RESEARCH

Q1 2009

CENTRAL LONDON

Quarterly

Knight Frank

HIGHLIGHTS

- Sentiment in the occupational market remained subdued in Q1 2009 with just 1.3 m sq ft of take-up across Central London, 70% below the long-term average level.
- The delivery of new space and the continued release of tenant space to the market resulted in a 23% quarter-on-quarter increase in availability, which now totals 22.3 m sq ft. This is the largest single-quarter increase since 2001.
- Occupier caution and increased supply continued to place rents under pressure across all markets.
- Investment turnover fell to £626 m, its lowest level for 7 years, as the continued lack of available debt restricted market activity.

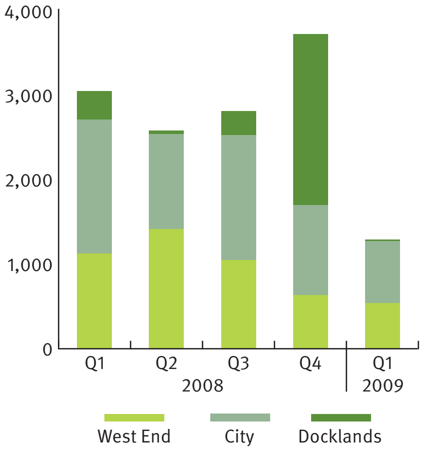
CENTRAL LONDON OVERVIEW

- **Take-up fell by 65% to 1.3 m sq ft, one of the lowest quarterly levels on record.**
- **Availability increased as speculative schemes completed and tenants continued to release space. The vacancy rates is now 10.0%.**
- **Speculative construction activity continued to fall to 6.2 m sq ft, 35% lower than last year, with only one construction start during the quarter.**
- **Investment turnover fell to £626 m, the lowest for 7 years and a 70% drop on the previous quarter.**

Figure 1

Central London take-up by quarter & market sub-area

Q1 2008 - Q1 2009 (000's sq ft)

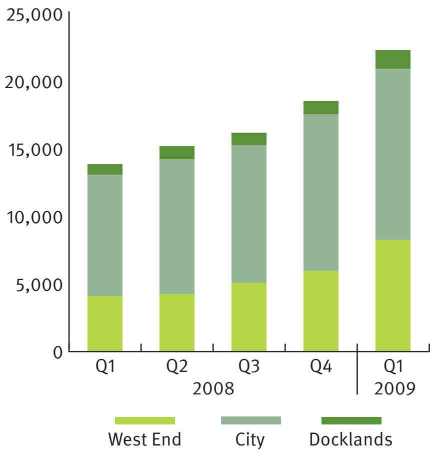


Source: Knight Frank

Figure 2

Central London availability by quarter & market sub-area

Q1 2008 - Q1 2009 (000's sq ft)



Source: Knight Frank

Demand and take-up

The global economic crisis continued to place pressure on occupier activity in the first quarter as take-up dropped to 1.3 m sq ft, a 65% fall on the previous quarter's level and one of the lowest quarterly levels on record. There were just 343,000 sq ft of transactions involving new and refurbished space, 80% below the long-term average, with only two deals in excess of 50,000 sq ft across the whole market. Also significant was the fall in transaction volumes involving second-hand space, which totalled just 950,000 sq ft, 36% lower than the previous quarter and 44% below the long-term average of 1.7 m sq ft.

Active demand levels fell across Central London as a number of requirements were placed on hold or withdrawn. There are now 6.2 m sq ft of active named requirements in Central London, 31% below the level witnessed 12 months ago.

Supply and development

Availability across Central London rose for the sixth consecutive quarter as more speculative schemes joined supply and tenants released space in a bid to trim costs. At the end of Q1 2009 availability totalled 22.3 m sq ft, which represents a vacancy rate of 10.0%. This indicates an increase of more than 60% over the last 12 months, although this is still considerably lower than the 36.3 m q ft reached in 1991.

Importantly, the level of speculative construction activity has fallen away considerably over the last 12 months as funding remains difficult to secure and the uncertainty in the occupational market continues. The only major scheme to start in Q1 2009 was The Shard, SE1 which is due for completion in 2012 and is pre-let in part to Transport for London.

