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“Prime yields compressed on average by 30bps.”

“Secondary yields showed mixed movements across sectors.”

## Executive Summary

- The July survey showed that property is still a buy with the South East as the most favoured region across all sectors. Selling remained very selective.
- For purchases, South East retail and offices were favoured by 64% of respondents, followed by South East industrial and Central London offices each by 50% and Central London retail by 43%.
- On the sell side, Welsh retail, North East offices and Yorkshire and The Humber offices were each favoured by 36% of respondents.
- The 2011 total return forecast was revised upwards to 6.2% pa (5.4% pa in March 2011 and 5.8% pa in November 2010).
- The 2012 total return forecast was revised to 7.0% pa from 8.2% pa in the March 2011 survey and from 9.2% pa in the November 2010 survey.
- Prime yields compressed on average by 30 bps, which went some way to counteract the outward movement of 20 bps that was seen in the March 2011 survey.
- Secondary yields showed mixed movements across the sectors with offices, business parks, retail shop units and retail warehouses moving outwards on average by 40 bps and secondary shopping centres, industrial and distribution compressing on average by 20 bps.
- Prime property was overpriced except for offices, but this is probably due to the Central London effect.
- Secondary offices, retail warehouses, industrial and distribution were underpriced, whereas secondary business parks, retail units and shopping centres were overpriced. The survey suggests selective buying opportunities in the secondary market.
- Rental growth for 2011 was downgraded across all sectors except for business parks and distribution. 2012 rental growth for the retail and office sector was downgraded.
- Capital growth for 2011 continued to be negative across all sectors except for offices and retail warehouses. 2012 capital growth forecasts were lowered across all sectors.
- Why invest in property now? 43% favoured property’s relatively high yield and 36% of respondents felt it produced a good income return.
- In response to the question on investing in good secondary property in the second half of 2011, responses were varied. 36% of respondents said that they would invest, 21% said they had already done so and the moment had passed, and 29% said that they were only looking for prime assets and were risk averse.
- 43% of respondents felt that the impact of the collapse of Southern Cross would have little effect on the investment in alternative (niche) real estate sectors.
- 36% of respondents felt that development activity outside of London would not happen for a couple of years.

# Investment Intentions

The survey indicates that property is still a buy, mainly focused on the South East and Central London. The South East was the most favoured region by respondents with 64% preferring offices and retail, followed by 50% targeting South East industrial. Central London was the next most popular region with 50% favouring offices and 43% retail.

The sell side was selective, with 36% of respondents targeting reduced exposure to Welsh retail, North East offices and Yorkshire and The Humber offices.

There is a broad polarisation, with the southern regions selected as purchases and the northern regions as sales. This, to an extent, reflects the level of economic activity and prospective job cuts in the public sector.

There continued to be muted interest in residential as a buy for Central London and the South East.

# Yield Levels

Prime yields compressed across all sectors by an average of 30 bps. Secondary yields moved out by 20 bps on average, but this disguised differential movement across the sectors.

The largest compression in prime yields was 60 bps for retail warehouses, followed by 50 bps for distribution. Retail units had the lowest yield of 5.1%, followed by retail warehouses at 5.5%. Prime business parks continued to have the highest yield of 7.4%, down from 7.6% in the March 2011 survey. The average prime yield was 6.1%, a decrease of 30 bps from 6.4% reported in the March 2011 survey.

The movement in secondary yields was varied, with offices, business parks, retail units and retail warehouses moving out on average by 43 bps and shopping centres, industrial and distribution moving inwards on average by 20 bps. The overall average movement was plus 20 bps. The largest outward yield movement was 80 bps for secondary retail shop units, followed by 40 bps for secondary business parks. The greatest compression was 40 bps for secondary industrials. The average secondary yield was 8.4%, a 20 bps increase from the 8.2% in the March 2011 survey. The highest secondary yield was for business parks at 9.7%, followed by distribution at 9.0%. The lowest secondary yield was 7.4% for retail units, followed by 7.5% for retail warehouses.

