Q2

MARKET UPDATE

2022

Commercial & Residential

allsop

Contents

The occupational markets are in good health with workers returning to their offices, retail stabilising and industrial occupation as strong as ever.

Economic Overview

The UK economy is being impacted by a range of challenging issues at present which are causing volatility, uncertainty and caution in the markets. We are currently facing the political turmoil of a change in leadership in the Conservative government following the resignation of Boris Johnson and a leadership race is on with a new prime minister due to be announced on September 5th. Government business, therefore, is effectively on pause for the summer.

The war in Eastern Europe continues, and now looks set to run for the longer term. The West continues to respond by tightening Russian sanctions and in return Russia is increasingly restricting its supply of gas, fuel, and grain, all of which are pushing inflation, heighted in any event by the pick-up of activity since the pandemic, to heights not seen for decades.

Inflation is the big concern for economists. Once set in it can be self-generating and its symptoms, including the increased cost-of-living, the erosion of the value of savings and the increasing cost of debt, are a major headache. The BoE has continued to increase its inflation forecasts and is now expected to peak towards the end of the year at 11%. In response the interest rate now at 1.25% is likely to be raised again in August. Commentators are increasingly of the view that a more aggressive set of interest rate hikes will be needed to control inflation, with some expectations of a peak in rates at over 2.5%.

The economy has returned to growth in May after shrinking in March and April and there is likely to be a bumpy road ahead, particularly if there is a more aggressive stance on interest rates.

The real estate markets have been buoyant in the most part for the first half of the year although the outlook for the second half is more cautious. The occupational markets are in good health with workers returning to their offices, retail stabilising and industrial occupation as strong as ever. Demand in the residential market remains unabated too despite the headwinds. The investment markets are however absorbing the uncertainty and the froth has certainly started to come out of those hotter commercial sectors with the industrial market, in particular, being pegged back. Investors have become wary of the extent of a downturn with some adopting the wait and see approach. There is much concern too over high construction costs and the effect these are having in the development markets. There is certainly plenty to consider over the summer recess.

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City & City Fringe Leasing Market

There continues to be a search for the Best in Class space so that occupiers are able to offer the best working environments for their staff. Best in Class Grade 'A' stock accounted for 90% of take up in the last quarter.

The second quarter of 2022 has continued the good run and strong activity experienced during the first quarter. This has led to a buoyant first half of the year with the greatest number of deals since March 2020.

The change in working practice is now settling into a regular pattern in the City with many businesses embracing flexible working and incorporating a working from home culture into occupier relocations. Many fit outs are now based on one person per 10 sqm and new working practices have increased levels of collaboration space, wellbeing, outside space and end of trip facilities. There is an ever increasing focus on sustainability and the genuine integration of this into new working environments. This is at the forefront of both occupiers and developers strategies in recent months given the wider media coverage on the issues with global warming. There continues to be a search for the Best in Class space so that occupiers are able to offer the best working environments for their staff. Best in Class Grade 'A' stock accounted for 90% of take up in the last quarter.

As we enter the second half of 2022, there is increasing pressure on the cost of materials with inflation leading to a concern over the delivery of schemes for Category 'A' and Category 'B' finishes.

The Allsop weekly viewings tracker has now recorded another month of record viewings witnessed since recording the full data at the start of lockdown in March 2020. 46 viewings were undertaken in the week ending 7th June. The running total is now averaging 30.8 viewings per week in 2022 compared to 18.5 in 2021 and 7.2 in 2020. The majority of viewings have been for sub 10,000 sqft with business focussing on fitted options sub 5,000 sqft.

The weekly active demand (monitored through the Agents Society) is now averaging 113.4 enquiries per week in 2022 compared to 87.7 in 2021 and 53 in 2020.

Take up for Q2 2022 represented the strongest level since pre-pandemic as a result of the major pre-lets in the City and West End Markets. The most significant deals included The Kirkland and Ellis letting at 40 Leadenhall Street for 400,000 sqft, albeit with significant expansion and contraction options and the short term letting to Hogan Lovells at 10 Fleet Place for 33,000 sqft at £67.50 per sqft for a 10 year lease and five year break.

Central London take up exceeded 3.7M sqft. The highest figures since 2018 although largely driven by The Kirkland & Ellis pre-let.

For the first half of the year, there were only 8 transactions greater than 50,000 sqft, however in the smaller size bracket between 10,000 and 24,999 sqft there were 69 transactions in total – more than any year since 2018. Deals below 20,000 sqft accounted for just less than 50% of take up.

City take up for Q2 totalled 1.59M sqft, which represents a 15% increase on the 5 year quarterly average, and 80% up on last year's Q2. 2.9M sqft has now been let this year, which again is a 15% increase on the 5 year average. Total space under offer remains 9% below the five-year quarterly average however standing at 1.51M sqft, albeit this is 15% above the same period in 2021.

Aside from the main deals highlighted above other key under offers include Reed Smith (127,000 sqft), King and Spalding (30,000 sqft) and Snowflake (37,000 sqft). The Legal sector continues to drive further demand with Proskauer Rose (40,000 sqft) and Goodwin Procter (80,000 sqft) all looking to expand into new premises as the war for legal talent drives businesses to search for better quality space. Many other businesses are still monitoring their space requirements and reviewing the work place strategy further. These include Vodafone, Grant Thornton and Accenture Digital.

Supply across the Central Markets has reduced to the lowest levels since Q4 2020 at 24.5M although does remain above the long term average. The City supply fell marginally to 12.1M sqft and a vacancy rate of 8.9%.

The City fringe market witnessed the launch of The Featherstone Building with record rents being achieved for Shoreditch at £90 psf to Dept Agency for the top floor.

Strong rents continue to be achieved for 'Best in Class' stock with Beamery taking Levels 20 and 21 at Hylo for a rent close to £90 psf for a Cat B fitted solution and Zeno securing the top floor at Spectrum, 160 Old Street at £80 psf. Best in Class stock, Bridge House in Southwark and The Bindery, Farringdon have set new record rents for small suites and fitted units sub 5,000 sqft.

Rents achieved for new Best in Class Grade A buildings, both glass and steel and warehouse style premises, are achieving rents in the low to mid £80's psf with high £80's psf for terraced floors.

Rents for typical Grade A space on a mid-floor have moved up slightly to £72.50 psf.

Rent free periods remain at 2.4 months per year although these are likely to move in slightly on upper terraced floors and where there is competition for good quality Grade A space. Grade B stock remains challenging and Landlords will offer longer rent free periods of 2.4 – 2.7 months plus.

The pressure of inflation and increased build costs may create further challenging conditions for the second half of 2022 for developers. This will however be countered with the drive for occupiers to appeal to staff driven by the war for talent, reposition their businesses and assist with policies to improve their sustainability agenda.

