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Savills World Research
UK Commercial

Spotlight
Birmingham Offices

Autumn 2017

After recent successes, 55 Colmore Row, above provides 54,360 sq ft of available prime Grade A office space

■ With Q3 2017 take up exceeding 400,000 sq ft and over 160,000 sq ft of other known deals under offer, we expect take up to exceed 850,000 sq ft by the end of the year, 20% above the 10 year annual average.

■ There remains a limited supply of prime Grade A space, which currently stands at 187,350 sq ft. With no new speculative developments scheduled to complete until Three Snowhill and 1&2 Chamberlain Square in 2019, competition for the best quality space will intensify.

■ Top rents in the city are £33 per sq ft and we expect the delivery of new speculative space to achieve in excess of £34 per sq ft by the end of 2019.

■ Office investment volumes in Birmingham reached £408m as at end Q3 2017, 2% above the 10 year annual average of £400m. However, the round-trip costs of buying and selling have discouraged landlords from disposing of assets in an income driven environment.

"Flexibility of lease term has grown to become a key requirement for many occupiers and landlords have adapted to embrace this." Ben Thacker, Director, Office Agency, Birmingham

Large scale urban regeneration, inward investment and key infrastructure projects are driving occupier interest in Birmingham city centre.

Unemployment has continued to fall

Strong growth in the number of people in work has seen the unemployment rate fall to 4.3%- the lowest level since May 1975. However, subdued annual wage growth of 2.1% coupled with CPI inflation rising to 2.9% has meant that real wages are continuing to fall.

Lower real wage growth has continued to boost employer sentiment. Employer sentiment provides an indication of future office demand, as we have seen across the UK regions since the EU referendum. Of the FTSE 100 CFOs surveyed by Deloitte at end Q2 2017, 9% expected to increase hiring over the next 12 months, a marked increase on the 1% recorded immediately post Brexit.

Whereas decision makers sat on their hands during the second half of 2016, occupiers have realised that "Brexit" is a process, not an event and occupational decisions must continue to be made. Nearly six months on from triggering Article 50, the self imposed deadline of March 2019 to leave the EU is rapidly approaching.

According to the Lloyds Bank Regional PMI Index, the West Midlands showed the strongest output and employment growth of all UK regions in August 2017, reaching 58.6, up from 56.7 during the previous month. Any figure above 50 indicates positive growth.

HS2 contracts, and the financial sector will drive larger deals

Birmingham's office take up over 1,000 sq ft reached 639,000 sq ft as at Q3 2017, 2% above the 10 year annual average of 627,000 sq ft. However, with around 160,000 sq ft of space currently under offer, we expect take up to exceed 850,000 sq ft by the end of the year, 36% above the 10 year annual average (Graph 1).

The GPU (Government Property Unit) announced HMRC's long anticipated 240,000 sq ft move to 3 Arena Central during the third quarter, which is being forward funded by L&G. Further GPU requirements are also in the pipeline for the next five years as departments including Ministry of Justice and DWP also seek to consolidate and upgrade their operational portfolios in line with government strategy.

Birmingham remains well shielded to Brexit, with sustained office requirements arriving from direct Hs2 contracts and the associated supply chain. The serviced office sector took 82,000 sq ft of space as at end Q3 2017, the strongest year on record. Co-working operator ihub signed for 18,000 sq ft at Colmore Gate, whilst landlord CEG have taken the initiative to open their own co-working serviced office business Alpha Works at their landmark refurbished Alpha tower scheme in a bid to support the city's growing number of start-ups and small businesses.

Top city centre office rent
£33/sq ft

Occupiers are increasingly on the look out for flexible lease terms amid new Hs2 and other infrastructure related contracts, the emerging tech sector and continued uncertainty around the ultimate implications of Brexit.

