

AEW RESEARCH

ASIA PACIFIC MARKET PERSPECTIVE

Q1 2018



Prepared by AEW Research, March 2018

This material is intended for information purposes only and does not constitute investment advice or a recommendation. The information and opinions contained in the material have been compiled or arrived at based upon information obtained from sources believed to be reliable, but we do not guarantee its accuracy, completeness or fairness. Opinions expressed reflect prevailing market conditions and are subject to change. Neither this material, nor any of its contents, may be used for any purpose without the consent and knowledge of AEW.

General Economic Overview

Regional growth is holding up well, aided by a robust external sector and strong domestic demand. Most PMI's are expansionary (above 50) indicating a strong manufacturing sector and export data remains positive. For example, Korea's April USD merchandise exports (excluding shipping) rose 10.4% year-on-year, up from 8.4% in March. Most forecasts anticipate slower trade volume growth as the year progresses due in part to higher base effects as well as a slight softening of global conditions.

Across gateway markets in Asia, business and consumer sentiment is mostly positive. Conditions are supportive for businesses to invest in their operations and forecasts are for private sector investment growth to pick up momentum in 2018 compared to 2017. The average growth rate across the major economies in Asia is 4.75% this year, versus 2.96% last year. China will lead this turn around.

Inflation pressures came under control and forecasts are for CPI rates to remain under or within target ranges this year. As a result some Central Banks will be looking to adjust policy settings, taking advantage of this period of good growth and low consumer price increase. For example the Monetary Authority of Singapore slightly tightened their policy setting at their April 2018 meeting. China is undertaking counter cycle actions at the moment, lowering the Reserve Requirement Ratios by 100 basis points to increase banking liquidity as a way of supporting domestic growth.

Over the first quarter, Asian currencies generally strengthened against the USD. Some of this USD weakness is related to short rates adjusting and U.S. Federal Reserve slightly tightening liquidity. Since the end of the quarter there has been a period of USD strength, bringing most Asian currencies back to levels they were close to at the beginning of the year.

MACROECONOMIC INDICATOR SUMMARY

Countries	GDP (y-o-y)		CPI (y-o-y)		Interbank rate/cash rate		USD exchange rate	
Year	2018	2019	2018	2019	2018	2019	2018	2019
Australia	2.74	2.57	2.36	2.40	1.50	1.75	0.77	0.77
China	6.42	6.02	2.37	2.60	3.09	3.40	6.20	6.16
Hong Kong	3.01	2.48	2.32	1.91	2.75	3.50	7.82	7.78
Singapore	3.04	2.40	0.77	1.78	1.81	2.56	1.33	1.34
S. Korea	2.79	2.60	1.60	1.96	1.75	2.25	1058	1050

Source: Oxford Economics

On a 12 month rolling basis, USD transaction volume (income-producing assets only) across major gateway cities were up 11%; the strongest increases were seen in Hong Kong (+89%) and Singapore (+20%), pulled up by several large transactions.

Property Market

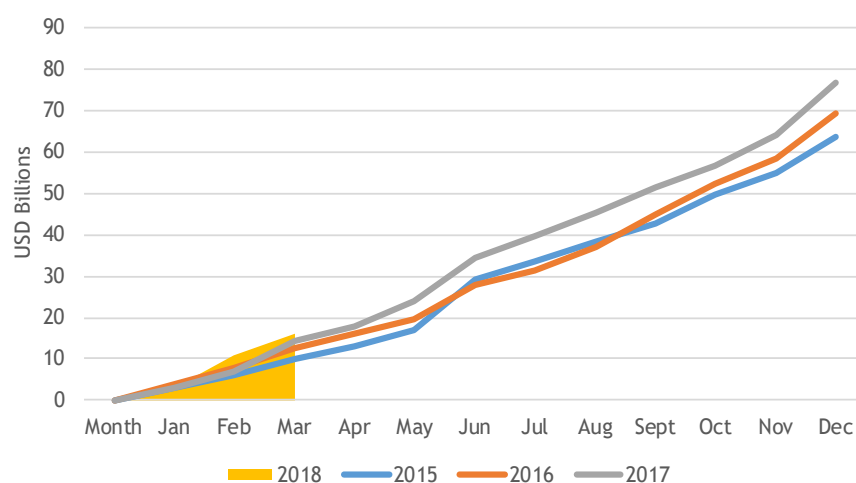
Income-producing property continues to be an attractive asset class. There remains a good spread over 10-year bond yields and opportunities to improve income by taking advantage of landlord favorable rental cycles (Australia, Singapore, Hong Kong, Shanghai) or selecting assets with improvement potential through repositioning or refurbishment. Podium retail conversion is an attractive strategy in locations with high footfall and good exposure.

In Q1, transaction volume was \$16.1 billion across major gateway cities, of which close to 50% was attributed to transactions in Hong Kong. Volume in Hong Kong was pulled up by two large transactions – LINK REIT neighborhood mall portfolio sale and 18 King Wah Rd office, which cumulatively amounted to \$4.2 billion. In terms of sectors, the office market dominated transaction activity, particularly in Hong Kong (\$3.1 billion) and Seoul (\$2.6 billion). Retail assets accounted for 33% of volume for the quarter, its highest level since Q2 2015.

On a 12-month rolling basis, USD transaction volume (income-producing assets only) across major gateway cities were up 11%. In local currency terms, the strongest increases were seen in Hong Kong (+89%) and Singapore (+20%), pulled up by several large transactions. Overall investment activity declined in Shanghai and Beijing by more than 25% while in Seoul the decline was a milder 5.5%. After adjusting for the unusually large IFC Seoul sale in 2016, volumes in Seoul were 15.5% higher. In Australia, investments into Melbourne increased by 11%, outpacing Sydney which grew by only 1.5% over the same time period.

Major transactions that closed in Q1 included the Link REIT neighborhood mall portfolio (\$2.9 billion) and 18 King Wah Rd (\$1.3 billion) in Hong Kong, K-Twin-Towers (\$665 million) and Pacific Tower (\$406 million) in Seoul, Chevron House (\$500 million) in Singapore as well as Two Melbourne Quarter (\$425 million) in Melbourne. Outside of the assets transacted in Hong Kong, buyers of these properties were all domestic players.

GATEWAY MARKET TRANSACTION VOLUME



Source: RCA

Hong Kong

KEY REAL ESTATE INDICATORS

	VACANCY RATE	RENTS	ABSORPTION	COMPLETIONS	CAP RATES
Office (Hong Kong Island)	1.8% ↓	↑	↑	↑	↓
Retail (Shopping Center)	2.6% ↔	↔	↑	↑	↔
Residential	3.7% ^a ↑	↑	↑	↑	↓

ECONOMY

Early data releases indicate Hong Kong's economy had a strong start to 2018. External demand held up well in Q1 2018 and exports grew by 10.7% year-on-year in the combined months of January and February. In March 2018, the Hong Kong PMI reading declined slightly to 50.7. Although the reading was above the expansionary level of 50, the decline was a reflection of the slowdown in China and expectations are for external demand to moderate going forward. Meanwhile, the solid labor market and overall wage growth have continued to bolster private consumption and domestic demand. Full-year GDP growth forecasts have been updated recently to 3% in 2018 and CPI inflation is anticipated to rise to only 2.3%, up from 1.6% as of Q4 2017.

