RESEARCH

The Big Nine

Quarterly update of regional office activity

Q1 2020

View >

TOP PERFORMERS

BIRMINGHAM

Occupier market

Birmingham city centre activity was headlined by BT agreeing a letting of 283,000 sq ft at Three Snowhill, leading to the highest Q1 figure ever recorded.

LEEDS

Investment market

Leeds received the largest volume of investment for Q1 2020, totalling £69 million. This was composed of multiple deals, including The Embankment, with UKRO (Hong Kong) paying £20.5m for the property.

Cobalt Business Park, Newcastle

CHARLES TOOGOOD
Principal and Managing Director,
National Offices Team

> "Whilst Q1 activity was indicative of strong positive sentiment at the beginning of the year and there are some deals that are in advanced stages, activity will be significantly down over the coming months

Q1 take-up reflects the healthy market pre-Covid-19

The first quarter take-up figures reflect the healthy state of the regional office market before the COVID-19 crisis, where there was pent-up demand from a broad array of sectors and constrained supply. Indeed total take-up across both the city centre and out-of-town markets in the Big Nine amounted to 1.96 million sq ft, 8% below the quarterly average.

There were a number of large deals agreed in Q1, headlined by BT's 283,000 sq ft letting at Three Snowhill in Birmingham and supported by 90,500 sq ft to the Scottish Government in Glasgow and 74,000 sq ft to Osborne Clarke in Bristol. As a result, these cities along with Manchester have performed the strongest with the city centre markets doing particularly well. However with activity skewed towards the larger deals, and deals unsurprisingly slowing towards the end of the quarter, the number of transactions was down on average by 20%.

COVID-19

Whilst Q1 activity was indicative of strong positive sentiment at the beginning of the year and there are some deals that remain in advanced stages, activity will be significantly down over the coming months. The lockdown is not only creating uncertainty around pricing and occupational requirements but significant practical difficulties. Viewings and due diligence cannot be carried out and materials for construction sites and fit-outs are being delayed.

However deals are being dealt with on a case by case basis and while some have been postponed, a number are progressing, including large pre-let deals, while others are taking a 'wait and see' approach. There are examples of Covid-19 clauses being inserted into contracts and occupiers are unlikely to sign leases where there is, or at least was, a need for immediate occupation; acutely aware of significant delays and with little option but to wait.

However we are already starting to see an increase in rent free periods to compensate for those delays to occupiers willing to proceed, and there are a number of examples of landlords being more competitive in order to close out transactions. Prime rents actually increased across four of the Big Nine cities during Q1, leading to a record average rent of £31.61psf, up 4% on a year ago. Of course how long this crisis continues will determine the scale of the recession and the effect on rental values. Nevertheless, the strong fundamentals in many of our markets will likely provide an element of resilience.

The UK office vacancy rate is at its lowest level in fifteen years and well below the long-term average. Additionally, half of the current stock under construction is pre-let and office-to-residential conversions have supported lower supply levels in recent years.

Furthermore, there is a breadth of demand for office space in the Big Nine cities. This was highlighted by the broad mix of sectoral activity during Q1, with a strong showing from the TMT sector, professional & financial services, manufacturing & industry and public services. However, following an almost exponential increase in activity over the past three years, co-working firms were significantly quieter in the first quarter, and have been quick in pulling out of deals since Covid-19.

How the flexible office sector rebounds is still to be played out but Covid-19 presents a longer-term challenge for the traditional office sector. With current working from home arrangements we expect some change in corporate behaviours – potentially fast forwarding a trend of increasingly agile working for a far greater number of businesses. Although its impact could reduce office footprints it will also re-emphasise the value of and importance of the 'office' and likely push landlords, developers and occupiers alike to rethink the importance of the space they occupy.

Before the crisis the Big Nine regional office markets were very well placed, with low vacancy, a number of large requirements and significant pent-up demand. There is more sectoral diversity in the regional markets than there has ever been from companies in tech, media and consumer services. This has been further enhanced by inward investment of companies from the South East to mitigate costs and will be further powered by the GPA Hub programme in the coming years. Whilst, there are more questions around the future of the office market than there were at the end of 2019, the strength and resilience of the Big Nine office markets remains. With vacancy levels at their lowest in fifteen years, the regional markets should be well placed to weather the storm.

TOTAL TAKE-UP IN Q1

1.96 million sq ft

▼ **8%** DOWN ON THE 10 YEAR QUARTERLY AVERAGE

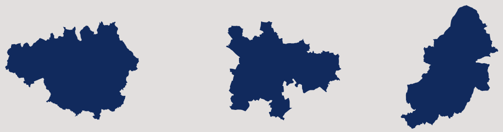
City Centre
1.38 million sq ft

Out-of-town
574,226 sq ft

UNDER CONSTRUCTION

5.1 million sq ft

SKEWED TOWARDS



MANCHESTER	GLASGOW	BIRMINGHAM
29%	22%	15%

HEADLINE RENTS AVERAGE

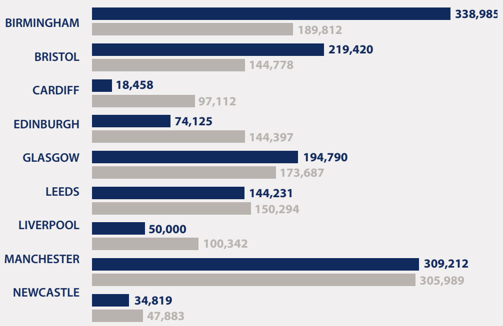
£31.61 psf ACROSS ALL NINE CITIES

City centre

TOTAL TAKE UP IN Q1

1,384,040 sq ft | ▲ **+2%** compared to the ten year quarterly average

TAKE UP (SQ FT)



Q1 2020   10 year quarterly average

TOP FIVE DEALS

City	Property	Occupier	Sq ft
Birmingham	Three Snowhill	British Telecommunications Plc	283,073
Glasgow	220 High Street	Scottish Government	90,528
Bristol	Halo, Finzels Reach	Osborne Clarke	73,991
Manchester	No1 Circle Sq	Hilti	42,559
Manchester	Arndale House	Coop/Marker Study	41,460

HEADLINE RENTS (£PSF)

Location	Rent (£) Q1 2020	Rent free (mths on 10 yr term)	Net effective rent*(£)	Net effective rent (£) Q1 2019
Edinburgh	37.00	15	33.30	30.63
Bristol	35.50	18	31.06	30.63
Glasgow	34.50	15	31.05	28.98
Manchester	36.50	24	30.11	28.88
Birmingham	34.50	24	28.46	27.23
Leeds	32.00	24	26.40	24.75
Cardiff	27.00	12	24.98	24.98
Newcastle	26.00	18	22.75	21.00
Liverpool	21.50	24	17.74	17.74
Average	**31.61**	**19.33**	**27.32**	**26.09**

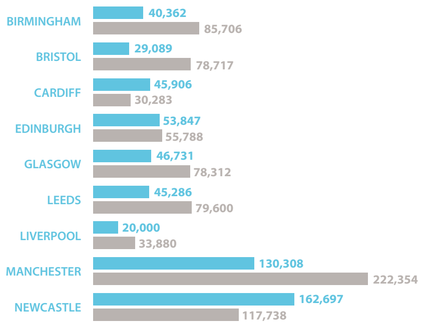
*including rent free period less three month fit-out.

