OFFICE MARKET UPDATE

RESEARCH

CENTRAL LONDON
Q3 2014

Guide to rents and rent free periods

Carter Jonas

THE LONDON OFFICE MARKET IN NUMBERS...

Prime City rents are **£55.00 - £65.00 per sq ft** and £67.50 - £77.50 per sq ft per annum for the upper floors of tower buildings

City Core rent, rates and service charge occupancy costs are typically **£82.50 - £100.00 psf** pa compared with £158.00 - £187.50 for prime West End space

Prime West End office rents have risen by up to 7.7% since Q3 2013 and **are now £105 - £125 per sq ft** per annum

Discounts on landlord's quoting rents are typically 2.5 – 5% throughout much of the London office market

City fringe east, Docklands and Stratford office rents are some of the lowest in London – **typically below £35.00 per sq ft** per annum for refurbished Grade A space

Rent free periods for 5 year leases – up to **11 months (City core)** and up to **8 months (West End prime)**

Midtown rents are **predicted to increase by 7.4%** and **South Bank** rents **by 8%** by Q3 2015

Average rents for new prime located Grade A City and West End office space are anticipated **to reach £65.00 per sq ft** and **£127.50 per sq ft respectively** by Q3 2015

OFFICE RENTS ARE CONTINUING TO INCREASE THROUGHOUT CENTRAL LONDON AS VACANCY LEVELS FALL.

Market dynamics are currently favouring landlords and this trend is set to continue for several years. It is likely to be 2017 / 18 until a more even balance between supply and demand is restored – when the current wave of speculative office developments reach completion.

OVERVIEW

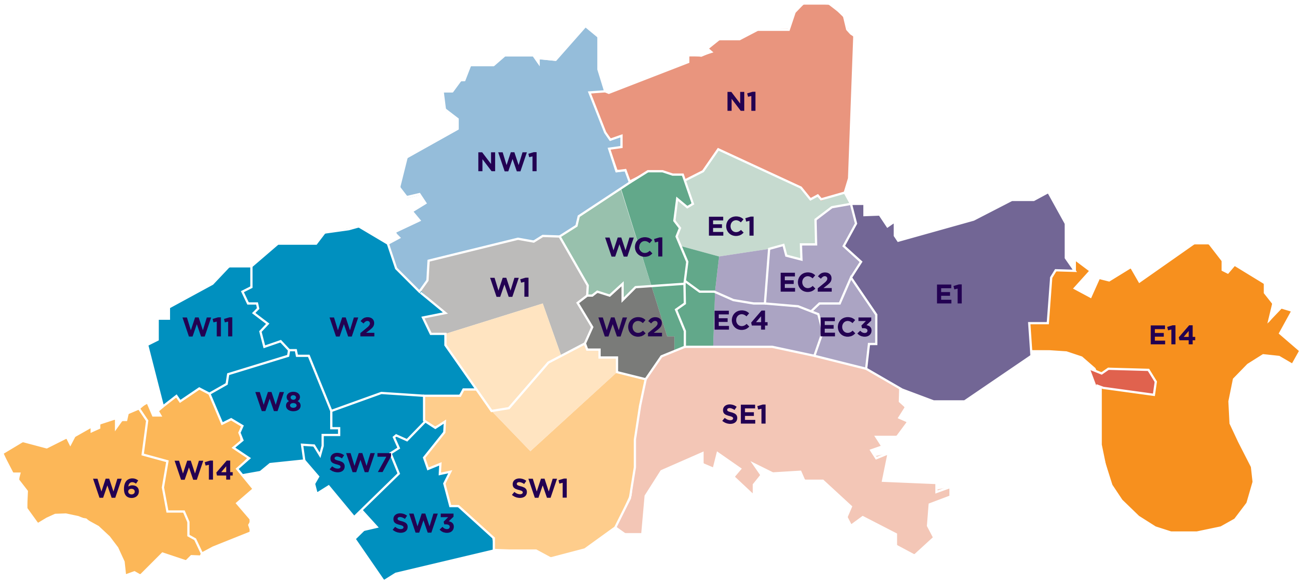
There was a virtual absence of speculative office development in Central London for several years in the wake of the international credit and sovereign debt crisis of 2008/09 as demand and rents fell, in some parts of London by over 40%, and development funding dried up. Six years on and rents for Grade A office space throughout most parts of Central London are at, or very close, to their pre-banking crisis levels and in the City of London and South Bank rents for the upper floors of tower buildings exceed those achieved at the peak of the market in mid 2007 – as have rents for new mid-rise buildings in west London and parts of the 'Midtown' office market.

Rental growth throughout Central London has been driven principally by the historically low levels of vacant office space, rather than resurgent demand, and new national planning policies that encourage the conversion of office buildings to residential use have further added to supply side constraints. Notwithstanding the easier availability of development finance, and the rise in developer optimism, the volume of new office developments currently reaching the market is insufficient to meet the increase in office demand, following the resumption of economic growth. Based on an analysis of the number and size of lettings that are currently taking place throughout Central London, the volume of speculative office development completions programmed over the next couple of years is unlikely to significantly alleviate the current imbalance between supply and demand.

