

Property Data Report 2013



Introduction

This document sets out some key facts about commercial property, a sector that makes up a major part of the UK economy in its own right, as well as providing a platform for virtually all the country's other major industries. It is a sector that plays a crucial role by providing places in which people can work, shop and enjoy leisure activities. Larger than the banking, leisure, communications and transport sectors, commercial property is also a significant investment asset for the pensions industry, and so contributes to the financing of retirement.

This latest *Property Data Report* has been fully updated but now includes, for the first time, additional information on the economic and fiscal contribution of commercial property to the overall economy and national Exchequer. This builds on the inclusion last year of new sections on the level of property debt and the sustainability of the commercial property sector, thus helping to provide a more rounded picture of the industry.

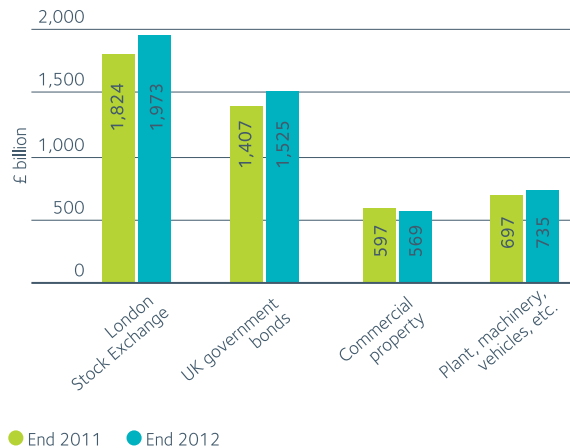
It has been produced by the Association of British Insurers, the Association of Real Estate Funds, the British Council for Offices, the British Council of Shopping Centres, the British Property Federation, the Investment Property Forum, the Royal Institution of Chartered Surveyors and the Urban Land Institute. All eight bodies are members of the Property Industry Alliance, which seeks to achieve a more co-ordinated and effective approach from leading property bodies on policy, research and best practice issues.

1 Commercial property by comparison

Commercial property primarily comprises the core sectors of retail, office and industrial (warehousing and factories). Cinemas, leisure parks, hotels, pubs, garages and petrol stations are also seen as commercial property.

The value of commercial property in 2012 declined to £569 billion. This compares with £597 billion in 2011, an estimate revised since last year's *Property Data Report* in the light of new research (see back notes for further explanation).

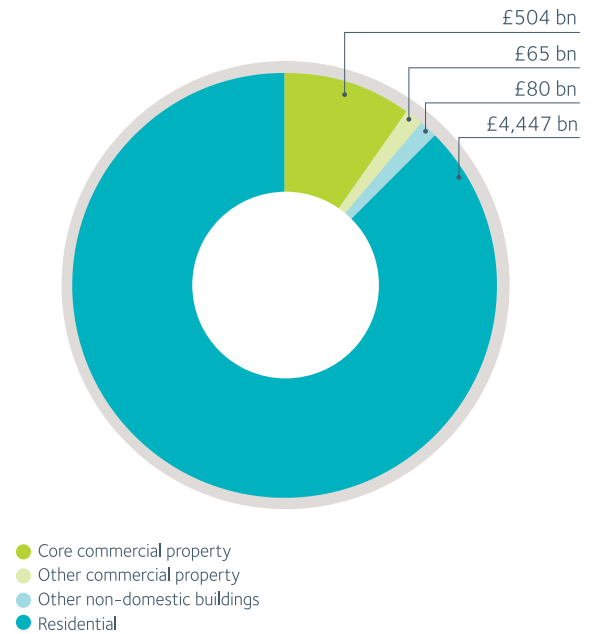
Commercial property is an important factor of production and is nearly as large as the country's stock of plant, machinery and vehicles.



Commercial property's value is around a third of that of government bonds and about 30% of UK equities. In contrast to commercial property, where prices fell by about 4.5%, the prices of both the equity market and government bonds rose in 2012, with bonds further inflated as the government issued more bonds to finance its budget deficit.

