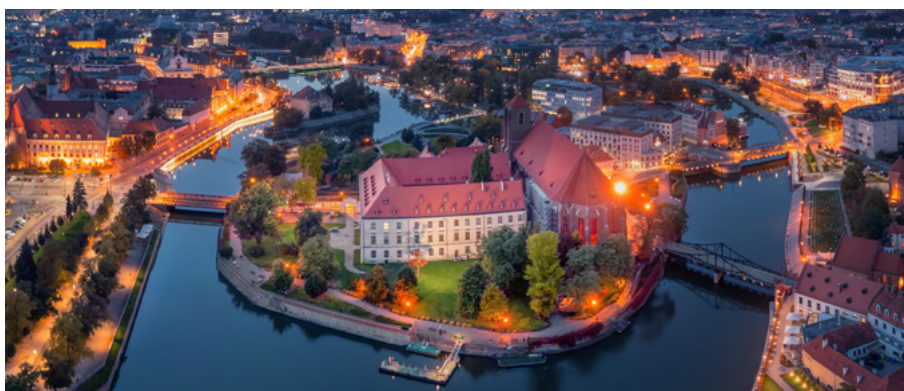


Office market in Wrocław



- Gradual increase of demand • Upcoming pipeline • Negative absorption •

🏗️ Limited developers activity resulted in the lowest level of supply since 2011 with only 21,800 sq m of office space delivered to the market.📉



641,200

Population
(VI 2021)



2.0%

Unemployment
rate (XII 2021)



PLN 7,136

Average salary
(XII 2021)



107,900

Students (2020)



26,400

Graduates (2020)



24

Universities
(2020)

Absorption - the biggest challenge

Economic overview

Almost two long years have passed since the outbreak of the Covid-19 pandemic during which our reality has changed significantly. We have experienced a remodelling of our private and professional lifestyles. Currently, everything indicates that business and individuals have adapted to the new environment and the first signs of improvement and return to the pre-pandemic everyday life are already visible on the horizon.

Due to the outbreak of the pandemic, Poland's economy experienced its first GDP decline since the political transformation (a drop of 2.5%). However, the decrease was smaller than in the strongest economies in the region, where the EU recorded a 5.9% decline in GDP, while the eurozone economy contracted by 6.4%. Current forecasts for the Polish economy are positive, according to Oxford Economics the Polish economy will grow by 5.1% in 2021. Currently, the greatest challenge for governments in the region, including Poland, apart from fighting the pandemic is undoubtedly the rising inflation, which in Poland in December

reached 8.6%, the highest in 20 years. In order to minimize the negative effects, MPC (Monetary Policy Council) decided to raise interest rates 3 times in a row, starting in October, ending 2021 with 1.75% interest rate, which is the highest since 2014. Currently the interest rate level is 2.25%, while further increases are expected due to persistently high inflation.

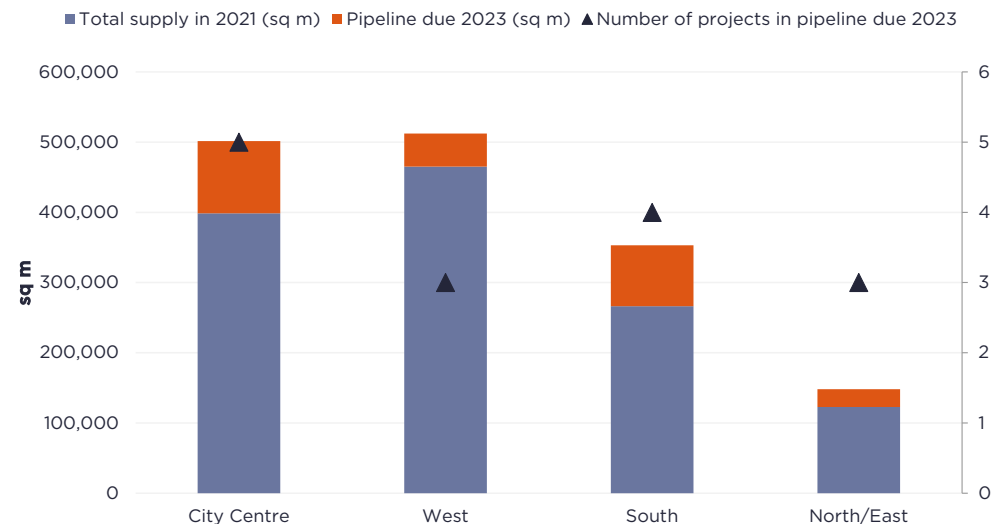
Wrocław is one of the leading economic centers in Poland. However, like the rest of the economy, the city saw its GDP fall by 2.3% in 2020. Despite the ongoing pandemic, forecasts for the city are positive. According to Oxford Economics, GDP growth will be 4.8% in 2021 and 5.6% in 2022. Such high increases in the city's GDP will certainly contribute to the development of commercial real estate and the labour market, which will directly translate into increased employment and demand for office space.

