BRISBANE

INDUSTRIAL MARKET BRIEF DECEMBER 2016

Key Facts

Occupier demand remains focussed on new stock; building product tenants are growing in response to the high residential construction

Effective market rents remain under pressure (down c3.0% p.a) as **incentives** become more entrenched in the market.

Land values have continued to appreciate (up by 11.3% on <5,000m² sites) as the stock of formed sites available for sale diminishes.

Investment demand remains high; average prime yields fell 13bps over the past year but core stock availability remains limited.

JENNELLE WILSON
Senior Director—QLD Research

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Investment demand remains strong, supported by the appetite for core assets. This continues to fuel construction as tenants favour new supply, delivered at highly competitive rentals, at the expense of existing assets.

Occupier Demand & Rents

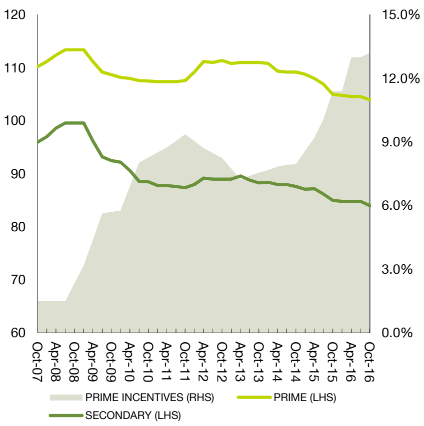
The leasing market has remained somewhat challenging over the course of 2016. While demand has been steadily building the relatively high vacancy has meant that tenants retain the upper hand. Take-up of vacant industrial space above 3,000m² (excluding D&C) was 356,789m² over the 12 months to October 2016. While this take-up level is well above the long term average (309,172m²) it is 7.6% below the take-up of the same period a year earlier.

Industrial vacancy, as measured by Knight Frank, increased by 14% in the quarter to October 2016, reversing the falls of the previous year as the market was impacted by an influx of speculative space commencing construction. With a total measured vacancy of 708,768m², speculative space (completed and under construction) accounts for 15% of the total, however it is generally quickly absorbed.

The continued drive for premises with greater efficiency has been the motivation for some of the major occupier moves, particularly in the 3PL and transport/logistics industries. The increasing residential construction across the south east Queensland region has also resulted in greater absorption of space for building products users such as G James Glass, National Glass, Beaumont Tiles, National Tiles, Franklyn Blinds and Beaulieu Carpets. Large food and beverage operators such as Scheweppes, Coca Cola Amatil and Bevchain have also committed to space.

Market rents have remained under downward pressure with slight face rent weakness compounded by the further entrenchment of incentives in the market. The average net face rents for prime and secondary space fell by 1.0% and 1.2% respectively over the past year. With incentives now averaging 12%-14% the implied reduction in the net effective market rental is –3.0% p.a for prime and –3.2% p.a for secondary.

FIGURE 1
Brisbane Region Rents & Incentives
$/m² net face rent prime v secondary



Source: Knight Frank Research

Development Activity

Construction and development activity for 2016 will be lower than recorded in the past three years with a total of 252,520m² expected to be delivered in the calendar year. To date 199,173m² of new industrial space has been completed, with a further 53,347m² in the final stages of construction. This is lower than both the 2015 (313,616m²) and 2014 (348,547m²) results with relatively fewer large scale completions.

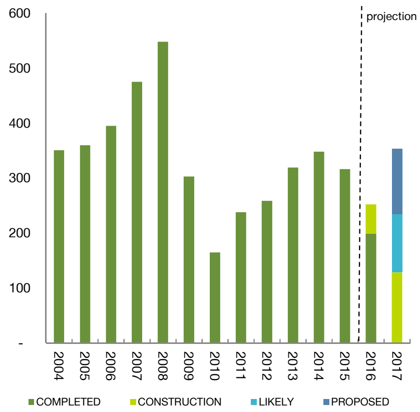
The proposed level of supply for 2017 is expected to increase, with some 128,548m² of space already under construction for completion next year. There is 106,315m² in development schemes classified as "Likely" with a further 118,840m² of completions in 2017 classified as "Proposed", however not all of these projects are expected to be completed during 2017.

Notable supply for 2016 included a speculatively developed facility at Larapinta (22,980m²), the pre-committed OI Glass Facility at Yatala (35,400m²) and a new owner-occupied facility of 29,271m² at the G James Glass factory at Eagle Farm. Overall, 42% of the new supply was for pre-committed space, reflective of the high activity and competition in that space. Speculative development accounted for 30% of supply with owner-occupiers not far behind at 27%.

