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**Savills World Research**
UK Commercial

# Spotlight
# **Birmingham Offices**

June 2014


5 St Philips Place, Birmingham, which is currently being sold by Climate Change Capital for around £38m (5.85 NIY). When traded in 2007 it set a record yield of 4.3%.

- After several challenging years, we are now at a turning point in the Birmingham office market and believe we will see a gradual improvement in take up throughout the year.
- Take-up at the end of 2013 reached 483,832 sq ft (654, 313 sq ft in the wider market) with 69% being in the prime core.
- We expect 2014 to end the year at 550,000 sq ft. 13% up on 2013 and 16% above the long time average.
- A real supply squeeze is being witnessed in the prime core, where Grade A supply has fallen by 26% over the last 12 months.
- The city has started to respond to changing market demands and is at varying stages of seeking to attract office development back into the city.
- Birmingham prime yields are now estimated to be in the region of 5.5% (moving in 75bp since March 2013)

"We expect rents to return to 2007 levels by 2017, with rents hitting £30 per sq ft by 2015"
Nick Williams, Director, Office Agency, Birmingham

## Occupational Market

■ Despite a challenging few years, we are of the belief that the Birmingham office market is now at a turning point, with the City being well placed to take advantage of the predicted improvement in the occupational market.

■ Take-up at the end of 2013 reached 483,832 sq ft (654, 313 sq ft in the wider market) with 69% being in the prime core. Demand has been concentrated on prime, good quality accommodation and this stock has continued to diminish.

■ Take up in the first quarter of 2014 was somewhat subdued when contrasted against 2013, however current enquiries indicate a strong second half of the year.

■ The largest office letting so far this year has been to law firm Weightmans, who have taken 14,682 sq ft at St Philips Point.

■ As Grade A stock diminishes and occupier confidence increases in line with general market improvements, the demand for modern efficient floor plates will increase. Moreover, with employment growth signaling a renewed optimism for office based sectors, as well as an increase in the number of relocations of large occupiers from London to more affordable locations, take-up is expected to increase over the next couple of years

■ We expect 2014 to end the year at 550,000 sq ft. 13% up on 2013 and 16% above the long time average.

■ The City has seen a 15% supply fall over the last 12 months across all grades, with an 8% fall in the last quarter. However, the real supply squeeze is being witnessed in the prime core, where Grade A supply has fallen by 26% over the last 12 months.

■ Looking forward through the rest of 2014, with a number of companies now less austerity driven, we predict a significant increase in Grade A activity during the year.

■ A element of ongoing demand will inevitably be a catalyst for pre-let activity, as sustainable take-up levels limit larger Grade A options.

■ From a supply perspective, the continuing erosion of Grade A stock across the city is now likely to trigger enquiries from a number of occupiers, with the fear of missing out on key opportunities a likely catalyst to move.

■ As a result, given the renewed demand in the regions, against the improving economic conditions, there are great opportunities ahead for those investors and developers with well located sites. Indeed, the growing confidence in regional office markets, with increasing demand and limited supply, is a reason for developers to act sooner rather than later.

■ The City has started to respond to these changing market demands and is at varying stages of seeking to attract office development back into the city. There is now an expectation that at least one scheme will start on site within the next 6 - 12 months.

■ Schemes capable of early delivery are well placed to take advantage of pre let opportunities and predicted rental growth. Applications for LIF to deliver advance public realm could further help position such schemes more strongly to occupiers.

■ Although availability of funding remains an issue for speculative development, attitudes to funding part pre-lets in the regions has now fully recovered.

■ The percentage needed has also decreased over the last few years. Schemes such as 1 Grand Central, which Savills are currently going to market with, could now be triggered by a 30% pre-let compared to 60% +12 months ago.

