

Briefing Brisbane Fringe Office

June 2019



Highlights

- Savills recorded \$820.5 million of Brisbane Fringe transactions over the 12 months to June 2019, which was 53% more than the record set in the previous period;
- Domestic funds and trusts dominated the market with 90% of total reported transactions in the current annual period;
- With only one development due for completion in 2019, there is little supply projected, which should protect rents at their current levels and perhaps even drive an increase.

A Grade Averages	Latest	Yr Change	Outlook
Rental – N.F. (\$/sq m)	485	+9.0%	↗
Incentives - Gross (%)	28.8	+00bps	↔
Rental – N.E (\$/sq m)	250	+8.7%	↗
Yield – Market (%)	6.15	-25bps	↘
IRR (%)	7.25	-75bps	↘
Capital Values (\$/sq m)	8,800	+3.5%	↗

Demand & Supply	Latest	PCP*
Vacancy	14.8	14.5
Net Absorb. ('000 sq m)	-8.6	-30.2
Stock U/C ('000 sq m)	35.1	21.6
- % of market	2.9	1.8
- % committed	68.9	78.0

*PCP = Previous Corresponding Period
Source: Savills Research

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Executive Summary

With the availability of more affordable options in rejuvenated precincts (particularly in the Urban Renewal precinct), the overall vacancy rate in Brisbane's Fringe market sits below that of the CBD at 14.8%. However, with incentives moving higher in the CBD, tenants are now being drawn back to the CBD, supported by anecdotal evidence suggesting firms are more eager to recentralise. New supply will be limited in the short term with only approximately 35,000 square metres of space coming onto the market in 2019 from 100-108 Alfred Street. Accelerating positive net absorption will outweigh the supply of stock, which is likely leading to a fall in total vacancy in the second half of 2019.

Fringe A Grade yields have continued to tighten, down a further 25 basis points, as demand for core quality assets remained strong with investors identifying more affordable options in Brisbane's Fringe market. The dominance of purchasing activity by domestic funds and trusts has continued in 2019 with 90% of total reported transactions in the current annual period.

PCA Summary Table – Brisbane Fringe (as at Dec-18)

	Prime	Secondary	Total	Aus Non-CBD
Total Stock ('000)	663.9	541.4	1,205.3	7,284.3
Total Vacancy ('000)	99.8	78.1	178.0	662.1
Vacancy (%)	15.0 (9.6)	14.4 (14.3)	14.8 (12.0)	9.1 (9.4)
Net Absorption ('000)	-11.6 (19.3)	2.9 (-9.6)	-8.6 (9.6)	7.6 (37.6)
Net Absorption (%)*	-2.0 (4.3)	0.6 (-1.9)	-0.8 (1.0)	0.1 (0.6)
Net Additions ('000)	4.2 (28.1)	-2.3 (-5.9)	1.9 (22.2)	18.1 (45.4)
- Stock Additions ('000)	38.5	3.1	41.5	133.0
- Stock Withdrawals ('000)	34.3	5.4	39.7	114.8
Net Additions (%)**	0.6 (5.7)	-0.4 (-1.0)	0.2 (2.1)	0.2 (0.6)

Source: Savills Research (10yr Averages shown in brackets); NB: Secondary Rents shown are for B grade; All rents equivalent to whole floor mid-rise

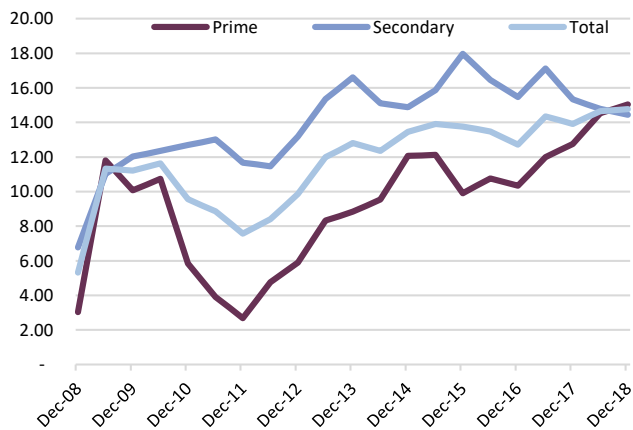
*As a percentage of occupied stock; **As a percentage of total stock

