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IPD/Acuitus Commercial Property Auction Data (cPad) Auctions report for May 2014

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Increasing competition in the auction room

Welcome to the latest Commercial Property Auction Data (cPad) Market Flash which analyses the £99.78m of commercial property assets that sold at the May 2014 sales.

The increasing volume of properties selling at auction follows the trend established in the previous two rounds of sales. This further underlines both investor demand and the willingness of sellers to bring their property to market.

Sharpening yields across all property types illustrates the increased competition in the auction room but the lower percentage of properties that have sold suggests that some sellers may have been overoptimistic in their expectations and the reserves they have stipulated.

Retail property continues to be the engine of the auction room. The improving economic situation and consumer confidence is being demonstrated in the sale room. Not surprisingly, the average retail yield has sharpened to its lowest level since October 2011.

Leisure property is proving to be an asset class of growing interest to investors. The latest round of auctions showed a 161% year-on-year increase in the volume of leisure properties selling at auction, with investors drawn to the longer leases that are the norm in the sector.

Once again, cPad paints a progressive picture. It is clear that investors remain extremely discerning and will be highly precise in their stock selection and pricing.

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

Key Stats

▲ **25%**
increase in sales volume
year-on-year

▼ **£600,000**
Average lot price down

▲ **161%**
increase in leisure asset
sales

▼ **8.3%**
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

Investors: hungry but discerning

May's commercial property auctions saw the volume of sales increase by 25% year-on-year (y/y) as £99.78m of assets found buyers.

This increase follows jumps in year-on-year volumes at the December 2013 (+62% y/y) and February/ March (+79% y/y) auctions, and reflects the continuing recovery of the market since July 2011

In contrast, the average sales rate at the May sales was somewhat disappointing at 70.3%. This was 5.7% below the corresponding rate in May 2013, and halted the trend of very high success rates experienced since October of last year.

This is perhaps a reflection of some over-optimistic pricing expectations from sellers. The recovery in retail sales is building from a low base and is distributed unevenly both regionally and across the retail hierarchy. Investor demand is similarly focused on the strongest retail locations so it is a mistake to think that because there is improved confidence and performance in some areas then this can be extrapolated to higher prices across the board.

The leisure sector continued to strengthen in the latest round of auctions with its share of sales increasing from 11% in February/March to 13% in May with year-on- year growth of 161% .

Leisure assets achieved a high sales rate of 80% overall while the mean average lot size was up from £504,000 in February/March to £811,000 in May. This was strongly influenced by the sale of one large lot: a long-leased public house and residential redevelopment opportunity in Birmingham. The mid-point of the range of sales achieved (the median price) declined from £900,000 to £730,000.

However, investors continue to be attracted to the long leases and buoyant businesses that the leisure sector features and it looks to be an asset class which will stay in favour for the foreseeable future.

Sales volumes in the office sector shrank from £50m in February/March to a little over £8m in May, representing 8% of total sales volume against 23% in the preceding round of auctions.

This is reflected in a corresponding reduction in the average lot size to £601,000 from £700,000 in the preceding auction period, but represents growth of 11% year-on-year.

Demand for more secondary office assets remains robust as investors continue to move up the risk curve in search of properties offering value-add opportunities. The sales rate for the office sector remained high at 81%.

Investor demand continues to favour London over the regions and is manifest in the continued high sales rate of 80% for London properties some 10.5% higher than for the rest of the UK.

The capital's strength is also reflected in pricing with London assets representing 21% of all sales by value but only 10.6% of sales by number. There is considerable variance in demand and pricing within London as evidenced by the large difference between the mean average and mid-point (median average) of the range in sales prices achieved (£1.3m and £0.5m, respectively). This value polarisation is less marked in the rest of the UK, which has a mean value of £0.52m and a median value of £0.34m.

Commercial property auction sales summary

Sector		May '14	Feb/Mar '14
Volume (£ million)	▼	99.8	187.2
Properties sold	▼	166	268
Average lot size (£)	▼	601,140	698,418
Sales rate	▼	70.3%	84.0%



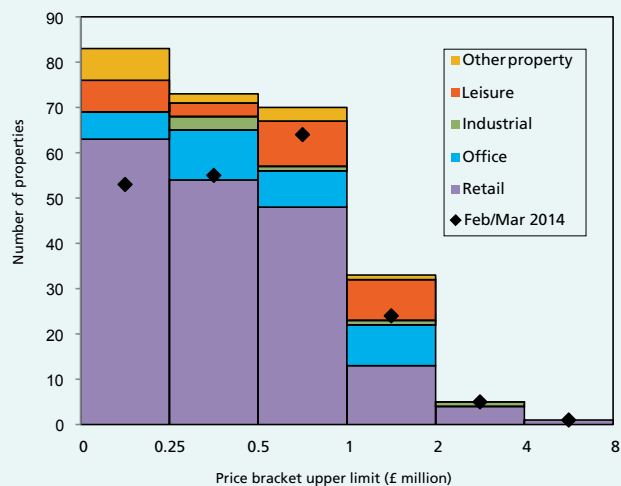
Commercial property auction sales, £million