Despite several U.S. Fed rate hikes in 2017, the impact on Hong Kong's interest rates was minimal in 2017 due to high liquidity in the banking sector. As 2018 progressed and interest rate differentials between the U.S. and Hong Kong have widened, the HKD dollar hit the weaker end of the HKD/USD peg (7.75 to 7.85) requiring the Central Bank to intervene several times to protect the band. Hong Kong's interest rates are likely to gradually rise as banking liquidity falls with households and businesses likely to feel the pressure from rising borrowing costs in the coming quarters.

PROPERTY MARKET - OFFICE

Tenant decentralization and expansion by co-working operators continued to be a key feature of new demand in Hong Kong as quarterly net absorption grew by 11.0% to 747,500 square feet in Q1. Given the robust demand and tight vacancy levels in most submarkets, rental increases were observed across the board.

Tenants are continuing to take advantage of the rental discounts outside Central, which range from 70% to 40%, to relocate to the more affordable markets of Hong Kong East and Kowloon East. These trends have also benefited leasing in upcoming buildings. For example, Swire Properties' One Taikoo Place reached a pre-commitment rate close to 80% after securing leases from EY and Kering, both relocating out of their offices in Central. At the same time, demand for flexible workspace remains high as occupiers attempt to manage costs and efficiency in an increasingly pricey rental environment. Wework and nakedHub (acquired by Wework in April 2018) have both leased new space in Hong Kong East and Kowloon East respectively, while Spaces (Regus's co-working brand) expanded their space requirements in Wanchai/Causeway Bay. The quarter also saw the entrance of Atlas (Guangzhou-based co-working operator) with plans to open two separate centers in Tsim Sha Tshui. Meanwhile in Central, leasing activity by People's Republic of China (PRC) firms was lower than usual owing to the Chinese New Year holiday period. Instead, tenants seeking expansion like Huaxia Bank's 15,000 square feet lease at Two IFC contributed to the net absorption within the district.

Across Hong Kong, between 2018 and 2019, about 4.5 million square feet is expected to be completed, about 50% of which will be on Hong Kong Island and the rest in Kowloon.

Across Hong Kong, between 2018 and 2019, about 4.5 million square feet is expected to be completed, about 50% of which will be on Hong Kong Island and the rest in Kowloon East. Hong Kong Pacific Tower in Kowloon East reached completion in Q1 2018 with a pre-commitment rate of 17%. Mapletree Bay Point (Kowloon East) and One Taikoo Place (Hong Kong East) will come online in Q2 and Q3 2018 respectively. Pre-commitment levels for both have increased steadily since last quarter and are currently at 40% and 75%, respectively. New supply going forward will be limited in Central, Wanchai and Tsim Sha Tshui.

In view of the stronger than expected demand levels observed in Q1, rental forecasts for 2018 have been revised upwards. Projections are for rents across Hong Kong Island submarkets to rise between 5% and 10%, led by Hong Kong East. Meanwhile submarkets outside Hong Kong Island are expected to benefit from ongoing decentralization trends, with rents forecasted to increase by 0% to 5% by year end. Despite the high vacancy of 11.8% in Kowloon East, rents are still likely to increase as it remains the only submarket with significant space availability.

PROPERTY MARKET - RETAIL

The four-year rental correction in Hong Kong's retail industry is likely to bottom in 2018. Improving retail sales from 2017 are expected to continue with a forecasted 4.0% year-on-year growth for 2018. Supporting infrastructure such as the completion of the Hong Kong-Zhuhai-Macau Bridge (Q2 2018) and the Guangzhou-Shenzhen-Hong Kong Express Rail link (Q3 2018) are also expected to improve tourist arrivals and retail sales. JLL estimates these will increase the number of mainland visitors to the city by 2.1 million per year.

Mass market retail sectors and Food and Beverage (F&B) have contributed to new demand in Q1. On the ground, pick up in rents in shopping centers are still viewed as building-specific rather than widespread as retailers remain fairly cautious and are focused on rebalancing and consolidating portfolios. For high-street retail, landlords are keeping flexible on rents amid high vacancies. High-street leases signed in Q1 were dominated by cost saving initiatives. For example, fashion brand Twist leased a two-storey shop at East Point Road at a monthly rent of HKD1.35 million (approx. USD27 per square foot per month), about 64% lower than the previous tenant. Nevertheless, improvements are expected in the second half of the year and will be driven by mass market rather than high-paying luxury retail tenants.

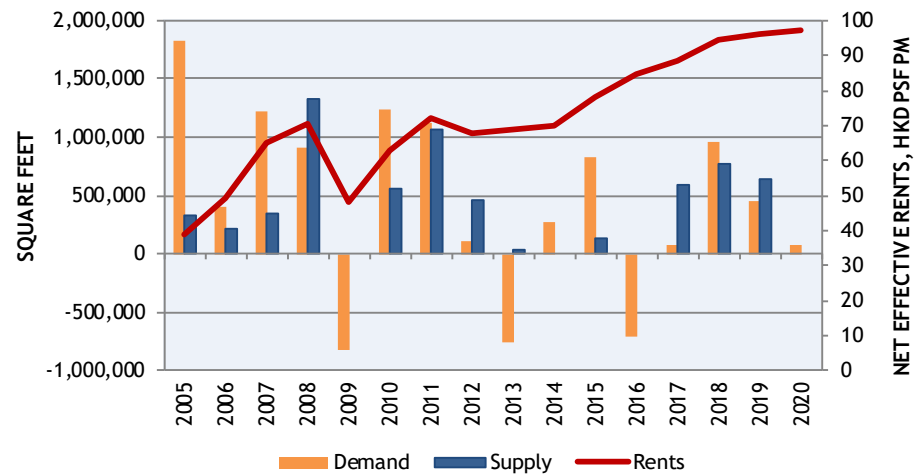
PROPERTY MARKET - RESIDENTIAL

Given the lack of cooling measures in the Government's 2018/2019 Budget statement, the housing sector remained upbeat in Q1. Overall transaction volume dropped by 8.0% quarter-on-quarter in Q1 to 15,000, but this was due to developers holding back on new launches in observance of the Chinese New Year festival in February. Correspondingly, primary transactions recorded a 36% quarter-on-quarter decline while secondary transactions saw a slight 2% increase in sales volumes. Prices continued to climb as sellers held firm on asking prices and mass market home prices rose by 4.4% quarter-on-quarter. In the luxury segment, new records were also set on a quantum and per square foot basis for a property on Mount Nicholson that transacted at HKD1.40 billion (USD180 million, \$19,400 per square foot). The sustainability of ever-increasing prices is uncertain with the expectation of increasing HIBOR rates. To date strong competition amongst banks have kept lending rates low, however, as the HIBOR rises there will be added pressure on banks to increase mortgage rates.

