RESEARCH

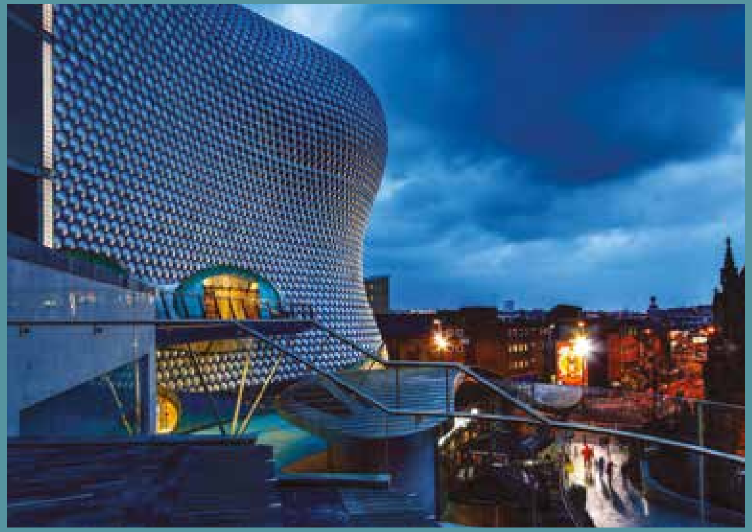
UK REGIONAL CITIES

OFFICE MARKET REVIEW

2017

6-7
Aberdeen

CONTENTS



8-9
Birmingham

20-21
Leeds

The Knight Frank Regional Cities Office Market Review analyses not only the performance of the ten major UK regional cities in 2016, but also gives opinion and insight into future trends.

FOREWORD

ALASTAIR GRAHAM-CAMPBELL
PARTNER, REGIONAL HEAD

A short reflection of our regional cities reveals that a renaissance is firmly underway. Each of our regional cities is evolving at pace through both public and private investment. Amenity and infrastructure now underpin each development plan, recognising the shift in employer focus toward offering a lifestyle to attract and retain talent.

Occupier activity over each of the past three years has been above the long-term trend. This statistic is testament to progress, illustrating not only the growth ambitions of local companies, but also the attraction to occupiers from further afield. Manchester is a good example of this, with inward investment accounting for close to 15% of take-up in 2016. This scenario is increasingly being reflected across the regional cities.

Moving forward, we must recognise that a number of UK wide factors threaten to undermine growth and confidence. The disruptive influence of Brexit is foremost, although reassuringly, the forecasts of economic disaster post the EU vote have for now, been buried. A smooth negotiation process will be definitive, but we can be sure that the political arena will again dominate in 2017.

> "Amenity and infrastructure now underpin each development plan, recognising the shift in employer focus toward offering a lifestyle to attract and retain talent."

Importantly, there is now the political will to empower the regional cities, something that arguably was missing in the past. The built environment is a fundamental component of this change agenda, one that is creating the right conditions for innovation and growth. The transformational journey of our regional city centres has momentum. Success will leave a legacy of economic, social and cultural gain to the benefit of future generations.

MARKET DRIVERS

01

A RESILIENT UK ECONOMY

The UK economy has surprised on the upside since the June 2016 referendum. Defying predictions of a recession, GDP growth was better than expected in Q3 and Q4 2016, 0.6% in each quarter. Unemployment has remained low, 4.8% at year-end, just below the rate before the referendum. Survey evidence suggests growth has a broad base across the UK regions.

In 2017, the UK economy will face challenges largely related to Brexit and rising inflation. Both of these challenges could potentially prove difficult or even beneficial for the economy. The triggering of Article 50 negotiations will cause some increase in concerns over the future trading environment for UK exporters. However, as the talks progress, more clarity could emerge on the future arrangements for trade, which will allow businesses to plan with more confidence.

A rise in inflation could dampen consumer spending if pay rises do not keep pace. However, with a tight labour market, employers may be eager to retain staff, and if pay increases do match, then current spending levels will continue.

Knight Frank forecasts indicate that the UK economy will grow by 1.5% in 2017, lower than 2016 but high enough to maintain a steady level of demand for commercial property.

02

CHANGING OCCUPIER REQUIREMENTS

Despite an uncertain backdrop, occupational demand across the UK in 2017 will be robust. On-going technological disruption is forcing businesses to rethink and restructure. The characteristics of market demand will however, change.

There will be a greater number of smaller deals driven by specialist project teams locating away from mainstream businesses, as well as from a burgeoning SME supplier base serving big business. Flexibility, either in lease terms or via the increased utilisation of co-working will feature more. We will continue to see demand gravitating towards amenity-rich buildings and locations that help occupiers attract and retain tech and creative talent.

On this basis, demand will concentrate on major cities rather than smaller towns within metropolitan areas.

03

CONTINUING INTEREST FROM OVERSEAS INVESTORS

The UK investment market has started 2017 in a positive mood having shrugged of the turmoil of early last year. Buoyed by positive economic data and active occupiers, investors are actively searching for regional opportunities. Investment transactions increased in the final quarter of 2016 following a pause in activity around the referendum and this momentum is expected to continue through the year. We expect UK institutions to be a key buyer group alongside overseas buyers who will be looking for regional UK opportunities in their search for yield, further encouraged by the recent weakness of sterling.

04

A STRONG FOCUS FROM GOVERNMENT

The government is set to play a major role in the fortunes of the regional cities both from a political and new business sense. Even before the Brexit vote, a core part of Government economic policy was to rebalance the national economy. Infrastructure investment underpins current strategy alongside the devolution of power to city regions, a process that will bring newly elected mayors to some cities and importantly, allow more autonomy in budgetary spending.

Consolidation of the government office estate is also creating opportunities in the regional office markets. The strategy of creating collaborative hubs has led to large-scale requirements for new office space across many UK centres. At the time of writing, the Government Property Unit (GPU) is actively seeking two million sq ft across seven of the ten major markets featured in this report. To contextualise this equates to roughly one third of the combined annual office take-up total.

ABERDEEN

OCCUPIER MARKET

Although the global oil price improved in 2016, occupier take-up was 51% below the 10-year average. With 'grey space' adding to new development, availability increased to twice the long-term average.

In 2016, Aberdeen recorded the lowest level of occupier take-up since 2009 with 279,000 sq ft transacted. This is 51% below the 10-year average. Interestingly, actual deal numbers were up in 2016 with 65 deals completed, compared to 55 deals in 2015.

The largest letting of 2016 was the 36,250 sq ft lease taken by charity, Somebody Cares at Trafalgar House One. This was one of two deals over 30,000 sq ft to complete during the year. The other was the new 31,300 sq ft lease taken by Marathon Oil at Kennedy Wilson's Marathon House, Hill of Rubislaw.

There were also four deals in the 10,000 – 30,000 sq ft bracket. PWC became the first occupier to sign at The Capitol taking 10,600 sq ft on a 15-year lease. The professional services firm moved 120 staff from its existing office at Albyn Place to the newly revamped development on Union Street. Additionally, AAM/Manse leased 10,500 sq ft at the AB1 refurbishment to The Crown Office & Procurator Fiscal Service. The other two deals were to serviced office providers. Citibase took a 22,000 sq ft sub-let of Anderson, Anderson, Brown's West End office at 9 Queen's Road, whilst Orega pre-let 26,000 sq ft in the Silver Fin building.

Energy and Utilities occupiers accounted for the highest proportion of take-up at 25%, down from 60% in 2015. Supported by the Trafalgar House deal, charities represented the next highest at 20%.

Grade A availability increased to 636,300 sq ft in 2016, a total twice that of the long-term average. This is the highest level on record for the city. The development pipeline in Aberdeen is significant with 402,000 sq ft due to complete over the next 12 months. Of this, 302,000 sq ft is speculative.

In 2016, prime headline rents held firm at £32.00 per sq ft, albeit occupier incentives moved out. We anticipate prime rents will fall to £30.00 by year-end 2017 driven by a continued market imbalance.

AB1, HUNTLY STREET, ABERDEEN

INVESTMENT MARKET

Investor sentiment remained subdued in 2016, meaning investment transactions were few in number. Yields moved out although evidence of prime pricing during the year was limited.

Total office investment volumes reached £19m in 2016, 76% less than recorded in 2015. This represents the lowest level of investment in the city since 2009. Only three investment deals completed during the year. This compares to four in 2015.

The acquisition of the Anderson, Anderson, Brown HQ at Prime Four Business Park for £17.2m was the largest transaction in 2016. This was the only sale over the £10m threshold. Subsequent to the sale, developer Drum Property Group submitted plans for a 320,000 sq ft retail development, which will sit adjacent to the existing office buildings.

The other sales were low value and include the £1.6m sale of 12/13 Albyn Terrace to a private buyer and the acquisition of 492 Union Street to Harlaw Investments Ltd for £187,000.

As such, private money represented 99% of investment volumes in 2016. This compares to just 28% in 2015.

Although investor appetite was weak in 2016, examples of new investment stock coming to market were few. In particular, there was a notable absence of secondary investment stock. Vendors remain cautious on account of the subdued occupational demand. With the oil price and exchange rate more favourable in recent months, this may stimulate more buyer and seller activity moving forward.

Prime office yields moved out by 25 bps to 6.50% in 2016 although few opportunities transacted during the year to test this level. Notably, yields are 100 basis points above the market peak of 5.50% recorded in 2007. This gap illustrates the current thoughts regarding risk in the market.

FIGURE 1
Aberdeen office take-up (sq ft)

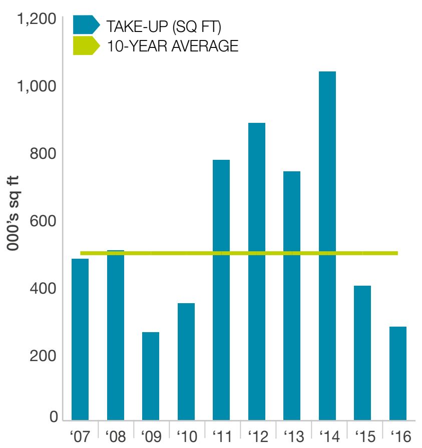
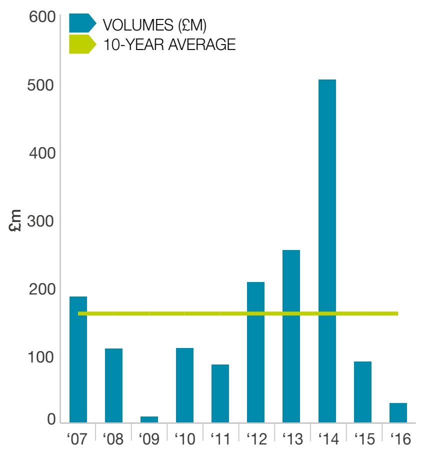


FIGURE 2
Aberdeen investment volumes (£m)



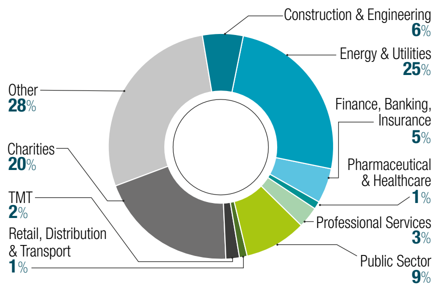
Source for all charts: Knight Frank Research, Property Data

OCCUPIER 2016

TAKE UP
0.3m Sq ft

GRADE A SUPPLY
0.6m Sq ft

TAKE UP BY SECTOR

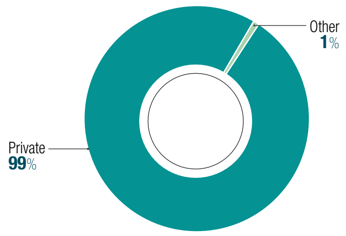


INVESTMENT 2016

VOLUMES
£19m

PRIME YIELD
6.50%

VOLUMES BY PURCHASER



KNIGHT FRANK VIEW

The consensus in the market is that the worst of the oil & gas downturn is now behind us. Most companies from the sector have been through a rationalisation of operations. Optimism is being renewed although, there will be a considerable time lag before this translates into a strong occupier market. As such, availability will remain at a high level in 2017.

Similarly, we anticipate that the property investment market will reach the bottom of its current cycle in the second half of this year or first half 2018. A steady increase in activity at all levels will follow but greatest activity could be in secondary "value add" investments with opportunistic buyers monitoring the market closely.

Given the favourable exchange rate, interest from overseas investors will increase, with Aberdeen representing value compared with other regional cities. As businesses weather the last of the storm and prepare for growth, we may see a return to sale and leaseback activity.

BIRMINGHAM

OCCUPIER MARKET

Although uncertainty stemming from the EU referendum slowed momentum in H2, take-up in 2016 was consistent with the long-term average. Availability remained at a historic low, but will rise in 2017 with development completions expected to be the highest since 2009.

Overall take-up fell 29% during 2016 reaching 692,700 sq ft at year-end. Despite the year-on-year decrease, the 2016 total is on par with the 10-year annual average for the city. Interestingly, deal number was up in 2016 with 139 transactions completed. This compares to 132 in 2015.

