GERALDEVE
A NEWMARK COMPANY

LONDON MARKETS

London office property
performance and key themes

Q1 2024

Read more

LONDON OFFICE MARKET SUMMARY

Take-up was 2.8 million sq ft in Q1, one of the largest quarterly volumes of the last year and 3% above the 5-year quarterly average. A two-tier occupational market is taking root as firms focus on the best quality space to meet modern workspace requirements.

There was continued positive rental growth in Q1, particularly for Grade A space, as occupiers vie for limited supply. In both the West End and the City, nominal annual rental growth has been positive for the past three years, but in real terms, accounting for inflation, rents haven fallen significantly.

Availability fell in Q1, with the rate now at 8.2%. This corresponds to 22.1 million sq ft, marking the lowest volume since Q3 2022. Availability remains low in core West End markets, especially Marylebone which boasts the lowest rate among the submarkets.

An estimated 230,000 sq ft completed across five schemes in Q1. Several larger office developments have been postponed until early Q2, with over half of the 2024 pipeline set for delivery in the upcoming quarter.

Refurbishment activity is on the rise, with nearly 7 million sq ft anticipated for delivery over 2024 and 2025. Nearly 60% of the total 8.3 million sq ft refurbishment pipeline is within a 10-minute walk of a Crossrail station, highlighting the importance of connectivity to modern occupiers.

Investment volumes reached £1.5bn in Q1 across 29 transactions. This was 7% below Q4 and just under a third below the 5-year quarterly average. Average deal size over the last three quarters stayed consistent at around £50m, highlighting the reticence from investors to utilise debt for acquisitions.

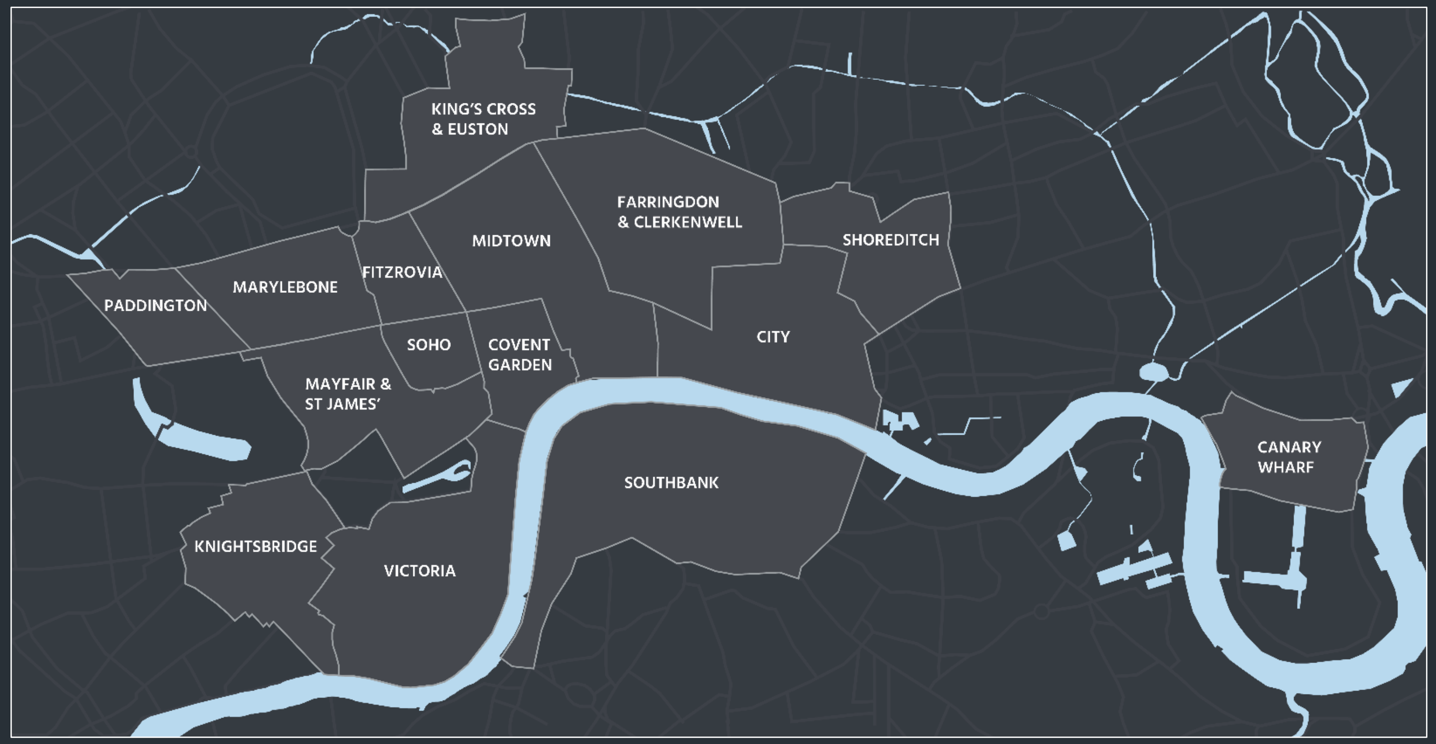
2.8m sq ft ▼
Take-up, Q1 2024

8.2% ▼
Availability rate, Q1 2024

£1.5bn ▼
Investment volume, Q1 2024

10.5% ▲
Marylebone Grade A annual rental growth, Q1 2024

GERALD EVE LONDON SUBMARKETS



LONDON'S ECONOMY

GVA

	2022	2023	2024
London	5.3%	0.7%	0.7%
UK excl. London	3.7%	0.2%	0.5%

ILO UNEMPLOYMENT RATE

	2022	2023	2024
London	4.5%	5.1%	5.4%

OFFICE-BASED EMPLOYMENT GROWTH

	2022	2023	2024
Central London	5.5%	5.8%	0.6%

Source: Oxford Economics

LONDON FLASH PMI MARCH 2024

57.1 ▲

Business Activity Index

New business inflows rose again, keeping the capital at the top of the regional rankings.

