

Bristol Office Survey

Summer 2010

The return of occupational demand remains tentative, but cranes are reappearing on the skyline



WestOne by Westmark Developments, the only speculative building completing this year (26,983 sq ft)

- Take-up for the first 6 months of the year totalled 489,113 sq ft, 74% up on the same period last year, driven by first quarter performance.
- Concerns surrounding the strength of the economic recovery following the emergency budget saw take-up slow during Q2. However, the out-of-town market was more robust.
- There was a return of large requirements to the market this year as occupiers benefited from current market conditions, securing new space on historically advantageous terms.
- Top achieved rents in the city centre were £27.50 and £21.00 out-of-town. We expect that rents will hold at current levels through to 2011/12.
- Investment activity slowed this year with transactions totalling £57.9m over the first half of 2010, 23% down on the same period last year.
- The slowdown has been in response to stock issues as investors have refocused their attention on under supplied prime assets in the face of negative newsflow surrounding GDP growth and public sector job cuts.
- UK Institutions are starting to make a tentative return to the market, being the biggest spenders this year. Their re-entry to the market and yield hardening has meant other purchasers have struggled to compete, particularly on prime assets.
- The biggest threat to Bristol's recovery is the forthcoming public sector job cuts and potential knock on effects on private sector confidence. However, the expected recovery of the city's private sector should provide some level of insulation.

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Take-up, supply & rents

Following a difficult 2009, there were some signs of recovery in 2010. Take-up for the first 6 months of the year totalled 489,113 sq ft, 74% increase on the same period last year. This was driven by first quarter performance, accounting for 61% of the half year total, due to a number of large lettings. The public sector figured strongly and key transactions included North Somerset Council acquiring 83,000 sq ft for their new headquarters at Castlewood in Clevedon. Avon & Somerset Police acquired 41,000 sq ft at Aviva's city centre 1 Bridewell Street building, taking a further 15,600 sq ft on Harlequin Park at Emersons Green.

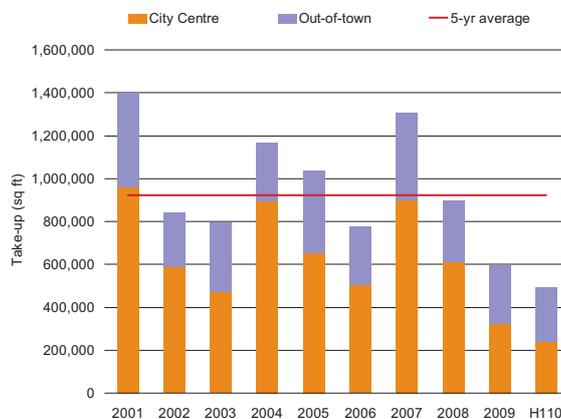
The slowdown recorded in Q2 was driven by concerns surrounding the strength of the economic recovery following the emergency budget. However, the city centre and out-of-town markets responded differently with the latter proving more robust. Out-of-town take-up was 8% down in Q2 on the previous quarter, whereas the city centre recorded a 59% drop.

The differing performance of both markets reflects their respective appeal and occupier mix. The city centre is driven by the financial and business service sectors, which were significantly affected by the recession. As wider economic concerns re-emerged, occupier plans to expand and/or take on new space have been put on hold, and those deals that do take place are taking longer to complete. In contrast, out-of-town is dominated by firms in the construction, technology and defence sectors, where space needs are driven by contractual obligations. With some signs of recovery, firms are taking on additional space in order to service contracts, feeding positively into out-of-town demand. However, there are concerns over the sustainability of this recovery for the remainder of the year.

It is interesting to note the return of larger requirements to the market. During the past 5 years only 3% of deals have been over 20,000 sq ft. This year they have accounted for 8% of transactions. This could be taken as an indicator of improving occupier confidence but it is more likely that occupiers are benefiting from current market conditions to secure new space on historically advantageous terms. Since the public sector accounted for a number of these transactions, the forthcoming cutbacks are likely to negatively impact total take-up during H2. In turn, availability which currently stands at c.3m sq ft, is set to increase.

