



Q1 2013
M25 OFFICES
Investment, development & occupier markets

HIGHLIGHTS

- The M25 and M4 corridor markets made a positive start to 2013, both recording take-up above their 5-year and 10-year quarterly averages in Q1. In contrast, the M3 market was relatively subdued, with Q1 take-up 20% below its 10-year quarterly average.
- Active named demand increased for a second successive quarter to stand at 6.53m sq ft, 11% above Q1 2012. Financial & Business Services continues to retain the largest share of activity, accounting for 25% of the total, followed by TMT, with 16%.
- The M25 vacancy rate fell to 7.7% in Q1, its lowest level since Q1 2009. Q1's sole new speculative development start was Building 7, Chiswick Park, which by itself lifted speculative development activity in the M25 by 30% to 981,000 sq ft.
- Investment turnover was £298m in Q1, 72% above Q4 2012's total and closely in line with the 5-year quarterly average. Demand for good quality secondary product has increased markedly, with limited supply putting downward pressure on yields.

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Demand and take-up

- M25 take-up was 646,517 sq ft in Q1 2013, its highest since Q4 2011 and 2% above the 10-year quarterly average. Q1 also saw 40 deals, the most seen in any quarter since Q3 2008 and indicative of an improving depth to occupier demand.
- Q1's two largest deals involved oil companies, and together they accounted for 30% of Q1 take-up. BP agreed to a 135,000 sq ft pre-let refurbishment at 2 New Square, Bedfont Lakes, Heathrow, while Cameron Oil acquired 57,153 sq ft at Building 5, The Heights, Weybridge.
- While the TMT sector accounted for a lower share of Q1 take-up, it was the most active sector with 14 deals, the most seen in a single quarter since 2001. The largest TMT deal was Virgin Media's 44,175 sq ft lease at newly refurbished Griffin House, Hammersmith.
- In the M4, Q1 take-up was 426,377 sq ft, rebounding by 46% from Q4 2012 and 3% above the 10-year quarterly average. Bracknell was home to six of the M4's 24 deals, the largest of which saw Lloyds Register acquire 24,085 sq ft at 5 Arlington Square.
- In contrast, M3 activity remains subdued with take-up of 179,616 sq ft in Q1, 20% below the 10-year quarterly average. Three deals in Weybridge accounted for over half of M3 take-up, with Cameron Oil, Dentsply (20,000 sq ft) and AB Initio (14,653 sq ft) occupying the remaining space at PRUPIM's The Heights, Brooklands.
- Underlining occupiers' continuing preference for high quality office accommodation, poorer quality Grade B category buildings accounted for only 17% of total space leased in Q1.



Supply and development

- Supply continues to edge down, reflecting a combination of robust take-up in Q1 and a relatively limited amount of existing space coming to the market. Wereldhave's 28,400 sq ft One Eton Street development in Richmond was Q1's only brand new completion, while three second hand buildings totalling 150,000 sq ft were acquired for change of use, tightening supply in the process.
- The M25 vacancy rate fell from 8.0% to 7.7% in Q1, its lowest level since Q1 2009, while the M4 vacancy rate fell to 9.8%, down from a peak of 12.0% two years ago. In contrast, the M3 vacancy rate increased to 8.9% in Q1, having stood at 8.7% for three successive quarters.
- Q1's only speculative development start was Building 7, Chiswick Park, the last remaining plot at the Blackstone-owned scheme. At 334,000 sq ft, this is the largest single speculative development in the M25 for over twenty years and by itself increased speculative activity in the region by 30% in Q1.
- There is now close to 1m sq ft of speculative development underway across 11 schemes in the M25, its highest level in four years. However, activity is focused in a handful of markets where New and Grade A space is in short supply, such as Staines, Hammersmith and Croydon.

