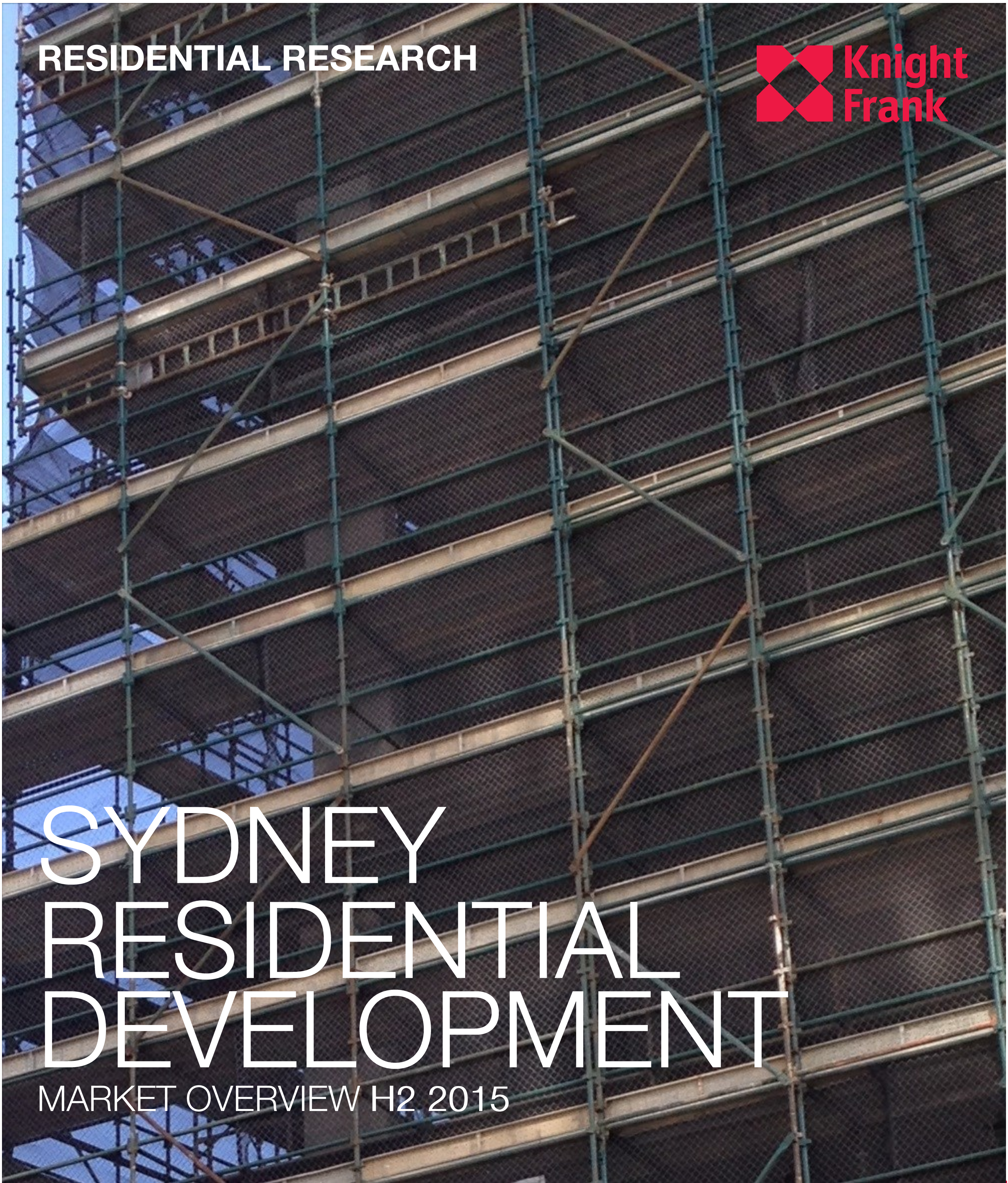


RESIDENTIAL RESEARCH

SYDNEY RESIDENTIAL DEVELOPMENT

MARKET OVERVIEW H2 2015

HIGHLIGHTS

Across Greater Sydney, at the end of August 2015, sites suitable for higher density development averaged $177,000 (ranging from $80,000 to $1 million) per apartment, up almost 35% on the prior year.

