RESEARCH

HIGHLIGHTS

- The Brisbane market has just completed a major supply surge with net additions of 303,000m² over the two years to January 2010. This, combined with a downturn in demand during 2009, saw the vacancy rate surge from previous lows of 0.7% up to 12.5%. A further three buildings under construction through to mid-2012 are likely to keep the vacancy in double digits over that period.
- Effective rents continued to soften over the past six months due to further growth in incentives; however the face rents now appear to have plateaued. Tenant demand has increased but has largely been limited to mining, engineering and infrastructure based companies.
- The investment market improved from late 2009 with a greater depth of purchasers emerging. There are indications of core market yields tightening by 15-20 bps, although this is partially due to softer underlying assumptions with only minor value uplift emerging to date.

Table 1
Brisbane CBD Commercial Market Indicators as at March 2010

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	913,337	11.6	71,468	71,900	660	25	7.80
Secondary	1,137,316	13.2	30,528	14,371	490	26	9.07
Total	**2,050,653**	**12.5**	**40,940**	**86,271**			

Source: Knight Frank/PCA ^ as at January 2010

SUPPLY & DEVELOPMENT ACTIVITY

The level of commercial construction across the Brisbane CBD has now peaked with only three projects still under construction. These three remaining projects are well spaced with forecast completion between late 2010 and mid-2012 which will not form another construction peak. Thus the amount of additional space added in 2009, at 209,000m² of new and 11,500m² of fully refurbished space, is not likely to be repeated in the medium term.

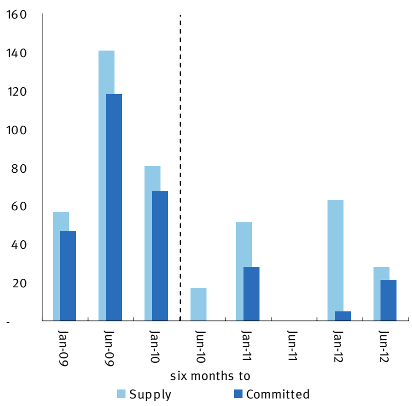
The next new building to come on-line is 123 Albert St, which is scheduled for completion at the end of 2010. With a current pre-commitment level of 72%, the building will be dominated by Rio Tinto, consolidating its operations from a number of locations.

For the majority of 2010, supply will be dominated by refurbished stock, largely the two Transit Centre buildings, with a total area of 29,120m². These buildings are undergoing base building services and common area upgrades with the floors to remain a mixture of fitted out and refurbished, open plan space. Other refurbished stock will include 160 Ann St (majority of the building), and 116 Adelaide St. While these buildings may not appear on the official supply list (only if withdrawn from the market during building works) they will have a significant influence.

New supply for 2011 is to be dominated by the completion of 111 Eagle Street which will add 62,400m² of premium stock to the Brisbane market late in that year. The developers have declined to confirm any tenant commitments.

The third project under construction is 145 Ann Street. This project, jeopardised by a lack of development finance, was purchased on a fund through basis by Colonial Property Office Fund in late 2009, allowing the project to proceed. The building has a current pre-commitment level of 67% (not including floors with first rights of refusal in place) and is due for completion in Q1 2012.

Figure 1
Brisbane CBD Supply
('000m²) Supply (new & refurb) & commitment



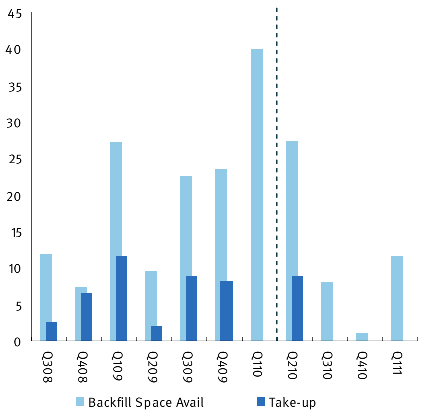
Source: Knight Frank

Beyond the buildings under construction there are presently no firm proposals for new office space within the market. While some sites of stalled developments are on the market or have changed hands (Vision site, 45 Elizabeth St and French Quarter), there remains selected sites with existing proposals and financially capable owners. However it would take major, long-term pre-commitments to bring these projects out of mothballs. Such tenant driven demand for new generation accommodation is plausible for 2013-2015 but unlikely before that time.

