LOGISTICS & INDUSTRIAL

OCCUPIER & INVESTMENT MARKET COMMENTARY **H1 2017**

Economic overview

The UK economy grew by less than expected in the first quarter of 2017. The latest figures released by the ONS show that UK GDP growth slowed to 0.2% in Q1 2017, down from 0.7% in Q4 2016. This is the weakest growth since Q1 2016, when output growth was also 0.2%.

The slowdown in the economy was largely driven by a drop-off in the dominant service sector, which accounts for around four-fifths of output, and was the slowest on record since the first quarter of 2015. Distribution and retail output also contributed to the slowdown in growth while manufacturing output rose by 0.5% (Figure 1).

Household consumption growth is expected to remain weak in the second half of 2017, and there is likely to be additional downward pressure on growth from political and Brexit uncertainties that could lead to a further depreciation in sterling.

Occupier market

In the first half of 2017 a total of 16.5m sq ft of logistic and industrial units above 50,000 sq ft was acquired for occupation. This is 24% below the level of take-up in H2 2016. However, the figures in H2 2016 were skewed by the 2.2m sq ft letting to Amazon at Tilbury. If this one transaction is excluded, take-up was just 15% down on the previous six months. Also when compared with the previous year, take-up was 2% up on H1 2016. Given the snap General Election and on going uncertainty surrounding Brexit, these figures are particularly encouraging (Figure 2).

Two underlying trends driving the market are the shift to online retailing and the move to urban logistics. Internet sales are continuing to rise and now account for around 15% of all retail sales in the country (Figure 3).

At regional level, the Midlands continues to dominate the market, with 32% of total take-up coming from this area, followed by the North West and London & the South East, which together accounted for a further 30% of total take-up.

Once again, pre-lets represented a significant proportion of deals in the first half of the year, with 35% of UK wide take-up of units above 50,000 sq ft in this category.

Availability continues to decline and land available for industrial development remains in short supply. There has been a 34% reduction in industrial land availability over the past 14 years in London with 268 acres per year being taken out mainly for residential use. In the big-shed market, new-build supply of units above 100,000 sq ft stood at just over 8m sq ft at the end of June 2017, compared with a peak of 28m sq ft in Q1 2008 (Figure 3).

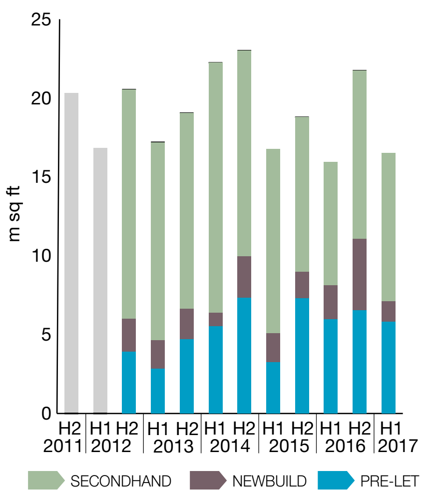
The outlook for the second half of 2017 is mixed. Given the economic slowdown affordability issues will constrain rental growth and a slowing of demand is masked by the lack of stock.

For more detailed commentary on the occupier markets, please refer to our regional LOGIC reports.

FIGURE 2

UK Logistics take-up

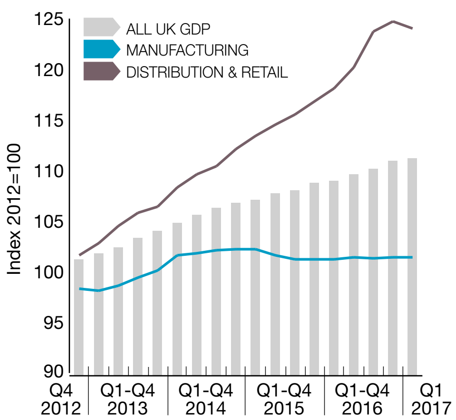
(50,000 sq ft plus)



Source: Knight Frank Research

FIGURE 1

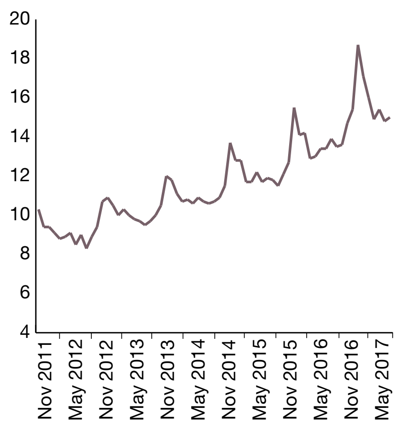
UK Economic output indices



Source: ONS

FIGURE 3

Internet sales as a percentage of total retail sales (%)