2 Overview of the commercial property sectors

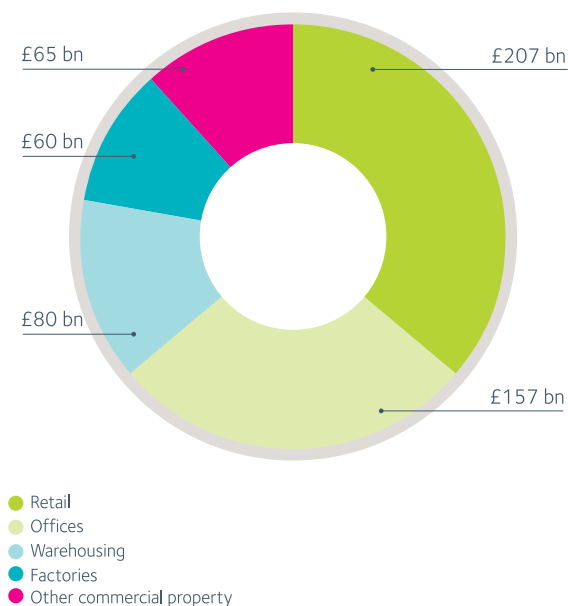
'Core' commercial, comprising retail, office and industrial property, dominates the commercial sector. The 'other commercial property' sector – leisure, hotels, pubs, car showrooms and petrol stations, etc. – is small by comparison.



Residential property far outweighs every other UK asset class including commercial property. Its value is almost eight times that of commercial property. The 'other non-domestic buildings' category includes public buildings, such as schools and hospitals.

3 The main commercial property sectors

Retail property, with a value of £207 billion, is the largest commercial property sector. This compares with 2011's revised estimate of £220 billion (see back notes for further details of the revision).



Offices are the second largest sector, with a value of £157 billion, compared with 2011's revised estimate of £163 billion. Hotels and pubs are the largest part of the diverse 'other commercial property' sector.

4 Commercial property sectors: a detailed look

Having accounted for less than a fifth of retail in 1993, the value of out of town retail property is now comparable to that in town centres. Retail warehouses and parks – typically located out of town – are the largest type of retail property.

DISTRIBUTION OF INVESTMENT VALUE OF COMMERCIAL PROPERTY IN 2012 AS MEASURED BY IPD

SEGMENT	% OF TOTAL
Central London shops	4
Rest South East shops	3
Rest UK shops	4
In town shopping centres	12
Out of town shopping centres	5
Retail warehouses and parks	17
Other retail (including food stores)	6
City of London offices	4
London West End offices	13
Rest South East offices	7
Rest UK offices	4
London and South East industrials	10
Rest UK industrials	6
Leisure	2
Other commercial types	4
TOTAL	100

SEGMENT	% OF TOTAL
All town centre retail	25
All out of town retail	25
Central London offices	16
All central London commercial property	21

Having seen strong capital value growth and relatively high levels of new development since 2010, central London offices account for well over half the value of offices in the UK.

5 Renting versus owning

Two thirds of commercial property is rented, compared to a little more than a third of housing. For commercial property, this is the same as last year's newly revised rented proportion (see back notes for further details of the revision).



The proportion of commercial property that is rented has grown over the last decade. This is because many businesses have become increasingly reluctant to commit the capital and management time required of owner occupation. More owner occupiers took advantage of high prices in the mid-2000s to participate in 'sale and leaseback' deals.

6 Renting commercial property: leases

The average length of a new lease continues to reduce and in 2011 was less than five years, compared to 8.7 years in 1999.

AVERAGE LENGTH OF NEW LEASES (YEARS)* 2011

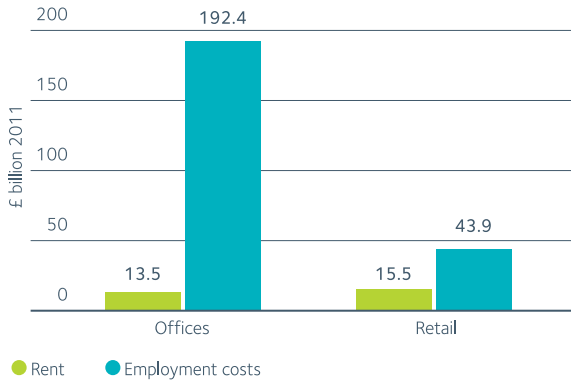
All	4.8
SMEs	4.1
Large companies	5.2
Retail	5.5
Offices	4.5
Industrials	3.5
Proportion of new leases 1-5 years long	76%
Proportion of new leases with break clauses	33%
Average rent free period (months)	8.8

* including exceptional licences and short leases and the effect of break clauses

Over three quarters of new leases now have durations of five years or less. Larger tenants, occupying bigger units, have relatively long leases. Many tenants benefit from rent free periods at the beginning of a lease. Retail warehouses, where demand from tenants has been relatively strong, have the longest leases and industrials the shortest.

