

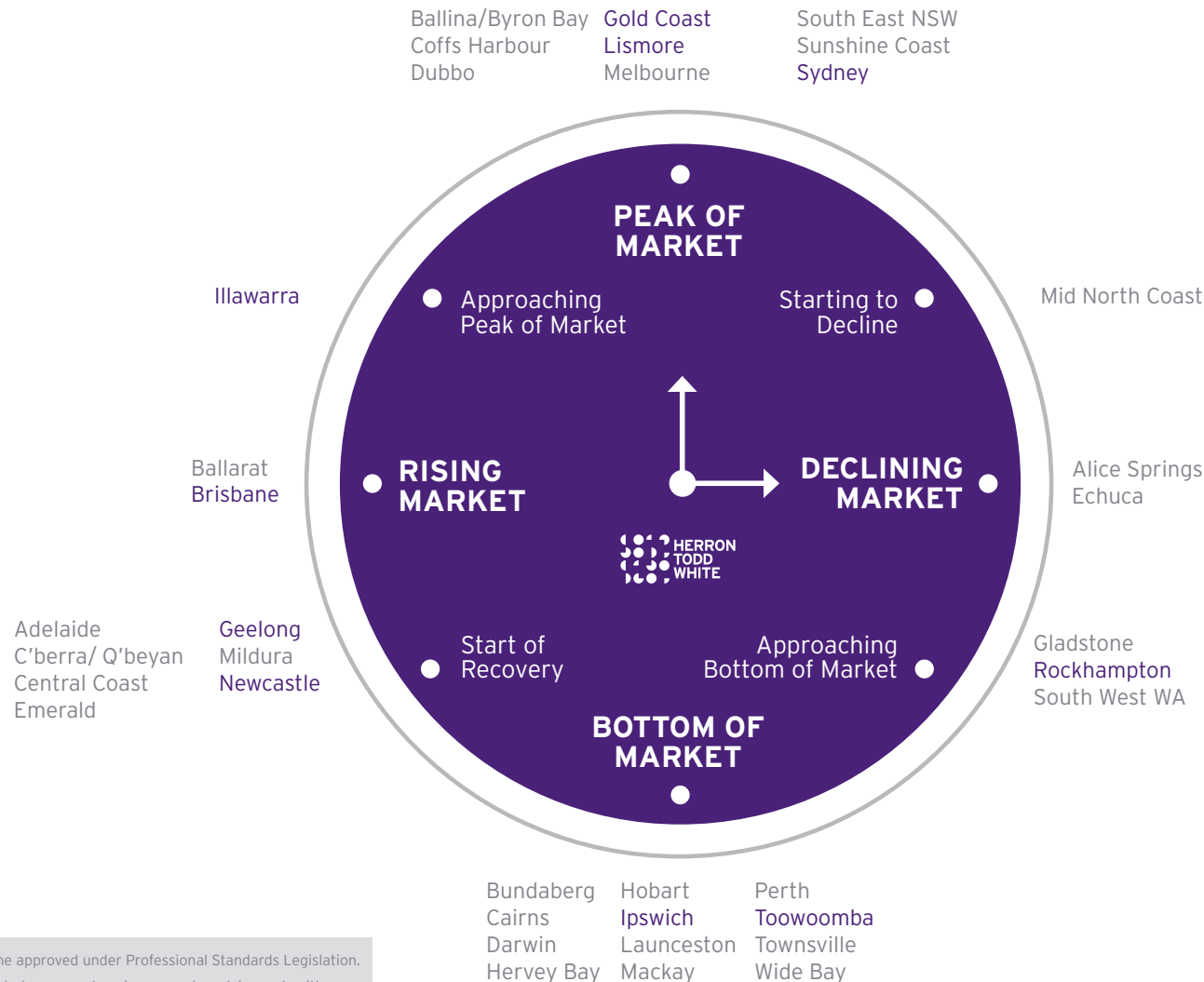


Office

December 2019

National Property Clock: Office

Entries coloured purple indicate positional change from last month.



Month in Review
December 2019



COMMERCIAL

New South Wales

Overview

Another year is coming to a close. As we enter the final month of 2019, it's time to take a look back at how office markets performed across the nation.

It should come as no surprise that there was a mixed bag of results. Many big-city investors were looking to shore up cash flow by concentrating on commercial stock, which led to incredibly strong prices, but in less-populated areas, the outcomes were a bit more subdued.

Sydney

2019 has been another strong year for the office market across both the Sydney CBD and metro centres. With rents continuing to climb and vacancy rates at record lows, it is no wonder that values have continued to rise.

