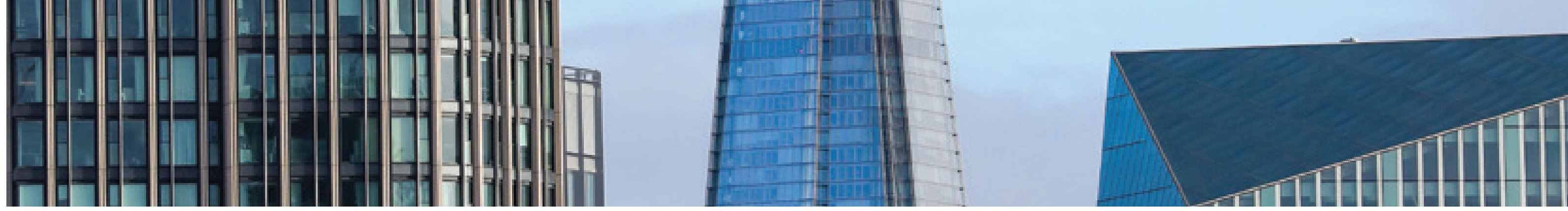
RESEARCH

The London Office Market Q4 2022

A Guide To Rents, Rent Free Periods & Market Trends



Recruitment & Climate Change Issues Continue To Shape Demand For London Office Accommodation

The economic fall-out from the short-lived Liz Truss premiership has done little to arrest demand for environmentally compliant Grade A central London office space – which has been underpinned by the restoration of political and economic stability following the appointment of Rishi Sunak as Prime Minister.

With many London-based businesses operating internationally, with revenues that are not necessarily reliant on the performance of the UK economy, domestic politics appears to play a less important role in influencing the investment decisions of those enterprises based in London.

The resurgence in inflation during 2022 and the consequent increases in interest rates is certainly an unwelcome addition to the operating costs of the business world but, as many economic commentators have pointed out, inflation should ease off later in 2023 as the 2022 cost increases in goods and services start to drop out of the various indices that measure UK inflation. Interest rates are also likely to peak later in the year, conferring a more stable environment upon which businesses can base their investment and recruitment decisions.

People and Property

Collectively, people typically represent the highest operating cost of most businesses, with real estate overheads coming a close second. Both cost variables used to be inextricably linked. In a pre-COVID world it would typically be the case that with increased headcount came a requirement for increased floorspace. However, in the post-pandemic era in which many employers have embraced more flexible operating practices, in particular working from home for part of the week, rising headcount does not necessarily translate into a requirement for more floor space.

Some employers are, very sensibly, "sweating" their real estate and adjusting their operating policies accordingly, as headcount increases, rather than investing in a move to larger office space.

Exceptions To The Rule

However, as has been stated in earlier editions of this publication, not all businesses are well suited to the "hybrid" operating model, especially those that are highly reliant on the flow of information between individuals and teams to aid innovation.

Hybrid working is also not conducive to advancing the training of junior members of staff – the life-blood of the future growth of any organisation. The legal profession is a case in point and it therefore comes as little surprise that this sector of business has been the key driver of demand for office space since the end of the COVID lockdowns. Indeed, since Q4 2021, there has been at least one letting in central London in excess of 100,000 sq ft to a law firm during every quarter.

Trends In Downsizing

In a bid to reduce real estate / operating costs, many businesses are, very prudently, using their forthcoming lease break option or expiry as an opportunity to reduce their property footprint.

However, there does not seem to be a "one-size-fits-all" formula that is being applied by the business community in order to assess the extent to which a reduction in floor space can be achieved. The scope to downsize tends to be business-specific, dictated by operating policies and forecast changes in headcount.

Based on the latest data collected by Carter Jonas, a 30 – 40% reduction in property footprint is not unusual.

Recruitment and The Environment

Despite downbeat forecasts on the performance of the UK economy for 2023, the fact remains that unemployment across the UK is low. Employers in many business sectors in London are continuing to struggle to recruit the brightest and the best which is stymying the ability of many to grow their business and enhance business performance.

This employment trend manifested itself before the pandemic and, at that time, the more "street-wise" businesses recognised the importance of real estate as a recruitment tool in providing an attractive, vibrant, work environment. Employers are continuing to adopt this strategy but, in a very subtle twist to an established trend, are focussing their attentions on energy-efficient buildings that are constructed from recycled / recyclable materials, that reinforce their green credentials and underpin the wellbeing of their employees.

