RESEARCH

APRIL 2011

PERTH CBD OFFICE

Market Overview

Knight Frank

HIGHLIGHTS

- 134,815m^2 of office space is under construction in the Perth Central Business District. 102,018m^2 was completed during 2010.
- The Property Council of Australia's (PCA) total vacancy rate as at January 2011 was 9.5%, down from 9.9% in July 2010. There was 66,670m^2 of net absorption during the twelve months to January 2011.
- Knight Frank calculates the current real vacancy rate at 5.3% - being office space actually available for lease.
- There is downward pressure on incentives and upward pressure on rents for Prime-grade property. Prime-grade rents now range from \$525 to \$825 per m^2 p.a. net face. Secondary-grade property rents have remained stable over the past year at \$400 to \$475 per m^2 p.a. net face.
- Major transactions in the Perth CBD totalled \$146.45 million during 2010, with over \$300 million contracted or under due diligence in the first quarter of 2011. Average investment yields remain stable at market based rates of around 8.00%- 8.25% for Prime assets.

PERTH CBD OFFICE

Market Overview

Table 1

Perth CBD Office Market Indicators as at April 2011

Grade	Total Stock (m²) ^	Vacancy Rate (%)^	Annual Net Absorption (m²)^	Annual Net Additions (m²) ^	Average Net Face Rent ($/m²)	Avg. Incentive Range (%)	Avg. Core Market Yield Range (%)
Prime	798,841	7.4%	87,876	90,481	671	0.0 – 15.0	7.50 – 8.50
Secondary	666,736	12.1%	-21,206	3,349	446	15.0 – 20.0	8.50 – 10.00
Total	**1,465,577**	**9.5%**	**66,670**	**93,830**			

Source: Knight Frank/PCA ^ as at January 2011

ECONOMIC OVERVIEW

The beginning of 2010 saw strengthening in the Western Australian economic environment with confidence returning to the marketplace as a result of improved local, national and international conditions. The demand for resources by foreign markets and increased commodity prices have seen companies' grow in the Perth Central Business District (CBD), requiring additional staff and thus office space to meet the growing demand.

Politics over 2010 did impact on the local office market, with the Federal Government's announcement of the Resource Super Profits Tax (RSPT) in April almost halting leasing enquiries in the market as uncertainty loomed regarding the tax and resource companies fought against its implementation. A change in Federal Labor leaders and the announcement of an early Federal election during quarter three cast further nervousness over the market, particularly with the subsequent outcome of the election being a stalemate.

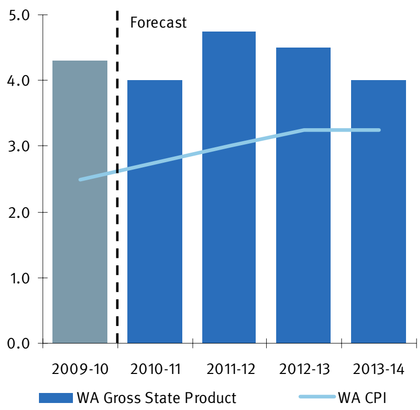
Since then, the political environment has settled and the resource sector has continued to strengthen through to the first quarter of 2011.

The Western Australian economy continues to grow strongly. Gross State Product increased in real terms by 4.3% during 2009-10 as a result of activity in the mining, oil and gas sectors. Growth in the State is forecast to remain stable in the coming years, particularly with sustained economic recovery in the global market.

Figure 1

Forecast Economic Growth

% p.a. Real Gross State Product Growth



Source: State Government of Western Australia

Strong economic growth in Western Australia has seen high employment within the State, the unemployment rate being the lowest of all Australian States at 4.2% in February 2011 (5.0% for Australia), with forecasts by the State Government predicting unemployment to remain low through to 2013-14.

Positive net overseas and interstate migration has contributed to a growth of 2.1% in population over twelve months. The Australian Bureau of Statistics estimates the population of Western Australia to be 2,306,200 as at September 2010. This was the highest growth recorded for all Australian States.

