

## Valuation Advisory – December 2011

### Finance

- US Federal Reserve Rate at 0.25%.
- UK Base Rate unchanged at 0.5%.
- 5-Year Swap Rate 1.75% (Beginning November 1.93%). 10-Year Rate 2.53% (Beginning November 2.84%).
- Bank of England restarted quantitative easing with £75bn, another tranche of £50bn likely.
- Bank lending, 60% maximum, margins range from 225 basis points plus, depending on asset, borrower and LTV with imperative of interest covered by income. Margins increasing. Lending tight.
- European banking market struggling to maintain liquidity. US banks not co-operating so limited dollar funding impacting on trade, to be eased by “dollar credits” for European Banks from US Federal Reserve, The Bank of England, The Bank of China, Bank of Japan and ECB.
- Margin of LIBOR above Base Rate circa 54 basis points (LIBOR at 1.04).

### Economic View

- The FT 100 index at 5,505 up from 5,422 at the beginning of November. Very volatile. This compares to 5,538 this time last year.
- Inflation RPIX (excluding mortgage interest payments) at 5.6%, forecast to be circa 5.3% for 2011. CPI annual inflation – the Government’s target measure – was 5.0% in October. Upward pressures from increases in the cost of clothing, electricity and gas.
- Average Earnings growth (including bonuses) at 2.3% in year to September. (2.4% private sector and 2.3% public sector).
- Retail sales volumes increased by 0.6% over the last month, and the value of sales increased by 0.7%. Feedback from retailers suggests that the monthly increase in sales volume and value was a result of pre-Christmas sales and in store promotions.
- The seasonally adjusted index of services increased by 1.2 % in September 2011 compared with September 2010.
- UK Manufacturing PMI fell to 47.6 in November. Lowest level since June 2009. Lower production was linked to reduced new order inflows, weaker global and domestic market conditions and clients becoming increasingly reluctant to spend.
- Unemployment at 8.3% of workforce. Further rises are anticipated.
- Seasonally adjusted manufacturing output increased by 0.2% compared with August 2011, this is the first rise in four months.
- UK house prices increased by 0.4% in November. Price of a typical home is 1.6% higher than one year ago.
- Food Prices rise by only 5% in the year to October (6.4% to September), down from double digit rises earlier in the year.
- GDP growth forecast revised slightly downwards to 1.0% for 2011. Gross Domestic Product rose by 0.5 % in the third quarter (Q3) of 2011, driven by strength in the Services sector (in particular) and the Production sector.

## Property View

- IPD Total Returns for all Property in the 12 months to October 2011 8.7% (October 2011 8.7%). Total returns were driven almost exclusively by income return.
- IPD Total Returns for the sectors in the 12 months to October 2011 were: - **Offices 9.7%** (September 2011 9.8%) **Industrial 8.1%** (September 2011 8.1%), **Retail 8.0%** (September 2011 8.1%). Office continues to outperform driven by growth in London offices, particularly MidTown & West End.
- All rents index remained stable. (Offices up 0.14%, Industrial down 0.09% and Retail down 0.09%).
- Investment volume £27,095m in year to 31st November 2011. (Compared to £30,098mn in 2010).

## Sentiment

More investments being offered. Prices stable but buyers are fickle. Demand selectively competitive for quality assets London and South East, UK wide prime and good property. Buyers from Sovereign Wealth Funds, Germany, US, Middle East also UK private/"opportunity" fund/investors property companies, UK institutions buying selectively. More sales from Bank disposals/restructuring. IPD all property equivalent yield at the end of November 7.19%. Risk of tenant default and falling rental values/voids still having negative impact on secondary values still falling, likely to continue for foreseeable future.

## International

- US economy improving, new manufacturing orders up in November, PMI at 56.7. GDP forecast to grow by circa 2.0%. Unemployment 8.6%. GDP in 2012 forecast circa 2.5% to 2.9%.
- Brent crude stayed above \$110 at \$111, holding onto its previous session gains, as Iran's escalating tensions with the West and an agreement by euro zone ministers to ramp up the firepower of their bailout fund helped support prices.
- European GDP is forecast to grow by 1.6% in 2011. Fundamental need for a successful integration of "Euro Currency Zone".
- A proposed Financial Transactions Tax threatens competitiveness of Europe's Financial Centres. An attempt to impose a FTT on Britain would damage City of London's leading position in many world markets and banking income.
- GDP in Eastern Europe to grow by 4.3% in 2011.
- Japan's GDP now forecast a decline of -0.4% in 2011.
- Business improving across Asia, GDP growth forecast for 2011 of 4.7%.
- China world second biggest economy, overall 2011 GDP forecast 9.3%. Government using every means to bring down inflation. Slower manufacturing growth as stimulus package is wound down. Bank lending has been cut by over 15% so far this year.

