

Quick Stats

Change from 2008

Take-Up	↓
Availability	↑
Prime Rent	↓
Capital Transactions	↑

OVERVIEW

Demand

- Logistics demand remained relatively healthy during 2009 with annual take-up reaching 12.5m sq ft compared with 14.3m sq ft in 2008. Tenants in the market were able to take advantage of the favourable terms being offered by landlords.
- Over the next 12 months, although a return to the excesses of 2006 and 2007 is not expected, the market is likely to experience a modest improvement in demand.

Supply

- Availability rose steadily during 2009 and at the end of December stood at 55.4m sq ft. The increase in supply was driven by the release of secondhand space onto the market.
- In contrast to the secondhand market, supply of new space is on a downward trajectory, spurred on by a dwindling development pipeline. By the end of the year a number of markets are expected to have significant constraints on supply of prime space.

Prime Rents

- With rising supply and weaker levels of demand, prime rents were under downward pressure in 2009.
- However, the outlook for prime rents is relatively optimistic, underpinned by activity in the design and build market which should help maintain prime rental levels.

Investment

- The first half of the year saw the investment market continue in a similar fashion to the latter part of 2008. However, by July, prime yields were showing signs of a sustained recovery and investor sentiment began to significantly improve. The year ended with a total of £1.4bn of investments, above the £1.31bn transacted in 2008
- Although there are still a number of ongoing concerns, the outlook for 2010 is that the investment market will begin to gather momentum.

UK Logistics Key Deals 2009

Address	Town	Size (sq ft)	Occupier
The Vault, Estuary Boulevard	Speke	618,800	B&M Retail
DC3, Prologis Park	Stoke-on-Trent	381,300	Marks & Spencer
G Space, 360 Eastgate Road	Runcorn	367,900	Eddie Stobart
Derby Commercial Park, Raynesway	Derby	361,000	Cyclamax
Radial 64	Washington	330,000	BAE Systems

Demand

At the start of 2009, the outlook for the logistics market was very pessimistic, with both landlords and tenants doing their best to cope with the challenging market conditions. As a result, leasing activity in the first two quarters was very low. Of particular significance was the retraction of the retail sector, a major source of demand for logistics space.

Although the annual total of 12.5m sq ft was the lowest since 2003, it is only 12% lower than the 14.3m sq ft let in 2008 which is a respectable performance in view of the severity of the economic downturn. Following the introduction of empty rates legislation there were a number of rate-saving deals where landlords offered their premises rent-free to avoid incurring the charges.

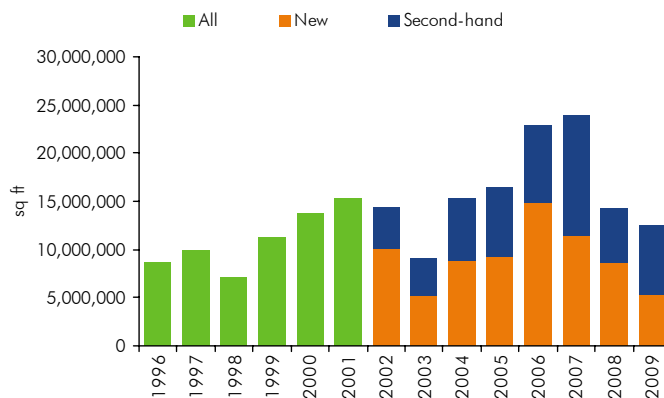
The largest deal of the year completed in Speke were B&M Retail bought the 618,800 sq ft freehold of The Vault on Estuary Boulevard. This compares with the top transaction from 2008 of 920,000 sq ft to WM Morrisons. An analysis of take-up by size shows that lettings for space in excess of 500,000 sq ft in 2009 accounted for only 4% of the total compared with 22% in 2008. This reduction in top tier lettings and the significantly smaller top deal for the year provides evidence that occupiers are taking a defensive approach to any potential relocations while remaining alert to any good opportunities on offer as a result of reduced occupational costs.

