

RESEARCH

The Big Nine

Quarterly update of
regional office activity
Q4 2018

TOP PERFORMERS

MANCHESTER Occupier market

There has been a record level of activity in the Manchester market this year, reaching 2.9 million sq ft, including 1.7 million sq ft in the city centre. In Q4 Amazon agreed the largest deal (90,000 sq ft) for its regional headquarters at Hanover House, Corporation Street.

MANCHESTER Investment market

For the year as a whole Manchester recorded almost £1 billion of investment activity. During Q4 Aviva invested in the mixed use scheme at Enterprise City, Spinningfields and the sale of SciTech for £180m was the largest out-of-town deal of the year.



STEAMhouse, Belmont Works, Birmingham

Another record year

2018 was another record year of take-up across the 'Big Nine' office markets, amounting to 10.7 million sq ft, compared to last year's previous best of 10.1 million sq ft. Both city centre and out-of-town activity were 30% up on the long term average.

The city centres were enhanced by significant inward investment during the second half of the year. Aside from the two largest deals to Barclays in Glasgow and Booking.com in Manchester, more recently Amazon also took 90,000 sq ft in Manchester for its first regional headquarters. Channel 4 has chosen Leeds for its regional headquarters and Talk Talk has announced it will be moving more jobs from London to Manchester.

In terms of sectoral activity, 2018 has been another strong year of take-up from Central Government, including the final two GPA deals. The banking sector, with some of the largest deals has had a record year, after two fairly quiet years of activity. Whilst Regus and WeWork dominated take-up in another strong year for the co-working sector, there were also deals with over ten other operators. Conversely professional services activity was slow in 2018 with legal, accountancy, property and engineering all showing below average take-up.

Transactional activity remained strong during the final quarter of the year. There was plenty of activity from the two star performers of 2018, Manchester and Glasgow, as well as both Birmingham city centre and out-of-town markets, and Cardiff which produced the best quarterly take-up figures for the year.

Build cost inflation and future economic uncertainty are continuing to restrict new development, and grade A availability (consisting of brand new stock and second hand grade A) is at a record low. This currently stands at just over 1 million sq ft across all nine cities (down from 1.6 million sq ft 12 months ago). There is also 2.7 million sq ft of speculative space under construction which equates to 1.4 years' supply based on average take-up rates, although this is skewed towards Manchester (40%), Birmingham (20%) and Glasgow (14%).

The lack of prime stock continues to impact on headline rents which now average £30.33 psf across the Big Nine cities. With an average rent free period of 20 months on a ten year term this equates to a net effective rent of £26.03 psf, an increase of 4.1% over the past 12 months and 30% over five years.



Charles Toogood

National Head of Offices

Market Data – Q4

City centre

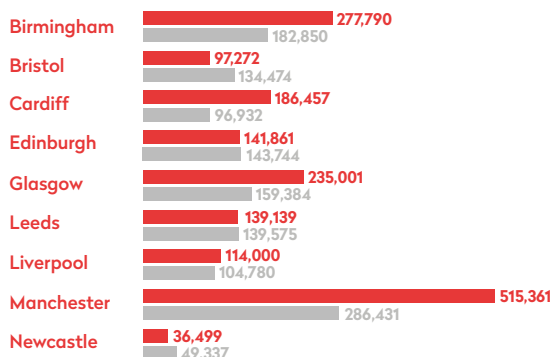
TOTAL TAKE UP IN Q4

1,743,380 sq ft

+34% compared to the ten year quarterly average

TAKE UP (sq ft)

■ Q4 2018
■ 10 year quarterly average



TOP FIVE DEALS

City	Property	Occupier	Sq ft
Birmingham	Belmont Works, Eastside	Birmingham City University	118,240
Manchester	Hanover House, Corporation St	Amazon	89,450
Manchester	Dalton Place	WeWork	76,174
Cardiff	3 Capital Quarter	Admiral Insurance	65,000
Glasgow	50 West Campbell St	Barclays	57,500

HEADLINE RENTS (£psf)

Location	Rents (£)	Rent free (mths on 10 yr term)	Net effective rent*(£)	Net effective rent (£) Q4 2017
Edinburgh	35.00	18	30.63	29.75
Bristol	35.00	18	30.63	28.44
Manchester	35.00	24	28.88	27.64
Glasgow	32.50	18	28.44	26.25
Birmingham	33.00	24	27.23	26.40
Cardiff	27.00	12	24.98	23.40
Leeds	30.00	24	24.75	24.75
Newcastle	24.00	18	21.00	20.56
Liverpool	21.50	24	17.74	17.74
Average	30.33	20.00	26.03	24.99

*including rent free period less three month fit-out.

