Research

Central London office analysis

Q3 2016

The White Chapel Building, E1

Our City Agency team has acquired c.13,400 sq ft on behalf of The Shipowners' Protection Ltd

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Central London
Market comment

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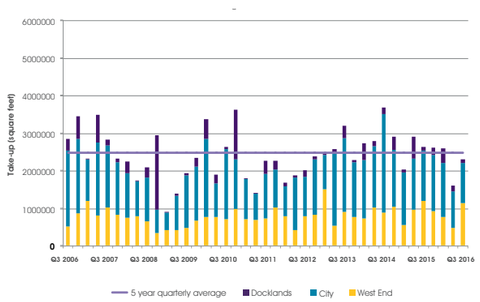
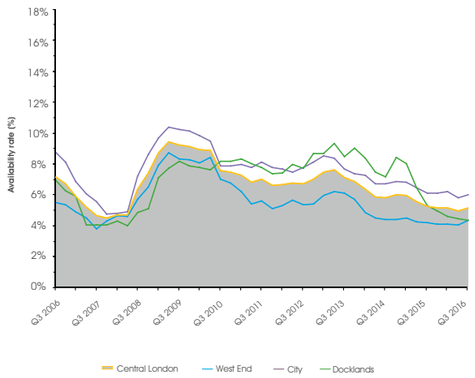
Central London take-up
Source: Bilfinger GVA, EGi, CoStar



Central London office availability rates
Source: Bilfinger GVA, CoStar



Welcome to Bilfinger GVA's central London office analysis; our detailed view of the market in Q3 2016.

The B word

The summer is traditionally a quiet time for the property market, with many decision makers on holiday or taking stock. During July and August, whilst activity was relatively sparse, speculation was in overdrive with forecasters, politicians, business leaders and agents all keen to have their say on what the results of the EU referendum might mean for the economy and the markets.

Whilst we are still yet to gain much insight into the future, the only thing we know for certain is that much uncertainty remains. This is already affecting confidence and confidence is everything.

For those looking for good news stories, there are some to be found. Without question the big news of the quarter was the pre-letting of nearly 500,000 sq ft at Battersea Power Station to Apple. It is understood that the rent was just under £60 per sq ft. The letting in itself is a great boost not only for the market but also for London as Apple will not be taking occupation of the building until 2021 and shows that they still have a long term commitment.

Elsewhere, household names such as WeWork, Wells Fargo and The Economist all completed on deals during the quarter, with McKinsey's, ITV and Lego all rumoured to be under offer. However, even with such commitment, there remains a fear that some occupiers, particularly within the financial services industry are unsure of maintaining their headcount in London. Many occupiers will wait to see what will becomes of 'financial passporting' before they can make decisions.

Should I stay or should I go?

With continued uncertainty, we expect many occupiers who have a proposed moving date over the next 12 to 24 months to deliberate as to whether it is worth committing to large capital expenditure.

With landlords in a similar position and more likely to be thinking of postponing redevelopment or new build, it will be no surprise to see an increase in short-term letting in those situations where it is mutually beneficial.

Revaluation time

Business rates will be changing on the 1st April 2017. It has been seven years since all non-domestic properties were nationally re-valued. The 2017 Revaluation will be based upon rental levels at 1st April 2015 and will form the basis of the business rates liability for the next five years.

The draft 2017 rating list was published at the end of September. Our Business Rates team have looked in detail at values applied to offices across London and are able to provide you with information on the change in rates payable per square foot.

As expected, the biggest increases are seen in the fringe locations which have seen sustained rental growth since the last 2010 list valuation date of 1 April 2008. Of particular note Shoreditch is up 55%, Clerkenwell 46% and Kings Cross 63%. Elsewhere the City Core is up by 21%, whilst Mayfair values have remained static with the amount payable falling by 3% due to a reduction in the UBR.