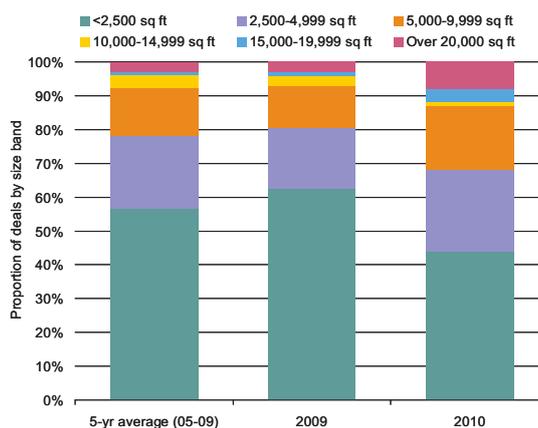
In terms of recorded rentals there has been a bounce back in city centre headline rents with £27.50 per sq ft achieved at The Paragon, whilst out-of-town saw a reduction to £21.00 per sq ft. We expect headline rents to hold at current levels through to 2011/12 with incentives also holding steady. The lack of new stock coming to the market, with only Westmark's WestOne development coming to the market this year and HDG Mansur completing 110,524 sq ft at Bridgewater House in 2011, will also help to maintain top rents.

Take-up slowed in Q2



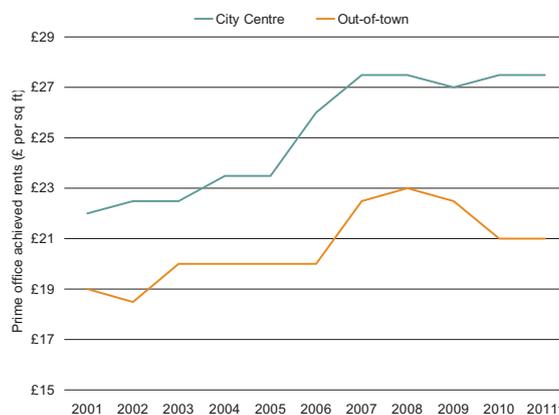
Source: OAS; Savills

Larger occupiers returning to the market



Source: OAS; Savills

Top achieved rents



Source: Savills

Investment & outlook

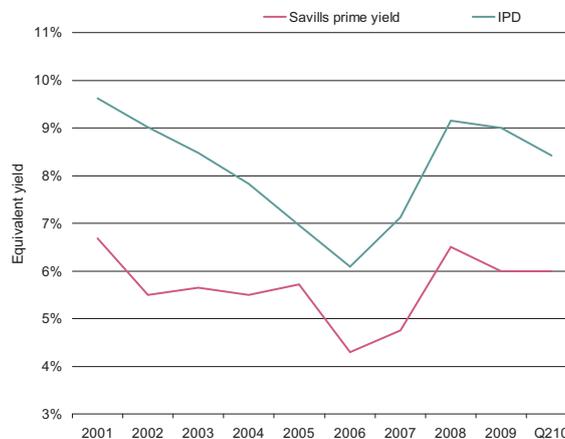
Investment activity slowed this year with transactions totalling £57.9m over the first half of 2010, 23% down on the same period last year. This slowdown has been primarily driven by stock issues. The negative newsflow surrounding GDP growth and the public spending review has dented investor confidence. In response, investors have refocused their attention on prime assets, notably those with a strong covenant with over 10 years of income. However, supply is heavily constrained and while there is a relatively good supply of multi-let secondary assets, demand is limited as investors have become increasingly more reluctant to move along the 'risk curve'.

Despite this demand/supply imbalance further hardening in yields this year looks remote. Prime yields are now in the range of 6% and are likely to stay at this level through to 2011. Transaction yields did hit 5.75% in Q2 with the purchase of 1 George's Square by the British Steel Pension Fund for £25.4m. Yet, anecdotal evidence suggests some easing in the market since this transaction.