Out-of-town

TOTAL TAKE UP IN Q1

574,226 sq ft | ▼ **-27%** compared to the ten year quarterly average

TAKE UP (SQ FT)



Q1 2020   10 year quarterly average

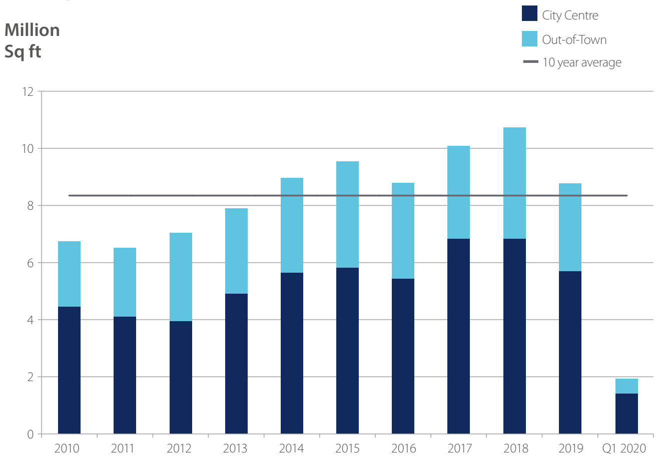
TOP FIVE DEALS

City	Property	Occupier	Sq ft
Newcastle	Spectrum 7. Spectrum BP	Great Annual Savings	47,398
Newcastle	NEON	Verisure	35,000
Manchester	Waterside Court	Hall Analytical	20,000
Manchester	Metro Building	HMCTS	17,700
Glasgow	Hamilton International Technology Park	Belcan	16,013

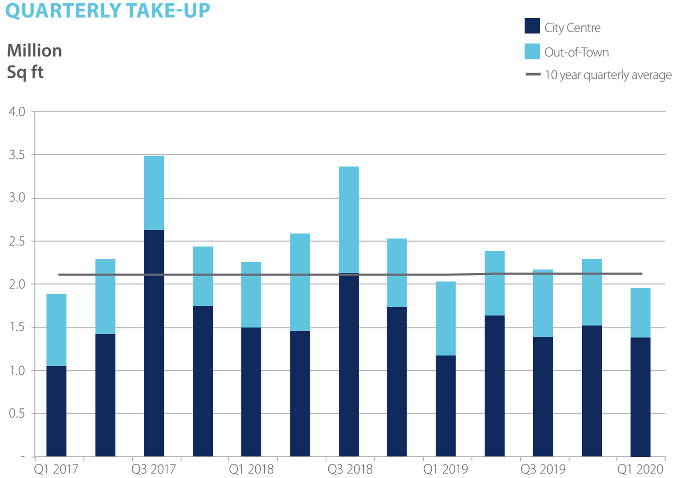
HEADLINE RENTS (£PSF)

Location	Rent (£) Q1 2020	Rent (£) Q1 2019
Birmingham	26.00	25.00
Leeds	24.75	24.75
Manchester	24.00	22.00
Bristol	23.50	23.50
Edinburgh	22.00	22.00
Newcastle	16.95	16.95
Glasgow	16.50	16.50
Cardiff	15.00	15.00
Liverpool	14.00	14.00
Average	**20.30**	**19.97**

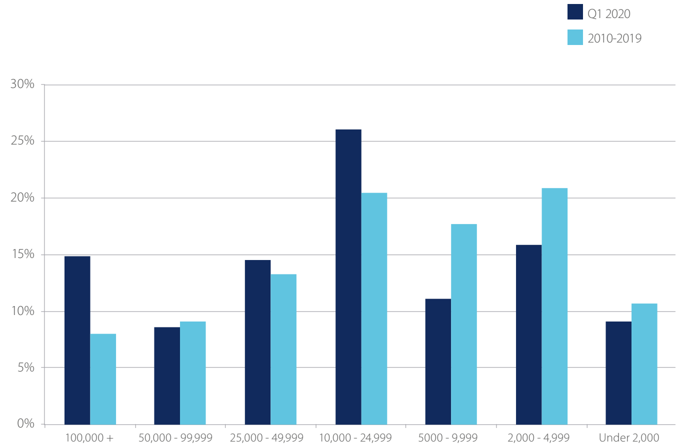
TAKE-UP



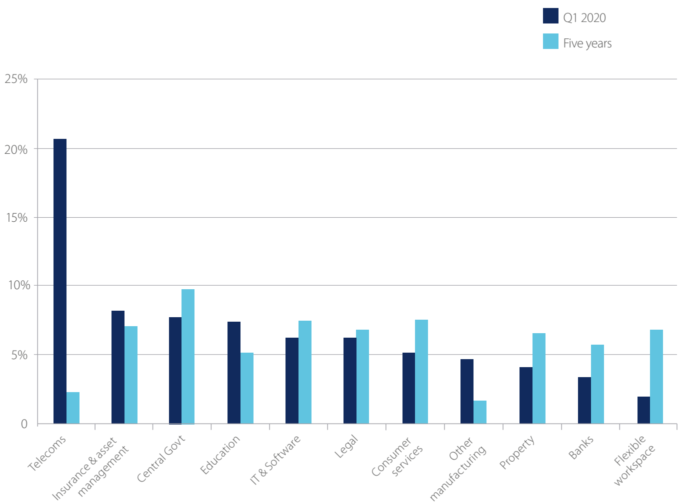
QUARTERLY TAKE-UP



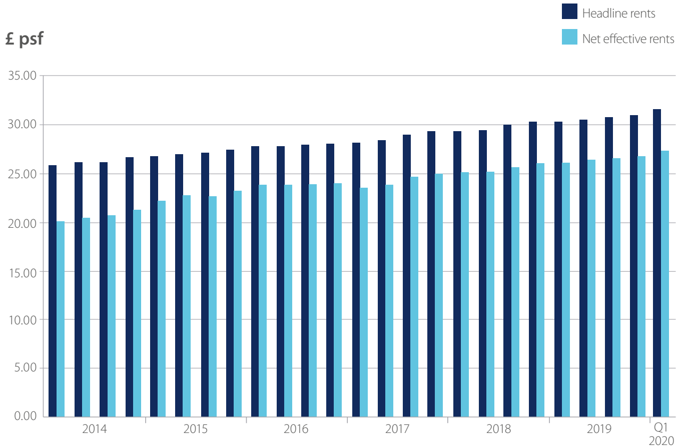
TAKE-UP BY SIZE BAND



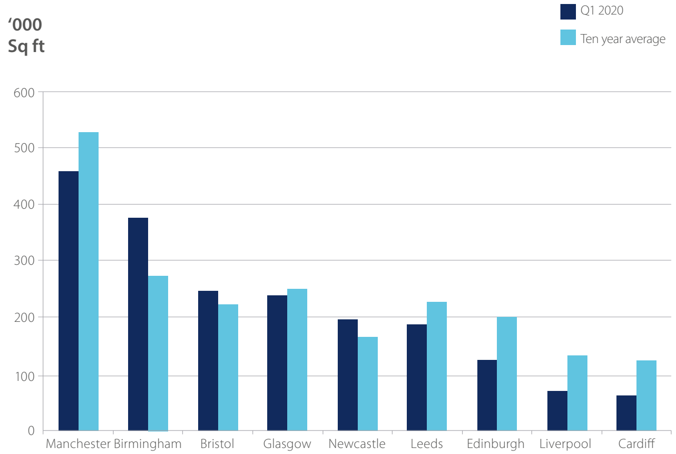
TAKE-UP BY KEY SECTORS



HEADLINE RENTS



CC AND OOT TAKE-UP



Birmingham

Take-up activity amounted to 339,000 sq ft in Birmingham city centre during Q1, the highest Q1 figure ever recorded.

BT Group signed the largest ever deal in Birmingham at the beginning of January, 283,000 sq ft at the recently completed 410,000 sq ft Three Snowhill. Deals were otherwise muted given the sentiment lag effect caused by the Brexit negotiations during H2 2019. The largest deal was 20,000 sq ft to Somerville House Ltd at 49 Calthorpe Road.

Occupier sentiment was showing strong signs of improvement during Q1, with enquiry levels up and healthy viewing activity across-the-board, helped by two or three large prospective inward investment enquires including Goldman Sachs. However, enquiry levels have tailed off significantly at the beginning of Q2 due to COVID-19. Whilst a few deals have collapsed, most lease completions have been delayed with occupiers reluctant to commit to space when social distancing measures are delaying tenants' beneficial occupation of accommodation.

Three significant office schemes are completing in Birmingham. Argent's 2 Chamberlain Square reached practical completion in March. The 167,000 sq ft building has been let in part, 40,000 sq ft to DLA – with strong interest in four of the remaining five floors and where solicitors have been instructed on part. A further 120,000 sq ft is available at Three Snowhill which remains the city's biggest ever speculative office building and Three Arena Central, where HMRC agreed a 240,000 sq ft pre-let will complete later this quarter.

Peak headline rents remain at £34.50 psf but other deals in lawyers' hands are showing further rental growth. Inducements currently remain flat at 24 months for a 10 year lease commitment.

