EMBARGOED UNTIL 11.30 AM WEDNESDAY 30 OCTOBER 2019

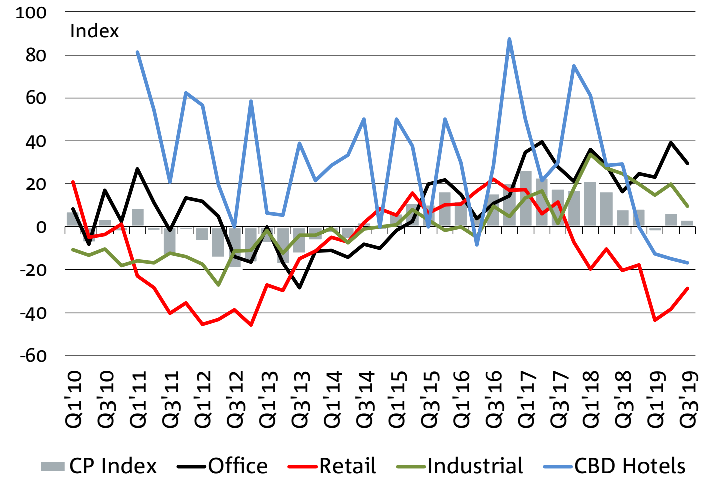
NAB COMMERCIAL PROPERTY SURVEY Q3-2019

Date October 2019 | NAB Behavioural & Industry Economics

KEY FINDINGS

- Commercial property market sentiment (measured by NAB's Commercial Property Index) fell 4 points to +3, in line with its long-term average (+3). It fell steeply to multi-year lows in VIC and NSW. QLD the big improver, led by Office where the improved economic environment has reportedly bolstered leasing activity. Sentiment was lowest in WA.
- By sector, Office and Industrial sentiment was highest, but fell as below average business conditions persisted. In CBD Hotels, it fell to a new survey low with reports major markets are experiencing lower room rates and occupancy amid new supply. Retail improved (but still weakest overall) as slow wage growth, high debt levels and stretched budgets continued to weigh on the household sector.
- Confidence softened against a backdrop of below trend economic growth. It was highest for Office and Industrial. In CBD Hotels, confidence waned further. In the long under-performing Retail space, there were positive signs as confidence lifted (albeit still negative). QLD was the most confident state for commercial property.
- Capital growth expectations for the next 12-24 months are positive for Office and Industrial, and negative for CBD Hotels and Retail. Office returns are expected to be highest in NSW and QLD, with these states also leading the way for capital growth for Industrial. Retail values are expected to continue falling or remain flat in all states.
- National office vacancy fell to 7.6% in Q3, but is expected to inch up to 7.8% in 2 years' time, with rising vacancy in NSW and VIC (to still very low levels) offset by modest tightening in QLD, SA/NT and WA. Retail vacancy climbed to a survey high 6.4% in Q3 and rose in all states bar SA/NT (but highest overall). Retail vacancy is expected to remain relatively high over the next 1-2 years. Industrial vacancy fell to 6.1% in Q3 (driven by market tightening in NSW where demand is reportedly strong amid a lack of supply) and is expected to tighten further over the next 1-2 years.
- Office and Industrial property also expected to lead the way for rental growth in the next 12-24 months. The highest returns for Office are forecast in QLD and VIC, with QLD also leading the way for Industrial rents. The outlook for Retail rents is negative and is expected to fall in all states, with SA/NT under most pressure followed by VIC and NSW.
- The number of property developers expecting to start new works in the next 0-6 months remains well below average - consistent with the latest activity indicators which are also showing weakness in both housing and non-residential construction.
- For developers starting new works, the number looking at residential projects (47%) remains well below average, reinforcing the view residential building activity has passed its peak (and which NAB Economics expects to persist for the next couple of years).
- Funding conditions stabilised but are still difficult. A net -32% said it was harder to obtain loans and -21% equity (unchanged from Q2). Funding conditions are set to improve over the next 3-6 months. Now, only -9% see debt and -10% equity funding worsening - putting conditions back to where they were in late-2015/early-2016.

NAB COMMERCIAL PROPERTY INDEX



	Q2 2019	Q3 2019	Next 12m	Next 2yrs
Office	39	30	37	36
Retail	-38	-29	-21	-2
Industrial	20	10	28	42
CBD Hotels	-15	-17	-33	-25
CP Index	**7**	**3**	**11**	**19**

MARKET OVERVIEW - NAB COMMERCIAL PROPERTY INDEX

Overall sentiment (measured by NAB's Commercial Property Index) fell 4 points to +3 in Q3, in line with its long-term average (+3).

Sentiment fell in all sectors, except Retail (up 9 to -29), although it was again lowest overall as slow wages growth, high debt levels and stretched budgets continued to weigh on the household sector.

Sentiment remained strongest for Office property (down 9 to +30) and well above average (+9). Interestingly, sentiment softened in the key markets of VIC and NSW, but rose strongly in QLD and SA/NT, while WA continued to under-perform.

Industrial sentiment also eased (down 10 to +10) as below average business conditions persisted, and was softer in all states bar SA/NT (albeit negative). In the CBD Hotels sector, sentiment continued to wane, falling to a new survey low (down 2 to -17) and well below average (+30). Property professionals in this space signalled a further fall in capital and rev-par growth and lower occupancy.

