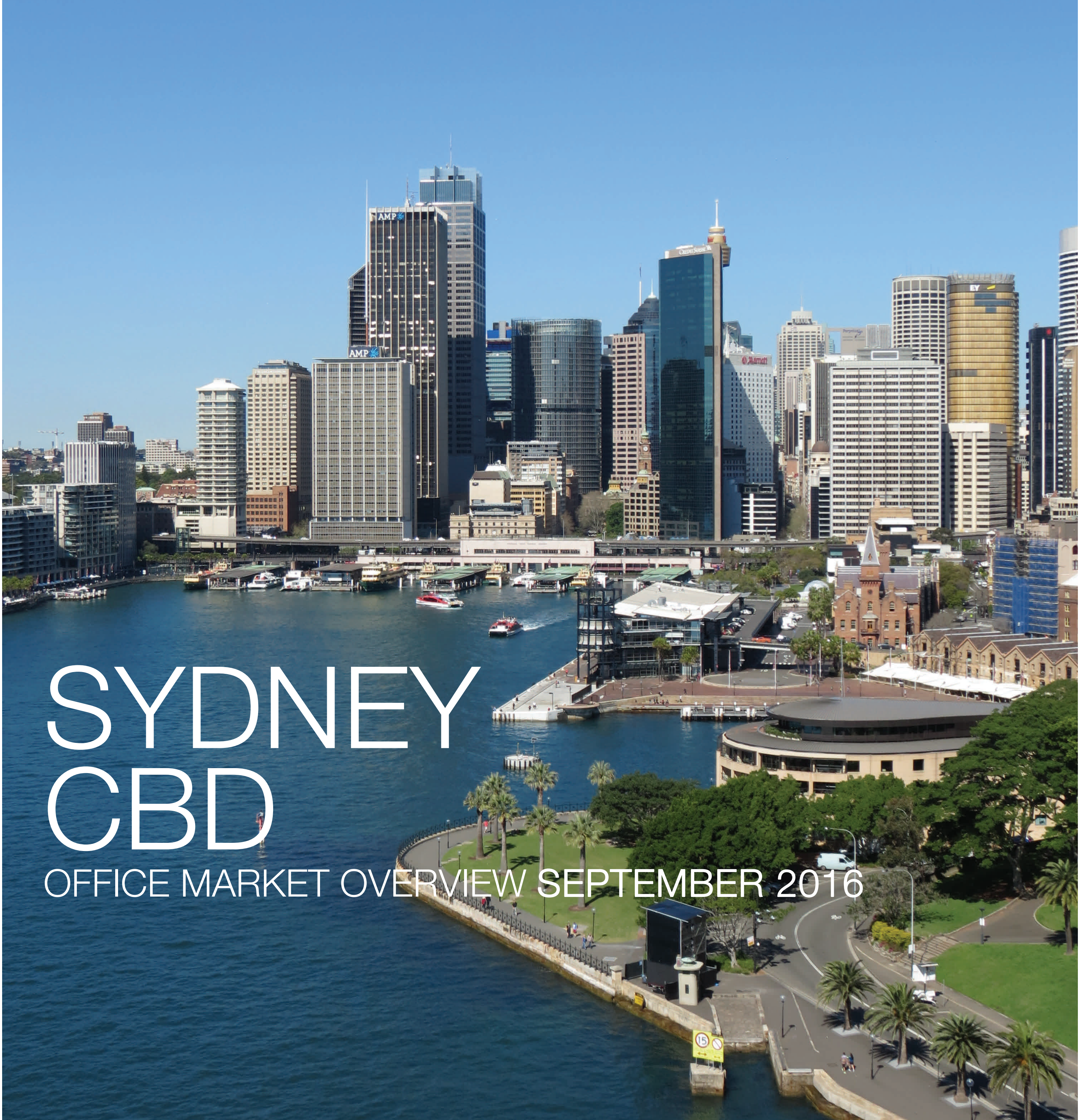
RESEARCH

Knight Frank



SYDNEY CBD

OFFICE MARKET OVERVIEW SEPTEMBER 2016

HIGHLIGHTS

The significant withdrawal of stock (circa 539,099m^2 over the next four years) amid declining gross supply could potentially lead to a period of undersupply in the Sydney CBD, post completion of Barangaroo.

Secondary rental growth outperformed prime rental growth, with gross effective growth rates measuring 16.6% and 13.2% respectively in the 12 months to July 2016.

About 10,000 new white-collar jobs have been added to the Sydney CBD employment pool over the 2016 financial year. This represents annual growth of 3.3%, triple the 10 year average of 1.1%.

KEY FINDINGS

Up to 539,099m^2 of office stock in the Sydney CBD is expected to be withdrawn permanently from 2016 to 2019.

The strong withdrawal pipeline amid declining gross supply could potentially send the Sydney CBD to a period of under supply beyond 2017.

The Sydney CBD office market recorded double-digit rental growth in the 12 months to July 2016 with secondary and prime gross effective rental growth rates measuring 16.6% and 13.2% respectively.

The overall vacancy rate is expected to fall to 3.5% by the end of 2018 with secondary vacancies declining at a faster pace than prime vacancies.

