



The Channel Islands Office Market Review 2022

+ SURVEY RESULTS
The future of offices
in Jersey & Guernsey

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Foreword

It's been another extraordinary year. From the very beginning 2021 seemed intent on giving 2020 a run for its money in terms of disruption and drama. From a personal perspective my year began under the restrictions of a Guernsey lockdown and ended with isolation in Jersey, courtesy of a case of Covid. However, whilst these were hardly auspicious memories, on balance the market offered up plenty to smile about.



“Close collaboration is essential to our business, and often we have overheard a conversation which has resulted in a deal which simply would not have happened working at our kitchen tables.”

Overall the occupational market has been stronger than last year, with a flurry of recent enquiries. Phase three of the International Finance Centre (IFC) is underway off the back of a 75% prelet, and Guernsey's first development for over 10 years has just completed. We are, however, also seeing some stock being released. It is tempting simply to point to increased numbers of home workers, but other factors are also at play, including several corporate sales, mergers, acquisitions and the acceleration of outsourcing. We are therefore at an intriguing crossroads, with some consolidating and downsizing for various reasons, but also some occupiers with an opportunity to relocate committing to new premises, including substantial prelets for 15-year lease terms or more.

In terms of our own occupational strategy, as office agents, home working runs counter to our business model. We therefore do not implement a hybrid working model, but can see the benefit of home working in some situations. Close collaboration is essential to our business, and often we have overheard a conversation which has resulted in a deal which simply would not have happened working at our kitchen tables. We also believe decentralising our workforce risks disadvantaging our emerging young talent. We intentionally position our graduates adjacent and opposite senior heads of business lines and Directors. This way their immediate colleagues can efficiently share their vast experience, so the

next generation of our management will be constantly enhancing both hard and soft skills. The frustrations of my 20-year-old daughter trying to work virtually from the kitchen table for a large company were particularly revealing. She quickly became disillusioned, yet was totally transformed and energised when working in the office, meeting new colleagues and socialising.

In this transformational time the need to gauge occupier sentiment is perhaps more critical than ever before. In this report we examine some of the key themes, from evolving working practices and their impact on the market to the growing importance of ESG. With 40% of global carbon emissions originating from our built environment, this is an increasingly important agenda.

Phil Dawes

Managing Director | D2 Real Estate

The Channel Islands Occupier Survey

It's been a year since our last survey and nearly 18 months since the first lockdown. Much has changed. The first lockdown, during a spell of fine spring weather, whetted employees' appetites for home working and greater flexibility. Predictably the "Is the office dead?" debate soon followed in various quarters, not least on social media platforms. Were bricks and mortar essential for businesses to function? The second lockdown was a very different story, occurring in one of the bleakest winters many of us have experienced. With the novelty of home working beginning to fade, virtual fatigue and burn-out took hold for many, and staff increasingly longed to return to the office. The Channel Islands have markedly different occupational dynamics to many other jurisdictions, with staff not having long commutes. Our research indicates that most businesses would prefer to have their staff return.

So, 12 months on from our last survey, what is the landscape? Has sentiment changed and what trends are starting to emerge? To answer some of these questions we conducted an in-depth survey of 145 of the Channel Islands' leading companies on their office occupation.

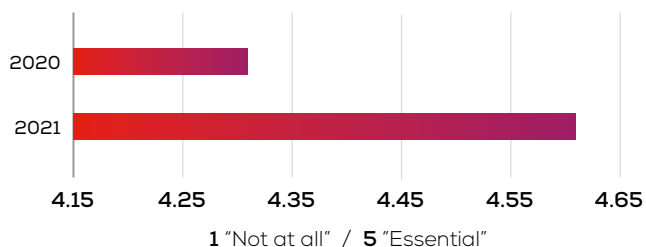
Our key findings from the survey and potential impact on the market:

- Reports of the office's death have been greatly exaggerated. The office remains highly relevant to occupiers and its endorsement has actually increased since our last survey.
- However other shifts have been seen, especially around the importance of staff wellbeing. Occupiers are investing in their premises or relocating to better-quality workplaces.
- This in turn has filtered through into the occupational market. Late 2021 saw a flurry of new enquiries. Occupiers are still entering into long term lease commitments, and rents are stable.
- Long term lease commitments and strong covenants are attracting a variety of investors, particularly from overseas, with the first US REIT entering the market. Liquidity is improving as new funds are being created and the local HNW's are making investments up to £50m with no debt.
- The impact of ESG is yet to be fully felt but is gaining momentum. Those that do not act now could be left behind.



