WEST PERTH

OFFICE MARKET BRIEF NOVEMBER 2015

Key Facts

The West Perth vacancy rate remained stable at 11% from 11.1% in January 2015.

The West Perth office market recorded net absorption of 1,397m^2 over the six months to July 2015.

Incentive levels have risen in the last 12 months to around 30-35% of lease terms.

New office developments in West Perth are highly unlikely in the short to medium term.

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The West Perth office market is expecting very little supply over the next few years, unlike the Perth CBD market which has 188,500m^2 currently under construction.

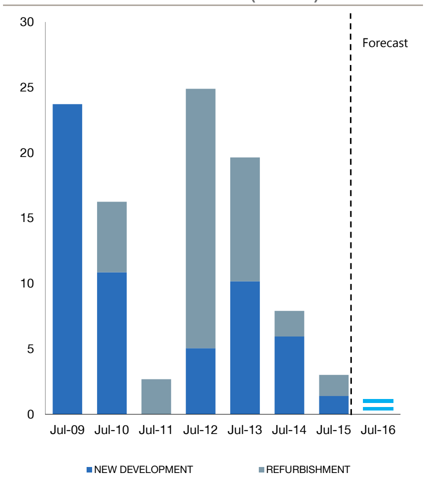
Development Activity

The West Perth office market, unlike the Perth CBD is expecting very little supply over the next 12 months. Supply for the six months to July 2015 totalled a mere 850m^2 according to the Property Council of Australia (PCA), lifting the total stock base to 423,690m^2. This addition to supply was at 1 Prowse Street, a nine level apartment building with a five level office building fronting Prowse Street.

West Perth has next to no stock under construction currently, with 1162 Hay Street, a two level office building with an NLA of 1,419m^2 presently undergoing a building upgrade with additional parking and internal improvements. Apart from this refurbishment, completing imminently, there is no other supply under construction or being refurbished or due for completion in 2016 and beyond.

Mooted and proposed projects for the West Perth area total approximately 35,000m^2. Due to the current state of the West Perth office market it is unlikely that these will break ground in the short to medium term. As the Perth CBD market is expecting new incoming supply of circa 134,556m^2 over the short term, West Perth is highly unlikely to develop new office buildings as the Perth market will take time to absorb the CBD supply.

FIGURE 1
West Perth Office Supply
New and Refurbished Stock ('000m^2)



Source: Knight Frank Research/PCA

Net Absorption & Vacancy

Net absorption has been quite volatile over the past few years, with negative growth recorded in 2013, then lifting to 1,642m^2 in the six months to July 2014. The West Perth office market recorded total net absorption in the six months to July 2015 of 1,397m^2 after totalling negative 6,159m^2 in the six months prior. Competitive pricing of vacant office space in West Perth is attracting new tenants to the markets higher grade office buildings. The increase in net absorption of 1,519m^2 for A Grade and 1,644m^2 for B Grade buildings has in turn lifted the overall absorption into positive territory over the first half of 2015.

The vacancy for the overall West Perth market increased from 3.3% in July 2012 to 11.1% as at the end of 2014, with vacancy levels increasing each consecutive six month period, albeit stabilising over the last six months.

However there is still 46,470m^2 of office space vacant in the market. As at July 2015 the PCA recorded West Perth's vacancy rate at 11.0%, slightly lower than the 11.1% recorded as at January 2015.

The Prime grade vacancy for West Perth office totalled 7,911m^2 representing 5.7% of total prime stock (138,459m^2) down from 6.8% recorded in the six months to January 2015. The vacancy seems to have peaked in January 2015 with a total of 9,430m^2.

The Secondary grade vacancy increased from 13.2% to 13.5% over the six months to July 2015. This amounts to 38,559m^2 of vacant secondary office space currently in the market. Falling rents have encouraged tenants to seek better quality office space which is demonstrated by the vacancy being heavily skewed to the secondary market.

In terms of sub-lease vacancy there was 4,504m^2 of space available in the six months to July 2015, down from 7,502m^2 in January 2015. The nominal contraction in total vacancy was a result of absorption increasing over the six month period with the sublease vacancy falling to just under 3,000m^2 since January 2015.

Tenant Demand & Rents

The current economic environment is challenging for landlords, but is producing some much needed opportunity for businesses to reduce operating expenses. This reduction could aid the transition to a more diverse tenancy mix in West Perth. Tenant demand remains soft due to the uncertainty in current economic conditions as well as businesses looking to improve cost efficiencies and consolidate their office accommodation.

Frasers Property (ex Australand) has confirmed their relocation to 1 Havelock Street taking 1,236m^2 on the second level. The now globally owned development company is moving from their West Leederville office and taking an eight year lease term.

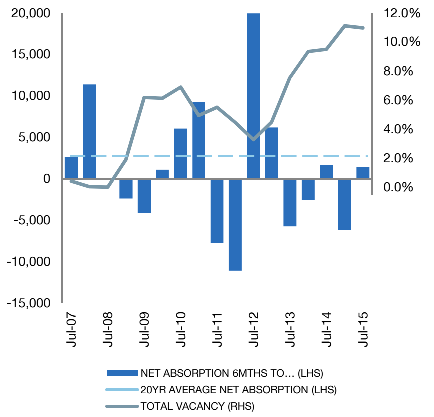
In this market tenants are adopting a more cautious approach before committing to a lease. This is apparent when looking at the fall in rents and shorter lease terms within contracts. Leases secured in the last 6-12 months have generally been for a term of 3-5 years.