7 Commercial property as a business cost

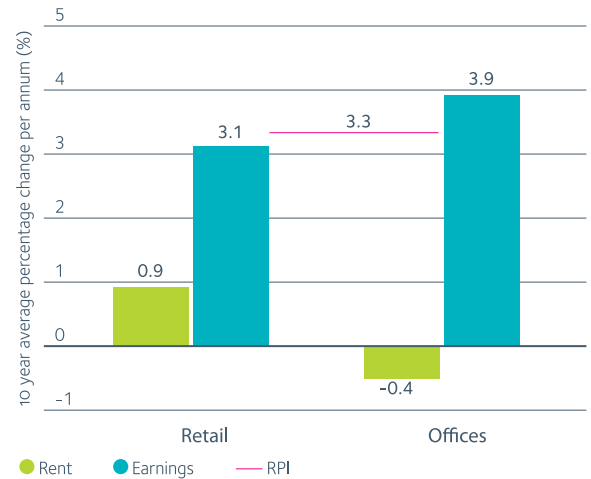
Office rents, at £13.5 billion, are very low (7%) relative to the staff costs of occupiers. By contrast, the rental costs of retailers, at £15.5 billion, are a third of the level of staff costs.



Even so, the rental costs borne by retailers represent a small fraction (about 5%) of their turnover.

8 Rents as a business cost: inflation

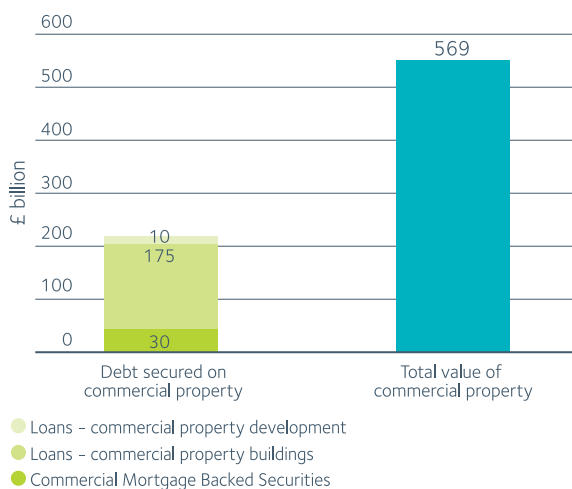
Rents, other than in central London, have been on a downward trend since 2008. While rents for offices in central London increased during each of the last three years, office rents generally are lower than 10 years ago. Inflation in retail rents has been muted. Although under pressure recently, salaries of shop and office staff over the last 10 years have broadly kept pace with, if not exceeded, inflation.



The rise in the cost of utilities, at almost 10% per annum over the last 10 years, has far outstripped inflation in rents, wages and retail prices.

9 Commercial property lending

Many occupiers and investors buy commercial property using a combination of debt and their own capital. While property values ended the last decade at the same level as they started, the use of debt increased fivefold between the end of 1999 and 2009. However, the value of outstanding loans has been falling since late 2009. Approximately £215 billion of debt is currently secured on commercial property (including developments), a fall of £20 billion over the year. The amount of debt represents two fifths of the total value of commercial property.



Most debt finance is still provided by traditional lenders such as banks. However, the banks have been reducing some types of commercial property lending. At the same time, non-traditional lenders, like insurance companies, have increased their lending capacity as margins have increased and loan to value ratios have reduced, thus improving returns and lowering risk. Investing in commercial property debt is also appealing to insurance companies, as well as to hedge funds, private equity and sovereign wealth funds, on account of the perceived attractive returns compared to direct equity investment.

