

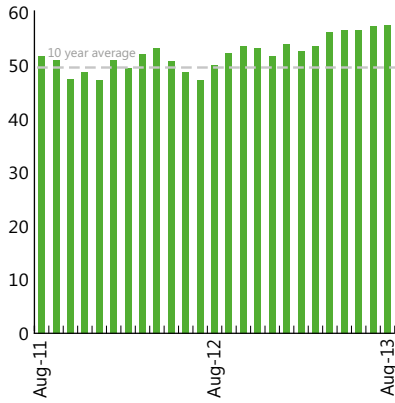


2013/14
CARDIFF
Office market

HIGHLIGHTS

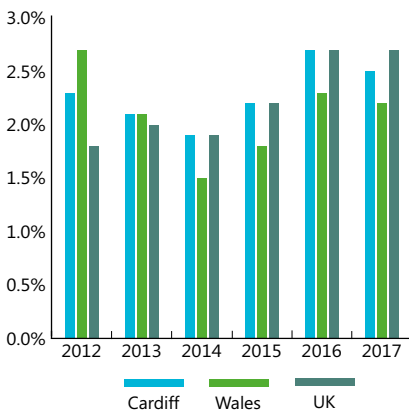
- Business confidence in Wales continues to rise. Financial & Business Services (F&BS) employment growth in Cardiff is forecast to exceed both Wales and UK growth between 2013 and 2017.
- Headline rents have been firmly established at £22.00 per sq ft in Cardiff Bay and £21.00 per sq ft in the city centre as at Q2 2013. 'Net effective' rents are expected to continue to improve for prime office stock across the city as availability remains limited.
- Cardiff is set to benefit from a range of government measures which should act as key drivers of the Cardiff office market and the wider regional economy.
- There are a number of active requirements for new office space and a potentially significant supply of new, speculatively constructed buildings which could be brought to the market within the next 2 to 3 years.
- The strength of investor appetite is still focussed on long-let, good quality office stock in established locations. However, with a lack of available prime stock, investment demand for good quality secondary and shorter income prime stock continues to grow.

Figure 1
Wales PMI Business Activity Index



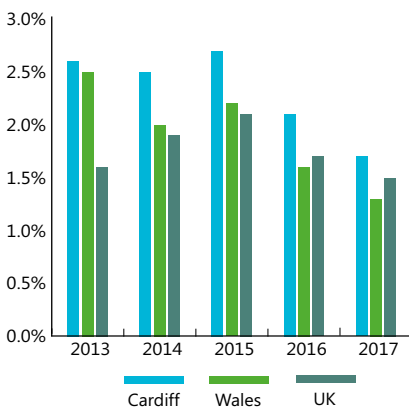
Source: Markit Economics

Figure 2
F&BS GVA growth forecast



Source: Experian

Figure 3
F&BS employment growth



Source: Experian

ECONOMIC OVERVIEW

The second estimate of Q2 GDP was revised upwards from 0.7%, compared to 0.2% growth in Q1, and minus 0.2% in Q4 2012.

Recently the OECD has revised up its forecast for full year UK growth to 1.5% in 2013, compared to its previous prediction of 0.8%.

The PMI Index for business activity showed a resurgence of business activity outside of London in August and this is the 12th month in a row that Wales had a reading of over the 50 mark, indicating growth.

Turning to Cardiff, Financial & Business Services (F&BS) GVA (Gross Value Added) output growth in the City was estimated by Experian, an economics and data consultancy, at 2.3% in 2012 compared to 1.8% in the UK. Looking ahead, Cardiff is forecast by Experian to see average annual F&BS output growth of 2.3% in the next five year period, compared with the Welsh rate of 2.0% p.a.

On F&BS employment, Experian believes Cardiff has significantly outperformed Wales and the UK as a whole in 2012, recording a striking 4.4% growth rate.



THE UK ECONOMY RETURNED TO GROWTH THIS YEAR, AND APPEARS TO BE GAINING MOMENTUM.



CARDIFF OCCUPATIONAL MARKET

After a weak first quarter, Q2 2013 has seen a pick-up in occupier take up, reflecting the improved economic environment.

Second quarter take-up was 84,216 sq ft – 86% up on the previous quarter and in line with the take-up level in Q2 2012. This brings the half year total to 129,369 sq ft. This was thanks to activity by media and professional firms and education, reflecting the growing importance of knowledge industries in most UK cities.

Headline rents have been firmly established at £22.00 per sq ft in Cardiff Bay and £21.00 per sq ft in the city centre as at Q2 2013. However, we expect net effective rents to continue to improve for prime product as availability in the city centre remains very limited.

