



CZECH REPUBLIC

MARKET OVERVIEW

QUARTER 3 | 2019



INVESTMENT MARKET

Q3 2019 Overview

With €574 million transacted in the third quarter of 2019, the year to date investment volume reached €2.4 billion, which is almost equal to the full year results from 2018.

The largest transaction of the quarter was the purchase of Drn for more than €100 million. It was the first investment of German KGAL Group in Czechia. Other significant transactions in Q3 included the purchase of Blox by Českomoravská nemovitostní for €85 million and Palmovka Open Park (now My Hive Palmovka) by Immofinanz for €80 million.

Czech capital dominated the investment volumes in the first nine months of the year, with a share of 37%. South Korean capital remained in second place with a market share of 21%, despite not closing a single

transaction during Q3. The Germans have increased their market share from 6% in mid-year to the current 12% after closing two significant transactions in Q3 (the above-mentioned purchase of Drn and the purchase of River Garden I by HIH group, another new name on the local market).

Whilst there is reasonably healthy new supply in both the office and I&L sectors, unlike the office sector, a significant % of the I&L sector is retained by the developers/operators on completion. As a result, the office sector continues to dominate investment volumes with a 53% share. Both industrial and retail (where new developments are limited) remain subdued, and thus the second strongest sector in the first three quarters of 2019 was hotels with a share of 18%.

OUTLOOK

Despite the current pipeline of more than 50 transactions, the amount of capital targeting the real estate sector far exceeds the supply of suitable properties for sale. Whilst retail is generally not considered the most attractive sector at present due to structural changes, its also noteworthy that the development of new shopping centres is virtually non-existent and the majority of the market is limited to mainly second hand properties. Prime retail opportunities are scarce.

In the last quarter of the year we still expect to see transactions in excess of €500 million being closed, which would bring the total investment volume to €3 billion and make it the third strongest year in the history of the market.

Whilst yields are now at a cyclical low, the demand for prime office properties could well drive further yield compression below the current 4.25%.



With expectations of a “lower for longer” interest rate environment in Europe and benchmark prime office yields in Germany now well into “the 2’s”, we expect that yield compression in Czechia will continue



Andy Thompson | Head of Investment, Czech Republic & Slovakia

FIGURE 4: INVESTMENT VOLUMES IN THE CZECH REPUBLIC (€ millions)