After a long period of undersupply, there is a push from the NSW government towards higher density living around established infrastructure hubs. This has resulted in suitable areas being rezoned.

The tightened lending environment is expected to have some impact on investors, although these measures endorsed by APRA could be negated if there are any further cuts to the cash rate.

KEY FINDINGS

Greater Sydney higher density residential development site sales tallied $4.61 billion in the year ending 31 August 2015.

In the past year, by value, **62.9% of Greater Sydney development sites were sold to foreign investors**.

Foreign investors have a proposed $10.39 billion worth of residential developments in the pipeline in NSW.

Lone person households are projected to have the highest growth of 1.9% per annum over the next twenty years

Largest pipeline of committed major infrastructure projects across the country, leading to positive employment growth

Currently there are 32,715 apartments under construction in Greater Sydney—led by the North West region.

MICHELLE CIESIELSKI
Director—Residential Research

SYDNEY RESIDENTIAL DEVELOPMENT SITES

A push from the NSW government towards higher density development around established infrastructure hubs has resulted in vast areas being rezoned, after a long period of undersupply. Many local and foreign developers are now competing for the diminishing suitable greenfield sites; amalgamating single dwelling allotments and redeveloping brownfield sites.

Sales Volume

Sales of major sites likely for higher density development in Greater Sydney totalled $4.61 billion in the year to 31 August 2015; this was up 6.9% on the previous year, as shown in Figure 1.

Sales turnover is trending significantly higher than volumes achieved in the years ending August 2011 and August 2012; before several key precincts across Greater Sydney had been rezoned for higher density residential. Since this time, the value of sales transactions have increased four-fold, first doubling to $2.01 billion in the twelve months to 31 August 2013; and then doubling again to $4.31 billion the following year.

FIGURE 1
Total Residential Site Sales Volume Greater Sydney
Potential Higher Density Development, $5M+

Source: Knight Frank Research

After a steep prolonged trajectory in site sale growth, more developers are now carrying out longer due diligence periods than previously experienced, so this could be a sign that the market close to reaching the peak for total sales volume.

Over the past two years to 31 August 2015, the South region recorded the highest volume of residential development site sales at $3.21 billion, followed by the Sydney CBD with $2.65 billion.

