RESEARCH


SEPTEMBER 2012

# SYDNEY CBD OFFICE

Market Overview

**Knight Frank**

## HIGHLIGHTS

- The negative net supply recorded over the first half of the year is an indication of things to come, with the total net supply between now and the end of 2014 forecast to be negative. Some imminent refurbishment completions and below average tenant enquiry levels are forecast to see the vacancy rate hold steady for the next 12 months before a gradual improvement in demand will underpin a 6% vacancy rate by 2015.
- Face rental growth for both prime and secondary assets have continued to track in line with CPI over the last six months, while we observed a slight uptick in average prime incentives. This was the first such increase in two years and is indicative of the below average enquiry levels and constraint being exhibited by tenants. Nevertheless supply driven factors are forecast to underpin a positive outlook for effective rents over the next three years, however this growth will be concentrated in two and three years time when demand is expected to improve from current levels.
- Sales transaction activity has slowed over 2012, largely due to the hiatus in offshore acquisitions despite continued interest. Offsetting this somewhat are local groups, who are now looking for acquisition opportunities to increase total returns, particularly given the large spread between debt costs and property yields. Prime core market yields have held broadly steady in the last six months and average between 6.25% and 7.25%. It is noted that no significant prime assets have been marketed and we would envisage strong demand for any core located prime assets if placed on the market, particularly as the trading prices of A-REITs have moved closer to NTA.

# SYDNEY CBD OVERVIEW

Table 1
Sydney CBD Office Market Indicators as at July 2012

| Grade | Total Stock (m²) | Vacancy Rate (%) | Annual Net Absorption (m²) | Annual Net Additions (m²) | Average Gross Face Rent ($/m²) | Average Incentive (%) | Average Core Market Yield (%) |
|---|---|---|---|---|---|---|---|
| Prime | 2,498,912 | 7.6 | 53,942 | 48,031 | 685 - 1,020 (891 Avg) | 26.7 | 6.25 - 7.25 (6.83 Avg) |
| Secondary | 2,403,825 | 8.9 | -2,184 | -55,328 | 500 - 630 (563 Avg) | 28.8 | 7.75 - 8.75 (8.18 Avg) |
| **Total** | **4,902,737** | **8.2** | **51,757** | **-7,297** | | | |

Source: Knight Frank/PCA NB. Average data is on a weighted basis

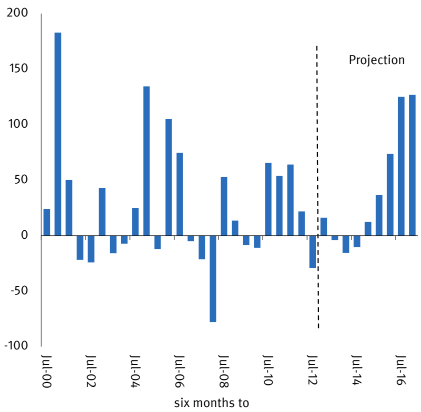
# SUPPLY & DEVELOPMENT ACTIVITY

New supply to the Sydney market has been particularly soft over the first half of 2012 with the PCA measuring only 13,225m² of completions in the six months to July. This supply was entirely made up of refurbished space coming back on line rather than new projects. However 42,237m² of withdrawals saw total stock levels contract by 29,012m² or 0.6%. With the next wave of supply not forecast to start coming online in a meaningful capacity until 2015 and 2016, the next two years are expected to see a continuation of negative net supply. The total stock level of Sydney's CBD peaked in January 2012 at 4,931,749m² and is not expected to return to this level until 2015.

While stock withdrawal for either refurbishment or re-development is a continual cyclical element of office markets, it is noted that an unusually large number of imminent withdrawals will undergo a change of use away from office. Such withdrawals account for 35% of the three year pipeline for total withdrawals. Residential conversions are the key contributor and include Goldfields House at 1 Alfred Street (although it is understood owner Blackstone is reviewing project timing), 161 Clarence Street, 131 Macquarie Street, 115 Bathurst Street and 71 Macquarie Street (formerly Amatil Building). The proposed hotel conversion of 34 Hunter Street by Cititel Hotels is another change of use example.

