

Bayleys Research

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Auckland CBD Office

New business formation and expansion outpaced office development again over 2016 resulting in a further reduction in vacancy rates across the City.

The results of the latest Bayleys Research office vacancy surveys has seen the availability of space falling in all major precincts. In the CBD the overall vacancy rate has fallen to 6.25% a trend mirrored across the CBD fringe precincts where the latest figure stands at 10.1%.

Unsurprisingly, given current market conditions, the development sector has been responding, particularly within the CBD's northern and western precincts, continuing a trend which has been apparent over recent years. While the largest single development, Commercial Bay will not be completed until mid 2019, 2017 will see a number of developments completing which will result in an easing of pressure on both the availability of space and rental appreciation.

A feature of the market over recent years has been the move by companies and local government organisations, to move staff from

multiple locations and consolidate within a single building a trend which will continue over the next few months.



CBD Availability Squeezed

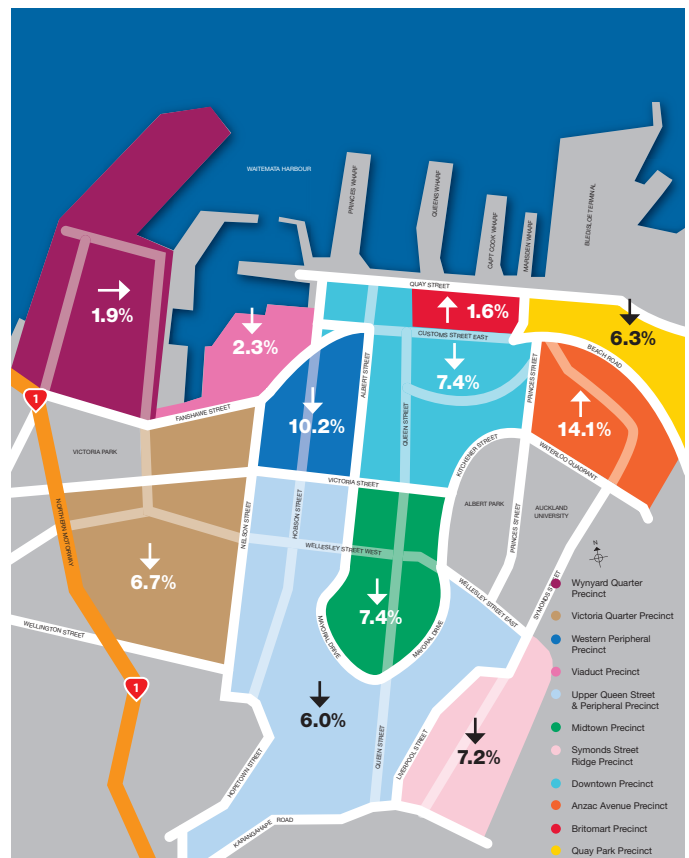
The results of the latest Bayleys Research's CBD office vacancy survey, which covers a total of 1,761,025m² of office accommodation show the overall CBD office vacancy rate has dropped to 6.25% from 7.8% in early 2016.

Prime grade (Premium and A Grade space) vacancy in the CBD has remained unchanged at a miniscule 2.4% despite an increase in the total inventory of 28,654m, the biggest increase in new supply for six years. This increase is largely due to the completion of Fonterra's new headquarters in Fanshawe Street and the BDO Centre at 151 Victoria Street West, now fully leased.

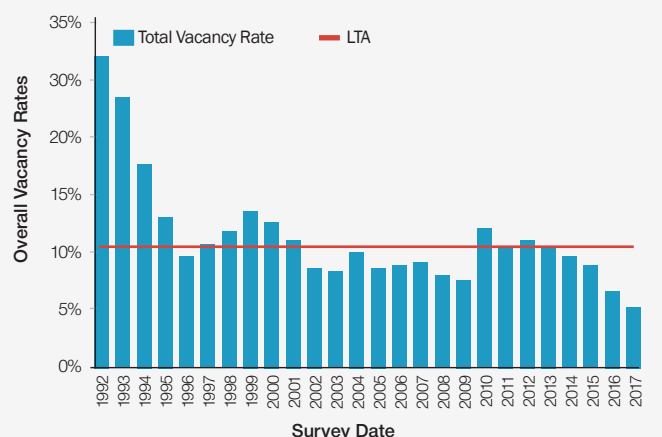
B Grade space still forms the largest sector of the CBD market although the inventory has dropped to 517,704m from 528,230m a year ago as a result of refurbishments underway and redevelopment projects, predominantly to apartments. The B Grade vacancy rate is now 9.4%, the first time that it has been below 10% since 2009.

