RESEARCH

Knight Frank

BRISBANE INDUSTRIAL

MARKET OVERVIEW JUNE 2016

HIGHLIGHTS

Occupier demand remains focused on new accommodation with only modest demand for existing stock due to the low rental differential between new and old space. Existing rents are under pressure.

Construction completions in 2016 are likely to be lower than that of 2015, despite the activity at the larger end of the market. Land values, particularly for smaller lots, have seen sustained growth.

Investment demand is strong with the market's preference for large, core assets largely unfulfilled. As a result, purchasers are accepting more longer term risks if there is a substantial WALE.

KEY FINDINGS

Supply was 9.2% lower in 2015 and is likely to be lower again in 2016; despite the good levels of larger occupier commitments, the smaller development market remains subdued

Vacant space has decreased over the past three quarters to 636,288m² with prime and secondary stock availability relatively equal.

Market rents for existing properties have continued to moderate with annual reductions in face rents of 3.0% and 1.6% for prime and secondary respectively.

Investor demand is still high and with true core assets rarely available, purchasers are willing to accept greater long term risks if the short term is mitigated by WALE.

JENNELLE WILSON
Senior Director—Research QLD

INDUSTRIAL OVERVIEW

Sizeable commitments to new space continues to dominate the user landscape, with pressure on existing building rents intensifying. Yields for core assets are still tightening, but overall transaction volumes are low.

In the Brisbane industrial market there has continued to be divergence between the occupier and investment markets. While a number of large, high profile tenants have recently, or are about to announce major relocations into newly built accommodation, occupier demand is relatively thin beyond these higher profile companies, with new space clearly being favoured.

In contrast, investment demand has continued to grow with further yield firming for core assets. There has also been an increased appetite to take on some leasing risk in the search for return, albeit confined to core locations. The tentative increase in land values for finished lots, which began a year ago, has consolidated, particularly for smaller lots. The englobo land market has remained tightly held with larger investors controlling the development pipelines to develop assets in favour of purchasing.

Vacancy Snapshot

Total vacancy in the Brisbane industrial market, as at April 2016, was 6.4% lower than that recorded a year earlier, with three consecutive quarters of reduction in the total vacancy. At 636,288m² the total available space remains well above the long term average levels of 430,000m², however the consecutive quarters of improvement is bringing some confidence back to the market.

Available space is dominated by existing buildings (86%) with 11% coming from completed speculative buildings and a further 3% in speculative development under construction (as at April 2016). The increasing speculative activity reflects the market's clear preference for new space and has contributed to the recent higher levels of prime vacant space (Figure 1).

