Research & Forecast Report

United Kingdom | Property Snapshot
October 2017

Economy

Economic activity expanded by a better than expected 0.4% q/q in Q3, supported by encouraging industrial output growth. This was still not enough to shift the economy into a higher gear. GDP forecasts for 2017 remain near 1.5%, as inflation acts as a drag on household spending, while 'Brexit' uncertainty inhibits investment. Despite uninspiring GDP growth, the labour market remains robust, with the unemployment rate reaching another record low (4.3%) in the three months to August. This has not yet led to strong wage growth, with the total pay (including bonuses) rising by 2.2% y/y over the same period. With inflation at 2.9% in August and 3.0% in September, real wage growth remains negative. Despite weak GDP growth, consumer spending and negative real wage growth, MPC forward guidance suggests an imminent base rate rise back to the pre-EU referendum level (0.5%). Further hikes are unlikely in the short to medium term.

***Colliers view**: Weakness in key economic drivers suggests a rate hike is premature, but the BoE may be seeking to rearm its depleted policy arsenal and firm its credibility.*

Investment

As is tradition, investment activity picked up considerably in September following the quiet summer months, almost doubling the monthly total compared with August. Trading volumes reached £6.9bn, up £1bn against September 2016. Overseas players continue to drive activity, accounting for 60% (£4.1bn) of purchases and remain focused on offices, industrial and leisure. Two of the top three deals of the month were hotel portfolios: Aprirose acquired 25 Qhotels for £525m -- the second largest leisure transaction of the year; and Henderson Park purchased two Hilton Metropole hotels in London and Birmingham for £500m. Preliminary data suggests that trading activity has slowed in October. Agents complain of a scarcity of stock. Total volumes, though, are likely to improve as further evidence becomes available.

Retail. Investment exceeded £1bn in September. While up on the meagre levels of August, it was down on an annual comparative basis (£2bn in Sep-16). UK institutions took the largest share (44%) of purchases. The most significant deal by value was the sale of a 7.5% stake of Bluewater Shopping Centre by Hermes for £155m at 4.4% IY. Retail warehouse trading was firmer, while shopping centre and supermarket trading remained limited.

Retail transactions	Value	Deals	September selected yields
Unit Shops	£243m	21	3.95% Brighton / 4.7% Edinburgh
Retail Warehouses	£319m	17	Circa 5.5% for good secondary
Shopping Centres	£178m	3	4.4% (Bluewater)
Supermarkets	£123m	4	5.8% to 5.9% for £40m-£50m assets

Source: Colliers International, Property Data Ltd.

Offices. In the absence of more super prime transactions in London, investors' focus shifted towards the regions where over £2bn worth of assets traded. This was led by the acquisition of the ABBP business park portfolio by TPG for £450m at 6.33% IY from L&G. Elsewhere, Frasers Centrepoint purchased an office park in Winnersh Triangle (Reading) from Oaktree for £365m.

Office transactions	Value	Deals	September selected yields
Central London	£500m	5	4.0% City and 4.6% Mid-Town
Regional	£2bn	61	3.5% Cardiff, 4.5% Birmingham

Source: Colliers International, Property Data Ltd.

Industrial. Almost £1.1bn worth of transactions in September, the bulk of which involved the £559m acquisition of a light industrial portfolio by Blackstone from a Brockton/Dunedin JV. Yields remain under pressure, exemplified by a sub-3% deal in West London.

Industrial transactions	Value	Deals	September selected yields
Distribution	£97m	11	6.1% Warwickshire
Multi-let parks	£983m	63	2.96% (London), 4.89% (Coventry)

Source: Colliers International, Property Data Ltd.

***Colliers view:** Overseas investors continue to determine activity, enticed primarily by attractive exchange rate dynamics, but with a stronger regional focus.*

Key Indicators

	Latest[1]	End Sep	End Aug	End-July
UK GDP (%q/q)	0.4(1st)	0.3(3rd)	0.3(2nd)	0.3(1st)
UK PMI (weighted average)	53.5	53.5	53.4	53.8
EURO PMI (composite)	55.9	56.7	55.7	55.7
UK CPI (%)	3.0	3.0	2.9	2.6
UK RPI (%)	3.9	3.9	3.9	3.6
UK BASE RATE (%)	0.25	0.25	0.25	0.25
UK 10YR GILT (%)	1.41	1.39	1.07	1.25
GBP 3M LIBOR (%)	0.42	0.33	0.28	0.29
STERLING EFFECTIVE (FT)	77.5	78.6	74.7	77.0
GOLD (USD)	1266	1283	1320	1269
OIL BRENT (USD)	60.4	56.7	52.7	52.6
FTSE 100	7505	7373	7431	7372
IPD All property IY	5.22	5.22	5.25	5.26
IPD All property EY	6.08	6.08	6.10	6.11

Oct 27th (data and revisions)
Sources: ONS, Markit, EIA, MSCI, Haver, DailyFX

OCCUPIER MARKETS

Retail

September sales figures offer grim reading. Volume growth (ex-petrol) fell in September by -0.7% m/m, bringing the annual rate down to 1.5% y/y, the lowest since February 2014. This looks to be a direct response to increased prices. The sales deflator rose to 3.1%, the highest level since December 2011. Food stores continued to feel the pinch, with the volume growth rate down to -1.3% y/y. In the year to end September 2017, total sales volumes (ex-petrol) grew by 1.7%, compared to 4.3% over the same period of 2016. Company failures in 2017 continue to increase, according to CRR, although the number of units affect remain relatively modest. Internet sales remain firm, up 2.3% m/m. With inflation unlikely to moderate until next year, physical store operators are likely to remain squeezed through the Xmas season as household disposal income continues to fall. Retail rents remain stable, according to MSCI. The month-on-month growth rate was 0.1%, while the annual rate reached a very modest 0.6% y/y.