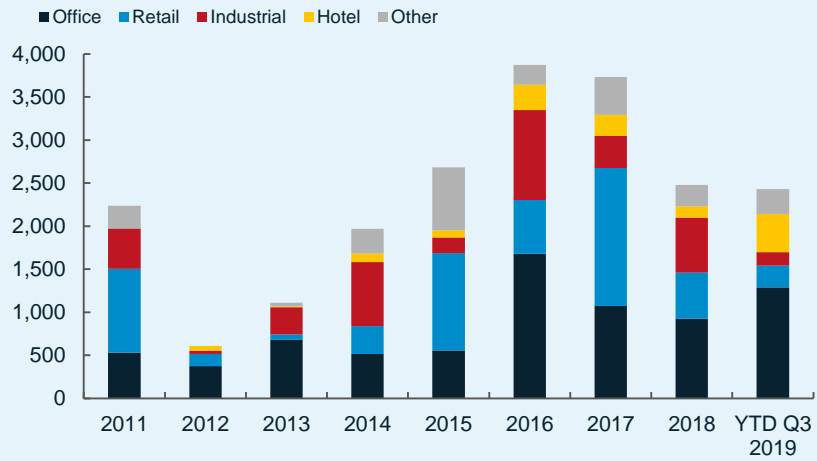


FIGURE 5: INVESTMENT SHARE PER COUNTRY ORIGIN OF BUYERS AND VENDORS – SEPTEMBER YEAR TO DATE

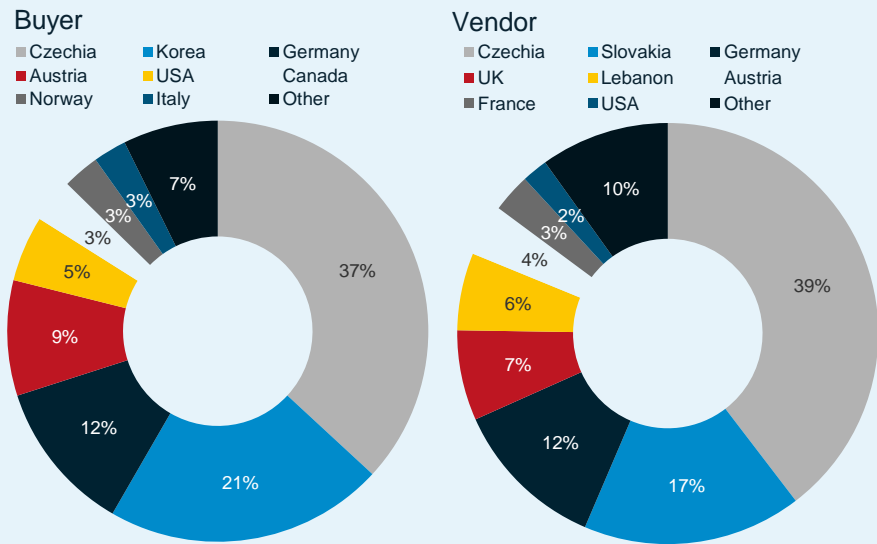
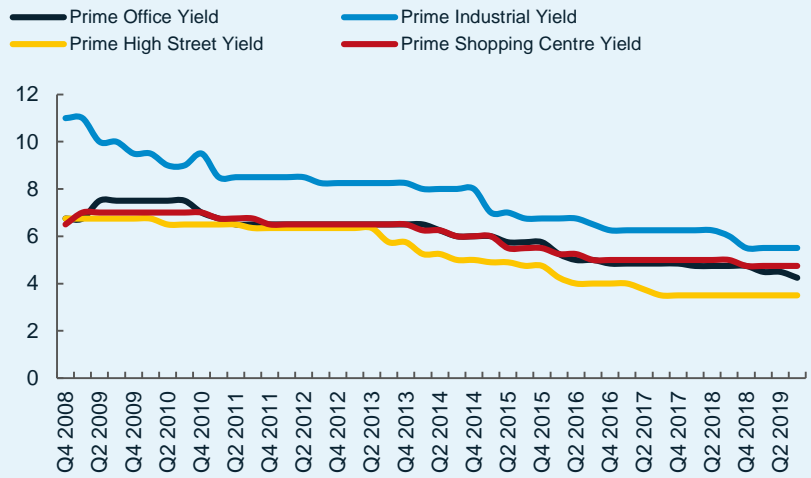


FIGURE 6: PRIME YIELDS (%)



Sources: Figures 4-6: Colliers International

OFFICE MARKET

Supply & Vacancy

In Q3 2019, the total office stock in Prague reached 3.59 million sq m with some 112,900 sq m added during the year, of which 32,900 sq m was during third quarter.

Completions include two new and one refurbished property: Dock In Three in Prague 8 (16,000 sq m), Argentinská Office Building in Prague 7 (5,800 sq m) and the refurbished Life Building C in Prague 4 (11,100 sq m). Unlike in previous quarters, more than 50% of the newly delivered space was vacant at the end of September, which is one of the reasons behind the further overall vacancy increase to 5.1% by the quarter end. This represents some 182,600 sq m of offices available for lease, up by 20,000 sq m compared to previous quarter.

Demand

Gross take-up in Q3 2019 reached 85,200 sq m. Cumulatively, for the first three quarters of the year it reached 299,300, down 16% year on year. Cumulative net take-up was 192,700 sq m, down by 18% year on year.

Quarterly net absorption in Q3 reached 9,100 sq m, cumulatively for Q1-Q3 2019 126,500 sq m and remains positive, although there is an apparent slow down. In fact, net absorption was the lowest recorded since Q1 2015, when it reached negative figures.

The growth of flexible work space is encouraging companies to explore this option when, for example, they need to expand rapidly and in a short timeframe due to special projects. We expect to see this trend continue over the coming years.

