D2 REAL ESTATE

The Channel Islands Office Market Review 2021

+ SURVEY RESULTS
The future of offices in Jersey & Guernsey

An alliance member of BNP PARIBAS REAL ESTATE

www.d2re.co.uk

Contents

Foreword

It is extraordinary to think that when we issued our annual office market review at the beginning of 2020, little did we realise that one of the most significant medical crisis since the Spanish Flu was so imminent. By March 2020, the UK was in Lockdown, quickly followed by both Guernsey and Jersey. The FTSE fell by 25%. As a relative "side show" there was continued Brexit turmoil post the General Election in December 2019! Against this backdrop it is not surprising the year 2020 has been a challenging one.

COVID-19 has had a huge impact on how we live our lives, run our businesses and on society as a whole. Companies have been forced to fast track their digital strategies with agile working becoming the norm. It is testament to us all that we have been able to quickly adapt whilst going through a work-place evolution.

As businesses implemented their "working from home" strategies, the big topic was what the future held for offices and everyone had a view, normally based on anecdotal evidence. In my own view, if you want colleagues to join you in the office, which for our business is vital, then we need to create the right environment. I suspect that those landlords who do not work collaboratively with occupiers will quickly get left behind.

"...if you want colleagues to join you in the office, which for our business is vital, then we need to create the right environment. I suspect that those Landlord's that do not work collaboratively with occupiers will quickly get left behind."

In terms of commercial real estate performance in the Channel Islands, when compared to the UK we have had a relatively easy ride. The market is seen as a safe haven for investors seeking yield and long leases let to strong covenants, so demand has been reasonably strong and yields have held up well. Take up in Guernsey and Jersey is on par with 2019, albeit in Jersey this is below the 5 year average.

With the vaccine now in circulation, the economic outlook is set to improve and we expect demand for investments in the Channel Islands to continue. However, there is no doubt the first quarter of 2021 will be turbulent!

So, once occupiers have undertaken their occupational strategies, what is the outlook for the office market in the Channel Islands post COVID-19? To find out, **Read On...**

Phil Dawes
Managing Director | D2 Real Estate

The Channel Islands occupier survey

During 2020 there has been much discussion on what the future holds for the office market, with some speculating the COVID-19 pandemic will be the "death of the office". What has been apparent is the pandemic has accelerated a trend towards more flexible working and different office working practices.

In our view, working from home may have initially been an attractive proposition for many and modern technology together with a robust and fast broadband service supported this. However the novelty has certainly worn off with it becoming "live at work" for some. For many staff, particularly those in the younger cohorts, the social interaction of working in an office is very important and we suspect that occupiers struggle with monitoring staff wellbeing. Equally, from a business perspective the ability to train and mentor staff may have been compromised. On a positive note, we consider that occupiers in the Channel Islands have fared better than their UK counterparts, given that workers are not faced with long commutes and the necessity to use crowded public transport systems to get to work and the Islands have managed the pandemic well.

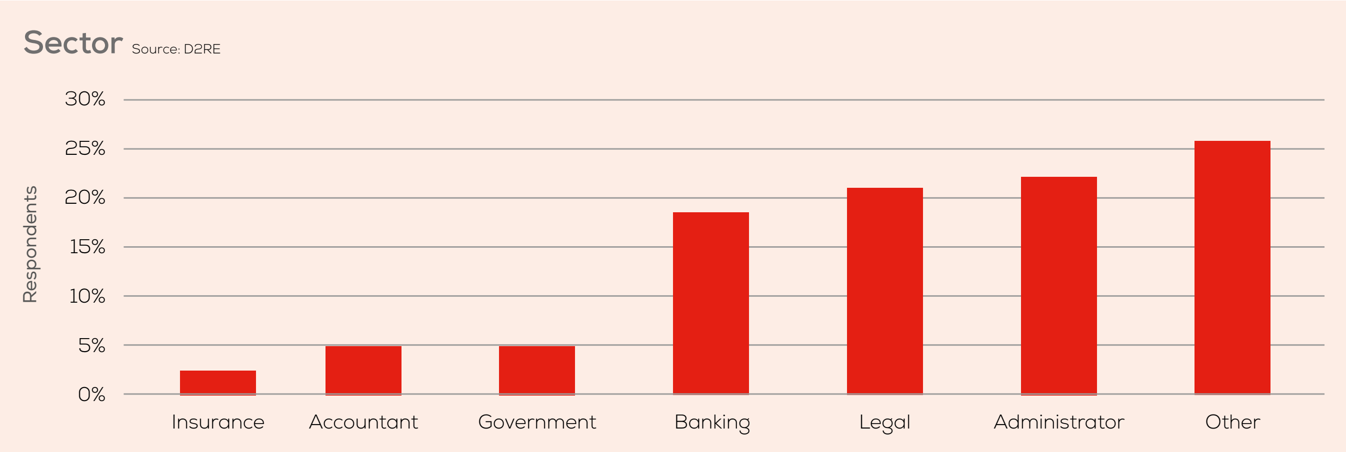
However, the above is largely based on anecdotal evidence and to provide some clarity D2 undertook a survey of major occupiers across both islands to identify key trends:

SAMPLE SIZE

We surveyed 115 companies across both islands and received a

70%

response rate. Our focus was on the larger occupiers, with Legal, Banking and Administrators all strongly represented. "Other" included sectors such as Investment Management, Wealth Managers and Fund Management. The survey was undertaken during December 2020 and January 2021.

