

OFFICE MARKET

In 2017, the total gross volume of concluded transactions reached a record-breaking 530,800 m², which means an annual growth of 30.5%.

During 2017, there was a decline in the vacancy of office space from 10.55% to 7.47%.

A large part of the demand consisted of IT companies and consultancy firms.

The phenomenon of shared space is expanding: there are currently more than 40 coworking centres with a total of 28 thousand m² in Prague according to our records, and other projects are being prepared.

PRAGUE

Demand

In 2017, the total gross volume of concluded transactions reached a record-breaking 530,800 m² (a total of 778 transactions), which means an annual growth of 30.5%. We can therefore see the continuous strong demand that we've known from the two previous years.

With regard to the structure of the concluded transactions, there is a trend of relocations (i.e. new leases), which means 43% of

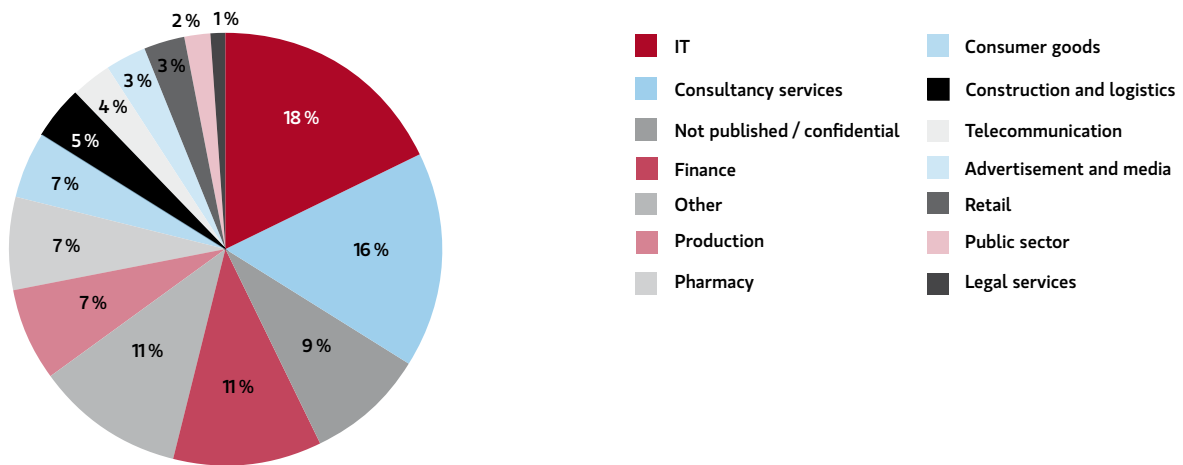
the whole demand prevails and the number of pre-leases increases. In 2017, there was 24% of pre-leases from the total of concluded transactions in this period. The renewed contracts in 2017 account for 26%, which is the same number as in the previous year. However, taking into account the decreasing vacancy, we expect that the percentage of renegotiations will increase.

"A slight increase of prices must be obviously reckoned with even in the segment of office real estate. Depending on the increasing occupancy rate of office areas, rents can very likely increase a little, too. This development is linked to an expected decrease of offers landlords provide to prospective tenants of office buildings."

Zdenka Klapalová, Knight Frank

GRAPH Take-up of offices per sector in 2017 (m²)

Source: Knight Frank Research / Prague Research Forum



GRAPH Gross take-up of offices per individual urban district in 2017 (m²)

