RESEARCH

Q4 2008

CENTRAL LONDON

Quarterly

Knight Frank

HIGHLIGHTS

- Take-up in Q4 reached 3.7 m sq ft across Central London although levels were buoyed by JP Morgan's forward purchase of Riverside South in Canary Wharf totalling 1.9 m sq ft. Take-up for the City was more than 30% below the long-term average, while in the West End, Q4 take-up was 50% lower than average.
- Vacancy rates continued to rise to 8.3%, driven by imminent speculative completions and the release of space to the market by tenants. There is now 18.5 m sq ft of space on the market across Central London, a 35% year-on-year increase, but still well below the 27.6 m sq ft witnessed in 2002.
- Investment turnover in the fourth quarter totalled £2.1 bn, much of which can be accounted for by HSBC's purchase of its own HQ tower in Canary Wharf from Metrovacesa. This brings the total for the year to £7.6 bn, 28% lower than the average for the last 10 years and 60% below the 2007 total of £17.2 bn.

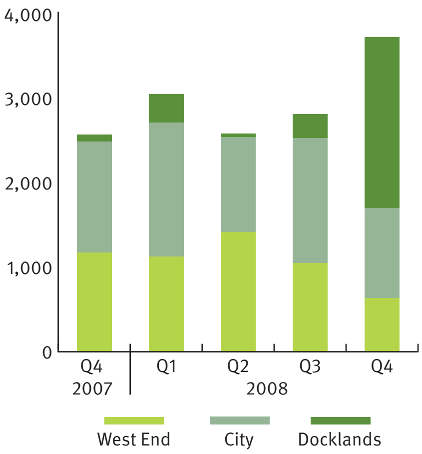
CENTRAL LONDON OVERVIEW

- **Take-up in Q4 2008 came to 3.7 m sq ft, bringing the annual total to 12.2 m sq ft, 22% below the total for 2007.**
- **Central London vacancy rose for the fifth consecutive quarter and is now at 8.3% compared to 6.2% twelve months ago.**
- **Speculative construction activity fell by 27% to 7.0 m sq ft, and is expected to fall further in 2009.**
- **Investment turnover totalled £2.1 bn in Q4 2008 bringing the total for the year to £6.8 bn, 60% lower than 2007.**

Figure 1

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

Q4 2007 - Q4 2008 (000's sq ft)

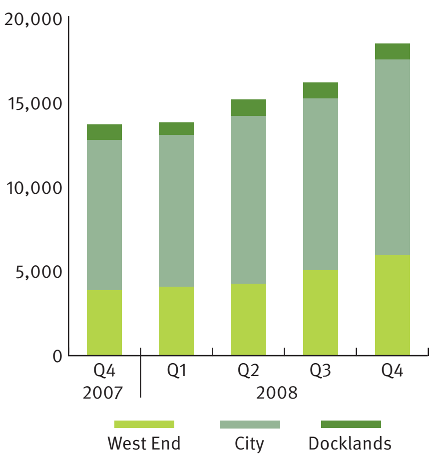


Source: Knight Frank

Figure 2

Central London availability by quarter & market sub-area

Q4 2007 - Q4 2008 (000's sq ft)



Source: Knight Frank

Demand and take-up

Total take-up for 2008 fell by 22% as the Central London office market began to feel the effects of the global credit crisis and the recession in the UK. Around 12.2 m sq ft was transacted over the course of the year, on par with the long-term average but the lowest since 2005. The largest transaction of the year was at Riverside South, Canary Wharf where JP Morgan forward-purchased 1.9 m sq ft for its own occupation. There was 3.7 m of take-up in the final quarter, 14% above the long-term average.

Active demand fell by 18% to 6.1 m sq ft, largely as a result of the removal of JP Morgan's requirement from our figures. While this is well below the 10.1 m sq ft of active requirements witnessed at the beginning of 2006, levels remain well above those at the bottom of the previous cycle, but 20% below the 5-year average.

