RESEARCH

CENTRAL LONDON
QUARTERLY – OFFICES
Q1 2017

CENTRAL LONDON RENTS REMAIN STABLE
CENTRAL LONDON PRIME YIELDS REMAIN STABLE
SUPPLY CONTINUES TO INCREASE ACROSS CENTRAL LONDON
The rise of Digital Ubiquity.

As an issue shaping occupier demand, leaving the EU will be gradually overshadowed in the next two years by the rise of Digital Ubiquity.

After the strong take-up recorded in Q4 last year, it would have been reasonable to expect a weak first quarter for occupier demand in Central London. Yet take-up has come in exactly at the long-term average – 3.1m sq ft. This cannot be dismissed as a few big deals inflating the figures. Deals of over 100,000 sq ft accounted for 17.5% of take-up, which is line with activity in the last ten years.

As in the previous quarter, the better-than-expected performance owes much to the on-going change in the composition of demand. In Q1, the Tech and Creative sector took over 700,000 sq ft of office space, towering over the finance sector at around 270,000 sq ft.

Take-up for Tech and Creative firms is running nearly 12% above long-term average, but this is perhaps generating a false impression of demand overall.

By holding up so well, tech is disguising the clear weakening of finance activity.

Meanwhile, Professional take-up was strong in part because some firms are consolidating and moving support jobs out of London.

Consequently, on demand we have a neutral situation. Some banks and lawyers reduce their London footprint (but do not leave entirely), then growth from the techs balances the books by absorbing the surplus space. The net result is average take-up, which is better than most would have expected nine months ago, but hardly the high-growth London we were so proud of back in 2015. So what might take demand above the average level in the future?

The answer relates to what I call Digital Ubiquity. I see this increasingly shaping office demand, as non-tech firms bring themselves in line with technology trends whose impact vastly overshadows the transitory phenomenon of Brexit.

At a time when there is concern over the outlook for the banking industry, we have the paradox of banks looking for new space to house their digital businesses. Some law firms are freeing up office space to start their own tech incubators and accelerators. Older tech firms are relocating from cheap out-of-town offices to trendy and more expensive central London districts, to be near the new wave in the digital revolution.

The tech and creative ethos and work practice is colonising the rest of the business world, as many firms are hungry to adapt to the sudden and unexpected arrival of digital start-up competitors in their industries. Adaptation requires investment in reshaping the work environment, as people are the bedrock of an innovation economy, and a new office format can energise idea-sharing and communication.

This march to Digital Ubiquity was tentatively emerging trend in 2015, then it hit a road bump in 2016 with Brexit, which put a lot of business investment on hold temporarily. However, there are signs that Brexit is not going to be as disruptive as previously feared. The government is hinting at a transition deal, whereby EU rules will stay in place and free movement of labour continues beyond March 2019. In other words, we are heading for a compromise.

As this becomes more evident, the brakes on investment in the business world will be removed, and more non-tech firms will turn their attention back to transitioning to Digital Ubiquity. Most firms in the future, irrespective of industry, will operate the tech way, with knock-on implications for office demand.

In January there was widespread concern that banks would leave London en-masse, then in February the German Finance Minister told a conference “the financial centre of London will remain and be important to the EU economy as a whole”. Brexit is receding as a threat to the outlook, and with employment levels currently at a record high, the pre-referendum trends in the London office market are resurfacing.

JAMES ROBERTS
Partner, Chief Economist

“Brexit is receding as a threat to the outlook, and with employment levels currently at a record high, the pre-referendum trends in the London office market are resurfacing.”
Take-up
Take-up in the first quarter of 2017 reached 1.47m sq ft, a rise of 44% on the previous quarter, and 27% ahead of the long-term quarterly average. Fitzrovia saw the largest increase in take-up, with 356,142 sq ft in the first quarter, 50% above the long-term quarterly average.

Active requirements
Total active requirements fell by 18% on the quarter to 3.21m sq ft, largely due to a number of requirements transacting during the last three months, however this is 17% ahead of the long-term average and is broadly in line with the same quarter last year. The demand profile was dominated by both TMT and corporates accounting for 37% and 20% of demand respectively. There were currently four requirements over 100,000 sq ft, and a further ten of 50,000 sq ft or over.