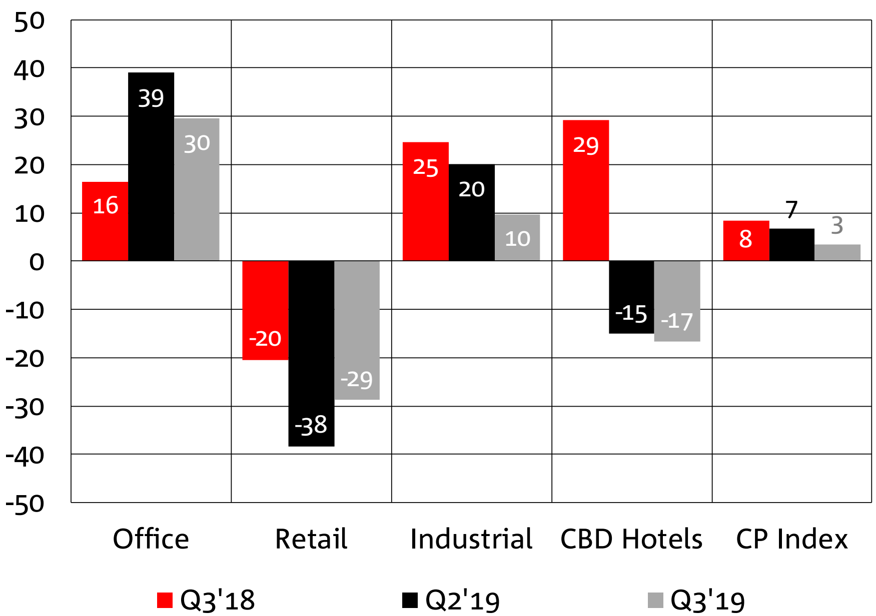
Overall confidence levels in commercial property markets have also softened against a backdrop of below trend economic growth. Confidence 12 months forward was down 3 to +14, with the longer-term outlook (2 years' time) unchanged (+23).

Confidence was highest for Office (down 10 to +37 in 12 months and down 10 to +36 in 2 years' time), followed by Industrial (down 5 to +28 in 12 months and down 1 to +42 in 2 years time).

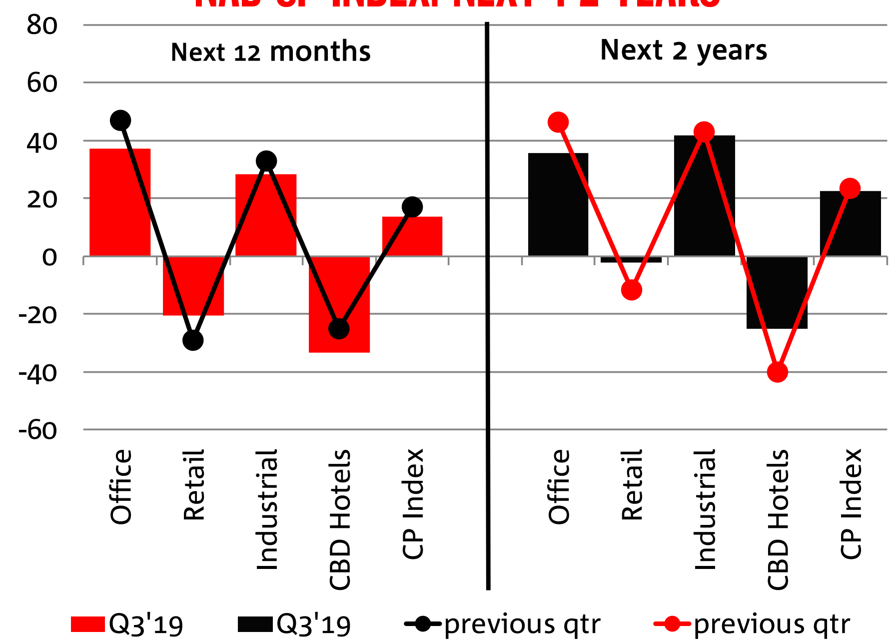
In the CBD Hotels sector, confidence waned further (and was lowest overall) at -33 in 12 months and -25 in 2 years' time amid reports most major markets are experiencing a decline in room rates and occupancy amid significant new supply, rather than lower demand.

In the long under-performing Retail space, there were some positive signs, with confidence up 8 to -21 in 12 months and up 10 to -2 in 2 years' time. That said, confidence in this sector is still very weak.

