

PERTH CBD

OFFICE MARKET BRIEF OCTOBER 2015

Key Facts

The Perth CBD vacancy rate increased to 16.6% from 14.8% as at July 2015.

Approximately 188,500m² of office supply is currently under construction in the Perth CBD of which 75% is pre-committed.

The Perth CBD recorded negative net absorption in the six months to July 2015; prime totaling – 6,256m² and secondary totaling –13,691m².

Incentive levels are expected to remain high and currently average around 45% of net rent.



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The office market is still experiencing negative net absorption as a result of a soft Perth CBD leasing market with negative 19,875m² recorded for the six months to July 2015, resulting in a rise in the vacancy to 16.6%.

Development Activity

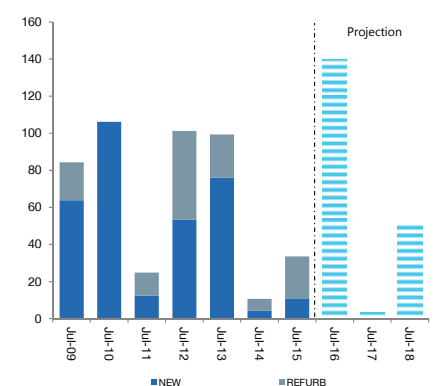
There was only 15,045m² of new supply added to Perth CBD stock in the six months to July 2015 which, given the lack of demand has limited the upward pressure on vacancy. A significant level of supply is due for completion in the second half of 2015 totalling 134,556m² and of this stock 68% has been pre-committed. The level of commitment varies, with the Old Treasury redevelopment and Kings Square (KS) 2 & 3 fully pre-committed, while KS4 is 72% pre-committed to HBF. Brookfield Place Stage 2 is 63% pre-committed and will soon be home to Ashurst, Brookfield Multiplex, Corrs, Deloitte and Wesfarmers.

Beyond these projects under construction, office development over the next two years will be limited, which will cushion the market somewhat. With much of the current development completed by late 2015, new stock entering the cycle has developers adopting a more cautious approach as construction works will only commence

when a robust level of pre-lease commitment has been secured.

The only addition to stock in 2016 and 2017 is a new development for Channel Nine Perth at 251-267 St Georges Tce. DA Approval was received last month for new studio space of 306m² to be

FIGURE 1
Perth CBD Office Supply
New and Refurbished Stock ('000m²) - annual



Source: Knight Frank Research/PCA

developed on parkland in front of 255 St Georges Tce, with site works to commence in November. Channel Nine will also occupy office space, pending refurbishment, at 255 and 267 St Georges Tce taking up 657m² and 1,512m² respectively, with the total NLA across the three buildings circa 2,500m². The parkland area will be an open air amphitheatre with media wall and visibility into the Studio.

The only other office building likely to be under construction in the CBD in 2016 is Woodside Petroleum's new headquarters at Capital Square, 98-124 Mounts Bay Rd (the Emu Brewery site) of 50,500m². Works have commenced on the site with completion due in 2018.

A significant increase in backfill space in Perth CBD is likely to make an impact over the next year as new developments reach completion. Crown Law has consolidated their offices and will be moving to the soon to be completed 28 Barrack St, leaving 20,000m² of space available at Westralia Square, 141 St Georges Tce. The completion of Brookfield Place 2, KS2, KS3, KS4 and 999 Hay St, will release circa 31,500m² of backfill from CBD tenants such as HBF, Deloitte, Ashurst, Corrs, Shell and GHD.

There will be some net inflow into the CBD, with circa 5,000m² of new space to be absorbed by tenants currently occupying suburban office space, with Brookfield and John Holland relocating to Brookfield Place 2 and KS3 respectively.

