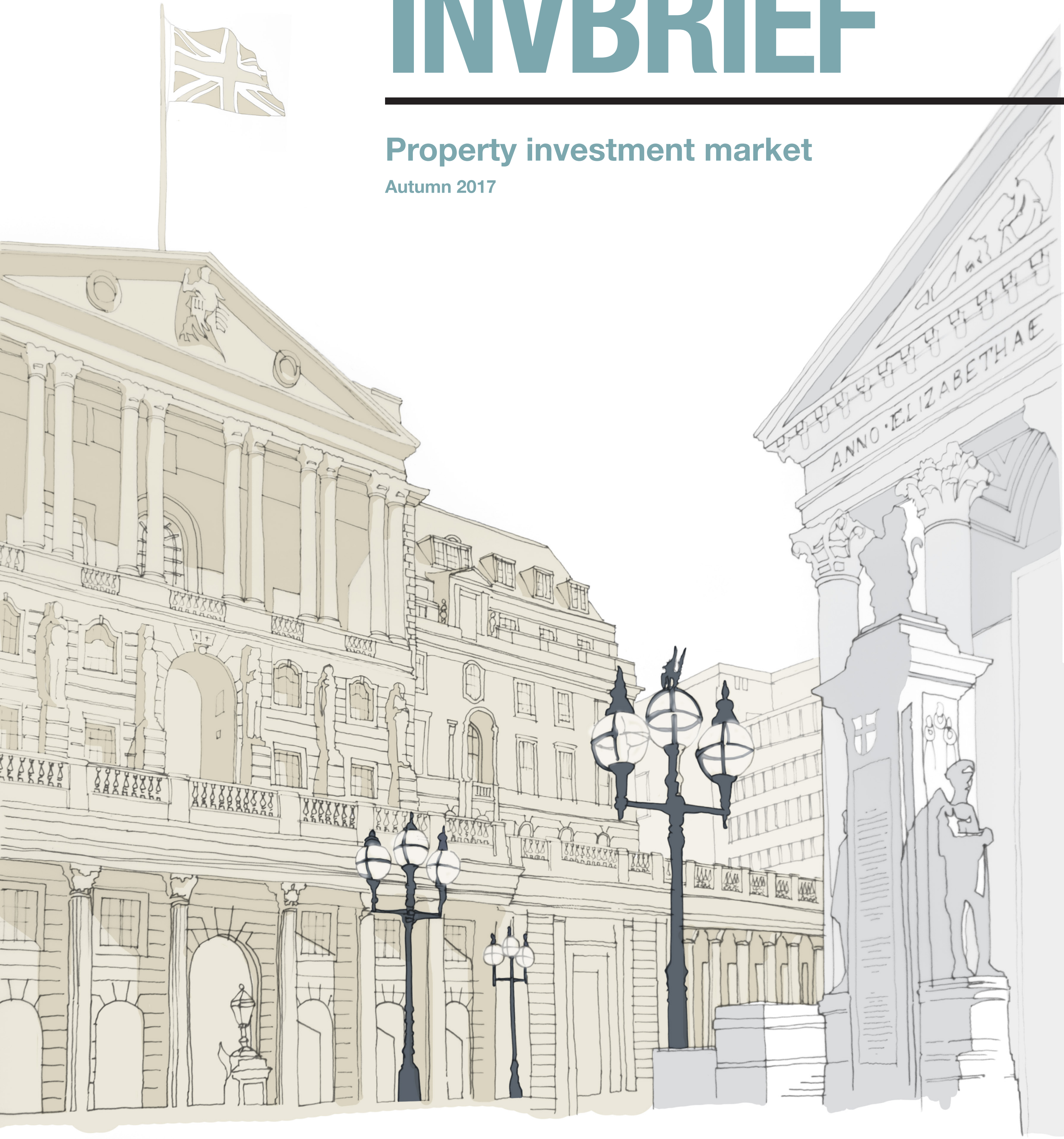
# INVBRIEF

## Property investment market

Autumn 2017




GERALDEVE

International Property Consultants

**2.9%**

**CPI Inflation August 2017**

" … a near term rise in interest rates… could be as early as the November MPC"

## ECONOMY

It is now over a year since the EU referendum result and we still seem no closer to knowing what Brexit will actually look like. Article 50 was served back in March, and since then we have had more political and economic uncertainty. A snap general election was called by Prime Minister Theresa May, who promised to deliver the "strong and stable" leadership necessary to negotiate a favourable Brexit outcome. With the polls predicting a Tory landslide at the time that parliament was dissolved, it looked as if the Prime Minister's gamble was going to pay dividends but another shock election night saw the Conservative party lose their majority. Theresa May now has the unenviable task of delivering Brexit from a weak governmental position.

Despite all this uncertainty, economic indicators remain positive. GDP figures show that the economy grew by 0.3% in Q2 2017, which equates to 1.7% over the 12-month period. Unemployment in the UK stands at 4.3%, the lowest it has been since 1975, and average weekly earnings are 2.1% higher than they were a year ago. These positive economic indicators coupled with a weak pound create an attractive investment environment for overseas investors into the UK.