Supply and development

Availability of both new and second-hand space rose for the fifth consecutive quarter and now totals 18.5 m sq ft, representing a vacancy rate of 8.3%. While availability has increased by 35% over the last 12 months, levels remain below the long-term average and around half of the level seen during the early 1990's.

In response to the uncertain economic conditions and the difficulty in obtaining funding, the volume of space under construction fell considerably to 7.0 m sq ft at the year-end. This represents a fall of 27% over the course of the year and we expect construction activity to fall further during the course of 2009. This should help ease pressure on availability from 2010 onwards.

Investment market

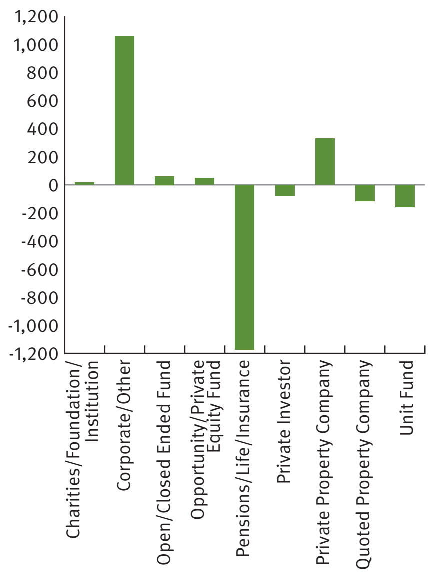
The slow-down in the wider economy was reflected in the continued fall in purchasing activity across Central London. While investment turnover for the quarter, at £2.1 bn, was almost double the previous quarter's level this included HSBC's purchase of its HQ in Canary Wharf for £838 m and Green Properties' acquisition of an estimated £240 m of assets from Pacific Group. While activity remains limited, the falling value of Sterling and the softening of prime yields may represent opportunities for private overseas investors in 2009.

The outward movement of prime yields continued in Q4 2008 as debt markets remained closed to investors. In the City, yields softened a further 50 basis points and now stand at 6.75% for prime investments while in the West End prime yields moved out to 5.75% from 5.35% in Q3. While debt markets remain frozen, prime yields will continue to come under pressure.

Figure 3

Central London net investment

Q4 2008 (£ m's)



Source: Knight Frank

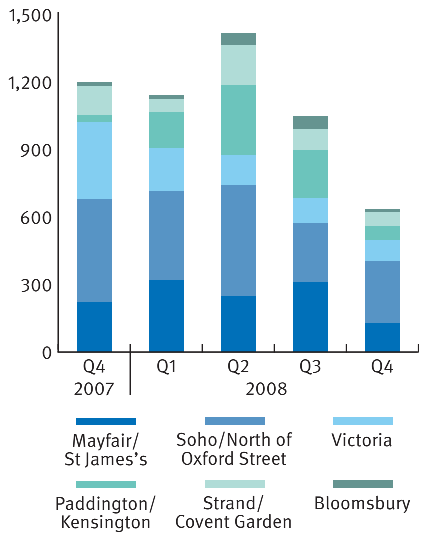
WEST END

- **Take-up for 2008 reached 4.2 m sq ft, 19% below the 10-year average.**
- **Availability rose to 6.0 m sq ft, reflecting a vacancy rate of 6.7%.**
- **Prime headline rents fell by 16% to £92.50 per sq ft during 2008.**
- **Investment turnover in the final quarter of 2008 totalled £706 m, bringing the total for 2008 to £3.0 bn.**

Figure 1

West End take-up by quarter & market sub-area

Q4 2007 - Q4 2008 (000's sq ft)



Source: Knight Frank

Demand & take up

Take-up in the final quarter totalled 0.6 m sq ft, 40% lower than the previous quarter of 1.1 m sq ft. 2008 take-up levels reached 4.2 m sq ft, nearly 20% below the long-term average.

