LBX Weekly Update #4: In The Pandemic Weeds With Tenants And Lenders

LBX investments

MARKET COMMENTARY

APRIL 13, 2020

Differences Rapidly Emerging Between Essential And Non-Essential Tenant Relief Requests

We Have Spent April Staying In Front Of Tenants And Negotiating With Lenders

Dear Investor,

We hope this message finds everyone healthy and safe. This week, we will discuss rent relief and lender forbearance – two topics that are inextricably linked in today's real estate climate. Additionally, we will provide a brief preview of next week's piece, which will explore how retail industry dynamics and customer behavior may change in the near-term as a result of the Coronavirus pandemic. Please see below:

Rent Collections and Lender Forbearances

- **Rent collection is still ongoing for April; as of today we are at 61% of collections, portfolio-wide**

Through Monday, April 13, we have received $1,006,136 of $1,648,587 in April billings (61.0% of total)*. Properties anchored by essential retailers (e.g., supermarkets, dollar stores and government tenants) have sharply outperformed centers anchored by non-essential retailers by a 24.2% margin (69.8% of collections vs. 45.6%). While additional rent checks are still trickling in, we do not expect many more collections to arrive for April. With funds still arriving, the collections process has taken much longer than usual this month, and several large "non-essential" national retailers are now taking aggressive stances against paying rent for April and beyond. See below for a breakdown of April rent collections across the portfolio, segmented by essential, non-essential, restaurant, and local ("mom-and-pop") tenants. To-date, we have received 90.9% of "Essential" collections from national and regional tenants, while we have received just 42.3% of collections from non-essential retailers and 29.3% of collections from restaurants.

Who's Essential? Breakdown of April Collections (Through April 13)

Tenant Categories	Count	Selected Tenant(s)	Billed	Collected	%
Regional and National Tenants					
Classified as "Essential"					
Supermarket	3	Publix, Food Lion, Lowe's	$149,278	$135,841	91.0%
Sporting Goods	3	Academy, Hibbett (2)	$73,324	$73,173	99.8%
Non-Retail Use	2	Sitel	$73,233	$73,233	100.0%
Financial	12	Amscot, H&R Block	$65,207	$53,840	82.6%
Liquor/Alcohol	1	Total Wines	$37,837	$37,837	100.0%
Dollar Store	2	Dollar Tree (2)	$25,906	$24,979	96.4%
Medical	5	Pearle Vision, Urgent Team	$25,664	$19,264	75.1%
Business Services	1	OfficeDepot	$22,228	$19,295	86.8%
Government	2	USPS	$12,649	$12,649	100.0%
Electronics	3	Verizon	$13,996	$12,050	86.1%
Health	3	GNC	$9,035	$0	0.0%
Subtotals	**37**		**$508,358**	**$462,161**	**90.9%**
Restaurants					
National Chains	12	Five Guys, Logan's	$59,552	$24,322	40.8%
Local Chains	25	Mom-and-Pops	$153,497	$38,104	24.8%
Subtotals	**37**		**$213,049**	**$62,426**	**29.3%**
Local Tenants (Ex-Restaurants)					
Local Retailers	69	Various Categories	$308,021	$219,443	71.2%
Subtotals	**69**		**$308,021**	**$219,443**	**71.2%**
Total LBX Portfolio	**182**		**$1,648,587**	**$1,006,136**	**61.0%**

Tenant Categories	Count	Selected Tenant(s)	Billed	Collected	%
Classified as "Non-Essential"					
Discounter	7	Ross, Five Below	$160,914	$111,262	69.1%
Department Store	3	JCPenney, Bed, Bath & Beyond	$97,039	$49,321	50.8%
Fitness	4	YouFit, Planet Fitness	$85,857	$0	0.0%
Books/Entertainment	3	Books-A-Million, 2nd & Charles	$32,539	$0	0.0%
Beauty Supply & Services	7	Sally Beauty, Great Clips	$26,292	$0	0.0%
Apparel	3	Clothes Mentor, Maurice's	$25,142	$5,387	21.4%
Furniture	2	RoomsToGo	$60,169	$60,169	100.0%
Specialty	5	David's Bridal, Kay Jewelers	$49,421	$1,376	2.8%
Pets	1	PetSmart	$24,767	$24,767	100.0%
Shoes	2	Foot Action, Shoe Show	$28,423	$0	0.0%
Home	1	Tile Shop	$25,162	$6,390	25.4%
Employment	1	Randstad	$3,435	$3,435	100.0%
Subtotals	**39**		**$619,159**	**$262,107**	**42.3%**

Source: LBX Investments

** Please note: Total billings were adjusted upwards by $6,400 in April due to a modeling error.*

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Rent Collections and Lender Forbearances (Continued)

- **We will offer 60-day rent deferrals to tenants who ask, though some national tenants are seeking special treatment**

Tenants have broadly fallen into four categories so far in their reaction to the pandemic:

a) They have paid their April rent with no relief requested,
b) They have paid their April rent but asked for some form of relief,
c) They did not pay their April rent and are requesting or demanding some sort of rent relief, or
d) They have not paid their April rent and are unresponsive to our outreach.