The most recent significant lettings include ITV Broadcasting’s lease of 10,819 sq ft and the Welsh Government’s Life Science Hub (12,489 sq ft), both at 3 Assembly Square, Cardiff Waterside.

Aecom completed a 7,700 sq ft sub-lease from Eversheds at 1 Callaghan Square and Zurich acquired 7,333 sq ft at 3 Callaghan Square at the start of the year as part of its wider relocation.

The remaining space at 18 Park Place has been leased to Bemaco Steel and Alder King. The 10,604 sq ft building is now fully let, following a comprehensive ‘Grade A’ refurbishment that was completed in January 2013.

Named and active requirements currently in the market total more than 350,000 sq ft including the BBC, Legal & General, Geldards, Morgan Cole, The AA, HSBC and Finance Wales. If these requirements result in relocations over the next few years, it can be anticipated that there will be a number of older, but good quality, buildings coming back onto the market during this timescale.

In terms of current supply, ‘Grade A’ stock remains in very short supply with less than 20,000 sq ft available in the city centre until completion of Number 1 Capital Quarter (80,000 sq ft) and only 40,000 sq ft in the Bay.

Recent trends

Cardiff is a successful centre for financial and business services, with a large number of global financial services companies, including Admiral Insurance, Zurich, Legal and General, Conduit BPO, Deloitte Global Risk Management and ING Direct, reflecting its focus on ‘competitive knowledge’.

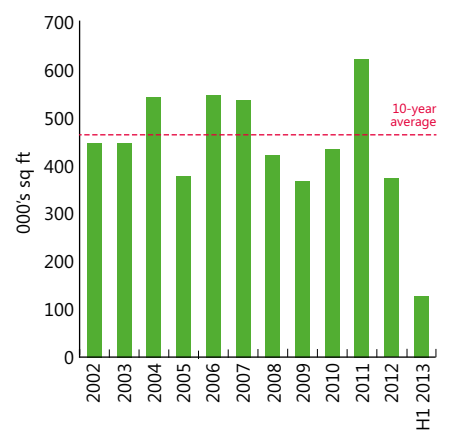
In addition, customer comparison sites Go Compare and Confused.com have headquarters in Cardiff and Newport. It is also home to one of the largest concentrations of media employment outside of London. There is now a strong collection of around 100 biosciences related companies and organisations operating in and around Cardiff.



Leasing transactions				
Address	Tenant	Size (sq ft)	Headline rent (£ per sq ft)	Date
3 Assembly Square	ITV Broadcasting	10,819	22.00	August 2013
3 Assembly Square	Life Science Hub (Welsh Government)	12,489	22.00	July 2013
1 Callaghan Square	Aecom	7,770	19.00	July 2013
Hodge House	Hugh James	19,383	15.50	March 2013
18 Park House	Multiple tenants	10,604	19.00 - 20.00	Q1/Q2 2013
3 Callaghan Square	Zurich Insurance plc	7,333	21.00	December 2012

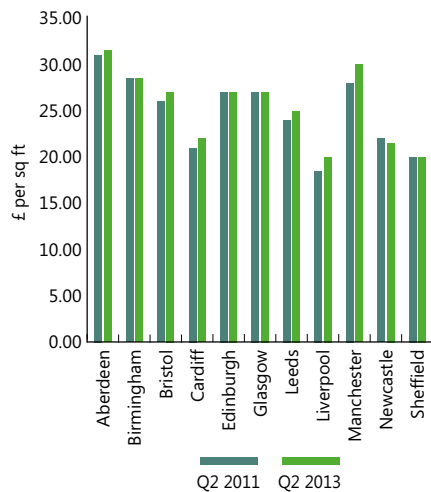
Source: Knight Frank

Figure 4
Cardiff city centre take-up



Source: Experian

Figure 5
Regional office prime headline rents



Source: Experian

Creative industries

Cardiff's creative offer has been strengthened with the opening of Roath Lock, the new BBC Wales drama studios in Cardiff Bay. The 175,000 sq ft studios are the permanent home to four flagship BBC dramas: Casualty, Pobol y Cwm, Doctor Who and Wizards v Aliens, as well as new productions in the future. With ITV's move to 3 Assembly Square, both major broadcasters now have a presence in Cardiff Bay.

In addition, BBC Wales is known to be considering the relocation of its Broadcasting House at Llandaff to a new, purpose built facility of up to 140,000 sq ft. A decision is likely to be made during 2014 for delivery in 2016.

Welsh Government's 32,000 sq ft Creative Industries centre is currently under construction on a prime waterfront site at Porth Teigr. Due for completion early in 2014, the building will provide a collaborative environment for creative businesses of all sizes and will further strengthen Cardiff Bay as the focal point for media related occupiers.

