

THE SYDNEY SUCCESS STORY

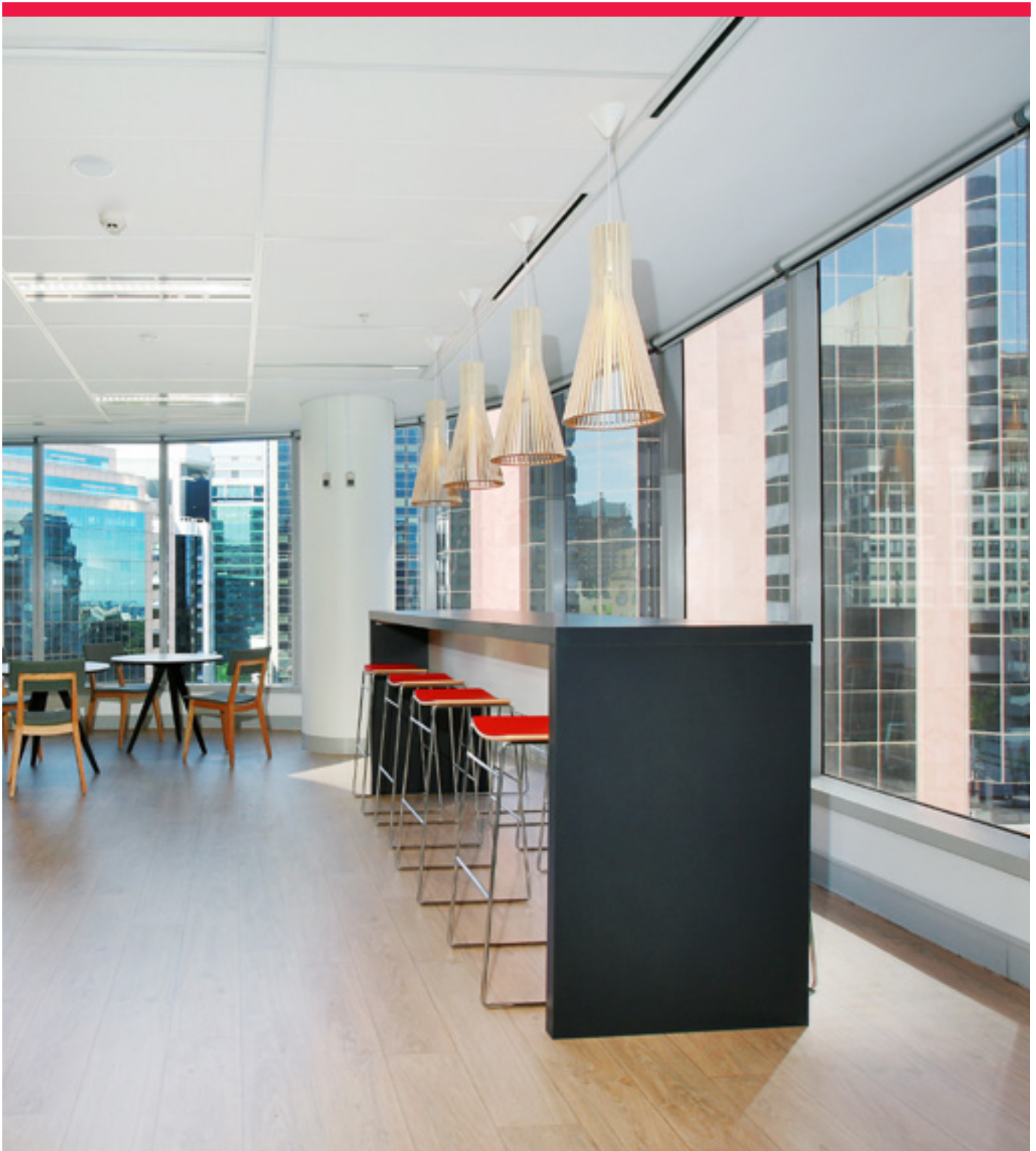
**SMALL OFFICE SUITES
OCTOBER 2015**





Over the past 12 months, we have witnessed a surge in demand for smaller (sub-500sqm) office suites in good quality B grade, and also A grade assets, which has facilitated solid effective rental growth through increasing face rentals and a compression in incentives.

So what are the drivers of this success story, and will it continue?