Source: Knight Frank Research / Prague Research Forum

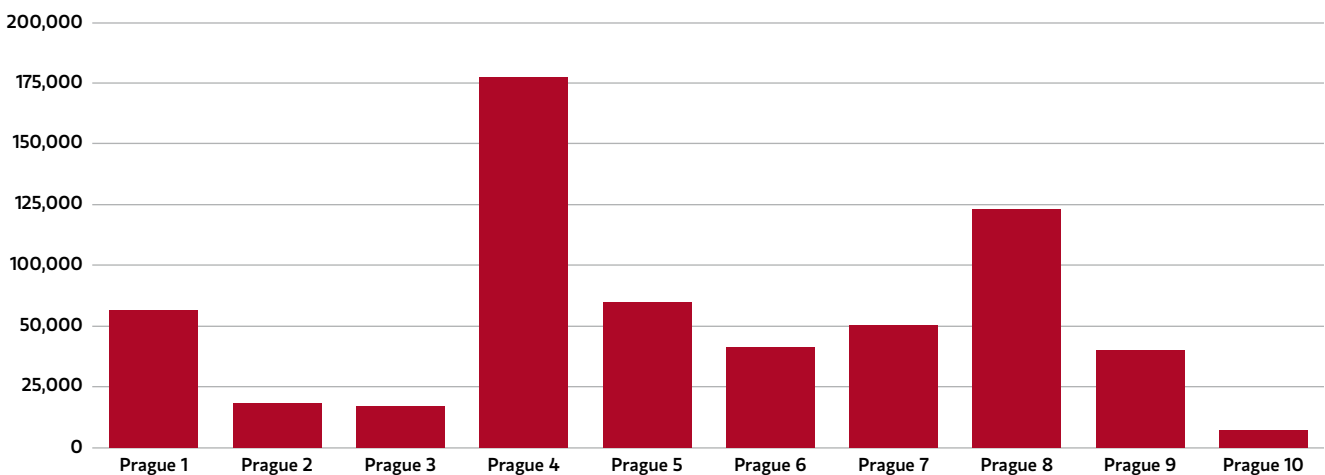


TABLE Overview of the ten largest transactions in Prague in 2017

Source: Knight Frank Research / Prague Research Forum

District	Building	Size (m ²)	Lessee	Sector	Type of transaction
4	BB Centrum A	21,500	Moneta Money Bank	Financial	pre-lease
3	Churchill square D	13,109	Deloitte	Consultancy services	pre-lease
8	Rustonka R1 (phase I)	12,512	Amazon	IT	new lease
9	Beethoven	12,420	Confidential / not published	Telecommunication	pre-lease
9	Beethoven	11,480	Confidential / not published	Others	pre-lease
8	KPMG Office Centre	11,044	KPMG Česká republika	Consultancy services	renegotiation
4	The Park 8;10;12	9,989	Honeywell	Production	renegotiation
7	A7 Office Centre A, D, E	7,805	CZECH NEWS CENTER	Others	renegotiation
7	Visionary	7,140	Accenture Central Europe	IT	pre-lease
4	The Park – building 2	6,858	IBM Česká republika	IT	renegotiation

From the whole volume of transactions in 2017 (as well as in the previous year), the IT sector contributed to this number the most (18.1%), followed by consultancy firms (16.5%) and the financial sector (10.7%). The biggest volume of lease transactions was recorded in three traditional Prague office locations – the highest demand was in Prague 4, followed by Prague 8 and then Prague 5.

Supply

The total supply of office space in Prague reached 3,342,100 m² at the end of 2017. Last year, a total of 136,000 m² of office space was completed, which, compared to the all-time low construction in the previous year (only 33,400 m²), means

TABLE Overview of completed buildings in 2017

Source: Knight Frank Research / Prague Research Forum

District	Project	Address	Developer	Capacity (m ²)
8	DOCK IN TWO	Voctářova	Crestyl	6,903
1	DRN	Národní třída	Sebre	7,655
5	Five	Na Valentince 504/4	Skanska	13,379
8	Rustonka R1 (phase I)	Sokolovská	J&T	11,280
5	Mechanica 01	Radlická	Penta	15,066
5	Mechanica 02	Radlická	Penta	11,353
4	Main Point Pankrác	Milevská 2095/5	PSJ	22,000
1	Palác Špork	Hybernská 5	Sebre	6,629
5	Aspira Business Centre	Bucharova 2928/14	Livesport	16,367
8	AFI Karlín	Pernerova	AFI	17,876
4	Pankrác Prime Office Building	Lomnického	Velska	7,482