10 Investors in commercial property

UK institutions – responsible for personal long term savings and pension plans – are still the biggest owners of commercial investment property. They directly own almost a quarter of the total, although their share is continuing to decline. Overseas investors are fast approaching the UK institutions as the biggest single category of owner and, as in the UK equity market, are set to become the largest owners. Overseas investors already own more than half the offices in the City of London, according to Development Securities' 2012 report *Who Owns the City*.

DIRECT OWNERSHIP OF UK INVESTED COMMERCIAL PROPERTY 2012

TYPE OF OWNER	£BN	% CHANGE 2003-12	% OF TOTAL
UK institutions (insurance companies and pension funds)	78	-4	22
Overseas investors	76	106	22
Collective investment schemes	68	127	20
UK REITs and listed property companies	50	38	14
UK unlisted property companies	38	3	11
Private investors	12	50	3
Traditional estates/charities	13	0	4
Other	13	8	4
TOTAL	348	37	100

Ownership by collective investment schemes (managed funds, property unit trusts, limited partnerships, etc.) has also grown substantially, reflecting increased interest in the asset class from smaller institutional and retail (individual) investors and overseas institutions, as well as a shift in personal savings habits towards unit trusts. Most of the capital invested in UK commercial property is used to provide pensions and savings for UK households.

11 The UK's institutional investors and commercial property

UK commercial property accounts for almost 5% of the £2.5 trillion invested by insurance companies and pension funds. Having stabilised earlier this decade, property's share fell marginally in 2012, as a result of property values weakening at a time when the prices of other asset classes were rising. This fall happened in spite of the fact that, in 2012, institutions put additional investment into property, particularly in collective investment schemes.

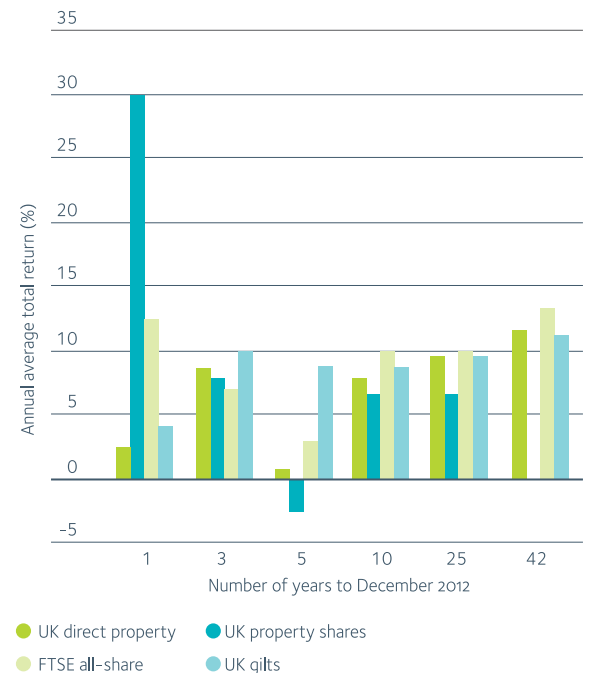
INSURANCE COMPANY AND PENSION FUND EXPOSURES TO PROPERTY IN RELATION TO THEIR TOTAL ASSETS

	2009		2012	
	£BN	% OF TOTAL ASSETS	£BN	% OF TOTAL ASSETS
TOTAL ASSETS (EQUITIES, BONDS, PROPERTY, ETC.)	2,170	100	2,450	100
Directly owned UK property	68	3.1	78	3.2
Investments in collective investment schemes (estimate)	29	1.3	38	1.6
Total property	96	4.4	116	4.7
UK and overseas property company and REIT shares (estimate)	na	na	36	1.5

Most large pension funds invest in property but only a small proportion of the smaller ones do so. However, investment amongst the smaller funds has grown as investing in property has become easier, for example through collective investment schemes, which now account for a third of institutions' investment in commercial property.

12 Commercial property investment performance

Directly owned commercial property total returns moderated to 3.3% in 2012, a markedly poorer performance than a resurgent equity market, but only slightly less than gilts. The performance of property company shares has been a lot more volatile than directly owned property, with their spectacularly strong performance in 2012 partly offsetting very negative returns during the height of the financial crisis.



Over the longer term, commercial property's performance, at 10.7% per annum since 1971 (IPD's earliest data point), sits between those of gilts and equities. This ranking is in line both with surveys of investors' longer term expectations, and with the historic pattern of risk – commercial property being less volatile than equities but more volatile than gilts.

