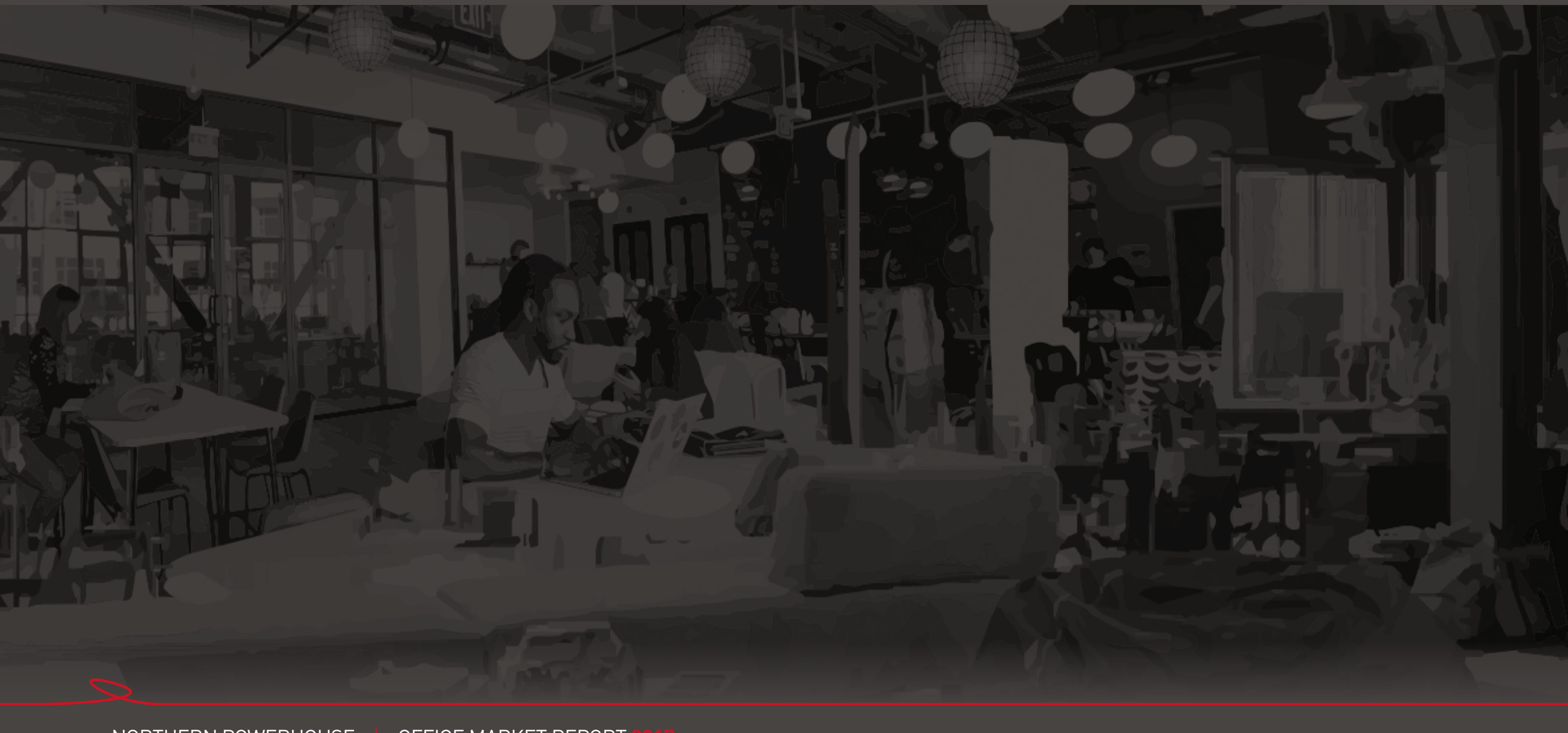
OFFICE MARKET REPORT 2017

NORTHERN POWERHOUSE



Lambert Smith Hampton

WELCOME

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Resilience is a term all too often bandied around by those in the commercial property industry. Yet, I can think of no other word more befitting than this to describe the north of England's response to the ongoing political and economical turbulence.

It has been little more than three years since the then Chancellor, George Osborne first coined the term 'Northern Powerhouse' and, in that time, we've witnessed an enormous amount of change. First, the UK's shock decision to leave the European Union, then a change in leader followed by a snap General Election and subsequent hung parliament, the election of Metro Mayors in Liverpool, Manchester and Teesside, a U-turn on plans to electrify the key transpennine route between Leeds and Manchester and, most recently, a £400m government funding boost for transport infrastructure improvements.

Despite all of this, the message from the North is abundantly clear; our economy is thriving. Our occupier and investment markets have performed admirably against an extremely challenging backdrop. Major announcements such as the Government Property Unit's decision to take 378,000 sq ft at Wellington Place in Leeds, supercar maker McLaren's 20-year deal to be based at Rotherham's Advanced Manufacturing Park and the appointment of Henry Boot as development partner at the North East's International Advanced Manufacturing Park – are strong indicators to the rest of the world that we are open for business.

The Northern Powerhouse may have been borne out of a Government initiative but I am a firm believer that its success rests at the feet of those who seek to benefit most – those located in the North. The failure of the Leeds, Sheffield and Newcastle city regions to agree on devolution deals undermines our ability to leverage the full weight of the North in Parliament and risks a continuation of the fragmented 'cap in hand' approach of years gone by. Political leaders must unite in order to rectify the decades of under-investment so that we can truly exploit the region's significant untapped potential.

In the meantime, we will continue in our role as ambassadors of the North to provide insight to those looking for opportunities in the region – be it from an occupational or investment perspective – so that they are able to make informed, intelligent and accurate property decisions.

If you would like any guidance or further information in respect of any of the Northern Powerhouse's office markets, please contact our team of experts – we'd be delighted to help.

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TAPPING INTO THE NORTH'S THRIVING SME SECTOR

by Adam Varley

Platform, Leeds (courtesy of Bruntwood)

Historically overshadowed by the activities of larger corporates and multinationals, small and medium-sized enterprises (SMEs) are now being recognised for their significant contribution to the growth of the UK economy. But, what are the reasons behind this evolution and are we creating the right physical environment in order for them to thrive?

THE IMPACT OF TECHNOLOGY

Technology, more specifically the internet, is changing the way businesses operate. The advantage of being bigger in order to be more efficient and profitable is rapidly being eroded.

Instead, technological advancements such as Cloud Computing have reduced overheads and lowered barriers to entry, spurring entrepreneurialism and leading an explosion of start-up's. Automated business processes have also enabled larger organisations to become more streamlined, improving productivity while simultaneously reducing headcount

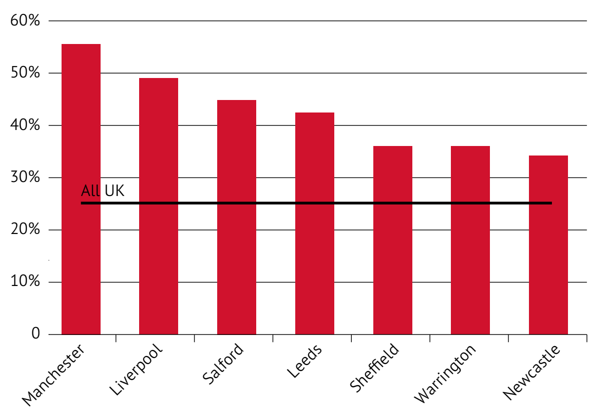
With the number of businesses employing less than 50 individuals having risen by 25% since 2012, SMEs have become an integral part of the UK economy. This is a trend which shows no signs of slowing, as new technologies such as Artificial Intelligence, Big Data and the Internet of Things become increasingly commonplace in the modern business environment.

THE NORTHERN POWERHOUSE EFFECT

The North of England – where office market activity has historically been underpinned by back office moves from blue chip organisations owing to its comparatively lower operational costs – has one of the highest concentrations of SMEs of any UK region; over 1m in fact, with a combined annual revenue of £214.9bn in 2016.

Fuelled by a clear commitment from the Government to supporting the organic growth of local businesses, including strong financial support in the form of the Northern Powerhouse Investment Fund, cities such as Manchester, Liverpool and Salford have become thriving hot-beds of SME activity.

Northern Powerhouse cities, growth in SMEs (2012 to 2017)



Source: UK Business Counts, ONS

With consistently above average take-up for smaller units, this trend has been clearly reflected in the occupier markets over the past few years. Furthermore, over the 12 months to Q3 2017, the eight key markets of the Northern powerhouse have seen well over 1,000 deals of below 5,000 sq ft, making up 82% of transactions.

EVOLVING WORKSPACE REQUIREMENTS

Historically, the majority of new supply that has come through the development pipeline has been aimed at larger corporates, ideally sole occupancy with large floorplates. The challenge for landlords is to react to the evolving workspace requirements brought about by this change in business structure in order to capitalise on the growing level of demand.

To a certain extent, this has already begun. Long lease structures traditionally favoured by institutions are becoming less common, with the average lease length now between three and five years. The historic cynicism surrounding covenant strength is also lessening.

Fuelled by the rise in popularity of CoWorking spaces from the likes of Work:Life and WeWork, the somewhat dated business model of the serviced office market is also undergoing a massive shake-up.

SPACE TO GROW

While serviced office and CoWorking space typically caters for between one and 10 employees, what of the 43,465 businesses across the North of England that employ between 10 and 50 members of staff?

Some forward-thinking landlords have begun to realise that they can maximise the use of second-hand space by targeting this growing cross-section of businesses.

This new concept of flexible workspace is typically provided in shell specification together with capped services and all inclusive rent and service charge deals, enabling tenants to occupy the space with maximum ease and minimal risk.

Bruntwood's Platform in Leeds is one such example. With a variety of evolved workspaces that can accommodate a mix of small, creative businesses, start-ups and SMEs, along with bigger, larger corporates, the 120,000 sq ft, 13-storey grade A office building provides the flexibility to grow within the building throughout the lifecycle of the business.

Elsewhere across the North, landlords are also responding to difficulties in attracting larger occupiers by repositioning existing buildings. Q11 Quorum Business Park in Newcastle was recently sub-divided into smaller suites and is now almost fully let, with Q10 due to be carved up to accommodate smaller grade A requirements following its success.

Urban Splash's iconic Grade II Listed Park Hill scheme in Sheffield has also seen unprecedented levels of demand, with just 4,425 sq ft remaining from of a total of 30,000 sq ft. As such, enquiries are now being taken for Phase 2, which includes proposals for circa 27,000 sq ft of commercial space.

SUPPORTING A THRIVING ECONOMY

While businesses of a certain size will always require larger floorplates, SMEs are a critical component of the future success and vibrancy of the Northern Powerhouse economy and are likely to have a transformative effect on the UK's commercial property market in the years ahead.

Landlords therefore have a vital role to play in nurturing our thriving SME sector by providing high-quality, flexible office space which is capable of responding to the ever-changing needs of modern businesses.

A RICH AND DIVERSE ECONOMY

In its Independent Economic Review published in June 2016, Transport for the North identified a core group of strategic industry 'capabilities' where the North of England has the greatest global competitive advantage. Ranging from financial services to digital and education, the diversity of expertise and unique strengths of each city are clear to see.

PROFESSIONAL SERVICES

Manchester is the undisputed capital of professional services in the Northern Powerhouse, with employment in the sector standing 65% above the UK average. Leeds, well known for its legal services cluster, follows behind with employment 45% above the UK position. While Sheffield's employment in professional services is in line with the UK position, it has recorded the fastest employment growth of the key locations in the region, expanding by 26% over the past five years.

FINANCE AND INSURANCE

While London is a recognised global hub for financial services, Leeds and Manchester are among two of the UK's leading regional locations outside the capital, with employment at well over 50% above the UK average. That said, of the six key industries outlined here, this is arguably under the most pressure, having been deeply impacted by the global financial crisis and subsequently affected by increasing automation. While employment has been steady in Leeds, Manchester's financial services workforce has contracted by 18% over the past five years.

TMT

The rapid growth of the TMT sector is arguably one of the region's biggest success stories over the past decade. The BBC's major relocation to Salford Quays in 2014 has proved a catalyst, with Salford's TMT employment standing at 76% above the UK average. Leeds and Manchester now boast among the highest concentrations of TMT employment outside London, collectively home to 60,000 TMT jobs, while Newcastle's TMT employment base has expanded by 26% over the past five years.

SCIENCE AND ENGINEERING

Warrington's reputation for science and engineering is clearly reflected in its labour force, with employment in the sector standing 37% above average. The town has long been regarded as the UK's capital of the nuclear industry, boasting globally renowned expertise in this field. While Sheffield's employment in this area stands some way below average, the wider South Yorkshire region is gaining a growing reputation, being home to the Advanced Manufacturing Park and an array of high tech manufacturers.

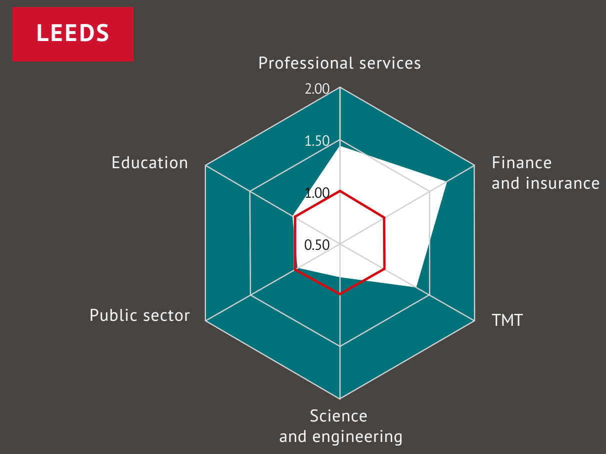
PUBLIC SECTOR

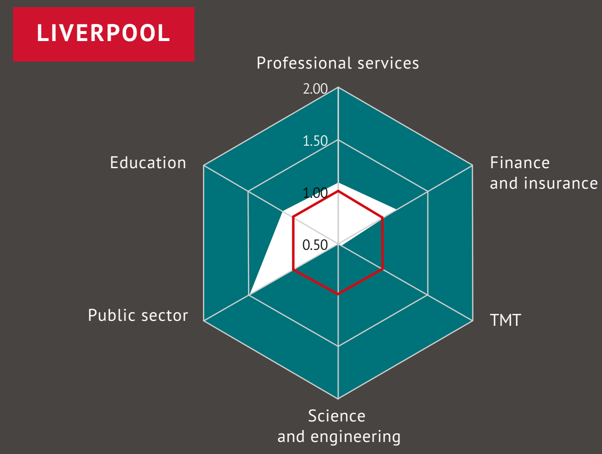
Across the UK, the public sector has been put under intense pressure as part of the government's austerity drive. Historically characterised by a relatively large public sector presence, this has been reflected in the Northern Powerhouse with employment falling by circa 10% in Liverpool and Sheffield over the past five years. However, the consolidation of central government functions has provided a massive boost to the occupier markets of Liverpool and Leeds, driving circa 500,000 sq ft of grade A take-up in 2017 alone.

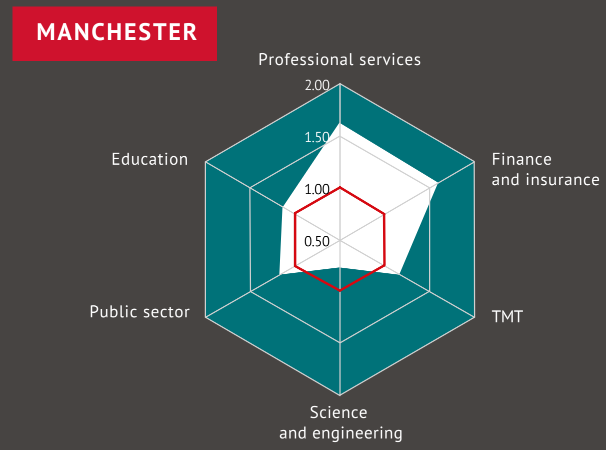
EDUCATION

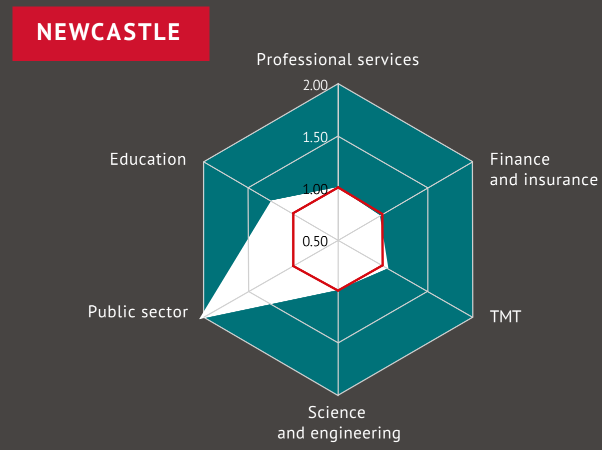
The Northern Powerhouse is home to six of the UK's 24 leading-edge Universities, underlining the academic prowess across the region. While the majority of the key locations displayed overleaf boast education employment above the national average, Sheffield stands proud with a location quotient 57% above the national average. However, for the region as whole, Lancaster has the highest concentration of all, standing at double the national average.