Out-of-town

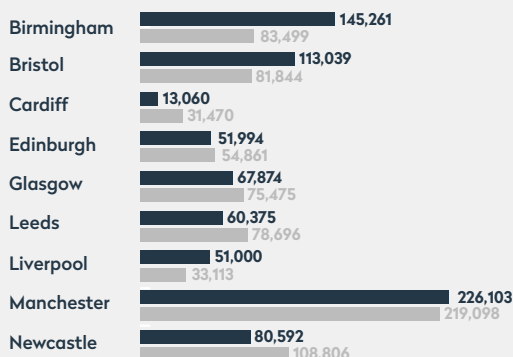
TOTAL TAKE UP IN Q4

809,298 sq ft

+6% compared to the ten year quarterly average

TAKE UP (sq ft)

■ Q4 2018
■ 10 year quarterly average



TOP FIVE DEALS

City	Property	Occupier	Sq ft
Newcastle	Meridian House	Cummings	33,840
Liverpool	Edward Pavilion, Albert Dock	Clockwise	33,000
Bristol	800 Aztec West	HM Government	32,007
Birmingham	3 Devon Way, Longbridge	Barnett Waddingham	21,120
Bristol	Gloucester Road	SCHQ	19,560

HEADLINE RENTS (£psf)

Location	Rents (£)
Birmingham (Solihull)	25.00
Leeds	22.50
Bristol	22.50
Manchester (South)	22.00
Edinburgh	22.00
Newcastle	16.95
Glasgow	16.50
Cardiff	15.00
Liverpool	14.00
Average	19.61

Market activity

Birmingham

A strong finish to the year in both Birmingham city centre and out-of-town markets brings the total for the year to 1.2 million sq ft, 9% above the ten year average.

In the city centre Q4 activity was led by Goodman's sale of 118,000 sq ft to Birmingham City University for an innovation centre at Eastside Locks. In addition, Zurich Insurance took 23,300 sq ft at the Colmore Building and there were a handful of deals over 10,000 sq ft to professional and financial services companies. Inward Investor Freightliner also acquired 16,000 sq ft in L&G's The Lewis Building in late December.

City centre grade A availability is now at its lowest point since 2005 but this is set to change as 577,000 sq ft of speculative development will complete this year; 167,000 sq ft at Chamberlain Square and 410,000 sq ft at Three Snowhill, the largest speculative development across the Big Nine.

The out-of-town market has seen the highest level of quarterly activity for three years. The largest deal was 21,123 sq ft to financial advisers Barnett Waddingham at 3 Devon Way, Longbridge. There were also a number of deals at Birmingham Business Park, including 17,600 sq ft to train manufacturer Zhuzhou and 13,300 sq ft to dental technologists Align Technology.

Bristol

Total take-up across the Bristol office market during 2018 amounted to 932,000 sq ft, 8% above the ten year average. The most active sector was education, led by the largest deal to the University of the West of England (77,600 sq ft) at Stoke Gifford earlier in the year. During Q4 there was approximately 100,000 sq ft of activity in both the city centre and out-of-town markets, with the largest deals out-of-town; 32,000 sq ft to HM Government at Aztec West and 19,600 sq ft to SCHQ at Bristol North Baths, Gloucester Road.

Grade A supply in the city centre remains very limited. However construction has recently started on the 200,000 sq ft speculative Assembly at Temple Quarter, whilst The Distillery, Glassfields is also on site comprising 93,000 sq ft over nine floors. Both are expected to complete in 2020. During summer 2019 70,000 sq ft of high quality refurbished space at 2 Trinity Quay will be delivered, bringing much needed additional capacity.

Cardiff

Strong city centre activity in Q4 helped bring Cardiff's take-up for 2018 in line with the ten year average of just over 500,000 sq ft. The largest deals were at JR Smart's Capital Quarter development. Admiral Insurance took 65,000 sq ft on a 10 year lease at No 3 Capital Quarter which completed in August. This is ahead of No 4 Capital Quarter (97,000 sq ft) which completes this Spring, where a 30,400 sq ft pre-let to solicitors Geldards was also agreed during Q4.

Further significant deals in the city centre were agreed for Monzo Bank (14,100 sq ft) at 2 Kingsway and Keolis Amey (11,200 sq ft) at St Patrick's House.

