

OFFICE MARKET

The total gross volume of concluded transactions in the Prague market declined slightly. Despite this, the trend of strong demand from previous years continues.

In Prague, the office vacancy rate dropped to 5.1%.

The Brno market remained relatively stable year-on-year.

The trend of offices as a service continues, with an emphasis on productivity, the use of new technologies and mobility.

PRAGUE

Demand

In 2018, the total gross volume of concluded transactions in Prague reached 519,200 m² – with a total of 666 transactions.

In my opinion, rent will increase as a result of the increase in construction work. This is likely to happen only in newly built buildings. I do not think that the interest in rental should decline because of the slight increase in price. I am a little worried that experts may speak about the impending crisis too much. As a result, tenants may be more concerned and lose interest.

Václav Thoss, GES REAL

Although there was a slight decline year-on-year, this is still an above-average result. The strong demand from previous years continues.

If we take a closer look at the structure of realized demand, we will find that in 2018 the proportion of renegotiations and new leases was basically equal. Both types of transactions occupied about 35% of the total volume. The third largest transaction in terms of volume were pre-leases, i.e. transactions with buildings that were under construction

at the time. In 2018 this type of transaction reached 19% of all the transactions executed in that period. In the future we expect pre-leases to continue to occupy a significant portion of the volume.

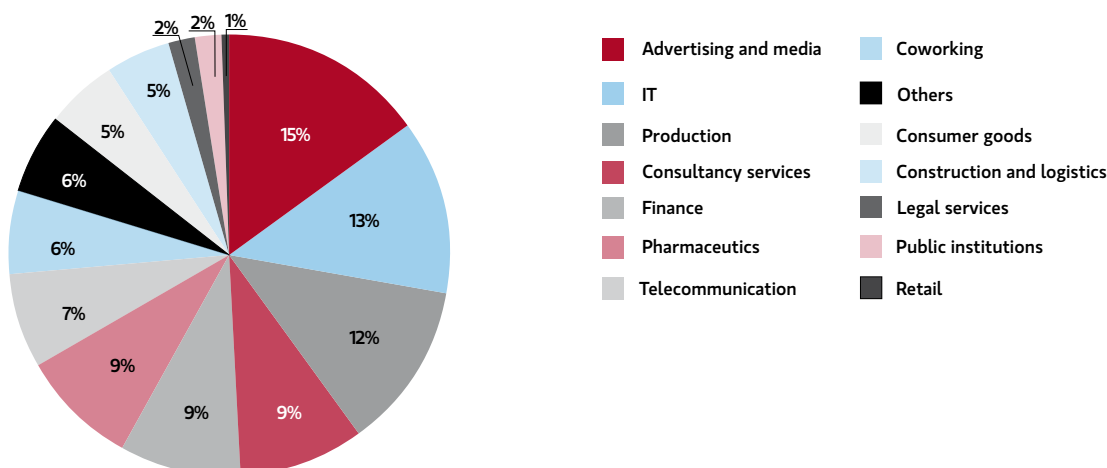
In terms of sectoral statistics of office demand in 2018, the advertising and media sector dominated with a 15% share in the total volume of transactions. This sector was followed by IT (13%) and production (12%). As in the previous year, the most desirable location in 2018 in terms of realized transactions was Prague 4 (25%), followed by Prague 8 (19%) and Prague 5 (18%).

Last year, world coworking center operator WeWork entered the Czech market and leased nearly 6,000 square meters in administrative building Drn in Prague 1. The company thus added to the plenty of other coworking operators, such as BusinessLink or HubHub, who also decided to bring their shared office concepts to the metropolis last year. The global boom of coworking, which we pointed out in last year's Trend Report, has reached the Prague market, and it will be interesting to see whether it will change the office space market like it did in Western metropolises.



