RESEARCH

BIRMINGHAM OFFICES

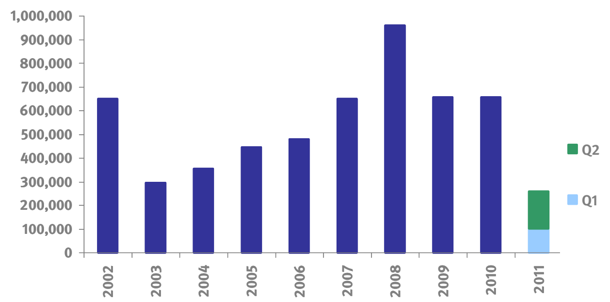
Market update Q2 2011

Knight Frank

Key highlights

- Birmingham city centre saw healthy take-up of 157,788 sq ft in Q2 2011, an increase of 55% on the previous quarter. However, the number of transactions was actually identical, with 26 deals taking place in both Q1 and Q2.
- Q2 saw four deals in excess of 10,000 sq ft, the largest of which was MOJ's 38,898 sq ft lease at The Axis Building. Grade A space accounted for just over one third of Q2 take-up, with the largest Grade A deal comprising Deutsche Bank's 27,604 sq ft lease of the 4th floor at Baskerville House.
- Prime headline rents held steady at £28.50 per sq ft in Q2 2011, unchanged since Q3 2010. Net effective rents also held firm in Q2 at £20.50 per sq ft, following an increase in Q1 from £19.00 per sq ft.

City centre take-up (sq ft)

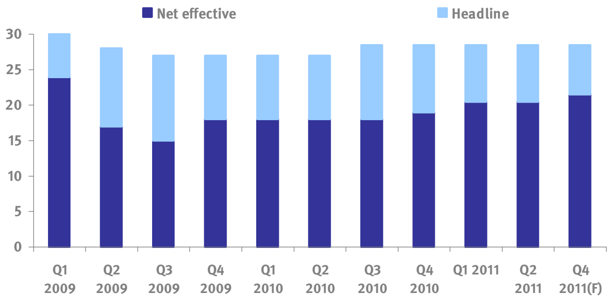


Source: Knight Frank Research / BOMF

Office gossip

- Recent market activity points to a strengthening of take-up into the latter half of 2011. The Law Society is expected to agree terms on 60,000 sq ft at 2 Colmore Square, while the CCRC and RSM Tenon are each expected to agree to circa 10,000 sq ft at St Phillips Plaza and Rutland House respectively.
- Reflecting improving occupier confidence in the city, active demand increased by a third during Q2 to stand at c.390,000 sq ft. One notable requirement is from Chartis Group, who recently short-listed a number of preferred options for Grade A space in the city centre.
- Q2 marked the return of development to the Birmingham office market, with Hines commencing on site at Two Snowhill. The 305,000 sq ft scheme is set for completion in mid-2013, with Wragge and Co. having already pre-let 185,000 sq ft in 2008.

Prime headline & net effective rents (£ sq ft)

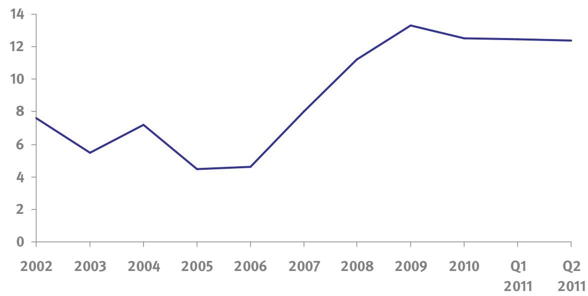


Source: Knight Frank Research

Looking ahead

- While 800,000 sq ft of Grade A space is available, we expect this to be absorbed over the next two to three years. Indeed, the recent commencement of new development in the city is testament to developer confidence in Birmingham's occupier market over the medium-term.
- While headline rents are set to remain stable, incentives on prime stock will harden steadily over the remainder of 2011 and into 2012 as available Grade A stock is gradually eroded.
- As a consequence of rising net effective rents on Grade A space, we anticipate a degree of rental growth to occur for good quality Grade B accommodation in 12 to 18 months.

