UNITED KINGDOM

SOUTH EAST OFFICES

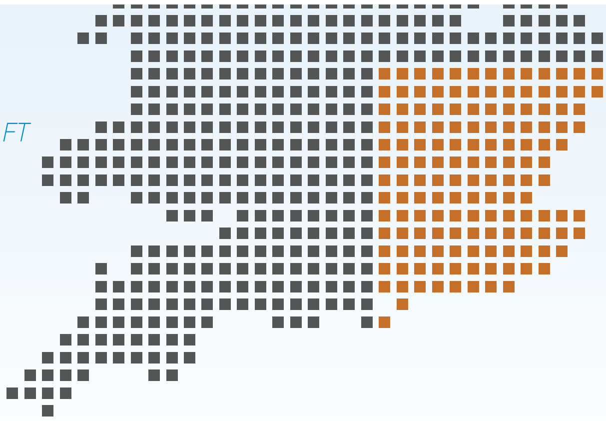
QUARTER 2 | 2018

Q2 18 TOTAL TAKE-UP

766,335 SQ FT

63.5%
QUARTER-ON-QUARTER

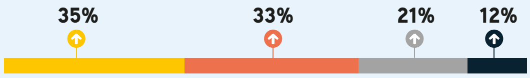
-5.2%
5-YEAR QUARTERLY AVERAGE



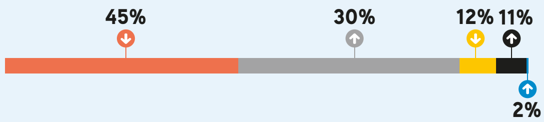
MARKET HIGHLIGHTS

- After a slow start to the year, take-up across the South East has rebounded significantly in the second quarter. Leasing activity is 63.5% up q-o-q and stands at 766,335 sq ft, which is only 5% below the 5 yr quarterly average (808,326 sq ft).
- Take-up was buoyed by the largest deal this quarter to Publicis who are consolidating from offices in Fitzrovia and Brick Lane. They took 212,000 sq ft at 2 Television Centre in White City, which is home to The White Company and Soho House who recently acquired space in this new building.
- 28% of deals were for space between 20,000 and 50,000 sq ft, comprising of six deals. (see Figure 1).
- The two largest deals in this size band were in excess of 40,000 ft. These included the letting at Chineham Gate, Basingstoke (49,500 sq ft) to Vyaire and the Office Group took 40,000 sq ft at 1 Lyric Square in Hammersmith. Lettings between 5,000 and 10,000 sq ft accounted for 23% of total take-up, with the average deal size 7,087 sq ft.
- The South East continues to see strong demand from the serviced office/co-working operators. Total take-up in the sector (since Q1 2017) now stands at 495,852 sq ft (see Figure 2). Q2 2018 has seen the greatest leasing activity from this sector at 138,800 sq ft. Spaces has been the most prevalent operator acquiring new premises making up 48% of leasing in this sector this quarter.
- Since 2010, annual levels of available space have decreased by 42%, this is because of the lack of supply across the region.
- Annual rental growth across the region can be found in key centres like Windsor (11%), Slough (9%) and St Albans (9%), where occupier demand and lack of supply are pushing up rents (see Figure 3).
- Occupiers continue to seek best quality space which many landlords/developers have embraced by delivering new or refurbished buildings that provide unique and more desirable space to differentiate from the market norm. We anticipate further rental growth in key towns against a backdrop of diminishing supply.

