MARKET IN MINUTES
Savills Research

UK Commercial – March 2023

City Office Market Watch

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Slowing transaction speed is proving detrimental to take-up figures, but boosting under offers

February continued the precedent set in the previous month, with take-up faltering once more, reaching 268,341 sq ft across 17 deals. Collectively, 2023 has seen just 35 transactions totalling 672,877 sq ft – this is down on the previous year by 27% and down on the ten-year average by 9%. With slowing take-up, the 12-month rolling average has fallen for the third consecutive month.

One of the main reasons behind the muted start to the year is occupier cautiousness surrounding the macroeconomic environment. This has attributed to the increasing length of time that space remains under offer. Currently, on average, this space will stay under offer for 6.8 months – this is compared to 2.7 months this time last year and 5.4 months in 2020 (pre-Covid-19). This results in slower take-up and an accumulation of space under offer. At present, under offers total 2.1m sq ft, 49% above the long-term average of 1.4m sq ft.

Positively, the amount of space month-on-month going under offer provides confidence to the market. In February this totalled 358,036 sq ft, which is marginally higher than the monthly long-term average. It should also be noted that active demand requirements are still high when compared to historical levels, reaching 8m sq ft across the City and Central London – this is up 20% on the long-term average.

Construction cost inflation has its part to play in the reduced take-up figure. Occupiers are now reassessing requirements, with many including a 'Stay Put' option in their shortlists. The argument being that unless moving to best-in-class space, the cost of dilapidations and fit-out is too high to warrant moving to marginally better-quality space. This has further intensified the polarisation in the market, with 94% of take-up this year being Grade A.

Three of the five largest deals last month involved serviced office providers. The Office Group acquired the first and part second floor at the Blue Fin Building, 110 Southwark Street (43,000 sq ft) – the terms of the deal remain unknown.

Huckletree and etc.venues also acquired 32,096 sq ft and 23,000 sq ft, respectively. The increased activity from the sector sees serviced office providers account for 16% of year-to-date take-up – this is compared to lower levels post-pandemic. This resurgence is partially fuelled by the sizing and term flexibility they offer in times of unpredictability.

Frontier Economics pre-let the sixth, seventh and eighth floors at HB Reavis' Worship Square development, 65 Clifton Street, EC2 (32,725 sq ft), on a ten-year term with a break option in the fifth year. The economic consultancy firm is reportedly paying a blended rent of £88.00 psf. Increasing interest rates and inflation has led to higher borrowing and construction prices, as well as lower GDVs.

Additionally, a main driver of construction cost inflation is a skills shortage in the industry. This combination has led to an increasing amount of schemes being delayed and pushed back, squeezing the future supply of prime office stock. Only 45% of the 2023–2027 pipeline is under construction, with this being front-loaded. We anticipate that more schemes will fall behind schedule or fail to commence any form of works.

The 2023–2027 development pipeline is expected to see 16.0m sq ft of speculative space complete. When comparing to the average annual Grade A take-up figure of 5.4m sq ft, there is a clear deficit that will continue to bolster prime rental forecasts. At present, 19% of the pipeline is pre-let – this figure continues to grow as demand for prime office buildings grows amidst a quick narrowing of supply. It must be noted that the proportion of pre-let will rise further still as more space is pushed further back on the pipeline.

672,877 sq ft year-to-date take-up, across **35** deals

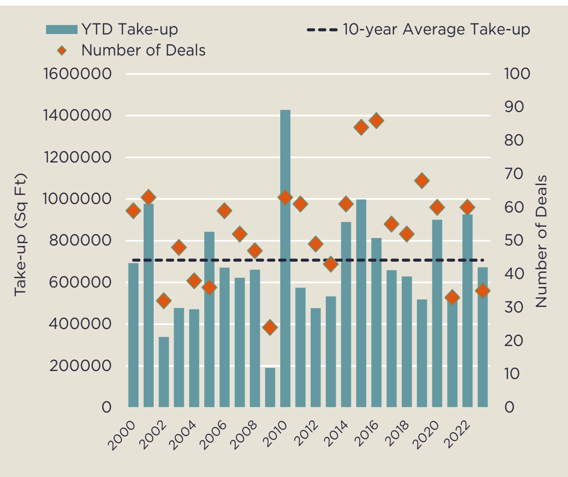
On average, units remain under offer for **6.8 months,** up **12%** on pre-pandemic levels

