Positive rental growth across all grades

- Occupational demand surpassed pre-downturn levels last year with annual take-up of just over 708,000 sq ft helped by improving corporate confidence. This was accompanied by a small annual increase in the vacancy rate to 13.1%, however, it remains far lower than that reported in 2007/8.

- This positive occupational demand continued into the first quarter of 2015 with take-up 26.4% higher than the same period in 2014, totalling just over 129,000 sq ft.

- In line with this improved demand, 2014 reported increases in both top rents and the Grade A average of 7.1% and 6.6% respectively, with a positive outlook for all grades of space over the next five years. A further 3.3% growth in top rents is expected by the end of 2015. Longer term forecasts point to average annual growth of 2.8% per annum.

- Availability constraints for good quality stock, which show no signs of abating in the immediate future, will be a key driver of this uplift; this is enhancing the attraction of refurbishment opportunities due to the speed to market they offer.

- Lack of grade A space has seen occupiers take refurbished space in key locations at rents very close to those seen for new build. This is demonstrated by the squeezing of the Grade A/Grade B rental differential, which has come in from 78.1% in 2011 to 28.2% in Q115. With the development pipeline to remain constrained over the next two years, there is a strong rental uplift story for asset management opportunities, particularly in core areas. The extensive refurbishment of 55 Colmore Row by IM Properties, which will deliver 165,000 sq ft of Grade A accommodation in 2016, is a good example of this.

- As well as facilitating refurbishment, the return of rental growth is aiding the reactivation of developments with approximately 900,000 sq ft of new space forecast to be delivered to the market in 2018.

- While 2014 take-up was back in line with 2008 levels, there was a marked difference in the source of occupational demand. Graph 3 compares take-up by sector in 2008 and 2014. While Banking and Professional Services dominated during the previous peak it were Public Services, Education & Health occupiers who dominated in 2014 accounting for 28.7% of take-up. This included the NHS Trust taking c54,000 sq ft and Birmingham City University c34,500 sq ft, albeit outside the core.

- However, we expect this to change. The recent c210,000 sq ft HSBC deal at Two Arena Central is likely to lead to additional banking requirements. The return in banking demand is already making itself felt in the Prime Core where it has accounted for 22.6% of total take-up since early 2014 (Graph 4).
TABLE 1

Significant Deals in 2014 and Q115

<table>
<thead>
<tr>
<th>Tenant</th>
<th>Address</th>
<th>Grade</th>
<th>Date</th>
<th>Floorspace (sq ft)</th>
<th>Rent £per sq ft</th>
<th>Lessor</th>
</tr>
</thead>
<tbody>
<tr>
<td>Michael Page</td>
<td>4 Brindleyplace</td>
<td>A</td>
<td>Mar-15</td>
<td>15,960</td>
<td>£25.00</td>
<td>Hines/Moorfield</td>
</tr>
<tr>
<td>HS2</td>
<td>Two Snowhill</td>
<td>A</td>
<td>Dec-14</td>
<td>97,958</td>
<td>£29.00</td>
<td>Hines/Ballymore</td>
</tr>
<tr>
<td>BDO</td>
<td>Two Snowhill</td>
<td>A</td>
<td>Dec-14</td>
<td>24,307</td>
<td>£30.00</td>
<td>Wragge Lawrence Graham</td>
</tr>
<tr>
<td>HSBC</td>
<td>120 Edmund Street</td>
<td>A</td>
<td>Oct-14</td>
<td>37,530</td>
<td>£20.00</td>
<td>M&amp;G</td>
</tr>
<tr>
<td>Vodafone</td>
<td>Colmore Plaza</td>
<td>A</td>
<td>Aug-14</td>
<td>22,924</td>
<td>£27.50</td>
<td>Carlyle</td>
</tr>
</tbody>
</table>

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