Net Absorption & Vacancy

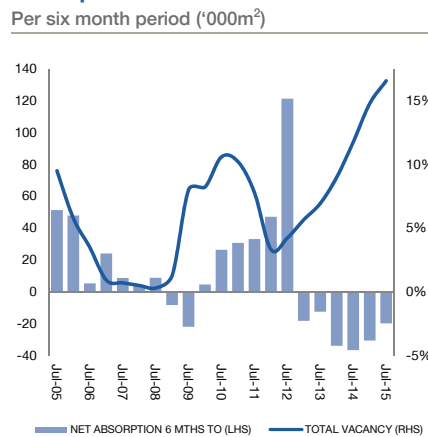
Net absorption in the 12 months to July 2015 was negative 50,457m². The Perth CBD market has continued to experience negative net absorption with July 2015

being the sixth consecutive quarterly negative result in net absorption since January 2012. Negative net absorption is also attributed to the increase in sublease space available in the Perth CBD, as companies are continuing to downsize.

The Perth CBD recorded a negative net absorption of 19,875m² over the six months to July 2015 as company contractions and tenant relocations made their impact. Prime assets recorded negative 6,256m², accounting for 31% of the total. Of that, Premium grade assets recorded negative absorption of 3,233m² following two consecutive half year periods of negative results, while A grade recorded negative absorption of 3,023m² to July 2015. Secondary assets recorded negative 13,619m², amounting to 69% of the total. This is the sum of B (-8,374m²) and C (-5,245m²) grade assets with D grade sitting at zero as at July 2015. The trend in the market is that net absorption will remain negative moving into 2016.

The CBD office vacancy was 16.6% as at July 2015, an increase of 4.8 percentage points from the July 2014 figure of 11.8%.

FIGURE 2
Perth CBD Vacancy & Net Absorption



Source: Knight Frank Research/PCA

The high vacancy rate is being caused by negative demand for new office space and some new office stock coming into the market. A total of 270,793m² of vacant space is available across the Perth CBD. This is an additional 30,861m² since January 2015.

On a grade by grade basis, vacancies increased across the board. The largest volume of space vacant is in A and B grade buildings with 98,045m² (36%) and 102,974m² (38%) respectively.

Sublease space continues to be a major factor within the Perth CBD office market. The sublease vacancy is sitting at 3.5%, up 10,901m² from 2.8% in January 2015.

A significant volume of supply is due for completion in the second half of 2015 which will have an impact on the vacancy rate moving into 2016. The total vacancy will continue to rise into 2016 and we expect a vacancy rate of around 22% by mid 2016.

Tenant Demand & Rents

The current Perth CBD office market is allowing tenants the opportunity to seek better quality space and obtain greater incentives and in turn reset their passing rentals. Tenants upgrading from secondary to prime grade properties are ideally looking for small to mid-sized space at competitive rents with a longer lease term and increased incentives. The incentives that tenants are seeking include rent free periods/rebates as well as capital contributions for office fit-outs which in turn minimises the cost for the tenant going forward with the move.

After speculation of anchoring a new tower at Elizabeth Quay, Rio Tinto has

TABLE 1
Perth CBD Office Market Indicators as at July 2015

Grade	Total Stock (m ²)	Vacancy Rate (%)	Annual Net Absorption (m ²)	Annual Net Additions (m ²)	Average Net Face Rent (\$/m ²)	Average Incentive (%)	Average Core Market Yield (%)
Prime	949,864	13.6	-20,042	18,647	560—664	45	7.00—8.00
Secondary	686,240	20.7	-30,415	13,153	406—442	45	8.00—9.00
Total	1,636,104	16.6	-50,457	31,800			

Source: Knight Frank Research/PCA

reportedly extended their office lease at Central Park, 152-158 St Georges Tce, which was due for expiry in 2018, for another 12 years from expiry taking the lease out to 2030.

