CoStar Portfolio Strategy Client Update

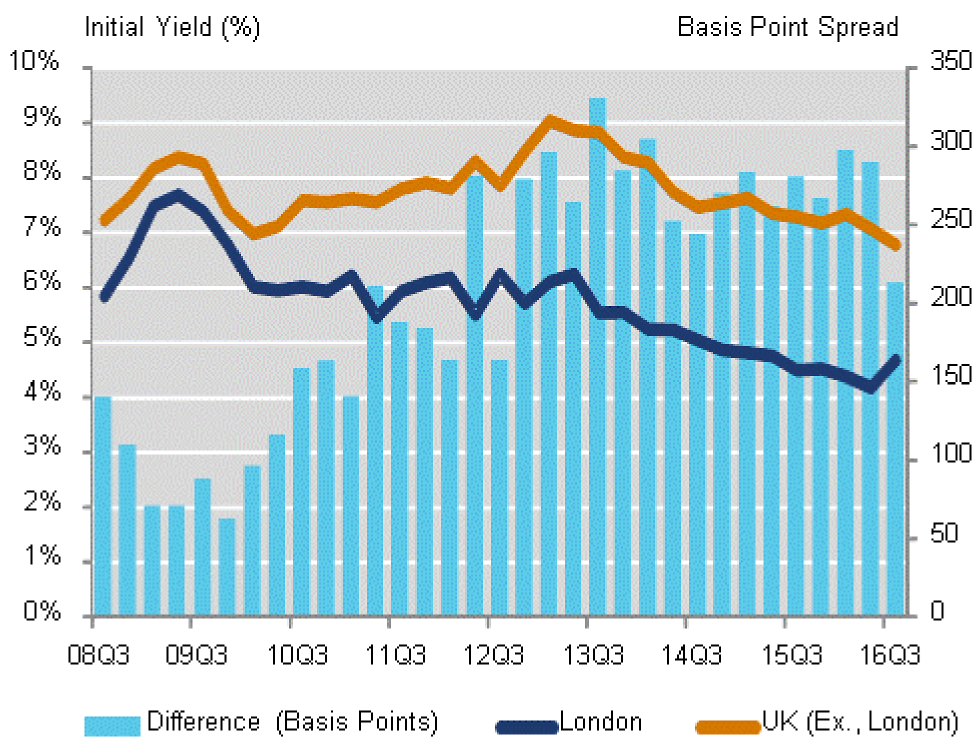
CoStar Investment Review: UK CRE Investment Continued To Decline Following Brexit Vote
By Mark Stansfield (mstansfield@costar.co.uk) | November 3, 2016

Investment in UK commercial property fell to a four-year low in 16Q3 as investors continued to rein in spending in the wake of the Brexit vote, according to CoStar's latest investment data.

The volume of trading in the third quarter (£8.7 billion) dropped by 27% from Q2's £12 billion and 42% from the same quarter a year ago. The drop was perhaps particularly acute because of Brexit, but it should be noted that volumes have been declining for several quarters now.

London offices were especially affected in Q3. Investment in Central London offices fell 64% Y-o-Y as a number of potential sales were withdrawn, while average yields ticked upwards across London (see *Exhibit 1*). Large deals were particularly scarce: Wells Fargo's £300 million acquisition of 33 Central in the City was one of only four deals above £100 million, down from 15 a year earlier. The market was supported by new overseas entrants, like China Minsheng, taking advantage of the weak pound. Overseas capital was behind a record 84% of total spending on Central London offices in Q3.

Exhibit 1: Average Yield In London Vs. Rest Of UK



Source: CoStar Group

As of 16Q3

In a quarter of weak activity, one trend stood out above all others: the emergence of local authorities as key buyers of commercial property. Motivated by central government cuts, low borrowing rates, and, in some cases, a desire to actively improve their areas, local authorities spent close to £800 million in 16Q3—more than in the previous three years combined.

On a sector-by-sector basis, offices and shopping centres were the big underperformers, with investment in the latter falling to its lowest quarterly level since 2009. Industrial investment also fell, but logistics is perhaps the sector best placed to withstand Brexit uncertainty as the shift from physical to online retailing is expected to continue regardless of wider economic conditions, fuelling demand for sheds in the right locations. Student accommodation investment held up strongly in Q3, and such defensive assets are likely to prove popular in the near term as investors shed risk.

Despite the continued fall in investment last quarter and the uncertainty surrounding Brexit, there is still much in favour of commercial property. Vacancy rates are at historically low levels in many markets across the UK, and property still offers attractive yield spreads over other asset classes such as government bonds. Anecdotal evidence suggests there is plenty of appetite to invest once nervousness about values is overcome.

For more information and analysis on these themes, including an investment breakdown by sector and region, a spotlight on pricing and further post-referendum analysis, click here to view **CoStar's 16Q3 UK Commercial Property Investment Review**.

Any Questions or Comments?
Contact: Mark Stansfield (mstansfield@costar.co.uk)

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CoStar Group | 1331 L Street, NW, Washington, DC 20005 | www.costargroup.com | 877-498-4425