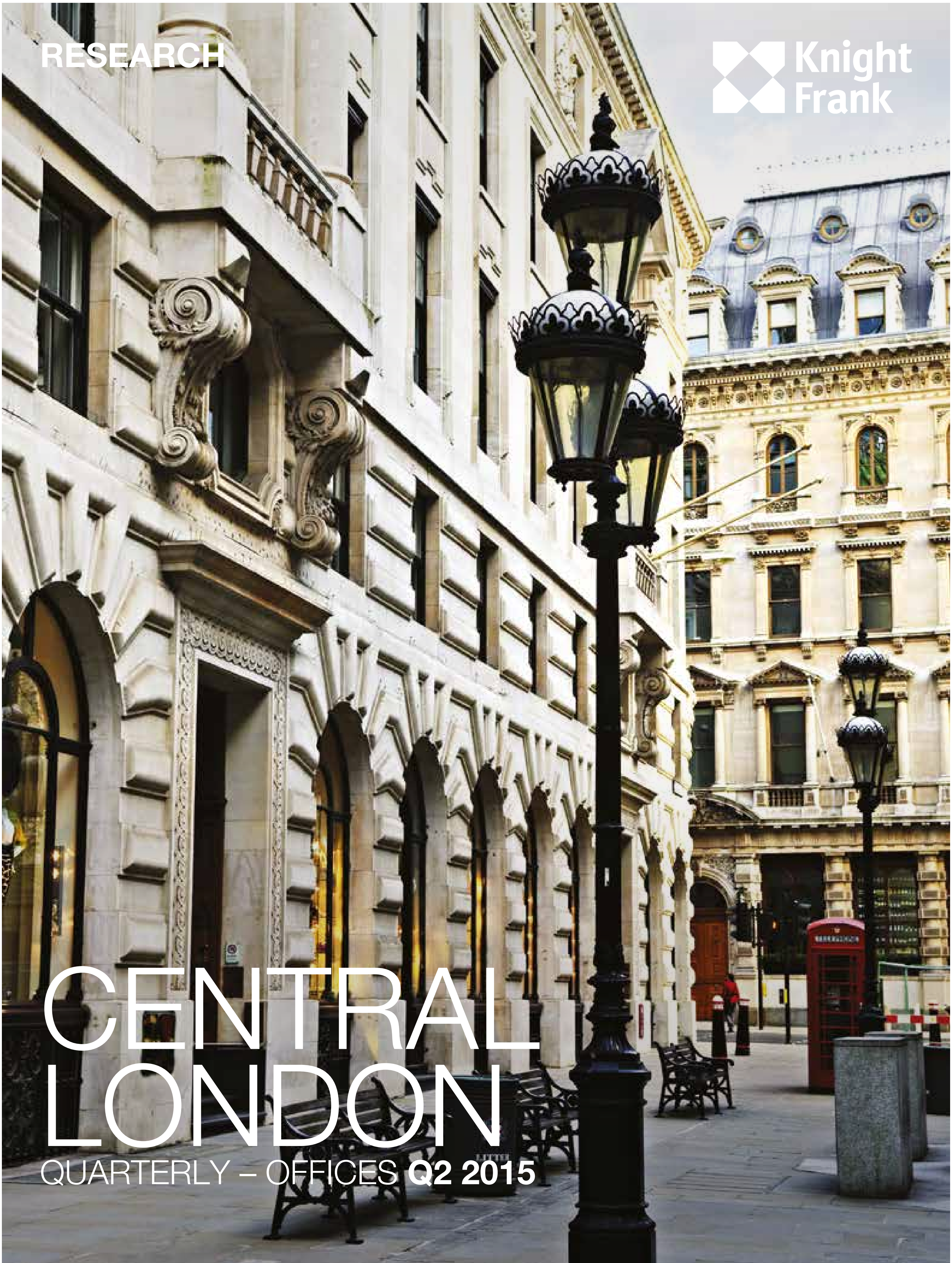


RESEARCH

Knight Frank

CENTRAL LONDON

QUARTERLY – OFFICES **Q2 2015**

TAKE-UP WELL ABOVE THE LONG-TERM AVERAGE

SUPPLY CONTINUES TO TIGHTEN

YIELDS STEADY IN CORE MARKETS

CHIEF ECONOMIST'S VIEW

The Q2 figures show leasing supply as tight, and developers are responding.