PROPERTY MARKET - RESIDENTIAL

The transaction market remained active in Q1 2018 with \$7.8 billion in sales recorded. This was about two times the volume transacted compared to the same period last year. Major transactions that closed in the quarter included Link REIT's neighborhood mall portfolio sale to a consortium led by Gaw Capital (\$2.9 billion), 18 King Wah Road to China Create Capital JV (\$1.3 billion, \$3,900 per square foot), One Harbour East to a JV between Angelo Gordon and family office (\$265 million, \$1,600 per square foot) and Bonham Circus to a Macau-based investment group (\$217 million, \$2,500 per square foot).

HONG KONG ISLAND DEMAND, SUPPLY AND RENTAL OUTLOOK



Source: JLL

Singapore

KEY REAL ESTATE INDICATORS

	VACANCY RATE		RENTS	ABSORPTION	COMPLETIONS	CAP RATES
Office (CBD)	8.1%	↓	↑	↑	↑	↓
Retail (Suburban)	2.6%	↔	↔	↓	↓	↔
Residential	7.4%	↓	↑	↓	↓	↔

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 Q4 2017 trend compared with the 12 months through to end Q4 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.

ECONOMY

After better-than-expected growth in 2017, the Ministry of Trade & Industry (MTI) has set growth projections ranging from 2.5%-3.5% in 2018. In Q1, Singapore registered a strong expansion in manufacturing (+10%) and moderate growth in services (+4%). The PMI stayed above 50 in Q1 as factory output registered a 5.9% growth in March 2018. However given the cooling in Chinese import demand and the US-China trade frictions, export-led sectors are expected to slow in coming quarters. This will be partially offset by an increase in domestic-orientated service sectors.

Singapore's monetary policy was tightened at the last bi-annual policy meeting in April 2018 after a 2-year long neutral stance. This was in spite of inflation easing to 1.5% in March versus the 1.7% in February. The government cited robust growth, a healthy labor market and wage growth as an indication of higher inflation in later half of 2018.

PROPERTY MARKET - OFFICE

Net absorption was 840,700 square feet in Q1, surpassing 2017's full year take up levels. This was led by scheduled relocations into recently completed offices- Marina One and UIC building, located in the Marina Bay and Shenton Way submarket respectively. Expectedly, net absorption levels in both these submarkets increased substantially during the quarter. As a number of these tenants were formerly located in Raffles Place, net absorption in that submarket was pulled down by the units that were released back to the market as vacant space. Vacancy levels in Raffles Place still remain below 5%, while vacancy in Marina Bay and Shenton Way are at 12.2% and 9.5% respectively. Grade A and Grade B CBD rents were up by 3.0% and 2.5%, respectively, in Q1.

Consistent with last quarter, demand was broad-based across technology, business services & finance as well as co-working operators expanding or setting up new outlets in Singapore. New entrants to the market included Yitu, a Chinese artificial intelligence company – who have set up a new office in Asia Square while co-working operators WeWork and The Great Room have both opened their second centers in the Central Business District (CBD).

Interest in non-CBD locations were also evident in Q1 and could gain further traction as corporations implement new technologies and strive to increase workplace efficiencies. For example, CBRE plans to give up the bulk of their main CBD office to relocate to Paya Lebar in 2019. The real estate firm will be consolidating their operations in 30,000 square feet lease at the new Paya Lebar Quarter development by Lendlease.

After a stellar year in 2017, Singapore's investment market was relatively muted in Q1 2018 with \$1.1 billion in transactions (excluding land sales), and another \$1.3 billion in pending deals.

PROPERTY MARKET - RETAIL

The retail sector appears to have turned a corner. After three years of consecutive decline from 2014-2016, total retail sales (excluding motor vehicles, at constant prices) grew by 1.3% in 2017. Further bolstering the retail industry are the on-going efforts to grow tourism. The Singapore Tourism Board (STB) is forecasting 1-4% growth in visitor arrivals and 1-3% growth in tourist receipts for 2018.

Demand in the quarter was broadly led by F&B, sports and wellness retailers. Net absorption however was flat as new take up was negated by some tenants exiting the market. In Q1, new-to-market entrants were dominated by F&B groups from Japan, Korea and Taiwan. There were also some cases of existing F&B operators expanding, but this was mostly within the suburban market where footfall tends to be high. Meanwhile, several clothing retailers have completely exited Singapore – these included American Eager Outfitter, Banana Republic and Gap.

Despite improvements in consumer sentiment, retailers remain conscious of the structural challenges in the retail sector. Landlords are re-orientating their leasing strategies to secure longer-term tenants and are generally more open to changes in the tenant mix and lowering rents. Landlords of struggling malls were also receptive to non-traditional retail users that are typically lower paying. For example, One Raffles Place mall has signed a lease with Spaces to set up a co-working office across a few floors in the mall.

There were no new retail openings in Q1 2018, but supply is expected to hit later this year and will intensify in 2019 with the completion of Jewel @ Changi Airport. Supply will be largely skewed toward suburban areas, but improved demand will keep suburban rents stable in the near-term. Beyond 2019 where supply will be limited, rents are expected to rise modestly.

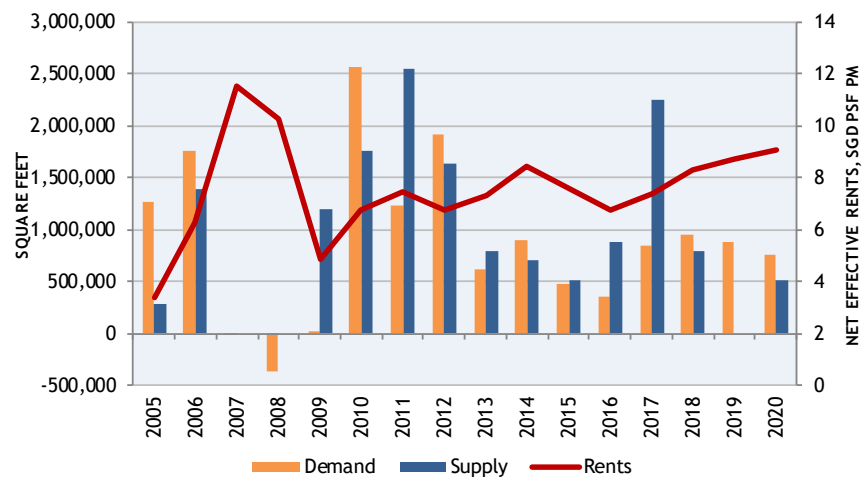
PROPERTY MARKET - RESIDENTIAL

The residential market continues to strengthen amid growing optimism and the near term tightening in supply following the enbloc sales. Owing to seasonal factors (Chinese New Year celebration in February), transaction volume in the Q1 2018 was down from the previous quarter but up 4% when compared to the same period in the 2017. Price increases ranging from 1.2% to 5.5% in Q1 were observed across the island. The prime districts in particular saw large increases as the gap between sellers and buyers expectations widened. The activity in the enbloc market has also carried forward to 2018 where the overall value of collective sales for 2018 is expected to cross last years \$8.2 billion. However there is some consensus that developer's landbanks have been sufficiently restocked and developers will become increasing selective with tighter policy measures taking effect. In Q1 2018, development charges for non-landed projects were raised while the MAS has asked for closer scrutiny of bank financing for development projects.