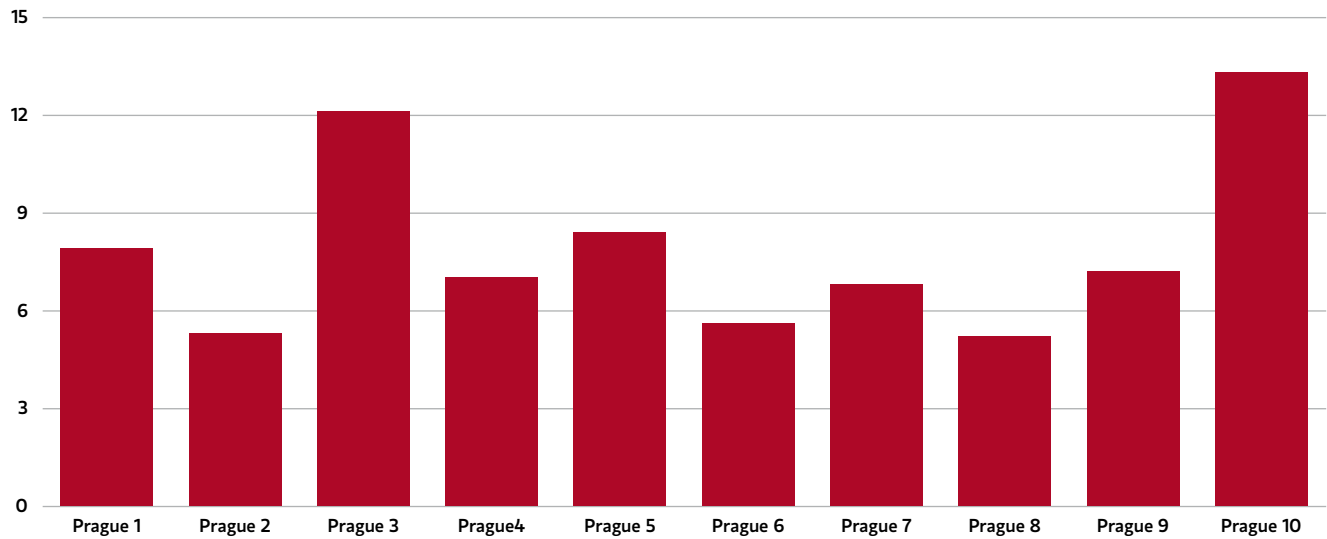
TABLE Projects with completion date in 2018

Source: Knight Frank Research / Prague Research Forum

District	Project	Type	Developer	Total office area (m ²)	Completion
1	Nekázanka 11	Reconstruction	Omnipol	5,600	2018 Q1
4	BB Centrum C	Reconstruction	VIG Fund	11,613	2018 Q1
4	BB Centrum D	Reconstruction	Passerinvest	3,826	2018 Q1
4	Trimaran (City Deco)	New construction	SB Gruppe	18,320	2018 Q1
5	City West A1	New construction	Finep	9,332	2018 Q1
7	Visionary	New construction	Skanska Property	20,477	2018 Q1
1	Národní Office Centre (Albatros)	Reconstruction	PSN	3,500	2018 Q2
1	Palác ARA	Reconstruction	ECE	2,590	2018 Q2
4	BB Centrum A	Reconstruction	Passerinvest	21,500	2018 Q2
5	Dynamica	New construction	Penta Investments	13,383	2018 Q2
8	Palmovka Open Park 3	New construction	Metrostav	9,776	2018 Q2
8	Palmovka Open Park 4	New construction	Metrostav	13,227	2018 Q2
8	Palmovka Open Park O	New construction	Metrostav	1,890	2018 Q2
8	Rustonka R2 (phase I)	New construction	J&T	11,328	2018 Q2
4	City Element	New construction	SB Gruppe	8,481	2018 Q3
4	Eurovia	New construction	Eurovia	3,000	2018 Q3
6	AFI Vokovice	New construction	AFI Europe	12,219	2018 Q3
5	ČSOB HQ. II	New construction	ČSOB	30,000	2018 Q4


GRAPH Vacancy rate in individual urban districts in QA 2017 (in %)

Source: Knight Frank Research / Prague Research Forum


GRAPH The development of prime rents in years (EUR/m²/month)

Source: Knight Frank Research / Prague Research Forum



a return to the figures of average construction from previous years.

Most of the finished projects were pre-leased due to the high demand for office space. The percentage of buildings with secured leasees accounted for up to 42.4% at the end of the year.

Currently, about 308,700 m² of office space are being constructed. We expect that 203,400 m² (52,000 m² being reconstructed) will be completed in 2018. Almost 45% of this office space is pre-leased before it is completed.

In 2019 105,300 m² of office space should be completed, but this number is very likely to increase as new constructions will be started on time. Therefore, the number of newly completed office projects should exceed the average in 2019 as well.

Vacancy

During 2017 there was a decline in the vacancy of office space in Prague from 10.55% to 7.47%. There was a decline in almost all districts, even in those that are not typical office locations. Like last year, the lowest rate of vacant office space is in Prague 8 (5.2 %).

