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Savills World Research
UK Commercial

Spotlight
Leeds Offices

November 2013

SUMMARY

- Take-up for the first three quarters of 2013 was 62% up on the same time in 2012 and is already an impressive 32% up on the end of year figures for 2012.
- Market sentiment and occupier demand continues to improve, with a number of larger requirements, both in and out-of-town, circling the market.
- Leeds saw a supply fall of 31% over the last 12 months, the largest of any of the regional cities with Leeds vacancy rate now standing at 5.4%, the lowest vacancy rate outside Central London.
- UK institutions and overseas investors are becoming more dominant in the Leeds office market, with investors looking more closely at Leeds as available space reduces with limited speculative schemes being developed.

"The growing confidence in the Leeds office market, with growing demand and limited supply, will be a catalyst for developers to act sooner rather than later." Paul Fairhurst, Director, Office Agency, Leeds

Occupational market

■ Leeds has come to life over the last 12 months with the opening of the one million sq ft Trinity Leeds development and the 13,500 seater capacity Arena, followed by the refurbishment of the Merrion shopping centre and the Victoria Gate development, due to start in 2014.

■ The office market has followed suit with a significant increase in take-up and a notable increase in the size of lettings and requirements circulating the market. The last 12 months have seen three large buildings taken up (The Mint, No1 Leeds and Broadgate), which has shrunk the supply pool to unprecedented low levels.

■ At 525,655 sq ft, take-up for the first three quarters of 2013 was 62% higher than the same time in 2012 and is already an impressive 32% up on the end year figures for 2012. This is the best three quarters since 2000. We expect end year figures to exceed 650,000 sq ft.

■ Take-up figures are showing a bias towards good quality stock, with 71% of this take-up being of Grade A standard. This is against the five year average of 56%.

■ 2013 has also been the year of the larger letting, with three deals in the first half of the year, over 50,000 sq ft, helping boost take-up figures. These include: 76,000 sq ft at Broadgate to the Yorkshire Building Society; 73,000 sq ft to Dart Group at The Mint and 60,000 sq ft on a pre-let to KPMG at 1 Sovereign Square. The second half of the year has seen the council take a part re-gear/part expansion on 170,000 sq ft at Town Centre Securities' Merrion House.

■ Market sentiment and occupier demand has continued to improve over 2013. Indeed, the largest increase in private sector employment outside London, was seen in Yorkshire and The Humber (82,000; 4.3%). With a number of larger requirements both in and out-of-town in the market, there is increasing optimism that further pre-lets will happen over the next 12 months, with SKY likely to be next.

■ Looking specifically at supply levels, Leeds saw an supply fall of 31% over the last 12 months, the largest of any of the regional cities. Leeds vacancy rate now stands at 5.4% (c.850,000 sq ft), the lowest vacancy rate outside Central London.

■ With a significant lack of large floorplates available and with a significant volume of lease events coming up over the next 36 months, one of the big questions concerning the Leeds office market is where will the 'suitable space' come from to accommodate this increased demand?

■ The pre-lets agreed with KPMG and Shulmans has allowed Leeds city council/MUSE and MEPC to kick-start some much-needed office development in the city core and is a clear sign that confidence is returning to the market. Indeed, the growing confidence in the Leeds office market, with growing demand and limited supply, is a catalyst for developers to act sooner rather than later.

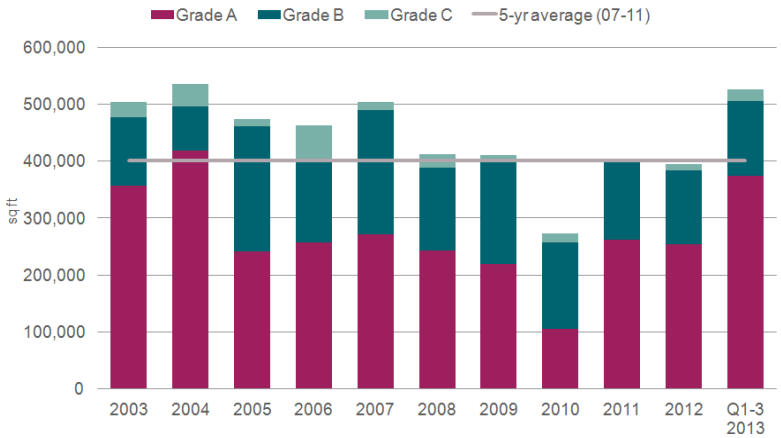
■ With the city in such a strong position in terms of its supply/demand dynamic, it is likely that one of the developments ear marked for office use is likely to attract forward funding over the next 12 months, with all eyes on which will be the 'next big scheme'. For those investors and developers with well located sites, there are great opportunities ahead of them.