55.6 ▼

New Business Index

Respondents reported new clients, projects, and higher demand from existing customers. However, some firms indicated that sales were slowing amid economic concerns.

74.0 ▼

Future Activity Index

Monthly fall from a two-year high but ongoing optimism from new business pipelines, new products, technology improvements and planned investment.

49.8 ▼

Employment Index

Qualitative responses show reduction in employment was due to staff leaving and difficulties finding replacements.

Source: IHS Markit
Arrow indicates monthly change, above 50 signifies expansion

London continues to lead the regions on forward-looking business activity indicators, with most PMI measures showing positive trends, albeit with a recent moderation in expansion.

While London's GVA growth for 2023 was revised down from 1.1% to 0.7%, it still outperformed the rest of the UK and is expected to be the highest-growing region in 2024.

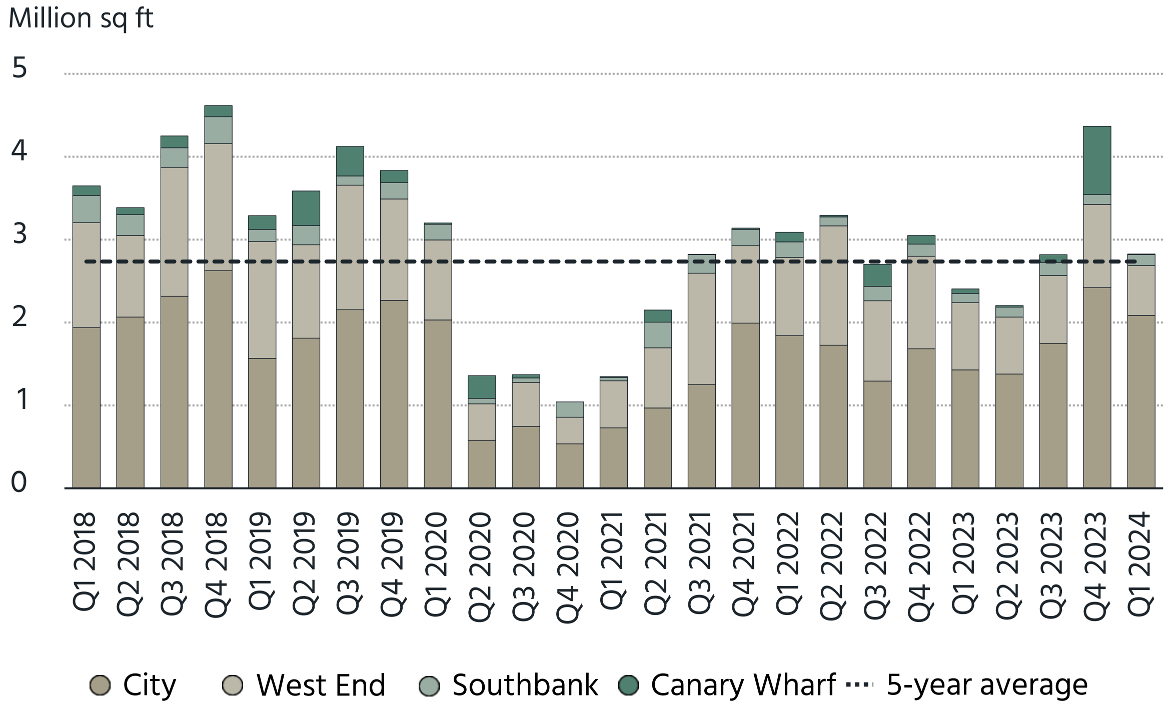
March PMI responses on employment highlight challenges in replacing staff with similar skills and experience, leading to bottlenecks for expansionary employment. The unemployment rate has been revised upwards and is expected to reach 5.4% in 2024.

Office-based employment is projected to grow by 0.6% in 2024, with administrative and support roles being the strongest sector, expected to grow by 2.1%. While there was an initial expectation of a decline, financial services employment is now forecasted to remain flat in 2024.

