

AEW RESEARCH

ASIA PACIFIC MARKET PERSPECTIVE

Q1 2017



Prepared by AEW Research, March 31, 2017

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Cover: Shanghai, China skyline

General Economic Overview

The most recent analysis by the International Monetary Fund (IMF) on the Asia Pacific economy (April 2017) highlighted that the outlook for the region was robust and “the strongest in the world” with recent data pointing to a pickup in momentum. They highlight the recent growth improvement from the largest economies in the region, as both China and Japan are benefiting from policy stimulus that is also flowing into other economies in Asia.

Exports have been a strong tailwind over recent quarters. A survey by Oxford Economics that was published in May 2017 indicated for the first time that a recovery in global trade was the biggest upside opportunity to the global economic outlook, replacing Trumps’ fiscal stimulus plan. The same forecaster has now raised their 2017 global trade growth outlook from 3.9% to 5.1%, reflecting the synchronized pick-up in trade volumes in several regions.

Forward-looking indicators such as the Purchasing Managers Index (PMI) suggest strength over the early part of 2017 will continue, and April’s PMI surveys pointed to an expansion in the Asia Pacific manufacturing sector across most of the region.

The positive start to the year has led many forecasters to raise their full year 2017 GDP growth outlook. The IMF now forecasts growth in the Asia Pacific region to be 5.5% for 2017, an improvement on both the previous forecast (5.3% as of October 2016) and last year’s growth of 5.3%. On the upside, growth momentum remains strong, particularly in advanced economies and in Asia. Additional policy stimulus, such as from U.S. fiscal policy, could provide further support to the outlook.

China is a large source of the latest momentum, where first quarter growth exceeded expectations. Chinese GDP growth accelerated to 6.9% year-on-year, from 6.8% in the fourth quarter of 2016. Export growth has turned positive, with Q1 2017 up 8.3% year-on-year in USD terms (versus a 4.5% decline in Q4 2016). Consumption continued to rebound over the first quarter and contributed 5.3 percentage points of the quarter’s growth (77% of GDP growth, an increase on Q1 2016’s 75%). This rebound is being driven by solid disposable income growth, moderate property tightening and a recovery of high-end sales and strong online sales. The Bloomberg consensus outlook for GDP growth is 6.6% in 2017 with modest CPI inflation of 2% and retail sales growth 10.4% (May 2017).

After weakening against the USD during the second half of 2016, the CNY has been stable over the early part of 2017 as capital outflow has stabilized. Similarly, the SGD has been stable as well, albeit with a slight appreciation bias over the early months of 2017. The KRW and AUD have been comparatively more changeable. Over the first two months of the year both appreciated against the dollar. Since the end of March, the AUD has given back most of these gains while the KRW has been more stable, trading within a reasonably tight range.

Monetary policy is predominantly accommodative in the gateway markets of the region. The Peoples Bank of China (PBOC) is the only significant bank with an effective tightening bias as they endeavor to both focus on financial market stability while providing the market necessary liquidity. The Bank of Korea (BOK) and Reserve Bank of Australia (RBA) both have policy rates at record lows. The Monetary Authority of Singapore (MAS) is maintaining a neutral policy setting.

Office occupational demand has been robust and retail demand drivers continue to be steady. Investment demand is high and intentions for further allocation are strong.

Property Market

The occupier markets in the regions gateway cities continue to be well balanced. The only new office construction during the quarter was in Shanghai. Seoul, Hong Kong and Singapore had no new completions while Sydney's CDB had a small amount of refurbished space return to the market. The average office vacancy rate of the Fund's five target markets was 8.4% at the end of the quarter and has been between 8.0% and 8.5% for three consecutive quarters. Hong Kong Island continues to stand out with a vacancy rate of 2.2%, in a market of close to 50 million square feet.

Contributing to this steady vacancy environment, office occupational demand has been robust. Net absorption has improved in each of the previous four quarters. Demand was strongest in Shanghai as occupiers expanded into some of the recent construction. Seoul also had a strong first quarter, building on gains made during the final quarter of last year. Demand is coming from tech-related firms, including co-working firms who are expanding aggressively, as well as professional service firms.

In the retail sector the demand drivers of previous quarters remain largely intact. Food and Beverage (F&B) and mid/mass market fashion are key occupier categories across markets. Conditions are generally tempered though as consumer sentiment and retail sales are challenged by elevated levels of uncertainty, which has tended to make consumers a little cautious.

Demand for high-end residential units remains strong but restrained by demand-side restrictions that have been in place for several years. There are currently no clear indications when some of these restrictions will be lifted.