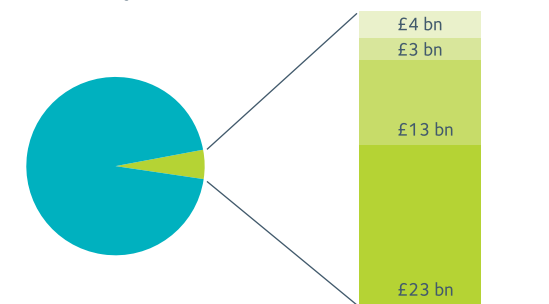
13 UK commercial property: economic contribution

The commercial property industry contributes to the economy in many ways. It is a significant part of the UK's economy, employing nearly 900,000 people.

The commercial property industry directly contributed about £42 billion to the UK's GDP in 2012, accounting for 3% of the national total. This is comparable to the combined size of the country's telecommunications and transport industries, highlighting its importance to businesses' and people's everyday lives.

COMMERCIAL PROPERTY INDUSTRY GROSS VALUE ADDED 2012 VERSUS WHOLE ECONOMY

Whole economy £1,383 bn Commercial property £42 br



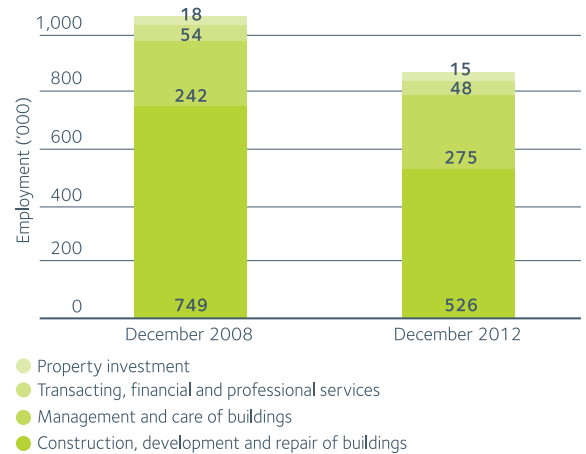
- Property investment
- Transacting, financial and professional services
- Management and care of buildings
- Construction, development and repair of buildings

Most activity involves the construction, development, repair, care and management of buildings. The property investment sector (investment and fund management, REITs and property companies) is a small but high value added part of the industry, and the largest in Europe. It generates around £250,000 value added per employee – six times the average for the economy as a whole.

14 UK commercial property: change in economic contribution

The commercial property industry has been amongst the worst of those areas affected by the recession, shedding 200,000 jobs since December 2008 and seeing a full percentage point drop in its share of national GDP. Only publishing and civil engineering have seen comparably proportionate falls in employment. Economic activity and employment continued to decline in 2012, in contrast to the rest of the economy.

EMPLOYMENT IN THE COMMERCIAL PROPERTY INDUSTRY BY TYPE OF ACTIVITY – 2008 VERSUS 2012

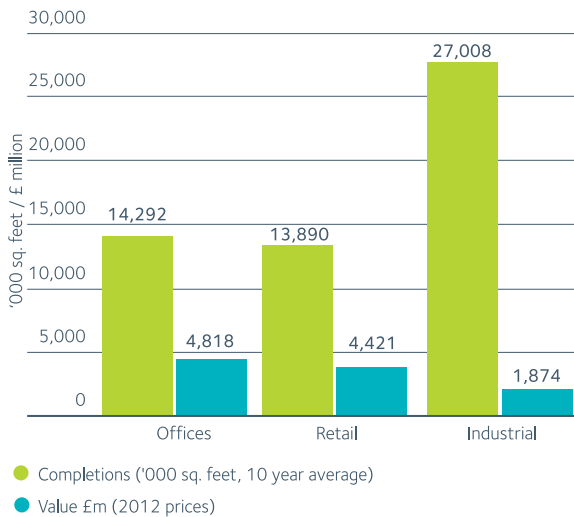


Property investment (hit by reductions in rental income and fund management fees) and commercial construction (with a 30% decline in jobs since 2008) have been the worst affected areas of activity.

