

REGIONAL OFFICES

OCCUPIER & INVESTMENT MARKET SUMMARY Q4 2015

Economy

The first estimate of Q4 UK GDP growth was 0.5% quarter-on-quarter, a small improvement compared with growth of 0.4% in Quarter 3. For 2015 as a whole, UK GDP growth was 2.2%, down from 2.9% in 2014.

For 2016, the consensus forecast is for a growth rate similar to 2015. This represents a healthy level in the current climate, and is better than that expected for all other G7 nations, with the exception of the US. Nonetheless, risks to growth have increased from 2015, not least from the continued slowdown in China and volatility in the oil markets. The EU membership referendum, now confirmed for June 23rd 2016, is likely to result in a degree of inertia from businesses in the lead up. This may curtail UK growth in the first half of the year, with the outcome of the vote shaping overall growth and market trajectory over the remainder of 2016.

Occupier markets

Take-up across the ten regional cities monitored in ROMP amounted to 3.1m sq ft in H2 2015, 11% less than in the first six months of 2015. This meant that the combined take-up total for year increased to 6.5m sq ft, marginally less

(5.9%) than 2014 but 17% above the 10-year average.

During the H2 period, four of the ten regional markets (Cardiff, Glasgow, Leeds and Newcastle) recorded an increase in take-up. The largest increase was recorded in Cardiff where take-up was more than double the H1 total at 399,500 sq ft. The sharp rise meant that total take-up during the year reached 619,150 sq ft, a record for the city.

Manchester, however, accounted for the largest proportion of take-up in 2015 with 1.3m sq ft transacted, 20% of total regional take-up. Although this was slightly less than in 2014, the 2015 total represented the second successive year of take-up exceeding 1.3m sq ft.

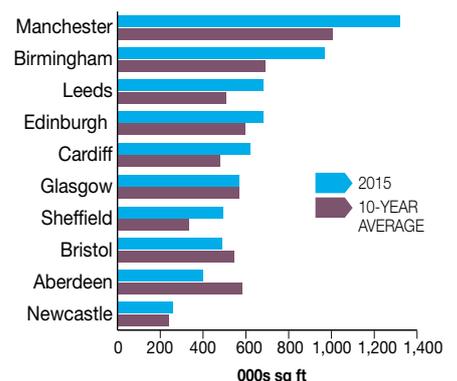
Accounting for 15% of regional take-up in 2015, Birmingham recorded a 36% year-on-year rise with 970,000 sq ft transacted, a total on par with 2008. Supporting the rise was the pre-let of 212,000 sq ft to HSBC – the largest regional leasing deal of 2015.

In total, five of the ten markets registered a year-on-year increase in take-up during 2015. Notably, eight of the ten were above their respective 10-year take-up average. Only Bristol and Aberdeen saw take-up levels fall below this benchmark during the year.

Overall Grade A availability increased by 7% in H2, reaching 2.4m sq ft at year-end. Despite the rise, total Grade A availability was 17% below the 5-year average of 2.9m sq ft. The lowest Grade A availability was in Cardiff where levels fell below 100,000 sq ft for the first time. The largest annual decrease, however, was in Bristol where levels fell by 46% in 2015.

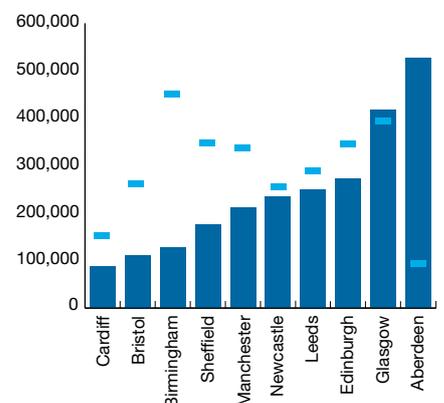
Given underlying demand and supply dynamics, an increase in prime headline rent was registered in six of the ten regional markets during H2. The largest increase was in Sheffield where rents increased by 15% to £23 per sq ft. Notably, forecasts indicate that by the end of 2016, rents will have grown further in seven of the ten regional cities.