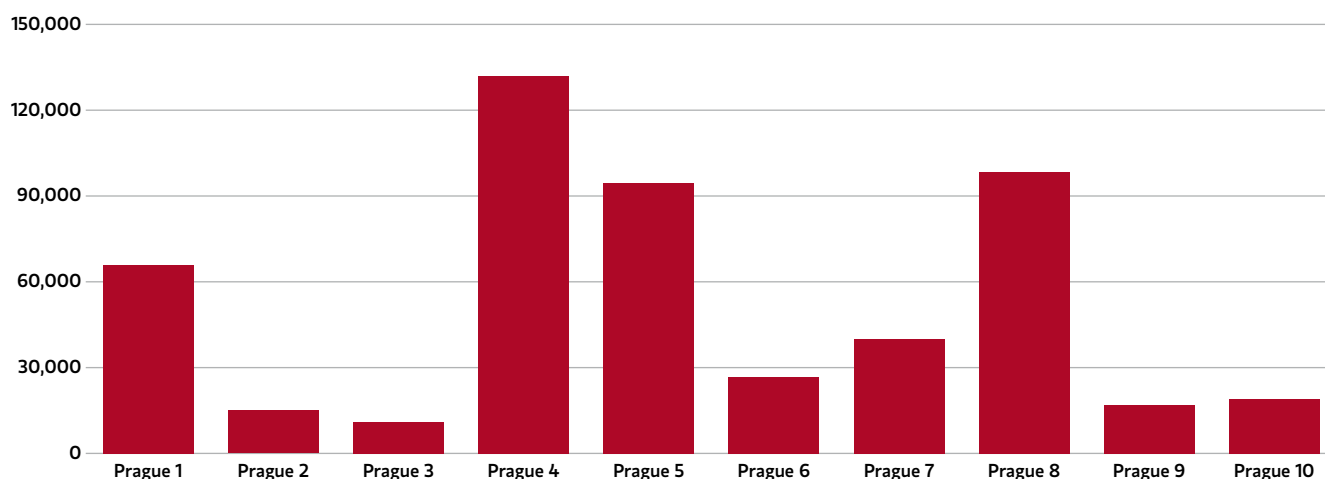
GRAPH Gross realized office demand according to sector in 2018 (m²)

Source: Knight Frank Research / Prague Research Forum




GRAPH Gross realized office demand according to individual municipal districts in 2018 (m²)

Source: Knight Frank Research / Prague Research Forum


TABLE Overview of the ten most important transactions in Prague in 2018

Source: Knight Frank Research / Prague Research Forum

Municipal district	Building	Size (m ²)	Lessee	Sector	Type of transaction
4	BB Centrum - Gamma	29,000	O2	Telecommunication	renegotiation
7	Bubenská 1	16,300	WPP	Advertising and media	pre-lease
5	City West B2	13,100	Siemens	Production	renegotiation
10	Centrum Vinice	11,800	FTV Prima	Advertising and media	pre-lease
5	City West B3	10,100	Siemens	Production	renegotiation
8	River Garden I	8,000	ADP Employer Services Česká republika	IT	renegotiation
1	Drn	5,800	WeWork	Coworking	new lease
8	Praga Studios	5,300	Edwards Lifesciences Czech Republic	Pharmaceutics	pre-lease
5	Dynamica	4,700	Strabag	Construction and logistics	new lease
5	Smíchov Business Park	4,400	Wunderman	Advertising and media	renegotiation

Supply

The total office space in Prague at the end of 2018 reached 3,475,100 m². Last year, an above-average amount of office space was completed, i.e. a total of 156,900 m², of which 76% were in newly constructed projects. As in previous years, in 2018, most of this office space was pre-leased before completion.

At the beginning of 2019, a total of 348,800 m² of offices

were under construction. About 80% of these offices are in new projects, and the remaining 20% are renovations. In 2019, 200,700 m² of offices are expected to be completed in a total of 16 projects, and more than 51% of this office space is currently pre-leased. The remaining 148,100 m² should be completed in 2020-2021. However, it is necessary to assume that this figure is not final and that it will change over the course of the year, depending on the actual commencement and completion of the construction of the buildings.

TABLE Overview of newly completed buildings in 2018

Source: Knight Frank Research / Prague Research Forum

Municipal district	Project	Developer	Total office area (m ²)
5	City West A1	Komerční banka	9,300
7	Visionary	CA Immo	20,500
5	Dynamica	Penta Investments	13,400
8	Rustonka R2 (phase I)	J&T	11,400
4	Trimaran	S+B Gruppe	18,300
6	AFI Vokovice	AFI	12,200
4	Eurovia	Eurovia	3,000
8	Palmovka Open Park 3	Metrostav	9,800
8	Palmovka Open Park 4	Metrostav	13,200
4	City Element	S+B Gruppe	7,600

