An MSCI Brand

Real Estate Auctioneering & Investment

IPD/Acuitus Commercial Property Auction Data (cPad) Auctions report

for Q3 2014

Published September 2014

Welcome to the latest Commercial Property Auction Data (cPad) Market Flash which analyses the £134.5 million of commercial property assets that sold at auction during July 2014.

Statistical analysis of the July commercial property auctions is always a very useful reference point before the final quarter of the year which does so much to set the tone for the year to come.

The message from the latest round of auctions is generally positive with volumes, sale rates and average lot sizes all increasing.

However, most interesting is perhaps the narrowing yield gap between assets with lease lengths of over 16 years or more and those with shorter term income. To date, investors have clung steadfastly to the prospect of greater security of income and have priced it accordingly.

However, the sharper yields achieved by assets with shorter income profiles would seem to indicate that investors are now more prepared to take a positive view of assets that may require active management but are not perceived to present as much risk as previously.

Similarly, in the July auctions the average yield for the lower quartile (prime) assets sharpened by 10 basis points (bp) from their May level while the upper quartile (secondary) average yield came in by 80bp.

We hope you find this cPad Market Flash useful and would be pleased to discuss any of the points that it raises.

Key stats

64%

increase in sales volume year-on-year

£623,000

Average lot price up

81%

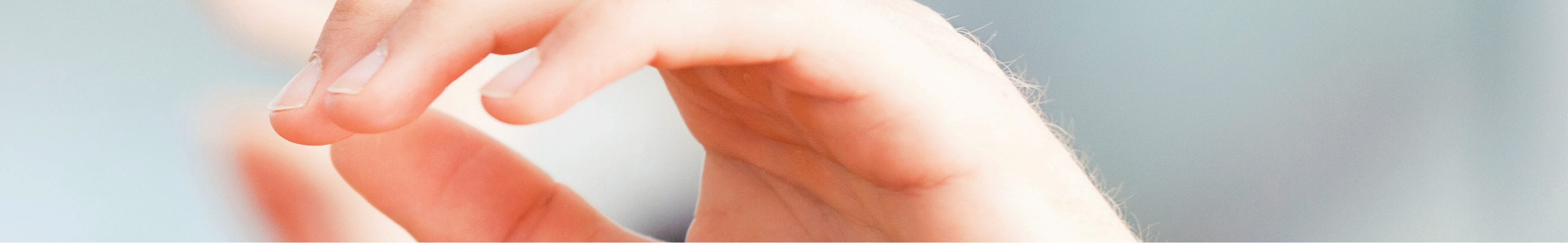
Sales rate up

8.1%

All property average yield

cPad

cPad is a joint initiative between Acuitus and IPD utilising auction sales data from EIG to provide a unique perspective on the commercial property market for private investors and private property companies. The aim is to create a valuable snapshot of today's market and help investors shape their future investment strategy.



In the auction room

Volumes and sales rates up as stock is released

The rate of sales volume growth in the auction room regained its very strong momentum in July, increasing by some 64% year on year to £135 million. This follows a slowdown in the rate of annual growth to 24% in May as the wider investment market paused. Increasing business confidence in the durability of the economic recovery both domestically and internationally is reflected in increasing investor appetite for good quality, higher yielding assets.

Strengthening demand and increased risk appetite is stimulating the supply of investment stock to the auction room, particularly financially distressed assets that offer good active management opportunities. Although, sales volumes in the May and July auctions have been on a par historically, the volume of sales in the latest July auction is some 34% higher than achieved this May.

The sales rate also rebounded to 81% in July. Excepting May, when the sales rate reverted to around its trend rate of 70%, the success rate in the auction room has been above trend since December 2012. The more recent variability stems from activity in the retail sector which represents the largest proportion of assets at auction by both number and value.

The sales rate for retail jumped to 81% in July following a sharp decline to 68% in May, which had been principally as a result of unrealistic pricing of locationally impaired assets in the wake of a revival of the wider retail market. The increased sales rate for the sector in July reflects the stronger locational characteristics. The average (mean) value of retail lots remained broadly stable at £560,000.