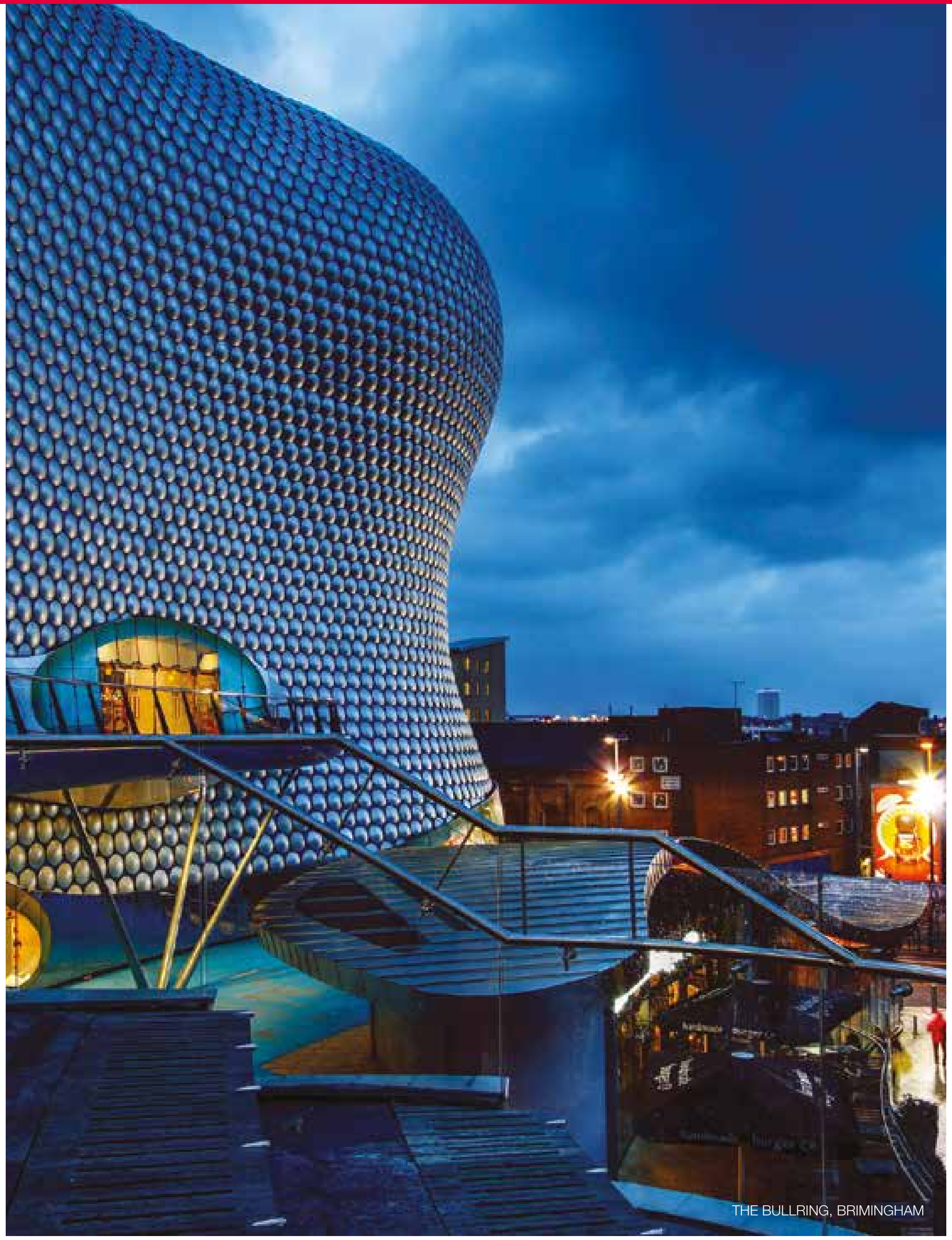
In 2016, large-scale transactions were again a feature of the market with two deals above 50,000 sq ft completing. The largest transaction of the year was the pre-let of 90,000 sq ft to PWC at One Chamberlain Square. The building is part of the much larger Paradise development owned by Hermes Investment Management, Canada Pension Plan Investment Board (CPPIB) and Birmingham City Council.

Following this, Hermes also secured the signature of Network Rail for 83,500 sq ft at Baskerville House. The move for Network Rail will support plans to consolidate existing tenancies held at the Mailbox and Smallbrook Queensway.

Occupiers from the professional services accounted for the highest proportion of take-up at 43%, supported by Pinsent Mason leasing 40,500 sq ft at 55 Colmore Row and DAC Beachcroft taking 40,000 sq ft at Tricorn House. Supported by the Network Rail letting, the public sector accounted for 16% of total take-up in 2016.

New Grade A availability in the city core remained at a historic low level in 2016 with just 127,000 sq ft on the market at year-end. This total is 60% below the long-term average. The development pipeline is however, significant with 0.7m sq ft due to complete by year-end 2018. Of this 550,000 sq ft is speculative.

Prime headline rents increased by 8% in 2016 to £32.50 per sq ft. We anticipate a further uplift to £33.50 per sq ft by year-end 2017.



THE BULLRING, BRIMINGHAM

INVESTMENT MARKET

Following the record level of investment in 2015, turnover dipped in 2016 although remained on par with the long-term average. Consistent with other UK markets, prime yields softened for the first time since 2012.

Total investment volumes fell by 50% in 2016 to reach £395m by year-end. Despite the fall, the 2016 total remained on par with the 10-year average for the city. Critically, only eighteen investment deals were completed, the lowest total since 2013.

Nonetheless, the £200m forward funding of Three Snowhill agreed between M&G Real Estate and developer Ballymore was the largest investment transaction of any major regional city during 2016. The 420,000 sq ft office development is in an enterprise zone and forms part of the Snowhill Masterplan. On completion in 2019, it will comprise of 385,000 sq ft of office space and 35,000 sq ft of retail and leisure. This was one of two investment deals over £50m to complete during the year.

The other saw the Canadian Pension Plan Investment Board (CPPIB) buy a 50% share in the first phase of the Paradise development for £75m. Owned by Hermes Investment Management and the city council, the Paradise scheme totals 1.8m sq ft. The first phase consists of 350,000 sq ft of office space across two buildings, One & Two Chamberlain Square.

Supported by the M&G deal, UK investors accounted for 77% of turnover during the year up from 53% in 2015. Other domestic deals include the acquisition of One Victoria Square by DTZ Investors for £24.1m and the sale of 55 Temple Row to IM Properties for £21.25m. Notably, the Temple Row deal reflected a net initial yield of 5.1%. Birmingham also continued to see strong interest from overseas buyers in 2016. Foreign investment represented 21% of volumes.

Prime office yields moved out by 25bps to 5.25% in 2016, reflecting the greater level of uncertainty post the EU referendum in June. At this level, prime yields are 75 bps above the market peak of 4.50% recorded in 2007.

FIGURE 1

Birmingham office take-up (sq ft)

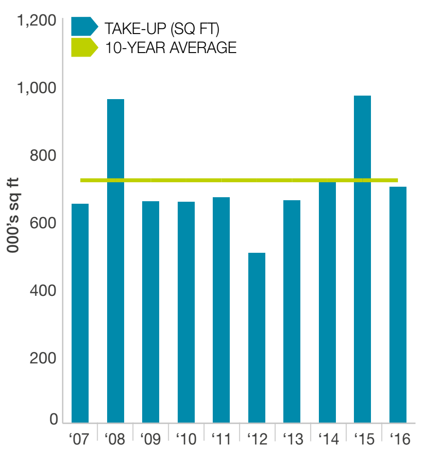
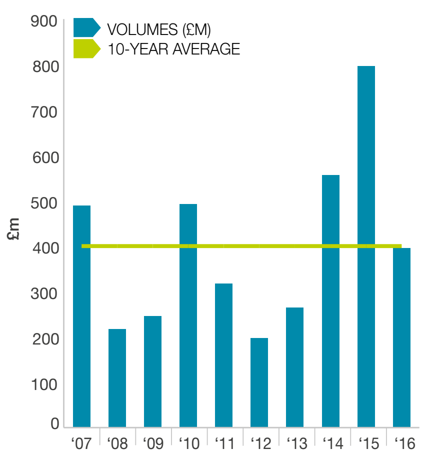


FIGURE 2

Birmingham investment volumes (£m)

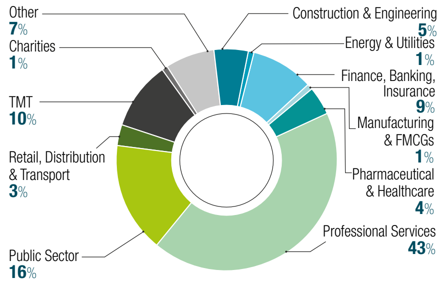


Source for all charts: Knight Frank Research, Property Data

OCCUPIER 2016

TAKE UP	GRADE A SUPPLY
0.7m Sq ft	0.1m Sq ft

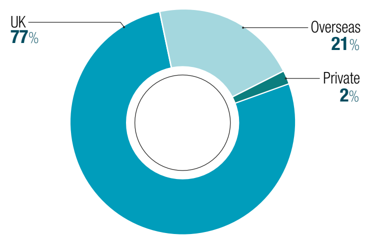
TAKE UP BY SECTOR



INVESTMENT 2016

VOLUMES	PRIME YIELD
£395m	5.25%

VOLUMES BY PURCHASER



KNIGHT FRANK VIEW

Birmingham will continue on the path of transformational regeneration in 2017, attracting further inward investment. Most significantly, we anticipate the Government Property Unit (GPU) to confirm the location of their 240,000 sq ft office pre-let, widely expected to be at Miller Developments' Arena Central scheme. The GPU space will be occupied by HMRC who are consolidating from various buildings within the Trillium estate. Many of these Trillium occupied buildings are older offices, which we expect to be redeveloped into residential apartments, hotels and student accommodation.

The High Speed 2 rail link (HS2) is now expected to receive Royal Ascent in February 2017, following which we expect more occupier demand from the Engineering sector, particularly within 1km of the new HS2 Headquarters at 2 Snowhill.

We expect prime yields to hold firm during 2017 due to the continued weight of overseas and domestic capital. There is an increasing trend towards more flexible leases on secondary buildings and secondary yields could soften as a consequence.

BRISTOL

OCCUPIER MARKET

Despite a quiet summer following the EU vote, office take-up increased significantly in 2016. This, combined with limited availability, has meant upward pressure on rents.

With the highest level of quarterly take-up for two years recorded in Q4, total office take-up in 2016 reached 782,900 sq ft. This total represents a year-on-year increase of 60% and notably, is 36% above the 10-year average. Indeed, take-up of standing stock reached its highest level in over 25 years.

The increase in take-up was supported by the 107,000 sq ft lease taken by HMRC at 3 Glass Wharf. The government department signed on a 25-year term. Salmon Harvester Properties are developing the scheme with HMRC expected to occupy the property in 2019. This was one of three deals over 50,000 sq ft to complete in 2016.

Preceding the HMRC deal was the 81,200 sq ft letting to EDF Energy at Bridgewater House. Driven by government approval for a new nuclear power station in nearby Bridgwater, the energy firm took occupation in Q1. Following this deal, Palmer Capital and Cubex sold Bridgewater House to a private foreign investor.

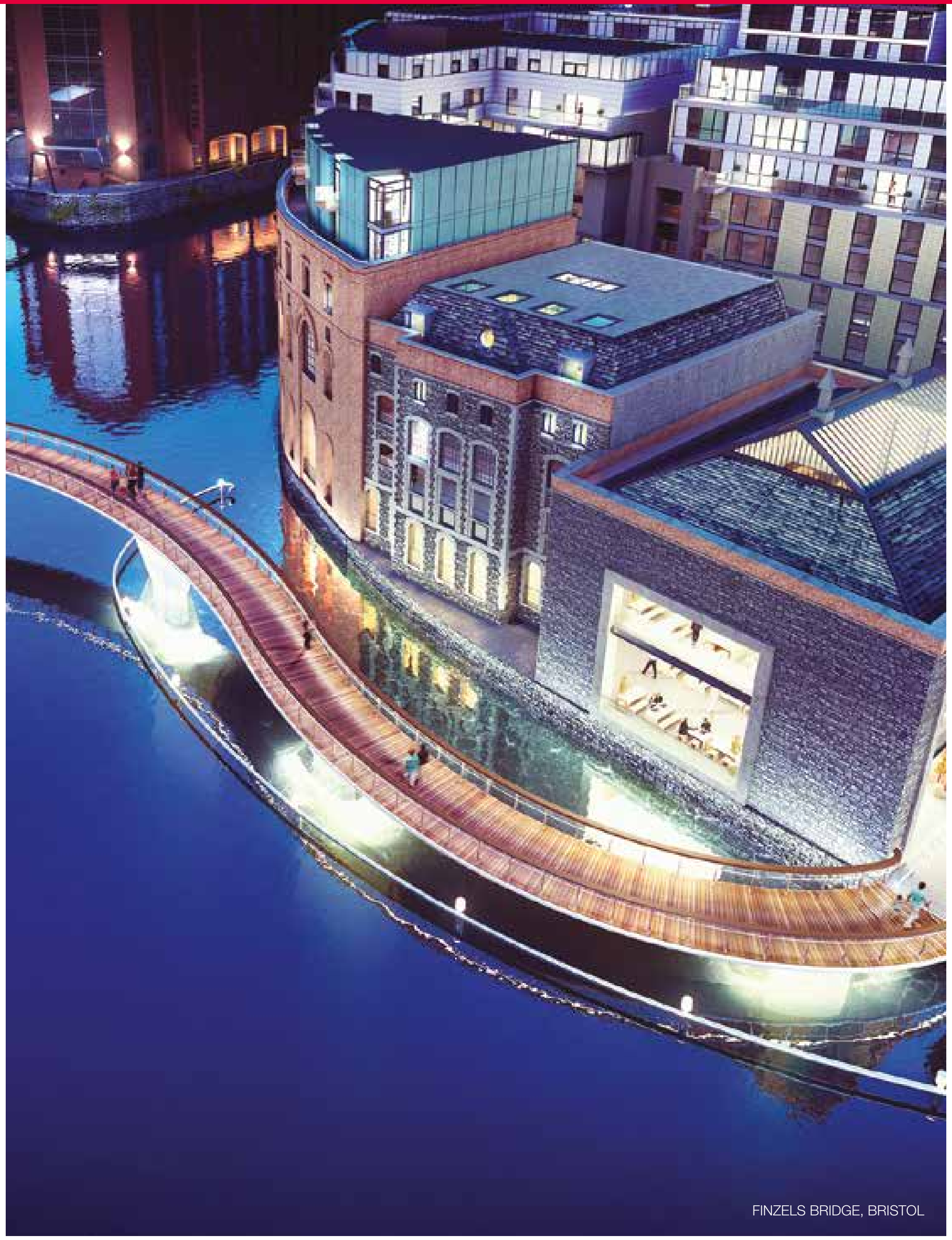
The other deal over the 50,000 sq ft threshold was the freehold purchase of The Core on Thomas Street by Direct Line.

Skewed by HMRC's pre-letting, the public sector accounted for the highest proportion of take-up at 21%, up from 17% in 2015. Professional service occupiers maintained their focus on Bristol, representing a fifth of annual take-up, whilst the TMT sector accounted for 18% of space let.

The availability of Grade A space fell to just 52,000 sq ft by year-end, the lowest level of any major regional city in the UK. This total is 77% below the long-term average.

The shortage of stock will persist in the coming 12 months. Only 95,500 sq ft of new space, together with 100,000 sq ft of refurbished office space, is due for delivery in the coming 12 months. The first completion date is not until Q3 however.

