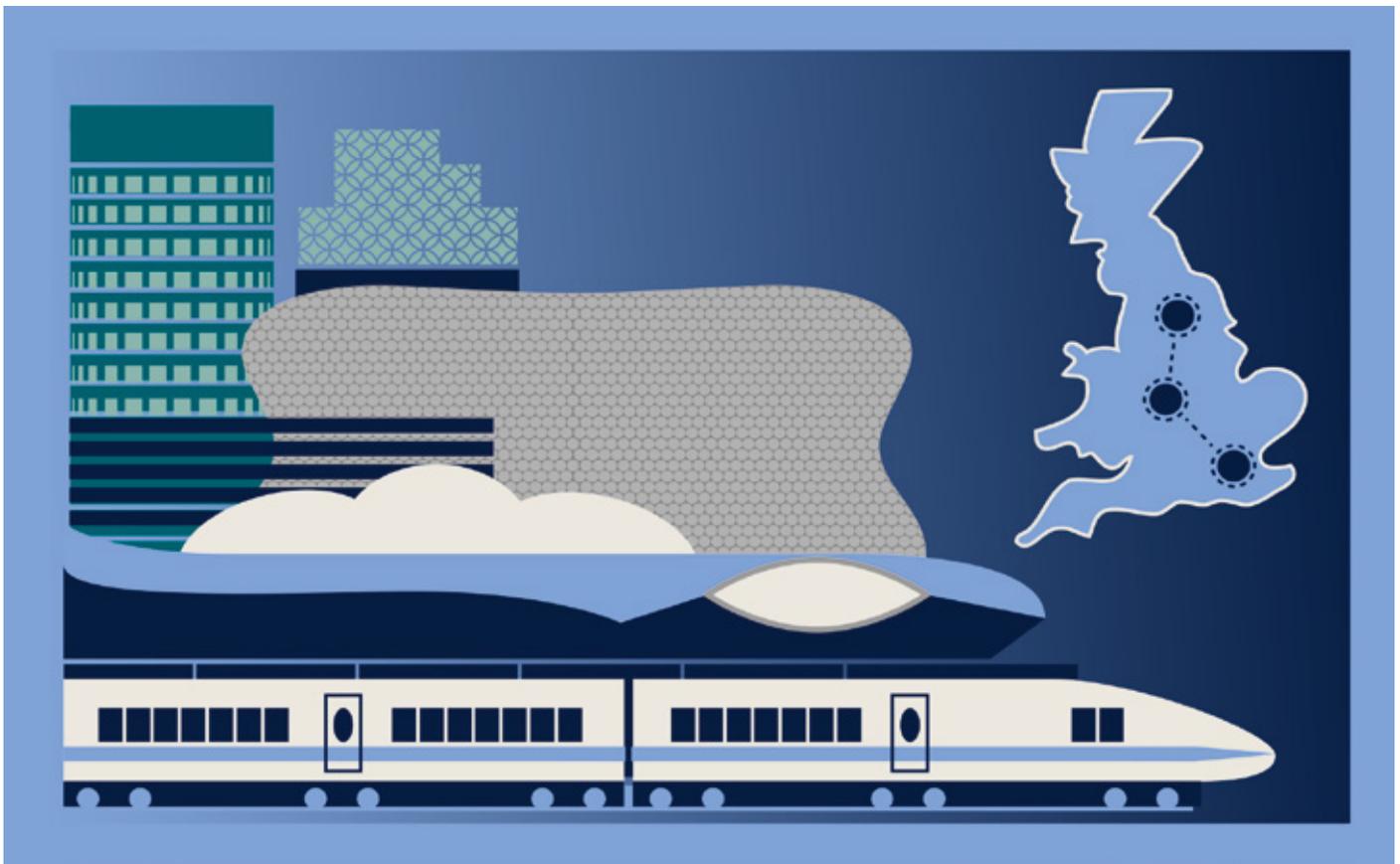


Spotlight | 2018

Birmingham: Delivering transformation



Summary Public and private investment combined with a growing economy is opening up new opportunities for development in Birmingham’s city centre and beyond

■ Investment in local and national infrastructure, particularly the Metro network, is opening up new areas of the city for development. Construction activity across all sectors is at its highest level since 2008.

