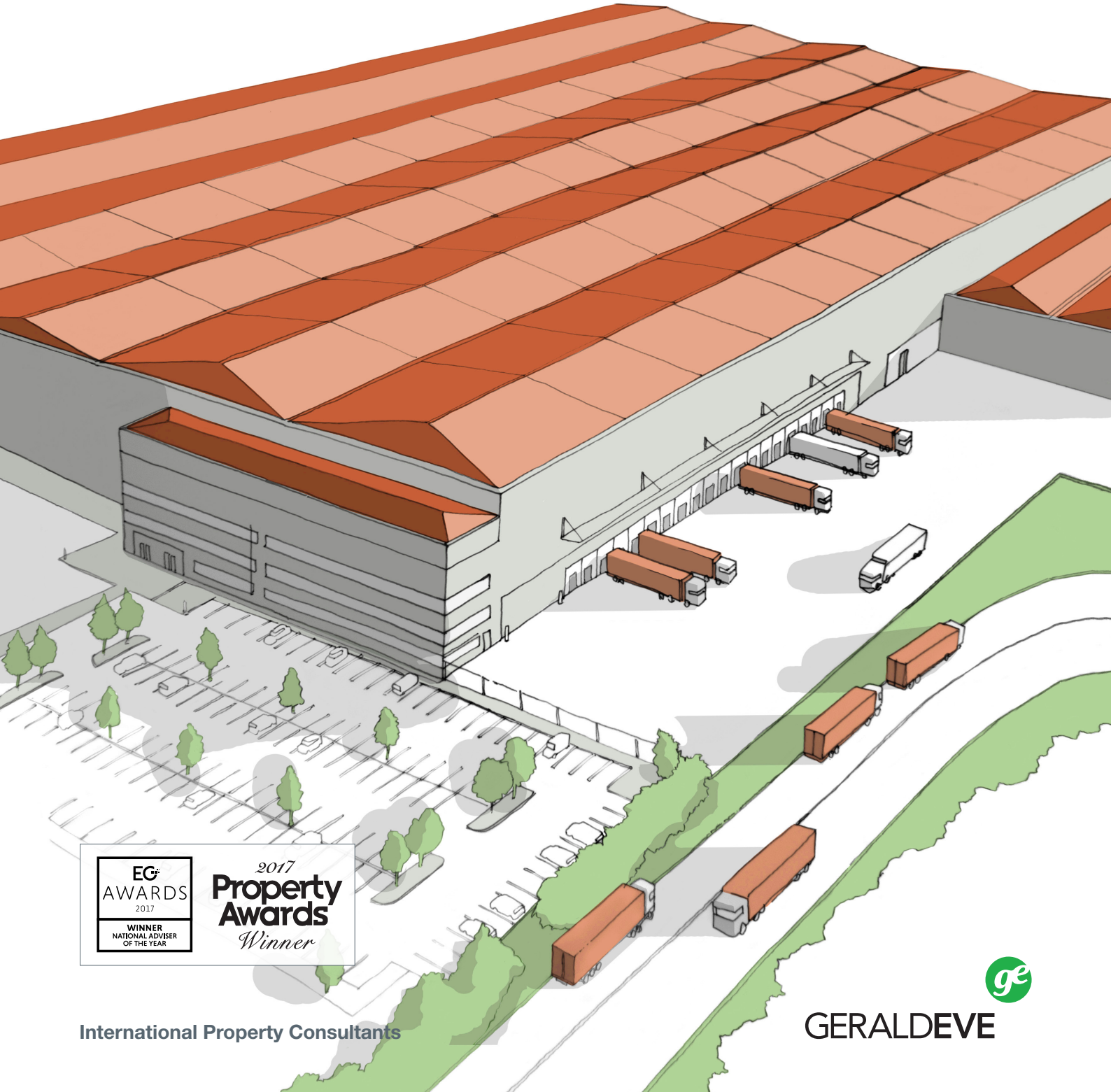
PRIME LOGISTICS

The definitive guide to the UK's distribution property market
Q1 2018 Bulletin



EG AWARDS 2017 WINNER NATIONAL ADVISER OF THE YEAR

2017 Property Awards Winner

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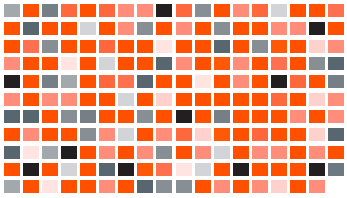
11.5m sq ft
up 20% on Q4



189,000 sq ft
average size of building taken-up in Q1

2.8m sq ft
started speculative development in Q1

STRONG START TO 2018

Following a disappointing end to 2017 in terms of occupier take-up, we recorded a strong rebound in activity in Q1 2018, with 11.5 million sq ft of space taken-up. This was a 20% quarterly increase and is 5% above the 11 million sq ft 5-year quarterly average.