In 2016, prime headline rents were unchanged at £28.50 per sq ft. Given the widening gap between supply and demand, we anticipate prime rents will increase to over £30.00 per sq ft by year-end 2017.



FINZELS BRIDGE, BRISTOL

INVESTMENT MARKET

Although transactions slowed following the EU vote, total office investment was well above the long-term average in 2016. With demand remaining solid, yields were unchanged despite greater market caution.

Although Bristol experienced a fall in investment volumes in the second half of 2016, turnover for the year totalled £350m, 79% above the 10-year average.

The largest deal of 2016 was the funding of 3 Glass Wharf at Temple Quay, which sold to Legal & General for circa £75m. This was one of three transactions over £25m to complete in 2016.

The other two included the acquisition of Bridgewater House by a private investor for £56.3m. The deal reflected a net initial yield of 5.35%. Following this, Two Temple Back East sold for £34.1m. Bought by Ardstone Capital from Deka Immobilien, the purchase price represented a net initial yield of 5.8%. The 87,500 sq ft Grade A office building is let to law firm Osborne Clarke until 2022.

Since the result of the EU referendum, a considerable number of UK investors have assumed a more cautious approach, which explains the below average number of transactions in H2 2016. Demand remained relatively strong from overseas investors however. Foreign investment accounted for 17% of investment volumes in 2016, with the favourable exchange rate likely to support continued interest in 2017.

Looking ahead, demand for Bristol city centre offices remains robust. Whilst rental growth forecasts are not quite as aggressive as prior to the EU referendum, the market recognises the supply / demand imbalance within the occupational market.

Prime office yields currently stand at 5.25% assuming a minimum term of 10 years let to an A1 covenant, rack rented with open market reviews. Yields for secondary offices typically range from 6.00% to 9.00% depending on age, quality and location.

FIGURE 1
Bristol office take-up (sq ft)

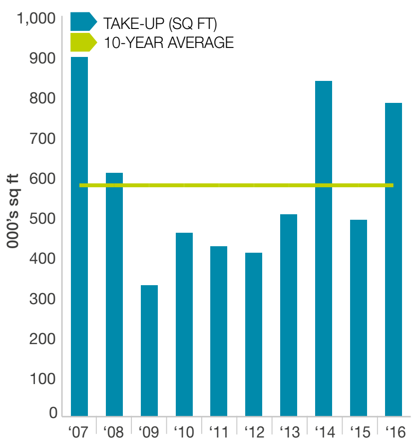
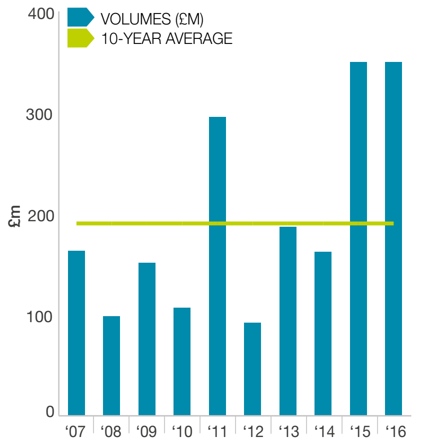


FIGURE 2
Bristol investment volumes (£m)



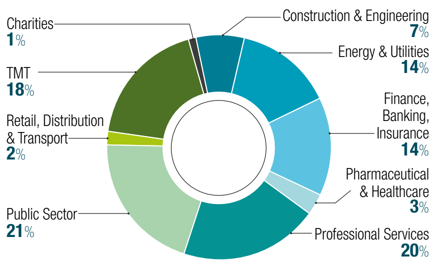
Source for all charts: Knight Frank Research, Property Data

OCCUPIER 2016

TAKE UP: **0.8m** Sq ft

GRADE A SUPPLY: **0.1m** Sq ft

TAKE UP BY SECTOR

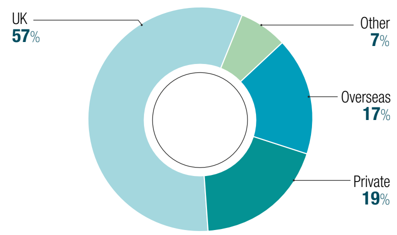


INVESTMENT 2016

VOLUMES: **£350m**

PRIME YIELD: **5.25%**

VOLUMES BY PURCHASER



KNIGHT FRANK VIEW

During 2017 we will have a market that is being pulled in many different directions. The occupational market remains robust due to a lack of supply. Whilst investors who are largely bullish on Bristol offices also share an appreciation that we are entering uncertain times following the vote to leave the EU.

On the occupational side, even if tenant demand does reduce over the next 12 months, the lack of supply across all quality grades will serve to support rents. Secondary office rents are likely to grow but not at the levels of the last two years. Prime office rents have stubbornly sat at £28.50 per sq ft for some time. However, this is more due to a lack of the right product than occupiers being overly rent sensitive. The first building to deliver the right level of specification, tenant amenity and in the right location will see rents significantly over £30.00 per sq ft.

The prime yield held firm at 5.25% and we expect this to be maintained over the next 12 months.

CARDIFF

OCCUPIER MARKET

The development pipeline is the highest for a decade with the new schemes attracting new occupiers to the city and supporting rental growth.

Overall office take-up increased 11% during 2016 to reach 685,600 sq ft, a total 39% above the 10-year average. This is the highest level of leasing activity recorded in the city for more than a decade.

The largest deal of 2016 was the pre-let of 100,000 sq ft at Two Central Square by Hugh James Solicitors. The firm agreed a 20-year lease with plans to consolidate its two existing offices on completion in August 2018. This was one of eleven deals in excess of 10,000 sq ft to complete during the year, up from nine in 2015.

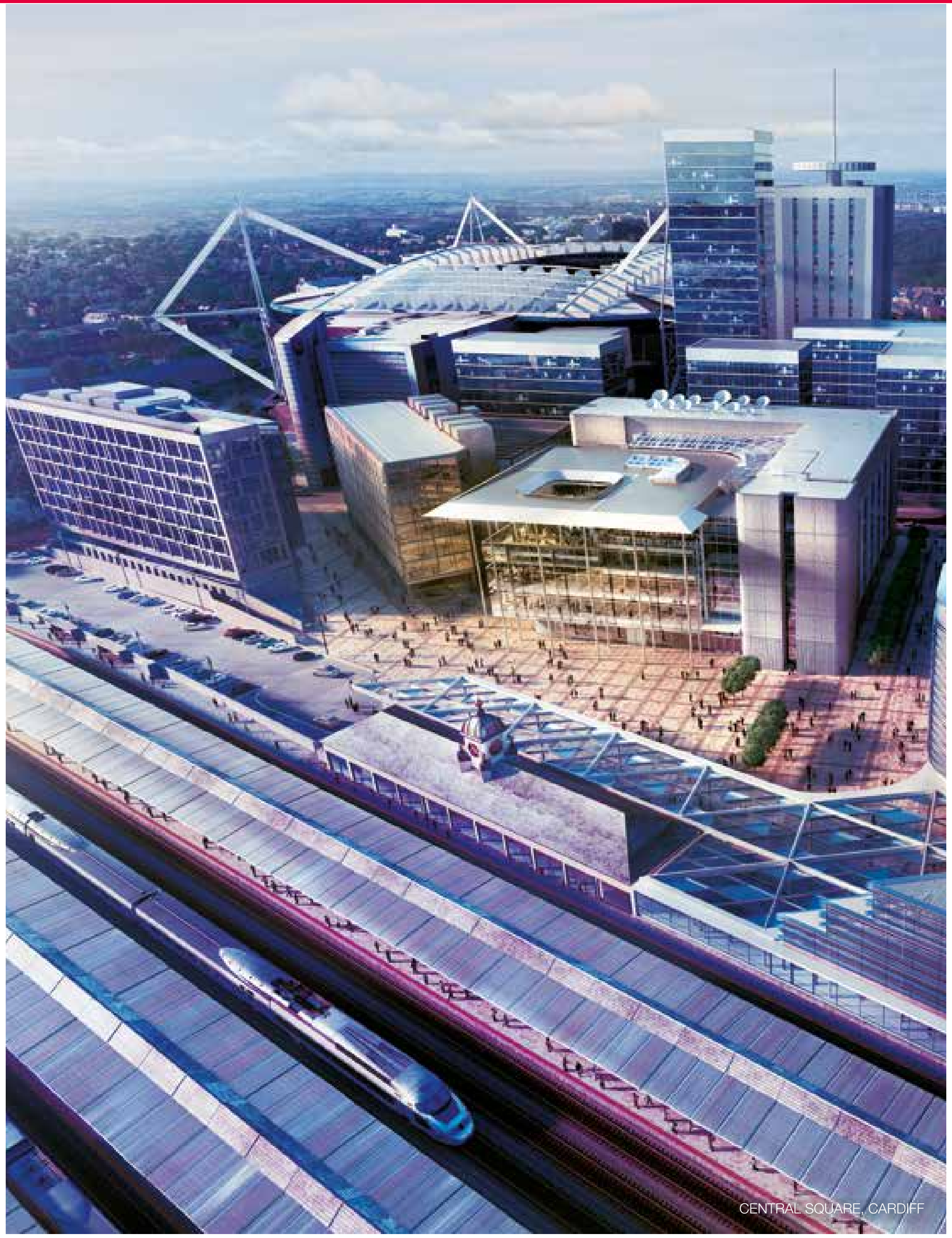
The public sector was the most active business group representing 23% of total office take-up. Notably, three of the five deals over 20,000 sq ft were agreed by a public sector organisation.

Despite the high level of leasing activity, Grade A availability had risen to 185,400 sq ft by year-end. This is twice the level recorded in Q4 2015. However, based on the current level of demand, this represents a Grade A supply of only nine months.

The level of new space coming to market in 2016 has contributed to the rise in vacancy. Development completions during the year total 308,000 sq ft of which, 214,000 sq ft came to market without a tenant secured.

The development pipeline up to the end of 2018 stands at 423,000 sq ft. Of this total only 173,000 sq ft is available. With further lease agreements prior to practical completion likely to reduce this number further, the impact of availability will be minimal.

Following the lettings at Central Square, the prime headline rent in Cardiff increased to £25.00 per sq ft in 2016, the first rise for three years. Forecasts indicate that the prime rent will be maintained at this level throughout 2017.



CENTRAL SQUARE, CARDIFF

INVESTMENT MARKET

A strong occupational market and favourable exchange rate supported investor interest in Cardiff during 2016. Yields have held firm and continue to offer value when compared to other regional opportunities.

Following a record level of office investment last year, investment activity in 2016 was more subdued. Investment turnover fell by 55% during the year with office sales amounting to £107m. Nevertheless, the fall is from a high base. Tellingly, the 2016 total is 12% above the 10-year average and represents the second highest total since 2007.

The acquisition of 3 & 4 Callaghan Square located in Cardiff's central business district, with current tenants include British Gas, the British Transport Police Authority and Zurich Insurance, by Deutsche Asset & Wealth Management for £32m was the largest transaction to complete in 2016. This sale was one of four sales over £10m completed during 2016.

The £21m acquisition of One Capital Quarter by a private investor was the second largest transaction of 2016. Significantly, private money accounted for 22% of total investment in 2016. This is up from just 4% last year.

Overseas buyers remained active in 2016 reflecting an acceptance of the growth vision for Cardiff. Foreign money accounted for 37% of investment turnover representing the highest concentration of overseas capital in the city since 2011. The fall in the value of sterling will further bolster the case for investment into UK property moving forward. Investment from domestic sources fell from 24% to 21% with UK institutions largely absent from the market.

Whilst the appetite for prime stock has held firm, the market for secondary assets has been more challenging. US Private Equity buyers continue to show interest, particularly for lot sizes in excess of £20m, albeit opportunities in 2016 have been few given the expected level of return.

Notwithstanding further market shocks, we anticipate that prime yields will stay at 5.75%. This is now unchanged for almost 2 years. At this level yields remain 75 basis points above the market peak of 5.00% recorded in 2007.

FIGURE 1
Cardiff office take-up (sq ft)

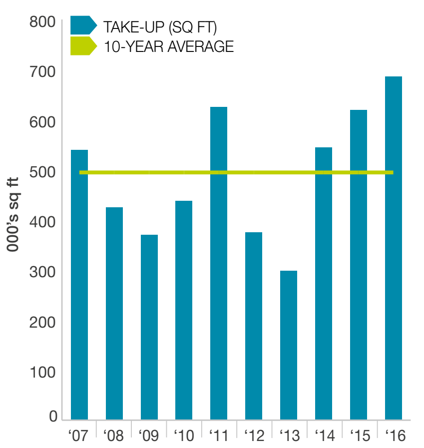
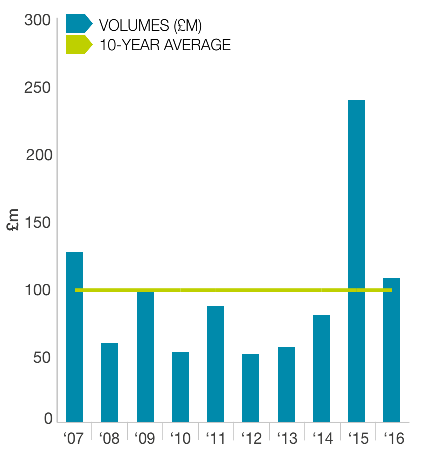


FIGURE 2
Cardiff investment volumes (£m)



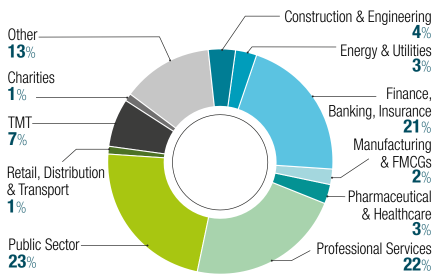
Source for all charts: Knight Frank Research, Property Data

OCCUPIER 2016

TAKE UP: **0.7m** Sq ft

GRADE A SUPPLY: **0.2m** Sq ft

TAKE UP BY SECTOR

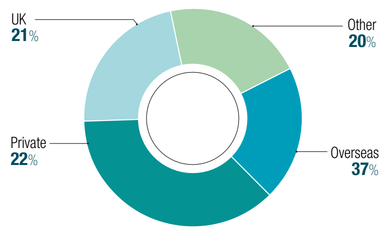


INVESTMENT 2016

VOLUMES: **£107m**

PRIME YIELD: **5.75%**

VOLUMES BY PURCHASER



KNIGHT FRANK VIEW

Cardiff has seen a number of significant occupiers commit to new space in the city centre over the last twelve months. The notable success at the Central Square and Capital Quarter schemes have, and continue, to deliver new Grade A stock that was previously in short supply. The increasing growth of the city's three universities is also notable, with these institutions providing the talent to support the staffing needs of current and potential occupiers.

