RESEARCH

Q3 2009

CENTRAL LONDON

Quarterly – Offices

Knight Frank

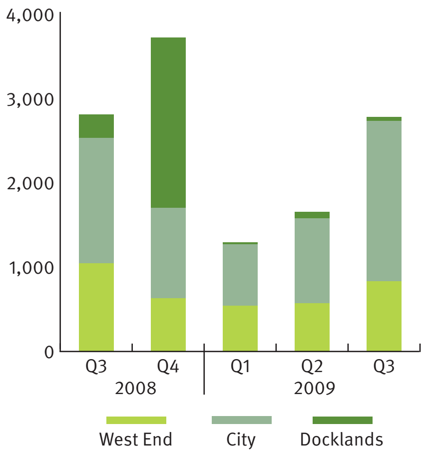
HIGHLIGHTS

- Take-up rose for the second successive quarter across Central London to 2.8 m sq ft as a result of a marked increase in occupier activity, particularly in the City where levels of take-up were the highest for 2 years.
- The Central London vacancy rate remained stable at 11.0%, and we expect it to fall next year as the volume of new and refurbished space on the market contracts.
- The volume of speculative space under construction fell for the sixth consecutive quarter and now stands at 4.4 m sq ft. The shrinking development pipeline and increased take-up will provide the impetus for a reduction of supply in 2010.
- Investment turnover was stable at £1.5 bn, although a lack of sellers is holding the market back. Prime yields hardened further as competition for the limited available stock continued to drive prices upwards.

CENTRAL LONDON OVERVIEW

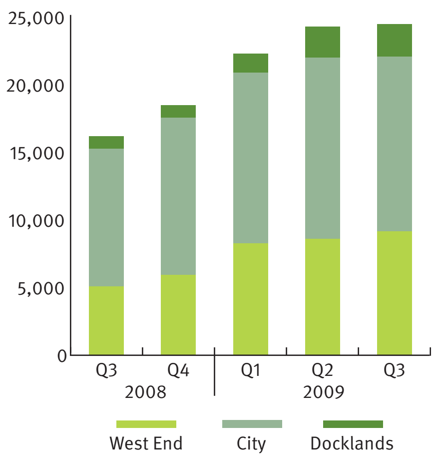
- **Take-up rose by 68% to 2.8 m sq ft as activity increased across all markets.**
- **Availability was stable at 24.5 m sq ft, reflecting a vacancy rate of 11.0%.**
- **Speculative construction activity continued to fall to 4.4 m sq ft, the lowest level for 3 years.**
- **Investment activity remained unchanged at £1.5 bn, and prime yields hardened in both the City and West End.**

Figure 1
Central London take-up by quarter & market sub-area
Q3 2008 - Q3 2009 (000's sq ft)



Source: Knight Frank

Figure 2
Central London availability by quarter & market sub-area
Q3 2008 - Q3 2009 (000's sq ft)



Source: Knight Frank

Demand and take-up

Activity levels in the third quarter showed a considerable improvement, with take-up rising to 2.8 m sq ft, 68% higher than Q2. The City saw a rebound of the large-unit market, which has been subdued for some time. Having recorded just one transaction in excess of 50,000 sq ft in the first half of the year, the City enjoyed four such deals in the third quarter, the largest of which was Nomura's acquisition of over 500,000 sq ft at Watermark Place, EC4.

Despite the removal of Nomura's requirement from our demand figures, active demand grew for the third consecutive quarter and now totals 8.3 m sq ft. A number of requirements shelved in response to the adverse economic conditions are now being re-activated as tenants look for bargains across the City and West End. However, take-up levels for Central London remain 15% below the average for the last 10 years.

Supply and development

Supply levels remained flat in Q3, with Central London availability at 24.5 m sq ft, representing a vacancy rate of 11.0%. This stabilising of availability is due to a slowing of speculative construction activity across all markets, and improved take-up. The City recorded a fall in availability for the first time since 2007.