A distinct lack of investable stock coupled with improved leasing fundamentals in the Sydney CBD will ensure the investment market remains tight going forward.

ALEX PHAM
Senior Research Manager

SUPPLY & DEVELOPMENT

The Sydney CBD is entering a period of unprecedented stock withdrawals, with 585,682m^2 earmarked for permanent withdrawal over the next four years.

The Sydney CBD market is entering a period of significant withdrawal of stock for Sydney Metro construction, residential conversion or re-development. The first half of 2016 saw 110,731m^2 withdrawn from the market, more than half of which was withdrawn permanently. On an annual basis, 157,948m^2 has been taken offline in the 12 months to July 2016, the highest withdrawal level in 18 years.

Permanent withdrawals for alternative uses in the first six months of 2016 include 234 Sussex Street (11,107m^2—converted to residential), 130 Elizabeth Street (9,140m^2—residential), 110 Bathurst Street (1,428m^2—hotel) and 230 -232 Sussex Street (1,022m^2—hotel). In addition, a number of existing buildings have also been withdrawn for re-development. These include 182 George Street and 33-35 Pitt Street (26,206m^2 in total) and 151 Clarence Street (15,280m^2).

On the other hand, supply additions were equally strong with 126,474m^2 of new stock having been added to the CBD market over the six months to July 2016. This is more than double the 10 year gross supply average of 60,842m^2 and has taken the rolling annual gross supply to 275,972m^2 as at July 2016.

Underpinning the supply pipeline in the first half of 2016 was the completion of Barangaroo Tower 3 (79,221m^2—76% committed), 200 George Street (38,676m^2—100% committed) and the refurbishment at 1 Farrer Place (GMT) (8,532m^2—fully leased).

On a net supply basis, 15,734m^2 of office space has been added to the market in the six months to July 2016. This is relatively in line with the 10 year average of 14,947m^2.

Looking ahead, we expect the gross supply pipeline to remain fluid for the remainder of 2016, with circa 120,000m^2 coming online. The new supply will include 101,729m^2 at Barangaroo Tower 1 (48% committed), 12,500m^2 at 333 George St (92% committed) and 6,713m^2 at One Wharf Lane, 161 Sussex Street (22% committed).

Beyond 2016, the projected supply is expected to taper off significantly whilst withdrawals accelerate due to the construction of Sydney Metro and residential conversion. These dynamics could potentially lead to a period of undersupply in the Sydney CBD office market in the medium term.

Knight Frank is tracking up to 539,099m^2 of office stock earmarked to be withdrawn permanently over the 2016-2019 period. This is equivalent to 10.6% of the total stock at the beginning of 2016. In addition, a further 300,000m^2 is expected to be temporarily withdrawn for refurbishment over the same period.

Major withdrawals for residential conversion over the next two years will include 1 Alfred St (27,118m^2) and 71 Macquarie St (9,447m^2). In addition, the construction of the Sydney Metro project will see 39 Martin Place (14,525m^2), 55 Hunter St (13,622m^2) and 175 Castlereagh St (11,848m^2) being demolished in 2017. Beyond this, significant withdrawals will occur at AMP's proposed Quay Quarter Sydney (QQS) re-development. Construction of the new buildings will remove up to 75,000m^2 of existing stock.