The development pipeline is significant with the large number of cranes on the city's skyline testament to the confidence and ambition that both occupiers and investors have in Cardiff's future. The challenge moving forward will be to spread the success being enjoyed in Cardiff to the wider city region. Fundamental to growth is transport infrastructure improvement. Success here will open up new areas of the city, encouraging the next phase of expansion.

EDINBURGH

OCCUPIER MARKET

Despite political factors undermining occupier confidence, demand levels held firm in 2016. In tandem, availability fell to a four-year low with the market imbalance fuelling rental growth.

Office take-up in Edinburgh's city centre fell by 14% during 2016 to reach 584,200 sq ft by year-end. Despite the fall, the 2016 total was on par with the long-term average.

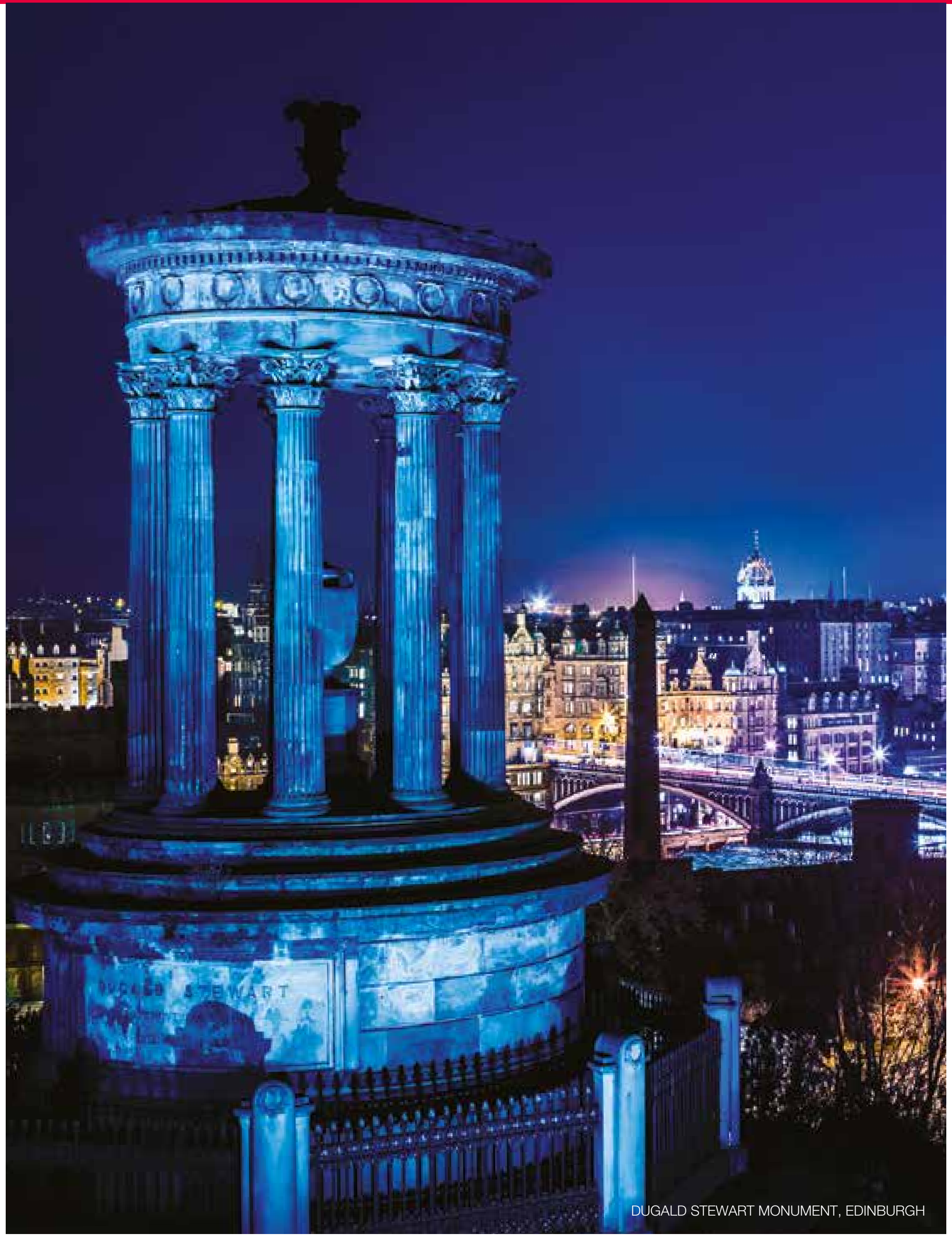
The largest transaction in 2016 was the 70,000 sq ft letting at Quartermile 4 to IT firm Cirrus Logic. Notably, the building – part of the mixed-use redevelopment of the former Royal Infirmary of Edinburgh – reached practical completion in Q2 2016 fully let. This demonstrates the imbalance between supply and demand of high quality space which was evident throughout 2016.

The Technology, Media and Telecoms (TMT) sector again accounted for the highest proportion of take-up during the year. The business group represented 32% of total office take-up in 2016, up from 29% last year. Significantly, TMT occupiers were responsible for four of the ten deals over 10,000 sq ft agreed in 2016.

The most active group in terms of deal number was professional services however, accounting for 24%, a similar percentage as 2015. The 32,000 sq ft lease to Ernst & Young at Atria 2 was the largest deal agreed by the sector.

Year-end availability of Grade A space stood at 267,000 sq ft, the lowest level since 2012. This total is 14% below the long-term average for the city. With just three schemes, totalling 185,000 sq ft due to complete over the coming 24 months, the supply shortage is set to continue.

In 2016, prime headline rents increased by 6% to reach £33.00 per sq ft, a record for the city. Current forecasts indicate that prime rents will surpass £35.00 during 2017.



DUGALD STEWART MONUMENT, EDINBURGH

INVESTMENT MARKET

Overseas buyer interest supported a 10-year high for office investment in 2016. Despite sentiment wavering around the EU vote, prime yields were unchanged highlighting the depth of demand.

Total office investment increased 35% in 2016 to reach £445m. This is not only 80% above the 10-year average but also represents the highest annual total achieved since 2006. Interestingly actual deal numbers were down when compared to 2015. Significantly, five transactions above £25m completed during the year. This compares with three in all of 2015.

The acquisition of Atria for £105m by DEKA Immobilien was the largest transaction to complete in 2016. Sold by the city council, the 200,000 sq ft Atria development is located in Edinburgh's Exchange District. Tenants include PwC, Brewin Dolphin, Aon, IBM, the UK Green Investment Bank, the Law Society of Scotland, Alliance Trust and Lothian Pension Fund. The deal represents the largest single investment transaction in the city for two years and is the second largest on record.

Overseas purchasers represented the principal source of investment in Edinburgh in 2016, accounting for 70% of total volumes. German investors accounted for 56% of investment turnover, and were responsible for all purchases above £50m with the acquisition of both Waverley Gate and Quartermile 4 by TRIUVA other notable deals completed in 2016.

The rise in interest from overseas buyers is timely, with interest from UK buyers slowing. Domestic money accounted for 27% of investment volumes in 2016, down from 51% in 2015. UK institutions in particular have been reluctant to invest in Scotland due to perceived political instability during the year. UK institutions accounted for just 5% of investment volumes in 2016. This compares with 43% in 2015.

Nonetheless, with demand strong, prime yields in Edinburgh remained at 5.25% throughout 2016, pricing that still offers a discount compared to other UK regional cities. At this level, yields are 75 bps above the 4.50% recorded at the peak of the last cycle in 2007.

FIGURE 1
Edinburgh City Centre office take-up (sq ft)

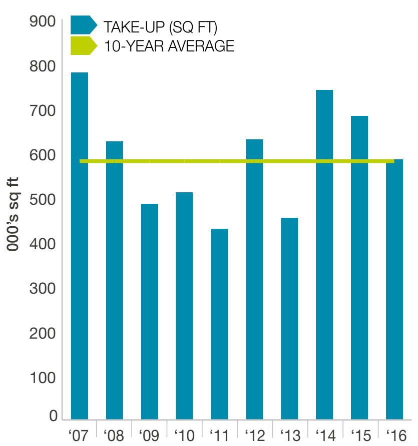
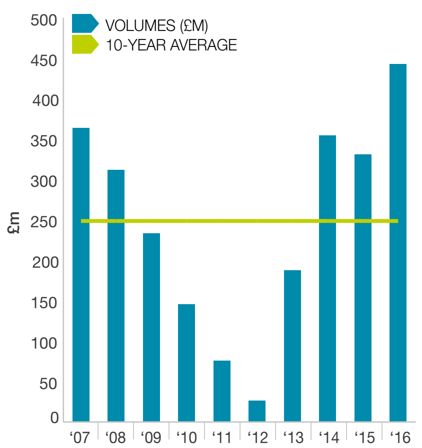


FIGURE 2
Edinburgh investment volumes (£m)

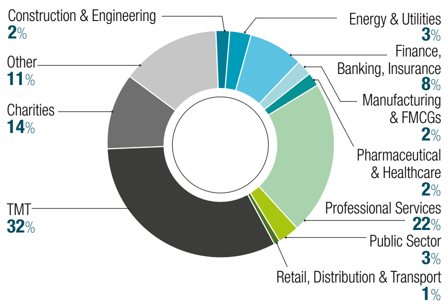


Source for all charts: Knight Frank Research, Property Data

OCCUPIER 2016

TAKE UP	GRADE A SUPPLY
0.6m Sq ft	0.3m Sq ft

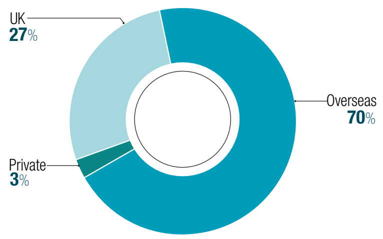
TAKE UP BY SECTOR



INVESTMENT 2016

VOLUMES	PRIME YIELD
£445m	5.25%

VOLUMES BY PURCHASER



KNIGHT FRANK VIEW

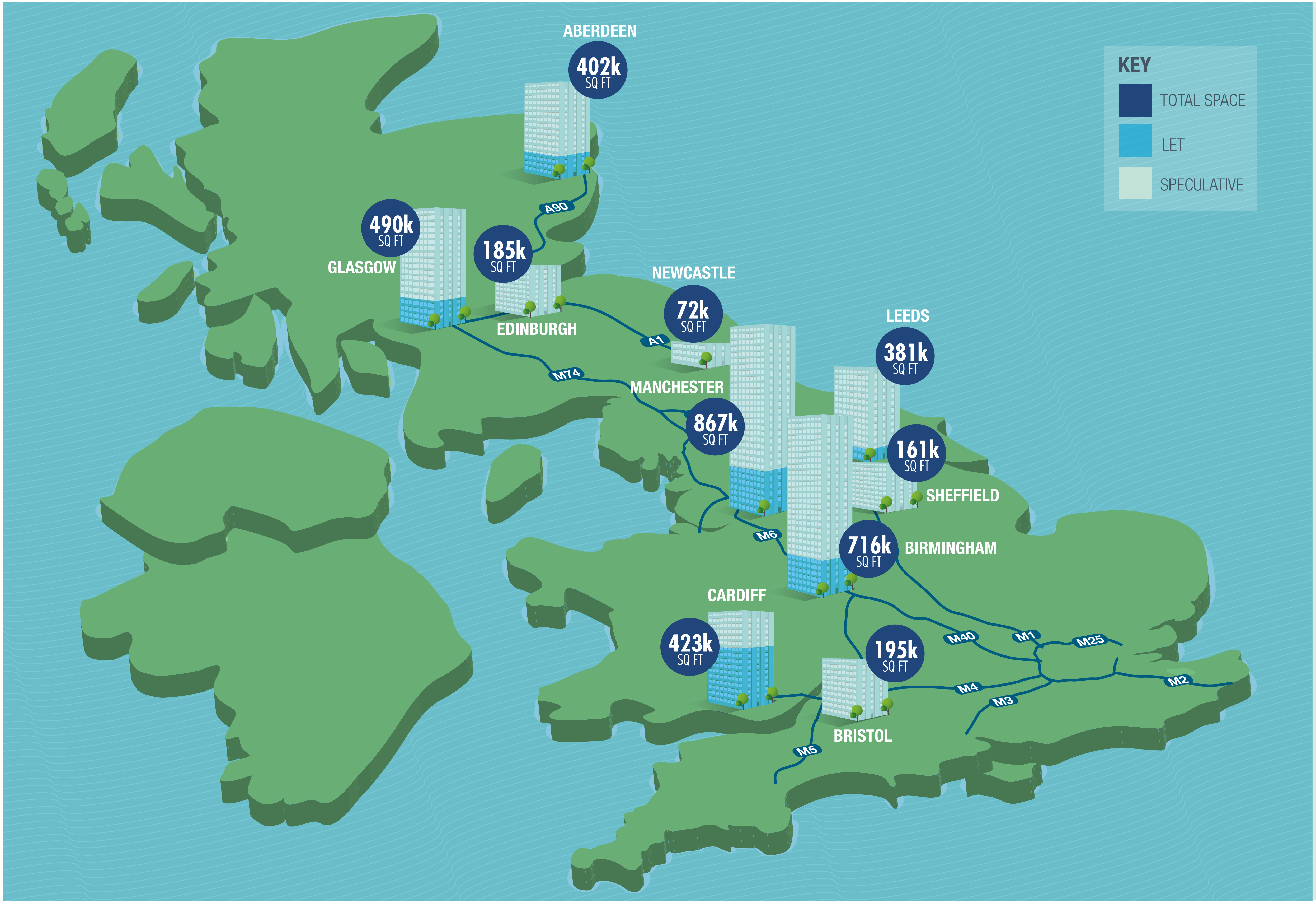
Encouragingly, occupier take-up was in line with the long-term average, with the TMT sector again a major source of office demand in 2016. Edinburgh's emergence as a major UK technology cluster will continue in 2017.