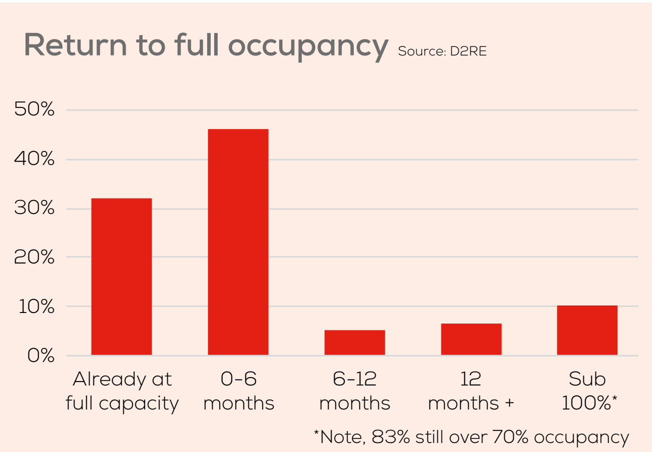


"...we consider that occupiers in The Channel Islands have fared better than their UK counterparts"

When would occupiers like to return to the office?

There was an unequivocal response from occupiers with 78% seeking to return to full capacity within 6 months, and of those 32% were at full capacity (albeit this will no doubt have changed since "working from home" directives have recently come into effect, first in Jersey and more recently in Guernsey). The sentiment is however clear, occupiers are intending to return. At the other end of the scale, 10% of respondents were not intending to return to full capacity, and of those, 83% of this sample are expecting to operate at 70% occupancy.

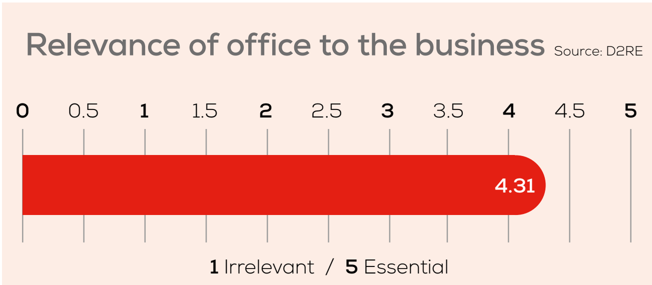
"...occupiers are intending to return."



Post COVID how relevant is having an office to your business?

We see this as being critical in terms of assessing the long-term future of offices in the Channel Islands. Respondents had the option of scoring between 1 & 5, with 1 being not at all relevant and 5 being essential.

It is telling that the average score was 4.3 out of 5. The results at the lower end of the scale were few and far between and didn't show any particular trend, albeit one was a major employer in the islands. Obviously, there is a knock-on effect with employees working from home as it will inevitably impact the retail and food & beverage sectors in St Helier and St Peter Port which rely on footfall.



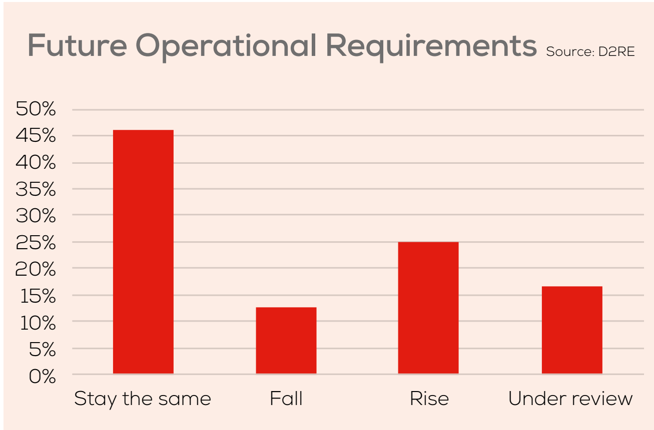
"Across both islands it's apparent how resilient occupiers have been and how quickly they have adapted. Rental collection across the islands has been excellent at 100%. There has been an acceleration towards working flexibly, however with 10 months experience from the initial lockdown it is clear going forward having a quality working environment is vital and will become increasingly more relevant to businesses"

Grant Irvine
D2 Head of Property Management

Are your future occupational requirements likely to fall or rise?

46% of respondents expected their occupational requirements to stay the same and 25% expected them to rise, which was higher than expected.

Only 12% expected this to fall. These tended to be the larger employers which could have an impact on other sectors, such as town centre retail and food and beverage. Not surprisingly some occupational strategic reviews are still underway.

