- *Prime Grade vacancy continues to decrease*
- *The firming of Adelaide CBD yields perpetuates into 2021*
- *The fringe lifestyle is enticing blue chip tenants*

Knight Frank

knightfrank.com/research

Adelaide CBD Office

Market Report, September 2021

NEW GENERATION PRIME STOCK IS IN DEMAND

Prime building vacancy is expected to decrease prior to the expected completion of gross supply forecasted for 2023+

10.7% FRINGE VACANCY

8.5% VACANCY new generation prime office located in core precinct

5.33% PRIME YIELD

"We are witnessing unprecedented amounts of new capital circling Adelaide based on genuine economic drivers and potential population growth."

GUY BENNETT

PARTNER, HEAD OF INSTITUTIONAL SALES, VIC & SA

The Key Insights

The Adelaide CBD vacancy rate has decreased from 16.0% to 15.7%. The decrease is attributed to the reduction in vacancy of new generation prime buildings.

The Adelaide fringe market is experiencing a decline in vacancy combined with growth in gross effective rents, creating the perfect opportunity for a further firming of yields.

Average Adelaide CBD prime incentives have decreased by 0.5% to 31.3%, with the average secondary incentive increasing by 1.8% to stand at 36.0%.

The Adelaide market is expecting a record number of sales in the second half of 2021 as investors seek to acquire assets with the unprecedented amount of capital circulating the market.

Yields for prime assets within the Adelaide CBD continue to firm with a current range between 5.0% and 5.75%. Strong demand prevails with properties offering long term lease covenants, particularly to government tenants.

Adelaide CBD Office Market Indicators — January 2021

GRADE	TOTAL STOCK SQM	VACANCY RATE %	SIX MONTH NET ABSORPTION SQM	SIX MONTH NET ADDITIONS SQM	AVERAGE GROSS FACE RENT $/SQM	AVERAGE INCENTIVE %	EFFECTIVE RENTAL GROWTH % YOY	AVERAGE CORE MARKET YIELD %*
Prime	623,496	11.9	6,566	0	554	25.0 - 35.0	0.93	5.00-5.75
Secondary	839,670	18.5	-3,540	0	394	30.0 - 40.0	-2.99	6.00-6.75
Total	**1,463,166**	**15.7**	**3,026**	**0**				

Source: Knight Frank Research/PCA *assuming WALE 5.0 years

TENANTS SEEK NEW GENERATION PRIME STOCK

Demand concentrated on new generation prime stock

The Adelaide market has seen little disruption since the onset of COVID as the market continues to strengthen with a perpetual demand for new generation prime stock. There remains a sustained divergence in demand, dependant on product type and location. Specifically, we are seeing a reduction in vacancy and incentives within A grade space in the Frame.

Since January 2021 the new generation prime market recorded a 0.6% decrease in vacancy, with the majority of vacant space attributable to the recent development of 108 Wakefield Street. If we hypothetically exclude this building as an outlier (due to lack of precommitment prior to construction) we observe that prime office vacancy would have fallen by 0.9% to stand at 2.4%.

We anticipate that as tenants shift toward quality stock, secondary building owners will be required to reposition their assets through restorations and refurbishments. We expect that incentives within secondary stock will persist at current levels as building owners attempt to compete with new generation prime buildings.

Net absorption on the rise

In the six months leading to August 2021, the Adelaide CBD has experienced a strong turnaround in absorption from a negative net absorption of 9,271m² to a positive net absorption of 3,026m². Prime CBD office space recorded a positive net absorption of 6,566m² and secondary space recorded a negative net absorption of 3,540m². The breakdown of the absorption data supports the continuing flight to quality trend.

We note that tenants are transitioning into smaller tenancies within new generation prime stock, due to the more efficient floorplates and fit outs. However, there still remains active requirements from Hood Sweeney for 2,000-2,500m² of office space, Commonwealth Government for 2,000m², WSP for 2,500-3,000m², Telstra for 4,500-7,000m² and NAB for 3,000-6,000m², highlighting that major tenants are still seeking large proportions of NLA.