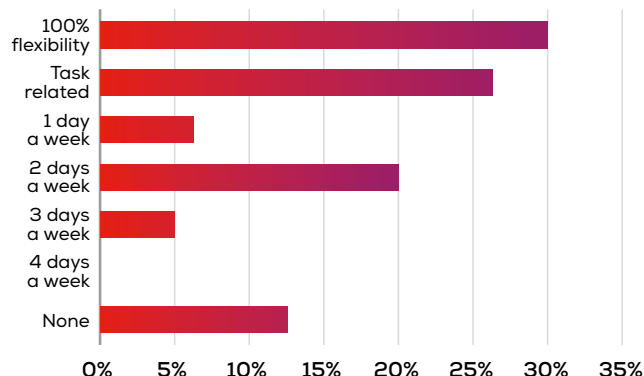
Does having an office remain important to your business?

Amid all the debate, this question perhaps gave the defining insight of how the pandemic has impacted the future of the office in the Channel Islands. Respondents were unequivocal. Asked to score from 1 “Not at all Important” to 5 “Essential”, in the 12 months since 2020’s survey the average score has actually increased from 4.31 to 4.63, with not one respondent giving a score of either 1 or 2. This suggests overwhelmingly that the power of in-person collaboration in the office is central to the fortunes of the islands’ economies.



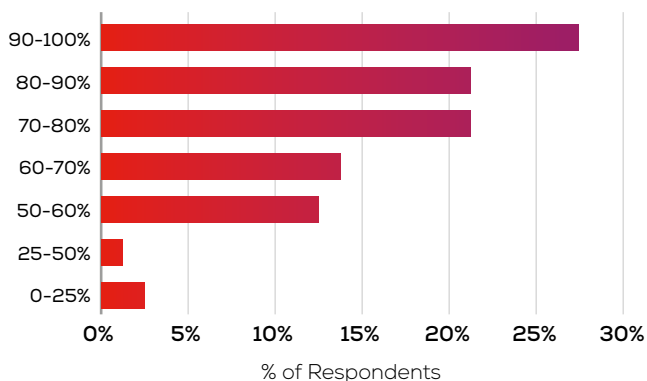
How many days a week are staff permitted to work from home?

The responses to this question reveal the importance of a degree of flexibility between office and home working. Our own experience tells us that situational judgement plays an important part here, and on occasion working from home to deal with a specific task can be more efficient without typical office distractions. Since companies were obliged to work from home everyone now has suitable IT capability and has worked out a home-working approach that suits them. It is therefore not surprising that flexibility is now offered in the majority of cases.



To achieve optimum performance what % of your employees would you like to be working in the office?

With the most popular response to this question ‘90% to 100%’ the survey results once again clearly endorse the importance of working in the office to achieve optimum performance.



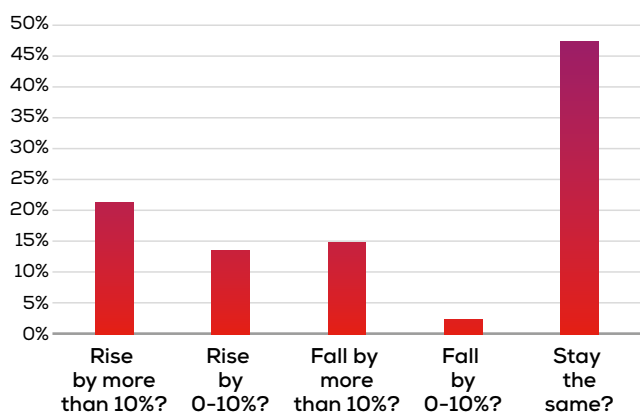
Post your homeworking experience, where would you prefer to do the following task:

Our survey respondents strongly favoured the office as the location best suited to each of the tasks we listed. However, we accept that the subject of home working, and its impact on both individuals and businesses, prompts much debate. Industry sector, corporate culture, management style, job function and the individual's personal preference all influence the suitability of home working. Where an individual or service provider typically works on bespoke projects, there may be few disadvantages to home working. In an environment that relies on a free and open flow of ideas, the pooling of information and insight, and high-energy culture in which there are clear shared goals, physical distance may be a hindrance. A key feature of the Channel Islands is that commutes are far less onerous than in the major UK conurbations, so the argument for employees repurposing their commute time to longer working hours is less relevant.



Within the next five years do you expect your floorspace in the Channel Islands to rise/fall/stay the same?