Despite the relative stability of the economy thus far, the Monetary Policy Committee (MPC) have voted to keep interest rates at their all-time low of 0.25% since shortly after the Brexit vote. Critics of this policy have warned that the low interest rates are having a downward pressure on the currency and also increase the risk of high inflation. Indeed, two of the current members have voted for a raise to 0.5% each of the last three times that the MPC have voted on interest rates. Some analysts argue that it is the current loose monetary policy that is stimulating the economy to maintain its current course, and once removed the economy will grind to a halt. There is also the risk that, should there be any further hiccups in the economic recovery, there is little further economic stimulus that can actually be provided. The governor of the Bank of England, Mark Carney has strongly hinted at a "near term" rise in interest rates which could be as early as the November MPC.

Inflation, as measured by the Consumer Price Index (CPI) reached 2.9% in August above the Bank of England's target rate of 2.0%. The Office for National Statistics' (ONS) new and preferred measure of inflation, CPIH, reached 2.7%. This measure was adopted in March 2017 and includes the cost of housing of home owners in the calculation. The Bank of England predicts that CPI inflation is set to rise even further to peak at 2.75% in Q4 2017 before gradually descending towards the target. Whilst in nominal terms wages have increased, the above-target inflation means that UK consumers' real purchasing power is being suppressed and, together with a weak sterling, imports are becoming ever more expensive. According to the ONS, growth in household spending fell to just 0.1% in the three months to June as the squeeze on consumers tightened.

### Outlook

Brexit uncertainties will continue to dominate the markets for the foreseeable future. Whilst there was a short shock to the economy in the immediate aftermath of the vote, the economy has proven to be relatively resilient thus far. There remains, however, much anxiety as to what the full impact of Brexit will have on the UK.

Important questions that still need to be answered include: will there be a trade agreement with Europe within the allotted two-year time-scale? Will there be freedom of movement for British people and Europeans? What passporting rights will the financial services sector in London enjoy?

With so much uncertainty it is becoming clear that, for the moment at least, the economy will only be able to move forward with a partial handbrake in place.

There are however reasons to be optimistic. The UK remains the fifth largest economy in the world and European countries such as Spain, Italy and Germany run a trade surplus with the UK. It has to be in the EU's interest to agree some kind of deal to enable trade with the UK. A trade deal with the USA appears a realistic prospect given the mutual advantages this will bring to both. The prospect of the UK leaving the EU whilst maintaining a healthy economy remains a reasonable position.

The Brexit negotiations are really only just getting under way and the process of the UK's withdrawal from the EU is set to be a long and protracted process. Article 50 provides for a two-year timeline for the removal of a member state from the EU, that two-year window closes at the end of March 2019. However, there is a further provision in Article 50 to extend the Brexit timetable beyond that date should all the member states agree.

The property markets continue to be resilient. This may be due to the "softer" Brexit overtones that have emerged over the summer following the general election. Perhaps this scenario is the one the property markets see as the most likely, thus underpinning the enduring positive property results over 2017. The overall outlook is that fundamentals have not altered, and we have not experienced a collapse in sentiment towards commercial property.

An Institute of Directors survey, undertaken immediately after the election, indicated that 20% of its members were optimistic for the UK economy over the next 12 months, compared with 57% who were quite or very pessimistic. By way of contrast, a CBI survey has cautioned that there is an enhanced risk that businesses will cut back on investment as a result of the ongoing Brexit uncertainty.

Due to the range of possible outcomes, the cautionary investment aspect was underscored in a speech by the Governor of the Bank of England. The impact on business is evidenced in deferral of investment activity, with consequent knock-on effects for commercial property. However, despite development projects being put on hold or postponed, one positive is that this will not inflate medium term supply.

Major concerns about the property market have diminished over 2017, with some of the investment downside lessened by a weaker sterling. The pound's general weakness continues to attract overseas investment, thus keeping investment yields at low levels. It seems that, despite the uncertainty surrounding Brexit, overseas investors continue to find the UK real estate markets attractive.

The longer the outcome of Brexit negotiations remains to be determined, the more we can expect there to be yet more twists and turns which will hold back investment and economic performance.

**Fig 1. Price of Sterling in foreign currency**
Source: Bank of England

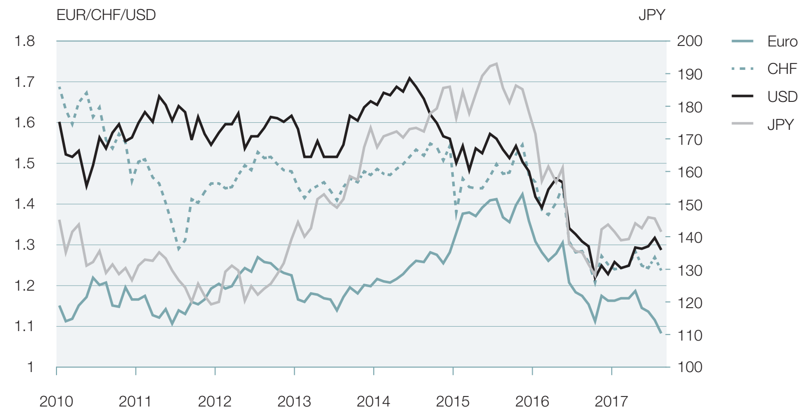
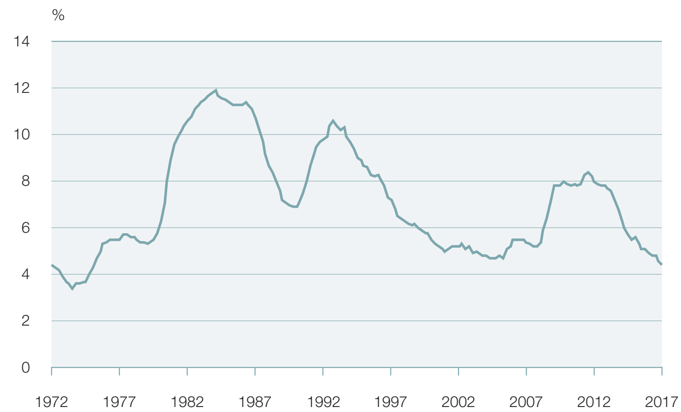



