Farebrother
CHARTERED SURVEYORS

Knight Frank

Fox Court, 14 Gray's Inn Road

Marketing Agent's Statement in Support of Planning Application

On behalf of The Trustees of the Rockspring Hanover Property Unit Trust

February 2013

The purpose of this report is to provide background market information in support of the proposed redevelopment of Fox Court, and will encompass three main issues, as follows:

First, we have provided a critique of the existing building, explaining both its weaknesses and strengths as well the recent loss of the largest tenant in the building, Interpublic, and the need to substantially refurbish the building in order to fill this void;

Secondly, we have provided an overview of the Central London office market, with specific commentary on the Midtown sub-market within which the building is situated;

And finally, we have provided a commentary on the proposed scheme, demonstrating how the deficiencies identified in the first section will be addressed.

1. ASSESSMENT OF EXISTING BUILDING

1.1 Weaknesses & Deficiencies

We have identified several aspects of the existing building that are likely to be perceived negatively by a prospective tenant and which would remain a hindrance if they are not addressed. They are:

- The main reception area on Gray's Inn Road is small and poorly configured, resulting in a weak arrival experience. The existing reception area is 1,369 sq ft, comprising 1.33% of the total Net Internal Area of the building. To place this in context, we would expect the reception areas in new 'Grade A' buildings to be between 2-3% of the total NIA. At Fox Court, this restriction is compounded by the fact that the reception area has poor street presence, owing to the fact that it is raised above pavement level and accessed by either steps or the disability ramp. The presence of a bus stop immediately outside the main entrance and poor external signage also detract from the arrival experience.

- The configuration of the office accommodation on the lower floor plates lacks flexibility, which restricts the way in which a prospective tenant may wish to occupy the space. In particular, the eastern end of the floor plate can only be accessed via the secondary service core on Brooke Street which restricts connectivity across the floor and the long, thin nature of the floor plate is also unattractive.

- The courtyard area to the north of the building has really only been used by the lower floor occupier and it detracts from the overall appearance of the building. It appears to be largely unused and offers an unattractive outlook from the upper floors of the building. This area provides an opportunity for dramatically improving the asset, both by providing additional office and retail accommodation, for which there is clear demand, and also some good quality outdoor space for which tenants will be prepared to pay a premium.

- As a general comment, the common parts to the building are in a tired and dated condition. Whilst this is largely a cosmetic issue, it highlights the age of the building and may lead prospective occupiers to have concerns regarding the lifespan of the M&E, the future running costs of the building and the impact these may have on the service charge.

- The lifts in the Gray's Inn Road core are operating at their absolute maximum capacity and are unsuitable for a modern office building. They are badly in need of a major overhaul.

- As it stands, the vacant office accommodation in Fox Court, which comprises some 53,000 sqft, might be graded as B minus space and is very much in need of a major improvement if it is to cater for the demands of 21st century occupiers.

1.2 Strengths & Advantages

Despite the weaknesses outlined above, both the building and the location benefit from many advantages that will be seen as beneficial by occupiers:

- The location benefits from excellent transport links, with Chancery Lane Underground Station within two minutes' walk, whilst Farringdon and City Thameslink stations are within 10 minutes' walk. The transport links across Central London will be further enhanced with the addition of Crossrail in 2018 (which will stop at Farringdon).

- The building benefits from a double aspect with entrances on both Gray's Inn Road to the West and Brooke Street to the East. At present, the Brooke Street entrance is used predominantly by a single tenant (Trillium), however the ability to offer this second entrance to tenants in the future will be beneficial in allowing flexible subdivision of the floors.

- The close proximity to the shops and services along High Holborn will be an important consideration for prospective occupiers. There are a variety of 'everyday' retail outlets on High Holborn including Eat, Starbucks and M&S Simply Food but also destination restaurants, bars and hotels in Clerkenwell and Farringdon (such as The Bleeding Heart, Zetter and Smiths of Smithfield).

- As a business location, Midtown has improved dramatically over the last 10 years and is now home to a diverse range of occupiers from the legal, corporate, financial and media sectors. Nearby office developments such as New Street Square have cemented the reputation of Midtown as an alternative to the traditional office markets of the City and West End. Over the last two years, the growth of the TMT sector, focused around 'Silicon Roundabout', has spread across to Clerkenwell and Farringdon, and the building is well placed to take advantage of this active business sector. Initiatives such as the Midtown Business Club and the Midtown Business Improvement District will help to ensure this trend continues over the next few years.

