COVID-19
INDUSTRIAL & LOGISTICS MARKET UPDATE

DTRE LEASING & INVESTMENT
APRIL 2020

A DECADE OF
2020 DTRE | LEASING & INVESTMENT

RESEARCH

The COVID-19 pandemic has had a catastrophic and debilitating effect on all economies and markets across the globe. From China in the East across to the USA, seemingly no nation will be left untouched by the virus, but aside from the obvious health warnings, how else will COVID-19 affect the markets and particularly property, moving forward?

It's all changed in such a short space of time. Just a few weeks ago the forecasters, ourselves included, were suggesting another strong year for industrial and logistics, with sentiment moving in the right direction, albeit a Brexit shaped cloud was on the horizon for later in the year.

Now? The idea of Brexit seems a lifetime ago. Q2 2020 will see some unprecedented numbers and we should all be aware of this, but we should not be despondent, and, of all the property sectors, it is industrial and logistics that is best placed to weather the storm.

The structural changes that were already underway might have been accelerated by the impact of COVID-19. The trend towards flexible and home working may be hastened, primarily impacting the office sector. Social distancing may speed up the decline of high street retail and leisure activity, whilst, conversely, the relentless rise of ecommerce, which has driven logistics market growth in recent years, may be given further impetus.

COVID-19 has already caused online's share of retail sales to surge to new highs, as consumers stay at home and opt to shop online in response to stock shortages in supermarkets or on the high street, where non-food retailers have been forced to close their doors.

Back to the nitty gritty and occupier-wise, decisions are likely to be put on hold. The result being that take-up this year will suffer. Average 5-year take-up of Big Boxes over 100,000 sq ft is currently 29m sq ft, but we are forecasting for demand to drop by around 20% and take-up to reach only 23m sq ft, albeit this would be twice the level of take-up we witnessed in 2009.

At a time of such uncertainty, secure long-income producing industrials represent something of a safe-haven for many investors, and whilst the rental growth story is likely to be put to the back burner for this year, once the crisis passes there will be potential for growth.

Whilst our forecasts below are at the 'All Property' level, it is expected that retail, particularly the high street and shopping centres will bear the brunt of the impact to values.

For all the macro reasons people are already aware of, mainly the rise and rise of e-commerce, industrial and logistics is well placed to weather the COVID-19 pandemic and bounce back in a relatively strong position and we once again anticipate industrial and logistics to be the best performing sector in 2020, just not quite at the levels we expected a few weeks ago.

Latest UK All Property Forecasts - April 2020

	2019	2020	2021
Rental Growth (% y/y)	-0.6	-3.2	2.4
Equivalent Yield (%)	5.6	5.9	5.8
Capital Growth (% y/y)	-3.3	-9.4	4.9
Total Return (% y/y)	1.2	-4.6	9.8

Source: Capital Economics/MSCI

LEASING MARKET

The leasing market has diverged post the COVID-19 lockdown, with surges in demand testing logistics supply-chains to their limit, whilst Government direction on rent payments has left holes in cashflows and created uncertainty.

So far we have not witnessed substantial leasing activity as a direct consequence of the COVID-19 pandemic. The supermarkets are widely reported as seeking substantial additional space, however our analysis suggests that these requirements have been satisfied by using 'grey space' across their existing network or by re-occupying units that have been marketed on a sublease/ assignment basis. The absorption equates to approximately 2.8m sq ft of accommodation.

This activity from the supermarkets has certainly reduced availability in the market, as over 1.2m sq ft of marketed accommodation is no longer available and won't be available again for an unknown period of time.

However, our analysis suggests there is approximately 5m sq ft of warehouse accommodation that is currently occupied by 'at risk' businesses. Unfortunately, we are going to see further administrations over this period of 'lock down' and there is the potential for this to quickly provide a net increase in warehouse supply.

At the smaller end of the spectrum our experience of the multi-let sector is that government subsidies and landlord concessions on rent payments have so far limited the amount of accommodation returning to the market. Looking beyond the limited examples of businesses experiencing a spike in demand, the majority of tenants have seen a reduction in business. The strain on business balance sheets is expected to be worst in the urban locations where rents reflect a premium.

Across all size ranges landlords have their eyes firmly fixed on quarterly rental income, with many grappling to collect from impacted tenants. Although we are also hearing that several landlords are having lease extension and 're-gear' dialogue with their customer.

There is the potential for substantial short-term take-up of warehouse accommodation nationwide from the MOD and NHS. Over the course of the next few weeks it is likely that there will be a further reduction in immediately available accommodation, as the government implements its emergency strategy for managing the COVID-19 pandemic.

Finally, looking at the market from a longer-term perspective it is undeniable that there will be a substantial change in our shopping habits once the pandemic subsides and our research suggests this is likely to generate further demand for warehouse accommodation.

Examples of retailers moving back into their grey space

	Unit	Sq Ft
Tesco	MW300 Stakehill (existing unit)	300,000
	Fenny Lock, Milton Keynes (existing unit)	617,000
Sainsburys	Maidstone DC (existing unit)	233,000
	Grey space at Shire Park Worcester (existing unit)	370,000
Waitrose	Chorley (existing unit)	45,000
Aldi	Grey space	1,200,000
Lidl	Weston Super Mare (existing unit)	315,000
	Total	**3,080,000**

INVESTMENT MARKET

The industrial sector, both single and multi-let, has produced outstanding performance over recent years, not only in terms of real estate but also when compared to other asset classes. Investors have continued to compete aggressively for stock given strong fundamentals. The main driver has been the potential to capture sustainable rental growth enabled by a market dynamic well supported by the structural shift and continued evolvement of the UK's e-commerce sector. Although the last two weeks will have seen a significant change to that momentum.