Due to the impact of a small number of very large lot sizes, the mid-point value (median) provides a more useful indication of the average price achieved. Interestingly, the mid-point value increased by 12.4% to £392,500. This supports the assertion that the higher sales rate was achieved due to an improvement in the quality of stock rather than re-pricing of poorer quality assets. Although total sales volumes for retail increased by 48% year-on-year and by 21% on that achieved in May, the sectors, share of total sales declined to 65% from 72% in both the previous year and the previous auction in May.

In contrast, the office sector increased its share of total sales to 19% in July, up from a mere 8% in May. The increase in office sales volumes proportionately is all the more remarkable given the strong growth in total sales; the office sector enjoyed a larger slice of a considerably bigger pie. As a result, sales volumes increased to £25 million, representing growth of 78% year-on-year and a staggering 205% relative to May. Activity in the leisure sector remains buoyant and with sales volumes increasing in line with total sales, its share of sales at auction remained stable at 13%.

The concentration of assets located in London increased to 30% in July from 21% in May and together with improved quality of stock, underlies the rebound in the sales rate.

Nevertheless, while assets located in London enjoyed a significantly higher sales rate of 95%, the sales rate for regional assets climbed from 69.4% in May to 78.2% in July. While the higher demand for investments within London persists, greater economic certainty is widening investor appetite for good quality assets in regional markets.

Commercial property auction sales summary

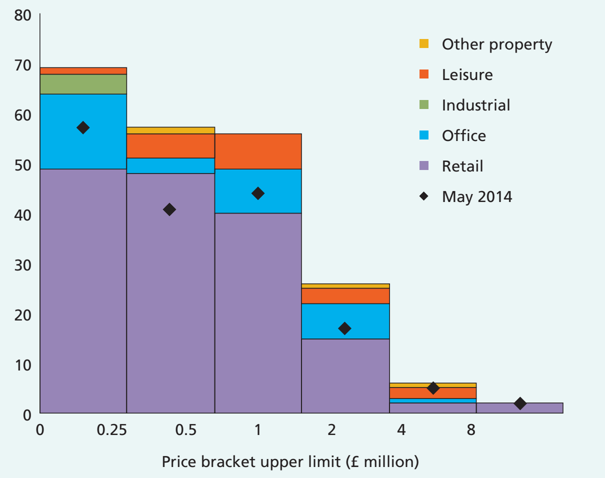
Sector		July 2014	May 2014
Volume (£ million)	▲	134.6	99.8
Properties sold	▲	216	166
Average lot size (£)	▲	622,965	601,140
Sales rate	▲	81.0%	70.3%

Commercial property auction sales, £ million

Sector		July 2014	May 2014
Retail	▲	87.4	72.1
Office	▲	25.0	8.2
Industrial	▶	0.4	0.4
Leisure	▲	17.7	13.0
Other	▼	4.0	6.1
Region		**July 2014**	**May 2014**
London	▲	40.3	21.1
Rest of UK	▲	94.3	78.7

Commercial property auction sales rate, %			
Sector		**July 2014**	**May 2014**
Retail	▲	81%	68%
Office	▶	81%	81%
Industrial	▲	100%	50%
Leisure	▼	72%	80%
Other	▼	75%	88%
Region		**July 2014**	**May 2014**
London	▲	95%	80%
Rest of UK	▲	78%	69%

Commercial property auction sales by price band



In the market

Yields sharpen across the board

The all property average yield fell by 29 basis points (bp) to stand at 8.1% in July. The office sector enjoyed the strongest inward yield movement, with the average office yield compressing by 190bp to 8.8%. Retail and leisure yields hardened by 40bp to 7.8% and 7.9% respectively.

Although this represents the lowest level recorded since July 2011, there are significant differences between the structure of sales comprising the May and July auctions in 2014. These suggest that the average yield shift recorded in July may understate the underlying market trend. The retail sector's share of total sales in the recent auction in July is below trend and the office sector is above trend.

