RESEARCH

BRISBANE INDUSTRIAL

MARKET OVERVIEW MAY 2015

HIGHLIGHTS

Occupier demand has remained strongest at the large end of the market with the competitive rents available for pre-commitments having a deflationary effect on rents in the wider market.

The level of industrial supply was up by 9.1% in 2014, and 2015 appears to be heading for similar levels. Owner occupier and pre-commitment construction has been stronger than speculative.

Investment demand has strengthened with falls in both prime and secondary yields. WALE appears the most important driver of pricing with the low yields supported by the cost of funds.

KEY FINDINGS

Supply increased by 9.1% in 2014 responding to good pre-commitment levels, owner occupier construction and some speculative activity

Vacant space has increased to 680,151m² a new record level for the market

Market rents for existing assets are under pressure with the current secondary rents falling to 2006 levels

Investor demand has built, firming yields across both prime and secondary; there is a premium paid to mitigate leasing risk through a long WALE

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INDUSTRIAL OVERVIEW

Occupier demand remains concentrated at the larger end, with users being seduced by the competitive pre-commitment rents on offer; supported by the tight yield environment. Secondary stock faces challenges.

The Brisbane industrial market has increasingly resembled the office market, with relatively modest occupier demand in contrast to the high investor demand. New supply has increased, largely as a factor of strong pre-commitment along with some speculative activity, so backfill space has contributed to an increase in the level of vacancy across the industrial market. This, and the competitive rents being offered for pre-commitments, has resulted in market rents being stagnant or decreasing along with incentives growing. In contrast, the investment market has strengthened with demand building and 2014 recording the highest total sales volumes since 2007.

Vacancy Snapshot

Total vacancy in the Brisbane industrial market increased during the first quarter of 2015 to record 680,151m² of available industrial space (over 3,000m²). This was 73% above the long term average and represented a record high for the series, which has been in place since 2007. Part of this increase can be attributed to the level of construction within the market as there has been 701,200m² of new stock supplied to the market since 2013 and over the same period the total vacancy has increased by 350,000m², indicating good absorption of the backfill space.

Available space remains dominated by existing buildings (93%) with 6% coming from completed speculative buildings and a further 1% (6,300m²) in speculative development which is currently under construction. The level of prime space available has climbed steadily over the past three years and is currently higher than the secondary space (Figure 1). Going forward this is expected to encourage upgrading from tenants given the increasing prevalence of incentives and soft rents, encouraging mobility.

FIGURE 1
Brisbane Industrial Vacancy
'000m² prime versus secondary available space