The second quarter has seen the vacancy rate drop to 4.8%, marking a fourteen year low.

Since quarterly records began in the early 1990s, the vacancy rate has only ever been at or below 4.8% during the period Q2 2000 and Q1 2001, which was the height of the 'dot com' mania, with an accompanying investment banking boom.

Back then an unprecedented surge in demand reduced supply to very low levels. This makes today's situation interesting, as demand is ahead of average but not booming as it was back in 2000-2001. The present supply crunch owes more to lack of development, due to a combination of the Euro Crisis deterring construction starts between 2010 and 2012 and limited availability of development finance during that period.

The concern for the market is that should the global economy hit fair winds in 2016 then demand could go higher still. Yet 2016 is a year in which it is no longer possible to deliver a brand new building, although refurbishments are still an option. The idea that next year the vacancy rate could once again match its Q3 2000 low of 3.3% looks plausible.

In short, unless the global economy moves into a fresh downturn in the meantime, 2016 looks set to be a good year for landlords. While the developers have recently responded to the shortage, the new development supply will arrive later not sooner. Between Q1 2015 and Q2 we have seen a net increase of 2.5 m sq ft in speculative space under construction, but 78% of the new starts will complete in 2017 or 2018.

For 2016, there is 3.6 m sq ft of speculative development set to complete, but take-up for new build and refurbished space in the last twelve months has been 6.3 m sq ft in central London. Even the 2017 and 2018 pipelines look thin, at 1.5 m and 1.3 m sq ft respectively. Developers with ready-to-go sites are looking well positioned.

The above, from a landlord or developer's perspective makes for upbeat reading, but it comes with the caveat that development activity is picking up. The volume of speculative construction is up 34% quarter-on-quarter, and 86% year-on-year.

At the time of writing the pipeline still looks inadequate, despite recent increases. However, the development pendulum is on the move.

FIGURE 1
Central London take-up by quarter & sub-market
Q2 2014 - Q2 2015 (000's sq ft)

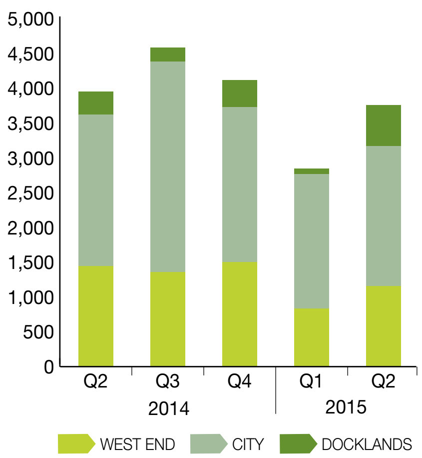


FIGURE 2
Central London availability by quarter & sub-market
Q2 2014 - Q2 2015 (000's sq ft)

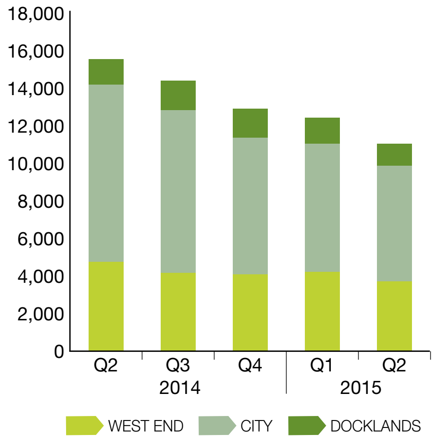
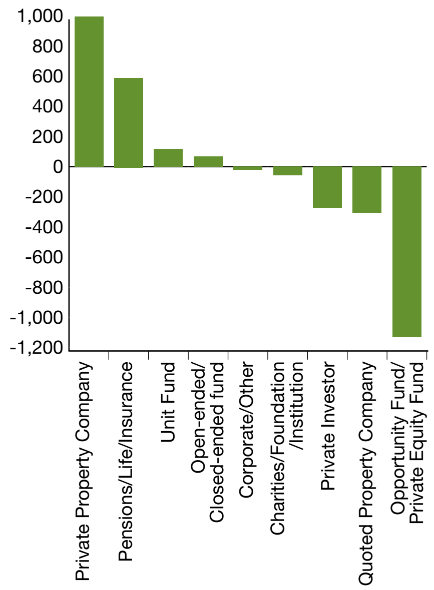


