

PARRAMATTA

OFFICE MARKET BRIEF SEPTEMBER 2018



Key Facts

Tenant relocation and expansion is forecast to triple office demand **over the next three years to 15,000-20,000 sq m p.a.**

Lack of new speculative stock has kept the vacancy rate steady at **3.2%, well below the 10 year average of 7.3%.**

Investment activity thus far in 2018 has totalled \$353 million, led by large domestic institutions, including the standout sale of 60 Station Street (\$277.6m)



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Tenant relocation drives absorption

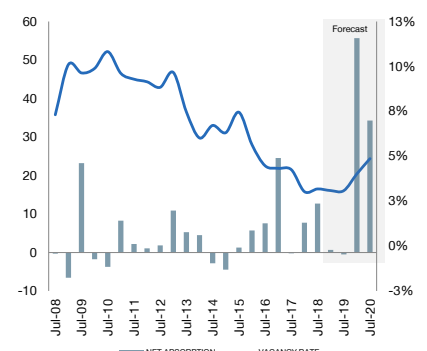
The positive tenant activity at the end of 2017 has continued into 2018, recording absorption of 12,691 sq m in the six months to July 2018, taking annual absorption to 20,442 sq m. The strong demand has stemmed from a combination of tenant relocation and organic expansion reflecting solid employment growth. The main contributor to this positive absorption is the NSW Department of Education relocating from the Sydney CBD to Parramatta occupying all of 105 Phillip Street (25,000 sq m). Additionally, smaller private sector tenants have driven the absorption, including Choice Business College (943 sq m) and Loan One (935 sq m) occupying space at 7 Hassall Street.

Office demand forecast to triple in coming years

Looking ahead, office demand in Parramatta over the next three years is forecast to be around 15,000-20,000 sq m pa, more than triple the historical average of around 5,000 sq m pa last 10 years.

Driving this demand will be the large corporations, including NAB and QBE in conjunction with the NSW Government relocating and expanding in the Parramatta market. On the back of this we expect to see further corporate tenant engagement with more prime stock becoming available through the development pipeline.

FIGURE 1
Net Absorption and Vacancy
Per six month period (000's, %)



Source: Knight Frank Research/PCA

Vacancy remains well below historical average

The Parramatta vacancy rate increased for the first time since July 2015 to 3.2% as at July 2018, slightly up from 3.0%. This remains well below the 10 year average of 7.3%. The prime market recorded 3,237 sq m of vacancy as at July 2018, the first time since January 2016 there has been available stock. The prime rate currently sits at 1% mainly due to tenant contraction within Jesse Street Centre. Secondary vacancy continued to decline with a modest fall from 5.3% to 5.0% as at July 2018.

Prime vacancy to remain tight over next two years

With the majority of future developments in Parramatta being substantially pre-committed by tenants relocating from other markets, we anticipate vacancy across the market to remain tight over the next 12 months. The overall vacancy rate in the Parramatta CBD is expected to remain steady at circa 3% until future developments reach completion. Additionally, a number of large tenant enquiries in the market are expected to keep prime vacancy at a minimum even as new stock comes online.

Enquiries in the market include Westpac actively seeking 9,000-11,000 sq m, Samsung (10,000-13,000 sq m) and Toyota (3,000 sq m) all of which have mandates with Parramatta as an option.

Rental growth across the board

Rental growth in Parramatta continues to be driven by the limited vacancy in both the prime and secondary market, in conjunction with rental growth across the wider Sydney market. The average prime gross face rent has increased by 7.2% YoY to \$649/sq m (\$534/sq m net face) as at July 2018, well above the 10 year growth average of 4%. Whilst face rents have increased significantly, prime incentives have remained steady at circa 18-19% over the past year, resulting in gross effective rental growth of 7.6%. This has enabled owners to capitalise on the favourable market conditions.

In the secondary market, current gross face rents average \$558/sq m (\$438/sq m net face) as at July 2018, up 10.6% YoY. Secondary incentives have declined to around 20%-21% from 22%-23% a year ago, boosting the gross effective rental growth to 11.3% YoY.

