

Canary Wharf Estate– Assets and liabilities

Morgan Stanley's Songbird consortium has emerged victorious in the year-long battle to take over Canary Wharf Group. The consortium, which offered 295p in cash per share, will inherit an improving estate, but one that still has significant liabilities. EGi's London Office Database, part of Estates Gazette Group, takes an independent, building-by building look at Canary Wharf's office assets – and its liabilities.

Introduction

It is just over ten years since Olympia and York, the then owners of the estate, went into administration and emerged as Canary Wharf Group. In that time, the working population has risen from 7,000 to almost 70,000 and the estate has attracted key office occupiers away from the City Core.

The estate, however, cannot be regarded as a success story – the inducements needed to attract tenants have been expensive and significant liabilities remain.

Below is a guide to the main buildings on the estate, outlining the key assets and liabilities for each. 5 & 25 Canada Square, which were sold in early 2004 to the Royal Bank of Scotland, are not included.

Key Buildings containing liabilities

Building	Size (sq ft)	Liabilities
One Canada Square	1.2 million	Around 62,000 sq ft on the market (not all from Canary Wharf Group)
25 Bank Street	1.05 million	200,500 sq ft on the market
BP1, 1 Churchill Place	1 million	327,500 sq ft on the market
10 Upper Bank Street	1 million	105,000 sq ft on the market; leasehold liabilities taken elsewhere
40 Bank Street	600,000	358,000 sq ft on the market with potential for more
20 Canada Square	554,000	87,900 sq ft on the market (subject to options) with additional leased space not occupied
30 South Colonnade	283,000	Let to Reuters but leasehold liabilities elsewhere; £3m refurbishment cost
50 Bank street	223,500	54,000 sq ft on the market
1 Westferry Circus	217,000	73,300 sq ft on the market

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One Canada Square
Office accommodation: 1.2 million sq ft
Age: 1991
Architect: Cesar Pelli & Associates
Assets: Multi-let. Largest tenants include Telegraph Group; Bank of New York and KPMG. No leases expire before 2010.
Liabilities: Around 42,500 sq ft on the market - although much of that is on subleases. KPMG, who occupies around 137,000 sq ft, has a break option in 2008.

This world landmark has few major liabilities, but as the centrepiece of the estate, it deserves attention. The 62,000 sq ft on the market is proving hard to let – the 19th floor, for instance, has been available since 2001 – but the building is always likely to have a high turnover of tenants. The most recent deals in the building came in the last quarter of 2003. Kilpatrick Stockton took 28,000 sq ft on the 39th floor and the 2012 Olympic Bid Committee took 14,000 sq ft on the 50th floor – the highest office space in Britain – but, of course, that tenancy is in the hands of the Olympic bid judges.



25 Bank Street
Office accommodation: 1.05 million sq ft
Age: 2003
Architect: Cesar Pelli & Associates
Assets: 847,100 sq ft let to Lehman Brothers.
Liabilities: 200,500 sq ft available through CB Richard Ellis and Knight Frank following Lehman Brothers exercising its put option.

Lehman agreed to prelet this building back in 2001 on a 30-year lease at around £41 psf. Construction completed in August 2003 and Lehman Brothers began taking occupation soon after. However, it soon emerged that it had surplus space and its put option on 203,000 sq ft became available in early 2004. All of this space, over the 14th to 21st floors, is still available at £42 psf.



BP1, 1 Churchill Place
Office accommodation: 1 million sq ft
Age: 2004
Architect: HOK International
Assets: 672,500 sq ft let to Barclays for 30 years
Liabilities: 327,500 sq ft available through CB Richard Ellis and Knight Frank

This is the only office scheme under construction in Docklands at the moment and it is due to finish in July 2004. Barclays will take occupation in 2005. The building is notable as it was designed after the 2001 World Trade Centre attacks in New York and incorporates panic rooms and more escape staircases than normal.
Barclays took a prelet on the entire building in September 2001 but it was evident from the outset that it had no plans to occupy all of the space. It originally planned to occupy 650,000 sq ft - but took an option on a further 22,500 sq ft earlier this year, reducing the amount on the market. Barclays is also said to have "call option" on BP2 (yet to commence construction) – an option to acquire either at a given price or a given time.