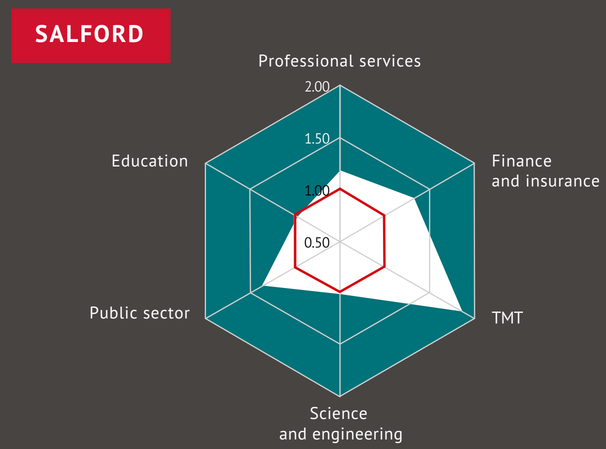
Employment location quotients

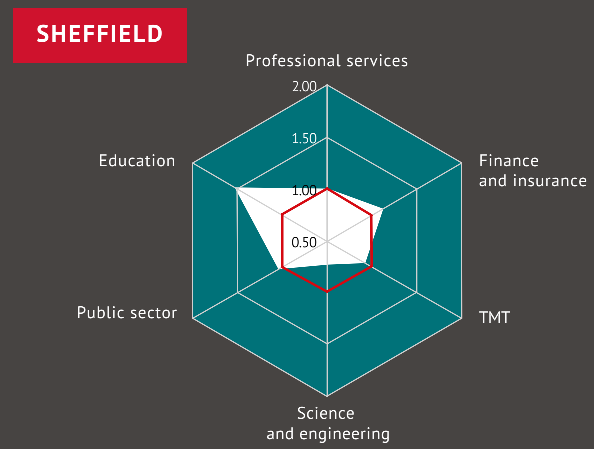


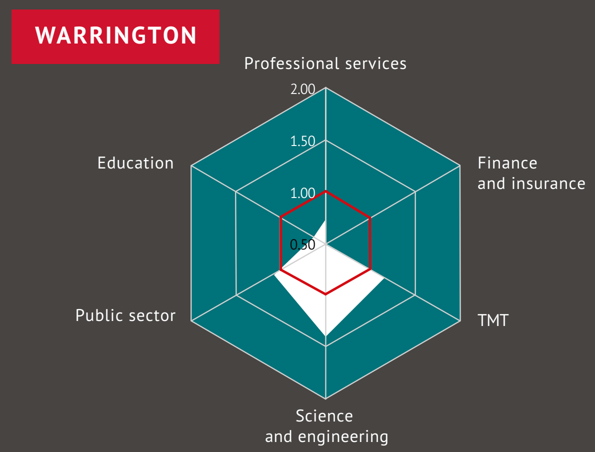












LOCATION QUOTIENT

Location quotient (LQ) is a ratio which helps to quantify how concentrated particular sectors are in local areas compared to the nation as a whole. A figure of 1.0 implies that the location is exactly in line with the national average.

National average Location employment quotient

Source: EMSI, LSH Research

DISRUPTIVE WORKPLACES FOR THE DISCERNING OCCUPIER

by Matthew Pickersgill

As the North of England cements its reputation as a breeding ground for exciting new tech businesses, it is attracting an increasingly discerning business community. Landlords must now look beyond the delivery of the standard office building in order to attract the modern day occupier.

Given the average person is awake for 16 hours a day and will spend the majority of this commuting and working, it is vitally important that the place of work is inspiring and enjoyable. With this in mind, employers are beginning to choose locations and buildings that increase productivity, offer interesting amenity, incorporate activities and, in turn, increase staff wellbeing and retention.

From a 'corporate' property perspective, this is simple to respond to. Understanding the demographic of the target audience is crucial, as well as what features can be incorporated that allow it to stand out. Office buildings are becoming so much more than just space – it's now what the building has to offer, from both its management and the micro-environment.

While very important, the idea of differentiation cannot simply be the internal and external aesthetics of a property – it is a building's identity and brand that will resonate with potential occupiers. There needs to be a confidence from occupiers that the building they work in can represent their company, in order to help attract and retain talent. This comes from how it operates with a customer-focused approach in mind and how it can add value to its occupiers in a way that makes them feel important.

A year on since our article on 'The Rise of CoWorking', the evolution has not slowed in pace, we've seen serviced office space in the region's two core cities of Leeds and Manchester account for over 10% of take-up in the period Q1-Q3 2017; amazing progress given that this sector only accounted for 5% of space leased from 2012-2016. This offers amenity with occupiers being able to use the shared collaboration space which often includes additional coffee shops and cafés.

We've also witnessed the reception area evolve over recent years. No longer are we seeing simple communal space used to sign in and/or walk through on the way to the office. This is now a space which can be enjoyed by both occupiers and clients alike, with added extras such as break-out spaces, business lounges and refreshment stations to name but a few.

The introduction of a concierge service, as opposed to simply having a front of house, brings with it an endless list of benefits. These can include event planning which will give the building a sense of community, as well as arranging anything from booking taxis and dry cleaning, to hiring building-branded bicycles. Umbrellas, irons, towels and hair dryers are also being installed as part of the shower and locker facilities.

An increasingly popular way of differentiating a building is to create a communal roof terrace which can be utilised in a number of ways, for example as collaborative working space that can double up as an event space complete with a café/bar. The roof terrace can also incorporate roof gardens for occupiers to enjoy and contribute to, instilling a sense of wellbeing.

Demand for the corporate style office building is noticeably waning, with the non-traditional offering increasingly at the forefront of occupiers' minds, both aesthetically and operationally.

It's not simply the most modern specification that wins out, it now extends more deeply, with occupiers wanting a customer-focused community that's rich in amenity.

Landlords need to understand their building is going to be an extension of what a company represents and the quicker they create occupier-focused products, the quicker they will reap the rewards.

CASE STUDY: WINDMILL GREEN, MANCHESTER

FORE Partnership's Windmill Green in Manchester is currently undergoing a comprehensive remodelling project and is a prime example of how incorporating some of the aforementioned elements creates a sustainable office property with its own identity. LSH purchased the building prior to the redevelopment, after being appointed as agents, and gave significant input in the design process. The property is already seeing businesses keen to buy into its community feel with a pre-let to the stylish CoWorking operator 'Our Space' over the part ground and first floors and brings with it an additional coffee shop offering.

The property keenly encourages cycling to work with its on-site cycle storage and state-of-the-art shower facilities. An on-site 'bike-centre' is also available for when puncture repairs are needed.

There is a communal roof terrace with bar, break-out space with bespoke furniture, roof gardens and an apiary for Manchester's bee colonies. A curator service, as opposed to just a standard 'front of house' set-up, will also be in part of the building's day-to-day operations.

DELIVERING A LONG-TERM TRANSPORT STRATEGY

by Richard Corby

Transport infrastructure is a critical catalyst to economic growth. Aside from improving accessibility, infrastructure development will create countless trade, investment and employment opportunities that could transform the North of England beyond recognition. Getting the strategy right is therefore central to achieving the Northern Powerhouse vision.

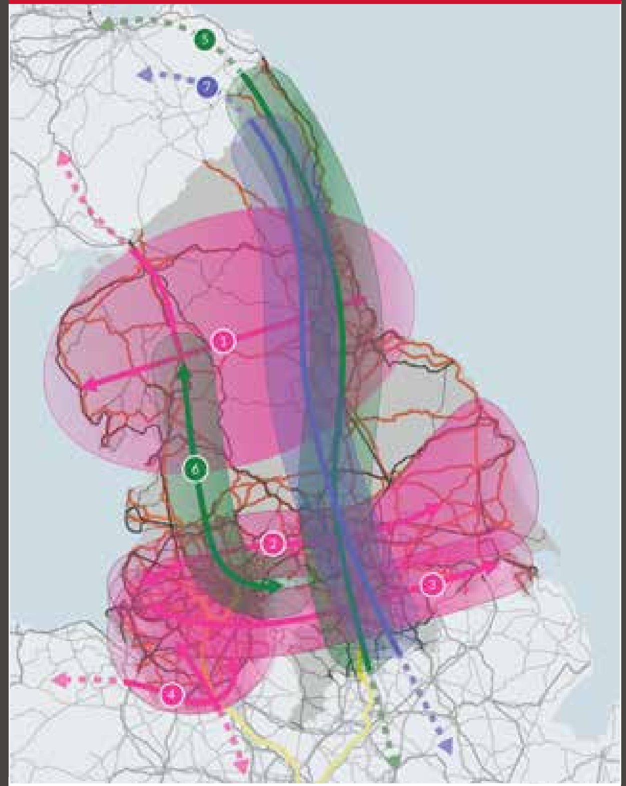
A COHESIVE VISION

Ask anyone from the North what they believe to be the single biggest factor inhibiting the region's economic growth prospects and the resounding response will be 'transport'. Specifically, issues surrounding connectivity, efficiency, reliability and congestion brought about by the absence of a cohesive vision and chronic under-funding.

Enter Transport for the North (TfN). Established in 2015 and empowered by a pan-northern partnership of civic and business leaders from across the region, TfN has been tasked with developing a Strategic Transport Plan (STP) and accompanying long-term Investment Programme for the North that will inform how HM Government, Network Rail, Highways England and High Speed Two (HS2) Ltd can work with partners in the North to deliver investment that will address these long-standing issues in an attempt to transform the economy.

Supported by an Initial Integrated Rail Report and Initial Major Roads Report, the STP will focus around nine Strategic Development Corridors, which include Northern Powerhouse Rail, Integrated and Smart Travel, and seven geographic connectivity priorities that reflect the economic links across the North.

TfN Strategic Development Corridors



1. Connecting the Energy Coasts
2. Central Pennines
3. Southern Pennines
4. West and Wales
5. East Coast Corridor to Scotland
6. West Coast to Sheffield City Region
7. Yorkshire to Scotland

Source: TfN

DEVOLUTION OF STATUTORY POWERS

A significant step towards achieving this goal will take place in late 2017, when TfN will be established as a Sub-National Transport Body – the first outside Greater London – providing it with the legal basis to ensure its plans are fully taken into account in current decision making and, more importantly, beyond the lifespan of a single government. This is a status currently only afforded to Transport for London (TfL).

The success of devolved bodies, such as TfL – which operates public transport in the capital and has direct control over services and spending – demonstrates the scale of the opportunities created in respect of infrastructure investment and its direct impact on economic growth.

However, in contrast, TfN's role will be largely advisory – a decision which has caused concern among some senior Northern Powerhouse supporters, despite TfN's powers remaining broadly in line with those which were envisioned when the organisation was formed.

CRISIS OF CONFIDENCE

Transport Secretary Chris Grayling's summer announcement that the TransPennine railway between Leeds and Manchester – one of the busiest in the country – was unlikely to be fully electrified, and that he was reviewing a plan to build two platforms at Manchester Piccadilly station to cope with extra trains, sparked a crisis of confidence over the Government's commitment to delivering the Northern Powerhouse vision.

However, this was quickly quelled by Chancellor Philip Hammond's pledge of £300m to 'future-proof' the railway network in the North, 'ensuring HS2 infrastructure can link up with future Northern Powerhouse and Midlands Rail projects while keeping open all options for services through Manchester Piccadilly'.

FUTURE PROSPECTS

Political conflicts aside, a number of Northern combined and local authorities have already begun to develop their spatial plans with consideration strategies in anticipation of the forthcoming STP – a key driver of business confidence and development activity across the region's office markets going forward.

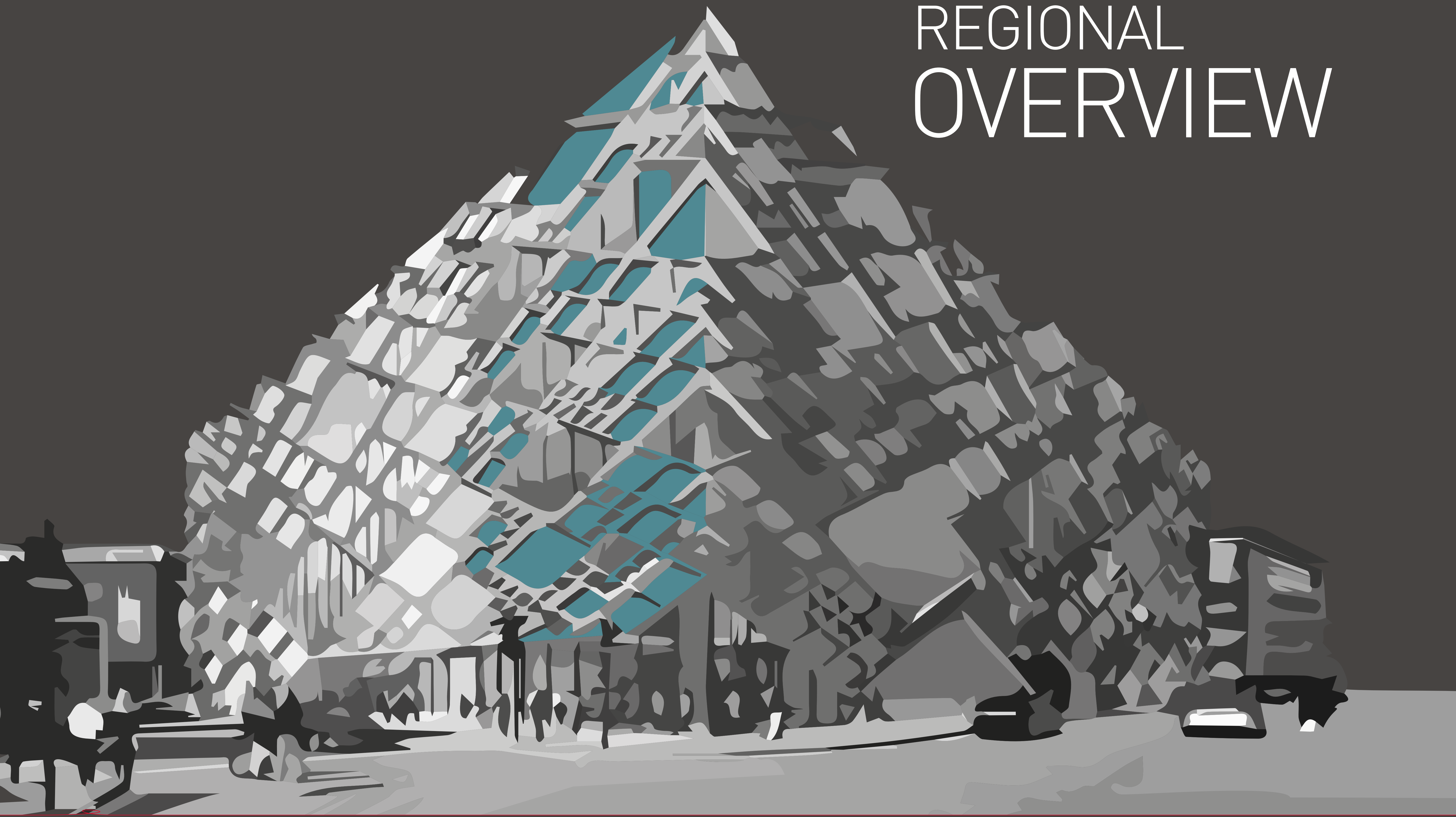
It is hoped that the 2017 Autumn Budget Statement will iron out any latent issues surrounding infrastructure investment across the Northern Powerhouse so that when the STP is published for public consultation in early 2018, it will provide a greater level of certainty and commitment which businesses need in order to thrive which, in turn, will lead to the creation of a stronger, more diverse and resilient Northern economy.

Commenting on TfN's role and anticipated delivery of the Strategic Transport Plan, Jonathan Spruce – Interim Strategy Director at TfN, said:

"TfN has a clear remit – to support a more productive and integrated Northern economy. Research and analysis collated by TfN indicates that investment in the region's transport infrastructure could help create close to a million new jobs and add almost £100 billion to the UK's economy by 2050.

"The draft STP will be published for public consultation in early 2018, and will outline the North's priorities for investment at a regional level over the next 30 years.

"Working collaboratively with our Northern partners and business across the North is crucial if we are to produce a plan that is fit for purpose and will deliver the potential economic benefits that underpin TfN."



REGIONAL OVERVIEW

OCCUPIER MARKET OVERVIEW

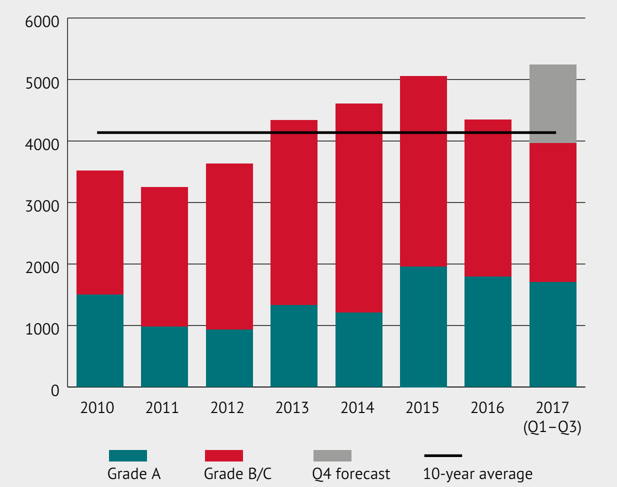
POWERING TOWARDS A RECORD YEAR

- 2017 is on track to be a record year for office take-up across the Northern Powerhouse. For the eight markets combined, Q4's forecasted take-up will take the annual total to 5.2m sq ft, narrowly surpassing 2015's high of 5.1m sq ft and 26% above the ten-year average.
- Admittedly, the year would have been quite different had it not been for two major government commitments which took place in Q3. HMRC was responsible for 2017's two largest deals; comprising a 378,000 sq ft pre-let at Wellington Place (including NHS Digital), Leeds and a 270,000 sq ft commitment at India Buildings, Liverpool. These two deals alone made up 16% of the total take-up in 2017 to date.
- Nonetheless, even if these deals are overlooked, take-up is still running above its trend level, a clear testament to the resilience of market demand in the face of heightened economic uncertainty. But, above all, there is an encouraging depth to market activity. The first three quarters of 2017 witnessed just under 1,000 deals across the eight key markets, up 13% on the same period of 2016.

