

# DYNAMIC OFFICE MARKET UPDATE

11.11

## Economic Overview

Amidst deepening economic uncertainty in the USA and Europe, the Australian economy has continued to consolidate, albeit with subdued GDP growth. Expectations of economic growth in the developed world are downward trending, which has led to a continually downward trending share market and widespread wealth reduction. Australia has some exposure to issues abroad, however between a strong resource sector and steady immigration, we are likely to see small but continued growth in the Australian economy.

## Occupancy

Modest growth in the Australian economy has been translated into positive net absorption of office space in the 6 months to July 2011 across all major capital cities. Demand for office space combined with small increases in supply resulted in a general decline in vacancy levels, down from 8.7% to 8.4% - the exception being the Sydney CBD where vacancy rose from 8.3% to 9.3%, mainly a result of 2 new buildings coming online: Darling Quarter being 56,000m<sup>2</sup> (fully leased to CBA), and 1 Bligh Street being approx. 43,200m<sup>2</sup> (56% leased to Clayton Utz). Perth and Brisbane experienced the largest reductions in vacancy, from 10.2% to 7.8% and 9.4% to 7.4% respectively.

| Economic Indicators                                  | Australia        |      |
|--|------------------|------|
| GDP June 2011<br>(Seasonally Adjusted)               | Quarterly Change | 1.2% |
|  | Yearly Change    | 1.4% |
| CPI September 2011<br>(Seasonally Adjusted)          | Quarterly Change | 0.4% |
|  | Yearly Change    | 3.5% |
| RBA Cash Rate  | Currently        | 4.5% |
|  | Nov 2010         | 4.5% |
| Unemployment Rate<br>(Seasonally Adjusted)           | October 2011     | 5.2% |
|  | October 2010     | 5.3% |
| Retail Trade August<br>2011<br>(Seasonally Adjusted) | Monthly Change   | 0.6% |
|  | Yearly Change    | 2.1% |
| NAB Business<br>Confidence (Base 100)                | September 2011   | 98   |
|  | September 2010   | 110  |

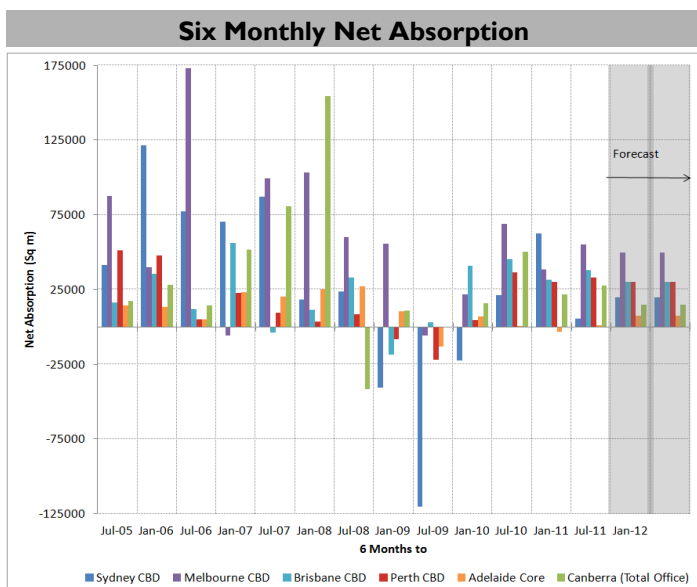
Source: ABS, RBA, NAB.

Uncertain global economic conditions continue to impact the office markets, resulting in a lack of business confidence and a corresponding decrease in demand for office space. This has impacted on the level of development activity and restricted supply levels (in most capital cities), resulting in relatively stable vacancy levels. New supply is predominantly pre-committed and the backfill space left by those tenants has resulted in vacant areas typically being of large size. Current demand is such that the backfill space is being absorbed.

