Economic downturn, tech slump send commercial real estate prices tumbling

Rental prices for office space in Israel plunged by 16% last year, as technology firms downsize and drive down demand

By **SHOSHANNA SOLOMON** FOLLOW
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Illustrative: Skyscrapers in Tel Aviv. March 2023. (Anna Arinshtein via iStock by Getty Images)

Rental prices for office space in Israel plunged by 16 percent last year, as tech firms — global and local — have been downsizing and driving up the supply of commercial property, according to a report by commercial real estate consulting firm Cushman and Wakefield Inter Israel.

The data shows that the average price per square meter in the nation's main business districts dropped to NIS 114 ($30.45) in 2023 from NIS 136 ($36.33) in 2022.

"The office rental market is a direct reflection of what is happening in the economy and in the Israeli tech sector, which is so dominant in Israel," said Yoram Blumenthal, the managing partner of Cushman and Wakefield Inter Israel, in an interview from the firm's offices in Ramat Gan.

"In a way, you could say it is the pulse of how the economy is doing," he added.

The price per square meter last year was still higher than the low of NIS 98 per square meter registered in 2020, amid the lockdowns triggered by the coronavirus pandemic that led to widespread virtual work practices. Prices started to rise again in 2021, to NIS 107 per square meter, and reached a high in 2022, as firms called workers back to the office. That year was also characterized by a technology boom that saw Israeli startups raise an unprecedented amount of money in investments and create a record number of tech unicorns.

Prices for office space surged in these boom years, with developers initiating new and ever more luxurious projects for their clients, propelled by the lowest-ever interest rates and sky-high demand. Then, suddenly, last year, it all came crashing down — much like the Israeli tech market, which saw investments plunge 56% to $6.7 billion in 2023 compared to the previous year, according to IVC Research Center which tracks the industry.

The slowdown of the global tech industry toward the end of 2022, the judicial overhaul in Israel proposed by the government of Benjamin Netanyahu, and the rise in interest rates globally, all contributed to the drop in prices in 2023, said Blumenthal.


Yoram Blumenthal, managing partner at Cushman & Wakefield Inter Israel. (Courtesy)

He added that it was still too early to assess the impact on the market of the first three months of the Israel-Hamas war, triggered by the terror group's shock October 7 massacre in southern Israel in which some 1,200 were killed and 253 taken hostage to Gaza. The Bank of Israel has lowered its growth forecast for the 2024 economy to 2% from a previous forecast of 3%, and in January cut its borrowing costs for the first time since April 2020 to help support households and businesses as the war continues.

The 16% decline in average office space prices is the steepest Blumenthal has seen since the pandemic lockdowns, he said. Rental prices declined 8.4% between 2019 and 2020, the Cushman and Wakefield Inter Israel data shows.

"Demand for office space has frozen," he said. If the economic crisis continues because of a prolonged war which may expand to other fronts, the glut of office space that is expected to come onto the market in 2026 and 2027 – from construction started in the years of record low interest rates and the tech boom – could create a further supply and demand imbalance in city centers, he warned.

Falling demand

The drop in the value of office buildings is a global phenomenon, triggered by the pandemic-era shift to remote work environments in which office attendance has stabilized at 30% below pre-pandemic levels, according to a July report by consultants McKinsey.

This shift is likely to erase some $800 billion from the value of office buildings in key global cities by 2030, the report said. The lower office attendance is more prevalent in the knowledge economy such as the professional services, information and finance industries, in which workers can easily work virtually. This will put the vibrancy of the cities, including New York and San Francisco, "at risk." Falling demand will result in surplus office space, particularly in lower quality and older buildings, the report said.

An illustrative photo of a center for high-tech companies in Herzliya Pituah, Oct 30, 2020. (Gili Yaari/Flash90)

The McKinsey report said that cities and buildings can adapt to the new reality by taking a "hybrid" approach as well – making sure to develop mixed-use neighborhoods, constructing more adaptable buildings, and designing multi-use office and retail spaces.

According to the Cushman and Wakefield Inter Israel data, Menachem Begin and Yigal Alon streets registered the greatest average drops per square meters in Tel Aviv, with prices declining in other business-centric cities as well including Herzliya, Rosh Ha'ayin and Kfar Saba.

The decline in demand for office space has not so much been triggered by the remote working trend, said Blumenthal, but by lower economic activity.

"Israelis like coming to the office because they prefer social settings and teamwork, which is a key factor for success," he said.

The lower rental prices could mean that developers will find it harder to finance and set up new projects, Blumenthal said. When added to a war-triggered lack of construction workers, this could mean that in the future we could see a delay and decline in the supply of office space, which would rebalance the market.

This delay could help developers meet a "more positive" economic cycle later on, he said. "Also, the dramatic decision of the Bank of Israel… to reduce the interest rate by 0.25% in combination with other global economic factors may signal the beginning of a reversal of the trend."

The recent outstanding economic performance of the global tech giants is also an indication of a positive turnaround of economies and eventually of Israel's office scene as well, he said, as Israel is home to R&D centers of most of the global tech giants.