The next major new commercial developments due to complete are 161 Castlereagh Street (GPT (GWOF)/LaSalle/ISPT, 54,450m², 90% committed) in the first half of 2013 followed by 8 Chifley (Mirvac/K-REIT Asia 19,100m², 42% committed) in the second half of the year. Supply is forecast to pick up from possibly late 2014, however more likely early 2015(refer Supply Map, page 3). Potential projects to complete include a number of DA approved re-developments including 13,500m² at 383 George Street (Fife Capital), 33,700m² at 5 Martin Place (Colonial/Cbus) and 20,000m² at 20 Martin Place (Pembroke). With Lend Lease having achieved pre-commitments at Barangaroo, the first tower, C4 (86,000m²), is projected to complete in late 2015 followed by the remaining two towers C5 (75,800m²) and C3 (98,300m²). 200 George Street by Mirvac (39,000m²) is also expected to reach completion in late 2016.

Figure 1
Sydney CBD Forecast Net Supply
Per six month period (000's m²)




Source: PCA/Knight Frank

## Backfill Space

The announcement of Barangaroo pre-commitments by Westpac, KPMG and Lend Lease are set to result in several large tenancy options that will become available to the market. KPMG will vacate 10 Shelley Street (27,000m²) and Lend Lease will vacate 30 The Bond (17,000m²). Westpac's move represents the consolidation of various tenancies in relatively older buildings. The majority of this stock will be withdrawn from the market for refurbishment (such as 6,319m² at 255 Elizabeth Street and 6,650m² at 55 Market Street) or redevelopment (28,500m² at 60 Martin Place). The circa 25,000m² of space at both 33 & 35 Pitt Street and 182 George Street will also be withdrawn, however the development outcome is yet to be finalised. Should PWC commit to Barangaroo, as has been reported, circa 39,500m² would be vacated at Darling Park Tower 2. Approximately 35,000m² at 1 Martin Place will also be available when Macquarie moves to 50 Martin Place in early 2015.

For projects due to complete in 2013, 161 Castlereagh will accommodate ANZ, whom are set to vacate 15,500m² at 20 Martin Place, which will be redeveloped, while approximately 10,000m² of sub lease will become available at 347 Kent Street. The 18,000m² that Freehills occupy at MLC will also become available when they relocate to 161 Castlereagh Street. Corrs Chambers Westgarth will vacate 7,000m² at GPT 1 Farrer Place when they relocate to 8 Chifley.

# MAJOR OFFICE SUPPLY

1. 1 O'Connell St# - 28,849m² [Crowe Horwath] - 32% committed^
APPF (Lend Lease)/ADIA - L8-16 Q3 2011, High rise 2012
2. 161 Castlereagh St (242 Pitt St) - 54,450 m² [ANZ/Freehills]
GPT (GWOF)/La Salle/ISPT - Q1 2013 - 90% committed
3. 99 Elizabeth Street# - 8,437m²
Kyko Group - Q1 2013
4. 8 Chifley Square - 19,100m² [Corrs]
Mirvac/K-REIT Asia - Q3 2013 - 42% committed
5. 52 Martin Place# - ~17,000m²
QIC - 2012/2013
6. Barangaroo C4 & C5 - 86,000m² + 75,800m²
Lend Lease/SHFA - 2015/16 - 70% committed
7. 180 Thomas St - ~14,000m² [Transgrid]
Transgrid - 2014 - 35% committed
8. Red Cross Building, 159 Clarence St - ~14,000m²
St Hilliers 2014+
9. 383 George St (38 York St) - 13,500m²
Fife Capital - 2014+
10. 5 Martin Place (120 Pitt St) - 33,700m²
Colonial (CPA)/Cbus - Q1 2015
11. 50 Martin Place# - ~18,000m²
Macquarie Group (Owner Occupy) - 2015
12. Barangaroo C3 - 98,300m²
Lend Lease /SHFA - 2016+
13. 190-200 George St - 45,000m²
Mirvac - 2016 (Stage 1 DA Approved, Stage 2 submitted)
14. 19-31 Pitt St- ~7,000m²
Cambooya - 2016+ (Stage 1 DA Approved)
15. 175 Liverpool Street# - 14,500m²
GIC - 2013/2014
16. 1 Martin Place# - 40,200m²
Charter Hall Office/ Macquarie Martin Place Trust - 2015
17. Central Park (CUB site) - up to ~70,000m²
Frasers - 2015+
18. 430-450 Pitt St (Belmore Park) - 22,500m²
Energy Australia - 2015+
19. ANZ Building - 20 Martin Pl# - ~20,000m²+
Pembroke Real Estate 2015+
20. 333 George St - ~14,000m²
Charter Hall Core Plus Office Fund - 2015+
21. 33 Bligh St - 26,000m²
Energy Aust./Investa - 2016
22. The Ribbon, 1 Wheat Road - ~40,000m²
Grocon/SHFA - 2016+
23. 151 Clarence St - 21,000m²
Investa - 2016+
24. 289-307 George St (City One) - 65,000m²
Thakral - 2017+
25. 182 George & 33 Pitt - ~45,000m²
Westpac - 2017+
26. George, Dalley & Pitt Sts - 35,000m²+
GE Real Estate - 2017+
27. Loftus & Young Sts - 35,000m²
AMP - 2018+
28. 60 Martin Place - ~28,500m² (full redevelopment likely)
Investa/Private Investor - 2018+

