RESEARCH

The London Office Market Q1 2023

A Guide To Rents, Rent Free Periods & Market Trends

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Carter Jonas

The London Office Market: The Mismatch Between Supply & Demand

Together with legal and financial services, the technology sector has been one of the key drivers of demand for London office space both before and following the COVID pandemic. The longer-term impact of the demise of Silicon Valley Bank on the growth of the global, and London-based, technology sector has yet to be established although it has been reported that at least one significant tech-company letting in London's "tech-belt" has been abandoned as a direct consequence of SVB's failure.

The demise of SVB follows the cost cutting measures that many of the global-tech giants such as Google, Facebook and Twitter have been implementing over the last six or so months, largely in the form for job losses and the offloading of surplus real estate. In London, it is understood that Google is undertaking a strategic review of its operational real estate which is likely to result in a significant volume of space being brought to the market.

The forced takeover of Credit Suisse by UBS, under orders from the Swiss government, a consequence of the impending insolvency of the former, is likely to result in significant job losses at the merged entity both in London and across the globe. There is, therefore, likely to be an appreciable downsizing in the space occupied by UBS's London operations. Other members of the international banking community, HSBC and Barclays, have recently announced plans to significantly reduce their London property footprints – a consequence of the post COVID trend towards hybrid working.

It's Not All Doom & Gloom

However, there is good reason to be optimistic about the future of the London office market: demand overall continues to remain resilient, even if some business sectors are in retrenchment. Social media firm TikTok has recently announced that it is leasing 140,000 sq ft at 150 Aldersgate Street, near Farringdon, in addition to the 88,500 sq ft that it leased in March 2021 at The Kaleidoscope Building at 4 Lindsey Street, situated above Farringdon Elizabeth Line station, as the company continues to expand and create new jobs. The higher education sector is also making its presence felt in the London office market as UK and overseas universities continue the trend towards setting up London campuses to exploit healthy demand from the international student community. York St John University's expansion of its campus at East India Dock, bringing the total occupied to 47,000 sq ft, and New York University's leasing of 75,000 sq ft at 265 Strand in London's "Midtown", are just two recent examples.

10M Population By The Mid-2030s

Research carried out by the Office For National Statistics and the Greater London Authority concludes that by the mid-2030s the population of London is likely to have increased by circa one million to reach ten million. During the same period London-based service sector jobs are forecast to grow by over half a million. There is, therefore, further reason to be optimistic about London's longer term prospects.

Weaker Demand In The Short Term

It is likely that the recent travails of the global banking sector will translate into weaker demand for London office space for the next few quarters as the wider business community takes a "wait and see" approach to establish how the world economy performs. Short term market weakness is likely to offer footloose tenants that are currently actively looking for space an opportunity to secure better rent and rent free period letting packages than might otherwise have been achievable.

While there is a degree of nervousness in the property industry associated with the retrenchment of the global tech sector and the impact of the demise of Credit Suisse and SVB, and the downsizing of other international banks, the forecast offloading of modern, environmentally compliant, space leased by tech businesses will be taking place in an already acutely undersupplied market segment. Further, save for UBS' 5 Broadgate accommodation, much of the space that is being vacated by the banking sector is older accommodation with poor sustainability credentials – just the type of office accommodation that footloose tenants do not want. The mismatch between supply and demand is therefore likely to persist in the short term.

Demand Continues For "Green" Buildings

As outlined in earlier editions of this publication there has, post COVID pandemic, been an acceleration in the structural shift in demand towards new and refitted, Grade A office space with good sustainability credentials. The shift initially being driven, prior to the pandemic, by the desire of employers to create an attractive working environment to underpin recruitment, retention, productivity and wellness policies. Post COVID, the need to encourage employees back into the routine of working from the office, and the increased sensitivity of the business community to demonstrate its environmental credentials by operating from energy-efficient, "green", buildings, has further reinforced demand for best in class, sustainable, office space.

Be Prepared For The EU's CSRD

From 2024 European Union businesses employing more than 500, or with a turnover of more than 40m euros, and EU listed companies, will be required to comply with the EU's Corporate Sustainability Reporting Directive. The Directive requires businesses to set out in their annual financial reports their sustainability, social responsibility, diversity, human rights and anti-corruption policies and to provide evidence of how these policies are being implemented. The knock-on effect of this legislation is that those businesses outside the EU that trade with EU entities, and that wish to maintain trading relations, will almost certainly similarly be required to provide the aforementioned data to their EU-based trading partners in order that the requirements of the CSRD can be complied with.

For service sector businesses, the real estate from which they operate will typically have one of the largest impacts on their sustainability credentials. As a consequence, the EU's introduction of the CSRD is likely to further underpin the shift in demand for energy-efficient buildings that have been developed from recycled and recyclable materials.

Interest Rates & Inflation

With many economic commentators forecasting the imminent peak in the current interest rate cycle, hastened by the recent turbulence in the banking sector and the easing of inflationary pressures by the end of the year, the stabilising macro-economic environment should underpin renewed investment in jobs. This should, in turn, translate into a recovery in demand for office space, albeit that the correlation between the rate of job creation and floor space required has been weakened by the widespread adoption of hybrid working practices.

The Shift Eastwards

The West End of London – in particular the Mayfair, St James's, Marylebone, Fitzrovia and Soho districts – is especially short of available Grade A office stock with good sustainability credentials. Rents in many of these areas for best-in-class space have risen above their pre-COVID levels: rents above £130.00 per sq ft per annum are now firmly established in Mayfair and St James's while rents in "super-prime" locations such as Berkeley Square and St James's Square are now typically around £150.00 per sq ft per annum. Some West End based businesses are therefore extending their property searches eastward to the City, where rents for equivalent quality space are typically £70.00 - £80.00 per sq ft for low / mid-rise space.