However, these figures do not take into account transitional phasing which is still in the consultation process. The Government's preferred option to introduce a new band for properties with rateable value over £100,000 would cap increases to 45% in the first year. Conversely, decreases would be limited to only 4.1%, which would substantially limit the actual decrease in liability at Canary Wharf which has seen a substantial decrease in value from 2008.

If you would like more information on how this might impact your business, please feel free to get in touch.

Patrick O'Keeffe
Head of London Markets

Central London
Occupier market

Take-up

Central London take-up for Q3 2016 totalled 2.3 million sq ft, 60% up on the previous quarter, but 6.6% down on the five-year quarterly average of 2.5 million sq ft.

During Q3, activity was focused on the City and West End fringes, accounting for 613,100 sq ft and 1 million sq ft respectively. Apart from the fringe Docklands and West End markets, all other submarkets were down on the five-year quarterly average.

The largest deal of the quarter was at Battersea Power Station (SW8), where Apple committed to taking the six upper floors of the Boiler House. In the City, Wells Fargo completed on 220,000 sq ft at 33 Central (EC4) and WeWork took 62,000 sq ft at Aldwych House (WC2).

Take-up of newly completed space made up 402,500 sq ft (17%) of take-up for the quarter, with pre-letting making up an additional 901,900 sq ft (39%). Second-hand grade A take-up made up 27% of the quarterly total and 614,400 sq ft, with second-hand grade B space a further 17%.

During the quarter, six deals over 50,000 sq ft completed, compared to one in the previous quarter.

Availability

There is currently 8.5 million sq ft available across central London, increasing from 8.1 million sq ft as of the end of Q2 2016. The vacancy rate is now up to 4.2% in line with the levels seen during the first quarter of the year.

Availability is 2% down on the corresponding period last year when the vacancy rate was 4.5%, representing a reduction of just 162,000 sq ft in available space over the last 12 months.

Development

During the quarter, 11 buildings totalling 1.1 million sq ft completed.

The largest building to complete in the City was One New Street Square (EC4) where Deloitte's new 271,000 sq ft office finished construction. In the West End, work completed at Howard de Walden's 55,000 sq ft 66 Wigmore Street (W1), which is fully let to Schon Klinik.

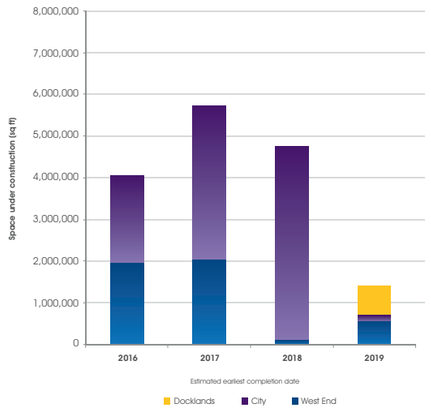
8 buildings totalling 1.2 million sq ft started during the quarter, following on from 1.1 million sq ft in the previous quarter. The largest starts were on the Southbank where 1&2 Southbank Place (SE1) went under construction.

There is currently 15 million sq ft under construction across central London, with 3.2 million sq ft (21%) due for completion before the end of 2016 and a further 5.7 million sq ft (38%) due before the end of 2017. Of the space currently under construction, 6.3 million sq ft (42%) has already been let, leaving 8.8 million sq ft of available space currently under construction.

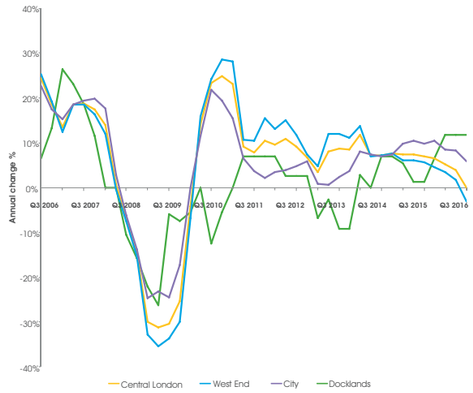
Rental growth

Central London prime rents fell for the first time since Q4 2009, after 26 quarters of consecutive growth. Prime rents decreased by 2.2% during the three months to end-September and are now at the same level they were this time last year. This can be attributed to the West End seeing a fall of 3.4%, whilst City and Docklands markets remained stable.

