

Offices



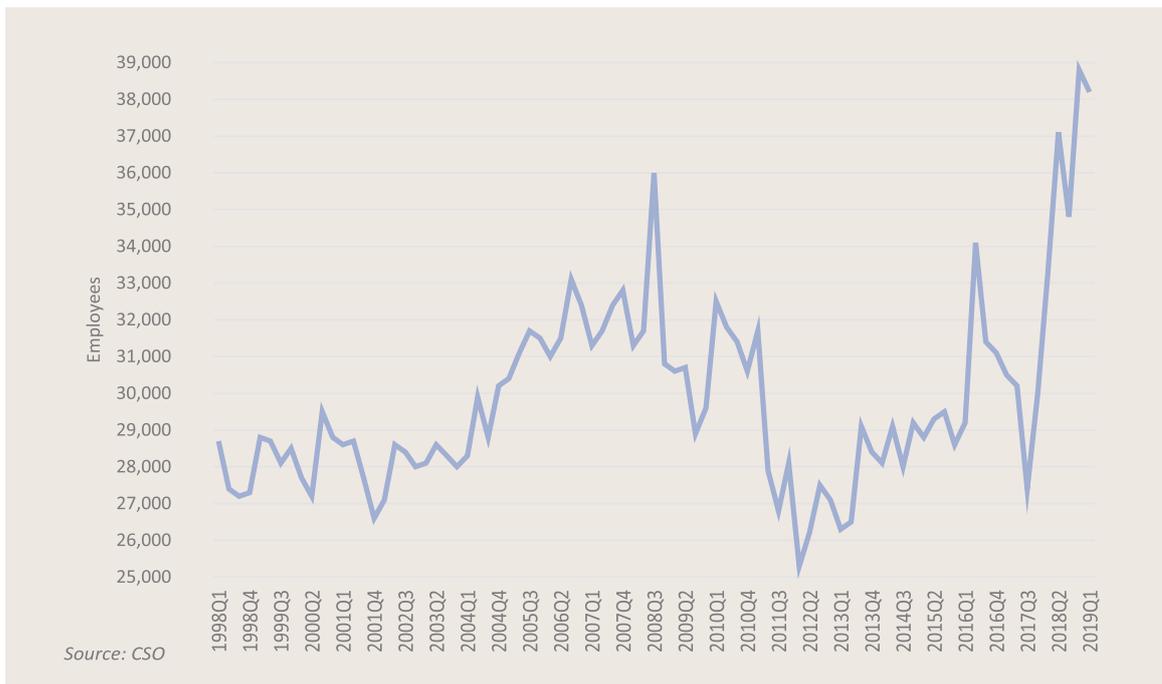
The Reflector, 113,000 sq ft let to Airbnb, LogMeIn and Wix. 7,300 sq ft available to lease

Introduction

The Irish economy has had an exceptionally strong start to 2019. Total employment is up by 3.7% in the year to March 2019, and 81,200 persons have been added to the payroll. This represents the fastest jobs creation since the height of the economic boom in Q3 2007. Twenty-six percent of the new jobs are located in Dublin, and more than two thirds of these (13,600 jobs) are in office-based activities. The strongest expansion has been in Government employment with more than one-in-three of the new office jobs being in Public Administration and Defence. As a result the headcount in this sector is now 6.1% above its pre-crisis peak in 2008, and more than 50% above its cyclical low in 2012.

However employers in other office-based sectors, including those in the professional services, financial services and ICT industries, have also been recruiting. Overall, office-based employment in Dublin has expanded by 5.6% in the last 12 months, and continues to comfortably outstrip the national average. The increasing dominance of office-based jobs growth in Dublin reflects two long-term trends; the continued urbanisation of Irish society and an ongoing sectoral shift towards service-based activities which is increasingly being facilitated by technological advances.¹

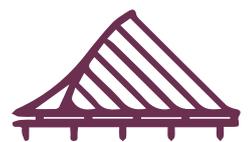
Figure 1: Employment in Public Administration – Dublin



