
Charterhall Drive, Chester - Office Market Assessment and Report





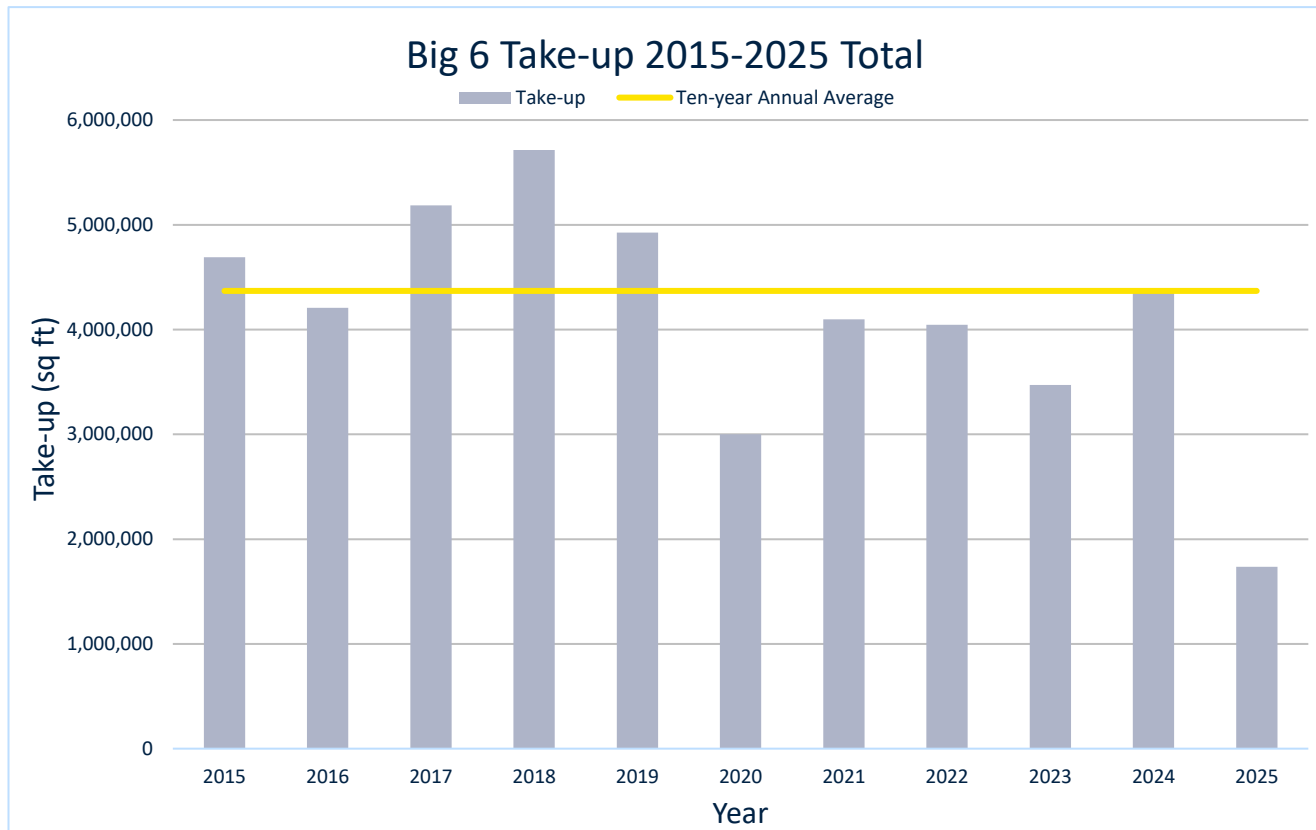
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1. The UK Office Market

The office market throughout the UK has experienced a tumultuous period since 2019. The global pandemic caused seismic shifts in the way businesses operated particularly in respect of their working patterns. The forced lock downs and consequent increase in prevalence of home working caused arguably one of the largest behavioural changes in the way businesses demanded and used office space.

The immediate short term outcome of the pandemic was a significant reduction in global demand for offices as businesses initially delayed relocations and capital expenditure projects. This resulted in an immediate slow down in demand for office space in all UK regions and an excess of supply. Following the end of the pandemic, significant uncertainty remained within the market attributable to the increase in agile working (work from home) and lack of clarity around how much space businesses would require into the future. This further delayed decision making from businesses who were considering an office relocation and created an environment of uncertainty which continued to impact office demand. As time has passed and organisations have slowly drawn conclusions around working patterns, demand has gradually returned to levels similar to that of long term averages. It should however be noted that despite this structural shock now alleviating, more traditional cyclical challenges associated with inflation, interest rate rises and economic uncertainty has presented further challenges to the office sector more generally. The below table illustrates these trends across larger UK office markets. (Please note Big 6 refers to Birmingham, Bristol, Edinburgh, Glasgow, Leeds and Manchester).



