Brisbane Fringe Office Market

April 2024

Brisbane Fringe market continues to strengthen with demand led by newly developed space

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Key Insights

New supply has been key in drawing strong net absorption to the market. As the supply pipeline thins, the lack of quality contiguous options will support rental growth

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13.9%

Total vacancy falling

Total vacancy decreased from 14.9% in July 23 to 13.9% in January 2024, with net absorption outweighing new supply H2 2023 (PCA).

45,830

Sqm net absorption 2023

Net absorption was higher in H2 2023, taking the annual net absorption to the highest level across Australia for 2023 (PCA).

-3,400

Sqm net additions forecast

For CY 2024 supply will be limited to refurbished space, the obsolescence of older stock is expected to keep net additions modestly negative.

9.5%

Prime gross face effective growth 2023

The steady reduction in contiguous space, particularly in high quality assets, has continued to drive rental growth in the Fringe

6.5%

Prime gross face rent growth forecast 2024

With limited new supply in the market over the coming year, rental growth will continue to be supported

7.55%

Prime median yield

The upward adjustment in yields is coming to the end of the cycle, softening by 185bps from the recent lowpoint. Institutional capital remains cautious but private capital is returning.

Brisbane Fringe Office Market Indicators – January 2024

Grade	Total Stock sqm	Vacancy Rate %	Annual Net Absorption sqm	Annual Net Additions sqm	Av Gross Face Rent $/sqm	Av Incentive %	Effective Rent Gth % y/y	Core Market Yield %*
Prime	729,618	14.1%	41,137	30,630	678	42	9.5	6.80 – 8.25
Secondary	614,248	13.8%	4,693	6,275	556	41	9.7	8.25 – 9.50
Total	1,343,866	13.9%	45,830	36,905				

Source: Knight Frank Research/PCA * assuming WALE 5 years

Moderating Economy

Economy has been supported by high population growth

LOWER INFLATION IS BRINGING MORE CONFIDENCE THAT THE CASH RATE CYCLE HAS PEAKED

Australian quarterly inflation is now sitting at 4.1% for 2023 with good progress made over the course of the year from the peak of 7.8% in December 2022. A similar trend across many advanced global economies has increased confidence that the interest rate cycle peak has been reached. While headline inflation has fallen substantially, the final contraction needed to bring CPI down to the target range may be longer and more difficult. This is being seen in the US at the moment with stubborn services inflation having stabilised at 4.95% for February.

The pace of reduction in cash rates and associated longer-term bonds remains in question. For Australia, any cash rate reduction is not expected until the third or even fourth quarter of the year, with limited falls expected prior to the start of 2025. The 10-year bond rate, presently sitting between 4.00%-4.30%, is forecast to return towards the neutral long-term expectation of c3.5% during 2026.

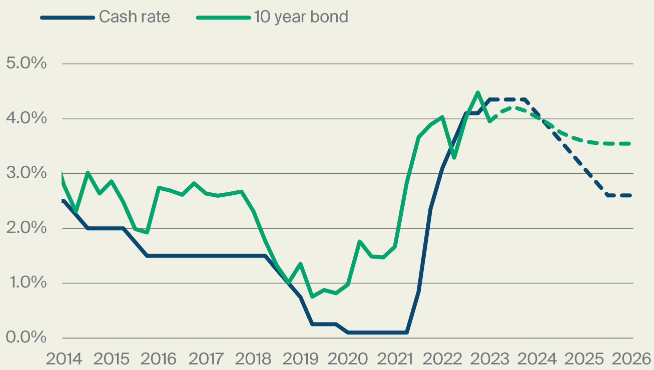
GDP GROWTH SLOWING AS EXPECTED

The Q4 2023 Australian GDP quarterly growth was 0.2%, a steady decline from the 0.3% of the previous quarter. This bought annual GDP growth to 1.6% for Q4 2023. While this is well below the target range, this represents steady slowing to the economy and outside of the COVID period represents the lowest growth since 2000. Economic growth is forecast to remain subdued for the next year with Oxford Economics predicting 1.6% for 2024 (Qld 3.2%) before recovering in 2025 (Aust 3.3%, QLD 3.1%). Economic growth has been boosted by the strong population growth over the past year with the per capita GDP growth negative for the past three quarters and down 1% overall.