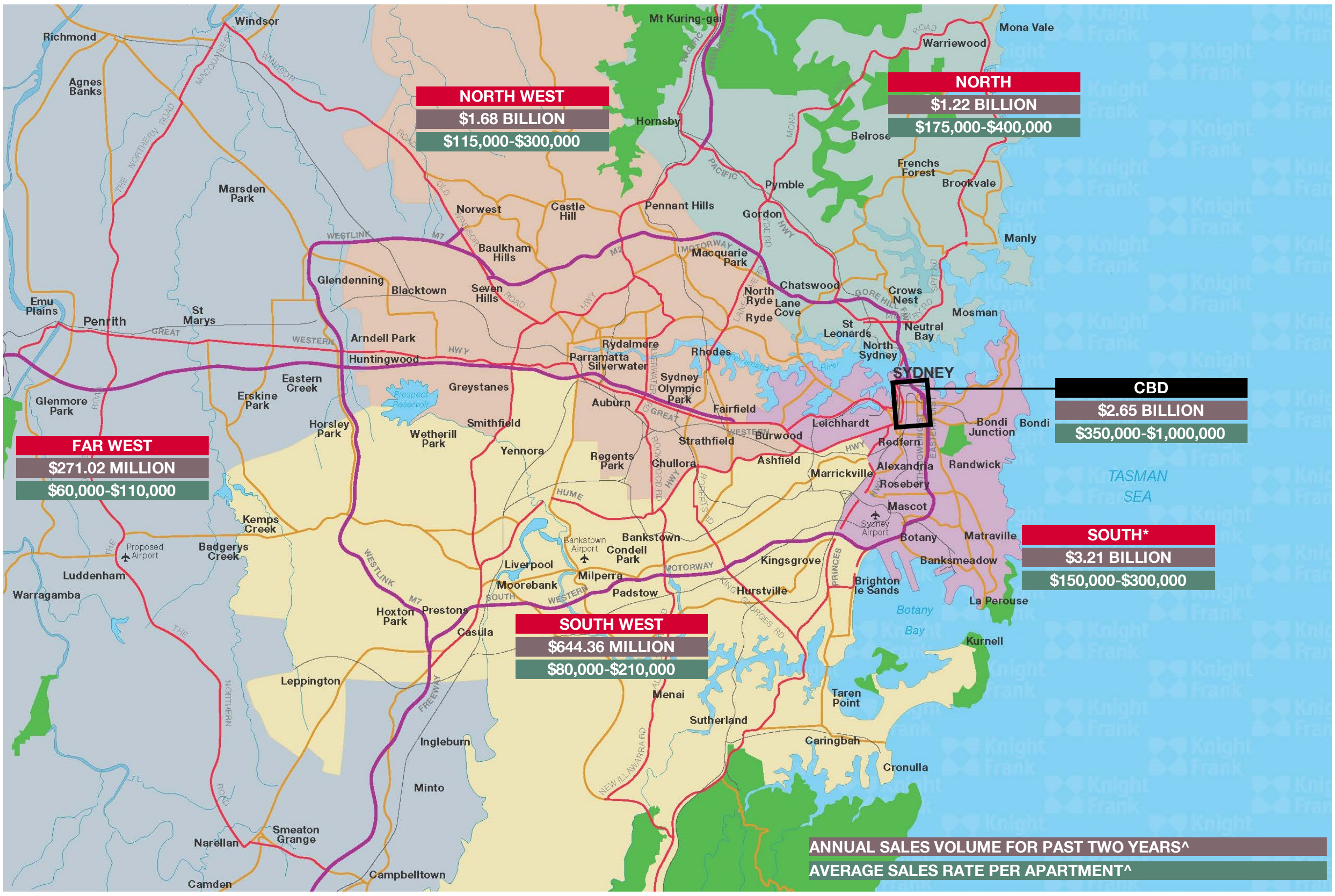
The North West region, which includes Parramatta, saw sales turnover in the order of $1.68 billion and the North region totalled $1.22 billion. This includes the August 2015 sale of the Channel 9 Studios for $147.50 million. The South West region saw sales turnover of $644.36 million, while the Far West region recorded $271.02 million in the same period. With the recent Government commitment of the Sydney Metro City & Southwest railway project and the Western Sydney Airport at Badgerys Creek, it is expect more opportunities to come to market in these western regions over the coming year.

Average Rates

Across Greater Sydney, at the end of August 2015, sites suitable for higher density development averaged $177,000 per apartment, up almost 35% on the prior year. At this time, Sydney CBD sites ranged from $350,000 to $1,000,000 per apartment; off the back of several office buildings selling that are earmarked for residential conversion. It's unlikely many apartments from these developments will be marketed this side of 2018, as many have long office leases still in place.

The North region achieved between $175,000 and $400,000 per apartment, as the South trended a tighter range, starting at $150,000 through to $300,000. In the west, average site sales per apartment were closer to $115,000 to

RESIDENTIAL REGIONS—GREATER SYDNEY SITES WITH POTENTIAL FOR HIGHER DENSITY DEVELOPMENT



Source: Knight Frank Research *Excludes CBD ^As at 31 August 2015

$300,000 in the North West, $80,000 to $210,000 in the South West and $60,000 to $110,000 in the Far West.

Type of Purchasers

Across all Greater Sydney development sites sold in the twelve months to 31 August 2015, with potential for higher density, it was found that by value, 62.9% were purchased by a foreign purchaser. An analysis of the country of purchasers within the group, indicates that 79.2% were from China.

This includes groups such as Aqualand, Dalian Wanda, Yuhu, Golden Horse, Far East Organisation and China Poly Group. As the Australian Dollar (AUD) remains low, it is likely that strong offshore interest for Sydney residential property will continue.

Foreign investors propose to invest $10.39 billion in New South Wales (NSW) residential developments in the coming years, according to applications submitted to the Foreign Investment Review Board (FIRB).

Looking at the distribution of foreign investment into residential developments, as shown in Figure 2, New South Wales is slightly behind Victoria (at $10.41 billion) as the preferred state to invest, but a long way ahead of Queensland ($2.81 billion) and Western Australia ($1.32 billion).