INVESTMENT MARKET

After a stellar year in 2017, Singapore's investment market was relatively muted in Q1 2018 with \$1.1 billion in transactions (excluding land sales), and another \$1.3 billion in pending deals. A major office transaction that concluded in the quarter was the sale of Chevron House to Oxley Holdings (\$500.6 million, \$1,916 per square foot). We expect transaction activity in the office sector to pick up in the later half of 2018, fueled favorable demand and supply dynamics. There has also been recent activity in the suburban retail space; in April 2018, CapitaMallTrust announced the divestment of Sembawang Shopping Centre (\$189.2 million, \$1,317 per square foot) to a joint venture by Lian Beng and Superfoods family office and SPH REIT announced the acquisition of Rail Mall (\$48.2 million, \$969 per square foot).

SINGAPORE CBD DEMAND, SUPPLY AND RENTAL OUTLOOK



Source: JLL

Seoul

KEY REAL ESTATE INDICATORS

	VACANCY RATE		RENTS	ABSORPTION	COMPLETIONS	CAP RATES
Office (Overall)	13.8%	↑	↔	↓	↓	↔
Office (CBD)	15.7%	↑	↑	↓	↓	↔
Office (Yeouido)	25.4%	↑	↔	↓	↑	↑
Office (Gangnam)	4.6%	↓	↑	↓	↓	↔

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 2018 trend compared with the 12 months through to end Q1 2018. 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.

ECONOMY

GDP grew by 1.0% in Q1 on the back of a healthy domestic demand and export growth. With lower world trade growth expected, export growth is likely to moderate gradually in 2018. The March PMI also fell to 49.1, suggesting that manufacturing activity is likely to face some near term headwinds. The economy is still expected to expand at a healthy rate of 2.8% in 2018 supported by strong consumption numbers and increased government spending. Consumer sentiment is currently at multi-year highs despite a weakened labor market and high household debt. Year-on-year retail sales were positive for the first three months of the year. This was also pulled up by improving tourist arrivals, up 10.7% year-on-year in March 2018, ending 12 straight months of decline. Even so, CPI inflation remains modest, with the March number easing to 1.3% year-on-year, below the target rate.

The Bank of Korea (BOK) raised the base rate by 25 bps in November 2017 to 1.5% but it has remained unchanged since. As inflation remains relatively muted and employment numbers have weakened, the scheduled pace of rate increase is likely to slow.

PROPERTY MARKET - OFFICE

Overall net absorption in Q1 was -251,000 square feet, pulled down by major tenant departures to owner-occupied buildings in Yeouido Business District (YBD) and Central Business District (CBD). Gangnam Business District (GBD) was the only submarket with positive net absorption (66,200 square feet) for the quarter. The overall vacancy rate across Seoul increased 2.2 percentage-points quarter-on-quarter to 13.8%, its highest level since Q3 2016. The relocation schedule of tenants to self-use buildings is at its tail-end and is expected to have less an effect on the market in 2018 compared to 2017.

In the CBD, net absorption in Q1 was -292,300 square feet, pulling vacancy up to 15.7%. Despite some positive take up in the quarter - for example WeWork at K Twin Tower and Hotel Shilla at 101 Pine Avenue, occupancy was dragged down by several tenant exits. The largest was Amore Pacific (426,000 square feet) vacating Signature Tower to move into their new HQ in Yongshan. Other smaller relocations out of CBD were from D-Tower (Daelim Groups) and Ferrum Tower (Barclays and SKT). As vacancies rose, landlords managed to hold firm or increase gross rents, but this was accompanied by a small increase in rent-free incentives in buildings with large vacancies. As a result, net effective rents declined slightly, 0.5% over the quarter. One major project Centropolis is expected to complete in H2 2018. To-date, there have been rumors of pre-commitments by smaller occupiers although nothing has been formally confirmed yet. Despite the

The economy is still expected to expand at a healthy rate of 2.8% in 2018 supported by strong consumption numbers and increased government spending.

increase in supply, vacancy rates are expected to be manageable due to healthy backfill leasing activity by a mix of finance and co-working firms. Landlords are expected to gradually lower rent free incentives over the next few quarters.

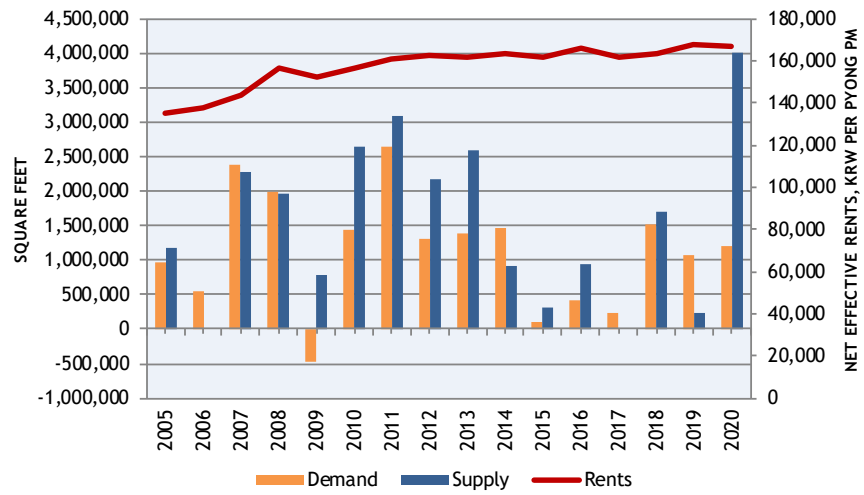
In YBD, vacancy levels rose to 25.4% in Q1 in the face of a new completion (KTCU Building, 472,000 square feet) and the relocation of LG affiliates group from FKI Tower to their new campus in Mangkok. The departure of the remaining LG group will likely take place in the later half of 2018. Net absorption for the quarter was negative 24,500 square feet. Outside of the departure, demand in the YBD was mostly from finance firms taking up space at IFC and FKI Tower. There was also interest from emerging sectors like cryptocurrency and Peer-2-Peer (P2P) finance firms. Landlords continued to increase incentives in Q1 to attract tenants, resulting in a 3.3% decline in net effective rents. YBD's high incentive levels (rent free period currently at 4.5 months) is appealing to tenants, which is increasing traction with new demand. For the remainder of 2018 and 2019, YBD will not receive any new projects, which will help to bring down vacancy levels and allow a mild increase in effective rents between 2018-2019.