QUEENSLAND HAS BENEFITTED FROM THE SURGE IN POPULATION GROWTH

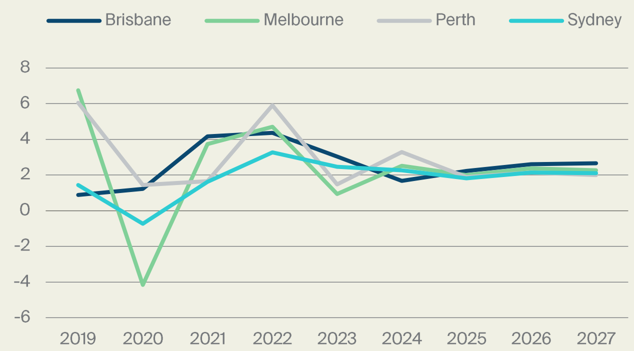
Queensland recorded 2.7% annual population growth to September 2023, ahead of the strong national figure of 2.5%.The temporary surge in net offshore migration has boosted population growth across Australia. Sixty-one percent of Queensland's population growth came from offshore migration during the year, compared to 83% for Australia as offshore migration reached 548,770 people. This surge is expected to be short-lived with a tiered reduction over the next four years base to the migration baseline of 235,000 per annum. Interstate migration remains an important source of population uplift for Queensland ensuring long term accelerated population growth. During FY23, 30% of the net interstate inflow came from those 0-19 years old, indicating strong family relocation.

Interest Rate Outlook



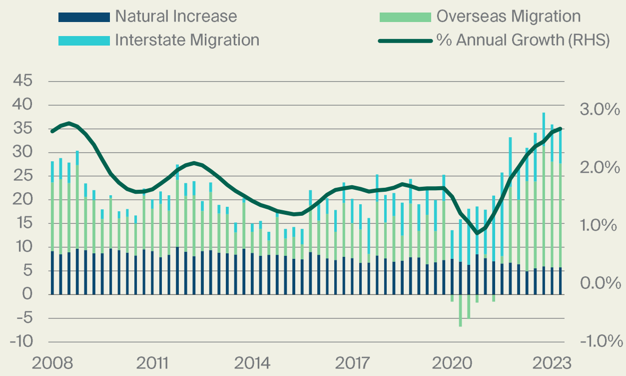
Source: Knight Frank Research, Oxford Economics

Office Workforce Growth by City
% change y/y, selected cities



Source: Knight Frank Research, Oxford Economics

Population Growth Queensland
Quarterly '000 increase by component & total growth rate



Source: Knight Frank Research, ABS

Nation-leading take-up

New supply continuing to boost net absorption

BRISBANE FRINGE LED AUSTRALIA FOR NET ABSORPTION IN 2023

The Brisbane Fringe market, buoyed by new demand and contiguous prime supply, led the Australian markets for net absorption in 2023. This comes as several of the larger southern office markets are experiencing contraction in office space occupied.

In contrast, the Brisbane Fringe and to a lesser extent the Brisbane CBD, has continued to benefit from new demand. This is due to expansion of growth industries (energy, construction), new tenants to the market and a continued overall migration of tenants from suburban locations to areas of greater amenity and quality of building form.

NET ABSORPTION BOOSTED BY INFLOW INTO NEW SUPPLY

The link between net absorption and new supply has re-established in the Fringe market since 2021. As the market matured in the decade from 2001, with an influx of new stock, there was a close relationship between the quantum of new supply and net absorption. Impacted by wider economic factors, this relationship broke down 2011 – 2020. While new supply was well supported and sought by tenants they were frequently moving from within precinct, thus not impacting the overall net absorption.

From the completion of 14 Stratton St in 2021 there has been a far greater correlation between new supply and net absorption. In part this has been due to this new supply drawing new users or new requirements into the Fringe market. Mater Health fully occupied 14 Stratton St by consolidating administration from a number of suburban locations. 152 Wharf St, Spring Hill was fully pre-committed by the ATO, which was new to the Fringe market, additionally 470 St Paul's Terrace, Fortitude Valley brought tenants such as Schneider Electrical into the Fringe precinct. The most recent major completion at 895 Ann St, Fortitude Valley has been committed by an undisclosed Federal Government requirement new to Brisbane.

