AVISON YOUNG

South East offices

Key towns update of activity

Q4 2019

PIERS LEIGH
Principal South East Offices

2019 saw the second town in the South East market achieve rents of £40 per sq ft with Oxford joining Cambridge. We anticipate further rental growth in our key towns in 2020 as demand picks up on the back of political stability and increased structural demand.

Introduction

The South East market is very difficult to assess as one market given the disparate nature of the towns and geography that it covers. In order to provide a meaningful and more detailed insight, we have picked 10 key markets made up of towns which have established in town and out of town markets covering the whole of the south east geographical area outside central London and the Greater London submarkets.

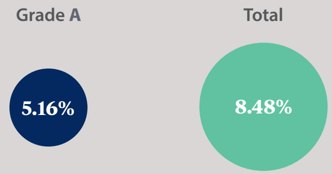
Our aim is to give you a snap shot of the demand and supply in these key towns and cities to identify trends which influence this important market area for the UK office sector. Our largest markets of Reading and Cambridge lead the way in terms of development and headline rents; however, smaller markets such as Crawley are also important to the overall make up of the market and establishing occupier sentiment and trends. We hope that this report is both informative and thought provoking and we will be continuing to increase our research in the South East with research papers being produced that look in more depth at key trends, opportunities and challenges that affect those that occupy and invest in office space in the South East. Our team of occupational and investment agents specialising in the South East are looking forward to working with you in 2020 and beyond.

2019 was a mixed year in terms of take up with occupiers and landlords reacting to the political uncertainty which dominated the year. Occupiers that could avoid making a decision delayed moves and landlords were reluctant to let occupiers leave, offering flexible lease extensions so that any void could be delayed until the uncertainty had passed.

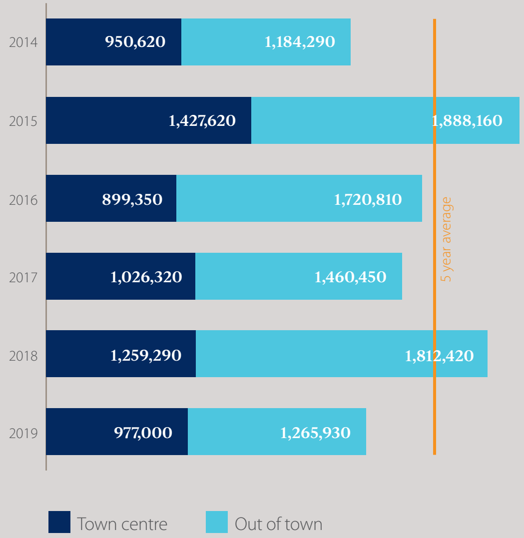
Having said that, a number of key transactions took place and where development has taken place in our 10 barometer towns, this bravery has been rewarded, most notably in Milton Keynes and Cambridge where prime rents moved forward significantly. Overall 2019 was a quiet year with take up across the South East 10 towns below the 5 year average. Some markets are now suffering from a chronic lack of stock rather than demand; Watford being a prime example of this.

On the investment side, transaction numbers were down but overall volumes were above the 5 year average with a good level of deals exchanging in Q4. Without the large transactions of Lakeside in Portsmouth and Croxley Business Park to boost the amount of money invested, it would have been a quieter year overall, however, despite the funds being largely sellers, property companies and overseas investors have filled the void. There remains a significant amount of cash looking for quality product which bodes well for 2020, as a degree of the political uncertainty has been removed due to the election result in December, which will act as a further boost to confidence.

Q4 2019 vacancy rates



Ten towns total take-up (sq ft)



Varsity corridor

CAMBRIDGE

Cambridge, despite continuing to see very strong rental growth, had a dip in overall take up in 2019 reaching 480,000 sq ft, 12% down on the 5 year average of 550,000 sq ft. This was in some way due to the over performance in 2018, but of more concern is the lack of opportunities due to stock starvation in the market. Take up in the town centre was unusually high at 60% of the total because of supply coming through on Station Road, part of Brookgate's CB1 regeneration with development funded by Aviva, this included the fully letting before completion of 50/60 Station Road (156,000 sqft) and the pre-letting of 80,000 sqft to Apple at 30 Station Road. Rents in 50/60 Station Road peaked at £46.00 per sq ft on the 8th and top floor which is the highest rent in the UK outside the M25. Supply is equivalent to c. 1½ years take up.

