CoStar GROUP
Real Estate Information

Central London Office Market Report 2008

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Central London Market Snapshot

	2007	2008
Take Up (million sq. ft.)	20.0	12.5
Supply (million sq. ft.)*	28.8	31.9
Asking Rent (psf)	£34.63	£33.20

TREND

Central London succumbed to the economic crisis and nosedived in H2 2008, resulting in take up levels falling by 38% on 2007 and supply increasing 11% on the previous year. 2009 will witness similar lows as rental values continue to decline.

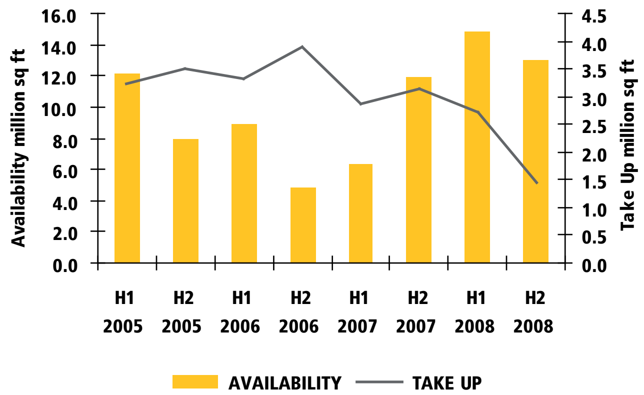
*Definition of Central London Market geography located on the back cover.

2008 has been a year of extremes for the Central London office market. CoStar has recorded exceptional swings in market activity, from the relatively positive signs in the first half of the year, to the spectacular slowdown of the year end.

Central London Market Highlights:

- **Lowest take up in over 5 years as levels fall 60% on 2007.**
- **Available space increases 10% across the Central London Market in 2008 to 31.9 million sq ft.**
- **Available space increases 16% in the top four markets (below) in 2008 to 26.6 million sq ft.**
- **Lease lengths shorten, incidence of break clauses increases.**

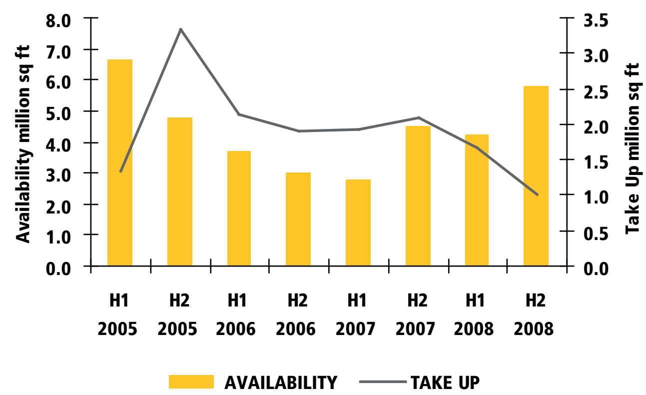
The City



COMMENT

The City took a big hit in H2 with only 1.4 million sq ft of take up, down 48% on the first half of 2008. Available space peaked mid year at 14.8 million sq ft, falling back to finish the year at 13.0 million sq ft.

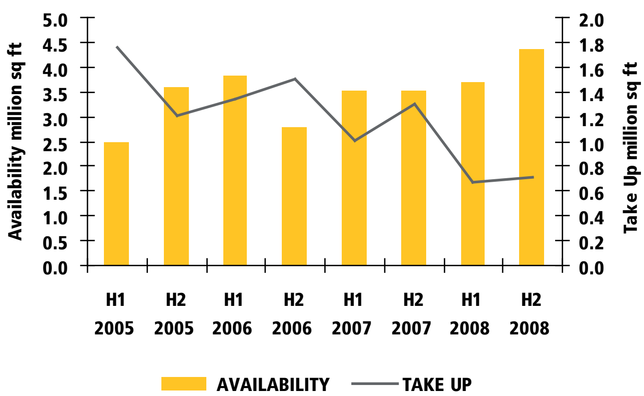
West End



COMMENT

The West End office market achieved take up of 2.7 million sq ft in 2008, down 33% on 2007 levels. Available space stands at 5.8 million sq ft, up 28% on H1 2008.

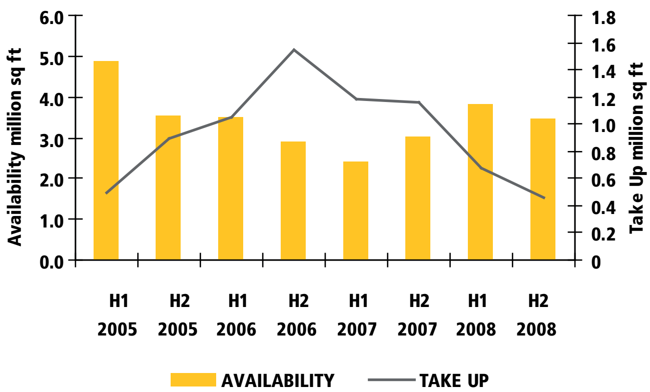
Midtown



COMMENT

Take up levels in Midtown did not exceed 1 million sq ft in neither the first or second half of the year, total take up for 2008 was a modest 1.4 million sq ft. Availability increased to finish the year at 4.4 million sq ft.

Docklands & E1



COMMENT

The Docklands & E1 office market experienced similar levels of activity as those reported back in 2005. Available space dropped to 3.4 million sq ft towards the end of 2008 having recorded just over 1.1 million sq ft in take up.

