PRIME LOGISTICS

The definitive guide to the UK's distribution property market
Q2 2017 Bulletin

Quarterly summary

- Q2 take-up rises 5% to 11.3 million sq ft
- 'Amazon effect' pushes volumes over 5 year quarterly average
- Increase in demand for smaller buildings recorded during Q2
- Return of a handful of large secondhand buildings increases availability rate
- Prime rent rises recorded in 20 of 51 centres
- Q2 speculative development starts increase by 129% to 2.2m sq ft
- Intense investor interest drives further prime yield compression
- Pricing premium on 'opportunities of scale'

International Property Consultants

GERALDEVE

TAKE-UP RISES 5% ON Q1

Overall take-up in Q2 2017 increased to 11.3 million sq ft, a 5% increase on both Q1 and the 5 year average quarterly volume. Regionally, it was take-up in the West Midlands which drove this total – with 29 individual deals and almost 3.5 million sq ft transacted in the region during Q2. Demand for logistics property in core markets remains robust, however volumes have softened when matched up against the record-breaking totals of 2016.

We also saw a significant increase in activity in the South West during the quarter, driven largely by Amazon's 33.5 acre land purchase at Central Park in Avonmouth where they intend to develop a 2.2 million sq ft multi-storey warehouse. This deal was crucial in elevating overall volumes to the heightened 'new normal' levels and highlights the importance of internet retail and Amazon in particular to overall occupier demand.

Only one other deal over 500,000 sq ft was agreed during Q2, as XPO Supply Chain, servicing a contract for Premier Foods, let a 645,000 sq ft unit in Tamworth from Logicor. The majority of deals agreed were on smaller buildings during the quarter.

ACTIVITY ON SMALLER SHEDS DRIVES DEMAND

51% of all occupier demand during Q2 was for buildings below 150,000 sq ft in size and the average size of building taken fell to 138,000 sq ft. This is a significant drop in average deal size and is reflective of the increased demand for smaller sheds either for urban logistics or for those in the manufacturing supply chain.

We saw 32 individual buildings taken by manufacturing occupiers during Q2. Those in the automotive sector were particularly acquisitive, as Honda (UK) signed up to 400,000 sq ft in Swindon and, in total there were nine transactions involving automotive manufacturers agreed during the quarter. We saw Aston Martin, Michelin, Grupo Antolin and Charge Automotive all commit to space totalling 1.3 million sq ft.

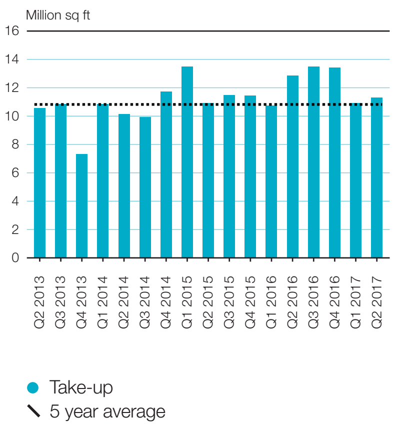
Linked to this increase in manufacturing demand, we have also seen a continuation of increased take-up of secondhand space during Q2, which accounted for 46% of all activity. The amount of recently- refurbished space taken-up also increased as landlords' decisions to refurbish properties were vindicated and almost 1.5 million sq ft of such space was taken-up during the quarter.

SMALL INCREASE IN AVAILABILITY RATE

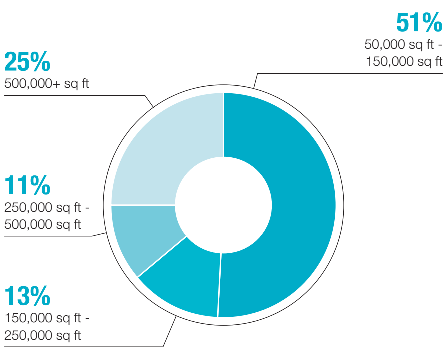
The overall rate of available space recorded a small increase during Q2 2017, to 6.2%. This increase was driven by the return of a handful of large secondhand buildings to the market – such as Sheffield 615 in South Yorkshire, the 500,000 sq ft Tesco NDC in Chesterfield and Warrington 379 in Greater Manchester. Even the addition of just a few buildings has made a material difference to the overall rate. In times of strong pre-letting activity such as we have seen over the last 18 months one would expect the return of some unwanted secondhand stock back to the market. Up until now, we have not seen such space returned, as tenants have occupied space to maximum efficiency and the net absorption of logistics space remains positive.