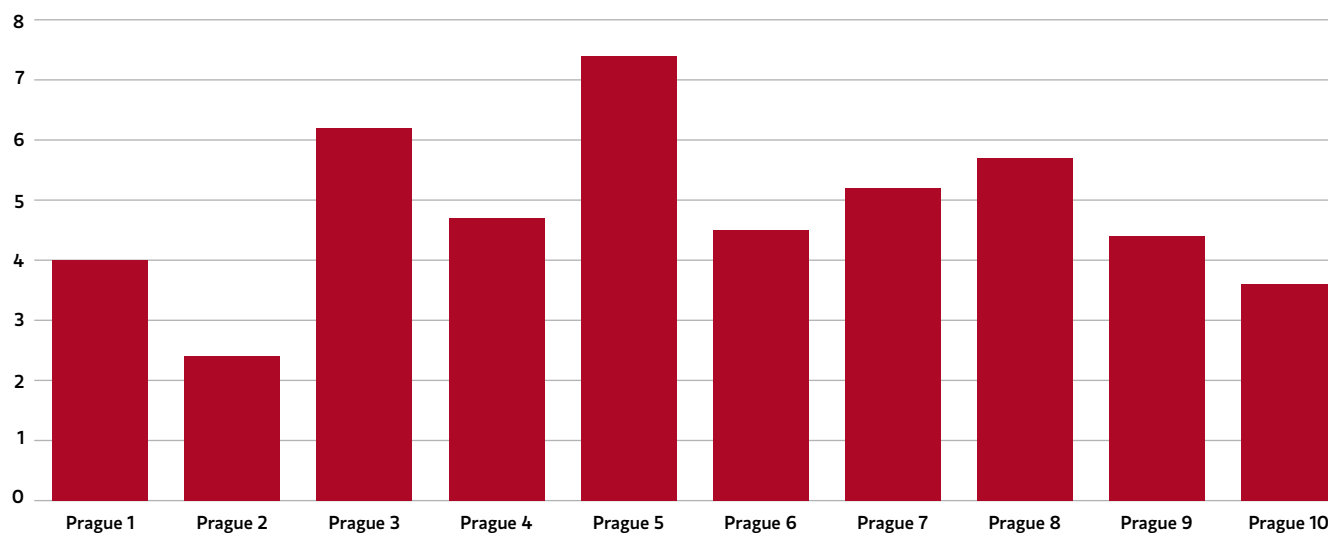
TABLE Projects with a completion date in 2019

Source: Knight Frank Research / Prague Research Forum

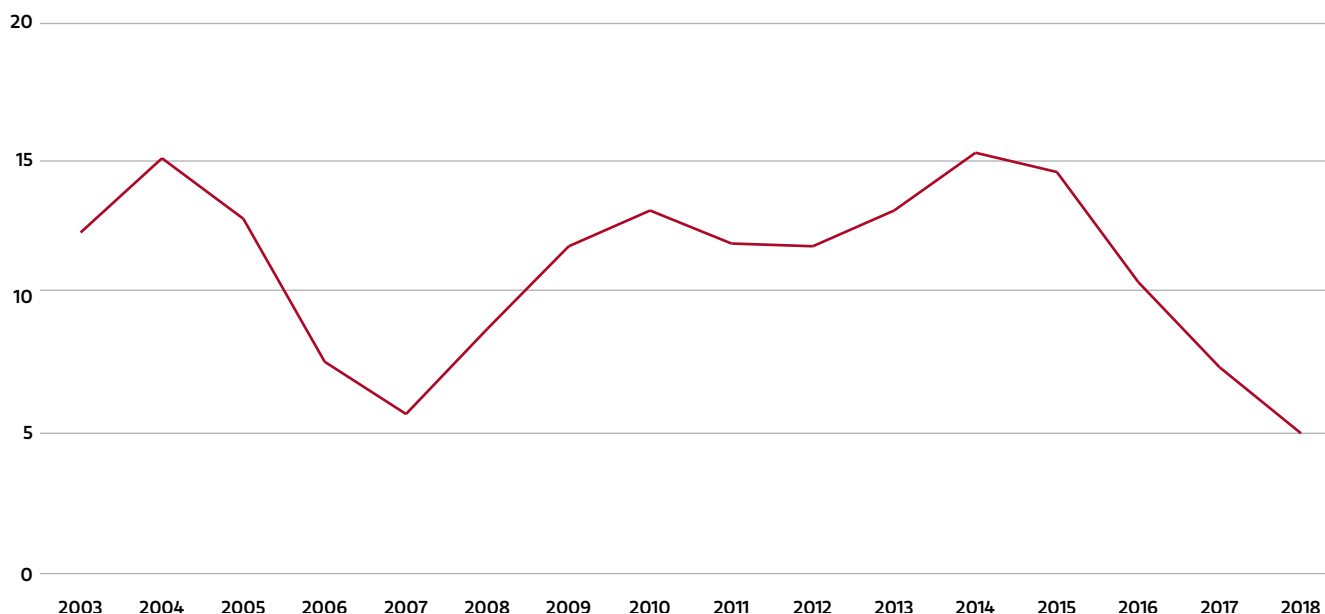
Municipal district	Project	Type	Developer	Total office area (m ²)	Completion
1	Palác ARA	Renovation	ECE Europeans Estates	2 600	2019 Q1
1	Na Poříčí 5	Renovation	Cecopra	1 300	2019 Q1
4	Mayhouse	New construction	CPI Group	7 400	2019 Q1
8	Rustonka R3 (fáze II)	New construction	J&T	11 400	2019 Q1
5	ČSOB HQ. II	New construction	ČSOB	30 000	2019 Q2
6	Telehouse	Renovation	BPD Group	20 900	2019 Q2
9	Harfa Office Center	New construction	KAPRAIN Group a Lighthouse Group	28 300	2019 Q2
5	Green Point	New construction	Karlovarské minerální vody	7 500	2019 Q2
8	Praga Studios	New construction	Skanska Property	11 200	2019 Q2
7	Argentinska Office Building	New construction	Sudop	6 200	2019 Q2
4	LifeBuilding C (BB Centrum C)	Renovation	VIG	11 100	2019 Q2
8	DOCK IN THREE	New construction	Crestyl	16 000	2019 Q3
2	Churchill I	New construction	Penta Investments	15 200	2019 Q3
5	SmíchOFF	New construction	Penta Investments	11 700	2019 Q3
10	Centrum Vinice	Renovation	GES Real	14 300	2019 Q4
7	Letná OC	New construction	Lordship	5 500	2019 Q4

