Dublin Office Market

Q2 2023

Spotlight: The impact of the Grey Market on the quality of available office space

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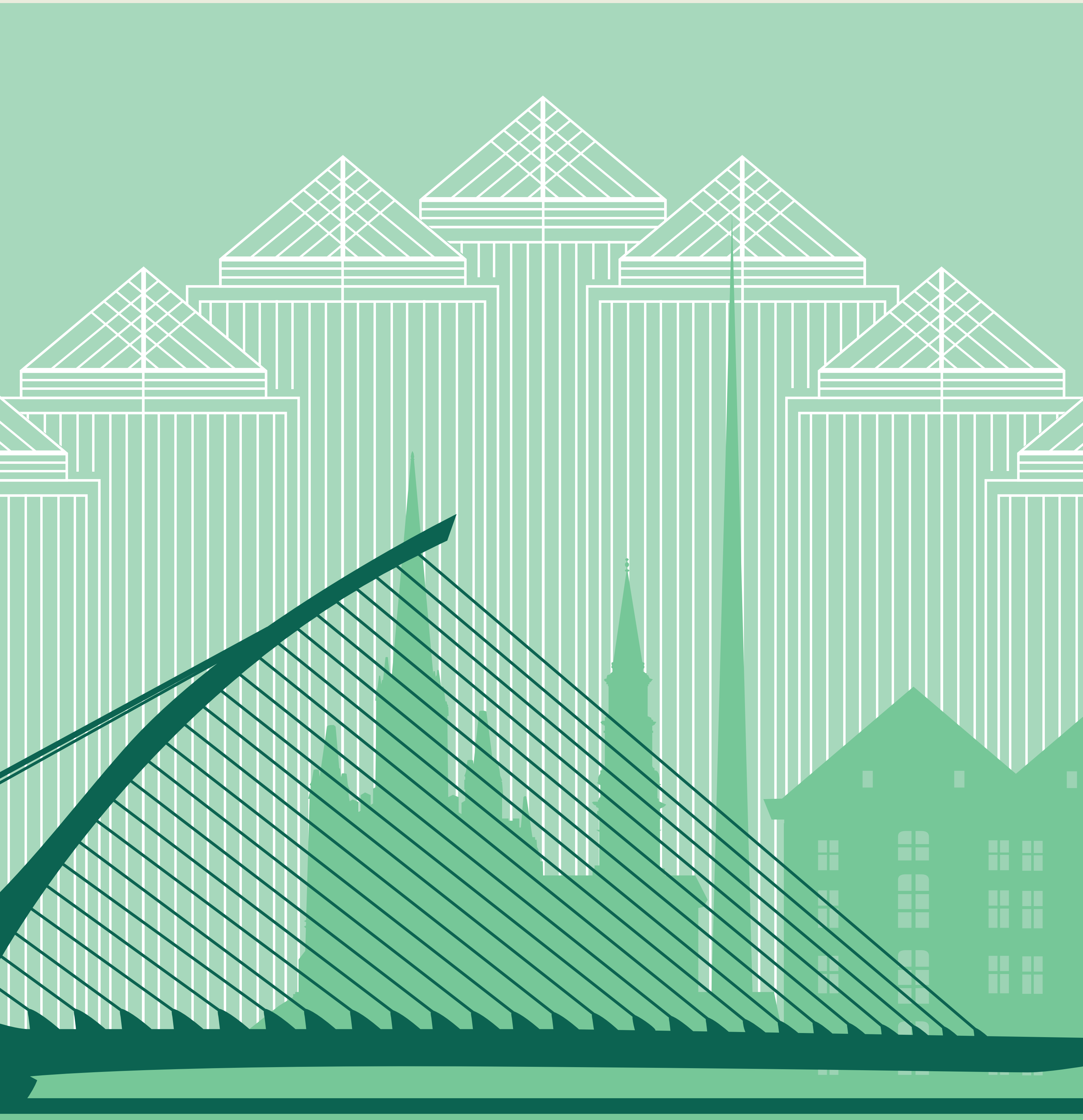

5 Key Takeaways

2.5%-4%

range of GDP forecasts for 2023

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405,968 sq ft

Office market take-up

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25%

of demand came from the Finance sector, 21% from Professional Services & 21% from the State

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30%

Of space due to complete in 2024 is pre-let

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€41.7m

Invested in office assets in Q2 2023

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Dublin Office Market Q2 2023

Amid the multiple challenges, in particular higher debt costs and inflationary pressures, the labour market remains firm, providing the momentum to keep Ireland in a growth position.

