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# MarketView

# Edinburgh Offices

H2 2011

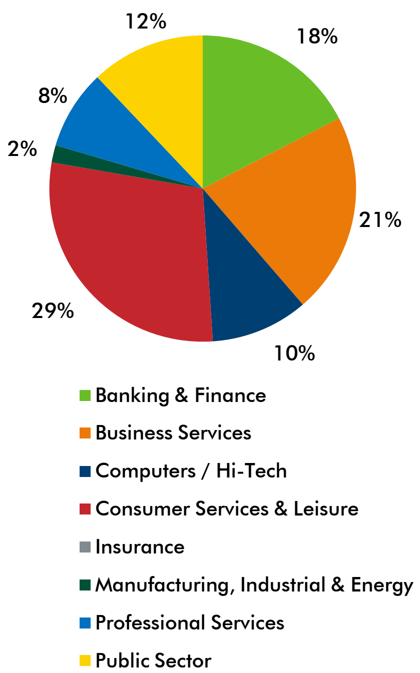
## Quick Stats

| | | Change from H1 2011 |
|---|---|---|
| Take-Up | ↓ | -9% |
| Availability | ↑ | 2% |
| Prime Rent | → | £27.50 |
| Prime Yield | → | 6.0% |

- Larger occupiers with potential requirements over the next 4 years are now moving more quickly and decisively as their options begin to close down. – *Stewart Taylor, Director, Agency*

- 2011 transactional volumes are low, however the supply of stock is tight. If the right product becomes available in Edinburgh in 2012 the buyers are there. – *Gavin Willins, Director, Capital Markets*

## Take-up by Business Sector, 2011




## Demand

Take-up in the second half of 2011 resulted in 319,067 sq ft of floorspace transacting, down slightly from the first half when just over 352,000 sq ft exchanged. While the total for the year of 671,513 sq ft taken is 8% down from 2010 it is still slightly above the five year annual average take-up of 633,589 sq ft.

The common theme driving demand through 2011 has been the timing of lease events in various guises but this is with a backdrop of a decreasing amount of good quality space. The larger occupiers specifically know that they could find themselves in a much weaker negotiating position in 18 months, and at all market levels the best space is disappearing.

Key active occupiers this year have come from the consumer services & leisure sectors (including Amazon's large deal earlier in 2011 for 57,442 sq ft), as well as the finance & business services sector (ie: Virgin Money's 30,943 sq ft deal also in H1). We also witnessed some significant inward investment from the likes of Avaloq, Craneware and Amazon (as mentioned above), which is unusual for Edinburgh and is partly due to the availability of well qualified graduates and staff in both the traditional financial sector and software design.

## Supply

Available space increased a small 1% in the last 6 months of the year to now stand at 2.75m sq ft. However, once again the real story is the lack of available good quality, Grade A stock, down now to just 738,421 sq ft, nearly 10% less than the same period last year.

In light of declining Grade A stock, Edinburgh is one of the only regional centres with a speculative development currently under construction with 190,000 sq ft available at the City Council-owned Atria (formerly 'HI') at 144/148 Morrison Street. There has been strong interest from occupiers in this property with 40,000 sq ft now under offer. It is due to complete in Q1 2013.

## Rents

Rents are currently static at £27.50, with incentives of circa 33 months on a straight 10 year lease. Going forward we feel that on existing space incentives may begin to come in as the better stock continues to diminish. On the sub-20,000 sq ft space we are unlikely to see any significant changes over the next 12 months but it is on the bigger space that things could change. Evidence of this is at Atria where we are already seeing the potential for below-market incentives and above-market rents.

## Outlook

Over the last 12-18 months we have seen a steady decrease in Grade A supply and as a result we've seen some occupiers moving more quickly to secure the space they want. While tenants have traditionally had the ability to have their pick of good quality space on flexible terms and at reasonable rents, to tick all three of those boxes is increasingly difficult. Occupiers know they have to move quickly and earlier or risk a compromise and are no longer quite so aggressive when discussing terms. Mid-market space is disappearing most quickly (eg: Waverleygate which has gone from 20% to 80% occupied over 12 months) and occupiers will increasingly either have to go up the rent ladder or down the quality slide.