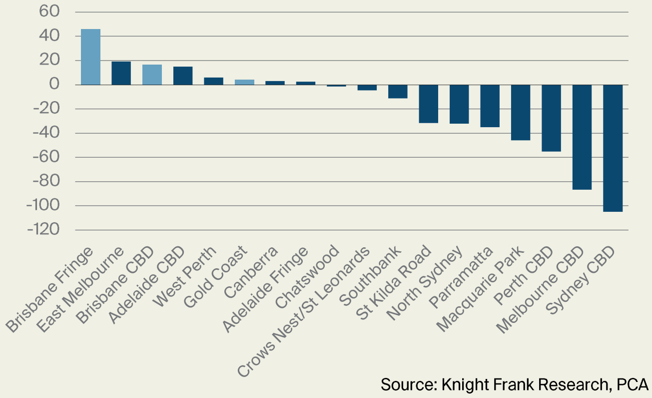
GREATER AMENITY FOR STAFF CONTINUES TO DRIVE RELOCATION

The prime market has dominated net absorption in the Fringe market in the past two years. The constant demand to improve amenity to maintain staff engagement, retention and attendance will continue to support quality buildings and locations across the Fringe precincts.

Additionally there has been steady demand from tenants in suburban or industrial locations to upgrade the location of their office, which will continue to support well located assets of all grades.

Annual net absorption CY2023

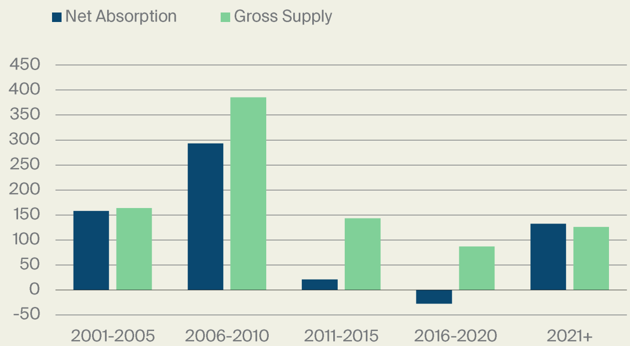
'000 sqm



Source: Knight Frank Research, PCA

Brisbane Fringe Demand and Supply Balance

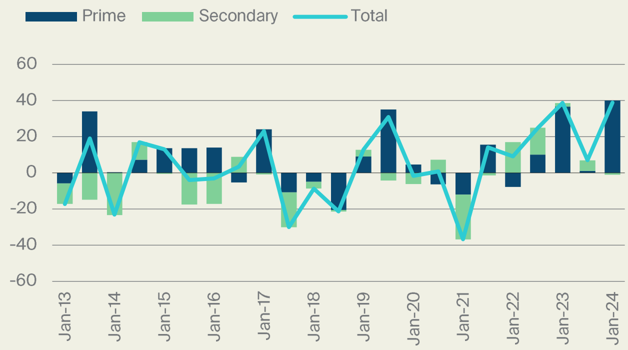
'000 sqm



Source: Knight Frank Research, PCA

Brisbane Fringe Net Absorption

'000sqm prime and secondary



Source: Knight Frank Research, PCA

Feasibility limiting new construction starts

AFTER HIGHER SUPPLY IN THE PAST TWO YEARS THE FUTURE IS FAR MORE CONSTRAINED

After supply additions of almost 100,000sqm in the past two years, there is little new stock expected in the next two years. The completion of 895 Ann St, Fortitude Valley means there is no major Fringe asset under construction. Supply over the past two years represented a stock uplift of 7.8% (3.9% p.a). While this was decidedly higher than the prior 10-year period, it remains well below the major stock surge of 2008-2011 when office stock increased by 37% over the four years (9.3% p.a).