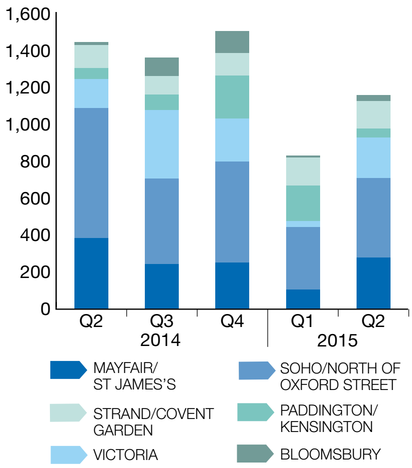
FIGURE 3
Central London net investment
Q2 2015 (£ m's)



WEST END

- Take-up increased to 1.2 m sq ft
- Availability fell by nearly 12%
- Prime headline rents remained at £115.00 per sq ft
- Investment turnover in Q2 totalled £2.3 bn

FIGURE 1
West End take-up by quarter & sub-market
Q2 2014 - Q2 2015 (000's sq ft)



Demand

The second quarter saw a significant increase in take-up levels. Almost 1.2 m sq ft was let, a 39% increase on the previous quarter's level and broadly in line with the long-term average. Take-up of new and refurbished space almost doubled, largely thanks to Google's acquisition of a further 183,000 sq ft at King's Cross Central. Technology, media and telecoms (TMT) occupiers have been the most active sector over the last 12 months, accounting for more than one-third of all transactions, and have also accounted for all three deals in excess of 100,000 sq ft.

However, the wider transaction profile was weighted heavily towards smaller units; more than two-thirds of all deals were below 25,000 sq ft. There has been a noticeable lack of large-unit transactions in 2015. In the six months to Q4 2014, the West End market saw eight transactions involving units in excess of 50,000 sq ft totalling 780,000 sq ft. In the first half of 2015, there have been just three deals totalling 300,000 sq ft.

Supply

Availability in the West End fell to 3.7 m sq ft, its lowest level for eight years. This represents a vacancy rate of 4.1%. Supply levels have fallen by more than 20% in the last 12 months and are now 32% below the long-term average. The volume of new and refurbished space on the market remained broadly unchanged and is in line with the long-term average.

Despite the rise in construction activity in the City and Docklands, levels in the West End fell for the second consecutive quarter. There is now 2.2 m sq ft under construction speculatively in the West End and due for completion in the next three years, although this remains above the long-term average of 1.8 m sq ft. However, given that take-up of new and refurbished space totalled 1.9 m sq ft in the last 12 months, this represents just a little over one year's worth of new supply.

Rental profile

Prime core headline rents remained unchanged at £115.00 per sq ft with rent free periods remaining stable at 15 months on a ten-year term. Further rental growth is expected during the course of the year.

Investment

Investment turnover in the West End totalled just over £2.3 bn during the second quarter of 2015, more than double the previous quarter's level and by far exceeding the long-term average of £1.2 bn. There were five deals that transacted over £100.0 m during Q2 2015, compared to two recorded in the previous quarter. Overseas purchasers accounted for 51% of total sales by volume. Private property companies accounted for nearly 36% of market share, followed by pension/life/insurance companies with 22%.

One of the largest deals of the quarter was the sale of 95 Wigmore Street, W1, which was purchased by a private investor from the Far East. The asset sold for £223.0 m which reflects a NIY of 3.43% and a capital value of £2,166 per sq ft. Prime yields remained at 3.50% for the second consecutive quarter after hardening during the first quarter of the year.