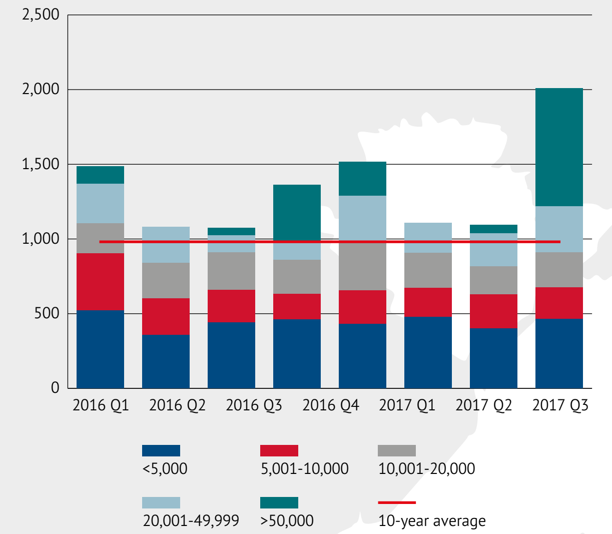
MAJORITY OF MARKETS BOAST ROBUST LEVELS OF DEMAND

- Understandably, the two HMRC deals have provided a massive boost to take-up in their respective markets. A record year for Leeds is now virtually assured, with take-up in 2017 set to break the 1m sq ft mark in the city centre for the first time ever, while Liverpool is set to record its best year since 2005.
- Even without an HMRC deal to their name, the majority of markets in the region are also set to have a strong, if not vintage year. Manchester city centre, which has enjoyed a four-year run of strong take-up, could also register a record year in 2017, albeit this depends on one or two large deals landing before the year end. With several notable deals set to transact in the latter stages of 2017, Sheffield is also on course for a good year, a market benefitting from particularly strong growth and expansion within the TMT sector.
- Newcastle is the only market set to disappoint. Recording only three deals over 10,000 sq ft, take-up in Newcastle city centre for 2017 as a whole is expected to fall circa 15% short of the 10-year annual average. However, despite the lack of large deals to drive take-up, the city has seen healthy activity seen among SMEs.

Annual take-up by grade (000 sq ft)

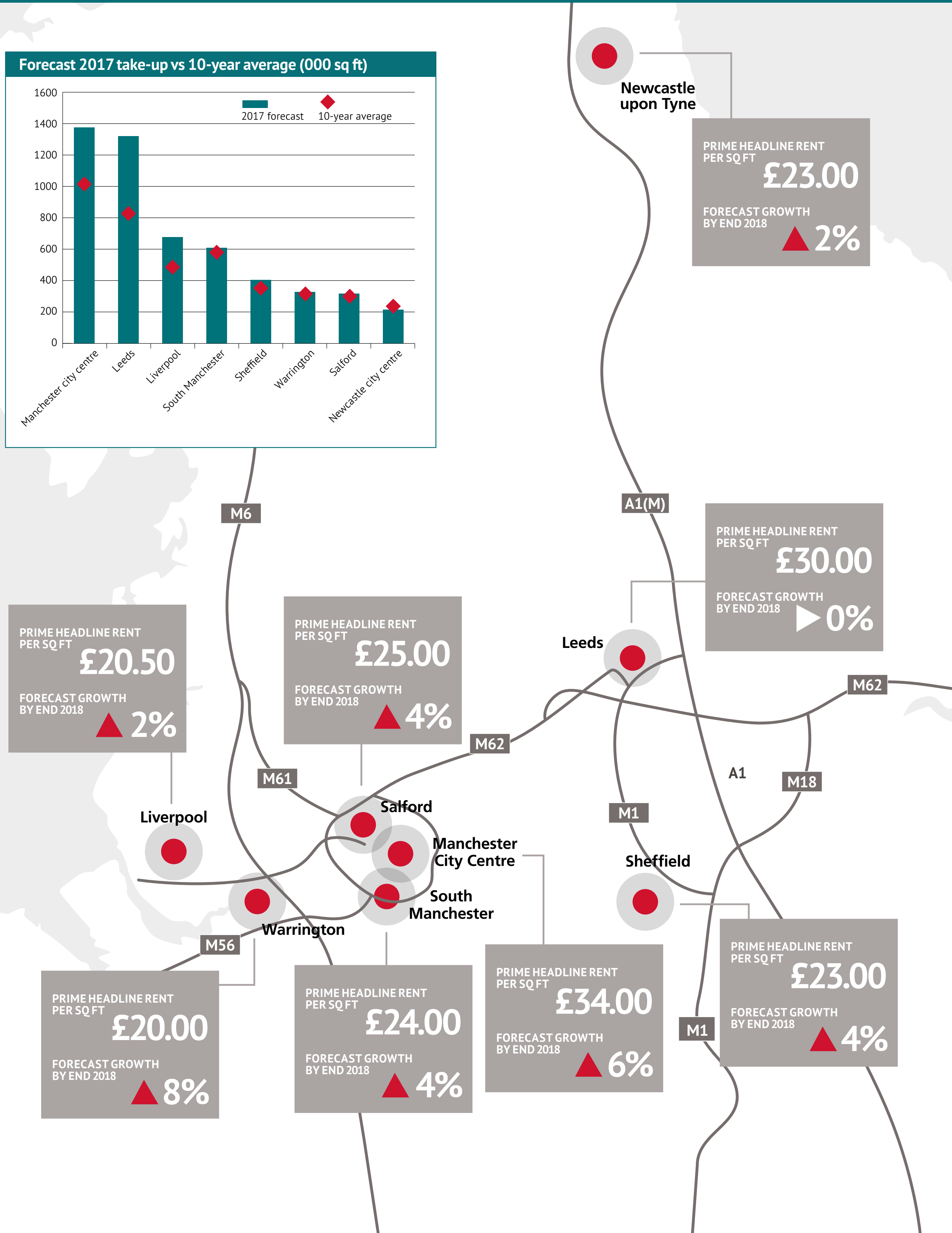


Quarterly take-up by size (000 sq ft)



Source: LSH Research

Forecast 2017 take-up vs 10-year average (000 sq ft)



OCCUPIER MARKET OVERVIEW

CONTINUED

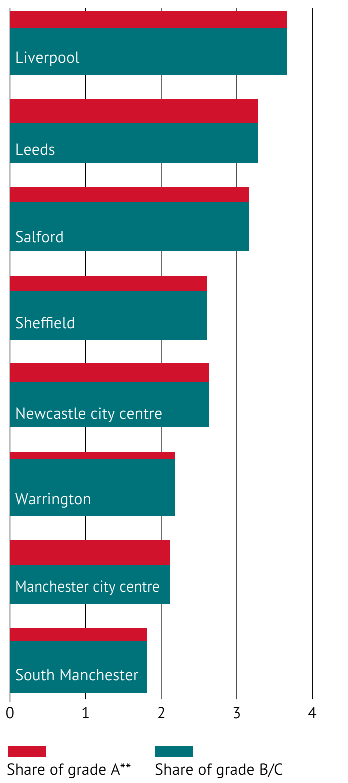
SUPPLY TIGHTENS FURTHER STILL

- Supply continues to ebb away across the region's key markets. Reflecting ongoing robust demand and a relatively measured response from developers in this cycle, total availability has contracted by 12% since the start of 2017 and now stands 31% below its 2012 peak. Of the eight markets, Warrington is the only location to have seen an increase in supply during 2017.
- Several locations, such as Manchester city centre, South Manchester, Newcastle city centre and Sheffield, now possess supply at record or near-record lows. Placed into context with average rates of take-up, South Manchester is the tightest of all the markets, with supply equivalent to only 1.8 years of average annual take-up, followed by Manchester city centre, with 2.1 years of supply available.
- The fall in supply of high quality space has been even starker,with grade A space contracting by 25% across the eight markets combined during 2017 to date. Moreover, with development this cycle overwhelmingly focused in Manchester and Leeds city centres, grade A supply accounts for a relatively small share of availability in the majority of the region's markets

SUSTAINED UPWARD PRESSURE ON RENTAL LEVELS

- Upward movements in prime headline rents have been limited during 2017 to date. Only Salford Quays and Leeds have recorded an increase in 2017, although in Leeds' case, the growth from £27.00 per sq ft to £30.00 per sq ft was an exceptional upward step by historic standards. Nonetheless, a number of markets are on the cusp of a rise, with prime headline rents expected to increase in Manchester, Sheffield, Newcastle and Warrington over the coming months.
- The real story, however, surrounds rental growth seen for quality refurbishments. The contraction in supply has prompted a steep increase in rental levels for existing space in some markets, particularly in Manchester, Leeds, Sheffield and Newcastle. This growth is testament to the sustained level of demand in the markets, particularly for SMEs.
- Encouragingly, evidence of rental growth for this sort of product should attract more landlords and developers into redevelopment. With supply tight, the opportunity to engage in asset management has arguably never been stronger in this cycle. As ever, location is absolutely key, while consideration towards novel, contemporary workspaces may offer best letting prospects.

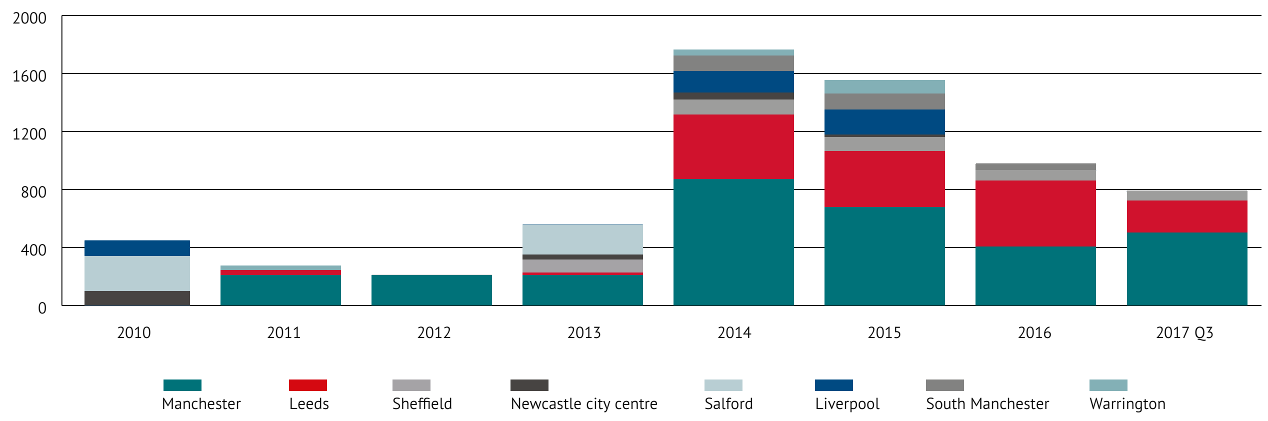
Availability as years of supply*



* Years of supply defined as current availability divided by 10-year average take-up

**Grade A includes speculative space completing in next 12 months

Speculative development under construction (000 sq ft)



SPECULATIVE DEVELOPMENT EASES DOWN

- Despite the compelling case for development, developers and funders are evidently taking a more cautious approach; a likely reflection of heightened levels of economic uncertainty. Speculative development has eased down considerably following a spike of activity during 2014 and 2015. At the end of Q3, circa 800,000 sq ft of speculative construction was taking place net of pre-lets, down 55% from its peak in 2014.
- Manchester city centre is the principal focus of new speculative development, currently making up 53% of the total activity across the region. The city is home to 502,000 sq ft of development across four schemes, followed by Leeds, where 219,000 sq ft is underway across three schemes. Sheffield is the only other market where new space is being delivered, comprising 67,000 sq ft at Steel City House.
- There is also little to suggest that this pattern will be reversed in 2018. Circa 715,000 sq ft of speculative development is anticipated to move forward in 2018, of which 565,000 sq ft is in Manchester city centre, with the rest made up of a single scheme in Sheffield and Newcastle respectively.

LOOMING PINCH IN GRADE A SUPPLY

- While 2017 will be a tough act to follow, healthy levels of active demand and an analysis of forthcoming lease events point to another year of above-trend activity and take-up across the region in 2018.
- Consequently, with development limited, the markets are heading towards a pinch in grade A supply by the end of 2018, as existing space is absorbed and not replenished. Indeed, aside from several refurbishments, Manchester city centre will not see any speculative completions in 2018, while Leeds has only one completion scheduled, namely Majestic (66,392 sq ft).

Source: LSH Research

TRACKING DEMAND

Relocation triggers and drivers

What has motivated businesses to acquire new office space across the core cities of the Northern Powerhouse and what has influenced their choice of property? Our analysis looks at activity above 5,000 sq ft over the past 12 months.

TRIGGERS – WHAT IS PROMPTING RELOCATION?

The majority of occupiers continue to base their office moves around lease events (expiries and breaks), which has accounted for 53% of all relocations above 5,000 sq ft over the last 12 months. This is an increase from the 44% recorded in 2016.

Positively, expansion accounted for a significant 28% share of office moves, in line with 2016. This is testament to the ongoing confidence among occupiers, despite the increased level of uncertainty in the economy. Leeds was exceptional, with expansion being the primary trigger for 44% of office moves.

While consolidation was the primary trigger for only 4% of office moves, it was the reason behind a number of large relocations. However, these accounted for a major share of actual take-up, with the four largest deals over the last 12 months triggered by consolidation, including the HMRC deals in Leeds and Liverpool.

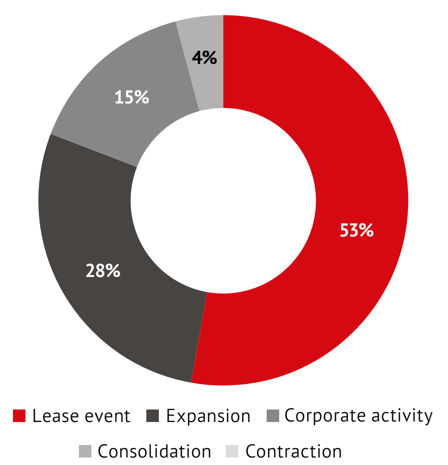
DRIVERS – WHAT DETERMINES END CHOICE?

Beyond the trigger for an office move, location continued to be the main driver choice of accommodation, accounting for 42% of transactions over 5,000 sq ft. This was evidenced by office moves to One and Two St Peter's Square in Manchester city centre, including DWP (77,449 sq ft), WeWork (44,000 sq ft) and Distrelec (16,271 sq ft), given its central location, close by amenities and access to St Peter's Square Metro Station.

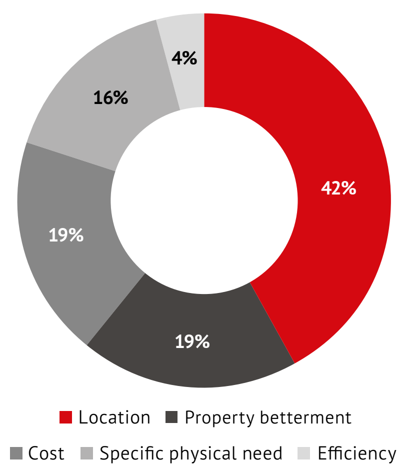
Cost appears to have become a more important factor, being the primary driver for 19% of building end choice, up from 11% in 2016. Cost was a key factor for moves in Salford, accounting for 38% of end choice, arguably reflecting the area's discount to Manchester city centre. Following Fairhome's expansion, its move to One Quays Reach at Salford Quays was primarily driven by cost.

Reflecting the significant take-up of grade A space, property betterment was the primary driver for 19% of end choice. Following lease events, the St Nicholas Building in Newcastle was chosen by Frank Recruitment Group (19,200 sq ft) and Sir Robert McAlpine (8,905 sq ft) as it was one of the few grade A buildings available following its extensive refurbishment.

Office move triggers (past 12 months)



Office choice drivers (past 12 months)



Looking ahead

While businesses are operating in a more uncertain environment following 2016's Brexit vote, our understanding of forthcoming lease events suggests there is the potential for a continuation of healthy occupier activity over the next few years.

A HEALTHY PIPELINE OF POTENTIAL DEMAND

For the eight markets of the Northern Powerhouse, there are over 550 known lease events in excess of 5,000 sq ft between 2018 and the end of 2020. For every market, including Manchester city centre, the amount of forthcoming lease events is running ahead of pipeline development.