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City & City Fringe Investment Market

Since a record quarter of transactions in Q1 2022, sentiment within the City and City fringe investment market experienced a swift and major change as we moved through Q2 2022. Despite the streets of the Square Mile being the busiest they have been since the end of 2019 and confidence in the occupational market for best-in-class product stronger than ever, the Central London Investment market has started to experience new challenges, some of which it hasn't experienced for many years.

Since the start of April interest rates have increased and they are yet to stabilise which has caused nervousness amongst lenders. Coupled with inflationary pressures and the on-going geopolitical situation in Ukraine, investor sentiment has become increasingly clouded. As many of the buyers in Central London finance their purchases with debt, this volatility has caused uncertainty and nervousness and gaps have quickly formed between vendor aspirations and prices purchasers are prepared to pay. The political environment domestically is also experiencing its own challenges and with Boris Johnson having resigned and uncertainty over who will lead the country next, purchasers seem to have more excuses than ever before to simply sit and wait.

During the second quarter of 2022 Allsop recorded only £1.146Bn of commercial property transactions exchanged or completed in the City and City Fringe Markets. This is a decrease of approximately 72% on Q1 2022's figures of £4.032Bn and even half of Q2 2021 volumes which was £2.375Bn. This total has been recorded across 23 transactions, which is ten lower than the four year quarterly average prior to the pandemic (33). 14 of these were sub £20M transactions in terms of lot size.

The total transactions figure for the quarter was skewed by two substantial transactions. One was the completion of Goldman Sachs and Greycoat's acquisition of Christchurch Court, 10-15 Newgate Street, EC1 for £370M, reflecting £1,218 psf which is a forward purchase of a building under refurbishment by HK-based, Shimao Property. The buyer is taking on substantial leasing risk but on refurbished space opposite St Paul's Cathedral and we understand there are already some major pre-let discussions taking place.

> The flight to high quality buildings with strong ESG credentials is becoming more and more evident

The other significant transaction of the quarter was the sale of Brookfield's 2 London Wall Place, EC2 to HK-based Kingboard for a purchase price of £302M, £1,600 psf reflecting a yield of 3.98%. This relatively new development is held long leasehold with a gearing of 5% and is multi-let to nine tenants showing a WAULT of 9.4 years to earliest determination. Even though the price was agreed in Q1, this acquisition shows that despite the uncertainties in the UK's financial and political landscape market, the appetite from overseas investors is still there for best in class assets in prime City locations.

The flight to high quality buildings with strong ESG credentials is becoming more and more evident. Allsop advised on the sale of Wool and Taylor, 10-12 Alie Street, E1 on behalf of Maurice Investments to Meadow Partners for a price of £26,000,000 reflecting £960 psf and a yield of 5.00%. The building is multi-let to five tenants with a WAULT of c.5 years to earliest determination. Recently refurbished the building benefits from EPC A and B ratings. A similarly high quality development was acquired by La Francais Group on Cannon Street, number 111 where Allsop were joint leasing agents. Developed by London and Oriental in 2018 the building was assessed to an EPC A and BREEAM 'Excellent'. Held long leasehold with an 8.5% gearing the building is multi-let to six office tenants off an average rent of £76.45 psf and La Francais paid the quoting price for the asset which was £27,870,000 and £1,480 psf reflecting a net initial yield of 4.50%. This is one of the highest capital values on record in the City core for a geared long leasehold but reinforces the attraction of high quality buildings to institutional purchasers especially if they benefit from strong ESG attributes.

The gap between vendors pricing aspirations and what purchasers are prepared to pay has widened, particularly on assets with a core plus profile where the increasing debt costs have really hampered returns. These conditions resulted in some large transactions being withdrawn from the market including Norges sale of 2 King Edward Street (c.£700M), CBREGi & Arax's sale of Duo, 280 Bishopsgate, EC2 (c.£500M) and Oxford Properties & Temasek's Mid-City Place (c.£425M). It will be interesting to see which of these are relaunched in Q4 2022 and if the quoting/guide pricing changes.

Allsop's household view is that prime City yields, which in Q1 2022 were reported as low as 3.75%, will start to move north of 4.00% with some commentators expecting movement out towards 4.25% and above. Buyer nationality is still skewed in favour of the UK purchaser who accounted for c.52% of transactions in terms of numbers, however the largest deals of the quarter were acquired by both US and HK-based money.

Despite lower transaction volumes there is still a significant amount of capital wanting to invest in Central London, particularly in the Value-Add sector where best in class can be created and there is currently very limited supply of this stock. There are also a number of substantial transactions currently under offer, totalling over £2Bn, which including the sale of Land Securities c.£1Bn 21 Moorfields as well as the sale of 20 Cabot Square c.£500M in Canary Wharf. This may result in a more buoyant Q3, however with debt becoming more expensive, no clear path to peace in Ukraine and increasing political instability domestically, purchasers are thinking twice before making any commitments. As a result the forecast is for a quiet summer period in the lead up to Q4.

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West End Leasing Market

Transaction levels in the West End have rebounded strongly in Q2 with take up reaching its 2nd highest level since 2014.

Transaction levels in the West End have rebounded strongly in Q2 with take up reaching its 2nd highest level since 2014. This was predominantly as a result of strong pre-letting activity occurring during the quarter. A number of these deals have been in negotiation for an extended period, but it reinforces the continuing occupier demand for large floorplate "best in class" new product.

In total there was just over 1.4M sqft let in Q2, up by c. 40% on the Q1 statistics and near the long-term average take up for the market. The quarter saw 29 deals over 10,000 sqft, the largest of which saw Capital Group securing 200,000 sqft at 1 Paddington Square, W2.

Other notable deals in the quarter included Qube Research & Technologies taking the 12th-15th floors (39,471 sqft) on a pre-let of Land Securities N2 development in Victoria at a blended rent of £93.50 per sqft, the United Talent Agency taking (27,575 sqft) on a sublet from Exane at One Newman Street, W1 and manufacturing company SharkNinja taking 25,000 sqft in Battersea Power Station, SW8.

In terms of supply, availability crept slightly upwards to c. 6M sqft, reflecting a vacancy rate at 6.9% across the West End (against 9.8% vacancy across Central London as a whole). As ever there is a distinct differential in submarket availabilities with Mayfair/St. James's at a historic low and Hammersmith at a historic high.

"Grey" space available from tenants has risen by c. 15% in the year to date, now totalling nearly 2M sqft. This is the highest level for over a decade, but notably comprises some very short terms available of sub three years in many cases.

Inflationary pressures and supply chain issues are continuing to affect the construction industry, and this has potential to affect delivery of new supply moving forward. There are currently 11.3M sqft of substantial refurbishment and new build schemes due for completion between now and 2025, 17% of which has already been pre-leased. There are a further 2.6M sqft of developments said to be targeting practical completion before the end of this year, although we are now seeing some of these timeframes slipping which could result in further supply side pressures.

