

RESEARCH



# M25 OFFICES

INVESTMENT, DEVELOPMENT &  
OCCUPIER MARKETS **Q3 2017**



# EXECUTIVE SUMMARY

## ◆ Leasing transaction rate slows in Q3

Leasing activity across the South East reached 544,400 sq ft in Q3, 30% short of the long-term quarterly average. Take-up for 2017 now stands at 2.1m sq ft, 11% below the 10-year average for the Q1-Q3 period. Positively, around 680,000 sq ft of space remained under offer at the close of the quarter. This demonstrates that occupier interest is holding firm, although extended negotiation periods are now more common and the rate of deal execution has slowed.

## ◆ Technology demand continues to grow

Demand from the Telecoms, Media and Technology (TMT) sector has been particularly strong in 2017, with the sector accounting for 28% of take-up across the South East. The M4 corridor, long associated with a strong tech presence, has been the principal focus of activity. Year to date, TMT firms represent 37% of total take-up in M4, the highest percentage since 2000. Interestingly, the rise in tech demand means that take-up in the M4 remains on par with the long-term trend for the market.

## ◆ M4 vacancy edging up

With 624,000 sq ft of speculative space in the M4 reaching practical completion during Q3, availability increased for the eighth consecutive quarter. The market vacancy rate for the M4 has now reached 9.7%, the highest level since 2013; although the Q3 vacancy rate remains consistent with the longer-term average. Looking ahead, the coming six months will see a further 668,000 sq ft of speculative space come to market. As such, a rise in vacancy to 10% is anticipated by Q1 2018 before returning to below the trend level by Q3 2018.

## ◆ Foreign buyers bolstering the market

South East office investment volumes reached £1.3 billion in Q3 2017, the highest quarterly total since 2013. Despite a slow H1, this takes total office investment in the South East in 2017 to £2.3bn, 60% higher than the 10-year average for the Q1-Q3 period. Supported by the acquisition of the Arlington portfolio by TPG Real Estate, foreign capital was the main source of investment in Q3, accounting for 67% of volumes. Given the impending sale of four of Oaktree Capital Management's UK business parks to Frasers Property International, this representation will increase further in Q4.

## ◆ Upward pricing pressure in the South East

Prime yields hardened to 5.00% in Q3, although there are now examples of institutions paying below this level for reversionary assets. As well as the overseas investors outlined above, UK buyers remain very active, with Funds, Councils and Permitted Development buyers keen to invest.

\*The South East is defined in the technical note on the back cover

# OCCUPIER MARKET

Although letting activity dipped in Q3, the fall was balanced by the level of space under offer. Vacancy remained consistent or below the long-term trend across the individual market areas, despite development completions reaching a 10-year high.

SOUTH EAST  
TAKE-UP

**544,400**  
sq ft

▼ -32%



TAKE-UP (SQ FT)

**M25** **370,100** ▼ -2%  
New and Grade A space 86%

**M3** **76,900** ▼ -64%  
New and Grade A space 71%

**M4** **354,500** ▼ -22%  
New and Grade A space 98%



SUPPLY (SQ FT)

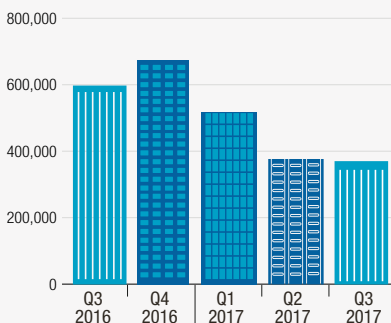
**M25** **7.1m** ▼ -4.0% **5.9%**  
New and Grade A space 84% 4.9%

**M3** **2.3m** ▼ -6.0% **6.0%**  
New and Grade A space 81% 4.8%

**M4** **6.4m** ▲ 6.0% **9.7%**  
New and Grade A space 94% 9.2%

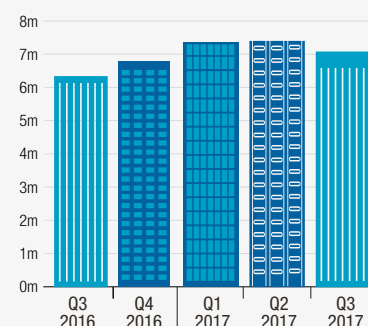
\*Arrows reflect quarter-on-quarter change. \*\* Number in blue shows vacancy rate across all grades. Number in grey denotes vacancy rate for new and grade A office space.

