LONDON

EXECUTIVE SUMMARY

- The diversity of the London office market will continue to be of paramount importance to ensure the on-going success of London as an international business centre.
- Subdued development activity matched by strong demand for larger prime office space is pushing rental values up across some London submarkets.
- Retailers are increasingly utilising their London flagship stores to drive success through customer experience, underpinned by London's ability to attract customers from a wide geography.
- There will be an increased focus on housing provision and meeting delivery targets, as Sadiq Khan looks to get re-elected as Mayor of London in May 2020.

THE DIVERSITY OF THE LONDON OFFICE MARKET

London continues to drive the U.K. economy, accounting for 24% of economic output and powering employment growth. Much of this growth stems from London's status as a key financial centre, with the sector accounting for a quarter of total employment. It is also a significant driver of office demand across the city.

In September 2019, London ranked second in the Z/Yen Global Financial Centres Index, just behind New York. Furthermore, the 2019 Bank for International Settlements survey found that daily trading in London's financial markets has increased by 29% since 2016 due to strong levels of FX trading, with London's already dominant share of daily volumes rising from 37% to 43% over the period.

In an increasingly connected world, exceptional digital and infrastructure connectivity will be paramount to continued economic growth. The Mayor of London has set in motion several infrastructure projects to better meet rising demand. Fibre is currently being installed throughout London, in addition to the provision of full mobile coverage on the tube network, initially starting with the Jubilee Line which will receive full mobile coverage in March 2020.

Office buildings increasingly hold a WiredScore digital connectivity certification which assigns a rating to a building's digital performance, acting as an assurance to both occupiers and potential investors. Across London, there is currently 15 million sq ft of space under this scheme, which is projected to rise further as technology plays an increasingly key role in the continued growth of London.

KEY MARKET METRICS – 2020 EXPECTATIONS

Annual growth rates, estimated for year-end 2020 vs year-end 2019.

	OFFICE	RETAIL	INDUSTRIAL
Rental Growth	↑	↓	↑
Vacant Space	↓	↑	↓
Construction Levels	↑↑	→	↑
Leasing Volume	→	↓	→
Investment Volume (all sectors)		↑	

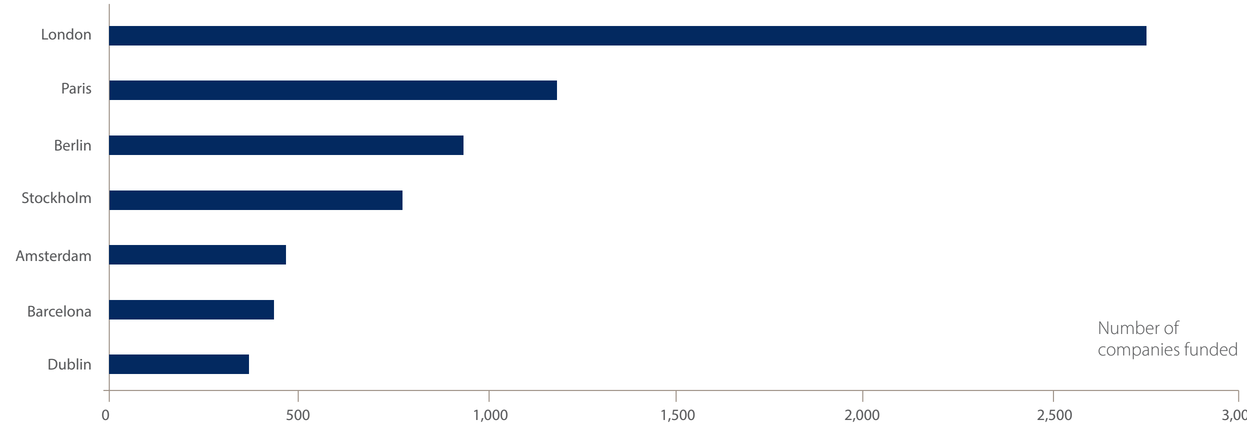
London's occupier market continues to diversify with a growing tech industry attracted by London's availability of talent and capital, both of which may be relatively dependent on the U.K.'s relationship with the EU. According to Eurostat, London is the most educated city in Europe with the highest proportion of tertiary educated residents; and a diverse workforce speaking over 230 languages, of which a significant proportion work in creative industries.