Grade A availability is at its lowest level for five years, with the development pipeline limited. The gap between supply and demand will not rebalance in 2017, opening up the prospect of further rental growth.

The likelihood of rental growth is one of a number of factors that have seen overseas buyers flock to invest in Edinburgh. Remarkably, given the events of 2016, investment volumes increased by 35% over the previous year and were 80% above the ten-year average. Overseas investors dominated in 2016 and will undoubtedly be the primary buyers in the year ahead.

With its attractive pricing, strong prospects for rental growth and continuing evolution into a European capital city, we expect Edinburgh's office market to perform strongly in the year ahead, from both an investment and occupational viewpoint.

THE DEVELOPMENT LANDSCAPE 2017/18



Supported by a shortage of Grade A supply across many regional centres, the amount of office space under construction reached the highest total since the financial crisis in 2016.

Total
(next two years)

3.9m sq ft

2017

2.9m sq ft

2018

1.0m sq ft

The statistics on this page represent office space known to be under construction with a delivery date before year-end 2018. Both new and comprehensive refurbishment schemes are included in the development pipeline.

GLASGOW

OCCUPIER MARKET

An increase in occupier demand in 2016, meant that take-up reached the highest total for three years. Grade A availability fell to a seven-year low before completions supported a rise by year-end.

Overall office take-up increased 21% during 2016 reaching 689,000 sq ft by year-end, a total 24% above the 10-year quarterly average. This is the highest level of leasing activity recorded in the city since 2013.

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 154,814 sq ft. This represents the largest occupier deal in the city for three years.

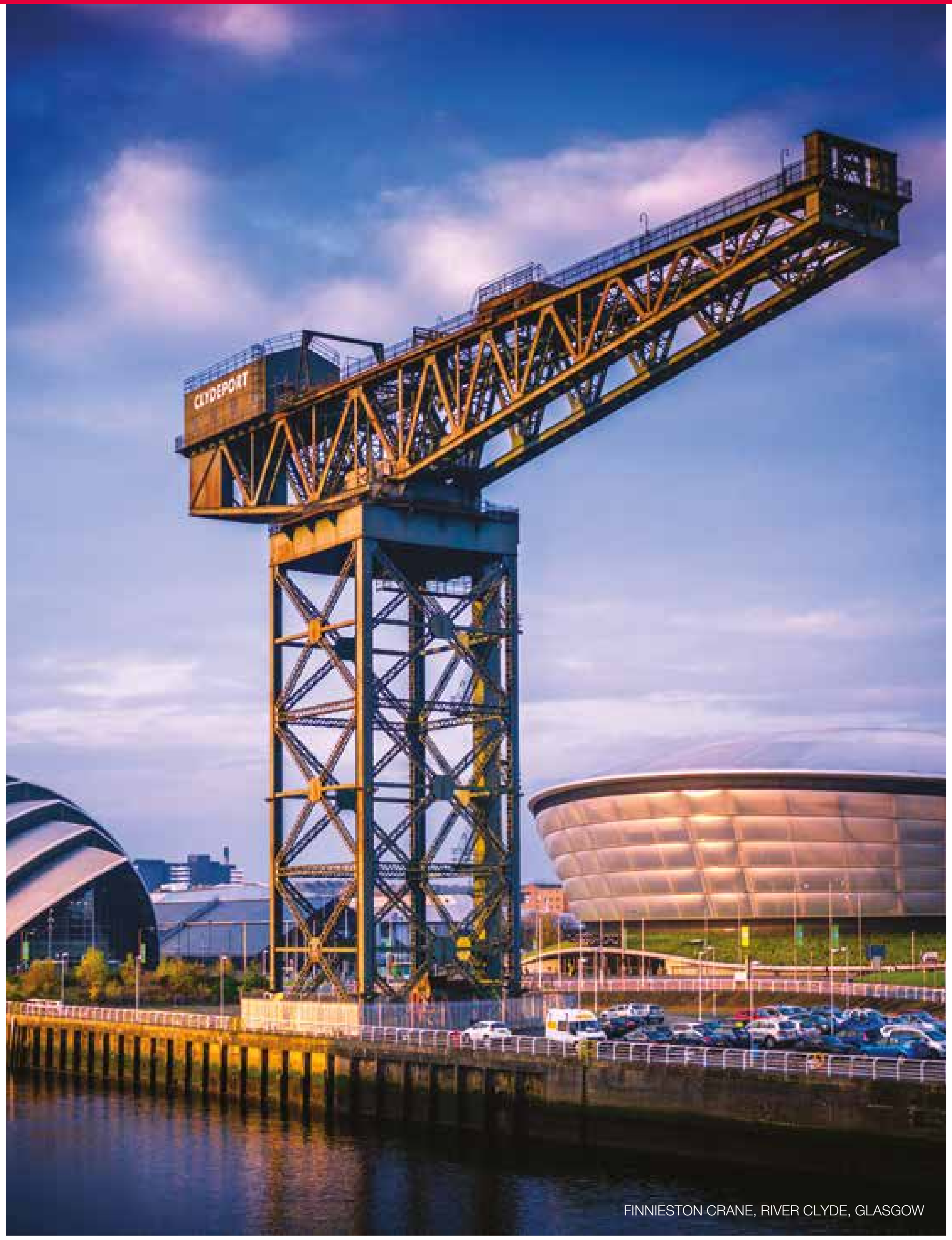
Other notable deals completed in 2016 include AXA agreeing terms on 50,000 sq ft at the Cuprum office building, rendering the property fully let. The deal meant that the insurance firm could vacate two Glasgow offices at Atlantic Quay and Hutcheson Street. In addition, serviced office provider Regus agreed terms on 30,000 sq ft at Tay House, Bath Street.

With three of the four lettings over 30,000 sq ft to a Financial or Business Services occupier, this business group accounted for the highest proportion of take-up in 2016, (39%). Occupiers from the professional services also maintained its strong interest in Glasgow in 2016. Supported by the 56,000 sq ft letting to ACCA, this group accounted for 19%.

On the supply side, Grade A availability had fallen to the lowest level for seven years in Q2 before rising to 386,500 sq ft by year end.

The development pipeline is due to deliver 490,000 sq ft over the next 24 months, of which 69% is speculative space. Notably, all schemes under construction are comprehensive refurbishments.

In 2016, following the completion of an exceptional deal, prime headline rents increased by 2% to reach £30.00 per sq ft. Given the level of demand at year-end, further growth is expected in 2017.



FINNIESTON CRANE, RIVER CLYDE, GLASGOW

INVESTMENT MARKET

A shortage of stock restricted investment activity in 2016 with volumes at a five-year low. Yields remained unchanged reflecting continued appetite for prime products.

Investment volumes fell 68% in 2016, with £109m of office stock sold during the year. This total is 46% below the 10-year average. Significantly, deal numbers were sharply down with just 12 transactions completing during 2016. This compares with 26 in 2015.

The acquisition of 2 West Regent Street by TH Real Estate on behalf of Warburg HIH for £31.50m was the largest transaction in 2016. The deal reflected a net initial yield (NIY) of 5.84%. The multi-let Grade A property sits within an improving street in the CBD and had a WAULT of 6.52 years. This was one of three sales exceeding £10m in 2016, compared to 11 in 2015.

Interestingly, overseas buyers were responsible for two of the deals over £10m with the 2 West Regent Street sale the largest. Following this, UBS Asset Management acquired the Grosvenor Building on Gordon Street for £17.85 million, reflecting a yield of 6.9%. Cigna and Bank of Scotland are the current tenants of the building. These purchases meant that foreign money represented 45% of investment volumes in 2016.

The other purchase over the £10m threshold was the acquisition of 50 Bothwell Street by Fore Partnerships for £23.5m. This was one of two purchases in Glasgow by the group in 2016. Standard Life Investments are the main tenant to the office building with part of the ground floor used for retail. This high value sale meant that private investors represented 32% of investment volumes.

Tellingly, sales to domestic buyers were few in 2016. UK investors accounted for 15% of investment volumes with the UK institutions largely absent from the market. This compares to 46% in 2015.

Prime yields in Glasgow remained at 5.50% throughout 2016, pricing that offers a relative discount to other UK regional cities. Prime yields at this level are a full 100bps above the market peak of 4.50% recorded in 2007.

FIGURE 1
Glasgow office take-up (sq ft)

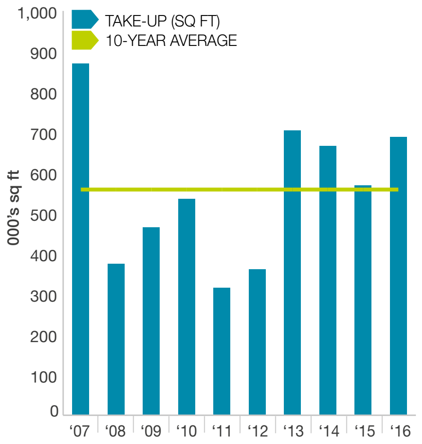
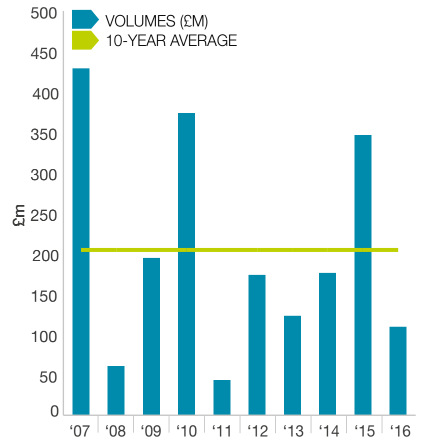


FIGURE 2
Glasgow investment volumes (£m)



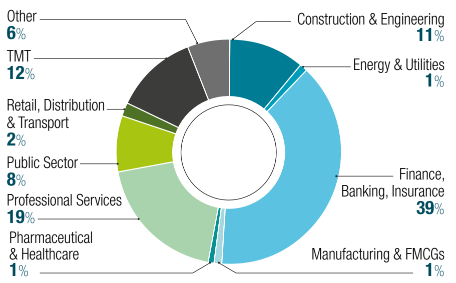
Source for all charts: Knight Frank Research, Property Data

OCCUPIER 2016

TAKE UP: **0.7m** Sq ft

GRADE A SUPPLY: **0.4m** Sq ft

TAKE UP BY SECTOR

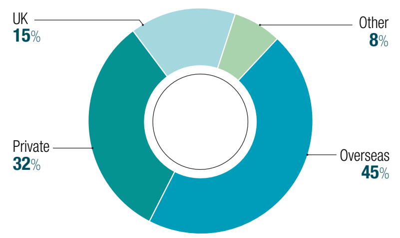


INVESTMENT 2016

VOLUMES: **£109m**

PRIME YIELD: **5.50%**

VOLUMES BY PURCHASER



KNIGHT FRANK VIEW

In 2016, investment transactions were below the 10-year average mainly due to a lack of quality investment product as opposed to a lack of demand. Over the course of 2017, there will be a number of quality developments becoming close to or fully let which is likely to release absolutely best in class assets to the market. We believe that this will attract aggressive bidding, particularly from international buyers, leading to higher transaction volumes.

In the occupier market, pressure on new Grade A space availability is mounting, which is presenting an opportunity for very good Grade A refurbishments, particularly for those that offer large floorplates. Occupier choice in the 4,000-6,000 sq ft market is greater however, meaning incentives are likely to remain favourable with competition for occupiers intense. Given this position and the uncertain political and economic environment, an increase in re-gears at this requirement size is anticipated in 2017.

LEEDS

OCCUPIER MARKET

Despite demand improving in the second half of the year, take-up in 2016 fell short of the long-term average. Development completions were the highest since 2008, which led to a rise in availability of Grade A space.

Following the high level of occupier activity last year, 2016 proved to be slower with 116 deals completed. This compares to 160 in 2015. As a result, take-up for the year reached 435,800 sq ft, 36% less than in 2015 and 13% below the long-term average. Notably, 60% of transactions completed after the EU referendum in June.

The two largest deals of the year completed in H1 however. In March, Sky Bet agreed terms on a 39,000 sq ft lease at Number Six Wellington Place. The online betting firm, already a tenant within the development, signed for an additional two floors. Following this, RSM leased 25,500 sq ft at Central Square on a 15-year term. The consultancy firm is due to take occupation in June 2017. These deals were two of four over 20,000 sq ft to complete in 2016.

In H2, the Department of Health leased 23,760 sq ft at APAM's Whitehall II building. The government department took the fifth and sixth floor on a 5-year term.

In October, the Medical Protection Society (MPS) acquired 22,685 sq ft at 1 Victoria Place. The deal follows the acquisition of 2 and 3 Victoria place by the MPS in 2012.

Professional Services accounted for 29% take-up in 2016, down from 35% in 2015. Supported by the Sky Bet deal, the TMT sector accounted for 25% as Leeds again proved an attractive location for digital occupiers.

Grade A availability increased to 441,000 sq ft, the highest total since 2011. The rise follows the completion of 280,000 sq ft of new Grade A accommodation. A further 271,000 sq ft across 3 Wellington Place, 7 Park Row and Platform respectively is due is 2017.

In 2016, prime headline rents were unchanged at £27.50 per sq ft, a level supported in various transactions. We anticipate prime rents will increase to £28.00 per sq ft by year-end as supply is absorbed quickly by several outstanding large requirements.

3 SOVEREIGN SQUARE, LEEDS

INVESTMENT MARKET

Transaction volumes in 2016 remained consistent with the long-term average with overseas investors driving the market. Yields stayed at the lowest level since 2014, with demand for prime assets remaining strong.

Investment volumes fell by 15% year-on-year to reach £175m at year-end. Despite this, the 2016 total is marginally above (1%) the long-term average for the city.

Interestingly, although fewer high value sales completed in 2016, the acquisition of 3 Sovereign Square by Leeds City Council for £43.75m represents the largest office sale in Leeds since 2011. The building, a new development bought from a Bruntwood Estates and Kier Group JV, is the new HQ of law firm Addleshaw Goddard. The law firm agreed a 50,000 sq ft lease in 2015. This was one of two deals above £25m in 2016.

The other, was the sale of Number One Leeds on Whitehall Road for £34.2m. Bought by Credit Suisse, the deal follows the acquisition of the Princes Exchange, 2 City Walk and 1 Park Lane by the investor (the latter two were both subsequently sold). Tenants at Number One Leeds include the Yorkshire Post newspaper and energy firm GDF Suez.

