SOUTH EAST OFFICES REVIEW
Q1 2019
KEY STATS AT A GLANCE

Leasing & Investment
504,914 SQ FT
Q1 2019 South East office take-up
-20% on Q1 2018

83%
South East office take-up Grade A and above
Demonstrates a clear flight to quality by occupiers

68%
% Take-Up in M4 and West London markets
Occupiers were drawn to the core South East and West London

£375 M
2018 South East office investment
-52% on Q1 2018

5.00%
South East prime office yield
+25bps on Q4 2018

32%
% of transactions by Local Authorities
LA’s continued to be the largest investor group over Q1 2019
LEASING
An in-depth overview
Following the strength of demand over 2018 alongside current political and economic uncertainty, it is perhaps not surprising that occupier activity has fallen back over Q1 2019.

Over the course of the quarter, take-up reached 504,914 sq ft, a 20% decline on Q1 2018 and below the long run average.

However, despite overall market activity falling back, there were still a number of significant leasing deals recorded. The largest deal of the quarter comprised Discover Financial Services’ letting of 45,788 sq ft at Ascent 3, Farnborough Aerospace Centre.

In times of uncertainty, there is always a clear flight to quality, with occupiers opting for higher quality stock. Q1 2019 has been no different, with 83% of take-up concentrated within Grade A and New Grade A buildings.

Following this, it is unsurprising that the majority of take-up has been focused in the core M4 and West London markets over Q1, amounting to 68% of total take-up. It is these markets which have recorded the lion’s share of speculative
development in recent years and possess an overall higher quality available stock profile as a result.

Whilst occupier activity has slowed over this first quarter, the South East office market is well placed to withstand a slightly slower pace of demand.

Available supply across the South East remains below the long run average and in certain towns vacancy is especially low in comparison to history.

The overall quality of vacant space has also improved, with a significant proportion of the market’s tertiary stock sold for conversion to alternative uses. The South East market's generally improved stock profile will help it remain an attractive location for prospective occupiers.

In terms of speculative development moving forward, the South East is due to see a limited number of schemes delivered. 2019 is due to see the delivery of just eight schemes totaling 550,000 sq ft, followed by four schemes totaling 394,000 sq ft in 2020.

"Take up in Q1 2019 was down on the five-year average, however this was more a factor of Q4 2018 being the best quarter for take up in 11 years and no significant transactions slipping into 2019."

"Looking ahead we expect take up to be more in line with the five-year average in Q2. Whilst we are unlikely to see a repeat of the significant size transactions recorded in 2018, there is strength and depth in the mid size ranges."

"It is encouraging to see identified demand increasing from 4.2m sq ft in Q4 2018 to 4.4m sq ft in Q1 2019, with 675,000 sq ft under offer."

Ed Smith, Head of Office Agency at BNP Paribas Real Estate
INVESTMENT
An in-depth overview
In line with the occupier market, the South East office investment market has also slowed over Q1 2019.

Total volumes for the quarter reached £375m, 52% down on the same quarter in 2018. However, given the current economic and political uncertainty affecting the UK, a slowdown in activity over this first quarter was to be expected.

A slower first quarter also does not necessarily predicate a weaker performance over the year: in 2016 Q1 volumes reached £316m but by year end volumes had surpassed £2.7bn, in line with the 10-year market average.

Over Q1 2019, investor caution and stalled decision making, alongside a relative lack of product on the market, has impacted volumes.

"With over half of purchases being driven by domiciled investors, this demonstrates continued confidence in the South East office market."

"Overseas investors continue to sit on the side lines while they try to understand the impact of Brexit on the investment market but, as with Private Equity, both investor types have considerable sums of capital to invest."

Hugh White, Head of National Office Investment
Another key impact on investment volumes over Q1 2019 comprised the lack of larger lot sizes transacted. Investor focus was instead concentrated on smaller lot sizes under £40m.

Prime yields have recorded some outwards movement at Q1 2019, standing at 5.00% in the South East, up from 4.75% at Q4 2018.

The South East still offers relative value in comparison to Central London offices with prime yields in the City and West End standing at 4.00% and 3.50% respectively.

At 5.00%, South East office yields also now sit slightly above a number of the Big Six cities. Birmingham, Bristol, Edinburgh and Manchester all stand at 4.75% at the Q1 stage, with Leeds (5.00%) and Glasgow (5.25%) sitting slightly above.

"Offices remain the amber sector, with the attractive income yield they generate meaning many landlords will continue to hold them."

"Prime assets continue to achieve strong yields, as we saw with NFU buying Victory House, Brighton for £36.1M reflecting 4.9% NIY in March."

"Looking ahead, Q2 has seen a number of assets come to the market which will assist in increasing volumes, namely; Davidson House, Reading, Ermyn House, Leatherhead and Bridge House, Guildford."

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