The nature of demand in the first quarter was in stark contrast to activity in 2017, not only in terms of building size but also the occupier sectors committing to space. Deals on buildings over 100,000 sq ft accounted for 85% of all transactions in Q1 and the average size of building taken-up was 189,000 sq ft – the largest quarterly average building size recorded since Q1 2007.

It was large scale occupier land purchases and pre-lets which drove this increase, with occupiers such as Lidl, Aldi and Eddie Stobart all making large commitments to space. Whether for reasons of business certainty or building specification, we have recorded an increased number of occupiers making land purchases over the last 18 months. Encouragingly, we have also recorded a sharp uptick in activity in the number of deals agreed between 200,000 sq ft and 500,000 sq ft in size.

RETAILERS DRIVE ACTIVITY

Manufacturers accounted for 34% of all activity during 2017. However, in Q1 2018, this fell substantially to only 16%. Whilst there have been some notable deals, such as Premier Farnell pre-letting space in Leeds, e-Leather pre-letting space in Peterborough and Black & Decker taking space in the North East, it was retailers who have been most acquisitive, accounting for 43% of Q1 take-up.

In Q1 we recorded a continued increase in the number of deals and volume of space taken-up through development land purchases, particularly by budget food retailers. Large land purchases by Lidl and Aldi in Luton and Dunstable drove up both the average building size taken-up and the importance of retail in Q1. It also meant that it was activity on new or refurbished space which was the overwhelming driver of take-up during Q1, with such space accounting for 65% of all activity.

The average size of building taken-up by logistics occupiers almost doubled during Q1 – to 236,500 sq ft. The increase was driven by Eddie Stobart committing to take space in Corby and Doncaster, and Yearsley pre-letting 400,000 sq ft in Peterborough.

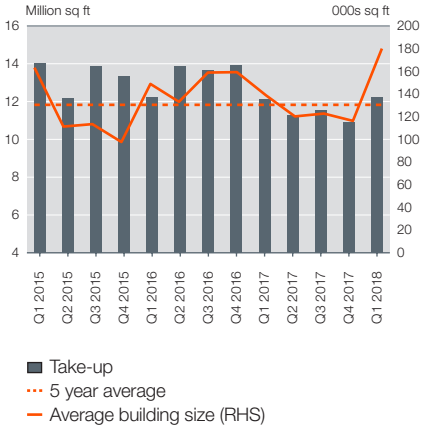
51% INCREASE IN SPECULATIVE DEVELOPMENT

2.8 million sq ft got underway speculatively in Q1 – a 51% increase on the 1.9 million sq ft that started in Q4 2017. This is a strong quarter for spec development starts and far in excess of the 5-year quarterly average of 1.5 million sq ft.

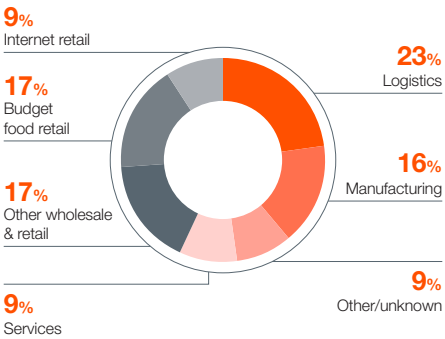
In total, 21 individual buildings started speculatively in Q1. Regionally, activity was strongest in Northern England and the East Midlands following First Panattoni and Goodman's decisions to commence developments. We also saw an increase in activity in our London West region during Q1 following starts in Hayes and Uxbridge.

For the second consecutive quarter, there were more speculative than purpose-built development starts. The average size of speculative development also continued to increase and averaged 134,300 sq ft in Q1. In a 'normal' market, this would be a concern in terms of market regulation; however in most markets supply remains incredibly tight, with UK average availability rates of 6.2%.

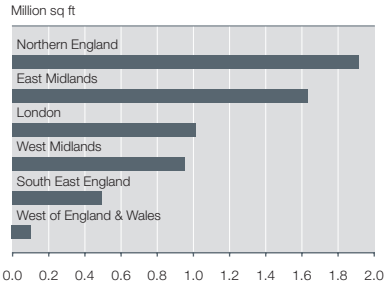
Quarterly take-up, 5 year quarterly average and average unit size taken-up , Q1 2015 - Q1 2018
Source: Gerald Eve



Q1 2018 take-up by occupier sector
Source: Gerald Eve



Space under construction speculatively at the end of Q1 2018
Source: Gerald Eve



1%

Quarterly prime headline rental growth in Q1

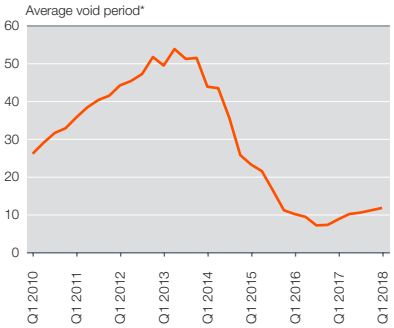
RENTS CONTINUE TO GROW

Q1 2018 was another quarter of positive prime headline rental growth and we recorded rises in 10 out of our 51 centres and an overall quarterly rental growth rate of 1%. Markets where rents increased further in Q1 include Corby, Daventry and Heathrow, where the restricted supply allied to the pent-up occupier demand has meant that the schemes that have been delivered have attracted enhanced rental profiles.

