

# Briefing Canberra Office

June 2019



## Highlights

- Average A and B Grade net face rents in Canberra Civic were recorded at \$370 and \$320 per square metre as at June 2019;
- Canberra witnessed over 105,000 square metres of leasing activity in the year to June 2019;
- Canberra saw over \$490 million of office deals transacted over the 12 months to June 2019;
- The vacancy rate has continued to trend downwards (11.4%), which is particularly evident in Civic (3.5%) and Barton (0.0%) as at Dec-18;
- Over 94,000 square metres are forecasted to enter the market by 2021.

A Grade Averages	Latest	Yr Change	Outlook
Rental – N.F. (\$/sq m)	370	+0.0%	↔
Net Incentives	17.5	+00bps	↔
Rental – N.E (\$/sq m)	285	-1.7%	↓
Yield – Market (%)	6.15	-10bps	↓
IRR (%)	7.50	-50bps	↓
Capital Values (\$/sq m)	7,300	+4.3%	↑

Demand & Supply	Latest	PCP*
Vacancy (%)	11.0	11.0
Net Absorb. ('000 sq m)	0.5	0.5
Stock U/C ('000 sq m)	94.2	65.2
- % of market	4.1	2.8
- % committed	50-	74.2

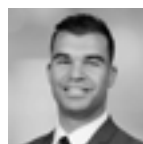
\*PCP = Previous Corresponding Period  
Source: Savills Research

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## Executive Summary

The Canberra office market consists of just under 2.32 million square metres of net lettable space (as at December 2018), split into 26 sub-localities. The largest precinct is Civic (Canberra's CBD) with 659,034 square metres. By grade quality, A Grade buildings account for the largest proportion of stock in Canberra, representing 48.3% of the market.

The performance of the Canberra office market is often resistant to the other major office market cycles in Australia. With the Government and Community sector the most dominant tenant type in the Canberra office market, (making up over 70% of total tenants as at December 2018) recent volatility in federal politics has caused consumer and business confidence to fall, which may have a tempering effect on leasing activity over the short to medium term.

Canberra's office market will be exposed to a surge of office supply from developments such as Constitution Place. Savills Research believes that co-working companies will be a contributing factor to the demand and success of these new developments.

## PCA Summary Table – Canberra (as at Dec-18)

	Prime	Secondary	Total	AUS CBD
<b>Total Stock ('000)</b>	1,113.2	1,204.7	2,317.9	<b>17,902.6</b>
<b>Total Vacancy ('000)</b>	57.9	196.1	254.0	<b>1,482.7</b>
<b>Vacancy (%)</b>	5.2 (11.2)	16.3 (13.3)	11.0 (12.3)	<b>8.3 (9.4)</b>
<b>Net Absorption ('000)</b>	35.2 (41.0)	-34.6 (-18.0)	.5 (23.0)	<b>230.7 (181.3)</b>
<b>Net Absorption (%)*</b>	3.4 (5.0)	-3.3 (-1.6)	0.0 (1.2)	<b>1.4 (1.2)</b>
<b>Net Additions ('000)</b>	-5.6 (39.7)	-53.6 (-5.0)	-59.2 (34.7)	<b>-46.2 (257.6)</b>
<b>- Stock Additions ('000)</b>	6.8	19.9	26.6	<b>317.8</b>
<b>- Stock Withdrawals ('000)</b>	12.3	73.5	85.8	<b>364.5</b>
<b>Net Additions (%)**</b>	-0.5 (4.5)	-4.3 (-0.4)	-2.5 (1.6)	<b>-0.3 (1.6)</b>