Investment market

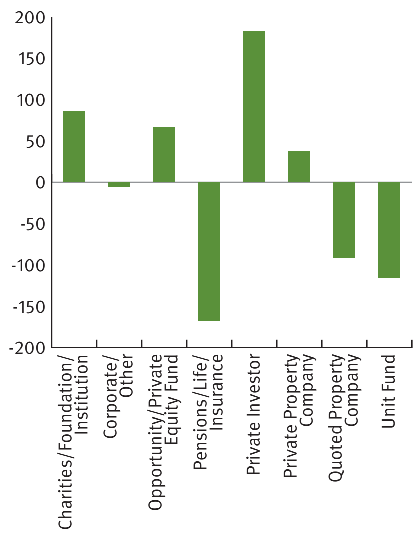
Investment turnover fell to £626 m in Q1 2009, 60% below the long-term average and 70% less than the previous quarter's level. The continuing lack of debt availability was apparent, with private investors accounting for almost 40% of total purchases across Central London. Despite the muted level of activity, there are positive signs that market sentiment is beginning to change, with Central London representing a potential opportunity to foreign investors looking to exploit the weak Pound.

The outward shift of prime yields appears to have stabilised, with yields in the City remaining at 6.75%. In the West End, prime yields softened to 6.00% although further outward movement is considered unlikely.

Figure 3

Central London net investment

Q1 2009 (£ m's)

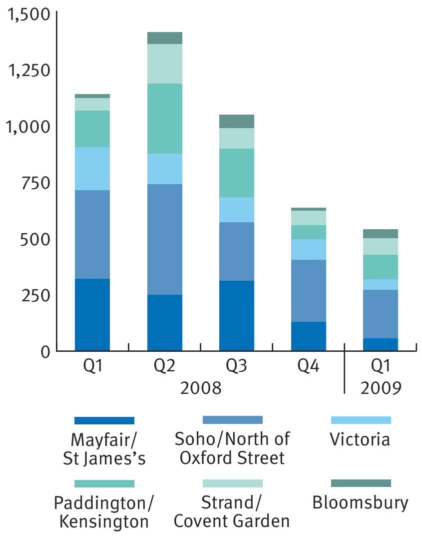


Source: Knight Frank

WEST END

- **Take-up was 0.54 m sq ft, 15% lower than the previous quarter.**
- **Active demand totalled 0.8 m sq ft, 66% below the same quarter last year.**
- **Vacancy rate now stands at 9.2% with availability increasing to 8.3 m sq ft.**
- **Prime headline rents have fallen by 19% to £75.00 per sq ft from £92.50 per sq ft at the end of 2008.**

Figure 1
West End take-up by quarter & market sub-area
Q1 2008 - Q1 2009 (000's sq ft)



Source: Knight Frank

Demand & take up

Take-up in Q1 2009 totalled 543,000 sq ft, the lowest quarterly total for at least 17 years and 57% below the long-term average of 1.3 m sq ft. Particularly notable is the fall in the level of transactions involving second-hand space. There were around 330,000 sq ft of second-hand space deals across the West End in Q1 2009 compared to 550,000 sq ft in Q4 2008 and a long-term quarterly average of 800,000 sq ft.

Active demand in quarter 1 fell over 17% to 820,000 sq ft as many occupiers have put their searches on hold. Significant requirements include occupiers such as Omnicom, Bovis Lend Lease and Red Bull all of whom will all be displaced by Crossrail. These three requirements accounted for 28% of the total active demand in the West End.

Supply & development

Availability rose for the seventh consecutive quarter to 8.3 m sq ft, a 39% increase on the previous quarter's level and 14% higher than the long-term quarterly average. This represents a vacancy rate of 9.2%, similar to the levels seen in early 2005, but still well below the 12.4% reached in 1992. Over 400,000 sq ft of this increase is due to the inclusion of British Land's Regent's Place in our figures, which is due for completion within the next six months.

The volume of space under construction speculatively fell by 24% to 1.9 m sq ft in the first quarter as a lack of funding and concerns over the occupational market led to developers placing schemes on hold where possible. A significant amount of short-term space came to the market as some landlords and developers are now seeking income prior to economic recovery.

