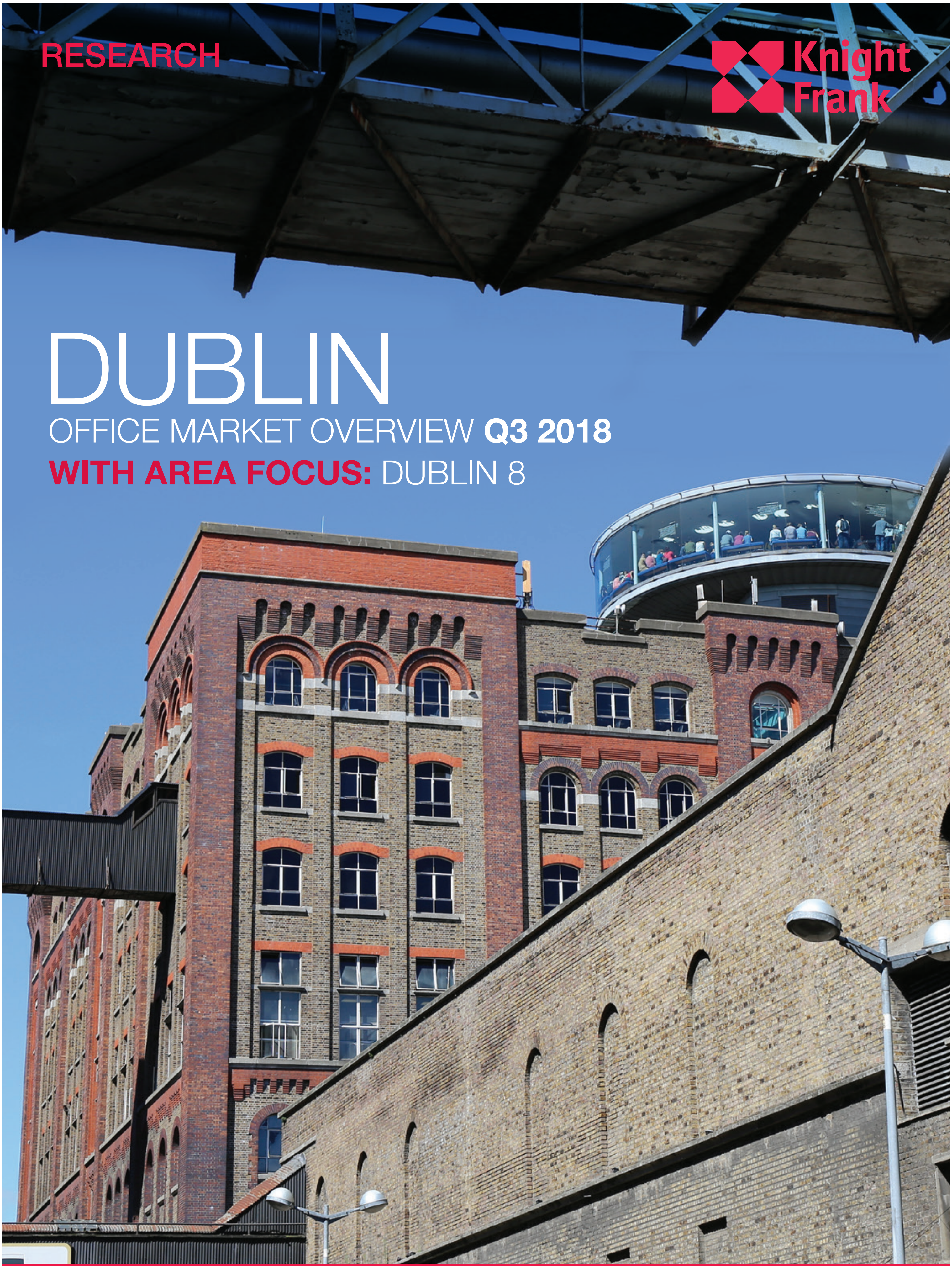
RESEARCH



DUBLIN

OFFICE MARKET OVERVIEW **Q3 2018**

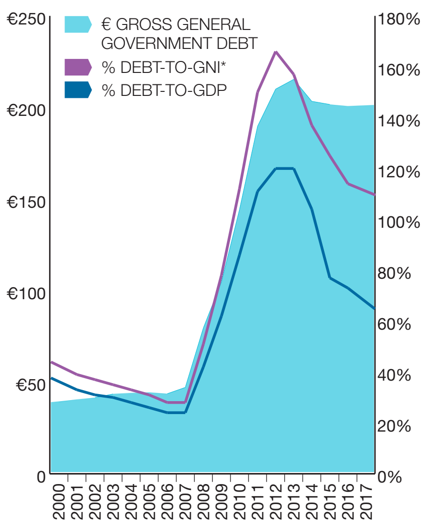
WITH AREA FOCUS: DUBLIN 8

OCCUPIER TRENDS | INVESTMENT TRENDS | MARKET OUTLOOK

SUMMARY

1. The ESRI upgraded their economic forecast for 2018 to 8.9% from 4.7%
2. 562,000 sq ft transacted in Q3, bringing take-up to 2.2 million sq ft for the first nine months of the year
3. Prime Grade-A rents stand at €62.50 psf in Q3, unchanged for the past 12 months
4. Office yields remain at 4.0%, unchanged since the end of last year
5. Dublin 8 is seeing heightened investor activity

FIGURE 1
Government debt
€Bn



Source: Knight Frank Research

Q3 OVERVIEW

Year-to-date office letting activity is 8% higher than at the same juncture in 2017.

Economy

The Irish economy continues to expand at a rapid clip. Stronger than expected domestic consumption combined with trade effects has prompted the Economic Social and Research Institute (ESRI) to revise up its 2018 GDP forecast to 8.9% in its Autumn Quarterly Economic Commentary, up from the 4.7% contained within its Summer forecast.

While GDP figures for Ireland need to be treated with a degree of caution due to the well documented distortions caused by the multinational sector, the alternative measure introduced in 2017 by the Central Statistics Office (CSO) designed to strip out these effects – Modified Gross National Income or GNI* – has illustrated broadly similar growth for the Irish economy over the last couple of years (12.3% for GNI* V 12.1% for GDP between 2016 and 2017).

The new measure was developed in response to the 2015 GDP growth figure which showed an expansion of 34.4% compared to 8.6% for GNI*, the former figure being grossly inflated by a number of one-off re-domiciliations of intellectual property to Ireland in the aircraft leasing sector. Overall, between 2013 and 2017, the economy grew by 43.3% as measured by GNI* and 67.9% as measured by GDP, with the variance between the two largely explained by the aforementioned activity in 2015.

By either reckoning, growth has been very strong and outperformed expectations. For example, in June 2012, the International Monetary Fund (IMF) forecast cumulative growth for Ireland of 22.7% between 2013 and 2017. Therefore, despite the recovery being much stronger than anticipated, it is worrying that the Government is still due to run a budget deficit in 2019 as a result of expansionary measures contained within the recent Budget. While Government policy following the crisis had been successful in introducing measures that reduced the country's high level of Government debt, progress has stalled since 2016 as a degree of complacency appears to have set in.

By threatening macroeconomic stability in the event of an economic downturn, persistent high levels of Government debt is the number one risk to the real estate market at this moment. With the IMF recently downgrading its global growth forecast for the first time in two years due to 'dangerous undercurrents', the emerging complacency regarding the elevated government debt position at this juncture is a cause for concern.

