23 Savile Row, W1

- **Availability falls by 5% to 525,700m²**
- **Vacancy rate down by 30 basis points to 7.1%**
- **Quarterly take-up totals 49,100m² bringing the total for the year-to-date to 109,650m²**
- **Prime rent bottoms out at £699.50m² (£65ft²) with 24 months rent-free**
- **£835 million invested in Q3 2009**
- **Rental growth on the horizon**

West End Contacts:
30 Warwick Street, London W1B 5NH. T: 020 7493 4933

Research
Catherine Jones catherine.jones@kingsturge.com

Agency
Chris Watkin chris.watkin@kingsturge.com
Andrew Barnes andrew.barnes@kingsturge.com
Joe Fuller joe.fuller@kingsturge.com

Lease Consultancy
Nicholas Smith nicholas.smith@kingsturge.com

Investment
Simon Beckett simon.beckett@kingsturge.com
Nick Deane nick.deane@kingsturge.com
James Maclachlan james.maclachlan@kingsturge.com

Land ahoy!

There were reasons to feel more positive about the West End office market at the end of Q3 and looking forward there is certainly light at the end of the tunnel.

In spite of a healthy increase in the number of deals in Q3, we are still on track for one of the worst years of take-up on record with just 109,650m² (1.2 million ft²) of lettings to date - due to poor Q1 and Q2 figures - against a 25-year annual average of 363,000m² (3.9 million ft²). The volume of activity in Q3 suggests that demand has begun a sustained return, with availability decreasing for the first time since Q2 2007. It is unclear, however, how much of space currently under offer will translate into take-up before the year end.

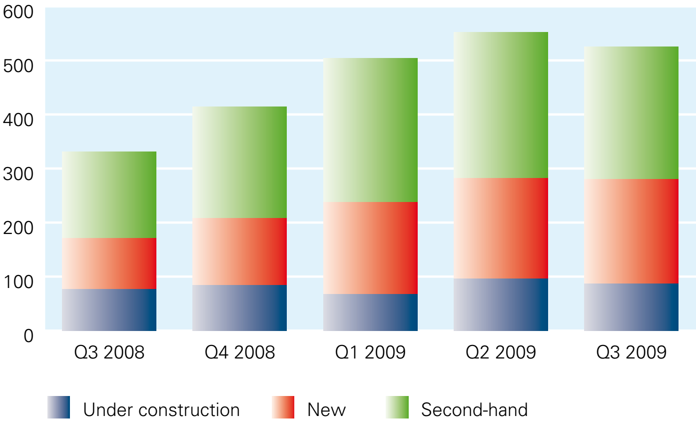
Added confidence can be taken from active requirements increasing by 19% at the beginning of the autumn. With a limited development pipeline, especially in Mayfair and St James's, it seems that rental growth may be seen earlier than predicted, assuming the economic recovery remains on track. With rents and incentives finally hitting the bottom, tenants are becoming aware that the next few months may be the cheapest time to move before the next upwards cycle.

The investment market also had its best quarter of 2009 so far, seeing 23 deals signed and £835 million invested. Sentiment remains cautious, however, given that a year ago a positive Q3 preceded a dismal end of year.

Looking forward, however, we expect a greater level of demand from UK Institutions and property companies to drive cap rates lower, as most now seem to be cash positive and in a position to start buying again. The returning confidence in agency markets is expected to further fuel investment demand. With quality stock in short supply, we expect values to rise quite steeply over the short to medium term for prime, and perhaps latterly in Q4 for more secondary product as well.

Supply

Availability (000m²)



Availability falls to 525,700m²

There is currently 525,700m² (5.7 million ft²) of available accommodation in 286 units in the West End, which represents a decrease of 5% on the previous quarter but a 59% increase over the last 12 months. Like the City market, the West End office market also experienced a fall in supply for the first time in two years, through a combination of lettings, under offers and withdrawals.

Vacancy rate at 7.1%

This level of supply equates to a vacancy rate of 7.1% which represents a 30 basis point decrease over the last three months.

Slight fall but still above average

Despite this quarter's slight fall in availability, this level still remains above the long-term supply average (382,000m² / 4.1 million ft²) and is equivalent to 1.5 years worth of long-term annual take-up (1984-2008). Mayfair and St James's, however, will soon start to see selective shortages of space. A large proportion of Grade A stock is located in Covent Garden, Euston and Paddington sub-markets and is all at similar rental levels.

All grades of space available

Current supply is evenly spread between Grade A (new and refurbished space including those development schemes six months off completion) and second-hand accommodation. And while there was evidence of tenants off-loading surplus space, the levels were not as high as first anticipated with 38% of total availability being offered by tenants rather than landlords.

Key New Availables (End-Q3 2009)

- 2 Kingdom Street, W2 (17,351m² / 186,766ft²). Under construction and due to complete Q1 2010 (part under offer),
- Trafalgar Place, 2-4 Cockspur Street, SW1 (8,888m² / 95,670ft²). Second-hand accommodation.
- 82-83 Piccadilly, W1 (6,918m² / 74,470ft²). Second-hand accommodation.