Perth office rents continued to moderate over the first half of the year and have fallen steadily since the peak in July 2012 when net face rentals reached \$805/m² for Prime grade office space and \$616/m² for Secondary. Net effective rents are being significantly impacted as rising incentives flow through. Average Perth CBD prime net face rents are at \$612/m² as at July 2015 after falling each quarter since July 2012—a fall of 24% since the peak. Furthermore, current rents and the cost of incentives are working against the viability of new developments. Demand is soft, but many tenants are taking advantage of incentives to relocate to higher quality office space.

Incentives have now risen to average circa 45%, up from 35% in January 2015. Incentive levels are expected to remain high as vacancy levels rise further into 2016.

Secondary grade net face rents currently average \$424/m² down from \$446/m² in January 2015 a fall of 31% since their peak in July 2012. The fall in net face rents in secondary grade buildings has occurred due to strong competition as prime leasing options become comparably cheaper.

Investment Activity & Yields

Investment activity for the 2014 calendar year saw a total of \$640.4 million transactions for the Perth CBD. The majority of activity happened in the first six months of the year with four of the six transactions occurring before

TABLE 2

Recent Leasing Activity—Perth CBD

Address	NLA	Term	Tenant	Lease Type	Date
15-17 William St	1,234	5	Probuild	New	Sep-15
1 Nash St	3,900	9.5	Dept Health & Aged	Sub-Lease	Sep-15
2 The Esplanade	175	1.2	Toyko Timor Sea	Renewal	Sep-15
	341	1.2	TEPCO Australia	Renewal	Sep-15
580 Hay St	564	5	Communicare	Sub-Lease	Sep-15
50 St Georges Tce	225	2.5	Vix Technology	New	Sep-15
44 St Georges Tce	152	5	SEEK Limited	New	Sep-15
12 St Georges Tce	234	3	AMCS*	New	Aug-15
999 Hay St	6,416	10	GHD	New	Jun-15
150 St Georges Tce	409	5	Axis Financial Group	New	Apr-15
1 William St	1,094	10	Gooding Partners	Renewal	Apr-15
	2,194	7	Empired Limited	New	Sep-15

Source: Knight Frank Research *Australian Migration & Citizenship Services

July 2014. The first six months of 2015 has seen very little activity in the office sector. The first major office building sale occurred in August for \$101 million at 45 Francis St, known as the Australian Tax Office Headquarters in Northbridge. The six level, 22,013m² building boasts very large floorplates.

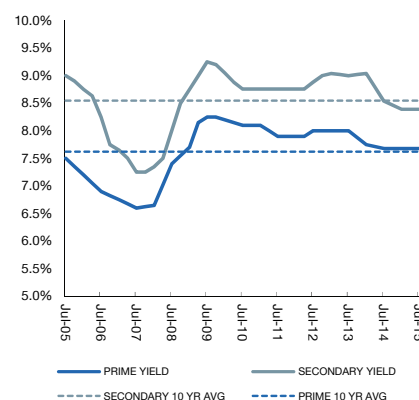
Average prime core market yields are estimated to range between 7% and 8%, with minimal firming occurring over the past year. Secondary core market yields are between 8% and 9%.

Office buildings in Perth CBD currently for sale include Brookfield Place, located at 123 St Georges Tce anchored by BHP and 50% of Exchange Tower located at 2 The Esplanade is now under contract. 363 Wellington St which is leased to Western Power with a total area of 23,215m² is also on the market for sale. The Insurance Commission of WA (ICWA), is disposing of three

commercial office buildings in the Perth CBD and two major retail suburban shopping centres; these assets forming a significant part of ICWA's total investment portfolio of approximately \$4.4 billion.