## Jones Lang LaSalle Prime Yields

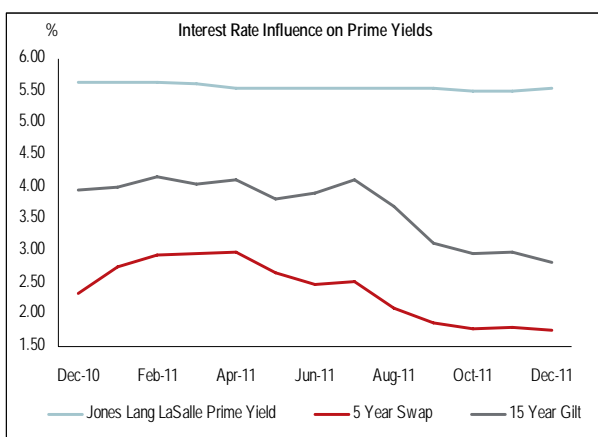
Sector	Yield	Movement since last month	Movement over last 12 months
<b>RETAIL</b>			
Prime High Street	4.75%	↔	↔
Regional High Street	5.75%	↔	↑
Food stores - Supermarkets	4.50%	↔	↔
Shopping Centre (regional dominant)	5.50%	↔	↔
Shopping Centre (secondary)	7.50%	↔	↔
Retail Warehouse, solus unit – Bulky	6.50%	↔	↔
Retail Warehouse (Open A1/Fashion parks)	5.00%	↔	↓
<b>OFFICES</b>			
City (lot size up to £40m)	5.25%	↔	↔
West End (£10m to £80m)	4.25%	↔	↔
M25 Towns Preferred	6.50%	↔	↔
Regional City Centre	6.00%	↔	↔
Business Parks – South East	6.75%	↔	↔
<b>INDUSTRIALS</b>			
South East Single Let	6.00%	↔	↓
Regional Single Let	6.75%	↔	↔
South East Multi Let	5.75%	↔	↓
Regional Multi Let	7.25%	↔	↔
<b>LEISURE</b>			
City Centre	7.00%	↔	↔
Out of Town	6.25%	↓	↓
<b>Jones Lang LaSalle Prime Yield</b>	<b>5.55%</b>	<b>↑</b>	<b>↓</b>
<b>MONEY MARKETS</b>			
Swap (5 year)	1.75%	↓	↓

Note: Yields are generated by Jones Lang LaSalle based on the latest evidence of deals by Jones Lang LaSalle and other agents. The prime yield series is a weighted yield (derived from capital values) based on individual prime yields.

Prime yield relates to well-specified, well configured Grade A stock let at a rack rent on a 10-15 years lease in a prime location to a strong covenant.

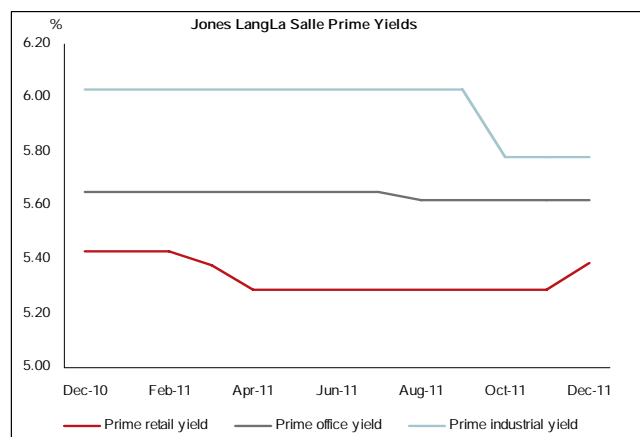
### Interest Rate Influence on Prime Yields

Source: Jones Lang LaSalle; Dalastream



### Jones Lang LaSalle Prime Yields

Source: Jones Lang LaSalle



There was outward yield movement across a number of sectors over the past month, including unit shops in market towns, town centre shopping centres and City offices between £40m - £125m. As a result, the Jones Lang LaSalle prime weighted yield softened by five basis points to 5.55%.

- International investors continue to dominate the City office market, attracted to London's 'safe haven' status. The UK institutions and PropCos are seeking value add and asset management opportunities. Despite the uncertainty London is still expected to outperform, with rental growth forecast towards 2015, driven by overseas capital and a diverse investor base. Prime yields for City offices with lot sizes of £40m - £125m and £125m+ both moved out by 25 basis points over the past month to reach 5.50%, whilst prime yields for City offices sub-£40m remained stable at 5.25% for a further month. Sentiment trended stable across all lot sizes.
- Within the West End office market, high net worth individuals are targeting smaller lots, whilst the larger lots available are being targeted by global sources of capital. Debt continues to be extremely hard to obtain, with deals taking an increasingly long time to complete. Whilst sentiment remains cautious, there has been no shift in demand. The market is thinner for larger lots but there has been no fall in pricing. Prime yields in the West End remained unchanged for a further month at 4.00% for lot sizes below £10m, 4.25% for larger lot sizes (£10m-£80m) and 5.00% for lot sizes over £80m. Sentiment continued to trend stable across all three groups.
- The spread between prime and secondary assets in the high street retail market continues to widen, with investors seeking 'best in class' units. Bank-led disposals of secondary assets are being packaged into portfolios to attract bidders; stand alone shops are struggling to attract attention. The institutions are seeking both unit shop and shopping centre lots, with assets in the South East that have affluent catchment areas experiencing competitive bidding. Prime yields for dominant shopping centres and prime unit shops remained stable for the seventeenth month running, at 5.50% and 4.75%. However, yields for unit shops in market towns moved out by 25 basis points to 6.00%, whilst pricing for shopping centres in town centres softened by 50 basis points to 6.50%. Sentiment trended weaker across all markets with the exception of regional shopping centres.
- The challenging conditions seen within the occupational market, namely retailer difficulties, are feeding though into the investment market. There has been a drop-off in demand for riskier assets, whilst US equity sources have been pulling out of the UK. A key deal this month was the sale of the Waitrose distribution centre in Milton Keynes to a domestic private investor, from Meghraj Properties. A price of £38.4m represented an initial yield of 6%. Jones Lang LaSalle acted for the vendor. Prime yields for both single and multi-let assets in the South East remained static at 6.00% and 5.75% in November. Sentiment trended stable across all markets.