The UK economy is extremely sensitive to changes in commercial construction. A recent report for the Investment Property Forum, *The Role of Commercial Property in the UK Economy*, found that a £1 fall in commercial construction leads to an overall fall of £2.09 in the economy as a whole, meaning that the deep recession in the commercial property sector has dampened the national recovery.

15 The commercial property industry: regeneration

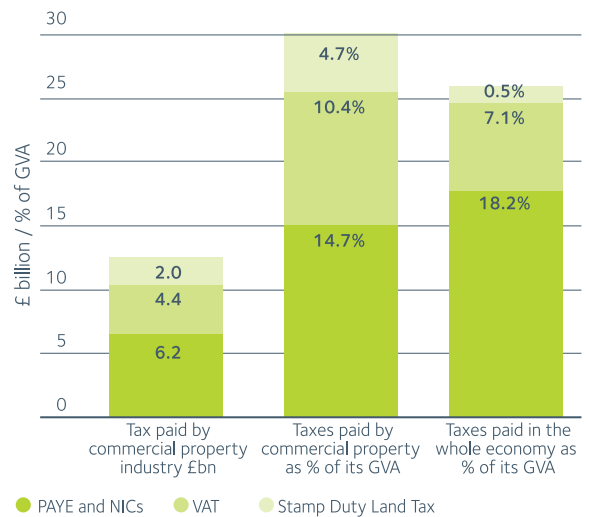
The UK commercial property sector on average adds over 50 million square feet of new space every year. This has an investment value of around £11 billion – about 1% of the UK's GDP. While the footprint of new development in the industrial property sector is high, the value of retail and office development is much greater.



New development has been affected badly during the global financial crisis. Property Market Analysis reports that completions of both retail and office space in 2012 were less than a third of the level recorded in 2008.

16 Taxes paid to the Exchequer

The commercial property industry is taxed directly and indirectly in a variety of ways. The contributions from some of these taxes – including Stamp Duty Land Tax, National Insurance contributions, VAT and PAYE – can be calculated with reasonable accuracy and are illustrated below. For these taxes, the commercial property industry's contribution is broadly in line with its share of the nation's GDP.



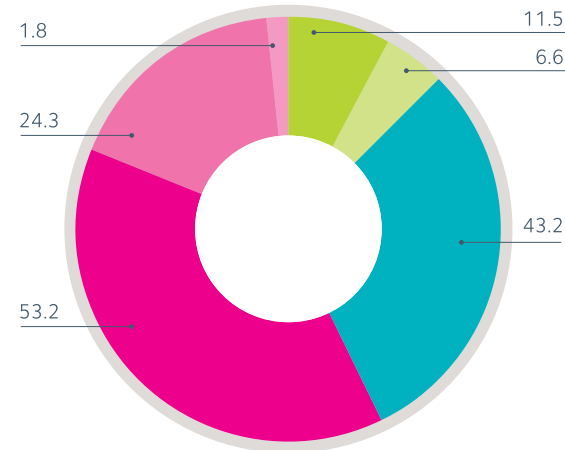
Other taxes directly paid by the industry, ranging from Corporation Tax to rates on empty property and the Community Infrastructure Levy, are much harder to assess.

In addition, occupiers of commercial property paid £20 billion in business rates, some of which will effectively be borne by property owners through lower rents.

17 Energy consumption

Commercial property buildings, excluding factories, and the activities within them, account for about 8.25% of the UK's energy consumption. Other non-domestic buildings – for example schools and hospitals – add about 4.75% to this. Transport and domestic uses are by far the largest sources of energy consumption.

ENERGY CONSUMPTION BY END USER, MILLION TONNES OIL EQUIVALENT 2012



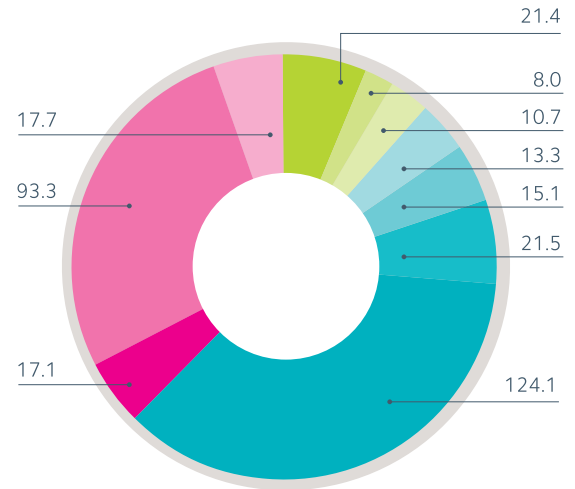
- Activities in commercial property (excluding industry and transport and distribution)
- Activities in other non-domestic property
- Domestic consumption
- Transport
- Industry (including factory buildings)
- Other

