BREXIT AND UK REAL ESTATE

House View

December 2018

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Brexit outcome still highly uncertain

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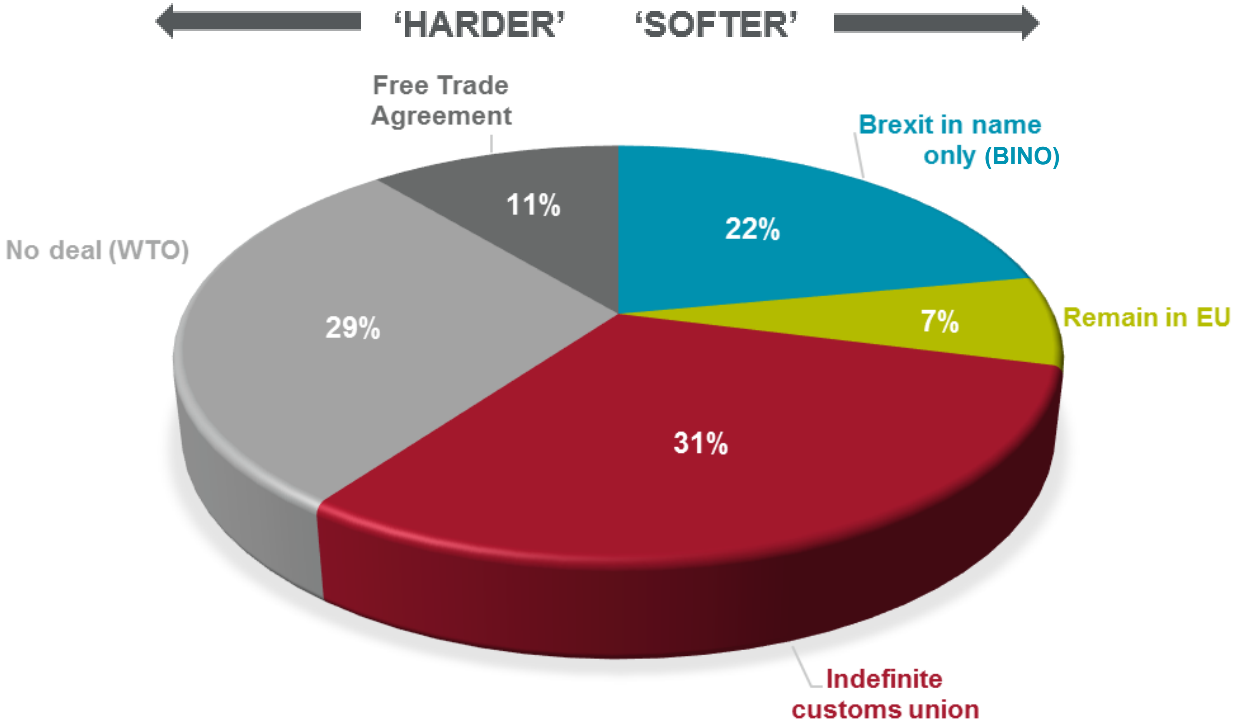
December 2018
- House of Commons “meaningful vote”

January / February 2019
- Deal passed into UK law

March 2019
- EU ratification

29 March 2019
- Brexit day

April 2019 to December 2020
- Trade talks & transition



Brexit Scenarios: Probabilities for the Ultimate Deal

Source: Oxford Economics

- The withdrawal treaty is now agreed but still a long way from any degree of certainty as the Brexit timeline shows.
- It looks unlikely that the Brexit withdrawal agreement will be approved by the UK parliament on the first vote.
- Further intense uncertainty is likely while hard-line ‘leavers’ and ‘remainers’ push to change course in the hope of forcing a general election or another referendum.
- This is separate to the ultimate trade deal where negotiations are yet to even start, despite the draft political declaration on the future relationship given alongside the withdrawal treaty.

