BNP PARIBAS
REAL ESTATE

Real Estate for a changing world

SOUTH EAST OFFICES REVIEW
Q1 2018

Leasing

- Take-up for Q1 2018 reached 627,962 sq ft, 12.9% down on the same period last year, but just 6.8% down on the 10-year quarterly average for Q1.
- In Q1 2018 the majority of leases agreed (61.8%) fell within the sub-10 years term-certain category, highlighting occupiers' increasing desire for flexibility.
- Following a peak in speculative deliveries in 2017, speculative development is scheduled to fall back over 2018-2019, with 923,500 sq ft currently underway across 14 schemes.

Investment

- South East office investment reached £559m in Q1 2018, 22.3% up on the same period last year and 73.0% up on the 10-year Q1 average (2008-2017).
- Of this, Hammersmith accounted for 56.5% of the South East total across five transactions.
- Following some yield compression over H2 2017, prime yields in the South East remain at 5.00% at Q1 2018, relative to 4.00% in the City and 3.50% in the West End.

Q1 2018 take-up figures reached

0.63M (SQ FT)

61.8% of deals agreed in Q1 2018 had lease terms of sub-10 years term-certain

61.8%

Current speculative developments expected to complete over 2018-2019 total

0.92M (SQ FT)

Q1 2018 South East office investment volumes reached

£559M

Hammersmith alone accounted for 56.5% of total investment across five transactions

56.5%

Q1 2018 prime yields in the South East remain at

5.00%

CONTACTS

Edward Smith
Head of National Markets
edward.smith@realestate.bnpparibas
+44 (0)20 7318 5136

Hugh White
Head of Office Investment
hugh.white@realestate.bnpparibas
+44 (0)20 7338 4415

Katie Taylor
Senior Research Analyst
katie.taylor@realestate.bnpparibas
+44 (0)20 7338 4346

LEASING

Take-up for Q1 2018 reached 627,962 sq ft, 12.9% down on the same period last year, but just 6.8% down on the 10-year quarterly average for Q1.

The largest deal of the quarter comprised Black & Decker's lease of 48,000 sq ft at 270 Bath Road, Slough. However, as was the case over 2017, the smaller size bands continued to dominate the demand profile, with 63.6% of overall take-up coming from lettings within the 5,000 – 20,000 sq ft size band.

With demand increasingly focussed within the smaller size bands, lease lengths are also shortening. In Q1 2018 the majority of leases agreed (61.8%) fell within the sub-10 years term-certain category. Both these trends highlight occupiers' increasing desire for flexibility and optimisation of their occupied space.

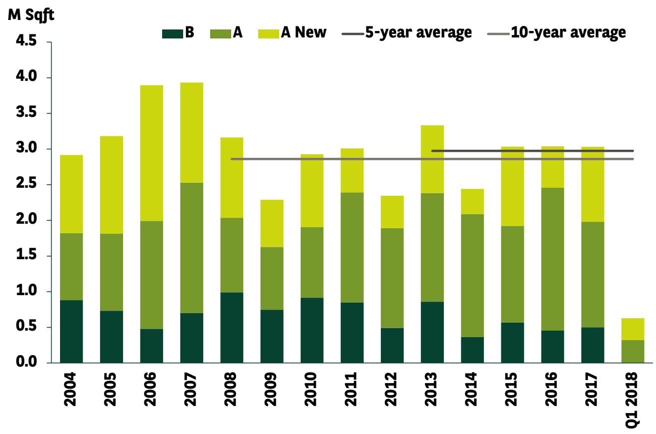
Whilst demand has fallen back slightly on previous quarters, there has been a concerted move towards higher quality space with all demand over Q1 2018 targeting Grade A and new prime schemes.

This increased competition for limited, high-quality stock has helped drive further prime rental growth over Q1 2018. Prime rental increases were recorded in Maidenhead, Reading and Basingstoke where prime rents rose to £39.00 psf (+2.6%), £38.00 psf (+3.4%) and £25.75 psf (+5.1%) respectively.

Following a peak in speculative deliveries in 2017, with completions reaching 1.79m sq ft across 18 schemes, speculative development is scheduled to fall back over 2018-2019, with 923,500 sq ft currently underway across 14 schemes. Q1 2018 recorded only one speculative completion: Aviva Investors' Victoria Gate in Woking totalling 63,000 sq ft. With speculative development levels declining, further upwards pressure will likely start building on prime rental levels in a number of South East towns over the course of the year.