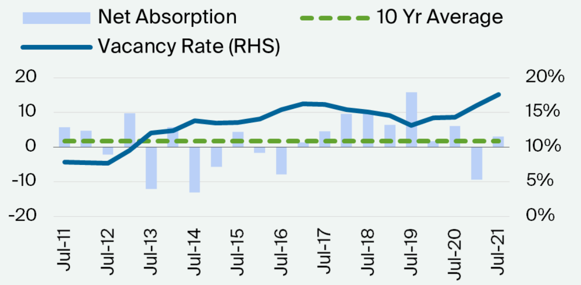
Major tenants lock into A grade office space around the city

The Adelaide CBD is receiving substantial interest from blue chip companies and government entities, as large portions of NLA within A grade buildings are snapped up throughout 2021. Examples of this include SA Water, who have recently renewed their lease of 17,477m² of NLA at 250 Victoria Square along with the negotiation of Renewal SA, who have locked in 1,452m² of NLA for 10 years at 11 Waymouth Street.

As the market continues forward there is limited space available within new generation prime buildings. Due to the lack of any new supply until at least 2023 we expect to see vacancies decrease across older generation prime buildings.

CBD Office Vacancy & Absorption

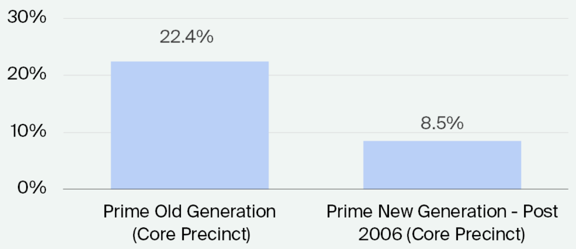
% total vacancy; '000 sqm net absorption



Source: Knight Frank Research, PCA

Prime Office Vacancy in Core Precinct

New vs Old generation (to January 2021)



Source: Knight Frank Research

LARGE FUTURE SUPPLY FORECASTED FOR 2023+

Supply forecasted for late 2022 to 2023+

The Adelaide CBD observed no new supply leading into July 2021. There are currently three office developments under construction and a further four mooted developments yet to begin construction with forecasted supply of 116,500m² of NLA in 2023+, 20,000m² of NLA in 2025 and 77,610m² of NLA with an unconfirmed completion date.

There are two developments that have both secured tenant pre commitment and are currently under construction within Adelaide CBD. Charter Halls 14 storey A grade tower with 40,000m² of office space and 3,600m² of retail space, at 60 King William Street with a 71.25% precommitment lease to Services Australia and CBUS' 17 storey A grade tower with 30,000m² of office space, 360m² of retail space and 120 onsite car parking bays with a 58% precommitment lease to DPTI.

Melbourne based ICD Property Group's development of three towers comprising 15,000m² of office and 6,000m² of retail space at The Adelaide Central Market is a current development awaiting major pre commitment before commencing construction. Other major developments currently mooted and awaiting tenant commitment include Kyren Group's 21,000m² tower at 42-56 Franklin Street and Le Cordon Bleu & Commercial General's 30,000m² tower at 200 North Terrace.

Tenants secured at Festival Plaza

Construction is due to begin mid October at the Walker Corporation's 44,500m² tower in Festival Plaza, after approximately 5 years of planning. The Walker Corporation has declined to comment on speculation regarding a precommitment lease to Flinders University, but confirmed that approximately 20,000m² of NLA has been secured by tenants. Fit out work for tenants is expected to commence in August 2022 with completion due in November 2023.

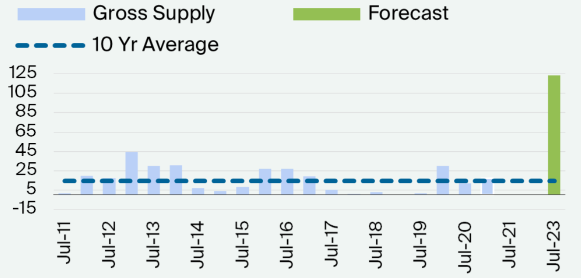
Prime rents remain stable into 2021

As at July 2021, the gross effective rents for prime stock within the Adelaide CBD observed a slight increase to $380/m² from $379/m², whereas secondary stock observed a decline from $259/m² to $252/m². The rise of prime gross effective rents is linked with the high demand for prime stock. Furthermore the market observed a decrease in incentives for new generation buildings as at July 2021 to stand at 31.3%.

