cPad

MARKET FLASH

Commercial Property Auction Data

APR 2012

The first round of commercial property auctions since the beginning of the year has brought some encouragement to the sector.

Sales volumes and sale rates are both up while buyers have increasingly looked beyond the confines of London and the south east for investments. Whilst retail remains dominant in the auction there has been a higher level of office and leisure lots finding buyers.

Retail yields hardened to 6.2% while the average property yield across all sales in the auction room was also sharper at 8.5%. The gap between prime and high yield properties has continued to open and is now at its widest for more than a decade.

Investors remain assiduous in their requirements and are now focusing on sustainable market rent in addition to lease length and tenant covenant strength. However, with volume in the auction room and more pricing evidence as a consequence, we remain cautiously optimistic that the market will move forward with more purpose as the year progresses.

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

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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

▲ **43%** Sales Volume

▲ **64%** of sales were retail properties

▲ **75%** Sales Rate

▼ **8.5%** average initial yield

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IPD

AUCTION COMMENTARY

In the room: more volume and more sales

Since the end of last year, the volume of auction room transactions has risen by 43% which is partly as a result of a build up of a number of instructions that missed the December round of auctions but also reflects an increased sale rate which has risen from 66% to 75%.

The increased sale rate is an indication that the uncertainty in the market that prevailed in the second half of 2011 may have lessened although considerable investor caution still prevails for more secondary assets. Interestingly, there was a significant increase in transactions involving properties outside London. The proportion of non-London properties selling since December rose by 65% and accounted for 85% of all properties sold.

Retail is still the dominant property sector accounting for 64% of properties sold but there has been a large increase in the office sector which accounted for 22%.This is the highest proportion on record. Encouragingly the sale rate for offices was equally high achieving 95% which is again the highest recorded.

The sale rates (excluding post auction sales) for all of the property sectors have risen since December with retail standing at 72% and leisure at an encouraging 75%. Leisure accounted for 15% of the total lots sold which suggests that investors are becoming more comfortable with this sector after concerns about sustainable profitability.

There has been a significant rise of the larger (>£1m) lot sizes and this may have brought to an end the continuous fall in average lots sizes that has been prevalent during the last nine months. In part this may be due to the availability of debt (albeit still small) for the better quality investments.

The figures would suggest that investors are happy to invest in sectors other than retail and in areas other than London but there may be a shortage of supply of the "right" type of assets at the correct market price.

COMMERCIAL AUCTION SALES SUMMARY

		Mar 2012	Dec 2011
Volume (£ million)	▲	56.7	39.7
Properties Sold	▲	99	84
Average Lot Size (£)	▲	572,530	472,786
Sales Rate	▲	75.3%	66.7%

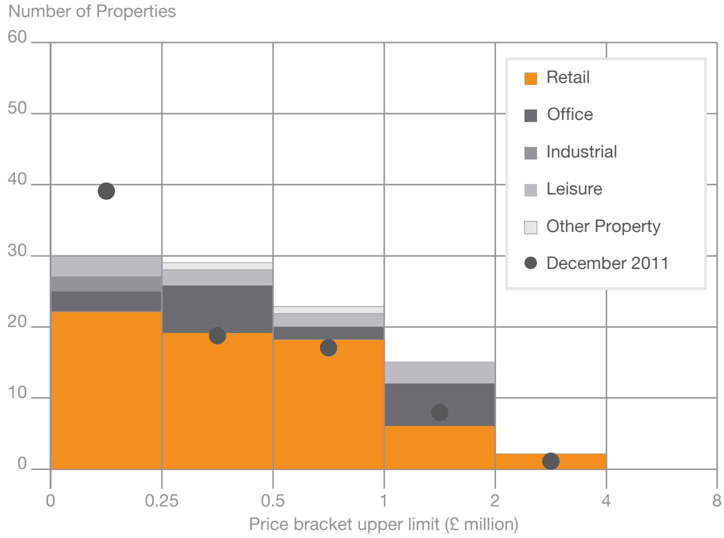
COMMERCIAL AUCTION SALES, £ MILLION

Sector		Mar 2012	Dec 2011
Retail	▲	36.0	21.0
Office	▲	12.3	9.8
Industrial	▼	0.2	0.4
Leisure and Other	▼	8.2	8.5
Region		**Mar 2012**	**Dec 2011**
London	▼	8.8	10.7
Rest of UK	▲	47.9	29.0

COMMERCIAL AUCTION SALES RATE, %

Sector		Mar 2012	Dec 2011
Retail	▲	72%	67%
Office	▲	95%	74%
Industrial	▲	100%	33%
Leisure and Other	▲	75%	62%
Region		**Mar 2012**	**Dec 2011**
London	▼	75%	82%
Rest of UK	▲	75%	64%

COMMERCIAL AUCTION SALES BY PRICE BAND



In the market: yields sharpen for better stock

Results from the auction market indicate that there has been a small improvement in confidence for better quality investments. The average initial yield hardened to 8.5% from 9.1% with the prime yield coming in 60 basis points to 6.2%.