Supply

Wrocław is the second largest regional office market in Poland, accounting for 21% of regional office space. Total modern office space available in Wrocław amounts to 1,253,100 sq m. Due to its size and maturity, the market has been divided into four characteristic zones. The zones include: City Centre (398,700 sq m), the largest – West (465,300 sq m), South (266,300 sq m) and the smallest office zone – North/East (122,800 sq m).

In 2021, the office market grew by two projects totalling 21,800 sq m) Krakowska 35 by Atal (11,800 sq m) in South zone and WPB Strzegomska Park II by Devco (10,000 sq m) in West zone. This is the lowest volume of new supply since 2011, when projects totalling 18,100 sq m were completed. Despite the increase in vacancy, developers continue to maintain positive sentiment towards the office market in the city. As an example, there are currently nine schemes under construction in the city with planned completion in 2023 with a total area of just under 140,000 sq m.

Supply development in Wrocław between 2021-2023



Source: Savills

42%

Renegotiations

36%

New leases

11%

Pre-leases

11%

Expansions

Take-up by type in 2021

Currently, most of the under construction space is located in the South zone (69,500 sq m) and City Centre (51,600 sq m). The largest projects under construction are Midpoint 71 by Echo Investments (36,700 sq m, due 2022) and Centrum Południe II by Skanska (24,000 sq m, due 2022). In addition, the developers have a number of projects with building permits totalling over 122,000 sq m which will start construction in the near future.

Letting activity

The city saw a decline in demand even before the pandemic broke out. From a record 2017, a decline in demand was observed which continued till 2019. On the other hand, after the outbreak of the pandemic, an increase in demand for office space was recorded in 2020 and 2021. In 2020, demand was 128,400 sq m, while in 2021 it was 6% higher reaching 136,300 sq m. Despite the gradual increase in demand, absorption in Wrocław in 2021 was negative (-3,500 sq m), significantly deviating from the 2010-2021 average when it remained at 60,000 sq m.

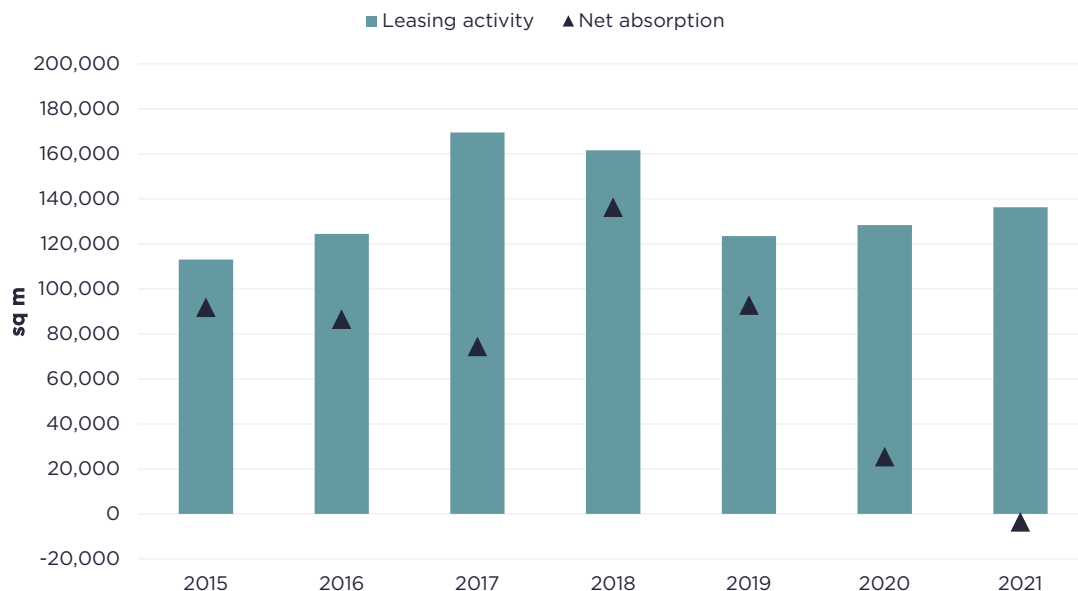
The systematic increase in demand since the outbreak of the pandemic is a positive trend. Additionally, there is growing