The decline in secondary buildings gross effective rents is associated with an increase in incentives. The average secondary incentive as at July 2021 is 36.0% observing an annual increase of 2.7% and a semi-annual increase of 1.8%.

CBD Office Gross Supply

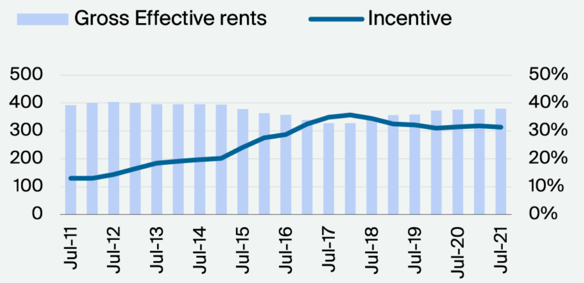
'000 sqm



Source: Knight Frank Research, PCA

CBD Office Rents & Incentives

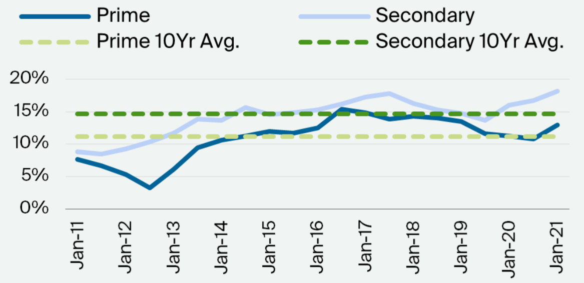
$/sqm prime effective rents; % prime incentives