As the reporting of this FIRB application data is lagged, it's likely a higher NSW volume will result given the increased number of sites sold to foreign purchasers, when Treasury releases the 2014/15 annual report.

FIGURE 2

Proposed Investment in Residential Developments

Distribution by Foreign Investors, when applications submitted in 2013/14

Source: Knight Frank Research, FIRB

TABLE 1

Major Sales—Development Sites With Potential For Higher Density Apartments, Greater Sydney

Address	Sale Price $ mill	Site Area m²	No. Apts~	Price $/Apt~	Price $/m²	Vendor	Purchaser	Sale Date
500-520 Pacific Hwy St Leonards^	150.00	3,752	477	314,465	39,979	Charter Hall	New Hope∞	Aug-15
Channel 9 Studios 6-30 Artarmon Rd, Willoughby^	147.50	30,640	400	368,750	4,814	Nine Entertainment Co	Euro Properties∞	Aug-15
472-486 Pacific Hwy St Leonards^	121.00	5,133	650	186,154	23,573	Leighton	Mirvac Group	Jun-15
Bay Park, Burroway Rd Wentworth Point±	100.00	26,000	678	147,493	3,846	Payce Consolidated JV Sekisui House∞	Piety Investments	Jun-15
Units 16-20, 39-41 1A Coulson St, Erskineville*	65.00	10,883	222	292,793	5,973	Fridcorp	B1 Development Group	Jun-15
1-9 Lachlan St & 2 Sam Sing St, Waterloo*	35.50	5,038	143	248,252	7,046	Becton Group	Golden Age and Time & Place∞	Jun-15
Strathfield Golf Club site 84 Centenary Dr, Strathfield±	52.50	20,239	300	175,000	2,594	Strathfield Golf Club	Metro Property Development & Alceon	Apr-15
The Compass Centre site 85-89 North Tce, Bankstown‡	45.00	8,174	477	94,340	5,505	Banna Property Group	Ganghui Pty Ltd∞	Apr-15
Fmr Woolstore complex 100 Harris St, Pyrmont*	90.00	7,813	361	249,307	11,519	Citilease Property Group	Mr Michael Teplitsky	Mar-15

Source: Knight Frank Research ~**Estimate**/Potential ∞Foreign Vendor/Purchaser Residential Regions (see map): ^North *CBD & South ±North West ‡South West

KEY DEVELOPMENT DRIVERS

The Economy

NSW is currently countering a sluggish Australian economy. The building and construction sector has injected much needed stimulus into the local economy which is counteracting the fallout of the weaker price of coal and iron ore, with a slowing Chinese economy. According to the Australian Bureau of Statistics (ABS), growth in State Final Demand in the quarter to June 2015 rose 0.8%, after recording 0.9% in the previous quarter; to total 3.2% over the year to June 2015. The AUD remains low, attracting local tourism and foreign investors to buy new dwellings to add to the housing stock.

Interest Rates

The Reserve Bank of Australia (RBA) left the cash rate at the historic low of 2.00% in September 2015; after earlier cutting the rate by 25 bps in May. Low interest rates have directed investors to actively invest in the property market over the past two years, with capital values rising to record highs in Sydney and to a lesser extent, in Melbourne.

Lending Environment

After two years of strong capital growth, dominated by the investor market in the Sydney and Melbourne property markets, a reduced and more responsible lending target was endorsed by Australian Prudential Regulatory Authority (APRA) in May 2015.

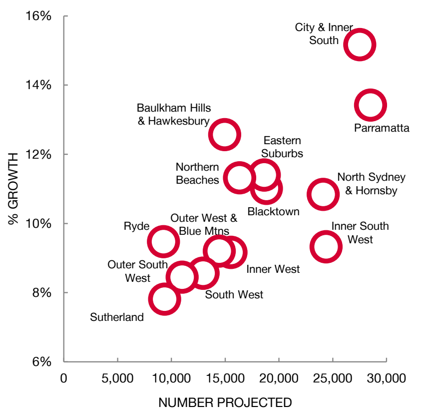
Since this time, banks have started to reduce their maximum LVR's, introducing new variable rates and requiring customers to provide evidence of existing loan repayments before being accepted. This is in addition to applying serviceability repayment loading buffers to existing mortgage repayments as part of borrowers serviceability assessment in a higher interest rate environment. These overall housing lending standards are only part of the concern, with APRA, more recently, commenting on the current lending environment; where house prices are high, interest rates are low and income growth is subdued. In addition, the potential for a slow but steady erosion of credit quality in home loan portfolios as investor lending (and the rate of growth) rises with interest-only loans and increased use of third-party originated lending. The tightened lending environment is expected to have some impact on investors, although the measures endorsed by APRA could be negated should the cash rate be cut any further.

