



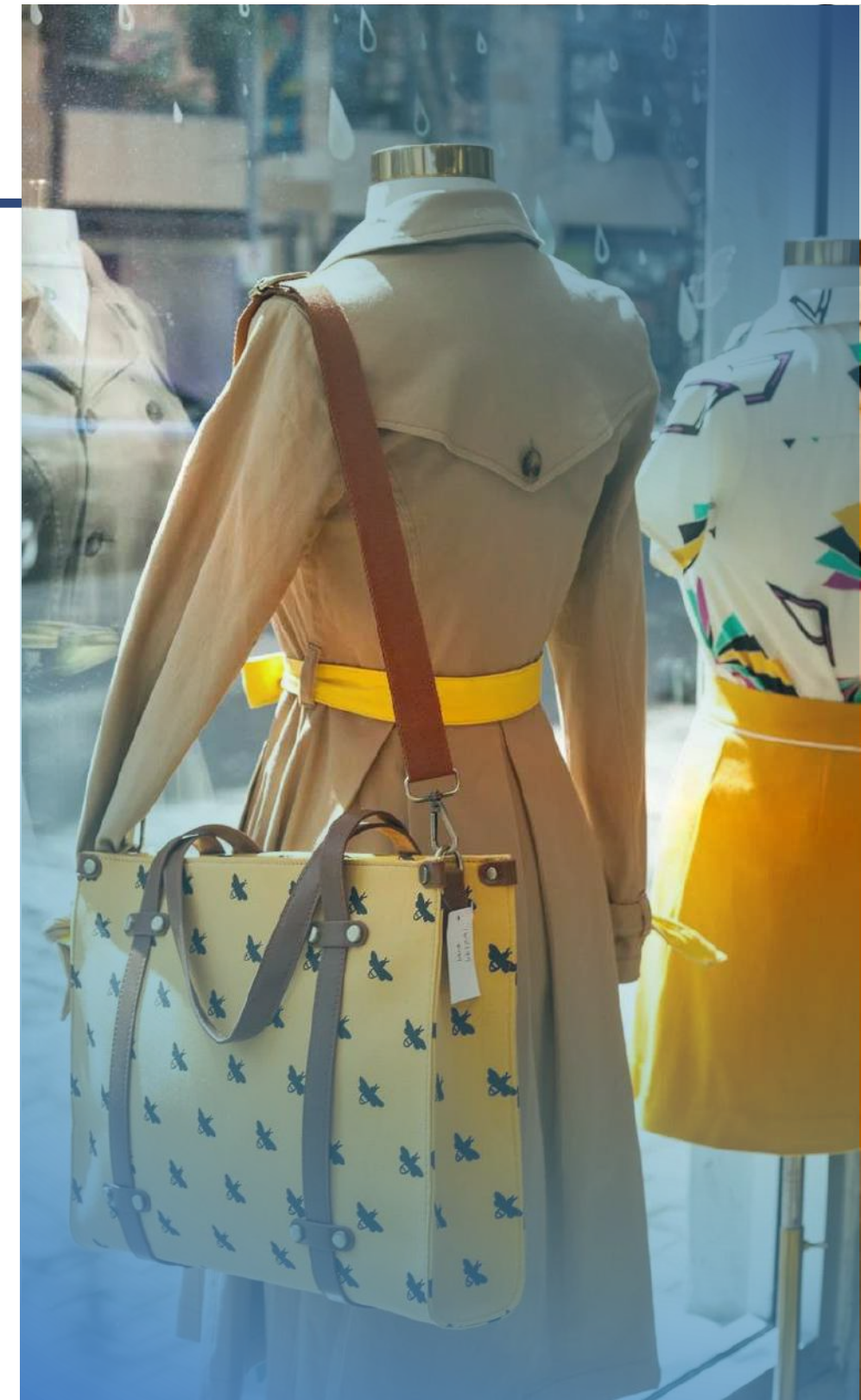
Turnover Leases... Getting to the Truth.

