1 *Occupier Trends* | 2 *Investment Trends* | 3 *Market Outlook*

Dublin Office Market Overview

Research, Q1 2020

With Special Focus: Impact of Covid-19

knightfrank.com/research

Summary

1. 817,000 sq ft was let in what was the second strongest opening quarter ever
2. The vacancy rate declined to 6.5%, down from 7.0% a quarter earlier
3. The TMT sector was the main driver of activity, comprising 91% of the entire space let
4. €363.9 million worth of office investments changed hands in Q1
5. Real estate markets across the globe hit by Covid-19 exogenous shock

Q1 OVERVIEW

Strong opening start to 2020 masks the severe disruption to the real estate market that is currently being caused by the outbreak of Covid-19

OCCUPIER MARKET

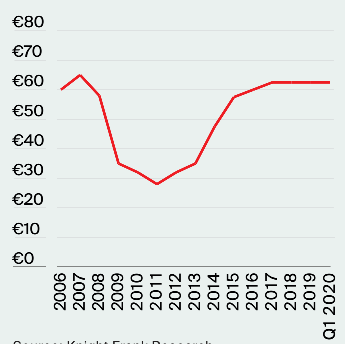
817,000 sq ft of office space transacted in Dublin in Q1 in what was the second strongest opening quarter on record, only behind Q1 last year when 1.4 million sq ft was let. The vacancy rate fell to 6.5% from 7.0% at the end of Q4 while the vacancy rate in the city centre declined to 5.0% from 5.3% previously.

Occupier activity was driven firmly by the TMT sector which accounted for 91% of the market. The largest transaction was Mastercard's taking of 249,000 sq ft at One and Two South County Business Park.

Mastercard is the epitome of the transition made by many financial companies towards the technology sector, with One and Two South County incorporating a new European Technology Hub which will develop the company's capabilities in areas such as artificial intelligence, cyber security and blockchain. The campus style development is also in tune with recent trends seen within the technology sector in Dublin with Microsoft, LinkedIn, Facebook and Google having led the way in this regard. One South County was completed last year while Two South County is a pre-letting which will be completed in 2022.

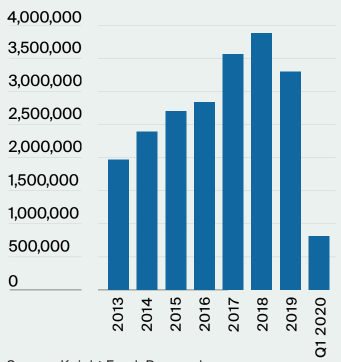
The second largest deal was Slack's pre-letting of 135,000 sq ft at Fitzwilliam 28, with delivery of the redeveloped former ESB headquarters expected later this year. Slack provides internal communication software for enterprises and, although it has been facing increasing competition from Microsoft

Fig 2. Prime office rents
€ per sq ft per annum



Source: Knight Frank Research

Fig 1. Office take-up
Sq ft



Source: Knight Frank Research

TOP 5 OFFICE LEASING TRANSACTIONS

PROPERTY	TENANT	SECTOR	SIZE (SQ FT)
One & Two South County Business Park, Dublin 18	Mastercard	TMT	249,164
Fitzwilliam 28, Dublin 2	Slack	TMT	134,656
Stemple Exchange, Blanchards-town Corporate Park, Dublin 15	Guidewire	TMT	85,000
Block I, Central Park, Dublin 18	Google	TMT	75,294
2WML, Dublin 2	Zalando	TMT	47,562

Source: Knight Frank Research

Teams over the last year, the company has the noteworthy distinction of having a higher stock price at the end of Q1 than at the start and before the Covid-19 turmoil disrupted financial markets. Other notable deals included Guidewire's taking of 85,000 sq ft at Stemple Exchange, Blanchardstown Corporate Park, Google's taking of 75,000 sq ft at Block I, Central Park and Zalando's taking of 48,000 sq ft at 2WML.

In terms of location, 42% of occupier activity occurred in the City Centre, marginally ahead of the South Suburbs on 41%. The West Suburbs and the North Suburbs accounted for 15% and 2% of the market respectively. We are holding prime benchmark rents at €62.50 psf although risks remain on the downside to this given the current environment.