Employment Growth

As at June 2015, unemployment stood at 4.9% for the Greater Sydney region, trending lower than the 5.1% recorded in June 2014. The Department of Employment have projected employment growth in Greater Sydney, by SA4 ABS regions. As shown in Figure 3, the traditional employment nodes of City & Inner South, Parramatta and North Sydney & Hornsby will continue to experience the most number of new jobs created in the five years to November 2019.

Inner South West is also expected to grow by over 24,000 new jobs whilst the regions for highest growth are projected for Baulkham Hills & Hawkesbury,

FIGURE 3
Employment Growth Projections Greater Sydney, SA4 level
Five years to November 2019



Source: Knight Frank Research, ABS, Department of Employment

Northern Beaches, Eastern Suburbs and Blacktown regions.

Cost of Construction

With a strong demand for construction products and services for housing and infrastructure, together with the elevated price of development sites over the past two years, there has been much focus on increasing cost of construction. Despite this, there are many examples of foreign developers continuing to build and jeopardise profit margins after paying a premium for the site in order to get established in the Australian market.

Over the twelve months to June 2015, building costs have increased an estimated 3.0% in Greater Sydney according to Rawlinsons; trending above the annual average growth recorded over the past five years of 2.4%. With a solid pipeline of projects, there are no signs of cost growth easing, with Rawlinsons expecting this to increase by another 1.9% in the last six months of 2015, in total rising a projected 5.0% over 2015.

Rawlinsons estimate that a standard high -density, multi-storey apartment project in Greater Sydney would now cost on average $1,980/m² to $2,995/m² to build to a basic finish (or equivalent to a range of $102,900—$110,900 per apartment) plus GST. A project with a prime finish would be closer to an average $2,955/m² to $4,240/m² (or equivalent to a range of $561,000—$604,500 per apartment) exclusive of GST.

Projected Population

With the rate of natural increase continuing to climb, and net overseas migration remaining strong, Greater Sydney is projected to reach a population of 6.6 million by 2036. This equates to an annual growth projection of 1.4% and is on-par with the projected Australian average. Over the past twelve months to June 2014, Greater Sydney experienced a better than expected population growth of 1.8%; led by Cobbitty-Leppington SA2 (18.5%), Parklea-Kellyville Ridge (9.4%) and Homebush Bay-Silverwater (8.3%).

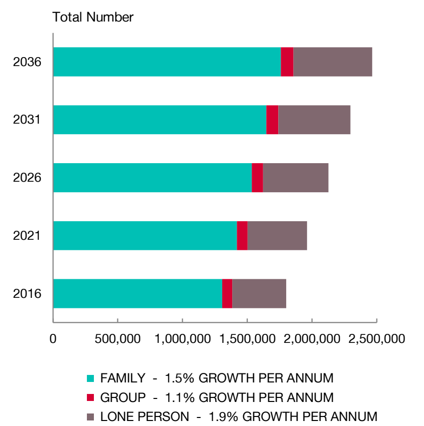
Projected Households

Greater Sydney households are expected to reach 2.46 million by 2036 according to the ABS; growing 1.6% per annum. Dissecting the total households into the configuration likely to take shape, it was found that 'Lone Person' Households would grow the most over this time, at 1.9% per annum to total an additional 230,000 households required to be suitable for this type of occupant. The 'Family' composition still dominates household structure as highlighted in Figure 4.

