Retail landlords in clover as stores feel the pain

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AUSTRALIA'S largest listed landlords have all posted strong rental growth and profits this reporting season — in sharp contrast to the bleak outlook provided by national retailers.

Despite the good results, industry sources say weaker centres are cutting rents by up to 10 per cent and more retailers are delaying renewing leases at higher rents.

Westfield Group reported a 7.1 per cent lift in property income for the year to December 31 of $2 billion, while its offshoot, Westfield Retail Trust, chalked up total rental income of $1bn in that period.

Other landlords — CSF Retail; Charter Hall Retail; GPT Group; Mirvac Group and Stockland — have also collectively enjoyed solid and steady rental growth.

They have all reported almost full occupancy and have been successful in filling the vacancy left by retailers that went to the wall last year, such as the Red Group and Colorado.

The key to their optimism is the arrival of international retailers seeking a presence in Australia.

Retailers such as Apple Stores have emerged to fill the void. Apple opened its first store in Australia in 2008 and today has 13 around the country.

JPMorgan's head of research, Rob Stanton, wrote in a note on CFS Retail that its portfolio was 99.7 per cent occupied and it was writing new leases that included standard 5 per cent annual increases.

Mr Stanton wrote that there were no signs of cracks from the weak sales environment.

In a recent note, Simon Wheatley, executive director of Goldman Sachs Australia, predicted that "leasing spreads" would continue to weaken.

The leasing spread is the difference between the existing rent and new rent when leases are renewed. However, Mr Wheatley estimates the impact of a 1 per change in leasing spreads on trusts' earnings would only be 0.2 per cent.

Under this scenario, regardless of how bearish the retail leasing environment was, it was extremely unlikely that there would be negative net rental growth, he wrote.

The big question still remains: how much longer shopping centre owners can keep increasing rent when retail sales continue to be sluggish.

Andrew McLennan, retail analyst with Commonwealth Bank, said: "We are hearing mostly from unlisted retailers that they are negotiating for rent reductions of up to 10 per cent."

Mr McLennan said most of these struggling retailers were in the mass market, in the apparel and fashion business.

Following the slow Christmas sales, analysts expect more retailers to go into administration in coming months. Retailers such as Specialty Fashion Group, Myer and Solomon Lew's Premier Retail have said they will exit underperforming stores.

Russell Zimmerman, Australian Retailers Association executive director, said it was true that new retailers were filling space in major metropolitan centres.

But beyond that, landlords would find it difficult to charge the current level of rent.

"You will find that retailers will no longer be prepared to pay the current level of rents," he said.

"I've been told that a number of national retailers have triggered their 'hold-over' provision on old leases."

This meant they were not signing their new leases immediately.

Several retailers have put between 20-30 per cent of their leases in a holding pattern as they try to negotiate lower rents.

Some of these retailers operated between 200 and 400 stores across the country, he said. However, he added most of these stores were located in smaller centres, anchored by discount department stores.

Industry observers said the worst affected areas were in southeast Queensland, which had been hit by floods and a sharp drop in tourist arrivals.

In past three months, more retailers had run into problems and it was likely that, among them, they would vacate up to 500 stores in coming months, said Simon Fonteyn, managing director of online leasing data company Leasing Information Services. Mr Fonteyn said there was a flight to quality.

Centres such as Westfield Bondi Junction were "fortress centres" and would be insulated in the current environment.

An industry source said he knew of at least one major retailer that managed to negotiate a year's rent holiday, and another had a two-year rent-free period in a Brisbane centre.

Kos Sclavos, national president of the Pharmacy Guild of Australia, said its members were struggling under the multiple effects of changes in the government subsidies to its Pharmaceutical Benefits Scheme, penalty wages and high rentals.

He said a study had found that 10 per cent of the guild's 500 members were on their banks' watch lists, meaning they were in financial trouble. And a large proportion of these traded out of regional shopping centres.

BILL HEARNE

Westfield Group has reported a 7.1 per cent lift in property income