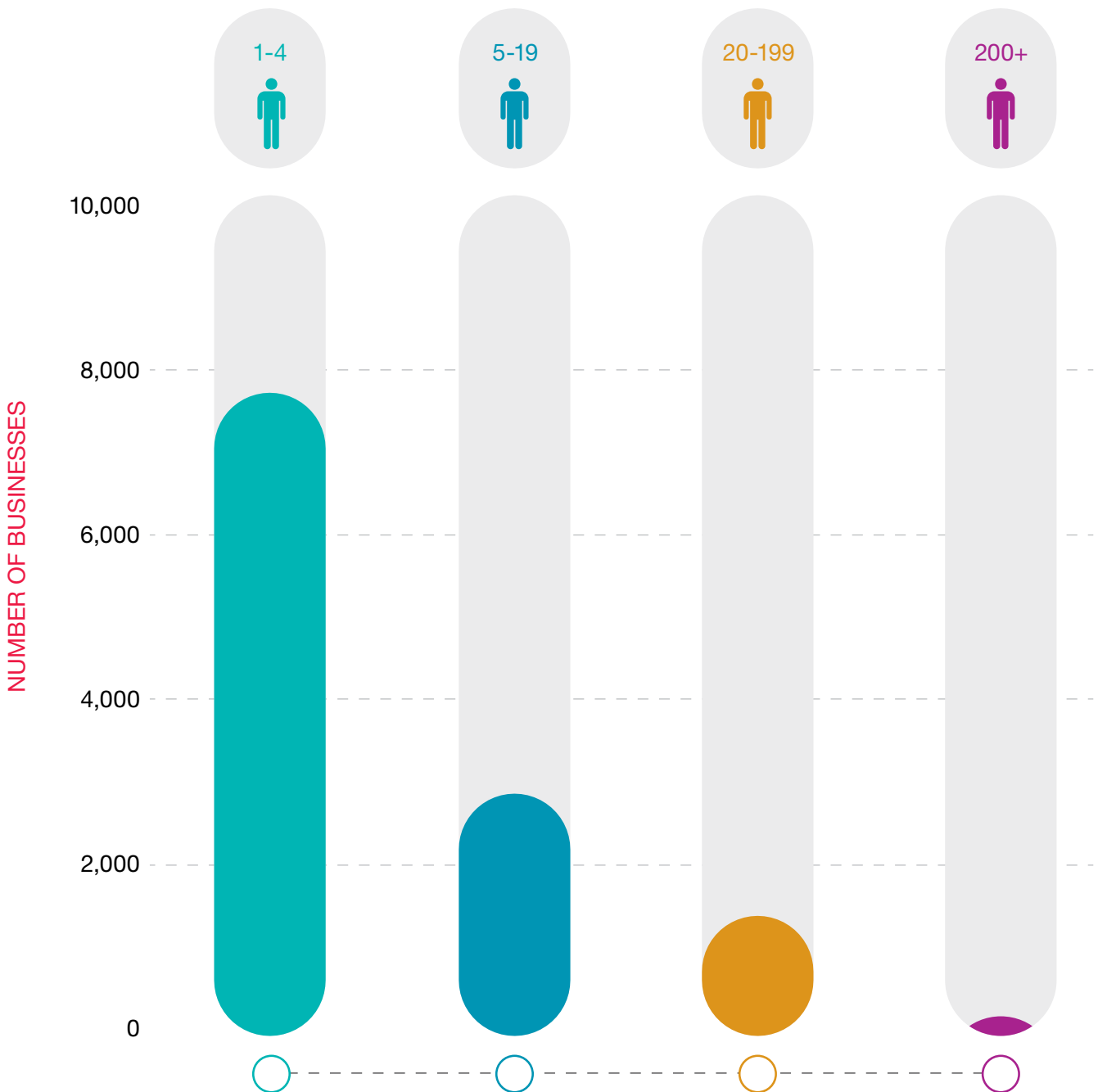


KEY DRIVERS

Demographic, technological and economic changes underpin the development and growth of small business, and thereby the demand for small suites. We have also witnessed an increase in the volume of private equity investors, and the rapid take up of crowd funding, creating available funds for new business startups which would historically have been viewed as risky by banking institutions and, as such, suppressed.