The Search For Space That Offers Good Value

For those footloose tenants that are seeking to secure sustainable new and refitted Grade A space at optimal cost, areas such as London Docklands (Canary and Wood Wharfs) would be obviousplaces to focus their property searches, where rents are typically £50.00 - £60.00 per ft per annum for mid-rise space. Transport connectivity to this area of London has improved vastly following the commencement of Elizabeth Line services – just 6 minutes from Liverpool Street and 14 minutes from Bond Street.

Pre-Letting Activity

While the number of planning applications for new office developments and refurbishments is increasing across London, the reality is that it is likely to be 2 – 3 years from the date of receiving planning consent before many of the proposed schemes will be ready to occupy. In the short term, tenants seeking environmentally-friendly Grade A space are therefore likely to continue finding choice limited.

In tandem with the decline in the choice of available good quality, sustainable, buildings across many parts of central London, there has been an increase in pre-letting activity since the last of the COVID lockdowns. An increasing number of occupiers are hedging against the risk of there being no operationally suitable space that fits their floor area requirement by contracting now to lease space that has yet to be built, or is under construction.

Office lettings in the West End during the first quarter of the year have been dominated by pre-lets which include 106,000 sq ft at 25 Baker Street, Marylebone, let to asset manager PIMCO and 83,000 sq ft let to Virgin Media at 3 Sheldon Square, Paddington. In the City fringe, the leasing of 140,000 sq ft at the Verdant building, 150 Aldersgate Street, EC1 to TikTok is another example of a significant pre-let. It is likely that pre-letting activity in the Grade A market segment will increase this year, reflecting the mismatch between availability and demand.

The forecast increase in office vacancy levels that is being underpinned by the pipeline of new office developments that are due for completion during the next couple of years is therefore being eroded by pre-letting activity. Footloose tenants should not therefore assume that operationally suitable space will necessarily be available when the various developments under construction complete: a significant number will have already been pre-let.

The Development Of Sustainable Buildings

Property developer Great Portland Estates' 2 Aldermanbury Square is an example of a building that is being constructed of "green" steel which has been manufactured without the use of fossil fuels and some of the materials from the building that is being replaced are being recycled and used in other construction projects.

The use of timber in building construction is nothing new. Wood not only serves as a store of trapped carbon but can be grown from natural resources without the need to undergo an energy-hungry, high carbon footprint, manufacturing process. Japanese timber company Sumitomo Forestry and Bywater Properties have recently entered into a joint venture to develop timber-framed buildings from sustainable sources and their first building "Paradise", a six-storey office building comprising 63,400 sq ft in Lambeth, south London, is currently under construction.

Planning Policy & The Environment

In a pioneering move, the City of London Corporation is introducing new requirements for property developers to provide data on the carbon impact of new developments to justify the demolition of existing buildings that could be refurbished. Glass, concrete and steel, the key components of modern office buildings, are hugely energy intensive to manufacture - in sharp contrast to the "embedded carbon" in existing structures that could be retained and refitted.

Reasons To Be Optimistic

As can be seen from this Q1 2023 commentary town planners, property developers, investors, legislators and occupiers are each, in their own way, driving the trend towards the development of a new generation of environmentally-friendly office buildings. In particular, the UK's and EU's environmental legislation is making a significant proportion of the European office market redundant while, at the same time, catalysing the shift in demand towards sustainable buildings. In London, in the short term, the mismatch between supply and demand is likely to intensify, reflecting the lag in the speed at which supply is able to respond to the structural shift in demand. However, there is good reason to be optimistic about the planet's future.

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Rents and Rent Free Periods

Advertised Rents

Rents for central London Grade A office space during the first quarter of this year have remained broadly static as a consequence of subdued demand in the aftermath of former Prime Minister Liz Truss' "mini" budget in the Autumn last year. The fallout from the failure of Silicon Valley Bank, the forced acquisition of Credit Suisse by UBS and the Bank of England's continued tightening of monetary policy, reflecting the inflationary macro-economic environment, are also factors that have contributed to undermine demand and stifle rental growth.

It is likely that rents across much of London, for new and refitted Grade A space, will remain flat for the next few quarters, reflecting weaker demand.

Rents for second-hand space with poor environmental credentials are likely to weaken for much of this year reflecting the shift in demand towards new and refitted, energy efficient, Grade A accommodation that is capable of underpinning employer's recruitment, retention, wellness and environmental policies.

Please refer to Table 2 which provides an overview of current typical landlord's advertised rents for the various London office sub-markets.

Rent Discounts

Discounts of 1 - 4% are now more typically being negotiated on landlord's advertised rents for new and refitted, environmentally compliant, Grade A space – with discounts at the higher end of the range more common in the City of London, City fringe and Docklands sub-markets, where vacancy rates are higher. Contrast with discounts of 2.5 – 6% that were typical during the first quarter of 2022.