Edinburgh

Take-up for Q4 across both Edinburgh markets was in line with the average. This brings the total for 2018 to 960,000 sq ft, following stronger activity earlier in the year, particularly from legal services and asset management companies.

The largest deal of the quarter was 16,000 sq ft to lawyers Burness Paull at Exchange Plaza. Other notable activity was in the tech sector which included deals to IT management company Pulsant (14,240 sq ft) in West Edinburgh and Google street view provider NCTech (9,600 sq ft) at Quartermile 1.

On the supply side, there is 256,000 sq ft of grade A city centre space currently available. Although there is an additional 370,000 sq ft of space under construction, only 48,000 sq ft is still vacant (at Capital Square).

Glasgow

Glasgow's record year of take-up was headlined by Barclays' 470,000 sq ft deal at Buchanan Wharf, bringing office development to the city's waterfront heritage.

City centre take-up reached 1.4 million sq ft in 2018, more than double the previous record for the last ten years, as Barclays and the Government Property Unit deal exceeded average city centre take-up on their own.

We expect the supply and demand imbalance to continue throughout 2019 for the largest requirements as the city prepares itself to embrace 'co-working operators' who have yet to expand in Scotland and take on Regus, who strengthened their dominant position in 2018.

In the final quarter, city centre activity again dominated take-up, headlined by a further 57,000 sq ft deal to Barclays and 30,000 sq ft to KPMG. The out-of-town market was quieter compared to the buoyant activity over the summer.

Leeds

It has been another strong year of activity in the Leeds office market, led by the 60,000 sq ft HMRC deal at 3 Wellington Place during Q3. Both city centre and out-of-town markets achieved take-up 20% above average, and over a million sq ft in total.

During Q4 the largest transaction in the city centre was 24,000 sq ft to an intermarketing company at The Malthouse and there were a handful of 10,000 sq ft deals to occupiers such as Equifax at One Wellington Place, co-working company Orega and Mott MacDonald. Also Channel 4's decision to locate its regional headquarters in the city is expected to act as a catalyst to further inward investment from other media occupiers.

130,000 sq ft of available grade A space will be supplemented by two schemes completing this year, 66,000 sq ft at the former Majestic Cinema and 46,000 sq ft at 34 Boar Lane.

Liverpool

Take-up in Liverpool during Q4 amounted to 114,000 sq ft in the city centre and 51,000 sq ft out-of-town, 20% above the ten year quarterly average. The key deals were to Clockwise (33,000 sq ft) at Edward Pavilion and Grant Thornton (13,058 sq ft) at the Royal Liver Building. Take-up has recently reached record levels in Liverpool primarily due to the HMRC deal (270,000 sq ft) at India Buildings.

Demand remains positive for the year ahead as there are a number of 20,000 sq ft plus requirements from occupiers such as Liverpool Football Club, Bibby Line Group and Taylor Wessing. There is no grade A stock available in the city but Liverpool City Council is currently developing 160,000 sq ft at The Spine, Paddington Village. It is due for completion in September 2020 and 80,000 sq ft remains available, following the deal to the Royal College of Physicians (80,000 sq ft) earlier in the year.

Manchester

There has been a record level of activity in the Manchester market this year, reaching 2.9 million sq ft. City centre activity smashed the previous record, totalling 1.76 million sq ft and the out-of-town total was the highest for three years at 1.2 million sq ft. The largest deals of the year included Booking.com (225,000 sq ft), HMRC (154,000 sq ft) and Royal London (140,000 sq ft).

Q4 activity produced some further significant deals and inward investment activity as Amazon agreed 90,000 sq ft for its first regional headquarters at the refurbished Hanover House. The co-working office market continues to be active as WeWork has concluded its third deal in the city with 76,000 sq ft at Dalton Place and are under offer on 55,000 sq ft at the Hyphen building. Central Working has taken its second building in the city, 18,000 sq ft at 55 Spring Gardens.

There is 1.2 million sq ft of offices under construction in Manchester and almost 90% is still available. 330,000 sq ft completes this year, with the majority following in 2020 but we expect pre-let activity to considerably diminish availability prior to completion.