A New Generation Of Office Buildings

Architects, developers and property investors are responding to the changing patterns in demand for office space by creating a new generation of buildings that address the recruitment and environmental issues referred to above. Air conditioning and lighting systems are the two most energy-hungry elements of any office building. The development and use of LED lighting is having a hugely beneficial impact on helping to reduce energy consumption in the commercial property sector.

In a break with tradition, Mitsubishi Estate and Stanhope, the developers of the 570,000 sq ft, 50 storey 8 Bishopsgate scheme in the City of London, have designed the building so that the air conditioning plant can be operated, and switched off, independently on each floor. This innovative design has shifted control and responsibility for energy usage away from the landlord to the tenant and, in the process, should help significantly to reduce energy usage, reflecting the different working patterns of the various tenants that will be operating from the building when it is completed.

The building also incorporates "wellness" features including communal terraces giving those working at the property the opportunity to have a break, unwind and take in the views across London.

Supply & Demand

The disruption in the property development and refurbishment pipeline caused by the COVID pandemic has interrupted the supply of new and refitted office space coming to the market. A supply "pinch-point" is now emerging caused by the slow, but confident, take-up of new Grade A space following the ending of the various lockdowns in mid 2021. It is likely to be 2025, at the earliest, before the imbalance between supply and demand will begin to be addressed as new developments currently under construction reach completion.

Those footloose tenants seeking Grade A space, with good green credentials, in the West End, Midtown and South Bank sub-markets are likely to find choice in all size ranges quite limited. The same comments apply to those seeking office space on the upper floors of City tower buildings.

The laws of supply and demand are most pronounced in areas of low vacancy. Despite the current uncertain macro-economic climate, advertised rents on some of the best in class Grade A buildings have been gradually rising in tandem with a contraction in rent free periods. While there may, over the next few quarters, be a weaking in these trends, reflecting a slackening in demand, over the medium-term higher rents and shorter rent free periods are likely to become the norm.

Tenant-Controlled Space

While it is possible that more "tenant-controlled" space might come to the market over the next few quarters via sub-letting, as a consequence of some businesses making redundancies, it is unlikely that this will have a significant impact in alleviating the current imbalance between supply and demand. Further, due to its age, tenant-controlled space is also less likely to meet the recruitment and environmental criteria that many footloose tenants have set, as detailed above.

Climate Change And Demand

As detailed in the Q2 2022 edition of this publication, and in a bid to combat climate change, the British Government is proposing to tighten the regulations under the existing Minimum Energy Efficiency Standards (MEES) legislation that will bar landlords from leasing properties that have poor energy efficiency ratings.

Well-informed footloose tenants are, rightly, planning well ahead of the introduction of the new regulations and are focussing their property searches on buildings that will be compliant with the new regulations which are proposed to be phased in from 2027. While the Government's proposals primarily affect landlords, they will also have an impact on tenants too – especially those that may later wish to sub-let surplus space.

Grade B office space will typically have poorer energy performance ratings compared with new and refitted Grade A accommodation. The Grade A and Grade B office markets are, as a consequence, diverging. Landlords of non-compliant space will therefore need to invest in an energy performance upgrade if they are to secure a return from their real estate investments.

Value For Money Locations

Those seeking more choice and better value accommodation are most likely to achieve their objectives by focussing their searches on low and mid-rise buildings in the City of London and in locations within the Docklands, Stratford and West London sub-markets.

Although peripheral locations such as Docklands and Stratford have typically been perceived by occupiers based in the West End, Midtown and City sub-markets as not being suitable, the now fully operational Elizabeth Line has significantly shrunk travel times. Improved transport connectivity and a lack of choice in the central districts of London are therefore likely to conspire to reinforce demand for office space in the East London sub-markets.

Tables 1 and 2 of this document provide the latest data on rents and rent free periods.

Lease Renewals And Rent Reviews

The terms that can be agreed in relation to lease renewals and rent reviews will be significantly influenced by the rents and rent free period letting packages that are being agreed on open market lettings of comparable office space. It therefore follows that those tenants seeking to renew their lease or agree a rent review on environmentally compliant Grade A accommodation may well be faced with a landlord that is seeking a rent increase to reflect the movement of rents over the last 18 or so months.

