

# **Response to the coronavirus crisis: experience of commercial property owners and investors in Scotland**

A survey by the Scottish Property Federation (SPF)

## **Executive summary**

This snapshot survey was conducted anonymously with commercial landlords and investors between 27 April and 20 May 2020. The survey was intended to identify landlord and tenant responses to the economic emergency caused by the coronavirus, and to examine the business conditions facing commercial property owners and investors.

Twenty-five individual commercial property owners and investors responded, representing more than 1,600 tenancies across Scotland. The highest proportion of tenants were in the retail and office categories, followed by industrial premises. Other types of tenant included logistics and distribution, leisure, public sector and charities.

The following SPF report is based on the combination of quantifiable data and respondent commentary gathered through the survey. The 16-question survey utilised a variety of question types to create a view of the commercial property owner and investor experience.

## **Key findings**

- All respondents had offered a change to rental terms including rent deferrals, rent free periods, monthly rental payments or amendments to leases.
- Most respondents reported that sole traders, small business owners and SMEs were most willing to engage with landlords to agree new rental/service charge arrangements.
- Conversely respondents found large businesses and multinational tenants the least willing to engage with landlords to agree new rental/service charge arrangements.
- 76% of landlords reported tenants seeking to impose terms without agreement.
- Over half (56%) of landlords said they had tenants able to pay rent but refusing to do so.
- Four landlords were seeking to recover rent via means other than irritancy.
- 64% of landlords reported additional empty property rates tax costs.
- Landlords and investors identified very little financial support for their businesses, although seven respondents had accessed the UK Government furlough scheme.
- Respondents reported some available support via banks to arrange new terms, usually to offer capital interest payments holidays.
- Over half of landlords reported significant financial implications with continued loss of income and additional financial costs, with bankruptcy or inability to service bank debts identified as a key concern.
- Most respondents say the coronavirus and the government responses have changed their intentions on future commercial property investment. One respondent cited the loss of a £500m fund from the UK as a result of the changes in legal rights for landlords.

**Detailed findings**

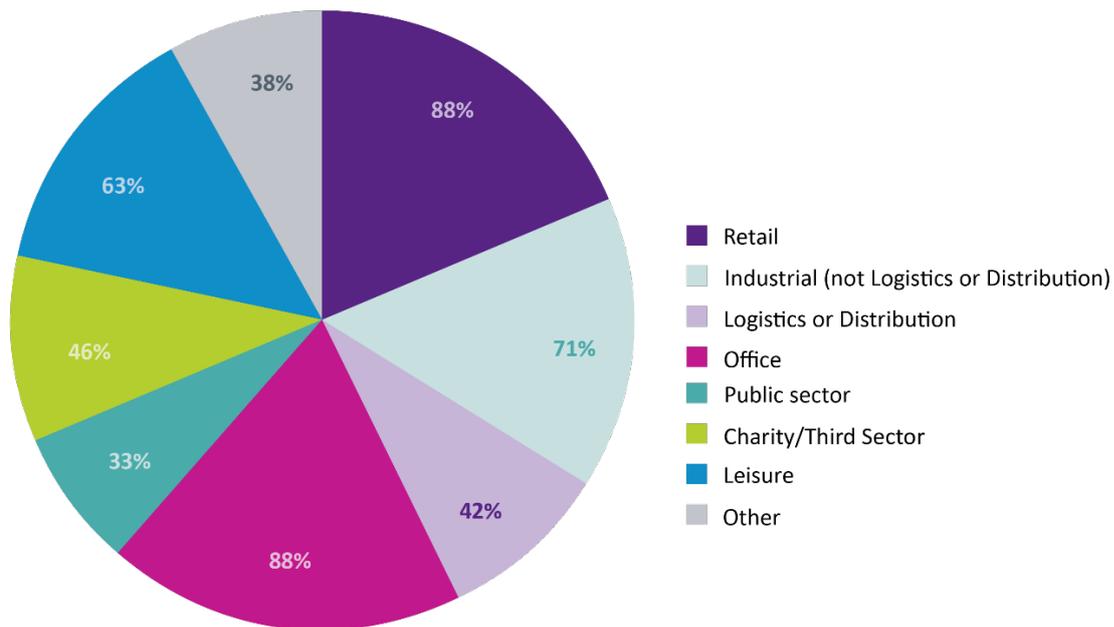
**Question 1 - Can you please provide some background on your property business?**