DEMAND

London office quarterly take-up by broad market

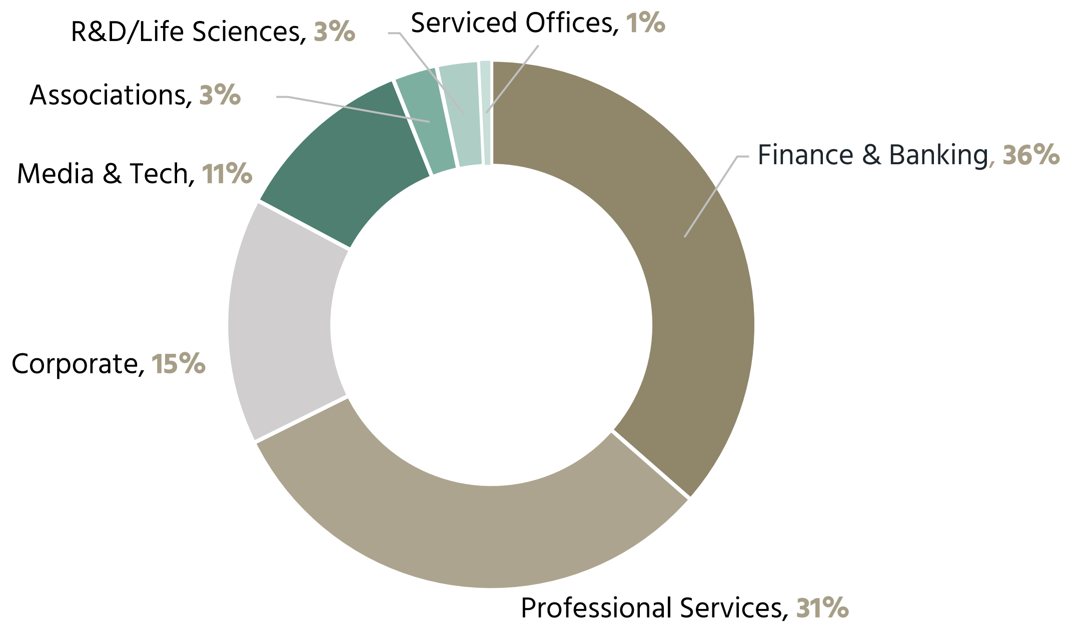
Source: Gerald Eve



Occupier activity kicked off the year on a strong note, as take-up reached 2.8m sq ft in Q1. This surpassed any quarter from 2023 — excluding the outlier in Q4 caused by the large HSBC and Barclays lettings — and exceeded the 5-year quarterly average by 3%. The City was the most active submarket, with leasing activity of over 1.4m sq ft, which marked the highest level since Q1 2020. Notably, seven of the ten largest lettings this quarter were in this submarket. Q1 boasted the highest deal count since Q3 2022, primarily fuelled by sub-10,000 sq ft lettings. In terms of volume, this size bracket reached just over 1.1m sq ft, the highest since Q4 2019.

Take-up by business sector, Q1 2024

Source: Gerald Eve



The finance and banking sector made up 36% of activity in Q1, led by a handful of sizeable commitments in the City. By subsector, insurance firms were particularly active making up a fifth of all demand from the wider sector. Professional Services were a close second with 31%, with nine of the top ten leases in the sector by size signed by law firms as they continue to be active in the market. Generally, large commitments have been focused on Grade A prime offices and there is a two-tier occupational market taking root in London offices, as certain building characteristics resonate more with tenants' new modern workspace requirements.

THE OCCUPATIONAL MARKET – WHAT IS RESONATING?

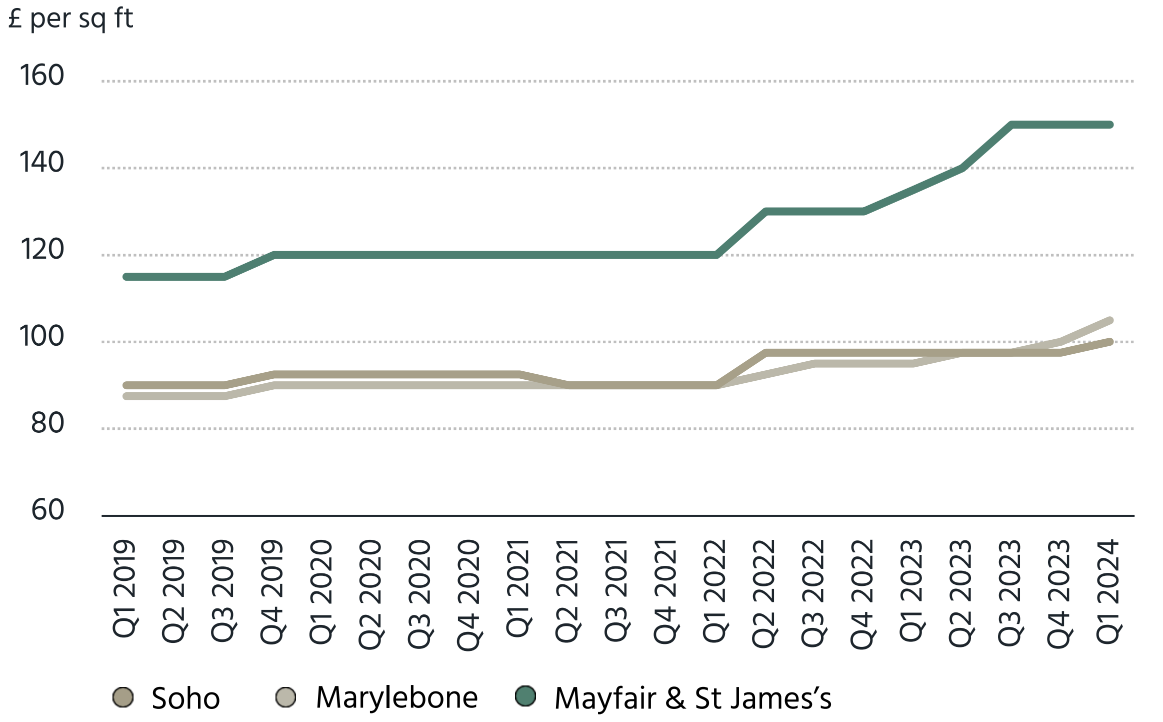
A two-tier occupational market is talking hold as firms meet new modern workspace requirements. Core demand is primarily focused on offices with the following characteristics:

- **Terraces and communal outdoor spaces** – focus on well-being and options for collaboration and amenity.
- **End of trip facilities** – including cycle spaces, lockers and showers.
- **Core location** – accessibility, nearby amenities and proximity to transport hubs.
- **Connectivity** – ease of access to multiple transport options, especially the Elizabeth Line.
- **ESG** – high EPC/BREEAM/NABERS rated buildings, with sustainability now a must have for large commitments.
- **Corporate Social Responsibility** – well-being of employees to secure and retain the best talent.

