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BECAUSE TOMORROW MATTERS

INDEPENDENT MARKET STUDY REPORT

2020

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As one of Singapore's REIT pioneers, Ascendas Reit has played a crucial role in the development of the Singapore REIT sector. It provides an attractive platform for investment in business and industrial properties across developed markets.

Ascendas Reit owns and manages a well-diversified portfolio, valued at S$13.7 billion, comprising 200 properties in Singapore, Australia, the United Kingdom (UK) and the United States (US).

Ascendas Funds Management (S) Limited (AFM), the manager of Ascendas Reit (the Manager), is a wholly owned subsidiary of Singapore-listed CapitaLand Limited (CapitaLand), one of Asia's largest diversified real estate groups.

VISION

To be a leading global real estate investment trust

MISSION

To deliver predictable distributions and achieve long-term capital stability for Unitholders

For more information, visit our website www.ascendas-reit.com

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As part of its environmental conservation efforts, Ascendas Reit continues to print limited copies of its Annual Report. PDF versions of its Annual Report, Independent Market Study Report and Integrated Sustainability Report are available for download from the corporate website: ir.ascendas-reit.com/ar.html.

Feedback
The Manager strives to continuously improve its business and sustainability practices. Stakeholders are encouraged to share their views, suggestions or feedback, which may be directed to a-reit@capitaland.com.

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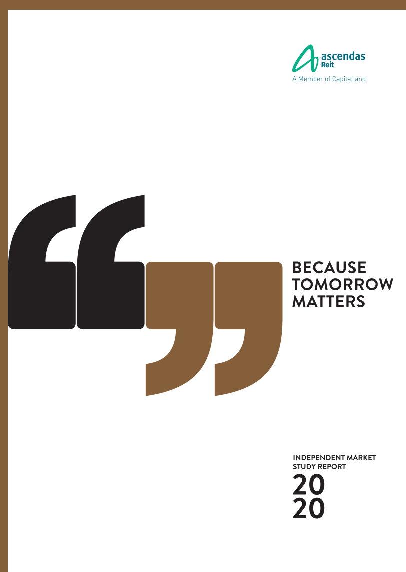


Underpinning the breadth of CapitaLand's activities is our continuous dialogue with our stakeholders which helps to shape our business as we aim to build sustainable communities. We place significance on our conversations and share our story with care and consideration for all involved. This annual report is part of that process and the motif we have chosen for this year's report reflects our focus on maintaining communication with our stakeholders with transparency and clarity.

SINGAPORE

INDEPENDENT MARKET STUDY

By Edmund Tie & Company (SEA) Pte Ltd

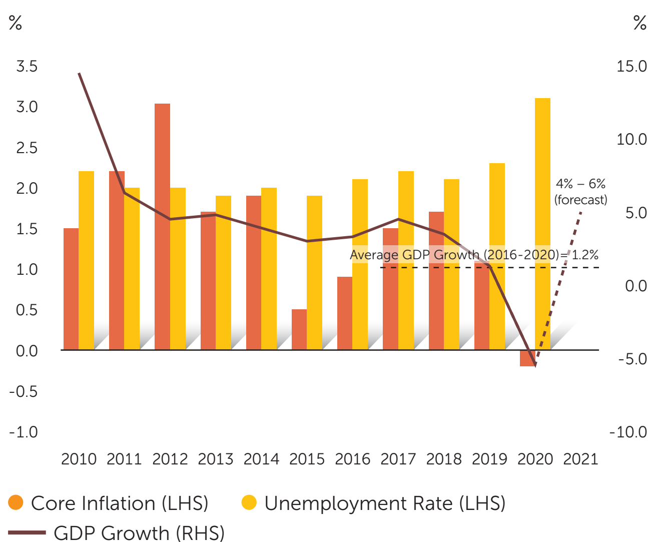
1.0 ECONOMIC OVERVIEW

Despite the COVID-19 outbreak in 2020, Singapore's economy is on track for gradual recovery in 2021, though global headwinds and uncertainties remain

In 2020, Singapore's gross domestic product (GDP) contracted by 5.4% amid a global pandemic-led downturn. The economy experienced deflation for the first time in almost two decades. The swift policy response by the government helped moderate the overall unemployment rate from a high of 3.8% in 2Q20 to 2.8% in 4Q20.

The manufacturing sector remained an economic bright spot, expanding by 9.5% y-o-y in 4Q20 and extending the 10.8% growth in 3Q20, supported by output expansions in the electronics, biomedical manufacturing and precision engineering clusters. The Index of Industrial Production, an indicator for manufacturing output, increased by 14.3% y-o-y in December 2020 on the back of an expansion in the electronics cluster (41.8%), chemicals (12.3%), precision engineering (11%) and general manufacturing (5.9%).

FIGURE 1: GDP GROWTH, CORE INFLATION[1] AND UNEMPLOYMENT



Source: Department of Statistics Singapore (DOS), MTI

While the roll-out of approved COVID-19 vaccines in Singapore has lifted business sentiment, the rebound of Singapore's economy to pre-pandemic levels will remain highly dependent on the global economic recovery and the state of COVID-19 containment both globally and domestically. MTI's growth forecast for 2021 as at 15 February 2021 is 4 to 6%.

2.0 KEY GOVERNMENT POLICIES AND PLANS

Formation of the Southeast Asia Manufacturing Alliance (SMA) to promote manufacturing activities in the region

Launched in February 2021, the SMA is a tripartite agreement between the Singapore Economic Development Board (EDB), Enterprise Singapore (ESG), and key private sector partners with the intent of reducing the barriers to entry for the manufacturing sector in the region. The agreement entails the formation and promotion of a network of participating industrial parks for global firms that are keen to strengthen their manufacturing footprint in Singapore and the region. Firms could also benefit from a differentiated tier of pricing for logistics service and complimentary consultation services for business set-up. Consequently, the demand for Business Park (BP) and Industrial spaces is likely to be positively impacted.

Budgeting for a Agri-Food Cluster Transformation Fund (AFCTF) to support technology adoption in the food sector

As part of the Singapore Budget 2021, a new $60-million AFCTF has been created to support the relevant firms' adoption or advancement of technology in the realm of food production. In view of the likely continuation of border controls due to COVID-19, which has implications on food imports, local food supply resilience will remain a key concern of the government. The demand and the use of Agriculture and Industrial land and spaces are likely to increase, in response to the government's continued efforts to ramp up local food production yields in order to achieve the nation's target of meeting 30% of its nutritional needs by 2030.

Continuation of grants and support to encourage digitalisation and adoption of technologies by local enterprises

The government has signalled a clear intent to aid local businesses through the continued provision of grants and supports that encourage enterprises to adopt technologies and digital platforms for their businesses. The 2020 Budget provided for a Digital Resilience Bonus (DRB) to support Small Medium Enterprises' (SME) digitalisation efforts, such as adoption of e-Payment modes and digital platforms for ordering of takeaways. Other digitalisation schemes include the Industrial Digital Plans, which provides trainings to Small Medium Enterprises (SMEs) on relevant, industry-appropriate digital solutions, or the newly-drafted Digital Leaders Programme and the Emerging Technology Programme, which aim to equip or co-fund local companies' trials and adoption of frontier technologies like 5G and Artificial Intelligence (AI). This is likely to sustain the trend of brick-and-mortar businesses moving onto the various digital platforms, which in turn supports demand for logistics and warehousing spaces.

1 Core inflation defined by the Monetary of Singapore is a measure that excludes the components of "Accommodation" and "Private Road Transport".

SINGAPORE
INDEPENDENT MARKET STUDY
By Edmund Tie & Company (SEA) Pte Ltd

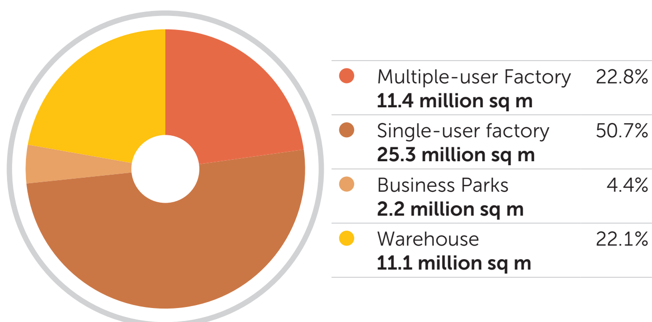
Unveiling of the Singapore Green Plan 2030 to guide the nation's medium-term sustainability plan

Announced in February 2021, the Singapore Green Plan 2030 a multi-ministerial concept plan to further Singapore's agenda on sustainable development. Some key goals of the Green Plan include ramping up the use of solar energy and sustainable fuels, as well as importing and promoting the use of cleaner-energy cars and Electric Vehicles (EV). The Green Plan is a signal of the government's sustainable land use strategy for the industrial sector over the next 10 years. The Green Plan is likely to continue facilitating the entry of key global players in the domain of sustainable development, such as Dell Technologies[2] and Hyundai[3], which in turn will buoy demand for industrial land and spaces.

3.0 INDUSTRIAL PROPERTY MARKET OVERVIEW

As at Q4 2020, about 50 million sq m[4] of industrial space is estimated island-wide, of which 86.9% (43.5 million sq m) is private stock. 50.7% (25.3 million sq m) of the total stock is single-user factory, followed by multiple-user factory (22.8%, 11.4 million sq m), warehouse (22.1%, 11.1 million sq m) and business parks (4.4%, 2.2 million sq m) (Figure 2).

FIGURE 2: ISLAND-WIDE INDUSTRIAL STOCK, IN NET LETTABLE AREA (NLA) (Q4 2020)



Source: JTC

Government Land Sales Program

The Government has lined up three sites each in the Confirmed List and the Reserve List in the H1 2021 Industrial Government Land Sales (IGLS) Programme, totalling some 3.86 hectares (ha). This marked a sharp drop from the 7.11 ha of industrial land offered a year ago in the H1 2020 IGLS Programme, reflecting the government's deliberate intent to curb the industrial supply. When combined, the Confirmed and Reserve Lists can potentially yield some 22,500 sq m and 37,200 sq m of NLA to the total pipeline supply respectively, a marginal increase of 0.12% relative to the current stock of 50 million sq m. All the land plots in the IGLS Programme are zoned Business 2 (B2) and all the sites are essentially small plots of 1.0 ha or smaller. With the exception of two plots on the Reserve list with 30-year leasehold tenure, the remaining plots are offered with 20-year leasehold tenure, in an effort to keep industrial land affordable for small industrialists. The largest plot offered (by GFA) is a 0.76 ha plot at Woodlands Industrial Park E7/E8, which can yield 19,000 sq m of space based on a gross plot ratio of 2.5.

Major Investment Sales

The largest transaction for industrial properties in 2020 was the sale of Alexandra Technopark by Frasers Commercial Trust to Frasers Logistics and Industrial Trust[5] for $606 million ($610 per sq ft per NLA) (Table 1). The second largest transaction ($223.6 million) was by Ho Bee Land, winning the concept and price tender to build, own and operate Biopolis Phase 6 at one-north. The 12-storey mixed-used facility is expected to be completed in 2022 and will add another 35,000 sq m of business park space for biomedical sciences (BMS) research and 6,000 sq m for office and retail use. While purchases were largely driven by domestic entities, the ongoing sale of The Sandcrawler by Lucasfilm to the Blackstone Group demonstrates continued interest in quality industrial assets by foreign groups. If successful, The Sandcrawler sale at a proposed price of $175.8 million will mark the third largest transaction for the year.

2 Dell Technologies has launched a Research & Redevelopment centre in Singapore to drive innovation in edge computing.
3 Work has commenced for Hyundai's $400 million EV-manufacturing plant in Jurong Innovation District and is expected to complete by the end of 2022.
4 All data on areas are NLA unless otherwise stated.
5 Now known as Frasers Logistics & Commercial Trust.

TABLE 1: SELECTED INDUSTRIAL INVESTMENT TRANSACTIONS (2020)

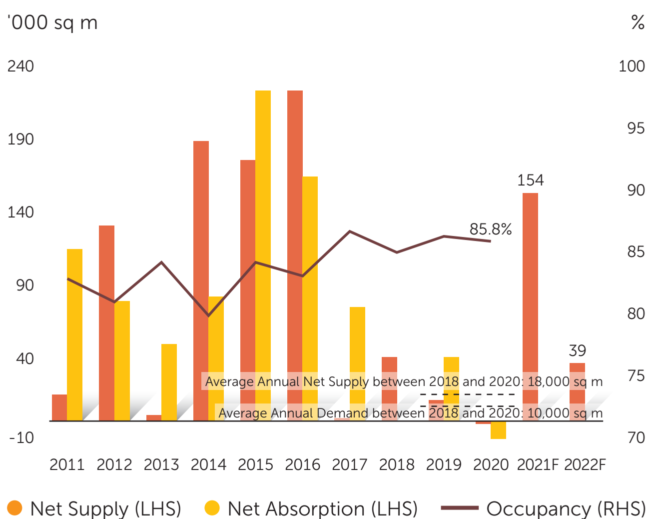
Development	Land Lease Tenure	Site Area (sq m/sq ft)	GFA (sq m/sq ft)	Vendor	Buyer	Transacted Price (S$ million)	Unit Price per GFA (S$ per sq ft)
Light Industrial							
Alexandra Technopark	99-year leasehold from 2009	–	95,939 / 1,032,679 (Net Lettable Area)	Frasers Commercial Trust	Frasers Logistics and Industrial Trust	606	610 (per NLA)
Big Box	30-year leasehold from 2007	56,645 / 609,725	130,064 / 1,400,000	Receivers & Managers Appointed of Big Box Pte Ltd	Perennial Real Estate Holdings, HPRY Holdings Limited and other investors	118	84
Thye Hong Centre	Freehold	5,952 / 64,067	13,641 / 146,832 (Net Lettable Area)	Thye Hong Properties	SLB Development	112.5	766 (per NLA)
Wisma Gulab	Freehold	5,070 / 54,576	11,821 / 127,240 (Net Lettable Area)	Ascendas REIT	Heap Seng Group	88	692 (per NLA)
Luxasia Building	30+30-year leasehold from 2007	7,950 / 85,573	–	Luxasia Group	PGIM Real Estate	66.1	772 (Land Premium)
Fraser and Neave	60-year leasehold from 1986	47,608 / 512,448	43,850 / 472,000	Coca-Cola Singapore Beverages	Wilmar International	29.5	63
International Press Building	60-year leasehold from 1990	4,998 / 53,798	12,500 / 134,549	International Press Softcom	Storhub Group	26	193
Tuas Techpark	60-year leasehold from 1993	7,968 / 85,764	9,975 / 107,373	Concrete Innovators Co. Pte Ltd	Chip Eng Seng Corporation Ltd	25	233
Business Park							
TH2-1 one-north	60-year leasehold from 2020	7,521 / 80,955	41,366 / 445,254	JTC	Ho Bee Land	223.6	502
The Sandcrawler (ongoing, pending regulartory approval)	30+30-year leasehold from 2010	6,817 / 73,377	22,297 / 240,000	Lucas Real Estate Singapore	Blackstone Group	175.8	733
Galaxis (25% stake)	60-year leasehold from 2012	19,283 / 207,560	68,835 / 740,933	Mitsui & Co	Ascendas REIT	102.9	850
Data Centre							
26A Ayer Rajah Crescent	30-year leasehold from 2013	10,214 / 109,942	35,749 / 384,800	Mapletree Industrial Trust	Equinix	125	325
Media Centre	60-year leasehold from 1980	24,892 / 267,935	–	SPH	SPH and Keppel Corporation	50	187 (Land Premium)
Warehouse							
7 Bulim Street	30-year leasehold from 2012	34,095 / 366,995	68,190 / 733,990	Titan (Wenya)	AIMS Apac Reit	129.6	177
25 Changi South Street 1	56-year leasehold from 1964	–	13,998 / 150,673	Ascendas REIT	Hao Mart Pte Ltd	20.3	135

Source: JTC, various REITs, OneMap, EDMUND TIE Research (as at 10 February 2020)

4.0 BUSINESS PARK

Demand for business park space was subdued but should pick up as the economy improves in 2021. Rents could still decline in 2021, with newer business parks being more defensive.

FIGURE 3: NET SUPPLY, NET ABSORPTION AND OCCUPANCY (BUSINESS PARKS)



F refers to forecast.
Source: JTC, EDMUND TIE Research

Stock and Supply

Total business park space was broadly unchanged at 2.2 million sq m as at Q4 2020, with 84.9% of the total stock being privately held (1.9 million sq m). The year saw just one business park asset completed: 15 International Business Park with 14,500 sq m of space. Net supply increase in 2020 was -2,000 sq m, significantly below the robust supply increases of 2014-2016 (196,000 sq m average per annum).

Demand and Occupancy

Occupancy for business parks declined in the East region

Despite the draw of business parks as vibrant and amenity-filled campuses for technology companies, the segment is not immune to the subdued business climate. In 2020, net absorption was -12,000 sq m, a decline from the 43,000 sq m recorded in 2019. Although demand held up in the Central and West Regions, it fell in the East Region. Net absorption was -13,000 sq m in the East Region in 2020, compared with -1,000 sq m in 2019.

The overall occupancy rate of business park space dipped slightly by 0.4 percentage points to 85.8% in 2020. The occupancy rate improved by 0.8 percentage points to 72.8% in the West Region while it declined by 2.5% to 82.1% in the East Region, with developments such as UE Biz Hub East and Changi Biz Park Central 2 listing an increased number of vacant units over the course of 2020. The occupancy rate was highest at 91.1% in the Central Region, unchanged from a year ago.

Potential Supply

Bulk of pipeline supply for business park space is in Jurong Innovation District

About 188,000 sq m (GFA) of business park space is expected in 2021, yielding an estimated 154,000 sq m in NLA (Table 2). The key supply coming forth in 2021 is from the JTC-developed Cleantech 3[6] located at Cleantech Park, Surbana Jurong Campusand the Grab HQ development by Ascendas Reit at Media Close. The Surbana and Grab HQ developments are already fully committed by the end-users. In 2022, Ho Bee Land will be developing a 29,000 sq m NLA business park as Biopolis Phase 6 in the one-north precinct.

6 Cleantech 3 will be an integrated development by JTC, for research laboratories and start-ups.

TABLE 2: PIPELINE SUPPLY (2021 TO 2024, BUSINESS PARK)

Development	Developer/ Owner	Location	Region	GFA (sq m)	NLA (sq m)
2021					
CleanTech Three	JTC Corporation	Cleantech Loop	West	61,690	50,586
Surbana Jurong Campus	Surbana Jurong Capital (JID) Pte Ltd	Cleantech Loop	West	41,350	33,907
Business park development	Ascendas REIT	Media Close	West	36,770	30,151
2022					
Business park development	HB Universal Pte Ltd	North Buona Vista Drive	Central	35,160	28,831
2023					
Business park development	CapitaLand Singapore (BP&C) Pte Ltd	Science Park Drive	Central	112,530	92,275
Business park development	Science Park Property Trustee Pte Ltd	Science Park Drive	Central	28,820	23,632
2024					
Business park development	JTC Corporation	Punggol Way	North-East	226,650	185,853

Source: JTC, EDMUND TIE Research

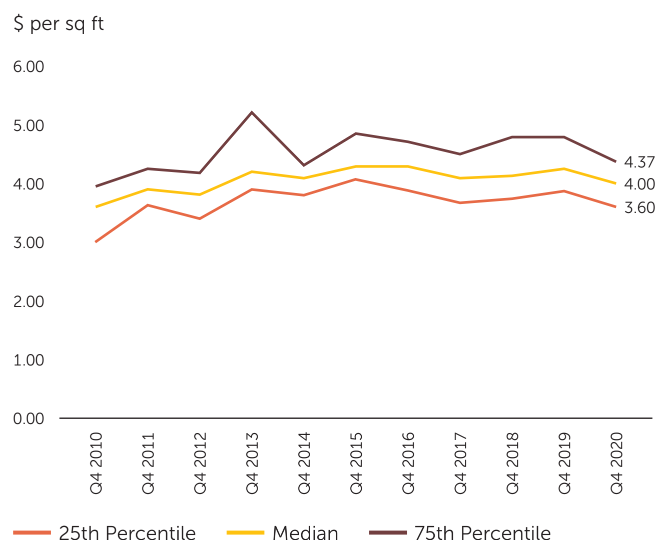
Rents

Despite the lack of supply pressures, the subdued demand for business park space led to downward pressures on rents. JTC's business park Rental Index declined by 1.1% in 2020. The 75th percentile rent[7] declined by 8.9% in 2020 to $4.37 per sq ft per month. The declines for the median rent and the 25th percentile rent[8] were more moderated, at 7.0% and 5.8% respectively. With the prevalence of work from home practices in 2020, the focus on cost savings rather than the appeal of decentralised quality spaces may have led to the more defensive outcome for aged assets (Figure 4).

Outlook

The economic realities remain sombre and business park rents are expected to continue to decline in 2021, albeit at a lower rate compared to 2020. As the economy gains a stronger footing in 2021, demand for business park spaces by bio-medical research & development, technology and e-commerce companies could return. Strong commitment rates for upcoming supply will mitigate the supply pressure. Quality business park space remains as an attractive alternative to office space in prime locations and rents of newer business parks are expected to decline by 0-1% in 2021, while rents for older spaces in business parks located in the West and East Regions could witness larger declines.

FIGURE 4: RENTS (BUSINESS PARK)[9]



Source: JTC, EDMUND TIE Research

7 75th percentile rents is a proxy for better and newer business park spaces.
8 The 25th percentile rents generally represents transactions in older stock.
9 Refers to gross rent per month including service charge but excluding Goods and Services Tax (GST).

SINGAPORE

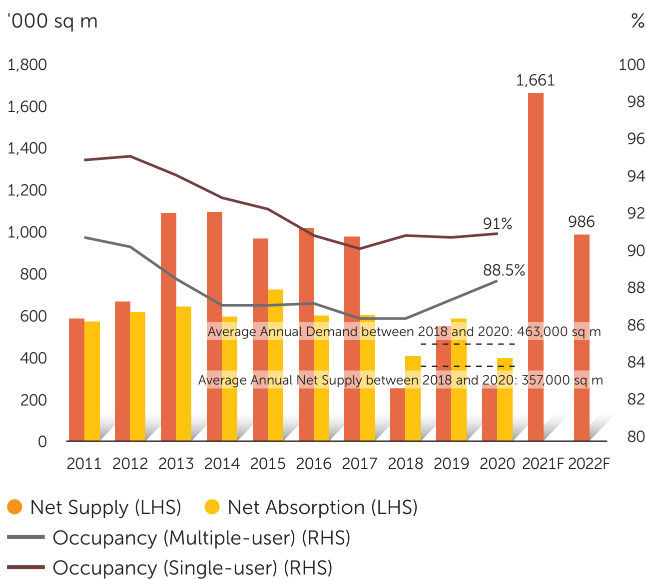
INDEPENDENT MARKET STUDY

By Edmund Tie & Company (SEA) Pte Ltd

5.0 HIGH-SPECS AND LIGHT INDUSTRIAL SPACE

The improving manufacturing outlook is counterbalanced by political uncertainties and greater supply pressures. Rents could post a slight decline in 2021.

FIGURE 5: NET SUPPLY, NET ABSORPTION AND OCCUPANCY (MULTIPLE-AND-SINGLE-USER FACTORY SPACE)



F refers to forecast.
Source: JTC, EDMUND TIE Research

Stock and Supply

In 2020, the total factory stock comprising high-specifications (or high-specs) industrial and light industrial space grew by 0.7% (270,000 sq m) to 36.7 million sq m. About 11.3% of this stock is high-specs industrial spaces (excluding data centres)[10].

There was one data centre completed in 2020, developed by Singapore Technologies Electronics with about 17,000 sq m NLA.

Demand and Occupancy

Net absorption for factory space weakened amid headwinds but occupancies improved

Overall demand for factory space moderated in 2020 amid headwinds from the border closures and declines in global manufacturing and trade; net absorption declined to 397,000 sq m from 585,000 sq m in 2019. The West Region proved to be the bright spot, recording an increase in demand from 214,000 sq m in 2019 to 273,000 sq m in 2020, likely due to the completion of several major industrial projects throughout 2020, such as Hup Hin Property's factory at 5 Tuas Ave 5 with a NLA of 41,131 sq m completed in Q1, and Tiong Lian Food's Tiong Lian Building at 202 Pandan Loop with a NLA of 10,414 sq m, completed in Q3. Although absorption was negative in Central Region in 2020, it was significantly lower than that in 2019 (-25,000 sq m vs -105,000 sq m). Positive net absorption helped improve occupancies nonetheless; the islandwide occupancy rate for multiple-user factory space rose by 1.0 percentage points to 88.5% in 2020 while single-user factory space rose by a more moderate 0.2 percentage points to 91.0%.

Potential Supply

Upcoming supply largely comes from Defu Industrial City

The pipeline of factory space for 2021 and 2022 stood at 2.3 million sq m NLA (6.4% of existing stock). The bulk (around 1.5 million sq m) will come onstream in 2021. Single-user factory constitutes 45.3% of the supply pipeline for factory space over the next two years.

About 304,000 sq m (GFA) of the 2021-2022 pipeline supply are expected to be high-specs industrial space, including 146,000 sq m (GFA) of data centres (Table 3). The most significant supply of factory space in 2021 is the development of Defu Industrial City (326,000 sq m GFA) by JTC, which features single-storey terrace workshops to four-storey industrial shops and land-based prototype factories. When completed, Defu Industrial City will be mainly occupied by tenants and lessees of land-based factories at the Defu Industrial Estate, who will be relocated in view of the site's impending redevelopment under JTC's Industrial Redevelopment Programme. In 2022, the completion of JTC Space @ AMK will bring forth 117,000 sq m GFA of factory space.

10 Based on EDMUND TIE's estimates.

TABLE 3: SELECTED PIPELINE SUPPLY (LIGHT INDUSTRIAL, HIGH-SPECS AND DATA CENTRES)

Development	Developer/ Owner	Location	Region	GFA (sq m)	NLA (sq m)
2021					
Light Industrial					
JTC Defu Industrial City	JTC Corporation	Defu South Street 1	North-East	325,770	267,131
Single-user factory	Malkoha Pte Ltd	Sunview Way	West	171,340	140,499
TimMac @ Kranji	JTC Corporation	Kranji Loop/Kranji Road	North	143,370	117,563
Kranji Green	JTC Corporation	Kranji Loop	North	133,040	109,093
Single-user industrial development	Tee Yih Jia Food Manufacturing Pte Ltd	Senoko Drive/ Senoko Road	North	79,580	65,256
Single-user factory	HL-Sunway JV Pte Ltd	Seletar North Link	North-East	62,480	51,234
Single-user factory	Hydrochem (S) Pte Ltd	Tuas South Avenue 3	West	48,630	39,877
Tuas South Connection	Yee Lee Development Pte Ltd	Tuas South Link 1	West	47,160	38,671
7 North Coast	JTC Corporation	North Coast Avenue	North	44,570	36,547
1 North Coast	JTC Corporation	North Coast Avenue	North	37,100	30,422
Single-user industrial development	Shimano Singapore Pte Ltd	Bulim Walk	West	35,600	29,192
Additions/ alterations to existing factory	Micron Semiconductor Asia Operations Pte Ltd	North Coast Drive	North	34,130	27,987
Samwoh Smart Hub	Samwoh Corporation Pte Ltd	Kranji Way	North	32,150	26,363
Additions/ alterations to existing factory	Neste Singapore Pte Ltd	Tuas South Lane	West	31,400	25,748
Single-user factory	Neo Garden Catering Pte Ltd	Quality Road	West	28,370	23,263
Additions/ alterations to existing factory	7000 AMK LLP	Ang Mo Kio Avenue 5	North-East	24,960	20,467
351 on Braddell	BP-Braddell LLP	Braddell Road	Central	24,210	19,852
Koufu Group HQ	Koufu Pte Ltd	Woodlands Height	North	20,390	16,720
High-specs					
Extension to existing factory	United Engineers Limited	Ang Mo Kio Street 64	North-East	60,180	49,348
Data Centres					
Single-user factory	Digital Singapore 2 Pte Ltd	Loyang Drive	East	32,050	26,281
Single-user factory	Equinix Singapore Pte Ltd	Sunview Drive	West	31,890	26,150
Single-user factory	STT Loyang Pte Ltd	Loyang Drive	East	27,240	22,337

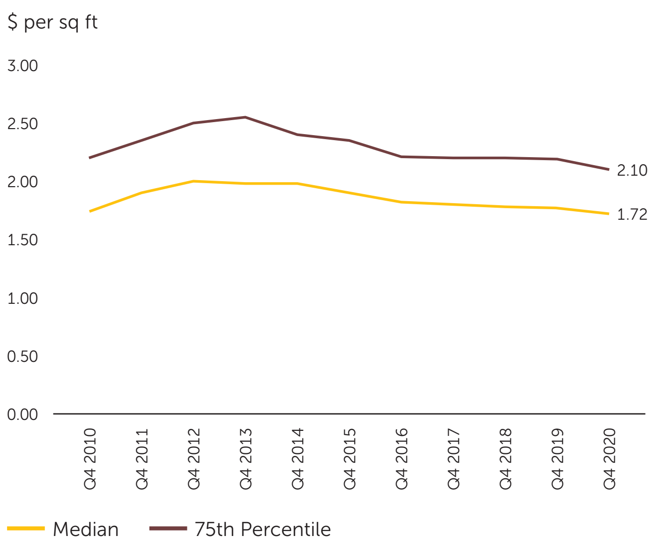
Development	Developer/ Owner	Location	Region	GFA (sq m)	NLA (sq m)
2022					
Light Industrial					
Bulim Square	JTC Corporation	Bulim Lane 1/2	West	159,400	130,708
JTC Space @ AMK	JTC Corporation	Ang Mo Kio Street 64/65	North-East	116,940	95,891
Solaris @Tai Seng	SB (Ipark) Investment Pte. Ltd.	Tai Seng Avenue	North-East	105,250	86,305
Single-user factory	Hyundai Motor Singapore Pte Ltd	Bulim Avenue	West	86,900	71,258
Liner	SB (Northview) Investment Pte Ltd	Tuas Bay Close	West	46,200	37,884
REVV	SB (Yung Ho) Investment Pte. Ltd.	Corporation Drive	West	32,000	26,240
Multiple-user factory	RBC Investor Services Trust Singapore Ltd	Tuas South Avenue 2	West	31,060	25,469
Ascent @ Gambas	SB (Gambas) Investment Pte Ltd	Gambas Way	North	29,900	24,518
Additions/ alterations to existing industrial development	Jurong Shipyard Pte Ltd	Tuas South Boulevard	West	27,150	22,263
Single-user factory	Amazon Asia-Pacific Resource Pte Ltd	Loyang Drive	East	24,130	19,787
Single-user factory	Amazon Asia-Pacific Resource Pte Ltd	Sunview Drive	West	20,750	17,015
High-specs					
Multiple-user factory	Mapletree Industrial Trust	Kallang Way	Central	80,420	65,944
Data Centres					
Multiple-user factory	AirTrunk Singapore Holding Pte Ltd	Loyang Drive	East	40,410	33,136

Source: JTC, EDMUND TIE Research

Rents

The reduced demand for factory space in 2020 resulted in rents falling across the board, with high-specs industrial space witnessing greater declines. The 75th percentile rents for multiple-user factory, a proxy for high-specs industrial, declined by 3.9% in 2020 to $2.10 per sq ft per month after remaining stable in the preceding three years. Median rents declined by 3.1% to $1.72 per sq ft per month. (Figure 6).