London has a growing FAANG (Facebook, Apple, Amazon, Netflix & Google) presence with larger tech occupiers acting as an anchor to drive tech clustering elsewhere in the city. Netflix launched a new 160,000 sq ft requirement at the end of 2019, which will increase its London office presence by around 700%, and help its expansion into the U.K. market. In addition, Google is currently building its King's Cross landscaper HQ to house 7,000 employees; Facebook recently took additional space in King's Cross for its new HQ and Apple and Regus brand No18 let the entire office element of Battersea Power Station, also acquiring 100,000 sq ft at 22 Bishopsgate, EC2 in late 2019. Amazon has an existing HQ at Principal Place, EC2 which houses 5,000 employees.

London also accommodates a growing SME presence, of which some expand to become tech unicorns (billion dollar start-ups). According to data from Tech Nation and Dealroom, London currently has 45 tech unicorns with a combined value of £116 billion; and produces one in five tech unicorns that originate in Europe. This is underpinned by significant venture capital investment which continues to rise despite market uncertainty. In 2019 alone, Greensill, a fintech company, raised a total of $1.6 billion in funding from Softbank.

London has long been considered the fintech capital, but 2020 is likely to see growth in hybrids such as proptech and legaltech that have been slower to adapt new technologies. Furthermore, London's existing presence as a centre for life sciences, supported by the strength of its universities and research institutions, is likely to create further hybrid companies within medtech, driving efficiencies in medicine and pharmaceuticals.

NUMBER OF TECH COMPANIES RAISING FUNDING, 2015 – SEPTEMBER 2019



Source: Dealroom and Atomico

LONDON OFFICES

CITY

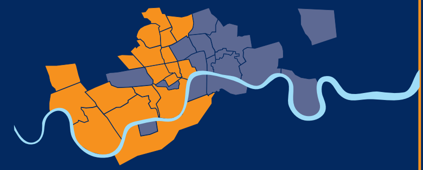
Take-up in the City market has remained very strong, with levels on average 150,000 sq ft above the 10-year average since the EU referendum. Take-up is likely to remain stable in 2020, driven by a healthy underlying level of demand, although supply continues to remain constrained.

Occupiers with large requirements will continue to have limited options. There are multiple instances of major occupiers having to search through a number of locations, or where occupiers have agreed an off-market deal due to an existing landlord-tenant relationship.

As a result of recent strong pre-letting activity, space under construction is currently close to 50% let. However, there are indications that the pipeline may start to increase in 2020 with several large developments rumoured to be commencing construction. These include 40 Leadenhall Street, EC3 (900,000 sq ft), One Leadenhall, EC3 (500,000 sq ft) and Elizabeth House, SE1 (1.2 million sq ft), which may alleviate the pressure on supply.

Although rental levels remained relatively stable during the first half of the year, the City has recently seen some upward pressure due to constraints on supply. Shoreditch and Clerkenwell which have previously seen very strong rental growth may slow in 2020, and City Core could potentially catch-up due to strong demand and increasingly limited supply.

Landlords are able to achieve premium terms and shorter voids by producing a best in class building. However, where only a minor redevelopment or refurbishment is undertaken, buildings are seeing extended void periods and inferior rental terms. Record rents are achieved for 'super-prime' space in the City, where the correct blend of amenities and public realm has taken rents above the prime level for their respective submarkets.



WEST END

West End take-up for the first three quarters of 2019 was higher than at any point since 2013 and this is likely to continue in 2020 despite very limited development supply. Overall, the under construction West End pipeline is 71% pre-let and without a sufficient level of development stock, the coming months may see occupiers turn to other markets to fulfil larger space requirements.

There are still many occupiers that prioritise the West End over other markets, as demonstrated by recent leasing evidence where record rents have been achieved for prime space outside the traditional core. This is particularly true for larger floor plates in the West End which are particularly limited given the market's historic planning restrictions. There are currently just 12 buildings over 100,000 sq ft under construction in the West End, of which seven have been entirely pre-let.