Rent Free Periods

Table 1 – Typical Rent Free Periods By Sub-Market – Q1 2023
New / Refitted & Refurbished Grade A Space

Location	Typical Rent Free Period (lettings over 5,000 sq ft)	
	5-year lease	10-year lease
City of London - St Paul's, Bank, Liverpool Street, Cannon Street	12 - 14 months	24 - 27 months
City Fringe North - Shoreditch, Clerkenwell, Farringdon	10 - 13 months	22 - 26 months
City Fringe East - Aldgate East, Spitalfields	12 - 15 months	24 - 28 months
Midtown - Bloomsbury, Holborn, King's Cross, Covent Garden	9 - 12 months	22 - 25 months
West End - Mayfair, St James's, Marylebone, Fitzrovia, Soho, Victoria, Paddington	8 - 12 months	20 - 24 months
South Bank - Waterloo, Southwark, London Bridge	9 - 12 months	21 - 25 months
East London - Docklands - Canary Wharf, Wood Wharf	13 - 16 months	26 - 32 months
East London - Stratford	13 - 15 months	25 - 28 months
West London - Hammersmith, White City, Chiswick	12 - 15 months	24 - 28 months
South West London - Vauxhall, Battersea	11 - 15 months	22 - 26 months

Source: Carter Jonas Research

By comparison, larger discounts of up to 10%, and more, on landlord's advertised rents are not unusual for low quality buildings with poor energy efficiency ratings.

Rent Free Periods

In tandem with underpinning rental growth, low levels of vacancy in the new and refitted Grade A office market segment in many parts of central London have fostered a compression in rent free periods, following the recovery in demand since the last of the COVID lockdowns in 2021. Since Q1 2022 rent free periods have typically declined by 1 - 2 months for a 5 – 10 year lease. Docklands is the exception, where rent free periods have increased slightly from a year ago, reflecting weaker demand for that sub-market and higher levels of vacancy relative to other, more central, sub-markets.

Rent free periods for low grade office space with poor environmental credentials have shifted little over the last twelve months.

Table 1 provides a summary of typical rent free periods for new and refitted Grade A space for each sub-market, prevailing during the first quarter of 2023.

Over the next few quarters it is quite likely that rent free periods across central London for new and refitted Grade A floor space will remain static. In some sub-markets including the City, Docklands and West London, where there is a better balance between supply and demand, rent free periods may expand by 1 -2 months as landlords use rent free period incentives to maintain headline rental levels in the wake of weaker demand.

"Canary Wharf and Wood Wharf, in London's Docklands, continue to offer good value where sustainable new and refitted Grade A space is available at rents of between £50.00 and £60.00 per sq ft per annum."

Summary of Forecast Market Trends

A summary of the key current and forecast trends in the London office market is provided below:

Advertised Rents

- advertised rents for best in class Grade A space are likely to remain flat across much of London at least for the next two quarters, reflecting weak economic growth and subdued demand

Rent Discounts

- the discounts that can be negotiated on advertised rents for new and refitted, well located, Grade A space may expand slightly from their current level of 1 - 4% during the next two quarters as the market adjusts to weaker demand

Rent Free Periods

- rent free period incentives for environmentally compliant Grade A space are likely to remain broadly static during the next two quarters and may expand slightly in those sub-markets where there is a better balance between supply and demand

Greater Lease Flexibility

- continued demand for greater lease flexibility – shorter leases and more frequent break options

Demand For Good Quality Office Space

- continued demand for good quality, energy-efficient, environmentally-friendly, Grade A office space – to reinforce return to the office, workforce wellbeing, recruitment, retention, productivity and environmental strategies

"Office rents for new best in class Grade A space in prime West End locations including Marylebone, Mayfair and St James's are typically £100 - £150 per sq ft per annum in contrast to the City core where rents are £70.00 - £80.00 per sq ft for equivalent quality mid-rise space. "

Downsizing

- a continuing trend towards businesses downsizing their real estate footprint, reflecting the adoption of new "hybrid" work from office / home operating practices

The bargaining position of landlords of Grade A space

- a gradual weakening in landlord's bargaining position in lease negotiations is likely for much of the year reflecting weaker demand, except in areas of particularly low Grade A vacancy - in the West End and Midtown sub-markets

Office Leasing Activity

- a steady decline over the next two quarters in the year-on-year levels of letting activity, reflecting weaker demand

Serviced Offices

- continued demand for serviced and co-working space from established businesses that wish to lease short term space, pending a move to longer term conventional office space, following a return to a more certain economic climate

Assessing A Building's Sustainability Credentials

Research demonstrates that real estate consumes circa 40% of global energy annually and contributes to approximately 20% of carbon emissions. Operating from energy-efficient, sustainable, accommodation is one of the key ways that a business can ameliorate its impact on the environment.

To assist footloose tenants in their quest to identify accommodation that will align with their adopted environmental policies a number of building certifications have been developed.

Energy Performance Certificates

Introduced under the UK Government's Minimum Energy Efficiency Standards (MEES) legislation, energy performance certificates (EPCs) are helpful in demonstrating whether a building is well insulated and fitted with building services, including heating and air conditioning plant, that are energy-efficient.

The Government's proposed phased tightening of the existing MEES regulations will mean that from 1 April 2027 landlords, and tenants with surplus space, will not be able to let or derive rental income from accommodation that has an EPC rating below C. At present a property must have an EPC rating of at least E before it can be offered to let. With effect from 1 April 2030 it will be necessary for commercial properties to have an EPC rating of A or B.

It is, however, proposed that some exemptions to the proposed new regulations will apply, providing that certain qualifying criteria are met. For example, some listed buildings will be exempt if the works to upgrade the energy efficiency rating of the property will adversely affect the architectural features of the building. Listed and non-listed buildings may also be exempt if the cost of the works to upgrade the property to render it compliant with MEES regulations exceed any savings in energy costs over a seven year period.

Depending upon a building's current energy performance rating, the switch to using energy generated from renewable resources, instead of fossil fuels, can sometimes be sufficient to boost a building's EPC rating to the extent that it will be compliant with the proposed tighter energy performance regulations.