FIGURE 3

Perth CBD Prime & Secondary Yield Quarterly with long term average



Source: Knight Frank Research

TABLE 3

Recent Sales Activity - Perth CBD

Address	Grade	Price \$ mil	Core Market Yield (%)	NLA m ²	\$/m ² NLA	WALE (yrs)	Vendor	Purchaser	Sale Date
45 Francis St *	B	101.0	12.11	22,013	4,588	6.2	Deka Immobilien	Warrington Property	Aug-15

Source: Knight Frank Research *Located in Northbridge



Outlook

Tenant enquiry levels indicate net absorption will remain weak for the remainder of 2015. Nevertheless, falling rents and increasing incentives are providing tenants with some favourable leasing options which is expected to stimulate tenant migration to better quality premises. Going forward, Perth CBD prime rents may begin to stabilise but little to no improvement is expected before 2017 as the market absorbs significant levels of supply forecast to come online in the Perth CBD.

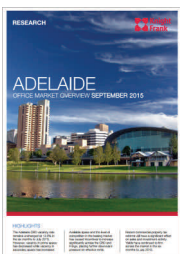
In terms of supply over the next six months, there is very little coming onto the market in 2016 and 2017 with one new development, Capital Square, on

the horizon for 2018. Knight Frank expects the vacancy to peak at around 22% in mid 2016 then remain steady through to 2017. Any reduction thereafter will only come from improving demand conditions and a continued lack of new supply.

With domestic and offshore investors seeking to expand their presence in the Perth market, coupled with a low Australian dollar and low interest rates, it is anticipated that investment demand for Perth CBD office assets will improve with the majority of buyer attention continuing to focus on securely leased prime assets. The limited number of sales is partly attributable to the tightly held nature of the market, with few properties being listed.

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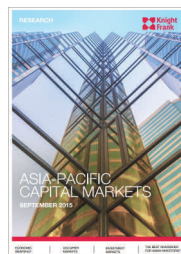
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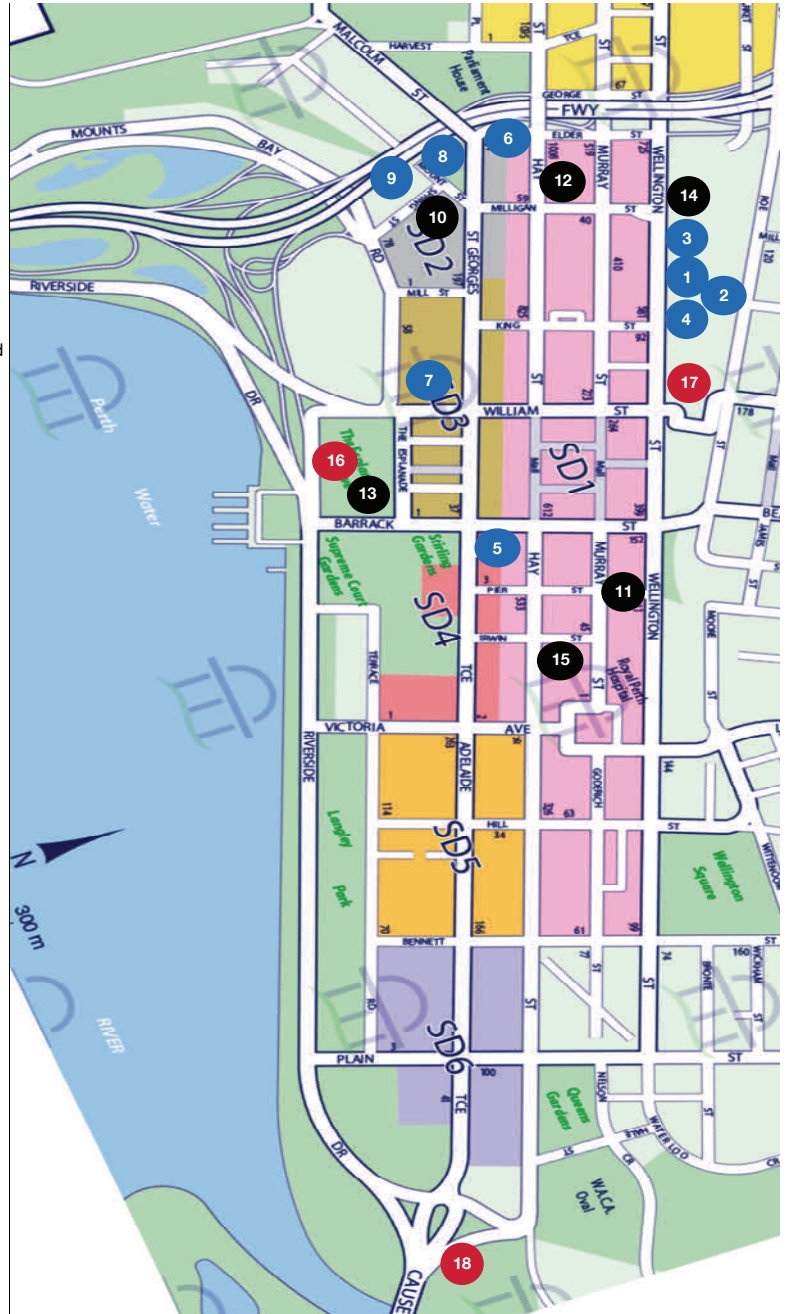