confidence in tenants' growth strategies, which is evident in the prevalence of new leases (36%), pre-leases (11%) and high levels of expansion (11%) compared to renegotiations, which accounted for 42% of demand.

Invariably, demand in Wrocław is driven mainly by the IT sector, which accounted for 34% of take-up last year. Other sectors with high tenant activity were manufacturing (19%), business services sector (13%) and finance sector (10%).

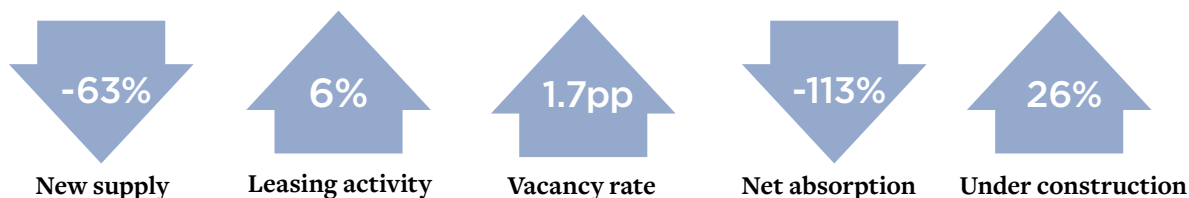
A current trend that may gain momentum over time is the increased interest in subleases. Companies looking to improve their financial performance may decide to sublease space from other tenants, which is usually associated with more favourable terms and a shorter lease term, allowing them to wait out more difficult times. In addition, we observe a significant increase in interest in serviced space, which thanks to its flexibility allows for effective management of a portfolio of leases among tenants who are planning expansion or need support in remodelling the corporate model forced by a pandemic.

Leasing activity in Wrocław between 2015-2021



Source: Savills

2021, change over year



Key office Indicators 2021



1.25 million sq m

Total supply of office space



139,700 sq m

Total under construction space



21,800 sq m

New supply



16.7%

Vacancy rate, Q4 2021



136,300 sq m

Total take-up



-3,500 sq m

Net absorption

Flexible office

Flexible office is a service that has been increasingly considered by tenants in recent years as a replacement for the traditional office. The current work transformation forced by the pandemic can only contribute to the even greater importance of serviced offices in the market.

As the third largest office center in the country, Wrocław is also characterised by a high level of flexible office availability with total stock exceeding 26,500 sq m, the majority of which was built after 2018. This result translates into a market saturation of flexible space at 2.1% (ratio of flexible to traditional space).

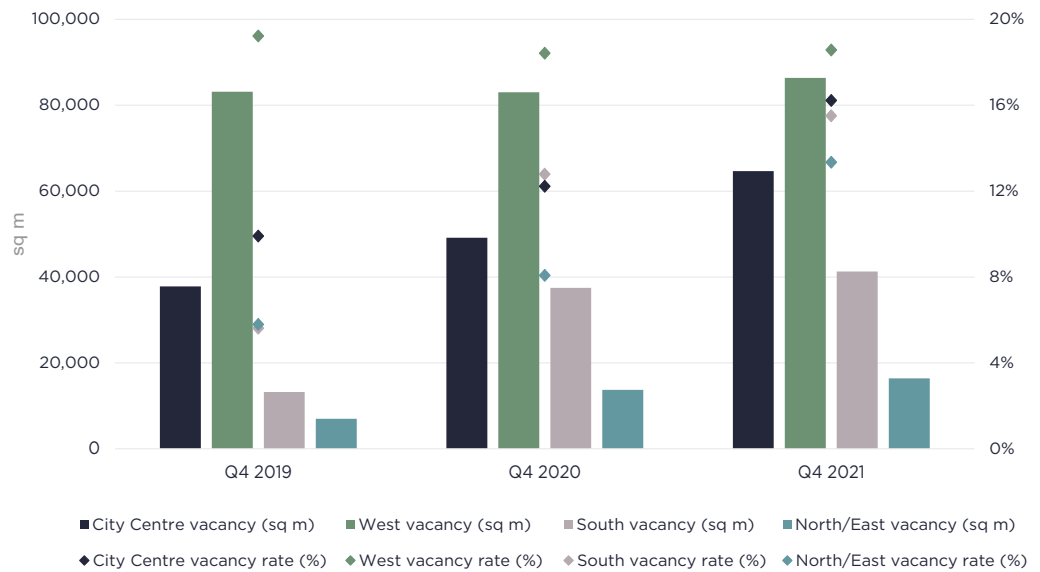
The largest operators include: City Space (7,300 sq m in three locations) and Concordia Design with largest location in the city (4,500 sq m). The remaining stock is fragmented amongst smaller operators.

