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Savills Offices
Ireland

Market in Minutes
Dublin Offices

Q1 2018

Introduction

Since our last report the economic news-flow has remained positive. Ireland's labour market is currently in a real sweet spot. On one hand strong and sustained jobs growth has brought unemployment down to 5.9% in April, its lowest rate for a decade. On the other hand there is still some spare capacity for additional growth – both through increased labour force participation and through a further contraction in the unemployment rate. Because of this, wages are only picking up modestly (+2.1% y/y) and the competitive gains that have been achieved in recent years remain in place.

The continued strength of the labour market has fed into a marked improvement in the public finances. Figures released in April show that the deficit was cut to just 0.3% of GDP last year and the debt ratio, which had reached 124.2% of GDP in early 2013, has now retreated to 68%. This figure is targeted to fall further and should reach the required 60% level by 2021.

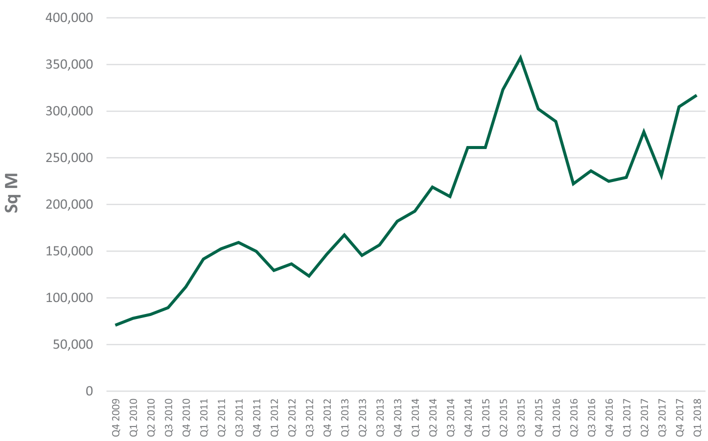
The improved public finances have created space to address some of Ireland's long-standing economic constraints. In February Project Ireland 2040 was launched, comprising a spatial strategy which covers the next 22 years (The National Planning Framework) and an integrated spending plan for the coming decade (The National Development Plan). Expenditure of €116bn should bring Ireland's public investment spending back above the EU average under this plan. And the various infrastructure, environmental and regional development schemes contained within it will enhance the competitivness of Dublin and Ireland's regional cities as business locations.

5 Earlsfort, Dublin 2.

Market Demand

After a very busy Q4 2017 when 136,851 sq m of purpose-built office space was taken-up, activity reverted to 61,700 sq m in Q1 2018 – broadly in line with the long term quarterly average. This is notably lower than the take-up figures quoted by some other agencies. The main reason is our understanding that the LinkedIn lease on One Wilton only became unconditional in Q2. This notwithstanding, the momentum that currently exists is evident in Graph 1 which shows continued growth in take-up on a four-quarter rolling basis, and April's lettings suggest that Q2 will be another strong quarter.

Graph 1:
Dublin Office Take-Up – 4 Quarter MA

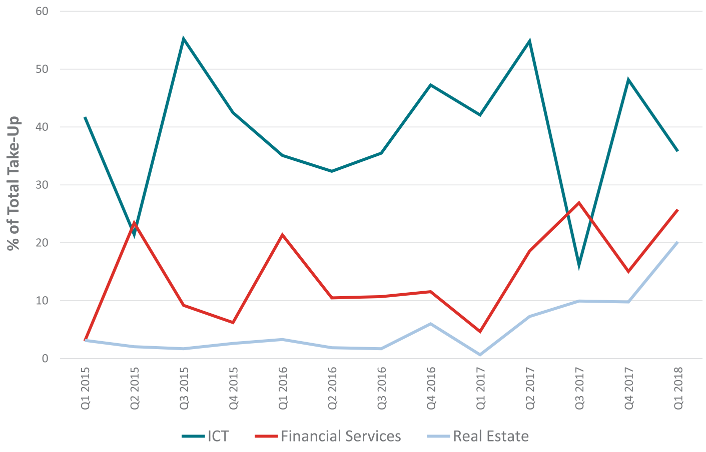


Source: Savills Research

Take-Up by Sector

22,000 sq m of Dublin office space was taken by occupiers from the ICT sector in Q1, and the share of space accounted for by this sector continues to hover in-or-around 40% of total take-up. The importance of US tech multinationals to the Dublin market was again evident with Google taking 7,900 sq m across two lettings in Sandyford. However, while ICT remains the dominant consumer of space, there has been a marked up-shift in the proportion of take-up accounted for by two other sectors. Financial companies took just under 16,000 sq m in 17 separate transactions (26% of total take-up). Larger lettings included Deloitte which pre-let 2,880 sq m at 3 Park Place, CNP Santander which took 1,970 sq m in the same building, Mastercard which let 2,526 in Block E in Central Park and Depfa Bank and Apex Fund Services which leased 1,830 and 1,394 sq m respectively in the Irish Life Centre.

