COMMERCIAL PROPERTY AUCTION DATA (CPAD) REPORT SUMMER 2017

Prepared by MSCI in association with Acuitus

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INTRODUCTION

Welcome to the MSCI /Acuitus cPAD report reviewing activity in the commercial real estate auction market. The report is underpinned by analysis of the long running Commercial Property Auction Data (cPad) series, which provides transaction based market prices. This, combined with performance trends in the wider IPD/MSCI UK investment universe, is used to develop a view of current market conditions for private investors, and more importantly the outlook for the remainder of 2017.

The second of this year's action rounds, ending in late May, were held against the backdrop of yet further political uncertainty. The snap election did little to bolster investor confidence across the market. However, even before the Prime Minister's election announcement, the market was seeing greater caution. UK investor activity slowed, although overseas investors, benefiting from the weaker pound, took up some of the slack in the prime market.

This year market activity saw a slight downturn compared with the previous two years. Investment grade assets transacted through the auction room stood at over £145 million, 6% down on the same point in the previous year. Overall private investors purchased £650m of real estate assets for the 3 months to the end of May 2017 (Property Data), of which over a fifth were investment grade assets bought in the auction room.

Increased caution in the market generally was seen in a slightly lower sale rate of 76%, marginally below the long run average. We predicted in the spring cPad report expectations of a stabilisation of prices during 2017. This was evident in the May auction round with the cPad All Property Rolling Average Yield (RAY) rising marginally in May to 8.29%, albeit still reflecting a fall of 10 basis points (bp) over the last 12 months.

The market saw some opportunistic buying with a relatively stronger sale rate for London assets. The capital accounted for almost a fifth of total transactions by value, almost three times the level seen this time last year. Properties with a positive income or added-value story also sold well. Certainly the attractive income return offered by the industrial sector continues to appeal to buyers. This, combined with the improved quality of industrial assets now sold in the auction room, drove a further sharp inward yield movement for industrial investments.

Looking ahead, it is likely prices for everything apart from the best quality will remain difficult to predict over the coming year as a result of the current economic and political uncertainty. In the transparent auction room environment we expect private investor demand to remain firm for institutional quality assets delivering a solid return or growth potential during this period of uncertainty to persist. We hope you find this cPad commentary useful and would be pleased to discuss any of the points it raises.

KEY STATS

▲ **8%**

Increase in the number of assets sold in May 2017 compared with same period 12 months earlier

▲ **10%**

Increase in the average retail asset lot size in May 2017 compared with the previous auction round

▲ **151%**

Increase in value of London assets transacted in May 2017 compared with May 2016

▼ **8.29%**

Rolling Average All Property Yield down 10bp in 12 months to May 2017

cPad is a joint initiative between Acuitus and MSCI 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 MARKET*

Over £145m of commercial real estate assets were sold in the May auction round, 6% down on the same period in 2016. The number of lots sold in the room totalled 256, an increase of 8% on the previous 12 months.

INCREASING IMPORTANCE OF THE AUCTION ROOM FOR £2M+ ASSET SALES

A fall in average lot size masks the wide range of stock transacted in the room. In fact the latest cPad Index shows a marked increase in the number and proportion of assets over £2m sold by auction. In excess of 6% of assets by number sold at over £2m, the highest proportion since the start of the cPad Index, with the exception of October 2015. The number of high value assets in the auction room started to rise in autumn 2016. Banks and institutional investors are opting for auction room sales to maximise value in the execution of their disposal and restructuring strategies.

The higher value stock includes both retail and office assets. At the lower end of the market, retail continues to dominate, but other assets, including land, storage and institional residential, are also well represented. Overall, the retail sector accounted for 72% of sales by value, ahead of the long run average.

In contrast, the number of office properties sold in the latest auction round was slightly lower than has been the case over the last year.

The sales rate during the May auction period averaged 76%, a lower level when compared with recent auction cycles. In recognition of the uncertain economic backdrop, assets with a long income profile and asset management opportunities sold well. This is illustrated by an 87% sale rate for industrial assets, with a strong performance seen across the value bands.

OPPORTUNISTIC BUYING IN LONDON

Over 80% of sold assets by value were located outside London during the May auction round, with an average lot size of over £0.5m. London assets saw a relatively high level of activity. A sale rate of 83% was achieved with an average lot size of £1.14m. The upturn in London asset investment in part reflects a desire by funds to disinvest from smaller assets and a concern over the weakening outlook for prime institutional property in the Capital. Traditional fund and property company investors are more cautions and sellers have been starting to tap the potentially wider auction market place, which has better access to new investors. Buyers continue to seek real estate investments, perhaps cognisant of likely ongoing volatility in the financial markets.