GRAPH Vacancy rate in individual municipal districts in Q4 2018 (in %)

Source: Knight Frank Research / Prague Research Forum


GRAPH Development of the vacancy rate in Prague according to year (in %)

Source: Knight Frank Research / Prague Research Forum



Vacancy rate

As in previous years, in 2018 there was a decrease in the vacancy rate of office space in Prague, Specifically from 6.2% to 5.1% (which represents about 178,800 m² of free office space). This is the historically lowest vacancy rate, surpassing the 5.8% of vacant offices in 2007. This is mainly due to continuing above-average demand, which is currently not satisfied by the supply of office space. However, the hunger for expansion associated with workforce recruitment is already at its peak and is slowly reaching its limits. The positive atmosphere of the past few years may result in a moderate cooldown in 2019.

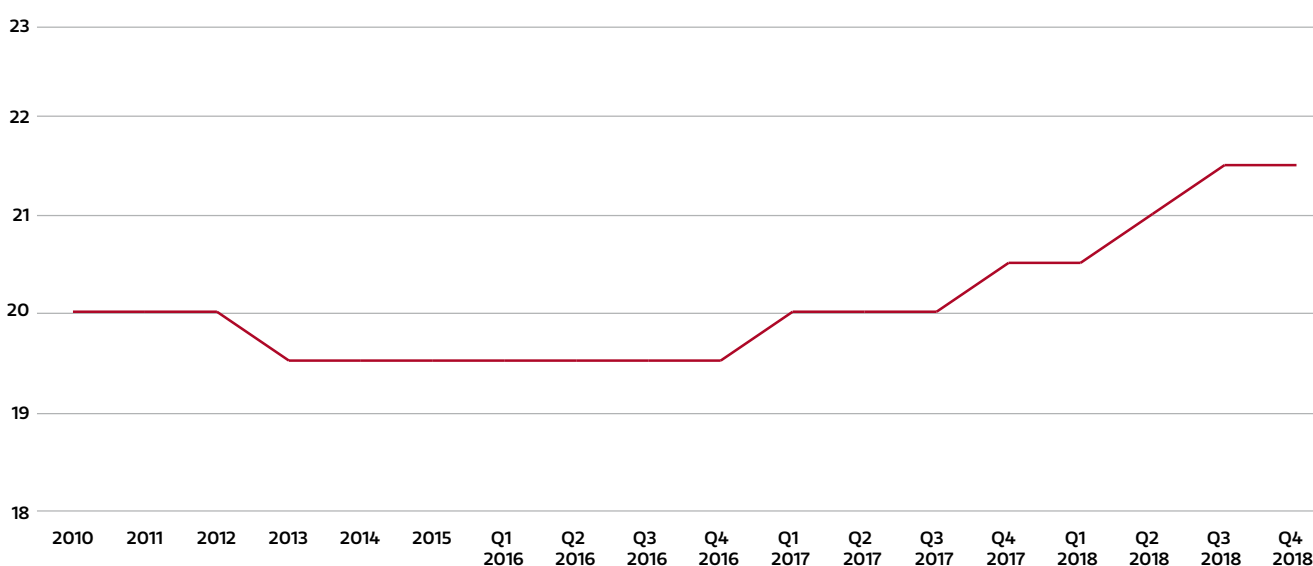
Rental rate

The highest achieved rental rate rose slightly during the year, and at the end of 2018 it was between 21.00–22.00 EUR/m²/month in the city center. In the area surrounding the center it was between 15.00–16.50 EUR/m²/month, and