

Economy

UK economic growth almost came to a standstill in Q1 18 as GDP rose just 0.1% q/q. Much of the weakness is likely a result of severe weather disrupting construction, distribution and consumer spending. The latest PMI results point to a modest April rebound and a GDP revision is a strong possibility. Nonetheless, the Bank of England revised down its growth forecast for 2018 to 1.4% from 1.8%. A base rate rise looks to have been postponed to either August or November. Weak GDP figures and a pessimistic outlook impacted on sterling, which currently trades at around US \$1.35, down from US \$1.40 at the end of March. CPI fell to 2.5% in March from 2.7% in February while RPI fell to a one-year low of 3.3%. Inflation will fall further. Despite a return of positive real wage growth (0.7% y/y in March¹), consumer confidence has not yet responded as signalled by the GfK index (-9) slipping from March's ten-month high (-7).

Colliers view: GDP growth will accelerate after a weak Q1, but 2% growth for 2018 now seems too optimistic despite a recovery of real wage growth. We still expect a base rate rise this year.

Investment

Preliminary Property Data figures highlight a weakening in investment volumes in April. At just £1.2bn, the April figure failed to reach £2bn for the first time in over six years. The largest property deal recorded was the £125m purchase of a residential block in South Bank Tower by the London based Jackyl Fund. Despite disappointing April figures, investor demand remains stable and May data, so far, point to a solid rebound in investment volumes. MSCI Q1 18 data shows that yield compression was recorded across the three main commercial sectors in Q1. Retail and offices saw hardening of net initial yields of 3bps over Q1, while industrial hardened by 12 bps. A retail parade in Clapham Junction was offered to the market earlier this year for £100m at 4% IY, but is being purchased by CBREGI for £130m at 3.25% IY, highlighting strong demand and firm pricing.

Retail: Retail investment in April was modest at £350m, with only 29 deals recorded so far. The largest deals in the sector were all part of mixed-use schemes dominated by offices. The largest pure retail plays included a £32m purchase of a 90,000 sq ft building in Newcastle by Sports Direct and a £17m purchase of the Heeley RP (7.15% IY) in Sheffield by Mayfair Capital. Only one shopping centre changed hands in April (Abbeygate SC in Nuneaton for £4.2m).

Retail transactions	Value	Deals	April selected yields
Unit Shops	£65m	13	4.1% Glasgow / 5.5% Leamington Spa
Retail Warehouses	£24m	4	7.2% Sheffield
Shopping Centres	£4.2m	1	n/a Nuneaton
Supermarkets	£26m	3	4.0% Ashtead

Source: Colliers International, Property Data Ltd.

¹ The 0.7% increase refers to the monthly data. The ONS reported a 0.4% increase in real wages for the period Jan'18-Mar'18 compared to the same period in 2017.

Offices: Investment volumes in the sector fell from £1.5bn in March to £620m in April, with international investors accounting for just 20%. There were very few 'vanilla' income purchases to report. The largest deals include the purchase of 5 Strand (Westminster Council/ Boots) in London by an Indian hotel developer (£90m at 4.6% IY) and Workspace Group's acquisition of Centro 1 & 2 in Camden (£76.5m at 4.9% IY). Outside of London, the West Midlands PF purchased City Point on King Street in Leeds (£26m at 5.8% IY).

Office transactions	Value	Deals	April selected yields
London	£331m	12	4.9% West End
Regional	£289m	31	5.8% Leeds

Source: Colliers International, Property Data Ltd.

Industrial: April was also a weak month for industrial, with deal volumes amounting to just £200m. Charlton Riverside in Greenwich was acquired by an undisclosed investor for £58m, including four industrial assets with river frontage. London and Metric Property also bought a portfolio of five urban warehouses for £26m at 5% IY.

Industrial transactions	Value	Deals	April selected yields
Distribution	£116m	12	6.2% Doncaster / 5% home counties portfolio
Multi-let parks	£84m	15	6.4% West Bromwich

Source: Colliers International, Property Data Ltd.

Colliers view: Despite weak April volumes, pricing is generally stable and investment demand steady. Prime retail is strong, but secondary suffers from lack of deals/evidence.

Key Indicators

	Latest ¹	End Apr	End Mar
UK GDP (%q/q)	0.1 (Q1)	0.4 (Q4 17)	0.4 (Q4 17)
UK PMI (weighted average)	52.9	52.9	51.7
EURO PMI (composite)	55.1	55.1	55.2
UK CPI (%)	2.5 (Mar)	na	2.7 (Feb)
UK RPI (%)	3.3 (Mar)	na	3.6 (Feb)
UK BASE RATE (%)	0.5	0.5	0.5
UK 10YR GILT (%)	1.50	1.49	1.41
GBP 3M LIBOR (% eop)	0.65	0.71	0.71
STERLING EFFECTIVE (FT)	78.8	79.5	79.8
GOLD (USD eop)	1319	1316	1321
OIL BRENT (USD eop)	77.4	75.2	70.3
FTSE 100 (eop)	7725	7509	7057
IPD All property IY	↓ 5.00 (Apr)	na	5.01 (Mar)
IPD All property EY	↓ 5.88 (Apr)	na	5.89 (Mar)

¹ May 14th (data and revisions)

Sources: FT, Haver, IHS Markit, MSCI, ONS

OCCUPIER MARKETS

Retail

The retail sector remained in the doldrums with sales volumes falling from 1.5% y/y in February to 1.1% y/y in March, one of the weakest rates seen in the past five years. Worryingly, latest data from the British Retail Consortium show that retailers suffered the largest drop in business in more than two decades in April as bad weather and the timing of Easter weighed on consumer spending. The GfK consumer confidence index also slipped. Despite a return of positive real wage growth, a revival in consumer spending has not yet materialised. Rental growth patterns remain unchanged in the sector with a Q1 18 rise of 0.9% y/y reported. Regional disparities persist. Standard shops in Central London continued to record the strongest rental growth, although at 4.9% y/y, the increase has moderated further from the double digit rates seen in the recent past. Interestingly, MSCI reports that out of town shopping centres saw rents rise at a 4% y/y rate, a considerable uplift on the 2.6% in Q1 2017. Meanwhile, 'Rest of UK' rents fell by 0.9% y/y.

