

Spotlight Birmingham Offices

March 2017



Three Snowhill, Birmingham. 420,000 sq ft under construction set for delivery in 2019.

■ Take-up in the CBD ended the year at 670,000 sq ft, hitting the five-year average. Birmingham city centre office market was a year of two halves in terms of take-up in 2016 with the first half the best on record.

■ Take up in Solihull/ M42 corridor has started to see a resurgence over the last 12 months.

■ Refurbishments will help 'plug the gap' while the city waits for new developments to complete.

■ Business parks are now looking to create a more appealing offer. Blythe Valley Business Park has listened to the needs of the worker and is creating a desirable mixed-use scheme.

■ The first quarter of 2017 has already seen £300 million transacted in the investment market with the key deal being Brindleyplace.

■ Birmingham office prime equivalent yields currently stand at 5.25% where we expect them to stay during the first half of 2017.

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 "The shortage of existing new Grade A space is facilitating rental growth in prime refurbished stock, closing the gap on existing new build"
 Nick Williams, Director, Office Agency, Birmingham

→ City centre market - a year of two halves

In the last 20 years, Birmingham has experienced massive urban regeneration and inward investment of circa £10 billion with a further £11.4 billion due to be invested by 2026.

With the £600 million redevelopment of Grand Central now complete and the extended Metro link to Grand Central Station now up and running, the city has created a truly integrated transport system.

Birmingham city centre is evolving outwards and the perception of the city's office district has been transformed by this. Occupiers are now looking at locations previously ignored as a business district.

The city centre office market was a year of two halves in terms of take-up in 2016, with the first half being the strongest on record. Although the second half was significantly down in comparison, October saw the market start to gain momentum again. With occupiers taking longer to make decisions, we expect a number of deals from the back end of last year to sign in the first half of 2017.

Take-up ended the year at 670,000 sq ft, hitting the five-year average. With increased demand and strong employment growth forecast in sectors such as tech and professional services, we expect 2017 take-up to reach 750,000 sq ft, 19% above 2016.

Although the bulk of take-up was made up of deals under 10,000 sq ft (68%) there were some notable larger deals including - PwC taking 90,000 sq ft at 1 Chamberlain Square and

Network Rail taking 80,000 sq ft at Baskerville House.

The insurance & financial sectors were the most prevalent sector in 2016, making up 23% of the market. There have also been a number of legal relocations over the last 12 months, including DAC Beachcroft who took 40,000 sq ft in Edgbaston, that markets largest occupational deal for 10 years, and Hill Hofstetter committing to a new 10-year lease at Blythe Valley Park. Pinsent Masons have also taken space in 55 Colmore Row and subsequently followed up with a further acquisition of 16,000 sq ft at 19 Cornwall Street.

Government requirements and HS2 will fuel demand

We anticipate that the year ahead will be fuelled by Government requirements and HS2 related demand.

2017 is likely to see Central Government requirements translate into deals, primarily driven by HMRC's requirement, which totals around 250,000 sq ft, centering around the prime core.

HS2 received Royal assent on 23rd February and this will inevitably be a catalyst for demand for centrally located office space driving further inward investment and recruitment of a new workforce to the region.

While the true benefits of increased connectivity won't be felt until the link is up and running, there will be an immediate impact on the regional economy. This will arise from the placement of construction and

consultancy contracts, related to HS2, within the city. The city has already seen Laing O'Rourke take 11,000 sq ft at 1 Victoria Square in 2016 and we expect engineering firms and consultants - off the back of HS2 - to be a dominant sector going forward.

Grade A supply continues to decrease

With increased demand anticipated this will have a marked impact on supply figures. Although Three Snowhill and Paradise are currently under construction, these schemes will not impact the supply figures until mid-2019.

Major re-developments, such as the much anticipated 55 Colmore Row (160,000 sq ft), Corner Block (112,000 sq ft) and the Lewis Building (110,000 sq ft) will all help bolster the supply as we wait for developments to complete.



