

RESEARCH



GLASGOW

OFFICE MARKET REPORT
2016





“Let Glasgow flourish’ has never been more apt as the city’s reputation as a business and lifestyle destination continues to grow.”

JOHN RAE
Managing Partner,
Knight Frank Glasgow

FOREWORD

With autumn approaching fast and the furore surrounding the EU referendum calming, it is an opportune time to consider the health of the Glasgow property market.

The EU vote was just the latest in a seemingly endless line of major political events that have affected market sentiment over the past two years. Despite these distractions, the office market in Glasgow has continued to flourish with occupiers, investors and developers across both the Grade A and secondary markets maintaining strong interest in the city.

On the occupational side, the Morgan Stanley and AXA acquisitions provide the best recent example of major corporate occupiers committing to the city. Both have secured new long-term space in the expanding CBD taking close to 200,000 sq ft between them. Notably, occupiers migrating into central areas from the fringe are further fuelling demand in the CBD. Weir Group, Scottish Power, Global, WSP and Edrington Group have all relocated in recent deals. These large-scale occupiers have moved their operations from the periphery into core CBD locations principally to provide their staff with the best working environment and importantly, place them close to the other thriving elements of Glasgow such as the retail and leisure scenes. The trend of increased amenity attracting occupiers will continue.

Back in 2012/13, Glasgow was one of the first UK regional cities to see speculative development restart. Abstract, BAM and Clearbell/M&G moved first with the development of three buildings totalling over 500,000 sq ft. It seemed a brave move at the time, but has brought success. This confidence has provided the catalyst for the next wave of new development although there will be a two year lag before new Grade A stock comes to market. This means that the refurbishment market will stay active, driving up rents in this subsector.

The lack of available Grade A stock is also stifling potential inward investment. This combined with the perceived threat of Scottish independence, has meant that inward investment has consistently fallen since the peak of 2006. A joined up approach to development between the local authority, Scottish Enterprise and Invest Glasgow is required to raise Glasgow’s profile further and allow the city to compete within the competitive UK, regional and international market.

Retention of ‘home grown’ Scottish talent cultivated in the leading Scottish universities will additionally aid in this goal. Today Glasgow is a fantastic city and offers an across the board attraction to occupiers and their staff. Construction of international class office buildings within an expanding CBD supports the attraction and retention of global occupiers.

The city must also drive forward as a ‘lifestyle destination’. The retail provision is one area that has improved greatly. The emergence of areas such as Finnieston, recently voted ‘the hippest’ place in the UK to live, is also testament to the advances the city has made. These successes must be built upon and through the continued support of new development combined with infrastructure improvement, Glasgow’s position as a truly global city will be cemented.



OCCUPATIONAL MARKET

Despite concern over the EU referendum, office take-up in the first six months of 2016 reached the highest recorded for an H1 period. Supply remains low and this imbalance is maintaining upward pressure on rents.

Take-up and demand

Total take-up across city centre and out-of-town areas amounted to 806,700 sq ft at mid-year 2016 – 16% greater than at the same point last year. In the centre alone, take-up reached 475,000 sq ft, more than double the amount recorded during the equivalent period in 2015 (fig 1). Supporting the high level of take-up has been some large-scale deals with four transactions exceeding 20,000 sq ft completing in the city core in H1 2016. This compares to just two during the same period of 2015.

The largest deal in 2016 was at 122 Waterloo Street, the first phase of Bothwell Exchange, where Morgan Stanley agreed a pre-let with HFD Property Group on 154,800 sq ft. Morgan Stanley will be decanting from surrounding buildings to occupy their new headquarters in 2018.

Also in Q1 2016, accountancy firm ACCA acquired 55,750 sq ft at 110 Queen Street on a 10 year lease, this is now the first of the three speculative developments to achieve full occupation. 1 West Regent Street attracted a string of occupiers including Weir Group, CMS and Shepherd & Wedderburn with only a small amount of space remaining available. Abstracts St Vincent Plaza also

attracted Registers of Scotland, Whyte & Mackay and KPMG who took the uppermost floors totalling 39,000 sq ft. In addition, Cuprum at 480 Argyle Street is now fully let following the letting to AXA who secured 49,250 sq ft.

