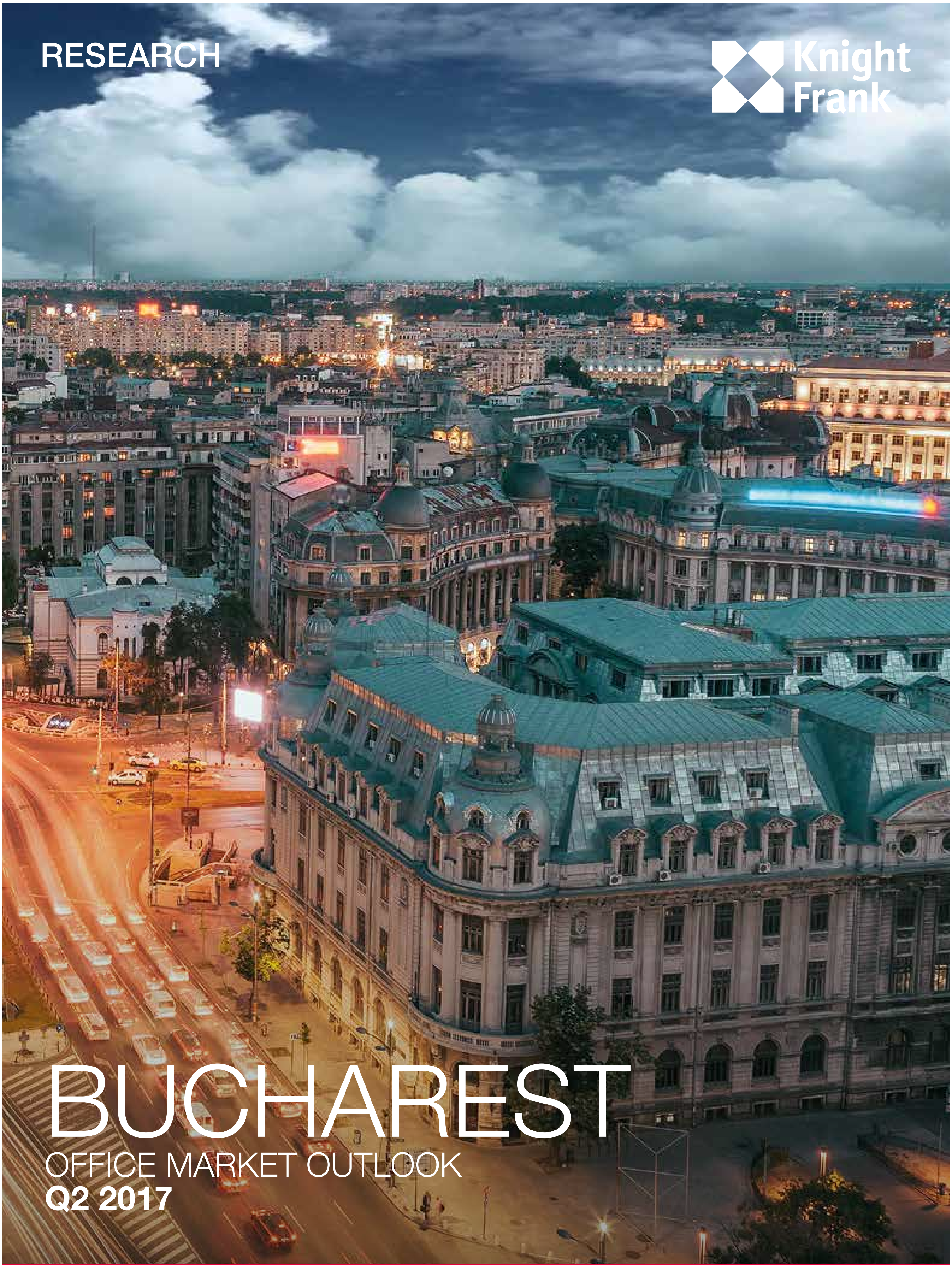
RESEARCH



BUCHAREST

OFFICE MARKET OUTLOOK
Q2 2017

OCCUPIER TRENDS | INVESTMENT TRENDS | MARKET OUTLOOK

KEY FINDINGS

Romania's economy grew by 4.8% in 2016, the fastest rate since 2008.