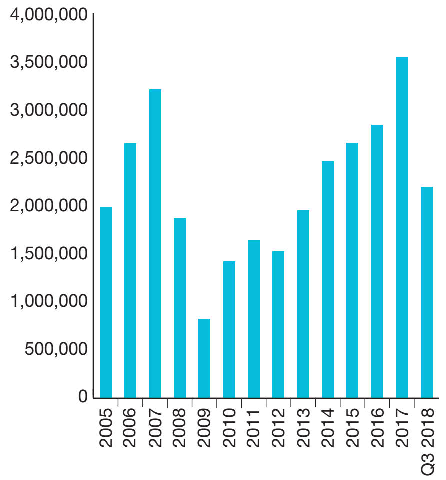
KNIGHT FRANK VIEW ON RISK

Figures released by the Irish Venture Capital Association have shown a sharp decline in venture capital funding to tech firms in the first half of the year. The analysis shows that venture capital funding fell by 9% in the first half of the year to €453 million but that Q2 volumes were down over 50% to €121 million, down from €252 million the previous year. While venture capital funding has expanded greatly over the last number of years, the organisation said that the figures bear out a softening in start-up funding which has been felt since the start of the year but masked in Q1 due to a couple of large deals transacting. The number of deals taking place in the first six months declined from 141 to 89 while very early stage seed funding fell by 37% in the first half of the year. Although the importance of the large tech firms to the Dublin office market is well publicised, the presence of a start-up community is vital in developing a vibrant tech ecosystem in Dublin. It remains to be seen whether this fall in funding is a temporary lull in activity or signals the start of a more serious tightening in an important sector to the city's economy.

Occupier market

Just over 562,000 sq ft transacted in Q3 which represents a 47% increase in comparison to the same quarter last year. This brings the year-to-date take-up to 2.2 million sq ft, 8% ahead of the same point of the record breaking 2017. The City Centre dominated letting activity, accounting for 53% of all transactions. Take-up in the City Centre was driven by the strong performance of Dublin 2, which comprised 40% of occupier activity and included the largest deal of Q3 which saw Google take 58,000 sq ft at One Grand Canal Quay. Dublin 2 also accounted for the third largest transaction of Q3 with biopharmaceutical company Biomarin taking 25,863 sq ft at 5 Earlsfort Terrace, which is currently being refurbished by IPUT.

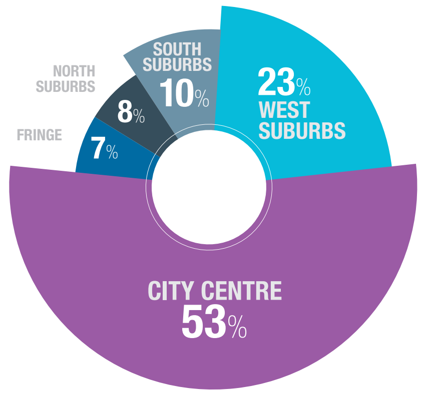
FIGURE 2
Office take-up sq ft



Source: Knight Frank Research

Interestingly, there were also a number of lettings that took place in the City Centre that are believed to be Brexit related. Following on from their announcement last year that it would be establishing a presence in Dublin, Simmons and Simmons will take 5,306 sq ft at Esprit's Waterways House. They will be joined by Standard & Poors who are taking 4,967 sq ft at the same development – a move designed to ensure that the company continues to meet European Union regulations for rating agencies after Brexit. Finally, insurance group Royal London and financial services firm DTCC were among the other Brexit related moves, occupying 2,097 sq ft at 4 Earlsfort Terrace and 1,413 at 23 Shelbourne Road respectively.

FIGURE 3
Take-up by location

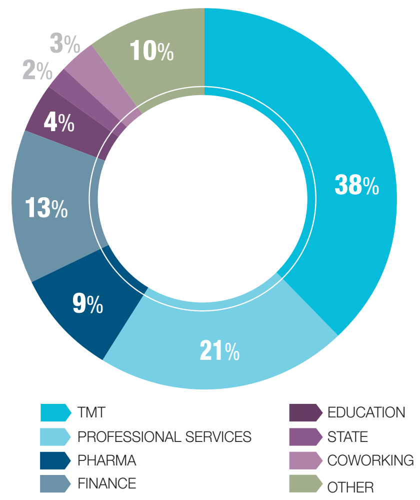


Source: Knight Frank Research

The West Suburbs accounted for 23% of take-up, significantly surpassing its 5-year average of 8%. Take-up in the West Suburbs was boosted by DPS Group's taking of 22,480 sq ft at 3096 Lake Drive, Citywest Business Campus. In the South Suburbs, PLR Worldwide Sales took 17,562 sq ft at Red Oak in the South County Business Park with the area accounting for 10% of letting activity, while the North Suburbs comprised 8% of the market with its share supported by the second largest transaction of Q3 which saw Kellogg's become the first tenant at Three Dublin Airport Central. The company is taking 39,008 sq ft – a move that will see them relocate from their current location at the Airside Business Park.