FIGURE 2
West End availability by quarter & sub-market
Q2 2014 - Q2 2015 (000's sq ft)

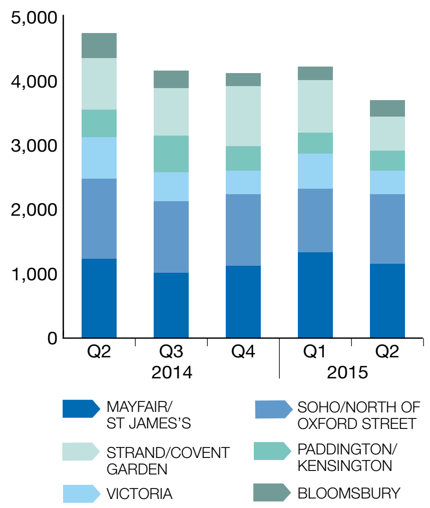
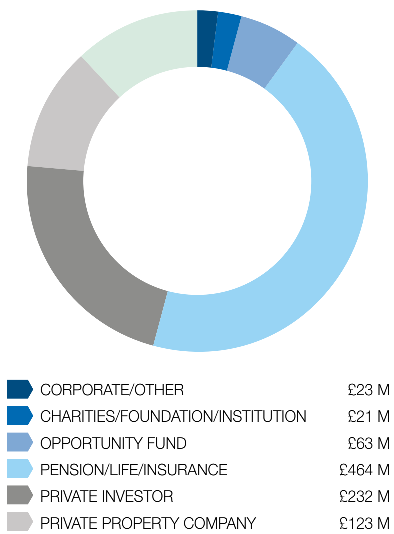


FIGURE 3
West End investment by purchaser
Q2 2015 (£m)



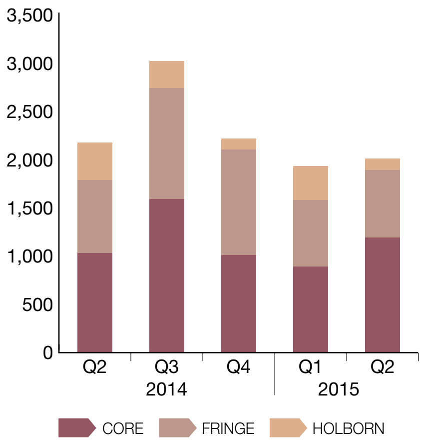
CITY

- Take-up totalled 2.0 m sq ft
- The vacancy rate fell further to 5.2%
- Prime headline rents remained at £65.00 per sq ft
- Investment turnover totalled £3.0 bn

FIGURE 1

City take-up by quarter & sub-market

Q2 2014 - Q2 2015 (000's sq ft)



Demand

Take-up in the second quarter saw levels reach just over 2.0 m sq ft, 4% above the previous quarter and 15% above the long-term average. The largest transaction of the quarter was DLA Piper's pre-let of Mitre House, 160 Aldersgate, EC1 totalling 150,000 sq ft. Nearly 60% of the market activity was located in the Core. Since the end of the quarter, Ashurst LLP has completed its deal taking circa 280,000 sq ft on a pre-let at the Fruit & Wool Exchange, Brushfield Street, which will be the largest deal of the year so far across the City and West End.

Active requirements remain strong, coming from a broad base of industries. Total active demand at the end of the second quarter of the year totalled 4.2 m sq ft, on par with the long-term average. Financial occupiers account for 32% of active searches followed by the professional sector with 18%.

Supply & development

Availability continued to be eroded across the City, falling nearly 10% from 6.8 m sq ft in Q1 to less than 6.2 m sq ft in the second quarter of the year. Levels of supply are now 37% below the long-term average of 9.9 m sq ft. The current vacancy rate in the City is now 5.2%, the lowest level since Q2 2001. The level of new and refurbished space continued its downward trend, with the quarter-end figure totalling 2.2 m sq ft, the lowest since Q3 2007. There are just two buildings in the Core that could provide an occupier 100,000 sq ft of new and refurbished space within the next six months.