The Apartment Market

Capital growth in Greater Sydney mainstream apartments is currently

FIGURE 4
Household Projections By Type Greater Sydney



Source: Knight Frank Research, ABS

PIPELINE OF MAJOR PROPOSED INFRASTRUCTURE PROJECTS—GREATER SYDNEY

2015
Barangaroo Point Reserve (completed)

Camden Valley Way upgrade

2016
Darling Harbour Live & International Convention Centre

Old Wallgrove Road upgrade

2018
Sydney CBD & South East Light Rail

NorthConnex

New Northern Beaches Hospital

2019
Sydney Metro Northwest

2023
WestConnex

2024
Sydney Metro City & Southwest

2025+
Western Sydney Infrastructure Plan

Western Sydney Airport Badgery's Creek

KEY SUBURBS FOR APARTMENT PROJECTS DUE BY END 2018—GREATER SYDNEY

CBD & SOUTH
Mascot
Zetland
Waterloo
Rosebery
Botany

NORTH
Lane Cove
Chatswood
Asquith
Waitara
Gordon

NORTH WEST
Parramatta
Wentworth Point
Epping
Homebush
Auburn

SOUTH WEST
Wolli Creek
Canterbury
Liverpool
Hurstville
Campsie

FAR WEST
Cempbelltown
Penrith
Schofields
St Marys
Mount Druitt

trending the highest in the country, to record an annual 15.4% growth in June 2015. Sales turnover has come back slightly (down 2.9%) to an elevated 44,818 sales that year. Vacancy continues to trend significantly below market equilibrium, being recorded at 2.1% in June. Off-the-back of this heated capital growth, gross rental yields were down 35 bps to 4.46% in the twelve months to June 2015.

Projected New Apartment Pipeline

Since January 2011, 46,490 new apartments have been added to the Greater Sydney residential stock, led by the North West and the CBD & South regions, as detailed in Figure 6. In total across Greater Sydney, there are currently 32,715 apartments under construction, with another 23,775 with DA approval which are expected on-line by the end of 2018. Looking at the regions projected to see the most increase in higher density apartment stock until the end of 2018, taking into consideration projects under construction and DA approved, the North West is forecast to see an additional 20,480 apartments, an extra 43% on the prior 2011-2014 period. The CBD & South are forecast to add another 14,190 apartments by the end of 2018 and the South West region will see an extra 12,540 apartments; up 17% and 104% respectively, than the previous 4 years in each region. Apartment numbers in Greater Sydney could grow further when approval is granted for the additional 28,005 apartments currently submitted. Gaining approval is proving to be a lengthy process compared to other cities around Australia, so some of these projects may get pushed out beyond this timeline.

New Apartment Price Range

The price of new apartments across Greater Sydney can still vary significantly depending on distance to transport, employment hubs and the harbour and most importantly, the quality of finish, as shown in Figure 5.

FIGURE 5
New Apartment Price Range
Greater Sydney
Average rate per m^2

Source: Knight Frank Research

FIGURE 6
New Apartment* Pipeline
Greater Sydney
Number of Apartments

Source: Knight Frank Research

*Includes projects 4+ storeys with 25+ apartments in complex

An average new apartment of standard finish can range from $9,000/m^2 through to $22,000/m^2 whilst an average prime apartment currently trends between $32,000/m^2 and $45,000/m^2.