Vacancy

There was an uptick in the total vacancy rate over the six months to December 2018, with the overall vacancy rate rising to 14.8% from 14.5% in June 2018, largely as a result of increasing prime vacancy rates. However, it is important to note that vacancy rates remain below that of the neighbouring CBD. The precinct with the lowest vacancy rate is the Inner South at 10%. Whilst rents remain lower in Brisbane fringe, tenants are being drawn back to the CBD where higher incentives are currently being offered.

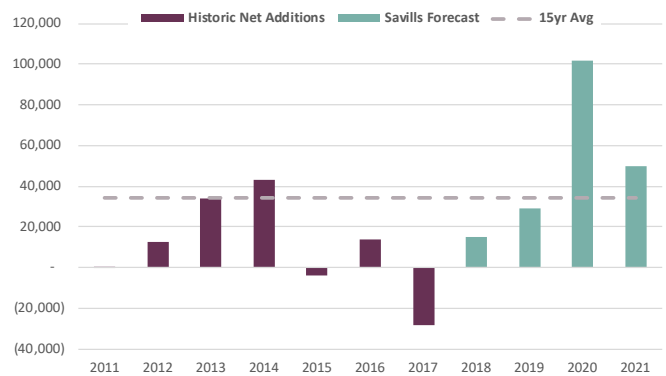
Savills Research anticipates vacancy rates to increase slightly over the short to medium term and remain stable in the long term with most developments from 2020 onwards are subject to pre-commitments before construction begins.

Historic Vacancy



Source: PCA / Savills Research

Net Supply by Year



Source: Savills Research

Supply

100-108 Alfred Street is currently under construction and due for completion in 2019. We will see approximately 35,000 square metres come onto the market across 2019, on top of the 15,000 square metres delivered by the newly completed 25 King Street in Bowen Hills during Q4 2018.

The 10-storey office building at 14 Stratton Street in Newstead has recently gained development approval from the council and is due for completion by the third quarter in 2020. Pre-commitments are required before developers commence construction.

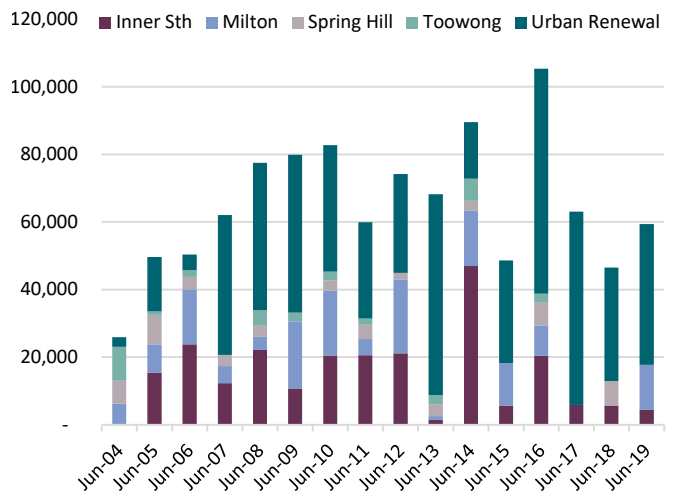
Leasing Activity & Demand

In the 12 months to June 2019, Savills Research recorded 65,947 square metres of leasing activity, up 35% on the 12 months prior and down 6.6% on the 10 year average (70,631 square metres). Approximately 70% of total leasing volumes occurred in the Urban Renewal precinct. Direct leases accounted for the majority of activity, comprising 64% of the total.