Although the office sector experienced a stronger average yield movement, it remains higher yielding than the retail sector. Thus, the all property average yield for July is elevated by the stronger weighting of the higher yielding office sector, despite the stronger yield compression within that sector.

Similarly, the yield compression recorded between May and July should be considered in the context of the overall improvement in the quality of stock offered for sale in July, which would of course be lower yielding, relatively.

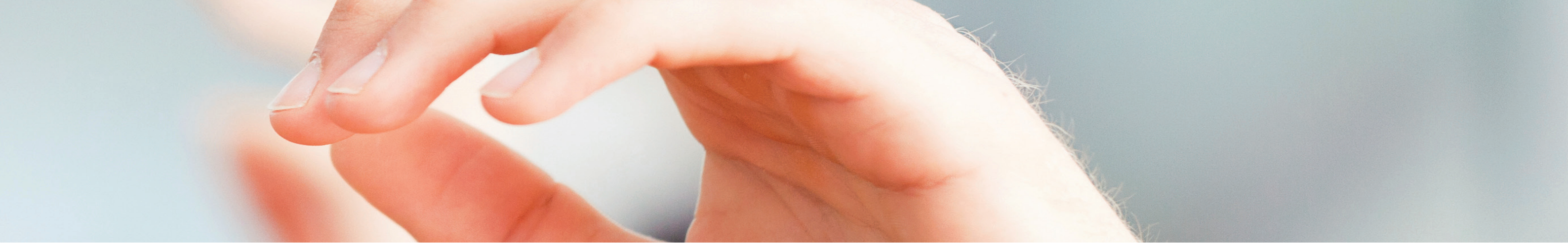
Indeed, analysis of yields achieved by the lowest (prime) and highest (secondary) yielding 25% of assets sold indicates that yields for the prime segment of properties at auction remained broadly stable at 6.3%, while yields for more secondary assets compressed by 80bp to 9.0%. What is more difficult to discern is whether this yield shift represents a higher quality of stock within the secondary segment in the July auction relative to May, or an increasing risk appetite for active management and/or mispricing opportunities. Most likely, it is a combination of both.

Analysis of yields by unexpired term indicates that the strongest yield compression occurred for assets with the shortest unexpired term, which compressed by 150bp to 9.5%. This suggests that given the strengthening economic outlook and improving occupier markets, investors are seeking active management and/or mispricing opportunities, albeit selectively. While risk appetite for redevelopment and tenant engineering opportunities has increased, it is strongly focused on strong locations and/or good quality assets.

Of course, income security is a critical determinant of investment value. Assets offering an income stream of over 16 years command a considerably lower yield of 7.2%. The strong yield compression occurring for short-leased assets should also be considered in the context of the wide spread that has persisted with income-secure assets since the onset of the downturn.

Despite more recent yield compression, assets with an unexpired term of less than five years continue to offer a 230bp spread over assets at auction with an income stream of over 16 years. The improved economic outlook is assisting the recovery of non-prime investment markets and investors are gradually gaining the confidence to exploit such mispricing.

As would be expected, the London yield is significantly lower than the Out-of-London yield with a current yield gap of 220bp. The London yield has hardened slightly to 6.30% with the Out-of-London yield remaining unchanged at 8.50%.



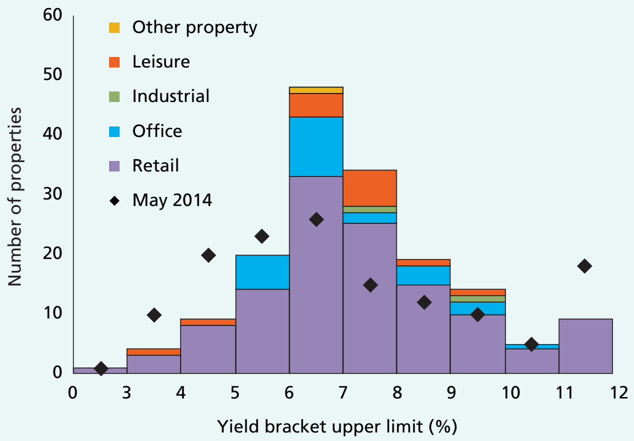
Yield summary			
All commercial property totals		**July 2014**	**May 2014**
Average initial yield	▼	8.1%	8.3%
Lower yield quartile	▲	6.3%	6.2%
Upper yield quartile	▼	9.0%	9.8%
Yield by unexpired lease term			
0-5 years	▼	9.5%	11.0%
6-15 years	▼	8.3%	8.6%
16 years +	▲	7.2%	6.7%

