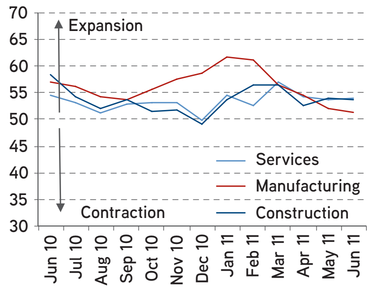
RESEARCH & FORECASTING UK

PROPERTY SNAPSHOT

Colliers INTERNATIONAL

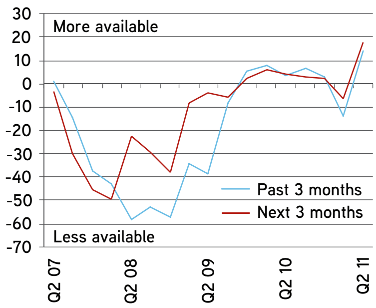
PURCHASING MANAGER INDICES



Source: CPI/Markit

"PMI data suggest limited economic expansion in Q2 11."

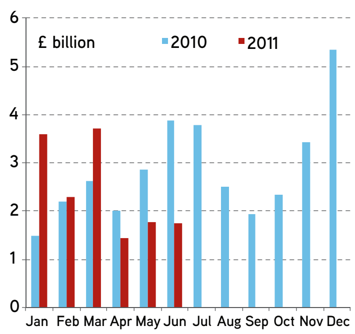
PROPERTY FINANCE EXPECTATIONS



Source: BOE, Credit Conditions Survey, Q2 11

"Investment levels have not regained momentum after the Easter break."

INVESTMENT TRANSACTIONS



Source: Property Data, 2011

"Few prime assets are available, but secondary offerings are gathering pace."

Economy

- Purchasing manager indices suggest limited economic expansion in Q2 11 GDP (est. 0.3% q/q). Services PMI was stable in June at 53.9, although Eurostat service sector confidence fell to -13.0 from -3.9 in May. Market sentiment is weak, the inflation outlook is benign and base rates are not expected to rise until mid-2012. CPI and RPI in April were stable at 4.5% and 5.2% respectively. Ten year gilt yields ended June at 3.42%, but are forecast to fall below 3%.
- Further quantitative easing is possible as GDP remains sluggish and money supply growth (M4) remains below target. Commercial lending to PNFCs fell in May by £4.9bn. Companies are hoarding cash and are reluctant to borrow due to fears about increased borrowing costs.
- Private employment rose by 104,000 in Q1 11, offsetting a public employment fall of 24,000. However the claimant count, rose in May for a third consecutive month to 1.49m, suggesting that private job creation may not be sustained. There are few signs of wage inflation.

Colliers view: Our April view remains unchanged. Increasingly sober UK economic views are impacting inflation and base rate expectations with further quantitative easing possible.

Investment

- The Bank of England Credit Conditions Survey shows improvement in debt availability for real estate in Q2 11. Further improvement is expected in Q3 11, although demand for finance is expected to be weak. The cost and availability of wholesale funds may be a constraint. Investment has not regained momentum after the Easter break. Year to date, volumes are similar to 2010 by value, but Q2 11 is down by 40% against Q2 10. Few prime assets are available, but secondary asset offerings are gathering pace.
- Retail: High Street: Few deals completed in June. In Edinburgh, 77-79 George Street sold to Pfizer's pension fund for £3.4m at 5% IY. Shopping Centres: Two deals completed in June; Old George Mall in Salisbury was sold to a fund for £80m at 6% IY and a group of assets with food and value retailers in secondary locations was sold to New River Retail for £60m at 8% IY. Secondary assets are attracting numerous bidders. Retail Warehouses: Funds bought several B&Qs at yields between 6% (Acton/Leyton) to 6.9% (Plymouth). The Crown Estate bought Morfa RP in Swansea with mixed open A1/bulky goods consent for £80.2m at 5.8%. DTZ IM bought a Wolverhampton retail park for £40.1m at 5.75%. Funds remain keen on retail parks.
- Offices: Redevelopment and receivership are main themes. City/Midtown: Oxford Properties bought a 50% stake in 71 High Holborn for £141m at 5.5% IY and NAMA sold 1 King William Street for £67.5m at 5.6% IY. These look like the only straight income deals. St Katherine's Estate, with expiring leases, was sold to a JV for £156m. Receivers sold 6-8 Bishopsgate with lease expiries in 2015 for £95m at 7% IY. BL bought Wardrobe Court with a lease expiry in 2014 as a residential resale or redevelopment opportunity for £57m at 4.7% IY. USS acquired a redevelopment project at 110 Canon Street for £48.5m. West End: 35 Marylebone High Street was sold to Scottish Widows for £32.2m (BBC to vacate in 2012); Newcombe House in Notting Hill was bought for £47.5m at 3% IY with a mixed-use redevelopment in mind; and Eastborne Terrace in Paddington was acquired for £76m by a pension fund with an eye toward the adjacent Crossrail development. Regions: Fairly quiet, but British Land purchased Grefell Island in Maidenhead for £74m at 7.5% and receivers have sold Aztec West in Bristol for £14.6m at 8% IY to a private investor. A few regional office secure income sales may be imminent.
- Industrial: A private fund bought a 586,240 sq ft Sainsbury's distribution hub in Sherburn-in-Elmet for £43.3m at 6.35% IY (15.5 years income). Private investors also bought a DHL warehouse near Heathrow for £24m at 5.85% IY. In the multi-let sub-sector, two portfolios changed hands with asset/tenant management opportunities. DTZ IM purchased a small portfolio for £28.5m at 7.6% IY (20% vacancy rate). M7 also purchased a portfolio for £9.5m (30% vacancy rate).