Availability

As at September 2016, total availability stood at 1.95m sq ft, 22% less than at the same point in 2015. Notably, this represents the lowest level of overall availability since Q3 2014. Availability of Grade A space has now fallen to the lowest level on record with only 125,000 sq ft currently available within the city core.

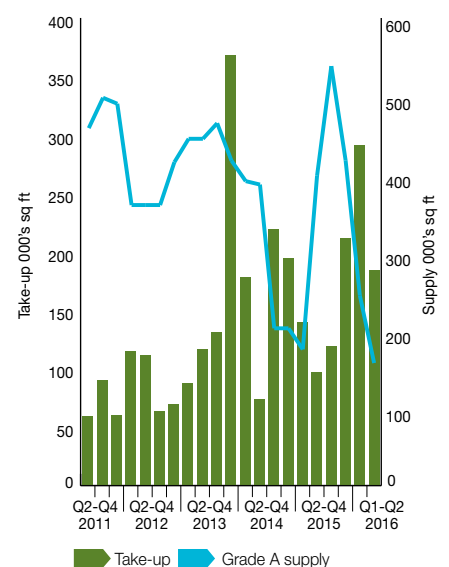
At the time of writing, there are no speculative developments under construction. As such, the development pipeline consists of refurbishment projects of Grade B stock. Over 250,000 sq ft is currently underway within the city core including 50,000 sq ft at 100 Queen Street and 38,000 sq ft at 58 Waterloo Street.

Headline rents

As at the end of Q2 2016, prime headline rents remained at £29.50 per sq ft. Current forecasts indicate that prime rents may surpass £30.00 within the next 12 months given the lack of new quality supply.



FIGURE 1
Glasgow office take-up



Source: Knight Frank Research/Property Data

Major leasing transactions (last 12 months)

Building	Tenant	Sq ft	Rent (per sq ft)	Date	Grade
122 Waterloo Street Bothwell Exchange	Morgan Stanley	154,800	Not known/confidential	Q1 2016	A
110 Queen Street	ACCA	55,750	£28.50	Q1 2016	A
Cuprum, 480 Argyle Street	AXA	49,250	£20.00	Q2 2016	A
St Vincent Plaza	KPMG	39,700	£24.00	Q4 2015	A
100 Queen Street	Edrington Group	30,000	Not known/confidential	Q3 2016	A

Source: Knight Frank Research

INVESTMENT MARKET

The number of office investment deals completed in 2016 has been low, clearly affected by concern over the EU referendum.

Investor sentiment noticeably cooled in the run up to the EU vote with the outcome only serving to solidify the 'wait and see' approach. A consequence of this stance has been that investment volumes reached just £70m at mid-year, 45% less than at the equivalent point in 2015 (fig 2).

The largest investment deal of 2016 to date has been the sale of 2 West Regent Street to TIAA Henderson for £31.50m reflecting a NIY of 5.84%. The multi-let Grade A property sits within an improving micro area in the CBD and had a WAULT of 6.52 years.

Following this sale, another multi-let office, The Grosvenor Building on Gordon Street, was bought by UBS for £17.85m in April 2016. The deal reflected a NIY of 6.9%. Comprehensively refurbished to provide Grade A specification, occupiers included Cigna (offices) and HBOS with Sainsbury's signed up to takeover HBOS' unit immediately on lease expiry. Tellingly, all other office investment transactions completed in the first half of 2016 were below £10m.