Yield summary			
Yield by value band		**July 2014**	**May 2014**
£0 - £250,000	▼	9.0%	9.8%
£250,000 - £500,000	▼	7.9%	8.6%
£500,000 - £1 million	▶	7.9%	7.9%
£1 million +	▲	7.5%	6.2%

Yield summary by sector			
Sector		**July 2014**	**May 2014**
Retail	▼	7.8%	8.2%
Office	▼	8.8%	10.7%
Industrial	▲	10.4%	10.1%
Leisure	▼	7.9%	8.3%
Other	▲	10.9%	5.4%

Yield summary by region			
Sector		**July 2014**	**May 2014**
London	▼	6.3%	6.5%
Rest of UK	▶	8.5%	8.5%

Yield summary by yield band



UK retail market analysis

Closing gap between prime and secondary markets?

The first half of the year has seen relatively strong capital value growth across all sectors in the UK and the standard retail sector is no different. Whilst the retail sector continues to lag behind the office and industrial sectors, encouraging signs continue to emerge from the High Street. July saw a continuation the strong value growth as both office and industrial sectors increased by 1.33% month-on-month and 1.25% month-on-month respectively. Although the retail sector recorded less substantial capital growth at 0.85% month on month, growth has remained positive for the last 12 months. With overseas investment into the prime retail assets in central London remaining a dominant driver behind value growth in London.

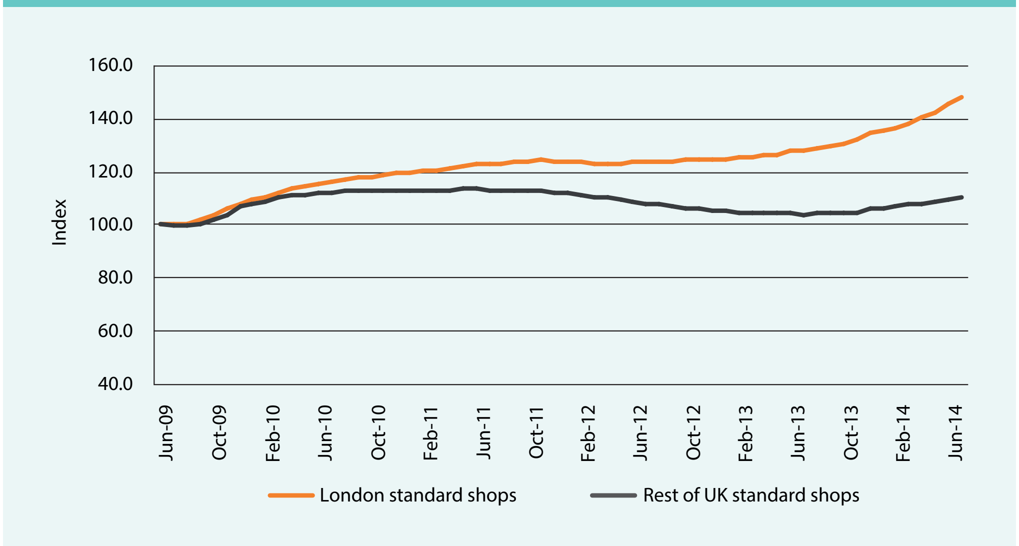
There continues to be a performance differential between London and regional High Street assets, however, the difference continues to converge. Growth across the UK was driven primarily by standard retail assets within London, which saw quarterly growth levels of 5.41% quarter-on-quarter in comparison to the 2.46% quarter-on-quarter experienced across the remainder of the nation.

