Office

September 2019

National Property Clock: Office

Entries coloured purple indicate positional change from last month.

Ballina/Byron Bay
Coffs Harbour
Dubbo
Illawarra

Melbourne
South East NSW
Sunshine Coast

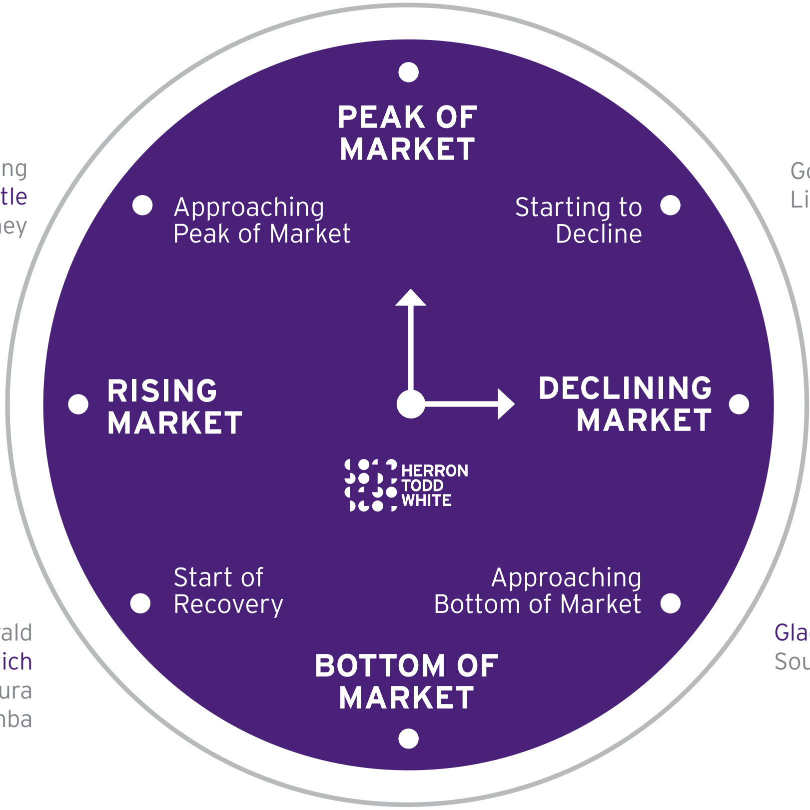
Geelong
Newcastle
Sydney

Gold Coast
Lismore

Mid North Coast

Ballarat

Alice Springs
Echuca



Adelaide
Brisbane
C'berra/ Q'beyan
Central Coast

Emerald
Ipswich
Mildura
Toowoomba

Gladstone
South West WA

Bundaberg
Cairns
Darwin
Hervey Bay
Hobart
Launceston

Mackay
Perth
Rockhampton
Townsville
Wide Bay

COMMERCIAL

HERRON TODD WHITE COMMERCIAL

New South Wales

Overview

The commercial sector has traditionally offered investors a way to boost yield in their portfolios, but as you'll see in our report, there are some surprises.

This month, we're taking a look at major transactions, both sales and leases, in office markets around the nation.

Quite a few of our major centres are seeing strong buyer demand for office space and this has translated into tight yields. Other localities are experiencing a struggle, which can spell opportunity for investors keen to purchase at the bottom of the cycle.

Sydney

The Sydney CBD office market has seen several big transactions so far in 2019 in both strata and freehold spaces.

The most significant transaction, at $800 million, was Dexus and its unlisted Dexus Wholesale Property Fund's purchase of GPT Group's half-share in the MLC Centre at 19-29 Martin Place. Dexus already owned fifty per cent of the property prior to this transaction and now with full control of the property, the transaction cements them as the largest office landlord in Australia. At 67 storeys, the MLC Centre was for many years the tallest office building in the country and the site remains one of the largest freehold sites within the Sydney CBD. There is also no questioning its prime location, set on the southern side of Martin Place within the primary city core precinct.

On a much smaller scale, the strata office market has seen a number of strong results, continuing to push square metre rates to unprecedented levels. Noonan Property's sale of Level 10 (398 square metres) of Heritage listed Culwalla Chambers, at 67-69 Castlereagh Street, achieved $6.395 million at auction, reflecting $16,068 per square metre of lettable area. A result such as this shows the continued strength of the office strata market, however the number of transactions does appear to have slowed.

On the leasing side, while there have been a number of large leases across the CBD, it is particularly worth noting the continued and growing presence of WeWork, who have recently signed a 12-year lease agreement over 11,000 square metres of office space across ten floors at 320 Pitt Street. This is WeWork's largest Australian lease to date and a reflection of the growing appeal of co-working space. WeWork has also fully secured 1 Sussex Street at Barangaroo, which will reach completion at the end of 2019 and is anticipated to open in early 2020. It's unclear what the impact of co-working space will have on the wider market, however it does present new options for tenants looking for more flexible options.

There are currently more than 20 hotels either under construction or approved for redevelopment.

RENT

3.7%

Vacancy rates across the CBD, reported as at July 2019 (PCA).

Vacancy rates remain very low across the CBD, reported at 3.7% as at July 2019 (PCA), down from 4.1% in January. Low vacancy continues to be driven by low supply which in turn continues to see above average rental growth. Supply was particularly hampered during the first half of 2019 by withdrawals outweighing supply, reflecting -23,400 square metres of net supply (PCA). A total of 32,039 square metres of office accommodation across eight sites was taken offline in the first half of 2019. Five of these sites are situated in the city core precinct.

New approvals for office accommodation are low across the CBD, with approvals being generally focused on residential and hotel redevelopment rather than traditional office space. As an example, there are currently more than 20 hotels either under construction or approved for redevelopment. That said, there is new office supply on the horizon, however the majority of this will not come online until 2020 or 2021.

For the time being, CBD rents are anticipated to remain strong, although will likely moderate, until supply catches up to demand and values are likely to remain strong for good quality stock.