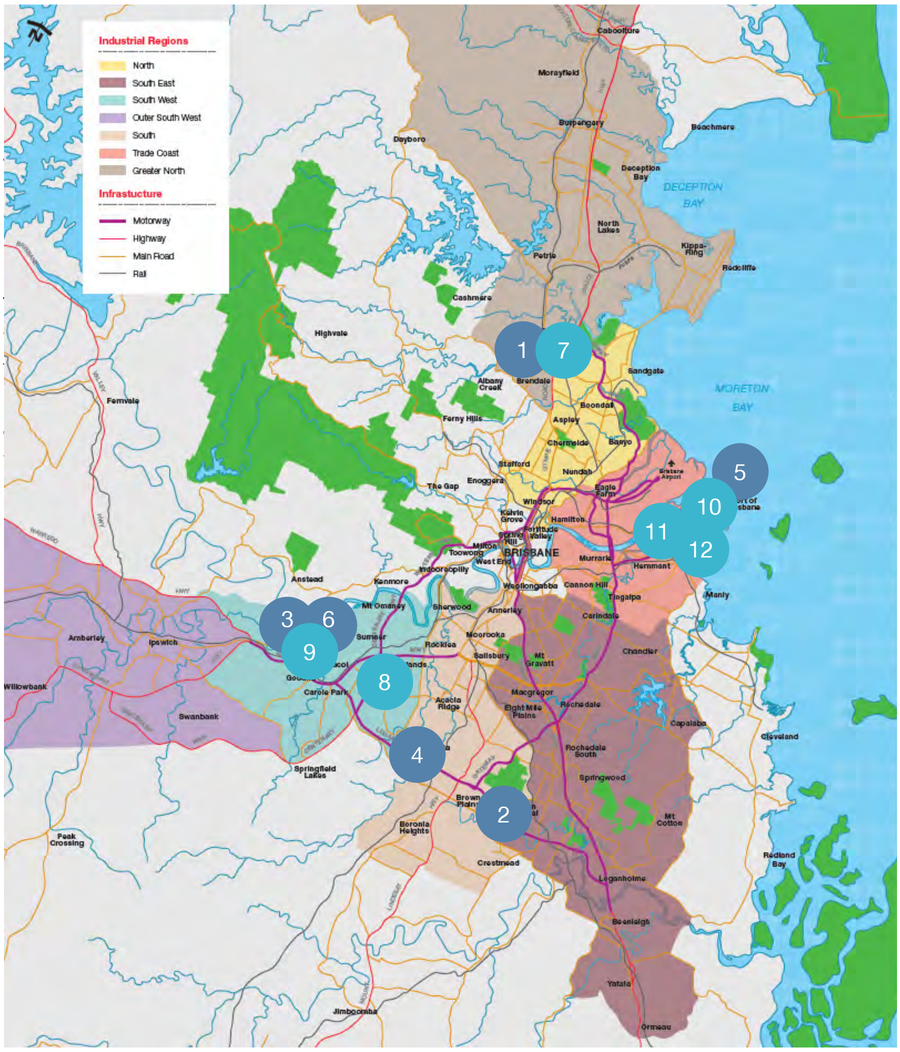
Source: Knight Frank

TABLE 1
Brisbane Industrial Market Indicators as at April 2015

Precinct	Avg Prime Rent		Avg Secondary Rent		Core Market Yields (%)		Avg Land Values <5,000m²		Avg Land Values 1—5 ha	
	$/m² net	(%p.a)	$/m² net	(%p.a)	Prime	Secondary	$/m²	(%p.a)	$/m²	(%p.a)
Trade Coast	116	-	95	3.3	7.25-8.00	8.00-8.75	335	1.5	275	-
North	107	-0.9	83	-2.4	7.35-8.00	7.75-8.50	325	4.8	250	6.4
South East	105	-1.9	83	-2.4	7.75-8.25	8.75-9.50	238	1.3	185	6.9
South	110	-	85	-3.4	7.30-8.00	8.15-9.15	275	-1.8	230	-6.1
South West	105	-0.9	85	-3.4	7.30-8.00	8.10-9.10	260	-3.7	220	-2.2
Brisbane Average	**109**	**-0.7**	**86**	**-1.6**	**7.40—8.05**	**8.15-9.00**	**287**	**0.6**	**232**	**0.6**

Source: Knight Frank NB Average market yields are based on an assumed WALE of 5-7 years for prime assets and 3-5 years for secondary

INDUSTRIAL PRECINCTS



2014 Major Completions

1. 93 Stanley St, Brendale—50,300m²
W H Soul Pattinson on-sold to KWAP
Pre-com *Super Retail Group*

2. 495 Wembley Rd, Berrinba—43,663m²
Toll vendor leaseback sold to GPT
Toll NQX

3. Robert Smith St, Redbank—31,400m²
Goodman Group
Pre-com *DB Schenker*

4. 20 Distribution St, Larapinta—23,550m²
Mainfreight
Owner Occupier

5. Bishop Dr, Fisherman Islands—15,500m²
IPS Logistics Owner Occupier

6. 62 Monash Rd, Redbank—14,800m²
Goodman Group
Speculative

2015 Major Supply

7. 68 Kremzow Rd, Brendale—55,881m²
ALDI
Owner Occupier

8. 301 Orchard Rd, Richlands—35,070m²
DEXUS Wholesale Property Fund
Speculative—*Target*

9. 100 Monash Rd, Redbank—27,775m²
Goodman Group
Pre-com *TNT Express*

10. Curlew St, Fisherman Islands—26,500m² Altis Property Partners
Pre-com *ACFS*

11. 37 Freight St, Lytton Bld 2—19,900m²
Goodman Group
Pre-com *Silk Logistics*

12. 37 Freight St, Lytton Bld 1—19,871m²
Goodman Group Speculative
Silk Logistics/Yusen Logistics