Since the end of the pandemic there has been much debate over the occupational preferences of businesses and how demand has changed. The majority of businesses recognise that there remains a need for an office citing its importance in attracting talent, building a corporate culture and driving productivity. What is less clear is the impact agile working has had on the size of office requirements. Initial thinking post pandemic was that demand would be impacted by as much as 50% as significant home working reduced the overall need for as much office space. In reality this has not played out and our house view is that the majority of occupiers (assuming no business growth or retraction) have reduced their spatial requirements by circa 10%. This however is highly nuanced and should only be treated as a broad rule of thumb.

Locational preferences remain a very business specific decision. More businesses see a City Centre location as preferable with retail and leisure amenity being a major draw for colleagues. This however is more applicable to large metropolitan areas with multi-mode public transport systems. Furthermore this trend is highly nuanced and dependent upon industry type. For example, professional services have a strong bias towards City Centres whereas more car dependent business with a sales function may favour Business Park locations.

Building amenities and sustainability continue to be a major factor in the decision making of businesses and a high priority. Strong energy performance is critical as is the provision of end of journey facilities e.g. showers, bike racks and lockers and more general break out / conferencing facilities. These factors have further fuelled build cost inflation.

2. The Chester Office Market

The Office market in Chester was traditionally made up of various smaller office buildings within the City Centre and a much larger scale offering at Chester Business Park. This Park was developed over several years and constitutes c. 1.2 million sq ft across a number of buildings.

More recently the "HQ" office building was developed (2009/10) providing circa 60,000 sq ft of Grade A office space within a mixed use scheme. At the time this was best in class office space within Chester and subsequently bought by the council for their own occupation. Shortly thereafter the building was reoffered to the market by the council to let. Leasing success was slow and the office void took several years to lease up.

In 2016, One City Place, a new Grade A, BREEAM Excellent office building completed adjacent to Chester Railway Station. The building measures 70,000 sq ft in total and is now fully let. Relevant characteristics of the office are as follows:-

- Multi Let with x8 different occupiers
- Lettings ranging in size from 2,000 sq ft to 24,000 sq ft
- The building took approximately 5 years to lease in its entirety
- Rents ranging from £18.44 psf to £23.80 psf
- A combination of 10 year leases (some with 5 year tenant only break options) and 5 year leases.

The leasing performance of this particular asset provides an excellent indication of the key market characteristics of the Chester office market. They are:-

- Large lettings of 10,000 sq ft or more are uncommon in the City. One City Place secured a letting of 23,600 sq ft, while all other lettings were below 10,000 sq ft. This indicates a market preference for smaller lettings, which led the developer to divide floors at One City Place, resulting in additional costs.
- Chester is characterised by a relatively small office market, which generally results in longer leasing periods. In 2024, approximately 130,000 sq ft of office lettings occurred across Cheshire West and Chester through 65 transactions, with around half of these in Chester City Centre.
- Rental growth in Chester has been limited. The initial letting at One City Place to RSM in September 2016 was agreed at £18.44 psf. Although rents between £20.00 and £23.00 psf were achieved in two cases (both involving an existing occupier, possibly reflecting a special purchaser premium), the most recent transaction was completed at £19.31 psf. This reflects a rental growth of 4.72% over about six years, equating to 0.79% per annum. This compares unfavourably to Big 6 average rental growth of approximately 3.4% per annum.

Active demand

Currently demand within Chester remains steady with the following live requirements considering a potential relocation:-





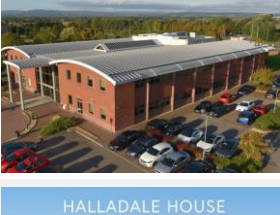

1. Oxbury Bank – Currently based in 2 separate offices, Oxbury are considering a wholesale relocation of 20,000 sq ft or alternatively acquiring a third separate office of c. 8,000 sq ft.
2. Mitchell Charlesworth – requirement for c. 6,000 sq ft
3. Alstom Engineering – early stages of a requirement for c. 6,000 sq ft
4. Undisclosed clients of Canning Oneil – 5,000 sq ft
5. Undisclosed clients of CBRE – 5,000 sq ft

This represents typical demand for Chester with a bias towards smaller requirements and no one sector being particularly dominant. Furthermore the majority of these requirements, as would normally be the case, are incumbent Chester businesses seeking to relocate. Consequently, there is very limited net erosion of office space and generally such businesses are moving out of office space which would subsequently be refurbished and added back into the available supply of office space (assuming such buildings are not then converted to alternative uses).

It is challenging to determine specific location preferences for business demand in the Chester market, as choices have typically depended on availability rather than desire. Throughout the UK, however, there is a clear trend toward prime locations, mainly due to occupiers seeking to attract staff with good connectivity and proximity to retail, leisure, and amenities. For Charterhall Drive, while the railway station may appeal to some businesses, most would likely prefer a comparable Grade A office in Chester city centre with better access to shops, cafes and general amenities.





Schedule of Comparables

We highlight below a schedule of recent office lettings. This reinforces the relatively small nature of office transactions (sub 10,000 sq ft) in disparate locations and at a rental tone of sub £20.00 psf.