Significant projects that will be delivered in 2017 include the 54,000m² pre-commitment to Super AMart at Rochedale, 30,000m² of speculative space in Lytton and 35,000m² pre-committed to Bevchain in Eagle Farm. There are also a number of 18,000—20,000m² developments in the pipeline which are a mix of pre-committed and speculative space.

While the quantum of industrial space delivered to the market has been lower in 2016, land prices have continued to appreciate, particularly in infill locations. With the major institutional owner/developers controlling large land banks for asset creation they are generally reluctant to sell land. As a result the values of formed, serviced land has increased over the past year with 11.3% growth in land <5,000m² and 10.2% for larger lots of 1-5ha. This growth has been greatest in the TradeCoast precinct where available freehold land is limited.

FIGURE 2
Brisbane Region Supply
'000m² new industrial construction (3,000m²+)



Source: Knight Frank Research/Cordell Connect

Sales & Investment Activity

Investment demand has remained heightened during 2016, however a lack of suitable stock has limited total turnover levels. Total industrial turnover for 2016 ytd is $610 million and is likely to finish the year well below the $948 million recorded over the calendar year of 2015. The 2015 result was boosted by the circa $305 million Ascendas portfolio sale, so excluding the impact of that portfolio the sales turnover levels are on a par with 2015.

Yields are still on a firming trend as the weight of money seeking core assets and stabilised income streams continues to build. The average prime yield is 7.32% across a range of 6.95% - 7.65% across the Brisbane precincts, a firming of 13 basis points over the past 12 months.

TABLE 1
Brisbane Industrial Market Indicators as at October 2016

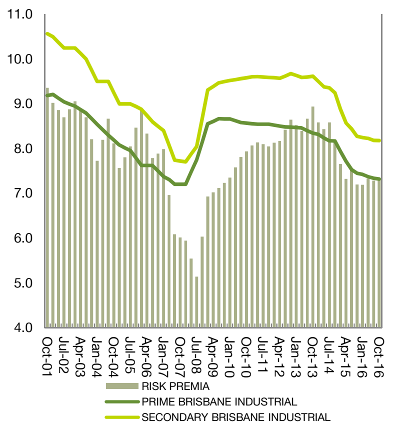
Precinct	Avg Prime Rent		Avg Secondary Rent		Core Market Yields (%)		Avg Land Values <5,000m²		Avg Land Values 1—5 ha	
	$/m² net	(%p.a)	$/m² net	(%p.a)	Prime	Secondary	$/m²	(%p.a)	$/m²	(%p.a)
TradeCoast	110	-	92	-1.1	6.95—7.60	7.60—8.70	420	21.7	330	20.0
North	103	-1.0	83	-	7.00—7.70	7.65—8.70	365	5.8	250	4.2
South East	100	-2.0	79	-1.3	7.00—7.65	7.65—8.80	255	6.3	200	7.0
South	104	-1.0	83	-2.4	6.95—7.70	7.65—8.70	300	11.1	250	8.7
South West	103	-1.0	83	-1.2	6.95—7.70	7.65—8.70	290	9.4	240	9.1
Brisbane Average	**104**	**-1.0**	**84**	**-1.2**	**6.95—7.65**	**7.65—8.72**	**326**	**11.3**	**254**	**10.2**

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
Wayne Goss Dr, Berrinba	S	105	13,150	5	National Tiles^	Jun 17
96-106 Freight St, Lytton	TC	120	6,400	5	Deliver Group#	Mar 17
Brickworks Rd, Rochedale	SE	115	8,042	10	Franklyn Blinds^	Feb 17
70 Radius Dr, Larapinta	S	105	11,032	7	Greens Foods#	Jan 17
70 Radius Dr, Larapinta	S	112	12,104	7	MJ Logistics#	Aug 16
44 Overlord Pl, Acacia Ridge	S	105	1,350	3	General Glass	Jun 16
39 Gardens Dr, Willawong	SW	100	1,400	3	World Wire Cables	Jun 16

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

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 of 8-12 years, and greater scale are likely to achieve yields in the range of 6.25%—6.75%, although there have been no recent single-asset transactions to confirm this. The largest recent sale, the $126 million purchase of 137 Magensium Dr, Crestmead reflected a 6.86% core market yield, however was part of a larger portfolio. Although sold with a long WALE of 13.6 years, the asset at 473 Newman Rd, Geebung is a specialised facility which limited the yield firming to 6.89%. With current tenant requirements in the market offering up to a 20 year lease, if such an asset was offered for sale, a sub-6% yield is to be expected.

With relatively few large core assets available for sale across the Brisbane market over the past year. purchasers seeking to gain exposure to the Brisbane market have been more likely to move up the risk curve, either by taking on leasing risk or more specialised built forms.