% TAKE-UP BY MARKET



% AVAILABILITY BY MARKET



TV | South M25 | West London | North M25 | SW London | NW London

VACANCY % AND TRENDS

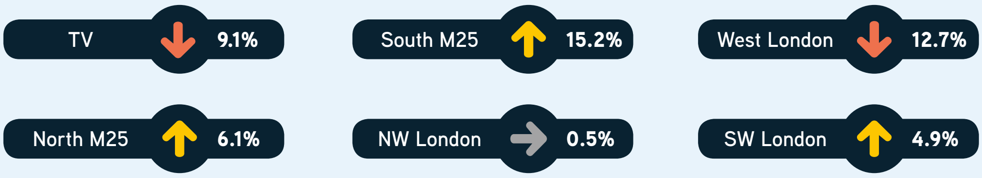


FIGURE 1: 2018 PERCENTAGE TAKE-UP BY SIZE BAND

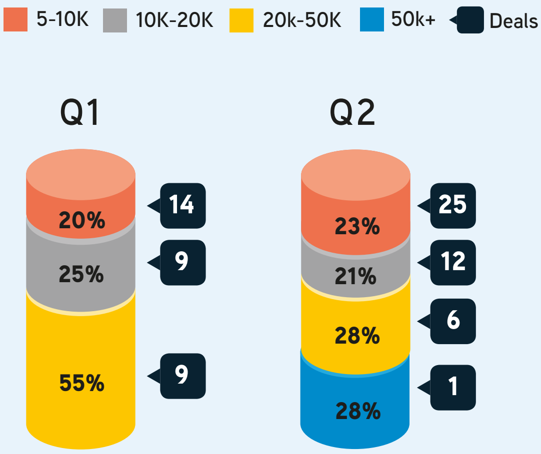


FIGURE 2: SERVICED OFFICE TAKE-UP Q1 2017-Q2 2018 (SQ FT)

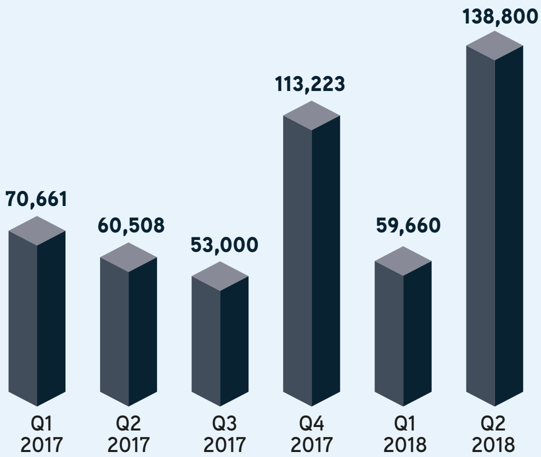
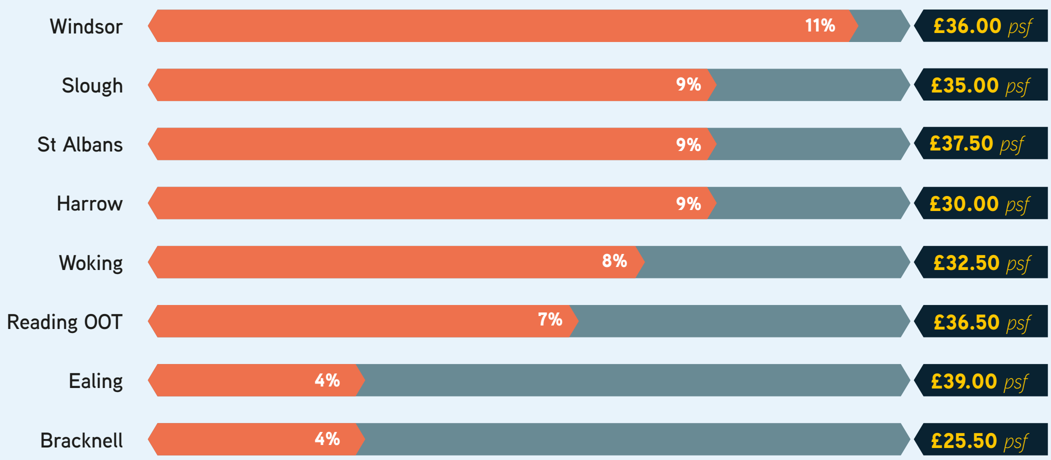


FIGURE 3: ANNUAL RENTAL GROWTH BY TOWN



TJX, Watford

Intu Shopping Centre, Watford

AREAS IN FOCUS
ST ALBANS AND WATFORD

Watford and St Albans are two of the key towns in the North M25. The total Watford office market is 3.5 million sq ft whilst St Albans has 1.05 million sq ft of stock. Both have seen substantial rental growth since 2015 with rents in St Albans increasing by 56% and by 38% in Watford. Both towns benefit from strong rail links into London, and have a strong town centre office market, tightly focused around the station.