Sector		May '14	Feb/Mar '14
Retail	▼	72.1	104.3
Office	▼	8.2	50.0
Industrial	▼	0.4	6.8
Leisure	▼	13.0	21.2
Other	▲	6.1	4.9
Region		May '14	Feb/Mar '14
London	▼	21.1	51.5
Rest of UK	▼	78.7	135.7

Commercial property auction sales rate, %

Sector		May '14	Feb/Mar '14
Retail	▼	68%	82%
Office	▼	81%	90%
Industrial	▼	50%	75%
Leisure	▼	80%	91%
Other	▲	88%	87%
Region		May '14	Feb/Mar '14
London	▼	80%	97%
Rest of UK	▼	69%	82%

Commercial property auction sales by price band





In the market

Yield compression across the board, but quality counts

While the lower sales rate suggests investors are discerning, the persistence of strong demand for attractively priced, good quality assets resulted in the cPad All-Property yield compressing by 90 basis points (bp) to 8.3% - and by 170bp when weighted by value. This is the lowest level for the All Property Yield since May 2012.

This sharpening was partly driven by the large proportion of retail assets in the May auction compared to the February/March sales. Retail assets tend to be lower yielding than the office and industrial sector.

The cPad Average Retail yield experienced strong downward pressure and moved downwards by 70bp to 8.2%. When weighted for value, the downward yield shift was 140 bp.

This was surpassed only by the leisure sector, which experienced an inward movement of 210bp in its weighted average yield. However, this was strongly influenced by the aforementioned sale of one high quality asset that commanded a yield of 5.5%. The non-weighted average yield compressed by 70bp.

This polarisation of investor demand by asset quality explains the seeming contradiction of a sharp fall in the sales rate between the February/March and the most recent auction in May, and the occurrence of strong yield compression resulting from strong pricing of the 70% of better quality assets that sold.

This is also reflected in the polarisation of demand by lot size. In May, larger lot sizes experienced very strong yield compression of 290bp in comparison to the February/March sales, and they commanded significantly lower yields than smaller lot sizes.

Lot sizes in excess of £1m sold at an average yield of 6.2% in comparison to 9.8% for lots of less than £250,000. While this yield movement undoubtedly reflects differences in the type and quality of the basket of assets comprising the larger lot size in each auction, it also represents the increased activity of institutional investors beyond the prime London market.

Lower quality secondary assets continue to experience weak demand from investors and occupiers alike. Indeed, the absence of a recovery in income expectations for such assets in the near term will impede a recovery in pricing; sellers should not expect weak assets to move in tandem with the wider market.

The yield spread between London and the Rest of the UK has narrowed by 110bp to 200bp, driven by yields falling to 8.5% in the regions, while London yields remained stable at 6.5%. While investors searching for value have increased their appetite for assets outside London, they remain focused on quality and it is noteworthy that better located assets enjoyed a much higher sales rate at auction in May.

Income profile is a critical component of risk and perceived asset quality and includes rental level, covenant strength in addition to lease length and vacancy risk.

The spread between assets with a short income profile (less than 5 years) and those with a strong income profile (greater than 11 years) remains wide at 430bp. While yields for assets with low security of income remained broadly stable, the pricing of longer income streams in excess of 10 years hardened by 50bp. Interestingly, assets with a medium income risk profile (lease length between five and 10 years) experienced strong re-pricing with yields moving in by 80bp. This may reflect growing investor confidence in the economic recovery, with investors increasing their appetite for properties that offer asset-repositioning opportunities in timing with the shift from recovery to growth in the next economic cycle.

Similarly, the gap between prime and secondary yields continued to narrow by 30bp to 360bp from March to May with prime yields falling by 50bp to 6.2%. Secondary yields compressed by 80bp to 9.8%. The movements in prime and secondary yields are equal in terms of their impact on capital growth. It is worth noting that the secondary data does not include those assets that failed to sell and thus is likely to understate the polarisation in investor demand.