It is likely to be 2017 / 2018 before a healthy balance between supply and demand is restored and in the meantime office rents throughout Central London are almost certainly going to continue increasing (see Figure 5) in tandem with diminishing rent-free period incentives and declining tenant choice.

Over the next few years, as the Central London office market becomes increasingly less tenant friendly, market knowledge will be the key to maximising rent discounts and rent-free period incentives and with this in mind the Carter Jonas Research and Tenant Advisory Teams have prepared this document specifically with the aim of assisting tenants with budgeting and planning for a lease renewal, rent review or office relocation.

LONDON OFFICE LOCATIONS



WEST END

- Paddington/Kensington/Chelsea
- Victoria/Westminster
- Mayfair/St James's
- Soho/North of Oxford Street
- Euston/King's Cross (West)

MIDTOWN

- Strand/Covent Garden
- Bloomsbury
- Holborn/Fleet Street
- King's Cross (East)

CITY/CITY FRINGE

- City Core
- City Fringe (East)
- City Fringe (North)

SOUTH BANK

- London Bridge/ Southwark/Waterloo

DOCKLANDS

- Canary Wharf
- Rest of Docklands

WEST LONDON

- Hammersmith/Olympia/ West Kensington

GRADES OF OFFICE ACCOMMODATION

For marketing purposes office accommodation is generally categorised into Grades which are defined as follows:-

Grade A - new or newly refurbished office space where the building specification includes suspended ceilings and fully accessible raised floors for data/telecoms cable management, passenger lift and air conditioning facilities.

Grade B - office space that may only incorporate under floor or perimeter trunking for data/telecoms cable management, rather than fully accessible raised floors, and/or air cooling facilities, instead of an air conditioning system that dehumidifies, filters and draws fresh air into the building. Grade B space also tends to be of a generally lower quality building specification.

"Comprehensively refurbished" office accommodation is defined as office space that is 'as new', having been completely refitted throughout, to include new fixtures and fittings to the common parts and reception area, new building services – including air conditioning and passenger lift facilities, electrical, plumbing and lighting systems, and new raised floors, suspended ceilings and sanitary ware. The refurbishment specification will comply with the latest health and safety legislation and may also include re-cladding the exterior of the building.

"Refurbished" space is defined as office accommodation where the landlord has redecorated and recarpeted the available office space (but not necessarily the common parts) and overhauled, but not renewed, the building services, such as the air conditioning and passenger lift facilities.