Spike in development completions

Development projections show there is 108,850m² (1.2 million ft²) of speculative space due to complete during 2010. As a result there will be a concentration of Grade A supply (97,100m² / 1 million ft²) in two West End sub-markets – Covent Garden and Paddington. In fact, 56% of this new supply falls into just three schemes currently on site:

- Central St Giles, 1-13 St Giles High Street, WC2 (35,557m² / 382,736ft²). Under construction and due to complete Q2 2010. Fully available.
- 2 Kingdom Street, W2 (21,936m² / 236,119ft²). Under construction and due to complete Q1 2010. Part pre-let to Astra Zeneca.
- Crown House, Aldwych, WC2 (12,431m² / 133,807ft²). Under construction and due to complete Q2 2010. Fully available.

Looking ahead…

While there has been a respite in the rise of supply this quarter, it is forecast to rise again in Q4 as some of the key development schemes mentioned above feed into availability by the year-end. However, from 2010 onwards, West End supply is set to fall back towards the long-term average against an outlook of returning demand and stabilising rents.

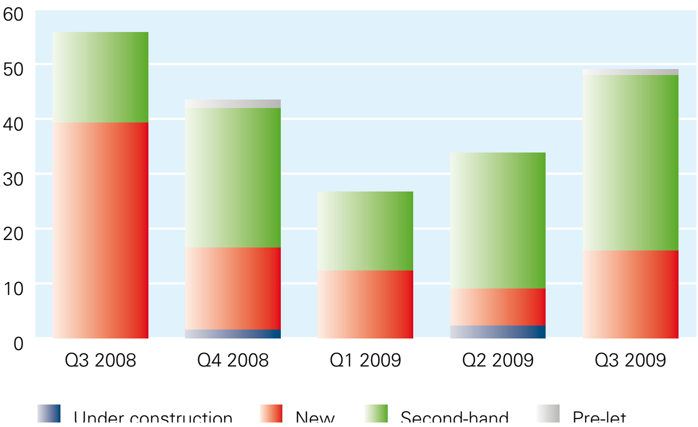
The development pipeline looks increasingly tight for 2011-2012, with many developers previously having 'put the brakes' on a number of development schemes in the West End. There will be a shortage of new supply, especially in the Core sub-markets, from as early as 2011 which is likely to help to push prime rents upwards again.

West End availability

000m²	Q2 2009	Q3 2009	Year ago
New / Refurbished	185.9	193.7	94.2
Second-hand	270.2	245.5	160.4
Available U/C	96.5	86.6	76.6
Planning permission	391.1	396.6	373.6
Completions	23.8	43.1	12.5

Demand

Take-up (000m²)



49,050m² let in Q3 2009

Following two quarters of historically low levels of take-up, there was a marked improvement this quarter as occupier demand returned. Letting activity in Q3 totalled 49,050m² (528,200ft²) in 49 units, which represents a 45% increase quarter-on-quarter.

Returning demand

This level of activity is almost double that seen in the first quarter of the year, as potential occupiers appear to be active once again, buoyed by increasing business confidence and stability. This sentiment is further echoed by a 19% rise in the number of current West End office requirements (2.98 million ft²) – which are sourced from a diverse group of business sectors including the Financial, Technology, Media & Telecommunications (TMT), Association, Professional and Service sectors.

Financials are back

A strength of the West End office market has always been the diversity of occupiers that have located here and this is reflected not only in active requirements but also letting activity.

Surprisingly, the most active group so far this year has been the Financials accounting for 19% of take-up in 24 deals. The next most active sector were the TMTs (18%), with 'new media' companies leading the way.

Most deals signed under £538m² (£50ft²) but 'froth' returns
An analysis of take-up by rent-band (based on the headline rent achieved) shows that the majority of deals (66%) were signed at £538m² (£50ft²) or under. Just five (out of a total of 95) deals over 500m² (5,382ft²) signed in excess of £872m² (£81ft²). Some of these "froth deals" are outlined below and are an encouraging sign of potential prime rental growth moving forwards. Further similar deals are expected in Q4.

Key lettings (Q3 2009)

- EDF Energy assigned 3,449m² (37,124ft²) of second-hand accommodation from IPG on the part 5th (E) floor at 80 Victoria Street, SW1, at a reported passing rent of £592m² (£55ft²), on a lease expiring in December 2021. This is the second largest deal of the year.
- Altima Advisors assigned 824m² (8,869ft²) of new accommodation from Fox-Davies Capital on the 6th floor of 23 Savile Row, W1, at a reported rent of £1,001m² (£93ft²), on a lease expiring in June 2019 with 12 months rent-free.
- Resolution Asset Management took 978m² (10,527ft²) of new accommodation on the 5th floor of 23 Savile Row, W1, at a reported rent of £979.50m² (£91ft²), on a lease expiring in September 2020 with 15 months rent-free.

Looking ahead...

This quarter's total brings the total for the year-to-date to 109,650m² (1.2 million ft²) which is 46% lower than the same nine-month period last year (202,550m² / 2.2 million ft²). Despite improvements this quarter, the projected year-end total of 167,000m² (1.8 million ft²) means that 2009 is still on track to be one of the worst on record (1984-2008).