We continue to see rental growth at the top end of the market in prime West End locations, with Mayfair & St. James's new developments continuing to set new record rents at over £130 per sqft. This is serving to highlight the increasing disconnect with Grade B rents which are continuing to fall, in some instances to levels not seen for nearly a decade.

In conclusion, demand for the best office spaces in the West End continues to remain buoyant in the face of macro-economic pressures. As the year progresses continuing upward pressure on rents is anticipated for new space as occupiers compete for an eroding development supply pipeline.

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West End Investment Market

We recorded a total of £1.7Bn exchanged or exchanged and completed in 24 transactions across Q2 2022, reflecting an average lot size of just under £72M. Similarly to Q1, volume was buoyed by one transaction, and if you were to remove the large ticket lot size of Singaporean sovereign wealth fund GIC's acquisition of a 75% stake in the Paddington Central Campus for £694M from the equation, this reduces the average lot size to £43M and illustrates a Q2 total volume of c. £1Bn, c. 23% below the five-year average (£1.3Bn).

This brings the H1 2022 total to £3.1Bn (41 transactions), marginally down on the pre-pandemic average of £3.6Bn and a rebound on 2021 half year totals that were 50% down (£1.8Bn).

Q2 2022 included four transactions over £100M - Sinar Mas Land's purchase of 40 Strand, WC2 (£195M / 4.20% NIY) following a change of purchaser by vendor Land Securities; LVHM's acquisition of their London flagship Dior retail store on Bond Street, W1 (c. £150M / c. 2.50% NIY) from O&H Properties; BC Partners purchase of one of London's most exciting development opportunities, Selkirk House, WC1 (£115M) from Teddy Sagi's property company Lab Tech; and Paddington Central W2, £694M (4.50% NIY).

International investment rebounded this quarter accounting for the usual norm of c. 75% of transaction volumes. Asian investors were back dominating the market in Q2 accounting for 56% of the total volume or c. £1Bn worth of transactions, being notably responsible for two of the four deals over £100 million – Paddington Central Campus and 40 Strand. Middle Eastern investors are still yet to return to the West End investment market fully being responsible for only one transaction so far this year, Alduwaliya's acquisition of 15-16 Bedford Street, WC2 for £34.8M (4.25% NIY) during Q2. By contrast however, Domestic UK purchasers continue to dominate the overall number of transactions, being responsible for 15 of the 24 deals or c 65%.

Over recent weeks the events being experienced in the financial markets and geopolitical environment – rising inflation, increasing interest rates, UK political leadership uncertainty and ongoing war in Ukraine, to name a few – has seen a number of sales being pulled from the market in a widely publicised fashion by the property press. However, the headlines fail to illustrate the full story. To date those sales which have been withdrawn have tended to be concentrated in the City market and have been generally been as a result of a disparity between Vendor and Purchaser expectations, rather than a lack of investor appetite or monies. During Q2 the themes of Q1 (that have continued throughout the wider post-pandemic period) remain unchanged. The West End market continues to be buoyed by investor demand for 'flight-to-prime' investment opportunities for example, Pembroke's sale of 49 Park Lane to BTV fronted by CBRE IM being agreed at £93M / 2.75% NIY – one of the few 'super-prime' office deals to hit sub-3.00%. Similarly, 'value-add' opportunities are still attracting significant interest for example, Allsop's ongoing sale of 7 Ridgmount Street, which is currently 'Under Offer' following 70+ inspections with c. 55 separate parties.

As we enter the summer, the market is also waiting with great anticipation to see what happens to a number of deals that have been under offer for a while and whether price renegotiations will take place to reflect changing market conditions. There are also a number of instances where bids have been received below quoting price or vendor aspirations - sellers will have a decision to make whether to accept a revised pricing or continue to hold the asset.

We have also seen a number of opportunities launched to the market in recent weeks, which is unprecedented and we suspect vendors wish to capitalise on the known market conditions of today rather than those of the future. We do however expect a busy end to the year as the market adapts and stabilises to revised market conditions as the sheer volume of global capital weighted to sheer volume of global capital allocated to Central London remains unchanged.

> International investment rebounded this quarter accounting for the usual norm of c. 75% of transaction volumes

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National Investment Market Overview

Despite rising inflation and the fifth increase in interest rates since December 2021, market sentiment towards commercial property remains broadly positive. Commercial property investment volumes in H1 have seen the strongest start to the year since 2015, however, the ongoing geopolitical crisis in the Ukraine and coronavirus outbreaks in China and the inflation and interest rate environment at home have dampened sentiment amongst investors.

Transaction volumes:

Full year 2021	H2 2022	Q2 2022
£55,202.82M	**£27,903.73M**	**£12,756.66M**
Up 26.55% on full year 2020	Up 17.41% up on H2 2021	Down 7.39% from Q2 2021

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Retail Market Overview

Considering the UK is predicted to witness the biggest reduction in household income since the 1950s, high street retail assets have fared well in Q2 2022. Whilst investor sentiment towards the retail market has slowed due to the gloomy economic forecasts resulting in a reduced pool of buyers, well-positioned assets with strong fundamentals continue to trade well.

Retail sales volumes fell by 0.5% in May and the outlook for consumer spending appears very tough as households tighten their belts. Investors are weary of the higher cost of living, high inflation and increasing interest rates and the knock on effects on the market as a whole.

There has been an evident pattern of funds exiting high street retail assets since the pandemic which will continue to be the theme later in the year. Notable high street transactions included abrdn's sale of 123-129 Buchanan Street, Glasgow which was purchased by Ediston Properties in April for £16M and 40 Broad Street, Reading purchased by a private investor. It is expected that high street retail will offer significant value for money for private investors in the latter stages of 2022.

Purchasers of such assets see the high street as an opportunity. Rents in most high streets have seen significant rebasing from before and during the pandemic and on average are now some 40% or more below the peak. Many high streets are now stabilising and occupiers are returning, but there is still caution and there are some locations with a long way to go before improvement is seen.

Food and beverage operators continue to take advantage of the struggling retail landscape and some occupiers are able to carry on their robust expansion plans. The retail landscape continues to change as no doubt will be the case for the immediate future.

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Retail Warehousing Market Overview

Q2 2022 continued to see an ongoing spike in transactional activity in the retail warehouse sector, with the key theme being portfolios. The Crown Estate brought the Peacock Portfolio to the market for circa £250M / NIY of 6.75%. This portfolio consists of four assets in Nottingham, Banbury, Newcastle-upon-Tyne and Maidstone, which are strong regional locations. The majority of Project Zebra, Sports Direct's portfolio disposal is under offer to an American Investor and M7's Boxes portfolio has been broken up between institutional investors with Great Lodge Retail Park in Tunbridge Wells looking to achieve sub 5% NIY. This again shows strong pricing being achieved for prime southeast schemes where there is a strong institutional market.