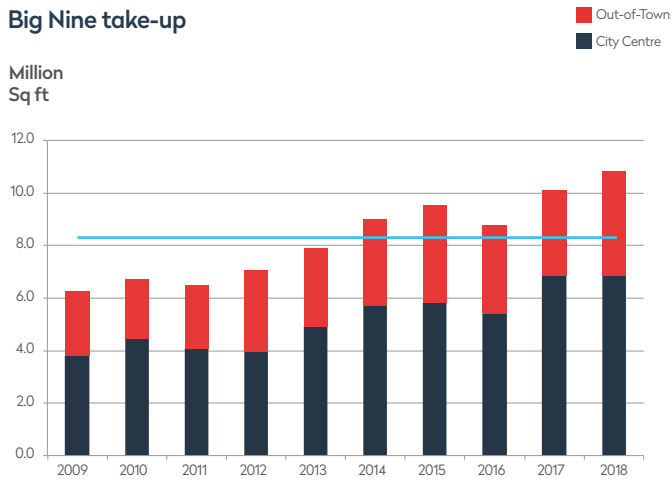
Newcastle

2018 has been a strong year for both the city centre and out-of-town markets, with the highest overall total for five years. This was led by the 63,000 sq ft deal to HM Courts and Tribunal Service at the Civic Centre, university deals in the city centre and a handful of consumer services deals out-of-town.

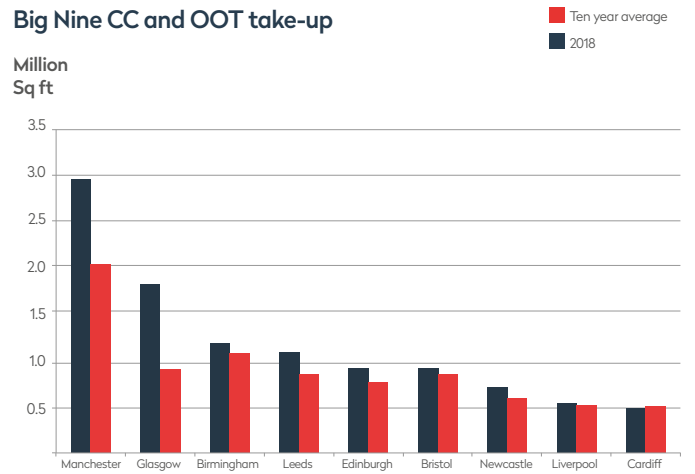
Q4 activity was strongest in the out-of-town market with two stand-out deals. Cummings took 33,800 sq ft at Meridian House and ESPA took 9,300 sq ft at North House, Sunderland.