NAB COMMERCIAL PROPERTY INDEX



NAB CP INDEX: NEXT 1-2 YEARS



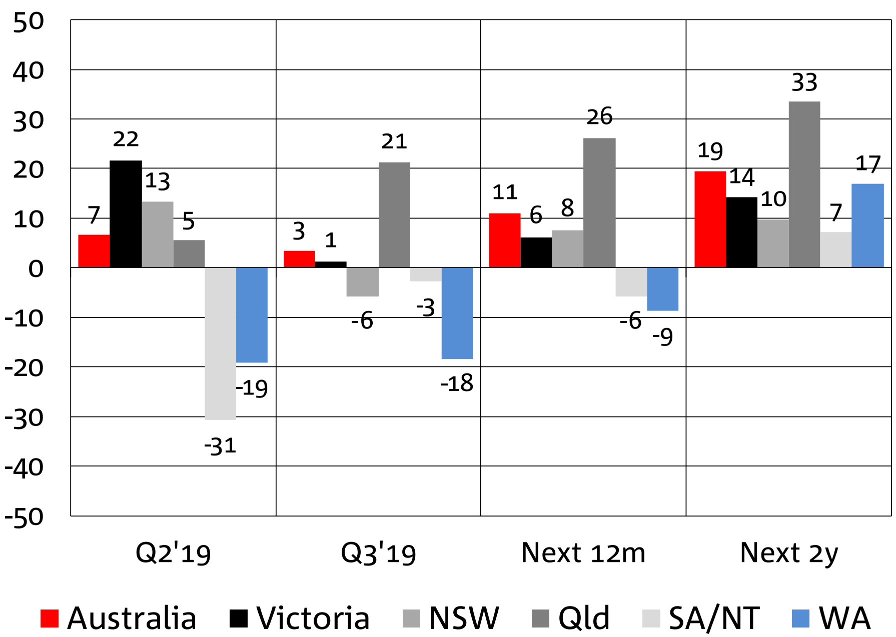
MARKET OVERVIEW - INDEX BY STATE

Overall market sentiment fell steeply in the key states of VIC (down 21 to a 5 year low +1) and NSW (down 19 to a six year low -6 and the first negative read since mid-2014), with weaker outcomes for Office and Industrial property. QLD was the big improver (up 16 to +21), led by Office (up 14 to a survey high +41) where the improved economic environment reportedly bolstered leasing activity.

Confidence over the next 12 months is highest in QLD (+26) by some margin, and also highest in all sectors. The outlook is mildly positive for NSW (+8) and VIC (+6), but negative in SA/NT (-6) and WA (-9).

QLD (+33) is also the most optimistic state in 2 years' time, and the most confident for Office property. Expectations are positive in WA (+17), and it leads the way for Industrial property. Property professionals were less positive in VIC (+14) and NSW (+10), but NSW leads the way for Retail. Confidence in SA/NT (+7) lifted.

COMMERCIAL PROPERTY INDEX - STATE



OFFICE PROPERTY MAKET INDEX – STATES

	VIC	NSW	QLD	WA	SA/NT	AUS
Q3'19	30↓	29↓	41↑	-20↓	40↑	**30↓**
Q3'20	40↓	40↓	44↑	-10↓	40↑	**37↓**
Q3'21	35↓	24↓	56↑	10↓	50↑	**36↓**

RETAIL PROPERTY MARKET INDEX – STATES

	VIC	NSW	QLD	WA	SA/NT	AUS
Q3'19	-24↑	-50↔	-18↑	-25↑	-43↓	**-29↑**
Q3'20	-26↑	-32↑	3↑	-25↑	-64↓	**-21↑**
Q3'21	-11↑	6↑	5↓	0↑	-43↓	**-2↑**

INDUSTRIAL PROPERTY MARKET INDEX - STATES

	VIC	NSW	QLD	WA	SA/NT	AUS
Q3'19	-5↓	13↓	26↓	-14↓	-17↑	**10↓**
Q3'20	15↓	32↓	39↓	14↑	0↑	**28↓**
Q3'21	30↓	41↔	47↓	64↓	0↑	**42↓**

LEGEND: ↑ up since last survey ↓ down since last survey ↔ unchanged

MARKET OVERVIEW - CAPITAL & VACANCY EXPECTATIONS

Capital growth expectations for the next 12 months were pared back for Office (1.4% vs. 1.9% in Q2), with returns highest in NSW (1.9%), and QLD (1.7%) and lowest in WA (-2.8%). Industrial returns also expected to be lower (0.9% vs. 1.0%) with SA/NT (3.8%) and QLD (1.8%) out-performing and WA under-performing (flat). Retail improved (-0.6% vs. -1.7%), but expected to fall in all states bar QLD (flat). CBD Hotel values now tipped to fall -2.5% (-1.8% in Q2).

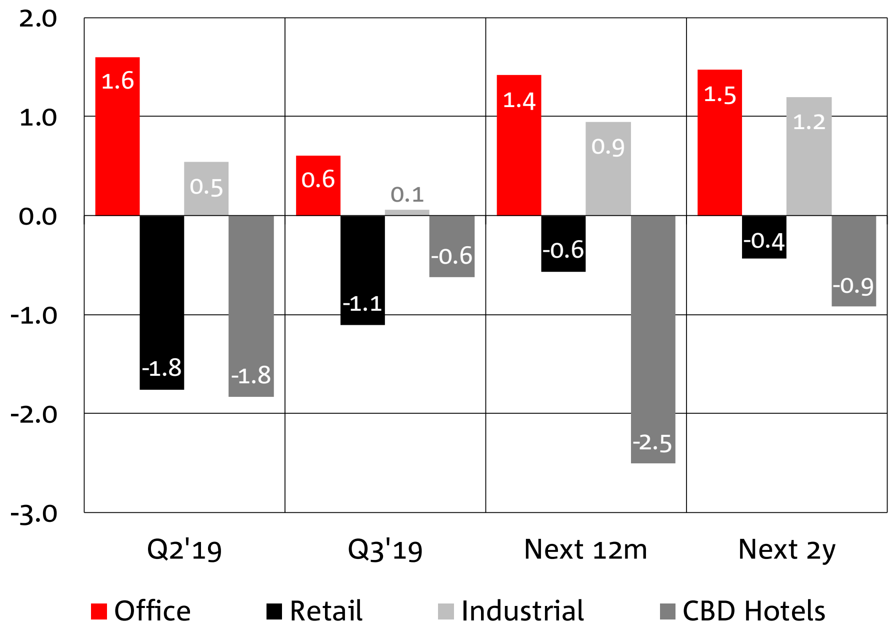
Capital returns for Office and Industrial property in 2 years' time were trimmed (1.5% vs. 2.0% in Q2 and 1.2% vs. 1.5% respectively). SA/NT (2.5%) and QLD (2.4%) expected to provide the highest returns for Office and QLD (2.3%) for Industrial. Retail values now tipped to fall just -0.4% (-1.7%, in Q2), and fall modestly in all states bar WA (flat). Capital values in the CBD Hotels sector are also predicted to fall by a more moderate -0.9% (2.6% in Q2)- **see page 10 for detail**.