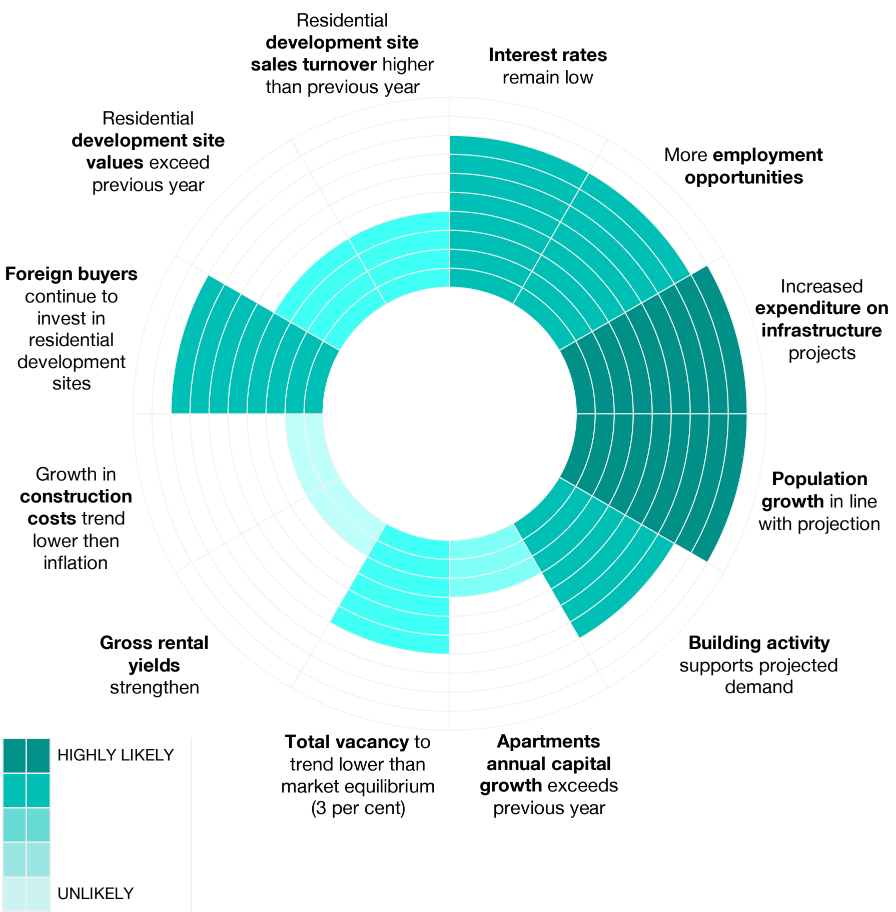
Foreign Investors

The Federal government has confirmed it will proceed with an initial fee of at least $5,000 for all foreigner investors purchasing into the Australian property market, with an additional $10,000 payable for every million dollar increment in the value of the property; slated from 1 December 2015.

The Victorian government have also introduced an additional two taxes: A 3% surcharge on the purchase price for a foreign investor and an on-going land tax fee for absentee owners. As yet, no other Australian states and territories have indicated they plan to introduce similar measures. Given Victoria has previously held one of the lowest stamp duty taxes payable for off-the-plan properties, this will now increase the relative competitiveness of the other states around the country.

The proposed changes may have an impact on those marketing to foreign investors as there has already been increased enquiry from offshore, but mostly surrounding the new penalties being introduced. While these additional fees may deter some foreign investors, they are not likely to significantly impact the current level of foreign investment activity within Australia, as foreign investors are looking for a longer term return – the lifestyle, access to good education institutions and a transparent ownership structure.

FIGURE 7
Key Development Drivers—One Year Outlook Greater Sydney



Source: Knight Frank Research

OUTLOOK

- Over the next twelve months it is likely that interest rates will remain low, with another 25bps cut possible and not being lifted before late 2016.
- With a solid pipeline of infrastructure projects committed by the State and Federal governments within Sydney growth corridors, it's expected that more employment opportunities will arise as a result.
- It is likely that population in Greater Sydney will continue to outpace the longer term projection of 1.4% growth each year to 2031 produced by the ABS.
- With the influx of development applications being submitted, planning delays are still experienced at some local councils. However this could improve with the recently updated Apartment Design Guide.
- The average timeframe between the project launch, to site works, has been shorter as minimum pre-sales have been hastily achieved. This timeframe has started to slightly widen and likely to continue over the next twelve months.
- Heated capital value growth is unlikely to be sustained at current levels, but above average capital growth will be experienced over the next year.
- As new supply comes on-line after a long time of undersupply; vacancy is expected to move closer to equilibrium although not reach 3% in the next year. Rents are likely to see lower growth; therefore keeping gross rental yields down.
- With a solid pipeline of projects, there are no signs of construction cost easing, with Rawlinsons forecasting an increase of 1.9% in the second half of 2015 (total 5.0% over 2015).
- As the AUD continues to remains low, it's likely that offshore interest for Sydney property for both development sites and apartments will remain high.
- Additional fees are unlikely to deter the majority of foreign investors, as it will just been seen as a cost of doing business in Australia.

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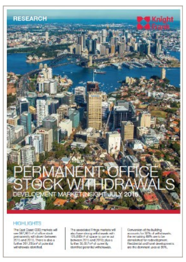

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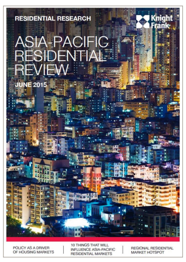

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