Newcastle

Office investment activity in Newcastle has been fairly subdued over the past 12 months. That was until the headline grabbing sale of 18 Honeysuckle Drive, Newcastle to IOOF Investment Management Ltd for a reported sum of $52.2 million of course. A record for office property in the city, Colliers International describes the property as:

"an A Grade, seven-level commercial building completed in 2017 that provides investors with a top tier asset featuring outstanding investment credentials. The 6,524 square metre building is 100% leased to a diverse list of corporate and Government tenants."

And it is well-positioned in the prominent Honeysuckle harbour front precinct of the Newcastle CBD.

The property was designed to meet a 4.5-star NABERS energy rating and was awarded a 5-Star Green Star rating. It provides purchasers with a passive asset featuring low forecast capex and numerous high quality attributes.

A modern CBD office building of 6,524 square metres, it was completed in 2017 and is 100% leased with WALE of 6.8 years, with a net passing income of $3,235,354 excluding GST underpinned by seven top tier tenants including the NSW Government and a variety of corporate businesses.

The sale reflects an approximate yield of 6.2% and reflects the continuance of low yields for well positioned and occupied investment stock in the current market. A-grade vacancy remains at historic lows and with major office developments around the Wickham transport interchange being built fully or majority pre-committed, this vacancy rate will remain low for some time.

Wollongong

Sales transactions in the office sector have slowed over the past 12 months mirroring the trend of the broader commercial real estate market across regional New South Wales.

The slowdown is coming at the end of a very buoyant three years where record sales prices were achieved resulting in yield compression across the board. This is exemplified by the sale of 90 Crown Street, Wollongong in late 2018 for $50.38 million showing an initial passing yield of 7.75% on a WALE of 3.5 years.

The slowdown in investment sales over the past year is attributed to several factors including the Banking Royal Commission, state and federal elections, volatility in the global markets, downturn in the housing market and just the normal market cycle. There is optimism that recent interest rate cuts will spur activity with most participants keenly watching to see if this will result in further yield compression in the sector or if there will be a more permanent re-assessment of risk despite lower borrowing costs.

$400-$450

per square metre for A-Grade gross face rents in Wollongong CBD.

During this period of low and reducing interest rates, owner-occupiers have remained relatively active in the sub-$1.5 million price category, however the limited availability of such properties particularly in the Wollongong CBD has seen owner-occupiers look further afield to the region's other major centres including Corrimal, Fairy Meadow, Dapto and Shellharbour.

Local agents are reporting a healthy level of enquiry for office space in quality, well placed buildings with MMJ securing several tenants for the recently refurbished 6-8 Regent Street, while Knight Frank has secured Aon Corporation on a new lease in the Corporate Square building on Burelli Street. Gross face rents in the Wollongong CBD generally sit in the order of $400 to $450 per square metre for A-grade and $350 to $395 per square metre for better quality B-grade stock in the CBD.

Lismore

The office market has traditionally returned one per cent to 1.5 per cent higher yield than retail on the New South Wales north coast. This is no longer the case given the superior strength in the office rental market in comparison to the weaker retail market (with the exception of Byron Bay).

Notable sales in New South Wales north coast locations for leased investment product include:

- **River Street, Ballina, NSW** for $780,000 (6.37%, $3,959 per square metre);
- **River Street, Ballina** under contract for $1.425 million (purchased on 7.5% yield, $4,095 per square metre);
- **Woodlark Street, Lismore** (1 February 2019) for $1.11 million (7.25%, $2,662 per square metre);
- **Molesworth Street, Lismore** (1 April 2019) for $190,000 (6.29%, $1,210 per square metre).

We are also aware of a recent significant transaction in Byron Bay comprising a strata office space. As is common, Byron Bay sets its own market with this being purchased for $3.5 million for owner-occupation, indicating $7,322 per square metre.

Owner-occupiers are active in the office market with two mixed use developments near completion in Lennox Head and Ballina selling strata office units off the plan reportedly all to owner-occupiers across a broad price range as low as $313,000 and up to $979,000, with rates per square metre showing $5,300 to $6,800. Because there is limited supply of this type of product in the locality, agents reported strong demand with more potential purchasers than product available.

A notable increase in value has been observed in the newly developed Habitat in Byron Bay, a mixed use live-work development which comprises units with 20 square metres of ground floor commercial space or home-office with the balance being residential. The units sold in 2016 off the plan for $650,000 each with two recent resales at $820,000 and $850,000.

Habitat, Byron Bay Source: realcommercial.com.au

The rental market across most areas of the north coast has remained relatively steady with broadly a balanced market except for Lismore which is generally weaker with increasing supply although rents are still holding.

Coffs Harbour

The office market has remained relatively stable during 2019. The market for leasing appears to have remained stable with supply and demand issues broadly balanced which has resulted in rents remaining stable.

Good quality office space is leased at $350 to $400 per square metre per annum. Specialist medical tends to command a premium above this with examples of $400 to $500 per square metre occurring. Secondary office accommodation tends to be more difficult to lease with rentals in the vicinity of $200 to $300 per square metre depending on size, quality and location.

The direction of yields tends to be stable with ultimately the strength of the tenant and lease term driving the yield. The traditional variation between retail and office markets (one per cent to 1.5 per cent in favour of retail) is no longer as evident as it once was.

The retail sector is currently experiencing higher vacancy and the longer lease-up periods are impacting value and saleability.

The office market appears the more stable at this time and into the future the yield trend between office and retail maybe reversed.

Orange/Dubbo

A recent upper end market sale was a commercial property at 129 -131 Byng Street, Orange for $6,062,500. The property was leased to a NGO agency on a ten plus five plus five year term commencing November 2018. The analysed yield was 6.94%. The building is the former two-level 1874 constructed Railway Hotel, now refurbished throughout for office use, extended to 1,569 square metres and fitted with a lift. The sale price equates to $3,864 per NLA and gross rent equates to $306 per square metre.

129 -131 Byng Street, Orange Source: realcommercial.com.au

In Dubbo, a number of sites have been procured for redevelopment for intended office or mixed use. These include the sale of 102-108 Macquarie for $2.25 million, a 2,517 square metre site on Dubbo's main shopping strip, for redevelopment into a six-storey business hub and the recently developed 1,076 square metre Brisbane two-storey office complex now on the market at rents of circa $320 per square metre.

