Q1 DUBLIN OFFICE MARKET 2023

BNP PARIBAS
REAL ESTATE

Q1 2023 KEY TRENDS

26,523 SQ M taken in a quiet Q1	**44 TRANSACTIONS** but no deals >5,000 sq m for 1st time since Q3 2021
Tech share **RECOVERED TO 42%** (from 11% in Q4)	Financial Services remained **STRONG AT 21%** (slightly down on 2022 average)
CONTINUED RISE IN SUB-LETTING 'Grey space' accounted for 36% of take-up	**c. 30,000 SQ M COMPLETED IN Q1** partially offset by decommissioned space
VACANCY EDGED UP from 12.4% to 12.6%	Prime headline rents unchanged at **€673 PER SQ.M.**
NOMINAL GROWTH SOFTENED from 8.7% y/y to 7.9% due to base effect	**REAL GROWTH IN PRIME RENTS MARGINALLY POSITIVE** but likely to turn negative as base effect becomes more challenging

RISING VACANCY REFLECTED IN SHORTENING LEASES
earlier breaks and increased rent frees relative to lease terms

MARKET ACTIVITY

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Office leasing is a winter sport. Incentives to close deals within the calendar year generally give rise to strong activity in Q4 and, reflecting this, 36% of the office space that has been taken-up in Dublin since 2014 was signed-for in the final three months of the year. Q1 usually benefits from the slipstream of this, catching deals that miss the year-end cut. Over the long run it has accounted for approximately 25% of take-up.

Given this context, Q1 2023 was unusually quiet, with just over 26,500 sq m of space leased – a 41% drop year-on-year. However this was not unexpected – our last report highlighted the strong correlation between take-up in the current period and the amount of space that was reserved one quarter previously. In that context we flagged a 25% drop in reserved accommodation between Q3 and Q4 2022 and warned that this was likely to drag on leasing activity in the new year.

26,500 sq m

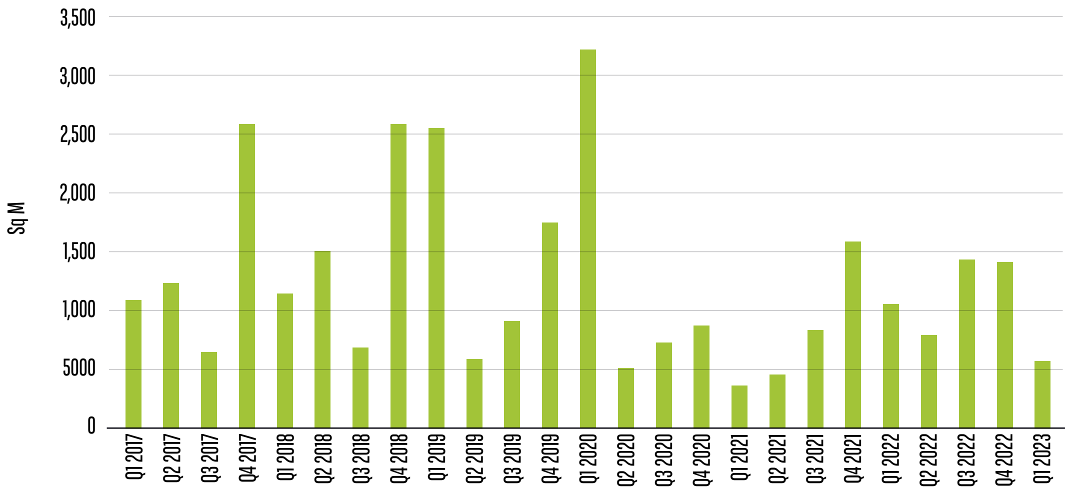
TAKEN-UP IN DUBLIN IN **Q1**

FIGURE 1: DUBLIN OFFICE MARKET TAKE-UP

Source: BNPPRE

Despite a sharp decline in the quantum of leased space, 44 deals were done in the quarter, two more than in Q1 2022. The logical corollary of this is that the average deal size plummeted from 1,074 sq m in the opening period of 2022 to just 603 sq m a year later.