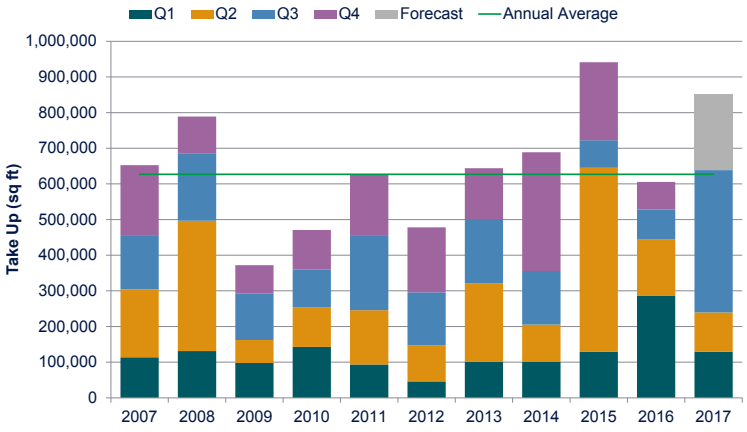
There remains a limited volume of prime Grade A supply which currently stands at 187,350 sq ft and without exception is targeting in excess of £30 per sq ft (Graph 2). With no new speculative developments scheduled to complete until Three Snowhill (420,000 sq ft) and 1&2 Chamberlain Square (232,000 sq ft) in 2019, competition for the best quality space will intensify, creating a positive outlook for well located Grade A product. At current rates of Grade A take up, Savills anticipates a significant proportion of the new space being delivered could be let before completion.

There remains strong demand for IM Properties' 55 Colmore Row, cover image, where just 54,360 sq ft of Prime Grade A space remains. Savills have taken 17,000 sq ft there on the sixth floor and will relocate more than 150 staff in January 2018.

Savills estimate that in the region of two million sq ft of office space has been converted to alternative uses since 2013. In light of this wave of

GRAPH 1

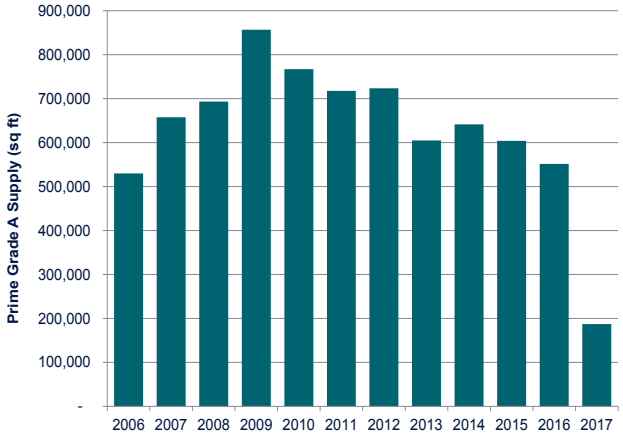
Take-up has exceeded the 10 year average by 2%



Graph source: Savills Research

GRAPH 2

Prime Grade A supply now stands at only 187,350 sq ft



Graph source: Savills Research

conversions to alternate use, there are increasingly fewer repositioning opportunities available on dated existing office buildings to achieve the kind of success enjoyed by Bruntwood at Cornerblock, Cornwall Street where the building has been almost completely let prior to practical completion.

We are seeing Birmingham's expansion over the inner ring road and into previously "fringe" areas. Great Charles Street is now achieving rents in excess of £20 per sq ft, whilst occupiers are now willing to pay in the high £20's per sq ft to be located at the Mailbox, attracted by the unique nature of the scheme, its rail connectivity and amenity offering. This is further supported as the traditional city boundaries to the west expand, helped by the redevelopment of New Street and Argent's redevelopment of Paradise.

The evolution of Westside will also benefit Brindleyplace where the redevelopment of Nine Brindleyplace will provide an additional 30,000 sq ft by the end of Q1 2018, with rents in the mid to late £20s per sq ft, as the area benefits from the Midland Metro tram extension.

Savills What Workers Want survey indicates the factor that workers most wanted to change was the length of commute to work. Creating mixed use environments, where workers can benefit from leisure/amenity provision and transport links after work is essential.

Top rents in the city centre are £33 per sq ft and we expect the delivery of new speculative space to achieve in excess of £34 per sq ft by the end of 2019 (Graph 3).

London cost pressures could increase north shoring

Figures from Oxford Economics indicate that the finance and insurance sector has seen a 3% fall in output per head over the past five years in the City of London, more than any other sector. This has been partly down to banking regulatory reform which has increased headcount, and ultimately, staff cost pressures on the banks. Of the 54,000 net additional office based jobs forecast in Birmingham over the next five years, 30,000 of these are expected to be delivered in Administrative and Support roles, representing growth of 8.6% in this sector.