London & The Economy

A Game of Two Halves

It is fair to say, for the global economy, 2008 will be recorded as an annus horribilis. Two notably different themes dominated the two halves of the year. Having coped with the problems of Northern Rock and worries about hidden financial problems highlighted by the Bear Stearns bailout, the focus through the first half of the year was about containing rapidly increasing inflation driven by escalating energy and commodity prices. The fear was stagflation; low growth and rising prices, which saw the Bank of England keep interest rates high despite the demands of those who feared that this could drive growth ever lower.

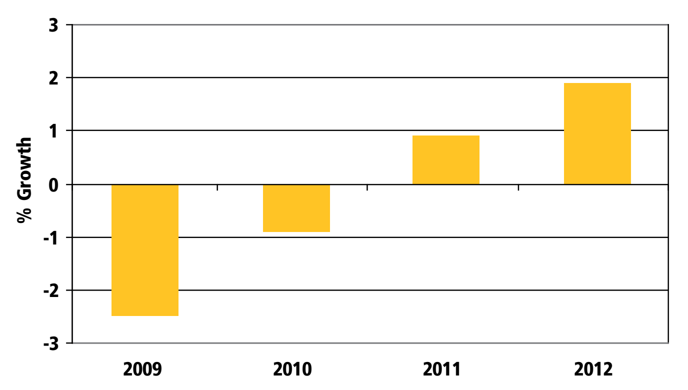
After the Summer Comes the Fall…of Banks!

After a summer lull, all hell broke loose, triggered by the unsupported collapse of Lehman Brothers, fears of global contagion of financial woes proved well-founded and the banking crisis spread around the world, taking distinguished Banks with it. Hundreds of billions of dollars globally were pumped into the money markets in a co-ordinated government effort to create some degree of liquidity between Banks and to stave off systemic implosion of the entire global banking system. Growth was already forecast to slow but, despite hopes that this was specifically a financial market crisis, the depth of the problem rapidly fed through to the real economy and most of the Western world is now in, or heading into recession. In the UK, monetary reaction has seen the minimum lending rate reduced to its lowest level since records began.

Central London, Further Falls in 2009

Commercial property values in the UK continue to fall. Driven largely by rising yields, further falls are expected in response to the deepening economic downturn, impacting prospects for rental value growth and increasing vacancies. As GDP continues to fall, businesses will continue to fail, consolidate and contract, further impacting demand for commercial office space. However, this market does present opportunities for some occupiers to trade up their office space into locations previously deemed too expensive.

GB Real GDP Growth Forecast - The Economist



Globally, whilst there is no hiding from the effects of the banking and economic crisis, the old failings of the property valuation process seem to have reappeared. It is only in the UK and Ireland where dramatic re-pricing has been seen. The US and the Netherlands have seen some minor falls but the rest of the "indexed" world seems to be unrealistically preserving valuations. This should work in favour of the UK investment market as activity increases in the face of ever improving value. There is little to persuade anyone that 2009 will be anything other than a very difficult year indeed, assuming the measures taken so far have the desired results. At least the UK property market has shown it can re-price itself to allow investment to continue to support the sector and deal with what ever lies ahead.

This report is based on CoStar data, as featured in the FOCUS database. Each detail is verified by our team of 103 researchers, to provide comprehensive and accurate information.

The City: Supply and Demand

	2007	2008
Take Up (million sq ft)	6.0	4.2
Supply (million sq ft)*	12.0	13.0
Asking Rental Price (Avg per sq ft)	£35.08	£33.89

3 Years Supply of City Offices… and Growing?

2008 has been a historic year in the City of London Office market; a year of extreme reactions to global problems.

Recorded take up in 2008 was 4.2 million sq ft compared with 6.0 million sq ft in 2007, a fall of 30%, and 7.2 million sq ft in 2006. This is directly attributable to the reducing requirements for space by the financial industry as businesses continue to go bust, contract and consolidate existing space, and put expansion plans on hold.

Whilst take up has fallen steadily since the second half of 2007, the rate of decline has accelerated notably during the final quarter of 2008 with just 0.4 million sq ft leased compared with 1.2 million sq ft for the final quarter of 2007.

By the end of 2008, CoStar Research was recording 13 million sq ft of space available or under construction, an increase in supply of 8% from the end of 2007 and a massive three-fold increase from the end of 2006, when 4.8 million sq ft was being marketed.

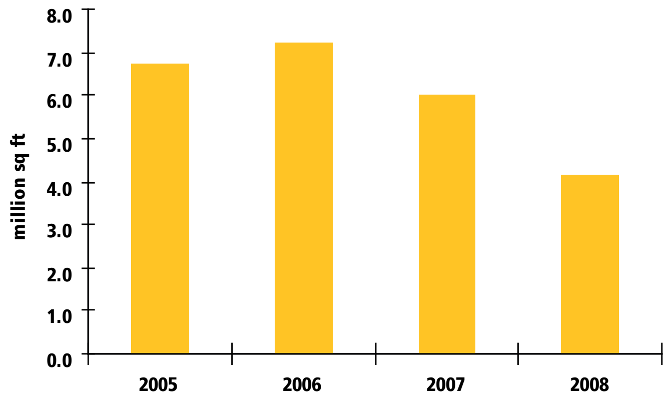
The average quarterly take up rate over 2008 implies there is at least 3 years supply of office space currently available in the City. Adding in the rate of delivery of newly vacated space and the forecast construction deliveries, will see this figure continue to rise throughout 2009.

Contrast in Deals

The largest single deal in Quarter 4 2008 was 33,809 sq ft taken by Fortis Bank at 63 St Mary Axe, contrasting with the largest deal in the first quarter of the year of 201,559 sq ft taken by Addleshaw Goddard Ltd at 1 Moor Gate.