The respondents represented over 1600 tenancies across all major forms of commercial property business. Six property owners reported being responsible for more than 100 tenants. Twenty-two of the 25 respondents identified themselves as either a small or medium sized business. A significant majority of respondents (17/25) also invested in development or regeneration activities. Two respondents had more than 100 staff, with over 300 staff employed by respondents in total.

**Question 2 - In your portfolio, what proportion of tenants - by rental income - come from the following sectors:**

The commercial properties included in the respondents’ portfolios represented a broad proportion of the economy, as identified in **Figure 1**. The highest proportion of rental income identified by respondents included retail and offices, both at 87.5%. The next highest proportion of rental income for respondents was from the industrial sector, closely followed by the leisure sector.

**Figure 1: Sector of tenants (by rental income)**

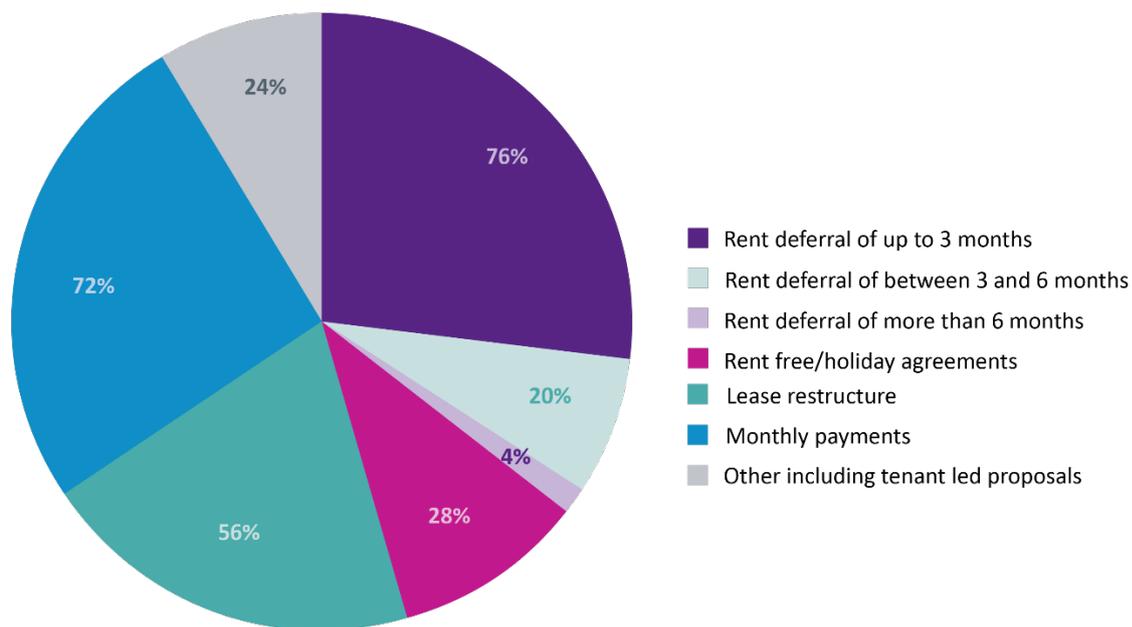


Seven respondents identified that more than half of their rental income was earned from retail tenants. Four respondents received over half of their income from office tenants. Three respondents received 50% or more of their rental income from industrial tenants.

**Question 3 - Have you agreed new rental arrangements with your tenants as a response to the coronavirus lockdown? If so, please identify the new arrangements and if possible, specify how many tenants benefit from these arrangements?**

All landlords who responded had offered some form of new rental or service charge arrangement with some or all of their tenants in response to the coronavirus crisis. The form of new arrangement varied greatly and is reflected in *Figure 2*.

