competition will now have to focus on formats and business acumen rather than beating the opposition through the adding of new space in new state of the art stores.
- As the foodstore operators continue to grow their freehold portfolios, so the potential for sale and leasebacks will increase as these operators open up new areas for trade within existing units or in new formats. The strong cashflows available in the food sector do however allow investment without unnecessary capital raising activities. On the other hand, given the bond qualities of tenants in this sector and the long leases usually required by the operators, yields of 5% and even lower are achievable producing high value assets which are readily saleable in today's hungry property investment market.

Leisure

Casinos

- The overhaul and liberalising of the UK's gaming laws has been the hot topic of the year. Proposed deregulation has seen considerable interest from both UK and US casino operators. The Government has 'watered down' its initial proposals following the large public outcry. In property terms it is likely to have an impact only where destination/resort casinos are developed in a few major centres. A number of developers have already identified opportunities in locations such as The Dome and Wembley in London, and other major UK cities including Manchester, Birmingham and Glasgow. Resort towns such as Blackpool see major casinos as a method of regenerating their outdated tourist industry. Others hope that casinos will be the catalyst to fund new sports stadiums.
- Resort Casinos are likely to give local economies a major boost and local authorities will welcome additional revenues from Section 106 agreements – Communities are however fearful of potential social costs which may arise.

Investment

- Leisure property continues to attract investors, offering good value and relatively long leases. Yields have hardened with a number of schemes being sold recently including Millennium Plaza Cardiff, purchased by Prudential at circa 7%; Brighton Marina going to X-leisure for £65 million, a reported net initial yield of 6.2%; and Turnstone Estates selling Cambridge Leisure Park quoting a price of £33.8 million reflecting an initial yield of 6.62%. Covenant strength and length of lease is still an important factor in establishing the level of yield.

Leisure Parks

- A number of leisure parks have recently been subject to their first round of rent reviews and many of the cinemas, health and fitness clubs, ten-pin bowls and night clubs have seen landlords rely on guaranteed rental uplifts as open market rents have remained fairly static in recent years. Asset management of leisure parks has therefore become crucial for investors to add value.

Cinemas

- As we predicted last year, the UK cinema market has continued to see further consolidation. Private equity firm Terra Firma purchased both the Odeon and UCI cinema chains. Vue and Cine UK are already owned by private equity firms. There were few new openings this year, with the most aggressive player in recent years, Cine UK, opening in Cambridge and Sunderland. Vue purchased the former Cinemark International theatres in Northampton and Scunthorpe. Next year will again see only a limited number of openings.

Health & Fitness

- The health and fitness sector continued to see consolidation with few new openings in the UK by the major operators. Privately owned Bannatynes has continued its cautious expansion and is on target to have 40 clubs by 2006, whilst retailer JJB has now expanded to 20 health clubs in the UK. Esporta is seeking to expand in the racquets club format in competition with David Lloyd Leisure and First Generation. L&G Ventures bought the 21 strong Total Fitness. Fitness First, the biggest UK operator with 150 clubs is expanding again whilst LA fitness with 66 clubs is taking a more cautious approach with only limited openings planned. Cannons and Holmes Place are rumoured to be considering a merger and further consolidation seems likely in 2005 as the customer base establishes its own level.

Rochester, Medway Valley Park: Rent reviews on behalf of Capital & Counties.

Kidderminster - Weavers Wharf
Letting on behalf of Centros Miller.

Night Clubs

- The nightclubs sector continued to feel the pressure as First Leisure went into receivership with its 28 clubs, and Bakersfield Entertainment's eight Mood clubs recently followed suit. Live music venue operator McKenzie Group, which owns Brixton Academy and Shepherds Bush Empire, was bought out by its management who intend to expand the Academy concept. Luminar Leisure intends to sell a number of unbranded venues.

Ten Pin

- AMF Bowl sold its 33 strong UK chain to Bourne Leisure, reducing further the number of players in this market.

Restaurants

- Private equity firms continue to be attracted to the restaurant sector with TDR Capital acquiring Ask Central with 170 outlets, adding the Ask and Zizzi brands to their Pizza Express ownership. Urban Dining bought the Tootsies chain. Restaurant chains including Nandos, Wagamama, La Tasca, TGI Fridays, Prezzo, Fat Cat, Tootsies, Carluccios, Frankie and Bennys, Strada and the more traditional offers Burger King and KFC continue to expand. McDonalds introduces more healthy alternatives in an effort to regain market share. Dominos and Pizza Hut go on major drive to expand take-away sites.

Public Houses

- Consolidation has continued throughout the public house sector this year with most operators continuing to review their estates including JD Wetherspoon, Regent Inns and SFI Group. Operators who are expanding include Barracuda, Urbium and London & Edinburgh Inns. Industry concern about a possible ban on smoking in pubs and recent press coverage highlighting the problems of binge drinking, together with the change in the licensing laws due next year make it an interesting time for the sector.

Further information and previous briefing papers

Further Information

Further copies of this and previous briefing papers may be obtained from Chase & Partners as may additional information or assistance on planning and development issues.

Chase & Partners provide comprehensive retail planning and development services to the private sector and local authorities, including 'health checks' and retail impact assessments, and the sequential approach. Graham Chase and Jim Morrissey, Directors of Chase & Partners, have advised over 100 private sector clients and 50 local authorities on retail planning matters in the past 5 years.

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Previous Briefing Papers

Retail Property Briefing Paper 1- October 1996 PPG6 Retail Warehousing: towards consensus? Matter of Control!
Retail Property Briefing Paper 2- November 1996 The Sequential test: Opportunity or problem?
Retail Property Briefing Paper 3- December 1996 End of year Round up - developments in the retail property market
Retail Property Briefing Paper 4- December 1997 End of year Round up - The Retail & Leisure property market
Retail Property Briefing Paper 5- May 1998 rating of commercial property - Update 1998
Retail Property Briefing Paper 6- December 1998 End of year Round up - The Retail property market
Retail Property Briefing Paper 7- December 1998 End of year Round up - The Retail property market
Retail Property Briefing Paper 8- July 1999 The 'need' for development
Retail Property Briefing Paper 9- December 1999 End of year Round up - The Retail property market
Retail Property Briefing Paper 10- February 2000 Flexibility and The sequential Approach.
Retail Property Briefing Paper 11- March 2000 Need and the sequential approach
Retail Property Briefing Paper 12- November 2000 Funding the improvement of Town Centre & town centre management schemes
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Retail Property Briefing Paper 15- November 2003 The governments Response to the proposed changes to the use classes order
Retail Property Briefing Paper 16- December 2003 draft Planning Policy statement 6. Planning Town Centres
Retail Property Briefing Paper 17- December 2003 the Retail Property Market End of Year Roundup 2003
Retail Property Briefing Paper 18- April 2004 Making better use of Supermarket Sites - The London Plan
Retail Property Briefing Paper 19- April 2004 Mezzanines

Dundee: Acquisition on behalf of Alliance & Leicester

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