APPENDIX 1

DTZ Advice on Hinckley Town Centre Bus Station Scheme

June 2013

1. Town Centre Retail Led Development

1.1 The town centre development market remains weak – for the first time in four decades there were no significant town centre schemes opened in 2012, with only one new shopping centre opening in the UK in 2013 (Trinity Leeds – opened March). Numerous town centre schemes conceived pre the property market boom have stalled. However, a high proportion of these are in the process of being re designed/re-engineered. This involves a combination of "right sizing" – reducing the floor space to a level commensurate with the contraction in occupier demand, cost engineering – omitting through re design expensive construction components and direct public sector investment – invariably making land available at values which reflect market reality.

1.2 There has been a reduction in the number of active developers in the market – several have gone into administration e.g. Thornfield Developments, Teesland and Modus, whilst others have become increasingly selective. Those active e.g. Stanhope, Hammerson, Land Securities, Henry Boot, Westfield and Centros with cash/capital available for new schemes are reluctant to pursue anything other than prime product/development opportunities in the strongest towns and cities, where market (occupier and investor/funding) risks are less pronounced. For many other developers the dearth of available short term bank finance has served to temper their appetite and this has led them to be similarly selective. Until there is a discernable change in lender attitudes, it is difficult to see any improvement or alteration to this pattern of developer demand.

1.3 Short term funding markets remain challenging with debt finance extremely scare, as banks seek to reduce their exposure to the real estate sector. Where finance is available from banks, this is limited to extremely low risk development opportunities with high pre let thresholds. Minimum requirements for the few lenders willing to consider funding now include either 100% or a significant majority of a property to be pre-let, increased developer's profit margins and ever decreasing loan to value (LTV) ratios. Even where these criteria can be satisfied, debt it is often only available for prime developments where the relationship between lender and borrower is strong, the borrower has a proven track record and a significant asset base and, notwithstanding satisfaction of these criteria, arrangement fees and interest costs are generally onerous. Funding for speculative development is all but impossible to secure.

2. Occupier and Investment Markets

2.1 The prevailing uncertain economic climate has made retail market conditions extremely challenging - pressures on discretionary expenditure has impacted upon consumer sentiment and sales, with any significant improvement unlikely over the short term at least. The weakness of the economy is one of the principal reasons behind the dramatic fall in occupier demand – it has

contributed to a number of well publicised administrations, with examples including Woolworths, Clinton Cards, Game, TJ Hughes, Jessops and HMV.

2.2 According to Centre for Retail Research, 2012 was the worst year since 2008 for retailer failures, with more than 48,000 employees affected, almost 4,000 stores and 54 retailers. The reasons include: a second economic downturn causing weak retail sales; the failure of a few retail giants (e.g. Peacocks and Comet), which bumped up the figures for affected employees and stores; and the exiting of many companies that could survive a year or so of recession but not four years of low profits or losses. The outlook for 2013, based on data to the end of May, looks poor.

	Companies failing	**Stores Affected**	**Employees Affected**
2013 (to end May)	31	1,905	18,645
2012 (12 months)	54	3,951	48,142
2011 (12 months)	31	2,469	24,025
2010 (12 months)	26	944	10,930
2009 (12 months)	37	6,536	26,688
2008 (12 months)	54	5,793	74,539
2007 (12 months)	25	2,600	14,083

2.3 In an effort to reduce costs and preserve margins, retailers have also been rationalising portfolios, reducing their requirements for new space and disposing of poorly performing stores, particularly those where the catchment population can be serviced from larger centres. This trend, which is expected to continue over the short term, has further led to rising vacancy levels (current UK average according to The Local Data Company is 14.1% - April 2013) and contributed to a widening gap in confidence between prime and secondary locations and between large regional centres/major out of town schemes (such as Meadowhall, Trafford Centre and Merry Hill, Dudley) and sub regional towns and cities. As such retailer demand and the pattern of rents has become polarised - rents particularly in secondary locations have fallen and even in the stronger centres where there has been limited growth, this is invariably sustained through an increase in landlord incentives.

2.4 Internet retailing is continuing to gain significant market share and while this has affected certain sectors more than others (music, DVD's and books) retailers have increasingly embraced its growing importance. It is clear that the threats and opportunities emerging from the increasing migration to online retailing will play a significant role in shaping the retail property market over the medium to long term. The days when a retailer needed a store in every town

have now gone - whereas five years ago a retailer may have sought a geographic footprint of around 200 stores to cover the UK, it is now considered that a good "multi channel" retailer will only require 60-70 stores in the UK by 2020. This means that a retailer will need a very compelling reason to enter a sub regional centre rather, as they would in the past, than to simply gain geographic coverage.

2.5 The challenges facing the delivery of viable new town centre developments are compounded by the cost of securing major fashion pre-lets. Increasingly, fashion retailers will seek 'anchor type' deals with significant rent free periods, capital incentives and enhanced specification in the units. Retailers who commit early in the process will expect better terms and will also insist on a number of 'adjacencies' to be delivered i.e. they will provide a list of perhaps 10 retailers and require that 4 of those are secured in the scheme for them to complete. Whilst these rental, letting and incentive trends are built into Tin Hat Company's appraisals, any significant improvement in occupier demand is unlikely over the short term, with correspondingly limited prospect for an improvement in the viability of the scheme in its current form.

