Lisney

OFFICE REPORT

Q3 2020

OFFICE SECTOR IN NUMBERS

ACTIVITY

21,150
SQM

SIGNIFICANTLY LARGER THAN Q2 BUT STILL A SMALL QUARTERLY FIGURE BY NORMAL STANDARDS

SUPPLY

380,000
SQM

ONE-THIRD OF NEW SUPPLY IS **GREY SPACE**

RENTS

-4.8%

PRIME HEADLINE RATE FELL IN THE QUARTER

UNDER CONSTRUCTION

414,000
SQM

54% ALREADY LET OR RESERVED

OVERVIEW

The Dublin office market was in somewhat of a hibernation in Q3 with most occupiers adopting a wait-and-see approach. While Q3 take-up was 20,150 sqm, many of the deals were agreed earlier in the year. Supply increased (+17.2% in the three months) as grey space (sub-lets) became a feature of the market once again. Construction activity continued with 44,000 sqm of accommodation finished in Q3 and with 414,000 sqm ongoing at the end of September.

ACTIVITY

Following the weakest quarter since 1989 in Q2, activity levels improved in Q3 with take-up across Dublin reaching 21,150 sqm. While this is a significant increase on the 6,900 sqm completed in Q2, it is still a relatively modest quarterly activity figure. Of note, many of the deals were agreed earlier in the year, prior to the onset of COVID-19 in Ireland. For the nine months to the end of September, take-up reached almost 116,000 sqm.

Given how small take-up was in Q3, analysis of the figures is somewhat meaningless. However, we have provided the details below for reference.

REGION

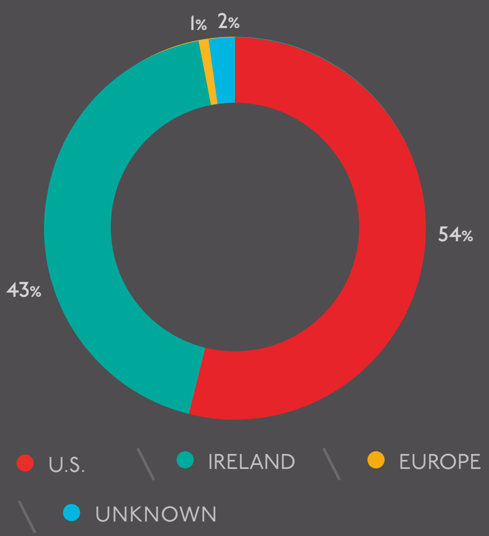
In Q3, 81% of activity was in the city centre with the five largest transactions occurring there. The largest deal comprised Microsoft taking 4,080 sqm at No. 3 Dublin Landings at North Wall Quay followed by the OPW taking 3,900 sqm at IGQ at George's Quay (for its own use and not that of a government agency). Other deals in the city centre included North Dock 2 (Gillead – 2,900 sqm), 78 Sir John Rogerson's Quay (Twilio – 1,900 sqm) and One Warrington Place (Regeneron – 1,270 sqm).

In the suburbs, 12% of activity was in the south with the north and west at 4% and 3% respectively. The largest deal in the suburbs was Beacon Hospital taking 800 sqm in the Concourse Building at Beacon Court.

ORIGIN

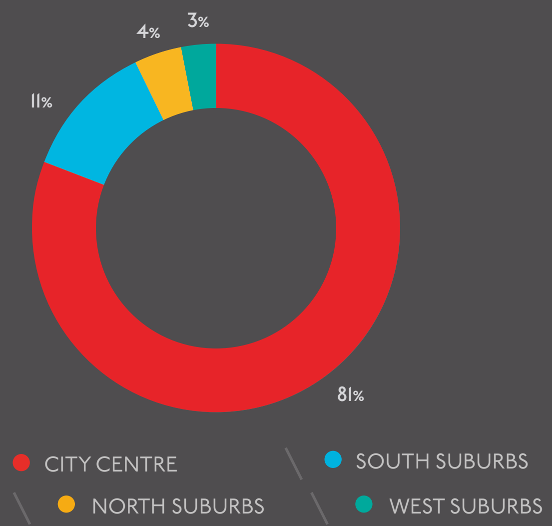
In Q3, 43% of activity related to domestic companies with those from the United States (54%) dominating international activity. However, in real terms the figures are small at 8,700 sqm and 10,750 sqm respectively. Over the nine months to the end of September, international occupiers account for 82% of take-up, driven by some of the large deals in the early months of the year.