RENTS

Core West End submarkets, Grade A rents

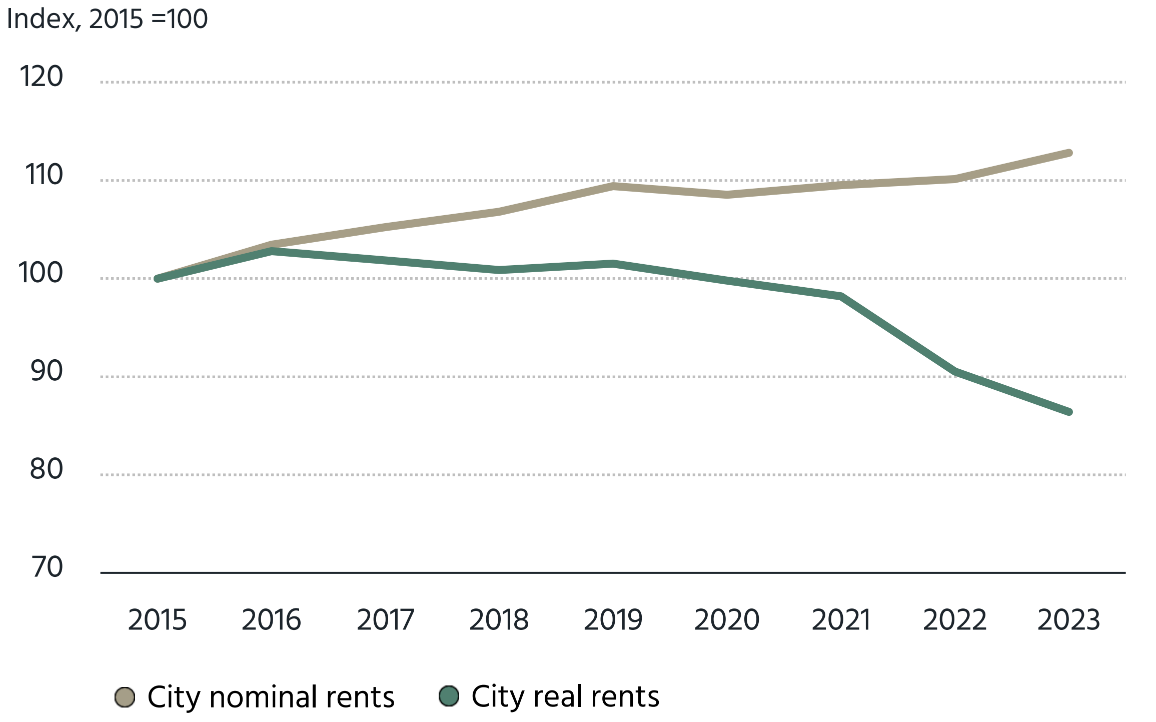
Source: Gerald Eve



Grade A rents in Marylebone rose to £105 per sq ft, while rent-free incentives fell by 3 months to 21 months for a typical 10-year lease. The submarket ranks second for annual rental growth, with rents rising 10.5%, behind only Mayfair & St James's at 11.1%. In Soho, Grade A rents increased by £2.50 to £100 per sq ft. Higher than average demand over the last two quarters and a lack available Grade A space contributed to this upward trend. Occupier interest is greater for top quality offices in the West End and diminishing prime availability rates in selected submarkets is supportive of further rental growth.

City nominal versus real rental index

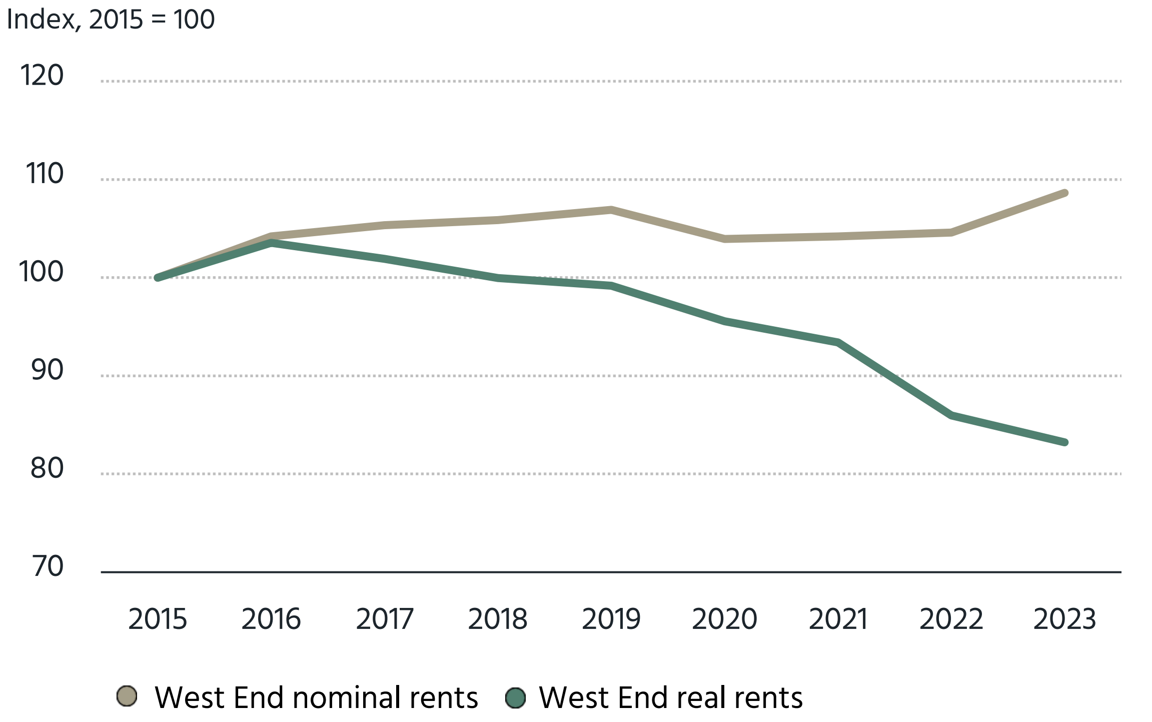
Sources: Gerald Eve, MSCI



Recent trends have shown headline rental growth, particularly for Grade A space, as occupiers vie for limited supply. While the rise in rents might raise concerns about affordability for potential occupiers in nominal terms, it's worth noting that inflation has outpaced rental growth in the last three years. Moreover, rent constitutes a small portion of occupier costs, especially for large firms where staffing expenses make up most of the operational expenditure. In both the West End and the City, despite nominal annual rental growth over the past three years, real-term rents haven fallen significantly due to high inflation in 2023.

