

Current Review

rent review and business development for retailers

June 2009, 69

Getting the economy to work for you

In June 1989, when I said " the emergence of the 'Green' consumer marks the onset of a major shift in attitude that will have repercussions for all aspects of future retailing," it wasn't Sir Philip Green that I had in mind!

I'm not especially competitive - I'm more than capable of coming up with original ideas to improve my services to businesses I admire and respect without having to take heed of what other surveyors are doing - so I've had to do some research into what a retailer that is into winning, but losing out, might do, to avoid having to change the error of its ways.

In sport, it's "cheating" but, in business, it's called "resorting to subversive tactics". To get away with that successfully, the visible side of the business, what it spends money on in public, must be held in check. Winning in business is about maximising profit, but the question is for whom? Most landlords are not easily fooled and, with the help of the media into reporting retailers, landlords are adept at identifying a difference between initiatives to attract custom and those solely of benefit to directors and owners. The only way for directors and owners to keep themselves lavishly is to make savings where the company dictates or has choice, such as staff and suppliers. Although departures from the terms of a lease are not in that category, the campaign for monthly rents has paved the way for a host of complaints about the property system but, in my opinion, jumping on the bandwagon when you can pay rent quarterly - which most retailers managed before the high-horse strode out (also, quarterly already enables the annual rent to be paid in 4 instalments) - is a mistake, because it's the trap of the downwards spiral. Although managing cash-flow is eminently sensible, how a business goes about it rubs off on managerial credibility. For example, the statement "everyone is in the same boat" does not hold water. Why is it assumed a recession is some sort of natural disaster which has come out of the blue? It's not: recession is 'man'-made: at macro level, how the UK economy has been managed in relation to the whole and, at micro, how each business has been managed in relation to the economy. And, in terms of foresight, also known as 'competitive advantage', it's not about working for the economy, but getting the economy to work for you.

As I see it, innumerable hard-working decent honourable tenants, good at what they do, have found their property costs inflated as a result of the knock-on effect of uneconomical rental evidence, the legacy of a bunch of irresponsible retailers that behaved like drunken idiots throwing their weight around when they could borrow lots and go on a spending spree but no longer full of confidence now the money-tap is off. Indeed, with balance-sheets hung up for all to see, it is interesting just how many retailers are heavily indebted. Which makes one wonder where all the money went.

Let's face it, an awful lot of retailers are not as good as they like to think, and many were struggling before recession arrived. It's also fascinating how many multiple retailers think the world owes them a living. And how fond they are of blaming rent, rates, the economy, for their loss-making. In retailing, as in any other competitive business sector, just because a company has been on a high doesn't mean that's its rightful place. Often it only got there because of the momentum of shopper-impulsiveness, or was better at hype than stocking what people want at prices they're happy to pay. Citing recession as the reason for falling sales is akin to telling off customers for being discerning. More often than not, and contrary to what they'd have you believe, the truth is a failure to address operational difficulties.

So, rather than expecting landlords to act like an extension of social services, retailers should get pro-active, both for their own good and for the good of the shopping public. Instead of joining in to encourage landlords to be accommodating to everyone, which is something retailers in trouble are good at, so as to muster support for a lost cause, forward-thinking retailers should urge landlords to stop giving concessions to retailers in difficulty - in effect, subsidising loser existence - because by doing so landlords are interfering with market forces, thereby imposing on those retailers that do have what it takes a need to perform so much harder than would be necessary if only all the duff retailers with outmoded business models could be got rid of, for once and for all. Which, if left to its own devices, is precisely what recession would do.

I look forward to helping you in some way

Recession: a time for transformation

As I say time and again, essentially, a problem is a fault in direction which, when left to its own devices, may fragment into seemingly different problems, so as to attract attention. It is not enough to resolve a problem: it must be transformed. Finding a solution simply dilutes the problem, until it is bearable. It is not enough to alter perception: when symptoms are merely relieved, the problem will crop up again.

Transformation is a thorough, possibly dramatic, change in underlying attitude. In my healing experience, such as it is, few people are adept at transforming problems into commercial opportunities as they go. Mostly, people metaphorically brush problems under the carpet, ignore them and hope they'll go away. They don't. The problem waits for an opportunity to arise again, often in different guises. When you have an unresolved problem, you will not progress. You, your business, are stuck.