MAJOR OFFICE SUPPLY

- 1 KS2 (Kings Square)*, 376 Wellington St - 19,282m² [Shell]
DEXUS & DWPF - Q3 2015 - 100% committed
- 2 KS3 (Kings Square)*, 376 Wellington St - 5,675m² [John Holland]
DEXUS & DWPF - Q3 2015 - 100% pre-committed
- 3 KS4 (Kings Square)*, Wellington St - 12,500m² [HBF]
HBF - Q3 2015 - 72% committed
- 4 KS1 (Kings Square)*, 376 Wellington St - 22,543m²
DEXUS & DWPF - Q4 2015 - seeking pre-commitment
- 5 Treasury Building, 28 Barrack St - 30,196m² [WA Gov't]
Mirvac / Keppel REIT consortium - Q3 2015 - 100% committed
- 6 999 Hay St - 10,760m² [GHD]
QUBE - Q3 2015 - 56% committed
- 7 123 St Georges Tce (Brookfield Place 2) - 33,600m² [Ashurst, Corrs,
Deloitte, Brookfield, Wesfarmers] - Brookfield - Q4 2015 - 63% committed
- 8 251-267 St Georges Tce # - 2,500m² [includes new studio of 306m²]
Primewest - late 2016
- 9 Capital Square, 98-124 Mounts Bay Rd - 50,500m² [Woodside]
AAIG - mid 2018 - 100% committed
- 10 239 St Georges Tce (Bishops See no.2) - 46,000m²+
Brookfield/Hawaiian - seeking pre-commitment
- 11 100 Murray St # - 4,000m²
AWD Diversified Ltd - seeking pre-commitment
- 12 950 Hay St (old Melbourne Hotel site) - 10,000m²
Oakesfield Pty Ltd - seeking pre-commitment
- 13 Crn Barrack St & The Esplanade - 70,000m² [Chevron]
Chevron - DA Pending
- 14 KS5 (Kings Square)* - 38,000m²
Seven Entertainment - DA Pending
- 15 480 Hay St - 34,000m²
BGC - DA Approved - seeking pre-commitment
- 16 Elizabeth Quay - 130,000m² excluding 70,000m² Chevron site
Leighton / Broad Construction Services
- 17 Perth City Link* - Circa 120,000m² exclusive of Kings Square
Mircvac/Leighton development consortium
- 18 Waterbank, near The Causeway - 17,000m²
Lend Lease / MRA - Initial site works

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

NB. Dates are Knight Frank Research estimates
Office NLA quoted
Major tenant precommitment in [brackets] next to NLA
Full refurbishment
* Mirvac/Leighton awarded the Perth City Link development contract excluding the Kings Square precinct.
KS 1 to 5 are being developed by Leighton / Seven Group.



Source of Map: PCA