Economic growth prospects vary significantly according to Brexit scenario

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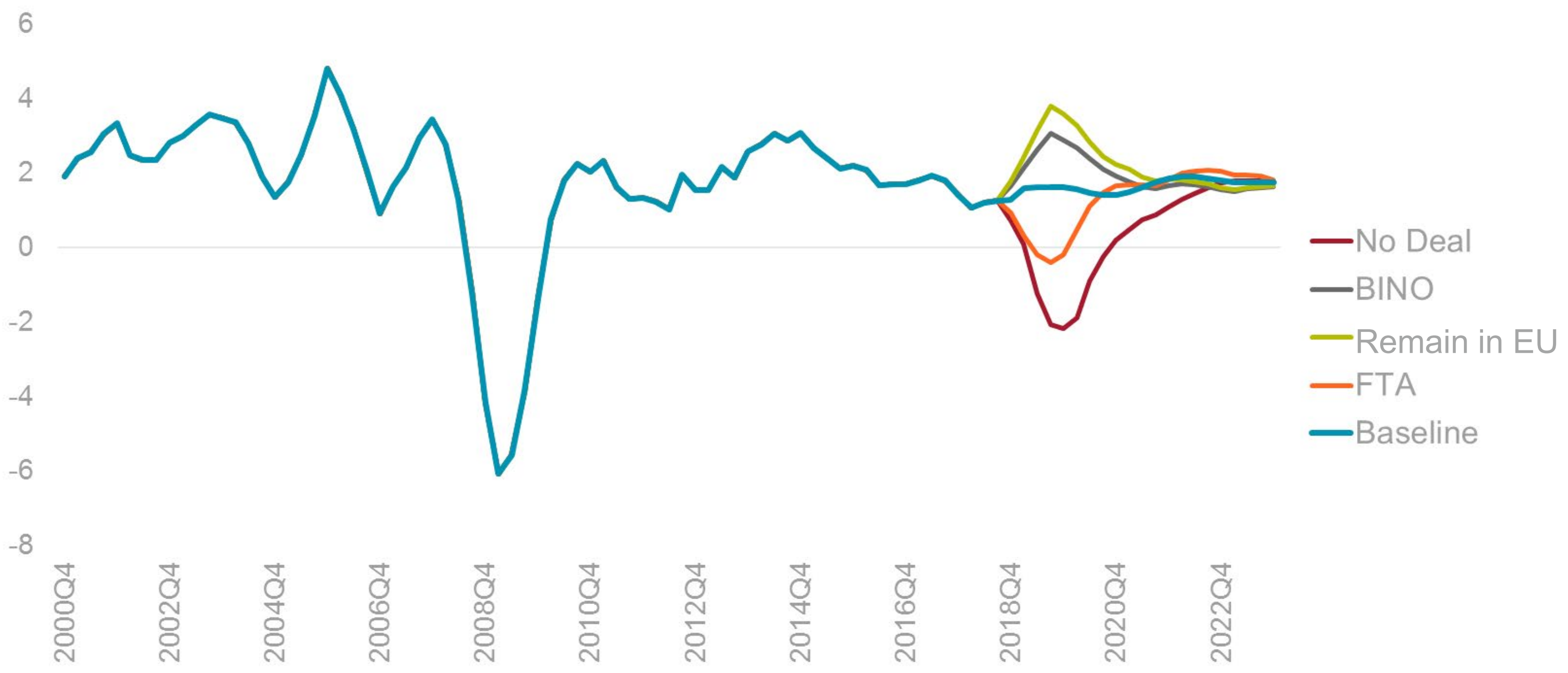
Brexit scenario's: Impact on UK GDP



Source: Moody's Analytics

- This chart shows just how varied the outlook for the UK economy still is, depending on which Brexit path the UK follows.
- There is a massive 6% spread between the best and the worst scenarios for economic growth next year
- The best scenario for the economy is judged to be 'Remain in the EU' which could see growth of nearly 4% in 2019.
- While the worst scenario is 'No Deal' estimated to result in a recession with GDP falling by 2%.

