

PERTH

INDUSTRIAL MARKET BRIEF DECEMBER 2016

Key Facts

Vacancy levels fell away recording a 22% decrease over the three months to October 2016.

Prime grade industrial rents continued to decline, with prime grade rents averaging \$88/m² as at October 2016, a fall of 3.8% over the past 12 months.

Core market yields have had a softening bias over the past six months, with average prime yields currently ranging between 7.17% to 8.25%.



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Recently, the vacancy rate has been dominated by an influx of vacant secondary grade buildings, with the common trend being businesses upgrading and relocating into better quality accommodation. This trend will continue to provide an excess of less desirable secondary grade options.

Economic Snapshot

The sentiment in the Western Australia economy continues to be a factor impacting the local industrial market. The ongoing affects of the mining industry directly impacts the industrial sector having been an integral part in both the Western Australia and National economy. The price of iron ore fell over 70% in 2015 to a record low of \$US38 a tonne but has since lifted to US\$80 a tonne as at late November 2016. The benchmark price has now risen by 82% so far in 2016 and more then double the low reached in late 2015.

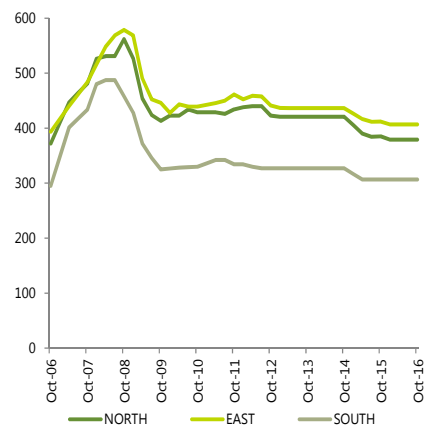
Companies requiring industrial space in the Perth market have either remained in their current locations or relocated into smaller space in desirable locations and better quality space. This is affecting the rental rates seen within the market and a decline is mostly apparent in the prime grade stock. The resources sector has a direct correlation with the Perth industrial market

where companies are contracting and not needing the same level of space as previously seen in the market.

Development & Land Activity

The continual flow of pre-commitment deals has kept some level of activity in the industrial land market but has not amounted to as active a market as recorded in 2008. This calendar year has seen development accounting for circa 200,000m² of newly developed pre-lease space added to the overall industrial stock. Development activity will be relatively subdued over the next 6-12 months. Areas that are considered less established or non-core industrial regions have seen limited speculative development and will continue to see low levels of activity due to the relative lack of demand and high levels of existing stock (mainly secondary) still to be absorbed.

FIGURE 1

Land Value by Region\$/m² average land value (2006–2016) <5,000m²

Source: Knight Frank Research

The 2016-17 State Budget mentions ongoing investment for infrastructure with a focus on transport related infrastructure (roads and public transport) budgeting \$1.8 billion with a further \$5.9 billion budgeted over the period to 2019/20. Key road and rail projects include the Forrestfield Airport link, Perth Freight Link, NorthLink WA and Gateway WA.

The \$2.2 billion Forrestfield Airport Link includes the construction of an underground tunnel between Bayswater and Forrestfield which will significantly improve traffic to and from Perth Airport. The \$1.1 billion NorthLink WA project will combine two projects, the Perth Darwin National Highway and Tonkin Grade Separations. Both are integral to improving freight efficiencies and travel time between the Perth Metropolitan region and North West Australia.

TABLE 2

Recent Industrial Leasing Activity Perth

Address	Region	Net Rent \$/m ²	Area m ²	Term (yrs)	Tenant	Date
58-68 Harrison Road, Forrestfield	East	73	15,250	10	M3 Logistics Pty Ltd	Oct-16
25-31 Casino Street, Welshpool	East	155	5,164	10	Tytec Logistics Pty Ltd	Oct-16
96 Armstrong Road, Hope Valley	South	97	2,619	5	WACO Kwik Form Ltd	Aug-16
7, 511 Abernethy Road, Kewdale	East	100	1,289	5	Advanced Electrical Equipment Pty Ltd	Jul-16
11 Prosperity Avenue, Wangara	North	131	1,800	6	Ranger Drilling Services Pty Ltd	Jul-16
5 Glyde Court, Malaga	North	120	2,039	3	Grama Bazita Service & Maintenance	Jul-16
521 & 523 Abernethy Road, Kewdale	East	100	4,113	10	TJM Products Pty Ltd	Jun-16
22 Ballantyne Road, Kewdale	East	85	2,350	1	Pindan Modular Pty Ltd	Jun-16
6 Dowd Street, Welshpool	East	94	4,325	7	Bluestar Global Logistics	Jun-16
31-33 Catalano Road, Canning Vale	South	87	2,755	5	Safemaster Safety Products Pty Ltd	Jun-16

Source: Knight Frank Research

Occupier Demand & Rents

The Perth industrial market is impacted by the resources sector and as a result companies are deciding to exercise lease options or move into smaller space requirements which is triggering downward pressures on rental rates, especially the prime grade stock.