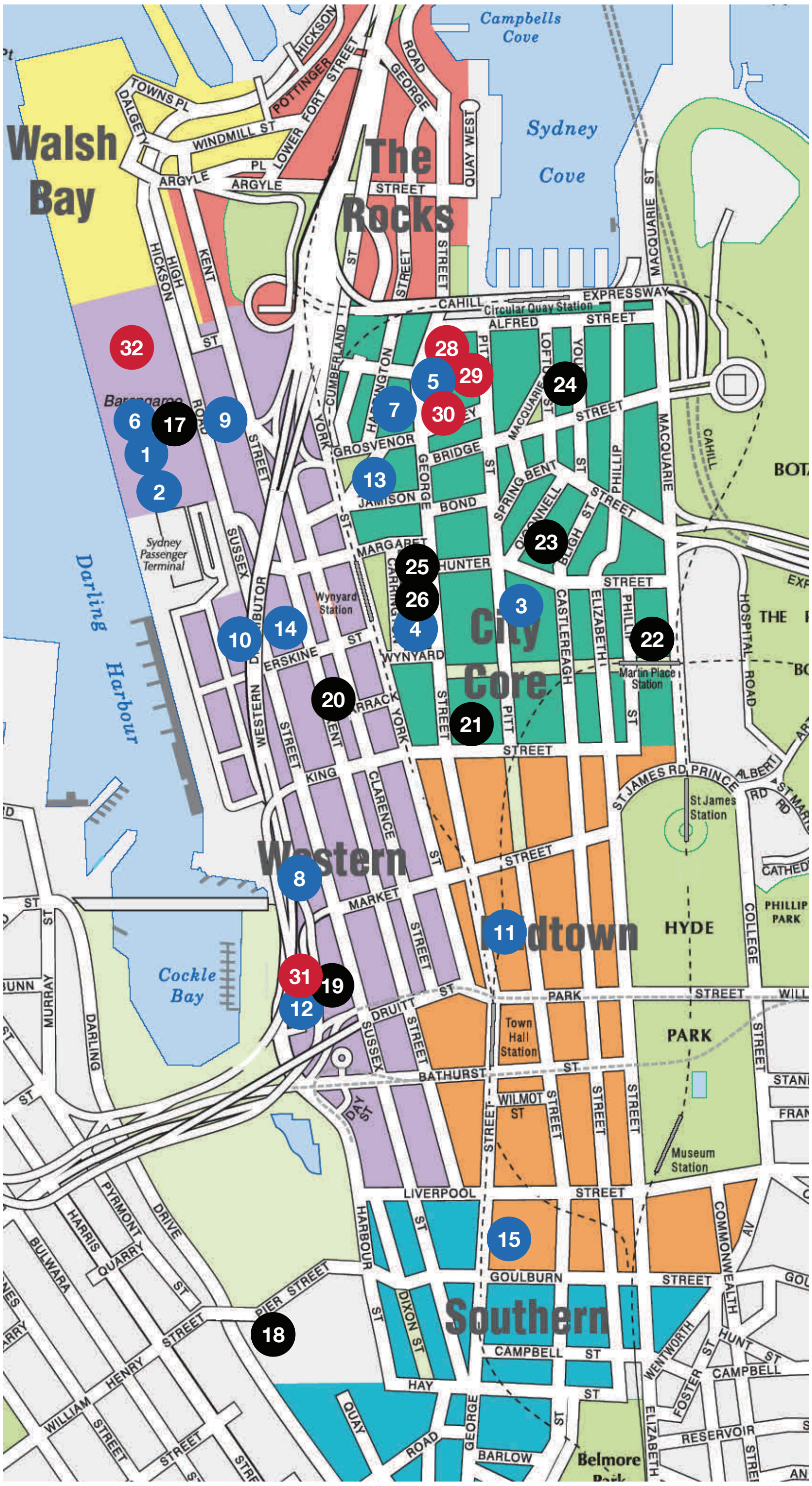
TABLE 1
Sydney CBD Office Market Indicators as at July 2016

Grade	Total Stock (m^2)	Vacancy Rate (%)	Annual Net Absorption (m^2)	Annual Net Additions (m^2)	Average Gross Face Rent* ($/$m^2$)	Average Incentive* (%)	Average Core Market Yield (%)
Prime	2,858,074	6.7	192,198	218,021	900 - 1,200	25.0 - 29.0	5.00 - 5.75
Secondary	2,224,141	4.1	-44,953	-99,997	650 - 850	19.0 - 25.0	6.00 - 6.75
Total	5,082,215	5.6	147,245	118,024			

Source: Knight Frank Research/PCA *Assuming full floor, mid rise, clear space and a 5 year lease

MAJOR OFFICE SUPPLY

1. Barangaroo T2 - 88,200m² [Westpac/Gilbert + Tobin/St George/BT]
LLITST - Q3 2015 - 89% committed
2. Barangaroo T3 - 79,221m² [KPMG/Lendlease]
LLITST - Q2 2016 - 76% committed
3. 80 Pitt St# (ex QBE) - 11,400m²
Yorkban P/L - Q1 2017 - 0% committed
4. 333 George St - 12,500m² [Clyde & Co/Aimia/WeWork]
Charter Hall Core Plus Office Fund - Q3 2016 - 92% committed
5. 200 George St - 38,676m² [EY/Mirvac]
Mirvac/AMP - Q2 2016 - 100% committed
6. Barangaroo T1 - 101,729m² [PWC/HSBC/Marsh & McLennan]
LLOneITST - Q4 2016 - 48% committed
7. 225 George St# (ex Ashurst) - 15,789m² [JLT]
DEXUS/CIC/CSC - H1 2016 - c.87% committed
8. One Wharf Lane, 161 Sussex St - 6,713m²
M&L Hospitality - Q3 2016 - 22% committed«
9. 30 The Bond, 30 Hickson Rd# (ex Lendlease) - 16,228m² [Roche]
DEXUS - H2 2016 - 31% committed
10. 10 Shelley St# (ex KPMG) - 27,778m² [Suncorp]
Brookfield - H1 2017 - 100% committed
11. 255 Pitt St# (ex Challenger, Apple) - 15,427m²
ISPT Core Fund - H1 2017 - 75% committed
12. 201 Sussex St, DPIII# (ex Marsh & McLennan) - 10,343m² [Advant]
GPT (GWOF)/AMP (ACPF)/Brookfield - H1 2017 - 48% committed
13. 259 George St# (ex Suncorp) - 20,352m²
Memocorp Australia - H2 2017
14. 275 Kent St# (ex Westpac) - 16,130m²
Blackstone/Mirvac - H2 2017
15. 680 George St# (ex EY) - 28,033m²
Brookfield/Arcadia - 2017
16. 55 Market St# (ex St. George)§ - 4,644m²
CIC - Q3 2016
17. Barangaroo C1 & C2 - circa 19,160m²
LLOneITST - 2019+ - 0% committed
18. Darling Square, Haymarket - 20,000m²> [CBA]
Lendlease - H1 2018 - 100% committed
19. 201 Sussex St, DPII# (ex PWC) - 33,000m² [IAG]
GPT (GWOF)/AMP (ACPF)/Brookfield - 2018 - 100% comm.
20. 151 Clarence St - 19,910m² [Arup]
Investa - Q3 2018 - 29% committed
21. 388 George St# - 36,151m² (ex IAG)
Investa/Brookfield - Q4 2018 - 0% committed
22. 60 Martin Place - 40,000m²
Investa/Gwynvill Group - H2 2019 - 0% committed
23. 33 Bligh St - 26,000m²
Energy Australia/Investa - 2020+ - 0% committed
24. Quay Quarter Sydney (QQS) - 90,000m²
AMP - 2021+
25. 275 George St - c. 7,000m²
LaSalle Investment Management - 2019+
26. Wynyard Pl - 68,000m² [NAB]
Brookfield - 2020 - 44% committed
27. 255 George St# - 22,500m² (ex NAB)
AMP - 2020
28. CQ Tower, 182 George & 33 Pitt St - 55,000m²
Lendlease - 2021+
29. 55 Pitt St - 30,000m²+
Mirvac - 2020+
30. 210 & 220 George St - 17,000m²
Poly Real Estate - 2021+
31. Darling Park Tower 4 - 70,000m²
GPT/Brookfield/AMP - 2022+
32. Central Barangaroo - TBC#
TBC* - 2024+



