

CANBERRA

OFFICE MARKET BRIEF APRIL 2018

Key Facts

As at January 2018, Canberra's overall vacancy rate measured **13.1%**, increasing from 11.6% six months prior stemming from numerous completions.

Sales of \$778.6 million, were transacted over 2017, fuelled by an improved buyer depth and stronger interest in the secondary market.

Owners offering speculative fitouts in order to attract tenants in the secondary market.

Tight vacancy in the Civic and Parliamentary precincts has **increased gross face rents by 3.3% to \$466/sq m**.



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Strong investment activity in both the prime and secondary markets highlights the positive market sentiment across the Canberra CBD and suburban markets.

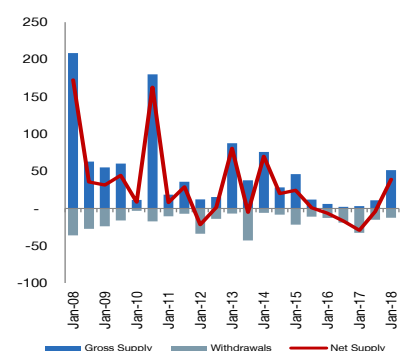
Surge in office supply

The Canberra office market experienced a surge in supply over the second half of 2017 with 51,364 sq m of new and refurbished space added to the market. The major new developments to have reached completion are 71 Athllon Drive, Tuggeranong (31,202 sq m—100% committed by The Department of Social Services), and the full refurbishment at 17 Moore Street, Civic (5,895 sq m), which remains predominately uncommitted with c4,800 sq m currently available. Additionally, there were partial refurbishments at 12 Brindabella Circuit, Airport (1,361 sq m) and 51 Allara Street, Civic (4,140 sq m).

In the six months to January 2018, 12,268 sq m was withdrawn from the market taking net supply for the period to 39,096 sq m well above the previous period of negative 4,098 sq m. Owners opting to withdraw and redevelop their sites for alternative uses continue to be a key contributing factor to office withdrawals amongst the secondary stock.

Over the next 18-24 months c40,000 sq m of new or refurbished space is expected to come online, primarily speculative space which will be a good test for the Canberra market. Developments include full refurbishments at 10 Brindabella Circuit (4,932 sq m—40% pre-committed) and 38 Sydney Avenue (9,098 sq m—available). Additionally, new speculative space will stem from the Civic Quarter development (c14,500 sq m) and Constitution Place development (c12,000 sq m) due for completion in mid 2019 and late 2020 respectively.

FIGURE 1
Supply Additions and Withdrawals
Per six month period (000' sq m)

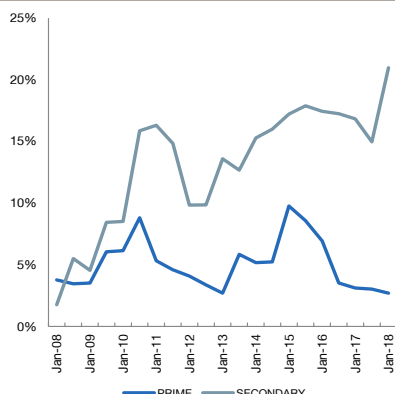


Market confidence in Canberra continues to improve following the surge in new developments and refurbished space coming online. Traditionally new stock has been pre-committed by large Government tenants. The improved confidence is highlighted by the increase to build speculatively and un-committed, and has resulted in attracting attention from private sector tenants.

Strong take up in A Grade market

The A Grade market experienced strong absorption of 51,580 sq m, the highest level in five years. Whilst across the total market, net absorption remained steady with 148 sq m absorbed over the six months to January 2018.

