JOURNAL

PROFILES INTERNATIONAL REALTY GROUP

Past and present of Cayman's commercial property market

Just over five years ago marked the start of the current 'financial crisis' when two CDO hedge funds run by Bear Stearns declared that they were halting redemptions. There has been a transformation that has taken place in the Cayman commercial property market over the last five years, it is prudent to take a moment and analyse what the changes have been, what have been the cause of these changes, how the market has adjusted and what the future of the market may look like.

Changes

Given that Cayman's commercial space market is dominated by offshore financial service providers, the damage has not been as bad as one may have feared. In 2007, total inventory of class A, B and C office space was approximately 1.5 million square feet. Today we have approximately 2.6 million square feet, with the market adding just over 200,000 square feet per annum over this period.

Total vacancy across the office space market has increased from about 60,000 sq ft, or 4 per cent in 2007 to over 400,000 sq ft, or 15 per cent today. Therefore, the absorption rate over the period has been around 150,000 sq ft per annum. Base rent rates of class A space have increased 20 per cent over the period. Base rent rates class B space have declined 7.5 per cent. Base rent rates class C space declined 25 per cent.

Cause of changes

The two main causes of change are the increased quantity and quality of class A office space, which in turn has raised tenants expectations and secondly the economic effect of the financial crisis on small and medium sized businesses.

The development with the biggest impact on the market over the past five years has, of course, been Camana Bay. The developer has added over 300,000 square feet of Class A office space to the market. This, in conjunction with the new government administration building makes up nearly 50 per cent of the additional office space inventory over the period.

The financial crisis seems to have affected some sectors of the economy more than others. Large multinational financial and legal firms have thrived over the past five years, expanding their occupied space and in many cases willing to pay higher rental rates for better space. Conversely, small and medium financial services firms together with service business' serving the local market have contracted the amount of space they previously occupied and have managed to negotiate rent reductions.

Market adjustments

The additional inventory at Camana Bay with its high quality design, construction, infrastructure, systems and management has raised the standard for class A office space in Cayman, with the effect that many buildings that previously were considered class A, can no longer be classified as such going by BOMA (Building Owners and Managers Association) standards.

The total sq ft of class A inventory is the same today as five years ago meaning that many buildings, which were classified as class A in 2007 now fall into the class B category. The main reason for this is that BOMA states, among other criteria, class A buildings have "above average rents", many buildings, which were commanding above average rents Five years ago, are now leasing at average rents.

The result of this being total class B inventory has increased by 700,000 sq ft or nearly 150 per cent. This substantial increase in supply has put downward pressure on class B rents and vacancy over the period. The vacancy rate for class B space is now more than 20 per cent. There has been a similar situation with class C inventory that has increased by 30 per cent over the last five years.

While class A rents have increased every year for the past five years and by a total of more than 20 per cent. Class B and C rents have decreased by 7.5 per cent and 25 per cent respectively over the period. Landlords of class B and C space are having to become more competitive not just on their base rent rates but also in regards to offering more concessions on fit out, installing back up generators and in many cases acquiring additional parking for tenants.

We are seeing landlords in the class B & C markets become more flexible in regards to lease renewals. Even if the renewal clause states that the rent will be a minimum of what was previously being paid landlords have recognised that an exiting tenant has never been more valuable, even if it means to keep the tenant, the landlord has to make concessions on rent and provide additional facilities.

Future

Both Camana Bay and Cricket Square have pre-leased more than 50 per cent of their new buildings. We would expect both of these new buildings to be fully leased by the end of the year meaning that the vacancy rate for class A space will decrease to under 2 per cent. While there are two new class A buildings projected to come onto the market over the next eighteen months we anticipate that rents in this sector will continue to climb 2-4 per cent per annum.

Over the next five years we do not anticipate the class B inventory to increase, it will more likely decrease as some buildings drop down to class C space, while others will be redeveloped or change their usage to residential. The absorption rate through the financial crisis has remained strong and with class B rates approaching half of class A rates, we believe vacancy rates will decline and base rates will stabilise in the class B market.

IRG

International Realty Group Ltd. (IRG) is Cayman's leading commercial property broker, specialising in the leasing, sale, acquisition and analysis of office, retail and general commercial space in Cayman and on commercially zoned raw land for development. IRG also provides tenant and landlord representation services to a wide range of Cayman commercial property owners, investors and tenants, and provides strategic advice on Cayman property asset and property management based upon our 20 years of experience in the commercial property business here.

IRG has an unrivalled working knowledge of the Cayman commercial space market and can offer its clients access to the only 20-year historical office space database in the Cayman real estate market, invaluable for market analysis and feasibility studies and assisting in tenant and landlord negotiations. IRG develops customised office and retail leasing and sales programmes for our clients' properties and offers tenants and investors the widest available knowledge of the Cayman office space market.

Our other services include, building development feasibility, office set up, office fit-out coordination, space planning and move management through our corporate relocation team IRC and sister company Cayman Office Concepts Ltd.

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