Tenants in Italics

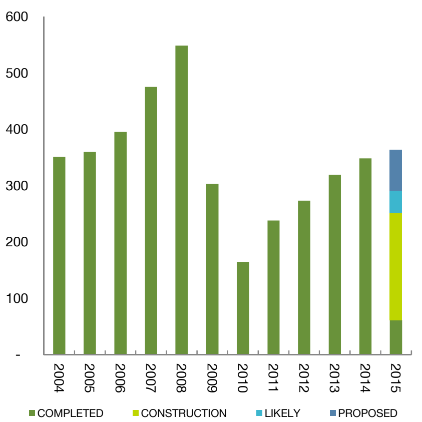
MAJOR INDUSTRIAL SUPPLY

Supply in the Brisbane industrial market has continued to increase with completed construction (3,000m²+) growing by 9.1% in 2014 to total 348,547m².

In 2014, 47% of completions came from owner occupier construction which was boosted by the 43,663m² Toll NQX building, constructed by the occupier before being sold to GPT on a long term leaseback. Other major owner occupier construction included Mainfreight's 23,550m² facility at Larapinta and IPS Logistics constructing 15,500m² at the Port of Brisbane. Underpinned by the 55,881m² ALDI warehouse at Brendale, owner occupier construction is currently expected to account for circa 40% of total construction during 2015.

Total supply in 2015 is expected to record a further increase to the construction levels, dependent on how many of the "Proposed" projects proceed to completion during the year. Pre-committed construction is currently expected to account for just under a quarter of the total construction (as opposed to 35% in 2014) . Speculative completions may account for up to 38% of construction completions during 2015, higher than the 18% speculative development accounted for in 2014. However at this time a number of speculative projects are waiting for improved tenant demand before commencing and that proportion is likely to decrease.

FIGURE 2
Brisbane Region Supply
'000 m² new industrial construction

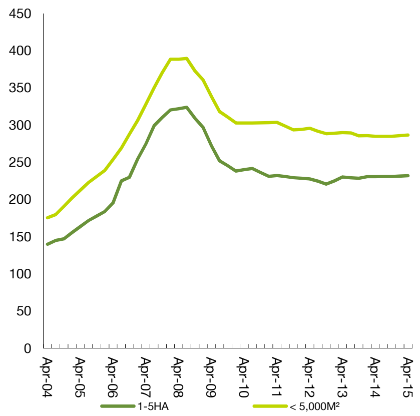


Source: Knight Frank/Cordell Connect

DEVELOPMENT & LAND VALUES

Activity in the land and development market has increased as the level of supply and construction has steadily grown over the past two years. With a number of long established estates having few development lots remaining, attention has been spreading to infill sites and also new broadhectare opportunities. The increase in larger tenant commitments has also fuelled the desire for major investors and developers to obtain control of large development sites.

FIGURE 3
Brisbane Average Land Values
$/m² land by size



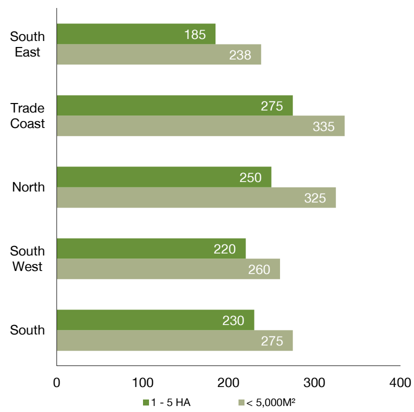
Source: Knight Frank

Transactions across the industrial land market have recently shown a divergence in pricing activity with the North and Trade Coast regions generally showing a steady level of growth due to limited stock in prime locations. In contrast, the South and South West have seen prices falling by between 1.8% and 6.1% over the past year, as the future pipeline of industrial development land looks far more robust. The South East market has begun to rebound (up 1.3%) from its low point, experienced in 2013. Despite the different conditions being experienced by the various precincts, the overall Brisbane market has seen very little change to the value of industrial land over the year, growing by 0.6%.