National office vacancy fell to 7.6% in Q3 (7.9% in Q2). Lower vacancy was reported in NSW (4.1%) and SA/NT (11.8%). Vacancy rose in QLD (11.4%) and VIC (to a still low 5.3%) and was steady in WA (15.0%). Overall vacancy is expected to inch up to 7.8% in 2 years' time, with rising vacancy in NSW and VIC (to still very low levels) offset by modest tightening in QLD, SA/NT and WA.

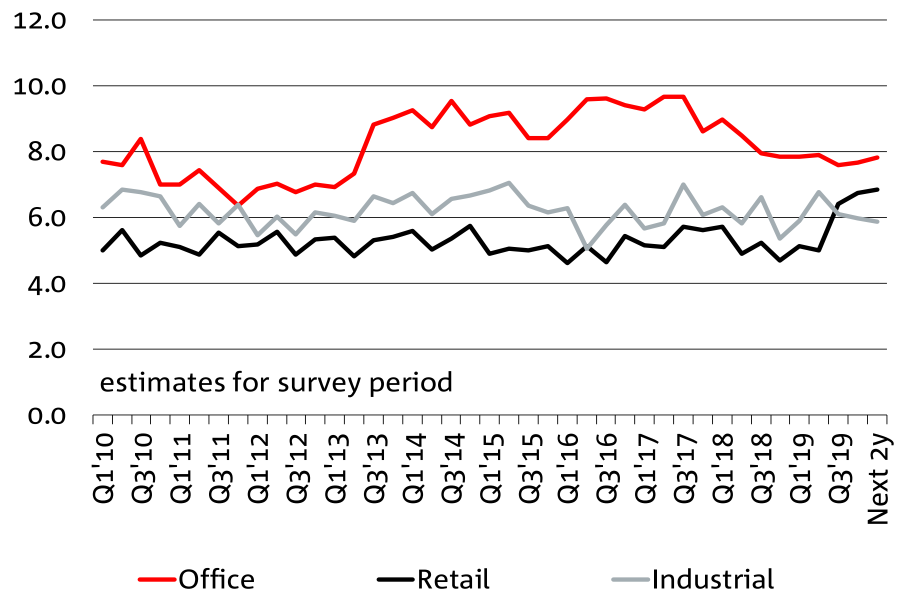
Overall Retail vacancy climbed to a survey high 6.4% in Q3 (5.0% in Q2). Vacancy rose in all states bar SA/NT (7.9%) but was still highest overall. Vacancy in this sector is expected to remain relatively high over the next 1-2 years in all states (except WA).

In the Industrial sector, vacancy fell to 6.1% in Q3 (6.8% (in Q2), driven down by market tightening in NSW (4.0%) where demand is reportedly strong amid a lack of supply. National vacancy is expected to tighten further in the next 1-2 years - **see page 11 for detail**.

CAPITAL VALUE EXPECTATIONS (%)



VACANCY RATE EXPECTATIONS (%)



MARKET OVERVIEW - RENTS & SUPPLY

Office and Industrial property are expected to lead the way for rental growth over the next 12 months, on average growing 1.0% each.

Office expectations are highest in QLD (1.1%) and NSW (0.8%), and weakest in WA (-2.8%). Industrial rents are expected to be highest in QLD (2.4%) and VIC (1.1%) and weakest in SA/NT (-0.7%).

Nationally, Industrial rents are set to out-perform the broader market in 2 years' time (1.8%), with QLD (3.7%) and WA (1.5%) generating the highest income returns. Office rents are also expected to grow 1.1% in 2 years' time, with the best returns expected in QLD (2.9%) and VIC (1.4%).

The outlook for Retail rents in the next 1-2 years is negative (-1.5% & -1.2%), Rents are expected to fall in all states over this period, with SA/NT under most pressure, followed by VIC and NSW - **see page 10 for detail**.

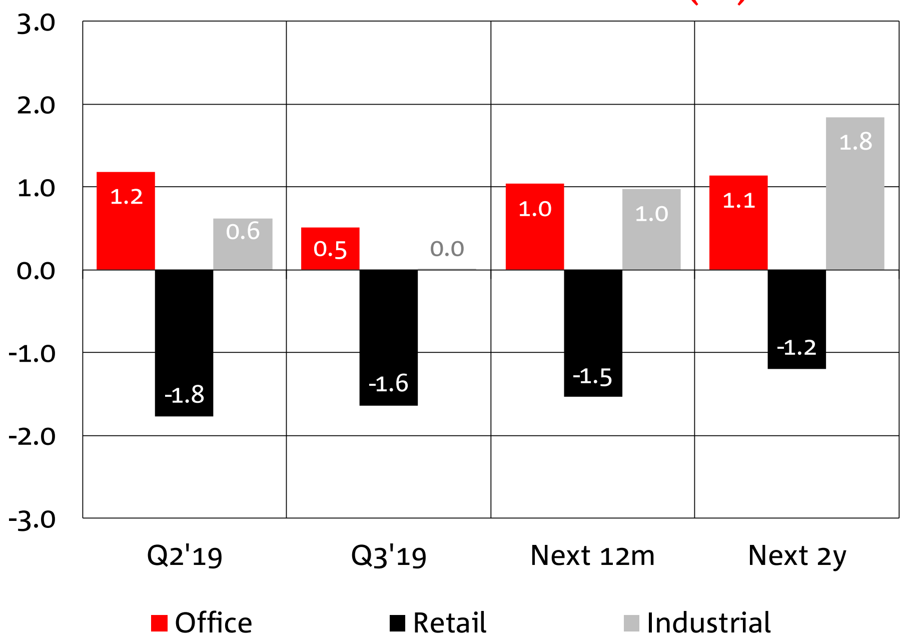
National supply conditions in Office and Industrial markets were 'neutral' in Q3 and will remain so in the next 1-5 years. But this masks big differences by state. NSW Office markets are now under-supplied but will return to balance in 3-5 years. But over--supply still a feature in WA and SA/NT (and will remain so in the next 1-5 years).