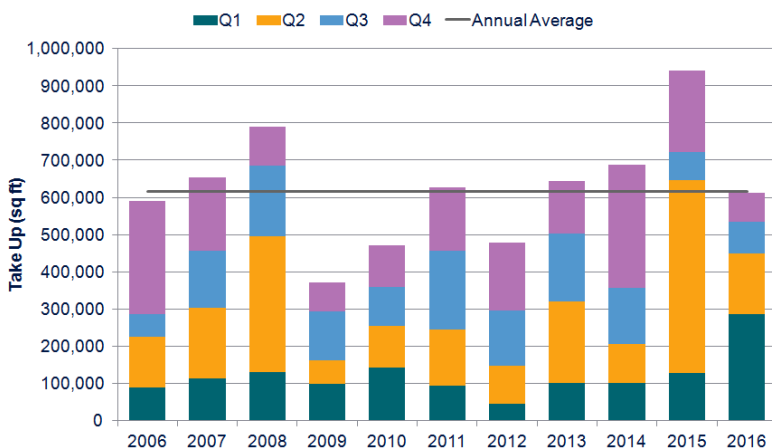
Top city centre office rent
£32.50/sq ft

Out-of-town market picks up pace

Solihull and the M42 corridor has seen a resurgence over the last 12 months. The M42 corridor remains the most significant office market in the West Midlands outside of Birmingham city centre. We expect this to continue to pick up pace and popularity as we go through 2017.

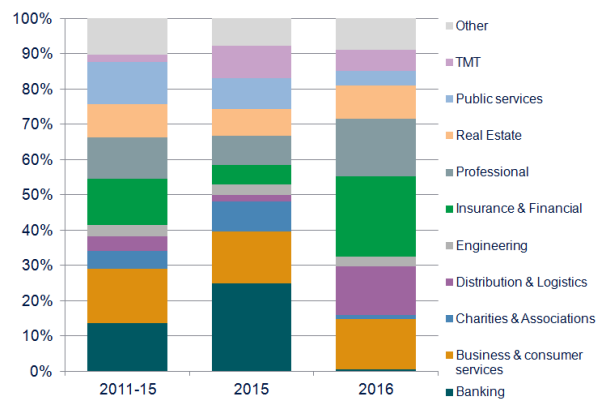
Solihull has benefitted from the infrastructure improvements and growth of Birmingham city centre as an office

GRAPH 1
2016 take-up was a year of two halves



Graph source: Savills Research

GRAPH 2
The insurance & financial sectors dominated take-up in 2016



Graph source: Savills Research

location. While they are two distinct office markets, Birmingham and the out-of-town market have begun to compliment each other. With HS2 connecting the airport, the M42 and the city centre market, we expect this new infrastructure to truly combine these areas.

According to Savills 'What Workers Want' survey, employees want leisure and retail on their doorstep. Blythe Valley Business Park has listened to the needs of the worker and is creating a desirable mixed-use scheme, created by the mix of residential, retail and leisure.

Occupiers are now starting to widen their net and the lines between in-town and out-of-town will become increasingly blurred over the next few years, with certain sectors less concrete in their location preferences. A recent example being ACS (an IT software developer) taking space in Birmingham city centre last year when historically these type of occupiers would have been expected to focus primarily out-of-town.

Although the out-of-town market is experiencing speculative development for the first time in 10-years, there are still supply constraints, in both the city centre and out of town, which will help drive rental increases during 2017. The best space out-of-town has seen a sharp increase in headline rents (16%) between 2015 and 2016 and this is expected to continue as we go through 2017, albeit not as strongly.

Prime rents in Solihull are £23 per sq ft, which is currently at a marked discount to £32.50 per sq ft in Birmingham city centre. This gap is likely to narrow as new build supply

and the development pipelines are restricted in both. We also expect the gap between refurbished and new build rents to reduce as top refurbishments are now hitting £30 per sq ft.

Investment - a strong start to 2017

In terms of investment volumes, Birmingham saw £433 million transacted in 2016. Although this is 46% down on the previous year it is still up 8% on the long-term average.

The first quarter of 2017 has already seen £300 million transacted, with the key deal being Hines and Moorfield's sale of Brindleyplace's 470,000 sq ft office space, purchased by HSBC Alternative Investments for £260 million. This generated a 6% yield. By the end of Q1 we expect almost 80% of the long-term average to have already been transacted.