Despite the fact that the proposed tighter energy performance regulations have yet to be introduced, the mere fact that they have been proposed is already having an impact on the office market. Footloose tenants that are currently seeking alternative premises are typically focussing their property searches on buildings that will be compliant with the new proposals, ahead of their introduction, to future-proof their ability to assign / transfer their lease or sub-let space that may later be surplus to requirements.

Energy performance certificates have a ten year life-space from the date of issue. It is a legal requirement for those leasing office office space to maintain a valid, in-date, EPC and to include in the marketing material details of the energy performance rating of the accommodation, which should assist footloose occupiers in avoiding properties that will be non-compliant when the new MEES regulations come in to force.

BREEAM & LEED

Other real estate environmental accreditations include BREEAM (British) and LEED (American), which are gradually being adopted internationally by property developers and investors, each of which include an assessment of a building's design and use of materials to benchmark its sustainability credentials.

Buildings that incorporate environmentally-friendly features such as roof gardens, solar panels, wind turbines, bike racks and shower facilities (to discourage the use of motor- based commuting), energy saving devices and mechanisms to harness and recycle rainwater will score high ratings. The use of recycled and recyclable building materials and materials derived from sustainable sources will also boost a building's BREEAM and LEED scores.

NABERS

In Australia, the NABERS real estate accreditation has been developed and is, similarly, being adopted internationally by real estate owners and developers to complement BREEAM and LEED accreditations. Unlike the latter, NABERS is an annually renewable accreditation and measures the environmental performance of a building and how efficiently it is being managed, with particular emphasis on energy and water consumption and waste recycling.

Landlords are responding to the structural shift in demand for sustainable accommodation by obtaining the aforementioned accreditations, details of which will typically be included in marketing material.

WELL

The WELL standard is another real estate accreditation that is complementary to the BREEAM, LEED and NABERS certifications. With its emphasis on the wellbeing of the users of real estate, a building's WELL accreditation will be concerned with the following:

- air and water quality (including drinking water)
- building design in so far as it affects / promotes the wellbeing of its occupants
- lighting levels and light quality
- the existence of any hazardous materials

> "The impact of the European Union's Corporate Sustainability Reporting Directive on those based outside the EU, that trade with EU businesses, is likely to reinforce demand for environmental-friendly Grade A office space in non-EU countries"

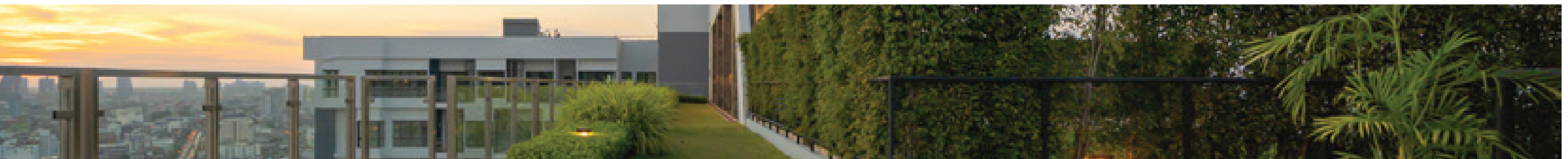


Table 2 – The London Office Market – Typical Landlord's Advertised Rents Q1 2023

£ per sq ft per annum | space over 5,000 sq ft | UF= Upper Floors

Location	Grade A		Grade B
	New/Refitted	Refurbished	Refurbished
City			
Prime - Bank, Leadenhall Street	£68.50 - £80.00 (UF = £82.50 - £110.00)	£57.50 - £67.50 (UF = £70.00 - £85.00)	£42.50 - £52.50
Secondary - Blackfriars, Aldgate	£62.50 - £72.50 (UF = £75.00 - £90.00)	£47.50 - £59.50 (UF = £65.00 - £77.50)	£38.00 - £45.00
City Fringe			
North - Shoreditch, Clerkenwell	£67.50 - £80.00 (UF = £82.50 - £92.50)	£55.00 - £65.00	£38.00 - £55.00
North West - Farringdon, Smithfield	£72.50 - £87.50 (UF = £90.00 - £97.50)	£57.50 - £69.50	£40.00 - £56.00
East – Spitalfields	£67.50 - £75.00 (UF = £77.50 - £82.50)	£52.50 - £65.00	£37.50 - £46.50
East – Aldgate East, Wapping	£49.50 - £59.50 (UF = £60.00 - £65.00)	£38.00 - £48.50	£34.00 - £37.00
South Bank			
Waterloo, Southwark, London Bridge	£67.50 - £75.00 (UF= £77.50 - £95.00)	£59.50 - £66.50 (UF = £67.50 - £75.00)	£42.50 - £58.50
Battersea, Nine Elms, Vauxhall	£55.00 - £67.50	£45.00 - £53.50	£37.50 - £43.00
East London			
Docklands Prime – Canary Wharf & Wood Wharf	£47.50 - £60.00 (UF = £62.50 - £72.50)	£32.50 - £42.50 (UF = £45.00 - £50.00)	£27.50 - £35.00
Docklands Secondary – Crossharbour	£32.50 - £39.50	£27.50 - £32.50	£22.50 - £27.50
Stratford	£45.00 - £49.50	£35.00 - £45.00	£22.50 - £29.50
West End			
Central – Mayfair, St James's (Prime)	£110.00 - £140.00 (UF = £145.00 - £155.00)	£85.00 - £105.00	£67.50 - £77.50
Central – Mayfair, St James's (Secondary)	£89.50 - £100.00	£72.50 - £88.50	£65.00 - £75.00
North – Euston	£72.50 - £85.00	£57.50 - £67.50	£42.50 - £52.50
North East – Fitzrovia	£87.50 - £97.50	£75.00 - £85.00	£52.50 - £65.00
North West – Marylebone	£88.50 - £100.00 (UF = £102.50 - £120.00)	£77.50 - £87.50	£60.00 - £70.00
South – Victoria, Westminster, Haymarket	£75.00 - £89.50 (UF = £90.00 - £95.00)	£65.00 - £72.50	£42.50 - £57.50
South West – Knightsbridge	£90.00 - £115.00	£75.00 - £87.50	£62.50 - £72.50
East – Soho, Regent Street, Leicester Square	£85.00 - £97.50 (UF = £97.50 - £110.00)	£72.50 - £85.00	£52.50 - £65.00
West – Paddington	£70.00 - £79.50 (UF = £82.50 - £90.00)	£55.00 - £66.50	£42.50 - £52.50
Midtown			
North – King's Cross	£75.00 - £87.50	£62.50 - £72.50	£47.50 - £55.00
South – Covent Garden	£75.00 - £85.00 (UF = £87.50 - £92.50)	£60.00- £72.50	£47.50 - £55.00
East – Holborn	£62.50 - £75.00 (UF = £77.50 - £82.50)	£52.50 - £60.00	£40.00 - £47.50
West – Bloomsbury	£77.50 - £90.00	£65.00 - £75.00	£47.50 - £57.50
South West London			
Chelsea	£77.50 - £90.00	£65.00 - £75.00	£47.50 - £60.00
West London			
Kensington	£75.00 - £110.00	£60.00 - £72.50	£45.00 - £55.00
Hammersmith	£52.00 - £58.50	£40.00 - £50.00 (UF = £55.00 - £57.50)	£32.50 - £42.50
White City	£46.50 - £56.50	£40.00 - £45.00	£32.50 - £40.00
Chiswick	£47.50 - £55.00	£37.50 - £46.00	£32.50 - £37.50
Ealing	£45.00 - £55.00	£37.50 - £42.50	£30.00 - £35.00