With regard to the high demand and the fact that the projects that are

under construction are already half occupied, we don't expect the vacancy rate to grow during 2018. It is expected that it will stay at 7 – 8%.

Rent

Prime rents increased at the end of 2017. They were between 20.00 – 21.00 EUR/m²/month in the city centre, and 15.00 – 16.50 EUR/m²/month in the wider centre. In the outer city, the prices were at about 13.50 – 15.00 EUR/m²/month. This increase is caused by the current low vacancy rate of office buildings in Prague. However, we expect the rents to be stable in 2018 because of the excessive construction. The number of incentives starts to decrease due to high demand.

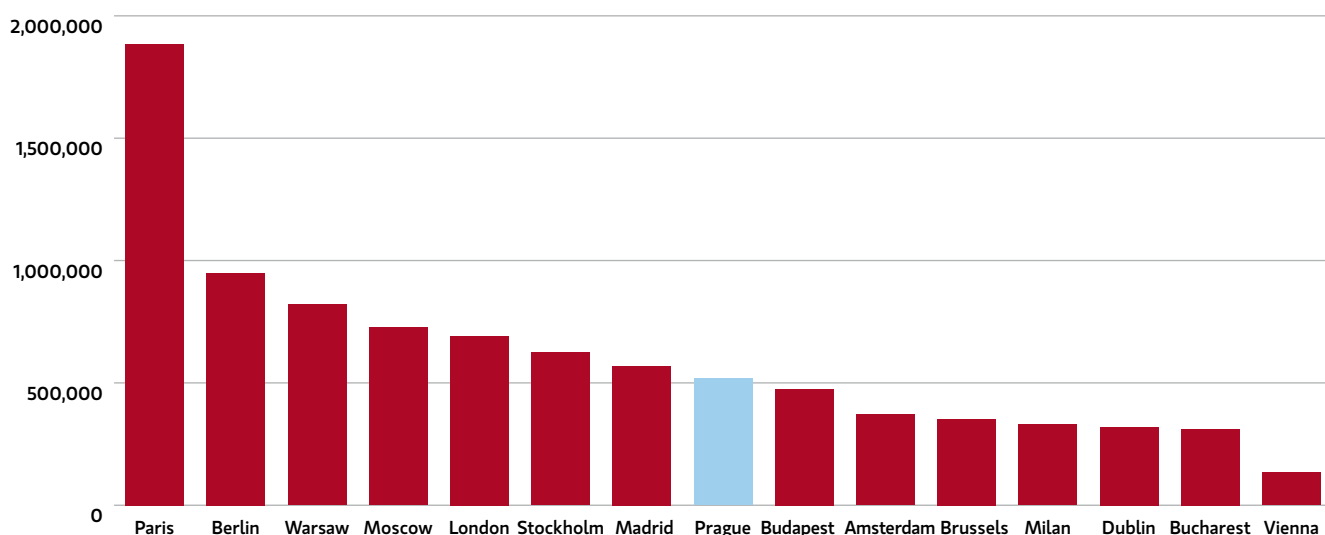
EUROPEAN CONTEXT

In Europe, there is still a positive economic climate, which is reflected in the economic growth of individual countries and decreasing unemployment. On the contrary, the number of office jobs is increasing as well as the demand for office space – some cities including Prague show a record-breaking demand. For example, Berlin, Dublin, Madrid, Paris and Warsaw are also reporting extremely high gross demand.

