THE CENTRE OF LONDON

2017-18 London Office & Retail Market Report

UNION STREET PARTNERS

Farebrother

IN THIS EDITION

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EXECUTIVE SUMMARY

2017 HEADLINES

4.4 m sq ft Total Take-up — **+27** % on 2016

4.1 % Availability Rate — **+0.3** pts on 2016

£5.1 bn Investment Turnover — **+56** % on 2016

The occupier and investment markets enjoyed a successful year. Performance across both exceeded expectations despite the shadow of Brexit and general market uncertainty. Although the General Election result was initially a shock, it had no effect on overall market activity and it was business as usual.

Total take-up in 2017 was 4.4m sq ft, the second highest over the past decade and 27% up on 2016. Pre-lets and new and refurbished took 55% of total leased volume, the highest for the past 10 years, compared with an average of 38% for the decade. The DAMIT sector once again accounted for the largest proportion of leasing activity. After a very strong finish to 2017, occupier activity is likely to moderate in the coming months.

Availability rose by 13% over the year to stand at 2.7m sq ft at the end of 2017. It however remained below the long-term average. Around 1.3m sq ft is currently under construction and due for delivery in 2018. This should alleviate some of the pressure on supply. The pipeline remains limited in 2019 and beyond and the market needs more development stock to cope with solid demand and restricted supply.

On the investment front, 2017 was notable for the first rise in interest for 10 years – up from 0.25% to 0.5%. Sterling remained weak for most of 2017 but rallied at the end of the year. Despite the unsettling effect of the General Election and Brexit politics, London outperformed its European rivals and delivered over 20bn of transactions, with overseas investment continuing to grow. Turnover in the Centre of London was £5.14bn, the second highest in 10 years. While investment activity is likely to soften, London's overall investment appeal seems unshakeable.

The retail and leisure market faced higher inflation and Brexit uncertainty in 2017. Even so, it performed well, and operators are delivering high-quality space throughout the Centre of London. Brexit has undermined retailer confidence for some deals, but activity will increase as consumer spending and confidence strengthen, while London remains a draw for retailers.

TAKE-UP

TOTAL TAKE-UP

4.4 M SQ FT

change on 2016
+27%
10-year Annual Average
3.8m sq ft

TAKE-UP NEW & REFURBISHED

2.5 M SQ FT

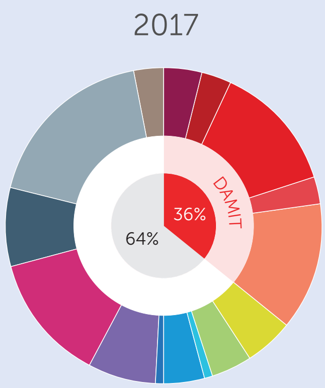
change on 2016
+31%
10-year Annual Average
1.5m sq ft

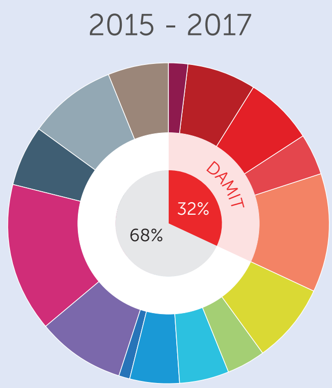
TAKE-UP SECONDHAND

1.9 M SQ FT

change on 2016
+22%
10-year Annual Average
2.3m sq ft

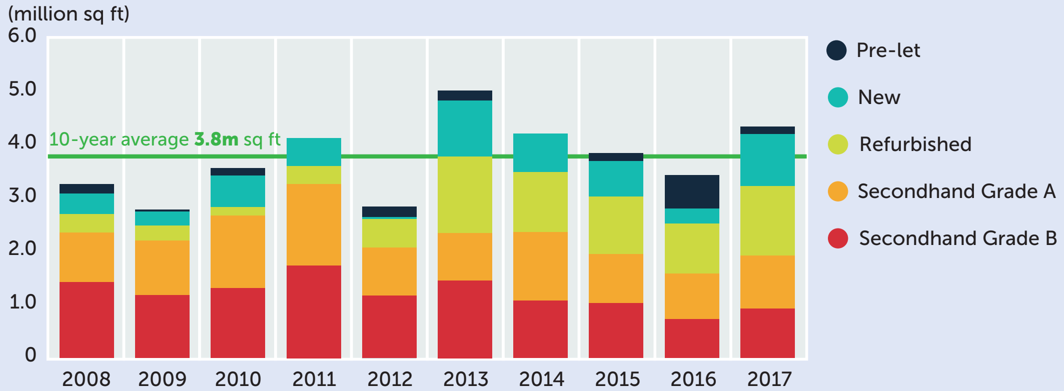
FIG. 1 TAKE-UP BY SECTOR





2017	SECTOR	2015 - 2017
4%	Design	2%
3%	Advertising, Marketing & PR	7%
13%	Media	7%
3%	Internet	4%
13%	Technology & Telecoms	12%
5%	Banking, Finance & Insurance	8%
4%	Charities & Associations	4%
1%	Corporate	5%
4%	Education	5%
1%	Government	1%
7%	Legal	9%
13%	Professional Services	15%
8%	Retail & Leisure	6%
18%	**Serviced Offices**	9%
3%	Other	6%

FIG. 2 ANNUAL TAKE-UP BY GRADE



Robust finish to the year with a spike in new & refurbished take-up

The market experienced continuing uncertainty during 2017, but the year finished strongly and we recorded the second highest level of take-up over the past 10 years. Total take-up reached 4.4m sq ft, 27% higher than 2016 and 16% above the 10-year average of 3.8m sq ft.

Occupier strategy in 2017 focused on upgrading their offices. Pre-lets and new and refurbished space accounted for 55% of total take-up throughout the year. This was the highest proportion over the past 10 years and compares with an average of 38% during the decade.

There was a surge in number of large transactions during 2017, with a total of 14 deals in excess of 50,000 sq ft across the whole of the Centre of London, up from eight transactions in 2016. More than half of these transactions were in WC1 and WC2. Conversely, smaller transactions predominated in SE1 and EC1, with 71 and 61 deals in the 1-3,500 sq ft range in these postcode areas respectively. Figures 3 and 4 illustrate the Centre of London take-up by size band and average transaction sizes across individual postcodes.

The two largest transactions in 2017 were done by WeWork at Two Southbank Place, SE1 (284,922 sq ft), followed by 125 Shaftesbury Avenue, WC2 (140,000 sq ft). Other notable deals were Spotify's leasing of 104,133 sq ft at The Adelphi, 1-11 John Adam Street, WC2, and McKinsey & Company's 96,999 sq ft transaction at The Post Building, 21-31 New Oxford Street, WC1.

