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Savills Research
UK Commercial

Spotlight
Glasgow office market

Summer 2012

Leasing market supply and demand

■ Occupier demand in the Glasgow office market remains subdued, with take-up in the first half of this year totalling just over 200,000 sq ft. While this points to a full year total that is significantly below the ten year average (Graph 1), it is broadly in line with the five year average for this market.

■ Those tenants that are in the market remain fairly cost-conscious, and while there have been several Grade A lettings in the first six months of this year, the largest being JP Morgan at 141 Bothwell Street, we are noticing more interest amongst tenants in good quality refurbishments.

■ One of the attractions for investors of Glasgow over Edinburgh is its more diverse occupier base, and certainly the City is not over-dependant on one business sector for its tenant demand. Recently there has been a rise in leasing activity from the legal sector (in common with a similar trend in the central London office market), and we expect the legal sector to remain active over the next 12 months.

■ The supply situation has remained broadly stable over the first eight months of 2012, and we estimate that the current availability in the CBD is around 2.2m sq ft (Graph 2). We estimate that less than a quarter of the available office space in the City is of Grade A quality, though this has risen slightly during the first half of 2012 due to second hand returns and the completion of one new scheme (Sixty7).

■ Glasgow's recent development cycle is fairly unique in that there was a degree of speculative development which completed in 2009/10 (the majority of the good accommodation in which has now been let). Since then, in common with all of the UK's other regional cities, the development pipeline in Glasgow is severely restrained. While there are a number of speculative office developments that could start in the next three years, at present the City's speculative development pipeline only consists of two refurbishments totalling 168,000 sq ft between them (George House & 151 St Vincent Street).

Rents

■ While occupiers remain fairly cautious, the last two and half years have seen a slight recovery in prime headline rents in the CBD from their slump in 2009.

■ While rents are yet to return to their peak of nearly £30/sq ft, 2011 and 2012 have seen several lettings at headline rents of £27-£28/sq ft. The most recent prime rental evidence was JP Morgan's acquisition of 19,000 sq ft on Bothwell Street at a headline rent of £27.50/sq ft.

■ Typical rent-free periods on offer for new lettings on a ten year lease in the CBD are around 30-36 months, and this means that the prime net-effective rent stands at £19.25/sq ft.

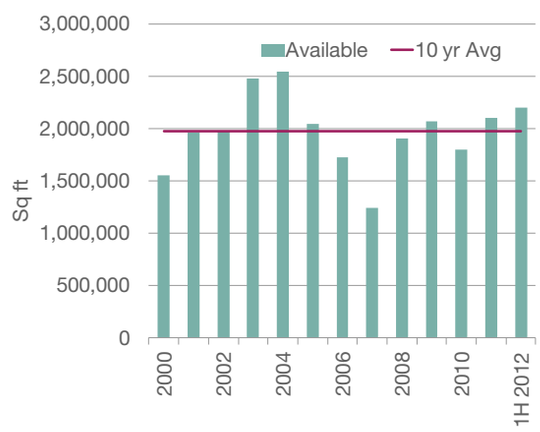
GRAPH 1

1H 2012 take-up remained below trend

Source: Savills

GRAPH 2

Availability is stable



Source: Savills

■ Away from the CBD the rental story is weaker, and we estimate that the prime achievable out-of-town office rents actually fell to £14.50/sq ft in 2011, and have remained at this level in 2012.

Investment market

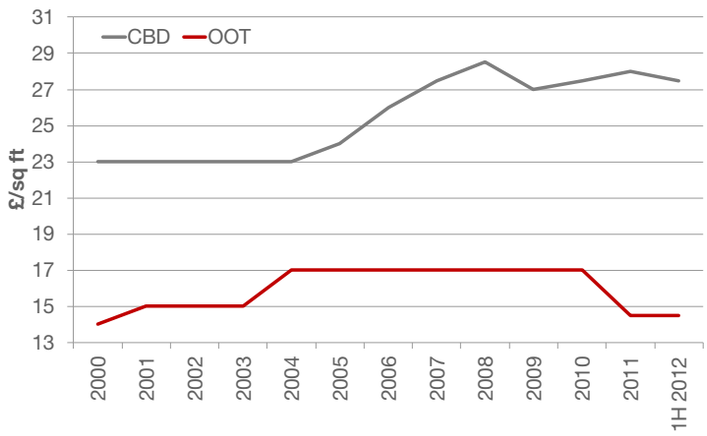
■ Glasgow continues to be one of a handful of UK cities that are of interest to domestic and non-domestic investors alike. This is particularly important at the moment due to the significant non-domestic investor interest in the UK.

■ Non-domestic investor demand is firmly focused on the prime and secure end of the market, with Union's purchase of G1, George Square (advised by Savills) setting the most recent benchmark for yields at the primest end of the market (6.25% NIY). 6.00% to 6.25% is broadly in line with prime yields in the UK's other Tier 1 office markets.

■ Another trend that is common to the whole of the UK is a fairly restrained level of investor demand for Grade B and "value-add" investments (though where such assets are ralistically priced they are finding willing buyers). Recent evidence in the City includes the Tristan Fund's purchase of Cuprum for 8.97%, and we believe there is still the potential for the prime/secondary yield gap to widen before investors start to see the secondary market as underpriced.

GRAPH 3

Prime headline rents in the CBD remain stable



Source: Savills

Outlook

■ The outlook for the Glasgow CBD office market depends heavily on the timing of the return of business optimism. While there is an impending pick-up in lease expiries, as those signed in the late 1990's boom fall in, the current prevailing occupier strategy remains to renew or negotiate a short-term extension.

■ The recovery in tenant demand in the City will be in line with the wider UK economic recovery. However, when this does happen (in mid 2013 on our current forecasts) those tenants who are looking for Grade A offices will return to a market that is relatively undersupplied with such space. We do not expect to see a return of speculative development lending in the foreseeable future. This will mean that the development pipeline in the City will remain severely restrained. Larger tenants will be able to negotiate attractive terms to unlock stalled schemes with a pre-let, but smaller businesses who are looking for prime office space will find themselves in an increasingly competitive market in 2014 and beyond.

■ As the overall, and more specifically the Grade A vacancy rate, start to fall from summer 2013 there will be more upward pressure on both prime headline and net effective rents. Our current forecast for the CBD office market is for £30/sq ft to be achieved by the end of 2015.

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