Energy consumption in commercial, other non-domestic, and residential buildings all increased in 2012, having fallen the year before. Weather conditions are responsible for much of this variation.

18 CO₂ emissions

About 15% of CO₂ emissions are directly and indirectly (i.e. emitted in the production of power) associated with commercial buildings. Retail outlets are the biggest single contributor within the commercial sector. Overall, housing and transportation account for the majority of emissions.

MILLION TONNES CO₂ EMISSIONS BY BUILDING TYPE/END USE 2011



- Retail
- Office
- Warehouse
- Industrial
- Other commercial
- Other non-domestic
- Domestic
- Transportation
- Industrial processes
- Other

Residential and, to a lesser extent, commercial and public sector buildings represent one of the most important untapped potential sources of energy savings and reduced greenhouse gas emissions.

Commercial property is primarily made up of the core sectors of retail, office and industrial (warehousing and factories), which dominate investors' portfolios. Cinemas, leisure parks, hotels, pubs and restaurants, garages and petrol stations are also seen as commercial property. Commercial property activity covers those organisations whose main business is the construction, development, design or care and management of buildings, the fund management, investment management or asset management of investment property and transacting (e.g. investment and letting agency). The contributions made to commercial property by the legal and property banking sectors are also included.

Restatement of the commercial property stock estimates for 2011 presented in the 2012 *Property Data Report*

The commercial property stock and total rental values estimates for 2011 presented in the 2012 *Property Data Report* have been revised following detailed new work for the Investment Property Forum as part of its *Size and Structure of the UK Property Market* research (to be published Q1 2014). In particular, the yields used to derive commercial property's capital value have been revised upwards compared to the previous assumptions in the *Property Data Report*; the approach used to estimate rental values has also led to downward revisions.

The 2011 estimates for the total and core commercial property stock, and similarly for retail, offices, warehouses and factories in sections 1-3, have all been affected, as have the estimates for retail and office rental values in section 7. The estimate of the amount of commercial property that is owner occupied, used to estimate the rented and owner occupation proportions in section 5, has also been affected; this is because it is calculated as the residual of the total commercial stock and the (unrevised) stock of investment property.

The table below shows the restated estimates for 2011:

	£ BN
Retail value	220
Office value	163
Warehouse value	84
Factory value	62
Total core commercial property value	529
Other commercial property value	68
TOTAL COMMERCIAL PROPERTY VALUE	597
Other non-domestic buildings value	81
Retail rental value	15.9
Office rental value	13.8
Share of commercial property that is rented	66%


