

Briefing West Perth Office

February 2017



Highlights

- Limited new supply in the pipeline for the West Perth market, with refurbishment of existing stock to drive activity in the short-term
- Savills identified approximately 35,500 square metres of leasing activity in the West Perth office market, in the 12 months to December 2016
- The average A Grade net face rent is \$325 per square metre per annum, a fall of approximately 13.0 percent in the last 12 months
- The majority of leasing deals reported in the 12 months to December 2016 were by the 'Property and Business Services' sector
- Savills has recorded approximately \$33 million worth of office transactions in the year to December 2016
- Market yields in West Perth typically range from 7.50% to 8.50% for A Grade, a 25 basis point firming over the year to December 2016

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\$33 million of
West Perth
office stock
sold in the 12
months to
December
2016

Savills Research
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Introduction

The West Perth CBD office market contains approximately 426,400 square metres of lettable space. Of this, approximately 138,500 square metres (32 percent) is of A Grade quality and the balance, approximately 287,900 square metres, is Secondary Grade.

Throughout this document rental rates reflect a net effective rent on a single, whole floor in the mid-rise of a building unless specifically otherwise stated.

Office Development

The West Perth office market has very few sites available for future development. In the short-to-medium term, there remains very little stock under construction in West Perth.

There is a mixed-use project at 957-959 Wellington Street that has development approval. However, the project is mooted for completion around 2018/2019 and is unlikely to go ahead without some pre-commitment. Plans include the construction of an eight level mixed-use building with four commercial tenancies covering approximately 1,414 square metres of office space.

Current West Perth CBD Office Development Activity

Property	Precinct	NLA (sq m)	Type	Status	Completion	Major Tenant(s)
957-959 Wellington St	West Perth	1,414	New	EP	Mooted	

Source: Cordell / Savills Research

UC: Under Construction

DA: Development Approval

EP: Early Planning/Development Application

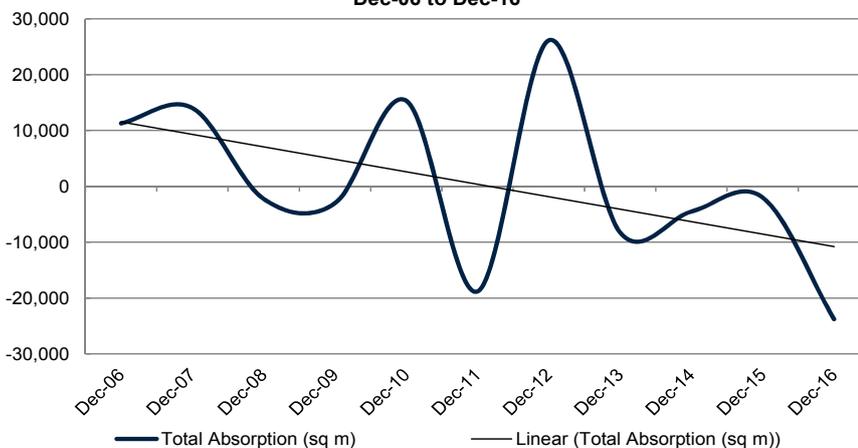
West Perth does have a high volume of ageing stock which presents a number of refurbishment and value-add opportunities. There are several existing tenancies which have low-cost upgrades to internal fitout either underway or in planning stage. We are likely to continue to see this trend moving forward.