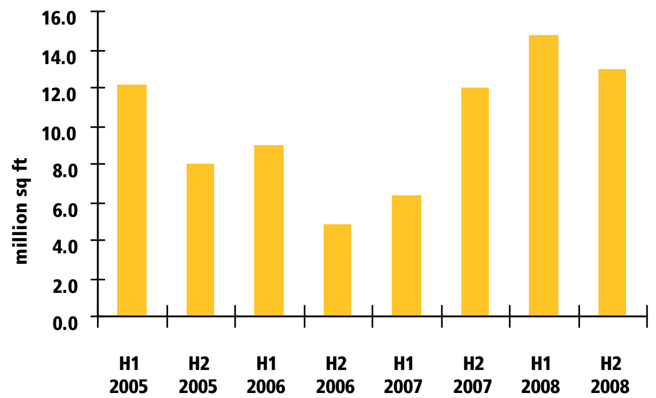
In the fourth Quarter of 2008, the average deal size was 3,555 sq ft, with 75% of deals being less than 5,000 sq ft. Our research also shows a dramatic increase in the willingness of landlords to offer more favourable lease terms. Concessions, such as higher frequency break clauses and longer rent free periods, are now commonplace to secure a letting.

City Office Market: Take Up



COMMENT: The number of transactions in the EC postcodes declined from 1,113 to 672 in 2008, a fall of 40% on 2007.

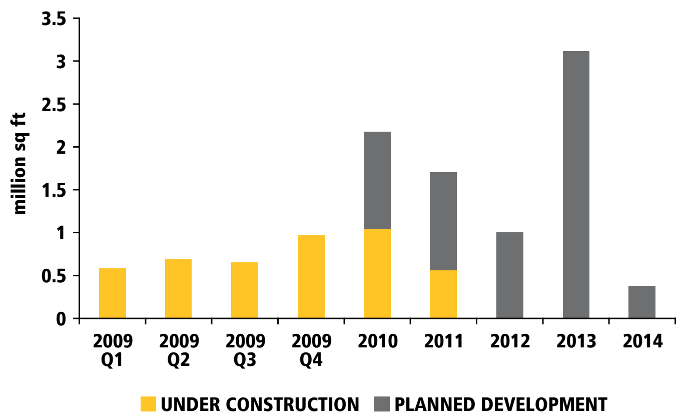
City Office Market: Availability



COMMENT: Available space in The City has increased three-fold in two years from 4.8 million sq ft in 2006 to 13.0 million sq ft in 2008. Space has been staying on the market for an average 390 days prior to leasing.

The City: Development

City Office Market: Development Pipeline



COMMENT

2.7 million sq ft set to deliver to the market in 2009 and a further 2 million sq ft in 2010.

Largest Developments Under Construction

Development	Size (sq ft)	Prelet (sq ft)	Delivery Date
Ropemaker Place	575,119		Q2 2009
St Botolphs, Houndsditch	531,606	84,498	2010
Watermark Place	500,802		Q3 2009
Heron Tower	461,478		2011
23 -29 Walbrook	430,119		Q4 2009

City Skyline Still Dominated by Cranes

The CoStar 2008 1st half Central London Report carried the headline '… Twice the supply and half the demand'.

This became further exacerbated during the second half of 2008. There is currently 8.7 million sq ft of completed space available in the City with an additional 4.3 million sq ft under construction; a level of new supply not seen since 2004.

In 2009, 2.7 million sq ft of the space under construction is scheduled to complete, with the majority in the second half of the year. This includes Ropemaker Place where there are currently no prelets agreed for the 575,000 sq ft development.

A further 2 million sq ft is currently scheduled to hit the market in 2010, of which 1 million sq ft is already under construction. It remains to be seen whether construction commences on the remainder in 2009.

Rental levels will continue to be subject to downward pressure as the market adjusts to increasing supply and contracting demand. Somewhat surprisingly, the average asking rent of all office space offered in the City in 2008, at £33.89 was only 3% lower than £35.08 for 2007. We would expect that figure to fall further through 2009.

This is not an attractive market into which to deliver new, high-quality office space, especially if funding is provided through debt agreements made a year or more ago. Furthermore, the Chancellor has fallen well short of providing any form of assistance through tax relief. So throw empty rates into the mix and the outlook for medium-term investor cashflow also looks bleak.

The City: Tenants and Leases

Pressure Mounts as Yields Rise and Rents Fall

The City Office market has been particularly impacted by the economic downturn and the continued uncertainty in global financial markets due to the occupier demographic.

Long established business models, that have served the City well for decades, are now being questioned with many proving less than sustainable during this historically severe downturn. The businesses to emerge strongly will be those whose strategies have built in downturn contingencies and those capable of implementing the structural and organisational change required to survive in the emerging new world.

From an investment perspective, falling rents and occupier uncertainty in the City are putting returns under immense pressure. A market once driven by cheap available debt and continual capital appreciation, is now firmly entrenched in a sustained period of rising yields and falling rental growth.

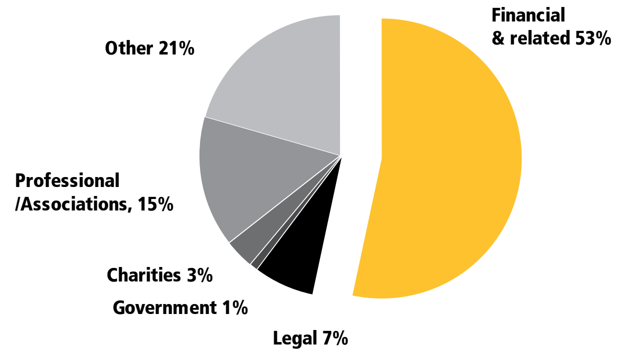
Income risk premiums continue to move out to reflect the uncertainty facing many industry sectors; the uncertainty associated with a serious financial crisis and an underlying economic recession. The result will be driven by basic economic fundamentals, leading to falling rents and more flexible lease terms for occupiers. This is substantiated by our own deal research that shows a higher incidence of break clauses in new leases. In 2007, 32% of new leases granted in the City contained a break clause, in 2008, this rose to 51%. We are also observing smaller space commitments being let on shorter leases, a continuation of the downward trend in lease lengths in the UK.