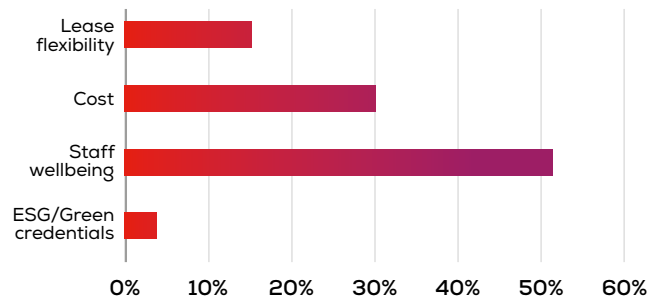
2021's responses to this question are broadly in line with the previous year. The most popular response was that occupiers' floorspace requirements are likely to remain unchanged. Our predictions are that more stock will come to the market over the next year or so, particularly in Jersey. However, as previously mentioned there are several reasons for this, and not simply an increase in home working. Businesses are sold and services are outsourced, so the market changes constantly. Working from home has given occupiers flexibility to expand and contract, and the opportunity for those occupiers outside the Esplanade an opportunity to relocate. In the latter part of 2021 we have seen a healthy volume of enquiries across both islands.



Key considerations in taking / retaining office accommodation – Rank in order of preference

Last year the categories of Staff Wellbeing and Cost carried broadly the same weighting. However 2021 has seen a notable shift toward Staff Wellbeing, with a raft of high quality refurbishments taking place to enhance the workplace environment. As our survey reveals, many key functions are considered better suited to the office but to attract and retain talent, which is critical due to the Channel Islands' limited labour pool, businesses are keen to make the workplace attractive and welcoming.

ESG / Green Credentials was named by 25% of respondents as their second priority, which is an improvement from last year. We expect this upward trend to continue.



The chart shows occupiers' No 1 Priority.

Conclusion

Early in the pandemic the need for office space was questioned, as occupiers could work from home. By late 2020 we began to see this thinking challenged, and this year's results make clear reading. Quite simply, businesses believe many of their core functions require an office.

Most businesses are now set up to offer the option of home working, and a degree of flexibility is allowed, particularly given the high priority cited for Staff Wellbeing. This has filtered through into the market with many occupiers

refurbishing their premises, and creating collaborative spaces. For many reasons, not exclusive to home working, some space is being released, but we are also seeing a high level of new enquiries, with some occupiers taking the opportunity to upgrade and relocate to prime locations.

Our survey reveals the Channel Islands' unique occupational market dynamics compared to other jurisdictions, with several distinctions, such as shorter commutes and minimal office supply, which is reflected in rents and pricing.

“Over the past 18 months we have seen workplace engagement irrevocably shift in a new direction. Occupiers are looking to create inspiring places for people to work, to drive collaboration and encourage innovation. There is now a clear understanding that a great office environment can attract the best talent, bring a brand to life, drive employee engagement and create a place where people want to be. It also allows an organisation to establish a hub where social, cultural and employee well-being can be nurtured. We have recently completed many high-profile refits for major corporate occupiers throughout the Channel Islands that embrace these values, with many more in the pipeline!”

Mark Coppins Axis Mason



CASE STUDY

Hawksford House, 15 Esplanade, St Helier

Following an extensive refit Hawksford House is a great example of how occupiers are now using their workplaces. Creating an “agile working environment”, incorporating flexibility, technology and collaboration. With open plan areas also including a variety of workstations, focus booths, collaboration zones and huddle pods, giving staff choice in how they would like to work. Over the past year we have seen a number of high quality refurbishments and it’s a trend that is going to become more commonplace as businesses focus on staff wellbeing.





“At Hawksford, we wanted to redefine the purpose of the office, making it a collaborative and inspiring open space where people can meet, grow, learn and achieve through quality interactions with others in a non-hierarchical, inclusive environment. We are incredibly proud of what we have created, and think the pictures and employee feedback speak for themselves!”