Figure 1
London Office Market – Typical Landlord Quoting Rents – Q3 2014

Location	Typical Quoting Rent per sq ft per annum		
	Grade A		Grade B
West End - W1, W2 & SW1	**New / Comprehensively Refurbished**	**Refurbished**	**Refurbished**
Mayfair / St James's - Prime locations e.g. Berkeley Square, St James's Square	£105.00 - £125.00	£85.00 - £100.00	£62.50 - £75.00
Mayfair / St James's - Secondary locations e.g. Albermarle Street, St James's Street	£77.50 - £97.50	£65.00- £77.50	£52.50 - £62.50
North of Oxford Street (west) - Prime locations e.g. Portman Square, Cavendish Square	£77.50 - £90.00	£62.50 - £75.00	£42.50 - £55.00
North of Oxford Street (west) - Secondary locations e.g. Baker Street (north), George Street	£62.50 - £72.50	£47.50 - £57.50	£40.00 - £45.00
North of Oxford Street (east) - "Fitzrovia" / Great Portland Street	£65.00 - £75.00	£52.50 - £62.50	£39.50 - £52.50
Soho, Regent Street	£65.00 - £87.50	£55.00 - £62.50	£40.00 - £50.00
Haymarket, Lower Regent Street	£55.00 - £69.50	£45.00 - £52.50	£35.00- £45.00
Victoria	£62.50 - £70.00	£47.50 - £60.00	£38.50 - £45.00
Westminster, Millbank	£47.50 – £55.00	£42.50 - £52.50	£35.00 – £40.00
Knightsbridge	£75.00 - £85.00	£57.50 - £67.50	£42.50 - £50.00
Paddington / Bayswater	£52.50 - £60.00	£42.50 - £52.50	£32.50 - £40.00
Euston	£60.00 - £70.00	£42.50 - £50.00	£32.50 - £40.00
"Midtown" - WC1, WC2, NW1, Pt EC1 & Pt EC4			
Bloomsbury	£55.00 - £65.00	£42.50 - £50.00	£35.00 - £42.50
Holborn – Prime locations e.g. New Street Square, High Holborn	£57.50 - £70.00	£46.50 - £56.50	£35.00 - £45.00
Holborn - Secondary locations e.g. Gray's Inn Road, Theobalds Road	£47.50 - £55.00	£38.50 - £54.50	£32.50 - £37.50
Covent Garden / Strand / Charing Cross	£62.50 - £70.00	£50.00 - £62.50	£40.00 - £47.50
Shaftesbury Avenue / St Martin's Lane	£60.00 - £70.00	£45.00 - £55.00	£37.50 - £42.50
Kingsway / Aldwych / Fleet Street	£55.00 - £69.50	£39.50 - £55.00	£32.50 - £37.50
King's Cross / St Pancras	£65.00 - £72.50	£45.00 - £57.50	£32.50 - £39.50
City of London – Pt EC1, Pt EC2, Pt EC3 & Pt EC4			
City of London - Prime locations e.g. Gracechurch Street, Lime Street / Fenchurch Street, Old Broad Street	£55.00 - £65.00 (£67.50 - £77.50)	£45.00 - £56.50	£37.50 - £42.50
City of London - Secondary locations e.g. Blackfriars, Old Bailey, Barbican, Liverpool Street, Aldgate	£48.50 - £59.50	£37.50 - £48.50	£30.00 - £37.50
Fringe City of London – Pt EC1, Pt EC2, Pt EC3 & E1			
City Fringe North / North West– Farringdon Clerkenwell, EC1, Finsbury Square & Shoreditch, EC2	£46.50 – £57.50	£37.50 – £45.00	£25.00 - £35.00
City Fringe East - Spitalfields, Aldgate East, E1 & Tower Hill, EC3	£32.50 - £51.50	£27.50 - £39.50	£19.00 - £24.00
"South Bank" - SE1			
Waterloo / Southwark / London Bridge / Borough	£50.00- £57.50 (£67.50 - £80.00)	£37.50 - £50.00	£25.00 - £35.00
Albert Embankment - river views	-	£32.50 - £38.50	£25.00 - £29.50
Docklands - E14 & Stratford – E20			
Docklands - Prime locations e.g. Canary Wharf / Heron Quays	£42.50 - £45.00	£27.50 - £39.50	£22.50 - £30.00
Docklands - Secondary locations e.g. Limeharbour, Marsh Wall	-	£22.50 - £29.50	£15.00 - £20.00
Stratford	£35.00 - £39.50	£25.00 - £32.50	£17.50 - £20.00
South West / West London, SW3, SW6, W4, W6, W8, W11, W14			
Chelsea	£55.00 - £65.00	£40.00 - £50.00	£27.50 - £37.50
Kensington / Queensway / Notting Hill	£50.00 - £57.50	£37.50 - £47.50	£27.50 - £35.00
Fulham / Hammersmith / West Kensington / Olympia	£45.00 - £50.00	£32.50 - £45.00	£25.00 - £30.00
Chiswick	£45.00- £52.50	£32.50 - £37.50	£25.00 - £30.00

Source: Carter Jonas Research

OFFICE RENTS

Throughout most parts of the London office market landlords have increased quoting rents by, typically, circa £1.50 and £3.50 per sq ft per annum since the beginning of the year.

The table opposite provides a geographical summary of typical office rents in each of the London office sub-markets as at Q3 2014. Rents for the upper floors of tower buildings are shown in brackets.

The rents for office space available on leases of less than five years have been excluded from figure 1 because they are often discounted to reflect the risks/ costs associated with the need to relocate within a relatively short period.

The variation in rents is reflective of:

- the different supply and demand dynamics of each sub-market
- the age, quality and specification of the available office space
- proximity to public transport

RENT FREE PERIODS

During the middle of 2009, the generally accepted low point in the London office market following the world banking crisis, rent free periods of circa 12-15 months for West End and South Bank office space, based on five year leases, and 24 - 30 months for ten year leases, were typical.

In the City, Docklands and 'Midtown' markets rent free periods have similarly narrowed since the middle of 2009 when rent free periods of 15 – 18 months (five year leases) and 30 – 36 months (ten year leases) were the market 'norm' contrasts with the rent free periods that are commonly available today – as outlined in the table below.

RENT DISCOUNTS

The extent to which discounts can be negotiated on landlord's quoting rents will be influenced by the supply and demand dynamics of each location and how long a particular property has been on the market. During the first half of 2013 rent discounts of 5 – 10% were commonplace, contrasts with discounts of 2.5 – 5% which are now more typical.

