midtown

Strand / Aldwych   Fleet Street   Clerkenwell   Smithfield   St Paul's   King's Cross

research Q3 2008

Farebrother
CHARTERED SURVEYORS

Commentary

Julian Hind

Q3

Twelve months into the credit crunch, the Midtown property market has continued to be sustained by demand from both occupiers and investors. Inevitably, the level of activity has slowed, but the data indicates that our market has continued to provide Central London occupiers and investors with value for money.

To date, the Midtown occupational market has only been marginally affected by external events. Office take-up, which ultimately underpins the market, was maintained in the first three quarters of 2008 at 85% of the level experienced between 2004 and 2007. In the circumstances, this was a strong performance.

We have seen sustained take-up and the maintenance of a relatively low availability rate,

which stood at 6.6% at the end of the 3rd Quarter 2008 compared to 9.3% in the City. Occupiers continued to be willing to enter into transactions in the low to mid-£50s psf in core Midtown and the mid-£40s psf in locations such as Bloomsbury. There is some evidence, however, of rent free periods being extended slightly.

In the investment market, the value of transactions was down on the exceptional levels of 2005-2007, but in the first three quarters of 2008 over £1.3 billion of Midtown property was transacted.

We are not complacent about the prospects for the Midtown office market and do expect to see a more restrained level of take-up and a gradual increase in availability as this cycle proceeds. Midtown's characteristics, however, provide some protection against not only a general downturn in demand in line with business confidence, but also the impact of oversupply in 2009 and 2010 in the neighbouring City market.

The amount of speculative construction in Midtown, and its programmed completion, is closely aligned to the average rate of take-up of new and refurbished space, providing potential protection against oversupply. Demand for Midtown offices is broadly based, with Banking and Financial Services, the sector most affected by global economic conditions, contributing only 13% to office take-up over the past two years. Three other sectors, Legal, other Professionals and Media were each of greater importance than Banking and Financial Services and together accounted for over 50% of Midtown take-up. A diverse occupier base will continue to generate requirements which Midtown offices can satisfy at competitive rents.

Lynton House, 7-12 Tavistock Square, WC1. Farebrother let over 42,600 sq ft in Q3, prior to completion

Take-up

In the 3rd Quarter 2008, Midtown office take-up was 656,000 sq ft, a reduction of just 8% on the 2nd Quarter (Figure 1). The selected lettings table gives an indication of the prevalence of take-up of new and refurbished space and the reduced significance of second-hand take-up in transactions over 10,000 sq ft. Year to date take-up is 1.94 million sq ft.

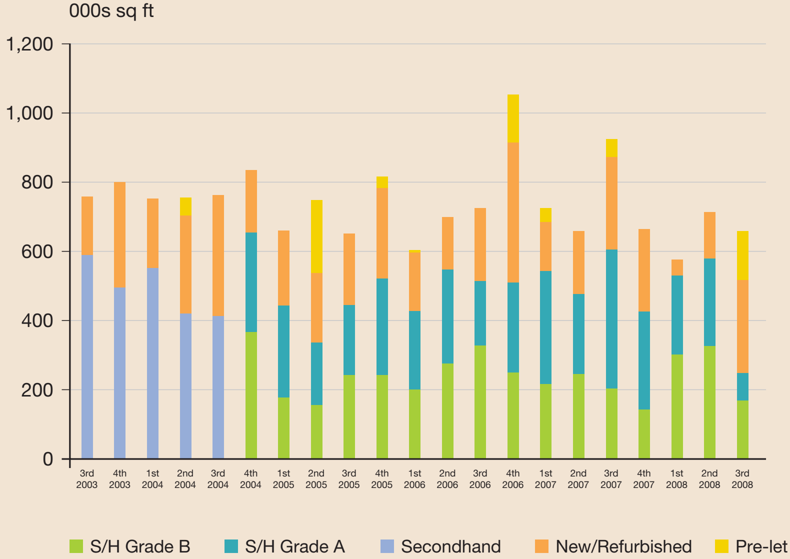
Pre-letting returned to the market with Cancer Research UK leasing part of Angel Building, 411 St John Street, EC1, from Derwent London, triggering a major refurbishment. Cancer Research is reported to be paying £41 psf on the 1st, 2nd and part 3rd floor and £35 psf on the ground floor, on a 20 year lease with a break at 15 years and two years rent-free. It also has an option during the construction phase either to lease a further 28,804 sq ft on the remainder of the 3rd floor, or to exclude the entire 3rd floor.

New and refurbished take-up was 269,000 sq ft in the 3rd Quarter, the highest figure since the 4th Quarter 2006, and encouraging in the light of lower take-up in the 1st and 2nd Quarters 2008. Floors at Centrium, Kingsway, WC2, continued to attract tenants with pharmaceutical company Takeda leasing 3rd and 4th and the Government's Nursing and Midwifery Council the 1st. There were lettings on a further 55,000 sq ft at 5 and 6 New Street Square, EC4.

