

# UK Commercial Market in Minutes

## Regional revival for investment and occupier demand

April 2014

### Yields still trending downwards

■ Several sectors saw prime yields move lower during March. City of London and Provincial Offices moved in by 25 bps. Multi-let industrials also fell by the same amount. Six other sectors are currently experiencing downward pressure on their yields.

■ The average prime yield across the range of sectors is now approaching 5%. In comparison, IPD 'average' equivalent yields are just over 7%.

■ The yield gap is below 200 basis points and has been moving lower since the end of last year, but IPD yields are still moving lower and faster than the prime measure. We believe that this is due to rising investor interest in secondary assets.

■ As shown in Graph 1 below, the IMA's figures for net retail and institutional sales, of OEICs and unit trusts, grew significantly throughout 2013.

■ While a smaller net proportion has usually been attributable to the institutions, the fact that they have recently been net disinvestors is interesting. Is this a blip or are some investors already locking in profit?

■ The chart also has annual capital growth, which is currently running at 5.5% per annum and showing signs of accelerating further during the next few months.

■ In the direct market, at present, not many UK funds are without requirements, with the weight of money leading to larger lot size requirements and greater interest in good secondary stock.

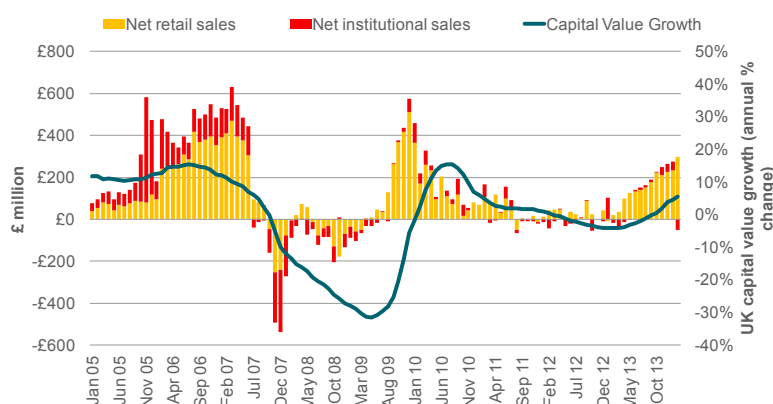
■ The usual story remains in that investor requirements out-weigh the available stock in the market. However, there is an anticipation of more stock coming through in the short-term, due to profit-taking and bank-led sales.

TABLE 1  
Prime equivalent yields

|                               | Mar 13 | Feb 14 | Mar 14 |
|-------------------------------|--------|--------|--------|
| West End Offices              | 3.50%  | 3.25%  | 3.25%  |
| City Offices                  | 4.75%  | 4.75%↓ | 4.50%  |
| Offices M25                   | 6.25%  | 5.75%↓ | 5.75%↓ |
| Provincial Offices            | 6.25%  | 5.75%  | 5.50%  |
| High Street Retail            | 4.75%  | 4.50%  | 4.50%  |
| Shopping Centres              | 5.00%  | 5.00%↓ | 5.00%↓ |
| Retail Warehouse (open A1)    | 5.25%↓ | 4.75%  | 4.75%  |
| Retail Warehouse (restricted) | 6.00%↓ | 5.50%↓ | 5.50%↓ |
| Foodstores                    | 4.50%  | 4.25%  | 4.25%  |
| Industrial Distribution       | 6.00%  | 5.75%↓ | 5.75%↓ |
| Industrial Multi-lets         | 6.00%  | 5.75%  | 5.50%  |
| Leisure Parks                 | 6.25%  | 6.00%↓ | 6.00%↓ |
| Regional Hotels               | 7.00%  | 6.75%↓ | 6.75%↓ |

Table source: Savills. Arrows indicate expected short term movement

GRAPH 1  
Net retail sales increase; institutional sales go negative



Graph source: Investment Management Association / Investment Property Databank

## → Clearer signs of regional appetite

■ Anecdotal evidence has pointed towards increased investment 'rippling' out from London and the South East. The market outside of the South East attracted a larger share of total investment during 2013, but was still below past trends.

