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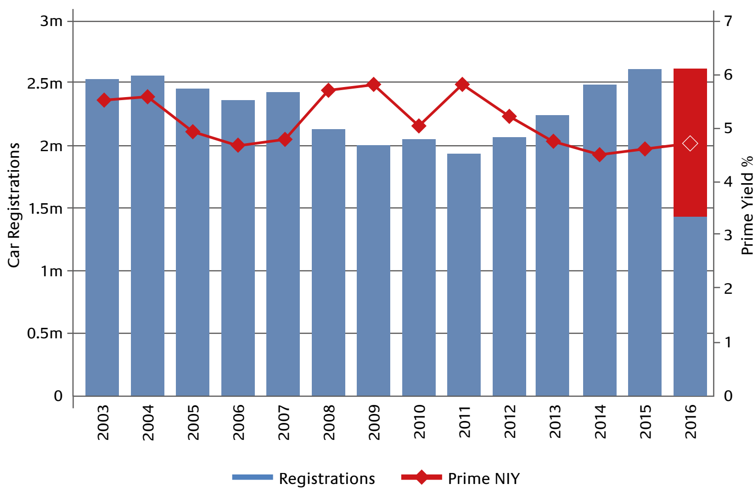
Motor Retail Property Bulletin – Summer 2016

Following a record year for vehicle registrations, the first six months of 2016 show an increase of 3.2% over the same period in 2015. However, the Brexit vote heralds a period of likely sales growth erosion with volumes for 2016 as a whole expected to be around the same level as 2015, and dropping in 2017. Compared to the 10 year trend there is not though expected to be any significant fall, and indeed this easing in sales push may well enable retailers to reinforce profit margins. All of the UK based car manufacturers together with European ones have pledged their commitment to the UK, Europe's second largest new car sales market. The UK car dealership market offers a wide range of income generating services extending well beyond new car sales, which typically represents 26% of a dealerships profit, and has the benefit of regional dispersal. With the prospect of quickening price inflation the motor retail sector offers a haven for investors with the predominance of long leases with inflation linked rent reviews let to strong covenants.

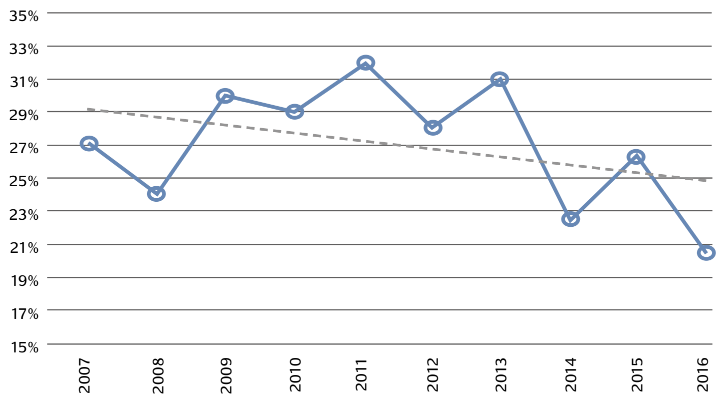
FIGURE 1: CAR REGISTRATIONS vs PRIME YIELDS



Occupier activity is resilient with a vacancy level of 3.5% and many new dealership developments coming on stream. The realignment of the Jaguar Land Rover network will continue to drive new dealership development and the search for larger sites in prime areas.

Parking remains a problem for many dealerships, exacerbated by manufacturers placing the imperative to store new cars on to the dealers themselves. Site densities have been trending down over the last decade (see Figure 2) and the last five years have seen the average fall from around 30% to 20% as dealers move to larger sites with extended car parking.

