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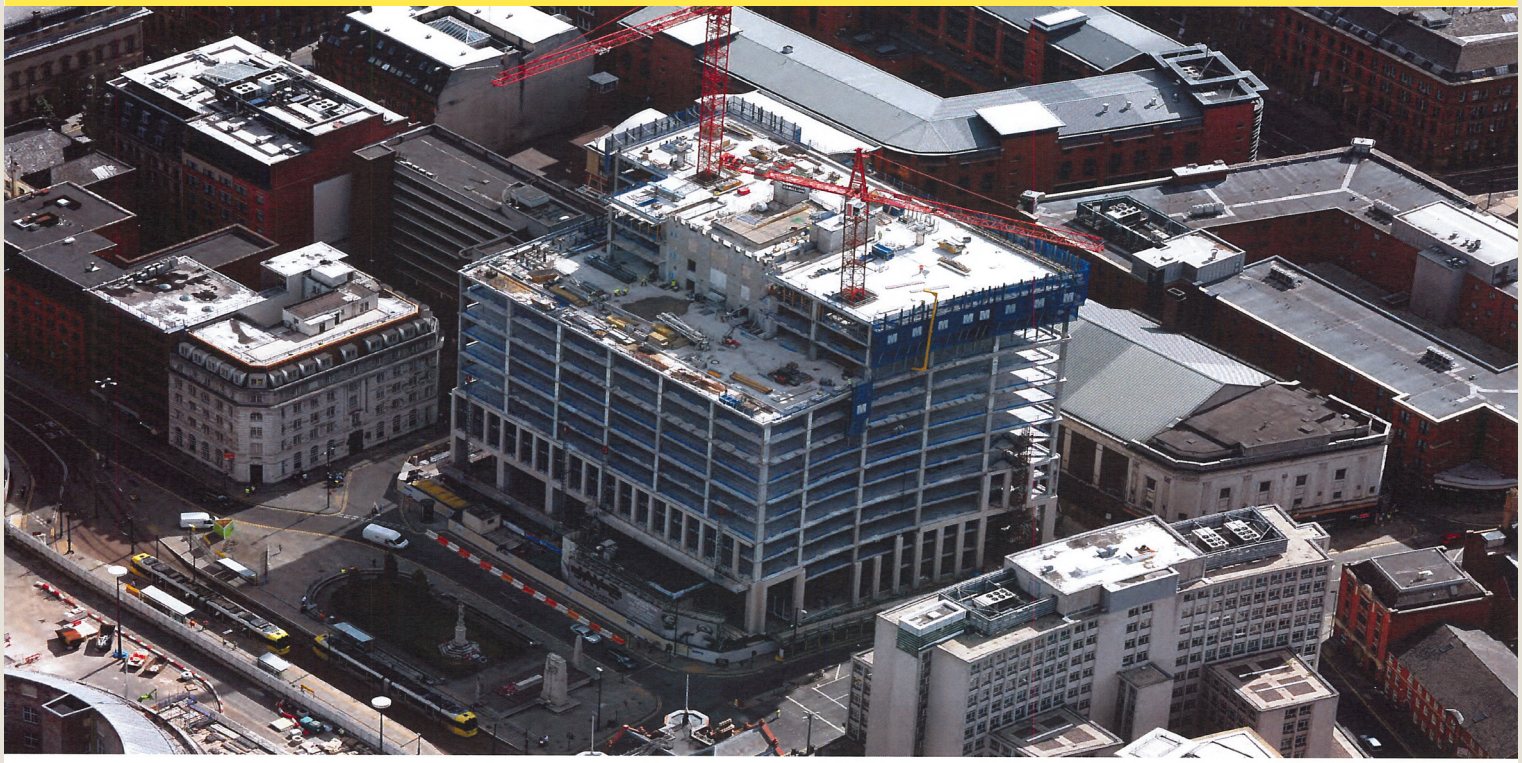
Savills World Research
UK Commercial

Spotlight
Manchester Office Market

September 2013



SUMMARY

■ Take-up for the first half of 2013 at 439,944 sq ft, was up an impressive 43% on the same period last year.

■ Much has been made of the lack of Grade A development stock being delivered within Manchester CBD. less attention has been given to the diminishing availability of large floor plate Grade B stock.

■ The Business & Consumer Services sector remained the most active sector acquiring office space in the City in the first half of 2013 with a 23% share of the market However, the TMT sector accounted for 22% of the total take-up, considerably up on the five years average for this sector (12%).