TABLE 3

Recent Land/Development Sales Activity Brisbane

Address	Region	Price $ mil	Area m²	$/m² of site area	Zoning	Vendor	Purchaser	Sale Date
3039 Beaudesert– Boonah Rd, Bromelton	SW	15.00	846,477	18	SDA	Korda Mentha	ARTC	Oct 16
220 Orchard Rd, Richlands	SW	7.00	20,000	350	GI	Private Investor	Coca Cola Amatil*	Aug 16
Dohles Rocks Rd, Murrumba Downs	N	3.60	28,000	129	I	Walker Corporation	Local Developer	May 16
96-106 Export St, Lytton	TC	13.60	52,350	250	GI	State Government	Goodman Group	May 16

Recent Improved Sales Activity Brisbane

Address	Region	Price $ mil	Bldg Area m²	Core Mkt Yield (%)	WALE (yrs)	Vendor	Purchaser	Sale Date
36 Fulcrum St, Richlands	SW	18.00	8,214	7.44	5.7	Private Investor	Fife Capital	Oct 16
473 Newman Rd, Geebung	N	24.54	14,331	6.89	13.6	National Glass‡	Private Investor	Sep 16
41-55 Platinum St, Crestmead	S	15.92	11,214	8.11	5.0	Private Investor	Primewest Industrial Income Trust 2	Jul 16
67 Bellrick St, Acacia Ridge	S	18.00	14,639	7.46	8.6	Heathley Diversified Property Fund	Trilogy Funds Mgt	Jun 16
111-137 Magnesium Dr, Crestmead~	S	126.00	89,254	6.86	6.0	Goodman Group	Blackstone	Jun 16
17 Sugarmill Rd, Pinkenba	TC	28.25	14,244	6.93	5.3	Charter Hall Core Plus Industrial Fund	Propertylink Aust Industrial Partnership	May 16

SDA Special Development Area GI General Industry I Industry * Adjoining owner ‡ vendor leaseback ~part of a portfolio sale

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

Purchasing activity during 2016 to date has been dominated by Unlisted Funds which have accounted for 49% of transactions by value with Fife Capital and Propertylink Australia Industrial Partnership active buyers along with a number of syndicators. Offshore investors, dominated by Blackstone, accounted for a further 33% of total transactions. Private Investors have remained an active segment in the market with 17% of transactions, dominating the $5-10 million price bracket.

Secondary yields have also shown continued firming, with the median 8.18% down by a further 10bps over the past 12 months, across a range of 7.65% - 8.72%. With secondary vacancy remaining stubbornly high there is a wide value range for secondary assets, depending on leasing risk. Owner-occupiers are expected to increase their purchasing activity of existing assets, particularly as land values appreciate and as vacant assets remain available.

Outlook

The larger tenants in the market have continued to show a clear preference for newly constructed accommodation both for increased efficiencies and due to the attractive rental deals on offer. This will continue to see backfill vacancy and elevated vacancy in existing assets and pressure on market rents. However, the pipeline of formed vacant industrial land is diminishing, with ownership concentrated in institutional hands and frequently only offered on a pre-lease basis. Infill sites and the recycling of obsolete assets is increasing and will only accelerate as the underlying land values continue to grow.

Investment demand remains high, but activity has been curtailed by a lack of suitable stock and this is likely to continue into 2017. Portfolio sales are likely to remain a key feature of the national industrial investment market due to the growing demand from offshore investors, prepared to pay a premium for scale.

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).

RESEARCH
Jennelle Wilson
Senior Director, Queensland
+61 7 3246 8830
Jennelle.wilson@au.knightfrank.com

Matt Whitby
Group Director, Head of Research & Consulting
+61 2 9036 6616
Matt.Whitby@au.knightfrank.com

INDUSTRIAL
Chris Wright
Director, Joint Head of Industrial QLD
+61 7 3246 8861
Chris.Wright@au.knightfrank.com

Mark Clifford
Director, Joint Head of Industrial QLD
+61 7 3246 8802
Mark.Clfford@au.knightfrank.com

Mark Horgan
Manager—Strathpine Office
+61 7 3482 6000
Mark.Horgan@au.knightfrank.com

NATIONAL
Greg Russell
Head of Industrial, Australia
+61 7 3246 8804
Greg.Russell@au.knightfrank.com

VALUATIONS
Tim Uhr
Director
+61 7 3193 6877
Tim.Uhr@qld.knightfrankval.com.au

Ian Gregory
Director
+61 7 3193 6844
IanGregory@qld.knightfrankval.com.au

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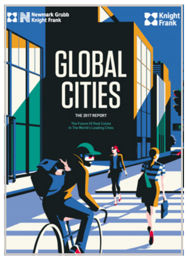

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