Figure 2
Typical Rent Free Periods – Q3 2014

Location	**Typical Rent Free Period Agreed (lettings over 5,000 sq ft)**	
	5 year lease	**10 year lease**
City of London Prime - Old Broad Street, EC2 / insurance district, EC3	9 - 11	21 - 24
City of London Secondary - Blackfriars, EC4, Barbican, EC2, Liverpool Street, EC2, Aldgate, EC3	11 - 13	24 - 26
City Fringe North / North West – Farringdon, Clerkenwell, EC1 & Shoreditch, EC2	5 - 7	10 - 16
City Fringe East – Spitalfields, Aldgate East, E1 & Tower Hill EC3	11 - 13	22 - 26
"Midtown" - Holborn, WC1 / Covent Garden, WC2 / King's Cross, N1	7 - 10	16 - 21
West End Prime - Mayfair, W1 / St James's, SW1	5 – 8	14 - 18
West End North – Marylebone, Fitzrovia, Soho, W1	7 - 10	17 - 22
West End South – Westminster, Victoria, SW1	8 - 11	19 - 24
"South Bank" - London Bridge / Southwark, SE1	7 - 10	18 - 23
West London - Hammersmith, W6, Olympia, W14	7 - 11	16 - 20
Docklands – Canary Wharf, E14	12 - 14	24 - 28

Source: Carter Jonas Research

The rent free period that can be agreed on a particular letting will be influenced by the prevailing market conditions and the extent to which the landlord may have interest in the office space from other prospective tenants.

On lettings of, typically, sub 5,000 sq ft, rent free periods tend to be circa 1-2 months shorter than those summarised in Figure 2 above, reflecting the more acute imbalance between supply and demand in that segment of the office market, and the tendency for some small and mid-size businesses not to retain a property consultant to represent their interests in lease negotiations.

MOVEMENTS IN OFFICE RENTS SINCE Q3 2013

Figure 3 opposite provides a summary of the movements in rents for new and comprehensively refurbished Grade A office space, excluding the upper floors of tower buildings, in the various Central London office sub-markets since Q3 2013.

COMPARISON OF TOTAL OFFICE COSTS – Q3 2009 VS Q3 2014

Rent, business rates and building service charge costs are the principal outgoings associated with leasing office space in a multi-tenanted building. Figure 4 opposite provides a summary, by sub-market, of the changes in office costs for prime located Grade A office space since mid 2009, which has been chosen as the base year from which to compare the increases in office costs because:

- mid 2009 is the generally accepted low point in the office market cycle, following the international credit and sovereign debt crises
- it is the year that immediately preceded the UK wide business rates re-valuation of commercial property which took effect from 1 April 2010. The re-valuation has resulted in significant above inflation increases in business rates payable in many Central London locations - most notably in the West End in areas such as Mayfair, St James's, Marylebone / North Oxford Street, Soho and Victoria.

THE OUTLOOK FOR TENANTS DURING THE NEXT 12 MONTHS

The continuing imbalance between the supply and demand for office space throughout London is resulting in a shift in the balance of negotiating power away from tenants, which is resulting in the following trends:

- lower levels of rent discount on landlord's quoting rents
- shorter rent free periods
- limited or no break option linked rent free periods
- a reluctance by some landlords to accept tenant only lease break options instead of agreeing the more usual leasing structure – a ten year lease incorporating a five year tenant break option
- larger rent deposits where the financial status of the proposed tenant is considered weak.

Figure 3
Changes In Typical Grade A Office Quoting Rents (per sq ft pa) Since Q3 2013

Location	Rent Q3 2013	Rent Q3 2014	% change
City of London Prime - Old Broad Street, EC2 / insurance district, EC3	£52.50 - £59.50	£55.00 - £65.00	4.8 – 9.2%
City of London Secondary - Blackfriars, EC4, Barbican, EC2, Liverpool Street, EC2, Aldgate, EC3	£45.00 - £52.50	£48.50 - £59.50	7.8 – 13.3%
City "Fringe" North/North West - Farringdon, Clerkenwell, EC1, Finsbury Square, EC2	£45.00 - £55.00	£46.50 - £57.50	3.3 – 4.5%
City Fringe East – Spitalfields, Aldgate East, E1 & Tower Hill, EC3	£28.50 - £39.50	£32.50 - £51.50	14.0 – 30.4%
"Midtown" - Holborn, WC1 Covent Garden, WC2	£57.50 - £69.50	£62.50 - £70.00	0.7 – 8.6%
West End Prime - Mayfair, W1 / St James's, SW1	£97.50 - £120.00	£105.00 - £125.00	4.2 – 7.7%
West End Secondary – Marylebone, Fitzrovia/North Oxford Street East, W1	£57.50 - £69.50	£62.50 - £75.00	7.9 – 8.7%
"South Bank" - London Bridge / Southwark, SE1	£45.00 - £52.50	£50.00 - £57.50	9.5 – 11.1%
West London - Hammersmith, W6	£40.00 - £47.00	£45.00 - £50.00	6.4 – 12.5%
Docklands - Canary Wharf, E14	£40.00 - £45.00	£42.50 - £45.00	Up to 6.3%

Source: Carter Jonas Research

Figure 4
Typical Office Costs - Prime Located New & Refurbished Grade A Space – Q3 2009 vs Q3 2014 (£ per sq ft pa)