FIGURE 1

Brisbane Industrial Vacancy

'000m² prime versus secondary available space

Source: Knight Frank Research

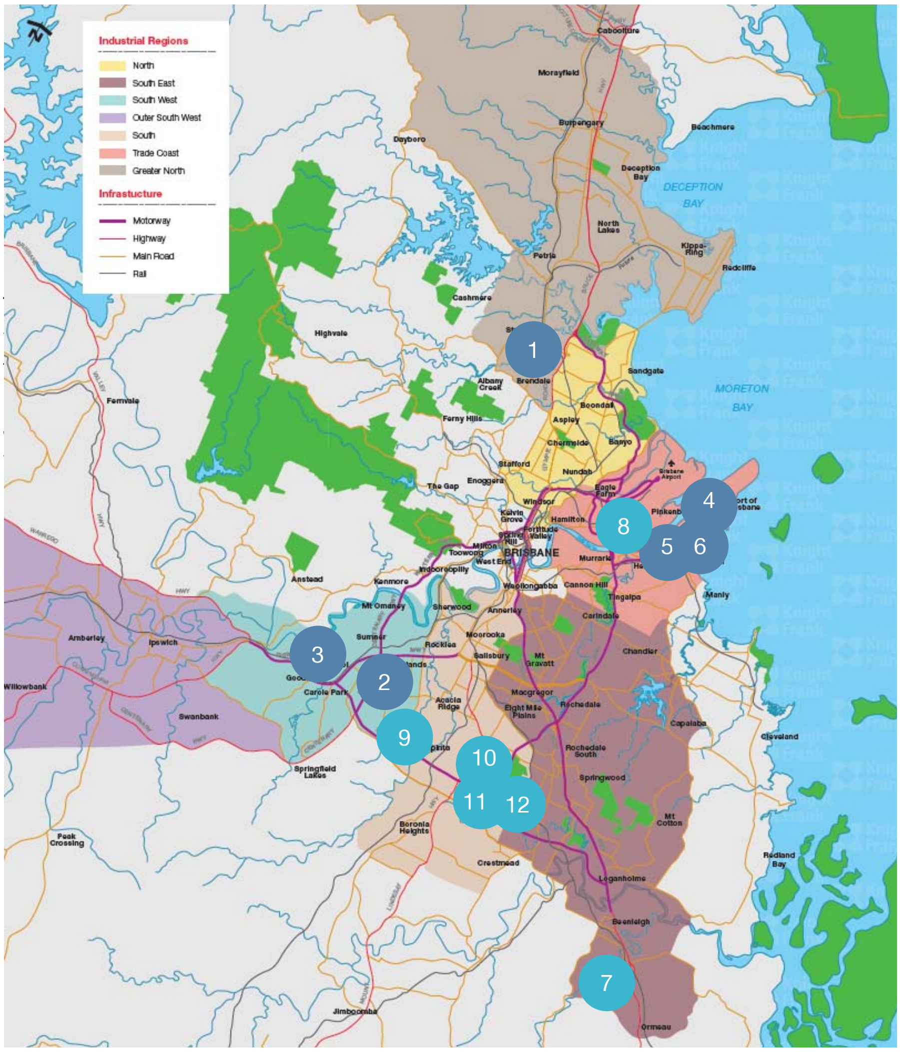
TABLE 1

Brisbane Industrial Market Indicators as at April 2016

Precinct	Avg Prime FaceRent#		Avg Secondary Face Rent		Core Market Yields (%)		Avg Land Values <5,000m²		Avg Land Values 1—5 ha	
	$/m² net	(%p.a)	$/m² net	(%p.a)	Prime	Secondary	$/m²	(%p.a)	$/m²	(%p.a)
Trade Coast	110	-4.3	93	-2.1	6.98—7.70	7.65—8.70	390	16.4	280	1.8
North	104	-2.8	84	1.2	7.10—7.70	7.70—8.70	360	9.1	240	-
South East	100	-4.8	79	-4.8	7.00—7.75	7.75—8.75	245	2.9	190	2.7
South	105	-2.8	85	-	7.00—7.75	7.75—8.75	280	1.8	233	1.3
South West	105	-	83	-2.4	7.05—7.75	7.75—8.70	265	1.9	220	-
Brisbane Average	**105**	**-3.0**	**85**	**-1.6**	**7.03—7.72**	**7.72—8.75**	**308**	**7.1**	**233**	**1.1**

Source: Knight Frank Research # existing stock NB Average market yields are based on an assumed WALE of 5-7 years for prime assets and 3-5 years for secondary

INDUSTRIAL PRECINCTS



2015 Major Completions

1. 68 Kremzow Rd, Brendale—55,881m²
ALDI
Owner Occupier

2. 301 Orchard Rd, Richlands—35,070m²
DEXUS Wholesale Property Fund
Speculative—*Target*

3. 100 Monash Rd, Redbank—27,775m²
Goodman Group
Pre-com *TNT Express*

4. Curlew St, Fisherman Islands—
26,500m² Altis Property Partners
Pre-com *ACFS*

5. 37 Freight St, Lytton Bld 2—19,900m²
Goodman Group
Pre-com *Silk Logistics*

6. 37 Freight St, Lytton Bld 1—19,871m²
Goodman Group Speculative
Silk Logistics/Yusen Logistics