Source: Knight Frank Research

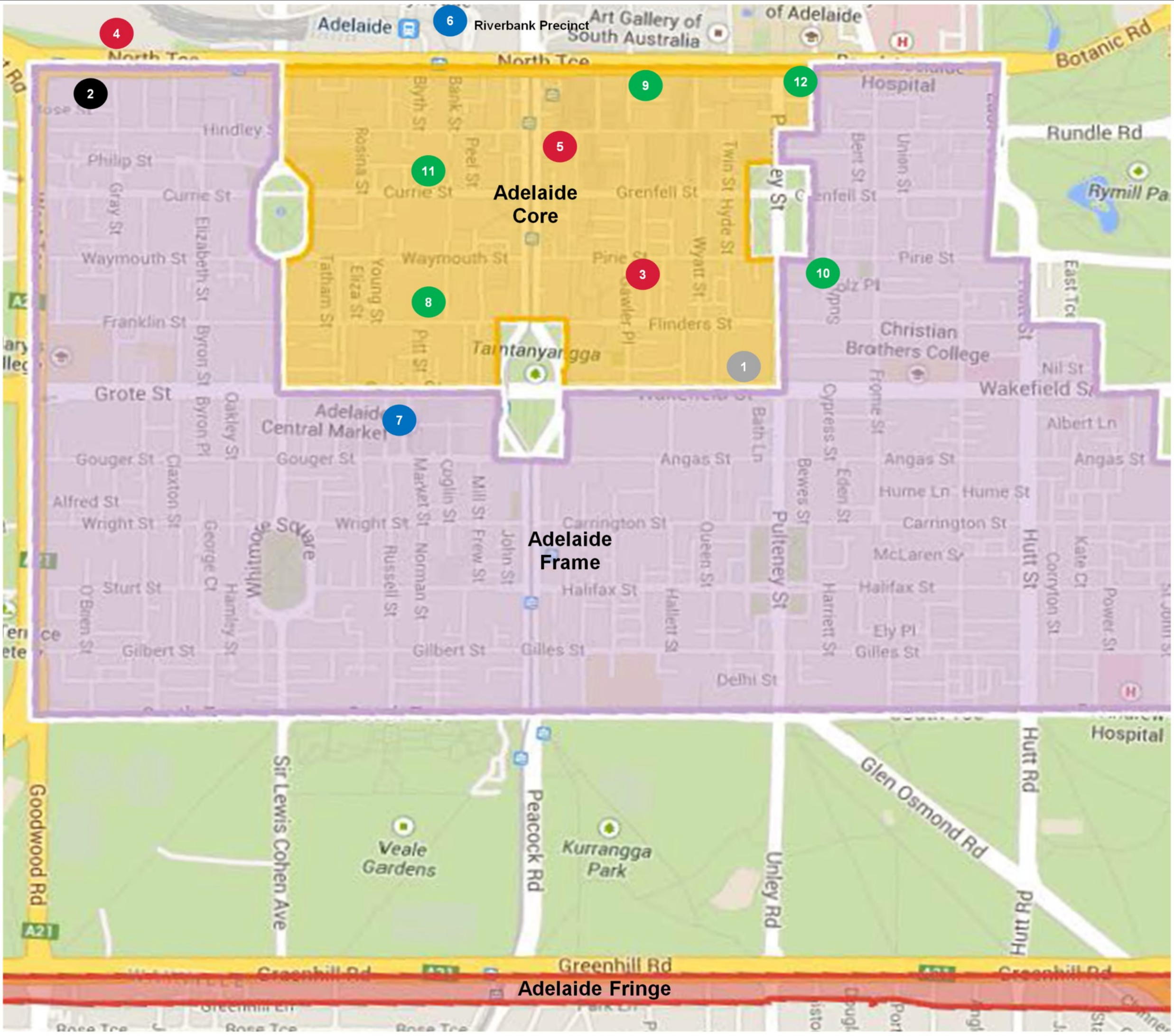
CBD Office Vacancy

% Prime vs Secondary



Source: Knight Frank Research

MAJOR CBD OFFICE SUPPLY



RECENTLY COMPLETED

1. 108 WAKEFIELD STREET–15,586 SQM (OFFICE) & 452 SQM (RETAIL)
   KYREN–0% COMMITTED Q4 2020

MAJOR REFURBISHMENTS

2 21 NORTH TERRACE–3,500* SQM (OFFICE/ MEDICAL)
LUCA GROUP–100% COMMITTED Q4 2021

UNDER CONSTRUCTION/ MAJOR PRE-COMMITMENT

3 83 PIRIE STREET–32,000 SQM [SA GOVERNMENT–DPTI]
CBUS–58% COMMITTED. 2023

4 SAHMRI 2, NORTH TERRACE–20,000* SQM (OFFICE) [SA GOVERNMENT & SAHMRI]
COMMERCIAL & GENERAL–2025

5 60 KING WILLIAM STREET–40,000 SQM (OFFICE) & 3,000 SQM (RETAIL)
CHARTER HALL– 71.25% COMMITTED.

DEVELOPMENT APPROVED

6 FESTIVAL PLAZA–44,500 SQM (OFFICE) & 4,500 SQM (RETAIL)
WALKER CORPORATION-2023+

7 CENTRAL MARKET–15,000 SQM (OFFICE) & 6,000 SQM (RETAIL)
ICD PROPERTY

DEVELOPMENT APPLICATION/MOOTED/ EARLY FEASIBILITY

8 42-56 FRANKLIN STREET–21,000 SQM
KYREN - MOOTED

9 200 NORTH TERRACE–26,000 SQM (OFFICE) & 3,000 SQM (RETAIL)
COMMERCIAL & GENERAL - MOOTED

10 185 PIRIE STREET – 6,300 SQM
PALUMBO-MOOTED

11 62 – 80 CURRIE STREET– (OFFICE/HOTEL)
PRIVATE DEVELOPER –2023+

12 FREEMASONS HALL– 33,000 SQM | 2,000 SQM (OFFICE) 1,000 SQM (RETAIL)
FREEEMASONS BRANCH-2023+

NB Dates are Knight Frank Research estimates
Major tenant commitment in [brackets] net to NLA
* approximate