Tenants from the ‘Property & Business Services’ sector continued to dominate the Brisbane fringe office leasing market, accounting for 29% of the total area leased. This is largely due to the commitments signed by Downer EDI (7,160 square metres) in 135 Coronation Drive and WSP (5,685 square metres) in 900 Ann Street. A notable transaction in this sector is DXC Technologies’ commitment of 6,625 square metres in 100 Brookes Street.

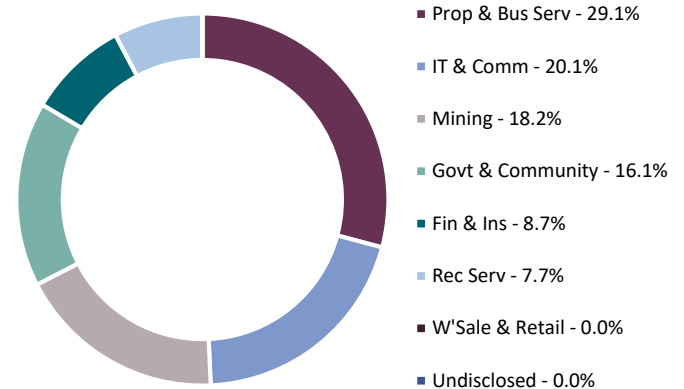
Negative net absorption remains a feature of the Brisbane fringe office market, with net absorption again recorded negative at 8,648 square metres (as at December 2018) which is largely due to tenants moving out from the Fringe and back into the CBD, attracted by higher incentives.

Leasing Activity by Precinct (> 500 square metres)



Source: Savills Research

Leasing Activity by Tenant Type (> 500 square metres)



Source: Savills Research

Recent Notable Leases (by Area Leased)

Property	Tenant	Deal Date NLA (sqm)	Type Rent Term
540 Wickham St, Fortitude Valley	AECOM	Oct-18 10,884	Renewal 560 (G) 7
135 Coronation Dr, Milton	Downer EDI	Aug-18 7,160	Direct 588 (G) 8
100 Brookes St, Fortitude Valley	DXC Technologies	Aug-18 6,625	Direct 600 (G) 7
900 Ann St, Fortitude Valley	WSP	Oct-18 5,685	Sublease 523 (G) 7
825 Ann St, Fortitude Valley	Macquarie Bank	Nov-18 4,301	Renewal 600 (G) 6
515 St Pauls Tce, Fortitude Valley	SunWater	Jul-18 3,000	Direct 570 (G) 10
315 Brunswick St, Fortitude Valley	Department of Housing & Public Works	Aug-18 2,580	Direct 525 (G) 6
1024 Ann St, Fortitude Valley	Workspace 365	Nov-18 2,194	Direct 485 (G) 10
61 Petrie Tce, Petrie Terrace	Southern Cross Austereo Brisbane	Jul-18 2,150	Direct 595 (G) 10
515 St Pauls Tce, Fortitude Valley	State of Queensland - Tourism	Aug-18 1,996	Direct 560 (G) 7

Source: Savills Research

Sales

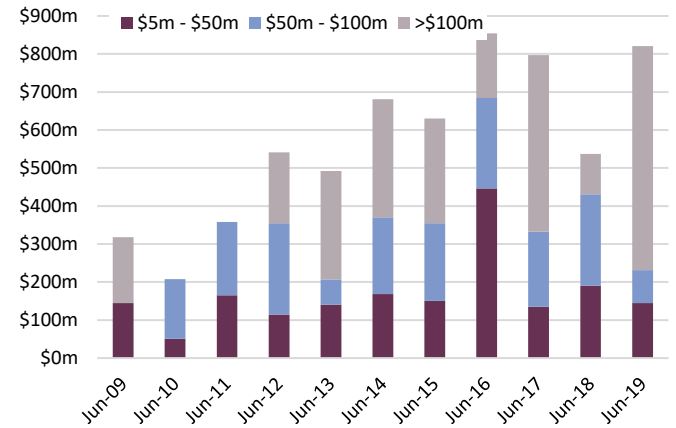
Savills recorded \$820.5 million worth of office transactions in the Brisbane fringe over the 12 months to June 2019, up 53% on the 12 months prior, indicating a continued interest in the fringe market for investment purposes.