2016 Major Supply

7. Peachey Rd, Yatala—35,400m²
Frasers Property
Pre-com *Owens-Illinios*

8. 1082 Kingsford Smith Dr, Eagle Farm—
29,300m²
G James Glass—Owner occupier

9. 70 Radius Dr, Larapinta—22,980m²
DEXUS Wholesale Property Fund
Speculative

10. 29 Faisal Hatia Way, Berrinba—
19,822m²
Charter Hall—Speculative

11. Huntress St, Berrinba—15,856m²
Frasers Property
Speculative—*Avery Denison (5,600m²)*

12. 53-101 Wayne Goss Dr, Berrinba—
14,990m²
Sigma Pharmaceuticals—owner
occupier

Tenants in Italics

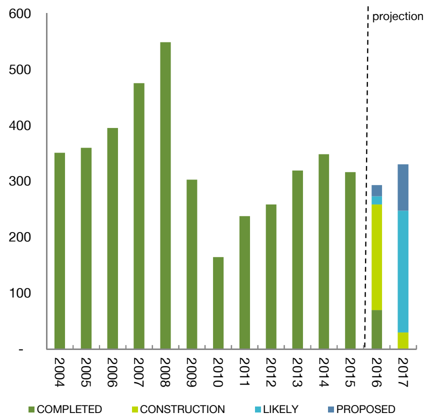
MAJOR INDUSTRIAL SUPPLY

Supply in the Brisbane industrial market moderated during 2015 with completed construction (3,000m²+) down by 9.2% at 316,616m², compared with the 2014 total of 348,547m². Over the course of 2015 completions were relatively evenly split between owner occupier facilities (31%), pre-commitments (39%) and speculative developments (30%). Owner occupier construction was boosted by the 55,881m² ALDI facility, which accounted for more than half of that total.

Supply for 2016 is expected to be slightly lower at 293,400m², however this can still be boosted by smaller/medium projects moving to construction phase through Q2 and Q3. Going forward, early indications, including some buildings already in early construction, are for stronger supply levels during 2017 with a number of larger pre-commitment deals to be announced in the coming months.

Pre-committed construction is expected to outweigh speculative completions during 2016, dominated by larger buildings such as Owens-Illinois (35,400m²), Beaumont Tiles (13,164m²) and National Glass (12,171m²). However there are a number of significant speculative developments in play with 70 Radius Drive, Larapinta (22,980m²) completed in early 2016 and 19,822m² and 15,856m² buildings under construction in Berrinba. In addition 30,200m² of speculative space has just begun construction in Lytton for completion in early 2017.

FIGURE 2
Brisbane Region Supply
'000 m² new industrial construction

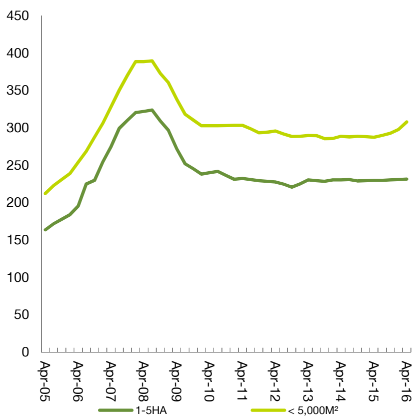


Source: Knight Frank Research/Cordell Connect

DEVELOPMENT & LAND VALUES

Industrial land market activity has continued to improve with relatively little englobo land entering the pipeline to replenish the stock which has been removed as construction levels picked up over the past three years. As established estates have diminished supply, attention is turning to emerging estates such as Connect West (Darra), Metroplex Westgate (Wacol) and the Rochedale Motorway Estate, along with other larger land holdings in Yatala and Larapinta. In addition, infill development has continued to grow, converting older large manufacturing bases to land suitable for warehouse and distribution uses—eg. Postle St, Acacia Ridge. Purchasing older facilities in good locations to land bank is expected to remain a tactic for investors seeking to gain some development exposure in the short term.