Although occupier demand remained under pressure, active demand rose slightly on the previous quarter reaching just under 1.0 m sq ft. This in part reflects a number of large corporate requirements coming to the market, such as Diageo looking for up to 80,000 sq ft and Red Bull looking for 25,000 sq ft in and around W1. However, the figures are probably time-lagged, and we expect demand to weaken in the near-term as the recession continues.

Supply & development

Availability rose by 17% to 6.0 m sq ft during Q4 2008, representing a vacancy rate of 6.7%. Although supply has continued to rise over the last 18 months, levels are still 9% lower than the long-term average. Having moved into a period of difficult economic conditions, the availability of second-hand space across the West End has reached its highest level in over three years totalling 4.7 m sq ft.

The volume of space under construction on a speculative basis increased 15% from 2.2 m sq ft to 2.5 m sq ft, but is down on the same time last year (2.8 m sq ft in Q4 07). Only three speculative schemes started construction compared to eight the previous quarter. With developers remaining concerned over the economy, the volume of space under construction speculatively could fall in 2009.

Rental profile

Prime rents fell by 14% in the final quarter of 2008 from £107.50 per sq ft to £92.50 sq ft. A fall in demand from the financial sector coupled with the growing expectation that availability will continue to rise, will put Core rents under further pressure in 2009.

Incentives continued to move out, with a typical rent-free period on a 10-year term now at 18 months.

Investment market

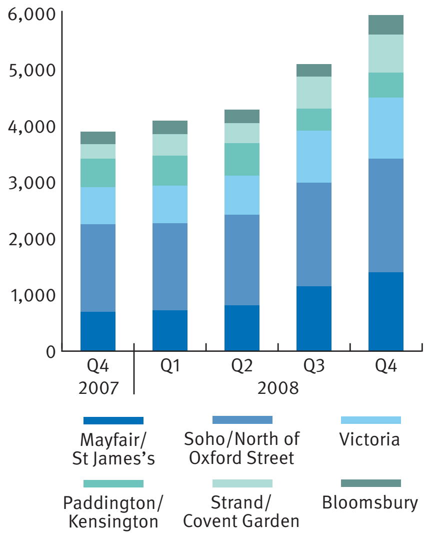
Investment turnover totalled £760 m in the final quarter of 2008, 63% higher than the same quarter last year and matching the long-term average of £760 m. Annual turnover for 2008 totalled £3.0 bn, 37% lower than 2007. It is worth noting that £506.7 m (67%) of the fourth quarter turnover in the West End was in three transactions comprising the sale of New Scotland Yard for £120 m, the sale of 40 Portman Square for £146 m and the acquisition by Green Property of assets from the Kallakis Portfolio for an estimated £240 m.

Private property companies dominated the market in the final quarter, accounting for 39% of purchases. The lack of debt availability continued to place prime yields under pressure. Prime yields moved out to 5.75% from around 5.25-5.50% in Q3 2008.

Figure 2

West End availability by quarter & market sub-area

Q4 2007 - Q4 2008 (000's sq ft)

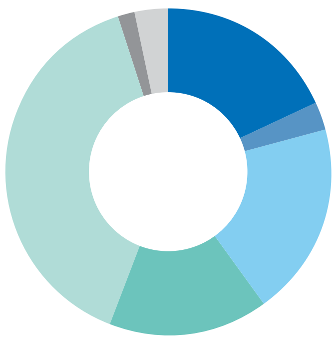


Source: Knight Frank

Figure 3

West End investment by purchaser

Q4 2008 (£ m's)



Corporate/Other	£138 m
Charities/Foundation/ Institution	£21 m
Open Ended/ Closed Ended Fund	£147 m
Private Investor	£120 m
Private Property Company	£298 m
Quoted Property Company	£12 m
Undisclosed	£24 m