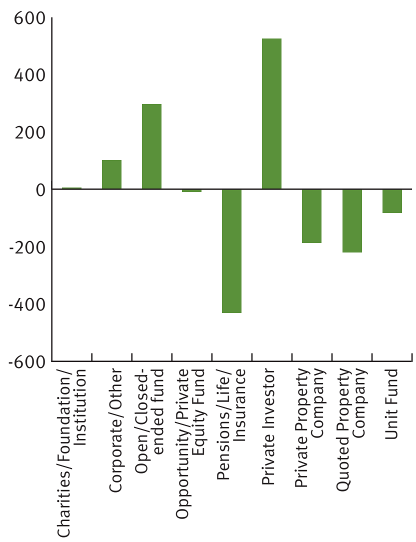
The volume of speculative space under construction continued to fall, and is now 48% lower than 12 months ago. Given the fall in speculative construction starts and the resurgent interest from occupiers in new and refurbished stock, it is anticipated that the availability of this type of space will be quickly eroded now confidence is returning to the market.

Investment market

Investment turnover was unchanged at £1.5 bn in the third quarter, as a lack of new sellers coming to the market has held back activity. Demand for Central London offices has continued to improve due to the weak pound and signs of recovery in the occupier market improving investor confidence.

Competition for the limited available stock, driven by the ongoing demand from overseas investors has resulted in a further hardening of prime yields across Central London. In the West End, the prime yield is now 5.50%, while in the City the prime yield has come in to 6.25%.

Figure 3
Central London net investment
Q3 2009 (£ m's)



Source: Knight Frank

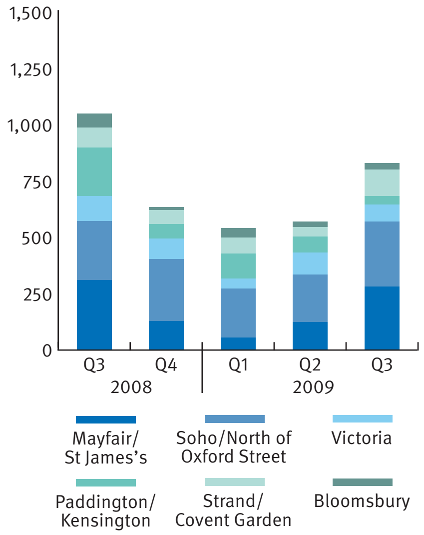
WEST END

- **Take-up increased 43% on the previous quarter to 0.8 m sq ft.**
- **Active demand has risen to 2.1m sq ft, the highest level since Q1 2008.**
- **Vacancy rate now stands at 10.2% with availability increasing 7% to 9.2 m sq ft.**
- **Prime headline rents at £65.00 per sq ft which we view as the end of the correction.**

Figure 1

West End take-up by quarter & market sub-area

Q3 2008 - Q3 2009 (000's sq ft)



Source: Knight Frank

Demand & take up

Take-up in the West End recorded a 43% increase totalling 830,000 sq ft, the highest level of take-up since Q3 2008. However, this is still 33% below the ten-year long-term average of 1.3 m sq ft. Although take-up rose significantly, there were no deals over 25,000 sq ft, it was the 5-10,000 sq ft bracket that rose by 44% accounting for nearly a third of take-up in the West End. The largest deal of the quarter was at 80 Victoria Street where EDF Energy took 24,000 sq ft on a 12 year lease-term.

Active demand rose to 2.1 m sq ft in Q3, a 39% increase from the previous quarter's level of 1.5 m sq ft. As well as being substantially above the long-term average of 1.6 m sq ft, these levels of demand have not been seen since early 2008.

Supply & development

Availability has increased for the ninth consecutive quarter, up 7% on the previous quarter to 9.2 m sq ft, 36% higher than the ten-year long-term average. This represents a vacancy rate of 10.2%, a level not seen since early 2005. However, supply is thought to have stabilised with the majority of development space having already entered the figures.

The volume of space under construction speculatively has fallen for the third consecutive quarter with levels now at 1.6 m sq ft, 17% lower than in Q2 2009. Additionally, levels of second-hand space have fallen for the first time since Q4 2007.

Rental profile

Prime headline rents in the West End fell once again to £65.00 per sq ft down from £70.00 per sq ft, however we do not anticipate any further fall in prime rental values. Rent free periods remained unchanged for the third quarter at 24 months on a ten-year term certain.