With no new completions in the quarter and healthy demand, vacancy rates in GBD dropped 0.6 percentage-points to 4.6%. In Q1, demand was evident from information technology companies and co-working operators, while similar to YBD cryptocurrency and P2P firms were emerging and sources. Despite inherent interest, physical demand was muted as low vacancies have limited the number of successful leasing transactions. Newly completed buildings have also filled up fast suggesting strong underlying demand – for example, newly constructed Icon Tower in Yeoksam has reached an occupancy of 82% within less than half a year. Co-working operators in particular were active in Grade B buildings - WeWork opened its fifth branch, taking 14 floors (128,100 square feet) at PCA Life Tower, while Myworkspace leased 16,300 square feet at A+ Asset Tower. Rents in Grade A buildings were mostly flat quarter-on-quarter, while in Grade B buildings, some landlords began to scale back on their rent-free incentives. In 2018, there will be two new completions in GBD- Gangnam N Tower and Luchen Tower, both of which have no pre-commitments to date. There is no expected supply in 2019. Given the tight vacancy levels, the effect of the new supply is expected to be minimal. Net effective rents are expected to rise by 4.9% over the next two years.

INVESTMENT MARKET

The investment market in Seoul was off to a strong start in 2018, with a total of \$4.1 billion in transactions (excluding land sales) for the first quarter of 2018. The momentum could continue into the year with another \$4.4 billion in pending deals. Currently in the works (but yet to be confirmed) is the sale of Centropolis located in the Jongno district of the CBD, expected to set a new record on total value basis for a single asset. Cross-border capital was active in Q1, contributing to 26% of transacted deals in Q1 but the market is still largely dominated by domestic players. Major transactions that took place in the quarter included The-K Twin Tower (\$664.8 million, \$732 per square foot), Pacific Tower (\$405.6 million, \$632 per square foot) and East Central Tower (\$316.9 million, \$293 per square foot). Buyers for all three assets were domestic players.

SEOUL DEMAND, SUPPLY AND RENTAL GROWTH OUTLOOK



Source: JLL

China

KEY REAL ESTATE INDICATORS

	VACANCY RATE		RENTS	ABSORPTION	COMPLETIONS	CAP RATES
SHANGHAI						
Office (CBD)	12.5%	↑	↔	↑	↓	↔
Office (CBD - Puxi)	12.3%	↑	↔	↑	↓	↔
Office (CBD - Pudong)	12.7%	↑	↔	↓	↓	↔
BEIJING						
Office (Overall)	4.3%	↓	↔	↓	↓	↔
Office (CBD)	3.9%	↓	↔	↓	↑	↔
Office (E. 2 nd Ring Rd)	0.5%	↓	↑	↑	↔	↔

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 Q4 2017 trend compared with the 12 months through to end Q4 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.

China's trade tensions with the US still remains a concern, however there is some consensus that the short-term impact will be minimal.

ECONOMY

China's economy expanded by 6.8% in Q1, pulled up by an increase in exports, active housing market and improving consumption levels. Notably, growth momentum slowed in March compared to February and January, alluding to the start of China's slowdown. Growth is expected to ease in 2018, with private sector forecasts broadly in-line with China's 6.5% target for the year. China's trade tensions with the US still remains a concern, however there is some consensus that the short-term impact will be minimal.

In March 2018 the presidential term limits were removed from the constitution and changes to key industry and regulatory bodies were announced. These are seemingly positive steps from an economic standpoint and will likely result in stability and the actualization of the government's strategy going forward. At the recent Boao Forum in April, President Xi also highlighted new initiatives that will broaden market access, improve the environment for foreign investors and speed up reforms in the financial sector. These are expected to benefit the economies of Shanghai and Beijing.

PROPERTY MARKET - SHANGHAI OFFICE

Vacancy rates remain elevated in the face of on-going new completions in the Shanghai. New completions peaked at 16.5 million square feet in 2017, almost twice the past 10-year average. The supply schedule continues to be robust in Q1, another 3.3 million square feet completed, which represents slightly less than one-quarter of the total supply expected for the year. Stock in the CBD increased by 6% in Q1. In Pudong CBD, new completions were concentrated in Lujiazui and included Lujiazui Finance Plaza, Lujiazui Fuhui Project and the Shanghai Tower Boutique Offices. In Puxi CBD, new completions were Hines' One Museum Place and Capitaland's Raffles City Changning.

Q1 demand in Pudong was led by domestic financial firms and co-working operators. Net absorption for the quarter was 580,000 square feet, up 41% from the past 4-quarter average. Major leases included China Continent Insurance (130,000 square feet) in Shanghai Tower, and KrSpace (54,000 square feet) in Century Link Tower. Of note, WeWork absorbed more than 160,000 square feet of Pudong's new completions.

Demand sources could expand to foreign firms going forward in view of the government's plans to open the industry to foreign ownership. Current vacancy levels of 12.7% are expected to gradually decline as occupiers take the opportunity to move in the Lujiazui market, which is known to be the preferred location for banks and finance related companies. New supply in Pudong will become extremely limited after 2018 and vacancy levels are expected to sharply decline between 2019 – 2022. In Q1, rents declined marginally in Q1 in face of the large supply, but this is not expected to be an on-going trend. Rents are expected to increase marginally by 0.7% in 2018, after which limited supply will place strong upward pressure on rents.

In Puxi, net absorption was 974,700 square feet, led by take up in newly completed buildings. Demand sources were a mix of domestic financial firms, co-working operators and technology-related companies. Over the past quarters, several tenants relocated to the decentralized markets, and landlords were forced to lower rents to fill vacancies. Puxi CBD rents have decreased by 3.9% over the past six quarters up to Q4 2017, but are now showing signs of stabilization. In Q1, rents increased marginally by 0.3%. As such, the forecast for 2018 has been revised upwards and rents are expected to increase by 1.1% this year. About 6.9 million square feet is expected to complete in Puxi CBD between 2018-2020, translating to an annual average supply of 2.3 million square feet. While this is higher than the annual average over the past three-years, most of the supply is outside the core district.

Due to healthy net absorption (1.7 million square feet) and limited completions (0.6 million square feet) in the quarter, vacancy rates in the decentralized markets declined 3.1 percentage points to 23.7%. In particular, Grade A projects have seen strong upgrade demand as well as cost-saving and consolidation interest from former Puxi CBD tenants.

Demand across submarkets is varied on account of affordability, industry focus and location. For example the Xuhui district is popular with technology-related firms, Pudong Expo holds many state-owned enterprises and North Bund is typically known as the financial district and is also the most expensive decentralized submarket. Examples of leases signed included tech firms Blue Focus (108,000 square feet) and Wisesoftware Co (22,000 square feet) in Xuhui, Pharma group with SOE background Sinopharm Group (47,000 square feet) in Pudong Expo, and investment firm Galaxy Futures (24,000 square feet) in North Bund. The large pipeline supply (2018-2022) in the decentralized market averaging 8.4 million square feet per annum remains a concern. However supply schedule in some submarkets have already matured (such as Shanghai Railway St, North Bund, Qiantan) and these are expected to outperform the others going forward.