UK Institutions are starting to make a tentative return to the market after being net divestors in 2008 and 2009, spending £38m in H1 2010. The British Steel Pension Fund purchase of 1 George's Square accounted for the bulk of this. The property is currently let to Clarke Wilmott with 13 years unexpired. With UK Institutions having re-entered the investment market and the hardening in yields, other purchasers have struggled to compete, particularly on prime asset sales. Overseas investors, key drivers of the market in 2008, have become net divestors this year flipping properties in order to maximise on the returning appetite from UK investors. For example, the previously mentioned 1 George's Square was purchased in 2008 by IVG for £21.9m, 14% lower than its sale price this year.

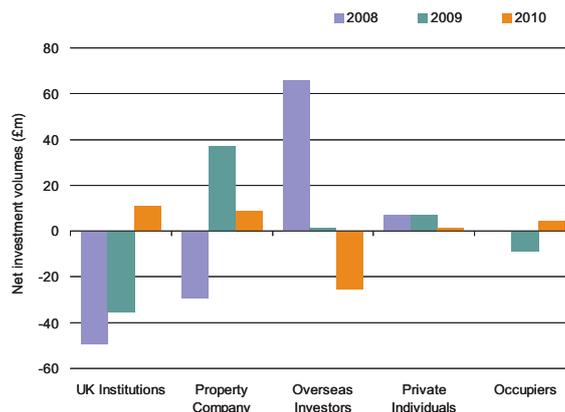
At the moment the biggest threat to Bristol's recovery is the upcoming public sector job cuts and knock on effects this may have on private sector confidence. A recent study by Local Futures forecast that Bristol could lose approximately 5,600 public sector jobs by 2016. While this is significant it would represent only 2.1% of all jobs and in comparison to other major regional cities was ranked 9th based on job losses. The expected recovery of the city's private sector should help to insulate it from the adverse effects job cuts may have. For example, in Oxford Economics European Cities and Regions service (Summer 2010), Bristol was ranked 12th across Europe for GDP growth (2.9%) over the next 5 years, second only to Inner London in the UK. With recovery expected to be relatively strong, for the more opportunistic investors and occupiers now may be the time to capitalise on stagnating yields and existing/ improving occupier incentives.

Hardening in prime yields stagnating



Source: Savills; IPD©

UK Institutions making a tentative return



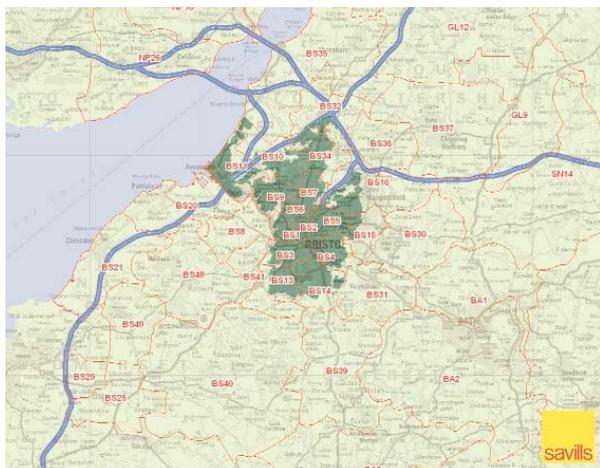
Source: Property Data

Bristol top ranking regional city for GDP growth

European Ranking	City	% change (2010-2015)
8	Inner London	3.5%
12	Bristol	2.9%
13	Leeds	2.8%
16	Edinburgh	2.7%
18	Glasgow	2.5%
19	Manchester	2.5%
23	Birmingham	2.3%
25	Cardiff	2.2%

Source: Oxford Economics

Survey area & key contacts



Total stock levels for Bristol city centre and outer areas is approximately 12.5 million sq.ft.

Definitions & statistical notes

Top rent

Highest rent achieved in one or more transactions.

Property criteria

Transactions and supply recorded for units in excess of 1,000 sq ft.

Grade A space

All new development (including speculative schemes reaching practical completion within six months, plus major refurbishments).

Grade B space

Space previously occupied, completed or refurbished in last 10 years.

Grade C space

Space previously occupied, completed or refurbished more than 10 years ago.

Total office stock

Total level of office space as recorded by the Office for National Statistics.

City Centre

City centre refers to BS1 and BS2 postcodes.

Out of Town

Out of Town refers to anything outside the city centre (anything outside postcodes BS1 and BS2).

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