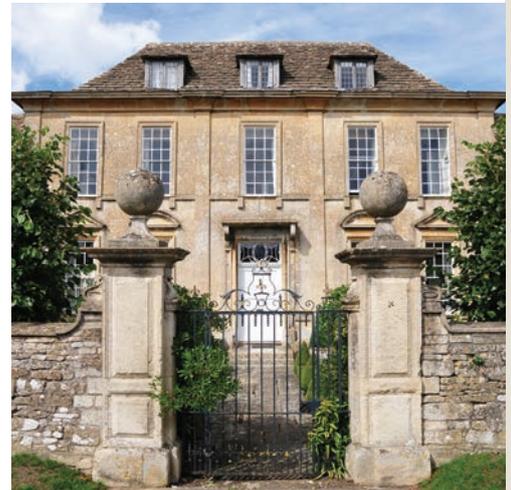
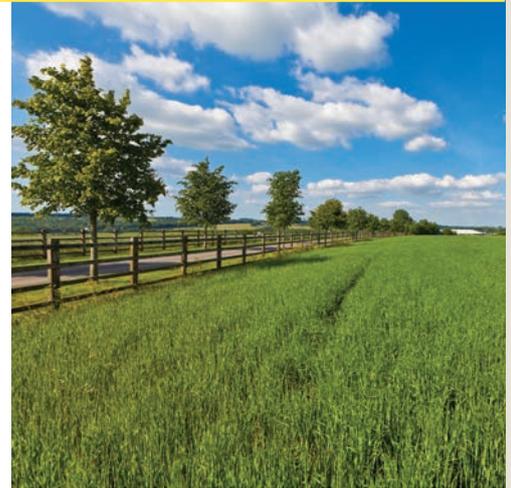


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Savills World Research  
Commercial, Residential & Rural

# Spotlight Key Themes for UK Real Estate in 2014

January 2014



[savills.co.uk/research](http://savills.co.uk/research)

# Forecast values

## WHERE TO INVEST IN 2014

Savills growth forecasts for the commercial, residential and agricultural sectors for 2014

Sector	Subsector	2014			Average 2014-18	
		Gross Yield	Capital Growth	Rental Growth	Capital Growth	Rental Growth
Retail	Prime	4.7%	7.8%	2.3%	4.1%	3.0%
	Secondary	6.9%	6.6%	-0.6%	2.7%	0.6%
Office	Prime	4.9%	10.1%	4.5%	5.5%	4.4%
	Secondary	8.3%	6.4%	0.0%	3.4%	1.5%
Industrial	Prime	5.8%	7.2%	2.5%	2.5%	1.6%
	Secondary	9.3%	7.8%	2.0%	3.0%	1.3%
Residential	Prime London	3.2%	3.0%	2.5%	4.3%	3.8%
	UK Mainstream	5.5%	6.5%	2.0%	4.6%	3.9%
	London Portfolio	4.8%	8.5%	3.5%	4.5%	4.7%
	Regional Portfolio	8.3%	6.0%	1.6%	4.6%	3.7%
Agricultural	Top Quality	2.0%	8.0%	9.0%	8.0%	9.0%
	All Farmland	1.6%	6.0%	7.0%	6.0%	7.0%
	Poor Quality	1.9%	3.0%	6.0%	3.0%	6.0%

# Overview

# THE UK REAL ESTATE MARKET IN 2014

The UK real estate market in 2014 will see a broader-based recovery than was seen in 2012 and 2013. Occupier and investor confidence will improve in line with the economic recovery, and market performance will be typical of the second stage of a recovery – albeit a slightly weaker recovery than we have seen coming out of previous cycles.

Risk-averse investors, both domestic and international, will continue to be attracted to prime residential, agricultural and commercial assets and locations. However, 2014 will also see increasing investor interest in some secondary markets where the recovery is about to begin, and capital value growth prospects are improving.

“Risk-averse investors will continue to be attracted to prime residential, agricultural and commercial assets and locations” Savills Research

## Growth story

2014 will also see the beginnings of the return of the domestic buyer to the UK real estate market, as home buyers and institutions regain their confidence in the economic outlook. In particular, we expect to see continued strong investor interest in residential property as a large-scale asset class.

Non-domestic investors will continue to remain heavily biased towards London real estate, reflecting its position as a globally recognised and highly liquid safe-haven.