Source of map: Knight Frank

- Under Construction/Complete
- DA Approved / Confirmed / Site Works
- Mooted / Early Feasibility

NB. Dates are Knight Frank Research estimates.

Includes select CBD major office supply (NLA quoted)

Major tenant precommitment in [brackets] next to NLA

LLITST refers Lend Lease International Towers Sydney Trust (50% CPPIB, 25% APPF Commercial, 15% Lend Lease, 10%

LLOneITST refers Lend Lease One International Towers Sydney Trust (37.5% Lend Lease, 37.5% QIA, 25% APPF Commercial)

Major refurbishment/backfill

« 2 floors of 1,491.4m² are under offer as at September 2016.

§ Westpac extended lease for 3 years.

> Office NLA only. Total NLA is 27,900m².

≠ Under the current plans, a maximum above-ground GFA of 150,000 m² and an unlimited amount underground are allowed. It is uncertain how much of this will be office space as at September 2016.

*A consortium consisting of Grocon, Scentre and Aqualand is reportedly the lead contender for development rights.

TENANT DEMAND & RENTS

Tenant demand in the Sydney CBD continued its momentum, evidenced by the net absorption of 53,162m^2 in the six months to July 2016. This is more than double the 10 year average of 23,450m^2. On an annual basis, 147,245m^2 has been absorbed over the 2016 financial year. This is the second strongest level of demand in eight years, following the strong absorption of 157,150m^2 in 2015.

Absorption was particularly strong in the prime market, with an annual net take-up of 192,198m^2 as at July 2016. This is the strongest level of absorption in the last decade and a reflection of the upgrading that is occurring and strengthening demand for prime space in the CBD.

Underpinning this strong demand in the Sydney CBD is the relocation of a number of tenants from the Fringe and suburban markets into the CBD. A recent example was Flexigroup relocating from St Leonards to circa 3,600m^2 over three floors at 179 Elizabeth Street. Looking forward, the completion of 333 George Street will see AIMIA moving from Pyrmont to join Clyde & Co and WeWork as anchor tenants.

In addition, Roche is expected to relocate to 5,000m^2 at 30 The Bond from the northern suburb of Dee Why, where their headquarters are being sold for potential residential conversion. Another suburban tenant being driven out of their current premises due to residential development is Reckitt Benckiser moving from West Ryde to circa 3,000m^2 A-Grade space at 680 George Street. Within the Sydney CBD, the depletion of secondary stock has seen some secondary tenants moving up to the prime market, resulting in the net outflow of –2,662m^2 in the secondary market in the six months to July 2016.

We expect this trend to continue over the next six months with Navitas upgrading from a C-Grade location (Wynyard Green 17 York Street) to an A-Grade building (255 Elizabeth Street), absorbing the space left by Westpac moving to Barangaroo.

Other secondary-to-prime moves will include Propex relocating from 299 Elizabeth Street (B Grade) to 66 Goulburn Street (A Grade), Maison Global transferring from 22 Market Street (B Grade) to 233 Castlereagh Street (A Grade) and TNS upgrading from a B-Grade building at 6 O'Connell Street to an A-Grade at 123 Pitt Street.

The Finance and Technology sectors continued to drive the strong take-up in the Sydney CBD market in the last 12 months. About 10,000 new white-collar jobs had been added to the Sydney CBD employment pool over the 2016 financial year. This represents annual growth of 3.3%, triple the 10 year average of 1.1%.