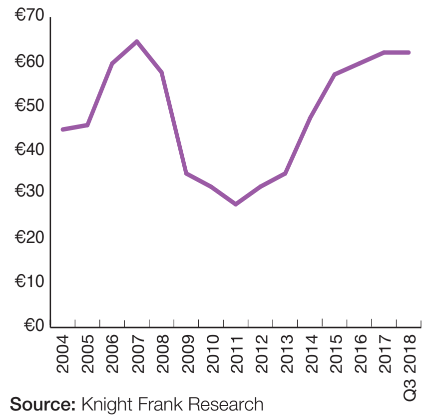
The Fringe market comprised the remaining share of take-up with 7%. Looking at a sectoral view of the market, TMT dominated occupier activity with 38% of deals. This was followed by the Professional Services and Finance sectors which accounted for 21% and 13% respectively. Prime rents remain stable at €62.50 psf, representing 12 months unchanged at this level.

FIGURE 4
Take-up by sector



Source: Knight Frank Research

FIGURE 5
Dublin prime office rents
€ per sq ft per annum



Source: Knight Frank Research

Top 5 office leasing transactions

Property	Tenant	Sector	Size (sq ft)
One Grand Canal Quay, Dublin 2	Google	TMT	58,000
Three Dublin Airport Central, Co. Dublin	Kellogg's	Other	39,008
5 Earlsfort Terrace, Dublin 2	Biomarin	Pharma	25,863
3096 Lake Drive, Citywest, Dublin 24	DPS Group	Professional Services	22,480
Red Oak, South County Business Park, Dublin 18	PLR Worldwide Sales	TMT	17,562

Source: Knight Frank Research

DUBLIN 8

OFFICE LETTINGS

1. The Brunel Building
Date: Q2 2018
Rent: €35.00 psf
Take-up: 31,225 sq ft
Tenant: HSE
Note: *Lease assignment with three years remaining*

2. 140 Thomas Street
Date: Q2 2018
Rent: €40.00 psf
Take-up: 5,974 sq ft
Tenant: Tibco

3. Fumbally Square
Date: Q3 2018
Rent: €42.50 psf
Take-up: 10,370 sq ft
Tenant: VSware

4. 31-36 Golden Lane
Date: Q2 2017
Rent: €47.00 psf
Take-up: 31,000 sq ft
Tenant: New Relic

OFFICE INVESTMENTS

1. 1 & 2 HSQ
Date: Q1 2018
Price: €176,000,000
Capital value: €806 psf
Initial yield: 4.9%
Buyer: CK Properties Ltd

2. Fumbally Estate
Date: Q3 2018
Price: €33,500,000
Capital value: €400 psf
Initial yield: 5.7%
Buyer: BCP Asset Management
Note: *Includes four residential units and a development site*

3. 1-3 High Street
Date: Q3 2018
Price: €5,850,000
Capital value: €408 psf
Initial yield: 3.9%
Buyer: Private Irish

4. The Chancery
Date: Q4 2017
Price: €23,800,000
Capital value: €689 psf
Initial yield: 5.8%
Buyer: Credit Suisse

5. 31-36 Golden Lane
Date: Q2 2018
Price: €25,500,000
Capital value: €823 psf
Initial yield: 5.3%
Buyer: KGAL