Local 'Fund' and 'Trust' accounted for a combination of 90% (or \$732 million) of total reported transactions in the current annual period. Notable transactions include 100 Skyring Terrace acquired by Growthpoint Properties (\$250 million at an equated yield of 5.87%), 2 King Street acquired by Abacus and Heitman (\$170 million at an equated yield of 5.69%) and 825 Ann Street acquired by Centuria Capital (\$169.5 million at an equated yield of 6.29%). The evidence from sales activity over the last 12 months suggested that yield compression has also taken hold in the fringe market.

Following strong acquisitions by foreign investors in 2017, there was a decline in interest in Brisbane fringe in the 12 months to June 2019, totalling only about \$64 million of transaction volumes. This was through the sale of 339 Coronation Drive by Singaporean group Keppel Capital.

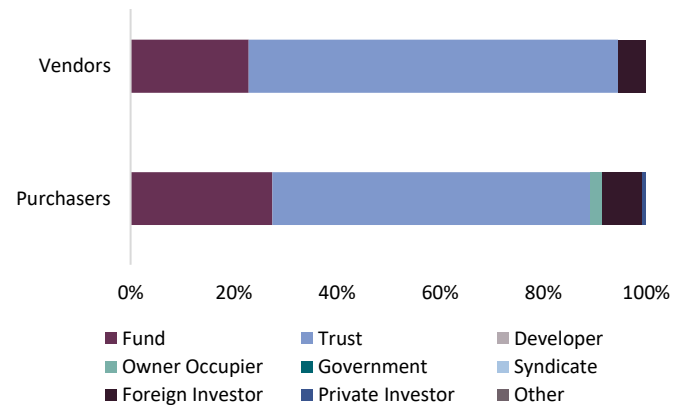
Whilst capital values in Brisbane fringe have increased marginally over the last 18 months, renewed interest from investors and a distinct lack of available quality assets for sale is likely to uplift that over the short term.

Sales Activity by Price (>\$5 million)



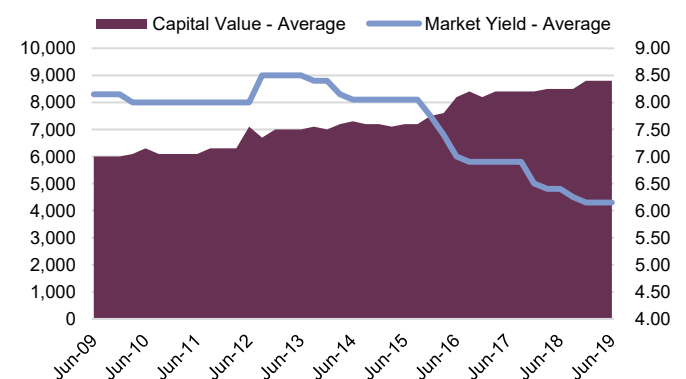
Source: Savills Research

Vendor & Purchaser Type



Source: Savills Research

Capital Values (\$/sq m) vs. Market Yield (%)



Source: Savills Research

Recent Notable Sales (by Sale Price)