Western Australia maintained its position as the dominant exporter in the Australian economy in the twelve-month period to January 2011, accounting for 44% of the total value of Australian merchandise exports (over $233 billion exported from Australia).

The Department of Mines and Petroleum has calculated that the resource sector currently has over $150 billion worth of projects either committed to or under consideration in Western Australia. Further to this, the State Government has $7.9 billion worth of non-resource projects underway, including the Fiona Stanley Hospital ($2.0b), Perth City Link ($656m), Perth Arena ($536m) and the Perth Waterfront ($440m).

OVER $150 BILLION WORTH OF RESOURCE PROJECTS COMMITTED OR UNDER CONSIDERATION IN WESTERN AUSTRALIA

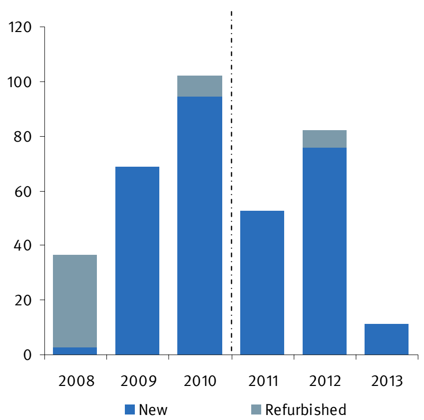
SUPPLY & DEVELOPMENT ACTIVITY

Development Cycle

Unprecedented demand for office space and corresponding low vacancy rates during the resources boom resulted in strong rental increases in the Perth CBD which supported the viability of new development. The 2010 calendar year saw the highest level of supply additions to the market as a result of the development boom, with 94,593m^2 of new stock and 7,425m^2 of refurbished space completed during the year.

Major projects completed during 2010 included Dynons Plaza (13,200m^2), 226 Adelaide Terrace (13,594m^2), 140 William Street (36,000m^2), Alluvion (21,980m^2), Westralia Plaza (9,819m^2), and 50 St Georges Terrace (7,425m^2 refurbishment).

Figure 2
New Supply, Perth CBD
New and Refurbished Stock ('000m^2)



Source: Knight Frank/PCA

The 2011 year should see a further 52,815m^2 of new office space come on to the market, with an additional 82,000m^2 of new and refurbished space due for completion in 2012. Beyond this time, there is the development of the Melbourne Hotel site at 942 Hay Street, incorporating the original heritage-listed building into a new 11,219m^2 building. This potentially is slated for completion by the end of 2013 at the earliest. Recent reports have noted the "Treasury" project coming back online, with 29,000m^2 of new development and refurbishment of the old building (8,000m^2). With no firm confirmation of this project to date, this has not been included in Knight Frank's forward projections.

The recent announcements of these new developments in the CBD will help curb the future space shortage, particularly in Prime-grade buildings.

Commitment Levels

Strong rental growth during the previous resources boom and high levels of pre-commitment to new buildings supported development in the current building cycle. Stock under construction and due for completion in 2011 is approximately 85% pre-committed, with stock due in 2012 approximately 93% pre-committed.

With the majority of space completed during 2010 fully absorbed and a pre-commitment of 90% to buildings currently under construction, companies seeking new space will have to look at future backfill or sub-lease opportunities in order to expand as new supply levels remain tight.

Development Sites

Last year saw the sale of three major development sites in the Perth CBD – 32 St Georges Terrace, 123 St Georges Terrace and the old Emu Brewery site at 98 Mounts Bay Road.

A receivership sale, 123 St Georges Terrace was purchased by Brookfield Multiplex in October for $23million from The Griffin Group. The 3,400m^2 site adjoins the City Square development site and has approval for a 14-level tower. This site sold at a rate of $6,765 per m^2 on the land area.