Also driving the small increase in availability was an increase in the amount of speculative development completions delivered to the market during Q2 – with 1.7 million sq ft over 9 buildings reaching practical completion, the largest of which was the 372,000 sq ft M6DC building in Cannock. However, despite The Range completing their 1.2 million sq ft purpose-built regional distribution hub at Central Park in Bristol during Q2, overall development completions fell by 26%.

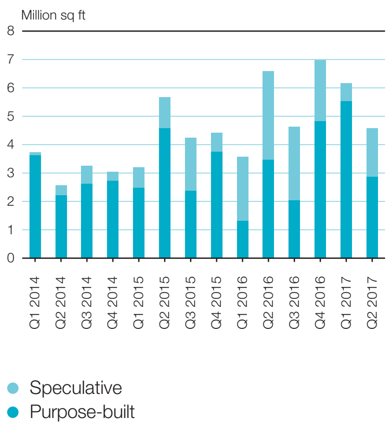
Quarterly take-up and 5 year average, Q2 2013 – Q2 2017
Source: Gerald Eve



Q2 2017 take-up (by volume) and by size band of property transacted
Source: Gerald Eve

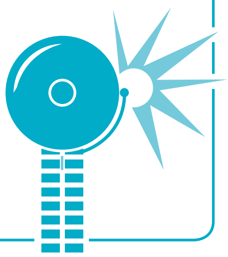


Quarterly development completions by type, Q1 2014 – Q2 2017
Source: Gerald Eve



129%

Increase in speculative development starts in Q2 2017



Q2 2017 KEY INVESTMENT TRANSACTIONS

Property	Purchaser	Vendor	Price (£m)	Size (sq ft)	Yield (%)	Tenant
Ultrabox portfolio	Oxenwood Real Estate	Lone Star	286.0	3,869,906	5.4	Various
Industrials.co.uk portfolio	Stenprop	Morgan Stanley RE	127.0	1,999,951		Various
Hams Hall, Coleshill	Korean consortium	Christian Vision Charity	100.0	699,983	5.2	Sainsbury's
Birch Coppice, Tamworth	Tritax	Undisclosed	92.3	699,983	5.3	Ocado
Kingston Park, Peterborough	Gulf Co-operation Council	DVS Property Ltd	86.4	736,688	5.8	Debenhams
Accolade Park, Avonmouth	CSUK1 Holdings Ltd	Keller Group Plc	62.0	871,981	6.5	Accolade Wines
Radway Green, Crewe	Korean consortium	Crewe Assets	56.0	349,991		BAE
Priestley Way, London	Legal & General UK PF	Undisclosed	51.9	250,909	6.2	JVCKENWOOD
Feilden House, Teal Park, Lincoln	Siemens Ltd	Dimah Capital (Kuwait)	35.0	135,992		Siemens

Sources: Gerald Eve, Property Data

SPEC DEVELOPMENT STARTS INCREASE

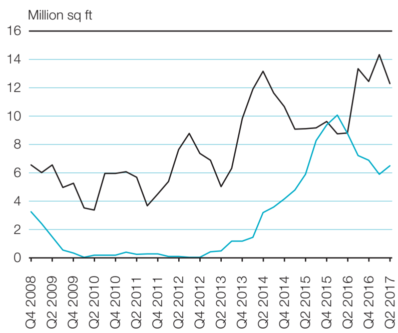
2.2 million sq ft of space got underway speculatively during Q2 – a 130% increase on the 970,000 sq ft which started during Q1. 18 individual buildings got underway speculatively during Q2, which both by count and by overall size, is the most speculative space starting in one quarter since Q3 2015. Speculative development drove the development market during Q2, representing 70% of all development starts by volume.

The average size of speculative development start was 124,000 sq ft, an increase on the 81,000 sq ft average size of building getting underway in Q1. This is reflective of the geographical location of these units, several of which were in the Midlands, although Bucks & Beds and Berkshire & Wiltshire also saw some significant speculative activity commence.