**Fig 2. Unemployment rate**
Source: ONS



**5.5%**

**All property total returns in year to June 2017 (MSCI quarterly data)**

" …positive capital growth figures suggest that the market has come to terms with the initial shock of the UK's EU referendum result. "

## COMMERCIAL PROPERTY

UK commercial property delivered total returns of 5.5% in the year to June 2017 according to MSCI quarterly data. This was the highest return over a consecutive four quarter period since the twelve-month period to June 2016. This figure is expected to improve in the next quarter as the impact of the weak Q3 2016 data in the aftermath of the EU referendum falls out of the annual figures.

Over the past two quarters average returns have reversed their deceleration, which, according to MSCI quarterly data, has seen All Property total returns fall from 18.5% in the year to Q2 2014 to 3.5% in the year to Q4 2016. The downward trend was attributed to both slowing rental growth and the adverse effect of yield impact on capital values. Whilst rental growth continued to dwindle to 1.9% for the quarter, the moderate capital growth of 0.6%, compared to the previous three quarters slight contraction, has been enough to improve total returns.

Capital growth has continued to increase in Q2 2017, average quarterly capital value growth being 1.1%, compared with 0.9% and 1.0% in the previous two quarters. The positive capital value growth figures suggest that the market has come to terms with the initial shock of the UK's EU referendum result, which caused capital values to slip into negative territory immediately after the vote.

### Total returns

Standard shops delivered returns of 6.3% in the year to June 2017, with growth for the quarter at 1.9% according to MSCI quarterly data. West End retail was the best regional performer in the sector for the quarter, with a return of 2.7%, ahead of City and Midtown retail at 2.2% and 1.5% respectively demonstrating the continued dominance of the central London retail market. Shopping centres and retail warehouses both had weaker quarters as their returns fell to 1.1% and 1.5% down from 1.3% and 1.7% respectively in Q1 2017.

Nationally, the office sector was the weakest performer of the three major sectors, returning 3.4% in the year to June 2017. City and West End both posted total returns below the average, at 3.3% and 3.1% respectively. Regional offices performed better, the best performing regions being the East Midlands and Wales, both at 7.3%, followed by Scotland returns being 6.2% and Yorkshire & Humber at 6.0%.

Industrial property was the best performing sector by a significant margin over the year to June 2017, continuing a trend since December 2015. Cumulative total returns for the year were 10.0%, whilst returns for Q2 2017 were 3.6%, the best returns for any sector since Q3 2015. London was the strongest performer in the industrial sector, returning 15.2% over the year and 5.3% in Q2. The other strongest performing regions were Eastern at 13.9%, South East at 13.6%, South Wales and West Midlands both at 10.4% and Yorkshire & Humber at 10.0%. Scotland was the weakest performer, returning just 3.0% over the year and 1.8% in the quarter. Total returns growth was 4.6% in the standard industrial segment, outperforming the distribution warehouse segment which grew by 3.4%.

### Rental growth

All property rental growth was 1.9% in the year to June 2017 and 0.5% in Q2 2017, according to MSCI quarterly data. The growth rate has remained largely static in the last 18 months, albeit at a lower level than the 0.9% quarterly average throughout 2014 and 2015.

West End retail had the greatest rental growth in the retail sector at 5.9% for the year to June 2017 and 1.5% over Q2 2017. This was followed by the Rest of London retail at 0.7% over the quarter, outstripping City & Midtown, where rental growth had fallen to 0.3%. On a nationwide basis annual retail rental growth fell to 0.9%, being the lowest growth rate since Q1 2015. Office rents grew by 1.5% in the year to June 2017 and by 0.2% in Q2 2017. City rental growth was 1.5% on an annual basis with growth of 0.1% in Q2. West End rental growth was slightly up at 2.1% and Midtown rents contracted by 0.8% for the quarter, dragging the annual rental growth down to -0.9%.

Outer London rents grew by 0.4% for the quarter, which translated into 2.3% on an annual basis. UK industrial assets delivered the strongest rental growth, being 4.3% for the year to June 2017 and 1.2% in Q2 2017. Standard industrial units saw average rents grow by 4.9% over the year to June 2017 and by 1.4% in the quarter; the respective figures for distribution warehouses were 3.1% over the year and 0.9% in Q2 2017.

### Yields

Equivalent yields continued to contract for the fourth consecutive quarter, contracting by 7bps in Q2 2017. The main driver for the yield contraction was the industrial sector which contracted by 31bps over the period. All property equivalent yields stood at 5.7% according to MSCI quarterly data, their lowest level since Q3 2007, as low interest rates continued to put downward pressure on investment income returns.

Retail equivalent yields were just 3bps higher than where they were 12 months ago at 5.6% in June 2017, with yield compression over the past three quarters cancelling out the expansion in Q3 2016. Whilst standard shops, 4.9%, shopping centres, 6.0%, and other retail at 5.0% experienced yield compression of 9bps, 6bps and 21bps respectively, average yields were pushed upwards by retail warehouses, 6.0%, and supermarkets, 5.0%, which experienced yield increases of 21bps and 8bps respectively.