Richard Summerfield CPO Hawksford

The Channel Islands Investment Rationale

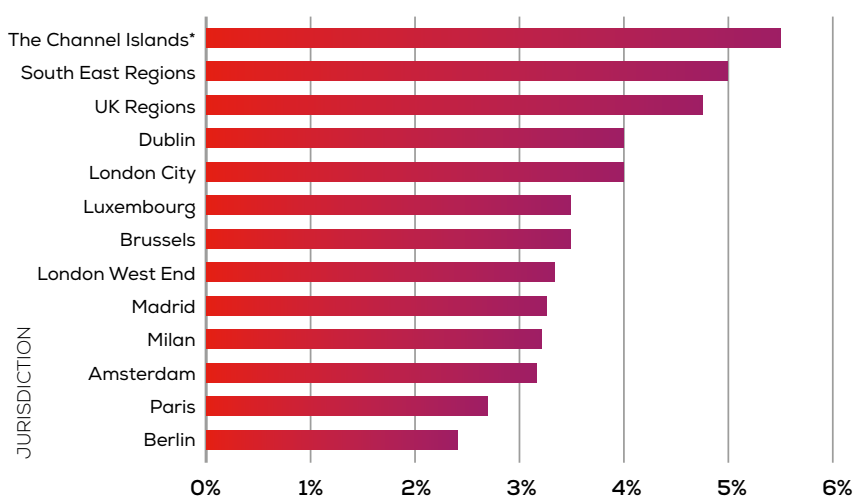
Our survey has demonstrated the resilience of the local markets. It is also worth examining the other key factors that have drawn investors to the Channel Islands:

Significant Yield Advantage

As activity in the Channel Islands has increased in recent years, the market has matured. The yield gap, compared to the UK, has shortened to around 50/75 basis points over the past 12 months, so is still at a significant discount to the UK and particularly Europe. This, coupled with the low interest rate environment in 2021, provides excellent income returns.

Prime Office Yields

Source: BNP Paribas Real Estate / *D2RE

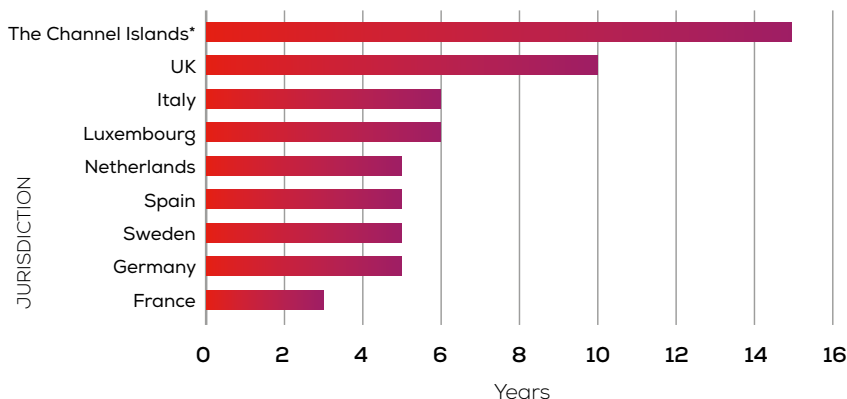


Long Lease Terms

Even with the disruption caused by Covid the majority of the occupational activity related to regears or prelets for terms of between 9 – 15 years. All the development activity in both Guernsey and Jersey is part prelet for unbroken lease terms of 15 years or more, to occupiers with an excellent credit rating. Lease length and tenant covenant strength is a major attraction in a market characterised by risk averse investors seeking security.