KEY DEALS - Q1 2020

Property	CC / OOT	Sq ft	Occupier
Three Snowhill	CC	283,073	British Telecommunications Plc
49 Calthorpe Road	CC	19,881	Somerville House Ltd
Cogen Court, Solihull	OOT	11,219	MV Kelly
No. 1 Colmore Square	CC	8,093	Reed Specialise Recruitment
Hedera Road, Redditch	OOT	7,825	Bio Care

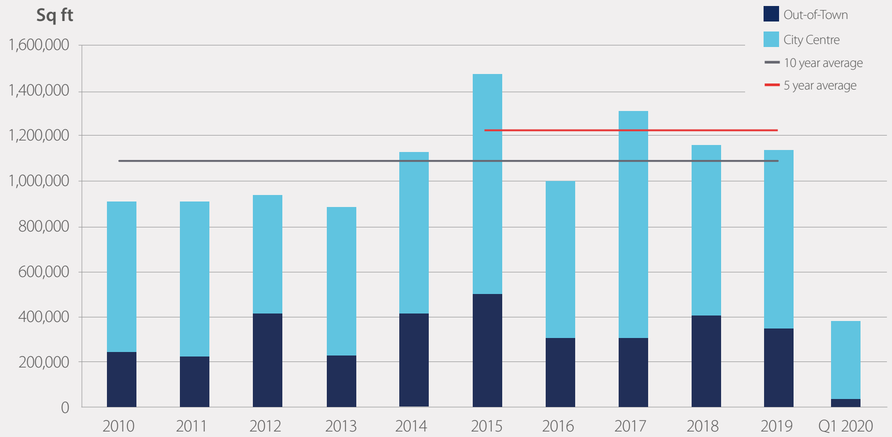
KEY SECTOR ACTIVITY FOR 12 MONTHS TO Q1 2020

Telecommunications
29%

Flexible workspace
24%

Advanced manufacturing
16%

TAKE-UP



Q1 TAKE-UP

City Centre
338,985 sq ft

Out-of-town
40,362 sq ft

HEADLINE RENT

City Centre
£34.50 per sq ft

Out-of-town
£26 per sq ft

UNDER CONSTRUCTION

748,000 sq ft

32%
prelet

PRIME YIELD

5.00%

Bristol

Take-up activity in the city centre market was strong during Q1, amounting to 219,000 sq ft, 52% above the quarterly average. This figure was headlined by the 74,000 sq ft pre-let to lawyers Osborne Clarke at 110,000 sq ft Halo, Finzels Reach.

Professional and financial services sectors accounted for the top five deals, with Sanlam Life & Pensions taking the largest standing stock transaction of 20,365 sq ft at One Temple Quay. There were four further deals greater than 10,000 sq ft, including engineering company WSP and lawyers Ashfords. The latest deals have moved headline rents to £35.50 psf and asking rents to £37.50 psf.

Occupiers are still trying to progress requirements that are well established. Restrictions on viewings and fit-out have slowed more recent enquiries but there remain some sizeable requirements such as 40,000 sq ft for Marsh & McLennan.

In the current circumstances demand in the flexible office market remains uncertain, although take-up in the sector has been relatively subdued in Bristol compared to some other regional markets, amounting to just over 200,000 sq ft during the past three years.

There are three speculative buildings under construction in Bristol, totalling 237,000 sq ft, of which circa 65% remains available. In addition to Halo these include all of the 93,000 sq ft Distillery at Glassfields, and the majority of 34,000 sq ft 1 Portwall Square by Nord Development. Melburg and Angelo Gordon have received planning consent for their planned refurbishment of the 110,000 sq ft South Plaza, which will include rebranding it as '360 Bristol'.

Conversely the out-of-town market had a subdued quarter, with a total of 29,000 sq ft transacted. On the supply side, at 800 Aztec West the MoD have vacated 32,000 sq ft of surplus accommodation which is being marketed by way of a lease assignment, or a new sub-lease at a quoting rent of £22.50 psf.

CEG are on site with the refurbishment of 1000 Aztec West, which will include the addition of an extra floor and extending the building, taking the NIA from 40,000 sq ft to 84,000 sq ft.

KEY DEALS - Q1 2020

Property	CC / OOT	Sq ft	Occupier
Halo, Finzels Reach	CC	73,991	Osborne Clarke
One Temple Quay	CC	20,365	Sanlam Life & Pensions Ltd
Programme	CC	16,377	NMI / Call Credit UK Ltd
Kings Orchard	CC	15,250	WSP
Tower Wharf	CC	13,613	Ashfords

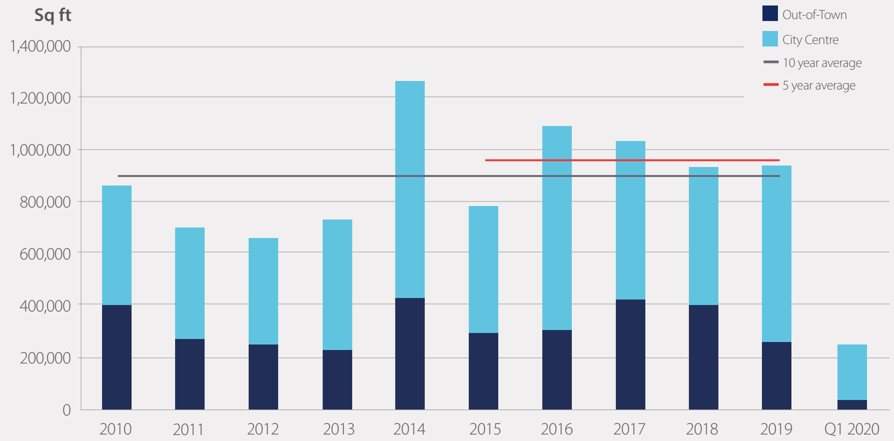
KEY SECTOR ACTIVITY FOR 12 MONTHS TO Q1 2020

Telecommunications 28%

Flexible workspace 16%

Legal 12%

TAKE-UP



Q1 TAKE-UP

City Centre **219,420 sq ft**

Out-of-town **29,089 sq ft**

HEADLINE RENT

City Centre **£35.50 per sq ft**

Out-of-town **£23.50 per sq ft**

UNDER CONSTRUCTION

437,000 sq ft

65% prelet

PRIME YIELD

5.00%

Cardiff

Office transactional activity in Cardiff has continued at the same subdued level seen in 2019, with total take-up of 64,000 sq ft, half the ten year quarterly average. However it was an encouraging quarter for the out-of-town market, which dominated activity.

There were three out-of-town deals more than 10,000 sq ft. The largest deal was to Bobath Children's Therapy Centre which took 13,500 sq ft at The Courtyards in Llanishen. On Eastern Business Park, St Mellons, financial services company Target Group took 12,300 sq ft and at Caxton House, electronics manufacturer Flintec took 12,000 sq ft. All other deals were below 5,000 sq ft, including those in the city centre.

The level of office availability has steadily declined in recent years, as much of the secondary stock has been converted to student accommodation. This is a healthy situation for the development market which continues to see considerable activity. JR Smart's 109,000 sq ft development at St John's street is under construction and demolition works at Central Quay are being carried out in preparation for 220,000 sq ft Ledger Building. In the refurbishment market 65,000 sq ft Fusion Point One on Dumballs Road is due to complete later this year.

KEY DEALS - Q1 2020

Property	CC / OOT	Sq ft	Occupier
1 The Courtyards, Llanishen	OOT	13,500	Bobath
Building 3, Eastern Business Park	OOT	12,300	Target Group
Caxton House	OOT	12,072	Flintec
Abacus House, Pentwyn	OOT	3,585	OCS
Market Buildings	CC	3,092	South Wales Police and Crime Commissioner

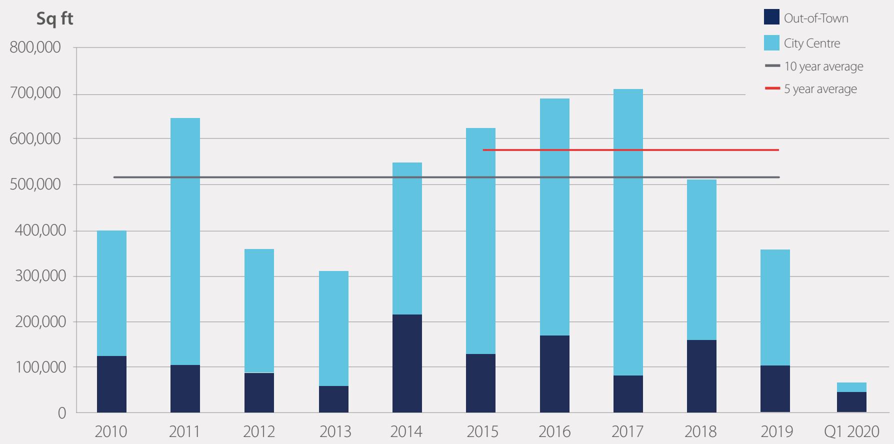
KEY SECTOR ACTIVITY FOR 12 MONTHS TO Q1 2020