However, the total available industrial space (>2,000m²) fell by 22% to 534,329m² as at October 2016. Perth's industrial sector has continued to be affected with escalating levels of vacant space in the market, this fall in the overall volume of vacant stock was attributed to a large portion of stock

being leased. Leasing activity in space above 10,000m² included 2 Bannister Road, Canning Vale and 4 Lodge Drive, East Rockingham. Activity above 5,000m² included six deals which were finalised, adding to the take up for the quarter.

Over the quarter to October 2016, leased prime space increased nominally totalling four transactions while leased secondary space amounted to 10 deals. The trend has continued from the middle of the year whereby an increasing number of older style secondary grade properties are taken up. The amount of secondary grade stock available is over 70% of the vacant stock meaning the trend of

TABLE 1

Perth Industrial Market Indicators as at October 2016

Precinct	Avg Prime Rent		Avg Secondary Rent		Core Market Yields (%)		Avg Land Values			
	\$/m ² net	(%p.a)	\$/m ² net	(%p.a)	Prime	Secondary	< 5,000m ²	(%p.a)	1–5 ha	(%p.a)
North	91	-4.4	63	-	7.25 – 7.75	8.50 – 10.00	379*	-1.6	223	-
South	83	-7.4	63	-	7.25 – 8.50	8.50 – 10.00	306	-	227	-0.1
East	89	-7.8	65	-	7.00 – 8.50	8.50 – 10.00	407	-1.2	293	-1.7
Perth Average	88	-3.8	64	-	7.17 – 8.25	8.50 – 10.00	364	-1.0	248	-0.7

Source: Knight Frank Research

*Average excludes Osborne Park land values

tenants migrating from secondary to prime grade buildings is still evident.

Even though vacancy levels dipped over the three months to October, the vacancy rate is still higher than average. This is providing challenges for landlords to sustain current levels of competition to secure tenants leading to heavy discounting of rental levels coupled with increasing incentives now above 10%. Over the year to October 2016, average prime market rents have fallen by 3.8% across the Perth region to \$88/m² net. The secondary market has remained unchanged at \$64/m² net across the precincts.

The Perth industrial market vacancy lifted in mid 2016 as a result of approximately

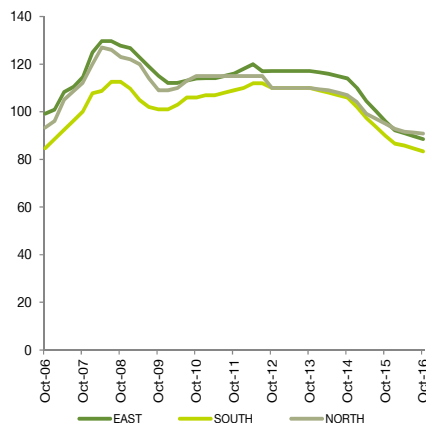
200,000m² of newly developed pre-lease space being completed. In the Jandakot industrial area alone a 42,000m² warehouse was pre-leased to K-Mart, Reece took 26,000m² and Super Amart and Oceaneering Australia both took 25,000m² and 9,000m² respectively. Similarly Hazelmere added 40,000m² for CEVA Logistics, 24,000m² was pre-leased to Mainfreight Transport, Austrans Container Service took 28,000m² and Wridgeways acquired 10,000m².

Moving forward, this will continue to impact the level of backfill space where tenants relocate into new industrial space. As a result the market is likely to see upward pressure on secondary grade stock vacancy, remaining around the 500,000m² level or rising further over the short to medium term.

Group for \$240 million. Leases in place at the time of sale included Linfox, Coca-Cola, Toll INPEC and MTU. This sale demonstrated the apparent demand for investments with long lease terms and secure occupier covenants.