■ The relocation of major employers to the city is driving high levels of office take up. City centre take up reached 1,005,000 sq ft during 2017, 51% above the 10-year average.

■ Residential development in the city centre has been supported by price growth, making complex regeneration schemes viable. New players are entering the market, including Build to Rent providers and housing associations.

■ Beyond the city centre, there is competing demand for land, both for residential and industrial development. Well connected logistics property is outperforming the national average.

■ Although volumes of residential development have picked up, there is still a shortage of delivery against housing need. There is a particular need for more 3 and 4 bedroom family housing.

On the cusp of reinvention

A bold vision for development in the city is unfolding thanks to investment in infrastructure

Birmingham is on the cusp of re-inventing itself. The Big City plan sets out an ambitious vision for the future. The HS2 trainline “presents an unprecedented opportunity to establish the West Midlands as a world-class business location”. But the transport upgrade won’t do it on its own; Birmingham has to provide considerable new commercial, industrial and residential space to meet its ambitions. As confidence in the city builds, growth is spilling out from the core into new quarters beyond the ring road.

The city's strengths

A key driver for Birmingham’s transformation is the newly invigorated government structure. The West Midlands Combined Authority (WMCA) covers 21 boroughs and three local enterprise zones, providing a unique opportunity for strategic planning for housing, commercial space and infrastructure.

The WMCA has the largest investment fund (£1.1bn) of any of the combined authorities, but has more limited powers in several key areas; unlike Greater Manchester and Liverpool, it has no strategic planning powers, and cannot form Mayoral Development Corporations. It will also see the benefits of new funding announced in the Autumn Budget to drive the Midlands Engine.

A second devolution deal has been agreed in principle to address local productivity barriers, including £6 million for a housing task force and £250 million for intra-city transport.

Birmingham Airport had its busiest ever year in 2017, carrying over 13 million passengers, and has ambitions to further consolidate its position as a major regional hub by serving up to 20 million passengers a year.

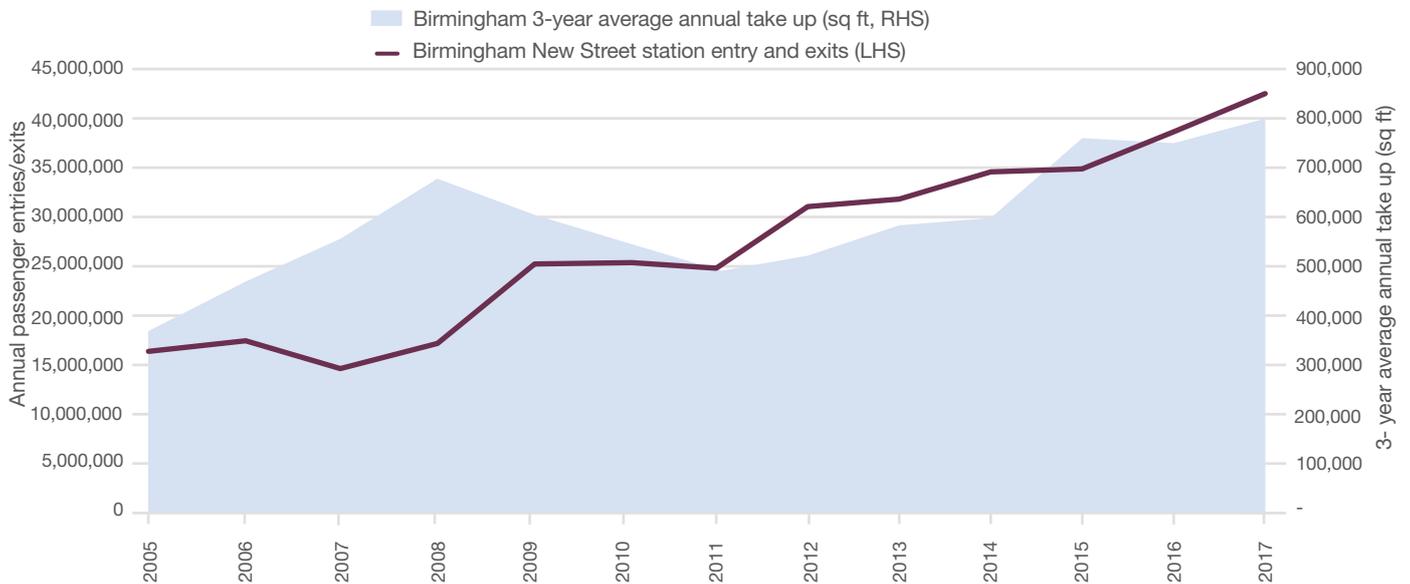
Investment in infrastructure is also having a transformative effect. Shorter travel times to the capital are increasingly encouraging London based occupiers to consider northshoring their functions to the regional cities.