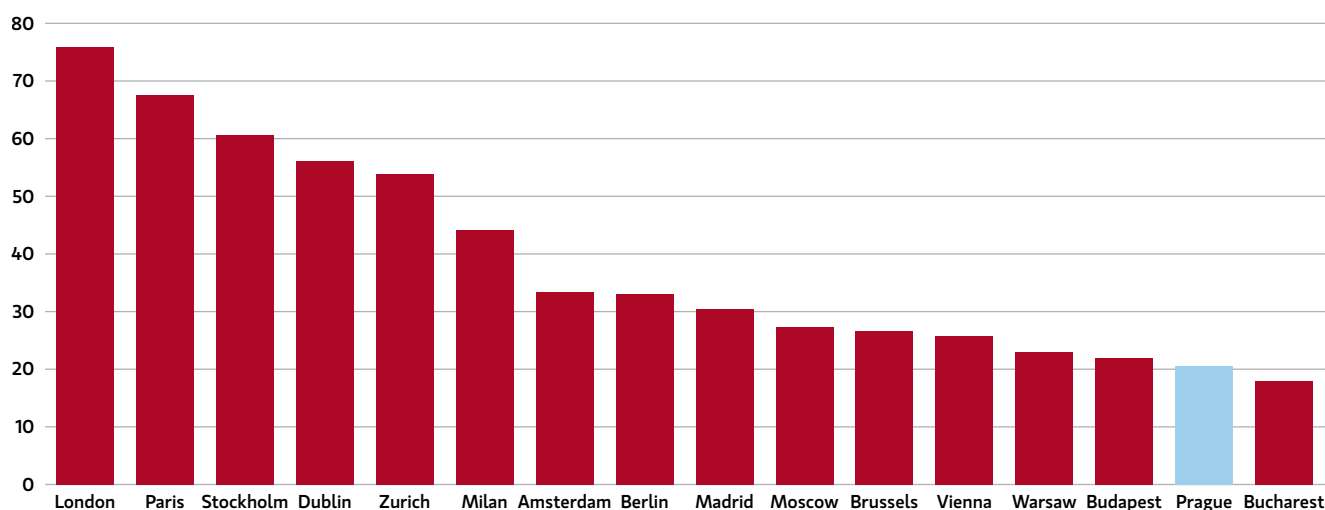
Prague is a European city with one of the lowest rents. Lower (prime) rents are only in Bucharest, where it is around 18.00 EUR/m²/month. It


GRAPH Volume of demand in individual European cities for 2017 (m²)

Source: Knight Frank Research / Prague Research Forum


GRAPH Prime rents in European cities in Q4 2017 (EUR/m²/month)

Source: Knight Frank Research / Prague Research Forum



is also necessary to mention that the level of the highest prime rents has increased in more than half of European cities, including Prague, by an average of 8%. The rents only decreased in Moscow and Warsaw.

The average vacancy rate is at the level of 7.50%, which is also the current vacancy rate in Prague. The lowest vacancy rate is currently in Berlin – 2.25%. The highest vacancy rate is currently in Moscow – 13%.

TABLE Highest prime rents in European countries (comparison of Q4 2016 and Q4 2017)

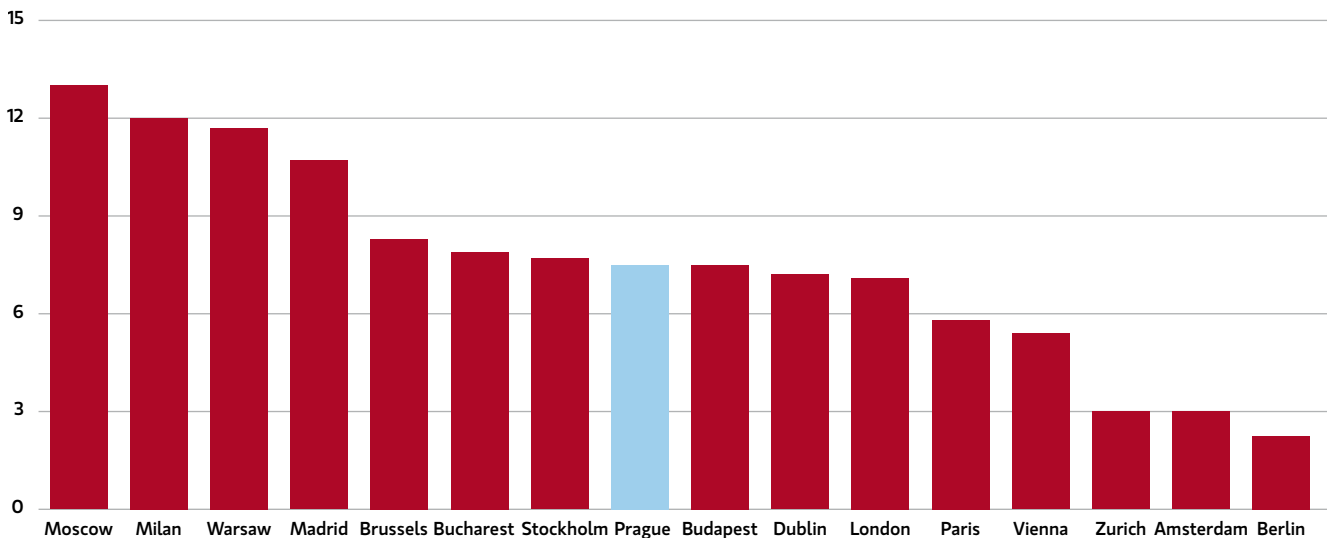
Source: Knight Frank Research / Prague Research Forum