The DAMIT sector, with a 36% share of take-up in 2017, again accounted for the largest proportion of leasing activity. Next, at 18%, was serviced office operators, a rapidly growing component of the Centre of London market, with their share of take-up doubling in the space of three years.

In third place was the professional services sector, representing 13% of the total annual take-up. The trend in the Centre of London is for an increasingly diverse and fluid tenant base, with occupiers moving in from other parts of the capital. An example is PetroChina, which relocated from Victoria to The Adelphi, 1-11 John Adam Street, WC2.

OUTLOOK

Despite economic and political uncertainty, occupier confidence is anticipated to remain strong in 2018. The market is backed by diversity and resilient fundamentals. DAMIT share of take-up has doubled since 2015 and continued growth is expected, while the rising demand for serviced offices across all size tiers will affect the dynamics of the occupier market, particularly the sub 5,000 sq ft bracket. However, after a very active finish to 2017, the occupier market is likely to see leasing volumes ease in the coming months.

FIG. 3 **PROPORTION OF TAKE-UP BY NUMBER OF TRANSACTIONS IN INDIVIDUAL POSTCODES**

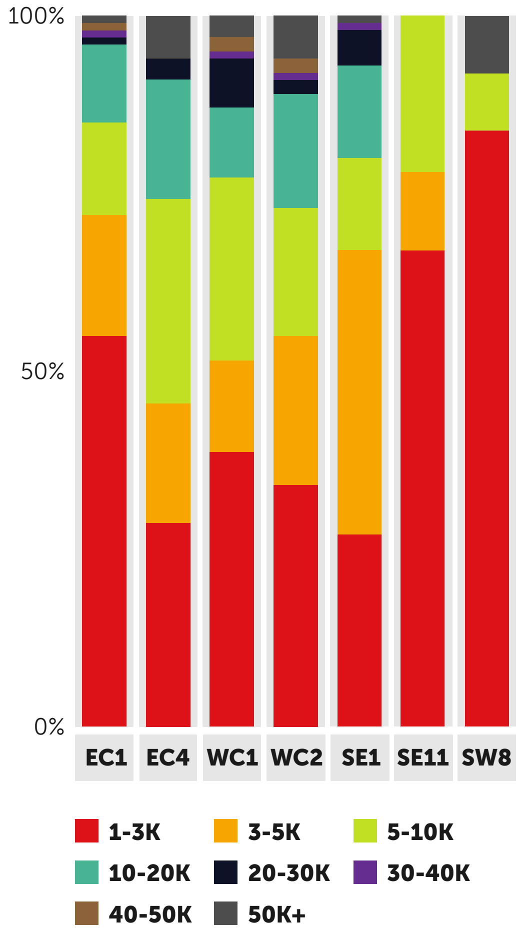
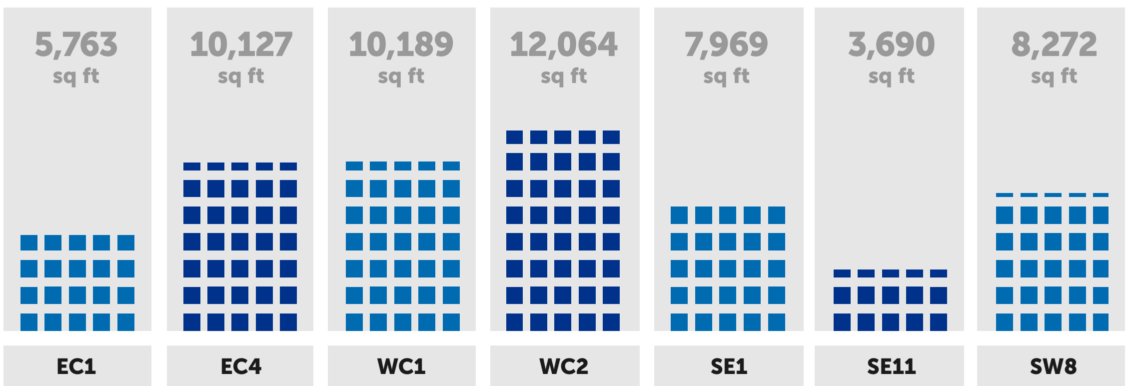
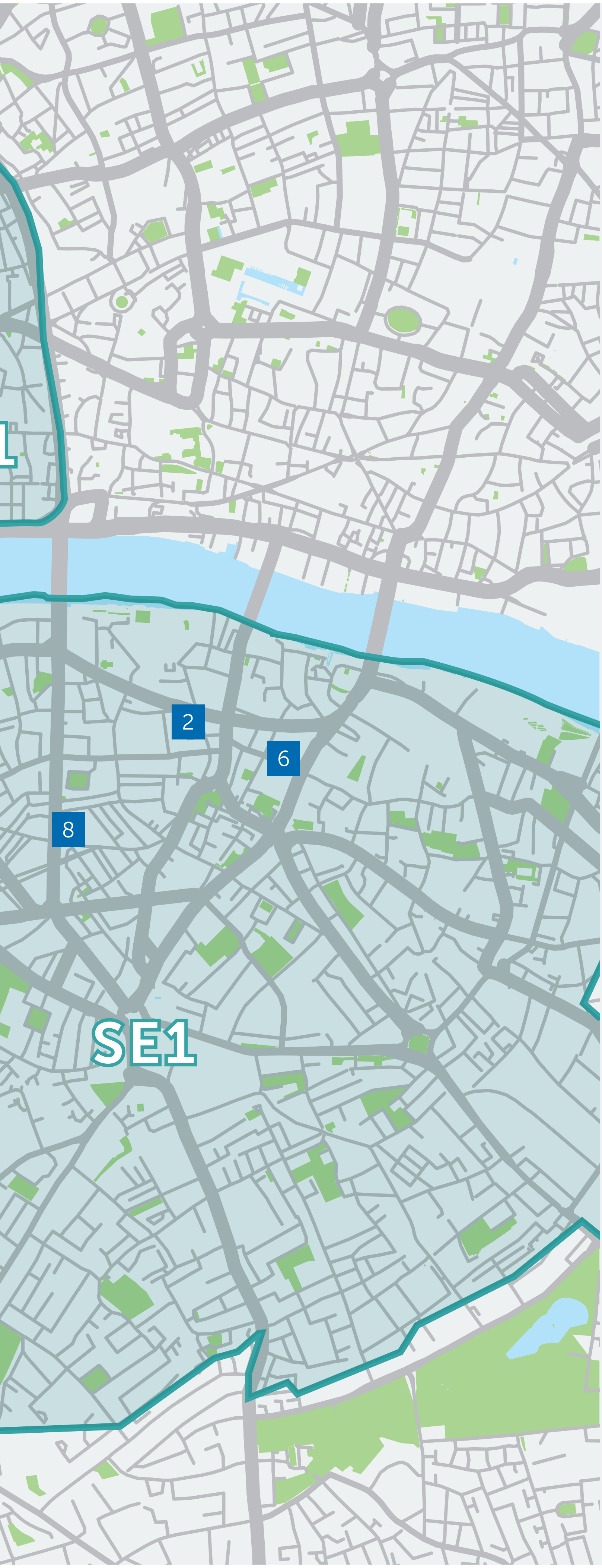