Backfill Space

Backfill space remains a major influence on the market. Backfill space continued to grow over 2009 as tenants moved into the new buildings. Knight Frank's analysis of backfill is limited to space made available through tenant relocations of >2,500m². Of the 124,000m² of backfill brought to the market during 2008 & 2009, 50% or 62,000m² remains available, of which half is secondary space. During the first quarter of 2010 a further 40,000m² has been added to the list and this will be followed by 27,000m² before the middle of the year (79% or 53,000m²of which is secondary space).

Figure 2
Brisbane CBD Backfill Space
('000m²) Backfill from tenant relocations >2,500m²



Source: Knight Frank

www.knightfrank.com

MAJOR OFFICE SUPPLY

2009 Completions

- 01 — 179 Turbot St – 24,657m² - APG – March 2009. 72% leased
- 02 — 53 Albert St – 18,440m² - Private – March 2009. 100% leased
- 03 — 275 George St – 40,306m² - Charter Hall – April 2009. 100 % leased
- 04 — 32 Turbot St – 34,500m² - Neilson Properties – June 2009. 96% leased
- 05 — 60 Albert St – 21,000m² -Trinity Funds Mgt – Sept 2009. 84% leased
- 06 — 140 Elizabeth St – 10,400m² - QIC – Q4 2009. 100% leased.
- 07 — 400 George St – 41,000m² - Leightons/Grosvenor – Q4 2009. 92% leased.

Under Construction

- 08 — 123 Albert St – 38,500m² - DEXUS – Q4 2010. 72% committed.
- 09 — 111 Eagle St – 62,400m² - GPT consortium – Q4 2011.
- 10 — 145 Ann St – 27,660m² - Leighton/CPOF – Q2 2012. 68% committed.