Grades of Office Accommodation

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

Grade A

Space fitted with air conditioning & passenger lift facilities & fully accessible raised floors for data / telecoms cable management

Grade B

Accommodation that typically incorporates under floor or perimeter trunking for data / telecoms cable management, rather than raised floors, and / or air cooling facilities, instead of an air conditioning system that dehumidifies & draws fresh air in to the building

Refitted space

Accommodation where the entire building, including the common parts, has been refitted and is "as new", incorporating new building services, including lighting, air conditioning and passenger lift facilities

Refurbished space

Premises where the existing building services have been overhauled, rather than replaced with new systems

Source: Carter Jonas Research

The London Office Market

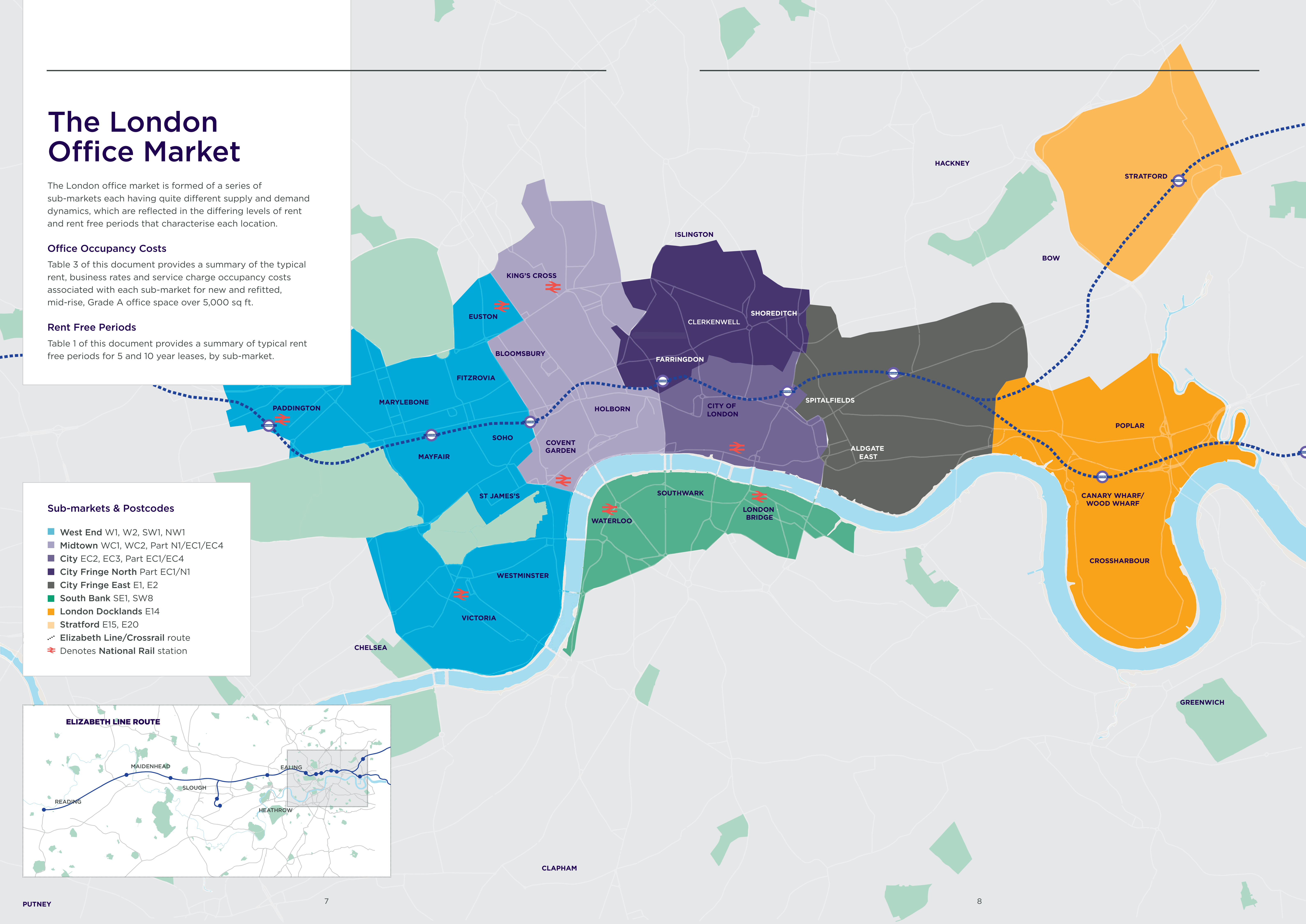
The London office market is formed of a series of sub-markets each having quite different supply and demand dynamics, which are reflected in the differing levels of rent and rent free periods that characterise each location.