Bucharest's office market registered one of the strongest years of take-up in 2016 reaching nearly 350,000 sq m.

Leasing activity was led by IT and Communication and Business Process Outsourcing (BPO) companies.

An increase in construction activity has compensated for low office volumes in recent years.

Romania's commercial real estate investment volumes totalled €706 million in 2016, with the retail sector seeing the greatest allocation of capital.

Prime office yields remained stable at 7.5% and only moderate yield compression is anticipated during 2017.

OCCUPIER MARKET

Leasing activity soared in 2016, making Bucharest's take-up highest in over a decade.

An active final quarter led to Bucharest's office take-up reaching nearly 350,000 sq m of Class A and B office space in 2016, surpassing the previous year's high by 41% (Figure 1). The significant boost emanated from pre-leases in the Center-West submarket by Renault (39,000 sq m) and BCR (20,000 sq m). The former represents a record transaction in Bucharest and was the largest deal in the CEE region in 2016.

Bucharest's occupational market has continued to show buoyancy in 2017. Almost 100,000 sq m of office space was leased in the first quarter alone. The IT and Communication and BPO industries have dominated office space demand. These industries have been drawn to the market due to the large pool of talent and quality of recently delivered office schemes. Although Bucharest's Northern-Central region has been the preferred location for headquarters and BPO companies, many companies have been expanding into second-tier cities in Romania.

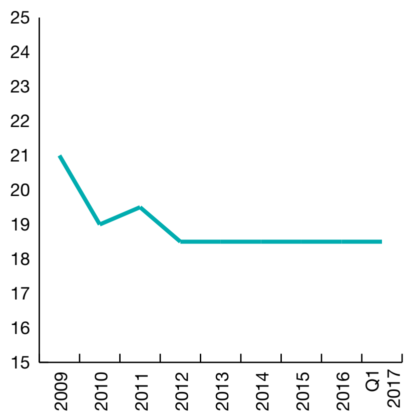
The entrance of multi-national IT&C and BPO companies has led to a change in Bucharest's occupational market dynamics. With the working environment becoming pivotal in employee retention and recruitment, BPO and SSC companies have become more demanding in their space requirements. Accordingly, developers have responded by delivering projects of a higher calibre and incorporating end user facilities, flexible office layouts and collaborative spaces to meet these occupier groups' requirements.

On the back of increased demand in Bucharest's office market, construction activity in 2016 was on an upswing. In 2016, 293,000 sq m of Class A and B office space was delivered across 15 new buildings and 12 projects compensating for historically low delivery volumes. Consequently, the overall vacancy rate increased to 15% at the end of the year. Yet less than one-third of the new space remains vacant. Deliveries in the first quarter of 2017 were low (10,000 sq m), however a further 350,000 sq m is forecast to be delivered throughout 2017 and 2018. Despite significant supply additions, prime headline rents have remained stable at €18-€18.50/sq m/month (Figure 2), with incentives likely to be impacted as landlords compete for occupiers.