HSBC is on track to relocate over 1,000 jobs from London to Birmingham partially to reduce costs, whilst Deutsche Bank has expanded in Birmingham, with over 2,000 employees now located in the city centre. Three year annual average take up in Birmingham city centre now stands at 799,000 sq ft, 52% above the level recorded five years ago.

The average saving per employee for businesses relocating from Central London to the UK regions is around £10,000 in staff costs and £10,000 in property costs. Housing is also much more affordable, with the average house price 7.2 times the average salary, in comparison to 16.6 times in London.

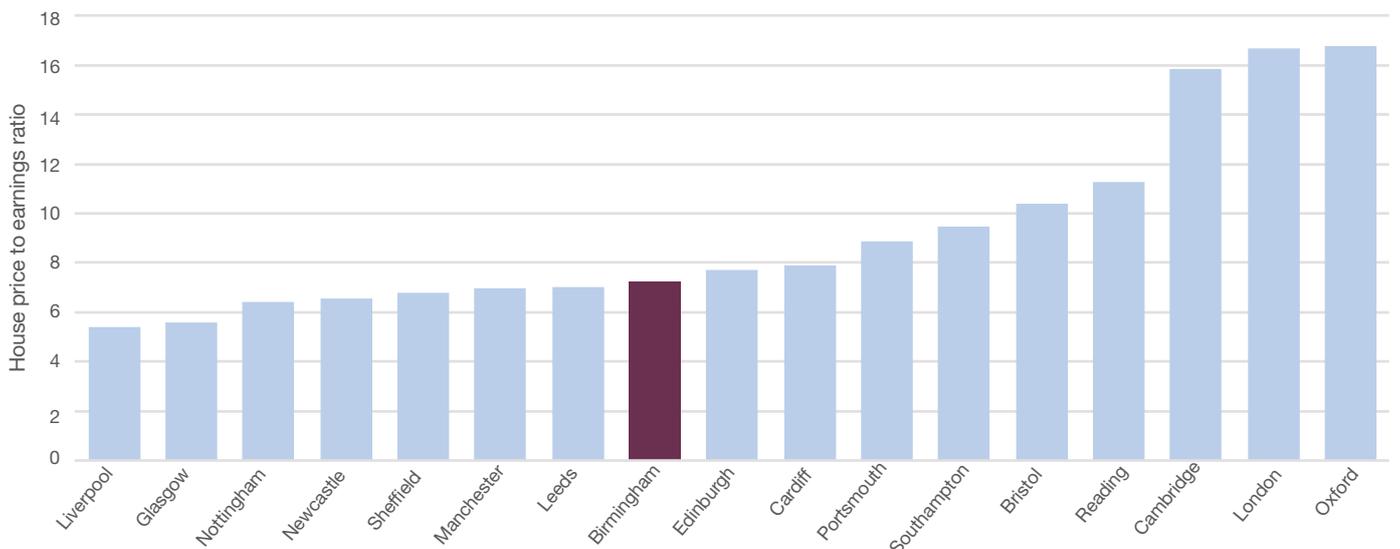


FIGURE 1 Birmingham New Street is now the busiest station outside London. As passenger capacity has increased, so has demand for office space in the city



Source: Savills Research, Office of Rail and Road

FIGURE 2 Housing Affordability Ratio 2016



Source: Centre for Cities

Challenges ahead

The West Midlands was the hardest hit region in England during the Global Financial Crisis. Although it has been rebuilding, with commercial investment in Birmingham reaching £1 billion during 2017, there are still significant challenges. Birmingham is the youngest city in Europe, with 40% of the population under 25. The city currently retains 49% of its students upon graduation, the second highest proportion outside London. However, only 28% of the city’s workforce have a degree, marking the lowest proportion among the major UK cities.