Office Occupancy Costs

Table 3 of this document provides a summary of the typical rent, business rates and service charge occupancy costs associated with each sub-market for new and refitted, mid-rise, Grade A office space over 5,000 sq ft.

Rent Free Periods

Table 1 of this document provides a summary of typical rent free periods for 5 and 10 year leases, by sub-market.



Principal Office Occupation Costs

To assist those tenants that are planning to lease new or refitted, energy-efficient, Grade A accommodation, we set out in the table below estimates of the typical rent, business rates and building service charge annual occupancy costs, as at 1 April 2023.

Since the first quarter of 2022, service charge costs have typically risen by 20 – 25%, reflecting the impact of rising energy costs.

The cost estimates in the table include business rates costs following the introduction of the 2023 business rates revaluation of commercial property in England and Wales, which took effect from 1 April. Consequently, business rates costs in the City, City fringe and South Bank sub-markets have risen, typically by over 10%. By contrast, business rates cost increases have been more modest in many of the West End and Midtown sub-markets. Transitional relief is available to businesses that are facing a significant increase in their rates costs and it is also possible to appeal the new 2023 rateable values. The Carter Jonas Team can advise further.

Table 3 – Comparison Of Rent, Business Rates and Service Charge Costs By Sub-Market – 1 April 2023

Typical costs per sq ft per annum for new and refitted mid-rise Grade A space over 5,000 sq ft

Sub-market	Rent	Business Rates	Service Charge	Total
City of London – Bank, Leadenhall Street	£75.00	£31.75	£14.00	£120.75
City Fringe North - Shoreditch, Clerkenwell	£72.50	£25.25	£13.00	£110.75
City Fringe North West - Farringdon, Smithfield	£85.00	£26.00	£13.00	£124.00
City Fringe East - Aldgate East	£55.00	£23.50	£13.00	£91.50
City Fringe East - Spitalfields	£72.50	£26.50	£13.00	£112.00
South Bank - Southwark, London Bridge	£72.50	£27.00	£13.00	£112.50
East London - Canary Wharf	£55.00	£16.75	*£18.25	£90.00
East London - Crossharbour	£35.00	£12.00	£13.00	£60.00
East London - Stratford	£47.50	£16.50	*£12.00	£76.00
Midtown West - Bloomsbury	£85.00	£33.00	£13.00	£131.00
Midtown East - Holborn	£70.00	£31.00	£13.00	£114.00
Midtown North - King's Cross	£85.00	£35.00	£13.00	£133.00
Midtown South - Covent Garden	£80.00	£35.00	£13.00	£128.00
West End Central - Mayfair, St James's	£125.00	£54.25	£14.00	£193.25
West End North - Marylebone	£98.50	£41.50	£13.00	£153.00
West End North - Fitzrovia	£95.00	£39.00	£13.00	£147.00
West End South - Victoria, Westminster	£77.50	£38.50	£13.00	£129.00
West End West - Paddington	£77.50	£27.00	£13.00	£117.50
West End East - Soho	£95.00	£40.50	£13.00	£148.50
West London - Hammersmith	£56.00	£24.00	£12.50	£92.50
West London - White City	£53.00	£22.50	£12.50	£88.00
South West London - Battersea, Nine Elms	£62.50	£22.00	£12.50	£97.00

Source: Carter Jonas Research

Please refer to the map overleaf which illustrates the various London office sub-markets.

Notes

- Rents are typical landlord's advertised rents and exclude the value of rent free periods
- Business rates cost estimates include the Crossrail levy
- * includes estate charge
- Total costs are estimates and exclude building insurance and tenant's own utilities costs
- Rents for the upper floors of tower buildings will typically command a premium of circa 15 – 30% above those illustrated in the table
- The cost estimates in the table are provided for guidance only. Actual occupancy costs and will vary from building to building

Reducing Real Estate Costs

A lease expiry or break option presents an ideal opportunity for a business to reduce its real estate costs by enabling:

- new lease terms to be negotiated - including a revised rent and a rent free period
- potential downsizing of the floor area occupied at the existing premises
- a relocation to smaller / lower cost / better quality, environmentally-friendly, premises

Negotiating A Cost-Effective, Tenant-Friendly, Lease

The principal terms set out below should form the bedrock of the lease negotiations, in order to cap future lease liabilities and to achieve the objective of securing a cost-effective, tenant-friendly, tenancy:

- a rent that reflects the current economic climate
- a rent free period, including additional post break option rent free periods
- landlord's capital contributions towards any refurbishment / fitting out works
- a service charge cap – to limit future increases in real estate costs
- the inclusion of regular tenant-only break options – to build in lease flexibility
- a cap on the tenant's repairing and removal of fixtures and fittings exit obligations
- tenant-friendly rent review valuation provisions (leases of 5 years, or longer)

Reducing The Property Footprint

Shrinking the property footprint occupied is another effective way of reducing exposure to rent, business rates and service charge costs.

