Ryden

79th Scottish Property Review

OCT/16

100 Queen Street, Glasgow

Scotland's slow economic growth through 2015 and early 2016 was attributed mainly to the weakened oil and gas industry. The economy is still growing and the unemployment rate has fallen, but the UK vote to leave the European Union has led forecasters to dampen their expectations for growth through 2017 and 2018, as inflation increases and uncertainty acts as a drag on business investment.

The property markets did react negatively to Brexit, although post-Summer there is some recovery in occupier markets. These continue to perform very differently by city and sector, as reported in the detailed market reviews. Uncertainty in the investment markets due to Brexit is confounded by the possibility of a second Scottish Independence Referendum.

DR MARK ROBERTSON, PARTNER

Economy

The Scottish economy slowed during 2015 and into 2016. Economic activity in Q2 2016 was 0.7% higher than in Q2 2015. During the second quarter of this year, overall economic growth rose to 0.4%.

The dominant services sector grew by 0.5% and the production sector grew by 0.3%, but overall growth was held back by contraction in the construction sector (-1.9%) as major public sector infrastructure projects neared completion.

The most recent Bank of Scotland Purchasing Managers' Index rose to a 14-month high in September (PMI = 51.2), ending a two month period of contraction which had followed the Referendum vote in June to leave the EU.

The Scottish unemployment rate for the three months June to August 2016 was 4.6%, the lowest level since 2008 and below the UK rate of 4.9%. EY's Item Club reporting in October 2016 suggests that UK unemployment will rise markedly next year to 6.0% by the end of 2017 as consumers face price inflation and businesses take a cautious approach to investment, both as a result of the EU Referendum vote.

The table opposite indicates that recent significant employment creation is in the engineering, technology and retail sectors across Scotland. Retailing has also recorded job losses and employment in the oil and gas industry continues to contract.

The Insolvency Service reports a total of 258 company insolvencies in Scotland in the second quarter of 2016; this is up by 15.7% on the same period in 2015, and is more than the 226 company insolvencies recorded in the first quarter of 2016.

According to the Scottish Government's Retail Sales Index for Scotland, sales grew by 0.2% during the second quarter of 2016, and by 3.2% on an annual basis. This is lower than the 3.9% recorded in Great Britain over the same 12-month period. More recent data from the Scottish Retail Consortium states that total retail sales in Scotland were 0.6% lower over the 12 months to September 2016. Although marginally negative, this performance reflects a slowing of the decline in sales and growth is positive (+1.1%), if price deflation is removed. Mixed retail data appears to be the norm now in an era of multi-channel sales and differential performances across locations and operators. The Scottish retail property market is reviewed on pages 14 and 15.

According to the Department of Energy and Climate Change, indigenous production of crude oil was 0.4% higher in the second quarter of 2016 compared with the same period in 2015. On a quarterly basis however this represented a flattening-off of oil production after four strong quarterly growth figures. Oil and gas production combined increased by 1.1% year-on-year. Comment on the impact of the oil and gas industry on the Aberdeen property markets is provided on pages 8, 9, 12 and 13 and Aberdeen's City Deal proposals are reviewed on page 5.

The Consensus Forecast for UK Economic Growth published by HM Treasury in October 2016 is for 1.9% growth across the UK economy in 2016, dipping to 1.0% in 2017. Although pointing downwards, these forecasts are an improvement on the 1.7% for 2016 and 0.7% for 2017 which were reported in the September Consensus Forecasts for the UK.

For Scotland, Fraser of Allander Institute's central forecast – published in July 2016 and therefore immediately following the Brexit vote – is for growth of 0.9% in 2016, 0.5% in 2017 and 0.7% in 2018.

Job gains:

Over **100 jobs are to be created** by bus manufacturer Alexander Dennis Limited (ADL) at its base in Falkirk.

Engineering services firm ID Systems is to create **120 new jobs** in Glasgow and Grangemouth.

A European HQ is being set up in Glasgow by California-based Cloudwick Technologies **creating 58 jobs**.

Eight 'Lidl of the future' discount supermarket stores are to be opened in Scotland and will **create 300 new jobs**.

CS Wind Corporation is expanding its facility at Machrihanish to accommodate the fabrication of larger diameter towers for the offshore wind sector **creating 160 new positions**.

Ascensos plan to open a new contact centre in Clydebank where **350 new jobs will be created**.

Engineering firm Ross-Shire Engineering in Muir of Ord is **creating 100 new jobs** and has safeguarded around 300 existing positions following a contract award to supply equipment to Scottish Water.

Job losses:

Standard Life announced **70 positions would be lost** within its IT department in Edinburgh.

HSBC is closing its technology centre in Stirling with the **loss of 90 positions**, and its call centre in Edinburgh is being closed and the **186 members of staff offered a transfer** to Hamilton.

Job losses continue in the oil and gas sector: Subsea 7 announced it is to **cut up to 430 jobs** in the UK, with the majority in Aberdeen; Technip stated that **130 jobs are currently at risk**; and Shell is **cutting 475 jobs** in the North Sea, with the majority of losses at its HQ in Aberdeen.

Retailer BHS went into administration leading to the closure of all 16 of its branches in Scotland which employed **over 520 members of staff**.

Over 100 positions have been lost with the administration of armoured vehicle firm Penman Engineering Ltd, based in Dumfries.

Dumper truck manufacturer Terex Trucks announced **an additional 65 redundancies** at its base in Motherwell.

Aberdeen based Nolan Seafoods announced **around 40 job losses following restructuring**.

Window supplier TFD (Scotland) Ltd in East Kilbride has gone into **administration with the loss of 63 jobs**.

SSE closed its remaining 37 Scottish Hydro Electric shops across Scotland leading to the **loss of 119 jobs**.

Engineering firm Galloway Group Ltd in Dundee went into **administration with the loss of 61 jobs**.

Retro American restaurant chain Ed's Easy Diner is closing four outlets in Scotland – Edinburgh, Livingston, Aberdeen and Inverness – **with the loss of nearly 60 jobs**.

Planning

Empowering planning to deliver great places – An independent review of the Scottish planning system, May 2016.

The much anticipated independent review of the Scottish planning system was published on 31 May 2016. A panel was appointed by the Scottish Government in September 2015 to undertake a root and branch review of the planning system. Its review proposed a "*fundamental rethink of the system as a whole and a planning profession that is bold and clear about its purpose, demonstrating a contribution to society.*" The outcome was 48 recommendations aimed at strengthening the planning system and transforming it in to an enabler of sustainable development.

The primacy of the development plan is unquestionably maintained, but there are proposals to replace strategic development plans at city region level with an enhanced National Planning Framework (NPF). The panel also recommends removing the Main Issues Report (MIR) and Examination stages of the Local Development Plan (LDP) review process.

This recommendation attempts to streamline the current system and front load the consultation process alongside the introduction of an 'independent gate-check' review. The latter will focus on key elements such as the housing requirement, transport appraisal and spatial strategy and "*all those with an interest*" should be part of that review at an early stage.

Should the issue of housing land requirement be debated by "*all those with an interest*" at a time when the focus of discussion should surely revolve around delivery? Attempts to further streamline the development plan system are to be supported, although removing the examination process is an interesting move. The previous planning system (pre-2006) was often criticised for allowing authorities to effectively ignore the recommendations of Reporters at local plan inquiries, so subsequent reforms placed greater emphasis on the Reporter's role and recommendations prior to the adoption of a plan. Whilst there are clearly concerns, predominantly at a local level regarding the over-centralisation of planning decisions, the current system does provide for an independent view on matters at a stage in the process when all sites and issues can be considered in the round.

LDPs would move to a 10-year review cycle with a 20-year vision of place. The emphasis is to refocus LDPs onto delivery, rather than being caught up in an eternal cycle of review. There may be concerns regarding the length of this cycle relative to the dynamic nature of economic circumstances. Nevertheless, this streamlining is a positive move and should see an end to the much publicised process of 'planning by appeal' experienced across a number of local authorities over recent years and driven by the extensive delays in delivering LDPs.

The inadequacy of infrastructure has long been a constraint to bringing forward major new development and we are pleased to see the thrust of the recommendations set out in Ryden's Planning for Infrastructure report for the Scottish Government echoed through the panel's review. Better information on infrastructure capacity and more consistent cross-agency working is key to overcoming infrastructure capacity issues and therefore, a national infrastructure agency with statutory powers is a positive proposal.

Greater clarity and transparency over the level and nature of developer contributions for infrastructure has long been a persistent gripe from the development industry. A move to satisfy those concerns and a more concerted effort to drive the delivery of infrastructure to enable the significant levels of new housing required across the country is welcomed. Proposals to minimise the use of S75 planning obligations will therefore be supported by the development industry, particularly the prospect of a 'national standard' template.

It may not be all positive news for developers however, as the prospect of a national or regional infrastructure levy to capture land value uplift may dampen initial positivity around the rationalising of S75 agreements (although some developers may welcome an increased certainty of infrastructure provision while reserving their position on the cost and apportionment).

The primacy and certainty around the development plan should be strengthened by the Planning Review and recommendations are proposed to afford allocated sites Planning Permission in Principle (PPP), exemption from pre-application consultation requirements, and fast-tracked appeals. Ryden was recently appointed to undertake further research into this issue on behalf of the Scottish Government and our work will directly inform any future reforms of this nature.