■ The first half of 2013 has seen a marked rise in investor interest in the UK regional cities, driven by the expectation of an imminent rental recovery, and the record wide yield gap between London and the regions.

"With robust demand and limited new stock coming on line in the next 12 months, we expect rents for high quality, large floorplate, Grade B stock to increase"

James Evans, Director, Office Agency, Manchester

Occupational Market

■ Sir Mervyn King recently described Manchester as having an 'exciting future' ahead, with key drivers of this undoubtedly being the strength of the private sector and the increasing attractiveness of the city region as a business location. Manchester's potential has already been identified by UK companies, with 65 FTSE 100 companies now having a presence in Greater Manchester and around 40% of the North West's Top 500 companies being based in the city.

■ Indeed, Oxford Economics published an interesting regional economic health indicator for the UK regions (Table 1). This indicator, based on a blend of unemployment, house prices, and employment data, shows that after London the North West came second, demonstrating sizeable falls in unemployment and rising earnings, indicating that regional cities outside London, especially the North West, are becoming much more favourable propositions.

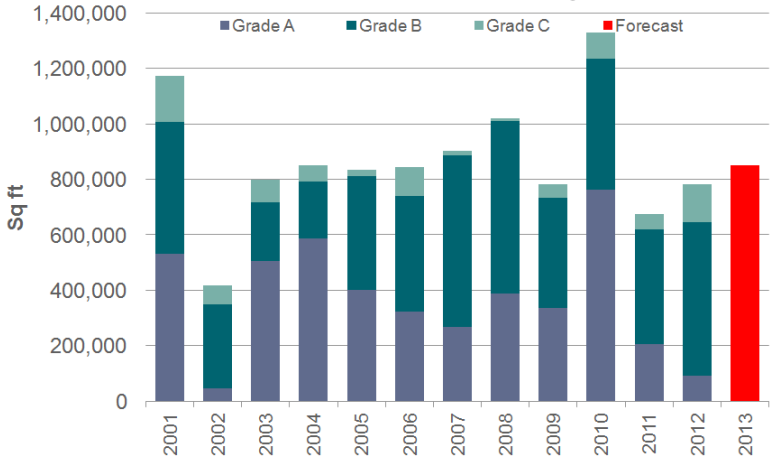
■ Looking into the figures, at 439,944 sq ft, take-up for the first half of the year was an impressive 43% up on the same period last year. With the level of requirements active in the Manchester office market remaining fairly steady throughout the year, 2013 will see a moderate improvement in take-up, but we do not expect to see above average levels of leasing activity until 2014. Notable lease events over the next two to three years, will help inflate take-up figures.

■ However, the next few years will continue to see a rise in austerity-led office moves, with companies looking to achieve great working environments at less than prime rents. Over 80% of take-up in the first half of the year can be attributed to second-hand space. Notable lettings include space taken at Sunlight House and Riverside House over the last twelve months. This trend is set to continue.

■ While there has been a lot of noise about the decreasing Grade A market, less attention has been focused on the diminishing availability of larger Grade B floorplates. Availability of Grade B floorplates has dropped by over 30% in the last 18 months. With