FIGURE 6: FACTORY RENTS[11]



Source: JTC, EDMUND TIE Research

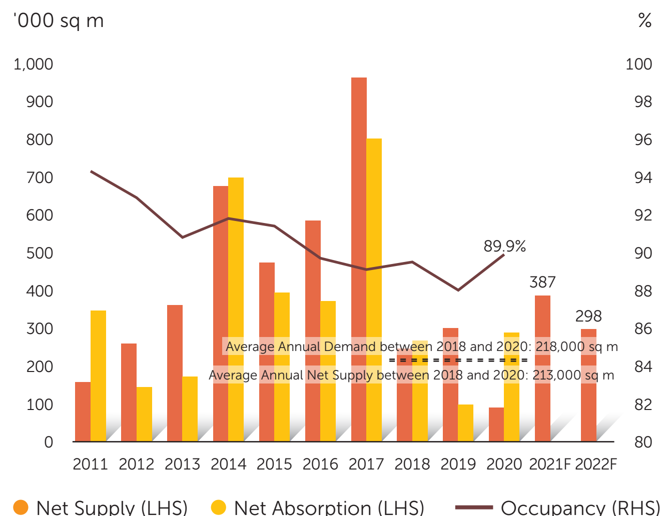
Outlook

The outlook for the manufacturing sector is brightening; the PMI has risen for the seventh straight month to reach 50.7 in January 2021, indicating that the sector is in an expansion mode. The increasing adoption of 5G technology in many countries will likely support the recovery in the global electronics cycle. There are considerable political uncertainties that could weigh on global trade, stemming from the new U.S. Biden administration and the US-China trade conflict. Greater supply pressures over 2021-2022 will also cap any rental growth. Factory rents are thus likely to post a slight decline of 0-2% in 2021.

6.0 LOGISTICS AND DISTRIBUTION CENTRES[12] (WAREHOUSE)

In response to the macroeconomic uncertainty and slow demand for older warehouse stock, rental rates for warehouses have declined by 6.2% annually in 2020. Meanwhile, as logistics companies continue to search for suitable spaces for their business and as more retail enterprises turn towards e-commerce operations, logistics and distribution centres with modern infrastructures are likely to command higher rents.

FIGURE 7: NET SUPPLY, NET ABSORPTION AND OCCUPANCY (WAREHOUSE)



F refers to forecast.
Source: JTC, EDMUND TIE Research

Stock and Supply

In Q4 2020, the total warehouse stock increased by 0.8% y-o-y to 11.1 million sq m. The net supply of 90,000 sq m in 2020 was considerably lower than that in 2019 (301,000 sq m).

There was only one warehouse completed in 2020, located at 5 Tuas Avenue 5 and developed by Hup Hin Property. The warehouse has an NLA of about 14,500 sq m.

11 Refers to gross rent per month including service charge but excluding Goods and Services Tax (GST).
12 As there are no official statistics on logistics and distribution centres in Singapore, warehouse data from JTC is used as a proxy.

Demand and Occupancy

Established global companies are taking up more warehouse space to expand their operations

The COVID-19 outbreak and the Circuit Breaker has propelled the adoption of e-commerce by consumers and businesses as mainstream channel of acquiring goods and services. Accordingly, demand has risen for logistics facilities and also warehouse space as various sectors like healthcare and supermarkets saw an increase in stockpiling requirements. Technology advancement continues to drive many requirements as logistics companies are faced with the challenge of meeting rising consumer expectations. For example, DB Schenker has commenced operations at its warehouse in the Airport Logistics Park, which serves as a regional hub for automated high-speed logistics.

Demand for warehouse space tripled from 98,000 sq m in 2019 to 288,000 sq m in 2020. Consequently, the occupancy rate rose by 2.4 percentage points to 89.9% in 2020. The greatest increase in occupancies was recorded in the Northeast Region, which saw occupancies rise from 78.6% in Q4 2019 to 89.6% in Q4 2020.

Potential Supply

JTC Logistics Hub @ Gul Circle, an integrated development, to provide around 115,000 sq m NLA of new warehouse supply in 2021

Around 688,000 sq m of warehouse space is expected to come onstream in 2021-2022, which amounts to about 6.2% of the existing stock. The incoming supply is about 76.0% higher than the net supply over 2019-2020.

Major potential supply includes JTC Logistics Hub @ Gul Circle[13] (140,000 sq m GFA), a next-generation innovative logistics warehouse facility and a 87,500 sq m (GFA) warehouse development by SH Cogent Logistics (Table 4).

TABLE 4: SELECTED PIPELINE SUPPLY (LOGISTICS AND DISTRIBUTION WAREHOUSE)

Development	Developer/ Owner	Location	Region	GFA (sq m)	NLA (sq m)
2021					
JTC Logistics Hub @ Gul	JTC Corporation	Gul Circle	West	140,090	120,477
Cogent Jurong Island Logistics Hub	S H Cogent Logistics Pte Ltd	Tembusu Crescent	West	87,500	75,250
Warehouse development	NTUC Fairprice Co-operative Ltd	Sunview Road	West	69,610	59,865
Single-user industrial development	F&N Foods Pte Ltd	Tuas Link 3	West	29,010	24,949
Warehouse development	Tiong Nam Logistics (S) Pte Ltd	Senoko Loop	North	24,940	21,448
2022					
Warehouse development	Pandan Crescent Pte Ltd	Pandan Crescent	West	119,710	102,951
Warehouse development	Allied Sunview Pte Ltd	Sunview Road	West	116,810	100,457
Additions/ alterations	Tuas South Avenue Pte Ltd	Tuas South Avenue 14	West	80,130	68,912
Warehouse development	Soilbuild Business Park REIT	Pioneer Sector 1	West	53,190	45,743
Single-user industrial development	2TPC Pte Ltd	Tanjong Penjuru Crescent	West	33,880	29,137
Warehouse development	Soon Bee Huat Trading Pte Ltd	Penjuru Lane	West	24,320	20,915
2023					
Additions/ alterations	Tuas South Avenue Pte Ltd	Tuas South Avenue 14	West	20,700	17,802

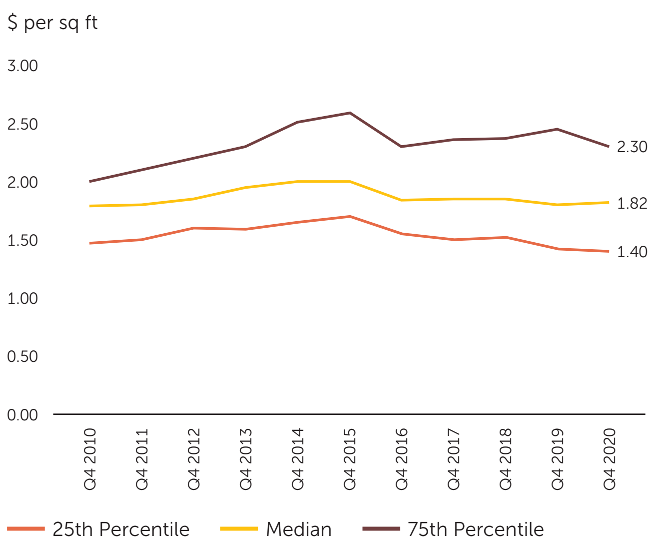
Source: JTC, EDMUND TIE Research

13 The innovative logistics facility will allow co-location of empty container depots, warehouses and a heavy vehicle park to improve the operational efficiency and productivity for logistics companies.

Rents

Median rents for warehouses rose by 1.2% y-o-y to $1.82 per sq ft per month in Q4 2020. However, 25th percentile rents, a proxy for traditional warehouses, saw a decline of 1.4% over the year while 75th percentile rents, a proxy for modern logistics and distribution centres, fell by 6.2%. The sharper decline in 75th percentile rents is more likely a correction from the strong rental escalations in the first half of the last decade amid a difficult environment rather than a softening of demand (Figure 8).

FIGURE 8: WAREHOUSE RENTS[14]



Source: JTC, EDMUND TIE Research

Outlook

The boisterous growth of e-commerce, aided by the continued proliferation of online ordering and mobile wallet platforms, will support demand for logistics facilities and warehouses. Warehouses with better specifications like high load capacity and large floor plates will see stronger demand. Government policies to aid businesses to adopt digital solutions and increase their online presence should support demand for the sector. With greater forthcoming supply, demand will likely rise in step and rents could trade sideways on average in 2021. Spaces with high specifications could see a marginal increase in rents in 2021.

14 Refers to gross rent per month including service charge but excluding Goods and Services Tax (GST).

AUSTRALIA
INDEPENDENT MARKET STUDY

By Colliers International, February 2021

ECONOMIC OVERVIEW

The outbreak of COVID-19 infections and the measures implemented to contain the spread of the virus have significantly affected the Australian economy. As a result, Gross Domestic Product (GDP) fell by 7% in the June 2020 quarter which was the largest decline since the quarterly accounts began in 1959. While the decline in GDP was significant, the contraction was less severe than in many other advanced economies because health outcomes here were less severe and policy support was substantial.

Encouragingly, a sharp recovery in economic activity is well underway with GDP figures for the September 2020 quarter growing by 3.3% which is the largest quarterly growth in 45 years. GDP does however remain 3.8% lower than where it was in Q3 2019 and on an annual basis is running at -3.8%. With strong quarterly growth also anticipated in the final quarter of 2020 and into 2021, the economy should be back at its pre-COVID-19 level by mid-2021. Nationally, more than half of the employment lost in the initial downturn has been regained, but significant spare capacity remains in the labour market.

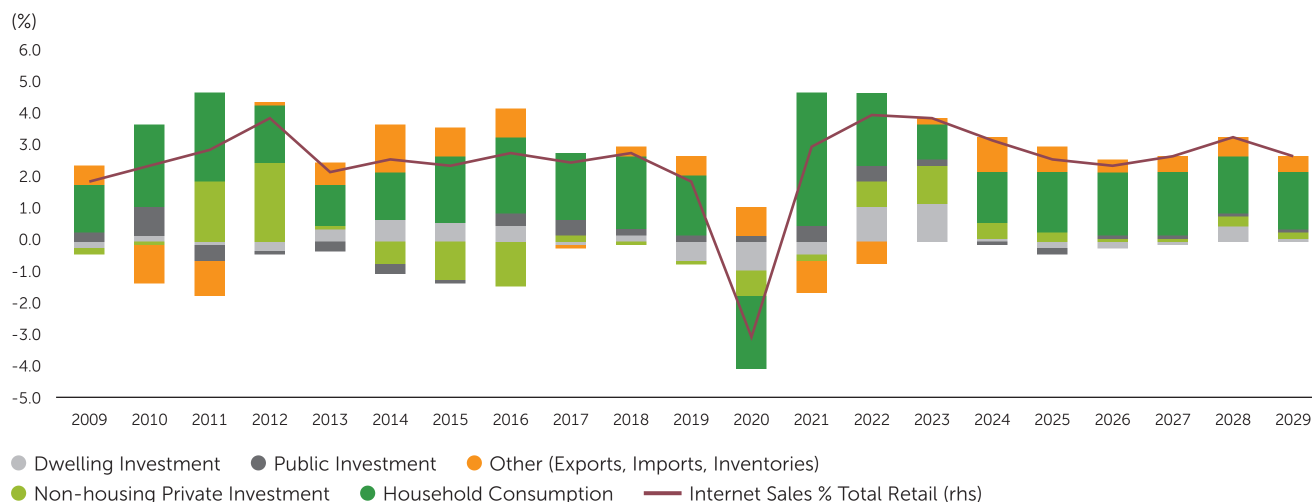
Key trends that are impacting the Australian economy are noted as follows:

Interest Rates	The cash rate was cut to at an all-time low of 0.1% in November 2020. This rate cut followed multiple cuts since March 2020 where prior to COVID-19 the cash rate stood at 0.75%. The RBA has indicated the current low cash rate setting is likely to be in place for some time. Although the RBA's prime focus is to keep inflation in check, unemployment is likely to be a key focus and inflationary pressure is expected to be minimal.
Inflation (CPI)	Australian Consumer Price Index (CPI) rose by 1.6% in the September 2020 quarter and followed a fall of 1.9% in the June 2020 quarter. On an annual basis, CPI rose by 0.7% which is well below the RBA target of 2-3%.
Jobs growth	In the year to December 2020, employment contracted by 0.5%, well below the 20-year average of 1.8% per annum. Between January 2020 and December 2020, there were 74,700 fewer people employed across the country. The unemployment rate has fallen to 6.6% in December 2020, down from the peak of 7.5% in July 2020, yet above the 5.1% recorded in February 2020 prior to COVID-19.
Population Growth	Population in Australia increased 1.3% over the 12 months to June 2020 (latest available statistics), down from 1.5% recorded a year prior Going forward, population growth will weaken significantly over the next 12 months given international border closures and Australia's strong reliance on net overseas migration. We are forecasting Australia's population to grow by just over 60,000 persons in 2021, reflecting a growth rate of just 0.2% for the period.
Wages Growth	Wages growth has slowed to 1.4% per annum over the year to September 2020, down from the 10-year average of 2.6% per annum.
Consumer Confidence	Consumer sentiment has continued to improve and is now 17.3% above pre-pandemic levels and is at its highest level since October 2010. The index currently stands at 112.0 in December 2020, up from 95.1 a year ago.

While GDP is expected to contract by around 3.0% in 2020, a large bounce back in the economy is expected in 2021 with Deloitte Access Economics forecasting growth of 3.0% for the year and 3.9% in 2022. The diversity of the Australian economy will result in an outperformance when compared to many of Australia's global competitors who have been harder hit by the impacts of the pandemic.

Separately, there has been a rise in trade tensions between Australia and China in recent months. In turn, this has led to price falls for local Australian producers who sell goods to China across a range of commodities (including barley, beef, wine, lobsters and thermal coal). While the impacts of this have been felt on individual businesses and sectors, the overall impact to the Australian economy has been minimal to date given the surge in iron ore prices. However, the medium to longer term outlook remains somewhat uncertain.

FIGURE 1. AUSTRALIAN ANNUAL GDP GROWTH



Source: ABS, Deloitte Access Economics

TABLE 1. AUSTRALIAN ECONOMIC FORECASTS

	Current (Q4 2020)^	2021	2022	2023	2024
GDP	-3.8%	3.0%	3.9%	3.9%	3.2%
CPI	0.7%	1.4%	1.3%	2.0%	2.3%
Population Growth	1.3%	0.4%	0.7%	1.2%	1.2%
Interest Rates*	0.10%	0.10%	0.10%	-	-
Wages Growth	1.4%	0.2%	1.8%	1.5%	2.7%
Unemployment Rate	6.6%	6.5%	6.3%	6.2%	6.0%

* Westpac
^ latest available data as at end of Q4 2020

Source: Deloitte Access Economics, Colliers International

Government Stimulas

The Australian Government announced a range of measures to support the economy, business and employment during COVID-19. Below is a summary of the main measures:

JobKeeper:

Under the JobKeeper Payment, businesses and not for profits significantly impacted by COVID-19 will be able to access a Government wage subsidy of A$1,500 per fortnight per eligible employee and business participant up to 27 September 2020.

The JobKeeper Payment was extended to 28 March 2021 at an additional cost of $16 billion. As part of the extension, the payment was reduced to A$1,200 per fortnight from 28 September 2020 to 3 January 2021 (A$750 per fortnight for those who worked on average less than 20 hours per week in the four weeks before either 1 March 2020 or 1 July 2020, whichever is higher)). From 4 January 2021 to 28 March 2021, the fortnightly payment will be further reduced to A$1,000 (and A$650 per fortnight for those who worked on average less than 20 hours per week in the four weeks before either 1 March 2020 or 1 July 2020, whichever is higher).

Employers (including not-for-profits) are eligible for the subsidy if, at the time of applying:

- Their business has an aggregated turnover of less than A$1 billion (for income tax purposes) and they estimate their turnover has declined or will likely decline by at least 30 per cent relative to a comparable period 12 months prior (of at least a month); or
- Their business has a turnover of A$1 billion or more and they estimate their turnover has declined or will likely decline by at least a 50 per cent relative to a comparable period a year ago (of at least a month);
- If they are an ACNC-registered charity (other than universities and schools) and they estimate their turnover has declined or will likely decline by at least a 15 per cent relative to a comparable period a year ago (of at least a month).

AUSTRALIA

INDEPENDENT MARKET STUDY

By Colliers International, February 2021

JobSeeker:
The Jobseeker payment is a payment available to employees stood down or let go, sole traders, self-employed, casual workers and contract workers who meet the income test as a result of the economic downturn due to COVID-19.

With this scheme, Jobseeker can get anything from $565.70 to $790.10 a fortnight depending on income (the more you earn the less you get). If you have a partner, their income may also affect what you're entitled to.

JobTrainer:
The Australian government announced a A$2 billion skills package called JobTrainer in mid-2020. The first part, worth A$1.5 billion, is aimed at keeping those already in apprenticeships and traineeships employed.

The second part is aimed at school leavers and those looking for work. It provides A$500 million for vocational education and training courses. That funding is conditional on matching funds from state and territory governments.

AUSTRALIAN INDUSTRIAL MARKET

As we look back on 2020, it has been a year where the industrial and logistics sector has been brought to the forefront and has outperformed all other mainstream real estate sectors. In the 12 months to September 2020, the industrial sector provided a total return of 11.2%, broadly split between capital and income return (5.5% from capital returns and 5.7% from income returns), and was above the 6.8% and -10.0% recorded for office and retail sectors respectively over the same period. Notwithstanding this, the sector's landscape has changed significantly, brought on by rapidly evolving economic conditions which have forced both industrial occupiers and investors to adapt to stay competitive.

On the occupier side, businesses have been forced to adjust to supply chain disruptions and as a result we have seen a significant investment in supply chain management solutions and diversification of supplier networks. While the leasing market remains strong, underpinned by requirements from transport, retail and food logistics groups, deals are taking longer to get over the line given the uncertainty on business operations and occupiers are increasingly staying put within their current facility. On the other hand, the investment market has not skipped a beat with the depth of capital from local and offshore groups remaining significant post COVID-19.

There have been winners and losers from changing market conditions. Occupiers tied to e-commerce, food logistics, pharmaceutical, transport and logistics have performed well with some businesses reporting a doubling of revenue since March 2020 while businesses who service industries in the leisure and hospitality sectors have been harder hit. The big winner in the investment market has been prime core assets backed by a strong covenant where continued yield compression has been recorded as the flight to quality thematic plays out. Alternatively, secondary assets have been harder to price as investors heavily scrutinise the covenant, location and overall condition of the asset.

Key Market Drivers

Besides population growth which will take a hit in the short term as Australian borders are closed to international travellers, the other key drivers of infrastructure investment and e-commerce growth will remain strong and will continue to be a positive influence on industrial occupancy and investor demand.

Infrastructure Investment	Australia is currently witnessing an era of transformation and renewal, with an unprecedented amount of funds being directed to transport infrastructure projects including new roads, rail, intermodal terminals and an airport. For the industrial sector, ultimately these projects will shape the location of industrial demand while areas that were once considered secondary may perhaps become prime demand areas. It is estimated that there is A$133 billion worth of transport infrastructure projects under construction and committed, 65% of which is scheduled for completion in the next three to five years.
E-commerce	The attractiveness of e-commerce has increased exponentially as a result of COVID-19 and the take-up of online retail will gain market share at the expense of brick-and-mortar retail sales as consumers are forced to buy online. COVID-19 is expected to pave way to a significant structural and cultural shift in the way consumers buy their goods, many of which have not shopped via online platforms before. Long term, these buying habits are expected to be permanent as consumers become accustomed to the simplicity of online shopping. As a result, COVID-19 will accelerate the growth of online retail. In the 12 months to September 2020, online retail sales growth increased by 71.2% which is at record levels with Australian's spending A$29.0 billion on online goods over the period. In response to COVID-19, online retail sales represented 10.6% of total retail sales, up from 6.3% a year ago. Despite recent growth, the proportion of online retail sales in Australia remains relatively small when compared to other comparable countries including the US and UK where it is as high as 26%.

Covid-19 and The Australian Logistics Market

Despite the outbreak of COVID-19, fundamentals within the Australian industrial and logistics market remain favourable. Notwithstanding this, there will be short term impacts (some positive and some negative) on the local logistics market.

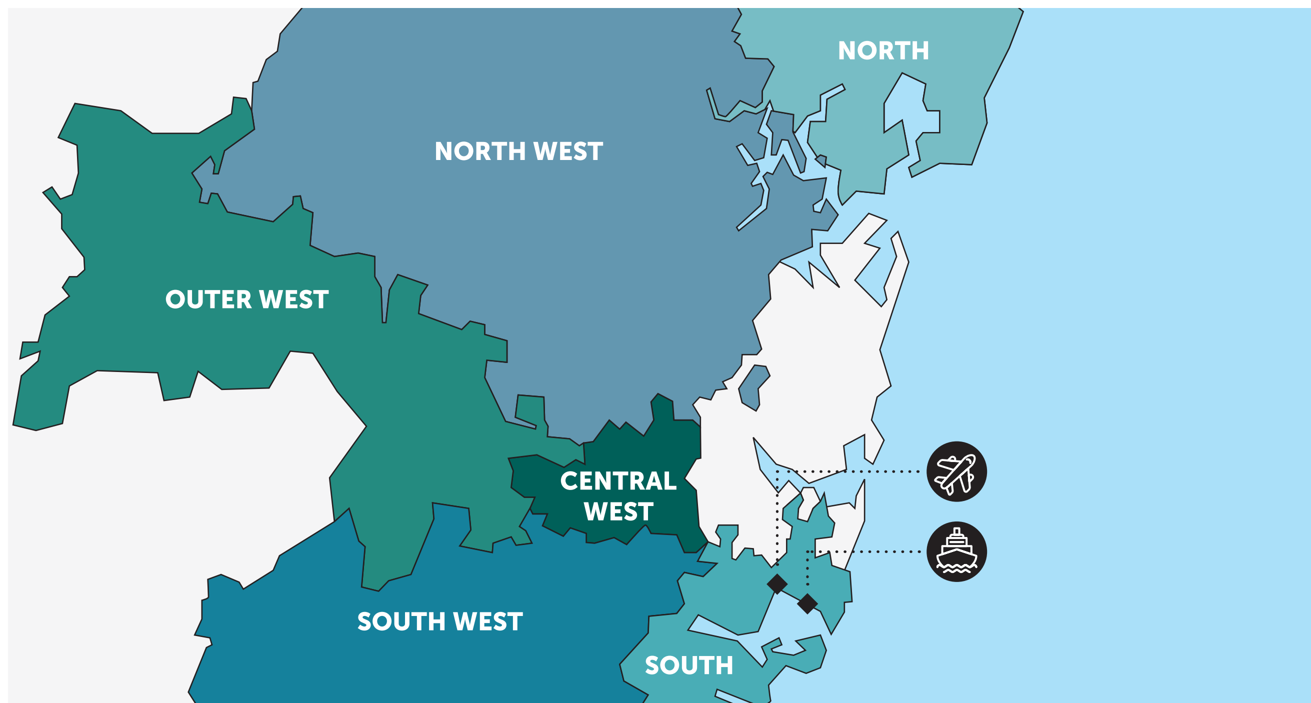
Key observations include:

- Supply chains have and will continue to be tested. Overall, supply chains held up quite well, albeit with longer delivery times for certain products. Since COVID-19, retailers and other businesses have focussed on their supply chain efficiencies and have developed strategies to better deal with periods of peak demand. Anecdotal evidence suggests some occupiers are now holding 5-10% more stock within their warehouses.
- The logistics market will benefit in the medium to long term as consumers increasingly opt to buy online. The take-up of online retail has been significant, and we expect these consumer habits to become permanent. As a result, this could translate to increased demand for industrial space as retailers look to further drive their e-commerce channels.
- Certain industrial occupiers have delayed expansion or relocation decisions in the short term as they adopt a 'wait and see' approach and are focusing on any potential impacts of the virus to their business. Anecdotal feedback from local leasing agents in each state suggests those occupiers who rely on imported goods from offshore markets have been hardest hit.
- Some speculative developments have not progressed with developers citing longer lease times and difficulty in sourcing some construction materials as the primary reasons.
- For the investment market, there has been a large shift to prime core assets as institutions chase income security. Private investors have become more active for core plus and secondary assets, particularly along the East Coast.

AUSTRALIA INDEPENDENT MARKET STUDY

SYDNEY INDUSTRIAL

By Colliers International, February 2021



1.1 MARKET OVERVIEW

The Sydney industrial and logistics market is broken into several major precincts; Central West, Outer West, North West, South West, South and North. The South market has traditionally been Sydney's most important industrial hub due to its proximity to Port Botany, the Sydney Airport and the CBD. The South precinct is predominantly occupied by logistics, retail and port-related tenants. In recent years, however, the South Sydney industrial market has experienced strong levels of stock withdrawal for alternative uses due to zoning changes. This has put significant upward pressure on rents and declining availability. A similar situation was experienced in the North industrial precinct where residential activity has continued to encroach on the industrial space market. The North industrial precinct today is dominated by smaller and high-value users such as IT, Pharmaceutical and Hi-tech industries.

In recent years, the lack of larger space availability in the inner-city markets has resulted in larger industrial users moving towards the South West, Outer West and North West precincts where much of the new supply is concentrated. The Western markets are benefiting from a significant level of road upgrades and infrastructure investment. Tenancy profiles include a diverse range of industries including Third Party Logistics (3PL), retail, supermarkets, construction and Fast-Moving Consumer Goods (FMCG), amongst others.

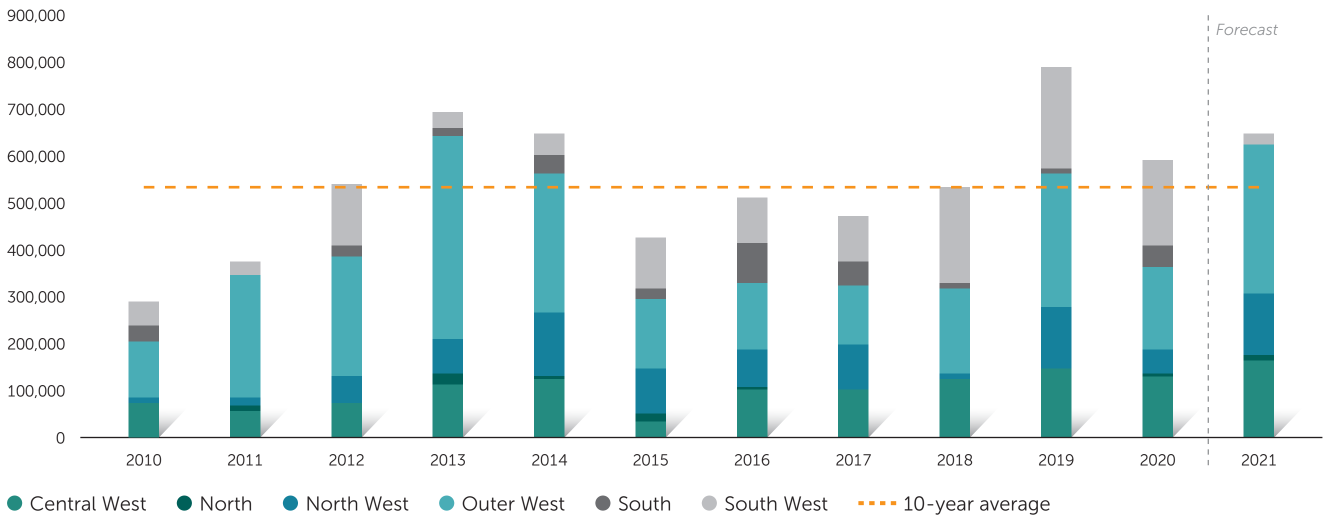
1.2 Supply

Industrial supply levels are forecast to total approximately 600,000 sqm in 2020, down from the 755,353 sqm added in 2019. Supply levels for 2020 have been impacted by a lack of developable land while a select number of projects mooted for speculative development have not progressed, likely due to COVID-19. As a result, 80% of supply in 2020 stemmed from pre-commitments.