The quality of pre-application consultation must be improved, with a suggestion in the Planning Review for applicants to hold a minimum of two community events allowing opportunity for further dialogue and feedback. This proposal follows a common thread within the review of increasing public involvement and confidence in the system.

The need for training within local authorities in issues such as development economics has long been advocated as a means of improving performance and engagement with the private sector. The panel advises that training for elected members should also be mandatory and enforced. In addition, training in community engagement for the development sector must also be initiated.

Contrary to expectations, some in the development community may welcome the proposed 'dramatic' increases to planning fees, assuming there is a corresponding improvement to service received. If such monies are not to be ring-fenced, then question marks may remain over the prospect of an improvement to resources and performance across all authorities.

A sigh of relief from the development industry, but no surprise to see the matter of third party rights of appeal dismissed as adding unnecessary delay, complexity and conflict. Nevertheless, there is a lot within this review to encourage local communities and representative bodies alike. The panel has certainly set out to empower the local community across all ages and aspires to a continuous and active engagement in the planning system by all, with a particular focus on young people.

In this regard, the most significant recommendation is that which enables communities to bring forward their own 'place plans', which will form part of the development plan. The panel's sentiment in seeking to raise the profile of planning in society and encouraging communities to take part in the process is generally welcomed. This is however, a potentially controversial proposal and along with other elements aimed at 'empowering' local communities, could in fact cause greater delays in the system than currently exist. We should be cautious about over-engaging and presenting opportunities to extend a process which we are trying to streamline.

There is a lot in the review to feel positive about regardless of individual experience with the planning system. It presents a mix of unsurprising suggestions, some bold aspirations and others which should be treated with caution. The Scottish Government has already committed itself to a new Planning Act but it seems likely that we will not see the Government's intentions by way of specific reforms until sometime in 2017.

City Region Deals in Scotland

The approval of Scotland's first City Region Deal for Glasgow and the Clyde Valley in 2014 marked an exciting and positive public sector investment in one of the UK's largest urban regions. The allocation of £1.13 billion provided jointly by the UK and Scottish Governments, across the eight local authority areas it spans, is set to focus upon improving roads and transport infrastructure, and creating jobs with the aim of creating the optimum environment required to unlock up to £3.3 billion of private sector investment. Since 2014, Glasgow has built on the legacy of the Commonwealth Games through the promotion of regeneration schemes across the city; whilst it continues to demonstrate high levels of demand for commercial and business space in the city centre. As a result, Glasgow finds itself in prime position to maximise the City Deal Infrastructure Fund to enhance the quality of life and continue to see further economic growth in the region.

While the outcome of Edinburgh's bid for a £2 billion deal has been delayed due to the result of the EU Referendum, proposals are in the pipeline for Dundee, and both Aberdeen and Inverness have already secured funding of £504 million and £315 million respectively.

In Aberdeen's case, this joint funding is vital to securing the future of the economy in the region through investment in transport and digital connectivity, life sciences, agri-food and biopharmaceuticals. A private sector partner – Opportunity North East – has been established to promote this agenda, while ensuring that the city's bedrock oil and gas industry evolves and navigates successfully through the choppy economic waters of the North Sea.

Integrated Joint Boards and Community Planning Partnerships have emerged to empower local communities and build on the vital links between public and private sector bodies, with the aim of guaranteeing resources are distributed to where they are most needed. Investment in local roads infrastructure in the North East will assist in creating a '*better functioning housing market*' – one aim of the Aberdeen City Region Deal – and regional funding assigned exclusively to transport should benefit the efficiency of the planning process, as well as being a catalyst in attracting and delivering development that is vital to the progression of the regional economy.

Offices

Scotland's city office markets remain divergent. Aberdeen is in a multi-year market adjustment while Edinburgh and Glasgow have weathered a difficult summer and face limited new-build development activity.

The relatively buoyant market in **Glasgow** during 2015 and early 2016 gave way to a notable slowdown in occupier activity and new enquiries over the summer months, although this does appear to have picked up slightly post-holiday period. The strong first half and recent pick-up have supported a healthy 12-month total take-up of 75,977 sq.m. This take-up excludes Morgan Stanley's pre-let of 14,739 sq.m. at 122 Waterloo Street, with development completion end 2017, and the letting of 2,777 sq.m. to Edrington Group of the top four floors at Esson Properties' 100 Queen Street, which concluded after our statistics cut-off date.

Deals to ACCA at 110 Queen Street (5,179 sq.m.); AXA at Cuprum, Argyle Street (4,592 sq.m.); and Regus at Tay House, Bath Street (2,696 sq.m.) were the highlights of city centre take-up at 26,560 sq.m., some 15% down on the previous period. Lettings at City Park to Sky (4,992 sq.m.) and Actavo (1,465 sq.m.) bolstered peripheral take-up at 10,163 sq.m., up by 24%.

A long standing feature of the market is that larger transactions have tended to focus on the new and higher quality large floorplate stock, which continues to reduce supply in this sector. No speculatively developed new build is programmed to commence in the foreseeable future with the result it will be well into 2019 or beyond before we see any new additions of scale.

For larger occupiers, there are only three new or refurbished buildings capable of providing over 1,858 sq.m. with floorplates over 1,394 sq.m. Abstract Securities' St Vincent Plaza is also the only new build that can provide more than 3,716 sq.m. with floorplates over 929 sq.m. As such, Glasgow has a shortage of new best in class space for the larger floorplate office market.

This lack of new pipeline puts Glasgow at a potentially serious disadvantage in competition with other UK cities in attracting footloose inward relocations. Whilst there are obvious implications of political uncertainty, Glasgow awaits the next cycle of new development.

This hiatus is to the potential benefit of forthcoming large scale refurbishments such as NFU Mutual's 191 West George Street (7,011 sq.m.) and Moorfield/Resonance's 1 and 3 Atlantic Quay (up to 9,868 sq.m. and 7,478 sq.m. respectively).

Whilst the larger end of supply has contracted, the choice for the traditional indigenous professional occupier has expanded with completion of a number of high quality refurbishments offering floors across the range 325 sq.m. to 790 sq.m. including: EPIC UK's 9 George Square; Esson Properties' 100 Queen Street; Northwood Investors' 180 St Vincent Street; and Cornerstone's 220 St Vincent Street.

Total supply has reduced slightly to 344,109 sq.m. with 214,030 sq.m. (62%) in the city centre and 130,079 sq.m. (38%) on the periphery.

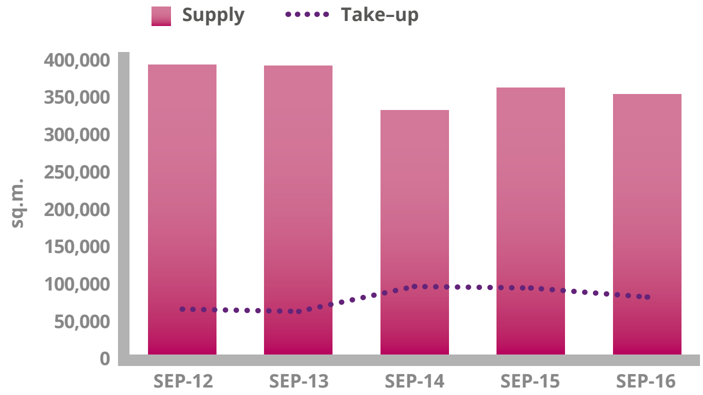
On the city centre periphery there continues to be regular multiple letting activity at Skypark; The Whisky Bond; The Hub at Pacific Quay; Templeton on the Green; and City Park. The Four Winds Building at Pacific Quay leased 785 sq.m. to Frame and Nova Business Park secured Urban Union for 309 sq.m. in Pavilion 1.

There was also activity in the out-of-town market with Document Data Group and Proact IT UK at Maxim Office Park; Network Rail at Airbles Road, Motherwell (1,628 sq.m.); NHS Greater Glasgow and Clyde (1,482 sq.m.) and Walker Love (495 sq.m.) at Smithshill Street, Paisley; Simply Construct at Clydesdale House, Glasgow Business Park (192 sq.m.); Beeks Financial Cloud Limited at Chiron House, Phoenix Business Park, Paisley (223 sq.m.); and Vokera at Cameron Court, Hillington (250 sq.m.).

Prime headline office rent in Glasgow remains £306-£323 per sq.m. Despite reducing supply of larger Grade A space, incentives remain very competitive as developers and landlords seek to secure their tenants.

There is greater choice for occupiers in the refurbished sector with a range of quality and rents. There are options available for good space from £178 per sq.m. rising to £231-£280 per sq.m. for high quality space, or potentially more for the best upper floors.

Glasgow office supply and take-up



Edinburgh's office market achieved 32,924 sq.m. of take-up during the six months to September 2016, giving a high total take-up of 96,145 sq.m. for the 12 months to September 2016, due largely to a strong period Q4 2015/Q1 2016.

Take-up in the city centre was 21,519 sq.m. across 55 deals, representing 65% of total take-up. Grade A and high quality accommodation accounted for 7,293 sq.m. or 34% of the city centre office take-up.

