allsop

Commercial and residential

Market Update

Q2 2018

Contents

Economic Overview

UK economic growth has provided a mixed message so far in 2018. The early cold weather and reduced consumer spending slowed matters to almost a halt in Q1 before the Royal Wedding, England's football World Cup run and the long hot summer provided the UK with a much needed morale and financial boost on the ground. Yet whilst the sunshine always helps to raise spirits and fuels a more positive national mood, there is general acknowledgement that the economic backdrop is one of continuing low level UK growth demonstrated by current forecasts of 1.3% for this calendar year rising to 1.6% in 2019. In terms of momentum, crucially, both forecast growth levels are down from previous estimates.

Politically, the minority Conservative government is seeking to soldier on as best it can, but has recently been unsteadied with recent cabinet minister resignations and a clear lack of unity across, not only the Tory party, but Westminster as a whole. With the degree of infighting in the backbench ranks starting to come to the boil, the sustainability of the current government, let alone the route to a Brexit solution, looks uncertain. The net result is continuing low growth in the short to medium term precariously underpinned by growing political and economic uncertainty.

According to ONS data, wage growth stabilised in May at 2.5% and CPI has continued the trend of becoming less aggressive; falling again to 2.3% in June from a recent high of 2.8% in Q4 2017. The income squeeze appears to be easing and although household spending has been falling, in theory the squeeze in marginal terms is reduced as wage growth outpaces inflation. The numbers suggest the economy is broadly on the right track in holistic terms, but this hides the severe impact on retailers and the casual dining sector. Retailers have been frantically trying to negotiate a way to cope with the double whammy of reduced consumer spending power and the change in shopping patterns away from the High Street. The pressure for some has been too great as has been widely publicised.

Residentially, much of the UK continues to be in relatively good shape although assets located in higher value areas, and Central London in particular, continue to be sluggish at best with continuing uncertainty in the Capital. In our experience, it is not unusual to see pricing under downward pressure where dwellings are worth above £750,000 in the eyes of vendors. In many areas nationally, however, pricing is supported by a shortage of new supply relative to long term demand and housing remains very high on the political agenda (albeit naturally not as high as Brexit). With wider political and economic recognition of the need for a balanced housing strategy – across owner-occupation, shared ownership, rent to buy, Build to Rent and affordable housing, there are increasing numbers of different opportunities for investors to partake in the housing investment sector. With an

uncertain commercial property world in several sectors, this appears to be providing a viable alternative for many larger scale and institutional investors.

The expectation that interest rates will increase remains, albeit incrementally, over the medium term and the risk of an Autumn general election feels greater than ever. The backdrop for UK real estate remains one of some caution with the depth of demand in many of the secondary markets thinning, but there is also resilience with regards to better quality, well located or sustainable stock. Nonetheless the longer term economic fundamentals of UK plc remain strong. This is arguably shown by a continuing presence of overseas buyers who are active in the regions as well as Central London recognising the long term opportunity offered here.

Any interest rate rise will have a negative effect on sentiment in the market but on the whole this is expected and is priced in. A general election, however, if called, would increase uncertainty to a new level – the market would inevitably pause (as it did in 2017) and weigh up the possibilities of various outcomes, some of which may not be as attractive to the investor fraternity as others. In any event the sunny uplands of a Brexit deal seem a long way off at this point.

West End Letting Market

Following on from what was a slow Q1, where take-up fell by 10%, we have started to see greater activity resulting in an increase of active requirements. In June alone we saw the amount of space under offer at its highest point in over a year. Throughout Q2 we have seen an increase in take-up with May and June being up 9% on the long term average and 11% on the same period last year. Notable Mayfair transactions include Houlihan Lokeys assignment of 43,000 sq ft at 1 Curzon Street and the serviced office operator, London Executive Offices, acquiring 32,000 sq ft at Park House.