Graph 2:
Take-Up Q1 2015 – Q1 2018 by Sector



Source: Savills Research

The amount of office space being taken by property companies has increased dramatically over the last 12 months and the real estate sector accounted for 20% of take-up in Q1 (see Graph 2). This trend has mainly been driven by serviced office providers who are meeting a market demand for business space that can be leased on flexible terms, with or without a range of bundled services.[1] Some 12,440 sq m of space was taken by flexible workspace suppliers in Q1 which will now be sub-let onwards or licenced on a desk / room basis. This is the strongest take-up recorded by such operators in the current cycle.

While numerous players are now active in this subsector, two of the largest were behind the serviced workspace lettings in Q1. Regus took 3,196 sq m at 77 Sir John Rogerson's Quay in Dublin's South

The EXO Building, Dublin 1.

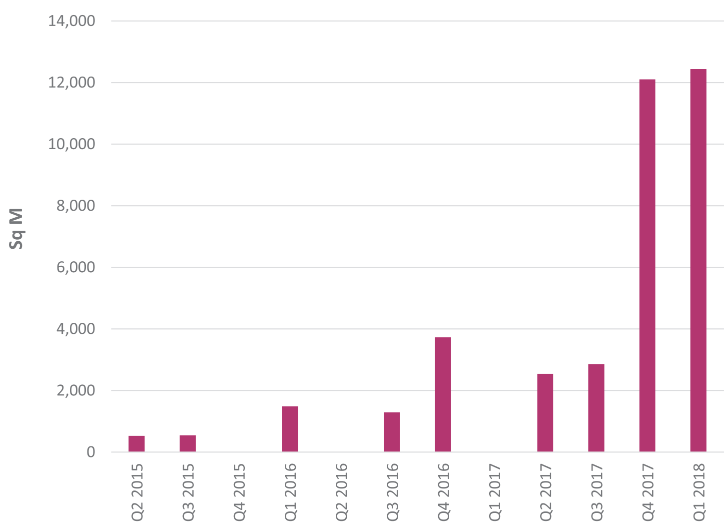
Docks while, just across the river on North Wall Quay, WeWork pre-let 9,244 sq m at Dublin Landings 2 – the largest letting of the quarter. It is interesting to note that, between them, these industry heavyweights have now secured over 24,000 sq m of purpose-built space in Dublin since the start of 2015 – 64% of the serviced workspace taken within that timeframe. Undoubtedly this proportion would drop somewhat if we included Georgian offices in our analysis as some smaller local operators specialise in this type of product. Nonetheless, given the importance of branding, marketing and global business networks in the delivery of the flexible workspace model, larger, established and well-resourced operators are likely to remain dominant as they can negotiate global cross-border desk agreements.

Take-up by location

The large Google lettings in Sandyford and Accenture's 2,450 sq m letting in Cherrywood demonstrate continued demand for larger parcels of suburban office space with good public transport links. Indeed Savills' active demand tracking system shows that a number of large suburban requirements have emerged in the early months of this year and suburban locations continue to appeal to mature, lower margin occupiers seeking a lower cost base. In this context we expect a pick-up in suburban lettings later in the year.

However Savills' active demand tracker shows that many occupiers retain a preference for city centre locations which are situated at the hub of Dublin's radial transport network and which offer access to the widest range of social, cultural and commercial amenities. Indeed, as the labour market has tightened and competition for talent has intensified, such factors are increasingly driving firms' locational decisions. Overall, 64.2% of space taken-up in Q1 was located in the Central Business District / South Docks area whereas the suburbs accounted for 30.3% (91% of which was in Dublin 18).

Graph 3:
Take-Up by Serviced Office Providers Q2 2015 - Q1 2018.