There is currently just under 6.2 m sq ft of speculative space under construction in the City, albeit nearly 2.0 m sq ft is already pre-let. There is 1.2 m sq ft that is under construction in the Core that will complete by the end of 2016. Just three of these schemes are over 100,000 sq ft, 8 Finsbury Circus, 1 Angel Court and Creechurch Place. 100 Bishopsgate started on site totalling circa 865,000 sq ft and is due for completion in 2018.

Rental Profile

Prime rents remained steady at £65.00 per sq ft, after having increased in Q1. Further rental growth is expected during the course of the year. Rent free periods have hardened slightly during the quarter, and now sit between 18 and 21 months on a typical 10-year term certain.

Investment

The investment sales volume was markedly higher in the second quarter of the year, up by 33% from £2.3 bn in Q1 to just over £3.0 bn in Q2 and well above the long-term average of £1.8 bn. There were 10 transactions over £100 m during the quarter, with the largest being the sale of The Walbrook Building for £575 m, purchased by Cathay Life at a NIY of 4.01%. Overseas investors continue to dominate prime asset purchases, acquiring 95% of all £100 m + transactions in the last 12 months

City office yields remained steady at 4.00%, although 10 year Gilt yields were at circa 2.00% at the quarter-end, a positive spread of 200 basis points. Economic uncertainty particularly in the Eurozone and China may well result in more foreign money targeting London but one must continue to monitor these risk levels closely.

FIGURE 2

City availability by quarter & sub-market

Q2 2014 - Q2 2015 (000's sq ft)

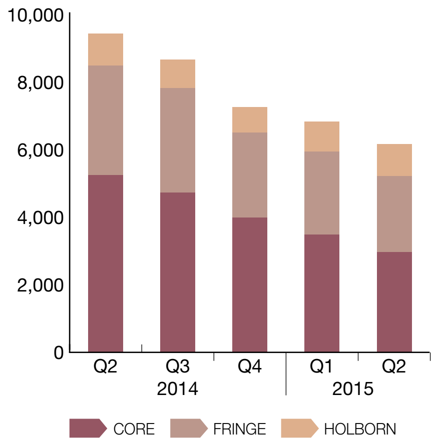
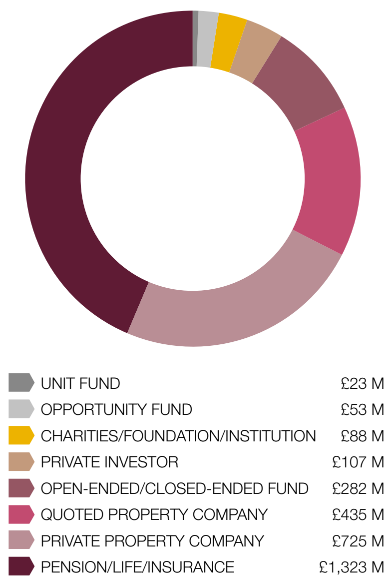


FIGURE 3

City investment by purchaser

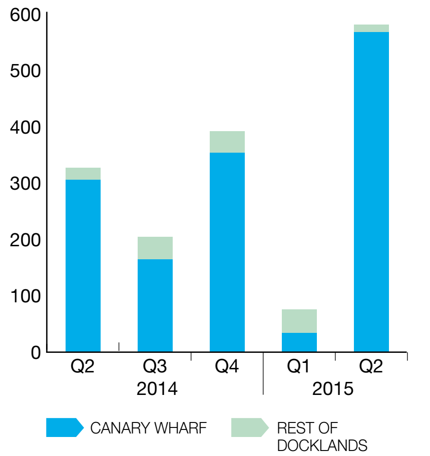
Q2 2015 (£m)



DOCKLANDS

- Take-up totalled 0.58 m sq ft in Q2
- The vacancy rate fell further to 5.5%
- Prime headline rents remained at £37.50 per sq ft
- Investment turnover totalled £19.3 m

FIGURE 1
Docklands take-up by quarter & sub-market
Q2 2014 - Q2 2015 (000's sq ft)



Demand

The second quarter of 2015 saw a significant rise in take-up levels, from just 76,000 sq ft in Q1 to over 582,000 sq ft. This was predominantly due to the largest deal of the year across Central London completing during the quarter. Deutsche Bank took circa 389,000 sq ft on a sub-let from Clifford Chance at 10 Upper Bank Street. Demand was up by 76% on the same quarter of 2014 and more than double the long-term average of 257,000 sq ft.