FIGURE 2: SITE DENSITIES



For many motor retailers, gross profit margins are under pressure leading to more market consolidation. This is evidenced by Mercedes-Benz Retail Group's sale of its entire Manchester and Birmingham regional market area businesses to the world's largest Mercedes retailer, Hong Kong-based Lei Shing Hong. Additionally, US dealer; Group 1 has acquired UK dealer group Spire Automotive. Spire has twelve sites operating primarily in Home Counties and North West London. Domestically, top five dealer group, Vertu Motors has acquired the family-owned Gordon Lamb Group with Toyota, Land Rover, Skoda and Nissan outlets in Chesterfield and a Skoda business in Derby.

Meanwhile, Marshall Motor Holdings has acquired the Berkshire based multi-franchise Ridgeway group. Ridgeway operates in the Southern Home Counties, representing twelve brands across thirty dealerships. Jardine Motors Group has acquired Birmingham based Colliers Motor Group. The acquisition includes the ownership of Colliers Group's Land Rover, Honda and Mazda dealerships located in Erdington as well as its Jaguar Tamworth site. Hendy Automotive have acquired South East based Lifestyle Motor Group placing the company in the top 25 dealer groups.

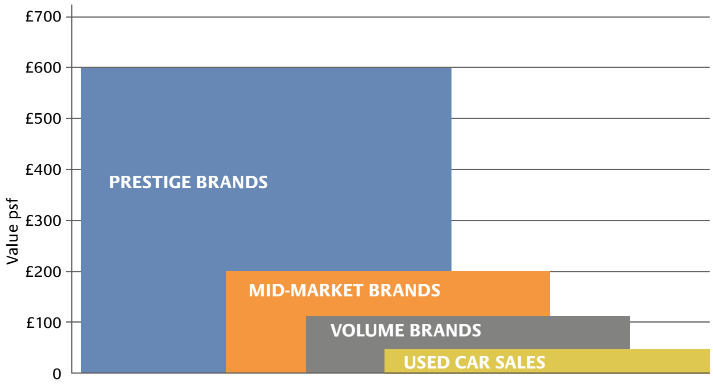
2016 Sold Averages	
Prime Yield	4.75%
Average Yield	5.75%
Average Rent psf	£14.21
Average Lot Size	£5.2m
Average CV psf	£239
Average Unexpired Lease Term	13.5 years
Average Floor Area	21,725 sq ft

Despite concerns raised by the Volkswagen emissions scandal and the unfolding Brexit story, demand for vehicles and allied services is expected to remain robust. Interestingly, sales of Alternatively Fuelled Vehicles increased by some 12.1% and this sector now has a market share over 3% compared with 1.3% five years ago. Although some commentators see market disruption in the growth of electric vehicles and autonomous technologies, Tesla provide a useful case study that shows a continuing demand for real estate assets.

As a manufacturer, Tesla has focused upon the prestige end of the market and is targeting sales of 80,000 in 2016 using its direct sales model – i.e. without full service dealerships. Nevertheless, Tesla currently has fourteen sales and service centres in the UK proving that electric or not, autonomous or not, demand for automotive real estate remains strong.

Used car sales are important to most dealerships but from a property perspective they sit at the bottom of the value hierarchy. Evidence from the market shows that prestige brands are paying as much as £600 per square foot for premises compared with the £200 per square foot paid by mid-market brands. This cascade of value sees sites sold for used car sales at circa £50 per square foot.