Life sciences

Cardiff has already benefited from a broad range of successful life sciences companies choosing to locate in Cardiff, including BBInternational, GE Healthcare, Molecular Light Technology, Q Chip and Concateno Trichotech.



In July, the Welsh Life Sciences Hub completed its lease at 3 Assembly Square. Welsh Government is supporting the establishment of the Hub demonstrating its commitment to this sector. The Hub will also accommodate the team from Arthurian Life Sciences Ltd managing the £100million Wales Life Science Investment Fund.



CARDIFF DEVELOPMENT

Cardiff is the main economic driver of the Welsh economy, reflecting its position as the capital of Wales. Indeed, Cardiff is set to benefit from a series of government measures for promoting business growth.

This includes investment in both the airport at Rhoose and the region's railway network, which will enhance communications, and support the creation of the Cardiff Central Enterprise Zone. Together they should act as key drivers of the Cardiff office market and wider economy of the city region.

Recently, Western Gateway, a consortium of academics and businessmen, submitted plans to the UK Airports Commission regarding the future of Cardiff Airport. With the infrastructure already available, the plan is for Cardiff Airport to become the long-haul airport for the south west of the UK. Also rail upgrades are expected to bring more passengers from the south of England into the crucial two-hour travel time to the airport.

In addition to the airport infrastructure, the upgrade and electrification of the existing railway will reduce Cardiff to London journey times. This will play an important role in attracting further investment and in stimulating and supporting the growth of local businesses. The reduced journey time will encourage tourism and bring more national and international events and leading sporting events.

Welsh Government has announced plans to prioritise delivery of a new road (the Eastern Bay Link) to improve connections into the city from the east as well as with the M4 motorway. This project will improve access to the Cardiff Central Enterprise Zone and Cardiff Bay, as well as enhance connectivity within the wider city region. Work also continues on developing plans for a region wide Metro system which would include better connectivity between the centre and Bay as an early phase.

The Business Minister announced the plan to create the Cardiff Central Enterprise Zone in 2012. This aims to enhance a new Central Business District within the heart of the city

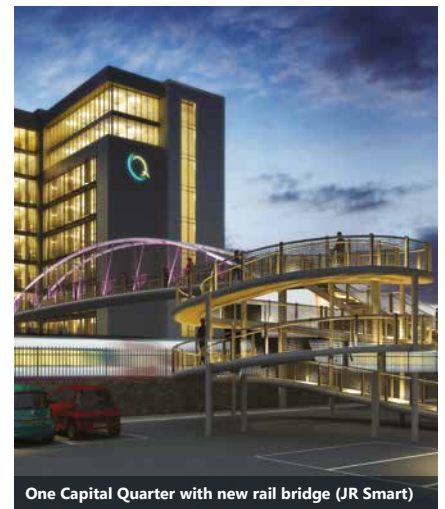
centre to provide a substantial amount of new 'Grade A' office space, financial support and infrastructure which will capitalise on Cardiff's existing strengths and predicted growth in financial and business services. The zone is aimed at attracting inward investment from the financial & professional services sector.

In January, Welsh Government acquired from MEPC the south side of Callaghan Square, within the enterprise zone, with the intention of ultimately developing up to 500,000 sq ft of office space. It has plans to directly deliver the first phase of 90,000 sq ft within the next 18 months on a speculative basis. It has also purchased the freehold of One Capital Quarter, also in the enterprise zone, from JR Smart to ensure that 80,000 sq ft of new 'Grade A' accommodation can be made available almost immediately.

At a local level, Cardiff Council has revived plans to procure a Convention Centre, as well as an Arena and appear to be progressing plans to assist in a comprehensive mixed use redevelopment around Central Station in consultation with Network Rail.

In conclusion, the supply of new 'Grade A' office stock is poised to increase dramatically, with potentially 310,000 sq ft of new development planned to be completed on a speculative basis by the middle of 2015, including Number 2 Capital Quarter; the first phase of Callaghan Square; and a planned new office building known as One Capital Square on the cleared site at Wood Street, adjacent to Central Train Station, which was acquired by Rightacres Ltd in March.

There are also a number of other significant sites in and around the city centre and Cardiff Bay with existing planning consents which could be brought forward for development quickly.