Despite the limited capital value growth in comparison to other sectors investors can still find optimism in the increasing scope of value growth within the UK retail sector; which begun its recovery from a much lower base. The six months to July 2014 recorded capital growth figures across the UK standard retail sector at 3.73%, a four year high. The same six month time period also saw a flat rental value growth across the retail sector for the first time since 2008, bucking the long standing trend of negative growth. These figures add weight to the continued assertion that the retail sector's recovery has gathered pace and that there has been a real upturn in consumer confidence and retail sales, a trend that could well continue throughout the remainder of the year.

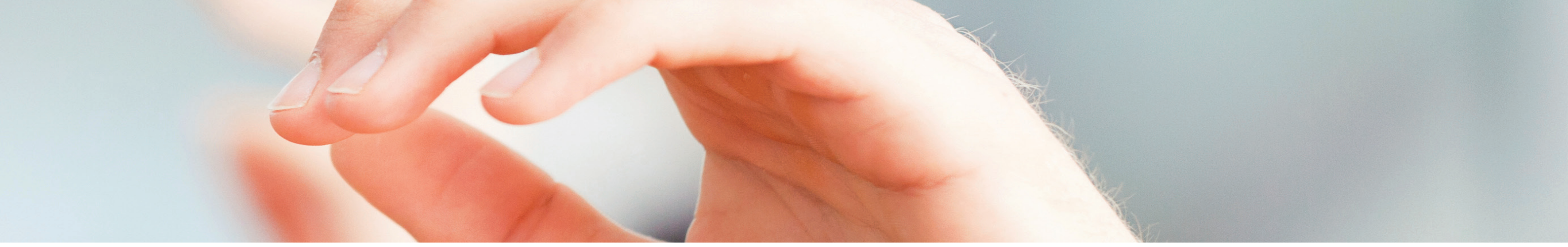
Over the course of the year, regional differences have been more apparent. Capital values grew by 15.58% year-on-year in London and standard retail values for the rest of the UK grew by 6.48% year-on-year. Although the rest of the UK continues to grow at a lesser rate, this figure is a clear jump on those previously experienced and the concept of the convergence in valuation movement between London and more regional standard retail assets is more apparent.

The improving health of retailers continues to drive investor sentiment into high street retail assets. Positive capital value growth of 1.02% quarter-on-quarter for secondary in the quarter to June 2014 also provides a real indication of a growing optimism for lower quality assets. Yields have also hardened for secondary assets as well as prime. However, whilst there has been an upturn in investor sentiment, depth of demand for high yielding assets is still fragile with investors remaining risk aware. Investors who have delved into the secondary market have tended to specifically concentrate on assets which have the potential for sustainable long-term income. That said, over time, sustained value growth in the secondary market coupled with accurate pricing and appropriately factored income risk, will further enhance the appeal of High Street assets.

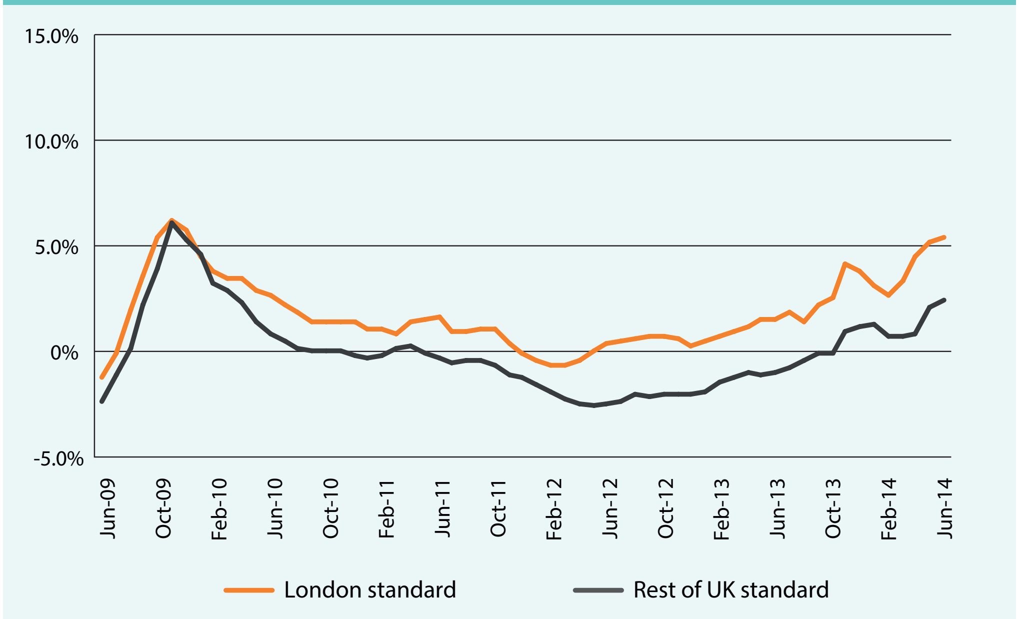
Standard shops capital value indexes by region, monthly



