COLLIERS OUTLOOK

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SEOUL OFFICE MARKET OUTLOOK

Office vacancy rates will likely rise due to new supply in 2020, then stabilize downward

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Summary & Recommendations

After peaking in 2020, new supply should decline in 2021, providing an opportunity for tenants to secure the benefit of long-term lease contracts of five years or more before market conditions change.

The GBD area should keep the lowest vacancy among the three main districts thanks to firm demand and the success of Pangyo Techno Valley, a tech cluster near Seoul.

Flexible workspaces have expanded beyond the GBD, a region which IT ventures or start-ups prefer, and are now found in the CBD and YBD. In addition, as new supply increases in the CBD and the YBD, tenants should consider relocating their offices from the GBD to the CBD and YBD in 2020 to obtain better benefits like rent-free periods.

		Q4 2018	Full Year 2019	2018–23 Annual Average
Demand	> We do not expect a demand recovery in the traditional industries like manufacturing due to a slow economy in 2019. Meanwhile, demand from flexible workspace operators will probably increase.	101,964 sq m	287,000 sq m	208,000 sq m
Supply	> Over the next five years, we expect total new supply in prime areas to exceed 1.1 million sq m (12.3 million sq ft). The YBD submarket will likely see oversupply during the same period.	0 sq m	203,000 sq m	244,000 sq m

		QOQ / End Q4	YOY / End 2019	Annual Average Growth 2018–23 / End 2023
Rent	> We expect rental growth over the next few years to be marginal, increasing about 2% per annum on average, as most office buildings will likely adjust their rates in line with inflation.	0.3% KRW 27,712	1.4% KRW 28,101	2% KRW 30,272
Vacancy	> The overall Grade A vacancy rate will probably continue to increase due to new supply. We expect the vacancy to rise and peak in 2020 due to heavy new supply in the YBD, then to fall by the end of 2023.	-1.4pp 9.5%	0.4pp 9.9%	+0.3pp 11%

Note:
1. This table shows aggregate figures for the Seoul CBD, GBD, YBD.
2. USD1 to KRW 1,119 as of end-Q4 2018. 1 sq m = 10.76 sq ft
Source: Colliers International

Colliers INTERNATIONAL

CENTRAL BUSINESS DISTRICT

CBD

Vacancy rate reduced due to massive relocation activity

In Q4 2018, the CBD's vacancy rate decreased to 12.3% due to the large scale relocation demand, which increased in H2 compared to the first half of the year.

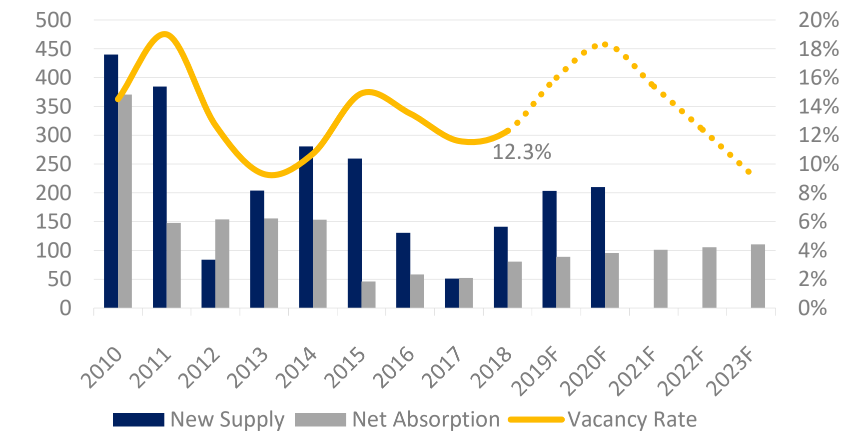
Notable tenant movements were centered on the Centropolis complex, including: Kumho Asiana Group's lease of six stories in Centropolis Building A, and SK Telecom's lease of three stories in Building B. These two transactions together accounted for a significant amount of the property's vacancy. Due to Kumho Group's massive relocation, their previously occupied area in the Concordian Building became available in Q1 of 2019. Law firm Shin & Kim also relocated to the Centropolis complex, moving out of Namsan State Tower to Centropolis complex Tower D.

In 2019, the Summit Tower and Seosomun 5 district project are scheduled to complete. Summit Tower is planned to supply 146,629 sq meters (1,577,728 sq feet) and is directly connected to the Euljiro 4-Ga Station. Daewoo E&C has planned to lease 60% of the total area, with the balance being used by BC Card. In addition, law firm Kim & Chang signed a contract to lease the entire Daewoo E&C building when its vacated.