DEVELOPMENT MARKET

Four projects were completed in Q1 delivering 104,000 sq ft to the market. The largest of these was Davy Real Estate's 45 Mespil Road which comprises 47,000 sq ft, followed by Block D, Charlemont Exchange which extends to 32,000 sq ft and marks the completion of the redevelopment of Charlemont Exchange which now totals 123,000 sq ft. Blocks A, B and C were completed in 2018 by Marlet – the scheme's previous owners – before being sold to Vestas Investment Management in 2019. The remaining two schemes delivered in Q1 were 61 Thomas Street and 42 Westland Row which consist of 13,000 sq ft and 11,000 sq ft respectively.

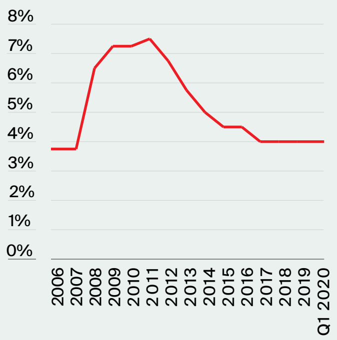
INVESTMENT MARKET

€363.9 million worth of Dublin office investments changed hands in Q1, representing a 34% increase in comparison to the same period last year. The largest transaction was Google's purchase of the Treasury Building for €115.5 million. Google has expanded its footprint in Dublin considerably such that it now stands at just over one million sq ft, and while the Treasury Building is presently leased to a number of tenants, it will eventually provide Google with additional space for its future growth in Dublin.

European purchasers targeted office assets in Dublin in a considerable way in Q1, comprising 55% of investor activity – ahead of buyers from the United States and Ireland which accounted for 32% and 8% of the market respectively. In addition, European buyers also purchased four of the five largest assets that traded during Q1. AXA IM – Real Assets, in conjunction with local partners BCP Capital, purchased La Touche House from Credit Suisse for €84.3 million. Elsewhere, Arena Invest – who made their first acquisition in Dublin in Q1 – paid €54.0 million for Blocks 4 and 5 of the Harcourt Centre which were originally acquired by Ares and Avestus for €47.0 million in 2017. Ares and Avestus also disposed of Classon House – which they purchased in 2016 for €20.4 million – to Corum for €29.3 million, while KanAm bought One Hatch Street from a private European investor for €35.1 million.

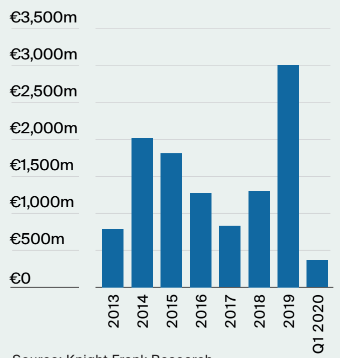
Although outside of the top five transactions, another high-profile asset to re-trade was Phoenix House which was sold to UK-based SW3 for €16.0 million, having been acquired by Henley Bartra for €8.3 million in 2018. It is noteworthy that Blocks 4 and 5 of the Harcourt Centre, Classon House and Phoenix House were all acquired and re-traded within the last four years, underlining the high liquidity of the market in recent years. While the indications in the early stages of Q1 were that yields were beginning to tighten, we now believe it is prudent to continue to hold the prime yield benchmark at 4.0%.