Notable city centre transactions include: People's Postcode Lottery at 28 Charlotte Square (3,085 sq.m.); Cirrus Logic taking further space at Quartermile 4 (2,097 sq.m.), which follows their pre-let acquisition of 6,507 sq.m. reported in the previous six month period; Intergen at 81 George Street (962 sq.m.); Nucleus Financial Group at Hobart House, 80 Hanover Street (883 sq.m.); Dexcom at Tanfield (847 sq.m.); Bravura Solutions (342 sq.m.) being the first occupier to sign a lease at IVG's Grade A refurbishment of 40 Torphicen Street; and Wood Mackenzie at Exchange Place 3 (317 sq.m.).

Prime office rents for existing stock in central Edinburgh remain around £300 per sq.m., although pre-letting activity on new build/Grade A refurbishment options is occurring above this level. Incentives remain around 18-24 months' rent free for a 10-year lease commitment to the highest quality covenant.

Older office stock continues to be targeted by developers for alternative uses. Notable examples include: the former HQ of Wood McKenzie at Kintore House, 74-77 Queen Street (3,315 sq.m.) bought by VALAD for conversion to serviced apartments and the sale of STMicroelectronics' offices at Pinkhill to Dandara for residential conversion.

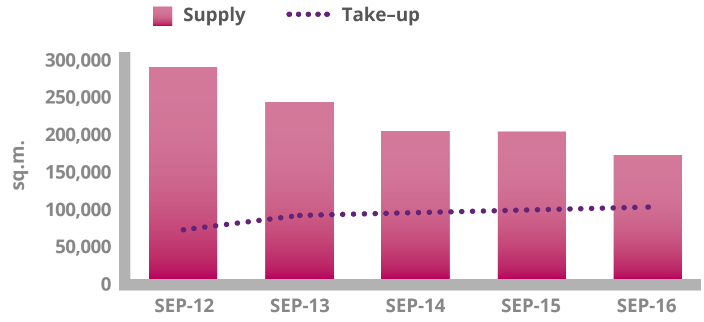
Edinburgh's peripheral office markets saw a total of 11,405 sq.m. transacted across 42 deals over the past six month period, a 43% decrease in activity from the previous six month period (which included one major transaction of 9,940 sq.m. to Edinburgh Napier University).

Within this, West Edinburgh saw a total of 3,494 sq.m. transacted across 12 deals including: HSBC securing additional space at 6 Lochside Avenue (833 sq.m.) and Quotient Clinical's relocation from Heriot-Watt Research Park to Haston House, 2 Redheughs Rigg (594 sq.m.). Prime rents in West Edinburgh are currently up to £172 per sq.m. for refurbished options in the South Gyle area, rising to £215 per sq.m. on Edinburgh Park.

Larger office deals in Glasgow over the last six months include:

Address	Size	Occupier
110 Queen Street	5,179 sq.m.	ACCA
Cuprum, Argyle Street	4,592 sq.m	AXA
City Park, Alexandra Parade	4,992 sq.m.	Sky
	1,465 sq.m.	Actavo
Tay House, 300 Bath Street	2,696 sq.m.	Regus
Spectrum Building, 55 Blythswood Street	878 sq.m.	Arthur J Gallagher Insurance
Inovo, George Street	871 sq.m.	CGI
Atrium Court, 50 Waterloo Street	847 sq.m.	Search Consultancy Ltd
	793 sq.m.	The Mortgage Lender
Four Winds Building, Pacific Quay	785 sq.m.	Frame
9 George Square	689 sq.m.	Egencia

Edinburgh office supply and take-up



In North Edinburgh, a total of 1,961 sq.m. was transacted across nine deals with the letting to Ajenta at Commercial Quay (483 sq.m.) accounting for 25% of total take-up in this sub-market. Other smaller transactions include: LUX at Sugar Bond (235 sq.m.); CD International Building Services at 13 Breadalbane Street (106 sq.m.); and ESI.info at 12 E&F Timber Bush (112 sq.m.). Prime rents in North Edinburgh are up to £150 per sq.m. although there is limited supply of quality stock with the general tone for the area closer to £130 per sq.m.

There is presently no speculative office development taking place in Edinburgh's peripheral locations and this lack of new build is expected to bring forward significant refurbishments, for example at Haston House, 2 Redheughs Rigg with the refurbishment of up to 6,968 sq.m. of vacant space.

Total office supply across Edinburgh at September 2016 is 163,476 sq.m., a further decrease of 12% from the previous six month recorded figure.

Although the city centre has a projected office development pipeline of 62,709 sq.m. over the next three years, only 10,278 sq.m. (16%) is currently progressing on-site within two buildings at Quartermile 3 (6,781 sq.m.) and 2 Semple Street (3,497 sq.m.). At the time of writing there are a number of deals of notable size currently in legal hands including: State Street (6,039 sq.m.); EY (3,252 sq.m.); STMicroelectronics (1,997 sq.m.); and Zonal Retail Data Systems (1,132 sq.m.). As these leases conclude the erosion of the Grade A quality product will be compounded.

There are also a number of larger requirements which are currently unsatisfied. These include the Government Procurement Unit (14,865 sq.m. by 2020) which has shortlisted four options – Haymarket, India Quay, New Waverley and the RBS offices at Dundas Street. It would appear that this government initiative is progressing at pace and will likely be in legal hands by the end of 2016. This will reduce the development pipeline which in turn will have an impact on lowering incentives and potentially accelerating rental growth.

The next wave of new office development will not be ready until Q4 2017/Q1 2018 with M&G's Quartermile 3 and GSS Developments' 2 Semple Street, mentioned above, being the earliest of the new build options to be delivered. Grade A refurbishment options are expected to fill the void in the meantime with One Lochrin Square (5,984 sq.m.) and Greenside, 12 Blenheim Place (3,981 sq.m.) both anticipated for delivery during the first half of 2017.

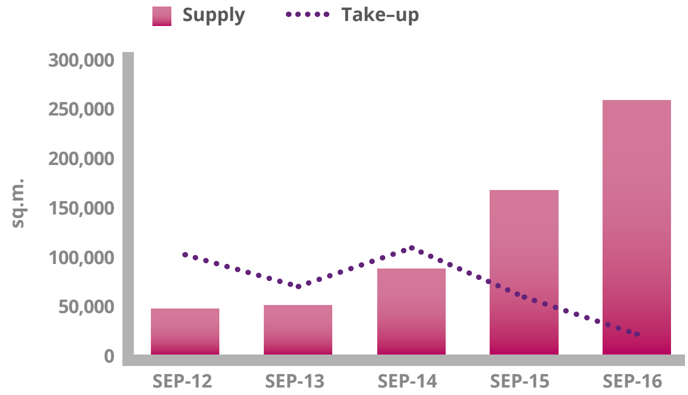
Although the price of a barrel of oil has risen from $40 to $52 in the last six months, this hasn't resulted in any meaningful change in the office market in **Aberdeen**. Drilling activity is at its lowest level since records began in 1982. Despite this, North Sea production has seen two years of increases in 2014 and 2015 due to huge investment in the years before the oil price crash. This, however, is likely to change with production levels predicted to plummet within a few years unless investment rises from unsustainably low levels. Without a rise in investment there is unlikely to be much change in the dynamics of the office market, where supply is drastically outstripping demand.

Supply has once again risen, to 252,000 sq.m., which is up another 13% from six month's ago. Of this, c. 28,400 sq.m. is under construction and nearly half, 118,500 sq.m., comprises modern, well-specified accommodation. Approximately 78% of the suites available are in excess of 929 sq.m. In the West End of the city there has been a large increase in office supply with various properties competing for a limited number of tenants.

Larger office deals in Edinburgh over the last six months include:

Address	Size	Occupier
28 Charlotte Square	3,085 sq.m.	People's Postcode Lottery
Quartermile	2,097 sq.m.	Cirrus Logic
81 George Street	962 sq.m.	Intergen
Hobart House, 80 Hanover Street	883 sq.m.	Nucleus Financial Group
6 Lochside Avenue, Edinburgh Park	833 sq.m.	HSBC
Haston House, 2 Redheughs Rigg, South Gyle	594 sq.m.	Quotient Clinical

Aberdeen office supply and take-up



Take-up has risen by 47% to 11,380 sq.m. over the past six months in 34 transactions. Of these deals approximately 78% were Grade A or modern suites. The largest increase was in the 200-500 sq.m. bracket where take-up has doubled. Annual take-up fell to only 19,105 sq.m.

Within the city centre, another suite of 515 sq.m. has been let to HM Ministry of Justice at AB1, Huntly Street, where only 1,070 sq.m. now remains available over two suites.

Muse's Marischal Square remains on target for completion in July 2017 and the top floor (1,766 sq.m.) of MSq1 is now under offer to Aberdeen Journals. Also in the city centre, the Silver Fin building is due to complete in March 2017 and 2,415 sq.m. has been let on the lower floors to Orega under a management agreement. Neither of these two Grade A transactions is yet included in our take-up statistics for the Aberdeen office market as they will only be recorded when the leases commence.

Serviced office provider Citibase has taken 2,045 sq.m. at 9 Queen's Road under a management agreement with head tenant Anderson Anderson & Brown, which has now relocated to Prime Four Business Park. 20 Queen's Road (822 sq.m.) has been let to Oil & Gas Technology Centre at a headline rent of £269 per sq.m.