Cambridge vacancy rates Q4 2019

Grade A	Total
3.16%	5.14%

Quarter 4 take up

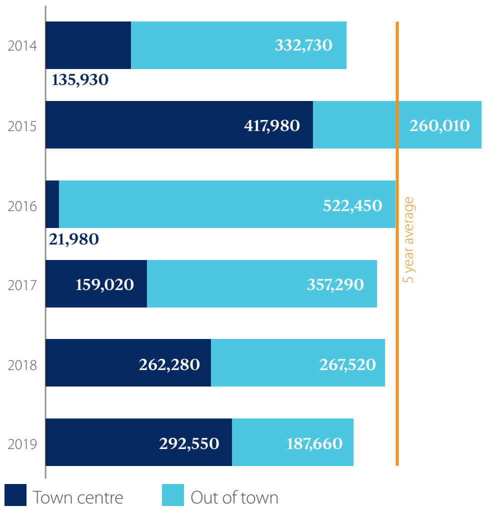
Town centre

26,410 sq ft

Out of town

37,120 sq ft

Annual take up



MILTON KEYNES

The office market in Milton Keynes has been greatly influenced in 2019 by the success of AW James's speculative development of 100 Avebury Boulevard. The 140,000 sq ft building attracted Spaces, Shoosmiths and Aiimi taking 70,000 sq ft while under construction. The building was completed in October and is now fully let following a final letting to Xero. A new rental figure of £27.50 per sq ft was achieved and this had a positive impact on the market. The best example of this is the Ashton and Norfolk House scheme which offers refurbished 1980's space where rents have risen during the year from £18.50 per sq ft to £22.50 per sq ft. With Milton Keynes' strategic location between Oxford and Cambridge and the proposed Varsity Line (rail) and Varsity Expressway (road) both running past Milton Keynes, we expect to see more appetite from investors and developers buoyed by the success of 100 Avebury Boulevard in the short to medium term.

Milton Keynes vacancy rates Q4 2019

Grade A	Total
3.64%	7.27%

Quarter 4 take up

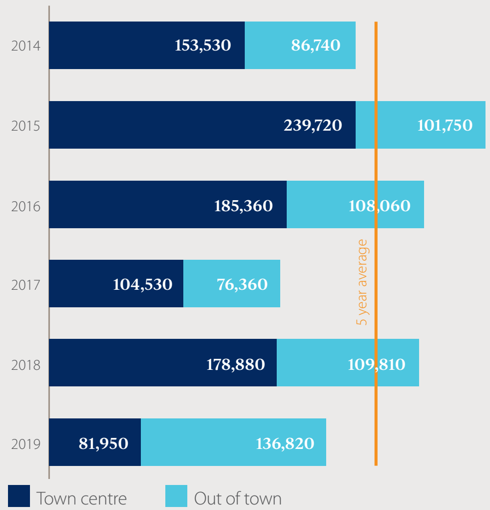
Town centre

5,000 sq ft

Out of town

0 sq ft

Annual take up

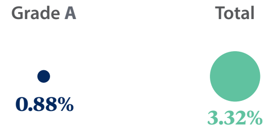


OXFORD

Oxford continued to enjoy significant rental growth during 2019 with prime rents breaking through the £40 per sq ft mark for the first time. In addition to this, the low vacancy rate and strong demand means secondary rents have also increased with good quality well located grade B space commanding over £30 per sq ft. The lack of development opportunities in the town centre mean new development is only likely to be seen in the out of town market.

Without a significant uptick in development activity take up figures will struggle to make the 5 year average due to a lack of stock. However, with plans for further development at the Oxford Science Park and with development land at Oxford Business Park, there is the potential to address this demand supply imbalance in the out of town market over the medium term.

Oxford vacancy rates Q4 2019

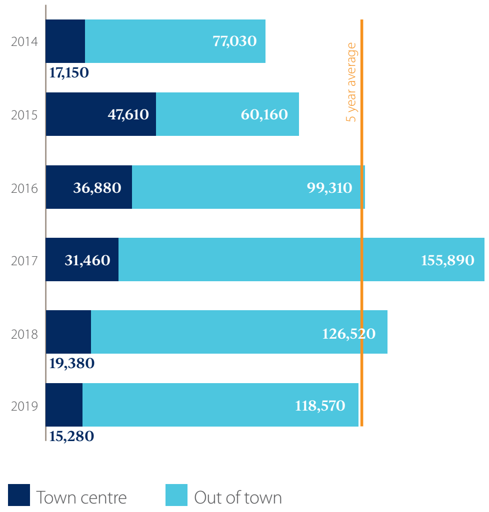


Quarter 4 take up

Town centre
0 sq ft

Out of town
40,870 sq ft

Annual take up



M3/M4 Towns

BASINGSTOKE

With landlords and developers taking advantage of the increasing level of demand in the Basingstoke area and comprehensively refurbishing buildings to Grade A specification, take up in 2019 was around 240,000 sq ft, just above the 5 year average of 172,000 sq ft.