Central London office space under construction
Source: Bilfinger GVA



Central London prime rental growth
Source: Bilfinger GVA



Central London
Investment market

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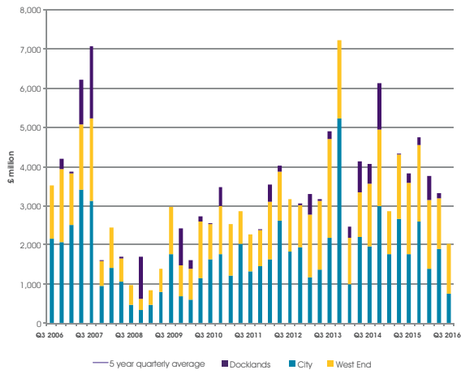
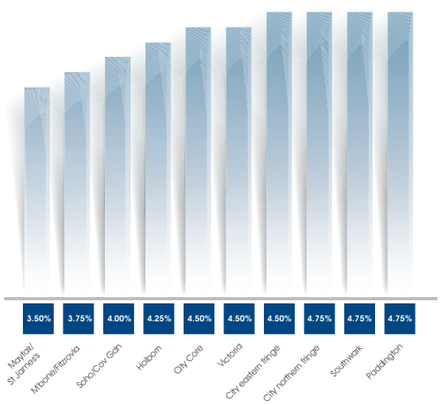
Central London office investment transactions
Source: Bilfinger GVA, PropertyData



Central London office yields
Source: Bilfinger GVA



Overview

A number of key transactions have completed in both the City and West End markets over the summer, which in this 'post-referendum' climate suggest that conditions are still favourable. Nonetheless, the market is undoubtedly subdued and we have not yet seen the normal flurry of activity that September and the beginning of Q4 usually bring.

The forced selling that was perhaps anticipated following the vote to 'Brexit' has not materialised, bar one or two exceptions.

Most active investors, be they UK or overseas, expect at least a small discount on pre-referendum pricing. Current exchange rates, should in theory make London more attractive than ever for overseas investors and UK investors seem to have renewed appetite following a brief pause in July/August but only if assets can be purchased at the 'right' price. With nobody wanting to overpay in this climate, and demand patchy, pricing has already come off slightly from June though it is not expected to soften further. .

There is an increase for vendors preferring to talk to Investors on a 'one on one' basis. We expect a number of rumoured high profile deals to be concluded on this basis, allowing the Vendor to sell with discretion and the Purchaser to buy without the competitiveness of a traditional 'best bids' situation.

Sales that are anticipated to be openly 're-marketed' will add to the levels of stock and should attract good interest if 're-priced' correctly. Significant examples are Samsung Life's Crown Place, Deutsche Fonds' 20 Moorgate, Aerium's 1 Wood Street and Orion House, all of which are back in the market with 'sensible' price reductions. However it remains to be seen whether or not there is sufficient appetite for such assets.

Transaction volumes

During Q3 2016, central London investment totalled just £2 billion across 42 deals, marking a 39% decrease on the previous quarter, when £3.3 billion was transacted, and a 47% decrease on the five-year quarterly average. This was the lowest level of investment since Q1 2010 and was £1.8 billion less than the corresponding quarter in 2015.

The West End saw £1.3 billion transacted, just 2% down on the previous quarter but 30% down on the corresponding period last year, and 17% down on the five-year quarterly average. The largest deal of the quarter was at 440 Strand (WC2) where RBS paid Henderson representing L&G £198 million for Coutts' HQ, representing a yield of 4%. In the core, the largest deal was Richemont Holdings' £198 million purchase of the Mulberry flagship store at 50 New Bond Street (W1).