The lack of choice for new and refurbished space is evidenced by the letting of offices that were still under construction at Lynton House, Tavistock Square, WC1, and 22 Chancery Lane, WC2. Lynton House has been particularly attractive to tenants with 50% of the available space leased during the 3rd Quarter prior to practical completion at rents in the mid-£40s psf. With Alexander McQueen joining Ben Sherman, Agent Provocateur and Timberland, Midtown has now become home to some of the World's leading fashion brands traditionally located in London's Noho, north of Oxford Street.

Second-hand take-up was significantly reduced in the 3rd Quarter at just 248,000 sq ft, the lowest figure since the 2nd Quarter 2003 and a 57% reduction on the 2nd Quarter.

Figure 1: Quarterly Office Take-Up in Midtown



Source: Farebrother

Selected office lettings in **Midtown**

Occupier	Address	Grade	Sq ft	Reported Rent £psf
Cancer Research UK	Angel Building, 411 St John St, EC1	Refurbishment (Pre-let)	139,500	41.00
Takeda Europe	Centrium, 2-18 Kingsway, WC2	Refurbishment	38,749	54.00
Her Majesty's Courts Service	110 Fetter Lane, EC4	New	29,273	Conf.
The Carbon Trust	5 New Street Square, EC4	New	23,312	50.00
Stewarts	5 New Street Square, EC4	New	23,311	50.00
Young & Rubicam Group Ltd	Lynton House, 7-12 Tavistock Square, WC1	Refurbishment	21,460	46.00
Nursing & Midwifery Council	Centrium, 2-18 Kingsway, WC2	Refurbishment	18,570	52.50
Harcus Sinclair	3-4 Lincoln's Inn Fields, WC2	Refurbishment	16,881	48.50
Dixon Wilson	22 Chancery Lane, WC2	New	12,605	60.00 (overall)
Sidell Gibson Partnership	1-4 Holford Yard, Holford Mews, WC1	Second-hand Grade B	12,600	Conf.
Alexander McQueen	76-78 Clerkenwell Road, EC1	Refurbishment	12,186	40.00
Michael Simkins LLP	Lynton House, 7-12 Tavistock Square, WC1	Refurbishment	10,663	45.00
CIFAS	Lynton House, 7-12 Tavistock Square, WC1	Refurbishment	10,515	46.00
Doubletake Productions	8-10 Bowling Green Lane, EC1	New	10,203	42.50 (best space)
McGrath Worldwide Plc	164 Shaftesbury Avenue, WC2	Refurbishment	4,581	56.00
Wedgwood Waterford	164 Shaftesbury Avenue, WC2	Refurbishment	3,641	55.10

Source: Farebrother

Availability

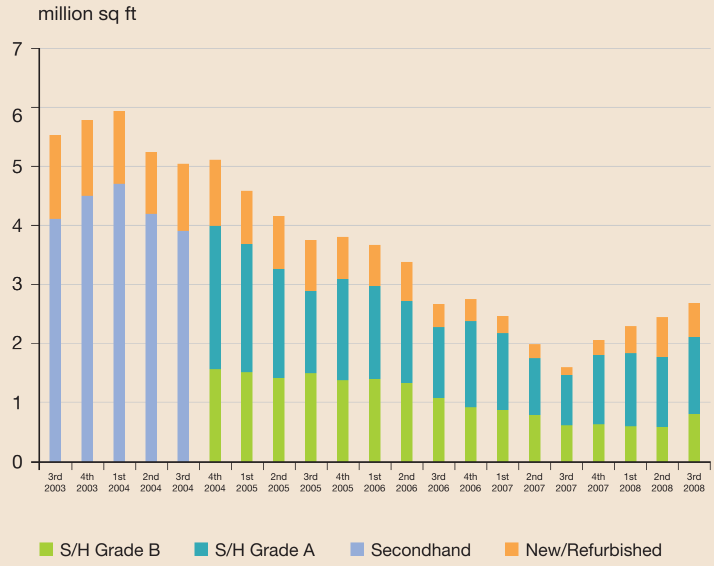
Increased supply is characteristic of the Central London office market at present. Midtown is no exception. Our data shows availability on a rising trend for the past year (Figure 2). This trend is expected to continue in the light of new supply and the impact of external economic influences on demand. The 3rd Quarter saw an increase of 17% in Midtown office supply with 400,000 sq ft added taking total supply to 2.78 million sq ft.