Source: IPD UK Monthly Property Index

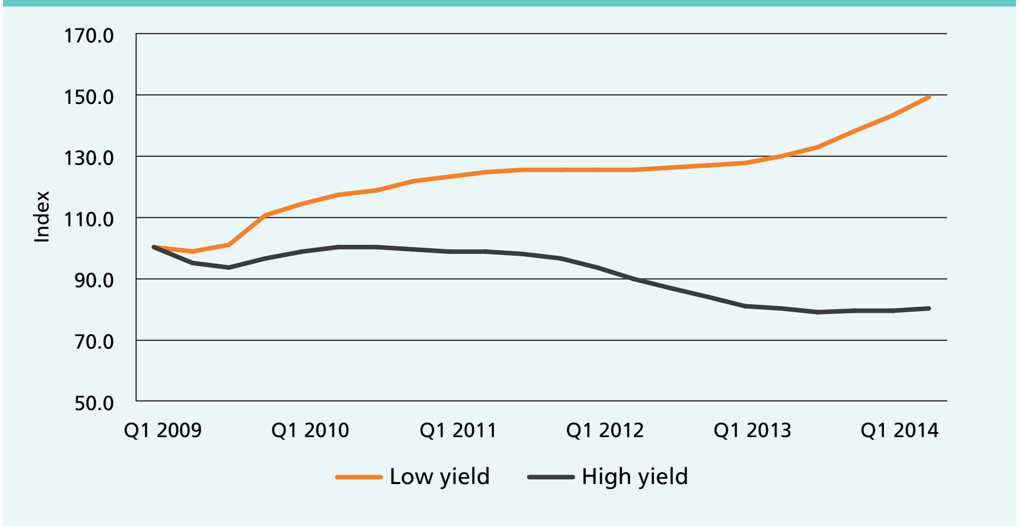


Standard shops three-month rolling capital value change, %



Source: IPD UK Monthly Property Index - repeat for all following refs

Standard shops capital value indexes by yield, quarterly



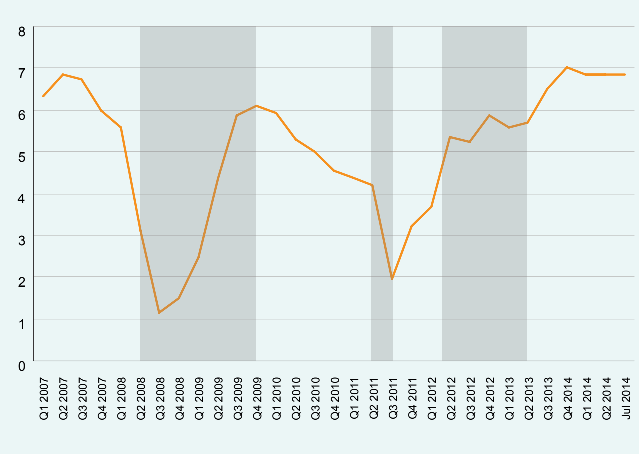
Source: IPD UK Quarterly Property Index

Economic score card

Economic score card average

Optimism in a slowly but surely growing economy have remained the common theme of the year to date, and the scorecard average remaining at 6.8 supports such optimism. Inflation being again the only indicator to score six as it fell a further 30 basis points to 1.6%. Inflation however still remains higher than wage rate growth. Unemployment has continued its slow decline and is now at its lowest point for six years.