Total employment is up
3.7%
in the year to March 2019



81,200
persons have been added to the payroll



26%
of the new jobs are located in Dublin

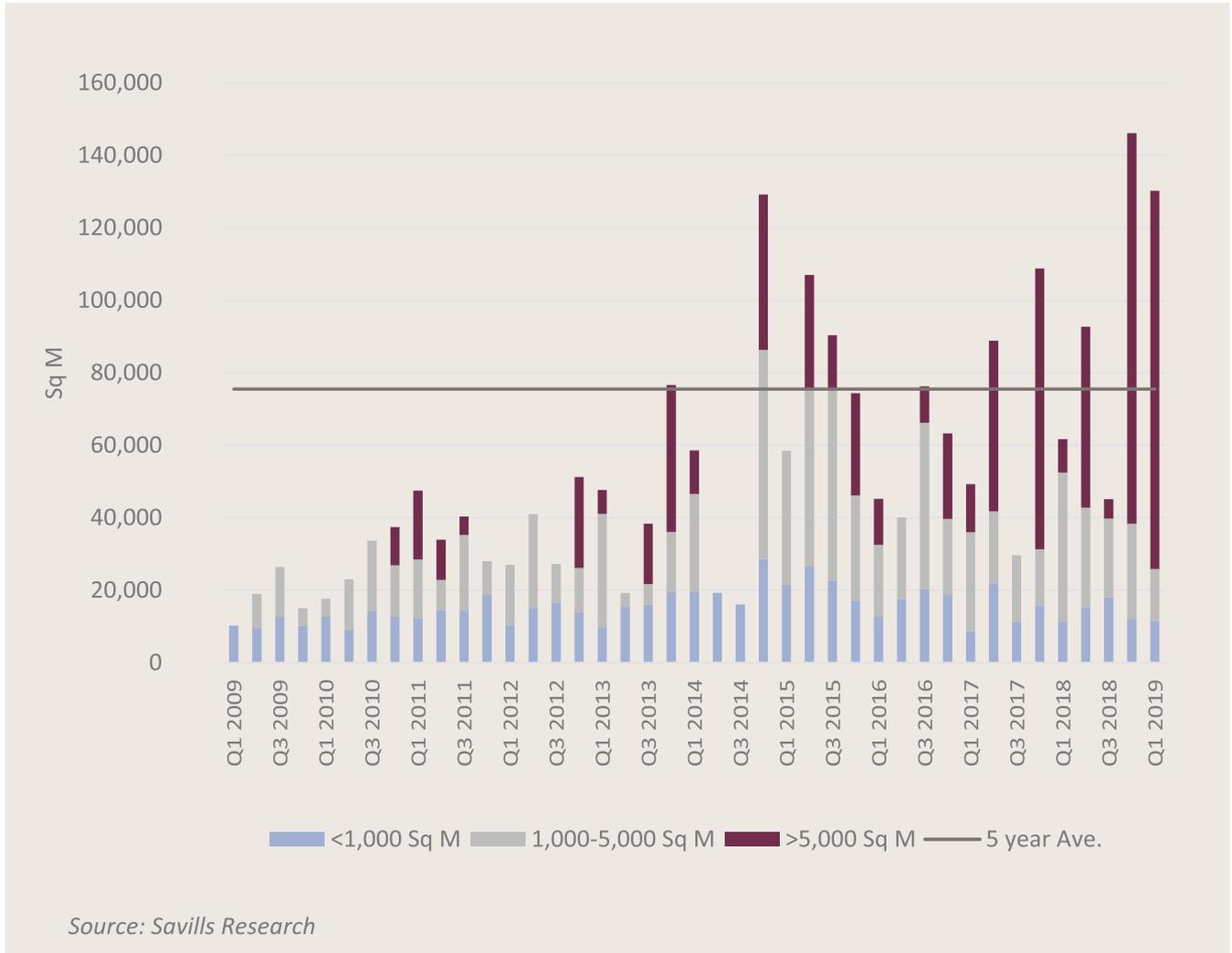
¹ Census data show that Ireland's population increased by 173,613 between April 2011 and April 2016. 80% of this increase was concentrated in urban centres (53% in Dublin) and Dublin accounts for 44% of the State's urban population.