FIGURE 1  
M25 Take-up (sq ft)



**0.7m**  
UNDER OFFER  
IN THE SOUTH  
EAST IN Q3 2017

FIGURE 2  
M25 Supply (sq ft)



**22%**  
BELOW THE  
10-YR AVERAGE  
IN Q3 2017



**EMMA GOODFORD**

Transactions are taking more time to execute meaning, bar the M4, take-up is lower than the 10-year average. Sustained activity in the M4 is encouraging news for both developers and landlords, with around 3m sq ft of development completed over the past 24 months.



**RODDY ABRAM**

Evolution from the serviced/co-working providers continues to positively shape strategies for multi let buildings. There are now signs of larger requirements returning, with occupiers taking an early view on future supply.

## Key leasing transactions Q3 2017

ADDRESS	SIZE (SQ FT)	OCCUPIER	RENT (PSF)
12 Hammersmith Grove (1st, 2nd & 3rd flrs), Hammersmith	52,800	WeWork	£55.50
Nexus, Crawley	40,000	L3	Undisclosed
The Porter Building (1st flr), Slough	28,400	Fiserv	£34.00
Westside (grd & 1st flrs), Hemel Hempstead	26,600	Harman International industries	£26.00
12 Hammersmith Grove (prt 7th & 8th flrs), Hammersmith	25,100	Creative Artists Agency	£57.50

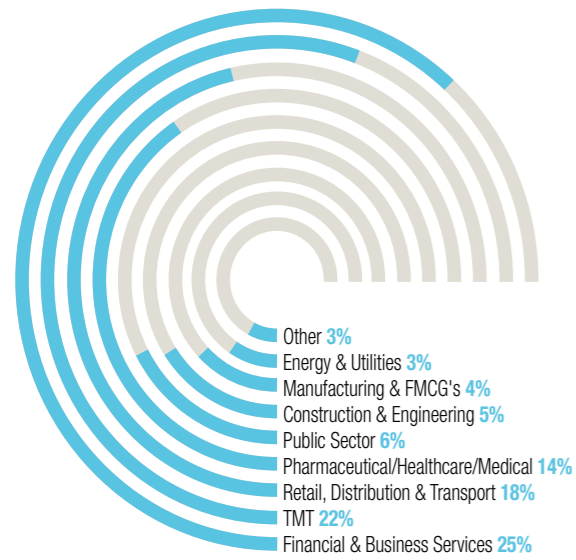
Source for all charts: Knight Frank Research