The gap between prime and secondary yields increased to 224 bps on average across all sectors from 182 bps seen in the March 2011 survey. The biggest change from the March survey was an increase of 90 bps in the prime vs secondary yield gap for both shops and retail warehouses. Industrial was the only sector that saw a reduction in the prime vs secondary yield gap (see Figure 1) from 260 bps to 230 bps. The largest gap between prime and secondary yields was 250 bps for distribution, followed by 240 bps for business parks. The smallest gap was 190 bps for shopping centres (see Figure 2).

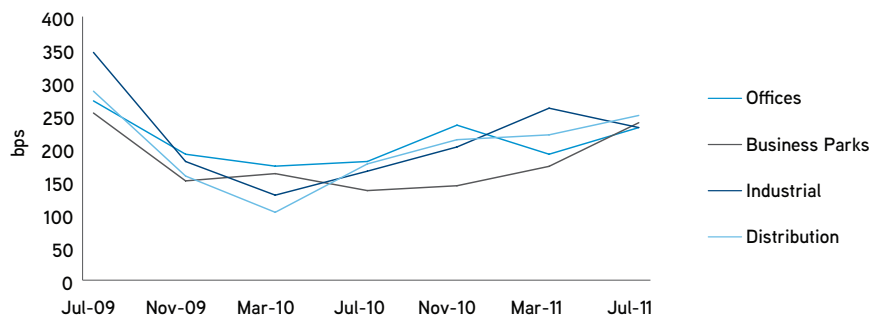
The survey suggests that prime property is overpriced across all sectors except for offices, but this is probably due to the Central London effect. Prime yields do not reflect the lower expectations for both capital and rental growth. Secondary offices, retail warehouse, industrial and distribution were underpriced, whereas secondary business parks, retail units and shopping centres were overpriced. The survey suggests that there are still selected buying opportunities.

Current Average Yield Levels %

Sector	Prime Rack Rented % pa	Secondary % pa
Offices	5.9 (6.0)	8.2 (7.9)
Business Parks	7.4 (7.6)	9.7 (9.3)
Retail Shop Units	5.1 (5.3)	7.4 (6.6)
Retail Warehouses	5.5 (6.1)	7.5 (7.3)
Shopping Centres	6.0 (6.3)	8.0 (8.1)
Industrials	6.6 (6.8)	8.9 (9.3)
Distribution	6.5 (7.0)	9.0 (9.1)

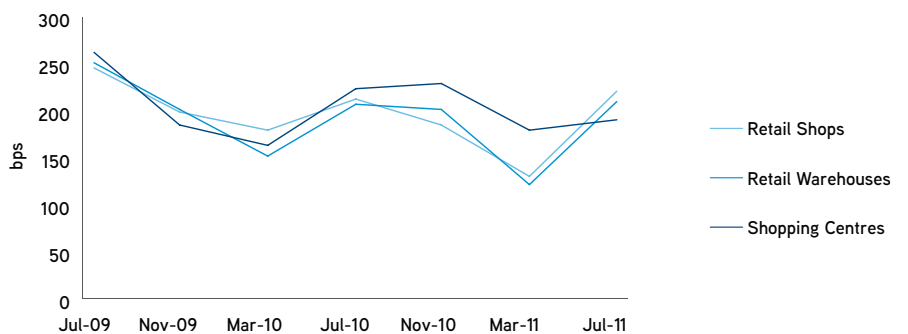
(March 2011 responses in brackets)

FIGURE 1: OFFICE AND INDUSTRIAL – PRIME VS SECONDARY YIELD SPREAD



Source: Colliers International/REC

FIGURE 2: RETAIL – PRIME VS SECONDARY YIELD SPREAD



Source: Colliers International/REC

## Rental Growth

Rental growth prospects for 2011 have been downgraded across all sectors except for business parks and distribution. Most of the rental upgrade seen in the March 2011 survey has been lost. The average change was a downgrade of minus 40 bps across all sectors. Most sectors are forecast to see negative rental growth, except for offices and retail warehouses. The greatest adjustment was in the retail sector with shopping centre rental growth being revised downwards by 100 bps, followed by shop units by 90 bps.