FIGURE 2
Canberra Vacancy Major Precincts*
Per six month period (%) - by grade



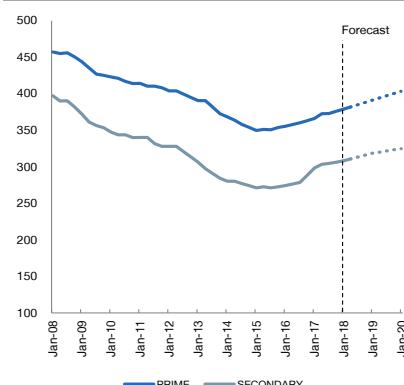
Source: Knight Frank Research/PCA
* incorporates Civic, Parliamentary Precinct & Town Centres

The catalyst for the high net absorption in the A grade market was the Department of Social Services (DSS) occupying 31,586 sq m at 71 Athllon Drive, Tuggeranong. In the private sector DXC Technology has taken circa 2,500 sq m at the refurbished 10 Brindabella Circuit.

Speculative fit outs driving take up for small suites

Demand by the private sector in the B grade market has also been strong, more specifically in the Civic precinct which recorded absorption of 3,083 sq m. Notable deals include Evolve FM occupying the 425 sq m at 60 Marcus Clarke Street, Civic and Avoka Technologies leasing 227 sq m at 64 Northbourne Avenue, Civic. These deals were taken with speculative fit outs which highlights owners opting to do generic fit outs in vacant spaces in order to attract time sensitive tenants.

FIGURE 3
Civic Gross Effective Rent
By Grade (\$/sq m)



Source: Knight Frank Research

New supply and DSS departure softens vacancy

The surge in new supply over the second half of 2017 which has been partly un-committed has driven the overall vacancy rate to 13.1% as at January 2018, up from 11.6% six months prior. By grade, the A grade market recorded a 10 year low of 8.5% down from 9.8%. In contrast with the overall secondary stock, vacancy climbed to 17.1% up from 13.2%, fuelled by the Department of Social Services vacating its old premises at Tuggeranong Office Park which now sits vacant. The Cromwell owned site is rumoured to potentially be withdrawn in the future to make way for alternative uses.

Looking at the vacancy of the major precincts* (Knight Frank definition—see back page) both primary and secondary markets continue to trend below the five year average. Prime vacancy has contracted to 2.7% in comparison to the five year average of 5.4%. With tenants opting for prime office space, vacancy in the major precincts secondary market climbed to 21% as at January 2018.

With A Grade vacancy in the Civic and Parliamentary Precincts at 4.5% and 0.4% respectively, the Civic Quarter (c14,500 sq m) and Constitution Place (c12,000 sq m) developments are expected to ease some of this pressure on the market come mid 2019. Upon completion the developments will add a new tier of stock to the prime market with rents anticipated to be in excess of \$600/ sq m.

TABLE 1
Canberra Office Market Indicators - January 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 Incentive (%)	Average Core Market Yield (%)
A Grade								
Civic (City)	299,888	4.5	-899	0	471	73	20	5.75-6.75
Parliamentary	261,910	0.4	2,254	0	462	74	18	6.75-7.00
Town Centres	252,201	3.0	32,567	31,568	405	65	25	7.75-8.25
Other	304,767	24.0	17,701	9,761				
Secondary								
Civic (City)	368,781	16.9	-5,222	7,193	406	88	24	7.50-8.50
Parliamentary	186,600	15.8	-9,796	-9,098	407	72	20	7.25-7.75
Town Centres	269,070	30.1	-24,283	-4,200	333	67	30	9.00-10.50
Other	433,929	9.7	7,247	-266				
Total Market	2,377,146	13.1	19,579	34,998				

Source: Knight Frank Research/PCA Parliamentary comprises Barton, Parkes and Forrest office precincts Other includes remaining PCA sub localities
* Modern upper prime assets with long WALEs trading below this range (sub 6.00%) Town Centres comprise Phillip, Tuggeranong and Belconnen office precincts