Supply in 2020 was heavily concentrated in the South West and Outer West submarkets, where collectively 56% of the 2020 forecast total is located.

Looking ahead, supply levels are expected to moderately increase in 2021 with almost 650,000 sqm expected to enter the market, of which approximately 70% is pre-committed. By submarket, 49% will stem from the Outer West submarket while a further 20% will come from the North West submarket. Notably, the level of supply for the year is down on previous forecasts as a number of projects will instead push in 2022 supply levels. For 2021, the largest project to be delivered is Amazon's facility at the Oakdale West Estate (206,192 sqm) while other major completions include Compass Logistics Estate at Eastern Creek (33,250 sqm) and Wetherill Park Distribution Centre (26,464 sqm) which has secured Marley Spoon for 14,200 sqm.

FIGURE 2. SYDNEY INDUSTRIAL SUPPLY



Source: Colliers Research

1.3 Occupier Market & Demand

Despite occupiers remaining cautious and taking longer to commit to long term space, industrial take-up in Sydney has been significant with approximately 1,300,000 sqm of industrial space (5,000 sqm+) being leased in 2020. Historically, industrial take-up across Sydney has averaged approximately 850,000 sqm p.a. over the past decade.

Leasing demand in 2020 was led by occupiers tied to the growth of online retail and food logistics with several significant pre-commitments being recorded this year. Notably, this includes Amazon (200,000 sqm at Oakdale West), Marley Spoon (14,200 sqm at Wetherill Park), Woolworths (75,300 sqm at Moorebank Intermodal) and Coles (30,000 sqm at Wetherill Park). Our analysis shows that pre-commitments have represented 52% of total tenant demand in 2020.

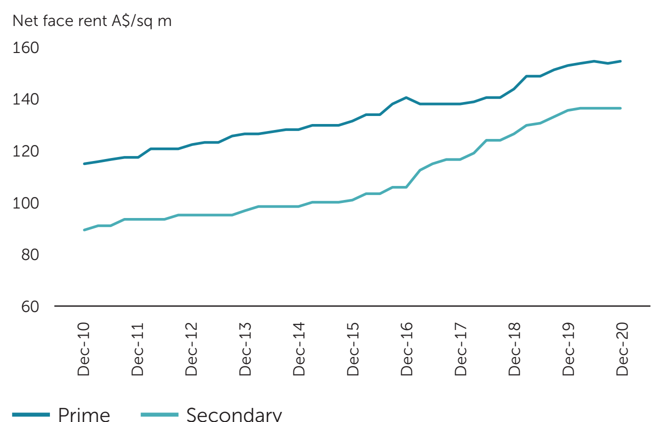
As at December 2020, the industrial vacancy rate (5,000 sqm+) in Sydney measured 4.9%, up from 4.4% recorded in September 2020. The increase in the vacancy rate is the result of an increase in Central West submarket. However, our understanding is a number of vacant facilities in the Central West submarket are in final negotiations and the vacancy rate is expected to fall again in 2021. Similarly, with approximately 1,300,000 sqm in current active requirements, downward pressure on the overall vacancy rate is expected, albeit varying between submarkets.

1.4 Rents & Incentives Trends

With regards to rents, all submarkets have remained largely unchanged in 2020 with owners instead opting to increase incentives in order to preserve asset values. More recently, we have seen incentive levels in some Western submarkets fall and is the result of improved sentiment from landlords. Prime net face rents currently average A$154/sqm per annum while secondary grade facilities currently average A$136/sqm per annum.

Incentive levels currently range between 9.0% and 17.5% across Sydney for both prime and secondary grades, up from 7.5% to 15.0% pre COVID-19 and as a result, net effective rents have fallen on average by approximately 4.0% over the past year across both grades.

FIGURE 3. SYDNEY INDUSTRIAL NET FACE RENTS (A$/SQ M PER ANNUM)



Source: Colliers Research

AUSTRALIA INDEPENDENT MARKET STUDY

SYDNEY INDUSTRIAL

By Colliers International, February 2021

TABLE 2. PRIME RENTS BY SUBMARKET, Q4 2020

Net Face Rents	South	Central West	Outer West	North West	South West
A$/sqm p.a.	199	135	130	128	124
6 months change	0.0%	0.0%	0.0%	0.0%	0.0%
12 months change	1.1%	2.9%	1.0%	0.0%	0.0%
Average Incentive	15.0%	11.5%	13.1%	12.5%	13.8%

Source: Colliers International

Going forward, we are forecasting rental growth to increase by sub 1.5% in 2021 at a broader Sydney level as economic conditions improve, with inner ring submarkets expected to outperform. From 2022, we are forecasting rental growth to revert towards the long-term average (~3.0%). Incentive levels are expected to stabilise and remain at their current levels in 2021, thereby resulting in growth in effective rents for the year.

1.5 Investment Market

Investor appetite for industrial and logistics assets located in Sydney continues unabated, with demand coming from a wide range of investors. In 2020, just under A$1.65 billion traded within Sydney across 25 assets ($10 million +), representing an average value of A$66.3 million. By comparison, investment volumes in 2019 totalled approximately A$2.0 billion.

Institutional investors have acquired 87% of assets by volume in 2020 and is skewed by the higher percentage of prime core assets which have been brought to market this year. Major acquisitions this year have included Aldi Minchinbury and Prestons (A$359.9 million collective total), Sigma's distribution centre at Kemps Creek (A$133.6 million), 37-39 Wentworth Street, Greenacre (A$100 million) and Culverston Road, Minto (A$207 million).

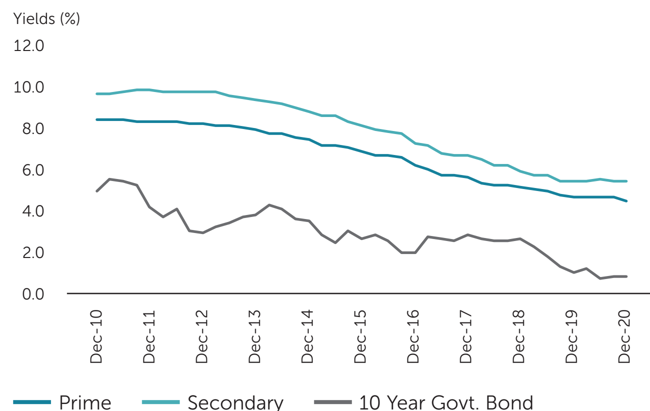
Mid-tier funds and private investors remain active within the secondary market seeking reversionary potential or asset management opportunities; however, few assets have been brought to market. The most notable sale within the secondary market in Sydney this year was 5 Williamson Road, Ingleburn (A$38.2 million). With 10 groups submitting a bid for the asset, a sharp yield was recorded (5.42%) which demonstrated there has been little to no softening recorded in the secondary market as previously anticipated.

Offshore groups have been unable to travel to Australia for inspections, however, they are increasing their allocations to the sector indirectly via a local manager. Notably, this includes GIC and Allianz and we expect this trend to strengthen in 2021.

1.6 Yields

From a pricing perspective, Sydney industrial and logistics yields currently average 4.50% (range of 4.25% to 5.00%) in the prime market and 5.40% (range of 4.75% to 6.00%) within the secondary market based on a five-year WALE. Assets backed by a strong covenant and 10+year WALE would trade tighter than this range. Looking ahead, the current momentum within the investment market is expected to place downward pressure on prime yields in 2021 while there is likely to be some upward movement in the secondary market in some instances as risk becomes priced in surrounding covenant, asset and location.

FIGURE 4. SYDNEY INDUSTRIAL YIELDS, HISTORICAL



Source: Colliers Research

1.7 Outlook

Despite recent events surrounding COVID-19, the short-term outlook for the Sydney industrial market remains positive. On the demand side, there has been a large pick-up in active requirements come to the market, totalling over 1,000,000 sqm which should flow through to lease deals in early 2021. By sector, demand is being led by transport and logistics and warehouse/storage while more recently there has been an evident pick-up in manufacturing requirements.

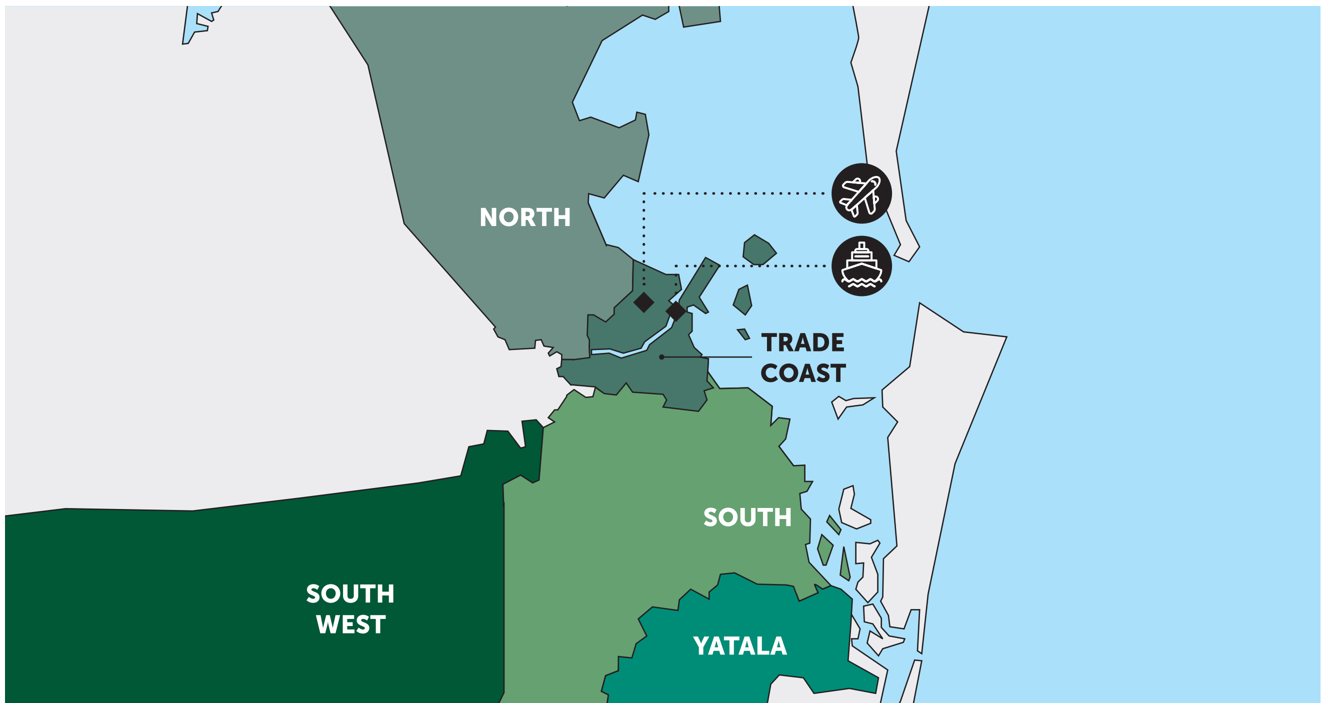
While rents have largely held steady in 2020, we are forecasting rental growth to improve in 2021 across most submarkets as economic growth picks up. Incentives are expected to stabilise following the rises recorded in 2020.

For the investment market, there remains significant capital seeking logistics assets within Sydney. However, stock is expected to remain tightly held and as a result we expect there will be pressure on yields, particularly within the prime market.

AUSTRALIA INDEPENDENT MARKET STUDY

BRISBANE INDUSTRIAL

By Colliers International, February 2021



2.1 MARKET OVERVIEW

The Brisbane industrial market has five key precincts: Trade Coast, Brisbane North, Brisbane South, Brisbane South West and Yatala. The Trade Coast extends across circa 8,000ha located only 6km from the Brisbane CBD and at the mouth of the Brisbane River. The precinct has direct links to air, sea, road and rail networks, including the Port of Brisbane and Brisbane Airport, which supports its desirability for investors and tenants. Investment stock is generally tightly held.

The Brisbane North precinct is in a rapidly growing area extending from the Brisbane North suburbs to the Moreton Bay region. This precinct benefits from overflow demand on the Trade Coast due to its proximity to the Brisbane Airport and the Port of Brisbane. The Brisbane South precinct covers the industrial area in Logan and Brisbane South. The A$512 million Logan Enhancement project along with the A$2.5 billion M1 upgrade master plan will improve connectivity from the precinct to interstate destinations.

The Brisbane South West precinct is a primary area for current and future industrial development, extending from Brisbane West to Ipswich and in proximity to urban areas experiencing solid population growth. Key industries in this precinct range from food and beverage manufacturing, steel fabrication, transport, warehousing, and logistics-based industry.

The Yatala Enterprise Area (YEA) is the largest zoned industrial land area in the Gold Coast and the city's leading industrial precinct. The YEA is strategically located less than 40km north of the Gold Coast CBD and 40km south of the Brisbane CBD and is only a 30-minute drive to the Port of Brisbane and the Brisbane International Airport. The YEA is a value-add manufacturing region with businesses in food and beverage, construction materials, machinery and equipment, plastic and chemicals as well as warehousing, transport and distribution.

2.2 Supply

In 2020, almost 400,000 sqm is expected to enter the market, 49% of which is already completed. Supply for 2020 will be the largest within the South West (156,558 sqm) and South (101,246 sqm) submarkets. Major developments for the period include Freeman Central (54,845 sqm) which is the largest speculative development ever recorded in Brisbane.

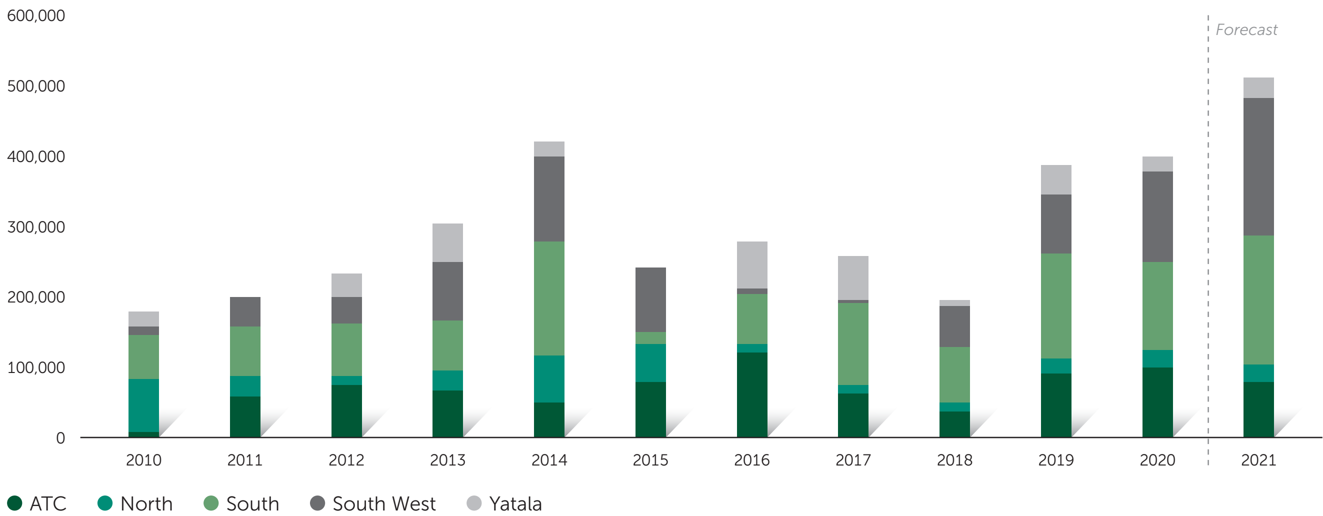
Supply levels are expected to remain strong in 2021 with approximately 510,000 sqm in the pipeline. We note, of this level of supply, approximately 340,000 sqm (or 66%) is dependent on pre-commitments so the final level of supply for 2021 is likely to be closer to the levels recorded in 2020.

AUSTRALIA INDEPENDENT MARKET STUDY

BRISBANE INDUSTRIAL

By Colliers International, February 2021

FIGURE 5. BRISBANE INDUSTRIAL SUPPLY (SQ M)



Source: Colliers Edge

2.3 Occupier Market & Demand

Occupier demand in the Brisbane industrial and logistics market has remained steady over the past six months despite the uncertainties triggered by the COVID-19 outbreak, with increasing demand from industrial operators within the pharmaceutical and logistics sectors. The flight to quality remains an ongoing theme with tenant activity focussed on the prime market as occupiers seek the operational efficiencies derived from newer facilities. Demand continues to be skewed towards new construction with a steady stream of major commitments to either design and construct (D&C) or speculatively developed space.

In contrast, the general leasing market is patchy with notably less demand for existing accommodation, particularly within the secondary market where a large portion of current vacancies exist. The movement of tenants upgrading to higher quality premises has been facilitated by favourable incentive metrics which in some precincts are as high as 20%, particularly in Outer precincts like the South and South West.

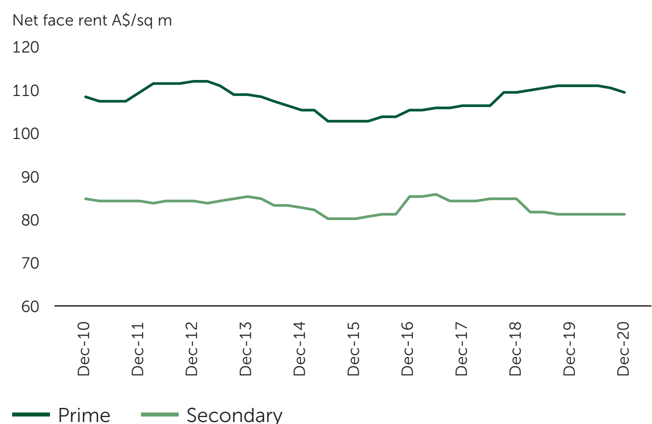
In 2020, just under 400,000 sqm of industrial space (for facilities sized 3,000 sqm and above) has been leased across Brisbane. By submarket, the South and South West submarkets have collectively accounted for 52% of take-up over the period and has been broadly spread across the industrial suburbs within these submarkets. By industry, take-up in 2020 has been strongest for manufacturing and 3PL sectors which have accounted for 36% and 16% of take-up respectively in the South and South West submarkets.

2.4 Rents & Incentives Trends

As at December 2020, prime net face rents across Brisbane averaged A$110/sqm, representing a small fall of -0.5% over the year as we saw a modest correction in rents and incentives for prime assets located in the ATC. This fall is just a consequence of the increasing competition of new development supply within the South and South West precincts.

For the secondary market, average net face rents currently average A$81/sqm, with incentives reporting an average increase of 2 percentage points from 17% in March 2020 to 19% in December 2020. While there is still limited supporting evidence that there has been an upward shift in incentive levels, we have seen market evidence that landlords have become more aggressive in their approach to secure tenants and to preserve value via holding headline rents steady. COVID-19 has been the catalyst behind the aggressive approach from landlords as they looked to lease vacant space, however, we expect this to ease as leasing demand picks up in 2021.

FIGURE 6. BRISBANE INDUSTRIAL NET FACE RENTS (A$/SQ M PER ANNUM)



Source: Colliers Edge

TABLE 3. PRIME RENTS BY SUBMARKET, Q4 2020

Net Face Rents	ATC	North	South	South West	Yatala
A$/sqm p.a.	110	110	112	112	105
6 months change	-6.4%	0.0%	0.0%	0.0%	2.0%
12 months change	-6.4%	0.0%	0.0%	0.0%	2.0%
Average Incentive	17.5%	17.5%	17.5%	17.5%	19.0%

Source: Colliers International

2.5 Investment Market

Investment sale volumes in Queensland have fallen in 2020 with A$1.3 billion trading (for transactions priced above A$10 million), compared to A$1.6 billion in 2019. Notwithstanding this, four assets above A$100 million have traded this year in Brisbane - ALDI Brendale (bought by Charter Hall/Allianz for A$132.5 million), ALDI Stapylton (bought by Charter Hall/Allianz for A$147.75 million), 338 Bradman Street, Acacia Ridge (acquired by Mapletree for A$114 million) and the remaining 50 per cent stake in the Coles cold storage distribution centre at Parkinson (bought by DWS for A$152.5 million).

Investment opportunities have generally been limited to off-market activity as owners use the strategy to hold onto the ownership to preserve value under uncertain market conditions. Despite the limited investment opportunities reaching the market, investment confidence from institutional investors has remained strong particularly for assets offering a long-WALE with defensive tenants.

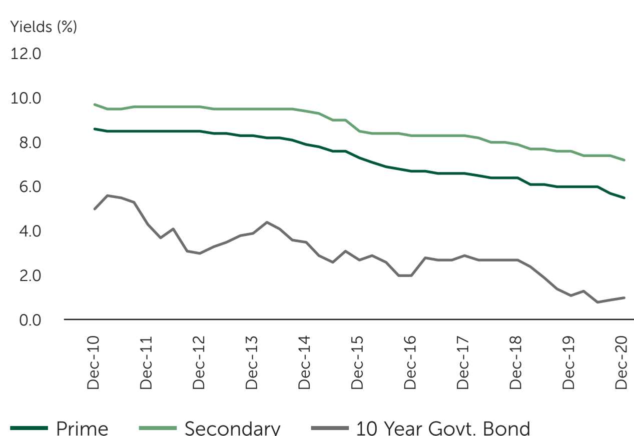
Unlike Sydney and Melbourne where the investment market has been dominated by institutions, the buyer profile in 2020 has been broadly split between institutions (53%), private investors (19%) and offshore groups (28%). Alternatively, 30% of assets to trade by volume have stemmed from corporates via a sale and leaseback arrangement. Notably, this includes the above-mentioned ALDI Brendale asset, Sigma's Berrinba asset and the EB Games distribution centre at Eagle Farm.

2.6 Yields

Due to the uncertain market conditions, capital has been redirected to perceived lower-risk profile investments triggering a compression of prime grade yields in the Greater Brisbane and Yatala industrial market of 49 basis points over the 12 months to December 2020.

Prime grade yields recorded an average yield of 5.45% in December 2020 compared to 5.69% over the previous quarter. In the case of the secondary market, average yields compressed by 38 basis points to 7.15% as at December 2020.

FIGURE 7. BRISBANE INDUSTRIAL YIELDS, HISTORICAL



Source: Colliers Edge

2.7 Outlook

As economic growth improves and industrial occupiers are more certain regarding their long-term growth, a pick-up in leasing activity is expected in 2021. However, occupiers are expected to further gravitate towards prime grade facilities as they take advantage of the recent rise in incentive levels.

Public investment in road infrastructure is expected to support industrial development across different precincts in Brisbane and Yatala. We have estimated about A$4.9 billion of public investment has the potential to enhance road connectivity within the industrial precincts of Outer North and South over the next 5-10 years as the Bruce Highway, the Gateway Motorway the M1 upgrade programs become a reality.

Within the investment market, there remains significant depth of capital seeking large scale logistics assets. However, stock remains tightly held and as a result we expect further yield compression to occur in 2021.

AUSTRALIA INDEPENDENT MARKET STUDY

MELBOURNE INDUSTRIAL

By Colliers International, February 2021

3.1 MARKET OVERVIEW

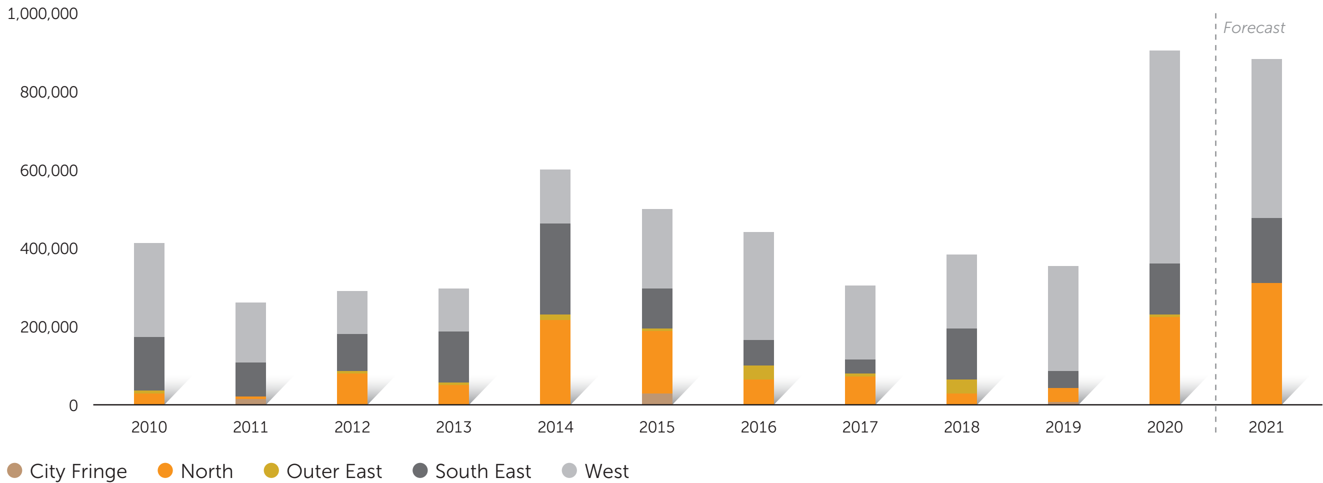
The Melbourne industrial market comprises five major precincts; the North, South East, West, Outer East and City Fringe. The City Fringe precinct primarily consists of smaller sites with higher rents specifically appealing to tenants that need to be located close to the city. Many of these industrial sites are being slowly converted to residential sites due to high underlying land values and diminishing availability of land suitable for residential development. The South East and Outer East precincts comprise larger land holdings with Industrial hubs including Moorabbin, Cheltenham, Clayton and Dandenong. The largest industrial precinct in Australia is the West precinct which has the largest industrial and logistics sites. This precinct continues to have new pockets of land unlocked in areas including Truganina, Tarneit and Ravenhall.

3.2 Supply

Supply levels for industrial space across Melbourne significantly increased in 2020 with 906,661 sqm entering the market, which represents a record year and well above the 356,280 sqm of completions recorded in 2019. By submarket, 61% of supply in 2020 stemmed from Melbourne's West.

Supply levels are expected to fall moderately to approximately 882,000 sqm in 2021 with 26% of completions for the year expected to stem from speculative facilities. Melbourne's West will again contribute the bulk of new supply in 2021 with just over 400,000 sqm expected to enter the market. Supply levels will also be strong in the North with 307,000 sqm expected to enter the market.

FIGURE 8. MELBOURNE INDUSTRIAL SUPPLY (SQ M)



Source: Colliers Edge

3.3 Occupier Market & Demand

Despite the recent Stage 4 lockdowns, occupier sentiment remains positive across the Melbourne industrial and logistics market, particularly at the larger end of the market with a number of major lease deals being recorded over the past quarter. For smaller occupiers, the impacts of COVID-19 have been more severe as they tend to be more reliant on the local economy and population, both of which have been severely impacted over the past six months. With the recent easing of some restrictions including the approval of one-on-one site inspections, a pick-up in enquiries has occurred and should crystallise into deals in 2021.

Tenant demand has been dominated by e-commerce, retailers and transport and logistics groups. The continued rise of online retail has underpinned this with the rate of growth in Victoria accelerating as Stage 4 lockdowns were introduced. Data from Australia Post showed that online retail in Victoria grew by 157% over the past year, compared to the national average of 89% over the same period. In addition, 38% of all online orders in September were from residents in Victoria, with New South Wales second at 29%.

In 2020, approximately 1,350,000 sqm (5,000sqm+) has been leased across the Melbourne industrial and logistics market and compares to approximately 1,370,000 million sqm in 2019. By market, leasing activity has been strongest within Melbourne's West where approximately 740,000 sqm has been leased, 60% of which has stemmed from the pre-commitment market. Elsewhere, leasing take-up has gathered momentum in the North and includes Ford pre-committing to 51,480 sqm at Merrifield Business Park while Reece have pre-committed to 11,670 sqm within the Melbourne Airport Business Park. Demand remains steady within the South East and Outer East markets with almost 300,000 sqm of take-up being recorded in 2020.

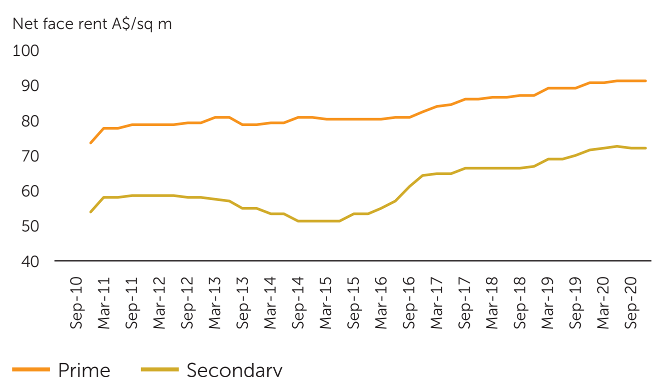
From a vacancy perspective, a modest rise from 3.0% to 3.3% was recorded in December 2020, with the bulk of vacancies being within the secondary market where the vacancy rate is higher at 5.1%.