There are several sites, particularly through the Urban Renewal corridor, with existing development approval for office development. However, ongoing difficulties in achieving feasibility hurdles for commercial development are continuing to stifle new development starts. These hurdles include the timeframe and cost of construction, the lack of builders in Brisbane with the experience and capacity to take on additional office construction, cost of funding and higher yields mitigating the end value of the development.

APPETITE FOR RESIDENTIAL DEVELOPMENT IS DIVERTING POTENTIAL DEVELOPMENT SITES

The increasing institutional investor demand for built-to-rent is causing some sites to convert to a BTR focus, however, despite a deep pipeline of approved BTR projects only a few have progressed to construction, with feasibility still difficult in this sector. 301 Wickham St, Fortitude Valley, previously slated for a 25 level office development, is now owned by Arklife with a 327 unit development approved but not yet commenced.

The wider residential development market is also experiencing an uplift in development appetite, although facing similar construction cost and funding headwinds.

TENANT DEMAND WILL SUPPORT NEW DEVELOPMENT IN THE MEDIUM TERM

In the short term, refurbishment and small developments will provide the only options for refreshed space, with no significant new assets under construction. Smaller developments like 56 Doggett St, Newstead (3,393sqm) and refurbishment at 388 Brunswick St, Fortitude Valley (2,160sqm) will provide boutique supply. The full building refurbishment of 30 Cribb St, Milton (8,623sqm) will provide contiguous floor availability with occupancy from early 2025, providing one option for larger tenants.

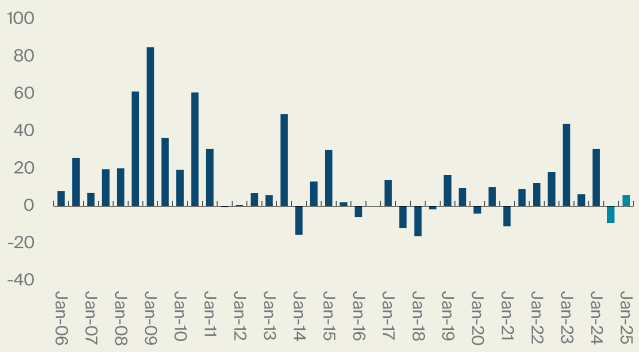
There are active or expected tenant briefs which have the potential to trigger new construction of assets of scale (10,000sqm+). However, in the current conditions even a major pre-commitment may not guarantee construction .

Significant Supply

Property	Office Area	Timing	Developer [Commitment]
Recently Completed			
Greenhouse- West Village, West End	6,425	H2 2023	Seisuki House [67% Frasers Property]
895 Ann St, Fortitude Valley	24,000	H2 2023	DWS [100 % Undisclosed Fed Govt Tenant]
Construction			
30 Little Cribb St, Milton (Full Building Refurb)	8,623	Q1 2025	Shayher Group
Actively Marketing			
56 Doggett St, Newstead	3,393	H2 2024	Private Investor
K2, 1 King St, Bowen Hills	21,950	STP	LendLease
166-180 Breakfast Creek Rd, Newstead	18,556	STP	Leishman Property
58 Morgan St, Fortitude Valley	11,500	STP	Quintessential Equity
52 Alfred St, Fortitude Valley	32,000	STP	LaSalle IM/Partners Group
South City Square, Woolloongabba	Up to 20,000	STP	Pellicano Group

Source: Knight Frank Research ^ includes income support

Brisbane Fringe Net Additions
'000sqm net of gross supply and withdrawals



Source: Knight Frank Research, PCA

Prime vacancy to tighten

RECENT FALLS IN VACANCY EXPECTED TO CONTINUE

Total vacancy across the Brisbane Fringe market decreased to 13.9% from 14.9% in the six months to January 2024. Prime vacancy decreased to 14.1% from 16.0% with positive net absorption of 40,081sqm above supply additions of 30,630sqm. The inclusion of a fully-leased new building was a major reason the vacancy rate fell, but solid demand outside of this new supply was also driving the vacancy rate lower. The secondary market vacancy rate increased from 13.6% to 13.8% in the six months to January 2024. Much of this was within the B grade market where vacancy increased to 13.4%, C grade fell to 13.8% and D grade was stable.