Leasing Activity

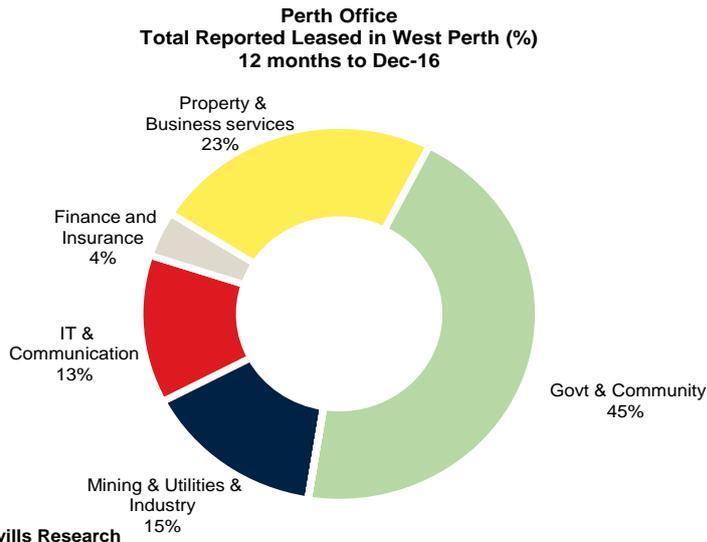
In the 12 months to December 2016, Savills identified approximately 35,500 square metres of leasing activity in the West Perth office market. This is an increase on the previous 12 months and above five year average of circa 22,500 square metres. These figures are reflective of publicly available transactions and may not represent the whole of the market.

By volume of space leased, 54 percent the deals identified were renewals, 41 percent were direct or new transactions, while the remaining 5 percent of activity was identified as sublease transactions. 'Property & Business Services' sector accounted for the greatest number of transactions.

**Perth Office
West Perth Net Absorption (sq m)
Dec-06 to Dec-16**



Source: Savills Research



A selection of recent leasing transactions is displayed in the table below.

Select West Perth Office Leases to December 2016

Date	Property	NLA (sq m)	Rent (\$/sq m)	Tenant
Aug-16	36 Parliament Pl	1,083	250	Oshgroup Pty Ltd
Aug-16	1060 Hay St	3,874 [#]	385	IBM
Aug-16	14 Ventnor St	267	na	JTMEC Pty Ltd
Oct-16	1101 Hay St	220	350	Engenuity Consulting Engineers
Nov-16	80 Colin St	900	na	Pilbara Minerals
Nov-16	836 Wellington St	11,973 [#]	467	Commonwealth of Australia

Source: Savills Research. NB – All rents equivalent to whole floor mid-rise na = not currently available or not disclosed *sublease #renewal

As at December 2016, net face rents in West Perth typically range from \$250 to \$400 per square metre per annum for A Grade and \$225 to \$275 per square metre per annum for B Grade. The average A Grade net face rent is \$325 per square metre per annum, a fall of approximately 13.0 percent on December 2015. The average B Grade net face rent is \$250, a decline of approximately 16.7 percent over the 12 months to December 2016.

Incentives began to rise in West Perth office market late 2013, resulting in a drop in face rents in 2014 and 2015. However, incentives have shown signs of stabilisation over the last two quarters.

Office Vacancy

The table below shows the breakdown of vacancy for West Perth office market. According to the Property Council of Australia (PCA), the West Perth office market vacancy as at December 2016 was 17.9 percent, an increase from 12.2 percent in December 2015.

West Perth Vacancy Rates – December 2016

Grade	Stock (sq m)	Vacancy (sq m)	Vac % Jan-17	Vac % Jan-16
A Grade	138,459	25,804	18.6	6.1
B Grade	176,068	28,835	16.4	13.6
C Grade	96,714	18,153	18.8	16.9
D Grade	15,114	3,545	23.5	21.2
Total	426,355	76,337	17.9	12.2