■ However, now that we have Q1 data, Graph 2 looks at the quarterly average investment levels for two five-year periods either side of the last major recession in the UK (Q1 2009). The quarterly average for the South East has moved from £960m in 2004-2008, to £770m in 2009-2013, but only £530m for the first quarter of this year.

■ Graph 2 shows the significant increase in some of the UK regions. It is clear from the data of the ripple-out from London and the South East has impacted. There has been above average investment, compared to the 2004-2008 period, in the Midlands, in particular, Yorkshire & The Humber, East of England and Wales.

■ However, some of these regions will have been lower during Q1 2014 due to the severe lack of liquidity. This may well be exacerbated in the future by rising domestic and international investor interest in the regions.

## The growth of the SME

■ Surprisingly, small and medium-sized enterprises (SMEs) account for approximately 99.9% of UK businesses, by number. As a definition, SMEs can employ up to 250 employees.

■ A significant proportion of employment is within SMEs, with the Department of Business Innovation & Skills (BIS) estimating it to be around 59% of private sector employment. The property requirement from this sector is significant. A recent report from GE Capital said that 12% of SMEs expect to increase capital spending by 12% over the coming year and plan to create 660,000 jobs. Of course, there is some spare capacity within their property, but this must also create additional floorspace demand in our view.

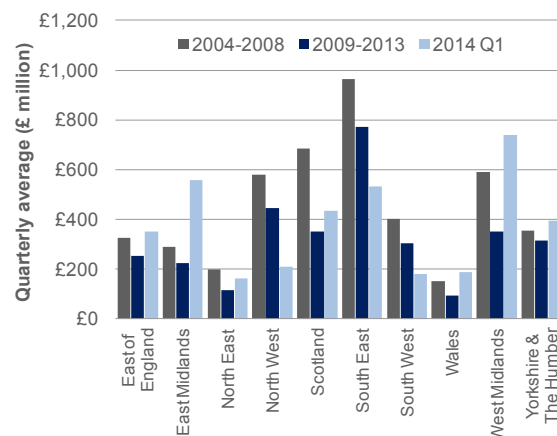
■ Graph 3 illustrates one particular question asked by BIS relating to SME key tasks during the next 12 months. These responses will also have an impact on floorspace.

■ More than half expect to hire new staff. However, it is also encouraging to see that 14% need to move to larger/better quality premises, 5% hope to make improvements to their property and 4% expect to acquire new/additional premises. These percentages may not be that large, but as a sample of the SMEs market, could translate into a much more buoyant level of occupier demand.

■ In support of the GE Capital's findings, BIS have recently released their SME Business Barometer. On the whole, confidence levels have improved and many businesses expect to employ more people over the next 12 months and anticipate higher turnover. Two-thirds of businesses aim to grow their business over the next 2-3 years. ■

GRAPH 2

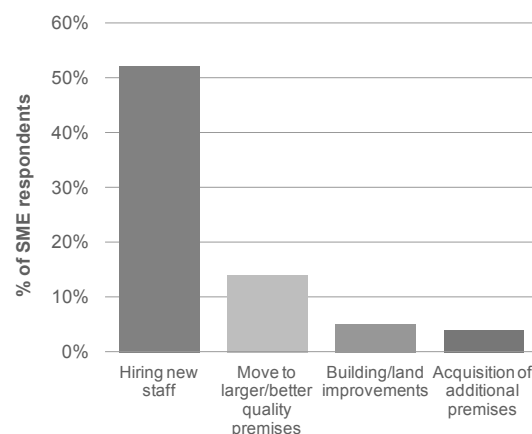
## Investment clearly moving out from the South East



Graph source: Property Data / Savills

GRAPH 3

## Keys tasks within the next 12 months for Business Services SMEs

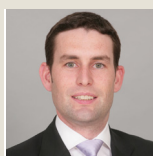


Graph source: Department for Business Innovation & Skills

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