On the back of this strong tenant demand, the vacancy rate in the CBD fell to 5.6% in July 2016 from 6.3% in January 2016. This is the lowest level of vacancy in the Sydney CBD market since 2009, and 170bps below the 10 year average of 7.3%. This is indicative of a landlord's market and places upward pressure on rents.

Notwithstanding the decline in the overall vacancy rate, there are significant divergences in vacancy rates across the different grades and precincts. Whilst the secondary vacancy rate fell sharply from 6.2% in January 2016 to 4.1% in July 2016, as a result of the significant withdrawal of secondary stock, the prime vacancy rate increased from 6.2% to 6.7% over the corresponding period (Figure 2). The increase in the prime vacancy rate was chiefly due to the delivery of the two Barangaroo towers (T2 and T3—167,421m^2 collectively).

Correspondingly, the Western Corridor (including Walsh Bay and Barangaroo) recorded the highest level of vacancy of 7.1% as at July 2016. Excluding Barangaroo, the Western vacancy rate was only 2.6% as at July 2016.

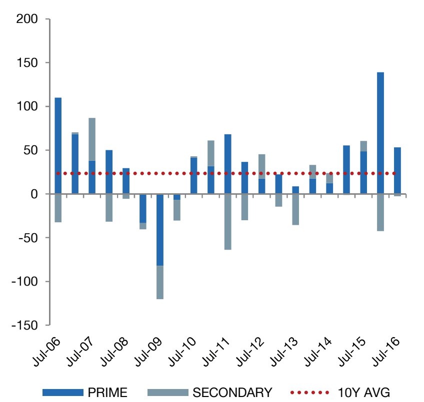
At the Barangaroo precinct, there is still 38,325m^2 of vacant space across T2 and T3 as at July 2016, or circa 87,626m^2 once T1 is included by the end of 2016. Therefore, prime vacancies are expected to remain elevated in the short term at Baragaroo. However, the opening of Wynyard Walk in mid-September 2016 coupled with declining secondary stock and rising rents may see some tenant demand channelled through to the Western Corridor from the other CBD precincts in the next 12 months.

At the other end of town, the Southern precinct remained the tightest sub-market in the Sydney CBD with a vacancy rate of 2.2%, followed by Midtown at 4.8%. These precincts have been characterised by the lack of new developments in addition to office stock lost to residential encroachment over the last few years.

FIGURE 1

Sydney CBD Net Absorption

Per six month period, by Grade (m²)

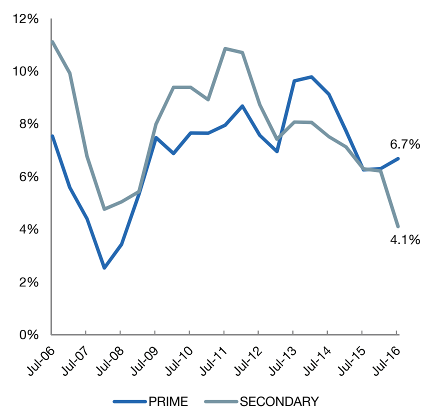


Source: Knight Frank Research/PCA

FIGURE 2

Sydney CBD Vacancy Rate

By Grade (%) - Past decade

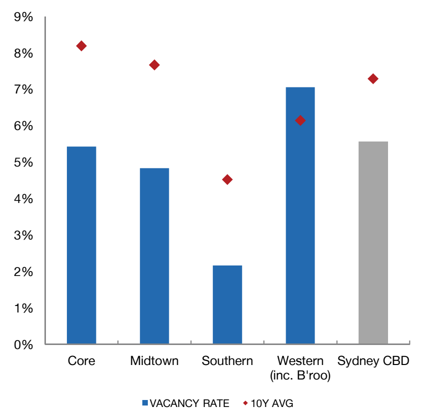


Source: Knight Frank Research/PCA

FIGURE 3

Sydney CBD Vacancy Rate

By Precinct (%) - July 2016



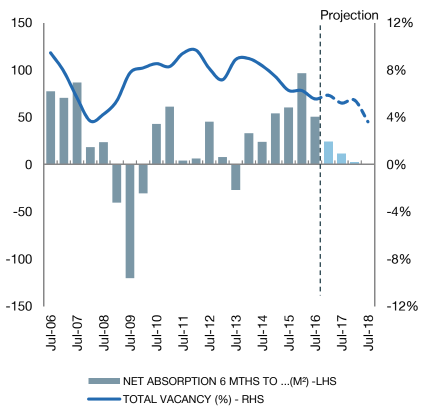
Source: Knight Frank Research/PCA

Anticipated Vacancy Levels

Looking forward, the overall vacancy rate in the CBD is expected to fall to 5.4% and 3.5% by the end of 2017 and 2018 respectively. Vacancies in the secondary market are forecast to decline at a faster pace than the prime market due to stock withdrawals. This will lead to some secondary tenants moving to the prime market or out of the CBD.

Beyond 2018, we anticipate the overall vacancy rate to revert back to the long term average at around 7.0% to 7.5% once the next development cycle commences. However, we expect secondary vacancies to remain low as the lack of secondary stock persists.