Whilst the tech and media sector remains very active, there has been an increase in activity from insurance and financial occupiers accounting for 40% of the market share in June. Serviced office providers continue their acquisition of office space accounting for 35% in June. Notably Knotel acquired the whole of 45-51 Whitfield Street from Derwent London.

West End supply stood Q2 at 4.58M sq ft, at the end of Q2 a 10 bps decline on Q1. With this we have seen a slight decrease in the vacancy rate to 3.7%. The Victoria sub-market experienced the most notable reduction in supply since the end of the last quarter falling from 500,000 sq ft to 315,000 sq ft.

There is 1.4M sq ft of development and extensive refurbishment completions scheduled for the second half of 2018. Demand for new developments remains strong with 67% of these being pre-let.

Prime rents in the West End have remained stable at £116 psf with Grade A rents falling to £75 psf and Grade B rents to £62.50 psf. The record rent for the year remains at 30 Berkeley Square where OCI paid £185 psf for a 10 year lease on the 5th floor.

Landlords continue to offer increasing flexibility and incentives with rent free periods now approximately 20-22 months on a 10 year lease and 10-12 months on a 5 year term.

> In Q2 we have seen an increase in take-up with May and June alone being up 9% on the long term average


Crystal Palace 3
Crystal Palace 3
LX08 KWA

West End Investment Market

The West End Team recorded a total of £2.1Bn exchanged or exchanged and completed in 33 transactions during Q2 2018.

This brings the half year total to £3.1Bn, some way below the record breaking 2017 H1 total of £4.7Bn, and at just below the £3.5Bn five-year average it is encouraging.

Six transactions in Q2 were in excess of £100 million and made up almost 60% of the total volume: the sale of Burlington Arcade to Motcomb; 20 Soho Square to a Private European Investor; CAA House to Seaforth Land; 135/137 New Bond Street to a Private Singaporean Investor; and 30 Warwick Street was bought in a Joint Venture between Norges Bank Real Estate Management & The Crown Estate (the latter are also the Freeholder).

UK institutions have been involved in almost a third of the deals this quarter being particularly active sellers of seven buildings including the sale Aviva Investors 20 Soho Square for £117.4M (3.98% NIY) to a Private European for £1,763 psf. This shows sustained investor appetite for freehold building's that offer long-term, secure income, which requiring minimal asset management and low capital expenditure going forward (- the property was redeveloped in 2016). Encouragingly, the institutions have also bought a couple of buildings this quarter and through Allsop's sales book we are aware that the institutions are actively looking.

Allsop completed the sale of 65-68 South Molton Street & 32 Brook Street, Mayfair on behalf of Columbia Threadneedle investments for £55M (2.81% NIY). This is one of the three largest retail-led investment transactions in the Core West End so far this year and illustrates that demand continues, particularly from international investors who are willing to pay sub-3% yields, for such 'trophy assets'.

Moving into Q3 there have been several further high-profile sales bought to the market in Q2 such as Adelphi, WC2 (now 'Under Offer'), Waterside House, W2 and Stirling Square, SW1 and a number of major buildings remain available including 23 Savile Row, W1 and 125 Shaftesbury Avenue, WC2. Combined these sales make up in excess of £1.5Bn of volume. We are currently tracking over £3Bn of available / 'Under Offer' stock however, the current market trend we continue to witness is the lack of 'average lot size' assets, around the £40-£60M mark, which is frustrating investors and turnover is suffering as a result.

Across the board, in the West End, investors (particularly overseas) remain attracted by quality assets offering secure income, minimal capital expenditure in the short-to-medium term and a relatively hands-off asset management strategy. Whilst depth of interest at bids stage for certain assets has certainly reduced, the yields achieved in the core market do show that the market remains strong for such assets. International investors have been involved in over half the Q2 purchases, and continue to dominate the W1 prime transactions. The geographic origin of this international capital is diverse; however there has notably been a distinct lack of activity from the Gulf region this quarter. Looking forward we expect this overseas interest to continue throughout the second half of the year.