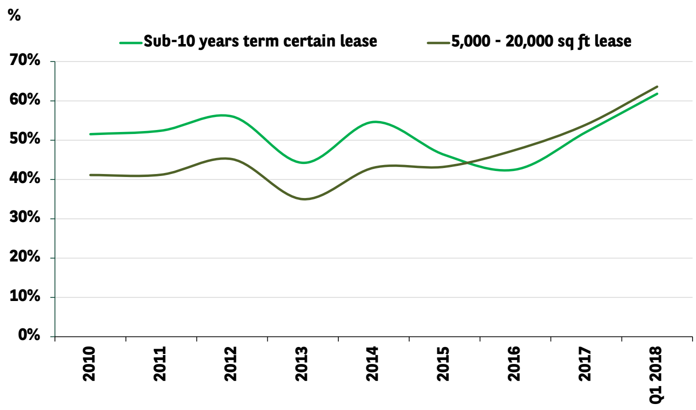
Looking ahead, identified demand levels have risen to 4.6m sq ft, up from 4.25m sq ft at Q4 2017. This, coupled with the c. 600,000 sq ft currently under offer, suggests we are in line for a stronger Q2 and overall positive outlook for the remainder of 2018.

SOUTH EAST ANNUAL TAKE-UP BY GRADE (MILLION SQ FT)



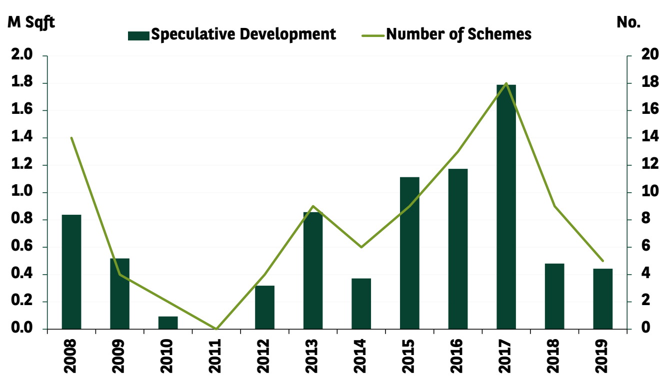
Source: BNPPRE

SOUTH EAST TERM-CERTAIN VS SIZE BAND AS % TOTAL TAKE-UP



Source: BNPPRE

SOUTH EAST SPECULATIVE DEVELOPMENT (MILLION SQ FT)



Source: BNPPRE

INVESTMENT

South East office investment reached £559m in Q1 2018, 22.3% up on the same period last year and 73.0% up on the ten-year Q1 average (2008-2017). Of this Hammersmith accounted for 56.5% of the South East total across five transactions.

A number of key investment transactions occurred over the first quarter. These include Spelthorne Council's purchase of 12 Hammersmith Grove for £170m, reflecting a 5.25% Net Initial Yield (NIY), which demonstrates the continuing investment drive from local authorities. In addition, First Property Group acquired Imperial Place in Borehamwood for £62.5m, a NIY of 6.39%, whilst Mayfair Capital purchased British Gas' office at Oxford Business Park for £35.04m. The latter, let for 9.8 years, achieved a 4.9% NIY, illustrating the continuing appetite for income in a low return environment.

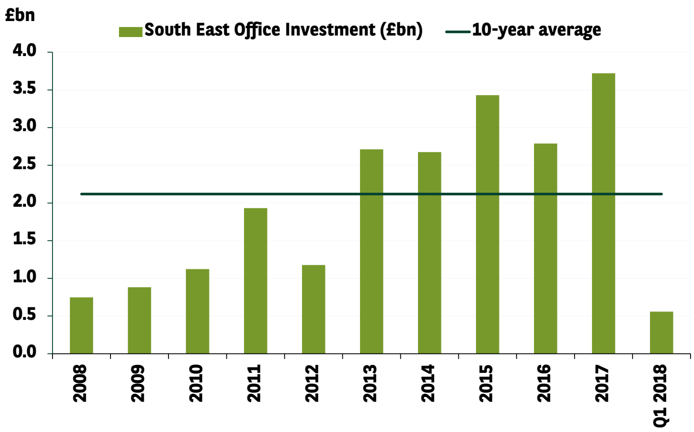
The profile of investors pursuing opportunities in the South East remains diverse, with Middle Eastern and Asia Pacific investors alongside US Private Equity firms and domestic investors all retaining a keen interest in the market.

The South East remains a key region for inward investment due to its strong market fundamentals and vibrant economy. The region is home to a thriving technology sector: latest data from NOMIS places the Information and Communication sector's share of employment at 13.2% within the Thames Valley Berkshire local enterprise partnership, relative to Great Britain at 4.2% and London at 8.0%.

Whilst offering these solid market conditions, the region retains a favourable yield gap between the South East and Central London. Following some yield compression over H2 2017, prime yield levels in the South East remain at 5.00% at Q1 2018, relative to 4.00% in the City and 3.50% in the West End.