New business entrants into the Australian market are plentiful, particularly those of 1 to 4 employees, as shown below:

New business ventures over the past 12 months. Source: ABS





THE NATURE OF THIS DEMAND HAS LED TO A TRENDING DOWNWARDS OF THE AVERAGE PREMISES REQUIREMENT SIZE OVER RECENT YEARS, SPECIFICALLY WITHIN THE PAST 12 MONTHS. IN SYDNEY, THE GREATEST ACTIVITY HAS BEEN IN THE SUB-500SQM FITTED SUITES, AS DEMONSTRATED BY A VOLUME OF RECENT TRANSACTIONS INCLUDING THE FOLLOWING:

Street No.	Address	Lessee	Area (sqm)	Term (Yrs)	Gross Rental (\$/sqm pa)
33	York Street, Sydney	Zomato	541 sqm	1	\$395
45	Clarence Street, Sydney	AOL	392 sqm	4	\$766
55	Clarence Street, Sydney	Sons of Centaur Australia	230 sqm	5	\$795
55	Clarence Street, Sydney	Silverback MDM	214 sqm	4	\$665
55	Clarence Street, Sydney	Taiwan Trade Centre	155 sqm	5	\$795
191	Clarence Street, Sydney	Linkara Group	353 sqm	3	\$522
332	Kent Street, Sydney	Pin Point	352 sqm	3	\$640
201	Elizabeth Street, Sydney	PEJR Property Developments	538 sqm	5	\$850
204	Clarence Street, Sydney	EMF Griffiths	300 sqm	5	\$650
50	Bridge Street, Sydney	Allure Media	572 sqm	3	\$819
1	Macquarie Place, Sydney	Taurus Funds Management	454 sqm	10	\$1,667
1	Macquarie Place, Sydney	CLSA	162 sqm	2	\$1,567
77	King Street, Sydney	N1 Finance	304 sqm	5	\$780
77	King Street, Sydney	Instructure	350 sqm	5	\$780
37	Pitt Street, Sydney	Job Support	409 sqm	1.5	\$500
50	Bridge Street, Sydney	Pembroke Resources	160 sqm	3.5	\$954
50	Bridge Street, Sydney	ATF Development	179 sqm	3	\$1,194
123	Pitt Street, Sydney	EDG Capital	215 sqm	3	\$912
1	Macquarie Place, Sydney	Kingold	300 sqm	5	\$1,617
123	Pitt Street, Sydney	AFMA	410 sqm	6	\$992
210	George Street, Sydney	Fish Vision	150 sqm	3	\$550
1	Castlereagh Street, Sydney	Equity Partners	177 sqm	3	\$750
9	Hunter Street, Sydney	Broadbean Technology	218 sqm	3	\$695
14	Martin Place, Sydney	Donald Cant Watts Corke	275 sqm	5	\$820
16	Spring Street, Sydney	Sales Pond	306 sqm	3	\$725
16	Spring Street, Sydney	Engenius	306 sqm	3	\$680
210	George Street, Sydney	Institute of Public Accounting	315 sqm	5	\$620
309	George Street, Sydney	Xero Australia	325 sqm	3	\$680
32	Martin Place, Sydney	Maximum Legal	395 sqm	5	\$630

WILL THE DEMAND CONTINUE?

In our opinion, demand will remain strong for good quality fitted office suites into 2016. Whilst the wave of demand earlier in the year may have slowed slightly, it remains strong.

The economic environment is such that the establishment of small businesses is currently very much supported, and Sydney is the central hub for new business creation. According to Sydney Councillor, Angela Vithoulkas, 64% of Australia's tech startups are located in the City of Sydney area.

The City of Sydney has also issued its draft tech startup's action plan, and is promoting startup business through initiatives such as SydStart 2015 and Sydney Startup Week 2015.

Stone & Chalk, the Fintech incubator, was oversubscribed and had to take on additional floor space even before it opened, and we understand that the Tyro Payments incubator space at 155 Clarence Street is also a success.