Epilogue - Market Knowledge

While the slowing in the UK economy is likely to weaken demand for office space during the first half of 2023 it is, nonetheless, likely to remain resilient, driven by a combination of downsizing and the desire of the more progressive businesses to operate from higher quality accommodation – to reinforce recruitment, return to the office and environmental policies.

Those seeking to relocate to environmentally compliant Grade A office space are likely to be surprised by the lack of choice and the "bullishness" of landlords in lease negotiations in many areas of central London, as supply-side constraints underpin the bargaining position of landlords.

Those operating from environmentally compliant Grade A space that are facing a lease renewal or rent review are likely to be confronted by a landlord seeking a rent increase.

Market knowledge will therefore be paramount if the best financial and most tenant-friendly lease terms are to be secured.

Michael Pain
Head of Tenant
Representation Team
07715 001013
michael.pain@carterjonas.co.uk

Rents and Rent Free Periods

Advertised Rents

Landlord's advertised rents for Grade A space across much of London have remained broadly static during the fourth quarter of 2022, underpinned by low vacancy - especially in the West End and Midtown office markets.

As reported during the third quarter of 2022, landlords with buildings that have poor environmental credentials and low energy efficiency ratings, which includes much of the Grade B office market, are struggling to secure lettings and there is downward pressure on rents in this market segment. It is likely that the combination of weaker demand over the next few quarters, reflecting declining economic growth, and the shift away from environmentally unsound buildings, will result in widespread reductions in advertised rents in this sector of the market during the first half of 2023.

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. Contrast with discounts of 2.5 – 6% that were typical during the first quarter of 2022.

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

Table 1 – Typical Rent Free Period By Sub-Market – Q4 2022
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 - 15 months	24 - 28 months
City Fringe North / North West - Shoreditch, 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 - 26 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

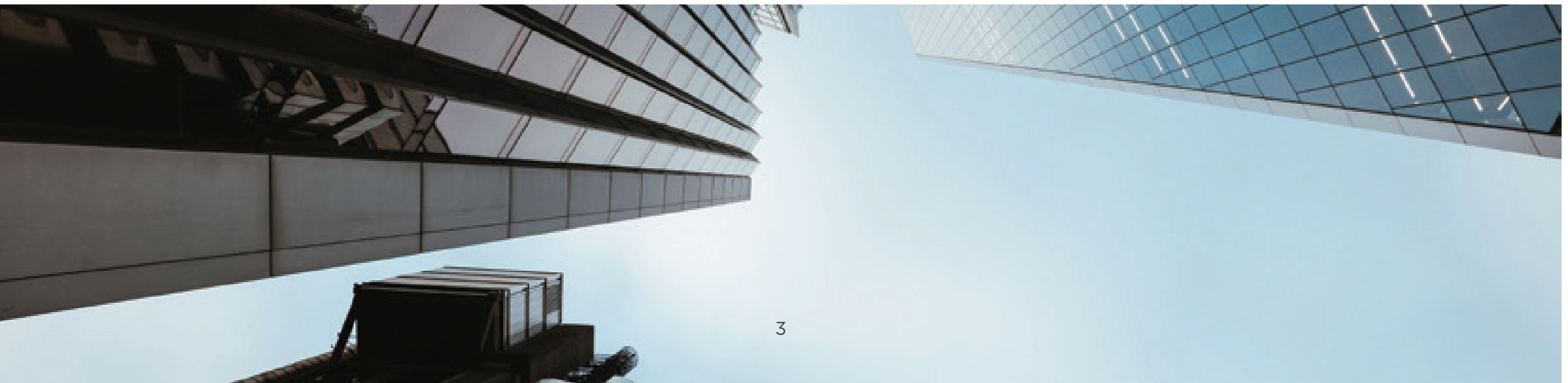
Source: Carter Jonas Research

Rent Free Periods

During the first half of 2023 rent free periods are likely to remain static and may, in some areas, where there is a better balance between supply and demand, including the City of London, Docklands and West London sub-markets, expand slightly, as landlords use rent free period incentives as a "shock absorber", reflecting weaker demand, in order to maintain the headline rents that were achieved during 2022.

Landlords of Grade B space with poor green credentials will continue to be under pressure to offer long rent free periods to attract tenants, reflecting the structural shift in demand away from low quality office space.