Leasing Activity

After a record year in 2018, take-up of purpose-built office space in Dublin remained very strong through Q1 2019, with 130,235 sq m of space

taken. This is the second highest quarterly take-up in over a decade and is more than twice the Q1 2018 figure.

Figure 2: Dublin Office Take-Up By Size And Quarter



As noted in recent reports Dublin has seen a pronounced rise in the number of larger lettings in recent years, and ICT firms have been behind many of these. There were eleven 5,000+ sq m deals in 2018 with technology giants such as Google, Facebook and LinkedIn taking large parcels of space in Dublin. This trend continued into Q1 2019 with Salesforce pre-letting 43,664 sq m at Spencer Place, Facebook taking 16,165 sq m in Sandyford, and Docusign leasing 9,162 sq m at 5 Hanover Quay. As shown in Figure 2, lettings of 5,000 sq m or more accounted for just over 80% of total take-up in Q1, and 65% of take-up over the last 12 months. In contrast to this has been a decline in sub-1,000 sq m deals from 100% of the space let a decade ago to 9% in Q1 2019. As noted in our Q4 report the increased availability of serviced office product has led to fewer companies directly leasing small quantities of space in the market.²

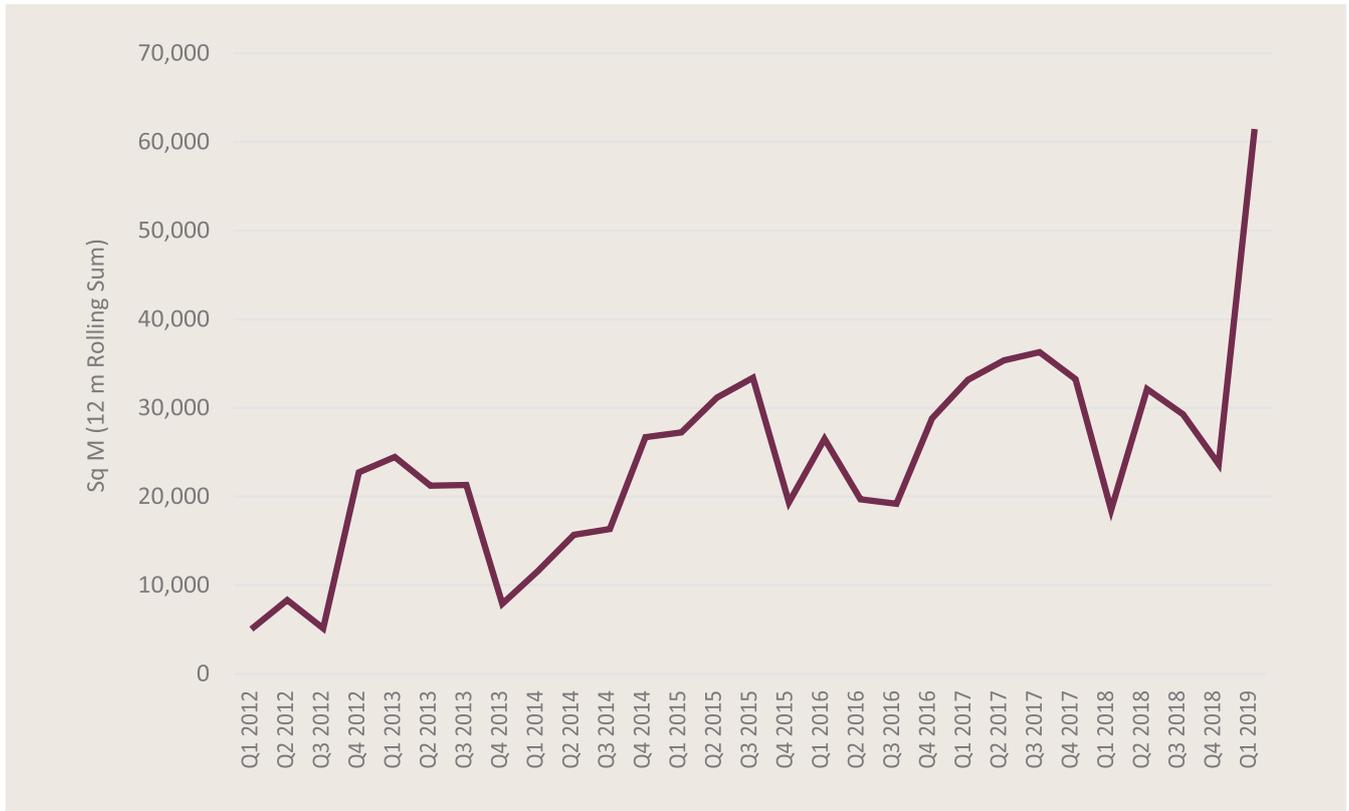
ICT's involvement in many of the larger deals means that this sector continues to account for a majority of total take-up in the Dublin market; 55.4% in 2018, and 55.8% in Q1 2019. This is before allowing for 'hidden' ICT take-up within serviced offices (where the initial leases fall into the 'Real Estate' category). The scale and growth of the ICT industry