Buoyed by three lettings over 300,000 sq ft totalling over 1m sq ft, the West Midlands saw the highest proportion of activity in the UK, accounting for 26% of all space let. With five deals in excess of 200,000 sq ft, including a 367,000 sq ft letting in Runcorn to haulage firm Eddie Stobart, the North West had the second highest proportion of leasing activity, with a 19% market share.

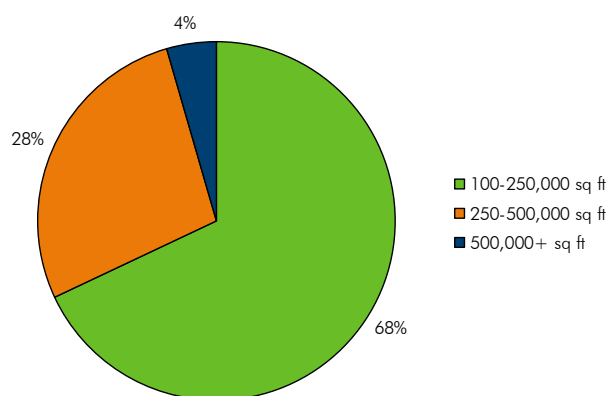
Going forward, waste companies are emerging as a new key driver of demand, with a number of lettings agreed during 2009 to companies such as Cyclamax and Biffa Waste. There are also a number of other anticipated deals in the pipeline. Increasing awareness of climate change is also creating a raft of other companies engaged in the green technologies sector that is fast becoming an important part of the UK logistics market.

At the end of 2009, the logistics market was undoubtedly in better health than at the end of 2008. Over the next 12 months, occupiers are likely to continue behaving cautiously in response to the ongoing economic problems. However, we are moderately optimistic that even though the peak conditions of 2006 and 2007 will not be repeated, 2010 will see a steady improvement in market sentiment and activity.