Looking at investor types, the institutions made up 66% of volumes in 2016. This was heavily swayed by Three Snowhill. Overseas buyers, attracted by the weaker pound, made up 20% of volumes in 2016 and we expect this to increase significantly as we go through 2017.

Birmingham office prime equivalent yields currently stand at 5.25% where we expect them to stay during the first half of 2017.

Lack of stock will be the big issue this year. There will be a number of parties who would like to sell but with limited opportunities to re-buy, may end up stalling. ■

Expert view

Ben Thacker director of Agency in Birmingham provides his insight on the market

The Midlands region is outperforming much of the rest of the UK at present and at the epicentre of this, the spotlight is firmly on Birmingham.

The city has repositioned itself with a renewed sense of self identity and an elevated image on an national and international stage. With office-based employment growing by 3.5% in the next five years (compared to 2.2% in the last five), the retention of almost 50% of its students post-graduation and its place as the number one destination for employee relocations from London are just a few of the factors driving this.

Office demand at the very prime top end of the market continues to recover from the political events in 2016. However, the regional economy is looking strong and the inevitable positive impact of HS2 receiving Royal Assent in February is now starting to be felt. This will be a catalyst to an associated supply chain anticipated to also invest their wider operations in the city and in the recruitment of a new workforce for years to come.

Traditional boundaries are changing. The delivery of several major transport infrastructure initiatives, combined with tangible progress on significant mixed use developments such as Paradise are collectively changing the way people access and move around the city, reshaping and growing the traditional office core to the benefit of both office occupiers and property investors alike.

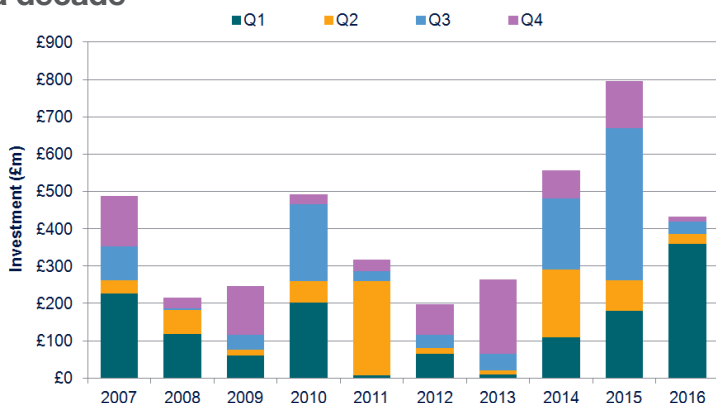
Whilst the traditional CBD continues to thrive, a new breed of occupier is emerging, placing less value on a traditional recognised address or location and more focus on quality of working environment, amenity and perhaps most importantly, connectivity, than was the case historically.

By way of illustration, over the past 12 months key landmark office buildings such as Mailbox, Alpha and Centre City located within the immediate vicinity of the newly redeveloped New Street Station have witnessed some of the highest demand and subsequent rental growth in the city and based upon identifiable current occupier demand, this looks set to continue.

This trend gives rise to improved viability for potential refurbishment and development opportunities for investors as occupiers become more open minded over the type of space they occupy and where it can be located.





This can only be healthy for a city the size of Birmingham, where offering the widest possible choice to occupiers is critical if the city is to fulfil its true potential in the years that lie ahead.

GRAPH 3 **2016 investment levels saw the strongest first half in a decade**



Graph source: Savills Research/Property Data

Headline stats, definitions and contacts

 8% office based employment growth over the next 10 years	 2 years worth of Grade A office supply in city centre	 684k office development currently under construction (excluding pre-lets)	 2.2% pa Predicted growth in Grade A office rents over the next three years
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Headline statistics	Take-up: in-town	Take-up: out-of-town	Top rents (£ per sq ft)	Prime yield
Full year 2016	670,000 sq ft	334,000 sq ft	£32.50	5.25%
End 2017 outlook	↑	↑	↑	→

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.

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