Colliers view: Ex-London rents are forecast to see further declines this year although, in H2 18, rising real wages will begin to offer respite to operators and landlords. London will outperform.

Offices

Central London: Headline rents in some submarkets have started to respond to an acute shortage of Grade A space. Locations such as Mayfair, St. James's (both have reached £120 psf) and Paddington all saw prime rental increases in Q1 18. Strong pre-letting activity continues. In the City, over 70% of the 800,000 sq ft scheduled for completion by mid-2018 is already let. **Regional CBDs:** Prime rents across the 'Big Six' markets are expected to rise further in 2018. Secondary rents are also likely to see further upward movements due to short supply of prime Grade A space. Prime Manchester rents are forecast to reach £40 psf by 2020.

Colliers view: Prime rents rose in some London submarkets in Q1, but elsewhere further cyclical cooling will moderate growth. Regional CBD rents will rise further for Grade A & B space due to supply shortages.

Industrial

Manufacturing output rose just 0.3% q/q in Q1 18 (ONS), following 1.3% and 1.1% outturns in the previous two quarters. The Manufacturing PMI fell to a 17-month low in April, highlighting that growth may have slowed further at the start of Q2 18. With backlogs of work falling and stocks of finished goods accumulating it is likely that output growth will remain subdued in the coming months. Occupier demand remains steady, with rents rising at a 5.3% y/y rate during the Q1 18, according to the MSCI quarterly index. Despite the belief that the logistics sector will be the key driver of demand for industrial space, standard industrial rents, which rose at a 6.1% y/y rate in Q1 18, continued to outperform distribution rental growth at 3.7% y/y.

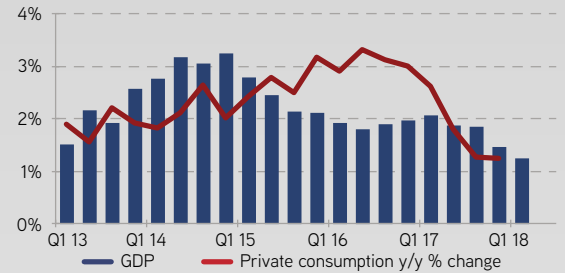
Colliers view: Unchanged. Stable demand and lack of Grade A space will support further rental growth.

Residential

The UK housing market remains muted. Residential property transactions decreased 11.8% in March 2018 compared to the same month in 2017, according to latest data from HMRC. At the same time, mortgage approvals for house purchases fell to 62,914 in March (63,781 in February). The figures may betray a greater caution by buyers as pressure on household finances continues to impact consumer confidence. It is also likely that the decline in transactions was not linked solely to consumer confidence, but that bad weather and a lack of supply in key areas acted as market constraints. According to Nationwide, house prices grew 2.6% y/y in April, up from 2.1% in March, while the Halifax measure pointed to a more modest rate of 2.2% y/y, down from 2.7%. Rising long-term bond rates over Q1 18 look to be impacting mortgage rates with the 75%LTV 2 year fix up by 19bps in March to 1.72%, the highest since July 2016.

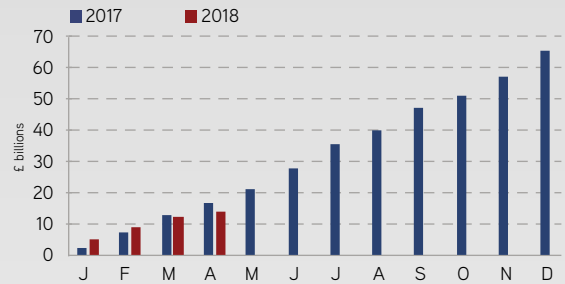
Colliers view: A lack of willing sellers and low mortgage rates will continue to support prices, but further price growth will be moderated by slow wage growth and affordability ratios.

GDP and private consumption



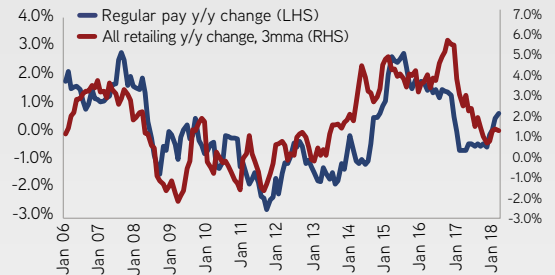
Source: Oxford Economics

Investment transaction volumes (cumulative)



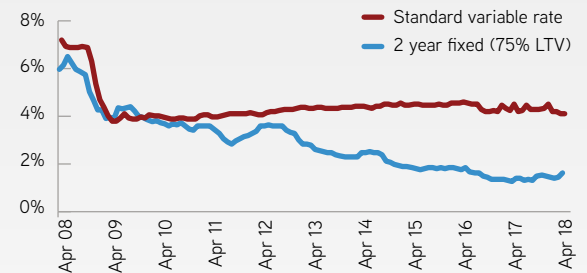
Sources: Property Data Ltd., Colliers International. April 2018 preliminary data.

Real wage growth and retail sales



Sources: ONS, Oxford Economics

Mortgage Rates



Source: Bank of England

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