The Sydney CBD saw vacancy rates decline over the first half of 2019 and were most recently recorded by the PCA in July 2019 at 3.7 per cent, a 1.1 per cent tightening since the same time in 2018. Tight vacancy kept rentals at record highs, particularly for prime and A grade stock, however agents have begun reporting softer demand for B through to D grade stock through 2019. That said, rentals have remained strong across the board and continue to be intrinsically linked to the continued rise in capital rates.

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. That said, there is a new office supply on the horizon, however the majority of this will not come online until 2020/2021.

The CBD office market saw a number of high profile sales in 2019, with and its unlisted Dexu Wholesale Property Fund's purchase of GPT Group's half-share in the MLC Centre at 19-29 Martin Place for \$800 million, through to record transactions for strata suites. Noonan Property recently achieved a sale price of \$8.8 million for Suite 56 at 5-7 Macquarie Street. At \$21,053 per square metre for 418 square metres, this sale reflects the highest rate to date for a strata suite over 400 square metres.

We note that there is a continued dominant demand from owner occupiers that appears to be propelling this strong value growth and for a variety of reasons. The current interest rate environment, seeing interest rates at record lows, is fuelling borrowing power and market sentiment across the board. The current low cost of money combined

SYDNEY VACANCY RATES

3.7%
July 2019

4.8%
July 2018

with the impact of rising rents has seen a significant increase in tenants looking to purchase to owner occupy over the past two years. This appears to be a strong driver in increasing capital values as tenants looking to owner occupy, as well as owner occupiers in general, are typically less reliant on potential yields and as such are more willing to pay a premium to secure the property they desire.

With the completion of the light rail project along George Street imminent and the first trams trialling the tracks, a new era of CBD accessibility is in sight. The completion of the majority of the construction has already improved what has been a particularly unpleasant streetscape over the past few years. The below shows one of the shiny new trams in action.



Light rail

Source: Herron Todd White

This sale reflects the highest rate to date for a strata suite over 400 square metres.



We also saw the opening of the Metro North West Line earlier in the year, providing a significant increase in accessibility to the secondary office precincts of Norwest and Macquarie Park as well as an additional line of access to Chatswood, increasing the overall appeal of these secondary precincts.

The continuation of the Sydney Metro project, due for completion in 2024, is considered to be of further benefit to the Sydney CBD and surrounding office markets. This important infrastructure project will further improve accessibility to the CBD and surrounds and we therefore expect it to have a positive influence on the market.

Outside of the CBD, there have been impressive performances in a number of other metro office sectors. In the west, the Parramatta CBD has been the best performing secondary CBD in the country, with the most recently reported vacancy rates at 2.7 per cent (July 2019, PCA). This has continued to be driven by low supply additions and the draw of more affordable rentals than the CBD.

Overall, the strong office market across Sydney continued in 2019 and is unlikely to weaken in the short term. We expect that there will continue to be strong appeal for quality properties in locations with adequate accessibility and particularly where supply is limited in the short term.



Victoria

Melbourne

According to the Property Council of Australia's Office Market Report, Melbourne's CBD Office overall vacancy rate slightly increased from 3.2 per cent to 3.3 per cent over the six months to 1 July 2019.

Melbourne CBD has still recorded the lowest vacancy rate amongst all of Australia's CBDs at 3.3 per cent, in front of Sydney CBD at 3.7 per cent. Low vacancy has led to competition for remaining space, driving up net face rents over the past 12 months. Incentives have also reduced however are still at relatively high levels. New supply of prime office accommodation was limited throughout 2019 however a deluge of new office supply is forecast for completion in 2020/21. As a result, the CBD office market saw strong rental growth over 2019 and is anticipated to level out as the new supply comes on line by 2021.

Sales volumes in the year to September 2019 were the highest in the Melbourne CBD in ten years owing to record low yields, low interest rates and strong demand from all buyer groups. Demand for good quality smaller office properties within the Melbourne CBD, metro and St Kilda Road office markets continues to be strong due to the lack of suitable stock on the market and sheer weight of capital for the limited investment opportunities. We highlight that whole level strata office floors within

**MELBOURNE
VACANCY RATES**
3.3%
July 2019

Melbourne CBD has still recorded the lowest vacancy rate amongst all of Australia's CBDs at 3.3 per cent in front of Sydney CBD at 3.7 per cent.

the CBD have averaged record-high performance in 2019 with office strata capital value rates in the eastern core precinct selling well above \$10,000 per square metre. Due to the tight leasing environment and record-low interest rates, vacant office floors are in demand and appeal to both owner occupiers and investors who are looking to capture the rental upside. We highlight that there is a possibility that the current overheating in the strata market will abate and yields may soften.