Market at a glance

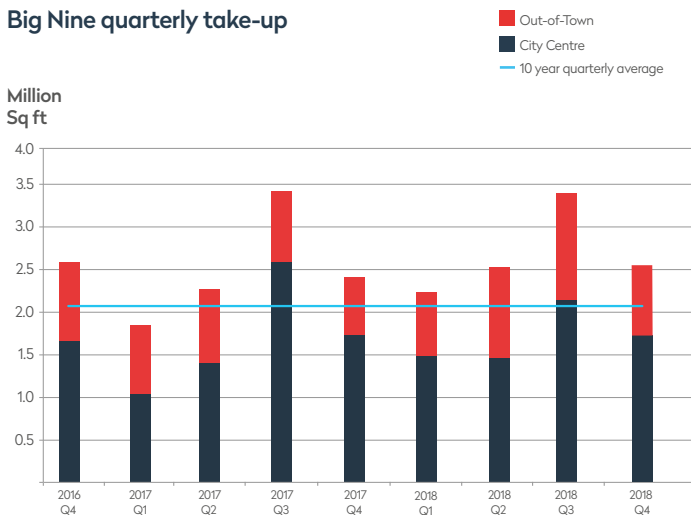
Big Nine take-up



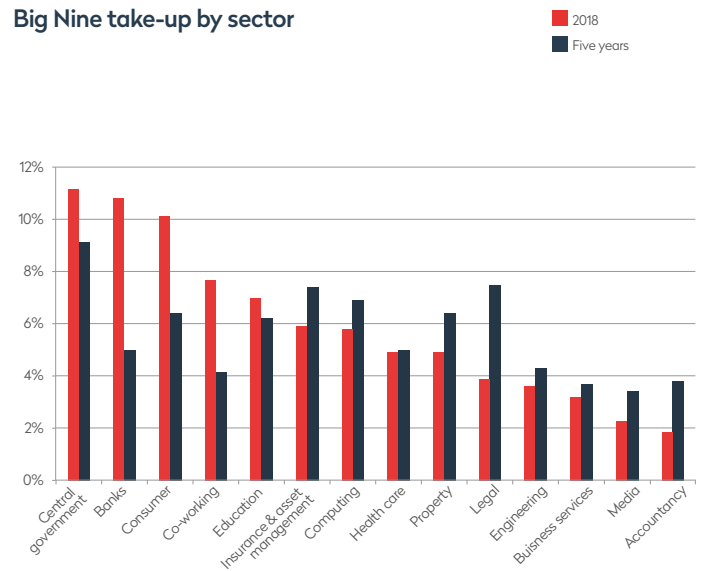
Big Nine CC and OOT take-up



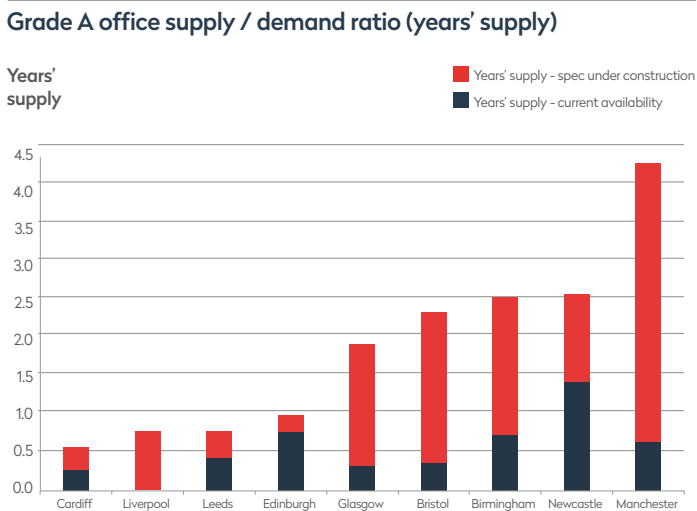
Big Nine quarterly take-up



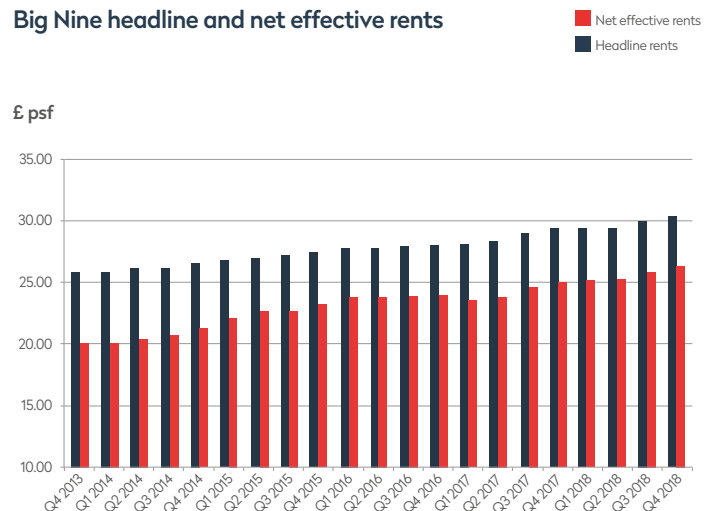
Big Nine take-up by sector



Grade A office supply / demand ratio (years' supply)



Big Nine headline and net effective rents



Strong finish to the year

Some very large office investment transactions meant Q4 was the strongest quarter of 2018 by deal volume at £1.08bn, double the 10 year quarterly average of £545m. This brings the total for the year to £3.1bn, in trend with the buoyant level of activity we have seen for the past five years.

It has been a strong finish to the year in Manchester which recorded almost half of all volume activity. In the city centre Aviva have invested in the mixed use scheme at Enterprise City, Spinningfields where Booking.com recently leased 225,000 sq ft. Circa £60m has been spent in Q4 with a further commitment to spend another £240m over the next 2 to 3 years. The largest out-of-town deal of the year was the sale of SciTech, for £180m to a new 50:50 joint venture with Bruntwood and Legal & General Capital, with 5 of the 8 assets in Manchester.

Elsewhere the Admiral building (1 David Street) in Cardiff was sold for £90 million by Amundi Real Estate to LaSalle Investment Management. Glasgow also recorded a strong finish to the year with deals at 1 Atlantic Quay (£55m), 19 Cadogan Street (£30.5m), and 100 Bothwell Street (£30.3m). Leeds also recorded key deals at 1 City Square (£32m) and Lawnwood Business Park (£26.5m) in the out-of-town market.

