

### Prime property yields have “topped out”

#### Prime yield compression continues

- Sentiment in the investment markets has improved significantly in the last two months with the majority of yields hardening, some by over 50 basis points since the turn of the year. As the overall market absorbs this trend, confidence will return and entice investors off the sidelines and back into the market.
- The investment news flow is improving as other market commentators are now reporting evidence of a small degree of yield compression; which has been evident to Savills since the first quarter for some sectors.
- As with the early-1990s recession, negative rental growth will lag capital value growth. However, well-let investments, with secure income, will remain on the ‘buy list’ of investors.
- The prime market represents a relatively small proportion of the market so sourcing product will remain the challenge in the coming quarters.
- The ‘gap’ between the cost of borrowing and yields is still wide, by historic standards. However, this gap is closing as Swap rate yields rise and all property yields decline. As it will emerge over the next year, the optimal time to buy may have passed, but there are certain opportunities to post superior returns when the stock becomes available.

#### Declining rate of capital value falls

- Compared to the early-1990s, the IPD ‘all property’ capital value index has been falling, at a faster rate, for nearly two years. It is currently down 44% from the market peak in July 2007.
- However, there is firm evidence that capital value falls in some sectors are beginning to recede.
- The outward movement of the ‘all property’ equivalent yield has started to slow. Indeed, the ‘all retail’ equivalent yield has shown a 25 basis point fall in the past month.
- From the peak in 1989, it took between 3 to 4 years before the capital value index presented positive monthly growth. We are now 2 years past the last peak and capital values appear to be close to bottoming out.

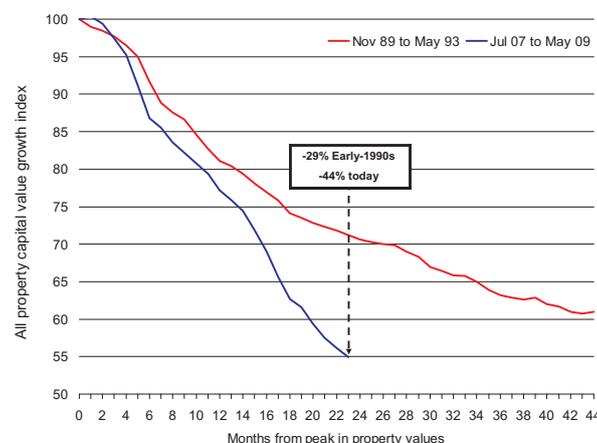
#### Prime equivalent yields

	Apr-09	May-09	Jun-09
West End Offices	6.0%	6.0%	5.75%
City Offices	6.5%	6.5%	6.5%
Offices M25	7.5%+	7.5%	7.5%
Provincial Offices	7.0%	7.0%	7.0%
High Street Retail	6.5%	6.0%	6.0%
Shopping Centres	7.0%+	7.0%	7.0%
Retail Warehouse (open A1)	7.0%	6.75%	6.5%
Retail Warehouse Park (restricted)	8.5%	8.25%	8.0%
Retail Warehouse (stand alone)	8.25%	8.0%	7.75%
Industrial Distribution	7.5%	7.5%	7.5%
Industrial Multi-lets	8.25%	8.25%	8.0%
Leisure Parks	8.5%	8.75%	8.75%
Regional Hotels	7.25%	7.25%	7.25%

Source: Savills

Note: In some sectors initial yield pricing is becoming more relevant than equivalent yields. This particularly applies to retail warehousing and hotels where the figures indicated above are net initial yields. The +/- against the figures in the table above reflects the expected direction of movement in yields over the next 3 months.

#### The average market rate of decline is slowing



Source: IPD

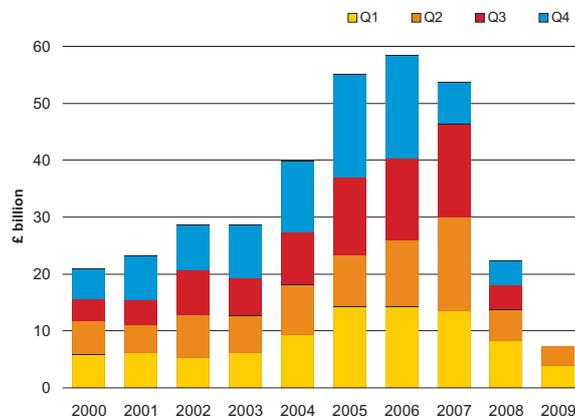
Note: Index adjusted for inflation

# Market in Minutes

## UK transactional levels remain low

- Based upon the preliminary mid-year data for the UK, investment levels over the first half of 2009 were 13% lower than the second half of 2008. Total transactions in the first six months of this year were approximately half the amount seen during the same period last year.
- This shows that the level of investment transactions remain muted, but the buy signals in the market suggest that Q3 will improve markedly if suitable stock is brought to the market.
- The latest Credit Conditions Survey (for Q2 2009) from the Bank of England reports that the commercial property sector continues to experience a reduction in credit availability.

## Q3 is expected to show higher investment levels

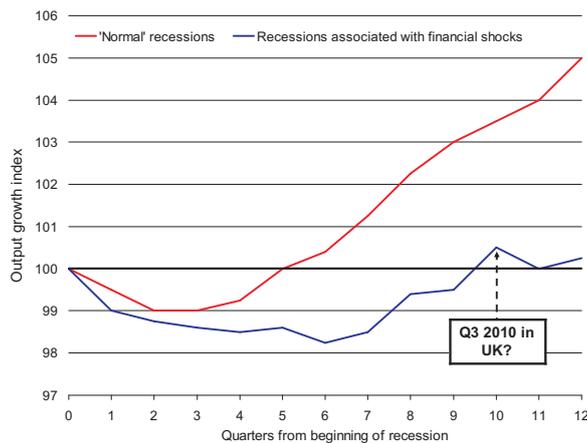


Source: Property Data

## UK economy remains poised for recovery

- The decline in GDP growth, during the first quarter in the UK, was the worst for fifty years. However, more positive signs are emerging.
- The latest consensus of economists for 2009 UK GDP growth showed a slight improvement from -3.8% to -3.7%. More positively, the expectation for 2010 moved much higher from 0.3% last month to 0.7% currently.
- The Organisation for Economic Co-operation and Development (OECD) says the world economy is near the bottom of the worst recession in post-war history. The OECD adds that recovery is likely to be "weak and fragile" for some time. International Monetary Fund (IMF) research suggests that recessions associated with financial shocks last longer than "normal" recessions.
- The Governor of the Bank of England has recently acknowledged that the UK may be over the worst, but stresses that challenges remain.

## Recessions led by a financial shock last longer



Source: IMF

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### Savills plc

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