MOST PRECINCTS RECORDED FALLING VACANCY

The Inner South vacancy increased to 16.4% in January 2024 from 16.0% mid-2023. There was supply of 6,836sqm in the precinct, higher than the net absorption of 3,688sqm.

Vacancy decreased in the Urban Renewal precinct from 13.3% to 11.8%. Net absorption of 30,015sqm well outweighed the new supply of 24,794sqm with activity concentrated in the larger modern assets.

Spring Hill vacancy fell to 12.5% from 14.6% in the past six months and down from 16.7% a year ago. There were no stock changes and net absorption remains steady at 3,298sqm.

Toowong vacancy is now 7.5%, down from 8.4% in July 2023. There were no changes to the stock base with the vacancy influenced by positive net absorption of 693sqm.

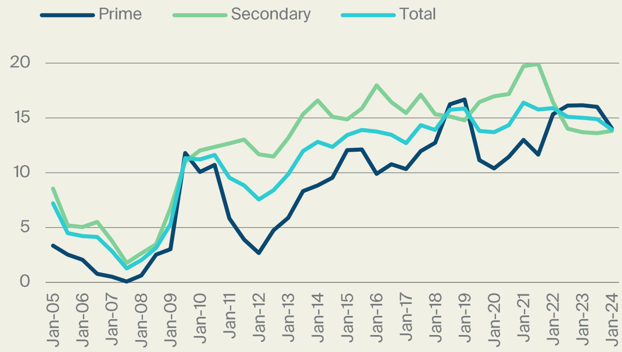
The Milton market remains the precinct with the highest vacancy rate at 19.1%, down from 19.7% six months ago. There was positive net absorption of 1,227sqm in the period. The vacancy rate was elevated by the inclusion of the fully vacant Milton Green Building 5 (8,623sqm) with the commencement of refurbishment works now imminent.

FURTHER FALLS IN PRIME VACANCY EXPECTED

Without new stock to spur above-average net absorption, the short term net absorption is forecast to remain positive, but at lower levels than over the past two years. This steady net absorption, in a climate of little additional supply, will continue to bring the total vacancy rate down. Vacancy is expected to fall to c12.5% over the course of 2024,

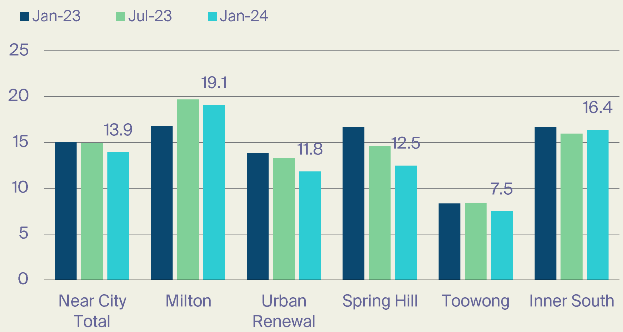
Similar to the CBD, the Fringe market now has quite limited full floor and contiguous vacancy which will increase competition for market leading assets. With upgrading to remain a key strategy, the prime market will tighten more quickly than the wider market. This will bring prime vacancy lower than total vacancy for the first time since early 2022.

Brisbane Fringe Vacancy
% vacancy rate prime v secondary



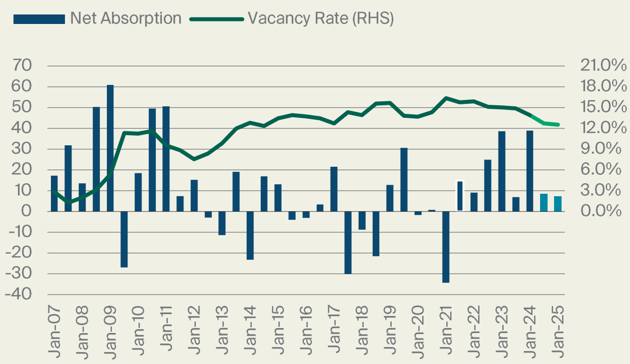
Source: Knight Frank Research, PCA

Brisbane Fringe Vacancy Rate
% vacancy rate by precinct



Source: Knight Frank Research, PCA

Brisbane Fringe - Demand & Vacancy
'000 square metres (LHS), % vacancy (RHS)