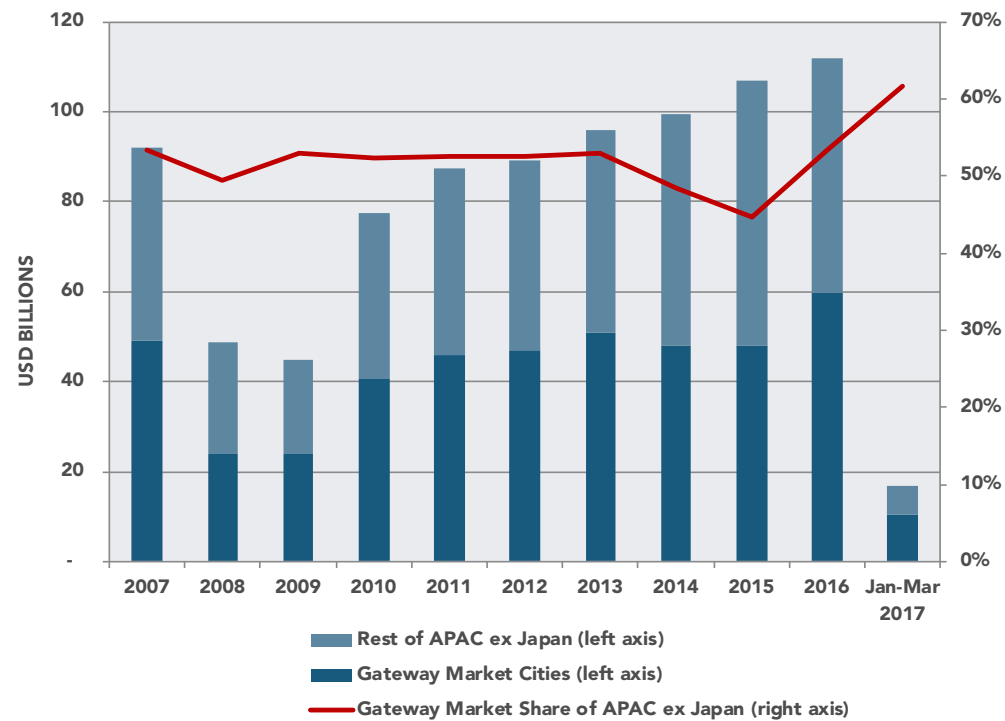
Investment demand for income-producing real estate in gateway cities remains high. Allocations to real estate continue to be below targets, investment intentions are strong and there was a large amount of capital raised in 2016 to be allocated to real estate globally and in the Asia Pacific region.

On a 12-month rolling basis, USD transaction volumes in the Fund's target markets were flat quarter-on-quarter, a slightly better result than the 3% contraction of overall Asia Pacific volumes. Hong Kong transaction activity fell 11%, as did Sydney's (down 9% quarter-on-quarter). In Singapore several large transactions during Q1 2017 helped to push volumes up 17% and in Seoul volumes were up 11% quarter-on-quarter. Shanghai transaction activity was unchanged over the quarter.

Four of the five largest sales in the Fund's target markets during the first four months of year were in Singapore. The largest was the Blackrock disposition of Asia Square Tower 2 (office) in Singapore to CapitaLand at a reported yield of about 3.5% (USD 1.9 billion, USD 2,480 per square foot). This sale follows the June 2016 sale of the adjacent but larger Tower 1 to the Qatar Investment Authority (USD 2.5 billion, USD 1,925 per square foot, about 3% yield).

Other sales in the top five included Singapore's Jurong Point, a regional shopping center (USD 1.6 billion, USD 1,574 per square foot); TripleOne Somerset, an office building in Singapore's Orchard Road district (USD 892 million, USD 1,577 per square foot, yield approximately 3%); Garden Square, an office building in Shanghai's Puxi CBD (USD 570 million, USD 946 per square foot) and the PWC Building in Singapore's CBD (USD 528 million, USD 1,484 million, yield approximately 3%).

GATEWAY MARKET TRANSACTION VOLUME



Source: RCA

Hong Kong

KEY REAL ESTATE INDICATORS

	VACANCY RATE		RENTS	ABSORPTION	COMPLETIONS	CAP RATES
Office (CBD)	1.5%	↓	↑	↓	↔	↔
Retail (Shopping)	1.8%	↑	↓	↑	↑	↔
Residential	3.8% ^A	↑ ^A	↑	↑ ^A	↑ ^A	↔

^A As at December 2016, the latest period reported

Source: JLL, Hong Kong Rating and Valuation Department

Note: For the vacancy rate, rents and cap rates the arrows reflect the trend for the current quarter compared with the comparable quarter one year earlier. For absorption and completions the arrows reflect the 12-months through to Q1 2017 trend compared with the 12 months through to end Q1 2016. For vacancy rates, a down arrow indicates declining vacancy rates or an improvement in market fundamentals. For cap rates, a down arrow indicates lower cap rates.

An improvement in global demand and further stabilization of the Mainland economy has been benefiting Hong Kong's economy. The economy continued to expand over the first quarter with solid export and import growth in the first few months of the year, indicating good tailwind momentum in both external and domestic demand.

Expectations are for domestic demand to outpace external demand this year as residential property prices are high, inflation is subdued and healthy job conditions are forecast to underpin household wealth and consumption. Imports continue to outperform exports, indicating the strength of the local economy as well. At the same time, the slightly negative net trade position will act as a small drag on overall growth this year.

First quarter growth accelerated to 3.6% year-on-year and full year growth is forecast to be 2.2% this year, an improvement from 2016's 1.9%. CPI inflation is forecast to fall from last years 2.4% to 2% in 2017.

In late March Beijing-backed Carrie Lam was elected Hong Kong's new Chief Executive. She will officially take office on 1 July, the 20th anniversary of the city's handover from Britain to China for a term of five years.

Although the U.S. Federal Reserve has been gradually raising their policy, the overnight HIBOR has remained very low, under 0.1% for most of the year so far, due to a large amount of liquidity in Hong Kong's interbank market. However, over time the market continues to expect a gradual increase in the HIBOR as U.S. interest rates continue rise.