A survey of leading UK retail brands and F&B operators about their perceptions of turnover leases and how expert asset management and data can create a working partnership

1. TURNOVER LEASES...

WHERE ARE WE NOW?

- The pandemic and the disruption it has caused has highlighted the potential for turnover-based leases to bring a more responsive, flexible and partnership approach to the leasing of retail and F&B property.
- There has been a rapid adoption and implementation of a number of different types of turnover leases, often by investors and asset managers with little experience in this specialism.
- However, there are some misconceptions about what constitutes an appropriately constructed turnover lease – and also around the attitude of occupiers to them.
- This situation has not been helped by the portrayal of some of the lease structures proposed as part of recent CVAs as being 'turnover leases'. In reality, these rarely, if ever, are a long-term, sustainable solution for either landlord or occupier.
- To address these misconceptions Total Turnover Solutions canvassed views from some of the best-known retail brands and F&B operators seeking their thoughts and opinions about the most equitable turnover-based approach to leasing property.



2. THE SURVEY SAMPLE & KEY FINDINGS

- For the survey, Total Turnover Solutions spoke to a wide range of retail multiples and F&B operators.
- Together, these businesses occupy more than 11,000 stores across the UK and represent a compelling sample of occupier attitudes from very different types of consumer offers.

11,000+

The number of UK stores and outlets operated by survey group

31

Respondents from major retail multiples and F&B offers



Said they are in favour of moving to turnover-based leases



The level of positivity among respondents was illustrated by their collective enthusiasm to participate in research which would communicate the attitudes of many occupiers.

The findings of the survey are emphatic: 80% of those canvassed were in favour of a move to turnover-based leases, which are correctly operated and result in good partnerships.

Only 12% of the sample were undecided without further detail of the outlet based model about a turnover-based strategy but only **8%** deemed it to be not suitable for them because of uses of operational property which are particular to their businesses. In this category would be, for example, the use of property as banks or showrooms for product demonstration, where there is little or no revenue flowing through tills onsite.