The 1.8 hectare site at 98 Mounts Bay Road sold for $54.45 million in August 2010 ($3,022 per m^2). This site was sold under instructions from receivers and proposals have included a 5-star hotel, premium office space and/or residential apartments.

The May Holman Centre at 32 St Georges Terrace sold for $30.0 million in June 2010 to an international investor. The site currently has a vacant building of 8,806m^2 ($3,407 per m^2) and a land area of 2,557m^2 ($11,732 per m^2) and was sold under receivership.

The number of development site sales is encouraging, showing growing confidence in the market both towards new office and residential developments. As an indication, Perth CBD land values are estimated at around $2,500 to $4,000 per m^2 in the eastern CBD, and between $5,000 and $10,000 per m^2 for Prime commercial/residential sites in the central and western sectors.

Table 2
New Office Development Perth CBD

Market	Status	2011 (m^2)	2012 (m^2)	2013 (m^2)	2014 + (m^2)
Raine Square, 300 Murray St	UC	43,000			
181 Adelaide Terrace	UC	7,115			
507 Murray Street	UC	2,700			
City Square, St Georges Terrace	UC		82,000		
Melbourne Hotel, Hay Street	DA Approved			11,219	
Potential Development 2014 *	Mooted				66,810
TOTAL		52,815	82,000	11,219	66,810

Source: Knight Frank * Knight Frank estimates of potential future space UC = Under Construction

TENANT DEMAND & RENTS

The Property Council of Australia (PCA) noted in its January 2011 report that the Perth CBD had a stock level of 1,465,577 m² of office space. The vacancy was 139,899 m², being 9.5%. Of this, direct vacancy was 86,030m² (5.9%), up by 0.2% over the July 2010 figure. Sub-lease vacancy dropped modestly during the six-month period to January 2011, with 53,869m² of space available (3.7%).

Knight Frank's calculation of vacancy, as at March 2011, is only 5.3%, and is based on space actually available for lease and takes into account pre-committed space.

Figure 3
Historical Vacancy, Perth CBD
Prime and secondary grade buildings

Source: PCA

Knight Frank expects that Secondary-grade buildings will be vulnerable to long-term vacancy as the overall standard of accommodation in the Perth CBD increased as a result of the recent building cycle. This is now reflected in the sharp increase in total vacancy rate for Secondary-grade buildings (B, C and D grades) to 12.1%. Historically, Prime-grade properties have tracked in similar ways to Secondary-grade properties (as can be seen in Figure 3), but the release of recent figures by the PCA in January 2011 is showing a greater variation in vacancy rates between the two grades of buildings. Prime-grade assets have had higher levels of absorption and therefore a reduced vacancy rate, as compared to twelve months ago.

Table 3
Perth CBD Vacancy Rates
Prime vs. Secondary

Grade	Vacancy % Jan 2010	Vacancy % Jan 2011
Prime	8.0	7.4
Secondary	8.5	12.1
Total	**8.2**	**9.5**

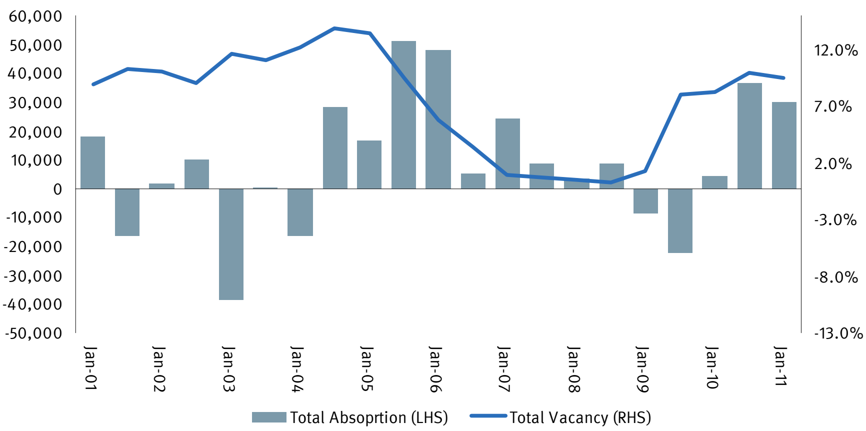
Source: PCA

Net Absorption

During the resources boom, net absorption levels decreased as the level of available stock reduced as the market went close to a 0% vacancy. As the Global Financial Crisis (GFC) hit, the twelve-month period to July 2009 saw negative net absorption recorded for the first time since 2004 and vacancy levels spike dramatically to 8.0%.