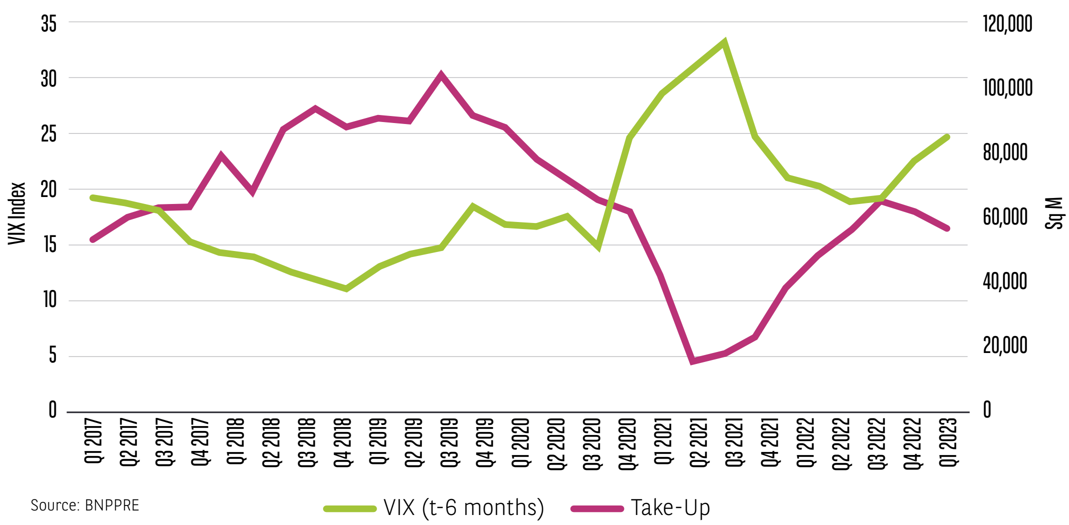
FIGURE 2: AVERAGE LEASING TRANSACTION SIZE



Source: BNPPRE

This is also as expected. Aggressive monetary tightening has disrupted the global economy over the last year. Previous periods of economic volatility, as illustrated by the VIX Index in Figure 3, triggered many multinationals to temporarily pause their leasing activities in Dublin. This left a residual of domestic occupiers with smaller business space requirements, suppressing the average deal size. There is good reason to believe this dynamic is in-play once again. However the extent to which the average deal size recovers once volatility abates may be dampened by hybrid working. Going forward even large global organisations may seek to reduce their space-per-employee ratios due to their staff spending fewer days in the office – although there is a possible offset in terms of increased collaboration space.

FIGURE 3: US STOCK MARKET VOLATILITY AND DUBLIN OFFICE TAKE-UP[1]



Source: BNPPRE

[1] The VIX Index measures expected price fluctuations of S&P 500 options over the following 30 days. It is a widely used metric for gauging market anxiety. Both series in Figure 3 are smoothed using a 4 quarter moving average for a visually clearer graph.

