RESEARCH

Knight Frank

PRAGUE

OFFICE MARKET OUTLOOK
Q4 2017

OCCUPIER TRENDS | INVESTMENT TRENDS | MARKET OUTLOOK

KEY FINDINGS

Gross take-up reached a record volume in the first nine months of 2017; the IT sector was the most active.

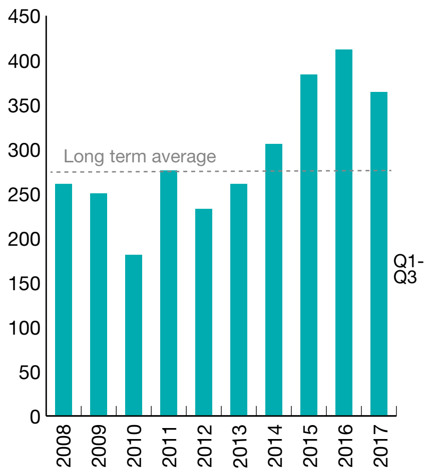
Vacancy levels have continued to come under downward pressure due to low completion volumes and robust demand.

Prime headline rents increased to €20 per sq m per month at the beginning of 2017 and have since remained stable.

Office investment volumes in Prague totalled €746 million in the first nine months of 2017, on par with the same period last year.

Prime office yields remain at 4.75% in Prague; the lowest of the CEE markets.

FIGURE 1
Total office take-up
sq m (000s)



Source: Knight Frank Research

OCCUPIER MARKET

Prague's office market is thriving. Development activity is in full swing with 333,200 sq m of office space under construction.

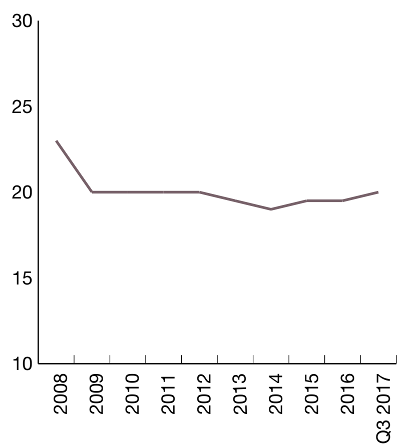
The Czech economy is in very good shape. Following a slowdown in 2016, the economy has returned to strength reflecting increased business and consumer confidence. The labour market is undergoing a peak period in an environment of economic prosperity. Employment has been increasing. In September this year, the unemployment rate dropped to a record low of 2.7% and for the last two years, the Czech Republic has maintained the tightest labour market in the EU.

Against a backdrop of solid macro conditions, the Czech market benefits from a stable political environment and relatively low cost of labour. These have in part contributed to the burgeoning business services sector and rising occupier demand in Prague's occupational market. To that end, leasing activity soared in the first nine months of 2017. Gross take-up reached a record volume (349,100 sq m, Figure 1). In line with recent trends, the IT sector was the most dynamic accounting for 18% of the total take-up. In this sector, Amazon took on the largest lease (12,500 sq m) in the first phase of the project Rustonka R1 in Prague 8.

Availability in the Prague office market has been falling over the past few years. At the beginning of 2016, the vacancy rate stood at 13.9% and has since decreased to 7.7% - the lowest level seen since 2008. This steep decline has been due to a combination of low completions and strong demand. New construction activity has now started to rise as a result. Over 330,000 sq m of office space is under construction and planned for delivery in the final quarter of 2017 and in 2018. It is possible that new deliveries will push the vacancy rate up slightly, but most projects under construction are already partially pre-leased.

Prime headline rents increased at the beginning of 2017 to €20 per sq m per month and have remained stable. As current market conditions favour the landlord, incentives and flexibility in negotiations have decreased slightly.

