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City Property Development

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Times

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Agenda

- The City Development Market
- Where is the development finance?
- What the future could hold

The City Development Market

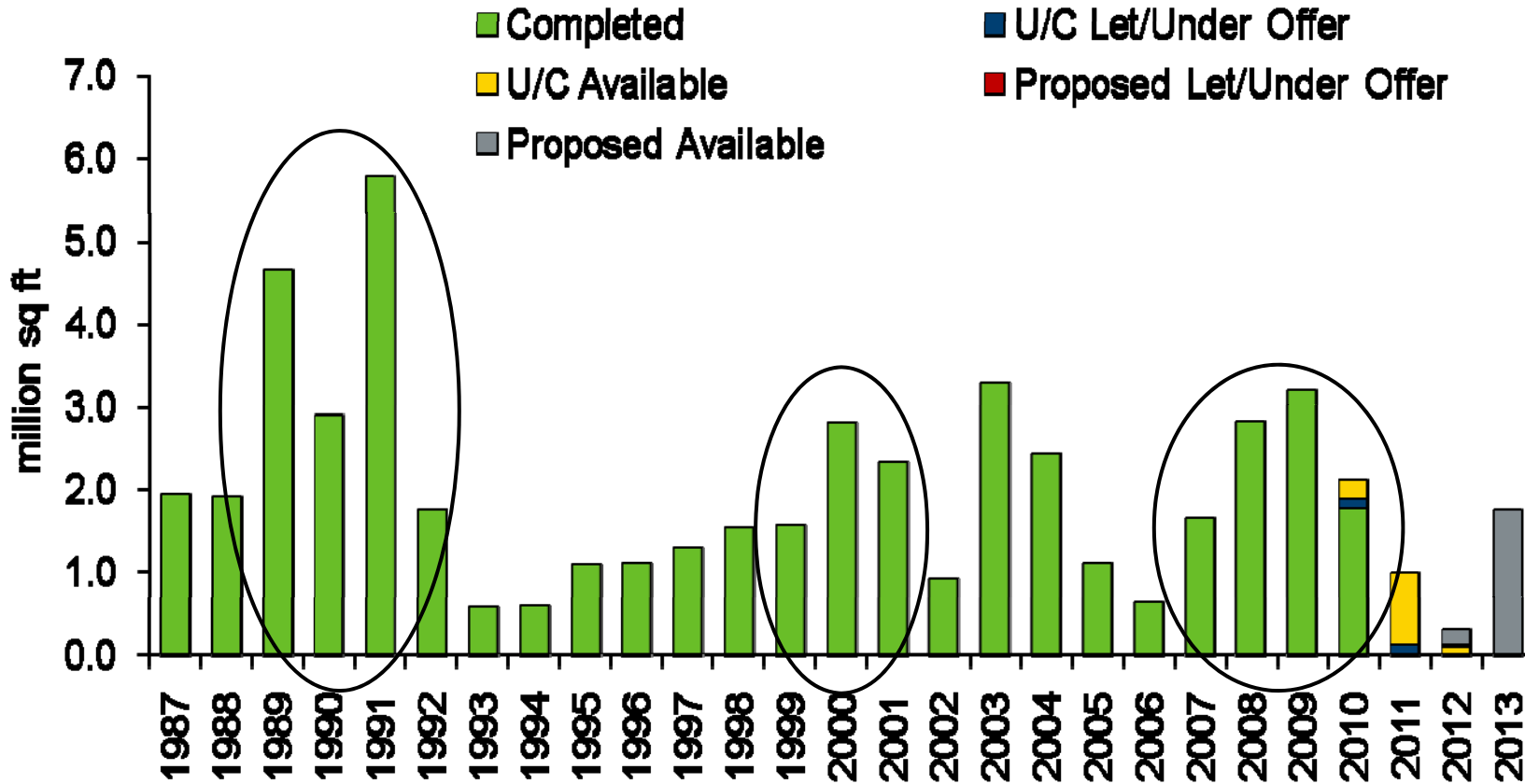