There is an increasing divergence between the rental levels achieved for Grade A supply and second-hand supply, which often sees significantly extended letting void periods. This has been termed a "honeymoon market" in which if space has not been let within two months, landlords need to prepare for a long haul with expensive void costs to deal with.

EAST LONDON

2020 may see a boost to East London take-up as occupiers struggle to find suitable space to meet their larger requirements elsewhere, and increasingly look for more affordable rents, with the City and West End rents increasingly topping £80.00 per sq ft.

The Elizabeth Line will improve connectivity and therefore the occupier perception of East London markets. Space is increasingly marketed as offering excellent transport connectivity and therefore continued demand will be reliant on the Elizabeth Line arriving soon, although recently announced delays throw a spanner in the works. With Stratford and Canary Wharf currently very public-sector focused, limited availability elsewhere may result in occupiers from a wider range of sectors acquiring space in East London.

London's occupier market continues to diversify with a growing tech industry attracted by London's availability of talent and capital

INVESTMENT MARKET

Brexit related uncertainty has undermined turnover for central London assets during 2019, with volumes to Q3 less than half that of the preceding year. A decrease in demand from buyers has coincided with a lack of available stock, although there is a weight of money waiting for greater economic certainty. 2020 is likely to see an increase in stock if certainty returns to support seller confidence. Core stock is particularly attractive to buyers in the current uncertain market, due to the surety of income. Increasingly, European cities are at a substantial yield premium to London, with prime yields in Paris and Frankfurt now below 3%, over 100 bps below the City Core prime yield. This strategically positions London as an attractive location for investment, supported by a very robust occupational market.

Year-end 2019 saw a return to strong buyer interest in long-income trophy properties attracted by relative pricing, with strong buyer interest likely to continue for 2020 following greater certainty brought by the December general election. 2020 may see yields start to compress as we expect strong buyer interest to return to drive pricing upwards. We have seen a return of German, Malaysian and North American investors to the London market after a 5 year hiatus in some instances. Notable investments include Brookfield's purchase of a 50% stake in London Wall Place for £354 million, EPF's purchase of Premier Place for £330 million and DEKA's acquisition of 40 Chancery Lane for £121 million.

Demand for value-add stock has recently picked up as buyers recognise the strong occupational market and potential low supply, which may translate into an increase in development pipeline stock next year. M&G recently announced its purchase of "Gotham City", 40 Leadenhall Street for £355 million which upon completion in 2023 will provide over 900,000 sq ft of Grade A space. Other examples include Mitsubishi's purchase of the London Television Centre, SE1 for £145.6 million, BT's £120 million sale of its Newgate Street, EC1 HQ to a fund run by Orion Capital Managers, and CBRE GI's purchase of 280 Bishopsgate, EC2 for £183 million.

CUSTOMER EXPECTATIONS

The increase in demand for serviced office space has characterised the office market during the latter half of this decade and will undoubtedly continue into the 2020s, although with some consolidation on the horizon. 2020 is likely to see a flight to quality over quantity by operators in order to maximise occupancy and profitability in an increasingly over-supplied market, and one in which occupier expectations are changing.

SMEs and large corporates will continue to require an element of flexibility, supported through improvements in technology which enable remote working. The growth in demand for serviced offices from SMEs, which make up 99.9% of London businesses, has caused a subsequent fall in demand for smaller units which come into direct competition with serviced offices. Void periods for conventional space extend up to 18 months in extreme examples, therefore landlords are updating their offer to a fully-fitted provision termed Cat A+, offered to tenants on flexible release terms, in order to properly compete.

2020 is likely to see an increase in the variety of serviced office provision, all centred on the importance of flexibility to occupiers of all sizes. Mainstream serviced office operators too are changing their models to reflect a greater variety of requirements; WeWork for example has grown its 'WeWork HQ' brand to appeal to corporates. Furthermore, landlords are increasingly looking to attract and retain traditional tenants by offering an element of serviced offices in-house to allow temporary expansion or project space.