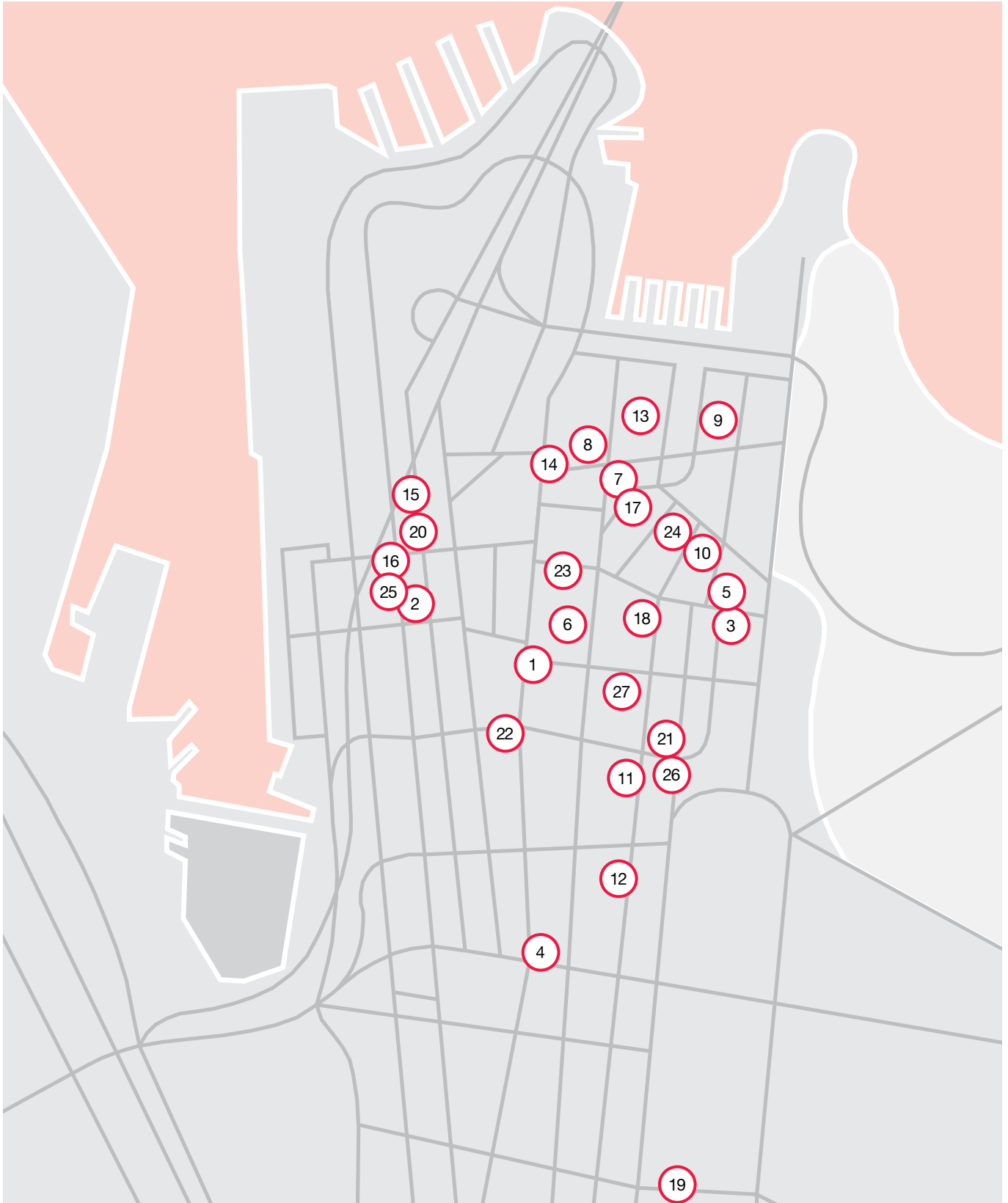
Of course, not all of these startups create immediate demand for office space, as many will start out life in Co-Working spaces. On this front, however, the news is also positive. Australia has more Co-Working space (per capita) than anywhere else in the world to cater for these startups, and as the businesses grow, there comes a point at which they need their own identity, the physical manifestation of which is their own office – generally a small suite to start out with.





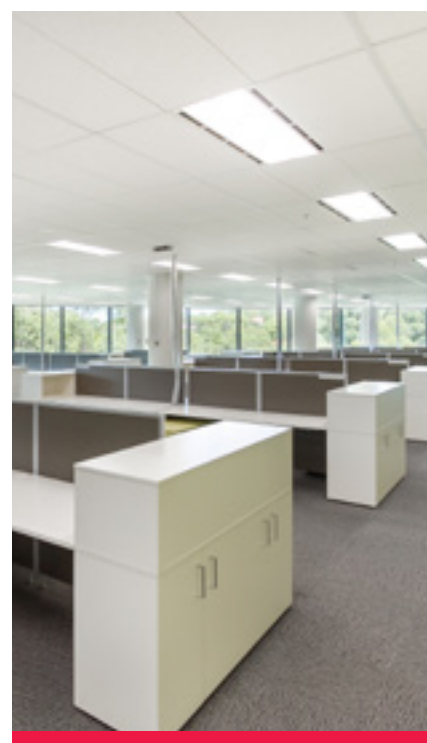
CURRENT SUPPLY

From a position earlier in 2015 where the supply of fitted small suites effectively 'dried up', many property owners have moved to sub-divide floors to take advantage of the evident demand. This has led to a plethora of options becoming available, and at the date of writing there are over 90 suites for lease, as shown below:



Legend as at October 2015

No.	Property	Address	No of suites available Sub-500 sqm
1	MLC Centre	19 Martin Place, Sydney	12
2	Metcentre	60 Margaret Street, Sydney	3
3	Deutsche Bank Place	126 Phillip Street, Sydney	2
4	Citigroup Centre	2 Park Street, Sydney	1
5	Aurora Place RBS Tower	88 Phillip Street, Sydney	9
6	Angel Place	123 Pitt Street, Sydney	2
7	Royal Exchange Building	56 Pitt Street, Sydney	5
8	Exchange Centre	20 Bridge Street, Sydney	2
9	AMP Centre	50 Bridge Street, Sydney	8
10	Chifley Tower	2 Chifley Square, Sydney	4
11	Skygarden	77 Castlereagh Street, Sydney	1
12	Piccadilly Tower	133 Castlereagh Street, Sydney	5
13	Gateway	1 Macquarie Place, Sydney	3
14	Exchange House	10 Bridge Street, Sydney	5
15	1 York Street	1 York Street, Sydney	1
16	One Margaret Street	1 Margaret Street, Sydney	2
17	Swire House	10 Spring Street, Sydney	2
18	City Freeholds House	15 Castlereagh Street, Sydney	5
19	175 Liverpool Street	175 Liverpool Street, Sydney	1
20	55 Clarence Street	55 Clarence Street, Sydney	3
21	75 Elizabeth Street	75 Elizabeth Street, Sydney	3
22	77 King Street	77 King Street, Sydney	1
23	9 Hunter Street	9 Hunter Street, Sydney	1
24	1 Bligh Street	1 Bligh Street, Sydney	1
25	45 Clarence Street	45 Clarence Street, Sydney	5
26	99 Elizabeth Street	99 Elizabeth Street, Sydney	2
27	United Overseas Bank House	32 Martin Place, Sydney	2





WHAT THE OCCUPIERS ARE LOOKING FOR

With the current breadth of competition, leasing small suites does need to be carefully considered in order to respond to occupier requirements. The occupiers we transact with are generally looking for the following key qualities:



- **Quality** – Good quality fitout;
- **Unique Space** – Increasingly, traditional base building finishes are viewed as dated. Tenants like unique or quirky spaces;
- **Scaleability** – Small businesses can expand swiftly and exponentially. 5 years ago LinkedIn occupied serviced office accommodation in Sydney! As such, the ability to expand is important;
- **Flexibility** – A flexible layout, and a willingness by the owner to alter the fitout to suit their exact requirements if necessary (although in our experience physical changes are rare);
- **Natural light** – Plentiful natural light flowing into the space;
- **Well maintained common areas** - including main lobbies, on floor circulation, WC's and end of trip facilities;
- **Speed** – A landlord who is able to move swiftly to conclude the transaction and facilitate business relocation as soon as possible. Often, small occupiers do not allow sufficient time to complete the transaction and relocation, and as such those owners who can react quickly are better placed to secure these tenants;
- **Advice & Information** - For many businesses, leasing a small suite may be their first ever commercial transaction, so high quality advice and accurate information provided by a leasing professional is key to the decision making process.



WHAT DOES THIS MEAN FOR OWNERS?

The shifting demand base and trending down of the average occupier space requirement has led many owners to re-think their leasing strategies for Sydney CBD office buildings.

The creation of fitted suites in buildings does involve a capital cost, and loss of NLA (net lettable area), and as smaller tenants tend to enter into shorter term leases there is a potential impact on the WALE (weighted average lease expiry) on the asset.

In our view, the high demand for suites experienced over the past 12 months is not a short term trend, it represents a fundamental shift in demand which is here to stay. Therefore, any owner of a good quality Sydney CBD asset with prolonged vacancy should consider a small suites strategy which will invariably lead to swift leasing of the space.

However, the strategy has to be carefully considered, and professional leasing advice based on market knowledge is key, as there are now more fitted small suites available than we have seen for over 18 months. This creates choice for occupiers, and competition for owners.

