Economics & Real Estate

Q4 2016

Economy growing despite pre-Brexit predictions

Economic Highlights

- The first estimate of GDP growth for the final quarter of 2016 came in at 0.6% versus Q3 and 2.2% higher than Q4 2015. GDP is now 8.7% higher than its pre-crisis peak in 2008. However, on a per capita basis the gain is a more modest 1.9%.
- Consumer price inflation (CPI) rose to 1.6% in the year to December, up from 1.2% in November. This is the highest CPI reading since July 2014. The food and transport sectors - which are highly reliant on imports and hence impacted by sterling weakness – were the largest contributors to the rise.
- The latest employment statistics for the three months to November 2016 show a decrease in employment of 9,000 when compared against the three months to August 2016. Unemployment fell by 52,000 to 1.6 million, with the unemployment rate falling marginally to 4.8%.
- Brexit update: the Prime Minister has confirmed that she will pursue a Hard Brexit with immigration controls and "frictionless" cross-border trade. Sterling recovered some ground on the back of the positive noises on the future trading relationship. Whether this can be achieved or not remains a matter of debate for now.

Consensus forecasts suggest a year of limited growth, but a recession is seen as very unlikely.

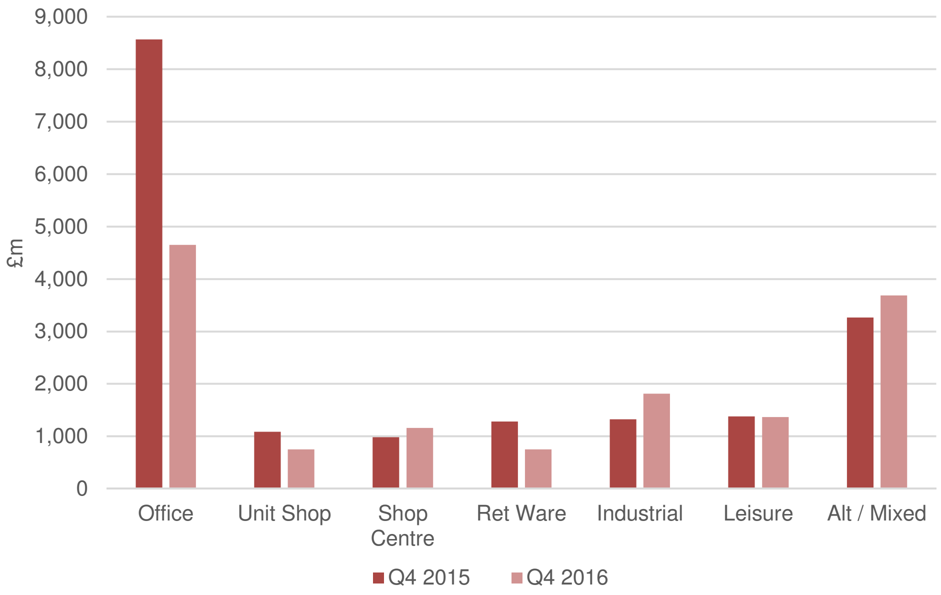
The key Purchasing Managers' Indices for the UK ended 2016 in strongly positive territory.

Sector Highlights

- Office – the UK Services PMI increased to 56.2 in December from 55.2 in November. The figure represents the fastest expansion since July 2015 and the third consecutive monthly rise. (Markit/CIPS)
- Industrial – the UK Manufacturing PMI improved in December, rising to a 30-month high of 56.1, well above the long-term average of 51.5. (Markit/CIPS)
- Retail – retail sales volumes in December fell 1.9% versus the previous month. The three months to December saw growth of 1.2% versus the previous three months, and a 5.6% increase against the same period last year. (ONS)
- Construction – the UK Construction PMI recording a reading of 54.2, up from the previous month's 52.8. The sector has now recorded four months of output growth on this measure. (Markit/CIPS)
- UK house prices increased 0.7% in Q4 2016, and were up 4.5% on an annual basis. London house prices saw growth of 0.3% in the fourth quarter, and are 3.6% higher than the same period in 2015. (Nationwide)

According to the average of independent forecasters' views compiled by HM Treasury for January, UK CPI is expected to be 2.8% in 2017. Above the Bank of England's 2% target.

Investment Activity



Source: Property Data as at 26/01/2017

Q4 2016 saw investment volumes of £14.2bn, 21% down on the same quarter last year (£17.9bn).

The IPD UK Monthly Property Index for the 12 months of 2016, reported a 2.6% total return for All Property, based on an income return of 5.6% and capital value decline of 2.8%.

Prime Yields

	Sector	Prime Yield*	Direction (next six months)
Industrial	Distribution Centre (15 years)	5.00%	Stable
Industrial	Industrial Estate - Greater London	4.50%	Stable
Industrial	Industrial Estate – National	6.25%	Stable
Office	City	4.25%	Stable
Office	West End	3.50%	Softening
Office	South East	5.25%	Stable
Office	Provincial	5.25%	Stable
Retail	High Street - Regional Centre	4.00%	Stable
Retail	Out of Town (open A1)	5.00%	Stable
Retail	Shopping Centre	4.50%	Stable
Alts	Healthcare	5.00%	Stable
Alts	Hotels	4.50%	Tightening
Alts	Student	4.75%	Stable

*The achievable yield for a freehold, prime investment; fully let and rack-rented to tenant/s of strong financial credibility on lease terms typical of prime property in that segment. Alts = Alternatives

Prime yields continue to hold their ground; although investors remain nervous around pricing, they retain significant dry powder that needs to be allocated.

In addition supply is limited, with much prime stock held by long-term equity investors with little appetite to sell and reallocate investment.

However, shorter-let and/or lower quality assets have seen, and will see, yields soften.

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