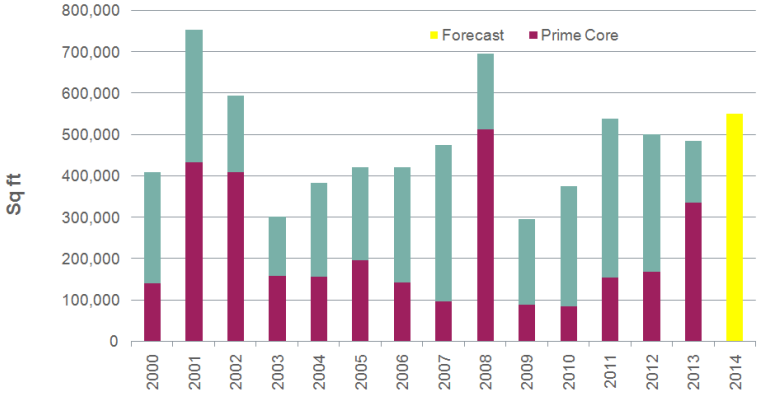
■ We also envisage seeing a continued steady rise in refurbishment activity in the Birmingham market as we go through 2014, typified by options such as Mailbox where Brockton Capital are refurbishing approximately 50,000 sq ft of space.

■ Predicted rental growth is a important factor in ensuring more comprehensive refurbishments are viable. Early growth prospects will facilitate far more ambitious strategies and inherently the provision of improved stock within the City's core market. The more aggressive approach is likely to reap rewards particularly where delivered in the clear window between the next phase of new build.

■ The trend for conversion to student housing is expected to continue in the short term and we also envisage seeing a steady rise of commercial to residential conversions as we go through 2014. This may be a quicker

GRAPH 1

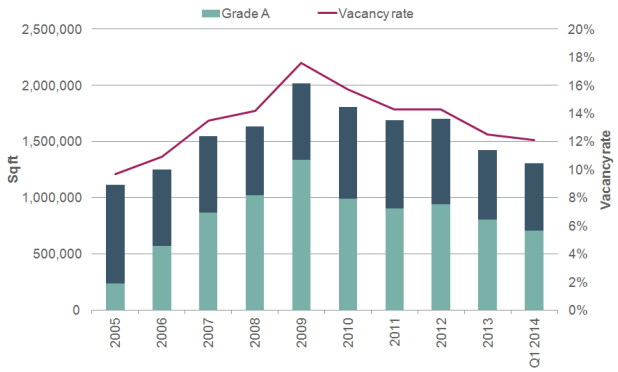
### Take-up is expected to pick up as we go through 2014




Graph source: Savills Research

GRAPH 2

### Availability continues to decrease, especially on Grade A space




Graph source: Savills Research

way of bringing down the second-hand space in the market.

■ Whilst it is fair to say that Birmingham still looks like good 'value for money', as the economic recovery really starts to take shape, we will start to see rental growth on prime space as we go through 2014 and beyond.

■ 3.3% growth per annum is expected over the next five years, with a return to rental growth from the end of the year onwards. Rents are expected to return to 2007 levels by 2017 ( £32.50 ), with rents hitting £30 per sq ft by the end of 2015.

■ Generally we anticipate a more robust Landlord approach to wider lease terms including term certain and available level of incentives.

## Investment Market

■ Investors started to look more closely at Birmingham during the latter half of 2013, driven by the expectation of an imminent rental recovery, and the wide yield gap between London and the regions. This has fuelled investor interest and subsequent pricing, which we expect to continue through 2014. Birmingham prime yields are now estimated to be in the region of 5.5% (moving in 75bp since March 2013).

■ While transactional volumes appear to be up, there is a limited amount of stock on the market, with investors struggling to find strong enough reasons to exit their investments, coupled with their concerns over being able to reinvest.

■ Although the occupational market out of town has yet to pick up, investors have started investing heavily in this sub sector, principally due to weight of money seeking higher returns and due to its relative value against prime in town office yields.

## Outlook

■ From the end of 2013 to the end of 2021, the expectation is for 13% rise in GDP output, which will have a significant impact on the demand for skilled labour and property in Birmingham.

■ According to the latest data, growth has returned to the West Midlands labour market. Birmingham's office based employment grew by 3% in 2013, and after that will grow by an average of 2.3% per annum over the next five years.