West End nominal versus real rental index

Sources: Gerald Eve, MSCI



However, inflation appears to be moderating, with the annual March reading dropping to 3.2% from 3.4% in February. According to Oxford Economics, inflation is expected to further decrease, with a forecast of 2.1% for 2024 and an average of 2.2% between 2025 and 2027. Although rental growth forecasts for the West End and the City exceed these inflation figures, the existing gap in real rents in both segments suggests there is potentially more room for additional nominal rental growth, particularly with true Grade A space still in short supply.

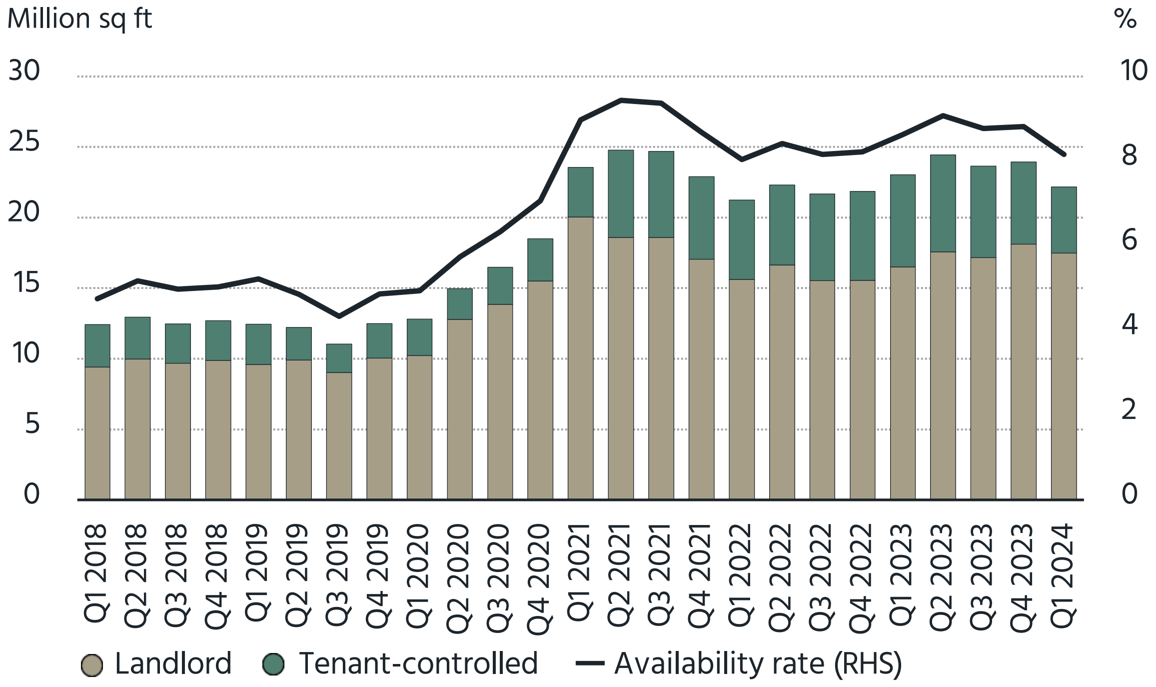
RENTS AND INCENTIVES BY SUBMARKET

Typical achievable headline rent for 'Grade A' space let on a typical 10-year lease on a mid-level floor with no terrace.

AVAILABILITY

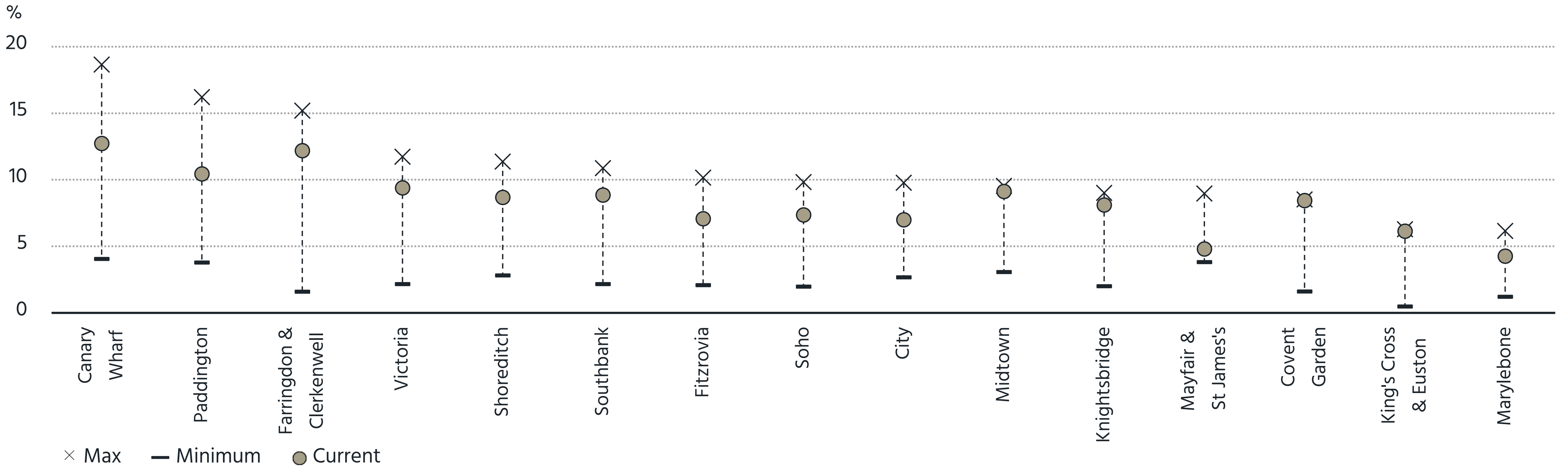
Central London availability by type of listing and rate

Source: Gerald Eve



Availability rate and historical range by submarket, Q1 2013 – Q1 2024

Source: Gerald Eve



The availability rate fell by 0.6%-pts to 8.2% in Q1. This corresponds to a total of 22.1m sq ft of available space, marking the lowest volume since Q3 2022. Landlord availability decreased by 0.6m sq ft to 17.5m sq ft due to positive take-up of such space, while tenant-controlled availability fell to 4.7m sq ft, its lowest level since Q1 2021. However, much of the decrease in tenant space is somewhat artificial, as over half a million square feet at 5 North Colonnade in Canary Wharf was withdrawn from the availability list when Barclays returned the tenancy to Canary Wharf Group.