Financial Services **35%**

Advanced manufacturing **14%**

IT & software **10%**

TAKE-UP



Q1 TAKE-UP

City Centre **18,458 sq ft**

Out-of-town **45,906 sq ft**

HEADLINE RENT

City Centre **£27 per sq ft**

Out-of-town **£15 per sq ft**

UNDER CONSTRUCTION

379,000 sq ft

71% prelet

PRIME YIELD

5.75%

Edinburgh

Take-up activity in the Edinburgh office market showed resilience during Q1 totalling 128,000 sq ft, headlined by two city centre deals, 16,100 sq ft to the Financial Conduct Authority at Quayside House and 14,600 sq ft to Smartsheet at Quartermile 3. In addition, a new city centre headline rent of £37 psf was achieved on the top floor of 40 Princes Street by investment company Cadence. Otherwise there was a good amount of activity in the sub 5,000 sq ft market in the city centre where there continues to be strong occupational demand.

54,000 sq ft of take-up in the out-of-town market was in line with the average, with key medium sized deals at Shawfair Business Park, the Curve at Heriot Watt and Scott House rather than on Edinburgh Park or South Gyle, highlighting the strength and versatility of the West Edinburgh office market.

The city centre saw 38,000 sq ft of lease re-gears in addition to 74,000 sq of office take up. It is expected that the ongoing trend for lease re-gears will continue with many occupiers wishing to extend their current occupation amidst the current backdrop.

The level of development and refurbishment activity has increased in Edinburgh. There is considerable interest in 380,000 sq ft M&G and QMile Group's 'The Haymarket', 110,000 sq ft of which is under construction and 270,000 sq ft in phase 2. Other city centre schemes include Vastint's New Fountainbridge scheme, 2 Freers Street and Capital Square.

In the out-of-town market 85,000 sq ft 1 New Park Square on Edinburgh Park is under construction by developer Parabola and due to complete next year. In addition, comprehensive refurbishments are being carried out on Knight Property Group's recently purchased 41,000 sq ft 4/5 Lochside Avenue and CEG's 68,000 sq ft Haston House in West Edinburgh.

KEY DEALS - Q1 2020

Property	CC / OOT	Sq ft	Occupier
Shawfair Business Park	OOT	17,599	Peoples Energy
Quayside House	CC	16,128	FCA
Quartermile 3, 10 Nightingale Way	CC	14,641	Smartsheet
The Curve, Heriot Watt	OOT	13,197	Fugro GB Marine Ltd
40 Princes Street	CC	8,494	Cadence

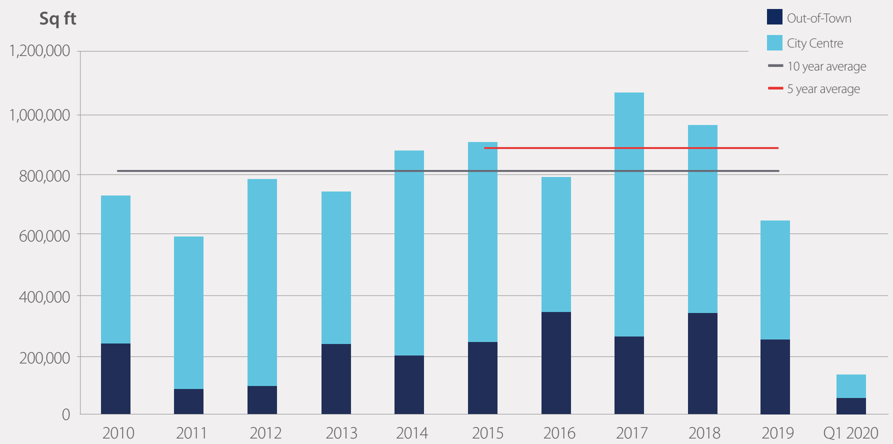
KEY SECTOR ACTIVITY FOR 12 MONTHS TO Q1 2020

Flexible workspace **24%**

Health & social care **18%**

IT & software **13%**

TAKE-UP



Q1 TAKE-UP

City Centre **74,125 sq ft**

Out-of-town **53,847 sq ft**

HEADLINE RENT

City Centre **£37 per sq ft**

Out-of-town **£22 per sq ft**

UNDER CONSTRUCTION

291,913 sq ft

23% prelet

PRIME YIELD

5.00%

Glasgow

The Glasgow office market saw a positive start to the year, with impressive Q1 take-up figures. The key deal of the quarter and the second largest across the Big Nine was the sub-letting of 90,500 sq ft to the Scottish Government for the new Social Security Scotland agency at 220 High Street.

The public sector also accounted for the next largest deal, 27,000 sq ft at 11 George Square and significant activity in the financial services sector continues with the 18,200 sq ft letting to insurance company Sedgwick International UK at Sentinel, 103 Waterloo Street. The level of activity means that prime headline rents have increased from £32.50 psf to £34.50 psf during Q1.

With enquiry levels falling back since the crisis, we expect there to be a low level of activity over the next six months. However some advanced deals in solicitors' hands are proceeding and there are some large pre-let requirements still showing an interest in transacting, taking a 'wait and see' approach', which in the current circumstances is a positive sign. The three speculative schemes under construction and able to accommodate larger pre-lets are due to complete during the next 12 months. These include 97,000 sq ft at 2 Atlantic Square, 94,000 sq ft at Cadworks and 77,000 sq ft remaining at the 300,000 sq ft 177 Bothwell Street.

The out-of-town market was relatively quiet, led by a 16,000 sq ft transaction at Hamilton International Business Park to engineering consultancy Belcan and 10,000 sq ft to Aggregate Land at Trilogy Business Park, Eurocentral.

KEY DEALS - Q1 2020

Property	CC / OOT	Sq ft	Occupier
220 High Street	CC	90,528	Scottish Government
Monteith House, 11 George Square	CC	27,000	Public sector
Sentinel, 103 Waterloo Street	CC	18,268	Sedgwick International UK
Hamilton International Technology Park	OOT	16,013	Belcan
Trilogy One	OOT	10,540	Aggregate Land

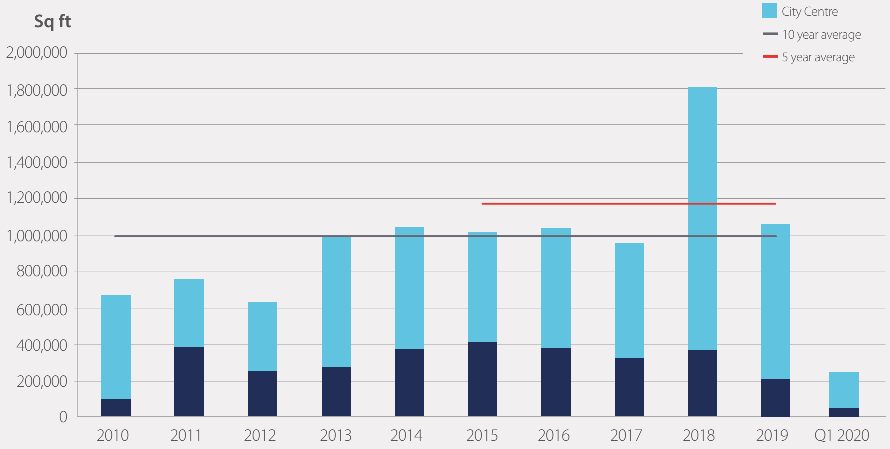
KEY SECTOR ACTIVITY FOR 12 MONTHS TO Q1 2020

Financial Services
44%

Public Services
14%

IT & software
13%

TAKE-UP



Q1 TAKE-UP

City Centre
194,790 sq ft

Out-of-town
46,731 sq ft

HEADLINE RENT

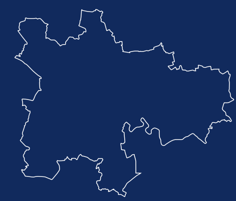
City Centre
£34.50 per sq ft

Out-of-town
£16.50 per sq ft

UNDER CONSTRUCTION

1.15 million sq ft

77%
prelet



PRIME YIELD

5.00%

Leeds

The Q1 take-up figures reflect the strong demand for space in Leeds city centre pre-COVID-19 and continues the robust level of take-up activity seen during 2019. A handful of deals between 10,000 sq ft and 30,000 sq ft raised activity in Leeds city centre to 144,000 sq ft, just above the long term average.