COMMERCIAL PROPERTY AUCTION SALES SUMMARY

SECTOR		MAY 2017	MAR 2017
VOLUME (£ MILLION)	▼	145.4	193.9
PROPERTIES SOLD	▼	256	331
AVERAGE LOT SIZE (£)	▼	567,875	585,684
SALES RATE	▼	76.0%	86.2%

COMMERCIAL PROPERTY AUCTION SALES (£ MILLION)

SECTOR		MAY 2017	MAR 2017
RETAIL	▼	104.7	116.1
OFFICE	▼	16.4	31.0
INDUSTRIAL	▼	4.5	9.7
LEISURE	▼	10.5	17.2
OTHER	▼	9.3	19.8

REGION		MAY 2017	MAR 2017
LONDON	▲	27.3	20.9
REST OF UK	▼	118.1	173.0

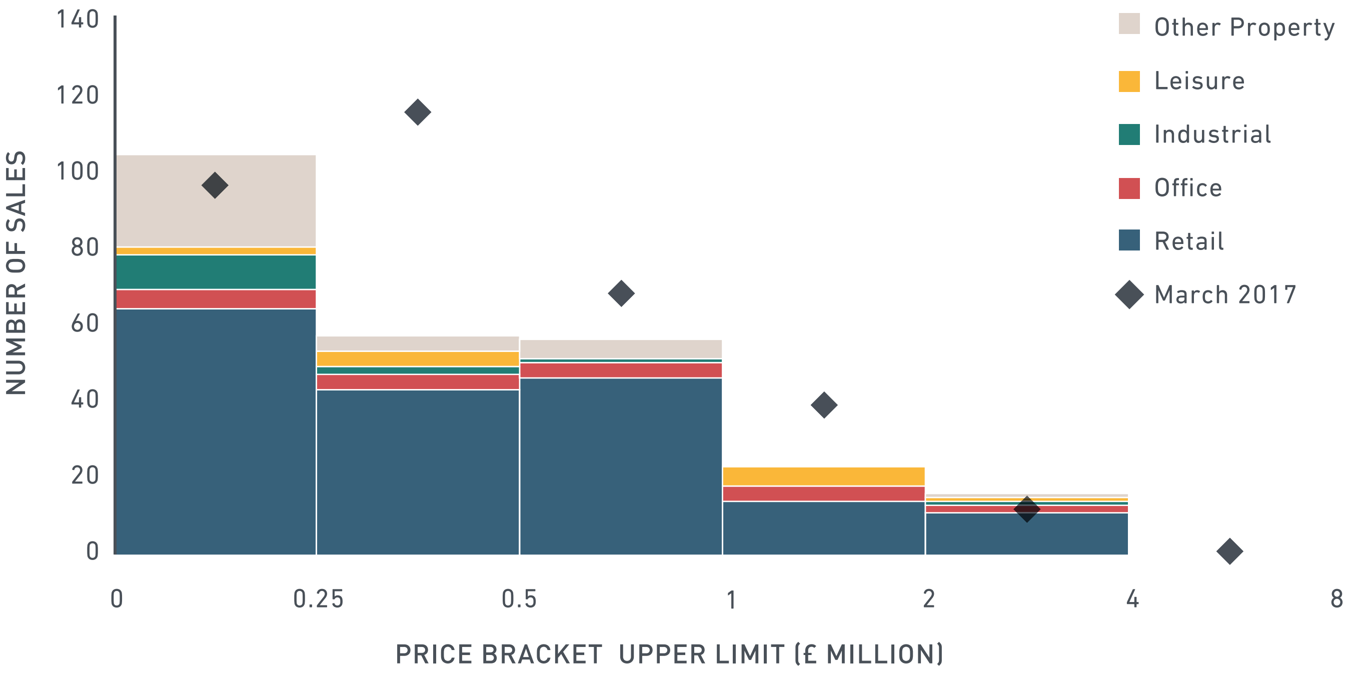
* The "In the market" section of the report has been prepared by Acuitus.

COMMERCIAL PROPERTY AUCTION SALE RATE (%)

SECTOR		MAY 2017	MAR 2017
RETAIL	▼	74%	87%
OFFICE	▼	70%	86%
INDUSTRIAL	▼	87%	94%
LEISURE	▼	67%	83%
OTHER	▲	92%	79%

REGION		MAY 2017	MAR 2017
LONDON	▼	83%	90%
REST OF UK	▼	75%	86%

COMMERCIAL PROPERTY AUCTION SALES BY PRICE BAND



Source: cPad

YIELDS STABILISING

Since the nature of the stock moving through the auction room varies between auction rounds, cPad provides a Rolling Average Yield (RAY) rather than a spot yield. This smoothes out variations caused by the sample size and the differences in the basket of properties sold between auctions. The RAY is a moving average of the current and four preceding auction rounds in a 12-month period.

