HWBC

DUBLIN OFFICE REVIEW

H1 2020

OFFICE STATISTICS H1 2020

Take Up	1.10m sq ft	**Under Construction**	CBD: 5.45m sq ft Suburbs: 750,000 sq ft
Vacancy Rate	Entire Market: 8.0%	**New Completions 2020** **% Pre-committed on PC**	600,000 sq ft 68.0%

Difficult Q2 as Covid-19 impacts the market

'May you live in interesting times'… never has an old proverb seemed so apt for the last few months in terms of economic and social upheaval to working and personal lives. While there was some talk of a dangerous virus in Q1 the impact did not fully hit until March when business and social life fell off a cliff. The effect on the Dublin office market was immediate and market activity stalled in Q2 with take up less than 100,000 sq ft. This was not entirely unexpected as most corporate occupiers put requirements on hold to assess the impact on their staff and business. Up to then the fundamentals of the market had been performing well with record activity in Q1 and predictions of another strong year ahead. Rents had been recovering since 2015 back to pre-crash levels with strong levels of occupier demand, however we were in the late phase of this cycle with rents plateauing for the last 18 months. Most astute market observers would have been predicting a return to more normalised levels of tenant demand, and an increasingly cautious approach from developers to supply of new space.

This is the second major setback for the office market in 10 years, with some querying if the same drastic correction will occur in terms of rental levels and vacancy rates. In our view the conditions of this 'black swan' event are structurally different from the previous crash, and the market is in much better shape heading into this crisis. There are a number of principal differences to consider.

- *The supply of new space has been controlled in this cycle and we are not in a position of over-supply, which was not the case in 2009. For the most part the development market has been spot on in terms of what, where and when to build offices to ensure that new space has been delivered to match tenant requirements in terms of specification, size, location and timing. Of the 5.5m sq ft under construction in the CBD for delivery over the next 3 years, over 50% is already reserved with the estimated annual supply over the next 3 years set out below;*

CBD Pipeline	Est. FY Completions (sq ft)	Pre-let/ Reserved (sq ft)	Available Supply (sq ft)
2020	1.45m	765,000 / 53%	685,000
2021	2.61m	1.4m / 54%	1.21m
2022	2.0m	1.18m / 59%	820,000

The HIVE Sandyford, Carmanhall Road, Sandyford, D18
New Grade A Offices 73,000 sq ft

- *There are strong levels of pre-commitments to pipeline supply and we expect this to tighten as more space is reserved in addition to a slowdown in new starts. This should help prevent a situation of market over supply and provide support to current rental levels.*

- *The funding and ownership structure of this market is made up principally of professional, institutional and fund landlords which was not the case previously, where the market had a more disparate ownership structure including domestic builders and private sector syndicates put together by banks and accountants. As a result we are less likely to see dramatic rent reductions in any market downturn and most institutional landlords will have a preference to agree more flexible lease terms and tenant incentives to reflect market conditions. In addition landlords in this cycle are well capitalised with near fully let portfolios so not under pressure to cut rents.*

- *Market funding has been principally from overseas investors and pension funds with little involvement of the domestic banking sector. This is in direct contrast to 2009 where massive over lending to domestic developers and speculators with minimal corporate governance and oversight from the Central Bank, eventually led to a banking crash and State bailout from the IMF.*

After record levels of market activity in Q1 with take up of 993,000 sq ft, the potential impact of Covid-19 is still to emerge in terms of FY take up and pressure on rental levels. Take up for H1 at 1.1m sq ft is below average and is likely to see the total for this year fall below 2m sq ft for the first time since 2012. Pre-Covid there were strong levels of tenant demand and there is currently over 500,000 sq ft of deals in advanced negotiation with large tech requirements due to complete by year end. Not surprisingly the tech sector dominated market transactions with the top 5 all completed in Q1.