FIG. 4 **AVERAGE TRANSACTION SIZE BY POSTCODE**





KEY TRANSACTIONS 2017

THE POST BUILDING,
21-31 NEW OXFORD STREET, WC1

Size: 96,999 sq ft
Grade: Let During Construction
Tenant: McKinsey & Co.
Rent: Confidential

HARLEQUIN BUILDING
65 SOUTHWARK STREET, SE1

Size: 14,591 sq ft
Grade: Secondhand A
Tenant: Wonga
Rent: £59.00 psf

125 SHAFTESBURY AVENUE, WC2

Size: 140,000 sq ft
Grade: Pre-let
Tenant: WeWork
Rent: Confidential

TWO SOUTHBANK PLACE, SE1

Size: 284,922 sq ft
Grade: Let During Construction
Tenant: WeWork
Rent: Confidential

THE ADELPHI, 1-11 JOHN ADAM STREET, WC2

Size: 104,133 sq ft
Grade: Refurbished
Tenant: Spotify
Rent: £62.50 psf (blend)
£82.50 psf (upper floors)

10-18 UNION STREET,
SE1

Size: 55,924 sq ft
Grade: Secondhand B
Owner: RCOG
Rent: Owner Occupier

THE CURSITOR BUILDING,
CHANCERY LANE, WC2

Size: 49,154 sq ft
Grade: Refurbished
Tenant: WeWork
Rent: £63.50 psf

160 BLACKFRIARS ROAD,
SE1

Size: 23,631 sq ft
Grade: Secondhand A
Tenant: Experian
Rent: £52.50 psf

AVAILABILITY

TOTAL AVAILABILITY

2.7 M SQ FT

change on 2016
+13%
10-year Annual Average
3.5m sq ft

AVAILABILITY RATE

3.8 %

change on 2016
+0.3 pts
10-year Annual Average
5.3%

AVAILABILITY NEW & REFURBISHED

921,599 M SQ FT

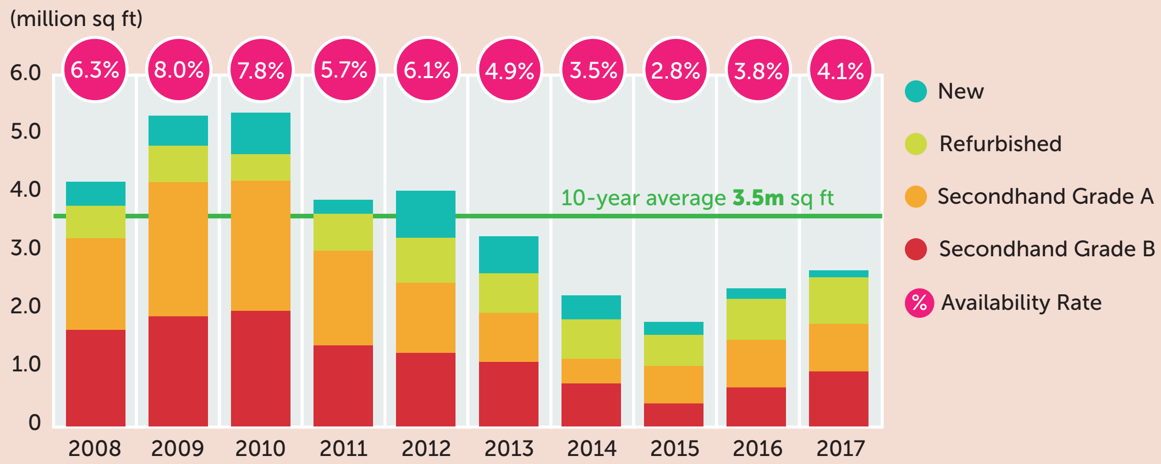
change on 2016
+4%
10-year Annual Average
1.1m sq ft

AVAILABILITY SECONDHAND

1.8 M SQ FT

change on 2016
+18%
10-year Annual Average
2.5m sq ft

FIG. 5 **AVAILABILITY BY GRADE**



Supply rose year-on-year but the proportion of new & refurbished availability shrinking

Availability increased across the Centre of London for the second year running and reached 2.7m sq ft at the end of 2017. Although this was 13% higher than 2016, it is still below the long-term average of 3.5m sq ft. The availability rate in the Centre of London stood at 4.1% at the end of the year, up from 3.8% in 2016. The Centre of London availability rate remained the lowest in the wider London market.

The amount of new and refurbished space entering the market during 2017 was high at 1.3m sq ft. However, space was eroded by lettings, resulting in only a marginal uplift of 4% over the year in this type of availability. New and refurbished availability stood at 921,599 sq ft, representing 34% of the total market supply. It remained approximately 18% below the long-term average of 1.1m sq ft.

Secondhand space increased during the year, in keeping with our projections in the last edition of the Centre of London report. There was an 18% rise in the amount of secondhand accommodation immediately available, reaching 1.8m sq ft at the end of 2017. This was the highest since 2013 and amounted to 66% of total market availability.

The uplift in secondhand supply is usually the result of tenants offloading space to the market, or new availability arising from a lease event, surplus created by mergers and acquisitions, or enterprises downsizing their operations.