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City Developments

1985 - 2013



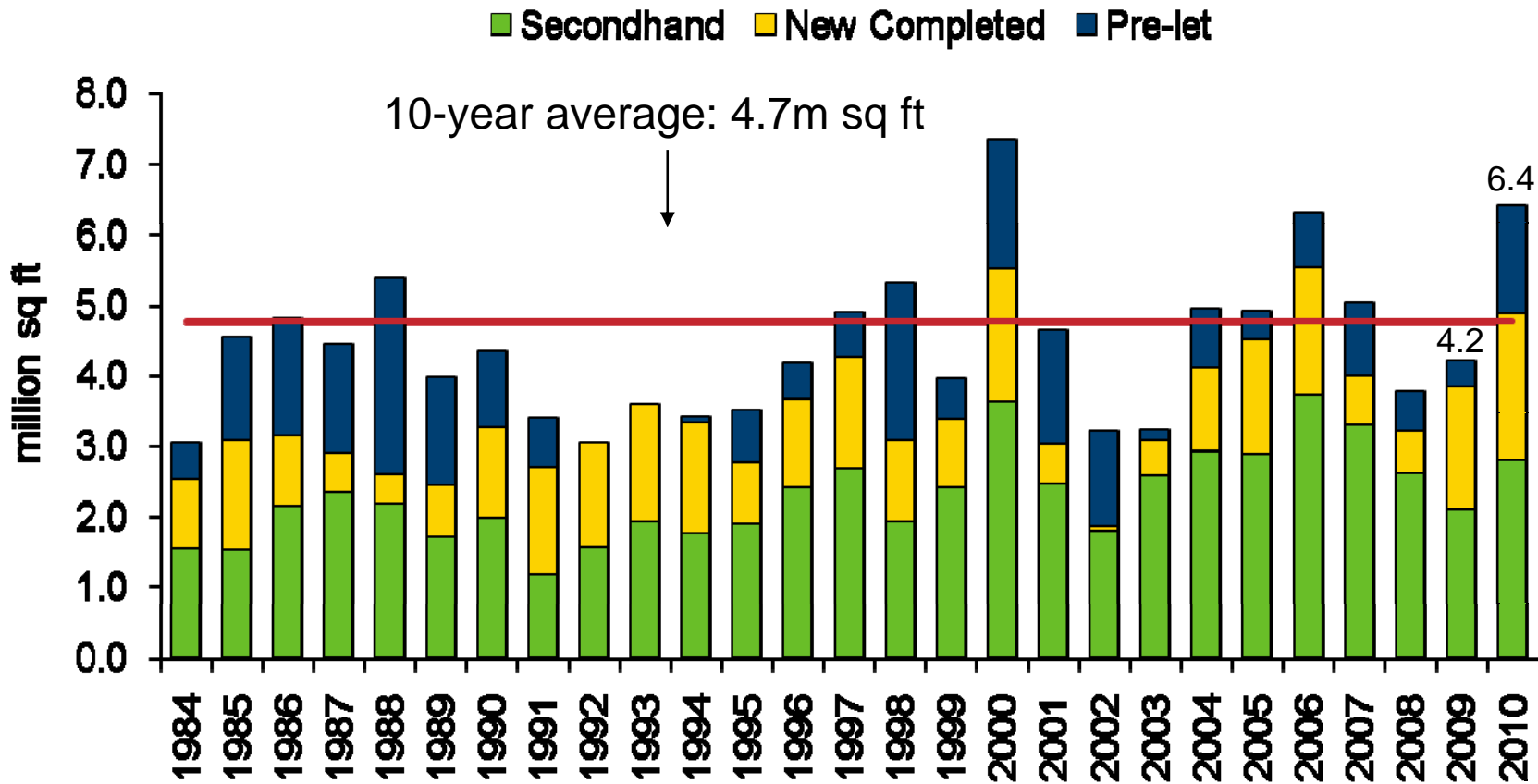
Source: CB Richard Ellis

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City Annual Take-up

52% above of 2009 take-up

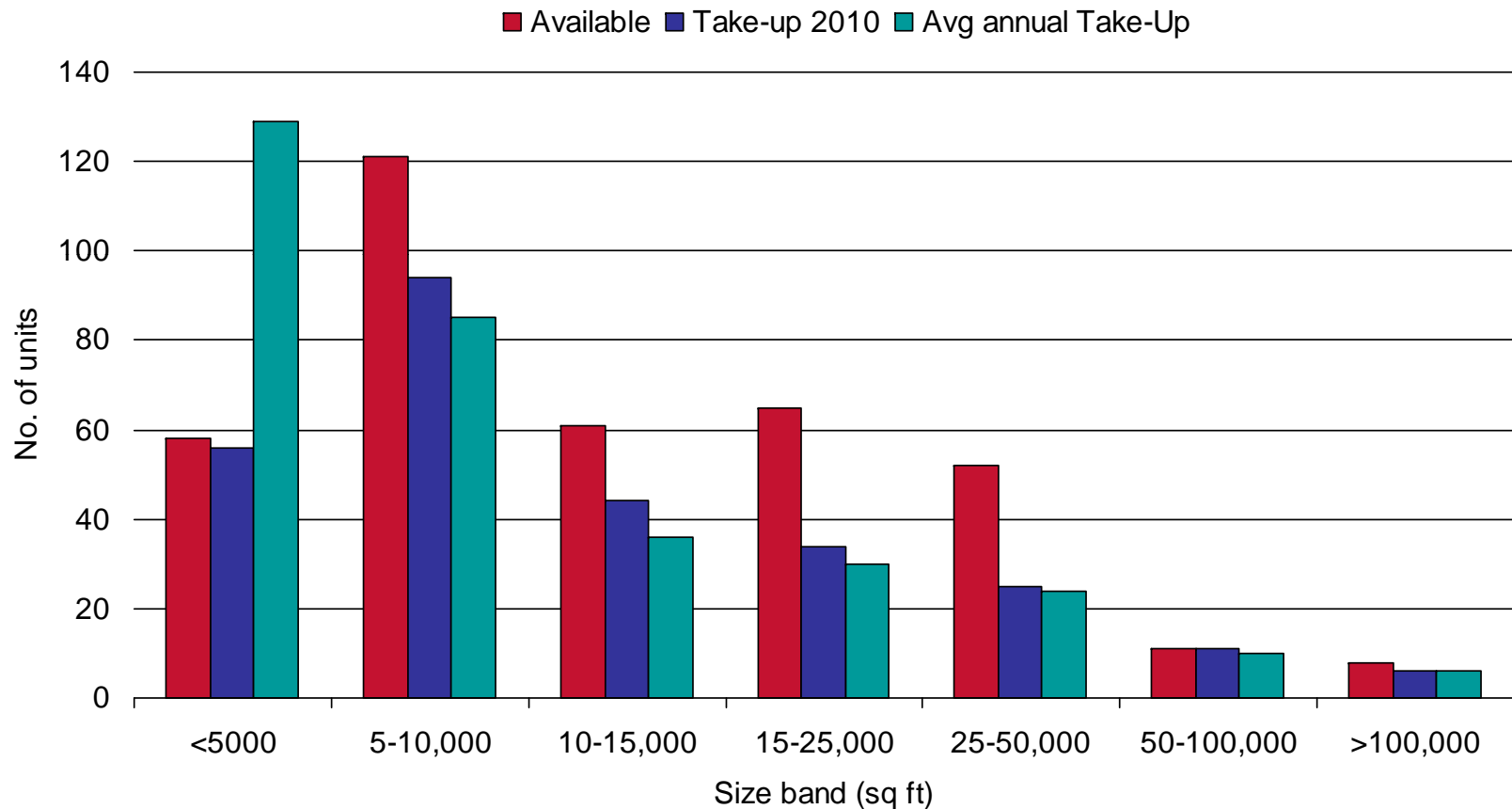


Source: CB Richard Ellis

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There is undersupply of some types of property