FIGURE 4
Net Absorption & Vacancy
Sydney CBD, per six month period (000's m², %)



Source: Knight Frank Research/PCA

Rental Levels

On the back of positive tenant demand and falling vacancies, rents have risen sharply across the prime and secondary markets, and moreso in the secondary market where the majority of withdrawals have occurred.

As a consequence, the average secondary gross face rent increased by 9.9% in the 12 months to July 2016 to $753/m² ($623/m² net). The secondary incentives declined to between 19% and 25% in July 2016 from above 28% a year ago, resulting in an gross effective growth rate of 16.6% in the 12 months to July 2016. This has taken the average secondary gross effective rent to $574/m² as at July 2016.

The lack of options in the secondary market is seeing gross rents at the top end of the B-Grade market sitting at circa $950/m² and pushing through $1,000/m² in some cases as at July 2016. At the same time, gross incentives for subdivided floors or small suites in some secondary buildings have fallen below 19%.

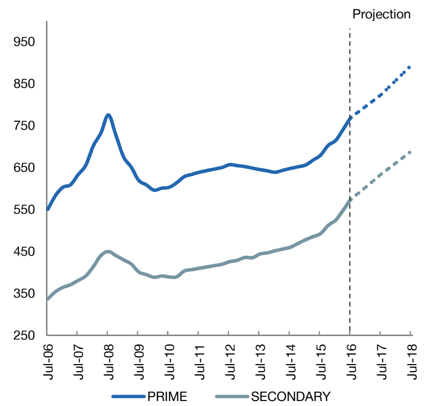
The prime market has also recorded healthy rental growth in the last six months, albeit not as strong as the secondary market. The average prime gross face rent rose by 9.2% YOY to $1,061/m² ($896/m² net). Prime incentives also decreased from above 30% in July 2015 to around 25% and 29% as at July 2016, boosting the average prime gross effective rent by 13.2% YOY to $769/m².

Looking ahead, the declining net supply of secondary stock is expected to see secondary rental growth continue to outperform prime rental growth over the next two years and the spread between prime and secondary rents will narrow.

Accordingly, the average secondary gross face rent is forecast to grow by an average of 7.0% p.a. over the next two years. Furthermore, secondary gross effective rent growth will be boosted to 9.6% p.a. due falling secondary incentives.

In the prime market, gross face rents are expected to rise by 5.0% p.a., whilst declining prime incentives will lift prime gross effective rents by 7.9% p.a. over the next two years.

FIGURE 5
Average Gross Effective Rents
Sydney CBD ($/m²)



Source: Knight Frank Research

TABLE 2
Recent Leasing Activity Sydney CBD

Address	Precinct	NLA (m²)	Term (yrs)	Lease Type	Tenant	Sector	Start Date
201 Sussex Street	Western	5,180	5	Direct	Avant Insurance	F&I	Apr-17
20 Bond Street	Core	1,035	5	Direct	New Zealand	Government	Dec-16
20 Bond Street	Core	669	5	Direct	Koda Capital Services	F&I	Dec-16
7 Macquarie Place	Core	539	5	Direct	The Customer Experience	TMT	Nov-16
20 Bond Street	Core	1,035	5	Direct	Bennelong Funds	F&I	Oct-16
2 Park Street	Midtown	420	5	Direct	Grandview	Real Estate	Sep-16
2 Park Street	Midtown	251	5	Direct	LATAM Airlines	Industrials	Sep-16
126 Phillip Street	Core	219	5	Direct	CECEP	Energy	Sep-16
123 Pitt Street	Core	500	6	Direct	TNS	TMT	Sep-16
2 Chifley Square	Core	1,288	5	Direct	KordaMentha	F&I	Aug-16
52 Martin Place	Core	263	5	Direct	Active International	TMT	Aug-16
175 Liverpool	Midtown	600	5	Direct	Ticketek	TMT	Aug-16
2 Park Street	Midtown	220	5	Direct	Country Garden	Real Estate	Aug-16
83 Clarence Street	Western	73	3.42	Direct	Watermark	Recruitment	May-16

Source: Knight Frank Research TMT refers Technology Media & Telecommunications

INVESTMENT ACTIVITY & YIELDS

The first seven months of 2016 saw $2.3 billion worth of office buildings transacted in the Sydney CBD. This has taken the rolling annual investment volume to $4.2 billion as at July 2016. As anticipated, this has fallen 35% short of the strong $6.4 billion in the 12 months to July 2015. The softer investment volumes can be attributed to a number of factors including; a distinct lack of stock available for buyers as well as limited re-investment opportunities for owners.

The largest office transaction recorded since the beginning of 2016 was the acquisition of the Macquarie building at 1 Shelley Street by Charter Hall and Morgan Stanley for $525 million from Brookfield Office Property. The deal was done on an core market yield of 5.35% and a 7.5 year WALE.

Another "trophy" acquisition was the purchase of 420 George Street, an A-Grade building with an NLA of 37,688m², by Investa and Mercer in two tranches. The initial 75% stake was acquired by Investa Commercial Property Fund from Fortius Active Property Trust No.1 for $442.5 million. The remainder 25% was subsequently purchased from Lendlease's Australian Prime Property Fund Commercial, for a new Investa-managed wholesale fund backed by Mercer, for about $150 million. The deals were done on a core market yield of circa 5.20% and a 5.2 year WALE.