PROPERTY MARKET - SHANGHAI BUSINESS PARKS

In Q1 there were three new completions - all located in Caohejing Business Park- resulting in an overall stock expansion of 1.9% over the quarter. These were Xinzhou Building, Shanghai Business Park Phase III-1 (B) and Pujiang Intelligence Valley Phase II (East Zone).

Demand for business parks was strong in Q1 at 2.2 million square feet (GFA), growing by 27% quarter-on-quarter. The bulk of take up for the quarter was in Zhanjiang, located on the east-side of the Bund. Demand stemmed mostly from domestics, across technology, finance and e-commerce sectors. Newer completions with better specifications are also encouraging some upgrader demand from tenants within that particular submarket.

Rents in business parks continued to increase in Q1 as many landlords made annual rental

Demand from co-working and flexible space operators is emerging as a significant trend in Beijing.

adjustments. Overall increase was 0.9% quarter-on-quarter or 2.6% year-on-year. By submarkets, the highest rental increases were in areas with improved transportation and with newer and higher quality buildings - such as Jingqiao, Zhangjiang, Caohejing and Linkong. Remaining supply in 2018 is expected to be 5.4 million square feet (GFA) of which the bulk will be located in Jingqiao and Zhabei, where supply has been limited in the past few years. The overall outlook remains positive, where vacancies are expected to reduce and rents will continue to gradually rise given the healthy demand levels.

Rents are expected to increase by 5% in 2018.

PROPERTY MARKET – BEIJING OFFICE

After 4.3 million square feet of new completions in 2017, there were no new completions in Q1. Vacancy levels declined by 2.8 percentage points in Q1 to 4.3% as large occupiers took the opportunity to move into recently completed buildings. Some leases signed included Petro China who leased the whole of Hengyi building (861,000 square feet) and Herald International at Gateway Plaza in 3rd Embassy Area.

Beijing's core office areas include five submarkets—3rd Embassy, CBD, East 2nd Ring Road, East Chang An and Finance Street. Across CBD, East Chang An and 3rd Embassy submarkets, demand came from finance and insurance service companies. Larger and more profitable enterprises leased in the CBD where rents are higher. Demand on Finance St was limited in Q1 due to increasing regulation while on 2nd East Ring Road, extremely low vacancies (<1.0%) limited transactions despite an increasing amount of queries. Demand from co-working and flexible space operators is also emerging as a significant trend in Beijing. Most are concentrated in lower-end buildings or converted retail space, but some are growing a presence in Grade A buildings. An example is the lease signed by The Executive Centre at China Central Tower in the CBD.

Within Beijing's core submarkets, about 7.3 million is currently under construction and meant to complete in 2018-2019. About 87% of this will be concentrated in Guomao, which is part of the CBD submarket. In April 2018, the building height restrictions for new developments in Guomao was capped at 100-180m, which will affect the projects which have yet to break ground. As a result, the new supply in Guomao has been delayed and reduced by about 14% over last quarter. Forecasted rents in the CBD have been adjusted upwards to reflect this change – rents are now expected to decline by 2.0% in 2018 and remain largely flat in 2019-2020. For overall Beijing, rents will increase by 1.4% in 2018 and a further 1.9% in 2019.

INVESTMENT MARKETS

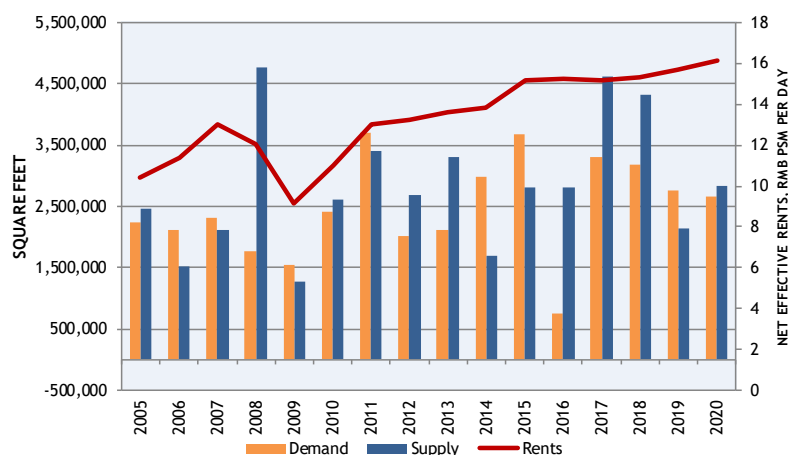
Excluding land sales, investment markets in Shanghai and Beijing were slow in 2018, registering a combined \$1.9 billion in sales in Q1. Shanghai accounted for the bulk \$1.1 billion of volume. Including land sales, the transaction volumes were substantially stronger at \$14.8 billion, up almost 23% from the same period last year. In Shanghai there were some office deals that closed in March and April that represented the largest transactions year to-date. These included Shengbang International Building (\$375.3 million, \$619 per square foot) to LaSalle Investment Management and Vi-Hub (\$289.7 million, \$619 per square foot) to Bank of China. There was also some activity in the retail sector—Bauhinia Square (\$468.3 million, \$629 per square foot) to Early Light International and the Gaw-TH Real Estate China Retail portfolio to Allianz. The latter transacted at an undisclosed amount. In Beijing, offices were mostly transacted on a strata-titled

basis in Q1. Interestingly, the three largest transactions year-to-date in 2018 were all hotel assets. These retailers are also getting creative, introducing novel customer experiences or are using digital strategies. For example, Starbucks Reserve Roastery debuted a new concept store at Taikoo Hui in Q4 2017, offering an interactive, multi-sensory coffee experience along with augmented reality via a phone app. Meanwhile, online integrated supermarket store He Ma Sheng and Super Species opened flagship stores in decentralized malls to serve a customer base within a three kilometer radius.

As many projects scheduled for completion in 2017 were delayed, a city-wide supply peak is expected from 2018 to 2019. Even though demand continues to be healthy, supply-side pressures will limit rental growth going forward.