Other noteworthy deals in 2016 include EPIC UK Ltd's acquisition of St. Paul's House from Boultbee Brooks Real Estate for £23.7m at a net initial yield of 6.00%. In addition, the sale of 1 Park Lane to a Private Middle Eastern investor for £19.1m completed at year-end.

Overseas money represented the highest proportion of investment in 2016, 48%. Domestic investors accounted for 20% of turnover down from 57% in 2015. In terms of deal number, UK buyers were responsible for 6 of the 13 deals completed in 2016.

The consistent level of demand meant that prime office yields held firm at 5.25% throughout the year. At this level, prime yields are 50 basis points above the market peak of 4.75% recorded in 2007. In 2017, we anticipate that yields for prime products to stay around 5.25%. Secondary yields may weaken however, with investors becoming more risk-averse post the EU vote.

FIGURE 1
Leeds office take-up (sq ft)

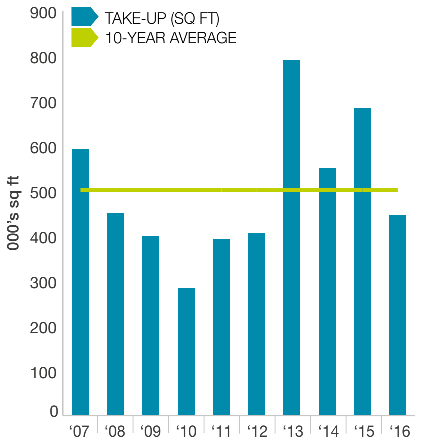
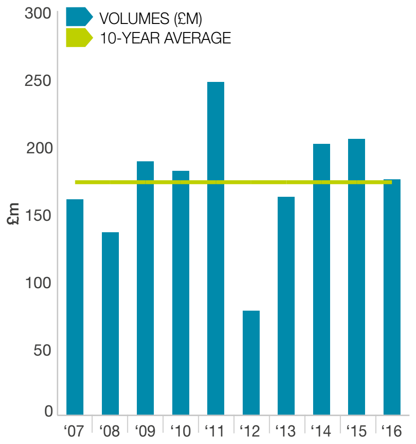


FIGURE 2
Leeds investment volumes (£m)



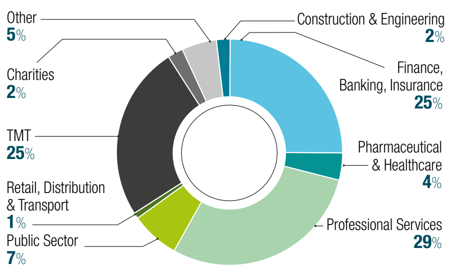
Source for all charts: Knight Frank Research, Property Data

OCCUPIER 2016

TAKE UP: **0.4m** Sq ft

GRADE A SUPPLY: **0.4m** Sq ft

TAKE UP BY SECTOR

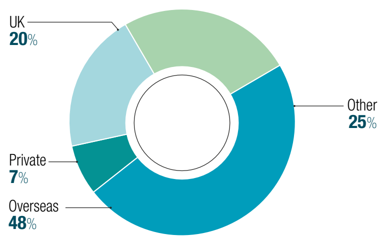


INVESTMENT 2016

VOLUMES: **£175m**

PRIME YIELD: **5.25%**

VOLUMES BY PURCHASER



KNIGHT FRANK VIEW

With the aspirations of landlords and tenants moving apart, the 'renewal rather than relocate' trend will be reversed in 2017. In particular, new and existing occupiers are requiring more flexible space solutions. A move toward mobile ways of working underpins this shift, a change in occupier focus that will drive an increase in space moves over the coming year.

In 2016, the headline rent of £27.50 per sq ft was re-established following the BDO LLP letting. This is significant as it means that new builds, which benefit from significantly lower running costs and efficient layouts, are looking good value. As such, we anticipate that rents of £28.00 per sq ft will be achieved at 6 Queen Street, Wellington Place, 3 Sovereign Square and Central Square in the very near future, moving forward to £30 per sq ft as occupiers compete for the best space in these buildings, in particular Platform.

MANCHESTER

OCCUPIER MARKET

A strong Q4 meant that take-up exceeded 1.3m sq ft for the third year running. Despite several development schemes reaching completion, availability remained 25% below the long-term average.

Manchester recorded the highest level of occupier take-up for six years in Q4 2016, with 621,000 sq ft transacted. This meant that total office take-up for the year reached 1.3m sq ft, a total 24% above the 10-year average. Interestingly, actual deal number in 2016 was less than in the previous two years with 263 deals completed. This compares to over 300 transactions in each 2015 and 2014.

Underpinning take-up was the 165,000 sq ft letting to Swinton Insurance at 101 Embankment. The building reached completion in Q3 2016 with the lease representing the largest occupier deal in the city since 2010.

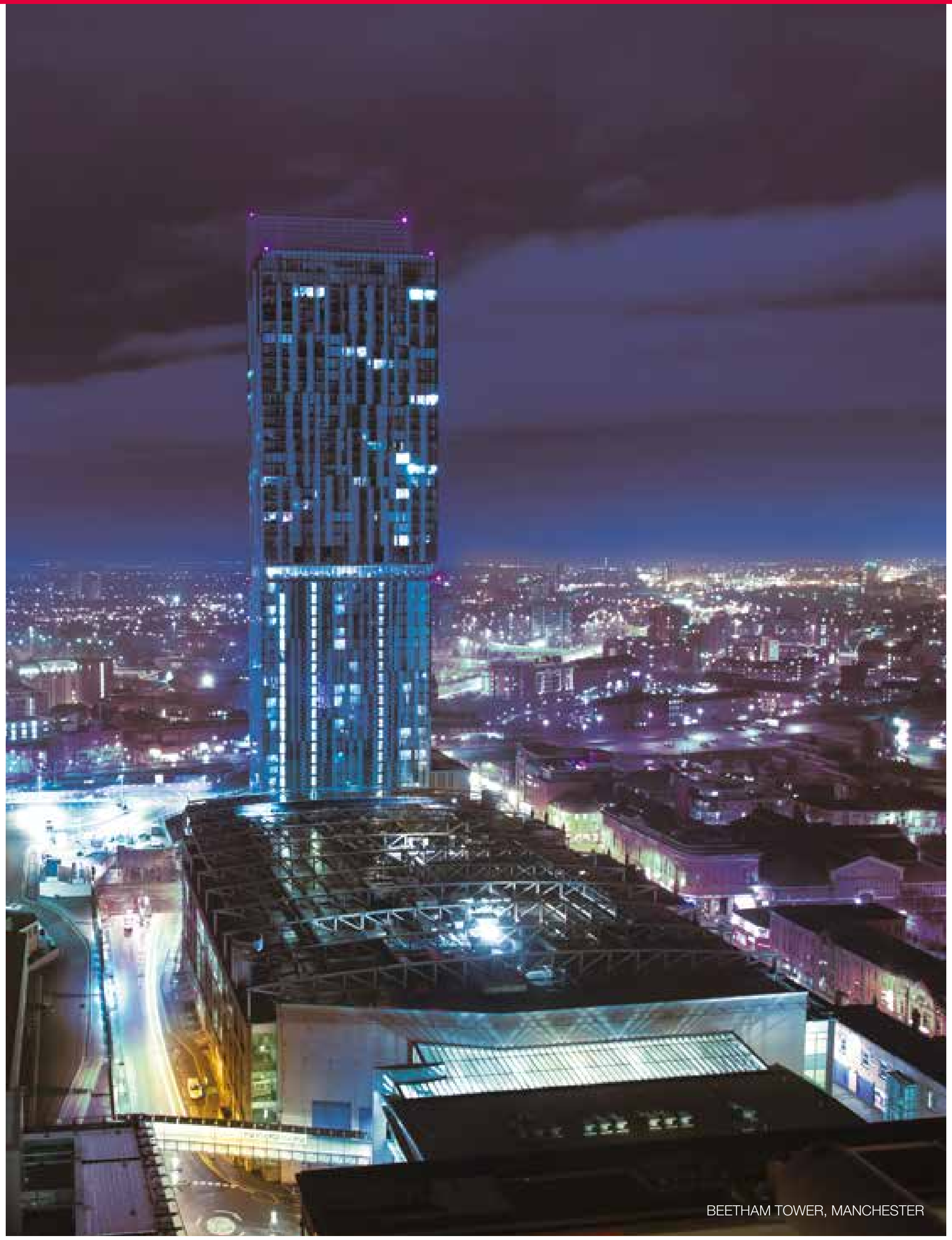
Prior to this, law firm Freshfields Bruckhaus Deringer leased 81,300 sq ft at One New Bailey. This deal represents the largest inward investment deal in Manchester on record. Before year-end, Manchester Metropolitan University also purchased 63,700 sq ft at 6 Great Marlborough Street. This meant that in 2016, three deals over 50,000 sq ft completed, the same number as in the previous two years.

Professional Services accounted for the highest proportion of take-up at 30% in 2016. A rise in demand from the TMT sector was most notable however, with this sector accounting for 20%.

Grade A availability increased marginally (4%) during 2016 to reach 220,000 sq ft. Despite the rise, the Q4 total is 25% below the long-term average for the city. Notably, this total represents just six months' Grade A supply.

In terms of future supply, the development pipeline in Manchester is significant, with 867,000 sq ft due to complete over the next 12 months. Of this 649,000 sq ft is speculative.

In 2016, prime rents increased by 6% to £34.00 per sq ft. A further rise is anticipated in 2017, driven by strong demand and limited supply. Forecasts indicate that prime rents will rise to £35.00 per sq ft by year-end 2017.



BEETHAM TOWER, MANCHESTER

INVESTMENT MARKET

Despite the EU vote unsettling the market, total office investment volumes stayed well above the long-term average. Overseas demand remained strong maintaining pressure on pricing.

Total investment volumes in 2016 reached £619m, 4% less than recorded in 2015. Nonetheless, the 2016 total is 36% above the 10-year average. Deal number was down year-on-year with 34 investment transactions completed in 2016. This compares to 43 in 2015.

The acquisition of 2 St Peters Square by Deka Immobilien for £164m was the largest transaction in 2016. This was the second £100m regional purchase agreed by the German investor in 2016 following the Atria acquisition in Edinburgh. Located in Manchester's business district, the multi-let Grade A property had a WAULT of 16 years at the time of purchase. Tenants include KPMG, DLA Piper, Addleshaw Goddard and Mazars.

High value sales were indeed a feature on 2016. Completed in Q1, the £114m sale of Three & Four Piccadilly Place to Ares Asset Management LLC was the first investment sale exceeding £100m in Manchester since Q3 2014. The purchase of the XYZ building by Union Investment RE for £85m followed this sale. Notably, the XYZ deal reflected an initial yield of 4.8%.

In 2016, Manchester continued to attract substantial interest from international investors. Overseas buyers were responsible for all investment deals over £25m. As a result, foreign money accounted for 71% of investment turnover. The £439m spent is the highest level of overseas investment since 2007.

Overall domestic investment by volumes decreased from 37% of turnover in 2015 to just 17%. Interesting in terms of deal number, UK buyers were the most active accounting for 53% of deals. All domestic purchases were below £20m, a statistic that illustrates a strategy driven by liquidity.

Prime yields in Manchester moved out by 25bps to 5.25% in 2016, reflecting the weakened risk appetite. At this level, prime yields are 75bps above the market peak of 4.50% recorded in 2007.

FIGURE 1

Manchester office take-up (sq ft)

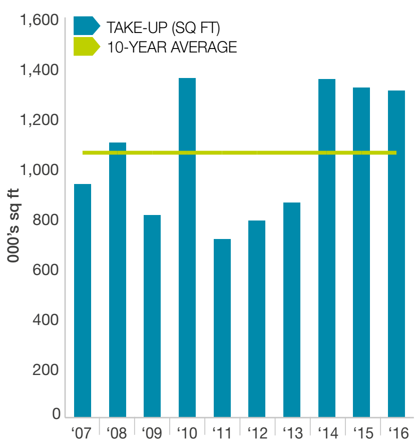
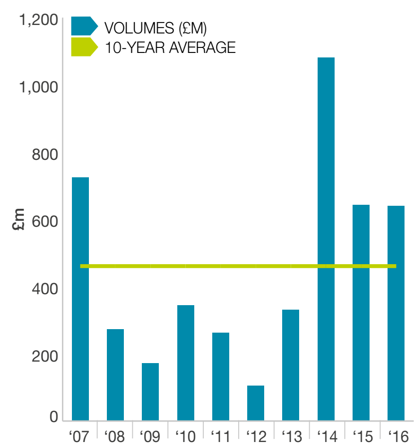


FIGURE 2

Manchester investment volumes (£m)

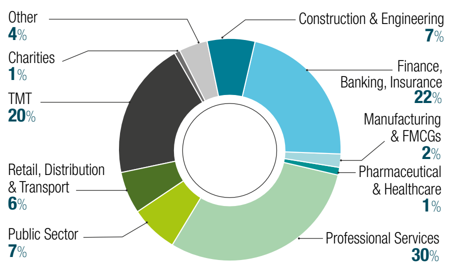


Source for all charts: Knight Frank Research, Property Data

OCCUPIER 2016

TAKE UP	GRADE A SUPPLY
1.3m Sq ft	0.2m Sq ft

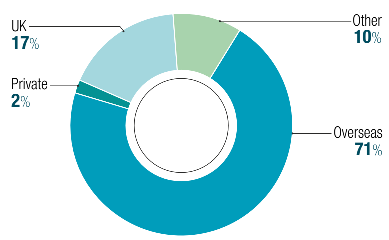
TAKE UP BY SECTOR



INVESTMENT 2016

VOLUMES	PRIME YIELD
£619m	5.25%

VOLUMES BY PURCHASER



KNIGHT FRANK VIEW

The occupational market shows no sign of weakening, with a number of large requirements yet to be satisfied. Significantly, an increasing number of international firms are looking at 'north shoring' departments into the city from London and further afield. This will put pressure on an already limited amount of supply of all grades of space, which will certainly lead to further new development during 2017, both new build and refurbished accommodation. This demand will continue to drive both prime and secondary office rents to £35.00 per sq ft and £28.50 per sq ft respectively.