Rental profile

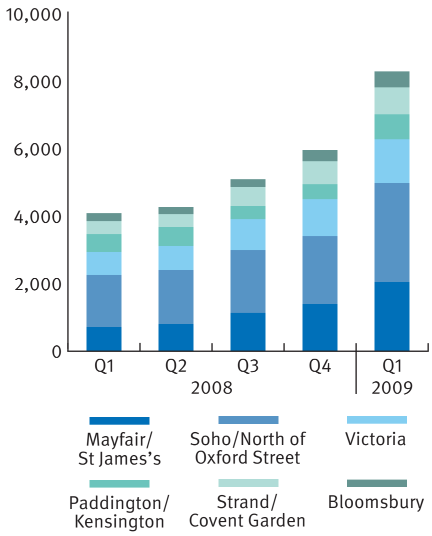
Prime headline rents in the West End continued to fall in Q1 2009 and are now £75.00 per sq ft, a 19% fall from the previous quarter's level and a 32% fall over the last 12 months. Rent free periods are now estimated to be 12 months for each 5-year of term certain.

Investment market

Turnover for the first quarter of 2009 totalled £263 m, 65% lower than the previous quarters figure of £760 m. There is £1.265 bn of investment stock currently available, of which approximately £500 million (40%) is under offer, with the American Embassy accounting for approximately 40%. The largest transaction in Q1 was Times Place, SW1 which exchanged for £56m, reflecting a NIY of 7.64%.

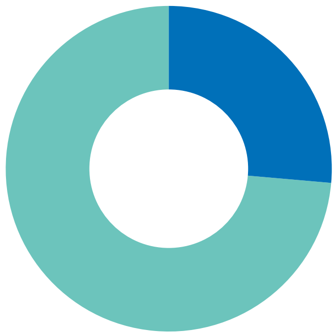
Private UK and overseas investors have continued to dominate the Core West End market, accounting for 70% of purchases, with Sterling looking good relative value. The threat of tenant default and the associated effect on performance is leading to a heavy discount on assets with higher risk tenants. Long-term secure income therefore continues to attract a premium. Prime yields have moved out by 25 basis points and are now at 6.00%, although there are signs that market sentiment is beginning to turn more positive.

Figure 2
West End availability by quarter & market sub-area
Q1 2008 - Q1 2009 (000's sq ft)



Source: Knight Frank

Figure 3
West End investment by purchaser
Q1 2009 (£ m's)



Pension/Life/Insurance	£67 m
Private Investor	£186 m

Source: Knight Frank

CITY

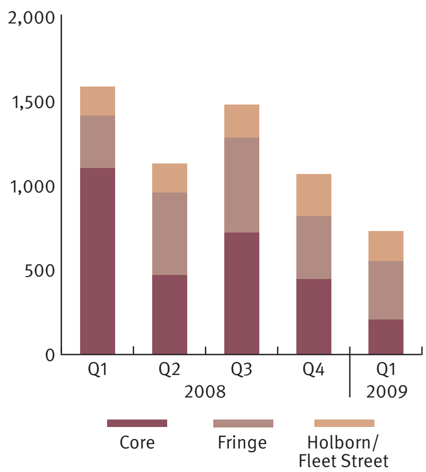
- **Take-up fell to 733,000 sq ft, the lowest level since Q4 2002.**
- **Availability increased to 12.6 m sq ft as upcoming developments approach completion.**
- **Prime City rent was £46.50 per sq ft, compared to £53.50 per sq ft three months earlier.**
- **Prime yields stabilised at 6.75% as investment market confidence improved.**

Demand and take-up

City take-up declined to 733,000 sq ft, which is significantly lower than the Q4 08 figure of 1.1 m sq ft and the long-term average figure of 1.7 m sq ft. Typically there is a six month time lag on developments in the economy reaching the office market, and therefore it is no surprise that following the US bank collapses in Q3 08 we have subsequently seen low take-up in Q1 09.

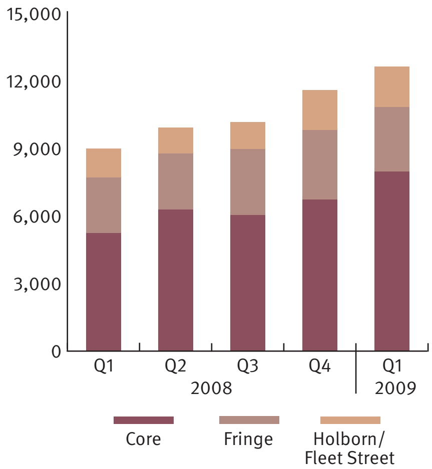
Since quarter-end we have seen the Mitsubishi-UFJ deals at British Land's Ropemaker (where 180,000 sq ft was acquired), which offers a boost for market confidence. There have in recent weeks been encouraging trading statements from the banking industry, and from Lloyd's insurance companies. We also note the introduction of quantitative easing, and changes to mark-to-market accounting rules in America. These developments have potential to ease pressures on the financial sector. This does create the possibility of a recovery in demand in the medium-term.