Demand for grade A office space across the city recovered over the first quarter, with net absorption rising 166,000 square feet, the first increase in occupied space in a year. With Central's vacancy rate at 1.5%, decentralization continues to gather pace, with Hong Kong East one of the main beneficiaries. This submarket will also benefit from the planned closure, demolition and redevelopment of Cornwall House (151,600 square feet) in Q2 2017. This is part of the Swire Taikoo redevelopment project that will create about 2 million square feet of grade A office space. Capital values and pricing continues to be supported by this medium-term demand supply imbalance, particularly in Central where it is very challenging to create additional supply. Competition among banks has kept debt funding costs low, supporting expectations of further gains.

There were no new completions during the quarter in Hong Kong's office market and vacancy rates across the sector generally continue to decline.

There were no new completions during the quarter in Hong Kong's office market and vacancy rates across the sector generally continue to decline. Rent's continued to grow during the quarter, albeit at a slightly slower rate of growth. Overall rents were up 0.8% quarter-on-quarter and Central rents rose 2% quarter-on-quarter.

Hong Kong's inbound tourism market is showing signs of recovery with visitor arrivals increasing 1.4% year-on-year in January and February. This compares to a slight fall of 0.4% year-on-year in the previous quarter, Q4 2016. Mainland Chinese arrivals rose 1.1% year-on-year over the same 2017 period and visitors from countries other than China grew 2.5% year-on-year.

This rise in tourism and the previously mentioned robust household wealth and consumption has helped to reverse the slump in retail sales. After two years of consistent declines, year-on-year retail sales rose in March 2017, up 3.1%. After posting a small year-on-year increase in February, the Jewelry and Watches category rose further in March, up 8.4%. Nonetheless, on a 12-month rolling basis, this category is down about 40% from its peak.

High street rents, which were highly exposed to this type of high-end retailer, followed suit, falling 40% from their mid 2014 peak. As retail sales conditions improve, the forecast is for high street rents to stabilize over the remainder of 2017, before starting to rise again over 2018 and beyond. AEW believes it is an interesting investment theme to target the high-street retail market at this point of the cycle. Re/leasing will be to active fashion retailers, such as Nike, Reebok or Adidas, who have been focusing on extending their presence in Hong Kong.

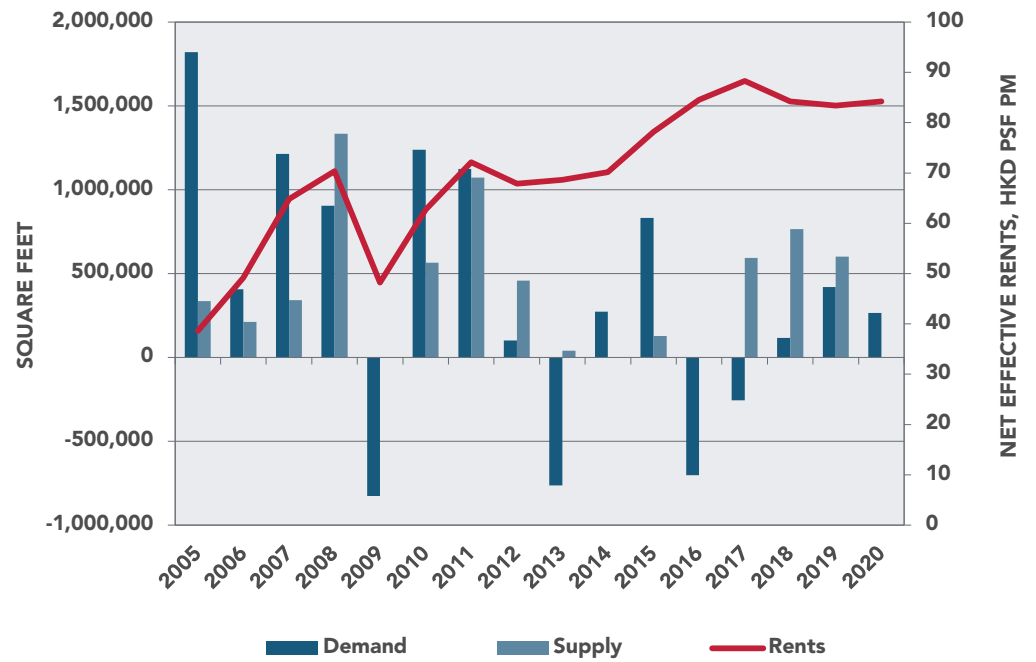
After a small correction over the fourth quarter of 2015 and first quarter of 2016, pricing in the residential sector has rebounded 18% from the March 2016 trough. Buyers, particularly in the high-end of the market, have been undeterred by the 15% stamp duty imposed on residential transactions. The duty was imposed in November 2016 on all residential transactions to quell the rise. In this high-end market, the focus remains on the primary sales market, however record prices are being set for irreplaceable units in prime locations.

The investment market remains strong, backed up by the high levels of liquidity in Hong Kong's monetary system, plus steady demand from mainland investors. Although transaction volumes were 11% lower at the end of the quarter (on a 12-month rolling basis), pricing remains firm with capital values rising faster than rents.

Market spot yields were slightly lower as a result. Strong investor sentiment is being underpinned by record high prices being achieved in the strata-titled office and land sale markets.

The Murray Road Carpark tender, the first grade A commercial site to be sold in Central in 20-years (as reported by the South China Morning Post, 17 March 2017), was highly anticipated and has been reported to be sold for USD 50,500 per square foot (USD 6,500 per square foot). The tender was won by a local developer, Henderson Land, with an estimated 3% yield on cost (JP Morgan, May 16).

