Research & Forecast Report

UK | Property Snapshot
January 2016

Colliers International

Accelerating success.

Economy

Now that the US Fed raised the target federal funds rate by 25 bps, the EU referendum has moved up the UK agenda judging by increased industry and government media comment. Cameron is keen for a June 2016 plebiscite to reduce the negative business impacts of uncertainty. The UK economy and public finances continue to disappoint, with the third estimate of Q3 15 GDP reduced from 0.5% q/q to 0.4% q/q. In contrast, UK purchasing manager indices remain consistent with steady expansion at 55.3 (weighted average), although public finances remain pressured by weak tax receipts. UK monetary policy will remain accommodative with CPI still on the cusp of deflation at 0.1% and oil prices falling further; RPI registered 1.1% in November. Manufacturing and exports remain buffeted by strong sterling and a weak global trading environment.

Colliers' view: UK monetary policy will remain accommodative, caught as it is between Eurozone stimulus, US tightening and exchange rate constraints.

Investment

UK direct investment topped £64bn according to Property Data Ltd, surpassing last year's £63bn. December 2015's volume (£4.4bn) was much lower than December 2014's phenomenal result (£11.3bn). Property Archive, though, reports that 2015 transactions topped £70bn, surpassing last year's £69bn total. On balance, it looks as though 2015 volumes were robust, but that the year was front loaded. Foreign investors continue to dominate the market taking a 50%+ share of purchases in Q4 15. Conditions look set for a continuation of cross border investment into the UK given the weight of international capital and on-going political and economic uncertainty globally. January 2016 looks to be off to a reasonable start, no doubt driven by deal overhang from December. UK institutions remain well-funded with net cash inflows stable in November (£176m), although down by half against November 2014 (£344m). Foreign investor demand is set to continue in 2016 with interest in alternative assets increasing. Property yields remain stable for core assets.

Retail Shops: The appetite for assets continues to exceed supply. Two sizeable portfolios changed hands; London & Cambridge bought 171 units (19 sites) across the UK (£36.7m) and Investra Capital bought 14 petrol station convenience stores (£31m at 6.25% IY). Regional prime yields are firm as evidenced in Winchester (4%) and Leamington spa (5%).

Shopping Centres: Prime assets are sought after as Standard Life's purchase of Monument Mall in Newcastle (£75m at 4.3% IY) suggests. Secondary assets with asset management angles are also in demand as New River's purchase of the Neptune Portfolio (£92.3m at 8% IY) also suggests. **Retail Warehouses:** UK funds were active with TIAA Henderson closing the largest deal, Borehamwood Shopping Park for £14m at 5% IY. Several other assets changed hands at yields ranging from 4.25% in Greenwich to 6.5% in Wrexham. Supermarkets: Only one deal completed; a local authority pension fund bought a Waitrose in Crewkerne for £13.2m at 5% IY.

Central London Offices: Foreign investors continue to drive the market, accounting for over 50% of transactions by value and also for the top two deals: King Street, SW1 (£232m at 3.6% IY) and Gracechurch Street (£136m at 4.2% IY). UK funds took a modest share, led by M&G that bought the freehold to Bloomberg Place for £92.5m.

Regional: Foreign investors completed several notable deals, including AEW Europe's purchase of the Bath Road multi-let offices in Slough from SEGRO for £325m at 6.3% IY. Ho Bee (Singapore) acquired Apollo and Lunar House in Croydon for £99m at 5.4% IY (government income to 2023). In Edinburgh, an overseas investor bought Standard Life's offices from Standard Life for £93.8m at 5.1% IY.

Industrial: The industrial sector remains the domain of UK investors, especially UK funds, which accounted for over 60% of transactions by value. Yields remain pressured, with Hermes PUT paying £21.9m at 4.9% IY for a distribution shed near Heathrow. Multi-let portfolios proved popular, led by DTZ Investors' purchase of four estates for £82.5m at 6.4% IY

Colliers' view: Transaction volumes in 2015 matched 2014, but look to be front loaded. Pricing remains firm, but deal volumes may soften in 2016 as owners hold to realise value.

OCCUPIER MARKETS

Key Indicators	Latest[1]	End-Dec	End-Nov	End-Oct
UK GDP (%q/q)	0.4 (3rd est)	0.4 (3rd est)	0.5 (2nd est)	0.5 (1st est)
UK PMI (weighted average)	55.3	55.3	55.5	55.2
EURO PMI (composite)	54.3	54.3	54.2	53.9
UK CPI (%)	0.1	n/a	0.1	-0.1
UK RPI (%)	1.1	n/a	1.1	0.7
UK BASE RATE (%)	0.5	0.5	0.5	0.5
UK 10YR GILT (%)	1.72	2.02	1.88	1.94
GBP 3M LIBOR (%)	0.59	0.59	0.57	0.58
STERLING EFFECTIVE (FT)	89.5	90.7	93.3	92.8
GOLD (USD)	1086	1060	1066	1142
OIL BRENT (USD)	30.8	37.6	44.3	49.4
FTSE 100	5933	6274	6356	6361
IPD All property IY	5.04	n/a	5.04	5.05
IPD All property EY	6.12	n/a	6.12	6.12

[1] 14 Jan 16 (data and revisions)

Sources: ONS, Markit, FT, EIA, IPD, Haver

Retail

The song remains the same. Sales (ex-petrol) were rising in November by a reasonable 3.9% y/y, but margins remain squeezed as turnover relies on discounting. The retail sales deflator recovered slightly to -2.3% y/y, with the non-store deflator at -2.6% y/y and the stores deflator at -2.3% y/y. Despite strong consumer confidence and improving wage growth, the lower cost base of internet sales continues to undermine physical stores. Furthermore, retailers are growing wary of the ***2017 rates revaluation*** which may prove shocking to Central London operators who track total occupation costs. In contrast, store operators outside London will potentially see substantial rate reductions, but no doubt accelerating rental growth. According to IPD data, rents in Central London were climbing at a rate of 9.8% y/y in November, while rents outside the South East and London continued to fall at a rate of -0.4% y/y.