GRAPH 1

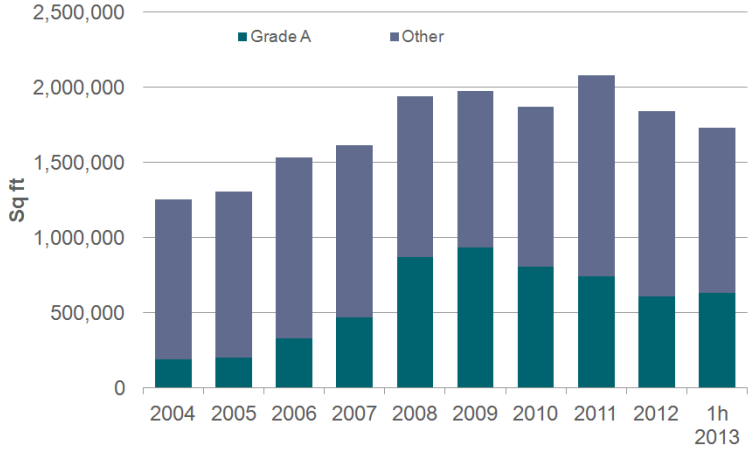
Manchester office take-up is increasing



Source: Savills

GRAPH 2

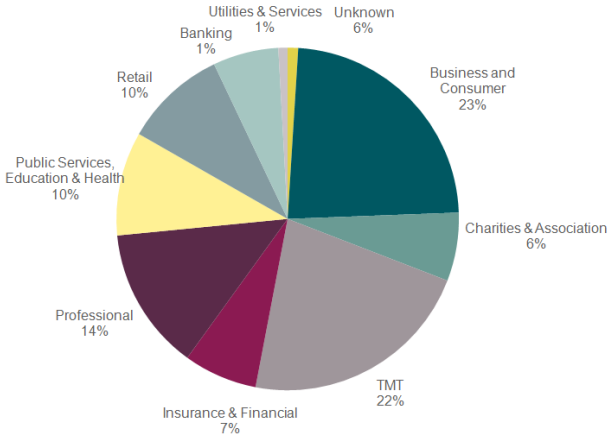
Grade B supply is starting to fall



Source: Savills

GRAPH 3

The TMT sector continues to perform well



Source: Savills

robust demand and limited new stock coming on line in the next 12 months, we expect rents for this type of stock to increase.

■ However, space will start to be released to the market, as businesses begin to trade up, when they reach a lease event. This then begs the question - where will the current tenants move to? With limited large floorplates available at the time of their lease event, this presents a significant opportunity for particular buildings and landlords.

■ Examination of existing occupiers gives us an indication of the type of businesses likely to be attracted to the city. As Graph 3 shows, the Business & Consumer Services sector remained the most active sector acquiring office space in the City in the first half of 2013 with a 23% share of the market.

■ However, the city is strong in a number of sunrise industries that are expected to be the drivers behind growth in the city. The growing TMT sector is one of these, accounting for 22% of the total take-up in the first half of the year, this is considerably up on the five years average (12%) for this sector.

■ The output of the TMT sector in Manchester will grow at an average of 3.8% per annum over the next decade, while the whole city's output will only grow at 3% per annum. Indeed, the TMT sector is forecast to be the fourth fastest growing segment of Manchester's economy. If the forecasts are right then the City will need to accommodate another 1,300 TMT employees over the next decade, which could equate to a need for an additional 140,000 sq ft of space for this sector.

■ £30 per sq ft was the highest rent achieved in Manchester in the first half of 2013. Grade A availability will continue to fall, and we expect to see upward pressure on rents, with rents at St Peter's Square (see front) being the next building to promote rental growth.

Investment Market

■ The first half of 2013 has seen a marked rise in investor interest from UK Institutions, Property Companies as well as overseas Opportunity Funds in the UK regional cities, driven by the expectation of an imminent rental recovery, and the record wide yield gap between London and the regions.

■ With a lack of prime stock available to occupiers and the pent up demand implied by upcoming lease breaks, this is leading investors to take on well-located secondary stock in need of refurbishment and asset management opportunities. Quality secondary stock at attractive prices with "Value-add" opportunities are rising in popularity.

■ With an increased weight of money looking at the regions, coupled with a lack of prime stock, we anticipate that prime office yields will harden to 6% and below.

Expert view

James Evans, Director of Leasing in Manchester, looks behind the statistics

With summer behind us, attention returns to market performance and what the remainder of 2013 holds for Manchester. Traditionally a quiet time, August has in fact witnessed a relatively higher level of both enquiries and inspections.

Surprisingly, not only have a number of large requirements moved forward, but a number have also been resurrected. Furthermore there has been a marked increase in the number of conversations involving the magic word, "growth". We should not see this as a return to a strong market but a genuine indicator of business confidence.

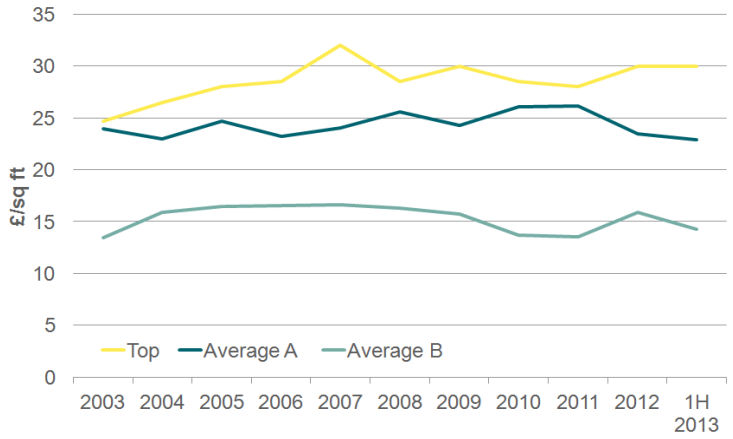
We anticipate this will filter through to take up statistics by year end. This will lead to opportunities in the market, in particular, the much talked about Grade A market will now start to see the impact of a limited supply pool.