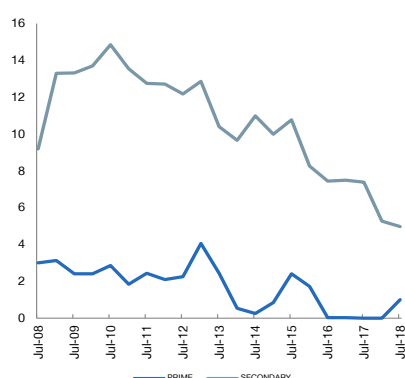
Limited speculative stock in pipeline

With the Parramatta development cycle well underway the first half of 2018 saw 25,000 sq m added to the market with completion of 105 Phillip Street for the NSW Department of Education. This represents the first major addition in new stock in Parramatta since 1PSQ in January 2017.

Withdrawals for the period totalled 10,797 sq m, the largest amount of stock taken offline since the first half of 2014 due to residential and retail conversions. This resulted in net additions of 14,203 sq m for the period and the total office stock base reach 719,619, a 4.3% increase over the past three years.

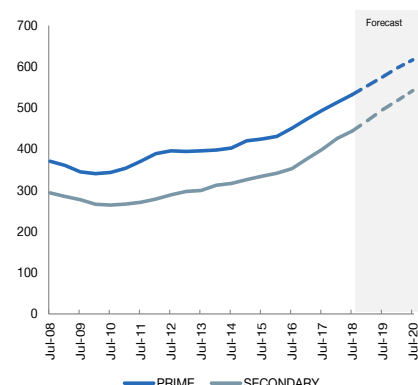
The next wave of supply will be mainly focused on the Parramatta Square precinct with 4PSQ (65,000 sq m – fully committed to the NSW Government) and 3PSQ (43,000 sq m – fully committed to NAB) due for completion in late 2019 and 2020 respectively. Additionally works have begun at the GPT owned 32 Smith Street site which will see 26,000 sq m added to the market by late 2020 to mid-2021, with QBE reported to have committed to 51% of the building.

FIGURE 2
Parramatta Vacancy
Total vacancy by grade (%)



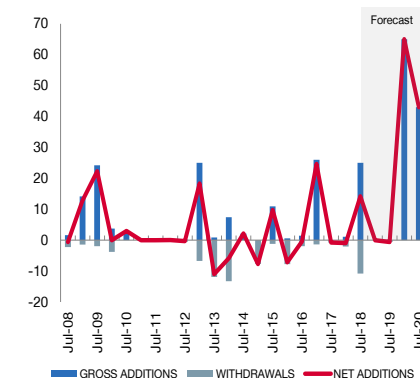
Source: Knight Frank Research/PCA

FIGURE 3
Average Gross Effective Rent
Parramatta (\$/sq m)



Source: Knight Frank Research

FIGURE 4
Parramatta office Supply
Per six month period (000' sq m)



