RESEARCH

BRISBANE

INDUSTRIAL MARKET BRIEF NOVEMBER 2015

Occupier demand has remained stable in 2015 with existing properties having to compete on price against D&C options which are being subsidised by the low yield environment for modern, long-WALE assets.

Key Facts

Retailers and logistics providers still dominate larger scale demand; construction firms are showing increasing demand

D&C rents are at particularly low levels for large users; supported by low yields and stable land prices

Market face rents fell by 4.6% and 2.5% respectively for prime and secondary properties

Investment demand remains high; average prime yields fell 72 bps over the past year but are now expected to stablilise

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Occupier Demand & Rents

Occupier demand has remained stable over the year to October 2015 with take-up of vacant industrial space (excluding D&C) up by 3% over the previous 12 months. Demand is coming from a wide spread of industrial users with retailers, logistics and increasingly companies involved in construction & building materials, providing the bulk of enquiry and significant relocations.

The relatively high vacancy and only stable demand has resulted in market rents softening to the point which has begun to engender higher activity levels. Across the Brisbane market the prime net rental average is $104/m² which reflects a fall over the past 12 months of 4.6%. At the same time incentives have stepped up, now ranging from 10% - 12%, which has resulted in a fall to the prime net effective rent of 8.2% over the past year.

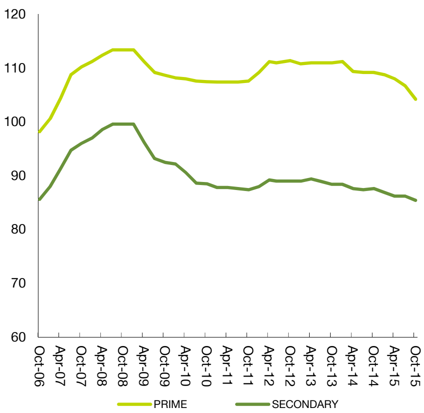
Rents for D&C projects have also continued to trend lower, particularly for larger sized facilities. The current premium in the market for investments of a large scale, driven by off-shore investor demand, has driven the yields for these super prime-assets to cyclical low levels; which enables these projects to be offered at particularly low rental levels compared with existing assets. D&C rents for small to medium tenants (sub15,000m²) are also still highly competitive, but not to the same extent as larger assets where there have been reported rents in the $75—85/m² range on a net effective basis. Major tenants seeking new accommodation, taking advantage of the deals on offer include Schweppes and Mitre10, plus other consumer goods and construction/building industry users.

Leasing activity in the secondary market has increased slightly over the course of 2015 as tenants have sought to curtail their occupancy costs. Average secondary rents have continued to drift, falling by 2.5% to $85/m² net as at October 2015.

FIGURE 1

Brisbane Region Rents

$/m² net rent prime v secondary



Source: Knight Frank Research

Development Activity

Construction and development activity in 2015 is expected to be at levels slightly below the 2014 figures. At the time of writing there had been 287,077m² of industrial space (over 3,000m²) completed during 2015 with a further 13,528m² in the final stages of construction. This is a 13.8% decrease on the 2014 result, which was a five year high.

Looking forward into 2016, with space already under construction of 108,725m², supply levels are expected to remain at similar levels to 2014 and 2015. There are a number of proposed speculative developments which, if commenced, could provide a boost to the supply total for 2016.

Completed new supply during 2015 has been dominated by larger facilities such as ALDI 55,881m², Target (spec) 35,070m², TNT 27,775m², ACFS 27,210m² and the Yusen/Silk Logistics facilities (39,900m² combined). These five largest builds accounted for some 62% of the supply (over 3,000m²) in 2015, indicating a continued lack of smaller to medium developments.

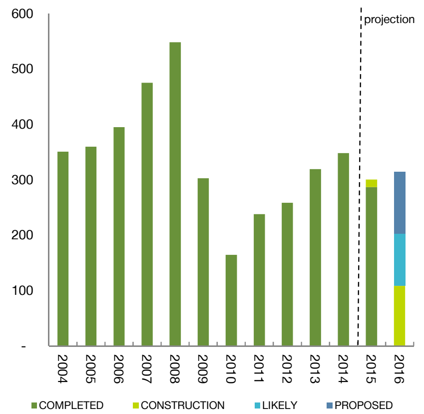
Significant projects under construction for delivery in 2016 include the 48,500m² reconstruction of the G James Glass facility at Eagle Farm, a 22,980m² speculative development by DEXUS at Larapinta and a 13,164m² warehouse committed by Beaumont Tiles at Rochedale. In addition, the 30,400m² building committed by O-I glass in Yatala will commence construction in Q1 2016.