Whilst more flexible lease terms may prove more sustainable for businesses in the future, by relaxing some of the burden of a traditional restrictive commercial lease, it is the UK lease structure that to date has proved so attractive to investors. Falling rents and increasing vacancy rates have further implications throughout the financial sector, in particular the CMBS and ABS markets where debt secured against property assets rely upon the rental income stream to service the debt repayments.

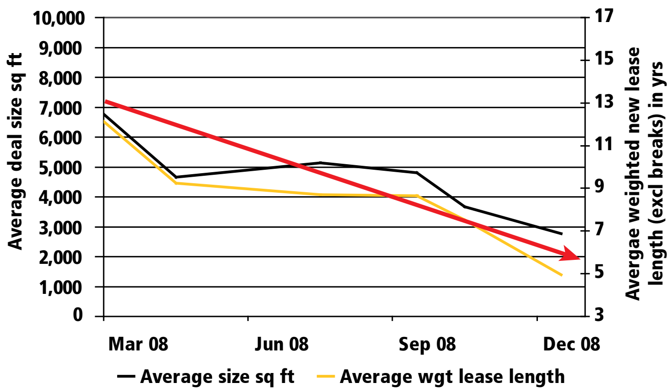
"Given the recent pressures on UK property values, CMBS and other ABS investors have shifted their focus to the downside, the next leg down is expected to come from market rent declines and tenant defaults. Based on our stress testing to date on a number of CMBS deals secured by London City offices, we show no losses on senior AAA rated bond classes, but significant losses on subordinated bond classes."

Han Vrensen
Barclays Capital,
Head of Securitisation Research.