Sources

- 1 The property figure is a Paul Mitchell Real Estate Consultancy update of IPF report *The Size and Structure of the UK Property Market (2005)*. Plant and machinery from the Office for National Statistics 2013 *Blue Book*, government bonds from the Debt Management Office, and equities from the London Stock Exchange.
- 2 Paul Mitchell Real Estate Consultancy update of IPF report *The Size and Structure of the UK Property Market (2005)*; residential property is Office for National Statistics 2013 *Blue Book*.
- 3 Paul Mitchell Real Estate Consultancy update of IPF report *The Size and Structure of the UK Property Market (2005)*.
- 4 Investment Property Databank Ltd © 2013.
- 5 Paul Mitchell Real Estate Consultancy update of IPF report *The Size and Structure of the UK Property Market (2005)* with the owner occupied stock estimated as the residual of the total stock and the investment stock, and, for housing, the Department of Communities and Local Government's Table 101 *Dwelling Stock by Tenure*.
- 6 British Property Federation: *IPD Annual Lease Review 2011*.
- 7 Paul Mitchell Real Estate Consultancy estimates. Rental payments derived from Valuation Office April 2012 rateable values updated from their April 2008 base date to December 2012 by IPD rental growth; employment costs derived from the Office for National Statistics (retail relates to SIC(2007) 47 less non-store trade, offices to SIC(2003)s J and K).
- 8 Rental growth from Investment Property Databank Ltd © 2013; earnings derived from the Office for National Statistics' *Monthly Wages and Salaries Survey*. RPI from the Office for National Statistics.
- 9 Paul Mitchell Real Estate Consultancy estimates using information from De Montfort University's *The UK Commercial Property Lending Market 2012 Year End* report.
- 10 Paul Mitchell Real Estate Consultancy update of IPF report *The Size and Structure of the UK Property Market (2005)*, based on data gratefully received from DTZ, Investment Property Databank, Property Funds Research and Real Capital Analytics.
- 11 Paul Mitchell Real Estate Consultancy estimates for 2012, updated using 2011 data from the Office for National Statistics *Investment by Insurance Companies, Pension Funds and Trusts*.
- 12 Investment Property Databank Ltd © 2013, FTSE.
- 13 Paul Mitchell Real Estate Consultancy estimates mainly based on the Office for National Statistics' data on employment and Gross Value Added. General approach is to apportion employment and GVA in property as a whole between commercial and non-commercial. The two main industry sectors are Construction (SIC(2007) Section F) and Real Estate Activities (SIC(2007) Section L) for which Gross Value Added is available, respectively, from the ONS's *Blue Book* and its *Annual Business Survey*. For construction, the ONS's *Output in the Construction Industry* Tables 4 and 5 indicate that around 25% of construction output is related to commercial property sectors. For the Real Estate Activities sector, the indicators used vary according to the specific sector (for example, commercial property's share of total property transactions is applied to SIC68.31 'Real Estate Agencies'); overall about two fifths of the Real Estate Activities sector (excluding the imputed rent of owner occupiers) is estimated to be commercial real estate. Part of SIC(2007) Section K (Financial and Insurance Activities) is incorporated for commercial property; this covers property banking, fund management, REITs, stock broking, insurance companies and pension funds. For these areas, estimates of employment relating to commercial property are mainly derived from a survey of company accounts and from fund managers' websites (grossing these up to the industry as a whole through the relationship between employment and funds under management), while GVA for REITs, fund managers, etc. is also based on company information relating to employment costs and profits, defined to be consistent with the national accounts measures of Gross Value Added. SIC(2007) Section M (Professional, Scientific and Technical Activities, mainly relating to legal services, architecture, and quantity surveying), and SIC(2007) Section N (Administrative and Support Service Activities, mainly relating to facilities management). In these sectors, commercial property's share and size tends to be small.
- 14 As above.
- 15 Paul Mitchell Real Estate Consultancy estimates derived from estimates of 10 year average floor space completions gratefully supplied by Property Market Analysis, and also Department of Communities and Local Government data and from 2012 investment values of completed development.

- 16 Draws on the approach outlined in the IPF's *The Role of Commercial Property in the UK Economy*. Based specifically on HMRC Tax Statistics and relates to the commercial property industry as defined in section 13. Total taxes derived from May 2013 *HM Revenue and Customs receipts*. PAYE, NIC and VAT for commercial property estimated from the corresponding HMRC estimates by broad industry, pro-rated according to commercial property's share of these industries. SDLT estimated by pro-rating HMRC estimates for non-residential according to the Paul Mitchell Real Estate Consultancy's estimate of commercial property's share of non-business property transactions.
- 17 Paul Mitchell Real Estate Consultancy estimates derived from the Department of Energy & Climate Change's statistics on energy consumption by final user 2012 and earlier data published by BRE.
- 18 Paul Mitchell Real Estate Consultancy estimates derived from the Department of Energy & Climate Change's statistics on estimated emissions of carbon dioxide by end user category 2011 and earlier data published by BRE.

Acknowledgements

Data compiled and estimated by Paul Mitchell Real Estate Consultancy Ltd (www.p mrecon.com). Supporting property market data gratefully received from Investment Property Databank, Property Funds Research, Property Market Analysis and Real Capital Analytics, none of whom bear any responsibility for the estimates in this document.



September 2013 | Design by Anderson Norton Design 020 7336 6992