RENTS & OUTLOOK

Rents

Prime office rents in the City Centre of Prague stand in the range of €22.50-€23.00, Inner City prime rent is at €15.00-€17.00 and Outer City prime rent at €13.50-€15.00. The further minor prime rental growth is being driven by the overall low vacancy levels across the city. We expect the prime rent growth to also affect secondary rents across the city.

Outlook

By quarter-end, some 315,600 sq m of office space was under construction or refurbishment in Prague. Three new properties commenced in Q3: two new buildings in River City Prague office park by CA Immo – Mississippi House (13,300 sq m) and Missouri Park (7,400 sq m)

in Prague 8 and a refurbishment of Sixty House (5,500 sq m) In Prague 4. All three projects are currently being built on a speculative basis. However, of the space under construction, 35% is already pre-let to tenants.

Some 28% of the space is still due for delivery in 2019 and 57% will be completed during 2020. The remaining space will be delivered in 2021.

Based on the absorption rate over the last 10 years and the current pipeline under construction, our internal forecast indicates only mild growth in vacancy over the next two years. This should help the market move to a slightly more balanced position and remove the pressure on further rental growth.

FIGURE 7: MODERN OFFICE STOCK & VACANCY IN PRAGUE DISTRICTS (sq m thousands)

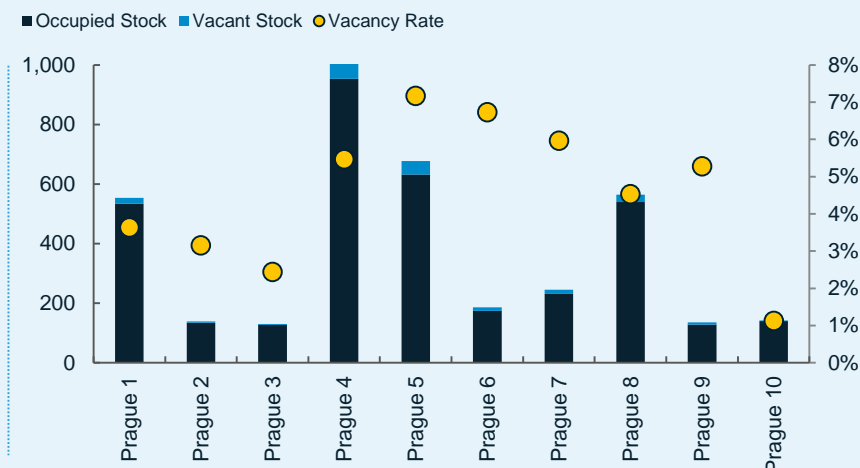


FIGURE 8: VACANCY RATE DEVELOPMENT & FORECAST

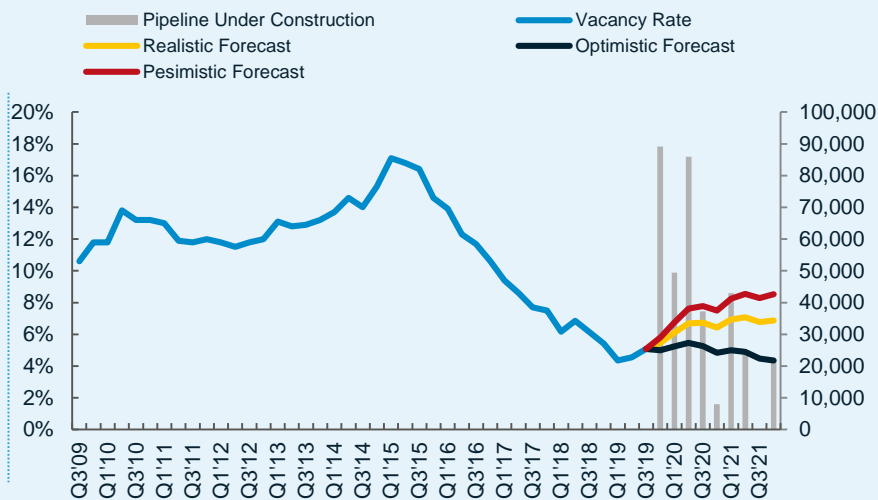
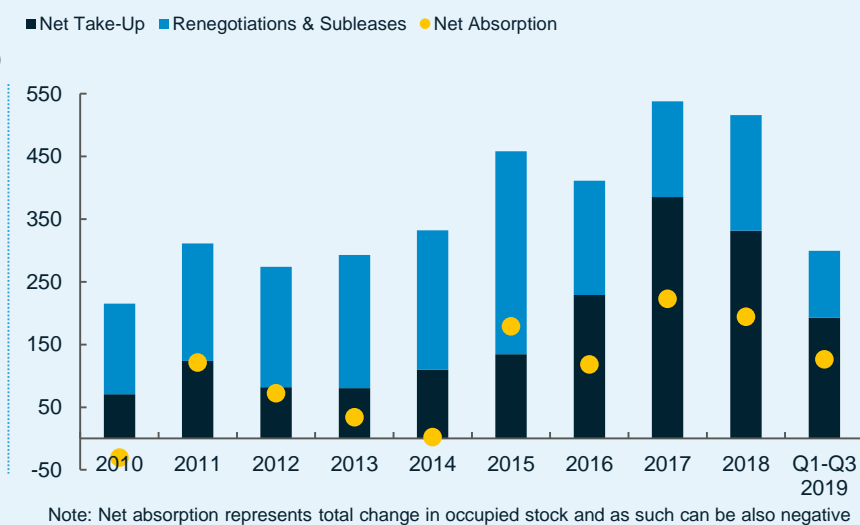