Colliers' view: Retail performance remains sensitive to prices and structural change. The 2017 rates revaluation is now on the agenda and likely to impact rental growth prospects UK-wide.

Offices

Central London: The London vacancy rate has been falling for almost three years and has fallen to just below 3% -- a 15 year low. Grade- A availability at the end of 2015 is down by 43% against the end of 2014 and Grade-B space down by 23%. Demand is coming from a wide range of sectors, including Fintech and the traditional City FBS sectors as well as Media and Tech in the West End. Demand across non-core submarkets continues to come from a wide range of occupiers looking for affordable Grade-A space. Supply continues to lag, with a considerable quantum of new space already pre-let. Regional: Rental growth is beginning to look entrenched, with IPD reporting positive year on year growth for the third consecutive quarter across all regions in Q3 15 in line with regional employment growth. New quarterly employment figures are due out this month, followed by the IPD index in early February.

Colliers' view: Unchanged. Occupier fundamentals continue to strengthen and demand across UK regions is holding up, supporting good to strong rental growth.

Industrial

The strength of domestic consumer goods demand continues to be the main support for the industrial manufacturing and distribution sectors, with exports continuing to struggle with weak global trade and exchange rate volatility. The headline purchasing manager data in December (51.9) suggests little respite. In contrast, rental growth remains strong UK-wide. IPD data shows a further acceleration in London to 8.9% pa growth in November, the highest since the series began in 1994, surpassing the previous high in 1998 of 8.7%. Likewise, the aggregate figure for the Rest of UK (ex-London and the South East) reached 3.6% pa, the highest level since 2000 when growth reached 4.2%. Given weak PMI and industrial production data, the lack of supply continues to look like the prime candidate for explaining this performance. Conventional bank development finance is still very limited for spec development, but developers claim that the real constraints are issues with the planning regime and lack of suitable sites, many of which have higher use values for residential.

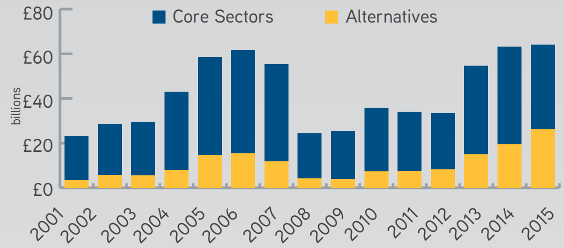
Colliers' view: Phenomenal rental growth continues across the sector due to lack of quality space and strength of the domestic economy. Global trading remains tough.

Residential

Prices finished 2015 up 10% on 2014 according to Halifax and up 4.4% according to Nationwide. Mortgage approvals registered 70,410 in November, up by 16% y/y. Mortgage rates fell in December to 1.89% for the 2-year fixed 75% LTV. So, in short, the market shows little sign of rapid cooling. Given disappointing wage growth, the sustainability of the mass market remains interest rate sensitive. The impact of the new buy-to-let taxation is not yet visible. An internet scan reveals several banks competing with very cheap BTL mortgages. A CML survey suggests that landlords will 'shrug off' the impacts. Nevertheless, a moderation in BTL activity in 2016 and 2017 is expected. Prime central London prices rose by around 6% in 2015, down from previous double-digit rates and further cooling is expected this year.

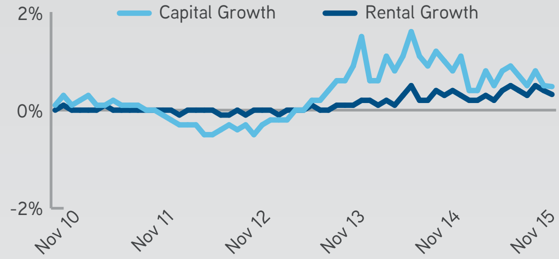
Colliers' view: Mass market price growth is moderating, but affordability is sensitive to mortgage rates. Recent BTL taxation impacts look to be marginal so far. London prime continues to cool.

Uk Direct Investment Volumes by Value



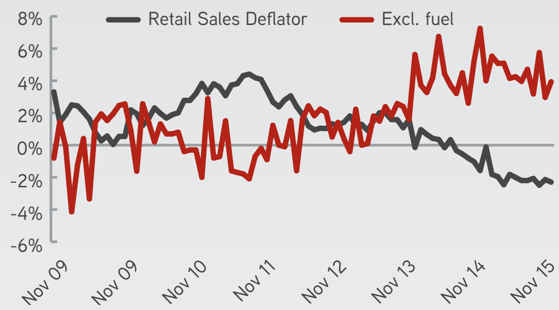
Source: Property Data Ltd

UK IPD All-Property performance



Source: IPD Monthly Index, November 2015

Retail Sales Growth %y/y



Source: ONS

Mortgage Rates

Source: Bank of England

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