

cPad

MARKET FLASH

Commercial Property Auction Data

NOV
2011

AUTUMN AUCTION SEASON BRINGS MORE VOLUME

The latest cPad Market Flash looks at the major autumn commercial property auctions which have now concluded. Investors and sellers had a long summer break to consider their strategy and there have been clear adjustments in market pricing in a downwards direction for all non-institutional assets.

Overall, the most positive news for investors was the large catalogues which provided a greater range of choice. However, buyers remain extremely selective and there is still a range of opinions as to where value lies.

We expect the current lower pricing, which in many cases already reflects the parlous state of the economy, to remain for the foreseeable future.

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

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.

KEY STATS

▲ **15%**
Sales Volume

▲ **8.4%**
average
initial yield

▼ **66%**
Sales Rate

▲ **77%**
of sales were
retail properties

AUCTION COMMENTARY

In the room: more choice as volumes rise

As predicted, the supply of properties coming into the auction room increased during the autumn sales. The total volume of properties that sold increased by 15% with retail – the dominant auction asset type - accounting for 77% of all sales.

Accurately predicting the prices of assets is proving more problematic post-summer as a result of the extreme difficulties in the financial markets and the volatility in equity prices. Overall, sale rates have slipped from 73% to 66% as investor demand has been more difficult to forecast especially for the riskier secondary assets that are let on short leases, have voids or are located outside London.

Both the number of properties offered outside London and those let on short leases increased as vendors increased supply in order to tap into the pool of private equity. However, correctly pricing this type of asset is critical - and also is sensitive to short-term changes in investor appetite. It is anticipated that post-auction sales will push the proportion selling to 75%-80% as a small adjustment in offer price is all that is needed in many cases to strike a deal.

Whilst there is an ongoing adjustment in the market and it is subject to external macro issues, it is still clear there are opportunities for investors with the requisite asset management skills and capital to lock into opportunities which will produce excellent medium- to long-term returns.

COMMERCIAL AUCTION SALES SUMMARY

		Oct 2011	July 2011
Volume (£ million)	▲	71.7	62.3
Properties Sold	▲	135	122
Average Lot Size (£)	▲	531,030	510,605
Sales Rate	▼	66.1%	72.7%

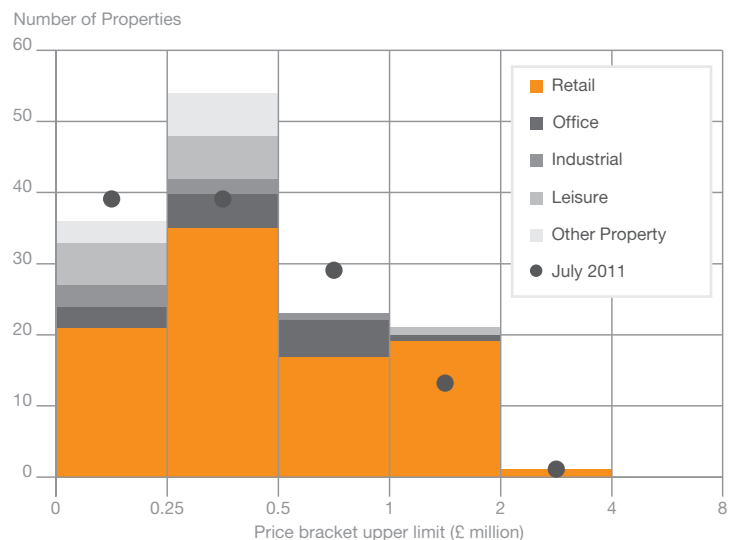
COMMERCIAL AUCTION SALES, £ MILLION

Sector		Oct 2011	July 2011
Retail	▲	55.5	45.9
Office	▼	7.5	8.1
Industrial	▼	1.6	2.6
Leisure and Other	▲	7.0	5.2
Region		Oct 2011	July 2011
London	▲	17.9	17.7
Rest of UK	▲	53.8	44.6

COMMERCIAL AUCTION SALES RATE, %

Sector		Oct 2011	July 2011
Retail	▼	66%	69%
Office	▼	57%	89%
Industrial	▼	86%	100%
Leisure and Other	▲	75%	69%
Region		Oct 2011	July 2011
London	▼	59%	91%
Rest of UK	▲	68%	68%

COMMERCIAL AUCTION SALES BY PRICE BAND



In the market: yield drift continues

Yields continued to weaken in the autumn with the cPad average all-property yield rising 40 basis points to 8.4% since the summer round of auctions. The retail yield rose 30bp to 8.2%, the office yield rose 90bp to 10.6% while the industrial yield showed the greatest increase as it rose by 260bp to 10.6%.