The best rental growth for 2011 was offices at 2.8% pa, followed by retail warehouses at 0.1% pa. The weakest rental growth for 2011 was for shopping centres at minus 1.1% pa, followed by retail units at minus 1.0% pa. The average rental growth across all sectors was minus 0.7% pa.

For 2012, rental growth was downgraded across the retail sector, with an average minus 110 bps adjustment, and the office sector with a minus 50 bps correction. The remaining sectors saw some upward adjustment – on average 20 bps. The average adjustment across all sectors was minus 50 bps.

The average rental growth for 2012 across all sectors was 0.9% pa. Offices continued to see the best rental growth of 3.0% pa, followed by distribution at 0.9% pa. Shopping centres were forecast to see 0.2% pa rental growth, which was the weakest submarket, followed by business parks at 0.3% pa.

In analysing the relative change from 2011 to 2012, retail units continued to see the strongest improvement, at 140 bps, followed by shopping centres at 130 bps. The smallest relative change was 70 bps for retail warehouses, which might suggest that the prospects for this sector have peaked. The retail sector analysis is interesting because it has seen the sharpest downgrades for 2011, but on a relative basis it is forecast to see the best improvement from 2011 to 2012.

### Latest Rental Growth Expectations – Average % pa

Sector	2011 % pa	2012 % pa
Offices	2.8 (2.9)	3.0 (3.5)
Business Parks	-0.9 (-1.2)	0.3 (0.2)
Retail Shop Units	-1.0 (-0.1)	0.4 (1.4)
Retail Warehouses	0.1 (0.9)	0.8 (2.2)
Shopping Centres	-1.1 (-0.1)	0.2 (1.2)
Industrials	-0.4 (-0.2)	0.7 (0.5)
Distribution	-0.2 (-0.2)	0.9 (0.6)

(March 2011 responses in brackets)

### Latest Capital Growth Expectations – Average % pa

Sector	2011 % pa	2012 % pa
Offices	1.5 (0.2)	1.6 (2.0)
Business Parks	-2.9 (-2.5)	-1.0 (-0.5)
Retail Shop Units	-1.4 (-1.5)	-0.2 (1.3)
Retail Warehouses	0.3 (-1.1)	0.2 (1.7)
Shopping Centres	-1.2 (-0.8)	-0.3 (1.2)
Industrials	-1.1 (-2.5)	0.3 (0.2)
Distribution	-1.5 (-2.5)	0.0 (0.3)

(March 2011 responses in brackets)

## Capital Growth

2011 capital growth forecasts remained in negative territory, except for offices and retail warehouses. Most capital growth forecasts improved from the March survey except for business parks and shopping centres, which were further downgraded. The average change across all sectors was 63 bps.

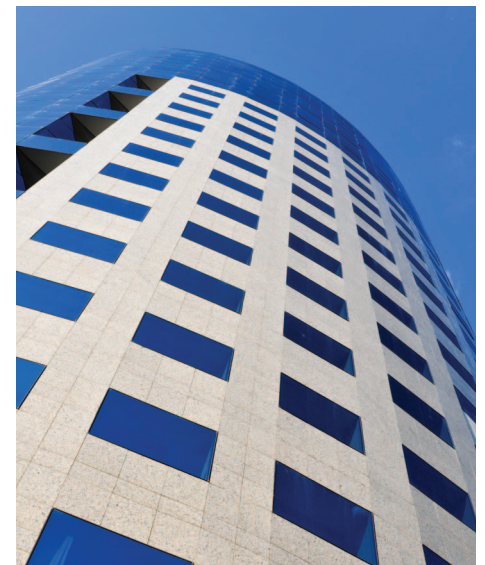
Offices are forecast to show the strongest capital growth for 2011 at 1.9% pa, followed by retail warehouses at 0.3% pa. The remaining sectors were all negative, with business parks the worst at minus 2.9% pa, followed by distribution at minus 1.5% pa. The average capital growth for 2011 was minus 0.9% pa.