6. Adelaide Chambers
Date: Q2 2018
Price: €7,230,000
Capital value: €398 psf
Initial yield: 2.9%
Buyer: Chartered Land

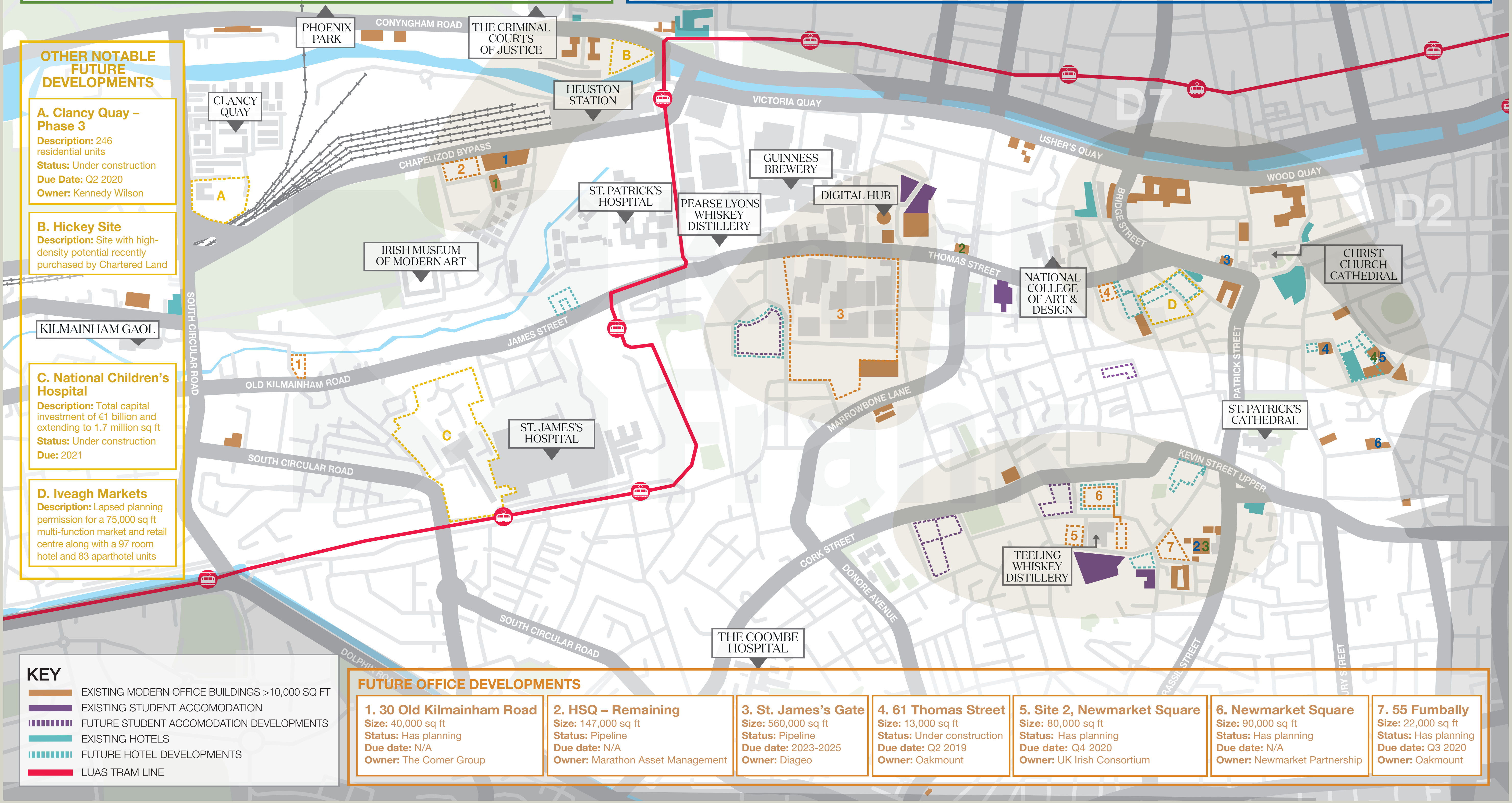
OTHER NOTABLE FUTURE DEVELOPMENTS

A. Clancy Quay – Phase 3
Description: 246 residential units
Status: Under construction
Due Date: Q2 2020
Owner: Kennedy Wilson

B. Hickey Site
Description: Site with high-density potential recently purchased by Chartered Land

C. National Children's Hospital
Description: Total capital investment of €1 billion and extending to 1.7 million sq ft
Status: Under construction
Due: 2021

D. Iveagh Markets
Description: Lapsed planning permission for a 75,000 sq ft multi-function market and retail centre along with a 97 room hotel and 83 aparthotel units



KEY

- EXISTING MODERN OFFICE BUILDINGS >10,000 SQ FT
- EXISTING STUDENT ACCOMODATION
- FUTURE STUDENT ACCOMODATION DEVELOPMENTS
- EXISTING HOTELS
- FUTURE HOTEL DEVELOPMENTS
- LUAS TRAM LINE

FUTURE OFFICE DEVELOPMENTS

1. 30 Old Kilmainham Road
Size: 40,000 sq ft
Status: Has planning
Due date: N/A
Owner: The Comer Group

2. HSQ – Remaining
Size: 147,000 sq ft
Status: Pipeline
Due date: N/A
Owner: Marathon Asset Management

3. St. James's Gate
Size: 560,000 sq ft
Status: Pipeline
Due date: 2023-2025
Owner: Diageo

4. 61 Thomas Street
Size: 13,000 sq ft
Status: Under construction
Due date: Q2 2019
Owner: Oakmount

