

Market in Minutes



Yields stable and investment volume past its nadir

The all sector prime yield remained stable last month at 5.21%, which perhaps indicates some stability returning to the investment market as lockdown began to be eased in the UK.

The most notable change in the individual sector prime yields this month is the return of downward arrows that indicate that we believe the outlook might be for yield hardening on West End offices, Industrial Multi-lets and Distribution. These changes reflect a very typical turning point for the commercial property market, with investor interest returning first to those sectors that are perceived as Core.

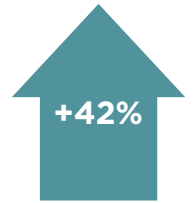
There is also some evidence that we may have passed the nadir of this cycle in terms of investment volumes in May, with June's turnover rising to £1.3bn, compared to £755m in May. While this is a small glimmer of optimism, it has not changed the overall story of Q2 2020 being the weakest quarter on record for investment activity in the UK commercial property market, and we estimate that investment volumes in the first half of 2020 were 43% below the five year average. Only one sector saw higher volumes in Q2 than Q1, and that was high street shops, reflecting a rise in investor interest in foodstores.

Savills prime yields

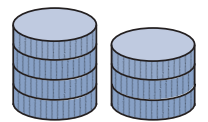
	June 2019	May 2020	June 2020
West End Offices	3.75%	3.75%↑	3.75%↓
City Offices	4.25%	4.00%	4.00%
Offices M25	5.00%	5.25%↑	5.25%↑
Provincial Offices	4.75%	5.00%	5.00%
High Street Retail	5.00%↑	6.00%	6.00%
Shopping centres	5.50%↑	6.50%↑	6.50%↑
Retail Warehouse (open A1)	6.00%	6.75%↑	6.75%↑
Retail Warehouse (restricted)	6.25%	7.00%↑	7.00%↑
Foodstores (OMR)	4.75%	4.50%	4.50%
Ind/ Distribution (OMR)	4.25%	4.50%	4.50%↓
Industrial Multi-lets	4.00%	4.25%	4.25%↓
Leisure Parks	5.50%↑	6.75%↑	6.75%↑
London Leased (core) Hotels	3.75%	4.00%	4.00%↑
Regional Pubs (RPI)	4.50%	4.75%↑	4.75%↑

Source Savills

Key Stats



The change in investment activity between May and June 2020



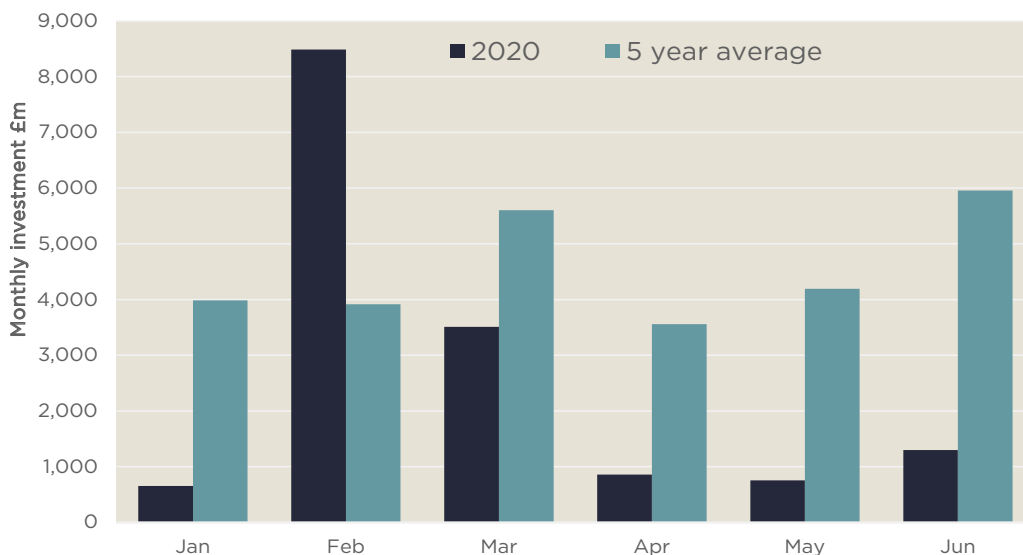
£15.6bn

The total commercial property investment volume in 1H 2020



The number of sectors this month where the forward trajectory for the yield is expected to be a downward movement

Q2 2020 investment volume was the weakest ever quarter, but month-on-month trends showed a marked rise in turnover in June



Source Savills

While GDP will recover in Q3, unemployment will remain a longer-term challenge

The shape of the UK economic recovery is increasingly looking “tick-shaped”, starting with strong quarter-on-quarter growth in Q3 2020, though with 2021 not showing a recovery of the magnitude of the fall that will have been seen in 2020. Consumers and businesses are expected to remain cautious for the remainder of the year, though sentiment surveys are pointing to a slightly stronger than expected start to Q3 at least in terms of output and activity.