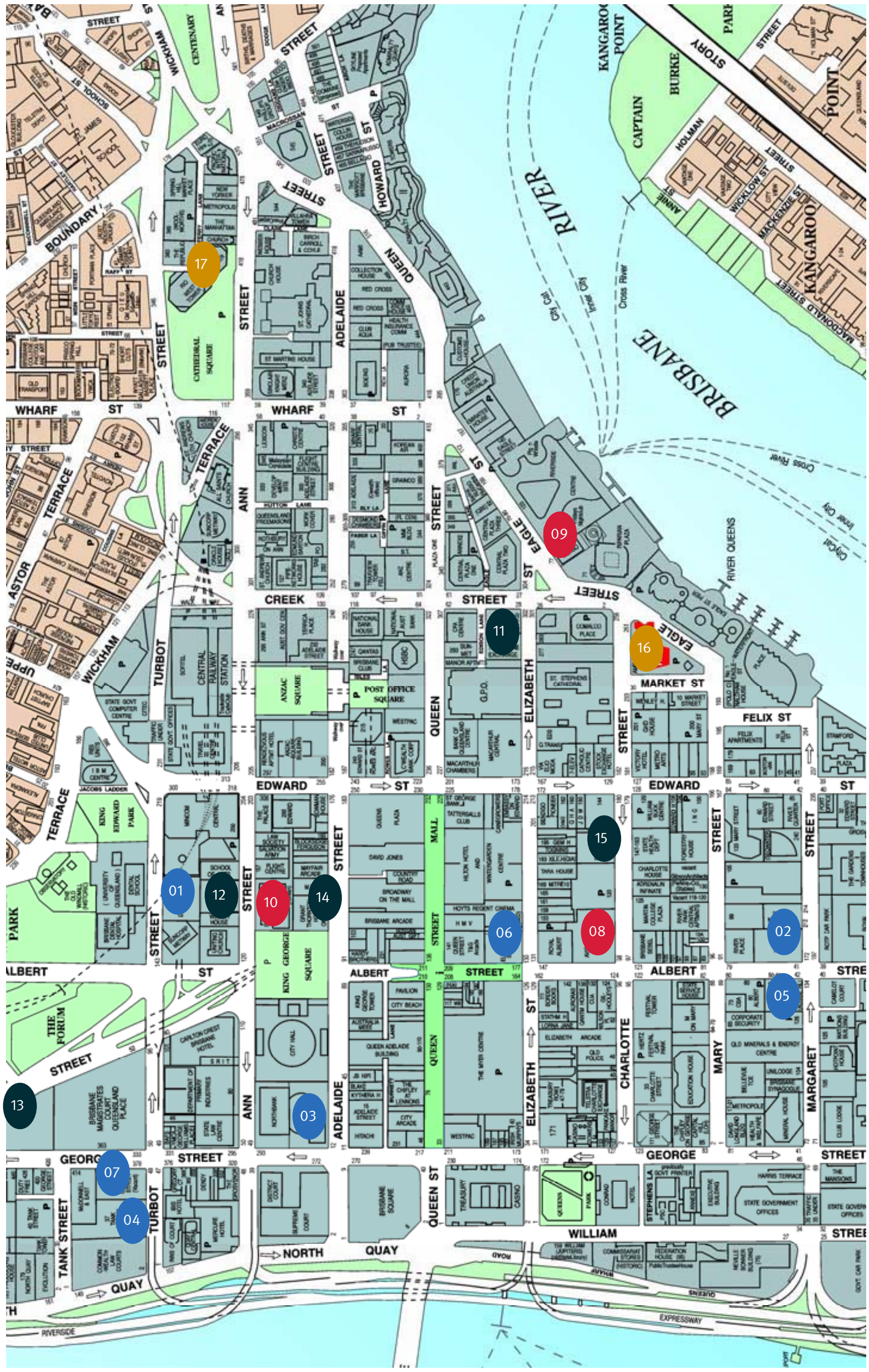
Refurbished Space

- 11 — 40 Creek St – 11,888m² - Charter Hall – Q2 2009. 17% committed.
- 12 — 160 Ann St – 12,570m² - Investa Wholesale – Q4 2009
- 13 — Roma Street Transit Centre – 29,120m² - GPT/APPF – Q1 2010
- 14 — 116 Adelaide St – 7,185m² - Private Investor – Q2 2010
- 15 — 150 Charlotte St – 11,255m² - Stockland – 2012

Existing larger space (5,000m²)

- 16 — 10 Eagle St – 10,250m² ^ - Brookfield – Q3 2009
- 17 — 410 Ann St – 6,373m²– Investa – Q1 2009.

Supply of over 5,000m² as at March 2010, excluding strata buildings ^non contiguous direct & sublease



TENANT DEMAND & RENTS

The vacancy rate for the Brisbane CBD has continued to increase as further supply additions impacted the market. The PCA office market survey recorded a total vacancy of 11.3% made up of 9.2% or 186,629m² in direct vacancy and 2.1% or 41,545m² of sub-lease space.

Table 2
Brisbane CBD Vacancy Rates
January 2010

Grade	Direct Vacancy %	Sublease Vacancy %
Premium	1.6	3.2
A Grade	7.6	2.0
A Grade KF view	*9.0*	*2.0*
B Grade	13.1	2.1
C Grade	5.1	1.7
D Grade	6.6	1.2
Total	**9.2**	**2.1**
Total KF View	***10.4***	***2.1***

Source: PCA/ Knight Frank

In Knight Frank's view there has been an inconsistency in the way newly completed buildings were treated between the July 2009 survey and the January 2010 survey by the PCA. In the July 2009 survey the newly completed 275 George St and 32 Turbot St were added as vacant space, despite fitout works for the major pre-commitments underway. In this survey the whole of 140 Elizabeth St and part of 400 George St were held off the stock lists despite the buildings being completed and undergoing fitout works. While this is largely an issue of timing, for the sake of consistency and comparison of market conditions over the past six months, Knight Frank has provided an alternative view to the official PCA survey.

If the completed buildings were added to the survey, the total vacancy rate for the whole of the CBD would sit in the order of 12.5% rather than 11.3%. In addition, the A grade market would be 11.0% rather than the official 9.6%. This essentially provides the 'worst case' scenario for the market. This discrepancy will be unwound at the next survey.