Figure 1
City take-up by quarter & market sub-area
Q1 2008 - Q1 2009 (000's sq ft)



Source: Knight Frank

Figure 2
City availability by quarter & market sub-area
Q1 2008 - Q1 2009 (000's sq ft)



Source: Knight Frank

Supply and development

Availability in the City rose for a sixth consecutive quarter to 12.6 m sq ft, and as with previous quarters this is largely due to speculative developments approaching completion. The increase in availability has been greatest in the City Core, particular for new and refurbished space.

On a more positive note, the development pipeline has dropped off sharply – 4.4 m sq ft of speculative space is under construction, down from 6.5 m sq ft twelve months ago. This will ease pressures on availability from 2011 onwards.

Rental profile

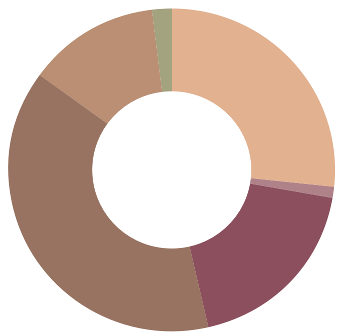
The prime City rent declined further to £46.50 per sq ft at the end of Q1, down from £53.50 per sq ft three months earlier. We expect the prime rent to remain under pressure for the rest of this year.

Investment market

Despite a disappointing first quarter investment transaction volume (£364 m, down from £457 m the previous quarter), confidence appears to have picked up in the City office investment market. We have left our prime yield figure unchanged at 6.75%, given a growing view in the market that yields peaked mid-quarter at 7% then hardened in March. Key factors behind the rally are foreign investors moving to take advantage of Sterling's weakness, and the attractive level of yields. A lack of sellers of prime stock is also an issue.

This is encouraging but must be viewed with due caution. A freer flow of credit will be a necessary prerequisite for an enduring stabilisation of the market. Concerns over the outlook for the occupier market continue to restrain domestic investor appetite, and there is a widening gap between the prime and secondary investment pricing. However, the case for investing in genuinely prime stock is strengthening, given the historically high yields and low comparative capital values.

Figure 3
City investment by purchaser
Q1 2009 (£ m's)



Charities/Foundation/Institution	£98 m
Corporate/Other	£4 m
Opportunity Fund	£68 m
Pension/Life/Insurance	£141 m
Private Investor	£47 m
Private Property Company	£7 m

Source: Knight Frank

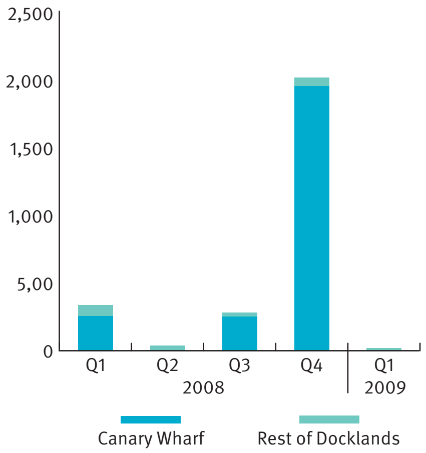
DOCKLANDS

- **Take-up was 19,000 sq ft, with no activity in Q1 at Canary Wharf.**
- **Availability increased to 1.4 m sq ft as upcoming developments joined supply.**
- **HSBC is considering the sale of its 8 Canada Square headquarters.**

Figure 1

Docklands take-up by quarter & market sub-area

Q1 2008 - Q1 2009 (000's sq ft)



Source: Knight Frank

Demand & take up

First quarter take-up for Docklands was 19,000 sq ft. Of particular significance was the absence of any deals at Canary Wharf, and no transactions of over 10,000 sq ft. While take-up figures for Docklands are volatile, this is a remarkably low level of activity. The largest deal of the quarter was a 7,000 sq ft letting to specialist publishing company, Thomas Telford Ltd, at 40 Marsh Wall.

