RESEARCH

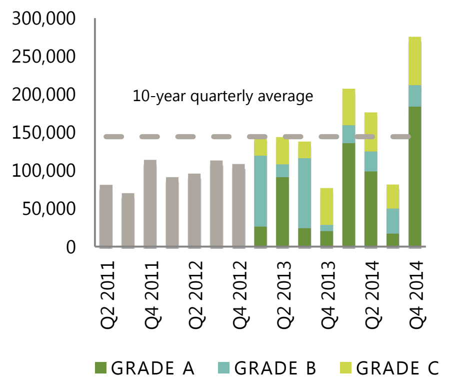
EDINBURGH OFFICES

MARKET UPDATE H2 2014

Occupier market

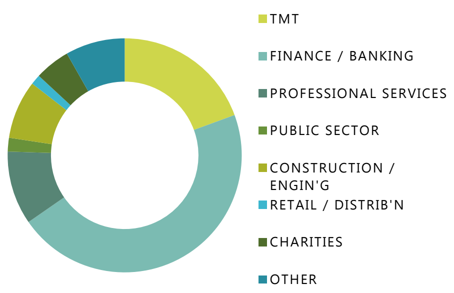
- In what can be described as the city's strongest performance since 2004, take-up in 2014 reached a very impressive 740,000 sq ft, providing further signs that occupier activity is back to pre-recession levels.
- Q4 in particular witnessed a surge in take-up activity, reaching in excess of 275,000 sq ft, far outstripping the 10-year quarterly average and up by an extraordinary 260% on Q4 2013.
- While take-up failed to match H1, it nevertheless posted a 36% increase on H2 2013, despite the impact of the referendum which caused the market to slow in Q3.
- Take-up was largely driven by Financial Services (163,000 sq ft) and Technology Media and Telecommunications (TMT, 68,000 sq ft), which together accounted for 65% of H2's total.
- Noteworthy deals in H2 included the pre-let of 108,000 sq ft at 6 St Andrews Square to Standard Life Investments, the largest pre-let since 2004. Elsewhere, other deals involving Grade A space saw Dell lease 14,000 sq ft at Tanfield, whilst FNZ expanded its presence at the same location by 12,000 sq ft.
- Currently, around 325,000 sq ft of Grade A is space available, down 28% on Q4 2013.
- The need for new supply is expected to become more acute given the lack of forthcoming developments this year, with the earliest scheduled to be completed by Q3 2016.
- While a contraction of supply may affect take-up activity, it is likely to lead to positive rental growth, with rents forecast to rise to £29 per sq ft by the end of 2015.

FIGURE 1
City centre take-up by grade (sq ft)



Source: Knight Frank LLP

FIGURE 2
H2 2014 take-up by sector



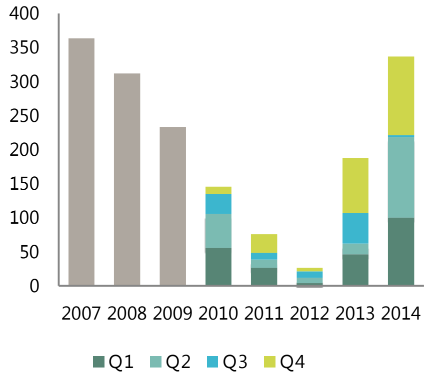
Source: Knight Frank LLP

Agent's view

Despite concerns surrounding the Scottish referendum, 2014 recorded the strongest levels of take-up in a decade, such was the buoyancy of the market. The falling supply of Grade A office space is likely to continue to dominate the market with no new developments scheduled for completion before late 2016, placing upwards pressure on rental levels. The pendulum is swinging back in favour of landlords, which is expected to result in more lease event driven demand translating in to new lettings. As incentives continue to harden, we will see an improvement in net effectives in 2015.

3 Lochside Way, Edinburgh Park, recently refurbished by Aston Property Ventures

FIGURE 3
Edinburgh offices investment turnover (£m)



Source: Knight Frank LLP, Property Data

In Q4, Port Hamilton was purchased for £105.5m by HSBC (HAIL).

Investment market

- 2014 saw investment activity reach its highest level since 2007, due to the biggest office deal ever in the city which involved HSBC Alternative Investment Ltd (HAIL) purchase of Port Hamilton for £105m, at a net initial yield of 5.1%.
- The range of bidders involved in the Port Hamilton deal suggest that for the right type of stock and with the necessary security of income, foreign investors will consider opportunities in Edinburgh and other major Scottish cities.
- Edinburgh's investment market experienced a significant degree of volatility during the final six months of the year. Q3 recorded the lowest investment volumes ever (£2.8m), as investors delayed making purchases in the run-up to the Scottish referendum. Meanwhile volumes in Q4 reached £115m, mirroring the figures achieved in Q2 2014 (Figure 3).
- Prime Office yields remained unchanged at 5.75% throughout the year.
- While the uncertainty surrounding the referendum has now dissipated, it remains to be seen whether Edinburgh and other major cities will be affected by the sharp fall in oil prices.

TABLE 1
Selected investment transactions in H2 2014

Date	Address	Purchaser / Vendor	Price	NIY
Dec 14	Port Hamilton	HSBC (HAIL) / Aberdeen Asset Management	£105.5m	5.1%
Dec 14	Castle Terrace, 1&2	Knight Property Group / DTZ Investors	£5.61m	6.68%
Dec 14	George Street, 110	Knight Property Group/ Danobe Securities LTD	£2.6m	6.75%
Oct 14	Quality Street, 3	Cairnmore LTD/ Nationwide Building Society	£1.23m	13.32%
Sep 14	North Castle Street, 46	Sundial Properties / Capital Fiduciary Group	£2.05m	7.48%

Source: Knight Frank LLP

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