

BRISBANE SUBURBAN

OFFICE MARKET BRIEF MARCH 2016

Key Facts

Supply for 2016 of 30,720m² reflects the conservative development environment, with **82%** pre-committed

Prime effective rents have softened marginally as **incentives increased to 30%**; but face rents were stable

Investment demand for **core assets remains strong**, but the **lack of scale** in this sector has curtailed transaction activity



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A conservative development environment has ensured that the majority of supply has been fully or significantly pre-committed. Investment demand for modern assets with longer WALES ensures these new assets are highly sought.

Development Activity

Additions to supply for the Brisbane Suburban market were only modest over 2015 with 15,660m² delivered over two buildings. With nine buildings currently under construction the total supply for 2016 is expected to be higher, covering some 30,720m². As befits the conservative development environment all but one of the buildings currently under construction were either fully or partly pre-committed, either from a tenant or an owner occupier.

The speculative development is the 3,910m² first stage within Innovation Square at the Brisbane Technology Park, Eight Mile Plains. Elsewhere in the park, at 21 Brandl St, a 3,000m² building is also under construction, triggered by a 1,500m² pre-commitment to Woolworths. Both Innovation Square and the wider Brisbane Technology Park have a number of further sites available for development, which are currently slated to deliver c25,000m² as demand warrants.

Other fully committed projects include the 6,000m² Puma Energy pre-commitment at BTP Hamilton, which is close to completion. The Brisbane Airport Corporation is building a 5,000m² facility for Airservices Australia at Boronia Rd and a 2,300m² office for Hanson in the Skygate Precinct. Owner occupiers are Churches of Christ finalising a 4,400m² headquarters in Kenmore and the CBIC (City of Brisbane Investment Corporation) developing 4,235m² at 375 Hamilton Rd, Chermside which will be occupied by a BCC library and North Regional Business Centre.

Despite some increased competition for sites from residential developers, the pipeline of supply remains plentiful from both smaller sites and future stages of existing office parks. In addition to Eight Mile Plains there are further stages at BTP Hamilton (c6,000m²), Southgate Cannon Hill (26,650m²), Boggo Road redevelopment (6,428m² Stage 1), Yeerongpilly Green (c9,800m² Stage 1) and the Mirvac redevelopment at Eagle Farm Racecourse (c13,000m²).

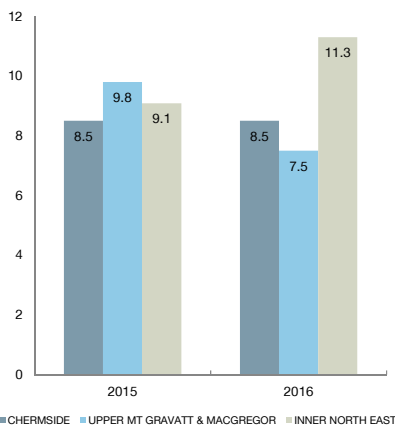
Net Absorption & Vacancy

Vacancy within the Chermshire precinct has been static over the past 12 months at 8.5%, after ticking higher mid-2015 at 9.1%. With no new supply or withdrawals in the precinct over the past year the net absorption was a minuscule -17m².

Upper Mt Gravatt & Macgregor improved over the course of 2015 with vacancy in January 2016 of 7.5%, down from 9.8% a year prior. This precinct also recorded no withdrawals or additions over the year and the improvement came as existing vacant space was absorbed, sometimes following refurbishment, resulting in annual net absorption of 2,351m².

Total vacancy has increased in the Inner North East to sit at 11.3% in January 2016. This has come in part due to new

FIGURE 1
Brisbane Suburban Office
% total vacancy by selected precinct



Source: Knight Frank Research/PCA

TABLE 2

Selected Brisbane Suburban Projects (2,000m²+)

Project	NLA m ² & (% Leased)	Developer	Status	Date
Barry Alexander Dr, Springfield	12,500 (93%)	Springfield LC	Complete	Mar 15
33 Remora Rd, Eagle Farm	3,160 (60%)	Shayher Group	Complete	Jun 15
331 Macarthur Ave, Hamilton	6,000 (100%)	BTP Hamilton	Construction	Mar 16
41 Brookfield Rd, Kenmore	4,400 (100%)	Churches of Christ #	Construction	Jun 16
2 Clunies Ross Ct, Eight Mile Plains	2,218 (-)	Graystone	Construction	Jun 16
21 Brandl St, Eight Mile Plains	3,000 (72%)	Graystone	Construction	Jun 16
Boronia Rd, Eagle Farm	5,000 (100%)	BAC	Construction	Jun 16
The Boulevard, Skygate Precinct, Eagle Farm	2,300 (100%)	BAC	Construction	Aug 16
375 Hamilton Rd, Chermshire	4,235 (100%)	CBIC	Construction	Dec 16

BAC Brisbane Airport Corporation CBIC City of Brisbane Investment Commission # owner occupier

Source: Knight Frank Research

supply (33 Remora St, Hamilton) and whole building vacancy in buildings such as 16 Edmondstone St, Kelvin Grove, 9 Hercules St, Hamilton and 39 Navigator Place, Hendra. Despite this the net absorption increased over the year by 2,150m².