C Grade vacancy continues to fall, now at 8.6% from 12.5%, with a continuing trend of C Grade space also being removed for change of use.

Empty CBD office accommodation is now at its lowest level since Bayleys Research began its CBD vacancy survey in 1992 and this is the first time overall vacancy has been below 7%.



Auckland CBD Overall Vacancy Rate



New Development To Ease Pressure

High levels of business confidence and employment growth in the service sector have been driving demand for office accommodation. However, it is likely that we have reached a cyclical low in terms of CBD vacancy as a substantial new development pipeline will begin to outpace demand. More than 50,000m² of prime space will come on stream this year. This will include three new buildings in the Wynyard Quarter – the Datacom building (16,000m²), the Innovation 5a building (8,500m²) and Bayleys House (8,000m²) plus 46 Sale Street (10,000m²). In addition Vodafone NZ Ltd will not be renewing the lease on its 14,000m² head office building on Fanshawe Street when it expires in April 2017 as it consolidates in Takapuna.

Most of these new premises have already been either fully or largely pre-let, or are likely to be by the time they are completed. The Bayleys building for example will be fully occupied by Bayleys, Mayne Wetherall and IBM. The Datacom building has just one office floor (2,165m²) currently vacant. The challenge will be back filling buildings which are being vacated by their current occupiers. In many of the cases, where tenants are centralising from a number of locations, they are leaving more space behind than they are moving to because these new buildings enable them to occupy space more efficiently. Also, the number of residential conversions could slow as a result of construction and funding capacity constraints. Therefore Bayleys Research expects CBD office vacancy rates to start heading back up again this year.

There are already indications the tide is close to turning, with only a small drop in vacancy in the past six months from 6.7% in Bayleys Research's July 2016 survey to 6.25%. The amount of vacant A Grade has increased over the past six months, its first upward movement in three years, due to the transition of large tenants in the northern CBD to premium grade buildings. Examples of this include, Meredith Connell which vacated five floors of Shortland Street's Forsythe Barr building to take occupation within 151 Victoria Street. Meredith Connell has joined NZME which moved staff from 46 Albert Street and 54 Cook Street.

The introduction of new stock will ease the pressure not only on availability but also rents. There has been significant rental inflation over recent times with premium rentals rising by up to 25% over the last three years, as new office builds set higher benchmark rents.

The fact that there will be a lift in space left behind by tenants on the move, is already seeing rental growth flattening with landlords having to become more proactive in order to drive rental appreciation. One approach which has proved successful is the reconfiguring of floor plates to provide for a greater number of small offices. An example of a building where this approach has been adopted and proved popular with new tenants is 55 Shorthand Street, owned by Robert Jones.

As reported elsewhere in this paper there has been a significant number of refurbishment and renovation projects undertaken over recent years. The lift in the standard of accommodation has increased the appeal of buildings and in many cases, such as the Tasman building in Anzac Avenue and 125 Queen Street, has resulted in a lift in the rental rates which can be achieved.

Consolidation a Favoured Option

As discussed above, a significant amount of tenant movement recorded across Auckland over recent months has been driven by the desire of organisations to bring operations, spread over multiple locations, together. Bringing staff together within modern office space brings a number of efficiencies. Modern design often means that organisations can accommodate staff within less space, thereby offsetting higher per m² rental rates.

With buildings within developments such as Goodman's VXV and Manson's 151 Victoria Street achieving five Star Greenstar ratings for design, occupation of new space allows companies to significantly improve sustainability.

Having the ability to house different departments in close proximity to each other promotes greater communication between teams further adding to productivity gains.

