Oxford Office & Industrial Survey

Winter 2009

With falling rents and increasing incentives, will 2010 continue to be a tenants' market?

Oxford Industrial Park,Yarnton,Oxford,OX5 1QU. Up to 54,000 sq ft available.

- Office take-up for the first 9 months of the year was 123,392 sq ft. This is 32% down on the same period last year. Quality of stock in out-of-town locations has continued to dominate.
- On a positive note, 42% of all office take-up in 2009 was Grade A, this is proof that there is still demand for good quality space within the Oxford office market.
- Analysis of 2009's office take-up figures illustrates that 60% of the total number of transactions were for space below 10,000 sq ft, indicating that the smaller end of the market is still holding up.
- The Oxford industrial market saw take-up figures reach 501,333 sq ft at the end of the third quarter 2009. This was down 89% on the same period in 2008, and 42% down on the five year average.
- 2009 has seen falling rents on both top and average rents in both office and industrial sectors. It is predicted that falling tenant demand will continue in to 2010 due to the economic conditions.
- Landlords are working hard to retain tenants and maintain income, often agreeing to flexible and highly competitive packages. Cash flow rather than yield is King!

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Oxford Office Market

The global recession has inevitably had an impact on the Oxford office market. Declining business confidence, on the back of worsening economic conditions, has restrained occupational demand throughout the final half of 2008, which has carried on throughout 2009.

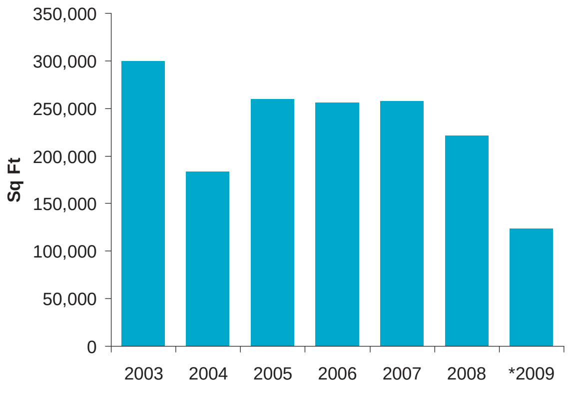
Indeed, take-up for the first three quarters of 2009 stood at 123,392 sq ft. This is 32% down on the same period last year and 48% down on the five year average. Quality of stock in out-of-town locations has continued to dominate in 2009, with 90% of all deals being out of town locations.

42% of all office take-up in 2009 was Grade A, this is proof that there is still demand for good quality space.

Analysis of 2009's office take-up figures illustrates that 60% of the total number of transactions were for space below 10,000 sq ft, indicating that the smaller end of the market is still holding up.

Significant larger deals include the Goodman's 8000 Hailwood scheme, where 22,113 sq ft was let to Oxford Fertility Clinic, this was on a 15 year lease with 18 months rent free. A letting of 12,562 sq ft to Kaspersky Labs at 97 Milton Park, acheived the highest rent of the year at £23.50 per sq ft. This was achieved in the first half of the year.

Take-up in 2009 is 32% down on the same time in 2008.



Source: *Savills* *to end Sep

A reoccuring theme is the proportion of the space leased out-of-town being significantly higher than the in-town market over the last five years. Has this bias towards out-of-town space changed in 2009?

Supply currently stands at 669,336 sq ft, a rise of 11% compared to the same point in 2008. However, the supply and demand picture in the two markets is still markedly different. Over 80% is still clustered within the out-of town market. If we concentrate on the city centre, there is still less than 30,000 sq ft of space situated there, with none of this stock being of Grade A standard. Due to the lack of Grade A stock in town, this still makes out-of-town the only choice for occupiers when looking for Grade A space.

The City centre owner occupier market still remains strong principally due to a very restricted supply,Savills have acted on two owner occupier deals in 2009 in this location. United Therapeutics a US biotech company purchased the former Cooper Callas building behind the Castle paying £3.1m for the 24,000 sq ft building. The Carlyle Group have sold Rochester House and the former GPO building in Pembroke St totalling 14,500 sq ft to The Story Museum for an undisclosed sum. In both cases the buildings generated significant developer and occupier interest. Both transactions have been excluded from the take up statistics as they were development opportunities.

