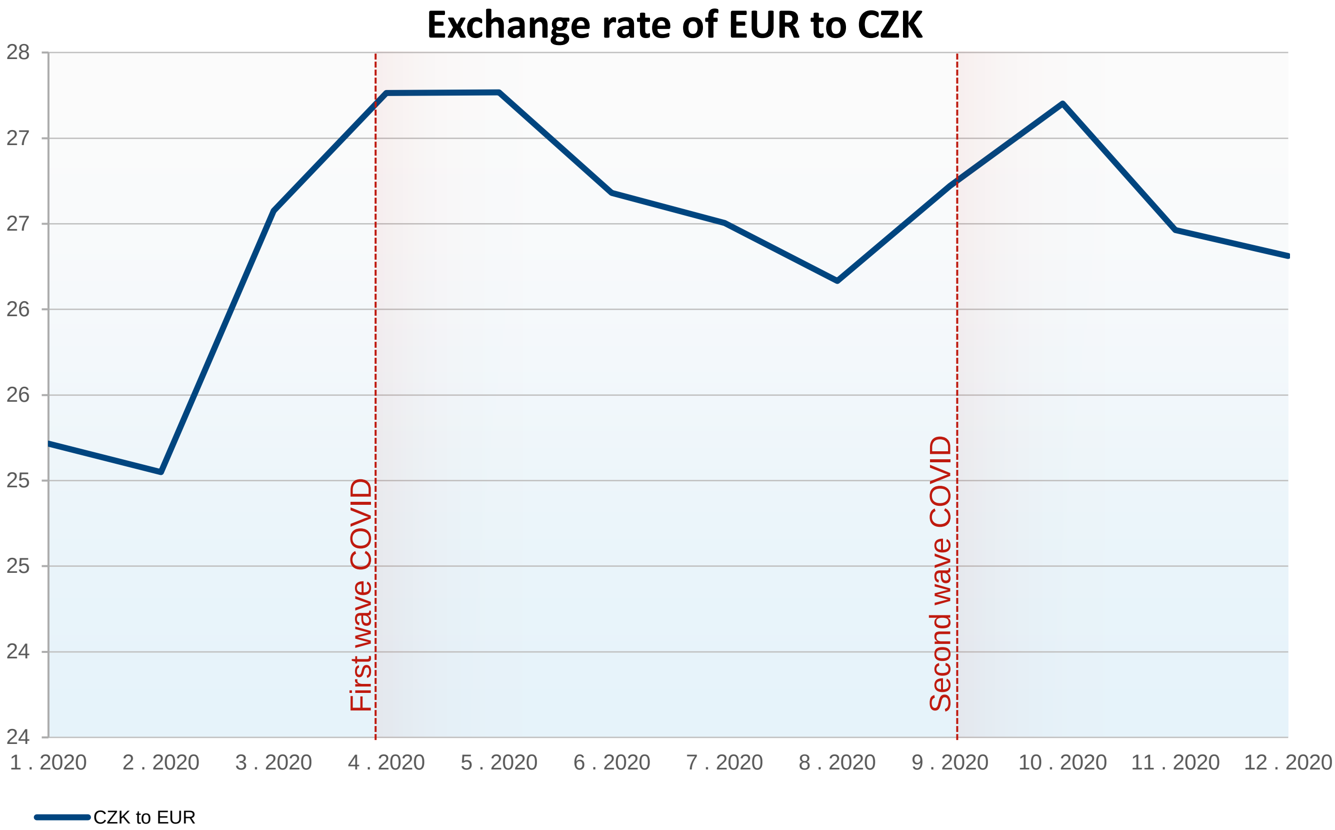
CZECH REPUBLIC

PRAGUE OFFICES

QUARTER 4 | 2020



MACROECONOMIC OVERVIEW

The Czech Republic is in a state of emergency from the first half of October until now. Although the first wave of COVID was managed well in the spring, the second wave is a completely different story. By the end of 2020, the Czech Republic has some of the worst numbers of new cases internationally. With the EU approval of new vaccines in late December, the government has begun distribution to the most endangered population groups and key medical staff. Shortly after this they outlined the first draft of vaccination plans, yet the details can change rapidly. GDP is expected to fall by almost 7% in 2020 and is expected to rise by 3.2% in 2021, mainly during the second half of the year.