While a recovery in GDP growth is imminent, as the chart below shows, unemployment is not expected to return to 2019 levels at any point in the next five

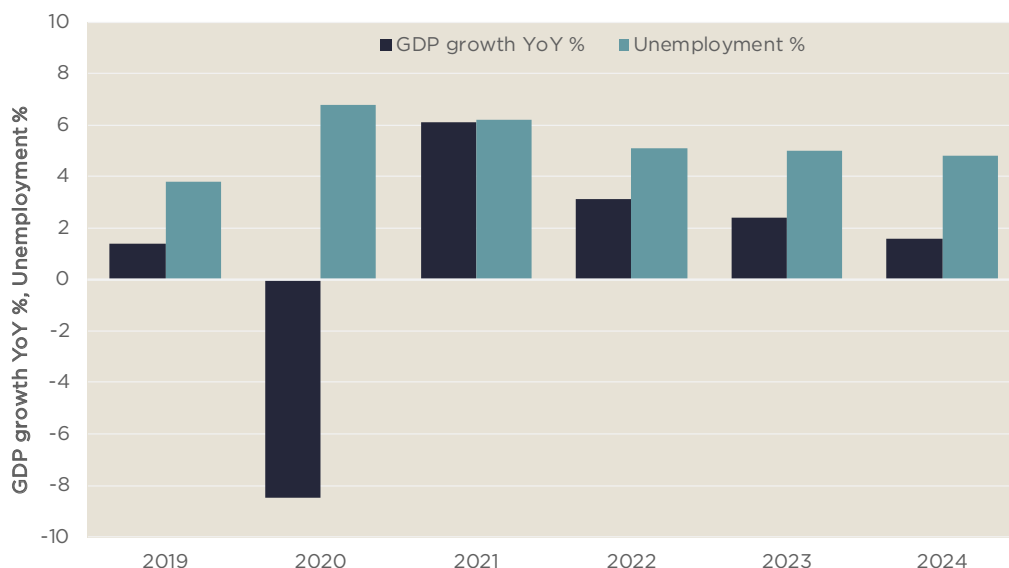
years. While returning to 2019 levels is not essential (indeed many businesses were reporting that difficulties in recruitment were a problem in such a tight labour market), high levels of unemployment do drag on consumer sentiment, boost precautionary saving and hence diminish retail spending.

Given the rash of recent large scale redundancy announcements across the hardest hit industries and the planned end to the government furlough scheme in October, we believe that the risks to the unemployment numbers remain firmly on the downside. Furthermore, the slower that unemployment comes down

the weaker the economic recovery will be.

However, on the positive side some global indicators are pointing to a very sharp recovery in economic activity in parts of the Asia-Pacific region, and if the UK economy were to mirror this pace of recovery then we would expect the outlook for 2021 and beyond to be slightly better than is shown below.

UK unemployment rate may not get back to 2019 levels until 2025



Source Focus Economics, July 2020 consensus view

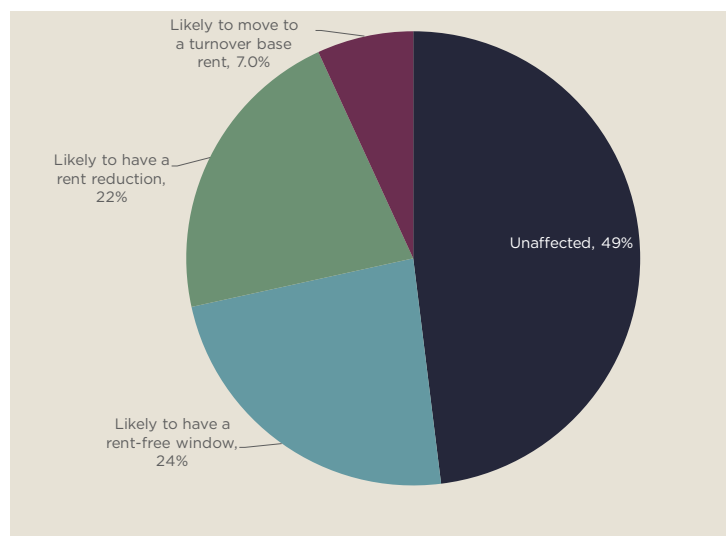
We carried out a nationwide survey of retailers and their landlords in June 2020 to establish what had happened to lease negotiations and how they expected them to move over the remainder of this year.

72% of the retailers who responded to the survey said that they had already approached their landlord for a deferment or a rent-free period on some of their leases. However, landlords expected that almost half of all leases would remain unchanged.

Looking ahead, rent free windows or deferment, are expected to account for around 24% of all lease changes in 2020, while rent reductions would affect 22%.

Interestingly, while there has been much debate around a swing towards more turnover-based leases, the survey results suggested that only 7% of leases would move to some element of turnover linkage.

Retail landlords expect that 7% of leases will move to a turnover base rent in 2020



Source Savills

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