Colliers INTERNATIONAL

# Baltics Retail Market response to Covid-19

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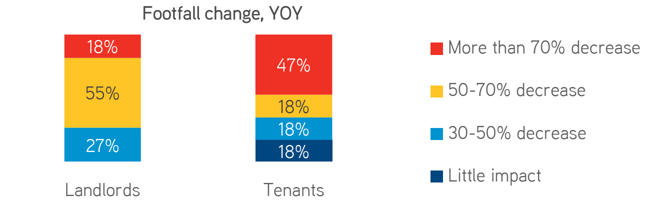
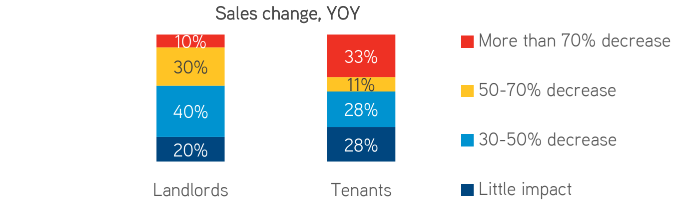
*The outbreak of COVID-19 has made an unprecedented impact on the economy and society on a global level. To better understand how the retail market has been affected so far, at the beginning of April 2020, Colliers has surveyed shopping centre owners and largest tenants in the Baltic real estate industry.*

## ONGOING RETAIL SECTOR TRANSFORMATION

The retail industry has been hardly hit due to the COVID-19 outbreak as firstly, people were advised not to go to the shopping centres, secondly, shopping centres were either closed or their working conditions were limited by the governments* and lastly, large amount of people lost their income. More than 80% of tenants and landlords state that their business activities are currently in some way restricted. 55% of tenants note that there is a reduced consumer activity, however 20% of tenants state that at least the e-retailing channels are doing good. More than 75% of still opened shopping center landlords indicate a footfall decrease by more than 50%. Only one fifth of tenants that are still working indicate stable or less than 30% decrease in footfall (grocery & pharmacy), however, one third indicate higher than 70% footfall decrease (mostly fashion).

Currently, retail is all about online and those who already implemented omni-channel strategies have the highest hope to survive. Even though 40% of tenants that have e-commerce platforms note that overall sales figures have either remained at the same level or increased compared to last year, those are the same segments that have suffered the least – grocery, pharmacy and pet stores. Almost 70% of companies that currently do not have e-commerce platforms believe that there will be increased usage of e-commerce in the future, while only half of those with such solutions already present agree to this.



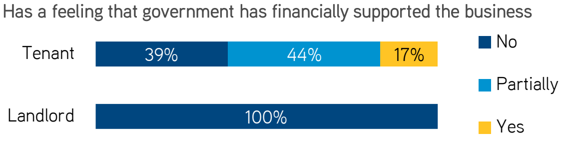



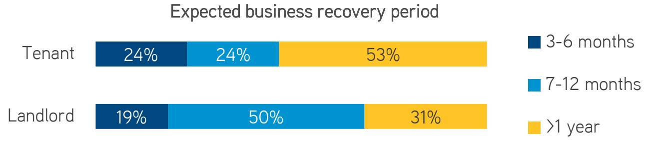

## LANDLORDS' SENTIMENTS VS TENANTS' SENTIMENTS

Large part of retail sector, except for retail supporting everyday needs, is currently idle – partly even closed*. Even though government have incentives to support industries that have been affected, almost 90% of landlords state that government have not financially supported them (directly or indirectly)**. On the other hand, more than 60% of tenants have a feeling that the government has supported them financially.

Overall, almost 90% of tenants are currently using at least one of the government support mechanisms while only 25% of landlords are doing the same. Landlords have been eligible and applied only for reduced/ offset local taxes while half of the tenants have applied for support to idleness workers, 20% have applied for reduced/ offset local taxes and 10% for reduced/ offset VAT obligations.

As of beginning of April, discussions regarding rent-free periods or rent discounts between landlords and tenants were just started. One-third of tenants stated that they are currently having initial discussions with landlords on how to mitigate the consequences of the situation; only 10% had already requested rent brake for less than 3 months and 20% for more than 3 months.



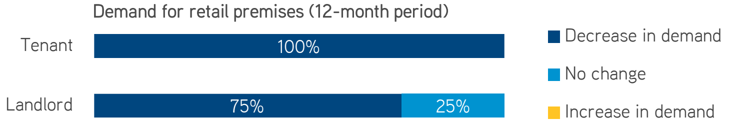
## OUTLOOK

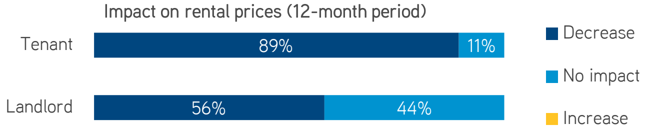
95% of the respondents believe that there will be a long-term impact on the retail industry due to the COVID-19 outbreak.

