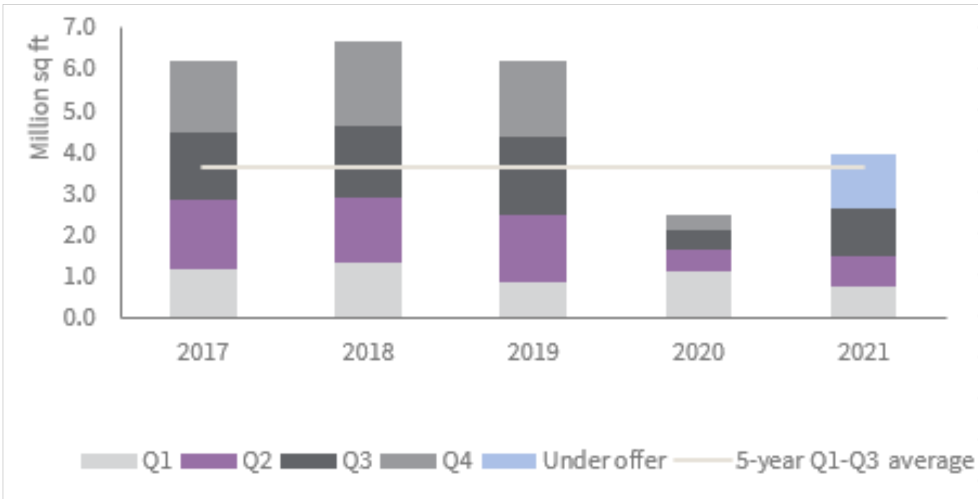
City Market Review – Q3 2021

Occupier take-up

Improving occupier sentiment

- The three-months to September saw the highest level of take-up since the beginning of the pandemic in the City. Take-up totalled 1.2 million sq ft for Q3, which was a 63% quarter-on-quarter increase, albeit it was still 17% lower than the 10-year quarterly average of 1.4 million sq ft.
- This took the year-to-date total to 2.6 million sq ft, which was 27% higher than the amount transacted in the corresponding period in 2020 (2.1 million sq ft) and ahead of the total 2020 volumes. While activity was robust, it remained a third lower than the long-term Q1-Q3 average (3.9 million sq ft)
- Take-up for the quarter was boosted by large transactions, with four deals greater than 100,000 sq ft concluded. The largest transaction of the quarter saw law firm Travers Smith pre-let 157,000 sq ft at Stonecutter Court, EC4. Other notable transactions include T. Rowe Price who pre-let 128,000 sq ft at Warwick Court, EC4 and 50 Finsbury Square, EC2, where Inmarsat pre-let the entire 121,000 sq ft building.
- As a result, pre-letting activity reached 405,00 sq ft or 35% of Q3 leasing volumes in the City. This was the highest level of pre-letting since the first quarter of 2020.
- At the end of September, there was 1.3 million sq ft under offer across City submarkets, a quarter-on-quarter rise of 16%. Whilst this is marginally below the 10-year quarterly average (1.4 million sq ft), it is 75% ahead of the corresponding period in 2020 suggesting take-up will remain buoyant in the final quarter of the year.



Active demand highest level since 2015

- Overall demand increased slightly to 9.5 million sq ft, compared to 8.2 million sq ft at the end of 2020. The quarterly increase was driven by an 3% uptick in active demand, which ended the quarter at 7.3 million sq ft, and is now 14% ahead of the 10-year average.
- Potential demand fell 9% to 2.1 million sq ft, 38% below the 10-year average of 3.4 million sq ft. This could be partly attributed to requirements activating searches earlier due to the low new build vacancy rate and limited speculative development pipeline.

- Professional services sector accounted for the largest share of active demand at 35%, driven largely by law firms, with 2.3 million sq ft required from 31 occupiers. The banking & financial sector remained active, with 32% share of floorspace required.

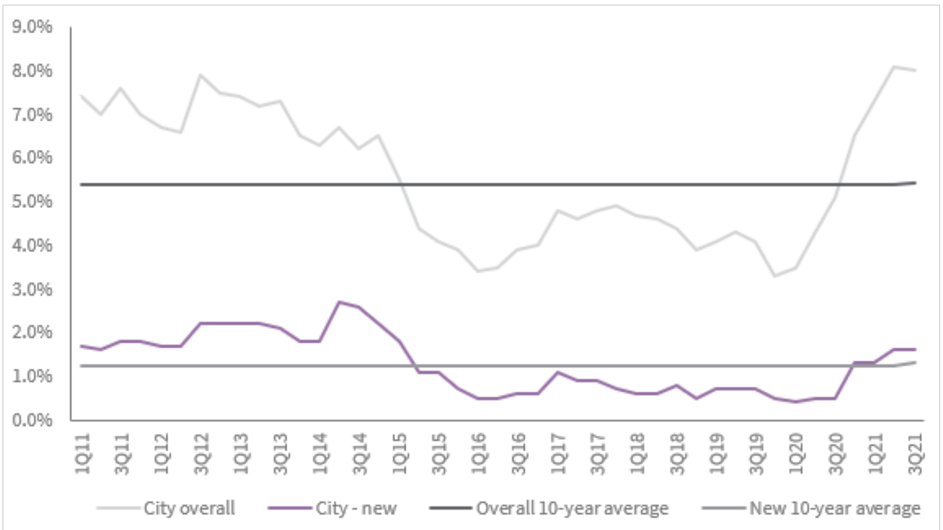
Vacancy falls for the first time in eighteen months

- Following six consecutive quarters of increase, availability started to fall in the City, declining by 2% over the quarter to 9.8 million sq ft, reflecting a vacancy rate of 8.0%. However, supply remained 59% higher than the 10-year quarterly average of 6.2 million sq ft and 63% up on the corresponding period in 2020.