Six transactions in Q2 were in excess of £100M and made up almost 60% of the total volume

City and City Fringe Letting Market

Demand for City offices has remained strong in Q2 with the highest levels of take up recorded since 2015 and under offers at their highest level for 5 years.

Take up for June reached 870,000 sq ft with the largest transaction being the purchase of Royal Mint Court, E1 by the Chinese Embassy for their new London HQ totalling 590,000 sq. ft. Take up for the first half of 2018 is circa 2.8 million sq ft and is 30% ahead of the 10 year average. This is however misleading given the underlying take-up for sub 10,000 sq ft which has been limited.

The serviced office sector continued to grow with Regus Spaces taking a further 40,000 sq ft at Minster Court on the ground and 6th floors at £65 psf per annum. This is in addition to their recent commitments at 30 Moorgate (26,000 sq ft) and The Epworth (40,000 sq. ft.). We Work are also continuing their expansion with a focus on several City and Midtown opportunities.

Minster Court continues the run of successful lettings with further lettings to Tower Research Capital and Make It Cheaper comprising a total of 35,000 sq ft. Lyst Fashions are also under offer to take 20,000 sq ft, relocating from the City Fringe and Hoxton Square to the insurance district.

22 Bishopsgate, due for completion in Q4 2019, is proving attractive with interest from 3 major insurance occupiers including Aspen Re (u/o on levels 43 and 44 for 52,500 sq ft), Beazley Insurance (u/o on levels 12 & 13 with rights over level 14; 50,000 sq ft), and Hiscox (u/o on levels 8, 9, and 10 with rights of first offer on level 11; 75,000 sq. ft.). The guiding rents have been in the mid to late £60's psf to secure early deals for pre-lets prior to an increase in rental levels.

Demand for City offices has remained strong with the highest levels of take up recorded since 2015 and under offers at their highest level for 5 years

Other key moves for HQ relocations include Cisco Meraki, Cap Gemini and Northern Trust all considering space in excess of 100,000 sq ft, with additional requirements from Bank of New York Mellon, Bank of Montreal and Quilter (formerly Old Mutual).

Shoreditch demand remains strong for the larger floorplates of 10,000 sq ft upwards. The Bower has recently signed 3 floors with FarFetch (an existing occupier within the estate) for levels 7, 8, 9 at a rent of £69 psf on a 9 year lease. Competition with the serviced office sector is however reducing the take up for suites of sub 5,000 sq ft and many Landlords are now looking to offer fitted out floors as an option.

Vacancy rates have increased slightly to 5.9% up by 0.3% although this still remains balanced for the longer term average. The increase has been due to additional second hand supply coming to the market. This is expected to increase further in 2019 with the completion of significant numbers of new build schemes completing. Many of these however are either pre-let or are expected to be placed under offer over the coming months.

Prime rents remain at £68.50 psf with premium rents in excess of £70 psf for trophy space. Given the latest demand/under offers, these rents are expected to increase slightly into Q4 2018, although the financial markets do still remain cautious given the Brexit negotiation. Many of the financial and insurance based occupiers are now weighing up the balance of requirements for European representation alongside space occupied in Central London.

City and City Fringe Investment

Following the strongest investment turnover on record in 2017 (£11.25Bn), the City market experienced momentum building towards the end of the first quarter, continuing to grow into the second.

Our City Investment Team has recorded a total of £3.71Bn either exchanged or completed in 34 transactions during Q2 2018 which is broadly in line with the long term Q2 average of circa £3.8Bn and significantly higher than the £2.645Bn recorded in Q1 2018. Investor sentiment remains strong and from a variety of purchaser types, with the increase in volume from Q1 reflective of an increasing level of product coming to market.