Tenant demand is continuing to rise in the city fringe. 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 is the lowest of all of Melbourne's metro precincts. The CBD's increasing rents are creating greater demand in city fringe locations as tenants seek cheaper alternatives.

Fringe CBD and inner suburban development sites with holding income are keenly sought after in the current market by developers and land bankers. In particular, there has been strong capital growth for commercial development sites in Cremorne and Richmond over the past 18 months which is backed by solid rental growth and low vacancy rate. There

are a number of commercial office developments under way in the precinct such as 510 Church Street, an 11-storey office building which is under construction and will provide 21,985 square metres of lettable area, and 600 Church Street, an eight-storey office building which is expected to be completed in Quarter 4, 2019 and will provide 5,799 square metres of lettable area. There is a potential that demand for office space may be saturated upon completion of the current developments. We note that there are existing pre-commitments in place over many of the approved developments.

The most active players within the sub-\$50 million market at present are private investors, syndicates and Self-Managed Superannuation Funds (SMSF). Overseas investors are also prevalent as an overflow effect of the lack of good quality commercial stock in the Melbourne CBD. We are witnessing strong buyer demand for well-located assets with strong underlying fundamentals such as long WALES, good lease covenants and low capital expenditure requirements. We have also observed more suburban transactions to overseas purchasers focusing on underlying redevelopment potential. There is also an increase in owner occupiers returning to the market through purchasing suburban office property as an alternative to leasing owing to the low interest rate environment.

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COMMERCIAL

Queensland

Brisbane

It has been quite a big year for the Brisbane commercial office market which has enjoyed positive capital growth in 2019.

The investment market in particular has been strong with CBD and fringe precincts including King Street, Ann Street, Gasworks and South Brisbane office precincts being very popular with investors. The high levels of demand had seen yields for Prime and A grade buildings fall to less than six per cent with capital growth of up to 25 per cent being achieved over the past three years. Overall, yields have fallen over the past three years by up to 150 basis points and the market is now starting to enter unprecedented yield territory with the potential for some final further compression in 2020.

The majority of the investor demand and market movement is primarily within the Prime and A grade sub-markets. These markets have seen some growth in gross face rental rates for the first time since the GFC, however incentives remain high at above 35 per cent. The lack of new stock entering the market has helped alleviate vacancy levels as they now have reached their lowest point for many years. Current vacancy levels for Prime CBD accommodation are now 8.7 per cent, their lowest rate since July 2015. For A grade space, the current CBD vacancy is ten per cent which is slightly up on January 2019 (9.9 per cent) but still at a near low point for the past five years. We note however that

the pending completion of 300 George Street will see the vacancy rate for Prime and A Grade space push back over ten per cent.



300 George St - Shortly to be Completed

Source: HTW

In the fringe markets, total vacancy is 13.8 per cent whilst A grade vacancy is slightly less at 12.7 per cent. There is limited current development activity

in fringe areas but there are a number of approved sites ready to go when required.

Secondary office precincts (Milton and Spring Hill) remain weak as vacancy rates and incentives remain stubbornly high. We note however that Milton's vacancy rate has reduced significantly by circa eight per cent in 2019 with approximately 26,000 square metres of lettable space being taken up in the 12 months from July 2018 to July 2019. This will come as a welcome relief for vendors as value levels have been negatively impacted by the weak leasing market.

With tight margins and a genuine lack of quality prime office stock available for sale, investors are looking for other investment and value-add opportunities. There has been a noticeable increase in the volume of well located, under-performing, secondary B grade office buildings sold with the intention of repositioning these assets. With improved leasing conditions, investors are seemingly more comfortable taking on the leasing risk by upgrading building services and amenities and creating more functional work environments. As there are limited opportunities available within the prime market and leasing demand remains positive, it is likely we will see

BRISBANE VACANCY RATES

8.7%

Prime CBD

10%

A grade CBD

12.7%

A grade fringe

Month in Review
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COMMERCIAL

It has been quite a big year for the Brisbane commercial office market which has enjoyed positive capital growth in 2019.

further yield compression and capital value improvement in this sub-market, albeit within well located office precincts.

Moving further afield, suburban markets have largely seen a lesser level of capital value growth in 2019. Leasing markets remain fickle, especially for secondary and tertiary grade commercial office assets. Well located assets that are modern and within close proximity to transport, road networks and retail amenities are still sought after by both tenants and buyers. Sale activity has generally been in and around North Lakes, Caboolture town centre, Mount Gravatt and Springwood. Investors and owner occupiers remain cautious of commercial office assets in secondary precincts or older style buildings.