On top of these portfolio sales there has been a flurry of retail warehousing stock come to the market totalling over £650M+. This includes Castle Marina, Nottingham and Tandem Centre in Colliers Wood both being sold by LaSalle. Purley Cross Retail Park Croydon, Solihull Retail Park, London Road Retail Park, Enfield and The Orange (B&Q) Portfolio.

We are still strong believers in the fundamentals of retail warehousing and its ongoing performance, however with the increase in cost of capital and one-off buyers now having filled their requirements we are anticipating a softening in pricing from the middle of the year. The occupational market is still in a positive position with downward pressure on the current vacancy rate which is now 5.4%. Retailer performance and covenant strength remain strong in the sector and, as a result, it has all but completed the rebasing of rents.

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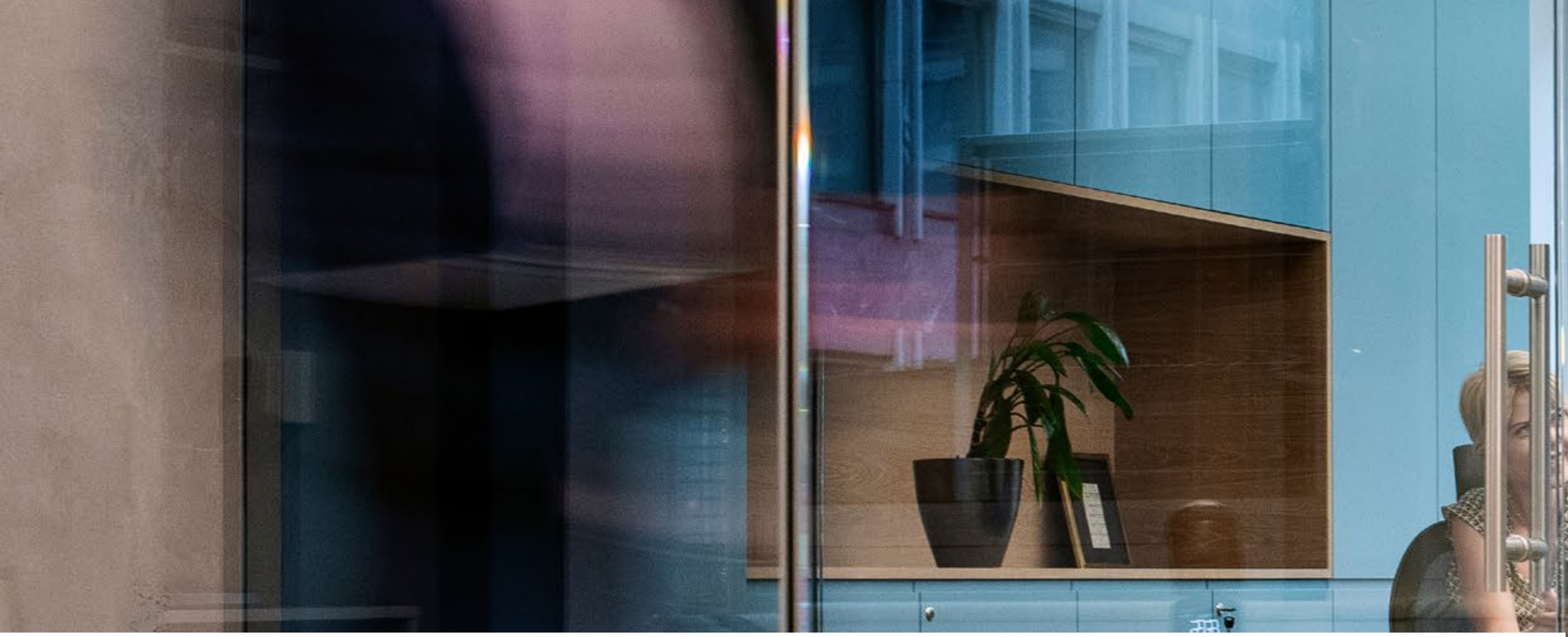

Office Market Overview

The national office market saw yield compression in Q1, with a strong level of demand being led by the overseas investment market. Whilst yields have remained mostly static in Q2, demand has once again been driven by overseas investors, accounting for 60% of transaction volume.

The majority of this investment has been larger lot sizes, with four transactions in excess of £100M, the largest of which being 177 Bothwell St, Glasgow. The property was purchased by PonteGadea Inmobiliaria in an off market deal for £215M in April. Indeed the average lot size for South East office deals was up to £38M (the 10 year average is £20M).

Allsop were at the forefront of regional office transactions this quarter, advising Citi Private Bank of their £100M acquisition of One Forbury Place, Reading, reflecting a NIY of 5.64%.

Other notable transactions include Colmore Plaza, Birmingham, which traded for £182M to Blackstone. Additionally, Q2 has seen a flurry of Business Park transactions totalling £400M including Gloucester Business Park (£130M), Capital Business Park Cambridge (£175M) and Oxford Technology Park (£185M). Following a similar pattern to the previous quarter, investment has been focused on the Big 6 cities, key regional towns, and life science opportunities around the Oxford / Cambridge arc.

Looking forward, rising debt costs and ongoing build cost inflation, Q3 is set to be an interesting period in the market. We expect these headwinds to be largely counteracted by rental growth for high quality accommodation and weight of international capital meaning we don't foresee meaningful repricing across the national office markets.

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Industrial Market Overview

Transaction volumes for H1 2022 continued on a trajectory set by the record-high of 2021 (£18.1Bn). Big-ticket investors were still focused on increasing their exposure to logistics however, the bright blue skies of the past six months now have one or two clouds lingering on the horizon. Amazon's announcement that it was scaling back its warehousing plans, caused a shockwave through the sector with Segro's share price falling an almost unimaginable 10% in one day.

Rising debt costs, soaring inflation and concerns over exit yields have meant that the UK's most active buyers of logistics, namely the Institutional Funds and US Private equity, might be excused for taking stock of the situation. This increased cautiousness has seen a softening of pricing on the sharpest priced assets with investors looking towards more opportunistic opportunities.

That said, the market fundamentals remain remarkably strong and we see this as a temporary pricing correction over Q3 and into Q4. Occupier demand continues to be overwhelmingly positive. Rents have risen by an average of 16% since the start of the year and vacancy rates have dropped to a record low of just 2.8%. Transaction volumes remain strong with Allsop completing over £100M of industrial transactions in May including the acquisition of Castle Park, Nottingham and the sale of Wye Estate, High Wycombe.

With continued rental growth expected to outperform other sectors, industrial should remain front and centre in the minds of institutional investors.