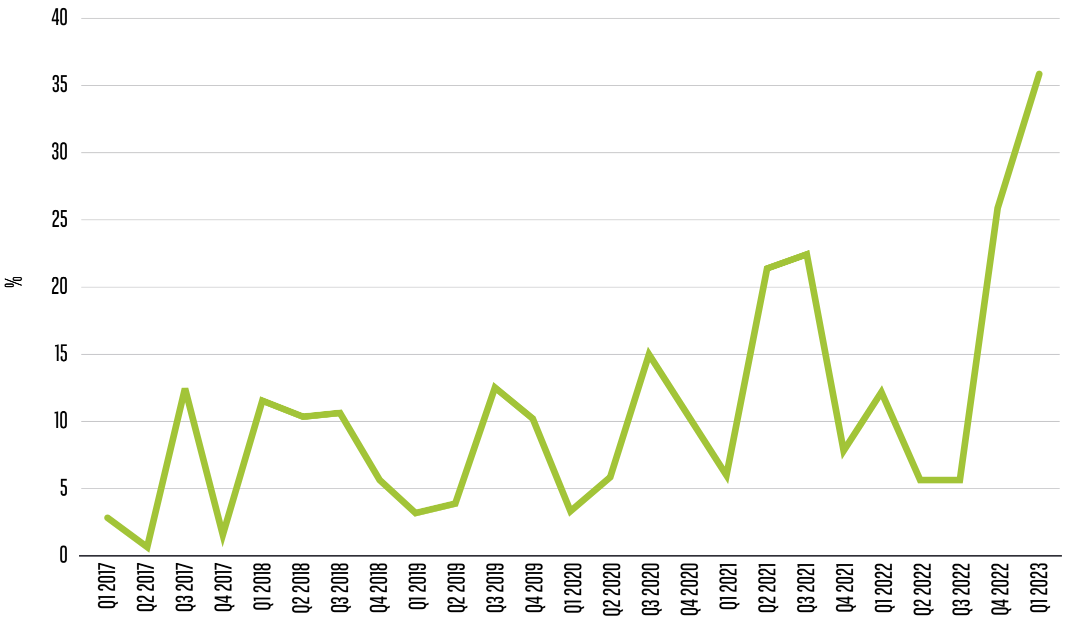
Given relatively thin trading activity one should not read too much into the sectoral distribution of Q1 lettings. However there was a notable rebound in the Tech share of take-up from 10.6% in Q4 to 42.2% in Q1. This may reflect the fact that Ireland's Tech industry has so far escaped the brunt of global headcount retrenchment – the latest monthly estimates suggest that ICT employment in January was just 1,600 lower than at its peak last August.

Profit and loss accounts in the banking sector generally benefit from a higher interest rate environment and there was a sharp rise in the share of office take-up accounted for by financial services organisations in 2022. This has continued with these firms taking 21% of the leased space in Q1 2023. However, this only represents 5,476 sq m in absolute terms and it remains to be seen what impact, if any, recent banking failures in America and Switzerland might have on leasing patterns in Dublin.

GREY SPACE

At a global level, cyclical factors and the increase in hybrid working have left some occupiers with surplus business space. In markets where shorter lease terms are the norm these occupiers have been able to quickly 'right-size' as leases expire. This has caused vacancy to pick-up sharply in some US markets, for example. In the Anglo Saxon world, where lease contracts are longer, 'right-sizing' is being achieved by tenants sub-letting or assigning their surplus space. Particularly where this sub-let space is already fitted-out, and/or available on flexible terms, it can be appealing to occupiers. As shown in Figure 4, the share of take-up accounted for by sub-leased and assigned space continued to rise sharply in Q1, accounting for 10 of the 44 deals done in Q1 and 36% of the space taken.

FIGURE 4: SUB-LEASED / ASSIGNED SHARE OF TAKE-UP



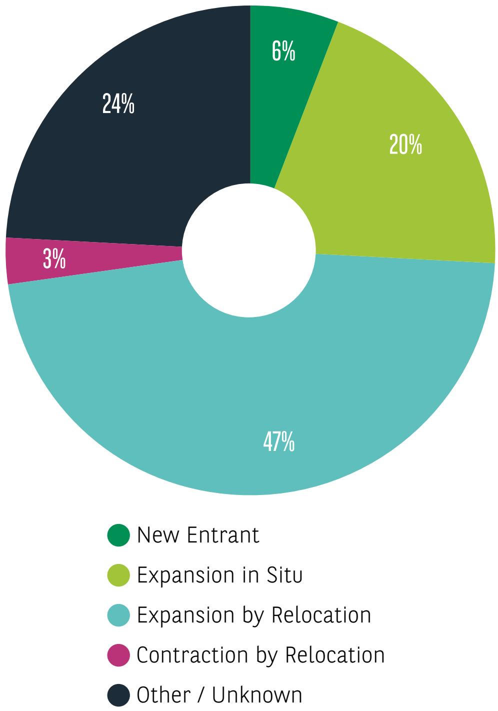
Source: BNPPRE

While the process is less direct, and may therefore take longer to percolate through, subleasing also eventually feeds into rising vacancy. Notwithstanding the fact that tenant offered space is technically not vacant (because it is leased and generating rental income), it competes with vacant landlord marketed space, slowing the rate at which that accommodation is absorbed.