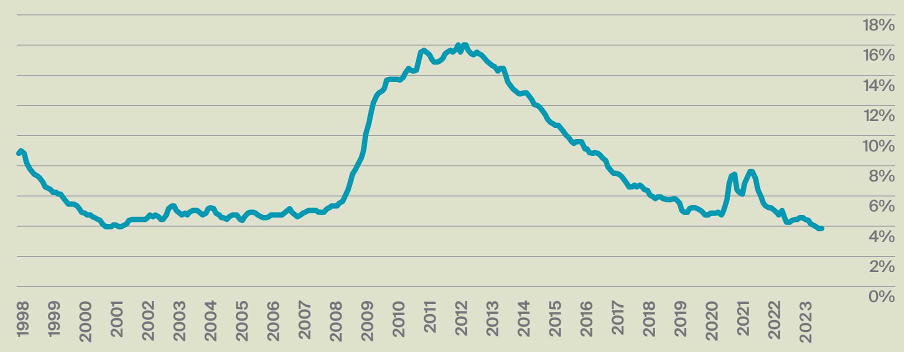
ECONOMY

Most forecasters at the start of 2023 were expecting GDP growth of 5-6% this year and between 2-3% for modified domestic demand (MDD). As the year progresses, forecasts for GDP growth are being revised downwards, while all indications are that MDD will increase by more than expected, reflecting strong activity in the domestic economy.

Q1 2023 GDP data were disappointing with the industry sector (largely driven by multinationals) showing a decline of 13.2% compared to Q4 2022 and more than offsetting growth of 4.9% in the ICT sector over the same period.

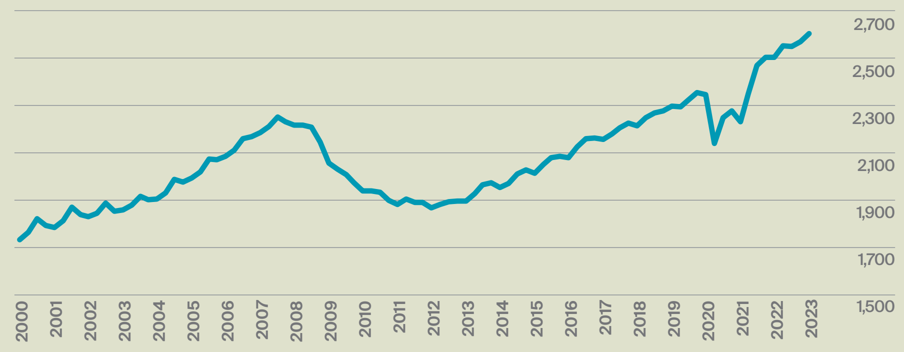
> "While there is some expectation that the ECB will pause after the next forecast increases, the reality is that interest rates are firmly at a much higher starting point and are set to remain so throughout 2024."

Unemployment (%)



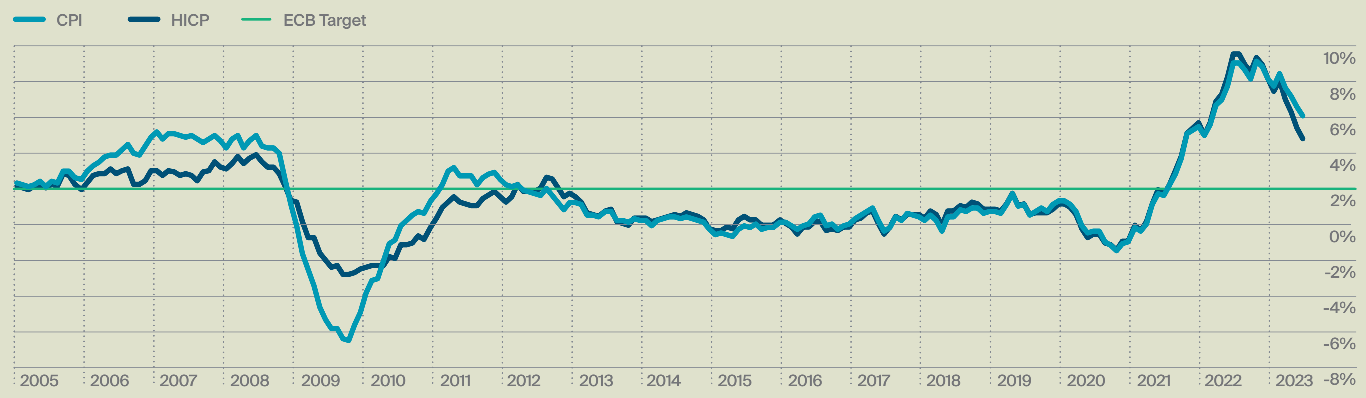
Source: CSO/Knight Frank Research

Employment (000's)



Source: CSO/Knight Frank Research

CPI & HICP inflation rate



Source: CSO/Knight Frank Research

Construction activity increased by 4.3% while Finance & Insurance grew by 8.4%. MDD increased by 0.1% in the quarter.