Economic score card average

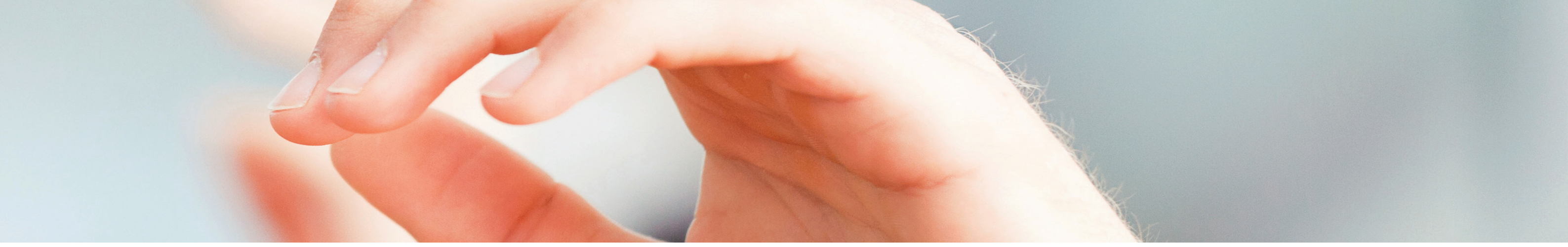


	2007				2008				2009				2010				2011				2012				2013				2014		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	May	July
Economic score card average	6.3	6.8	6.7	6.0	5.6	3.1	1.1	1.5	2.5	4.4	5.9	6.1	5.9	5.3	5.0	4.5	4.4	4.2	2.0	3.2	3.7	5.4	5.2	5.9	5.6	5.7	6.5	7.0	6.8	6.8	6.8
Inflation (CPI y/y)	4	6	7	7	6	2	1	4	5	7	5	5	3	4	4	2	1	1	1	1	3	6	7	5	5	5	5	7	6	6	7
FTSE All-Share (q/q)	7	7	6	7	4	5	1	1	5	7	7	7	7	5	7	7	7	7	2	7	7	7	7	7	7	6	6	7	7	7	6
Nationwide House Price Index (q/q)	6	7	6	5	2	1	1	1	3	7	7	7	6	6	4	4	6	5	4	5	4	4	5	5	5	6	7	7	7	7	7
Consumer confidence	7	7	7	7	6	1	1	1	1	2	6	6	7	5	3	2	1	3	1	1	1	1	2	3	2	3	7	7	7	7	7
Unemployment expectations	7	7	7	7	7	5	2	1	1	1	3	4	5	4	3	3	2	4	4	2	4	5	6	7	7	7	7	7	7	7	7
Retail trade confidence	7	7	7	5	7	4	1	1	1	4	7	7	7	6	7	7	7	5	1	4	3	7	4	7	6	6	7	7	7	7	7
Expected retail trade	7	7	7	4	7	4	1	1	1	2	6	7	7	7	7	7	7	5	1	3	4	7	5	7	7	7	7	7	7	7	7

Source: IPD, ONS, EcoWin, Nationwide

Score card key

7	6	5	4	3	2	1
Fully functioning market		Partially functioning market		Impaired market function		Severely impaired function