**Under Construction/Complete**

**DA Approved / Confirmed / Site Works**

**Mooted / Early Feasibility**

NB. Dates are Knight Frank Research estimates
Major tenant precommitment in [brackets] next to NLA
# Major refurbishment
Office NLA quoted
^ includes NLA under negotiation/HOA

Source of Map: Knight Frank

# TENANT DEMAND & RENTS

After the subdued tenant demand recorded over 2011, the first half of 2012 provided a surprise increase in the amount of occupied space within the CBD market. PCA figures recorded 45,309m² of positive net absorption, well above the 10,709m² recorded over the entire 2011 year. Combined with the impact from 42,237m² of stock withdrawals from the market the CBD vacancy rate contracted to 8.2% as at July from the 9.7% recorded six months prior.

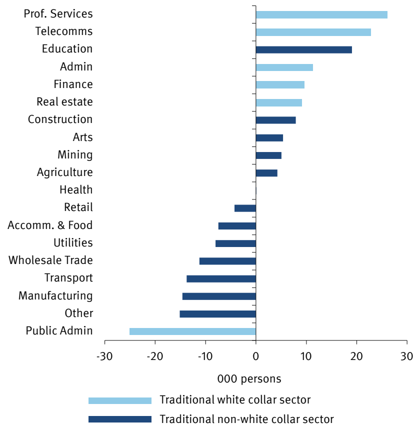
Table 2
Sydney CBD Total Vacancy Rates
July 2011 to July 2012

| Grade | July 2011 % | Jan 2012 % | **July 2012 %** |
|---|---|---|---|
| Premium | 2.5 | 7.4 | 7.8 |
| A Grade | 10.1 | 9.2 | 7.5 |
| B Grade | 10.5 | 10.1 | 7.8 |
| C & D Grade | 11.6 | 12.0 | 11.1 |
| **Total** | **9.4** | **9.7** | **8.2** |

Source: PCA/Knight Frank

Although the upside result was somewhat at odds with the anecdotal feedback from leasing agents, it was nevertheless consistent with employment data over the same period. Detailed labour statistics from the ABS for the six months to May showed that the NSW labour market increased by 0.6%. Although this growth is below the long term average, five of the top six best performing sectors were made up of sectors that traditionally drive white collar employment (Refer Figure 2). Although Public Administration was the weakest sector, a large majority of this sector is not located within the Sydney CBD, but rather suburban locations.

Figure 2
Employment growth by sector
Six months to May 2011




Source: ABS/Knight Frank

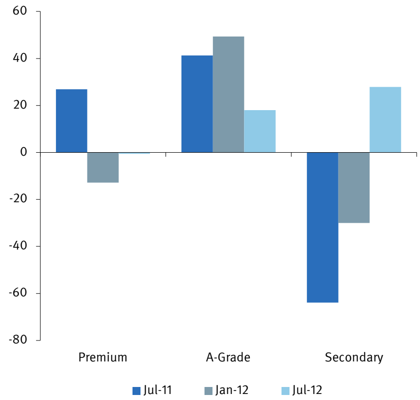
## Net Absorption

Demand proved to be strongest within A and B-grade buildings with the two grades accounting for 86% of net absorption in the six months to July. The net absorption of A-grade space has been strong for almost three years, with positive results since the beginning of 2010. However, the positive performance of B-grade absorption marked a turnaround from the negative absorption recorded in 2011. This trend has partly been enhanced by budget conscious tenants prepared to take advantage of more attractive rents and incentives available in refurbished upper B-grade stock. With the A-grade vacancy rate having fallen for three successive half year periods and likely to fall further, diminishing A-grade options in addition to cost factors are expected to sustain improved demand for upper B-grade assets.