As the development pipeline has recovered over the past four years the overhang of development land has been eroded. With a greater than ever concentration of large englobo sites within the hands of institutional owners to undertake their own developments, the supply of development sites for purchase has reduced over the past 18 months. There has been some price appreciation across smaller lots (<5,000m²), led by TradeCoast, North and South East markets, while the South and South West have lower or stable prices with few prime lots available and a large bank of existing properties for lease. Significant englobo transactions have occurred in the South precinct with GPT acquiring 21ha at Berrinba and Logos purchasing 24.5ha at Heathwood for a reported $50 million.

FIGURE 2

Brisbane Region Supply

'000m² new industrial construction



Source: Knight Frank Research/Cordell Connect

Sales & Investment Activity

Investment demand has remained high over 2015 with both local and offshore investors seeking to increase their exposure to the Brisbane industrial market. Prime assets with long WALEs or portfolios of assets to achieve scale, remain the most sought after.

The average prime yield is 7.45% (range of 7.15%- 7.75%) across the Brisbane regions, representing a tightening of 72 basis points (bps) over the past year and 120bps over the cycle. The average yield data series analyses assets with a 5-7 year WALE and sub-20,000m² in size; brand new assets with longer WALEs and greater scale are likely to achieve yields in the range of 6.50%—7.00%, although there have been no recent single-asset transactions to confirm this.

TABLE 1

Brisbane Industrial Market Indicators as at October 2015

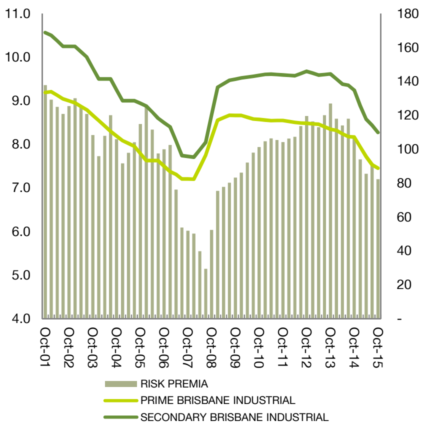
Precinct	Avg Prime Rent		Avg Secondary Rent		Core Market Yields (%)		Avg Land Values <5,000m²		Avg Land Values 1—5 ha	
	$/m² net	(%p.a)	$/m² net	(%p.a)	Prime	Secondary	$/m²	(%p.a)	$/m²	(%p.a)
Trade Coast	110	-5.2	93	-3.1	7.00—7.75	7.75—8.75	345	3.0	275	-
North	104	-4.6	83	-2.4	7.20—7.75	7.75—8.75	345	4.5	240	2.1
South East	102	-2.9	82	-3.5	7.25—7.75	7.75—9.00	240	2.1	187	6.9
South	105	-4.5	85	-1.2	7.12—7.75	7.75—8.75	270	-1.8	230	-2.1
South West	100	-5.7	84	-2.3	7.20—7.75	7.75—8.75	265	-1.9	220	-2.2
Brisbane Average	**104**	**-4.6**	**85**	**-2.5**	**7.15—7.75**	**7.75—8.80**	**293**	**1.4**	**230**	**0.6**

Source: Knight Frank Research

FIGURE 3

Brisbane Region Yields

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



Source: Knight Frank Research

TABLE 2

Recent Leasing Activity Brisbane

Address	Region	Net Rent $/m²	Area	Term (yrs)	Tenant	Date
Peachey Rd, Yatala	SE	Undis	30,400	5	Owens-Illinois^	Jun 16
2637 Ipswich Rd, Darra	SW	200	12,000	20	Wild Breads^	Jun 16
100 Postle St, Acacia Ridge	S	Undis	11,165	12	Lindsay Australia^	Jun 16
35 Evans Rd, Salisbury	S	Undis	12,000	undis	Couriers Please	Oct 15
13-23 Badu Ct, Crestmead	S	100	4,536	1	Owens-Illinois	Aug 15
19 Distribution St, Larapinta	S	100	4,119	5	Medline	Jul 15
28 Flint St, Richlands	SW	100	5,000	n/a	Britz'n Pieces#	Jul 15
55 Musgrave Rd, Coopers Plains	S	95	9,600	5	Curtain Wonderland	May 15

Source: Knight Frank SE South East SW South West S South ^pre-commitment #Sub-lease

The $1.07 billion portfolio sale between GIC/Frasers Property and Ascendas included seven Brisbane industrial assets, covering a total of 156,000m² of building area, and was the most significant transaction of 2015. Across the total Australian portfolio of 26 assets (630,000m²) the investment had a WALE of 5.7 years and represented a reported initial yield of 6.4%.