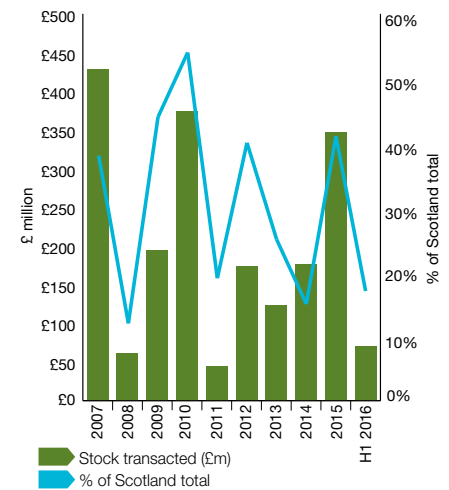
A notable trend of the past few years following the financial crisis has been growth in overseas investors. Foreign buyers accounted for over one third of purchasers in 2015, although in 2016 market disruption has meant activity has

slowed. We anticipate that overseas interest will rise as market sentiment improves, particularly given the recent depreciation of sterling.

At the mid-year point, prime yields were settled at 5.50%, a level 100 basis points above the market peak of 4.50% recorded in 2007. However, the EU referendum and the traditional summer holiday has meant that examples of new prime investment opportunities coming to market have been few. As more stock comes to market we expect deal numbers to rise and yields to harden.

FIGURE 2

Glasgow offices investment volumes



Source: Knight Frank Research/Property Data



50 Bothwell Street sold to Fore Partnership

Major investment transactions in Glasgow (Q3 2015-YTD 2016)

Building	Price (£m)	Yield %	Date	Purchaser	Vendor
Atlantic Quay	60.70	8.54	Sep 2015	Moorfield REF III LP	M&G Real Estate
Cadogan Street, 19	33.40	5.25	Oct 2015	Amundi Real Estate	Union Investment RE
West Regent Street, 2	31.50	5.84	Mar 2016	TIAA Henderson	Kennedy Wilson Europe
Cadogan Street, 5	23.85	6.01	Dec 2015	Private overseas	M&G Real Estate
50 Bothwell Street	23.25	8.41	Sep 2016	Fore Partnership	M&G Real Estate
Gordon Street, 72	17.85	6.89	Jun 2016	UBS Asset Management	Standard Life UK REF

Source: Knight Frank Research/Property Data

KNIGHT FRANK VIEW

Vibrant, amenity rich and well connected; Glasgow is a city in demand. Evolution of the city is continual, embracing both the needs of modern firms and the local residents. Glasgow can truly boast of being a city capable of competing on the world stage.



JOHN RAE
MANAGING PARTNER

"Whilst there is undoubtedly caution in the market in the aftermath of the Brexit result we do continue to see strong interest for Glasgow offices both in investment and occupational markets. I believe that the lack of Grade A stock combined with the absence of new development will see us witness rental growth within the Grade B+ markets with rents moving towards the mid £20s and incentives reducing. With the potential for a handful of best in class Grade A buildings to trade over the next 12 months we will see a litmus test for the Glasgow market and I believe that we will see yields achieved in line with other major UK cities."



COLIN MACKENZIE
PARTNER

"There is now only a limited amount of new Grade A stock available in the city, currently only in two buildings. This means we are at least 24 months away from any new stock and this is still subject to funding being secured. This is a great opportunity for owners / buyers of current stock to refurbish to a Grade A standard to capture occupiers in this tier. There are some standout examples coming through the design / construction stage at the moment that will no doubt win out if the owners have the confidence to spend fully to create the right environment."