Rents in the Northern M25 have historically trailed the core Thames Valley and South M25 markets, sitting between high teens to mid-£20's psf. Given the lower rental tone in comparison to the remainder of the South East, and subdued demand recovery since 2007, new development has not been viable. The office pool has reduced further as stock has been removed via Permitted Development and not been replaced with new development. Supply has become increasingly constrained, resulting in strong levels of rental growth in both of these key towns.

There have been no new developments in St Albans since 2007, and the only new build in Watford in the last decade was Clarendon Works, which was pre let during construction in 2017 to Salmon. The other key office development site opposite Watford Junction Station was purchased in 2016 by the town's major occupier, TJX to develop 150,000 sq ft for their own occupation, demonstrating their commitment to the town.

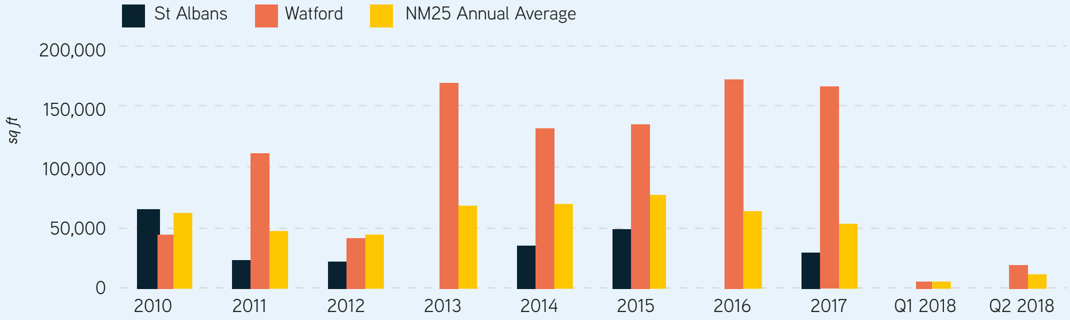
Watford Borough Council has recently committed to a redevelopment programme for the town centre. Over the next 10-15 years, more than £1.5bn will be invested in the town, including an extension of the Intu Watford shopping centre, extension of the Metropolitan Underground Line, and a major mixed use redevelopment of the land surrounding Watford Hospital.

St Albans saw over 60,000 sq ft of take up in 2017, which is almost twice the long term average of c.32,000 sq ft per annum, and exceeded the North M25 Town average for 2017. Key transactions included lettings to Apple, AECOM and Sherrard's Solicitors.

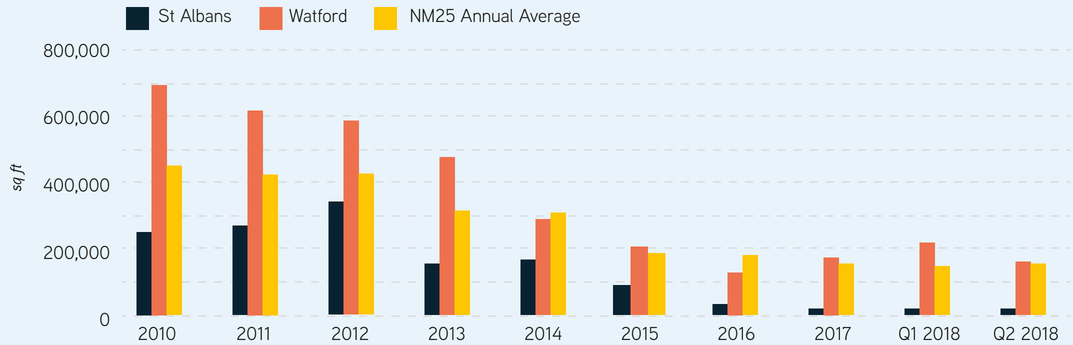
Given the strong market characteristics identified above, both Watford and St Albans continue to prove popular with investors. To put this in to context, in the past 24 months, Watford has witnessed 14 office investment transactions totalling £153 million whilst St Albans saw £39 million invested across three transactions. Prime net initial yields on Clarendon Road, Watford and in St Alban's town centre currently sit between 5.0% - 5.5%.