D&C Activity

The increase in D&C demand, particularly by larger users, has been instrumental in re-igniting activity in the industrial land market. Development demand has been a factor of both major investors with land banks creating their own investments and the desire of occupiers to upgrade their accommodation, seeking cost efficiencies. This has been facilitated by the falling yields and demand for long WALE investments, which has improved the feasibility of projects and enabled the rents to be pitched at extremely attractive levels.

FIGURE 4
Brisbane Region Land Values
$/m² of land



Source: Knight Frank

Estates with current or imminent capacity above 20ha includes Redbank Motorway Estate (42ha), Metroplex Wacol (up to 90ha), Citiswich (34ha) and Connect West (45ha) in the South West; Transition Archerfield (24ha) and 408 Stapylton Rd (32ha) in the South; Rochedale Motorway Estate (40ha), Yatala Central (25ha), Empire Industrial Estate (34ha) and 77 Darlington Drive (20ha) in the South East plus Trade Coast Central (20ha), PortWest (60ha) and Anton Rd (20ha) in the Trade Coast.

TABLE 2
Recent Land/Development Sales Activity Brisbane

Address	Region	Price $ mil	Area m²	$/m² of site area	Zoning	Vendor	Purchaser	Sale Date
21 Radius Dr, Larapinta	S	2.50	15,300	163	GI	Radius Industrial	Pooma Pty Ltd	Apr 15
506 Lytton Rd, Morningside	TC	22.10	274,900	80	PD	Exxon Mobil	Private Investor	Feb 15
55 Harris Rd, Pinkenba	TC	12.50	84,700	148	GI	Australand	United Terminals Qld	Jan 15
Lot 1, Anton Rd, Hemmant	TC	26.00	122,000	213	GI	Marine Holdings	DEXUS Property Group/ Future Fund	Nov 14
Mica St, Carole Park	SW	5.25	97,000	54	RBI	Qld Govt	Unison Projects	Oct 14
86 Depot St, Banyo	N	3.15	8,466	373	GI	Private Investor	Owner Occupier	Oct 14
67 Logistics Pl, Larapinta	S	2.40	15,850	151	GI	Private Investor	Brazil Enterprises	Oct 14
Weedman St, Redbank	SW	74.13	874,000	85	-	Aurizon	Goodman Trust Aust	Sep 14
237 Gooderham Rd, Willawong	SW	11.99	154,200	78	Rural	Private Investor	Charter Hall Core Plus Fund	Sep 14

Source: Knight Frank S South TC Trade Coast SW South West N North GI General Industry PD Particular Development RBI Regional Business & Industry

OCCUPIER DEMAND & RENTS

Occupier demand has remained patchy through the first few months of 2015 with a month of strong enquiry frequently followed by a quieter period. Larger tenants have continued to be active with the search for cost efficiencies and upgrading of accommodation and technologies continuing to fire D&C demand. Warehouse users both 3rd party logistics and major retailers/distributors have remained at the forefront of tenants seeking to obtain new premises.

At this stage the number of occupiers actively pursuing a D&C programme is lower than has been seen in recent years with Mitre10 and Schweppes among the larger tenants currently seeking space.

The preference for new accommodation, which can be delivered at highly competitive rental levels while industrial yields are low, is continuing to have an impact on existing accommodation and as outlined above vacancy levels have continued to increase. This has placed pressure on market rents, which have largely been stagnant or softening over the past two years. Over the past 12 months prime rents have fallen by 0.7% while secondary rents have softened by 1.6%. This trend is expected to continue as the available existing space remains high, with further discounting expected over the coming 18 months.

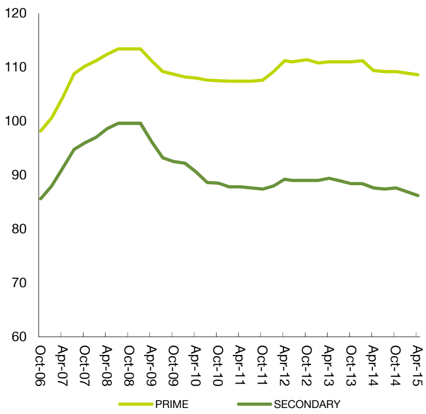
Prime rents have remained relatively stable with the precincts recording either flat or slightly negative movement over the past year. Trade Coast, at an average of \$116/m² net, remains the most expensive region, ahead of the South at \$110/m² net. The remaining three precincts record a tight range of \$105—\$107/m² net.