In the City, just £757 million was transacted across 20 deals, 60% down on the previous quarter and 63% down on the five-year quarterly average. The largest deal of the quarter was Wells Fargo's owner occupier £260 million purchase of 33 Central (EC4). Elsewhere, clients of Westminster Real Estate purchased 33 Gracechurch Street (EC3) for £75 million, representing a yield of just under 5%, whilst Allegra sold 5 King William Street (EC4) to a private investor for £88 million, representing a yield of 3.7%. Whilst the City had a quiet quarter, we expect Q4 to be busier, with more stock being launched or relaunched to the market at the beginning of the quarter.

This quarter overseas money accounted for £1.2 billion (61% of total investment). Owner occupiers, primarily in the form of Wells Fargo, accounted for £290 million, and 14% of investment. UK property companies accounted for £129 million of investment for Q3 2016 (6%), whilst UK institutions were responsible for just 1% of total investment for the quarter.

During the quarter, there were seven purchases of over £100 million, with just one of those in excess of £200 million.

Yields

Q3 2016 saw yields move out 25 basis points in all submarkets. Prime yields in Mayfair and St James's are now at 3.5%, with City core at 4.5%. The market seems to have readjusted post-Brexit, although evidence continues to be patchy.

28 Fitzroy Square, W1

Bilfinger GVA have been advising the Magistrates Association on the sale of their headquarters at 28 Fitzroy Square and the purchase of a replacement building. The sale of Fitzroy Square has now exchanged.

West End Occupier market

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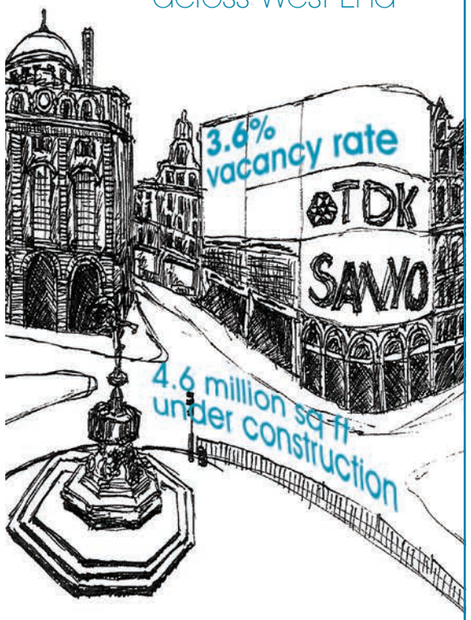
1.1 million sq ft let
31% up on 5 year
quarterly average

-3.4%

Quaterly rental growth
across West End



£115 per sq ft
prime rent

Take-up

Take-up during the quarter reached 1.1 million sq ft. Due to Apple, this was over twice that measured in the previous quarter and 31% above the five-year quarterly average. If we were to discount the Apple deal, take-up across the rest of the West End would be 30% up on the previous quarter but 25% down on the five-year quarrterly average.

The healthy take-up can be largely attributed to the largest deal of the quarter, which was at Battersea Power Station (SW8), where Apple committed to taking the six upper floors of the Boiler House (SW8).

During Q3 2016 pre-letting space accounted for 648,800 sq ft and 57% of take-up across the West End. Deals on recently completed space totalled just 182,700 sq ft, and 16% of take-up for the quarter.

Take-up of second-hand space made up 299,100 sq ft of take-up and 26% of activity for the quarter.

Availability

Availability increased from 2.7 million sq ft to 2.9 million sq ft during the quarter. The vacancy rate is now up to 3.6%, its highest since Q1 2016. Availability is 4% higher than this time last year, equating to 105,000 sq ft more space. Vacancy is still very low, and has been below 4% for 10 successive quarters.

Development

117,100 sq ft completed across the West End during Q3 2016. The largest building to complete was Howard de Walden's 55,000 sq ft 66 Wigmore Street (W1), which is fully let to Schon Klinik. In the core, British Land finished work on the 45,000 sq ft 7 Clarges Street (W1).