Compared to Q1 2022, GDP increased by 2.2%, the ICT sector grew by 10.1% year on year and the Industry sector expanded by 1.5%.

Overall, Ireland's position remains positive with Standard & Poor's (S&P) expecting that Ireland will continue to outperform its main trading partners, forecasting GDP growth of 2% this year and 2.5% in 2024, with other forecasters expecting GDP growth of up to 4% for both years.

S&P also upgraded Ireland's long-term sovereign rating to AA from AA- and with a stable outlook. A driving factor is that solid tax revenue growth is expected to deliver budget surpluses out to 2026 allowing Ireland's net debt/GNI* ratio to fall below 60% in 2024, earlier than expected.

The unemployment rate has fallen to 3.8%, the lowest level on record. The number of people in employment, at just over 2.6m, is the highest on record.

Consumer Price Inflation (CPI) peaked in 2022 and continues to edge downwards in 2023. Average consumer prices increased by an annual rate of 6.1% in June compared to an annual rate of 7.5% in January. Meanwhile, HICP moderated to an annual rate of 4.8% in June compared to 7.5% in January.

Expectations are that average inflation will continue to slowly decline, but cost pressures will remain a concern across all sectors.

Debt costs and debt market challenges are set to remain. Consecutive ECB interest rate increases have added 400 basis points to interest rates.

The risk also remains that this cycle of rate increases could turn out to be longer than currently expected, particularly if underlying inflation remains challenging to reduce. This variable is set to continue to weigh on real estate market activity for the rest of 2023, despite the wider positive economic backdrop.

TAKE-UP

405,968 sq ft of office space was let in the Dublin market in Q2. While considerably more than in Q1, when 281,913 sq ft was let, the total for the first half of the year is down compared to the same period in 2022, when just under a 1m sq ft of space transacted.

This reflects the more difficult backdrop being faced by the real estate sector in 2023.

Smaller deal sizes continued to be a feature of the market in Q2. Of the 52 deals that closed, 43 were for space of less than 10,000 sq ft.

Take-up in the city centre amounted to 39% of the total, compared to a typical quarterly percentage of above 50% and compared to 2022 when 76% of take-up was located in the city centre.

> "The largest deal was the letting of 79,600 sq ft at Haymarket House to the National Transport Authority (NTA)."

However, space reserved at this point of the year indicates that take-up in the city centre will exceed 50% for the year as a whole.

The suburbs also accounted for 39% of take-up in Q2, where the largest deal was Jacob's decision to take 30,500 sq ft at the Termini Building in Sandyford.

The largest five deals made up 49% of take-up in Q2. Two were located in Dublin 2, two were located in the suburbs and the largest was at Haymarket House in Dublin 7 in the city fringe.

VACANCY

There has been an increase in the vacancy rate to 13.4% compared to 13.1% in Q1.

This quarterly increase has been largely driven by an increase in suburban space, in particular two buildings in Dublin 15 (Paypal's previous headquarter building and The Aurora Building, both of which are now for sale).

New space due to complete in the city centre later this year and into 2024 will add to vacancy, with a potential increase of over 1% expected over the coming quarters.

RENTS

More cautious demand, at a time of increased supply, has resulted in downward pressure on rents.

> Prime headline rents have edged down from €70 per sq ft at the end of 2022 to €65 per sq ft mid-year. Evidence at this point is that enhanced incentives and rent-free terms are keeping prime rents at or close to €65 per sq ft.

OUTLOOK

The market at this point in 2023 is at somewhat of a cross-roads. Continued economic growth and a strong labour market typically add momentum to office occupier demand. But a set of wider variables – an atypical increase in the supply pipeline, coupled with a more challenging lending environment and cautious international sentiment – set the scene for a quieter than would otherwise be expected second half of the year.

While there are a number of large professional services occupiers active in the market, others, who have not started the process yet may act slower, taking a more cautious approach into 2024.

