Birmingham Office Market Overview

Winter 2010

With a muted development pipeline, supply will continue to fall in 2011.

One Snow Hill, Birmingham

- Figures recorded to date show 278,035 sq ft of space let in the prime core, which is 18% up on the same time last year. End year figures are anticipated to reach in the region of 350,000 sq ft.
- Take-up will improve as the economy enters a firm recovery in 2011, which, combined with the lack of development completions, will lead to sharp fall in Grade A vacancy rates and upward growth in net-effective rents from next year.
- We are forecasting rental growth over the next few years with the potential for strong growth driven by lack of Grade A supply and increasing demand in 2012.
- Focusing on the supply side, encouragingly, the development pipeline peaked in 2009 and this has resulted in supply falling from its peak of 17.6% at the end of 2009 to 16.5% currently.
- Conversely, given the need to cut costs, public sector demand will remain low over the short to medium-term as Central Government embark upon the rationalisation process for departments.
- Investment levels have increased throughout 2010, with the last 12 months seeing the largest transactional volumes ever recorded.

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Leasing Market

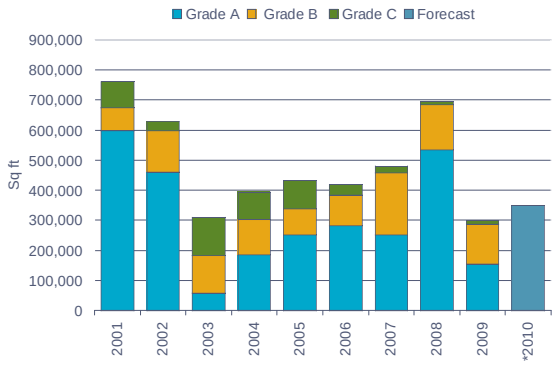
Figures recorded to date show 278,035 sq ft of space let in the prime core, which is 18% up on the same time last year. End year figures are anticipated to reach in the region of 350,000 sq ft.

The wider CBD take-up totalled 546,863 sq ft, which was bolstered by a 107,000 sq ft deal at Calthorpe House, Edgbaston to medical technologies company Binding Site.

Forecasts for the remainder of the year suggest that total take-up will be in the region of 350,000 sq ft, in line with 2009 levels.

While there is no immediate prospect of a return to normal levels of take-up, we expect that the key driver of the market in 2011 and beyond will be the fact that there are now no planned development completions in the immediate future. This has resulted in severely restricted new supply coming to the market, which is good news for those landlords with standing stock as the supply/demand balance moves in their favour.

Take-up remains muted in 2010.



Source:Savills

Take-up over the last five years has been dominated by the public sector, however, conversely, given the need to cut costs, public sector demand will remain muted over the short to medium-term as Central Government embark upon the rationalisation process for departments. However, the view is that the tax rises and less capital spending will result in fewer job losses in the public sector than we saw during the early-1990's recession.

Following October's spending review there has been much focus on how public sector austerity will hit some regions more than others. All cities need to radically review the role of the public sector in their economies. While the public sector will remain a major employer in cities, it will not be a driver of employment growth over the next decade.

Rental growth will not emerge until job creation in the private sector picks up. Will 2011 be the re-emergence of the corporates?

The expected recovery of the city's private sector should help to insulate it from the adverse effects public sector job cuts may have. Encouragingly, according to Deloittes, 344,000 jobs have been created in the private sector this year in the UK, with private sector employment set to improve over the next 12 months.

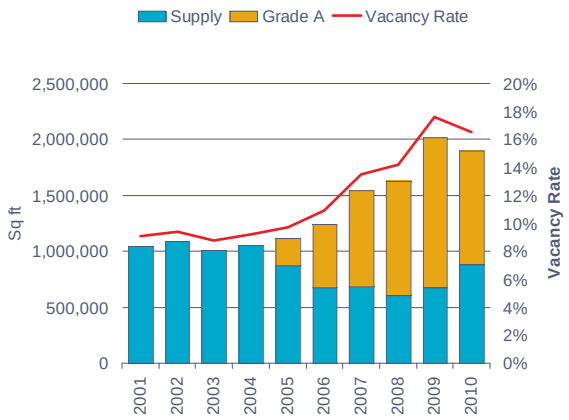
The recovery in take-up is expected to start from 2011 onwards with signs of a pick up in tenant demand becoming more apparent with larger financial requirements now looking more seriously at Birmingham as a place to do business.

These requirements include; a 60,000 sq ft requirement for Pinsent Masons, a 50,000 sq ft requirement for Rare Games (part of Microsoft), along with a number of financial requirements in the market, totalling around 600,000 sq ft. This is a clear sign that the private sector is coming back, with positive signs that companies are starting to look towards pushing their businesses forward.