5. Site 2, Newmarket Square
Size: 80,000 sq ft
Status: Has planning
Due date: Q4 2020
Owner: UK Irish Consortium

6. Newmarket Square
Size: 90,000 sq ft
Status: Has planning
Due date: N/A
Owner: Newmarket Partnership

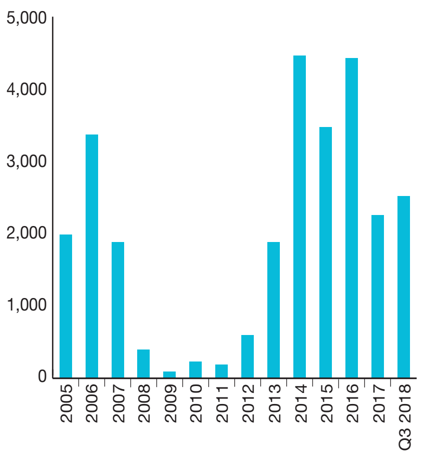
7. 55 Fumbally
Size: 22,000 sq ft
Status: Has planning
Due date: Q3 2020
Owner: Oakmount

Note: All areas and delivery times noted above are approximate estimates only and subject to change.

Development market

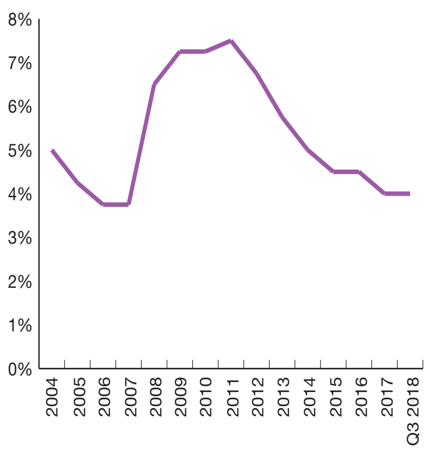
550,000 sq ft of new office space was brought to the market in Q3 as a number of new office buildings reached practical completion. The largest of these was the Seamark Building at Elmpark Green which comprises 182,500 sq ft and was developed as a joint venture by Starwood Capital Group and Chartered Land. Elsewhere, 117,757 sq ft was delivered at 13-18 City Quay, a scheme pre-let to Grant Thornton and forward funded by Irish Life. Also located on the South Quays, IPUT were granted planning permission for a 75,000 sq ft office scheme at the former Tropical Fruit Warehouse at 30-32 Sir John Rogerson's Quay. Finally, Marlet were granted approval to demolish College House where they will be constructing a new 157,600 sq ft office scheme.

FIGURE 6
Irish commercial investment volumes € million



Source: Knight Frank Research

FIGURE 7
Dublin prime office yields



Source: Knight Frank Research

Investment

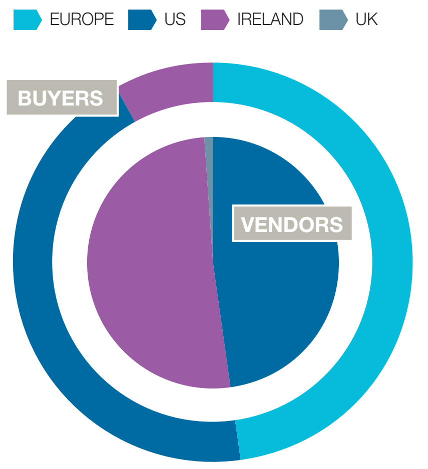
€631.0 million worth of investment transactions changed hands in Q3. This represents an increase of 19% in comparison to the same quarter last year. The year-to-date spend of €2.5 billion is almost double the amount that transacted during the corresponding period in 2017 when €1.3 billion transacted. Of the Q3 figure, the office sector accounted for 42% or €266.9 million. Dublin remains the primary destination for this activity with a market share of 97% or €259.6 million.