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10 Upper Bank Street
Office accommodation: 1 million sq ft
Age: 2003
Architect: Kohn Pederson Fox
Assets: 895,000 let to Clifford Chance
Liabilities: 105,000 sq ft available through CB Richard Ellis and Knight Frank after Clifford Chance exercised put option. Canary Wharf also took over a key Clifford Chance leasehold to get the law firm to E14.

This building shouldn't have contained liabilities for Canary Wharf, but Clifford Chance's decision to utilise its put option led to 105,000 sq ft being handed back. There have been no deals as yet. Canary Wharf also took on the 437,000 sq ft 200 Aldersgate Street, EC1 which is currently available through CB Richard Ellis at £35 psf. That building will also be refurbished at an undisclosed cost.



40 Bank Street
Office accommodation: 600,000 sq ft
Age: 2003
Architect: Cesar Pelli & Associates
Assets: Leases to Allen & Overy and Skadden Arps Slate Meagher & Flom on around 209,000 sq ft
Liabilities: 358,000 sq ft available through CB Richard Ellis and Knight Frank and up to 67,000 sq ft of surplus space from Skadden Arps with potential to come to the market

Allen & Overy agreed to take space here back in September 2001 and Skadden Arps Slate Meagher & Flom signed a month later. Construction completed in March 2003 with 357,000 sq ft available speculatively. When Skadden Arps started to move in, however, it became evident that it was not occupying all the space it signed for – it was only occupying 73,000 sq ft across the 20th to 23rd having originally signed for almost 140,000 sq ft. This surplus space is yet to emerge to the market, but Skadden was reported to have a put option on 58,000 sq ft.



20 Canada Square
Office accommodation: 554,000 sq ft
Age: 2003
Architect: Skidmore Owings & Merrill
Assets: Leases to McGraw Hill & BP
Liabilities: 87,900 sq ft on the 5th and 6th floors still available through CB Richard Ellis and Knight Frank (subject to options to BP). The 9th floor, comprising around 43,800 sq ft, is held on a lease by McGraw Hill but is not occupied – could be released in the future.

McGraw Hill and subsidiary companies Platts and Standard & Poor's occupy the majority of this building, after taking a 310,000 sq ft prelet in October 2000. Construction began soon after, but McGraw Hill's tenancy was immediately subject to speculation after it appointed consultants to determine how much it should occupy and whether it should exercise its options on remaining available space. It eventually chose to exercise a put option on the 6th floor, comprising 47,000 sq ft, handing it back to Canary Wharf Group. Construction completed in June 2003 with around 248,000 sq ft of vacant, speculative space.
In September 2003, it was announced that oil giant BP was taking 128,000 sq ft – 101,000 sq ft at first, with options on more space. The announcement caused problems with McGraw Hill subsidiary Platts – renowned oil journalists – and staff in BP's trading division itself. The conflict of interest was such that some sources thought the deal could be under threat, but BP eventually signed in February 2004. In May 2004, BP took its option on the 30,800 sq ft 4th floor meaning it had an option on the 5th exercisable until September 2004. Should it take this, it will have an option on the 6th until November 2004.

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30 South Colonnade
Office accommodation: 283,000 sq ft
Age: 1991
Architect: Kohn Pederson Fox
Assets: Entire building let to Reuters until 2019
Liabilities: Canary Wharf had to offer significant inducements to secure Reuters deal; lease break on part after 5 years.

Although a 15-year lease on a 283,000 sq ft building at £35 psf should be considered an asset, the costs Canary Wharf incurred in getting Reuters to sign were considerable. Canary Wharf has just commenced a £3 million refurbishment programme – paid for itself – agreed in the deal. On top of that, Canary Wharf took on a number of Reuters leasehold and freehold interests in London to tempt it to Docklands:

- It purchased Reuters' freehold interests at 85 Fleet Street and St Bride's House, EC4 for £32.3 million; agreeing a lease back to Reuters at its Fleet Street building until 2005 at £1.6 million p.a.
  Canary Wharf has since disposed of the freeholds to UBS Global Asset Management on behalf of Triton for £30 million – a £2.3 million loss. A profit sharing agreement had originally been agreed with Reuters.
- Canary Wharf also took on Reuters' leasehold interests at 200 Gray's Inn Road, WC1 (48,000 sq ft) expiring in 2008; Meridian House, Farringdon Street, EC4 (42,000 sq ft) with a break option in 2009 and at Apollo and Gemini Court, Thomas More Square, E1 (108,400 sq ft) with a lease break in 2008.

