RESEARCH

WINTER 2012

ABERDEEN

Industrial market activity report

Knight Frank

HIGHLIGHTS

- The buoyancy of the North Sea oil & gas industry has fuelled strong demand in Aberdeen's industrial market. Building on 2011's strong performance, take-up is projected to reach a 10-year high of 800,000 sq ft in 2012.
- Strong demand has put significant pressure on existing supply. As a result, an increasing number of occupiers have had to relocate to other areas in order to satisfy their requirements.
- At £8.50 per sq ft, Aberdeen's prime industrial rents are the highest in the UK outside London and the Thames Valley. Meanwhile, strong occupier demand has narrowed the rental premium between prime and good quality secondhand space to just 15%.
- The strength of Aberdeen's market, coupled with oil and gas related covenants, has spurred significant demand from institutional investors. However, activity is being constrained by a lack of buying opportunities and restrictive lending on riskier assets.

Economic overview

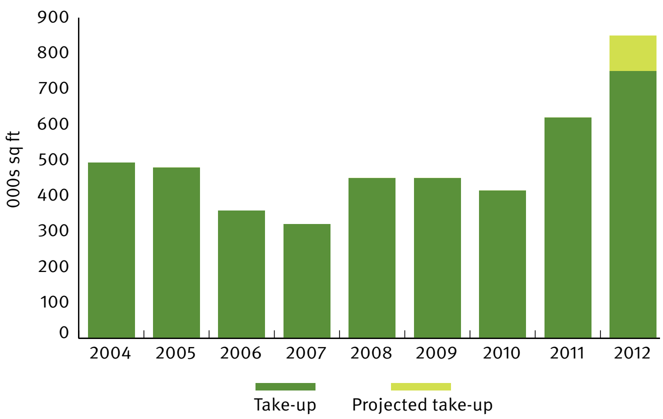
Aberdeen is widely regarded as the energy capital of Europe, with the Aberdeenshire region home to in excess of 1,000 companies operating within the North Sea energy industry. While Aberdeen's economy and property market are heavily reliant on this sector, it is also vital to the UK economy, supporting 440,000 jobs nationwide.

The well-documented success of Aberdeen's energy sector has been driven by the high and relatively stable oil price seen throughout 2011 and 2012, with the price of Brent Crude generally above $100 per barrel throughout this period. Renewed confidence has been reflected in several major investments announced by leading oil and gas companies with, for example, BP, Chevron, Conoco and Shell's decision to collectively invest almost £10bn in North Sea oil exploration.

The sector received another boost in September following the government's partial U-turn on the taxation of oil profits. The new Brown Field Allowance will shield up to £500m of oil and gas income derived from mature oil and gas fields, saving firms up to £160m. Importantly, it is widely expected to increase the viability of extraction, and could attract a further £2bn of investment to this sector.


The North Sea oil industry continues to drive Aberdeen's economy

Figure 1
Industrial take-up



Source: Knight Frank Research


In June 2012, Ashtead Technology leased Discovery Drive, Westhill at a headline rent of £8.50 per sq ft. Knight Frank acted for the landlord

Occupational market

Aberdeen's industrial market is dominated by the North Sea oil and gas industry. Distribution and trade counter operators have a limited presence in the market, with the vast majority of industrial occupiers engaged in energy-related activities. While the nature of this demand has traditionally focused on units below 20,000 sq ft, 2012 has seen a surge in demand across all size ranges.

Confidence in the oil industry has been reflected in buoyant market activity, as many industrial occupiers have sought to upgrade their accommodation or expand their operations following new contracts. Following a marked improvement in take-up in 2011, take-up in 2012 to-date stands at 750,000 sq ft and is projected to reach a 10-year high of 800,000 sq ft by year end (Figure 1). Despite the strength of activity, however, take-up is arguably being constrained by both a lack of existing supply and restrictions on debt finance which is hindering new development.

Five key transactions have accounted for 30% of take-up in 2012 to date. These include Cameron's £3.975m owner-occupier purchase of the Carron Facility at Badentoy, RST Trading Ltd's lease of an additional 52,000 sq ft at Wellheads Terrace and Expro's assignation of Halliburton's lease at the Cairn Facility in Dyce. The smaller end of the market also forms an important part of Aberdeen's demand profile, particularly so in recent months, with sub 5,000 sq ft units at terraced schemes accounting for 22% of 2012 take-up.

