PRIME LOGISTICS

The definitive guide to the UK's distribution property market
Q3 2017 Bulletin

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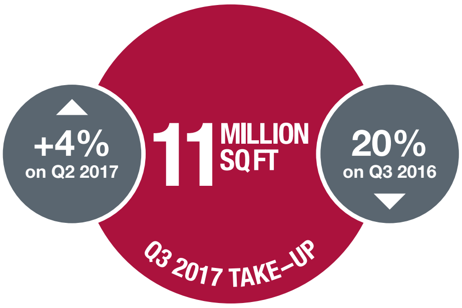
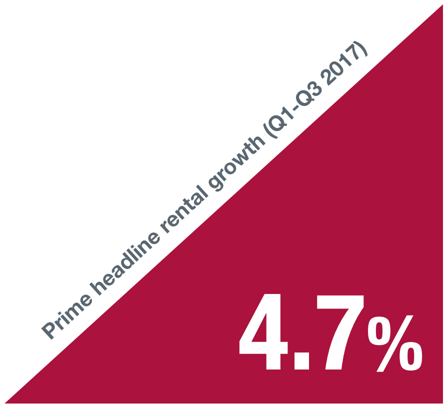
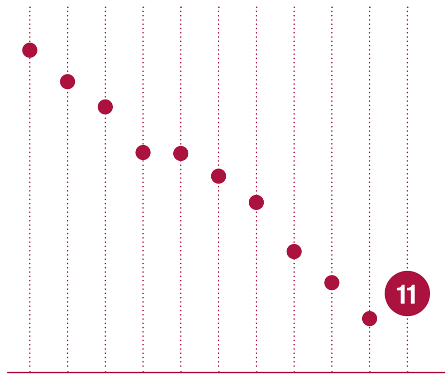






11 month void period on spec developed space

DEPTH TO OCCUPIER DEMAND

Overall take-up recorded during Q3 2017 increased 4% on Q2 to 11 million sq ft and is illustrative of a relatively busy summer period for the logistics property occupational market. Whilst occupier demand has undoubtedly softened in comparison to the record–breaking 2016, Q3 take-up was in line with the 5 year quarterly average and 11% above the 10 year quarterly average.

Regionally, occupier demand continues to be focused on core markets – specifically the West Midlands, where 3.6 million sq ft was taken-up over 16 buildings. We also saw an increase in demand for logistics facilities in key locations in London and the South East during Q3, with sharp increases in take-up recorded in London West and Buckinghamshire & Bedfordshire.

By their own standards, Amazon has been less acquisitive so far in 2017 and the retail and wholesale sector only accounted for 23% of all Q3 activity. Instead, it was manufacturing occupiers, in particular the pharmaceutical, automotive and food manufacturers, which drove demand and accounted for 39% of all quarterly activity.

INCREASED OCCUPIER ACTIVITY ON SPEC DEVELOPMENTS

During Q3, we continued to see the supply shortage shape the profile and nature of demand. Occupiers with large requirements for space, such as Jaguar Land Rover, Lidl, H&M and Nestlé, have all made commitments to develop bespoke facilities over 500,000 sq ft during Q3 and pre-lets and development sales accounted for 42% of all Q3 activity.

At the other end of the spectrum, another knock-on effect of the supply shortage is that we have seen an increase in the number of buildings taken-up below 100,000 sq ft in size. The recent addition of a number of smaller speculatively-developed and refurbished buildings to the market has provided occupiers with more choice and we have seen several of these smaller buildings taken-up during Q3.

Such activity has also drastically affected the rental profile of certain locations. We have seen a step-change in rents recorded in certain locations such as Reading, and, across the UK, prime rents grew by an average 1.9% during Q3. This takes the average prime rental growth rate to 4.7% during 2017, which has already surpassed our 4% forecast growth rate made at the start of the year.