Tightening A Grade CBD vacancy strengthening rents

The tightening vacancy rate across all major precincts in the A grade market coupled with the strong absorption in the six months to January 2018 has fuelled rental growth in the A grade market. Across the A grade Civic and Parliamentary precincts, gross face rents increased by 3.3% to \$466/sq m (\$393/sq m net) in the 12 months to January 2018, significantly above the 10 year growth average of 0.2% p.a. In the secondary market rental growth eased due to the increase in available stock, this has resulted in YoY gross face rental growth of 3.4% to \$406/sq m (\$326/sq m net), which is still well above the 10 year growth rate of 0.1%. Incentive levels across the major Canberra precincts dropped slightly in the prime market to 21.0% down from 21.7% 12 months prior. Secondary incentive levels remained unchanged at 24.5% throughout 2017.

Steady growth outside CBD

Outside the Civic and Parliamentary precincts, Town Centre rental growth has remained steady following limited tenant activity besides the DSS relocating within the Tuggeranong Office Park. Whilst new tenant activity has been limited there has been notable tenant retention, this includes the Department of Home Affairs at 6 Chan Street, Belconnen and the Department of the Prime Minister and Cabinet at 16 Bowes Place, Woden. Prime gross face rents in Town Centres recorded growth of 3.8% YoY as at January 2018 to measure \$405/sq m (\$340/sq m net). In the secondary market rental growth has remained unchanged in the six months to January 2018 with a surge in new supply following the Departure of the DSS from their old headquarters. Gross face rents have remained at \$332/sq m (\$265/sq m net). The airport precinct recorded the strongest gross rental growth in the prime market of 6.5% YoY to \$412/sq m (\$364/sq m net) on the back of a five year high of net absorption (12,051 sq m).

TABLE 2

Recent Leasing Activity Canberra

Address	NLA (sq m)	Gross Rental (\$/sq m)	Term (yrs)	Tenant	Date
64 Northbourne Ave, Civic	227	420	5	Avoka Technologies	Mar-18
7 London Circuit, Civic	6,951	U/D	10	Commonwealth Superannuation Corp	Jan-18
60 Marcus Clarke, Civic	425	425	5	Evolve FM	Jan-18
71 Athllon Drive, Tuggeranong	31,202	U/D	15	Department of Social Services	Sep-17
2 Constitution Ave, Civic	1,000	U/D	3	NACCHO*	Sep -17

Source: Knight Frank Research U/D: Undisclosed *National Aboriginal Community Controlled Health Organisation

Yields remain firm in investment market

Investment in Canberra recorded the strongest year on record with \$778.6 million (\$10 million+) in transactions over 2017, up from \$451.6 million in the 2016 calendar year. The record year has been driven by improved buyer depth, with investors seeking alternative value add assets in the secondary market in addition to the traditional low risk high WALE assets.

The standout sale of the year of 50 Marcus Clarke Street, trading for \$321 million on a core market yield of 5.69%. This reflects the tight yield for best in class assets and highlights the strength in the Civic and Parliamentary markets. Additionally, the purchase of 44 Sydney Avenue, Forest by Charter Hall for \$64.7 million, sold on a core market yield of 6.25%, it attracted strong interest due to its favorable expiry profile, strong tenant covenants and prime location. These sales have firmed the prime yield range in the Civic and Parliamentary precincts to average 5.75% to 6.75%.

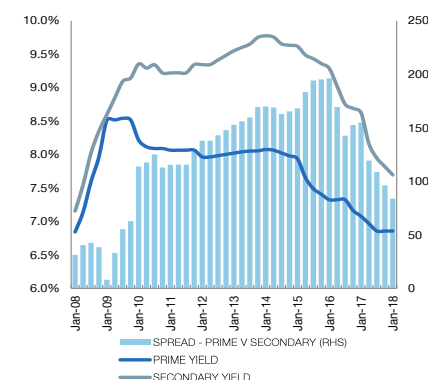
Improved interest for secondary stock

In the secondary market EG Funds Management acquired 42 Macquarie Street, Barton for \$15.6 million on a core market yield of 8.45%, with Hadley Green purchasing 169 Gladstone Street, Fyshwick for \$17 million on a core market yield of 8.40%. These sales reflect a tightening gap between prime and secondary stock. Across the CBD and Parliamentary precincts the average yield spread is down to 84bps in comparison to 155bps 12 months prior.

