Building on previous periods, the UK commercial property market continued its recovery in Q3 2021 with GBP 14.1bn\(^1\) of transactions. Activity has shown continuous improvement over the course of the year with the gradual removal of lockdown restrictions and the steady resumption of business activity. Deals which had been put on hold because of the pandemic are now coming back to the market and we anticipate a strong end to the year, which is traditionally the busiest period for transactions.

There is still a strong demand for UK commercial assets and overseas investors remain the dominant force in the UK market. Buyer interest year-to-date has been spread almost evenly between Offices (31% of YTD transactions), warehouse/logistics (29%) and ‘alternative properties’ such as business parks and student accommodation (29%). Retail property activity (11%) is focused almost exclusively on secure income assets such as supermarkets and retail warehouses with little interest in unit shops or shopping centres.

**COMMERCIAL PROPERTY**

**INVESTMENT ACTIVITY CONTINUES TO RECOVER**

Ongoing recovery in investment activity;
Strong performance from both UK REITs and direct commercial property over the period;
Property viewed as a good hedge against rising inflation;
Yields continue moving downwards although could slowdown if UK rates increase;
Industrial property returns benefiting from supply chain disruption;
Investment case for healthcare and student accommodation remains robust;
UK house prices expected to cool further in H2 2021;
Prime Central London market recovering with resumption of international travel.

Source: PropertyData, 2021

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\(^1\) Source: PropertyData, 2021
### TOP 10 LARGEST UK COMMERCIAL PROPERTY TRANSACTIONS YTD 2021

<table>
<thead>
<tr>
<th>BUILDING / TRANSACTION NAME</th>
<th>LOCATION</th>
<th>SECTOR</th>
<th>PRICE GBPM</th>
<th>DATE</th>
<th>VENDOR (NATIONALITY)</th>
<th>PURCHASER (NATIONALITY)</th>
</tr>
</thead>
<tbody>
<tr>
<td>ASDA Portfolio</td>
<td>UK Wide Portfolio</td>
<td>Industrial</td>
<td>1,700.0</td>
<td>Jul-21</td>
<td>ASDA (UK)</td>
<td>Blackstone Real Estate (USA)</td>
</tr>
<tr>
<td>Student Portfolio</td>
<td>UK Wide Portfolio</td>
<td>Student Accom.</td>
<td>969.0</td>
<td>Jul-21</td>
<td>GCP Student Living (UK)</td>
<td>iQ Student and Scape Student (UK)</td>
</tr>
<tr>
<td>Arlington Portfolio</td>
<td>UK Wide Portfolio</td>
<td>Business Park</td>
<td>714.0</td>
<td>Jun-21</td>
<td>TPG Real Estate (USA)</td>
<td>Brookfield Asset Mgt (Canada)</td>
</tr>
<tr>
<td>30 Fenchurch St, EC3</td>
<td>City of London</td>
<td>Office</td>
<td>635.0</td>
<td>Jun-21</td>
<td>Trustees of Moise Safra (Lebanon)</td>
<td>Brookfield Asset Mgt (Canada)</td>
</tr>
<tr>
<td>1 Braham Street E1</td>
<td>Central London</td>
<td>Office</td>
<td>468.0</td>
<td>May-21</td>
<td>Aldgate Developments (UK)</td>
<td>Union Investment RE (Germany)</td>
</tr>
<tr>
<td>Times Square EC4</td>
<td>City of London</td>
<td>Office</td>
<td>450.0</td>
<td>Aug-21</td>
<td>Blackstone Real Estate (USA)</td>
<td>Generali Group (Italy)</td>
</tr>
<tr>
<td>3 Minster Court, EC3</td>
<td>City of London</td>
<td>Office</td>
<td>353.0</td>
<td>Jun-21</td>
<td>Ivanhoe Cambridge (Canada)</td>
<td>Suntec REIT (Singapore)</td>
</tr>
<tr>
<td>Wembley / Whitechapel</td>
<td>Central London</td>
<td>Student Accom.</td>
<td>342.0</td>
<td>Jun-21</td>
<td>Unite Group plc (UK)</td>
<td>GIC Real Estate (Singapore)</td>
</tr>
<tr>
<td>Retail Park Portfolio</td>
<td>UK Wide Portfolio</td>
<td>Retail Warehouse</td>
<td>330.0</td>
<td>Apr-21</td>
<td>Hammerson plc (UK)</td>
<td>Brookfield AM (Canada)</td>
</tr>
<tr>
<td>Quintain Portfolio</td>
<td>UK Wide Portfolio</td>
<td>Student Accom.</td>
<td>315.0</td>
<td>Apr-21</td>
<td>Fusion Students (UK)</td>
<td>Lone Star (USA)</td>
</tr>
</tbody>
</table>

Data to 01 November. Source: PropertyData, 2021
Momentum was maintained in the private market with a total return of 4.6% in Q3 2021, bringing year to date performance to 11.1%. Average UK commercial property values have risen by 6.9% so far this year, primarily because of exceptional performance from the industrial sector. Competition for deals in general remains intense and continues to push down yields aggressively across the board. The UK All Property yield – an average yield across all sectors of commercial property - now stands at 4.68%.