HONG KONG ISLAND DEMAND, SUPPLY AND RENTAL OUTLOOK



Source: JLL

Singapore

KEY REAL ESTATE INDICATORS

	VACANCY RATE		RENTS	ABSORPTION	COMPLETIONS	CAP RATES
Office (CBD)	5.9%	↔	↓	↑	↑	↔
Retail (Shopping Center)	3.8%	↔	↓	↑	↓	↔
Residential	8.9%	↔	↔	↑	↑	↔

Source: JLL, Singapore Urban Redevelopment Authority

Note: For the vacancy rate, rents and cap rates the arrows reflect the trend for the current quarter compared with the comparable quarter one year earlier. For absorption and completions the arrows reflect the 12-months through to Q1 2017 trend compared with the 12 months through to end Q1 2016. For vacancy rates, a down arrow indicates declining vacancy rates or an improvement in market fundamentals. For cap rates, a down arrow indicates lower cap rates.

Based on advance estimates, the Singapore economy grew by 2.5% on a year-on-year basis in the first quarter of 2017, easing from the 2.9% growth in the previous quarter. A cyclical recovery in global trade will continue to support exports and help underpin a pick-up in services during 2017. The external sector is the most active at the moment with domestic demand challenged by the housing market correction and a soft labor market. Reflecting stronger exports full-year GDP forecasts have been raised to 2.7%, from 2.4% previously.

On the macro policy front fiscal spending will be mildly stimulatory following the Budget's announcement that several infrastructure projects will be brought forward. As expected, the MAS left its policy of zero appreciation in the SGD Nominal Effective Exchange Rate (NEER) unchanged at its April bi-annual monetary policy meeting. Monetary policy settings will likely stay unchanged through 2017 and the early part of 2018, after which the MAS is expected to return to its gradual appreciation bias.

The Singapore CBD office sector is close to the end of the current grade A supply cycle. There will be two office completions this year. The redevelopment of UIC Building (285,000 square feet) is anticipated to finish by mid-year, as will the newly built Marina One (1,880,000 square feet). Local news reports have suggested Marine One is more than 60% pre-leased, representing about 1 million square feet of activity. Earlier in the year it was reported Facebook would take up about 13% of the total NLA. Other tenants include PWC and the Swiss private bank Julius Baer in addition to Bank of Tokyo-Mitsubishi UFJ (BTMU), the first tenant to sign on to the project.

Of note, co-working space is becoming a large occupier of office space in Singapore taking up space in grade A building such as Marina One, OUE Downtown Gallery and UIC Building. According to CBRE Research, the amount of co-working space will increase from about 400,000 square feet at the end of last year to 700,000 square feet by end-2017. Users of this co-working space are tending to be corporate. For example, Australian-listed property group Lendlease will be moving 100 workers in its Asia-Pacific headquarters, including its CEO for Asia, to the co-working space at The Work Project at OUE Downtown Gallery.

The CBD vacancy rate remains low, at 6% in Q1 2017, even though the market is close to the end of a supply cycle. Forecasts continue to be for the vacancy rate to rise to about 11-12% by the end of the year, however the success landlords have at backfilling space vacated by upgrading tenants will determine the extent to which conditions change. Beyond 2017, forecasts are for vacancy to be flat over 2018 before falling in 2019 and 2020.

Rents will likely follow a similar path as vacancy. After falling 20% in the CBD, and 27% in the Marina Bay district which is dominated by prime buildings, rental declines will likely slow over the balance of 2017 before recovering in 2018.

AEW believes the Singapore office sector will be presenting an interesting entry point to access a sector that is consistently in demand from investors due to its high transparency and positive long-term outlook built on the good governance from the Government.

Retail sales rose 2.1% in March from a year earlier, recovering from a revised 2.6% fall in February, according to data from the Department of Statistics. Sales without motor vehicles, whose turnover rose by 6.9%, were up by a smaller 0.7% year-on-year. Sales activity has been held back by a challenging labor market, a fall in house prices and a dip in sentiment.

Retail rents have corrected about 11% from March 2015, declining at a rate of about 1.5% every quarter. In Q1 2017 rents were down 0.9% quarter-on-quarter. Leasing activity during the quarter was tepid as both retailer's and consumer sentiment remaining largely cautious.

A few new international retailers entered the market during the quarter, mostly in the F&B space. There was also activity in the health and beauty sector. Lastly, demand for physical retail space is being challenged as retailers focus on building out their e-commerce capability and evaluate their store requirements over the medium term.

Residential prices have been correcting for several years as supply has built and demand-side restrictions held back activity. Pricing was down 2.8% year-on-year in March bring the peak to trough fall to 12%. Initial market speculation was the government would target a price fall of about 10-12%. There are no signs at the moment of any pending relaxation of the demand restrictions in place but as incomes have risen as prices fell, affordability has increased significantly.

High-end residential prices in central locations have incrementally increased since the middle of 2016. Over Q1 2017, prices were mostly flat but full year forecasts estimate pricing could increase between 4% and 6%.

As highlighted earlier, Singapore saw a number of large investment deals close during the quarter, led by the sale of the landmark Asia Square Tower 2 (USD 1.9 billion, USD 2,480 per square foot). Also of note was the sale of Jurong Point (USD 1.6 billion, USD 1,574 per square foot), a large suburban shopping center, an estimate yield of 4.2%.

Subsequent to the end of the quarter a 50% interest in One George Street was reported to have been transacted. CapitaLand Commercial Trust (CCT), a Singapore listed REIT, divested the interest for about USD 846 million (USD 1,890 per square foot) which represents a yield of about 3.2%. The momentum in the investment market is likely to be maintained.