Source: Knight Frank Research, PCA

Strong rental growth

RENTAL GROWTH IS STRONG, DRAWN UPWARDS BY THE BEST IN CLASS ASSETS

Prime face rents grew strongly during 2024, up by 7.6% in the year to average $678/sqm. This has been driven by uplift in the new and best-in-class assets, where there is limited contiguous vacancy, and through benchmarking to the CBD, where prime rents have also appreciated strongly. With the top of the market driving growth there is a wider range of prime rents in the market. New construction and buildings with a prime location are now in the $725 – 775/sqm bracket, while older or more vanilla A grade product may be within the $600 – 700/sqm range. This bifurcation of the market is expected to continue to widen.

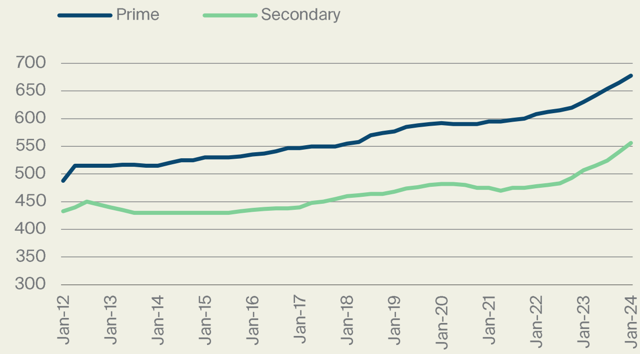
Prime incentives did receive some downward pressure over 2023, but overall remain elevated at an average of 42%, down from 43% in the year. Incentives are expected to remain an important factor in facilitating tenant relocation but will gradually contract in the coming two years.

Secondary rents have also seen good growth during 2023, up by 9.7% to an average of $556/sqm gross face.

ECONOMIC RENTS TO TRIGGER DEVELOPMENT REQUIRE A FURTHER STEP UP FOR THE MARKET

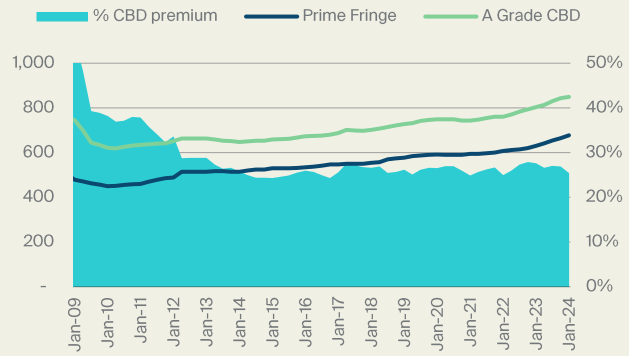
The gap between A grade CBD rents ($850/sqm gross face) and prime fringe rents is currently 25.4%, slightly lower than the recent gap, but in line with long term averages. The uplift in economic rents to trigger new Fringe developments has anecdotally put those rents in the $850 – 900/sqm range. This means new developments are competing directly with existing CBD A grade stock, even as the supply of contiguous A grade floors falls in both the CBD and Fringe markets. While tenant demand remains for new supply, this will require an additional significant step-up in rents.

Brisbane Fringe Rents
$/sqm gross effective prime v secondary



Source: Knight Frank Research

Fringe and CBD Relativities
$/sqm av gross face rents (LHS), % CBD A grade premium (RHS)



Source: Knight Frank Research

Recent significant tenant commitments

Occupier	Property	Precinct	Size sqm	Face Rent $/sqm	Incentive %	Term yrs	Start Date
Peabody Energy	31 Duncan St, Fortitude Valley	Urban Renewal	2,005	730	40+	10	Dec 2023
Youi Insurance	825 Ann St, Fortitude Valley	Urban Renewal	1,601	670	40+	5	Dec 2023
Workday	88 Tribune St, South Brisbane	Inner South	1,012	725	35-40	5	Sep 2023
Built	12 Commercial Rd, Newstead	Urban Renewal	842	610	Sub-20	u/d	Oct 2023

Source: Knight Frank Research u/d - undisclosed

Investment market still constrained

INVESTMENT SALES REMAIN LIMITED

Transaction volumes for the Brisbane office market fell during 2023, as did most major markets across Australia and globally. This is due to an ongoing gap between vendor and purchaser expectations with some vendors still defending book values which are slowly adjusting to the changed market and yield expectations.