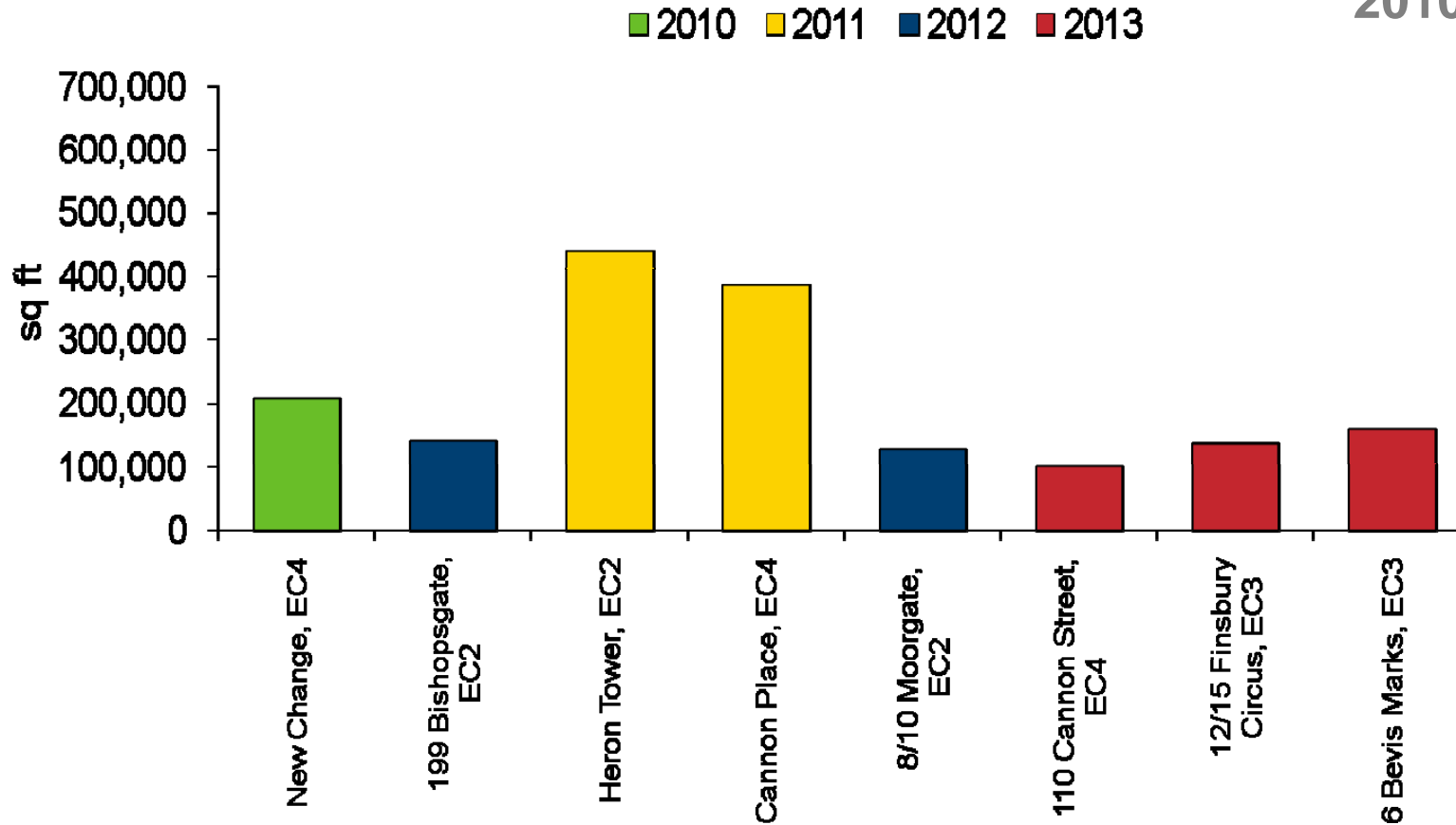


Source: Savills

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Major City Developments

2010 - 2013



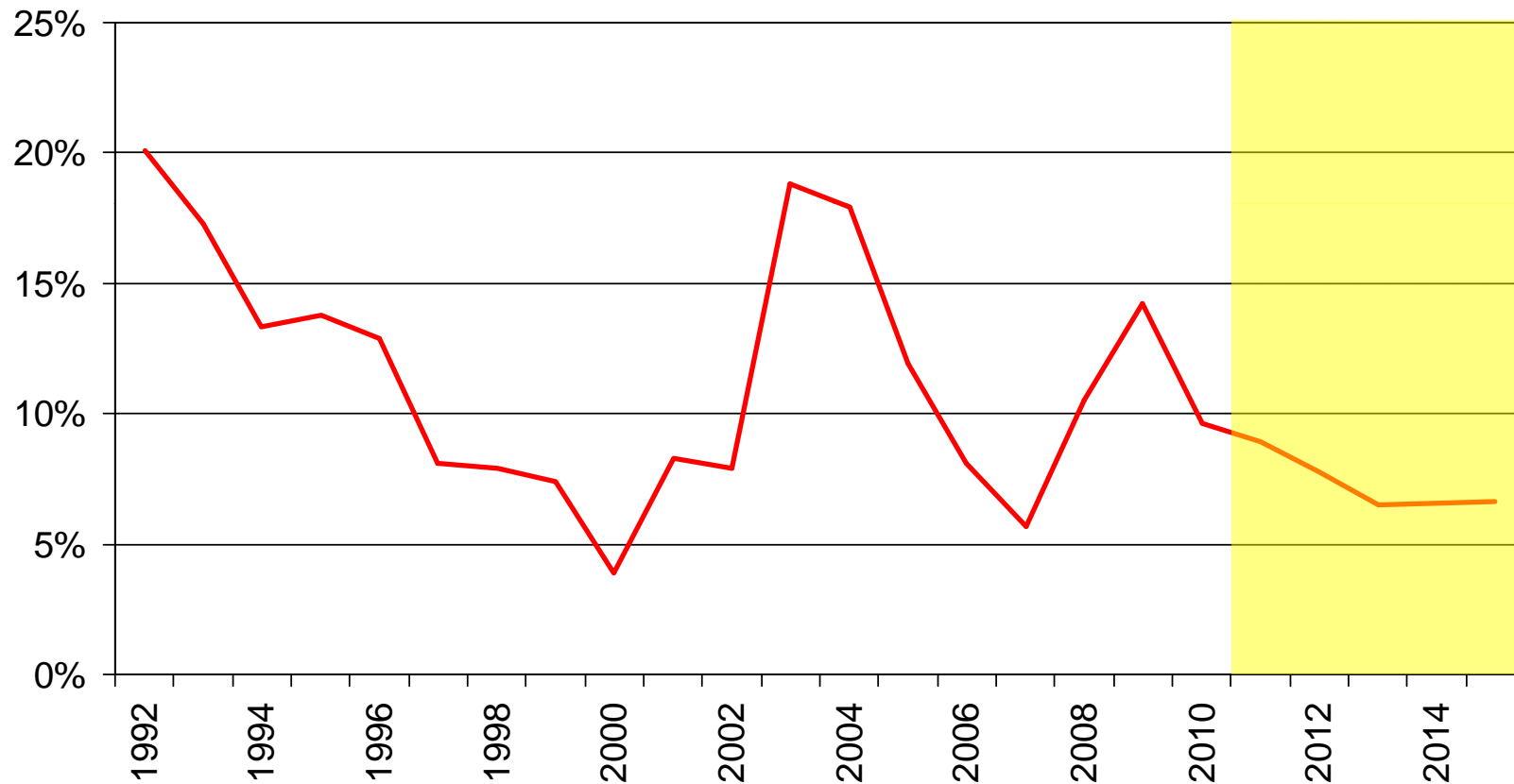
Note: Figure shows schemes with speculative element of 100,000 sq ft or more, excluding completed schemes

