RESEARCH

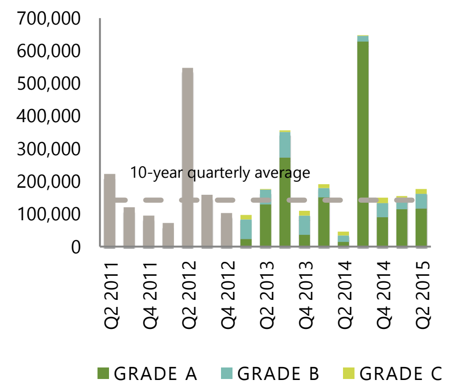
ABERDEEN OFFICES

MARKET UPDATE **H1 2015**

Occupier market

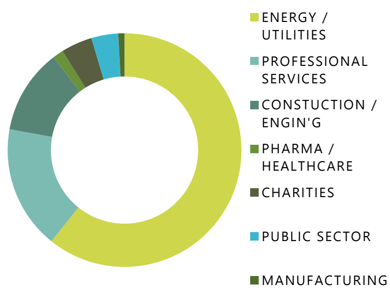
- Following the significant drop in oil prices which occurred in the final quarter of 2014, total take-up in H1 2015 (336,852 sq ft) was down 58% from H2 2014.
- H1 2015 take-up was bolstered by a number of major pre-lets, which included two deals at Prime Four Business Park - LR Senergy (100,000 sq ft) and Anderson Anderson Brown (45,000 sq ft). KCA Deutag also secured 70,000 sq ft at City South.
- Typically, the Oil & Gas sector continued to dominate the Aberdeen market, with take-up figures in Energy/Utilities (200,661sq ft) accounting for 60% of the total (Figure 2).
- While take-up in Q2 posted a 14 % increase on Q1, both quarters performed above the 10-year quarterly average (Figure 1).
- Despite the slide in oil price, speculative development in Aberdeen has continued. The Capitol office development (70,000 sq ft) is due for completion in Q1 2016 and Titan's Sliver Fin development totalling 132,000 sq ft has recently commenced. Muse's Marischal Square mixed use development, due for completion in Q2 2017, has also begun, and will deliver 177,000 sq ft of Grade A office accommodation over two buildings.
- Recently completed schemes include Annan House, EnQuest's new HQ facility totalling 121,599 sq ft, which was completed in June 2015. Knight Frank were instructed to market surplus space within the building over three floors extending to 43,000 sq ft. This space is now 'under offer' in its entirety to an undisclosed party.
- Other developments completed in H1 2015 include Stratus Building at ABZ (16,775 sq ft), Pavilion 4, City View Business Park (32,820 sq ft) and City South (Phase 1, 32,160 sq ft).
- Headline rental levels are expected to remain unchanged at £32 sq ft until the end of year.

FIGURE 1
Take-up by grade (sq ft)



Source: Knight Frank LLP

FIGURE 2
H1 2015 take-up by sector



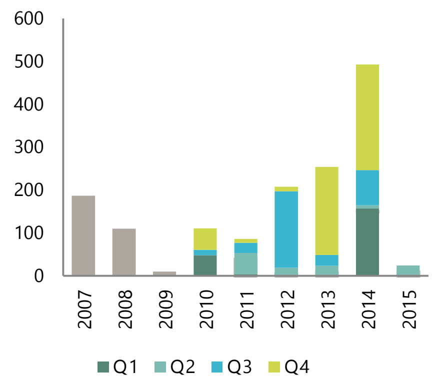
Source: Knight Frank LLP

Agent's view

The decline in oil prices has had a significant impact on Aberdeen's office market, resulting in a substantial decrease in demand. Many occupier requirements have been put 'on hold' while the market re-adjusts to the fall in oil price. With larger requirements now on a downward trend and a number of new office developments scheduled to come to fruition in the next 6-18 months, we expect to see an over-supply of office space in the market, which will likely manifest itself in a softening of deals being offered by developers/landlords. Activity in H2 2015 will be a good indicator of occupier sentiment, a year on from the fall in oil prices.

The Secretary of State for Communities and Local Government leased 12,000 sq ft at AB1 in June 2015. Knight Frank were joint letting agents.

FIGURE 3
Aberdeen offices investment turnover (£m)



Source: Knight Frank LLP, Property Data

In June 2015, a private investor acquired KCA Deutag HQ for £23.5m, reflecting a net-initial yield of 6.03%.

Investment market

- The volume of investment transactions deteriorated in H1 2015, following a significant fall in oil prices which occurred in the final quarter of 2014. The lack of activity in H1 highlighted the level of apprehension in the market, as investors opted to 'wait and see' before making any decisions.
- The last time Aberdeen saw such a lack of investment activity in the first six months of the year was in 2009, when the city faced the impact of the global financial crisis and the last oil price crash.
- However, the absence of investment stock in H1 2015 was a major factor in limiting investment volumes. It is understood that vendors of secondary assets were unwilling to put these up for sale, in fear of receiving little or no interest.
- Nevertheless, this should not discourage investors looking at Aberdeen, as well-let opportunities to strong covenants continue to attract good levels of interest at higher yields than most regional cities. The 20-year pre-let of the KCA Deutag HQ at City South for a yield of 6.03% illustrates this point. Furthermore, as the price of secondary assets continues to 'cool', it is expected more opportunities will open up in the market.
- Prime office yields softened in Q1 2015 to 6.25%*, in the wake of the fall in oil prices, and are forecast to remain unchanged until 2016. At present, this represents the highest yield since Q2 2013.
- With the current low price of oil, Aberdeen may struggle to reap the benefits of its oil-based economy unless the industry becomes more efficient.
- This view is widely shared by many analysts who believe that the best way to mitigate the risk to Aberdeen is for energy firms to become more efficient. This could not only reduce the cost of production, but it could also help bring some cautious investors back to the Aberdeen market.

* - Based on 10-year income

TABLE 1
Selected investment transactions in H1 2015

Date	Address	Purchaser / Vendor	Price	NIY
Jun 15	KCA Deutag HQ, City South Business Park, Portlethen	Private Investor / Dandara	£23.5m	6.03%

Source: Knight Frank LLP

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