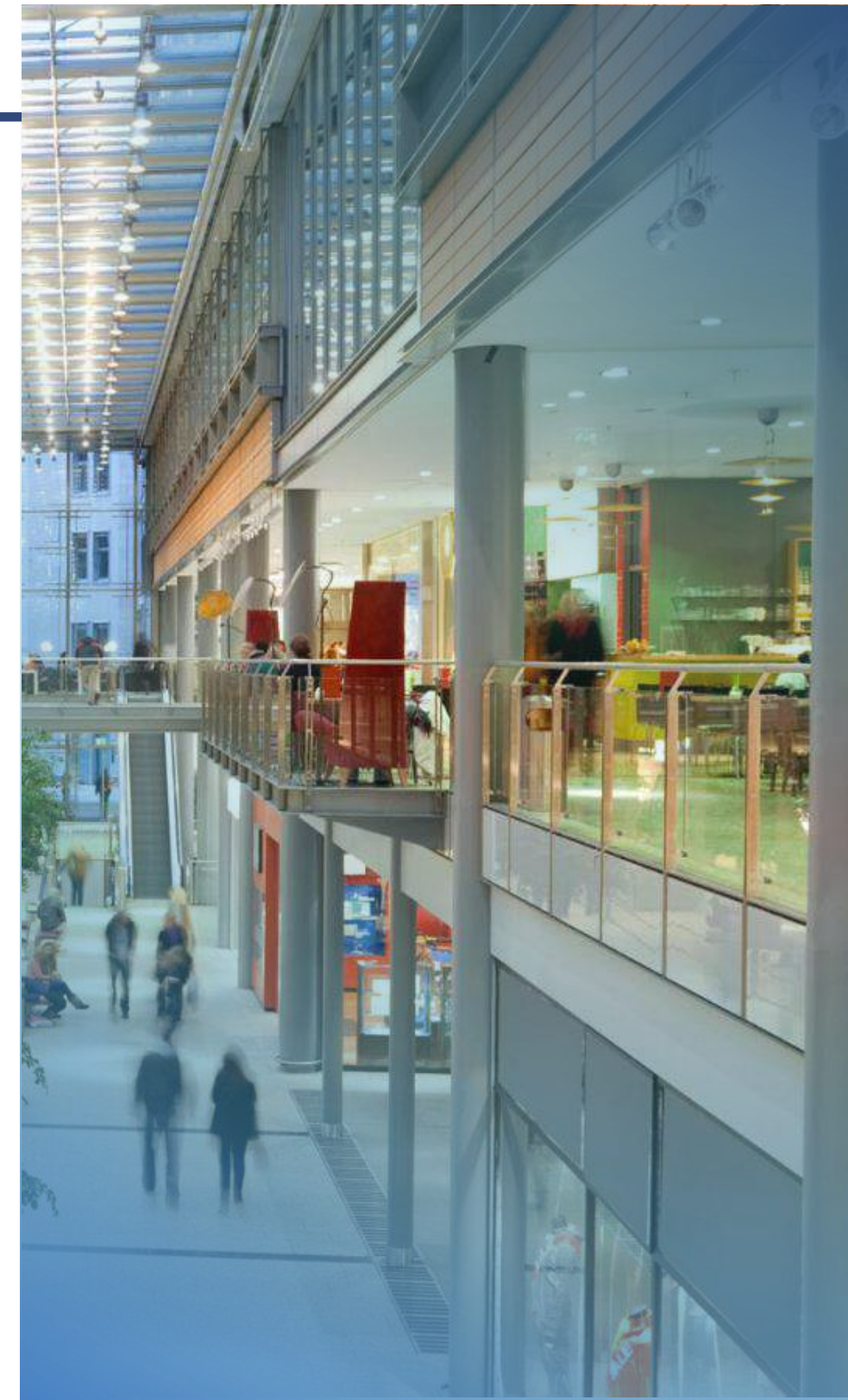
Only 8% of respondents said Turnover Rents were not suitable for their business, mainly due to showrooming where little or no revenue flows through tills on site.

Mark Phillipson of Total Turnover Solutions comments: “That such a large proportion of occupiers are entirely amenable to moving to a lease structure which **creates partnership** and **aligns their interests** with the landlord to **provide potential upside** is very positive news for investors.

“It is important that both sides acknowledge the need to negotiate an appropriate level of base rent, which will underpin the investment and funding criteria of a shopping centre.”

“These key characteristics of a turnover-based lease are an essential step towards creating assets which **provide sustainable income** and **can be accurately valued**, which in turn **create attractive investments**.”

“And, of course, a more flexible, ‘revenue responsive’ approach to property leasing also helps to de-risk lease liabilities for occupiers and is something which is likely to make them more likely to stay in occupation thereby minimising voids.”



3. WHAT THE RETAILERS SAID

A selection of comments from the research respondents:

“We feel the outlet model would work really well in shopping centres”

“Landlords need to thoroughly understand our businesses; the margins we need to achieve; and the ‘effort rate’ which is required to be profitable in any given location”

“Landlords must be set up with the right systems to collect the data etc so that it does not become a burden on us”

“No shopping centre lease will be signed off unless it is a turnover rent”

“We mainly have fixed rents at full price but may look to change going forward. We like the idea of working in partnership”



4. GETTING TO THE TRUTH.. IT'S ALL ABOUT THE OPERATION

Accessing accurate turnover data is key to structuring and sustaining a turnover-based approach to leasing. At present, some landlords obtain turnover data as part of the rent collection process but do not apply it in a way which could **enhance their income streams** and, in return, provide their occupiers with a **more flexible leasing platform**.