Colliers view: Transactions are limited, but receiver stock is on the market with many deals linked to redevelopment and asset/tenant management opportunities. Yields are stable, although secondary is expected to weaken over the course of H2 11.

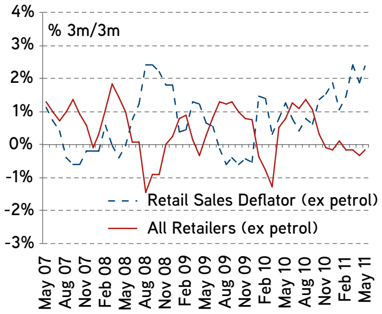
Occupier markets

RETAIL

- The household savings ratio fell again from 5.1% in Q4 10 to 4.6% in Q1 11. Households may be saving less due to decreasing real disposable income, which also fell in Q1 11 by 2.7% y/y. Households are squeezed and retailers continue to struggle. Retail sales (ex-petrol) were down 1.5% q/q in May across most sub-sectors, although non-store sales were up 1.9%.
- With some exceptions, operator profits are suffering. Jane Norman is in administration, Haldanes has filed for administration, and TJ Hughes issued a notice of intent. Thorntons is to close 120+ stores, Life & Style, 22 stores and Comet, 17 stores. Administrations are well off 2009 levels, but trading is tough. Operators are looking at new formats, services and reviewing local performance. John Lewis sales soared by 18.2% in late June as clearance sales began.

Colliers view: Retailers continue to face difficult trading and tight margins as consumers look for value. Costs are undermining profits and operators are looking at new formats and services.

RETAIL SALES VOLUME GROWTH



Source: ONS

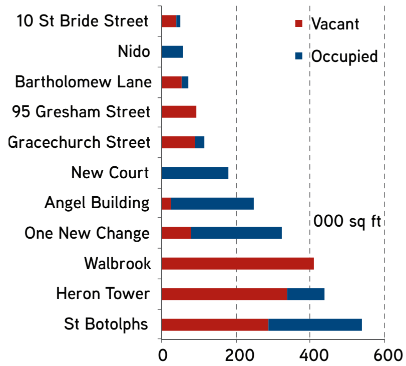
"John Lewis reports that sales soared as clearance discounting began."

OFFICES

- City: Take-up improved in Q2 11, due mostly to Aon's 191,000 sq ft letting. Incentives and headline rents (£57.50 psf) are stable. Aside from Aon, no letting over 35,000 sq ft was reported in the City Core in Q2. Heron Tower rents have reached £62.50 psf.
- West End: With leasing completing at Central St Giles and Regent's Place, most activity is linked to churn. Headline rents have reached £95 psf with Grade A space scarce. Rents are also rising in non-core areas with new Soho schemes set to change the area's rental tenor.
- Regional: Demand in Birmingham is improving; the Law Society is looking for 60,000 sq ft. Lack of Grade A space in Glasgow and Bristol has potential occupiers looking at non-core areas; Bristol may see an increase in pre-letting. Elsewhere, leasing is sluggish.

Colliers view: The West End is seeing rental growth in all sub-markets due to lack of Grade A space. The City is less pressured. Region leasing is sluggish with vacancies stable, but high.

CITY COMPLETIONS 2010 - 2011



Source: Colliers International

"Over 50% of all new space released in 2010 and 2011 is under offer or occupied."

LOGISTICS & INDUSTRIAL

- SMEs are not expanding and not taking on new debt due to worries about increasing capital costs. SMEs may be hoarding cash and may soon become self-financing. In the absence of organic growth, trade counters are seeing M&A activity with Travis Perkins acquiring BSS for £558m, creating the largest UK plumbing and heating company.
- Supermarkets and food processors are looking for space, as well as internet firms consolidating and centralising distribution. Amazon took 700,000 sq ft from Gazeley in Rugeley, leaving few Grade A alternatives in the Midlands. 'Design and builds' are dormant, although land banks are growing. London and the M25 continue to look 'bubble-like' as steady demand outstrips supply.

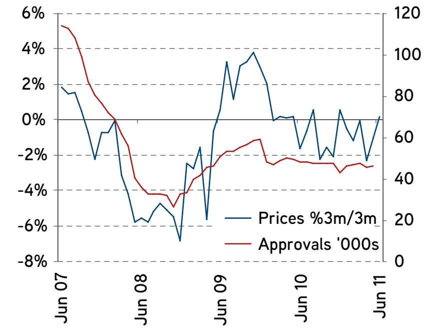
Colliers view: Sector indicators are positive, but demand is patchy except for supermarkets and internet sales distributors who are absorbing the remaining large Grade A large floorplates.

Residential

- The RBS Halifax derivative curve changed little in June and continues to suggest a 6.5% price fall in 2011. Mortgage approval rates were unchanged in May at around 45,000. Re-mortgaging increased slightly, suggesting that house refinance is supporting lifestyles. Mortgage arrears fell by 6.7% y/y in Q1 11 to 337,060. Banks though are less discretionary, with 'forbearance loans' falling from 4,013 in Q1 10 to 1,638 in Q1 11. Foreclosures are up slightly.
- Central London residential remains resilient. Sales to overseas private investors is strong. The London rental market is also very strong and the FT reports that London & Stamford plans to invest in private rental accommodation in London by providing finance to cash strapped developers.

Colliers view: House price stability remains very sensitive to interest rates, mortgage availability and wage growth. Price declines are expected in 2011, although London continues to attract investors.

HOUSE PRICES AND MORTGAGE APPROVALS



Source: Halifax, BOE, Colliers International

"Banks are less discretionary, with forbearance loans falling from 4,013 in Q1 10 to 1,638 in Q1 11."

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