The city therefore needs to keep retaining graduates, and attract skilled workers from elsewhere. The UK Commission for Employment and Skills’ (UKCESS) report shows that the sector with the highest skills gap is engineering and advanced manufacturing at over 7%. With a number of contractors and associated consultants looking to expand in Birmingham off the

back of HS2, and other large infrastructure projects underway, the supply of labour for this sector will become even more stretched. However, the recent let of 47,000 sq ft to WSP at The Mailbox for a new regional headquarters for 700 people suggests that companies are finding ways to fill the skills gap.

Delivering the transformation

There is undeniably a huge amount of brownfield potential; notably, Smithfield Market, the largest regeneration site in Europe. These schemes are becoming increasingly viable, thanks to strong house price growth of 31% over the past five years. There are over 6,500 residential units under construction, and a further 14,700 in planning.

The city needs to continue to identify a variety of sites, and ensure that development is supported by infrastructure to connect housing to employment hubs. ■

Pushing the boundaries of the city centre

Opportunities exist outside of the traditional core

With mixed use city centre regeneration schemes including Arena Central and Paradise both underway, Birmingham's traditional office core is expanding to previously fringe areas. Innovation and flexibility in funding, tenure and design is bringing forward complex sites, resulting in the highest level of construction activity since the Global Financial Crisis.

Shifting focus

Strong commercial occupier requirements combined with a shortage of developable sites in the traditional core has encouraged developers to look beyond the former inner ring road and into previously fringe areas. The redevelopment at New Street station has improved access to the west of the station, supporting growth at Brindleyplace and Arena Central.

The first phase of 1.8 million sq ft of mixed use development is currently underway at Paradise, of which PwC have pre-let 150,000 sq ft of office space. Arena Central will also provide 670,000 sq ft of office space when fully developed, of which the UK Government pre-let 240,000 sq ft at 3 Arena Central, whilst HSBC signed for 212,000 sq ft at 1 Centenary Square. Nearer the traditional core, Ballymore's 420,000 sq ft scheme at Three Snowhill shows significant confidence in the Birmingham market, and is expected to complete during Q1 2019.

Growth beyond the city core is likely to continue over the coming decade, shifting both to the east and west of the city. The Axis redevelopment proposals are for up to 1 million sq ft adjoining Arena Central. The Birmingham Curzon Masterplan, supported by the arrival of HS2 anticipated the delivery of 4,000 new homes and 6.5 million sq ft of employment space. Within the masterplan area, there are several enterprise zone sites, particularly in Digbeth, where a tech and creative hub is emerging. Further out, the link between the city centre and Birmingham Airport will be a key corridor for growth.

New entrants in the residential market

Residential development in the city centre is also diversifying. It has not traditionally been an area of focus for the major housebuilders. But more specialist developers are looking to Birmingham as the market slows in London, such as Berkeley and Galliard. The result of this influx of these developers and institutional funders to the city centre is that local and regional developers are looking for opportunities beyond the city centre. With many housing associations looking to begin delivering new homes for market sale alongside affordable housing, there is potential for further expansion.

Developers are also looking beyond the open market sale model; there are 12 build to rent schemes currently in the pipeline. A variety of tenures on offer can increase absorption rates and help those struggling with affordability pressures. But this means build to rent developers cannot just target the top end of the market. There is a need for good quality, affordably priced stock suitable for young professionals and families. Delivering this type of stock will require funding with a focus on longer term income returns rather short term recycling of capital. ■