NEW ENTRANTS, EXPANSIONS AND CONTRACTIONS

The rate at which take-up passes-through to net absorption typically weakens in a slowing economy. This is because new entrants and expansions tend to have a lower weighting within the transactional mix. Figure 5 shows that just over one quarter of leased space in Q1 was taken by new entrants and tenants expanding in their current locations. Logically, in such transactions, there should be a 1:1 relationship between the amount of space leased and the amount of space absorbed. A further 47% of space was taken by tenants expanding by relocation. This is also a driver of absorption, but to a lesser extent as the resulting increase in occupied space is partially offset by the handing back of vacated accommodation. Meanwhile, only 3% of the space taken was by occupiers moving to smaller premises. These deals result in negative absorption.

FIGURE 5: BREAKDOWN OF Q1 TAKE-UP BY TENANT ACTIVITY



SUPPLY AND VACANCY

Approximately 30,000 sq m of new space reached practical completion in Q1. However, the net increase in stock was considerably less due to demolitions (most notably the deletion of the former Garda headquarters at Harcourt Square). Nonetheless, as the rise in total stock exceeded net absorption in a quiet quarter for leasing, the vacancy rate edged-up from 12.4% to 12.6%.

RENTS AND LEASE TERMS

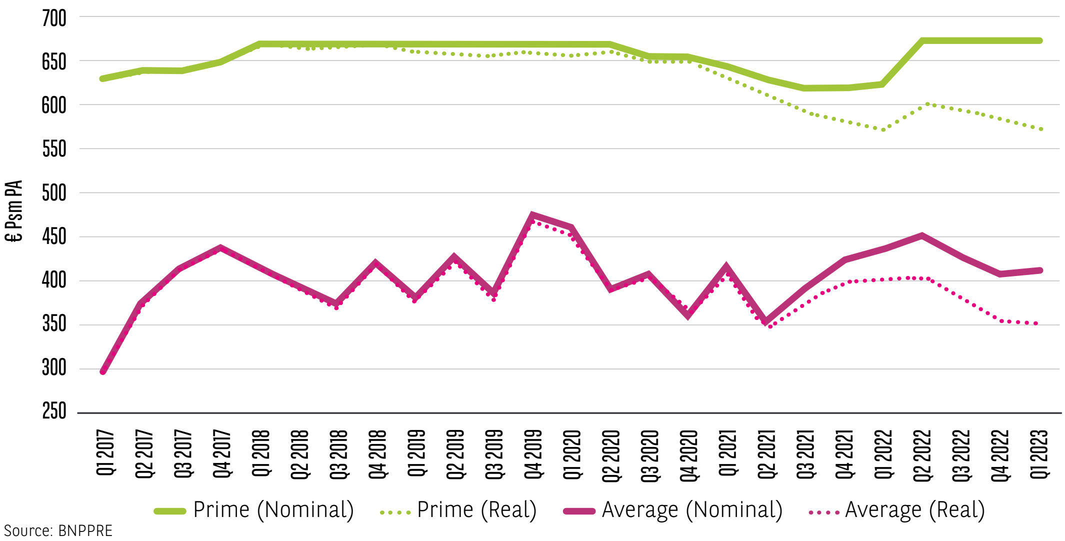
Reflecting their ESG commitments, global occupiers remain heavily focused on modern, low carbon offices in prime city centre and docklands locations.[2] As these buildings remain scarce, prime headline rents held up at €673 per sq m per annum in Q1 2022. Due to a significant uplift between Q1 and Q2 last year, this still represents an annual growth rate of 7.9% in nominal terms.