Whether staying-put and downsizing or relocating to smaller premises, the most effective floor area reduction strategies will typically incorporate:

- the adoption of new operating practices such as "hybrid" working from home and the office, adopting a rota system - to reduce desk-count
- a greater emphasis on use of the office as a "drop-in when required" collaboration hub
- the use of smaller desks and less office furniture
- a move to "cloud" based data storage and the digitisation of documents – to negate the need to allocate floor space for a server room and archive storage

Minimising Relocation Costs

If the decision is taken to move a relocation cost saving plan can be devised to preserve working capital and minimise the negative impact of the office move on cashflow.

A relocation cost saving plan would typically include:

- focusing the property search on "plug-in-and-go" ready fitted out space that includes meeting rooms, senior manager's offices, kitchen facilities, data / telecoms infrastructure and furniture
- where non-ready fitted out space is to be leased, tendering the fitting out contract to drive down interior design and construction costs
- making use of HMRC capital allowances tax breaks (where paying UK corporation tax) to reduce fit out costs
- employing a suitably experienced building surveyor to challenge, and negotiate, the landlord's lease exit liabilities claim relating to the existing premises
- developing a detailed relocation timetable to benchmark and regulate the speed of the project, to synchronise the move, so that overlap rent, business rates and service charge costs are minimised

The Carter Jonas Tenant Representation Team can provide further advice on the various issues outlined above.

Key Leasing Transactions During Q1 2023

As illustrated below in Table 4, take-up during the first quarter of 2023 has been dominated by the lettings of energy-efficient, new and refitted Grade A space, reflecting the continuing shift in demand away from low grade accommodation. The lettings data underscores the high priority that occupiers are placing on return to the office, recruitment, retention, wellness and environmental issues when selecting office space. Significantly, many of the lettings have been pre-lets.

Table 4 – Key Office Lettings – Q1 2023

Sub-market	Tenant	Business Sector	Property	Floor Area (sq ft)
City of London	Dentons	Legal Services	1 Liverpool Street, EC2	80,000
City Fringe North - Shoreditch	Frontier Economics	Business Services	Worship Square, 65 Clifton Streeet, EC2	32,735
City Fringe North - Shoreditch	Buro Happold	Civil Engineering	The Featherstone Building, 66 City Road, EC1	31,100
City Fringe North West - Farringdon	TikTok	Social Media	150 Aldersgate Street, EC1	140,000
South Bank - Southwark	Fora	Flexi-Offices	The Blue Fin Building, 110 Southwark Street, SE1	43,300
South Bank - Southwark	The Carbon Trust	Business Services	Arbor, Bankside Yards, SE1	13,800
Midtown - Covent Garden	Page Group	Business Services	80 Strand, WC2	40,000
Midtown - Covent Garden	ECI Partners	Financial Services	80 Strand, WC2	13,000
West End - Marylebone	PIMCO	Financial Services	25 Baker Street, W1	106,000
West End - Paddington	Virgin Media O2	Telecoms	3 Sheldon Square, W2	83,000
West End - Victoria	WeWork	Flexi-Offices	123 Buckingham Palace Road, SW1	27,000
West End - Mayfair	Hayfin	Financial Services	65 Davies Street, W1	22,947
West End - Mayfair	UPL	Business Services	80 New Bond Street, W1	14,218
West London - Kensington	Essilor Luxottica	Healthcare	The Kensington Building, 1 Wrights Lane, W8	22,931
West London - Kensington	Manchester United	Leisure - Sport	The Kensington Building, 1 Wrights Lane, W8	16,000
South West London - Nine Elms	Omega Pharma	Pharmaceuticals	One Embassy Gardens, SW8	21,000
South West London - Chelsea	Oakley Capital	Financial Services	Holbein Gardens, Sloane Gardens, SW1	26,500
East London - Docklands	York St John University	Education	The Export Building, 2 Clove Crescent, East India Dock, E14	23,000
North London - Camden	Moo	Media	Labs Triangle, Chalk Farm Road, NW1	18,500

Source: Carter Jonas Research

Comparing The Costs Of Relocating & Staying Put

The existence of a lease break option or expiry presents a tenant with an opportunity to assess its real estate options which could include:

- using the existence of the break option / expiry, and the option of relocating, as a bargaining counter to negotiate a new tenancy that offers better value and more tenant-friendly lease terms
- relocating to alternative premises – which may offer better value and the ability to downsize, or operate from larger premises to accommodate growth, as well as the opportunity to create a new, vibrant and engaging work environment which will underpin ESG policies and return to the office, workforce wellbeing, recruitment, retention and productivity strategies

Stay-put / Relocate Property Options Cost Appraisal

In order to assess and compare the costs of staying put or relocating, and to assist with obtaining Board approvals for budgets, it would be prudent to undertake a stay put / relocate property options cost appraisal. The appraisal will also identify where the largest cost savings can be made.