Just one building of 30,200 sq ft went under construction during the quarter, with Academy House now being refurbished. The building is due to complete in mid 2017. As of the end of Q3 2016, there is 4.6 million sq ft of development activity in the West End.

Rental growth

After two quarters of prime rents remaining stable, the third quarter of the year saw a decrease of 3.4% across the West End. This is the first decrease since Q4 2009, with the movement during the quarter resulting in prime rents being 3% down on the year.

In Mayfair and St James's, prime rents fell from £120 per sq ft with rent free periods at 15 months to £115 per sq ft with rent free periods at 18 months. Net effective rents are now £97.75 per sq ft, the lowest since Q4 2013 and 7% cheaper than the previous quarter. Super-prime headline rents fell from £150 per sq ft to £135 per sq ft, with rent free periods increasing from 15 to 18 months.

As well as the prime markets of Mayfair and St James's, the other market to see a substantial fall in prime headline rents was Marylebone, where rents decreased 8% from £97.50 per sq ft to £90 per sq ft. The only submarkets to see growth were Paddington and Vauxhall, with rent frees increasing in all but two of our submarkets.

10 Old Burlington Street, W1

Bilfinger GVA are disposing of 7.434 sq ft

City Occupier market

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Head of City and Docklands Agency

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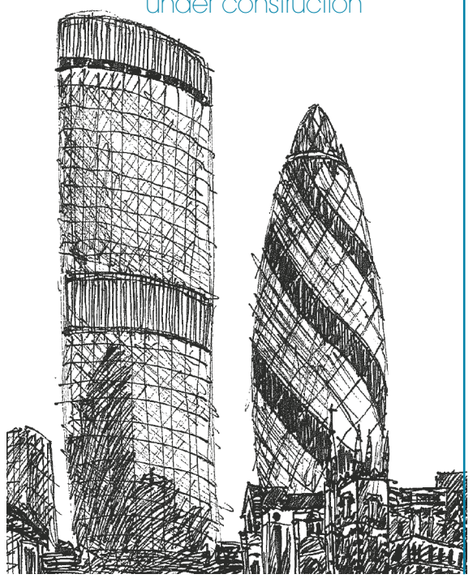
5.4%
vacancy rate

1.1 million sq ft
take-up, 12% up on Q2 2016

24% of take-up on pre-letting

£70.00
per sq ft prime rents

9.8 million sq ft
under construction



Take-up

Take-up during Q3 2016 totalled 1.1 million sq ft, which was 24% down on the five-year quarterly average but 12% up on the total measured in Q2 2016.

The largest deal in the City was Wells Fargo completing on 220,000 sq ft at 33 Central (EC4).

Pre-letting for the quarter made up 253,100 sq ft, 24% of total take-up, with take-up on new space accounting for 219,700 sq ft (21%). Second-hand space totalled 597,100 sq ft, and 56%.

Availability

Availability in the City increased slightly from 4.7 million sq ft to 4.9 million sq ft, with the vacancy rate increasing to 5.4%. Availability is 1.4% down on the corresponding period in 2015.

Development

During the quarter 986,900 sq ft completed across eight buildings, with the largest being Land Securities' One New Street Square (EC4). Other notable completions during the quarter include the 225,000 sq ft South Bank Central (SE1) and Derwent London's 185,000 sq ft White Chapel Building.

Construction started on 1.2 million sq ft across seven buildings during the quarter including 566,000 sq ft across 1 & 2 Southbank Place (SE1) and 165,000 sq ft at The Tower, The Bower (EC1).

There is now 9.8 million sq ft under construction in the City. Of this, 1.3 million sq ft is due to complete later in 2016, with 3.7 million sq ft earmarked for 2017. There is currently 4.6 million sq ft of space under construction due for completion in 2018.

Rental growth

Prime rents in the City remained stable during the quarter, meaning that in the last six months, rents have increased by just 0.3%. Prime rents are nevertheless up 6% on the corresponding period last year.