- The new build vacancy rate stabilised at the end of September at 1.6%, however it remained above the level of 0.5% seen at the end of Q3 2020 and above the 10-year quarterly average of 1.2%. The new build vacancy is expected to reduce throughout the remainder of 2021 given the large amount of new build space under offer at the end of September.

- Tenant-controlled supply, which has almost doubled from pre-pandemic levels, remained stable over the quarter at 3.0 million sq ft after six consecutive quarters of increase. Tenant controlled space now accounts for 31% of overall supply, but just under half of this space is available on leases of less than 5 years.

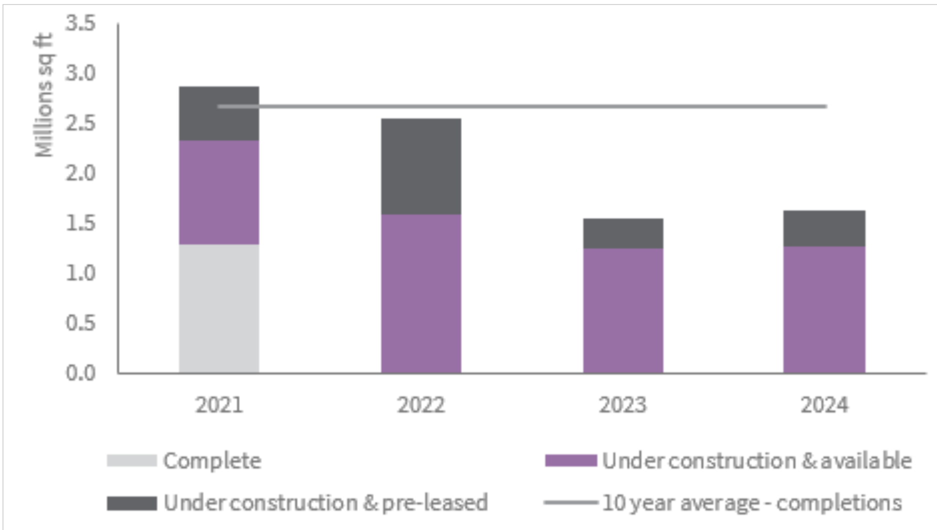
- Development completions slowed during the quarter with just 103,000 sq ft across three schemes reaching practical completion. The largest building to complete was The Luminary, 35 Vine Street, EC3 where 49,000 sq ft is available.



New starts highest since Q1 2020

- Development starts reached their highest total since Q1 2020 with development underway on seven schemes totalling 1.1 million sq ft. The largest scheme to commence construction during the quarter was One Leadenhall, EC3, where 230,500 sq ft remains available following the 200,000 sq ft pre-let by Latham & Watkins.

- At the end of the quarter a total of 5.1 million sq ft of speculative space was underway – over 70% of which is in new schemes and the remainder is refurbished space - compared to 4.7 million sq ft at the end of June.



Increase in prime rents

- Prime rents increased to their pre-pandemic level of £72.50 per sq ft, a quarterly rental increase of 3.6%. Typical rent-free periods remained unchanged at 27 months, based on a 10-year lease term.

Continued weight of demand for core assets led to yield compression

- Investment volumes continued its upward trajectory and rebounded in Q3 to reach £2.0 billion, the second consecutive quarter volumes were over £2 billion, and higher than the 10-year Q3 average. This brought year-to-date investment turnover to £4.9 billion, significantly ahead of the £1.7 billion traded during the same period in 2020 and just 9% below the 10-year Q1-Q3 average of £5.4 billion.

- Turnover in Q3 was supported by eight transactions over £100 million, compared with just one transaction in the corresponding period in 2020. The largest transaction of the quarter was the purchase of Times Square, 160 Queen Victoria Street, EC4, bought by Generali for £460 million, reflecting a net initial yield of 4.14% and capital value of £1,226 per sq ft.

- Overseas purchasers were dominant during Q3, accounting for 92% of quarterly turnover. Incoming overseas capital was driven by European and US investors, accounting for 41% and 32% respectively. The largest transaction purchased by an investor from USA was Milton Gate, 60 Chiswell Street, EC1, bought by Brookfield for £220 million, representing a net initial yield of 4.56%.

- Investor demand remains high in the City, especially from European investors. However, a disconnect between this demand and deliverable stock is evident. Whilst this imbalance has resulted in more approaches being made off market, there is also more stock being prepared for sale on the open market as owners seek to capitalise on the frustrated capital and marked lack of supply.

- With the impact of the pandemic starting to ease and travel re-opening, the weight of international capital targeting London is increasing rapidly with core deals high up the agenda. This renewed activity and competition for best-in-class assets is translating into prime yields sharpening by 25bps to 3.75%.