52% of take up was situated on Basing View in the town centre as corporate occupiers have been seeking good value Grade A office space with excellent travel links and good quality local amenities, retail and leisure offerings, and wellbeing at the core of some of their business requirements. Prime office rents in the town are now being quoted at £28.50 per sq ft, which is £2.50 per sq ft higher than the level achieved in 2018.

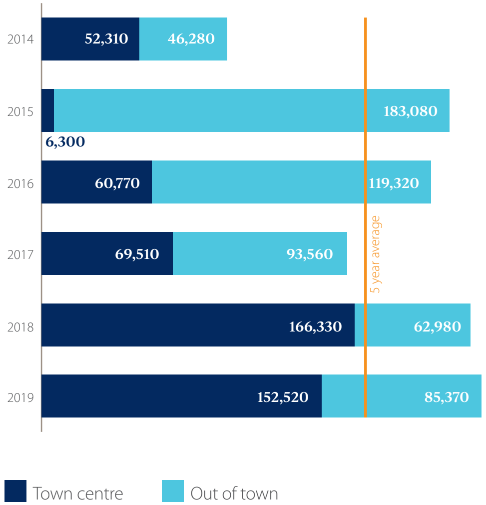
Basingstoke vacancy rates Q4 2019

Quarter 4 take up

Town centre
0 sq ft

Out of town
28,570 sq ft

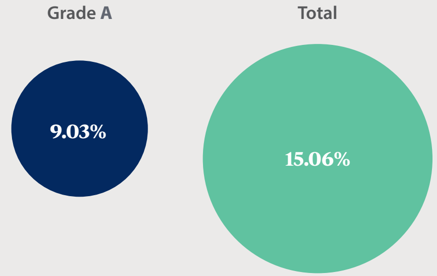
Annual take up



READING

Overall take up in the Reading market last year was 515,000 sq ft which is 7,600 sq ft below the 5 year average and 147,400 sq ft of this was in the town centre. Grade A supply in Reading town centre has almost halved since 2014. A significant amount of Grade B and C space in the town centre has been converted to residential and there is now a lack of floorplates over 10,000 sq ft. Only 4 buildings are able to offer in excess of that on one floor, two of them being available for sublease. The combination of the lack of Grade A space in the town centre and Landlords providing new amenities to business parks to meet tenant demand for better health and wellbeing at work has allowed for strong take up in the out of town business parks. This has been met by an up tick in supply for the out of town market on the back of refurbishments and in Q1 2019, Green Park started a 234,000 sq ft speculative development of offices at 400 and 450 Longwater Avenue, to be delivered in September 2020.

Reading vacancy rates Q4 2019

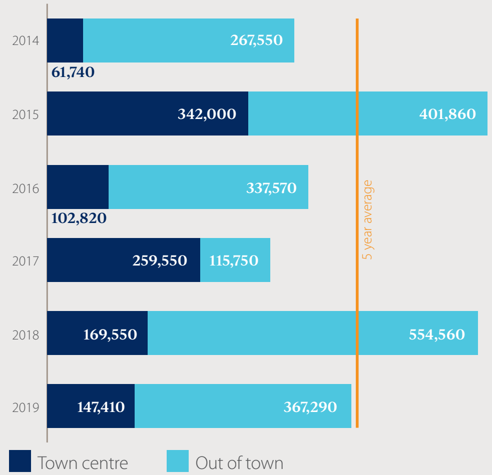


Quarter 4 take up

Town centre
49,000 sq ft

Out of town
5,840 sq ft

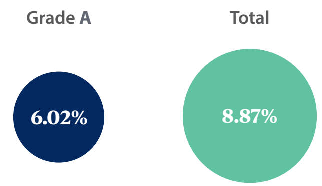
Annual take up



MAIDENHEAD

Maidenhead saw below average levels of take-up in 2019 at 107,000 sqft with over two-thirds in the out of town market where the majority of the supply is located. The town centre suffers from a lack of supply with only 20,000 sq ft of Grade A offices available in Berwick Hill's Lantern which was completed in Q2 2019. The pipeline for the town centre is more encouraging with Clearbell's 22 Market Street and Orbit Southern's Arena Court undergoing a comprehensive refurbishment and Smedvig's site at The Landing now cleared for building to start. Out of town, one of the few new buildings under construction in the Thames Valley is 5 Foundation Park (68,000sq ft) which is due for completion in Q2 2020. The largest letting of the year was Regus taking 16,800 sq ft at Concord Park. The long-anticipated arrival of the Elizabeth Line should bring increased demand and there is potential for pre-letting activity to be seen in the town centre.