The Seosomun project, which is planned to be finished in Q3 2019, has yet to secure any tenants. It will likely be the only new Grade A office building in 2019. Considering the vacated space that is coming available due to the large corporate relocations, the CBD's vacancy rate would likely increase when the Seosomun project is completed. However, since the Seosomun project is the only new supply and assuming absorption follows the recent trend, the vacancy rate will likely not escalate significantly in 2019. As Gateway Tower and SG Tower are scheduled to come online in 2020, the vacancy rate would likely increase annually through 2020.

As supply decreases after 2020 and the demand for flexible workspaces continues to expand, the CBD market should shift to a landlords' market. Therefore, the CBD's vacancy will likely continue to decline, but if Hana Financial Group decides to relocate their headquarters to Incheon, we expect that the CBD vacancy rate in 2022 will probably increase again.

CBD, supply & demand ('000 sq meters)



Source: Colliers International

CBD, future supply

Submarket	Property	Area (sqm)	Completion
CBD	Centropolis	141,471	Q3 2018
	Summit Tower (Sewoon 6-3)	146,629	Q1 2019
	Seosomun 5 district	38,235	Q3 2019
	Gateway Tower	84,823	Q2 2020
	SG Tower	125,367	Q2 2020
	Janggyo 12 district	N/A	N/A
	Total (2018-2020)	**536,545**	

Source: Colliers International

GANGNAM BUSINESS DISTRICT

GBD

Demand remains strong but space shortage in the long-term

In 2018, IT companies continued to prefer the Gangnam area and flexible workspace operators actively expanded their offices. We expect this trend to continue in 2019.

The GBD is becoming an increasingly competitive area for flexible work space operators, creating a barrier to entry for companies without a foothold in this market. For example, in the Q4 2018, Lotte Asset Development launched a new flexible workspace, *WorkFlex*, in Gangnam N Tower. Spark Plus opened its sixth location in Daelong Seocho Tower in the GBD area. Moreover, WeWork leased additional space in KG tower, which is located near Gangnam Station.

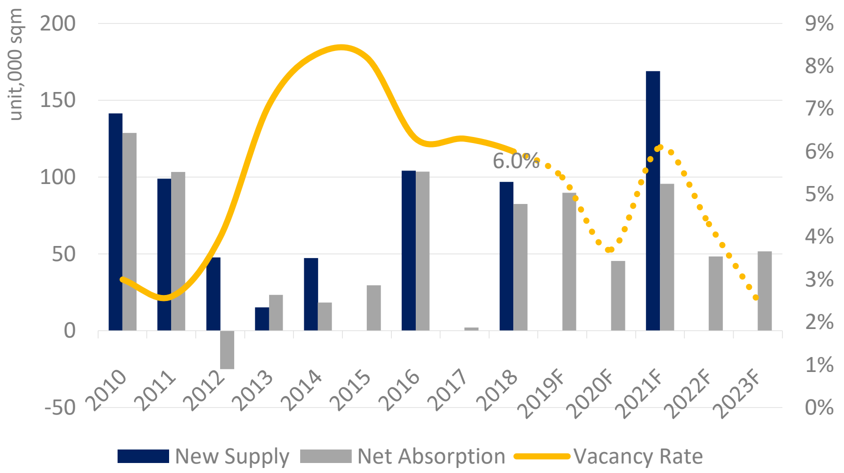
We expect competition between flexible workspace operators to intensify in the GBD area as current operators expand aggressively and new entrants continue to open.

Luceen tower and Gangnam N tower, coming online in H1 2018, saw demand, which helped push the vacancy rate in the GBD to a record low of 6% in Q4 2018, the lowest among the three submarkets. With flexible workspace operators' active expansion and IT companies' strong preference for offices in the GBD, we expect that tenants' demand for the GBD will likely continue growing.

Furthermore, the Renaissance Redevelopment site will probably be the only prime grade office supplied in the GBD area over the five years. Thus, we expect the GBD will probably be a stable market with limited office supply, propelled by strong demand from IT companies and flexible workspace operators.

Average rental rates in the GBD continue to rise, thanks to the active demand and limited supply, and the increased rents may push some tenants to other submarkets. In addition, as demand is spilling over from Pangyo (the sub-market south of Gangnam) into Gangnam, we expect Gangnam will likely be the most desirable investment market in Seoul.