Supplementary development
Availability across the West End totalled 5.0m sq ft at the end of the first quarter of 2017, a fall of 12% on the previous quarter, and the first time West End supply has fallen for five consecutive quarters. Despite this, availability is still 14% above long-term average levels and 26% ahead of the same point last year. The decrease in supply can be attributed to a strong quarter of take-up, pared with a reduction in development completions in comparison to previous quarters. Another factor is the 26% fall in second-hand Grade A supply quarter-on-quarter. Looking forward, supply levels are likely to be kept in check by the severely restricted speculative development pipeline in 2017.

Prime rents and incentives
In the West End, the prime rent remained stable at £105.00 per sq ft for the second consecutive quarter. Rent free periods remained unchanged at 18-21 months on a typical 10-year lease.

Investment
West End investment turnover in Q1 2017 totalled £2.05bn, 19% below the level recorded in Q4 2016, but just 6% below the long-term average of 1.73m sq ft. The only submarket to record a growth in take-up from the previous quarter was Midtown, where levels increased by 58%.

The largest deal in the City, and across the entire London market, was the pre-letting of circa 256,000 sq ft to Freshfields Bruckhaus Deringer LLP at 100 Bishopsgate, EC2. The TMT sector continued to be the most active during Q1; the sector accounted for 39% of take-up, and half of the 10 largest deals. The professional sector was also buoyant, accounting for 32% of take-up.

Active requirements
Total active requirements increased by 24% from 3.65m sq ft in Q4 to 4.54m sq ft in the first quarter of the year, 12% above the long-term average. There was a significant rise in demand from both the TMT and financial sectors. Demand from the TMT sector increased by 77% totalling over 1.16m sq ft, while financial sector demand increased for the second consecutive quarter, totalling 1.47m sq ft, the highest level since Q2 2014.

Supply and development
City availability increased 12% from 7.73m sq ft at the end of 2016 to 8.60m sq ft by the end of Q1 2017, however levels are still 8% below the long-term average of 9.32m sq ft. The vacancy rate now stands at 7.1%, the highest level since Q3 2014. Despite the increase in supply, it should be noted that a significant amount (1.60m sq ft) of stock is currently under offer across the City. Supply of new and refurbished space totalled 3.39m sq ft on par with the long-term average.

There is currently 5.39m sq ft under construction speculatively, 14% above the level recorded the same quarter last year. There is just over 2.25m sq ft under construction due to complete this year; however 25% is already committed.

Prime rents and incentives
The prime rent remained stable at £105.00 per sq ft for the sixth consecutive quarter. Rent free periods remained unchanged from the previous quarter’s level at 21-24 months on a typical 10-year term certain.

Investment
Investment turnover in the City was £2.59bn on par with the previous quarter and 42% above the long-term average. Overseas purchasers accounted for 81% of all transactions during Q1 by value. The largest transaction of the quarter was the purchase of The Leadenhall Building for £1.15bn, which accounted for 44% of the total deal volume. Far Eastern investors continued to be dominant, accounting for 82% of total sales. There were seven transactions which took place over £100m, six of which involved overseas purchasers. Domestic buyers accounted for 17 of the 35 deals which took place during Q1, which accounted for 44% of the total deal volume. Far Eastern investors continued to be dominant, accounting for 82% of total sales. There were seven transactions which took place over £100m, six of which involved overseas purchasers. Domestic buyers accounted for 17 of the 35 deals which took place during Q1, which accounted for 44% of the total deal volume. Far Eastern investors continued to be dominant, accounting for 82% of total sales.
Central London has witnessed the birth of a number of new markets in recent times; the Southbank, Paddington and King’s Cross to name a few. These markets have succeeded due to the quality of space constructed, extensive transport infrastructure (both existing and new), and the delivery of new amenity encouraging a mix of uses.

White City is the latest new market, and has a clear advantage over the other new office markets created in Central London over the last 20 years: much of the infrastructure, amenity and culture for which new areas strive is already in place.

The area has one of the highest ratings for public transport accessibility in London; Westfield London, Television Centre and nearby Notting Hill provide existing and planned leisure provision; and the future presence of Imperial College’s campus, the Royal College of Art, and Soho House will contribute by offering an academic, creative and social environment.