A property options cost appraisal would typically include an analysis of the following, taking into account the value of any rent free periods and the landlord's capital contribution incentives that can be negotiated as part of the letting package:

- **the one-off capital expenditure associated with staying put including:**
  - transaction costs – solicitor's and property consultant's fees and stamp duty land tax
  - refurbishment costs – the costs of any upgrade / reconfiguration works that the tenant may wish to make to its existing office space
  - the cost of funding the capital expenditure
- **the capital costs associated with moving – including:**
  - the exit costs associated with the existing premises – repairs / dilapidations
  - fitting out costs at the selected premises, including furniture and any upgrades to data / telecoms hardware, in the absence of finding suitable ready fitted out space
  - the overlap rent, business rates and service charge costs payable from the date of commencement of the lease on the selected premises to the date of expiry of the lease on the existing accommodation
  - transaction costs – solicitor's, property consultant's and building surveyor's fees and stamp duty land tax
  - the cost of funding the capital expenditure
- **the annual running costs of the existing premises, subject to the new lease, which will include:**
  - the negotiated rent
  - business rates
  - building service charge and insurance premium contribution
  - utilities costs
- **the annual running costs of alternative premises –** which will account for the same variables, as detailed above

Further information on carrying out a stay put / relocate property options cost appraisal is available on request from the Carter Jonas Tenant Representation Team.

The Serviced Office & Co-Working Sector

The London co-working and serviced office sectors have continued to flourish during the first quarter of 2023 as an increasing number of businesses take a "wait and see" approach to the movements in the UK and world economies and lease short term serviced / co-working space before committing to leasing longer term accommodation on "conventional" leases.

This trend is likely to continue until a sustained pattern of economic growth manifests itself.

Demand for "flexi" office accommodation is translating in to higher profits for the likes of IWG, the owner of the "Regus" and "Spaces" brands, which has recently announced its year-end results.

In a further display of confidence in the co-working and serviced office sector, WeWork has resumed its growth strategy after a hiatus of several years, by recently committing to a letting of 27,000 sq ft at 123 Buckingham Palace Road in Victoria.

Serviced / Co-working Office Space - The Pros & Cons

The key advantages of serviced / co-working office space are that it is "cash-flow friendly" and offers a high degree of lease flexibility – enabling a relocation to more permanent accommodation to be effected at short notice.

"Demand for serviced and co-working office space is continuing to prove resilient driven, in part, by those businesses seeking a temporary central London "hub" to provide a base for client meetings and to support collaborative working between teams, pending a move later, in more certain economic times, to longer term, conventional, office space."

In detail, serviced / co-working space offers the following advantages:

- Ready fitted out with data / telecoms infrastructure and furniture – therefore little or no capital expenditure
- Enables the level of working capital available for investment in the business to be maximised
- Cashflow-friendly
- A quick, plug in and go, accommodation solution
- Typically no dilapidations / repairing / exit costs – a contribution to which is usually reflected in the rent payable
- Short form service agreement that can be issued and signed within a matter of hours – no complicated, lengthy, real estate lease requiring the advice of a real estate lawyer
- The ability to expand and contract quickly in response to changes in market conditions
- No stamp duty land tax payable on the grant of the service agreement

However, serviced / co-working office space is not suitable for all businesses, especially those that require a high degree of data security such as private client wealth managers and law firms, or those businesses that wish to stamp their own brand on their office space.

The London Office Investment Market

A summary of the latest trends in the London office investment market is set out below:

- Investment in Central London totalled £1.69bn for the first quarter. This was down 68% year on year and 39% below the five-year quarterly average.
- The City of London recorded the highest investment among the submarkets. The City investment totalled around £1.2bn and accounted for just above 70% of the total in Central London. In contrast, West End recorded just above £100 million in the first quarter, which was the lowest quarter for office investment in the West End for more than a decade.
- The sub markets which usually attract debt backed buyers, such as the South Bank, have seen the lowest traded volumes with yields moving out further than the West End sub-market which typically attracts overseas cash buyers.
- Investor demand continues to focus on prime assets in core locations with strong ESG credentials.
- Notable transactions include the sale of St Katherine Docks to CDL for £395m, the sale of 60 Gracechurch Street to Obayashi for £140m and the purchase of 1 New Street by ChinaChem for £350m.
- Transactional volumes remain low as there continues to be more buyers than sellers. The high cost of finance and inflation plays on buyers and sellers minds resulting in decisions being deferred and delayed until market conditions stabilise.
- Despite the cautious environment, yields are expected to stabilise and in some cases contract, particularly for prime assets, during the second half of the year. We are also expecting transactional volume levels to recover. Much of the investor interest is expected to come from overseas, in particular from Asia and private equity backed investors from the US.

The Tenant Representation Team

Our tenant representation services include:

- Office space search & cost appraisal
- Break option linked lease re-negotiation
- Workplace design & floorspace re-configuration
- Marketing & leasing services – surplus space
- Serviced & co-working property searches and negotiations
- Office move management
- Lease renewal negotiation
- Relocation budgeting & planning
- Lease & rent review negotiation
- Repairs/dilapidations cost assessment & negotiation
- Building, air conditioning & passenger lift surveys
- Business rates analysis & appeal
- Service charge audit

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

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Our Experience

Lease negotiations and relocations 10,000 sq ft+

43,000 sq ft
UK Payments Administration
2 Thomas More Square, E1

39,000 sq ft
Care Quality Commission
151 Buckingham Palace Road, SW1

28,000 sq ft
Warner Bros/Shed Media
85 Grays Inn Road, WC1

27,000 sq ft
Reinsurance Group of America
22 Bishopsgate, EC2

17,500 sq ft
Hackett Limited
The Clove Building, SE1

16,000 sq ft
Circle Housing
Two Pancras Square, N1

15,000 sq ft
Hitachi Rail Europe
40 Holborn Viaduct, EC1

11,000 sq ft
Salamanca Group
50 Berkeley Street, W1

The data in this document is provided to illustrate the key trends in the London office market. We recommend that the advice of an experienced property consultant is sought where a specific property transaction is being contemplated before any irreversible decisions are made.