Serviced Office Providers have accounted for **16%** of year-to-date take-up

Active requirements for the City & Central London have surpassed **8m sq ft**

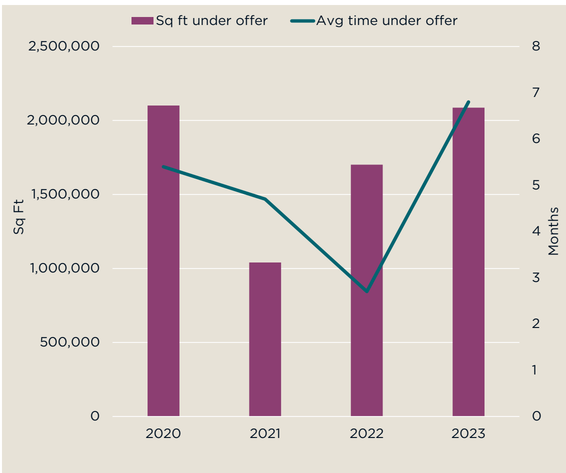
City year-to-date take-up

Graph 1



City under offer duration

Graph 2



Source: Savills

Analysis close up

Monthly take-up

Table 1

	Sq ft	% Grade A	12 month rolling take-up
Mar-22	488,201	92%	5,445,535
Apr-22	288,470	91%	5,372,878
May-22	897,729	93%	6,061,729
Jun-22	562,665	91%	6,409,946
Jul-22	172,117	91%	6,189,240
Aug-22	256,626	91%	5,843,350
Sep-22	845,413	90%	6,468,560
Oct-22	153,318	91%	6,128,265
Nov-22	815,422	92%	6,184,304
Dec-22	417,937	92%	5,823,927
Jan-23	404,536	91%	5,894,781
Feb-23	268,341	94%	5,570,775

Supply

Table 2

Total	% Grade A	% chg on prev month	Vacancy rate (%)
12,985,821	87%	5%	9.3%
12,933,492	87%	0%	9.3%
12,669,761	87%	-2%	9.1%
12,715,255	86%	0%	9.1%
12,862,646	86%	1%	9.2%
13,309,212	86%	3%	9.5%
13,413,477	86%	1%	9.6%
13,464,167	86%	0%	9.6%
13,238,224	85%	-2%	9.5%
13,354,569	86%	1%	9.6%
13,546,203	87%	1%	9.7%
13,358,967	87%	-1%	9.5%

Year to date take-up

Table 3

	Sq ft	% change on previous year	% Grade A
Jan 22 - Feb 22	926,029	81%	93%
Jan 23 - Feb 23	672,877	-27%	94%

Development pipeline

Table 4

Sq ft	Refurb	Devs	Total	% Pre-let
2023	1,415,825	2,527,351	3,943,176	38%
2024	1,833,389	2,753,110	4,586,499	27%
2025	2,311,123	1,328,840	3,639,963	11%
2026	750,000	2,291,000	3,041,000	19%
Total	6,310,337	8,900,301	15,210,638	24%

Rents

Table 5

£ per sq ft	Top	Average			
		Grade A	Grade B	Prime*	Rent free**
Mar-22	£103.50	£65.26	£44.00		25
Apr-22	£87.50	£69.83	£43.75		
May-22	£90.00	£67.83	£45.07		
Jun-22	£105.00	£65.85	£47.12	£83.72	23
Jul-22	£87.00	£71.63	£45.27		
Aug-22	£90.00	£71.15	£35.15		
Sep-22	£103.50	£67.51	£45.12	£85.61	24
Oct-22	£73.50	£63.02	£37.50		
Nov-22	£107.00	£73.58	£60.94		
Dec-22	£93.00	£64.35	£49.50	£88.36	23
Jan-23	£81.00	£71.10	£39.00		
Feb-23	£88.00	£68.02	£50.00		

Demand & Under-offers

Table 6

City Potential Requirements (sq ft)	2.0m
City Active Requirements (sq ft)	8.0m
City Total Requirements (sq ft)	10.0m
% change on 12 month ave	-4%
Total under offer (sq ft)	2.1m
Under offer this month (sq ft)	358,036
% change on average (total)	49%
Landlord controlled supply	75%
Tenant controlled supply	25%

*Average prime rent is for preceeding 3 months

** Average rent free on leases of 10 years with no breaks for preceding 3 months

Note: Completions due in the next 6 months are included in the current supply figures