3.4 Rents & Incentives Trends

Similar to broader trends, net face rents have remained steady over the past six months and currently average A$91/sqm p.a. for prime grades and A$72/sqm per annum. for secondary grades (excl. City Fringe). Looking ahead, we are forecasting rental growth to improve in 2021, albeit below the 10-year average of 2.1% per annum, before picking up in 2022.

For incentives, rises in the order of 2.5% to 7.5% have been recorded since March 2020 across both prime and secondary grades. The upward movement has been most pronounced within the secondary market, underpinned by the higher vacancy rate. In markets such as the Outer East where there is a higher proportion of private ownership (43% of total buildings), the increase in incentive levels has been less distinct.

FIGURE 9. MELBOURNE INDUSTRIAL NET FACE RENTS* (A$/SQ M PER ANNUM)



Source: Colliers Edge

* Excludes the City Fringe Submarket

AUSTRALIA INDEPENDENT MARKET STUDY

MELBOURNE INDUSTRIAL

By Colliers International, February 2021

TABLE 4. PRIME RENTS BY SUBMARKET, Q4 2020

Net Face Rents	City Fringe	North	South East	West	Outer East
A$/sqm p.a.	145	87	94	82	103
6 months change	0.0%	0.0%	0.0%	0.0%	0.0%
12 months change	0.0%	2.2%	0.0%	0.6%	0.5%
Incentive	11.3%	17.5%	18.8%	19.6%	16.4%

Source: Colliers International

3.5 Investment Market

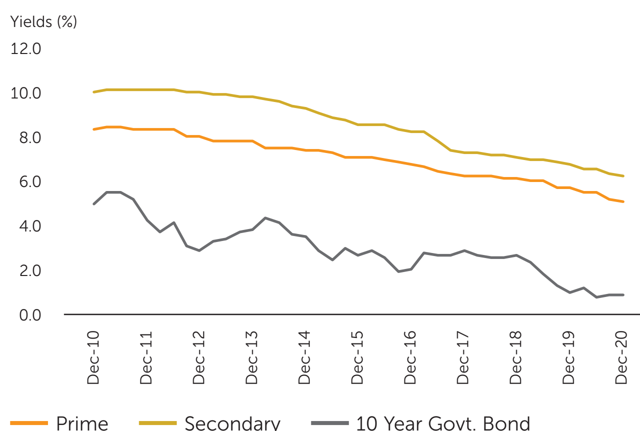
Investment activity within the Melbourne industrial and logistics market has been strong in 2020, albeit restricted by a lack of assets being brought to the market for sale. In 2020, almost A$2.1 billion has traded within the Melbourne market (A$10 million +) across 38 assets. At an average price point of A$54.5 million, this is significantly higher than the A$27.9 million in 2019 and highlights the flight to quality as the bulk of transactions to trade this year have been prime assets.

The largest sale to occur so far in 2020 was Centuria's acquisition of the Telstra data centre at Clayton for A$416.7 million. Other major sales in Victoria included Aldi Dandenong South (A$158.6 million), Ford Mickleham (A$73.5 million) and 415 Cooper Street, Epping (A$71.5 million). A combination of few assets for sale and significant levels of demand has led to further compression in yields in 2020, however, this has been concentrated within the prime market.

3.6 Yields

Melbourne industrial and logistics yields currently average 5.10% (range of 4.75% to 5.75%) in the prime market and 6.25% (range of 5.25% to 7.00%) within the secondary market based on a five-year WALE. We are forecasting some modest yield compression in the prime market in the order of 15 basis points on average over the next 12 months while yields for secondary assets are expected to see some softening in some cases as investors apply a greater discount to asset, location and covenant risk.

FIGURE 10. MELBOURNE INDUSTRIAL YIELDS



Source: Colliers Edge

3.7 Outlook

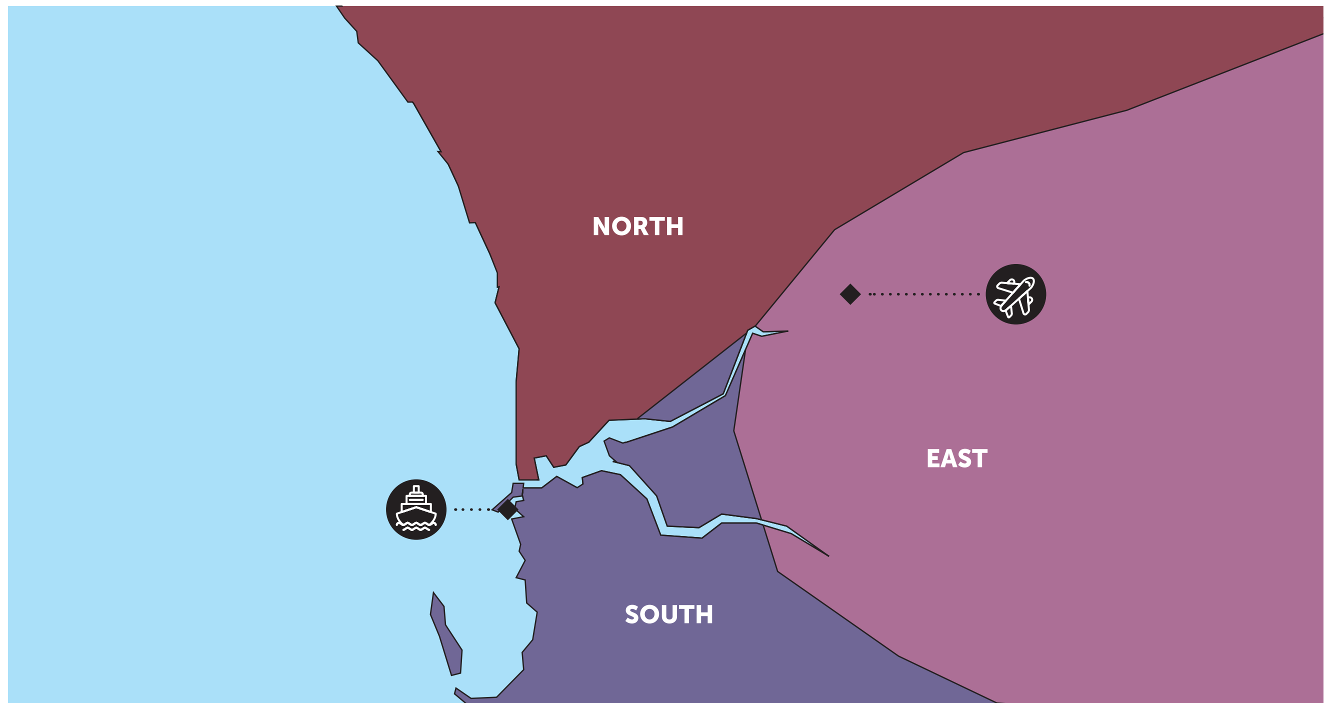
Despite the uncertainty triggered by COVID-19, conditions within the Melbourne industrial and logistics market are expected to remain sound in 2021. There is early evidence that leasing enquiries within the market are starting to revert to "pre COVID-19" levels which should contain any falls in rents across the submarkets. However, incentives have risen since March 2020 and are likely to remain at that level in 2021.

Continued pressure on yields is expected in 2021 as a number of major institutions seek to reweight to the logistics sector.

AUSTRALIA INDEPENDENT MARKET STUDY

PERTH INDUSTRIAL

By Colliers International, February 2021



4.1 MARKET OVERVIEW

The Perth industrial market is divided into three regions North, East and South. The main transport and logistics precincts are in Perth's East and South industrial regions.

The largest precinct in terms of major (>2,000 sqm) industrial space stock is Kewdale/Welshpool. Located approximately 6km east of the Perth CBD and sitting immediately south of the Perth International Airport, this precinct has traditionally been Perth's premier transport and logistics precinct. It is home to the Kewdale Freight Terminal which is linked by rail to Perth's seaports and all other intra and interstate rail freight lines; hence it has historically been the focus of Institutional and major industrial investors.

The second largest precinct is Forrestfield/Hazelmere/ Perth Airport, which hosts the largest international, national and state transport and logistics providers including TOLL, Rand, Northline, CEVA, FedEx, DHL, Mainfreight & Centurion. Additionally, the precinct is home to the state distribution facilities for Coles and Woolworths. The precinct is situated along the freight line that links to the east coast and has emerged as the main in-land automotive transport & logistics precinct.

4.2 Supply

In 2020, approximately 220,000 sqm of new industrial space will be delivered to the Perth market, slightly down from the 232,610 sqm added to the market in 2019. A large portion of the 2020 supply has arisen from design and construct facilities for committed tenants. The East region accounted the bulk of supply in 2020 at 55% while 35% stemmed from the South region.

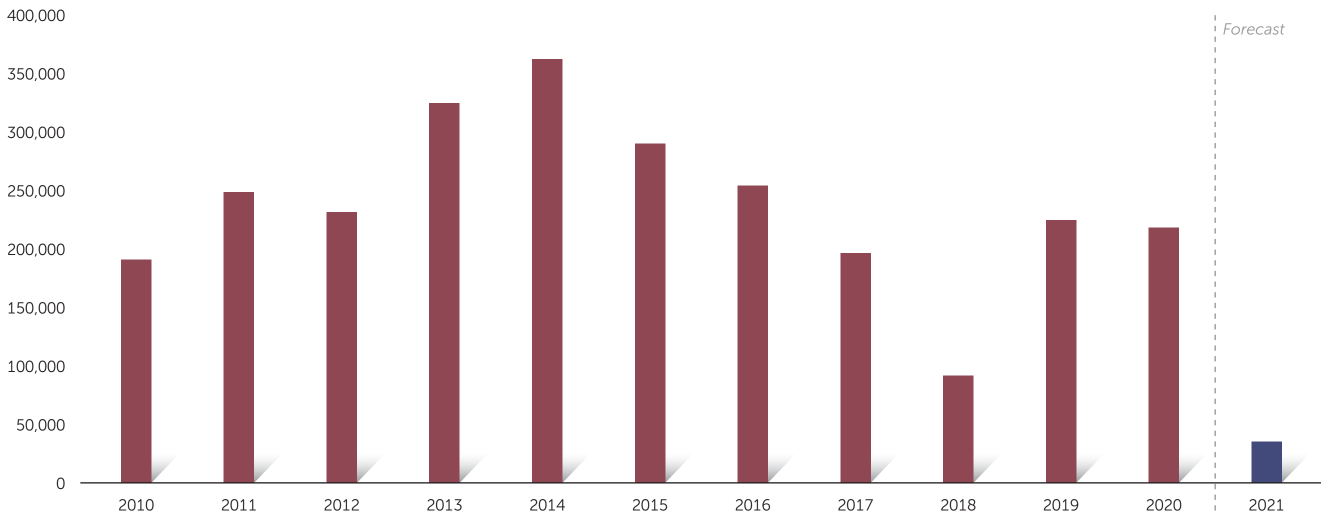
Developers have reported strengthening enquiry levels, which we expect will translate into more project commencements. The supply outlook for 2021 is currently low with only 35,215 sqm expected, however, this is likely to increase as more speculative and design and construct activity eventuates over the course of the next year.

AUSTRALIA INDEPENDENT MARKET STUDY

PERTH INDUSTRIAL

By Colliers International, February 2021

FIGURE 11. PERTH INDUSTRIAL SUPPLY (SQ M)



Source: Colliers Edge

4.3 Occupier Market & Demand

The Perth market generally remains a tenant's market. Leasing enquiries have improved significantly following the COVID-19 lock-down period and they are returning to pre-COVID-19 levels while some developers are reporting even stronger tenant interest than pre-COVID-19.

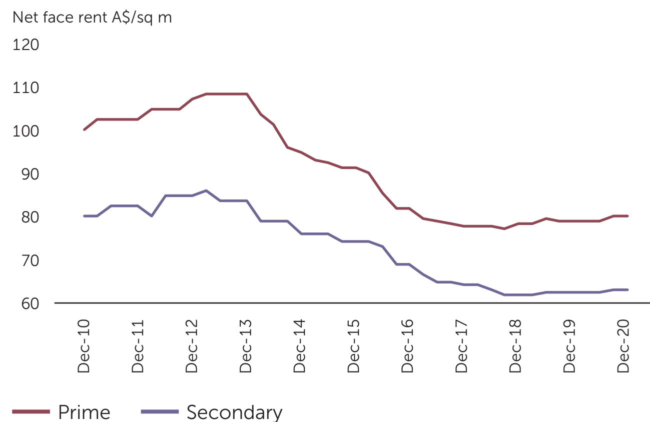
The Perth industrial market was progressing on a recovering trajectory pre-COVID-19. Post lockdown, tenant demand is starting to generate better prospects for rental growth in the larger (5,000 sqm +) prime segment. Like other major city markets, demand from the transport and logistics sector is also strengthening as a result of the shift towards digital transactions. Demand for space has been particularly strong around Perth Airport, the rail intermodal precincts and logistics parks.

Perth's industrial vacancy has increased marginally to 8.7% over the six months to October 2020. The increase was largely attributed to rising vacancy in the South region – which saw an increase of 26,024 sqm to 411,513 sqm. The East region saw an increase of 9,480 sqm to reach 340,180 sqm (or 7.1%), while the North declined 8,865 sqm to 140,525 sqm (or 8.2%).

4.4 Rents & Incentives Trends

Prime rents generally ranged between A$70 and A$95/sqm p.a. At the same time, secondary rents ranged between A$53 to A$73/sqm per annum during the December 2020 quarter. Incentives were stable across secondary assets, while consolidating landlord sentiment resulted in a pull-back in the prime class. Incentives ranged between 10% and 25% for secondary and 10% and 17.5% for prime accommodation.

FIGURE 12. PERTH INDUSTRIAL NET FACE RENTS (A$/SQ M PER ANNUM)



Source: Colliers Edge

4.5 Investment Market

Industrial investment activity in Perth has been subdued by historical standards and reflects a lack of stock being brought to the market rather than demand. Just four assets above A$10 million traded in 2020 with investment volumes for the period totalling A$170.9 million. However, this surpasses the level recorded in 2019 where volumes totalled A$105.4 million. Two major transactions were recorded and were Channel 7 West Perth, Osborne Park (A$75 million) and Stockland's divestment of the Balcatta distribution centre - 22 Geddes & 20 Kenhelm Streets, Balcatta (A$63.5 million) to Charter Hall.

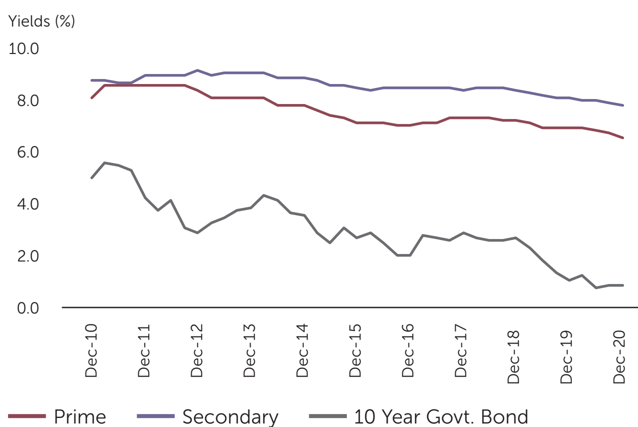
Despite just four assets trading, demand remains elevated, evidenced by the sales campaign of the Balcatta distribution centre where there were eight bids received at the close of round one and included institutional, offshore and private capital.

4.6 Yields

Average prime yields declined by 38 basis points over the year to December 2020 across the Perth industrial market and generally range between 5.75% and 7.35%. As the market reverts to a recovery phase and broader market rental growth prospect returns in a falling interest rate environment, we envisage yields could tighten towards 5.50% for prime properties over the next year or so.

Secondary grade yields have recorded 27 basis points of firming over the 12 months to December 2020 with yields ranging from 7.00% to 8.25%.

FIGURE 13. PERTH INDUSTRIAL YIELDS



Source: Colliers Edge

4.7 Outlook

Overall, the outlook for the Perth industrial market remains positive. In general, the impacts of COVID-19 on the local market have been modest, particularly when compared to other sectors. However, it still remains early to understand the long term impacts it will have on leasing demand as a number of occupiers have held off their leasing decisions until the economy improves.

Heading into 2021, the market will be supported by heightened levels of infrastructure spending and demand for key commodities such as iron ore. Given this, the Western Australian economy is likely to outperform other states in 2021 which could trigger an increase in industrial demand across the Perth market.

AUSTRALIA INDEPENDENT MARKET STUDY

FUTURE OF OFFICE

By Colliers International, February 2021

Over 2020, the COVID-19 pandemic has turned life and work upside down. We have all had to get used to social distancing and businesses rapidly adapting to shutdowns with many white-collar employees required to work from home. During the early weeks of work from home, many businesses reported productivity was being maintained or even increased as they grappled with the rapid change in economic conditions and what that meant for their businesses. For many it is a matter of survival with revenue drying up overnight. This resulted in a massive shedding of jobs and reduced work hours which led to the largest stimulus packages in Australian history including JobKeeper, increases in JobSeeker and now JobTrainer.

So, what does all of this mean for the demand for offices going forward? Looking at the data on occupancy from past shocks can assist in forming a view of what is likely to happen in the future. We know that changes to workplaces is nothing new and they have evolved substantially over the last couple of decades. At the heart of change is the technological advances we have seen including development of Wifi (1997), Google (1998), cloud computing (2006) the iPhone (2007), Apps (2008) the iPad (2010) and Skype for Business (2015). Within workplaces we have seen activity-based working adopted in the 2000s, hot desking and the use of flex-space in more recent years. Although there is still a high level of uncertainty as to how long the pandemic will last, we are starting to turn our minds to how offices will look and what lasting impact this pandemic will have on office demand in the medium and long term. We have seen a plethora of workplace surveys on the effectiveness of work from home and the preference of some to continue to do so permanently.

Technology has advanced significantly including the rapid adoption of video conferencing and ability to access work servers remotely with this technology being put to the test globally during the pandemic. In the short term many white-collar sectors were able to move to remote working with limited impact on productivity. However, as the pandemic has progressed, and we have needed to work remotely for longer, the novelty has worn off and some of the cracks of working remotely are starting to show. Decision making can be slower, and collaboration is more difficult due to the lack of face-to-face contact. The ability to train new starters and turn around to ask a colleague how to do something or their thoughts on a problem is more difficult remotely. The conversation around the water cooler with those outside your team where an idea is shared doesn't happen. The absence of all of these things in the medium to long term are likely to impact the team's creativity, collaboration and productivity.

There have been many surveys conducted on work from home which survey worker preferences, however they do not provide true insight into the decisions regarding occupancy, the location of offices and other factors such as, cybersecurity, workplace safety, staff retention, training of new staff, client engagement and corporate culture. The trend across most of these surveys is the majority of office workers still want to have some face-to-face contact with colleagues but would prefer that not all work hours are in the office. One of the larger surveys conducted in late April was from Bates Smart and showed that only 17% of people would give up their permanent desk as 84% missed the social interaction with their colleagues.

These evolutions have changed how we occupy office space and the type of space we occupy, rather than reduced our need for offices. We suspect that once the health crisis has passed and business starts to return towards more normal operations that this shock will be no different. Until 2004, secondary grade space had higher occupancy than prime grade and by 2010 prime grade had higher occupancy than secondary grade space. Occupancy in secondary grade space is still equivalent to what it was in 1993, despite having cheaper rents than prime grade. This indicates that there is a tenant preference for newer buildings which allow more efficient and technologically adaptable workplaces, which improves staff retention, engagement and therefore productivity.

We are starting to see some trends start to emerge. In larger cities there is talk of a 'hub and spoke' model, where there is a smaller CBD hub office and there are several satellite offices which are closer to home. An interesting example is banking where the branch network could also be utilised as an office for some of the current CBD workforce. This could lead to higher demand in suburban office locations. Conversely there are also some tenants which are looking at consolidation of leases once a lease expires and moving to one central location.

We are starting to see some tenants looking for more flexibility in lease terms with the ability to increase and decrease occupancy as their business needs change. We think that this is likely to lead to more adoption of flex-space for the increases in demand when the business need requires. While we are seeing that the pandemic has changed the way we work, we think that this will lead to the next evolution as to how we use office space rather than all of us taking our laptops and moving home. They are more likely to be collaborative spaces with more break-out areas and more flexible hours where some employees work in the office and some from home. Ultimately people are wired for social connection and offices play a key part in providing a place for that connection to take place. We see this as being key to underpinning the next evolution of office design and the use of office space.

AUSTRALIA INDEPENDENT MARKET STUDY
SYDNEY SUBURBAN OFFICE

By Colliers International, February 2021

6.1 MARKET OVERVIEW

Sydney suburban office markets are quite diverse and fragmented with the City Fringe and South Sydney being the largest markets amongst them. The City Fringe has about a million square metres of office space and is considered a commercial hub for IT, Technology, Digital, Media and Creative industries. Major tenants in the precinct include Google, IBM, Channel 7, Fairfax Media, Domain and Thompson Reuters, to name just a few. Recent years have witnessed the rapid rise of flex-space operators with the likes of WeWork and HUB Australia having a strong presence in the area. Tenants have been attracted to the City Fringe due to a wide range of amenities, public transport (Central Stations, Redfern and the new Light Rail Link to the CBD) and proximity to major universities such as the University of Sydney, University of Technology Sydney and University of Notre Dame.

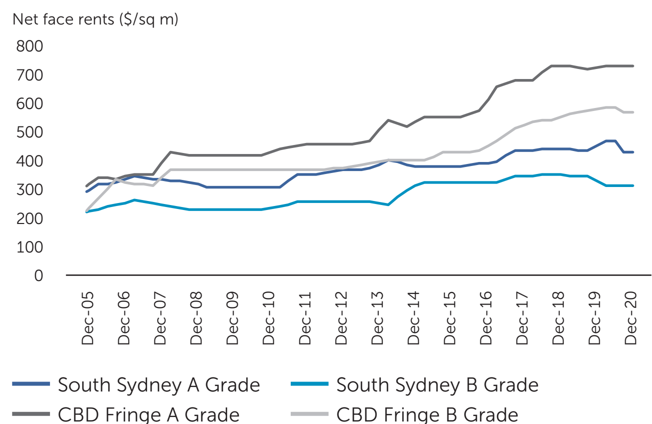
The South Sydney office market (including Mascot) comprises about half a million square metres of office space with a major portion of it being corporate parks and Strata offices. Due to its location, South Sydney is dominated by airport-related industries, transportation, logistics and government agencies. The area is currently undergoing a significant urban regeneration program which also sees many office and industrial buildings be converted to residential uses. Tenant demand, however, has remained strong on the back of improving connectivity with the CBD and business amenities.

6.2 Leasing Activity, Demand and Supply Drivers

The more inner markets of North Sydney, St Leonards and Chatswood recorded increases in vacancy over the first 6 months of 2020. This is a result of negative net absorption, rather than any major increases in supply. While Parramatta and Macquarie Park also recorded vacancy increases, these were off much lower bases, and in the case of Macquarie Park, was very much driven by an increase in vacancy in secondary grade space.

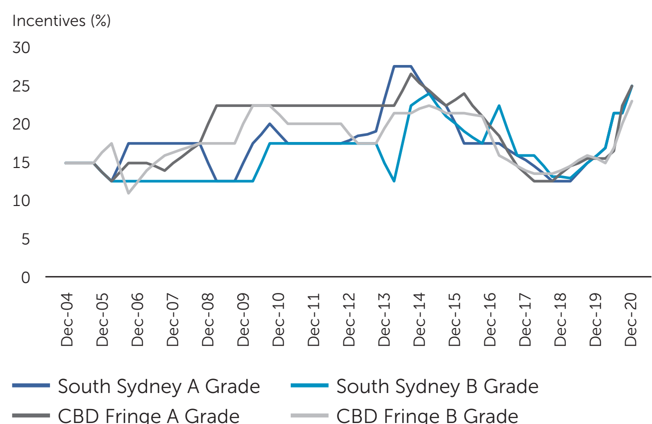
While there is currently a clear divergence between the vacancy rates in the North Shore markets versus Parramatta and Macquarie Park, we do not anticipate that this will remain the long-term dynamic. Vacancy in both Parramatta and Macquarie Park are forecast to increase as significant new supply reaches completion in those markets over the next 2 years. The Parramatta market will increase in size by almost 200,000sqm over the next 2 years, which is a significant 26% increase. Macquarie Park should grow by 94,000sqm (10.5%) over the next 2 years, but also has the potential to add an additional 100,000sqm over the 2 years following (2022 to 2024) if pre-commitment activity eventuates to support these additional new developments.

FIGURE 14. SYDNEY FRINGE AND SOUTH A & B GRADE NET FACE RENTS, 2004 TO 2020



Source: Colliers Edge

FIGURE 15. SYDNEY FRINGE AND SOUTH A & B GRADE INCENTIVES, 2004 TO 2020



Source: Colliers Edge

AUSTRALIA INDEPENDENT MARKET STUDY

SYDNEY SUBURBAN OFFICE

By Colliers International, February 2021

TABLE 5. NET FACE RENTS BY MARKET, Q4 2020

Net Face Rents	City Fringe		South Sydney	
Q4 2020	A Grade	B Grade	A Grade	B Grade
A$/sqm p.a.	$725	$565	$425	$310
6-month change	0.0%	-2.6%	-8.6%	0.0%
12-month change	0.7%	-1.7%	-5.0%	-5.3%

Source: Colliers International

6.3 Rents and Incentives Trend

The decline in A Grade net face rents in Sydney over the past six months was largely attributable to an 8.6% decline in the South Sydney precinct. Parramatta recorded a modest increase in face rents (0.4%) while all other markets were flat. While leasing deal volumes are below those recorded this time last year, enquiry evidence tells us that markets that are furthest from the CBD are performing somewhat better. This is due to the current COVID-19 climate, and the preference by some tenants to be in less dense suburban markets. Norwest presents the best example of this trend, with A Grade net effective rents in this market actually increasing over the year by 3.7% over the past six months.

Macquarie Park saw flat growth in net face rents over the six months to December 2020, however, a rise in incentive levels saw net effective rents fall by 8.4% over the same period. Parramatta recorded a 6.4% decline in effective rents, South Sydney a touch over 15% (15.1% decline) while all other markets recorded net effective rent declines of between 4% and 10%.

While incentives have increased since the start of the year in all markets, these increases have been far less dramatic than those recorded in the CBD. The largest incentive increase since Q4 2019 has been recorded at St Leonards, where average incentives have increased from 20% to 32% in Q4 2020. Parramatta and South Sydney have recorded a 8% and 9% rise respectively over the same period, while all other markets were between 4% and 10% increases. The increases in South Sydney and the CBD Fringe are in response to limited tenant demand and new supply, while in Parramatta, the more institutional nature of the market, as well as the very low incentives on offer at the end of last year (15% in Q4 2019), meant that an above metro average rise in incentives was not unexpected in that market.

6.4 Sales and Construction

There were a few transactions in Sydney metro office markets which produced evidence of no movement in our current yield ranges. In late 2020, CapitaLand (Ascendas REIT) acquired 1-5 Thomas Holt Drive in Macquarie Park from AMP Capital for A$288.9 million, reflecting an initial yield of 5.90% and a capital value of A$7,372/sqm. Similarly, the sale of Pinnacle Office Park in Macquarie Park to Singapore's Keppel REIT is another good example of a recent transaction that was struck at the top end of our average yield range of 5.25%. The asset was purchased off Goodman Group for A$306 million in early September 2020, and the total NLA is 35,132sqm. Also, in Macquarie Park, Ascendas REIT has recently completed a A$167.2 million deal to acquire 1 Giffnock Avenue (MQX4), Macquarie Park from developers Frasers Property Industrial and Winten Property Group. A 3-year rental guarantee has been provided, with the building due for completion in mid to late 2022. The initial yield on the rental guarantee portion of the transaction was 6.1%.

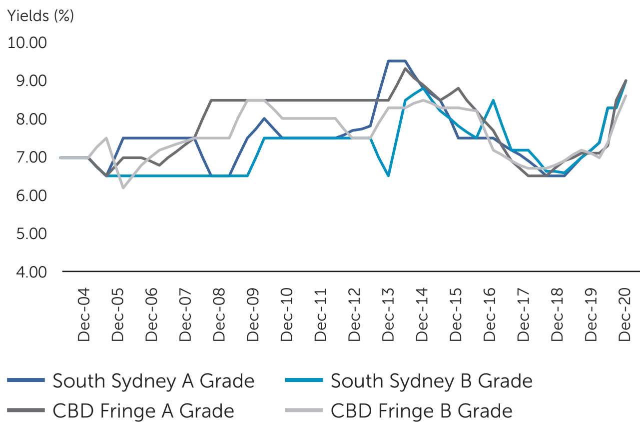
6.5 Yields

The outlook for yields is still very difficult to determine with a lack of transactional evidence. At this point, any impact to the overall value of office assets is still attributable to specific adjustments to the Discounted Cash Flow (DCF) model, that takes into account weakness in occupancy markets. These include a reduction in face rental growth outlook, an increase in letting up timeframes, and an increase in incentives for incoming tenants. That being said, it is likely that commercial property across all asset classes will be viewed through a lens of higher risk, as the majority of underlying tenant covenants have been negatively impacted, and the risk to cash flow has increased. The exception would be fully leased, government-tenanted assets, where it is arguable yields could continue to

compress in this environment, particularly given the low Australian dollar. The sale of 45-53 Kembla Street, Wollongong is a prime example of this dynamic. The asset is fully occupied by the Australian Taxation Office (ATO) on a 15-year lease ending in September 2028. The equivalent yield for the transaction is 5.50%, which is equivalent to an average yield across our Sydney Metro precincts as at September 2020. Given the scarcity of these types of assets around the country, we can reasonably deduce that an asset with same metrics and covenant would transact for below average yields in a capital city market.