2 million sq ft

of office space converted to alternative uses since 2013



603,000 sq ft

of speculative commercial space under construction



1,800

Build to Rent units under construction



21,200

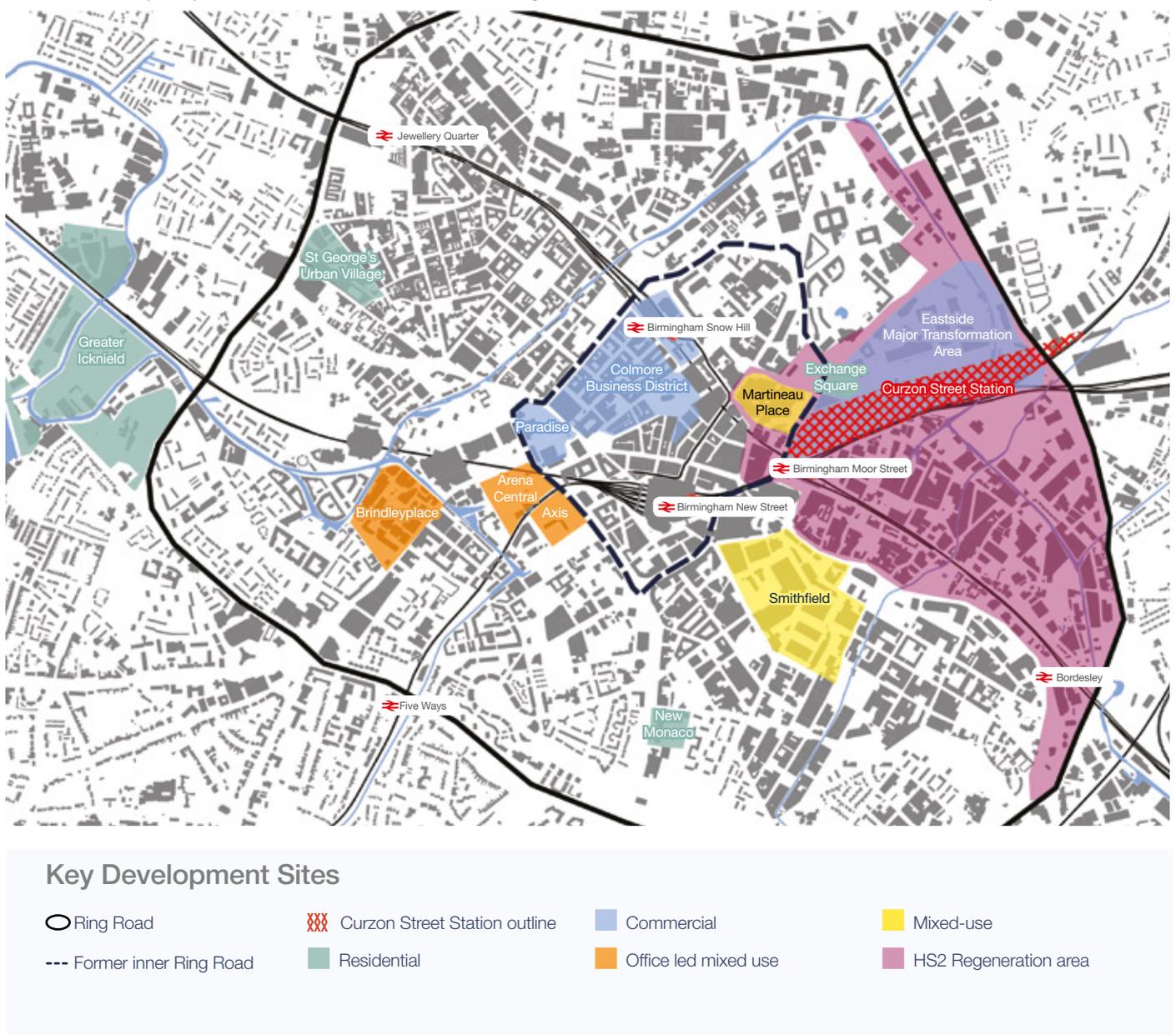
residential units in planning or under construction

Birmingham's ambition At 420,000 sq ft, Three Snowhill demonstrates the depth of confidence in the Birmingham market.

Strong commercial occupier demand has encouraged developers to look beyond the traditional core.

Average residential values have grown by 31% over the last five years, improving viability for complex sites.

FIGURE 3 Many key development sites in Birmingham are located in new areas of the city



Source: Savills Research

Demand from competing uses

There is strong pressure on land for both residential and commercial development in the city

The demand for homes

In line with Birmingham's economic renaissance, there is increasing demand for housing. Birmingham's population is projected to grow by 150,000 (13.7%) by 2031.