We also highlight that the owner occupier market remains strong with a combination of second tier buildings well below replacement costs and mortgage costs well below leasing. This is primarily confined to the sub-\$5 million office markets.

Gold Coast

Going into 2019, the Gold Coast was still upbeat from the successful 2018 Commonwealth Games, although the elephants in the room were the Banking Royal Commission, with its findings to be handed down in February, and the federal election due in May.

It's fair to say that there was a bit of trepidation in the commercial property market moving into 2019, however, to a degree, this was offset by the continuing low interest rate environment which had and was continuing to encourage buyers, both large and small, from high wealth individuals, to SMSFs and owner occupiers across all sectors, from investment to vacant properties for owner occupation, encompassing smaller strata units

through to the larger assets.

Fair to say that the outcome of the Banking Royal Commission was expected. However, the main upshot from a property perspective, being stricter lending criteria, did put a bit of a dampener on the commercial market. This was then countered by the somewhat unexpected federal election result, meaning that negative gearing and capital gains tax were going to be unchanged, well at least for the next four years.

Coupled with a few reductions in the official cash rate by the RBA over the course of 2019, the picture moving forward looked good. The market responded to this general sentiment and the remainder of 2019 moved along quite nicely.

In terms of sale transactions of office buildings, the Gold Coast marketplace has been quite respectable. There have been several stand alone buildings sold over the course of the year, with the action noticeably up after the completion of the Banking Royal Commission. There have been a number in the over \$7 million tier (mid to larger size for the Gold Coast) and a number also in the low to mid-size tier of \$2 million to \$5 million.

Yields have remained reasonably strong, although we do consider they softened over the latter part of 2019. In general, the expected yield range

GOLD COAST VACANCY RATES

11.6%
January 2019

12.9%
July 2019

7% - 7.75%
Expected yield range

for the Gold Coast office sector would be 7% to 7.75%. There have been transactions below this range, although generally such properties would have some other element on offer, such as redevelopment scope.

Examples of larger office buildings to have sold on the Gold Coast over the course of 2019 to date include: 130 Bundall Road, Bundall in January for \$11 million (source: CoreLogic) reflecting an analysed yield of 7.34 per cent and \$2,988 per square metre on lettable area; Lakeside 1, Bermuda Point, Lot 1101/1 Lake Orr Drive, Varsity Lakes in March for \$25.1 million (source: CoreLogic) reflecting an analysed yield of 8.75 per cent and \$4,105 per square metre on lettable area; 169 Varsity Parade, Varsity Lakes in May for \$14 million (source: CoreLogic) reflecting an analysed yield of 6.85 per cent and \$4,172 per square metre on lettable area; 7-11 Short Street, Southport in July for \$8.2 million (source: valuation) reflecting an analysed yield of 7.7 per cent and \$3,356 per square metre on lettable area.

Examples of other notable sales include: 145 Wharf Street, Tweed Heads in March for \$2.925 million (source: CoreLogic) reflecting an analysed yield of 7.52 per cent and \$3,140 per square metre on lettable area; 34 Thomas Drive, Chevron Island in March for \$4.1 million (source: CoreLogic) reflecting an analysed yield of 5.37 per cent and \$4,409 per square metre on lettable area; 13 Hicks Street, Southport in March for \$2.65 million (source: CoreLogic) reflecting an analysed yield of 6.91 per cent and \$3,529 per square metre on lettable area; 16-20 Railway Street, Southport in July for \$4.07 million

Coupled with a few reductions in the official cash rate by the RBA over the course of 2019, the picture moving forward looked good.

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Leasing agents report there has been a general flight to quality, with tenants seeking to move from D and C grade space to B and A grade space.

(source: CoreLogic) reflecting an analysed yield of 7.54 per cent and \$4,409 per square metre on lettable area; strata Lots 12 and 13 Premion Place, 39 White Street, Southport in September for \$2.25 million (source: CoreLogic) reflecting an analysed yield of 7.04 per cent and \$6,048 per square metre on lettable area.

The overall level of vacancy across the Gold Coast office sector as monitored by the Property Council of Australia (PCA) reflected 12.9 per cent in July 2019, which was up from 11.6 per cent in January 2019. Leasing agents had noted a tougher first half for 2019 but suggest the second half of the year has been better. It is expected that the level of vacancy will hold at the next PCA report in January 2020.