The office stock is dominated by the new White City Place development, offering 822,000 sq ft of space across four buildings:

- The MediaWorks, a 231,000 sq ft new building, has secured a 70,000 sq ft pre-let to online retailer Yoox Net-a-Porter, with a further 23,000 sq ft let to HuckleTree
- Garden House, totalling 39,000 sq ft has been let to The Royal College of Art
- WestWorks, a new 296,250 sq ft building, is under construction and due for completion in Q2 2017
- 2 Television Centre, a new 273,000 sq ft speculative scheme under construction and due for completion in Q1 2018

The paucity of development pipeline space across Central London along with prime headline rents near all-time highs in the majority of submarkets, will drive tenants’ searches towards attractively-priced, quality space. The relative discount of White City, where the prime rent is estimated to be £52.50 per sq ft with business rates of circa £17.00 per sq ft, suggests the area will increasingly feature in tenants’ searches.
“Although take-up in Docklands has been uncharacteristically low, this is the first time levels have dropped below 50,000 sq ft in four years.”

Demand
Total take-up for Q1 2017 totalled just over 30,000 sq ft, the lowest figure for some years and well below the long-term average of 245,000 sq ft. The largest transaction of the quarter was at Capstan House, 1 Clove Crescent where Deliveroo acquired circa 15,000 sq ft on a short-term lease.

Take-up has been uncharacteristically low; this is the first time levels have dropped below 50,000 sq ft in four years. The level of take-up in Q4 2016 was the highest quarterly figure recorded in the last six years.

Active requirements
Total active requirements in Docklands increased by 18% to 709,000 sq ft, nearly 55% above the long-term average. The largest source of demand came from the corporate sector followed by the public sector.

Supply and development
Supply levels increased by 44% quarter-on-quarter from 0.81m sq ft in Q4 2016 to 1.17m sq ft in the first quarter, but still below the long-term average of 1.41m sq ft. The vacancy rate increased from 4.1% to 6.0%. Availability continues to comprise second-hand stock, with no new or refurbished supply on the market since Q3 2015.

There is no new & refurbished stock due to be delivered to the market until Q2 2019, and there is still just one building in Canary Wharf that is under construction: 1 Bank Street totalling 700,000 sq ft, which is not due for completion until 2019, but are likely to remain on hold until a pre-let is secured.

Rental profile
The prime headline rent remained stable at £39.00 per sq ft for the sixth consecutive quarter.

Investment
There were no investment sales during Q1 in Canary Wharf or the wider Docklands market. There is just one asset for sale in Canary Wharf: 20 Canada Square which is currently on the market for £418m, reflecting a NIV of 5.25% and a capital value of £720 per sq ft. The lack of stock in this market will continue to influence the investment figures for the foreseeable future.

Docklands Take-up (sq ft)

Central London take-up remains healthy, the first quarter of 2016 saw take-up reach long-term average levels and exceeded the long-term Q1 average by 12%

Central London Investment Turnover
Q1 2017
Overseas investors continue to target Central London assets
**KEY STATISTICS**

Central London office market

### CONSTRUCTION REQUIREMENTS

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<tr>
<th>Quarter</th>
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### AVAILABILITY (% CHANGE)

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### UNDER CONSTRUCTION (sq ft)

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### ACTIVE REQUIREMENTS (sq ft)

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### TAKE-UP (sq ft)

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### INVESTMENT (£ mn)

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#### THE CENTRAL LONDON OFFICE MARKET

**WEST END**

- **West End Core** – West End Core refers to Mayfair and St. James’s, 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.
- **North of Mayfair** – North of Mayfair refers to the area north of Oxford Street, west of Portland Place.
- **Fitzrovia** – Fitzrovia also known as Noho, refers to the area north of Oxford Street, east of Portland Place.
- **Soho** – Soho refers to W1B, W1F and W1D.

**CITY**

- **City Core** – City Core refers to EC2 (excluding EC2A), EC3, EC4 (excluding EC4A and EC4Y), and EC4A.
- **Midtown** – Midtown refers to EC1N, EC1A, EC1Y, WC1 (excluding Bloomsbury), and WC2 (excluding Strand/Covent Garden).
- **Shoreditch/Clerkenwell** – Shoreditch/Clerkenwell refers to EC1 (excluding EC1A and EC1N), and EC2A.
- **Aldgate/Whitechapel** – Aldgate/Whitechapel refers to E1.
- **Southbank** – Southbank refers to SE1.

**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 Royal Business Park (excluding Canary Wharf).

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Source: Knight Frank Research
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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