The average deal size for Q2 2018 was £109M compared to £98.5M in Q2 2017 and demonstrates the continued strength of demand from overseas investors for larger core City assets, particularly from Asian investors. For example, Ho Bee continued their Central London buying spree by purchasing Ropemaker Place, EC2 for £650M/ 4.62%/ £1,081 psf, whilst Hong Kong based CK Asset Holdings purchased 5 Broadgate for circa £1Bn/ 3.95%/ £1,364 psf. We are also aware of good interest in another large lot size, Goldman Sachs new Headquarters building at 40 Shoe Lane, EC4. This ongoing sale and leaseback opportunity has been quietly marketed at an asking price in the order of £1.2Bn.

What has been notable so far in 2018, is the lack of available product on the market, particularly in the sub £50M lot size range.

Investor sentiment remains strong even for riskier assets in this lot size range, with a large number of bids received on several openly marketed properties. For example, Clerkenwell development opportunity Edward Rudolf House, WC1 attracted over 15 bids, before exchanging at £17M/ £735 psf against an asking price of £15M/ £649 psf. Similarly, Mitre House, Borough High Street, SE1 attracted over 12 bids and is rumoured to be under offer at circa £25M/ 4.82%/ £792 psf, with a guide price of £22.5M/ 5.26%/ £713 psf. 2018 has seen a return of UK institutions to the market, with many now experiencing historically high levels of cash, following a more cautious approach to new acquisitions in the wake of the Brexit vote.

The People's Republic of China purchased Royal Mint Court, EC3 from Delancey and LRC Group for £255M in one of the largest ever owner occupier deals in the City of London. The 5.4 acre site is situated opposite the Tower of London and will house the new Chinese Embassy. The site has a planning consent for approximately 600,000 sq ft of office accommodation and 1.8 acres of public realm. Other owner occupier deals continue to be prevalent in the market place. Carlisle Group completed the off market purchase of Crosspoint, 34-37 Liverpool Street, EC2 for £43.02M/ £1,035 psf, for their Uncommon co-working brand. The newly developed office building was sold by Amsprop with vacant possession demonstrating how co-working providers are willing pay premium prices for vacant offices, in outstanding strategic locations.

Asian investors have continued to dominate the

2018 has seen a return of UK institutions to the market, with many now experiencing historically high levels of cash

market turnover. Korean investors have continued their interest in £100M + well let assets, with Korea Investment Management purchasing 70 Mark Lane for £200.5M/ 4.62%/ £1,106 psf. In terms of numbers of deals, UK investors have carried out the most with 25 in H1 demonstrating positive market sentiment not only from overseas investors, albeit, this in the sub £50M lot size bracket.

Evidence displayed during Q2 2018 suggests that London will continue to attract overseas investors despite Brexit, drawn primarily to London's safe haven status and the fact it offers good value in comparison to other major cities globally. The increased presence of UK investors bidding competitively for smaller, riskier assets, buoyed by a positive occupational market, shows strong market sentiment across the investor spectrum. We expect this to continue into the next quarter with prime yields remaining at their historic low of 4.0% - 4.25%.

Following the first interest rate rise in 10 years, in November 2017, it is widely anticipated there will be a further rise later in 2018. If an increase in interest rates is quickly succeeded by a further rise, this may have an impact on property investment yields. However, we anticipate only a gentle increase in the short to medium term.

National Investment Market

Despite the current political and economic uncertainty with the culmination of BREXIT fast approaching, together with the continued threat of an interest rate rise, the UK's national investment market remained resilient in Q2 2018.

With the exception of High Street investment, transactional volumes were strong for the quarter. Total volumes equated to £25.25Bn for Q1 and Q2 2018 which is much in line with the same period in 2017. The industrial sector continues to go from strength to strength and the office market, particularly in Central London and city centres, has proved extremely popular with investors.

> Total volumes equated to £25.25bn for Q1 and Q2 2018 which is much in line with the same period in 2017

Industrial

Investment in the industrial sector remains strong with prices being well supported. The weight of money, both institutional and private is increasing with new entrants to the market likely to lead to continued yield compression.