Prime rents in St Albans and Watford achieved in this cycle currently sit at £37.50 psf and £33.00 psf respectively.

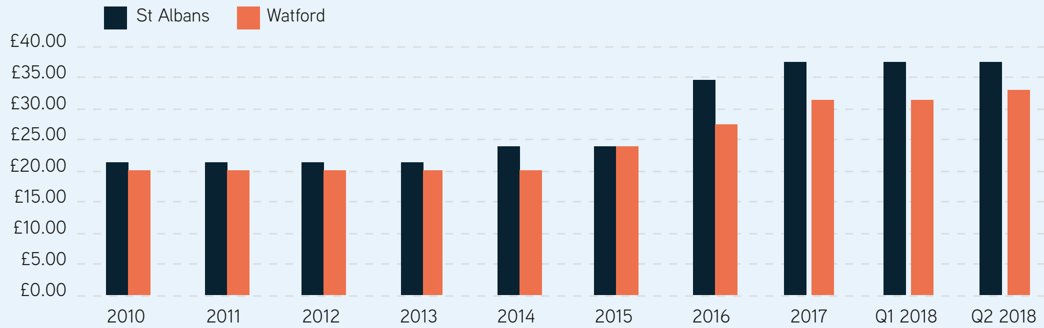
ST ALBANS VS WATFORD TAKE-UP TRENDS

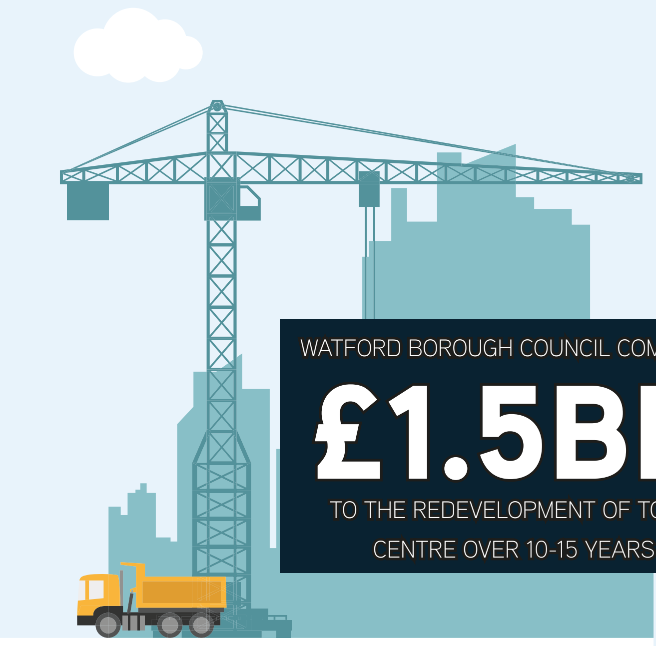


ST ALBANS VS WATFORD AVAILABILITY



ST ALBANS VS WATFORD RENTAL GROWTH

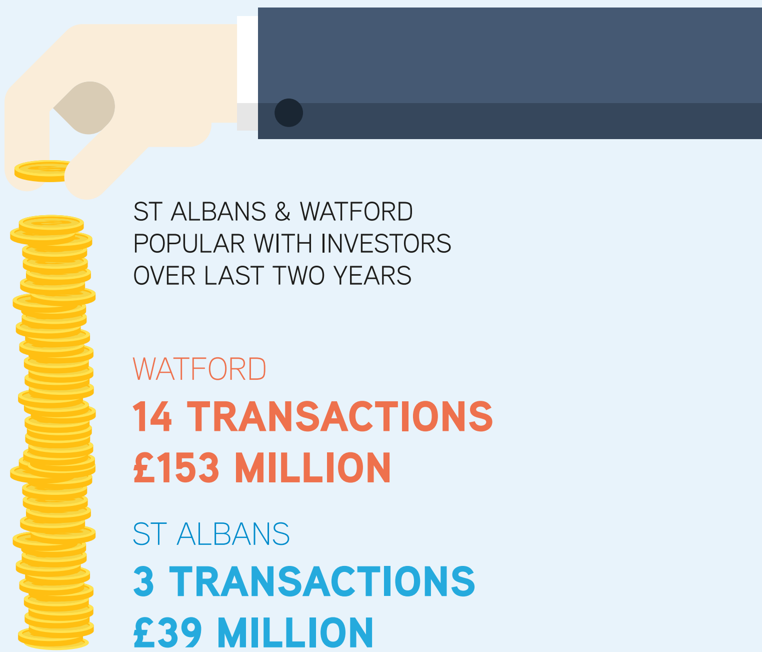




WATFORD BOROUGH COUNCIL COMMITED

£1.5BN

TO THE REDEVELOPMENT OF TOWN CENTRE OVER 10-15 YEARS



ST ALBANS & WATFORD POPULAR WITH INVESTORS OVER LAST TWO YEARS

WATFORD

14 TRANSACTIONS
£153 MILLION

ST ALBANS

3 TRANSACTIONS
£39 MILLION

INVESTMENT COMMENTARY

Q2 2018 witnessed 38 South East office transactions totalling approximately £690 million. This is a 15% decrease on Q1 volumes which saw 37 transactions totalling £810 million.

Transaction volumes and the number of deals are similar to the levels achieved in Q2 2017 which witnessed 40 deals and £700 million transacted.

The key trends for the second Quarter were:

- Strong appetite remains for secure multi-let town centre offices
- Limited supply of openly marketed investment opportunities
- A significant weight of money is still pursuing office investment opportunities in the South East
- Fewer Permitted Development opportunities being marketed although demand remains strong
- Varied buyer diversity with Financial Institutions, Property Companies, Private Investors and Councils all actively targeting South East offices
- Financial Institutions were busiest in the Quarter and responsible for 29% of all acquisitions
- Councils remain one of the key buyers of offices in the market
- An absence of Private Equity and Overseas Investors acquiring in the Quarter
- Prime net initial yields remain resilient at 5%

Five transactions accounted for £326 million, which is the equivalent of 47% of the total volume of all transaction in Q2. These included;

- Runnymede Council's acquisition of Pine Trees, Staines for £80.7 million
- Royal London's £78 million acquisition of Cambridge Research Park
- Lincoln MGT's £67 million acquisition of the 930,000 sq ft Station Hill, Reading redevelopment site
- Aberdeen Standard's £50.25 million acquisition of The White Building in Reading
- Runneymede Council's acquisition of the Volkswagen Financial Services UK HQ in Milton Keynes for £50.15 million

Whilst investor demand for South East offices remains strong, there are fewer sales being openly marketed which in turn has led to suppressed levels of transaction volumes. This trend has developed over the past two years where overall transaction volumes have been weighted to the second half of each year as evidenced in the graph below. This was particularly evident in 2017 when almost 70% of stock by value transacted in the second half of the year.