However, as demand continues to improve, annual take-up will rise back towards the long-term trend (annual average of 382,000m² / 3.9 million ft²) from 2010 onwards.

West End take-up

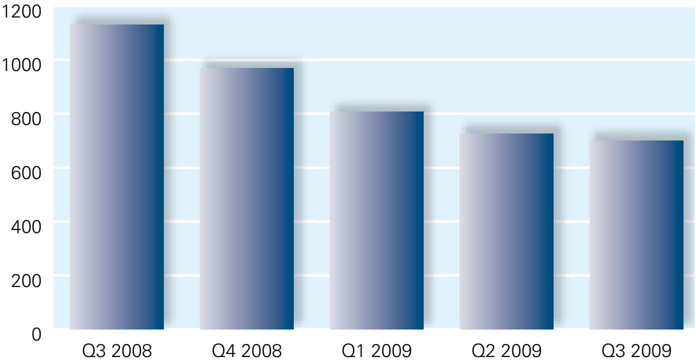
000m²	Q2 2009	Q3 2009	Year ago
New / Refurbished	6.8	16.0	39.3
Second-hand	24.8	32.0	16.6
Under construction	2.3	0.0	0.0
Pre-let	0.0	1.1	0.0
Under offer	27.4	68.4	29.9

West End Offices

King Sturge

Rents

Prime rent (£m²)



Prime rent bottoms out at £699.50m² (£65ft²)

The King Sturge West End prime rent fell from £726.50m² (£67.50ft²) to £699.50m² (£65ft²), a fall of 4% over the quarter and 42% since the peak rent of 1,211m² (112.50ft²) in Q1 2008. Incentives have also now levelled at 24 months for a ten-year lease.

Looking ahead

Despite a number of headline deals at 23 Savile Row, W1, signing in excess of £915m² (£85ft²), more generally rents have levelled off. As a result the West End prime rent will stay at its current level for the remainder of this year though is it not expected to fall any further and prime rental growth will be on the horizon quicker than expected.

Rental value growth – IPD monthly data

IPD monthly data for September 2009 shows RVG for West End & Midtown offices over Q3 2009 to be -3.3%. Over the last nine months (Q1-Q3) RVG was -19.0%. This equates to an annualised figure of -24.5%.

Resilient reversions

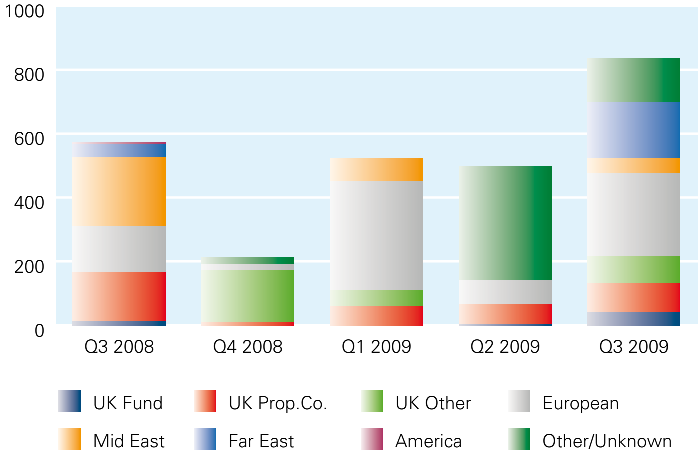
Rent review agreements remain difficult to conclude in some instances due to the range of evidence available and lack of open market letting agreements.

Reversions remain achievable with historic rental levels from 2004 at relatively low levels, although not in all cases.

As activity returns to the letting market, a clearer picture will be provided to assess rental levels for future rent review and lease renewal agreements.

Investment

Investment (£m)



£835 million invested in Q3 2009

There was a significant rise in investment activity during Q3, as £835 million transacted in 23 deals. This represents a 68% increase on the previous quarter and brings the total for the year-to-date to £1.9 billion. Most investors this year have been from overseas (76% of the total) including Azerbaijan, Libya and South Africa.

Return of UK investors is nigh?

The market continues to be dominated by private overseas money (strengthened by weak sterling) although evidence is now emerging of rapidly increasing domestic demand for Central London offices - British Land & GPE have both completed acquisitions and as a result, we expect UK institutions to return to the London market during Q4.

With a dearth of suitable investment product and excessive demand, pricing for most assets continued to harden during Q3. Demand seems to be focussed on the Core locations and lease length is now viewed as less important. However, medium to long-term income streams in Core buildings will create very competitive pricing, an example of which is Quadrant House, Pall Mall, SW1 - a Grade B building which is considered rack-rented and is currently under offer at a price reflecting a sub-5% initial yield. Non-Core locations and secondary properties are more difficult to sell but, because of limited availability and an increasing pressure to spend, we expect this stock to continue to increase in value over the short-term.

Key deal (Q3 2009)

- Windsor House, 50 Victoria Street, SW1 – Freehold - £115 million – 5.70% initial yield - London & Oriental (purchaser).