- The building has ample space for tenant facilities at basement level, in particular secure cycle storage and shower facilities. These facilities are limited at present but they will be provided as part of the proposed development scheme and they are increasingly important to occupiers. They will be offered as part of the base building provision on other competing buildings in the area.

1.3 Background to Redevelopment

Interpublic (with their group companies Weber Shandwick, Golin Harris and Futurebrand) were formerly the largest single tenant within the building, occupying approximately 45,000 sqft over the ground to third floors. Their lease expired in September 2012, and although efforts were made to persuade them to re-new their lease, these discussions were not successful. It appears that the main motivating factor for Interpublic leaving the building was the poor quality and specification of their office space, combined with the dated common parts and a general desire to improve their working environment. Whilst it would have been possible to undertake a refurbishment with the tenant in-situ, this would have resulted in significant disruption to business continuity, which they were keen to avoid.

The three buildings which were short-listed by Interpublic were 2 Waterhouse Square, EC1 (ultimately their chosen option), 200 Aldersgate, EC1, and 123 Victoria Street, SW1. All three of these buildings are comprehensive refurbishments (as opposed to new buildings) offering good quality office accommodation at a rental discount to brand new stock. Clearly the intention is now to replace them with another tenant (or tenants) of a similar or better covenant strength, on an institutional lease term (10 years minimum) and on the best financial terms achievable. In order to achieve this, the redevelopment of the building is essential in order to re-position the building in-line with the competition – the most direct comparable being 2 Waterhouse Square.

It is noted that the 6th floor (comprising 8,151 sqft) has already undergone a cosmetic refurbishment, although it is not the intention to actively market this space until the wider redevelopment works have been completed. This is for two reasons: firstly, it is difficult to market the space to prospective occupiers in the knowledge that they will face up to 12 months of significant disruption whilst the redevelopment works are undertaken; secondly, it is the intention to align the rental tone of the 6th floor with the 'new' (i.e redeveloped) building, rather than the 'old' existing building, and this will only be possible when these works are complete, including the upgraded entrance, reception and lifts on Gray's Inn Road.

2. OVERVIEW OF CENTRAL LONDON OFFICE MARKET[1]

2.1 Demand & take-up

The Central London occupational market received a welcome boost in the final quarter of 2012 as take-up rose to almost 3.0 m sqft, the highest since Q3 2011 and above the long-term average. The City performed particularly well, recording the highest level of activity for more than two years. In the West End take-up also rose, recording the strongest quarter in more than 12 months. However, on an annual basis, year-by-year take up remains significantly below the long term average across Central London.

There has been limited activity from the financial sector in 2012, however the insurance and technology, media & telecoms (TMT) sectors have been particularly active. TMT was the most active sector accounting for almost 30% of all take-up across Central London in 2012. There have been some significant headline transactions from insurance sector occupiers, focused on new City stock. We expect continued demand from both of these occupier sectors into 2013.

2.2 Supply

Availability rose marginally in the final quarter to 16.6 m sqft, although this remains well below the long-term average of 20.0 m sqft. This rise reflects the entry of The Place, London Bridge Quarter, SE1, 10 & 30 Brock Street, W1 and 62 Buckingham Gate, SW1 in to the year-end figures. These new developments are due to reach practical completion within the next 6 months and total around 850,000 sqft. Significantly, the availability of second-hand space is now just 10.5 m sqft, a fall of 1.0 m sqft since the previous quarter and 20% below the long-term average of 13.3 m sq ft,

[1] Market statistics provided by Farebrother & Knight Frank research.

2.3 Micro – London Midtown Office Market - 2012

Fox Court sits within the Midtown market of Central London, which comprises approximately 33.5m sqft of office stock. All the numbers and statistics mentioned below relate to this market, which is broadly bordered by Tottenham Court Road to the West, Euston Road to the north, Farringdon Road/Street to the east and the River to the south. The boundary is shown on the map below.

2012 was a year of two halves for the Midtown office market. Despite underperformance in the first half of 2012, better take-up, a lower availability rate and well-above average investment turnover in the 3rd Quarter, together with a reasonable, if unspectacular, 4th quarter, made for a more positive year end. So much so that total take-up for the year exceeded Farebrother's projection of 1.6m sqft, finishing the year at a healthy 1.66m sqft.