The reason, which will provide a solid foundation for the further development of flexible offices, is undoubtedly the fact that this type of service is no longer being considered only by smaller, expanding companies, but also by global corporations, which appreciate the benefits of flexibility and the ability to easily adapt their real estate portfolio to project requirements.



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Vacancy evolution in Wrocław between 2019-2021



Source: Savills

Vacancy

Slower demand growth due to the pandemic outbreak, prolonged commercialisation process of newly developed buildings have contributed to an increase in vacancy rates in the city. At the end of Q4 2021, the city had 207,700 sq m available office space, which translates directly into a vacancy rate of 16.7%. This is a significant increase of 400 bps since Q4 2019.

Compared to the pre-pandemic period at the end of 2019, vacancy in the city has increased in every office zone except West, where a decrease by 70 bps was recorded. The largest increases were in the South zone (by 990 bps), North/East zone (by 760 bps) and City Centre zone (by 630 bps) zones. The main reasons for these increases, in addition to lower demand, is the high vacancy rate in buildings that were completed in 2020-2021, where the vacancy rate currently stands at 28.2%.

Rents

Even despite pandemic, prime headline rents remain on stable level. Actually in the range of EUR 13.50–15.50/sq m/month. Taking into consideration actual situation on the office market - no further movement in rental levels is predicted in the nearest future.

As mentioned, even during the pandemic, headline rents remained stable. However, we forecast further changes in effective rents, mainly due to higher vacancy which translates directly into higher competitions for landlords, who will be forced to operate on incentives packages, due to rent free periods or fit-out contribution. Rising inflation will directly impact higher fit-out contribution costs, mainly due to prices of materials and contracting. The habit of tenants to get a turnkey office is unchanging, so this affects developers.

Outlook

During the last two years, a pandemic has constantly accompanied us, which has contributed to the rearrangement of our lifestyles, both private and professional. At present, all indications are that the situation is slowly stabilizing, and individuals and businesses have begun to adapt to the new reality. The stabilization is reflected in positive economic forecasts, according to which the economy will grow at a high rate, which will directly translate into the labor market, i.e. also the office market, which is an important element of it.

While demand for office space in the city remains strong, we forecast further significant growth as economies stabilize. Higher demand will contribute to the absorption of existing office space in the short term, meaning a decrease in vacancies and further stabilization of the office market. In the long term, a decrease in vacancy will be an incentive for developers to increase the amount of space under construction, which, thanks to strong economic growth, will be gradually absorbed by tenants, keeping rents at stable levels.

🔗 Rising inflation may prove to be a key factor affecting lower effective rents, mainly through higher fit-out contribution costs. 🔗



For further information please contact:

Office Agency

Daniel Czarnecki
Head of Landlord
Representation
+48 519 033 717
dczarnecki@savills.pl

Jarosław Pilch
Head of Tenant Representation
& Workthere Poland
+48 694 497 800
jpilch@savills.pl

Bartosz Plewa
Regional Manager
+48 668 347 247
bartosz.plewa@savills.pl

Dominika Babiarz
Junior Consultant
+48 600 327 127
dominika.babiarz@savills.pl

Research

Wioleta Wojtczak
Head of Research
+48 600 422 216
wwojtczak@savills.pl

Jarosław Jachura
Senior Consultant
+48 507 334 167
jaroslaw.jachura@savills.pl