The average all-property RAY saw a small rise of 3 bp, returning to the level recorded at the end of 2016. As expected office yields have started to drift upwards, rising almost 40 bp in May. In contrast, the industrial sector RAY stands at its lowest since 2011 at 8.05%, reflecting the depth of private investor demand for assets in this sector. This represents a hardening of 91 bp over the last year. However, we expect some of these gains to be lost over the coming 12 months.

The Lower Quartile RAY, which reflects the higher quality segment of the market, fell again in May to 6.33%, the lowest level since 2011. However, unlike London's super prime commercial market, the sub £5m market has not seen unsustainable levels of growth driven by a weight of global capital. There are, however, unlikely to be further yield driven gains in the coming period as investors take a more cautious approach and GDP growth falls.

An early signal of this is evident in the Upper Quartile segment of the market, which reflects more secondary property, where a further outward movement was recorded.

PRIVATE INVESTORS UNABATED BUT SELECTIVE

The May cPad Index suggests greater caution amongst investors over the coming year, which is to be expected given political and economic circumstances. However, the data does not suggest private investors are withdrawing from the market. In fact activity in advance of summer sales suggests an eagerness to place money in solid income producing assets in advance of the inevitable uncertainties ahead. The overall investor universe is also likely to grow not just because of the buy to let residential investors entering the commercial property market but also new technology aligned with improved knowledge is lowering the barriers to entry. Intense competition for such assets, particularly in the £1-£5m value range, is expected over the coming twelve months. Weaker assets without the benefit of an income story or capital uplift potential will find a thinner market. We anticipate this will be reflected in the Upper Quartile RAY.

The GAP store at 192 Western Road, Brighton sold for £2.81m at the Acuitus May auction

SPOT YIELD SUMMARY

ALL PROPERTY		MAY 2017	MAR 2017
AVERAGE INITIAL YIELD	▲	8.3%	7.8%
LOWER YIELD QUARTILE	–	5.9%	5.9%
UPPER YIELD QUARTILE	▲	9.6%	9.3%
YIELD BY UNEXPIRED LEASE TERM		**MAY 2017**	**MAR 2017**
0-5 YEARS	▼	2.1%	9.5%
6-10 YEARS	▲	7.8%	7.6%
11-15 YEARS	▲	8.2%	6.8%

YIELD BY VALUE BAND		MAY 2017	MAR 2017
£0 - £250,000	▼	8.9%	9.5%
£250,000 - £500,000	▲	8.1%	7.4%
£500,000 - £1 MILLION	▲	8.2%	7.4%
£1 MILLION+	▲	7.7%	7.0%

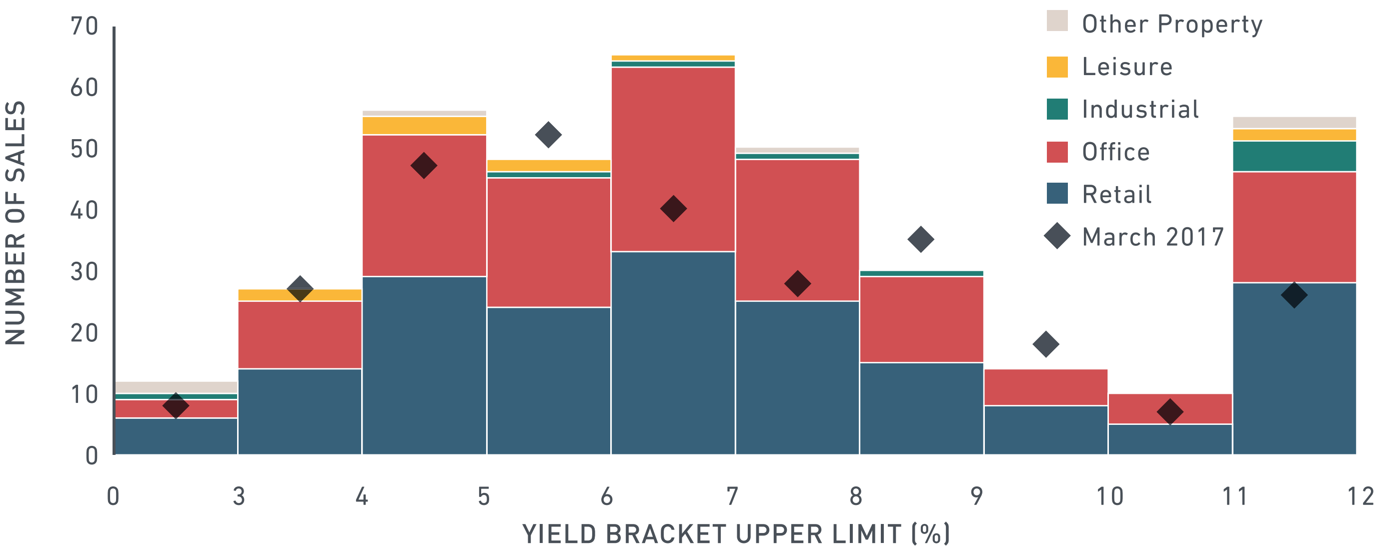
SPOT YIELD SUMMARY BY SECTOR

SECTOR		MAY 2017	MAR 2017
RETAIL	▲	8.1%	7.8%
OFFICE	▲	11.1%	8.6%
INDUSTRIAL	▲	8.2%	6.4%
LEISURE	▼	7.7%	8.6%
OTHER	▲	8.7%	6.6%