Leasing agents report that there has been a general flight to quality, with tenants seeking to move from D and C grade space to B and A grade space. Rates have demonstrated growth at least in line with movement of the CPI and in some instances higher increments. Incentives have tended to settle at around eight per cent of the first year's lease rental. For D and C grade space, being of lesser quality, incentives continue to be reflected in the level of the rental rate rather than any rent free period or contribution to fitout, which form the main basis of incentives in the Gold Coast marketplace. In summary, expected rental levels across the Gold Coast would be:

- ▶ D and C grade: \$250 to \$300 per square metre per annum gross;

- ▶ B grade: \$310 to \$375 per square metre per annum gross
- ▶ A grade: \$400 to \$475 per square metre per annum gross, although there are instances where over \$600 per square metre per annum gross has been achieved
- ▶ Car parks - basement: \$110 to \$150 per bay per calendar month; undercroft: \$100 to \$120 per bay per calendar month; open: \$80 to \$100 per bay per calendar month.

Yield would appear to have been the primary driver for investors in the Gold Coast office sector in 2019. Certainly levels of seven per cent to 7.75 per cent have been superior to returns in the capital cities and in many cases are on par with larger regional cities. The dearth of new office buildings on the Gold Coast for several years now has assisted in reducing vacancy levels, which has in turn filtered down to create anticipation of sustainable rental growth going forward.

Whilst there are headwinds in terms of global issues (trade wars, Brexit) and interrupters for Queensland and the Gold Coast such as state and local government elections coming up in 2020, the general feeling in the Gold Coast marketplace is that in all likelihood, conditions will hold fast next year. Notwithstanding this sentiment, there is also an amount of deleterious commentary (print media and telecommunications) around global economic headwinds and dare we say it...recession predictions. So, nothing is a sure bet.



145 Wharf St

Source: HTW Gold Coast



169 Varsity Pde

Source: Ray White Commercial

Sunshine Coast

The office market across the Sunshine Coast performed in line with general expectations during 2019. Expectations at the end of 2018 were that the market would show a range of issues due to the high levels of supply that entered the market during 2017 and 2018 with circa 45,000 square metres of space added in that time.

We note that in general, leasing conditions have been impacted by this large level of supply. This has impacted secondary style locations to a greater level with these complexes noting impacts on lease renewal of drops in rental levels of up to 20 per cent. Good quality buildings in prime locations





1,615 square metres and 60 on-site car parks. The building was fully leased to two government tenants. Sale price of circa \$7.4 million with a passing net yield of circa 8 per cent.

- **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 of \$4.65 million with a passing yield of circa 7 per cent.

Cairns

The Cairns office market is relatively shallow and experiences limited sales activity. The market has also experienced limited new development, with the last large office building constructed in Cairns being the state government office tower completed in 2010. There are no known new developments in the pipeline.

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

Toowoomba

Following years of limited new office development in Toowoomba, construction has been completed on a new building located on the corner of Campbell and Raff Streets in the northern fringes of Toowoomba's CBD. The building is multi-level and will contain a food/café tenancy on the ground level (currently for lease). This project was driven by multiple owner occupiers and is strata-titled.

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

Leasing demand for commercial office accommodation in Toowoomba was subdued in 2019 which continued the trend from the previous couple of years. As a result there has not been a significant growth in rentals and evidence that some lease incentives may be required to secure tenants.

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

- **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. WALE of 2.4 years. Sale price of \$10.5 million with a passing net yield of circa 12 per cent.
- **146 Herries Street, Toowoomba City** - This is a two level building with a net lettable area of

have had a lower overall impact to leasing rates this year, though there has still been some impact felt, though typically less than ten per cent.

PCA statistics are yet to be released for the 2019 calendar year, although overall absorption appears to have been above long-term averages of circa 4,000 square metres. This would still leave a high overall level of vacancy for the region with further stock planned to enter the market in 2020.

One of the unusual factors noted during 2019 was the continued strong sales of larger stand-alone complexes. Sales included Lakeview Centre at Main Drive, Birtinya for \$4.2615 million analysing to a yield of 7.29 per cent and \$4,864 per square metre and 1-5 Plaza Parade, Maroochydore for \$3.65 million analysing to a yield of 7.24 per cent and \$3,509 per square metre. These sales indicate that overall values held firm during 2019 even with the volatility surrounding the rental market. This is likely to have been driven by the continued low interest rate environment and the high overall cost to develop new office stock in the area.

The overall stability of the market is unknown moving into 2020 as vacancy is still considered to be high. If there are any changes to macro-economic conditions, including the current level of migration to the Sunshine Coast, then this could impact negatively.

One of the unknowns is the impact of the Submarine Broadband Internet Cable, which will be connected during 2020 and may lead to increased demand for office space from a range of users. This has the potential to improve overall leasing conditions and subsequently the overall outlook for the office market.

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 \$2,000 to \$4,500 range.