## Anticipated Vacancy Levels

Despite the encouraging first half results, demand over the forthcoming 12 month period is expected to slow. Feedback from leasing agents suggests that tenant enquiry levels remain inconsistent with very few major tenants looking to increase occupied space in a meaningful way. Knight Frank estimates the net effect of current leasing activity in the market to be close to zero. This is based on some anticipated occupancy reductions from the accounting and finance sectors being offset by several expansions in addition to some external tenant inflows (including TAL relocating from North Sydney to 9,872m² at 363 George Street in H2 2013). The diminishing prime leasing options in non-CBD markets in conjunction with attractive CBD incentives is likely to see a continuation of this inflow trend. This subdued outlook for the next year is consistent with forward looking employment indicators such as the ANZ job advertisement series, which as at July had decreased 9.1% yoy.

Figure 3
Sydney CBD Net Absorption by Grade
(000's m²) per six month period

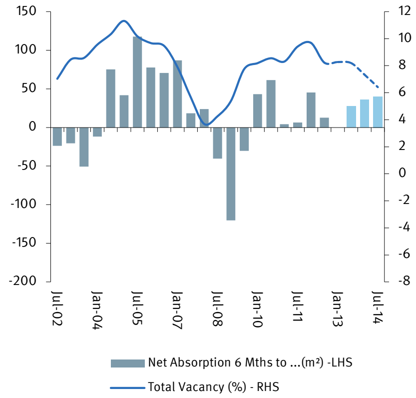



Source: PCA/Knight Frank

These conditions are forecast to play out in very modest net absorption over the next year of approximately 12,000m², equivalent to only 23% of the long term average. With net supply over the coming 12 months only slightly positive courtesy of some relatively small refurbishments coming back online, the vacancy rate is expected to hold steady over the next 12 months.

Longer term, the vacancy rate is forecast to perform somewhat of a 'V' shaped pattern. Towards the end of 2013 and into 2014, the positive impact of improved global growth is anticipated to support demand returning to levels more commensurate with long run averages. Combined with negative net supply, the vacancy rate is forecast to reduce more sharply to sub 6% by the end of 2014. However, from the end of 2015, as the next wave of supply, including Barangaroo amongst other projects, starts to reach completion the vacancy rate will start to rise. However the low vacancy starting base and the assumption of normalised demand underpins an outlook for the rise in the vacancy rate to be limited to sub 9%.

Figure 4
Sydney CBD Net Absorption & Vacancy




Source: PCA/Knight Frank

## Rental Levels

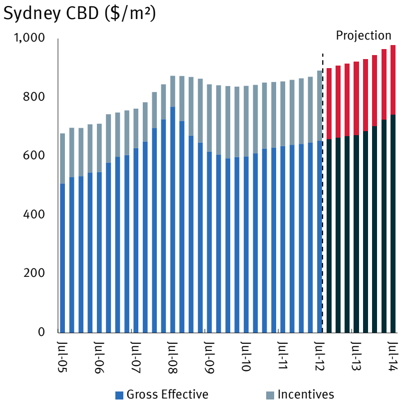
Sydney CBD prime face rents have largely tracked with CPI since the beginning of 2011 and now average \$891/m² (\$741/m² net).

However after two years of gradual reductions, the last six months saw prime gross incentives tick up marginally to 27%. The spread between prime incentives for lease renewals and new leases has started to close with renewal incentives averaging between 20% and 22.5%. This trend partly stems from the pressure on lease renewals as developers look to entice new tenants. The potential increase in sub-lease space in the next half could add further pressure to this spread closing.

Although tenants are expected to continue exercising constraint when making premises decisions over the coming six to twelve months, face rents are expected to increase at a supply-driven 3.5% over the forthcoming year with new incentives holding steady. Further ahead, the expectation of improved demand and a contracting vacancy rate is forecast to underpin a pick up in rental growth over the 2014 and 2015 financial years. Incentives are forecast to contract with a slight lag to vacancy to 24% by mid-2014 and 20% by mid-2015.

In the secondary market average face rents on a gross basis now average \$563/m² (\$440/m² net). Although prime incentives increased slightly, secondary incentives held steady at 29% on a gross basis. Incentives at this level have effectively been capped with landlords reluctant to offer a 30% incentive, however willing to negotiate on factors such as commencement date.