The largest deal of the quarter was a 31,000 sq ft freehold purchase of Cloth Hall Court by Leeds University. Other key deals included 22,000 sq ft to tech design company TTEC at West Gate and 16,600 sq ft to engineering company JN Bentley at King Street.

A new headline rent of £32 psf has been achieved in the city centre as recruitment company Charlton Morris leased 10,000 sq ft at the recently refurbished 34 Boar Lane. The highest quoting rent is for the remaining space at another recent refurbishment, the former Majestic cinema at £34 psf.

All construction activity is at Wellington Place. The speculative developments at 11 and 12 Wellington Place, totalling 245,000 sq ft, are due to complete next year and currently have all space still available. Pre-let 7&8 Wellington Place (378,000 sq ft) has recently completed and 4 Wellington Place (134,000 sq ft) is due to complete this year.

A more subdued out-of-town market consisted of 22 deals, all below 5,000 sq ft apart from the largest, 11,750 sq ft to a confidential owner-occupier at Springwood House, Horsforth. Kirkstall Forge, Thorpe Park and Pavillion Business Park were all active with the smaller deals.

KEY DEALS - Q1 2020

Property	CC / OOT	Sq ft	Occupier
Cloth Hall Court	CC	31,389	Leeds University
West Gate	CC	22,367	TTEC
Bank House, King Street	CC	16,671	JN Bentley
1 The Embankment	CC	15,799	Interactive Investor
Springwood House, Horsforth	OOT	11,750	Confidential purchaser

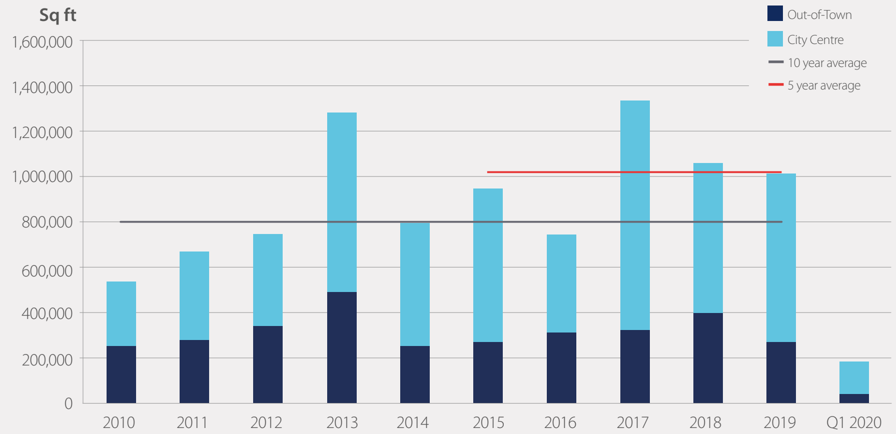
KEY SECTOR ACTIVITY FOR 12 MONTHS TO Q1 2020

Consumer services 27%

Media 16%

IT & software 13%

TAKE-UP



Q1 TAKE-UP

City Centre
144,231 sq ft

Out-of-town
45,286 sq ft

HEADLINE RENT

City Centre
£32 per sq ft

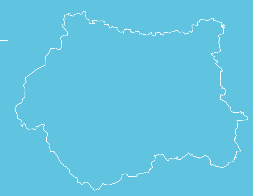
Out-of-town
£24.75 per sq ft

UNDER CONSTRUCTION

378,879 sq ft
35%
prelet

PRIME YIELD

5.00 %



Liverpool

In the first quarter of 2020, total take-up across Liverpool's office market amounted to 70,000 sq ft, half the ten year average.

Leasing activity was generally focused in the city centre, which accounted for 70% of the total. There were only two transactions more than 10,000 sq ft in Q1, 16,017 sq ft to lawyers Carpenters at No 1 Tithebarn and Plus Dane Group took 15,000 sq ft at Atlantic Pavillion.

The majority of Q1 deals took place during the first two months of the year when occupier sentiment was more positive and there were a healthy number of large requirements in excess of 10,000 sq ft. These included BT (100,000 sq ft), MAERSK (15,000 sq ft) and Firesprite (20,000 sq ft), all of whom were actively seeking to acquire space either on a pre-let basis or during the latter part of this year.

However, occupier activity declined towards the end of the quarter. Covid-19 has had a significant impact on the Liverpool market, with mobility restrictions and economic uncertainty severely constricting demand, as many occupiers have adopted a 'wait and see' approach. This is likely to have a huge impact on Q2 and Q3 take-up figures.

Supply is still one of the biggest challenges in the market in both the city centre and out-of-town locations and is currently at its lowest level in 20 years. Much of this space is of poor quality and there are only a handful of buildings that are able to provide good quality space across both markets. The only building which is currently under construction is the The Spine at Paddington Village (160,000 sq ft), which is due to complete in late autumn.

KEY RECENT DEALS

Property	CC / OOT	Sq ft	Occupier
The Plaza	CC	39,688	Instant Offices
Daresbury Park 2100	OOT	27,212	Greensill
No 1 Tithebarn	CC	18,473	Disclosure & Barring Services
No 1 Tithebarn	CC	16,017	Carpenters
Atlantic Pavillion	CC	15,000	Dane Group

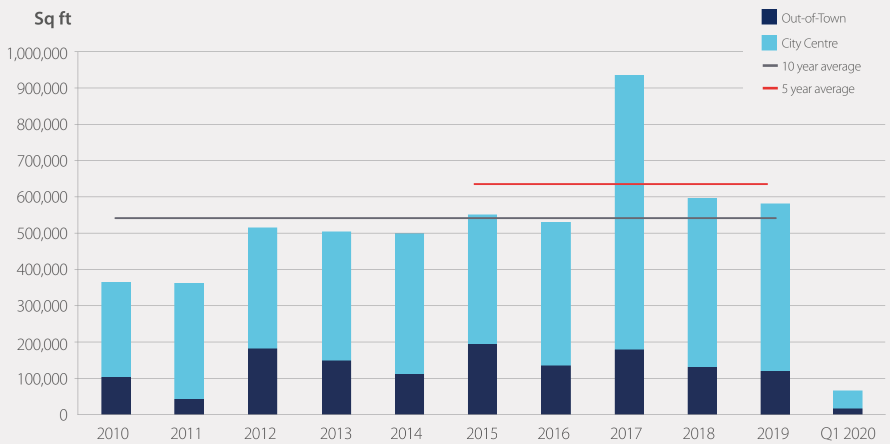
KEY SECTOR ACTIVITY FOR 12 MONTHS TO Q1 2020

Property **21%**

Media **17%**

Financial Services **16%**

TAKE-UP



Q1 TAKE-UP

City Centre **50,000 sq ft**

Out-of-town **20,000 sq ft**

HEADLINE RENT

City Centre **£21.50 per sq ft**

Out-of-town **£14 per sq ft**

UNDER CONSTRUCTION

160,000 sq ft

44% prelet

PRIME YIELD

6.00%

Manchester

Manchester city centre office take-up amounted to 309,000 sq ft during Q1, in line with the ten year quarterly average. Among this was a broad mix of sectoral activity across professional & financial services, manufacturing & industry and the TMT sector.

The largest deal was a 42,000 sq ft pre-let to manufacturer Hilti at No 1 Circle Square, which is due to complete later in the year. Another recent development, Windmill Green, which completed in 2018 also secured notable lettings including 27,000 sq ft to co-working company Hana. Other deals included 41,500 sq ft to CoOp / Marker Study at Arndale House and 25,000 sq ft to Bet 365 at Core. This positive start to the year pre-crisis was supported by a very healthy level of requirements to occupiers such as Grant Thornton, Deloitte, HSBC and others.

There is 1.5 million sq ft of space under construction in Manchester city centre. The largest developments with the majority of space still available include 2 Circle Square (230,000 sq ft), 100 Embankment (166,000 sq ft) and 180,000 sq ft Landmark Oxford Rd, which has recently completed.