Building	Building Name	Tenant	Transaction details
	HQ	Springer Healthcare (7,400 sq ft)	Rent – £20.00 psf Lease term – 10 years (5 year break) Date – Aug 2024
	Knights Court	DTM Legal (6,600 sq ft)	Rent – £17.50 psf MRF Lease term – 10 years (5 year break) Date – Nov 2024
	27 Newgate Street	GHD Engineering (3,654 sq ft)	Rent – £15.00 psf Lease term – 15 years (5 year break) Date – March 2024
	Carlton House	Anchor Security (6,275 sq ft)	Rent – £15.00 psf Lease term – 5 years (no break) Date – Dec 2023
	Foundation	Xeniadin (7,500 sq ft)	Rent – £22.50 psf Lease term – 10 years (5 year break) Date – April 2025
	Halladale	Tute Education (4,523 sq ft)	Rent – £20.00 psf Lease term – 11 years (6 year break) Date – March 2024

Existing Supply

We highlight below the available accommodation within Chester City Centre. Please note the below represents a selection of higher quality office availability, other lower grade office accommodation is also available to let.

Building	Building name	Availability	Comment
	Nicholas House	20,000 sq ft	20,000 sq ft. The tenant has vacated and the owner is looking at refurbishment with a target rent of £22.50 psf Available from 5,000 sq ft +
	Gorse Stacks House	14,000 sq ft	30,000 sq ft. Virgin Money have vacated 14,000 sq ft and this is available for occupation at £15 psf
	Heronbridge House Chester business park	32,000 sq ft	32,000 sq ft available Refurbished office Grade A Will split floors £22.50 psf.
	Eden House Chester Business Park	5,209 sq ft	5,209 sq ft available Fully refurbished Grade A £22.00 psf

Future Supply

Office development across the UK is currently constrained by rising build costs, limited available equity, and higher investment yields due to increased UK Base Rates. As a result, speculative office development has largely ceased over the past year, a trend unlikely to reverse soon, especially in smaller markets like Chester. Refurbishing existing offices is now the preferred strategy, since it requires less capital and carries lower construction risk, addressing current market demand more effectively. In Chester, new office development is not viable without public sector support, as detailed further in this report.

3. Hypothetical Development

To illustrate the challenges in office development we have undertaken a hypothetical development appraisal based upon the following assumptions :-

- An office building of 80,000 sq ft net internal area (95,000 sq ft gross internal area)
- Build cost of £275 psf plus fees on the gross area (these figures have been provided by Arcadis) excluding fees
- Investment yield of 9% (please note One City Place is currently being sold and the likely yield will be 10%+).
- Zero land value
- Building 100% let within 2 years
- 15% return on cost to the developer

Based upon these assumptions the economic rent to achieve the 15% return on cost would be £48.55 psf. This is c. 100% higher than any rent achieved by any building in Chester City Centre. For completeness we have undertaken some sensitivity analysis and altered both build cost and investment yield in a more bullish direction. This is illustrated in the table below and even with these “blue sky” assumptions the rents required are significantly higher than anything achieved in Chester (and Liverpool).

Build Cost (psf)	Yield	Rent (psf) required to achieve 15% Profit on Cost
£250	8%	£38.95
£275	8%	£42.85
£300	8%	£46.75
£250	9%	£44.15
£275	9%	£48.55
£300	9%	£53.00

Please note we have based the build cost on advice received by Muse and based on our knowledge of current schemes being considered elsewhere in the North West. Arguably the build cost would be marginally lower at an out of Town scheme such as Chester Business Park based on the assumption that a site on a business park is likely to be more easy to develop from a practical perspective than a busy City Centre location (e.g. road stopping, construction management etc). Assuming a reduction in build cost due to minimal ground remediation (we have been advised this would reduce build costs by c. £115,000) this moves the target rent to £48.35 psf.

This is a hypothetical appraisal to illustrate the challenges associated with office development in a city such as Chester. In our opinion the principle of this type of development is entirely unfeasible at this time. This is partly due to the economics of any appraisal along with no appetite from investors to deploy capital into this type of development situation.

4. Conclusions

The Chester office market is characterised by a predominance of existing occupiers relocating within the City with limited examples of new occupiers taking amounts of office space. Consequently the market is best described as “churn” driven with space being recycled and then relet upon lease expiry.

The two examples of new development over the last 16 years, “HQ” and One City Place, took several years to lease (albeit HQ was bought by an owner occupier and subsequently relet). Rental growth and investment performance has been weak in both assets.

Chester Business Park has for many years provided different sizes and grade of office accommodation that has generally catered for much of the demand in the area. A combination of available offices in this location as well as high quality refurbishments are likely to cater for ongoing demand in Chester in the near term, with ongoing churn in the market also likely to contribute to the supply in future years.

Projecting forward, future office development in Chester is highly unlikely to occur as consequence of the economic challenges faced by the development industry. Hypothetically if capital were available to develop, rents would need to be at record levels (£48.00 psf +) to make any such development remotely viable.

Turley Office
5th Floor
Transmission
6 Atherton Street
Manchester
M3 3GS

0161 233 7676