The average yield for retail has hardened to 8.1% with the office yield standing at 10.6%. London is still more popular with investors with average yields standing at 110 basis points lower than for the rest of the UK. The gap of 380 basis points between prime and high yield property is the widest since 2001.

Since December, the upper quartile yield weakened 40 basis points to stand at 10% - the highest level for 10 years. This is due to a number of factors including the risk premium required to compensate for tenant failure and voids, and also the impact of over-rentedness. The fact that there are buyers for these secondary assets is encouraging. Their sale is generating pricing evidence and this could stimulate the release of further assets onto the market.

Arguably better quality stock may now need to include a new criterion - sustainable market rent - to add to length of unexpired lease and strength of the tenant's financial standing. A new letting in today's market is clearly more desirable to investors than an existing rent that was agreed five years ago. Of particular concern to an investor in buying existing leases is not only trying to estimate the level of over-rentedness but also to judge how long the tenant can continue paying a rent that might be double the current market rent.

Yields by lot size are arguably counter-intuitive with the lowest average yields not being for the smaller investments. The lowest average yield is for investments over £1m. Whilst many pundits believe yields on the smaller lots should be lower than the larger lots because there will be more buyers for the smaller lots, and indeed this may be true, this does not lead to a correspondingly higher price and lower yields for them. Rationally the yields should be broadly unaffected by size because the investment criteria are the same and the returns required will therefore be consistent.

* Weighted by Sale Price

**AIY = Average Initial Yield

YIELD SUMMARY

All Commercial Property Totals		Mar 2012	Dec 2011
Average Initial Yield	▼	8.5%	9.1%
Lower Yield Quartile	▼	6.2%	6.8%
Upper Yield Quartile	▲	10.0%	9.6%
Yield by Unexpired Lease Term			
0-5 years	▼	9.6%	12.6%
6-15 years	▼	8.4%	8.9%
16 years +	▼	8.6%	8.8%
Yield by Value Band			
£0 - £250,000	▼	8.5%	9.0%
£250,000 - £500,000	▼	8.9%	9.3%
£500,000 - £1 million	▼	8.6%	8.7%
£1 million +	▼	7.6%	9.7%

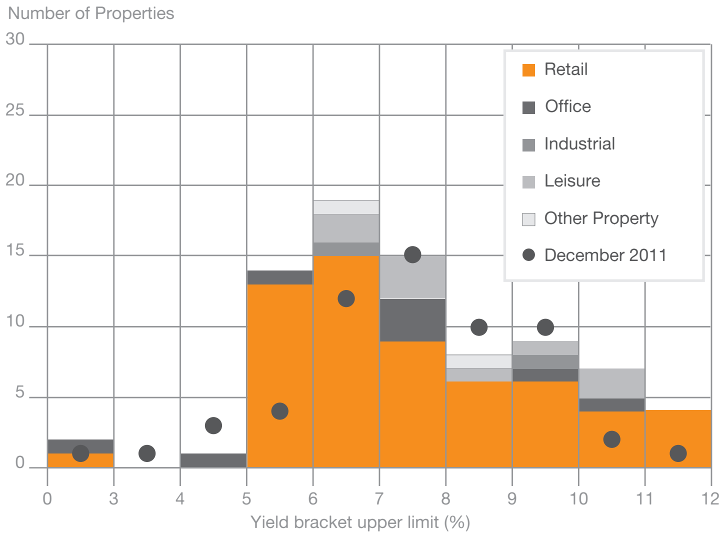
YIELD SUMMARY BY SECTOR

Sector		Mar 2012	Dec 2011
Retail	▼	8.1%	9.3%
Office	▲	10.6%	10.5%
Industrial	▼	7.8%	9.7%
Leisure and Other	▲	8.2%	6.7%

YIELD SUMMARY BY REGION

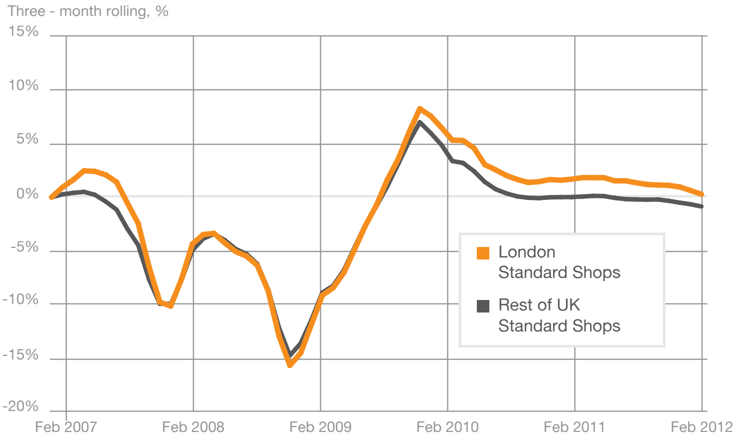
Sector		Mar 2012	Dec 2011
London	▼	7.5%	9.1%
Rest of UK	▼	8.6%	9.1%

