# Big Shed Briefing

July 2016

Logic 233 in Dagenham where Savills, acting for Logicor, have leased 232,965 sq ft to Coca-Cola Enterprises

## SUMMARY

■ Demand in the logistics sector remains strong with 14.62m sq ft of warehouse space taken up in the first half of the year, which is ahead of the long term average of 11.3m sq ft.

■ Grade A and large unit supply continues to fall. Indeed, any occupier requiring a grade A unit over 400,000 sq ft only has one option, Quantum at Magna Park, which is not ready for occupation until the autumn.

■ In turn this is ensuring that occupiers have to turn to the build-to-suit (BTS) market to satisfy larger requirements. In 2016 so far 48% of the space transacted has been for bespoke BTS units.

■ The rate of speculative announcements has slowed in 2016 with just 11 recorded so far this year. We expect that the second half of 2016 will see few announcements detailing new speculative delivery as developers lease existing space and also await the impact of Brexit to become clear.

■ The investment market for logistics units continues to perform well. In the first half of 2016 £1.2bn of stock was transacted, which is £350m above the long term average. Investors are also increasingly comfortable with the shift towards online retail and the Amazon covenant as two of the three keenest yields paid this year have been for Amazon units.

"The supply of good quality large units remains at critically low levels, meaning that the increased prevalence of the build to suit segment within the market is here to stay for the foreseeable future" Kevin Mofid, Head of Industrial & Logistics Research

## Availability

■ The supply of existing units over 100,000 sq ft across the UK currently stands at 29m sq ft, across 170 separate units, which is a fall of 14% since the start of the year. Whilst total supply has fallen by 15% in 12 months the second quarter saw 35 units added to our supply figures. Of these 62% were second hand and the rest are completions of speculatively constructed units.

■ Even given the recent increases in speculative delivery, at a national level the market is still skewed towards poorer quality stock. Of the units currently on the market we classify 64% as grade B and C, and just 36% as grade A. Of the 10.5m sq ft classified as grade A 30 units, equating to 50%, are second hand.

■ Over recent years the availability of larger scale units (over 400,000 sq ft) has decreased with every quarter that passes. In 2014 supply of units over 400,000 sq ft was 4.7m ft across nine units. Currently, the supply is just 1.3m sq ft over three units, a fall of 72% in just two years. Indeed, any occupier requiring a grade A unit over 400,000 sq ft only has one option, Quantum at Magna Park, which is not ready for occupation until the autumn.

■ Regionally, the North West has the highest supply of stock at 5.5m sq ft. However, of the 33 units on the market 27 are between 100,000 & 200,000 sq ft, the most of any region. Of the core logistics regions the West Midlands has the lowest total supply at just 2.4m sq ft, giving just 0.6 years of supply compared to the national average of 1.3 years of supply.

## Take-up

■ At the half year point in 2016 take-up has reached 14.62m sq ft, across 60 separate transactions. This is just 150,000 sq ft down on 2015 but 3.4m sq ft above the long term average of 11.3m sq ft.

■ Whilst 2016 so far has seen strong levels of take-up for units over 500,000 sq ft (five this year in total, compared to a yearly average of seven), there has also been strong churn in the smaller size ranges with 80% of transactions, by deal count, between 100,000 and 300,000 sq ft.

■ The aforementioned lack of supply of units over 400,000 sq ft has also increased the prevalence of the build-to-suit (BTS) market in 2016. By size, 48% of the market so far this year has been for BTS units with budget grocer Lidl being particularly active completing, in the second quarter, on two deals totaling 1m sq ft at Central Park, Bristol and iPort, Doncaster.

■ Regionally, the take-up picture is varied, with a number of anomalous data points being recorded. Firstly, for the year to date 3.6m sq ft of space has been leased in the South West, which is 2.1m sq ft more than the annual average. Whereas the South East has recovered in the second quarter with 1.3m sq ft of deals compared to a record low first quarter when just 262,000 sq ft was taken.

■ Examining demand by occupier type demonstrates the clear increase in take-up from online retailers and parcel delivery companies, which account for 25% of the market in 2016, up from the previous record of 17% in 2015.

## Development Pipeline

■ Analysing our development pipeline database we are tracking 32 schemes, totaling 5.9 m sq ft, that are due for delivery in the remainder of 2016 and into 2017.

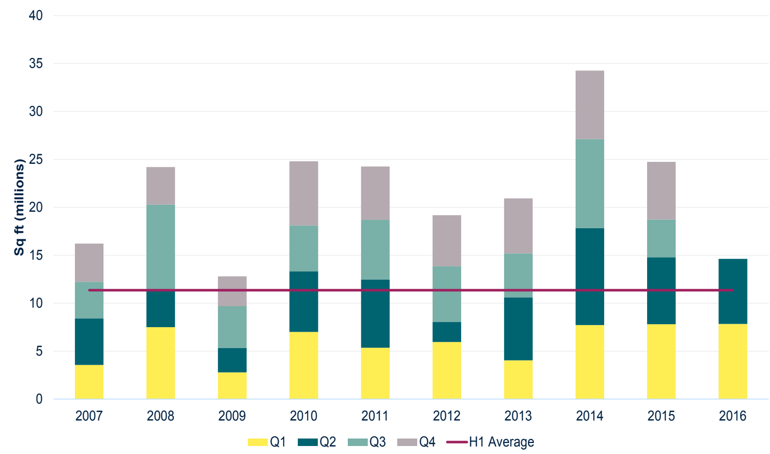
■ The rate of speculative announcements has slowed in 2016, with 11 units over 100,000 sq ft announced to date, compared to 47 in 2015.