We have already seen both HSBC and Deutsche Bank relocate over 1,000 roles from Central London and Savills expect more London based companies from the financial and insurance sectors to be weighing up the benefits of north shoring in order to reduce costs going forward. Savills estimate the average savings per employee for businesses relocating from Central London to the UK regions to be £10,000 in staff costs and £10,000 in property costs.

Office investment has already exceeded the annual average

Office investment volumes in Birmingham reached £408m as at end Q3 2017, 2% above the 10 year annual average of £400m. This was largely driven by the £265m Brindleyplace acquisition during the first quarter of the year, the largest regional office transaction this year (Graph 4).

In line with the UK regions, Birmingham's prime office yields have moved in from 5.25% to 5% during the course of 2017. This yield sharpening has been partly driven by overseas investors in search of attractive income outside London for the first time. The spread between prime assets in Birmingham and City of London now stands at 100 basis points.

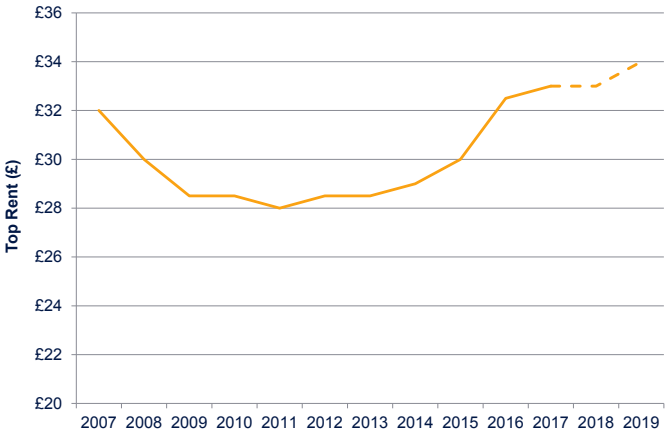
Despite UK institutions having funds to spend, they have been unwilling to meet landlords' valuations. The round-trip costs of buying and selling have also discouraged landlords from disposing of assets.

Property companies have been active during the third quarter of 2017. Kier Property acquired 19 Cornwall Street from Standard Life Investments for £35m, their first purchase in the West Midlands, whilst Longmead Capital acquired 145 Great Charles Street for £13m.

A shortage of on market stock will continue to limit buying opportunities as landlords look to sit on long income. However, we expect 2017 office investment volumes to exceed the £433m recorded during 2016 and yields to remain stable for the rest of 2017.

GRAPH 3

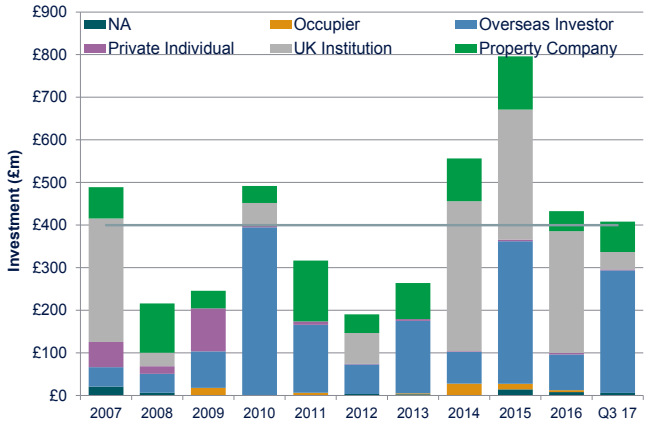
Top rents will continue on an upward trend



Graph source: Savills Research

GRAPH 4

At end Q3 2017, office investment volumes are 2% above the 10 year annual average



Graph source: Property Data

Headline stats, definitions and contacts

8.6%
administrative employment growth over the next five years

7
months worth of Prime Grade A office supply in city centre

652k
office development currently under construction (excluding pre-lets)

£34 per sq ft
Predicted top rents at end 2019

Headline statistics	Take-up: in-town	Take-up: out-of-town	Top rents (£ per sq ft)	Prime yield
Q3 2017	239,000 sq ft	140,000 sq ft	£33	5.00%
End 2017 outlook	↑	↑	↑	→

Property criteria	Transactions and supply recorded for units in excess of 1,000 sq ft.
Top rent	Highest rent achieved in one or more transactions during given period.
Prime Grade A	New and comprehensively redeveloped buildings considered to be located and specified of the highest quality and capable of achieving rents close to the market headline.
Grade A	All other Grade A quality buildings including both new build and 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.

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