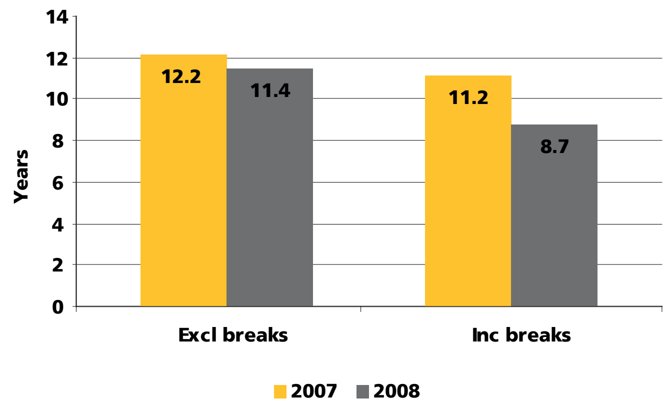
City Office Market: Tenant Composition



City Office Market: 2008 Lease Lengths

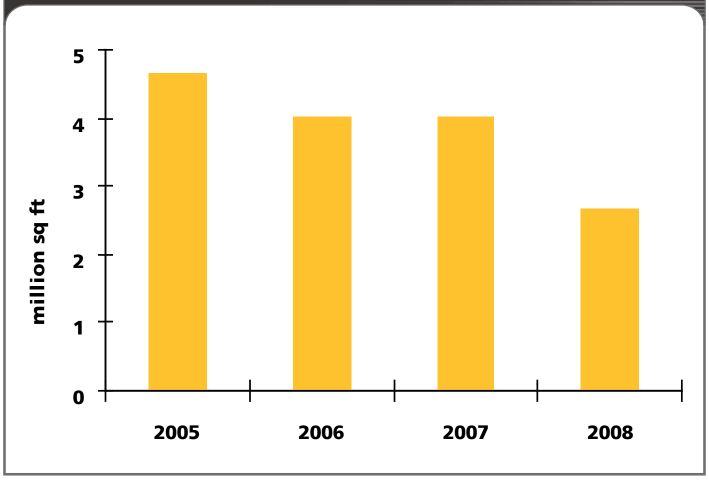


City Office Market: Average Lease Lengths

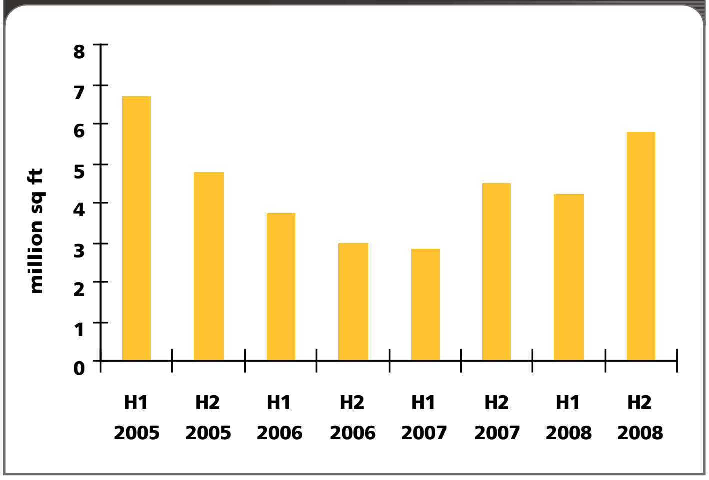


The West End

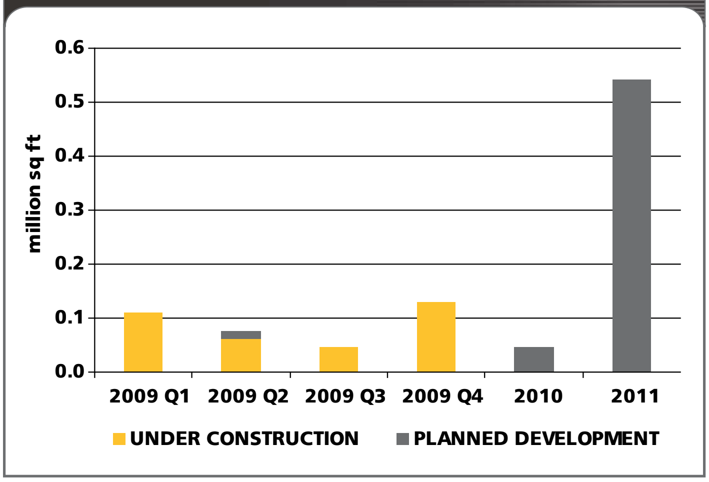
West End Office Market: Take Up



West End Office Market: Availability



West End Office Market: Development Pipeline



	2007	2008
Take Up (million sq ft)	4.0	2.7
Supply (million sq ft)*	4.5	5.8
Asking Rental Price (Avg per sq ft)	£49.07	£51.34

West End Take Up Falls 52% During 2008

In early 2008, demand for West End office space proved relatively resilient as it was hoped the effects of the banking crisis would be limited to the main financial district. However, by year end, the West End market was feeling the full effects of the economic downturn and total take up in 2008 was 2.7 million sq ft, the lowest in 4 years with average deal sizes falling from 3,576 sq ft in 2007 to 3,000 sq ft in 2008.

The largest deals in 2008 included 70,050 sq ft at 20 Manchester Square, 46,169 sq ft at 28 King Street and 37,700 sq ft at 55 Baker Street, all of which took place in the first half of the year. In the second half of the year only 1.4 million sq ft was leased and in Quarter 4 only 373,548 sq ft was leased compared with 1.3 million sq ft for the same period last year, implying the worst is yet to come.

Total available space currently stands at 5.8 million sq ft; levels last seen in 2005. New/refurbished space is at 1.8 million sq ft and second-hand space levels are at 2.7 million sq ft. The largest single available spaces include Ashdown House, Victoria Street, 1a Page Street and 1 Drummond Gate. Only the latter has a quoting rent, which is currently at £45.00 per sq ft.

"We have expanded our Central London Research team to keep pace with the amount of space coming onto the market. The West End seemed to be holding up in the first half of 2008. However, we are seeing a marked increase in the amount of second hand space being marketed and expect this to continue throughout 2009."

Grant Anderson, Central London Research Manager, CoStar.

One bright spot on the horizon is that the current supply in the West End is not being exacerbated by the development pipeline. There is currently only 350,000 sq ft under construction and due to be delivered in 2009. The most significant being 23 Savile Row at 96,214 sq ft and The Peak on Wilton Road in Victoria at 78,029 sq ft. Planning permission has been granted for a further 600,000 sq ft although none of this potential space has yet broken ground.

The impact of the economic downturn is now being felt across the West End. In particular, the high profile Hedge Funds which have been largely responsible for driving prime rents in the West End to unsustainable levels, have now all but disappeared from the market.

Docklands & E1

	2007	2008
Take Up (million sq ft)	2.3	1.1
Supply (million sq ft)*	3.0	3.4
Asking Rental Price (Avg per sq ft)	£23.02	£25.58

Docklands & E1 Shaken But Not Stirred

Office take up in the Docklands & E1 market has seen a decline since the recorded highs of 2006. In 2008, CoStar Research observed that just 1.1 million sq ft was transacted, a 50% decrease from 2.3 million sq ft in 2007 and 2.6 million sq ft in 2006. This makes the Docklands & E1 market, the hardest hit market in Central London.

The Docklands & E1 postcodes have felt the pinch in 2008, the amount of space coming onto the market has continued to increase steadily to 3.4 million sq ft at the year end, a rise of 13% on the 2007 level of available space. 1.2 million sq ft of this is under construction, half of which is scheduled to be delivered in 2009. More worryingly, there is also 6.1 million sq ft in the development pipeline; supply is clearly set to outstrip demand over the coming years. The Docklands market has always been seen as a pressure valve for the City market, but when the EC postcodes are experiencing over supply, will lower rents attract occupiers into a market that is also burgeoning with space?

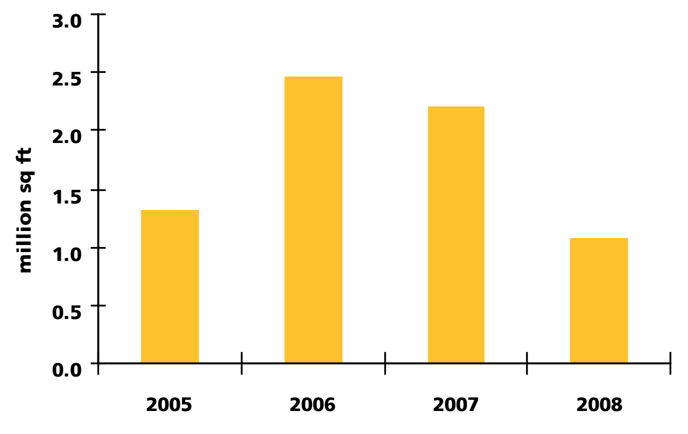
Key Deals

The largest single deal was in March 2008, 169,887 sq ft was let by Moody's Investors Service Ltd from the Canary Wharf Group plc on a 15-year lease at £7,729,858 pa, equating to £45.50 psf. In the second half of the year, the largest space taken was at 25 Canada Square, where the TFL Group leased 115,974 sq ft from Citigroup Ltd on a 10-year lease at £46.50 psf.