For the commercial and residential real-estate markets the growth story

will no longer just be about London and the South East, with business and consumer confidence rippling outwards to the prime regional and sub-regional locations.

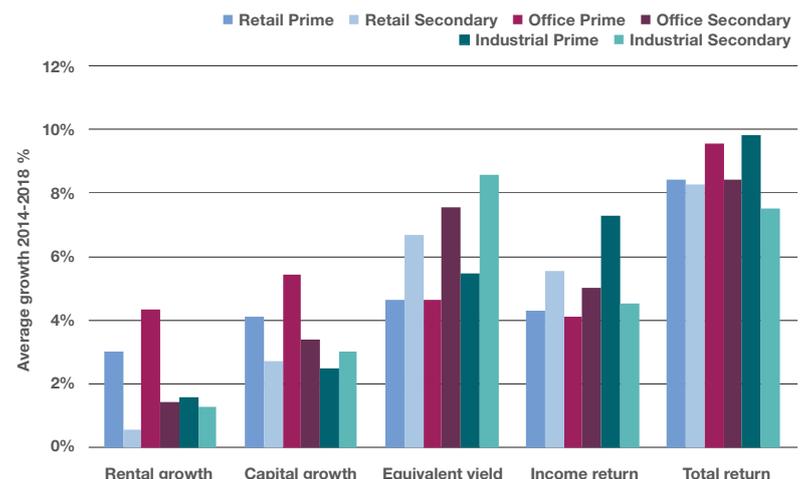
Agricultural land will continue to be the best performing of the three asset classes due to the scarcity of prime farmland that will come to the market.

## Risks

The biggest risks to the UK real estate market in 2014 are political and economic. If interest rates start to rise before the economy is recovering robustly, then the recovery will undoubtedly be delayed.

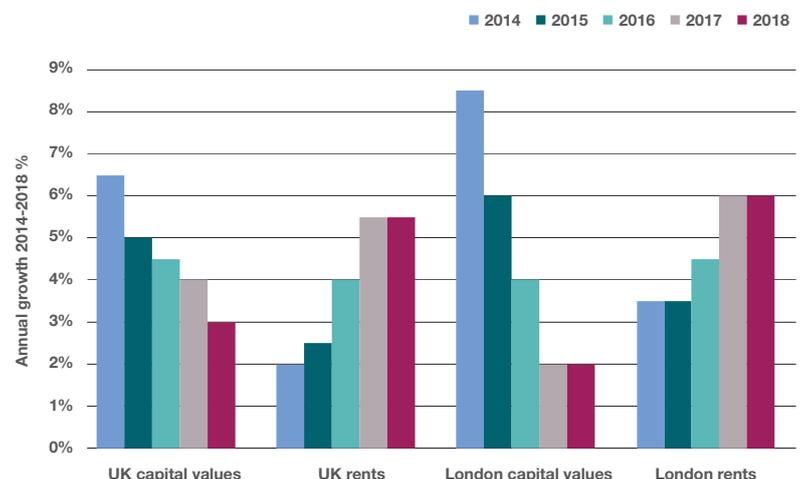
Furthermore, too much pre-election tweaking of real estate related taxation could also damage the impending recovery. →

GRAPH 1 Outlook for key commercial sectors



Source: Savills Research

GRAPH 2 Residential property price forecasts



Source: Savills Research

## Commercial

The major theme in the UK commercial property market in 2014 will be a more widespread recovery. 2013 saw a continued robust pick-up in tenant and investor demand for all types of commercial property in London, but we expect that 2014 will see this interest widening to cover the key regional cities, distribution hubs, and regional malls.

This recovery will be driven by improving business confidence on the back of the better domestic and global economic outlook.

We expect debt markets to loosen slightly, though finance for speculative development and tertiary investments will remain virtually non-existent outside London.

.....  
 “The recovery will be driven by improving business confidence on the back of the better domestic and global economic outlook” Savills Research  
 .....

Risk-averse international investors will continue to be heavily biased towards the capital city, but some will be tempted to the regions by higher yields and less competition. The more risk-embracing investors will be looking to capitalise on the historically wide spread between London and regional yields, as well as the even wider spread between prime and secondary.