SPOT YIELD SUMMARY BY REGION

REGION		MAY 2017	MAR 2017
LONDON	▼	5.0%	5.6%
REST OF UK	▲	8.7%	8.0%

SPOT YIELD SUMMARY BY YIELD BAND



Source: cPad

UK RETAIL MARKET ANALYSIS*

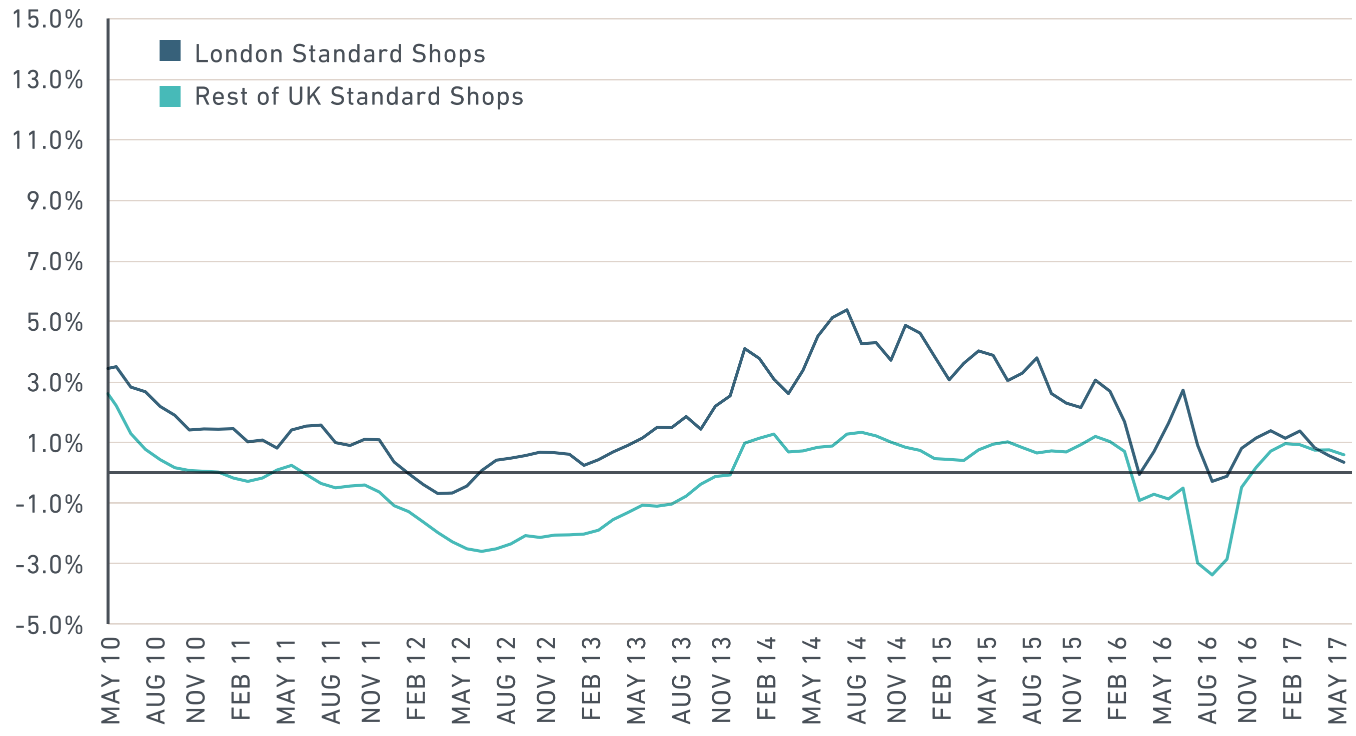
Following three consecutive years of rising capital values, the U.K. commercial property market saw values fall on average by 1.3% in the year to May 2017, according to the IPD UK Monthly Property Index. The unexpected result of the EU Referendum in June was a major cause of this decline, as values fell by 3.6% in the quarter to September 2016 – the only quarter of the year in which values fell. Returns steadied post September, with values increasing by 1.1% in the quarter to December and by 1.0% in the quarter to May 2017.