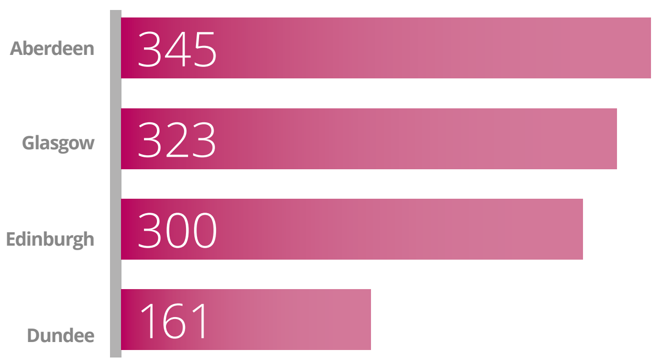
There have been no substantial deals in peripheral locations and the majority of transactions have been under 500 sq.m. Across the whole market only seven transactions were in excess of this size. The rebranded H1 (formerly Seafield House) at Hill of Rubislaw has been overhauled and part of the offices have been refurbished to provide 2,900 sq.m. of high quality accommodation which can be split into varying sizes.

Until the offshore industries stabilise at a sustainable rate of investment, there is unlikely to be a corresponding increase in activity in Aberdeen's office market. In its annual economic report, Oil & Gas UK stated that while costs have fallen and the fiscal regime has been improved, many potential investors are unable to access the finance they require to develop assets. Oil & Gas UK reports that the industry is producing at four times the rate at which it is discovering new reserves, and this is unsustainable. As noted in the Economy section on page 3, some operators continue to shed jobs. Until this changes we are unlikely to see a marked difference in the office market.

The **Dundee** office market remains relatively subdued. Demand is healthy for smaller office premises, but the market offer is relatively thin and the choice of quality accommodation is limited. Recent transactions include: Reagent Games taking an assignation of a lease of 526 sq.m. of space within the Vision Building and Scotland's largest mobile app developer Waracle relocating its Dundee headquarters to the Engine Room at Bash Street (344 sq.m.). The lack of a real choice of quality modern office accommodation remains a concern, with the remaining space at River Court/DundeeOne, The Vision Building and West Port House being the exceptions.

In the largest office letting of the past six months, Insights Learning & Development has expanded into Innovation House, 17 Luna Place, Dundee Technology Park (913 sq.m.).

Prime city office rents 2016 (£ per sq.m.)



Larger office deals in Aberdeen over the last six months include:

Address	Size	Occupier
9 Queen's Road	2,045 sq.m.	Citibase (management agreement)
20 Queen's Road	822 sq.m.	Oil & Gas Technology Centre
Level 5, City Wharf, Shiprow	549 sq.m.	V-Ships
AB1, Huntly Street	514 sq.m.	HM Ministry of Justice

Industrial

The events of the 23rd and 24th of June contributed to what was a mixed summer for the Scottish industrial market. General enquiry levels and the number of significant new entrants were both lower than expected.

However, a flow of transactions has continued and the long term effects are not yet apparent. Ryden has evidence of only two deals in the **West of Scotland** industrial sector where Brexit was directly cited as the reason for a deal not progressing.

The key statistics in the market remain favourable for landlords and developers. Utilising Costar data, the current vacancy rate for the Greater Glasgow market is 7.9%, which rises to 10.3% with the inclusion of vacant leased properties. A significant proportion of vacant space is now in need of re-development or extensive refurbishment. Many key estates remain close to full occupancy due to new lettings and existing tenants renewing leases due to the lack of suitable options.

Enquiry levels have increased and the majority of transactions involve Scottish businesses with a UK focused market. There has also been continued interest for heritable property possibly due to low interest rates. There is however a shortage of good quality second hand or new build units to purchase.

The Glasgow Airlink Estate near Glasgow Airport in Paisley is an estate which demonstrates the increased appetite. Area Estates bought the estate from CBRE Investors with the intention of selling off the individual units to occupiers and investors. The estate provides units from 279 sq.m. to 697 sq.m. and is now fully occupied with the majority via sales or with leasehold interests then sold at auction. Capital rates of up to £613 per sq.m. have been achieved for early 1980s product in moderate condition. Rental rates are £54 per sq.m. Occupiers include: Loganair, TMS Motor Spares, Adlib Audio, Xpress Despatch and Consult Lifts.

The development market has begun to respond to the favourable market dynamics but it remains at a low level. Clyde Gateway and its partners have responded through direct provision on the retained plots at Clyde Gateway East. The development will involve a highly specified 2,550 sq.m. unit targeted at the engineering and manufacturing market with a site start anticipated before the end of 2016 at a quoting rent of £81 per sq.m.

MEPC, also at Clyde Gateway East, has secured a letting of a 1,790 sq.m. unit from its phase 1 development following the decision of Torishima to relocate. Dentec Scotland Limited leased the unit within a matter of weeks of it becoming vacant and has taken a 15-year lease at £78 per sq.m. MEPC also secured a pre-let of its 1,500 sq.m. building 604 which is due to complete in November 2016. The rent will be £81 per sq.m. for the first two years, rising to £86 per sq.m. on a 10.5-year lease. Further phases of development are under consideration.

Rutherglen Links in Rutherglen is a new location brought forward by Clyde Gateway to provide plots ready for development. Plots have been sold to Harris Finance and Plot C is being developed to provide a 1,858 sq.m. unit completed to shell specification by the end of November 2016. The quoting rent, including a provision of offices, is £81per sq.m.; a 929 sq.m. unit will follow, which is attracting interest from roadside related users.

At Hillington Park, Patrizia AG and Oaktree are well advanced with the construction of Evolution Court, a development of four units scheduled for completion in December 2016. The units range from 1,650 sq.m. to 2,225 sq.m. and the quoting rent is £81 per sq.m. Elsewhere in the Park, 450 Hillington Road (2,756 sq.m.) is undergoing extensive refurbishment and the works have attracted strong occupational interest. A number of provisional pre-let interests have been agreed for a trade park and further commitment is being sought before development commences.

Fusion Assets/CBC's Western Campus will complete in November 2016 and 37% of the space has been taken in pre-let deals. The achieved rents range from £81 per sq.m. for 929 sq.m. to in excess of £86 per sq.m. for units of up to 557 sq.m. The rate of letting reflects the excellent location and scarcity of product on the popular Strathclyde Business Park, which will be further enhanced by the various road improvement works. The joint venture's other development nearby at Dundyvan, Coatbridge is nearing full occupancy following recent deals on 464 sq.m. units including Eric Wright Water and King Communications.

Larger industrial deals in the West of Scotland over the last six months include:

Address	Size	Occupier
Atlas, Central Point, Eurocentral	5,249 sq.m.	Hermes Parcelnet Ltd
2 James Street, Righead, Bellshill	4,830 sq.m.	HSS Hire
Springhill Parkway, Glasgow Business Park	4,274 sq.m.	Euro Car Parts
6 Bedlay View, Tannochside, Uddingston	2,880 sq.m.	Clipper Logistics PLC
OKI Way, Cumbernauld	18,766 sq.m.	William Grant & Sons Ltd

In April the Scottish Government announced changes to the business rates system ending the 100% relief for empty industrial buildings. Relief is now restricted to the first six months of vacancy after which it reduces to 10%. Where this leads to the demolition of poorer, older stock as it falls vacant, it will be good for the health of the market. However, many Scottish businesses start from low cost property and the removal of such options will make matters difficult for low margin businesses. It is also leading to soft deals in the less prime areas in an attempt to limit the potential liability. This provides little incentive to spend money on improving the stock and with the liabilities of The Assessment of Energy Performance of Non-Domestic Buildings (Scotland) Regulations 2016 it is possible that demolition will become more prevalent.

The big-box market has been disappointing over the summer months with only one letting, namely Buccleuch Property's 5,249 sq.m. Atlas to Hermes Parcelnet Ltd at Eurocentral at a rent of £65 per sq.m. following the expansion of the yard. The occupancy level at Eurocentral is extremely high and the letting leaves Vertex at 12,000 sq.m. and the Colossi buildings providing 8,750 sq.m. and 8,873 sq.m. as the only available space. Eurocentral's status as the prime logistics location in the West has been underlined by Lidl's decision to purchase c. 20 hectares from Scottish Enterprise for the construction of a c. 55,740 sq.m. Regional Distribution Centre. The development is currently awaiting planning consent and is expected to be approved.

The upgrading and alterations to the M8, M73, M74 and A725 have caused widespread disruption throughout 2016, however the works are scheduled for completion in Spring 2017 and the structure of the amended network is becoming clear. It is envisaged that the amended routes will improve the road network significantly and confirm this key area as the prime logistics location in Central Scotland when combined with the extensive railhead at Mossend.

Market conditions in the industrial property sector in **East Central Scotland** are effectively as reported in our April 2016 review, with a limited availability of modern accommodation and a steady, if occasionally unpredictable, level of demand.

There is now only one large scale industrial building available within the boundaries of Edinburgh. Scotmid's refurbished space at Queen Anne Drive in Newbridge totals 8,758 sq.m. and is available as a whole or in four sections with a quoting rent of £37 per sq.m. In addition to the Scotmid premises, 4,645 sq.m. at Edinburgh Distribution Park, Newbridge and two units within Edinburgh Interchange totalling over 7,432 sq.m., are available.