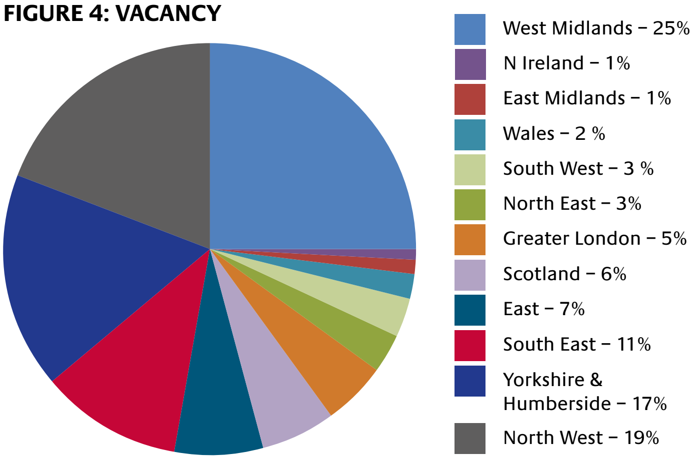
FIGURE 3:
CASCADING CAPITAL VALUES FROM PRESTIGE BRANDS TO USED CAR SALES



VACANCY, REQUIREMENTS & AVERAGE RENTS

As at the beginning of June, Automotive Property Consultancy are able to identify just over 1.5 million square feet of motor retail property on the market. Over 70% of this vacancy lies in the Midlands and North with the West Midlands region alone providing a quarter of the total.

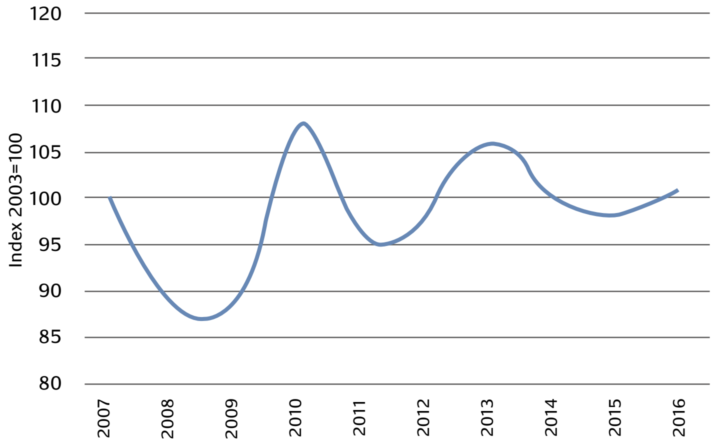
FIGURE 4: VACANCY



Requirements, by comparison are well down on the levels seen over the past two years. Geographically, half the current requirements have been targeting Greater London or the South East – the area that only represents 12% of the vacancy. Typically, the requirements are for between 1 and 4 acres of land with between 10,000 and 20,000 square feet of premises.

Based upon limited evidence, average rents in 2016 have begun to rise again following two years of relative decline. Figure 5 shows the volatility in average rents over the past decade. Whilst we anticipate some weakening in occupier demand pressure on space and shortages of land in key areas is still likely to combine to squeeze rents upwards supplemented by committed developments coming on stream.

FIGURE 5: AVERAGE RENTS



CONCLUSIONS

Physical presence on main roads remains the primary conduit to market. Modern technology has been embraced by motor retailers with parallel retailing directing customers to bricks and mortar sites. Cars cannot be serviced remotely, and customers still overwhelmingly want to see and test drive their vehicles before purchase. This feeds the widening sales and services options offered within car dealerships; evidenced by the typical 80% of new cars being sold with stapled finance, and significant headroom for used car sales to follow suit. The broadening current trend is towards bigger and fewer outlets, and this has created a more clearly segmented market than before, exacerbated by continuing market consolidation, establishing distinctive value bands. This places those controlling the best properties at the apex of the opportunity curve to secure the best franchises and generate the best returns.

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For more information please contact:
Automotive Property Consultancy Ltd
100 Pall Mall, St James, London SW1Y 5NQ
Tel: 0203 588 7200

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Bill Bexson BSc FRICS
Managing Director
RICS Registered Valuer
Investment, Agency, Development, Valuation, and Corporate Consultancy
Tel: 07831 827442
bbexson@automotive-property.com

Adam Shorey BSc (Hons) MRICS
Director
Professional, Agency and Asset Management
Tel: 07825 684706
ashorey@automotive-property.com

Kristina Simpson MSc MRICS
Associate Director
Agency, Development and Corporate Consultancy
Tel: 07585 705336
ksimpson@automotive-property.com