DEMAND REMAINED STRONG FOR CORE ASSETS

Strong demand for quality investment assets

As at July 2021, 111 Gawler place is the only asset recording a sale above $10 million in the Adelaide CBD. The asset held a WALE of 3.5 years and was purchased by a private investor for $18million. This excludes the sale of properties currently under construction such as $43.0 million for the land component at 60 King William Street and a reported $446.2 million for SAHMRI 2, with both settling on completion. This compares with $402.05 million and $787.49 million for 2020 and 2019 respectively.

Highlighting that due to the pandemic, major transactions have been reduced throughout 2021 as international and interstate investors tend to hold off on acquisitions until borders restrictions ease. Leading into the final quarter of 2021 the market is expecting a record number of sales as investors seek to deploy their capital in the Adelaide market.

There is continued demand for South Australian assets, primarily through off market discussions, reflecting the ongoing strength of the state economy. The South Australian market is expected to strengthen further as a result of infrastructure upgrades and job prospects associated with long term Defence related investments . Along with the above traits, the South Australian market is observed as a safe haven, reflective of the way the state responded to COVID combined with the stability shown in both the property and economic market.

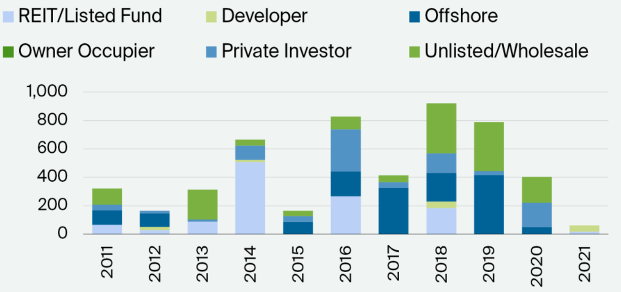
Yield compression continues in Adelaide

Reflecting the weight of demand, the average prime yield in Adelaide CBD has compressed by 62 basis points since January to stand at 5.33%. The firming of yields has continued in spite of economic disruption due to COVID-19, and shows that in the case of Adelaide, lower interest rates have offset the impact of uncertainty within the occupier market.

Investors are still seeking properties offering long term lease covenants, particularly with government tenants.

CBD Office Investment Turnover

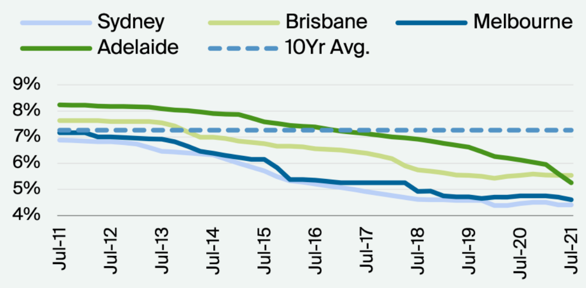
'$ millions



Source: Knight Frank Research

CBD Office SA vs East Coast Yields

% core market yields



Source: Knight Frank Research

Recent significant sales

PROPERTY	PRICE $M	CORE MARKET	NLA SQM	$/SQM NLA	WALE	PURCHASER	VENDOR	SALE DATE
21-25 Nile Street, Port Adelaide*	62.75	c5.63	6,423	9,770	11.3	Centuria Capital	Charter Hall	U/C
60 Wakefield Street & 21 Divett Place, Adelaide	51.00	c6.44	4,500	11,333	6.7	Charter Hall	Private Investor	Oct-20
75 Hindmarsh Square, Adelaide	40.50	c6.15	4,662	8,687	3.8	Harmony Property	Private Investor	Oct-20
22 King William Street, Adelaide	47.02	c6.93	9,604	4,896	2.7	Intergen Property Partners	Southern Cross Equity Group	Oct-20