Source: Knight Frank Research/PCA

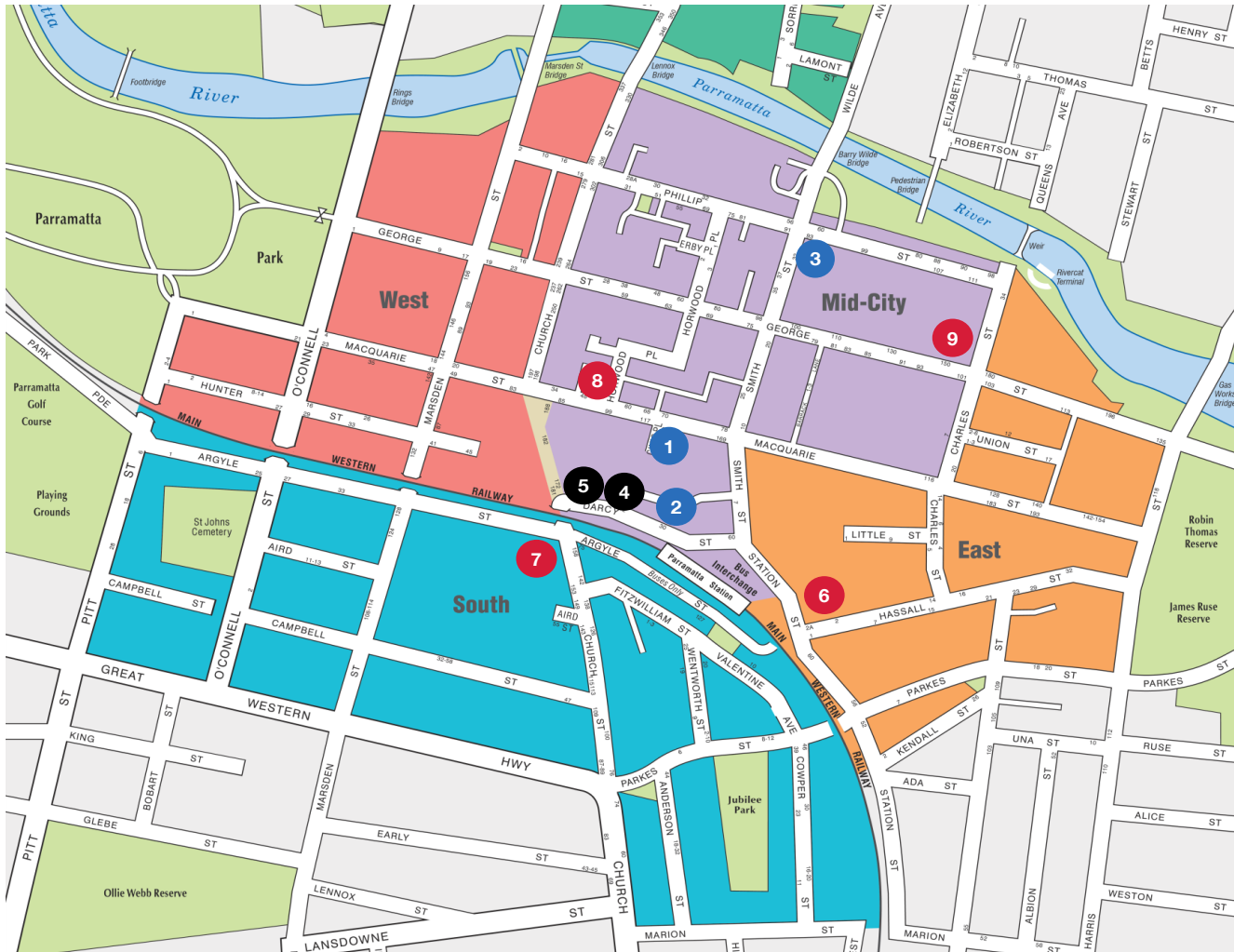
TABLE 1
Parramatta Office Market Indicators as at July 2018

Grade	Total Stock (sq m)	Vacancy Rate (%)	Annual Net Absorption (sq m)	Annual Net Additions (sq m)	Average Gross Face Rent (\$/sq m)	Outgoings (\$/sq m)	Average Net Incentive (%)	Average Core Market Yield (%) [^]
Prime	324,617	1.0	21,763	25,000	649	116	18.0	5.25 - 6.50
Secondary	395,002	5.0	-1,321	1,136	558	121	20.5	5.50 - 7.00
Total	719,619	3.2	20,442	26,136	604			

Source: Knight Frank Research/PCA

[^] Based on an assumed 5 year WALE

MAJOR OFFICE SUPPLY



Source of map: Knight Frank

- 1 153 Macquarie St (Parramatta Square Stage 3)[^] - 43,000m² [NAB]
Walker Corporation - Mid 2020
- 2 Parramatta Sq. Stage 4[^] - 65,000m² [NSW Government]
Walker Corporation - Mid 2019
- 3 32 Smith St - 26,000m² - DA Approved [QBE -51%]
GPT - 2021
- 4 Parramatta Sq. Stage 6[^] - 50,000m²+
Walker Corporation - 2021+
- 5 Parramatta Sq. Stage 8[^] - 70,000m²+
Walker Corporation - 2021+
- 6 2-6 Hassall Street - 28,000m²
Charter Hall -2020+
- 7 Westfield, 159 Church St - 112,000m²
Scentre Group - 2021+
- 8 Greenway Plaza - 35,000m²
Coombes Drivas - 2021+
- 9 140 George Street - 45,000m²
Dexus -2021+

- Under Construction/Complete
 - DA Approved / Confirmed / Site Works
 - Mooted / Early Feasibility
- NB. Dates are Knight Frank Research estimates
Includes select major office supply (NLA quoted)
Major tenant pre-commitment in [brackets] next to NLA
* Part of Parramatta Square project

Domestic institutions driving investment activity

Following strong sales activity in 2017 with \$498 million in transactions, this has continued into 2018 with \$353 million traded thus far in the year. The sustained demand for assets in Parramatta has been driven by evidence of strong tenant demand for new stock and the rental growth outlook. Investors now seeing Parramatta as an attractive investment destination coupled with being priced out of other major CBD markets.