Colliers view: Price inflation continues to impact sales performance significantly, but underlying retail property performance remains stable, if lacklustre.

Offices

As anticipated, Q3 17 take-up in London recorded a fifth consecutive quarterly rise, reaching 3.1m sq ft, the highest since Q1 16. Nevertheless, London's overall vacancy rate rose to 5.5%, a four year high, although supply shortages are expected to reappear in 2018 and 2019 given steady demand and a slowdown in completions of new space. Headline rents have stabilised at £118 psf in Mayfair/St James and the City Core at £68.50 psf. Ex-London, take-up in Birmingham was the strongest since Q2 15 at over 400k+ sq ft. Availability in Bristol is at an all-time low with Grade A vacancy at 3% and overall vacancy at 5%. Bristol has joined the £30 psf club. In contrast, South East office leasing is characterised by churn, with limited evidence of expansionary demand, although Hammersmith and West London are faring better and rents remain generally buoyant, especially for Grade A stock.

Colliers view: Unchanged. Occupier markets are stable UK-wide, while leasing activity in Central London continues to defy 'Brexpectations.' Prime rents are stable UK wide.

Industrial

Despite economic indicators suggesting a softening of demand across the industrial sector, PMI data for September 55.9 suggests that the sector was still expanding at a steady pace. Cost pressures and rising output prices continue to rise. Sterling still remains down by around 10% against pre-referendum levels, hence exporters continue to be supported, and revised data shows that net exports are making greater contributions to GDP. Occupier demand remains steady across the UK. Industrial rents continue to rise at an annual rate of 4.9% in September (MSCI). Rents in London are in the 'upper teens.' Occupiers are increasing willing to pay for greater leasing flexibility, but space remains at a premium due to increasingly tight land supply and flexibility remains the exception, not the rule.

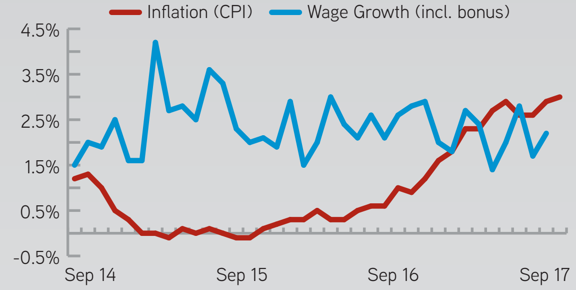
Colliers view: Structural change is evident, but workforce constraints and investor needs are limiting occupier and developer response. Limited space will continue to support rental growth.

Residential

Annual house price growth fell to a 2.0% y/y rate in September on the less volatile Nationwide Index. Mortgage approvals are also stable at 66,580, in line with the twelve-month average of 66,113. The two-year 75% LTV fix remains at 1.4%. HMRC reports that year-on-year transactions are up by 5% to 100,850, although a modest month-on-month slowdown was also reported. Despite stable transaction volumes, mortgage approval rates and low mortgage rates, RICS national house price expectations for the next three months fell to a -8% net balance, although regional price expectations are generally positive. The Government looks very likely to offer additional market supports when the Autumn Budget is released in late November, including house building stimuli. It is not clear who the winners and losers will be, but new affordability tests for 'portfolio landlords' (4+ properties) effective from 30th September may offer a clue. Implementation of affordability tests by banks is still fragmented.

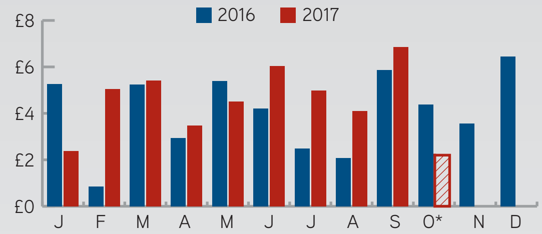
Colliers view: The UK housing market has stabilised, but is subject to further shocks from heavy handed government policy changes.

Inflation and Nominal Wage Growth



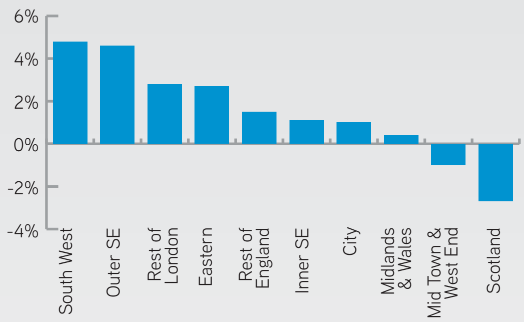
Source: ONS

Investment transaction volumes



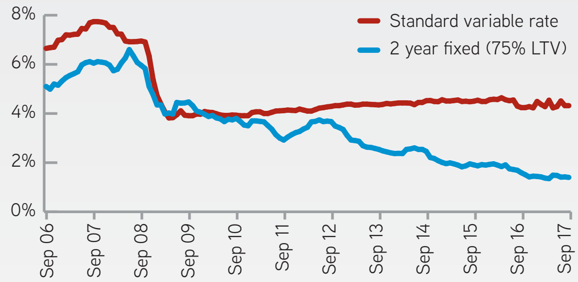
Sources: Property Data Ltd., Colliers International
October preliminary data

Office Annual Rental Growth (Sep-17)



Source: MSCI Monthly

Mortgage Rates



Source: Bank of England

For more information, please contact:

Walter Boettcher
+44 20 7344 6581
walter.boettcher@colliers.com

Colliers International
50 George Street
London W1U 7GA