Source: CB Richard Ellis

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Vacancy rate will remain on a downward path until development completions pick up in 2014/15



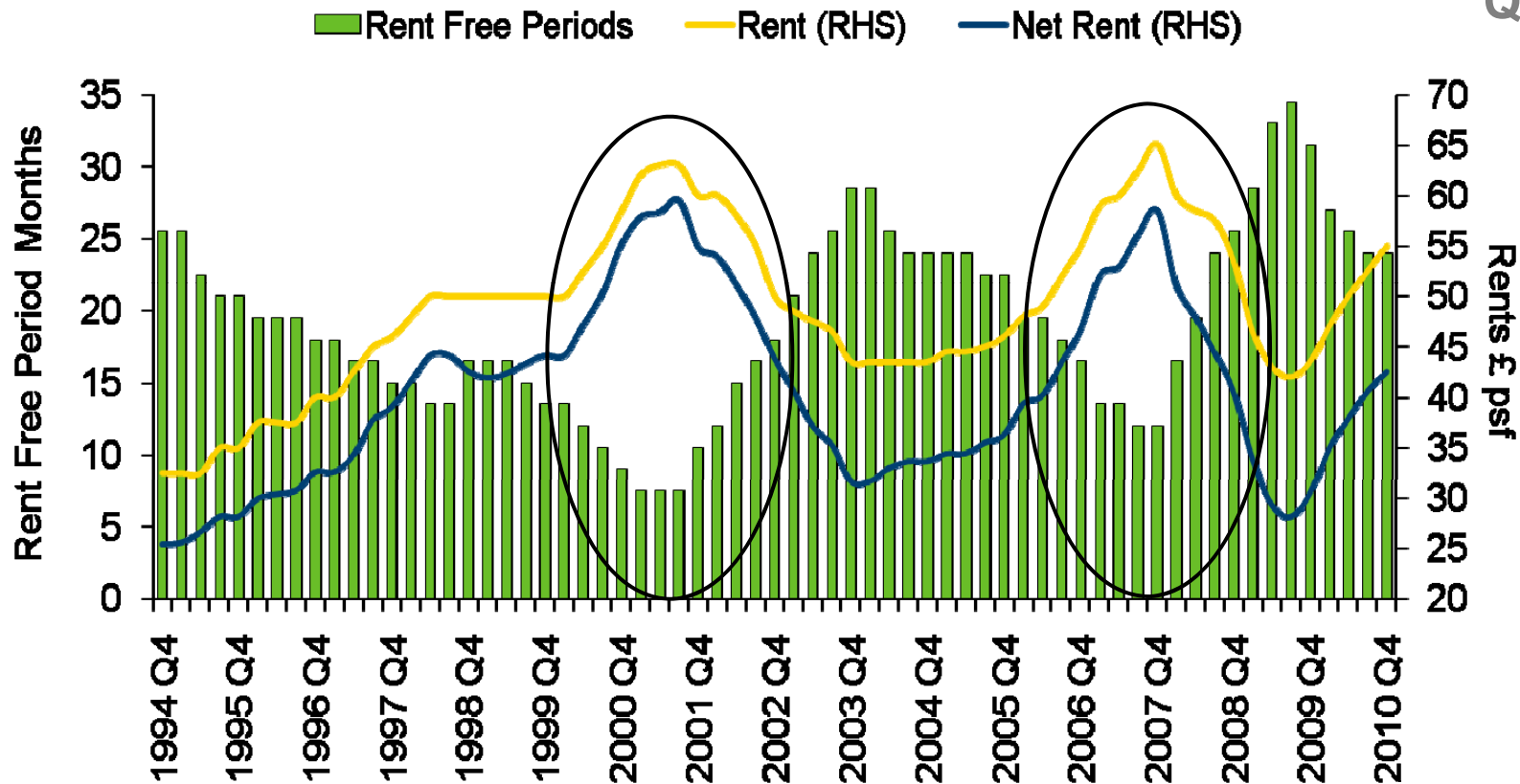
Source: Savills

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City Top Prime Rents vs Rent Free Periods