Source: PCA / Savills Research

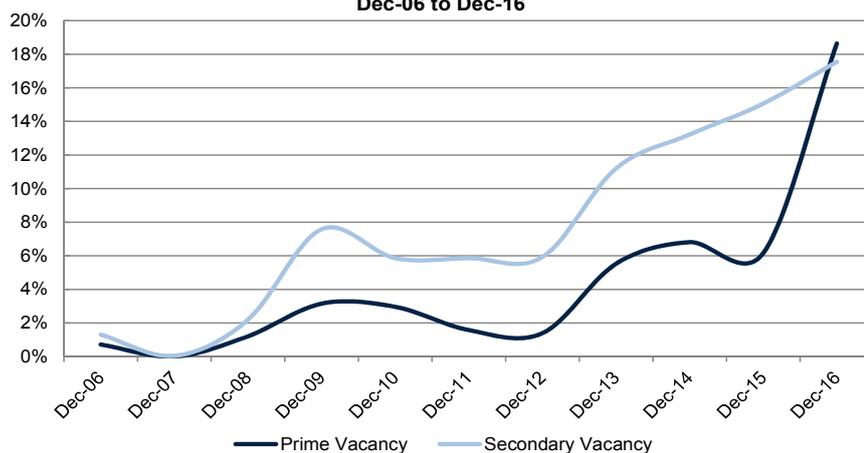
This is the highest vacancy rate in West Perth since early 1993 and comes off the back of 24 months of negative net absorption. The long-run average for the vacancy rate is about 9.0 percent.

While demand has fallen consistently since 2014, the largest decline in net absorption was recorded in the six months to December 2016. The decline in demand represents negative net absorption of 12,731 square metres in the last six months and almost 24,000 square metres over the year. West Perth is a small market and is sensitive to any shifts in demand.

There has been an increasing number of tenants relocating to the CBD from West Perth, legal firms in particular, which has underpinned the increase in the vacancy rate in the last 12 months. Recent examples include Bentleys and Donald Cant Watts Corke. Notwithstanding this trend, a slight increase in leasing transactions in the December 2016 quarter was recorded and this may not be reflected in the vacancy rate until mid-year.

There is now 76,337 square metres of vacant space in the precinct, up 24,592 square metres on the previous 12 months. Stock levels are unchanged. Both direct and sublease vacancy rates have increased, with sublease vacancy now 3.5 percent, up from 1.5 percent in January 2015 and direct vacancy 14.4 percent, up from 10.6 percent in January 2016.

**Perth Office
West Perth Vacancy by Grade (%)
Dec-06 to Dec-16**



Source: PCA / Savills Research

Sales Activity

Select West Perth Office Sales to September 2016

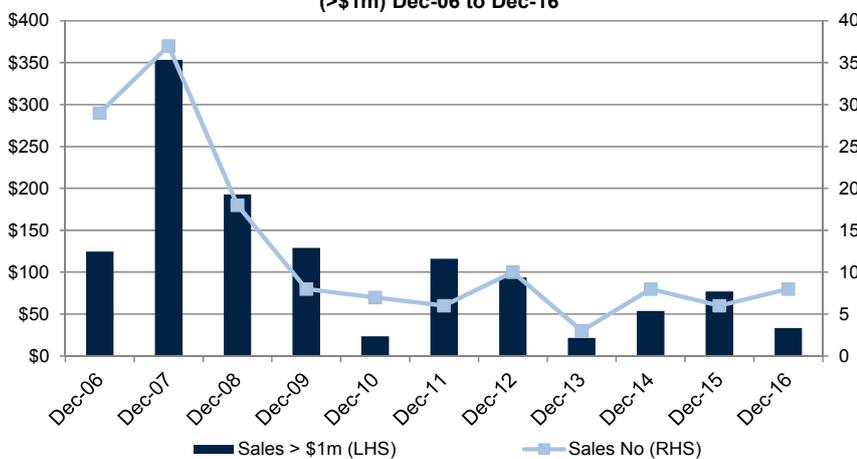
Date	Property	Price (\$m)	NLA (sq m)	\$/sq m	Yield (%)
Jun-16	10 Thelma St	1.35	180	7,488	VP
Jun-16	Unit 3, 14 Ventnor St	1.38	274	5,018	VP

Source: Savills Research

VP = vacant possession

Savills has identified approximately \$33 million worth of office transactions (greater than \$1 million) in the 12 months to December 2016 in the West Perth area. This is down from the \$77 million in the previous 12 months, and below the five year average of \$56 million. During the last 12 months, eight properties were identified as sold, up from the previous year of six, and up on the five year average of seven.