Source: Knight Frank

CITY

- **Take-up was 1.1 m sq ft in Q4 08 compared to 1.5 m sq ft in Q3 and 1.2 m sq ft in Q4 07.**
- **Availability increased for a fifth consecutive quarter to 11.6 m sq ft.**
- **Prime City rents declined further to £53.50 per sq ft .**
- **Prime yields rose to 6.75%, representing a 150 bp increase over the course of the year.**

Demand and take-up

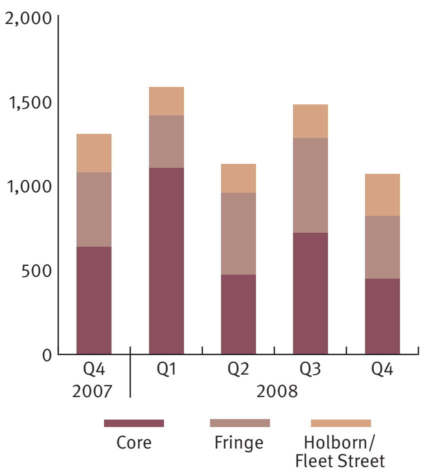
The City office market recorded its fifth consecutive quarter of below average take-up in Q4 08, as the impact of the global financial crisis continued to weigh on demand. At 1.1 m sq ft, fourth quarter take-up compares unfavourably with the long-term average of 1.7 m sq ft per quarter, and is less than the 1.5 m sq ft recorded in Q3 08. The quarter-on-quarter fall reflects a marked deterioration of market sentiment in the aftermath of the Lehman Brothers collapse.

The largest deal in Q4 was Takeda, a pharmaceuticals company, acquiring 39,000 sq ft at Centrium on Kingsway. FirstRand

Figure 1

City take-up by quarter & market sub-area

Q4 2007 - Q4 2008 (000's sq ft)

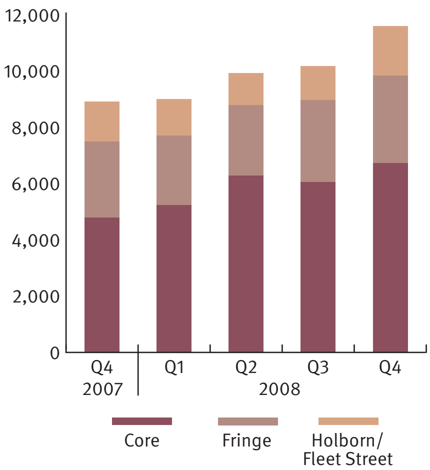


Source: Knight Frank

Figure 2

City availability by quarter & market sub-area

Q4 2007 - Q4 2008 (000's sq ft)



Source: Knight Frank

Group taking 27,000 sq ft at 20 Gracechurch Street was the largest letting in the Core, as well as the biggest deal to a financial firm. That financial markets instability has continued into 2009 has pushed further back the turning point for the City occupier market. Much will depend on whether the government's new banking rescue plan restores confidence in the financial system.

Supply and development

Availability continued to rise, through a combination of approaching development completions and less take-up to absorb second-hand space returning to the market. Supply increased to 11.6 m sq ft by the end of Q4, compared to 10.2 m sq ft three months earlier. This was the fifth quarter in a row of rising availability, and we expect supply to continue to increase throughout 2009.

The level of speculative space under construction fell from 5.8 m sq ft in Q3 08 to 4.4 m sq ft in Q4, confirming that developers have responded quickly to the change in demand and delayed schemes. This should offer some respite for availability levels in the medium-term. Lack of finance and rising availability suggest that the level of construction activity will continue to decline this year.

Rental profile

The prime City rent declined to £53.50 per sq ft at the end of 2008, compared to £63.50 per sq ft a year earlier.