Maidenhead vacancy rates Q4 2019

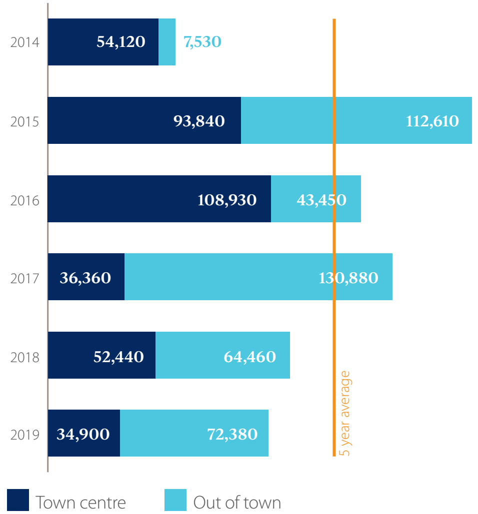


Quarter 4 take up

Town centre
7,330 sq ft

Out of town
21,460 sq ft

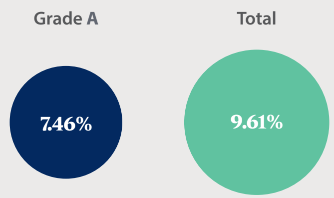
Annual take up



SLOUGH

Take-up in Slough last year was the lowest in ten years with just short of 80,000 sq ft recorded, only half of the 10 year average of 158,000 sq ft. This comes on the back of an impressive 2018 when 320,000 sq ft transacted, which was the best year since 2005. Spelthorne Borough Council's 27,400 sq ft letting to Mattel at The Porter Building helped boost the figures in Q4 2019, which means the 111,000 sq ft speculative office development is now fully let. Take-up has been muted, due in part to the uncertain political landscape, which has resulted in occupiers delaying decisions where possible. This has not been helped by supply in the market remaining at its lowest level since 2000 with around 560,000 sq ft currently available. Prime headline rents are currently £36.00 per sq ft, and with a reduction in Grade A availability and relatively limited supply, we expect to see prime headline rents remain stable in 2020.