The current Strategic Housing Market Assessment (SHMA) sets annual housing need at 4,057 new homes per annum, although the adopted target in the local plan is significantly lower at only 2,550 new homes per annum. Delivery in the year to March 2017 was still well short of this reduced target, at 1,750.

It's not just in the overall numbers where delivery falls short. According to the 2013 SHMA, 38% of newly arising households need Affordable Housing, with the vast majority requiring homes for Affordable Rent. Although the balance of delivery of affordable housing was weighted towards Affordable Rent, overall affordable delivery only accounted for 20% of all new build completions.

What size?

It is also questionable whether the right mix of property types is being delivered. 54% of housing need is for three and four bedroom homes.

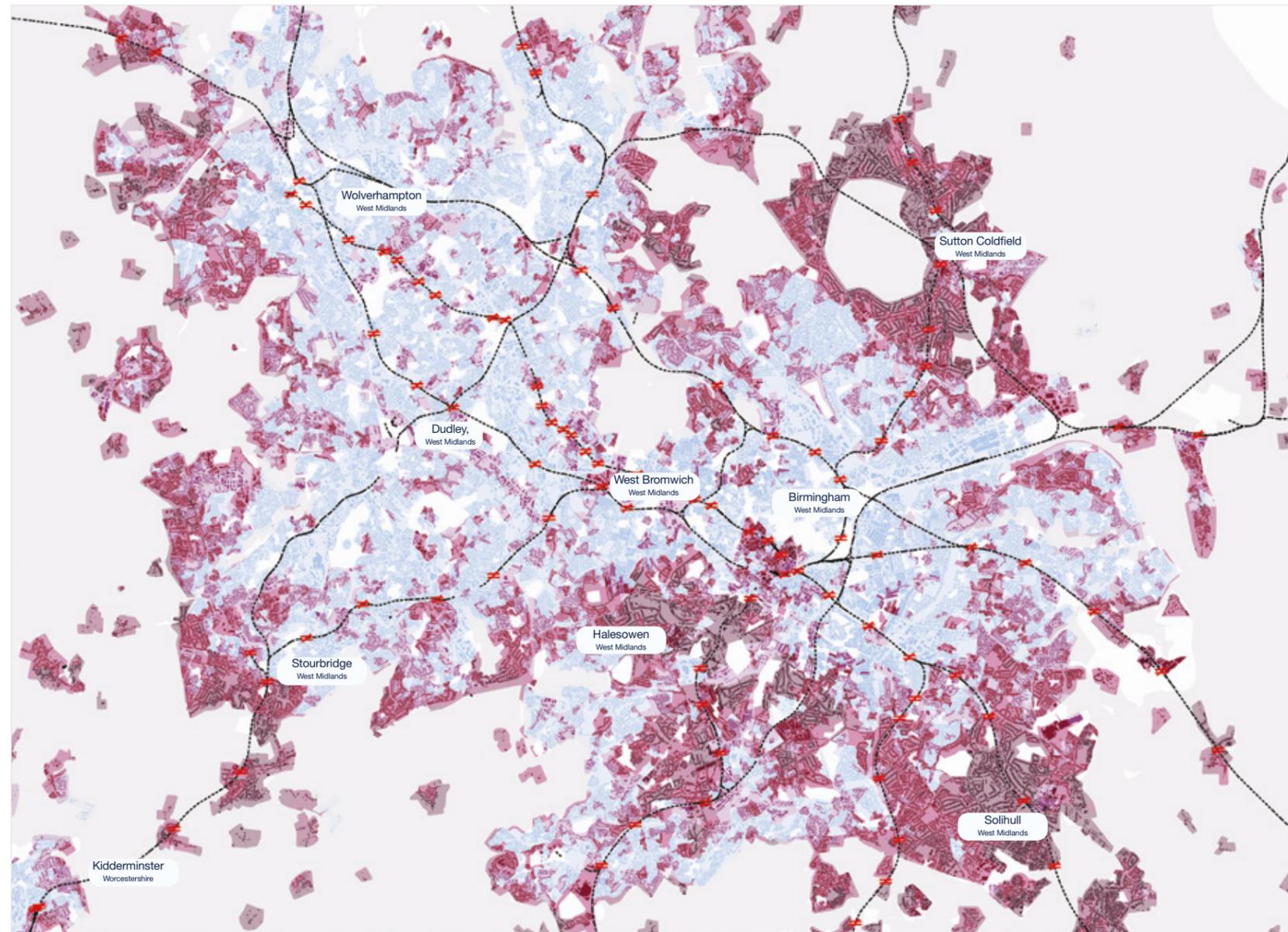
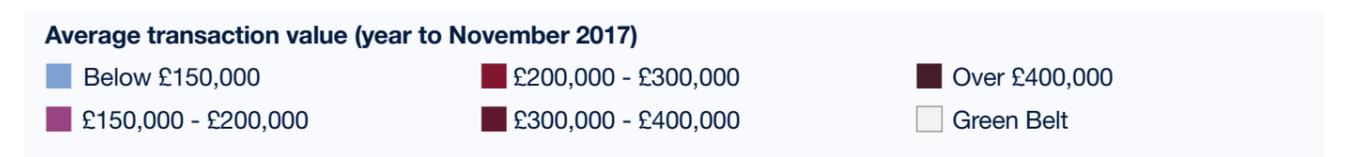
While we don't have data on the breakdown of new homes by number of bedrooms, the distribution of new build property by floor space shows that 62% of new build sales in 2016 were properties of under 700 sq ft – suggesting that most new stock is one and two bedroom flats, rather than the family housing that is required.