It is our base case forecast as at Q4 2020 that prime grade yields will soften by 12.5 basis points over the year to September 2021, and secondary grade by 25 basis points, as purchasers' price in the higher vacancy and cash flow risk of those assets. Our yield outlook has improved since our Q3 2020 forecast update based on the continued flow of capital still searching for quality Sydney metro assets, as well as the significant progress that Sydney has made in containing COVID-19, allowing the metro markets to stabilise somewhat quicker than we previously thought.

FIGURE 16. SYDNEY FRINGE AND SOUTH A & B GRADE YIELDS, 2004 TO 2020



Source: Colliers Edge

6.6 Outlook

The outlook for the Sydney metro A Grade market is still broadly positive, as we expect Flexspace operators to begin a substantial push into metro office markets to meet the demand of small start-up businesses and those CBD based businesses who want to provide a 'spoke' option for their employees. We are forecasting average A-grade net face rents across the Sydney Metro markets to remain fairly stable at 0.2% over 2021 before recovering in 2022 with 3.3% expected. We are forecasting the 3-year annual average growth rate of net face rents to be around 1.8% which compares to 3.2% over the previous 3 years. It is still a reasonable outlook given the extremely challenging global and local economic conditions. For the B-Grade market, the outlook is of very limited face rental growth over the next few years with an annual average of 1.1% expected compared to 4.4% over the previous 4 years. Landlords will have to offer very attractive deals to keep tenants when good A grade options will be relatively plentiful. We do expect, however, that A grade incentives will peak higher than B Grade, which is more to do with ownership structures (i.e. institutional owners are more prepared to offer higher incentives) than underlying demand.

AUSTRALIA INDEPENDENT MARKET STUDY

BRISBANE SUBURBAN OFFICE

By Colliers International, February 2021

7.1 MARKET OVERVIEW

The Brisbane Fringe Office market extends across five precincts. Urban Renewal is the largest growing area in the Brisbane Metro market, contributing about 520,745 sqm of stock, or the equivalent to 43% of the office stock in the Fringe region. It extends from New Farm to Bowen Hills and includes Fortitude Valley.

Inner South is the second largest office precinct in Brisbane Fringe, contributing about 261,671 sqm of stock to the market. It extends from South Brisbane to Greenslopes, including also Woolloongabba and West End.

Milton is the oldest Brisbane Fringe precinct offering circa 232,132 sqm of net lettable area. Milton is undergoing a continual transformation with some of the well-known buildings going through refurbishments (e.g. 339 Coronation Drive). Milton is home to a diversity of knowledge-based businesses in the fields of engineering, design, civil contracting, and the digital industries. Spring Hill is well-located adjacent to the CBD area and generally offering strata offices and a net lettable area of circa 134,904 sqm. Toowong is the smallest fringe precinct in Brisbane offering circa 75,000 sqm of net lettable area.

7.2 Leasing Activity, Demand And Supply Drivers

Employees are gradually returning to the office as the infection rate remains very low within the state. However, office occupancy is still below pre-pandemic levels as various employers continue to actively support flexible and working from home arrangements.

There has been limited leasing activity recorded this quarter in the Brisbane metro market, like what we have seen across all other office markets in Australia. However, we recorded a few medium-size deals bringing hope that demand levels are gradually heading in the right direction and providing tangible evidence of solid market fundamentals.

Some of the largest deals fully executed over the past few months include:

- 194 Breakfast Creek Road in Newstead: co-working operator, Work Club Global, leased 1,600 sqm for $675/sqm p.a.
- 33 Park Road in Milton: Conoco Phillips, American energy corporation, leased 1,527 sqm for $525/sqm p.a.
- 339 Coronation Drive in Milton: Fusion Sport, providing data analytics and engineering services to the sports industry, leased 1,200 sqm for $550/sqm p.a.
- 100 Melbourne Street in South Brisbane, Acciona Geotech Group Services subleased 2,300 sqm of sublease space for $615/sqm p.a. from Peabody.

Secondary fitted stock has driven demand and enquiry levels this quarter as tenants are generally looking for more flexible and fast-tracked relocation opportunities taking advantage of softer market conditions.

The next 6-18 months are expected to be challenging for the office market and within this timeframe we expect to see more evidence of the extent of the structural changes over the long term.

Updated Property Council of Australia (PCA) vacancy data has revealed an increase on the vacancy rate from 13.6% in January to 14.2% in July 2020 with many precincts (except Inner South) reporting a gradual increase in vacant space over the past 6 months.

Forecast market vacancy is expected to reach 17.3% over the next 12 months and remain at high levels due to the new development pipeline and some space to be vacated by occupiers affected by the pandemic within the Spring Hill, Urban Renewal and Inner South precincts.

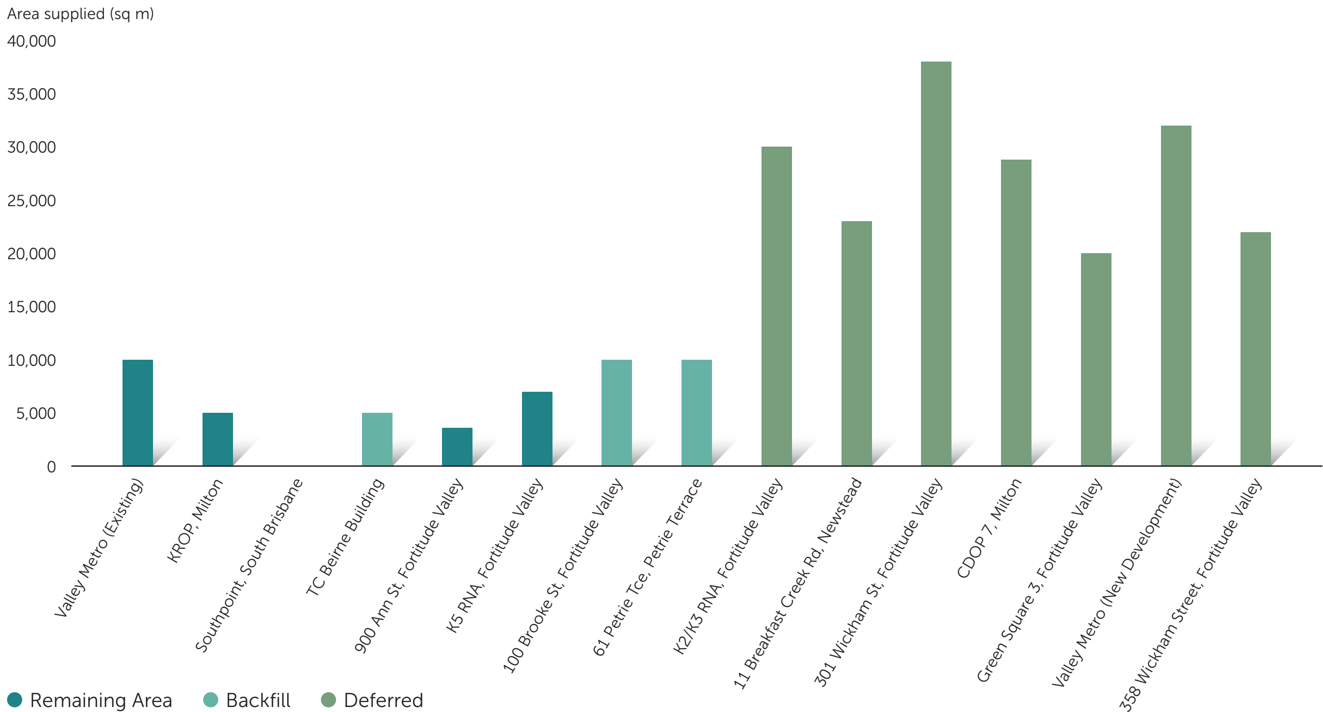
The Urban Renewal precinct remains the largest and tightest precinct across the metro market recording a vacancy rate of 11.5% in July in 2020. This precinct was the only one operating with a vacancy rate below its respective long-term average (of 12.6%) over the first half of the year. This trend has changed over the second half of the year as Virgin Australia has vacated 13,220 sqm (equivalent to 2.5% of the precinct stock) at 56 Edmonstone Road in Bowen Hill and relocated its reduced workforce to the Flight Centre headquarters subleasing approximately 9,000 sqm at 275 Grey Street in South Brisbane.

Office stock within the Urban Renewal precinct increased by 3,500 sqm to 524,245 sqm in July 2020 as The Eminence project reached practical completion (PC) over the first half of the year having a reported occupancy of about 80%.

Over the first 6 months of 2020, the Inner South precinct was the only precinct reporting a reduction on the vacancy rate to 12.8% as at June-2020 (from 13.6% in January 2020) following a positive net absorption of circa 1,950 sqm. The expected completion of the speculative development known as the Mobo project in late 2021 may trigger a large increase in vacancy if leasing demand does not recover over the next 12 months.

The Milton precinct reported the largest 6-months net absorption of 4,641 sqm in July 2020, albeit the vacancy rate increased slightly to 18% (from 17.7% in January 2020) as the refurbishment of the building at 2 Gardner Close was completed adding 4,237 sqm of B Grade space.

FIGURE 17. BRISBANE METRO OFFICE SUPPLY PIPELINE – 5,000+ SQM



Source: Colliers International

The smallest precincts of Spring Hill and Toowong reported vacancy levels of 20.9% and 13.9% (respectively) in July this year. Our forecast indicates that vacancy levels within these two precincts will most likely remain elevated due to the low stock quality.

Sub-lease space across all precincts and grades has held relatively steady in the range of 1.2-1.3% over the past year. Over the next 6 months, we forecast an increase of sublease space of about 10,000 sqm or the equivalent to 0.8% of the market stock. We understand that the Inner South and Spring Hill precincts will report the largest increase in sublease space over the next 6 months. Specifically, the University of Sunshine Coast is expected to vacate and offer circa 3,500 sqm of sublease space at 52 Merivale Street in South Brisbane. International Education Services is expected to vacate and offer 6,000 sqm of sublease space at 433 Boundary Street in Spring Hill.

7.3 Rents and Incentives Trend

In Q4 2020, gross face rents have held steady across all precincts and grades. However, we have seen landlords being more willing to negotiate incentives which have generally increased in the range of 1.5-2 percentage points depending on the precinct and grade.

A-grade average incentives have increased from 36.7% in June 2020 to 38.5% in December 2020, while B grade average incentives have increased from 35.8% in June 2020 to 37.9% in December 2020.

A ‘wait and see approach’ across occupiers has continued to dominate the market due to the decline in business revenue and the uncertainty about business outlook. However, this quarter we have witnessed a few deals across the largest precincts supporting our view that gross face rents are holding steady and incentives are reporting a gradual increase, particularly in the way of rental abatements.

AUSTRALIA INDEPENDENT MARKET STUDY

BRISBANE SUBURBAN OFFICE

By Colliers International, February 2021

Over Q4 2020, the Queensland State Government also announced a 25% land tax rebate and an additional 3 months referral of tax liabilities for the 2020/21 assessment year. This assistance is expected to reduce outgoings growth over the next 6 months and partially offset the negative impact on net effective rents caused by the increase in incentives. To access this financial support, landowners are required to lodge an application with the Office of State Revenue.

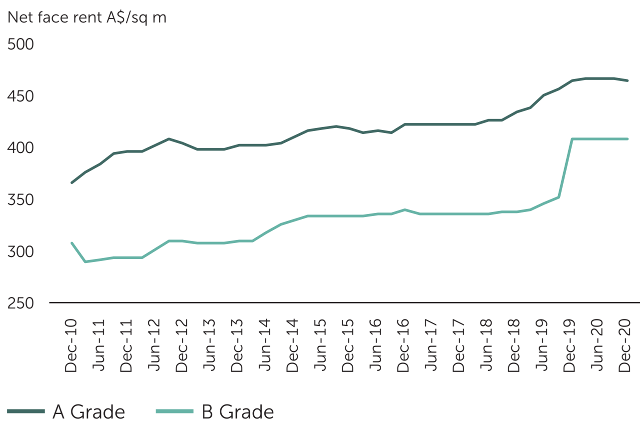
Considering the current and forecast stock imbalance between supply and demand, net effective rents for A and B grade buildings are forecast to follow a downward trend until June 2021. We expect the recovery will take a few years as net effective rents are forecast to return to pre-pandemic levels by 2024. Average net face rents are summarised below:

TABLE 6. NET FACE RENTS BY MARKET, Q4 2020

Net Face Rents	Inner South		Urban Renewal		Milton		Toowong	
Q4 2020	A Grade	B Grade	A Grade	B Grade	A Grade	B Grade	A Grade	B Grade
A$/sqm p.a.	$496	$435	$509	$413	$439	$390	$436	$399
6 month rental change	-0.2%	-0.2%	-0.2%	-0.3%	-0.2%	-0.2%	-0.2%	-0.2%
12 month rental change	0.1%	-0.2%	-0.2%	-0.3%	-0.2%	0.7%	-0.2%	-0.2%

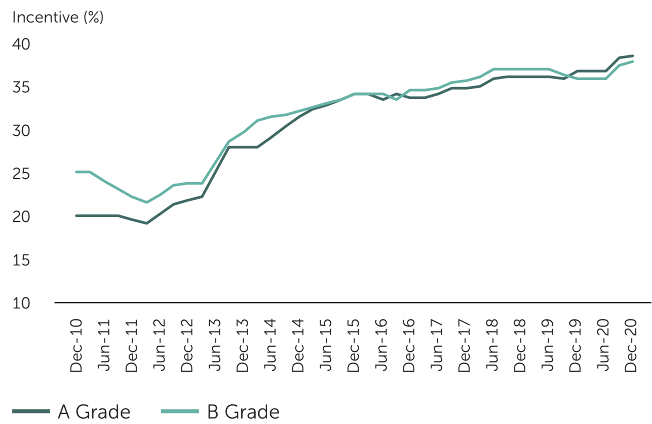
Source: Colliers International

FIGURE 18. BRISBANE METRO OFFICE NET FACE RENTS, 2010 TO 2020[1]



Source: Colliers Edge

FIGURE 19. BRISBANE METRO OFFICE INCENTIVES, 2010 TO 2020



Source: Colliers Edge

1 The Brisbane metropolitan market went through a recovery process in 2019, with the market reporting the largest fall in vacancy nationally over the first half of 2019. As a result of improved market conditions and the limited availability of contiguous space, average B grade net face rents in the Brisbane metro market reported an increase of 2.2% in Q4 2019. Brisbane metropolitan vacancy also tightened significantly in 2019, from 15.7% in January 2019 to 13.6% in January 2020, underpinned by an annual market net absorption of circa 30,800 sqm.

7.4 Sales and Construction

Office investment transactions (above $5 million) in the Greater Brisbane region have remained subdued this quarter, reaching $32 million of settled sales for the year to date. If we add the two deals (pending settlement) associated to the sale of the new development at 14 Stratton Street in Newstead, sales volumes would increase to about $225 million. This is in fact the lowest number and volume of sales recorded since the start of the investment sales series in 2007.

Investment opportunities offering long-WALEs and supported with defensive tenants remain heavily sought after due to the limited investment opportunities reaching the market. The sale of the new development at 14 Stratton Street in Newstead which involved two different deals is a clear evidence of this trend.

Office projects under construction are forecast to add 77,550 sqm (representing about 6.3% of the current stock), with 39,750 sqm of pre-committed space across three projects (out of a total of six projects under construction). If we add to the forecast supply the speculative project at 895 Ann Street (commenced in late 2020), the new supply will increase to 100,550 sqm (representing 8% of the current stock and potentially adding nearly 2 percentage points to vacancy levels).

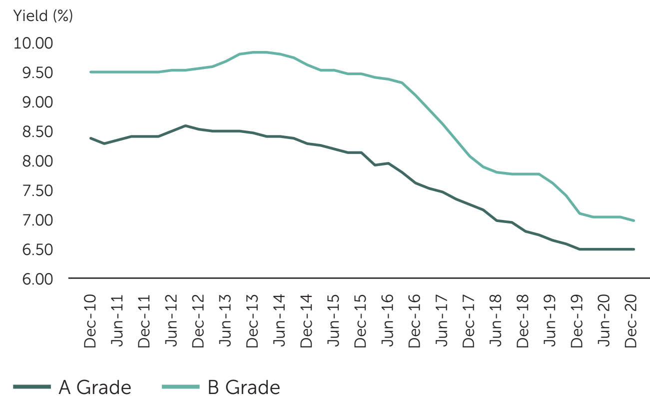
Prior to the start of the pandemic, we expected the uncommitted space from new developments under construction was going to be easily absorbed in about one year. Under current market conditions wherein current and forecast office supply is exceeding demand, we expect that the new development supply would cause a flight to new and quality stock, triggering a larger gap between prime and secondary occupancy potentially reaching levels of 9-10 percentage points (as seen about a decade ago). At present the occupancy gap between prime and secondary stock sits at about 5.5 percentage points. The increase in the gap is forecast to occur as new developments will most likely offer substantial incentives to lock in quality tenancies.

7.5 Yields

The lack of transactional evidence and the uncertainty in relation to the discounted cash flows for office investments make the yield outlook very difficult to determine.

Our A grade yield forecast is for a steady outlook over the forecast period considering that pending transactions indicate long WALE prime assets having a more stable forecast with the potential for yields to tighten for high-grade defensive assets. In the case of B grade buildings, we expect to see a modest softening of yields towards the second half of 2021 due to the weak cash flow fundamentals, albeit there is limited evidence of this happening yet.

FIGURE 20. BRISBANE METRO OFFICE YIELDS, 2010 TO 2020



Source: Colliers Edge

7.6 Outlook

We are commencing to see some potential structural changes happening across the Brisbane Metropolitan office market. In the case of the leasing market, flexibility is driving occupiers' decisions with expectations that the office will consolidate as a central location to maintain company culture and add value to business performance and productivity, while allowing employees to work under more flexible working arrangements. Landlords on the other hand have become more willing to change the way they do business to meet the needs and requirements of tenants.

Under these changing market conditions, the Brisbane Metropolitan vacancy is expected to peak at about 19% by late 2021 as the recovery of white-collar employment will take about two years and over 31,000 sqm of spec developments will reach practical completion in 2021 putting further upward pressure on vacancy. Average gross face rents are expected to hold firmly, albeit average incentives will continue the upward trend potentially approaching 40% for A grade buildings by late 2021. As a result of these trends, net effective rents will fall about 7% compared to pre-pandemic levels by 2021/22, with the recovery extending to 2024/25.

In the case of the investment market, the pricing of risk has become more sophisticated and aligned to the risk profile of the particular investment disregarding traditional popular locations, perceptions of the market and even growth potential while raising the value of secure and long-term revenue streams and returns. The investment market has shown solid signs of improvement over the second half of 2020 and this trend is expected to continue in 2021, with sales volumes commencing the recovery process over the next 6 months and consolidating over the second half of 2021. Yields have become heavily dependent on the specific risk profile of the investment and this trend is expected to continue in 2021. Hence, we expect to see further compression of yields for distinctive assets offering secure long WALE, while assets needing repositioning will most likely be more harshly priced.

AUSTRALIA INDEPENDENT MARKET STUDY

MELBOURNE SUBURBAN OFFICE

By Colliers International, February 2021

8.1 MARKET OVERVIEW

The Melbourne metro office market comprises five precincts, the largest market being the City Fringe which covers approximately 983,000 sqm, or the equivalent to 30% of total office stock in the metro region. The City Fringe includes major inner-city office markets including Richmond, South Yarra, Collingwood and South Melbourne. Tenants in this market are attracted to the connectivity to the city as well as the retail amenity and attracting staff who wish to work closer to where they live. This market is experiencing a rise in office development due to rising tenant demand to be located in this market- particularly those migrating from further out locations.

The second largest market is the Outer East, also comprising 30% of the total office stock and attracts tenants to larger office business parks. Compared to inner office market, rents in outer east are lower and appeal to tenants that require larger spaces. The Inner East is a well-connected submarket and includes major office hubs such as Camberwell and Hawthorn. These areas are well serviced with public transport as well as retail amenity. The South East is a tightly held market and attracts a hybrid of tenants who also wish to be located close to industrial areas. Office markets in this precinct include Oakleigh and Moorabbin where public transport options are quite limited. The fifth sub-market is the North & West which geographically covers a large area however a small office footprint. These areas are dominated more with industrial tenants, office markets are Essendon Fields extending out far west to Werribee.

8.2 Leasing Activity, Demand and Supply Drivers

Leasing activity over the 3rd quarter of 2020 continued to be severely constrained as tenants were prevented from inspecting buildings as a result of Melbourne's Stage 4 lockdown. However, one notable transaction was the Bunnings deal at Growthpoint's newly completed building at Botannica Business Park. Bunnings have leased circa 13,900sqm of space in a 19,500sqm building which was completed prior to our March 2020 data collection. This deal alone equates to a 2% reduction in the City Fringe vacancy rate. Bunnings will vacate space in two buildings located in Cato Street and Auburn Road, Hawthorn. Both of these buildings sit within our Inner East precinct, and we have recognised this vacancy in the September 2020 figures so that it accurately reflects the tenant flow. Given the relatively small size of the Inner East market (581,000sqm), the departure of a tenant of the size of Bunnings has had a large impact on the vacancy rate. Vacancy in the Inner East has risen by 4.4% from March 2020 to 10.97% as at September 2020.

Sub lease vacancy makes up 22% of total vacancy in the City Fringe market. It is important to note that given the lockdown in Melbourne at the time of collecting data, we have assumed that all space available to sublease is vacant. In reality, as tenants make their way back into the office in Q4 2020 or Q1 2021 (assuming permission is granted), it is likely that some of this space will continue to be occupied as a sub-lessee is sought. As we move in to 2021, and assuming improving economic and health conditions, we anticipate that some of this space will be removed from the sub-lease market.

Vacancy, however, is likely to remain elevated through 2021 and in to early 2022, as almost 195,000sqm of net new supply is due for completion in the City Fringe in the next 18 months. We have made an assumption that some secondary space will be vacated in the next 18 months also, although these assumptions are conservative given the outlook for alternative uses is also unclear. However, it is worth noting that following the City Fringe vacancy reaching its previous peak of 8.64% in September 2013, the City Fringe total market size actually shrunk by 6,156sqm. It is therefore entirely possible that significantly more withdrawals will take place over the next 2 to 5 years, which will in turn impact our vacancy outlook, and we will be monitoring this trend closely. Net absorption is forecast to be 170,000sqm over the next 18 months, falling just short of net supply. However, beyond mid-2022, we expect absorption to outpace supply, resulting in a falling vacancy rate.

All Melbourne metro precincts are expected to broadly follow a similar vacancy trend as the City Fringe. However, we do expect that the South East and Outer East will settle at a higher vacancy rate than the other markets, as tenants move to newly developed space with generous incentives. We also expect numerous Flex-space operators will prefer new A Grade space close to public transport nodes.

The overall Metro Melbourne vacancy rate is 11.2%, significantly above the long-term average of 6.9%. The metro market added a total of 41,415sqm of new supply in the 6 months to September 2020, while almost 110,000sqm was vacated. Again, with reference to sublease space, we note that almost half of the 'vacated' space is made of sublease, and at the time of writing it was not possible to know what is occupied and what is not. Therefore, this number may look quite different in March 2021 when occupancy is hopefully normalised.

The St Kilda Road market and Southbank market vacancy as at July 2020 were 9.28% and 10.49% respectively, with St Kilda Road being the only metro market where the vacancy rate sits below the long-term average. However,

as with other markets, we have calculated space we know to be vacated since that time, and also space that is available for sublease, and anticipate a significant rise in vacancy in St Kilda Road, to 13.9%, in January 2021. Vacancy in Southbank is expected to rise to 14.3%. Both of these markets have continuing upcoming supply forecast, and therefore the outlook for the vacancy rate to remain higher than average. Again, St Kilda Road has a long history of buildings being withdrawn for residential development and we have made an assumption that this trend re-emerges by late 2021.

8.3 Rents and Incentives Trend

The largest decrease in net effective rents recorded was in the A Grade City Fringe market, where net effective rents declined by 15.4% over the 6 months to December 2020. This is as a result of average incentives increasing from 16% in March 2020 to 26% in December 2020. The New A Grade market saw a smaller increase in incentives – from an average of 25% (June 2020) to 32%, (December 2020) meaning the impact on net effective rents was not as pronounced. Face rents also remained stable for New A Grade product, although we expect a minor decrease in face rents over the next year, as competitive pressure increases with new buildings reaching practical completion. Still, like most markets around Australia, the response of landlords to the challenging economic conditions has been to increase incentives, which appeals to tenants as it reduces or negates any upfront capital costs with regards to fitout and potentially some rent free period.

Given the Outer East market already had reasonably high vacancy prior to COVID-19, the impact on rents has been more subdued, largely because a lot of landlords are already close to the peak of the incentive they can offer. This market now offers some of the best value office space in the country, with average effective rents for newly built A Grade product ranging from $178 to $215/sqm per annum. We expect that from mid to late 2021, especially if the government's incentives to grow the manufacturing sector prove successful, that manufacturing and wholesale trade type tenants will expand again in that market.

On St Kilda Road, net face rents have grown considerably over the last 6 months, at 14.4% for A Grade and 1.4% for B Grade. Incentives, however, have also risen rapidly, which has reduced effective rents by 4.1% for A Grade and 9.1% for B Grade. Given the institutional ownership of this market, incentives now resemble those on offer in the CBD, rather than the more privately held suburban metro markets. In Southbank, a large increase in incentives was also recorded in the A Grade market, again, as this market is in direct competition with A Grade CBD product.

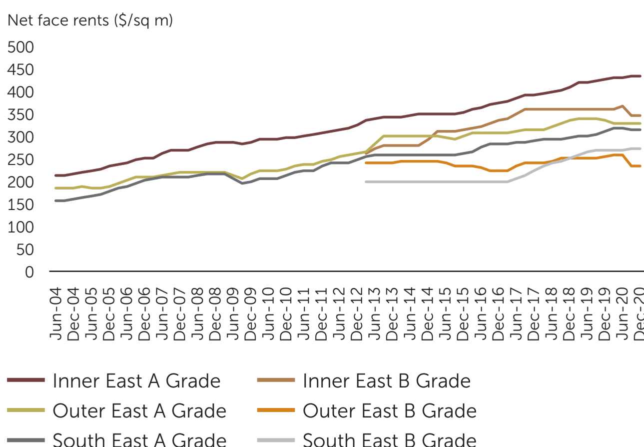
Average net face rents are summarised below:

TABLE 7. NET FACE RENTS BY MARKET Q4 2020

Net Face Rents	Inner East		South East		Outer East	
Q4 2020	A Grade	B Grade	A Grade	B Grade	A Grade	B Grade
A$/sqm p.a.	$435	$345	$315	$273	$315	$235
6 month rental change	0.6%	-6.1%	-1.6%	0.9%	-4.5%	-9.6%
12 month rental change	1.5%	-4.2%	0.8%	0.9%	-6.0%	-7.8%

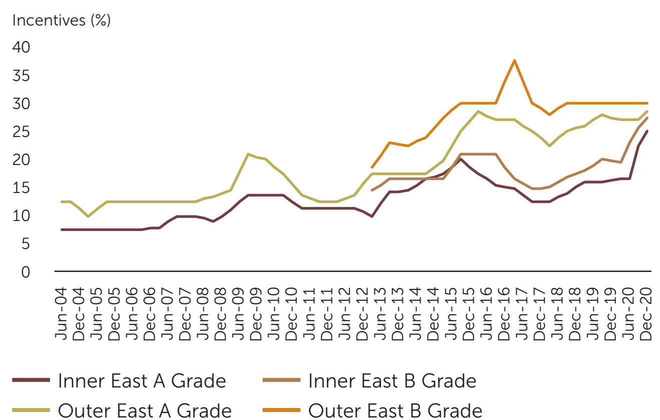
Source: Colliers International

FIGURE 21. MELBOURNE INNER EAST AND OUTER EAST, A & B GRADE NET FACE RENTS, 2004 TO 2020



Source: Colliers Edge

FIGURE 22. MELBOURNE INNER EAST AND OUTER EAST, A & B GRADE INCENTIVES, 2004 TO 2020



Source: Colliers Edge

AUSTRALIA INDEPENDENT MARKET STUDY

MELBOURNE SUBURBAN OFFICE

By Colliers International, February 2021

8.4 Sales and Construction

The Melbourne Metropolitan office market recorded five office sales (above $5 million) in Q3, with a total sales volume of circa $55 million. Year to date, the Melbourne Metropolitan office market has recorded a total of 16 office sales (above $5 million), with a total sales volume of circa $307 million, which is below typical sales volume levels transacted in recent years.