FIG. 6 **AVAILABILITY IN CONTEXT OF THE WIDER LONDON MARKET**

AVAILABILITY	WEST END	CENTRE OF LONDON	CITY
New & Refurbished (sq ft)	1,177,872	921,599	1,627,714
Secondhand A (sq ft)	2,008,591	818,218	3,721,786
Secondhand B (sq ft)	766,330	946,050	1,852,911
Total (sq ft)	3,952,793	2,685,868	7,202,411
Stock (sq ft)	72,598,236	65,085,416	69,303,244
Availability Rate (%)	**5.4**	**4.1**	**10.4**

OUTLOOK

There is an underlying lack of supply in the Centre of London, and the availability of grey space will continue to be an important market driver. With new and refurbished accommodation still below the long-term trend, choice remains limited for occupiers across much of the market, albeit some uplift is anticipated throughout 2018. Landlords should consider strategies to deliver additional tenant amenity to the market.

DEVELOPMENT PIPELINE

TOTAL SPECULATIVE SPACE UNDER CONSTRUCTION

1.8 M SQ FT

change on 2016 -44%

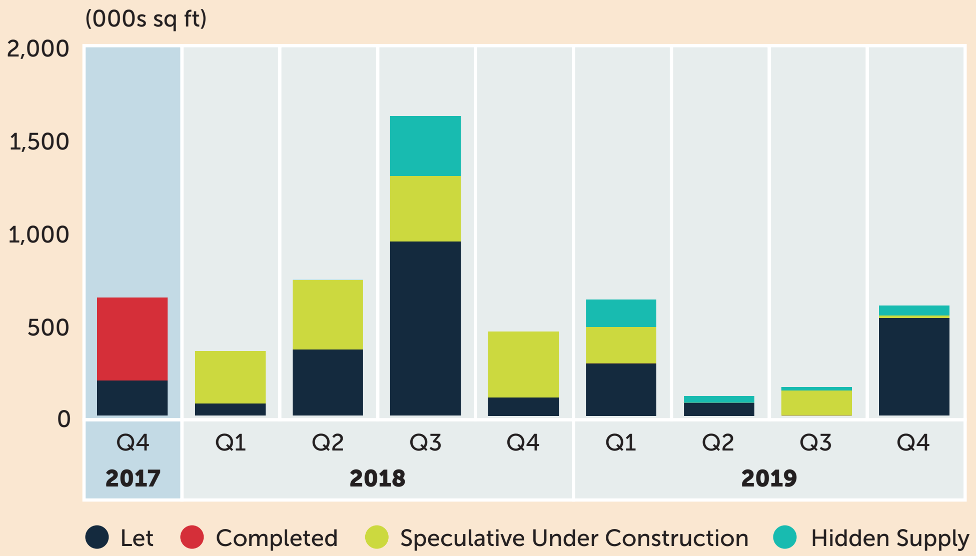
SPECULATIVE CONSTRUCTION H1 2018

658,169 SQ FT

SPECULATIVE CONSTRUCTION H2 2018

619,284 SQ FT

FIG. 7 **FUTURE SUPPLY BY STATUS AND QUARTER OF DELIVERY**



Majority of speculative space under construction scheduled for delivery in 2018

A total of 4.0m sq ft was under construction across the Centre of London market at the end of 2017. However, more than half of this space was committed, with 1.8m sq ft under construction speculatively. Compared to 2016, the volume of speculative space under construction contracted by 44%, mainly as a result of WeWork's leasing of the entire Two Southbank Place, SE1.

Just under 1.3m sq ft is due for delivery in 2018, with completions peaking in the second half of the year. HB Reavis's schemes at 20 Farringdon Street, EC4 (84,554 sq ft) and Cooper & Southwark, SE1 (64,443 sq ft) are the most notable deliveries expected in the first quarter of 2018.

One Bartholomew Close, EC1 (211,244 sq ft), by developers Helical Bar and Ashby Capital, is due in the third quarter. A further 137,000 sq ft of speculative space is anticipated to complete at The Post Building, 21-31 New Oxford Street, WC1, in the fourth quarter of 2018. The developers are Oxford Properties and Brockton Capital. The Ray Farringdon, EC1 (88,908 sq ft), by Viridis Real Estate, is also due in the final quarter.

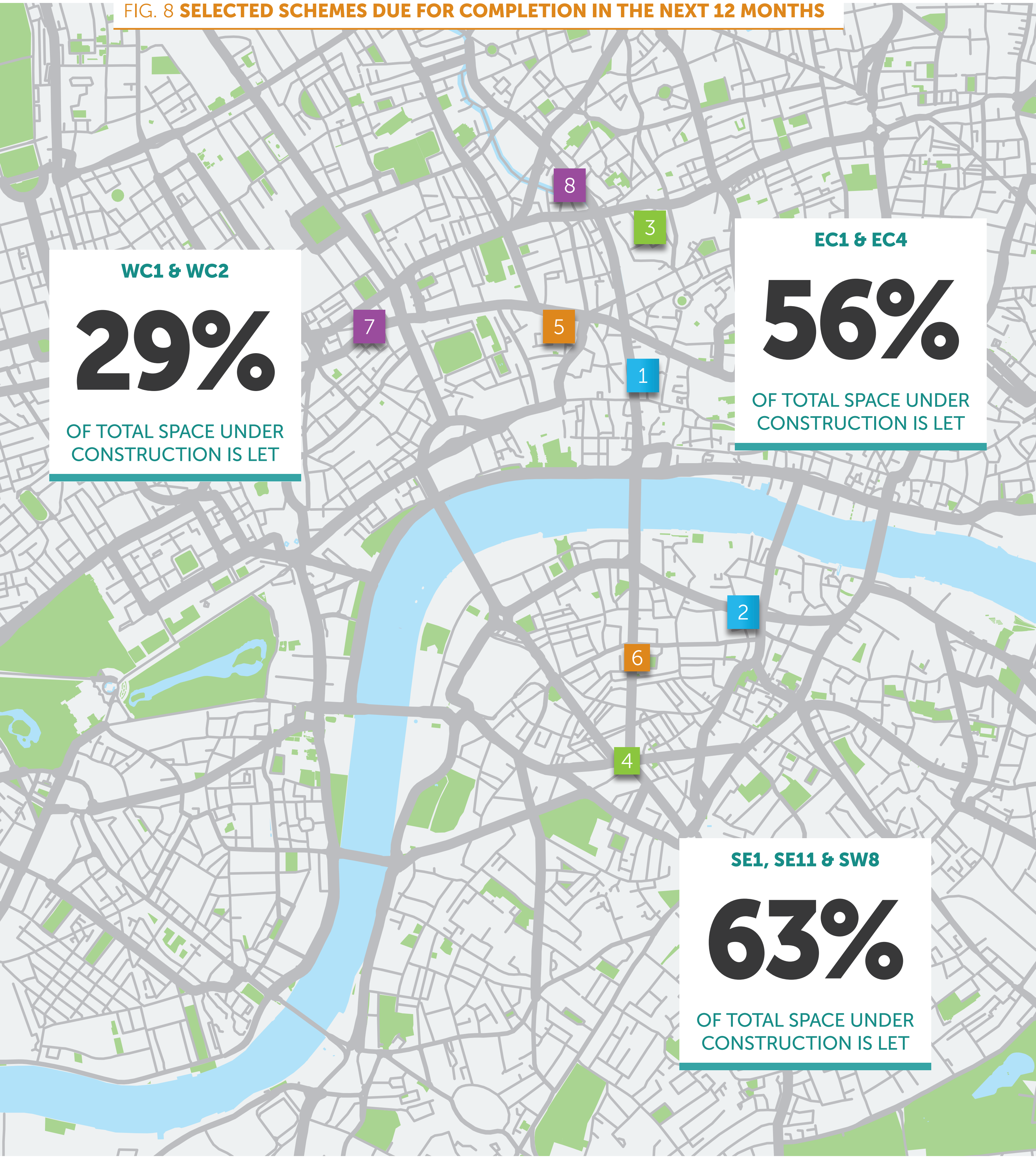
Looking to 2019 and beyond, the pipeline remains limited. There is currently 428,783 sq ft under construction and scheduled for delivery by the end of 2020. The most notable scheme north of the river is The Farmiloe Building, 34 St John Street, EC1 (59,234 sq ft), by Aberdeen Standard Investments. Construction began in the fourth quarter of 2017 and is expected to complete in the first quarter of 2019. South of the river, the key schemes are Two Southbank Place, SE1, along with Battersea Power Station, SW8, which are both let.