SPEC SUPPLY INCREASES AVAILABILITY

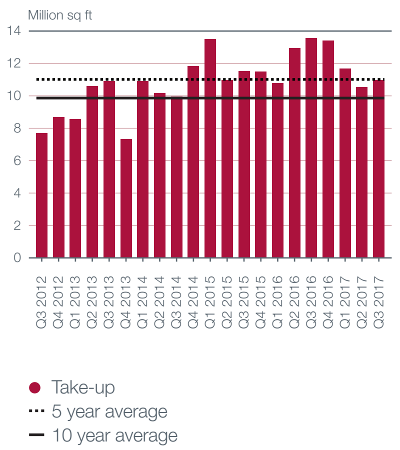
The overall UK availability rate rose for the second consecutive quarter from 6.2% to 6.5% at the end of Q3. This increase was driven by the addition of new speculatively-developed and recently refurbished space to supply, rather than the release back to the market of secondhand space, which, to date, has been limited.

15 buildings totalling 1.6 million sq ft completed development speculatively during Q3, with a relatively small average size of 104,000 sq ft. Whilst we have seen robust levels of occupier interest in such space, given the intense investor interest in funding such schemes and the commensurate expected uptick in future starts, we are closely monitoring the speed with which such developments let.

Since the end of 2013, the average void period on speculatively-developed space has fallen sharply. However, since Q3 2016, the time on the market of such space following development completion has started to rise and stood at an average of 11 months at the end of Q3. Developers remain targeted and measured in the schemes they start speculatively.

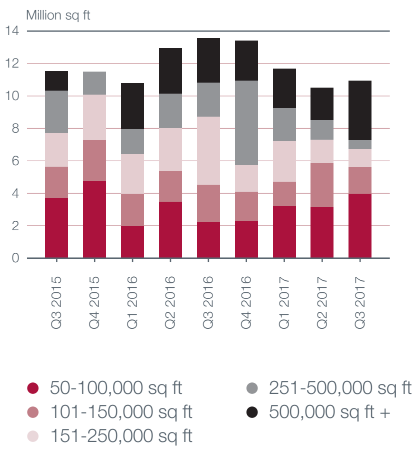
Quarterly take-up and 5 and 10 year average Q3 2012 – Q3 2017

Source: Gerald Eve



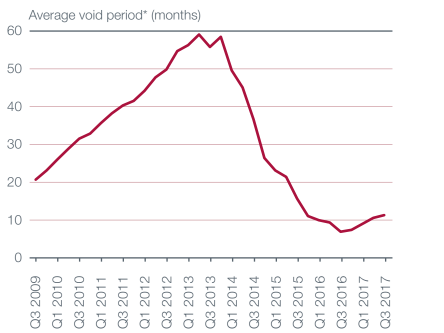
Quarterly take-up by size band, Q3 2015 – Q3 2017

Source: Gerald Eve



Average void period of speculatively developed space, Q2 2009 – Q3 2017

Source: Gerald Eve



** For this calculation, the void period runs from PC and speculative developments let during construction are given a zero month void period*

Development completions Q3 2017

8.3M SQ FT

Q3 2017 KEY INVESTMENT TRANSACTIONS

Property	Purchaser	Vendor	Price (£m)	Size (sq ft)	Yield (%)	Tenant
Light Industrial	Blackstone Real Estate	Brockton Capital	559.0			Various
Cabot Portfolio	LondonMetric Property	Cabot Properties	116.6	13,992,599	6.1	Various
Prologis Ryton	West Mids Pension Fund	Network Rail	35.8	302,025	4.89	Network Rail
City Park, Welwyn Garden City	L&G	Aviva	27.0	202,336	5.42	Various
Team Valley Industrial Estate	Teeside Pension Fund	BMO Real Estate Partners	16.2	207,808	5.22	Royal Mail
Lister Road, Basingstoke	BMO	CBRE GI	9.6	58,504	5.15	Bunzl
Watford Trade Park	Morden College	JPR Group	8.5	28,524	4.47	Various