Slough vacancy rates Q4 2019

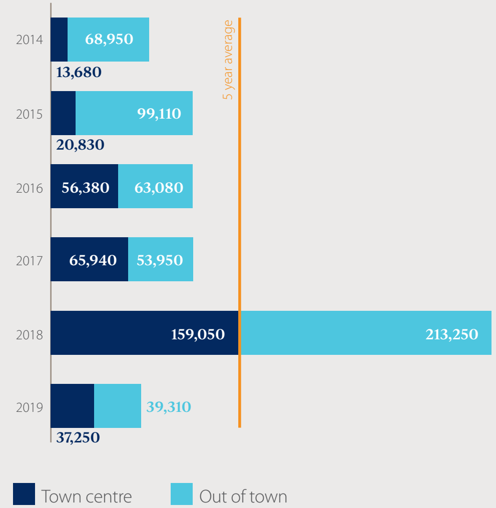


Quarter 4 take up

Town centre
27,400 sq ft

Out of town
7,140 sq ft

Annual take up

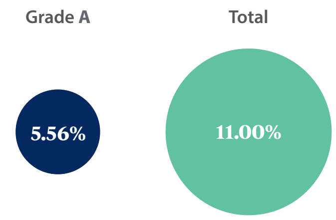


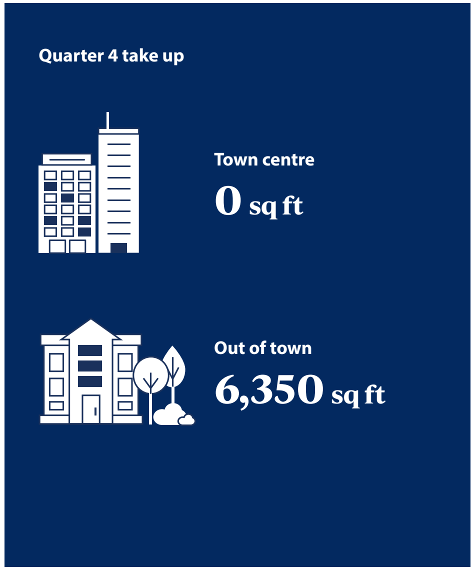
M25 Towns

CRAWLEY

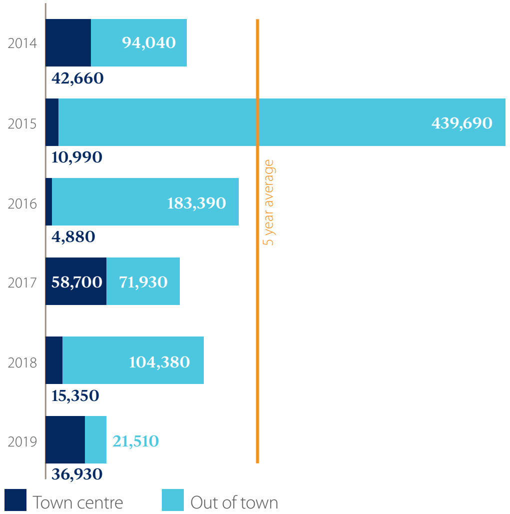
Crawley had another year of poor take-up at 52,000 sq ft which is the fourth year in a row since the strong take up of 2015 when take-up reached over 500,000 sq ft with 2 lettings of over 100,000 sq ft to Elekta and Virgin Atlantic. The majority of the supply is in the out of town market, concentrated in Manor Royal next to Gatwick Airport, accounting for just 31% of take-up. The largest letting was only 12,000 sqft taken by RAPP in Galleria, a refurbishment of a 1980's ex-Virgin Holidays building close to Crawley rail station, relocating from Manor Royal. Prime rents are £27.00 per sq ft at Manor Royal, but there are generous rent free periods available as landlords battle for the attention of the limited demand in the market and competing schemes. This is likely to result in more office space being converted to alternative uses in the out of town market, including industrial, due to its excellent domestic and international connectivity.

Crawley vacancy rates Q4 2019





Annual take up



GUILDFORD, WOKING & WEYBRIDGE

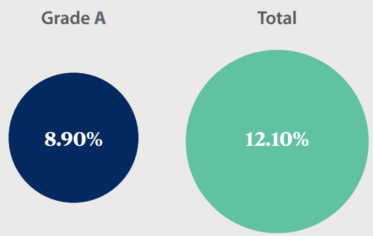
Guildford had a bounce back in terms of take up for 2019 to around 130,000 sq ft which is more in line with the 5 year average and above the relatively low levels of take up recorded in 2018 of over 60,000 sq ft. The market was again dominated by smaller transactions, landlords have responded by dividing up their offering and being more flexible with the terms they are prepared to agree. Rental growth remained flat throughout 2019, however prime rents look set to increase in early 2020 with strong interest in recently completed schemes such as Riverworks and 255 High Street.

Woking had a quiet year in terms of take up but ended with a flourish with news that Surrey County Council are set to purchase Midas, 62 Goldsworth Road for their own occupation as part of their long anticipated move out of Kingston. Redevelopment and refurbishments at the Forge, Space and Brook House in Woking have all combined to increase prime rents to £36.00 per sq ft which rose above prime rents in nearby Guildford for the first time. The majority of demand during the year was driven by existing Woking occupiers either expanding or upgrading their occupation, however Astellas Pharma taking 12,500 sq ft at the newly developed Space Woking highlighted the towns superb connectivity to both London and the South Coast and ability to attract new occupiers. 2020 is set to start with a boost in take up with circa 120,000 sq ft under offer at year-end, driven by Surrey County Council's deal at Midas, and Asahi under offer to take a pre-let of 35,000 sq ft at Brook House following a refurbishment by CBRE GI.

Weybridge saw a great deal of activity in 2019 recording almost 150,000 sq ft of transactions. The Dakota Building, completed in 2017, welcomed its first tenants: Robert Half and Yooserv, who took a combined total of 15,000 sq ft.

At The Heights, AXA, Dairy Crest and Willmott Dixon took approx. 50,000 sq ft of space, but by far the largest deal was Astellas taking 55,000 sq ft at the Bourne Business Park, following the letting of their 90,000 sq ft Chertsey building to Samsung. The best rent achieved is £35.00 per sq ft with quoting rents now at £36.50 per sq ft.

Guildford, Woking & Weybridge vacancy rates Q4 2019



Quarter 4 take up

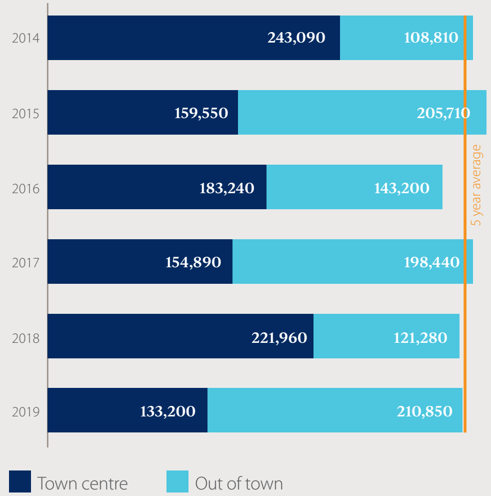
Town centre

1,700 sq ft

Out of town

46,150 sq ft

Annual take up



WATFORD

Watford had a poor year in terms of take up in 2019 and this reflects the stock starved nature of the market with a critically low vacancy rate of sub 3% across all grades and under 2% in the crucial Grade A category. With construction set to begin at 53 Clarendon Road on a new 100,000 sq ft speculative office development in 2020, and with a number of larger requirements looking for space. We anticipate take up to bounce back in 2020 but only on a limited basis due to the constrained supply and development pipeline. Prime rents in Watford now stand at £37.50 per sq ft.