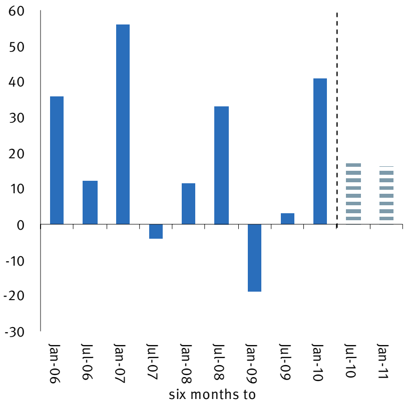
Net Absorption

Net absorption was surprisingly strong as the expansion by tenants on longstanding pre-commitments was not diluted by company downsizing across the rest of the market during the second half of 2009. This is a major positive for the Brisbane CBD market. The net absorption across the Brisbane CBD was again supported by growth of tenants relocating into the newly built space. These movements by larger tenants accounted for approx 37,500m². However the stronger than expected net absorption of 40,940m² was also due to the strength of the smaller tenant market. Despite the relatively sombre mood and staff reductions across many industries in 2009, the existing Brisbane market saw little to no reduction in total occupied space.

The current and future net absorption levels have also been supported by some of the larger, relocating tenants, not moving from their old accommodation or, having moved out expanding back into that space and removing it from the sublease market. This has recently happened to companies such as Worley Parsons (1,100m²) and the ATO (3,636m²). This is also reflective of the quick, but selective, growth in employment levels which is occurring across certain sectors of the economy, largely project driven.

Forecasts of net absorption in the short term show moderate gains as the economy is forecast to continue to improve over the next 18 months. With almost all of the newly completed space now leased, the market's attention will turn towards prime backfill space until the completion of 123 Albert Street at the end of 2010. This should continue to tighten the A grade vacancy rate during the course of 2010.

Figure 3
Brisbane CBD Net Absorption
('000 m²) per 6 month period

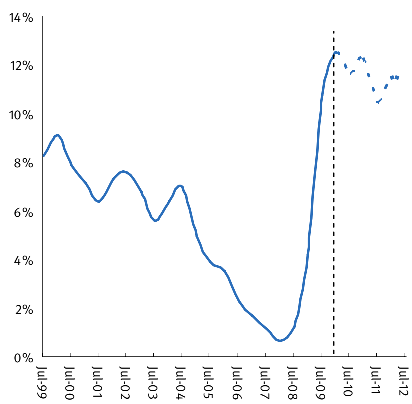


Source: PCA/Knight Frank

Anticipated Vacancy Levels

The vacancy rate for the Brisbane CBD at 12.5% (or 11.3% depending on definitions) has increased markedly as expected over the past 12 months, given the level of new supply combined with slower tenant demand. In the short term the continued addition of a new building each year during 2010 – 2012 will maintain the vacancy at relatively high levels. The net additions to stock to mid-2012 of 115,000m² will roughly be matched by the forecast net absorption of 127,000m² which leaves the market at a relative plateau over that time.

Figure 4
Brisbane CBD Vacancy
Total vacancy



Source: Knight Frank/PCA

Tenant Demand

Tenant demand and enquiry levels were substantially higher towards the end of 2009 and into the New Year as companies that had deferred making decisions during 2009 saw the New Year as a deadline to take action. These tenants had largely educated themselves about the market and space on offer and thus were quick to make decisions. In addition several larger mining and related industry projects or contracts created immediate demand for significant space for selected tenants – ie McConnell Dowell, Zektin and Worley Parsons.

After this flurry of activity, tenant enquiry has slowed to some extent. Tenant demand is still higher than for the majority of 2009, however has come back from what was a very active start to the year. With landlords pro-actively managing their tenants and with many having space within their buildings for the first time in several years, many deals are being done directly with tenants shifting within a building or taking on adjacent space. Formal tenant requirements have been recently dominated by larger professional firms with 2011/12 expiry, testing the waters and their existing landlord's nerves by going to the market.