The annual income return to U.K. commercial property closed the year at 5.6%, a slight increase on 2016 (5.5%). This was the lowest income return levels recorded since 2007, maintaining the trend that started in December 2009, when income return peaked at 8.2%.

The average net initial yield across the U.K. commercial property market stood at 5.3% in May 2017, up from the 4.9% in May 2016, with the initial yield for standard shops – the focus of the CPAD report – closing at 5.2%. Yields in this market have compressed from highs of 7.1% (initial yield) and 9.0% (equivalent yield) at the bottom of the market in 2009, highlighting the recovery in values for this type of property, albeit mostly driven by strong Central London performance.

Standard shops in the Rest of the UK, excluding the South East and London, recorded a total return of 3.5% in the year to May 2017, driven by a sector-leading income return of 6.4%. Meanwhile, capital values here fell by an average of -2.8%, mainly due to deterioration in investor sentiment towards the sector, reflected in a yield impact of -1.9%. The rental market also saw a drop off, with average asset rental values falling by 0.1% over the year, continuing a trend that started in January 2015.

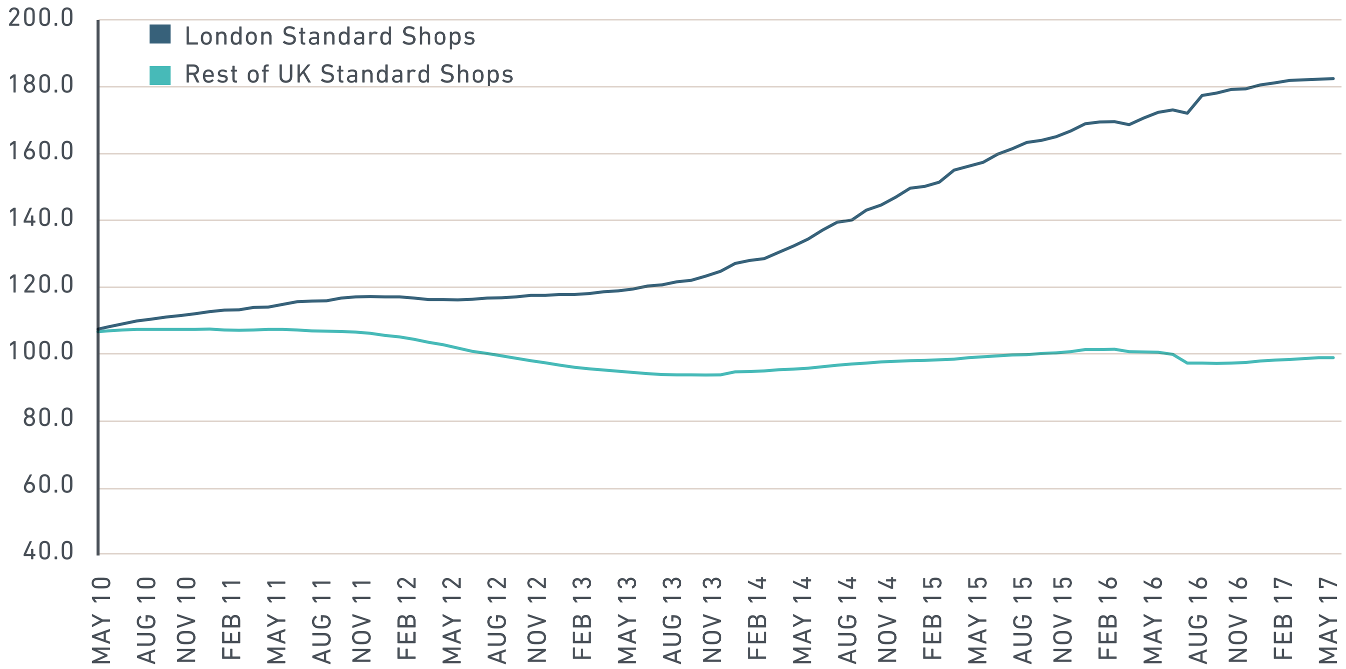
STANDARD SHOPS CAPITAL VALUE INDICES BY REGION (MONTHLY)