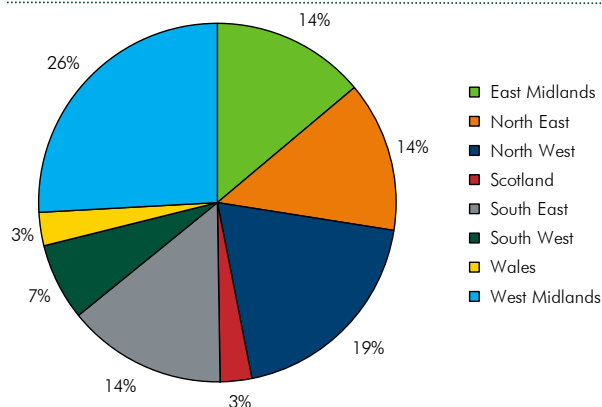
Take-up by Quality



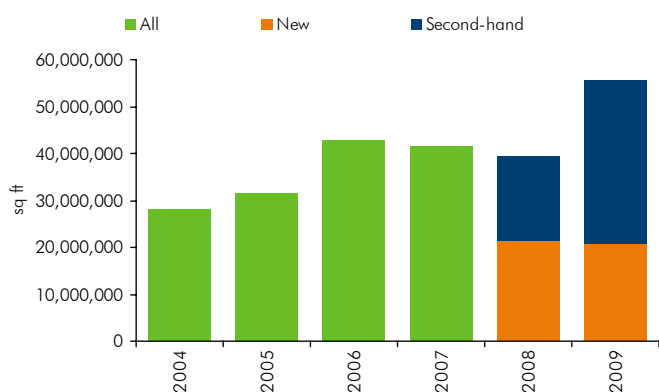
Take-up by Size



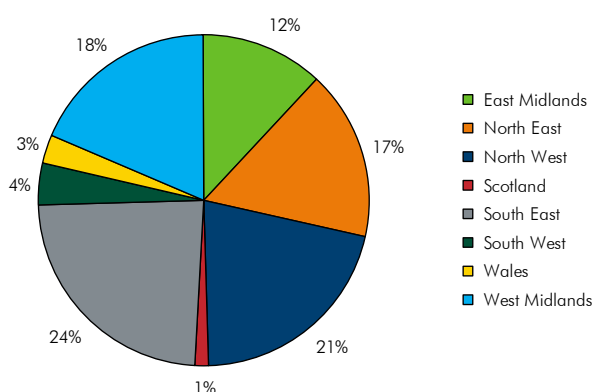
Take-up by Region



Availability by Quality



Availability by Region



Key Availables

Address	Town	Size (sq ft)
Ivatt Way	Peterborough	1,075,000
Plot 2, East Midlands Distribution	Castle Donnington	814,000
Flair, G. Park	Rugeley	697,700
666 Sherbern Distribution Park	Leeds	666,900
The Big Ram, Dorcan Industrial Estate	Swindon	612,700
Crossflow 530	Barnsley	530,100

Availability

At the end of the fourth quarter, availability in the UK stood at 55.7m sq ft, having steadily increased throughout 2009. In view of the subdued level of demand going into the year, the completion of any remaining developments still under construction and most importantly the unexpected collapse of key occupiers such as Woolworths and MFI, it was inevitable that supply would increase in 2009.

The principal catalyst of the increase in availability was a sharp rise in the volume of secondhand space on the market. During the course of the year it rose to 34.9m sq ft as both tenants and landlords released unwanted space back onto the market. A high proportion of this secondhand space is of poorer quality. In contrast, supply of new space registered a marginal decline from 21.4m sq ft to 20.6m sq ft.

Another major characteristic of the current supply picture is that despite the presence of a eight very large units (500,000+ sq ft) in the UK, the most prevalent type of unit on the market ranges from 100,000 – 250,000 sq ft. Units within this size bracket represent over 50% of the total. Occupiers with imminent lease events that require the acquisition of a substantial volume of space will find their options becoming increasingly limited going forward.

From a regional perspective, the South East accounts for the highest proportion of supply with a 24% market share. However, both the North West (21%) and the West Midlands (18%) also have a fairly substantial market share.

Although secondhand space dominates the supply picture, one of the most notable characteristics is that early marketed space (under construction and within 12 months of completion) stands at only 2.7m sq ft, accounting for under 5% of overall availability. With no speculative development activity expected over the next 12 months, it is likely that some regions will have very low levels of new space by the end of the year. Birmingham and Manchester, for example, already have no units in excess of 200,000 sq ft available. Furthermore, there are a number of imminent deals in the South East which will significantly reduce options for large existing units in the region.

Rather than undertake risky speculative development, in the current climate developers are aiming to develop new premises on their land banks on a design and build basis. This will further exacerbate any potential undersupply that may emerge during 2010. Until we see a sustained improvement in the availability of debt-finance, and a rebalancing of the supply and demand situation, speculative development will not be viable.

Prime Rents

Prime rents and incentive packages were under downward pressure throughout 2009 as landlords competed for occupiers and at the end of the year the logistics market was very much favouring the tenant. Occupiers undertaking lease re-gears were in some instances able to secure a reductions of up to 15%. However, by the end of the year, such significant reductions were becoming increasingly uncommon. On new leases, tenants were being offered with 12 months rent free for every five year commitment.

The outlook for prime rents remains largely positive. The shortage of supply in some areas is likely to result in an increase in design and build schemes which command higher occupational costs that should help support headline rental values. In contrast secondary rents are likely to suffer as a result of the high volume of supply on the market.