TAKE-UP BY OCCUPIER ORIGIN
Q3 2020



Source: Lisney

TAKE-UP BY REGION
Q3 2020



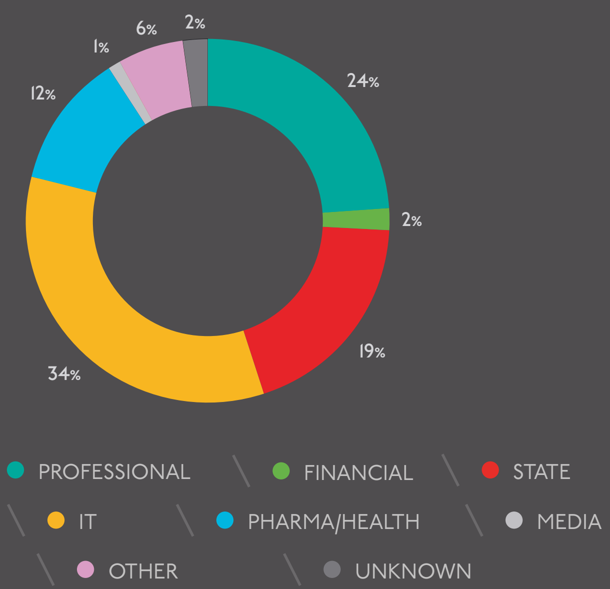
Source: Lisney

SECTOR

The tech sector made up for one-third of all activity in Q3 with two of the top five deals related to this businesses in this sector. This was followed by professional services companies at 24% and the Irish State at 19% (the entirety of which related to the one OPW deal).

As to be expected, for the second quarter in a row there was no activity by serviced office providers with just 1,750 sqm of take-up in this sector since the start of 2020. Also absent from the market in 2020 were companies in the education sector.

TAKE-UP BY SECTOR
Q3 2020



Source: Lisney

DEMAND

While occupier demand is present, the market is in somewhat of a hibernation. Understandably, most businesses are adopting a wait-and-see approach until they have a better understanding of the impact of COVID-19 on their long-term space requirements. It will be difficult for decision makers to opt to proceed with deals in the short-term as any space taken may not be occupied in any meaningful way for nine months to a year. Consequently, for those with leases expiring soon, their default position will be to extend the lease in the short-term, which most landlords will accept. For occupiers that were in expansion mode, decisions about additional space will be on hold for the majority.

In spite of the current situation, demand from international tech companies for Dublin office accommodation will remain. TikTok is reportedly considering Dublin with a requirement of up to 45,000 sqm. In the health and pharma / life sciences / med tech sectors, there are also several occupiers with requirements.

TERMS

The lack of transactional evidence in the last six months means it is difficult to assess the full impact of COVID-19 on rents. This dearth of activity, combined with poorer market sentiment means that headline rates across most regions and quality of stock fell in Q3. This is the first time since mid-2011 that prime office rents in Dublin have fallen. For Dublin overall, Lisney's office rental value index fell by 1.8% in the three months with the prime city centre headline rate falling by 4.8% (i.e. from €678psm / €63psf to €646psm / €60psf).

SUPPLY

At the end of September 2020, there was just over 380,000 sqm of modern office accommodation vacant across Dublin. This means that supply levels are now back to where they stood 12 months ago. In Q3, supply grew by 17.2% with one-third of the increase coming from grey space (sub-lets) being returned to the market. While it is to be expected that occupiers will downsize, the timing of this is very quick.

Also adding to supply was the newly completed The Sorting Office (19,000 sqm) on Cardiff Lane in Dublin 2. Construction finished in Q3 and while the building had been under active negotiation with Google since late 2019, the tech company decided not to proceed with the letting in September. It is now the biggest individual building available in Dublin.

The majority of available property is in the city (57% of the total) with 17% in the west suburbs, 15% in the south suburbs and 12% in the north suburbs. Over half (56%) is previously occupied space with just 18% new buildings, never before occupied. Grey space now accounts for 12% of supply with refurbished buildings also accounting for 12% of supply. While previously at higher levels, sub-standard accommodation is now just 3% of the total of what is available.

The overall Dublin headline vacancy rate was 9.5% at the end of September (8.6% city region and 10.9% in the suburbs). If sub-standard space is removed, the true vacancy rate was 9.2% (8.4% in the city). Notably, the true vacancy rate in Dublin 1, Dublin 2 and Dublin 4 were 9.6%, 7.0% and 9.9% respectively.

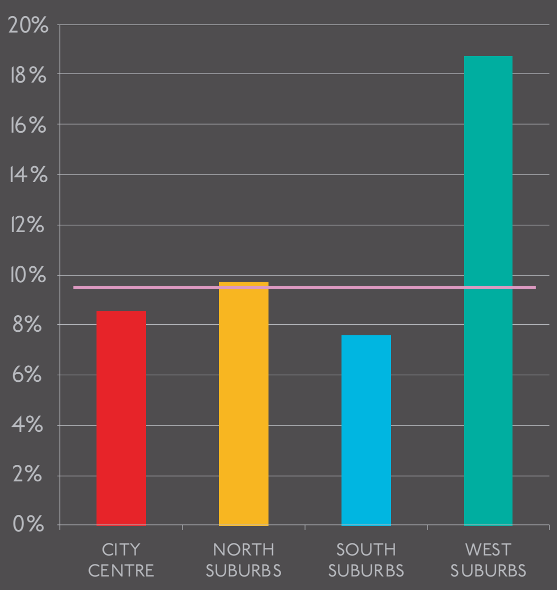
NEW STOCK

44,400 sqm of new office stock was completed in Q3 bringing the total for the nine months to the end of September to 96,400 sqm. There was only one building in the city centre completed in Q3, The Sorting Office on Cardiff Lane (19,000 sqm), which is now available to let. In the north suburbs, Block 3 Dublin Airport Central (8,450 sqm), 1 Semple Exchange in Dublin 15 (7,900 sqm) and Block B Dublin Airport Business Park (930 sqm) were finished while in the south suburbs 8,080 sqm at Enterprise House in Blackrock Shopping Centre completed.