The out-of-town market saw 130,308 sq ft of take-up. This included five deals of more than 10,000 sq ft, the largest of which was 20,000 sq ft to Hall Analytical. Bibby Financial Services and HMCTS were also among the larger occupiers.

KEY DEALS - Q1 2020

Property	CC / OOT	Sq ft	Occupier
No1 Circle Sq	CC	42,559	Hilti
Arndale House	CC	41,460	Coop/Marker Study
Windmill Green	CC	26,888	Hana
Core	CC	25,029	Bet 365
Waterside Court	OOT	20,000	Hall Analytical

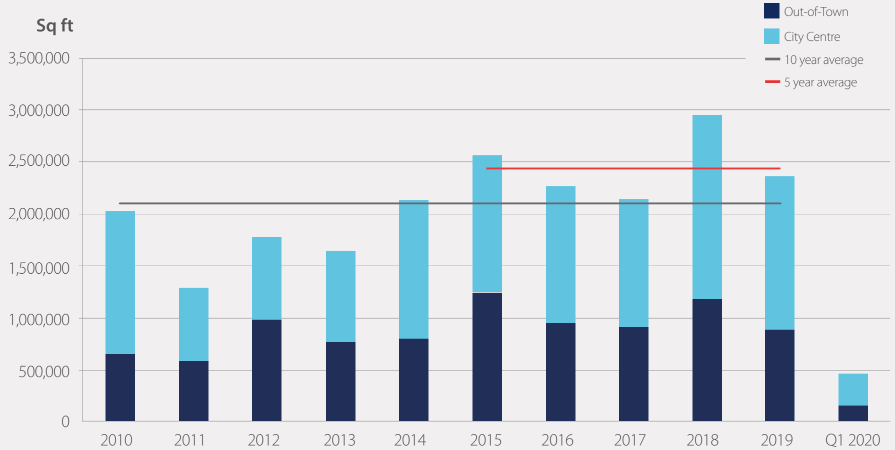
KEY SECTOR ACTIVITY FOR 12 MONTHS TO Q1 2020

Flexible workspace 16%

IT & software 11%

Legal 9%

TAKE-UP



Q1 TAKE-UP

City Centre
309,212 sq ft

Out-of-town
130,308 sq ft

HEADLINE RENT

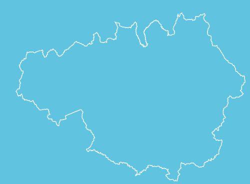
City Centre
£36.50 per sq ft

Out-of-town
£24 per sq ft

UNDER CONSTRUCTION

1.47 million sq ft

46%
prelet



PRIME YIELD

5.00%

Newcastle

Total take-up in the Newcastle office market achieved 197,500 sq ft for the first quarter of 2020, 18% up on the 10 year average. The out-of-town market dominated Q1's take-up, accounting for 163,000 sq ft, 82% of the total.

The two largest transactions of the quarter were located in the out-of-town market, with 47,000 sq ft at Spectrum Business Park being leased to business services company Great Annual Savings, and 35,000 sq ft at Neon, leased to Verisure. Elsewhere the recently completed Beam in Sunderland has signed software company, Asset 55 to 11,000 sq ft.

Q1 take-up and advanced deals in the pipeline in Newcastle have been very encouraging. There are a number of well advanced deals in solicitors' hands in both the city centre and out-of-town markets and most are expected to complete, particularly where occupiers need to be out of their existing building. However less advanced deals and recent enquiries will be slowed down, with viewings and fit-outs unable to be carried out.

There is considerable interest in the two city centre office buildings. The 106,000 sq ft Lumen office building completed in March and the next phase of the scheme, 107,000 sq ft The Spark is expected to complete in 2021.

KEY DEALS - Q1 2020

Property	CC / OOT	Sq ft	Occupier
Spectrum 7, Spectrum BP	OOT	47,398	Great Annual Savings
NEON	OOT	35,000	Verisure
Baltic Place	CC	10,933	Cambridge assessments
The Beam, Sunderland	OOT	10,881	Asset 55
Jam Jar Studios, Gateshead	OOT	10,120	What Culture

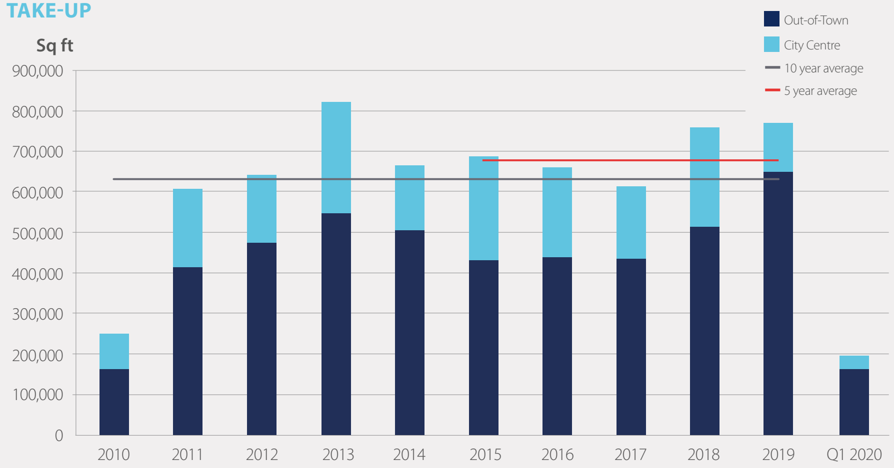
KEY SECTOR ACTIVITY FOR 12 MONTHS TO Q1 2020

IT & software **42%**

Financial Services **12%**

Property **9%**

TAKE-UP



Q1 TAKE-UP

City Centre **34,819 sq ft**

Out-of-town **162,697 sq ft**

HEADLINE RENT

City Centre **£26 per sq ft**

Out-of-town **£16.95 per sq ft**

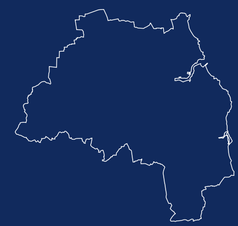
UNDER CONSTRUCTION

107,000 sq ft

0% prelet

PRIME YIELD

6.00%



MARK WILLIAMS
Principal and Managing Director,
Regional Investment

> "Although all investors are more cautious there is evidence of increased interest from overseas buyers attracted by long-lease properties, made more attractive by the weaker pound relative to other currencies.

Q1 slowdown in investment activity

Unlike the occupier market, investment volumes for Q1 reflect a sharp slowdown in activity. The first quarter of 2020 saw just £226 million transact across the Big Nine cities, similar to the level of activity during Q1 last year but well down on the quarterly average of £561 million.

Leeds received the largest volume of investment for Q1 2020, totalling £69 million. This was composed of multiple deals, including The Embankment, with UKRO (Hong Kong) paying £20.5m for the property. Liverpool attracted the next largest investment volume for the period, achieving £40m solely from the sale of the largest transaction of the quarter of 20 Chapel Street to Square Ape Ltd; followed by Newcastle's £26.3m sale of the fully-let Cobalt 23 by Moorfield and Highbury Properties to LCN Capital Partners.

REACTION TO COVID-19

Since lockdown, the overriding theme is of a pause in the market. The vast majority of deals have slowed as investors and vendors alike take a view of the 'new normal', with a number of investors citing additional time required to assess tenant defaults and price movement, in addition to the added logistical difficulties in completing due diligence at this time.

We saw a number of deals exchange or complete in March, and believe that there has been limited movement on pricing on those deals. Furthermore, there are a number of examples of deals progressing as business as usual, which is reassuring. However there have been examples of deals falling through with investors taking a view on pricing post-crisis. A number of investors, including funds, have paused completely and there is inevitably little new investment stock coming to the open market, with examples of properties and portfolios being withdrawn.

OVERSEAS BUYERS SHOWING INTEREST

Although all investors are more cautious there is evidence of increased interest from overseas buyers attracted by long-lease properties, made more attractive by the weaker pound relative to other currencies. Overseas investors contributed 42% of the total investment volume for Q1 2020, which included the two largest deals of the quarter, while few UK institutions engaged with large-scale investments. We are seeing more interest from cash buyers in the market but it may be too early for substantial pressure from banks or investors to undertake distress sales.