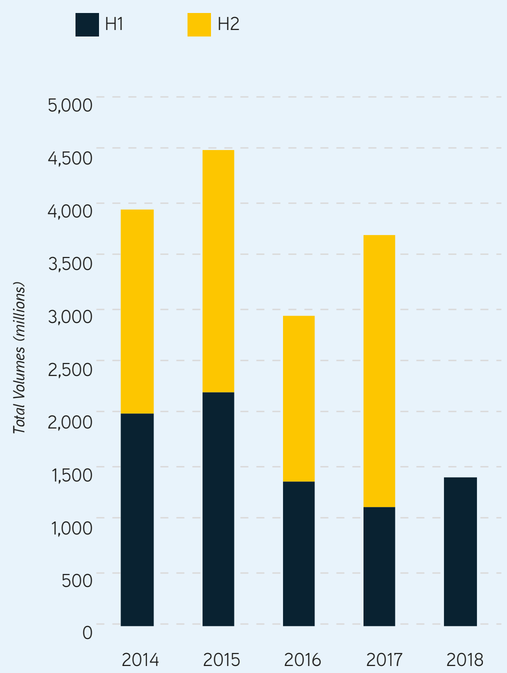
Financial Institutions continue to be the dominant buyer of South East Offices, accounting for 29% of all transactions in the Quarter. Other active investors in Q2 included; Property Companies (21%), Private Individuals (18%), Councils (13%), Owner Occupiers (11%), and Residential Developers (5%). There was a notable absence of Overseas Investors and Private Equity acquiring in the Quarter.

Another key trend for the Quarter has been the improvement in investor sentiment towards South East Offices. With the industrial sector undergoing significant yield compression, offices are increasingly looked at by investors as a sector where greater returns are achievable. With CrossRail nearing completion and a continued reduction of office stock through permitted development rights, many South East office markets continue to experience rental growth.

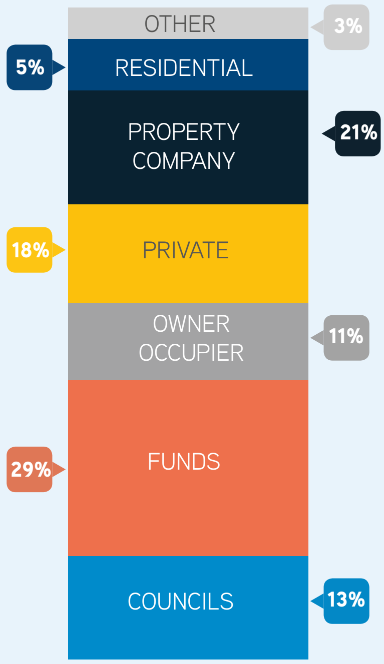
Councils have continued to show a strong appetite for long income single-let offices, most notably the £50.15 million acquisition of the Volkswagen Financial Services UK HQ in Milton Keynes by Runneymede Borough Council.

The secondary out of town office market has struggled in Q2 as investors have reservations regarding the possible effects of Brexit on the occupier market.

TOTAL ANNUAL TRANSACTION VOLUMES



NUMBER OF TRANSACTIONS BY INVESTOR TYPE (%)



Q2 2018 SE INVESTMENT HIGHLIGHTS

Size (sq ft) | AWULT to Expiry (Break) | Price | Net Initial Yield | Purchaser

PINE TREES, STAINES
- 170,000
- N/A
- £80,700,000
- N/A
- Runnymede Council

VOLKSWAGEN FINANCIAL SERVICES HQ, MILTON KEYNES
- 101,237
- 21.6 years (16.6 years)
- £50,150,000
- 4.83%
- Runnymede Council

CAMBRIDGE RESEARCH PARK, CAMBRIDGE
- 160,000
- N/A
- £78,000,000
- £488 psf
- Royal London