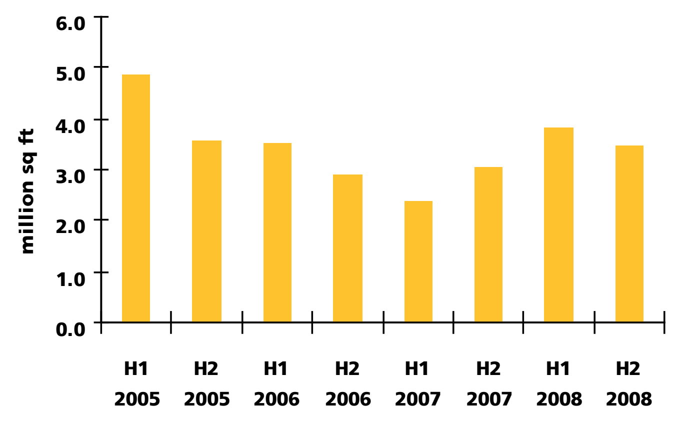
In November 2008, JP Morgan purchased the 999 year lease on the Riverside South development site for £237 million, to develop their new European HQ, providing approximately 1.9 million sq ft of office space. This commitment is good news for the Docklands but less so for the beleaguered City office market which will see JP Morgan vacate their space as the business consolidates its UK operations. Development has yet to commence.

NB: All References to Docklands include the postcodes E14 and E1

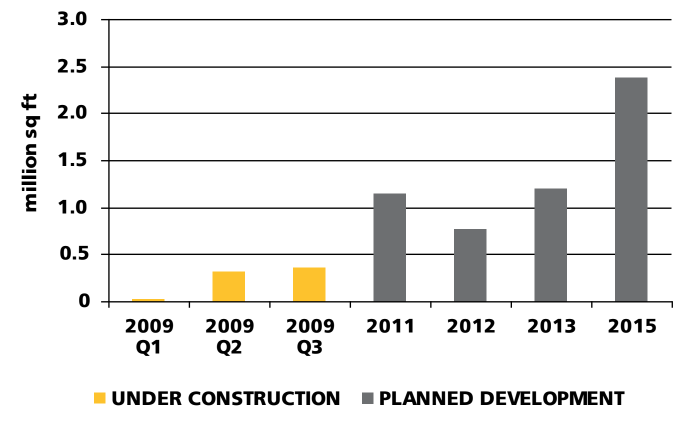
Docklands Office Market: Take Up



Docklands Office Market: Availability

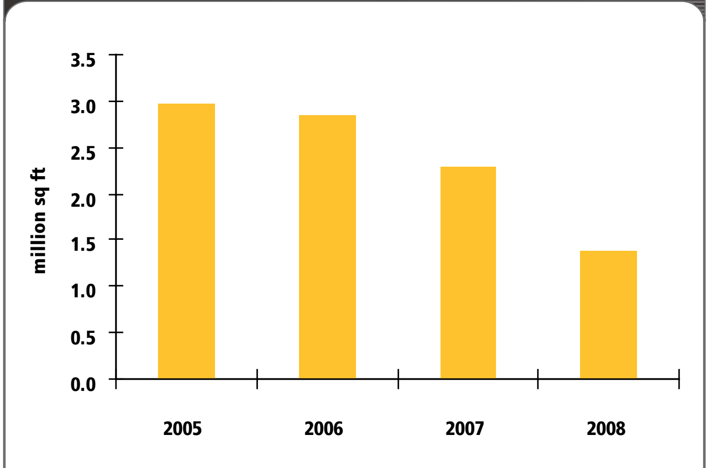


Docklands Office Market: Development Pipeline

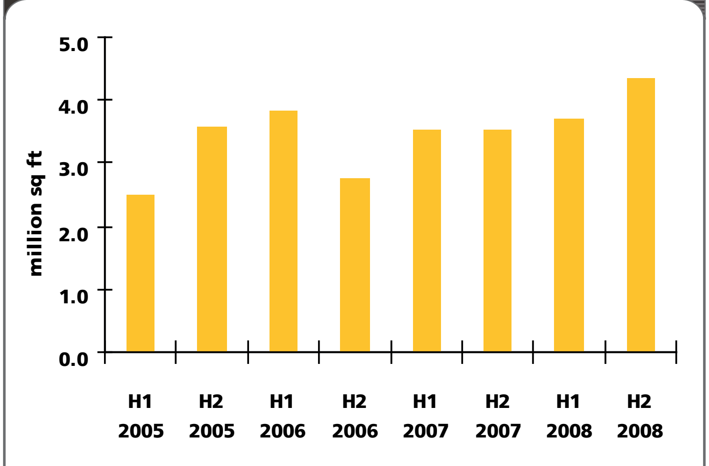


Midtown

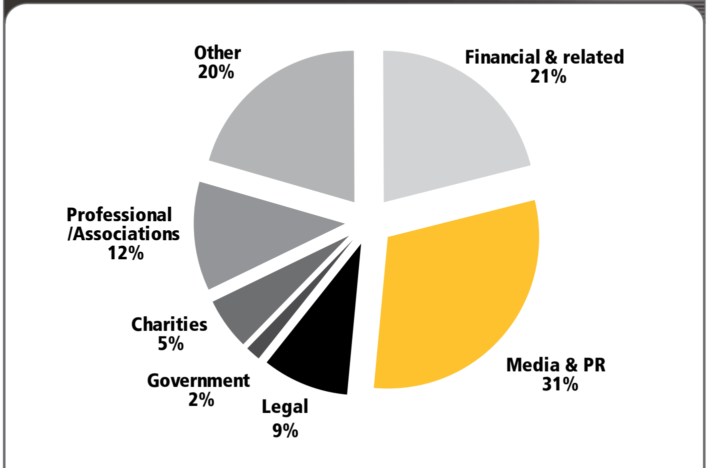
Midtown Market Office: Take Up



Midtown Market Office: Availability



Midtown Market Office: Tenant Composition



	2007	2008
Take Up (million sq. ft.)	2.3	1.4
Supply (million sq. ft.)*	3.5	4.4
Asking Rental Price (Avg per sq.ft.)	£35.34	£37.34