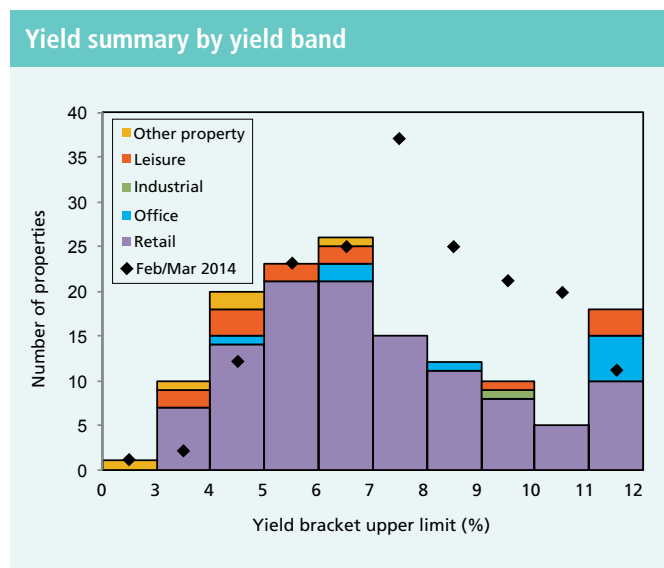


Yield summary			
All commercial property totals			
		May '14	Feb/Mar '14
Average initial yield	▼	8.3%	9.2%
Lower yield quartile	▼	6.2%	6.7%
Upper yield quartile	▼	9.8%	10.6%
Yield by unexpired lease term			
0-5 years	▲	11.0%	10.9%
6-10 years	▼	8.6%	9.4%
11-15 years	▼	6.7%	7.2%

Yield summary			
Yield by value band			
		May '14	Feb/Mar '14
£0 - £250,000	▼	9.8%	10.3%
£250,000 - £500,000	▼	8.6%	8.8%
£500,000 - £1 million	▼	7.9%	9.0%
£1 million +	▼	6.2%	9.1%

Yield summary by sector			
Sector			
		May '14	Feb/Mar '14
Retail	▼	8.2%	8.9%
Office	▼	10.7%	10.9%
Industrial	▼	10.1%	11.5%
Leisure	▼	8.3%	9.0%
Other	▼	5.4%	7.2%

Yield summary by region			
Sector			
		May '14	Feb/Mar '14
London	▶	6.5%	6.5%
Rest of UK	▼	8.5%	9.6%





UK retail market analysis

High street recovery?

Although there are still challenges ahead for the consumer economy, a real recovery has now begun. Consumer confidence has steadily improved over the last 6 months, with levels now close to those recorded prior to the global financial crisis. Polarisation within the sector, still remains significant, with demand in certain regional locations remaining patchy. So far in 2014, national values in this sector have gained 1.1% while London standard retail units have gained 5.6%. The two-speed market remains very much in force across the British retail sector.

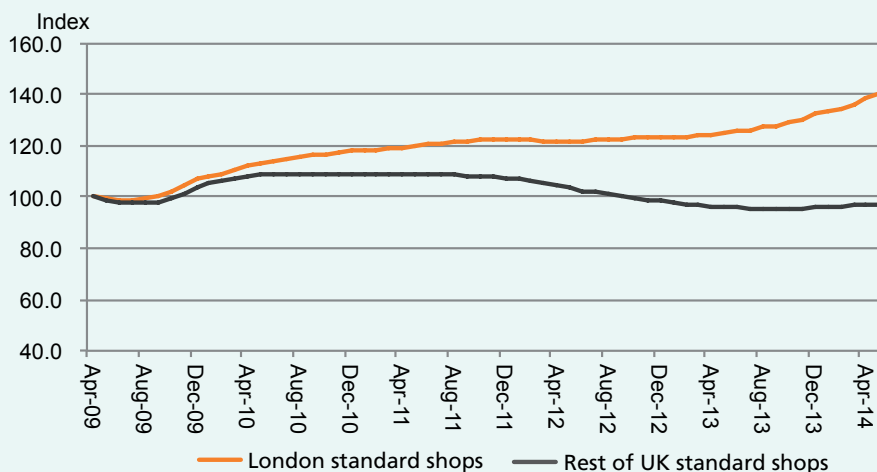
During the month to the end of May 2014, national retail values increased by a further 1.1% m/m according to the latest figures from the IPD UK Monthly Index. This growth was not evenly spread by geography or type. London continued to outperform strongly across all retail segments while shopping centres continued to record value growth.

There is little doubt that the retail sector's recovery is gathering pace and with the consumer economy now beginning to show signs of real life, the latter half of 2014 should see some promising growth within the previously strained retail market.

Over the last three months, standard retail values in London continued to gather momentum and outperform their regional counter-parts. Values in London increased by 4.5% q/q with regional values increasing by 1.0% q/q; a vast improvement on last years figures where the value of standard retail assets outside London fell by 1.0% q/q.

