Economics & Real Estate
Q2 2016

STRUTT & PARKER

Research

Signs of a post-Referendum slowdown, but this is not 2008

Economic Highlights

– The first estimate of GDP for Q2 2016 showed that the economy grew by 0.6% during the quarter; following 0.4% growth in Q1. Representing the fourteenth consecutive quarter of growth. Service sector output increased by 0.5% and production increased by 2.1%. In contrast, construction declined by 0.4%.

The dominant services sector continued to grow in Q2, with retailing a key driver of this growth.

– The Consumer Prices Index (CPI) increased by 0.5% in the year to June, up from 0.3% in May. Going forward CPI is expected to increase at a greater rate than it otherwise would have done, given the sharp decline in sterling following the UK's vote to leave the EU.

– The latest employment statistics for the three months to May 2016 showed an increase in employment of 176,000 when compared against the three months to February 2016. Unemployment decreased by 54,000 to 1.65 million, resulting in a fall in the unemployment rate to 4.9%.

PMI data suggests that manufacturing and services output was still increasing in June.

Sector Highlights

Please note the bullet points below include data Flash PMI data from Markit collected between 12-21 July. Although these Flash PMI figures give us some insight into the post-Referendum environment, we should bear in mind that they are based on approximately 70% of usual PMI responses. Final PMI estimates will be released during the first week of August, and will give more reliable figures.

- Office – The UK Services PMI fell to 52.3 in June from 53.5 in May, matching April's 38-month low but still indicating expansion. The Flash UK Services PMI for July reported a reading of 47.4, indicating contraction. (Markit/CIPS)

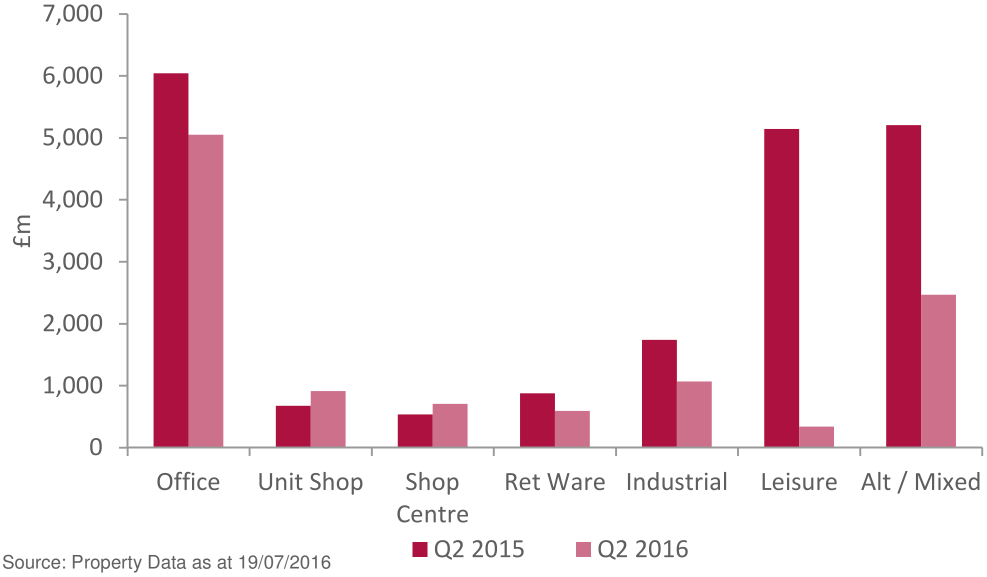
- Industrial – The UK Manufacturing PMI improved in June, rising to 52.1 from May's 50.4, its highest reading since January. The Flash UK Manufacturing PMI for July reported a contraction of activity, with a reading of 49.1. (Markit/CIPS)

- Retail – retail sales decreased by 0.9% month-on-month in June, the worst outturn since December last year. The three months to June saw growth of 1.6% versus the previous three months, and a 4.9% increase against the same period last year. (ONS)

- Construction – the UK Construction PMI turned negative in June, recording a reading of 46, down from the previous month's positive 51.2. (Markit/CIPS)

Following the vote to leave the EU, the IMF has downgraded its economic forecasts for the UK. 2016 growth is now expected to be 1.3%, with an expansion of 1.7% in 2017.

Investment Activity



Source: Property Data as at 19/07/2016

Q2 2016 saw investment volumes of £11.2bn, 45% down on the same quarter last year. (£20.2bn).

In the aftermath of the vote to leave, we have seen transaction volumes remain low, owing to the continued uncertainty. That said, where stock has been brought to market, there remain many motivated and competitive buyers.

Prime Yields

Sector		Prime Yield*	Direction (next six months)
Industrial	Distribution Centre (15 years)	5.00%	Stable
	Industrial Estate - Greater London	4.75%	Stable
	Industrial Estate – National	6.25%	Stable
Office	City	4.00%	Mild softening
	West End	3.75%	Stable
	South East	5.25%	Mild softening
	Provincial	5.25%	Mild softening
Retail	High Street - Regional Centre	4.00%	Stable
	Out of Town (open A1)	4.50%	Mild softening
	Shopping Centre	4.50%	Mild softening
Alts	Healthcare	5.00%	Stable
	Hotels	4.25%	Stable
	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

For Q2 2016 we have kept our prime yields broadly stable.

Given the current lack of market liquidity, we feel it is prudent to await further evidence on market value before rushing to judgement on any major yield shifts.

Early activity has been encouraging; however, the outlook is far from clear and consequently we expect some marginal widening of prime yields in some sectors.

Contact us

Thomas Grounds
Associate Partner
Thomas.grounds@struttandparker.com
Tel: +44 (0)20 7318 4676