Office Consolidation

Organisation	New Primary Address	Precinct	Floor Space(m ²) *	Former Premises	Floor Space(m ²) *
Fonterra	109 Fanshawe	Wynyard Quarter	15,885	7-9 Princes Street + Others	17,960
Auckland Transport	20 Viaduct Harbour Ave	Viaduct Harbour	16,350	6 Henderson Valley Road + Others	21,200
Datacom	58 Gaunt Street	Wynyard Quarter	13,165	210 Federal Street + Others	11,330
NZME	4 Graham Street	Victoria Quarter	9,300	56 Albert Street / 54 Coojk Street	19,100
BDO	151 Victoria Street	Victoria Quarter	3,100	120 Albert Street	3,140
NZI	1 Fanshawe	Viaduct Harbour	7,280	Queen Street (151 and 131) + Others	9,360

* Approximate floor area

Source: Bayleys Research, Core Logic, Press reports, Company announcements

Precinct Review

Anzac Avenue

Vacancy has remained relatively flat increasing by just 50 basis points. Departures from lower grade space has slightly outpaced the impact of a take up of B grade space and the removal of inventory for refurbishment or conversion. Renovations such as at the Tasman Building, 16 Anzac Avenue, have met with increased tenant demand. The transition of lower grade office space to apartment use continues as illustrated by 29-31 Anzac Avenue which has been removed from the office inventory and marketed as "The Maritime".

Symonds Street Ridge

Vacancy fell for the third successive year, the result, predominantly, of significant uptake of space at 67 Symonds Street. Capacity has again fallen due to greater residential use within buildings zoned for commercial and residential use such as 38 Whitaker Place and 71 Symonds Street.

The education sector is the largest occupier of space within the precinct although there has been expansion of the legal, IT and communication industries.

Britomart

Having registered 0% vacancy in early 2016 a small amount of B and C grade space has become available in the recent past. Premium and A grade space remains fully occupied.

The most significant addition to the precinct's office inventory has been the reintroduction of the Australis Nathan Building following its renovation. The property is fully let having attracted tenants such as Duncan Cotterill.

The area is popular with companies operating within the property and digital design industries with there having been recent growth in the fashion, web based business and IT sectors.

Downtown

Vacancy within the CBD's largest precinct eased over the last 12 months despite a small increase in overall inventory a result of the reintroduction of space following renovation.

Vacancy within secondary grade space has increased slightly the result of the departure of tenants such as Meredith Connell and Anderson Lloyd to the Victoria Quarter and Britomart respectively.

Vacancy is set to increase over the next few months as space is reintroduced following refurbishment. The most significant contributors will be 125 Queen Street, BNZ building, and 138 Queen Street, ASB Building. Completion of these projects will see approximately 20,000m² of space return to market. Works at 125 Queen Street are now all but complete.

Midtown

Vacancy has fallen sharply over the last 12 months. A major factor being the uptake of space within 300 Queen Street. This is an excellent illustration of the lift in demand for B grade space resulting from the extreme lack of availability within prime grade premises. In addition vacancy within C grade space also fell sharply, approximately 33%.

The education sector, which has, for a number of years, been a strong influence within the precinct has seen its presence reinforced over recent months with the New Zealand School of Tourism taking space within 350 Queen Street.

Once again it is likely that the vacancy rate within Midtown has bottomed out with tenant movements already confirmed such as BDO's imminent move to the Victoria Quarter.

Western Peripheral

Having increased between early 2015 and 2016 the last 12 months has seen conditions tightening again with overall vacancy falling to just over 10%.

The decrease is, to some extent, the result of removal of space for refurbishment such as at West Plaza and Albert Plaza.

Vacancies within the ANZ Centre and Chorus House has seen A grade vacancy within the precinct increasing while, again, vacancy rates within C grade space have fallen, driven by an uptake of space from a large number of small occupiers.

Peripheral and Upper Queen

Vacancy within the Peripheral and Upper Queen precinct has fallen to its lowest level since July 2002.

The refurbishment and therefore temporary removal of 54 Cook Street (Radio Network Building) is partly responsible along with uptake of B grade Space. A grade space within the precinct is fully occupied.

The uptake of space within the precinct has, predominantly, been driven by business sectors already influential within the area such as education and administration. Examples being new occupation by the Northern Health School and expansion of the Defence Force within 385 Queen Street.

Quay Park

Being the smallest of the CBD office precincts vacancy figures within the area are relatively volatile given the significance of relatively small tenant movements.

As at this year's survey, the uptake of space on the eastern side of 32-34 Mahuhu Crescent, now fully leased, has offset the departure of House of Travel from 8 Tangihua Street and seen the overall vacancy rate fall to 6.34%.

Victoria Quarter

Vacancy has fallen to 6.75% from 10% a year ago despite an increase in the precinct's inventory.