Quarter two should see some recovery in activity with two medium-sized deals under offer at Canary Wharf. Mastercard are under offer on 40,000 sq ft at 10 Upper Bank Street on a sub-let from Clifford Chance. Also, the Olympic Security Service are under offer on c20,000 sq ft in 1 Churchill Place on a sub-let from Barclays. The interest from Mastercard is a positive development demonstrating that Canary Wharf is still attracting tenants from the City, and beyond the investment banking and broking industries. Nevertheless, activity in Docklands is expected to remain subdued in the near- to medium-term.

Supply & development

Docklands availability increased by 44% to 1.4 m sq ft at the end of Q1 09, compared to 957,000 sq ft three months earlier. The inclusion of two new developments in the figures as they approached completion mostly accounted for the increase. Added to availability in quarter one was 5 Churchill Place, where 264,000 sq ft is on the market for assignment from JPMorgan Chase and 52,000 sq ft from Canary Wharf Group. Also included was the 198,000 sq ft that Fimalac is planning to sub-let at 30 North Colonnade.

During quarter one it was announced that Morgan Stanley agreed with Canary Wharf Group an early exit from floors 347,000 sq ft at 20 Cabot Square. This space will be vacant by September 2009, but will likely require extensive refurbishment given the age of the building. The prospect of Bank of America exiting 5 Canada Square, where they occupy 350,000 sq ft, has been widely discussed in the market although no formal announcement has yet been made. Likewise, there has been much discussion on how much space will be released by the receivers to Lehman Brothers at 25 Bank Street, though there has still been no official announcement.

Rental profile

Prime headline rents in Canary Wharf are difficult to measure in the current economic climate. We estimate they had declined to circa £37.00 per sq ft by the end of the first quarter. Outside Canary Wharf we estimate the prime rent to be £27.50 per sq ft. Given the difficult occupier market conditions, and high exposure of the market to global investment banking, rents will remain under pressure for the rest of the year.

Investment

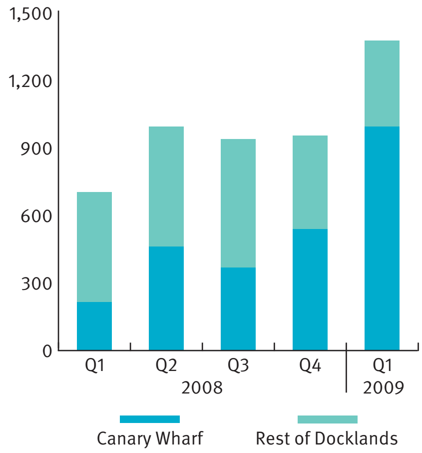
There were no investment deals in the Docklands in quarter one, however the Northern & Shell Tower on Selsdon Way is under offer. RREEF, the current long leaseholder was quoting £9.55 m, reflecting a yield of 9.0%. Express Newspapers hold a lease for a further 13.5 years paying a rent of less than £17 per sq ft.

HSBC has also confirmed it is considering selling 8 Canada Square, a building it purchased back from Metrovacesa late last year.

Figure 2

Docklands availability by quarter & market sub-area

Q1 2008 - Q1 2009 (000's sq ft)

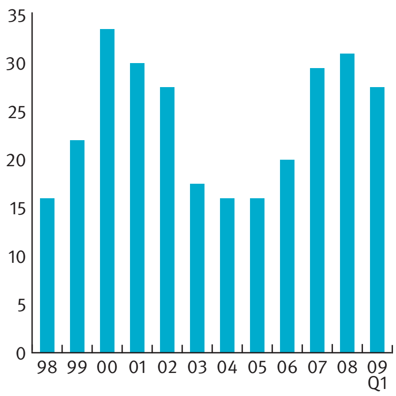


Source: Knight Frank

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)	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	3 months % change	12 months % change
West End	4.07	4.29	5.09	5.97	**8.29**	38.9%	103.8%
City	9.01	9.94	10.19	11.28	**12.65**	12.1%	40.3%
Docklands	0.71	1.00	0.94	0.96	**1.38**	43.9%	95.4%
Central London	13.79	15.22	16.22	18.21	**22.32**	22.5%	61.9%

Vacancy Rate (%)	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	3 months % change	12 months % change
West End	4.5	4.8	5.7	6.7	**9.2**	n/a	n/a
City	7.9	8.8	9.0	9.9	**11.0**	n/a	n/a
Docklands	3.5	5.0	4.7	4.8	**6.8**	n/a	n/a
Central London	6.2	6.8	7.3	8.2	**10.0**	n/a	n/a

