

Briefing note

Falling incentives as the office market improves

June 2014

An improved picture overall

■ Rent incentives are determined by the different market fundamentals (availability, demand, confidence) combined with the individual local characteristics. They are therefore a good indicator of the general market sentiment.

■ Compared to last year's survey, the general mood has improved, although the extent of this varies from market to market, and is not fully reflected in demand levels yet.

■ Prime CBD headline rents have grown strongest in Dublin as well as the Scandinavian and German cities, mostly as a result of tight demand and supply conditions. Generally, the market is now driven by large-scale requirements that are facing supply constraints in many markets. After about three years of limited new developments on the markets, the best space has been absorbed and most of the vacancy is now concentrated in

secondary locations and buildings.

The average rent-free period is falling

■ Compared to the same period in the previous year, the average rent free period granted by landlords has fallen by 11.4% across the 21 markets surveyed. However, a fall of rent free months was only recorded in 8 of the markets while the period remained stable in the remaining 13.

■ The highest reduction in rent free months was recorded in Dublin and Hamburg (-50% each), Amsterdam (-33%) and London City (-25%).

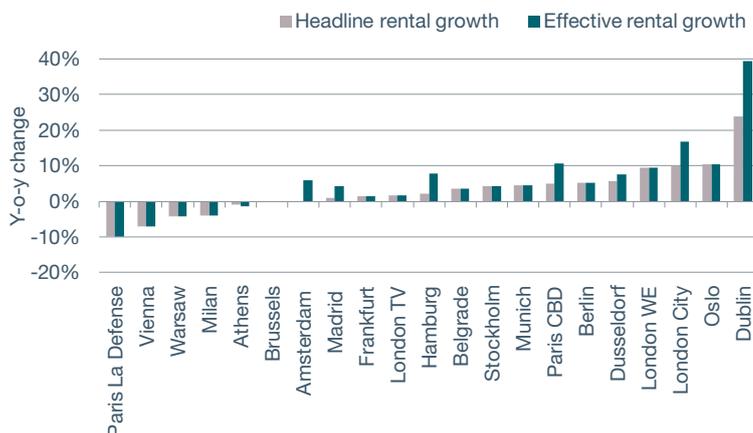
■ The average discount* offered stands at 10.3% in H1 14, down from 12.3% in the same period last year.

■ The highest discount is still offered in Milan (25%), followed by Paris La Defense (21%) and London Thames Valley (TV) (18%) where rent free months have stayed unchanged since the last survey.

TABLE 1
Rental concessions 2014

	Discount*	Change in discount 2013-2014	Net effective rental growth 13-14
Amsterdam	10%	-33%	5.9%
Athens	2.5%	0%	-1.3%
Berlin	5%	0%	5.2%
Belgrade	5%	0%	3.6%
Brussels	8.3%	0%	0%
Dublin	10%	-50%	39.3%
Dusseldorf	6.7%	-20%	7.7%
Frankfurt	6.7%	0%	1.3%
Hamburg	5%	-50%	7.8%
London City	15%	-25%	16.7%
London West End	10%	0%	9.5%
London TV	18.3%	0%	1.6%
Madrid	13.9%	-17%	4.4%
Milan	25%	NA	-4%
Munich	5%	0%	4.4%
Oslo	5%	0%	10.5%
Paris CBD	16.7%	-20%	10.6%
Paris La Defense	20.8%	0%	-9.9%
Stockholm	6.7%	0%	4.4%
Vienna	8.3%	0%	-7.1%
Warsaw	11.7%	0%	-4.2%

GRAPH 1
Headline vs effective rental growth H1 2013-2014



Graph source: Savills

*As a percentage of rent free months over a typical lease period for prime CBD office space.

→ ■ Athens offers the lowest available discount at 2.5%, followed by the three largest German cities (Berlin, Hamburg, Munich), Belgrade and Oslo which are all at 5%. This has equally stayed unchanged since last year (with the exception of Hamburg).

Where the sentiment improves, the discount is going down...

■ Generally, we can say that incentives have come down in all markets where supply of prime space is constrained and/or the markets are picking up from the aftermath of the crisis, and landlords are able to rethink generous discounts.

■ Of all markets surveyed, the rent free period has only remained stable in Oslo since our first survey in 2008. While the incentives have not come down yet in Vienna, Warsaw, Paris La Defense, Brussels and Milan since the beginning of the crisis, Amsterdam and London City are the only two markets where the discount has continuously been decreasing since 2009.

■ In Dublin, the falling discount is an indicator of the overall improved market. As the Irish economy has recovered, employment in the service sector has accelerated and given new dynamics to the leasing market. The discount is now only 10% - down from 20% in previous years - which is slightly below the European average.

■ London City has seen a similar surge in take up (at the highest level since 2000), which has reduced one of the previously highest rental discounts in the survey area to 15%.

■ The German markets have proved stable throughout the financial crisis, with the discount on offer never exceeding 10%, while headline rents have not faded either. The reasons behind this are the low new development activity over the past years which has shortened supply, as well as the general resilience of the German labour market and wider economy.

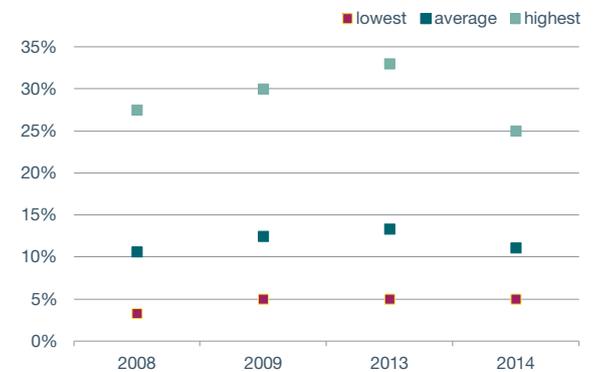
...and effective rents are growing

■ Incentives have an impact on the net effective rental growth in office markets. Thanks to the decrease of rental discount on average, the effective rental growth in Q1 2014 is 5.1% y-o-y, compared to an increase of headline rents of 2.9%.

■ Based on net effective rental growth, the strongest y-o-y increase has been recorded in Dublin (39%), London City (17%) and Paris (11%).

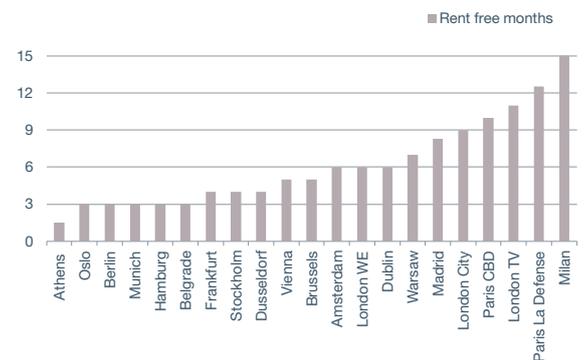
■ Depending on the change in rental discount, the difference between headline and net effective rental growth/ rents can be significant (>5%). These markets include Dublin, Paris, Hamburg, Amsterdam, Madrid and London City. On the other hand, effective rental growth was below headline change in Athens due to the reduction of the lease length there. ■

GRAPH 2 Discount on offer in European office markets Recovery from the peak in 2013



Graph source: Savills

GRAPH 3 Rent incentives over a 5-year lease period The European average is 6 months



Graph source: Savills

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