FIGURE 1
2015 take-up vs 10-year average



Source: Knight Frank Research

FIGURE 2
Years of Grade A supply



Source: Knight Frank Research

FIGURE 3
Prime rents and forecast (per sq ft)

| | 2015 | End 2016 F |
|------------|--------|------------|
| Aberdeen | £32.00 | £30.00 |
| Manchester | £34.00 | £34.00 |
| Birmingham | £30.00 | £33.50 |
| Glasgow | £29.50 | £30.00 |
| Bristol | £28.50 | £29.50 |
| Edinburgh | £31.00 | £32.00 |
| Leeds | £26.50 | £27.50 |
| Sheffield | £23.00 | £23.00 |
| Cardiff | £22.00 | £25.00 |
| Newcastle | £22.00 | £23.00 |

Source: Knight Frank Research

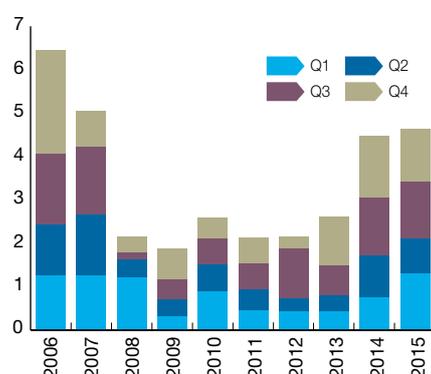


One St Peters Square, Manchester

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FIGURE 4
Regional office investment volumes (£bn)



Source: Property Data

FIGURE 5 Prime yields (%)
Reflects 10 year income

| | 2014 | 2015 | Yield sentiment |
|------------|------|------|-----------------|
| Aberdeen | 5.75 | 6.25 | ▲ |
| Birmingham | 5.25 | 5.00 | ◆ |
| Bristol | 5.50 | 5.25 | ◆ |
| Cardiff | 5.90 | 5.75 | ◆ |
| Edinburgh | 5.75 | 5.25 | ◆ |
| Glasgow | 6.00 | 5.25 | ◆ |
| Leeds | 5.75 | 5.25 | ◆ |
| Manchester | 5.25 | 5.00 | ◆ |
| Newcastle | 6.00 | 6.00 | ◆ |
| Sheffield | 6.25 | 6.50 | ◆ |

Source: Knight Frank Research



Investment activity

Investment volumes increased by 21% during H2 2015 with £2.5bn of sales recorded. This meant that total turnover in 2015 reached £4.6bn, an increase of 6% when compared to 2014. Notably, the 2015 total represents the highest level of investment into regional offices since 2007.

Supported by the acquisition of Colmore Plaza by Ashby Capital, Birmingham accounted for the largest proportion of turnover in H2. This was one of four acquisitions over £50m in the city during the second half of the year. At year-end, total investment in Birmingham offices had reached £796m, an increase of 43% when compared to 2014 and the highest level of turnover of any major regional city.

Following a 28% increase in investment in H2, total office investment in Manchester reached £642m for the year. Although this is less than recorded in 2014, the 2015 total is 40% above the 10-year average. Supporting the H2 rise was the purchase of Two St Peters Square for £100m by Deutsche Asset & Wealth Management. This represented the largest investment deal in Manchester during 2015. Construction of the building will complete in 2017 with Ernst and Young taking 40,000 sq ft on a 15 year lease.

In total, five of the ten major regional cities recorded an increase in investment turnover during the year, with six above their respective 10-year average. The largest year-on-year increase (three-fold) was in Cardiff underpinned by the L&G investment in Central Square. Similarly, the £72m acquisition of 120 Bothwell Street by M&G supported an increase of 96% in Glasgow. Bristol and Newcastle were the other cities where an annual increase was recorded.

With investor appetite increasing for regional opportunities in 2015, seven of the ten major regional cities registered yield compression. The largest annual change was in Leeds, Edinburgh and Glasgow with yields moving in by 50bps. Birmingham, Bristol, Cardiff and Manchester also saw a rise in capital values in 2015. However, at the close of the year, yields were still above the peak of the market in all cities. This leaves the possibility of further yield compression in some centres during 2016.

Major regional office investment deals in 2015

| Date | Street | Purchaser / Vendor | Price £m | Yield % |
|--------|--------------------------------------|--|----------|---------|
| Aug-15 | Colmore Plaza, Birmingham | Ashby Capital LLP/ Carlyle EREP | 140.00 | 6.00 |
| Feb-15 | Brindleyplace, 7, 8 & 10, Birmingham | VGV/Tritax Assets Ltd | 131.00 | 5.75 |
| Aug-15 | 2 St Peter's Square, Manchester | Deutsche Asset and Wealth/ Mosley Street Ventures | 100.00 | NA |
| Dec-15 | Lothian Road, 30, Edinburgh | Overseas Investor/ Standard Life | 93.75 | 5.08 |
| Jan-15 | Hardman Square, 3, Manchester | M&G/CS Euroreal | 91.70 | 5.79 |
| Jul-15 | 1 Colmore Square, Birmingham | Legal & General UK PF/IBRC | 87.30 | 4.04 |

Source: Knight Frank Research

Please refer to our bi-annual reports for more detailed accounts of the city markets <http://www.knightfrank.co.uk/research/ROMP/>



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