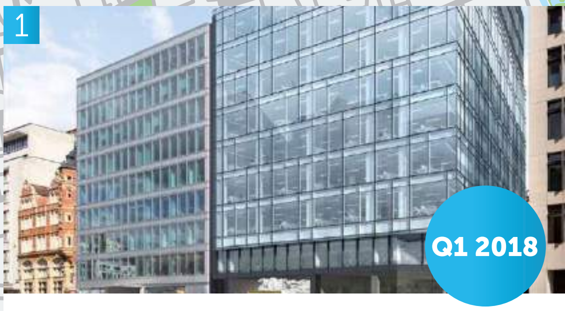
In addition to the schemes currently in the pipeline, we have also reviewed potential future opportunities. Just under 324,000 sq ft of Hidden Supply, mainly north of the river, is likely to come on to the market during 2018.

OUTLOOK

The amount of speculative space under construction is declining and more development stock will be needed to meet strong demand. There are also concerns about the impact of Brexit on developers' risk appetite and available funding options. This may lead to refurbishments with shorter delivery times and quicker returns, rather than major developments and new schemes.

FIG. 8 **SELECTED SCHEMES DUE FOR COMPLETION IN THE NEXT 12 MONTHS**



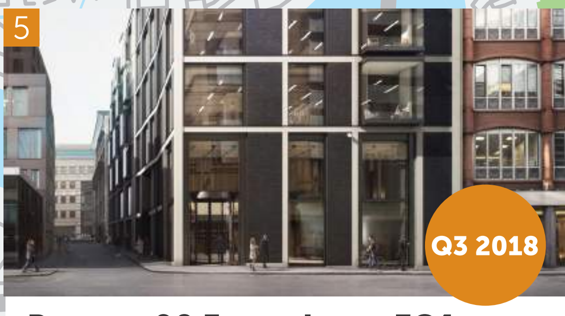


20 Farringdon Street, EC4
84,554 sq ft

Cooper & Southwark, SE1
64,443 sq ft

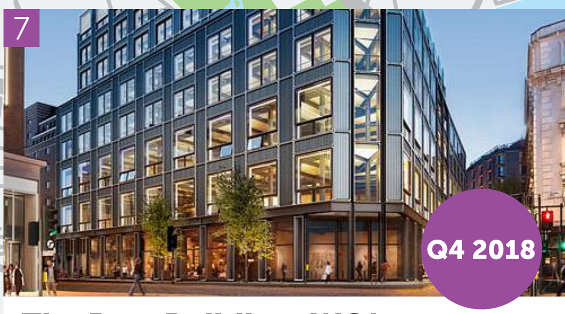
The Smithson, 6-9 Briset Street, EC1
47,905 sq ft

Blackfriars Circus, SE1
31,317 sq ft



Bureau, 90 Fetter Lane, EC4
60,859 sq ft

209 Blackfriars Road, SE1
31,218 sq ft



The Post Building, WC1
263,000 sq ft (137,000 sq ft speculative)