There has been a notable shift in sentiment with the deadline of 29th March looming and continued uncertainty on the Brexit outcome. However this was sufficiently late in the quarter not to impact on volumes.

For the year as a whole Manchester was again the stand out regional city with almost £1 billion of investment activity. Birmingham, Bristol, Cardiff, Edinburgh, Glasgow and Leeds all recorded total activity in the region of £300m.

2018 has been a record year of activity from UK institutions with key deals during Q4 to Aviva investors, Legal and General and LIM (Royal Mail Pension Fund). This is against the trend in the wider market of reduced activity from UK institutions, which are tending to hold cash reserves.

The impact of overseas money has diminished, falling to 24% of total volumes during 2018, compared to 38% for the past three years. This year overseas money has come from Europe and the Middle East but there has been very little activity from German and American investors, with the latter tending to be active in markets that are less advanced in the investment cycle.

The latest average equivalent yield for the regional office markets according to the MSCI monthly index was 7.12% at the end of December, down from 7.17% on the previous month, 7.56% a year ago and 9.8% before the recovery started in 2013.

Looking forward to 2019 there has been a sentiment shift as many investors adopt a wait-and-see approach in the first quarter of 2019 until a clearer picture of Brexit becomes apparent. We expect transactional volumes to be below trend levels, with performance driven by income as capital values come under pressure. That said, with the development pipeline limited (having been below trend for the last decade), debt levels and LTVs recovering to long term trend levels and significant global capital allocated to UK real estate, there is no material 'distress' to suggest any notable fall in capital values.

We expect an upward trend in bond yields over the medium term but this is likely to be modest and the gap to property yields will remain above the long term average.

The impact on sterling of the continued uncertainty has provided increasingly attractive conditions for overseas investors, although we have already seen a drop off in their exposure in the regional markets.



Mark Frampton
Senior Director, Investment

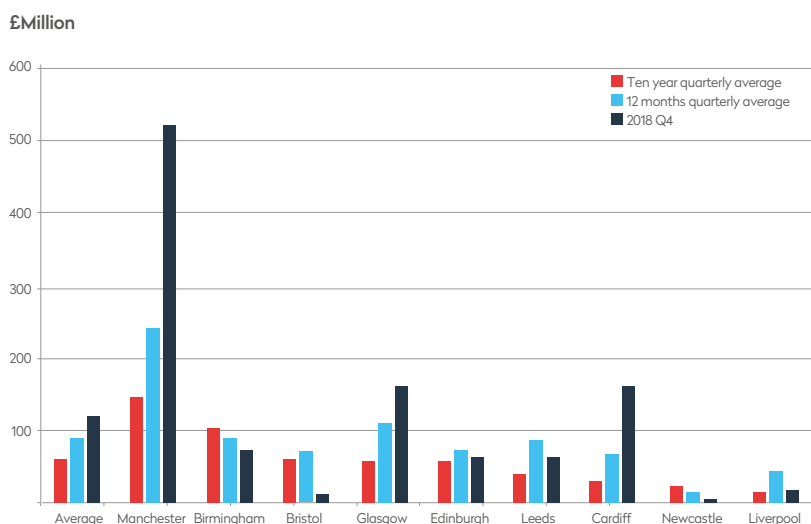
Market Data – Q4

TOTAL INVESTMENT VOLUMES IN Q4 2018

£1.08 billion

Compared to
£687m (previous quarter – Q3 2018) £1.23m (a year ago – Q4 2017) £545m (ten year quarterly average)

BIG NINE INVESTMENT VOLUMES (£ million)



PRIME CITY CENTRE YIELDS

Location	Q3 2018	Q4 2018	Trend for last 12 months	Peak (2007)
Birmingham	4.75	4.75	→	4.5
Bristol	4.75	4.75	↓	5
Cardiff	5.50	5.50	→	5
Edinburgh	4.75	4.75	↓	4.75
Glasgow	5.00	5.00	↓	4.75
Leeds	4.75	4.75	↓	4.75
Liverpool	5.75	5.75	↓	5.5
Manchester	4.75	4.75	→	4.5
Newcastle	5.75	5.75	↓	5.25