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

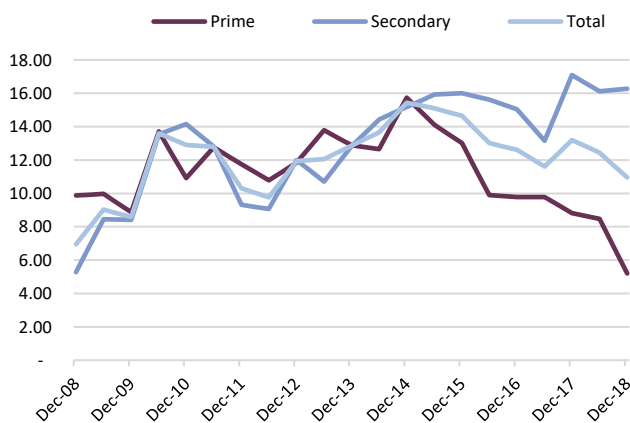
\*As a percentage of occupied stock; \*\*As a percentage of total stock

## Vacancy

As at December 2018, the overall vacancy rate of 11.0% demonstrated a decrease of 140 basis points from the June 2018 rate of 12.4%. The improvement over the year was driven primarily by net absorption throughout the six months to December 2018. The Prime Grade markets in Canberra, recorded a slight increase in vacancy to 16.3% remaining close to the record high levels that were seen in December 2017 (17.1%). The Canberra A Grade market has mirrored the total market vacancy movements with the vacancy rate now sitting at 4.9% from 8.5% in January 2018. This is mainly due to the Airport achieving a reduction in A Grade vacancy of 21.4% to 12.5%, the lowest levels since July 2006. CBD A Grade space reduced further to 1.7% in January 2019 and could now be considered under supplied until new developments reach completion in 2020-2021.

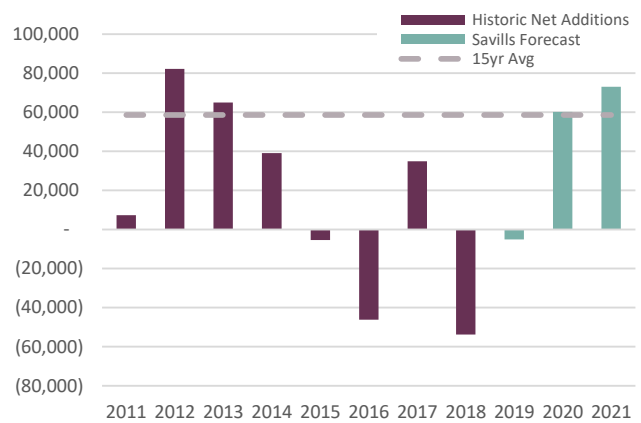
Savills expect the gradual tightening in vacancy to continue until the influx of developments (currently under construction) are presented to the market across 2020/2021. As a result of major infrastructure projects including the light rail network, it is expected that vacancy rates particularly within prime assets will continue to fall as demand for high quality office space remains strong.

Historic Vacancy (Canberra)



Source: Savills Research

Net Supply by Year



Source: Savills Research

## Supply

Canberra’s supply pipeline is expected to return to historical norms by the end of 2020 as we expect to see over 70,000 square metres of office space added when projects such as Constitution Place are completed. Approximately 50,000 square metres has already been pre-committed from tenants including Minter Ellison, KPMG and Access Canberra.

This additional supply will exceed the 15-year average. Savills Research believe the developments will be fully leased by the time they reach practical completion due to the recognisable demand for Canberra’s A Grade office space. Looking forward, it is highly unlikely that speculative office development will occur outside of the CBD and the Barton/Forrest precinct in the coming few years, without pre-commitments.

## Leasing Activity & Demand

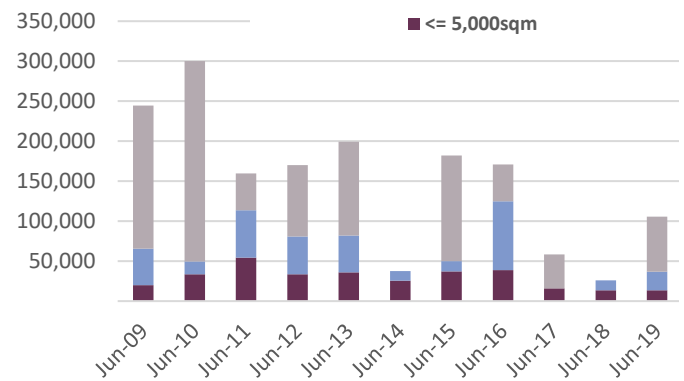
Savills Research identified just over 105,000 square metres of leasing activity (over 1,000 square metres) in Canberra’s office market throughout the year to June 2019. This is closely in line with the five year average (circa 108,000 square metres).