Investment activity was focused on the City Centre with 47% of transactions occurring in this location. In the IFSC, Hibernia REIT sold the Bank of Ireland tenanted New Century House – which was its first office acquisition following the initial public offering in 2013 – to Credit Suisse for €65.3 million, with the deal representing a net initial yield of 4.0%. Credit Suisse also purchased the Sharp Building for €56.3 million from The McGarrell Reilly Group for a net initial yield of 4.4%. Both of these transactions ensured that European investors were the most active source of capital in Dublin comprising 48% of transactions in Q3.

The Fringe market accounted for 37% of investment deals in the capital, supported by the largest transaction of Q3 which was the sale of the Belfield Office Campus to US investors Spear Street Capital for €90.0 million. The transaction represents another substantial purchase for Spear Street Capital following its acquisition of the Cherrywood Business Park last year for €145.0 million. The deal ensured that US buyers accounted for 44% of investor activity in the Dublin office market with Irish buyers comprising the remaining share with 8%.

While the suburbs comprised only 16% of the market, there were a number of notable suburban transactions. This included the PayPal occupied buildings at Ballycoolin Business Park in Dublin 15, which sold for €22.1 million at a net initial yield of 9.1%. Meanwhile, the Intreo tenanted Ninth Lock Road in Clondalkin sold for €5.9 million with the deal representing a net initial yield of 5.1%. Prime office yields in Dublin remain stable at 4.0%.

FIGURE 8
Dublin office buyer and vendor source



Source: Knight Frank Research

Top 5 office investment transactions

Property	Seller	Buyer	Approx. price
The Belfield Office Campus, Dublin 4	Colony Capital	Spear Street Capital	€90.0m
New Century House, IFSC, Dublin 1	Hibernia REIT	Credit Suisse	€65.3m
The Sharp Building, Dublin 2	The McGarrell Reilly Group	Credit Suisse	€56.3m
Buildings 2-5, Ballycoolin Business Park, Dublin 15	Xerox	Confidential	€22.1m
Ninth Lock Road, Clondalkin, Dublin 22	Varde	Private Irish	€5.9m

Source: Knight Frank Research

AREA FOCUS: DUBLIN 8

It is hard to argue with the assessment that Dublin 8 has underperformed as an office location. Despite its central location adjoining Dublin 2, it has remained a fringe office location accounting for just 2.7% of total take-up between 2013 and 2017. However, there are signs that the area's fortunes are changing. In this Area Focus, we examine the dynamics at play in this sub-market and evaluate its prospects for future growth as an office location.

REGENERATION STORY

While having a rich historical heritage dating back a thousand years to the very foundation of Dublin near Christchurch, Dublin 8's evolution in the 20th Century saw it become characterised as an area of low density working class housing and heavy industry.

Times are changing however. As illustrated in the map, there are a number of ongoing regeneration projects across a range of uses that are helping to revitalise Dublin 8. In particular, regeneration is being driven by the forces of housing and tourism:

Housing: Government led regeneration projects of old 1950's built residential flat complexes (Fatima Mansions, Dolphin House and St Teresa's Gardens) have helped address social problems in the area. This, combined with its proximity to the city centre, is seeing young professionals move to Dublin 8, a trend facilitated by the significant delivery of PRS in the area. Clancy Quay is one of the largest such complexes in Ireland, while lands near the Coombe Hospital have the potential to deliver 1,000 new residential units, of which a substantial portion will also be PRS. Finally, Dublin 8 has also emerged as an area of key importance for student housing development, with 1,430 beds delivered over the last two years and a further 2,040 in the pipeline, of which 887 are under construction.

Tourism: While Dublin 8 has always had a strong tourism offering – Kilmainham Gaol, the Irish Museum of Modern Art, the Guinness Storehouse – visitors to Dublin 8 have tended to limit their visits to the main attractions and not strayed to explore the wider area. However, the opening of three new whiskey distilleries is designed to capitalise on the area's brewery/distillery theme, and give tourists cause to linger longer in Dublin 8. This tourism factor is being supported by the opening of new hotel rooms, with 2,594 rooms in the pipeline, of which 725 are under construction. This will add considerable capacity to the current stock of 1,070 rooms, which includes the 137 rooms recently opened at the Maldron on Kevin Street.

This regeneration is supported by an accommodative public policy stance, with Dublin City Council locating six of its 18 'Strategic Development and Regeneration Areas' in Dublin 8, the highest of any postcode. Meanwhile, the Government's decision to locate the new €1 billion National Children's Hospital next to the existing St. James's Hospital will double the number of workers on campus. With two other existing hospitals in close proximity, the area has the potential to become a medical innovation hub.