Even though the cash rate is considered to have reached its peak for this cycle, the easing cycle is expected to be slow during 2024 and into 2025. This is not yet providing the relief in debt cost and required investment hurdle rates that many market participants had expected.

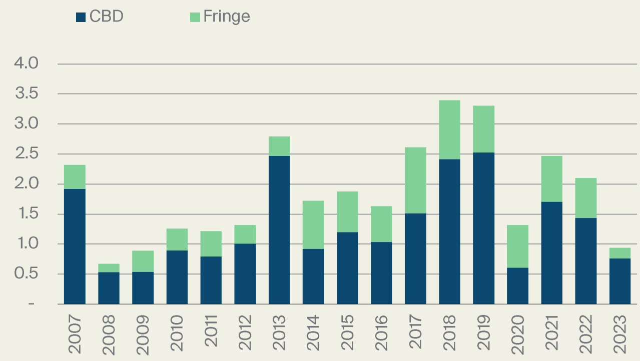
After a quiet 2023 the first months of 2024 have remained subdued with relatively few formal campaigns run for major office assets. Sales which have occurred have been skewed towards private buyers, and frequently in the $10- 20 million price bracket.

YIELDS ARE APPROACHING THE TOP OF THIS CYCLE

The lack of transactions has continued to hamper quantification of the current yield range. Low transaction volume has arisen due to offers not meeting the expectation of vendors but also due to failed DD periods where capital has not been able to be raised at targeted return levels.

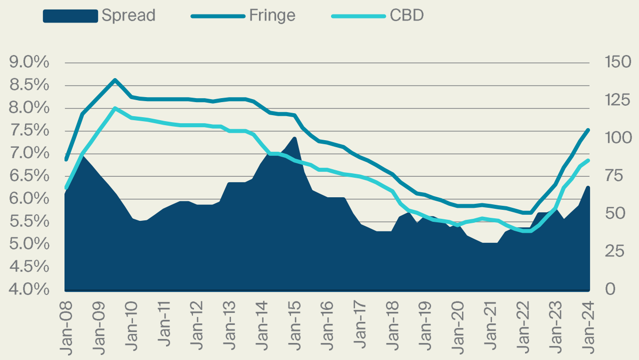
Prime yields in the Fringe market have softened by 120 bps in the past year and 185 bps during this cycle overall, currently ranging 6.8% - 8.25%. The median prime yield of 7.55% is expected to be approaching the peak for this cycle, however greater transaction volume and money market stability are needed for this to be confirmed. The newest, prime assets have held tighter than those exposed to leasing risk as the yield band widens. Secondary yields are 128bps softer in the past 12 months to a range of 8.30% - 9.50%.

Brisbane CBD & Fringe Office Sales
$ billion volume for sales $10m+



Source: Knight Frank Research, RCA

Brisbane Fringe v CBD Prime office yields
median yields (LHS), bps gap (RHS)



Source: Knight Frank Research

Recent significant sales

Property	Price $ m	Core Market Yield %	NLA sqm	$/sqm NLA	WALE	Purchaser	Vendor	Sale Date
55 Russell St, South Brisbane	38.6	5.14	4,081	9,458	1.75	Private Investor	Barwon Investment Partners	Jan 24
518 Brunswick St, Fortitude Valley^	11.9	VP	2,582	4,609	VP	State Government	Local Developer	Dec 23
520 Wickham St, Fortitude Valley	107.3	6.48	14,588	7,355	2.3	Savills IM	M&G Real Estate	Feb 23

Source: Knight Frank Research ^ purchased with vacant possession with conversion from office use likely

We like questions, if you've got one about our research, or would like some property advice, we would love to hear from you.

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Recent Research

Sydney CBD Office Market February 2024

Queensland Population Grwoth February 2024

Australian Industrial Review Q1 2024

Brisbane's Accelerated Development

Australian Horizon Report 2024

The Wealth Report 2024