TOP FIVE CITY CENTRE DEALS – Q4 2018

Date	Property	City	Purchaser	Vendor	Price (£m)	NIY (%)
Oct-18	Enterprise City, St Johns	Manchester	Aviva Investors	Allied London Properties	£300*	n/a
Nov-18	1 David Street	Cardiff	Royal Mail Pension Fund	Amundi Real Estate	£90	4.25
Dec-18	1 Tanfield	Edinburgh	Greenridge Regional UK	PATRIZIA Immobilien AG	£65	6.0
Oct-18	1 Atlantic Quay	Glasgow	BLME Investment Solutions	Moorfield REF III LP	£55	5.2
Dec-18	1 City Square	Leeds	Britannia Invest	Aviva Investors	£32	6.25

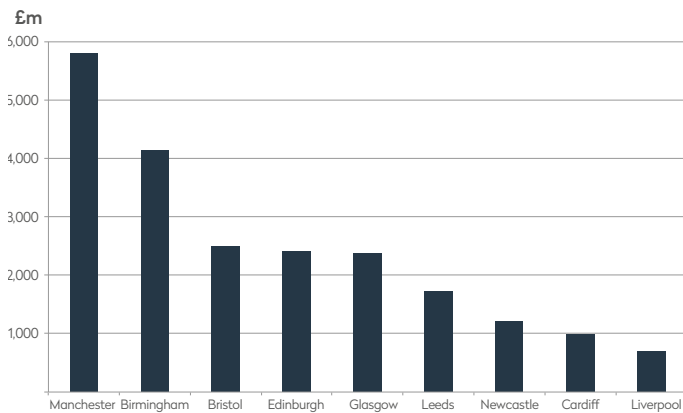
*Circa £60m in Q4 with a further £240m commitment over the next 2 to 3 years

TOP FIVE OUT OF TOWN DEALS – Q4 2018

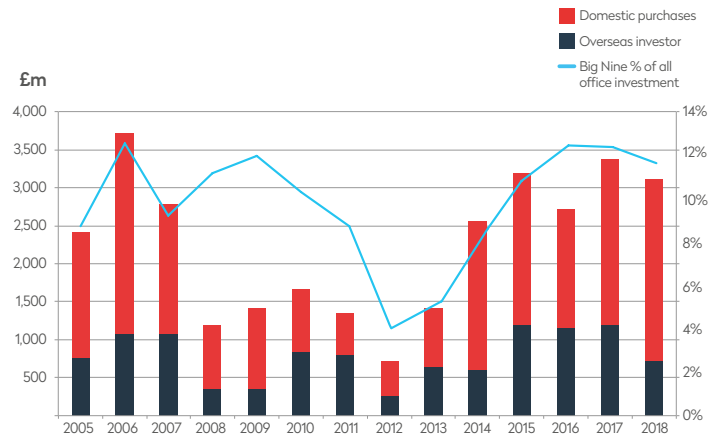
Date	Property	City	Purchaser	Vendor	Price (£m)	NIY (%)
Oct-18	Bruntwood SciTech	Manchester	Legal & General Capital	Bruntwood Estates Ltd	£180	n/a
Dec-18	Treforest Business Park	Cardiff	Legal & General	Rightacres Prop Co Ltd	£71.3	4.0
Oct-18	Maxim Office Park	Glasgow	Shelborn Asset Management	Cerberus Capital Man	£38	n/a
Dec-18	Lawnswood Business Park	Leeds	Hillview Real Estate	Centurion Properties Ltd	£26.5	8.3
Dec-18	Hercules Business Park	Manchester	Private investor	Royal London Asset Man	£5.1	8.7

Market at a glance

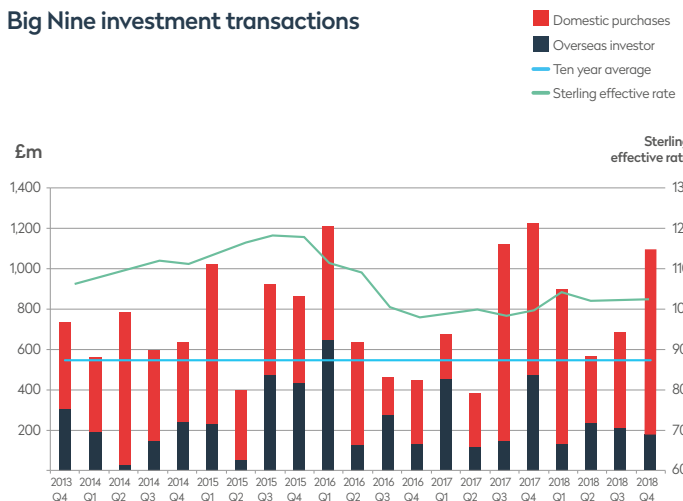
Big Nine investment volumes 2009 to 2018