FIGURE 3
Brisbane Average Land Values
$/m² land by size

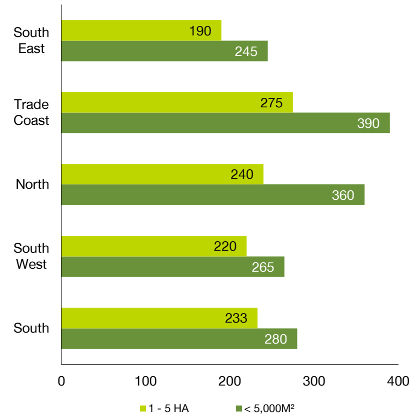


Source: Knight Frank Research

As a result of lower availability for immediately available land, there have been increases in values achieved for smaller blocks under <5,000m² in size (up 7.1% p.a) while larger blocks (1-5ha) have also shown some improvement, increasing by 1.1% p.a on average across the Brisbane region.

TradeCoast land values, particularly for smaller sites, have rebounded, up by 16.4% over the past year (compared with 1.8% for larger lots) while land in the North has increased by 9.1% for smaller lots. The South East has also seen some value growth, although it remains the precinct with the lowest average land values and potentially the greatest medium term pipeline.

FIGURE 4
Brisbane Region Land Values
$/m² of land as at April 2016



Source: Knight Frank Research

D&C Activity

Demand for D&C accommodation, particularly at the larger end has continued, although deals still appear to be slow to reach conclusion. Construction is underway or recently completed for pre-commitments to Owens-Illinois (35,400m²), Beaumont Tiles (13,164m²), National Glass (12,170m²), Couriers Please (11,800m²) and Lindsay Transport (11,165m²).

Knight Frank is currently tracking in excess of 175,000m² of pre-commitment requirements, greater than 10,000m², across the Brisbane region with these tenants considering a range of locations across the TradeCoast, South East and South West precincts. With competition high between developers the majority of these requirements remain confidential, however well known larger requirements include Amart for circa 40,000m² and Schweppes for c22,000m².

TABLE 2
Recent Land/Development Sales Activity Brisbane

Address	Region	Price $ mil	Area m²	$/m² of site area	Zoning	Vendor	Purchaser	Sale Date
1466 Ipswich Rd, Rocklea	S	1.50	11,000	136	GI	Cousins Truck Sales	AKR Metal	Mar 16
211 Lavarack Ave, Eagle Farm	TC	1.80	3,002	600	GI	WB Enterprises	Local Developer	Jan 16
16 Shettleston St, Rocklea	S	0.78	2,219	352	GI	Private Investor	Private Investor	Nov 15
408 Stapylton Rd, Heathwood	S	53.60	24.62 ha	218	GI	Private Investor	Logos Property Group (for an offshore group)	Nov 15
192 Lavarack Ave, Eagle Farm	TC	3.98	7,246	550	GI	Frankipile Australia	Undisclosed	Nov 15
1517 Lytton Rd, Hemmant	TC	6.00	17,766	338	GI	Private Investor	Charter Hall CPIF	Oct 15
207 Potassium St, Narangba	N	1.84	14,720	125	RI	State Government	Fulton Hogan	Sep 15

S South TC Trade Coast N North GI General Industry RI Restricted Industry
Source: Knight Frank Research

OCCUPIER DEMAND & RENTS

Occupier demand has generally remained subdued across the market. There has been improving activity observed in larger tenants (10,000m²+), however given the current accommodative development environment, the vast majority of these leases have been done in new buildings, either pre-committed or speculative. As indicated above there is presently a significant amount of pre-commitment space in various stages of negotiation, however as with many elements of the market at this time, these have frequently been slow to reach completion.