Industrial markets remain somewhat under-supplied in NSW and VIC, but somewhat over-supplied in WA and SA/NT. All markets are expected to return to balance in 3-5 years, except NSW (under-supplied) and VIC (somewhat over-supplied).

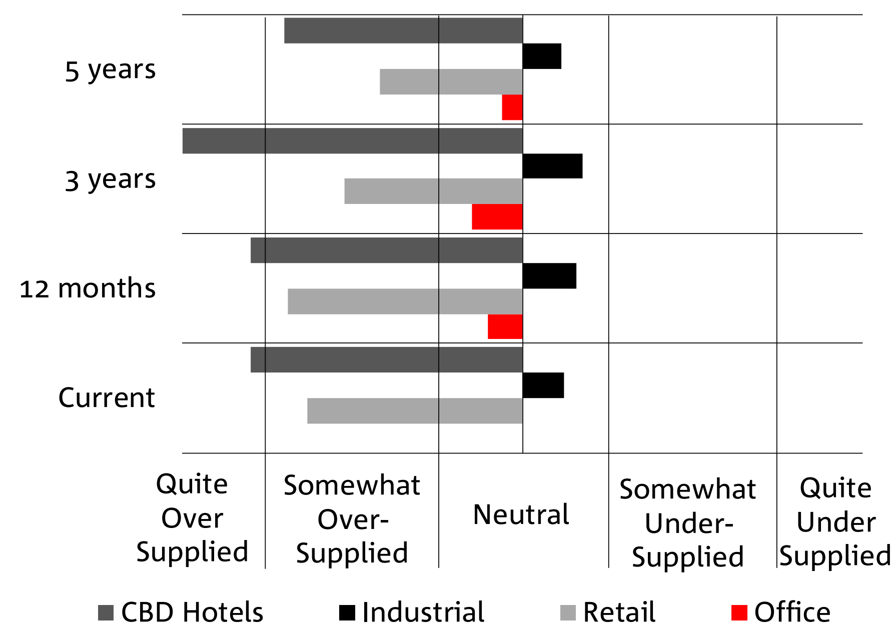
In Retail, all state markets are currently over-supplied, will remain so over the next 1-5 years (except in QLD which is neutral in 5 years).

CBD Hotels markets are quite over-supplied, and also expected to remain so over the next 1-5 years as growth in new supply continues across major markets.

GROSS RENTAL EXPECTATIONS (%)



SUPPLY CONDITIONS



MARKET OVERVIEW - DEVELOPMENT INTENTIONS

The number of property developers expecting to start new works in the next month fell to just 6% in Q3 (13% in Q2), and those planning to start in the next 1-6 months rose to 29% (26% in Q2). Overall, just 35% plan to start new works in the short-term (or next 6 months, this was down from 39% in Q2 and well below average (49%).

The number who said they plan to start new projects in the next 6-12 months was broadly unchanged at 28% (27% in Q2). Those planning to start in the next 12-18 months was also broadly unchanged at 18%, but those with a longer time frame fell to 10% (13% in Q2).

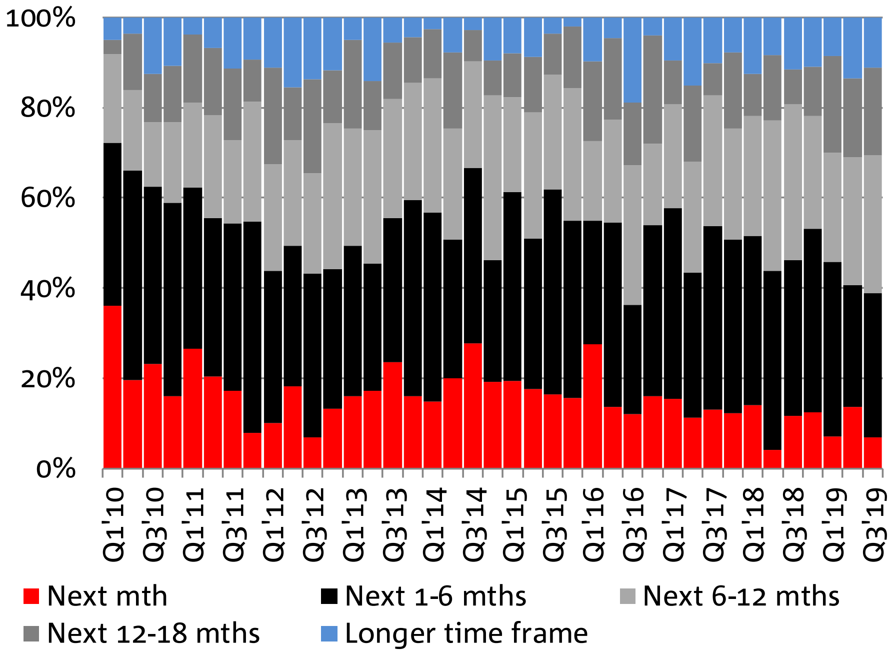
These results appear consistent with the latest activity indicators which are also showing weakness in both housing and non-residential construction.