With continued demand from our main trading partners for resources mined in the State, confidence in the economy has brought about a demand for more space within the Perth CBD, and net absorption has increased as a result.

Figure 4
Net Absorption, Perth CBD
('000m²) Net Absorption vs. Total Vacancy (%)



Source: PCA

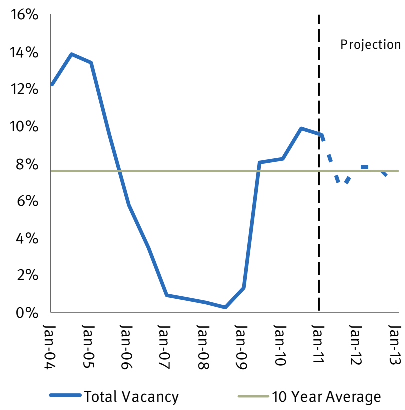
As with historical vacancy rates, Prime-grade assets have shown the greatest level of absorption over the last twelve to eighteen month period – some 99,287m² of space has been absorbed in this grade over the past eighteen months.

Anticipated Vacancy Levels

PCA analysis has the January 2011 total vacancy level at 9.5%, which includes the unoccupied space at 140 William Street (36,000m²), Westralia Plaza (9,819m²) and 226 Adelaide Terrace (13,594m²). The majority of these new buildings are pre-committed to tenants (95%).

It is anticipated that the vacancy rate will fall from 9.5% to 6.6% by July 2011 as a result of absorption of the stock completed in 2010 and additional space absorption driven by strong recent demand. Anticipated new supply completions of 52,815m² during the year will see the vacancy rate rise again, albeit modestly, to around 7.8% by the close of 2011. New stock completing in 2012 will see the vacancy rate remain steady, but with this space fully committed, and minimal predicted backfill space available, Knight Frank anticipates that the vacancy rate will fall to 6.7% by the end of 2012. Beyond this, stock withdrawals from the office market and minimal supply additions should see the total vacancy rate fall further, fuelling the next supply cycle.

Figure 5
Total Vacancy, Perth CBD
Historical and Anticipated Levels



Source: PCA/Knight Frank

Tenant Demand

Office space west of Barrack Street continues to be highly sought after, but as this space is absorbed we are seeing a trend of space being taken up outside this core area. This is shown by FMG taking up an additional 12,760m² of space at the Hyatt Centre, Shell moving into 2 Victoria Avenue, and ENI taking over 4,672m² of space at 226 Adelaide Terrace.

Rental Levels

The beginning of 2010 saw the stabilisation of face rents with upward pressure on incentives beginning to dissipate within the market as a result of the increasing demand for space as confidence within the economy improved.

Indicators show that within the Perth CBD, Prime net face rents have increased over the past six months, and Secondary-grade net face rents have remained stable.

Prime net face rents on average are now considered to be between $525 and $825 per m² with incentives at an average of 10% (down from 17.5% at the beginning of 2010). As pre-commitment levels are high for new stock under construction, Knight Frank anticipates that upward pressure on rental levels will be placed on existing available stock.

The vulnerability of Secondary-grade assets in the market at present is being seen, where net face rents are on average between $400 and $475 per m² and incentives remain at approximately 15-20%.