FIGURE 2

Prime office rents

€ per sq m per annum

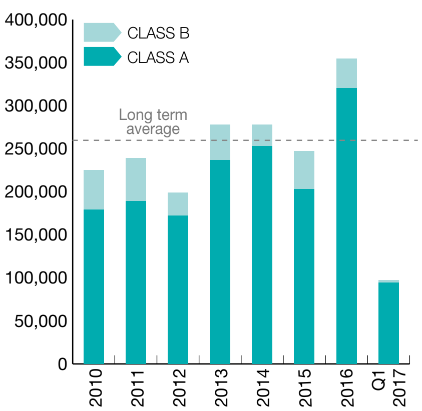


Source: Knight Frank Research

FIGURE 1

Class A and B office take-up

sq m



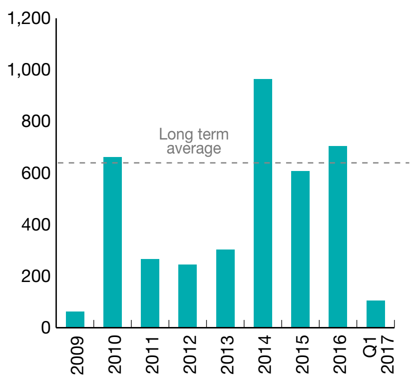
Source: Knight Frank Research

Key recent office leasing transactions

Quarter	Property	Tenant	Sector	Size (sq m)
Q4 2016	Renault Office Building	Renault	Automotive	39,000
Q2 2016	The Bridge	BCR	Finance/Banking /Insurance	20,000
Q1 2017	North Gate	Renault	Automotive	20,000
Q1 2016	City Gate	Telekom	IT & Communication	13,000
Q3 2016	Green Gate	Teamnet	IT & Communication	11,000
Q1 2017	City Gate	Rompetrol	Manufacturing Industrial & Energy	10,000

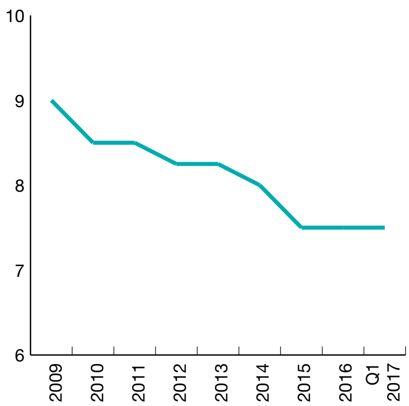
Source: Knight Frank Research

FIGURE 3
Romania property investment volumes
€ million



Source: Knight Frank Research

FIGURE 4
Prime office yields
%



Source: Knight Frank Research

INVESTMENT MARKET

Commercial property investment volumes reached €706 million in Romania in 2016, around 16% higher than 2015 (Figure 3). Although the retail sector saw the greatest allocation of capital at a 37% share of the total investment volume, the office and industrial sectors also saw a significant volume of transactional activity (31% and 30% respectively). Commercial investment volumes totalled €172 million in the first three months of 2017 and were slightly down compared to the same period of last year, but were still one of the strongest first quarters.

Established investors familiar with the market expanded their portfolios by acquiring income-producing assets. In contrast, new market entrants sought both income-producing assets and some with value-add potential.

Foreign funds continued to be the primary protagonists, accounting for almost the entire transaction volume. The Metropolis Centre was a major office transaction and was acquired by Czech PPF Real Estate. Other market players that featured in Romania's investment market originated from the Isle of Man, Singapore, France, the Netherlands and the USA.

Despite improved levels of activity in 2016 compared to 2015, there was no significant hardening of yields. Prime office yields remained stable at 7.5% at the end of the first quarter of 2017. The gap between the local market and leading markets in the wider CEE region (Prague and Warsaw) is still above 200 bps, suggesting that there is scope for moderate yield compression in 2017.

Key recent property investment transactions

Quarter	Property	Seller	Buyer	Approximate price (€)
Q4 2016	P3 Logistic Park	TPG Real Estate	GIC	190,000,000
Q2 2016	Mega Mall	Real4You	NEPI	72,000,000
Q1 2016	City Gate 41%	Bluehouse	GTC	60,000,000
Q3 2016	Metropolis Center	Soravia	PPF Real Estate	50,000,000

Source: Knight Frank Research


The SkyTower, Bucharest's tallest building where Oracle renewed its lease in Q1 2017.

KNIGHT FRANK VIEW

There will be an ongoing trend toward consolidation requirements, as companies seek to move their operations into a single location. The relocation of BCR to The Bridge is a significant example. Outsourcing companies will continue to enter and expand into the market. Developers have demonstrated their ability to offer multi-national companies customised office solutions at lower rents than in some other CEE markets, and the growth in this industry will continue to lead to change in Bucharest's occupational market dynamics.

Around 200,000 sq m of new space is planned for delivery in 2017, oriented towards Center-West and the CBD as well as the traditional northern suburbs. Rental levels are anticipated to remain stable as existing landlords and active developers compete for tenants. Occupiers however will benefit from increased incentives.

In 2017, investment sentiment is expected to remain positive due mainly to economically favourable conditions and competitive risk-adjusted returns. Prime office yields may see some moderate yield compression throughout the year.

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