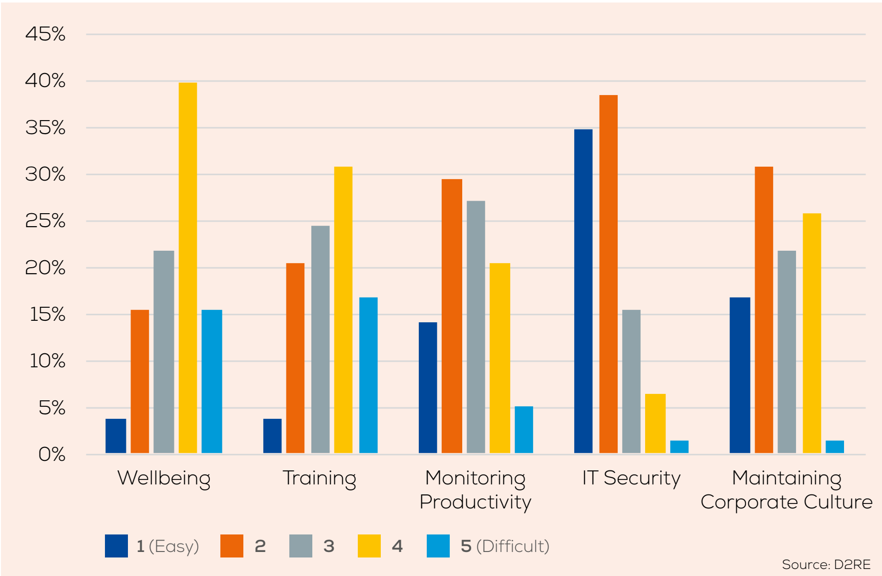


46% expect occupational requirements to stay the same

25% expect occupational requirements to rise

12% expect occupational requirements to fall

Operational efficiency?



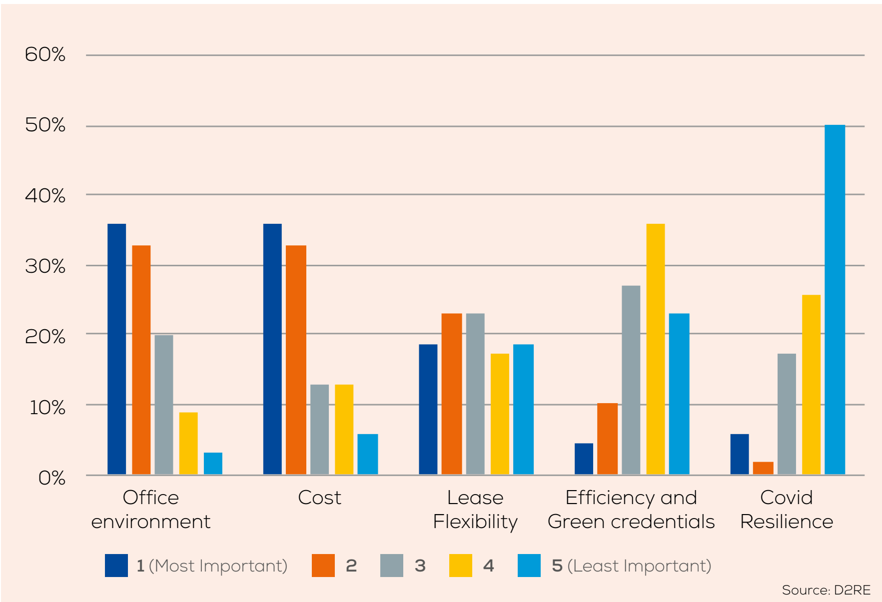
There has been plenty of discussion around operational efficiency and the results are reasonably compelling. Respondents were given the opportunity to rank each element in terms of ease/ difficulty.

Maintaining staff wellbeing is a concern and not easy to monitor whilst working from home. Training is proving very difficult.

Monitoring productivity was ranked as relatively easy by the majority, albeit we suspect that many of the respondents will be using timesheets, so perhaps this is less of an issue for this group.

Once systems were in place IT security was clearly not an issue for the majority.

Future occupational priorities?



Respondents were given the opportunity to rank in order key preferences when choosing an office.

Not surprisingly Cost was still near the top, however a high proportion of respondents put Office Environment above Cost.

Lease Flexibility was neutral, which is certainly not the case in the UK, which indicates that occupiers are still prepared to enter into long term lease commitments in the Channel Islands.

Green Credentials would have probably been much less relevant a few years ago and it will be interesting to see how this evolves over the years to come.

At the time of our survey, COVID Resilience was not a major consideration for the vast majority of respondents. This may change over time!

“Lease Flexibility was neutral, which is certainly not the case in the UK”

So what can we take from this survey?

In our view, the above demonstrates the resilience of the local market. We suspect the high score against "Relevance of the Office" would not be replicated in other jurisdictions, particularly the UK at the current time.

As will be revealed later in the report, occupiers are still willing to enter into long term lease commitments unlike the UK, so perhaps it is not surprising that Lease Flexibility is neutral and in complete contrast to the UK. It is also telling that across our managed portfolio (£450m+), rent collection over the past 12 months currently stands at 100%, well ahead of the UK. This bodes well for the investment market, as one of the key attractions of the local investment market is the opportunity to buy buildings let on long leases to strong covenants.