City	Q4 2016 (EUR/m ² /month)	Q4 2017 (EUR/m ² /month)	Growth vs. Decline	Change in comparison Q4 2016
Amsterdam	30.42	33.33	Growth	9.56%
Berlin	30.00	33.00	Growth	10.00%
Brussels	25.00	26.67	Growth	6.68%
Budapest	22.00	22.00	–	no change
Bucharest	18.00	18.00	–	no change
Dublin	53.83	56.08	Growth	9.56%
London	75.83	75.83	–	no change
Madrid	28.00	30.50	Growth	8.92%
Milan	41.67	44.17	Growth	5.99%
Moscow	28.90	27.26	Decline	-5.67%
Paris	64.17	67.50	Growth	5.18%
Prague	19.50	20.50	Growth	5.12%
Stockholm	54.44	60.69	Growth	11.48%
Vienna	25.75	25.75	–	no change
Warsaw	24.00	23.00	Decline	-5.67%
Zurich	53.90	53.90	–	no change




GRAPH Vacancy rate in individual European cities in QA 2017 (in %)

Source: Knight Frank Research / Prague Research Forum



The economic growth of Europe should continue in the coming years, which means positive prospects for most European office markets. We expect stagnation in the next 12 months, and in some cases also an increase in prime rents in European big cities¹.

BRNO

Supply

The total area of modern office space in Brno was 551,800 m² in the second half of 2017. Class A buildings accounted for 81% of the total area, and class B offices accounted for the remaining 19%.

Since 2000, a total of 393,200 m² of office space has been built in Brno. The average annual construction is 23,100 m². In the first half of 2017, 3 office buildings were completed in Brno. Šumavská Towers C (8,300 m²), ROZMARYN office & parking (4,700 m²) and Technology Park II building C (4,300 m²). In the second half of 2017, no office buildings were completed.

Currently, 51,100 m² of office space are being constructed. This consists of five projects: Areal Slatina P (15,300 m²), Campus Science Park building D&E (13,200 m²), Vlněná Office Park F&G (12,000 m²) and Šumavská Tower B (10,600 m²). All buildings should be completed during 2018.

Demand

In 2017, the gross take-up including renegotiations in Brno reached a total of 55 700 m², which was about 6,9% less than in the previous year. The largest transaction in 2017 was the pre-lease of an anonymous company in Vlněná Office Park F&G (8,500 m²), followed by a new lease of an anonymous company in Areal Slatina O (4,100 m²) and the expansion of SAP in the buildings of Spielberk Office Center IQ (3,700 m²). In the long term, the demand in the office market is driven by IT companies, which are also one of the most expanding companies, and by companies from the production sector.

Since 2014, the demand in Brno has been stable between 50 and 60 thousand m² every year with a slightly increasing trend. This

trend will continue in 2018. Currently in Brno (like in Prague), we can see an excess of demand over supply thanks to the strong economic situation. Developers would particularly like to make use of this situation and deliver 51,100 m² of office space to the market in Brno. It's no exception that new office projects are often fully pre-leased before their completion. If the economy continues to do well, lessees will have to deal with the lack of office space in the coming years.

Vacancy

The vacancy rate during the second half of 2017 decreased by 2.4 % and reached a value of 7.3%. We expect a short-term increase in vacancy with regard to the completion of certain projects. However, with regard to the high demand, the situation of pre-leases (for example, the present phase of Vlněna project had an occupation of 95% on the completion date according to this report) and lower number of completed projects, we expect that vacancy will decrease in 2018–2019.

Rent

Prime rents in Brno were stable at 13.50 EUR/m²/month in the second half of 2017. We expect that the lack of new offices may result in a further increase of rents.

During 2015–2017, there was quite a significant difference between Prague and Brno in the extent of provided incentives. While incentives in Prague reached 30% and in some cases even 35% (for new leases), the difference between nominal and effective lease in Brno was not that large².

OSTRAVA

Supply

The total area of modern office space in Ostrava was 213,400 m² in the second half of 2017. Class A buildings accounted for 73% of the total area, and class B offices accounted for the remaining 27%.