There have been numerous landmark deals in the previous quarter including Orchard Street's acquisition of Zenith Industrial Estate, Basildon for £36.2M reflecting a net initial yield of 3.85%. Westbrook have purchased the Sterling Industrial Portfolio, formed of 28 industrial estates nationwide, for £162M reflecting 6.77%, as well as Martinbridge Trading Estate, Enfield for £53.75M reflecting a low initial yield of 3.1%. M&G purchased the Mountpark Logistics Portfolio, formed of 5 newly developed buildings, for £93.8M reflecting 4.56%.

Despite the looming Brexit deadline, strong occupier demand and a slow development pipeline means rental growth prospects in this sector are strong. E-Commerce will remain the primary driver for growth in demand for logistics space with both larger distribution hubs and "last-mile" depots allowing retailers to service more efficiently an ever expanding and demanding consumer base.

High Street

The woes of the High Street continue as more and more retailers enter liquidation or CVAs – retailers who have suffered financial problems and failures in Q2 include House of Fraser, who are closing 31 stores, Mothercare who are axing 50 branches, Poundworld who have entered CVA and now M&S who have announced plans to close over 100 stores in the next 3 years. Crippling rents and high rates bills have proved the downfall of the High Street and without a successful 'on-line' offer, many retailers are now hitting the wall. We expect this trend to continue as the year goes on although the good Summer weather and World Cup "feel good" factor may provide a brief respite.

Investor confidence in the sector is very low and yields have suffered accordingly. Not only are investors concerned about the quality of the tenant but rents that were re-based a few years ago suddenly appear over-rented and a further re-basing may be required.

It is not all doom and gloom with the core High Street section of strong towns and cities holding up well and London and surrounding suburbs still continue to attract investors, particularly those looking for defensive investments let on long leases.

In Q2, we have seen real evidence of the polarisation between the sharp yields being paid for well-let retail in strong towns and double digit yields which are now the High Street norm in weaker towns.

Retail Warehousing Deals

The raft of recent CVA's mentioned above has created a lot of negative noise towards the whole retail sector and retail warehousing has not been immune to this. This sentiment has resulted in the softening of yields across the board with a more significant impact to values on the secondary and tertiary parks where rental values are being re-based even further. The future of these secondary and tertiary schemes remains in question and there may well need to be a repositioning of some of this excess retail warehouse accommodation to residential, logistics or other alternative higher value uses.

Prime retail parks, particularly those in the south east, are still experiencing modest rental growth but this is very specific on a case by case basis.

The current negativity towards retail warehousing and the resultant outward yield shift may offer an opportunity to investors who want to take a counter cyclical view. Yields are well below long term averages and retail warehousing is a sector that should be able to weather the storm of structural changes better than the High Street. Through a better collaboration of 'click and collect' and last mile delivery, retail warehousing offers the potential to adapt to retailing trends and changes.

National Offices

There has been an increase in activity within this sector in relation to the first half of the year. UK regional centres are experiencing strong demand in a setting of limited availability of quality accommodation. This could lead to rental growth in specific centres.

Institutions and Local Authorities continue to have significant funds to invest in the provincial office sector – especially in locations with strong fundamentals including strong workforces, leading universities, tight office space supply and that are deemed attractive places to live. Best in class buildings are particularly popular in the current market alongside buildings which can be repositioned and refurbished to drive rental growth. Prime office yields in the UK regions remain highly attractive by comparison to the City and West End office markets and to Industrial yields that are continuing to fall further.

Notable deals include Northamptonshire County Council's HQ building at One Angel Square, Northampton which was purchased by Canada Life Assurance at £64M, Bank of Scotland's office at New Uberior House, Edinburgh which transacted at £71M and UK Commercial Property REIT acquired the White Building in Reading for £51M reflecting 5.75%. In addition, we recently sold Workspace's Acute Portfolio – three North London multi-let office buildings for £51.85M reflecting 4.38%.