Although a more flexible working culture is inevitable and welcomed, the need for the office to enable effective training and mentoring, as well as being the physical embodiment of the brand and culture remain high priorities. Crucially, this survey has confirmed that the majority of the respondents strongly believe that in order to retain and attract the best staff the office environment is critical and certain key areas, such as staff wellbeing, are extremely challenging to maintain in a purely "working from home" environment. There will inevitably be a period of consolidation, where some businesses contract and others expand, but in essence, the office is still highly relevant. There is no doubt in our mind that offices in the Channel Islands will continue to have a major role to play as part of our working culture, where people want to go to work and as a place to encourage and drive business.

Survey respondents comments:

"Create an environment that supports flexible working and CSR/ESG, eg energy ratings, green walls, cycle storage, shower facilities, wet storage etc. After a prolonged period of people working at home Landlords in conjunction with the tenants and the States of Jersey/Guernsey need to make sure the office environment and the locality is a place that staff/people want to come back to."

"Use of virtual meeting software is now a permanent feature. Making this work when more staff (but not all) are back in the office will require cost effective methods for such calls to take place without disturbing others (e.g. meeting pods, VC enabled rooms, etc.)"

"Default working from home has been a quick fix, but not sustainable in the longer term for many businesses. Flexibility of accommodation is key here. The ability to reconfigure space to optimise attendance while maintaining physical distancing measures provides certainty in business continuity. Consequently, the standard floor area per employee metric needs to be reconsidered in light of the current pandemic and any future accommodation capable of addressing both BAU and pandemic scenarios"

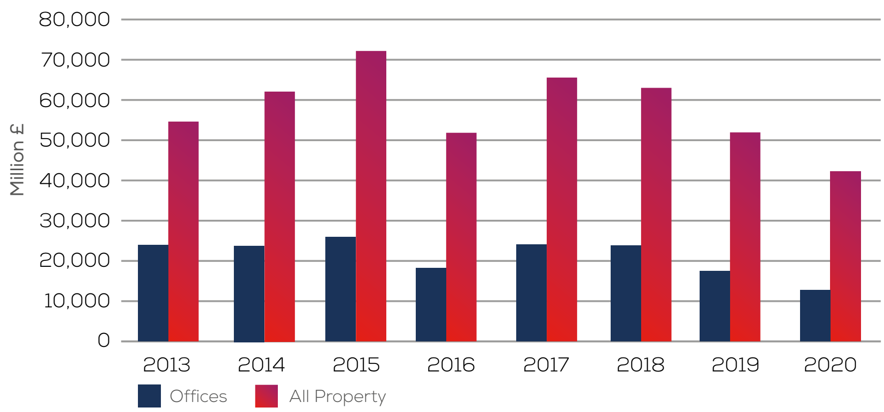
2020: The UK Market

The UK market remains an important benchmark with any yield shift on the mainland having significant relevance for the Channel Islands. Prudent investors will be comparing returns from equivalent assets in multiple jurisdictions, particularly with larger lot sizes.

Following the UK General Election result in December 2019 and the clarity of direction in relation to Brexit, 2020 started full of optimism for the UK property investment market. Unfortunately, all that changed with the onset of the COVID-19 pandemic and the year became rapidly more challenging.

UK Investment

Source: Property Data/BNP Paribas Real Estate Research

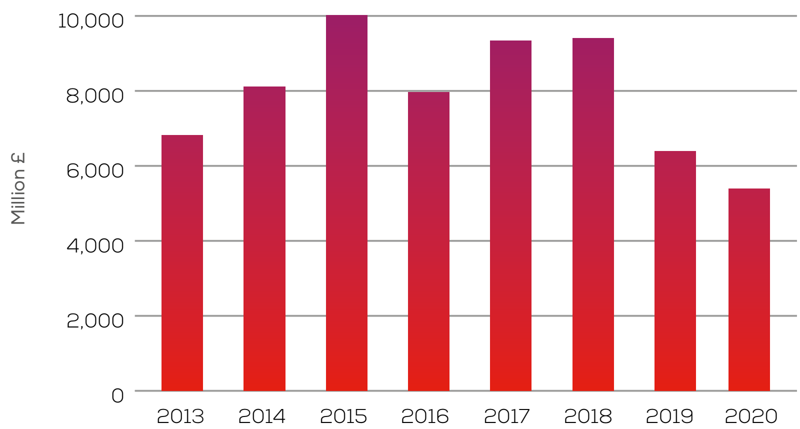


2020 Investment Volumes

Despite the usual end of year surge in investment activity, UK total investment volumes in 2020 were significantly lower than 2019. Whilst 2019 was defined by the uncertainty over the UK's withdrawal from the European Union, 2020 was dominated by the COVID-19 pandemic. No surprise with this backdrop that investors were more cautious resulting in total investment volumes of £42.24bn for 2020 *(Source: Property Data/BNP Paribas Real Estate Research)*. This is a 25% decrease in transactional activity when compared to the £53.51bn invested in 2019 and almost 40% down on 2018's total of £63.90bn. Interestingly, overseas investors accounted for over 50% of all investment in 2020, its highest ever share.