Even though it is quite hard to predict short-term impact on the market in the current stage, all tenants indicate that there will be a decrease in demand for retail premises during the next 12 months. At the same time, part of landlords is more optimistic – around 25% believe that there will be no impact on demand. Landlord optimism is observed also for long-term forecasts as nearly 20% of landlords think that more retail space will be needed in the long term, while none of the tenants have indicated it. By contrast, 50% of tenants believe that less space will be needed.

Tenants and landlords currently have quite a different look on the rental rate changes during the next 12 months as more than 45% of tenants believe headline rents will decrease and another 45% believe that rental incentives aimed to decrease the rental payment will be implemented. However, less than 15% of landlords believe that incentives for rent decrease will be needed, while they agree that headline rents might decrease. In the long term, 55% of tenants believe there will be an increased usage of turnover rents, while less than 40% of landlords expect the same. It might seem that tenants are looking for more flexibility, however, despite the growing tendency of pop-up shops and similar short-term concepts, only half of landlords and less than 40% of tenants believe this will be an increasing tendency.

Both landlords and tenants are quite sceptical that due to the current events there will be increased automation or more digital implementations in stores, less than 25% believe such impact will take place. Similar situation is with re-development and repositioning of retail premises as less than 25% are expecting that current situation will have any long-term impact on this.




## EMEA/GLOBAL TRENDS

Most of EMEA is now on lockdown, with physical retail businesses – aside from essential services – closed for the foreseeable future. The effects of this pandemic are already having a profound impact on retail businesses – notably on cash-flows and credit scores.

Most retailers have engaged in cost management, primarily cutting employees from the pay roll, cutting/closing stores indefinitely or looking for alternative ways to operate as a business, i.e. e-commerce. In a way, this does present a unique opportunity for retailers to reassess their businesses, look for new opportunities, and highlight areas where they can slim operations and costs. Meaning, with no possibility to trade via physical stores, many businesses are upping their online activities. For some, this is an unfamiliar territory and brings its own set of unique challenges: maintenance, marketing, and deliveries. This comes at a significant cost, and many businesses' models simply cannot make the switch in such a short time frame.

Most landlords across EMEA have adopted some form of rental concessions to safeguard the mutual interests of the landlord and tenant. Looking forward, although landlords will offer heavy discounts to incentivise retailers to their schemes, vacancy in high-streets and shopping centres are expected to increase as more businesses collapse or begin cutting stores from their estate. Lease lengths will likely shorten as tenants avoid signing longer-term deals amidst future (economic & market) uncertainty. While some retail assets will experience negative rental growth, others - notably supermarkets or retail parks anchored by supermarkets - will likely see positive rental growth.

Lastly, businesses that were ready to sign in Q1 have still put pen to paper. But most retail businesses have put any new projects on hold and are adopting a "wait and see" approach until market conditions become more favourable.

## SUMMARY

The results of the survey show that the retail market is suffering as the footfall and sales decrease can be observed in almost all segments. Even though some businesses already have e-commerce platforms and some have rushed to implement them in a short time frame, consumers are not as quick to adjust – in this case it is not only about adopting to restrictions and new sales channels, but also about the lost household income, decreased consumer confidence and non-existent demand for several goods categories. For several years, shopping centres have been implementing a lot of changes to become more service and entertainment-oriented centres where people spend a lot of time, however, now they are forced to switch away from this activity – it is currently unclear how this will affect buyer behaviour after the COVID-19 pandemic is over.

So far, no retail development plans have been postponed, however, it is going to be harder to attract new international tenants to Baltics.

Existing tenants are using government support and are expecting landlords to offer some incentives as well, while landlords currently have the least support available. In short term, we expect asking rent rates to slightly decrease, while vacancy is expected to increase due to some tenants being forced to cut their operations.

Overall, shopping centre cash flows will suffer, meaning that investors will be even less encouraged to look at this segment, while stores with daily needs retailers might still be a compelling choice.

** In Estonia and Latvia state of emergency was declared March 12th, in Lithuania on March 16th. In EE shopping centres (except grocery & pharmacies) have been temporarily closed since. Starting from March 24th shopping centres in LV have been closed on weekends except for grocery, pharmacy, DIY and veterinary stores. Gyms, casinos, cinemas, and other entertainment places are closed on all days. At the time of the survey, in LT only the essential grocery, pharmacy, optics and veterinary stores were open. As of 16th of April, restrictions have been eased to stores having a separate direct entrance from the outside, and to household and repair service providers.*

*** At the time of the survey, the government support was not confirmed. As of the 15th of April, the Lithuanian government announced initiative up to 50% rent subsidy for a landlord, provided the landlord provides not less than 30% discount for a tenant.*