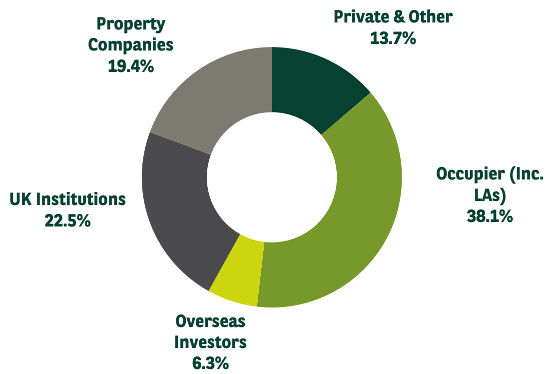
Looking ahead, further yield compression for prime town centre assets is expected following the trend witnessed in the large regional cities over Q4 2017 and Q1 2018. The challenge will be finding value in a stock-starved market, however, we consider that there will be good opportunities for growth in short-income town centre offices and tier 2 towns which are only just experiencing rental jumps. Crossrail towns are also likely to see above-average rental growth benefits arising from their increased connectivity.

SOUTH EAST OFFICES INVESTMENT VOLUMES (£bn)



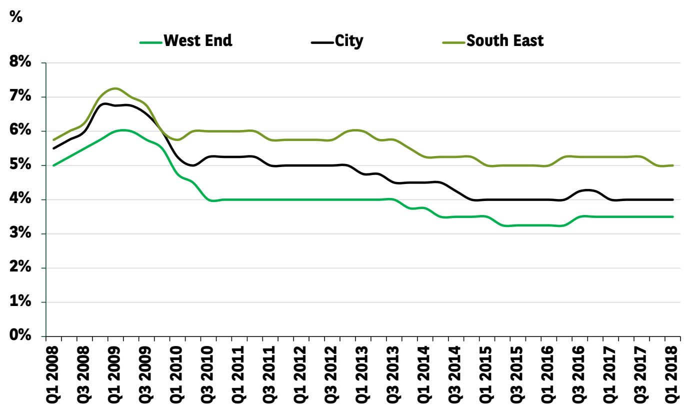
Source: BNPPRE/ Property Data

SOUTH EAST OFFICES INVESTOR PROFILE Q1 2018 (%)



Source: BNPPRE/ Property Data

SOUTH EAST PRIME YIELD VS CENTRAL LONDON SUBMARKETS (%)



Source: BNPPRE

6 BUSINESS LINES in Europe

A 360° vision

Main locations*

EUROPE

FRANCE
Headquarters
167, Quai de la Bataille
de Stalingrad
92867 Issy-les-Moulineaux
Tel.: +33 1 55 65 20 04

BELGIUM
Avenue Louise 235
1050 Brussels
Tel.: +32 2 290 59 59

CZECH REPUBLIC
Pobřežni 620/3
186 00 Prague 8
Tel.: +420 224 835 000

GERMANY
Goetheplatz 4
60311 Frankfurt
Tel.: +49 69 2 98 99 0

HUNGARY
117-119 Vaci ut.
A Building
1123 Budapest,
Tel.: +36 1 487 5501

IRELAND
20 Merrion Road,
Ballsbridge, Dublin 4
Tel.: +353 1 66 11 233

ITALY
Piazza Lina Bo Bardi, 3
20124 Milano
Tel.: +39 02 58 33 141

LUXEMBOURG
Axento Building
Avenue J.F. Kennedy 44
1855 Luxembourg
Tel.: +352 34 94 84
Investment Management
Tel.: +352 26 26 06 06

NETHERLANDS
Antonio Vivaldistraat 54
1083 HP Amsterdam
Tel.: +31 20 305 97 20

POLAND
Al. Jana Pawła II 25
Atrium Tower
00-854 Warsaw
Tel.: +48 22 653 44 00

ROMANIA
Banul Antonache
Street n°40-44
Bucharest 011665
Tel.: +40 21 312 7000

SPAIN
C/ Emilio Vargas, 4
28043 Madrid
Tel.: +34 91 454 96 00

UNITED KINGDOM
5 Aldermanbury Square
London EC2V 7BP
Tel.: +44 20 7338 4000

MIDDLE EAST / ASIA

DUBAI
Emaar Square
Building n° 1, 7th Floor
P.O. Box 7233, Dubai
Tel.: +971 44 248 277

HONG KONG
25 /F Three Exchange
Square,
8 Connaught Place, Central,
Hong Kong
Tel.: +852 2909 2806

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** Coverage In Transaction, Valuation & Consulting

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