Investment market

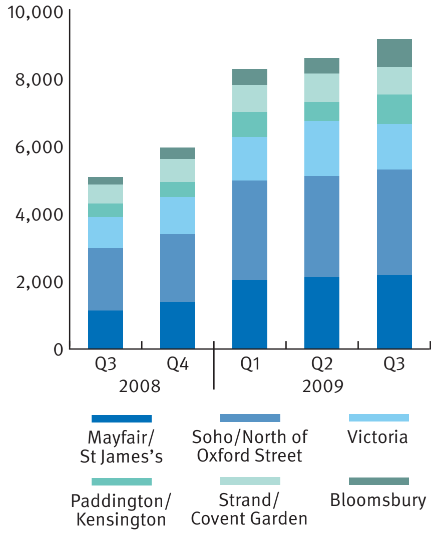
Turnover for the third quarter totalled £877m, up 13% on the previous quarter. Market sentiment continues to strengthen and marketing periods are being significantly reduced with the majority of sales being concluded by best bids scenarios. Private investors have once again dominated the market accounting for over 71% of purchasers. The largest transaction of the quarter was Windsor House, SW1 which exchanged at c.£113.5m, reflecting a net initial yield of c.5.85%

Prime core West End yields are currently stable at 5.50%, following a 50bp inward shift over the last two quarters. This partly reflects the imbalance in the market between the low availability of prime stock, as the weight of money in the market increases. Moreover, there is an acceptance that London will continue to offer long-term value.

Figure 2

West End availability by quarter & market sub-area

Q3 2008 - Q3 2009 (000's sq ft)

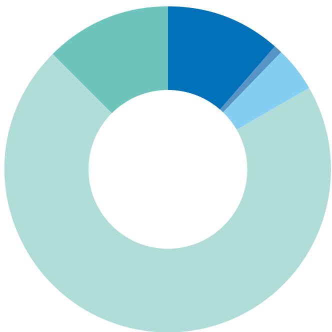


Source: Knight Frank

Figure 3

West End investment by purchaser

Q3 2009 (£ m's)



Corporate/Other	£100 m
Charities/Foundation/ Institution	£9 m
Pension/Life/Insurance	£39 m
Private Investor	£622 m
Private Property Company	£108 m

Source: Knight Frank

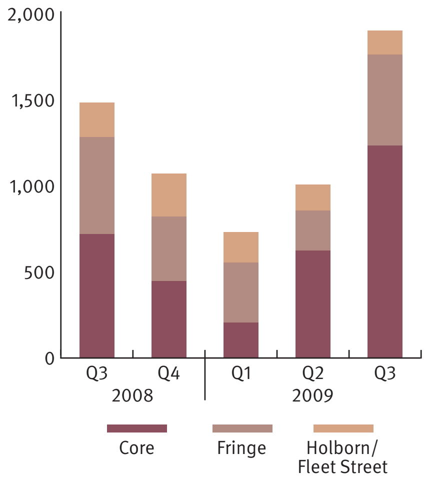
CITY

- **Strong take-up in Q3, due to the Nomura deal and a broad based recovery.**
- **Availability fell for the first time since 2007 to 12.9 m sq ft.**
- **Space under construction declined due to a lack of new development starts.**
- **Prime yields continue to harden on shortage of assets for sale.**

Demand and take-up

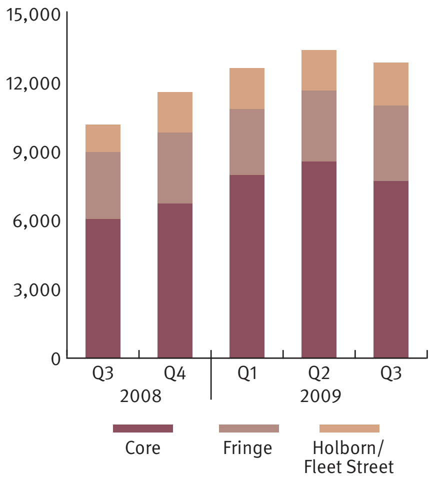
City take-up increased by 89% quarter-on-quarter to 1.9 m sq ft, up from just over 1.0 m sq ft in Q2. This was partly due to the 540,000 sq ft Nomura deal at Watermark place. However, even if we set this deal aside, City take-up increased by 39%, due to a recovery in activity in the broader market. Asia-Pacific banks, insurers, and professional firms were the main acquirers.

Figure 1
City take-up by quarter & market sub-area
Q3 2008 - Q3 2009 (000's sq ft)



Source: Knight Frank

Figure 2
City availability by quarter & market sub-area
Q3 2008 - Q3 2009 (000's sq ft)



Source: Knight Frank

With Pinsent Masons agreeing terms at 30 Crown Place, Bank of China poised to buy 1 Lothbury for its own occupation, and Macquarie under offer at Drapers Gardens, momentum has continued into Q4. Consequently, we are of the view that Q1 of this year marked the low point for the City occupier market, which is showing tentative signs of recovery.