Victoria

Melbourne

According to the Property Council of Australia's Office Market Report, Melbourne CBD's office overall vacancy rate has increased slightly by 0.1% as of July 2019. Melbourne CBD continued to record the lowest vacancy rate amongst all of Australia's CBDs at 3.3%, in front of Sydney CBD at 3.7%.

Tenant demand is continuing to rise in the city fringe. According to online research reports, the office leasing market within the city fringe and inner east was strong over the past 12 months. Tenants, especially from the creative, technology and business service sectors, actively compete for well-located high-quality office accommodation. Vacancy rates in the city fringe, inner east and outer east are well below long term average vacancy levels. The vacancy rate in the inner east fell to 3.58%, making it the lowest vacancy rate of all of Melbourne's metro precincts. The CBD's increasing rent level is creating greater demand in city fringe locations as tenants seek cheaper alternatives.

Incentives are currently broadly ranging from circa 10% to 25% net depending on the tenancy size, lease term and location. In the south-eastern and outer-eastern markets where vacancy rates are high, incentives are at their highest whilst in the city fringe and inner eastern markets, incentives are at their lowest.

There has been strong capital growth for commercial development sites in Cremorne and Richmond over the past two years, particularly within the past 18 months. Larger development

37 and 39-41 Little Collins Street Source: realcommercial.com.au

sites above 1,000 square metres are in high demand in the current market as they allow greater development scale as opposed to smaller sites. Record high land rates have resulted in Cremorne and Richmond this year with a number of development sites selling for land rates in excess of $13,000 per square metre. However, we highlight that the development market in these areas is considered to be at the peak.

Buyer demand is still solid for CBD, city fringe and suburban well-located sub-$50 million investment commercial assets. Properties in this price range are keenly sought by higher net worth private investors, syndicates and overseas investors. For instance, two adjoining properties at 37 and 39-41 Little Collins Street in the CBD were sold at a strongly contested auction conducted by Colliers International in June 2019. 37 Little Collins Street, a double storey fully refurbished period building which is leased to Bar Lourinha, was sold for $5.85 million, reflecting a passing net yield of 2.2% while 39-41 Little Collins Street, which has three street frontages and is improved with a circa 1919 three storey hospitality and office building, was sold for $16.5 million, representing a passing net yield of 1.1%. Both properties were sold significantly above the reserve prices to businessman Rob Phillpot, the co-founder of Aconex.

In the suburban office market, a local private investor purchased 19-23 Prospect Street, Box Hill in March for $21.6 million, reflecting an analysed market yield of approximately 6.3%. The property comprises a circa 1988 five-storey office building including two levels of basement parking and a total net lettable area of 4,275 square metres. Investment yields within the inner city are being influenced by the underlying land values of the properties. Land rich assets usually reflect lower yields compared to investment assets which have been fully developed.

The office leasing market within the city fringe and inner east was strong over the past 12 months.

Queensland

Brisbane

For a number of years, the performance of the Brisbane office market has been underwhelming, to say the least, and has lagged behind the broader Brisbane commercial markets.

Stubbornly high vacancy rates due to constant supply additions and patchy conditions across key industries resulting in an ongoing competitive leasing market and limited rental growth have been key factors as to why the office market has been sluggish virtually since the GFC.

Brisbane is however currently undergoing a major transformation with a number of significant infrastructure projects that have either recently been completed or are currently under construction. These projects, coupled with the low interest rate environment, are having a positive impact on the CBD and fringe CBD leasing markets and are seeing increasing appetite from investors, both on a private and an institutional level.

Recent vacancy statistics released by the Property Council of Australia (PCA) have indicated that the overall Brisbane CBD vacancy rate compressed further in July 2019 to 11.9%, which is its lowest rate since January 2013. Furthermore, the overall Brisbane fringe CBD market also reduced to 13.8%, its lowest since January 2017. Vacancies for prime grade CBD accommodation are now below 9% and more tellingly, there is no sub-lease space now available in these properties. A-grade vacancies in fringe areas have also dropped markedly from 16.7% to 12.7% over the past six months.

Brisbane is however currently undergoing a major transformation.

Given the improving leasing markets, it is likely we will see gross face rents stabilise for prime and A-grade office accommodation in the CBD and fringe CBD. Stronger performing precincts such as King Street and Ann Street (Fortitude Valley), Gas Works precinct (Newstead), South Brisbane and the Golden Triangle (Brisbane CBD) are likely to see rental growth over the remainder of the year for modern quality developments. We may also (finally!) see incentives start to fall.

The positive vibe coming out of Brisbane is now starting to translate into a number of strong investment transactions and the opportunity and appetite for re-positioning underperforming commercial office assets is on the rise.

Notable recent re-positioning transactions in Brisbane include:

8 Gardner Cl, Milton

Sale Date	Sale Price	Lettable Area (m2)	WALE/ Lease Term Certain	Analysed Market Yield (%)	$/m2 Lettable Area
Jun 2019	$25.23M	4,271	5.22 yrs	6.87%	$5,907
Aug 2017	$10.625M	4.271	1.18 yrs	10.95%	$2,488

The property is a modern style, four level, multi-tenanted commercial office building situated in Milton.

8 Gardner Cl, Milton   Source: realcommercial.com.au

The building was largely vacant (approximately 75%) in 2017 when it was acquired by Quintessential Equity Pty Ltd. The asset was re-positioned by undertaking a number of building modifications and upgrades in order to revitalise the property in line with market expectations and undertake a new leasing campaign.

At the commencement of 2019, the building was 100% leased, reflecting a steady cash flow and solid WALE.

164 Grey St, Southbank

Sale Date	Sale Price	Lettable Area (m2)	WALE/ Lease Term Certain	Analysed Market Yield (%)	$/m2 Lettable Area
Jul 2019	$44.65M	3,115	7.1 yrs	5.30%	$14,334
Jan 2016	$30.30M	3,065	1.4 yrs	6.50%	$9.886

This property is a modern style, four level, multi-tenanted mixed use commercial building situated at Southbank.

