KEY POINTS

- Commercial property in Northern Ireland posted a total return of 7.0% y/y in 2013. This is a marked turnaround in performance following a negative return of -0.4% y/y the year prior;

- Capital values in Northern Ireland have fallen 33% since the peak in 2006. However, the maintenance of strong levels of passing rent has resulted in a high level of income return which grew to 8.9% y/y in 2013. This means that assets are discounted but with the benefit of highly competitive income streams;

- Market rents recorded their first significant increase since the market crash, with average rental values growing by 2.8% y/y for commercial property. This is clear evidence of the improved confidence of occupiers, especially in the retail sector;

- Belfast property recorded a positive total return of 4.5% y/y outperforming a number of key European cities including Amsterdam, Barcelona and Lisbon;

- Equivalent yields remained stable between 2012 and 2013 at 8.0%, suggesting a stabilising in investor sentiment as the broader recovery begins to take hold.

**FIGURE 1: PERFORMANCE SUMMARY, % Y/Y**

<table>
<thead>
<tr>
<th>Component</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income return</td>
<td>+8.9%</td>
</tr>
<tr>
<td>Capital growth</td>
<td>-1.8%</td>
</tr>
<tr>
<td>Cross product*</td>
<td>-0.1%</td>
</tr>
<tr>
<td>Rental value growth</td>
<td>+2.8%</td>
</tr>
<tr>
<td>Yield impact</td>
<td>-3.2%</td>
</tr>
<tr>
<td>Residual*</td>
<td>-1.4%</td>
</tr>
</tbody>
</table>

TOTAL RETURN 7.0%

Year end: 43 properties valued at £677.1 million

* Cross product: capital gain/loss in reinvested income
** Residual: impact of delays in income stream, mainly effect of over-renting

Source: MSCI Real Estate - IPD
The improving performance of UK commercial property throughout 2013 along with the significant rebound in the Republic of Ireland has helped bring investor returns from Northern Ireland commercial property back into positive territory. Total returns from UK property grew to 10.7% y/y, up from 3.4% y/y in 2012. The turnaround in performance in the Republic of Ireland was more dramatic as returns climbed to 12.7% from 3.0% the year prior.

Performance of property in the Northern Ireland followed improving market trends in the rest of the UK. Traditionally, the Northern Ireland sample had followed that of the broader UK market, posting positive total returns in 2010 and 2011 as the UK market stabilised after the crash rather than aligning with the market in the Republic of Ireland which suffered continued declines until late-2011. Figure 2 illustrates total return trends in the Northern Ireland market between 2007 and 2013.

**FIGURE 2: TOTAL RETURN PERFORMANCE, 2007-13, % Y/Y**

![Graph showing total return performance from 2007 to 2013.](Image)

Source: MSCI Real Estate - IPD
For the year ending December 2013, commercial property in Northern Ireland produced a total return of 7.0% y/y, improving from the negative -0.4% y/y performance posted in 2012. The enhancement in total returns was largely due to a strengthening income return as continued declines in capital values weakened over performance.

Income return has averaged 7.6% y/y over the 32 years IPD has been analysing investor performance in Northern Ireland, with the 8.9% y/y posted in 2013 amongst the highest annual income rate across the time series. Positive income return along with the fact that capital values remain heavily discounted makes assets in Northern Ireland highly competitive. This has clearly tempted further investors into the market with transaction volumes up from previous years.

Crucially, rental values recorded their first significant growth since the market crash with rents appreciating by 2.8% y/y on average across Northern Ireland in 2013. This contrasts with an average decline of 7.8% y/y in 2012. Overall, rental values have only fallen by a modest 11.3% since rents peaked in 2008, compared to an average decline of 47% in the Republic of Ireland. This is more in line with the rest of UK market where rents stood at 7.2% off their previous peak at the end of 2013.