Despite take up in Q4 being 28% down on Q3 the year still ended positively with the availability rate continuing to fall. It has now dipped below 5% level and ended the year at just 4.7%. This is mainly on the back of a good level of take up in the second half of the year (H1 – 720,000 sqft, H2 – 932,000 sqft) together with continued restriction of the development pipeline. By comparison, the vacancy rate in The City of London now stands at 8.4%. These figures therefore demonstrate the very tight supply of good quality office space for Midtown occupiers and the need for more schemes to be delivered.

Take up and demand continues to be dominated by the TMT (Technology, Media and Telecommunications) sector, although with the likes of Stewarts Law, WH Smith, Grey Communications and Blick Rothenburg all agreeing transactions of over 10,000 sq ft during the second half of the year the corporate occupiers are underpinning the market. We saw very little new space transacted throughout the year, partly due to lack of supply, but also due to pricing. The market is currently demanding good quality, reasonably priced and well refurbished or second-hand Grade A space; this will position Fox Court very well. Whilst the floors will be significantly extended, the space will still fall into the refurbished category and should be appropriately priced to generate strong interest.

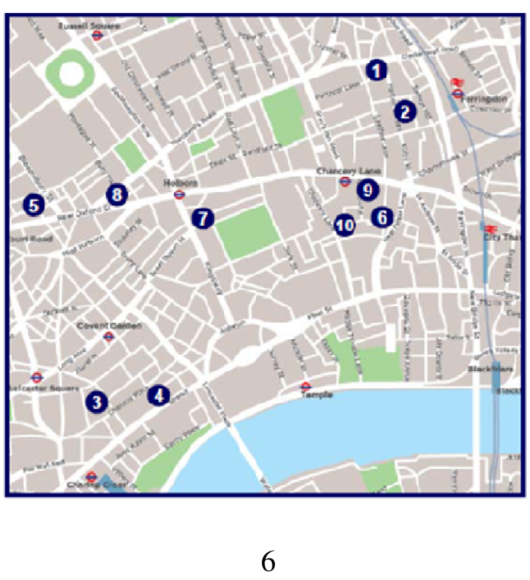
As mentioned above, availability fell consistently across 2012 and should continue to do so throughout 2013. Whilst take up and demand are at relatively modest levels, the continued lack of new space coming onto the market is resulting in a continued downward trend in availability. At 4.7% the availability rate is the lowest since late 2007. With second-hand take up dominating the numbers it was no surprise to see the availability of the second-hand space finish the year nearly 20% down from where it started the year. The levels of new and refurbished space finished the year broadly at the same level, with just a 3% reduction from the start of the year, highlighting again, where the market is.

The development pipeline remains constrained. 143,000 sqft was delivered to the market in the final quarter of 2012 at 280 High Holborn, WC1, 6 Agar Street, WC2 and 51-55 Strand, WC2. There is a further 530,000 sqft due to complete in Q1 and Q2 2013, but there are then no completions due beyond the 2nd quarter 2013 until Derwent London's 40 Chancery Lane, WC2, which will deliver 100,000 sqft in the 4th Quarter 2014. The delivery of good quality refurbished space at Fox Court in mid 2014 will be much needed, to a market then starved of any significant space.

We anticipate that the completions in Q1 and Q2 2013 will see the availability rate rise temporarily before continued take up and no new deliveries see the rate drop to around 4.5% by the end of 2013.

The list and map below show the schemes that are due to be delivered over the next two years in the Midtown market; with the bulk of the space being delivered in WC1 and WC2. There is little or no supply currently programmed for completion, between the summer 2013 and the end of next year. Midtown requires high quality supply, to maintain the expanding, diversified tenant base.

1. The Lever Building, 85 Clerkenwell Road, EC1 – 30,000 sq ft – Q1 2013
2. 28 Kirby Street, EC1 – 24,000 sq ft – Q1 2013
3. 10-14 Bedford Street, WC2 – 27,000 sq ft – Q2 2013
4. Manfield House, 1 Southampton Street, WC2 – 30,000 sq ft – Q2 2013
5. 100 New Oxford Street, WC1 – 55,000 sq ft – Q2 2013
6. New Fetter Place, EC4 – 92,500 sq ft – Q2 2013
7. Africa House, 64-78 Kingsway WC2 – 117,000 sq ft – Q2 2013
8. 10 Bloomsbury Way, WC1 – 155,000 sq ft – Q2 2013
9. Marlborough Court, 14-18 Holborn EC1 – 18,000 sq ft – Q3 2013
10. 40 Chancery Lane, WC2 – 99,000 sq ft – Q4 2014



Looking beyond the immediate Midtown / WC postcode area, we have also identified (detailed in Appendix A), additional pipeline buildings. The overriding themes of this potential supply are:

- It completes well before the anticipated Fox Court refurbishment project;
- Or has no definitive start date;
- Would not be considered as direct competition.