The prime (lower quartile) and secondary (upper quartile) yields are at 6.7% and 9.6% respectively.

The demand for London investments has produced a two-tier market between the capital and the rest of the UK with a 180-point yield gap.

We expect average yields to weaken further as more secondary assets come to market and investors progress up the risk curve to obtain high initial returns to compensate for uncertain medium-term capital growth.

With increasing evidence of over-rentedness and a rising probability of tenants not renewing leases, investors are taking a very cautious approach to pricing and are seeking to factor in all possible negatives. Short leases, falling rents and occupier financial weakness naturally weigh heavily on the minds of those who invest their own cash but this current "Doomsday" approach may mean that an over-correction in pricing may become apparent when the debt market normalises.

Commentary: Acuitus

YIELD SUMMARY

All Commercial Property Totals		Oct 2011	May 2011
Average Initial Yield	▲	8.4%	8.0%
Lower Yield Quartile	▲	6.7%	6.3%
Upper Yield Quartile	▲	9.6%	8.8%
Yield by Unexpired Lease Term			
0-5 years	▲	8.7%	8.5%
6-15 years	▲	8.3%	8.0%
16 years +	▲	8.6%	7.8%
Yield by Value Band			
£0 - £250,000	▲	9.5%	8.8%
£250,000 - £500,000	▲	8.5%	8.1%
£500,000 - £1 million	▲	8.0%	7.5%
£1 million +	▼	7.1%	7.4%

YIELD SUMMARY BY SECTOR

All Commercial Property Totals		Oct 2011	July 2011
Retail	▲	8.2%	7.9%
Office	▲	10.6%	9.7%
Industrial	▲	10.6%	8.0%

YIELD SUMMARY BY REGION

All Commercial Property Totals		Oct 2011	July 2011
London	▲	6.9%	6.6%
Rest of UK	▲	8.7%	8.5%