■ However, in the short term, with less that 100,000 sq ft of Grade A supply currently on the market, Leeds needs to look for more creative ways to cater for increasing demand. Refurbishments at 1 City Square, 1 Victoria Place, 21 Queen Street, Minerva House and Capitol House are helping to 'fill the gap', although, with smaller floorplates, these wont be enough to satisfy the increase in larger requirements going forward.

■ Examination of existing occupiers gives us an indication of the type of businesses likely to be attracted to the regions. The technology sector has seen job growth at its fastest pace since 2010, outpacing the private sector at 4.3% vs. 0.9% per annum. It has certainly gained momentum in Leeds during 2013, dominating take-up with a 34% share (against a 6% share in 2008). Oxford Economics predicts that employment in the technology sector, in Leeds is forecast to grow by 8% over the next five years, which will help boost demand levels.

GRAPH 1

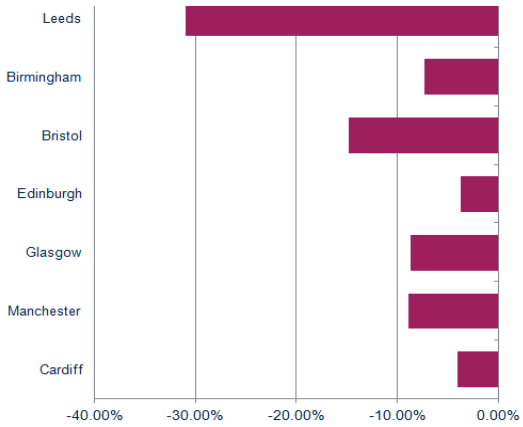
Take-up levels are 32% up on 2012 end year figures



Graph source: Savills Research

GRAPH 2

Leeds has seen the biggest fall in supply across all regional cities



Graph source: Savills Research

■ More traditional sectors, like the professional sector, have helped underpin the market over the last five years, taking a 23% average share. This sector continues to account for a large share of take-up (28%) as we go through the first three quarters of 2013. In some cases, companies have moved their entire operations to Leeds. Law firm Dickinson Dees is a good example, having moved from York to Leeds, before completing a successful merger with Bond Pearce. Education provider The University of Law is also relocating from York to Leeds at the end of 2014.

■ The out-of-town market is also seeing a revival. With 94,260 sq ft taken up in the third quarter of the year, a 57% rise on the same time last year. We expect this market to continue to pick up over the next 12 months, as this becomes an over-spill for larger companies unable to find suitable space in Leeds CBD.

■ Prime headline rents have remained static at £25 per sq ft during 2013, however, Incentives will start to fall, with a likelihood of rental growth in 2014 and beyond, with the pre-let market underpinning rents. Savills are predicting headline rents to grow by 2% per annum over the next five years.

■ The over-riding message for Leeds in 2013, is one of confidence, which has been further bolstered by the hosting of the Grand Depart of the Tour de France in 2014, which is a significant good news story for both the city and the region. Also underpinning this is significant occupational demand, demonstrating further confidence in the local economy and helping to kick start the return of speculative development in the city.

Investment market

■ UK institutions and overseas investors are becoming more dominant, with investors starting to look more closely at Leeds. This is driven by the expectation of an imminent rental recovery, combined with improving confidence, and the record wide yield gap between London and the regions. Yields continue to harden and are now at 6.25% as witnessed at 1 Sovereign Square, with more downward pressure expected.