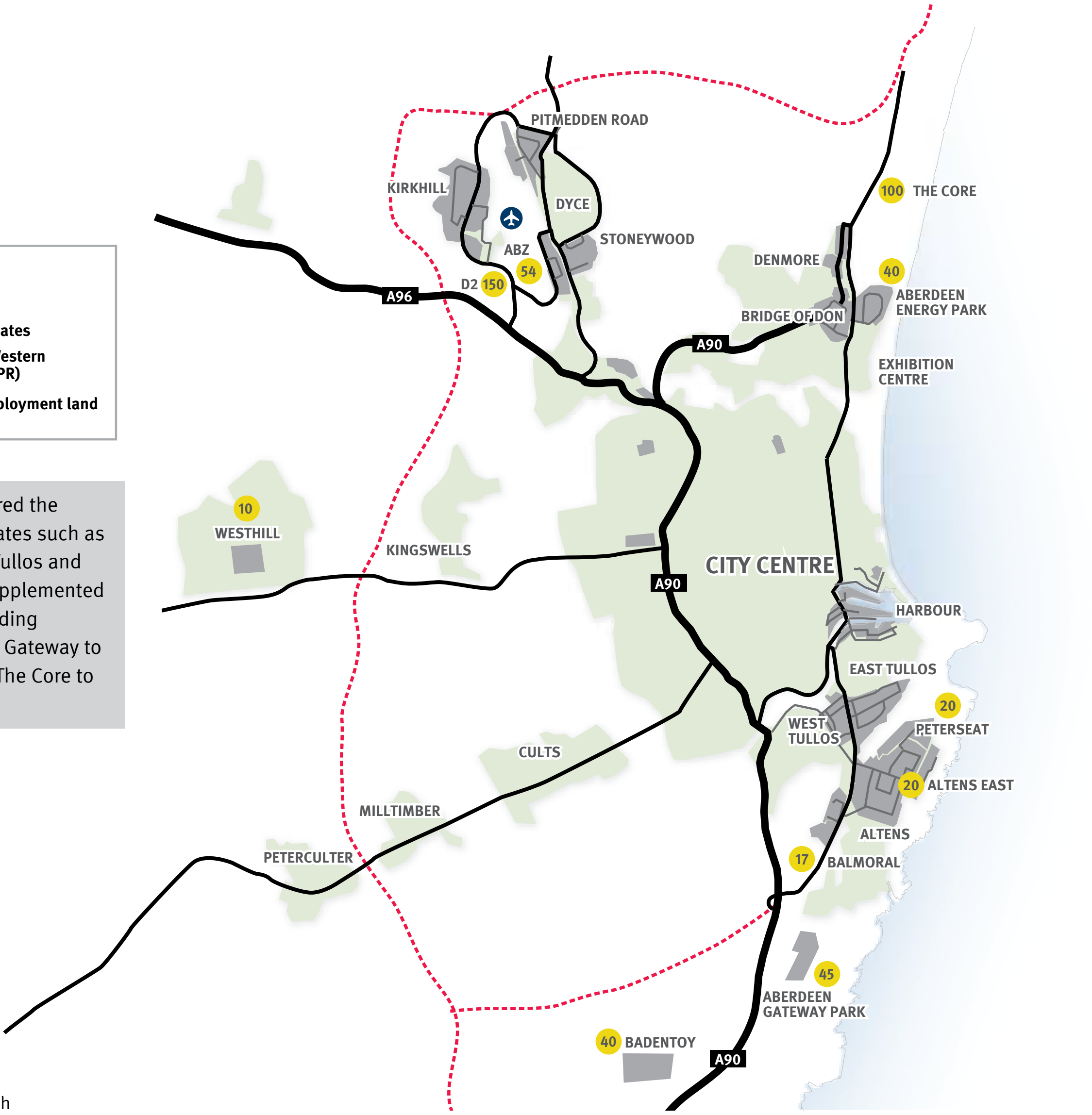
A severe shortage of supply within Aberdeen's established industrial estates has forced a host of occupiers to relocate to unfamiliar surroundings, particularly in search of units in excess of 10,000 sq ft. While a number of companies have moved from north to south, around Altens, the most notable trend has been a movement of occupiers to the west. Notable westward relocations this year include ASCO and Petrofac committing to a combined 120,000 sq ft at Kintore, Advantec and Elliott Group establishing bases within Kirkwood Commercial Park, Inverurie and HB Rentals acquiring 30,000 sq ft near Sauchen.

Aberdeen industrial and business areas

KEY

- Built up areas
- Existing industrial estates
- Proposed Aberdeen Western Peripheral Route (AWPR)
- X Acres of available employment land

As the market has matured the original established estates such as Kirkhill, Bridge of Don, Tullos and Altens are now being supplemented by modern estates including Badentoy and Aberdeen Gateway to the south, ABZ, D2 and The Core to the north and Westhill.