A range of developers started speculative space during Q2, including SEGRO, IDI Gazeley, Stoford and db Symmetry. The largest building to start development during the quarter – purpose-build or speculative – was at Magna Park in Milton Keynes where IDI Gazeley started construction of their 575,000 sq ft speculative unit.

Rolling four-quarter development starts by type, Q4 2008 – Q2 2017

Source: Gerald Eve



Purpose-build
Speculative

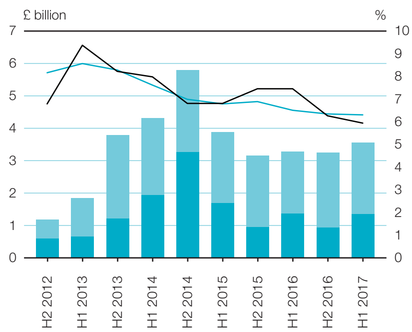
INCREASED YIELD COMPRESSION FOR SHORT INCOME AND 'CRITICAL MASS'

There remains a significant weight of capital, both domestic and overseas, targeted at the sector. Logistics property remains one of the most attractive asset classes out of all commercial property sectors and prime yields have hardened further, particularly in locations where demand continues to outweigh investment supply. We recorded prime yield compression in 24 out of our 49 centres during Q2 2017 and in Heathrow and Park Royal we have seen prime yields fall to 4%.

During H1 2017, we have recorded over £3.5 billion of industrial property transactions, including seven deals over £100 million in size. We have also seen yields harden at a faster rate on shorter income opportunities so far in 2017 as the concept of 'optionality' and increasing value through asset management has increased investor competition. Given the number of investors wishing to get large scale exposure, logistics is one of the few sectors which attracts a 'portfolio premium' and we have seen increased yield compression on average transacted portfolio yields compared to single-let assets.

Portfolio and industrial volumes and average transacted yields H2 2012 - H1 2017

Sources: Gerald Eve, Property Data



Industrial investment volume
Portfolio investment volume
Average portfolio yields (RHS)
Average industrial yields (RHS)

2017 OUTLOOK

Compared to H1 2016, take-up is down 4% at the half way point of 2017 and we envisage that 2017 demand will be down by around 10% on the record-breaking 2016. Whilst we have seen an encouraging number of smaller deals agreed so far in 2017, there is also a heavy reliance on the large scale pre-lets to keep volumes above average.

We have seen the number of speculative development starts increase during Q2 as investors continue to see it as an effective way to get exposure to the sector and have become comfortable with the difference between the development yield and up-and-built yield. The level of speculative development completions expected this year looks set to be about half the volume which completed during 2016, so we could see more speculative funding in H2 2017 to help meet demand.

The key pinch-point however, especially for last-mile delivery services, remains the loss of industrial space to higher value uses such as residential and the restricted availability of sites. Operators want to get as close as possible to 'chimney pots' – and often the more affluent areas – but it is those same locations which are seeing pressure for residential development. Innovative arrangements such as 'beds and sheds' and multi-storey facilities are expected to become increasingly attractive in such circumstances.

Such is the perception by the broader investment market of the relative strength of logistics property, particularly when compared to other commercial property asset classes, that we expect continued investor interest even if occupier demand doesn't match the volumes recorded in 2016.

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.

David Moule
advised Sicame UK on a 64,417 sq ft leasehold design and-build scheme on a 3.2 acre plot at Goodman's London Medway Commercial Park.

Mobile +44 (0)7905 764910

Nick Ogden
advised Columbia Threadneedle on its disposal of a 182,000 sq ft warehouse on the eastern M62 which was let to XPO Logistics.

Mobile +44 (0)7825 106681

Josh Pater
advised Ocado on the acquisition of a 60,000 sq ft unit at City Park, Welwyn Garden City.

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

Midlands
Richard Ludlow
Tel. +44 (0)121 616 4802
rludlow@geraldeve.com

Myles Wilcox-Smith
Tel. +44 (0)121 616 4811
mwilcox-smith@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
John Upton-Prowse
Tel. +44 (0)20 7333 6248
jupton-prowse@geraldeve.com

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

Chris Long
Tel. +44 (0)20 7333 6444
clong@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.

Prime Logistics is a short summary and is not intended to be definitive advice. No responsibility can be accepted for loss or damage caused by any reliance on it.

GERALDEVE