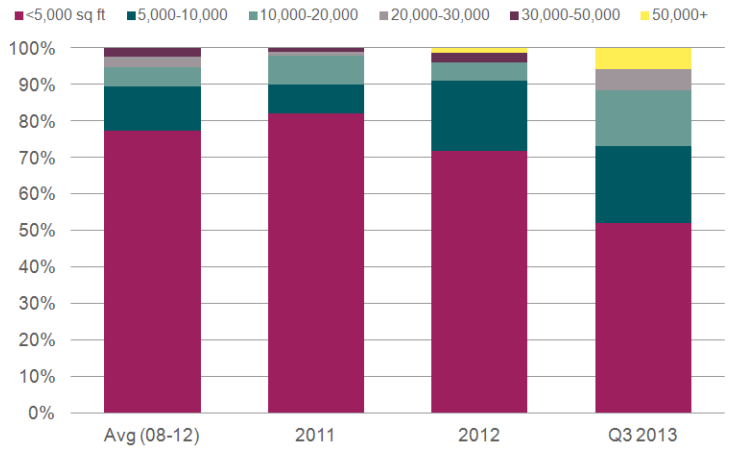
■ The largest deal in Leeds in 2013 was the sale of Toronto Square for £29m, which reflected a net initial yield of 7%. However, what is interesting about this deal is that it was 20% vacant when purchased by M&G from Highcross in August, highlighting the belief that strong tenant demand for high quality offices in the city, will ensure the rest of the building will let quickly in an increasingly tight city centre market.

■ What can we expect from late 2013/early 2014?

■ There will be a limited desire to sell, however, investor appetite for regional offices are increasing and investors are looking more closely at the region as available space reduces with limited speculative space being developed, which could fuel investor interest and subsequent pricing as we move into 2014.

GRAPH 3

2013 has seen the return of the larger letting



Graph source: Savills Research

Expert view

Simon Lister director of office investment in Leeds, looks behind the statistics

There were c.£77m of transactions in 2012, which was considered poor. This poor performance was primarily driven by stock issues, owners who did not need to sell chose to hold off as realistic sale prices are often below valuation.

The story across the board is that there is strong demand for primary and secondary assets with not enough stock available. Continued strong demand and lack of stock continues to support downwards yield shifts in the office sector as well as improved occupational demand and take-up.

Total in town office transactions for the first three quarters of 2013 have totalled c.£111 Million, which reflects this renewed confidence in Leeds as an office location and also a sign that both vendors and purchasers pricing expectations are becoming more aligned.

Recovery in regional markets is usually driven by UK institutions, who appear to have recognised the supply/demand dynamic within the city centre which is resulting in more transactions and seemingly downward pressure on yields to reflect the anticipated rental growth and continued levels of office take-up. Correspondingly, yields have moved dramatically since March. It is fair to say that Leeds still looks like good value in terms of both headline rents and also levels of return available when compared with other regional cities.

Investor appetite for regional offices is increasing and investors are looking more closely at the region as available space reduces and limited speculative space is being developed, which could fuel investor interest and subsequent pricing during the latter part of 2013 and into 2014. We anticipate that UK Institutions and overseas investors will become more dominant in the regional markets and a number of developers will be seeking funding on the back of significant pre-lets. This has been successfully demonstrated by the funding of KPMG's 1 Sovereign Square development by British Steel Pension Fund.

Despite this it will be some time before any speculative development takes place as funding of a speculative nature is still very difficult to secure, but we may see some funding of part pre-let schemes as stock levels remain scarce and occupational demand continues to improve.

Headline stats, definitions and contacts

Headline statistics	Take-up: In Town	Take-up: Out of Town	Top rents (£ per sq ft)	Prime yield
Full year 2012	394,622 sq ft	330,031 sq ft	£25.00	6.5%
Q1 - Q3 2013	525,655 sq ft	289,762 sq ft	£25.00	6.25%
End of year outlook	↑	↑	→	↓

Definitions & statistical notes

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

Please contact us for further information

Paul Fairhurst
Leasing
0113 220 1207
pfairhurst@savills.com

Simon Lister
Investment
0113 220 1208
slister@savills.com

Mark Wilson
Investment
0113 220 1254
mwilson@savills.com

Patrick Carter
Leasing
0113 220 1203
pcarter@savills.com

Clare Bailey
Research
020 7409 8863
cbailey@savills.com

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