Despite the ongoing political and economic uncertainty, investor appetite for multi-let industrials remained buoyant in Q1 2020. It's been the lack of investment opportunities which has frustrated buyers, who were anticipating a spike in sales following the Conservatives winning a majority.

This uptick didn't materialise, with our data indicating Q1 '20 investment volumes were approximately 20% below the Q1 '19 levels. In the coming weeks, we do not anticipate many new opportunities to be openly marketed, with vendors opting to drive returns through active asset management initiatives rather than selling multi-let holdings.

There are still a number of leasing transactions progressing across the multi-let sector, which in turn are increasing the rental tone and long term returns for those assets.

Investors have been reiterating the message to us since the outbreak that they remain focussed on the sector. This is best illustrated at scale by two c. £200M lot sizes, with Perivale Industrial Estate, West London and Trafford Park, Manchester both being hotly contested by a significant depth of buyers with strong prices agreed. We note that Perivale Industrial Estate has been reported as withdrawn from the market for the time being.

Below we provide a summary of current multi-let transactions and available opportunities, whilst overleaf we detail a summary of single-let transactions and opportunities.

Multi-let: Sold

Address	Area (sq ft)	Tenure	AWUTC	No. of Tenants	Price	NIY	Price psf
***Sands Ten IE, High Wycombe**	132,440	Freehold	5.10	5	£21.65m	4.71%	£163
***Westgate 40, South Ruislip**	130,364	LLH	6.80	12	£29.60m	4.04%	£249

* Deal agreed prior to 23rd March

Multi-let: Under Offer

Despite the high-level of uncertainty and effective economic 'lockdown' since the outbreak of the virus we have not witnessed a high proportion of abortive transactions. In most cases, in our experience, both sides remain engaged and are looking to work in partnership to find solutions and progress the necessary due diligence. The main obstacle being the ability to carry out on-site surveys, which we expect will temporarily stall some transactions until the current social distancing measures are loosened.

Address	Area (sq ft)	Tenure	AWUTC	No of Tenants	Quoting	NIY	Price psf
Units 1-12 Warner Drive, Braintree	27,376	Freehold	3.92	8	£3.365m	5.50%	£123
Schooner Park, Dartford	27,380	Freehold	4.96	7	£5.20m	6.00%	£190
Vaughan Park, Tipton	81,198	Freehold	4.04	4	£9.17m	5.75%	£113

Multi-let: Available Assets

DTRE are actively monitoring over £300m of MLI opportunities. We are happy to discuss this with you, but some openly marketed estates include:

Address	Area (sq ft)	Tenure	AWUTC	No of Tenants	Quoting	NIY	Price psf
Units 4-7, Stretton Business Park, Burton-upon-Trent	43,489	Freehold	2.00	2	£3.90m	6.75%	£90
Bowthorpe Park Industrial Estate, Norwich	245,730	FH & LH	4.08	44	£20.72m	6.00%	£84
Brunel Park, Chippenham	48,824	LLH	4.90	5	£4.66m	6.50%	£95

INVESTMENT MARKET

The on-going COVID-19 lockdown will impact levels of trading and change the appetitie for risk among investors, but, long-dated income will remain an attractive proposition in an uncertain world. The single-let market, particularly long income deals of 15 years plus, secured to strong covenants, with inflation linked increases having been the most aggressively sought over the past twelve months and we would anticipate this continuing.

Single-Let: Sold

We are aware of the following deals which have completed since the outbreak became more serious in the UK.

Address	Tenant	Area (sq ft)	AWUTC	Price	NIY	Price psf
Boulevard Industrial Estate, Speke, Liverpool L24 9JW*	AstraZeneca	219,619	13.2	£20.76m	5.50%	£95
150 Yeats Close, Wembley, NW10 0BN*	Selco	45,300	11.6	£16.10m	3.57%	£355
Welwyn Garden City*	Hertfordshire County Council	122,500	5.9	£23.00m	4.19%	£188
Aston Lane North, Whitehouse Industrial Estate, Runcorn WA7 3BN*	DHL	650,313	5.25	£34.89m	5.50%	£53

* Deal agreed prior to 23rd March

Single-Let: Under Offer

The primary obstacle slowing the sales process over this period has been conducting inspections. Pre bid inspections as well as surveys have been prevented by the introduction of social distancing measures put in place by companies and the government. We have however seen a number of deals have been agreed since the introduction of more strenuous countermeasures by the government, as outlined below.

Address	Tenant	Area (sq ft)	AWUTC	Quoting	NIY	Price psf
Blackpole Road Trading Estate, Worcester WR3 8YB	Arrow XL	258,334	21.0	£22.50m	6.25%	£87
Harrier Park, Hucknall NG15 6EU	RM Educational Resources	195,644	15.0	£19.90m	5.33%	£102
Foxbridge Way, Normanton WF6 1TL	Unipart	153,473	16.7	£11.28m	6.00%	£73
Stratton Business Park, Biggleswade SG18 8XP	CEF	214,431	22.0	£18.11m	4.05%	£84
Units 1&2, Gelder Road, Leeds LS12 6BE	Clipper	90,464	3.7	£7.15m	6.00%	£79

Single-Let: Available Assets

DTRE are currently monitoring 24 available single-let units, totalling over £265m. For more information, please get in touch with one of the Industrial Investment Team

Address	Tenant	Area (sq ft)	AWUTC	Quoting	NIY	Price psf
Midpoint 18, Middlewich CW10 0LE	Wincanton Ltd	373,947	3.9	£27.20m	6.25%	£72
Middlemarch Business Park, Coventry CV3 4PB	World of Books	104,170	13.25	£13.20m	4.61%	£127
Normanton Industrial Estate WF6 1TN	Kongsberg Automotive	63,642	9.1	£6.46m	6.00%	£101

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