Figure 1
M25 take-up

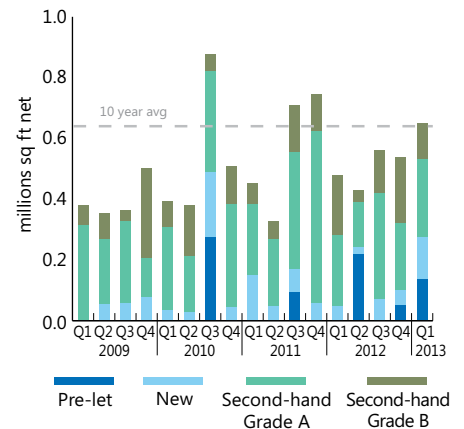


Figure 2
M4 take-up

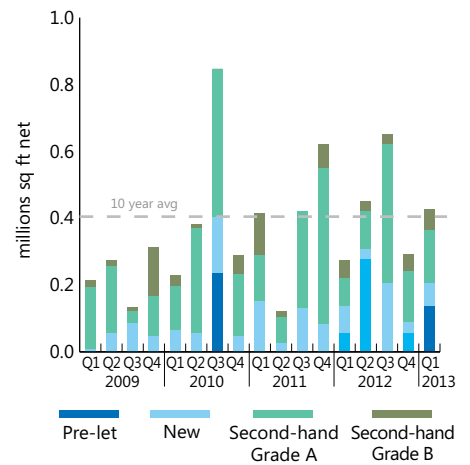
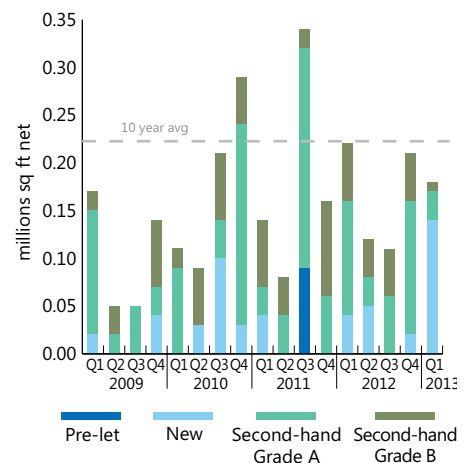


Figure 3
M3 take-up



Source: Knight Frank Research

Market statistics

Table 1
Key town prime rents & forecasts

Town	Q1 prime rent (psf)	Rent free (months)
Basingstoke	£18.00 ▶	33 ▼
Bracknell	£20.00 ▶	36 ▶
Brentwood	£21.00 ▶	24 ▶
Chiswick	£49.00 ▲	18 ▼
Croydon	£24.50 ▲	24 ▼
Gatwick	£22.50 ▶	30 ▶
Guildford	£29.50 ▶	21 ▼
Hammersmith	£45.00 ▲	18 ▼
Heathrow	£31.00 ▲	27 ▼
Maidenhead	£32.00 ▶	21 ▶
Reading	£30.50 ▶	27 ▶
Slough	£21.00 ▶	32 ▶
Staines	£32.00 ▲	21 ▶
St Albans	£23.00 ▶	24 ▶
Uxbridge	£32.00 ▲	21 ▶
Watford	£22.50 ▶	27 ▶
West Malling	£20.50 ▶	24 ▶

Based on new/Grade A building:
10,000 sq ft, 10 yr lease with no breaks
Note: ▲ = forecast for next 12 months

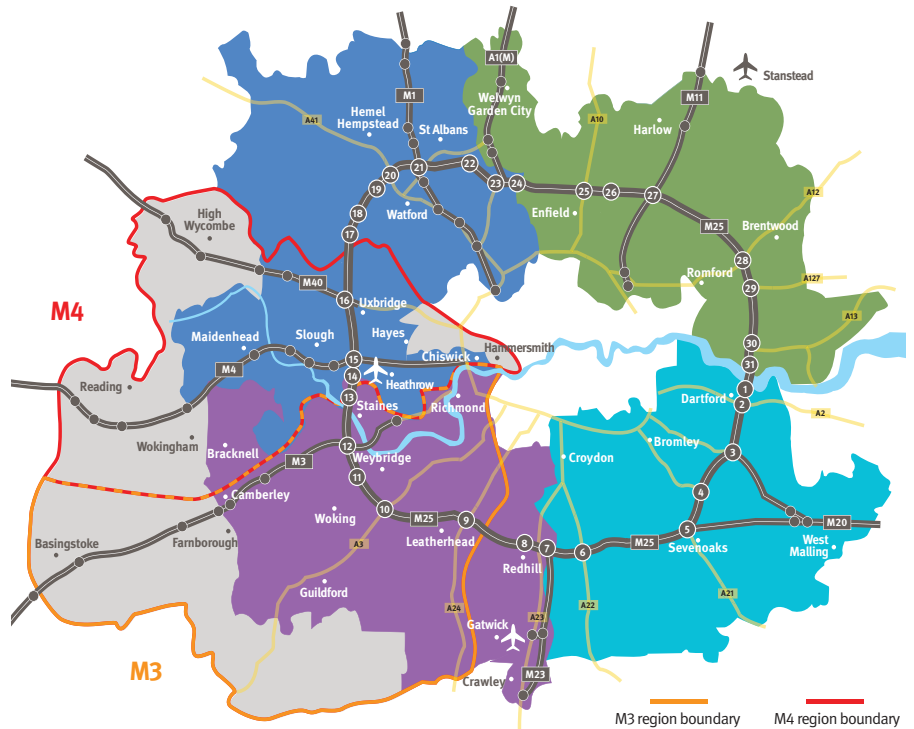
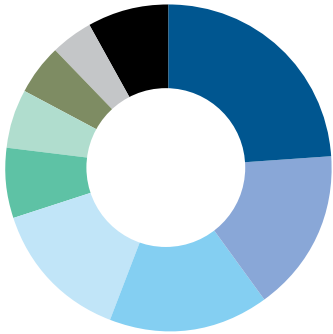