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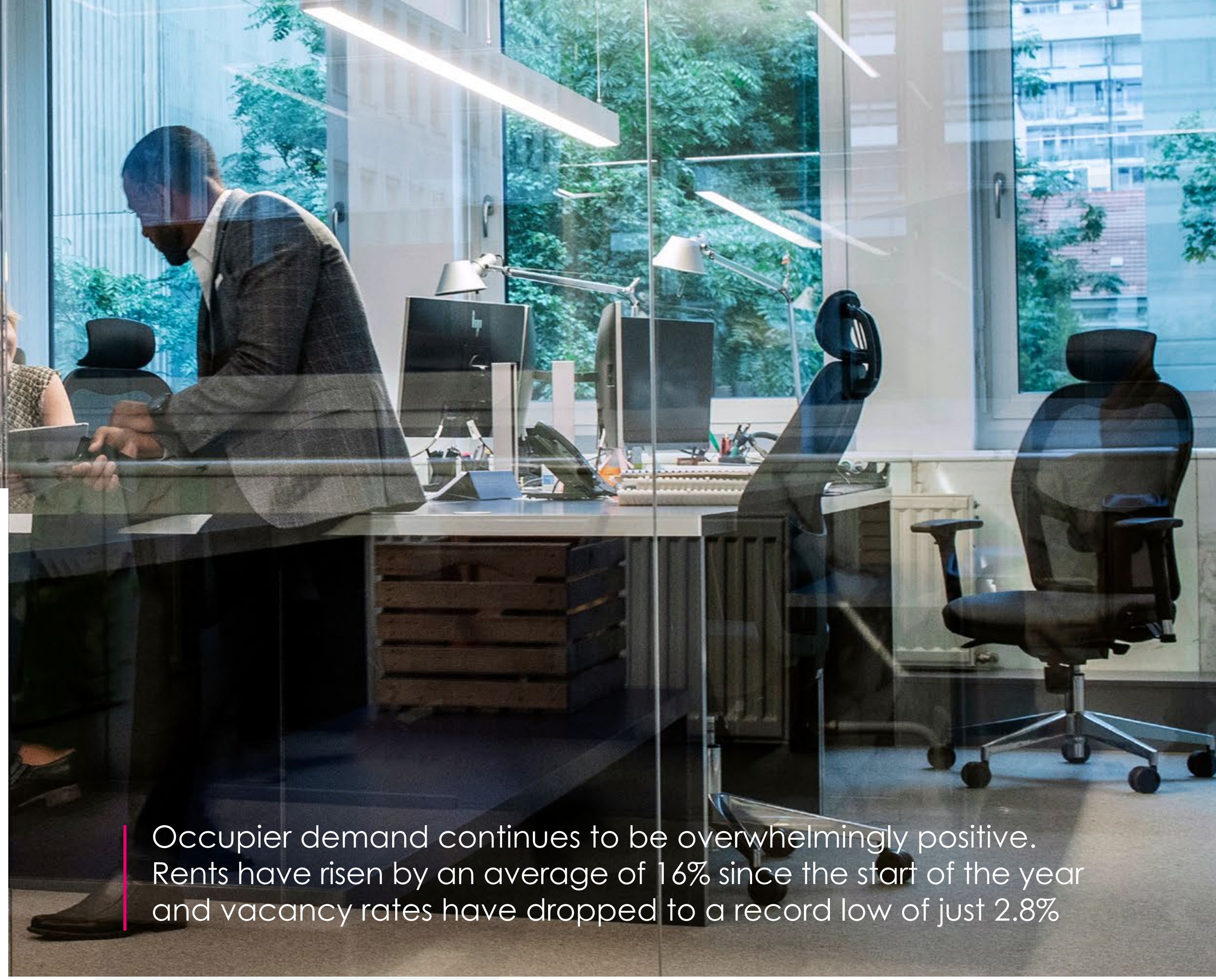

Portfolio Market Overview

It feels like déjà vu when talking about the portfolio market and the Industrial sector's dominance in recent years.

Whilst the industrial sector continued to mark its territory, accounting for a third of all transactions, it was the alternatives sector, in particular care homes that saw over £300M invested across eight deals reflecting the biggest competitor to the Industrial sector this quarter.

Approximately 25% of all transactions were captured within the £20M - £60M range, marking an improvement from Q1, compounding our comments made in the previous edition.

However, Q2 was dominated by larger transactions with 11 deals taking place in excess of £70M, accounting for roughly 70% of transaction volume.

The largest transaction was Kennedy Wilson's £227M logistics portfolio, acquired from Leftfield Capital, marking the largest of four £100M+ deals recorded this month.

The portfolio market was tipped to have a very strong Q2, and whilst there were a number of large deals, it underwhelmed against previous expectations. It is becoming apparent there is greater investor uncertainty surrounding markets due to dampening economic conditions and wider geopolitical factors, all of which hold more weight when analysing high value portfolios and the added risks these may present.

As we look ahead to H2, there remains a strong weight of capital ready to be deployed into UK Real Estate and the market is set to race on after the summer.

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Commercial Auction Market

Unsurprisingly, early May saw another interest rate rise as inflation continued to climb to a 40-year high and headlines of the cost-of-living crisis became ever more prevalent. As we approached our 25th May auction, we were conscious of how this would impact market sentiment and the private investors' appetite for commercial real estate.

However, the strong results of the sale proved that the market was as yet undeterred by a more unsettling economic environment and, with now £101M raised at the auction through the sale of 116 lots, it proved to be the second largest online property auction ever held in the UK. Of the lots sold, 36 achieved £1M or more and this highlighted continued buyer confidence in acquiring larger lots. The average lot size across the catalogue increased to £875,000 and 23 lots achieved yields of 5% or better.

> Encouragingly we saw a 25% increase in the number of registered bidders for this sale which evidently filtered through to the positive results achieved on the day

Encouragingly we saw a 25% increase in the number of registered bidders for this sale which evidently filtered through to the positive results achieved on the day. Many of these registered bidders were completely new to the commercial real estate market, likely as a result of significant volatility in other investment markets. Our market continues to be cash driven with the majority of our buyers informing us they are initially purchasing without the requirement for finance. Demand for further acquisitions remains unabated, with more than 90% of purchasers indicating they wish to buy again within the next 12 months.

The ever-popular convenience store sector once again featured prominently in our May auction with 12 such investments sold, three of which were at 5% NIY or better. The most notable of these was in Colchester town centre. Let on a new 20-year lease to Tesco (with 15 year break) and RPI linked reviews, the property sold prior to auction for £2.4M reflecting a net initial yield of 3.9%.

The Boots portfolio saw further positive results on the day with 16 such investments sold realising a total of £22.32M and reflecting an average lot size of £1.395M (5.4% NIY). Lot 3, Raynes Park, had 25 registered bidders on the day and sold for £812,000 (3.94%). The future redevelopment angle of the upper floors was clearly a driver of demand and buyers were perhaps more focused on the capital rate psf (£351) as opposed the net initial yield as a barometer of pricing.