Canary Wharf continues to attract a variety of occupiers, with the highest level of take-up recorded since Q4 2010. There is currently over 260,000 sq ft already under offer in Canary Wharf, which should see levels in the following quarter above average once more.

Supply & development

Following the increasing level of take-up across Docklands and Canary Wharf in particular, the level of supply has continued to fall quarter-on-quarter. Availability in Docklands fell by 15% from 1.4 m sq ft in Q1 to 1.2 m sq ft in Q2 2015, which reflects a current vacancy rate of 5.5%. In Canary Wharf, supply fell to just under 750,000 sq ft, the lowest level since Q4 2008.

Following the recent pre-let at 1 Bank Street, construction started on site totalling circa 700,000 sq ft, in which Société Générale will occupy circa 280,000 sq ft upon completion in 2018.

Rental profile

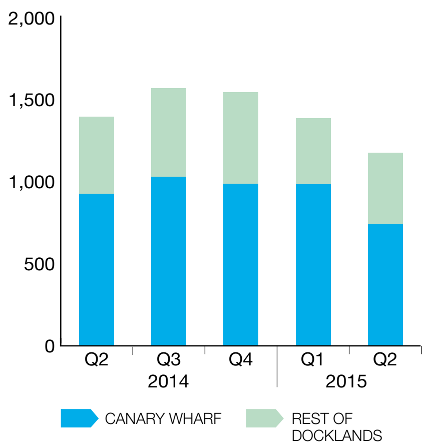
Prime rents in Canary Wharf remained unchanged at £37.50 per sq ft.

Investment

There was just one investment sale that transacted during the quarter; 8 Greenwich View Place was purchased by M&G for £19.3 m, which reflected a NIY of 4.77% and a capital value of £553 per sq ft. Transaction volumes continue to reflect lack of stock in this market.

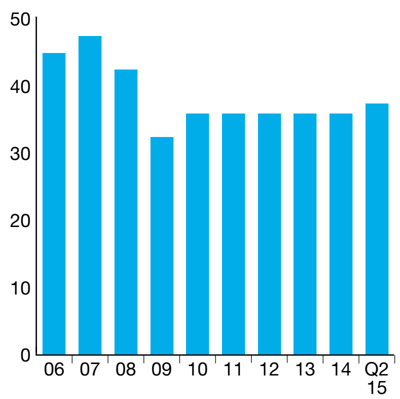
The most notable asset on the market in Canary Wharf is 30 South Colonnade, with a quoting sale price of £215.0 m, which reflects a NIY of 5.27% and a capital value of £704 per sq ft.

FIGURE 2
Docklands availability by quarter & sub-market
Q2 2014 - Q2 2015 (000's sq ft)



> "Take-up in Docklands during the second quarter of the year was at its highest level since Q4 2010."

FIGURE 3
Canary Wharf prime rent
2006 - Q2 2015 (Prime £/sq ft)



KEY STATISTICS

Central London office market

Availability (m sq ft)	Q2 14	Q3 14	Q4 14	Q1 15	Q2 15	3 months % change	12 months % change
West End	4.75	4.17	4.08	4.23	**3.84**	-9.2%	-19.2%
City	9.45	8.68	7.27	6.83	**6.04**	-11.6%	-36.1%
Docklands	1.40	1.58	1.55	1.39	**1.18**	-15.1%	-15.7%
Central London	15.60	14.43	12.90	12.45	**11.06**	-11.2%	-29.1%