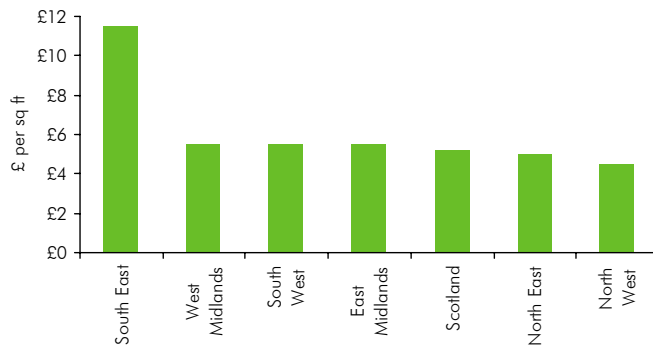
Investment

In 2009, £1.4bn was invested in the distribution warehouse market, compared with a similar total of £1.31bn in 2008. The year was very much a tale of two contrasting halves, with the poor sentiment that characterised 2008 prevailing until June. In the second half of the year, as prime yields showed signs of a sustained recovery, there was a widespread improvement in investor sentiment led by the retail funds who enjoyed a reversal of fortunes from redemption pressure to large cash inflows.

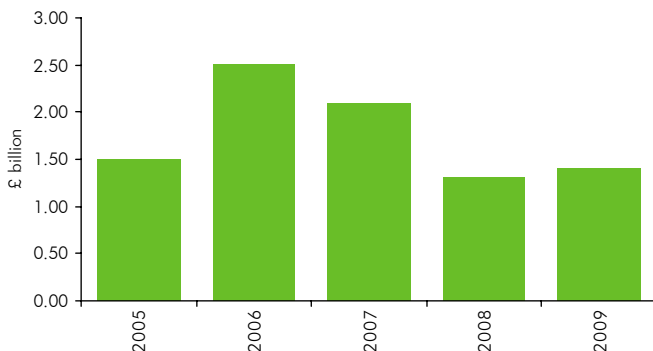
Investment activity in 2009 was largely concentrated in Southern England, with both the South East and Greater London each taking a 26% share of total transactions. UK Institutional investors emerged as key buyers in the latter part of the year, and were ultimately responsible for nearly half of all transactions in 2009. In contrast, overseas investors, who were very active in the first half of the year and helped build the recovery's momentum, were ultimately overshadowed by the strong re-emergence of the UK Institutions and ended up with a 29% market share.

Throughout the year, the majority of investors focused their attention on defensive stock characterised by long leases to strong covenants, avoiding more risky secondary assets on the back of residual concerns about the underlying health of the occupational market and the lack of available debt for this type of investment. This created a significant level of competition that caused prime yields to trend downwards, resulting in the emergence of a two-tier market in which the yield gap between prime and secondary assets increased to a historic high of 450 basis points.