2.6 Long term Investor/funder requirements for town centre retail schemes largely mirrors the pattern of occupier demand, with a focus on prime stock in the best sub regional and regional centres. Here yields have remained firm, but away from prime locations yields have increased and according to the latest data from Investment Property Databank (IPD) this trend is continuing, with the gap in yields between prime and secondary stock widening. There is very limited speculative development funding activity, with funders reluctant to consider any such schemes, unless they are substantially pre let (75%+), even in the best centres, with healthy prospects for letting the remaining units. We expect this funding trend to remain for at least the short term (18 months – 2 years).

Food Store Development Market

2.7 Since Tesco published below par trading figures early in 2012, they placed a moratorium on new store development, pending completion of a strategic review. The review remains ongoing, although early recommendations, including a downsizing of new stores with a shift in emphasis to convenience goods, are already being implemented. In practice this means a shift away from large "Extra" stores typically with a gross area of 100,000 sq ft +, with their largest stores now likely to comprise 70,000 sq ft. This clearly has implications for site requirements – whereas a typical at grade "Extra" store would require a site of 9-11 acres, the smaller at grade formats can be accommodated within 5-7 acres.

2.8 The significance of their shift in policy on the wider market can be assessed in the context of UK market share – Tesco at 30.70% is almost double the next largest being ASDA at 17.60%, with the remaining 2 of the "big 4" Sainsbury and Morrisons, respectively having 16.60% and 11.90%. Since Tesco announced its new store strategy, their competitors have similarly been reviewing new store requirements. Evidence is emerging which suggests that most are reining back requirements and becoming more selective over location/store size criteria. The majority of the other "big 4" have less exposure to large format (100,000 sq ft) stores with generally, smaller areas given over to comparison goods.

2.9 Although too early to discern the extent to which these changes in market dynamics are impacting on broader trends in rental levels and yields, through

DTZ's involvement on other sites we have witnessed a limited number of either renegotiations or offers at lower rent levels than would have been achieved (or were agreed, but not contracted) some 6 months ago. In each case, however, there was negligible operator competition and, thus, there is some doubt over whether this pattern would be mirrored if such competition can be established or demonstrated.

2.10 In contrast to occupier demand, there has been no measurable change in the investment market, with strong demand from funds for food store product where the benefits of investments secured on long leases to financially undoubted tenants such as the "big 4" are highly sought after. Prime yields at 4.50% - 5.00% remain at a premium over yields achieved for other forms of retail property investment such as high street shops or fashion parks.

Leisure Market

2.11 The Food & beverage market had a robust 2012 trading year, despite the weak economy. The signs so far in 2013 have been for a similar performance in the sector overall. There continues to be a geographical divide with London & the south east weathering the recession better than the rest of the country, but with unemployment remaining relatively high and pressures on disposable incomes, operators remain cautious over their expansion plans.

2.12 The main restaurant groups that continue to acquire for their various brands, are seeing the current market as an opportunity to further strengthen their dominant position in the market, acquiring units on favourable terms. It has also led them to focus on key requirements and, with investors and developers increasingly looking to court the leisure market, this has extended the choice to operators. Those groups chiefly acquiring in the casual dining market include:

- Gondola: owners of Byron, Pizza Express, Ask, Zizzi
- The Restaurant Group: owners of Frankie & Benny's, Chiquitos, Coast to Coast and their pub brand Brunning & Price
- Nandos – VC investors also own GBK
- Mitchells & Butler: owners of All Bar One, Browns, Harvester, Miller & Carter, Toby Carvery
- Prezzo & Chimichanga – major share holders are the Kaye family who also own Richoux cafe, Wild Wood & Dim T.
- Carluccios
- Wagamama
- Tragus: Ortega, Strada, Bella Italia & Cafe Rouge & Rouge Express
- Slug and Lettuce:
- Increasing number of street food operators and express catering linked to the super prime shopping centres.

2.13 Following the recent withdrawal of Byron from the market parent company, Gondola Group has instead said they will accelerate the expansion of their other brands highlighting their confidence in the UK market.

2.14 The fast casual market remains strong with operators having reinvigorated their brands such as McDonalds following the success of their sponsorship of the Olympics. The biggest growth area in this section of the market has been in street markets. In reality, the preparation, purchase and consumption of food street-side has been a consistent feature for years. It is the change in the types of food served extending to faster casual dining concepts like Tapas

Revolution, Rhythm Kitchen, Pho. All are looking to extend their offer outside of London in strong retailing locations, ideally in more affluent food clusters rather than the traditional Food Court environment.

Summary

2.15 The combination of economic uncertainty, significant changes (decline) in retailer demand, developer failures and severe short term (bank) funding constraints have resulted in a marked reduction in town centre development. Those developers currently active are afforded the luxury of choice and as such they are being highly selective, focusing on larger towns and cities where occupier demand is strong and delivery risks are perceived to be low. We are therefore doubtful that, if the Bus Station opportunity, as proposed in the 2007/8 Development Brief, was put out today, there would be anything other than very limited developer interest for the delivery of the comprehensive scheme, as then envisaged. This position is likely to remain for the foreseeable future.