For developers planning to commence new works, the number targeting residential development projects rose to 47% in Q3 (44% in Q2), but remains below average (54%).

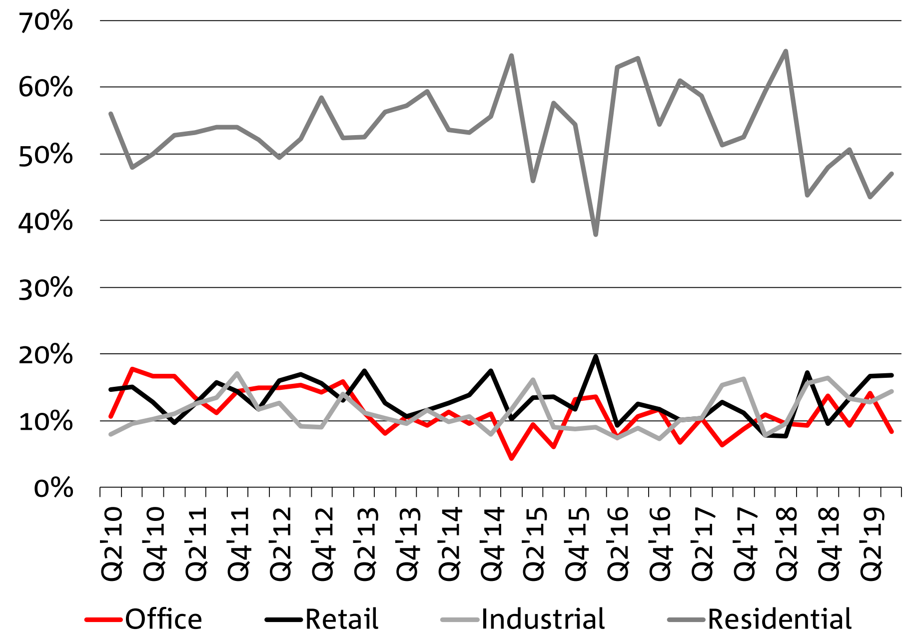
These results reinforce the view residential building activity has passed its peak. The latest official data shows that building approvals are continuing to trend down and feeding into lower construction levels - a situation that NAB Economics expects to persist for the next couple of years.

In other sectors, property professionals pointed to below average numbers of developers targeting Office (8%) property, but a higher than average number targeting both Retail (17%) and Industrial property (14%) during the quarter.

COMMENCEMENT INTENTIONS - TIME



COMMENCEMENT INTENTIONS - SECTOR



MARKET OVERVIEW - LAND SOURCES & CAPITAL INTENTIONS

The number of property developers looking to use land-banked stock for their new projects fell to 53% in Q3 (63% in Q2), and was below average (59%). Given the residential property market is in correction mode, developers may now be waiting for the market to turn before releasing new land.

The number who said they were seeking new acquisitions increased to 23% (20% in Q2), but this was down from 27% at the same time last year, and below average (26%).

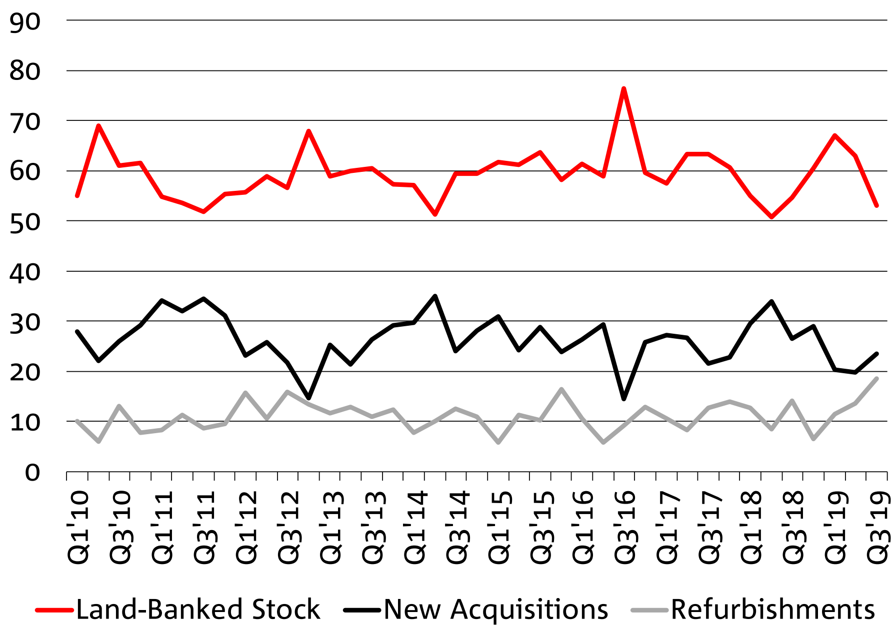
The number of developers looking at refurbishment opportunities also continued to climb, reaching a survey high 19% in Q3, up from 14% in Q3 and well ahead of average (11%).