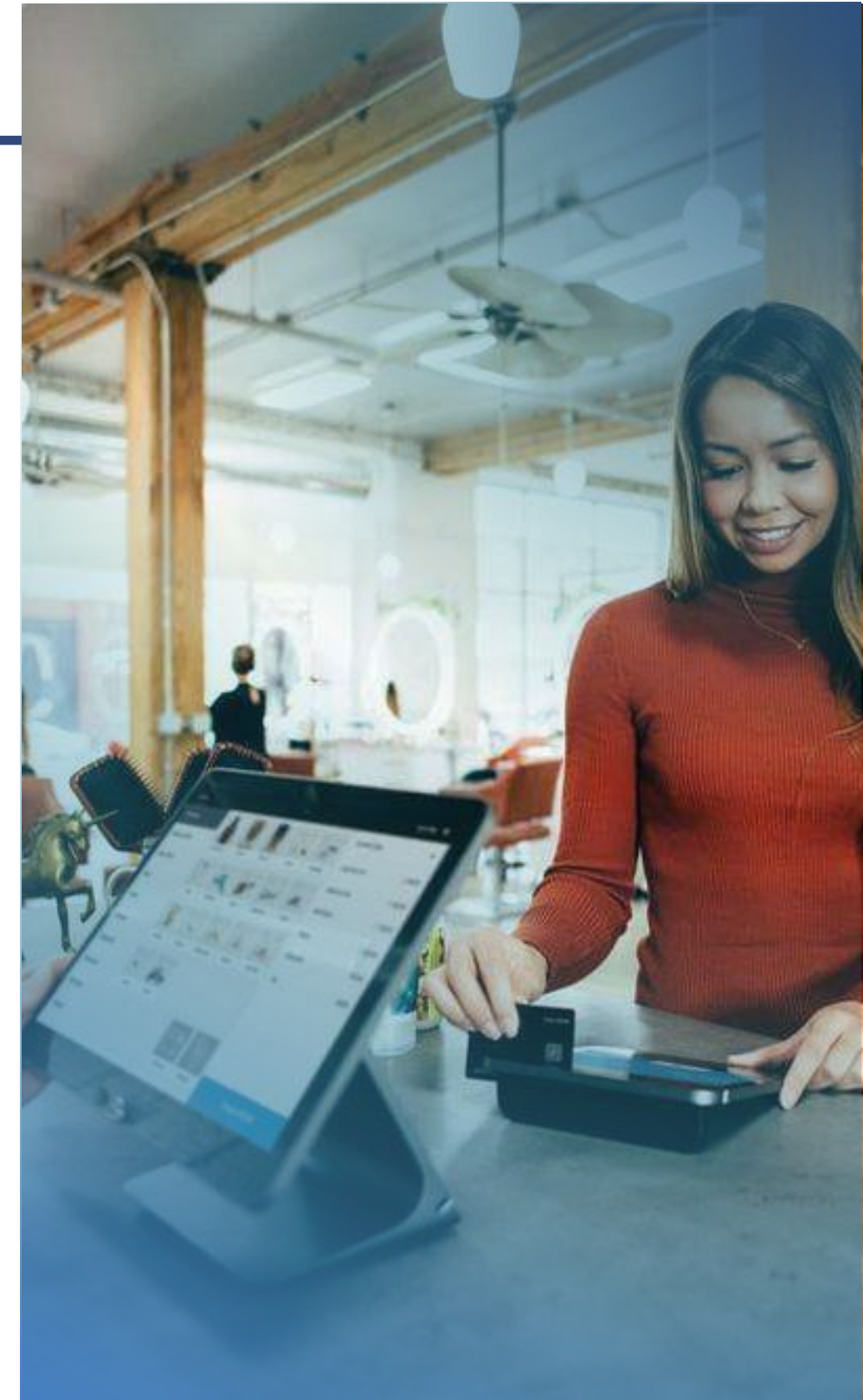
It was clear from the survey discussions that this cross-section retailers and F&B operators would be **overwhelmingly willing to supply turnover data** provided the process is **secure, easy to do** and **they can benefit from the aggregated data** perspectives about their locations and use that intelligence to inform their future trading projections and performance measurement.