Retail continues to be the dominant sector in the auction room (c.70% of the lots sold) but there is no shortage of demand for lots away from this sector. The largest lot sold in this auction was a vacant warehouse and office of c.92,000 sqft in Bognor Regis which sold prior for £4.3M whilst a tyre depot in Bedfont saw strong competition from seven bidders on the day and achieved £1.865M (4.8%).

A trend highlighted in our Q1 update which has continued into the second Quarter of the year is the number of tenants, including franchisees, particularly on the retail side that have been actively looking to acquire their freeholds and have been successful on numerous occasions. These tenants range from well-known Plcs through to independent retailers.

At the time of going to print our July auction catalogue is in the market and we wait to see what impact a turbulent few weeks at Westminster may have on market sentiment. It seems clear that following a Conservative Party leadership race we should have a new Prime Minister in place by early September. This should provide some stability in the political world and some clarity as to the likely direction of travel for policy which should provide private investors with guidance and confidence to continue to see commercial real estate as a safe haven for investment.

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LOT 24: BOGNOR REGIS

LOT 14: ISLINGTON


LOT 21: COLCHESTER

LOT 3: RAYNES PARK

Residential Auction Market

The second quarter of 2022 was not without its obvious challenges. Russia had recently invaded Ukraine, interest rates had begun to rise, inflation was gathering pace, building materials were in short supply and increasingly costly and the prime minister and his party were facing increasingly indefensible criticism. Despite all of this, the residential auction market demonstrated characteristic resilience as bidders' confidence in the sector remained stable.

The first residential auction of the second quarter was held on 12 May. On the day £40M was raised from the sale of 94 lots as a mix of investments, development opportunities and vacant homes sparked fierce competition. A total of 3,722 bids were placed with 958 individuals having registered to participate in the sale. At the time of writing, post sales have raised the total auction result to £43.5M with 81% of all lots offered now sold.

The highest price realised was for a freehold detached apartment building in Gravesend, Kent, containing 12 self-contained flats. With a total current rent reserved of more than £120,000 a year, it sold in excess of its guide price for £2.3M, a yield of 5.22%.

One of the most sought after lots of the day was a freehold former health centre in Leeds extending to 6,261sqft. A planning application had been submitted for the demolition of the existing building and erection of seven dwellings with associated landscape and parking. The property attracted 200 bids and sold for £351,000 from a guide price of £150,000.

The auction market was proving robust amid challenging economic circumstances. Sellers had identified the potential for significant returns from residential property. Those who priced assets realistically were rewarded by competitive bidding. Whilst interest was evident in lots across the country, London investments stood out in popularity. For example, a long leasehold self-contained flat with three bedrooms located in South Kensington ultimately sold for £2.2M after fierce bidding between 13 parties. It was offered subject to an assured shorthold tenancy producing £78,000 pa and was guided at £1.3M. The sale price reflects a gross yield of 3.54%.

The next sale of the quarter was held on 23 June and demonstrated an equally stable market. From all transactions to date it has generated a total of £57M – a success rate of 85%. Significantly, this sale raised £10M more than the equivalent sale of 2021.

London lots continued to draw bidders' interest. The most valuable lot to sell under the hammer was a freehold unbroken mid-terrace building arranged as 12 self-contained flats in Arundel Gardens, Notting Hill, London. It generated a rental income of £70,000 pa and was sold under the hammer for £4.9M – a gross yield of 1.4%.

A former register office in Grove Road, Walthamstow, London proved to be one of the most popular lots with over 160 bids received from 14 bidders. It sold for £2.4M – substantially in excess of its guide price of £1.6M.

Development opportunities continued to draw interest, subject to the correct pricing, despite the rise in the cost of building materials. A site with planning consent for seven family houses, situated in Ball Hill, Newbury, sold for £2.5M.

Ground rent investments remained popular, despite impending legislation to change enfranchisement pricing. Albany House, Judd Street, Bloomsbury, London was an attractive red brick mansion block arranged as 106 flats, each subject to a long lease. The landlord manages and insures the building. Total ground rents were £31,800 pa, doubling every 20 years, the next review being in 2031. It was knocked down for £985,000 – a gross yield of 4.89% or 20.45 years' purchase (YP).

Half way through the year, Allsop residential has raised £191M with 82% of lots offered sold. The next sale will be held on 4th August.

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MAY 2022, GRAVESEND


MAY 2022, SOUTH KENSINGTON


JUNE 2022, NOTTING HILL


JUNE 2022, BLOOMSBURY


JUNE 2022, WALTHAMSTOW

Residential Transactional and Living Markets

Investment

As anticipated in my Q1 update, the demand for all things residential has continued unabated across the sector and across the UK.

We have recently concluded sales on some larger portfolios, reversionary ground rents, regulated tenancies and AST's in locations as diverse as the Isle of White, Sittingbourne, Reigate, Manchester and Birmingham. Vendors remain varied as usual and these sales have been on behalf of a mixture of private vendors, property companies and Receivers. As always, accurate pricing is key and with the variety of opportunities that come across our desks, having the mother of all databases to hand has been crucial for us to flush out some of those more random buyers and undoubtedly give us an edge over the competition.

> The sales and acquisitions pipeline remains very healthy with some excellent assets in the market in Pimlico, Canada Water and Peterborough to name a few

I'm pleased to report that the carbon neutral houses in Sittingbourne, mentioned in the Q1 update, quickly sold to a fund with strong ESG credentials and the block in Southampton went to a private high net worth investor. The mixed commercial and residential block in Goodmayes also mentioned is currently under offer and in solicitors hands, so by the time you read this will have exchanged contracts.

Two recent acquisitions of particular interest were in the reversionary ground rent sector. Despite the uncertainty in this sector due to on-going governmental intervention, one investor in particular has taken a very positive stance and recently acquired circa £7M of stock through us in prime central London.

Portfolio sales have always been high on our agenda and remain as popular as ever. A widely publicized off market transaction of increasingly rare regulated tenancies on behalf of Addington Capital was snapped up by Mountview Estates for £10.6M and a geographically diverse portfolio of AST stock quickly went under offer for circa £20M.

In the north, the feedback from our colleagues in Leeds is that it remains a sellers' market with this trend expected to continue into Q3. Investors continue to chase income and there is a lack of good stock available. Recent bid deadlines on portfolios in Manchester and the North East have resulted in multiple offers where the gross yields sit between 6-8%.

Due to such unprecedented demand the team have decided to launch some new opportunities now in order to take full advantage of this sentiment over the traditionally quieter summer period, rather than wait until September when everyone returns to their desks from the holiday period.

The sales and acquisitions pipeline remains very healthy with some excellent assets in the market in Pimlico, Canada Water and Peterborough to name a few and there are some more portfolios due to surface in the near future.