Unemployment is rising slowly, but with a rate of 4% in December 2020, it was still one of the lowest in the EU. It is expected that the unemployment rate will continue to increase, mainly as a result of the impact on the travel, hospitality and food and beverage sectors.

The Government budget for 2020 ended in deficit by approximately 367 billion CZK. A similar scenario is already approved for 2021 with a planned deficit of 320 billion CZK. The result of 2020 is the worst deficit in Czech history, almost doubling the deficit from 2009 and the GFC. The forecasted development of inflation is currently stable between 2% and 3% for 2021. Rates from the Czech national bank have been kept at minimal levels since May 2020. As for the residential market, in contrary to public belief, mortgage rates fell under 2.0% during 2020 and these extremely cheap loans are currently encouraging clients to invest in the residential sector, despite the continued strong increase in pricing. A record total volume of approved mortgages in 2020 is only proof of this trend.

FIGURE 1: **Czech GDP compared to Eurozone**

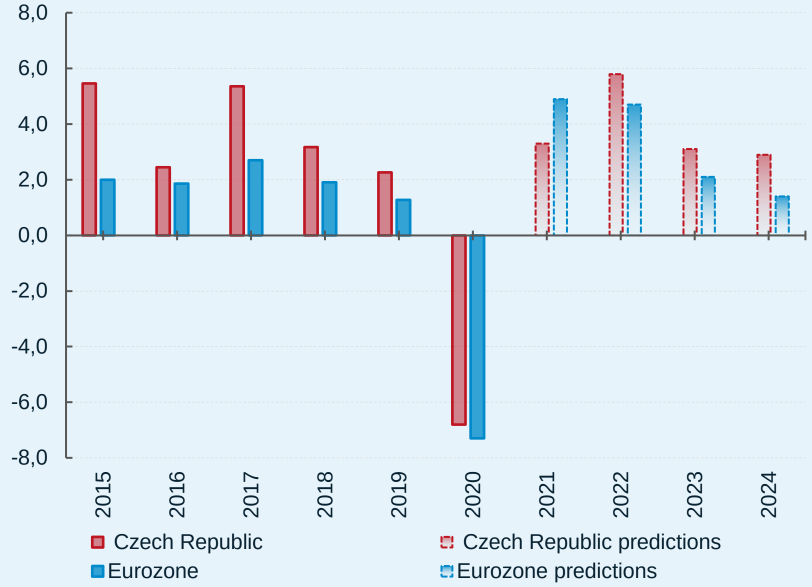


FIGURE 2: ***Unemployment rate***

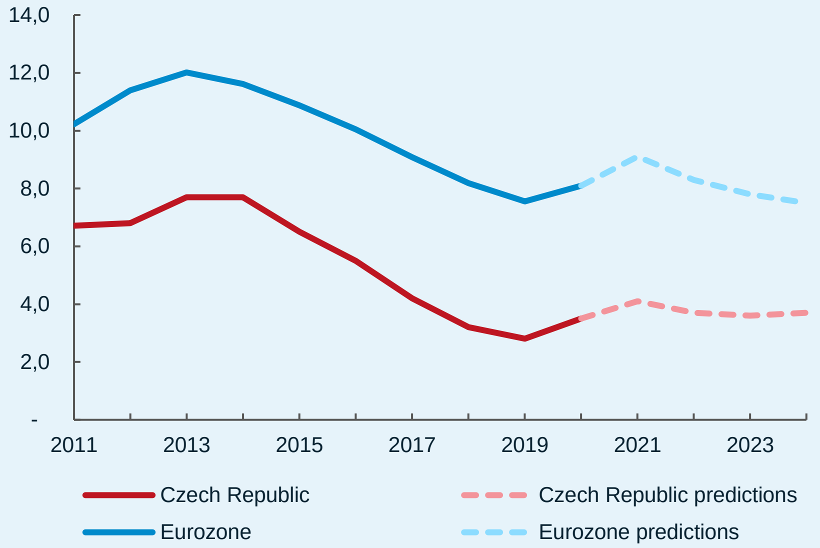
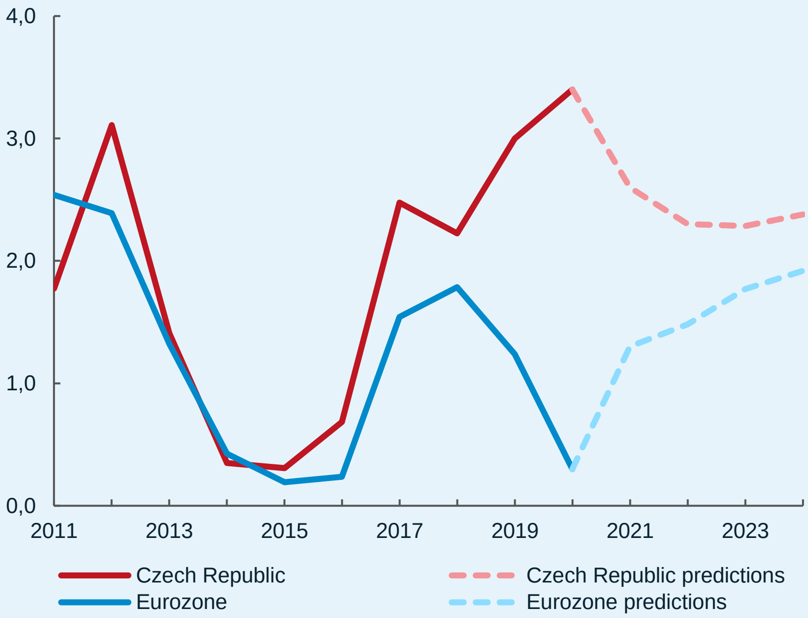


FIGURE 3: **Consumer Price Index**



Sources: Figure 1: Oxford Economics, Colliers International | Figure 2: Colliers International, Oxford Economics | Figure 3: Colliers International, Oxford Economics

STOCK & DEMAND

Stock & Vacancy