164 Grey St, Southbank Source: commercialrealestate.com.au

The building was acquired by Marquette who fully upgraded the building services, created a new office lobby and building entry and increased the lettable area by adding an additional retail tenancy. The building was fully re-leased, securing long term tenants and strengthening its overall cash flow position.

The property was recently sold reflecting a strong yield which was underpinned by the strong cash flow position of the asset and its prime location.

These two sales are a stark contrast of how a fully leased commercial office asset with good cash flow fundamentals will perform versus assets that are largely vacant with significant cash flow risk. We are seeing an increase in appetite for value-add commercial office assets that are well located.

The near-term outlook for the Brisbane office market appears positive .

The market generally has been active over the past 12 months with notable transactions (see table below).

Selling agents are reporting that demand is also increasing for underperforming, older style office assets that can be re-positioned and re-let.

The near-term outlook for the Brisbane office market appears positive and it is possible that further yield compression may occur should interest rates decline further. Furthermore, the yield spread between Brisbane and its southern counterparts (Sydney and Melbourne) is still significant and the coming infrastructure projects are likely to increase Brisbane's attraction as an investment destination.

Other Notable Investment Sales	Sale Date	Sale Price	Lettable Area (m2)	WALE/ Lease Term Certain	Analysed Market Yield (%)	$/m2 Lettable Area
CBD						
201 Charlotte St, Brisbane	Apr 2019	$126.7M	13,291	5.1 yrs	5.90%	$9,533
133 Mary St, Brisbane	Mar 2019	$96.5M	12,976	2.7 yrs	6.02%	$7,437
61 Mary St, Brisbane	Nov 2018	$275M	28,749	10.4 yrs	5.95%	$9,566
CBD Fringe & Inner City						
381 Macarthur Ave, Hamilton	Apr 2019	$19.73M	2,825	5.12 yrs	6.58%	$6,984
19 Corporate Dr, Cannon Hill	May 2019	$35.05M	6,028	2.91 yrs	7.32%	$5,814
Building 2, 747 Lytton Rd, Murarrie	Jun 2019	$17.26M	3,346	3.12 yrs	6.98%	$5,158

Gold Coast

Agents report that conditions within the Gold Coast office market have been slowing for a while now. Exacerbating this sentiment in 2019 to date was the Royal Commission into misconduct in the banking, superannuation and financial services industry and the federal government election campaign. However after a marketplace hiatus over this period (February to May) the impact of these events seems to have well and truly passed and business appears to have moved back into normal mode once again.

Continuation of the low interest rate environment, with rates reducing yet again, is certainly a positive for the market place in a general sense.

To date in 2019, we have seen settlement of several sizeable office building transactions. These include:

- **In January:** 130 Bundall Road, Bundall. 3,682 square metre lettable area on a 2,226 square metre site at $11 million (source: CoreLogic). 70% occupied and reflecting a WALE of 2.16 years (by income). Passing yield circa 5.43%. Analysed yield 7.34% (with 7.5% PVA). $2,988 per square metre on floor area. Owner-occupier buyer.
- **In March:** Lakeside 1, Bermuda Point, Lot 1101/1 Lake Orr Drive, Varsity Lakes. 6,114 square metres lettable area on a 7,916 square metre site at $25.1 million (source: CoreLogic). Reported as circa 96% occupied and returning a net passing income in the order of $2.285 million. Based on these metrics, passing yield would be in the order of 9% with a lettable floor area rate of circa $4,105 per square metre, although we consider the passing rental level full.
- **In May:** 169 Varsity Parade, Varsity Lakes. 3,364 square metres lettable area on a 13,000 square metre site at $14 million (source: CoreLogic). Fully leased and reflecting an

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estimated WALE of 1.38 years (by income). Passing yield circa 8.73%. Analysed yield 6.85% (with 5% PVA). $4,172 per square metre on floor area. Considered a future residential redevelopment site.

- **In August:** Confidential. Circa 2,500 square metres lettable area U/C exceeding $8 million. 95% occupied and reflecting a WALE of 1.5 years (by income). Will reflect a passing yield of circa 7.6%.

Several other larger office buildings have also been put to the market place. All have drawn interest from prospective buyers. Based on bone fide offers received, interest in the Gold Coast office sector would appear to be holding firm, although our observation is that yields may be softening slightly, to analysed yields ranging from 7.25% to 8%.

Supply of larger office floor space (1,000 square metres plus) has been hampered on the Gold Coast for some time now due in the main to no new office buildings being developed.

Acuity Business Park at Robina is under construction with anticipated completion in mid 2020. The development will comprise two buildings of three storeys above basement car parking. Stage 1 (5,937 square metres LFA) reportedly has a substantial pre lease commitment. Stage 2 (3,627 square metres) is available. Rental rates are in the order of $460 to $470 per square metre per annum gross plus car parking at $150 per bay per calendar month.

The Ivy Pearce Building at Bilinga adjoining the Gold Coast Airport is a three year old, A-grade office building at the southern end of the Gold Coast. The dominant tenant is the Australian Federal Police. There is available office space between 480 and 1,014 square metres. Asking rental is in the order of $350 per square metre per annum net plus outgoings of $75 per square metre. Car parking is extra.

Ivy Pearce Building Source: realcommercial.com.au

The lack of new buildings has attracted entrepreneurial investors to older buildings in the Gold Coast's older established office precincts such as Southport, Bundall and Surfers Paradise. Buildings such as 7-11 Short Street, Southport and 130 and 132 Bundall Road, Bundall are good examples of refurbishment drawing tenants looking to move from C-grade floor space into B- or A-grade buildings. They are attracted by the affordable rentals that would typically range from $325 to $400 per square metre per annum gross plus extra for car parking.

50 Cavill Avenue, Surfers Paradise, which underwent a major refurbishment several years ago, has had the top floor recently lease at $450 per square metre per annum net plus outgoings of $120 per square metre. Car parking is extra at $150 to $175 per bay per calendar month. This level of rental is reflective of the upper range for Gold Coast office space, being surpassed only by the likes of the Oracle at Broadbeach where rates up to $600 per square metre per annum gross are achieved.