## Residential

2013 saw a revival in the UK housing market with increased buyer numbers taking advantage of low interest rates. Further short term price growth is likely to be driven by strong buyer sentiment underpinned by an improved economic outlook. Beyond price growth prospects will be dependent on earnings growth given an erosion of mortgage affordability due to rate rises.

With the potential impact of Help to Buy limited by lending criteria and the ability of borrowers to meet them, the demand for rental accommodation is likely to continue to be underpinned

by a lack of accessibility to home ownership. Households in the private rented sector are expected to grow by one million in the UK over the next five years presenting a significant opportunity for institutional investment.

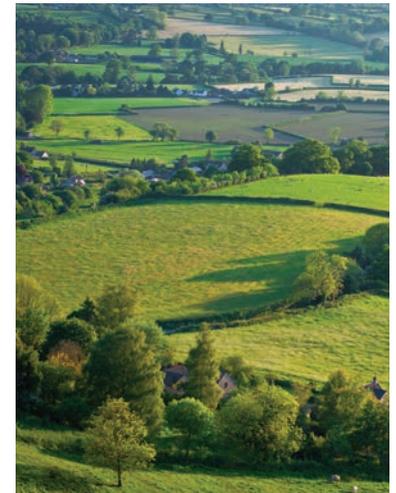
Prime Central London has been the best performing residential market since 2005, fuelled by wealth from the financial services sector and strong overseas demand. In 2013 price growth slowed in response to stamp duty changes.

Further political focus on high value property taxation is likely to temper pre-election demand, with the tax policy adopted the next government determining growth prospects immediately thereafter.

## Agricultural

Prospects for further growth in UK farmland values remain positive but land quality, type and location are critical. However, the influences for future growth are finely balanced against the risks.

On the one hand, supply is historically low, the product is finite. The increased demand for land to provide renewable energy sources, which is competing with food production to feed growing populations amidst rising concerns for food and fuel security are all drivers for a competitive marketplace.

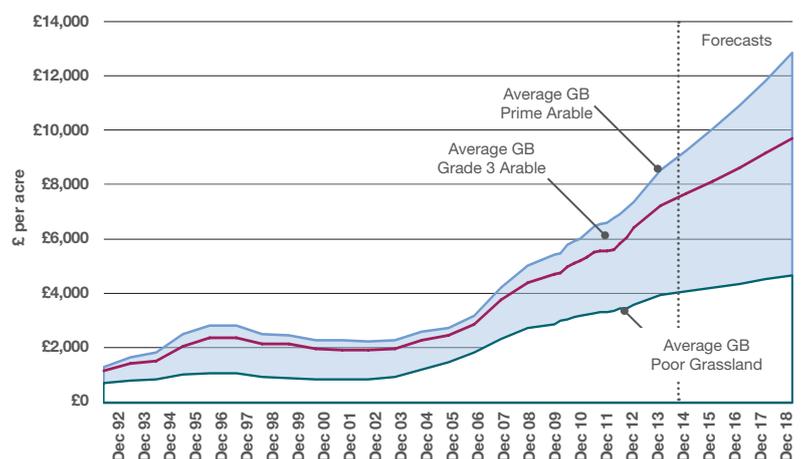


However, there are always issues which threaten to upset the balance including interest rates, debt due to pressure on profitability and cash flows, changes to taxation and subsidy regimes – all of which have the potential to increase the supply of land available, therefore putting pressure on future price growth.

During the next five years we forecast growth will be more muted than that recorded over the past 10 years.

We also expect significant variations between the rates of growth across the farmland market. Currently the value gap between the best and the poorest land, is as much as £4,600 per acre (see Graph 3 below).

GRAPH 3 Price gap widens for best farmland



Source: Savills Research

## TOP PICKS FOR 2014

### Commercial

#### ■ Prime London offices and retail

The best prospects for double-digit rental growth this year, with the West End remaining heavily undersupplied and City yields looking attractive.



#### ■ Top seven regional city office markets

Falling vacancies, recovering tenant demand and no development activity will drive a rental recovery from 2014. Yield spread over London looking interesting.



#### ■ Big sheds and local hubs

Continued growth of internet retailing will drive demand for large warehouses for big retailers and 3PL operators. Challenge of 'last mile' will drive interest in local hubs.



### Residential

#### ■ London and the South East

Most major cities offer investment opportunities but we expect a focus on London & the South East where capital growth prospects are strongest.