The number of property developers planning to source more capital to fund their developments in the next 6 months was broadly unchanged at 23% in Q3 (24% in Q2). Around 59% had no intention to source capital in the short-term (unchanged from Q2) and 18% were unsure (17% in Q4).

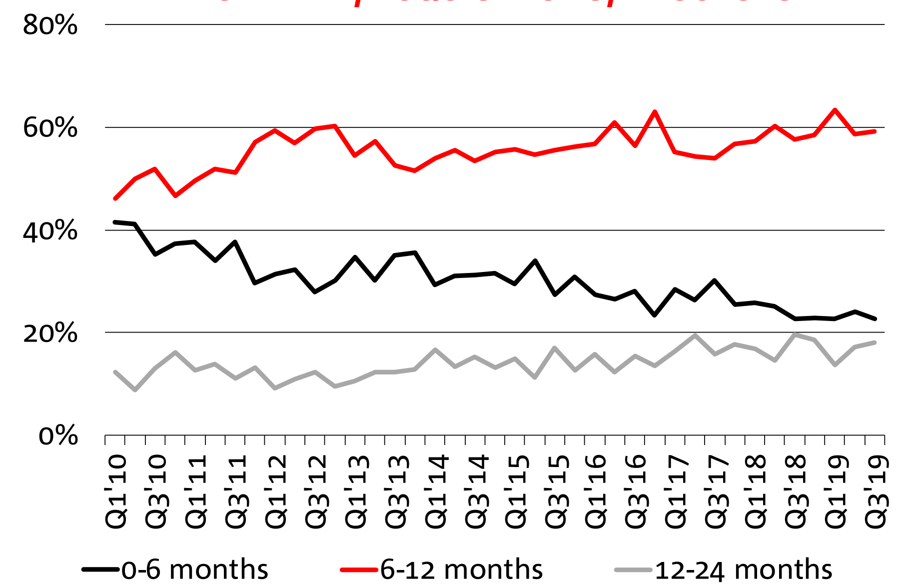
The number of developers planning to source capital in the next 6-12 months was also broadly unchanged at 27% in Q3 (28% in Q2), Around 48% had no intention to source funds and 26% were unsure.

Slightly more developers (31%) intended to source more capital in the longer-term (12-24 months), but 34% said no and 35% were unsure.

SOURCES OF LAND DEVELOPMENT (%)



INTENT TO SOURCE MORE CAPITAL FOR DEVELOPMENT/ACQUISITIONS/PROJECTS



MARKET OVERVIEW - FUNDING & PRE-COMMITMENTS

The net number of property professionals who said it was harder to obtain borrowing or loans (debt) needed for their business was unchanged at -32% in Q3.

The net number of property professionals who said it was harder to obtain equity funding was also broadly unchanged at -21% (-22% in Q2.

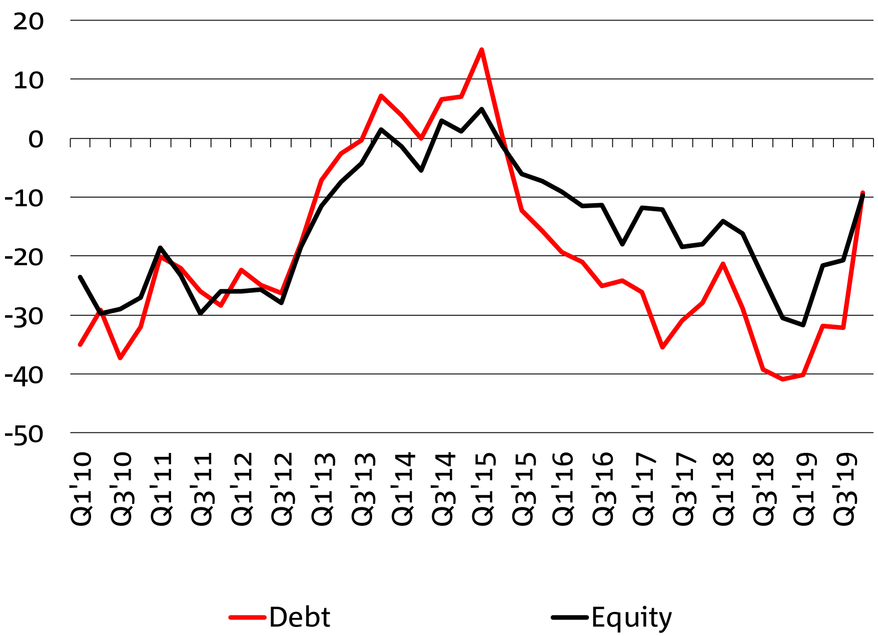
Looking ahead, however, the outlook is for debt and equity funding conditions to improve significantly over next 3-6 months. Only a net -9% of property professionals see debt funding conditions worsening over this timeframe, and just -10% said it will be harder to obtain equity financing. This would put funding conditions back to where they were in late-2015/early-2016.

The average pre-commitment to meet external debt funding requirements for new developments across Australia fell to 61.9% for residential property (65.6% in Q2), and 57.5% for commercial property (58.0% in Q2).