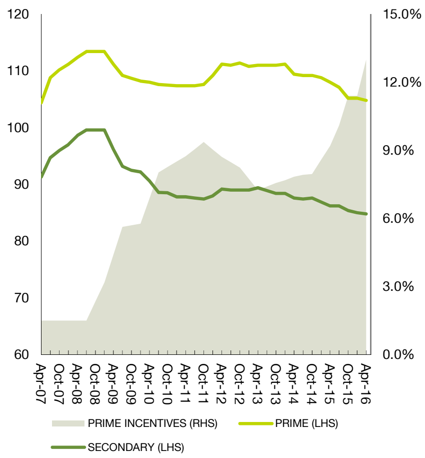
With new accommodation absorbing the majority of demand, particularly for larger warehouse and logistics space, backfill and existing space has become more difficult to lease. As a result market rents for existing buildings have continued to fall, due to the difficulty in competing against the allure of new buildings at highly competitive rental levels.

Across Brisbane the average prime net rents range between $100—110/m² with relatively little difference between precincts at this time. The average prime net rent across the city as a whole is $105/m² which represents a decrease of 3.0% over the past 12 months. Incentives have continued to increase, with the average for prime assets now sitting at 13%.

Once largely confined to negotiations over new assets or pre-commitment deals, incentives are now largely prevalent across the market, particularly for institutional owners and tenants above 3,000m². Private owners who choose not to negotiate on incentives will have to adjust their face rents accordingly.

Secondary rents have continued to soften, although at a slower pace, with the average net secondary rent sitting at $85/m², 1.6% below the levels of a year ago. While the secondary face rents are only slightly lower over the past year, average incentives have increased from 10% to 13%, resulting in a reduction in the effective rent of 5.0%. Despite the relatively mild reduction in both face and effective rents, the difficulties within the secondary market should not be under-estimated with face rents decreasing by 15% since the peak in late 2008. In addition, analysis of vacancy data indicates an average time on the market for vacant secondary stock (3,000m²+) of 16.5 months.

FIGURE 5
Brisbane Region Rents & Incentives
$/m² net rents (LHS) & prime incentives (RHS)



Source: Knight Frank Research

> "Aside from competitive rents, new accommodation provides the opportunity to upgrade both operational efficiency and environmental credentials"

Despite the availability of both prime and secondary existing stock, it is expected that the focus of leasing activity will remain in new accommodation, either D&C or speculative. Aside from highly competitive rents, supported by the low yield environment, new accommodation provides the opportunity to upgrade both operational efficiency and environmental credentials, which is attractive to the major corporate occupiers.

TABLE 3
Recent Leasing Activity Brisbane

Address	Region	Net Rent $/m²	Area	Term (yrs)	Tenant	Date
4-6 Brickworks Rd, Rochedale	SE	120	5,650	12	Japan Food Corporation#	Dec 16
Lot 101 Wayne Goss Dr, Berrinba	S	115	5,600	5	Avery Denison#	Jan 16
Peachey Rd, Yatala	SE	undis	30,400	5	Owens-Illinois^	Jun 16
2637 Ipswich Rd, Darra	SW	undis	12,000	20	Wild Breads^	Jun 16
100 Postle St, Acacia Ridge	S	undis	11,165	12	Lindsay Australia^	Jun 16
163 Viking Dr, Wacol	SW	115	5,799	3.5	Cotton On	Jun 16
170 Lindum Rd, Lytton	TC	100	6,329	5	Deluxe Freight	Mar 16
180 Holt St, Pinkenba	TC	114	9,354	7	Sandvik Mining	Jan 16
2637 Ipswich Rd, Darra	SW	128	5,700	10	Cascade^	Dec 15

SE South East SW South West S South TC Trade Coast ^pre-commitment #Spec
Source: Knight Frank Research

INVESTMENT ACTIVITY & YIELDS

Investment demand has remained elevated for the Brisbane industrial market, however a lack of available assets, particularly core, has hampered the total level of transactions. The calendar year of 2015 recorded $619.5 million in transactions ($5 million+), which was a decrease of 27% on 2014. To date in 2016, confirmed sales have only totaled $168.6 million, however a number of larger sales are understood to be close to fruition which could effectively see that total double in the short term.