Office equivalent yields expanded by 9bps over the year to June 2017, with average equivalent yields standing at 5.9%. The expansion pattern was similar to that of retail, also contracting in Q3 2016 and expanding for the following three quarters. The West End and Midtown experienced a contraction of 5bps and 12bps to 4.4% and 5.1%, whilst the City and most regional offices experienced yield expansion.

The industrial sector had the strongest yield compression as investor appetite for the asset class grew. Equivalent yields as reported by MSCI reached 6.0%, the lowest yield in the data available from MSCI. Industrial equivalent yields fell in the year to June 2017 across all regions barring East Midlands, where they climbed by 10bps to 6.3%. London equivalent yields contracted by 26bps to 5.3%.

**Fig 3. Total returns composition by sector – Year to June 2017**
Source: MSCI

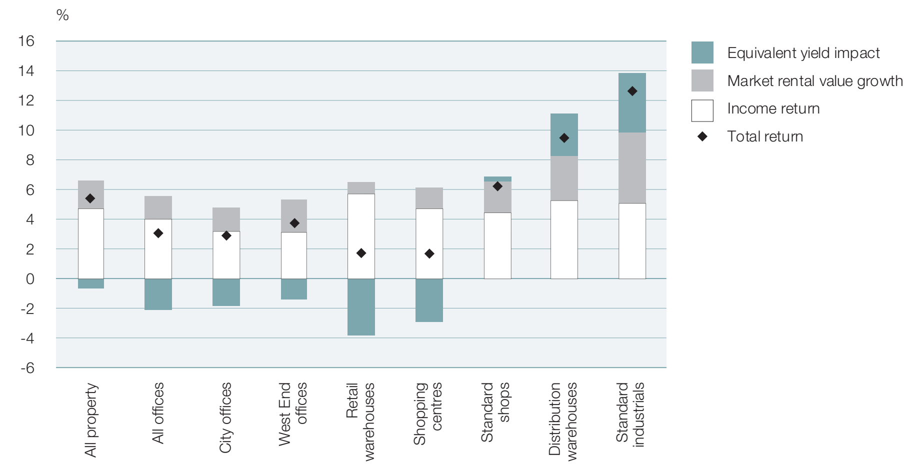



**Fig 4. All property rolling 12-month total return**
Source: MSCI

# 6.6%

**Gerald Eve Total Return forecast for 2017**

"Total returns will be driven by income returns over the next two years."

## FORECASTS

**Rental growth**

The immediate fundamentals for commercial property have not changed since our Spring 2017 issue. However, we have adjusted our forecasts for rental growth given the encouraging performance to date over 2017. The postponement of projects resulting from the Brexit factor will have a constraining impact on supply across the board, in both 2017 and 2018, which is a positive for rental growth.

Household real disposable income and consumer spending have gradually come under pressure, accompanied by weaker sentiment and consumer confidence, over 2017. Household goods sales have fallen-off as a result of a weaker housing market. The result is that occupiers are facing more fragile trading conditions, which does provide a less than encouraging backdrop for retail rental growth.

The outlook for the retail sector continues to remain challenging. With anticipated higher rates of inflation, real consumer expenditures will be weaker. Furthermore, a portion of the increased costs resulting from a weaker pound will most likely be passed onto consumers. The cost pressures will be further exacerbated by rate revaluations, especially in central London. All of this will have a negative impact on prospective rental growth.

West End office demand remains strong with availability below the ten-year average. Over the two years 2017 and 2018, the position regarding new office space supply is constrained. Some two-thirds of central London office space coming onto the market in 2017 is under offer or pre-let.

Whilst new office supply coming onto the market is likely to be delayed, and, taken together with the likely subdued demand for space, on balance we expect a fall-off in office rental growth over 2018 and 2019 compared with 2017. Regional office rental growth has remained relatively steady which we expect will continue.

Industrial rental growth continues to be strong across the UK, due to restricted availability of Grade A space, strong take-up and low vacancy rates. Strong demand for distribution warehouses from online retailers continues to drive rents positively, which we expect will continue.

Rental growth to date and the outlook for the remainder of 2017 suggests that, apart from standard industrials and distribution warehouses, rental growth across the other forecast sectors will be lower than in 2016, the pattern of lower growth continuing into 2018.

The West End and City office markets are expected to deliver negative rental growth in 2018, which we put at -0.8% and 1.2% respectively, with a little pick-up into positive territory in 2019. Given the, as yet unknown, potential impact of Brexit on City employment, the downside to our City office rental growth forecasts remains significant.

**Table 1. Rental growth forecast (%pa)**

| Sector | 2017 | 2018 | 2019 | Average 2017-21 |
|---|---|---|---|---|
| Standard shops | 0.8 | 0.6 | 0.8 | 0.9 |
| Shopping centres | 0.4 | 0.4 | 1.1 | 0.9 |
| Retail warehouses | 1.1 | 0.6 | 0.8 | 0.9 |
| West End offices | 1.0 | -0.8 | -0.9 | 1.5 |
| City offices | 0.8 | -1.2 | 0.3 | 0.8 |
| South East offices | 2.1 | 1.5 | 1.6 | 1.5 |
| Offices (all) | 1.1 | -0.3 | 0.5 | 1.0 |
| Standard industrials | 4.6 | 2.1 | 1.7 | 2.2 |
| Distribution warehouses | 4.4 | 2.2 | 1.9 | 2.3 |
| All property | 1.7 | 0.6 | 1.0 | 1.2 |
| | *(0.6)* | *(0.3)* | *(0.7)* | *(0.9)* |