In addition to this, a constrained supply of large floorplate, Grade B stock will see opportunities for landlords who can position themselves accordingly. Unfortunately, we anticipate the smaller floorplate market to remain challenging, albeit not as tough as the last two years.

However, there are opportunities in the smaller end of the market, in particular for those landlords who can be fleet of foot and offer flexible terms and specifically where tenants can agree mechanisms whereby growth can be accommodated. Innovative terms will see occupiers commit now as opposed to sitting on their hands for even longer!

GRAPH 4

Manchester's strong private sector will help the city return to rental growth



Source: Savills

TABLE 1

Economic Indicator

Rank	Region
1	London
2	North West
3	South West
4=	South East
4=	West Midlands
6	Scotland
7	Yorkshire & Humber
8	North East
9	East Midlands
10	Wales

Source: Oxford Economics

■ Following on from the sale of One Angle Square for £142m, the most significant deals to complete so far this year are 100 Barbirolli Square for £41m and Bauhaus for £16.25m. Both of these deals represent a move up the risk curve towards fundamentally good, well located assets, with shorter leases and future refurbishment plans.

■ However, the availability of debt for the more secondary deals will determine the scale of this activity. Savills has seen increasing life in the lending market with money available for the 'right' investment. Yet caution prevails with the banks, which may push secondary/tertiary yields out further.

Outlook

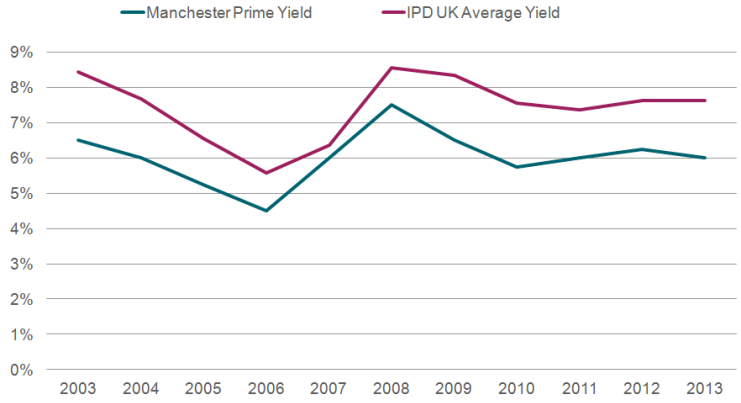
■ We believe the key to leasing success, in the current environment, will be attention to detail and differentiation. Grade A stock will continue to become increasingly sparse, with the rise of refurbishment market going some way to fill the gap.

■ Landlords are now in a position to capitalise on their investment if the refurbishment is done correctly Our recent What Workers Want survey, concluded that 69% of respondents who work in an office with a less corporate/traditional fit-out noted a positive impact on productivity, suggesting that delivering an office design employees want and therefore a place people want to work, may help boost the bottom line.

■ Buildings which can not differentiate will be left behind. Manchester benefits from a host of quality buildings, however the burgeoning TMT sector very often want unconventional space and very often on unconventional terms. Landlords, along with their buildings, will need to evolve to capture such tenants. Equally more traditional stock must provide leasing terms that allows tenants to move now but provide "up sizing" opportunity to accommodate potential growth in the early stages of an economic recovery.

GRAPH 5

Prime yields have continued to harden



Source: Savills /IPD

Property criteria	Transactions and supply recorded for units in excess of 1,000 sq ft.
Study area	City centre as broadly delineated by the inner ring road.
Top rent	Highest rent achieved in one of more transactions during given period.
Grade A	All new development (including speculative schemes reaching practical completion within six months, plus major refurbishments).
Grade B	Space previously occupied, completed or refurbished in last 10 years.
Grade C	Space previously occupied, completed or refurbished more than 10 years ago.

Savills Manchester Office Agency & Investment

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