Property	Price (\$m) Date GLA (sq m)	Yield Type \$/sq m
100 Skyring Tce, Newstead	250.00 Nov-18 24,665	5.87 e 10,136
2 King St, Fortitude Valley	170.00 Sep-18 16,341	5.69 e 10,403
825 Ann St, Fortitude Valley	169.50 Oct-18 19,155	6.29 e 8,849
100 Brookes St, Fortitude Valley	86.50 Oct-18 9,602	6.18 e 9,009
153 Campbell St, Bowen Hills	76.00 Jun-19 15,691	7.85 i 4,844
339 Coronation Dr, Milton	40.25 Aug-18 13,180	8.20 e 3,054
16 Marie St, Milton	25.50 Aug-18 3,901	7.06 e 6,537
8 Gardner Cl, Milton	25.23 Jun-19 4,271	7.11 i 5,907
55 Russell St, South Brisbane	23.65 Feb-19 4,081	6.80 e 5,795
39 Sherwood Rd, Toowong	23.50 Jun-19 5,211	7.20 r 4,510
74 High St, Toowong	19.00 Mar-19 4,431	7.06 e 4,288

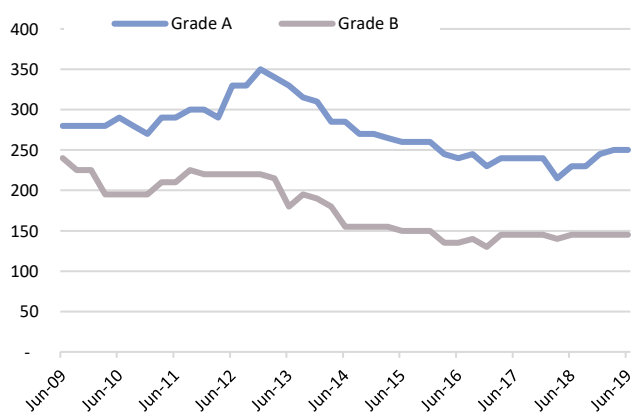
Source: Savills Research; Yield Types: i = Initial, r = Reported, e = Equated, v = Vacant, dev = development

Rents

Rents in Brisbane fringe increased over the year to June 2019 with A Grade net face rents rising 9%, up to \$485 per square metre from \$445 per square metre.

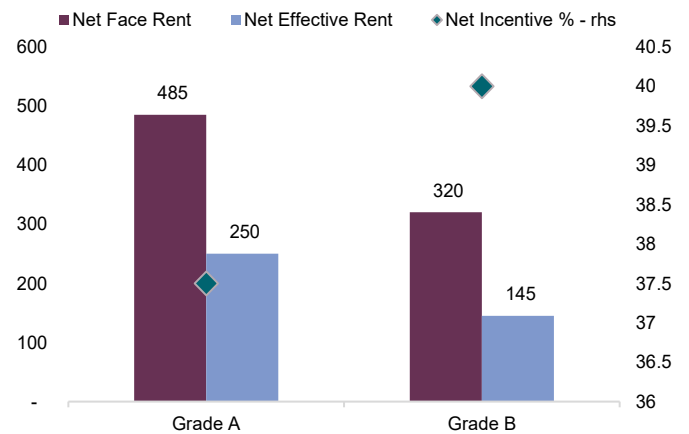
Savills Research, with only one development coming onto the market in 2019, rents are likely to be driven up due to a lack of supply.

Net Effective Rents by Grade (\$/sq m)



Source: Savills Research

Net Face & Net Effective Rents (as at Jun-19)



Source: Savills Research

PCA Summary Table by Precinct – Brisbane Fringe (as at Dec-18)

	Inner South	Milton	Spring Hill	Toowong	Urban Renewal	Brisbane Fringe (Total)
Total Stock ('000)	260.691	223.228	133.998	75.077	512.301	1,205.30
Total Vacancy ('000)	26.128	47.939	22.818	8.564	72.531	177.98
Vacancy (%)	10.0 (7.8)	21.5 (14.3)	17.0 (14.2)	11.4 (8.7)	14.2 (12.4)	14.8 (11.7)
Net Absorption ('000)	-16.4 (2.0)	-21.0 (-2.3)	0.8 (-4.6)	0.3 (-1.4)	27.6 (15.9)	-8.6 (9.6)
Net Absorption (%)*	-2.2 (3.9)	1.0 (0.3)	-3.1 (-3.8)	-4.2 (-2.0)	-6.5 (6.7)	-3.6 (2.4)
Net Additions ('000)	0.0 (8.8)	2.3 (3.1)	0.0 (-2.9)	0.0 (-0.6)	14.4 (28.5)	16.7 (36.9)
- Stock Additions ('000)	0	2.3	0	0	14.4	16.7
- Stock Withdrawals ('000)	0	0	0	0	0	0