The majority of transactions in the 12 months to June 2019 fell between the 1,000-5,000 square metres category, with renewals made by Commonwealth Government departments. As expected, the ‘Government & Community’ sector dominated the leasing total, taking up approximately 90,000 square metres. This was largely due to the Department of Health and Ageing renewing their lease across 44,896 square metres at 23 Furzer Street, Phillip for an additional 10 years. They will pay a gross rental rate of \$510 per square metre.

Despite Government departments accounting for the majority of leasing activity (~93.0%), the ‘Finance and Insurance’ sector was next in line, taking up approximately 5,000 square metres of office space. Savills Research recognised consistent demand for A Grade space as 91,000 square metres of leasing activity (> 1,000 square metres) were in A Grade assets.

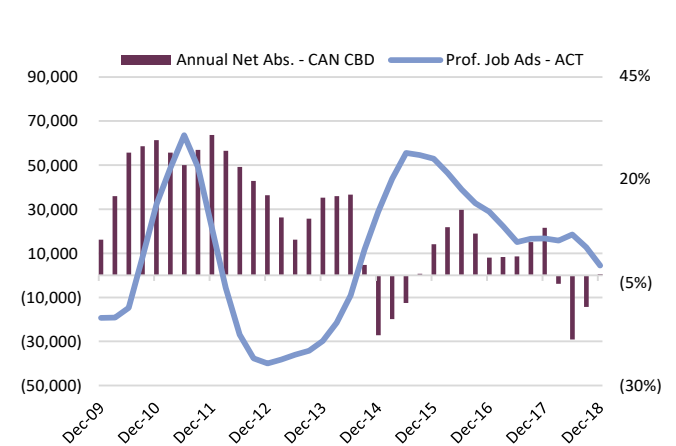
Savills Research anticipates that there will be increases to both rents and capital values as several large Commonwealth Government tenant briefs have recently been disclosed. Noteworthy briefs include the Department of Defence identifying the need for 30,000 to 65,000 square metres of office space as well as the Department of Agriculture and Water Resources requiring between 30,000 to 32,000 square metres of office space. These tenant briefs are likely to increase volumes of development applications.

Leasing Activity by Precinct (> 1,000 square metres)



Source: Savills Research

Net Absorption vs. Growth in Professional Job Ads



Source: Savills Research

## Recent Notable Leases (by Area Leased)

Property	Tenant	Date   NLA (sqm)	Type   Rent   Term
23 Furzer St, Phillip	Department of Health & Ageing	Feb-19   44,896	Renewal   510 (G)   10
23-25 Constitution Ave, Canberra	Commonwealth Government of Australia	Jul-18   9,747	Renewal   420 (G)   10
1 Dairy Rd, Fyshwick	Commonwealth of Australia	Jul-18   6,872	Direct   325 (G)   10
16 Marcus Clarke St, Canberra	National Health and Medical Research Council (NHMRC)	Feb-19   4,020	Direct   480 (G)   10
53 Wentworth Ave, Kingston	Leidos	Dec-18   3,861	Renewal   501 (G)   5
40 Macquarie St, Barton	Australian Strategic Policy Institute (ASPI)	Feb-19   2,047	Direct   390 (G)   7
121 Marcus Clarke St, Canberra	Regus	Jul-18   1,427	Direct   480 (G)   10
40 Blackall St, Barton	Adore Building	Nov-18   1,009	Renewal   390 (N)   1
16 Marcus Clarke St, Canberra	Boston Consulting Group	Jul-18   1,005	Direct   480 (N)   7

Source: Savills Research

## Sales

Savills Research recorded over \$490 million of office transactions (> \$5 million) in the 12 months to June 2019. This is 37% greater than the 12 months prior (\$357.2 million) and is higher than the 10 year average. In the year to June 2019, transaction numbers had increased, with 11 assets exchanging over the period.