Cash reserves were being bolstered during 2019 in anticipation of fallout from political and economic uncertainty related to Brexit, and it is now likely that these will be held for longer still to help defend against COVID-19's impact on the economy. There is the potential for those who weather the storm to drive a post-crisis surge in transactional activity as restrictions are relaxed from both overseas and UK institutional investors.

LONG INCOME HOLDING UP

In times of uncertainty the most likely sales to be proceeding or going under offer are long income deals with strongest covenants. Long income transactions are generally progressing but there are limited new deals coming through. Due to volatility in bond rates and economic stress there was initial movement on some commercial covenants, however these have recently improved.

BANKS AND CLAUSES

There are now numerous examples of requests for COVID uncertainty clauses being inserted into contracts to remove liability in case a deal does not complete on time post-exchange. Interestingly these uncertainty clauses are not preventing lending with increased scrutiny on lease lengths and security. Nevertheless, bank lending continues to be restricted at this time as resource is allocated towards mitigating existing risk.

YIELD MOVEMENT

The consensus view is that the industry will not be making significant value adjustment at the March quarter date due to lack of information, and the uncertainty in the market, with the uncertainty clause in valuations being a clear and obvious example. At the end of March, prime yields averaged 5.31% across the Big Nine cities, unchanged from Q4 2019. However, we expect this figure to move out over the next quarter as pricing is reviewed and a further bank of evidence is established. This movement has just started to register on the MSCI monthly index, recording regional office equivalent yields of 7.08% in March 2020, compared to 7.03% in February.

TOTAL FOR Q1

£226 million

▼ **60%**

DOWN ON THE 10 YEAR QUARTERLY AVERAGE

VOLUMES BY CITY

LEEDS	LIVERPOOL	BIRMINGHAM
£69m	£44m	£41m

VOLUMES BY INVESTOR TYPE

UK PROPERTY COMPANY	OVERSEAS INVESTOR	UK INSTITUTION
46%	42%	8%

PRIME YIELD	PREVIOUS PEAK (2007)
5.00%	4.50%

Occupier market | Occupier data | Occupier charts | Investment market | Investment data | Investment data | Lease Advisory | Contact

Birmingham | Bristol | Cardiff | Edinburgh | Glasgow | Leeds | Liverpool | Manchester | Newcastle

TOTAL INVESTMENT VOLUMES IN Q1 2020

£226 million

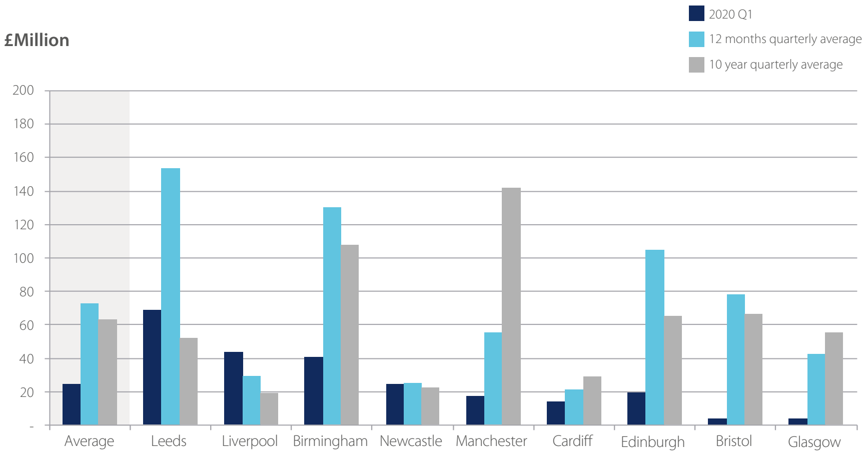
Compared to:

£640m (previous quarter – Q4 2019)

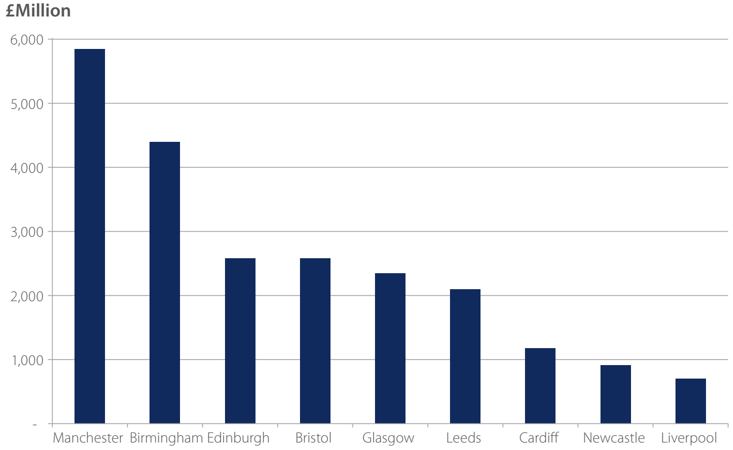
£291m (a year ago – Q1 2019)

£561m (ten year quarterly average)

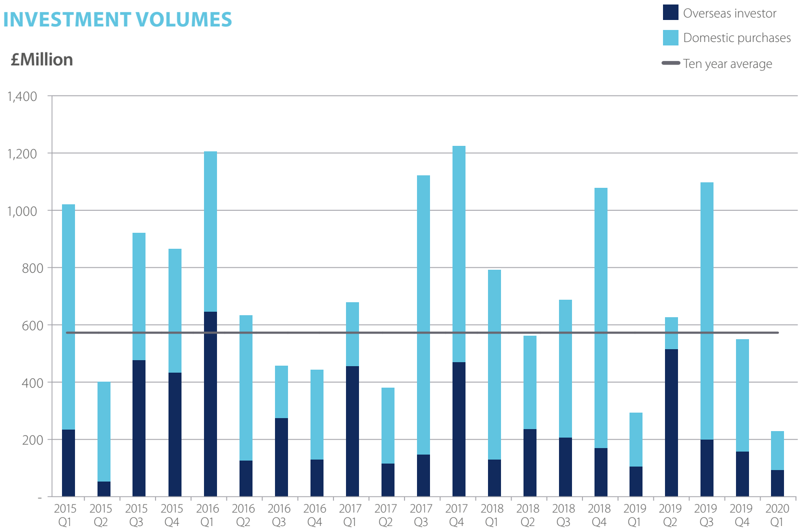
INVESTMENT VOLUMES



INVESTMENT VOLUMES 2010 TO 2019



INVESTMENT VOLUMES



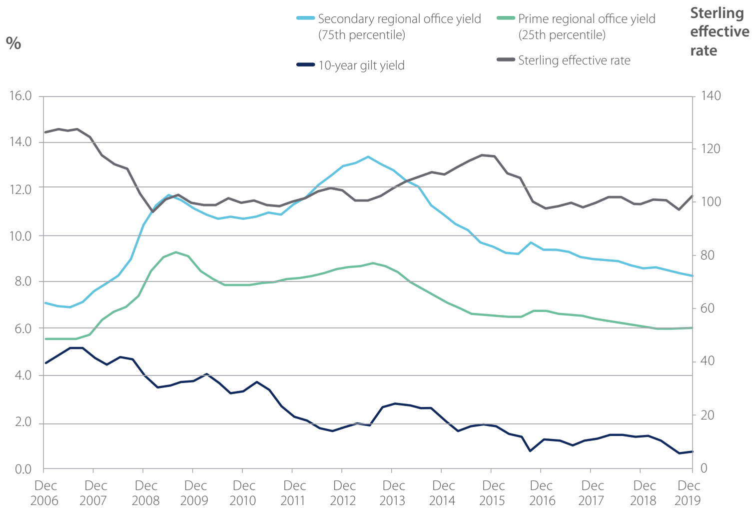
TOP FIVE DEALS – Q1 2020

Date	Property	City	Purchaser	Vendor	Price (£m)	NIY (%)
Mar-20	Chapel Street, 20	Liverpool	Square Ape Ltd	Canmoor Asset Management	40	6.30
Mar-20	Cobalt 23	Newcastle-upon-Tyne	LCN Capital Partners	Moorfield REF IV LP	26.3	6.60
Mar-20	Yorkshire House / The Hub	Leeds	Castleforge Partners	FORE Partnership	22.15	4.90
Feb-20	The Embankment, 3-4	Leeds	UKRO (Hong Kong)	XLB Property	20.5	6.78
Feb-20	Broad Street, 111	Birmingham	Taylor Grange Development	Freshwater Group	15	N/A