Perth Office
West Perth Office Sales (\$m and number)
(>\$1m) Dec-06 to Dec-16



Source: Savills Research

Traditionally, few major assets above \$25 million change hands in the West Perth market, with just two assets being exchanged in this price bracket over the last five years. The last being the sale of 53 Ord Street in 2015 to Singaporean REIT, Mapletree Investments for \$59 million.

Private investors were the most active buyers of the sales (\$1m+) identified in the 12 months to December 2016, followed by foreign investors - a trend not dissimilar to the last decade. The vendor profile for West Perth was also dominated by private investors.

The average sale price in 2016 was \$4 million and transactions were mixed between investment assets and those selling with vacant possession.

**Perth Office
West Perth Office Sales Vendor Profile
12 months to Dec-16**



Source: Savills Research

Market yields in West Perth as at December 2016 typically range from 7.50% to 8.50% for A Grade buildings, and between 8.25% and 9.50% for Secondary grade buildings. The average A Grade yield is currently 8.00%, representing a 25 basis point firming over the year.

Capital values in West Perth as at December 2016 typically range between \$2,950 per square metre to \$5,300 per square metre for A Grade buildings, and between \$2,400 per square metre and \$3,300 per square metre for secondary grade buildings. Average A Grade capital values are currently \$4,050 per square metre, a 11.0 percent fall over the 12 months to December 2016.

Key Market Indicators – December 2016

West Perth	A Grade		B Grade	
	Low	High	Low	High
Rental – Gross Effective (\$/sq m)	300	430	250	315
Rental – Net Face (\$/sq m)	250	400	225	275
Rental – Net Effective (\$/sq m)	155	250	140	175
Outgoings – Operating (\$/sq m)	80	90	50	55
Outgoings – Statutory (\$/sq m)	65	90	65	90
Outgoings – Total (\$/sq m)	145	180	115	145
Typical Lease Term (years)	3	5	3	5
Yield – Market (% Net Face Rental)	7.50	8.50	8.25	9.50
IRR (%)	8.00	8.75	8.00	10.00
Cars Permanent Reserved (\$/pcm)	300	325	300	350
Cars Permanent (\$/pcm)	325	350	300	325
Office Component Capital Values (\$/sq m)	2,950	5,300	2,400	3,300

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

Rental rates reflect single, whole floor, net effective and mid-rise rental rates unless specifically otherwise stated. Discounts and premiums exist for low and high rise space for significant occupiers.

Outlook

There has been some confidence returning to the mining and resources sector off the back of a stabilisation in iron ore prices at the end of 2016 and a number of producers are looking at new project investments for 2017 as a result. In addition, the announcement in December 2016, that from March 2018, Perth will have a regular non-stop flight route to and from London, bodes well for both consumer and business confidence. This may help drive a slight improvement in demand over the medium-term.

Leasing enquiry is typically isolated to tenant renewal or relocation plans, with most considering occupancy options well before current lease expiry. This is unlikely to change in the short-term.

As mentioned in the previous briefing, with favourable incentives on offer for CBD located assets, there may be some reshuffling of tenants into the CBD and likewise, inner suburban to West Perth location. In the short-term, this has appeared to place upward pressure on the vacancy rate, particularly in A grade buildings. With numerous prime options available in the CBD for sub 1,000 square metre tenants, this trend could potentially extend for another quarter at least.

There remains limited activity above 1,000 square metres. However, moving forward we may see an increase in these transactions as there are a number of larger occupiers in the precinct considering renewal options in the next two years.

Although there has been an increased focus on the Western Australia market from both domestic and offshore capital, chasing value-add / counter-cyclical opportunities, interest has mostly been directed to the CBD market. There have been limited major assets come to the market from West Perth, with investment activity narrowing to the sub \$10 million segment. It is likely this trend will continue in the short-term, as private investors and owner occupiers continue to look for entry-points into the West Perth as a counter-cyclical play.

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