Judging by the most recent buyer feedback, the sentiment for Q3 indicates an understandable note of caution thanks to high inflation and the threat of interest rate hikes. However, there remains a marked lack of supply in the residential markets and history tells us that in general terms over time, property tends to keep pace with inflation and sometimes even outstrips it. So for those investors sitting on cash the lure of residential investment will be overpowering.

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Residential Development

There has been a notable change in sentiment in the past quarter with a number of negative factors impacting on the decision making and the mindset of developers. The cost of living impact, the winding down of Help to Buy and the increase in inflation and build costs have all created uncertainty.

This is particularly evident in London where the planning system is still holding back development. All these factors combined are making development more challenging in viability terms. This has resulted in developers looking at alternatives to the typical residential market including student development, Build to Rent and we are continuing to see, on smaller sites where high density isn't achievable, the alternative of industrial and logistics development, albeit this market has cooled more recently.

However fundamentally there appears to be a significant shortage of stock and developers are therefore competing heavily for good unconditional development sites that could accommodate a mix of uses. The market for consented opportunities is challenging and the polarisation we have seen continues with accessible and best in class sites being well received and peripheral sites attracting little interest. For the good sites, with minimal room for build cost savings, competition is now forcing certain developers to trim their profit margins in order to acquire the right stock.

Market conditions feel comparable to 2010/11 when central London rather than outer London and the south east was the priority. With the absence of the housing associations as a motivated buyer and the majority of the housebuilders focussed on greenfield housing, there has been a noticeable slow down in outer London. Discussions around land values rebasing have been a hot topic for a long time and that feels like it is now starting to happen.

We continue to see strong demand for best in class development sites in regional city centres. The flip side of the increased costs of living and the potential slow down in the residential sales market will bolster the interest in the Build to Rent and residential investment markets. We expect to see continuing interest in development opportunities in city centre locations with Build to Rent exits. There are a wide breadth of residential investment funds and exits that are variations on affordable housing and Build to Rent that give developers a multiplicity of options.

The emergence of single family Build to Rent continues to be the most notable aspect of the residential development market in the regions. We have seen considerable interest and new entrants in this sector now that there are examples of stabilised investments and a greater breadth of strategic landowners entering the sector.

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> We continue to see strong demand for best in class development sites in regional city centres

Student Housing

The student accommodation sector continued to prove its resilience during Q2 2022. UCAS announced that more than 683,650 applications were received for 2022-23 and the application rate for UK 18 year olds hit a record high of 44.1%. HESA also reported that full time student numbers grew by 8% in 2020/21 providing a positive sentiment that demand for student accommodation continues to grow. In addition, a recent UCAS report highlighted that the UK continues to be a top destination for international students despite the impacts of the pandemic. International applications are set to rise by almost 50% within five years providing further confidence to investors and operators targeting international students.

Q2 is an important period for PBSA schemes to secure bookings for the following academic year and is the period when the market can start to take stock and analyse performance. Unite, for example, announced that 90% of their 74,000 student rooms have now been sold for 2022/23, slightly exceeding the pre-pandemic levels of 89% in 2019/20. At the same time, Unite are also confident of achieving rental growth of around 3-3.5% from last year.

Appetite for PBSA operational portfolios remains strong with several large-scale transactions completing during the past quarter. For example, Brookfield, the third largest PBSA provider with 23,000 beds, sold their Student Roost branded portfolio to GIC and Greystar for £3.3Bn which reflected £143,478 per bed. There was strong competition from Unite, Blackstone and GSA. This sale represents one of the largest deals in the PBSA sector since Blackstone purchased IQ in 2020.

Watkin Jones and Tide Construction also sold five PBSA schemes as part of Project Utah to EQT Exeter for £134M. This was EQT Exeter's first investment into the UK PBSA market demonstrating the continued attractiveness of the UK student market. The transaction comprised 2,063 beds in Bath, Nottingham, Swansea, Bristol and Glasgow and reflected £65,000 per bed.

Palamon Court in Canterbury recently exchanged for £110M representing the largest single regional PBSA asset to trade since 2017. Comprising 915 bedrooms, the deal reflects £120,000 per bed and a net initial yield of 5.3%. McClaren also successfully sold a further two PBSA assets in Southampton and Dundee for just over £18M reflecting 6.8% NIY.

On the development side, Godwin sold Bendigo Buildings in Nottingham to Bricks Group. With a GDV of £130m, the consented scheme comprises 783 beds across two sites offering both studios and cluster bed accommodation. It is understood that the land price reflected a unit value between £22,000 and £25,000 per bed. Furthermore, Watkin Jones purchased the Metalworks site in Bristol with planning consent for 819 beds. We understand this has been pre-let to the University of Bristol on a 15-year nomination agreement. The purchase price of £20.1M reflected £24,542 per bed. These sales demonstrate the strong demand for sites despite the increase in inflation and the cost of materials.

There is further pressure on private developers after the government approved National Code was changed to allow students who suffer disruption from delayed PBSA schemes to be provided with automatic compensation. Lower room rates for students with disabilities and better support for students with mental health are expected to also follow.

The HMO market has also experienced a positive quarter with the vast majority of HMO operators now fully forward let for 2022-23. HMO landlords continue to benefit from increasing student demand with many experiencing rental growth. Combined with a limited new supply, the HMO market is increasingly competitive. In some cities, we are experiencing HMO bed space values equalling and moving beyond PBSA bed space values, reaching £90,000+ per bed.

Despite the positive quarter, The Bank of England are now predicting that inflation will increase to above 11% in October when energy costs also rise. For many investors, the cost of making acquisitions and stabilising assets has increased significantly. Debt is more expensive than it was only a short time ago and some investors are absorbing the cost of hedging their facilities from the outset, adding upfront costs. Longer term costs are harder to forecast due to turbulence in the energy market, therefore affecting stabilised returns. We are yet to see these factors have an impact on the market, but it is possible we will see some softening through the next quarter - something to keep an eye on.

Nevertheless, what sets student accommodation apart from other real estate sectors is the visibility of future cashflow. Marketing and renewals start as early as one academic year ahead and this is supported by parental guarantees. Student accommodation also benefits from upfront payments from international students and flexibility in adjusting rental rates annually.

In terms of the general outlook, the depth of investor demand for PBSA and HMO portfolios, the strong fundamentals and the lack of operational stock is overall likely to sustain yields and repel the many negative macro-economic factors we are currently experiencing.

Appetite for PBSA operational portfolios remains strong with several large-scale transactions completing during the past quarter

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The Build to Rent Market

Investment in Q1 climbed 50% YOY with £1.7Bn deployed and Q2 has seen significant activity with several transactions concluding. This has been in the face of the challenge of rising construction costs making the delivery of BTR schemes more challenging. The regions remain particularly attractive, aided by operating assets in those areas showing strong occupational and rental levels, whilst London and the south east have recovered strongly after Covid related impacts, as occupation and rental levels now returning to pre-pandemic levels.