The profile of lease events varies throughout each of the next three years. Most notably, the number of larger lease events (i.e. 10,000 sq ft and above) in 2018 is much more prevalent than in 2019. The one constant is the prevalence of events ranging from 5,000 to 10,000 sq ft, a trend worth considering in asset management strategies.

Naturally, a significant proportion of lease events will not result in relocation, but it is nonetheless an essential trigger of demand, particularly for occupiers of poor quality space. The risk is that, without the appropriate supply in place to attract this latent demand, occupiers will have little choice but to stay in situ.

NEWCASTLE LEADS THE WAY

Placed into context with current stock, Newcastle shows the most demand potential, with known lease events between 2018 and 2020 equivalent to 18% of stock. Other markets also offer strong potential, with events equating to at least 12% of stock in six of the markets, including Leeds and all of the Greater Manchester locations.

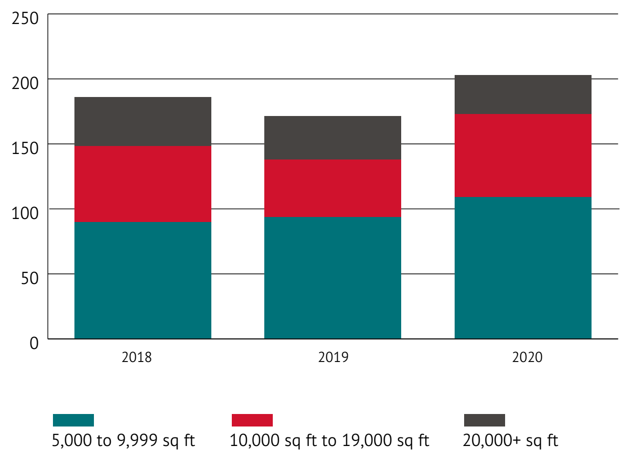
At the other end of the scale, Liverpool and Sheffield appear to have less potential demand in the pipeline, with lease events equivalent to less than 8% of stock. However, this reflects a lack of particularly large lease events, with a healthy number of smaller events, as is evident throughout the region.

THE RISE OF THE REFURB

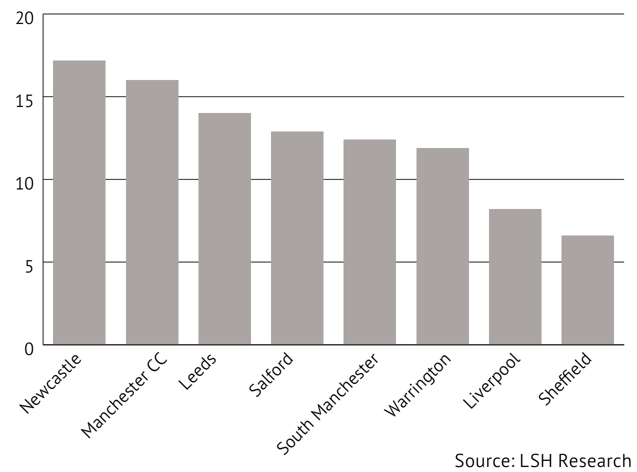
Investors will no doubt appreciate the compelling case for development in the region but, without complete confidence in the outlook, they remain understandably wary at the present time. However, with availability of grade A space set to become increasingly acute by the end of 2018, the current dynamics in the market support the repositioning of existing buildings through refurbishment.

As millennials come to dominate the workforce, occupiers are becoming ever-more discerning in their requirements. When considering refurbishments, landlords that can differentiate their offer to be more creatively inspired and suited to increasingly flexible ways of working stand to benefit most.

Number of lease events in the eight key markets



Volume of lease events as share of stock (2018 to 2020, %)



Source: LSH Research

INVESTMENT MARKET OVERVIEW

The summer period brought a welcome return of investment activity, signalling much improved confidence in the market. While the economic outlook remains uncertain, tight supply and evidence of meaningful rental growth provides a compelling argument for investment in the region.

IMPROVING CONFIDENCE SPURS VOLUME

Following a quiet first half of 2017, the summer saw a revival of investment activity across the Northern Powerhouse. At £570m, Q3 volume was among the strongest quarters on record and surpassed the combined total for both Q1 and Q2. Improved confidence among buyers and, crucially, vendors over their pricing aspirations has been pivotal.

Q3 volume was admittedly skewed by Warrington Council's major £200m purchase of Birchwood Park, Warrington, the region's largest ever office deal outside Manchester. However, Q3 saw a flurry of other sizeable deals with Manchester dominating in typical fashion, accounting for seven of the region's 11 transactions in excess of £10m.

Two major deals in the early part of Q4, namely Schroders' £200m purchase of No.1 Spinningfields, Manchester and L&G's £130m purchase of the India Buildings, Liverpool have provided the platform for a strong finish to the year. Despite a quiet H1, volume for 2017 as a whole is now expected to reach circa £1.5bn, a level only bettered in 2014 post the great recession.

INSTITUTIONS MAKE EMPHATIC RETURN

The turnaround in H2 is largely attributable to the institutions, which have returned to the market emphatically following a quiet 12 months after the Brexit vote. Major deals in Q3, such as M&G's £105m purchase of 101 Embankment and Aviva's £20m purchase of 55 Spring Gardens, Manchester have propelled the institutions back as the top buyer-type in the region.

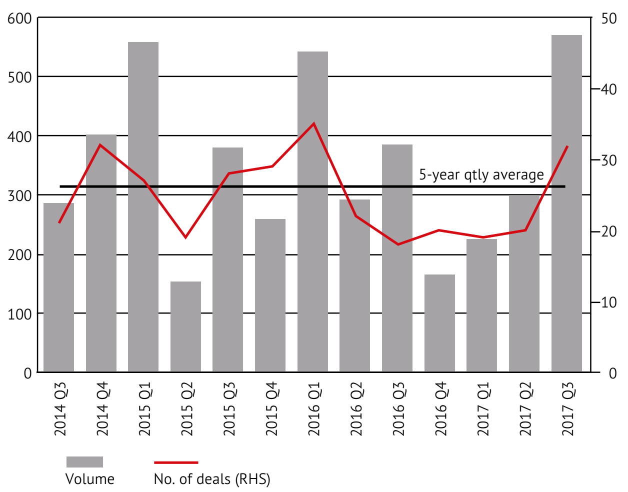
Local authorities have been the largest net buyers of offices over the past 12 months. That said, their volume of £317m was confined to only three deals; Warrington Council's purchase of Birchwood Park, Salford Council's £100m forward purchase of 100 Embankment, Salford and Bracknell Forest Council's £17.1m purchase of 1 Nunnery Square, Sheffield.

The peculiar emergence of the local authorities as major buyers of commercial property reflects their ability to borrow at preferential rates alongside a growing need to generate income. Whether this trend can be sustained largely depends on whether the Government takes action to curtail use of public funds purely for investment purposes.

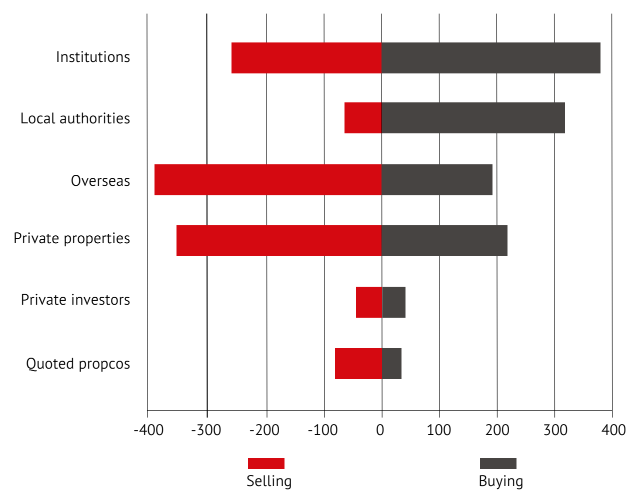
Buoyed by the post-Referendum fall in the pound, overseas buyers remain very much active, with far Eastern, US private equity and European investors all seeking value-add opportunities. However, overseas buyers were net sellers over 12 months to Q3, reflecting a number of major sales including Patrizia and Oaktree's sale of Birchwood Park.

Evidence of improving occupier demand and tight supply in the out-of-town markets has also driven overseas interest in office parks. Attracted by their scale and income return attributes, overseas buyers have been particularly active, with notable deals in 2017 including Longmead Capital's £25m acquisition of Trident Office Park at Manchester Airport and Squarestone PIM's £18.2m purchase Capital Park, Leeds.

Office investment volume (£m)



Office investment by buyer type (12 months to end Q3 2017, £m)



PRIME YIELDS BACK UNDER PRESSURE

Recent evidence indicates pricing for prime, well-let office assets has largely returned to its pre-Referendum level across the region. Prime yields in Manchester stand at circa 5.00%, confirmed by Schroders' purchase of No.1 Spinningfields in October and 25bps keener than prices achieved at the end of 2016, not long after the Referendum.

Reflected in volume and pricing, Manchester remains the undisputed focus of investment demand in the region, typically followed by Leeds. However, with a favourable yield discount on offer, strong demand exists for high quality product elsewhere, albeit micro-location is always uppermost in investors' considerations.

While Liverpool has seen only three deals during 2017 to Q3, this largely reflects a lack of suitable product. In Q3, Aberdeen AM bought 4 St Pauls Square from Muse Developments for £18.7m following Corestate's Q1 purchase of the Royal Liver Building for £48m (NIY 6.2%). With prime yields standing in excess of 6.00%, Liverpool and Sheffield are attractive for yield-seeking investors.

SHOULD INVESTORS BE WORRIED BY INTEREST RATE RISES?

November 2017 brought the first interest rate rise in over a decade. However, the 25bps rise only restores the base rate from its post-Referendum 'emergency' level back to 0.5% from a year ago. By itself, this is unlikely to have an impact on sentiment and is already priced in to investors' expectations.

Further potential escalation in the base rate over the next 18 months, say to around 1.0%, poses more of a challenge. However, the investment market is relatively well-placed to cope under this scenario; the current cycle is far less debt dependent than it previously was, while the historically high margin between base rate and property yields offers scope to accommodate small, gradual rate hikes.

That said, while further rate rises are not expected to impact adversely on yields, they might act to dampen the prospects for further compression, particularly at the prime end of the market. In Manchester, some investors have been expecting prices to move to sub 5.0%, but this could arguably be curtailed if further interest rate hikes are announced.

MARKET FUNDAMENTALS SUPPORT ASSET MANAGEMENT ANGLES

Broadly speaking, the dynamics in the occupier market provide an increasingly compelling case for asset management. Investors should be particularly attracted by evidence of steep rental growth for good quality refurbishments seen across the region's key markets.

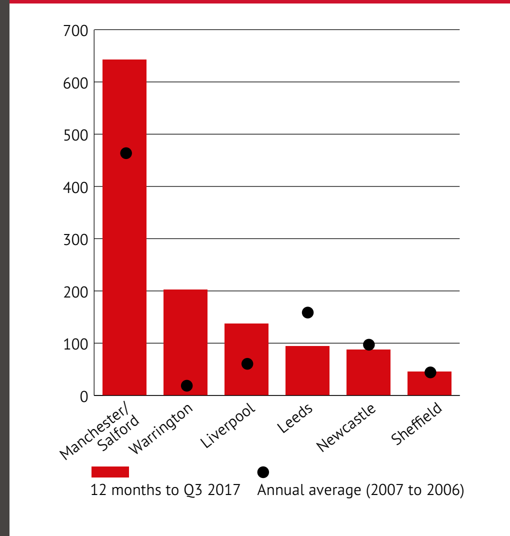
Manchester and Leeds have long been a prime target for these sorts of opportunities. Notable purchases in 2017, such as CIS Tower, Manchester and 1 East Parade, Leeds are prime examples of investors looking to capitalise on positive conditions in the market by repositioning existing assets.

Thus far, investors have been more cautious elsewhere. However, recent evidence of strong growth for refurbished product in cities such as Sheffield and Newcastle could shift wider opinion.

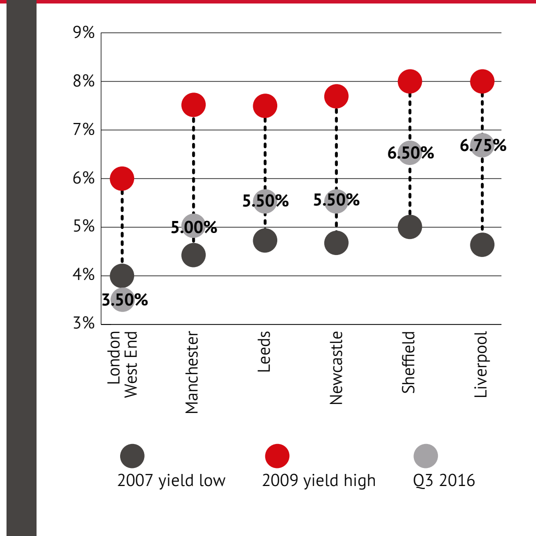
We have seen consistent healthy demand from SME occupiers whose requirements tend to be driven more by location, character and affordability. Investors who can tap into this part of the market with unique or differentiated offerings may reap the rewards.

As ever, location is absolutely critical and a detailed knowledge of the local markets is essential.

Office volume vs average (£m)



Comparison of prime office yields



Source: LSH Research

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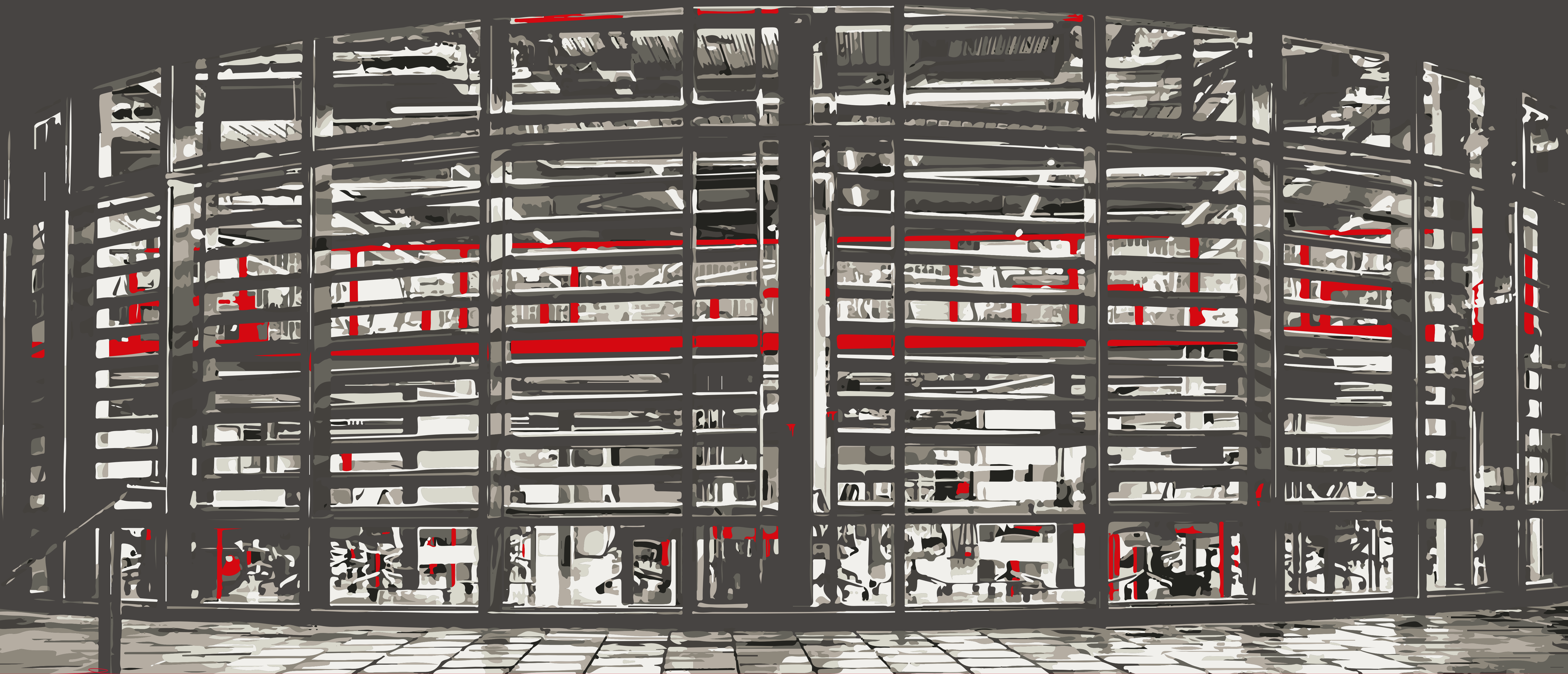
Leeds Dock courtesy of Jonathan Walls

MARKET INSIGHT



LEEDS

Highlights

- **Take-up received a huge boost in Q3 following HMRC and NHS Digital's 378,000 sq ft Leeds Government Hub pre-let at Wellington Place.**
- **Leeds' prime headline rent moved to a new high of £30.00 per sq ft in Q2.**
- **Grade A supply in the city centre will be boosted by two completions before the year end.**
- **A lack of space in the pipeline points to a sharp pinch in grade A supply by 2019.**

Demand

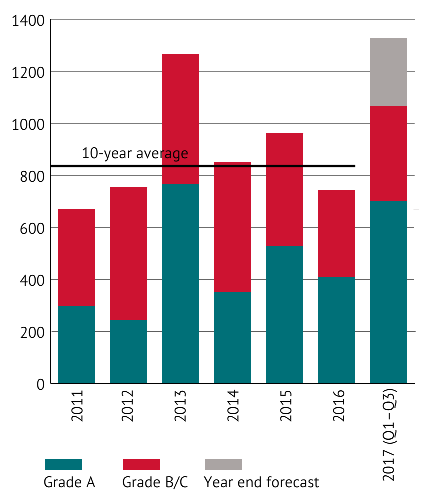
2017 is set to be a standout year for the Leeds office market. In the city centre, take-up is on course to reach the 1m sq ft mark by the end of the year for the first time ever, while out-of-town activity will comfortably exceed the annual average.