YIELD SUMMARY BY YIELD BAND



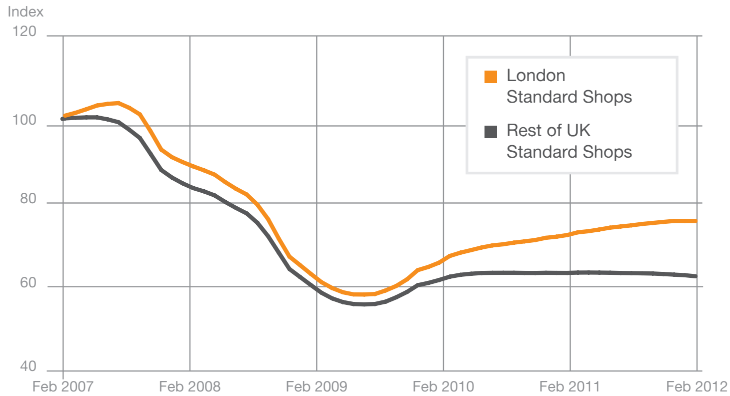
STANDARD SHOPS
THREE-MONTH ROLLING CAPITAL VALUE CHANGE, %

Source: IPD UK Monthly



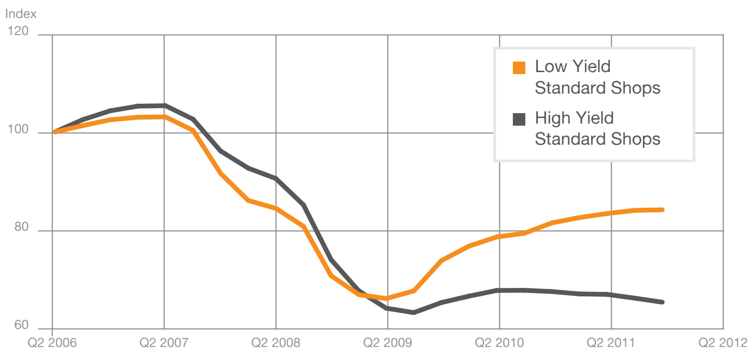
STANDARD SHOPS
CAPITAL VALUE INDICES BY REGION, MONTHLY

Source: IPD UK Monthly



STANDARD SHOPS
CAPITAL VALUE INDICES BY YIELD, QUARTERLY

Source: IPD UK Quarterly



IPD PROPERTY MARKET COMMENTARY

Retail capital values have fallen further in the last few months. According to the IPD Monthly Index, a fall of 0.4% m/m was recorded in February 2012. The recent downward pressure on the price of retail assets has resulted in negative capital growth on a 12 month rolling basis, for the first time since 2009.

In contrast to the consistent growth seen in the second half of 2011, the price of standard shops in London rose by just 0.3% in the three months to February. Regional economic growth remained sluggish and shops outside of London continued to see their values suffer, falling 0.9% over the same period. Despite the economy contracting in Q4 2011, a number of signs have suggested that the outlook for 2012 may be more positive than expected.

The out performance of prime over secondary stock continued into Q4 2011. Low-yielding assets (regarded as a proxy for prime), saw capital appreciation of just 0.1% q/q or 3.3% y/y while the price of high-yielding assets (secondary) continued to fall at a similar rate as the previous quarter, 1.2% q/q or 3.2% y/y. Strong income returns have continued to aid performance. The reliance of prime stock on income was noticeable in Q4 2011 when prices rose minimally.

2011 was an unsettled year and previously, cPad highlighted that 2012 may bring new opportunities to investors equipped with equity and asset management skills. Yields rose throughout most of 2011 but the latest EIG data revealed that yields, particularly prime, have fallen since December 2011. Secondary yields have continued to move out.