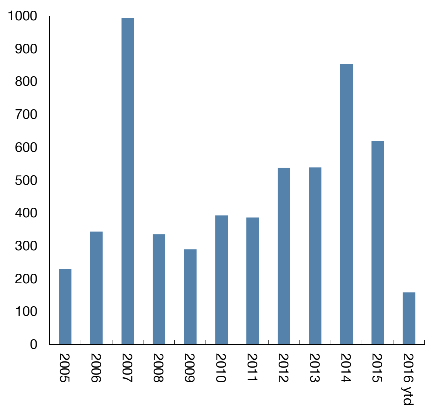
The largest investment sale was the $62.5 million Logos Properties purchase, on behalf of Swiss-based Partners Group, of the leasehold interest at 1-5 Bishop Drive on the Port of Brisbane. The purchase from IPS Logistics had a relatively short WALE for such a core asset, however leases on-port tend to be aligned with logistics contracts. Logos Properties, backed by a middle-east investor, also outlaid $53.60 million for a large parcel of land at Larapinta. These transactions assisted to make offshore purchasers the dominant purchaser class over the past year, accounting for 35% of transactions by value. Cache Logistics Trust, Sedco Capital and NZ syndicator Augusta Capital also made significant purchases.

The other dominant purchaser classes were the unlisted/syndicate sector (31%) and private investors (23%) who were also the largest sellers of assets. The unlisted sector activity was dominated by Fife Capital which has undertaken almost $99 million of acquisitions in the Brisbane industrial market over the past three quarters, amassing significant scale in the market.

Answering market demand for long WALE investments, there has been further vendor leaseback activity from companies such as Tyremax and QFFS.

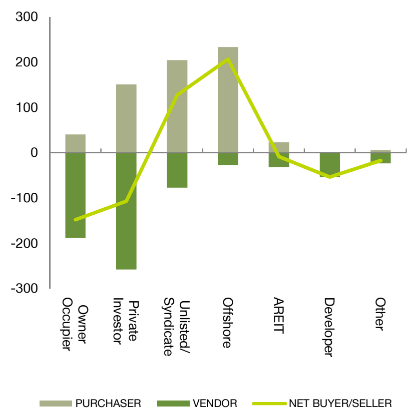
"Offshore purchasers accounted for 35% of transactions by value"

FIGURE 6
Brisbane Industrial Transactions
$million sales $5million+



Source: Knight Frank Research

FIGURE 7
Brisbane Vendor/Purchaser
$million sales $5million+ 12 mths to June 2016



Source: Knight Frank Research

TABLE 4
Recent Improved Sales Activity Brisbane

Address	Region	Price $ mil	Bldg Area m²	Core Mkt Yield (%)	WALE (yrs)	Vendor	Purchaser	Sale Date
1-5 Bishop Dr, Lytton	TC	62.50	73,000	undis	c3.0	IPS Logistics#	LOGOS Properties (Partners Group)	Mar 16
75 Ebbern St, Darra~	SW	14.50	7,110	8.34	5.0	QFFS#	Fife Capital	Feb 16
2642-2666 Ipswich Rd, Darra	SW	29.45	9,732	undis	12.8	Private Investor	Fife Capital	Feb 16
76 Quinns Hill Rd, Stapylton	SE	23.00	12,771	7.07^	8.9	Private Investor	Augusta Capital	Feb 16
102 Trade St, Lytton	TC	14.50	14,479	VP	VP	Frasers Property	Fife Capital	Dec 15
127 Riawena Rd, Salisbury	S	15.00	18,989	VP	VP	TNT Australia	Motorama Group	Dec 15
1937 Ipswich Rd, Rocklea	S	23.30	14,364	7.17	7.0	Tyremax#	Fife Capital	Nov 15
1 Lahrs Rd, Ormeau	SE	29.00	9,590	7.00	11.0	Private Investor	Propertylink (Sedco Capital)	Oct 15
203 Viking Dr, Wacol	SW	27.00	13,363	7.00^	7.9	One Investment Group	Cache Logistics Trust	Oct 15

Source: Knight Frank Research SE South East SW South West TC Trade Coast N North # vendor leaseback ^ passing yield ~cold store

Yields

The sustained increase in investor demand across all investment markets has translated into further decreases to core market yields across the Brisbane industrial market. Average prime yields, for properties with a WALE of 5-7 years, is currently 7.37%, across a range of 7.03% - 7.72%. This reflects a firming of 35 basis points over the past year and a total of 129 basis points from the cyclical high in 2009.