Take-up was propelled by the announcement in Q3 that HMRC and NHS Digital (via the Cabinet Office's Government Property Unit) will pre-let 378,000 sq ft at Wellington Place in the city centre. This is Leeds' largest ever office deal and the UK's largest in 2017 to date outside Central London.

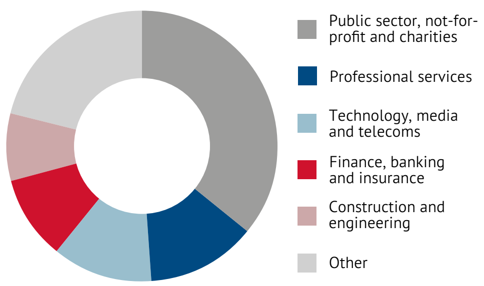
Even discounting the above deal, take-up is above trend with a healthy level of demand and depth to activity. In 2017 to date, the city centre has seen 11 deals in excess of 10,000 sq ft, encompassing a broad range of occupiers, such as Burberry (40,058 sq ft), Sky Subscription Services (25,740 sq ft) and Willis Towers Watson (25,968 sq ft).

The out-of-town market has also performed well in 2017. The headline deal to date being Zenith's lease of an additional 18,145 sq ft at CEG's 1 Kirkstall Forge development, having pre-let 45,079 sq ft in Q4 2016. Elsewhere, Paradigm, Thorpe Park (31,650 sq ft) is presently under offer and will boost 2017 take-up further.

Leeds take-up (000 sq ft)



Leeds take-up by sector (past 12 months)



Current supply

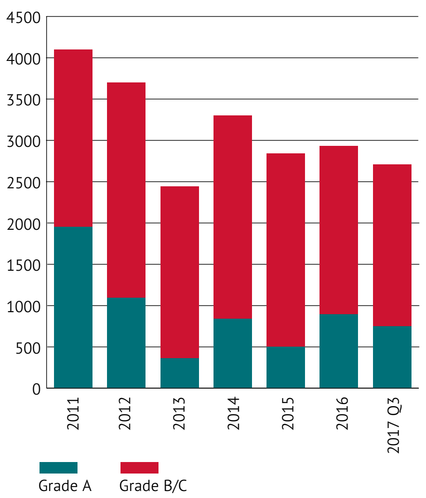
Despite several prominent completions, overall supply across the city centre and out-of-town markets combined has edged down by 7% during 2017 to stand at 2.7m sq ft. Placed into context with average levels of take-up, this equates to circa 3.3 years of supply.

The market is tighter in the city centre, however, with just 2.7 years' worth of supply. Circa 540,000 sq ft of grade A space is available, much of which comprises the remaining space at recent speculative completions, such as Central Square (72,928 sq ft), Platform (77,425 sq ft) and 5 Wellington Place (71,784 sq ft).

Three schemes are presently under construction in the city centre. CBREi's comprehensive refurbishment of 7 Park Row (40,874 sq ft) within the traditional core and MEPC's 3 Wellington Place (111,419 sq ft) in the West End are approaching practical completion, while Rushbond's Majestic (66,392 sq ft) is scheduled to complete in 2018.

Elsewhere, in the newly-formed Innovation District, The University of Leeds' £40m innovation centre – Nexus – is under construction and expected to complete in September 2018. The building will provide high quality office and laboratory accommodation, offering a collaborative environment for the city's growing technology-led companies.

Leeds availability (000 sq ft)



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Forecast 2017 take-up vs 10-year average	Years of supply	Share of grade A supply	Q3 2017 headline rent (per sq ft)	Prime yield
+60%	3.3	28%	£30.00	5.50%

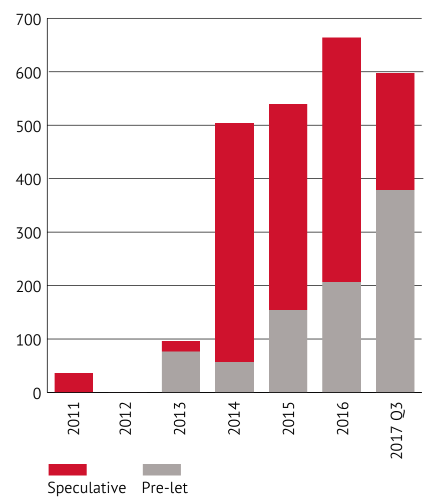
Development prospects

Beyond what is under construction, there are no additional new-build developments expected to come forward during 2018. Indeed, given the healthy levels of demand and the pipeline of lease events over the next 12 months, there is a genuine prospect of a sharp pinch in grade A supply emerging in 2019.

A number of refurbishments have been mooted and are expected to commence over the coming year, albeit they are likely to end up being pre-let. This includes Benson House (72,192 sq ft) and Sovereign House (80,643 sq ft) in the city centre and Optim, White Rose Business Park (Munroe K, 39,422 sq ft) out-of-town.

Longer-term, the focus of new supply is expected to shift towards the South Bank, reflecting the greater abundance of development sites relative to the city core. Vastint's former Tetley Brewery site has outline consent and has the potential to provide 915,000 sq ft of employment space, while CEG's Temple Quarter and Carillion's Tower Works sites also have the potential for a further 405,000 sq ft of grade A office space.

Leeds under construction (000 sq ft)



Market rental values and yields

In the city centre, Burberry's 40,000 sq ft lease at 6 Queen Street pushed the prime headline rent to a new high of £30.00 per sq ft, an 11% increase from its previous level. Similarly, limited quality supply in the prime out-of-town locations has seen prime headline rents increase by 20% to £22.50 per sq ft during 2017.

Well-located, good quality, refurbished grade B buildings are also attracting high rents, especially those differentiated from conventional product. For example, Boultbee Brooks' Concordia Works recently achieved £25.00 per sq ft.

The investment market has been relatively active in 2017, with 11 transactions over the year to date, albeit volume has been below average due to a lack of big ticket deals. The largest deal was JP Morgan's £22.2m purchase of Toronto Square from M&G. While there is little direct evidence to confirm pricing, prime yields have remained stable at 5.50% over the past 12 months, although sentiment indicates potential hardening to 5.25%.

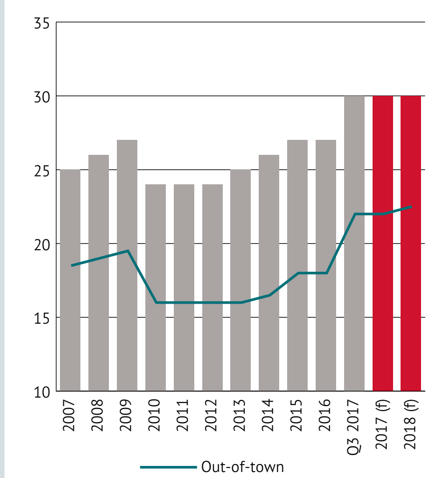
Outlook

While 2017's outstanding year for take-up is unlikely to be repeated, 2018 is expected to be another busy year for the market, evidenced by a healthy level of requirements and a pipeline of lease events. There is arguably sufficient grade A supply available to cater for demand over the next 12 months, although the lack of any development starts in 2018 could leave the market short of grade A space by 2019.

Following a step-change in 2017, we expect prime headline rents to remain stable within the city centre over the course of 2018. That said, we also expect headlines of, or near, £30.00 per sq ft to be achieved more consistently as the existing grade A space is steadily absorbed. Prospects for further growth above the level are contingent on new development coming forward.

End 2018 ▶ £30.00 per sq ft

Leeds prime headline rent (£ per sq ft)



Data source: Lambert Smith Hampton

LIVERPOOL

Highlights

- **Take-up in 2017 was exceptional, with the highest total volume recorded in recent years.**
- **Activity was significantly boosted by HMRC's decision to locate a state-of-the-art regional hub at the 270,000 sq ft India Buildings on Water Street.**
- **Overall supply has continued to decline, although grade A availability has increased due primarily to large refurbishment projects.**
- **Prime rents remain unchanged at £20.50 per sq ft since 2012, although rental growth is anticipated in 2018.**

Demand

Take-up has been very strong in 2017, surpassing the annual total in every year since 2010 with a quarter still to run.

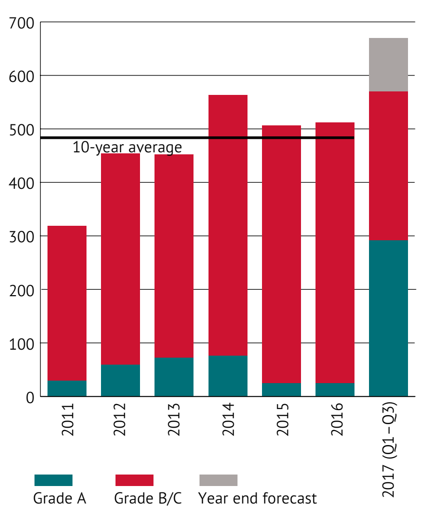
Take-up has been spurred by HMRC's letting of the 10-storey 270,000 sq ft India Buildings in the heart of Liverpool's commercial district and Liverpool John Moore's 58,000 sq ft lease at the former Victorian Exchange Station on Tithebarn Street.

The next largest deals were both in out-of-town locations, with North West Ambulance Service leasing 42,000 sq ft at Estuary Point in Speke and Kura leasing 34,983 sq ft at Caspian House in Atlantic Park.

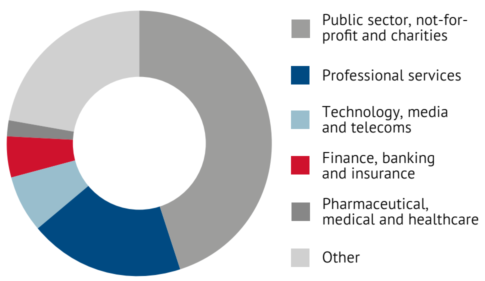
Boosted by the HMRC deal, the public sector, not-for-profit and charity organisations accounted for almost half of take-up over the past 12 months. However, despite accounting for a modest 20% of take-up, professional services have been particularly active, with 36 deals over the period. Notable transactions included DLA Piper's 16,300 sq ft lease at Walker House and Castlerock Recruitment's 13,000 sq ft lease at 20 Chapel Street.

Demand continues to be focused in Liverpool city centre, making up 80% of take-up. However, engineering, energy, utilities and pharmaceutical/medical occupiers were more likely to take space out-of-town, with traditional service sector occupiers in finance and professional services clustered in the city centre.

Liverpool take-up (000 sq ft)



Liverpool take-up by sector (past 12 months)



Current supply

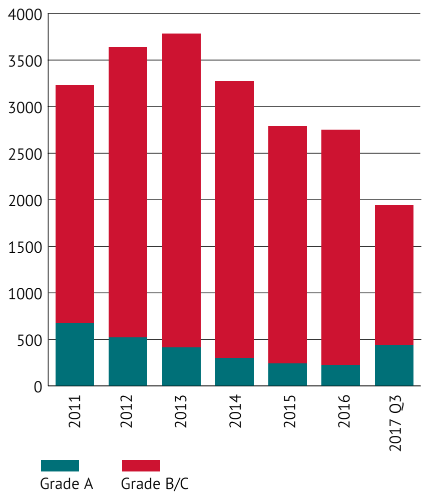
Standing at circa 1.9m sq ft, availability has fallen by 30% since the end of 2016. Based on average annual take-up, this translates into 4.0 years supply. While overall availability has been decreasing, the supply of grade A stock has risen significantly since the end of 2016, currently standing at 437,792 sq ft or 26% of supply.

A significant amount of grade A stock has been delivered via large refurbishment projects, much of which is within some of Liverpool's most iconic buildings. Example include the Royal Liver Building (95,633 sq ft), the former Lewis' department store renamed The Department (38,126 sq ft) and the Port of Liverpool Building (18,469 sq ft).

The only new-build space is at the Atlantic Container Line building, Duke Street, where 20,000 sq ft is available.

The loss of poorer quality office space to other uses such as hotels, residential and student accommodation is also a contributing factor to the sharp decline in availability. Recent examples include 1 Arthouse Square (converted to an apart-hotel), 47 Castle Street (converted to a hotel) and Silkhouse Court on Tithebarn Street (converted to residential).

Liverpool availability (000 sq ft)



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Forecast 2017 take-up vs 10-year average	Years of supply	Share of grade A supply	Q3 2017 headline rent (per sq ft)	Prime yield
+39%	**3.6**	**26%**	**£20.50**	**6.75%**

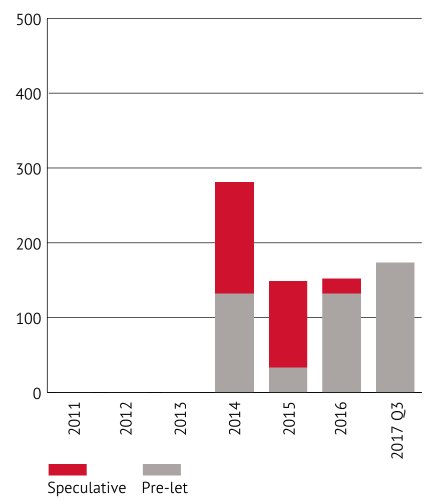
Development prospects

While traditional speculative development has been largely absent in Liverpool in recent years, new quality stock has been delivered through purpose builds or pre-let development. Purpose builds completing in the second half of 2017 include Merseyside Police's £48m 107,800 sq ft Operational Command Centre at Estuary Business Park, Speke, and the £25m 65,300 sq ft Liverpool Life Sciences Accelerator Building in the new Royal Liverpool Hospital health campus.

The 25,000 sq ft Sensor City building, a joint venture between University of Liverpool and Liverpool John Moores University which completed in June 2017, is a recent example of speculative development. This building, however, is a collaborative hub for sensor technology development and not traditional office stock open to the whole occupier market.

Liverpool City Council has announced it is seeking to address the shortage of new build stock, specifically in the commercial district, by bringing forward a joint venture to redevelop Pall Mall Exchange and deliver an additional 400,000 sq ft of space.

Liverpool under construction (000 sq ft)



Market rental values and yields

Liverpool's prime city centre headline rent remains unchanged since 2012 at £20.50 per sq ft. High quality refurbishments are attracting rents around £17.00-£18.00 per sq ft. Tight supply and a lack of speculative development are however putting rental levels under pressure, and we expect to see rents increase to £21.00 per sq ft during 2018.

Prime office yields currently stand at 6.75% with a number of transactions in the last year providing evidence on pricing. India Buildings on Water Street was bought by Legal and General Investment Management in August 2017 for a reported £130m, with the letting to HMRC secured. Other examples include the landmark Royal Liver Building which was purchased for £49m (NIY 6.08%) in February 2017 by Royal London Mutual, and Exchange Flags was purchased by Lone Star for £42m (NIY 8.75%) in November 2016.

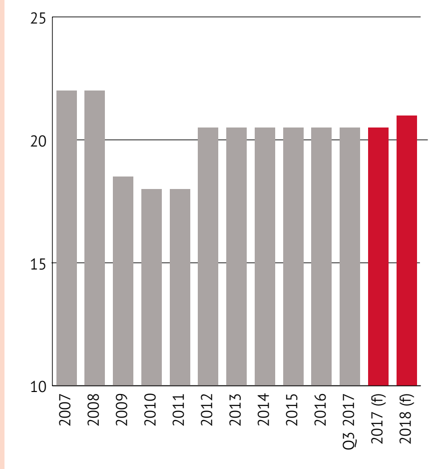
Outlook

2017 was a record year for the Liverpool office market, and while we do not anticipate that 2018 will top this, the market dynamics bode well for take-up and rental growth in the next 18 months.

Over the last few years the city has relied on refurbishment projects to satisfy demand for quality office space. Along with the loss of space to conversion schemes, conditions are ripe for speculative development. The proposed £200m joint venture Pall Mall scheme presents an excellent opportunity for developers, investors and tenants.

End 2018 ▲ £21.00 per sq ft

Liverpool prime headline rent (£ per sq ft)



Data source: Lambert Smith Hampton

MANCHESTER CITY CENTRE

Highlights

- **Annual take-up for 2017 is on course to reach a new record.**
- **Sizeable grade A options are limited to a handful of buildings, despite significant development in recent years.**
- **An absence of new-build completions in 2018 will put grade A supply under acute pressure.**
- **After a two year pause, prime headline rents will increase in 2018 as existing space is steadily absorbed.**

Demand

Manchester city centre is on course for a record 2017, fuelled by particularly strong take-up in Q3, including DWP's lease of 77,000 sq ft at Two St Peter's Square – the largest deal of 2017 to date – while Clyde & Co leased 69,000 sq ft at Manchester Royal Exchange.

