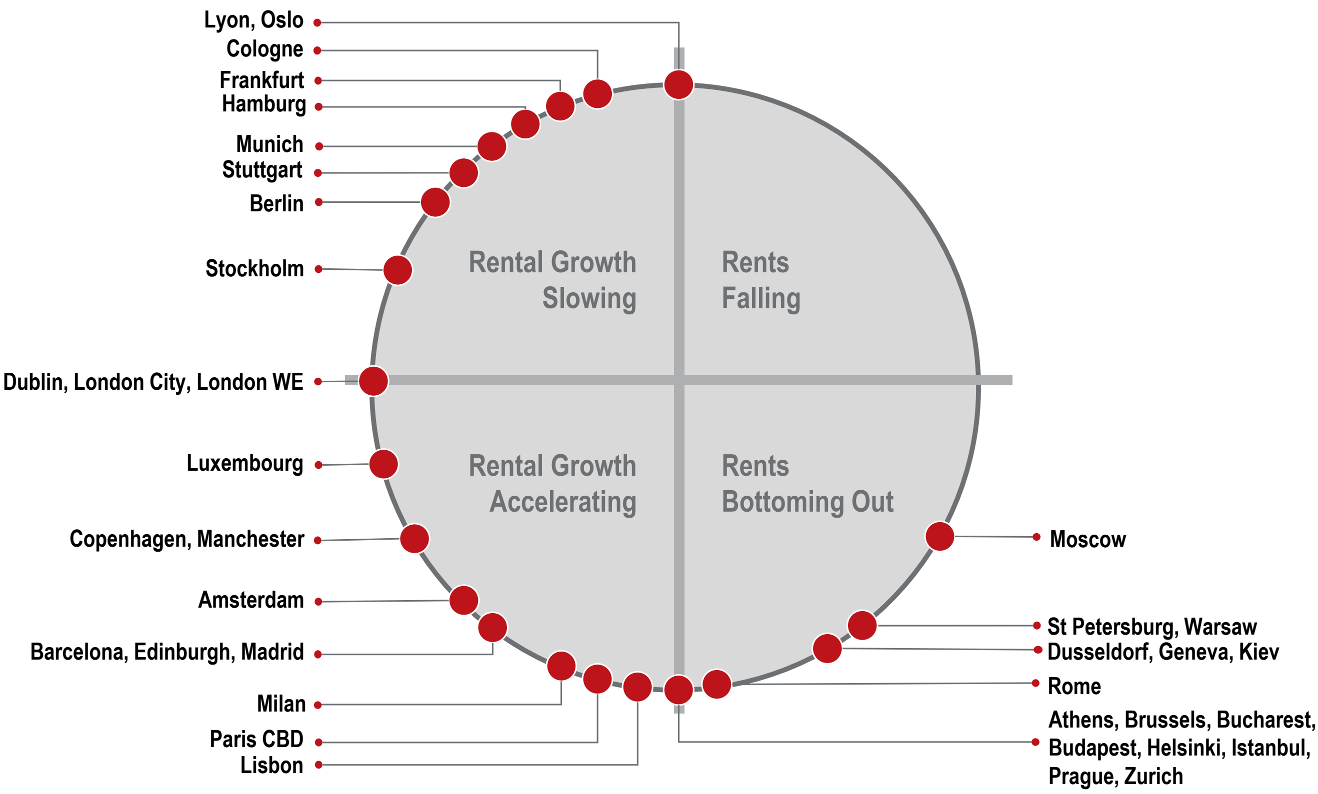
JLL Office Property Clock Q3 2015

EMEA Offices Research

European office leasing accelerates in Q3

- Office leasing activity up 29% y-o-y and the strongest Q3 on record.
- European leasing volumes boosted by a bounce back in activity in Paris, where Q3 take-up was up 39% y-o-y.
- Office Rental Index up by 1.2% q-o-q as prime rents increase in six markets.
- European office vacancy rate declined by 20bps to 9.1%.



Source: JLL, October 2015

The clock diagram illustrates where Jones Lang LaSalle estimates each prime office market is within its individual rental cycle as at end of September 2015. Markets can move around the clock at different speeds and directions. The diagram is a convenient method of comparing the relative position of markets in their rental cycle. Their position is not necessarily representative of investment or development market prospects. Their position refers to prime face rental values. Markets with a “step pattern” of rental growth do not tend to follow conventional cycles and are likely to move between the “hours” of 9 and 12 o’clock only, with 9 o’clock representing a jump in rental levels following a period of stability.