Source: Knight Frank Research

Table 1

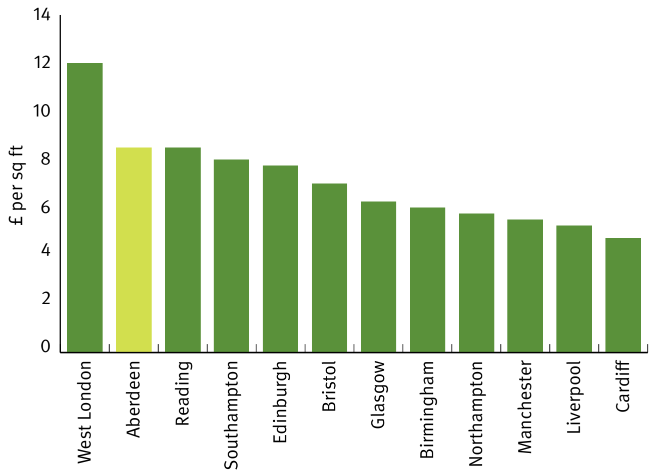
Selected occupier transactions in 2012

Address	Transaction	Occupier	Area (sq ft)	Rent per annum / Price	Date
Carron Facility, Badentoy	Freehold purchase	Cameron	54,815	£3.98m	Jun 12
Z3, Badentoy	Freehold purchase	Stauff	20,732	£2.90m	Jun 12
Wellheads Terrace, Dyce	New lease	RST Trading Ltd	52,075	£442,000 p.a.	Aug 12
Cairn Facility, Dyce	Assignation	Expro North Sea Limited	43,516	£380,000 p.a.	Sep 12
Aberdeen Gateway	Freehold purchase	Coretrax	11,700	£1.67m	Sep 12
Unit 8, Minto Commercial Park, Altens	New lease	Rotech Subsea	15,720	£211,500 p.a.	Oct 12
Unit 3, Minto Commercial Park, Altens	New lease	Pipelines 2 Data	15,161	£190,000 p.a.	Oct 12

Source: Knight Frank Research

At £8.50 per sq ft, Aberdeen's prime industrial rents are the highest of any UK market outside London and the Thames Valley area. Rents have been relatively stable at this level since 2008, and largely reflect Aberdeen's prevailing high land values of c.£450k per acre, rather than being driven by market demand. Recent transactions at new-build developments such as Carnegie's Discovery Drive, Westhill and Gilcomston Investment's two units at Raiths Industrial Estate, Dyce confirmed prime rents at £8.50 per sq ft.

Figure 2
Prime industrial rents (units under 20,000 sq ft)



Source: Knight Frank Research

While prime rents have held steady, increased demand has led to a clear narrowing in rental levels between prime and secondhand space. Headline rents for good quality secondhand buildings currently stand at c. £7.50 per sq ft, having increased by 15% since 2010. Landlords have reaped the benefits, with minimal void periods, limited incentive packages and headline rental growth. Notable deals in 2012 include Uniconn, Pipelines 2 Data and Sabre Safety, each of whom recently agreed 10-year leases.

The owner-occupier market has also been surprisingly strong. Rather than renting, some occupiers have opted to deploy their capital reserves to acquire new-build accommodation. For example, Stockland Muir completed two speculative developments at Aberdeen Gateway that subsequently sold to Special Piping Materials and Coretrax, while GSS Developments' Z3, Badentoy also sold in 2012 for a price of £2.9m. These deals established prime industrial capital values at £140 per sq ft.

Following years of constrained land supply, 2012 saw a substantial increase in the availability of development land. There is currently in excess of 500 acres of employment land being actively promoted, marketed or developed. For example, Ribnort, Balmoral and Chap have each completed servicing and infrastructure works to supplement the established business parks of Aberdeen Gateway, Aberdeen Energy Park and Peterseat Park, totalling an additional 80 acres. Elsewhere, Miller Developments and Generate Land have launched D2 Business Park and The Core which together have the potential to provide 250 acres.

Reflecting the sheer weight of occupier demand, Aberdeen is one of the few UK industrial markets to have seen speculative development in recent years. The handful of schemes which have been developed speculatively, such as Carnegie Property's Discovery Drive and Stockland Muir's Aberdeen Gateway, have proven very successful, attracting strong commercial terms and no voids.

The lack of debt finance has nevertheless continued to deter speculative development, with the majority of developers holding out for design and build packages on long-term leases. However, following the success of the above-mentioned schemes, other developers are now pressing ahead with speculative development. For example, Buccleuch Property has launched an initial phase of three new units in Aberdeen Energy Park while Ribnort and Dandara have committed to developing sites in Dyce and Westhill respectively.