## Key Edinburgh Market Statistics 2011

| | H1 2011 | H2 2011 |
|---|---|---|
| Take–up | 352,446 sq ft | 319,067 sq ft |
| *Long-term half-yearly average* | *348,684 sq ft* | *348,684 sq ft* |
| Availability | 2,708,663 sq ft | 2,749,142 sq ft |
| Prime Rent (per sq ft) | £27.50 | £27.50 |
| Investment Transactions | £69.24m | £27.5m |
| Prime Yield | 6.0% | 6.0% |

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## Investment

The office investment market in Edinburgh has been subdued in 2011 with very limited activity. This is largely due to availability and no newly developed stock becoming fully let to release new investment product. Owners of new stock are focusing on lettings rather than considering an exit of part let buildings. Activity has been limited to eight principal transactions this year with a total volume of £96.74m, however much of this came in the first half of the year, with just a further c£27.5m exchanging in the latter half.

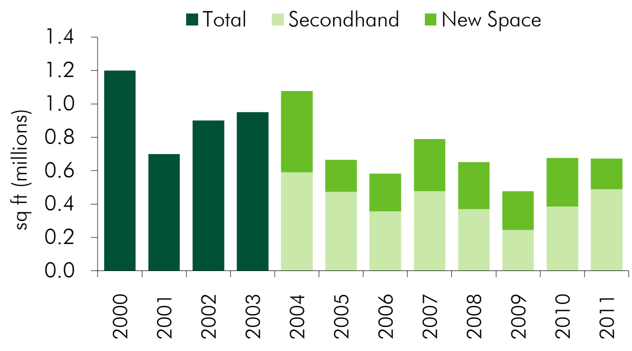
A lack of activity however, should not be taken as a lack of investor demand. To a large extent in 2011 it has been a lack of available prime product coupled with a mismatch in pricing between what were potential sellers and genuine buyers by probably around 25 basis points.

The largest deal of 2011 (completed in H2) was Edinburgh One for in excess of £23.5m which was sold to German investors. This has also been the only Grade A building to exchange this year, and indeed the only Grade A building that has come to the market. Just one further key deal completed in H2, with a property company taking 116 Dundas Street for £3.65m in September.

Looking forward we expect that German and other overseas investors will continue to be buyers for the right product. If there is yield drift it could attract more private wealth money and UK institutions for good quality buildings, however if that does happen it could make owners of such stock resistant to selling. Activity in the secondary market (which Edinburgh does not have a large inherent supply of) will also be limited unless driven by a forced seller. We do not anticipate a significant spike in availability in 2012.

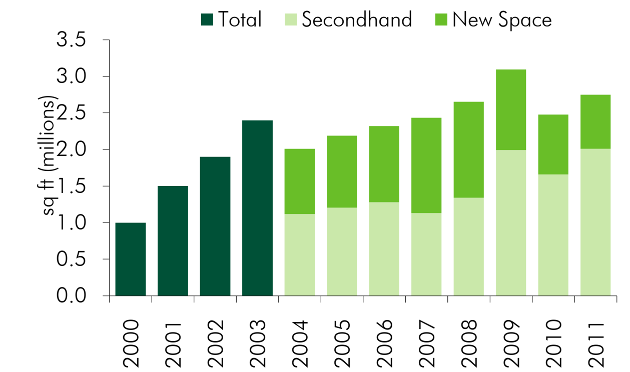
Prime yields remain at 6%, but this is only for the very best quality assets of a manageable lot size with strong covenants and long (15yrs) leases. We feel the gap between true prime stock and true secondary will widen moving forward with less assets sitting in this true prime category. Indeed, if any building deviates from a true prime asset let at a sensible rental, yields can quickly move out. For example even if the stock is a good quality building if it is only medium term income, purchasers will require more of a discount towards yields approaching 'mid 6s' to invest.

## Edinburgh Take-up



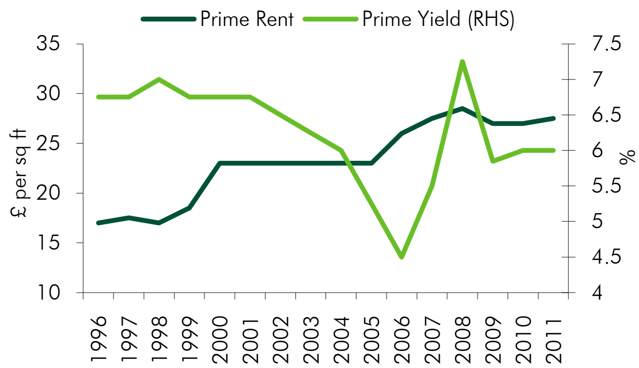

Source: CBRE

## Edinburgh Availability




Source: CBRE

## Prime Rents and Yields




Source: CBRE

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