FIGURE 9: TAKE-UP AND NET ABSORPTION (sq m thousands)



INDUSTRIAL MARKET

Supply & Vacancy

With 149,000 sq m of newly completed warehouse space in Q3 2019, the total stock in the Czech Republic reached 8.2 million sq_m. Completed space comprises 12 new buildings across the country, with one quarter of the space completed in the Greater Prague region. The Ústí nad Labem region saw the completion of 16% of the new space, Central Bohemia and Olomouc region both received 15%.

Year to date completions reached 423,500 sq m, with the largest share in the Moravia-Silesia region (24%), despite zero completions in Q3.

Overall vacancy stood at 4.2%, which was 24 basis points lower than in Q2 and 20 basis points higher than in Q3 2018. The total available space reached 343,700 sq_m. Despite this seemingly high number, the availability of larger space is worse than in previous quarters, with only seven properties offering space in excess of 10,000 sq m. Combined with the low average vacancy rate it

creates an ideal environment for build-to-suit development, depending on the availability of land and permits.

Demand

Gross take-up in Q3 reached 365,000 sq m, registering a 5% decrease on the previous quarter, but a 14% increase year on year. Cumulative take-up, Q1-Q3, reached 1.125 million sq m, up 8% year on year, showing a robust Industrial market.

Net take-up reached 231,300 sq m, 11% up q-o-q and 22% up y-o-y. Cumulatively, the Q1-Q3 net take-up was 17% higher year on year.

The share of renegotiations on total gross take-up for the first three quarters is at 37% and we do not foresee any significant changes. That is due to both the relatively low vacancy and also the situation on the labour market, where companies prefer to stay in established locations rather than facing the issues of hiring new staff when the countrywide unemployment rate is below 3.0%.

RENTS & OUTLOOK

Rents

Prime industrial rents in Prague and Brno stand in the range of €4.25-€4.70/sq m/month. Other in demand regions such as Ostrava, Plzeň and Ústí nad Labem have rents in the range €4.00-€4.35/sqm/month. The previously common incentives of one month rent free per year of lease is no longer the standard and the developers now provide incentives based on location, lease size and length and also on the tenant profile.

Outlook

Around 523,900 sq m of warehouse space was under construction by the end of Q3, which is 56,200 sq m

more than in Q2. The pre-lease level on the space under construction exceeds 52% on average, which is in line with our expectations. Due to the continued situation with low vacancy, we do not expect this trend to change.

In Q4, more than 214,700 sq m is due to be delivered to the market. That would bring the total annual completions close to 700,000 sq m, making it one of the most active years in the market's history in terms of new space construction and cementing Czech Republic as one of the most sought after countries within Europe.