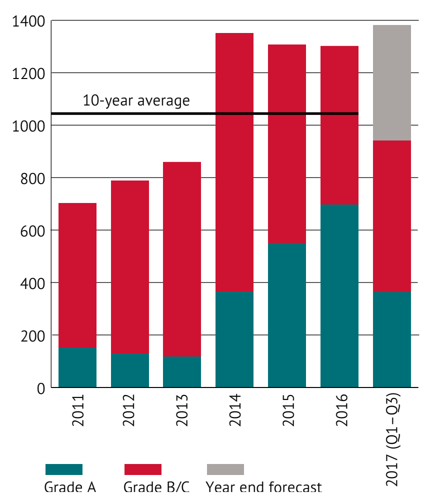
Q3 also saw CoWorking office provider WeWork acquire 44,000 sq ft at One St Peter's Square, following its 55,000 sq ft acquisition at No.1 Spinningfields in Q2. WeWork's meteoric expansion has largely focused on London but its attention has clearly turned to Manchester, with additional requirements in the market.

There are also a number of potentially sizeable deals in the pipeline for Q4, including Amazon, which is rumoured to be closing in on up to 100,000 sq ft.

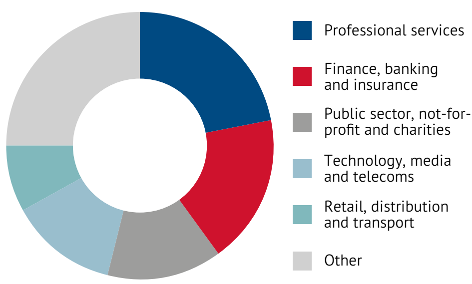
Aside from the headline deals, the smaller end of the market continues to enjoy consistent levels of activity, with deals of below 5,000 sq ft accounting for 81% of total transactions and a 30% share of take-up over the past 12 months.

The city is also being buoyed by the arrival of new international businesses, including electronics distribution giant Distrelec which confirmed Manchester for its new UK base with the acquisition of 16,300 sq ft at Two St Peter's Square.

Manchester CC take-up (000 sq ft)



Manchester CC take-up by sector (past 12 mths)



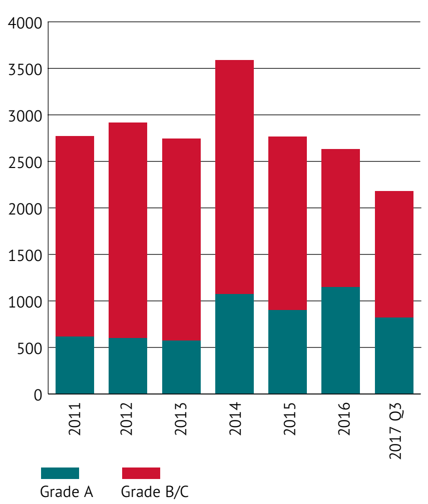
Current supply

Despite a steady stream of completions over the past few years, consistently strong demand continues to put pressure on supply. Overall availability has contracted by 18% from the turn of the year to stand at a record low of 2.2m sq ft, equivalent to 2.1 years of supply.

The year has seen several prominent completions, although a significant proportion was either pre-let or rapidly absorbed, leading to a 30% fall in grade A supply. Examples include Two St Peter's Square (167,500 sq ft), where 25,197 sq ft remains, and No.1 Spinningfields (283,000 sq ft), where only 28,000 sq ft remains.

Indeed, of the 821,000 sq ft of grade A supply, only 563,000 sq ft is available for immediate occupation. There are also relatively few sizeable options, notable examples include The Corner Block, (55,000 sq ft), 3 Hardman Square (40,000 sq ft) and 55 Spring Gardens (28,000 sq ft).

Manchester CC availability (000 sq ft)



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Forecast 2017 take-up vs 10-year average	Years of supply	Share of grade A supply	Q3 2017 headline rent (per sq ft)	Prime yield
+23%	2.1	38%	£34.00	5.00%

Development prospects

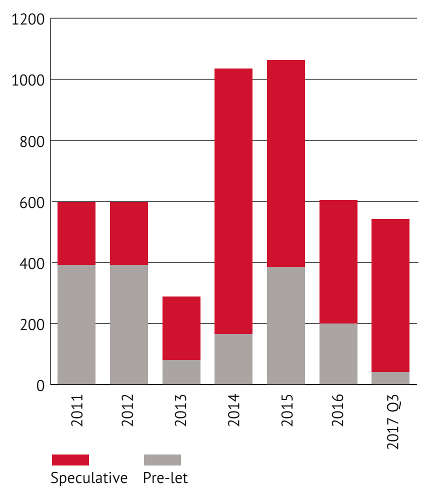
On face value, there is a reasonable quantum of speculative development taking place, with 542,000 sq ft under construction across four separate schemes. However, only one of these is set to complete in the near-term, namely Patrizia's First Street (173,000 sq ft) in the Cultural Quarter, where delivery is imminent.

With completion scheduled in 2019, the three other schemes comprise The Landmark (180,000 sq ft), 125 Deansgate (110,000 sq ft) and 11 York Street (79,000 sq ft). An absence of new-build completions in 2018 suggests grade A supply will come under acute pressure by the end of 2018, as existing space is absorbed but not replenished.

That said, a number of landlords are capitalising on strong demand by delivering refurbishments. Several high quality schemes are underway and set for delivery in 2018, including Hanover (100,000 sq ft), 101 Barbirolli (87,000 sq ft), Windmill Green (80,000 sq ft) and Dalton Place (65,000 sq ft).

Several new-build schemes are widely expected to come forward during 2018, although this supply will not be delivered until at least 2020. At the 'Island Site', Greater Manchester Property Venture Fund (GMPVF) has a 100,000 sq ft scheme planned, while others include 100 Embankment (167,000 sq ft) and Two New Bailey (189,000 sq ft).

Manchester CC under construction (000 sq ft)



Market rental values and yields

Prime headline rents in the city core have been steady at £34.00 per sq ft, reflecting healthy choice in the market. Elsewhere, however, rental growth has been dramatic. The once down-at-heel Northern Quarter is now widely sought after, with rents moving from circa £13.00 per sq ft to £20.00 per sq ft within the space of three years and further growth anticipated, given the lack of supply.

The summer saw an emphatic revival of investment activity, signalling a much improved confidence in the market and the return of institutions. The city centre has seen 10 deals in excess of £20m in 2017 to date, the largest of which was Schroder's £200m purchase of No.1 Spinningfields in early Q4. With an NIY of 5.00%, the deal also provided confirmation of the city's prime yield.

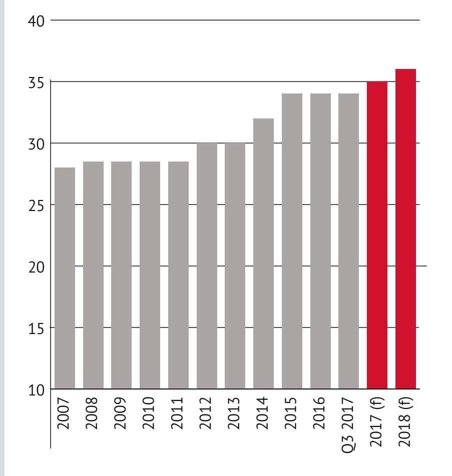
Outlook

A slowing in the rate of completions during 2018 will put a steady upward pressure on rental levels. Manchester's prime headline rent is expected to move up to £35.00 per sq ft by the end of 2017 and continue its upward trajectory in 2018 to hit £37.00 per sq ft. Meanwhile, rents for high quality refurbishments are expected to break £30.00 per sq ft.

Manchester has enormous potential to benefit from inward investment over the next few years and is arguably the best alternative to London in terms of the quality and breadth of its workforce. The city is also well-placed to capture overseas occupiers looking for a regional or European base, without the high occupancy costs associated with Central London.

End 2018 ▲ £36.00 per sq ft

Manchester CC prime headline rent (£ per sq ft)



Data source: Lambert Smith Hampton

NEWCASTLE

Highlights

- **2017 has seen strong activity among SMEs, driven by the expansion of tech occupiers.**
- **A new prime headline rent of £23.50 per sq ft is anticipated by the end of the year.**
- **Refurbishments tailored to SME-type demand have let-up well and secured high rents.**
- **The first of the two 100,000 sq ft office buildings at Science Central is set to be on site by Q1 2018.**

Demand

Take-up in Newcastle city centre stands at 139,848 sq ft for the first three quarters of 2017, up 16% on the equivalent period in 2016. That said, with only three deals over 10,000 sq ft in the year to date, take-up for 2017 as a whole is expected to fall circa 15% short of the 10-year annual average.

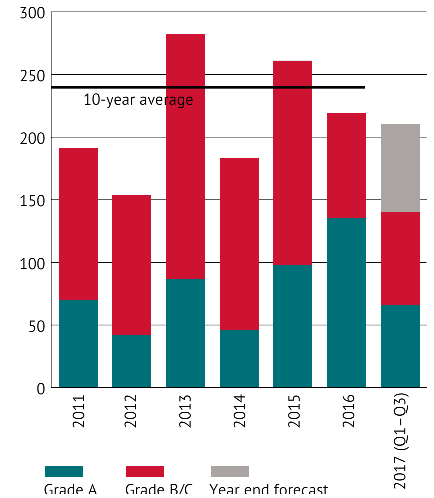
Once again, however, the out-of-town market has led the way in terms of take-up, with activity over the first three quarters of 2017 reaching 367,188 sq ft, 11% up on the 10-year average. The largest out-of-town deal in 2017 to date was Durham Police's 33,600 sq ft purchase of 6 Admiral Way, Doxford.

Modest take-up has largely reflected a lack of major deals, with healthy activity seen among SMEs. Reflecting this, the average deal size stands at 3,800 sq ft, 17% below the 2016 average and 33% below the 2015 average.

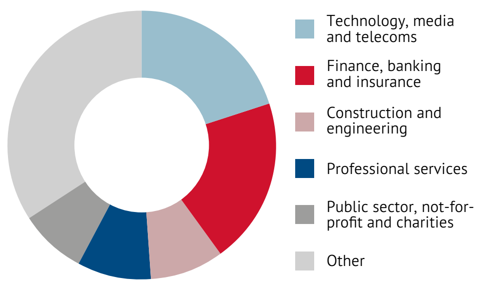
Activity among smaller TMT occupiers has been notable, with numerous transactions driven by expansion. Generator Studios has successfully attracted this sort of demand and is now fully let after deals to Hedgehog (4,068 sq ft), Real Time Claims (3,931 sq ft) and Atlas Cloud (2,636 sq ft). The success of the scheme is testament to strong demand for contemporary-style office accommodation with exposed services.

In terms of active demand, there are two major requirements in the city centre and out-of-town of 20,000 sq ft and 90,000 sq ft respectively. Other requirements are limited to smaller sizes of below 5,000 sq ft.

Newcastle city centre take-up (000 sq ft)



Newcastle take-up by sector (past 12 months)



Current supply

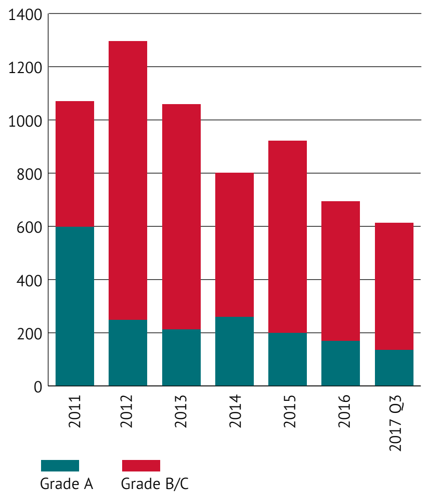
In the city centre, total availability has fallen by 11% since the beginning of 2017 to stand at 613,821 sq ft. This is equivalent to 2.6 years of supply based on annual average take-up.

Meanwhile, grade A supply reduced by 21% from the beginning of the year to 134,601 sq ft. Central Square South accounts for a third of this and offers the largest floorplates in the city centre. Situated within the Stephenson Quarter and adjacent to Newcastle Central Station, both this area and the Business District north west of the city typically attract professional and financial services occupiers.

The east of the city centre, encompassing Carliol Square (which includes Campus North) and the Generator Studios, are hubs for startup and TMT businesses. Buildings with contemporary fit-outs have proved popular, and those refurbished to this type of specification have let-up well.

Supply is plentiful out-of-town, with Quorum and Cobalt Business Park each having almost 300,000 sq ft of grade A space available. Responding to difficulties in attracting larger occupiers, building Q11, Quorum was recently sub-divided into smaller suites and is now almost fully let. Following its success, Q10 is also due to be carved up to accommodate smaller grade A requirements.

Newcastle city centre availability (000 sq ft)



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Forecast 2017 take-up vs 10-year average	Years of supply	Share of grade A supply	Q3 2017 headline rent (per sq ft)	Prime yield
-13%	2.6	22%	£23.00	5.50%

Development prospects

While there are no developments currently underway, there are a number of exciting schemes in the pipeline.

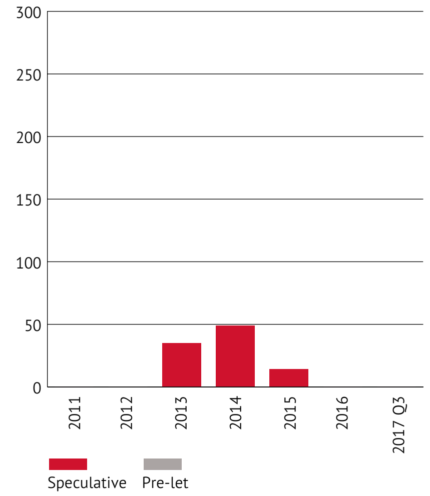
On the former Newcastle Brown Ale brewery site, a joint venture between L&G, Newcastle University and Newcastle City Council will deliver up to 500,000 sq ft of office and lab space. The first of the two 100,000 sq ft grade A buildings within the scheme is due to commence in Q1 2018 and, once this is 60% let, plans are in place to deliver a further 100,000 sq ft.

Alongside this, Marrico's Strawberry Place site is another proposed development in the offing, with outline consent now in place to include 107,000 sq ft of grade A offices.

Elsewhere, Taras Properties Ltd is due to submit a planning application for 100,000 sq ft of offices on the site adjacent to Pilgrim Street, albeit the scheme remains two-to-three years away from completion.

Having been prolific in 2016, instances of office conversion to student accommodation have slowed markedly in 2017 as fewer opportunities now exist, combined with a market which is nearing saturation. One of the few examples in 2017 comprised the 43,000 sq ft No 1 Kings Manor, which was sold for conversion in Q2.

Newcastle under construction (000 sq ft)



Market rental values and yields

Prime headline rents in the city centre have remained stable at £23.00 per sq ft over the past two years. However, a new rent of £23.50 per sq ft is expected to be achieved by the end of 2017.

Meanwhile, rental levels for grade B refurbished buildings have shown marked growth. For example, following their refurbishment, headline rents at Earl Grey House and the St Nicholas Building were driven up from circa £17.00 per sq ft to in excess of £20.00 per sq ft, while the latter is now almost entirely let following Frank Recruitment Group's 19,200 sq ft lease in Q1.

Prime yields have sharpened throughout the year and were pushing towards circa 5.50% at the end of Q3. The deal to note is Keel Row House, occupied by law firm Ward Hadaway and sold to a private buyer for £8.855m, reflecting 5.57% NIY.

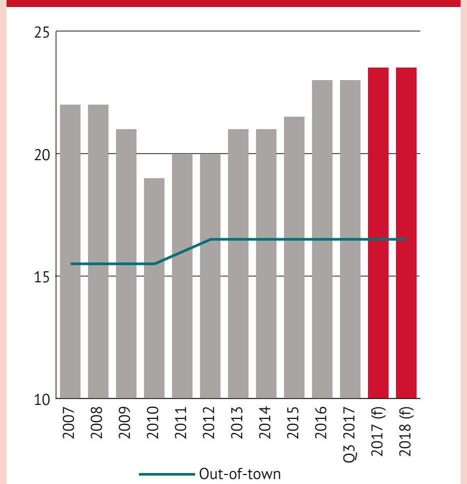
Outlook

A respectable level of take-up is expected in the final quarter of 2017, although it will fail to bring the annual total into line with the 10-year average. However, the exciting schemes in the pipeline should be a catalyst for activity over the next few years.

In the meantime, proactive landlords who look to tailor their assets to occupier demand, whether that be via contemporary fit-outs or smaller-sized suites, are likely to benefit from stronger leasing potential and rental growth.