One Capital Quarter with new rail bridge (JR Smart)



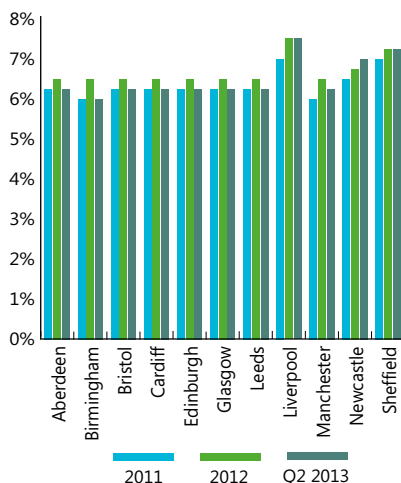
Proposed offices at Callaghan Square (Welsh Government)



Proposed offices at One Capital Square, Wood Street (Rightacres Ltd)



Figure 6
Regional office prime yields



Source: Knight Frank

CARDIFF INVESTMENT TRENDS

In recent years the difficult trading environment has encouraged investors to focus on the safety of major population centres, particularly those which boast blue chip firms as local employers.

The result has been a growing shortage of genuinely prime assets, which is encouraging UK and international investors to look more widely in search of good quality assets.

There have been no prime office sales in Cardiff in the last 12 months due to a lack of available product, however, Cordea Savills acquired Helmont House in Cardiff in May 2013 from Rightacres Ltd for £23.15m, reflecting a NIY of 7.87%, although this mixed-use investment is 50% let to Premier Inn, on a lease with 23 years unexpired and RPI linked reviews.

The last sale of a prime office building was the sale of 1 Callaghan Square by Cordea Savills in February 2012. The offices, let to Eversheds LLP with 10.3 years unexpired, sold for £25.50 million reflecting a NIY of 6.50%.

These transactions demonstrate that investor appetite has focussed on long-let, good quality office stock in established locations. With a lack of available prime stock, investment demand for established, good quality secondary and shorter income prime stock is returning.

As investor demand continues to improve we expect transaction volumes in the regional markets to increase as investors

are priced out of the Central London and South East markets. We also expect the range of buyers into the regions to expand from the traditional UK based investors and institutions to include overseas investors. In fact, many of these investors have already started to look to the regions for value, with Chinese and American investors buying in Manchester and Birmingham respectively.

Based on London's recovery pattern, we believe cities with a track record for technology and media industries, and a strong base of professional services, will be best positioned in the new cycle. This would favour Bristol, Birmingham, Leeds and Manchester, as well as Cardiff.

Market sentiment suggests prime yields will improve over the coming months and we are already starting to see evidence of this appearing in other regional markets. We await the evidence to confirm this in Cardiff, but our view is that prime office yields for Cardiff have moved into 6.25%. Yields on good secondary stock should also start to improve as demand increases, and prime product remains a rare commodity, although the outlook for tertiary stock will remain cautious for the rest of 2013 and into 2014.

Investment transactions

Building	Price (£m)	Yield (%)	Unexpired lease term (years)	Tenant	Purchaser	Vendor	Date
Toronto Square, Toronto Street, Leeds	29.00	7.00	4.30	Multi-let	M&G Real Estate (Knight Frank advised)	Highcross	Aug 2013
84 Colmore Row, Birmingham	11.00	5.82	11.50	Mills & Reeve	Private investors (Knight Frank advised)	Bank of Ireland	Aug 2013
1 Brindley Place, Birmingham	30.00	6.29	11.00	Deutsche Bank	Trinova Real Estate	British Airways Pension Fund	July 2013
Barhaus, Manchester	16.25	7.60	5.00	Multi let	Orchard Street	Blackrock	May 2013
Admiral Headquarters, Cardiff	58.60	5.85	25.00	Admiral	Union Investments	Stoford Developments (Knight Frank advised)	Mar 2012
1 Callaghan Square, Cardiff	25.50	6.50	10.3	Eversheds LLP	Capital Trust (Knight Frank advised)	Cordea Savills	Feb 2012
5 Callaghan Square, Cardiff	14.27	7.00	8.90	Multi-let	Credit Suisse	MEPC (Knight Frank advised)	Oct 2011

Source: Knight Frank

KNIGHT FRANK VIEW

- With improving economic conditions, we anticipate that demand from occupiers in Cardiff will continue to increase, beyond the 350,000 sq ft of active requirements already in the market.
- There is potentially a new supply of 'Grade A' office space, which could be on the market within the next two years, totalling 310,000 sq ft in the city centre alone.
- In the short term, due to the lack of available 'Grade A' space, we expect to see a reduction of incentives offered to tenants, which will improve 'net effective' rental levels, which should lead to an increase in 'headline' rents in 2014/15.
- As investor demand increases, and prime office investments remain a rare commodity, both prime and good secondary office yields will continue to move in.
- Coupled with an improving economic outlook and an increasing interest from investors in regional office markets, landlords with second-hand space should consider the viability of undertaking higher quality refurbishment in order to take advantage of these positive indicators.
- Irrespective of your views on direct public sector intervention in the commercial markets, it appears that recent activity by both central and local government will act as a catalyst to a more active period in the Cardiff office market, but to what end result remains to be seen.



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