SINGAPORE CBD DEMAND, SUPPLY AND RENTAL OUTLOOK



Source: JLL

Seoul

KEY REAL ESTATE INDICATORS

	VACANCY RATE		RENTS	ABSORPTION	COMPLETIONS	CAP RATES
Office (Overall)	10.8%	↔	↑	↑	↑	↔
Office (CBD)	13.4%	↔	↑	↑	↔	↔
Office (Yeouido)	13.6%	↔	↔	↑	↔	↔
Office (Gangnam)	6.4%	↔	↑	↑	↑	↔

Source: JLL

Note: For the vacancy rate, rents and cap rates the arrows reflect the trend for the current quarter compared with the comparable quarter one year earlier. For absorption and completions the arrows reflect the 12-months through to Q1 2017 trend compared with the 12 months through to end Q1 2016. For vacancy rates, a down arrow indicates declining vacancy rates or an improvement in market fundamentals. For cap rates, a down arrow indicates lower cap rates.

Overall net office demand has picked up and the vacancy rate fell in all three submarkets.

The Korean economy grew by a stronger than anticipated 0.9% quarter-on-quarter in Q1 2017. Growth was underpinned by a recovery in exports and investment. As with other economies, the faster than expected pick up in external demand prompted an upgrade to the short-term forecast. Growth in 2017 is now expected to reach 2.5%, 0.2 percentage points higher than previous estimates.

Moon Jae-in of the liberal Demographic Party was elected President on May 10th by a significant margin. Moon's victory brings to an end a decade of conservative rule and a change in political and economic ideology. Moon campaigned on a range of policies including job creation, shaking up the family-owned conglomerates that dominate the Korean economy and bringing stability back to the Korean peninsula by re-establishing diplomatic and economic ties with Pyongyang. Observers anticipate the new president will implement an approximately USD 8.8 billion stimulus package, accelerating fiscal spending.

While the external sector has been a welcome demand push factor for an economy where domestic demand has been muted, the deployment of the missile defensive system THAAD created a negative response from China. Tour groups to Korea were banned and Korean retailers operating in China saw a meaningful fall in sales revenue.

The BOK is expected to continue its easing bias through 2017 at least. The BOK has left the policy rate unchanged since June 2016, when it was lowered by 25 basis points to 1.25%, a record low. Expectations are for no further cuts. The Bank will look to balance a recovery in external demand that is still in its infancy, soft private consumption, geopolitical tensions and high levels of household debt which could be exaggerated further by reducing interest rates even more.

Overall net office demand in the three main submarkets of Seoul was about 300,000 square feet in Q1 2017, a pick up from one year when Q1 2016 net demand was negative. The vacancy rate fell in each of the three submarkets, led by the CBD where it decreased 165 basis points to 13.4%. The overall vacancy rate is 10.8% (YBD 13.6%, GDB 6.4%). New business expansion is coming from the IT sector, assisting this fall in vacancy. There continues to be relocation activity from conglomerates, especially Samsung entities.

During the quarter three new buildings were completed. In the CBD, SK D&D, South Korean real estate developer, completed their extensive refurbishment of Soosong Square. The building is scheduled to be fully occupied by SK E&C during the second quarter. In the Jamsil sub-district

Both the leasing and investment markets are competitive.

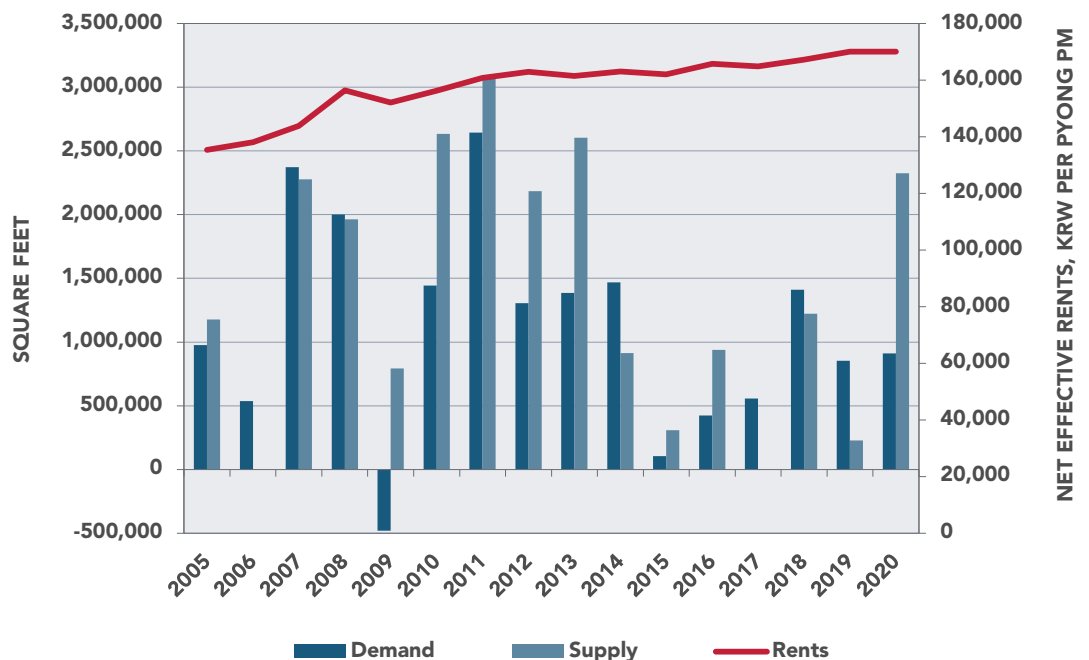
Lotte World Tower completed in February. A little more than 30% of the approximately 1.5 million square feet of office GFA is currently occupied by Lotte affiliates. Another 12% has been leased to a third party tenant, Descente Korea. The third building completed during the quarter was the grade B K Tower which is 80% committed to SK Securities, HP and Mirae Asset Life Insurance.