Q4 2010



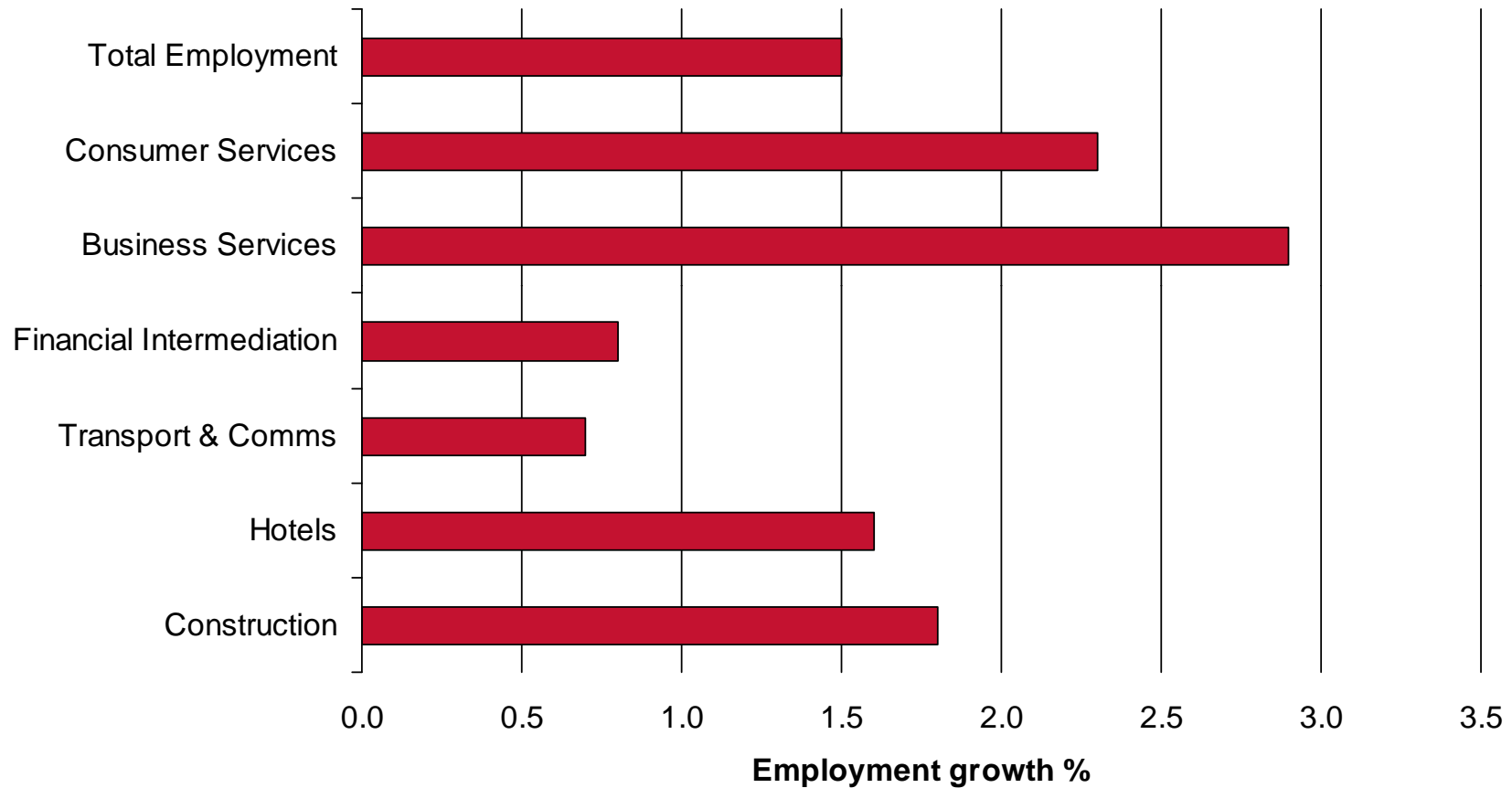
Note: The net effective rent is calculated using a DCF over 10 years @7% and assumes a 3 month fitting out period

Source: CB Richard Ellis

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City of London in 2012 – Back to Employment Growth