The growth in serviced offices has also highlighted the increasing importance of space as a service to promote health and wellbeing, and therefore buildings achieve record rental levels and high occupancy when these elements are considered. Google's new HQ which is currently under construction at King's Cross will provide next-level amenity provision including a running 'trail', sports hall, floor-to-ceiling windows to enable natural light, retail units and an amphitheatre.

In the retail sector, a shift towards greater online spending against a backdrop of rising costs and squeezed profit margins, is presenting a major challenge to retailers. The changing retail market has caused several retailers to now utilise their London flagship stores as a means of driving brand image through customer experience; personalisation of products and interactivity through technology. This is creating pockets of retailers that are able to significantly outperform the market.

Perhaps the most high profile example in London is the Samsung facility at King's Cross which does not call itself a store and in which there are no tills. Customers can decorate walls with digital graffiti and race cars with the latest VR technology; in addition to it being a showcase of its latest high-profile digital products. It is not just tech companies however that are utilising technology to optimise customer experience, the Zara flagship store in Stratford has smart mirrors with technology that recognises the items you holding, in addition to robot powered pick-up locations and self-scan registers.

London's prime retail markets have a reach that extends far beyond their immediate vicinities, acting as a beacon to domestic and international tourists. According to Mastercard's Global Cities Index, London ranks second highest in Europe after Paris for number of visitors, but records the highest total spend by overnight visitor with £13.5 billion, compared to £11.5 billion in Paris.

The growth in online spending has altered customer expectations with individuals and businesses now expecting to receive goods faster, more cheaply and and in a more flexible manner. This is putting increasing pressure on industrial supply to meet demand, exacerbated by new entrants to the industrial market which are improving the efficiency of operations through technology and innovation, putting operating models and profitability under strain.

INDUSTRIAL INTENSIFICATION

Changing expectations and the historic erosion of London's industrial stock to residential use continues to limit its industrial supply. The Government has now recognised the erosion of industrial stock has gone too far; London vacancy currently stands below 8% with some boroughs achieving vacancy rates well below these levels. Under Policy E7 of the London Plan, due to be adopted in 2020, construction of residential stock on industrial land must ensure there is no net loss in industrial floorspace capacity within designated SILs AND LSISs. Whilst we have seen some evidence of industrial intensification allocations in the planning system to manage the no net loss principle, it is not yet at the levels required to manage target vacancy rates at 5% and 8% for land and floorspace respectively.

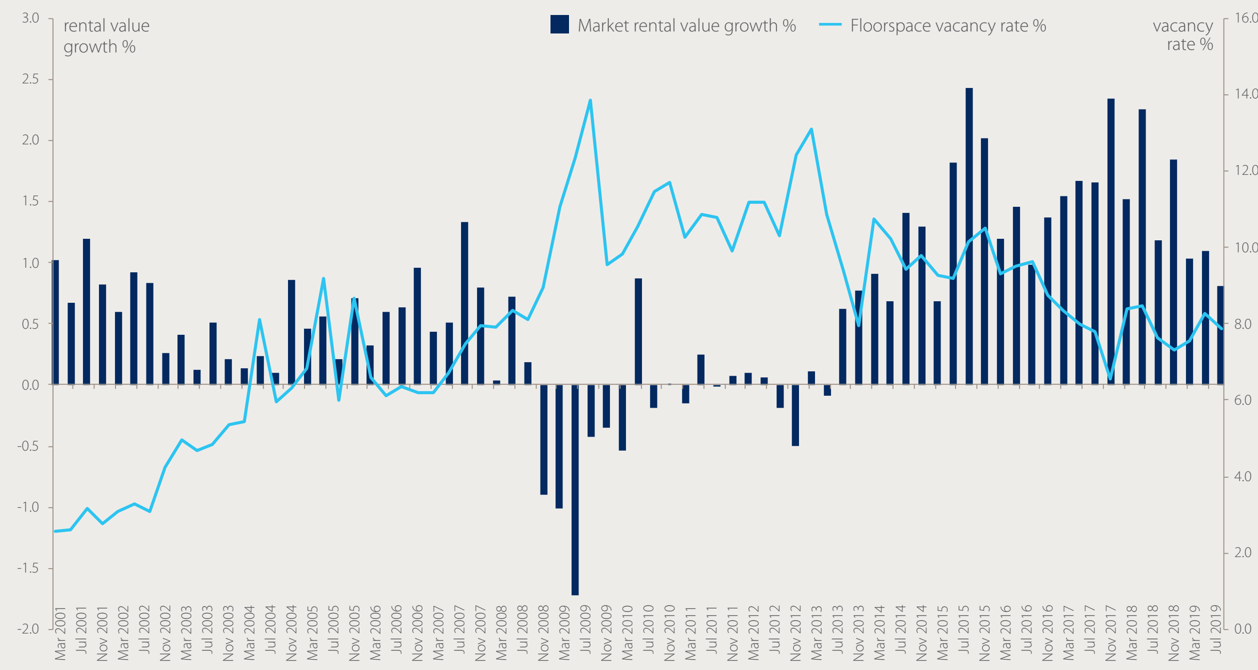
Mutli-storey development, whilst a feature of some international markets, is a potential new addition to the London market with some developers considering taking on the associated risk. Gazeley has proposed a development of a multi-storey urban logistics hub totalling 426,000 sq ft across three storeys. Plans submitted to Newham Council have received objections, although these are likely to be resolved in 2020.