There has, however, been greater divergence in results between the precincts for secondary rents. While the Trade Coast recorded an annual increase of 3.3% in secondary rent to \$95/m² all other precincts saw falls. The North (-2.4%) and South East (-2.4%) recorded modest falls over the past year, however reflective of the level of available stock, the South and South West saw secondary rents fall by 3.4% to \$85/m².

FIGURE 5

Brisbane Region Rents

\$/m² net rent prime v secondary



Source: Knight Frank

With prime rents having been largely stable since 2010, tenants coming to the end of leases with fixed reviews are now frequently seeing their passing rent in excess of market rental levels. While this has fuelled much of the D&C demand, it is also expected to contribute to a higher level of tenant mobility in the coming year. Tenants are expected to explore the options of alternative locations and also potentially upgrade their space for little to no increased cost compared with their current expenditure.

This will place increasing pressure on landlords to refurbish and update their assets to avoid competing for tenants on a price basis only. Secondary rentals in particular are expected to see material softening over the next 12 months.

At the same time that rents have been stable or softening there has been a steady increase in the level of incentives in the market. Across the Brisbane market, prime incentives currently average 9.15%, up from 7.85% a year ago. Secondary incentives are similar and in most regions average 9-10%, with the South potentially up to 12% given the greater levels of vacant secondary product.

TABLE 3

Recent Leasing Activity Brisbane

Address	Region	Net Rent \$/m²	Area	Term (yrs)	Tenant	Date
Peachey Rd, Yatala	SE	133+	10,800	15	Cope Sensitive Freight^	Sept 15
237 Gooderham Rd, Willawong	SW	c28-30	113,163*	25	Prixcar^	Jul 15
Curlew St, Port of Brisbane	TC	Undis	27,210	20	ACFS^	Jul 15
56 Main Beach Rd, Pinkenba	TC	Undis	8,000	10	CEVA^	May 15
1B 37 Freight St, Lytton	TC	118	10,821	10	Silk Logistics#	May 15
11 Inghams Pl, Hemmant	TC	98	8,591	8	Burson Auto Parts	Feb 15
180 Holt St, Pinkenba	TC	152+	8,136	14	AP Eagers	Feb 15
51-57 Qantas Dr, Eagle Farm	TC	100	22,912	15	Repco	Dec 14
103 Bancroft St, Pinkenba	TC	116	7,304	7	E.D Oates	Nov 14
1 Lahrs Rd, Ormeau	SE	210	9,600	12	Markwell Foods‡	Nov 14
42 Randle Rd, Pinkenba	TC	130	7,000	6	Easy Roll^	Nov 14

Source: Knight Frank SE South East SW South West TC Trade Coast ^pre-commitment #Spec
*total hardstand (covered and uncovered) NLA of bld is 4,587m² ‡Purpose build cold storage and food prep
+large hardstand component

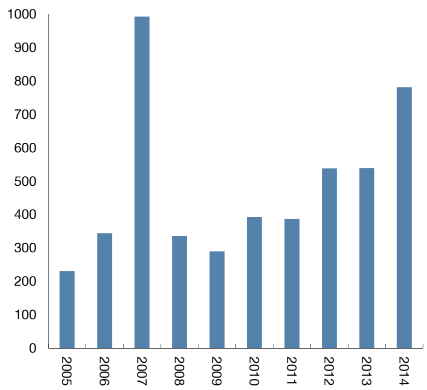
INVESTMENT ACTIVITY & YIELDS

Investment activity across the industrial market has been building over the past 18 months, however the increasing investor demand has been tempered by a lack of assets on the market. The calendar year of 2014 recorded $781.9 million in total transactions (over $5million) which is a 45% increase over the 2013 transaction total.

FIGURE 6

Brisbane Industrial Transactions

$million sales $5million+



Source: Knight Frank

Core investors, both local and offshore, have increased their focus on industrial sector, however have remained selective, seeking both core assets and economies of scale in their investments.