As a result, availability in Canary Wharf dropped to 12.7% in Q1, marking the lowest rate in over two years, albeit still the highest among the tracked submarkets. Canary Wharf is currently undergoing a transformation, repositioning offices with life science or residential components in mind. However, this transition may pose challenges on the path to normalised supply. With a large pipeline of life science developments in the medium term, and more office space slated for delivery, an increase in development-led supply is inevitable unless followed by a corresponding uptick in demand.

Availability remains low in core West End markets, especially Marylebone which boasts the lowest rate among the submarkets. The scarcity of supply here is supportive of further rental growth, particularly for Grade A space. Meanwhile, in Soho, sustained demand over two quarters well above the 5-year quarterly average has driven availability down to 7.4%, a decrease of 2.2%-pts from Q3 2023. Similarly, positive demand in the City resulted in availability dropping by 0.8%-pts to 7.0% in Q1, marking the lowest rate since Q3 2020 and marking a streak of five consecutive quarterly declines.

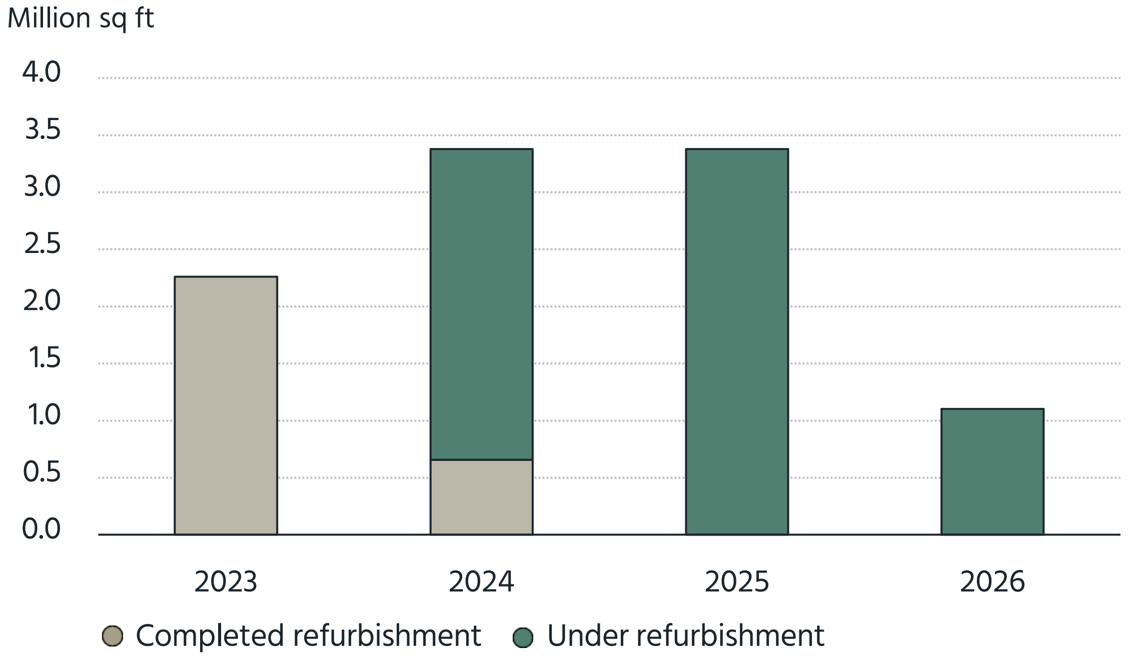
DEVELOPMENT

London office development pipeline, new build

Source: Gerald Eve

London office development pipeline, refurbishment

Source: Gerald Eve



London office refurbishments, proximity to Elizabeth Line

Source: Gerald Eve

<10-min walk from Elizabeth Line >10-min walk from Elizabeth Line

The year started sluggishly for development completions, with an estimated 230,000 sq ft completed across five schemes in Q1. Several larger projects have been postponed until early Q2, with over half of the 2024 pipeline set for delivery in the upcoming quarter. Depending on absorption rates, newly-completed schemes may increase availability, especially in submarkets with weaker demand. Development timelines are routinely delayed, with estimates indicating that just over 1.7m sq ft earmarked for 2024 completion has been pushed into 2025, bringing the total completion volume for next year to 5.7m sq ft.