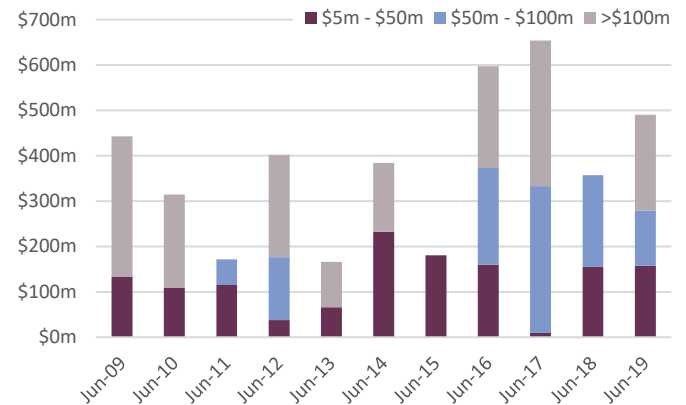
As expected, the activity within Canberra’s office market was dominated by domestic institutional investors, amounting to almost 60.0% of all transactional activity (> \$5 million) in the year to June 2019. This was largely contributed by Charter Hall acquiring A Grade office located at 16-18 Mort Street for \$108.5 million. The sale reflected a capital value of \$7,655 per square metre which sold on an equated yield of 5.85%.

Foreign Investors accounted for over 40.0% of transactional activity. This was largely contributed by Japanese fund, NTT Urban Development taking a 50% stake at 121 Marcus Clarke Street, for \$102.9 million. The sale of the A Grade office reflected a capital value of \$8,003 per square metre and was sold on an initial yield of 6.12%.

Market yields in Canberra Civic, as at June 2019, are estimated to range between 5.50% and 6.75% for A Grade office buildings, tightening 25 basis points in the high range during the year. Average B Grade office yields sharply tightened from 9.00% down to 8.15% across the same period, as lower-range yields reached levels of 6.25%.

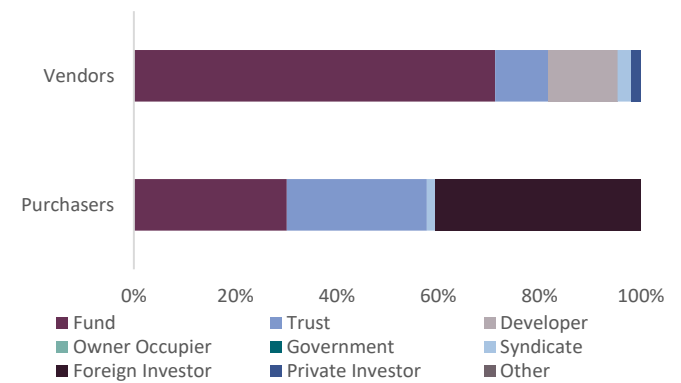
As at June 2019, A Grade capital values in Canberra Civic ranged from \$6,200 per square metre to \$8,500 per square metre, witnessing an average increase by 4.3% across the 12 month period. B Grade capital values ranged between \$4,000 per square metre and \$5,100 per square metre which equates to a 13.0% rise in average capital values over the year to June 2019.