Source: *IPD* UK Monthly Property Index

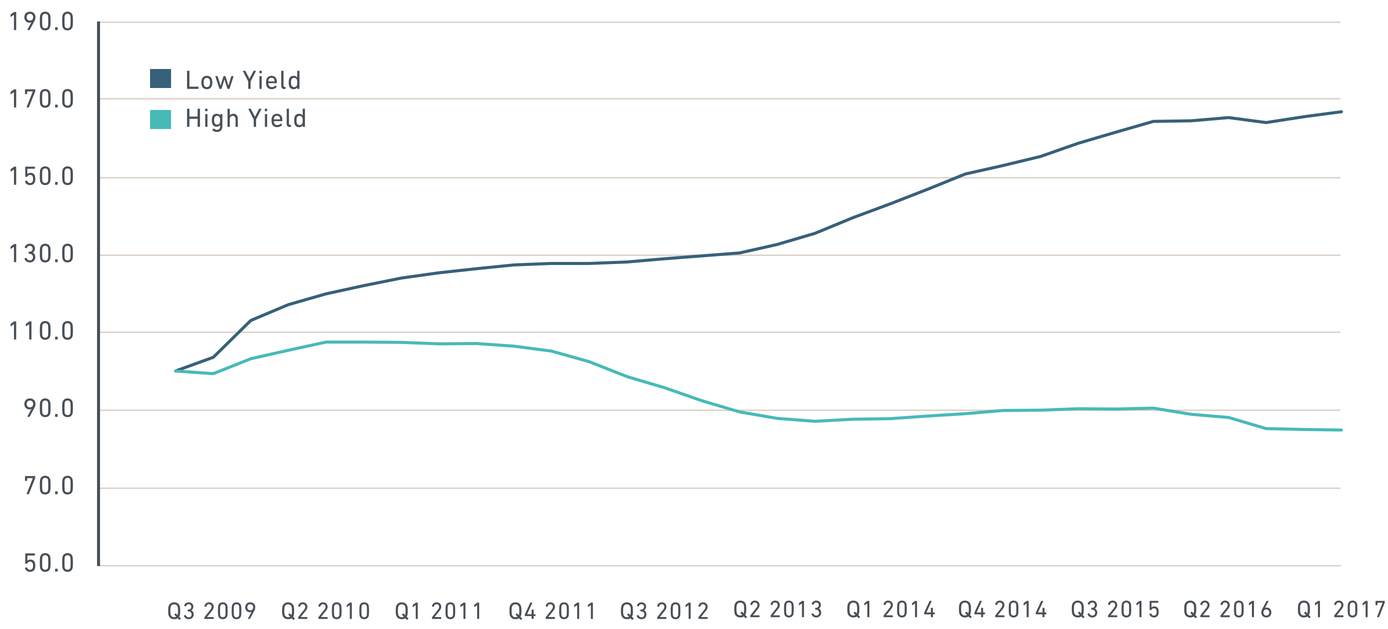
* The "UK Retail Market Analysis" section of the report has been prepared by MSCI.

STANDARD SHOPS THREE-MONTH ROLLING CAPITAL VALUE CHANGE (%)



Source: *IPD* UK Monthly Property Index

STANDARD SHOPS CAPITAL VALUE INDICES BY YIELD (QUARTERLY)



Source: *IPD* UK Quarterly Property Index

ECONOMIC SCORE CARD*

ECONOMIC SCORE CARD AVERAGE

All leading economic indicators continued to prove resilient in the second quarter of 2017, with economic growth remaining positive, although slowing, and unemployment levels continuing to fall. However, risks remain for the U.K. economy, with the reduction in the value of Pound Sterling starting to filter through to inflation, and the general election result still awaited at the time of this report.

As of May 2017, annual inflation stood at 2.7%, 40bps above the 10-year average, continuing to be ahead of the Bank of England target rate of 2.0%.

The Economic Score card dipped to 6.0 in May 2017, down from 7.0 in March 2017, still 40 basis points above the 10-year average of 5.6%. This further underlined continuing confidence in the wider U.K. economy.

ECONOMIC SCORE CARD AVERAGE	2007				2008				2009				2010				2011				2012				2013				2014				2015				2016				2017	
	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	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
	6.9	7.0	6.5	6.2	5.7	4.0	1.6	1.7	2.4	4.4	5.9	6.5	6.6	5.5	5.7	5.3	5.1	5.3	2.3	4.3	4.7	5.4	5.6	6.6	6.4	6.4	7.0	6.9	6.3	6.6	6.2	6.1	6.2	5.9	6.2	6.5	5.2	5.9	6.6	6.8	7	6
Inflation (CPI y/y)	6	7	5	6	7	4	1	6	7	5	3	7	5	6	6	4	3	3	1	3	5	7	6	7	7	7	7	6	4	5	3	1	1	1	1	3	1	1	4	5	7	7
FTSE All-Share (q/q)	7	7	5	6	2	5	1	1	2	7	7	7	7	1	7	7	6	6	1	7	7	4	7	7	7	5	7	7	5	6	5	6	7	5	7	7	1	7	7	7	7	7
Nationwide House Price Index (q/q)	7	7	7	6	3	1	1	1	3	7	7	7	7	7	4	4	7	6	5	6	5	5	6	6	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7
Consumer confidence	7	7	7	7	7	4	3	1	2	4	7	7	7	6	5	4	3	5	3	2	3	3	4	5	4	5	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7
Unemployment expectations	7	7	7	7	7	6	3	1	1	2	4	4	6	5	4	4	3	5	4	4	4	5	6	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7	7
Retail trade confidence	7	7	7	6	7	4	1	1	1	4	7	7	7	6	7	7	7	6	1	4	4	7	5	7	6	7	7	7	7	7	7	7	7	7	7	7	6	6	7	7	7	7
Expected retail trade	7	7	7	5	7	4	1	1	1	2	6	7	7	7	7	7	7	6	1	4	5	7	5	7	7	7	7	7	7	7	7	7	7	7	7	7	7	6	7	7	7	6