> "Those seeking to relocate to environmentally compliant Grade A space are likely to be surprised by the lack of choice in many parts of London."



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 Grade A space with good green credentials are likely to remain flat at least for the first quarter of 2023, reflecting weaker demand against a background of uncertain economic growth and rising interest rates and inflation

Rent Discounts

- the discounts that can be negotiated on advertised rents for new and refitted, well located, Grade A space are likely to remain at their current level of 1 - 4% during the first half of 2023, 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 first quarter of 2023 but may begin to expand during the second quarter to reflect weaker demand and the keenness of landlords to maintain headline rent levels

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 ESG strategies

> "The disruption in the property development and refurbishment pipelines, caused by the COVID pandemic, has interrupted the supply of new office space coming to the market."

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 during the first half of 2023, 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 steady 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

"2023 will most likely witness a weakening in demand for office accommodation across central London in response to declining UK economic activity.

However, low levels of vacancy in the environmentally compliant Grade A market segment will limit choice for footloose tenants and underpin rents."

"Low and mid-rise City of London buildings and the Docklands and West London sub-markets offer more choice and better value."

Table 2 – The London Office Market – Typical Landlord's Advertised Rents Q4 2022

£ 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	£67.50 - £77.50 (UF = £82.50 - £110.00)	£57.50 - £67.50 (UF = £72.50 - £85.00)	£40.00 - £52.50
Secondary - Blackfriars, Aldgate	£57.50 - £70.00 (UF = £75.00 - £90.00)	£47.50 - £57.50 (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 - £55.00 (UF = £57.50 - £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)	£57.50 - £66.50 (UF = £67.50 - £75.00)	£40.00 - £55.00
Battersea, Nine Elms, Vauxhall	£55.00 - £67.50	£45.00 - £53.50	£37.50 - £43.00
East London			
Docklands Prime – Canary Wharf & Wood Wharf	£49.50 - £59.50 (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	£87.50 - £97.50 (UF = £100.00 - £120.00)	£75.00 - £85.00	£60.00 - £70.00
South – Victoria, Westminster, Haymarket	£75.00 - £89.50 (UF = £90.00 - £95.00)	£65.00 - £72.50	£45.00 - £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	£72.50 - £85.00 (UF = £87.50 - £92.50)	£60.00- £70.00	£47.50 - £55.00
East – Holborn	£62.50 - £75.00 (UF = £77.50 - £82.50)	£52.50 - £62.50	£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	£55.00 - £65.00	£40.00 - £52.50
Hammersmith	£52.00 - £59.50	£40.00 - £50.00 (UF = £55.00 - £57.50)	£35.00 - £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	£40.00 - £50.00	£36.50 - £42.50	£29.50 - £36.50