In the secondary market, investment activity remained solid with offshore investors continuing to set the pace. Among the major secondary transactions was the purchase of 210 & 220 George Street for a total consideration of $160 million by Chinese Poly Group from Anton Capital, representing Goldman Sachs. The buildings with a total NLA of 13,674m² are expected to be re-developed in the next three years.

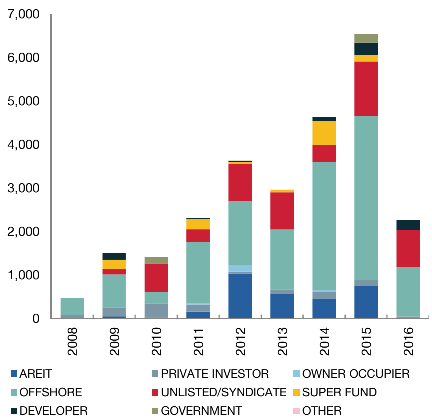
Malaysian investment group Citadin has sold two of their properties in the CBD at 284-287 Elizabeth Street and 10-14 Quay Street to different offshore groups. The buildings at 284-287 Elizabeth Street with a total NLA of 5,566m² were sold to a Hong Kong-based private investor on an initial yield of 4.9% and a WALE of 3.0 years. Another Hong Kong-based private investor acquired 10-14 Quay Street (4,381m² combined NLA) on a tight initial yield 3.9%. These firm yields are a further indication of the strong appetite of offshore investors recently, particularly from Hong Kong purchasers, for CBD assets with re-development potential.

Another example of offshore buyers purchasing office buildings for re-development was Chinese Macrolink Group, in partnership with local

FIGURE 6

Sydney CBD Sales $10 million+

By Purchaser Type ($m)



Source: Knight Frank Research
N.B. 2016 figure is year to July 2016

TABLE 3

Recent Sales Activity Sydney CBD

Address	Price ($ mil)	Core Mkt Yield (%)	NLA (m²)	$/m² NLA	WALE (yrs)	Vendor	Purchaser	Sale Date
284-287 Elizabeth St	55.00	4.90*	5,566	9,881	3.0	Citadin	AMA Holdings (HK)	Jul-16
10-14 Quay St	42.00	3.90*	4,381	9,587	N/A	Citadin	George 777 Pty (HK)	Jul-16
220 George St[×]	109.19	N/A	8,916	12,246	c.3.0	Anton Capital (G.S.)	Poly Real Estate	Jul-16
210 George St[×]	50.81	N/A	4,758	10,679	c.3.0	Anton Capital (G.S.)	Poly Real Estate	Jul-16
420 George St (25%)[≡]	150.00	c.5.20	37,688	15,920	5.2	Lendlease (APPFC)	Investa/Mercer	Aug-16
140 Sussex St	130.00	c.5.75	12,440	10,450	1.2	RREEF	Bank of China	Jun-16
3 Spring St	70.00	c.6.50	7,450	9,396	c.5.0	Christie	Brookfield	Jun-16
1 Shelley St	c.525.00	c.5.35	32,986	15,916	7.5	Brookfield	Charter Hall/MSRE	May-16
420 George St (75%)[≡]	442.50	c.5.20	37,688	15,655	5.2	Fortius (FAPT1)	Investa (ICPF)	Apr-16
71 Macquarie St[+]	158.50	N/A	9,447	16,778	N/A	AMP Capital	Macrolink/Landream	Mar-16
149-151 Castlereagh St	120.00	6.04	12,855	9,335	4.4	Blackstone	Deutsche AM	Mar-16
77 King St	160.00	5.76	13,626	11,742	4.2	Keppel REIT	ARE Noble	Jan-16
61 York St	33.00	5.19	3,091	10,678	1.8	Nick Manettas	Levanai Nominees	Dec-15
60 Margaret St (50%)	279.5	5.72	46,826	9,935	4.5	MTAA	Pacific Alliance Group	Dec-15

Source: Knight Frank Research *Initial yields G.S refers Goldman Sachs MSRE refers Morgan Stanley Real Estate APPFC refers Lendlease-managed Australian Prime Property Fund Commercial FAPT1 refers Fortius Active Property Trust No.1 ICPF refers Investa Commercial Property Fund

×Purchased in one line. To be redeveloped. ≡ acquired by Investa and Mercer in two tranches +To be converted to residential developer Landream, acquiring the former Coca-Cola site at 71 Macquarie Street for $158.5 million. The existing office building of 9,447m^2 is expected to be converted to a mixed-used tower consisting of residential units, serviced apartments and retail component on the ground floor.

Since the beginning of 2016, offshore investors have been equally active on both the buy and sell sides of the market (Figure 7). Whilst offshore privates continued to dominate the buy side, offshore institutions were the biggest sellers since the beginning of the year. Offshore vendors in the last seven months include global investment bank Goldman Sachs (through Anton Capital), Deutsche Bank's RREFF, Canadian Brookfield, US-based Blackstone (via 151 Property) and Singaporean Keppel REIT.