Demand is driven by a strong desire from residents, generally 23 – 35 year olds, to live in good quality rental accommodation, in central locations, with cohesive communities where residents can feel secure with longer term tenancies. The success of BTR schemes which have opened over the past six to 12 months is proven by the vast majority of schemes in main centres such as Bristol, Birmingham, Manchester and Leeds being over 90% let.

The British Property Federation's (BPF) latest figures show a total number of units either complete, under construction or with planning standing at 225,352. Numbers in the regions continue to grow at a faster rate than London, accounting for approximately 131,096 with 94,256 in the capital.

The BTR single-family housing (SFH) market has remained extremely dynamic, activity of note includes:

- Allsop launched a portfolio of 1,200 homes across 10 sites to the forward funding investment market on behalf of Harworth Group
- TPG Real Estate Partners and Gatehouse Bank launched their £500M BTR platform, Start Living, targeting an initial 2,500-homes. Subsequently Start Living is partnering with Countryside to develop 150-homes in the Midlands
- Nuveen agreed to back Apache Capital's platform 'Present Made' and will aim to secure a 3,000-home pipeline

Activity of note within the BTR multi-family market this quarter includes:

- Heimstaden Bostad AB agreed to acquire Platform's 464-home scheme in Edinburgh for £124.4M
- US investor Cortland Group agreed to forward fund the £138M BTR element of Marrico and Helios mixed-use development in Leeds which comprises 629-apartments
- The John Lewis Partnership identified their first three sites in Bromley, West Ealing and Reading, to start its BTR venture
- Citra Living purchased 110-apartments in Ashford developed by GRE Assets
- Grainger have agreed to forward fund Phase.II of Redcliff Quarter in Bristol for £128M comprising 374-units

Funding yields remain strong for well-designed multi-family BTR stock in prime, practical locations. This is helping to reduce the impact of increasing delivery costs, a result of in part, labour and material shortages and rising utility costs. In London and strong south east locations, NIYs range from 3.25% to 4.00%, with major regional centres at 3.75% to 4.50%. Secondary locations are in the region of 4.50% to 5.00% NIY. For pipeline opportunities of scale, NIY's for single family BTR across large parts of the country are now dropping below the 4.00% mark. Competition is fierce for limited opportunities.

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Investment in Q1 climbed 50% YOY with £1.7Bn deployed and Q2 has seen significant activity with several transactions concluding

Residential Letting and Management

Turmoil in the UK's political landscape has dominated headlines in recent days with the business of government effectively on hold until an new Conservative leader and prime minister is announced on the 5th September. This lack of stability is having a real impact on millions of people who are already facing huge financial pressures, as a plan to address the need for affordable housing is unlikely to be imminent until a committed minister is in post.

Legislation updates

In addition to recent political and world events, numerous pieces of legislation have come into force in the sector in recent months and more are on the way:

1. On the 28th June, the Building Safety Act 2022 became law. It provides leaseholders with legal protection from unfair bills by putting the responsibility of historical safety defects onto the freeholder.
2. The Government have also signed contracts for a new Professional Insurance Indemnity Scheme that will help assessors conduct ESW1 assessments to identify whether buildings have fire safety risks.
3. A Fairer Private Rented Sector (PRS) White Paper has also been published. It includes a ban on Section 21 evictions, the right for a tenant to request a pet in their house, a cease on arbitrary rent clauses, outlawing bans on renting to families with children or those in receipt of benefits and the creation of a Private Renters' Ombudsman to enable disputes between landlords and renters to be settled quickly without going to court. It is set to be introduced in the next 12 months.
4. Despite the sector going through significant changes, the recommendations in the final report on the regulation of property agents (RoPA) are still being considered, therefore a delay in driving up the standards for sales, letting and managing agents could hamper the effect of new regulations, especially the new building and fire safety requirements, expected to come into force next year.

Demand

Demand in the PRS remains very high with an average of 113 new applicants registered per branch in May according to Propertymark. This is an increase since February when 78 new applicants was the average. The cost of renting has continued to rise throughout the second quarter of the year, with 75% of agents reporting a month-on-month increase in April. This compares to a pre-pandemic figure of just 31% on average. These recent statistics from Propertymark highlight how the PRS needs more properties to meet the tremendous demand from tenants, as it is resulting in offers over the asking price, which in turn is creating an increasingly competitive market.

> Demand in the PRS remains very high with an average of 113 new applicants registered per branch in May according to Propertymark

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It is advisable that ratepayers review the current Rateable Values on their properties to highlight any situations where the figure has been over assessed and an appeal should be submitted before the deadline

Business Rates

The main focus of discussion relating to Business Rates has moved onto anticipating the impact of the forthcoming 2023 Rating Revaluation. This will place revised Rateable Values on all 2.1M properties liable for business rates. The draft 2023 Rateable Values are to be published no later than 31st December 2022.

The impact of the 2023 Revaluation on Rates Bills will depend on the following:

- 2023 Rateable Value – the new Rateable Values will be based on rental levels prevailing on 1st April 2021. With the current Rateable Values being based on rental levels prevailing over seven years ago, there are likely to be big swings in liability change following the 2023 Revaluation. The biggest changes are likely to be seen in the retail sector, where significant reductions in liability are anticipated, while other properties in parts of the logistics and industrial sector are expected to see substantial increases.

- 2023/24 Uniform Business Rate (UBR) – At a revaluation the UBR is reset in order to bring in the same tax income in real terms to the Government. For example if the total Rateable Value of the county following the revaluation was reduced by 10% then the UBR would increase by 10% to bring in the same income. Some early surveys undertaken have predicted a small fall in the total Rateable Value which will lead to a small increase in the UBR. This figure however will then be further increased by the prevailing level of CPI inflation in September 2022. With the current high level of inflation this could on its own lead to a 10% increase in the UBR. It is anticipated that the Government will announce the likely 2023/24 UBR sometime in the autumn.

- Rates Phasing – Following a new revaluation the rates liability on some properties can increase substantially. The Government are required by law however to introduce a rate phasing scheme in order to provide some protection to those businesses facing large overnight increases. The cost of this scheme however is financed by also placing caps on the level of reductions ratepayers can receive. One option the Government are considering is whether to permit those ratepayers seeing a significant reduction in their rates bills to receive the reduction immediately rather than it being phased in over a number of years.

Online Sales Tax

The Government are currently considering the responses received to their consultation relating to the potential introduction of an online sales tax. The Government have advised that if this tax is introduced then the money raised will be used to reduce the rates payable in the retail sector.

Deadline for Appeals

In conjunction with the introduction of the 2023 Rating Revaluation on 1st April 2023 the Government are introducing a deadline for appeals against the current Rateable Values of 31st March 2023. There are certain situations where a later deadline may apply. It is advisable that ratepayers review the current Rateable Values on their properties to highlight any situations where the figure has been over assessed and an appeal should be submitted before the deadline.

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