does, however, tend to obscure the expansion of other sectors. Figure 3 shows that, in absolute terms, there has been a steady increase in office leasing by public bodies since early 2014. In part this reflects a proactive approach by the Office of Public Works (OPW) to achieve greater efficiencies through active management of its business space portfolio, and to modernise its office stock to enhance the working environment for staff and achieve productivity and environmental performance improvements. Recent examples of this include moves by the Department of Health from Hawkins House (built 1965) to the newly refurbished Miesian Plaza (heavily refurbished 2017) and the NTMA from the Treasury Building (completed 1990) to No. 1 Dublin Landings (built 2018).

However it also reflects jobs growth. Employment in Public Administration and Defence bottomed-out in 2012 but, as outlined above, has been rising strongly since then, particularly since the lifting of the public service recruitment moratorium in Budget 2015. This has inevitably fed into a greater requirement for office space.

² Providers of this service office space accounted for 11% of traditional lettings in 2018.

Figure 3: Public Sector (Ex. Semi-State) Take-Up of Dublin Offices



Navigation Square Cork. High quality new office development. Available now.

Net Absorption

Strong economic growth should lead to increased office space absorption as the share of expansions and new entrants increases as a proportion of total lettings. Based on an occupancy rate of 10.3 sq m per employee,³ the 13,600 additional office jobs created in Dublin over the last 12m should be

expected to translate into approximately 140,080 sq m of business space absorption. Broadly in line with this back-of-the envelope calculation, and when we allow for some occupiers procuring space in advance, net absorption of 161,350 sq m was actually recorded.

Box 1: Calculating Occupational Density in the Dublin Office Market

Occupational density (average space per office-based employee) is useful to know, not least because it enables us to translate employment forecasts into forecasts of office demand. It is straightforward in principle to calculate the occupational density ratio as the occupied stock, divided by the number of office-based workers.

For many years Savills has been tracking Dublin's office stock and decomposing this into its occupied and vacant elements. However accurately measuring office-based employment - the second item that is necessary to work out occupational density - is slightly compromised by data availability. The quarterly Labour Force Survey (LFS) is the main source of employment data in Ireland. LFS data are routinely published for Dublin at the single-digit sector level. This is sufficient for tracking trends in office employment, but not for pinpointing the absolute number of workers who consume office space in Dublin. There are two reasons for this. Firstly, LFS is predicated on place of residence rather than place of occupation. So any office workers who live outside Dublin and commute into town for work are not counted. Secondly, the standard single-digit sectoral classifications used by the LFS are quite broad. When using the LFS, we assume all employees in the following sectors are 'office-based';

| NACE 1 Digit | Description |
|--------------|-----------------------------------|
| J | ICT |
| K-L | Finance, Insurance, Real Estate |
| M | Professional Services |
| N | Administrative & Support Services |
| O | Public Administration |

However this is clearly a simplification. For example some people in the financial services industry are based in retail units rather than office blocks. And, equally, some employees in omitted sectors e.g. manufacturing actually work in office buildings.