Total sales transactions for 2020 across the Melbourne Metro Market has totalled $801.9 million. Owner occupiers have been particularly active in Q3, purchasing two properties in the City Fringe and Inner East markets. The Royal Australian and New Zealand College of Obstetricians and Gynaecologists (RANZCOG) purchased 1 Bowen Crescent, South Melbourne for $19.6 million. Another owner occupier purchased 1211-1213 Toorak Road, Camberwell for $6.9 million.

Investment sales for Q3 include the off-the-plan sale of 93A Heatherdale Road, Ringwood which was 100% pre-leased to VicRoads for 12 years and sold to an offshore buyer for $9.3 million on a circa 5% yield. 90-94 Camberwell Road, Hawthorn East was 100% leased to Epson for five years and was purchased by a local private investor for $6 million on a 4.65% yield. 71-73 Palmerston Crescent, South Melbourne sold for $12.45 million to Vantage Property Investments.

Sales activity has been subdued particularly in Q3 due to Metropolitan Melbourne being under Stage 4 lockdown since the beginning of July as a result of COVID-19, which has limited the movement of residents throughout Melbourne and has prevented property inspections and auctions taking place.

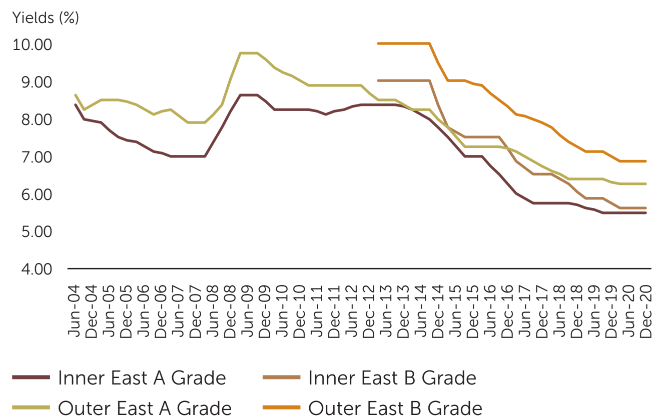
Potential vendors are holding back and waiting for some certainty from the Victorian Government regarding the lifting of restrictions before they commit to placing their properties on the market. Although there is certainly motivation from vendors to sell in the current market, understandably there has been reluctance from vendors to commit to putting their properties on the market when buyers are unable to inspect.

Although sales activity has been down from previous years, the metrics of recent sales demonstrate that the Melbourne Metropolitan market fundamentals are still strong. There is plenty of demand from investors and owner occupiers, however the stock available on-market has been limited. With low interest rates and significant pent up demand, we expect good quality assets will trade at only slightly softer metrics to 2019 once restrictions have been lifted in Metropolitan Melbourne.

8.5 Yields

Yield compression has been recorded across the City Fringe and Inner East precincts over the last 12 months, in line with the majority of office markets nationally. City Fringe average A grade equivalent yields have compressed by 25 basis points from 5.50% to 5.25% over the last 12 months to now range 4.75% to 5.75%. Inner East average A grade yields have also compressed by 25 basis points over the same period to now range 5.00% to 6.00%. Yields across the Outer East precinct have remained steady over the past 12 months remaining between 6.00% to 6.75%.

FIGURE 23. MELBOURNE INNER EAST AND OUTER EAST, A & B GRADE YIELDS, 2004 TO 2020



Source: Colliers Edge

8.6 OUTLOOK

We are forecasting A Grade rents to rise on average across the metro market by 1.2% annually over the next 3 years. While this is significantly below the 3.8% recorded on average over the preceding 3 years, it is still a reasonable outlook given the challenging global and local economic conditions. For the B Grade market, the outlook is one of very limited face rental growth over the next 3 years (0.3%) and continued declines in effective rents, as landlords will have to offer very attractive deals to keep tenants when good A Grade options will be relatively plentiful. We do expect, however, that A Grade incentives will peak higher than B Grade, which is more to do with ownership structures (i.e. institutional owners are more prepared to offer higher incentives) than underlying demand.

The outlook for Melbourne office as a whole continues to be impacted by the outlook for migration. The Federal budget released in early October included a downgrade of the forecast for international migration returning to Australia with negative 71,000 forecast for 2021. However, once this does occur in around 2022/23, Melbourne's relative affordability, economies of scale and strong logistics, manufacturing and health sectors, should ensure that migrants do eventually choose to locate to Melbourne for the reasons that existed prior to COVID-19.

Capital markets activity has been subdued as a result of the uncertainty of both purchasers and vendors. However, low interest rates, continued infrastructure improvements, the upcoming re-opening of Melbourne, as well as some positivity around occupier preferences and requirements in metro markets means that December 2020 yields remain relatively stable. That being said, we are factoring in some softening of yields of around 10 basis points by the end of 2021 to account for weaker income growth going forward, and a higher risk profile of commercial property in general.

UNITED KINGDOM

INDEPENDENT MARKET STUDY

By Knight Frank LLP, January 2021

1. MACRO TRENDS IN THE UK ECONOMY AND REAL ESTATE MARKET

Section 1.1: UK economic performance and outlook

The United Kingdom faces major challenges and uncertainty stemming from the global COVID-19 crisis and exit from the European Union Single Market. UK Real GDP grew 1.5% in 2019 and is forecast to contract -9.5% in 2020, before rebounding in 2021, with forecast growth of 8.3% (Source: Oxford Economics). In Q3 2020, GDP contracted -8.6% year-on-year, this is up from -20.8% in Q2 2020, when the full effects of the coronavirus and associated restrictions were having a dramatic impact on the economy.

Unemployment rates have ticked up in recent months, with many businesses forced to close or significantly reduce their operational capacity due to the coronavirus pandemic and national lockdowns imposed. Jobs in retail and leisure have been particularly affected. However, the unemployment rate remains remarkably low (4.8%) due to the government's Coronavirus Job Retention Scheme (JRS), which has been extended to 31st April 2021 and expected to be extended further, into the summer when the chancellor delivers his budget in March. The UK unemployment rate stood at 5.0% in November 2020, up from a low of 3.8% recorded in November 2019.

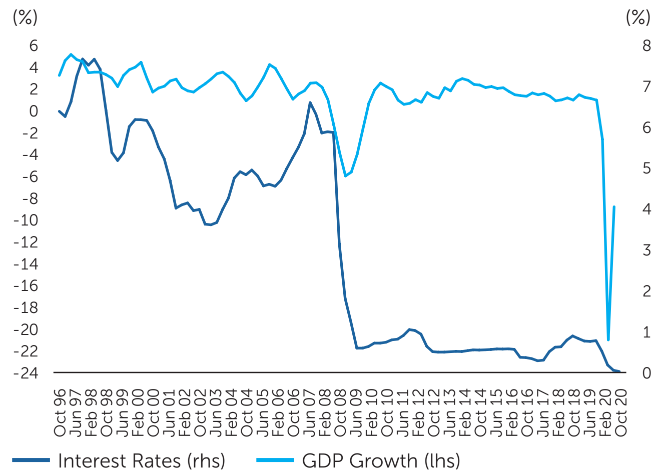
Unemployment is currently low compared with historic figures, though is expected to increase further, peaking in Q1/Q2 2021, coinciding with the end of the JRS, before gradually subsiding thereafter. The retail and hospitality sectors are likely to see the biggest impact, due to business closures directly resulting from the pandemic as well as shifting consumer preferences (which the pandemic has accelerated) which will render some business activities and jobs no longer viable. The UK's changing relationship with the EU may also result in some job losses in the manufacturing sector.

COVID-19 vaccine breakthroughs have dramatically brightened the economic outlook. The vaccines have already started to be administered to the most vulnerable and frontline health workers since December 2020 and will continue to be rolled out across the population in 2021, with the government on target to vaccinate all over 50's by May 2021. The rollout of the vaccine is a real game changer for the labour market and economists are revising their unemployment forecasts down as a result. Capital Economics had revised its unemployment rate estimate downwards from 9%, to peak at 6.5% by the end of the year.

The pandemic has created some pockets of very high inflation. For example, prices of second-hand cars and of computer games and toys have risen sharply due to increased demand. However, falling food and clothing prices have been the largest downward contributors to the rate of inflation and there are currently few signs of a widespread strengthening in price pressures. Inflation has slowed over the past three years, at 0.65% in December 2020 (Source: ONS), the rate of inflation is well below the Bank of England's target of 2.0%. A strengthening global economy along with a recovery in oil prices and quantitative easing, could see inflation pick up in 2021. However, UK inflation is expected to remain below the 2% target in 2021.

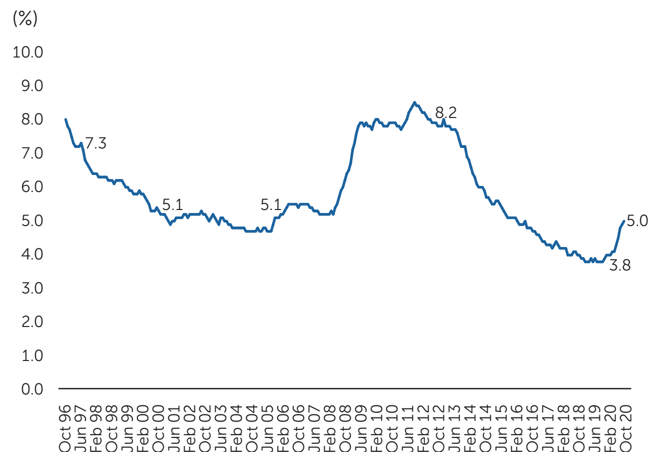
UK interest rates are currently at an all-time low of 0.10%, following two rate cuts from 0.75% in March 2020 to support the economy. Despite the long term aim to raise interest rates, with inflation remaining below the target, it seems likely rates will remain low. Calls for the introduction of negative interest rates have been growing, though if

UK GDP GROWTH AND INTEREST RATES (%)



Source: Office of National Statistics

UK UNEMPLOYMENT RATE (%)



Source: Office of National Statistics

negative rates are introduced, they would be very modest and for a limited amount of time. Though interest rates in the UK are at an all-time low, they are currently above those across most of Europe. The European Central Bank introduced 0.00% interest rates across the Eurozone and Denmark and Switzerland now have negative interest rates. Interest rate hikes are several years away and the combination of a strong economic recovery and ultra-loose policy should buoy UK assets.

Although most households have reported a drop in income since the crisis, the wage support offered through the government's Coronavirus Job Retention Scheme and Self-Employment Income Support Scheme, have helped protect household incomes and expenditure.

Following a slump at the peak of the COVID-19 crisis, when non-essential shops were mandated to close during the national lockdowns, retail sales volumes have started to recover. The combination of economic uncertainty along with pandemic-induced social changes has led to a shift in retail demand, with consumers staying at home more, there has been increased demand for essentials such as food and electronics and less spent on clothing and luxury goods. Recent data showing a rise in retail spend (year-on-year), underlines the importance of the emergency support measures put in place. The volume of retail sales rose in October 2020; up 5.6 % on October last year.

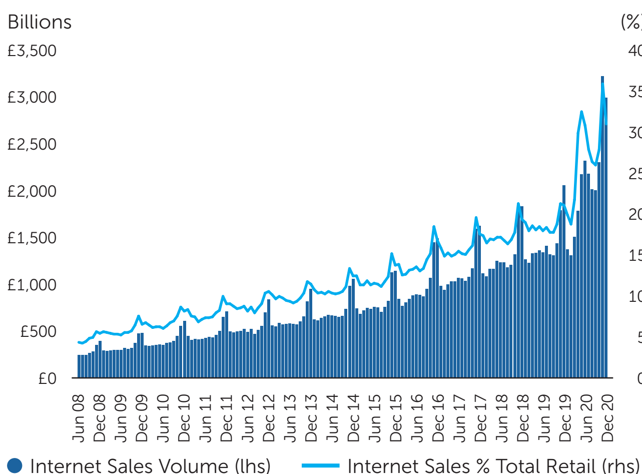
There has also been a marked shift towards online shopping and home delivery. The online segment accounted for 19.2% of UK retail sales in 2019, this rose to 27.9% for 2020, reaching a high of 36% in the month of November (Source: ONS). The online grocery retail market has witnessed significant growth, with penetration rates rising from around 5.3% pre-pandemic to 9.9% in December 2020 (Source: ONS). The growth in e-commerce underpins demand for a large proportion of warehouse and distribution facilities and the robust forecast for retail spending coupled with rising online penetration rates should support continued demand for retail goods and distribution services.

The Office of National Statistics has reported 2020 retail sales on a par with those of 2019, with £436 billion spend in 2020 compared with £438 billion in 2019 (0% change). Oxford Economics are forecasting growth in 2021, with retail sales expected to be around 7% up on the 2020 total. Online retail sales volumes are expected to grow and increase as a percentage of total retail. The COVID-19 pandemic has accelerated the shift towards higher online penetration rates and online sales are expected to account for nearly a third of all total retail sales (excluding fuel) by 2024.

Section 1.2: COVID-19 - Impact on the UK economy and logistics market

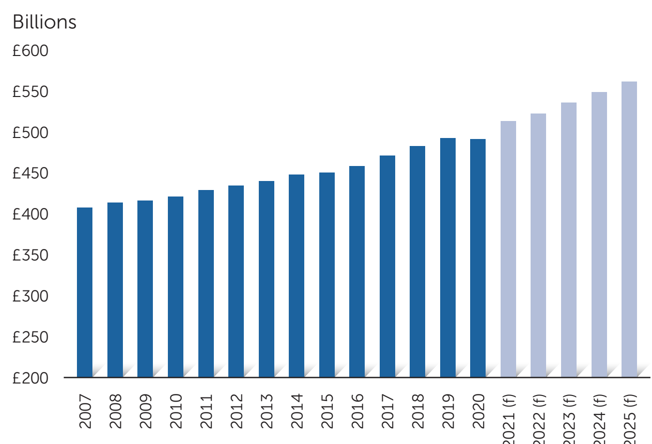
COVID-19 has had a dramatic impact on the UK economy. The initial impact was a supply shock, disruptions to international supply chains led to delayed delivery of raw materials and component parts which resulted in many UK production lines being interrupted. However, as supply-side pressures have eased and production has been able to resume, consumer and industry demand for goods has shifted due to the economic impacts. Consumers have been spending less on travel and non-essential goods and more on household goods and groceries. Aerospace manufacturing has been negatively impacted due to falls in international travel. Automotive and machinery manufacturing has also faced falling demand as consumers and businesses cut back on big-ticket purchases.

UK INTERNET RETAIL SALES (MONTHLY)



Source: Office of National Statistics

RETAIL SALES VOLUMES (£BN)



Source: Office of National Statistics, Oxford Economics

UNITED KINGDOM

INDEPENDENT MARKET STUDY

By Colliers International, February 2021

The pandemic has tested the operational resilience of businesses and supply-side disruptions have highlighted risks associated with just-in-time production practices and with reliance on lengthy, international supply chains. The problem of reliance on the supply of goods made thousands of miles from where they are needed became evident as the UK faced a shortage of ventilators in Spring 2020. As global COVID-19 infection rates spiralled, countries were competing to source and stockpile medical equipment. Many nations, including the UK urgently called upon domestic manufacturers to switch production and to design and produce essential equipment including ventilators and Personal Protective Equipment. This led to calls for re-establishing UK production of critical medical components and essential equipment.

Supply chain disruptions have renewed interest in reshoring or nearshoring; moving production back to or close to the location of the consumer market. Data from the Institute for Supply Management's (ISM) July survey showed that 20% of firms across Europe are planning, or have already begun, to reshore or nearshore some of their operations. However, as cost implications mean that it will not be a suitable strategy for all firms, companies currently operating just-in-time production methods may seek to increase their stock holdings in order to bolster the resilience of their supply chain.

COVID-19 and the associated social and economic impact has driven a shift in consumer demand. For much of the year, many shops and restaurants have been closed or offering collection only. Those who can do so, have been encouraged to work from home, and city centre footfall has dropped dramatically. With people spending more time at home, demand has shifted away from city centre locations into suburban locations; from in-store to online and from restaurants to supermarkets. This meant increased demand for groceries, essential goods and home delivery. Online grocery sales have doubled year-on-year (the value of sales were up 99.2% year-on-year in October 2020, ONS) and retailers have struggled to increase capacity to meet the surge in demand.

Section 1.3: Brexit - Impact on the UK economy and logistics market

The UK left the EU single market and customs union at the end of December 2020. Following intense negotiations between the UK and EU governments, an agreement on future EU-UK relations was reached at the end of December 2020. The agreement provides clarity to UK export businesses and means that goods exchanged between the UK and EU countries are not subject to tariffs or quotas. However, additional costs will still be imposed on bilateral exports through non-tariff barriers (NTBs), such as customs or regulatory bureaucracy. The new border processes and controls in place will have an impact cross-border supply chains.

Air, sea and rail port locations are expected to become more important as logistics locations post-Brexit. Prior to the UK's departure from the single market, most (55%) of the international freight traveling through UK ports was to or from EU ports. Additional border controls imposed from 2021, may interfere with freedom of movement and impact the speed of movement of goods. Additional infrastructure and warehousing may become a necessity at borders such as international ports and airports. UK supply chains are expected to become increasingly domestic in focus, with an increased reliance on UK ports.

The government have announced plans to establish ten free ports, with the first of these to be operational by the end of 2021. Freeport designation will provide tax benefits and offer different customs rules to the rest of the country. These free ports would allow businesses to import foreign goods into special delimited areas of the UK, store them on site or manufacture other goods with them, then re-export them to other countries without paying import tariffs. Free ports could serve as a way to maintain regulatory alignment, and therefore free trade, with the EU, while at the same time establishing trade deals with other countries.

The economic and social impacts of the COVID-19 pandemic have largely overshadowed concerns around Brexit, and the backdrop of weakening global trade and business environment may lessen the impact. Take-up of industrial units over 50,000 sq. ft. in 2020 totalled 51.6 million sq. ft., compared with 34.1 million sq. ft. taken in 2019. Structural trends tied to e-commerce including the growth of online grocery remain the key drivers of demand for industrial space and the COVID-19 pandemic has served to accelerate this shift to online shopping.

2. UK LOGISTICS MARKET

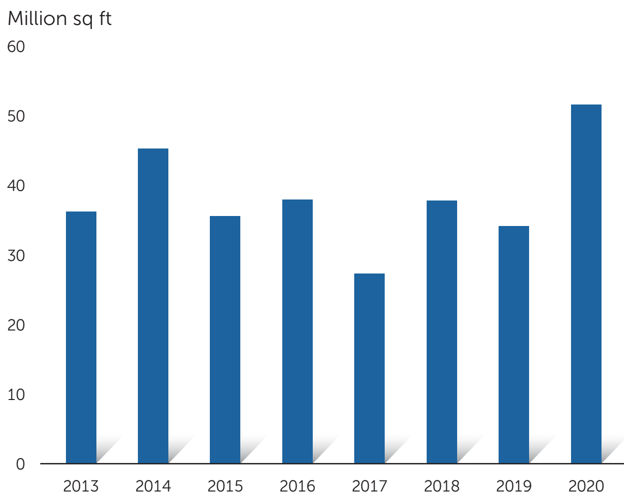
Section 2.1: Occupier Market Overview

Occupier demand for space has been exceptionally strong in 2020, with a record 51.6 million sq. ft. of take-up (units over 50,000 sq. ft.). Demand is currently being driven more by structural forces, rather than the economy, e-commerce has been a key driver for the uptick in leasing activity this year. There have also been examples of occupiers taking space in relation to Brexit planning. Retailers and distributors are also navigating changing trade arrangements with the EU, this is having implications for cross-border supply chains and warehouse location choices. Belgian logistics company Weerts Group, recently took 870,000 sq. ft. at Suffolk Park, Bury St Edmunds. Weerts plan to use

this UK based storage and distribution facility in order to help companies minimise administrative and logistical implications of Brexit. The location was chosen due to its closeness to the Port of Felixstowe; the UK's busiest container port; with connections to continental Europe.

Robust occupier demand is prompting increased interest in development, though construction activity has been hampered this year. Vacancy rates remain low and pre-let activity has increased this year, while units that are ready for immediate occupancy are attracting a premium.

TAKE-UP (50,000 SQ FT +)

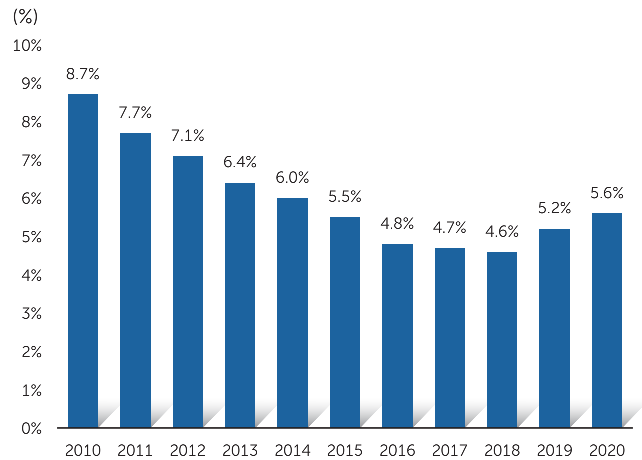


Source: Knight Frank Research

Despite expectations that vacancy rates would rise in 2020, on the back of business casualties and caution in the market, vacancy rates remain relatively low at 5.6%, though this is up from a low of 4.6% recorded at the end of 2018. Over the past ten years, vacancy rates have been falling as older redundant stock is removed from the market. The reduction in floor space has been felt most acutely in London where pressure to redevelop out-dated industrial stock for residential use is strongest.

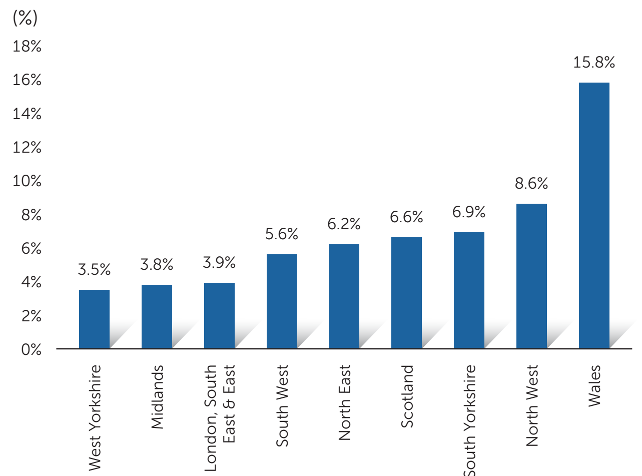
As online retailers and parcel delivery companies seek to expand their operations, there has been a rise in demand for last-mile assets and for large, centrally-located distribution centres. 50% of take-up (units over 50,000 sq. ft.), was in units of 250,000 sq. ft or more, units between 50,000 sq. ft. and 100,000 sq. ft., accounted for just 16% of take-up in 2020 (units over 50,000 sq. ft. only). Vacancy rates are low in the London, South East and East region, currently at just 3.9%, down from 4.5% at the end of 2019. Vacancy rates have also fallen in the Midlands, from 4.6% recorded at the end of 2019, they now stand at just 3.8%. Wales and North West regions have the highest vacancy rates having recorded an uptick in vacancy rates this year. The South West has also recorded an uptick in vacancy rates, due to a rise in development activity in the region.

UK INDUSTRIAL VACANCY RATE (%)



Source: Knight Frank Research

VACANCY RATE BY MARKET (%)

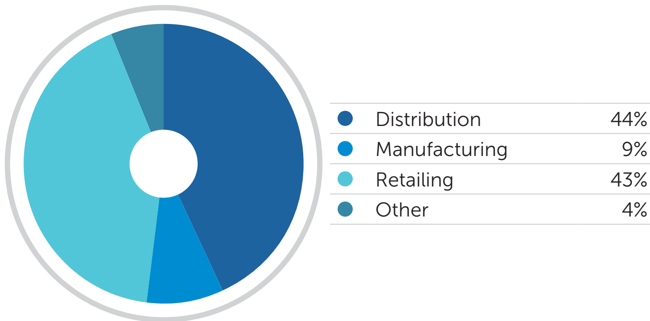


Source: Knight Frank Research

Analysis of the occupiers taking space show retailers and distribution companies have dominated so far this year – together accounting for 87% of total take-up (units over 100,000 sq. ft.). The growth in online retail is driving demand for logistics properties by both retailers and distribution companies as they expand their home delivery capacity. With the exception of Amazon, most retailers outsource distribution and delivery via a distribution company. Distribution companies account for more than a third of take-up (44%), and this increase in demand for space is driven by rising numbers of retail partnerships and rising volumes of retail sales being transported through their networks. This demand for

space has boosted take-up, investment volumes and occupancy rates in the logistics sector. Manufacturing has accounted for just 9% of take-up so far this year (units over 100,000 sq. ft.).

UK TAKE UP BY SECTOR IN 2020 (UNITS OVER 100,000 SQ FT)



Source: Knight Frank, PMA

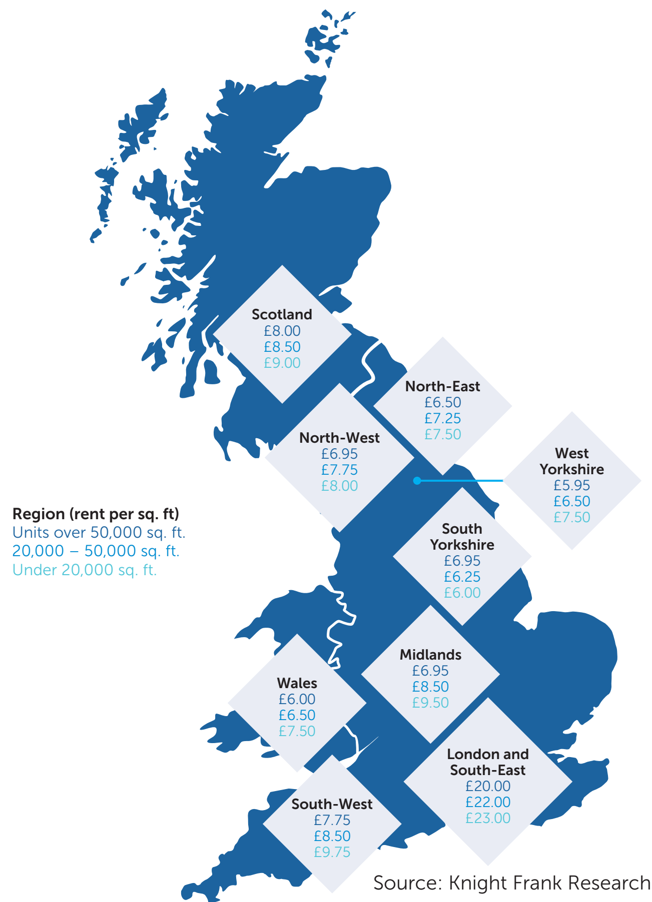
At the end of Q4 2020, there was a total of 8.5 million sq. ft. of speculative space (units over 50,000 sq. ft.) under construction, this is down from 9.2 million sq. ft. of speculative development under construction at end of 2019. London and the South East region has the largest pipeline of speculative development, with 4.3 million sq. ft. of space being built speculatively. The Midlands also has a large development pipeline, with 3.7 million sq. ft. of speculative development. However, these regions also have the highest take-up figures of all regions. Most of the speculative developments in London and the South East is located outside of Greater London, with significant developments around Bedford and Milton Keynes. Speculative developments in the region may help satisfy some of the demand for regional distribution centres and urban logistics, provided schemes are well-located and have the correct specification.

Availability of second-hand space has risen. At the end of Q4 2020, there was 35.1 million sq. ft. of second-hand space available, compared to 30.1 million sq. ft. at the end of 2019 (units over 50,000 sq. ft.). However, much of the space currently available is of lower quality stock, the availability of grade-A second-hand space has reduced. The rapid expansion of the e-commerce market has driven a need for retailers to rapidly expand their capacity in order to capture market share and good quality, well-located second-hand space that is ready for occupancy is proving desirable. 3PL company Clipper Logistics have recently agreed a lease on Sherburn 667; a 666,898 sq. ft. distribution centre in Leeds, West Yorkshire in order to grow their e-commerce operations. Prior to being let, it was the largest available unit in the UK and demonstrates strong demand for Grade-A second-hand space.

Section 2.2: Rents & Incentives

Prime rents have risen across several regions over the past year. Prime rents in London and the South East are the highest, with prime rents for large, 50,000 sq. ft. plus units at £20.00 per sq. ft., up from £16.00 per sq. ft. at the end of 2019. Prime rents for smaller (under 20,000 sq. ft.) units are now reaching £23.00 per sq. ft., up from £17.50 per sq. ft. at the end of 2019. In the South West, prime rents for units over 50,000 sq. ft. are now reaching £7.75 per sq. ft., up from £7.25 per sq. ft. as at end of 2019.

PRIME RENTS BY REGION AND SIZE BAND (Q4 2020)



Source: Knight Frank Research

Average rents have also risen across all regions of the UK in 2020. The largest growth in average rents was recorded in London, the South East and Eastern regions. Average rents rose 2.9% in the South East region and 3.7% in London (year to December 2020). Prime rents have been increasing faster than average or secondary rents over the past year.

Further business insolvencies are expected which will bring second-hand grade-B space back to the market. While quality second-hand units may compete with new speculative schemes, second-hand grade-B stock is less able to compete. This will drive up void rates and occupier incentives and there is likely to be further increase in the spread between prime and secondary rents.

Section 2.3: Investment Market Overview

Investment into UK industrial and logistics totalled £9.3 billion in 2020, this is up from £7.7 billion in 2019. Despite difficulties with international travel and inspections made more difficult due to the COVID-19 pandemic, investors have remained highly active and there has been a rise in the number of big-ticket transactions such as Blackstone's £473 million acquisition of Prologis UK portfolio of 22 warehouse assets, in Q4 2020.