The leasing market remains competitive. Landlords whose buildings have lingering vacancy are using incentive packages to make their properties more attractive to tenants. Grade A net effective rents in the CBD and YBD adjusted 1.7% quarter-on-quarter and 4.5% quarter-on-quarter. Gangnam is the more stable of the three core submarkets. Net effective rents increased 1.3% quarter-on-quarter in Q1 2017.

The rental decline the CBD was led by three buildings recently acquired by Booyoung, all of which have sizeable vacancies. Rents also declined at Signature Tower and Pine Avenue 101, both of which have pending vacancies of around 50%. At the same time though, there were several examples of landlords with high or stable occupancy buildings who were able to increase rents. Similarly, in the GBD there were examples of buildings who removed rent incentives due to their high and stable occupancy (e.g. Posco Center, SI Tower and Gangnam Finance Center).

The investment market remains active in Seoul. On a 12-month rolling basis USD investment volumes rose 11% in Seoul with office sales heavily dominating activity. Both domestic and international investors have been active, with many transactions involving some degree of vacancy risk. The largest sale during the quarter was the purchase of Susong Tower by Morgan Stanley related entities (USD 330 million, USD 687 per square foot). PGIM purchased T Tower, a CBD grade B office asset for approximately USD 155 million (USD 347 per square foot). T Tower was purchased with a degree of vacancy. IGIS Asset Management purchased Samsung Taepyeongno Building on behalf of domestic capital for USD 190 million (USD 442 per square foot). Following the relocation of Samsung Life Insurance (the previous owner) the asset now has a significant amount of space to lease.

SEOUL DEMAND, SUPPLY AND RENTAL GROWTH OUTLOOK



Source: JLL

Shanghai

KEY REAL ESTATE INDICATORS

	VACANCY RATE		RENTS	ABSORPTION	COMPLETIONS	CAP RATES
Office (CBD)	12.6%	↑	↔	↓	↑	↔
Office (CBD - Puxi)	12.1%	↑	↔	↓	↑	↔
Office (CBD - Pudong)	13.1%	↑	↑	↑	↑	↔

Source: JLL

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Shanghai's GDP grew 6.8% year-on-year in the first quarter of 2017, a better than expected performance due to a recovery of industrial output and the sustained growth of the service sector. Service sectors, including finance, shipping, and consultancy, contributed some 70.7% to Shanghai's economic growth according to the Shanghai Statistics Bureau.

After the introduction of policies to limit speculation in the residential sector, transaction volumes have fallen dramatically. Transactions of new homes in Shanghai dropped 67.2% while transactions of pre-owned homes dropped 72%. Pricing has stabilized with the average home price down 0.1% month-on-month in March.

Demand for office space in Shanghai remains very high. In the CBD net absorption was 1.7 million square feet in Q1 2017, bringing the total amount of space taken up from Q2 2016 to Q1 2017 to almost 2.3 million square feet. There was an additional 3.7 million square feet of net absorption in decentralized locations during this same time period. Because this high level of demand has been sustained for a number of years, a supply response was expected.

New construction in 2017 is expected to peak at about 7.1 million square feet in the CBD and 12 million square feet in decentralized locations. Leasing activity in this new supply is robust however as it completes, vacancy rates are forecast to rise.

In the CBD, supply over Q1 2017 was 3.8 million square feet, about 54% of the total supply anticipated during the full year. This supply was led by Shanghai Tower, a super skyscraper in the Pudong District that completed with 50% occupancy. As a result of this new supply, the CBD's vacancy rate rose from 8.6% at the beginning of the year to 12.3% at the end of the first quarter.

In the decentralized market, supply was more even, with about 3.2 million square feet entering over Q1 2017, approximately 27% of the full year supply. The vacancy rate in this market rose from 18% to 23% during the quarter.

Although supply was greater than demand over the quarter, leasing competition in existing buildings helped overall CBD rents to remain flat during the quarter. Landlords of prime office buildings, with low vacancy, in Pudong's CBD continued to push rents up, helping the overall district rental index to rise 1.7% quarter-on-quarter. Puxi landlords are more conservative and have been more flexible on rental negotiations. Rents in Puxi were flat over the quarter.

Shanghai's retail sales grew 7.8% year-on-year in Q1 2017, a marginal decline from the 8% year-on-year growth in Q4 2016. Growth in sales activity is consistent with the continued growth in the service and consumption sectors over recent years.

Demand for office space remains very high while the investment market is very active.

F&B retailers continue to drive most of the leasing activity in shopping centers. Many of these operators have collaborated with mobile takeaway platforms to expand rapidly throughout the city. Brands can use mobile base marketing strategies to carve out a niche and drive increases in footfall.

In addition to the expansion of F&B, fitness centers, sportswear brands and tenants related to healthy lifestyles continue to expand as well. International sports brands such as Nike and Polo Sport have been active in recent quarters – both opened more than five stores in the past two quarters. Gyms have emerged as a ‘must-have’ large format tenant in many medium- to large-scale shopping centers.