30%

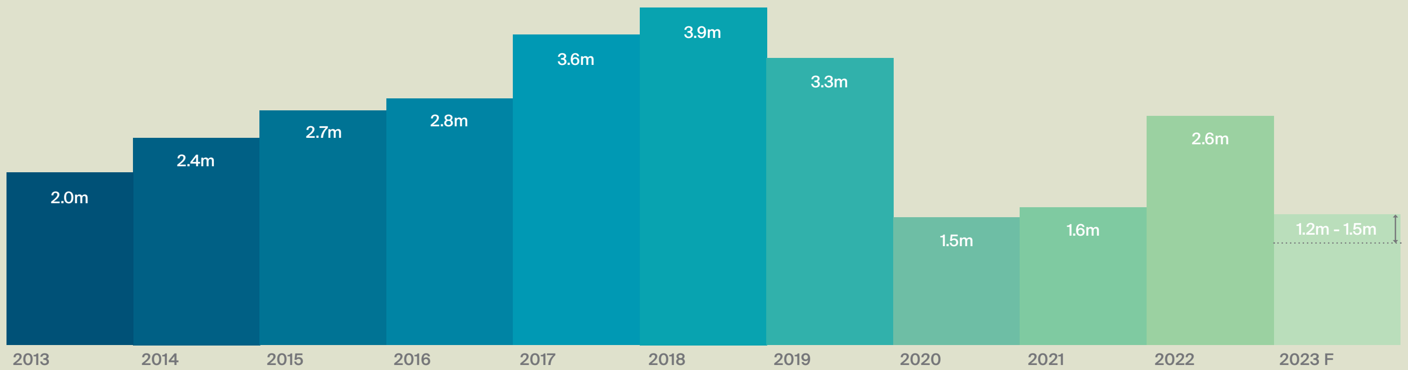
of total space let in Q2 was located in Dublin 2.

Top 5 office leasing transactions, Q2 2023

Property	Tenant	Sector	Size (Sq ft)
Haymarket House, Dublin 7	NTA	State	79,600
Cadenza, Dublin 2	KKR	Finance	39,236
Termini, Dublin 18	Jacobs	Professional Services	30,500
Harcourt Square, Dublin 2	KPMG	Professional Services	27,105
2 Stemple Exchange, Dublin 15	Synopsys	TMT	22,892

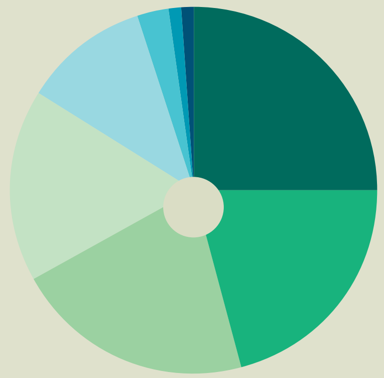
Source: Knight Frank Research

Office take-up
sq ft (millions)



Source: Knight Frank Research
F=forecast

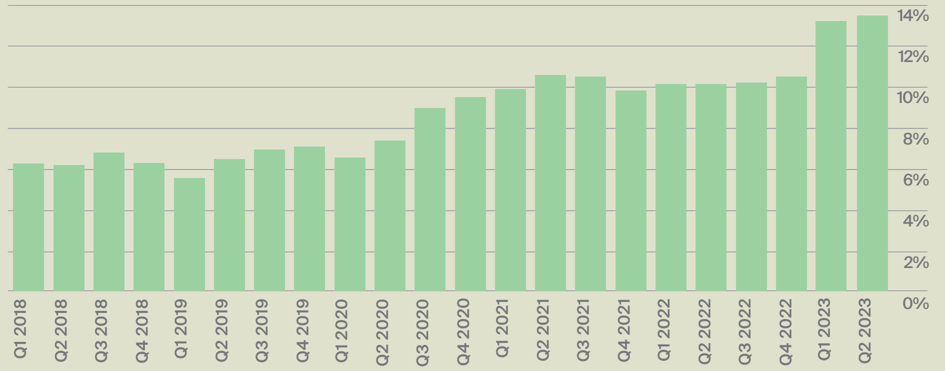
Take up by sector, Q2 2023



Finance	25%
Professional Services	21%
State	21%
Other	17%
TMT	11%
Medical	3%
Pharma	1%
Coworking	1%