House view on Brexit and the UK economy

Cushman & Wakefield's third party provider of economic data and forecasting is Oxford Economics. Our property market forecasts utilise those national and local level economic forecasts alongside our in-house real estate market data.

Short term	Medium term	Long term
Oxford Economics do not expect that the Brexit withdrawal agreement will be approved by the UK parliament on the first vote. Further intense uncertainty is likely over the coming months until March 2019.	The EU is unlikely to offer major changes to May's proposed deal, so if an election or second referendum are not achievable, then it is likely that the withdrawal agreement will be passed on a second vote as the least worst option available.	The withdrawal agreement will keep the UK in a customs union until it can be superseded by the new trading arrangement. The probabilities of the ultimate deal broadly balanced at this point.

- There is a massive 6% spread between the best and the worst scenarios for economic growth next year. The best scenario for the economy is judged to be 'Remain in the EU' which could see growth of nearly 4% in 2019 while the worst scenario is 'No Deal' estimated to result in a recession with GDP falling by 2%.
- Assuming the base case, outlined above, the UK economy is set to grow by 2.0% per annum over the next 5 years, compared to 2.1% over the 5 years prior to the referendum.
- Employment is also set to increase despite record low unemployment rates and a tight labour market, with 1.3m new jobs created over the next 5 years, down from 2.9m over the 5 years to 2016.
- Interest rates are set to rise reaching 2.75% by end 2023, from a low of 0.25% in 2016, and following the policy normalisation already underway since 2015 in the US.

OFFICE

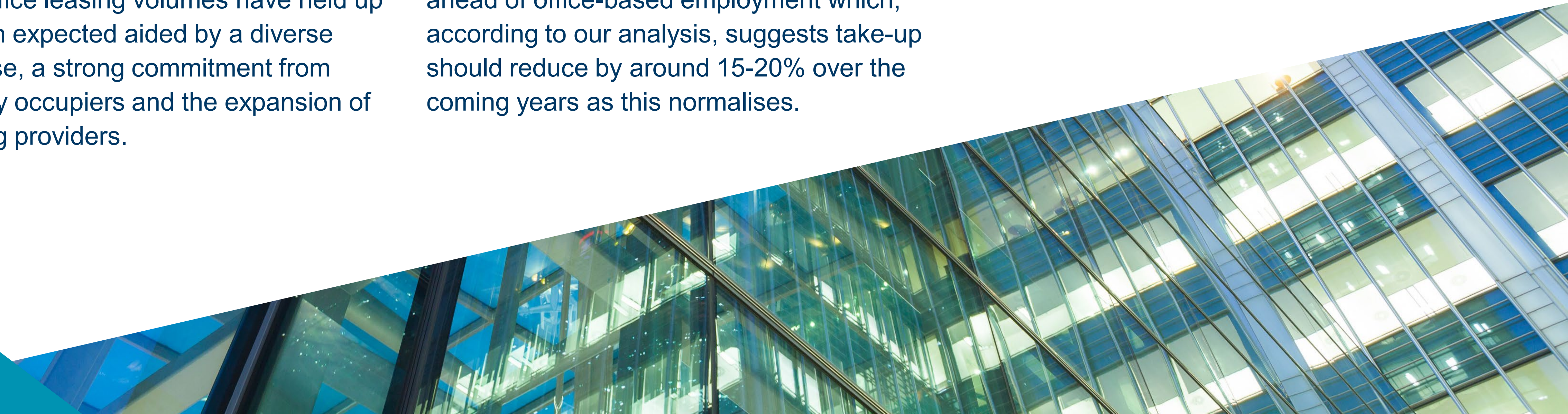
In the property market since the referendum, there has been an acute focus on the London office market due to the importance of finance & banking, the high number of European and global companies and the significance of EU nationals to the job market.

