UK Commercial – June 2020

MARKET IN MINUTES

Savills Research

UK Regional Office Investment Market Watch

savills

Yields shift outwards due to COVID-19

Office investment volumes reached £1.3 billion outside of central London in Q1 2020, which was a 24% increase in volumes recorded in Q1 2019 although 15% below the long term average. Notable transactions in Q1 2020 included Frasers Property buying Lakeshore, Bedfont Lakes for £135 million, CapitaLand buying Arlington Business Park, Reading for £129 million and Citi Private Bank acquiring 300 Capability Green, Luton for £62 million.

The initial impact of the coronavirus pandemic resulted in a rise of sale and leaseback activity with certain occupiers seeking to raise capital. There has been an element of investor caution which has resulted in the overall prime regional office yield moving out by 25 basis points to 5.00%.

There is however still good demand for prime and long income assets and we expect prime yields to move back to their previous position once the lockdown restrictions are fully lifted. The caution amongst investors has weakened immediate demand for value add opportunities and therefore secondary yields have also moved out, notably by 50 basis points in the M25, Leeds and Bristol. The regional office market is still proving attractive to investors, Savills estimate there is £10.45 billion of capital which is seeking to invest in the UK regional office market highlighting the appeal of the market.

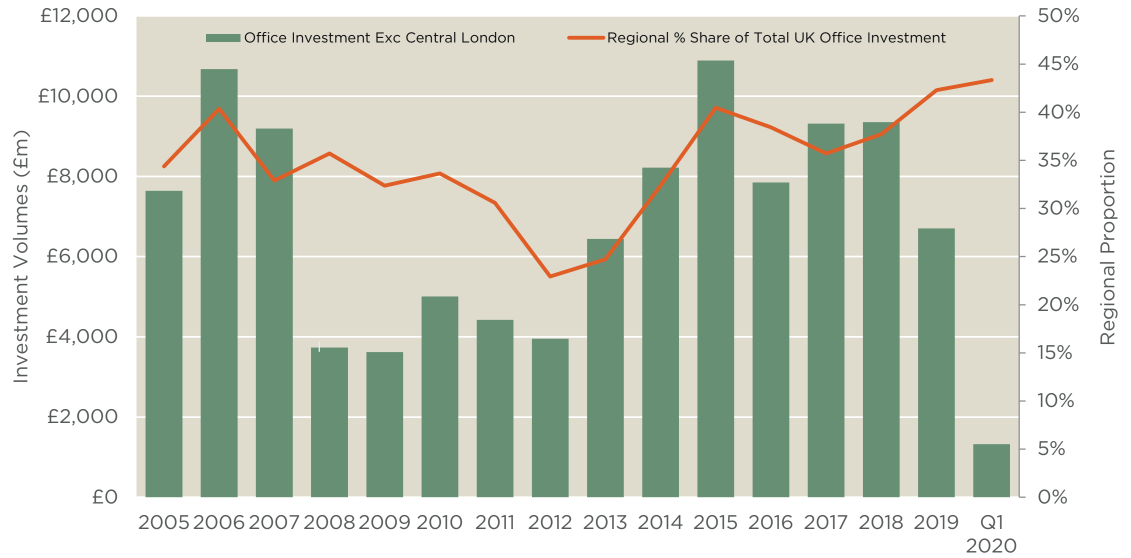
Regional Office Yields May 2020

	Prime	Secondary*	Spread
Aberdeen	6.50%	8.50%	200 bps
Birmingham	5.00%	6.75%	175 bps
Bristol	5.00%	6.75%	175 bps
Cardiff	5.50%	7.00%	150 bps
Edinburgh	5.00%	6.50%	150 bps
Glasgow	5.25%	6.75%	150 bps
Leeds	5.00%	7.25%	225 bps
Manchester	5.00%	6.75%	175 bps
M25	5.25%	7.00%	175bps

Source Savills Research

*Secondary yields refer to buildings in core locations of both a lower quality and rental price point

Office Investment Volumes- Investor demand was strong in Q1 2020 with volumes 24% above the total reached in Q1 2019

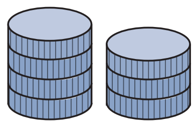


Source Property Data/Savills

Key Stats

5.00%

Prime regional office yield



£1.3bn

Office investment volumes outside of central London in Q1 2020

43% of office investment in the UK was outside of central London in Q1 2020.