Portfolios

The UK Commercial Portfolio Market continues to exhibit a high level of transactional activity. Total transaction volume totalled in excess of £5.31Bn for the first half of 2018, a notable increase on the previous year; which, was considered by many, to represent a standout year for the UK Portfolio Market.

Portfolio composition remains critical as investors continue to be drawn to high quality investments providing secure long-term income. The market has benefitted from a recent resurgence of secondary portfolio supply, in particular within industrial and logistics sectors benefiting from strong capital fundamentals and continued rental growth prospects. Demand remains strong for well-located assets and we anticipate total market transactions will increase in Q3 2018 as these deals come to fruition.

Institutional Funds remain acquisitive with substantial cash allocations to deploy at present. Active requirements remain high for a majority of use types and, we anticipate this will continue for the foreseeable future.

Notable recent portfolio deals include:

Dolphin Portfolio (Industrial)	£22m
Bluebell Portfolio (Mixed use)	£39m – 6.9%
Platinum Portfolio (Industrial)	£55m – 4.37%
The Sterling Portfolio (Industrial)	£162m – 6.77%
Starwood Hotel Portfolio (Hotel)	£858m – n/a
Acute Portfolio (Offices)	£51.85m – 4.38%


allsop

Commercial Auction Market

After four auctions in 2018 Allsop Commercial Auction Team has raised £314million at a success rate of 82%.

H1 2018 has seen a ready supply of unsettling High Street headlines which have contributed to bringing an element of caution to the auction room. This has resulted in heightened price-sensitivity from the private investor. However, despite this uncertainty, there remains an abundance of cash rich buyers with a healthy desire to invest and the weight of money pursuing the better quality assets is as high as ever. Additionally, there is continued appetite for larger lots with a total of 86 lots having sold for £1M or more.

This continued demand has resulted in a hardening of yields for 10-15 year income nationwide to sub 6%, in from 6.8% in the preceding six months.

Conversely, and perhaps unsurprisingly, yields for short-term income have moved out, reflecting the heightened risk, continuing pressure on rental levels on some High Streets and perceived uncertainty over the future of the High Street in some locations. This yield gap may well widen further in the latter part of the year.

Away from the High Street, non-retail alternatives account for approximately 25% of our total value this year. The pool of buyers seeking such opportunities is ever widening and we wait to see if supply can keep up with the unsatisfied demand.

The traditional fundamentals remain unchanged but our results through the first half of the year suggest investors are placing added weight on the location of an asset and paying premium prices to reflect this. Value added opportunities and future use potential continue to appeal to our wide audience and push pricing on further.

Enduring Brexit negotiations have resulted in heightened political uncertainty which cannot be ignored. For some this may push them to adopt a 'wait and see' strategy, for others the safe haven of better quality real assets could prove to be tempting.

> Long-term income has been one of the main focuses for investors throughout 2018

Residential Development Market

There is continuing political pressure for developers to provide new homes to reach the government's target of 300,000 new homes a year.

This will be delivered through sites of varying scale requiring a range of developers to contribute to meeting targets. This ranges from housebuilders and housing associations, through to small and medium sized developers, as well as the Build to Rent market which continues to grow.

We have seen continued demand for residential development land over recent months, with a continued focus on lower value well located stock in Greater London and well located sites in the regions. Recent examples of which include Meadow Mill in Stockport, a residential conversion opportunity with planning for 213 residential units which received strong interest and sold for around the £7m guide price.

Whilst the London market has been focussed on Help to Buy areas primarily, we have seen increasing levels of activity in more central London locations. A prime example is the recent sale of an office building overlooking Clapham Common in London with consent to convert to 61 residential units for which we had over 450 interested parties and sold in excess of the £18.5M guide price and exchanged and completed in a week.