VACANCY

12.9%

total vacancy factor for the **Gold Coast** July 2019

The Property Council of Australia July 2019 Office Market Report indicates a total vacancy factor for the Gold Coast of 12.9%. This is up from 11.6% in their January 2019 report. Leasing agents had noted a tougher first half for 2019, but expect the second half to be better. Further, the negative net absorption of -6,850 square metres is attributed to businesses consolidating into smaller premises, etc.

Overall, we consider the increased level in the Gold Coast vacancy factor may dampen some investors' views of the Gold Coast office sector, with the result being solidification of slightly higher yields, but on the positive side of the ledger, rental rates appear to be achieving moderate gains. So all in all, the bottom line is likely to be retention of asset value levels over the remainder of 2019.


Acuity Business Park, Robina Source: Acuity Business Park

Sunshine Coast

The office market on the Sunshine Coast has continued to remain relatively stable during 2019.

One of the big questions has been, "What will be the effects be of the large supply of which entered the market during 2018?"

The answer to this has generally been a reduction in rentals for tenants, though in prime locations and A-grade stock, that reduction has been lower than the remainder of the market. We have seen significant incentives for vacant space, though overall reductions in market reviews for existing tenants are not as significant. One of the reasons for this is likely the high costs associated with moving work spaces for the majority of tenants with over 150 square metres of space. As a result, we have continued to see sales of existing offices in the market.

Sales of note include:

- **1-5 Plaza Parade, Maroochydore** comprises a mix use, two level, lifted complex comprising six tenancy areas and a NLA of 1003 square metres. The property sold in April 2019 for $3.65 million indicating a yield of circa 7.2% on the reported net income with a reported WALE of 1.65 years and $3639 per square metre.
- **72 Simpson Street, Beerwah** comprising a strata-titled mainly medical style centre across a single level. The complex has nine separate lots though is split into four tenancy areas only. It sold in March 2019 for $3.6 million indicating a yield of circa 7.5% with a reported WALE of 2.58 years and $5128 per square metre.
- **17 Wyreema Terrace, Caloundra** comprises a semi modern, two-level walk up stand-alone complex of 253 square metres. The property sold in vacant possession to an intending owner occupier in March 2019 for $1.25 million indicating a value of $4941 square metre.
- **4/77 The Esplanade, Mooloolaba** is a 227 square metre strata within a refurbished, lifted office complex with good views over Mooloolaba Beach. This property was purchased by the sitting tenant in March 2019 for $1 million indicating a value of $4405 square metre.

These sales indicate that the market is still liquid for a range of holdings. The owner-occupier market is still dominating sales up to $1.5 million with owners looking to secure high quality space generally above $4000 per square metre with lower quality space typically in the $3000 to $4000 per square metre range.

Investors are looking for multi-tenanted holdings to spread overall cash flow risk in this market, which has high vacancy, with sales typically being seen in the seven to eight per cent range depending on WALE, quality of complex, location and redevelopment potential.

We have not seen a higher end sale over $5 million in the office space to date in 2019, though there has not been stock available to the market in this range.

The next influx of supply is due to enter the market during the early months of 2020 with the first building within SunCentral due to be completed at that time with construction recently commenced.

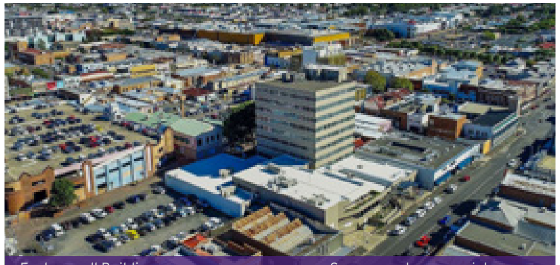
Toowoomba

Leasing demand for commercial office accommodation in Toowoomba continues to be subdued. As a result there has not been significant growth in rentals with evidence that some lease incentives may be required to secure tenants.

Owner-occupier demand continues to be strong, particularly for premises with floor areas of up to 300 square. There has been a reduced supply in this market segment, which has resulted in some sales achieving premium prices.

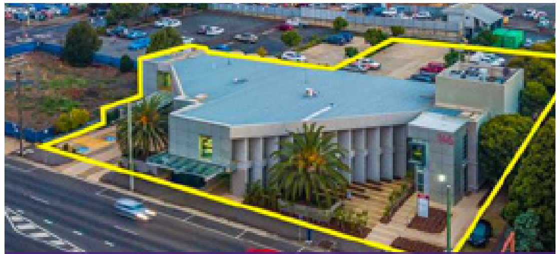
There have been a number of major investment sales in 2019 following many years of limited activity. The sales of note include the following:

- **Easternwell Building – 10 Russell Street, Toowoomba City** – This is a nine level office building with a net lettable area of 7,126 square metres and 101 on-site car parks. Major tenants include Easternwell Group, Southern Cross Austereo, Neato Employment and two state government tenants. There were a number of vacant tenancies and leases with short remaining lease terms. The WALE is 2.4 years and sale price was $10.5 million with a passing net yield of circa 12%.



Easternwell Building Source: realcommercial.com.au

- **146 Herries Street, Toowoomba City** – This is a two level building with a net lettable area of 1,615 square metres and 60 on-site car parks. The building was fully leased to two government tenants. Sale price was circa $7.4 million with a passing net yield of circa 8%.



146 Herries Street, Toowoomba City Source: realcommercial.com.au

- **70 Neil Street, Toowoomba City** - This is a single level building with a net lettable area of 948 square metres and 26 on-site car parks. The building was fully leased to a legal firm and Darling Downs Radiology . Sale price was $4.65 million with a passing yield of circa 7%.