European Office Occupier Markets

European office occupier markets showed increased activity as sentiment continued to improve on the back of a steady recovery in the Eurozone economy and relatively healthy prospects. While individual markets continue to show a mixed picture, with cities moving at very different speeds, the overall direction is up, with leasing volumes increasing significantly in Q3 after a more subdued H1.

Office rents

The European Office Index rose by 1.2% q-o-q in Q3, following more modest growth in Q2 (+0.3%). Rental increases continues to be concentrated in a few major markets. Indeed off the 24 index markets, six saw q-o-q rental increases (compared with seven in Q2 2015). Excluding Moscow (where currency volatility has significant impacted rents), Europe recorded a y-o-y rental increase of 3.1% in Q3, the strongest rate since Q4 2014.

The main driver causing this acceleration was increases in rents in the larger European markets, including Paris and London. Paris, which recorded two consecutive quarters of rental decline in H1 2015, experienced a turnaround, with prime rents up by 2.8% in Q3 on the back of a gradual, but solid, demand side recovery. In London, robust occupier demand combined with an exceptionally tight supply side, forced prime rents up in both the City and the West End. Both now stand at 09:00 representing very strong rental growth. Looking ahead, there are no signs of rents levelling out, with strong growth forecast to continue in 2016-17.

Dublin again topped the rental growth chart in Q3, with prime rents increasing by 10% q-o-q. However, Dublin is not operating in normal market circumstances, with rental growth accelerated by the severe shortage of quality office space. Supply now stands at its lowest level in 15 years and 2016 will be the sixth consecutive year that no new office buildings will be delivered. Elsewhere in Europe, the robust recovery in Spain translated into the fourth consecutive quarter of rental growth in Barcelona (+2.6%q-o-q), while Madrid recorded its sixth consecutive rise at 1.9% q-o-q.

Office demand

European office leasing volumes continued to strengthen in Q3, with take-up totalling just over 3 million sq. m. This represents a 29% increase on Q3 2014 and is the strongest Q3 take-up figure on record. We expect a strong end to the year, with total European take-up forecast to reach around 11.5 million sq. m, up 8% on 2014.

European take-up was boosted by a bounce back in activity in Paris, which had dragged down the aggregate numbers in H1. The occupier recovery in Paris is gaining momentum with a 39% y-o-y increase in take-up in Q3 and should continue to do so over the next 12 months with the improving economic outlook.

Meanwhile, the German office market moves from strength to strength, with most of the largest markets reporting an increase in take-up against healthy Q3 2014 figures. Hamburg was the sole market showing a decrease in take-up (-37% y-o-y). The combined 775,000 sq. m transacted in Q3 across Germany is the highest Q3 since 2006. Next year should see a continuation of this, although the annual growth rate may slow from recent highs. The robust demand-side has consistently put German office markets on the growth side of the office clock. With the exception of Dusseldorf, the largest German office markets have moved past 6 o'clock and consistently recorded growth over recent years. Indeed, Berlin, Cologne, Hamburg, Stuttgart and Munich have been placed along the growth trajectory (6:15 – 11:45) since Q2 2011.

Other noteworthy demand trends in Q3 were continued strong growth in Spain (Barcelona +135% and Madrid +74% y-o-y) and early indications of a recovery in Moscow. Elsewhere in Europe, sentiment was largely positive as well, with 17 out of the 24 largest European office markets recording an increase on Q3 2014. While y-o-y comparisons with a strong Q4 2014 may be less flattering, we anticipate a strong finish to the year. Next year should see further acceleration, as more and more markets revive on the back of improving sentiment and employment creation.

We do anticipate the multi-speed environment, which has defined the offices landscape over the last few years, to continue at least in the short term, although it will be less about different directions of growth and more about markets performing at a very different pace.