The average prime core market yield is currently 7.71% (an average range of 7.17% - 8.25%), a reduction of four basis points over the past 12 months, albeit a softening bias over the past six months. Investment interest in prime assets, particularly for investors seeking a core, passive income stream has remained relatively firm. Average secondary core market yields have remained stable over the past six months at 9.25% (an average range of 8.50% - 10.00%).

FIGURE 2
Perth Region Prime Rents
\$/m² average net rent (2006–2016)



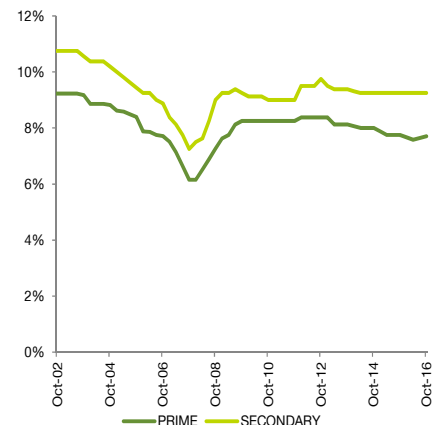
Source: Knight Frank Research

Investment Activity & Yields

Recent sale transactions reflect a growing sale and leaseback trend emerging in the Perth market. Private investors and owner occupiers remain the most active purchasers in the market.

Investors are focusing on well located assets with strong value-add prospects. The sale of Stockyards in December boosted the overall volume of transaction for the year resulting in a higher than average number of transactions. The Stockyards Industrial Estate was acquired by Charter Hall from Goodman

FIGURE 3
Average Core Market Yields
Prime & Secondary (2002-2016)



Source: Knight Frank Research

TABLE 3
Recent Investment & Vacant Possession Sales Activity Perth

Address	Region	Price \$ mil	Area m ²	Passing Yield (%)	WALE (yrs)	Vendor	Purchaser	Sale Date
1 Stockdale Road, O'Connor	South	5.17	2,302	7.80	3.6	Listor Pty Ltd	Linton Investments Pty Ltd	Sep-16
52 Cooper Road, Cockburn Central	South	2.15	1,731	VP	VP	Mine Maintenance Management Pty Ltd	Co-opoly Property Holdings Pty Ltd	Aug-16
5 Chifley Brace, Jandakot	South	3.30	2,135	VP	VP	Lenori Property Group & Miktad Holdings Pty Ltd	Kia Kaha Property Trust	Aug-16
34 Canvale Road, Canning Vale	South	2.40	2,100	VP	VP	Semangat Pty Ltd	Two Oceans Pty Ltd	Jul-16
14 Ledger Road, Balcatta	North	5.35	2,692	VP	VP	Grama Bazita Australia Pty Ltd	PFJ Commercial No. 6 Pty Ltd	Jun-16

Source: Knight Frank Research VP—Vacant Possession



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Outlook

The level of pre-commitment leasing demand has softened as compared to previous years. This trend could change over the next 12 months. The level of activity in the works could potentially lead to developments in the medium term. Speculative development has been limited. Moving forward it is expected that the older, less desirable stock will be repositioned or refurbished to cater to the demand from tenants which is for a more modern and efficient facility.

The current level of tenant interest in the market has remained stable with leasing enquiry expected to remain positive in the short term. This will more than likely be in the more traditional and established areas.

In terms of investment and activity there is still demand in the industrial sector but it is confined by location. The lack of good quality Prime grade investment stock in well located precincts has slowed and is unlikely to improve.

There will more than likely be a rise in secondary grade activity as the activity in prime grade opportunities becomes less because stock will continue to be absorbed in the better quality and prime locations as opposed to the less desirable stock which will, as a result, be left on the market.

The land value associated with secondary grade investments could prove to be appealing to potential investors looking to expand their portfolios.

Definitions:

Prime: Asset with modern design, good condition & utility with an office component 10-30%. Located in an established industrial precinct with good access.

Secondary: Asset with an older design, in reasonable/poor condition, inferior to prime stock, with an office component between 10-20%.

Core Market Yield: The percentage return/yield analysed with the assessed fully leased market income is divided by the adopted value/price which has been adjusted to account for property specific issues (ie rental reversions, rental downtime for imminent expiries, capital expenditure, current vacancies, incentives etc).

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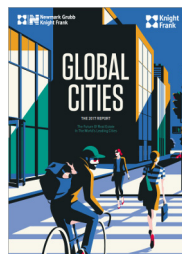
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