After incurring all the above costs, Reuters still has the option to break its lease on part at 30 South Colonnade after only 5 years and its fixed rental uplift in years 5 to 10 is only to £41 psf.



50 Bank Street
Office accommodation: 223,500 sq ft
Age: 2002
Architect: Cesar Pelli & Associates
Assets: Leases on 169,500 sq ft to Northern Trust and Goldenberg Hehmeyer & Co
Liabilities: 54,000 sq ft still available through CB Richard Ellis and Knight Frank

The Northern Trust took a prelet on 135,000 sq ft in September 2000 when works had just started. It took a further 18,000 sq ft in April 2002. Construction completed in July 2002 leaving around 54,000 sq ft available speculatively. This space has proved hard to let with the only deal coming from Goldenberg Hehmeyer & Co in December 2003 on a single 18,000 sq ft floor. The remaining space, on the 1st, 2nd and 4th floors, remains available.



1 Westferry Circus
Office accommodation: 217,000 sq ft
Age: 1992
Architect: Skidmore Owings & Merrill
Assets: Around 144,000 let to Chevron Texaco
Liabilities: 73,250 sq ft available through CB Richard Ellis and Knight Frank

Chevron Texaco used to hold the freehold of this building, but sold it back to Canary Wharf for £82.5 million in 1999 in a sale and leaseback deal. Credit Suisse First Boston then took 73,300 sq ft on the lower three floors but vacated for existing space in 2003. This space is now on the market through CB Richard Ellis and Knight Frank.

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Key Development Opportunities



Canary Riverside Phases 2 & 3 & North Quay (Shed 35)

Canary Riverside 2 & 3 is a 1.8 million sq ft Richard Rogers-designed office scheme.

North Quay, formerly known as Shed 35, is adjacent to the Riverside site and will comprising 1.9 million sq ft of office space, designed by Cesar Pelli & Associates. Both elements are still at application and CB Richard Ellis and Knight Frank are pre-marketing. The buildings, which will comprise two towers of 43 and 37 storeys, will have a lower link building comprising retail space and a public realm area in between.

The sites, however, fall outside of the Canary Wharf Enterprise Zone so permission could be more difficult to attain. Although the plans have been praised for exceptional architecture, construction is highly unlikely to commence in the near term.



Canary Wharf DS3, 15 Canada Square

The scheme is designed by Skidmore Owings & Merrill and is still at permission. It will comprise 600,000 sq ft and is being premarketed by CB Richard Ellis and Knight Frank.

Enron agreed terms to take a prelet here back in September 2000, but a disagreement with Canary Wharf over subletting terms on surplus space forced negotiations to end – before Enron's bankruptcy would have ended talks anyway. Groundworks have completed, but Canary Wharf's freeze on speculative space has meant there has been no progress for three years. Construction is unlikely to start without a prelet.



BP 2-4, 10-20 Churchill Place

These three buildings will total 730,000 sq ft and are being premarketed by CB Richard Ellis and Knight Frank. Full construction is a long way off, although groundworks could start on BP4 (10 Churchill Place) soon. Barclays is said to have a "call option" on BP2 (see above).



Wood Wharf, Preston's Road, E14

Canary Wharf did not own this 20-acre site before the Songbird takeover, but it represents a key opportunity for the new group. As the picture shows, the site is situated next to the Canary Wharf Estate and should a rival developer win a bid to become a joint venture partner with current owner British Waterways, competition with the Canary Wharf Estate will be fierce.