### Sales Activity by Size (>\$5 million)



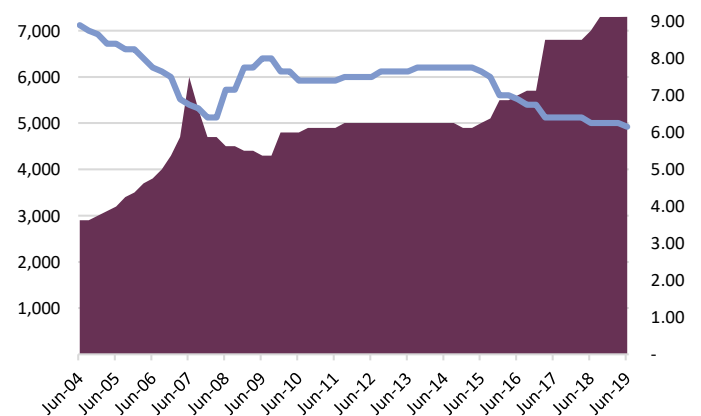
Source: Savills Research

### Vendor & Purchaser Type (>\$5 million)



Source: Savills Research

### Capital Values (\$/sq m)



Source: Savills Research

### Recent Notable Sales (by Sale Price)

Property	Price (\$m)   Date   NLA	Yield   Type   \$/sq m
16-18 Mort St, Canberra	108.50   Jun-19   14,155	5.85   e   7,665
121 Marcus Clarke St, Canberra (50.0%)	102.90   Apr-19   25,714	5.70   e   8,003
1 Constitution Ave, Canberra	62.00   May-19   28,519	n.a   n.a   2,174
14 Moore St, Canberra	59.00   Mar-19   11,047	6.30   e   5,341
14 Mort St, Canberra	51.00   Jun-18   9,384	6.35   e   5,435
10 Moore St, Canberra	35.00   May-19   6,709	6.65   e   5,217
24 Wormald St, Symonston	29.75   Mar-19   4,628	6.35   e   6,428
40 Macquarie St, Barton	29.00   Oct-18   5,444	6.70   e   5,327
17 Moore St, City	20.65   Oct-18   5,717	8.10   e   3,612
165 Canberra Ave, Fyshwick	11.50   Jun-18   3,277	6.94   e   3,509

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

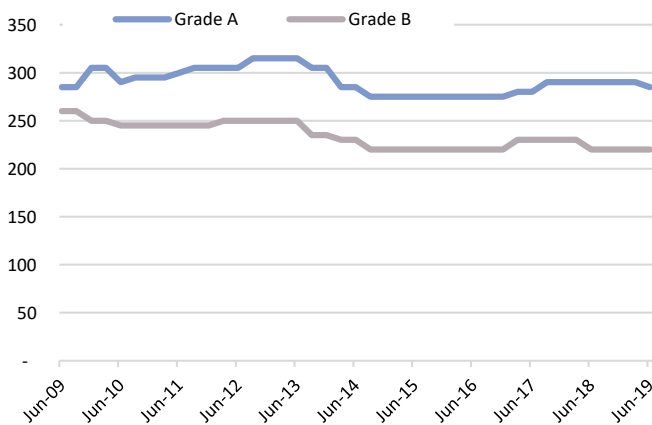
### Rents

Rents in Canberra traditionally exhibit lower volatility compared to other Australian CBD’s. This can be traced to the typically long-term lease structures of the most dominant lessee, the Commonwealth Government, with terms ranging from 10 to 15 years and fixed annual rental increases.

As of June 2019, average A Grade net face rents in the Canberra Civic precinct were at \$370 per square metre and \$320 per square metre for B Grade. On an effective basis, average A Grade rental rates were at \$285 per square metre where average B Grade net effective rents were at \$220 per square metre.

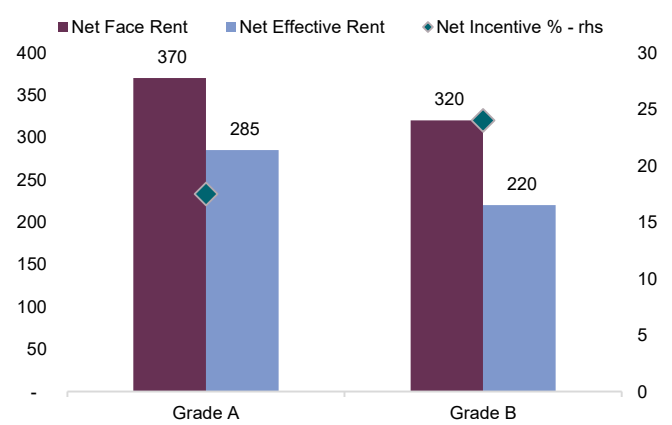
Average A Grade net incentives are recorded at 17.5% and average B Grade incentives at 24%, both not realising any change over the year period.