Below, we outline our response to each category:

1. **Paying Their Rent With No Relief Requested:** We are generally expecting a sharp decline in rental revenues for May but several of our retailers remain open. Unless they can demonstrate a significant negative impact on their business from the pandemic, we are not planning to offer them rent deferrals. In particular, retailers such as supermarkets and dollar stores are classed as "essential" and, in most cases, seeing sales increases. We do not believe they need rental assistance. We have been staying on top of store openings, closings and traffic, in part, to protect against tenants claiming hardship when they are open and thriving.

2. **Paid April Rent But Have Asked For Relief:** We are preparing to offer – **upon their request** – 60-day rent deferrals to most tenants. This cohort could potentially represent more than 75% of our retailers (by number of tenants). As noted in previous updates, we do require tenants requesting relief to provide financials and demonstrate they have applied for government assistance, but are planning to offer them lease amendments that cover base rent for April (retroactively) through May for some, and May through June for others. During the deferral period we will still ask tenants to pay their expense reimbursements, such as common area maintenance ("CAM"), taxes, and insurance. The deferred base rent will then either be a) tacked on to the end of their lease along with a minimum of one year of extra term (we are going to push for two or more) or b) amortized evenly over a 12-month period which will start in December, 2020. The 12-month period will not start immediately because we anticipate that retailers will need time to restart their businesses. The amendments will also contain caveats related to the pandemic; for example, if stores were to reopen before the expiration of the 60-day period they would need to start paying rent again within a couple weeks.

3. **Did Not Pay April Rent, Are Requesting/Demanding Relief:** Several larger tenants including Ross Dress For Less, Bed Bath & Beyond, David's Bridal, Five Below and 2nd & Charles/Books-A-Million have sent formal letters to landlords around the country stating their intent to temporarily cease rent payments. Here is sample text from one of these notices, for instance:

> "The Lease requires that we remain open for business and maintain certain operating hours more particularly described in the Lease. In accordance with the Lease, we are hereby declaring that the WHO's declaration of a pandemic, the President's declaration of a national emergency and the actions of the applicable state, county and/or municipal actions constitute events of force majeure, which excuses the performance of our obligations under the Lease including, without limitation, the obligations to pay rent. Further, the performance of our obligations under the Lease shall continue to be excused (i) for so long as the pandemic continues, (ii) for so long as the national emergency declared by the President, and/or (iii) for so long as the applicable state, county and/or municipal orders, rules, directives or other communications remain in effect."

Each national retailer that has sent us a communication like this has made a different request. Some have stated their intent to pay CAM and other reimbursements while they forgo rent, or pay a portion of rent. Some have postured aggressively, stating they do not intend to pay any rent or reimbursements for several months, or for an undefined period. Some have said nothing about payment and that they would reach out to discuss. **Regardless, these declarations all mean the same thing: rent payments from this group of retailers will be significantly reduced and/or delayed while we respond to them and then negotiate agreements on a case-by-case basis.**

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Rent Collections and Lender Forbearances (Continued)

These negotiations will be complicated, as national retailers have legal teams, financial resources that smaller tenants lack, and often, lease clauses and positioning within our centers that must be evaluated. We will certainly leverage our position wherever possible, however. In exchange for rent relief, we will seek to remove or tweak unfavorable clauses such as co-tenancy provisions or use restrictions that are commonly baked into leases with national retailers. In addition, we may use this opportunity to provide us with greater flexibility around any tenant across our portfolio that we view as suboptimal for our centers or the space they currently occupy.

4. **Have Not Paid April Rent And Are Unresponsive To Outreach:** This cohort represents slightly more than 5% of our portfolio (10 tenants). We have begun the process, of placing most of these in default with the intent to force a more productive discussion that will lead to either a lease amendment as noted above or removal from our centers if that is the optimal outcome.

- We are negotiating 90-day mortgage forbearances across the portfolio

Tenants and their rent payments represent the asset side of our business. Lenders and our mortgage payments represent our liabilities. We have (or will have) paid April mortgages in full by the end of this week (although the cash was available, we delayed payments in certain instances for negotiating purposes). Going forward, we are finalizing negotiations with lenders to fully defer mortgage payments for 90 days.