Sale and leaseback transactions have been an important aspect in driving investment volumes since the COVID crisis hit. With cash strapped businesses seeking to liquidate real estate assets in order to help them survive or to finance business expansion or redirection plans. Many investors are reluctant to sell and want to retain their exposure to a market which has consistently outperformed other sectors and the rise in investor – developer partnerships has meant that stock that would have been traded on by developers is no longer being offered up to the market.

Demand for high quality assets with long-income has compressed yields at this end of the market. For example, the Marlin Portfolio acquired by Canmoor / AIMCo recently for £260 million, representing an initial yield of 4.0% and the sale of the Metro Portfolio to InfraRed Capital Partners for £50.75 million (4.75% initial yield).

Yields on secondary distribution assets have softened over the past two years, widening the gap between prime and secondary assets, to around 2.0% in December 2020. Falling UK government bond yields have boosted the premium offered by industrial property. The robust returns seen in the industrial and logistics sector have been attracting real estate investment. The demand for high-quality, well-located warehousing as well as a growing need for build-to-suit property means that in the UK yields and demand are likely to remain stable for the foreseeable future.

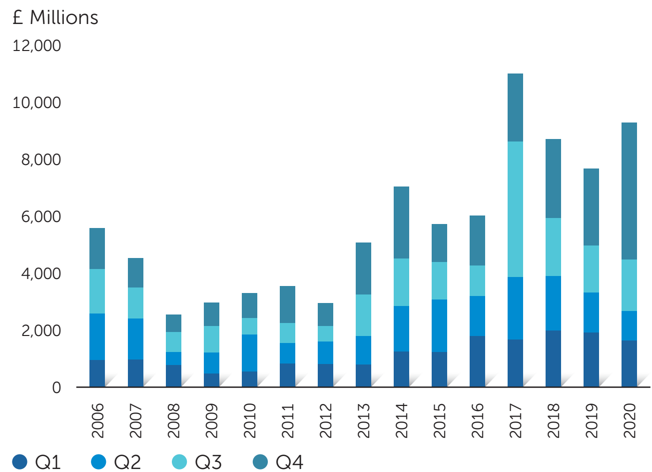
MSCI report annual total returns of 8.7% in December 2020 for UK Industrial property. Capital growth has accelerated in the second half of 2020, boosting returns and returns for industrial property continue to outpace other sectors. Total returns for industrial and logistics are forecast to remain strong over the next four years.

Section 2.4: Market Trends

Rising e-commerce demand due to the COVID-19 pandemic has had a significant impact on the UK's industrial and logistics market in 2020. There has been a significant shift in retail demand and a step change in the way people shop. In December 2020, online retail sales volumes were up 46% on last year and accounted for 31.3% of all retail sales (excluding fuel). Shop closures and in-store restrictions have driven shoppers online, even those who were previously reluctant. A consumer attitudes survey by RetailX revealed that 24% of new online shoppers said that they will continue to shop online even after the COVID-19 pandemic is over. Though online retail penetration rates are likely to dip as stores reopen and restrictions are removed, COVID-19 has served to accelerate the rate of online adoption and online retail penetration rates.

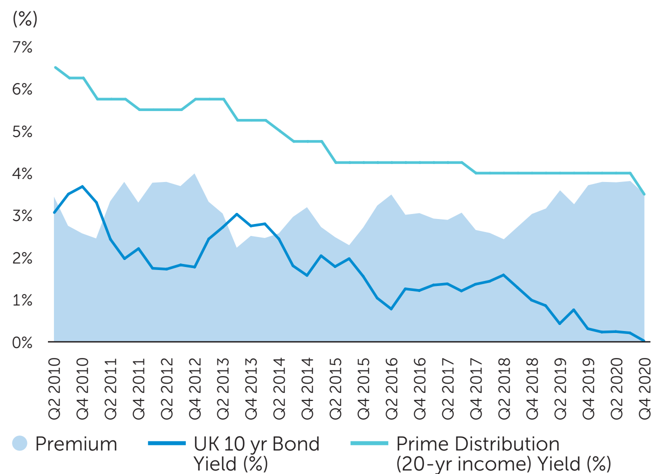
In the grocery market segment, online sales have more than doubled year-on-year, in December 2020 online food retail accounted for 11% of sales, volumes were up 126% on December 2019. Many shoppers who previously did not shop online, or did not do their grocery shopping online, are expected to continue using it in the future. Longer term, additional warehouse capacity will be

INDUSTRIAL & LOGISTICS - INVESTMENT TOTAL (£ MILLIONS)



Source: Knight Frank Research, Property Data

PRIME LOGISTICS YIELD PREMIUM OVER THE 10 YR BOND RATE (%)



Source: Knight Frank Research, Macrobond

needed to accommodate lasting structural changes and address the quantum leap in online grocery demand.

Many traditional retailers are adapting their retail models and their warehousing needs are changing as more space is allocated to e-commerce activities. Retailers are adapting their distribution centres, to accommodate B2C customer deliveries, alongside store deliveries. To service this growth, demand for largescale fulfilment and 'near-urban' warehousing will continue. Recent analysis by Knight Frank Research shows the growth of e-commerce could drive demand for 92 million sq. ft. of warehouse space across the UK by 2024. By examining five-year data for online sales, take-up of warehouse space and retailers' warehousing networks, Knight Frank forecasts that for every additional billion pounds of online retail sales, 1.36 million sq. ft. of warehouse space is required.

The rapid growth in the e-commerce and particularly in the grocery delivery market is stimulating a rise in automation and an increasing need for specialist distribution centres that can quickly process large numbers of small orders. Customised automation solutions can be expensive to install and can make relocating prohibitively expensive. This has led to longer leases and higher income security for landlords. Though average lease lengths have decreased slightly this year, this is likely due to the rise in short term requirements associated with the COVID-19 pandemic, rather than being part of a longer term structural trend.

Job losses in the retail sector are likely to lead to increased capacity in the jobs market and unemployment is forecast to rise in 2021. However, Oxford Economics forecast that unemployment will peak in Q2 2021 and fall throughout the second half of the year and will be back below 5% by the end of 2022. Therefore, longer term, accessing labour pools will remain highly important for logistics operators, particularly in terms of the location and accessibility of a warehouse.

In addition to very large distribution centres and warehouses, rising demands from e-commerce are also driving demand for warehouses located within close proximity to consumer populations and urban centres. These urban logistics centres enable retailers and parcel carriers to offer their customers rapid delivery options. Small-scale logistics sites within close proximity to consumers are highly desirable, as part of the "last-mile" element of the delivery chain. Capital values for industrial are rising and increasingly competing with edge-of-town retail warehouse values and in some specific locations, particularly around London, this is driving retail to logistics conversions. Recent examples include Toys R Us in Croydon, South London and Ravenside Retail Park in Edmonton, North London.

Section 2.5: Outlook

Economic impacts stemming from the pandemic slowed the rate of rental growth in 2020, particularly in Q2 2020. However, rental growth accelerated in the second half of the year. Despite the economic challenges the UK faces in 2021, the underlying structural shifts in ecommerce are continuing to drive demand for industrial and logistics properties and competition for well-located assets is expected to drive positive, albeit modest rental growth in 2021. However, as the economy recovers and grows over the next four years, rental growth is forecast to accelerate. The outlook for rental growth varies across the UK regions, with London, the South East and Eastern region forecast to lead. Average rental growth in Scotland, the North East and Yorkshire is expected to lag the rest of the UK over the next four years.

Even prior to the COVID-19 pandemic, the structural change towards online spending was already benefiting the industrial sector. With an increasing proportion of retail spend taking place online rather than in-store, retailers have a need to shift their operations from the store to the warehouse to service the rising demand for home deliveries. Some retailers have not adapted quickly enough and this has resulted in insolvencies. With COVID-19 accelerating the pace of change, further retailer insolvencies are likely and this will continue to bring some warehouse space back to the market. Challenges in the manufacturing sector and supply chain restructures are also bringing some second-hand industrial units to the market. As a result, vacancy rates are expected to rise across several regional markets.

The industrial and logistics sector remains an attractive investment compared to other sectors, with total returns expected to outpace those of other sectors over the next four years. However, the prospects for further yield compression remain modest, yields for prime warehouse and logistics properties are expected to remain flat over the next few years. UK gilt yields (10-year government bonds), on the other hand, are forecast to remain very low in 2021 before slowing rising from 2022 (Source: Oxford Economics). The current spread (331 basis points in Q4 2020) between prime logistics yields and bond yields is likely to narrow over the next few years as bond yields slowly rise. Despite a narrowing risk-premium, the appeal of logistics property will continue to be driven by strong sector fundamentals.

UNITED STATES

INDEPENDENT MARKET STUDY

By JLL

U.S. ECONOMY OVERVIEW

After entering 2020 on the tails of a decade-long expansion, the onset of COVID-19 in the United States in March led to an unprecedented macroeconomic contraction, with a disparate recovery underway with wide variation in terms of geography and industry. Heading into 2021, the containment of the second wave of COVID-19 and ability to vaccinate at scale will be critical in determining the rate of rebound, while a change in government administration is expected to result in greater additional stimulus, currently estimated at $1.9 trillion. This is likely to be supplemented by an increased focus on infrastructure investment slated to benefit connectivity and greater levels of development.

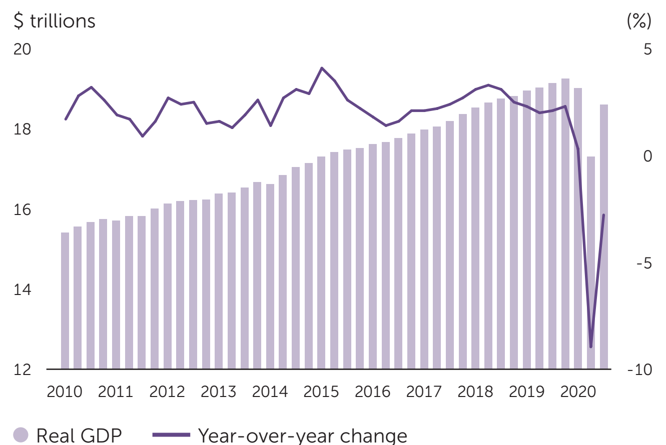
The effects of COVID-19 have been profound: from February through April, the U.S. labor market contracted by 22.2 million jobs, equivalent to 14.5% of pre-pandemic employment, and employment remains 6.3% below February levels. Office-using employment, however, has been more resilient, and currently rests at just 3.8% below pre-pandemic levels. Buoyed by a recovered in consumer spending, GDP at year-end 2020 is now at 97.5% of its Q4 2019 estimate, when it had previously peaked.

In an effort to combat the economic fallout from the pandemic, Congress passed an unprecedented stimulus in the form of the CARES Act. This included a package valued at roughly $2.2 trillion comprising direct payments, the Paycheck Protection Program, industry-specific bailouts and state and local government funding along with enhanced unemployment benefits to supplement state payments. After expiration in December and a political stalemate, a second stimulus of $900 billion with smaller and more targeted aid as well as an extension of business and unemployment programs passed as part of the more comprehensive Consolidated Appropriations Act for 2021. In line with the flipping of the Senate and the executive branch, a third round of stimulus, known as the American Rescue Plan and valued at $1.9 trillion, is currently going through the reconciliation process in Congress.

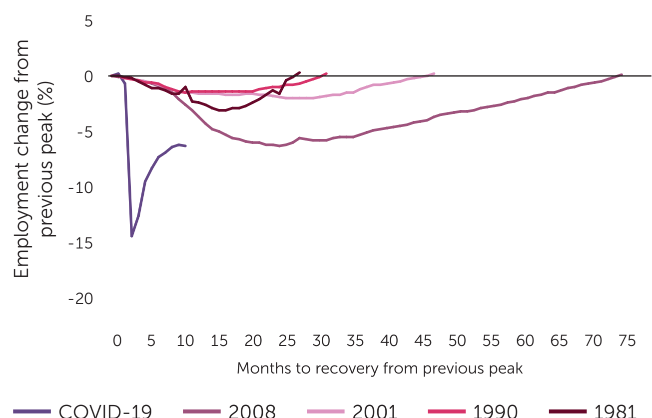
Importantly for the office market, the COVID-19 pandemic is a service- rather than office-driven downturn: office-using employment has held up remarkably well, with the few segments of the sector still suppressed being limited to on-site building and clerical services that cannot be performed remotely. There has been a slight uptick in permanent layoffs for professional services due to the prolonged macroeconomic slowdown, but this is low in comparison to the drop-off in leisure and hospitality employment and activity.

Moving forward, the economic recovery will likely take hold beginning in the latter portion of the second and into the third quarter of 2021, once vaccines are widely available outside of front-line workers and those over the age of 65, enabling an opening up of many businesses with less risk of straining health care capacity. In the interim, unemployment may see a short-term increase – already borne out in initial claims – given seasonality and the current surge in cases leading to a reduction in overall activity. Further government relief will stabilize economic conditions and improve cash-on-hand for consumers to maintain spending, while longer-term infrastructure and health investments will boost GDP in the coming years.

REAL GDP APPROACHING PRE-COVID LEVELS, DOWN 2.8% Y-O-Y



JOBS RECOVERY IS TRENDING TOWARDS A "W" RATHER THAN A "V"



UNITED STATES

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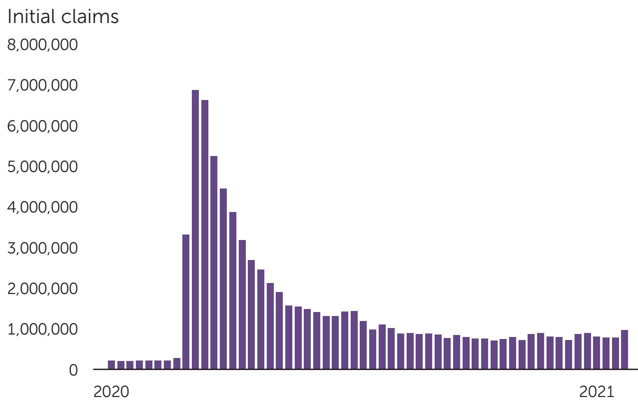
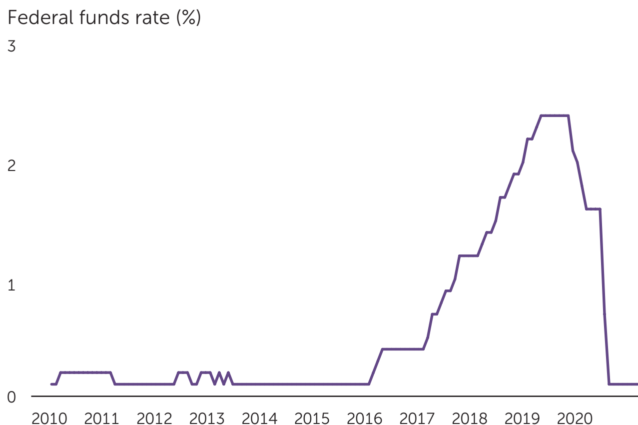
WEEKLY UNEMPLOYMENT CLAIMS DOWN SIGNIFICANTLY FROM PEAK



NEAR-ZERO INTEREST RATE POLICY LIKELY TO CONTINUE



U.S. OFFICE OVERVIEW

Widespread uncertainty over both economic and health conditions impaired office market fundamentals in 2020 and led to an unprecedented disruption in key indicators such as leasing velocity, net absorption, sublease inventory, sales volume and pricing. Tenants delayed making long-term leasing decisions given heightened risks, unknown timelines for office re-openings and expanded remote work programs.

Entering 2021, tenants and owners alike continue to navigate rapidly changing conditions and a continued pause in activity across markets, industries and asset classes. The fourth quarter marked the third consecutive quarter of limited leasing since the onset of COVID-19, with widespread space give-backs, accelerating occupancy loss and rising vacancy, but newfound optimism as vaccine rollouts gain momentum.

Gross leasing in Q4 was once again heavily subdued compared to historic norms, reaching just 25.2 million square feet, bringing 2020 volumes to 125.6 million square feet. Compared to 2019, this represents a 47.3% drop-off over the year in transaction activity as long-term planning remains difficult apart from select highly capitalized users. Pulling down activity in Q4 was a lack of large-scale renewals that helped to buoy Q3 figures, particularly from financial firms, along with greater hesitation from much of the tech sector, which has been a core driver of net expansion over the past decade. Notable, however, has been the relative resilience of mega-cap tech users in both gateway and secondary markets as they build out national hub-and-spoke office models as well as life sciences. The latter has become popular with office investors, who have begun to acquire assets for conversion or full-scale development to lab space, most prominently in Boston's Seaport District at 2 Harbor Street and the Innovation and Design Building.

Tenants continue to opt for shorter leases to delay decision-making as an interim step: 68.7% of quarterly transactions were renewals, of which 43% were five years or less in duration. As a result, the average deal term dropped even further in Q4 to 6.7 years for leases larger than 20,000 square feet, well below the pre-COVID average of 8.5 years. Lease lengths will likely increase as the market begins to recover later in 2021 and into 2022 as re-entry enables occupiers to determine their space configurations and needs so that they can make longer-term commitments. Greater flexibility will become a core component of leases moving forward and will result in 10+ year terms being a smaller share of broader activity.

Mirroring broader macroeconomic and demographic trends, gateway markets saw a 51.5% reduction in year-over-year leasing compared to 42.9% elsewhere on account of higher exposure to remote-work-friendly industries such as tech, demographic shifts and more restrictive virus containment measures. Activity should pick up in mid-2021 as vaccination becomes more widespread and stay-at-home restrictions are progressively eased.

The U.S. office market recorded its largest quarterly occupancy drop on record in Q4, with 40.6 million square feet of negative net absorption, bringing total 2020 occupancy losses to 84 million square feet. This compares to 55 million square feet of occupancy losses experienced during the entirety of the 2008-09 Global Financial Crisis.

Underlining the structural challenges for denser gateway geographies, 52.1% of negative net absorption

occurred in CBDs despite them comprising 38.5% of national inventory. This has helped suburban markets, where occupancy declines are taking place 27% slower than in their urban counterparts and sublease expansion has been less acute. Rent volatility is also less severe in suburban submarkets, whereas concession packages have spiked by more than 48.1% over the course of the COVID-19 pandemic in urban office properties.

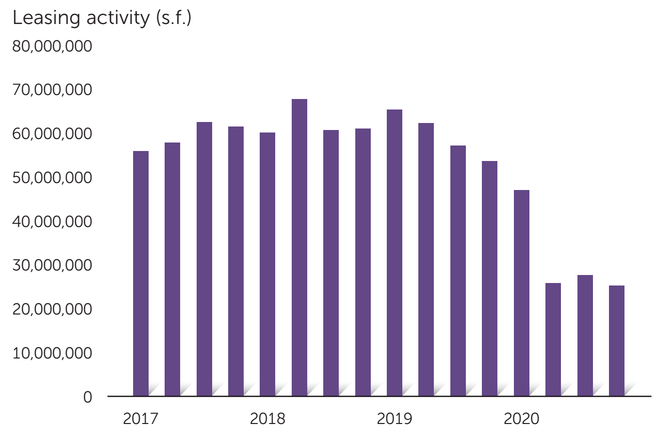
As with leasing, occupancy losses have been most pronounced in gateway geographies. More than one-third of 2020's give-backs took place in New York and the Bay Area alone, approaching 30 million square feet in the process, at a rate 2.2x faster than the national office market as a whole. This contrasts with secondary and tertiary markets, which were more resilient, benefiting from more diversified tenant bases and expectations for inbound migration: metro areas with less than 60 million square feet of total inventory recorded net absorption of -1.3% of inventory, 60 basis points lower than the national average. Major inbound destinations for corporate and individual migration such as Austin, Charlotte, Miami, Nashville, Phoenix, Raleigh and Salt Lake City all recorded negative net absorption of less than -1.5% of inventory, underlining shallower office market downturns.

This mix of give-backs (both planned pre-pandemic and in response to changing needs in the past nine months) and new supply hitting the market pushed vacancy up 110 basis points to 17.1%, rising twice as fast in CBDs than in the suburbs. Unlike net absorption, however, vacancy rose faster for Class A product on account of completions, which will reverse as tenants relocate to higher-quality buildings. Supply delivered since 2010, for instance, has a vacancy rate of 14.6% compared to 17.1% across all age brackets, and this trend will apply to both recent and upcoming deliveries.

Liquidity once again improved in Q4, bringing sales volumes up by a further $24.8 billion to $78.6 billion at year-end. At 42.4%, annual sales volumes for office trailed industrial and multi-family significantly, but remained above retail and hotels. As with leasing, secondary markets have seen a softer shift in dynamics with less volatility: secondary market cap rates have increased by 12 basis points since the onset of COVID-19 compared to 21-basis-point growth in gateway geographies. This has translated to the suburbs – where leasing and investment fundamentals have been more consistent.

Office closures, work-from-home initiatives and financial pressures led many tenants to place space on the sublease market. In Q4, an additional 18.4 million square feet of sublease space hit the market, bringing the segment to more than 141.5 million square feet.

LEASING HAS DECLINED RELATIVE TO PRE-COVID LEVELS



SHORT-TERM EXTENSIONS ARE PULLING DOWN TERM LENGTHS

Over the course of the pandemic, sublease inventory has expanded by nearly 47.6 million square feet, or 50.7%.

Shadow space – sublease product that is available but not yet vacant – now stands at 48.8 million square feet, which will keep total vacancy on an upward trend through much of 2021 as current users eventually vacate these blocks. Sublease has been a disproportionate contributor to rising vacancy: despite representing 13% of current vacancy, it has been responsible for 29% of space added onto the market since the onset of the pandemic. As a result, sublease as a share of total vacancy is up 38% and set to rise further as much of the current shadow space is realized as vacant in the coming quarters. This is occurring more acutely in Class A product, where sublease vacancy is 2.5% of inventory compared to 1.6% for Class B, although the former is concentrated in second-generation rather than newer Class A space.

UNITED STATES

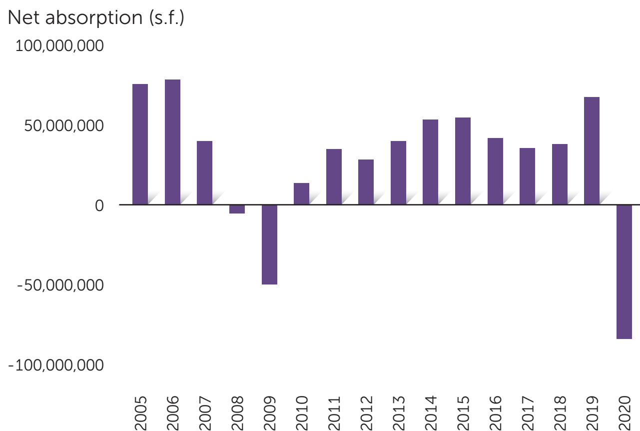
INDEPENDENT MARKET STUDY

By JLL

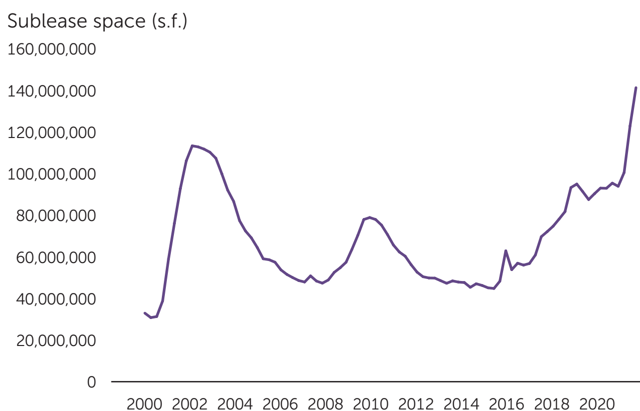
Annual completions fell in 2020 compared to 2019 by 16.8%, largely a result of COVID-19 induced construction delays, leading to the broader construction pipeline remaining relatively static at 123.9 million square feet. Oversupply remains a significant risk through 2022, however, despite a longer timeframe for delivery of projects currently underway through 2025.

Few large-scale projects delivered in Q4, with only three (167 N Green in Chicago, the TSA HQ in Northern Virginia and 45 L in Washington, DC) larger than 500,000 square feet being occupied during the final three months of the year. Groundbreakings were even more restricted; apart from Visa's new headquarters beginning construction in San Francisco, all starts were less than 250,000 square feet, almost all of which were majority or fully pre-leased at the time of groundbreaking. Preparatory works for the expansion of 1 Madison in New York also started, underlining the positive longer-term sentiment for top-tier space in gateway hubs.

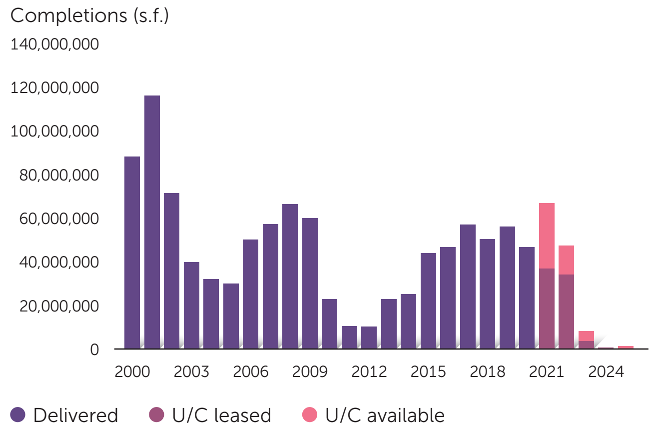
NET ABSORPTION HIT A RECORD LOW OF -84 M.S.F. IN 2020



SUBLEASE SPACE HAS FAR SURPASSED DOT-COM BUBBLE LEVELS



2021 WILL SEE A JUMP IN COMPLETIONS, ADDING TO VACANCY



INNOVATION CLUSTERS

For decades, economists have noted outsized economic returns from innovation clusters and density of skilled workers, and these clusters have translated over the past decade to similarly disproportionate growth in the office market, from higher demand to rent premiums, lower vacancy rates and most robust construction pipelines. In the aftermath of the COVID-19 pandemic, a focus on these geographies will be even more critical for investors seeking greater returns in both urban and suburban locations.

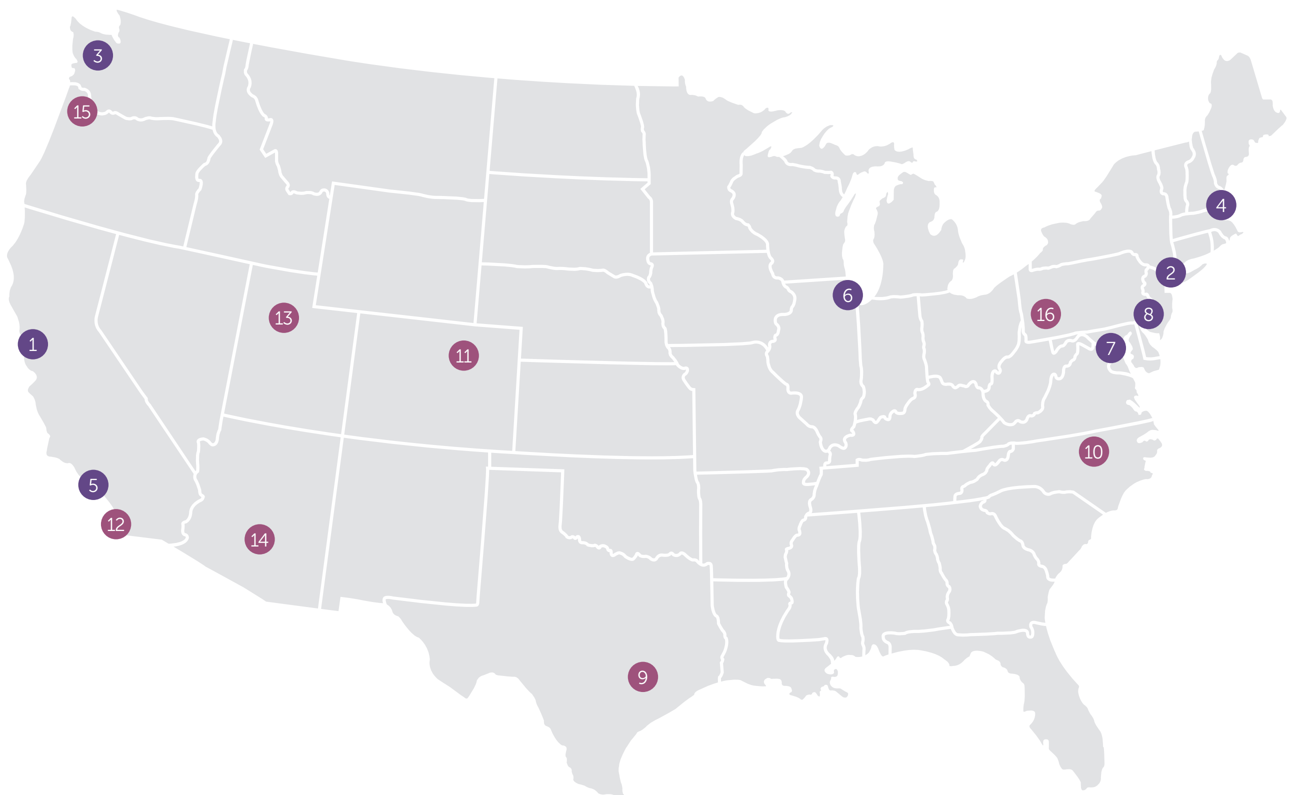
To date, the most famous example of such clustering is Silicon Valley, maintaining its position as the world's leader in technological innovation, venture capital and tech-related real estate investment even with fierce competition from rapidly growing hubs domestically and internationally. Despite representing only 1.5% of national office inventory, it has been the location of 8.8% of net occupancy gains across the country since 2010.