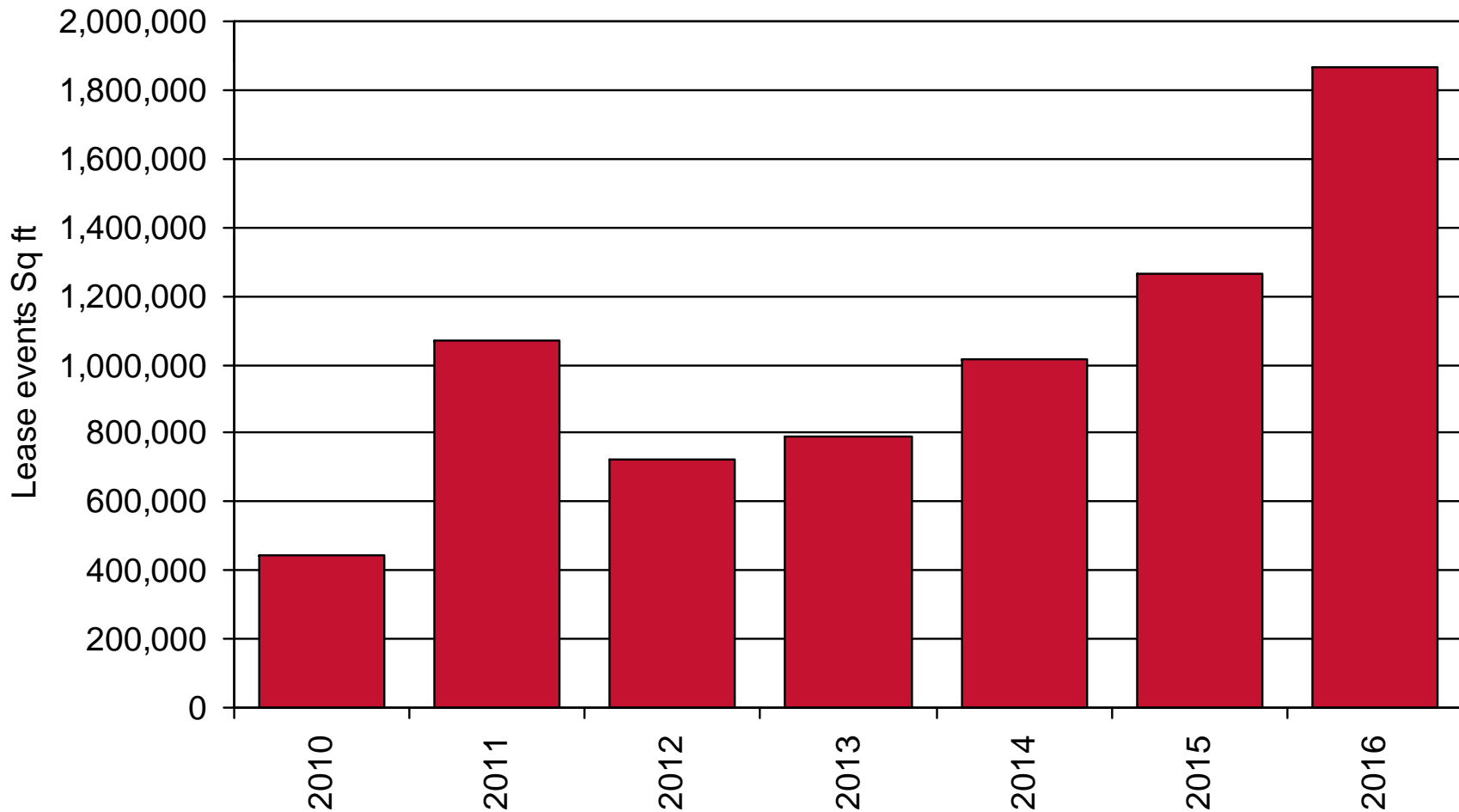


Net growth of 6,000 jobs in 2011 and 2012, back to peak level of office-based jobs in 2012

Source: Oxford Economics

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So, what else will drive demand?



Source: Savills

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Lawyers have been major players in the last five years – will they still be?

Global law firms by share of M&A advice - 2010

| Firm | Deals advised on \$bn | In London | Moved recently? | Likely to move within 3 yrs |
|-----------------------------------|-----------------------|------------|-----------------|-----------------------------|
| Skadden | 268.7 | YES | NO | |
| Sullivan & Cromwell | 243.3 | YES | NO | |
| Freshfields Bruckhaus | 209.0 | YES | NO | |
| Linklaters | 194.1 | YES | NO | |
| Simpson Thacher | 194.0 | YES | NO | |
| Cleary Gottlieb | 181.1 | YES | NO | |
| Wachell Lipton | 169.1 | NO | - | |
| Latham & Watkins | 165.1 | YES | NO | |
| Allen & Overy | 134.6 | YES | NO | |
| Dewey & LeBoeuf | 130.9 | YES | NO | ✓ |
| Shearman & Sterling | 113.7 | YES | NO | |
| Davis Polk & Wardwell | 113.1 | YES | NO | |
| Clifford Chance | 109.6 | YES | NO | |
| Gibson Dunn & Crutcher | 108.5 | YES | NO | ✓ |
| Blake Cassels & Graydon | 103.8 | YES | NO | |
| Craveth Swaine & Moore | 103.5 | YES | NO | |
| Vinson & Elkins | 102.6 | YES | NO | |
| Herbert Smith | 93.4 | YES | NO | |
| Jones Day | 81.5 | YES | NO | |
| Debevoise & Plimpton | 81.0 | YES | NO | ✓ |

Source: Reuters M&S league table, Savills

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What about Banks?

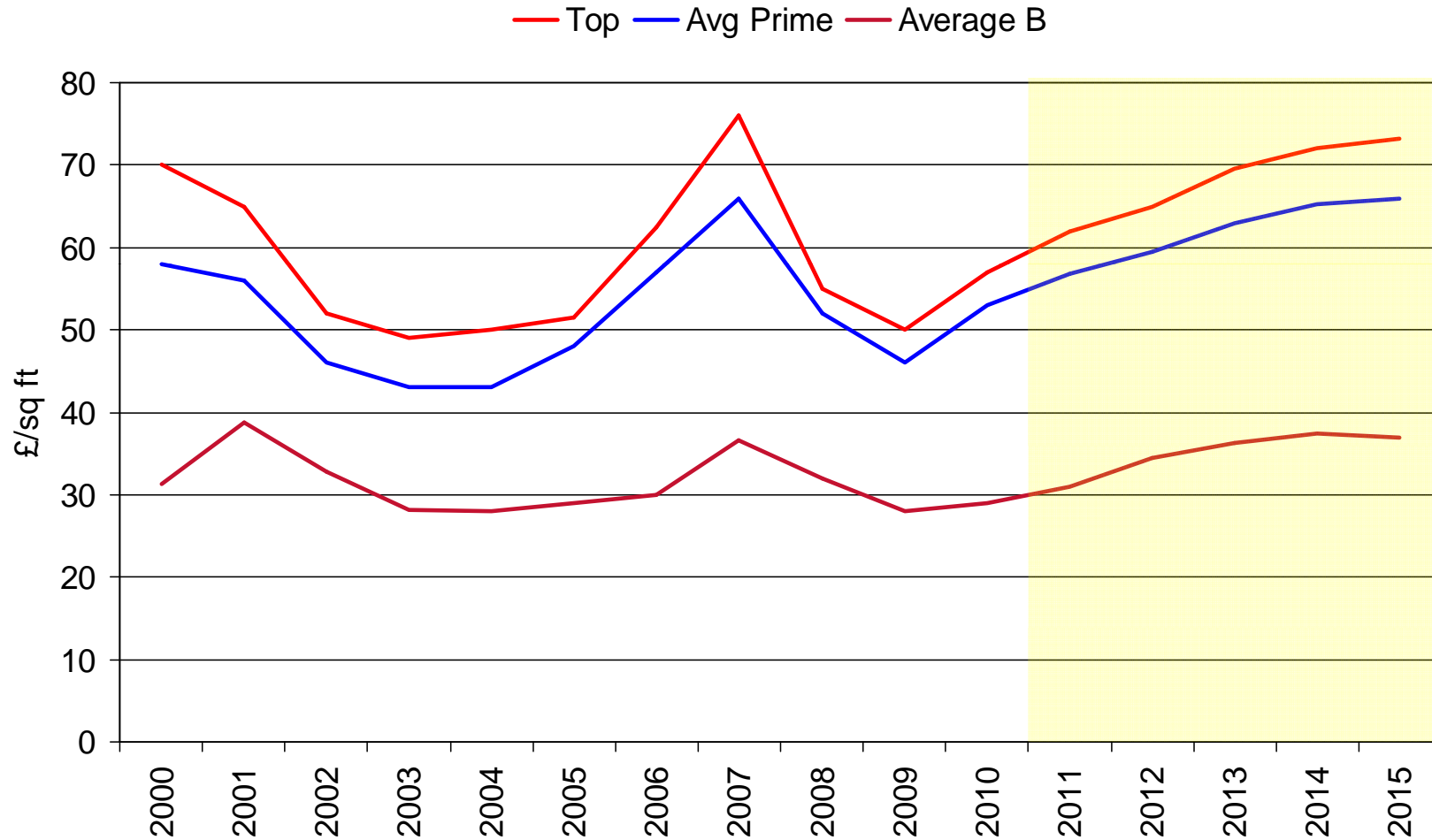
| Bank (by size) | Turnover 2010 vs 2009 | Possible requirement? |
|------------------------|--------------------------|--------------------------|
| Goldman Sachs | 1.5% | ✓ |
| Morgan Stanley | 12.8% | ✓ |
| Credit Suisse | 12.4% | |
| Deutsche Bank | 12.3% | ✓ |
| Barclays Capital | 25.2% | ✓ |
| UBS | 8.6% | |
| RBC Capital Markets | 38.5% | ✓ |
| Wells Fargo | 14.7% | ✓ |
| Mizuho Financial Group | 30.3% | ✓ |
| Lazard | 25.3% | |
| Rothschild | 6.8% | |
| Jefferies & Co | 78.6% | ✓ |
| Sumitomo Mitsui | 73.9% | ✓ |