Economic score card variables	Score	Jul 2014	10-yr avg	Analysis
Economic score card average	6.8	6.8	5.3	The economic score card average rose to its highest level in July 2014 as the UK economy recovers to what is considered close to a 'fully functioning market'. The strong position is representatives of the improvements in the broader UK economy as consistent growth continued nationwide. The score of 6.8 at the end of July was consistent with the May statistic meaning that this marker for the UK economy remains well above the 10-year average of 5.3. This was further evidenced by the healthy 0.8% q/q GDP growth in the UK during the three-months to the end of June 2014, as UK exports seem undeterred by the crisis in Ukraine and the sanctions on Russia which have had little impact on UK trade.
Inflation (CPI y/y)*	6	1.6%	2.7	Recorded inflation continued to fall below the Bank of England's target rate of 2.0% in July 2014. The represents a fall that was more than expected for July as the cost of clothing, footwear, food and non-alcoholic drinks eased further. Crucially, with inflation now running at a level comfortably below the 2.0% target, the Bank of England has little need to adjust interest rates to tame inflation, meaning investors may find reassurance in continuing 'business as usual' pattern for the UK investment property market.
FTSE All Share (q/q)	7	0.2%	2.2%	The UK Equities market has witnessed a distinct moderation in quarterly growth levels in the three months to the end of July. Returns across Europe fell back due to concerns emanating from Russia and the Ukraine which have cautioned markets. For the UK this is despite the fact that Russian sanctions have, so far, had little effect of UK trade but as further financial sanctions are implemented the situation is likely to change. As a result, international fears continue to weigh on certain sectors, particularly for commodities, and as the situation in Ukraine worsens, reverse sanctions from Russia are likely to affect European trade, especially for agriculture and food. Additionally, growing concerns in the Middle East have impacted performance with growing instability in the region.
Nationwide House Price Index (q/q)	7	0.8%	0.0%	National house prices had been resurgent in recent months, but the level of growth moderated significantly during the summer of 2014, with monthly value growth falling from 2.4% in May to 0.8% in July, as market uncertainties weigh. Indeed, the Building society which is responsible for one of the most authoritative and long-running house price indices, has sounded its most cautionary note in years claiming the outlook was "highly uncertain". However, the cautious message came as index showed consistent monthly increases in house prices which have pushed annual price rises up to 10.6% to the end of July 2014.
Consumer confidence	7	4.8	-11	UK consumer confidence fell for the first time in six months during the month of July, suggesting that consumer attitudes are less upbeat that expected about the burgeoning economic recovery although this decline may also be attributed to the summer lull, as the indicator picked up significantly in August.
Unemployment expectations**	7	4	34	Unemployment has continued to fall through the 2014, with the rate falling to 6.4% by the end of June. The figure is at its lowest level is almost six years according to the ONS. However, total pay growth is still marginal, at 0.3% in the year to July, making it the lowest growth rate since 2009. Significantly, the youth jobless rate (16 to 24-year-olds) which had struggled to improve dropped to 16.9%, down from 17.8% in March.
Retail trade confidence	7	15	-1	Retail sales in the UK weakened for the second month running in July 2014 as the supermarket price war hardened and continued low levels of food price inflation meant shoppers are spending less on food. Like-for-like sales were down 0.3% compared to July 2013, with much of this decline again driven by declining food sales as non-food sales continued to strengthen, up 2.4% in in July 2014 compared to the same month last year.
Expected retail trade	7	15	8	Expected retail trade continued to strengthen in July on the back of the improving economic indicators for the UK, albeit with a weaker positive score of 15 down from 40 recorded in May when pre-summer optimism was high. While levels have moderated, performance remains well ahead of the long term average score of 8.

* Scoring is based upon deviation (either above or below) from the Bank of England's target CPI rate of 2%

** Scoring is inverted. e.g. high value equals low score.

Sources: IPD, ONS, EcoWin, Nationwide

For further information on cPad or the services provided by Acuitus, IPD and EIG, please contact:

Acuitus

Richard Auterac
Chairman and Auctioneer
+44.20.7034.4851
richard.auterac@acuitus.co.uk

Acuitus Real Estate
Auctioneering & Investment
14 St.Christopher's Place
London W1U 1NH
acuitus.co.uk

IPD

Frederick Newman
Research Operations, UK and Ireland
+44.20.7336.9364
frederick.newman@ipd.com

IPD | An MSCI Brand
Ninth Floor
Ten Bishops Square
London E1 6EG
+44.20.7336.4783
enquiries@ipd.com
ipd.com

EIG

David Sandeman
Managing Director
+44.1737.232289
davids@eigroup.co.uk

Essential Information Group -
The Property Auction
Information Specialists
9 Castlefield Road
Reigate
Surrey RH2 0SA
eigroup.co.uk

All data, graphs and charts sourced from IPD