in the outer city it was 13.50–15.00 EUR/m²/month. This is mainly due to the long-term low vacancy rate of office space. On the other hand, since an above-average number of office projects should be completed in 2019, we do not expect a dramatic increase in rental rates, but rather their stabilization.

As far as incentive rates are concerned, it is no longer true that lessees can dictate their amount, as was the case in the years after the crisis. Given the current market situation, it can be said that the lessor has a clear advantage.

GRAPH Development of the highest achieved rental rate according to year (EUR/m²/month)

Source: Knight Frank Research / Prague Research Forum



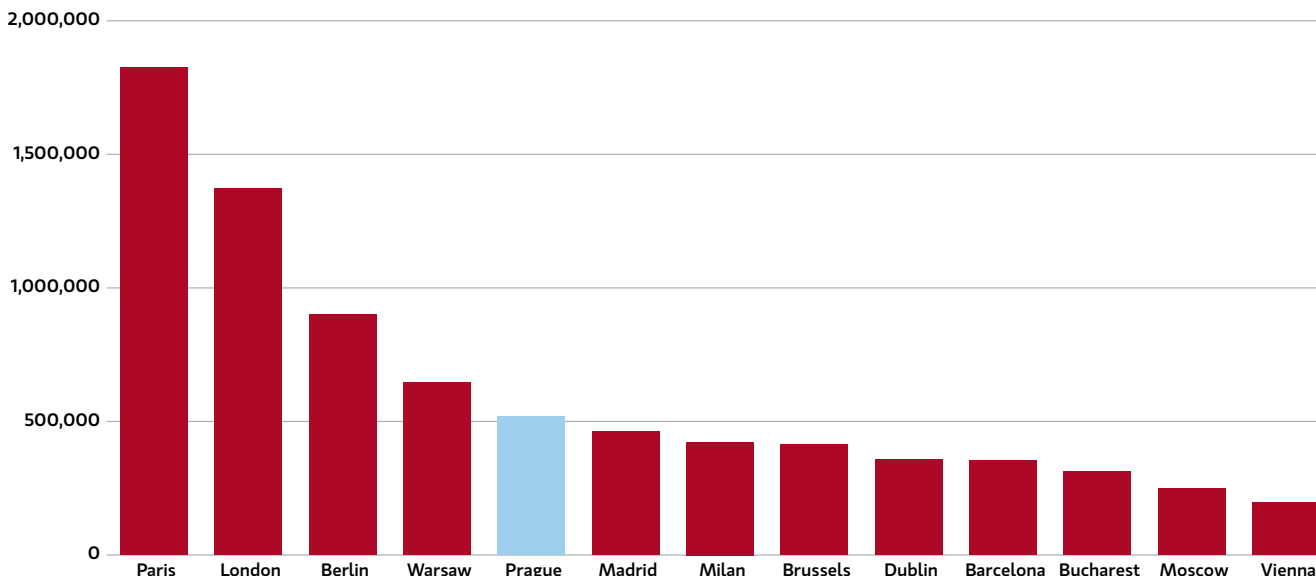
EUROPEAN CONTEXT

The continuing positive economic climate and low unemployment rates across the EU have led to a high demand for office space, but in many metropolises there is a lack of vacant space.

This is a long-lasting phenomenon, and nothing suggests that it will change. The demand in individual European countries therefore continues to be above average. A record volume of demand this year was reported by Milan and Dublin.

