

# Occupancy levels continue to recover leading to rental growth

May 2014

- **Industrial take up increased by 24%**
- **Regional office take-up in Q1 2014 is holding strong at 7% higher than the five-year average**
- **Out-of-town take-up in the regions was 651,000 sq ft, 6% up on the five-year average**

Continuing improvement in the UK economy is set to have a material impact on the commercial property market. Data confirms that the initial boost to the economy was largely provided by the housing market and consumer spending. The expected shift in an improving economic landscape is that growth will principally be driven by business investment through 2014.

It is this growth in business investment which is predicted to have the greatest impact on the property market, with occupiers in the industrial and office sectors expected to acquire new premises to feed growing staff numbers and business activity.

GVA's Big Nine report confirms that regional office take up is now 7% ahead of the 5 year average from 2008 with out of town up 6%. With industrial take up increasing at even greater levels the lack of speculative development since the financial downturn is putting pressure on supply and therefore rental levels.

IPD figures suggest rental growth in all three main sectors of the property market through both 2014 and 2015, of 1.9% and 2.0% respectively. Leading the charge on the increases is the office sector at nearly 5% and 4% for each year. Industrial shows a more steady performance at 0.7% and 0.8% with retail lagging behind at 0.3% before progressing further in 2015 to 1.3%.

It is the lack of development outside central London since 2008 putting pressure on the top performing centres in terms of availability. LSH report a market imbalance in terms of supply and demand in the industrial sector in the West Midlands, North West, South East, East and London. This trend can be seen clearly in the strong regional office centres also.

Increases in take up and rents should see yields continue to harden through 2014 providing further scope for a further year of yield driven capital growth. However the occupier recovery is far from even across all regions in the UK and therefore examination of the micro economies is an essential part of stock selection.

## Focus on Finance

In the debt markets, the availability of senior and mezzanine debt continues to improve and competition is bringing margins down further. Overcrowding in the core is focusing more interest on higher risk markets as lenders old and new jostle for opportunities and this competition only looks set to increase given the number of debt funds raised in 2013.

It is problematic to provide current typical available rates given the individual nature of debt finance, but increasing competition should certainly be of benefit to the property investor.



## What they're saying

Much has been made by market commentators about the availability of investment stock or rather, lack thereof. **Cushman & Wakefield** however, sound a cautious note of optimism:

*"Some signs of an improvement are now tentatively being seen, with some profit taking on existing stock for example as well as interest in new development in some cases".*

**DTZ** note the continuing trend of investors willing to spend outside of the M25:

*"The yield gap between prime London and prime regional offices is at record levels. This is encouraging investors to move up the risk curve and acquire more non-London assets. Prime yields have fallen in most regional markets over the last six months. We expect further compression in 2014"*

**GVA** director comments on the economic impact in the regional markets:

*"GVA director and head of national offices Carl Potter said: "It is great to see that, after such a strong rebound in 2013, there is little sign that the positive sentiment is set to abate. The economic conditions for growth are right, business confidence is high, and the employment market is recovering well, so it is great to see that the UK's Big Nine cities are all thriving and continuing to push ahead."*

The generally positive sentiment on the UK commercial property market is echoed by the institutional investors. Philip Nell, manager of the **Aviva Investors Property Trust** Comments:

*"The UK commercial property market is in a very buoyant phase. It is encouraging to see the return of domestic investors over the last few months, with a significant increase in demand from the UK institutional sector. Some UK private investors are back in the market, even the banks are more positive about lending. Indeed, the net balance of lenders increasing rather than decreasing funding levels is probably at one of the highest levels seen since the credit crisis began in 2007".*

## Any Questions

We hope that this has provided some food for thought and if you have any queries about the investment market or property management please:

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## Around the Regions: Manchester

Manchester is the largest commercial property sector outside of London – historically associated with the textile industry and scientific research base; it is now increasingly growing off the back of Technology, Media and Telecoms (TMT) expertise.

Growth has been driven by the establishment of MediaCityUK in Salford Quays, providing a new base for the BBC and ITV. As a result, an important digital media and gaming sub-sector has emerged and larger technology companies are also showing interest in the city.

An entrepreneurial spirit is fuelling demand for office space in Manchester, particularly in the Piccadilly, Castlefield and Northern Quarter areas. Occupiers which have previously been reluctant to invest capital in expansion are now expressing confidence in the wider regional and national economic picture.

In addition, more money is being attracted into the area, benefiting from a pool of skilled university graduates and a positive culture for industry and trade. Renewed investment from landlords has seen vacancies fall and average rental prices rise, providing good returns for commercial property investors.

However, the supply of office space in Manchester remains constricted by lack of supply, with availability down 15% in 2013 and likely to decline further. New build projects should help to temper this shortage.

Much of the future growth is expected to come from the clustering of SMEs across the city; these occupiers prefer more affordable units, typically in second-hand buildings and this is where LRI see the opportunity for investors.