2020 will be remembered for many years to come as a game changing year. We were all tested in wide range of new situations, either personal or work related. In relation to the commercial real estate sector, the Prague office market also encountered many new situations but, due to its strong fundamentals, managed to pass through 2020 with relatively minor scratches.

During Q4 2020, only one new development was completed and added 19,700 sq m to the market, bringing the total modern office stock to 3.75 million sq m. The most recent addition is Bubenská 1, an historically protected landmark building in Prague 7. The building underwent an extensive refurbishment and is now the home of several international tenants. Some smaller developments, originally planned for Q4, such as Holečkova 26 in Prague 5 and Hybernská 1 in Prague 1, were rescheduled and will be completed during early 2021.

Total supply for 2020 reached 150,500 sq m. This is a slightly lower volume compared to last three years, but still above the 10-year average thanks to a strong second quarter when almost 90,000 sq m was delivered. Looking at the current pipeline of buildings under construction and due for delivery in 2021 and 2022, there is likely to be a significant drop compared to recent years or either 5-year or 10-year averages. A total of ca. 136,000 sqm is due in this period and ca. 30% of that space has already been secured by a tenant.

The vacancy rate throughout the city remained at almost the same level as in the previous quarter. Total vacant offices represent approximately 261,500 sq m, or 7.0% of the total modern office stock. This is a 150-bps increase YoY.