A problem at micro-level becomes a macro large-scale. In CR (QC06) December 1985, I said "Costs in the property industry have reached record levels. The actual amount of money involved in day-to-day transactions imposes constant pressure to meet critical financial targets. Any attempt to question or stop is met by a barrage of vested interests intent upon maintaining momentum. The cost of error is rapidly reaching the point whereby individual foresight will be crushed by the weight of uncontrollable dynamism. *In the prime shop market, the corporate income of some retailers is inextricably bound up with the consumer's willingness to keep on spending on credit. It only needs a few months' lull for the structure to crack under the weight of operating costs.*"

And in CR50, June 1998, "When retailers get carried away and form the wrong impression of reality, the knock-on effect is destabilisation. Flat demand is caused by an addiction to competition."

Generally, retailers don't care where the money comes from. As long as it does. As long as the business plan is approved

by the bank and facilities can be renewed, as long as customers can be persuaded to spend more, as long as the lust for more shops can be satisfied, as long as landlords can be dumped or treated like any other supplier, that's all that matters. Operating in splendid isolation, indifference to the wider long-term consequences cannot be appeased by giving to charity: playing power-games, bullying tactics, is completely the wrong approach for long-term consistent success.

Not only retailers, but also landlords and surveyors have fallen down the slippery slope. Indifference to repercussions of pro-active asset management, over-developing, over-estimating values, manipulating rents, it all fuels the get-rich-quick mentality, and the greed has so rotted the core that they're going cap in hand to shareholders and banks for more money to feed the cravings.

It's not the market's fault. That is akin to admonishing customers, the source of spending-power. It's not that the market suddenly turned, or no one could have foreseen. The direction had been changing for years. It merely needed to tip the balance. It was foreseen, but warnings went unheeded. Views like mine are not what most people want to hear. In December 1985, I said "success in retailing today is too dependent upon the availability of credit. Credit enables retailers to control the concept of what represents value for money." As I said in June 1998, "the cost of prejudice: a preference for conformity. It is thinking problems are normal."

Credit interferes with the law of balance. It increases the money-supply artificially. You cannot blow something out of all proportion and expect it to stay there. A time must arrive when it bursts, a point at which it is so fed up it cannot contain itself. In my opinion, the bubble was about to burst in mid-2004, but greed gave it a final blow. In April 2008, as I put in my blog "in my opinion, the sub-prime crisis was deliberately orchestrated by some very shrewd operators who have made trillions of \$ or whatever out of the

debacle." Be that as it may, the credit-crunch has highlighted just how much pretentiousness exists.

Credit creates its own vicious circle of spiralling costs. Artificial growth, opening more shops, for more than fair share, gives an impression of strong demand, thereby attracting competitors, increasing pressure for performance. Also, the terms of a loan can restrict the freedom to synchronise with reality: the direction in which customers are going. Businesses and properties exist to serve customers: not the other way round.

Borrowing is considered par for the course, but whereas it is okay to want a helping hand to begin with, there comes a point surely, when a business ought to stand on its own feet? In my opinion, for a business to consider itself successful it should have no need of debt. That is not to say it should not have any borrowing facility, simply it should rarely need to use it. The credit crunch shows just how much businesses that depend on borrowing have become a drag. In the aftermath of years of a booming economy, that few businesses have amassed cash confirms most directors are more interested in "living the life of Riley" than ploughing the profits into developing the business.

The money has to come from somewhere. To live off borrowings, assuming they would always be replenished on the strength of the business plan, is the result of allowing the art of avoiding challenging questions to run companies. It is a wonder of the pyramid, whereby the person in charge surrounds themselves with layers of management, so as to create the illusion that person must be very talented. Not realising the light at the end of the tunnel could be the train coming towards you can lead to a series of mistakes that start when someone is sold on an idea and there is no stopping them. By the time the idea is up and running, it is failing all over the place and costing a packet.

I think it's sad, not to mention a waste of resources, that retailers and landlords are obliged to fail, and for shareholders to suffer, before directors will learn how to listen. Perhaps it's hardly surprising: their contemporaries are on the same wavelength: standing firm and resolute

With lease restructuring, it may be necessary to think a long way ahead to avoid problems in the making.

I act for a successful retailer in East Anglia, one of whose branches is on a under-lease from Homebase Ltd. Like many large companies, Homebase has a residual estate: numerous properties that it used to occupy, but which have long since been conveyed to others.