¹ Brexit negotiations have not had a direct influence on the London office market as it was originally expected. On the contrary, the total volume of demand in London grew by almost 19.3% in 2017.

² The extent of incentives only reached slightly more than 20% for relocations, and are usually between 15 and 20%, provided that they continuously decrease.

In 2017, one office building – ABC Alfa (6,500 m²) – was completed in Ostrava. Currently, one office building is being constructed and its completion is planned for 2018. This is the Red House (4,500 m²) building. Compared to Brno, the construction of office buildings in Ostrava is negligible.

Demand

The total gross take-up reached 20,500 m² in 2017, which means an annual growth of 44%.

The largest transactions in 2017 were the renegotiation of an anonymous company in the premises of Orchard Ostrava (2,600 m²), followed by the renegotiation and expansion of an anonymous company (1,500 m²) in the same premises, and the expansion of ABB (900 m²) in the premises of Nová Karolina Park.

Vacancy

At the end of the second half of 2017, 28,400 m² of vacant office space was registered in Ostrava. The vacancy rate therefore decreased by 4.3% to 13.3% compared to the first half of 2017. During 2018, we expect a further decrease in vacancy due to the limited supply and the expansion of current lessees in the location.

Rent

Again, prime rents in Ostrava were at 11.50 EUR/m²/month in the second half of 2017. Rents are therefore stable, even though the demand is increasing and little construction is planned for the future. A slight increase in prime rents to up to ca. 12.00 EUR/m²/month can be expected in the course of this year.

CURRENT TRENDS

Most corporations continue to see offices not as an expense, but as tools to retain and attract new staff, as well as an environment that should move them forward in terms of innovations. As a consequence, lessees try to get closer to people with their offices. They should therefore be located in places that suit their employees best. The employees should also not adapt to their work environment (some don't like open spaces, some like it), their work environment should adapt to them, mostly to the nature of their job and to what suits them. The best is to achieve the above-mentioned qualities with regard to flexibility and as little liabilities for the future as possible, which is caused by the dynamics of these days.

What impact does this have on the office market?

- From the point of view of potential lessees' requirements:
- Requirements for interiors are growing, the layout is changing
- The location plays a greater role than it used to because of employees
- Requirements for the flexibility of a lease are growing

Impact for lessors

- The importance of location is growing – a “corporate” environ-

- ment is not attractive (e.g. business parks in peripheral locations)
- Effort to create a community environment
- The pressure to improve the quality of services provided in the building (and not only the quality but also the range of services)
- The implementation of digital services
- Requirements for the management of the building are increasing
- Flexibility (lease term, etc.)
- Future trend – coworking space as an integral part of the building

One of the consequences of the above-mentioned trends is the rapid expansion of coworking spaces. Some time ago, coworking centres belonged to start-ups and freelancers. However, the demand for this type of space is also increasing among corporations due to the mentioned reasons, which started using coworking space for some of their project teams or departments. These are the benefits:

- Flexible contracts that allow working on projects or autonomous teams
- Attractive work environment – coworking centres are usually designed in a way to make people choose them as their work environment
- Environment in which both company and employees are clients – the provision of office space is also a service
- There is a wider community around them, which brings contacts, inspiration and a contagious atmosphere in a community that is positive about entrepreneurship
- Supplementary services and training sessions that are usually offered by the operators of coworking centres

There are more than 40 coworking centres with a total of 28,000 m² in Prague according to our records³, but this is still only 1% of the total volume of office space in Prague. For example, coworking space takes up over 4% of the total office space in London.

In 2018 and 2019, we expect a large expansion of coworking centres in the Czech capital as well. On the basis of the market demand, we predict that transactions related to coworking centres with between 18 and 20 thousand m² of newly expanded areas could be concluded in 2018.

It is clear that with such volume the demand has to move more towards traditional administrative buildings (in attractive locations). Taking into account the limited supply (low vacancy rates), the pressure on the increase in rents will be greater. At the same time, it can be expected that some lessors will start operating coworking centres.

It can be also expected that not only parts of departments or project teams will be moved to similar spaces, it is also possible that whole companies will move and work in a coworking environment. After all, it is already happening abroad.

PAVEL NOVÁK AND RENATA PRAŽÁKOVÁ
Knight Frank

³ Precise data are not recorded which is also because of the fact that most coworking centres are not located in “traditional” administrative buildings that are monitored by Prague Research Forum.