Table 2
Demand & Supply

Take-up	M25	NW	SW	NE	SE	M3	M4
Sq ft	646,517	295,553	270,902	48,104	31,958	179,616	426,377
Change Q1 13 vs Q4 12	18% ▲	-7% ▼	32% ▼	100% ▲	31% ▲	-12% ▼	46% ▲
Change Q1 13 vs Q1 12	35% ▲	63% ▲	72% ▲	-49% ▼	-31% ▼	-16% ▼	56% ▲
Q1 pre-let (sq ft)	135,000	135,000	0	0	0	0	135,000
Q1 % New & Grade A (inc. pre-lets)	82%	80%	80%	100%	86%	93%	85%
Forecast 2013 take-up (m sq ft)	2.10	1.00	0.85	0.10	0.15	0.85	1.75
Availability	M25	NW	SW	NE	SE	M3	M4
Sq ft	10,094,316	4,383,489	3,899,544	403,805	1,407,478	3,733,143	6,534,173
Change Q1 13 vs Q4 12	-4% ▼	-5% ▼	-1% ▼	-15% ▼	-2% ▼	1% ▲	0% ▲
Change Q1 13 vs Q1 12	-6% ▼	-9% ▼	-3% ▼	-9% ▼	1% ▲	-2% ▼	-6% ▼
Q1 % new	14%	13%	19%	13%	5%	11%	20%
Q1 % second-hand Grade A	51%	62%	49%	39%	22%	59%	60%
Q1 % second-hand Grade B	35%	25%	32%	48%	73%	30%	20%
Q1 vacancy rate (▲/▼ movement from Q4 12)	7.7% ▼	8.7% ▼	9.5% ▼	2.3% ▼	6.9% ▼	8.9% ▲	9.8% ▼
Under construction	M25	NW	SW	NE	SE	M3	M4
Sq ft (net approx)	1,266,905	694,298	293,524	0	279,524	293,524	997,345
Change 12 months	40% ▲	38% ▲	-27% ▼	-	100% ▲	-19% ▼	59% ▲
Pre-let	285,755	215,755	70,000	0	0	70,000	215,755

Figure 4

M25 active named enquiries by sector



Active demand is 6.53m sq ft at Q1 2013

Financial & Business Services	24%	▲
Technology, Media & Telecoms	16%	▲
Manufacturing & FMCGs	16%	▼
Retail, Distribution & Transport	14%	▲
Pharmaceutical & Medical	7%	▲
Construction & Engineering	6%	▼
Public Sector	5%	▼
Energy & Utilities	4%	▲
Other	8%	▼

Note: % = current share of demand
▲ = 12 month change (absolute terms)



FORECAST AT A GLANCE

Take-up:

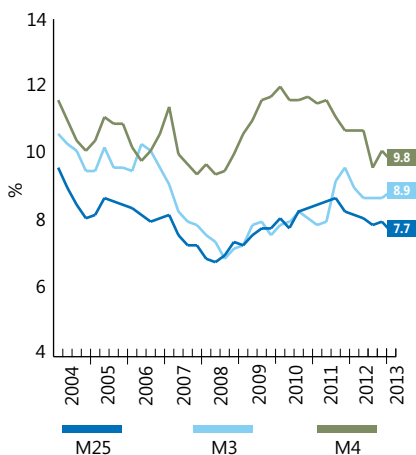
- 2013 started in positive fashion, albeit occupier activity remains predominantly focused in West London and the prime Thames Valley towns. Sentiment appears to be improving, reflecting the recent recovery of UK services sector output to its pre-recession high. Instances of lease re-gearing have reduced, while business expansion has replaced lease events as the dominant driver of activity.
- However, with active named demand standing a modest 11% higher than 12 months ago, our forecast remains one of gradual, rather than rapid, improvement in take-up. In the M25, 2.1m sq ft of take-up is forecast in 2013, up 5% on 2012 but 15% below the 10-year average. With demand continuing to focus in the Thames Valley markets, our forecast for the M4 is more bullish at 1.75m sq ft, or 5% above the 10-year average.
- With its resident supply of highly skilled labour and diverse occupier base, the South East market's longer term prospects are also positive. Continuous improvements to transport infrastructure, such as Heathrow Terminal 2 and Crossrail will also secure the South East's position as a key UK foothold for inward investment from the world's fast growing emerging markets, such as India, China and Latin America.

Supply and rents:

- Just as occupier confidence starts to show signs of improvement, the choice of accommodation is starting to diminish. Key markets in the Thames Valley and West London, such as Staines, Heathrow, Richmond and Hammersmith have reached tipping point, with less than two years' worth of supply available, given anticipated demand.
- However, with developers remaining cautious, the larger requirements in the market will increasingly be realised via pre-let commitments. Speculative development will occur selectively in resilient markets where passing rents can ensure a scheme's viability, typically in excess of £30 per sq ft. We also expect a significant proportion of future supply to involve back-to-frame refurbishments, with prime pitch, 1990s built stock being seen as increasingly ripe for repositioning.
- Much has been made of the government's relaxation on planning laws, allowing conversion of obsolete office space to residential uses. While this could be very positive in boosting housing supply and rebalancing a number of office markets, our analysis of current availability suggests that a maximum of 640,000 sq ft has the potential for residential conversion, equivalent to just 14% of total available Grade B space.

Figure 5

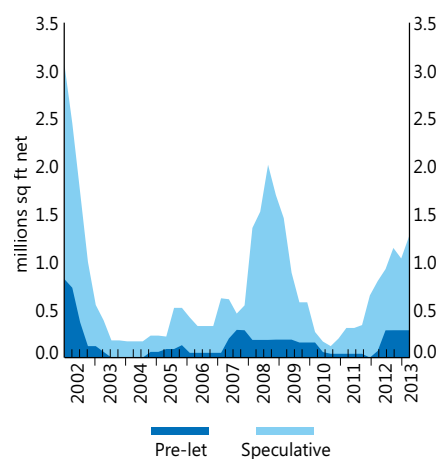
Vacancy rates



Source: Knight Frank Research

Figure 6

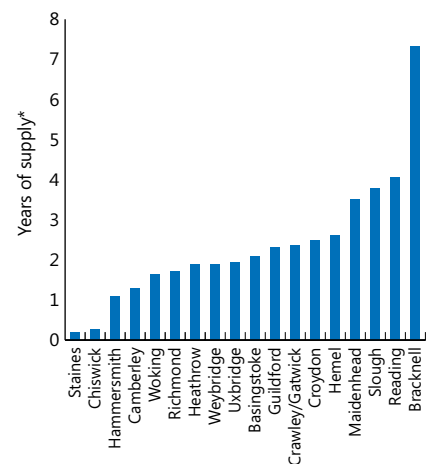
Space under construction in the M25



Source: Knight Frank Research

Figure 7

New & Grade A supply in key markets



Source: Knight Frank Research
* Based on average New & Grade A take-up vs current New & Grade A availability

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Investment market

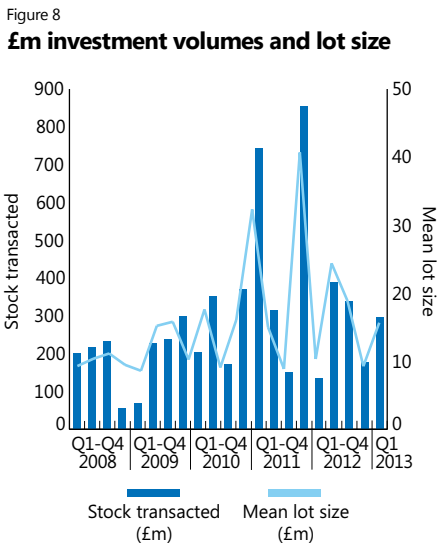
Table 3
Key investment transactions Q1 2013