Tenant Demand & Rents

Tenant demand across the suburban market has remained concentrated in the small to medium size bracket, with only relatively few larger requirements. Larger requirements have generally triggered new development, supported by the low yield environment for modern, long-WALE assets. Recent examples have included the Puma Energy 6,000m² commitment to Hamilton and the mooted c6,000m² commitment to Yeerongpilly Green by Catholic Education.

Effective rents for the suburban market have continued to be under pressure over the past year. Prime face rents have remained stable across the three main precincts, however incentive levels for the Chermshire and Mount Gravatt markets have increased to 30%, bringing them in line with the Inner North East market.

The Inner North East, which has a greater proportion of more modern, large floorplate assets, remains the most expensive of the suburban precincts with an average gross face rent of \$460/m². As this precinct abuts the Fringe market in places it is the most closely aligned with the larger CBD and Fringe markets. Overall rents are expected to show very little change in the short term across the suburban market with landlords facing increasing competition from CBD secondary space where

TABLE 1

Selected Brisbane Suburban Office Market Indicators as at January 2016

Sub-Market	Total Stock (m ²)	Vacancy Rate (%)	Annual Net Absorption (m ²)	Annual Net Additions (m ²)	Av. Gross Prime Face Rent (\$/m ²)	Av. Prime Incentive (%)	Average Prime Core Market Yield (%)
Chermshire	34,298	8.5	-17	-	400	30	7.50—8.50
Upper Mt Gravatt & Macgregor	101,515	7.5	2,351	-	410	30	7.50—8.50
Inner North East	150,067	11.3	2,150	3,160*	460	30	7.50—8.50
Total[^]	285,880	9.6	4,484				

Source: Knight Frank Research/PCA [^]Represents the totals only for the precincts above, does not reflect the whole Brisbane Suburban market * gross supply NB See definitions on Page 4

generous deals are on offer as a result of the higher vacancy levels. Tenant demand, particularly for the larger suburban tenants (2,000m²), is expected to remain focussed on new construction with investment market demand for modern assets subsidising rental levels.

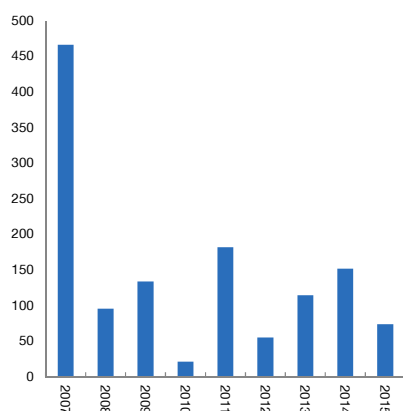
Investment Activity & Yields

The high investment demand for office assets did not transfer to the Brisbane Suburban market in 2015 with only \$73.55 million in transactions recorded (over \$5 million). In part this is due to a lack of suitable stock, and the generally relatively lower quantum of investment in the suburban market which tends to fall

FIGURE 2

Brisbane Suburban Office

\$ total sales (over \$5 million)



Source: Knight Frank Research

TABLE 3

Recent Leasing Activity Brisbane Suburban Market

Address	Precinct	NLA m ²	Face Rent \$/m ²	Term yrs	Tenant	Date
The Boulevarde, Eagle Farm	INE	2,300	undis	10	Hanson*	Aug 16
Macarthur Ave, Eagle Farm	INE	6,000	c365 n	15	Puma Energy*	Jul 16
21 Brandl St, Eight Mile Plains	SE	1,500	undis	undis	Woolworths*	Jun 16
25 Musgrave Rd, Kelvin Grove	INE	2,200	205 g	5	Halfbrick	Dec 15
7 Clunies Ross Ct, Eight Mile Plains	SE	1,525	475 g	10	Toshiba	Sep 15
Bld 19-2404 Logan Rd, Eight Mile Plains	SE	1,500	440 g	7	Metro Health South	May 15

n net g gross *pre-commitment INE Inner North East SE South East

Source: Knight Frank Research

below the thresholds required for larger AREIT and offshore investors.