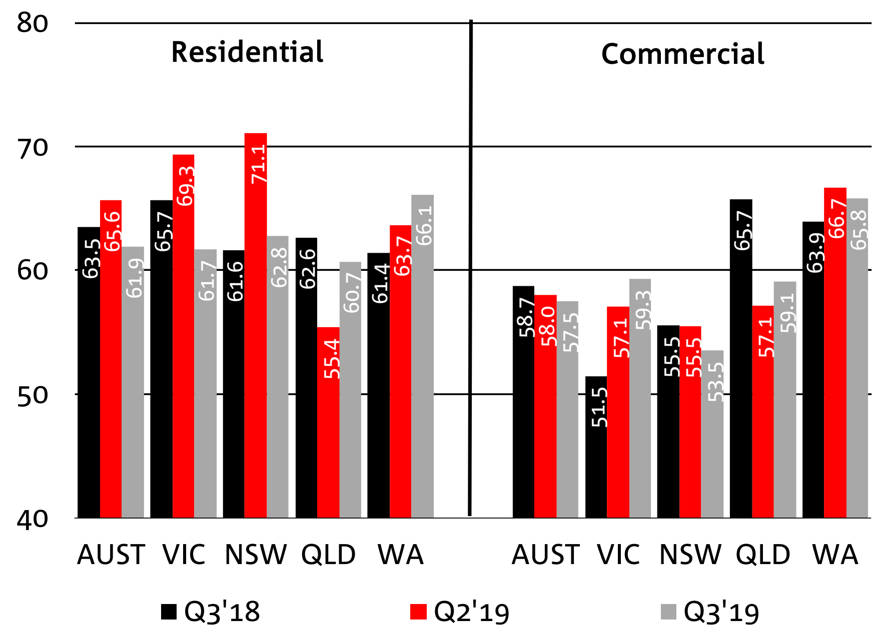
Residential requirements fell in VIC (61.7%) and NSW (62.8%), but increased in QLD (60.7%) and WA (66.1%). Commercial property pre-commitments were lower in NSW (53.5%) and WA (65.8%), but rose in VIC (59.3%) and QLD (59.1%).

On balance, more property professionals now expect pre-commitment requirements to improve going forward - a net +3% for residential property in the next 6 months and +21% in 12 months' time, and +7% in 6 months and +19% in 12 months for commercial.

EASE OF ACQUIRING DEBT/EQUITY (NET)



PRE-COMMITMENT REQUIREMENTS (%)



SURVEY RESPONDENTS EXPECTATIONS (AVG) Q3-2019

OFFICE CAPITAL VALUES (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q3'19	0.3	0.9	1.1	-3.3	1.1	0.6
Q3'20	1.3	1.9	1.7	-2.8	1.5	1.4
Q3'21	0.9	1.2	2.4	-0.2	2.5	1.5

OFFICE RENTS (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q3'19	0.4	0.8	1.1	-2.8	-0.1	0.5
Q3'20	1.7	1.0	1.8	-2.4	0.4	1.0
Q3'21	1.4	0.3	2.9	-1.3	1.2	1.1

RETAIL CAPITAL VALUES (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q3'19	-1.1	-1.4	-1.0	-1.9	-1.1	-1.1
Q3'20	-0.9	-0.8	0.0	-1.4	-1.3	-0.6
Q3'21	-0.5	-0.9	-0.4	0.0	-0.8	-0.4

RETAIL RENTS (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q3'19	-1.9	-2.2	-0.8	-0.6	-2.9	-1.6
Q3'20	-2.0	-2.2	-0.3	-0.5	-3.1	-1.5
Q3'21	-1.7	-1.3	-0.2	-0.6	-2.9	-1.2

INDUSTRIAL CAPITAL VALUES (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q3'19	-0.1	0.3	0.6	-1.3	-1.5	0.1
Q3'20	0.8	0.8	1.8	0.0	3.8	0.9
Q3'21	0.3	0.8	2.3	1.3	0.0	1.2

INDUSTRIAL RENTS (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q3'19	-0.2	0.1	1.1	-1.6	-2.1	0.0
Q3'20	1.1	0.5	2.4	-0.1	-0.7	1.0
Q3'21	0.8	1.2	3.7	1.5	0.0	1.8

SURVEY RESPONDENTS EXPECTATIONS (AVG) Q3-2019

OFFICE VACANCY RATE (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q2’19	5.3	4.1	11.4	15.0	11.8	7.6
Q2’20	6.1	4.6	10.6	14.5	11.4	7.7
Q2’21	7.0	6.0	9.6	11.0	11.5	7.8

RETAIL VACANCY RATE (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q2’19	6.0	6.1	7.0	6.0	7.9	6.4
Q2’20	6.8	6.6	6.9	5.0	8.1	6.8
Q2’21	6.9	7.0	6.8	4.3	8.1	6.8

INDUSTRIAL VACANCY RATE (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q3’19	5.8	4.0	7.8	8.7	9.0	6.1
Q3’20	6.2	3.9	7.4	8.0	9.0	6.0
Q3’21	6.8	4.1	7.1	6.0	9.0	5.9

NOTES:

Survey participants are asked how they see:

- capital values;
- gross rents; and
- vacancy rates

In each of the commercial property markets for the following timeframes:

- annual growth to the current quarter
- annual growth in the next 12 months
- annual growth in the next 12-24 months

Average expectations for each state are presented in the accompanying tables.

**Results for SA/NT may be biased due to a smaller sample size.*

ABOUT THE SURVEY

In April 2010, NAB launched the first NAB Quarterly Australian Commercial Property Survey with the aim of developing Australia’s pre-eminent survey of market conditions in the commercial property market.

The large external panel of respondents consists of Real Estate Agents/Managers, Property Developers, Asset/Fund Managers and Owners/Investors.

Around 350 property professionals participated in the Q3 2019 Survey.

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