Source: *IPD*, ONS, EcoWin, Nationwide

SCORE CARD KEY

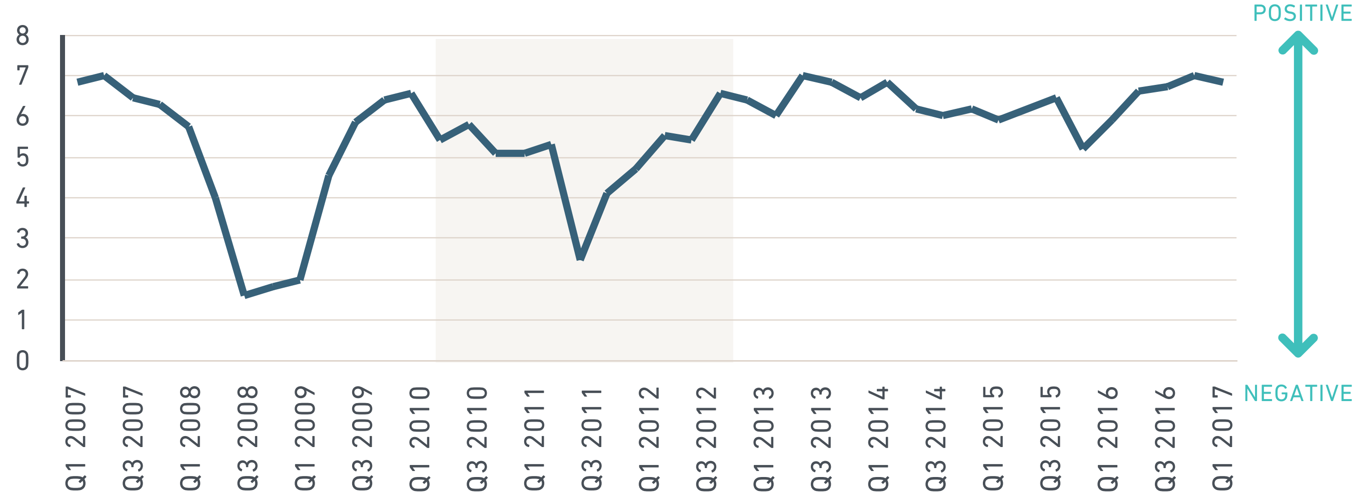
7	6	5	4	3	2	1
Fully functioning market		Partially functioning market		Impaired market function		Severely impaired function

The Economic Score Card is an economic indicator tailored to monitor the health of consumers and retailers. For each component, a score of seven is awarded if the data point is greater than its 10-year average.

For every third of a standard deviation the data point is below the average, the score is reduced by one. Each score contributes to the overall average, which is weighted using the same methodology as the European Commission's ESI methodology.

* The "Economic Score Card" section of the report has been prepared by MSCI.

ECONOMIC SCORE CARD AVERAGE



Source: *IPD*, ONS, EcoWin, Nationwide

Units 11 - 15 in the Portland Walk shopping centre in Barrow-In-Furness sold for £3m at the May Acuitus auction

ECONOMIC SCORE CARD VARIABLES	SCORE	MAY 2017	10-YR AVG.	ANALYSIS
ECONOMIC SCORE CARD AVERAGE	6.8	6.8	6.0	The Economic Score Card Average dipped slightly in the first part of Q2 2017, standing at 6.0 at the end of May. There remained lingering concerns about Britain's election in June and departure from the EU. Nevertheless, equity performance was still strong, unemployment fell and the economy continued to grow steadily, if at a slightly slower rate than previously. The Score Card currently is still above its long-term average of 5.6, suggesting that the U.K. economy remains close to full capacity.
INFLATION (CPI Y/Y)*	6	2.9%	2.30	According to the Office for National Statistics (ONS), the rate of inflation rose to 2.7% in the year to May 2017, with recreational and cultural goods and services seeing the biggest price rises. As expected, inflation has continued to increase in the wake of the EU referendum, as the fall in the value of Pound Sterling started to filter through to consumers. The annual rate of inflation remains above the Bank of England's target rate of 2.0%, and has been growing month-on-month since April 2016.
FTSE ALL SHARE (Q/Q)	7	3.2%	0.03%	U.K. and global equities continued to progress through the second quarter of 2017. U.K. equities have reached record highs – breaking the 7500 mark for the first time in May. A recovering oil price, backed by speculation of reduced supply and an increased infrastructure spending in China bolstering commodity prices. But analysts remain cautious, particularly in the context of upcoming elections in the U.K.
NATIONWIDE HOUSE PRICE INDEX (Q/Q)	7	1.1%	0.01%	U.K. house price growth slowed in May 2017, with the annual growth rate of 2.1% down on the previous 12 months, and prices on average falling by 0.2% during May. The third consecutive monthly fall in values, the first time this has happened since 2009. Rising inflation and affordability concerns in certain markets have created head winds in the market. Although the conditions for growth still persist – a shortage of supply combined with low long-term interest rates.