In the investment market, sellers are few in number currently as vendors are busy completing business plans and are keen to catch rental growth. There is an increasing amount of buyers however, both domestic and overseas keen to secure asset management and income opportunities in the North West. As such we expect yields to sharpen in 2017.

NEWCASTLE

OCCUPIER MARKET

Office take-up in the city centre dipped in 2016, although stayed broadly consistent with the long-term average. Availability remained low, a feature of the market that will persist in 2017 with the development pipeline consisting of a small number of comprehensive refurbishment schemes.

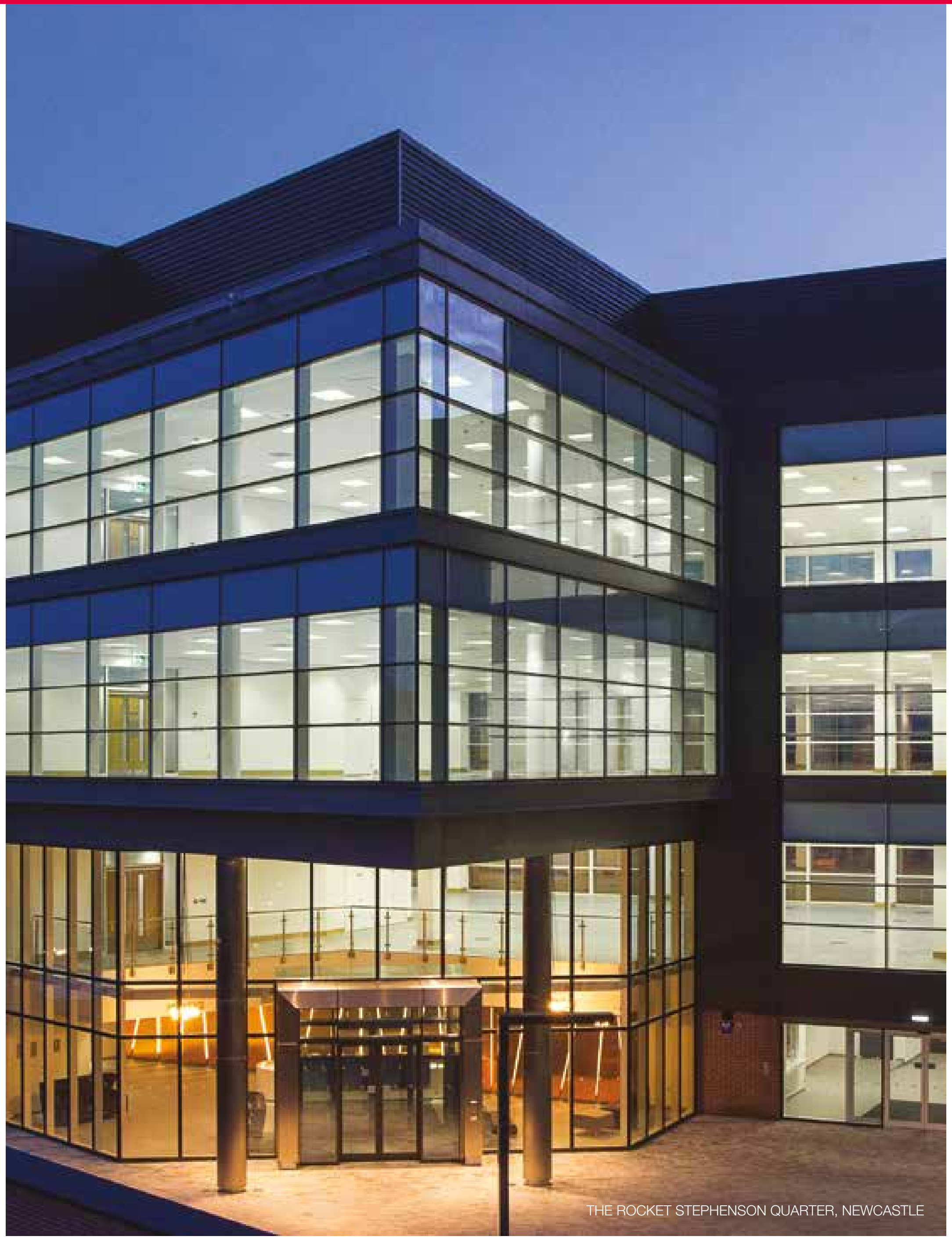
Office take-up in Newcastle city centre fell by 15% during 2016 to reach 220,000 sq ft at year-end. Tellingly, overall deal number was down year-on-year with 46 transactions completed in 2016, compared to 64 in 2015. Despite this however, total take-up in 2016 finished marginally below (4%) the long-term average for the city.

The 35,000 sq ft letting to Convergys at The Rocket in the Stephenson Quarter was the largest transaction of the year. Developed in partnership by Clouston Group and Newcastle City Council, the building reached practical completion in 2015 and forms part of the first phase of a £200 mixed-use development.

Following this deal, Regus acquired 12,875 sq ft at Cale Cross House, Newcastle Quayside. The occupation is over three floors and supplements existing Regus centres at Merchant House in the Cloth Market and Rotterdam House on Newcastle Quayside. Notably, this, combined with the Convergys deal meant that Business Services accounted for the largest proportion of city centre take-up in 2016, 22%. The TMT sector continued to flourish in Newcastle over 2016 with the most significant letting being Zerolight's new lease of the entire Liveworks development on Newcastle Quayside.

Grade A availability fell by 26% during 2016 to reach 173,300 at year-end. This total is 23% below the long-term average. The development pipeline over the next two years consists of just 72,000 sq ft split across two comprehensive refurbishment schemes. With the first completion date not until Q4 2017, this means low Grade A availability will again be a feature of the market in 2017.

In 2016, prime headline rents increased by 5% to reach £23.00 per sq ft. This is the lowest prime rent of the major UK regional cities. We anticipate prime rents will increase to £24.00 per sq ft by year-end 2017.


THE ROCKET STEPHENSON QUARTER, NEWCASTLE

INVESTMENT MARKET

The investment market in Newcastle continued to thrive in 2016 supported by strong domestic interest. Prime office yields were unchanged throughout the year, with the relative discount to regional neighbours particularly attractive.

Total investment volumes fell marginally (-2%) in 2016 to reach £181m at year-end. This total is 46% above the 10-year average for the city. Importantly, larger scale deals were a feature of the market in 2016. Two office deals over £50m completed during the year, these being the first examples above this threshold since 2010.

The largest investment deal was the £65m forward funding agreement between Legal & General Capital, Newcastle City Council and Newcastle University. The £65 million paid is an initial payment and will fund completion of two buildings that, once complete, will offer over 200,000 sq ft of Grade A office space. The deal is the largest office investment to complete in Newcastle since 2007.

The other was the sale of Newcastle University Business School for £60m. The building was acquired by Aviva Investors on behalf of its Lime Property Fund, and is located on the former Scottish & Newcastle brewery site. Newcastle University are the long-term tenants having agreed a 35 year lease on the property expiring in 2031.

Supported by these two large transactions, UK investors accounted for all office investment in Newcastle during the year. This represents the highest representation of domestic buyers since 2010. Other domestic deals included the acquisition of Citygate by Ediston Property Investment Company plc for £18.95m reflecting a net initial yield of 6.5% and the sale of Sandgate House by Legal & General for £10.75m. Interestingly, the deal for Sandgate House reflected a net initial yield of 5.88%.

Prime office yields remained at 6.00% in 2016, now unchanged since 2013. At this level, prime yields are 125 basis points above the market peak of 4.75% recorded in 2007. Strong bidding on prime assets may realise more aggressive pricing in 2017.

FIGURE 1
Newcastle office take-up (sq ft)

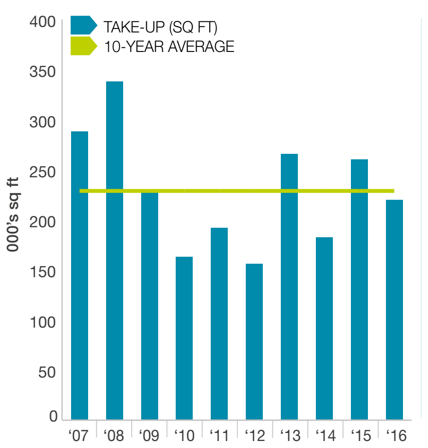
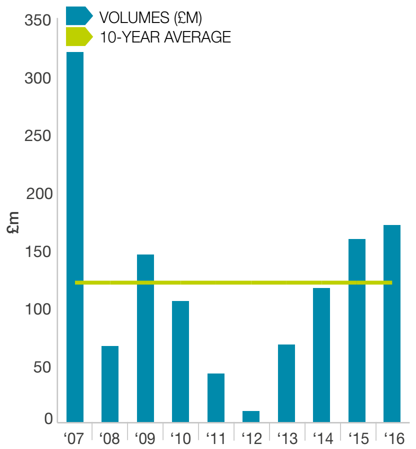


FIGURE 2
Newcastle investment volumes (£m)

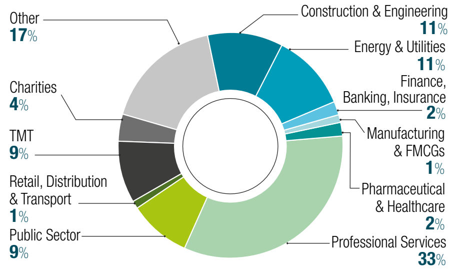


Source for all charts: Knight Frank Research, Property Data

OCCUPIER 2016

TAKE UP	GRADE A SUPPLY
0.2m Sq ft	0.2m Sq ft

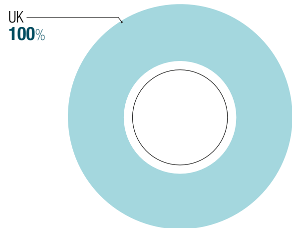
TAKE UP BY SECTOR



INVESTMENT 2016

VOLUMES	PRIME YIELD
£181m	6.00%

VOLUMES BY PURCHASER



KNIGHT FRANK VIEW

The lack of Grade A availability will continue to be the dominant theme in 2017 with only refurbishment schemes set to complete. Legal & General's initial investment of £65m in Science Central will bring forward the first 200,000 sq ft phase, but construction will start late 2017. Low supply coupled with an increase in occupier demand is likely to add upward pressure on rents, with a rise expected by year-end.

Given the political and economic events of 2016, it was inevitable that the 'Business Planning Season' at the beginning of 2017 was going to extend into February. Notwithstanding the slow start to the year, the North East Investment market is in a robust state with good prospects for rental growth across the sectors. With this in mind, and the discount on yield from the top six regional centres, we anticipate a strong year in 2017. Investment volumes should remain constant with the common theme being a hardening in prime yields as investors continue the flight to prime.

SHEFFIELD

OCCUPIER MARKET

Grade A availability fell to a historic low in 2016 with little change expected until late 2017. Occupier activity slowed which meant take-up remained below the long-term average.

Following the record level of take-up in 2015, occupier activity in 2016 proved slow with 63 deals completed. This compares to 84 in 2015. Despite the decrease in deal number, total office take-up in 2016 reached 201,500 sq ft, 36% below the 10-year average.

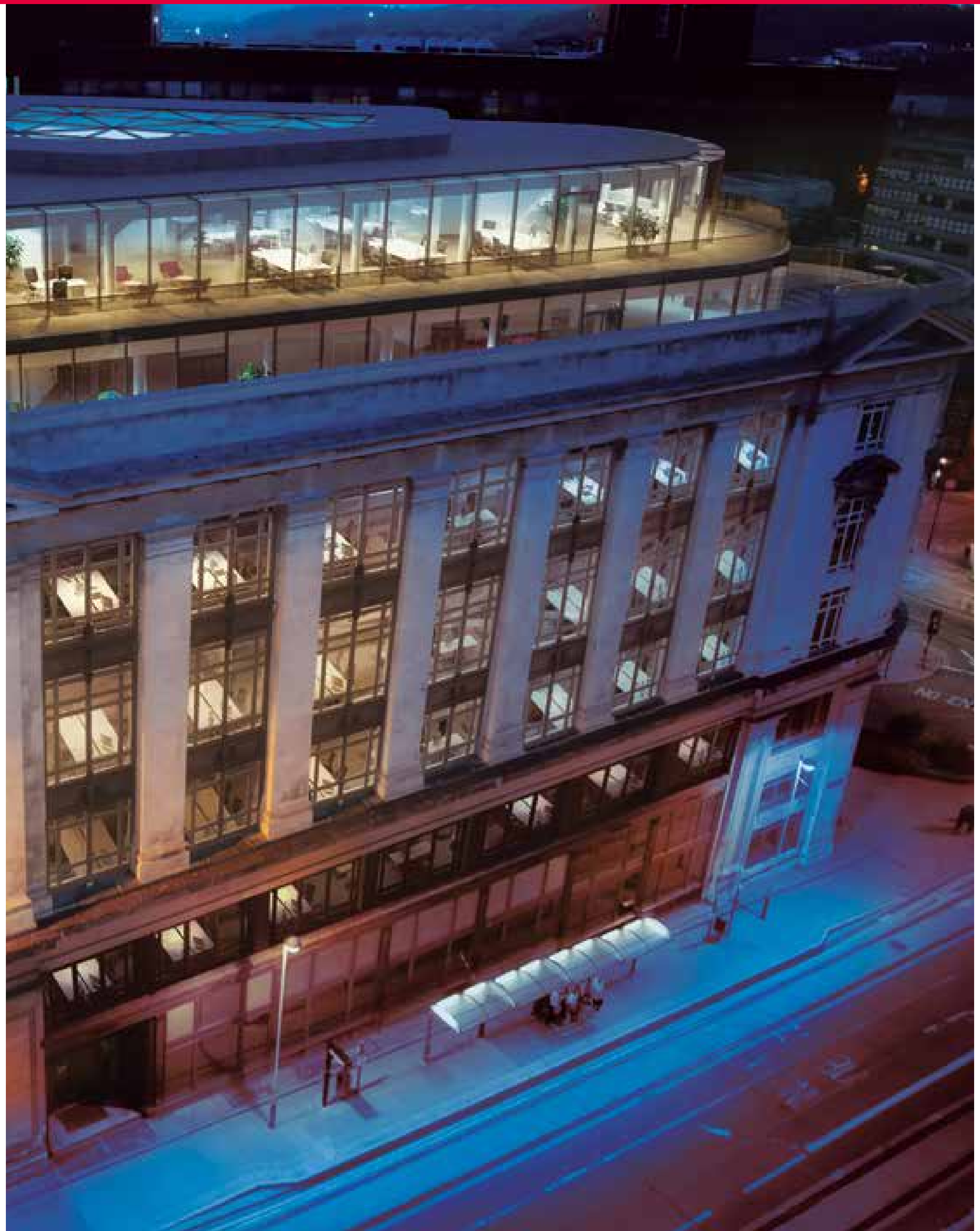
The total for 2016 however, does not yet include the 140,000 sq ft agreement to lease by HSBC. The bank is to anchor the first phase of Sheffield's new £480m Retail Quarter with completion due in spring 2019. The deal masks a more subdued letting market in 2016.