The Ray Farringdon, EC1
88,908 sq ft

INVESTMENT

INVESTMENT TURNOVER

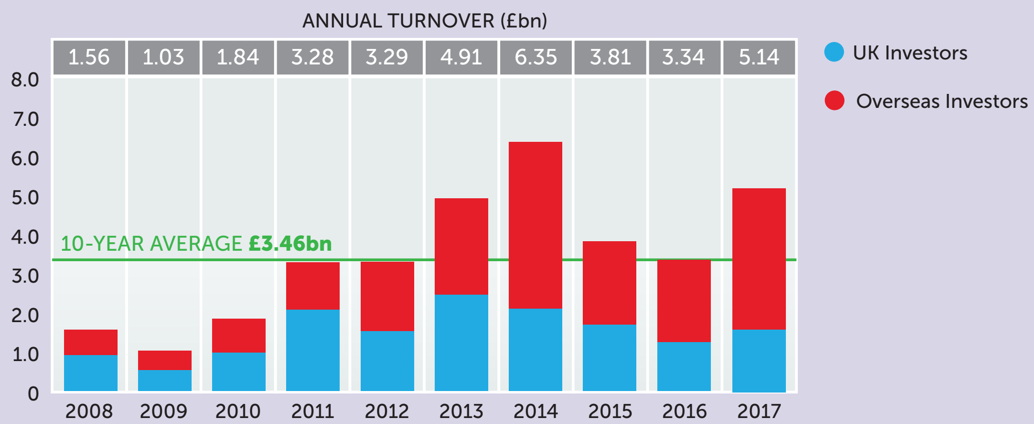
£5.1 BN

change on 2016
+56%
10-year Annual Average
£3.5bn

FIG. 9 **KEY INVESTMENT TRANSACTIONS 2017**

QUARTER	ADDRESS	SIZE (SQ FT)	PURCHASER	RENT (£ PSF)	YIELD (%)	PRICE (£M)
Q1	Whitefriars, 65 Fleet Street, EC4	219,996	JMI Properties	41.00	5.56	160
Q1	Fox Court, 18 Gray's Inn Road, WC1	103,555	Private Israeli	50.86	5.10	101.45
Q1	Rose Court, 2 Southwark Bridge, SE1	157,144	WPP Group	27.65	4.31	94.5
Q1	1 Long Lane, SE1	24,936	Adir Group	VP	0.24	19.5
Q2	Bankside 2 & 3, Southwark Street, SE1	453,904	Deutsche AM	42.00	4.70	385
Q2	Elizabeth House, York Road, SE1	279,494	HB Reavis	N/A	N/A	241
Q2	70 Gray's Inn Road, WC1	34,513	Trinity IM	42.67	4.38	31.5
Q2	36-38 Hatton Garden, EC1	25,226	Orchard Street IM	56.84	4.66	28.8
Q3	Riverside House, Southwark Bridge Road, SE1	171,036	Alduwaliya	39.93	4.5	150
Q3	Lacon London, 84 Theobald's Road, WC1	216,555	Al Ain Properties	59.00	4.5	285
Q3	Aldwych House, 71-91 Aldwych, WC2	174,000	Angela Leong	64.66	4.25	250
Q3	Park Plaza, 6 Hercules Road, SE1	200,000	Adir Group	28.00	3.25	161.5
Q4	200 Aldersgate Street, EC1	445,265	Samsung SRA	38.95	5.22	311
Q4	160 Aldersgate Street, EC1	200,000	Union Investment	52.50	4.73	208
Q4	240 Blackfriars Road, SE1	226,271	Al Gurg Group	49.50	3.94	267
Q4	42 Southwark Bridge Road, SE1	96,714	UBS	42.39	5.07	76

FIG. 10 **ANNUAL INVESTMENT TURNOVER**



Second highest performance over the past decade

Last year saw the first rise in interest rates for 10 years – a nominal increase from 0.25% to 0.5%. We also saw employment rise to 75.3%, the highest since figures began in 1971, equating to an unemployment rate of 4.3%. But wages are well below the rate of inflation, which means that pay is still falling in real terms. This is a challenge for the interest-rate setters at the Bank of England, who tend to view low unemployment as evidence of a buoyant economy, yet we are still waiting for wages to grow in response. There is also an affordability challenge in respect to rising interest rates.

Sterling was weak during 2017 but regained strength at the end of the year, while the General Election dominated the political agenda mid-year but had no significant impact. However, the outcome of Brexit is a source of continuing uncertainty and will affect the markets for the foreseeable future.

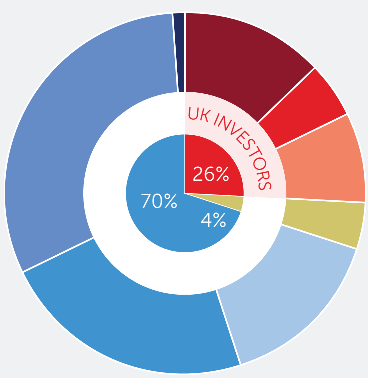
Against this mixed backdrop, London outperformed its European rivals and delivered more than £20bn of transactions compared with £16bn in 2016. Turnover in the Centre of London was £5.14bn, the second highest in 10 years, of which £3.58bn came from overseas. Far East investors contributed 31%, followed by the Middle East with 23%. We also had some European activity, particularly German, which reflects London's pricing advantage when set against some of Germany's key markets.

As expected, UK vendors dominated the market, continuing the theme in recent years for ownership to pass from the UK to overseas. The UK vendors accounted for £3.92bn, led by UK property companies with 41% of sales. The biggest transactions were Southwark Street, SE1 (£385m), bought by Deutsche Asset Management, followed by 200 Aldersgate St, EC1 (£311m), bought by Samsung SRA.

Prime yields are broadly stable year-on-year. The Centre of London achieved 4.25%, the City 4%, and the West End 3.25%. These prime yields reflect the most risk-averse end of the spectrum.

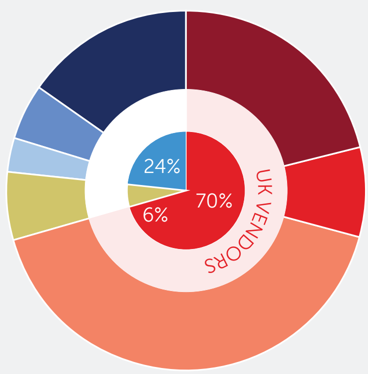
FIG. 11 **INVESTOR & VENDOR BREAKDOWN 2017**

INVESTOR



Investor		Vendor
13%	UK Fund	41%
8%	UK Property Company	21%
5%	UK Private / Other	8%
4%	Owner Occupier	6%
31%	Far Eastern	16%
23%	Middle Eastern	5%
15%	European	3%
1%	Other	0%

VENDOR



OUTLOOK

Despite the economic and political headwinds, the market fundamentals will remain strong with capital inflows from China, Hong Kong and the Middle East continuing to support investment activity across the Centre of London.

RETAIL & LEISURE

Hotel Sector

There was strong growth in this sector during 2017, with approximately 8,500 rooms added across London. The weaker pound boosted tourism and contributed to an average rise in room rates of 5% across the UK. This did, however, result in increased costs for imported goods and services, which had a negative impact on margins.

Looking ahead, there are two principal threats to the sector; the slow-down in economic growth is likely to have a negative impact on domestic spending on hotels, and Brexit may dampen demand for business travel.

Despite these constraints, the outlook for 2018 is optimistic. Growth is expected, if not quite at the level of 2017, with 7,000 new rooms forecast to be added. Institutional investors remain very keen on the sector due to the long-term nature of income derived from hotels, and this combined with scarcity of stock has produced some benchmark yields, 3.25% in one SE1 example.

One major change to the sector in recent years is the competition created by the alternative lodgings sector, driven by the growth of the sharing economy. There are now numerous operators who provide accommodation on a short-term basis for both leisure and business travellers, and the largest and best known is Airbnb. It alone has 4m listings across 191 countries, and London has the third largest number of listings of any city in the world.

The general consensus is that while hotel operators need to improve elements of their businesses, in particular their online platforms, this new sector is unlikely to have any long-term negative impact on hotel viability. Airbnb and their competitors can also have negative impact on the traditional housing market by restricting residential rental supply. This has led to several city authorities, including those in New York, Miami and Barcelona, placing restrictions on operators and imposing minimum stay periods of a month or more. Whether London will follow suit remains to be seen.