Regional Office Investment

Source: Property Data/BNP Paribas Real Estate Research



2020 Regional Office Performance

Mirroring the wider investment market, regional office performance has been characterised by strong demand for prime buildings with long term income. Stock selection is under even more scrutiny and we have witnessed a tightening of what is considered prime. There is a larger disparity between prime and secondary with even more emphasis on location and property fundamentals, building quality, secure income and tenant covenants. Prime yields in the key regional cities remained firm and in line with 2019 levels; standing at 4.75% in Birmingham, Bristol and Manchester and 5.00% in Leeds.

Investment volumes outside of Central London reached £4bn in 2020, almost 40% below the 2019 figure. Overseas investors were prevalent again as evidenced by Union Investment's acquisition of 55 Colmore Row in Birmingham for over £100m / 4.65%. Considered one of the best business addresses in the city and comprehensively refurbished in 2018, the acquisition highlights that premium prices remain achievable for the very best in class assets.

Looking forward to 2021, it could well be a year of two halves for the regional office sector. There is definitely a pent-up demand from investors but caution as the pandemic continues to evolve and affect the way people use offices. Given the large weight of capital waiting to enter the market, we anticipate an uptick in activity in the second half of the year; however, a lack of available stock could hinder investment volumes.

"With continuing uncertainty in mainland UK investment markets, the Channel Islands remains a very attractive property investment opportunity. Through the strength and resilience of their local economies, their positive supply / demand fundamentals and longer than average lease structures, they represent a safe haven for risk averse investors. Most importantly, the Channel Islands represent a significant pricing discount relative to major UK centres".

Alex Titheridge
Managing Director | D2 Guernsey

2020: The Channel Islands' investment market

Investment Overview

As we anticipated, 2020 was always going to be a quieter year in terms of investment activity. The records achieved in 2018 and 2019 (£185m and £220m respectively) were a result of the unprecedented level of development activity that has taken place over the past 5 years.

Investor demand remains strong as they are drawn to assets with defensive qualities. This is an area the Channel Islands scores highly. Compared to the UK, occupiers are prepared to take long leases and given the islands' resilient finance industry, occupiers' covenant strength provide income security. Indeed, over the past 12 months, the rent collection within D2's managed portfolio is 100%. So, it is certainly not a case of lack of demand for investment opportunities, more a lack of stock.

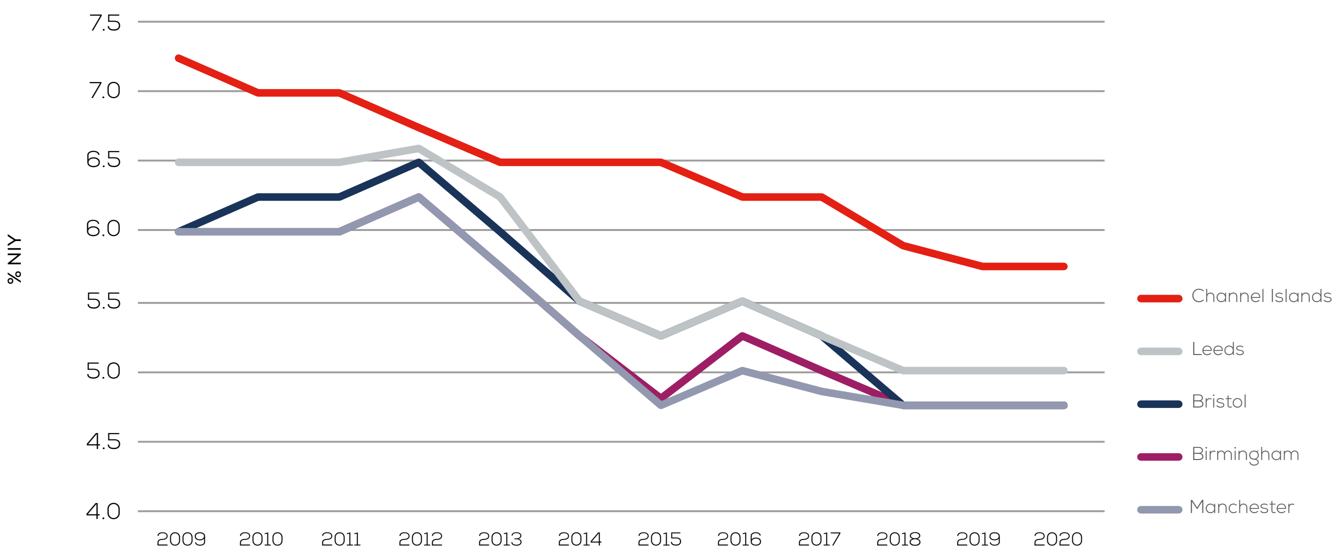
During 2020, around £61m of office stock has been transacted, with activity again evenly spread across both islands. Buyers include a listed fund, a syndicate and private investors. All the sales comprised second generation buildings and none were BREEAM rated, but in the main offered long unexpired lease terms let to strong covenants.