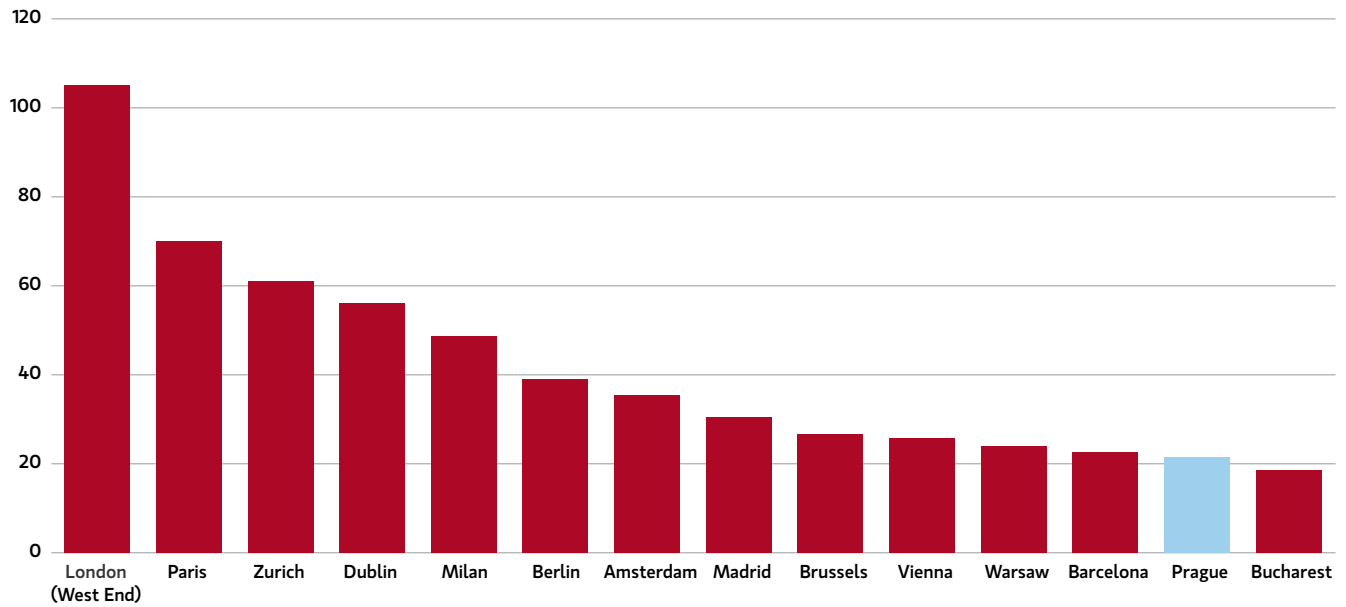
GRAPH The volume of demand in individual European cities for 2018

Source: Knight Frank Research / Prague Research Forum




GRAPH Highest rental rates in European cities in Q4 2018 (EUR/m²/month)

Source: Knight Frank Research / Prague Research Forum

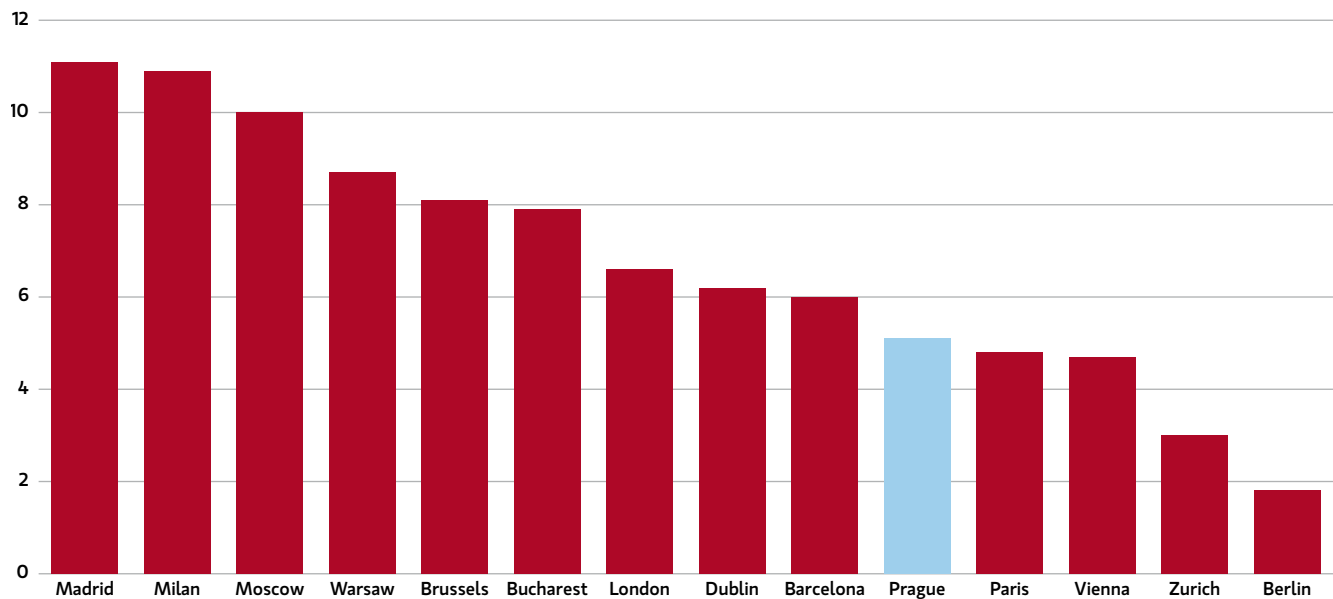


Prague continues to rank among cities with the lowest rental rates. As in 2017, in 2018 European cities also recorded an increase in the achieved (premium) rental rate, at an average