Average Lease Lengths

Source: BNP Paribas Real Estate / *D2RE

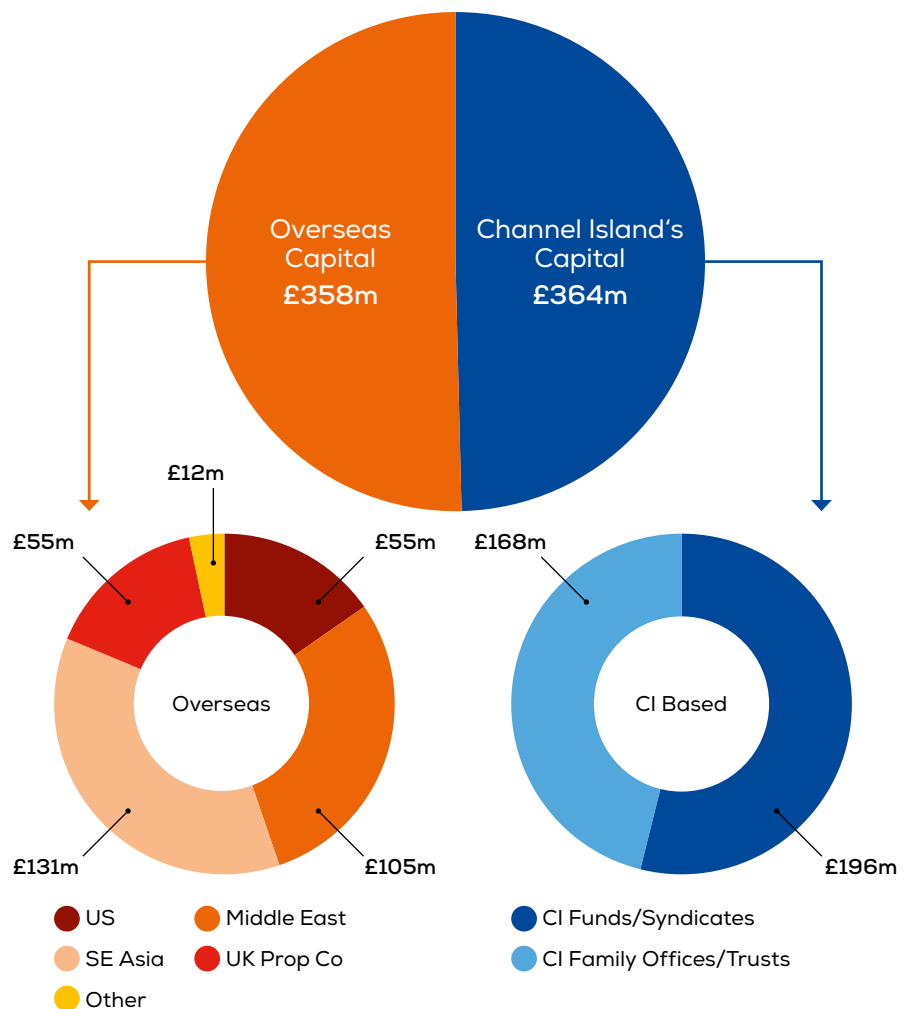


Liquidity

This has historically been the Channel Islands investment market's Achilles' heel, but as the market has become more established buyers have become more plentiful. There is strong interest from overseas particularly the Middle East and South East Asian investors, along with Channel Islands based Listed Funds, Family Offices and locally based syndicates. Last year the largest asset was acquired by a US REIT, attracted by the income return and covenant strength. However, direct investment from UK institutions is still relatively thin and by applying a larger risk premium, they are often uncompetitive on pricing.

The other key buyer segment is locally based high net worth investors. Traditionally they have been active in lot sizes of up to £10m, but this has changed in recent times as more wealthy individuals and family offices have relocated to the islands. Acquisitions in lot sizes of up to £50m+ with no recourse to debt are now relatively commonplace.

Overseas vs Local Capital Investment 2017 - 2021 Source: D2RE

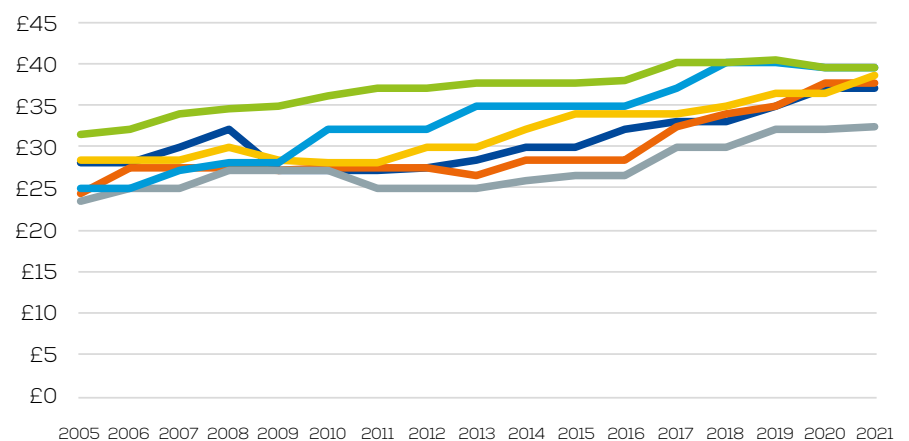


Steady Rental Growth

Limited supply has resulted in steady rental growth over the years. Aside from the 3 yearly rent review pattern in the Channel Islands, most rent reviews typically have fixed uplifts or some form of indexation.



Prime Headline Rents Source: D2RE



2021: The Channel Islands Investment Market Review

Investment Overview

As with 2020, buyers were plentiful in 2021. There was, however, a relative lack of opportunities, particularly when compared to 2019's investment boom, caused by significant development activity during the preceding two years.