Dynons Plaza on Hay Street was completed during 2010 and has been fully leased to Chevron for 10 years

PRIME GRADE ASSETS HAVE HAD HIGHER ABSORPTION AND HENCE A REDUCED VACANCY RATE

Table 4
Recent Leasing Activity Perth CBD Office Market

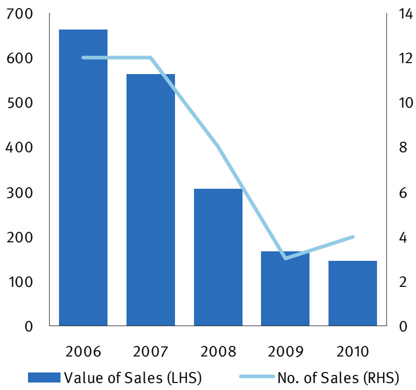
Address	Area (m²)	Face Rental ($/m²)	Term (yrs)	Lease Type		Start Date
226 Adelaide Terrace	2,247	550 n	10	Direct	New	May 2011
2 The Esplanade	1,030	790 n	3	Direct	New	Feb 2011
503 Murray Street	1,180	450 n	7	Direct	New	Jan 2011
256 St Georges Terrace	12,500	525 n	6	Direct	New & Renewal	Jan 2011
15 William Street	2,146	575 n	5	Direct	Renewal	Dec 2010
Forrest Centre	1,732	650 n	4	Direct	New	Dec 2010
15 William Street	1,235	600 n	4	Direct	New	Dec 2010
226 Adelaide Terrace	4,672	550 n	10	Direct	New	Nov 2010
12-14 The Esplanade	1,029	625 n	6	Sub Lease	New	Nov 2010
Central Park	2,640	725 n	10	Direct	New	Jul 2010
226 Adelaide Terrace	4,336	600 n	10	Direct	New	Jul 2010
Hyatt Centre	12,760	425 n+	10	Direct	New & Renewal	Jun 2010
QV1	19,363	720 n	7	Direct	New & Renewal	Jan 2010

Source: Knight Frank   n = net   *Knight Frank's estimation of incentive calculated on a straight line basis   + Average

INVESTMENT ACTIVITY & YIELDS

Eight major sales have occurred in the Perth CBD since the beginning of 2010. Of these, three were for development sites, each with an element of distress attached to the sale.

Figure 6
Perth CBD Sales Transactions
($ mill) Sales Value ›$10 mill & No. of Sales



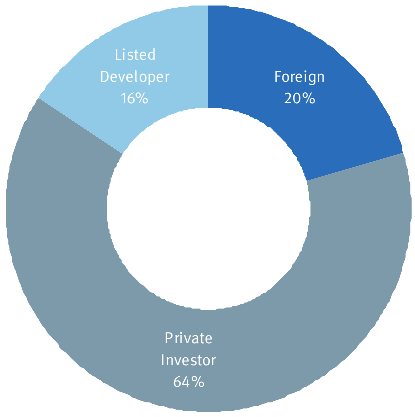
Source: Knight Frank

Overall, the market has been challenging due to the low availability of finance, although high net-worth individuals, syndicates and overseas buyers have gone against this trend and have been the largest group of investors in Perth property over the past twelve to eighteen months. The high Australian dollar has impacted upon overseas buyers, limiting interest from this sector of the market.

Minimal transaction activity from institutional investors has occurred during 2010 in the Perth CBD, with the only sale being the Brookfield Multiplex purchase of 123 St Georges Terrace. However, this has picked up during the beginning of 2011 and at present a 50% share in QV1 has been reported to be under due diligence for a consideration of more than $300 million by an institutional investor.

The start of 2011 has seen strong transactional activity in the market, with four properties under contract or settled at a value of almost $275 million. These sales include 99 St Georges Terrace, 182 St Georges Terrace, 30 The Esplanade and 197 St Georges Terrace with 1 and 5 Mill Street. We are presently aware of another commercial transaction in the due diligence stage for a consideration of around $30 million.