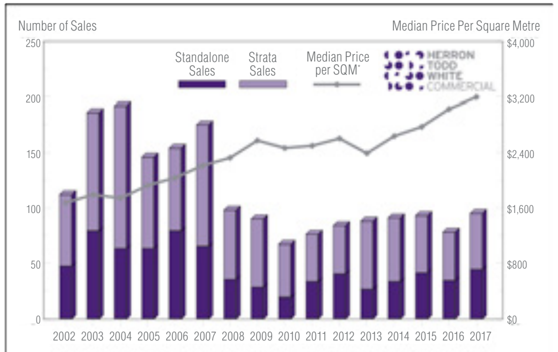
70 Neil Street, Toowoomba City Source: realcommercial.com.au

Cairns

The Cairns office market is relatively shallow and experiences limited sales activity. The market has also experienced limited new development, with the last very large office building constructed in Cairns being the state government office tower completed in 2010.

The level of general commercial property sales in Cairns, inclusive of retail and commercial office premises, highlights that activity in the Cairns commercial market remains well below the levels achieved in the 2003 to 2007 period. Sales volumes have been gradually rebuilding over the past nine years, but are still only averaging around 90 to 100 sales per annum. Median prices paid specifically for strata titled premises have increased mildly over the past seven years, but our general impression is that prices per square metre of floor area are mostly stable within the $2,500 to $4,500 range.

Commercial Property Sales in Cairns



* For strata sales only
Source: HTW Analysis of RP Data

Most new office space leasing demand is for smaller areas and for modern, good quality green star rated premises, however there is only a handful of such buildings in Cairns. These buildings achieve high levels of occupancy and are experiencing stable rent levels typically of $350 to $450 per square metre per annum. Demand for lesser quality space remains limited and there is a large oversupply of good quality non-inner CBD and well exposed secondary space in the $200 to $300 per square metre per annum rental range. These conditions have placed downward pressure on secondary rents and have seen the emergence of incentives.

The most recent sale of a large office building was the design and construct of the new Ergon premises in Bunda Street, Cairns City. The property sold for $14.7 million in May 2019 providing an analysed yield of 6.4%. The building comprised two levels of high quality office with a total area of 2,400 square meters, 68 car parks and an initial ten year lease term.

Townsville

The biggest office transaction to have occurred in the Townsville market over the past 12 months was for a nine-level CBD office building constructed in 2013 and leased to blue chip tenant Ergon Energy with National Australia Bank occupying the ground floor. The property sold in December 2018 for $63.5 million with a passing yield of 7.3% and weighted average lease expiry of 9.6 years. This is the biggest office transaction to have occurred in the Townsville market.

We are currently seeing a CBD office building that was acquired fully vacant undergoing a major redevelopment including external façade upgrades and internal upgrades, with the building being rebranded Precinct 21. The refurbishment is reportedly at a cost of $10 million and will offer five levels of commercial office space.

We are also seeing construction well underway of a new 4,000 square metre, four-level office building in the fringe City Centre Central development. This is a purpose-built building to be wholly occupied by the Australian Taxation Office from 2020 on a ten-year lease plus options. The property is currently being marketed for sale via expressions of interest. The completion of this building and the relocation of the ATO from its current tenancy will likely see a large amount of quality office space come onto the leasing market. The current depth of the local private sector is unlikely to be able to absorb this space based on the current environment.

Rockhampton

The office market in Rockhampton has stabilised, however remains relatively flat. There have been no major office developments in the CBD since the completion of the NAB building in 2012, however there is still a significant vacancy rate and until existing vacancies are absorbed across the CBD, it is unlikely we will see any other major office developments in the immediate term.

We note that the Council has recently let the contract for the construction of a new art gallery in the CBD on a 2,800 square metre site. It will require the demolition of existing office buildings which provide about 3,000 to 4,000 square metres of office space.

$225-$300
office rentals per square metre within the Rockhampton CBD

$300+
office rentals per square metre for prime office tenancies

Rentals have been relatively stable over the past 12 to 24 months, however leases that were negotiated some five to ten years ago that are coming to an end are seeing some re-negotiations as the previous rentals are now considered above market. Generally speaking, office rentals within the Rockhampton CBD have been ranging from about $225 to $300 per square metre gross. Rentals above $300 per square metre gross are for prime office tenancies only.

There have been no recent major transactions of office buildings. The most recent was the sale of the NAB building which transacted in 2016 for $9.35 million. Owner-occupiers remain fairly active in the market, with most activity in the sub-$1 million price bracket. Vacant office buildings have been very thinly traded above the $1 million price bracket in recent years.

With multiple infrastructure projects commencing and in the pipeline, things are looking positive for the office market in Rockhampton in the short to medium term.

Gladstone

Office conditions in Gladstone have seen some not so positive years, however conditions are now considered to have stabilised. Whilst there are still vacancies to be filled, we have seen some new rentals in the CBD negotiated in the past six to 12 months that fall within the low to mid-$300 per square metre gross, which is a positive sign for this sector. Notwithstanding this, we consider the market remains volatile and rentals at this level are difficult for landlords to achieve.

The market is still recovering from years of increasing vacancies and downward pressure on rentals. Due to the existing vacancies, there are no known major office developments in the pipeline to report on, and until such time as vacancies are absorbed, we are unlikely to see any new major office developments. There have been no known major transactions of office properties in recent years, however more recently we have seen some investment activity at lower price brackets.

Most recently, a strata office unit at 174 Goondoon Street sold for $1 million, reflecting a yield of about 9%. The property had a WALE of 2.88 years. Other activity for office properties has predominantly been in the sub-$1 million price bracket.

Wide Bay

The Wide Bay commercial office market has remained stable with a balance of supply and demand for an extended period.

Notable office developments include The Avenue at Hervey Bay. This development will comprise a community titled walk up office complex in a prominent business location of Hervey Bay.

Office sales within the Wide Bay are typically reflecting yields of 7.5% for good quality buildings in prominent locations with good quality tenants on long-term leases to 9% for lesser quality buildings in secondary locations with lesser quality tenants on shorter leases.