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

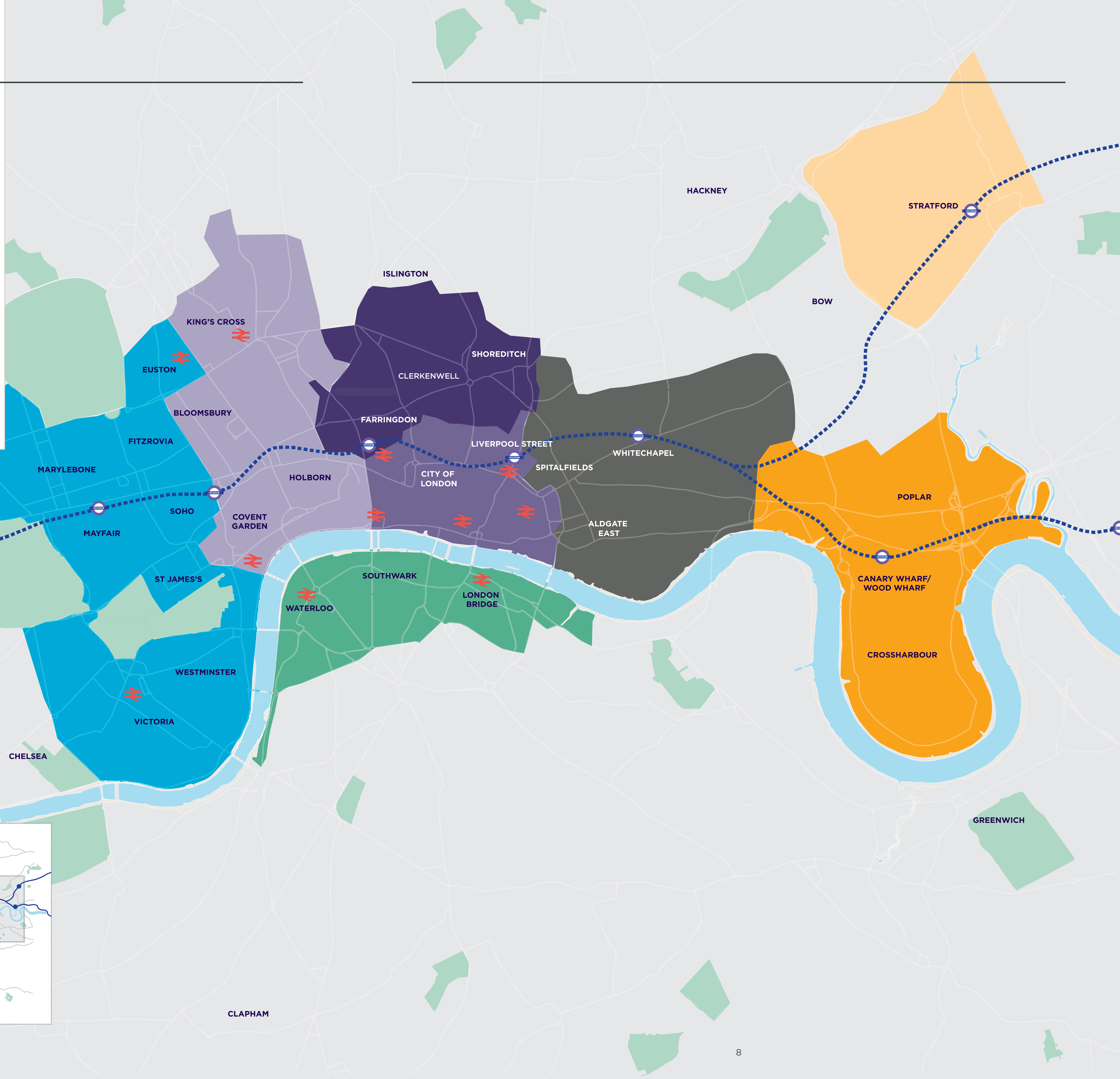
The London office market is formed of a series of sub-markets each having quite different supply and demand dynamics, which are reflected in the differing levels of rent and rent free periods that characterise each location.

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.

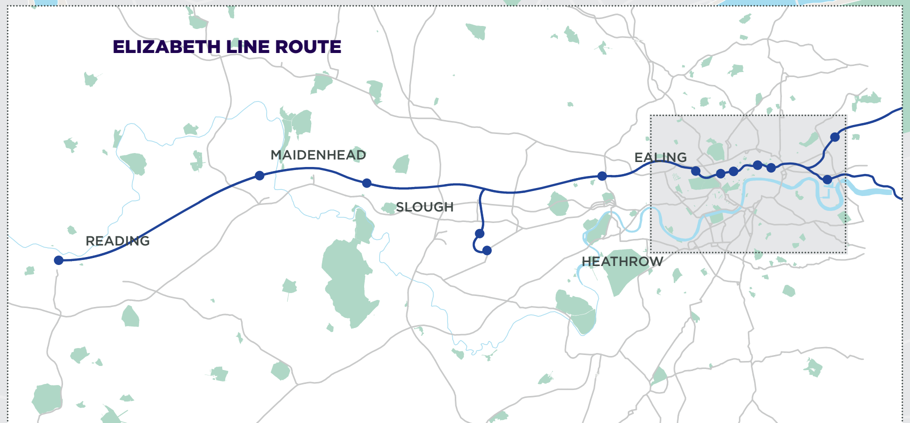
Rent Free Periods

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



Sub-markets & Postcodes

- **West End** W1, W2, SW1, NW1
- **Midtown** WC1, WC2, Part N1/EC1/EC4
- **City** EC2, EC3, Part EC1/EC4
- **City Fringe North** Part EC1/N1
- **City Fringe East** E1, E2
- **South Bank** SE1, SW8
- **London Docklands** E14
- **Stratford** E15, E20
- **Elizabeth Line/Crossrail** route
- Denotes **National Rail** station



Principal Office Occupation Costs

The fourth quarter of 2022 has seen an increase in London office occupancy costs for new and refitted Grade A space, reflecting two key trends:

- the gradual increase in rents for best in class Grade A buildings in those sub-markets with low vacancy
- inflation in service charge costs, driven by rising energy costs – a trend that is not location-specific and which is affecting all London sub-markets

Continued Cost Pressures
The aforementioned cost pressures are unlikely to ease for the foreseeable future and are likely to be the hallmark of the London office market during 2023 as take-up continues to erode Grade A vacancy in an under-supplied market, and as energy cost inflation continues to push up service charge costs.