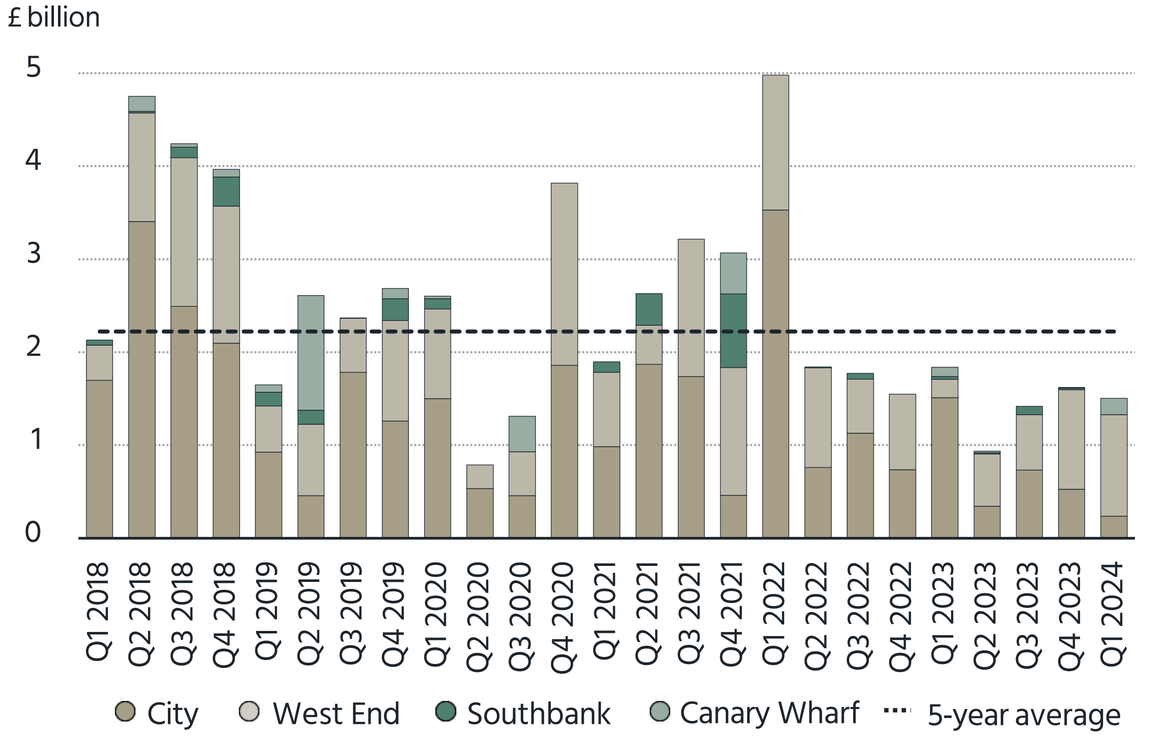
Refurbishment activity is on the rise, with nearly 7m sq ft anticipated for delivery over 2024/25, compared to the 6m sq ft estimated in Q4. Increasing finance and construction costs have subdued new starts for office construction projects, with refurbishments a more cost-effective, and thus, appealing alternative. Value-add investors are increasingly acquiring discounted offices to renovate, spurred by recent outward yield shift. Landlords with lower-quality office spaces are undertaking refurbishments to regain value, particularly in submarkets where secondary office values have notably declined.

Refurbishment projects are centred around fundamentals of location, connectivity and configuration. These link with occupier drivers of transport, amenities and sustainability and the Elizabeth Line has become a focal point for both investors and landlords, influencing redevelopment decision-making. Nearly 60% of the total 8.3m sq ft refurbishment pipeline is within a 10-minute walk of a Crossrail station, highlighting the importance of proximity to this key transportation link for landlords, developers, and occupiers alike.

INVESTMENT

Quarterly investment volumes by broad market

Sources: Gerald Eve, Real Capital Analytics



The volume of investment in Q1 was £1.5bn across 29 transactions. This was 7% below Q4 and a third below the 5-year quarterly average. The average deal size over the last three quarters has been consistent at around £50m, highlighting the ongoing reluctance from investors to utilise debt for acquisitions. The top two acquisitions of the quarter are symptomatic of an emerging conversion trend present in London offices. MCR Hotels acquired the BT Tower to reposition into a hotel, and Royal London took a 50% stake in 1 Triton Square for a JV with British Land to redevelop Facebook's never-occupied office into life sciences.

UK property companies were the most active investor group in Q1, with acquisitions totalling £601.7m across 10 transactions. The group was active at the top end of the market, making three of the top five investments this quarter, all of which were over £75m. Overseas investors were relatively quiet on the buy-side in volume terms, with £340.2m invested in Q1 and 9 of the 11 purchases by the group on lot sizes under £50m.

UK institutions continue to be active on the sell-side, disposing of £644.7m across 13 transactions. Most of these were in the West End with the group taking profit on well-located and multi-tenanted offices with good income.