FIGURE 4

Core Market Yields & Spread

Canberra Blended Average – Prime & Secondary



Source: Knight Frank Research

TABLE 3

Recent Sales Activity Canberra

Address	Price (\$ mil)	Core Mkt Yield (%)	NLA (sq m)	\$/sq m NLA	WALE (yrs)	Vendor	Purchaser	Sale Date
Anzac Park West, Parkes	51.0	8.34	14,486	3,521	10	Dept. of Finance	EG Funds Mgmt	Nov-17
44 Sydney Avenue, Forrest	64.7*	6.25	9,948	6,054	7.7	Quintessential Equity	Charter Hall	Nov-17
14 Childers Street, Civic	92.15	N/A	15,047	6,124	3.7	Private	Challenger	Nov-17
50 Marcus Clarke Street, Civic	321.0	5.69	40,201	7,985	8.2	CIMB	Mirae Asset Global	Mar-17

Source: Knight Frank Research *headline price adjusted to \$58.6 million (net sale price) to account for outstanding incentives)

Outlook

- Canberra is set to see a strong surge in speculative supply in the next 18-24 months. The Civic Quarter development is set to add c14,500 sq m in conjunction with the Constitution Place development (c32,000 sq m) and the refurbishment of 38 Sydney Avenue and 10 Brindabella Circuit this is anticipated to increase vacancy in the tightly held Parliamentary and Civic A grade precincts.
- Following the increase in supply and the development pipeline Knight Frank research forecasts rental growth to be no more than 2% across both the prime and secondary markets over the next 24 months. Incentive levels are expected to remain firm if not increase in order for landlords to attract tenants into their buildings as new supply increases.
- Investment activity is anticipated to remain firm over 2018 with positive sentiment across most sub markets and the increase in buyer depth from both private and institutional investors seeking value add opportunities. Yields are expected to remain steady with potential for slight compression across the board due to the lack of opportunity nationally and an increase in the number of investors moving up the risk curve in search for opportunistic assets.

MAJOR OFFICE SUPPLY

- 1 3 Molonglo Drive, Airport - 36,000m² [DoI&BP*]
Capital Airport Group - Complete - 100% committed
- 2 2 Constitution Ave[^] - 4,930m²
ISPT - Complete (total NLA 20,014m²) - 75% committed
- 3 33 Allara St[^] - 9,201m² [MDBA]
Molonglo Group - Complete - 43% committed
- 4 17 Moore St[^] - 5,895m²
CorVal - Complete
- 5 Tuggeranong Office Park - 31,568m² [Dept of Social Services]
Cromwell Property Group - Complete, 100% committed -
- 6 Constitution Place[^] (Bld. 2) - 12,000m² ≈
Capital Property Group - Q3 2020
- 7 Constitution Place (Bld. 1)[^] - 20,000m² [ACT Govt]
ACT Govt/Capital Property Group - Q3 2020, 100% committed
- 8 Civic Quarter, Northbourne Ave[^] - 14,500m² ≈
Amalgamated Property Group - Q3 2019
- 9 5 Nangari Street, City - 1,600m²
Molonglo Group - 2020+
- 10 13-15 Challis St, Dickson - 13,000m² (MVR site ‡)
100% committed - 2019+
- 11 Section 96[^] - 37,500m²
QIC - 2019+ subject to pre-commitment
- 12 2 Darling Street, Barton - 11,500m²
Doma Group - 2019+
- 13 Section 12 (Block 9 & 10) - 35,000m²
A&S Haridemos - 2020+
- 14 45 Furzer St, Phillip - 40,600m²
Doma Group - 2020+ subject to pre-commitment
- 15 25 Catalina Drive, Airport - 25,000m²
Capital Airport Group - 2020+