Building	Size (sq ft)	Price	Net Initial Yield	Vendor/Purchaser
Chiswick Tower, Chiswick	143,000	£56.50m	7.00%	Harbert / Hermes
5 Longwalk, Stockley Park, Heathrow	114,392	£42.45m	6.32%	Schroders / Peninvest
Pearson Building, Harlow	139,714	£23.10m	10.25%	AXA / M&M Fund Management
Harman House, Uxbridge	129,831	£17.26m	9.36%	Threadneedle / Mercer
45 Grosvenor Road, St Albans	62,361	£10.15m	8.75%	PRUPIM / Threadneedle

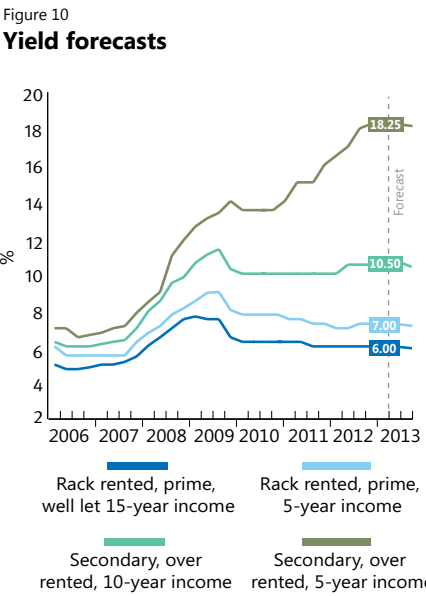
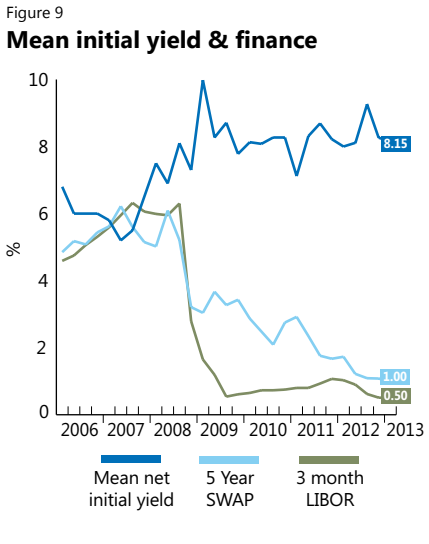
	Transaction volume	Mean lot size	Mean NIY
Q1 2013	£297.53m	£15.66m	8.15%
Change 3 mths	72% ▲	72% ▲	116bps ▲
Change 12 mths	136% ▲	49% ▲	58bps ▲

INVESTMENT VIEW

- For the 'right' type of product, investment demand for South East offices is stronger now than at any time during the last six years. With limited stock available, yields for both prime long income product and good quality secondary stock are expected to come under downward pressure as the year progresses.
- Total turnover amounted to £298m in Q1, 72% above Q4 2012's total and closely in line with the five year quarterly average. However, the increase was largely owed to several large lot-sizes changing hands, with Q1's 19 deals equal to the amount seen in the previous quarter.
- Buoyed by signs of recovery in the occupier market, the traditional UK Funds and a number of overseas investors are seeking higher yielding, asset management opportunities. Examples from Q1 include Mercer's purchase of Harman House, Uxbridge and Threadneedle's purchase of 45 Grosvenor House, St Albans.
- There is also a growing perception among overseas investors that the South East market represents good value compared with Central London. Q1 saw the latest Middle Eastern investor enter the market, with Peninvest's purchase of 5 Longwalk, Stockley Park, Heathrow, while there is evidence of growing interest from Far Eastern investors looking to acquire secure assets in the South East.



Source: Knight Frank Research



Americas

USA
Canada
Caribbean

Australasia

Australia
New Zealand

Europe

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

Africa

Botswana
Kenya
Malawi
Nigeria
South Africa
Tanzania
Uganda
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Technical Note

- Knight Frank define 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 66.5m 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 42.0m 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.
- The market definition used, shown in the map on page 3, is based on Local Authority District boundaries.
- 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 128m sq ft (net), an M4 market stock of 63.5m sq ft (net) and an M3 market stock of 42m sq ft (net).
- 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.
- 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 March 31st 2013.

Front cover image: Griffin House, Hammersmith which is owned by LaSalle Investment Management and where Virgin Media leased 44,175 sq ft in Q1.

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