Yields achieved in 2020 ranged from circa 6.25% to 7% for assets let on leases with 8 to 15 years unexpired. These are not "super-prime" Grade A BREEAM-rated buildings and as a result, in the event a "best in class" asset was available, we feel yields of 5.5% - 5.75% should be achievable. As seen in the UK, the gap between "best in class" and "prime" is widening and the same principle should apply here in the Channel Islands. In our view the yield gap (100bps) between the Channel Islands and the UK offers scope to tighten, given the quality of assets potentially on offer and nuances of the local market.

"...the rent collection within our managed portfolio is 100%"

Prime Yields

Source: D2RE / BNPPRE



As highlighted in our survey, occupiers will be increasingly drawn to buildings offering an excellent working environment, to create the "hub" for collaborative thinking to drive their businesses. We are starting to see large corporate occupiers demanding that new premises are BREEAM rated. Throughout our managed portfolio, we are working with occupiers and landlords to deliver ESG initiatives and this service is becoming increasingly relevant. This is feeding into the investment market, particularly for larger lot sizes that may appeal to overseas investors.

For 2021 the pipeline is relatively strong so we should see an increase in activity. However, given the travel restrictions, this is going to make marketing buildings challenging and in all likelihood sales will be delayed until Q3 and Q4, when travel restrictions are hopefully relaxed. However, it should not be forgotten that the most active pool of investors over the past few years have been the locally based high net value residents and syndicates, so not necessarily restricted by travel, and they have demonstrated they have the ability to acquire assets of £50m + with no requirement for debt.

2020: Jersey's occupational market

Overview

Total Stock
3,000,000 sq ft

Total BREEAM Rated Stock
600,000 sq ft

Prime Location
Esplanade, St Helier

Potential Development Pipeline:

- States of Jersey Development Company: International Finance Centre, Buildings 2 & 6 (140,000 sq ft)
- Dandara: 8/9 Esplanade (50,000 sq ft)
- Le Masurier: J1 St Helier (200,000 sq ft +)

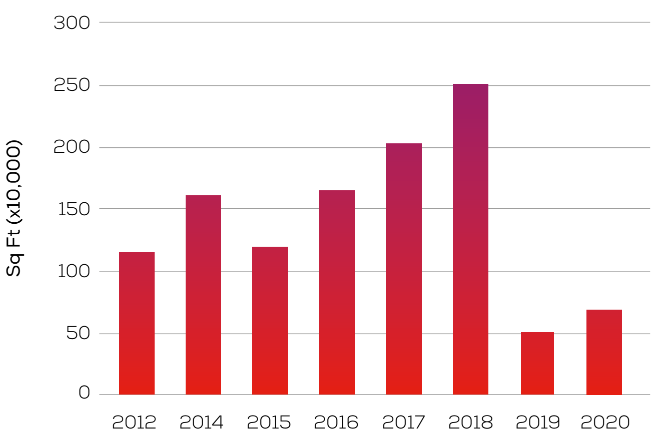
Occupational Take up

Take up volumes have been aligned with the investment market in terms of activity. The amount of new development from 2016 – 2018 was unprecedented, creating record levels of take up throughout 2017 and 2018 (200,000 sq ft and 250,000 sq ft respectively). Once the new space was let, take up levels have been relatively subdued and fell to 50,000 sq ft in 2019 and the same applies for 2020 where around 69,000 sq ft* of office space was let during the course of the year. Of this 69,000 sq ft, there were five lettings between 7,500 sq ft to 10,500 sq ft. Given the extraordinary circumstances relating to the COVID-19 pandemic and lack of stock, an increase in activity from 2019 was encouraging.

A notable feature of 2020 has been the amount of activity relating to lease re-gears, even during the peak of the pandemic. Where some occupiers are downsizing, others are expanding, and this has paid dividends for Landlords owning multi-let buildings who have benefited from proactive asset management. Leases with unbroken terms between 9 and 15 years have been signed, which again supports the data from our survey that occupiers are prepared to commit long term, demonstrating the relevance of the office to their business.

For 2021 there is one significant requirement in circulation (40,000 sq ft +) that we would expect to be signed this year, however the bulk of the activity is likely to fall in the bracket of 5,000 – 10,000 sq ft. The big question is whether "One Gov" (The Government of Jersey's office consolidation) proceeds. At 110,000 sq ft this would be one of the largest office transactions to ever have taken place in the Channel Islands!

St Helier Take Up Source: D2RE



Rental Tone

Due to the limited level of take up and general uncertainty relating to the pandemic, sentiment would suggest that rents are likely to decrease. However, there is very much a two-tier market in evidence. As we have previously reported, the difference between the rental tone for "BREEAM rated" buildings at £40 per sq ft to "prime, second generation" (defined as prime location, older buildings) is significant but this gap has narrowed slightly during 2020 as we highlight below.

"BREEAM RATED":
For 2020 the jury is still out. Large pre-let opportunities have been and continue to be in short supply and there are a number of developers keen to secure them. With the dearth of transactional evidence for prime BREEAM rated buildings it is difficult to establish the current headline rental tone. For larger lettings we believe the rate should be around £39 - £40 per sq ft but suspect this may come under downward pressure given the competitive nature of the market and limited number of enquiries in circulation.