2023 Business Rates Revaluation
Inflation in office occupancy costs is likely to be further exacerbated by the business rates revaluation which will take effect from 1 April this year.

Table 3 – Comparison Of Rent, Business Rates and Service Charge Costs By Sub-Market – Q4 2022

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	£72.50	£28.00	£14.00	£114.50
City Fringe North - Shoreditch, Clerkenwell	£72.50	£22.00	£13.00	£107.50
City Fringe North West - Farringdon, Smithfield	£85.00	£23.50	£13.00	£121.50
City Fringe East - Aldgate East	£55.00	£21.00	£13.00	£89.00
City Fringe East - Spitalfields	£72.50	£24.00	£13.00	£109.50
South Bank - Southwark, London Bridge	£72.50	£24.50	£13.00	£110.00
East London - Canary Wharf	£55.00	£17.25	*£18.25	£90.50
East London - Crossharbour	£35.00	£12.50	£13.00	£60.50
East London - Stratford	£47.50	£12.50	*£12.00	£72.00
Midtown West - Bloomsbury	£85.00	£31.25	£13.00	£129.25
Midtown East - Holborn	£70.00	£28.00	£13.00	£111.00
Midtown North - King's Cross	£85.00	£32.00	£13.00	£130.00
Midtown South - Covent Garden	£80.00	£32.25	£13.00	£125.25
West End Central - Mayfair, St James's	£125.00	£52.00	£14.00	£191.00
West End North - Marylebone	£97.50	£40.50	£13.00	£151.00
West End North - Fitzrovia	£95.00	£35.95	£13.00	£143.95
West End South - Victoria, Westminster	£77.50	£35.25	£13.00	£125.75
West End West - Paddington	£77.50	£26.00	£13.00	£116.50
West End East - Soho	£92.50	£40.50	£13.00	£146.00
West London - Hammersmith	£56.00	£22.50	£12.50	£91.00
West London - White City	£53.00	£18.75	£12.50	£84.25
South West London - Battersea, Nine Elms	£62.50	£21.00	£12.50	£96.00

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

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 Q4 2022

The fourth quarter of 2022 has been no different to the previous three quarters of 2022 – take up has again been dominated by the lettings of energy efficient, new and refitted Grade A space, reflecting the high priority that occupiers are placing on recruitment and environmental issues when selecting office accommodation.

The table below illustrates the key lettings that have taken place during Q4 2022 in the various London office sub-markets.

Table 4 – Key Office Lettings – Q4 2022

Sub-market	Tenant	Business Sector	Property	Floor Area (sq ft)
City of London	Clifford Chance	Legal Services	2 Aldermanbury Square, EC2	321,000
City of London	Grant Thornton	Business Services	5 Broadgate, EC2	105,000
City of London	Apple	Technology	22 Bishopsgate, EC2	76,140
City of London	Levin	Business Services	155 Bishopsgate, EC2	23,000
City Fringe East - Spitalfields	Reed Smith	Legal Services	Blossom Yard & Studios, Norton Folgate, E1	126,800
City Fringe North West - Farringdon	Partners Group	Financial Services	The JJ Mack Building, 33 Charterhouse Street, EC1	37,825
Midtown - Bloomsbury	GSK	Pharmaceuticals	The Earnshaw Building, 77-91 New Oxford Street, WC1	155,000
Midtown - Covent Garden	New York University	Education	265 Strand, WC2	75,000
Midtown - King's Cross	London BioScience Innovation Centre	Life Sciences	The Apex, Granary Street, N1	31,127
West End - Mayfair	Blackstone	Financial Services	Lansdowne House, 57 Berkeley Square, W1	226,000
West End - Marylebone	Lazard	Financial Services	20 Manchester Square, W1	78,500
West End - Victoria	Javelin Global Commodities	Commodities Trading	27 Eccleston Square, SW1	21,473
West End - Fitzrovia	Creo London	Serviced Offices	60-62 Margaret Street, W1	21,340
West End - Victoria	Pemberton Asset Management	Financial Services	5 Howick Place, SW1	20,000
West End - Soho	Centerview Partners	Financial Services	Lucent, Sherwood Street, W1	19,500
West End - Paddington	Bark	Business Services	30 Eastbourne Terrace, W2	12,000
West End - Paddington	St James's Place Wealth Management	Financial Services	Fifty Paddington, 50 Eastbourne Terrace, W2	10,000
East London - Docklands	Citibank	Financial Services	40 Bank Street, Canary Wharf, E14	94,174