Supply and development

Availability fell to 12.9 m sq ft, down from 13.4 m sq ft in Q2, due to Watermark Place being acquired. In our Q2 report we expressed surprise that a greater volume of sub-let space had not come to the market from the banks. This is still the case, and with financial markets rallying and banks reporting rising profits, the possibility of a large release of space from the banks is ebbing.

There is currently 2.8 m sq ft of speculative space under construction, of which 1.1 m sq ft is already included in our availability figures. To set this in context, the ten year average take-up in the City is 6.7 m sq ft per annum. This suggests supply will quickly come under pressure in 2010.

Rental profile

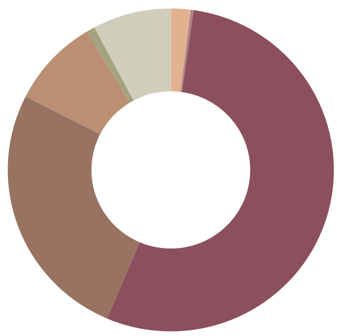
City rents declined further in Q3 to £42.50 per sq ft. However, with take-up rising again, availability expected to fall in 2010, and a thin development pipeline, we believe this marks the low point for rents in this cycle.

Investment market

The investment transaction volume edged down from £712 m in Q2 to £596 m in Q3. Lack of available stock continues to be the main constraint on activity, but this is exacerbated by ever-growing demand. The most notable trend of the quarter was the return of the UK institutions and property companies to the demand profile, signalling increased investor confidence in the occupier market.

Prime yields moved a further 25 basis points downwards in Q3 to 6.25%, continuing the downward trend. The hardening of yields has now also reached the secondary market, with increasing demand for shorter income investments offering future exposure to the perceived improvements in the occupational market.

Figure 3
City investment by purchaser
Q3 2009 (£ m's)



Charities/Foundation/Institution	£12 m
Corporate/Other	£2 m
Open/Closed-Ended Fund	£324 m
Pension/Life/Insurance	£156 m
Private Investor	£52 m
Private Property Company	£5 m
Quoted Property Company	£46 m

Source: Knight Frank

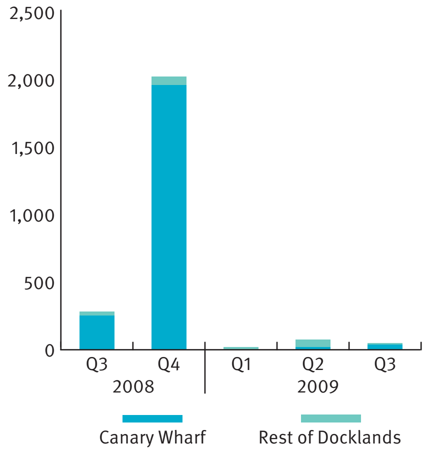
DOCKLANDS

- **Take-up has been subdued, but is set to improve significantly.**
- **20 Cabot Square under offer after only a short marketing period.**
- **Availability increases marginally to 2.4 m sq ft.**
- **Uncertainty over the amount of space that could be available at 25 Bank Street weighs on the market.**

Figure 1

Docklands take-up by quarter & market sub-area

Q3 2008 - Q3 2009 (000's sq ft)



Source: Knight Frank

Demand & take up

Docklands take-up was 50,000 sq ft in Q3, continuing a nine month period of subdued activity. The Mastercard deal at 10 Upper Bank Street, accounted for the majority (39,000 sq ft) of space transacted. Outside the Wharf, activity was weak with just the 11,000 sq ft deal at City Reach 1 to Haydon.

An encouraging development since quarter end is news that all the space Morgan Stanley handed back to Canary Wharf Group at 20 Cabot Square (347,000 sq ft) is now under offer, it is thought to BarCap. This space has only been on the market nine months, which considering the economic environment is a fast turn around for one of Canary Wharf's older buildings. EMEA has placed all the space at 7 & 11 Westferry Circus under offer, and LOCOG has agreed terms on 89,000 sq ft in the 25 Canada Square tower.

Supply & development

Availability edged up to 2.4 m sq ft, compared to 2.3 m sq ft three months ago. The long-term average for supply is 1.4 m sq ft. Nomura's decision to move the former-Lehman operations at Canary Wharf to the City should result in further space in 25 Bank Street coming to the market in 2010/11. The availability rate for Docklands is now 11.9%.