While this remains a positive story there are some important caveats. With generalised inflation running at 7.7% per annum, the real increase in prime office rents is barely positive at 0.17% per annum. In addition, the effect of rising vacancy is evident in the 'soft indicators'. Average lease terms in the city centre market have shortened considerably since mid-2022 and, understandably in that context, earlier break options have also become available.

While the prime headline rent is a well understood benchmark, it relates to a specific part of the market and does not necessarily capture the overarching trend across a full spectrum of transactions. The average rent on new lettings is a simple measure which captures a wider sweep of deals, and it fell by 5.6% (nominal) and 12.3% (real) in the year to Q1 (Figure 6). Due to potential mix effects we must be cautious about relying too heavily on a simple average, particularly in light trading. But the trend in this measure does reflect what agents are witnessing at the coalface.

[2] 62.3% of office space that has been taken-up between Q1 2022 and Q1 2022 had a BER rating of B3 or better.

FIGURE 6: HEADLINE RENTS, NOMINAL AND REAL (Q1 2017 PRICES)



Source: BNPPRE

OUTLOOK

Monetary authorities' war against inflation will continue for some time. Reflecting this, the global and Irish economies are expected to grow more slowly than in 2022. However market expectations around terminal interest rates have reduced somewhat. As such, forecasters have recently raised their 2023 growth projections for the Irish economy.[3] This should continue to provide a supportive environment for the Dublin office market. Moreover, with the amount of reserved space rising by 14% in Q1, there is reason to expect some near-term pick-up in leasing activity. Having regard to this, and active requirements in the market, we are tentatively pencilling a full year take-up forecast of 180,000 sq m - a potential 27% reduction compared with 2022.

With a possible 190,000 sq m of further space to be delivered before year-end, and considering the continued influence of subleasing and 'churn' on absorption rates, this means the overall vacancy rate will likely edge towards 15% by year-end.

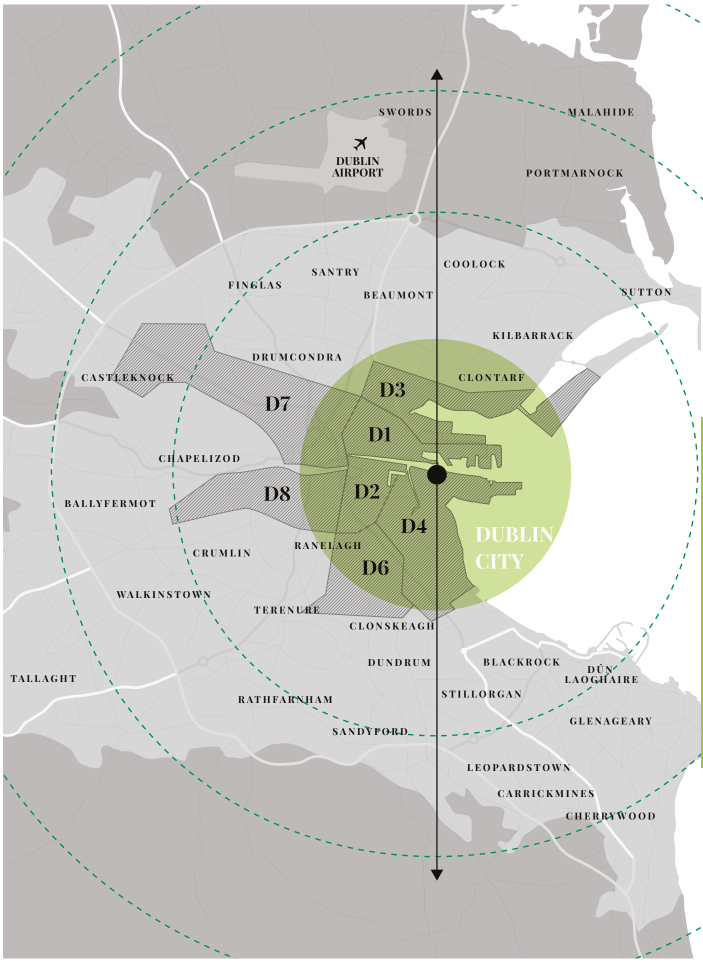
The annual rate of prime rental growth will be challenged by a sharp base effect from next quarter as a big uplift between Q1 and Q2 2022 washes out of the annual comparison. Rising vacancy will add to this pressure and, in addition to increased tenant incentives, nominal growth in prime headline rents is expected to stall.