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 seen the emergence of incentives.

The Cairns office market overall has experienced little change during 2019 and is expected to remain steady in the short to medium term moving forward into 2020.

Townsville

Throughout 2019 the office market has remained relatively stable with interest for larger assets being underpinned by national investors.

One of the biggest changes currently underway in the CBD office market is the construction of a new 4,000 square metre, four-level office building in a

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. Upon completion, the ATO will relocate from their current CBD office, which is likely to 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.

Throughout 2019 we have also seen the re-development of an existing CBD office building to include upgrades to external facades and internal upgrades at a reported cost of \$10 million. The property was rebranded Precinct 21 and comprises five levels of commercial office space of over 5,000 square metres which is being offered to the market for lease.

The leasing sector remains soft with better quality A grade stock appearing to be holding value levels, although new tenancies to non-government or multi-national tenants are still seeing high levels of leasing incentives in the 15 per cent to 25 per cent range. Lower quality B grade product is continuing to see downward pressure. Overall, rental rates for the market as a whole appear stable as a result of the market correction that has occurred over the past few years, however market corrections are very much property specific with downward pressure still occurring in some leases.

Rockhampton

At the start of 2019, we forecast that 2019 would see some positivity return to the commercial sector in Rockhampton, not necessarily by way of substantial value rises, but more by way of decreased vacancies, new developments and increased activity in general. As the year draws to a close, we consider that while the office market has remained relatively flat, most of the above

rings true to what we have seen in the office sector.

There has been a notable increase in market confidence generally as a result of the continued recovery of the resources sector as well as commencement of major infrastructure projects in the region.

Sales activity has been limited, however owner occupiers have remained active and investors are actively still seeking quality investment opportunities. Rentals have remained relatively stable over the past 12 months, indicating a range of about \$225 to \$300 per square metre gross for the average semi-modern to modern office space within the CBD.

We have however seen a number of smaller tenancies signing up in the \$300 to \$350 per square metre gross range for modern, well located office tenancies, a positive sign for the market.

Secondary tenancies are still likely to prove difficult to lease and incentives are still common in leasing negotiations for these tenancies. The same continues for large office tenancies in excess of about 250 to 300 square metres. There are few tenants locally that require tenancies of this size and these continue to sit vacant.

Gladstone

Throughout 2019, conditions in Gladstone's office sector have continued to remain stable.

Whilst there are still vacancies to be filled, we have

ROCKHAMPTON RENTAL RANGE

\$225 to \$300
Semi-modern office space cost per sqm

\$300 to \$350
Small tenancies cost per sqm

seen some new rentals in the CBD negotiated in the past 12 to 18 months that fall within the low-to-mid \$300 per square metre gross, which is a positive sign for this sector. Notwithstanding, 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. Sales activity has been very limited and owner occupiers are still the most active in the market, taking advantage of the stage of the property cycle coupled with record low interest rates. Investors have returned to the market, however are very sensitive to tenant strength and unexpired lease terms.

Most recently, a strata office unit at 174 Goondoon Street sold for \$1 million, reflecting a yield of about nine per cent. The property had a WALE of 2.88 years.

Wide Bay

The office market throughout the Wide Bay had a relatively stable year with a low volume of sales occurring throughout the three main localities. Notable activity includes the continued construction of The Avenue at Hervey Bay and some medical and professional services businesses completing construction works in Bundaberg.

Vacancies remain high in Maryborough and at a moderate level in Hervey Bay and Bundaberg. This is a continued trend from previous years with little on the horizon indicating a change in market conditions over the short term.

Mackay

This has been one of the quietest years for office sales in Mackay. There were only two transactions.

These included the mortgagee sale of vacant premises at 92 Wood Street at a price of \$505,000 and the sale of a combined office and residential flats property at 89 Sydney Street at a price of \$799,900.

The office leasing market was also noticeably slower throughout 2019. Office rental rates are highly variable and in some cases tenants have been able to negotiate fairly low rentals of between \$150 and \$200 per square metre per annum net for older tenancies or for large floor plates in secondary fringe localities. Better quality tenancies still achieve rentals of up to \$300 per square metre per annum.

The Department of Resources, Mines and Energy is relocating from its tenancy at 22-30 Wood Street in December to the new state government building at 44 Nelson Street. This 1,500 square metre, mostly upper level tenancy has recently been listed for lease. The office market remains oversupplied.