The sustained low-growth rental market has resulted in assets becoming over-rented within a few years of lease start and the passing and core market yields are increasingly divergent because of this, skewing analysis. Examples have included 203 Viking Drive, Wacol which had a 7% passing yield in comparison to the core market yield of 5.88% and 85 Radius Dr, Laraptina where the passing yield of 7.8% was well in excess of the core market yield of 6.7%. Both of these assets had relatively long WALEs of 7.9 and 6.6 years respectively and the offshore purchasers appeared comfortable to place greater weight on the passing income and review mechanisms than the market rent. This underscores the weight the market is currently placing on longer WALEs.

TABLE 3

Recent Land/Development Sales Activity Brisbane

Address	Region	Price $ mil	Area m²	$/m² of site area	Zoning	Vendor	Purchaser	Sale Date
115 Corymbia Pl, Parkinson	S	1.63	7,967	205	GI	HM Australia Holdings	Torluccio Investments	Sep 15
Wembley Rd, Berrinba	S	23.20	210,000	110	n/a	Logan City Council	GPT Group	Jul 15
173 Pine Rd, Richlands	SW	1.52	12,880	118	II	QLD Government	Strainer Post Aust	Jun 15
462 Boundary Rd, Richlands	SW	1.36	19,580	70	GI	Private Investor	VTS Cranes	Jul 15
88 Pearson Rd, Yatala	SE	1.25	27,600	45	GIBI	Energex	Owner Occupier	Apr 15

Recent Improved Sales Activity Brisbane

Address	Region	Price $ mil	Bldg Area m²	Core Mkt Yield (%)	WALE (yrs)	Vendor	Purchaser	Sale Date
203 Viking Dr, Darra	SW	27.00	13,363	5.88~	7.9	One Investment Group	Cache Logistics Trust	Oct 15
39 Silica St, Carole Park	SW	20.00	14,210	9.93^	0.5	Crescent Capital#	Fife Capital	Oct 15
29-41 Lysaght St, Acacia Ridge	S	21.57	18,488	8.28	2.8	DEXUS Wholesale Property Fund	Wholesale Australian Property Fund (AMP)	Sep 15
92-116 Holt St, Pinkenba	TC	16.40	14,494	8.50	2.7	GPT Funds Mgt 2	Private Investor	Jul 15
85 Radius Dr, Larapinta	S	18.15	10,081	6.70~	6.6	Private Investor	Investec Australia Property Fund	Jul 15
285 Lavarack Ave, Eagle Farm	TC	14.50	13,371	8.23	1.0	OneSteel#	Private Investor	Jun 15

GI General Industry GIBI General Impact Business & Industry II Industry investigation ^ passing yield # vendor leaseback ~over-rented

Source: Knight Frank Research TC Trade Coast SW South West S South SE South East

Despite the sustained investment interest, transaction activity over the year to November 2015 has totalled $536.07 million in non-portfolio sales ($5 million+), which is 38% below the corresponding period a year earlier of $865.29 million.

Purchasing activity (excluding portfolio sales) was dominated by Wholesale/ unlisted funds (33%) and private investors (30%). Private Investors have been particularly active in the $5—15 million price bracket as they seek higher returns. AREITs accounted for 17% and direct offshore investment was 10% of transactions.

Private Investors also dominated selling activity, accounting for 36% of sales, followed by owner occupiers at 27% as a result of a number of vendor leasebacks. With relatively fewer sales and an increasing view that long term funds are rising, yields are expected to show some stabilisation in the wider industrial market.

Outlook

Leasing market sluggishness and strong competition from developers for pre-commitments will continue to place downward pressure on market rents. Pre-commitment driven construction and speculative development will remain supported by the tight yield environment (particularly for large scale, long WALE assets) and steady demand from large corporate occupiers. This will support supply levels in 2016 on a par with the prior two years. This backfill space will maintain pressure on existing building rents, particularly for secondary space.

Investment demand will remain strong, however there is slightly more caution in evidence for non-prime assets with higher income returns not always drawing investors upwards on the risk curve. The limited number of large-scale, prime investments will continue to limit activity and concentrate demand on those assets.

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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