Rental Levels

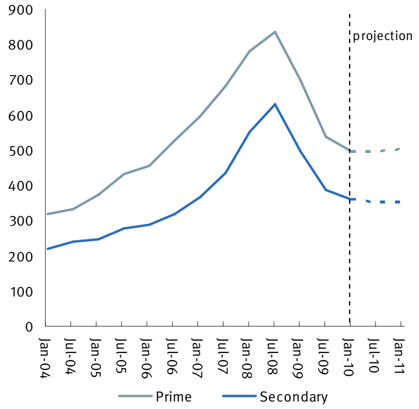
Rental rates continued to fall over the past six months, however at a far slower rate as effective rents are now near to the bottom for prime and potentially secondary space (however more deals are required at these price levels to confirm this). Prime face rents have begun to stabilise with the majority of the fall in effective rents over the past six months (4%), due to increasing incentive levels rather than movements in the face rents. On an annual basis, prime gross effective rents have fallen by 27.2% to March 2010 to average $495/m² gross ($660/m² gross face @ 25% incentives). This represents a fall in the effective rental level of 41% since the market peak of $835/m² gross effective in mid-2008.

As expected, the B grade buildings have been placed under pressure as tenants relocate into newer space. With a current vacancy rate of 15.2%, the competition for tenants between landlords of these grade of properties is intense. Face rents for secondary properties have been relatively stagnant over the past six months to average $490/m² gross, however incentives have continued to build and have reached an average of 26%.

Figure 5

Brisbane CBD Rents

$/m² p.a average gross effective rent



Source: Knight Frank

Prime rents now appear to be stabilising and may start to increase towards the end of 2010 if prime backfill continues to be favoured by the market, as most of the new accommodation is now largely taken up. Secondary rents may also be approaching their low-point, although this requires greater absorption of space by tenants to be confirmed. Secondary buildings can be a good option, particularly for project space, where there is good quality fitout and owners that are more accepting of a <5 year term.

Table 3

Recent Leasing Activity Brisbane CBD

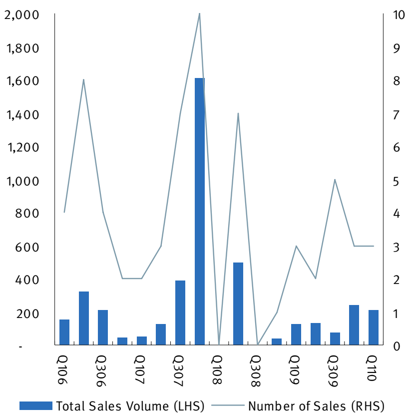
Address	Grade	Area (sq m)	Face Rental ($/m²)	Term (yrs)	Incentive (%)`	Lease Type	Tenant	Start Date
145 Ann St	A	3,387	650 g	10	<20	Pre-commitment	Grant Thornton	Jun 12
145 Ann St	A	7,447	625 g	10	20-25	Pre-commitment	GHD	Mar 12
145 Ann St	A	5,666	650 g	10	<20	Pre-commitment	Credit Union Aust	Mar 12
295 Ann St	A	7,876	537 g	10.3	undis	New	Q Rail	Sep 10
295 Ann St	A	1,219	550 g	10.4	undis	New	Q Rail	Jul 10
179 Turbot St	A	6,330	575 g	10	20-25	New	MBF (BUPA)	May 10
400 George St	A	1,040	675 g	8	<20	New	ACCC	Apr 10
179 Turbot St	A	1,800	625 g	8	25+	New	AHPRA	Mar 10
144 Edward St	B	1,538	540 g	4	20-25	New	Zektin	Mar 10
171 George St	B	1,012	<400 g	2	-	Sub-lease	McConnell Dowell	Mar 10
179 Turbot St	A	3,004	560 g	8	20-25	New	RTA	Mar 10
140 Creek St	A	2,473	600 g	4	undis	New	Centrelink	Mar 10
10 Eagle St	A	911	<400 g	2.5	-	Sub-lease	Aston Resources	Feb 10
10 Eagle St	A	954	650 g	3	25+	New	Talisman Energy	Jan 10
410 Ann St	B	3,386	486 g	10	-	New	NAVITAS	Jan 10
369 Ann St	B	1,503	525 g	3	20-25	New	Clough	Dec 09

Source: Knight Frank g = gross `Knight Frank's estimation of incentive calculated on a straight line basis.