None of our submarkets saw rental growth during the quarter, whilst rent free periods increased in seven out of our ten submarkets. This means that on a net effective basis, prime rents are now cheaper than they were in Q2 in all but Clerkenwell, Shoreditch and Waterloo.

Prime headline rents in the City core remain at £70 per sq ft, 8% up on the year, with rent free periods increasing from 18 to 20 months. Net effective rents in the City core are now at £58.33 per sq ft.

Docklands Occupier market

Take-up

Five deals completed during Q3 totalling 101,600 sq ft, 36% down on the previous quarter and 48% down on the five-year quarterly average. Despite this, the Docklands fringe saw its highest take-up since Q3 2012, mainly due to Time Inc's acquisition of 40,300 sq ft across three floors at Scandinavian Centre (E14), at a rent of £30 per sq ft.

The second largest deal of the quarter was also done in the fringe, with British American Tobacco taking 20,800 sq ft at 4 Harbour Exchange (E14) at a rent of £34 per sq ft. The largest deal in Canary Wharf was HSBC taking 19,400 sq ft on part of the 24th floor at 25 Canada Square (E14).

Availability

Available space decreased from 710,000 sq ft to 696,000 sq ft during the quarter, with most of this space available on a sublet basis. The vacancy rate decreased from 3.7% to 3.6% during the quarter, its lowest since Q2 2008.

In the last year, availability in Docklands has decreased by 22%, a reduction of 195,000 sq ft. Despite this substantial fall, availability is still 11% higher than the peak of the last cycle.

Development

695,000 sq ft is under construction at 1 Bank Street (E14), due to complete in 2019. Elsewhere, Canary Wharf Group have submitted new plans for 10 Bank Street (E14), which would see a further 700,000 sq ft delivered to the market.

Rental growth

In Canary Wharf, prime rents remained stable at £42 per sq ft, with rent free periods at 20 months.

The disparity between asking rents for landlord space and space available on a sub-let from occupiers has reduced markedly over the last nine months. During this time, occupier space has reduced substantially.

Outside the Wharf, prime rents remain at £35 per sq ft with rent free periods at 21 months, whilst in Stratford prime rents increased are £40 per sq ft, with 21 months rent free.

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Director

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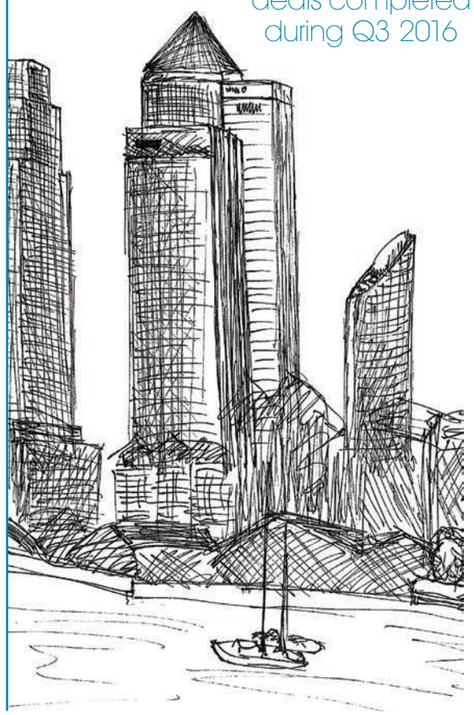
3.6%
vacancy rate

695,000 sq ft under construction, due before end-2019

101,600 sq ft
of take-up

Prime rents
£42 per sq ft

5
deals completed during Q3 2016



Midtown Occupier market

Take-up

Take-up during Q3 2016 totalled 202,100 sq ft, which was 41% down on the five-year quarterly average and 21% down on the total measured in Q2 2016. Take-up was the quietest since Q4 014.

The largest deal during Q3 was WeWork's acquisition of 62,000 sq ft at GI Partners' and Rown Strategic AM's 174,000 sq ft Aldwych House on a 20 year lease. Elsewhere, UCL signed for 23,500 sq ft at 1 St Martin's Le Grand, whilst Exterion Media took 22,800 sq ft at Lacon House.