Strategic Development and Regeneration Areas in Dublin 8

Heuston and Environs
St. Michael's Estate
St. Teresa's Gardens and Environs
Dolphin House
St. James's Hospital Campus and Environs
Liberties and Newmarket Square

Source: The Dublin City Development Plan (2016-2022)

DUBLIN 8 AS AN OFFICE LOCATION

Dublin 8 is a large postcode and, as the zones of activity make clear in the map, there are four areas of interest from an office perspective:

Overflow from Dublin 2: Due to its location on the edges of Dublin 2, the area along Golden Lane and Christchurch is benefiting from spillovers in occupier demand from the city core. The most significant letting in Dublin 8 in the recent past occurred here, with New Relic taking 31,000 sq ft at 31-36 Golden Lane for €47.00 psf in Q2 2017. The letting represented the successful execution of a value-add strategy by Mm Capital who acquired the building in Q2 2017 before refurbishing, letting and then disposing it to German Investors KGAL for €25.5 million, representing a net initial yield of 5.3%. Nearby, Credit Suisse paid €23.8 million for The Chancery in Q4 2017, representing a net initial yield of 5.8%. Oakmount's 61 Thomas Street is the only new delivery of office stock due next year in Dublin 8, with the quoting rent of €45.00 psf representing a significant discount on prime headline rents in Dublin 2 of €62.50 psf.

Newmarket and Fumbally: Few areas of Dublin are witnessing such concentrated and rapid development across a mix of uses, with tourist, student housing, hotel and office developments all taking place in close proximity. In terms of the latter, 170,000 sq ft of office space is due to come on stream at Newmarket Square with a further 22,000 sq ft due at nearby 55 Fumbally. The Fumbally Estate is the main standing office asset and was recently sold for €33.5 million by M7 Real Estate to BCP Asset Management, representing a net initial yield of 5.7%. The Fumbally Estate was purchased by M7 Real Estate in Q1 2017 for €21.5 million for a net initial yield of 7.9%.

Heuston: The area around Heuston Station is of key importance in planning terms, and one of only four areas of the city designated for a height cluster (along with the Docklands, Connolly and Georges Quay). This is reflective of the Council's view that developing an eastwest commercial axis along the Liffey is crucial to act as a counter weight to the Docklands. Recent deals include the HSE taking an assignment of 31,225 sq ft at the Brunel Building for €35.00 psf, with three years remaining on the lease. 1 HSQ is currently on the market for sub-lease/assignment by Eir for a rent of €40.00 psf, while 2 HSQ is believed to be reserved. 1+2 HSQ were purchased in Q1 by CK Properties for €176.0 million, representing the third largest office deal ever in the Dublin market. Other activity includes Chartered Land's purchase of the landmark Hickey site which has the capacity for a large mixed-use scheme.

St. James's Gate: This mixed-use development has the potential to be a game changer for Dublin 8. With an estimated delivery of up to 560,000 sq ft of office space slated from 2023, the site will bring critical mass and scalability to Dublin 8, enabling it to compete with more established office locations in Dublin by becoming an occupier location in its own right. It is expected that the project's historic setting in the home of one of the world's iconic brands will ensure that occupier demand will be very strong from the tech industry, helping to realise the original ambitions for the Digital Hub. The site's critical location in the heart of Dublin 8 will also play a key role in helping to link-up the currently disparate parts of Dublin 8 by bringing HSQ closer to the Digital Hub and Newmarket/Fumbally.

CONCLUDING REMARKS

While Dublin 8's vacancy rate is currently at 7.1%, it drops to 3.6% when one excludes the 56,000 sq ft under reserve at 2 HSQ. That a building of modest size has such a large impact on the vacancy rate illustrates that the office market in Dublin 8 is very thinly spread. By having the potential to expand Dublin 8's office stock by a third in one location, it also illustrates the important role that the St. James's Gate scheme will have in deepening the Dublin 8 market and tying together its currently disparate parts. While the lack of stock is holding take-up levels back, investors are clearly bullish on Dublin 8's future prospects as evidenced by the variety of investment funds deploying capital across a range of uses in the postcode.

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