Portfolio investments, particularly where a long term sale and leaseback is involved, have also been popular with recent examples including The Ingham portfolio, McPhee Transport and Pentair. At a major investor level, portfolios have also been offered by Altis Property Partners, Abacus Property Group and GIC Logos, drawn to the market by the low yields on offer.

Purchasing activity within the Brisbane market over the year to May 2015 has been relatively evenly spread across Unlisted Funds (30%), AREITs (29%) and also private investors (20%). Offshore investors accounted for 15% of transaction activity.

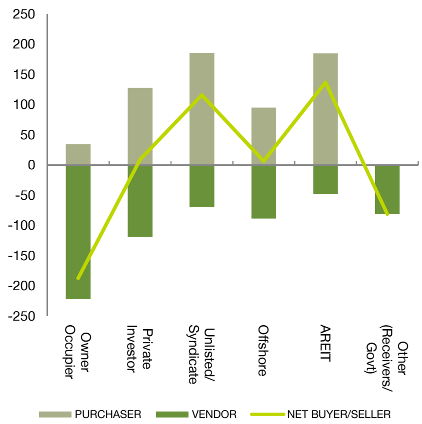
Vendor activity has been dominated by owner occupiers as companies are taking advantage of market conditions to release capital for their business. This owner occupier vendor activity ranged from long term leasebacks (ie Greens Foods $23.9 million, BJ Ball $18.65 million, and Trend Doors $8.5 million) through to divestment of development sites or land rich operations (Hills Industries $15.6 million, Aurizon $74.13 million or Nth Qld Heavy Haulage $9.15m). Private Investors were also strong sellers over the past year, particularly of secondary assets where yield compression was in place.

> “Owner occupiers have been strong net sellers, taking advantage of the investment demand”

FIGURE 7

Brisbane Vendor/Purchaser

$million sales $5million+ 12 mths to May 2015



Source: Knight Frank

TABLE 4

Recent Improved Sales Activity Brisbane

Address	Region	Price $ mil	Bldg Area m²	Core Mkt Yield (%)	WALE (yrs)	Vendor	Purchaser	Sale Date
93 Burnside Rd, Stapylton	SE	17.45	14,491	8.37	2.9	Private Investor	Ringmer Pacific	Apr 15
51 Musgrave Rd, Coopers Plains#	SW	10.70	9,456	7.92	1.5	McPhee Developments	Cache Logistics Trust	Jan 15
112 Cullen Ave, Eagle Farm	TC	20.70	12,005	7.85	4.8	City of Brisbane Investment Corp	DEXUS Wholesale Property Trust	Dec 14
7-9 French Ave, Brendale#	N	18.65	12,282	7.33	7.2	BJ Ball Ltd	AMP Capital Wholesale Industrial Fund	Nov 14
30 Enterprise St, Cleveland#	SE	18.65	8,942	n/a^	20	Inghams Enterprises	Charter Hall DIF No 2	Nov 14
1510 Lytton Rd, Hemmant#	TC	12.40	n/a^	n/a^	20	Inghams Enterprises	Charter Hall Core Plus Industrial Fund	Nov 14
69 Rivergate Place, Murarrie	TC	27.00	11,558	7.47	8.6	Trinity Funds Management	360 Capital Industrial Fund	Nov 14
136 Zillmere Rd, Boondall	N	25.00	15,619	7.85	8.8	Pellicano Group	360 Capital Industrial Fund	Nov 14

Source: Knight Frank SE South East SW South West TC Trade Coast N North # vendor leaseback ^ part of a vendor leaseback portfolio sale with limited details

Yields

The increasing investor demand across the industrial market has seen the further dip in the cost of funds in Q1 2015 spur competition between purchasers to a point where yields have firmed significantly over the past six months. Average prime yields, for properties with a WALE of 5-7 years, is currently 7.72% across a range of 7.40% - 8.05%. This represents firming of 45 basis points over the past six months and 95 basis points in the current firming cycle. Given the relatively soft current occupier demand fundamentals some investors have appeared to be pricing longer WALE periods ahead of the underlying building and tenant quality.