FIGURE 10: CZECH INDUSTRIAL STOCK & VACANCY (in sq m thousands)

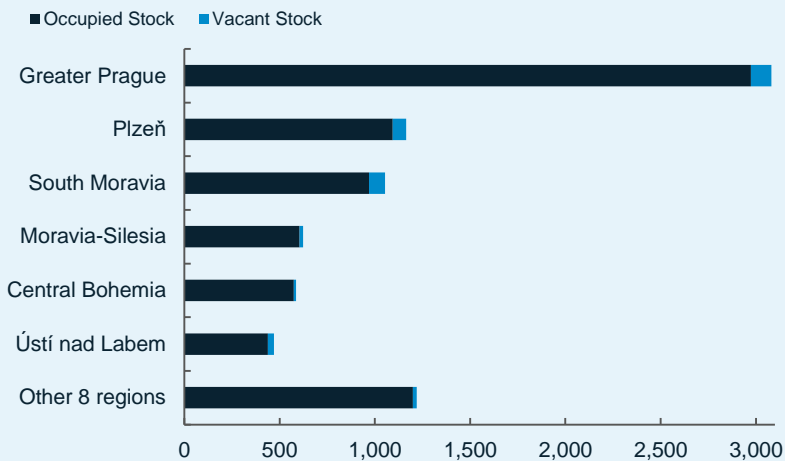


FIGURE 11: ANNUAL SUPPLY (sq m thousands)

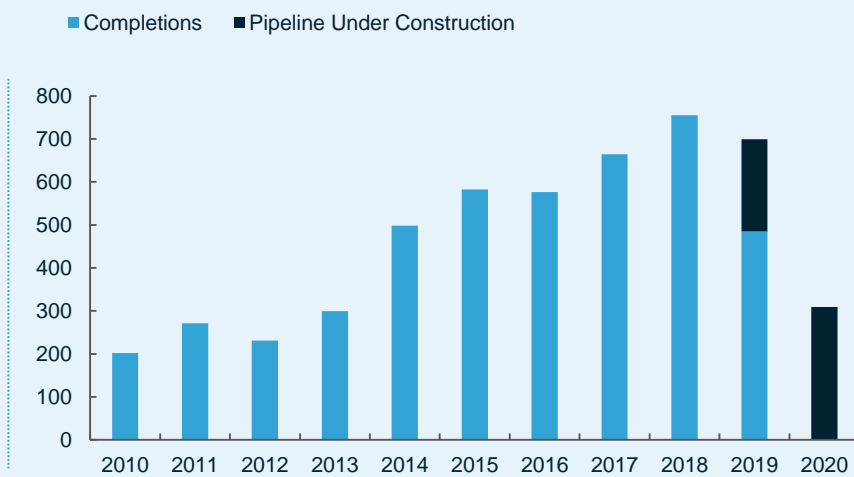
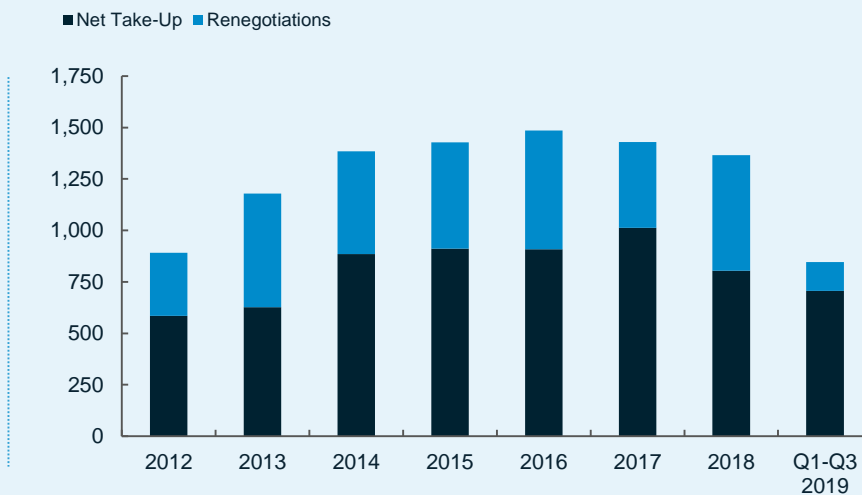


FIGURE 12: TAKE-UP (sq m thousands)



Sources: Figures 10-12: Industrial Research Forum, Colliers International

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