At the end of September, there was almost 414,000 sqm of office space under construction in Dublin. The city centre accounted for 86% of this with the largest scheme under construction in Ballsbridge, the 54,200 sqm Fibonacci Square already taken by Facebook. Another particularly large scheme still under construction heading into Q3 was Salesforce Tower at Spencer Place (43,670 sqm), the company's new European HQ. These schemes, among others, are already committed to by occupiers. In fact, 54% of the space under construction across Dublin is either pre-let or reserved, leaving 46% or 190,000 sqm available.

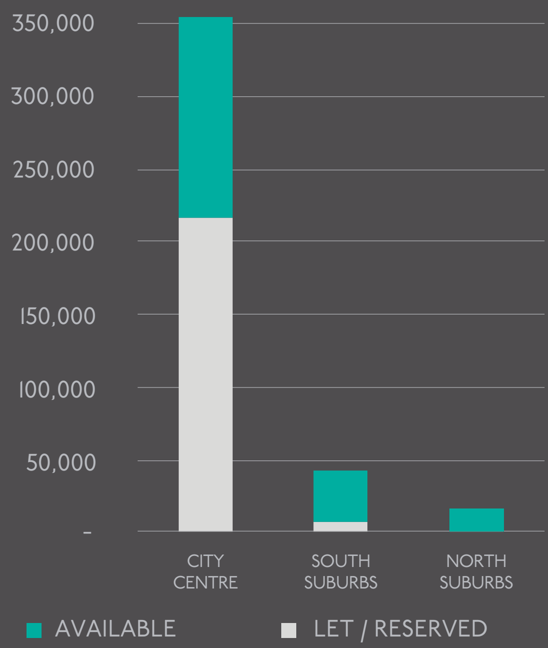
The development pipeline will be affected in the short to medium-term by the lockdown and the closure of sites for seven weeks or more. Given the COVID-19 related health and safety measures, delays in schemes being completed could be up to six months.

HEADLINE VACANCY RATE BY REGION
Q3 2020



Source: Lisney

UNDER CONSTRUCTION BY REGION
Q3 2020



Source: Lisney

IN FOCUS

THE OFFICE

Will COVID-19 have a long-term impact on the future of the office?

Just a few weeks into the pandemic discussions on this question began. With most workers demonstrating an ability to successfully work remotely, self-taught in video conferencing and adopting new work practices, some predicted a shift away from the office.

Six months on, most people continue to work from home and office occupancy by staff is very low with some buildings fully unoccupied or at best with just 10% to 20% of essential staff on-site. This will persist into 2021 with businesses unlikely to ask workers to return in significant numbers prior to a vaccine being widely rolled out.

In the longer-term, the office sector will evolve in different ways as policies put forward by companies vary. As discussed in Lisney's Q2 2020 Office Market Report, some companies will seek to split their office accommodation across both city and suburban locations, thereby offering an easier commute for staff. Some will work remotely indefinitely. Certain large multi-nationals have already announced that particular staff can continue to work from home forever. For most however, a hybrid model will be adopted, offering employees greater flexibility to split time between the office and home once the outbreak abates.

There are lots of surveys showing different findings in terms of what working practices office-based staff want in the future. It is most likely that those in a position to do so will want to split time two / three days at home and the remainder in the office. From a collaboration, work structure and mental health point of view, full-time remote working will not work for everyone. For younger workers it is perhaps more difficult as they will not have that sense of inclusion and social involvement in the company community. Additionally, for employers the lack of an office causes issues in terms of training and getting to know new staff, building relationships, generating ideas, creating and maintaining a company culture and ensuring staff wellbeing. We believe that while many businesses will require less space in the future as workers become more agile, there will still be a need for an office.

OUTLOOK

1. In terms of future activity levels and demand, Q4 2020 and Q1 2021 will be the acid test for the market given the incubation period of office deals before signing is about nine months. For take-up to improve in the first half of 2021, deals need to be under negotiation now. We estimate that the full year 2020 take-up will be 130,000 sqm, the lowest level since 2009 and two-thirds of which was completed in Q1.

2. Further falls in rents are likely and this will vary from region to region but the city centre is likely to fall the furthest.

3. Accommodation available to sub-let has been absent from the market for several years but has returned. This is a trend that will continue in the months ahead and will escalate supply and vacancy levels over the final months of 2020 and into 2021. If supply grows significantly, it will act as a drag on market rents as businesses sub-letting some or all of their accommodation tend to collect what rent they can and view it as a cost recovery mechanism.

4. Finance for speculative office development will be more difficult to secure in the short to medium-term. Funding generally has moved towards the private residential rented sector (PRS) and this might assist in cushioning the blow to office rents as significant quantities of new speculative stock will not be built.

5. While currently on hold, demand from international tech companies for Dublin office accommodation will remain with several requirements in the market.

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