of 5%. In Berlin, the highest rental rate increased by 18% year-on-year.


GRAPH Vacancy rate in individual European cities in Q4 2018 (in %)

Source: Knight Frank Research / Prague Research Forum



The average vacancy rate in European capitals is around 6.1%, which is only a 1% difference in comparison with Prague. The lowest vacancy rate was reported in Berlin (1.8%), and the highest rate was in Madrid (11.1%).

BRNO

Demand

In 2018, gross demand in Brno, including renegotiations, amounted to a total of 58,200 m², which represents a year-on-year increase of 6%. Demand in Brno therefore continues to remain at a steady level as in previous years. Not surprisingly, IT companies have become the most active sector in terms of overall demand with a 50% share. The largest transaction in Brno was the pre-lease of Moravia IT (8,500 m²) in the new

office project Vlněna Office Park AB, followed by the renegotiation of AT&T (8,000 m²) in the building Campus Science Park C.

Supply

The office space supply in Brno amounted to a total of 583,400 m² in the second half of 2018. Class A buildings accounted for 82% of the total area, and 19% consisted of class B offices.

In 2018, 38,800 m² were completed in four office buildings. Specifically: Campus Science Park DE (13,300 m²), Vlněna office park FG (12,400 m²), Vlněna office park H (6,400 m²) and CTOffice A3 (6,700 m²).

There are currently 6 office projects with a total area of about 60,000 m² under construction. All these projects should be completed during 2019.

Vacancy rate

The vacancy rate in Brno gradually increased in 2018 reaching 9.6% at the end of 2018. This was a 2.3 % increase in comparison with the previous year. However, we consider this increase to be a short-term phenomenon that occurred due to the supply of a higher volume of newly built office space to the Brno market, as Brno-based companies are struggling with the lack of adequate office space.

Rental rates

The highest rental rate in Brno during 2018 rose to 14.50 EUR/m²/month. Nevertheless, rental rates in Brno are still tens of percents lower than in Prague, which, along with other added value such as a high proportion of college students and a shorter distance to Austria and Slovakia, makes Brno an attractive place to locate business.

OSTRAVA

Demand

The gross demand in 2018 reached a total of 21,920 m². This is a relatively low year-on-year increase of 7%. The largest transaction in Ostrava in 2018 was the renegotiation of Okin (7,300 m²) in the Orchard office complex.

Given the current market situation in Ostrava, it is likely that demand for offices will increase in the course of 2019.

Supply

Office space in Ostrava did not change in 2018, and it amounted to 213,400 m². Class A buildings accounted for 73% of the total area, and the remaining 27% consisted of B class offices.

A total of 10,000 m² of office space is under construction in the Smart Innovation Center office complex, which is due to be completed in the first half of this year.