Watford vacancy rates Q4 2019

Grade A	Total
1.65%	2.92%

Quarter 4 take up

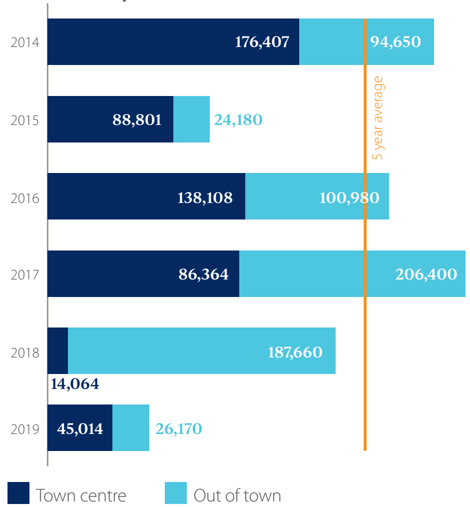
Town centre

19,120 sq ft

Out of town

11,680 sq ft

Annual take up



Investment market update

Despite a challenging environment in 2019 the outlook for 2020 looks cautiously optimistic. Brexit and the future trading relationship with Europe will continue to dominate the headlines and further delays could take place, however given a more stable political platform we expect business to be able to plan for the future with more certainty than they have enjoyed since 2016. With this in mind we expect volumes to bounce back in 2020 and already some of our South East 10 towns have healthy levels of space under offer and strong interest which should make for good Q1 2020 total volumes.

The major concern for occupiers is the lack of speculative development and the low levels of supply which in turn will lead to spikes of rental growth in some markets and make occupiers look further afield to satisfy their requirements. Rents are set to increase across the majority of our South East 10 markets in 2020, however incentives are likely to remain generous for longer leases and large amounts of space.

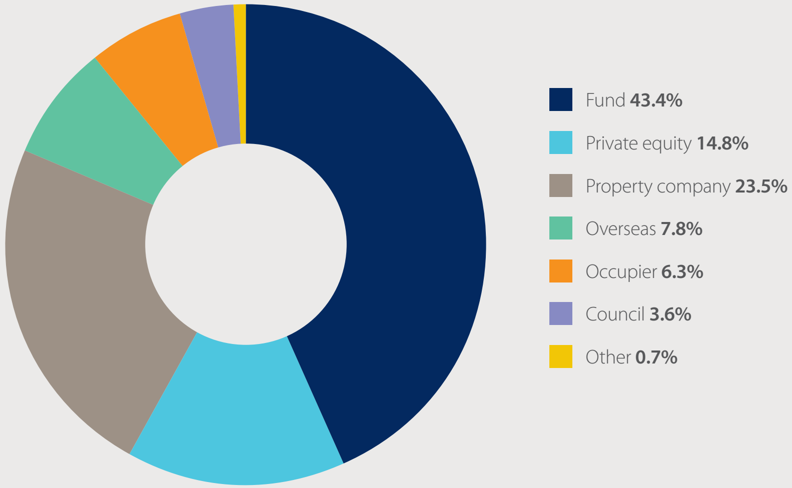
Despite an expectation of activity slowing down whilst the UK awaited greater clarity on Brexit and a looming General Election, investment volumes across the South East remained encouraging throughout 2019 with sale volumes totalling in excess £1.3bn for Q4, 42% up on the Q4 5 year quarterly average.

Total take up for 2019 was £3.68bn, a 5% decrease on 2018 volumes, reflecting the wider economic volatility.