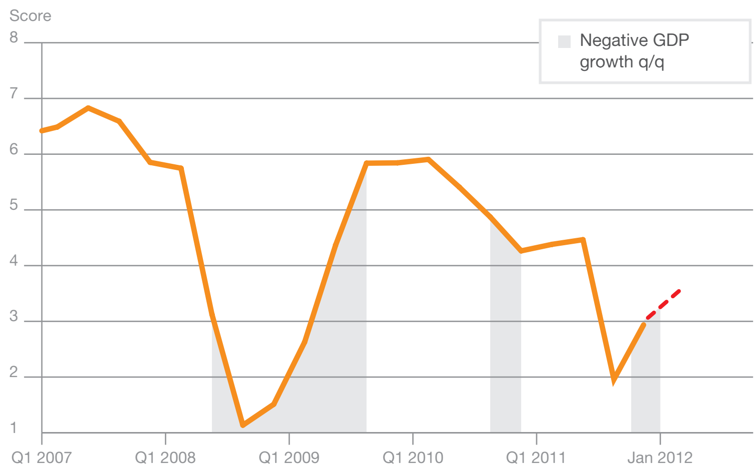
So far in 2012, capital value losses have been fairly mild and the price of prime stock is still holding up, despite London shops declining m/m in January and February (flat on a 3 month basis). A close watch on retailer sentiment is needed to gauge potential occupier demand, which is important for an income-dominated market. This at least shows some promise even if investor sentiment is still weak.

KEY MARKET DATA

Economic Score Card Average

The economic score card average rose to 3.4 in January 2012, up from 3.0 in Q4 2011. This was largely down to the improvement in equity prices while consumer confidence posed as a drag on the overall score. Leading indicators are still fairly weak but despite this, retailers seemed to be buoyed after a decent Christmas and there has been an improvement in retail trade confidence. Inflation seems to be heading in the right direction and house prices experienced a slight fall.

ECONOMIC SCORE CARD AVERAGE



	2007				2008				2009				2010				2011				2012
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Jan
Economic Score Card Average	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	3.0	3.4
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
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
Nationwide House Price Index (q/q)	7	7	5	4	3	1	1	1	4	7	7	5	6	7	3	2	6	7	4	3	3
Consumer Confidence	7	7	7	7	6	1	1	1	1	2	6	6	7	5	3	2	1	3	1	1	1
Unemployment Expectations	7	7	7	7	7	5	2	1	1	1	3	4	5	4	3	3	2	4	4	2	2
Retail Trade Confidence	7	7	7	5	7	4	1	1	1	4	7	7	7	6	7	7	7	5	1	4	4
Expected Retail Trade	7	7	7	4	7	4	1	1	1	2	6	7	7	7	7	7	7	5	1	3	4

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

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ECONOMIC SCORE CARD VARIABLES

Economic Score Card Variables	Score	Jan 2012	10-yr avg.	Analysis
Economic Score Card Average	3.4	3.4	5.7	The ESC average improved from 3.0 in Q4 2011 to 3.4 in January, thanks to improvements to the scores of the inflation and the expected retail trade. However the score is still well below the 10-year average of 5.7.
Inflation (CPI y/y)*	3	3.6%	2.2%	Inflation has been falling since October 2011 and stands at 3.6% year-on-year in January 2012. It is still well above the 2% target. Downward pressure came mainly from fuels & lubricants, products bought in restaurants & cafes, tobacco and vehicles.
FTSE All Share (q/q)	7	7.1%	0.0%	There is still high uncertainty and volatility in the markets. Overall, shares ended the month 7.1% up on the prior three months, well above the 10-year average of 0%. In November it was -7%.
Nationwide House Price Index (q/q)	3	-2.1%	1.8%	UK house prices declined by 0.2% in January but are 0.6% higher than one year ago. Due to the high level of uncertainty in the last part of 2011, it comes as no surprise that prices are below the level reported in the three months prior. Demand for homes remain cautious.
Consumer Confidence	1	-22	-8	The consumer confidence index came in at -22 in January, up from -24 in November as lower energy costs and retailer discounts provided hard-pressed consumers with some relief.
Unemployment Expectations**	2	50	30	The situation on the job market is still difficult as the jobless total hit a 17-year high at the end of January. January saw the survey return a score of 50, up from 48 in November 2011 and well above the long-term average of 30.
Retail Trade Confidence	4	-12	1	Retail trade confidence was less negative at -12 at the end of January 2012, up from -26 in November though it is well below the 10-year average of 1.
Expected Retail Trade	4	-7	11	Expected retail trade confidence is also improving: it was at -7 at the end of January, up from -30 in November 2011. However, it remains well below the 10-year average of 11.

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

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

Source: IPD, ONS, EcoWin, Nationwide

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 below.

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

Acuitus

Richard Auterac
Chairman and Auctioneer
+44 (0)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

Greg Mansell
Research Manager
+44 (0) 20 7336 9384
greg.mansell@ipd.com

Investment Property Databank
1 St John's Lane,
London EC1M 4BL

ipd.com

EIG

David Sandeman
Managing Director
+44 (0)1737 232289
davids@eigroup.co.uk

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

eigroup.co.uk