Cost Variable	West End		City of London		Docklands		Midtown		South Bank	
	2009	2014	2009	2014	2009	2014	2009	2014	2009	2014
Rent	60.00 - 85.00	105.00 - 125.00	45.00 - 50.00	55.00 - 65.00	32.50 - 40.00	37.50 - 42.50	45.00 - 52.50	62.50 - 70.00	32.50 - 42.50	50.00 - 57.50
Business Rates	18.00 - 22.50	44.00 - 50.00	15.00 - 17.75	18.50 - 22.50	12.50 - 14.50	14.75 - 16.00	12.75 - 15.25	23.00 - 27.00	11.00 - 14.25	16.50 - 18.25
Service Charge	7.00 - 10.50	9.00 - 12.50	7.00 - 10.50	9.00 - 12.50	9.00 - 12.50	11.94 - 15.44	7.00 - 10.50	9.00 - 12.50	7.00 - 10.50	9.00 - 12.50
Total	85.00 - 118.00	158.00 - 187.50	67.00 - 78.25	82.50 - 100.00	54.00 - 67.00	64.19 - 73.94	64.75 - 78.25	94.50 - 109.50	50.50 - 67.25	75.50 - 88.25
% Increase	**58.9% - 85.9%**		**23.1% - 27.8%**		**10.4% - 18.9%**		**39.9% - 45.9%**		**31.2% - 49.5%**	

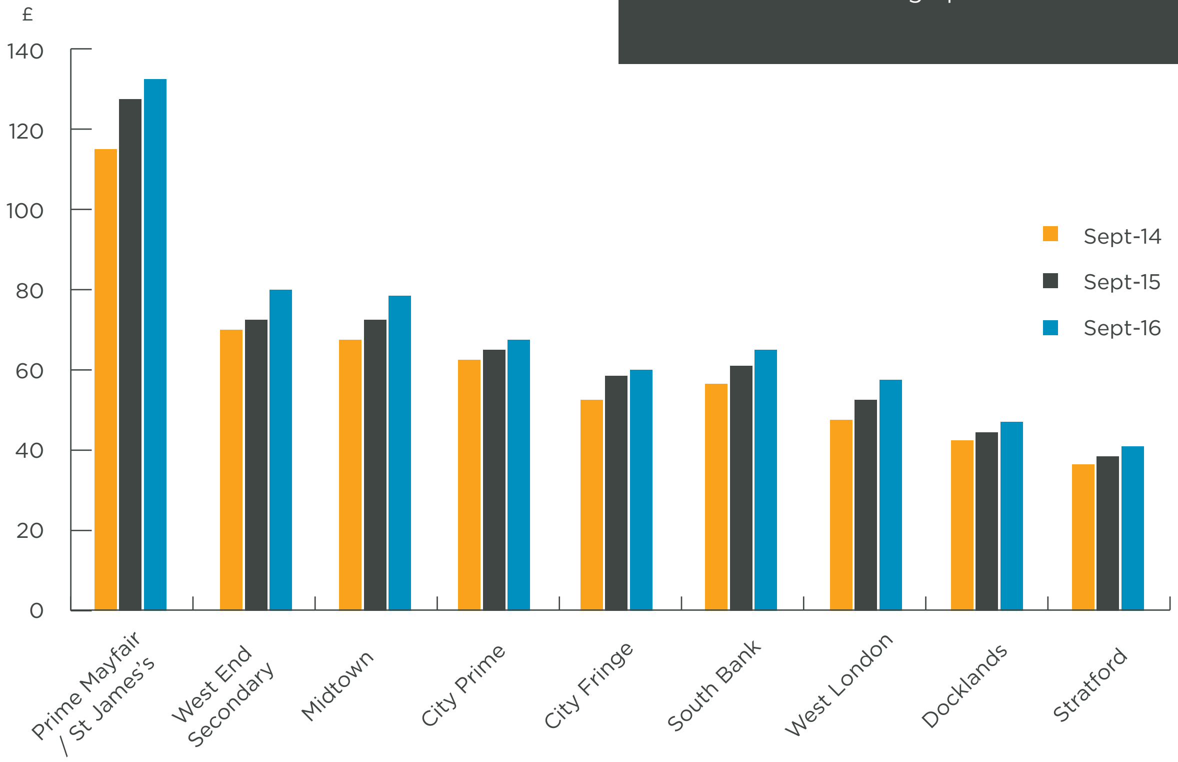
1. The rents in the table relate to Grade A office space, i.e, new or comprehensively refurbished accommodation incorporating air conditioning and fully accessible raised floors for data / telecoms cable management.
2. Rents for the upper floors of tower buildings typically command rental premiums of 15 - 25 % and have been excluded.
3. Geographical definitions - the prime office locations for each Central London office sub-market set out in the table above comprise the following:
   - West End = Mayfair, W1 & St James's, SW1
   - City of London = Old Broad Street, EC2 & the insurance district, EC3
   - Docklands = Canary Wharf, E14
   - Midtown = Covent Garden, Strand and Kingsway, WC2
   - South Bank = London Bridge, SE1
4. Docklands service charge costs include the Canary Wharf estate charge, currently £2.94 per sq ft pa.
5. Business rates are based on the rental value of a property - and will therefore be higher in areas associated with high rents.