Vacancy rate

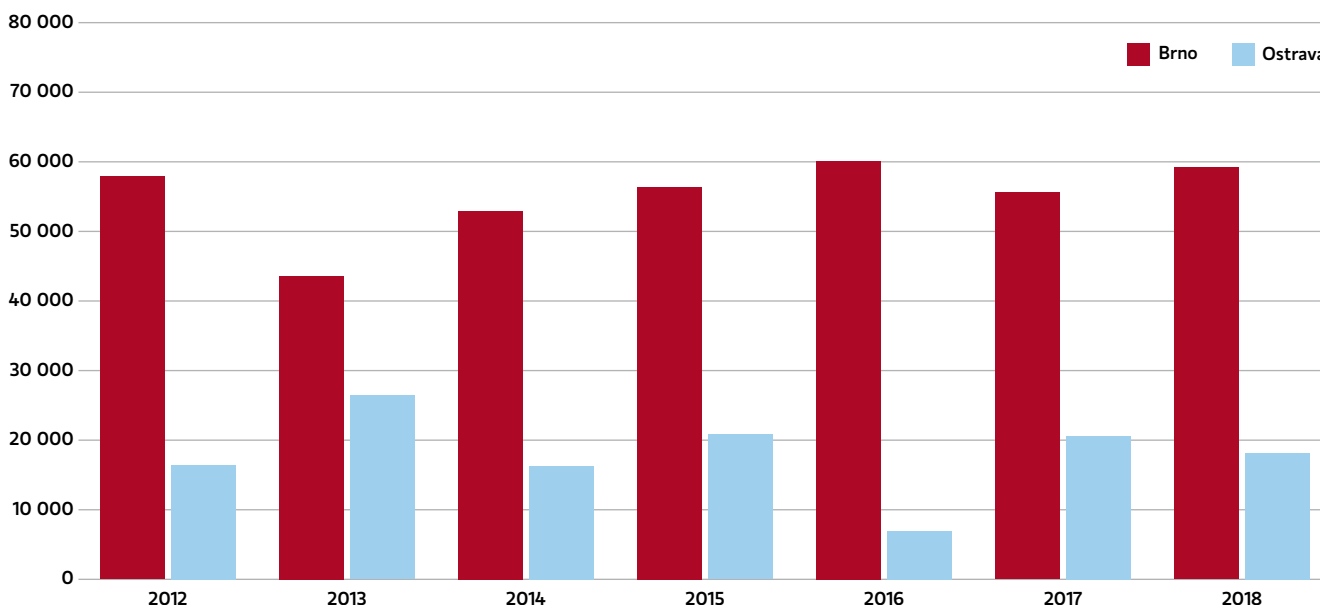
At the end of 2018, a total of 19,600 m² of free office space was registered in Ostrava. The occupancy rate therefore declined by 4.1% to 9.2% compared to the previous year. The office vacancy rate in Ostrava will stagnate or increase in the short term in regards to the occupancy rate of the Smart Innovation Centre project. However, the currently limited supply in Ostrava will reduce the amount of vacant space in the long run.

Rental rates

The highest rental rate in Ostrava in 2018 remained stable and ranged between 11.50-12.00 EUR/m²/month. A slight increase in the rental rate may be expected, taking into account the development of demand in Ostrava.

GRAPH Realized office demand in Ostrava and Brno according to year 2012–2018

Source : Knight Frank Research / Prague Research Forum



TRENDS

Now more than ever, it is necessary to follow trends and be aware of their direction on a global scale. In cooperation with our transnational colleagues, we have jointly identified the five main areas that will shape and form the demand for offices and the work environment. However, it can be said that the following trends apply at a local and transnational level:

1. Offices as a service

Tenants' interest in investing and caring for spaces as such continues to decline. This naturally results in the prospering of coworking centers and operators of shared offices, but even traditional landlords and developers must free themselves of the mere ownership or development of real estate and come up with service innovations, community building and improve-

ment of the work environment. This increases demands on the skills and competencies of lessors.

2. Productivity instead of costs

Instead of pressure to reduce costs, we can see a high level of space efficiency. This does not mean efficiency in terms of high concentration (in order to save), which has turned out to be counterproductive ("crowded open space"). Instead, it seems more effective for a number of companies to strengthen interactions between people and their satisfaction, which they will achieve by creating an adequate working environment. This should result in higher productivity, however, but demands and costs of interiors are rising.

3. New technology

Artificial intelligence (AI), robotics and automation will have a growing impact on business processes and organizational structure. Companies will demand a different type and number of employees. They will look for offices with different demands, of different sizes and with different location requirements. The nature of demand is changing.

4. Company transformation

The technological development of humanity forces companies to re-evaluate their business models. In order to survive, many companies have to start moving to areas that have so far been completely beyond their competence (especially in the digital

domain). In addition, the demographic composition is changing, and cultural changes are taking place in companies.

5. Era of mobility

We live in an era of mobility, and the Czech Republic is becoming less and less isolated. Record activity in M&A (at a local and transnational level) is undoubtedly one of the driving forces of current demand in the rental market. In addition to the primary consequences, i.e. company relocations and expansion, we can also observe secondary effects (subleases, premature termination of contracts, etc.) in association with M&A market activity. In general, however, there is a move towards labor force, or talent, but also lower (wage) costs.

Naturally, the account of all the trends currently affecting the office rental market would be very long, and many are specific to the Czech market (which locations are considered attractive, as well as the eating habits of employees). In this chapter we are also ignoring "green certificates," which were discussed in earlier Trend Reports and would undoubtedly require a separate chapter.

Nevertheless, the above-mentioned trends require attention and will be the main determining factors of the coming period.

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