High vacancy levels have added further pressure on landlords to accept rental levels much lower than two years ago. Prime net face rents have fallen gradually each quarter since April 2012. Average net face rents are currently sitting at \$440/m^2 as at October 2015, which is an annual drop of 8.5%. Similarly, secondary net face rents have been on a downward trend since April 2012 (\$508/m^2) and are currently averaging \$325/m^2 as at October 2015. This fall is due to strong competition as leasing options become comparably cheaper. As a result, tenants are benefitting from increasing incentives in the form of rent free periods and capital contributions for office fit outs which are in turn minimising the costs associated with tenant relocation.

FIGURE 2

West Perth Vacancy & Net Absorption

Per six month period (m^2)



Source: Knight Frank Research/PCA

TABLE 1

West Perth Office Market Indicators as at October 2015

Grade	Total Stock (m²)^	Vacancy Rate (%)^	Annual Net Absorption (m²)^	Annual Net Additions (m²)^	Average Net Face Rent (\$/m²)	Average Incentive (%)	Average Core Market Yield (%)
Prime	138,459	5.7	1,463	1,404	440	35	7.75—8.50
Secondary	285,231	13.5	-6,225	196	325	35	8.50—9.25
Total	**423,690**	**11.0**	**-4,762**	**1,600**			

Source: Knight Frank Research ^PCA data as at July 2015

The Perth CBD is becoming much more appealing to office tenants with 2015 seeing a number of tenants move from suburban locations into the Perth CBD office market. The move is widely due to very attractive incentives reaching as high as 45-50% compared to lower rates in suburban office markets. Prime and secondary incentive levels in West Perth have crept up to 30%-35% of lease terms for the second half of 2015. These levels have increased but are not yet at the levels being recorded in the CBD.

TABLE 2

Recent Leasing Activity West Perth

Address	NLA m²	Term yrs	Tenant	Lease Type	Date
1 Havelock Street	1,236	8	Frasers Property	New	Oct-15
513-525 Newcastle Street	178 343	3	3 Monkeys 3 Monkeys*	New Renewal	Sep-15
2 Richardson Street	139	2	IMX Resources	New Direct	Aug-15
41-47 Colin Street	350	1.75	Sheffield Resources	New#	Jul-15
44a Kings Park Road	300	3	Oilex	New Direct	Jun-15

Source: Knight Frank Research *Audio Visual #Sublease

Investment Activity & Yields

The cyclical change from a decade of resources sector investment spending has come to the tail-end, resulting in soft tenant demand for the West Perth office market. Investment sales activity has remained somewhat subdued over the first half of 2015. The lack of quality stock combined with uncertain economic conditions has affected sales with 2015 reporting minimal activity.

The West Perth office market recorded no sales transactions during the first six months of 2015. In August the first sale for the year was finalised at 53 Ord Street with a NLA of 6,864m^2 to Singaporean firm Mapletree Investments. The five level A Grade modern office space with a yield of 7.4% is 100% occupied by Texas energy corporation ConocoPhillips with a lease term expiring in 2022.

The second half of 2014 saw the sale of 16 Parliament Place for $22.60 million on a core market yield of 7.50% in October 2014 and 21 Colin Street for $2.35 million in August.

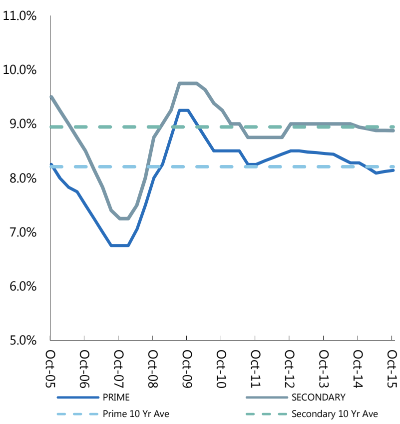
It has also been reported that Perth-based fund manager, Primewest, have listed the Australia Federal Police Station located on 619 Murray Street as part of $250 million portfolio.

> "No sales transactions were recorded during the first six months of 2015."

FIGURE 3

West Perth Prime & Secondary Yield

Quarterly with long term average



Source: Knight Frank Research

Market yields in West Perth as at June 2015 typically range from 7.75%-8.50% for Prime office space and 8.50%-9.25% for Secondary assets. Yields for good assets are expected to remain around current levels with the possibility of some tightening should demand in investments continue to build.

TABLE 3

Recent Sales Activity West Perth

Address	Grade	Price $ mil	Core Market Yield (%)	NLA m²	$/m² NLA	WALE (yrs)	Vendor	Purchaser	Sale Date
53 Ord Street	A	59.00	7.40	6,864	8,596	7.4	Primewest	Mapletree Investments	Aug-15
16 Parliament Place	B	22.60	7.50	2,989	7,561	5.6	Primewest	Private Investor	Oct-14

Source: Knight Frank Research

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, West Perth 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 future supply, there are no buildings under construction or being refurbished that are due for completion in 2016 and beyond. Knight Frank expects the vacancy to remain at around current levels (11%) 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 the low Australian dollar and high interest rates, it is anticipated that investment demand for West Perth office assets will improve with the majority of the 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 for sale.

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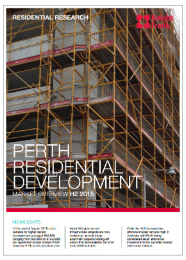

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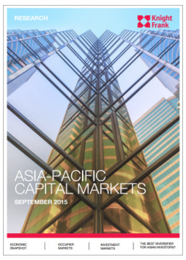

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