With the completion of 5 Churchill Place (JP Morgan), 30 North Colonnade (Fimalac) and 15 Canada Square (KPMG), there are now no buildings under construction in the Docklands market. Fimalac and KPMG are set to move in to their buildings during 2010.

Rental profile

The lack of deal activity hinders analysis of rent levels in Docklands. The Mastercard deal (which signed in August) was for a rent of c.£35.00 per sq ft, although the rents have almost certainly weakened further since then but there has not been a deal to prove this.

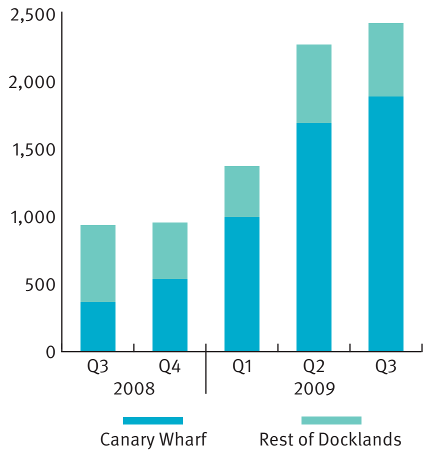
Investment

While the transaction volume for Q3 was zero, since quarter end Credit Suisse has sold 20 Columbus Courtyard on a sale and leaseback deal to M1 Real Estate for £155m, reflecting a net initial yield of 5.8%. The high level of interest in this building may encourage other Docklands landlords to consider selling. HSBC is in talks on the sale of its headquarters, 8 Canada Square, with media speculation suggesting a c.£800 m asking price. Outside of Canary Wharf, Ballymore are marketing 7 Greenwich View Place (asking price c.£10.0 m).

Figure 2

Docklands availability by quarter & market sub-area

Q3 2008 - Q3 2009 (000's sq ft)

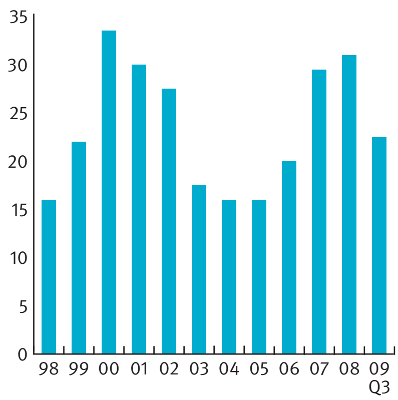


Source: Knight Frank

Figure 3

Rest of Docklands prime rent

1998-2009 (Prime £/sq ft)



Source: Knight Frank

Key statistics

Central London office market

Availability (m sq ft)	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09	3 months % change	12 months % change
West End	5.09	5.97	8.29	8.62	**9.19**	6.6%	80.4%
City	10.19	11.28	12.65	13.42	**12.90**	-3.9%	26.6%
Docklands	0.94	0.96	1.38	2.28	**2.44**	7.0%	159.1%
Central London	16.22	18.21	22.32	24.32	**24.52**	0.8%	51.2%

Vacancy Rate (%)	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09	3 months % change	12 months % change
West End	5.7	6.7	9.2	9.6	**10.2**	n/a	n/a
City	9.0	9.9	11.0	11.6	**11.2**	n/a	n/a
Docklands	4.7	4.8	6.8	11.1	**11.9**	n/a	n/a
Central London	7.3	8.2	10.0	10.9	**11.0**	n/a	n/a

Take-up (m sq ft)	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09	3 months % change	12 months % change
West End	1.05	0.64	0.54	0.57	**0.83**	44.9%	-20.9%
City	1.48	1.07	0.73	1.01	**1.90**	88.8%	28.3%
Docklands	0.28	2.02	0.02	0.08	**0.05**	-36.7%	-82.4%
Central London	2.82	3.73	1.29	1.66	**2.78**	67.7%	-1.2%