Figures in brackets represent IPF Consensus Forecasts

**Table 2. Total return forecast (%pa)**

| Sector | 2017 | 2018 | 2019 | Average 2017-21 |
|---|---|---|---|---|
| Standard shops | 7.3 | 3.6 | 5.8 | 5.2 |
| Shopping centres | 3.3 | 4.2 | 5.8 | 5.2 |
| Retail warehouses | 6.0 | 4.7 | 6.5 | 5.5 |
| West End offices | 5.2 | 1.4 | 4.8 | 4.7 |
| City offices | 4.6 | 1.6 | 4.3 | 4.2 |
| South East offices | 8.0 | 6.0 | 6.0 | 5.2 |
| Offices (all) | 5.5 | 2.7 | 4.5 | 4.4 |
| Standard industrials | 11.7 | 6.3 | 6.0 | 6.7 |
| Distribution warehouses | 9.6 | 6.7 | 7.3 | 6.6 |
| All property | 6.6 | 4.1 | 5.6 | 5.3 |
| | *(4.8)* | *(4.1)* | *(4.9)* | *(5.2)* |

Figures in brackets represent IPF Consensus Forecasts

Over the period 2017-2021, we anticipate that distribution warehouses and standard industrials will deliver the highest annual average rental growth, being in the region of 2%.

Overall, we expect all property to deliver an annual average rental growth around 1% over the period 2017-2021. This compares with an average figure of 2% over the previous five years, 2012-2016.

**Total returns**
In its recent Financial Stability Report, the Bank of England (BOE) took the view that commercial real estate prices look stretched, 'based on a range of sustainable valuations.' The governor of the BOE commented that this makes commercial property '...vulnerable to a re-pricing whether through an increase in long-term interest rates, adjustments to growth expectations, or both.' We should be mindful that this assessment is based on a variety of assumptions, some debatable, including that yields revert 'to their 15-year historical average.'

On the investment front, international money continues to support the market, the impact of a devalued sterling having contributed. Regional markets have benefitted from local authorities investment.

The largest volume of transactions has been seen in the distribution warehouse sector. With yields remaining stable, this underlines the ongoing appetite for commercial property. We anticipate a continuation of demand for this sector.

The highest returns in 2017 will be delivered in the industrial and distribution warehouse sectors, being 11.7% and 9.6% respectively. Medium term, we expect these sectors to deliver the best performance.

We predict total returns for all property in 2017 to be 6.6%, outperforming the 2016 figure by some 2.7%. We anticipate lower all property returns in 2018, with a pick-up in 2019.

Overall, we currently expect all property to deliver an annual average return in the region of 5% over the period 2017-2021, being almost half the average annual figure over the previous five-years, 2012-2016. Essentially, total returns over the period 2017-2021 will be driven by the income component, with some rebound in values in the latter part of the five-year period.

**Fig 5. Historic and forecast five year annualised total return**
Sources: Gerald Eve, MSCI

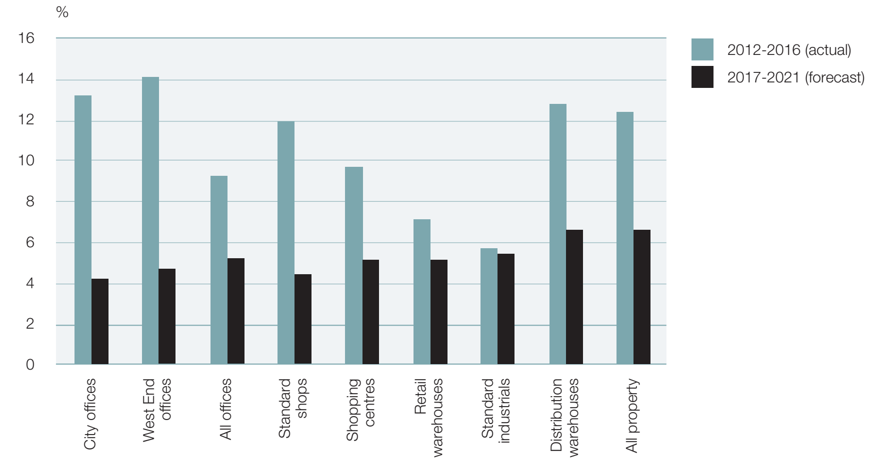
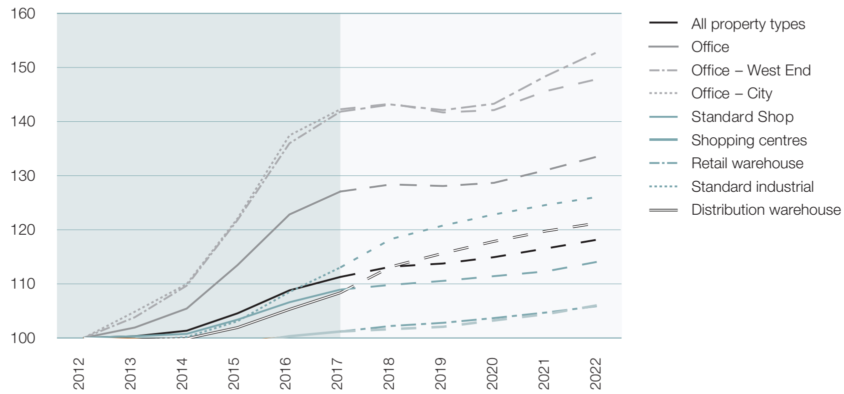



**Fig 6. Rental growth index (Jan 2012=100) to 2021 with GE forecasts**
Source: Gerald Eve, MSCI



" Strong demand for London offices… from European investors. "

" … 20 Fenchurch Street (Walkie Talkie) represents the UK's largest single asset property transaction at £1.3bn. "

## INVESTMENT & FINANCE

**West End Offices**

£192m of West End offices were traded in the third quarter of the year, which brings the overall transaction volume for 2017 to £2.6bn, a 5% increase on the same point last year according to Property Data.