Compared to 2020's £62m worth of stock transacted, 2021 saw around £100m, principally due to the sale of Trafalgar Court. There was a mix of buyers, including UK property companies, a new CI fund, a US REIT and local investors and developers.

There were two significant transactions to note.

Trafalgar Court

Trafalgar Court, Guernsey at £55m was the largest transaction to have taken place in the past few years. It was sold to Global Net Lease, a US REIT, their first foray into the Channel Islands investment market. They were attracted to the income return, the quality of the building and asset management opportunities, particularly potential lease restructuring. There was also letting risk, hence a yield of 7.9%, however it is clear they bought into the reliability of the building and strength of the local market in the event the lease restructures were unsuccessful. The weighted unexpired lease term at the time of purchase was only 6 years.



“Trafalgar Court, Guernsey at £55m was the largest transaction to have taken place in the past few years”

No 1 The Plaza

No 1 The Plaza, Guernsey was sold for in excess of £24m. This asset had very different characteristics to Trafalgar Court, with 75% being let on a long lease of 15 years to Bank Julius Baer, considered an excellent tenant covenant, with the remainder being vacant and having a rent guarantee. The yield applied to the income underpinned by Bank Julius Baer is rumoured to reflect 5.5%, an improvement of 25 basis points from the sale of IFC5 in 2019. Given the almost Bond-like qualities, pricing on this asset is to an extent aligned to the financial markets, albeit at a discount given liquidity. This yield still offers at least 50 – 75 basis point discount to the prime UK regional cities. The buyer was a newly formed Channel Islands fund.



2021: Jersey's Occupational Market

Overview

Total Stock
3,000,000
sq ft

Total BREEAM
Rated Grade A
600,000
sq ft



Prime Location
Esplanade,
St Helier

Overall
Vacancy Rate

8.5%

(of which Grade A)

1.25%

Prime Rents

£38 - 40 psf

Investment Volumes
since 2017

£445million

Occupational Take up

The big news in Jersey is the prelet of IFC6, the third phase of the International Finance Centre. With the site cleared, construction has now started. The total prelet is for 50,000 sq ft with an option of further space on the first floor. The ground floor will be a combination of office space and food and beverage use. It is encouraging to see that amenity space is being incorporated within the development as well as its BREEAM Excellent rating, which will become more and more relevant in future years. The 15 year+ lease agreement makes a clear statement by the occupier of their belief in the future of the office post-pandemic.

Prime headline rents are in the region of £40 psf, having accounted for fixed rental increases on the latest prelet. Car parking rates on the best buildings are achieving between £3,750 and £4,000. Typical rent frees for prime prelets are similar to cities such as Bristol in the UK, at around 1.5/2 months for every year of the term. It should be noted rent frees on prelets are often more generous than a letting on a completed development. Rents in older buildings but located in prime locations, being the Esplanade, are now achieving £30 psf+ and £3,250/£3,500 per car space and in secondary locations anywhere between £20 - £25 psf.

The overall vacancy rate has climbed from around 7.8% of total stock in 2020 to 8.5% in 2021. The vacancy rate for prime, BREEAM Rated buildings is still very low at 1.25%. As previously mentioned, this only partly reflects changes in home working, as there have also been some corporate structure changes that have freed up space. In a small market this can have a noticeable impact. However, it would be naïve to suggest that working from home hasn't had some impact, and consequently we are seeing the odd floor plate being released. However, there is also an uptick in enquiries, amounting to around 50,000 to 60,000 sq ft.

In terms of new development, we have mentioned IFC 6, with one further building within the International Finance Centre planned once another prelet is secured. Dandara have planning on 50,000 sq ft on 8 Esplanade. The other big news is the Government of Jersey's commitment to a new office on the site of Cyril Le Marquand House, totalling 100,000 sq ft and La Masurier development along Commercial Street, providing a mixed-use scheme that, if approved, will enhance the town centre.