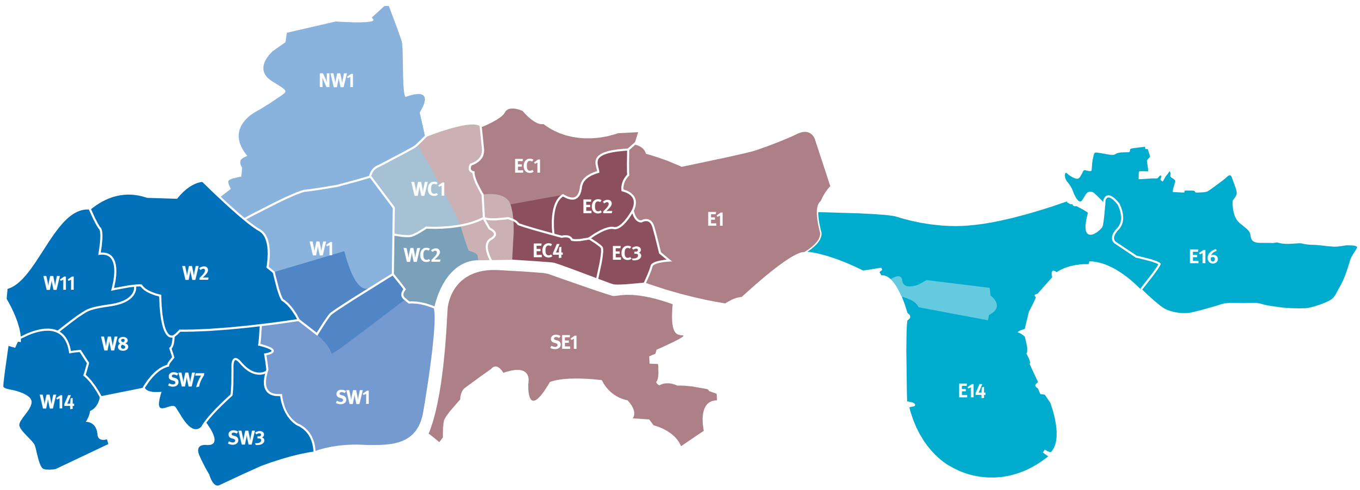
Active Demand (m sq ft)	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09	3 months % change	12 months % change
West End	0.82	0.99	0.82	1.49	**2.07**	38.8%	152.2%
City	3.37	3.49	3.56	4.12	**3.64**	-11.7%	7.8%
Docklands	0.12	0.08	0.07	0.35	**0.33**	-6.3%	182.6%
Unspecified Central London	3.12	1.56	1.76	1.63	**2.30**	41.2%	-26.1%
TOTAL Central London	7.43	6.12	6.22	7.59	**8.34**	9.9%	12.3%

Under Construction (m sq ft)	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09	3 months % change	12 months % change
West End	2.86	3.06	2.57	2.57	**2.17**	-15.4%	-24.0%
City	7.55	5.98	6.17	5.26	**4.48**	-14.8%	-40.6%
Docklands	1.77	1.03	0.72	0.98	**0.72**	-26.8%	-59.4%
Central London	12.18	10.08	9.46	8.81	**7.38**	-16.3%	-39.4%

Investment (£ m)	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09	3 months % change	12 months % change
West End	470.6	760.1	262.5	776.5	**877.6**	13.0%	86.5%
City	597.2	457.3	363.7	712.0	**596.5**	-16.2%	-0.1%
Docklands	0.0	838.0	0.0	0.0	**0.0**	n/a	n/a
Central London	1067.7	2055.4	626.2	1488.5	**1474.1**	-1.0%	38.1%

Source: Knight Frank

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).

RESEARCH

Americas
USA
Bermuda
Brazil
Caribbean
Chile

Australasia
Australia
New Zealand

Europe
UK
Belgium
Czech Republic
France
Germany
Hungary
Ireland
Italy
Monaco
Poland
Portugal
Romania
Russia
Spain
The Netherlands
Ukraine

Africa
Botswana
Kenya
Malawi
Nigeria
South Africa
Tanzania
Uganda
Zambia
Zimbabwe

Asia
Cambodia
China
Hong Kong
India
Indonesia
Macau
Malaysia
Singapore
Thailand
Vietnam

The Gulf
Bahrain

Commercial Research
James Roberts, Partner
Head of Central London Research
+44 (0) 20 7629 8171
james.roberts@knightfrank.com

John Snow, Partner
Head of Central London Offices
+44 (0) 20 7629 8171
john.snow@knightfrank.com

Knight Frank Research provides strategic advice, consultancy services and forecasting to a wide range of clients worldwide including developers, investors, funding organisations, corporate institutions and the public sector. All our clients recognise the need for expert independent advice customised to their specific needs.

Knight Frank Research Reports are also available at **KnightFrank.com**

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.

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

Newmark
Knight Frank
Global