Figure 7
Purchaser Profile, 2010 Calendar Year
Sales Value ›$10 mill



Source: Knight Frank

Commercial transaction activity within the office market is expected to increase further during 2011, with purchaser confidence being boosted by reducing vacancy levels and improved prospects of rental growth across the markets. Continued project commissioning within the resources sector and the associated take-up of large tranches of office space should continue to rejuvenate

Table 5
Sales Activity – 2010/11 Perth CBD

Address	Price ($ mil)	Core Market Yield (%)	NLA (m²)	$/m² NLA	Vendor	Purchaser	Sale Date
30 The Esplanade *	50.0	8.40	7,003	7,140	AMP	API	Feb 2011
99 St Georges Tce *	41.6	8.40	6,161	6,752	Private Investor	Private Investor	Jan 2011
197 St Georges Tce, 1 & 5 Mill St *	152.0	10.60^	26,553 13,502	3,795^	Colonial First State Property Limited	GDI Property Group	Jan 2011
182 St Georges Tce *	31.0	8.85	5,317	5,830	Hawaiian Group	Standard Life	Jan 2011
123 St Georges Tce	23.0	Site	3,400 ‘	6,765 ‘	The Griffin Group	Brookfield	Oct 2010
98 Mounts Bay Rd	54.45	Site	18,017 ‘	3,022 ‘	Turnstone Nominees	AAIG Pty Ltd	Aug 2010
Kings Complex, 517 Hay St	38.0	8.90	4,841	2,479	Private Investor	Private Investor	Jun 2010
32 St Georges Tce	30.0	VP	8,806	3,407	Investec	Private Investor	Jun 2010

Source: Knight Frank ^ Analysed in one-line * Under Contract VP = Vacant Possession ‘ Site m² and $/m² site
Core Market Yield: the percentage return/yield analysed when the assessed fully leased market income is divided by the adopted value/price which has been adjusted to account for property specific issues (i.e. rental revisions, rental downtime for imminent expiries, capital expenditure, current vacancies, incentives, etc)

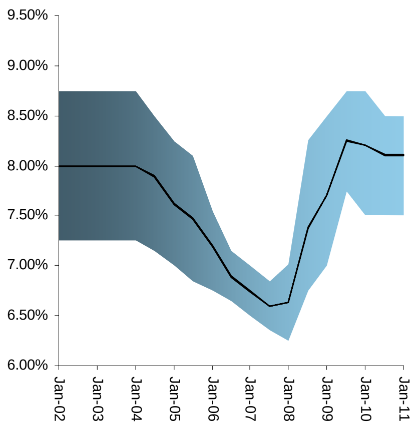
the market, particularly for Prime assets. We are also now beginning to see renewed institutional interest in the Perth market.

Yields or capitalisation rates within the office market remain stable with no major yield compression evident. Core market yields for Prime assets range from 7.5% and up to 8.5%, but centred around 8.00%-8.25%. Secondary core market yields are slightly higher at around 8.5% to 10.0%. Purchasers remain yield conscious, so that low-yielding properties remain difficult to transact.

Figure 8

Yields, Perth CBD

Prime Core Market Yield Range



Source: Knight Frank

OUTLOOK

That last twelve months has seen resilience in the economy and strengthening conditions which has buoyed confidence in the market. The PCA indicated that during this time the Perth CBD recorded 66,670m² of space being absorbed by the market as the space requirements of companies grew in line with growth in the resources sector.

This period also saw 102,018m² of office stock completed, with an additional 134,815m² due for completion to the end of 2012. Beyond this, the previously mooted Melbourne Hotel redevelopment at 942 Hay Street will bring a further 11,219m² of space to the market at the earliest in 2013. Knight Frank's calculations estimate that there is over 190,000m² of office space mooted, which includes the Treasury Building at 37,000m².