The development is the first of its kind in the U.K. and if successful, London is likely to see an increase in multi-storey industrial developments.

In addition, Formal Investments are currently preparing for the construction of a new facility at Rectory Park, Hounslow which will provide underground industrial space. The ground works are projected to last a further six months, after which the two year construction period will begin. The project won the Mayor's Award for Innovation in Planning in 2018 for its innovative design.

Drawn from the London Plan, co-location developments are increasingly viewed as a solution to both shortages in industrial and residential supply. The Mayor's London Plan has stated that an additional 65,000 homes a year will be needed to keep up with rising population and demand, particularly at affordable levels. There are currently few developments with planning permission for co-location in the pipeline; however this is expected to rise in 2020 with several important mixed-use developments currently at the planning application stage in London.

LONDON INDUSTRIAL RENTAL VALUE GROWTH AND VACANCY



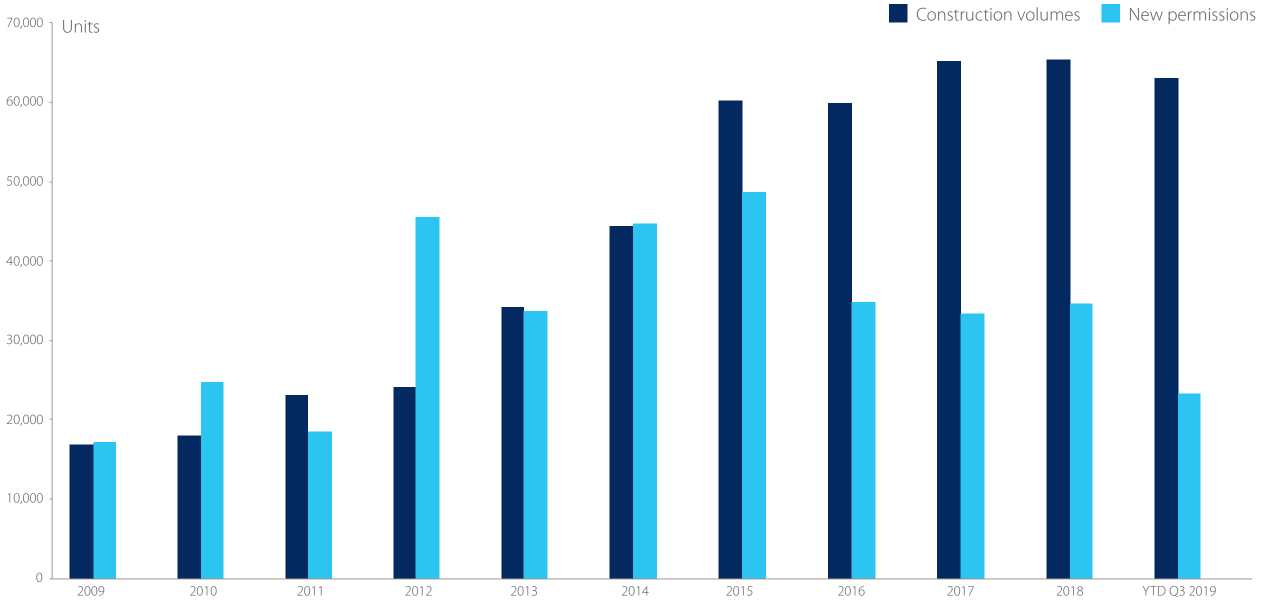
Source: MSCI

LONDON'S HOUSING CRISIS

In 2016, the Mayor of London committed to building 116,000 new affordable homes by 2022, including homes on a social rent, living rent and shared ownership basis. As of June 2019, just over 40,000 affordable homes had started construction, just 36% of the target. Private developments with over 10 units are obligated to deliver a minimum of 35% affordable housing to meet the target, however to date just 24% of projects have met this target. In the lead up to the May 2020 mayoral election there is likely to be an uptick in affordable housing development and a tightening of loopholes that allow developers to ignore the targets, at least in the short term.

The rising importance of Build to Rent (BTR) to solving London's housing crisis cannot be understated. The proportion of London's population who rent rather than own their property is increasing. In 2016, just 28% of households lived in the private rented sector; however this is expected to rise to 40% by 2025 which will put particular pressure on the housing industry to provide suitable rented accommodation. According to a report by London First, 15,000 BTR units have been built to date, with a further 19,000 under construction and 38,000 going through planning.

LONDON RESIDENTIAL CONSTRUCTION VOLUMES AND NEW PERMISSIONS



Source: Molior

Wembley Park, owned by Quintain, is the largest build to rent development in the U.K. due to provide a total of 5,000 homes over several phases. The scheme comprises 78% PRS and 22% affordable housing. Three sites are due for delivery in 2020 providing over 1,600 residential units, in addition to other uses. Placemaking and amenity provision is increasingly considered important to ensure the success of BTR. If the housing sector is to come close to tackling London's growing housing crisis, the speed of delivery of placemaking is going to be critical and with Build to Rent's absorption rates being swifter than traditional sales, Build to Rent has to form a more significant part of proactive planning policy across the capital, irrespective of who wins the mayoral election in May.