To work around these problems Savills has obtained, by request from CSO, employment data from the 2016 Census that is both predicated on place of occupation and disaggregated to 2-digit sector level. The former enables us to capture office workers living outside Dublin who occupy office space in the capital. The latter enables us to more precisely identify persons who are genuinely office based.

Using this dataset Savills estimates that there were 315,557 office-based employees working in Dublin as of April 2016. Matching this against the 3,246,991 sq m of occupied office space in Dublin as of Q2 2016, gives us an implied occupancy ratio of 10.3 sq m / employee. This verifies the accuracy of agents' traditional 10 sq m / employee 'rule-of-thumb' as an average.

Although absorption has been strong over a 12m timeframe, Q1 2019 was something of an anomaly. Despite more than 130,000 sq m of lettings, occupied space rose by just 12,580 sq m. This quirk arises from the fact that 61% of the space taken-up between January and March 2019 was pre-let. Such transactions get reflected in take-up when the lease is signed. But they do not add to occupied space until the buildings are actually completed some time later. Eventually, however, this lag will unwind - when the new office blocks reach practical completion they will immediately count as occupied space and will drive net absorption at that point. Because of this anomaly it is theoretically possible to have a quarter in which absorption exceeds take-up, and we may well experience this when some of the recent large pre-lets reach practical completion (PC) over the coming years. Three examples of large pre-commitment deals in Q1 were;

Table 1: Major Pre-commitment Deals Q1 2019

| Building | Occupier | Sq M |
|-------------------------------------|-------------------------|--------|
| Spencer Place | Salesforce | 43,664 |
| 4 & 5 Dublin Landings* | Central Bank of Ireland | 18,674 |
| The Distillers Building, Smithfield | OPW | 16,722 |

* Forward purchase



Kildress House, 22,000 sq.ft available to let, delivering Q4 2019

³ For a more detailed analysis of occupational density in the Dublin office market please see accompanying text box