Similarly, and despite the relatively weak leasing fundamentals, secondary yields have also firmed over the past year to currently average 8.23% across a range of 7.72% - 8.75% which is a 34 basis point reduction over the past year. In line with the prime market, this is a 127 basis point reduction across the tightening cycle.

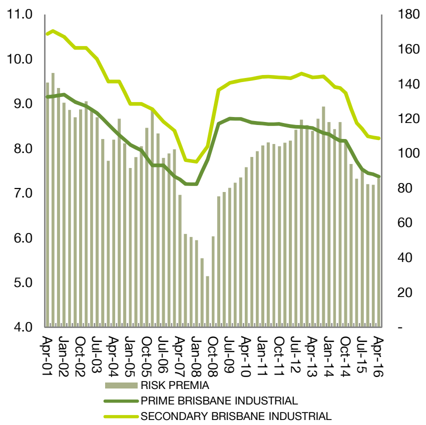
The divergence between conditions in the capital market and leasing market is creating some anomalies in the market. The first is the increased weight and value which is being allocated to longer WALEs. This can manifest either as investments with longer WALEs (5 years+) achieving yields in the "prime" range whether or not the building fabric can be considered as prime. Alternatively investments with particularly long WALEs (12 years+) have created a new category of "super prime" investments, the yields for which are 5.75% - 6.75% and appear to have no limit to their firming as bond yields return to record lows.

The other emerging inconsistency in the market is the increasing level of rental reversion in play for many assets. As market rents have fallen steadily over the past four years at least, assets with fixed annual rental reviews are quickly having the passing rent outpacing market rental levels. Therefore if an asset is sold 3-4 years, or more, into the lease term it is likely that the passing rent will be well above market levels.

In the current investment climate it has appeared that in these cases, particularly if the WALE is 5 years plus, the purchasers have priced the property predominantly on the basis of the passing yield, with little to no regard for the core market yield. Recent significant sales have occurred where it appears that the passing yield of 7.0—7.50% alone has been used for determining the purchase price of the asset. Given expected significant negative rental reversion at the end of the lease/s, these purchases indicated yield of sub-6% on a core market basis.

The hiatus in sales activity across Brisbane and also the delay in a number of large national portfolio sales appears to be unwinding with a strong end to the financial year and third quarter for transactions. It would seem that the resistance to the lower yields, in evidence earlier in the year has eased, supported by bond rates returning to cyclical lows as the US appears to back away from increasing rates again in 2016.

FIGURE 8
Brisbane Region Yields
% Core market yield (LHS) & bps Premia (RHS)



Source: Knight Frank Research

Outlook

- Occupier demand has remained skewed towards larger users and new accommodation, whether speculatively developed or D&C. Despite dominating the demand these tenants are still slow to conclude deals with little urgency in the market.
- Prime rents are expected to continue to soften as the level of backfill space competes with speculatively developed accommodation. Incentives now appear to be firmly entrenched, expanding from institutionally owned assets to encompass the whole market.
- Secondary rents are now back to the same levels that were in the market 10 years ago, with further gradual softening likely. If not suitable for a change of use, owners will need to choose between undertaking some refurbishment, lowering the asking rent or accepting a long let-up period due to the soft leasing market.
- Speculative development has picked up with approximately 70,000m² of completed speculative space available, and a similar amount of space under construction.
- The land market is improving with newly released estates such as Metroplex Westgate achieving good take-up of initial releases. There is also greater activity on infill sites in good locations as obsolete manufacturing stock is demolished and replaced with warehouse facilities.
- Investment demand is expected to remain high with the demand for core stock of an economic scale to remain largely unfulfilled in the Brisbane market. As investors look to build scale in Brisbane they are more likely to accept some rental reversion risk and/or immediate leasing risk.
- Yields have continued to tighten, although at a slower pace than a year ago. A return to lower bond yields indicates no upward pressure at this time.