NB. Dates are Knight Frank Research estimates

Major tenant precommitment in [brackets]

* Dept of Immigration & Border Protection

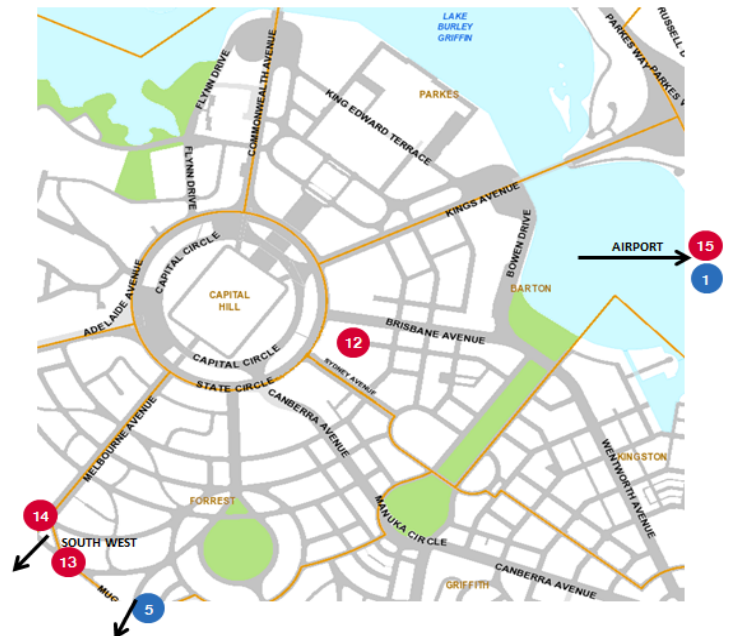
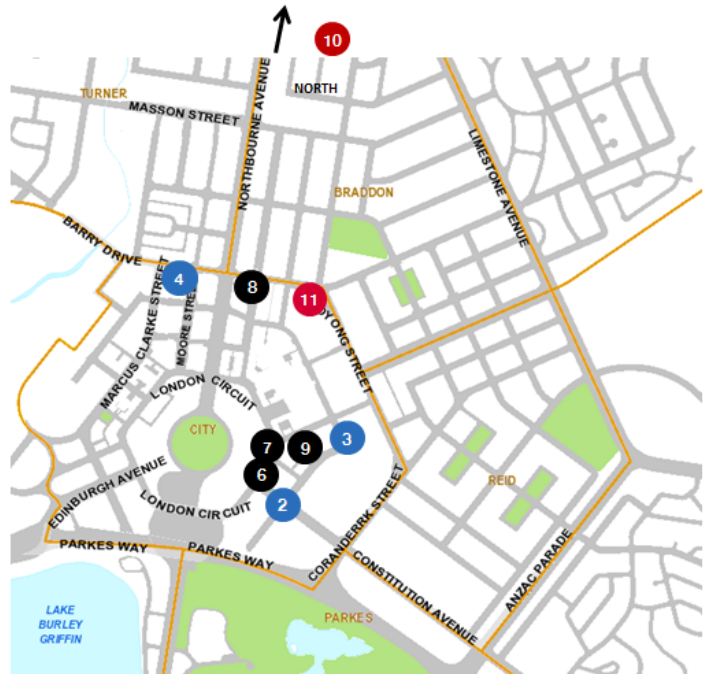
≈ Speculative development

[^] Civic precinct

Office NLA quoted

Major refurbishment

- Development is of the same size as what it's replacing



- Under Construction/Complete
- DA Approved / Confirmed / Site Works
- Mooted / Early Feasibility

Source of Map: ACT Planning and Land Authority (ACTMAPi)



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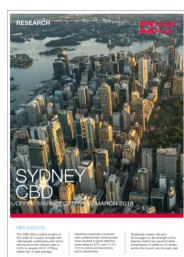
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Front cover photo: 2 Constitution Avenue, City

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