End 2018 ▲ £23.50 per sq ft

Newcastle prime headline rent (£ per sq ft)



Data source: Lambert Smith Hampton

SALFORD

Highlights

- **Grade A supply is limited reflecting strong occupier demand and a lack of development.**
- **MediaCity's reputation as a tech hub continues to attract both large corporates and SME occupiers.**
- **Salford's prime headline rent is expected to reach a new high of £26.00 per sq ft in 2018.**
- **Transactional evidence indicates the prime yield hardened by 25 bps over 2017 to stand at 6.25%.**

Forecast 2017 take-up vs 10-year average	Years of supply	Share of grade A supply	Q3 2017 headline rent (per sq ft)	Prime yield
+4%	3.2	20%	£25.00	6.25%

Demand

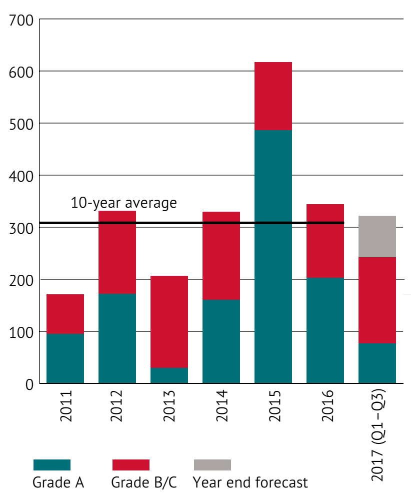
Take-up in the first three quarters of 2017 was 241,578 sq ft, down 14% on the equivalent period in 2016. That said, take-up for the year as a whole is expected to be closely in with the 10-year average. Demand remains healthy, particularly among TMT occupiers, as the market offers good access to the city centre but discounted overall rents in direct comparison.

Notably, Salford was home to Manchester's fifth largest deal of 2017 to date, Kellogg's 48,120 sq ft lease at MediaCity in Q3 2017. The deal will see the company relocate from its headquarters in Old Trafford to the Grade A Orange Tower in 2018.

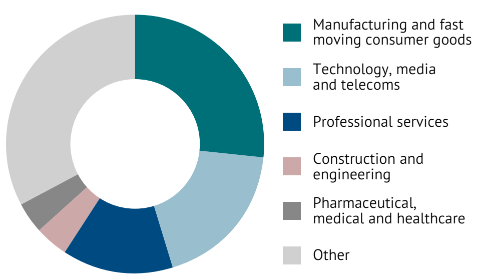
Kellogg's move into grade A accommodation reflects the demand for quality space, which is not only evident among large corporates but also the SME tenants. The Tomorrow Building continues to attract deals to smaller occupiers, with seven deals below 5,000 sq ft transacted in the last 12 months, largely within the TMT sector.

MediaCity has attracted manufacturing and fast-moving consumer goods occupiers throughout 2017, with deals including the likes of Kellogg's and JTI. At 27%, this tenant type accounted for the largest proportion of Salford's take-up over the 12 months to Q3.

Salford take-up (000 sq ft)



Salford take-up by sector (past 12 months)



Current supply

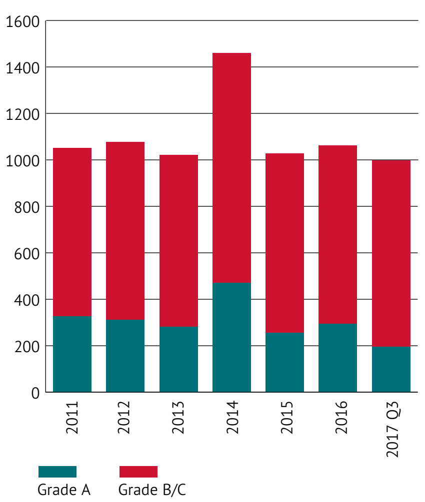
Since the beginning of 2017, total availability has fallen by 6% to 1.0m sq ft. This is equivalent to 3.2 years of supply based on the average annual take-up over the past ten years.

However, demand for high quality accommodation has driven a steady erosion of grade A supply. Grade A space has fallen by 33% since the start of 2017 to stand at less than 200,000 sq ft, very limited when placed into the context of strong grade A take-up over the past few years.

Options are becoming increasingly limited at MediaCity. A flurry of activity over the past 12 months has left the Orange Tower and Tomorrow Building with combined availability of just 42,000 sq ft, or just 29% of the total built space.

Elsewhere, Exchange Quay offers 62,000 sq ft of refurbished accommodation across a number of buildings at the end of Q3.

Salford availability (000 sq ft)



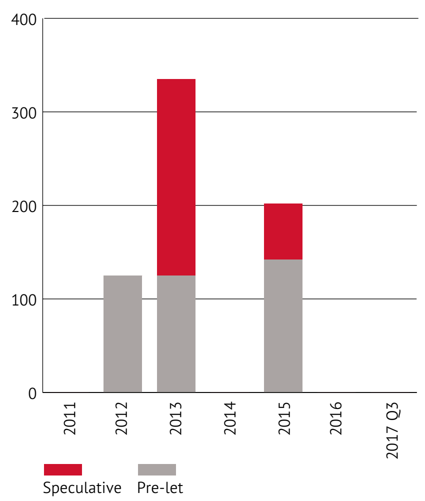
Development prospects

There are no developments currently underway in the market but conditions are ripe, given the rate at which grade A supply is diminishing.

In the meantime, talks are ongoing around the potential third phase of the Soapworks by owner Peel Group. The refurbishment project would deliver 160,000 sq ft of offices but is unlikely to commence for a couple of years.

Longer-term, MediaCity has the potential to expand by a further 1.6m sq ft but there are constraints relating to the decommissioning of the industrial gas works which sits opposite.

Salford under construction (000 sq ft)



Market rental values and yields

Prime headline rents increased by 2% in 2017 to stand at £25.00 per sq ft. This was achieved by JTI's 16,040 sq ft lease at the Orange Tower in Q1. Incentives have remained unchanged over the last 12 months but, given the tightening of grade A supply, there is potential to see reductions going forward.

Sentiment indicates that prime yields have hardened by 25 bps during 2017 to stand at 6.25% at the end of Q3. Two major deals transacted in Salford this year, the largest of which was Greater Manchester Pension Fund's £60.0m (NIY 6.3%) acquisition of Soapworks from Carlyle Group in September.

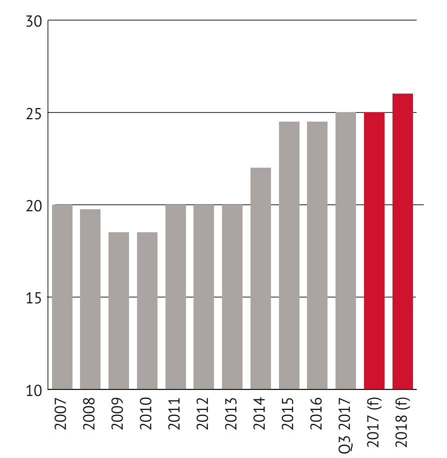
Outlook

Salford's credentials as a major UK tech hub continue to strengthen. The final quarter is expected to bring 2017's take-up to circa 320,000 sq ft, 4% above the 10-year average despite being slightly down on 2016's total.

With no development underway, dwindling grade A supply is likely to see a new prime rent achieved in 2018. The remaining space at the Orange Tower and Tomorrow Building is expected to achieve £26.00 per sq ft over the next 12 months.

End 2018 ▲ £26.00 per sq ft

Salford prime headline rent (£ per sq ft)



Data source: Lambert Smith Hampton

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SHEFFIELD

Highlights

- **Activity is set to outperform the annual average in 2017, with take-up likely to exceed 400,000 sq ft.**
- **Take-up has been less reliant on the public sector than previous years, with a handful of large deals across a range of sectors.**
- **A new headline rent of £24.00 per sq ft is expected to be achieved by the end of 2017.**
- **Vidrio, Digital Campus is anticipated to commence construction in 2018, delivering 50,000 sq ft of speculative office space.**

Demand

At 310,287 sq ft, take-up across Sheffield for the first three quarters of 2017 almost exceeded the total recorded for 2016. The year as a whole is expected to exceed 400,000 sq ft, surpassing the 10-year annual average by 13%.

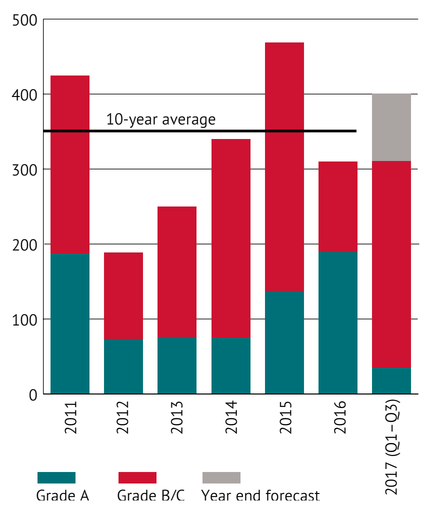
While take-up in 2016 was boosted by HSBC's pre-let of 140,000 sq ft, no major deals of a similar scale transacted in 2017. However, unlike 2016, the year has seen several large transactions in excess of 15,000 sq ft.

While take-up has historically been driven by the public sector or back office operations, Sheffield has seen a marked increase in demand from the creative industries. At 31%, TMT occupiers accounted for the largest proportion of take-up of any sector over the last 12 months. This was boosted by the city's largest deal of 2017 to date, Johnson Publishing's 27,000 sq ft lease at The Balance.

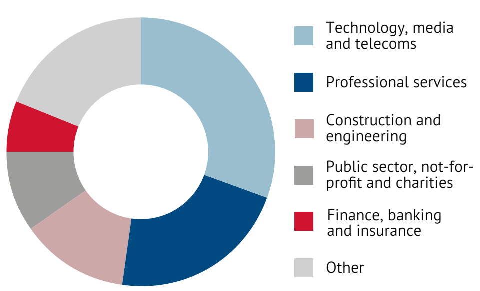
Out-of-town, demand is focused along the M1 corridor although with a lack of development in this cycle, the market remains subdued. That said, further afield, the success of The Advanced Manufacturing Park (AMP) is having a positive effect on the wider South Yorkshire market with globally renowned occupiers including Rolls-Royce and McLaren establishing bases in the region.

The Sheffield office market should continue to perform well over the coming months, with a number of deals currently under offer as well as several prominent active requirements. This includes one notable inward investment, namely Jet2's requirement for circa 6,000 sq ft.

Sheffield take-up (000 sq ft)



Sheffield take-up by sector (past 12 months)



Current supply

Since the beginning of 2017, supply across Sheffield has fallen by 14% to stand at 917,344 sq ft at the end of Q3. This equates to 2.6 years of supply based on the ten-year average take-up.

Grade A supply is very low by historic standards, despite the Q3 completion of Acero Works at Digital Campus which delivered 80,500 sq ft to the market. Furthermore, four floors in the building are currently under offer, with over half of the building expected to have let by the end of 2017.

Acero Works' relative success is arguably attributed to its larger floorplates, which offer up to 14,694 sq ft. 3 St Paul's, which completed in 2015, provides further grade A space in the city centre, offering smaller floorplates of up to 8,248 sq ft.

Permitted development rights have had a positive impact on the market, consolidating tertiary and poorly located office stock. One such example is Crown House, which recently completed its redevelopment into luxury student accommodation having stood empty as an office for 10 years.

Sheffield availability (000 sq ft)

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Forecast 2017 take-up vs 10-year average	Years of supply	Share of grade A supply	Q3 2017 headline rent (per sq ft)	Prime yield
+13%	2.6	19%	£23.00	6.50%

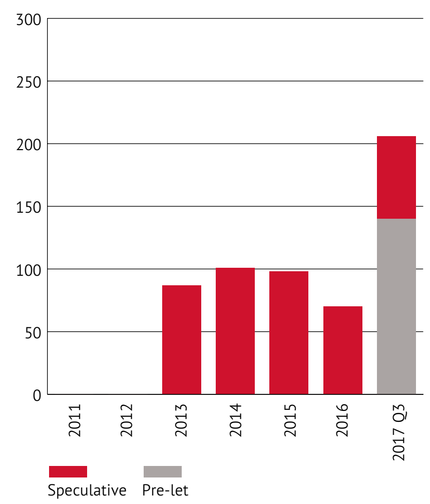
Development prospects

Steel City House is currently the only office development underway. Scheduled for completion in early 2018, the Grade II-listed building is being developed into offices with two new floors added to the roof which have been let to The British Business Bank.

The next phase of Digital Campus, Vidrio, is anticipated to start once Acero Works is 50% let. Given the interest and space under offer at Acero Works, Scarborough Group's development is likely to commence in early 2018 which will deliver 50,000 sq ft of office space by H1 2019.

Following HSBC's pre-let in 2016, its bespoke building is set to be occupied in summer 2018. This, combined with the recent public realm improvements, is expected to act as a catalyst for further development and occupier activity in the new Retail Quarter.

Sheffield under construction (000 sq ft)



Market rental values and yields

Prime headline rents have remained stable for a number of years at £23.00 per sq ft. The completion of Acero Works has provided the opportunity for rental growth, with prime rents expected to climb to £24.00 per sq ft by the end of 2017.

As refurbished schemes continue to let well due to a lack of supply, high-end grade B space has shown marked increases in rents. For example, following its refurbishment, quoting rents at St James House were driven up from circa £8.00 per sq ft to in excess of £12.00 per sq ft and is now almost entirely let.

Prime yields have hardened in 2017, moving in 25 bps to stand at 6.50% at the end of Q3. This was supported by two deals, including UK CPT's £20.165m acquisition of 2 Cutlers Gate from EPIC-REIT, reflecting a 5.00% NIY.

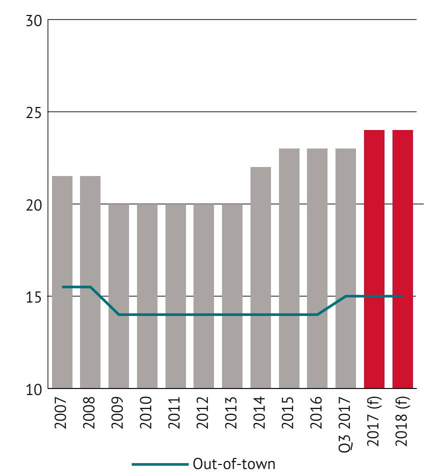
Outlook

The final quarter is expected to see 2017 take-up exceed 400,000 sq ft, almost 30% up on 2016, despite HSBC's major pre-let that year. A new prime rent is expected to be achieved by the end of 2017 as transactions at Acero Works complete.

Benefitting from competitive occupier costs and a highly educated workforce, Sheffield has been successful at attracting inward investment. Ongoing developments at Digital Campus and the Retail Quarter stand the city in good stead over the coming years.

End 2018 ▲ £24.00 per sq ft

Sheffield prime headline rent (£ per sq ft)



Data source: Lambert Smith Hampton

SOUTH MANCHESTER

Highlights

- **Take-up in 2017 is on course to exceed both 2016's level and the 10-year average.**
- **Overall supply is at a record low, while grade A space accounts for only 16% of the total.**
- **The new-build development at One Stockport Exchange demonstrates strong occupier appetite for high quality space.**
- **Prime headline rents are forecast to remain stable at £24.00 per sq ft into 2018.**

Demand

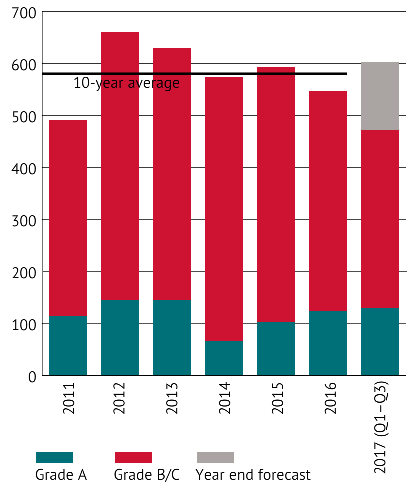
Take-up reached 472,263 sq ft in the first three quarters of 2017, currently standing at 82% of the 10-year average (574,637 sq ft). Activity in Q4 is forecast at circa 130,000 sq ft, bringing total take-up for 2017 to an above-average 600,000 sq ft and 10% above 2016's level.

The largest deal in the last year was social housing provider Great Places Housing's 36,003 sq ft acquisition of 1 Christie Fields in West Didsbury.

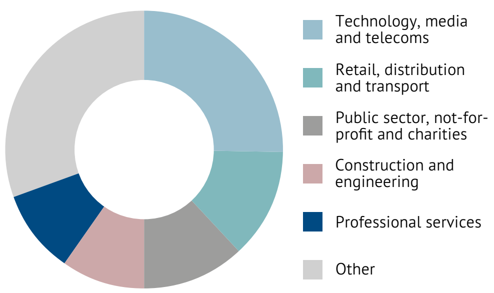
Activity has been dominated by small deals, with transactions below 5,000 sq ft accounting for 87% of deals over the past 12 months. The larger transactions, however, were concentrated in the premier locations, such as Didsbury, Manchester Airport or along the A56 corridor.

The TMT sector has been particularly active over the past 12 months, accounting for a quarter of take-up across 28 deals, the most of any sector. Key examples include UKFast's 35,237 sq ft lease at Number 3 Archway and Vodafone's 33,567 sq ft lease at Pacific House.