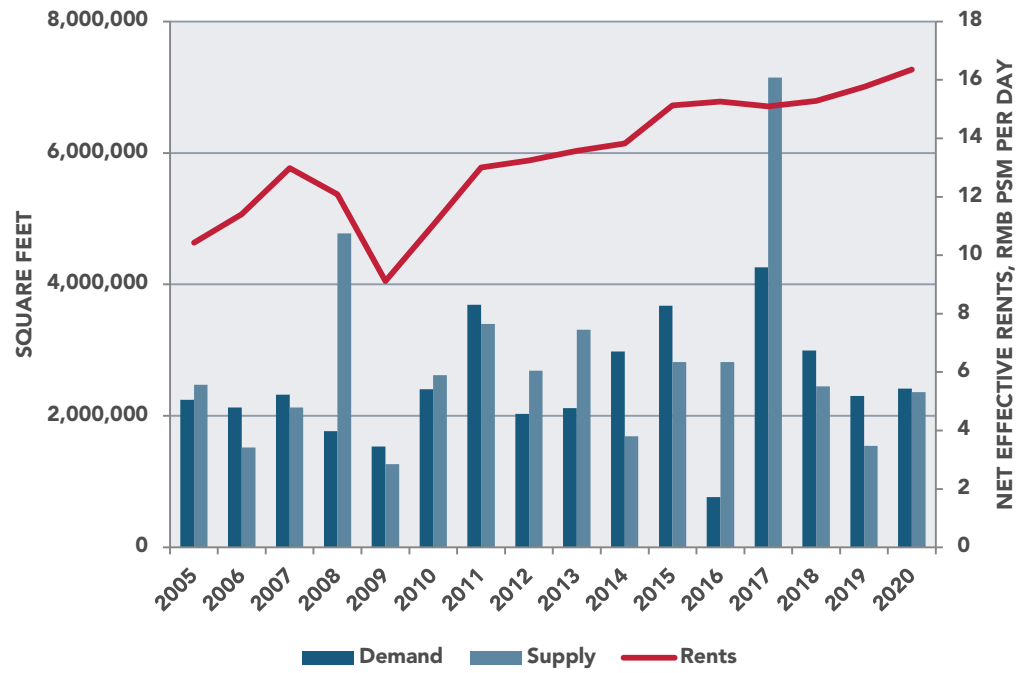
Demand drivers for the rest of 2017 are to remain similar to those in the latter half of 2016, with strong expansion demand expected from F&B, health and experience-oriented brands (including those targeting children). Many landlords see these types of tenants are key foot traffic generators. It is also possible there will be more online and offline integration.

While new supply during the first quarter was much lower than the final quarter of 2016, supply this year is anticipated to be high. In Q1 2017 slightly less than 800,000 square feet was completed while forecasts for full year 2017 are about 10.6 million square feet. Demand forecasts are strong, with take up of about 8.9 million square feet this year, but as supply is exceeding demand, the vacancy rate is anticipated to increase. It was 9.8% in Q1 2017, and by the end of the year it is forecast to be 10.5%.

Shanghai’s investment market was very stable at high levels over Q1 2017. The volume of income-producing transactions has been steadily increasing over many years. In the 12-months ending March 2017, about USD 15.2 billion was transacted in Shanghai, the second busiest annual period recorded. Volumes have grown from between USD 6 to 10 billion per 12-month period in 2009 to 2013, to now regularly ranging between USD 10 and 15 billion per 12-month period in 2015 to 2017.

This activity is driven by several factors. Shanghai has developed as a center of commerce and China’s financial capital over the past decade. Real estate transparency has improved, new sources of domestic capital are now able to invest into the real estate sector (for example insurance firms) and foreign capital is increasingly seeing the market as an equal gateway market when compared to other key cities in the Asia Pacific region.

SHANGHAI CBD DEMAND, SUPPLY AND RENTAL OUTLOOK



Source: JLL

Sydney

KEY REAL ESTATE INDICATORS

	VACANCY RATE		RENTS	ABSORPTION	COMPLETIONS	CAP RATES
Sydney CBD (prime)	8.1%	↑	↑	↓	↑	↔

Source: JLL

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Recent data from Australia are supporting the view momentum in the economy remains solid. Goods exports have benefited from an improvement in the global economy, with robust demand from China supporting exports volumes and commodity prices. The weaker AUD has also made Australia services exports, such as tourism and education, more attractive.

Domestic conditions are showing some weakness. Retail sales growth has been trending down for several years and March's 2.1% year-on-year growth is the slowest increase since mid 2013. Expectations are for consumer spending growth to be subdued going forward with households constrained by slow growth in employment (particularly full-time employment) and wages.

That said, positive external conditions, expansionary business confidence and a trade balance still in surplus have led to a GDP growth forecast of 2.8% this year, an improvement from last years 2.5%. CPI inflation is anticipated to remain low at about 2.1% for 2017. This is in the lower half of the RBA target range of 2% to 3%. Low inflation combined with an economy operating below capacity, expectations are for the RBA to have a weakening bias. Certainly, if the labor market weakens further, they may decide to cut the cash rate again, to 1.25%.

Occupier demand remained strong across the Sydney CBD office market in Q1 2017. Demand for space was broad based, with multiple industry sectors active in taking space. About 250,000 square feet of prime space was taken up during the quarter, lowering the prime vacancy rate to 8.1%. The average vacancy rate since the beginning of 2015 has also been 8.1%, despite prime office stock rising 13% during the same period, indicating a strong take up of new construction as it complete's.