Recent transactions of large buildings include: 35,303 sq.m. let to Amazon at Logicor's J4M8 380, Bathgate for a distribution facility; Regenersis renewing its lease at Westwood One, Westwood Park, Glenrothes (16,861 sq.m.) at c. £21 per sq.m.; and the sale of the former Asda distribution premises, DC2, West Mains Industrial Estate, Grangemouth to Whyte & Mackay (11,706 sq.m.) at a price in the region of £2.8 million (£239 per sq.m).

The position with medium sized buildings of 1,858 – 4,645 sq.m. and smaller is similar. The acute shortage of modern accommodation within Edinburgh continues to see rent levels increase across all size spectrums and locations. A selection of the key deals are: 24 West Shore Road, Granton (293 sq.m.) let to Siemens PLC on a five-year lease at £95 per sq.m.; following the sub-division of 23 South Gyle Crescent, South Gyle Industrial Estate by Tilstone (1,650 sq.m.) has been let to DFS on a 10-year lease at £75 per sq.m.; a stand-alone Unit 13 Roseburn Street, Edinburgh (491 sq.m.) has been let to Screwfix on a new 10-year lease at £97 per sq.m.

C&W Assets has been the most active developer of small units over recent years. The first phase of its development at Inchwood Park in Bathgate is now fully let at rents of £70 per sq.m. In addition, the last units which the developer undertook recently at West Edinburgh Business Park, South Gyle are now under offer with a quoting rent of £81 per sq.m. Given the positive market position, but concerns over increasing build costs and the economic environment, it will be interesting to see whether C&W Assets make the decision to proceed with future phases of these two developments, particularly on a speculative basis.

The backbone of the industrial property supply in East Central Scotland over the last 10-15 years has been the existing accommodation in Livingston. The majority of

Larger industrial deals in the East of Scotland over the last six months include:

Address	Size	Occupier
J4M8 380, Bathgate	35,303 sq.m.	Amazon
DC2, West Mains Industrial Estate, Grangemouth	11,706 sq.m.	Whyte & Mackay
A1 Gogarbank, Gogar Station Road, Edinburgh	1,689 sq.m.	Technologistics Ltd
23 South Gyle Crescent, South Gyle Industrial Estate, Edinburgh	1,650 sq.m.	DFS
Brunel Road, Dundee	1,880 sq.m.	Expert Logistics Limited

these estates and buildings were constructed in the 1970s and 1980s, which creates a natural concern over the configuration and life expectancy of the buildings. Brucefield Estates Trustees, the owners of Brucefield Industry Park in Livingston, probably the largest single ownership industrial estate in the area, are currently working their way through a refurbishment programme and are encouraged by the level of interest and resulting lettings which this investment has generated.

West Lothian including Livingston has seen the highest level of activity over the last six months in East Central Scotland with over 22 deals recorded. Historically, due to the oversupply of similar accommodation, rental levels have struggled to surpass the £45 per sq.m. barrier, however recent transactional evidence suggests that this level has now been breached. Key deals include: Unit 9 Inchwood Park, Bathgate let to Danwood (222 sq.m.) on a 10 year lease at £70 per sq.m.; the entire parade of Units 1-7 at Westerton Road, Broxburn relet to a variety of tenants with the most significant deal to Drilltools Ltd with Units 6 & 7 (913 sq.m.) at £48 per sq.m.; and only one unit now remains at Cedarwood Asset Management's Easter Inch Park, Bathgate following the letting of Unit 4 (770 sq.m.) to Q2 Solutions on a five-year lease at c. £54 per sq.m.

The projected completion date for the new road bridge over the Forth, the Queensferry Crossing, is May 2017 and this will not only be a benefit to Fife but also Scotland as a whole with improved connectivity between major towns and cities.

Some rental growth is anticipated in certain areas of Fife, but the counter to this may be the concerns over the oil and gas industry and the closure of some key occupiers. That said there has also been market activity over the past six months with three deals concluded at Kiros Development's Fife Food and Business Park, Glenrothes: Unit 39 let to Park Ferme Ltd (284 sq.m.), Unit 38 let to Rotawave Scotland Ltd (284 sq.m.) and Unit 30 let to Immortal Fabrications Ltd (185 sq.m., all at rents of £43 per sq.m.

The former TT Electronics factory on Eastfield Industrial Estate, Glenrothes has been purchased by CN Properties who plan five new units here. The firm has also redeveloped the former Coachworks on Woodside Road in Glenrothes, creating seven workshop units.

The Caledon Property Group has purchased the remainder of the Simclar accommodation on Pitreavie Business Park in Dunfermline, which comprises 11,148 sq.m. of accommodation and development land. It is understood the largest of three buildings is to be demolished and replaced by new smaller units.

Midlothian with its excellent transportation links to Edinburgh continues to benefit from supply shortages in the city. Recent deals concluded at Bilston Glen and Pentland Industrial Estate include: Kames Capital letting Unit 2 Dryden Vale (239 sq.m.) to Speedy Services Ltd at £73 per sq.m.; and James Hay Pension Trustees letting Unit 10 Borthwick View (206 sq.m.) to Devine Electrical on a five-year lease at £70 per sq.m. Continued demand has created rental growth year-on-year and landlords also tightening their offer on rental incentives.

The Falkirk/Stirling/Grangemouth area continues to be an attractive destination for industrial and trade occupiers. Recent lettings include: Unit A2 Etna Road, Middlefield Industrial Estate, Falkirk (493 sq.m.) to Rinus Roofing Supplies at £70 per sq.m.; and Eurocell committing to Unit 12 Broadleys Business Park, Stirling (325 sq.m.) at £80 per sq.m. Falkirk Council is mid-way through the development of four speculative 232 sq.m. industrial units at Abbotsford Business Park in Falkirk.

In the Scottish Borders, Catalyst Capital recently acquired a number of units within Tweedbank Industrial Estate, Galashiels and has embarked on an extensive refurbishment of the vacant units. Subsequently Block 4 Unit 1 has been let to Meigle Colour Printers (929 sq.m.) and Block 4 Unit 2 to Borders College (929 sq.m.). The latter was let at c. £37.50 per sq.m.

The industrial market in **Aberdeen** has again experienced a difficult and challenging six months. The prevailing trend of low oil prices, decreasing reserve size opportunities and capital constraints means that turning discovery opportunities into viable commercial developments in the oil and gas sector is difficult and as a consequence, property markets are suffering.

Larger industrial deals in the North of Scotland over the last six months include:

Address	Size	Occupier
Unit 1, Kingshill Commercial Park, Westhill	1,725 sq.m. + yard	Swellfix UK Ltd
Unit 3, Kingshill Commercial Park, Westhill	1,440 sq.m. + yard	AIS Group
Unit 4, Kingshill Commercial Park, Westhill	1,441 sq.m. + yard	Dentec (Scotland) Ltd
E7, Aberdeen Gateway Business Park, Cove	1,812 sq.m. + yard	ERIKS Industrial Services Ltd
Badentoy North, Badentoy	865 sq.m. + yard	BT Plc
Crathes & Kildrummy Buildings, Aker Village, Howe Moss Avenue, Dyce	7,100 sq.m.	Aker Subsea Ltd

Industrial take-up in the last six months totals 29,434 sq.m., which represents a 13% increase in comparison with the previous six months. The number of deals concluded fell though, by 32% from 40 to 27. Take-up has increased in the 465 – 929 sq.m. (61%) and over 930 sq.m. (67%) size ranges through a number of new-build deals at Kingshill Commercial Park in Westhill (Knight Property Group) and at Aberdeen Gateway (Muir Group) to the south of the city. Take-up for small units below 464 sq.m. is down by 40%.

The transactions at Kingshill Commercial Park comprise: Unit 1 (warehouse 649 sq.m., office 1,076 sq.m. and yard) let to Swellfix UK Ltd; Unit 3 (warehouse 929 sq.m., office 511 sq.m. and yard) to AIS Group; and Unit 4 (warehouse 929 sq.m., office 512 sq.m. and yard) to Dentec (Scotland) Ltd.

Supply has increased by 55% in the last six months from 85,560 sq.m. to 132,372 sq.m. The number of properties available in the market place has risen from 91 to 126, a 38% increase. Supply is up in all size ranges, most notably by 119% in the 186 – 464 sq.m. size band and by 80% in the 465 – 929 sq.m. size range.

Rental levels remain stable with new build rents remaining at £97 per sq.m. for industrial accommodation, £194 per sq.m. for offices and £21 per sq.m. for secure concrete yards. It remains a tenants' market however, with landlords having to offer incentives and entertain flexible lease arrangements in order to attract or retain occupiers. The changes to vacant industrial rates relief have also meant that landlords are keener than ever before to avoid having vacant units.