Figure 5
Average Prime Gross Effective Rents
Sydney CBD (\$/m²)




Source: Knight Frank

Table 3
Major Leasing Activity (New Leases over 1,000m² & Significant Renewals over 1,250m²) Sydney CBD

| Address | Precinct | Area (sqm) | Term (yrs) | Lease Type | Tenant | Start Date |
|---|---|---|---|---|---|---|
| Barangaroo - C5 | Western | ~33,750 | 14 | Pre-commit | KPMG | Jan-16 |
| Barangaroo - C5 | Western | ~21,800 | TBC | Pre-commit | Lend Lease | Jan-16 |
| Barangaroo - C4 | Western | ~57,800 | TBC | Pre-commit | Westpac | end 2015 |
| 363 George Street | City Core | 10,500 | 12 | New | TAL | 2013‡ |
| 8 Chifley Square | City Core | 8,080 | 12 | Pre-commit | Corrs Chambers Westgarth | Oct-13 |
| 60 Castlereagh Street | City Core | 2,248 | 7 | New | Centric Wealth | Jan-13 |
| 133 Castlereagh Street | Midtown | 1,714 | 7 | New | University of Sydney | Jan-13 |
| 1 O'Connell Street | City Core | 5,400 | 7 | New | Middletons | Dec-12 |
| 201 Sussex Street | Western | 3,079 | 6 | New | Adobe | Nov-12 |
| 1 Bligh Street | City Core | 3,274 | 12 | New | Oil Search | Oct-12 |
| 201 Sussex Street | Western | 1,593 | 7 | New | Urbis | Sep-12 |
| 400 George Street | Midtown | 1,803 | 10 | New | Mills Oakley Lawyers | Aug-12 |
| L6-7, 59 Goulburn Street | Southern | 1,251 | 6 | New | House of Travel | Aug-12 |
| 341 George Street | City Core | 6,400 | 5 | New | Atlassian | Jul-12 |
| 1 Bligh Street | City Core | 4,891 | 12.7 | Pre-commit | C'Wealth of Aust. | Jul-12 |
| 1 O'Connell Street | City Core | 3,100 | 10 | New | Crowe Horwath | Jul-12 |
| 20 Bond Street | City Core | 2,903 | 7 | New | Hudson Recruitment | Jul-12 |
| L3-4, 260 Elizabeth Street | Southern | 2,690 | 8 | New | Teachers Health Fund | Jul-12 |
| 1 Margaret Street | City Core | 6,756 | 13 | Renewal | PKF | May-12* |
| 1 Bligh Street | City Core | 2,642 | 12 | New | Bloomberg | May-12 |
| 133 Castlereagh Street | Midtown | 2,472 | 7 | New | Smartsalary | May-12 |
| 1 York Street | Western | 1,720 | 8 | Renewal | Clarius Group | May-12 |

Source: Knight Frank ‡ Current lease in North Sydney expires Dec 2013, however tenant move may be earlier * 10 year extension negotiated three years in advance

# INVESTMENT ACTIVITY & YIELDS

Sales activity over 2012 has slowed somewhat from the levels achieved in 2011. To date, calendar year sales in excess of $10m measure $756 million. At the same time last year, 2011 calendar year sales had reached $1.33 billion before going on the reach $2.32 billion for the whole calendar year. The slowdown in sales largely reflects the relatively limited offerings for prime core assets, which have generally been the asset type sought by investors, albeit some recent evidence suggests buyers are beginning to look further up the risk curve at core plus type assets. Nevertheless, some general caution in the market has also impacted on sales volumes with some disparity between buyer and vendor expectations on several assets being brought to market.

A number of the 2012 sales have been complicated by parties exercising pre emptive rights, which have accounted for 54% of sales by value. The largest example has been 126 Phillip Street, where Investa sold a $176.25 million, 25% share to each of Investa Commercial Property Fund (ICPF) and IOF. Although a related party transaction to some extent, the transaction reflected a core market yield of 6.35% and equated to a rate of $16,684/m². 7 Macquarie Street was another example with UniSuper exercising pre emptive rights after an expression of interest campaign. UniSuper already owned a 50% share in the asset and acquired the residual 50% from Stockland for $55 million on a core market yield of 7.3%.