As mentioned above, 2012 saw 22 transactions of over 10,000 sqft, with the number increasing quarter on quarter throughout the year, thus demonstrating the demand for large floor plates in a market where historically these have been few and far between. 8 of the 22 transactions were for units in excess of 20,000 sqft. Listed below are the top ten deals of 2012, all but 3 of which were for more than 20,000sqft.

- Q4 – Stewarts Law – 5 New Street Square – 23,191 sq ft – S/H Grade A - £57.50 psf
- Q4 – CRU International – Chancery House – 17,342 sq ft – S/H Grade B - £30.00 psf
- Q4 – WH Smiths – Victoria House – 13,487 sq ft – S/H Grade A - £35.00 psf
- Q3 – Skype – 2 Waterhouse Square – 88,800 sq ft – Refurbished - £43.50 psf
- Q3 – Blick Rothenburg – New Brook Buildings – 25,000 sq ft – Refurbished - £45.00 psf
- Q3 – Kings College London – 22 Kingsway – 91,000 sq ft – S/H Grade B - £33.00 psf
- Q2 – Webber Shandwick – 2 Waterhouse Square – 65,600 sq ft – Refurbished - £47.50 psf
- Q2 – Burges Salmon – 6 New Street Square – 11,600 sq ft – S/H Grade A - £43.40 psf
- Q1 – Bindmans – 222 Grays Inn Road – 21,600 sq ft – S/H Grade A - £31.00 psf
- Q1 – Telefonica – Shropshire House – 20,795 sq ft – S/H Grade A - £42.00 psf

In terms of tenants' specific requirements, the fundamentals (generally Grade A specification) remain the same, albeit with emphasis on some additional key factors. Occupiers will require secure bike storage and plenty of good quality shower facilities as more and more people cycle into work. This is becoming a critical requirement for most occupiers and will be addressed as part of the scheme.

3. COMMENTARY ON PROPOSED SCHEME

Having understood the weaknesses and deficiencies of the existing building, we set out below our commentary on the proposed scheme and how it addresses section 1.1.

In general terms, the works outlined below encapsulate a significant improvement in the quality of the existing building, from what might be considered by tenants to be second hand/Grade 'B', to an enhanced Grade 'A-' standard. The only differentiating factor between the finished building and what the market would consider to be a prime Grade 'A' building is that it is a redevelopment of an existing structure, rather than a brand new development.

3.1 Reception Area

- The façade is to be extended in line with the existing building line creating a better approach to the property and an improved street presence on Gray's Inn Road.

- Visitors will enter the property at pavement level, prior to stepping up to the reception, with a disabled lift to the right of the steps. This will allow all visitors to have the same arrival experience as they enter the space, which is a significant improvement from the current DDA access provision which is via a long ramp.

- The proposed layout of the reception allows for a more natural flow through the space towards the reception desk and then onto the lifts. The reception area will also be of a substantially higher quality than the existing entrance, including new doors, floor & wall finishes and a new reception desk. This will improve the overall arrival experience and will increase the appeal to prospective occupiers.

- The reception will be fully refurbished and extended to facilitate the increased numbers of staff that the building will accommodate after the proposed works. It will become a space that is appropriate for both the quality and size of building. The total reception (including the Brooke Street entrance) size will be an estimated 2,077 sqft which is anticipated to be 2.1% of the total net internal area. In the absence of Interpublic, Trillium is now the majority occupier in the building. It is proposed that they will create and utilise a dedicated reception at the rear of the property on Brooke Street, which provides a neater solution for them as a tenant with their own entrance more appropriate for their needs. This will to the similar high quality to the main Gray's Inn Road reception and will be a significant improvement to the access arrangements that are currently in position, which is very much a secondary point of access as opposed to another main reception. This core will additionally benefit from a new firefighting lift and the lifts in situ will be overhauled as part of the ongoing maintenance.

- The capacity of the lifts (in the Gray's Inn Road reception) will also be improved by replacing the 3 existing lifts with 4 brand new lifts. These will carry a greater number of passengers at a higher speed.