The standout sale for 2018 and largest sale on record in the Parramatta market was 60 Station Street (Eclipse Tower) which traded in August for \$277.6 million. The asset was purchased by GPT from REST Super on a core market yield of 5.57%, fully leased on a four year WALE. The acquisition sees GPT with a strong footprint on the Parramatta office market adding to its current development at 32 Smith Street. Once complete GPT will join Walker Corp, Dexus, Charter Hall and Brookfield with substantial holdings in Parramatta.

By purchaser type, AREITS and Unlisted/Syndicates have accounted for 81% of total sales since January 2017. This has reaffirmed the increased appetite of institutional owners in the Parramatta market, which has been traditionally dominated by private investors. Looking ahead, investment sales are forecast to outperform 2017 with a number of assets currently undergoing off market and public campaigns. Of note is 33 Argyle Street and 91 Phillip Street which are expected to see strong interest with their tenure profile and steady income in conjunction with future re-development potential.

Yield compression continues

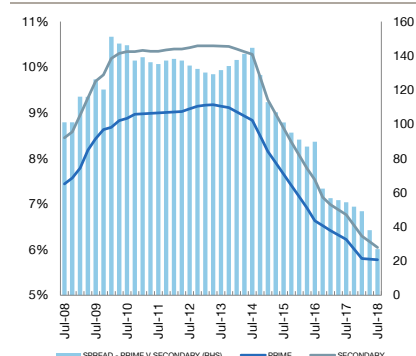
Amidst the strong investment activity over the past 18 months yields have continued to tighten across both the prime and secondary markets. Average prime yields have compressed by circa 64bps since January 2017 to measure 5.78% and range between 5.25-6.50% as at July 2018. The secondary market has seen further compression in comparison to the prime with the average yield declining by circa 93bps to measure 6.05%. This has taken the prime and secondary yield spread to 27bps, the tightest gap on record. Downward pressure on yields is forecast to continue, however we anticipate rental growth to be the main driver of performance over the next 12 months.

TABLE 2
Recent Leasing Activity Parramatta

Address	NLA (m ²)	Face Rental (\$/m ²)	Term yrs	Lease Type	Tenant	Lease start date
60 Station Street	2,644	590N	4	Renewal	Landcom	Sep-19
10 Smith Street	1,164	535N	7	Renewal	GPNSW	Nov-18
87 Marsden Street	949	495N	10	New	Countrywide	Oct-18
88 Phillip Street	590	480N	3	New	AJ Gallagher	Aug-18
7 Hassall Street	935	350G	5	New	Loan One Pty Ltd	Apr-18
110 George Street	937	510N	5+3	New	TAFE NSW	Mar-18

Source: Knight Frank Research n refers net g refers gross

FIGURE 5
Average Core Market Yields
Parramatta Yield (LHS) and Spread bps (RHS)



Source: Knight Frank Research

TABLE 3
Recent Sales Activity Parramatta (\$10m+)

Address	Price (\$ mil)	Core Mkt Yield (%)	NLA (sq m)	\$/sq m NLA	WALE (yrs)	Vendor	Purchaser	Sale Date
60 Station Street	277.6	5.34	25,729	10,789	4.0	REST	GPT	Aug-18
12-14 Wentworth Street	10.5	5.44	1,243	8,447	N/A	Private	Private	Aug-18
2-6 Hassall Street	40.0	N/A	2,648	15,106	N/A	Private	Charter Hall	Aug-18
75 George Street	86.3	5.51	9,568	9,020	3	CorVal	Mirvac	Nov-17

Source: Knight Frank Research



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