Over the course of the last 12 months, regional differences remain intact. Capital values grew by 12.5% y/y in London and standard retail values for the rest of the UK grew by only 1.3% y/y.

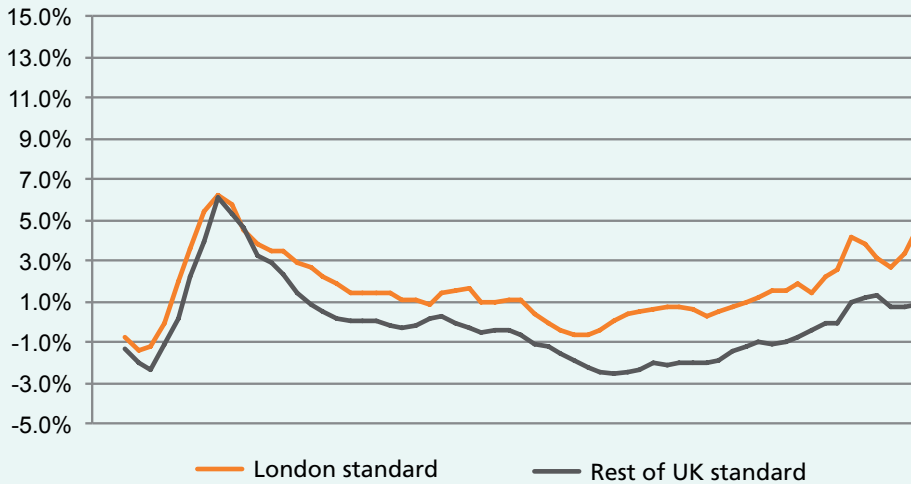
Standard shops capital value indices by region, monthly



Source: IPD UK Monthly Property Index

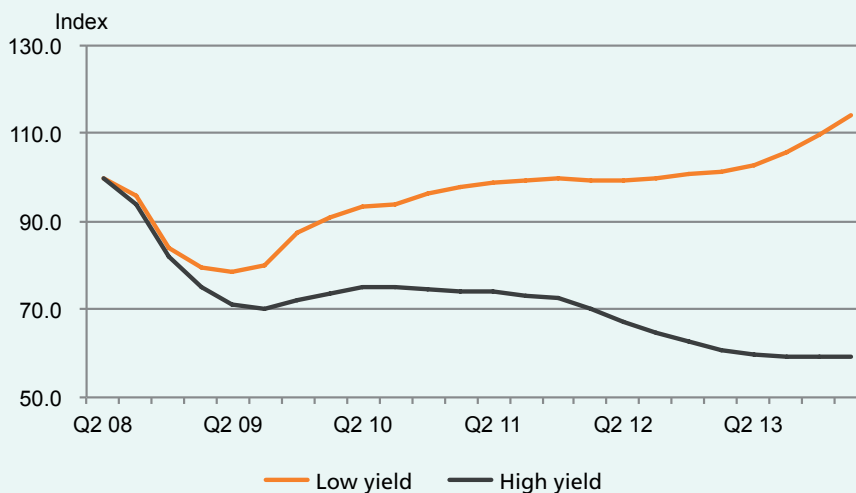


Standard shops three-month rolling capital value change, %



Source: IPD UK Monthly Property Index

Standard shops capital value indices by yield, quarterly



Source: IPD UK Quarterly Property Index

While location plays a significant role in determining performance, the spread between prime and secondary assets nationwide, paints a similar picture. For this analysis, the standard retail unit sample is split into high and low yielding assets to compare performance. The first quarter of the year saw prime retail unit's capital values rise by 3.8%, while secondary asset's growth remained flat. Heightened demand for prime assets with unexpired leases in excess of 10 years continues to tighten the market. Although we have seen a continued reduction in the yield gap between prime and secondary assets, larger enthusiasm for risk is yet to be realised.

Overall the improvement in market sentiment in the retail sector is supported by increased confidence in retailer outlook. The trading environment for UK retailers will continue to improve over the remainder of the year and recovery across the retail sector will begin to ripple out to the regions.