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 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

As with the previous two quarters of 2022, activity in the London serviced / co-working office market has continued at a brisk pace during the fourth quarter, driven by a combination of factors, including:

- a move away from the traditional operating model, where all staff are expected to attend the office on a specified number of days each week, to a "hub" based accommodation model where staff work from home and attend the office only when required to collaborate in team activities
- the desire of those that have exercised break options or not renewed leases to hedge their bets and move to short term, temporary, accommodation pending the return of a more certain economic climate
- the inability of some organisations to find conventional / non-serviced accommodation that meets their operational and budgetary criteria in their preferred area of search – moving to serviced offices to "tread water" until suitable accommodation becomes available

Demand for serviced, co-working and managed office accommodation across central London is likely to be underpinned by the factors set out above for at least the first half of 2023.

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.

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

"For those businesses that are facing a break option or lease expiry, the option of moving temporarily to service office accommodation is quite an attractive proposition.

The serviced office accommodation model offers a stop gap to enable businesses to establish how the impact of COVID, and the current slowdown in the UK economy, is likely to affect their financial performance, and influence how much floor space will be required in the medium to longer term."

- 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.

Central London Office Investment Market Commentary

The second half of 2022 saw immense political and economic upheaval, with investors reassessing their risk assumptions as long and short-term interest rates rose rapidly to counter double-digit inflation. Central London office yields shifted upwards as a result, although for prime product this occurred to a more modest extent than much of the mainstream commercial property sector.

Central London office investment transaction volumes were down sharply in Q4, even compared with a fairly subdued Q3. This pause in activity reflects the current elevated level of pricing uncertainty for buyers and sellers, with sentiment showing significant and rapid changes in recent weeks (both positively and negatively). This has been reflected in sharp swings in the level at which prospective buyers are prepared to place bids. Indeed, it is fair to say that the current market is one of the most uncertain that we have experienced.

We expect to see this picture improve significantly in 2023. The fundamentals for London offices remain strong and there is considerable underlying interest from a broad variety of purchasers. Overseas buyers are additionally helped by the favourable level of Sterling against the US Dollar. We believe the volume of central London office transactions will recover during the year, with investors keen to deploy cash reserves once pricing has settled to a level which reflects the current risks and opportunities.

However, with occupiers now focussed on excellence in ESG and providing a first-class environment for their employees, the flight to quality will only intensify. Uncertainty over long-term demand levels in the occupational market will therefore remain a feature. For investors, this will mean a further widening of the pricing gap between prime and the rest of the market, with yields for secondary property continuing to move out. In contrast, we should see resilience in the pricing of those assets that are 100% prime.

The Tenant Representation Team

Our tenant representation services include:

- Serviced & co-working property searches and negotiations
- Break option linked lease re-negotiation
- Workplace design & floorspace re-configuration
- Marketing & leasing services – surplus space
- Conventional office space search & cost appraisal
- Office move management
- 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.

Key Contacts

Michael Pain Partner
Head of Tenant Representation Team
07715 001013
michael.pain@carterjonas.co.uk

Ali Rana Partner
Head of National Investment
07739 019717
ali.rana@carterjonas.co.uk

Daniel Francis Head of Research
07801 666137
daniel.francis@carterjonas.co.uk

Ed Caines Partner
07966 188632
ed.caines@carterjonas.co.uk

Ollie Lee Associate
07815 039501
ollie.lee@carterjonas.co.uk

David Simnock Associate
07765 937001
david.simnock@carterjonas.co.uk

Anders Horwood Associate
07836 246049
anders.horwood@carterjonas.co.uk

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