2020 is likely to see a further increase in the level of BTR provision as developers grapple with uncertainty in domestic and overseas markets and de-risk, particularly within larger regeneration areas. However, more proactive policy from key decision makers is required to ensure the industry creates homes more quickly. In addition, investment into affordable housing looks set to follow the same growth path. Until recently, affordable housing was the sole preserve of housing associations but according to the latest figures from City Hall, the number of affordable home starts in London doubled from 2018/2019 to 2019/2020 and is expected to grow further as institutional investors increase their exposure to the sector. However, to make sizeable inroads into the creation of housing, more innovation will be needed to create a greater depth and variety of affordable housing to meet the varying needs across London.

HOTELS

The London market performed especially well in 2019 with revenue per available room increasing 4% over the year to November 2019. This was due, in part, to a major uplift in North American visitors which increased 11% over the year to August 2019. Healthy hotel market performance has been driven partly by the weakness of sterling relative to other currencies, in addition to the popularity of events which attracted significant tourism throughout 2019. Key drivers included the London Games and All Points East music Festival, conferences such as Roots Tech and BSC Expo, and sporting highlights such as the ICC Cricket World Cup.

Further strong demand is expected for 2020 as the capital continues to benefit from both domestic and overseas tourism with the UEFA Euro 2020 football championships likely to generate a significant boost. Hotel development continues to be high in response to strong occupational market fundamentals and 2020 is projected to see a further addition of 9,627 new rooms in London including the completion of Zedwell Piccadilly Trocadero, W1 and The NoMad London, WC2. Avison Young tracked 25 hotel sales in London in 2019, equating to £3.2 billion of investment (59% of the UK total). 2020 is likely to see further strong investment levels as hotel investment opportunities continue to attract both international and institutional money. The political certainty brought about by the general election in December 2019 has improved the outlook for London hotel investment, with yields likely to remain stable or possibly show some sharpening in the year ahead due to lack of available stock.

There continues to be a significant weight of capital with multiple investors looking at hotel investment opportunities