South Manchester take-up (000 sq ft)



South Manchester take-up by sector (past 12 months)



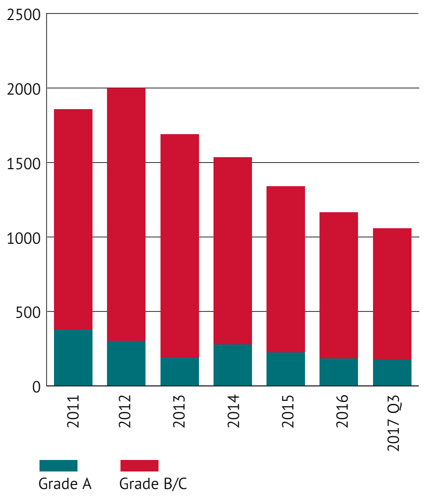
Current supply

Availability has almost halved from its 2m sq ft peak in 2012, currently standing at a record low of 1m sq ft. Based on average take-up this equates to only 1.8 years of supply, the lowest of the key markets in the Northern Powerhouse.

Diminishing supply reflects both a lack of speculative development and robust market activity. In recent years there has been much expansion from businesses already located in this market, resulting in an uptake of space. Along with this, inward investment from new occupiers has accounted for approximately 10% of take-up per year.

Supply of grade A space is a key concern. Accounting for only 16% of total availability, 172,849 sq ft of grade A space is available across nine properties, most of which are clustered in the Manchester Airport area. The largest available grade A properties include 48,343 sq ft at Cheadle Royal Business Park and the 45,500 sq ft at Atlas Business Park with the balance being spread across a number of buildings.

South Manchester availability (000 sq ft)



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Forecast 2017 take-up vs 10-year average	Years of supply	Share of grade A supply	Q3 2017 headline rent (per sq ft)	Prime yield
+5%	1.8	16%	£24.00	6.50%

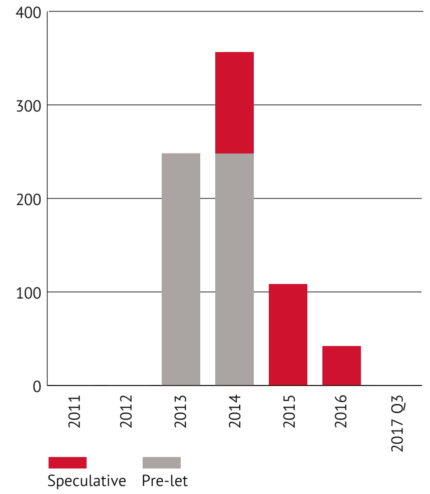
Development prospects

The market has seen the first new-build speculative development since 2009 complete in Q1 2017. One Stockport Exchange brought 50,000 sq ft of new-build space to the market in the first phase of the £1bn regeneration plan for Stockport, which includes 375,000 sq ft of office space. During construction, however, leases were agreed by musicMagpie (10,118 sq ft) and Stagecoach (33,000 sq ft).

While new-build development has been elusive, landlords have been capitalising on occupier demand by repositioning existing properties. Rental values for high quality refurbishments have moved up to a range of £18.00–£24.00 per sq ft for prime locations, with recent examples at Towers Business Park, Didsbury, Trident Office Park and 4M at Manchester Airport.

New-build development is predicted to commence at Airport City in early 2018, but this is likely to be pre-let. Atlas Business Park is in the process of developing a masterplan for new development and Manchester Business Park has land available.

South Manchester under construction (000 sq ft)



Market rental values and yields

Prime headline rents have been climbing steadily for the last decade, although there was no movement between the end of 2016 and Q3 2017, where prime rents have remained steady at £24.00 per sq ft. This level was achieved at the end of 2016 by Stryker's lease at Worthington House, Towers Business Park in Didsbury.

Meanwhile, ranging from £20.00 to £22.00 per sq ft, the best rents in locations close to Manchester Airport are discounted from prime levels. However, these are expected to move into line with prime levels during 2018.

Prime office yields stand at circa 6.50% in the South Manchester market. In 2016, the £82m purchase of Towers Business Park by Kennedy Wilson Europe Real Estate reflected 6.40% NIY. Notable transactions in 2017 include Trident Office Park purchased for £25m (NIY 7.31%) and Virgin Media House on Concord Business Park purchased for £19.7m (NIY 8.29%).

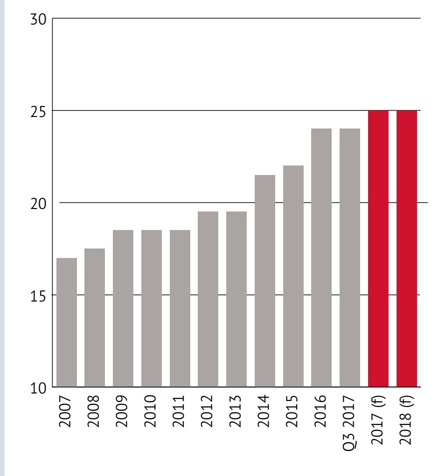
Outlook

The demand in South Manchester set against a diminishing level of availability will remain a challenge in the short to medium-term. In order to sustain this robust level of activity into 2018, however, additional supply is required to satisfy current requirements and attract good quality tenants.

Prime rents are forecast to remain stable at £24.00 per sq ft into 2018, as currently there is no suitable supply to achieve higher rents. With rental growth in second-hand space and occupier appetite for new-build space, as demonstrated at One Stockport Exchange, conditions are ripe for speculative development. We anticipate that speculative development will commence during 2018 and a step-change in prime headline rents will occur in 2019.

End 2018 ▲ £25.00 per sq ft

South Manchester prime headline rent (£ per sq ft)



Data source: Lambert Smith Hampton

WARRINGTON

Highlights

- 2017 take-up is on course to exceed the annual average for a fifth successive year.
- Comprehensive refurbishments have been key to the delivery of grade A space during this cycle.
- An increase in prime headline rents is dependent on new-build stock being delivered to the market.
- Warrington Council's purchase of Birchwood Park bodes well for the long-term development potential of the site.

Demand

The Warrington market has enjoyed another robust year of activity. Take-up in 2017 to Q3 stands at 267,000 sq ft, with activity for the year as a whole on course to surpass the annual average for a fifth successive year.

2017's standout deal was Cavendish Nuclear's 47,149 sq ft lease of 106 Dalton Avenue, Birchwood Park. Birchwood Park is the hub for the UK's nuclear industry, while Birchwood itself falls within the Cheshire Science Corridor Enterprise Zone, an attractive location for science and engineering firms.

The above deal was one of seven transactions in excess of 10,000 sq ft during 2017. Reflecting the importance of the construction and engineering sector, notable examples included Murphy Group at Stonebridge Business Park (16,000 sq ft) and IESA (11,000 sq ft) and Taylor Wimpey (10,600 sq ft) at Birchwood Park.

With supply limited, 2017 has seen only three deals involving grade A space, all of which were at Birchwood Park. These comprised Cavendish Nuclear at 106 Dalton Avenue, together with Ricoh and Areva, both of whom leased 7,500 sq ft at Bridgewater Place. Both buildings were comprehensively refurbished.

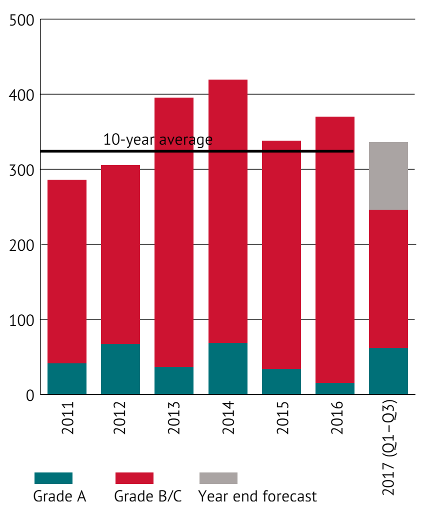
Current supply

The Warrington market is dominated by business park and out-of-town product. The premier locations are in Birchwood and Daresbury, both of which benefit from excellent road connections via the M62 and M56 respectively.

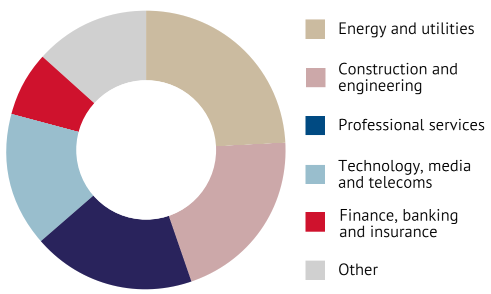
Warrington is the only key Northern Powerhouse market to have witnessed an increase in supply during 2017, rising 14% since the start of the year. This reflects several buildings coming back into the market, such as Sankey House, Birchwood Point Business Park (28,000 sq ft). Nonetheless, availability is equivalent to only 2.2 years of supply based on average take-up, making it one of the tightest of the eight markets.

As much of Warrington's existing stock is already relatively modern, occupiers are generally content to relocate locally into refurbished space. Indeed, virtually all the grade A space delivered to the market speculatively in this cycle has comprised extensive refurbishments.

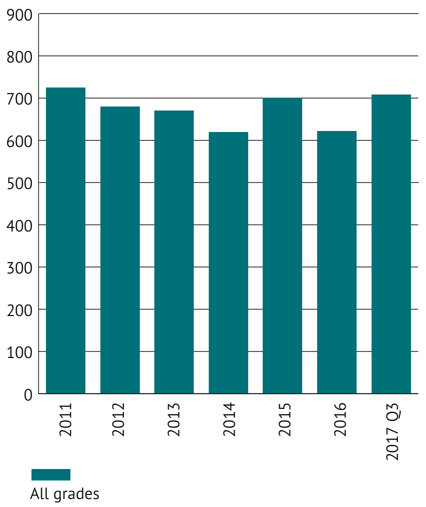
Warrington take-up (000 sq ft)



Warrington take-up by sector (past 12 months)



Warrington availability (000 sq ft)



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Forecast 2017 take-up vs 10-year average	Years of supply	Share of grade A supply	Q3 2017 headline rent (per sq ft)	Prime yield
+5%	2.2	10%	£20.00	6.75%

Development prospects

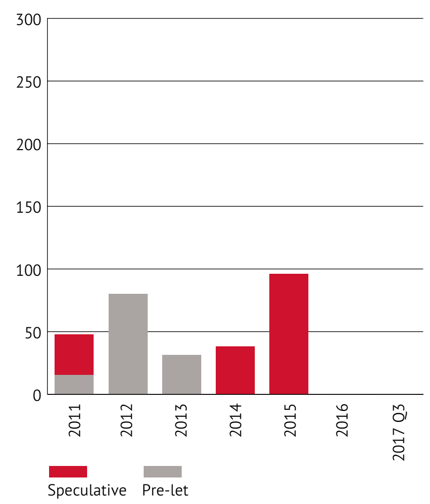
Pre-lets and purpose built agreements remain the most likely route to new development at the current time. However, there are no serious requirements of this nature in the market at present.

The largest scheme in the pipeline is in Warrington town centre. Time Square is a mixed-used scheme by Muse Developments in partnership with the Council. A key part of the proposal will see Warrington Council occupy circa 100,000 sq ft of brand new office space, with completion scheduled for 2019.

While new-build speculative development is unlikely during 2018, there is ongoing potential for major refurbishments. However, none are scheduled at present.

There is a substantial amount of development land with planning consents. This includes potential for circa 0.5m sq ft at additional capacity at Birchwood Business Park, as well as significant capacity at Daresbury Park and Omega North/South.

Warrington under construction (000 sq ft)



Market rental values and yields

Warrington's prime headline rent has held steady at £20.00 per sq ft, standing unchanged from 2016. This level has been confirmed during 2017, however, following the two lettings at 305 Bridgewater Place, Birchwood Park.

Good quality refurbishments are available from as little as £15.00 per sq ft at Birchwood Business Park and nearby surrounding areas, preserving the area's status as a competitively-priced location for back office and call centre operations.

In Q3 2017, Warrington Council purchased Birchwood Park from Oaktree Capital Management for £200m, the largest office investment deal in the Northern Powerhouse in 2017 to date. The purchase bodes well for the longer-term development of the site, as the Council will seek to maximise income and boost the local economy.

This major deal and general sentiment in the market indicates that prime yields stand at circa 6.75%, representing a significant discount to the other markets in the region.

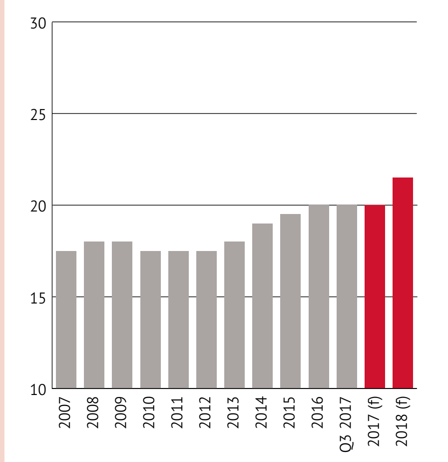
Outlook

Warrington benefits from consistent, healthy churn among a diverse range of smaller businesses, as well as offering competitively-priced space for larger, potential inward investors.

With speculative supply dominated by refurbishments, further growth of prime headline rents is contingent upon a pre-let transaction being secured. If this type of deal takes place during 2018, we envisage prime rents moving to a new high of £21.50 per sq ft.

End 2018 ▲ £21.50 per sq ft

Warrington prime headline rent (£ per sq ft)



Data source: Lambert Smith Hampton

Northern Powerhouse Microsite

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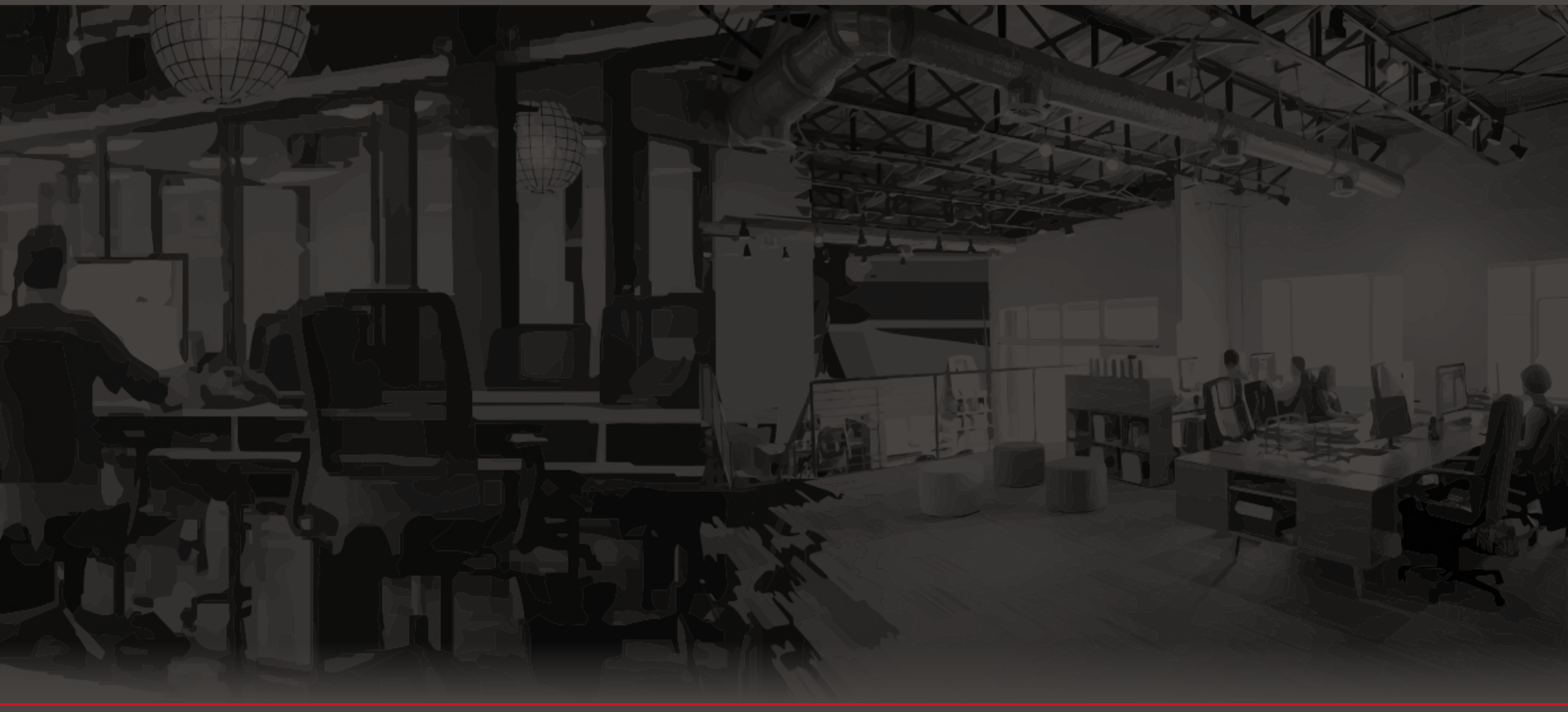

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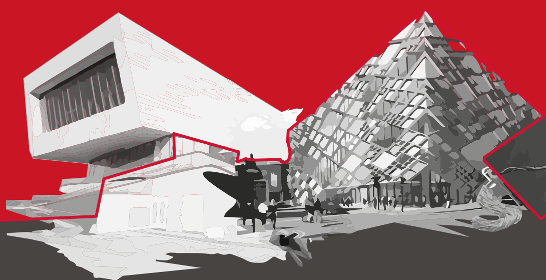

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