Far Eastern investors have been very active during 2017 and continue to take advantage of the favourable exchange rate, with a number of significant investments across the West End, notably Sinar Mas Land's purchase of 33 Horseferry Road in Victoria. Brockton Capital sold their freehold interest in the building to the Indonesian conglomerate for £207.5m, reflecting a Net Initial Yield (NIY) of 3.7%. Two properties located in St James were also acquired by investors from Hong Kong. Chinese Estate Holdings purchased 11-12 St James's Square from Malaysia's Employees Provident Fund for £175m, which reflected a NIY of 4.4%, whilst Joint Treasure acquired 3 St James's Square from WELPUT for £135m.

Strong demand for London offices has also come from European investors, with Norges Bank Real Estate Management securing the largest transaction in Q3 2017 when it acquired an additional 25% stake in 20 Air Street from the Crown Estate for £112.5m. In addition, Union Investment Real Estate also purchased the Copyright Building in North of Oxford Street. The building, which is currently under construction, was sold by Derwent London for £165m and was fully let to Capita in 2016.

**City Offices**

Over £1.6bn of office space was transacted in the square mile in Q3 2017, a 20% increase on Q2 2017, and takes the overall volume for the year to £5.1bn.

The stand out deal of the quarter was for Infinitus Property Investment, a subsidiary of Hong Kong oyster sauce maker LKK Health Products Group, which bought 20 Fenchurch Street, widely known as the Walkie Talkie, for £1.3bn, reflecting a NIY of 3.4%. The transaction is the UK's largest ever single asset property deal, surpassing the £1.2bn paid by the Qatar Investment Authority to acquire the HSBC Tower in Canary Wharf in December 2014.

The dominance of investors from the Far East has been evident in 2017 following the sale of The Leadenhall Building to Hong Kong-based investor CC Land Holdings for £1.2bn earlier in the year. There were other key deals including Hong Kong based Tenacity Group, which acquired 70 Gracechurch Street, from Legal & General Investment Management for £271.4m, reflecting a NIY of 4.4%.

European investors have also been active in the City, with Deka-ImmobilienGlobal and WestInvest InterSelect's purchase of Cannon Place. The 418,000 sq ft building which sits above Cannon Street station was sold by Hines to the German funds for £485m, reflecting a NIY of 4.4%.

**Retail**

The retail sector saw approximately £4.4bn of investment in the first half of 2017 which reflects a 17% increase from the first half of 2016.

Prime yields for high street retail have been stable throughout 2017 and stand at approximately 4.0%. Prime high street assets in London remain the preferred location for investors resulting in competitive bidding for the limited available stock. Thor Equities' acquisition of 18 Conduit Street, occupied by Vivienne Westwood is evidence of this, purchased for £7m reflecting a NIY of 1.7%.

Two high street deals of particular note took place in Q2 2017. Knight Frank Investment Management were met with bidding competition for 35-38 George Street, Richmond but secured the transaction from LaSalle Investment Management (LaSalle IM) at a price of £21.3m equating to a NIY of 3.7%. British Land acquired 10-40 The Broadway, Ealing, a 1.4 acre mixed use site composed of 21 high street retailers for £49m reflecting a NIY of 3.9%. Both deals highlight the investor appetite for assets with strong retail pitches in Greater London.

There is continued demand for the best high street stock outside of London. This is demonstrated by Surrey County Council's £15.8m purchase of Debenhams, Winchester from LaSalle IM trading at a NIY of 4.2% and LaSalle IM's sale of Debenhams, Eastbourne to a private investor for £14.1m reflecting a NIY of 5.9%.

A total of 16 shopping centre transactions have completed in H1 2017 amounting to an aggregate value of £844m which marks a decrease in transaction volumes from H1 2016. Notable transactions include Invesco's (50%) purchase of Southside Shopping Centre, Wandsworth at a price of £150m reflecting a NIY of 4.5% and Frogmore's purchase of Stratford Shopping Centre for £142m representing a NIY of 5.5%.

Prime shopping centres in the regions also remain in strong demand demonstrated by Talisker Corporation's purchase of Friars Walk in Newport for £83.5m reflecting an NIY of 5.9%.

Market sentiment in the supermarket sector has improved in 2017 with the 'Big 4' reporting improved trading figures. Prime yields have hardened from 4.5% in H1 2016 to 4.25% in H1 2017. British Steel's purchase of Morrisons, Loughborough is testimony to this, transacting at £32.5m, a NIY of 4.25%.