3.2 Office Floors

- The configuration and increased size of the office accommodation on the lower floor plates will allow for greater occupier flexibility and as a result will increase the appeal of the floors. Traditionally this part of Central London has appealed to corporate occupiers, however we have seen recently (particularly during 2011/12) an increased diversity of tenants. Of particular note being increased activity from the TMT / creative sector, as evidenced by recent activity from Skype, Karmarma and Austin Reed. As a result the property needs to be flexible to appeal to a broader occupier base. The existing building would be considered as a 'B-' grade building but the new proposed scheme will provide new grade 'A-' office space throughout which will be more marketable and appealing to the likely tenant mix.

- Given the current strength of the TMT sector and the projected recovery of the corporate and financial sectors by 2016, the base-build specification for the building will need to accommodate a broad range of occupiers. As mentioned above, we believe that the requirements of all sectors are now largely driven by the ability to fit more employees in to less space and the building has been designed to meet these requirements.

- The availability of large floor plates in this area in Central London is very limited and therefore buildings such as 2 Waterhouse Square, where floors plates are c.30,000 sqft, have let well which is partly down to a lack of choice in this demanding market. Other properties of note in the near vicinity which can also provide a large floor plate are The Johnson Building, Mid City Place and 5 New Street Square. All these buildings had relatively quick leasing success indicating that there is a good market for tenants wanting to accommodate a large number of employees on a single floor. As already mentioned in section 2, this has been an ever increasing trend in the London Midtown office market.

- The introduction of an atrium to the floors will enhance natural light to the centre of the building and may also allow a future tenant taking more than one floor to introduce a feature staircase, creating greater inter-connectivity between floors for multi floor occupiers.

- The connectivity between the main part of the office floor and what has previously been called 'the annex' is also significantly improved, with this area now becoming part of one large floor plate instead of being a separate space accessed only by passing through the Brooke Street core. The improved connectivity will also prevent the annex space from trading at a discounted rent. Additionally it will allow occupiers great flexibility to sublet the space without a large loss in net internal area.

- Increasing the net internal area by expanding across the courtyard area to the rear of the property will utilise this space more efficiently. This space is unused, whereas the proposed development will create greater amenity for some tenants by way of balconies on the third floor. This will add to the appeal of the property and change the profile of rent. It is worth noting that very few properties in the vicinity offer outside space by way of a balcony, which will set the building apart from its competition.

- The services that are provided on the floor are to be increased and improved to accommodate the greater numbers of personnel anticipated. The service provision on the existing floor plate is already restricted and would have needed to be increased regardless of the development work for a new tenant to occupy the existing floor plate.

- The common parts will be refurbished as part of the works. The fact that these were dated and not fit for purpose was one of the reasons that Interpublic decided to move as it was felt that the working environment did not satisfy them. The refurbishment proposals include bicycle storage, showers, changing areas and lockers for use by all occupiers, which is a growing requirement for tenants. These will not only provide better tenant amenity but also improve the green credentials of the development and encourage tenants to commute in a more 'green efficient' way.

3.3 Retail Space

The introduction of a retail use into the ground floor of the building will serve two main purposes:

a) It will meet the needs of local shoppers, for whom there is no convenience store of a decent size within a 5 minute walk; and

b) It will remove the letting risk for the most difficult floor to let in the building if it were to remain in office use.

Typically, ground floor units will trade at a discount if let as office space, as tenants do not want to be overlooked and dislike the 'goldfish' bowl effect. Due to these concerns, this space is often the last to let and therefore will have the greatest letting risk. The retail unit will not only remove this extended void period but create a fantastic tenant amenity for the building and add to its appeal when occupiers are looking at the space. The unit will be very separate from the office entrance and not affect the office occupier's enjoyment of the space.

4.0 CONCLUSION

In conclusion, we believe that the existing building – in its current condition, or simply refurbished - is not fit for purpose to respond to the demands from tenants who are active in today's market. The building is not to a standard that persuaded Interpublic to remain in occupation, as they sought to upgrade their working environment and address the weaknesses that had been identified. As a result the letting void would be significantly increased if the space was to be let as is and the rent achievable would be restricted.

The proposed scheme addresses the weaknesses and deficiencies at the property and will reposition the asset to be a high quality refurbishment which will be able to compete in the current market. The market conditions support the development of larger floor plates and we believe that there is, and will be, a continued demand from tenants to accommodate their employees on as few floors as possible. The development pipeline is restricted in Midtown with a noticeable lack of good quality, larger floor plates coming on stream. Coupled with this, availability has been falling; therefore Fox Court will be well placed to capitalize on the inevitable short supply.

Report jointly prepared by Knight Frank LLP and Farebrother

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