However, looking forward, 23,000 sq ft of space will be developed speculatively at Trajan House in the city centre, where the quoting rents will be £23.50 per sq ft. This will not only help attract tenants to the city centre, but the rent quoted will help set new rental trends going forward.

The question is which sectors will remain resilient during this recessionary period?

Given the uncertainty surrounding the financial institutions and overall negative levels of business sentiment, the 'financial & business services' sector will see low levels of demand over the next couple of years. On a positve note, unlike a number of regional cities, Oxford isn't reliant on this sector as it does not account for the majority of take-up in any given year.

Although the current economic climate has had a negative effect on the demand from corporates with limited take up from the private sector in 2009, the Public sector has underpinned the market in 2009.

Deals of note throughout the year involve education and research, with the Pharmaceutical sector also taking a significant share of the market. This goes some way to explain the attraction of Milton Park in 2009, although most lettings were to existing occupiers.

Rents appeared to remain stable in the first half of 2009. However in the latter half of the year incentive packages on the business parks have increased to up to 2 years rent free on 5 year leases, or rents substantially reduced, i.e East Point,to £9.99 per sq ft, which equates to similar net effective rents.

We are predicting that this trend will continue into 2010. We expect that businesses will remain cautious over the next 12-18 months with a close eye on cost control. There will be a strong bias towards "clever" property decisions in terms of the balance between rent, building quality and location.

Oxford Office & Industrial Survey

The in-town refurbishments helped close the gap between in-town and out-of-town rents in 2008. With in-town refurbishments achieving £22.50 per sq ft. However, there have been no Grade A deals in the in-town market so far in 2009.

Rents have fallen, with increased incentive levels

Source: *Savills* *to end Sept

Demand will no doubt remain subdued going into 2010. Our research indicates that there is a reasonable level of latent demand still in the market. Savills are tracking tenants with expiries and break options to ensure an accurate assessment of demand.

Targeting those occupiers with potential new requirements is set to become all the more important. Whilst many occupiers may elect to remain in their existing space or delay relocation until economic conditions improve, there will be those that will see 2010 as an opportunity to secure new premises on terms which may not be available in12 months time.

Oxford Industrial Market

The industrial market saw a decline in take-up in 2009, as news of the financial situation worsened across the globe. The Oxford industrial market saw take-up figures reach 501,333 sq ft at the third quarter. This was down 89% on the same period in 2008, and 42% down on the five year average. However, with 175,000 sq ft under offer, the eventual outturn is likely to be better than expected.

Almost 30% of this take-up was situated in Didcot. With a 107,000 sq ft deal to OKA at 170 Milton Park, in quarter three, boosting the figures. However, due to Oxford's location, most industrial deals are made up of smaller units taken by indigenous occupiers.

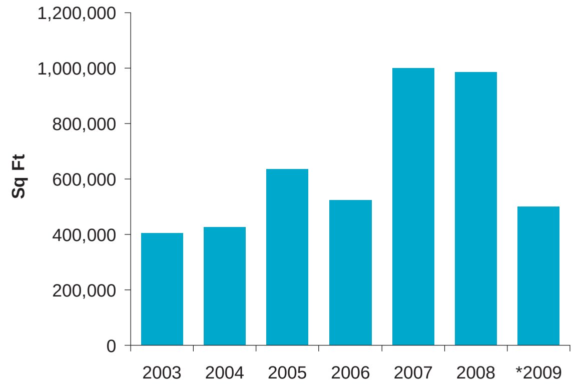
Analysis of 2009's take-up figures illustrates that 73% of the total number of transactions were for space below 15,000 sq ft, indicating that the smaller end of the market is still holding up.