INVESTMENT ACTIVITY & YIELDS

Investment sales in the Brisbane CBD picked up in the second half of last year after a long hiatus. As shown in Figure 6 below, both the quantum and total value of sales remain far below peak levels. While there was an increase in the number of CBD sales over the first three quarters of 2009, it was not until institutional purchasers returned in late 2009/early 2010 which took the total volume of sales beyond $200 million per quarter for the first time in 18 months.

Figure 6
Brisbane CBD Major Sales
Sales Volume >$5mil ($mil) & Number



Source: Knight Frank

During the whole of 2009, ten of the 13 sales recorded were under $25 million and were predominantly secondary properties. While this allowed for the disposal of non-core assets to mostly private investors, it did little to return long term confidence to the market. The first signs of confidence emerged as larger assets began to find purchasers. However this also co-incided with many listed entities, having recovered their balance sheet positions, removing their assets from the market. Thus several potential transactions in late 2009 (ie 100 Creek St & 60 Albert St) did not eventuate.

Nevertheless this returing confidence was soon demonstrated through the Commonwealth Property Office Fund's purchase and fund-though of the 145 Ann Street development for $208.1 million. The 27,660m² A grade building has a scheduled completion of March 2012. It is currently 68% committed with predominantly 10 year lease terms to tenants such as GHD, Credit Union Australia and Grant Thornton. The sale is understood to reflect a forecast initial yield of 8.0% and $7,598/m² of NLA. The 28 level building has 1,100m² floorplates and will target industry leading Green Star rating.

MANY VENDORS REMOVED THEIR ASSETS FROM THE MARKET AS THEIR BALANCE SHEETS RECOVERED

This confidence was consolidated by the purchase of 50% of 275 George Street for $166.0 million in January 2010. This heralded the long-awaited re-entry of international investment funds, with the purchser K-REIT being a property trust listed on the Singapore stock exchange. 275 George St is a 30 level commercial building that was completed in April 2009 with the office tower fully leased to Telstra and Qld Gas on 10 year terms. The sale, which included an income top-up, reflected an initial yield of 7.7% and an improved rate of $7,954/m². The market has now seen a further shift from vendors, with more assets being formally offered to the market, although with materially different vendor motivations and expectations.

Table 4
Recent Sales Activity Brisbane CBD

Address	Grade	Price ($ mil)	Core Market Yield (%)	NLA (m²)	$/m² NLA	Vendor	Purchaser	Sale Date
26 Wharf St	C	8.00	10.04 ^	3,088	2,591	TERF	Private Investor	Feb 10
10 Market St	B	34.25	10.06 ^	6,851	4,999	Heathley Inv Mgt	GDI Syndicate	Jan 10
275 George St	A	166.00*	7.70 ^#	41,738	7,954	Charter Hall Core+4	K-REIT	Jan 10
140 Alice St	Site	24.88	n/a	2,067`	12,037`	Devine Ltd	Sunland Group	Dec 09
145 Ann St	A	208.10	8.00~	27,660	7,598	Devine/Leighton	CPOF	Nov 09
96 Albert St	C	15.25	n/a	3,341	4,565	Devine Ltd	Private Investor	Oct 09
400 Queen St	B	15.75	9.44	3,983	3,948	TERF	Private Investor	Oct 09
410 Queen St	B	23.80	9.95	5,878	4,094	TERF	Private Investor	Sept 09
180 Queen St	C	22.00	8.45	3,667	5,999	Mirvac	Private Investor	Sept 09
157 Ann St	B	21.50	VP	6,679	3,219	MOT	CBIC	Aug 09
355 Queen St	B	8.68	8.85^	1,050	8,262	Private Investor	Private Investor	Aug 09
20 Wharf St	C	5.50	8.66	2,277	2,415	TERF	Private Investor	Aug 09
190 Edward St	C	11.50	8.51	2,452	4,690	Canegrowers	Private Investor	Aug 09