Onsite delays have resulted in the deferral of some 2023 completions until next year. Nonetheless the pipeline of new development falls away considerably after this year and vacancy should be moving on a path back towards its natural level in 2024.

There were
NO DEALS OF GREATER THAN 5,000 SQ M
for the first time since Q3 2021

Sub-leased space accounted for
36% OF TAKE-UP
in Q1 2023

[3] The latest IMF World Economic Outlook (April 2023) forecasts global growth to slow from 3.4% in 2022 to 2.8% in 2023. However, it predicts that Ireland will remain the EU's fastest growing economy with growth of 5.6% in 2023 – 7x the EU growth rate. The IMF, like the Central Bank and ESRI, has recently uplifted its 2023 outlook for Ireland relative to its Q4 2022 position.



2023 Q1 Take-Up

26,523 sq m

DUBLIN CITY (DUBLIN 1,2 and 4)	DUBLIN FRINGE (DUBLIN 3,6,7 and 8)	SUBURBS
16,755 sq m	539 sq m	9,229 sq m
63.2%	2.0%	34.8%

> “Rising vacancy and a challenging base effect from Q2 will contribute to a further slowdown in rental growth through the remainder of this year ”

JOHN MCCARTNEY
Director,
Head of Research,
BNP Paribas Real Estate Ireland

> “Despite a slow Q1, we expect leasing to pick-up in the near-term. The amount of reserved space has risen and there remains good levels of activity on the ground in the sub-1,000 sq m market ”

KEITH O'NEILL
Executive Director,
Head of Office Agency,
BNP Paribas Real Estate

TOP 10 DEALS Q1 2023

	BUILDING	LOCATION	SECTOR	SQ M	BER RATING
1	One & Two Dockland Central	Dublin 1	DataDog	4,067	C1
2	60 Dawson Street (Grafton Place)	Dublin 2	Pinterest	2,577	A3
3	Block A, Westland Park, Willow Road	Dublin 12	Virtual Access	2,367	D1
4	Part 2nd Floor, Three Park Place	Dublin 2	Scotia Bank	1,969	A3
5	2nd floor, Building 3 Cherrywood	Dublin 18	OUTsurance	1,691	D1
6	The Reflector, Hanover Quay	Dublin 2	Pluralsight	1,287	A3
7	Part Fifth Floor, Two Dublin Airport Central	Co. Dublin	HorseWare	960	A3
8	One Park Place	Dublin 2	Confidential	683	B1
9	1 WML, Windmill Lane	Dublin 2	Ocorian	682	B1
10	10-3 Blanchardstown Corporate Park	Dublin 15	Unknown	586	C2

60 DAWSON STREET
Grafton Place
Dublin 2

	CITY CENTRE	SUBURBS
Highest Rents	€673 per sq m pa	€345 per sq m pa
Number of Deals	26	16
Average Deal Size	644 sq m	577 sq m
Typical Lease Term	15/20 years	15 years
Typical Lease Break	10 years	5 years

* Grade A sustainable buildings.

	<500 SQ M	500 / 999 SQ M	1,000 / 1,999 SQ M	2,000 – 4,999 SQ M	5,000 – 9,999 SQ M	>=10,000 SQ M
City Centre	18	4	2	2	0	0
City Fringe	2	0	0	0	0	0
Suburbs	12	2	1	1	0	0

1 & 2 DOCKLAND CENTRAL

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North Dock,
Dublin 1

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