Take-up (m sq ft)	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	3 months % change	12 months % change
West End	1.13	1.42	1.05	0.64	**0.54**	-14.7%	-52.0%
City	1.59	1.13	1.48	1.07	**0.73**	-31.5%	-53.8%
Docklands	0.34	0.04	0.28	2.02	**0.02**	-99.1%	-94.5%
Central London	3.06	2.59	2.82	3.73	**1.29**	-65.3%	-57.7%

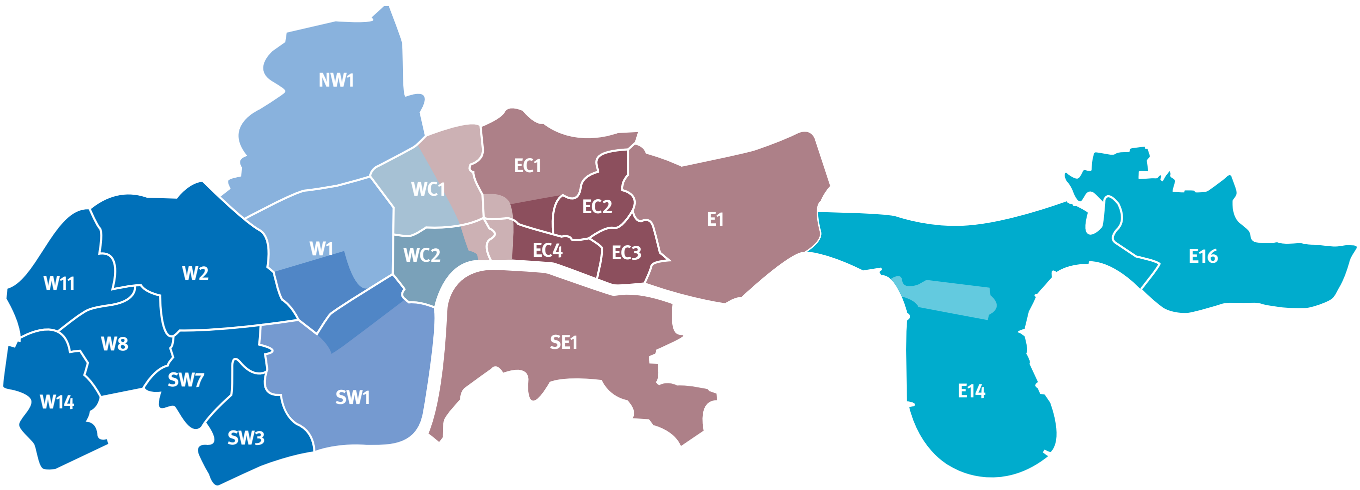
Active Demand (m sq ft)	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	3 months % change	12 months % change
West End	2.43	1.75	0.82	0.99	**0.82**	-17.4%	-66.2%
City	4.17	4.28	3.37	3.49	**3.56**	2.2%	-14.5%
Docklands	0.25	0.07	0.12	0.08	**0.07**	-10.3%	-71.6%
Unspecified Central London	2.15	2.44	3.12	1.56	**1.76**	12.7%	-18.1%
TOTAL Central London	8.99	8.54	7.43	6.12	**6.22**	1.6%	-30.9%

Under Construction (m sq ft)	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	3 months % change	12 months % change
West End	3.87	3.67	2.86	3.06	**2.57**	-16.1%	-33.6%
City	8.04	7.72	7.55	5.98	**6.17**	3.1%	-23.3%
Docklands	1.76	1.77	1.77	1.03	**0.72**	-30.1%	-59.1%
Central London	13.68	13.16	12.18	10.08	**9.46**	-6.2%	-30.9%

Investment (£ m)	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	3 months % change	12 months % change
West End	1148.6	592.4	470.6	760.1	**262.5**	-65.5%	-77.1%
City	970.1	914.6	597.2	457.3	**363.7**	-20.5%	-62.5%
Docklands	0.0	40.8	0.0	838.0	**0.0**	n/a	n/a
Central London	2118.6	1547.8	1067.7	2055.4	**626.2**	-69.5%	-70.4%

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

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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

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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

Knight Frank
Newmark
Global