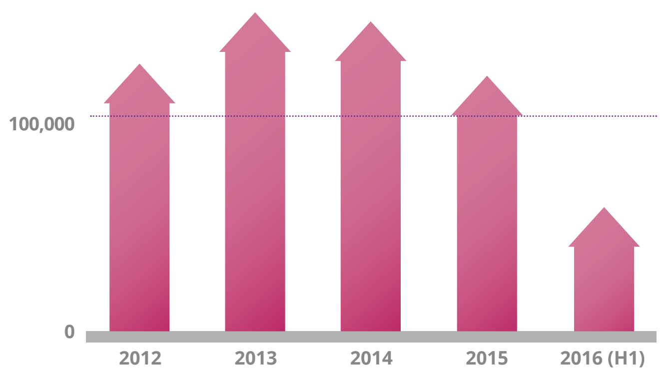
Despite the challenging market conditions, developers continue to press ahead with speculative industrial developments. E8, Aberdeen Gateway Business Park, Cove by Muir Group comprises warehouse (929 sq.m.), offices (418 sq.m.) and yard (1,579 sq.m.); and Unit 2 Kingshill Commercial Park by Knight Property Group comprises warehouse (929 sq.m.), offices (511 sq.m.) and yard (1,313 sq.m.).

Occupiers continue to seek good quality industrial accommodation and are still prepared to commit to long term leases for the right building. It is generally lease events (expiries and break options) which are creating requirements, as well as occupiers seeking to consolidate from a number of properties under one roof in order to save costs and improve efficiency.

In recent years the majority of industrial property transactions in **Dundee** have involved small to medium sized second-hand space. That trend continues, although an increasing shortage in the availability of good quality modern accommodation is noted.

Encouragingly, a number of larger requirements have recently emerged which have resulted in new letting activity taking up some of the larger space availability. Home delivery specialists Expert Logistics Limited has secured its first depot in Dundee at Brunel Road (1,880 sq.m.). In addition, one of the world's largest providers of fuel retailing solutions, Tokheim has expanded its Dundee operation by taking a lease of the former Scotherbs building at Longforgan (1,995 sq.m.) and Aerospace Tooling Limited has extended its occupation at Piper Street, Baldovie Industrial Estate (c. 3,716 sq.m.) for a further 10 years. There are also a number of other large scale requirements which remain to be satisfied, which is positive news for the market moving forwards.

Number of industrial transactions in Scotland



Retail and Leisure

High Street and out-of-town market activity continue to reduce retail vacancies. Most locations are improving or holding their own in comparison to our last report in April 2016, when net closures of one shop per week were being witnessed.

Post-Brexit vote retail market indications are difficult to read at this stage. However, the food and beverage market appears to be robust with little or no change in the requirements and aspirations of operators in this sector, although very recently the spectre of significant price inflation (through currency devalue) raised its head in negotiations between Tesco and Unilever. Indicators also suggest that the value retail market will maintain sales and perhaps any potential uncertainty in the market may allow the increasing successful value retailers to secure new sites.

Retailer/occupier demand has been strong in the first half of 2016, led by the food/clothing markets. Several new entrants to the market have helped, but established retailers have led their weight to those actively seeking opportunities for new stores.

High profile market failures during 2016 include: BHS, Austin Reed, Store Twenty One and My Local (including former Morrisons M Local Stores). However, there are several retailers pushing on with new stores at this time, including: Holland & Barrett, Joules, Paperchase and Office who continue to seek further High Street representation. Active retailers, both in and out-of-town, include: Next, Aldi, DFS, Lidl, Oak Furniture Land, Tapi, Ann Summers, Sports Direct, B&M and Home Bargains.

Drive-thru opportunities are on the increase with occupiers including: McDonald's, KFC, Burger King, Starbucks and Costa opening new sites during 2016. Costa has secured sites at Cameron Toll, Edinburgh; Bridge of Don, Aberdeen and Broxden, Perth, with others to follow at Fort William and Milton Link, Edinburgh. McDonald's has agreed terms at Cameron Toll and is active at other sites including: Dalmarnock Road, Glasgow; Great Western Retail Park, Glasgow; Inshes Retail Park, Inverness; and Kittybrewster Retail Park, Aberdeen.

Glasgow has seen more activity within the leisure sector to further its reputation in the restaurant market, through lettings to Smashburger (399 sq.m.) at 165 Sauchiehall Street and Chilango (139 sq.m.) at 197 Sauchiehall Street. Pizza Punks opened its first restaurant in the former bank premises at 90 St Vincent Street following on from Iberica (450 sq.m.) at 140 St Vincent Street. Retail lettings on Sauchiehall Street include: Hackett (1,858 sq.m.) with their first store in Glasgow at No. 123; Ryman (230 sq.m.) at No. 42 and Millets (398 sq.m.) at No. 171.

Formal Investments has announced a redevelopment of the BHS building on Sauchiehall Street to transform the former department store into a 12-storey tower with 12,077 sq.m. of office accommodation.

On Princes Street, **Edinburgh** HMV closed at No. 129/130 following the purchase of the building by Sports Direct which plans to open a store here. Jeweller Chisholm Hunter is opening in the former USC unit at No. 97/98 Princes Street and Ann Summers relocated from No. 89 to the former Footlocker unit at No. 87. Elsewhere in the city centre, Joules has relocated to No. 85 George Street and Bobbi Brown, opened at No. 37b.

The demise of BHS on Princes Street has opened the way for landlord LaSalle Investment Management to announce plans for a new retail, hotel and restaurant development within the 11,334 sq.m. property. With demolition of the St James Shopping Centre now underway to facilitate the development of the new Edinburgh St James, not only the city's retail and leisure offer, but the Edinburgh skyline, is due some significant changes over the medium term.

At Ocean Terminal in Leith, HMV opened a store following its closure on Princes Street and Sports Direct is opening here. Poundworld has recently opened, however as elsewhere, the BHS closed.

In **Dundee**, the recent growth in the number of food operators has continued. The Overgate Centre has attracted another new addition to the city's food offering with Italian/American themed restaurant Frankie & Benny's opening a new outlet. Patisserie Valerie plans to open its first Dundee store at 75 High Street (271 sq.m.); Café Montmartre opened at 91 Perth Road (88 sq.m.); and independent Dundee eatery, Avery & Co is due to open at 304 Perth Road. Outwith the city centre Domino's Pizza and Papa John's are both to open new pizza delivery outlets at Kingsway East Leisure Park and Arbroath Road respectively. Domino's Pizza and Starbucks are also poised to open new outlets at Dunsinane Industrial Estate.

In **Aberdeen**, BMO Real Estate Partners, the owner of the Bon Accord and St Nicholas centres, is in discussions with a cinema operator to take the upper floor within the scheme in order to take advantage of the demand from the leisure sector. Lettings have been announced at the new Marischal Square development where on completion Mackie's will open an ice cream and coffee shop along with restaurants All Bar One and Prezzo.

East Kilbride is due to open its Olympia Leisure Quarter around the ice rink in November 2016, which comprises 7,432 sq.m. and is 85% let. Only four units remain available (two of which are under offer). Lettings include: Frankie & Benny's, Chiquitos, Filling Station, Nando's, Pizza Express, Bella Italia and Handmade Burger Co. The last 12 months have seen the landlords secure 14 deals elsewhere within the centre with occupiers including: Yours, Peacocks, Pep&Co, The Works, Bestseller, JD Wetherspoon, Eurochange, Prime Vapour and Chopstix.

Lettings at **Glasgow Fort** include Thaikhun (279 sq.m.) and GBK (232 sq.m.) which join other restaurant occupiers recently opening at the fashion park.

At **Silverburn**, Tortilla has now opened a new Mexican themed restaurant at the entrance to the Winter Gardens and HMV has re-opened a store. Card Factory has taken its first unit within the centre and The Entertainer toy store is currently being fitted out.

Ediston Real Estate is close to completion of the second phase at **Port Glasgow** Retail Park, on behalf of the Clydebuilt Fund. The completion of the development will see 8,360 sq.m. let to Aldi, B&M, Watt Brothers, TK Maxx and Marks & Spencer, to sit alongside existing occupiers B&Q and Costa.

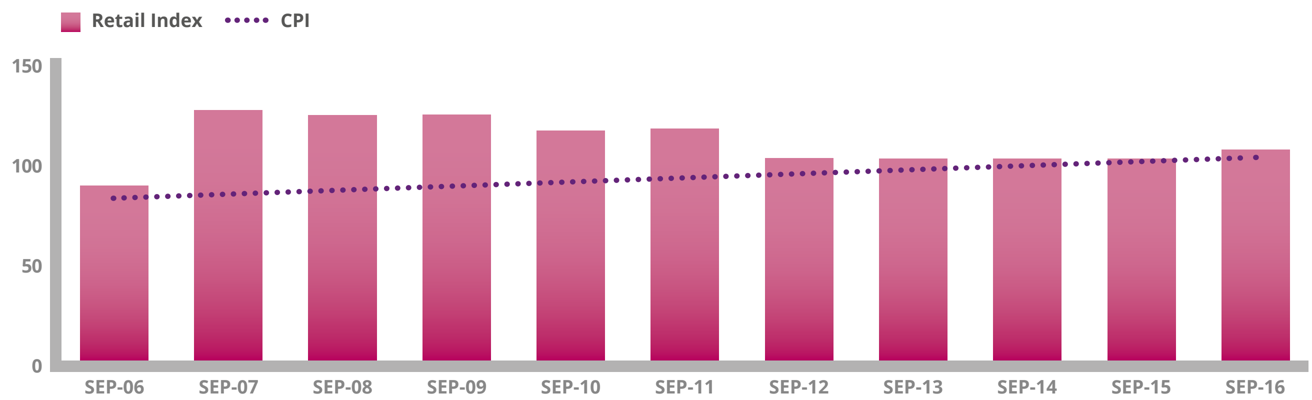
In **Falkirk**, Watt Brothers has opened in the former HMV store at Howgate Centre and at Central Retail Park, Marks & Spencer has opened a 1,393 sq.m. Simply Food store in the former JJB unit.