We could not let the opportunity pass without mentioning the current building insurance issue also related to the market for office investment properties which has now reached crisis point in northern Australia. At the time of writing, we had just attended a public forum on the matter which was organised by our Federal MP and attended by the Federal Assistant Treasurer. This forum confirmed our observations that premiums

have now risen so disproportionately high in comparison to southern Australia that they are now constraining net returns from passive and going concern commercial property investments. This is having a direct and adverse impact on commercial property valuations above the Tropic of Capricorn.

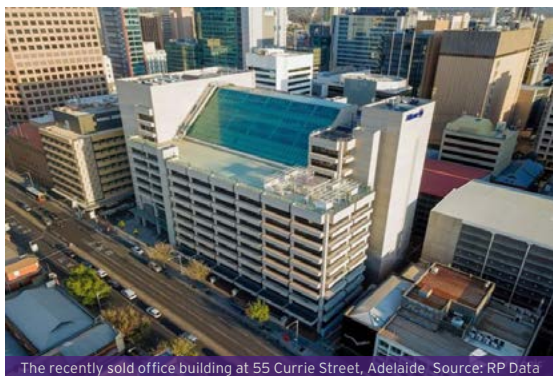
 *We could not let the opportunity pass without mentioning the current building insurance issue which has now reached crisis point in northern Australia.*

South Australia

Adelaide

Adelaide's office market continued its steady performance throughout the past few months. Interest remains high for purchasing and leasing office space throughout the Adelaide CBD, with the core sector continuing to attract the major investment. The cash rate was left on hold at 0.75 per cent, while potential land tax changes and the trade war between the US and China are the major influences on property market transactions through the latter half of this year.

It will come as no surprise to readers that the Adelaide CBD itself gathered the most interest in office buildings throughout metropolitan Adelaide, particularly within the core sector. Of the sales listed above, 55 Currie Street, 25 Grenfell Street and 80 Flinders Street are all located in the CBD core sector, while 149 Flinders is situated in the frame sector. Overall, sales volumes are slightly below the levels of this time last year and the total volume of Adelaide CBD office sales has decreased



The recently sold office building at 55 Currie Street, Adelaide. Source: RP Data

THE HIGH PRICE POINTS FOR ADELAIDE OFFICE SALES IN 2019

Address	Sale Date	Sale Price	Site Area (m ²)	Building Area (m ²)	\$/m ² Building Area	Reported Yield (%)
55 Currie Street, Adelaide	10/09/19	\$148,250,000	5,578	26,062	\$5,688	8.00%
25 Grenfell Street, Adelaide	01/11/19	\$134,220,283	1,968	25,131	\$5,341	8.36%
80 Flinders Street, Adelaide	25/09/19	\$127,000,000	1,398	12,154	\$10,449	6.10%
7 Laffer Drive, Bedford Park	12/04/19	\$23,500,000	32,990	6,430	\$3,655	5.46%
149 Flinders Street, Adelaide	01/10/19	\$18,400,000	530	2,144	\$8,582	N/A

in each of the past two years from the highs set throughout 2017.

Adelaide CBD vacancies currently measure just 12.8 per cent as per the latest statistics provided by the Property Council of Australia. Within the CBD specifically, vacancies in the core sector sit at 13.8 per cent while vacancies in the frame sector are nine per cent.

Looking to the fringe of the Adelaide City encompassing Greenhill Road, Fullarton Road and Dequetteville Terrace, vacancies measure 13.1 per cent. Furthermore, we are continuing to see B and C grade space refurbished, fuelling the flight to quality as tenants look to secure space in A grade

ADELAIDE CBD VACANCIES

12.8%
Overall

13.8%
Core sector

9%
Frame sector

buildings. Looking back on 2019, we have seen vacancies in the core sector drop from 15.5 per cent in January to 13.8 per cent in July, while frame vacancies have decreased from 9.7 per cent to nine per cent in that same timeframe.

NAB's reports of record-low levels in South Australian business confidence combined with recent interest rate cuts, higher than expected unemployment, land tax uncertainty and geopolitical tensions, have been the major influences on South Australian property markets of late, keeping activity rather subdued in most sectors.

Looking to leasing deals, the major leasing transactions in the Adelaide CBD in the past few months include:

- **80 Flinders Street** - The A grade office building recently purchased by Centuria Capital Group attracted tenants BAE Systems and Beach Energy earlier this year.

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► **30 Pirie Street** - Known as Telstra House, the 23-level A grade office tower has recently undergone refurbishments and attracted tenants, with BAE Systems also securing space here along with Boeing.

► **11 Hindmarsh Square** - SA Health renewed its lease in Hindmarsh Square in April of this year.