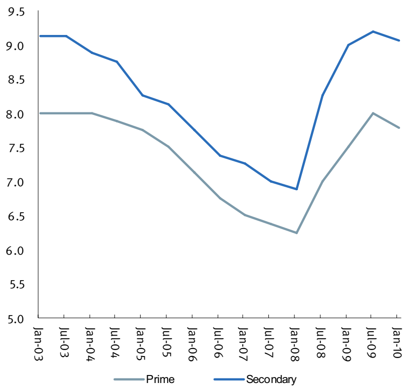
Source: Knight Frank *50% interest only ^passing yield ~forecast passing yield # includes income top-up `site and $/m² site

Although limited completed sales evidence is available, the general market consensus is that core market yields have firmed by 15-20 points since late 2009. However much of this can also be attributed to softer rental/take-up assumptions which underlie core market yields. The current core market prime yield range is 7.25% - 8.50% while secondary properties span the range of 8.50% - 9.65%. Passing yields remain under pressure as the market digests properties with widely varied WALEs, tenant covenants, passing incomes and current/anticipated vacancy levels.

Figure 7

Brisbane CBD Yields

(%) Prime & Secondary Core Market Yield



Source: Knight Frank

The gap between prime and secondary yields has continued to be substantial at 128 basis points as befits a market where there is far less tolerance to risk.

275 George St, Brisbane. A 50% share was purchased by K-REIT Asia for $166.0 million

OUTLOOK

The economic environment has continued to strengthen over the past six months, despite lingering concerns surrounding the sovereign debt in the Middle East and Europe. The recovery in commodity prices has rejuvenated several mining and related infrastructure projects, which has had a direct benefit on demand for Brisbane CBD accommodation.

While the major surge in new developments is now complete, the further three buildings that are under construction will add another 128,720m² over the next two years. This, in tandem with the large tracts of backfill space already on the market, will ensure that tenants retain the upper hand in negotiations over the medium term.

This is particularly the case in secondary buildings, with a growing overhang of vacant secondary space (150,000m² as at the January 2010 PCA survey) which will be further added to as the majority of backfill space (62,000m² of 76,300m²) to come onto the market during 2010 will be within secondary accommodation. Secondary rents now appear to have reached the level where the space becomes attractive on a cost basis and landlords who have adopted these pricing levels have found some success in the market.

Face rents, particularly for A grade and premium space have stabilised, with the slight softening in the effective rents over the past six months being attributable to increasing incentives. Thus the face rents have now fallen to the level where they will be 'defended' by building owners.

Tenant demand increased over late 2009 and early 2010 with most of the demand linked to engineering, mining or associated infrastructure industries. While these project related tenancies can quickly absorb large tracts of space, there are concerns that this demand is relatively one dimensional. Broader demand from service industries is likely to take a little longer to recover and hence our expectations of net absorption are higher for 2011 than 2010. This aligns with general economic forecasts which shows forecast Qld Gross State Product growth of 2.5% for CY2010, accelerating to 4.8% in 2011 (Access Economics).

The accelerating demand will be largely matched by the completion of the further three buildings and therefore the total vacancy rate is anticipated to stay within the range of 10.4% - 12.3% through to mid-2012. Effectively vacancy rates have hit peak levels, although vacancies are expected to fluctuate upwards as the new buildings, particularly the 62,400m² from 111 Eagle St, are added to the calculations.

VACANCY RATES EFFECTIVELY AT THEIR HIGHEST: ALTHOUGH WILL FLUCTUATE BETWEEN 10.4% - 12.3% TO MID-12

Capital market activity has increased over the past six months and the market improved to the point where 'distressed' assets have now largely been removed from the market. There are a few exceptions to this, particularly development sites within the CBD, however in general, vendors' perception of the market and rationale for selling have changed markedly between December 2009 to the current time.

The sales of two larger modern buildings to a local and international listed real estate trust was exactly the news that the market had been waiting for to underscore a change in market conditions. However since that time sales activity has been relatively scarce, largely due to their being far fewer assets on the market. Purchasers, and more particularly lenders, remain focussed on passing yields with only limited regard given to core market yields if there is short term vacancy risk.

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