# DEMAND

**5.2m**sq ft  
OF ACTIVE NAMED DEMAND  
IN THE SOUTH EAST



Active named demand



# DEVELOPMENT

**1.8m**sq ft  
SPACE UNDER CONSTRUCTION  
IN THE SOUTH EAST



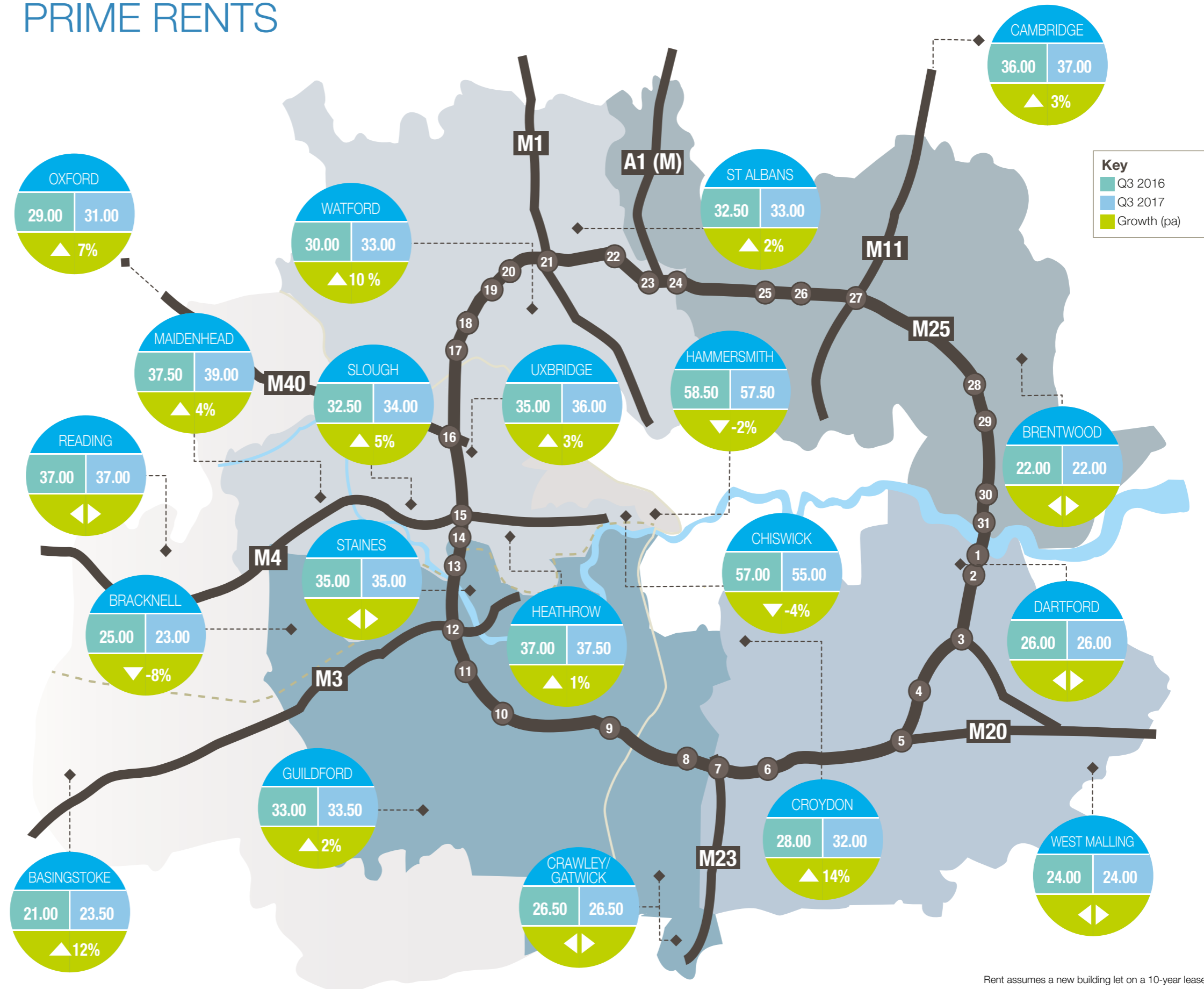
\*This includes pre-let and speculative space

Speculative development (sq ft)  
Due to complete before Q1 2019



Source for all charts: Knight Frank Research

# PRIME RENTS



Rent assumes a new building let on a 10-year lease.

# INVESTMENT MARKET

The completion of several large deals supported a threefold rise in investment volumes in Q3. Yields have moved in, with competitive pressure from a diversifying buyer pool continuing to exert upward pressure on pricing.

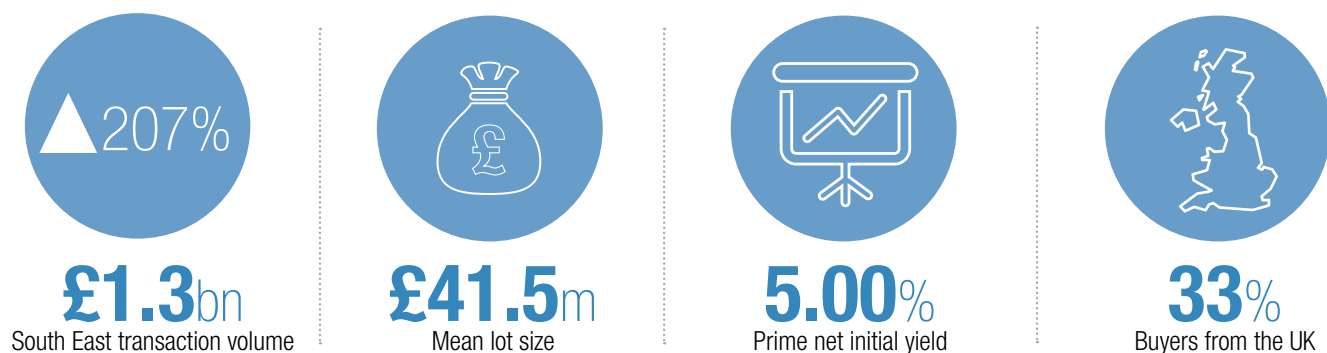
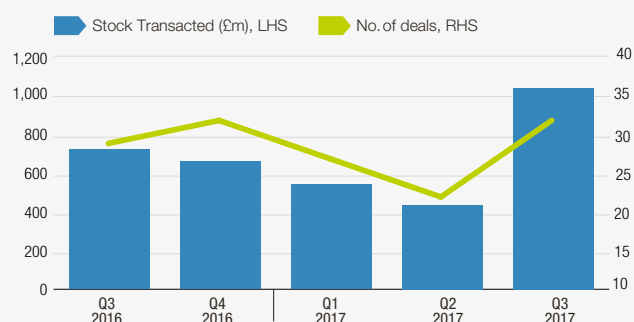