The Victoria Quarter has been one of the favoured areas for development over recent years and has experienced significant growth. The total inventory within the precinct has grown from 89,400m² in 2011 to 112,000m² this year with the latest addition being Manson's development at 4 Graham Street / 151 Victoria Street. As a result of the high levels of recent development the precinct is dominated by higher grade buildings with Premium grade and A grade buildings making up approximately 63% of the area's inventory.

The higher grade buildings have attracted high profile occupiers, a trend which is ongoing illustrated by the recent addition of BDO and Pernod Ricard to the precinct's tenant list.

The appeal of the area will be further enhanced as a result of major infrastructure projects occurring within, and in proximity to it such as the International Convention Centre and Central Rail Link.

Viaduct Harbour

Vacancy within the precinct has remained stable over the last 12 months declining to 2.3% from 3.1%.

The next few months however will see the departure of Bayleys to the newly built Bayleys House in the Wynyard Quarter and Auckland Transport which will take occupation within Vodafone House once Vodafone's lease terminates. This will leave vacant space to be back filled at 4 Viaduct Harbour Avenue.

Wynyard Quarter

Vacancy within the precinct has remained unchanged over the last 12 months despite a sharp increase in inventory. The Wynyard quarter continues to see dynamic growth with the new Fonterra headquarters being completed and occupied over 2016.

2017 will see the completion of Bayleys House and Datacom House within Goodman's VVX development. These premises come to completion all but fully leased, just one floor within Datacom House is currently to be leased. Work within the Innovation precinct also continues apace with Innovation 5a to be completed in the second quarter of the year. These three properties will add approximately 31,000m² to the precinct's inventory taking total floor space to, just short of 100,000m². In early 2011 this figure stood at just over 27,000m².

Auckland CBD Commercial Offices Leasing Trends 2017

Precinct	Leasing Market		Market Rental (\$/m ²)		Outgoings (\$/m)		Carparks \$/pcpw
	Demand	Supply	Low - High	Trend	Low - High		
Viaduct Harbour							
Prime Quality	Steady	Sufficient	300 - 360	▼	220 - 280		100 - 120
Secondary Quality	Steady	Sufficient	200 - 250	▼	180 - 220		
Upper Queen St & Peripheral							
Prime Quality	Steady	Sufficient	200 - 250	►	75 - 95		60 - 80
Secondary Quality	Weak	Surplus	180 - 225	►	60 - 75		
Midtown							
Prime Quality	Strong	Shortage	280 - 375	►	80 - 120		120 - 145
Secondary Quality	Weak	Sufficient	160 - 200	►	75 - 100		
Symonds St Ridge							
Prime Quality	Strong	Shortage	220 - 250	►	85 - 105		55 - 70
Secondary Quality	Steady	Sufficient	180 - 205	►	75 - 85		
Downtown							
Premium Quality	Strong	Shortage	500 - 700	►	140 - 180		120 - 150
A-Grade Quality	Strong	Sufficient	300 - 550	►	100 - 125		
Secondary Quality	Steady	Shortage	270 - 400	►	65 - 100		
Anzac Ave							
Secondary Quality	Steady	Sufficient	170 - 300	►	45 - 100		55 - 70
Britomart							
Prime Quality	Strong	Shortage	450 - 600	▼	90 - 140		100 - 150
Secondary Quality	Strong	Shortage	300 - 400	►	100 - 140		
Western Peripheral							
Prime Quality	Steady	Shortage	350 - 550	►	95 - 150		80 - 110
Secondary Quality	Steady	Sufficient	260 - 350	►	60 - 90		
Quay Park							
Prime Quality	Steady	Sufficient	300 - 450	►	120 - 140		70 - 80
Secondary Quality	Steady	Sufficient	250 - 320	►	80 - 120		
Wynyard Quarter							
Prime Quality	Strong	Shortage	450 - 650	▲	100 - 150		100 - 120*
Secondary Quality	Steady	Shortage	250 - 350	►	80 - 150		
Victoria Quarter							
Prime Quality	Strong	Shortage	450 - 650	►	95 - 120		80 - 110
Secondary Quality	Steady	Shortage	250 - 350	▼	80 - 100		

NB: Net rent rates exclude GST and carparking costs. Outgoings inclusive of rates and ground rent where applicable
 Prime Quality = Premium and A-Grade accommodation
 Secondary Quality = B and C Grade accommodation

pcpw = per car per week
 All rates as at February 2017

SOURCE: BAYLEYS RESEARCH

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