Market Supply and Vacancy

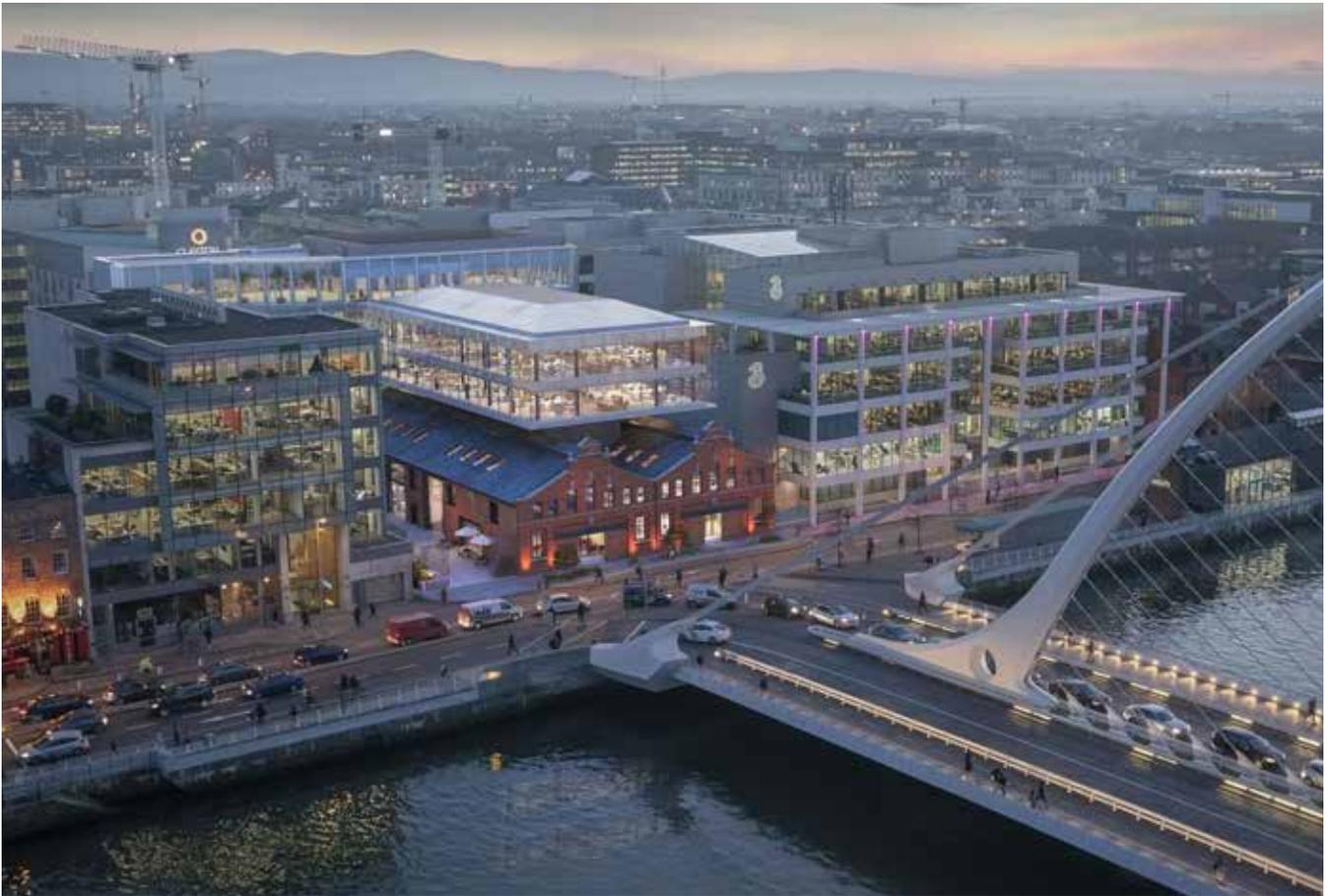
Development

The office development cycle in Dublin has now been underway for four years and 508,723 sq m of new space have been delivered in this time. However, when we subtract demolitions, net additional space is a modest 229,165 sq m. This wedge between gross and net completions has become a critical factor in understanding current and future supply / demand dynamics in the market; the potential for new development to outstrip the absorption of space is being materially offset by the decommissioning of older stock. In Q1 2019 some 46,321 sq m of new space was completed. But 15,168 sq m of this was offset by demolitions, resulting in net completions of 31,153 sq m for the quarter.

Savills has detailed intelligence on the point at which new buildings are being let during their construction programme.⁴ The proportion of space remaining vacant when buildings are newly completed has been

quite flat over the last 18 months, and has actually edged lower in the prime postcodes of D1, D2 and D4. Eighty five percent of the stock that completed in 2018 is now either let or reserved. Moreover, of the office space that is due to complete in 2019 and 2020, 56% and 50% respectively is already now committed. The latter is a remarkably high figure for stock that is almost two years away from completion.

However, as the development cycle matures it is inevitable that more buildings will reach PC without having been fully absorbed through pre-letting or mid-letting activity. The conclusion is that developers may be prudent to factor in some post-PC voids in their underwriting, especially in the suburbs where a number of buildings have recently completed without being fully let.



The Tropical Fruit Warehouse, 80,000 sq ft of exceptional office space delivering in Q2 2021

Development Sites

Flattening growth in capital values, increased build-cost inflation, and the potential for post-PC voids would ordinarily be expected to translate into downward pressure on office site prices. However there is no evidence of this as yet. For now, site prices are strong at over €4,300 per sq m

(on target nett lettable floor areas) for super-prime sites, though perhaps there is a countering effect of increased aspirations for capacity on sites when developers are forced to compete for sites. Arguably this is being driven by the new Urban Development and Building Heights Guidelines.⁵

⁴ Available by request.

⁵ Introduced in December 2018: https://www.housing.gov.ie/sites/default/files/publications/files/aa_conclusion_statement.pdf

Vacancy

With net completions outstripping absorption, the amount of vacant space rose slightly in Q1, and the vacancy rate across Dublin now stands at 8.4% of stock. As ever vacancy rates vary by location and building quality.

The CBD vacancy rate is currently 5.2%, with 4.5% of the docklands office space standing vacant.