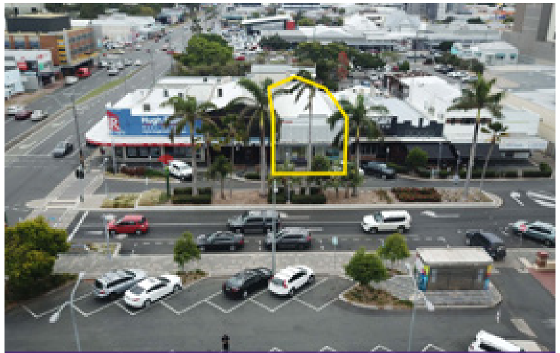
Gross rental growth prospects in the short term appear to be limited, with the market expected to remain well balanced over the short term.

Mackay

There is very little leasing activity within the office sector in Mackay. The market remains fairly subdued. Some office users around the city have reduced their tenancy areas.

Sales activity has been limited to the more affordable end of the market at less than $550,000 and comprise:

- An older office property at 92 Wood Street, Mackay City was recently sold by receivers at $505,000 with land area of 365 square metres and net lettable area of 323 square metres. This property was sold after an extended marketing period in vacant possession.



92 Wood Street, Mackay City Source: realcommercial.com.au

17 Shakespeare Street, East Mackay Source: realcommercial.com.au

- An office property at 17 Shakespeare Street, East Mackay sold with vacant possession at $545,000. It comprises a 1,642 square metre aggregation of two adjoining lots in a residential area and is improved with an older style, single level, brick building with reported area of approximately 400 square metres. It had been used by a community organisation and has been acquired by a medical services provider. The sale price is well below replacement cost.

We are also aware of a sale contract over another vacant possession property at 14 Grendon Street, North Mackay. This is an older style house which has been converted for use as a medical practice.

We have noticed an increased level of demand for office space over the past couple of years from community, disability and medical service providers.

Unfortunately, the relatively high combined cost of local authority rates and building insurance premiums is eroding investment returns and investor demand for office property in Mackay.

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South Australia

Adelaide

Adelaide's office market continues its solid performance with vacancy rates dropping to their lowest level in over four years. Interest rates remained unchanged in the RBA's August meeting with the cash rate now just 1%, as Governor Philip Lowe noted that economic growth has been lower than expected over the first half of 2019.

In our previous office market update, Adelaide CBD total vacancies were recorded at 14.2%, whereas now, according to statistics published by the Property Council of Australia, CBD vacancies measure just 12.8%. Adelaide's fringe office market, which encompasses the arterial roads of Greenhill Road to the south of the city and Fullarton Road and Dequetteville Terrace to the east, has recorded vacancies of 13.1%, a slight increase since our last update in June. This reflects the desire of tenants to base themselves within the CBD, as Adelaide continues to present itself as an attractive base for both international and local businesses. Furthermore, within the CBD office market, A-grade vacancies decreased by 0.5% and B-grade vacancies also reduced by 0.2%, while C-grade office vacancies increased by 0.5%, reflecting tenant demand for high quality and sustainable office space.

Nationwide vacancies are forecast to reduce to 7.7% over the next two years, with modest improvements in South Australia, Queensland and Western Australia offsetting slight vacancy increases in New South Wales and Victoria.

Adelaide's office market continues its solid performance with vacancy rates dropping to their lowest level in over four years.

Owners are continuing to reposition B and C-grade space to increase the quality and fuel the flight to quality within the Adelaide CBD, further closing the gap between premium and secondary space.

Recent major transactions within the Adelaide market include the Real Estate Institute of South Australia (REISA) building at 249 Greenhill Road, Dulwich. The 801 square metre building sold for $3.215 million in July. In addition to this, the city frame site of 104 South Terrace sold for $3.435 million in March, encompassing 772 square metres of lettable area. Activity has been high in the city frame market recently, as a multi- level office building with underground car park at 67 South Terrace sold for $2.244 million in June. Outside of the city, there has been activity in the eastern suburbs, with offices selling in Norwood and Stepney over the past few months. 57 Beulah Road, Norwood sold late in June for $1.37 million for 606 square metres of lettable office space on a site measuring 826 square metres. 65 Magill Road, Stepney also sold in June for $2.5 million for a property that encompasses a multi-level office building with lettable area of 545 square metres and quality main road exposure.

VACANCY

14.2%

Adelaide CBD total vacancies

104 South Terrace, Adelaide Source: realcommercial.com.au

On the leasing front, the most significant transaction to occur in recent months is the renewal of the lease to South Australian Health at 11 Hindmarsh Square in the city core area. SA Health renewed its lease in April this year to extend its stay in Hindmarsh Square for a further five years, encompassing 13,750 square metres of lettable area. Smaller profile leases have been much more common in recent months, with tenants picking up space on the first floor of Adelaide Arcade, the ground floor at 120 Hutt Street, also home to Connekt Urban Projects, while various office suites at Aurora on Pirie, 147 Pirie Street, have also been leased to new tenants.

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Overall, sentiment in the office market is encouraging, with net absorption remaining positive. As businesses grow and expand, office space continues to be sold and leased and pressure is put on B and C-grade space to adapt and improve to remain attractive to prospective tenants.

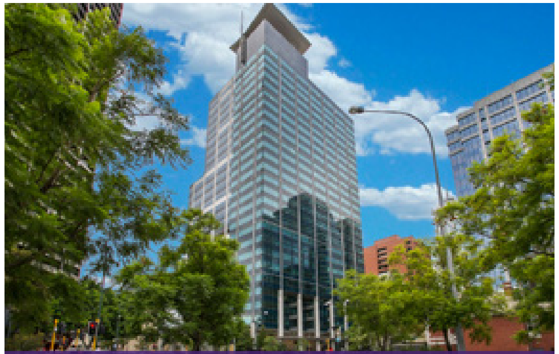
Western Australia

Perth

To date in 2019, the Perth office leasing market has seen both rental incentives and rental rates stabilise. The most recent Property Council of Australia (PCA) Office Market Report indicates the total vacancy rate for office space in the Perth CBD dropped marginally from 18.5% to 18.4% in the six months to July 2019. The reduction is attributed to positive demand for premium and B-grade buildings.

Whilst an encouraging sign, Perth's CBD has the highest vacancy rate of all capital cities in Australia.