Logistics Prime Rents – Q4 2009

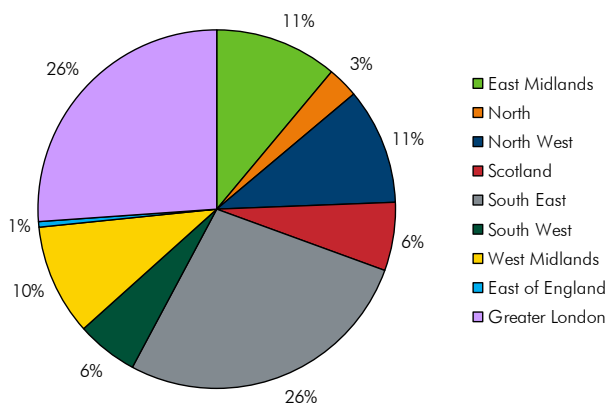


Logistics Investment Transactions



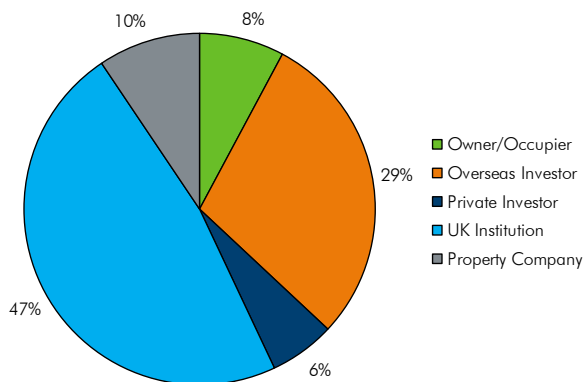
Source: CB Richard Ellis/Property Data

Investment by Region



Source: CB Richard Ellis/Property Data

Investment by Purchaser



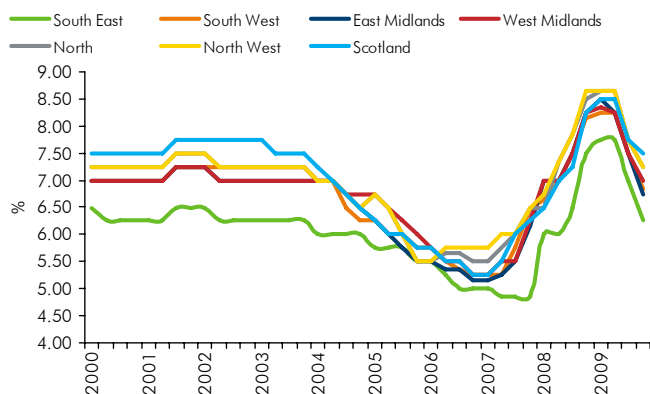
Source: CB Richard Ellis/Property Data

Key Transactions

Address	Town	Purchaser	Price/Yield
WM Morrisons G.Park	Sittingbourne	WM Morrisons	£80m – Freehold Sale
Brixton Portfolio	Heathrow, Feltham, Greenford	AEW Europe	£70.25m/ 7.60%
Sainsbury's, Waltham Point	Waltham Abbey	Deka Immobilien	£68.41m/ 7.50%
Prologis Portfolio	Hemel Hempstead, Northampton, Thurrock	Harbert Management Corporation	£64.4m/ 8.89%
Iceland, Innova Park	Enfield	Aegon	£32.88m/ 5.84%

Source: CB Richard Ellis/Property Data

Logistics Prime Yields



By the end of the year, competition for prime assets and an acute shortage of supply led some investors to turn their attention towards 'good secondary' assets. An example is F&C Commercial Property Trust's purchase of a portfolio of three distribution warehouses on the well-established Hams Hall Distribution Park in Birmingham for £34.8m, reflecting a net initial yield of 9.00%. The three units total 617,200 sq ft and had an average weighted unexpired term of 6.45 years.

Another consequence of the unprecedented compression of prime yields was that a number of investors who bought in late 2008 and early 2009, at historically low levels, opportunistically offered these properties back to the market in an attempt to crystallise their profits and take advantage of the high level of demand and lack of stock. Probably the best example of this is the Iceland unit at Innova Park in Enfield. The property was purchased in December 2008 for £24.5m, reflecting a net initial yield of 7.60%, and in December 2009 was re-sold for £32.88m, reflecting a net initial yield of 5.84%.

Prime yields began to stabilise in the final weeks of 2009, and if the high level of demand for prime assets continues, then over the next 12 months we may see some further yield compression for the very best properties. This yield compression may also begin to be felt in the secondary market, with investors who are deterred by the competition for the limited prime stock becoming increasingly attracted by the higher yields available.

Turning to future supply, the severe lack of stock that characterised the market over recent months could change if yields continue to harden. Vendors may become increasingly willing to bring stock to the market to take advantage of the favourable market conditions for disposals. Also worth considering when looking forward at potential supply levels is the UK banks who continue to work through their property loan books and are involved in the ongoing process of balance sheet adjustment. The market is waiting to see whether this will translate into more sales, such as the Pascal Portfolio that was brought to the market by the Royal Bank of Scotland. The portfolio was purchased, with debt provided by the Royal Bank of Scotland, in a joint venture between Rockspring and IO Asset Management for £27m, reflecting a net initial yield of 13.50%.

The weight of money entering the market has meant that the underlying occupational concerns have largely appeared to have been ignored during the recent market recovery. This continued uncertainty within the occupational market could also finally begin to temper any further yield compression. The continued lack of stability within the wider economy could also have repercussions in both the occupational and investment markets.

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