Drivers of performance
The improvement in market rental values during 2013 set a positive tone for Northern Ireland property in 2013, despite the continued decline in capital values. The growth in rents suggests that there is growing competition from occupiers for space, especially in the retail sector, and further implies that retailers expect trading conditions to improve in coming years. This positive trend is illustrated by Figure 3 which shows the key drivers behind total returns over the last five years.

Total return is made up of two components; capital value growth and income return. In turn, capital value growth is primarily driven by rental value and yield movements, with a residual element that reflects valuer perception of the risk to the future cash flow.

Income return remains positive provided rent being collected exceeds the investors’ expenses, improving income (passing rent) levels push income return higher while declining capital values have a similar effect provided passing rent is stable. This means that income return plays a dual proxy role of occupier and income risk in the market. The increased level of income return during 2013 in the Northern Ireland market was due to capital values continuing to decline, at -1.8% y/y, given that passing rent also fell by -0.7% y/y.

Source: MSCI Real Estate - IPD

FIGURE 3: DRIVERS OF TOTAL RETURN, 2009-13, % Y/Y
BELFAST MARKET IN CONTEXT

This analysis compares the Belfast commercial property market with 15 other key cities across the European Union. Belfast property returned 4.5% y/y in 2013 below the European average of 5.9% y/y but outperforming many major European cities including Lisbon, Barcelona, Amsterdam and Copenhagen.

The underperformance of Belfast was due to the continued contraction in capital values, which fell by 3.7% y/y, while the stronger markets, including Dublin and London, outperformed due to their impressive levels of capital value growth. These comparable markets are illustrated by Figure 4. Overall, capital value growth averaged only 0.5% y/y across Europe as declines in Spain, Portugal and Italy pulled the performance downwards.

Belfast returns were bolstered by a high level of income return, at 8.5% y/y, which was the second highest recorded after Dublin’s 9.3% y/y. The average income return for 2013 in Europe fell from 5.5% y/y to 5.4% y/y as risk receded somewhat from 2012. The high level of income return in the Belfast market makes it highly competitive to new investors looking at buying, particularly given that tenant risk is largely similar to the rest of the UK reflecting the pre-dominance of retailer multiples.

FIGURE 4: BELFAST VERSUS KEY EUROPEAN CITIES IN 2013, % Y/Y
The IPD commercial property sample for Northern Ireland comprised 43 properties with a total capital value of £677 million as at the end of December 2013. The average lot size of assets in this sample was £15.7 million as at the end of 2013, of which 88% were retail sector assets. Figure 5 illustrates the sample breakdown, by capital value, for each commercial property sector in 2013.

**TABLE 1: TOTAL SAMPLE SIZE**

<table>
<thead>
<tr>
<th>Sector</th>
<th>No. of properties</th>
<th>Value £m</th>
<th>% of Total Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>ALL PROPERTY</td>
<td>43</td>
<td>677.1</td>
<td>100</td>
</tr>
<tr>
<td>RETAIL</td>
<td>29</td>
<td>593.7</td>
<td>88</td>
</tr>
<tr>
<td>OFFICE</td>
<td>6</td>
<td>29.0</td>
<td>4</td>
</tr>
<tr>
<td>INDUSTRIAL</td>
<td>3</td>
<td>30.0</td>
<td>4</td>
</tr>
<tr>
<td>OTHER</td>
<td>5</td>
<td>24.5</td>
<td>4</td>
</tr>
</tbody>
</table>

*Source: MSCI Real Estate - IPD*
ABOUT IPD | AN MSCI BRAND

IPD is a leading provider of real estate performance and risk analysis, providing critical business intelligence to real estate owners, managers, brokers, lenders and occupiers worldwide. Our unique database holds searchable information on 79,000 properties, valued at approximately USD 1.7 trillion, which are located in 33 countries, with a long performance history (25+ years) and which are mostly appraised quarterly.

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* INREV/ANREV Fund Manager Survey 2012  
** MSCI 2013

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