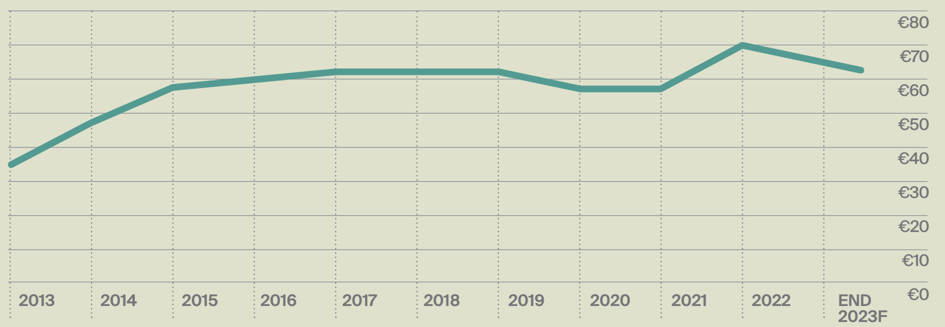
Source: Knight Frank Research

Dublin market vacancy rate



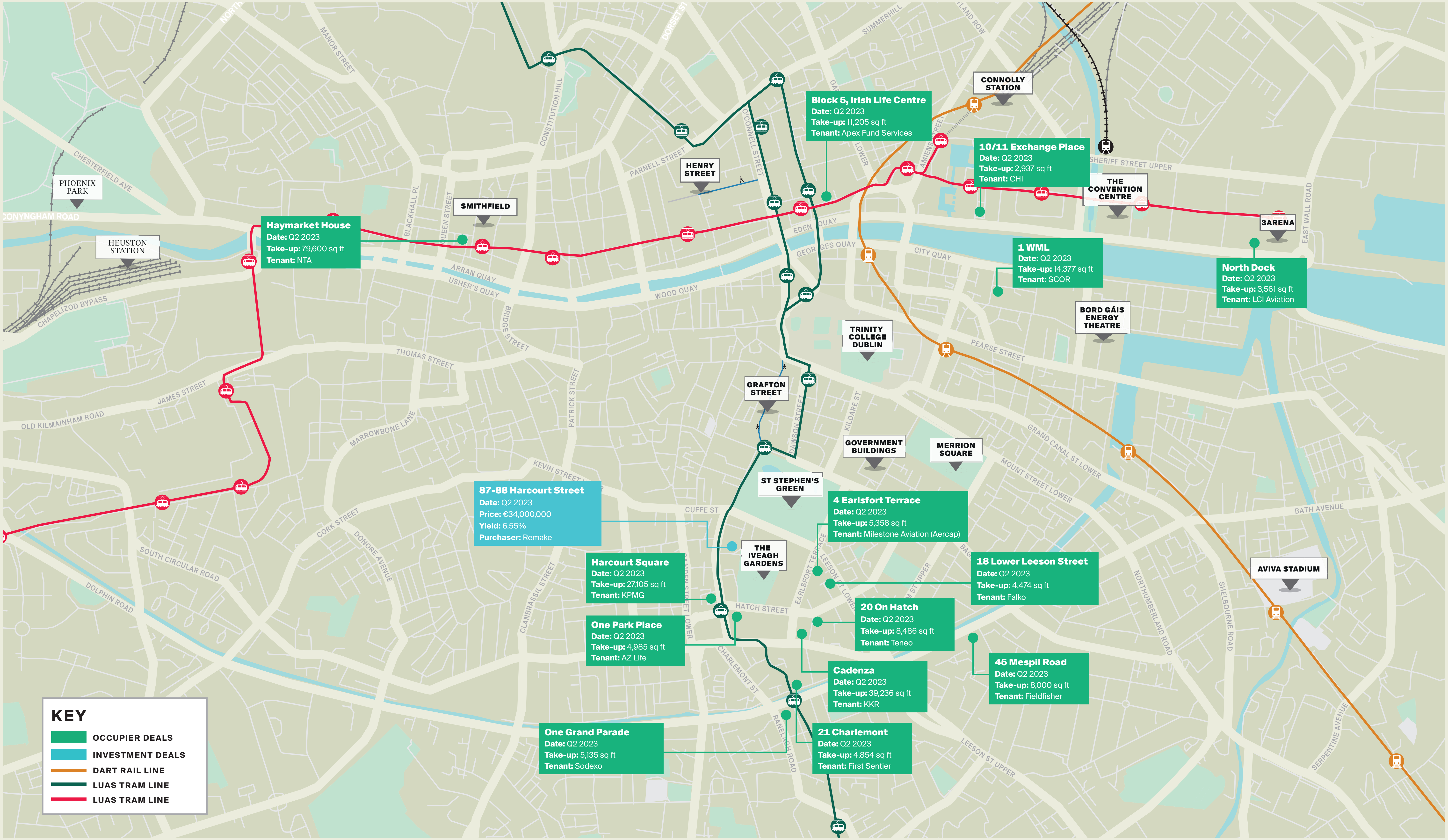
Source: Knight Frank Research

Prime rental series (per sq ft)



Source: Knight Frank Research

Notable Deals Q2 2023



Source: Knight Frank Research

30%

of the office space due to complete in 2024 is pre-let.

OFFICE DEVELOPMENT

Varying levels of delays to completion timelines continue to be felt across the market, with no buildings making the PC dates indicated for Q2. Quarter two was expected to see the delivery of 900,500 sq ft, across eight buildings, all of which are located in the city centre. These are now expected to reach completion in Q3.

At present, close to 2.1m sq ft is expected to complete in 2023, but some of this could edge into 2024.

There are four buildings in the city centre, each over 100,000 sq ft, due to complete in Q3.