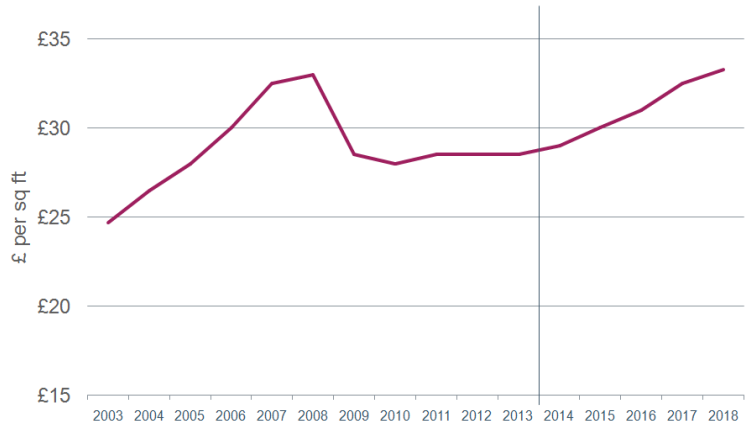
■ This implies a net increase of 9,600 office-based workers, which in turn will drive a steady level of demand for office space in the city.

■ The fastest growing sectors will all be predominantly office-based, with the Professional, Real-estate and TMT sectors all forecast to see jobs growth of more than 1.5% per annum.

■ This will translate into a steady recovery in take-up to above average annual levels over the period 2014-2017 (though Grade A take-up could be held back by lack of new stock in 2015/16).

GRAPH 3

### Top rents are expected to hit £30 per sq ft by 2015




Graph source: Savills Research

TABLE 1

### Recent Birmingham investment deals

| Address | |
|---|---|
| 5 St Philips Place | The building totals approximately 80,331 sq ft, with a passing rent of £2,285,358 per annum.<br><br>The offices are let to First Secretary of State equating to 76% of the total income. The ground floor retail is let to Sainsbury's, Bank of Scotland Plc and most recently Pret a Manger.<br><br>The building is currently under offer at circa £38m (5.85%) |
| Priory & Temple Court, Bull Street | The 247,337 sq ft site includes a retail parade of nine units totaling 6,194 sq ft and an 11,000 sq ft pub, with the remainder being office space let to 13 different tenants.<br><br>It has a total annual rent of £7.7m.<br>They have an overall average weighted unexpired lease term of more than 11 years.<br>Sold to L&G for £87.5m (8.28%) |
| 55 Colmore Row | The building comprises approximately 150,000 sq ft over lower ground, ground and three upper floors.<br><br>The building was redeveloped in 1992 behind the traditional facade and is let to Wragge & Co until 2017 at a passing rent of 3.3m.<br><br>The property has recently been acquired by IM Properties for £3.5m, which equates to a NIY of approximately 9.25%. |
| M&B Head-quarters, 27 Fleet Street, | Constructed in 2003 to provide 94,630 sq ft of Grade A office accommodation and a 120 bed Hotel.<br><br>30 years unexpired to M&B with RPI reviews (2.5% to 5% collar & cap).<br><br>Sold to LaSalle for £51m (5.34%) |

# Headline stats, definitions and contacts

| Headline statistics | Take-up: Total | Take-up: Prime CBD | Top rents (£ per sq ft) | Prime yield |
|---|---|---|---|---|
| **Full year 2013** | 654,313 sq ft | 483,832 sq ft | £28.50 | 6.25% |
| **Q1 2014** | 102,353 sq ft | 47,081 sq ft | £28.50 | 5.5% |
| **End of year outlook** | ↑ | ↑ | ↑ | → |

## Definitions & statistical notes

| | |
|---|---|
| **Property criteria** | Transactions and supply recorded for units in excess of 3,000 sq ft |
| **Prime Core** | Transactions and supply recorded for prime units in excess of 3,000 sq ft in the city centre and Brindleyplace |
| **Top rent** | Highest rent achieved in one or more transactions in the given period |
| **Grade A** | All new development (including speculative schemes reaching practical completion within six months, plus major refurbishments) |
| **Grade B** | Space previously occupied, completed or refurbished in the last 10 years |
| **Grade C** | Space previously occupied, completed or refurbishment more than 10 years ago |

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