Take-up of newly completed space accounted for 105,900 sq ft and 40% of take-up, with second-hand grade A space making up 85,220 sq ft. a further 32%. There was no pre-letting during the quarter.

Availability

Availability in Midtown increased slightly from 986,420 sq ft to 1.2 million sq ft, with the vacancy rate increasing from 2.6% to 3.4%. Availability is 14% down on the corresponding period in 2015.

Development

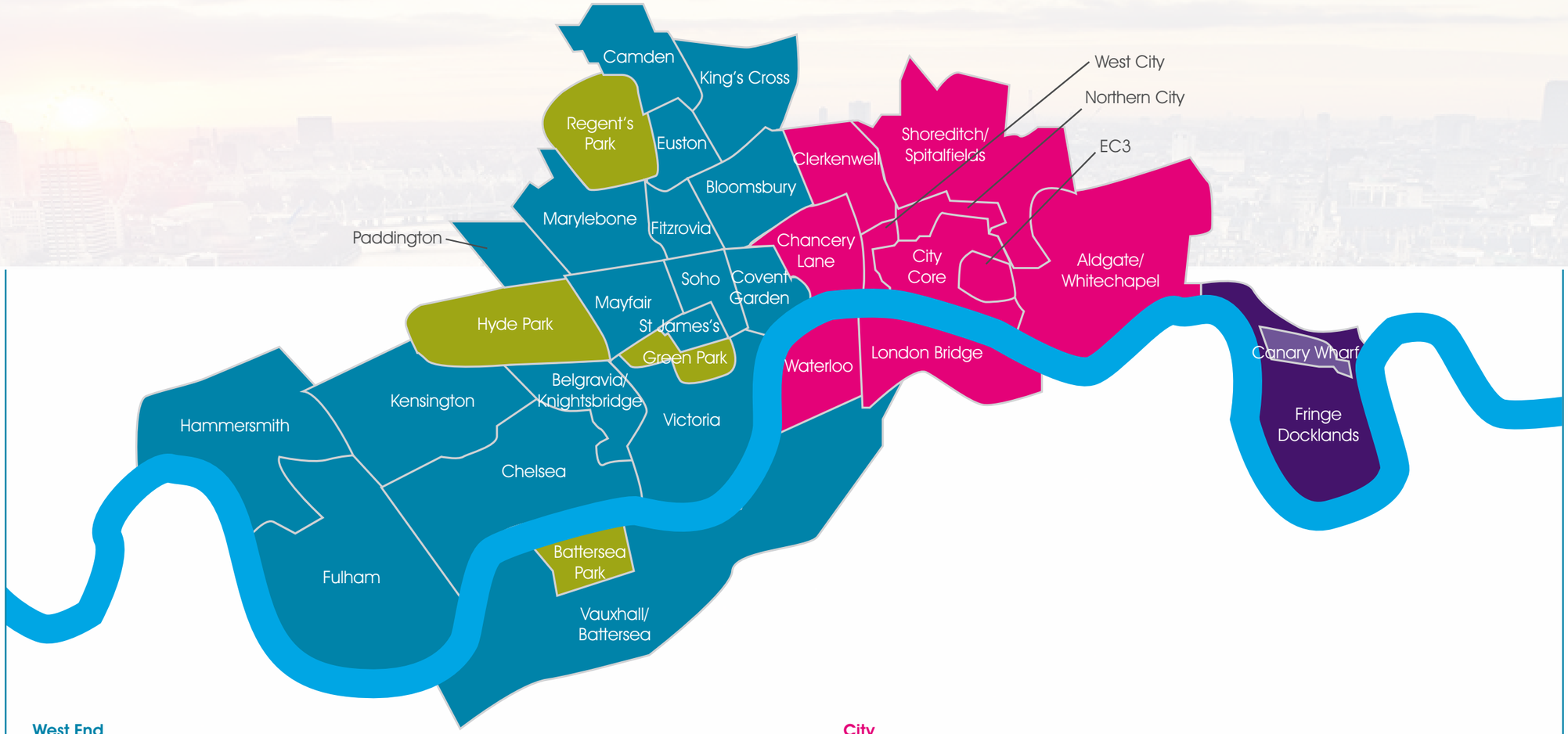
During the quarter 337,433 sq ft completed across three buildings, with the largest being Land Securities' One New Street Square (EC4). The other completions during the quarter were GE Real Estate's 66,500 sq ft 98 Fetter Lane (EC4) and Frogmore's 63,400 Weston House (WC1). There were no new starts during the quarter.