Vacancy rate (%)



Source: Knight Frank Research / BOMF

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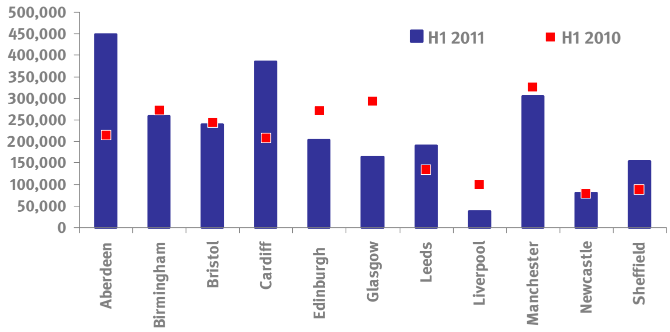
UK REGIONAL OFFICES ROUND-UP

Q2 2011

Occupier demand

- Across the eleven markets combined, total take-up for the first half of 2011 stands 11% higher than H1 2011. However, if Admiral Insurance's 200,000 sq ft pre-let in Cardiff is excluded, take-up is almost identical.
- H1 2011 take-up in Birmingham, Bristol, Manchester and Newcastle was remarkably consistent with the equivalent period last year, suggesting occupier sentiment has remained relatively robust.
- Buoyancy of the North Sea oil sector continues to fuel strong demand in Aberdeen, with H1 2011 take-up more than twice that seen in H1 2010. In contrast, Edinburgh and Glasgow have seen less transactional activity on last year, while activity remains extremely subdued in Liverpool.

City centre take-up, H1 2011 vs H1 2010 (sq ft)

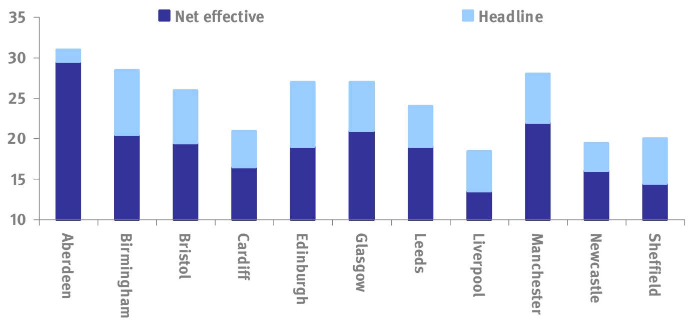


Source: Knight Frank Research

Supply and rents

- The commencement of Two Snowhill in Birmingham is the first major speculative development to progress across the 11 cities in almost a year. However, most of Hines' 305,000 sq ft scheme is pre-let, and this is likely to provide the only means through which large developments will move forward in these markets over the next 12 months.
- Supply continues to ebb away in the absence of new development completions. At the end of Q2 2011, Grade A supply across the 11 cities combined was down 25% on Q2 2010, with the largest falls seen in Aberdeen (-89%), Edinburgh (-47%) and Sheffield (-35%).
- Headline rents slipped in Liverpool and Newcastle to £18.50 and £19.50 in Q2. However, more generally, incentive levels are either hardening or expected to harden across the regional centres, in reflection of this steady erosion of Grade A supply.

Q2 2011 Prime headline & net effective rents (£ sq ft)



Source: Knight Frank Research

Investment market

- Investors' aversion to secondary assets and a shortage of available prime stock has stymied activity in the first half of 2011. Latest figures from Property Data reveal that H1 2011 turnover was c.£716m outside London and the South East, down 52% on H1 2010.
- Investment demand is becoming increasingly polarised according to perceived strengths of each occupier market. When prime office stock becomes available in Birmingham, Manchester and Bristol, aggressive bidding is ensuing. Elsewhere, however, investors are more cautious and need to see clear value. Consequently, prime yields softened by 25bps in Liverpool, Leeds and Sheffield in Q2.
- The secondary investment market remains problematic. Yields are likely to soften given an anticipated increase of stock to the market as lenders become more willing to offload properties and crystallise their losses.

Prime office yields

	2010		2011		Yield sentiment
	Q3	Q4	Q1	Q2	
Aberdeen	6.00%	6.00%	6.00%	**6.00%**	◄ ►
Birmingham	5.75%	5.75%	5.75%	**5.75%**	◄ ►
Bristol	6.00%	6.00%	6.00%	**6.00%**	◄ ►
Cardiff	6.25%	6.25%	6.25%	**6.25%**	◄ ►
Edinburgh	6.00%	6.00%	6.00%	**6.00%**	◄ ►
Glasgow	6.00%	6.00%	6.00%	**6.00%**	◄ ►
Leeds	6.00%	6.00%	6.00%	**6.25%**	◄ ►
Liverpool	6.50%	6.50%	6.50%	**6.75%**	◄ ►
Manchester	6.00%	6.00%	6.00%	**6.00%**	◄ ►
Newcastle	6.50%	6.50%	6.50%	**6.50%**	◄ ►
Sheffield	6.50%	6.50%	6.50%	**6.75%**	◄ ►