Rents are now an average £7.20 per sq ft in the UK, the highest average prime rent on record. Based on the volume of space under construction speculatively, which is currently around 6 million sq ft, the total expected in 2018 is likely to be roughly the same as that delivered in 2017.

We continue to closely monitor the average void period on these speculative developments, which, across the UK, has risen for the third consecutive quarter to 12 months. Whilst rising, this average is driven by a handful of individual long-standing voids, notably in Scotland and Northern England. Regionally, such voids are considerably lower in core markets such as the West Midlands, London and the South East, which in turn could drive further rental growth.

Void period on speculatively developed space, Q1 2010-Q1 2018
Source: Gerald Eve



*For this calculation, the void period runs from PC and specualtive developments let during construction are given a zero month void period

14bps

inward movement in UK prime yields in Q1

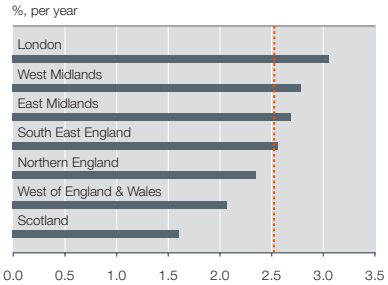
LACK OF INVESTMENT STOCK

There continues to be a burgeoning weight of capital targeting the UK logistics sector. The strong occupational fundamentals and impressive investment performance figures, together with the ongoing structural change to internet retail have resulted in fierce bidding on the limited amount of stock that does come to the market.

This in turn hardening UK prime yields by a further 14bps in Q1. Nationally, average prime yields are now the lowest on record at a UK average of 5.11%. UK institutions, overseas investors and REITs have been the largest net purchasers of distribution warehouse property so far in 2018.

It is likely that over the medium term, logistics property values will be supported much more by growth in rents than significant levels of yield compression, especially so given the potential for future interest rate increases. We forecast an average 3.4% UK rental growth in 2018 and an average 2.6% per year over the next five years. Regionally, we expect the strongest growth in prime rents in core markets in the West Midlands and London, especially those locations with pent-up demand, very weak supply and that can offer occupiers fast access to key markets.

Prime rental growth forecast by broad region, 2018-2022
Source: Gerald Eve



3.4%

2018 forecast UK prime rental growth

A STRONG YEAR AHEAD

Given the strong start to 2018 and the elevated levels of space under offer and requirements in the market, we expect that take-up will remain above the long term average through 2018. It is likely that 2018 will be defined by the take-up of new space through pre-lets, occupier interest in speculatively-developed buildings and occupier land purchases.

The restricted availability of land continues to be a concern for the market, especially given the continued loss of employment land to higher value uses. This will keep upward pressure on land values and continue to push the boundaries of building design in terms of multi-storey facilities and intensification of use. We have seen industrial land close to London transact at very high prices so far in 2018 and several leading developers are committed to the development of multi-storey facilities. The availability of large and reliable volumes of power to accommodate these new building concepts and uses is crucial.

The availability of logistics space is likely to increase throughout 2018. A combination of the delivery of speculative developments and the potential for the return of secondhand space, perhaps as a result of the spate of high profile retail administrations or through retailers such as M&S and Shop Direct deciding to move certain operations to core markets, which could in turn start to feed through to a welcome increase in occupier choice.

GERALDEVE

GERALD EVE IN THE MARKET

Gerald Eve is well-established in the logistics property market and covers the full range of property services, from national occupational and investment agency through to lease consultancy and valuation. Our specialists have been involved in several high profile transactions during the quarter. Please contact them directly for more information.

Jon Ryan-Gill
joined us in March as head of the Birmingham office and will lead the Midlands industrial team.

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Prime Logistics is the definitive guide to the UK's distribution property market. Dealing with logistics units of 50,000 sq ft and above, this research report gives detailed analysis and statistics for 26 key distribution areas – from take-up, stock and development statistics to drivers of occupier demand, growth forecasts and regional outlooks. All previous editions can be downloaded from our website.

United States and European Alliances

Gerald Eve has an international alliance with Lee & Associates who have offices in 56 US and Canadian cities and a number of Europe alliance partners in 20 cities across 16 European countries.