GBD, supply & demand ('000 sq meters)



Source: Colliers International

GBD, future supply

Submarket	Property	Area (sqm)	Completion
	Luceen Tower	45,847	Q3 2018
	Gangnam N Tower	51,119	Q3 2018
GBD	Renaissance Redevelopment	168,956	Q1 2021
	Hyundai Motors Business Center	N/A	Q2 2023
	Total (2018-2020)	**265,889**	

Source: Colliers International

YEOUIDO BUSINESS DISTRICT

YBD

Influenced by large supply and redevelopment

In 2018, the YBD's vacancy rate rose to 22.3% due to the massive relocation of LG Group out of the submarket in H1 2018. But aggressive marketing of prime-grade buildings lowered the vacancy rate to 9.5% in Q4 and it continues to decrease.

Since prime-grade buildings like the IFC and FKI buildings are offering rent-free benefits, many corporates actively relocated from other submarkets to the YBD. For instance, according to *the bell* website and other industry news, Carrier leased 2 IFC in Q4 2018, and MERITZ Securities signed a lease for 3 IFC.

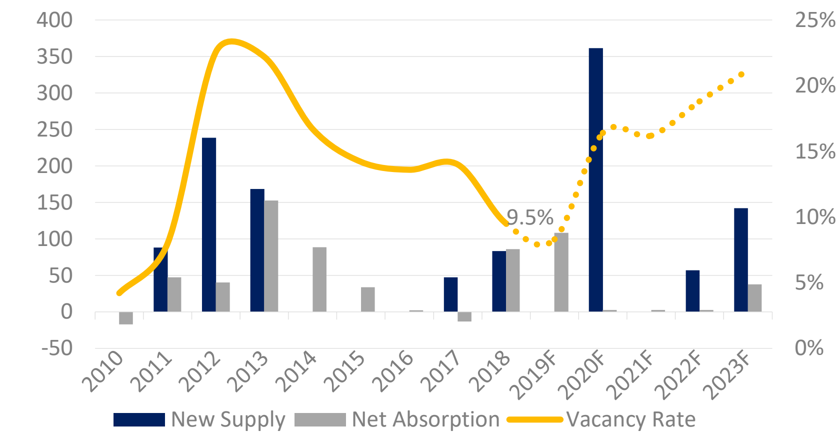
We expect that the vacancy rate in the YBD will probably be stable for a period of time, as the large vacant space in IFC and the FKI have been leased and the new office supply will likely slow in 2019.

However, we expect that Parc1, coming online in 2020 with 224,970 sq meters (2,420,677 sq feet) of office space, will likely increase the vacancy rate. This is despite POSCO E&C leasing about 57% of the building.

In 2022, the Yeouido MBC redevelopment site is scheduled to supply about 57,000 sq meters (613,320 sq feet) of office space. The reconstruction of the Teachers Pension office, scheduled for 2023, is planned to supply 142,087 sq meters (1,528,856 sq feet), with Teachers Pension signing a lease contract for space at FKI until then. When the reconstruction is completed, Teachers Pension is planning to lease 10% of the building as its headquarters, and the remaining area should be available on the market.

The YBD's vacancy rate will likely rise gradually to 19% through 2022, as 2020 is scheduled to see the largest quantity of new supply in the YBD submarket in the last 10 years. Thereafter, it will probably stabilize gradually. Although some space will likely be used as corporate headquarters, when new office buildings are completed and bring in corporate tenants, the YBD's vacancy rate will likely be increased.

YBD, supply & demand ('000 sq meters)



Source: Colliers International

YBD, future supply

Submarket	Property	Area (sqm)	Completion
YBD	KTCU	83,381	Q1 2018
	Parc 1	224,970	Q1 2020
	KB Financial Group	67,683	Q3 2020
	Post Office	67,698	Q3 2020
	MBC redevelopment	57,000	2022
	Teachers Pension office	142,087	2023
	Total (2018-2020)	**644,224**	

Source: Colliers International

CONCLUSION & STRATEGY

Traditional industry submarket preferences weakening

The traditional tendency of industries to cluster in specific submarkets is weakening. Previously, corporate conglomerates preferred the CBD, IT companies clustered in the GBD, while financial companies preferred the YBD. We expect only the YBD to have new supply in 2020, and other submarkets' new supply should decrease after 2021, pushing non-financial tenants into the YBD because of the new supply. In addition, the changing nature of business, propelled by improved IT infrastructure like fibre internet and flexible workspaces, will likely blur the distinction between each submarket's boundary. As flexible workspace operators expand to the CBD and YBD, many IT companies will likely lease space in the CBD and YBD rather than the GBD.