Stockland Muir's speculative development at Aberdeen Gateway was purchased by Special Piping Materials in January 2012

KNIGHT FRANK VIEW

- Although occupier demand is strong enough to warrant concerted speculative development, ongoing restrictions on debt finance will continue to impact on the level of activity in the short term.
- As a consequence, we anticipate occupiers with larger requirements to turn increasingly towards design and build solutions over the next 12 to 18 months. However, given that in many cases occupiers continue to prefer the greater flexibility associated with leasing existing accommodation, landlords could benefit from undertaking refurbishment.
- We expect 2013 to see exceptional deals with rental rates reaching £9.00 per sq ft, albeit confined to the most sought after locations. However, while the sharp increase in development land is welcome, the competition it brings will ensure that the majority of prime deals will remain at £8.50 per sq ft.

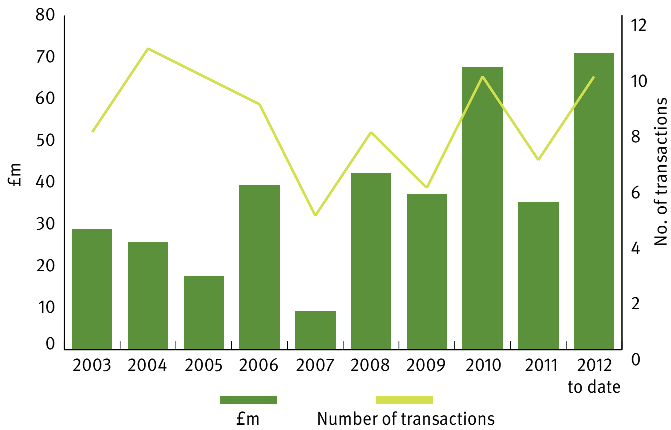
Investment market

While the challenging economic backdrop continues to impact the majority of the UK's markets outside London, Aberdeen's buoyant occupier market and restricted level of supply make a compelling case for investment in the city's office and industrial markets. Funds and institutions are increasingly attracted to the Aberdeen market, backed by strong oil and gas covenants and a perception that the city currently represents good value in comparison with the UK's other regional cities.

Industrial investment in Aberdeen has reached £71m in 2012 in the year to date, and has already eclipsed 2010's previous record of £67m. However, the actual number of deals has been broadly comparable with previous years with two transactions in excess of £10m boosting overall turnover.

The largest deal in 2012 was CBRE Global Investors' £19.9m purchase of Wellheads Industrial Centre. The 218,725 sq ft multi-let industrial estate had a Weighted Average Unexpired Lease Term (WAULT) of 5.5 years. The price paid reflected a net initial yield of 7.61% and a reversionary yield of 8.78%.

Figure 3
Industrial investment



Source: Knight Frank Research/Property Data


Knight Frank was recently instructed by Carnegie Property Company to sell Claymore Drive, Bridge of Don, totalling 30,201 sq ft

Prime industrial yields currently stand at c.7.00% in Aberdeen although, as with elsewhere in the UK regions, buying opportunities are extremely rare in this segment of the market. Indeed, the last investment sale at this level took place in 2011, where Palmer Capital purchased the Smith International Facility in Badentoy, a modern facility let to a strong covenant for 15 years. If prime opportunities do become available, Aberdeen's strong occupational story will inevitably attract investors with mandates to invest in the UK regions.

While the majority of funds are typically looking to acquire larger lot-sizes in excess of £10m, buying opportunities for this type of stock have been in short supply. Consequently, the market has followed a similar trend to the previous two years, with activity focused on lot-sizes ranging from £3m to £7m with equity-backed funds and institutional investors driving transactional activity.

Activity for smaller lot-sizes ranging from £1m to £3m has typically been the preserve of private individuals, family trusts or property companies. Unsurprisingly, however, this segment of the market has been very subdued in recent years, due to a combination of restricted debt finance and limited motivation to sell among owners. Indeed, of late, the majority of purchases in this sector have been by owner-occupiers, with one exception being FWM Limited's £2.31m purchase of Discovery Drive, reflecting a net initial yield of 7.55%.

Table 2
Selected investment transactions in 2012

Address	Area (sq ft)	Price	Purchaser	Vendor	NIY (%)	Date
Minto Avenue, Altens	86,267	£11.5m	Ropemaker Properties	Stainton Group	8.50	Apr 12
Noskab House, Badentoy	28,825	£4.4m	Cedarwood Asset Management	Stainton Group	9.19	Jul 12
Wellheads Industrial Centre, Dyce	218,725	£19.9m	CBRE Global Investors	F&C Reit	7.61	Jul 12
Discovery Drive, Westhill	13,682	£2.31m	FWM Ltd	Carnegie Property Company	7.55	Oct 12

Source: Knight Frank Research

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