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



Source: Savills Research

Net Face & Net Effective Rents as at Jun-19 (\$/sq m)



Source: Savills Research

## Development

The table below details the major upcoming and planned development projects in the Canberra office Market.

Building Address	Dev Stage	NLA	Exp. Comp	Precinct	Tenant
72 Northbourne Ave	UC	16,000	2019	Canberra	
Cnr of Constitution and London Cct	UC	24,000	2020	Civic	ACT Government
Cnr Constitution and London Cct	UC	12,000	2020	Canberra	Minter Ellison, KPMG, Dixon Advisory, Kingwood Mallesons
Stage 1, 13-15 Challis St	UC	13,200	2020	Dickson	Access Canberra
90 Denison St	UC	8,000	2022	Deakin	
2 Darling St	PS	12,000	2021	Barton	
6 Brindabella Cct	UC	21,000	2021	Brindabella	
London Cct, Cnr Edinburgh Ave (Section 100)	EP	40,000	2022	Canberra	

Source: Savills Research; UC = Under Construction, DA = Development Approved, EP = Early Planning

## Outlook

The prospect of a more active Commonwealth Government sector has lifted sentiment in Canberra. Signs of recovery are already emerging, as indicated by the declining vacancy rate and modest effective rental growth. This follows a two year period of flat rental growth as market activity waned due to savings measures implemented by the Commonwealth Government, which took a toll on market activity and sentiment.

Savills Research anticipate the gradual tightening in vacancy to continue until the surge in new supply in 2020 / 2021 helps to alleviate pressure, particularly in the prime market. Modest growth in effective rents are a likely consequence, although confined to Civic and Barton, where acute vacancy rates (1.7% and 0.0% respectively) and strong demand maintain downward pressure on incentives. Savills Research anticipates a steady rise in pre-commitment volumes with the current shortage in available Prime Grade office space. The forecasted new developments planned for 2020 and beyond will definitely be a more viable option for occupants as rents remain affordable.

The market is experiencing a noticeable growth in co-working which has been highlighted by Regus, who recently opened their third co-working hub in Canberra Civic. Co-working will offer affordable rents and flexible terms which will continually attract to smaller to medium sized companies, aiding in the absorption of vacant office space. We expect this movement to further grow the demand for the Canberra office market in the short to medium term.

## Canberra Key Indicators (Q2-19)

	Civic				Non-Civic			
	A Grade		B Grade		A Grade		B Grade	
	Low	High	Low	High	Low	High	Low	High
Rental - Gross Face (\$/sq m)	440	500	400	435	400	500	365	400
Rental - Net Face (\$/sq m)	340	400	300	335	306	405	270	305
Incentive Level Net	10	25	18	30	15	25	18	30
Rental - Net Effective (\$/sq m)	265	315	205	230	225	305	180	210
Outgoings - Operating (\$/sq m)	55	70	60	70	55	70	60	70
Outgoings - Statutory (\$/sq m)	30	40	30	40	25	37	25	37
Outgoings - Total (\$/sq m)	85	110	90	110	80	107	85	107
Typical Lease Term	5	15	3	10	5	15	3	10
Yield - Market (% Net Face Rental)	5.50	7.00	6.50	10.00	5.50	8.25	7.25	11.00
IRR (%)	7.25	8.50	8.00	10.75	7.50	9.00	8.50	11.75
Cars Permanent Reserved (\$/pcm)	320	385	320	385	175	240	175	240
Office Capital Values (\$/sq m)	6,000	8,500	4,000	6,000	4,775	7,725	3,500	5,250

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



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