**Fig 7. Sectoral cumulative rental growth 2017**
Source: MSCI

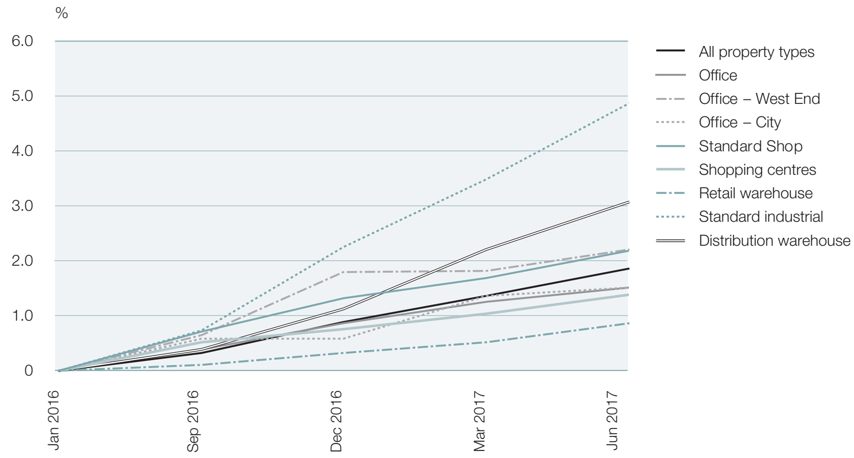



**Fig 8. Net investment by investor type – year to June 2017**
Source: Property Data

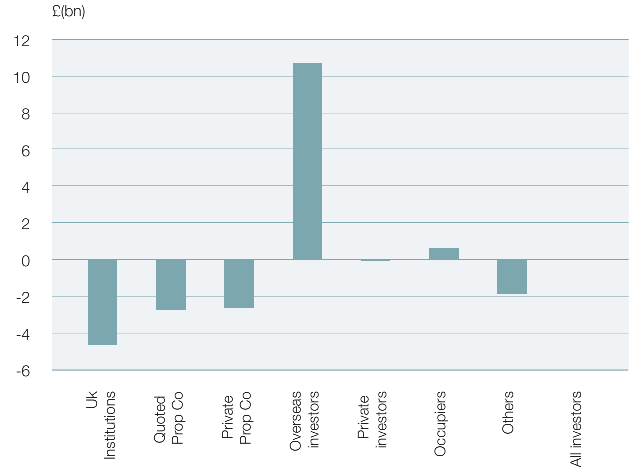
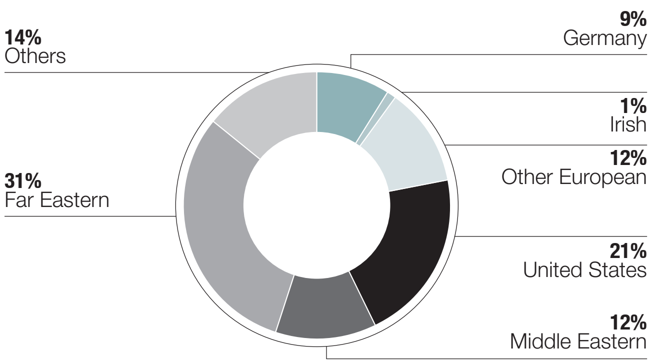



**Fig 9. Overseas investors – purchases year to June 2017**
Source: Property Data



" Whilst pricing (for industrial) is currently highly competitive the outlook for the sector remains positive…"

" Appetite for indexed-linked, institutional leases in the leisure sector has continued to gain momentum."

**Industrial**

There is still a significant weight of capital targeting the UK industrial sector, both for single and multi-let assets. Strong occupational fundamentals – rising rents, low supply and relatively limited levels of speculative development, together with the ongoing structural change to internet retail have resulted in strong levels of investor demand. A range of investors, including domestic institutions and property companies, overseas capital and even local authorities have been active over the last few months.

We have seen a strong increase in the volume of industrial property investment during 2017 – as almost £5.3bn traded, up on the £4.5bn which transacted during the first three quarters of 2016. Such a strong showing for 2017 has been driven by portfolio activity – we have recorded 25 industrial portfolios traded to the end of September – including nine individual deals over £100m.

There are a number of new entrants to the market keen to get large scale exposure to the UK industrial sector and during Q3 2017, we saw several private equity investors look to make the most of this increase in demand and crystallise higher returns through portfolio sales. Indeed, portfolio sales in the industrial sector have totalled £788m during Q3 – a large increase on the £120m portfolio sales agreed during the same period last year – driven in large part by Blackstone's £559m purchase of a light industrial portfolio from Brockton Capital in September.

As well as the Blackstone purchase above, London Metric purchased a portfolio of 14 assets from Cabot Properties for £116.6m, reflecting a 6.1% NIY. Tritax Big Box REIT continued to be acquisitive through their purchase of 50 ha of land for development at Littlebrook for £65m and Royal Mail's Midlands RDC at Atherstone for £32.7m, reflecting a 6.1% NIY.

Demand for prime multi-let investment opportunities also remains strong as evidenced by an undisclosed purchaser purchasing the three ac Zennor Road Industrial Estate in London for £30m, reflecting a NIY of 2.9% and reportedly at an 84% premium to the March 2017 valuation.

Whilst pricing is currently highly competitive, the outlook for the sector remains positive, with investors continuing to be attracted to the strong occupational dynamics. Such is the strength of demand, that there could be further inward yield movement in core locations before the year is out despite yields already sharpening in most locations since the start of 2017.

**Leisure**

2017 has been a strong year for the Leisure sector so far, following on from the increased transactional volumes in 2016. Appetite for indexed-linked, institutional leases in the leisure sector has continued to gain momentum. This was reflected in terms of transaction volumes and yield compression back to pre-2007 levels.