Eclectic Tenant Mix Protects Market From Big Hit

Total take up of offices in Midtown in 2008 was 1.4 million sq ft, down 39% from 2.3 million sq ft in 2007. Take up in Q4 was down 47% compared to the same time last year, the lowest quarterly level since 2004.

The largest letting of the year took place at the newly refurbished New Brook buildings in Great Queen Street. Fladgate LLP pre-let 42,580 sq ft from Henderson Global Investors at £65.00 psf in May. However, a few months later, we recorded 40,508 sq ft taken nearby at the newly refurbished Centrium building on Aldwych by Takeda at £54.00 psf.

Availability in Midtown increased to 4.4 million sq ft at the end of 2008, a level not seen in over 10 years. Of this, 1.5 million sq ft is new or refurbished space. The largest new buildings to the market in 2008 include New Court, 48 Carey Street at 54,863 sq ft, Merdian House, 34-35 Farringdon Street at 42,101 sq ft and 1 New Oxford Street at 29,504 sq ft.

Second-hand space represents 48% of total available space and has increased in response to business failures and contractions in the face of continued economic uncertainty. The most significant second-hand space becoming available includes Mid City Place, 71 High Holborn at 37,970 sq ft.

Available space is set to further increase during 2009 with CoStar Research reporting that just over 1 million sq ft is under construction, with 63% of this due for completion in 2009. Most notably 157,412 sq ft at Nexus Place and 106,692 sq ft at 1 Southampton Row. Beyond 2009, there is 392,596 sq ft due to be completed at Central St Giles in 2010 and 505,000 sq ft with planning permission not yet to break ground. However, compared with other Central London submarkets, future supply is relatively modest and should, to some extent, protect rents going forward.

"The market is moving faster than we have ever seen. The quality of stock currently available and tenant diversification, make previous trends irrelevant. Landlords need to be creative with deal structures and better understand tenants' needs."

Alistair Subba Row, Managing Partner, Farebrother.

Paris: The International Context

	2008	
	Central London	Paris
Take Up (million sq ft)	12.5	21.0
Supply (million sq ft)*	31.9	44.2
Under Construction (million sq ft)	7.7	13

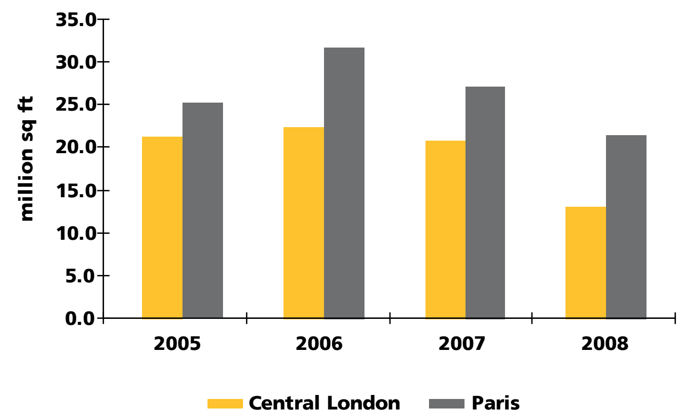
Paris Region - Falling Demand and Increasing Supply, a Familiar Story!

It is looking increasingly likely that the French economy will shortly follow the UK into recession; the wider Eurozone is already officially in recession following 2 successive quarters of negative GDP growth.

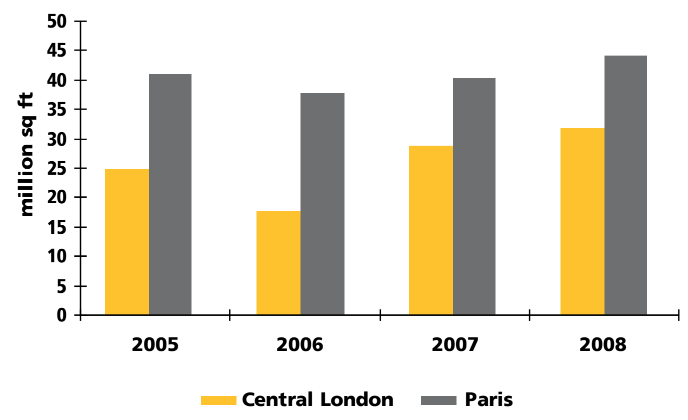
In response to the current climate, occupiers in the Paris Region, like London, are contracting and consolidating their commercial space requirements. This is borne out by a significant drop off in take up throughout the latter half of 2008. Take up of 21 million sq ft in 2008 compares with 26 million sq ft in 2007, a decline of almost 20%. For the same period, the Central London Office Market recorded a fall in take up of almost 38%.

CoStar Research in France, carried out by our subsidiary Grecam S.A, reported a clear increase in the amount of available office space in the dominant Paris Region with significant increases of new and second-hand space coming onto the market in 2008. As in Central London, this is set to be further compounded by the development pipeline. In 2009, there is almost 15 million sq ft of new office space due to be delivered to the Paris Region office market.