SUMMARY BY YIELD BAND

Number of Properties



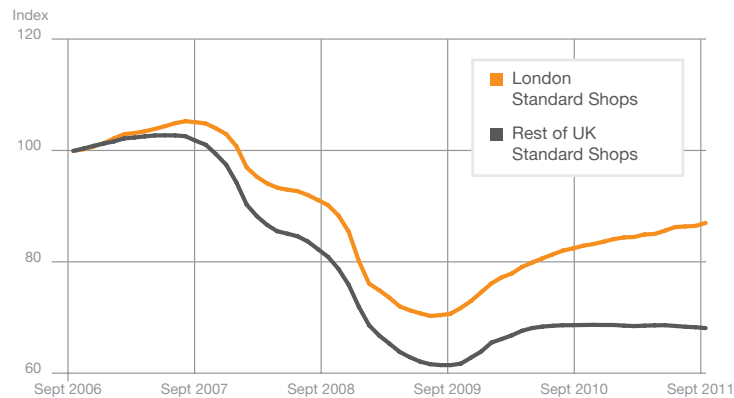
STANDARD SHOPS THREE-MONTH ROLLING CAPITAL VALUE CHANGE, %

Source: IPD UK Monthly



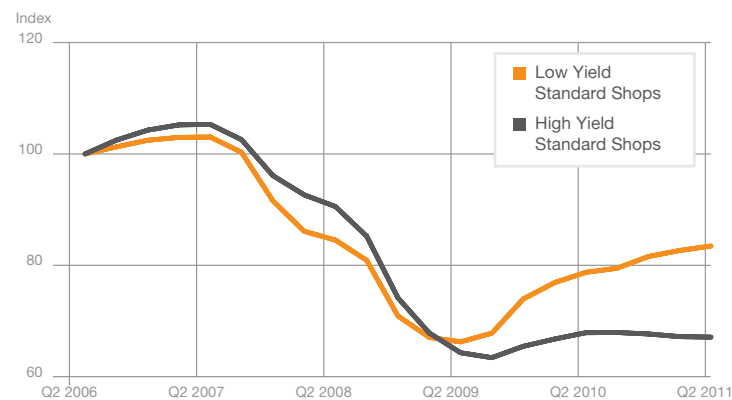
STANDARD SHOPS CAPITAL VALUE INDICES BY REGION, MONTHLY

Source: IPD UK Monthly



STANDARD SHOPS CAPITAL VALUE INDICES BY YIELD, QUARTERLY

Source: IPD UK Quarterly



IPD PROPERTY MARKET COMMENTARY

Prime properties remain resilient

Capital values for standard shops in London ended the third quarter 0.9% up on Q2 2011, according to the IPD Monthly Universe. However, the majority of that rise occurred in September following minimal changes in July and August. Outside London, shop values fell by 0.6% q/q. The decline in values has gained momentum since the relapse began in June 2011 and has partially eroded prior gains, leaving values back where they were in April 2010.

In Q3 2011, the UK economy grew by 0.5% q/q according to the preliminary estimate, up from 0.1% q/q in Q2 2011. The boost is viewed as partly anomalous, due to distortions caused by the royal wedding in the second quarter, which depressed output. However, the strong performance of the service sector was the main driver of growth, allowing the UK to maintain economic expansion.

Political posturing has exacerbated investors' doubts over a timely and adequate resolution to the current European debt crisis. Uncertainty surrounding the political phase of the crisis has manifested itself as declining economic indicators; whether this will translate into a future decline in output has yet to be seen.

At the present point in this property cycle prime properties and properties in prime locations have remained resilient to wider economic problems, whereas secondary properties have suffered. However, the EIG auction data shows yields for properties in London were 30bp higher in October than observed in July. The lower quartile yield, our proxy for a typical prime property yield, rose by 40bp.

Looking over the last five years, low-yielding assets (the bottom quartile of the sample by equivalent yield and a proxy for prime) saw values fall by 35% in the crash and have recovered 25% to date, according to the IPD Quarterly Universe as at Q2 2011. High-yielding assets (the top quartile) fell by 40% and only recovered 6% by Q2 2010, which is back down to 4% in Q2 2011, following the return of value losses.

Pressure will be on investors to assess if the defensive characteristics of prime property and property in London are enough to justify further price increases. The EIG auction data already shows that both buyers and sellers in this forum have been prompt at re-pricing additional risk and weaker growth prospects, even for prime property.

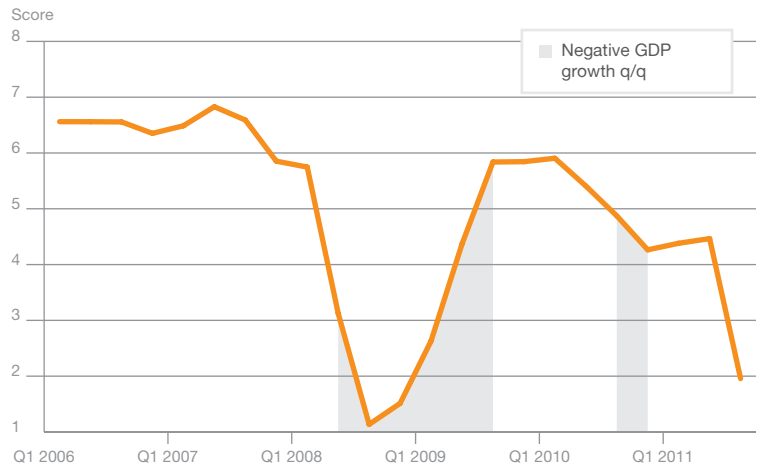
Conversely, the wider institutional investment market, as tracked by IPD, is by nature, slower to adjust to economic changes and doubts are emerging over whether the mild yield movements observed in the open market over 2011 reflect the true strength of the assets or such movements have yet to incorporate the decline in economic sentiment.