We have seen a noticeable increase in opportunities that benefit from planning consent, as the reported industry reduction in new homes sales and construction starts has caused some prop co's and smaller developers to consider selling their consented sites. This is particularly the case where planning gain can be realised with the upside of reducing the sales risk of their portfolio, safe in the knowledge that sensibly priced consented stock will still sell well.

We have recently completed on a number of unconditional land sales across London in the £5-10M bracket. There remains a strong demand for opportunities to add value through planning with a large volume of money ready to be invested in this space.

This comes at a time where there is an increasing shortage of unconsented land deals. This is partly due to increasing planning restrictions around change of use and the strong existing use values of office and industrial stock. We continue to see fierce competition for well located unconditional land with a good planning story.

Whilst the London market has been focussed on Help to Buy areas primarily, we have seen increasing levels of activity in more central London locations

Residential Investment Market

The residential investment market continues to offer a competitive market place, particularly for regional opportunities between £1M and £5M where there are a number of active buyers. Requirements are however growing for opportunities that provide scale in the regions and there is a market for opportunities with pricing in excess of £10M. It is fair to say there is a short supply of income producing blocks of residential assets across the country though which makes reading the market that little bit tougher. Regionally we are witnessing new buyers enter the market, providing further competition for the core investors who are actively seeking to increase their portfolios. Pricing though has remained consistent. We suspect there are fewer buyers than there were in 2017 for opportunities in London and the South East.

It is an important footnote, that strong supporting evidence of the quality and sustainability of rental income streams cannot be understated when considering the marketability of and likely price an asset will sell for. This is due to the defensive nature of the return profile active core investors are looking for.

With less stock on the market, a wider range of locations and properties are being considered – but investors are tending to specialise in the types of assets that they are prepared to acquire and are still discerning. Equally, assets that are being offered to the market are usually where investors have decided to take a different strategy with their investments for the next market period so maximising, and crystallising, return is often critical. Traditionally popular regional centre locations are being supplemented more secondary locales as investors consider how best to diversify or grow portfolios based on the stock available.

Closer to Central London, the market can be difficult to assess on a broader brush more regional basis. There is much more emphasis in Greater London, for example, on potential buyers assessing their own view at a very locational specific micro market taking into account development/added value potential when considering acquisitions. In all cases though, our experience demonstrates that if vendor expectations are realistic and in step with today's marketplace, then there will likely be buyer interest.

Following the Government's announcement in December 2017 that it plans to ban leasehold houses, limit future apartment ground rents to a peppercorn and reduce the costs of lease extension when parliamentary time for legislation allows, the residential ground rent market is starting to show signs of becoming more active again after a hiatus in the first half of 2018. Our investment teams in London and Leeds have a small number of ground rent investments under offer presently which is encouraging.

Regionally we are witnessing new buyers enter the market, providing further competition for the core investors who are actively seeking to increase their portfolios

The Build to Rent Market

Quarter two of 2018 continued to witness a plethora of press releases charting the progress of potential new build to rent developments and transactions, demonstrating BTR is now a firmly established sector. Whilst there are still new BTR stories worthy of mention, as we enter Q3 it would appear the pace of new BTR announcements has cooled somewhat. Arguably, this is in part due to the BTR sector now being in the 'development phase', with the focus having shifted towards existing stock management including mobilisation of assets in development and new acquisitions for current players, rather than the novelty of first scheme acquisitions.

The British Property Federation (BPF) latest figures estimate an impressive 117,893 build to rent units either completed or planned across the UK; including 20,863 completed, 33,075 under construction, and a further 63,955 with planning permission. Other announcements worthy of mention include: British Land, the UK's second-largest property company, announcing plans to push into BTR; planning granted for 200 build to rent apartments at London's Old Oak by Aurora Developments, forming part of a £26Bn residential development plan; Lincoln MGT's (a JV between US Lincoln Property Company and UK MGT Investment Management) first acquisition of a BTR development site in Reading; M&G and Crest Nicholson's third project of 114 suburban apartment scheme in Arborfield Green; and Lambeth Council investing £42M from its pension fund into Invesco Real Estate's BTR strategy.