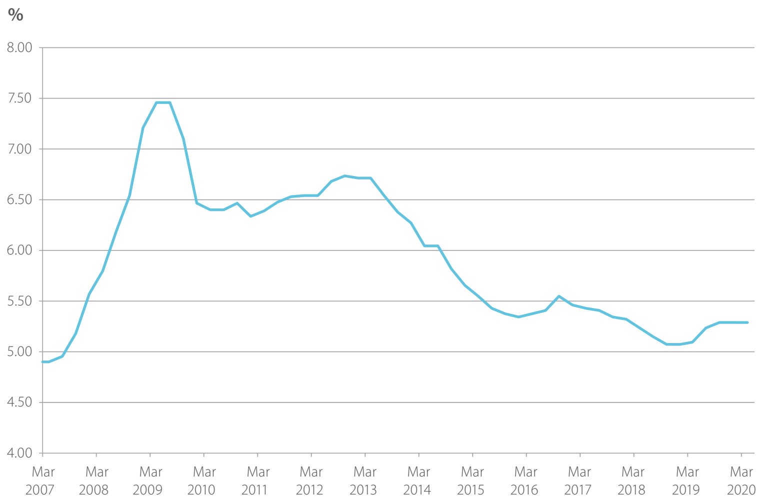
PRIME CITY CENTRE YIELDS

Location	Q4 2019	Q1 2020	Trend for last 12 months	Peak (2007)
Birmingham	5.00	5.00	↑	4.50
Bristol	5.00	5.00	↑	5.00
Cardiff	5.75	5.75	↑	5.00
Edinburgh	5.00	5.00	↑	4.75
Glasgow	5.00	5.00	→	4.75
Leeds	5.00	5.00	↑	4.75
Liverpool	6.00	6.00	↑	5.50
Manchester	5.00	5.00	↑	4.50
Newcastle	6.00	6.00	↑	5.25

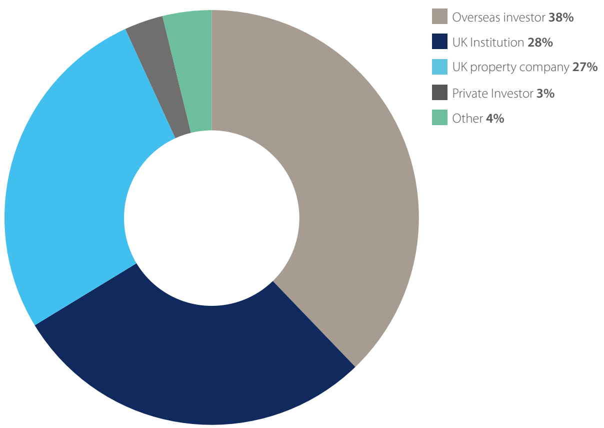
REGIONAL OFFICE YIELDS VS 10 YEAR GILTS



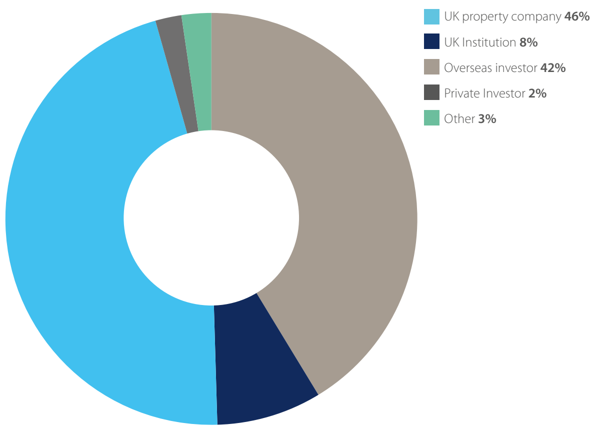
AVERAGE BIG NINE PRIME YIELD



INVESTOR VOLUMES BY PURCHASER TYPE 12 MONTHS TO Q1 2020



INVESTOR VOLUMES BY VENDOR TYPE Q1 2020



> “Overseas investors contributed 42% of the total investment volume for Q1 2020, which included the two largest deals of the quarter, while few UK institutions engaged with large-scale investments

Covid-19: a conundrum for UK lease renewals

COVID-19 has considerably impacted on what was previously a functioning office market and is now challenging the inner workings of Part II of the Landlord and Tenant Act (LTA) 1954, for commercial leases in England and Wales. In Scotland the renewal process is primarily based around negotiation, where the tenant has very limited renewal rights.

In the office market, some transactions have continued to move towards completion, but in many cases, lettings have been halted – at least temporarily – either because of practical difficulties in completing them, or because the business outlook for at least one of the parties has changed materially. Across the market as a whole, the number of transactions has reduced and is likely to reduce further over the coming months (particularly as very few new transactions are currently being initiated). For leases expiring during this period – or indeed for any outstanding renewal that has yet to be resolved - this has multiple implications.

The lease advisory specialists are used to dealing with periods where the number of transactions, and thus the amount of "comparable evidence", is lower than usual. Rarely do we see situations where the entire market slows as significantly as at present. Current circumstances pose two fundamental challenges to the lease renewal process.

1. Many tenants can legitimately argue that they have no idea what length of lease they can commit to under current conditions. The business environment is so challenging, that they cannot guarantee the future existence of their business.

2. There is minimal evidence of the appropriate market rent for most leases, given the dramatic change in trading conditions and business outlook for most markets and sectors. Arguably, at the time of writing, a large proportion of offices have been forced to close which would potentially lead to arguments regarding the rental levels being reduced significantly during this period.

A state of limbo …?
Under the circumstances, it is difficult to see how negotiations can proceed when there is so little evidence available upon which to base a judgement. However, it is important to remember that all such negotiations are, to a large degree, voluntary. Each party can fall back on its contractual and legal rights, adopting the 1954 Act renewal process for properties in England and Wales – but there are also commercial considerations to take into account.

Most landlords would ideally wish to suspend negotiations for as long as possible given weak market conditions, preferring to wait for a stronger market before agreeing to a new lease. Tenants holding over on an expired lease contractually should be paying their previous rent; but they are under no obligation to renew and in a weakening market they will have an increasing range of relocation or rationalisation options to reduce costs. Better to lock a footloose tenant in now – especially if they are a viable business – than risk losing them to a competing property?

As there will be no meaningful comparables for the foreseeable future, then the lease renewal market will be creating the market and not following the market. Tenants and landlords will have significantly opposing views as to the market rentals post COVID-19. The credibility of the expert evidence will be called into question by the courts (and ultimately the market). The experts will be scrutinised even more so than normal, with their having a greater reliance on hearsay evidence. Valuers will need to be experienced and credible in providing opinions, which can be justified by market intelligence and knowledge of similar circumstances.

Even so, there will be significant uncertainties around the appropriate treatment of letting incentives. The 1954 Act does not dictate how any particular incentives should be treated, with the courts providing judgement that the new rent should reflect the effective rent, net of typical letting incentives being agreed in open market lettings, including for fitting out. In the current market, many landlords are granting rent-free periods of various kinds to help tenants deal with reduced revenues; and fitting-out periods are having to be extended due to practical constraints on contractors completing fit-outs. It remains to be seen how valuers and the courts will treat these exceptional circumstances when reviewing current market evidence to determine the appropriate rent on renewals.

A Potential Solution
There are interesting compromises where both parties are keen to avoid the time and costs involved in a court dispute. The introduction of a preliminary period of rent with an interim review after 12 months, perhaps, in the hope that more normal conditions have returned, allowing tenants time to commit? Or a short interim agreement coupled with an option for a reversionary lease at some point in the future.

If you would like to understand what the implications of Covid-19 on the lease renewal process means for you please contact:

Stuart Powlesland
Director,
Lease Consultancy

stuart.powlesland@avisonyoung.com
0117 988 5208

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

Charles Toogood
Principal and Managing Director,
National Offices Team
charles.toogood@avisonyoung.com
0121 609 8448

Mark Williams
Principal and Managing Director,
Regional Investment
mark.williams@avisonyoung.com
0161 956 4144

Giles Tebbitts
Research
giles.tebbitts@avisonyoung.com
020 7911 2670

Visit us online
avisonyoung.com/research

Avison Young
65 Gresham Street, London EC2V 7NQ

@AYUKviews