One is almost completely let (60 Dawson St with just 29,000 sq ft remaining to let), while the other three are available.

OUTLOOK

While there is a considerable amount of space due to complete in 2023, the current delivery estimates for 2024 and 2025 are considerably lower.

Just over 1m sq ft is due to complete in 2024, all of which is located in the city centre, and the same is the case for 2025.

> "This total of 1m sq ft due in 2025 comprises just seven buildings, three of which (33% of the total space) are pre-let. The largest scheme due to be delivered in 2025 is the Camden Yard development which offers just over 400,000 sq ft adjacent to St. Stephen's Green in Dublin 2."

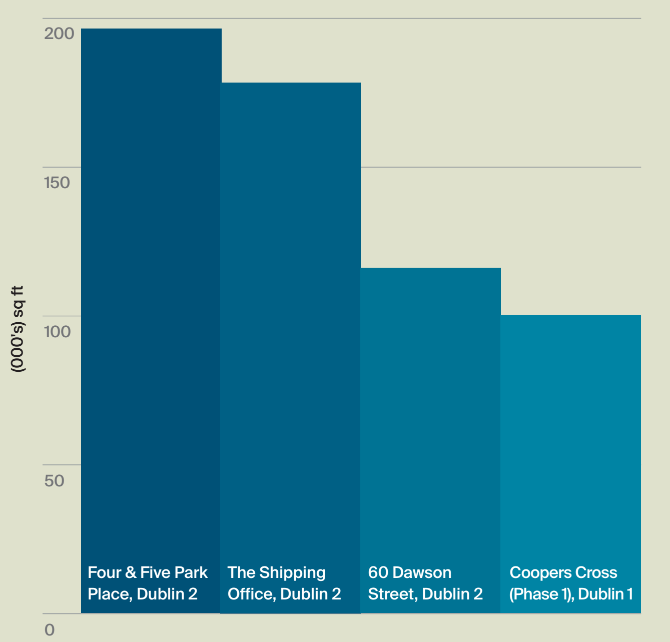
Conditions in 2023 continue to represent an anomaly, with multiple schemes effectively being delivered at the same time as a result of market disruptions since 2020. This will put upward pressure on the vacancy rate by year end.

As this space is absorbed into the market, the pipeline will look tight versus long term annual demand.

Until then however, there are opportunities for occupiers to secure new prime office space at lower rents compared to this time last year and in many cases, with enhanced incentives.

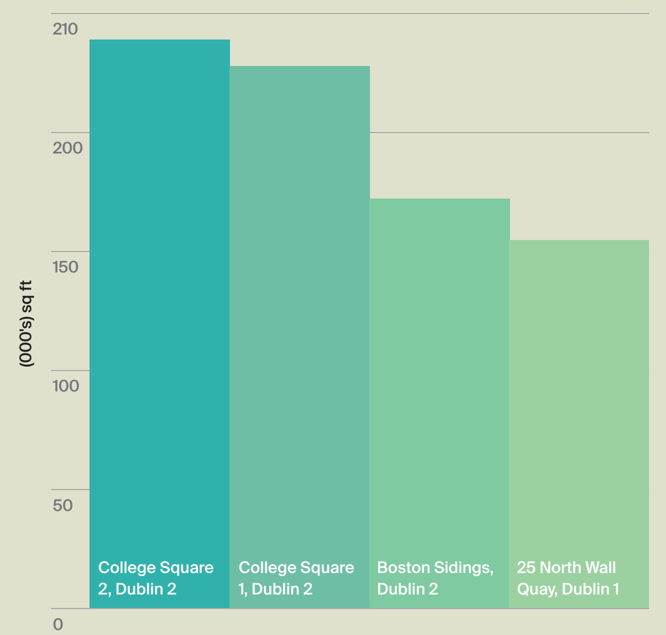
Source: Knight Frank Research

Buildings over 100,000 sq ft due to complete in Q3 2023
sq ft



Source: Knight Frank Research

Buildings over 100,000 sq ft due to complete in 2024
sq ft



Source: Knight Frank Research

Spotlight: The impact of the Grey Market on the quality of available office space

The overall vacancy rate in Dublin's office market has increased from 10.1% at the end of Q2 2022 to 13.4% at the end of Q2 2023.