"Prime, Second Generation":
As expected, in 2020 we have seen some growth in this sector through the lease re-gears we have completed. Headline rents have increased from £28.50 per sq ft to £30 per sq ft. There will always be exceptions, and over the last year evidence has been limited, but it is almost inevitable that with the shortage of supply and the rental differential between "BREEAM" and "Prime, Second Generation" buildings that rents had to move.

"Secondary":
Outside of Esplanade, the rental tone is in the region of £20 - £24 per sq ft. Much of the stock has been redeveloped for residential use, however there are still some high-quality buildings providing a good working environment at a significant rental discount when compared to Esplanade. It is important to note, not all occupiers want to pay Esplanade rents.

The vacancy rate during 2020 is consistent with 2019, and now sits at 7.8% as a percentage of total stock. For the prime, BREEAM rated buildings, it stands at only 3.5%.

**Excludes lease completions that were a result of pre-lets, which have been allocated to the year that the agreement to lease was signed.*

2020: Guernsey's occupational market

Overview

Total Stock
2,000,000 sq ft

Total Stock classed as Grade A
500,000 sq ft

Prime Locations
St Julian's Avenue
Glategny Esplanade, St Peter Port
Admiral Park

Potential Development Pipeline:

- Comprop: Admiral Park
  Phase 1 - 30,000 sq ft,
  Phase 2 - 45,000 sq ft subject to planning
- Comprop: St James Place (18,000 sq ft)

Occupational Take Up

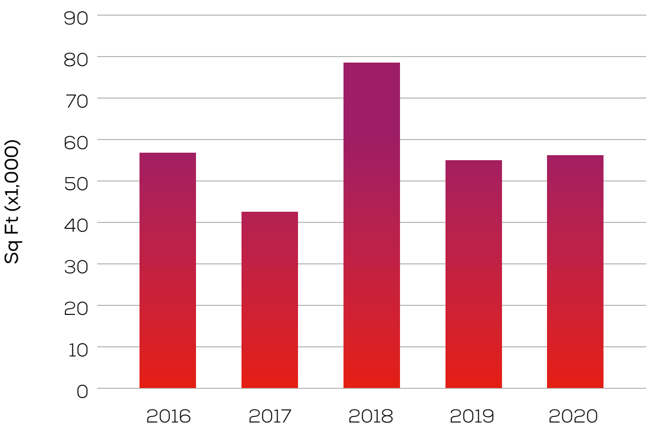
For the first time in over a decade, new developments are underway, the majority of which have been pre-let. As we have previously reported, if developers bring the right product to the market then there is strong occupier demand. Therefore, in spite of the COVID-19 pandemic the Guernsey office market has proven to be resilient with take up in the region of 57,000 sq ft (including the pre-lets), so broadly in line with the 5 year average. As is consistent with previous years there were a couple of larger lettings, the largest being 23,000 sq ft to Bank Julius Baer, with the remainder in smaller suites up to 5,000 sq ft.

Guernsey office market take up
57,000 sq ft

Largest Prelet: Bank Julius Baer
23,000 sq ft

St Peter Port Take Up

Source: D2RE



"... if developers bring the right product to the market then there is strong occupier demand."

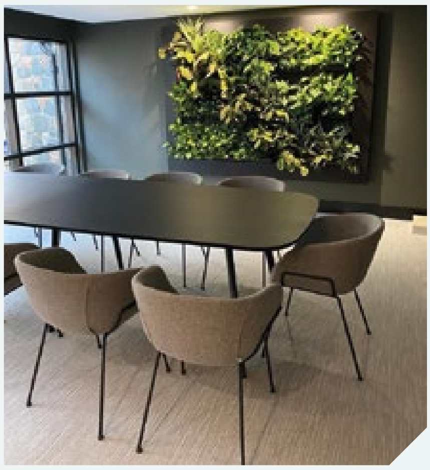
CASE STUDY

Windsor House, St Peter Port

There have been some notable success stories. Mirroring our own survey findings, and demonstrating the importance of the office environment, Windsor House on Le Pollet is a case in point. The property was comprehensively refurbished, including new flooring, lighting & air conditioning, refurbished common areas, kitchenettes, WCs & showers, exposed ceilings, communal meeting room, terraces and bike racks. The completed fit out provided something unique and contemporary to the Island, compared to the traditional standardised office accommodation on offer. As a result, the property is now 100% let and rents have naturally moved forward.

"We have been delighted with the quick take-up and successful completion of Windsor House. Tenants are less willing to settle for uninspiring offices and this project is proof that there is a strong and growing demand for high-quality, design-led and contemporary workspaces."