ART'OTEL, BATTERSEA POWER STATION

ART'OTEL BATTERSEA POWER STATION ROOFTOP POOL

NEW ADDITIONS

There have been, and will be, some exciting new additions in the Centre of London. Covent Garden, an area with very high demand and low supply will see four new additions, totalling 350 new rooms. Recognised brands The Nadler and Z Hotel will open on Bedford Street and the boutique hotel group behind The Greenwich in New York, partially owned by Robert De Niro, will open on Wellington Street. In addition, conversion of the former Bow Street Magistrates Court is likely to commence bringing new life to a rather quiet corner of the Opera Quarter.

Moving south of the river, a staggering 1,100 new rooms are planned along the northernmost end of Blackfriars Road. The Marriot Autograph at One Blackfriars is due for completion during summer 2018, while The Hoxton, Blackfriars, which will have a bar and restaurant operated by Soho House, is due to open in 2019. In addition to these, there is a 550 bed consent within the proposed 18 Blackfriars Road scheme and a further 275 rooms proposed on the former Lewisham College site.

FIG. 12 **SELECTION OF NEW HOTELS IN CENTRE OF LONDON**

Waterloo Transformation

The South Bank retail market is experiencing a dramatic transformation with more than 1.5m sq ft of new retail and leisure space being delivered from Battersea to Vauxhall, Elephant & Castle to London Bridge, as well as at the northernmost end of Blackfriars Road. Waterloo is a key part of this changing landscape, with over 200,000 sq ft of space coming forward across three current schemes, and what will likely be a significant amount of additional space as part of HB Reavis' plans for Elizabeth House.

Southbank Place will be delivered in late 2018 and will offer 48,000 sq ft of new space. Occupiers already signed up include Boots, M&S, Gail's and Notes, with restaurant operators yet to be announced.

Union Street Partners is involved with two further schemes that are regenerating the area around London's busiest railway station. The first is Leake Street Arches, a 25,000 sq ft scheme in eight former railway arches. It is due to open and begin trading in the summer, and we have curated an independent tenant mix anchored by Lost Rivers who will have a microbrewery, two bars, a restaurant and events space across three of the arches. Alongside will be operators offering cuisine from Vietnam to Poland, cocktails in a space with word-class sound technology and fun and games for all throughout the day.

The second scheme to complete is Waterloo Retail, a 135,000 sq ft retail and leisure scheme planned for the former Waterloo International Terminal. Scheduled for completion in late 2020, the scheme will provide a much-needed major hub for the area. We are shortly to commence formal marketing of the space and we are already in discussion with some very interesting anchor tenants, with an ambition to do something slightly different to the norm.

LEAKE STREET ARCHES, SE1
(25,000 SQ FT OF LEISURE)

SOUTH BANK PLACE, SE1
(48,000 SQ FT OF RETAIL & LEISURE)

WATERLOO RETAIL, SE1
(135,000 SQ FT RETAIL & LEISURE)

ELIZABETH HOUSE, SE1
(10,500 SQ FT RETAIL & LEISURE)

The Restaurant Market

The A3 restaurant market has been very strong in recent years with significant rental growth in most areas. Harden's London Restaurant Guide reported a record high of 246 openings in London in 2017, 40 of which were in the Centre of London. But there was also a downside: 84 restaurants closed in 2017 compared with 76 in 2016.

There is an obvious squeezed middle ground in the sector at present: operators at both the top and value ends of the market are performing well while those sitting in the middle are struggling. This trend is evident in Carluccio's, Strada, Jamie's Italian and Pizza Express, among others, all of whom are looking at ways to restructure and offload leases.

Building on this, a multitude of operators who began with a single, high-end restaurant are now expanding. The investors behind such operators/ concepts prefer a model that can be scaled, because it is difficult to make a single site sufficiently profitable. The trend largely began with The Ivy being rolled out by Caprice Holdings, and it is now looking to do the same with Harry's Dolce Vita. Other examples include Hawksmoor, M, Temper and The Frog.

Food markets have been popular on the London food scene for several years and a number of operators now coordinate the traditional outdoor format. Recently, there has been a shift towards comprehensive, indoor markets: a trend arguably kickstarted by Time Out Market in Lisbon. Having struggled to get consent for a site on Commercial Road, Time Out has been pipped to the post where London is concerned, following the establishment of Market Halls. This growing brand has acquired the former Pacha in Victoria, 10,000 sq ft in Fulham Broadway and a large part of the former BHS on Oxford Street and will be trading each of them as permanent indoor food markets.

The sector will continue to face numerous challenges as we move through 2018. The weaker pound has led to a rise in the cost of imported goods and Brexit has placed a particular strain on operators' ability to recruit and retain staff – the sector being reliant on EU nationals, many of whom are now relocating. Added to this are the rise in staffing costs, following the introduction of the living wage, and increased occupational costs.

Despite these challenges, London has a population of 9m residents and received record numbers of visitors last year, meaning the fundamentals for successful trading remain strong. Landlords need to think carefully about delivering the right space in the right place and be alert to the fact that incentives are on the rise, particularly for shell units where the initial capital required to fit out can be problematic for operators and their investors.

THE IVY, 1-5 WEST STREET, LONDON, WC2H 9NQ

RETAIL & LEISURE TRANSACTIONS

KEY TRANSACTIONS 2017

Q1 17

113 WATERLOO ROAD, SE1

Dough Bro
Size: 1,568 sq ft
Type: New Lease
Rent: £150,000 pa
(£95.65 per sq ft)

52 LAMB'S CONDUIT STREET, WC1

La Fromargerie
Size: 1,171 sq ft
Type: New Lease
Rent: £60,000 pa
(£115 per sq ft Zone A)

Q2 17

74 CHANCERY LANE, WC1

Bill's - assigned to Freshii
Size: 3,125 sq ft
Type: New Lease
Rent: £160,000 pa
(£84.00 per sq ft headline)

111 WATERLOO ROAD, SE1

Tonight Josephine
Size: 1,436 sq ft
Type: New Lease
Rent: £145,000 pa
(£101.00 per sq ft)

Q3 17

UNITS 4/5A SOUTH BANK CENTRAL, SE1

Black Sheep Coffee
Size: 1,696 sq ft
Type: New Lease
Rent: £75,000 pa
(£45.00 per sq ft)

UNIT 1 CHICHESTER RENTS, WC2

Urban Fitness
Size: 5,436 sq ft
Type: D2 use
Rent: £190,000 pa
(£35.00 per sq ft)

Q4 17

148 FLEET STREET, EC4

Grabthai
Size: 721 sq ft
Type: New Lease
Rent: £75,000 pa
(£246 per sq ft Zone A)

ARCH 7, LEAKE STREET ARCHES, SE1

Aures
Size: 1,620 sq ft
Type: New Lease
Rent: £68,000 pa
(£42.00 per sq ft)

OUTLOOK

Press negativity surrounding 'retail' is commonplace, particularly in light of a spate of recent failures, CVAs and profit warnings. Our view is that the headlines offer a simplistic picture of a market which is varied and complex, and company-specific factors are often overlooked in favour of a narrative that spells Armageddon for the retailing sector.