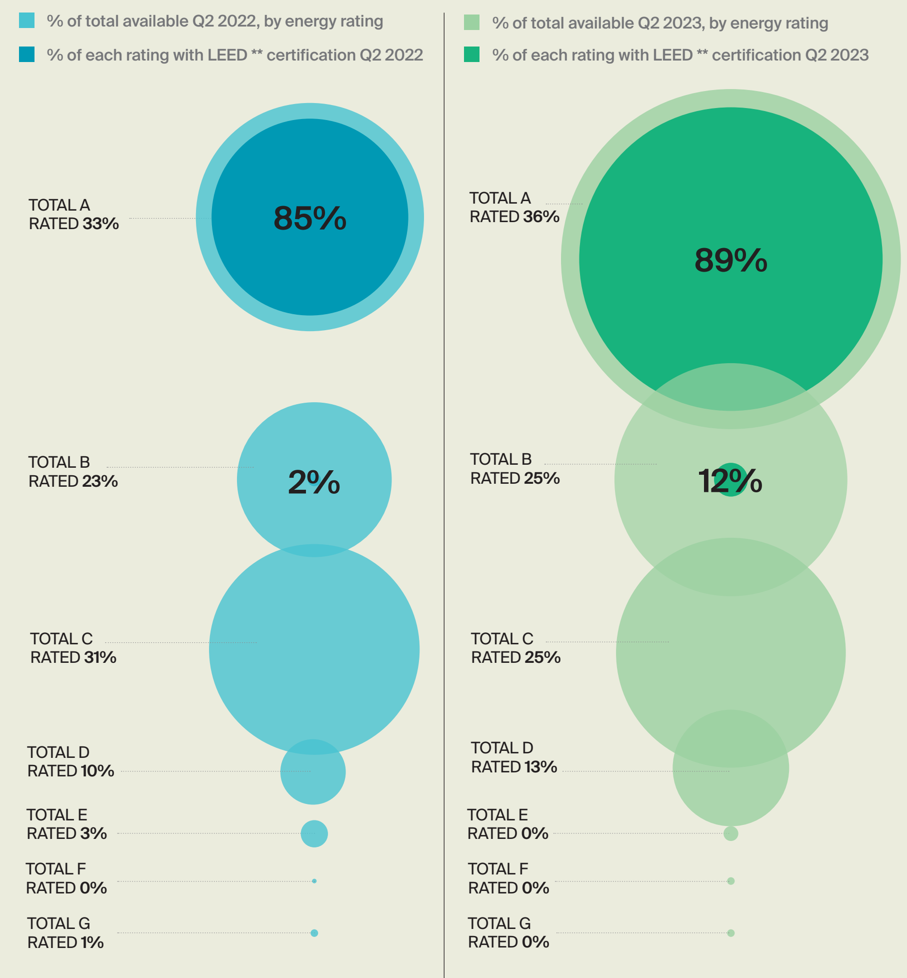
This increase has largely been driven by an unexpected increase in the amount of space that has come back to the market via the grey market.

There are six large buildings (each in excess of 70,000 sq ft) which make up close to 50% of the total grey market space, each of which has been returned to the market by companies in the TMT sector.

The return to the market of some of these buildings has not only increased the amount of space available, it has also increased the amount of space available that have higher energy (BER) and sustainability credentials.

> The vacancy rate for BER A rated space in the city centre with LEED Platinum certification stood at 2.9% at the end of Q2. This compares to 0.8% a year ago.

Available standing stock in the Dublin market by BER* energy rating



Source: Knight Frank Research/SEAI*
** LEED Platinum & Gold

Only two of the largest six buildings on the grey market, Fibonacci Square (387,000 sq ft) and Cadenza (73,000 sq ft), have BER A energy ratings as well as LEED Platinum certification, which is considered to be Tier 1. Excluding Fibonacci however, the amount of choices for space in this top category has changed only marginally in the city centre, with increased availability at 5 Dublin Landings and the return of space at Cadenza being the main changes.

While 20% of the space available in the suburban market has a BER A energy rating, none have LEED Platinum certification and only 13% have LEED Gold certification.

Tier 2 is space with a B energy rating – which equates to 25% of the space currently standing and available across the whole market, an increase from 23% compared to this time last year. Only 12% of that space has LEED credentials. Two city centre buildings offer BER B and also LEED Platinum (Earlsfort Terrace and 1 Cumberland, both in Dublin 2).

> If space available on the market with an BER Energy rating of C and below is excluded, the vacancy rate has increased to 7.6% compared to 5.2% a year ago.

INVESTMENT MARKET

Transactional activity slowed considerably in Q2.

€333m worth of deals completed in the quarter, compared to €1.2 billion in Q2 2022, (excluding the €1.2 billion Hibernia Reit transaction).

Cautious investor sentiment was particularly evident in the office sector, with €42 million transacting across three deals.

Prime yields are under pressure across all sectors.

> "The largest office deal was the purchase for €34m of No. 87 – 88 Harcourt Street by French investor Remake."

Prime office yields are considered to be close to 5% with the low level of activity making it difficult to be exact.