Source: Savills Research

[1] The sharp increase in demand from flexible workspace providers reflects a trend that we have already seen in London. For more detail on this and the factors that are driving demand for flexible workspace see Savills' last Dublin Offices Market in Minutes report (March 2018) - http://pdf.euro.savills.co.uk/ireland-research/market-in-minutes/northern-ireland-research/market-in-minutes--offices-q4-2017.pdf

The Hampstead Building, Carrickmines, Dublin 18.

Net Absorption

Net absorption – the change in occupied space – was 33,418 sq m in Q1. However, this figure was artificially inflated by two factors. Firstly, three occupied buildings which had been converted from industrial use were added to our stock list. This directly boosted occupied stock by 11,262 sq m in Q1 - despite the fact that the occupation of these premises as offices took place sometime previously. Secondly 6,754 sq m of space was withdrawn by landlords during the quarter. By default we remove this from available space and add it back to occupied space. However the likelihood is that it will quickly resurface as available space – perhaps with a new agent. Adjusting for these factors a net absorption figure of 15,402 sq m (33,418 – 11,262 – 6,754 sq m) is arguably more representative of the quarter.

Leaving aside such arguments, the usual positive gap was observed between gross lettings (61,699 sq m) and measured net absorption (33,418 sq m). More than half of this gap (15,943 sq m) can be explained by pre-lets; Leases were signed in Q1 2018 but, because the buildings are still under construction, the increase in occupied space can only be registered upon practical completion. This space is, however, guaranteed to be absorbed in the coming quarters. The remainder of the gap (12,338 sq m) is 'churn' – i.e. lettings were partially offset by occupiers returning vacated space to the market.

Market Supply and Vacancy

After a bumper Q4 when 73,642 sq m of new office space was finished, completions fell to 15,396 sq m in the first three months of 2018. This represents the lowest output since Q1 2016. In analysing the impact of new development on the supply / demand balance it is critical to consider not only completions but also demolitions of existing space. Some 21,080 sq m of older space was withdrawn for redevelopment Q1 making it the first quarter since Q4 2015 with negative net completions. For a given level of vacant space, the percentage vacancy rate should rise in the face of negative net completions – because this reduces the total office stock. However, in this case net absorption subtracted from the quantum of vacant space and so the vacancy rate pushed down to 8.4% in Q1 - its lowest level since 2000. As ever the vacancy rate varies by location and building quality, with rates lowest for Grade A stock in prime business districts.

Rents

Given the decline in vacancy rates it is perhaps unsurprising that the tone of rents picked-up marginally in Q1. In line with our December 2017 forecast which predicted a further modest uptick in rents this year, our view is that headline rents for prime offices in Dublin's Central Business District are now approaching €700 per sq m per annum.

The Wythe Building, Dublin 2.

North Dock, Dublin 1.

[2] The Skyline Report by Savills' office agency department will provide a very detailed analysis of the Dublin office development pipeline. It will be available at www.savills.ie later in Q2.

Outlook

Looking ahead, Ireland's economic prospects remain very favourable and there has been a slew of upgrades to macro-economic forecasts since our last report in March. The current consensus is for GDP growth of 4.7% this year and 3.8% in 2019 with jobs growth of around 50,000 and 42,000 this year and next. Undoubtedly there are risks to the Irish economy – for example Brexit, global tax reform, and the concentrated corporation tax base. Moreover, accumulating inflationary pressures in Europe mean that the prospect of monetary tightening is drawing closer. At this point in time, however, the Irish economy appears to be in very good shape and this should underpin the demand for business space over the coming quarters.

Notwithstanding the likelihood of continued solid demand, prospects for the office market also depend on the supply of additional stock. Savills' office agency team has done its own detailed analysis of the supply pipeline in the 2018 *Skyline Survey*.[2] Excluding refurbishments which do not create additional space, this year should see gross new office completions of just over 220,000 sq m. However, withdrawals of older space will significantly reduce the extent to which this raises the total office stock. Furthermore it is notable that 47% of the stock that is currently under construction is already committed. Nonetheless, net absorption is unlikely to digest all of the net additional space that is coming, meaning that the vacancy rate is likely to edge up over the remainder of 2018. Given our low starting point, however, vacancy rates will remain well below their 'natural' level of 12-15%. As such our view is that headline rent levels will hold station, or possibly tick up slightly over the reminder of the year.

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