As a reminder to investors, we have employed moderate and flexible leverage across our portfolio in order to keep coverage ratios high and offer downside protection. We typically work with relationship lenders like banks and life insurance companies because we find these lenders are often significantly more flexible than their CMBS (commercial mortgage backed securities) counterparts and can – in troubled times – more easily customize their loans to the needs of the investment.

Thus far, negotiations have gone smoothly with our lenders. As we do with our tenants, lenders have asked us to provide real-time property information including revised budget estimates, updated financials, and specific information around rental collections and tenant operating status.

- **CMBS Loan (1):** We have one CMBS loan in our portfolio which is anchored by two essential retailers (a supermarket and a call center) and covered debt service by 1.9x in April (vs. 3.1x in March). We have no reason to approach the servicer for this asset at this time.

- **Bank and Insurance Loans (8):** We have provided requested information, held multiple discussions and are finalizing forbearance agreements at our remaining centers, with the exception of Chapel Hill (which we are in the process of refinancing).

Full details of loan forbearance agreements for specific properties will be provided to investors along with quarterly reports later this month.

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How Is Retail Responding To Coronavirus?

Last week, one of the national restaurant chains in our portfolio held a webinar for their landlords. They are still operating approximately 90% of their stores on a limited basis, but during March they went from 20% "off-premise" sales to 100% off-premise overnight, as their dining rooms were forced to be closed due to government restrictions. Per the call, half of their revenues evaporated immediately, they furloughed half their corporate staff, and their corporate focus immediately shifted to maintaining their solvency. They are now reaching out to landlords individually to work through their lease obligations, but this is not an isolated case. Many retailers are following a similar playbook globally: cutting costs aggressively, hoarding cash (and in some cases, raising cash through debt issuances), and fighting for survival. As new cases of Coronavirus start to level off and different markets begin to reopen, some semblance of normalcy will eventually return but as landlords, we are grappling with questions related to both retailer and shopping behavior because while some retailers may bounce back quickly, others are going to take time to recover, the shape of that recovery will be uncertain, and some will go out of business permanently. Questions we are assessing include the following:

- **When retailers reopen, what changes will they need to implement in order to incorporate social distancing into brick-and-mortar formats?**

Retailers will likely take time to get up and running while they figure out how to keep customers safe and limit their liability. Restaurants may need to separate tables by several feet, fitness chains may need to space out equipment and hire additional staff to sanitize machines after use, and movie theaters may need to figure out ways to accommodate crowds that are a fraction of their previous capacity.

- **How will retailers adjust their growth plans?**

On the call mentioned above, the retailer stated they do not believe it is in "anyone's interest to make long-term decisions" based on the "new normal." The extent to which retailers pull back on expansion plans, attempt to be opportunistic, or pull back on store refurbishments remains to be seen but thus far, most of the retailers we work with are taking a pause on growth while they focus on managing through this period.

- **Will China serve as a model for what to expect?**

On an industry update webinar last week with JLL, one of the largest commercial real estate service providers, China was offered up as a potential template for how a recovery might look. While China and the U.S. are very different, their hypothetical timeline below suggests more of a U-shaped than V-shaped recovery:

"Lessons From China" (How A Potential Retail Recovery Might Look)

Country	Mid-January – February	March 1 – 15	Week of March 15	Week of March 22	Week of April 15
China	"Lost Month"	Government "encourages" all tenants to reopen and most did	Sales at 30% - 40% of prior year	Sales at 45% - 50% of prior year Food and beverage at 60%	• Project sales back to 80% of prior year • Food & Beverage at 65% of projected sales
United States Corollary	U.S. contagion was several weeks behind China	China's March would equate to May in the U.S.		March 22nd would equate to June 1 in the U.S.	April would equate to July with a bowl-shaped recovery

Source: JLL

The main takeaway from this slide is that China is several weeks ahead of the United States because the Coronavirus peaked there earlier in January/February. Should we begin to see re-openings in May or June, it is not unreasonable to believe that sales will take time to rebound, even though cabin fever is understandable. As an example, JLL cited that Uniqlo, a prominent Japanese retailer, is seeing sales of approximately 70% of last year's totals. They pointed out how the world's perspective has changed, noting, "They are down 30% and they are heroes."

Coming Up

Next week, we will provide a portfolio update and begin to look towards May. We will also take a deeper dive into some of the ways we expect Coronavirus to impact the retail sector over the coming months. In the meantime, please feel free to contact us directly with any questions.

Sincerely,
Rob Levy, Phil Block and Heath Binder

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