FIGURE 2
Prime office rents
€ per sq m per month



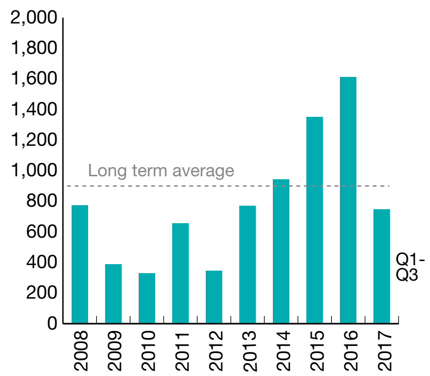
Source: Knight Frank Research

Key office leasing transactions in 2017

District	Address	Tenant	Size (sq m)
Prague 4	BB Centrum A	Moneta Money Bank	21,500
Prague 8	Rustonka R1 (Phase I)	Amazon	12,500
Prague 8	KPMG Office Centre	KPMG Czech Republic	11,000
Prague 4	The Park 8;10;12	Honeywell	10,000
Prague 7	A7 Office Centre A, D, E	Czech News Center a.s.	7,800
Prague 7	Visionary	Accenture Central Europe	7,100

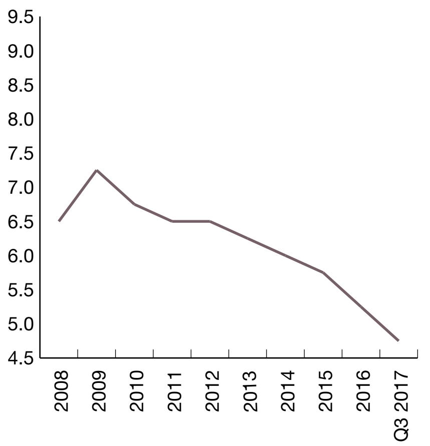
Source: Knight Frank Research / Prague Research Forum

FIGURE 3
Prague office investment volumes
€ million



Source: Knight Frank Research / Real Capital Analytics

FIGURE 4
Prime office Yields
%



Source: Knight Frank Research

INVESTMENT MARKET

Prague was CEE's top performer for office investment in the first nine months of 2017. A total of €746 million worth of assets transacted over this period, bringing the transactional volume on par with the same period last year (Figure 3). The rise in investment activity over recent years reflects growing investor appetite in view of the market's economic and political stability, transparency and higher returns. Although full-year office investment volumes are unlikely to match last year's total, 2017 will be another solid year.

Several large-scale transactions concluded over the first nine months of 2017. The mixed-use development Palác Euro / Astra (€86 million) and Blox (€68.5 million) were the largest deals to materialise, both acquired by cross-border investors. Indeed, the investor profile has broadened to a wider geographic area. Prague has been attracting capital from the US, China, Germany and Switzerland. Despite this, domestic capital remains the most prevalent.

The uninterrupted weight of capital entering Prague's commercial real estate market is causing property prices to escalate. Prime office yields have fallen by 50 bps over the last year to 4.75% and are now the lowest of the CEE markets. The weight of capital is likely to put further downward pressure on yields.

Key office investment transactions in 2017

Property	Seller	Buyer	Approx. price (€ million)
Palác Euro / Astra	Dragon Capital	Generali	86
Blox	BPD development	CFH Group	68.5
Avenir Business Park	Lone Star	Mint Investments / Tristan Capital Partners	60
River Garden I	IAD Investments	LaVA (LASalle)	57
Futurama Business Park (A,B,C)	Invesco Real Estate	Caerus Investment Management	Confidential

Source: Knight Frank Research / Real Capital Analytics


Mechanica, completed by Penta Investments

KNIGHT FRANK VIEW

Occupier activity in Prague has been exceptional in 2017 and there are no signs of this abating. International corporates continue to target Prague as a hub for Business Process Outsourcing (BPO) activities in view of its favourable economic and political landscape, and a skilled, relatively low cost labour force. Due to a sizeable development pipeline, prime office rents are expected to maintain stability into 2018, placing occupiers into a better negotiating position.

Prague has been increasingly on the radar for global investors. With the Czech economy forecast to strengthen, investor confidence is likely to grow. Any high quality office product coming to the market is likely to attract strong investor interest. Strong capital flows are expected to be sustained in 2018, with intense competition for product placing yields under further downward pressure.

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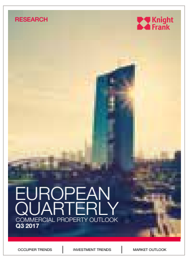

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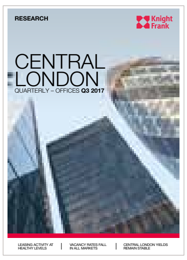

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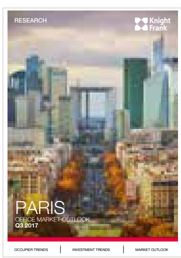

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