New and refurbished supply increased marginally during the 3rd Quarter from 586,000 sq ft to 601,000 sq ft, with new and refurbished completions largely balanced by a significant increase in the take-up of new and refurbished space. There was also evidence of delay on some schemes, now expected to reach practical completion in the 4th Quarter 2008. New and refurbished supply represents just 1.4% of the total Midtown office stock and only 20% of total availability.

As a corollary to low take-up of second-hand space, the 3rd Quarter witnessed a significant increase of 21% in availability from 1.79 to 2.18 million sq ft. Second-hand Grade A space increased only marginally by 50,000 sq ft to 1.26 million sq ft. In a reversal of a long-term trend, however, there was a very significant increase in the availability of second-hand Grade B space, which was up 57% from 583,000 to 915,000 sq ft. With low vacancy rates on the new and refurbished stock, it would be wise for those with second-hand offices to let to consider refurbishment, increasing the chance of achieving lettings.

At the end of the 3rd Quarter the overall Midtown availability rate was 6.6%, an increase of almost one percentage point during the quarter. During the quarter the distinction in rates between west and east became more pronounced, with the rate in WC1 and WC2 at less than 5%, while in EC4 the rate stood at 7.5% and in EC1 it went into double-digits at 10.2%.

Figure 2: Quarterly Office Supply in Midtown



Source: Farebrother

Future supply

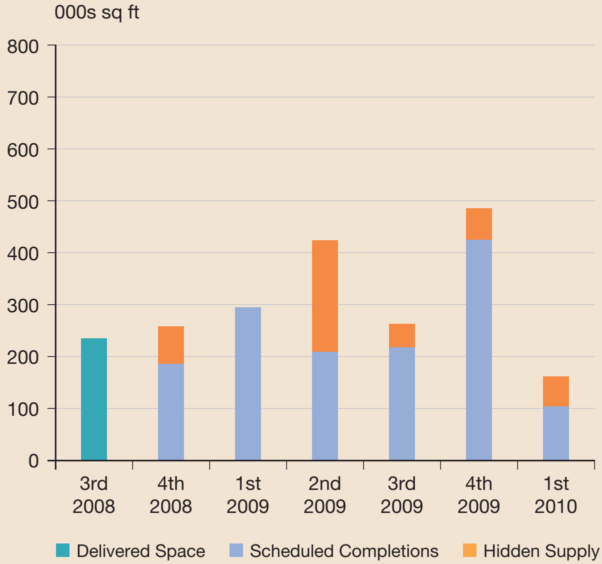
For the second successive quarter both overall and speculative construction in Midtown declined in the 3rd Quarter 2008. Overall construction (including pre-committed space) fell marginally by 4%, dropping below 2 million sq ft for the first time since the 2nd Quarter 2007. The level of speculative construction declined quite significantly from 1.75 million sq ft to 1.45 million sq ft, a fall of 17%, all of which is set to complete over the 18 months to 1st Quarter 2010 (Figure 3).

In a pre-let driven start, Derwent London commenced the major reconstruction and extension of a former BT office at the northern end of St John Street, EC1. Known as Angel Building, the development will increase the office space by 60% from 155,000 sq ft to 247,000 sq ft, with Cancer Research UK having pre-leased 139,500 sq ft. This leaves 107,000 sq ft of speculative space in the building, although under the terms of the lease it is possible for the occupier to take none, half or the whole of the 3rd floor under option agreements – hence the speculative element could be between 81,000 sq ft and 132,000 sq ft.

Work also commenced in the 3rd Quarter on the former PRUPIM offices at Princeton House, 271-273 High Holborn, WC1, which was sold by Prudential to a private investor in October 2007. This is a major refurbishment which is set to complete in the 3rd Quarter 2009, delivering 80,000 sq ft of offices and retail. Demolition work continues on UK & European's new behind façade 100,000 sq ft development of 1 Kingsway, WC2, with a full construction start due in November 2008.

The rate of speculative completions in Midtown is typically in the range of 200,000-300,000 sq ft per quarter, with a peak in the 4th Quarter 2009 of over 400,000 sq ft, reflecting the projected completion of Legal & General/Mitsubishi's Central St Giles scheme. This compares with the ten-year average take-up of new and refurbished space of 215,000 sq ft per quarter.

Figure 3: Future Supply in Midtown 2008-2010



Source: Farebrother

Investment

Niall Gallagher

In the 3rd Quarter the Midtown investment market, like the rest of Central London, continued to be characterised by caution. The market was by no means moribund, however, with £320 million changing hands during the quarter. This represents a reduction of 28% on the 2nd Quarter 2008, and brings the year-to-date value of transactions to just over £1.3 billion.