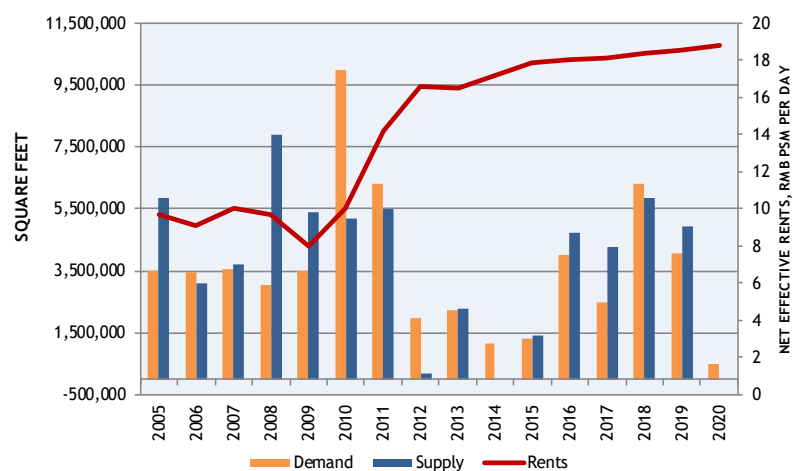
Investment activity continues to be strong in Shanghai with transaction volume (excluding land sales) coming in just a hair below 2016 levels. Cross border buyers represented about 41% of the activity in 2017, a significant jump from the 25% in the previous year. More than half of cross-border sales in the year was from capital sourced from Hong Kong and Singapore. The most notable deal in 2017 was from the sale of the Sky Soho Project to Gaw Capital for about \$753 million (\$545 per square foot). This was a group of Grade A office buildings developed by SOHO China in Linkong Economic Park, west of Changning district. Other major deals in the year included Eco City by Ting Hsin International Group for \$928 million (\$1,285 per square foot), Garden Square by KLand for \$570 million (\$946 per square foot) and Soho Hongkou for \$525 million (\$696 per square foot) by a consortium comprising Keppel Land, Alpha Investment Partners and Allianz.

SHANGHAI CBD DEMAND, SUPPLY AND RENTAL OUTLOOK



Source: JLL

BEIJING OVERALL DEMAND, SUPPLY AND RENTAL OUTLOOK



Source: JLL

Australia

KEY REAL ESTATE INDICATORS

	VACANCY RATE	RENTS	ABSORPTION	COMPLETIONS	CAP RATES
SYDNEY					
Office CBD (overall)	5.5%	↑	↑	↓	↔
Office North Sydney (overall)	6.9%	↓	↑	↓	↔
MELBOURNE					
Office CBD (overall)	5.5%	↓	↑	↓	↔

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 2018 trend compared with the 12 months through to end Q1 2018. 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.

ECONOMY

Australia's economy is expected to expand by 2.7% in 2018. Bright spots such as the accelerating business investment and government spending will be weighed down by a slowing housing market as well as weaker employment and wage growth. Initial estimates in Q1 showed that consumer confidence had shifted positive however, due to softer labor market statistics, this is not expected to hold and consumer spending is likely to be a drag on the economy in 2018.

CPI inflation was 1.9% in Q1, below the Reserve Bank of Australia's (RBA) 2-3% target inflation range. A gradual pick up of inflation is expected for 2018, although this is likely to be contained due to slower wage growth and competition in retailing. Under current circumstances, the RBA has left the overnight cash rate unchanged at 1.5% and indicated that there no compelling case for monetary policy adjustment in the near term until sustainable growth and inflation targets are achieved.

PROPERTY MARKET- SYDNEY CBD OFFICE

Net absorption in Q1 was -75,500 square feet, but this was not indicative of market weakness. Latent demand continues to be strong and ranged across professional services, finance & insurance and co-working sectors. Instead, the on-going secondary stock withdrawals process and a major government tenant's (Railcorp) relocation to a decentralized market have negated the effects of the positive demand. Additionally, the lack of contiguous space options in Sydney's CBD have placed a cap on leasing activity in existing buildings. Even so, prime and secondary grade vacancy rates remained low - currently at 5.8% and 4.9% respectively.

Even though the withdrawals schedule will taper off in the next couple of years, net supply will fall far below future demand projections. From 2018-2019, the 962,000 square feet of new space that will be delivered will be reduced by another 650,300 square feet from planned withdrawals, resulting in 155,900 square feet of net supply per annum. The next supply cycle is expected to peak in 2020 with the completion of several office projects – the largest of which is AMP's Wynyard Place (61% pre-committed).

As mentioned earlier, leasing in existing buildings have been limited by the lack of large floorplates available. This has prompted many occupiers to forward commit to leases in upcoming projects that typically have larger floorplates and are of better quality. Pre-leasing activity was strong this quarter with a total of 353,300 square feet committed across multiple

The lack of contiguous space options in Sydney's CBD have placed a cap on leasing activity in existing buildings.

Leasing demand held up well in Q1, mostly from media and technology companies.

developments. 151 Clarence and 60 Martin Place, both completing in 2019 are now 82% and 41% pre-committed respectively.

Given low vacancies and strong demand, net effective rents across both prime and secondary grade buildings continued to increase in Q1 by an average of 4% after a full year increase of 22% in 2017. These included reductions in incentives which have reached a new low since 2008. Net effective rents range from AUD577 - AUD791 per square meter per annum while incentives are between 16%-18%. The widening rental gap between Sydney CBD and other suburban markets are likely to encourage smaller-sized cost conscious occupiers to lease outside the CBD in the fringe markets like Macquarie Park and North Shore which can offer discounts of up to 50%.

Net effective rents are expected to continue to grow between 11-14% in 2018, but will see growth rates decelerate quickly in 2019 and 2020 on the back of new supply and possible cost-saving relocations.

PROPERTY MARKET- NORTH SYDNEY OFFICE

Like Sydney CBD, the North Sydney market has also benefitted from the on-going withdrawals of secondary stock. Vacancy levels are currently at 6.9%, significantly below the 10-year average vacancy level of 9.1%.

Leasing demand held up well in Q1, mostly from media and technology companies. In Q1, the largest leasing deal across the North Shore market was signed in North Sydney – a 54,000 square feet lease at 111 Pacific Highway by Nokia who have relocated from the Pyrmont submarket. Over the past year, brokers have also reported a notable increase in leasing enquiries from Sydney CBD tenants looking for a less costly alternative for their secondary operations. Compared to the CBD, North Sydney rents are currently 34% lower. Overall net absorption for Q1, was negative 33,300 square feet, brought down by the withdrawal of 59-61 Lavender Street. After accounting for this, demand was a positive 66,700 square feet for the quarter.

There were no new completions in Q1. In the next two years (2018-2019), 485,000 square feet of new office space will be delivered, but the net supply will still be negative due to an estimated 522,000 square feet in withdrawals for the year. Only one major office is expected to complete in the near term- Dexus's 100 Mount which is expected to add 437,000 square feet to overall office stock by Q4 2018. The project has a pre-commitment rate of 65% and is expected to increase prior to its completion date. Others in the pipeline are smaller developments 88 Walker and 148 Pacific Highway. Supply will then peak in 2020 with the completion of Winten Group's 1 Denison (697,000 square feet) and Zurich Properties' 118 Mount Street (252,900 square feet).

Given limited quality stock options and various sources of demand, net effective rents across both prime and secondary grade buildings continued to grow by 1.5% and 3.5% respectively in Q1. Expectations are for prime grade rents to increase by 8.5% over the 2018-2019 while the increase in secondary grade rents could be slightly stronger due contracting stock.