Fig 4. Dublin prime office yields



Source: Knight Frank Research

Fig 3. Dublin office investment volumes



Source: Knight Frank Research

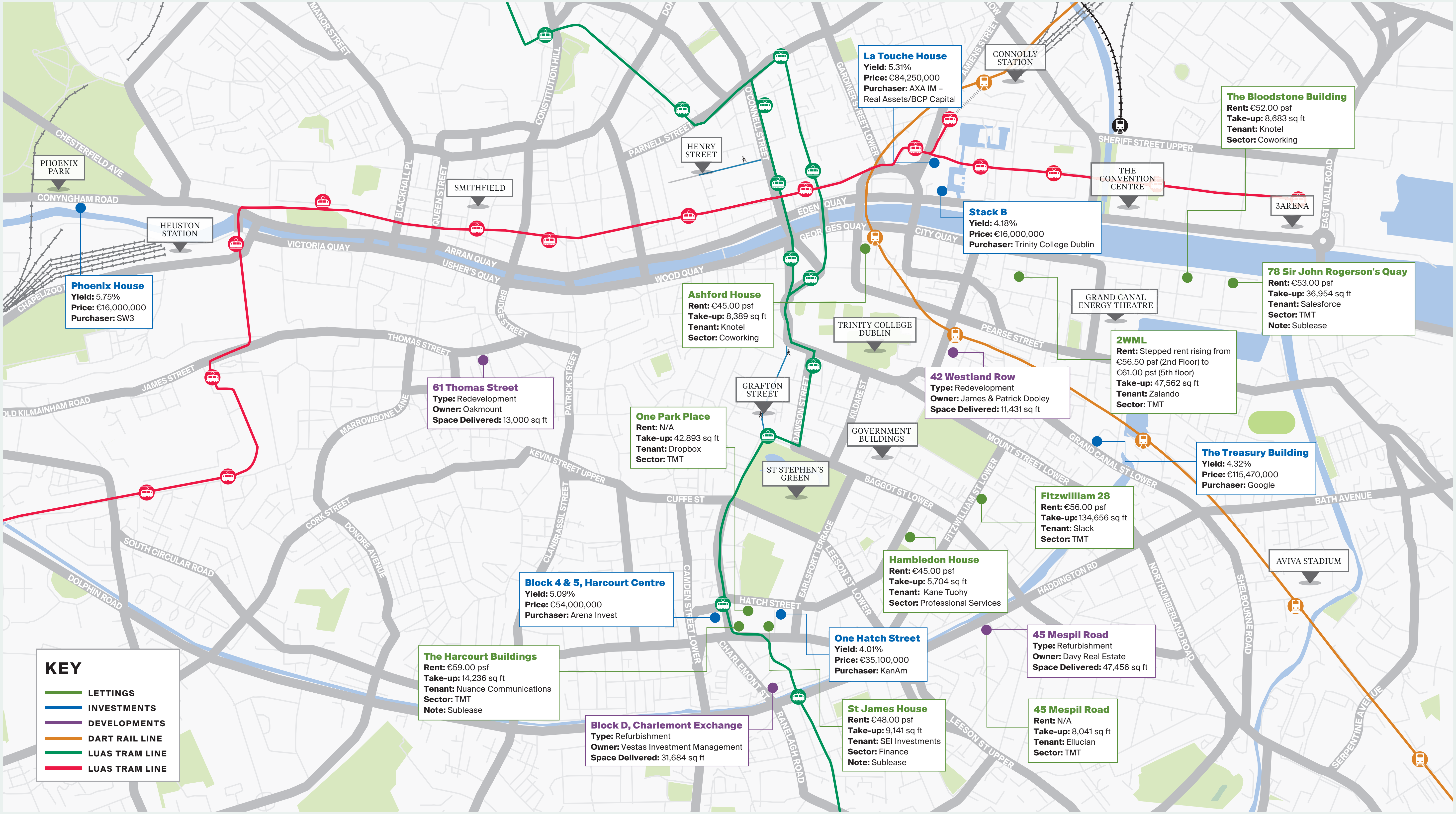
TOP 5 OFFICE INVESTMENT TRANSACTIONS

PROPERTY	SELLER	BUYER	APPROX. PRICE
The Treasury Building, Dublin 2	Jayfield Ltd and Percy Nominees	Google	€115.5m
La Touche House, Dublin 1	Credit Suisse	AXA IM - Real Assets/ BCP Capital	€84.3m
Blocks 4 & 5, Harcourt Centre, Dublin 2	Avestus/Ares	Arena Invest	€54.0m
One Hatch Street, Dublin 2	Private European	KanAm	€35.1m
Classon House, Dundrum Business Park, Dublin 14	Avestus/Ares	Corum	€29.3m

Source: Knight Frank Research

DUBLIN OFFICE MARKET OVERVIEW Q1 2020

TOP LETTINGS, INVESTMENTS AND DEVELOPMENTS IN Q1



SPECIAL FOCUS: IMPACT OF COVID-19

CONTEXT

The global spread of Covid-19 in Q1 ignited huge volatility in the world's financial markets with the CBOE Volatility Index, also known as the VIX, recording its highest ever level in March.

The Dow Jones fell by 23.2% in Q1, making it the worst quarterly performance since 1987 and the worst Q1 on record while the Irish stock market (ISEQ) fell by 28.4%. The price of crude oil fell by two thirds making it the worst ever quarterly performance with March also having the distinction of being the worst monthly performance on record. The global indirect property market was not spared, with the S&P Global REIT benchmark falling by 29.6%.

These swings in the financial environment will obviously have significant ramifications for the Dublin office occupier and investment markets. Less obvious is what those ramifications will be. Nevertheless, in this special focus, we give our initial views on what is a fast and continually evolving situation.

WHAT IS DRIVING THE VOLATILITY?