Source: Carter Jonas Research

Figure 5
Current and Predicted Office Rents

RENTAL GROWTH PREDICTIONS

Based on an analysis of the office development completion pipeline and predicted patterns of office demand, the Carter Jonas Research Team has prepared a series of rental growth predictions for prime located Grade A office space in each of the London office sub-markets which are summarised in the graph below.



Source: Carter Jonas Research

MARKET TRENDS

Persisting supply side constraints, and improving demand, are contributing to the following trends which are becoming established within the London office market:

- **an increase in landlord's quoting rents** throughout most parts of London, typically of between £1.50 - £3.50 per sq ft per annum since the beginning of the year with the largest increases being in the South Bank, City secondary and prime West End office markets, reflecting strengthening demand and declining vacancy levels
- **a narrowing of rent free periods** since Q3, 2013 of between one and two months, based on five and ten year lettings, respectively
- **increasing speculative office development** and refurbishment activity as rents and tenant demand increase and the availability of development finance continues to improve
- **the continued migration of tenants from the West End** - especially from high cost locations such as Mayfair, St James's, Marylebone/North Oxford Street and Soho where rents and business rates costs have risen significantly since mid 2009 (see Figure 4), to lower cost areas such as the South Bank, City of London and City fringe. Law firm Howard Kennedy FSI's relocation from the West End to 54,500 sq ft at No 1 London Bridge on the South Bank is one of several recent examples of this trend.
- the **availability of newer, better specified, offices in** areas such as King's Cross, **Docklands, The City and South Bank,** that are often capable of accommodating space requirements on a single floor, is another factor this **is catalysing the migration of West End tenants.**
- **demand from the banking, insurance, financial and professional services sectors,** traditionally the mainstays of the City of London and prime West End office markets, **has continued to improve** since the beginning of 2014, as the UK and world economies emerge from recession.
- the **technology, media and creative industries are also continuing to underpin demand** for office space, particularly in the "Midtown" and City fringe sub-markets, with companies such as Google and Facebook expanding and leasing additional office space.
- **demand** for London office space **is being further**

supported by tenants that are being displaced following the decision of some landlords to secure a higher rate of return from their property **by redevelopment, refurbishment or residential conversion.**

- **the undersupply of vacant floor space,** and limited tenant choice, **is encouraging some tenants to start their property searches a good deal earlier** than would otherwise be the case, with a sizeable proportion of tenants entering into 'pre-letting' agreements on new and refurbished office space before the buildings are completed and ready for occupation. The letting of 2 New Ludgate, EC4 in its entirety, comprising 193,000 sq ft, to Mizuho is just one of several recent large scale Central London pre-lettings, as tenants compete to secure space that meets their location and operational needs in an undersupplied market.
- although not an uncommon feature of the City of London office market, **pre-letting is**, unusually, now **becoming an established trend in the West End** office market, where Esteé Lauder and KPMG have recently agreed pre-lets on, respectively, 144,000 sq ft at 1 Fitzroy Place, W1 and 40,000 sq ft at 20 Grosvenor Street, W1, reflecting the limited availability of suitable existing buildings.
- compared with Q3 2013, **there are now just four,** out of a total of nine, **London office sub-markets capable of offering refurbished, air conditioned, office space**, incorporating fully accessible raised floors for data / telecoms cable management, **at rents below £35 per sq ft per annum** - these include Stratford, Docklands, east City fringe and west London.
- **after a period of nearly six years of falling and, more latterly, static, rents, the Docklands office market is witnessing a resurgence in rental growth - rents for Grade A space at Canary Wharf have recorded an increase of up to 6% since Q3 2013**, reflecting renewed interest in the location as rising rents in other sub-markets such as the West End, South Bank, Midtown and City encourage tenants to seek better value elsewhere.
- following the 2012 Olympics, **Stratford is emerging as a credible option for tenants seeking affordable office space at rents below £35 per sq ft per annum.** The profile of the area has recently been given a further boost following the decision of the Financial Conduct Authority and Transport for London to lease space of 425,000 sq ft and 250,000 sq ft respectively at Stratford's 'International Quarter'.
- **the north City fringe**, traditionally regarded as a low cost property option for media and the creative industries that have been priced out of areas such as Soho and Covent Garden, is rapidly becoming a 'mature' market. **Demand from technology, media and creative businesses has**, over the last few years, **fuelled the rise in office rents** to a point that has significantly reduced the cost advantages of the location. As a consequence, those tenants seeking better value are now focusing their searches in the east City fringe, in areas such as Aldgate, Spitalfields and Tower Hill, where rents for refurbished air conditioned space are typically £27.50 - £39.50 per sq ft per annum, contrast with Clerkenwell and Farringdon, where rents for equivalent quality space are now typically £37.50 - £45.00 per sq ft per annum.
- **the continued erosion of the stock of office buildings** in London, in particular in the West End and Midtown areas, **to residential conversion is further underpinning growth in office rents** as those tenants displaced from buildings that are subject to conversion seek office space in a market where the supply of suitable alternative accommodation is declining.
- **the rise in office rents and strengthening of demand is fuelling an increase in speculative office development**, including high rise mixed use buildings, typically incorporating residential units on the upper floors and also, in some cases, hotel and retail uses.
- **the increase in high rise development**, in particular **in the City and South Bank areas, is partly a function of the lack of available large scale development sites upon which to construct low/mid-rise office buildings** and partly a tacit acknowledgement by local planning authorities that, in order to stem the loss of employment-generating floor space to residential use, it is necessary to compromise and allow developers to construct taller buildings offering both office and residential accommodation.
- **businesses that are reliant on a highly skilled, young, creative workforce** are beginning to buck the traditional trend of moving out of high cost areas in Central London to business parks along the Thames Valley / M4 corridor and are, instead, **relocating their businesses closer to the pool of skilled labour in Central London.** Amazon's decision to relocate from Slough to 213,000 sq ft at 60 Holborn Viaduct, EC1, is just one such example of this trend.
- by shrinking journey times, **Crossrail, when completed in 2018, is likely to reinforce the trend for tenants in high cost Central London locations to relocate to areas offering better value** – such as Docklands (13 minutes on Crossrail from Bond Street) and Stratford (15 minutes from Bond Street). These areas are likely to become increasingly popular with tenants currently based in the West End and Midtown areas, where business rates and rental costs are significantly higher – see Figure 4.
- **the office environment is increasingly being viewed by occupiers as a fundamentally important element in the battle to attract and retain skilled staff** and this trend is translating itself into better building design with the inclusion of shared roof gardens and roof terraces, better levels of natural light with the use of floor to ceiling height glass curtain walling and the provision of secure bike storage, shower facilities and collaborative work