Office investment activity and investment transaction levels in Ireland reflect the wider trend being experienced across all European markets in 2023. Total investment volumes across Europe are estimated to be down 60% between Q1 2022 and Q1 2023.

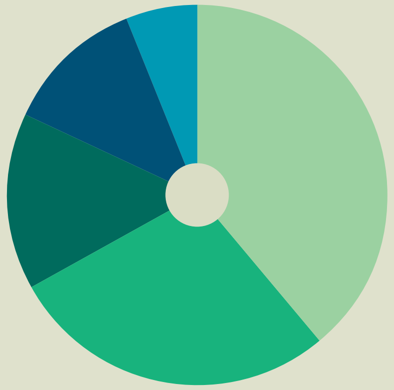
The cost of finance is the main driver of the drop in activity as investors wait and see what the impact will be on pricing. Very limited liquidity is resulting in few active buyers and as a result continued outward pressure on yields is expected across all sectors.

Top Dublin office investment transactions, Q2 2023

Property	Vendor	Buyer	Price	Yields
87- 88 Harcourt Street, Dublin 2	Receiver	Remake	€34,000,000	6.55%
Block A, Westland Park, Dublin 12	Private Irish	Iroko Zen	€4,970,840	7.71%
15 Harcourt Street, Dublin 2	Confidential	Confidential	€2,700,000	4.62%

Source: Knight Frank Research

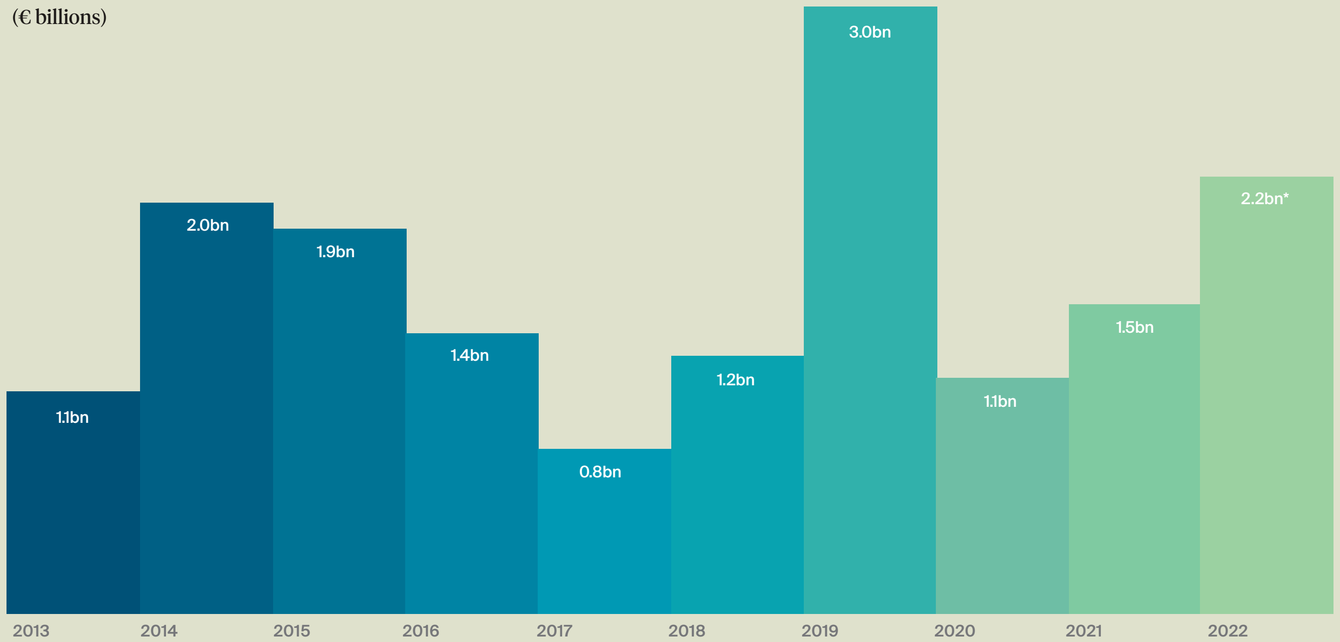
Total investment spend by sector,
Q2 2023



Retail	39%
PRS	28%
Industrial	15%
Office	12%
Mixed-Use	6%

Source: Knight Frank Research

Dublin office investment volumes
(€ billions)



Source: Knight Frank Research
*Includes Salesforce.

Dublin Office Market Q1 2023

New Homes Construction Survey 2023

The Wealth Report 2023

Ireland Residential Investment Market Overview Q1 2023

Ireland Investment Market Overview Q4 2022

Active Capital 2022

We like questions, if you've got one about our research, or would like some property advice, we would love to hear from you.

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