This may be a consequence of the challenges of developing in the city centre, where sites require higher densities to be viable.

This underlines the importance of not just concentrating housing delivery in the city centre, but also allocating sites for housing in more suburban locations.

Industrial rents in well connected areas are outperforming the national growth rate of 2.5% per annum

FIGURE 4 Average residential transaction values



Source: Savills Research

The recent release of greenbelt land for 6,000 homes at Langley is a positive step. But it will also be necessary for the surrounding local authorities to absorb overspill demand, particularly for family housing. To open up new sites, it will be crucial for the WMCA to continue to invest in the Metro rail network to maximise the potential of outlying stations. Homes within 2km of stations in the West Midlands have outperformed neighbouring areas by 12-16% over the past five years.

Changing demands for land

The pressure on demand for land is complicated further by Birmingham's position as a hub for nationwide distribution, and as a centre for advanced manufacturing. Robust occupier enquiry levels show demand for industrial and logistics space in the Midlands is strong despite current economic uncertainty, pointing to a positive outlook for 2018 for the sector.

Those holding strategic land positions and able to deliver well located speculative schemes or build-to-suit options will continue to reap the rewards as overall demand outweighs supply.

The key driver of the location of logistics schemes is access to the national road network. Historic industrial land allocations that are more centrally located and linked to the canal network may no longer be suitable.

Consequently, industrial rents in well-connected areas such as the M42 corridor are outperforming the national growth rate of 2.5% per annum, and are expected to reach £7 per sq ft in 2018.

Similarly, sites developed in the 1980s and 1990s are not on the scale required for modern day use. Big sheds remain the preferred choice of new development, and occupiers are particularly looking for increased eaves heights and yard depths.

However, more small and medium sized stock of between 30,000 sq ft and 80,000 sq ft is still needed closer to the city centre thanks to the rise of e-commerce and demand for 'last mile' delivery hubs. ■

WEST MIDLANDS VIEW

Birmingham's prime office yields remain at 4.75%, in line with the prime regional average. In an income driven environment, prime yields remain attractive against West End (3.25%) and City offices (4%). We expect yields to hold firm throughout 2018 as overseas investors become increasingly open to looking outside London to the regional cities.

In the residential market, we forecast growth will be subdued in 2018, but will pick up in line with improving consumer confidence as the UK's future relationship with the EU becomes clearer. 5-year growth will be in line with the UK average, outperforming London and the South East. ■

FIGURE 5 Residential forecasts

	2018	2019	2020	2021	2022	5-year compound growth
United Kingdom	1.0%	2.5%	5.0%	2.5%	2.5%	14.2%
West Midlands	1.0%	3.0%	5.0%	2.5%	3.0%	14.8%

Source: Savills Research

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