space which can be made available for use by all tenants in a multi-tenanted building.

MINIMISING OFFICE COSTS

Property costs are typically a business' second largest overhead after staff costs. Since mid 2009, the low point in the Central London office market following the international credit crisis, office rents and business rates costs have risen significantly above the rate of inflation – see figure 4 – as a consequence of unprecedented low vacancy levels and, in the case of the West End office market, Central Government's 2010 business rates revaluation of commercial property.

Increasing numbers of office occupiers are therefore migrating to lower cost areas and are using the relocation as a catalyst for change in their working practices and use of technology in order to minimise their property footprint and reduce operating costs. As a consequence, a number of trends are emerging among London based office users, including:

- **choosing buildings that have been designed to accommodate a higher occupancy density** – traditionally office buildings have been constructed to accommodate one person per 107 sq ft / 10 sqm but improvements in design and technology, particularly with regard to air conditioning capacity, coupled with IT hardware that generates less heat, is enabling developers to create buildings capable of accommodating up to 1 person per 87 sq ft / 8 sqm.
- **hot desking** – the sharing of workstations between staff that are not permanently office based. This office occupancy strategy is particularly relevant to management consultancies and sales organisations that employ high numbers of project/field based staff.
- **'agile'/remote working** – increasing numbers of organisations are exploiting the freedom to operate remotely from the office which has been conferred by advances in mobile data / telecoms technology, including the use of laptops, smartphones and tablet computers, which has enabled some occupiers to reduce their property footprint.
- **smaller desk sizes** – ten years ago desks were typically 1600 -1800mm wide. Advances in flat screen technology and the greater use of laptops and tablet computers, coupled with electronic, rather than hard copy, filing means that today's office workforce can work as efficiently with smaller desks of 1400 - 1500mm.
- **cloud technology** – the use of cloud computing technology negates the need to develop dedicated data / telecoms rooms, incorporating expensive supplementary air conditioning systems, and also enables savings to be made in the quantum of floor space to be leased.
- **tenant's office fitting out costs are one of the largest items of capital expenditure associated with an office move.** There are several ways in which these costs can be mitigated, including:
  - leasing space that is being marketed with the previous tenant's fitting out works in situ – although some adaptation may be required, it is often possible to make significant savings by modifying the existing fit out
  - making use of HMRC tax reliefs including Investment and Capital Allowances
  - using tax efficient finance leasing to fund the fitting out works

ISSUES TO ADDRESS WHEN NEGOTIATING A LEASE

We summarise below the key issues that we recommend are addressed in order to secure best value lease terms on office accommodation when negotiating with a landlord:

- **financial components**
  - rent discount
  - rent free period and break option linked rent free periods
  - landlord capital contributions towards any refurbishment / fitting out works that the tenant may wish to undertake
- **limiting exposure to increases in annual running and future "exit" costs by including:**
  - a service charge cap
  - a rent review cap - where the LL is seeking to include a rent review
  - a schedule of condition to record the condition of the office space before the lease is granted – to limit future repairing and dilapidations costs
- **building flexibility into the tenancy by addressing:**
  - the length of lease to be granted
  - the timing and frequency of tenant only lease break options
  - the minimum period of notice required to exercise the break option(s)
  - the scope of the pre-conditions to be complied with in order to exercise the break option
- **security of tenure**
  - exclude landlord break options
  - where landlord break options are to be included, ensure that they can only be exercised on meeting certain pre-conditions, for example, when the landlord wishes to redevelop – as evidenced by placing a demolition or building contract
  - negotiate a lease that is to be granted within the security of tenure and compensation provisions of the 1954 Landlord and Tenant Act – which confers rights on tenants of business premises to a new lease and compensation in the event that the landlord later wishes to redevelop the property or occupy for it's own use.

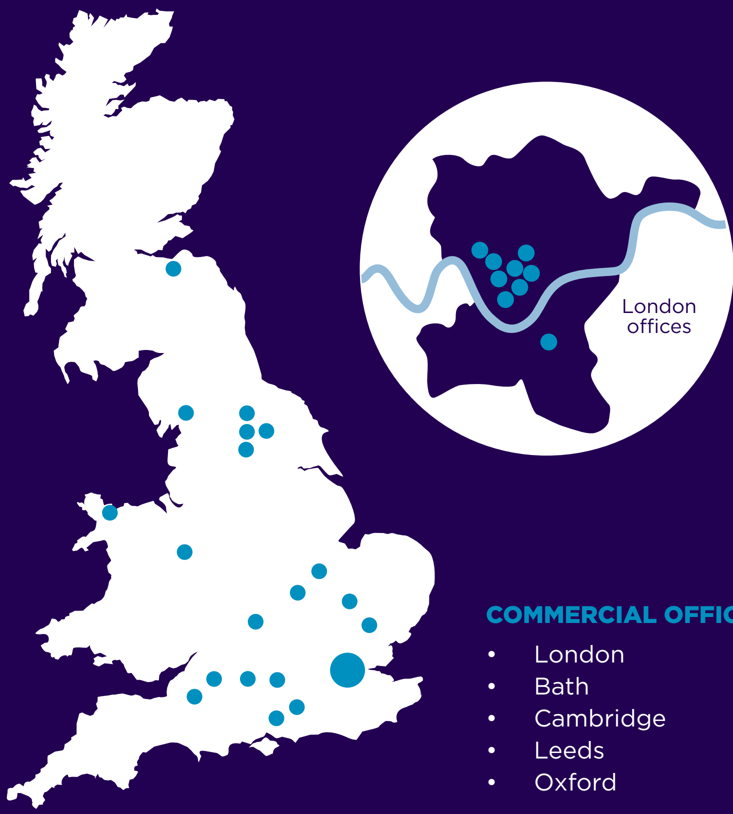
AS OFFICE RENTS CONTINUE TO RISE IN THE UNDER-SUPPLIED CORE CENTRAL LONDON OFFICE MARKETS SUCH AS THE WEST END, MIDTOWN, CITY AND SOUTH BANK, PERIPHERAL SUB-MARKETS SUCH AS DOCKLANDS, STRATFORD AND EAST CITY FRINGE ARE LIKELY TO CONTINUE BENEFITTING FROM OUTWARD MIGRATION AS TENANTS SEEK BETTER VALUE FOR MONEY

THE TENANT ADVISORY TEAM

The Tenant Advisory Team does not provide property consultancy services to landlords. Our tenant representation services include:

- Office search and relocation management services
- Lease and rent review negotiation
- Relocation budgeting and planning
- Repairs/dilapidations assessment and negotiation
- Building, air conditioning and passenger lift surveys
- Business rates analysis and appeal
- Service charge audit

For more data on the Central London office market, office availability, rents and rent free periods and information on budgeting and planning for a lease renewal, rent review or office relocation please contact one of the team.



COMMERCIAL OFFICES

- London
- Bath
- Cambridge
- Leeds
- Oxford

CASE STUDIES

Lease negotiations and relocations 10,000 sq ft+

37,000ft	**Frank Hirth** 236 Gray's Inn Road, WC1
33,000ft	**UK Payments Administration** 2 Thomas More Square, E1
28,000ft	**Warner Bros / Shed Media** 85 Grays Inn Road, WC1
23,000ft	**Nursing & Midwifery Council** Two Stratford Place, E20
17,500ft	**Hackett Limited** The Clove Building, SE1
16,000ft	**Circle Housing** Two Pancras Square, N1
15,000ft	**Hitachi Rail Europe** 40 Holborn Viaduct, EC1
11,000ft	**Salamanca Group** 50 Berkeley Street, W1

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