Luke Daynes
Commercial Director, Field Day Developments



Rental Tone

There have been several pre-lets during the course of 2020 which we understand have achieved rents below £40 per sq ft. Although it is generally accepted that pre-lets are often slightly discounted as they are the catalyst for the development, our view is that prime rents have softened over the past 12 months. Conversely, we have seen car parking rates rise over the past 12 months with £3,250 per space per annum firmly established in St Peter Port. Not surprisingly car parking is still an essential requirement in St Peter Port and this is reflected in a pricing premium for spaces.

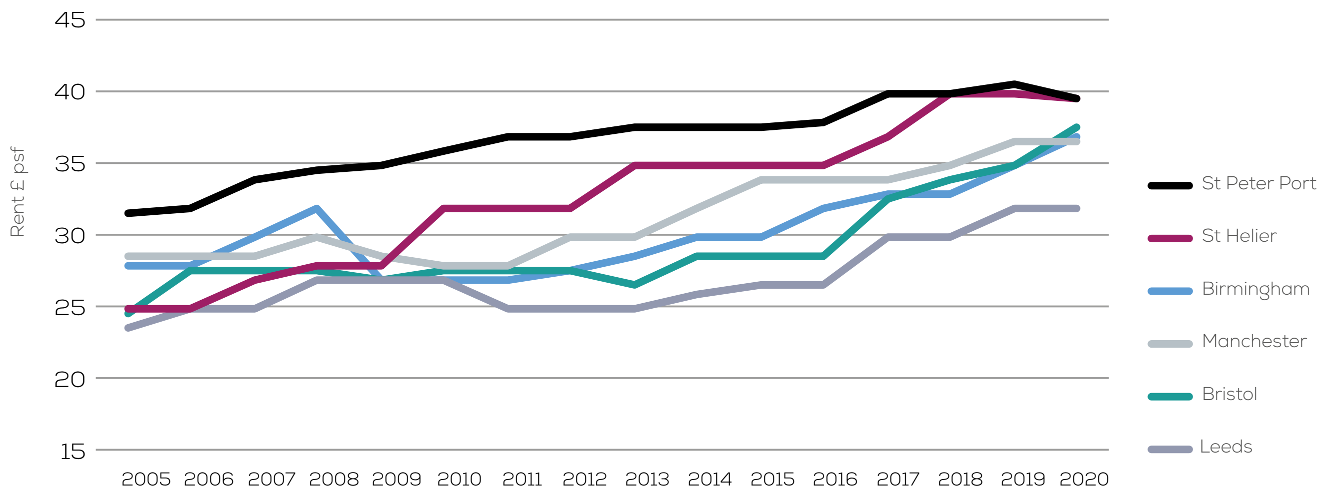
Prime:
In our view the general tone for prime headline rents in buildings offering car parking is in the region of £39 - £40 per sq ft. There will no doubt be variances between the buildings and rents up to £42 psf have been achieved in recent years. This will again be tested throughout 2021 as there are several prime refurbished suites that have come onto the market recently.

Secondary:
For good quality older stock, rents are in the region of £30 - £33 per sq ft. Again, car parking is a crucial factor in attracting tenants.

In terms of the vacancy rate over the past 12 months, several larger prime floorplates have been refurbished and are on the market, so therefore there has been a modest increase in the prime office vacancy rate. We estimate the prime vacancy rate stands at around 6% of total prime stock.

Guernsey adopted an elimination response to the COVID-19 pandemic and indeed during 2020 was the first area to become virus free in the British Isles. This strategy has raised Guernsey's profile internationally and underlined its credentials as being a secure jurisdiction to do business, which in part will have helped boost the confidence within the occupational market. The States of Guernsey also put in place an ambitious "Revive and Thrive" strategy in June 2020. The aim being to stimulate the Island's economy to where it would have been without COVID-19, through capital investment projects. This should have an impact in future years and is all the more relevant given the further COVID-19 restrictions that came into effect on 23rd January 2021.

Rental Growth Source: D2RE / BNPPRE



To find out how we can support your real estate strategy with research insights and strategic advice, please contact the team:

Investment & Strategic Advice

Phil Dawes (MRICS): ____________ phil.dawes@d2re.co.uk
Alex Titheridge (MRICS): ____________ alex.titheridge@d2re.co.uk
Chris Daniels (MRICS): ____________ chris.daniels@d2re.co.uk

Agency

Guernsey: Alex Titheridge (MRICS): ____________ alex.titheridge@d2re.co.uk
Jersey: Nick Trower (MRICS): ____________ nick.trower@d2re.co.uk

Valuation

Chris Hamilton (MRICS): ____________ chris.hamilton@d2re.co.uk

Property Management

Grant Irvine (MRICS): ____________ grant.irvine@d2re.co.uk

Local market experts with a global mindset

D2 REAL ESTATE

An alliance member of
BNP PARIBAS REAL ESTATE

JERSEY

4th Floor, Conway House,
7-9 Conway Street, St Helier, Jersey, JE2 3NT
T *+44 (0) 1534 629001*
E *enquiries@d2re.co.uk*

GUERNSEY

Carinthia House, 9-12 The Grange
St Peter Port, Guernsey GY1 2QJ
T *+44 (0) 1481 723375*
E *enquiries@d2re.co.uk*

www.d2re.co.uk

Company Number: 80923