Frank-Dodd reform act means that all US banks will be spinning out prop trading e.g. Morgan Stanley 60 people in London

Source: Savills

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Grade A rents to rise steadily as supply shortage intensifies



Source: Savills

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Market Conclusions

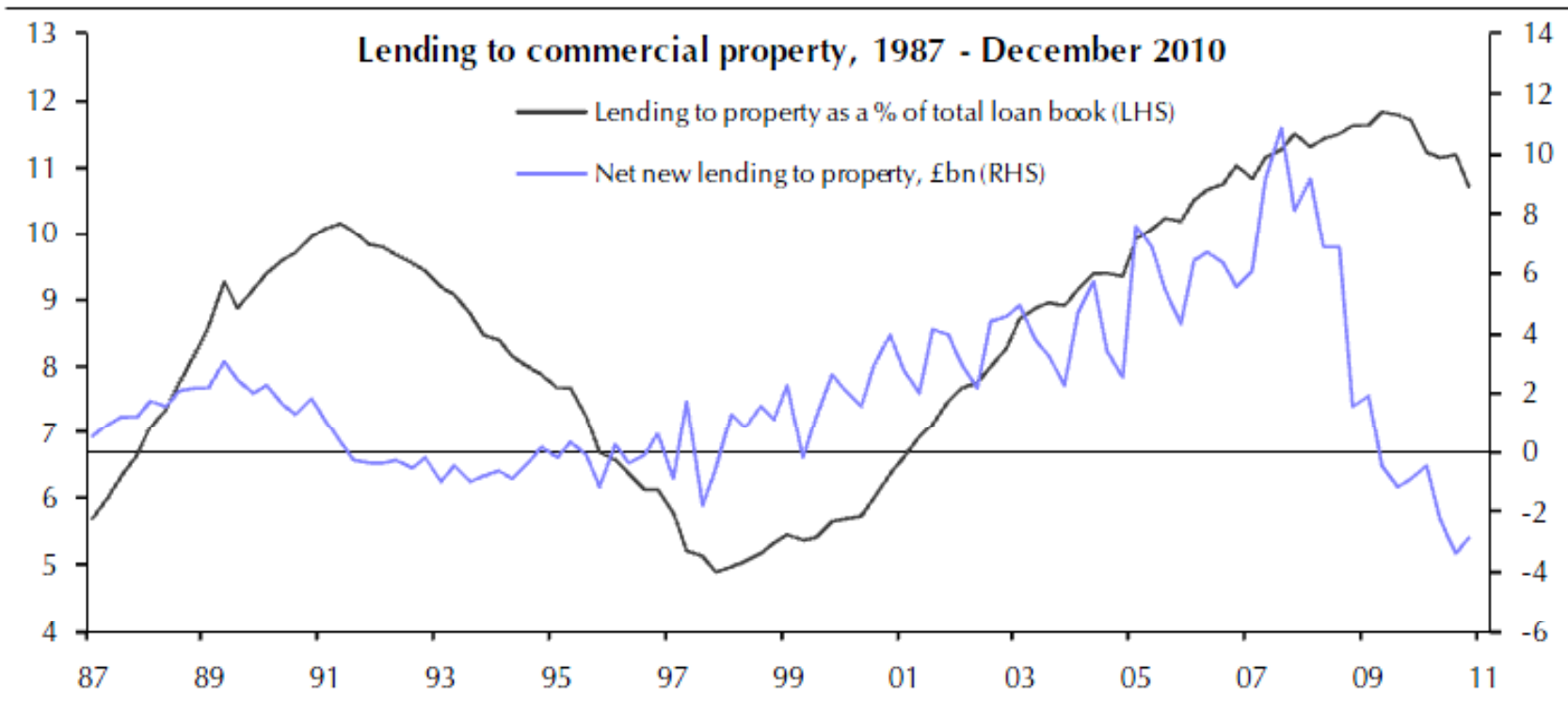
- Recovery is underway, but demand will remain driven by lease events rather than a jobs boom
- Undersupply will be the driver of rental growth
- Undersupply is most prevalent in units of 50,000 sq ft and above
- **Cautious lenders will restrain development pipeline**, but 2015 and beyond is hard to predict

Where is the Development Finance?