As the trend of subleases continues, we have registered approximately 71,700 sq m of immediately available subleases throughout the office market. This could be represented as additional 1.9% of “grey” vacancy to the number mentioned earlier. Another 13,400 sq m should become available in the upcoming months, but conditions or the approach of current tenants can alter. Subleases vary strongly in available sizes, fit-out levels or simply in the asking rent approach, as we register offers from €10 to €18 per sq m for A class premises.

Demand

Gross take-up increased to 98,700 sq m in the fourth quarter representing a growth of almost 18% QoQ. Net take-up represents 44% of this volume. Compared with last quarter, we registered increased activity in pre-leases and also in new leases. Still, renegotiations took the largest share with 51%, representing office area of approximately 51,000 sq m.

Annual gross take-up reached 332,800 sq m. This is a decrease of 24% in overall leasing activity compared to 2019. Annual net take-up totalled 167,300 sq m, down by 36% compared to the previous year.

The major transactions of the fourth quarter of 2020 were all renegotiations including: Internet Mall (6,300 sq m) in Gen in Prague 7, Havel & Partners (5,200 sq m) in Florentinum in Prague 1 and NET4GAS (4,800 sq m) in Kavčí Hory Office Park in Prague 4. The largest new occupation was TNT/Fedex (3,800 sq m) in Kotelna Park II in Prague 5. One positive sign is the aforementioned increase in share of pre-construction deals on total take-up. Developer Crestyl managed to secure over 7,000 sq m for their project Hagibor through pre-leases, which will contribute towards the commencement of construction.

RENTS & OUTLOOK

Rents

A similar trend is happening in neighbouring CEE markets as rents come under downward pressure. Current prime headline rents decreased slightly to range between €22.00 and €22.50 in the city centre. Landlords who suffer with larger vacancies in their properties are trying to offer more generous incentives. Inner city and outer city rental levels remained stable between €15.50 and €17.00 and €13.50 and €15.00 respectively.

Outlook

As the government continues to prolong the state of emergency and any significant easing of pandemic countermeasures is out of sight, we all have to adapt to this new normal. 2021 will definitely bring only 5-digit supply of new offices and we have to still bear in mind that some projects under construction could still be postponed, especially the ones scheduled for late 2021. Several projects are expected to commence speculative construction soon, for example PORT7 by Skanska, however most of the developers are currently working on securing pre-leases for their current pipelines before starting the building process. Although we expect to see the vacancy rate rise by some additional basis points, the lower levels of supply will soften the speed of this increase. Larger tenants with floor space requirements in the thousands of square meters, should certainly start to look at their options even sooner than in past years, as pre-leasing and the demand for new, smart, contactless and safe office buildings will become more common.