The largest sale during 2015 was the \$31.23 million paid by a CorVal administered unlisted fund for the Puma Energy headquarters, which is now close to completion. The reported fund through capitalisation rate of 7.2% is indicative of the premium currently paid by the market for assets which are both modern and also have longer lease tails, with this sale reflecting a WALE of 15.0 years.

The first sale of 2016 was of a far larger scale than that which occurred during 2015 and at \$57 million accounts for three quarters of the total transaction level for 2015. The sale at 28 Macgregor St, Mount Gravatt is a 14,286m² building which is fully leased to the ATO with 4.9 years remaining on the lease. While it is

understood that the ATO will shortly be coming to the market for a new brief to amalgamate their suburban office holdings it is not certain that this asset will be vacated at lease end. There is also additional potential development land of approx 3,000m² attached to the property. The yield of 8.28% is reflective of the balance between long term risk and the attraction of a fully leased building with a WALE which takes the building beyond the immediate leasing market weakness.

Suburban prime yields currently range between 7.50% and 8.50%, with the lower yield range only available to the larger, modern assets. Secondary assets continue to trade on a broad range with some owner occupier activity in place for secondary stock. Secondary yields, depending on their tenant profile, can vary between 8.75% and 9.75%.

TABLE 4

Recent Sales Activity Brisbane Suburban Market

Address	Precinct	Price \$ mil	Core Market Yield %	NLA m ²	\$/m ² NLA	WALE	Vendor	Purchaser	Sale Date
28 Macgregor St, Mount Gravatt	SE	57.00	8.28	14,286	3,990	4.9	Private Investor	LaSalle Asia Opportunity Fund IV	Jan 16
473 Lutwyche Rd, Lutwyche	INE	22.50	7.05	4,925	4,569	10.0	Harvest Property	Private Syndicate	Sep 15
Macarthur Ave, Hamilton	INE	31.23	7.20	6,000	5,205	15.0	Alceon Group/ Graystone	CorVal Syndicate	Jul 15
371 Macarthur Ave, Hamilton	INE	13.50	7.44 [^]	2,450	5,510	5.0	Alceon Group/ Graystone	Private Syndicate	Jul 15
33 Corporate Dr, Cannon Hill	E	17.00	VP	4,218	4,030	n/a	Merlin Australia Sub Pty Ltd	Endeavour Foundation	May 15

Source: Knight Frank Research [^] passing yield SE South East INE Inner North East E East



Outlook

The suburban market is expected to experience a continuation of recent market conditions into the medium term. With the vast majority of new supply tied to either a partial or full pre-commitment, the supply cycle for the suburban markets is benign. There is significant longer term potential supply across a number of office park and mixed use projects, however at this time there is only limited appetite to speculatively develop any of these assets, with pre-commitments required.

Demand for suburban office space, in line with the wider office market, has remained subdued with tenants relatively likely to relocate at lease end, however with minimal expansion. The exception at this time is coming from Queensland Government tenants, particularly Health.

Face rents are also expected to remain at similar levels to the current, with competition from both the Fringe and CBD markets high. Incentives will be under pressure, particularly for secondary assets which have not undertaken a recent major refurbishment. For tenants which require a suburban location due to parking needs or to service a trade area opportunities for both existing and new developments remain plentiful enough to ensure tenants have the upper hand.

The strong investment demand of the past two years did not result in high transaction levels for the suburban market, in part due to the lack of scale in Brisbane suburban investments. Yields for newly built assets with long WALEs to major corporations may continue to see downward pressure over 2016, however for other assets yields are expected to stabilise.

Suburban Market Definitions:

Chermside and Upper Mt Gravatt & Macgregor are two precincts tracked by the PCA, however they form only selected hubs of the wider Brisbane Suburban market. Knight Frank has recently begun to track a new precinct known as the Inner North East, which is defined as the area to the north east of the CBD, beyond the existing Brisbane Fringe (Fortitude Valley, Bowen Hills) but not as far north as the Chermside precinct. This includes suburbs such as Hamilton, Hendra, Eagle Farm, Nundah, Windsor, Lutwyche and surrounding areas.

Knight Frank classifies the Brisbane suburban office market in the following broad regions: **Inner North East** (as above), **North** (which includes the PCA precinct of Chermside plus areas such as Strathpine), **East** (ie Murarie & Cannon Hill), **West** (ie Indooroopilly, Darra) and **South East** (which includes the PCA precinct of Upper Mt Gravatt & Macgregor plus areas such as Eight Mile Plains).

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