Top 5 Office Deals 2020	Size (sq ft)	Tenant
1. One & Two South County, Leopardstown D18	245,500	Mastercard
2. Fitzwilliam 28, Fitzwilliam Street D2	135,000	Slack
3. One Park Place, Upper Hatch Street D2	103,000	Dropbox
4. Stemple Exchange, Blanchardstown D15	85,000	Guidewire
5. Block 1 Central Park, Leopardstown D18	72,000	Google

Office users both large and small are reviewing their occupational requirements and the future use of office space to re-think what changes will be required going forward. Large corporate occupiers are only beginning to get staff back to the office, and this process is likely to run to at least year end before any real clarity emerges. New Working from Home (WFH) measures have worked well for most companies and no doubt will be a feature of the future work life balance.

The increase in WFH policies is not new for a number of sectors and may not have the dramatic effect on office use and demand for space as some commentators have predicted. The technology sector has been leading this change to work practices for a number of years, and they are by far the largest driver for demand in the Dublin market. Large tech companies have typically operated on an occupancy rate of 50/70% so WFH is not new to that sector and will impact their business model least. This is already evident in the US with companies such as Amazon and Facebook proceeding with plans for large acquisitions of additional office space for continued expansion, showing further commitment to physical space.

Where the new WFH practices will impact most is the professional and financial sectors such as banks, solicitors and accountants who would normally operate on a near 100% occupancy model, with all staff typically having their own desk space. This is going to change going forward and will impact demand for space from these sectors, with many companies looking at ways to reduce physical footprints to reflect the new reality. However dramatic cost savings may be difficult to achieve as having fewer staff in the office will be offset somewhat by the requirement to have more space per employee to comply with new health & safety guidelines. The digital transformation to work practices was expected to take around 10 years and this is now being condensed into 12 months, which is a big adjustment for employers to make.

We expect Covid to have an impact on office use in the suburbs as large occupiers consider the benefits of having a suburban base with shorter commute times, as part of the strategy and re-think of staff returning to the office. There are a number of large occupiers looking at the 'hub and spoke' model as opposed to the traditional single HQ, which combines a city hub with a strategic suburban location for a more flexible workspace and working style. The benefits of this strategy include lower costs and the option for staff not to travel to the city for everyday commutes to improve work/life balance.

Headline Office Rents (H1 2020)	
CBD (Grade A)	€60 - €62.00 per sq ft
Suburban (Grade A)	€30 - €32.00 per sq ft
Car spaces; City	€4,000 pa per car space
Car spaces; Suburbs	€1,750 - €2,000 pa per car space

OUTLOOK

There is no doubt the Dublin office market has received a severe shock with the arrival of Covid-19 and it is still too early to gauge the full impact on long term office use. There is no real evidence of headline rents moving lower, however a reduction in net effective rents and increased tenant incentives by year end would be a reasonable assumption.

We would expect a more cautious approach from developers yet to go on-site so the supply of new space should begin to slow. The industry wide shut down will also have a knock-on effect on expected completions for 2020. To off-set this there is likely to be an increase in the amount of 'grey space' offered to the market, as companies look to dispose of surplus offices to implement increased WFH policies. This will be particularly evident within the CBD as the professional and financial sectors adjust to the new reality.

Given the strong run the market has had over the last number of years, a late cycle correction would not have been unexpected but certainly not in the manner of the immediate hit in March which will take some time to fully play out. There is also the small matter of Brexit to be finalised by year end, and the outcome of trade negotiations and final agreements will be closely watched by the office sector.

One Haddington Buildings (42,000 sq ft), D4.
Acquisition / Development / Leasing / Disposal (SPP)

CONTACT OUR OFFICE AND BUSINESS SPACE TEAM

Paul Scannell
Director - Head of Offices

T +353 1 77 50 527
E pscannell@hwbc.ie

Emma Murphy
Divisional Director

T +353 1 77 50 519
E emurphy@hwbc.ie

Conor Kevany
Director

T +353 1 77 50 506
E ckevany@hwbc.ie

HWBC

HWBC
80 Harcourt Street, Dublin 2
D02 F449, Ireland

T 353 1 77 50 500
E info@hwbc.ie
W hwbc.ie

CORFAC International
PSRA Number 002098