The market was initially led by foreign investment benefiting from the post Brexit exchange rate adjustments, seeking post Brexit bargains. However, 2017 (and Q4 2016) has witnessed the return of UK institutional investors and dollar-pegged funds, which saw the largest uplift in transactional activity. Councils have also invested heavily, especially within their own districts in part due to the cost of borrowing and returns. The weight of money has seen yields continue to compress to record levels.

In addition, the underlying operational leisure sector has remained strong with the provincial hotel sector showing continued RevPAR growth.

In merger and acquisition activity, the largest transaction saw Punch Taverns agree to the joint takeover bid from Heineken and Patron Capital, at 180 pence per share, or £403m, totalling approximately 3,000 pubs. This deal was approved by the regulators following Heineken pledge to sell off 33 pubs by the end of the year. Other activity includes Stonegate's acquisition of Sports Bar and Grill bringing the total estate to 703 sites. Stonegate have also placed a conditional offer to acquire Revolution Bars Group, valuing the business at circa £100m (£2 per share), it is understood that this is the front running bid for the company. This activity further demonstrates large firms seeking to benefit from economies of scale, returning to the days of vertical integration.

In terms of investment, yields continue to compress to record levels. In March, Gerald Eve advised on the acquisition of the enhanced ground rent at Park Plaza Waterloo, which was acquired by CBREGi at a NIY of 3.25%. Additionally, Gerald Eve advised on the NFU Premier Inn portfolio, which reflected a NIY of 4.4%. Other recent activity has seen the Travelodge Southwark sell for a reported NIY of 3.35% which Gerald Eve also advised on and the Travelodge Brighton reportedly under offer at a sub 4% yield.

**Fig 10. Sectoral total UK investment – year to June 2017**
Source: Property Data

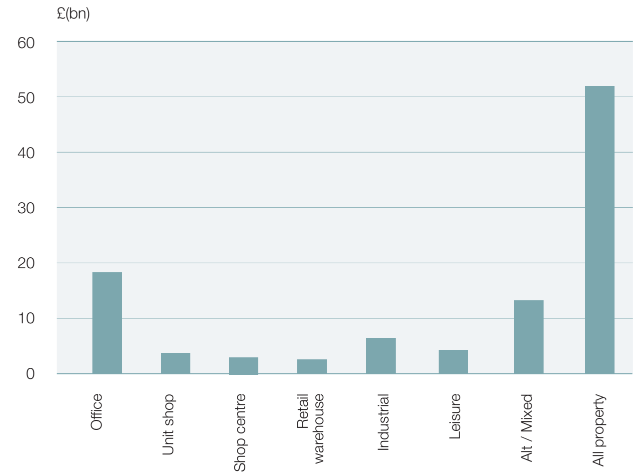



**Fig 11. Hotel room and occupancy rates**
Source: STR Global

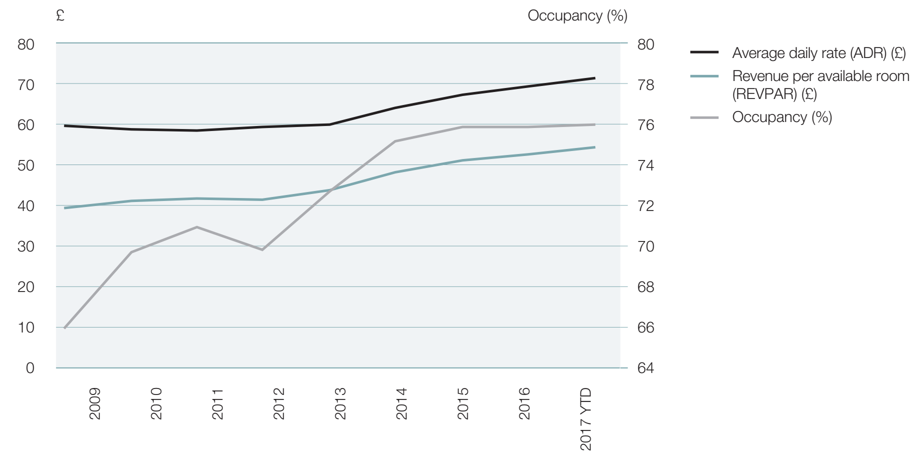



**Table 3. Key leisure investment transactions**
Source: Gerald Eve

| Property | Location | Reported price £ | Reported NIY, % | Tenant |
|---|---|---|---|---|
| Park Plaza Waterloo | London | 161,500,000 | 3.25 | Park Plaza |
| Travelodge Southwark | London | c.50,000,000 | 3.35 | Travelodge Hotels Limited |
| NFU Portfolio | London | 37,950,000 | 4.40 | Premier Inn Hotels Limited |
| Mecca Rochdale | North West | 3,600,000 | 8.70 | Mecca Bingo |
| Mecca Leeds | Yorks & Humberside | 4,120,000 | 7.50 | Mecca Bingo |
| Library Members Club | London | 9,300,000 | 2.50 | Independent |

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Useful web links
Gerald Eve research derives some of its information for the production of Invbrief from the following sources:

www.swaprates.co.uk
www.bankofengland.co.uk
www.ons.gov.uk
www.treasury.gov.uk
www.dti.gov.uk
www.cebr.co.uk
www.oanda.com
www.ipf.org.uk
www.ipd.com
www.propertydata.com
www.property-week.co.uk
www.chamberonline.co.uk

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