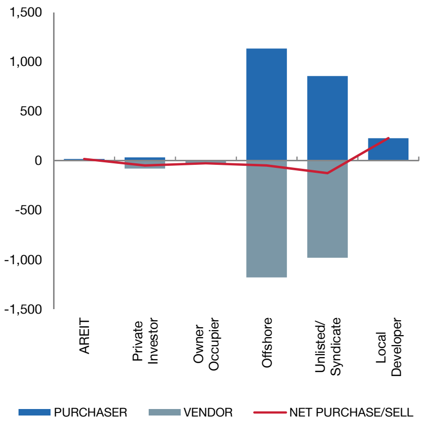
On a net purchasing basis, local developers were the most active purchasers whilst unlisted funds were the most active sellers since the begin of 2016. Underpinning the strong activity by developers is the elevated leasing markets coupled with the prospect of an undersupply of office space in the Sydney CBD over the next few years. These dynamics have also seen some local funds focusing on development to grow their asset pools rather than direct acquisition as yields are at their historical lows.

With respect to yields, both the prime and secondary markets have seen further tightening over the first six months of 2016. However, as anticipated, the rate of yield compression in the prime market has moderated, registering a slight decline of 6bps in the last six months. As at July 2016, prime assets with 5 year WALEs are expected to trade on between 5.00% and 5.75% core market yields.

In the secondary market, yields continued to compress on the back of the lack of stock and improving leasing fundamentals. In the six months to July 2016, secondary yields saw a further compression of approximately 25bps to measure between 6.00% to 6.75%.

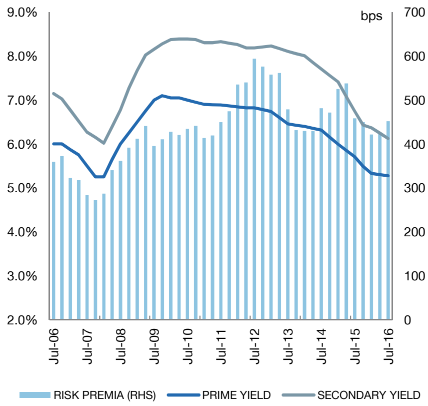
Despite the firming of yields, the spread between prime yields and bond rates is still above the long-term average. As at July 2016, the average prime yield spread was 452bps, which was slightly above the 10 year average of 436bps. This is supportive of the current market pricing.

FIGURE 7
Sydney CBD Purchaser/Vendor
$10 million+ sales—YTD 2016



Source: Knight Frank Research

FIGURE 8
Sydney CBD Yields & Spread
Core Market Yields - Prime vs Secondary



Source: Knight Frank Research

Outlook

- The strong pipeline of office space supply is expected to be maintained over the second half of 2016 before tapering off significantly post Barangaroo. On the other hand, withdrawals are expected to accelerate leading to a period of undersupply in the Sydney CBD beyond 2017.
- Tenant demand in the Sydney CBD market is expected to remain strong over the next two years, underpinned by the Finance and Technology sectors. However, the potential lack of secondary stock and rising rents will result in some secondary tenants moving to the prime market or out of the CBD.
- The overall vacancy rate in the CBD is expected to rise moderately over the second half of 2016 before trending down towards 5.4% and 3.5% by the end of 2017 and 2018 respectively.
- Vacancies in the secondary market are forecast to decline at a faster pace than the prime market in the next two years due to secondary stock withdrawals.
- Secondary rental growth is forecast to outperform prime rental growth and the spread between prime and secondary rents is expected to narrow over the 24 months.
- Secondary and prime gross face rents are forecast to grow by 7.0% p.a. and 5.0% p.a. over the next two years respectively. With incentives trending downward, effective growth rates are projected to be boosted to 9.6% p.a. and 7.9% p.a. for prime and secondary rents respectively.
- A distinct lack of stock and improved leasing fundamentals will ensure the market remains tight. CBD assets expected to be traded over the next 12 months will include 55 Clarence Street (back on the market as at September 2016), 362 Kent St, 66 Goulburn Street, 92 Pitt Street and 28 O'Connell Street.
- The proposed Central Sydney Planning Strategy is expected to be a game changer for future development in the CBD. Among the major changes is a 50% residential cap in developments over 55 metres in height.

The Western Corridor precinct includes Walsh Bay and Barangaroo.

Sydney - Haymarket - The Rocks SA2 region:
A Statistical Area Level 2 (SA2) region is an Australian Bureau of Statistics (ABS) defined area as part of the Australian Statistical Geography Standard (ASGS). The Sydney - Haymarket - The Rocks SA2 region broadly encompasses the Sydney CBD, extending south to Central Station, east to the Botanic Gardens, west to eastern part of Pyrmont and north to Sydney Harbour.

Knight Frank Research provides strategic advice, consultancy services and forecasting to a wide range of clients worldwide including developers, investors, funding organisations, corporate institutions and the public sector. All our clients recognise the need for expert independent advice customised to their specific needs.

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