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

ECONOMIC SCORE CARD VARIABLES	SCORE	MAY 2017	10-YR AVG.	ANALYSIS
CONSUMER CONFIDENCE	7	-6.1	-9.80	U.K. consumer confidence grew in May 2017, though it still remained negative, with the number of pessimists outweighing the number of optimists. Many commentators expected this to fall further. However, the U.K. consumer has proved resilient- even as inflation has started to feed through to retail prices - the continuing low interest rate environment and expectations of future inflation are encouraging a tendency to "buy sooner rather than later".
UNEMPLOYMENT EXPECTATIONS**	7	17.7	29.10	U.K. employment levels have continued to improve through 2017, with the April month-end unemployment rate of 4.6% at its lowest since 1975. Although still beyond the lowest rate ever recorded of 3.4%, at the back end of 1973. According a survey by the employment group Manpower, there seems to be increasing pessimism in hiring staff in 'remain' areas of the UK with London and Scotland seeing the largest shift.
RETAIL TRADE CONFIDENCE	7	4.3	0	U.K. retail sales grew in the 3 months to May 2017, with official volumes increasing by 1.3%, a return to growth, however in month-on-month figures to May growth fell back by 1.1%. The largest increases were seen in textile clothing and footwear stores. Average retail prices rose by 3.2%, driven by the reduction in value of Pound Sterling. The increase in oil price meant that petrol stations experienced the biggest jump, with prices rising by 7.3% in the year to May 2017.
EXPECTED RETAIL TRADE	6	6.2	9.60	Many analysts forecast a reduction in the consumer confidence and retail spending, however in the quarter to May 2017 this has not been realized. While prices have continued to steadily grow and inflation sits at 2.7% beyond the Bank of England target rate of 2%. This is against a backdrop of increasing employment, and general economic growth. The challenge, it seems, for retailers is how quickly they pass on increased prices to consumers, who remain relatively buoyant even with growing headwinds.

** Scoring is inverted. (High value equals low score)

Sources: MSCI, ONS, EcoWin, Nationwide

ABOUT MSCI

For more than 40 years, MSCI´s research-based indexes and analytics have helped the world´s leading investors build and manage better portfolios. Clients rely on our offerings for deeper insights into the drivers of performance and risk in their portfolios, broad asset class coverage and innovative research.

Our line of products and services includes indexes, analytical models, data, real estate benchmarks and ESG research.

MSCI Services 97 of the top 100 largest money managers, according to the most recent P&I ranking.

For more information, visit us at **www.msci.com**.

ABOUT ACUITUS

Since it was founded in 2010, Acuitus has sold more than £1bn of commercial property assets at auction and delivered a new, innovative and hugely successful approach to the auction process.

The firm has transformed auctioneering from a simple means of buying and selling property into a sophisticated platform for enabling investment strategies.

It collaborates with MSCI to produce the commercial property auction sector's leading research studies.

www.acuitus.co.uk

ABOUT EIG

EIG is recognised as the Industry Standard for auction information and currently includes details on over 800,000 lots. With 35,000 lots coming to auction each year, it is used by investors and developers to identify buying opportunities

In addition the fully searchable historic database spanning 26 years is a valuable resource for valuation comparables.

www.eigpropertyauctions.co.uk

MSCI

T: +44 20 7336 4783

E: realestate@msci.com

MSCI
Ninth Floor, Ten Bishops Square
Spitalfields, London E1 6EG

ACUITUS

Richard Auterac
Chairman and Auctioneer
T: +44 20 7034 4851
E: richard.auterac@acuitus.co.uk

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

EIG

David Sandeman
Managing Director
T: +44 1737 232 289
E: davids@eigroup.com

Essential Information Group -
The Property Auction
Information Specialists
9 Castlefield Road, Reigate
Surrey RH2 0SA

msci.com

acuitus.co.uk

www.eigpropertyauctions.co.uk