Sources: Gerald Eve, Property Data

RECORD VOLUME OF QUARTERLY DEVELOPMENT COMPLETIONS

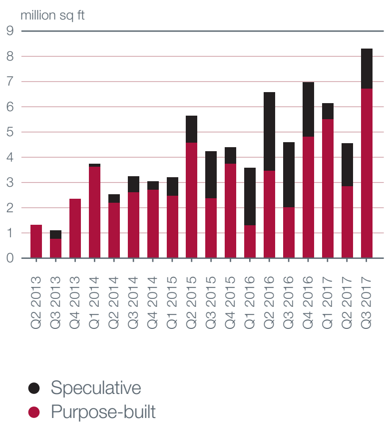
8.3 million sq ft completed development during Q3 over 35 buildings, the largest volume of space to reach practical completion in one quarter on record. This follows on from the record number of pre-lets and development sales agreed last year and Q3 volumes were driven by Amazon completing on two large buildings – a multi-storey 2.2 million sq ft facility in Tilbury and a 1.1 million sq ft warehouse in Doncaster.

In terms of speculative development completions, the overall volume completing remained relatively flat compared to Q2 at 1.6m sq ft. Whilst we are seeing speculative developments come through, the average building size is small and given their predominantly core locations they are proving of interest to occupiers.

In terms of development starts, internet and discount food retailers are driving activity, with Amazon and Lidl each adding more than 1 million sq ft to quarterly volumes on their schemes at Central Park, Avonmouth, Eurocentral and iPort in Doncaster.

Quarterly development completions by type, Q2 2013 – Q3 2017

Source: Gerald Eve



STRONG INVESTMENT MARKET FUNDAMENTALS

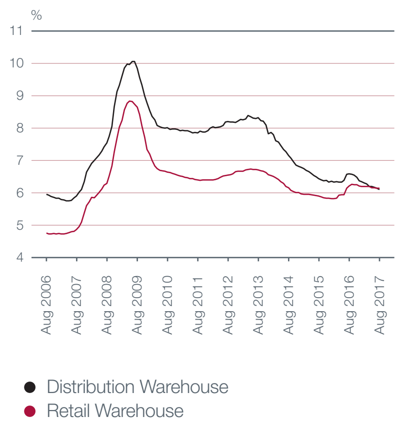
Robust occupational fundamentals, together with the ongoing structural change to internet retail have resulted in high levels of domestic and overseas investor demand. However, there remains a shortage of investible stock, which has limited the volume transacted and has pushed pricing to record highs.

According to MSCI, July was the first time since the early 1990's that the average equivalent yield for distribution warehouses was sharper than retail warehouses. This highlights the difference in investor appetite for the two asset classes, but is also illustrative of the changing nature of how consumers are shopping.

Investors are looking to find value through thematic approaches such as favouring buildings let to one specific tenant sector or restricting their target geographies. Prime core plus and value-add opportunities are all high on the agenda and there is an increased appetite for platform deals. Such is the strength of demand, that there could be further inward yield movement in core locations before the year is out – despite yields already sharpening in most locations since the start of 2017.

Monthly equivalent yields, Aug 2006 - Aug 2017

Sources: Gerald Eve, MSCI



OUTLOOK

Whilst occupational conditions have softened compared to 2016, there are several good reasons to be positive about the outlook for logistics property. Perhaps most encouraging is the fact that the relatively subdued nature of demand from internet retailers has been off-set by other sectors such as manufacturers and discount retailers so far this year. There is a depth to demand beyond internet retail.

What has also been encouraging is the response of developers. We are seeing an increase in the number of speculative schemes getting underway, but these are by-and-large, appropriately-sized buildings for the demand profile in a given region and purpose-builds continue to dictate development activity. The speculative schemes that are being delivered to the market are generating strong occupier interest and occupiers are paying the rents necessary to secure such space. We have seen occupiers agree to commit to longer lease terms and increased headline rents in return for a share of the impact such a commitment would have on the investment yield profile of the building. Given the strength of investor interest, this is a tenant tactic we could see more of.

As we approach the end of the year, take-up looks set to be down by around 10% on 2016, prime rents on average look set to rise by more than 5% and with one of the highest forecast total return of all asset classes over the next five years, investor interest in logistics looks set to remain elevated to year-end. Whilst pricing is relatively high, the outlook for the sector remains positive. We expect investors to continue to be attracted to the postive effects of the strong occupational dynamics on investment performance.