There are no significant building projects in the pipeline until 2020 and the revitalisation of the CBD landscape, with major infrastructure projects such as Elizabeth Quay continuing to move ahead. Incentives for quality buildings in Perth's core CBD have even experienced some downward pressure with early signs of growth in the space needs of particular tenants.



240 St Georges Terrace, Perth Source: realcommercial.com.au

The total vacancy rate for office space in the Perth CBD dropped marginally from 18.5% to 18.4% in the six months to July 2019.

Some of the more notable leasing deals are highlighted below:

- **240 St Georges Terrace, Perth:** The former Woodside Plaza building owned by Dexus (circa 47,000 square metres) has managed to secure multiple tenants including Macquarie, CBH Group and Iluka Resources during the past 12 months or so and reportedly sits at around 92.5% occupancy.
- **556 Wellington Street, Perth** – Some 8,500 square metres of office space within Kings Square 1 has reportedly been let to the Department of Human Services.
- **150-152 St Georges Terrace, Perth:** Co-working and work place design company WeWork has reportedly taken just under 8,000 square metres in Central Park.

Property owners continue to be proactive in trying to entice existing tenants to recommit and in order to attract new tenants. Accordingly, incentives are still being offered in the market place (typically between 25 and 50%).

Furthermore, landlords are providing their existing and prospective tenants with bespoke floor plates, flexible work spaces, meeting hubs, refurbished foyers, some featuring concierge services, gymnasiums or wellness centres with some more innovative landlords looking at child care or child minding facilities within their buildings, in addition to the obligatory end of trip facilities, bike storage rooms and, in some cases, bike repair shops.

In terms of capital transactions, demand for office property in the Perth CBD has been felt predominantly from institutions and foreign (south-east Asian) buyers seeking counter-cyclical acquisitions of secondary assets with good prospects for re-positioning.

We highlight the following recent transactions:

- **Exchange Tower, 2 The Esplanade, Perth:** $326 million, December 2018;
- **34 Stirling Street, Perth**: $24 million, December 2018;
- **179 St Georges Terrace, Perth:** $18.25 million, February 2019.

These and other recent sales in the CBD have shown (analysed market) yields in the order of 7% to 8.75%.

The West Perth office market has not fared as well as the CBD for the six months to July 2019 as the total vacancy rate rose from 14.8% to 16.9%. Similar to the Perth CBD however, vacancy rates for A-grade space actually tightened during this period however this was off-set by a substantial increase in vacancies for lower grade premises.

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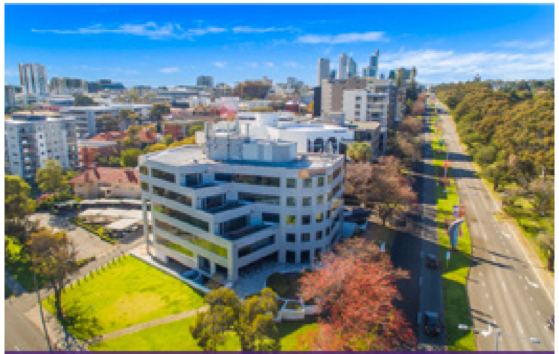
There have been very few sales in West Perth during the past 12 months but we make mention of the following asset acquired by RG Property:

- **76 Kings Park Road, West Perth:** circa $20 million, December 2018.

The lack of quality office stock with medium to long term WALEs combined with subdued economic conditions has affected transaction activity. We expect these trends to continue in the short term.



76 Kings Park Road, West Perth Source: realcommercial.com.au

Australian Capital Territory

Canberra

2019 has seen vacancy rates continue to tighten for A-grade office stock in the nation's capital, having fallen to 5% from 5.4% in the six months to July 2019 and having already decreased from 8.6% for the six months prior to that (July 2018). Absorption of A-grade stock has continued to improve, primarily for property in close proximity to the CBD and predominantly by Commonwealth government departments. While the supply level for premium office stock is currently tight, new stock coming on-line in 2020 and 2021 will relieve this pressure and potentially offset any significant rental growth experienced currently, especially in the premium sector.

Notable office development currently taking place within the CBD includes Amalgamated Property Group's Civic Quarter, situated alongside the Northbourne Avenue development corridor with direct exposure to the light rail system. The development is set to be twelve levels with a total office space area of 16,000 square metres. Completion is expected by late 2019.

Construction is also well underway on a new $300 million development by Capital Property Group. The property, located on the corner of Constitution Avenue and London Circuit in Canberra's CBD, is to feature 20,000 square metres of office space spread across 12 levels. The space is already set to be leased by the government for 20 years, with an option of another five years, and will house a total of 1,700 public servants upon completion. Construction for this development began in

40 Macquarie Street, Barton Source: commercialrealestate.com.au

December 2017 and is expected to be completed by mid 2020. While there has been very strong interest in the above mentioned projects by both government and corporate tenants alike, demand for office space certainly exists outside of the CBD.

Some recent notable or large leasing transactions in 2019 include:

- **23 Furzer Street, Phillip.** Leased/ renewed for a ten year term to the Department of Health & Ageing in February 2019. Comprises 44,896 square metres of NLA at $510 per square metre gross.
- **16 Marcus Clarke Street, Canberra.** Leased for a ten year term to the National Health and Medical Research Council in February 2019. Comprises 4,020 square metres of NLA at $501 per square metre gross.
- **40 Macquarie Street, Barton.** Leased for a seven year term to the Australian Strategic Policy Institute in February 2019. Comprises 2,047 square metres of NLA at $390 per square metre gross.

An example of a significant sale transaction is 16-18 Mort Street, Canberra City in June 2019 for $108.5 million. The property was constructed in 1992 and features a total of 14,506 square metre B-Grade office space.

The continued popularity and growth of co-working spaces and buildings with shared facilities to satiate an ever growing mobile office population that demands more flexible spaces coupled with a move towards smarter more energy efficient buildings will see an increased proportion of current B-grade stock undergoing substantial refurbishment and modernization in order to stay competitive and garner local and offshore investment interest.

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