Uncertainty regarding how long economic restrictions are likely to remain in place is the key factor driving current market volatility. Currently, there is a wide range of estimates among market participants regarding how long the present lockdown will last. Without a consensus regarding a timeline back to normality, it is very hard to assess the full impact and reliably underwrite the risk associated with assets. Global volatility is likely to remain elevated for some time but will reduce as a path out of the crisis becomes clearer.

In Ireland's case, we can turn to comments made recently by Dr. Cillian De Gascun, who is the Chair of the Covid-19 Expert Advisory Group to the Health Service Executive. When asked whether twelve weeks was an optimistic timeline for the Government's COVID-19 Income Support Scheme to last, he suggested a three to six month period would be more realistic. For their part, The Central Bank of Ireland have released a provisional estimate for a 8.3% contraction in GDP in 2020, but that is predicated on containment restrictions lasting three months which is at the lower bound of the likely impact. Even under that scenario, the deficit as a percentage of GNI* will reach 10.7% in 2020.

The early stages of this crisis saw sovereign yields across Europe spike before the ECB stepped in with a €750 billion Pandemic Emergency Purchase Programme. The question of how the emergency response to Covid-19 will be paid for has not gone away however, and is a topic that is likely to come to the fore in European politics when the medical emergency wanes. This could have wider implications for the bloc's future.

IMPACT ON THE INVESTMENT MARKET

Evidence from publically traded real estate companies, both domestically and abroad, would suggest that there will be a material impact on prices in the direct property investment market. In practice, however, we are unlikely to see transactions take place until we are emerging from this crisis at which point the financial markets may be much further along the road to recovery which would insulate real estate from much of the volatility. Nevertheless, if equity prices remain significantly below where they were when we entered this crisis, we may see rebalancing activity as the large multi-asset portfolio managers seek to dispose of some their real estate holdings in order to keep their portfolio exposure at the targeted risk-return level.

However, it is worth remembering that Dublin's office investor base is extremely well diversified internationally with the resulting pooling of risk increasing the market's resilience. Much of the capital that has invested in the Dublin office sector is long-term stable income focused and well capitalised to weather short-term fluctuations in the market. While rents may be adversely affected, this is mitigated somewhat by the increasing use of capped/collar and indexed rent reviews, although the majority are still open market reviews. Furthermore, talk of late cycle investing was dominating the market and many were positioning their portfolio for end of cycle risks and taking a more defensive stance even before Covid-19 arrived.

Looking ahead, much of the stock of prime assets in Dublin have already been purchased by long-term core investors meaning competition for such assets that are brought to the market for sale will remain strong. In recent years, the main source of prime investment product has been new builds. However, with construction halted, the supply of opportunities will dwindle which will support values for standing assets. Given the pressure on corporate debt that is emerging and the importance of tenant liquidity in weathering the current uncertainty, investment grade tenants with continued access to capital markets will be especially valued. The yield spread between prime assets with long unexpired terms and riskier strategies with active management will widen further.

IMPACT ON THE OFFICE MARKET

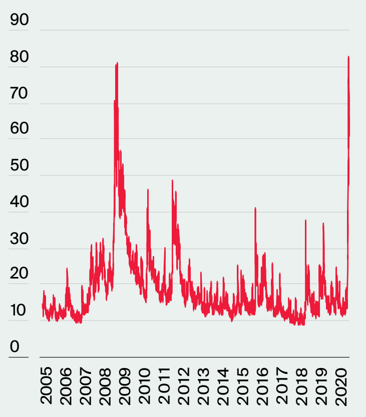
Some feel that the office sector is uniquely exposed to the Covid-19 crisis as it has turbo charged the secular trend towards remote working with detrimental consequences for the office market. Indeed, we can see in Fig. 8 the gains that remote working stocks have made in Q1, going against the overall decline seen in the S&P 500.

While we do envisage an increase in remote working, we see it complementing rather than replacing office space with employees given greater flexibility to work remotely one or two days a week. Overall, however, we believe that the current crisis has underlined the value of the office as a place of collaboration and socialisation for employers and employees. Companies have long learned that real estate is a key business infrastructure for driving productivity that more than outweighs the direct real estate cost.

We have seen predictions of technology heralding the demise of the office before. Back in the 1990's, it was predicted that the introduction of the internet and email to the work place would lead to companies moving to cheaper suburban offices as the need for face-to-face communication would be negated. However, it was discovered that the more people communicated using technology, the more they wanted to meet-up in person, which resulted in the reversion of occupier demand to city centre locations, especially from tech companies themselves.