Median yields for secondary assets have also tightened over the past six months with the current average of 8.58% reflecting a range of 8.15% - 9.00%. As investors have continued to chase higher yields, the secondary market has seen increasing purchasing activity by both listed an unlisted entities. Reflecting the premium being paid to bypass short term leasing risk, secondary assets which have sold with longer WALES (in excess of 7 years) have achieved prices on yields tighter than the market average.

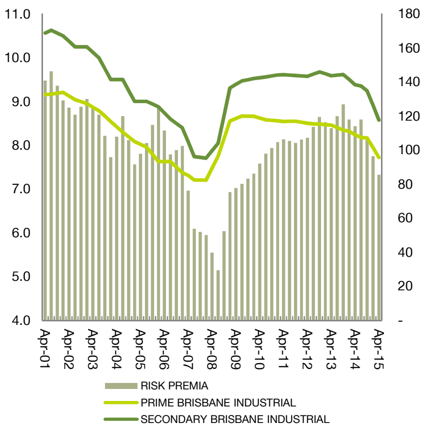
The recent increase in long term bonds, up 65 basis points from the lowpoint of 2.28% recorded in mid-April, has flagged that a floor may be forming under yields in the medium term. However the recent increase has seen the long term Commonwealth bonds return to levels which were in evidence during late 2014 and further increases would be required to reverse the tightening trend for yields.

As investors recognise the leasing risk which is inherent across existing buildings at the moment, the premium which is being paid for a long WALE may extend beyond the current levels. This has the potential to create divergent fortunes within the market for properties with relatively similar physical and locational characteristics. While at the moment the quest for yield has seen a number of purchasers taking on leasing risk for a higher return, this remains in the minority with the strongest demand for long WALE assets.

FIGURE 8

Brisbane Region Yields

% Core market yield (LHS) & bps Premia (RHS)



Source: Knight Frank

"Some purchasers appear to be buying WALE primarily, and looking at the tenant and building quality as a secondary consideration"

Outlook

- Occupier demand for smaller and medium sized users is expected to remain patchy in the short term, aligned with business confidence and profitability. Larger corporates will continue their search for greater efficiencies and cost savings through relocation and upgrading of premises where-ever available.
- Prime rents are expected to maintain their softening bias under competition from D&C and speculative development. Incentives will continue to play a larger part in negotiations and may be seen more commonly in excess of 10%.
- Secondary rents are currently at the lowest levels since 2006 and further falls are likely. This is expected to trigger some recycling and change of use in obsolete stock.
- There remains a healthy pipeline of speculative development, however early 2015 has seen the deferment of some construction starts, seeking greater indication of tenant demand.
- The increase in major tenant commitments, over 30,000m², has re-ignited activity in the land market with institutional investors moving to secure medium or longer term land banks. This will continue, however the growing pipeline of future land supply is expected to maintain pressure on values in current estates.
- Investment demand is expected to maintain its current high levels as both core and value-add investors look to the industrial market for greater income returns.
- Yields have tightened significantly over the past six months and this bias will be maintained, particularly for longer WALEs. The recent increase in the long term bond rate indicates that this trend will not continue indefinitely.

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Definitions:
Core Market Yield: The percentage return/yield analysed when the assessed fully leased net market income is divided by the adopted value/price which has been adjusted to account for property specific issues (i.e. rental reversions, rental downtime for imminent expiries, capital expenditure, current vacancies, incentives, etc).
Prime Grade: Asset with modern design, good condition & utility with an office component 10-30%. Located in an established industrial precinct with good access.
Secondary Grade: Asset with an older design, in reasonable/poor condition, inferior to prime stock, with an office component between 10-20%.
WALE: Weighted Average Lease Expiry
Vacancy Methodology:
This analysis collects and tabulates data detailing vacancies (3,000m²+) within industrial properties across all of the Brisbane Industrial Property Market. The buildings are categorised into 1) Existing Buildings – existing buildings for lease. 2) Speculative Buildings – buildings for lease which have been speculatively constructed and although have reached practical completion, still remain vacant. 3) Spec. Under Construction – buildings for lease which are being speculatively constructed and will be available for occupation within 12 months.

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