COMMERCIAL BRIEFING
For the latest news, views and analysis of the commercial property market, visit knightfrankblog.com/commercial-briefing/

Definitions:
Core Market Yield: The percentage return/yield analysed when the assessed fully leased net market income is divided by the adopted value/price which has been adjusted to account for property specific issues (i.e. rental reversions, rental downtime for imminent expiries, capital expenditure, current vacancies, incentives, etc).
Prime Grade: Asset with modern design, good condition & utility with an office component 10-30%. Located in an established industrial precinct with good access.
Secondary Grade: Asset with an older design, in reasonable/poor condition, inferior to prime stock, with an office component between 10-20%.
WALE: Weighted Average Lease Expiry
Vacancy Methodology:
This analysis collects and tabulates data detailing vacancies (3,000m²+) within industrial properties across all of the Brisbane Industrial Property Market. The buildings are categorised into 1) Existing Buildings – existing buildings for lease. 2) Speculative Buildings – buildings for lease which have been speculatively constructed and although have reached practical completion, still remain vacant. 3) Spec. Under Construction – buildings for lease which are being speculatively constructed and will be available for occupation within 12 months.

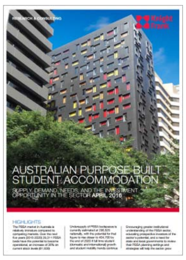
Knight Frank Research provides strategic advice, consultancy services and forecasting to a wide range of clients worldwide including developers, investors, funding organisations, corporate institutions and the public sector. All our clients recognise the need for expert independent advice customised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

RECENT MARKET-LEADING RESEARCH PUBLICATIONS

Brisbane Industrial Vacancy Analysis April 2016

Brisbane Office Fringe Market Overview May 2016

Melbourne Industrial Market Overview June 2016



Student Accommodation Insight April 2016

Knight Frank Research Reports are available at **KnightFrank.com.au/Research**

Important Notice
© Knight Frank Australia Pty Ltd 2016 – This report is published for general information only and not to be relied upon in any way. Although high standards have been used in the preparation of the information, analysis, views and projections presented in this report, no responsibility or liability whatsoever can be accepted by Knight Frank Australia Pty Ltd for any loss or damage resultant from any use of, reliance on or reference to the contents of this document. As a general report, this material does not necessarily represent the view of Knight Frank Australia Pty Ltd in relation to particular properties or projects. Reproduction of this report in whole or in part is not allowed without prior written approval of Knight Frank Australia Pty Ltd to the form and content within which it appears.

RESEARCH
Jennelle Wilson
Senior Director, Queensland
+61 7 3246 8830
Jennelle.wilson@au.knightfrank.com

Matt Whitby
Group Director, Head of Research & Consulting
+61 2 9036 6616
Matt.Whitby@au.knightfrank.com

INDUSTRIAL
Greg Russell
Head of Industrial, Australia
+61 7 3246 8804
Greg.Russell@au.knightfrank.com

Mark Clifford
Director
+61 7 3246 8802
Mark.Clfford@au.knightfrank.com

Chris Wright
Director
+61 7 3246 8861
Chris.Wright@au.knightfrank.com

Mark Horgan
Manager—Strathpine Office
+61 7 3482 6000
Mark.Horgan@au.knightfrank.com

VALUATIONS
Tim Uhr
Director
+61 7 3193 6877
Tim.Uhr@qld.knightfrankval.com.au

Ian Gregory
Director
+61 7 3193 6844
IanGregory@qld.knightfrankval.com.au

Newmark Knight Frank Global