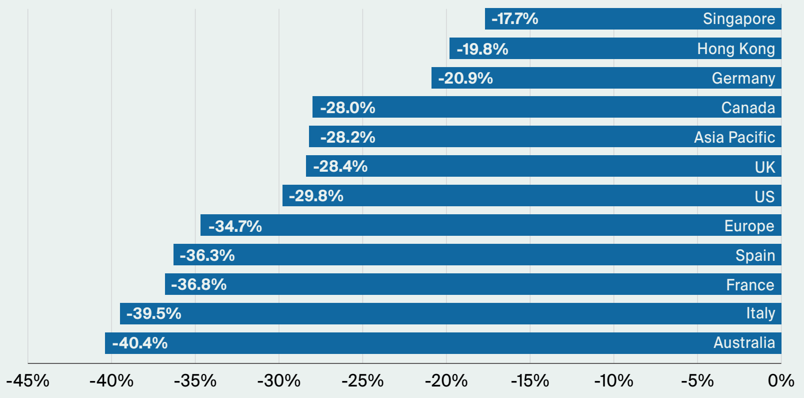
In the same way, demand for physical offices will remain despite the experiment in remote working that we are all undertaking at this time. It is also why Slack, one of the leading providers of remote working software, expanded into 135,000 sq ft of new office space at Fitzwilliam 28 in what was the second largest deal of Q1.

Fig 5. Volatility Index



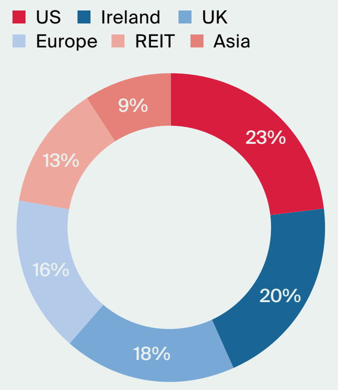
Source: CBOE Volatility Index

Fig 6. Q1 Performance of REITs globally



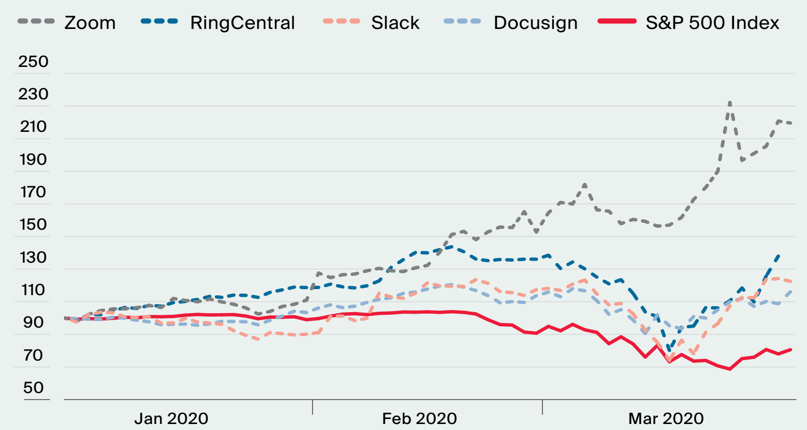
Source: Various

Fig 7. Dublin office buyers by origin 2013 - Q1 2020



Source: Knight Frank Research

Fig 8. Remote working stocks

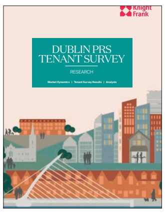


Source: S&P

Brexit Under Pressure
#3 - March 2020

The London Report
2020

The Wealth Report
2020



Dublin PRS Tenant
Survey

Please get in touch with us

Research

John Ring, Head of Research
john.ring@ie.knightfrank.com

Robert O'Connor, Research Analyst
robert.oconnor@ie.knightfrank.com

Capital Markets

Adrian Trueick, Director
adrian.trueick@ie.knightfrank.com

Peter Flanagan, Director
peter.flanagan@ie.knightfrank.com

Ross Fogarty, Director
ross.fogarty@ie.knightfrank.com

Offices

Declan O'Reilly, Director
declan.oreilly@ie.knightfrank.com

Paul Hanly, Director
paul.hanly@ie.knightfrank.com

Jim O'Reilly, Director
jim.oreilly@ie.knightfrank.com

Gavin Maguire, Associate Director
gavin.maguire@ie.knightfrank.com

Mark Headon, Associate Director
mark.headon@ie.knightfrank.com

Knight Frank Research Reports are available at knightfrank.com/research