Source: PCA / Savills Research (10yr Averages shown in brackets); *As a percentage of occupied stock

Outlook

As is the case with Brisbane CBD, there appears to be a turnaround in Brisbane Fringe. With almost 180,000 square metres of stock due to be delivered in the next 2 years, supply will play a major part in the Brisbane Fringe office market over the short to medium term as developers have identified a potential lack in prime space. This will provide significant opportunities for larger office occupiers. Whether this is enough to counter the negative effect from increased competition from Brisbane CBD where higher incentives are being offered remains to be seen.

Demand fundamentals are looking increasingly positive as the Australian economy continues on its path to recovery. A recovering labour market will further provide some boost to rental growth rates. Renewed investors' interest in Brisbane Fringe office market is likely to boost capital values whilst driving yields further down. The cost of funds has been falling in recent months with the interest rate cut to 1%. This will further exacerbate tightening yields.

Development

The table below summarises some of the major upcoming and planned development projects in the Brisbane Fringe.

Building Address	Dev Stage	NLA	Exp. Comp	Precinct	Tenants
36-52 & 100-108 Alfred St, Fortitude Valley (Valley Metro Building)	UC	35,067	2019	Urban Renewal	-
11-15 Breakfast Creek Rd, Newstead	DA	27,500	2020	Urban Renewal	John Holland
301 Wickham St, Fortitude Valley	DA	30,000	2020	Urban Renewal	-
801 Ann St, Fortitude Valley*	DA	39,332	2020	Urban Renewal	-
14 Stratton St, Newstead	DA	9,000	2020	Urban Renewal	-
31 Duncan St, Fortitude Valley	DA	22,738	2021	Urban Renewal	-
30 Little Cribb St, Milton*	PS	12,000	2021	Milton	-
89-91 McLachlan St, Fortitude Valley	PS	4,564	2021	Urban Renewal	-
152 Wharf St, Spring Hill*	PS	24,416	2021	Spring Hill	-
25 Green Square Cl, Fortitude Valley	DA	20,000	2022	Urban Renewal	Brisbane City Council
470 St Pauls Tce, Fortitude Valley	DA	17,554	2022	Urban Renewal	-
949 Ann St, Fortitude Valley	DA	13,490	2022	Urban Renewal	-

Source: Savills Research; UC = Under Construction; DA = Development Approved; PS = Plans Submitted; EP = Early Planning; *Subject to pre-commitments

Brisbane Fringe Key Indicators (Q2-19)

	A Grade		B Grade	
	Low	High	Low	High
Rental - Gross Face (\$/sq m)	575	680	400	485
Rental - Net Face (\$/sq m)	450	515	273	368
Incentive Level Net	35%	40%	35%	45%
Rental - Net Effective (\$/sq m)	235	260	115	175
Outgoings - Operating (\$/sq m)	70	105	65	90
Outgoings - Statutory (\$/sq m)	25	45	20	40
Outgoings - Total (\$/sq m)	95	150	85	130
Typical Lease Term	3	10	3	7
Yield - Market (% Net Face Rental)	5.75	6.50	7.00	8.25
IRR (%)	7.00	7.50	7.75	8.50
Cars Permanent Reserved (\$/pcm)	300	395	220	310
Cars Permanent (\$/pcm)	275	385	200	300
Office Capital Values (\$/sq m)	6,500	11,000	3,500	7,000

Source: Savills Research NB: All rents equivalent to whole floor mid-rise

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