WIth a low cost base the regional office markets are likely to see the return of back office functions, where low cost, high quality, larger floorplates, with an access to a wide ranging skill set, come at a discount to London.

Focusing on the supply side, encouragingly, the development pipeline peaked in 2009, with nothing currently under construction. This has resulted in supply falling from its peak of 17.6% at the end of 2009 to 16.5% currently. There are now only three buildings over 100,000 sq ft currently available on the market.

Supply continues to fall.



Source:Savills

However, if we compare the total availability with the average annual take-up in Birmingham, there appears to be nearly four years supply of office space currently on the market and until this is chipped away at rental

Leasing & Investment Market

growth will remain elusive.

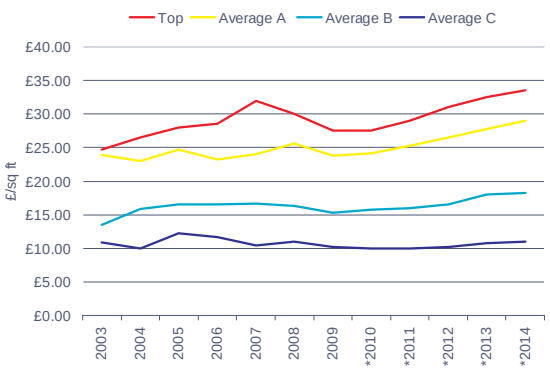
The attractiveness of the refurbishment market will come into its own, with 2 Colmore Square being an inspiration for the city. These refurbishments will be beneficial for tenants who are looking for attractive, lower cost buildings and also for developers where, as well as being cheaper to fund, the speed to market means it is much quicker at generating an income.

The shoots of recovery in the occupational market are expected from 2011, as the low levels of development completions begin to impact on demand. There is definitely no boom in demand ahead, but a gradual return to average annual levels of take-up, combined with a limited development pipeline will continue to diminish the amount of good quality office space that is on the market in Birmingham.

Indeed, prospects for regional office rental growth are improving. With London offices now showing upward rental growth on both prime and average rents we believe it will only be between 12 and 18 months before we see sustained office rental growth in the regional markets.

From a landlord's point of view 2010 has been a tough year with heavy competition for the comparatively few requirements putting pressure on headline and net-effective rents. Current rents and the incentives on offer present occupiers with a 'bottom of the cycle opportunity' to acquire office space on very favourable terms, however, 2011 is expected to see the first real signs of rental growth, with a 2% growth forecast on top rents

Top rents will stabilise in 2010, with rental growth expected from 2011 onwards.



Source:Savills **forecast*

By mid-to-late 2011 we expect to see net-effective rents beginning to rise, and this will be followed by headline rental growth in the most sought after locations in and around the City.

The Investment Market

Looking at the investment market, the collapse of the commercial property market which 'bottomed-out' in early 2009 saw average values almost halve from their peak in mid-2007. However, since then, pricing recovered significantly through the second half of 2009 and the first half of 2010.

Investment levels have increased throughout 2010, with the last 12 months seeing the largest transactional volumes ever recorded in Birmingham. However, the majority of investors remain relatively risk adverse, focusing on acquiring prime, well-secured assets displaying strong property fundamentals.

Prime yields have continued to harden during 2010, albeit at a slower rate. There has been a compression of over 150 bp from summer 2009, with prime yields now standing at 5.75%.

With a lack of Grade A stock available to occupiers and the pent up demand implied by upcoming lease breaks, this may lead investors to take on well-located Grade B stock in need of refurbishment and asset management opportunities if they can be acquired at attractive prices. However, the availability of debt for these types of deals will determine the scale of this activity.

Savills has seen increasing life in the lending market with money available for the 'right' investment. While there is still significant demand for prime assets, the margin between prime and secondary is widening and we expect this to continue into 2011.

Significant deals Include:

Building	Price (£m)	Yield	Vendor	Purchaser
2010				
0ne Snow Hill	126 m	6.15%	Ballymore	Commerz Real
Mitchells & Butler Bldg, Fleet Street	40 m	5.85%	Moorfield	Private Overseas Investor
Rutland House	27 m	6.1%	Remax	Aviva
Bank House	21 m	8.2%	API	F&C

Source:Savills

Birmingham Map & Key Contacts

Definitions

Grade A: New developments (including speculative schemes reaching practical completion within the next 6 months).

Grade B: Space previously occupied, completed or refurbished in the last 10 years.

Grade C: Space previously occupied, completed or refurbished later than 10 years.

Note: We monitor space over 3,000 sq ft.

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