In the largest transaction of the 3rd Quarter CommerzReal, the property arm of Germany's CommerzBank, acquired the long leasehold of Athene Place, Shoe Lane, EC4, from Scottish Widows for £92.4 million reflecting a yield of 5.85%. This 150,000 sq ft office building constructed in 2002 is fully let to Deloitte until 2027, who have a tenant break in 2019. The other major office transaction was the purchase of the long leasehold interest of 21 Tudor Street, EC4, from Henderson Global Investors by Lanebridge, an investment manager. The £65 million price reflected an initial yield of 4.9%, rising to 6% on the basis of an imminent pre-agreed rent review to £50 psf.

Midtown continues to be attractive to purchasers of non-office assets. During the 3rd Quarter the Crowne Plaza Hotel changed hands for the second time in two years, as Italian Grupo Statuto sold to a private Middle East investor for £85 million. Australian property company Valad completed its purchase of a student housing scheme at Therese House, Glasshouse Yard, EC1, for its University Capital Trust Fund. At 31-33 High Holborn, WC1, Farebrother acted in the sale of the building with vacant possession by BT to a residential developer. A continuing feature of the market in the 3rd Quarter was acquisitions by owner-occupiers, taking advantage of the reduction in values over the past 12 months.

While the majority of investors have been seeking an income stream, it is interesting to note the exchange on Lonsdale Chambers, Chancery Lane, WC2, between owners Aviva Investors and Private Middle Eastern investors for £24.6 million. The building was sold with vacant possession and has planning permission for redevelopment into two office buildings of 92,000 sq ft and 22,000 sq ft. Along with all property markets, Midtown has witnessed a major adjustment in values since August 2007 and although it is possible that values could fall further before bottoming out, the longer term potential is for a return to capital growth.

Selected transactions in **Midtown**

Address	Size sq ft net	Vendor	Purchaser	Reported Price £m
Athene Place, 66-73 Shoe Lane, EC4	148,280	Scottish Widows	CommerzBank	92.4 (Long lease)
Crowne Plaza Hotel, New Bridge Street, EC4	203 rooms	Grupo Statuto	Private Middle East Investor	85.0
21 Tudor Street, EC4	97,218	Henderson Global Investors	Lanebridge Investment Management	65.0 (Long lease)
Therese House, 29-30 Glasshouse Yard, EC1	247 student rooms	HG Mansur	Valad Property Group	30.0
Essex House, 12-13 Essex Street, WC2	17,000	Private	Taylor Nelson	12.0 (Owner occupier)
7 Carmelite Street, EC4	35,225	Tanin Group	Private Occupier	11.0 (Owner occupier)
St Paul's House, Warwick Lane, EC4	30,555	UBS	Private UK	11.0
31-33 High Holborn, WC1	11,350	BT Plc	Westcombe Group	4.9 (Long lease)
17-18 Britton Street, EC1	13,862	ING	Private	4.0
7-11 Britannia Street, WC1	5,018	Ravenhart Securities	Musicians Benevolent Fund	2.84 (Owner occupier)

Source: Farebrother

Athene Place, Shoe Lane, EC4.
Bought by CommerzBank in Q3 for £92.4m

Retail

Jonathan Quelch

The absence of fresh retail market research on Midtown has been a sticking point for occupier and developer investment in the area for years. A strategic view of the market is now available through Farebrother Research. Our research looked at the market positioning of the primary retail streets within Midtown, compared them to the West End and revealed some interesting facts that will help to refocus interest in the area as an important Central London location.

Midtown office space has increased by 6% since 1998 and an area once famous for its government, legal and utility offices is now home to a much broader range of occupiers with higher paid employees. As a result, Midtown now has a much higher proportion of upper-mid & up-market retailers in its primary retail locations than the West End.

The streets benefiting most are Strand, Ludgate Hill, Lamb's Conduit Street, Kingsway, Holborn, High Holborn and Fleet Street. Over the past 10 years, Fleet Street has remained fairly consistent in terms of market positioning, with approximately one third of retailers classified as upper-mid to up-market and 50% classified as mid-market. The level of High Holborn retail floor space, against all other uses, has similarly remained stable over the same period, with space occupied by leisure operators (including sandwich operators and restaurants) having increased by 10%. High Holborn has seen mid market retailing decrease by 10% but up-market operators increase. Fashion retailing on Strand has increased by 14% in 10 years with occupiers such as Jigsaw, Lewins & Top Shop operating from key sites.

Lamb's Conduit Street is an important shopping destination. 48% of fascias there now provide an upper-mid market offer. Independent, up-market fashion operators such as Oliver Spencer, Folk & Pokit have selected the street as their preferred London location and dismissed many of the more traditional West End ones, now occupied by high street brands. 90% of fascias are independent. The majority owner of the street has successfully implemented a marketing campaign that prioritizes independents, maintaining the eclectic atmosphere that helps make the street so popular with workers from Midtown's new occupiers, firms like Ben Sherman, Warner Bros and McCann Erickson.

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