In respect of on-line sales and any threat this imposes upon the market, recent research has shown that most people try on clothes before a purchase. Shopping habits have become a multi-channel experience and the physical environment must embrace a balance over convenience and destination retail. Shopping centres are the preferred environment for those seeking fashion and footwear, specifically centres under single ownership delivering a cohesive experience within the additional facilities shoppers' demand.

In terms of market outlook, prime rents are generally stable with upward pressure on the super prime locations. Supply for quality stock is falling away with the emerging additional development pipeline beginning to look healthier. Demand is stable within core locations, although in areas identified for major development, demand may weaken for more secondary/second tier locations.

Ryden's prime retail rent index (covering Scotland's top twenty shopping locations, see chart below) has seen a continued rise this year, with increases during 2016 recorded in Glasgow, Edinburgh and Perth.

Retail rent index



Source: ONS/Ryden. Index baseline of 100 is at 2015.

Investment

Another Scottish Property Review... another Referendum. On this occasion the European Union Referendum has dominated the commercial property investment market over the past six months and dampened activity.

As the Scottish Referendum hangover subsided after 2014, the Scottish commercial property market had enjoyed a period of steady recovery. However this process slowed to a near standstill in Q2 2016. With many decisions delayed until post-EU Referendum, the unlikely result caused significant fall-out. Brexit clauses were exercised and many transactions that were under offer were either renegotiated or fell through.

As investor sentiment faltered, some of the larger retail funds suffered redemptions and were forced to act. Some devalued to dissuade withdrawals and sold liquid assets in short order. Others closed and some are only now beginning to re-open. Many fund managers have been forced to sell in order to retain liquidity and manage their cash positions.

On the sidelines certain investors have watched developments with interest and many have taken advantage of the perceived distress. Overseas and opportunistic investors expecting discounts of 10-15% from pre-Referendum levels have enjoyed some success. UK local authorities seeking income and able to borrow at interest rates of sub 2% with attractive loan-to-value ratios, have also taken advantage. Although the full implications of Brexit are far from clear, the weakness of Sterling continues to fuel demand from overseas investors.

All Property Total Returns for Scottish Property for the four quarters to June 2016 were recorded at 6.6%, a significant reduction on the equivalent period to June 2015 of 10.9% and below the IPD UK All Property Total return of 8.9%. It is apparent from data that the market was already slowing in the lead up to the EU Referendum. Although Scottish property enjoyed a better income return than UK property over the period, it suffered from negligible capital growth. In the aftermath of the Referendum it is certain that capital growth will have deteriorated and that total returns will have declined further.

Office Property

Investor demand for offices in Scotland over the last six months has been significantly impacted by the EU Referendum vote in June, both in the lead up to the vote and the aftermath of the unexpected outcome. Several large transactions stalled in the process, with deals either being renegotiated with incumbent purchasers, or in some cases purchasers taking fright and pulling out, leaving sellers to look elsewhere.

Transaction volumes have fallen with potentially three months lost due to the combination of the Referendum and the annual summer holiday period. In common with our last Review, most of the activity has again been centred around Edinburgh and to a lesser extent Glasgow, with Aberdeen seeing very little of the market action. Inevitably, activity is being influenced by the comparative strengths of occupier demand and prospects for rental growth in the three cities. Edinburgh continues to lead the way with investors attracted to tighter supply fundamentals as a consequence of the limited development in recent years and also a steady conversion of older office stock for residential use.

Earlier in the year, M&G Real Estate began the process of reducing the Scottish weighting of their Property Portfolio fund and the fruits of this strategy were realised to a significant extent by September with the conclusion of over £150 million of office sales comprising three buildings, two in Edinburgh and one in Glasgow. In Edinburgh, Triuva, the German real estate investor, acquired both Quartermile 4 (£68 million) and Waverley Gate (£63 million), two highly respected buildings for low yields in the 5%s, as outlined in the table of transactions. In Glasgow, 50 Bothwell Street, a higher yielding opportunity with an element of retail space, was acquired by FORE Partnership for £23.25 million, reflecting an initial yield of 8.42%.

In Aberdeen, only one transaction of any note occurred during the Review period. The latest building at Prime Four Business Park was completed in the early summer when 4,289 sq.m. was pre-let to Anderson Anderson & Brown, a local firm of accountants. This was subsequently acquired by an overseas client of Citi Private Bank for £17.242 million. At the time of writing, the sale of the new Wood Group HQ at Altens (CityPark 1), mentioned in our last report, was rumbling on after many months of negotiations, and hopefully a successful completion will be reported in our next edition.

Looking to the future, it is anticipated that the volume of office transactions will slowly increase as investors come to terms with the Brexit vote, albeit there will be residual uncertainty for some time yet. Edinburgh in particular continues to offer some substantial buildings including Saltire Court, one of the city's most prestigious assets, for £69 million. With many of the UK funds still in recovery mode following the Brexit vote, we anticipate that overseas buyers will continue to be the successful bidders for prime office buildings in Scotland as and when they become available in 2017.

Yields for prime stock in Edinburgh and Glasgow are estimated to remain in the 5.25% – 5.75% range. Aberdeen is harder to estimate due to the lack of recent transactions, although well secured prime Grade A buildings in the city would be expected to sell for around 100 basis points cheaper than in Edinburgh or Glasgow.

Total Returns for Scottish office property for June 2015 were 5.5%, a fall from 11.6% in June 2014, mainly as a result of Capital Growth reducing from 5.4% to minus 0.2%. In comparison, Total Returns for UK offices for June 2015 was 10.8%, although again falling from 20.7% a year earlier.

Office property investment deals include:

Address	Property	Purchaser
50 Bothwell Street, Glasgow	8,343 sq.m. Grade B Listed landmark office building. 88% income let to Standard Life Plc until December 2017. Retail units on ground floor let to Marks & Spencer, Costa and Superdrug on short to medium term income	FORE Partnership for £23.25 million (8.42%)
177 West George Street, Glasgow	1,834 sq.m. Grade B multi-let office building, c. 50% vacant with rental guarantees. Tenants include HSB Engineering Insurance and Royal College of Nursing	Private investor for £2.89 million (c. 9.6%)
Fintry House, Hamilton Business Park, Hamilton	3,601 sq.m. modern office building let to John Lewis on FRI terms expiring February 2020. Passing rent of £723,794 pa	Praxis for £4.6 million (14.83%)
Quartermile 4, Edinburgh	Multi-let office scheduled for practical completion 2016. Leased to FanDuel and Cirrus Logic for 15 year terms	TRIUVA for c. £68 million (c. 5.21%)
Waverley Gate, Waterloo Place, Edinburgh	Multi-let office at the east end of Princes Street. Tenants include Amazon, NHS and H&M	TRIUVA for c. £63 million (c. 5.7%)
Mercury House & Moyen House, Heriot-Watt University Research Park, Edinburgh	Multi-let office investment in Edinburgh's largest science park. Tenants include Computer Application Systems and Origo Services Ltd. WAULT of c. 5.5 years	Capability Scotland (for part owner occupation) for c. £1.175 million (c. 9.14%)
Hillside House, 1-4 Laurelhill Business Park, Stirling	Multi-let office, tenants include Toshiba Medical Systems Ltd and Central Scotland Valuation Joint Board. WAULT of c. 6.5 years	Private investors for c. £940,000 (c. 9.21%)
AAB Building, Prime Four Business Park, Aberdeen	4,287 sq.m. office building let to local accountants, Anderson Anderson & Brown for 15 years	Overseas client of Citi Private Bank for £17.242 million

Industrial Property

Following the slowdown in investment activity which was noted in our previous Review, the subsequent six months to October 2016 brought a further decline. While the summer holiday period is traditionally quieter, the impact of the EU Referendum was undoubtedly a factor, firstly in reducing supply coming on to the market in the run up and then wilting investor demand in the immediate aftermath.

Four months on the from the Referendum, investors are now returning to the market and some limited activity has been noted. However, as the deals schedule in the table highlights, there has been little to get excited about.

The market is also coming to terms with the reduction in vacant rates relief on the industrial sector and, while the very high occupancy levels across the Central Belt and Aberdeen markets will limit the immediate impact of the change, there is little doubt that property with current or imminent void exposure will be repriced to factor in this risk. This is most noticeable in secondary/tertiary buildings – with demolition becoming more common for obsolete units – but also for larger, single-let distribution units where net income is most volatile.

Demand for medium to long term income industrial opportunities remains steady and this is one of the few areas of the market where institutional buyers may currently emerge.