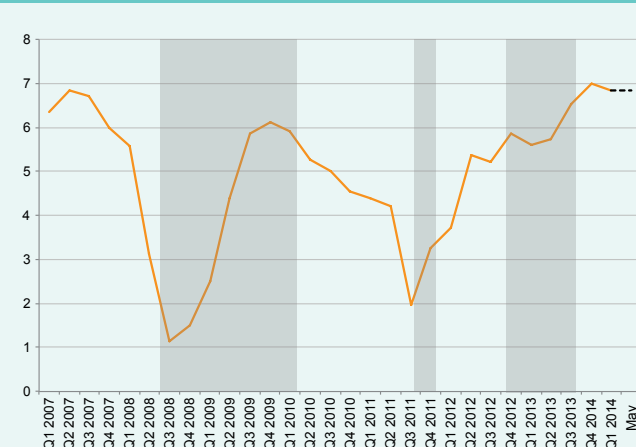


Economic Score Card

Economic Score Card Average

2014 will be a year of improving optimism with the economic recovery showing no signs of slowing down. The economic scorecard average fell 20 basis points to 6.8 in May 2014 – solely due to inflation falling 50 basis points below the Bank of England's target rate of 2%. Inflation however still remains higher than wage rate growth and over the next year will weight heavily on policymakers. Retail trade and retail confidence have begun to pick up with notable declines in savings ratios.

Economic Score Card average



Source: IPD, ONS, EcoWin, Nationwide

	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	May
Economic Score Card Average	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
Inflation (CPI y/y)	5	7	5	5	3	4	4	2	1	1	1	1	3	6	7	5	5	5	5	7	6	6
FTSE All-Share (q/q)	5	7	7	7	7	5	7	7	7	7	2	7	7	7	7	7	7	7	6	7	7	7
Nationwide House Price Index (q/q)	3	7	7	7	6	6	4	4	6	5	4	5	4	4	5	5	5	5	7	7	7	7
Consumer confidence	1	2	6	6	7	5	3	2	1	3	1	1	1	1	2	3	2	3	7	7	7	7
Unemployment expectations	1	1	3	4	5	4	3	3	2	4	4	2	4	5	6	7	7	7	7	7	7	7
Retail trade confidence	1	4	7	7	7	6	7	7	7	5	1	4	3	7	4	7	6	6	7	7	7	7
Expected retail trade	1	2	6	7	7	7	7	7	7	5	1	3	4	7	5	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	May 2014	10-yr average	Analysis
Economic Score Card Average	6.8	6.8	5.3	The Economic Score Card Average remained strong to the end of May 2014 as the broader UK economy continued the trend of modest, but consistent, growth. The score of 6.8 at the end of May, up marginally from 6.7 in February highlights the growing stability in the UK economy and was well above the 10-year average of 5.3. Further sustained growth in the UK economy along with a pick-up in performance in the broader European Union has strengthened UK trade while job growth continues at pace as the private sectors expands.
Inflation (CPI y/y)*	6	1.5%	2.7	Recorded inflation remained well below the Bank of England's 2.0% target rate in May 2014 recording the lowest level of price growth in almost five years. The Consumer Price Index came in at 1.5% to the end of May compared to 1.8% in April meaning that it was the sixth consecutive month in which inflation has been below the MPC's target rate.
FTSE All Share (q/q)	7	1.1%	0.0%	The UK Equities market has continued to record growth, albeit modest compared to the same period in 2013, with investors expecting an improved return as businesses and trade pickup. International fears continue to weigh on certain sectors although the instability in Ukraine has had less of an effect than previously expected but now growing concerns in Iraq may impact performance.
Nationwide House Price Index (q/q)	7	2.4%	0.0%	National house prices have been resurgent in recent months, with May alone recording value growth of 2.4%. In particular, the momentum has been with regional locations, especially outside London and the South East, as these markets return to value growth after a sustained period of decline.
Consumer confidence	7	8	-11	Consumer confidence in the UK was at a record high by the end of May 2014 and rose most sharply amongst young people and those in full-time employment. Confidence was boosted by an improved sense of job security given the more upbeat view of the domestic economy.
Unemployment expectations**	7	-1	34	The UK employment market has continued to improve through the first months of 2014, with the unemployment rate falling to 6.6% by the end of April. However, wage increases also slowed sharply during the same period, falling back below inflation. The total number of unemployed is now at its lowest level in over five years as the continued improvement in the economy meant continued strong jobs growth in the private sector.
Retail trade confidence	7	26	-1	Retail sales continued to improve in May, for the sixth consecutive month, in tandem with consumer confidence hitting record highs. Retailers, particularly in regional locations which have struggled with higher than average levels of unemployment have also grown in confidence as private sector employment picks up in these locations and as job security improves.
Expected retail trade	7	40	8	Expected Retail Trade strengthened on the back of the improving economic, employment and consumer figures, with a score of 40 up marginally from the 39 recorded in February, and 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

Economic Score Card Variables

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 Economic Sentiment Indicator (ESI) methodology. For further details, email IPD using the contact details on the back page.



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