Figure 4: Vacancy Rate - Dublin Offices

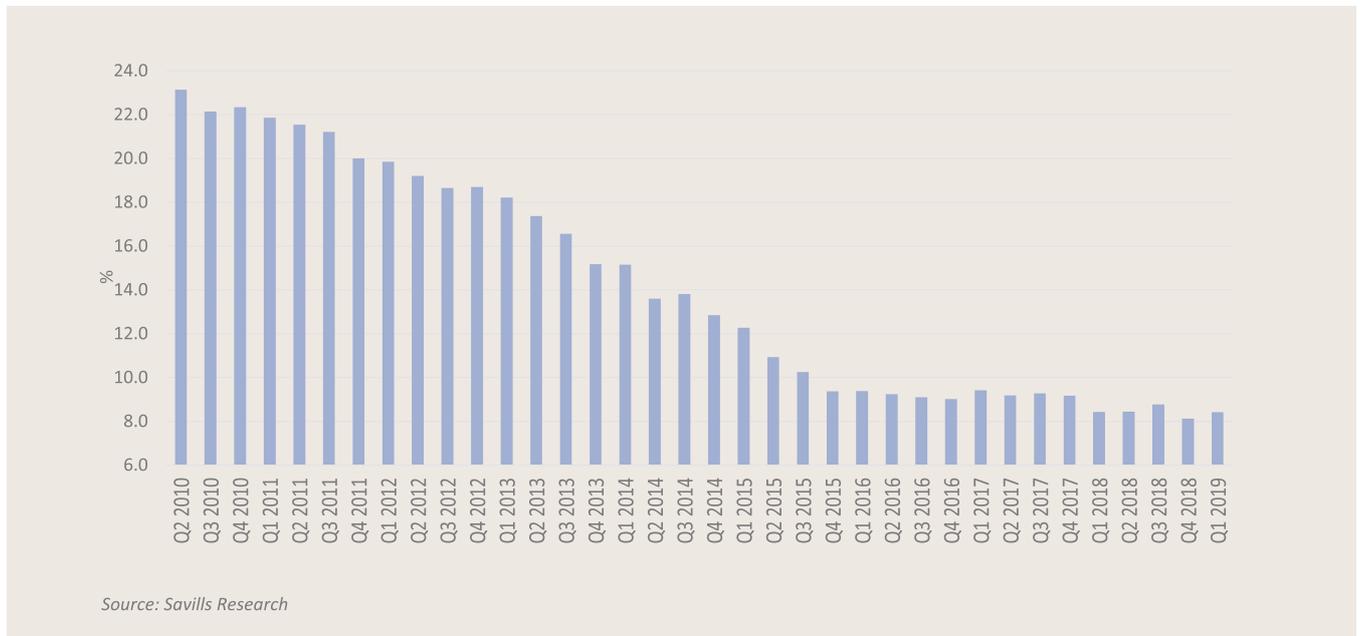
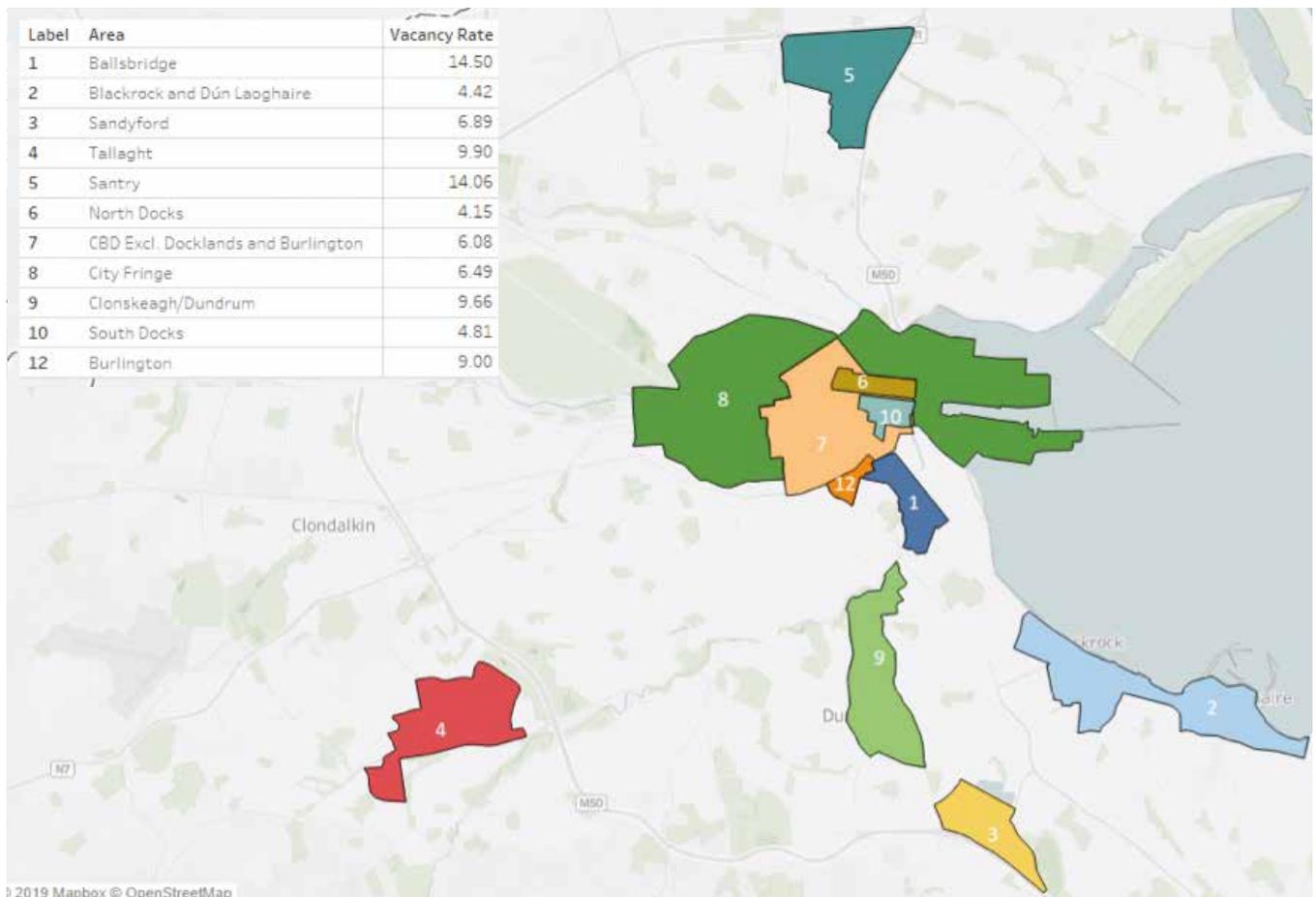