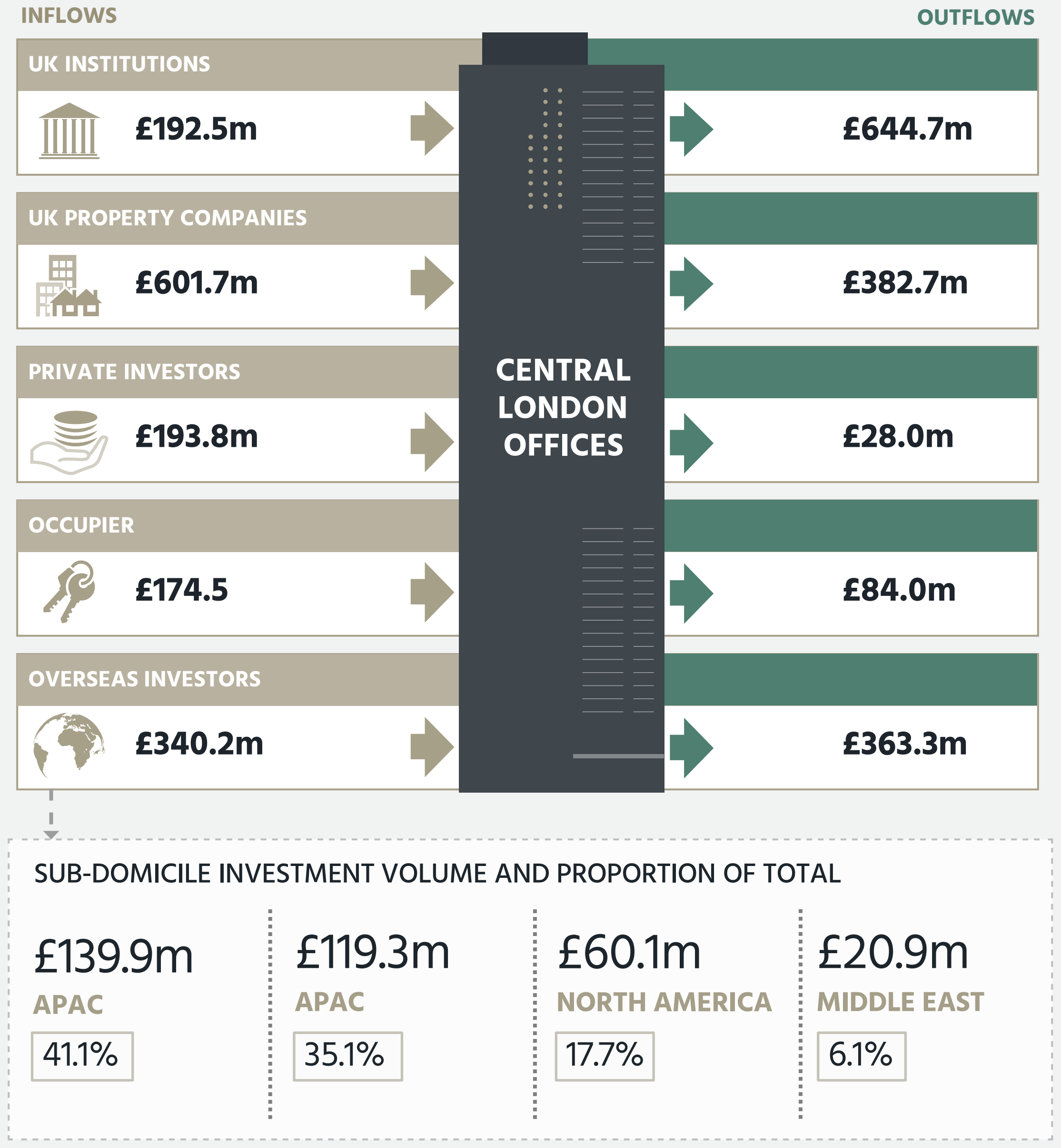
INVESTMENT MARKET OUTLOOK

Broader disinflationary forces mean overall inflation is set to continue to fall to the Bank of England's 2% target over the coming months. But the latest data is unlikely to allay lingering concerns over stickiness in core inflation and services pay growth, with the first cut not expected until June. Oxford Economics has revised down its forecast of 100bps of cuts this year to 75bps and retained the 100bps in 2025, which will take the Bank Rate to 3.5% by the end of 2025.

More accommodative monetary policy later this year will lead to a gradual thawing of the investment market. The gap between buyer and seller price aspirations, made more challenging by escalating debt costs, has been a considerable obstacle to market activity. So, while challenges persist in the central London office investment market, opportunity is afoot for savvy investors willing to navigate the evolving landscape.

CENTRAL LONDON OFFICE CAPITAL FLOWS, Q1 2024

Sources: Gerald Eve, Real Capital Analytics



GERALD EVE IN THE MARKET

RECENT LETTINGS

103 Wigmore Street, W1

Acting on behalf of the landlord, Duke Street Property, we have let 12,000 sq ft over the newly refurbished 2nd floor to Fenwick, who will relocate staff from the iconic department store on New Bond Street following the sale to Lazari in December 2022.

Please contact Rhodri Phillips or James Lunn for more information.

ACTIVELY MARKETING

210 Pentonville, N1

Acting on behalf of Global Holdings, we are marketing a selection of newly fitted and CAT A refurbished floors totalling 47,000 sq ft in King's Cross.

Please contact Rhodri Phillips, James Lunn or Viviana Thurstan for more information.

Belgrave House, 76 Buckingham Palace Road, SW1

On behalf of private equity clients, we have brought to market a 'CAT A+' presented penthouse suite of 6,000 sq ft.

Please contact Rhodri Phillips, James Lunn or Viviana Thurstan for more information.

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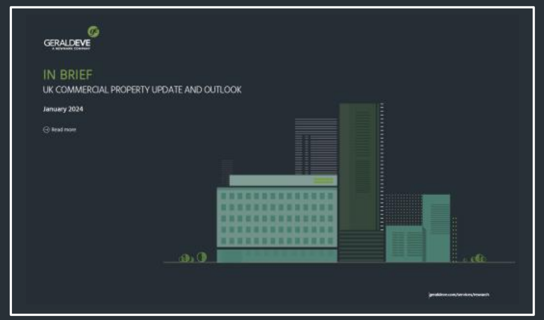
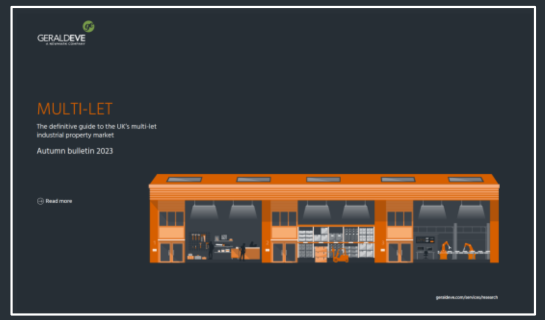
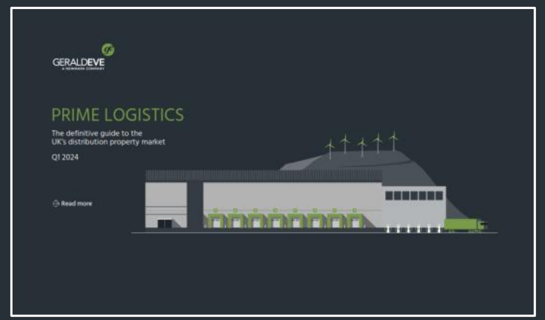
FURTHER INSIGHTS



In Brief
March 2024



Multi-let
Autumn 2023



Prime Logistics
Q1 2024

For further information on all our Research, visit our website **here.**

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