Aside from the HSBC deal, the largest occupier deal in 2016 was Arup taking 16,000 sq ft at 3 St Pauls Place. The building is part of the £130m Heart of the City project. The ten-storey speculative, office development was the first speculative build to complete post the recession. Another notable deal was the 9,500 sq ft letting to leisure and gaming company Rank Group at Navigation House. The move is a relocation of operations from London.

Occupiers from the TMT sector represented 23% of total take-up. The most notable deal from a tech occupier was the 7,840 sq ft letting to Zoo Digital at City Gate. The broadcasting support firm will move from Furnival Tower on Furnival Gate.

Grade A availability fell to just 175,000 sq ft by year-end 2016, the lowest level on record for the city. This total is 39% below the long-term average. Around 161,000 sq ft of office space is due for delivery in the coming 12 months, the majority of which is due in the third quarter.

In 2016, prime headline rents were unchanged at £23.00 per sq ft. We anticipate prime rents will increase to £24.00 per sq ft by year-end 2017.



STEEL CITY HOUSE, SHEFFIELD

INVESTMENT MARKET

With deal numbers up, office investment in 2016 increased to the highest total since 2010. Yields remained at the lowest level since 2014, but continue to offer discount compared to other regional centres.

Total investment volumes increased four-fold in 2016 to reach £83m by year-end. Not only is the 2016 total 60% above the 10-year average, it also represents the highest level of office investment in Sheffield for six years. Importantly, deal number was sharply up year-on-year with ten investment transactions completed. This compares to just two in 2015.

The largest investment deal of 2016 was the acquisition of Vulcan House at the J2 Riverside Exchange by Spanish investor Trinova Real Estate. The purchase price of £30.9m reflected an initial yield of 6.78%, illustrative of the yield gap to other regional centres. The Home Office are the current occupants of the 119,000 sq ft office building with a lease running to 2028.

Notably, the Trinova acquisition was the largest transaction to complete since 2014 and was one of two sales over £10m during the year.

The sale of the Riverside East office building for £23.4m was the other, a deal, which reflected a net initial yield of 6.73%. Bought by 90 North Real Estate on behalf of Arzan Wealth and Sidra Capital, the 75,600 sq ft office building is let to UK law firm Irwin Mitchell until 2027.

With overseas buyers behind the two largest deals of the year, foreign investment accounted for the largest percentage of turnover, 82%. The £68 million spent is the highest level of overseas investment into Sheffield offices on record.

In terms of deal number however, UK investors were the most active accounting for five of the 10 deals completed. The largest transaction from a domestic buyer was the purchase of Derwent House by Pramerica Real Estate Investors on behalf of John Lewis Pension Fund for £8.7m.

Prime office yields held firm at 6.50% throughout 2016 representing the lowest level for two years. At this level, prime yields are 150 basis points above the market peak of 5.00% recorded in 2007.

FIGURE 1
Sheffield office take-up (sq ft)

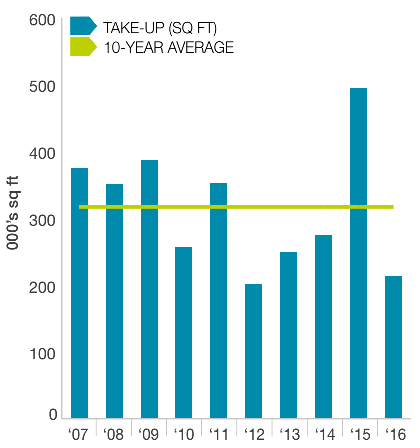
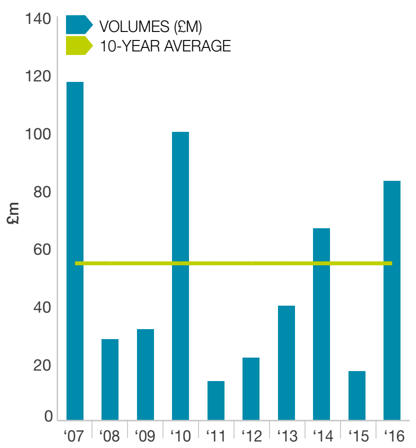


FIGURE 2
Sheffield investment volumes (£m)



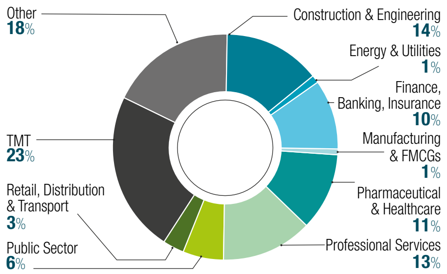
Source for all charts: Knight Frank Research, Property Data

OCCUPIER 2016

TAKE UP: **0.2m** Sq ft

GRADE A SUPPLY: **0.2m** Sq ft

TAKE UP BY SECTOR

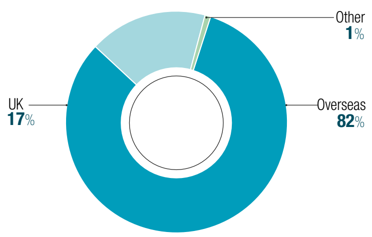


INVESTMENT 2016

VOLUMES: **£83m**

PRIME YIELD: **6.50%**

VOLUMES BY PURCHASER



KNIGHT FRANK VIEW

Although the Sheffield office market has suffered a recent period of reduced activity, there are still encouraging signs of future opportunities. In particular, the continual reduction of traditional office stock through student residential schemes continues to support speculative redevelopment.

With respect to active occupational requirements, although the traditional average deal size tends to be 3,000-5,000 sq ft and predominately from the public sector, there are a number of larger requirements in excess of 10,000 sq ft outstanding which span a diverse range of occupier backgrounds.

Undeniably, the 'Brexit effect' led to a greater level of market caution in 2016. As economic stability is reconfirmed in 2017, this may support an improvement in occupier activity, although the market will remain cautious due to the on-going EU negotiations.

DATA DASHBOARD

OCCUPIER

FIGURE 1
Combined city take-up (m sq ft)

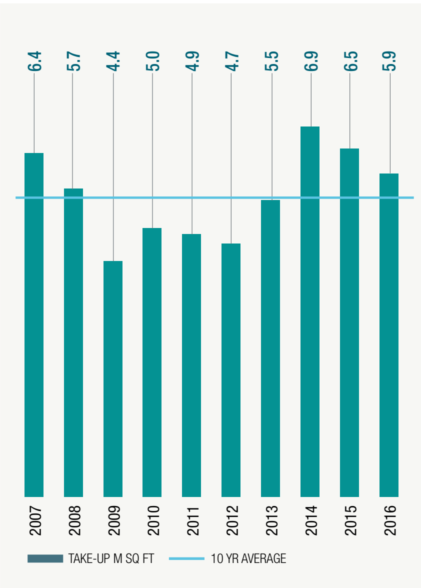


FIGURE 2
Take-up by sector

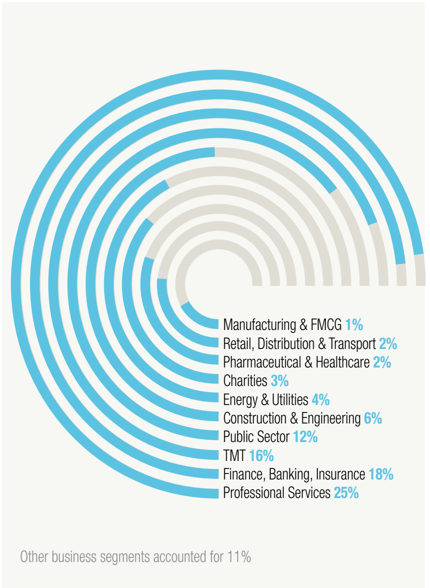
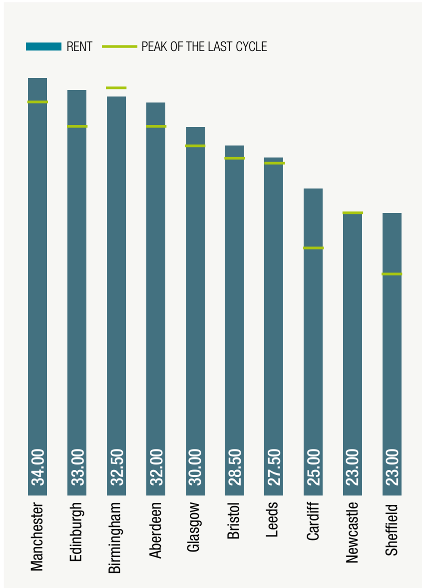


FIGURE 3
Prime rent £ per sq ft



INVESTMENT

FIGURE 4
Combined city investment volumes £bn

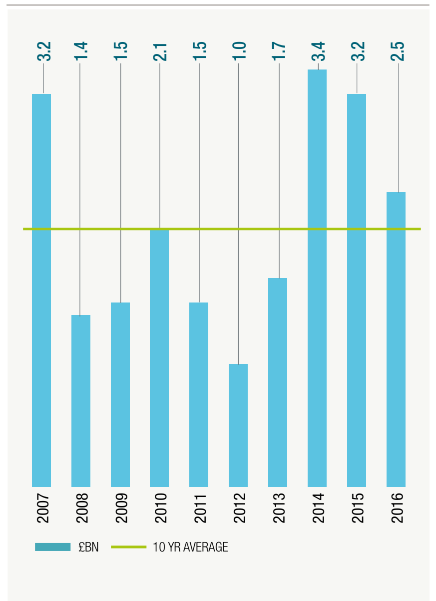


FIGURE 5
Purchaser type

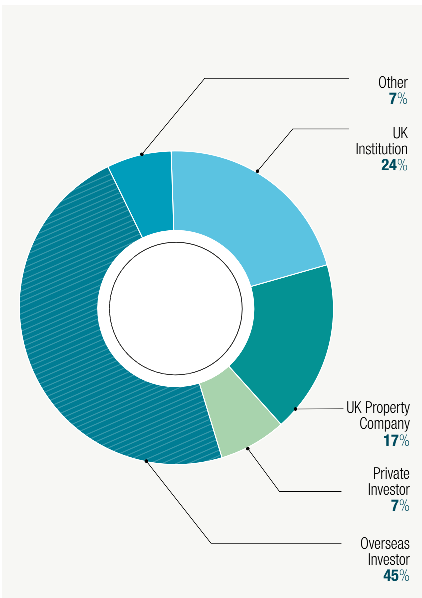
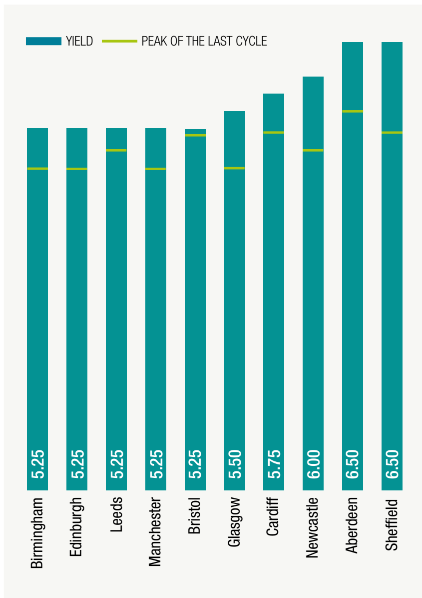


FIGURE 6
Prime yields %



		2014	2015	2016	COMPARISION % Y-on-Y	COMPARISION % Long-term average
TAKE-UP (sq ft)	Aberdeen	1,036,200	400,700	279,000	-30%	-51%
	Birmingham	713,500	970,500	692,700	-29%	-3%
	Bristol	836,900	490,800	782,900	60%	36%
	Cardiff	544,300	619,100	685,600	11%	39%
	Edinburgh	703,500	682,500	584,200	-14%	-1%
	Glasgow	666,700	568,500	689,000	21%	24%
	Leeds	549,100	680,100	435,800	-36%	-13%
	Manchester	1,352,700	1,318,300	1,310,800	-1%	24%
	Newcastle	182,700	260,200	220,000	-15%	-4%
	Sheffield	274,600	494,300	201,500	-59%	-36%
SUPPLY (Grade A sq ft)	Aberdeen	74,600	526,000	636,300	21%	208%
	Birmingham	205,500	127,500	127,500	0%	-60%
	Bristol	208,800	111,700	52,000	-54%	-77%
	Cardiff	100,000	87,800	185,400	111%	34%
	Edinburgh	325,400	273,100	267,000	-2%	-14%
	Glasgow	201,800	417,500	386,500	-7%	12%
	Leeds	250,000	250,000	441,000	76%	84%
	Manchester	290,000	211,100	220,000	4%	-26%
	Newcastle	201,200	234,000	173,300	-26%	-23%
	Sheffield	250,000	175,000	175,000	0%	-39%
INVESTMENT (£m)	Aberdeen	504	79	19	-76%	-88%
	Birmingham	556	796	395	-50%	0%
	Bristol	162	350	350	0%	79%
	Cardiff	80	239	107	-55%	12%
	Edinburgh	354	331	445	35%	80%
	Glasgow	176	347	109	-68%	-46%
	Leeds	201	205	175	-15%	1%
	Manchester	1,081	642	619	-4%	36%
	Newcastle	116	185	181	-2%	46%
	Sheffield	67	17	83	387%	60%

Source for all charts and data table: Knight Frank Research, Property Data

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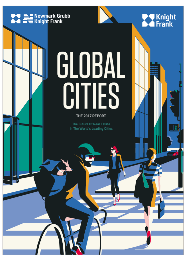

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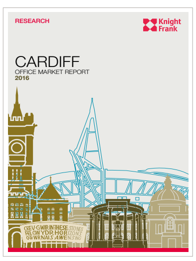

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