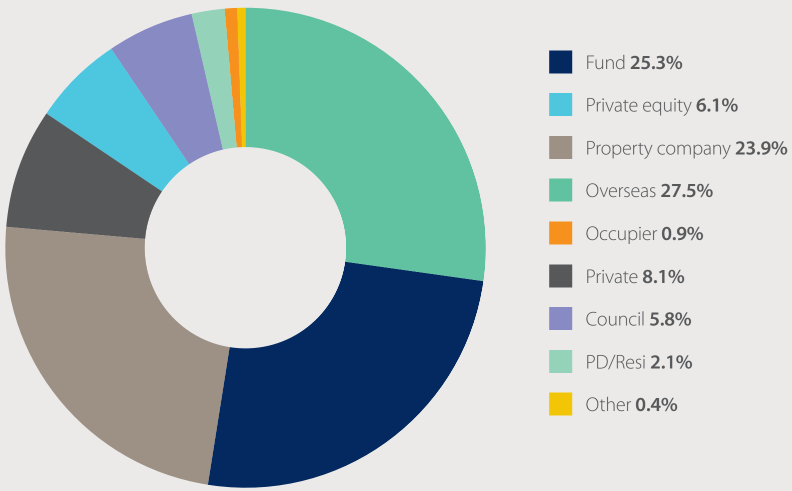
Key Q4 transactions included:-

- **ASOS, Leavesden Park, Watford**
  197,364 sq ft – Price: £86m– NIY: 5.4% – Purchaser: Rostamani – Vendor: Kennedy Wilson
- **The Heights, Weybridge**
  349,903 sq ft – Price: £136m – NIY: 7.06% – Purchaser: Kennedy Wilson – Vendor: M&G
- **King House, 174 Hammersmith Road, Hammersmith**
  59,470 sq ft – Price £51.1m – NIY: 5.7% – Purchaser: Catalyst Capital – Vendor: Kier/Investec
- **50/60 Station and 30 Station Road, CB1 Cambridge**
  237,848 sq ft – Price: £125m for 50% from Aviva – Purchaser: Public Sector Pension Investment Board
- **Seacourt Tower, Botley, Oxford**
  176,442 sq ft (offices and retail warehousing)– Price: £80m – NIY: 4.84% – Purchaser: Brockton Capital – Vendor: BA Pension Fund
- **Clockwork Building, 45 Beavor Lane, Hammersmith**
  39,626 sq ft – Price: £36.40m – NIY: 6.14% – Purchaser: CLS Holdings – Vendor: Westbrook Partners and Stone Real Estate

Q4 2019 Vendors



Q4 2019 Purchasers



Secure income buyers, both domestic and overseas, continue to dominate demand in search of attractive yields in comparison to the fixed income markets, Central London and prime industrial assets. As such, prime yields held stable at 5%. Significant capital remains in place for well-let core assets, despite a shortage of product frustrating many investors.

UK Institutions were the net vendors for 2019 following a turbulent year of redemptions on their open-ended retail funds. Whilst much of the institutional acquisition focus has been on core assets, the funds have remained relatively muted within the secondary/core plus sector, leaving behind a void and opportunity for property companies to fill. CLS Holdings recent flurry of acquisitions in Q4 serves as a prime example of this trend.

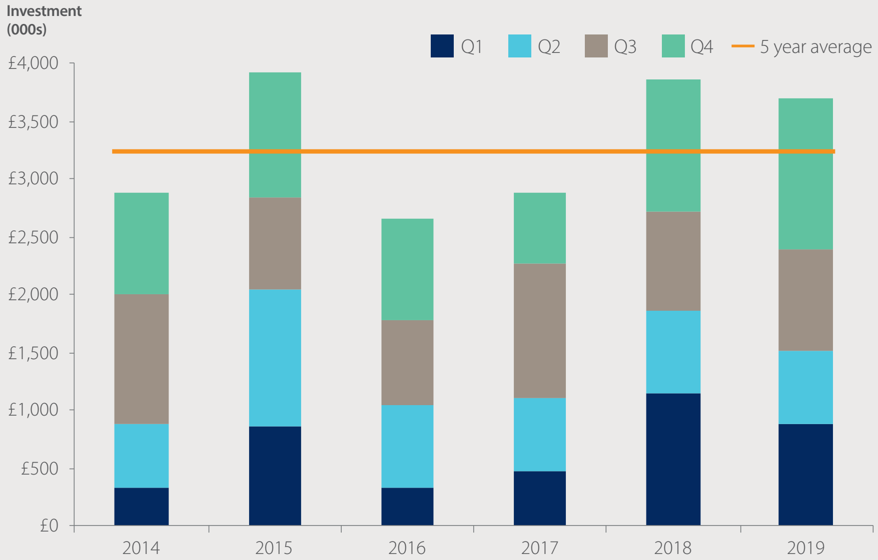
Local Authorities have reduced their volumes from the levels seen in 2018, following a period of re-strategising and some negative press. In addition, the 1% interest rate hike on Public Works Loan Board borrowing has also served as a contributing factor to this decline. Though for some Local Authorities, the funding gap from central government remains and as such further property acquisitions are vital to their investment strategies.

The yield gap between prime and secondary product continues to widen and this is creating a disparity between vendors, valuations and the pricing appetite of buyers. With the current low interest environment and lack of vendor distress, the challenge for investors in 2020 will be whether they are prepared to pay a premium for prizing out off-market stock or risk fierce competition in an open market scenario.