Vacancy Rate (%)	Q2 14	Q3 14	Q4 14	Q1 15	Q2 15	3 months % change	12 months % change
West End	5.2	4.5	4.4	4.6	**4.2**	n/a	n/a
City	7.9	7.3	6.1	5.7	**5.1**	n/a	n/a
Docklands	6.5	7.4	7.2	6.5	**5.5**	n/a	n/a
Central London	6.7	6.2	5.6	5.4	**4.8**	n/a	n/a

Take-up (m sq ft)	Q2 14	Q3 14	Q4 14	Q1 15	Q2 15	3 months % change	12 months % change
West End	1.45	1.37	1.51	0.83	**1.16**	39.8%	-20.0%
City	2.18	3.02	2.22	1.94	**2.02**	4.1%	-7.3%
Docklands	0.33	0.20	0.39	0.08	**0.58**	625.0%	75.8%
Central London	3.96	4.59	4.12	2.85	**3.76**	31.9%	-5.1%

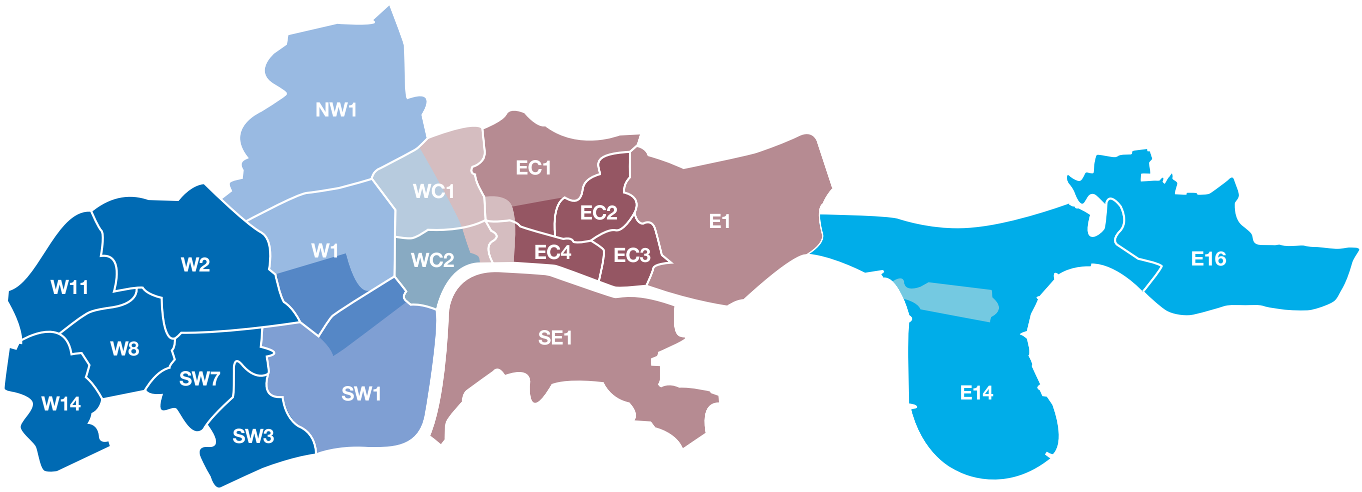
Active Demand (m sq ft)	Q2 14	Q3 14	Q4 14	Q1 15	Q2 15	3 months % change	12 months % change
West End	1.75	1.09	1.51	1.64	**1.59**	-3.0%	-9.1%
City	5.08	2.95	4.30	4.46	**4.23**	-5.2%	-16.7%
Docklands	0.99	0.97	0.94	1.03	**0.98**	-4.9%	-1.0%
Unspecified Central London	1.38	0.78	0.51	1.65	**1.83**	10.9%	32.6%
TOTAL Central London	9.20	5.79	7.25	8.78	**8.63**	-1.7%	-6.2%