While a number of offshore parties continue to seek assets in the CBD, only two purchases have been finalised so far in 2012. The most recent was by Blackstone, who acquired 149 Castlereagh Street for $40.6 million. The unoccupied asset was sold by Ernst and Young who were receivers acting on behalf of Allco Property Development Fund No.1. Prior to this, the Chinese-backed developer Maville Australia Group acquired 333 Kent Street in February. The asset, located in the western corridor, was sold fully leased with a 5.2 year WALE for $47.75 million and equated to a core market yield of 8.4%.

The trend of offshore parties participating as wholesale JV partnerships with local developers has also continued in 2012. Lend Lease has launched a new commercial wholesale trust to fund the development of the first two commercial towers at Barangaroo South, to be known as “International Towers Sydney”. The trust has received commitments for $2 billion in funding with a $1 billion commitment from the Canada Pension Plan Investment Board supplemented by Lend Lease committing up to $500 million and a further $500 million in total from local wholesale investors APPF Commercial, First State Super and Telstra Super.

Table 4
Recent Sales Activity Sydney CBD

| Address | Price ($ mil) | Core Mrkt Yield (%) | NLA (m²) | $/m² NLA | WALE (yrs) | Vendor | Purchaser | Sale Date |
|---|---|---|---|---|---|---|---|---|
| 50 Carrington St≈ | 58.5 | 8.0 | 11,293 | 5,180 | 2.2 | REST | DEXUS | Jul-12› |
| 60 Clarence Street | 14.25 | 6.8 | 1,846 | 7,719 | 4.7 | Harbour & Co | Private Investor | Jul-12 |
| 7 Macquarie Place | 55.00^ | 7.3 | 13,582 | 8,099 | 2.7 | Stockland | UniSuper | Apr-12 |
| 161 Clarence Street | U/D | ‡ | 2,902 | U/D | VP | Brookfield Multiplex | Crown International | Mar-12 |
| 149 Castlereagh St | 40.60 | VP | 13,947 | 2,911 | VP | Ernst & Young as Receiver (Allco) | Blackstone | Mar-12 |
| 48-50 Martin Pl & 9-19 Elizabeth St | circa 150.00 | VPɨ | 25,344 | ~5,919 | n/a | CBA | Macquarie | Mar-12 |
| 126 Phillip Street | 176.25* | 6.35 | 42,256 | 16,684 | 4.7 | Investa Property Group | ICPF#/Investa Office Fund† | Mar-12 |
| 333 Kent Street | 47.75 | 8.4 | 8,938 | 5,342 | 5.2 | AMB Property | Maville Group Aust. | Feb-12 |
| Bond Store 3 | 17.00 | 9.0 | 3,653 | 4,655 | 1.7 | PPB Advisory | Primewest | Feb-12 |
| 20 Bridge Street | 185.00 | 7.0 | 19,799 | 9,344 | 4.8 | Korda Mentha as Receiver (BOSI) | RREEF | Dec-11 |
| 50 & 54 Park Street | 90.00 | n/a | 18,138 | 4,962 | circa 5 | AMP | Kyko Group | Nov-11 |
| 140 Sussex Street | 84.00 | 7.8 | 12,440 | 6,752 | 5.6 | Eureka Funds Management | RREEF | Nov-11 |

Source: Knight Frank
^ 50% share
* 25% share
† Pre-emptive right to acquire 25% share
› Settlement due November 2012
U/D refers undisclosed
# exercised pre-emptive right to acquire 25% increasing ownership to 50%
~ Represents $2.1m income support provided by the vendor
‡ bought for residential re-development
≈ Reported
VP refers vacant possession
ɨ bought for owner occupation

While the majority of 2011 sales were underpinned by demand for large core assets, some sales such as 309 George Street and 20 Martin Place were starting to indicate some willingness for investors to look further up the risk curve. Opportunistic value add plays continue to sit on the radar for investors such as the recently announced purchase by DEXUS of 50 Carrington Street. DEXUS acquired the asset for $58.5 million on a relatively short 2.2 year WALE with two thirds of the building occupied. The purchase reflected a passing yield of 5.2%, however equated to a reported core yield of 8.0%.

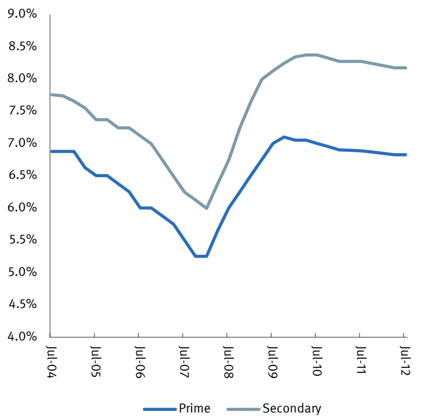
Assets within the sub $20 million range continue to perform well with interest from a number of smaller private investors enhancing the market depth for assets of this relative size. This was seen with the July sale of 60 Clarence Street, where the fully leased asset of 1,846m² NLA was acquired on a relatively tight core market yield of 6.8%.