Overall capital growth forecasts for 2012 saw improvement from the 2011 figures, although all sectors bar industrial show weaker forecasts than in the March survey. The biggest negative change was across the retail sector (shop units, retail warehouses and shopping centres), which was downgraded by 150 bps. The average change across all sectors was minus 80 bps.

The average capital growth for 2012 across all sectors was 0.1% pa. Offices continued to see the best capital growth at 1.6% pa, followed by

industrials at 0.3% pa. Business parks were forecast to see the worst capital growth of minus 1.0% pa, followed by shopping centres at minus 0.3% pa.

In looking at the relative change in the capital growth forecasts from 2011 to 2012, business parks saw the best improvement at 190 bps, followed by distribution at 150 bps. Business parks have fallen off the radar of many institutional investors – perhaps now is the time to have another look?



## Total Returns

The 2011 total return forecast was revised upwards to 6.2% pa from 5.4% pa in March 2011 and 5.8% pa in November 2010. The main factors contributing to this return were relatively evenly spread, with 36% of respondents citing income return and 21% of respondents each mentioning the slowing economy, flat capital values and limited growth in the occupier markets.

The 2012 total return continued to be revised downwards to 7.2% pa from 8.2% pa in March 2011 and 9.2% in November 2010. Contributing factors include: gentle rental growth (36%), rising interest rates (29%) and a gradual improvement in the economy (21%).

Why invest in property now? 43% favoured property's relatively high yield and 36% of respondents felt it produced a good income return. Other reasons given were diversification, hedge against inflation, real asset and better returns in the medium term.

43% of respondents said they would invest in any vehicles, jvs or derivatives. 50% of respondents offered no opinion.

## Topical Questions

Respondents were asked whether or not they would invest in good secondary property in the second half of 2011. 36% of respondents said "yes", 21% said that they had already done so and that the moment had passed, and 29% said "no" as they were risk averse and only targeting prime assets. Some said that secondary was not cheap enough; others felt that careful consideration needed to be given to lease length, tenant quality, location and other risk factors. 29% of respondents felt that the South East was a good area to look for good secondary, followed by the major provincial cities.

43% of respondents felt that the impact of the collapse of Southern Cross would have little effect on the investment in alternative (niche) real estate sectors. The alternative sector often differs due to specific operational property needs, the business model and the quality of management. Respondents felt that Southern Cross was not representative of the alternative sector, but some stated that the opco/propco model should be avoided. Southern Cross is a reminder of the risks involved and there will now be more emphasis on the property fundamentals, rental levels and re-lettability.

For the development market outside London, 36% of the respondents felt that it would recover in a couple of years. The favoured location was South East offices, by 29% of respondents, as well as the big six regional cities. Some respondents felt that patchy tenant demand would subdue development prospects.

## 512 offices in 61 countries on 6 continents

United States: 125  
Canada: 38  
Latin America: 18  
Asia Pacific: 32  
ANZ: 182  
EMEA: 117

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The Colliers International / Real Estate Capital Property Pricing Survey is in its eighteenth year. The survey analyses the pricing of the different property sectors for both prime and secondary product. Analysis is undertaken on yield levels, breaking down the capital and rental growth expectations and their relationship to total returns. Views on property investment compared to the other asset classes are obtained as well as on various topical property related issues.

This survey is unique. It analyses the views across the entire property investment community to provide a short term detailed market analysis of the industry's expectations for capital and rental growth. These results play an indispensable role due to the changing nature of the timing and pricing of property investment activity. There was a 18.1% response rate to the questionnaire which is above average.



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