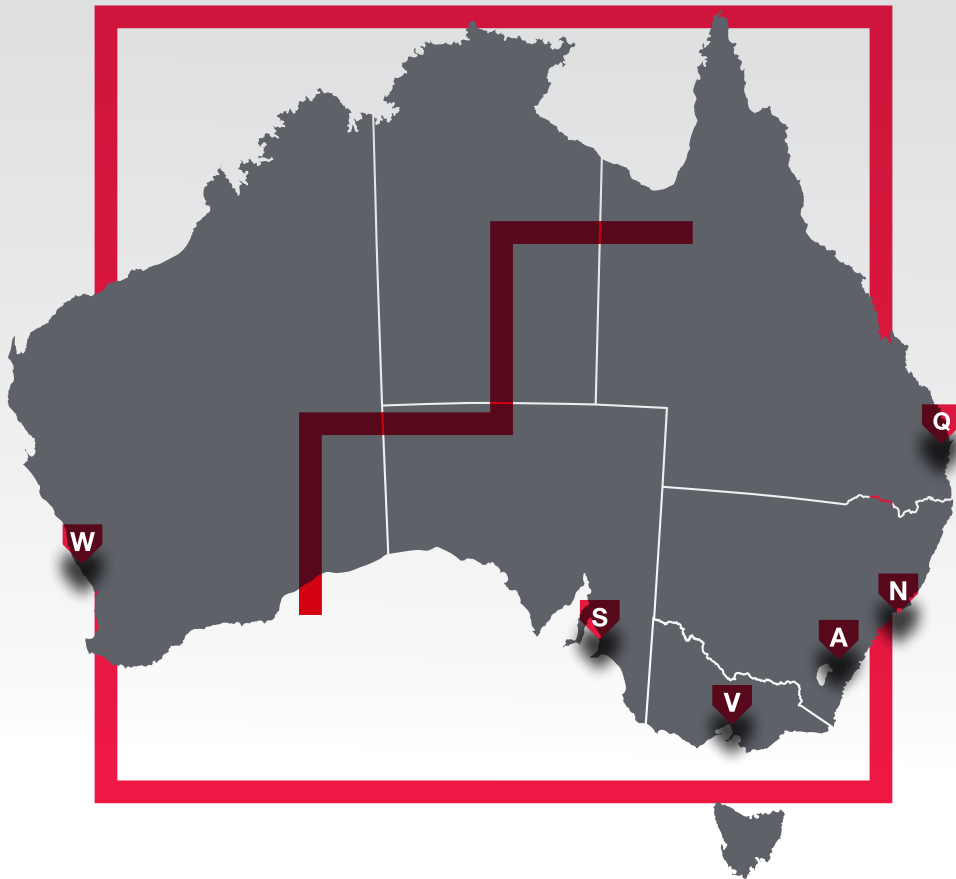
Remember that quality is key, and occupiers crave unique space. A suite with a below par base building finish, average common areas, and a cheap fitout, could sit vacant for some time. But a quirky building with a well designed and high quality fitout could lease in days.

Well advised owners will position themselves to lease space swiftly, and on good commercial terms which will more than offset capital expenditure and loss of NLA. Further, embracing a shorter WALE provides an opportunity to regularly take advantage of rental upswings.


KNIGHT FRANK IDENTIFIED THIS SECTOR OF DEMAND VERY EARLY, PREPARING OUR TEAM TO BE PROACTIVE AND ACHIEVE GREAT RESULTS FOR OUR CLIENTS. THROUGH BEING AHEAD OF THE CYCLE, AND PROVIDING GREAT ADVICE, WE HAVE CONCLUDED IN EXCESS OF 100 SUB-500 SQM TRANSACTIONS WITHIN THE PAST 12 MONTHS.


THROUGH THIS EXPERIENCE, WE HAVE A VALUABLE INSIGHT INTO THE DRIVERS OF SMALL BUSINESS AND THEIR PROPERTY REQUIREMENTS, AND AN EXPERT TEAM TO HARNESS THIS DEMAND.

WITH KNIGHT FRANK AT YOUR SIDE, YOU CAN BE SURE THAT YOUR SUITES WILL BE LEASED TO QUALITY OCCUPIERS IN THE SHORTEST POSSIBLE TIMEFRAME AND ON THE BEST COMMERCIAL TERMS.




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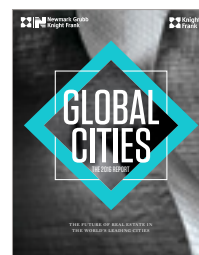
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