The first major REIT to focus purely on the private rented sector has started strong, the float price was 100p and in early trading in June, shares hit a high of 107p. Sigma will use the new vehicle as long-term holding for assets it has developed. A pipeline of over 2,500 new homes costing c. £375M has been identified and contracted. Two thirds of the pipeline will be funded by the REIT with Sigma acting as development manager; the rest will be developed by Sigma and sold to the REIT.

Q2 2018 continued to witness a plethora of press releases charting the progress of potential new build to rent developments and transactions, demonstrating BTR is now a firmly established sector

We are repeatedly seeing secondary cities and well-connected large towns becoming higher on the agenda, with investors seeking to deploy remaining and growing capital in secondary or even tertiary areas, given experience from other stabilised schemes in their portfolios providing the confidence that security of income can still be achieved. On the back of this trend, the move towards build to rent housing continues. Houses offer residents the space, flexibility and perks of living in a well-managed new house without the need to save for a deposit or mortgage. It is anticipated that larger BTR homes will be viable in more suburban locations generally in regeneration areas where rents are at a healthy level and offer growth potential but open market sales values are not too high. These target areas must offer a good provision of amenity, schools and transport infrastructure in order to suit the family demographic and those considering alternatives to city centre living.

Yields remain strong for well-designed BTR stock in prime, practical locations; with a 3.25% to 3.75% NIY still being accepted in London and the South East, and closer to 4% or 4.5% in a number of major regional centres.

As the BTR market establishes itself further, the sector needs to continue to build on the data being gathered from stabilised schemes and adapt the customer service offering accordingly.

Residential Auctions Market

The first quarter of 2018 saw investor appetite return for London lots, despite concerns that central London residential values had cooled.

In the second quarter, May's residential auction brought a number of attractive residential buildings in prime locations to market, including a stunning four-bedroom end of terrace house in Chelsea. With sellers looking for success before the summer slowdown, the catalogue showed a large number and wide variety of lots. More than 300 properties were initially listed, making it one of the largest of the year.

Despite investor caution in the market, the auction raised over £70M with a success rate of 80%. Lots that were sensitively priced and of high quality were particularly sought-after. These included a number of investments in London and the South East. An unbroken block of flats in the affluent commuter town of Royal Tunbridge Wells achieved £3.08M and was the largest lot sold under the hammer that day. We also saw investments in the regions perform well, with a block of flats comprising 10 units in Oadby, Leicester raise £1.54M at 5.84%.

Amidst concerns about the country's political future, the market is still determined to get business done. Whilst business perseveres, caution within the residential market is on the rise and getting the guide price right is proving especially critical. Opportunities presented at modest guides have done incredibly well, whereas lots priced optimistically have drawn limited attention.

Overall, we believe 2018 will progress to be a year of correction as different sectors of the market and regions of the country come to terms with tougher taxation and mortgage regulation, rising interest rates and political instability.

In the short term we are likely to see investors continue to adjust their portfolios in response to tougher market conditions this year, rather than leave the sector, particularly those with larger portfolios. So far this year landlords have mostly shown they want to stay in the game and we have seen good appetite for investment, which we anticipate will continue throughout the year, albeit, with some investors seeking yield and greater capital value growth from further afield.

We are likely to see investors continue to adjust their portfolios in response to tougher market conditions this year, rather than leave the sector

Head office
33 Wigmore Street,
London W1U 1BZ
Tel: +44 (0)20 7437 6977

City office
2 Copthall Avenue,
London EC2R 7DA
Tel: +44 (0)20 7588 4433

Leeds office
8th Floor, Platform,
New Station Street,
Leeds LS1 4JB
Tel: +44 (0)113 236 6677

Brighton office
Princes House,
53-54 Queens Road,
Brighton BN1 3XB
Tel: +44 (0)1273 322 013

www.allsop.co.uk