KEY MARKET DATA

Economic Score Card Average

The economic score card average fell to 2.0 in Q3 2011, representing a fall of 2.5 on Q2 2011. This is similar to the fall observed in Q2 2008; the onset of the recession. Turmoil in Europe caused a rapid sell-off in UK equity markets, depressing business confidence. However, much of the damage done to consumers and retailers was due to CPI inflation increasing to 5.2%, and further eroding consumers' disposable income. Consumers are acting accordingly by reducing their borrowing and spending. Retailers have felt the change with immediate effect. The economic score card demonstrates how the current economic environment has a number of similarities with that of the onset of the recession and given the gravitas of the problems discussed, the outlook for next quarter is for conditions to remain as they are at present.

ECONOMIC SCORE CARD AVERAGE



	2006				2007				2008				2009				2010				2011		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Economic Score Card Average	6.6	6.6	6.6	6.4	6.5	6.8	6.6	5.9	5.7	3.1	1.1	1.5	2.6	4.4	5.8	5.8	5.9	5.4	4.9	4.3	4.4	4.5	2.0
Inflation (CPI y/y)	7	6	6	4	4	6	7	7	6	2	1	4	5	7	5	5	3	4	4	2	1	1	1
FTSE All Share (q/q)	7	6	7	7	7	7	6	7	4	5	1	1	5	7	7	7	7	5	7	7	7	7	2
Nationwide House Price Index (q/q)	7	7	7	7	7	7	5	4	3	1	1	1	4	7	7	5	6	7	3	2	6	7	4
Consumer Confidence	7	7	7	7	7	7	7	7	6	1	1	1	1	2	6	6	7	5	3	2	1	3	1
Unemployment Expectations	7	6	5	6	7	7	7	7	7	5	2	1	1	1	3	4	5	4	3	3	2	4	4
Retail Trade Confidence	5	7	7	7	7	7	7	5	7	4	1	1	1	4	7	7	7	6	7	7	7	5	1
Expected Retail Trade	6	7	7	7	7	7	7	4	7	4	1	1	1	2	6	7	7	7	7	7	7	5	1

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

On the pulse of the property world

ECONOMIC SCORE CARD VARIABLES

Economic Score Card Variables	Score	Sept 2011	10-yr avg.	Analysis
Economic Score Card Average	2.0	2.0	5.7	The ESC average fell to 2.0 in September, following declines in July and August. At 2.0 the ESC average is now below levels seen in Q2 2008 and Q1 2009, two quarters that saw GDP contract quarter-on-quarter.
Inflation (CPI y/y)*	1	5.2%	2.2%	CPI annual inflation stands at 5.2%, up from 4.5% in August. Transportation and gas and electricity charges were the main protagonists, outweighing declines in clothing.
FTSE All Share (q/q)	2	-14.2%	0.0%	September saw little improvement on the collapse equities witnessed in August. Uncertainty over Europe's economic and political prospects heightened in advance of October's EU summit to address such issues.
Nationwide House Price Index (q/q)	4	-1.2%	1.8%	House prices slipped over the last quarter and sit -0.3% down on the previous year, cancelling out prior gains. Buyer confidence was dented by a weak labour market and economic concerns.
Consumer Confidence	1	-22	-8	Consumer confidence fell to -22 in September, down from -20 in August. Confidence has now fallen for four consecutive months and remains adrift from the 10-year average of -8. High energy bills and transport costs were particular culprits for eroding disposable income.
Unemployment Expectations**	4	44	30	Job security continued to deteriorate in September, as private sector job creation failed to compensate for public sector losses. Youth unemployment (under-25s) continued its march towards one million people.
Retail Trade Confidence	1	-29	1	Retail trade confidence continued its dramatic collapse from -4 in May 2011 to -29 in September. Reports of Tesco's first six-monthly decline in UK sales for 20 years underlined the harshness of the current retail environment.
Expected Retail Trade	1	-31	11	Retailers' outlook has deteriorated at a similar rate to that seen just before the onset of the recession. A series of profit warnings by high-profile retailers exacerbated the bleak outlook.

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

Source: IPD, ONS, EcoWin, Nationwide

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

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. For further details, email IPD using the contact details found below.

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