Figure 5: Vacancy Rate by Detailed Location, Q1 2019





The EXO Building, Dublin's tallest office block. 170,000 sq ft delivering Q4 2019

Rents and Outlook

With vacancy rates well below their natural level, theory suggests that there should be upward pressure on rents. However agents report no movement in prime headline rent figures over the last 12m, observing that landlords are more focused on the quality of covenants and on securing income through longer lease terms, rental caps-and-collars etc.. This is because of the manner in which investments are being priced given upwards and downwards rent reviews. Savills' view is that headline rents of up to €700 per sq m per annum are being achieved for the best buildings in the best locations, although most CBD lettings are at rent levels which are below this. Typical rent-frees are 6-12 months depending on minimum lease length and covenant strength, among other factors.

Looking ahead, the supply pipeline remains very well contained and Savills expects only around 121,000 sq m of net additional space to be built this year – after adjusting for demolitions. If we follow consensus jobs growth forecasts, more space than this should be absorbed during the year – 135,000 – 145,000 sq m – meaning that the vacancy rate is likely to squeeze lower again later in the year. We expect the vacancy rate across the entire of Dublin to be around 7.5% by year end – its lowest figure for more than 20 years. At the very least this should provide support for current rent levels and could, arguably, lead to further modest rental growth.



76 Sir John Rogerson's Quay 100,000 sq.ft. of Grade A office HQ space with undisturbed river fronting views available in Q4 2019

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