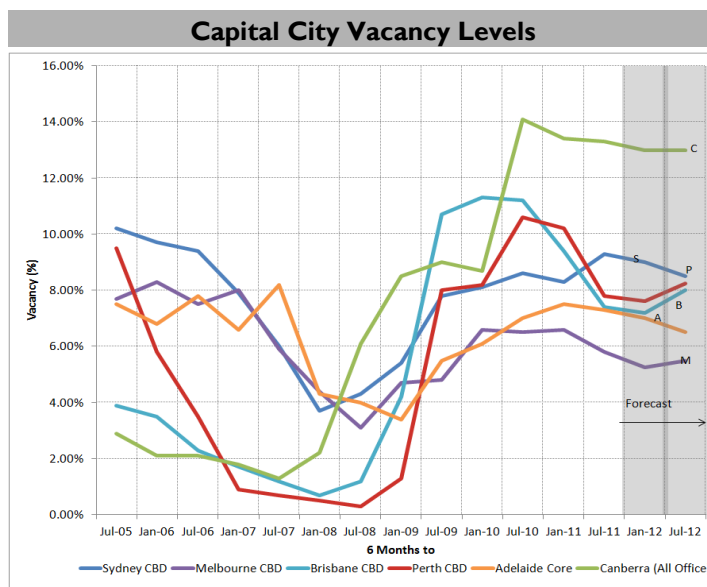
| CBD Net Face Rents | Sydney         | Melbourne     | Brisbane      | Perth         | Adelaide      | Canberra      |
|--------------------|----------------|---------------|---------------|---------------|---------------|---------------|
| Premium & A-Grade  | \$550 - \$1100 | \$400 - \$625 | \$500 - \$725 | \$600 - \$850 | \$275 - \$425 | \$300 - \$400 |
| B-Grade            | \$425 - \$550  | \$275 - \$375 | \$350 - \$500 | \$400 - \$600 | \$200 - \$325 | \$225 - \$300 |
| Incentives (net)   | 20% - 30%      | 10% - 25%     | 15% - 30%     | 0% - 15%      | 0% - 20%      | 10% - 25%     |

Note: Indicative only.

In the current economic climate, tenants are reluctant to commit to wholly funding their office fit-outs. This in turn is increasing pressure on Landlords to maintain a high level of incentive in order to fund the majority, if not all the cost of a tenant fit-out. As demand for office space strengthens and new buildings come on-line, we expect tenant demands for fit-out incentives to remain high, and an increase in face rents is expected.



Source: PCA, Property Dynamics. Note: Forecasts are indicative only.



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## Sales & Investment

While the outlook for the domestic economy has been lacklustre, the outlook in the USA and Europe is significantly worse. Prime assets (especially in the Sydney CBD) have experienced increased foreign investment through 2011, and this trend looks set to continue given Australia's high interest rates and stable economy. In the meantime, domestic institutional investors have experienced slightly eased credit conditions, and have remained very active in the major CBD marketplaces. These factors, combined with some rental growth, have resulted in firming yields and increased capital values - especially for prime assets.

Looking ahead, we expect transactional activity will remain buoyant and yields to continue tightening over the next 12 - 24 months.

| CBD Office Yields | Sydney       | Melbourne     | Brisbane      | Canberra     | Adelaide     | Perth        |
|-------------------|--------------|---------------|---------------|--------------|--------------|--------------|
| Premium & A-Grade | 6.25% - 7.5% | 6.75% - 7.75% | 7.0% - 8.25%  | 7.0% - 8.0%  | 7.5% - 9.5%  | 7% - 8.5%    |
| Secondary         | 7.5% - 9.0%  | 8.0% - 9.25%  | 8.25% - 9.75% | 9.0% - 11.0% | 8.5% - 10.0% | 8.5% - 10.0% |

Note: Indicative only.

## Directions Summary

|                       |   |   |                          |   |  |
|-----------------------|---|---|--------------------------|---|--|
| <b>Leasing Demand</b> | ↔ | Overall stable  | <b>Rental Incentives</b> | ↔ | Generally steady due to fit-out financing difficulties |
| <b>Supply</b>         | ↓ | Generally lowering of supply levels given pre-commitments on development pipeline | <b>Yields</b>            | ↓ | Slight tightening as rentals increase                  |
| <b>Vacancy</b>        | ↔ | Expected to be relatively stable  | <b>Capital Values</b>    | ↑ | Increasing moderately                                  |
| <b>Rental Levels</b>  | ↑ | Increasing moderately   | <b>Sales Activity</b>    | ↔ | Recently increased activity to remain buoyant          |

*Disclaimer: Please note that information provided above has been based on a varying range of resources. Figures quoted are approximate and indicative only and should not be relied upon other than for a general guide of the current market conditions. All figures and commentary relate to Australian CBD Office properties valued over \$5 million. If you wish to receive more specific advice regarding any of the above information please contact our offices during business hours on 1300 883 609 or at [info@propertydynamics.com.au](mailto:info@propertydynamics.com.au).*

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