On a very fundamental level, some landlords are concerned that occupiers may **misrepresent turnover** levels for their own advantage. In reality, the **perspective that TTS already has** on how **different occupiers trade** in different locations plus the fact that trading figures are invariably subject to independent auditing **means that there is virtually no scope for manipulating the figures** and any attempt to do so would soon be recognised.



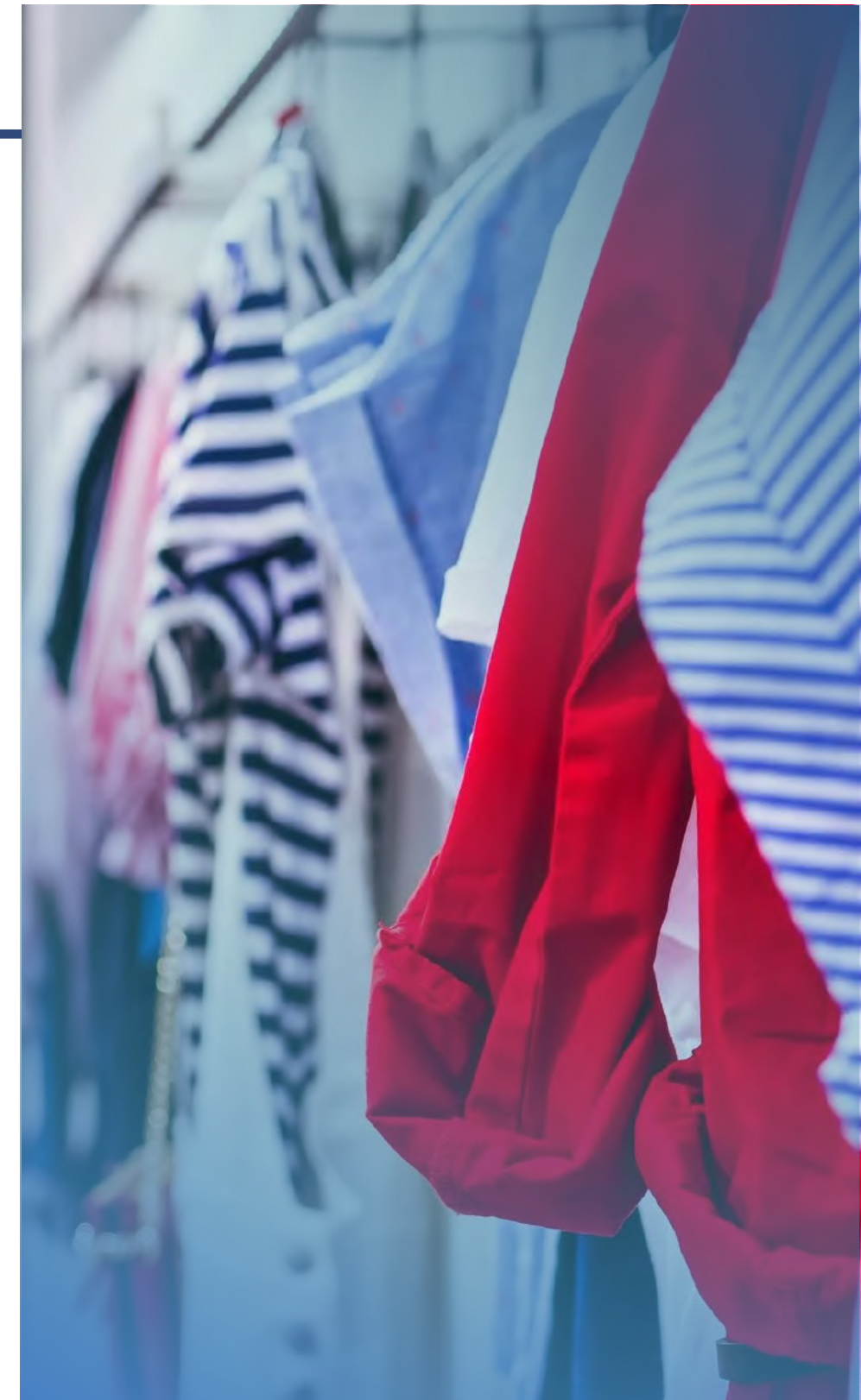
5. KEY LEARNINGS FROM THE RESEARCH:

- Looking at a monthly or quarterly turnover figure from one of your occupiers doesn't tell you much in isolation. It's only when you also know what happened last week, last month or last year that the true picture emerges. **You need a continual stream of comparative data.**
- You have to understand the differences between retailers and what their respective 'effort rates' are in terms of being profitable in a particular store or retail environment. **Each retailer is unique.**
- Data collection without interpretation is pretty futile. Measuring footfall in malls is of little value without understanding conversion rates within individual stores and their subsequent sales densities. **Your data needs specific and expert interpretation.**
- You need a data platform which is comprehensive, verifiable and can also factor in other variables such as the impact of events and marketing initiatives. The correct analysis of the data by experienced professionals will enable the optimum asset management and performance of a centre to be delivered. **Your data needs to be meaningfully extrapolated to be valuable.**
- Retailers have confirmed their performance is maximised when working in genuine partnership with an experienced asset manager that has a fundamental understanding of their businesses, someone who speaks their language and is resourced to drive their turnover. **You need a cohesive partnership.**
- Ultimately, anything short of the outlet methodology and operation will not deliver the returns expected by retailers and investors alike.



6. THE RIGHT LEASE

- Turnover leases require expert drafting that captures each nuance and detail of what encompasses the scope of partnership-based, revenue-responsive agreement.
- This can range from basic points such as accommodating the differing lengths of calendar months and turnover periods through to precisely agreeing what sources of revenue are included in overall turnover figures. For example, is it only what goes through the in-store tills or does turnover also encompass click-and-collect revenues?
- The successful model which has been developed and is readily accepted by occupiers in the outlet centre sector is mostly predicated on leases outside of the 1954 Landlord & Tenant Act. This approach mirrors Scotland where the Act does not apply, and yet has developed a mature and fully functioning leasing market.
- Today, the perceived 'safety net' of the 1954 Act is no longer as pertinent to the leasing process, or the creation of investable assets.
- **Dan Mason of Total Turnover Solutions comments:** "It is vitally important that turnover leases are drafted correctly by solicitors with the relevant experience".



7. MAKING TURNOVER OPERATIONS FIT FOR PURPOSE

- The vast majority of landlords – with the exception of those who have been active in the outlet centre sector for the past 20 years – do not have the data infrastructure or asset management expertise to accommodate a switch to truly proactive turnover-based leasing.
- To assist landlords' transition to turnover leases, we have:
 - data infrastructure
 - a detailed understanding of occupier performance
 - 20 years of proven turnover lease asset management expertise
 - investment perspective to enhance value
- **Dan Mason of Total Turnover Solutions comments:** “To implement a turnover-based approach to leasing requires creating an essential framework of having an agreement which is fit-for-purpose; a powerful data system which gives the necessary perspective; and experience what asset management initiatives enhance turnover. “
“Total Turnover Solutions offers a fast-track to landlords looking to get in-step with what is happening across the occupier markets. Agreement, analysis and asset management are what makes turnover leasing successful. It is also going to be central to creating investable assets retail and F&B assets with sustained income and the ability to change in response to the changed world in which we live.”



Total Turnover Solutions

Asset Management

To discuss the findings of this survey and the advantages of a turnover-based leasing strategy, please contact:



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TOTAL TURNOVER SOLUTIONS

Total Turnover Solutions is a specialist asset management consultancy focused on implementing revenue responsive management strategies within the UK retail property sector.

We utilise a platform which enables the collection, analysis and application of turnover data. This is integrated with our deep understanding of the retail, F&B and leisure sectors and enables the creation of effective and equitable turnover-based lease agreements which produce investable real estate assets.

For more information, please go to total-turnover.com