Current supply amounts to 3.5 million sq ft, which represents a rise of 69% compared to the same time in 2008. Ironically in the last report we talked about there being little scope for larger new sheds to emerge and a general lack of redevelopment opportunities. However, in 2009 this has reversed, with five buildings over 100,000 sq ft coming back on stream. Over 850,000 sq ft of this space is situated in Didcot. This is evidence of a large amount of 'grey' space being put back onto the market by occupiers as rationalisation inevitably takes place. These units include, The Bathstore warehouse, the ASDA distribution warehouse,the Ryobi building and 182 Milton Park. 82% of this tenant space is Grade A.

If we look at take-up by Grade, the recession has had a impact on the type of space taken. Only 15% of deals in the first three quarters of 2009 were Grade A, compared to a five year average of 30%.

With a trend towards cheaper Grade B stock, will these large units have to drop their quoting rents to attract tenants?

At the end of Q3 2009, take-up was 89% down on the previous year.



Source: *Savills* *to end Sept

Coupled with lower occupational demand, the impact of empty rates has also focused developers minds on whether to deliver new speculative space to the market and there is now evidence of schemes being put on-hold, where letting risks are higher. This means that what is developed will be increasingly led by the preferences of the occupier,and this will enable occupiers to specify exactly what want when pre-letting a building. This will also allow current supply to be soaked up before any new stock replenishes the market.

So what effect is all this having on rents?

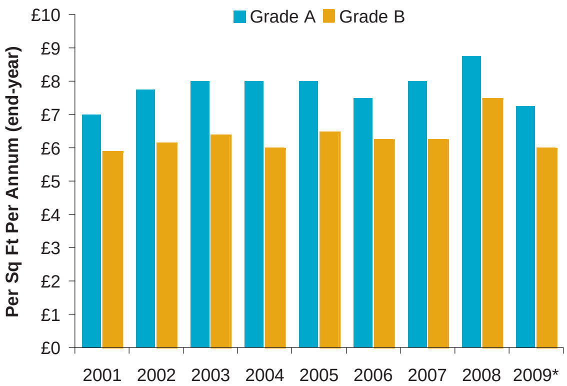
The highest rent achieved this year to date was £7.25 per sq ft at in Eyston Way, Abingdon. This is a 28% fall on the top rent in 2008.

However, on a more positive note, Oxford Industrial Park is quoting rents of £8.75 per sq ft with fitted out 9,000 sq ft unit currently under offer in excess of £9 per sq ft, which would help close the gap.

Oxford Office & Industrial Survey

Incentives are still moving out but should start to stabilise in the next 12 months. So is 2010 set to continue as a tenants' market?

Top rents have fallen from their 2008 peak.



Savills **to endSept*

Increasing rent free periods and falling rents means that there are attractive deals out there for occupiers. The combination of contracting demand and increased supply will lead to falling rents and increased incentives to occupiers. Occupational demand will no doubt remain subdued in Q4 2009 and into the first half of 2010, with annual take up expected to be down on the five year average.

Economic Overview and Investment

The consensus of economists suggests that the worst may have already passed as has been evidenced in a plateau in consensus expectations over the last few months. In addition, the 2010 expectations have improved markedly. However, given the depth of the downturn, the resurgence in activity is yet to materialise. There are tentative signs of recovery, with recent economic figures for Germany and France, prompting many commentators to predict that recovery has started.

Some commentators are struggling with the concept of an investment recovery whilst the occupational markets are still below trend and debt remains scarce. This is a fair point, but the falls in rental growth are beginning to recede, but will be some time before they move back into positive territory. Additionally, for investors, the currency play is strong. More encouragingly, however, the momentum of total returns, based upon the three-month movement, shows positive growth as at the end of September.

It is also interesting to look at the expectation for the changing nature of the employment structure for the county over the next 10 years, which will have an impact of the likely demand for commercial property.

Encouragingly, the Financial and Business Services (F&BS) sector in Oxford is set to experience a net increase in employment levels over the next 10 years (+16%). This will have a positive impact on long term net demand for office space in the Oxford market

While the UK economy is yet to emerge from the recession, there are beginning to be signs of a recovery in confidence and activity. As we move through the final quarter of the year, it is clear that the sentiment in the investment market has changed significantly from the beginning of the year.