PROPERTY MARKET - MELBOURNE CBD OFFICE

After new completions peaked in 2015-2016 (2.4 million square feet), excess space has been sufficiently absorbed. Supply was limited in 2017 (295,000 square feet) and in Q1 2018, vacancy rates in Melbourne CBD dropped to a new low of 5.45%.

This was below the past 10-year average of 7.6%.

Q1 net absorption was 395,000 square feet. The bulk of demand in Melbourne CBD has traditionally stemmed from smaller sized occupiers, but in Q1 there was an increase in expansionary activity by larger tenants (>10,000 square feet). For example, professional services firm Civia Pty Ltd and education provider Laurete led demand in the quarter with leases signed in excess of 59,000 square feet. There were also several examples of co-working and flexible office providers expanding their portfolios within the CBD - these included Space and Co, Hub Australia and Clear Edge Offices. Take up by the co-working sector is expected to gain momentum in coming quarters.

Because of limited new supply in 2017, available space in the market was steadily absorbed over the past year. Between 2018 and 2019, new completions in the CBD will reach 2.8 million square feet, spread across 7 new projects. Of the new space that will be delivered in the next two years, about 90% has already been pre-committed. New office completions in 2018 will only be in the Docklands precinct where vacancy rates are exceptionally low (1.4%). These projects include Southern Cross Station, Collins Square 5 and One Melbourne Quarter. Leasing activity for backfill space has been active and several landlords have already secured replacement tenants.

Low vacancy levels and strong demand have pushed net effective rents up by 13-14% in 2017 and a further 3-4% in Q1 2018 across both prime and secondary grade buildings. Incentive levels however remain high at around 29-30%. Prime net effective rents are expected to grow by 13.8% in 2018 before slowing to 4.3% and 1.3% in 2019 and 2020.

INVESTMENT MARKET

Sydney and Melbourne maintained moderate investment activity in Q1, recording about \$1.0 billion in sales each. Cross border capital was active in both markets, representing 52% and 36% of Q1 transactions in Sydney and Melbourne respectively.

In Sydney, major transactions in the quarter included 52 Goulburn Street (\$272.1 million, \$1093 per square foot) to Arcadian Property, the retail portion of York and George (\$205.6 million, \$2,582 per square foot) to PGIM Real Estate and Colonial House (\$158 million, \$800 per square foot) to Blackstone. There is potentially another \$2.0 billion deals that could close in the coming months which include some larger-sized deals. For example, Northpoint in North Sydney (est. \$463 million) and Allianz Centre (est. \$463 million) in Sydney CBD.

In Melbourne, major transactions for Q1 were Two Melbourne Quarter (\$452 million, \$806 per square foot) by local superannuation fund and 699 Bourke Street (\$156.9 million, \$767 per square foot) by Morgan Stanley. There is currently another \$560 million in additional sales likely to close.

For more information,
please contact:



GLYN NELSON

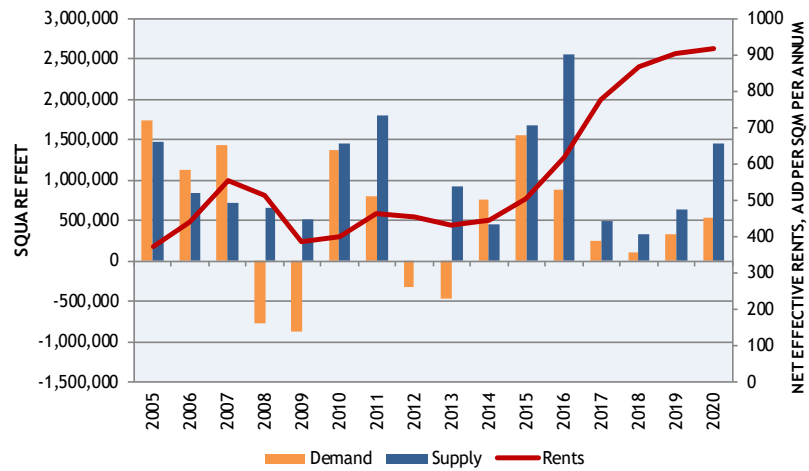
Director of Research, Asia Pacific

glyn.nelson@aew.com

+65.6303.9016

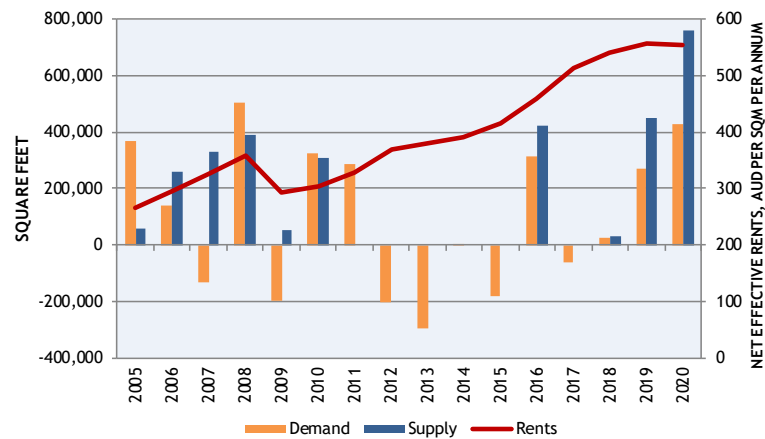
www.aew.com/asia

SYDNEY CBD DEMAND, SUPPLY AND RENTAL OUTLOOK



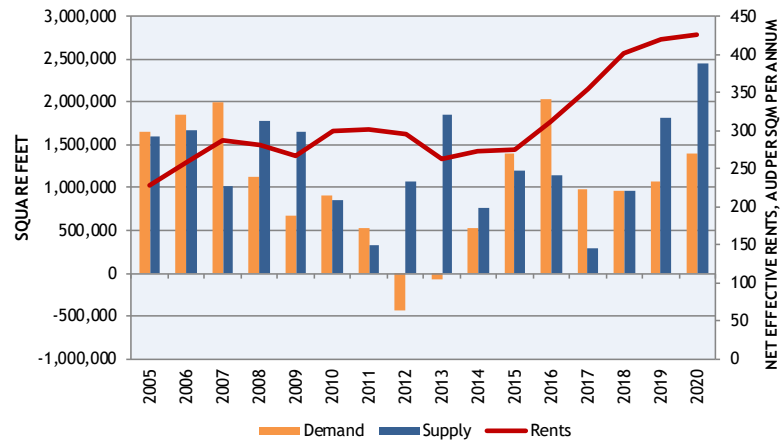
Source: JLL

NORTH SYDNEY DEMAND, SUPPLY AND RENTAL OUTLOOK



Source: JLL

MELBOURNE CBD DEMAND, SUPPLY AND RENTAL OUTLOOK



Source: JLL