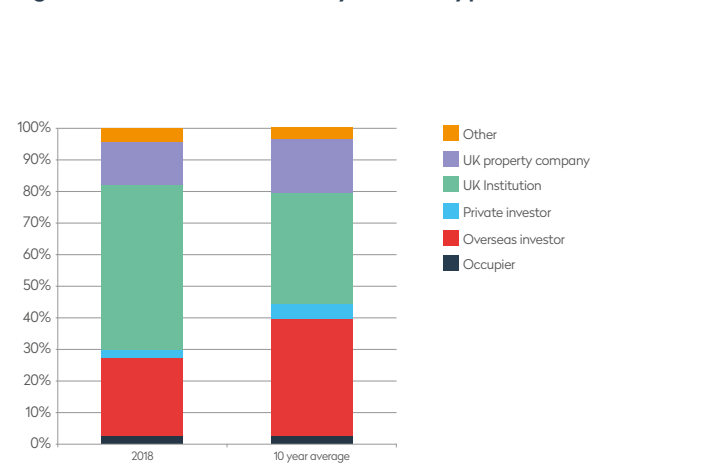
Big Nine investment transactions



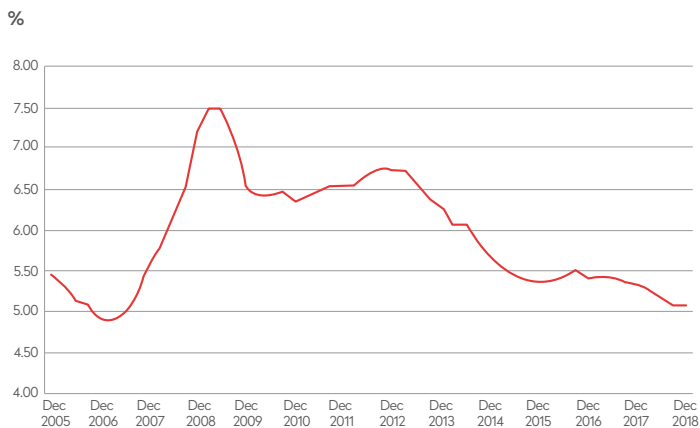
Big Nine investment transactions



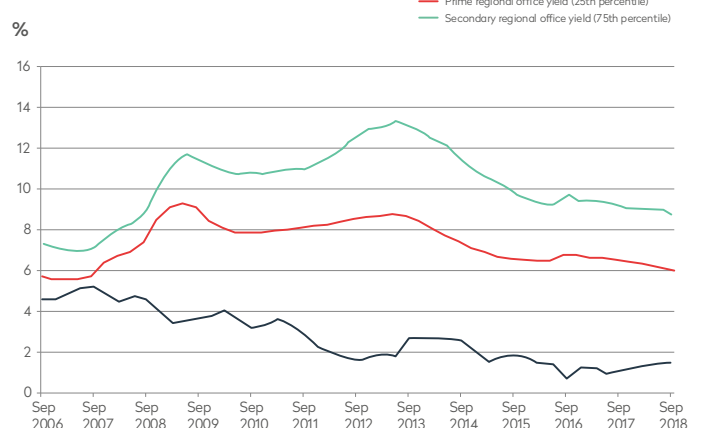
Big Nine investment volumes by investor type - 2018



Average Big Nine prime yield



Regional office yields vs 10 year gilts



Source: GVA, Property Data, MSCI

Outlook

- The private sector is increasingly seeing the benefits of locating in the UK's regional cities, with lower occupancy and labour costs and remote working more viable. 2018 saw another step change in activity with the Barclays (470,000 sq ft) and Booking.com (225,000 sq ft) deals and we expect this broad trend to continue.
- This increased level of commitment by occupiers to the prime regional markets continues to encourage investors. Long-dated income assets with strong covenants remain in significant demand as they provide more security from the continued economic uncertainty.
- If there is more clarity on Brexit and the uncertainty dissipates, then we expect to see a resumption in occupier and investment decisions as well as increased development and lending.
- Judging by the reported ambitions of the co-working sector, 2019 will be the third year in succession of over 500,000 sq ft of take-up for the sector.
- According to MSCI, average annual regional office rental growth was 1.3% to November 2018. We expect a similar level of growth over the next two years.

Should you wish to discuss
any details within this update
please get in touch.

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