**Figure 2: New rental arrangements with tenants as a response to the coronavirus lockdown**



With 19 respondents indicating their agreement, the most popular form of new arrangement was rent deferral for three months. Seven respondents reported they had agreed rent free arrangements with some tenants. Moving to monthly payment plans was also popular with 18 landlords reporting this new arrangement had been agreed with tenants.

Other responses included examples of future break waivers in exchange for a rent-free agreement now. Another reported agreeing a phased payment plan through the May quarter. Another agreed a half rental plan for six months while another response cited extensions of tenancies that would otherwise terminate during the crisis.

In terms of sectors, there was a widespread form of support offered to different properties. Retail property was highlighted as an area supported by rent deferrals and rent-free periods which reflected the restriction to trade for large parts of the retail industry.

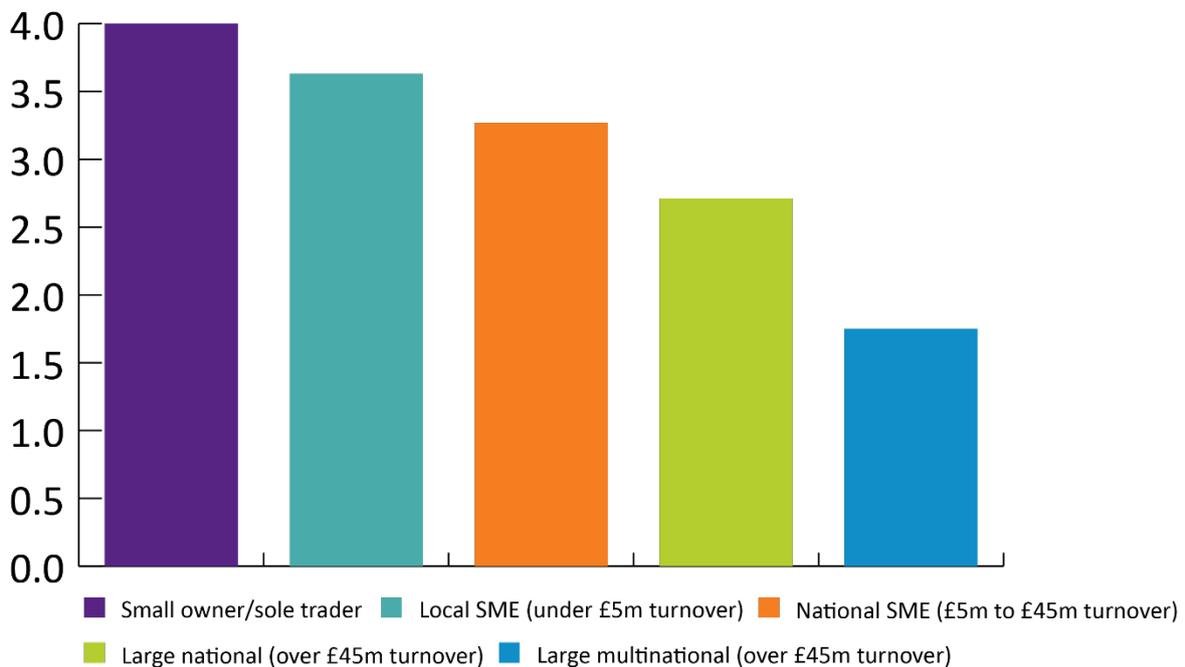
**Question 4 - What proportion of your tenants are small and medium sized businesses as identified by the UK Treasury (under £45m annual turnover)?**

Most respondents (64%) said that 50% or more of their tenants were SMEs.

**Question 5 - Which category of business has been most willing to engage with you and agree new property rental/service arrangements - please identify?**

The responses to this question were analysed using a weighted average score based on a scale of 1 to 5 with 1 representing the most willing category of business to engage in discussing new arrangements. Most respondents (67%) identified sole trader or small business owners as the most willing to enter new arrangements.