Office supply

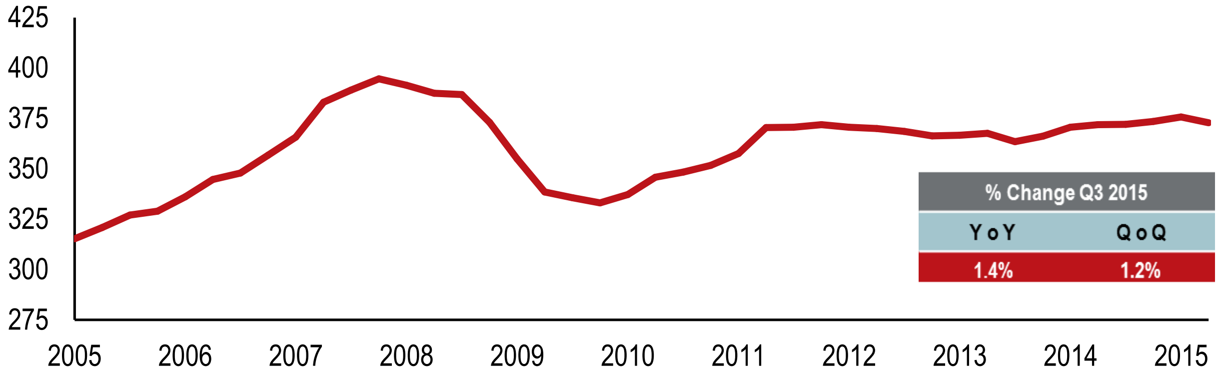
Most European office markets recorded a decline in vacancy rates in Q3, with just Luxembourg, Rotterdam and The Hague rising.

Total vacancy dropped by 20 bps over the quarter to 9.1%. While some of this can be attributed to strengthening demand, office completion levels have also fallen this year, totalling just 2.6 million sq. m (down 25% on Q1-Q3 2014). With an additional 2.5 million sq. m scheduled to be delivered by the end of this year (some of which may potentially slip into 2016), vacancy is likely to edge up marginally in Q4.

While the overall vacancy rate is still well above the previous peak (of 7.1% in Q2 2008), Grade A vacancy rates have dropped close to record lows in many markets, including London, Dublin, Munich, Hamburg and Berlin. A lack of the best quality space in particular has supported rental growth in these cities.

Overall we expect that the strengthening of the occupier market and a lack of speculative completions will further squeeze already-tight office markets across Europe in 2016.