■ Of the units under construction and due to reach practical completion the largest is 360 Logistics North, Bolton which totals 357,700 sq ft and will be available in Q3 2016. Of the remaining units due for delivery in 2016/17 72% are between 100,000 & 200,000 sq ft and the average size unit is 185,301 sq ft.

■ Regionally, the North West has the most space due for delivery across 11 units, which total 2.2m sq ft. Following the practical completion of the IP2 A & B buildings at iPort in Doncaster (and subsequent letting of IP2 B to Fellowes Distribution) Yorkshire now has no units under construction speculatively.

GRAPH 1

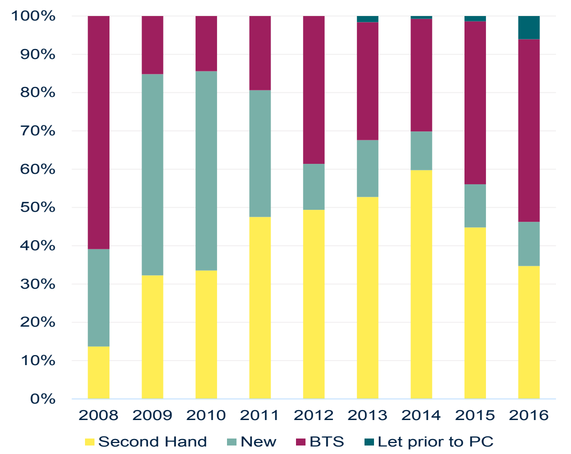
### First half take-up above average




Graph source: Savills

GRAPH 2

### BTS increases in prevalence




Graph source: Savills

## Investment

■ Given that the referendum on the UK's membership of the EU came at the end of the second quarter, a slowdown in the second quarter was anticipated and perhaps inevitable.

■ However, the drop in volumes has not been as severe as initially suspected with the second quarter seeing £526m transacted giving a first half of the year investment volume of £1.2bn, which compares favorably with the long term average of £850m for the same period.

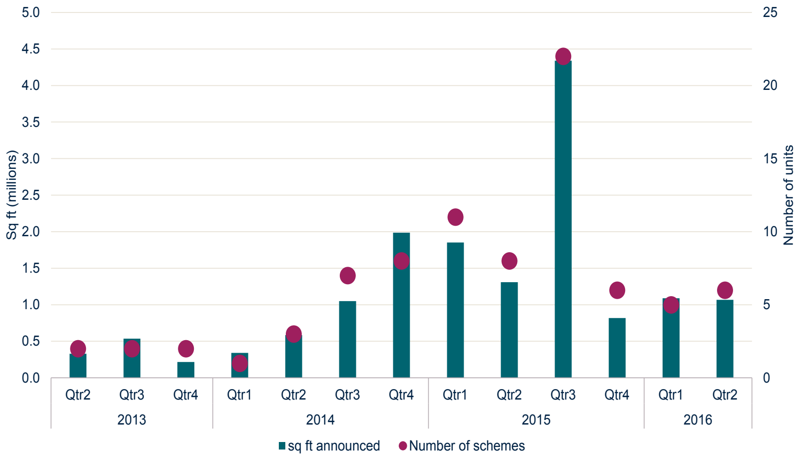
■ Key to this has been the increased prevalence of overseas investors in the market combining with the increased levels of take-up from online retailer Amazon creating a supply of prime investment stock. Indeed the second quarter saw two of the three keenest net initial yields paid this year, both for Amazon units, 4.5% at Bardon and 4.66% at Airport City, Manchester, and both to overseas investors: A private Korean investor for Bardon and HansaInvest for Manchester

■ Acting for the vendor Savills also advised on one of the largest deals of the quarter as Tritax Big Box REIT continued to build their portfolio with the purchase of the DSG unit in Newark for £77.3m, reflecting a net initial yield of 5.76%.

■ The Savills prime yield for distribution warehouses remains at 4.75% having moved out 25bps in 2016 so far. As further transactional evidence appears following the results of the EU referendum we expect some upward pressure to be applied to this.