**Figure 3: Category of business most willing to engage with landlord**



**Question 6 - Which category of business has been least willing to engage with you to agree new rental/service arrangements - please identify?**

The answers to this question were analysed using a weighted average score of responses, based on a scale of 1 to 5 with 1 representing the category of business identified by respondents as least willing to engage in discussions on new arrangements with their landlord. Most respondents (74%) highlighted that multinational tenants were the least willing to engage with landlords on new terms (see *Figure 4*).

**Figure 4: Category of business least willing to engage with landlord**



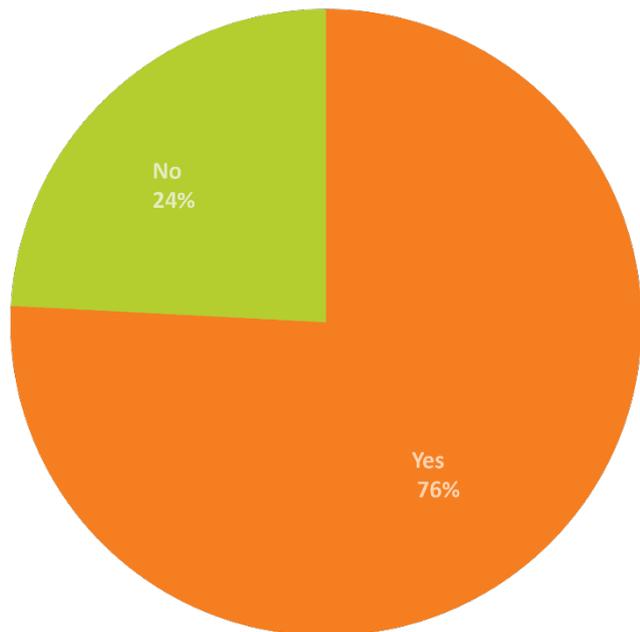
**Question 7 - Have you experienced tenants seeking to impose new arrangements without negotiation?**

A majority of respondents reported experience of tenants seeking to impose new arrangements without negotiation, (see Figure 5).

The respondents highlighted significant cases of their tenants being unwilling to collaborate. One respondent noted that *‘some tenants are simply not paying nor contacting us.’*

Another argued that *‘without exception these are well funded national brands who adopt their approach without consultation or even notification.’*

**Figure 5: Landlords experiencing tenants seeking to impose new arrangements without negotiation**



**Question 8 - Have you any evidence of tenants who could pay rent, but are deciding not to do so since additional protections from eviction for non-payment of rent were introduced under the Coronavirus Acts in the UK and Scotland?**

More than half of respondents (56%) stated they had evidence of tenants who could pay rent but have chosen not to since the law was changed to forestall landlord action for non-payment of commercial rent. This view was highlighted by a respondent who commented, *'some are using the virus and the restrictions on landlords as an excuse not to pay'*.

Other landlords noted:

*'Various tenants deciding to change terms of payment with no forewarning or consultation. In most [cases] these tenants are capable of paying or have alternative means of sourcing finance.'*

Several landlords suspected more evidence of tenants choosing not to pay would happen after the next Scottish Quarter Day.

Another theme identified was the uncompromising approach of some national multi-outlet businesses. A landlord observed that *'some national tenants are looking to impose arrangements across their portfolio.'*

**Question 9 - Have you initiated other forms of rent/costs recovery action beyond irritancy proceedings (now 14 weeks since Coronavirus Act)? If so, for how many tenants and please add further information on the circumstances if possible?**

Four landlords reported they had initiated action for recovery of rental or service charges.

**Question 10 - Are you able to identify how much rental and service charge income your business has lost since the coronavirus lockdown?**

Respondents provided a wide range of answers to this question. Of those providing cash figures (7) some £2.8m was reported as lost income. A further two respondents cited 100% and 60% of income respectively. Only three said they had as yet no lost income.

**Question 11 - Can you specify the level of empty property rates liabilities you have for your properties?**

Most respondents said they had incurred additional tax costs of empty rates due to coronavirus. Eight respondents said they had no such additional costs at this stage. Of the seven respondents who indicated actual costs (£1.16m combined), an average additional tax charge of £166,000 was reported.