Overall, the office sector in Adelaide has performed steadily throughout 2019. The ongoing land tax debates continue to halt investment by private investors. The proposed changes to the South Australian land tax system would reduce the top rate of land tax to 2.4 per cent but would eliminate the ability of owners to aggregate their tax expenses across different entities. The PCA has been vocal in its scrutiny of the changes to the aggregation rules and we expect to see the debate continue into the near future.



Western Australia

Perth

The Perth office property market maintained the status quo in 2019.

The Property Council of Australia Office Market Report published in July 2019 indicated that the total vacancy rate for office space in the Perth CBD was 18.4 per cent, down from 18.5 per cent recorded six months prior.

Although the vacancy rate recorded in July 2019 was the lowest since July 2015, Perth's CBD still has the highest vacancy rate of all capital cities in Australia.

Property owners continue to be proactive in trying to entice existing tenants to recommit and also in order to attract new tenants.

Generally speaking, both rental incentives and rental rates have stabilised however the disparity between rental rates achieved for Premium and D grade space remains pronounced. Incentives for quality buildings in Perth's core CBD have experienced some downward pressure with occasional signs of growth in the space needs of particular tenants, yet incentives are still being offered in the marketplace (typically between 25 per cent and 50 per cent).

There are no significant building projects in the pipeline until 2020 however the revitalisation of the CBD landscape with major infrastructure projects

such as Elizabeth Quay continues to move ahead.

The emergence of co-working space has been a talking point throughout the year with the number of offerings in Perth having increased substantially. The popularity of these spaces appears to be driven by the increasing number of small businesses and start-ups entering the market with a need to minimise overheads. Corporate entities are also showing an interest in taking up these flexible work places rather than secure fixed term lease agreements as a risk mitigation measure given the local economic climate.

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.

In recent activity, industry sources indicate the 17-floor BGC Centre (28 The Esplanade, Perth) is under offer to the Singaporean based Redhill Partners for circa \$100 million. Fund managers such as Redhill Partners, Centuria Capital and EG Funds Management have been particularly active in this space throughout 2019. Sales in the CBD have shown (analysed market) yields in the order of seven per cent to 8.75 per cent during the year.

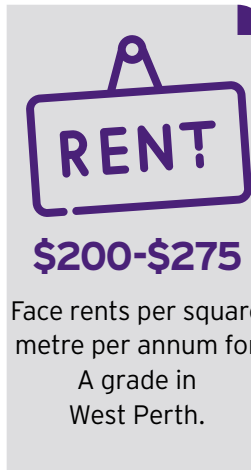
The West Perth office market has not fared as well as the CBD for the six months to July 2019 as the total vacancy rate rose from 14.8 per cent to 16.9 per cent. Similar to the Perth CBD however, vacancy rates for A grade space actually tightened during this period, however this was offset by a substantial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

Face rents for A grade accommodation in the West Perth office district tend to be lower in comparison to the CBD and typically fall between \$200 and \$275 per square metre per annum.

There were very few sales of stand alone office buildings in West Perth during 2019. The lack of quality office stock with medium to long term WALEs combined with subdued economic conditions has affected transaction activity.

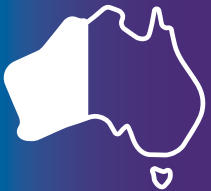
In summary, whilst it feels like the worst of the market conditions are behind us, there remain some challenging times ahead for owners of lesser grade and strata titled accommodation. These asset types continue to suffer from poor interest and an oversupply of available stock.

As Yazz and the Plastic Population sang, "the only way is up, baby".



RENT
\$200-\$275
Face rents per square
metre per annum for
A grade in
West Perth.

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Australian Capital Territory

Canberra

The Canberra office sector throughout 2019 has witnessed continued stabilization, tightening of vacancy rates for premium (A and B grade) stock as well as increased vacancy for non-centralised lower grade commercial stock. The growing discrepancy between prime and secondary stock uptake levels is expected to continue into next year with new premium offerings coming online in early 2020 reinforcing an increasingly competitive leasing environment.

Incentives have continued to increase throughout the year in both prime and secondary sectors with agents reporting average incentives for A grade stock being as high as 20 per cent. Demand for more specialised and flexible tenancies continues to drive the refurbishment of secondary office stock to meet market expectations.

A popular trend witnessed in 2019 was the emergence of the small scale shared co-working space. Spaces which traditionally would have been single tenanted are being refurbished with shared amenities including kitchen, printing facilities and meeting rooms. The flexibility of these spaces allows them to be sublet to multiple tenants often negotiated on a price per desk basis.

Continued increases in municipal or council rates throughout the territory (often outweighing CPI

rental increases) has resulted in an increase in net leases. It is becoming more prevalent for landlords to elect to pass on any increases to outgoings over the base year to the tenant.

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