Outline plans for the site involve 4.95 million sq ft of commercial and residential space with an end value of £2 billion. Interested bidders include British Land; Hammerson; Grosvenor; Development Securities; Stanhope (with its affordable housing arm First Base); AMEC with Morley; Argent and Miller. Canary Wharf submitted a bid with Manhattan Loft as a jv partner. Canary Wharf's own Paul Reichman had submitted a bid himself through his IPC Advisors vehicle, but the Canary Wharf board threatened legal action over the conflict of interest and he has since pulled out.

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Other Stock



8-16 Canada Square
Office accommodation: 1.1 million sq ft
Age: 2002
Architect: Foster & Partners
Assets: Held by HSBC on virtual freehold
Liabilities: None



10 Cabot Square, 5 North Colonnade
Office accommodation: 636,000 sq ft
Age: 1992
Architect: Skidmore Owings & Merrill
Assets: Let to Barclays Bank and Ogilvy & Mather
Liabilities: None



33 Canada Square
Office accommodation: 562,685 sq ft
Age: 1999
Architect: Foster & partners
Assets: Held by Citigroup on a lease until 2027. Citigroup did have a virtual freehold, but sold it back to Canary Wharf in December 1999.
Liabilities: None



10 South Colonnade, 18-20 Cabot Square
Office accommodation: 559,000 sq ft
Age: 1991
Architect: Kohn Pederson Fox
Assets: Let to Barclays Capital and Morgan Stanley
Liabilities: No current liabilities, but this building is of note following the deal to Barclays Capital in March 2004. The bank took a sublease from Credit Suisse First Boston on 70,000 sq ft after CSFB had chosen to occupy space it was disposing of at 5 Canada Square (now owned by RBS).

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1-5 Cabot Square

Office accommodation: 547,000 sq ft
Age: 1999
Architect: Pei Cobb Freed & Partners
Assets: Held by Credit Suisse First Boston on virtual freehold
Liabilities: None



20 Bank Street

Office accommodation: 512,000 sq ft
Age: 2003
Architect: Skidmore Owings & Merrill
Assets: Let to Morgan Stanley until 2038
Liabilities: None



25 Cabot Square

Office accommodation: 449,000 sq ft
Age: 1991
Architect: Skidmore Owings & Merrill
Assets: Long leasehold held by Morgan Stanley
Liabilities: None



25 North Colonnade

Office accommodation: 363,000 sq ft
Age: 1991
Architect: Troughton McAslan / Adamson Associates
Assets: Let to Financial Services Authority
Liabilities: None



17 Columbus Courtyard

Office accommodation: 199,500 sq ft
Age: 1999
Architect: Gensler
Assets: Let to Credit Suisse First Boston until 2024 with 5 yearly rent reviews.
Liabilities: None

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7 Westferry Circus
Office accommodation: 187,000 sq ft
Age: 1992
Architect: Skidmore Owings & Merrill
Assets: Let to European Medicines Evaluation Agency, EDS Eurostand and Edward Jones Limited
Liabilities: All leases expire by 2009. EMEA has break option on majority of building later in 2004.



15 Westferry Circus
Office accommodation: 174,000 sq ft
Age: 2001
Architect: Skidmore Owings & Merrill
Assets: Let to Tubelines on sublease from Morgan Stanley
Liabilities: None

Conclusion

The Canary Wharf Estate has come along way since the Isle of Dogs first became an enterprise zone in April 1982. It has, perhaps, come slightly too far. London Office Database figures show a total of 1.3 million sq ft of new stock on the market in E14 and the vast majority of that is on the Canary Wharf Estate. Canary Wharf arguably developed one building too many and it has had to make hugely generous offers to soak up space.

When the put options contained in many leases were announced to the market in March 2003, Canary Wharf Group's share price dropped by 1/5th to 180p. The shares currently trade at around 290p and prospects are looking good. Canary Wharf sensibly reduced its exposure with the £1billion sale of 5 and 25 Canada Square - 25 has 495,220 sq ft available – albeit on a sublease – and there is surplus space in number 5.

The financial sector – the key occupier on the estate – is employing again and space is coming off the market. Speculative construction is highly unlikely and the estate has plenty of time to consolidate.

Nevertheless, the recent history of undisclosed lease liabilities and the amount of speculative space yet to be absorbed is sobering. Songbird inherit an improving estate, but there is a long way to go before it is a secure one.

Further Information

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