M&G REAL ESTATE REVEALS ‘POST-ARTICLE 50’ OUTLOOK

- ***Varying short-term rental growth prospects for different sectors***
- ***Private rented residential and industrial sectors boast ‘strong’ short-term rental growth***
- ***Central London offices market set to be most impacted by ‘Brexit uncertainty’***

LONDON, 30 March 2017 – With the UK having formally triggered the Brexit process, M&G Real Estate, one of the world’s largest property investors, has issued an updated outlook for UK commercial property markets.

M&G Real Estate states that commercial property capital values are currently rising because rental growth has remained positive and because yields have been hardening again following the weakening seen last summer.

However, a very different picture emerges for different parts of the market. Buying interest is concentrated on prime assets, investors are still avoiding secondary stock and yields on these riskier assets continue to face upwards pressure.

Similarly, M&G Real Estate reports that there is rental growth within prime property, but far less so for secondary, with rents still declining for many weaker assets.

Strong short-term rental growth prospects for selected sectors:

Residential Private Rented Sector

- continues to boast a ‘strong’ short-term rental growth outlook due to an acute shortage of purpose-built residential rental housing, particularly in Greater London and South East England
- the slowdown in house buying activity, resulting in more people in rented accommodation, will boost rents
- reduced EU migration is likely to ease the shortage only marginally

Industrial and logistics

- ‘strong’ short-term rental outlook with demand driven by the continued evolution of online retailing and the low supply of space, particularly in the South East of England, gives further support to rents

Regional Offices

- faces a 'fairly strong' outlook for prime assets located in city centres; rental growth potential reduced a little for markets with higher concentration of financial services companies
- sector to benefit from the push for regional growth by government
- rents to be supported by tight Grade A supply

Central London offices

- likely to experience 'weak' short-term rental growth
- segment likely to be the most impacted by Brexit uncertainty given its exposure to financial services
- offices outside of the prime Central London core will be more resilient

Retail

- 'fair' short-term rental outlook
- polarisation between 'good' retail assets such as dominant shopping centres with leisure offerings and 'bad' retail assets such as high street shops in oversupplied second tier towns

For UK commercial property in general, M&G Real Estate believes that investment is supported by a wide spread of yields above bonds, as well as an improvement in the relative value of the UK compared to other property markets around the world. Furthermore, it states that foreign investors can continue to take advantage of sterling's depreciation to acquire UK assets cheaply.

Richard Gwilliam, Head of Property Research at M&G Real Estate, says: "The triggering of Article 50 merely confirms what everyone was expecting and, while it sets in motion a potentially volatile process, the UK economy is resilient and likely to continue growing despite Brexit uncertainty.

"Buoyed by robust rental fundamentals, the UK commercial property market has already begun to recover from declines seen last summer. However, ongoing risk aversion related to Brexit uncertainty is likely to cause further weakening of non-core assets, effectively making them cheaper. Central London offices are most vulnerable to weakening over the short term – but volatility may present buying opportunities later."

Amongst buyers, M&G Real Estate reports enthusiasm from Middle East, Asian and US investors, with appeal boosted by cheap sterling. It states that domestic investors are seeking selective opportunities and UK local government funds are taking advantage of low borrowing costs to buy commercial property around the country.

It adds that retail investor funds are still receiving a large number of off-market approaches and that there is particular interest for assets with strong income and/or alternative use.

On the seller side, M&G Real Estate notes that retail investor funds have completed the majority of their required selling to fund redemptions and rebuild liquidity levels, although outflows are continuing – albeit at a slower, more manageable pace.

Richard Gwilliam concludes: "With no evidence of forced selling and little appetite for sellers to accept heavily discounted prices, there is limited pressure and little desire from institutional investors to sell in the current market."

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Notes to Editors:

About M&G Real Estate

M&G Real Estate is the real estate fund management arm of M&G and is one of the top 25 real estate fund managers in the world by assets under management, with over £26 billion invested in a broad spread of properties across Europe, North America and the Asia Pacific region (as of 30 December 2016). M&G Real Estate has a sector leading approach to responsible property management, and is committed to assessing and improving the sustainability performance of funds under management.

M&G is the investment arm of Prudential Plc in the UK, Europe and Asia. For more information please visit www.mandg.com/realestate

About M&G

M&G is an international active asset manager, investing on behalf of individuals and institutions for over 80 years. As of 30 June 2016 the firm manages over £255 billion of assets through a wide range of investment strategies across equities, bonds, property and multi asset.