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GERALD EVE IN THE MARKET

Gerald Eve is well-established in the logistics property market and covers the full range of property services, from national occupational and investment agency through to lease consultancy and valuation. Our specialists have been involved in several high profile transactions during the quarter. Please contact them directly for more information.

John Rodgers advised LGIM on its acquisition of City Park, Welwyn Garden City, a multi-let industrial estate totalling 202,336 sq ft across nine units for £27m reflecting a 5.42% net initial yield.

Mobile +44 (0)7810 307422

Jason Print advised distribution and warehousing specialist RJ Edwards on the letting of 101,000 sq ft at Appleton Thorn in Warrington.

Mobile +44 (0)7833 170680

Josh Pater advised SEGRO on the disposal of two units at Gatwick Airport Distribution Centre totalling over 123,000 sq ft.

Mobile +44 (0)7782 271355

INDUSTRIAL & LOGISTICS CONTACTS

Agency

London
Mark Trowell
Tel. +44 (0)20 7333 6323
mtrowell@geraldeve.com

David Moule
Tel. +44 (0)20 7333 6231
dmoule@geraldeve.com

Josh Pater
Tel. +44 (0)20 3486 3473
jpater@geraldeve.com

Midlands
Georgina Harrington
Tel. +44 (0)121 616 4833
gharrington@geraldeve.com

North West
Jason Print
Tel. +44 (0)161 830 7095
jprint@geraldeve.com

South West & Wales
Richard Gatehouse
Tel. +44 (0)29 2038 1863
rgatehouse@geraldeve.com

Scotland
Sven Macaulay
Tel. +44 (0)141 227 2364
smacaulay@geraldeve.com

Investment
John Rodgers
Tel. +44 (0)20 3486 3467
jrodgers@geraldeve.com

Nick Ogden
Tel. +44 (0)20 3486 3469
nogden@geraldeve.com

Lease Consultancy
Chris Long
Tel. +44 (0)20 7333 6444
clong@geraldeve.com

Ian Gascoigne
Tel. +44 (0)121 616 4812
igascoigne@geraldeve.com

John Upton-Prowse
Tel. +44 (0)20 7333 6248
jupton-prowse@geraldeve.com

Rating
Keith Norman
Tel. +44 (0)20 7333 6346
knorman@geraldeve.com

Valuation
Richard Glenwright
Tel. +44 (0)20 7333 6342
rglenwright@geraldeve.com

Research
Steve Sharman
Tel. +44 (0)20 7333 6271
ssharman@geraldeve.com

OFFICES

London (West End)
72 Welbeck Street
London W1G 0AY
Tel. +44 (0)20 7493 3338

London (City)
46 Bow Lane
London EC4M 9DL
Tel. +44 (0)20 7489 8900

Birmingham
Bank House,
8 Cherry Street
Birmingham B2 5AL
Tel. +44 (0)121 616 4800

Cardiff
32 Windsor Place
Cardiff CF10 3BZ
Tel. +44 (0)29 2038 8044

Glasgow
140 West George Street
Glasgow G2 2HG
Tel. +44 (0)141 221 6397

Leeds
1 York Place
Leeds LS1 2DR
Tel. +44 (0)113 244 0708

Manchester
No1 Marsden Street
Manchester M2 1HW
Tel. +44 (0)161 830 7070

Milton Keynes
Avebury House
201-249 Avebury Boulevard
Milton Keynes MK9 1AU
Tel. +44 (0)1908 685950

West Malling
35 Kings Hill Avenue
West Malling
Kent ME19 4DN
Tel. +44 (0)1732 229423

Prime Logistics is the definitive guide to the UK's distribution property market. Dealing with logistics units of 50,000 sq ft and above, this research report gives detailed analysis and statistics for 26 key distribution areas – from take-up, stock and development statistics to drivers of occupier demand, growth forecasts and regional outlooks. All previous editions can be downloaded from our website.

United States and European Alliances

Gerald Eve has an international alliance with Lee & Associates who have offices in 56 US and Canadian cities and a number of Europe alliance partners in 20 cities across 12 European countries.