Investment market

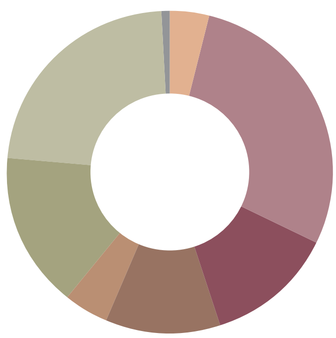
City investment turnover fell to £457 m in Q4, the lowest quarterly volume figure since Q1 2002, reflecting subdued market conditions. Foreign investors were prominent among the buyers. The largest deal of the quarter was the sale of 14 Cornhill to the Libyan Investment Authority for £120 m, reflecting a net initial yield of 6.1%. There was some evidence of UK buyers returning to the market, with London & Stamford paying £74 m for 1 Fleet Place.

There is very little evidence on prime investment transactions, but those that occurred suggest prime yields softened by a further 50 basis points to 6.75% in the three months to the end of December; and over the course of 2008 prime yields have risen 150 bp. However, it is notable that prime yields are offering an attractive premium to a number of other investments, and appear exceptional value compared to historic levels – the long-term average for City yields is 5.78%.

Figure 3

City investment by purchaser

Q4 2008 (£ m's)



Charities/Foundation/Institution	£19 m
Corporate/Other	£130 m
Open Ended/Closed Ended Fund	£58 m
Opportunity Fund	£52 m
Pension/Life/Insurance	£21 m
Private Investor	£71 m
Private Property Company	£105 m
Undisclosed	£3 m

Source: Knight Frank

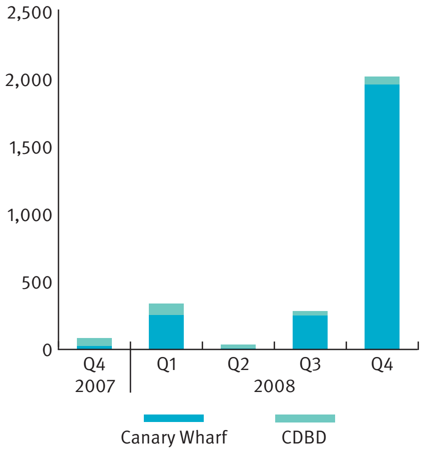
DOCKLANDS

- **Take-up reached a record 2.0 m sq ft thanks to a major pre-sale for occupation at Canary Wharf to JPMorgan.**
- **Availability was unchanged at 1.0 m sq ft.**
- **Prime rents on single floors at Canary Wharf declined to £42.50 per sq ft.**
- **Minimal amount of space under offer at Canary Wharf.**

Figure 1

Docklands take-up by quarter & market sub-area

Q4 2007 - Q4 2008 (000's sq ft)



Source: Knight Frank

Demand & take up

JPMorgan Chase purchasing the Riverside South site to develop as a 1.9 m sq ft headquarters took Q4 Docklands take-up to 2.0 m sq ft – a record quarter. This is an impressive deal for the Wharf given both its size and that it was signed to a backdrop of extreme volatility for the US banking sector. Also, Nomura formalised their 353,000 sq ft short-term tenancy to March 2011 in 25 Bank Street on the space its newly acquired Lehman operations currently occupy.

The long-term future property strategy of the merged bank is currently undecided – Nomura's London headquarters is in the City.

There is a great deal of uncertainty surrounding the demand outlook for Docklands, given the market's high exposure to an embattled financial sector. The recession is also dampening prospects for the occupier market, and much will depend on Docklands' ability in the coming year to appeal to a broader range of occupiers, beyond the financial sector.

Supply & development

Availability in Docklands remained steady in the final quarter at 957,000 sq ft. The market is watching as to when Lehman's vacant offices in 25 Bank Street will be formally marketed so are not included in the availability figures. JPMorgan is marketing 258,000 sq ft in 5 Churchill Place that was originally intended to be Bear Stearns' London headquarters, although as space under construction this will not join the availability statistics until the next quarter. Also, Citi has 131,000 sq ft remaining to lease in 25 Canada Square, after a number of recent transactions.