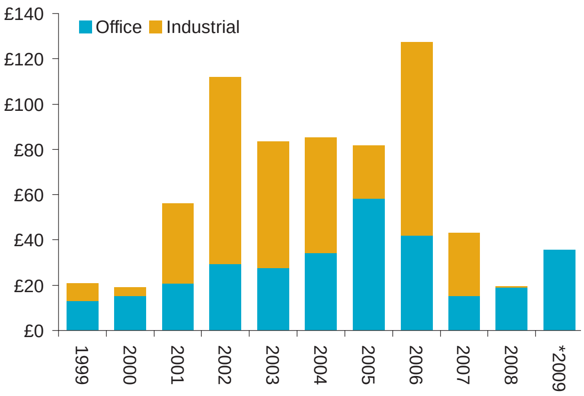
Traditionally the second half of the year has always been more active, primarily as a result of funds chasing to fulfil their asset allocation plans that were set at the start of the year.

This year may well be different and not due to a lack of willing buyers, but a lack of willing sellers. Many sellers have now become buyers as they sense the bottom of the cycle. Furthermore, the distress that many new entrants to the market have been hoping for has not emerged. Because of this we expect that prices will continue to rise on the best, and begin to stabilise on the rest, but volumes could remain low for some time.

Market evidence indicates that yields on prime property have softened by around 100 basis points (bp) to around 8%, over the last 18 months and 100-150 bp on secondary property. No significant deals were recorded throughout 2008 and the first two quarters of 2009. However, despite muted demand over the last 18 months, office yields in Oxford strengthened in the second half of the year for the first time in more than two years and now stand between 7.25% and 7.5%.

The third quarter of this year saw two deals sign at Oxford Business Park. In August,Threadneedle Property Investments acquired Blackwell Publishing's 65,000 sq ft building for £14.5 million, reflecting a yield of 8.3% and Astro Properties aquired the 21,500 sq ft at Oxfam House in September. This sold for £21.65 million, reflecting a yield of 7.36%. Encouragingly, this has seen investment levels on offices in 2009, exceed 2008 figures.

Oxford Investment Levels (£ millions)



Source: Property Data / Savills **to endSept*

Planning

Between now and 2026 Oxfordshire will become a major area for growth while Oxford City will be the primary focus for regeneration as well as expansion.

South East Plan

The Regional Spatial Strategy (RSS) for the South East of England (known as the South East Plan), published by the Secretary of State on the 6th May 2009, sets out the long term spatial planning framework for Oxfordshire until 2026. The South East Plan contains nine sub-regional strategy areas. The Central Oxfordshire sub-region covers a large part of Oxfordshire including Bicester in the north, Oxford to the east, Didcot to the south and Witney to the west. The plan sets out the strategy for the sub region including employment policy and housing figures.

Additional land for employment will be provided where justified at Bicester and Didcot, for the expansion and relocation of existing local firms to foster knowledge-based industry. In Oxford, development for employment uses will be expected to take place primarily on previously developed land and former safeguarded land or in conjunction with development schemes for mixed uses incorporating housing, town centre or other facilities. In the city centre, development which maintains and enhances the sub-regional role and diversity of the centre will be permitted, provided it is consistent with the protection of Oxford's architectural and historic heritage.

The Central Oxfordshire sub-region will make provision for 40,680 net additional dwellings between 2006 and 2026; an average of 2,034 dwellings per annum. These figures recognise and reflect regional, economic, demographic and other local imperatives, the ability of the sub-region to accommodate at least the numbers proposed, the heritage importance of Oxford, the extent of the Wessex Downs and Cotswolds Areas of Outstanding Natural Beauty and the existing pattern/future delivery of infrastructure. While contributing in due part to the regional reuse of previously developed land target of 60%, some greenfield development that includes housing, will be necessary. A selective review of the Oxford Green Belt will be carried out in accordance with Policy CO4.