There is no doubt that the market has changed during 2017. Inflation has restricted household spending, affecting sales in many parts of the sector, and the ongoing political uncertainty surrounding Brexit has certainly impacted retailer confidence, with changing hurdle rates and more stringent decision-making across the board.

The Centre of London is faring well, however, and we are seeing continuing occupational demand for a wide range of use classes. Putting space on the market and waiting for interest is a marketing strategy of the past. Well-thought-through, targeted campaigns are the best way to see good results in this market and that is how we continue to operate. Here is a selection of trends we see developing and continuing through 2018:

RETAILER PORTFOLIO 'RIGHT-SIZING'

Nationally speaking, there is too much space in the wrong locations. The Centre of London is a slightly different beast but a reasonable level of secondary stock and over saturation of certain uses will mean we will see the effects of retailers looking to offload leases to rationalise their portfolios. A1 and A3 food, banks and large fashion outlets and department stores will probably be the most visible examples. We tend to view this is an opportunity rather than a threat, as it leaves space for change and new entrants to the market.

COMPETITION FOR COMPETITIVE SOCIALISING

Drinking and eating are no longer enough, it would seem. The trend of bar/restaurant concepts built around some form of competitive activity took hold during 2017 and we expect to see this continue. There are numerous examples where traditional concepts such as darts, bowling, miniature golf and table tennis are being reinvented. A more novel trend is escape rooms and even axe throwing.

'CLICKS TO BRICKS' GATHERING MOMENTUM

All retailers are aware of the importance of being 'omnichannel' and the UK has a relatively mature online retail market, evidenced by the slowing growth in online sales. A variety of sources predict that online sales will account for between 18% and 20% of total retail spend by 2022, which leaves a substantial remainder for traditional bricks and mortar – albeit they are more and more mutually dependent. A small number of solely online retailers are now making the move to physical stores and we expect this trend to gain momentum, demonstrating the importance of physical stores for showcasing brands and products. Many markets within the Centre of London offer the perfect environment for this transformation.

LONDONERS GET LEANER, RENTS GET KEENER

No change here from our 2017 predictions; demand from the D2 health and fitness sector remains strong and supply is still fairly limited. Rents boomed through 2016 and we saw growth level off through 2017 as many operators struggled to get to the newly set tone. In our view, this year will see slightly more sustainable growth with a good selection of both quality and value brands actively looking for space.

HOUSE VIEW

LEASING MARKET

With the market remaining uncertain as Brexit continues to unfold, 2018 is likely to be a year of mixed fortunes. Confidence was strong last year, and we expect the same in 2018, but leasing volumes will probably fall below 2017 levels. This year will see the highest number developments completed for a decade, which is a positive for the market but, with robust demand for new and refurbished space, we do not anticipate a significant spike in the Centre of London supply by the end of 2018.

The Centre of London will be at the heart of the changing transport network in 2018. The Elizabeth Line will open in stages during 2018, with the entire line due to be in operation by December 2019. The new transport network will make London more accessible, reducing journey times from Heathrow Airport and other key destinations, and will in turn have a positive effect on the occupier market in the Centre of London.

The serviced offices market is stimulating new ways of working in the Centre of London, and a more collaborative and flexible approach to workspace is developing that is attractive to many occupiers. The growth of serviced offices will not only impact leasing market dynamics and take-up and supply trends, it will also affect landlords' leasing strategies. We have already seen some landlords developing ways to offer flexible space, such as British Land launching Storey, a new brand providing flexible workspace. This is a key trend to watch in 2018.

INVESTMENT MARKET

Looking at the year ahead, the macro political and economic environment will test investors, and investment volumes in London might shrink by 15-20%. This should not be perceived as a negative, since the markets have been trading at a high watermark for a number of quarters.

The depth and diversity of capital remains resilient and, for certain sectors, it is competitive against the background of an uncertain world. This makes for more challenging decisions. As such, price realisation will become more unpredictable. However, the Centre of London will retain its investment appeal due to its strong market fundamentals and strategic opportunities.

RETAIL & LEISURE

The market faced several challenges in 2017, such as higher inflation and Brexit uncertainty, but still fared well. Retail and leisure operators are now more focused on delivering high-quality space throughout the Centre of London. This comes against a backdrop of sector negativity due to retail failures and profit warnings, but because the sector is complex and trading situations vary, it is important not to oversimplify this varied market.

Inflation has placed pressure on household spending, but this is expected to moderate and thus boost purchasing power and retail spending. Because Brexit has shaken retailer confidence, hurdle rates have changed and decision-making is taking longer. As a result, some deals are foundering. Although this is likely to continue, retailer confidence will improve in parallel with increased consumer spending, while the Centre of London's distinctive character will always appeal to those in the retail & leisure sector.

DEFINITIONS

Centre of London - Midtown comprising WC1, WC2, EC1 (West of Goswell Street), and EC4 (West of Aldersgate Street and New Change) & South Bank including SE1, SE11, SE17, and SW8

Stock - office accommodation, excluding offices under construction

Floorspace - net internal area, unless otherwise stated

Availability - office space available for immediate occupation

Availability Rate - available offices as a proportion of total stock

Take-up - completed transactions where offices are let or sold to an occupier

New - brand new buildings or buildings developed behind a retained façade

Refurbished - buildings which have undergone a major refurbishment

Secondhand Grade A - previously occupied higher quality space with features such as air-conditioning or raised floors

Secondhand Grade B - previously occupied lower quality space with features such as central heating or perimeter trunking

Construction start - development where the main contract has commenced, normally excluding demolition or stripping out

Construction completion – development where the main contract has reached practical completion

Hidden Supply - space which is not currently on the open market, but likely to come available in the near future

DAMIT - Design; Advertising, Marketing & PR; Media, Internet; and Technology & Telecoms

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