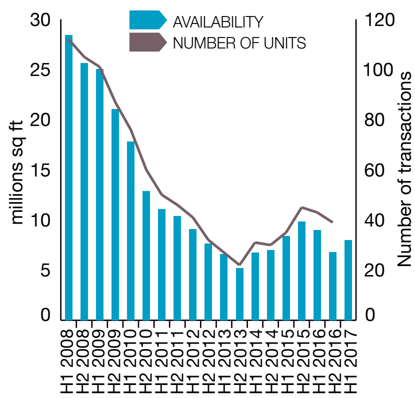


Source: ONS

FIGURE 4

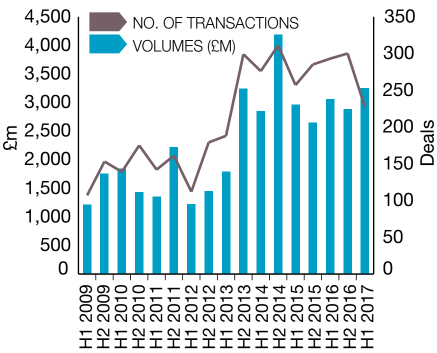
New sheds available

(100,000 sq ft plus)



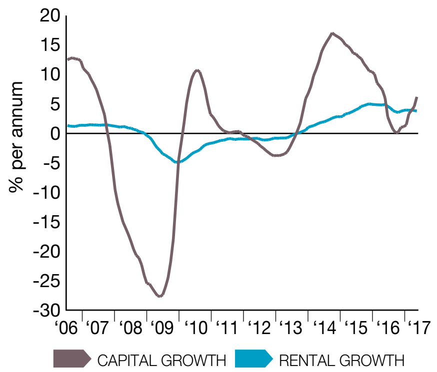
Source: Knight Frank Research

FIGURE 5
Industrial investment transactions



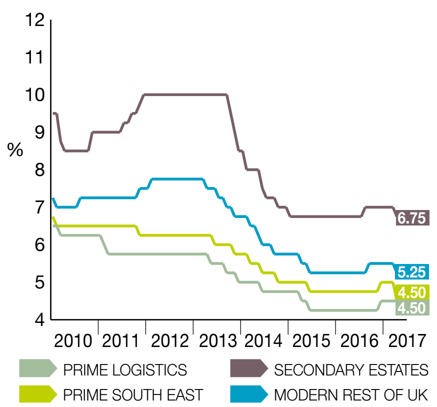
Source: Property Data / Knight Frank

FIGURE 6
Industrial sector performance



Source: IPD/Knight Frank

FIGURE 7
Single-let and multi-let warehouse yields



Source: Knight Frank

Investment market

Investor demand for logistics and industrial assets remains strong, buoyed by the sector's favourable underlying demand and supply conditions, and income generating attributes. The latest figures from Property Data show that £3.2bn worth of industrial property assets changed hands during H1 2017. This represents an increases of 13% on the previous half year's volume of £2.9bn (Figure 5).

There have been more large deals since the start of the year, with 227 industrial transactions recorded in H1 2017, compared with 300 in H2 2016. Key investment deals during the first half of 2017 include DVS Property's purchase of Kingston Park for £86.4m, reflecting a net initial yield of 5.80%, Keller Group's purchase of Accolade Park for £62.0m (NIY 6.50%) and Goldman Sach's acquisition of Boreham Interchange for £36.7m (NIY 4.97%).

Overseas investors and property companies have been the major players so far this year accounting for 34% and 31%, respectively, of total investment activity over H1 2017. UK institutions accounted for a further 25%.

The IPD Monthly Index shows that industrial capital value growth remains on an upward trajectory with industrial values now rising at an annual rate of 6.2%. Industrial rental value growth continues to exceed inflation with an annual rental value growth of 3.8% in June 2017 (Figure 6). In terms of the wider market, industrials continue to outperform the other two core sectors, with London and the South East leading the way.

Positive market sentiment for the industrial sector has contributed to steady yield compression. The IPD All Industrial Equivalent Yield stood at 6.16% in June, 29 bps down since the start of the year, and the lowest on record since October 2007. While Yields between prime and secondary assets are still narrow by historic standards, with single-let distribution yields at 4.50%, and prime multi-let and secondary estates at 5.25% and 6.75%, respectively, demonstrating the ongoing demand for this sector (Figure 7).

Selected warehouse / logistics transactions in H1 2017

Property	Vendor/Purchaser	Price	NIY	Date
Kingston Park, Flaxley Road,Peterborough	DVS Property Ltd/Gulf Co-operation Council	£86.4m	5.80%	Jun-17
Accolade Park, Avonmouth	Keller Group Plc/CSUK1 Holdings Ltd	£62.0m	6.50%	May-17
Boreham Interchange, Chelmsford	Goldman Sachs/Tesco Pension Fund	£36.7m	4.97%	Mar-17
Logistics City, West Thurrock	Kier Property/CBRE UK Property PAIF	£33.1m	4.60%	May-17
Signia Park, Didcot	Clowes Development UK/ Tritax Big Box REIT Plc	£29.2m	5.82%	Feb-17
Woodside Industrial Estate	Colony Capital/Knight Frank IM LLP	£24.2m	5.96%	Jan-17

Source: Knight Frank Research

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