It is assumed that about 4,900 will be built at Bicester, about 8,750 at Didcot and about 3,400 at Wantage/Grove. The Vale of White Horse and South Oxfordshire, via their local development documents (LDDs) or by other means, will ensure that Didcot's growth is achieved in a phased and timely manner within the Plan period. This may include the pooling of resources and/or development contributions to help deliver any needed transport improvements that support growth in the wider area or help reduce pressure on the A34.

An allocation of 4,000 dwellings for the period up to 2026 is included on Green Belt land to South of Oxford. South Oxfordshire District Council is opposed to the extension of Oxford and is challenging the South East Plan in the High Court.

Oxford's 'Northern Gateway'

In September 2009 the Oxford Northern Gateway proposals, which form part of the Local Development Framework (LDF) Core Strategy, were examined at a public inquiry. The aim of the inquiry was to establish whether the scheme is deliverable. The land is currently 'safeguarded' by the adopted Oxford Local Plan 2001-2016. Within the LDF Core Strategy the land is earmarked for Class B related uses as well as residential housing. The site is considered to strengthen Oxford's key sectors of employment relating to science and technology research, education and the biotechnology industry. Highway improvements will also reconfigure the road network at this 'entrance' to improve congestion issues.

Infrastructure Planning Commission

The Planning Act 2008 established a new body, the Infrastructure Planning Commission (IPC), which will be responsible for considering and determining new Nationally Significant Infrastructure Projects (NSIP's). This is being set up as an independent body comprising a panel of appointed commissioners, with specialised professional knowledge, and supporting staff. The main purpose is to help create a more efficient, transparent and accessible planning system which can deliver the critical infrastructure

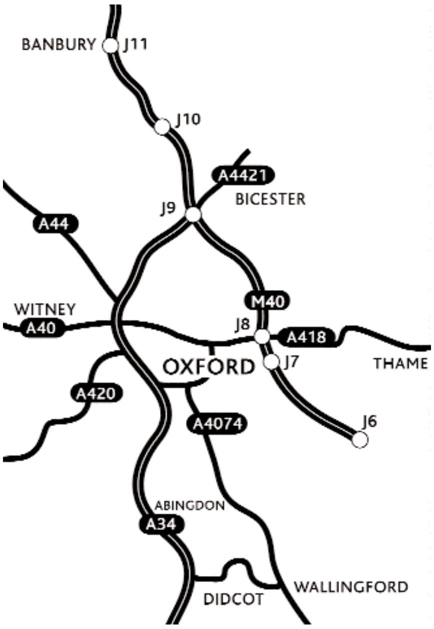
The IPC will consider applications for major infrastructure projects, such as wind farms and power stations over 50MW. Previously, consent for such schemes was given under numerous different regimes, but with applications to the IPC all relevant consents will be granted in a single development consent order.

The main policy framework for NSIP's will be set out in new National Policy Statements (NPS's), anticipated for publication late 2009/2010, and decisions on NSIP's will be made primarily in accordance with these policy statements. The independent panel of commissioners will apply their technical and professional judgment to the determination of applications, and disregard irrelevant or frivolous matters put to them.

To ensure that comments and views are considered by the developer, the new regulations and guidance discussed in this briefing note aim to "front-load" the process and ensure that a high standard of consultation is carried out with statutory and non-statutory consultees and local communities. The regulations therefore require more thorough notification of future applications, and more interaction between developers and consultees throughout the process, and not simply as a "token" gesture.

A key change is that developers are now required to prepare a Statement of Community Consultation (SOCC) prior to any application, stating who, when, and how they will consult on the project. A Consultation Statement is then required with the application to demonstrate that the consultation has been carried out in line with the SOCC and published guidance.

Survey area & key contacts



Definitions & Statistical Notes

Survey area
Oxfordshire, but concentrating on core office and industrial locations.

Offices
B1(a) and B1(b) units in excess of 5,000 sq ft with more than 50% office content.

Industrial
B1(c), B2 and B8 units in excess of 5,000 sq ft.

Stock
11.7m sq ft of Commercial Offices and 41.7 million sq ft of Industrial building. The local authority district of Oxford dominates, hence the dominance of Oxford within this survey. The chart below illustrates the proportion of total land area by each of the property types.

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