Central London vs Paris : Take Up



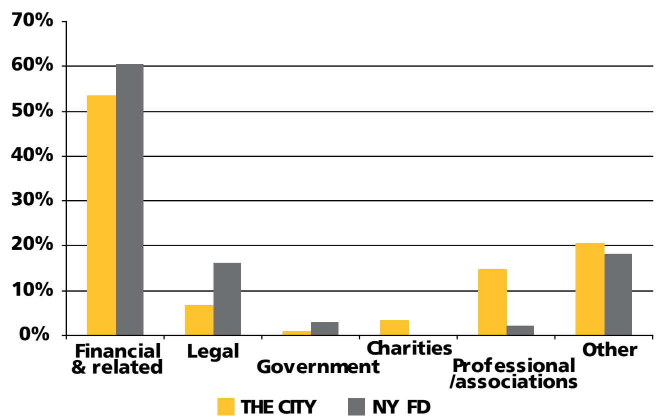
Central London vs Paris : Availability



grecam | Data supplied by GRECAM, CoStar's French subsidiary.
For access to office, industrial or residential availability and deals in the Paris region, visit www.grecam.com

New York Financial District: The International Context

The City vs New York FD: Tenant Composition



	2007		2008	
	The City	NY FD	The City	NY FD
Take Up (million sq ft)	6.0	2.1	4.2	2.0
Supply (million sq ft)*	12.0	3.4	13.0	2.7

Can New York's Financial District Weather The Storm?

The major Financial Districts of both New York and London were subject to massive downward pressures in 2008 in the face of the banking crisis, and continue to be challenged during the deepening economic downturn. However, the supply and demand dynamics have driven a different response and both markets face different medium-term futures.

Leasing activity in the NY Financial District has proved more resilient than its British counterpart , having seen only a 5% decrease in take up levels from 2007 to 2008 compared to the 30% fall in the City. The occupier diversification of these markets is, however, similar in composition and indeed both are similarly exposed to the Financial Services sector.

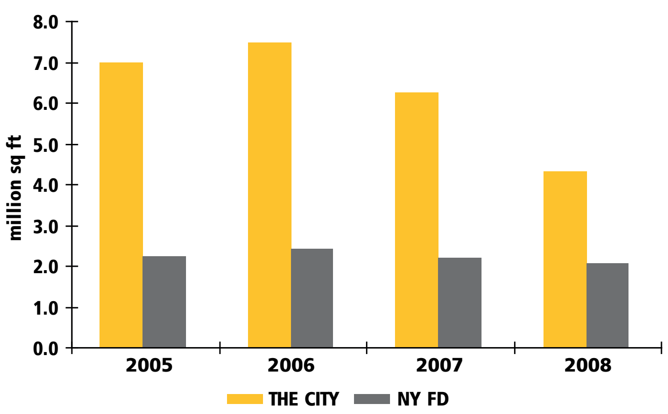
One reason for this maybe the tighter confines of the New York Financial District and the lack of suitable alternative space in the neighbouring submarkets. Indeed until completion of the new development around the World Trade Center, where 11 million sq ft is under construction and will be delivered over the next 5 years, new supply in Central Manhattan will remain constricted.

Also, the relative strong performance of the NY market is heavily skewed by a small number of very large deals, for instance, in June, the global insurance giant AIG, subleased 803,000 sq ft at the Continental Center on Maiden Lane from Goldman Sachs. This took the take up in the second quarter to 1.2 million sq ft. In the absence of this deal less than 0.4 million sq ft would have been leased in the Financial District.

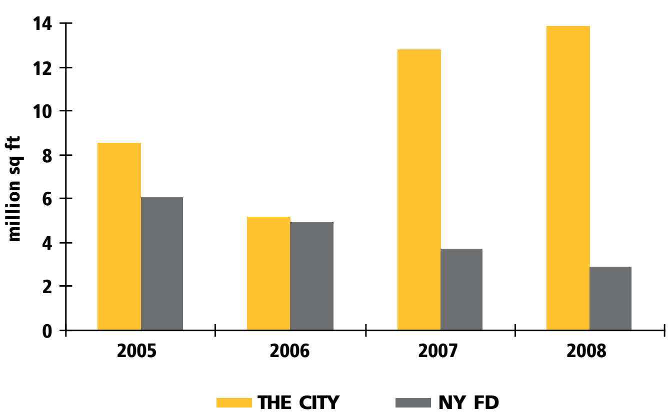
In New York the amount of available space has actually been in decline in 2007 and 2008. There is currently 2.7 million sq ft of available office space with little new space in the development pipeline. This contrasts with the City of London where 2.7 million sq ft is scheduled to be brought to market in 2009 alone.

The majority of construction work that is in progress is in the neighbouring World Trade Center submarket, where 11 million sq ft is under construction and will be delivered over the next 5 years.

The City vs New York FD: Take Up



The City vs New York FD: Availability



Data supplied by CoStar Property Professional. For access to US office, industrial or retail availability and deals visit www.costar.com

Central London Geographic Definitions

The City:
EC1, EC2, EC3, EC4 (excluding EC1N, EC4A, EC4Y)

West End:
W1, SW1

Midtown:
WC1, WC2, EC1N, EC4A, EC4Y

Docklands & E1:
E14, E1

South Bank:
SE1, SE11

Northern Fringe:
N1, NW1

Western Fringe:
SW3, SW5, SW6, SW7, SW10, W2, W4, W6, W8, W9, W11, W12

Data Definitions

Availability:
New, Refurbished, Second Hand, Under Refurbishment, Under Construction. Availability data accurate as at 6th January 09.

Take Up:
New Lease, Assignment, Sublease, Pre-Let.

Asking Rental Price
Asking rents shown are an average of all available space per sq ft.

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