GRAPH 3

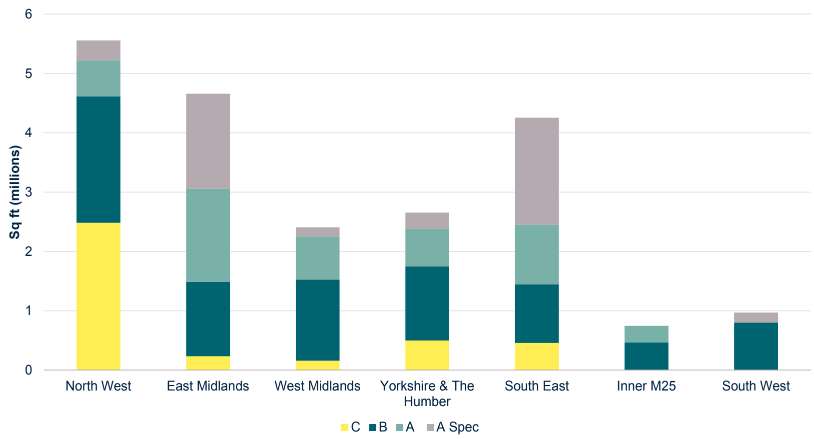
### Speculative announcements slow




Graph source: Savills

GRAPH 4

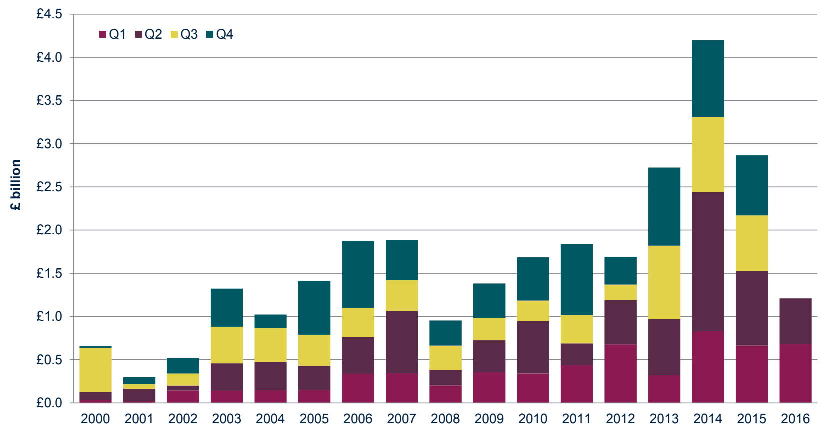
### Current supply by region and grade




Graph source: Savills

GRAPH 5

### Distribution warehouse investment volumes




Graph source: Savills/ Property Data

# OUTLOOK

## Constrained development pipeline will assist in keeping vacancy rates low....

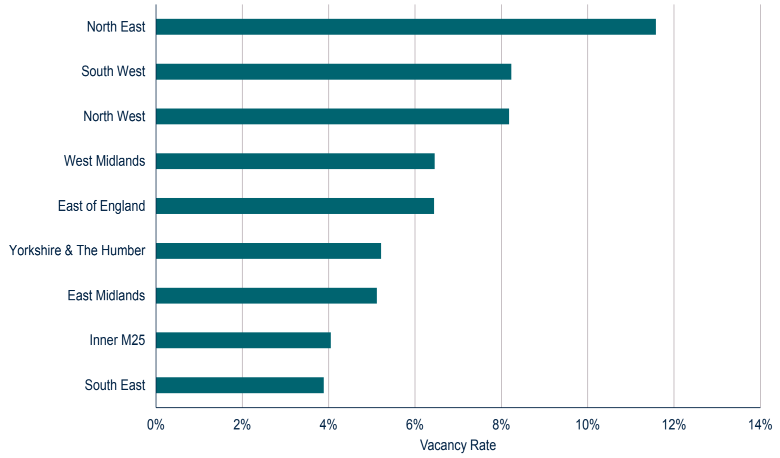
■ Savills has produced a stand alone research paper covering the potential impacts of the result of the referendum to leave the EU. This will be updated, on our website, over the summer months as further information and data becomes available.

■ However, our key initial observations are that the market is in a fundamentally different place to where we were in 2008/9 when almost 100m sq ft of space was actively being marketed. Even accounting for the development pipeline, current supply remains at historic lows and take-up levels remain robust.

■ We envisage that speculative announcements will slow in the second half of 2016, however we do not anticipate take-up levels to decrease. Indeed there are many large unsatisfied requirements, including Lidl in the North West who require 40 acres, Makita and Decathlon in The Midlands who require over 500,000 sq ft and Amazon who continue their roll out of their Prime Now and Fresh service.

GRAPH 6

### Regional vacancy rates




Graph source: Savills/UKWA

### Key Occupier Data

**Current Grade A / new supply (over 100,000 sq ft):**
5.9m sq ft, down 8% year/year

**Average annual take-up:**
22.4m sq ft

**2016/17 speculative development completions:**
7.1m sq ft (32 schemes)

**UK Vacancy rate:** 7.1%

### Key Requirements

| Occupier | Region | Size |
|---|---|---|
| Lidl | North West | 30-40 Acres |
| Wayfair | North West | 300-400,000 sq ft |
| Makita | Midlands/SE | 600,000 sq ft |
| 3PL | North London | 500,000 sq ft |
| Matches/ XPO | South East | 200,000 sq ft |

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