There is just over 1.0 m sq ft under construction, of which technically 950,000 sq ft is pre-let, but as mentioned 258,000 sq ft is being marketed by JPMorgan for sub-let. In addition, Fitch/Fimilac will be seeking to sub-let just under 200,000 sq ft in the under construction 30 North Colonnade. No schemes are scheduled for completion next year. Work is set to commence on the Docklands Crossrail station, located adjacent to the North Quay site, which will in the long-term improve transport access and link Canary Wharf to Heathrow airport.

Rental profile

Prime headline rents in Canary Wharf on whole floors were approximately £42.50 per sq ft at the end of Q4 08, down from £47.50 per sq ft a year earlier. Outside Canary Wharf the prime rent edged down from £32.50 per sq ft in Q3 to £31.00 per sq ft in Q4.

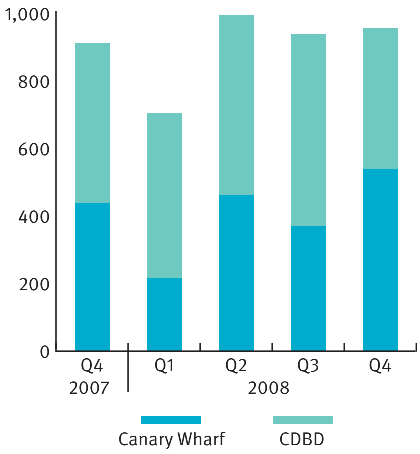
Investment

JPMorgan Chase paid £237 m for the Riverside South site, which is set to be developed by Canary Wharf Group. Also, HSBC reacquired its headquarters building, 8 Canada Square, from Metrovacesa for £838 m, after the failure to syndicate the bridging loan to finance the original deal.

Figure 2

Docklands availability by quarter & market sub-area

Q4 2007 - Q4 2008 (000's sq ft)

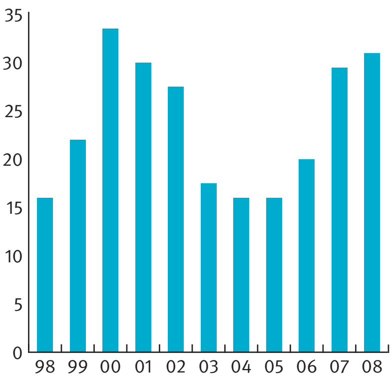


Source: Knight Frank

Figure 3

Docklands CBD prime rent

1998-2008 (Prime £/sq ft)



Source: Knight Frank

Key statistics

Central London office market

Availability (m sq ft)	Q4 07	Q1 08	Q2 08	Q3 08	Q4 08	3 months % change	12 months % change
West End	3.89	4.07	4.29	5.09	**5.97**	17.2	53.4
City	8.92	9.01	9.94	10.19	**11.61**	13.9	30.2
Docklands	0.91	0.71	1.00	0.94	**0.96**	1.8	4.8
Central London	13.72	13.79	15.22	16.22	**18.53**	14.3	35.1

Vacancy Rate (%)	Q4 07	Q1 08	Q2 08	Q3 08	Q4 08	3 months % change	12 months % change
West End	4.4	4.5	4.8	5.7	**6.7**	n/a	n/a
City	7.9	7.9	8.8	9.0	**10.2**	n/a	n/a
Docklands	4.6	3.5	5.0	4.7	**4.8**	n/a	n/a
Central London	6.2	6.2	6.8	7.3	**8.3**	n/a	n/a

Take-up (m sq ft)	Q4 07	Q1 08	Q2 08	Q3 08	Q4 08	3 months % change	12 months % change
West End	1.20	1.13	1.42	1.05	**0.64**	-39.5	-47.1
City	1.31	1.59	1.13	1.48	**1.07**	-27.9	-18.3
Docklands	0.08	0.34	0.04	0.28	**2.02**	n/a	n/a
Central London	2.60	3.06	2.59	2.82	**3.73**	32.4	43.7