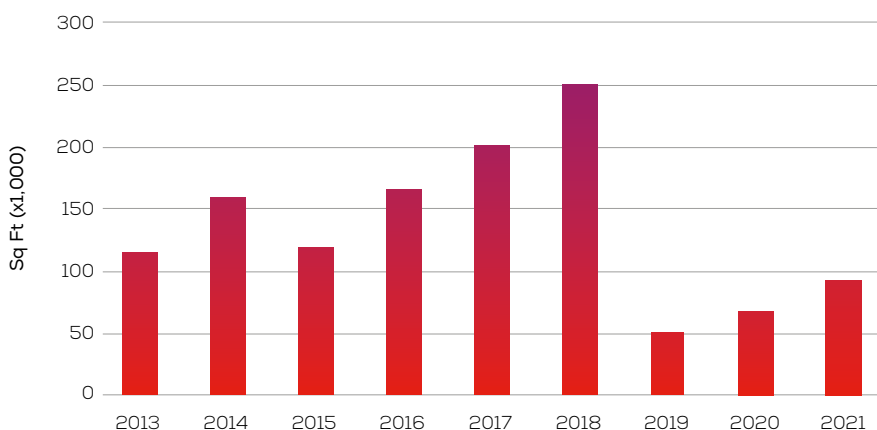


Chris Daniels
chris.daniels@d2re.co.uk



Phil Dawes
phil.dawes@d2re.co.uk

St Helier Take Up Source: D2RE



2021: Guernsey's Occupational Market

Overview

Total Stock
2,100,000
sq ft

Total Stock classed as Grade A
550,000
sq ft



Prime Locations
St Julian's Avenue
Gategny Esplanade
Admiral Park

Overall Vacancy Rate
10.95%

(of which Grade A)

1.7%

Prime Rents
£40 psf

Investment Volumes since 2017

£285million

Occupational Take Up

The new development of No 1 The Plaza is now complete, and St James Place is due to complete in Q2, 2022. The majority of the buildings are prelet. The second phase of Admiral Park, comprising around 60,000 sq ft, has planning and is awaiting a substantial prelet so development can start. We understand there is interest from a number of parties, and this would complete the Admiral Park development alongside a recently constructed Premier Inn and standalone restaurant.

Compared to previous years take up has been quite subdued. Year on year this has been around 50,000 sq ft, however, with the only major letting totalling 16,000 sq ft, take up for 2021 is more modest (this excludes prelets as these were taken into account in the previous year when agreement to lease were signed) at around 25,500 sq ft. However this belies the true level of activity. Similar to Jersey last year, most of the activity has centred around regears and lease extensions, such as Aztec's regear at Trafalgar Court on 26,146 sq ft.

Prime headline rents on the latest prelets are in the region of £40 psf, having accounted for minimum rent increases throughout the term of the lease. Although there are examples of smaller, prime suites, where this has been exceeded. Car parking rates in St Peter Port are achieving £3,250 and in Admiral Park around £1,750 per space. Typical rent frees for prelets on prime stock are similar to regional cities in the UK at around 1.25/1.5 months per year of the lease.

The overall vacancy rate has increased slightly from 9.32% of total stock in 2020 to 10.95% in 2021, albeit Grade A vacancy rate is very low at 1.7%. There are around 50,000 sq ft of enquiries so we expect the overall vacancy rate to diminish over the next year, albeit some of this could be absorbed by Phase 2 Admiral Park, depending on the timing of the development and lease expiries.