Knight Frank has calculated the actual real Perth CBD office vacancy at 5.3%, based on space actually available for lease as at March 2011. The next six months will see vacancy levels fall further as stock continues to be absorbed by the market, despite additional stock completing later this year.

From the start of 2012 a modest rise in the vacancy rate is anticipated as backfill space from Bankwest Tower comes onto the market following the completion of Raine Square. Further to this, City Square is expected to be completed during the year, but with this space 100% pre-committed, minimal backfill space available, and combined with the anticipated strong absorption levels, the vacancy rate is predicted to taper moving into 2013.

Gross State Product is expected to grow on average by 4.3% per year for the next 4 years, led particularly by the State's strong resources sector. Strong business sentiment has been pivotal for confidence in the market and the flow-on effects have included a strong demand for labour, both in the Perth CBD and regional areas.

Sustained economic growth in the State will ensure continued upward pressure on Prime net face rents and downward pressure on incentives as the availability of space within Prime-grade assets reduces. It is anticipated that as the availability of office space within Prime assets reduces, space within Secondary grade assets will be absorbed, placing pressure on incentives and rents.

Yields have remained stable over the past twelve months and are expected to remain so over 2011, with limited or no real yield compression anticipated.

197 St Georges Terrace with 1 and 5 Mill Street sold in January 2011 for $152 million. The buildings (total NLA 40,055m²) were sold by Knight Frank to GDI Property Group with a core market yield of 10.6% (analysed in one-line).

SUSTAINED ECONOMIC GROWTH IN THE STATE WILL ENSURE CONTINUED UPWARD PRESSURE ON PRIME NET FACE RENTS

RESEARCH

Americas
USA
Bermuda
Brazil
Canada
Caribbean
Chile

Australasia
Australia
New Zealand

Europe
UK
Belgium
Czech Republic
France
Germany
Hungary
Ireland
Italy
Monaco
Poland
Portugal
Romania
Russia
Spain
The Netherlands
Ukraine

Africa
Botswana
Kenya
Malawi
Nigeria
South Africa
Tanzania
Uganda
Zambia
Zimbabwe

Asia
Cambodia
China
Hong Kong
India
Indonesia
Macau
Malaysia
Singapore
South Korea
Thailand
Vietnam

The Gulf
Bahrain
Abu Dhabi, UAE

Knight Frank Research

Matt Whitby
National Director – Research
+61 2 9036 6616
Matt.whitby@au.knightfrank.com

Alison Smith
Research Analyst – WA
+61 8 9225 2434
Alison.Smith@au.knightfrank.com

Jennelle Wilson
Associate Director – Research QLD
+61 7 3246 8830
Jennelle.wilson@au.knightfrank.com

Nick Hoskins
Research Manager – NSW
+61 2 9036 6766
Nick.Hoskins@au.knightfrank.com

Justin Mahnig
Research Manager – Vic
+61 3 9604 4713
Justin.Mahnig@au.knightfrank.com

Matthew Mason
Research Analyst –SA
+61 8 8233 5232
Matthew.mason@au.knightfrank.com

Commercial Agency Contacts

Gary Ryan
Managing Director, Western Australia
+61 8 9225 2402
Gary.ryan@au.knightfrank.com

John Corbett
Director, Agency
+61 8 9225 2561
John.corbett@au.knightfrank.com

Greg McAlpine
National Director, Office Leasing
+61 8 9225 2426
Greg.mcalpine@au.knightfrank.com

Ian Edwards
Director, Asset Services
+61 8 9225 2420
Ian.edwards@au.knightfrank.com

Valuation Contact

Marc Crowe
Director, Valuations
+61 8 9225 2521
Marc.crowe@au.knightfrank.com

Knight Frank Research provide strategic advice, consultancy services and forecasting to a wide range of clients worldwide including developers, investors, financial and corporate institutions. All recognise the need for the provision of expert independent advice customised to their specific needs.

Knight Frank Research reports are also available at www.knightfrank.com.

Knight Frank Newmark Global