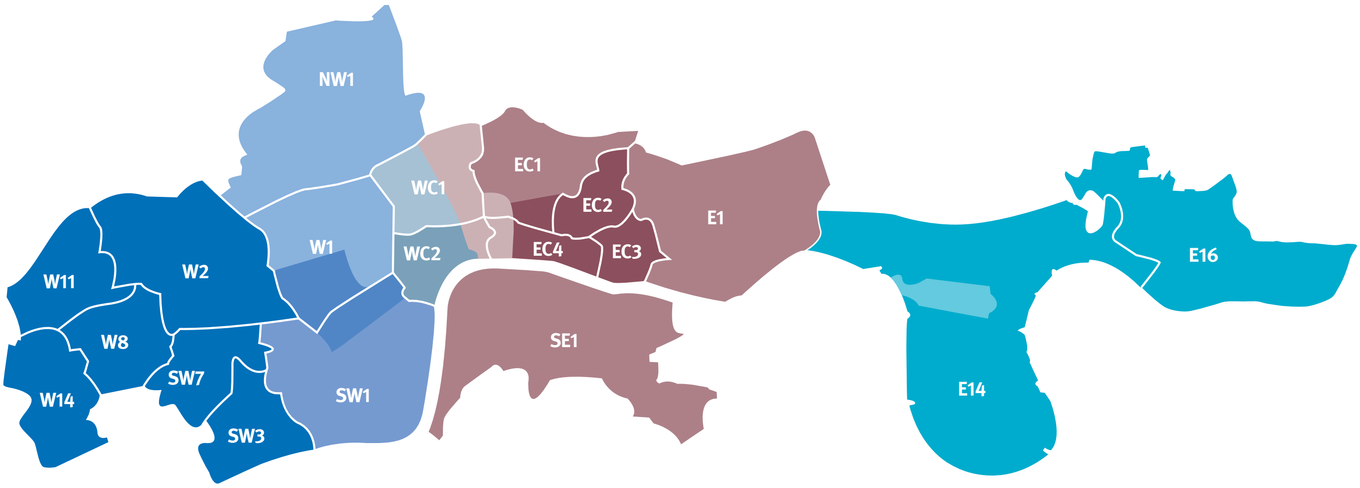
Active Demand (m sq ft)	Q4 07	Q1 08	Q2 08	Q3 08	Q4 08	3 months % change	12 months % change
West End	2.88	2.43	1.75	0.82	**0.99**	20.6	-65.5
City	3.85	4.17	4.28	3.37	**3.49**	3.4	-9.4
Docklands	0.25	0.25	0.07	0.12	**0.08**	-32.6	-69.0
Unspecified Central London	1.41	2.15	2.44	3.12	**1.56**	-49.8	10.7
TOTAL Central London	8.39	8.99	8.54	7.43	**6.12**	-17.6	-27.0

Under Construction (m sq ft)	Q4 07	Q1 08	Q2 08	Q3 08	Q4 08	3 months % change	12 months % change
West End	3.99	3.87	3.67	2.86	**3.06**	7.0	-23.2
City	8.09	8.04	7.72	7.55	**5.98**	-20.7	-26.0
Docklands	1.76	1.76	1.77	1.77	**1.03**	-41.9	-41.5
Central London	13.84	13.68	13.16	12.18	**10.08**	-17.3	-27.2

Investment (£ m)	Q4 07	Q1 08	Q2 08	Q3 08	Q4 08	3 months % change	12 months % change
West End	555.2	1148.6	592.4	470.6	**760.1**	61.5	36.9
City	814.5	970.1	914.6	597.2	**457.3**	-23.4	-43.9
Docklands	0.0	0.0	40.8	0.0	**838.0**	n/a	n/a
Central London	1369.8	2118.6	1547.8	1067.7	**2055.4**	92.5	50.0

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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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