Outlook ahead:

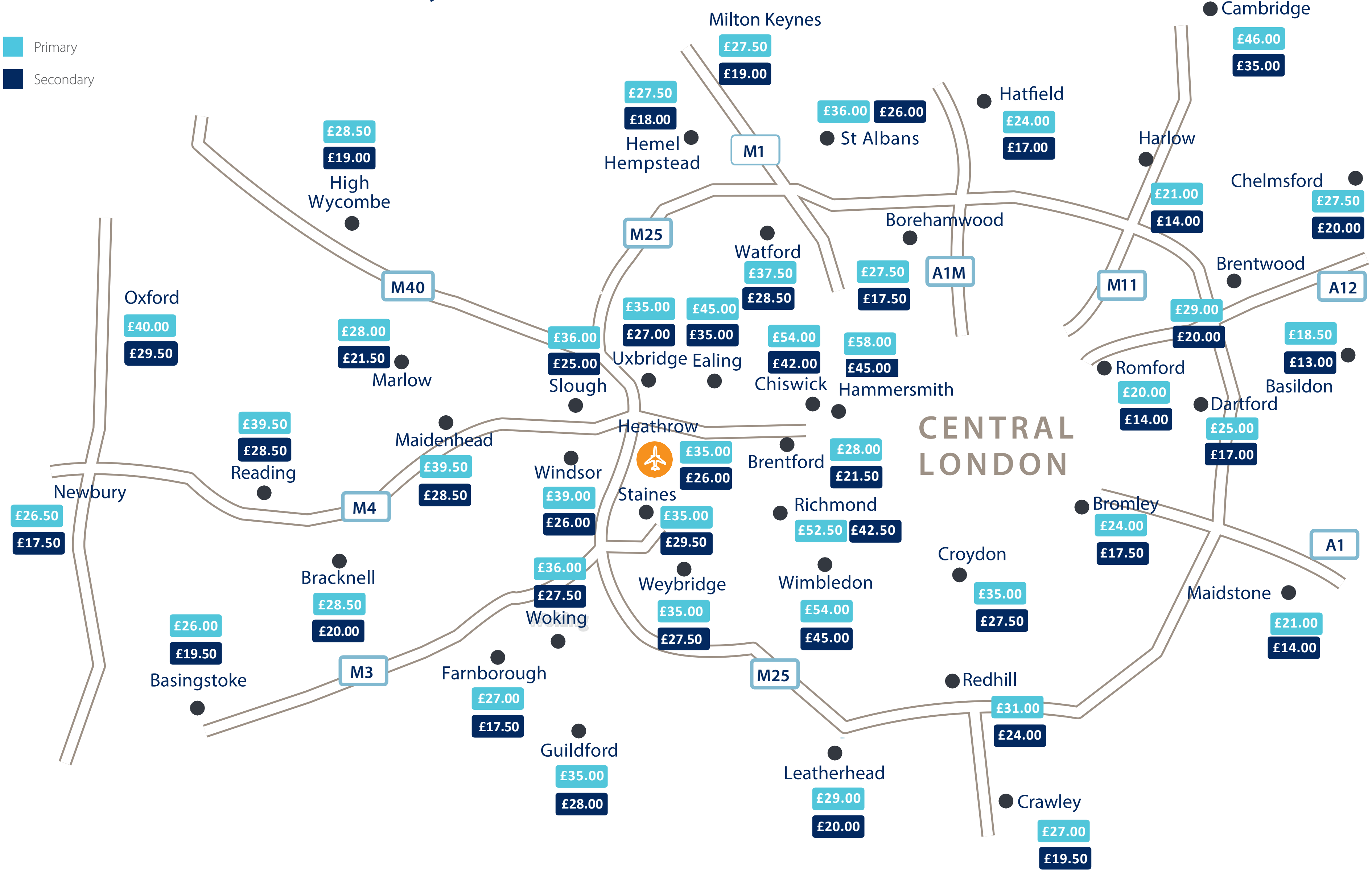
- At the end of Q4, £650m of South East offices were under offer which we expect to sell in Q1 2020.
- Property companies and private equity investors will continue to capitalise on the absence of funds in the secondary/core + sector.
- H1 2020 to surpass H1 2019 volumes following a sentiment boost post-election and the EU withdrawal.
- Volatility to return in H2 2020 as the EU future trade negotiations are expected to conclude.
- Currency fluctuations will continue to attract overseas investors.
- The occupational supply/demand imbalance will continue which will offer strong rental growth prospects.
- Competition will remain fierce for core/prime assets.
- Prime yields will remain stable at 5%.

Average transaction volumes



£1,308 million	**Q4 2019**
Compared to:	
Previous quarter – Q3 2019	**£876 million**
A year ago – Q4 2018	**£1,144 million**
Five year quarterly average	**£920 million**

Prime and secondary rents Q4 2019



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The Heights, Weybridge, purchased by Kennedy Wilson in December 2019.

Should you wish to discuss any details within this update please get in touch.

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