In the secondary market, conditions continue to be highly landlord favorable. Occupier demand remains strong but demand indicators are being distorted by the withdrawal of stock. About 184,000 square feet was withdrawn from stock during the quarter, spread across four buildings in each of the Core, Midtown, South and Western Corridor precincts. This brings the total amount of stock withdrawn from the market in the past 12-months (Q2 2016 to Q1 2017) to slightly more than 1.5 million square feet. Whereas prime stock has grown over recent years, secondary stock has contracted 6% in the past year.

Vacancy rates in the secondary market are tight at slightly less than 6%, more than two percentage points below the ten-year average.

The rental market is reflecting these positive physical market fundamentals. Prime gross effective rents increased by a strong 7.3% quarter-on-quarter, improving year-on-year growth to 23%. A reduction in incentives is the primary driver of this. Prime incentives have fallen from a peak

of more than 30% in early 2015, to 22% in Q1 2017. And the momentum continues to build, incentives fell 2.8 percentage points in Q1 2017 after contracting 2 percentage points in Q4 2016.

Similar to the prime market, rents in the secondary market continue to reflect the favorable landlord conditions. Secondary gross effective rents were up 5% quarter-on-quarter in Q1 2017, due, again, in large part to the fall in incentives. At 19% this is the lowest they have been since late 2008. AEW is aware of the secondary leases being renewed with incentives much lower than this level, in the low double digits.

Similar to the national trend, New South Wales (NSW) retail turnover has been moderating for some time but continues to be one of Australia's strongest retail markets. Seasonally-adjusted retail turnover in NSW increased by 4.0% year-on-year in the 12 months to February 2017 and is 1.5 percentage points below the five-year monthly average growth rate (5.5% year-on-year), according to the Australian Bureau of Statistics (ABS).

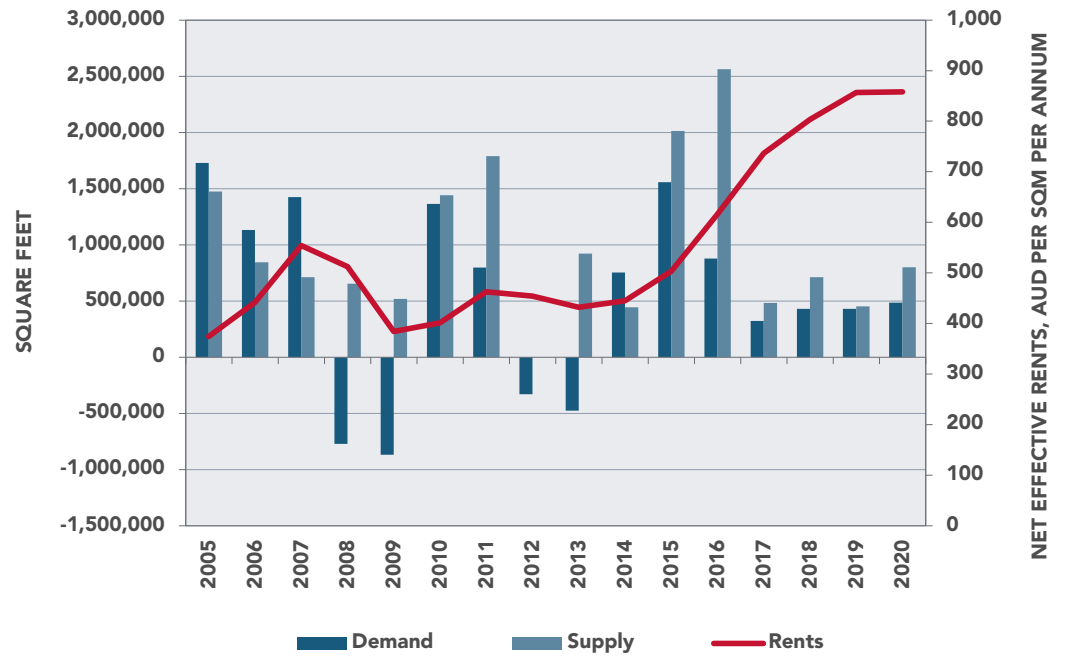
The online retail market continues to expand with more retailers adopting a digital platform to broaden their customer reach and build brand awareness. Retailers with an existing store network are building capabilities to link their online presence with their physical stores. In addition, there continues to demand from international and domestic luxury brands in Sydney CBD and NSW. Van Cleef opened their first Sydney store in the first quarter and Tiffany and Co. secured a new flagship location after the building they were in was compulsorily acquired for the new metro train line.

Investment enquiry and sentiment remains strong for Sydney office assets. However, only two office assets transacted in Q1 2017. Heathley Diversified Property Fund divested two assets, 8 Spring Street (USD 49 million, USD 914 per square foot) and 56 Clarence St (USD 45 million, USD 810 per square foot). Local media reported the buildings sold at passing yields under 5%.

The low number of transactions is, in part, attributed to seasonal factors, with the first quarter typically more subdued. During April, activity picked up with two significant office assets reported sold. 20 Bridge Street was sold by Investa Property Group, on behalf Malaysia's second largest pension fund Kumpulan Wang Persaraan for a reported record yield, for a property of this size, of 4% to 4.5% (USD 262 million, USD 1,223 per square foot).

Sydney Plaza also transacted in April, (USD 121 million, USD 573 per square foot). This building is on the southern edge of the CBD and was exchanged between two offshore, Singapore based firms; Roxy-Pacific sold to Far East Organisation.

SYDNEY CBD DEMAND, SUPPLY AND RENTAL OUTLOOK



Source: JLL

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