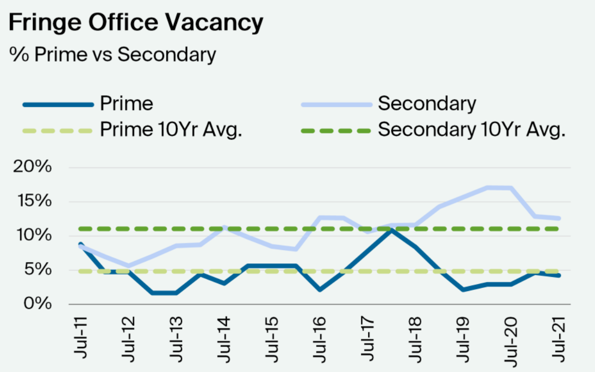
c Circa *Not Settled

STRONG INVESTMENT POTENTIAL IN THE FRINGE

Vacancy on the decline within fringe market

The Adelaide City Fringe has recorded a decrease in the vacancy rate, from 11.2% to 10.7%. The decrease was a result of both prime and secondary markets experiencing a reduction of 0.5% and 0.3% respectively. Specifically the decrease in the secondary market is associated with a withdrawal of stock. We note that due to the reduced size of the fringe market, smaller withdrawals of stock have a greater impact on the vacancy rate.

The recent growth observed within the Fringe market is accountable to a tenant desire for the perceived 'lifestyle' within the market. The Fringe provides high traffic, corporate exposure, ease of accessibility and car-parking availability. GPA Engineering recently negotiated a lease at 120-121 Greenhill road for 3,100m² of NLA on a term of 6 years accountable to the 95 car parking spaces available.

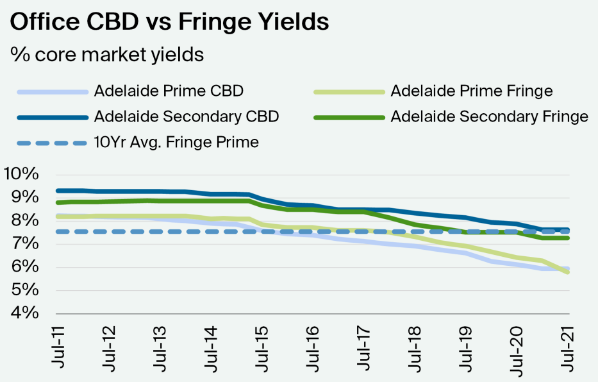


Source: Knight Frank Research

Rent remains firm as yields continue to firm.

In the six months leading into July 2021 prime gross effective rents throughout the Fringe precinct have remained steady at $374/m² p.a. whereas secondary gross effective rents saw an increase from $260/m² p.a. to $262/m² p.a., with incentives remaining steady at 20.5% and 27.5% respectively. This follows an increase of 2.28% for prime gross rents on a year to date basis and a decrease of 2.66% for secondary effective rents.

The yields within the Fringe have experienced a firming within the past six months of 50 basis and 100 basis points to sit at 5.80% and 6.28% for prime and secondary assets respectively. The strength of the 'Suburban/Fringe' office market is unequivocal, with the recent sale of 21-25 Nile Street, Port Adelaide achieving a yield of 4.6%. The asset sold fully leased to the Minister of Transport and Infrastructure & Urban Renewal Authority reflecting a WALE of 11.3 years.



Source: Knight Frank Research

Recent significant tenant commitments

OCCUPIER	PROPERTY	PRECINCT	SIZE SQM	FACE RENT $/SQM	TERM YRS	START DATE
Commonwealth Govt. Services Australia	60 King William Street	Core	28,500	N/A	10	Circa 2023
SA Government (D.I.T)	73-85 Pirie Street	Core	17,500	N/A	10	Circa 2023
Renewal SA	11 Waymouth Street	Core	1,452	575g	10	July 2021
Honeywell	100 Pirie Street	Core	2,050	495g	5	July 2021
AIB	1 King William Street	Core	2,296	530g	5	March 2021

g Gross   n Net   *approximate   (r) renewal

We like questions, if you've got one about our research, or would like some property advice, we would love to hear from you.

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