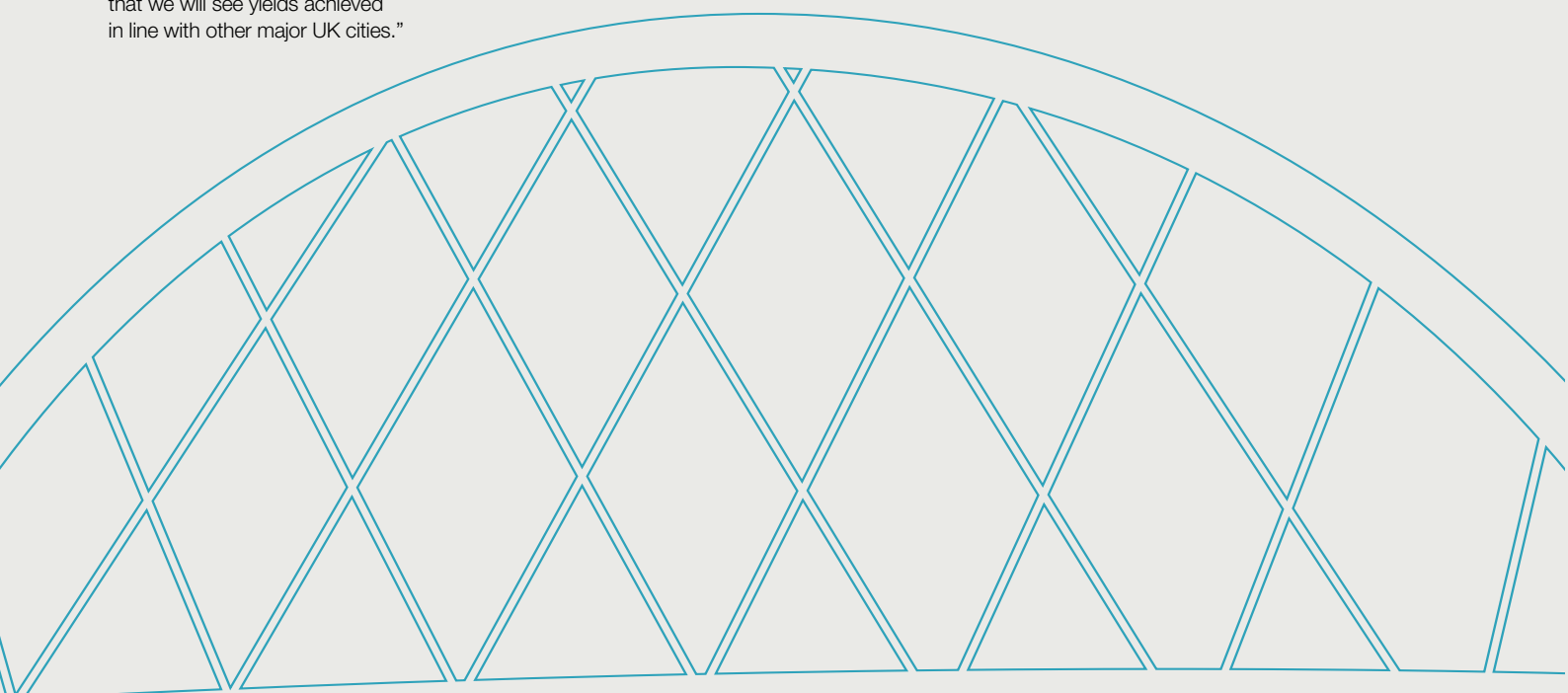
PATRICK FORD
PARTNER

"Glasgow is seeing continued interest from overseas funds and private investors, who are targeting large lot sizes over a range of asset types ranging from "Trophy" to "Core-plus" and "Value add". Glasgow has a history of attracting foreign investors owing to the robust fundamentals of the Glasgow office market. Further, these investors are seeking to capitalise on the post-Brexit market which offers a favourable exchange rate combined with income yields that are exceptionally attractive in comparison to Gilt yields which are at a record low level across the board."



PETER LEBURN
ASSOCIATE

"The lack of office stock especially in Grade A or upper size bracket (50,000 sq ft plus) will mean that for the first time in Glasgow occupiers will not have a readymade choice of Grade A office stock to consider. There is a genuine need for occupiers to consider their occupational strategy at an earlier stage as they may have to commit to refurbishments underway or even pre-letting which to date has been very limited in Glasgow with the exception of the very largest occupiers."





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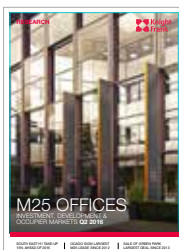
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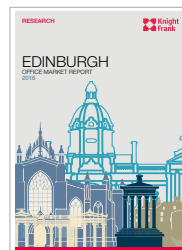
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