Significant February transactions

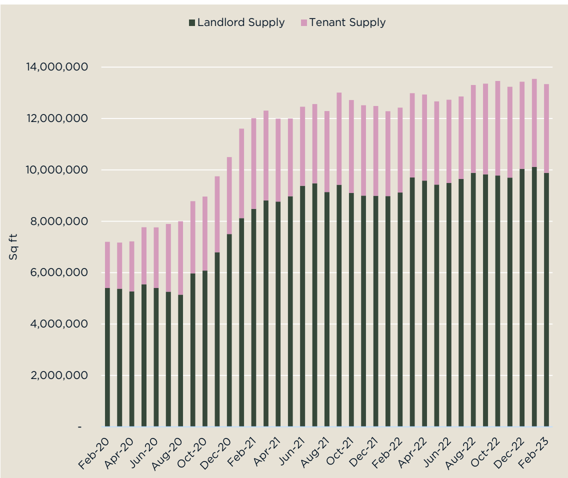
Table 7

Address	Floor/s	Sq ft	Grade	Rent achieved	Tenant	Lessor
Blue Fin Building, 110 Southwark Street, SE1	1, part 2	43,000	A	Confidential	The Office Group	Oxford Properties
Worship Square, 65 Clifton Street, EC2	6, 7, 8	32,725	A	£88.00	Frontier Economics	HB Reavis
199 Bishopsgate, EC2	1, 2, 3	32,096	A	Confidential	Huckletree	British Land/GIC
The Featherstone Building, 58-64 City Road, EC1 Y	5-8	31,057	A	£74.50	Buro Happold	Derwent
155 Bishopsgate, EC2	2	23,000	A	Confidential	ETC Venues	British Land/GIC

In Focus - Tenant-controlled supply analysis

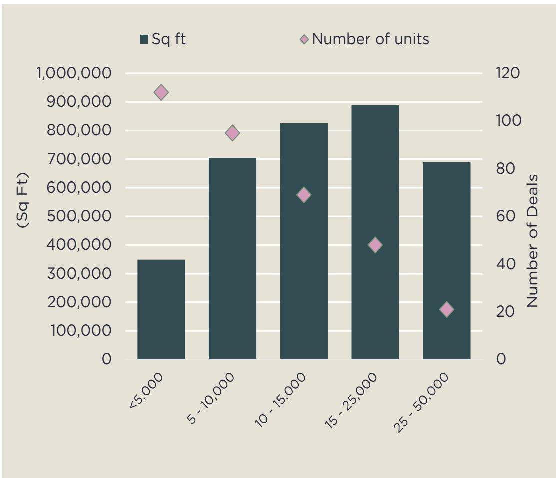
City landlord vs tenant supply

Graph 3



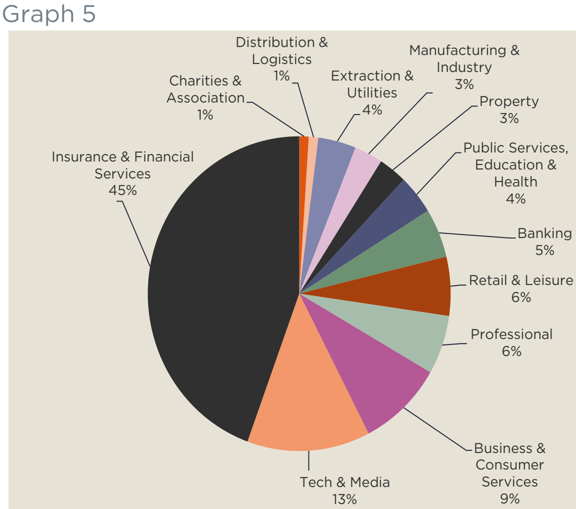
City tenant supply by size-band

Graph 4



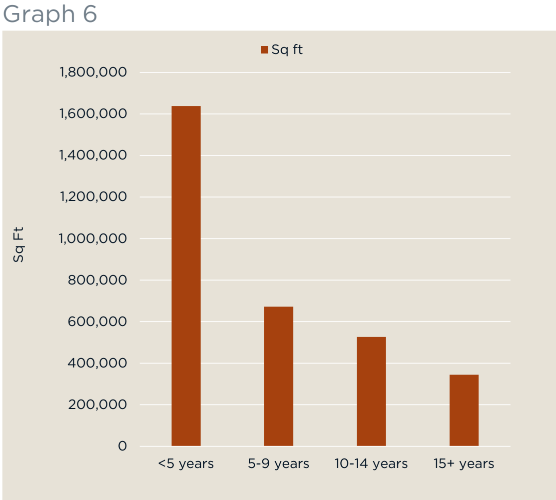
Known City tenant supply by business sector

Graph 5



City tenant supply by lease term

Graph 6



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