**Question 12 - Have you been able to access any government related business support measures?**

Only one respondent has been able to access a government grant (for a leisure property). No respondents said they had been able to access Coronavirus Business Interruption Loan Scheme (CBILS). One respondent had been granted the time limited empty property rates relief (for 3 months for a newly vacant property). Two others had applied to their local authorities and awaited a reply. Seven respondents have accessed the UK Government furlough scheme.

**Question 13 - Have you been able to access further financial support during the crisis? If so, please provide as much information as you feel able to, including any interest costs or fees you are being required to cover?**

Six respondents have been able to access some form of support from their lenders. This is typically in the form of capital and/or interest repayment holidays. There was no further support identified from insurers, financial markets or debt funds reported.

**Question 14 - Have you been required to lay off or furlough staff as a result of the economic impact of the virus?**

Seven respondents have laid off staff so far.

**Question 15 - What are the implications for your business of further losses of rental income or service charge cost recovery - can you specify a time frame on these implications if you are able to do so?**

Most respondents reported serious financial implications facing their business, including likely bankruptcy, failure to service bank debts or loss of pension income.

*'If rental income remains unpaid, we will go into a loss and eventually have problems in servicing bank debt'. This view was echoed in another response: 'if no rental income [is] received then the company will be insolvent in 6 months' while another remarked 'within six months the business will no longer sustain the employees.'*

Another respondent summarised the loss of rental and service charge income would mean *'potential bankruptcy of business after nine months of this'*. Other respondents highlighted the consequences of lack of service charge income: *'Service Charge recovery reduction has an impact on service delivery and the supply chain that provides those services.'*

The relationship between rental and service charge income, and development was also explained in detail by respondents:

*'Best case, lack of free cash to be able to fund development activities on the other side of the business. Worst case, breach of loan covenants, be they interest/debt service cover (due to shortfall of income and additional cost) or LTV (due both to likely capital markets impact on the current situation, but also the valuation impact of non-paying tenants, or voids as a result of tenant failure) leading to action by Banks requiring crystallisation of sales at [a] bad time'.*

A respondent noted the impact on pension income: *'If my business loses 60% of annual income, and has to pay business rates, it will be running at an annual loss. I rely on net income as I have no pension in lieu of owning retail property'.*

The responses highlighted a combination of negative factors contributing to severe financial implications for landlords and investors. This 'perfect storm' of challenges for landlords was illustrated by a respondent who summarised their experience as follows: *'Voids, extortionate vacant rate costs, loss of profit, loss in capital value of assets which could trigger bank default'.*

**Question 16 - Has the response to the virus changed your intentions on future commercial property investment?**

Most respondents (16) cited changed investment intentions for commercial property investment. Comments to this question highlighted the implications for future office investments and changing asset allocations. One respondent cited the loss of a £500m fund to the UK.

*'Yes. We buy out of town offices and will continue to do so. We will be very unlikely to ever buy high street retail or retail parks or leisure. We previously would have bought city centre high rise offices but now we would be very cautious of properties that cannot easily socially distance staff (i.e. lift access) and have no car parking, forcing staff to use busy public transport provision.'*

*'Yes, a number of our investment partners are from overseas, they invest with us on the basis of the mature and transparent legal system within the UK which [is] designed to protect all parties. Given the [government] have moved the problem to landlords and changed the legal system overnight, the mature stable view that was held six weeks ago has evaporated overnight. Acquiring a property for a value which is based on contractual obligations to receive rent has undermined the market, we will not be investing in the UK commercial property market until the [government] either changes its stance or Landlords are shown the same sort of recognition and protection that tenants have. We had circa £500m allocated to the UK market over the next 12-18 months. Whilst part of that has fallen away overnight as a result of the [government] stance, we will not be investing the residual of our investment pot.'*

Contact:

David Melhuish

Director, Scottish Property Federation

[dmelhuish@bpf.org.uk](mailto:dmelhuish@bpf.org.uk)

07387 272376