According to April 2009 accounts, in the public domain, Home Retail Group plc, which owns Homebase, made £117.3M provision for onerous lease charges. The past catches up!

In this case, Homebase wanted to assign its lease with an indemnity for the remainder of the term for a difference in repairing covenants, so my Client would be no worse off.

Terms were agreed in principle. At the onset, I said I should not recommend my Client instruct solicitors until the freeholder's consent had been obtained. The head-lease contains a surrender-back clause, also I did not want my Client to incur costs unnecessarily. Homebase applied for the licence, a draft was submitted by the freeholder's solicitors, and I was told by the surveyor acting for Homebase consent had been given. However, what was not disclosed until much later on was that the freeholder had not actually given consent, because it was still awaiting reply to its enquiries about my Client's accounts. [Whether the freeholder's solicitors,

Thinking further Ahead Pitfalls in lease restructuring



in having issued a draft licence, was enough to deem consent was never resolved: that would've meant applying to court for a declaration, which Homebase would do provided contracts to assign were first exchanged, (on condition if the application failed then the transaction would abort.)]

As the conveyancing progressed, I started thinking further ahead. Even if the freeholder were shown to be unreasonably withholding consent, I felt my Client would be off to a bad start if the landlord were ordered to consent against its will. No matter the business tenancy law, the human element in the ongoing relationship between landlord and tenant is important. Then there was the question of personal surety. The underlessee has no surety, which would mean, on expiry of the head-lease when Homebase's interest ends, and the under-lease is renewed direct with the freeholder, there would be no need for surety in future. (The under-lease is inside the 1954 Act so has renewal rights.) In the head-lease, the freeholder can require personal surety

for a ltd company assignee. My Client offered an associate company, but not a personal surety. Had the matter gone to court, it is possible the court would have ordered a personal surety with any licence to be granted, which would mean my Client worse off.

The difference in repairing covenant could also cause problems. The under-lease contains a schedule of condition, whereas the head-lease is full repairing. The cost of the difference is estimated at £100,000, at least. I got Homebase to agree to extend the indemnity beyond expiry of the term into any holding-over period, but that benefit would only have practical effect if the freeholder were to serve a schedule of dilapidations whilst Homebase were around. There would be nothing to stop the freeholder waiting until Homebase were completely out of the picture before serving it on my Client. Similarly, if my Client did not want to renew, then its terminal obligation would be limited. Also, by taking on the head-lease, the under-lease could have been extinguished, losing the benefit in having the schedule of condition continue on renewal of the lease direct with the freeholder.

I concluded the risks outweighed the benefits, so I recommended withdrawal from the transaction.

You will find more case histories in my blog at www.michaelliver.co.uk

on a massive psychological block A clean-sweep is necessary: to remove from positions of power those that need tangible evidence before they'll act.

Fact is when you ignore the signs and don't change willingly, change will be forced upon you. It's as simple as that.

For long-term consistent success, to be progressive, to avoid coming unstuck in times of change, you have to think deeply and not allow superficial influences to cloud your judgement. As I say on my web site, "I think it important to have a feel for what you do, because then you can find your way around in the dark". It is clear to me what is happening. It's a

shift, to living true to form and allowing business development to unfold naturally. If you would like to know what that means for your own business then I should be pleased to advise.

PS - Every little helps Tesco to lose

As you may know, everyone, staff, supplier, adviser, associated with your company is an 'ambassador' of the company. What you may not know is that some surveyors are prone to 'surveyor-rage' when they cannot get what they want. I doubt Tesco care,

since it's only interested in numbers, but if they should want an example of why their UK market share is slipping, they should look to their own people, because I shall never spend a penny again at Tesco (except reluctantly at a sub-post office). During negotiations for a rent review at one of its shops, where I was acting for the landlord, their external surveyor was so aggressive towards me that I was physically shaking by the end of the telephone conversations when he rang me.

Mind you, we do our proper shopping at Waitrose. Always have done, always will.

Holistic Credentials

I've always had an unusually good understanding of retailing as well as property, but my retailing understanding used to come from reading and observation which is like thinking you know all about negotiating rent reviews because



you've a shop or two. So, to bring myself into the real world, in my spare time, from 2003 to Christmas Eve 2008, I helped my wife, Clio, run a shop in Ledbury and I'd like you about our experience.