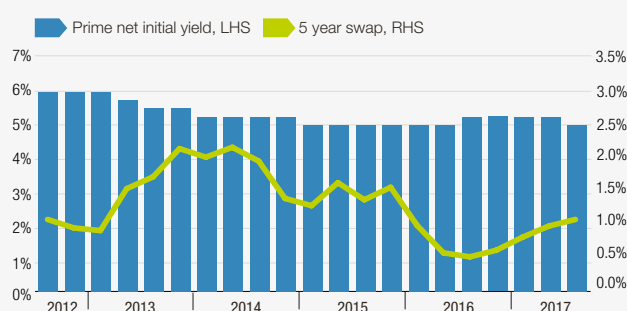
FIGURE 3  
Investment volumes



**TIM SMITHER**

After a slow start to the year, activity increased sharply in Q3, driving up investment volumes. With several deals ongoing and a significant amount of equity still to be deployed, a busy end to 2017 is anticipated.

FIGURE 4  
Prime net initial yield and finance



**SIMON RICKARDS**

We are seeing the investor base continue to broaden in the South East office market, with far Eastern investors increasingly active alongside US private equity, Middle Eastern families and domestic investors. Trading volumes remain held back only by a lack of stock.

## Key investment transactions Q3 2017

BUILDING	PRICE (£M)	NET INITIAL YIELD	VENDOR	PURCHASER
<b>Arlington Portfolio</b>	£350.00	Undisclosed	Goodman / L&G	TPG Real Estate
<b>Milton Park, Abingdon</b>	£200.00	Undisclosed	Hermes Investment Management	Canada Pension Plan Investment Board (CPPIB)
<b>10 Hammersmith Grove, Hammersmith</b>	£112.00	5.00%	Tai United Holdings	Blue Horizon investors
<b>Interchange, Croydon</b>	£71.50	6.25%	Canmoor / Carval	Tristan Capital Partners
<b>Marlow International, Marlow</b>	£68.00	7.03%	London Metric	Kildare Partners

Source for all charts: Knight Frank Research

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## TECHNICAL NOTE

- Knight Frank defines the M4 market as extending from Hammersmith, west to Newbury, incorporating Uxbridge and High Wycombe to the north and Staines and Bracknell to the south. Reading is also included. Existing built office stock in the M4 market totals 66m sq ft.
- The M3 market incorporates the main South West London boroughs and encompasses Leatherhead, Guildford and Basingstoke extending north to the M4 boundary described above. Farnborough and Camberley are also included. Existing built office stock in the M3 market totals 39m sq ft.
- The figures in this report relate to the availability of built, up-and-ready office/B1 accommodation within the M25 market. Vacant premises and leased space which is being actively marketed are included.
- All floorspace figures are given on a net internal area basis (as defined by the RICS).
- A minimum 10,000 sq ft (net) cut-off has been employed throughout. Major and minor refurbishment have been treated as new and second-hand respectively. Data is presented on a centre and quadrant basis. Classification by centre relates to the locational details contained within the marketing material for available properties. Classification in this manner is clearly somewhat arbitrary.
- Vacancy rate data is based on a total M25 stock measure of 121m sq ft (net), an M4 market stock of 66m sq ft (net) and an M3 market stock of 39m sq ft (net). Please note that a revision to total market office stock figures was applied in Q1 2017 to reflect 'change of use' permitted through the Town and Country Planning Order 2015.
- Second-hand floorspace has been sub-divided into A and B grade accommodation, reflecting high and low quality respectively. Whilst subjective, this categorisation is based on an assessment of each property's age, specification, location and overall attractiveness.
- The South East is defined as the market area shown in the map on pages 4 & 5.
- Pre-let = The letting of proposed schemes not yet under construction and those let during the construction process.
- All data presented is correct as at September 30th 2017.

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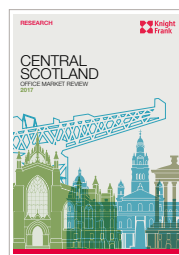
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