Multi-let estate activity has been particularly sparse, with a lack of stock in the market over the summer, although there are some larger deals in the pipeline. The exception is Catalyst Trade Park in Edinburgh which was acquired by Springfield Properties for a price reflecting just over 9%. Encouragingly, there are some larger deals in the pipeline, including Rockspring's disposal of Queenslie Industrial Estate in Glasgow as part of a portfolio.

Total Returns for Scottish industrial property for the 12 months to June 2016 were 9.5%, a fall from 13.2% in 2015, primarily due to Capital Growth reducing from 6.1% to 2.9%. In comparison, Total Returns for UK industrial for the 12 months to June 2016 fell to 11.7%, the previous figure being 16.8%.

Industrial property investment deals include:

Address	Property	Purchaser
Stephenson House, Hamilton Business Park, Hamilton	6,464 sq.m. modern purpose built warehouse with offices. Let to Babcock on FRI terms expiring in February 2025. Lease has fixed annual rental uplifts of 1.5% pa	Aprirose for £8.85 million (9.98%)
MKM Building Supplies, 71 Nuneaton Street, Glasgow	3,446 sq.m. single let industrial/trade counter facility. Let to MKM Building Supplies until August 2032. 5 yearly upward only rent reviews to the greater of 2.5% pa compounded or OMV	Savills Investment Management for £3.07 million (6.97%)
Catalyst Trade Park, Sighthill, Edinburgh	Multi-let trade counter investment. Tenants include Multi-Tile Limited, Stevenswood and the National Trust for Scotland. WAULT of approximately 4.25 years	Springfield Properties for c. £2.55 million (c. 9.13%)
Badentoy Avenue, Badentoy Park, Portlethen	1,095 sq.m. industrial unit let to Aker Solutions for 5.5 years	Danobe Securities for £1.2 million (8.85%)
Unit 1, Dyce Avenue, Kirkhill, Aberdeen	2,400 sq.m. training centre let to Bristow Helicopters for 13 years	Private overseas investor for £7.5 million (7.32%)

Retail Property

The retail property investment sector has enjoyed rather selective activity over the Review period, once again due in large part to the disruption caused by the EU Referendum. The steady recovery that the sector had been experiencing as the occupier market stabilised has stalled, as investors pondered a number of negative factors, including reports of a decline in consumer confidence and continued tough trading conditions highlighted by high profile failures such as BHS and Austin Reed.

The uncertainty surrounding the retail sector has resulted in a more bearish approach. A narrower definition of prime and a more defensive approach to stock selection are two consequences of the present market. Particular regard is being paid to tenant covenant, the true rental value of retail accommodation and the implications of default/void on cash flow and in turn upon pricing. The perception of risk has increased, and in turn this is being reflected in the pricing of assets. Pricing has however remained firm for well-secured prime and good secondary High Street assets, with continued demand from private, overseas and pension fund investors.

Post-Referendum, a number of larger retail assets have come to the market. Interest in these multi-let retail warehouse and shopping centre assets seems to be confined to specialist funds, overseas investors and opportunity funds. There is a significant weight of money seeking core-plus and value-add stock of this nature, however the aspirations of these investors for higher returns will inevitably demand a discount in pricing.

Retail property investment deals include:

Address	Property	Purchaser
Bothwell Road, Uddingston	1,301 sq.m. modern high quality retail scheme let on long term income to Marks & Spencer, Costa and Domino's	Private Irish investor for £4.95 million (5.68%)
Clyde Retail Park, Clydebank	13,847 sq.m. open class 1 retail park weighted average unexpired lease term of 7.9 years. Tenants are TK Maxx, KFC, Home Bargains, Matalan, GO Outdoors and Halfords	Valad for c. £17.1 million (c. 7.3%)
Corstorphine Retail Park, Edinburgh	Multi-let retail park on arterial route west of Edinburgh city centre. Tenants include DSG Retail Ltd, McDonald's and Cancer Research UK	Ropemaker Properties Limited for c. £13.28 million (c. 7.39%).
Rose Street, Edinburgh	Mixed use multi-let retail and office investment of three city centre buildings. Tenants include ECCO Shoes, Timpson, Flight Centre, Macmillan Cancer Support and Scottish Women's Aid	Hazeldene House for c. £8.8 million (c. 8.45%).
2-4 Shandwick Place, Edinburgh	Prominent retail unit let to Greggs on a 15 year FRI lease subject to tenant break options in years 5 and 10	Private investors for c. £1.72 million (c. 5.21%)
Shandwick House, 67-83 Shandwick Place, Edinburgh	Mixed use property comprising three retail units at ground floor with four floors of office accommodation above. Tenants include Savers, Ryman and Skills Development Scotland	Westerwood Development Company for £4.65 million (c. 7.81%)
Edinburgh Retail Portfolio	Portfolio of seven city centre retail investments and one restaurant investment	Private family trust for c. £4.7 million (c. 6.6%).
Stoneywood Road, nr Dyce	1,486 sq.m. retail unit let to Marks & Spencer for 20 years	Private investor for undisclosed sum – quoting price £4.1 million (5.5%)
Argyll Road, Dyce, Aberdeen	530 sq.m. petrol filling station let to Certas Energy for 15 years	Sydney & Arbroath Properties for £1.25 million (6.44%)
57-69 Union Street & 1-9 Market Street, Aberdeen	2,029 sq.m. retail and leisure unit multi-let including Sports Direct and Poundland with WAULT of 5 years	Hunter UK Retail Trust for £7.66 million (8.91%)

It is encouraging to see that TH Real Estate has secured an alternative funding partner for Edinburgh St James where Dutch pension fund APG is taking a 75% stake in the regeneration project with TH Real Estate retaining a 25% interest. This has the potential to significantly elevate Edinburgh as a retail centre and transform the east end of the city centre.

The leisure market continues to thrive and investor demand for this sector is burgeoning both in terms of standalone restaurant units and larger, mixed leisure use schemes. The appeal of strong covenants, long leases and geared uplifts is apparent and it will be interesting to see how the £75 million sale of Omni, Edinburgh's prime leisure centre, is received by the market.

Total Returns for Scottish Retail property for the 12 months to June 2016 were 6.2%, down from the 8.7% recorded in the year to June 2015. The decline in capital growth from 2.8% to a negligible 0.6% was the principal contributor with income return broadly similar. In comparison, total returns from UK Retail property over the same period registered a more pronounced decline from 11.1% in June 2015 to 6.5% in June 2016, with capital growth declining from 5.5% to 1.3%.

Outlook

The uncertain outlook for the UK economy seems set to continue as the terms of the proposed exit from the EU become clearer. Meanwhile the outlook for the Scottish economy is further complicated by the recent announcement from the First Minister of the intention to publish a new Independence Referendum bill.

A second independence referendum could have serious consequences for the Scottish commercial property market, which prior to the EU referendum had been enjoying a steady recovery. The further layer of uncertainty that this would create would inevitably drag upon investment and development within the Scottish market and adversely affect commercial property values.

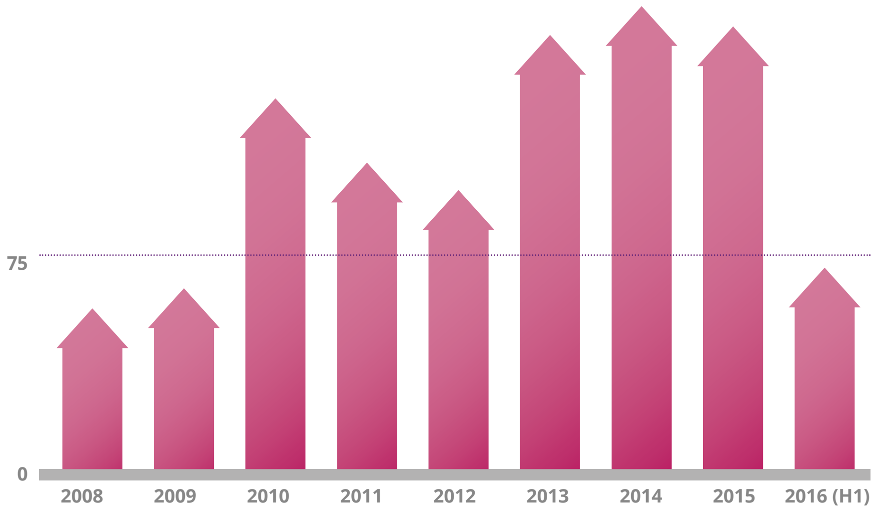
Investment into key sectors of the Scottish property market (such as Edinburgh offices and Central belt industrials) in order to stimulate activity and economic development is already being curtailed by risk aversion. The uncertain landscape is not helpful and is having an adverse impact on both occupiers and investors.

It is anticipated that transactional volumes will decrease over the short to medium term as the redemption pressures experienced by a number of the larger retail funds subside. Interest in prime, core-plus and value-add opportunities will continue from UK and overseas investors. UK institutional investment in the Scottish market is expected to be selective at best.

The healthy appetite of investors for alternative sector stock appears set to continue. Long income student, hotel and serviced apartment developments remain in demand and with a weight of money seeking such defensive opportunities it is anticipated that pricing will continue to improve for such assets. Many of these assets will offer a hedge against inflation if, as anticipated, this begins to rise.

Investment tracker:

Number of transactions over £1 million in Scotland



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We are grateful for the assistance of CoStar and MSCI/Investment Property Databank (IPD).