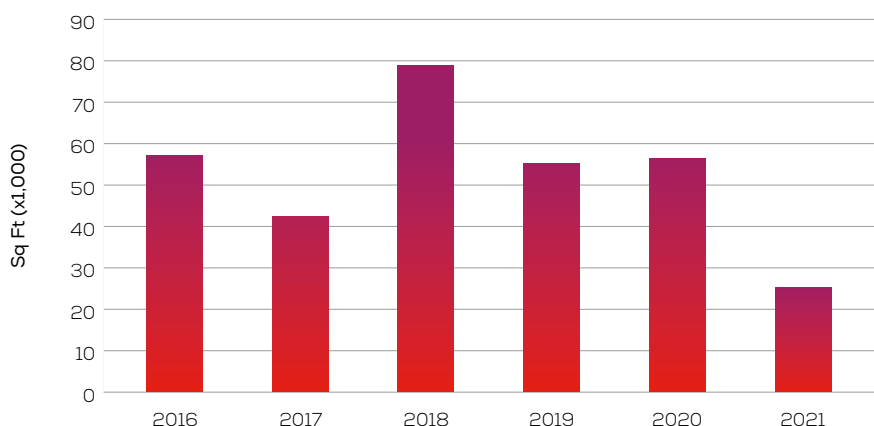


Alex Titheridge
alex.titheridge@d2re.co.uk



Charlie Davies
charlie.davies@d2re.co.uk

St Peter Port Take Up Source: D2RE

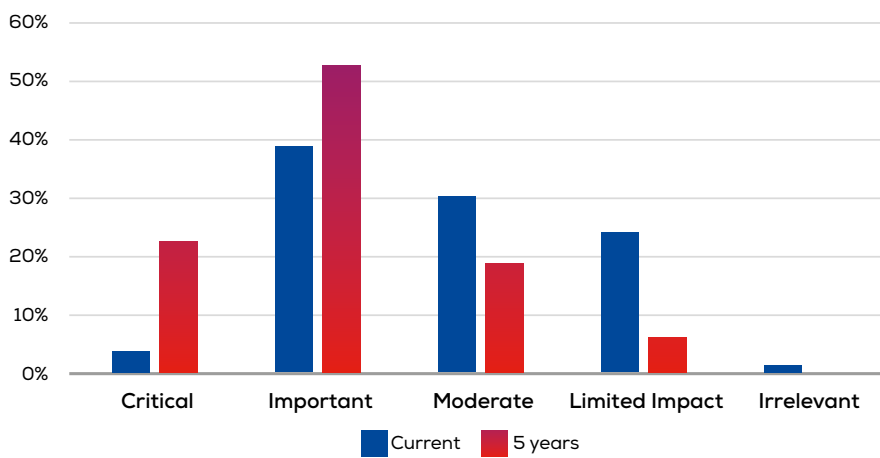


FUTURE TRENDS

It is unsurprising that the global pandemic has affected how we live and work. However as our survey results have confirmed, the majority of businesses still see the office as central to their operation and culture. It is clear that companies now have a renewed focus on their most valuable asset – their people. Attracting and retaining the best talent demands the right environment for teams to thrive and be productive. Over the past 12 months we have seen occupiers across the islands investing in their premises, through refurbishment, creating collaborative areas, technology spaces, amenity areas and enhancing IT.

The other key issue is the drive towards “net zero”. Ambitious targets have been set that will, if unmet, have a profound impact on future generations. The built environment creates 40% of global CO2 emissions, broadly split between building operations at 28% and the construction process at 12%. Here in the Channel Islands we feel there is still a long way to go, and although occupiers are talking ESG, it is still a relatively low priority when choosing an office. However, there is no doubt the ESG agenda is gaining momentum, as our survey has demonstrated.

Relevance of ESG policy in shaping the way you use your office space - current / 5 years time Source: D2RE

















This indicates that investors and developers addressing these issues effectively could ultimately benefit financially. Their buildings will become more desirable, offering great places to work. However, the issue runs deeper than this. Companies will scrutinise the environmental sustainability of their building and take more notice of its ratings concerning health and wellbeing. They will also become more aware of how their own actions can be more sustainable. We are starting to see occupiers placing specific demands, particularly on prelets. Those who factor this in now will be at an advantage. We have already seen rental premiums on such properties, and in the UK, the first signs that Banks are linking Energy Performance Certificates (EPC) to their lending criteria. The danger for some is that they will soon get left behind if there is a brown discount versus green premium on valuations.





Some of the initiatives that are commonplace in the UK and have been, or could be, adopted by developers and investors in the Channel Islands:

NEW BUILDS:	EXISTING BUILDINGS:
 Cycle parking / indoor cycle storage / onsite bike shop	 Installing motion sensors
 Car "CLUB" Spaces	 Upgrading windows and insulation
 Creation of Green Spaces	 Intensive internal planting
 In house and outdoor gym facilities	 Support for local charities
 Public Realm / tree planting	 Support of skills / education programmes
 Excellent natural light and floor to ceiling heights	 Green roofs / Green walls
 Green roofs / Green walls / Encouraging biodiversity	 Solar panels
 Rainwater harvesting and solar panels	 Bike stores
 Zero carbon building standards	 Defibrillators
 BREEAM	 BREEAM "in use"
 SKA GOLD	 Fitwel, WELL, WIREScore
 Fitwel, WELL, WIREScore	

ESG is a vital area that demands strong, clear and decisive leadership. The respective governments across both islands must play their part, through creative master planning and the provision of the necessary infrastructure. Progress has been made in Jersey on repurposing buildings and is gathering momentum in Guernsey. If governments are serious about Net Zero then this should be actively encouraged and incentivised. The "new build" contribution toward CO2 emissions is a substantial 12%. It may also help ameliorate the housing crisis across both islands if repurposing obsolete stock is actively encouraged. If governments are interested in substantial and lasting change then they could use the planning process to start implementing green agendas, perhaps reducing tax on green buildings or offering grants.

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: Chris Daniels (MRICS): _____ chris.daniels@d2re.co.uk

Valuation

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

Property Management

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

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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