This level of success has made finding the "next" Silicon Valley one of the defining features of office investment strategies. The ever-accelerating shift to digital services and growth, high costs of living in the Bay Area, labor market saturation and the need to find talent are leading to many innovation clusters sprouting in primary, secondary and even tertiary metro areas with increasing levels of specialization.

Outside of the Bay Area, New York's Midtown South sub-region is America's largest concentration of tech, creative and media innovators and insatiable demand for a limited supply of office product pushed rents up by 52.3% throughout the current cycle. Similarly, spillover from San Francisco and a number of globally

recognized tech anchors catalyzed the development of Seattle's South Lake Union to the north of the CBD, which has grown by 160.5% in the past decade. Boston's East Cambridge is a global hub for life sciences, and sub-5% vacancy for a number of years and rents exceeding $85 per square foot have catalyzed users to look throughout the market for space. Even in slower-growth metros such as Chicago, Fulton Market has become a rapidly developing submarket for office, residential and hotel uses alike. The University of Pennsylvania is an anchor for Philadelphia's biotech start-up environment in University City as well.

In secondary markets, the suburbs are home to many of these locations. Austin's Domain is equidistant from the urban core and the traditional tech hubs in the northwestern suburbs, and its walkable retail area has spurred development for companies such as Facebook. In Raleigh, the Research Triangle Park continues to land top-tier life sciences users and is now undergoing repositioning to maintain them in light of shifting tenant preferences. Absorption and rent growth over the past decade have also been propelled in San Diego's inner northern suburbs, Boulder in Denver and Utah County south of Salt Lake City, among others.



1. Silicon Valley
2. Midtown South (New York)
3. South Lake Union (Seattle)
4. East Cambridge (Boston)
5. Westside (Los Angeles)
6. Fulton Market (Chicago)
7. I-270 Corridor (DC)
8. University City (Philadelphia)
9. Domain (Austin)
10. RTP (Raleigh)
11. Boulder (Denver)
12. UTC/Sorrento Mesa (San Diego)
13. Utah County (Salt Lake City)
14. Tempe (Phoenix)
15. Close-in Eastside (Portland)
16. East End (Pittsburgh)

Note: dark purple clusters are established innovation hubs; light red represent emerging nodes.

UNITED STATES

INDEPENDENT MARKET STUDY

By JLL

PORTLAND

Market overview

Less exposed to the tech and creative industries active in the urban core, Portland's suburbs have seen mixed and often bifurcated performance throughout the current cycle. Amenitized, well-located and transit-accessible properties as well as traditional professional services hubs continue to benefit from the metro area's population and employment growth, while others have flatlined.

In combination with a number of planned relocations to new, build-to-suit campuses, vacancy increased across the suburbs to 15.3% (+210 basis points), the result of 1.1 million square feet of occupancy losses in 2020. The majority of this came from Nike vacating 280,000 square feet at the Tektronix campus as part of its movement to and consolidation into its build-to-suit headquarters campus.

In part due to an incredibly strong 2019, when sales surpassed $1 billion for the first time on record, suburban office property trades were much quieter in 2020, totaling $299 million. Pacific Coast's acquisition of the Amberglen Business Center in Hillsboro was responsible for $69.7 million of this total (priced at $166 per square foot), with additional trades of note including the Vancouver Innovation Center and One Embassy Center.

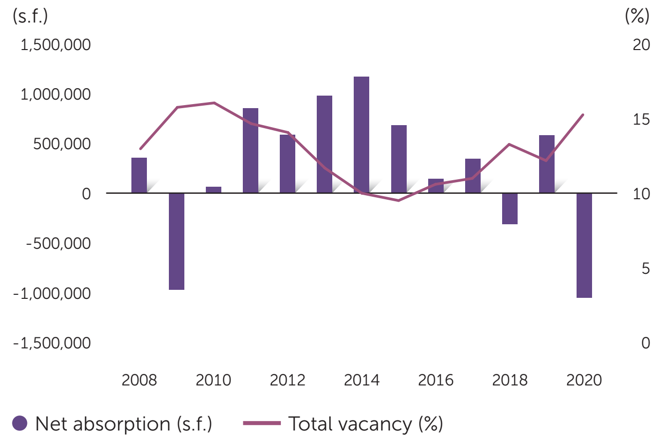
Submarket commentary

Planned and COVID-induced give-backs of Class B and C space hampered fundamentals in both the Sunset Corridor and 217 Corridor/Beaverton submarkets, but both remain among the most liquid in the metro area with positive longer-term growth prospects. Class A vacancy in both submarkets falls below the Westside average and they maintain a meaningful rent discount to more expensive nearby locations such as Kruse Way at $26.06 and $28.62 per square foot, respectively, a roughly 19% discount. This will enable greater tenant attraction and retention as occupiers seek to gain real estate cost efficiences.

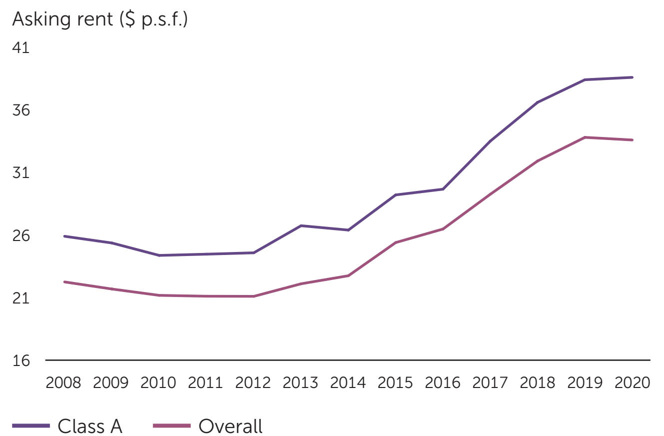
In 2020, leasing largely came in the form of renewals such as Nike at both the Evergreen Corporate Center and Beaverton Creek. At the same time, Microsoft entered the market with an 85,000-square-foot transaction at Ambercreek in Hillsboro, further confirming the Sunset Corridor's importance as a suburban tech cluster for the region. Outside of these leases, most transactions fell below the 20,000-square-foot threshold and larger users with impending expirations took a wait-and-see approach.

Moving forward, moderately elevated vacancy is likely to be temporary as the construction pipeline in both submarkets is thin. The two properties underway – the renovation of Ambercreek and the City of Beaverton's Public Safety Center – are both pre-leased and represent just 107,253 square feet of space. Commodity space will remain challenged, however, given the need for top-tier ventilation systems and wellbeing amenities.

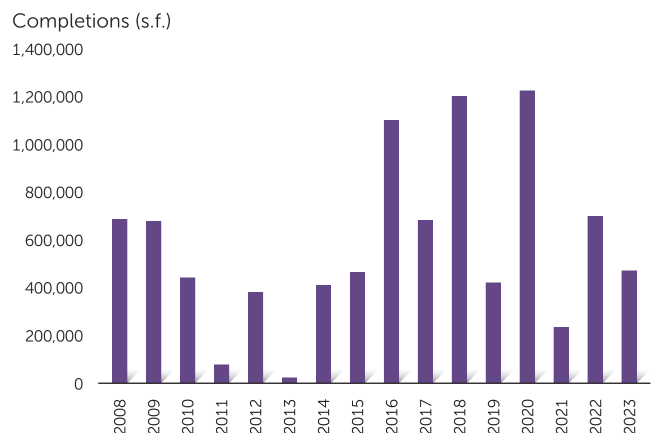
VACANCY ROSE PAST 15% AFTER 1.1 M.S.F. OF OCCUPANCY LOSS



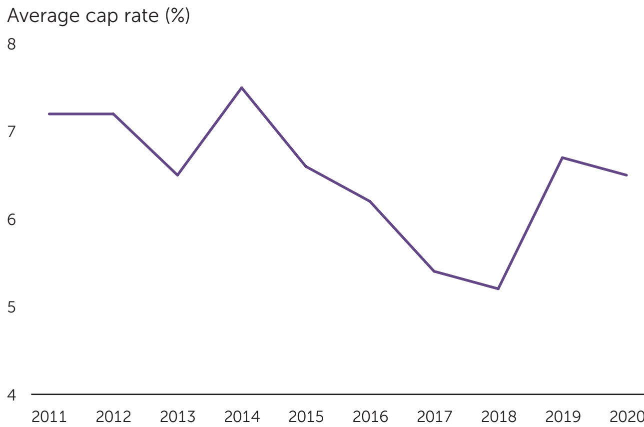
CLASS A RENTS HOLDING FIRM; OVERALL DECREASING SLIGHTLY



PORTLAND'S SUBURBS HAVE SEEN ACTIVE BTS DEVELOPMENT



CAP RATES HAVE SEEN INCREMENTAL DECREASES IN 2020



Outlook

Portland's suburban market will continue to stand out in contrast to the more development-heavy but volatile urban core. Portland is anchored by larger corporate users and aided by a build-to-suit-heavy pipeline that will limit the potential for additional oversupply and enable a faster vacancy correction. Portland's suburbs stand to benefit from record amounts of dry powder from institutional investors and REITs seeking yield and a more attractive cost basis.

RALEIGH-DURHAM

Market overview

The 2010s saw Raleigh-Durham emerge as the second fastest-growing metropolitan area of more than one million people nationally after Austin, recording a 23% increase in its population between 2010 and 2019. This intense level of growth strained both the urban and suburban segments of the market, resulting in constraints that pushed vacancy into almost single-digit territory (10.2% in Q1 2020) and a surge in asking rents of 37.4%.

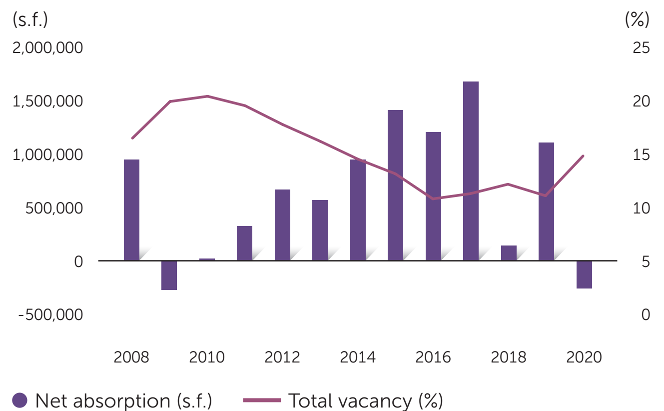
Such sustained increases in employment – notably in the life sciences, tech and pharmaceutical manufacturing industries – were in large part responsible for only 259,455 square feet of negative net absorption in 2020. As a share of inventory, this represents a decrease of only 0.6% over the year, while suburbs nationally experienced occupancy losses occurring 2.5x more quickly. Suburban vacancy of 14.6% is on par with peer markets such as Charlotte (14%) and below Nashville (15.7%) and Atlanta (20.2%).

From a sales perspective, Raleigh-Durham is beginning to emerge as a target for institutional investment from owners looking at geographical diversification, search for yield and to get a foothold in the region's burgeoning biotech cluster. This resulted in Raleigh-Durham being one of the few geographies with a marked increase in sales volume in 2020: the $1.7 billion in suburban sales this year was the second-highest on record after the $1.8 billion seen in 2018, driven by Alexandria's acquisition of the five-building, 2.1-million-square-foot Karlin portfolio in the Research Triangle Park for $574 million.

Submarket commentary

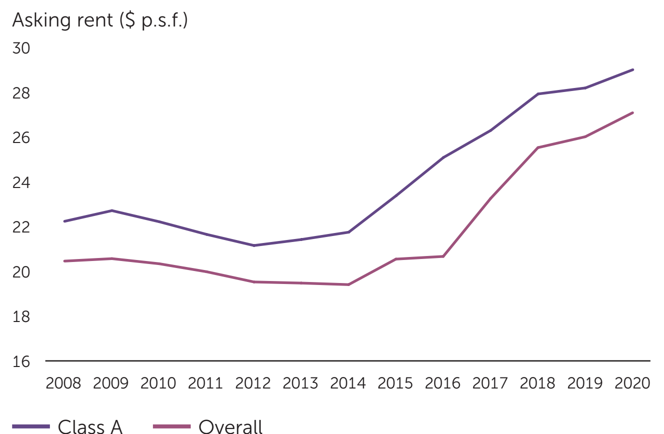
The Research Triangle Park is the nexus of Raleigh-Durham's life sciences industry, being the original home to the industry upon its creation in 1959 and benefitting from being equidistant between the Raleigh and Durham CBDs as well as proximity to Duke, UNC Chapel Hill and NC State Universities. It is one of the largest purpose-built research parks nationally and has been responsible for the region's disproportionate influence in biomedical innovation.

ABSORPTION TURNED NEGATIVE AFTER A DECADE FOR EXPANSION



Note: statistics only cover suburban submarkets.

NEW SUPPLY PUSHING ASKING RENTS UP DESPITE SOFTENING



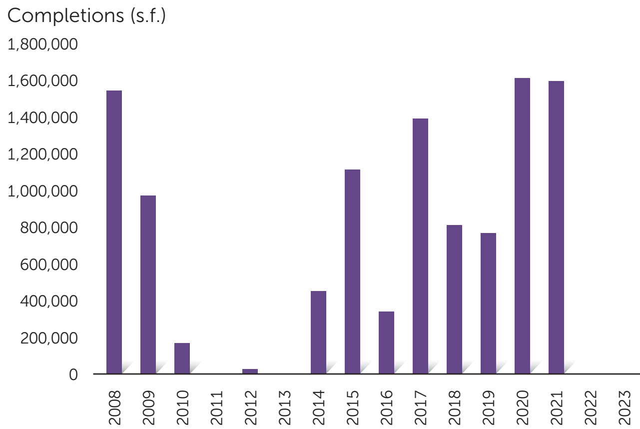
Note: statistics only cover suburban submarkets.

UNITED STATES

INDEPENDENT MARKET STUDY

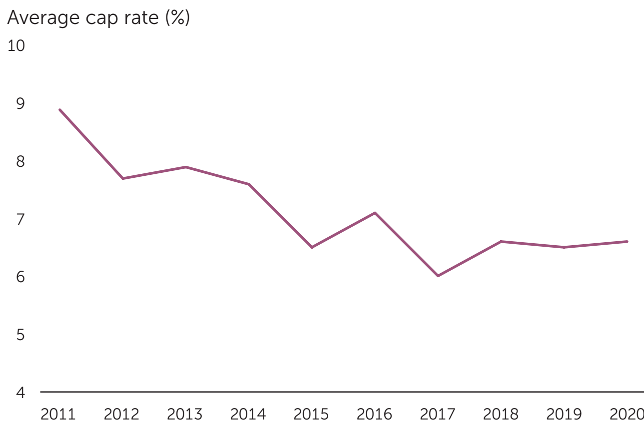
By JLL

25.2% OF SUBURBAN SUPPLY WAS BUILT IN 2010 OR LATER



Note: statistics only cover suburban submarkets.

CAP RATES ARE HOVERING IN THE 6.5% – 6.6% RANGE



Note: statistics only cover suburban submarkets.

In recent years, the submarket's aging inventory, car dependence and limited amenitization, however, have led to more polycentric growth and the expansion of the Downtown Raleigh, Cary and Six Forks submarkets, resulting in marginally greater tenant friendliness and higher vacancy of 16.6% than the region as a whole. Even so, Q2's 322,384-square-foot expansion in the submarket at Parmer Ellis was one of the largest leases across the metro area in 2020 along with deals larger than 100,000 square feet from both Grail and Biogen.

Outlook

Raleigh-Durham will be one of the first office markets to recover as a result of beneficial demographic and macroeconomic fundamentals. Investors and developers will find a more favorable operating environment with greater room for rent and capital value appreciation along with sustained inbound movement from higher-cost geographies and an array of site selection opportunities.

SAN DIEGO

Market overview

Although high costs of living and doing business have placed pressure on San Diego's office environment and regional economy as a whole in light of the shift to remote work throughout 2020 and into 2021, the market proved to be more resilient than many others in California, most notably the Bay Area and Los Angeles.

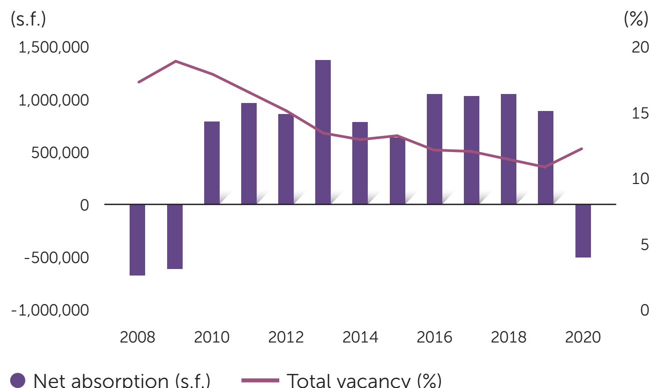
San Diego's suburban-heavy office market and strengths in life sciences, tech and advanced engineering and manufacturing helped to soften the effects of COVID-19 considerably. Suburban net absorption totaled only -1.1% of inventory, 40 basis points below the national suburban average in 2020, while vacancy rose to only 12.2%, among the lowest rates in the country. Submarkets such as Del Mar Heights, Sorrento Mesa and Eastgate in fact saw occupancy growth throughout the year. In comparison, Downtown San Diego recorded occupancy falling by 329,807 square feet and vacancy of 19% at year-end.

Sales activity cooled markedly as investors took on a more cautious approach, in many cases putting greater emphasis on lab and life sciences investment in lieu of traditional office space. Suburban San Diego sales totaled $1.3 billion, a 39.5% drop from 2019 and the lowest level since 2013. However, pricing rose by 26.3% to an average of $390 per square foot, highlighted by the Pointe at Torrey Pines achieving a price of $701 per square foot.

Submarket commentary

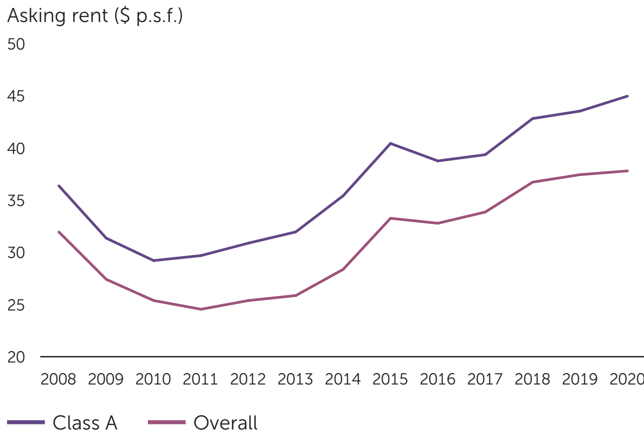
Sorrento Mesa and Rancho Bernardo positions well in relation to the broader metro area, as both submarkets registered positive net absorption in 2020 and capture a significant share of life sciences and skilled office-using talent. At $37.80 and $38.28, they remain advantageous cost-wise compared to Del Mar Heights, UTC, La Jolla and the North Beach Cities, and still have enough available blocks to absorb future demand and spillover from more expensive submarkets.

VACANCY ONLY MODERATELY ROSE IN 2020



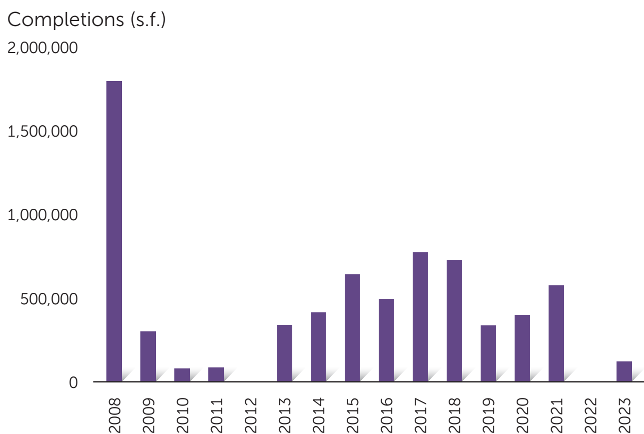
Note: statistics only cover suburban submarkets.

RENTS REACHED $45 PER SQUARE FOOT IN 2020



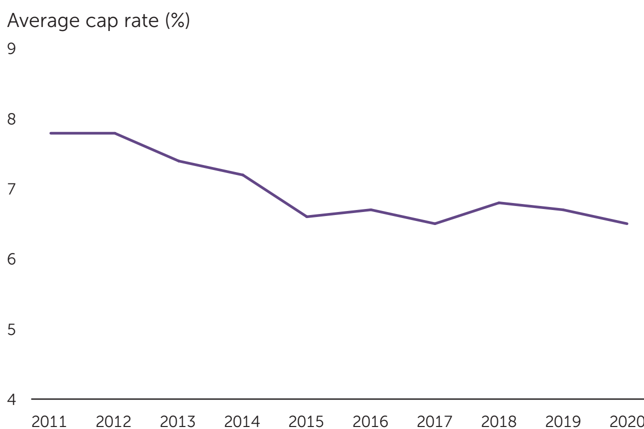
Note: statistics only cover suburban submarkets.

NEW SUPPLY HAS DELIVERED IN A PIECEMEAL FASHION THIS CYCLE



Note: statistics only cover suburban submarkets.

CAP RATE COMPRESSION CONTINUES, BUT MORE SLOWLY



Note: statistics only cover suburban submarkets.

As with most of the country, renewals dominated activity in these submarkets. Northrop Grumman and Qualcomm both stayed in place for a combined 333,606 square feet, joined by smaller relocations and expansions from DexCom, Intel, Intuit and Google, among other tenants. Construction activity remains nearly non-existent, which will challenge occupiers looking to relocate or expand and keep vacancy balanced and rents buoyant.

Outlook

San Diego's suburbs are poised to recover on par or faster than the country as a whole despite a number of challenges in terms of cost, business climate and domestic population flows given the market's strengths in life sciences, defense, engineering and skilled professional services. The relative lack of new construction compared to many other large suburban markets has created a built-in cap on vacancy and aging office stock can be repurposed easily for lab or alternative uses. Improved connectivity as a result of new public transit will provide a boost to UTC and in turn push priced-out users to markets to Sorrento Mesa, Rancho Bernardo and similar submarkets.

SAN FRANCISCO

Market overview

San Francisco experienced the most abrupt shift in office market dynamics of any market as a result of the COVID-19 pandemic. Previously one of the tightest office markets in the country with a vacancy rate of 5.2% at the end of 2019, the sudden movement to remote work combined with a reliance on tech companies more amenable to permanent work-from-home strategies, stringent stay-at-home orders, rents in excess of $90 per square foot and a potential exodus to less-dense and lower-cost geographies resulted in 6.2 million square feet of negative net absorption in 2020, nearly tripling vacancy to 13.6% in the process.

The market now faces one of the largest sublease inventories in the country: 7.5 million square feet, up from 2.4 million square feet at the end of 2019 and equivalent to 9.4% of inventory. Many major occupiers such as Dropbox, Levi Strauss, Glassdoor and Zendesk have partially or entirely subleased their headquarters, further amplifying the current market correction and leading to markedly more aggressive concession packages from landlords, with Dropbox finding success in Vir Biotechnology signing on for 134,000 square feet of Dropbox's sublease space.

Conversely, investment has held up well in the context of widespread economic disruption. After a banner year in 2019 with $7.2 billion in office sales, 2020 approached the

UNITED STATES

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By JLL

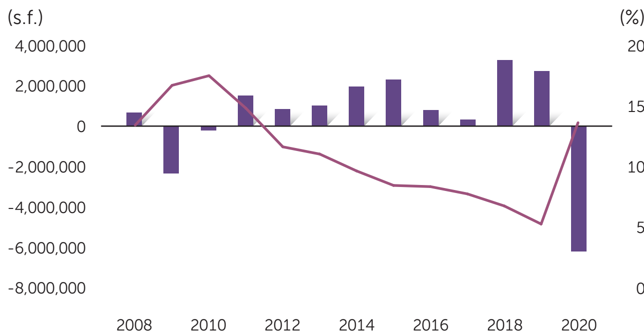
$3 billion mark, ranking ahead of 2019 and closer in line with earlier years in the cycle. Pricing rose once again to an average of $1,164 square feet, up 25.3% compared to 2019. Sales of note included DWS taking on 49% interest at 525 Market as well as 221 Main, 123 Mission and 900 7th all selling for more than $200 million.

Submarket commentary

As a local, domestic and international hub for tech users, South of Market (SoMa) is particularly exposed to a short-term stall in market activity. Negative net absorption of 12.5% of inventory is 470 basis points above average and rents have now fallen below those of the market overall. At 16.5%, vacancy is 290 basis points higher as well.

Leasing was modest in 2020 and almost entirely comprised of leases smaller than 50,000 square feet, the primary exception being Knotel's 82,824-square-foot signing at 301 Brannan. Other tenants taking on space in 2020 included Formagrid, UserTesting, People. AI, Clearbit and Lob.

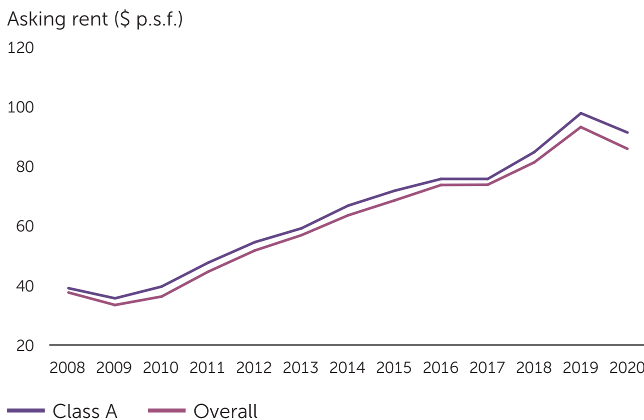
VACANCY NEARLY TRIPLED IN 2020 AFTER -6.2 M.S.F. OF ABSORPTION



Net absorption (s.f.) Total vacancy (%)

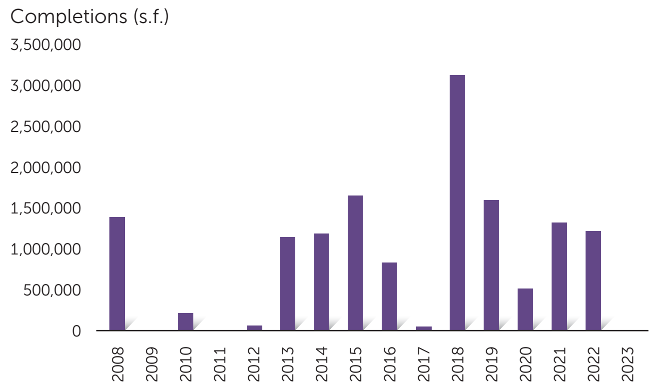
Note: statistics cover San Francisco proper only.

ASKING RENTS HAVE DECREASED ONLY MARGINALLY



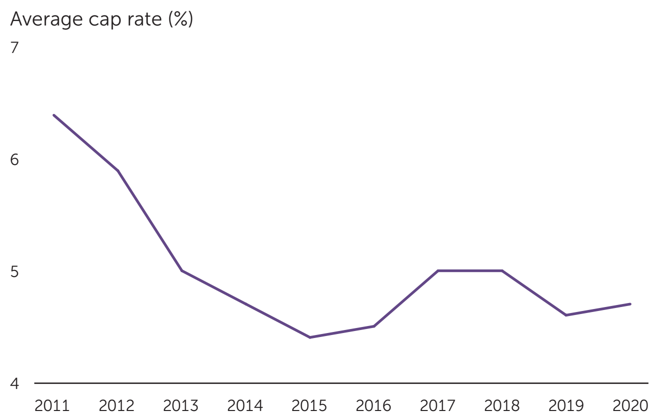
Note: statistics cover San Francisco proper only.

THE END OF THE CURRENT DEVELOPMENT CYCLE IS APPROACHING



Note: statistics cover San Francisco proper only.

CAP RATES REMAIN BELOW 5%



Note: statistics cover San Francisco proper only.

Only one building (345 4th) is currently under construction in SoMa, with construction largely in the neighboring South Financial District and Mid-Market neighborhoods. This lack of impending new construction will mitigate short-term elevated vacancy.

Outlook

San Francisco faces one of the most challenging recoveries nationally, but its deep talent pool, existing physical and social infrastructure and status as a global capital of technology home to many of the world's most important industry leaders makes its appeal difficult to replicate elsewhere. A period of minimal new construction and greater clarity on re-entry and pricing will help to renew activity beginning in mid-2021. Despite office market headwinds, venture capital funding, IPO activity and big tech hiring all remain healthy, with the ongoing pandemic driving robust demand for cloud and software services. Over the longer term, this positions San Francisco and the broader Bay Area well as a global hub for top-tier tech talent and innovation, in turn buoying office demand.

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ASCENDAS REAL ESTATE INVESTMENT TRUST

Ascendas Funds Management (S) Limited
Company Registration Number: 200201987K

168 Robinson Road
#30-01 Capital Tower
Singapore 068912
Tel: +65 6713 2888
Fax: +65 6713 2999
Email: a-reit@capitaland.com

www.ascendas-reit.com

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