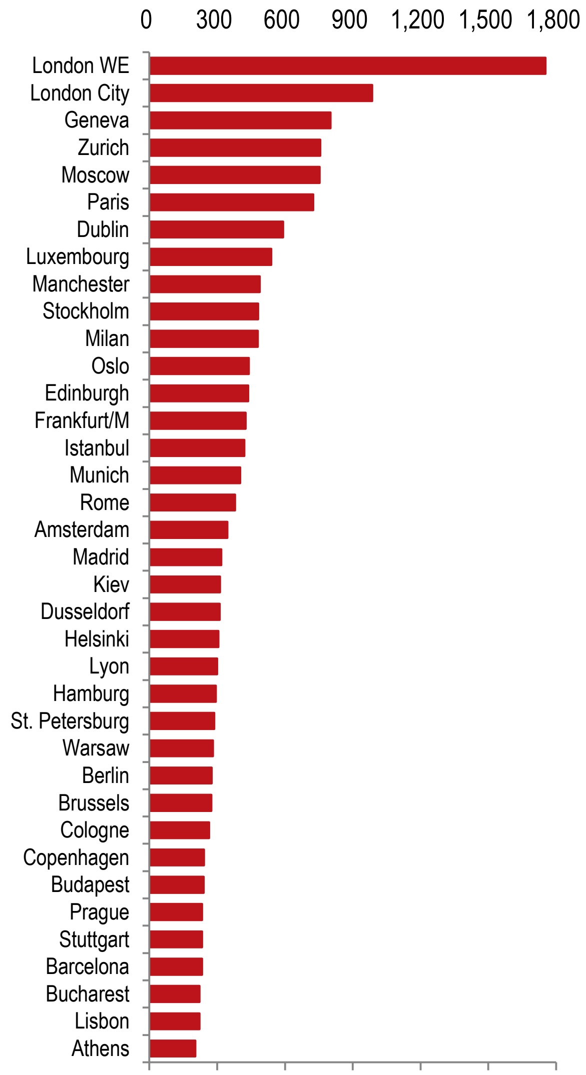
Prime European Office Rental Index



% Change Q3 2015	
YoY	QoQ
1.4%	1.2%

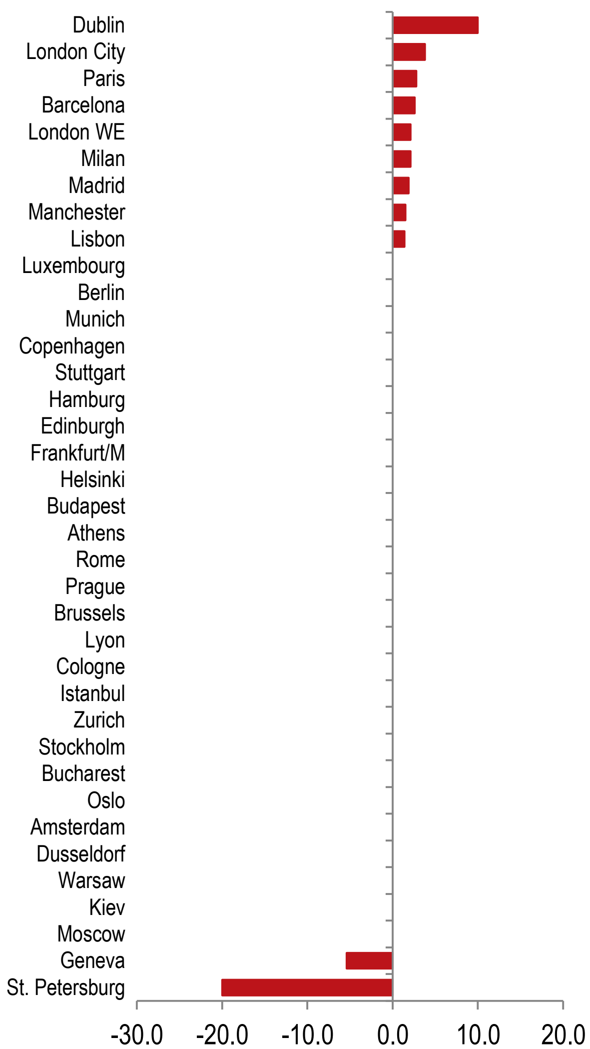
Weighted Nominal Rental Trend, 1980 = 100
Source: JLL, October 2015

Prime Office Rents Q3 2015 (EUR / sq. m pa)



Source: JLL, October 2015

Prime Office Rental Change Q3 2015 (% Q-o-Q)



Note: Q-o-Q rental change is based on the local currency.
Source: JLL October 2015

Definitions

Prime Rent

Represents the top open-market rent that could be expected for a notional office unit of the highest quality and specification in the best location in a market, as at the survey date. The rent quoted normally reflects prime units of over 500 m² of lettable floor space, which excludes rents that represent a premium level paid for a small quantity of space. The Prime Rent reflects an occupational lease that is standard for the local market. It is a face rent that does not reflect the financial impact of tenant incentives, and excludes service charges and local taxes. The Prime Rent represents Jones Lang LaSalle's market view and is based on an analysis/review of actual transactions for prime office space, excluding any unrepresentative deals. Where an insufficient number of deals have been made for prime office space, an assessment of rental value is provided by reference to transactions generally in that market adjusted accordingly to equate to prime.

Take up

Take-up represents floor space acquired within a market for occupation during the survey period (normally three-monthly). A unit is registered as taken-up when a legally-binding agreement to acquire the unit has been completed. Take-up includes floor space leased and sold for occupation, and the pre-lettings of floor space in course of development or prior to the start of construction.

Annual Net-Absorption

Represents the change in the occupied stock within a market during one year. Net Absorption is calculated on the basis of "top-down" estimates of occupied stock derived by subtracting vacant office stock from the total office stock of that market. Mothballed stock, i.e. floor space held vacant and not being offered for letting, usually pending redevelopment or refurbishment, is excluded

Vacancy Rate

The Vacancy Rate represents immediately vacant office floor space, inclusive sub-lettings, in all completed buildings within a market as at the survey date (normally at the end of each quarter period), expressed as a percentage of the total stock.

Completions

Completions represent floor space completed during the survey period (normally annually and projected forward by three years) within a market. Completions include both new development and refurbished accommodation that has been substantially modernised. An office is regarded as complete when the developer will undertake no further work until a tenant/occupier is secured. In the majority of instances this means that all main services are completed and suspended ceilings and light fittings are installed. Some developments are considered to be completed when they reach "shell-and-core" condition where the accommodation is to be marketed in that state.

Future completions

Represents the total floor space of new and refurbished developments, either pre-planned, planned or under construction, that are expected to complete in a given year or the remainder of a current year (e.g. at Q1 2012 for Q2+Q3+Q4 2012). The total volume contains developments of high completion probability which are usually already under construction, have obtained building permits/authorisation, or are considered for other reasons highly likely to be completed

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JLL Contacts

Alexander Colpaert
Associate Director
EMEA Offices Research
London
+65 6494 7084
alex.colpaert@ap.jll.com

www.jll.eu

The JLL Office Property Clocks – Q3 2015