Although a degree of yield tightening amongst prime assets was evident around six months ago following the completion of some major transactions including 126 Phillip Street, yields have broadly remained steady since. Average core market yield ranges are estimated to range between 6.25% to 7.25% for prime and 7.75% and 8.75% for secondary assets.

Figure 6

Sydney CBD Average Yields

Prime and Secondary Core Market Yields




Source: Knight Frank

# OUTLOOK

Although CBD tenant demand remains inconsistent, the lack of forthcoming supply over the next three years is set to underpin a tightening market. The vacancy rate is expected to hold steady over the coming 12 months, however forecasts of negative net supply out to the end of 2014 is forecast to underpin a reduction in the vacancy rate to 7.3% by the end of 2013 and 5.5% by the end of 2014. This assumes a continuation of subdued demand for the next 12 months before a gradual improvement in FY 2014. It is noted that soft organic growth in tenant demand (and in some cases tenant downsizing) in the short term will be offset somewhat by some pending tenant moves from outside the CBD area. Some IT related tenant enquires have the potential to further supplement demand, however the forecast has not included these enquires given the uncertainty around timing.

Rental forecasts reflect this pattern. Over FY 2013, face rental growth is expected to track slightly in excess of CPI at 3.5%, with incentives showing no downward movement. However expectations of improved tenant demand in FY2014 will see expanding tenants faced with fewer options given the next wave of development is unlikely to start completing in a meaningful way until at least 2015. This is forecast to see prime face rental growth in FY2014 and FY2015 increase to an average of 6.0% per annum. Prime gross incentives are forecast to start reducing from FY2014 to reach 20.0% by mid 2015. This will underpin prime effective rental growth averaging approximately 10% per annum during FY2014 and FY2015. While fluctuations in sentiment stemming from Europe will likely persist, this forecast is based on no material deterioration going forward.

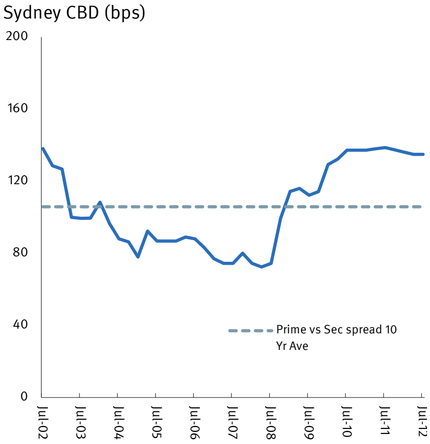
Offshore investor interest in Australian CBD markets remains firm despite the reduction in recorded transactions over 2012. This fall has partly been attributable to factors such as the persistently high $AUD and some uncertainties surrounding the tax regime following the doubling of the MIT final withholding tax. Nevertheless, the low cost of debt, relative attractiveness of Australia's office yields and stable capital values will remain attractive attributes for offshore investors. These factors are expected to support sales levels over the remainder of 2012 with one transaction to an offshore party of circa $100 million currently in final negotiations. Helping to fill the transaction gap in the market is the emerging buying activity by local groups. The acquisitions by DEXUS and Investa have both shown that local participants will look for earnings accretive opportunities. The low cost of debt, particularly in a relative sense to yields provides scope for buying activity to improve on the levels recorded thus far in 2012, while in the listed space, the narrowing gap between trading prices and NTA will also support AREITs looking at acquisitions.

A number of factors suggest a tightening bias for core yields including positive expectations for rental growth, large spreads to debt levels and yields sitting at above average levels. Although the tightening in yields since 2009 has favoured well tenanted, prime assets, the above average spread between prime and secondary yields continues to present value opportunities for secondary assets. Nevertheless, with the cost and availability of debt favouring prime assets and tenant movements concentrated in A-grade or upper B-grade assets, this yield spread will likely persist over 2012.

Figure 7

Risk premium – Prime vs Secondary

Sydney CBD (bps)




Source: Knight Frank

# RESEARCH

**Americas**
USA
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Ireland
Italy
Monaco
Poland
Portugal
Romania
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