In line with transactional activity, UK REITs continued their strong performance into Q3 due to improved occupier conditions, better rental collection rates and the ongoing demand for yield. UK REITs have been the best performing asset class year-to-date and have outperformed the wider UK equities market which moderated in September due to inflationary concerns. Traditionally, property is viewed as a better hedge against inflation compared to most other asset classes, with the exception of gold and commodities, as it can have either an implicit (e.g. market rental increases) or explicit (e.g. cost of building materials) link to inflation.

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Industrial/logistics property has had a strong year, with average values rising by 17.8% and average rents by 4.7%⁴. Despite being a standout performer over the past few years, fuelled by the rise of e-commerce and a structural shift in consumer habits, the sector was given extra impetus in 2021 due to global supply chain problems caused by the COVID pandemic. The UK faced perhaps more acute problems compared to other countries due to the lingering effects of Brexit. On top of external factors such as a blockage in the Suez Canal in March and a deficiency of shipping capacity in general, a lack of Heavy Goods Vehicle ("HGV") drivers and the common use of a ‘Just in Time’ inventory system left many UK companies without enough stock when demand unexpectedly recovered. This has led to some high-profile shortages and periods of panic buying for certain items – most infamously toilet roll in March 2020 and petrol in September 2021. The gradual adoption of a ‘Just in Case’ inventory system to avoid such problems in the future has led to substantially higher occupier demand for warehouse space. Year-to-date, there has been 35.8m sq ft of take-up⁵, a record high and there are still 3 months to go before the end of the year. Supply has not been able to keep up and is sitting at an all-time low⁶. This imbalance explains the rampant growth of the sector this year and the trend is expected to continue into 2022. We still strongly favour industrial property, especially the urban warehouse sub-sector due to the critical need for businesses to fulfil the ‘last mile’ of product delivery in a timely manner. Warehousing in urban areas is experiencing an acute constraint on supply due to restrictive UK planning laws. At the same time, there is robust competition for sites from other potential occupiers and from UK housing developers.

⁴Source: MSCI, 2021
⁵As at 30 Sep. Source: BNPPRE, 2021
⁶Source: CBRE, Allsops, 2021
We also continue to favour primary healthcare and student accommodation in the alternative sector. The COVID pandemic has stressed both sectors in different ways but their fundamental investment cases remain intact. The UK has an aging population with rising and more complex healthcare needs. This is a demographic reality unaffected by financial markets, economics or politics. Modern, purpose-built primary healthcare assets, such as care homes or doctors’ surgeries, are needed to deal with these needs although the healthcare itself is provided by either the National Health Service or specialist care home operators. The UK also remains home to some of the world’s best universities and student numbers continue to climb, despite the disruptions of the past 18 months. We believe that the focus should be on the so-called ‘Russell Group’ of research universities and that the presence of an operational platform (in addition to the bricks & mortar) is the key to success.

Source: BNP Paribas Real Estate, 2021

Source: HESA, Bloomberg, 2021

Source: ONS, 2019

Source: UCAS, 2021
The UK residential market cooled over the period, as anticipated, with the gradual removal of the Stamp Duty holiday between 01 July and 30 September. Average UK property prices are up 7.4% higher year-on-year\(^8\), but there was a discrepancy between the performance of houses (8.8% for detached, 8.9% for semi-detached) compared to apartments (6.1%) as buyers sought more rooms and outdoor space in response to the pandemic. Greater London underperformed the other UK regions for the same reason. A potential rise in interest rates (i.e. higher borrowing costs), inflationary pressures on the cost of living and a traditionally slow winter period is likely to lead to further cooling before year end.

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**UK House Prices, Annual % Change SA**

\(^8\)Data as at end Jun-21. Source: Halifax/Lloyds Banking Group, 2021
PRIME CENTRAL LONDON RESIDENTIAL

The Prime Central London ("PCL") market has experienced a recovery after a prolonged period of stagnation due to COVID. Transaction activity has steadily increased since mid-July due to a combination of workers returning to their offices and relaxation of international travel restrictions. Key metrics were extremely encouraging with the number of new prospective buyers 27% above the 5-year average with offers and exchanges showing similar reassuring increases.

Demand for PCL property is heavily influenced by overseas investors and we retain a positive outlook for the remainder of the year now that prospective buyers can travel more freely.

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Source: Knight Frank, 2021

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PCL vs UK Housing

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PCL vs UK House Prices & Net Mortgage Lending

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Source: HIS Markit, Knight Frank, Bank of England, 2021
OUTLOOK

This has been another strong period of performance for commercial property driven mainly by extraordinary performance from the industrial sector due to an enduring acute supply-demand imbalance. Current inflationary concerns have been viewed as favourable for the asset class and money continues to target the attractive relative yields on offer. If the current trend continues, average yields may well surpass their historic lows in the coming months with only the prospect of rising UK interest rates able to slow the current rate of compression.

Industrial and income-focused properties will continue to lead the market in coming periods as the key factors driving these areas - e-commerce, supply chain disruption and premium income returns - remain firmly in place. Alternative sectors have had a mixed reaction to the pandemic but the fundamental case for investment in them has not changed and we anticipate a more favourable return environment now that restrictions have largely been removed.

The wider UK residential market will continue to cool over the course of H2 2021 after the removal of stimulus measures and the prospect of rising interest rates. By contrast, there is now a better outlook for the Prime Central London market which has found its floor after a long period of turbulence and we anticipate an accelerated recovery from this point onwards.

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