FIGURE 1: **Modern office stock & vacancy in Prague districts (sq m thousands)**

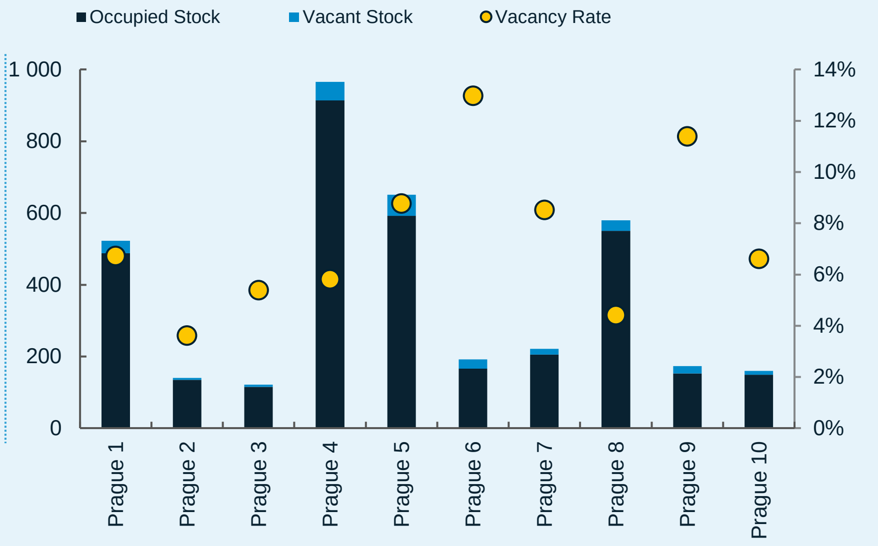


FIGURE 2: **Vacancy rate development & forecast**

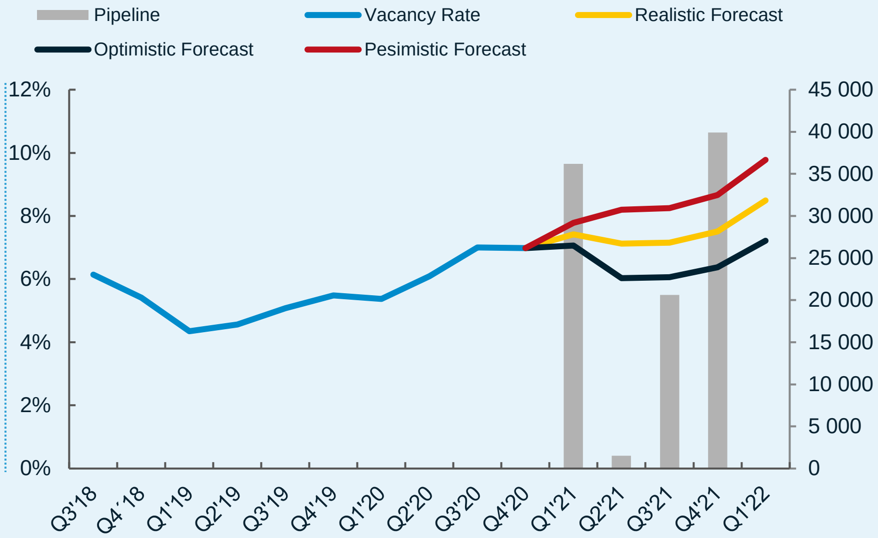
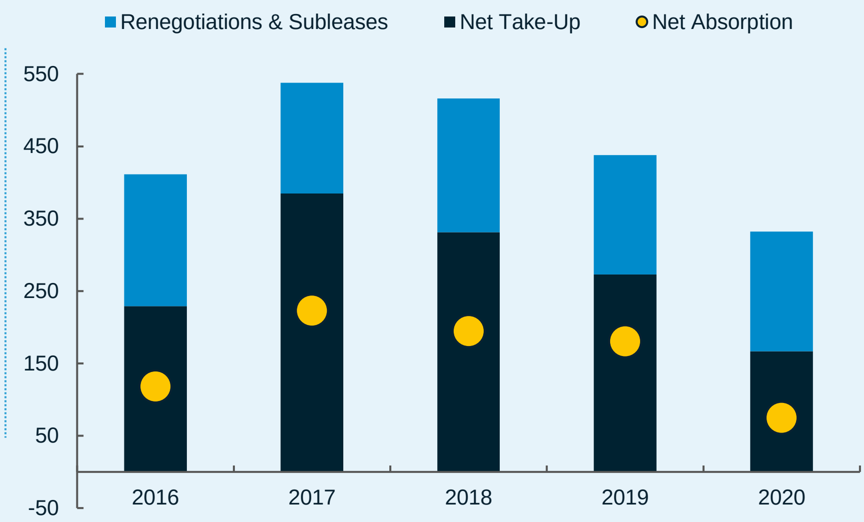


FIGURE 3: **Take-up and net absorption (sq m thousands)**



Note: Net absorption represents total change in occupied stock and as such can be also negative

Sources: Figure 1 to 3: Prague Research Forum (PRF), Colliers International

FOR MORE INFORMATION

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