#### ■ Second tier London boroughs

Such markets have the potential to deliver the next phase of price growth in the capital without undue reliance on mortgage debt.



#### ■ Rich markets in London's hinterland

With London having outperformed the rest of the UK since 2005, these markets are likely to benefit most from the ripple effect in the short to medium term.



### Agricultural

#### ■ Large commercial arable farms

Will continue to benefit from a flight to quality with buyers focusing on cropping flexibility and yield targeting farms with top quartile income potential.



#### ■ Quality rural estates

Signs of a recovery will improve activity from lifestyle buyers for estates with a diverse property portfolio offering income potential free of commodity price volatility.



#### ■ Residential farms

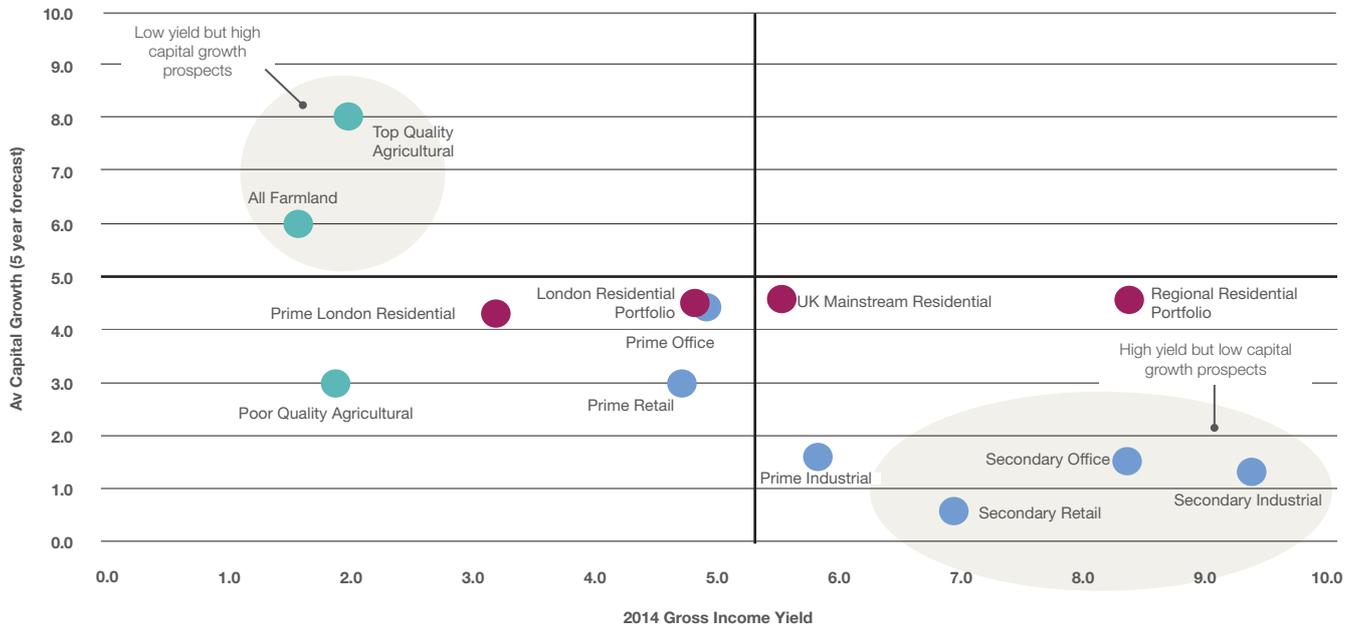
With the residential market forecast to recover the potential uplift in residential farm values may offer some opportunities but location and quality will still be key.



GRAPH 4

## Returns matrix Relationship between income and capital returns by property sector

● Commercial ● Residential ● Agricultural



Source: Savills Research

## Savills Research Department

Expert analysis and specialist insight in every area of real estate

The Savills research team is unique in providing advice and analysis to clients across all commercial, residential and agricultural sectors of the property market. The geographical coverage spreads from Central London to all

markets in the UK and also includes the key market across Europe. Our established research team has a strong reputation for producing accurate, well-informed and, above all else, independent analysis and commentary. The team

is also able to provide demographic/ GIS services and assist with investment decisions. External clients include developers, landlords, investors and occupiers.

## Please contact us for further information

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### Residential

### Agricultural