SIGMA HOUSE, BASILDON
- 161,986
- 11 years
- £28,250,000
- 6.55%
- Black Sand

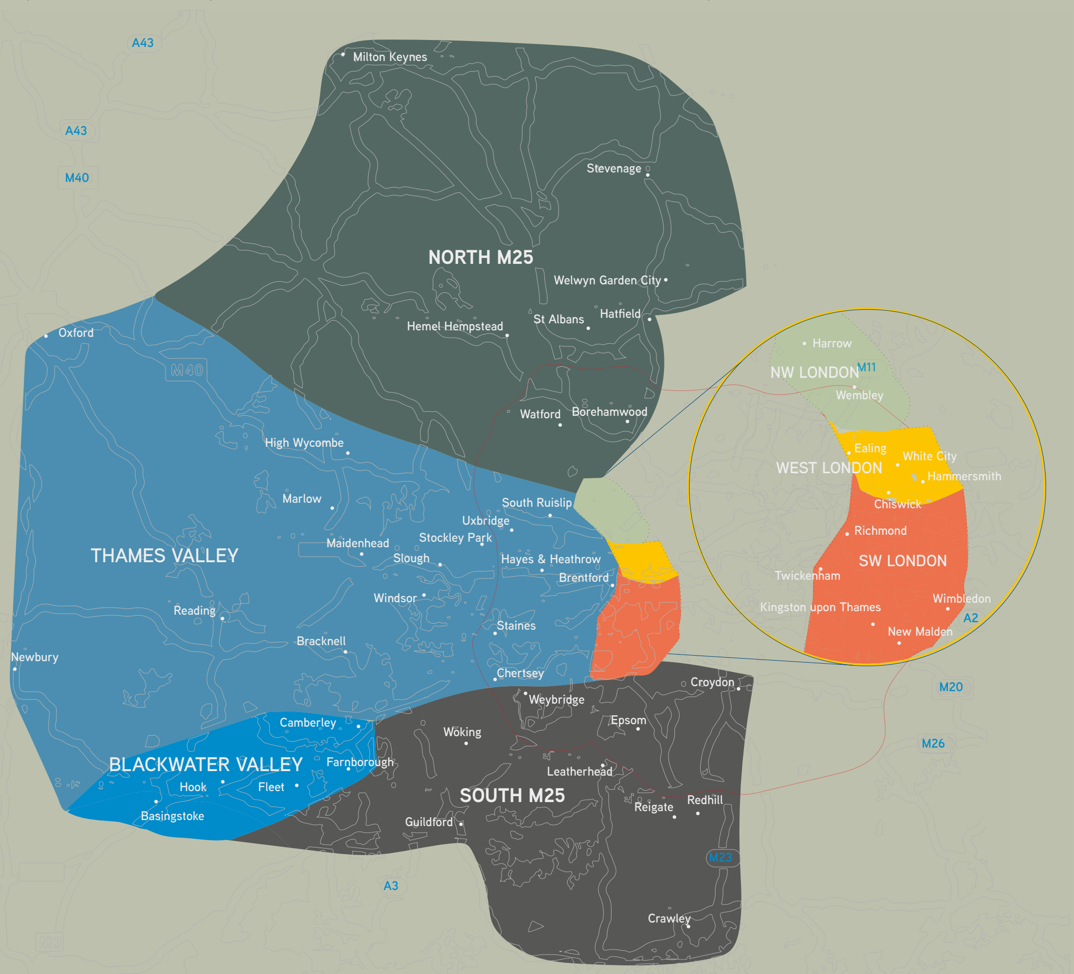
3 ARLINGTON SQUARE, BRACKNELL
- 67,376
- 7.2 years (3.4 years)
- £22,645,000
- 6.25%
- Orchard Street

AXIS ONE, LANGLEY
- 56,697
- 9.2 years
- £20,000,000
- 4.80%
- Runnymede Council

MOTT MACDONALD HOUSE, CROYDON
- 64,560
- 6.8 years
- £21,070,000
- 5.50%
- Rockspring

METHODOLOGY AND CHANGES TO STATISTICAL ANALYSIS

Colliers International South East Offices has changed our geographic boundaries to separate out NW London, West London and SW London. The map below provides a detailed representation of the towns and cities included in these groupings.



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