London office leasing volumes have held up better than expected aided by a diverse tenant base, a strong commitment from technology occupiers and the expansion of co-working providers.

Outside of London, leasing activity has also been very healthy with quarterly take-up in 2018 running 30-40% ahead of the 10 year historic average. Activity has been driven by banking & finance, professional services and the government property unit (GPU).

However, UK office take-up has moved ahead of office-based employment which, according to our analysis, suggests take-up should reduce by around 15-20% over the coming years as this normalises.

Prime rental growth for UK offices is expected to remain positive overall. We are most optimistic on cities where there is a strong digital and technology industry base. Our forecasts are less optimistic for markets acutely exposed to financial services given the uncertainty Brexit poses to office based employment in this sector.



RETAIL

Challenges in the retail sector are largely structural as online sales growth reduces the need for physical retail space. However, there is also a cyclical component to the weakness, stemming from lower overall consumption.

Our forecasts focus on the best high street locations in the UK which have strong footfall and benefit from tourism, therefore have the lowest risk of disruption.

Prime UK high street retail rental growth is expected to remain positive over the forecast period (2019-23), but considerably slower than the 5% p.a. recorded over the last 10 years.

Our outlook for shopping centres is more challenged, and we expect headline rents for the majority of centres to weaken with inducements also increasing.

The level of rents and amount of floor space are uneconomic for many bricks and mortar retailers. For this reason, we expect an adjustment in rents across many segments of the retail market.

On the investment side, retail is expected to be the weakest performing sector in 2019.

LOGISTICS

The logistics sector continues to be a strong sector, benefitting from supply chain reconfiguration in order to service a larger share of online retail sales and the demand for faster delivery.

Rents are rising nationally as occupier demand is strong, largely driven by retailers and online operators looking to optimise their distribution networks. Urban logistics units are in exceptionally high demand.

Brexit-related stockpiling is driving up the cost of short-term space in UK warehouses, as companies across the country guard against a no-deal outcome that could cause gridlock at ports and chaos in cross-border trade.

Logistics rental growth is forecast to be positive over the next 5 years. In some markets, record rental levels have spurred a supply response, including speculative developments.

Logistics exposure has been highly sought after by investors, for a number of years, and yields have compressed to all time lows.

Industrial yields (IPD) now sit below retail and office for the first time ever. This is a remarkable data point for the sector long regarded as the highest yielding of all property types.

CAPITAL MARKETS

We are at an advanced stage of the property cycle, this is the ninth year of continuous UK prime capital value growth eclipsing the 1990s upswing which lasted 8 years. Prime yields have remained low for a prolonged period with aggressive pricing for the best assets.

A weight of capital remains focused on the UK, particularly from cross border investors (US, South Korea and China). Notwithstanding this, YE 2018 UK investment volumes are likely to be down on 2017 (our estimates are c. 10-15%), largely driven by the retail sector.

A strong rebound in investment volumes is possible next year if there is a reduction in Brexit related uncertainty – a relief rally - and the avoidance of a ‘no deal’ scenario.

Our central case is that rising interest rates will lead to a re-pricing across all asset classes including real estate. Our view is that yields have broadly bottomed out and will increase over the next few years, but with a lag to the expected movement in gilts.

We are forecasting modest rental growth and outward yield shift leading to a more challenging environment for investors looking for value.

Prime total returns are expected to be driven mainly by income return with investors focused on sustainable rental growth.

Total returns for logistics are still expected to be better than retail or offices.

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Cushman & Wakefield (NYSE: CWK) is a leading global real estate services firm that delivers exceptional value by putting ideas into action for real estate occupiers and owners. Cushman & Wakefield is among the largest real estate services firms with 48,000 employees in approximately 400 offices and 70 countries. In 2017, the firm had revenue of $6.9 billion across core services of property, facilities and project management, leasing, capital markets, valuation and other services. To learn more, visit www.cushmanwakefield.com or follow @CushWake on Twitter.