Under Construction (m sq ft)	Q2 14	Q3 14	Q4 14	Q1 15	Q2 15	3 months % change	12 months % change
West End	2.31	2.67	3.09	2.50	**2.40**	-4.0%	3.9%
City	4.52	4.03	4.74	5.08	**6.17**	21.5%	36.5%
Docklands	0.00	0.00	0.00	0.00	**0.70**	n/a	n/a
Central London	6.83	6.70	7.83	7.58	**9.27**	22.3%	35.7%

Investment (£ m)	Q2 14	Q3 14	Q4 14	Q1 15	Q2 15	3 months % change	12 months % change
West End	1135.2	1899.0	2771.8	1031.1	**2,317.3**	124.7%	104.1%
City	2107.3	2146.5	4603.6	2281.5	**3,035.4**	33.0%	44.0%
Docklands	828.8	353.7	1333.3	0.0	**19.3**	n/a	-97.7%
Central London	4071.3	4399.2	8708.7	3312.6	**5,372.0**	62.2%	31.9%

Source: Knight Frank Research

THE CENTRAL LONDON OFFICE MARKET



The West End

Mayfair/St James's
Mayfair and St James's refers to the area bounded by Oxford Street, Regent Street and Park Lane in W1 and by Green Park, St James's Park and The Mall in SW1.

Soho/North of Oxford Street
Soho/North of Oxford Street refers to NW1, and W1 (excluding Mayfair).

Victoria
Victoria refers to SW1 (excluding St James's).

Paddington/Kensington
Paddington/Kensington refers to SW3, SW7, W2, W8, W11, W14.

Bloomsbury
Bloomsbury refers to the area of WC1 bounded by Southampton Row, New Oxford Street, Tottenham Court Road and Euston Road.

Strand/Covent Garden
Strand/Covent Garden refers to the area of WC2 bounded by Kingsway, Aldwych, Victoria Embankment, Charing Cross Road and New Oxford Street.

The City

Core
Core refers to EC2 (excluding EC2A), EC3, EC4 (excluding EC4A and EC4Y), and EC1A.

Fringe
Fringe refers to SE1, E1, EC1 (excluding EC1A and EC1N), and EC2A.

Holborn/Fleet Street
Holborn/Fleet Street refers to EC1N, EC4A, EC4Y, WC1 (excluding Bloomsbury), and WC2 (excluding Strand/Covent Garden).

Docklands

Canary Wharf
Canary Wharf refers to the area comprising Canary Riverside, Westferry Circus, Columbus Courtyard, Cabot Square, Canada Square, Blackwall Place and Heron Quays (East).

Rest of Docklands
Rest of Docklands refers to E14 and E16 including The Royals Business Park (excluding Canary Wharf).

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General Note

This report has been prepared by Knight Frank Research, the research and consultancy division of Knight Frank. Knight Frank Research gratefully acknowledges the assistance given by the West End, City and Docklands Offices in the compilation and presentation of this material. Certain data sourced from LOD. All graph data sourced by Knight Frank.

Technical Note

The following criteria have been adopted in the preparation of this report.

i. All floorspace figures quoted in this report refer to sq ft net.

ii. Take-up figures refer to space let, pre-let, or acquired for occupation during the quarter.

iii. Availability refers to all space available for immediate occupation, plus space still under construction which will be completed within six months and which has not been let.

iv. Availability and take-up are classified into three grades:
New/refurbished: Space under construction which is due for completion within six months or space which is currently on the market and is either new or completely refurbished.
Second-hand A Grade: Previously occupied space with air-conditioning.
Second-hand B Grade: Previously occupied space without air-conditioning.

v. Demand figures quoted in this report refer to named requirements for over 10,000 sq ft.

vi. Under construction figures quoted in this report refer to developments of over 20,000 sq ft which are currently underway. They do not include properties undergoing demolition.

vii. Investment figures quoted in this report refer to accommodation where the majority of income/ potential income is from office usage and comprises transactions of £1 m and above.
The data includes standing investments, site purchases and funding transactions.

viii. This report is produced to standard quarters.
Quarter 1: January 1 – March 31,
Quarter 2: April 1 – June 30,
Quarter 3: July 1 – September 30,
Quarter 4: October 1 – December 31

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