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Banks are focused on sorting out existing loans



Source: Capital Economics

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But sources of funding have changed

| | |
|-------------------------------|------------------------|
| Institutional forward funding | Limited availability |
| Balance sheet | Shareholder wary |
| Contractor funding | Little appetite |
| Bank funding | Equity bridge required |

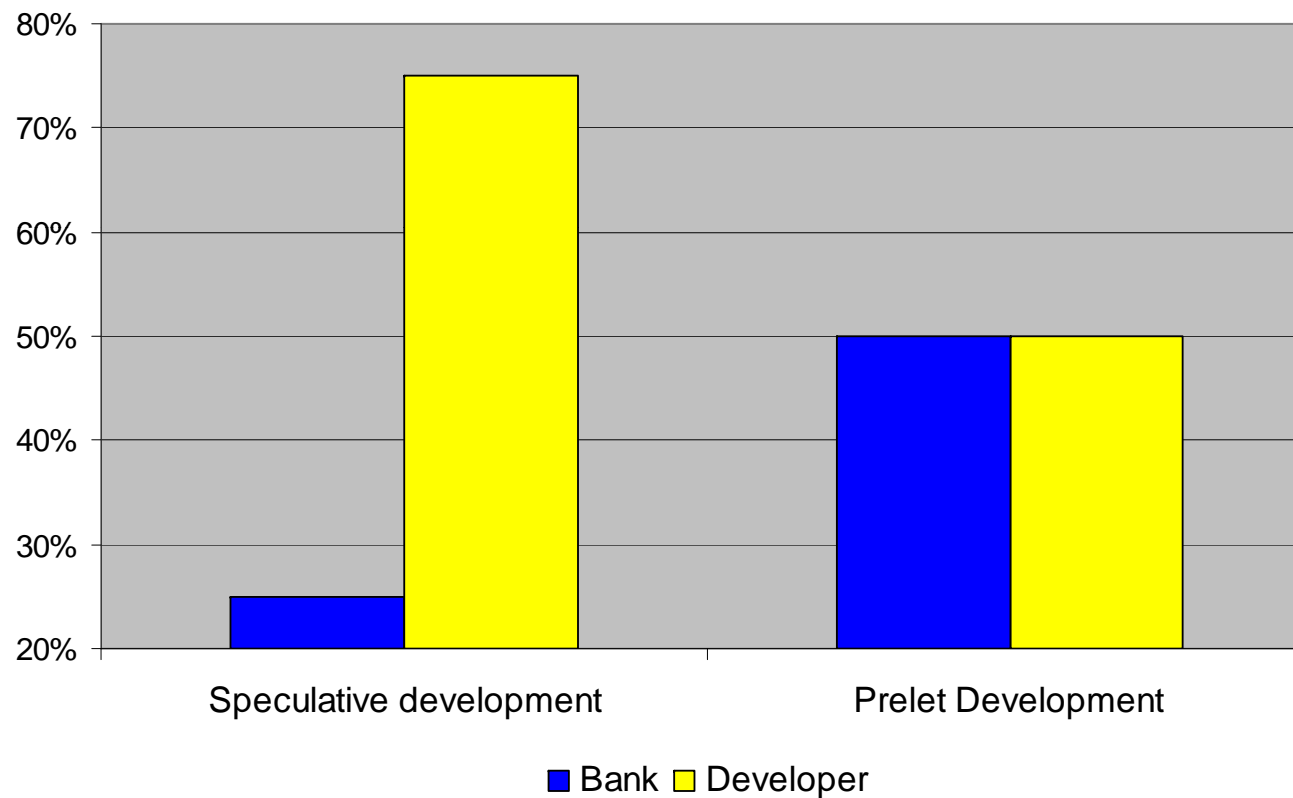
Speculative vs Prelet models

- Development is a risk purchase
- Who is best placed to take this risk?

Developments Risks

- Land & tenure issues
- Entitlements / adjoining owners
- Construction costs
- Programme certainty


Who is funding the gap?



Source: Hines

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What does this mean to the development industry?



- Smaller buildings or refurbishments
- More prelets with longer leases
- Greater use of GMP contracts
- Hedging of variable costs
- Partnering where possible
- Shorter programmes to deliver to a known market

Who will be the Investors?

| | | | |
|---|--|--|---|
| <p>UK REITs</p> <ul style="list-style-type: none"> • Well financed • Will to take on development risk | <p>UK Funds</p> <ul style="list-style-type: none"> • Inflows likely to increase • Limited development • £25-£50m | <p>Opportunity Funds</p> <ul style="list-style-type: none"> • Geared returns 15% IRR + • Development difficult | <p>German Funds</p> <ul style="list-style-type: none"> • Open ended • Grade A only £75-200m • Limited speculative development |
| <p>Overseas High Net Worth</p> <ul style="list-style-type: none"> • £25-200m • Prime only • Low risk assets • No development | <p>Far East Institutions</p> <ul style="list-style-type: none"> • Core income • Grade A • Limited development | <p>Middle East Investors</p> <ul style="list-style-type: none"> • £100m + • Possible development • £100m + | <p>SVFs</p> <ul style="list-style-type: none"> • Equity investors • £100m + • Speculative development • Core assets |

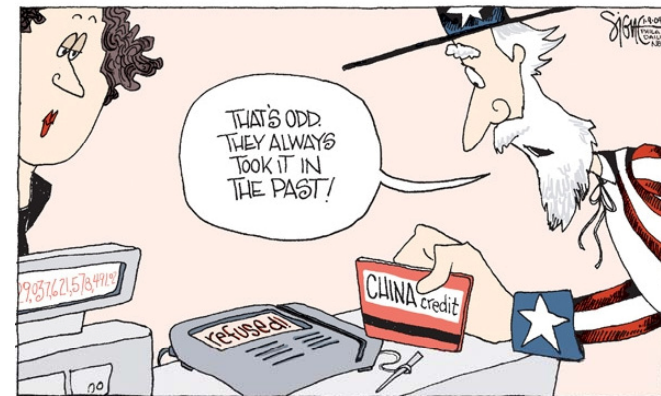
Financing – In and Out



- Equity
- Debt – lower leverage
- Simple CMBS
- Personally managed pensions
- Sovereign wealth funds
- Phantom equity workouts with banks
- Sharia finance
- Increased regulation



- Debt – high leverage
- CDOs and everything that looks like it
- Final salary pension funds (Hermes etc.)
- Equity guarantees



What will the future hold for City development?

- Clear rental growth prospects until 2015
- Reduced supply of speculative buildings
- Smaller buildings with shorter programmes
- Greater price volatility
- Entry of international investors, especially SWFs to exploit situation
- A return to cyclical development?

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