To be honest, it was my idea: ever since I became an organic wholefood vegetarian in 1984, and involved in the holistic movement, I'd felt the urge to run a health-food shop but, for one reason or another, it remained a dream. When the opportunity arose to have a go, the shop was a Grade I listed building in a mews in the heart of Ledbury. Although Ledbury's population is only about 10,000, the retail mix is impressive, including 4 banks, a sub-post office, Tesco, Somerfield, Boots, Greggs; CC opened recently; also a railway station with direct line to London, Birmingham and South Wales; and Ledbury is a popular market town for tourists. For the lease, we took 12 years with an option to break at the 6th year and rent reviews at 3 yearly intervals. I deliberately over-agreed the rent, so there was no increase at the review. We could've paid rent monthly but I opted for quarterly because that would hold us in better stead with the landlord. Clio designed the shop. I won't tell you the source of inspiration in having bespoke shelving, made of pear-wood, except to say it involved multimillionaires which we are not. The effect was such that virtually every customer remarked what a lovely shop (and after we vacated the landlord relet it within days). Clio is an excellent salesperson, but neither of us had experience of actually running a shop, so it was a shock to discover just how much there is to do all the time. And for me, that meant overloading so as to continue with rent reviews, etc for clients. We installed CCTV for security of staff; to a Saturday schoolgirl, we paid £6 an hour (in 2004): about 40% more than she got working in Somerfield. To provide

a quality service, we went for EPOS in a limited way. z1 became familiar. No cheques, it was cash and credit cards only and we were possibly the first in Ledbury to have chip and pin. We traded as The Rice Cake. I created an information-only web-site. For the launch, I delivered a leaflet to every

house in Ledbury and we got interviews on BBC local radio. We wanted to sell organic groceries, only what we'd use ourselves or recommend, avoiding items that don't stand up to scrutiny when you read the small print on the label, but it became obvious our taste was too purist for many customers; we conceded, but so uncomfortable were we with some products that we hid them in a cupboard and only sold them when the customer asked. There was another health-food shop in Ledbury and locals were partisan. We were co-existing okay, until a 3rd health-food shop, a multiple, opened and our older and poorer customers deserted. So we changed the name of our shop to Muse Organix, The Skin Care Centre, and started selling organic and natural skin-care products, which suited Clio because she has a Cidesco Diploma. It was much more enjoyable to have adult conversations with customers, particularly women choosing their Dr. Hauschka. Of make-up or, as I used to tell them, face painting for adults, "can I give the impression of being helpful" was my sales-talk. People shopped from miles around: we could beat supermarkets, department stores and the Internet on price: we gave 5% off RRP when customers spent at least £10 and 11% discount when £20+. A month before Christmas 2008, we held a private sale for regulars so they could buy the best stuff before the final days bargain-hunting vultures got to hear. A few weeks after we closed voluntarily, the 3rd health-food shop went broke, blaming the economy! Served them right. For us, it was fun, including the rubbish tip every week. I learned a lot, especially how suppliers use packaging regulations to sell direct via the Internet to customers. Nowadays, although I miss not being able to buy at cost price, whenever I go into a skin-care or health-food shop, I'm glad I'm a customer; I imagine they think the same.

Next time you are on the internet, please visit www.michaellever.co.uk

I specialise in negotiating rent reviews for and business tenancy advice for landlord and retailers.

My fee scale is in keeping with the times. For example, for tenants, at rent review, I charge £500 + 10% of the saving on the proposal with a maximum fee of £1500 (exclusive of VAT) and I do not charge extra for 'arbitration'.

For my year ending May 2009, my revenue has exceeded my target by 15% so, to complement my services, I have launched some new initiatives.

I am compiling a series of ML Guides about rent review, shop investment and business development, and which can be downloaded free from my web site. I hope you find the information useful.

To avoid "you are" as the answer to the question: "borrow at 3-5%, buy at 8%+, what's the catch?", I am creating an on-line resource for landlords and investors in shop property in England and Wales, at www.shopinvestment.co.uk

At www.photoshopfront.org you will find a gallery of photographs of the types of properties I deal with.

On my blog at www.michaellever.co.uk you will find comment, news and case histories. To keep in touch, please click the RSS feed and add the link to your bookmarks. I contribute to the community blog at Reuters RealEstate; and Mary Portas follows me on Twitter.

I offer my healing gift through business development and relationship marketing advice. If you feel help could be of service then please contact me.

In short, the benefit in my services is access to unusual skills, which will contribute far more than most towards the profitability of your business.

Thank you.

Michael Lever