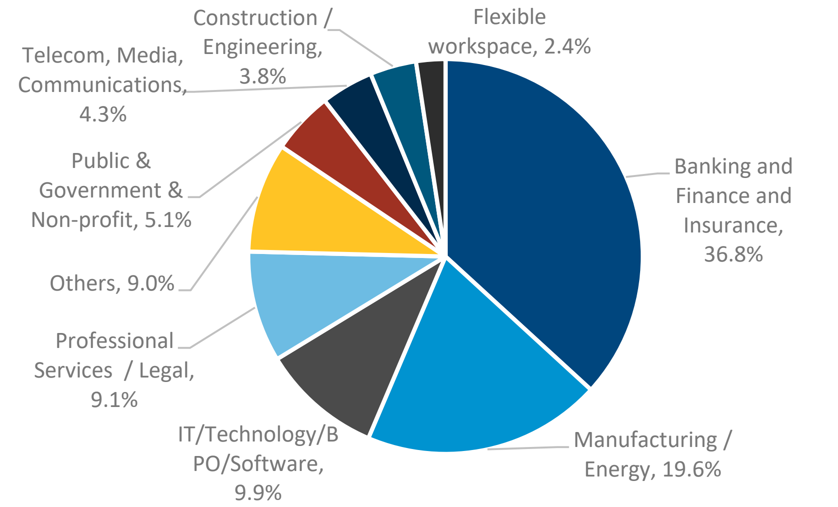
Impact of major financial headquarters' consolidation

The relocation of Hana Financial Group is likely to affect the Seoul office market. According to their plan, most of Hana Financial Group's affiliates plan to move to Cheongra International City in Incheon by 2022. In addition, the KB Financial Group and Korea Post's headquarters buildings are scheduled to be completed in 2020. As KB Financial Group plans to use the entire area for its headquarters, the branches scattered around Seoul are likely to be consolidated into the headquarters, which will increase the vacancy rate not only in the YBD but also in other submarkets as well.

2020 is an opportunity to relocate

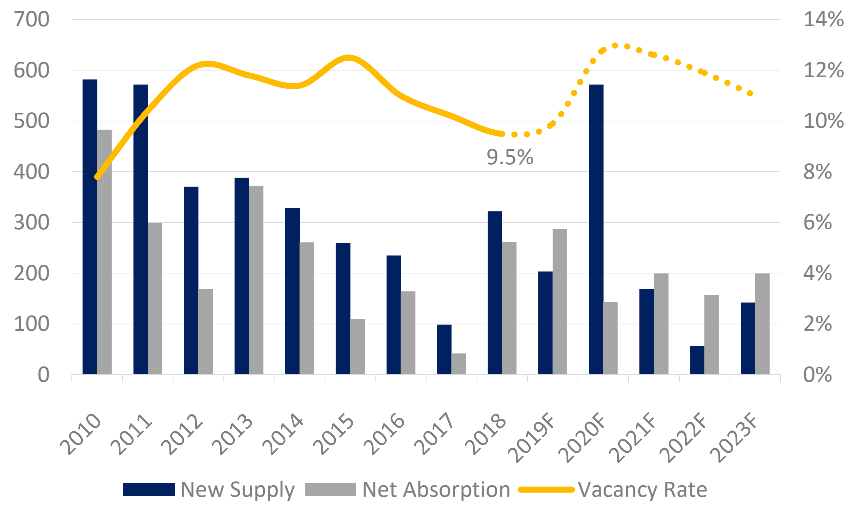
In 2019, the vacancy rate is likely to be stable due to the limited new supply, and rising with the large-scale supply in the YBD in 2020. After that, we expect the vacancy rate to decrease again due to increased flexible workspace demand and decreased office supply in the next five years. In Seoul, fluctuations in supply tend to effect vacancy more than demand. Spikes in Seoul's vacancy show a recurring pattern of declining rapidly over the following year as leasing progresses. Therefore, tenants should use increased new supply in 2020 to relocate their offices. Tenants should be able to get rent free benefits in 2020, in which year new supply will be concentrated.

Tenant distribution by industry



Source: Colliers International

Seoul, Grade A supply & demand forecast ('000 sq meters)



Source: Colliers International

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