The regional office market has the highest forecast rental growth in the UK property market

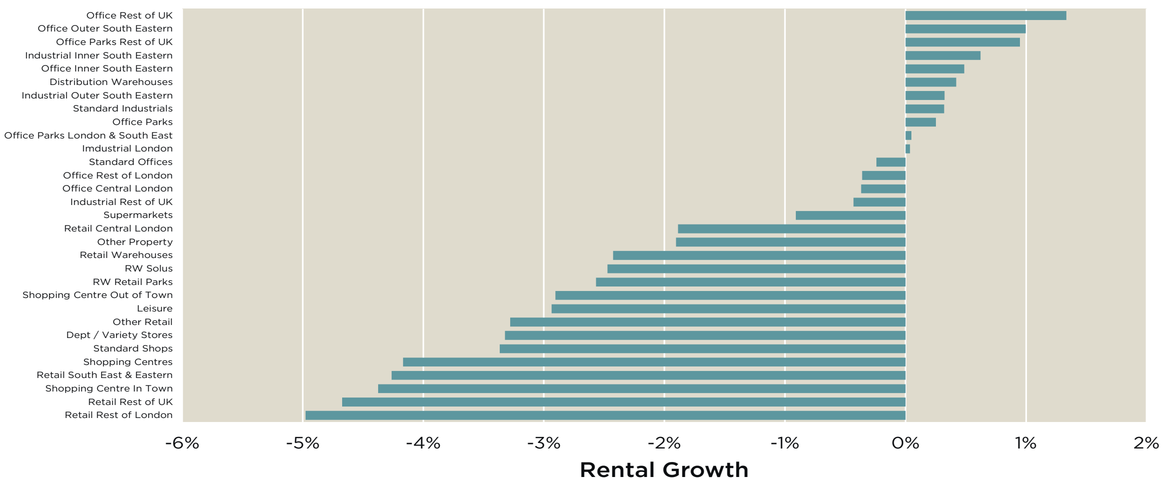
The lack of supply in both the Greater London & South East and Regional City office markets continued in Q1 2020. Total supply in both markets combined is 23.9 million sq ft which is 13% below the five year average. Every core regional city market (Aberdeen, Birmingham, Bristol, Cardiff, Cambridge, Edinburgh, Glasgow, Leeds, Manchester, Oxford) has below two years of grade A supply and 14 submarkets in Greater London & South East have below two years of grade A supply.

The development pipeline is limited and will not alleviate the supply constraints that are present in the market. There is currently 4.48 million sq ft under construction and 56% of this total space in the regional city office market has been pre-let.

Nine of the regional office markets (Bristol, Cambridge, Cardiff, Edinburgh, Glasgow, Leeds, Manchester, Oxford and M25) have a vacancy rate below 10% which Savills classify as undersupplied. The total vacancy rate across the core regional office markets combined is 7.1% which compares favourably to the long term average of 10%. Savills have produced vacancy rate forecasts which underline the robust nature of the market.

The strong occupational market fundamentals are highlighted by the rental growth forecasts recently published by RealFor. The Rest of UK Office property segment of the MSCI property index is forecast to have the strongest rental growth at an average 1.3% per annum for the next five years. This is the highest figure when compared to all other segments of the index.

Rental Growth Forecasts Rest of UK offices have the highest average rental growth projections per annum for the next five years.

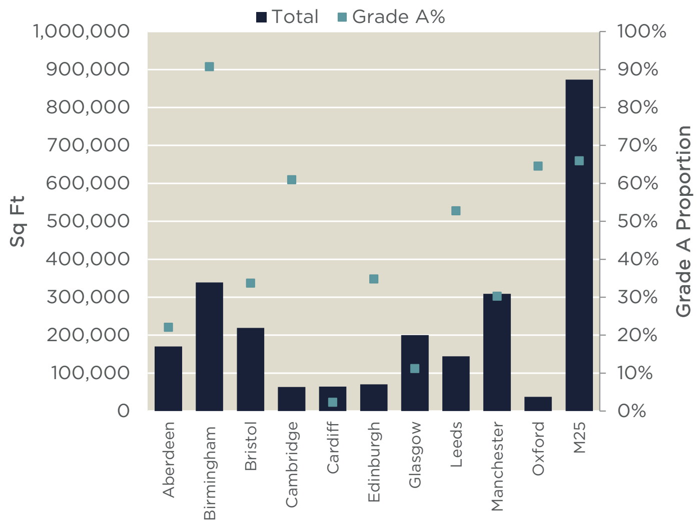


Source: Realfor

At the end of Q1 2020 there was 2.49 million sq ft transacted in the regional office market which was 26% above Q1 2019. This was driven by notable market activity in Birmingham, Glasgow and the M25. The largest ever single building letting was recorded in Birmingham City Centre in Q1 2020 where BT let 283,073 sq ft at 3 Snowhill. GPA (Government Property Agency) pre-let 329,500 sq ft at Buildings 2&3 Ruskin Square, Croydon which was the largest letting recorded across the regional office market in Q1 2020.

Our initial analysis shows that there is still occupier activity in the market despite the coronavirus pandemic. At the end of April, 409,000 sq ft was placed under offer since the lockdown and there is a further 2 million sq ft which was placed under offer before the lockdown and is known to be still progressing.

Regional Office Take-Up Office take-up in the regional office market in Q1 2020 was 26% above Q1 2019



Source Savills Research

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