There is now 2.4 million sq ft under construction across Midtown. Of this, 509,900 sq ft is due to complete later in 2016, with 807,300 sq ft earmarked for 2017. There is currently 1.1 million sq ft of space under construction due for completion in 2018.

Rental growth

Prime rents across Midtown submarkets increased by 0.9% during the quarter meaning that prime rents are up 5% on the corresponding period last year.

Bloomsbury was one of few central London submarkets to see an increase in headline rents, from £72.50 per sq ft to £75 per sq ft. Rent free periods increase across all Midtown submarkets apart from Clerkenwell. In Holborn, prime rents remained stable at £65 per sq ft, with rent free periods increasing from 15 to 17 months.



West End

Area	Prime rent (£ per sq ft)	Rent free period (months)	Business rates	Total occupancy costs (inc. service charge and building insurance)
Belgravia / Knightsbridge	£95.00	18	£45.39	£150.64
Bloomsbury	£75.00	18	£25.50	£110.75
Camden	£55.00	18	£17.34	£82.59
Chelsea	£95.00	18	£33.15	£138.40
Covent Garden	£85.00	18	£28.56	£123.81
Euston	£75.00	18	£28.56	£113.81
Fitzrovia	£82.50	18	£26.01	£118.76
Fulham	£45.00	18	£16.32	£71.57
Hammersmith	£56.00	18	£18.87	£85.12
Kensington	£65.00	18	£23.46	£98.71
King's Cross	£82.50	18	£23.46	£116.21
Mayfair	£115.00	18	£46.92	£172.17
Mayfair/St James's "super-prime"	£135.00	18	£52.02	£197.27
North of Oxford St	£90.00	18	£40.80	£141.05
Paddington	£72.50	18	£26.15	£108.90
Soho	£95.00	18	£33.15	£138.40
St James's	£115.00	18	£46.92	£172.17
Vauxhall	£57.50	22	£15.10	£82.85
Victoria	£82.50	18	£30.09	£122.84

City

Area	Prime rent (£ per sq ft)	Rent free period (months)	Business rates	Total occupancy costs (inc. service charge and building insurance)
Central City Core	£70.00	20	£21.52	£101.77
Chancery Lane / Midtown	£65.00	17	£25.14	£100.39
City Eastern fringe	£57.50	20	£17.24	£84.99
Clerkenwell	£67.50	15	£14.28	£92.03
Insurance Sector	£65.00	20	£22.29	£97.54
London Bridge / More London	£63.50	18	£19.02	£92.77
Northern City	£65.00	20	£17.44	£92.69
Shoreditch	£65.00	15	£11.88	£87.13
Waterloo / Bankside	£63.50	15	£19.02	£92.77
West City	£70.00	20	£19.18	£99.43

Docklands

Area	Prime rent (£ per sq ft)	Rent free period (months)	Business rates	Total occupancy costs (inc. service charge and building insurance)
Canary Wharf	£42.50	20	£16.17	£68.92
Other Docklands	£35.00	20	£11.63	£56.88
Stratford	£40.00	21	£7.50	£57.75

London
Birmingham
Bristol
Cardiff
Dublin
Edinburgh
Glasgow
Leeds
Liverpool
Manchester
Newcastle

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