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Strategic Property Consulting

Research insight

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Location within the Central City office market: How and why is it changing ?

The central Melbourne office market is readying itself for the first delivery of new generation space in almost a decade. Apart from differences in built form characteristics between upcoming and previous generations of buildings, there are a number of fundamentally different factors driving corporate relocation and expansion decision making. These changes are becoming reflected in the spatial distribution of new projects across the CBD, St Kilda Road, Southbank and now Docklands markets.

The spatial distribution of new projects across the central city markets (see Figure 1) is quite different from that observed in the early 1990s. A valid question is therefore raised about whether new office projects are marketable because of inherent location attributes or whether location has become less important as other dynamics at play in corporate real estate decision making come to the fore.

Whilst upcoming quantum of new stock is undoubtedly substantial, it is still significantly less than the 1.15 million m^2 of new space completed between 1990 and 1994 …

New office supply in Central City markets

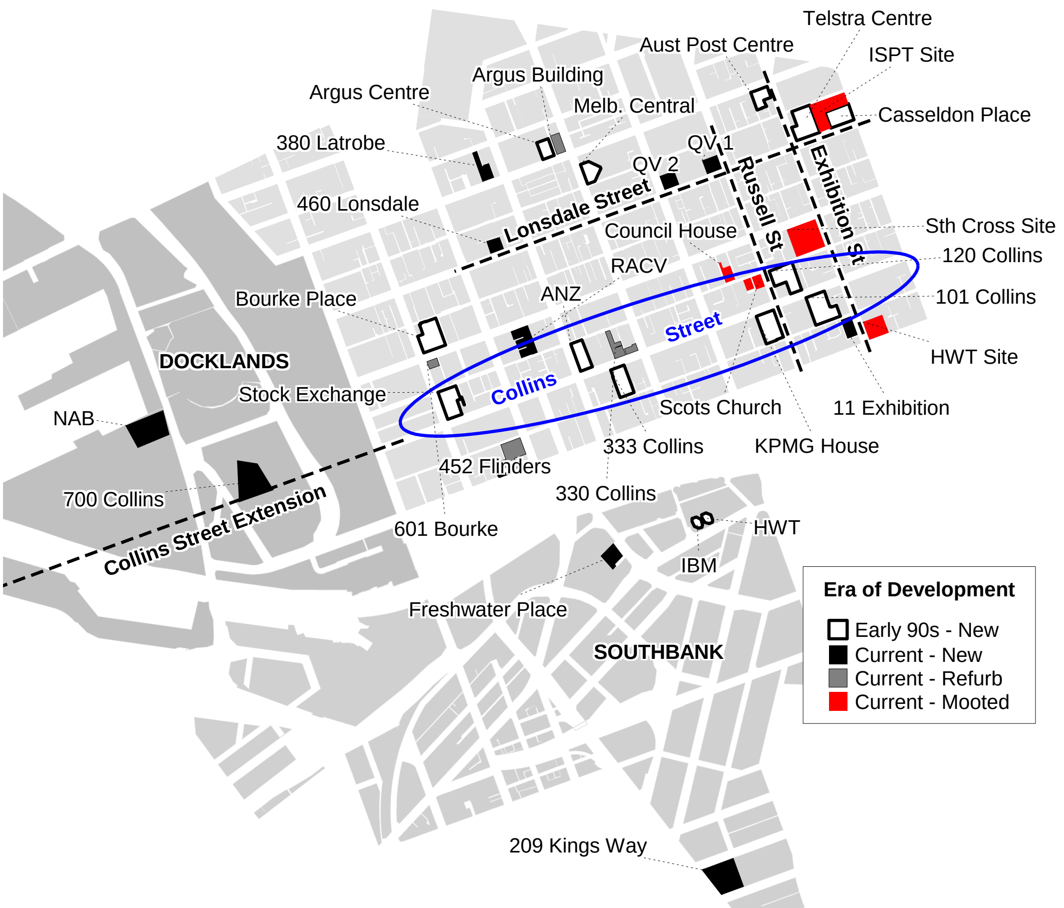
Over the past decade, significant advances have been achieved in workplace design concepts, building technologies, ESD principles and ITT infrastructure, coupled with fundamental shifts in corporate culture. Accommodation is being increasingly recognised as an integral factor in facilitating organisation and cultural change as partly evidenced by major refurbishments, but as yet, not fully expressed and integrated into a new major office building in Melbourne.

In the CBD and surrounding Southbank and Docklands markets there are ten new buildings containing 330,000 m^2 under construction or about to commence with expected delivery between 2002 and 2005. Another four buildings containing around 200,000 m^2 are also expected to commence in the short term subject to the confirmation of pending precommitments. Nearly 160,000 m^2 across several older buildings is also being refurbished and upgraded.

Figure 1:

Spatial distribution of major developments:

Current and Early 1990s



New office buildings at Docklands will effectively be located within an essentially massive mixed use project …

Another interesting characteristic of upcoming office buildings is their much better integration with complimentary uses. Apart from significant office components, projects such as Freshwater Place, QV, Urban Workshop, Yarra Yarra and the RACV Centre will offer a mix of retail, residential and hospitality related elements that will provide points of difference to other office environments.

Spatial distribution of upcoming supply

It is evident that new projects are being pushed towards peripheral locations, not only within the CBD but also outside it. Spines of higher quality office space are emerging along Lonsdale Street, Exhibition Street and, to a lesser extent, Russell Street. These spines are evolving with new projects such as QV, 11 Exhibition Street, Urban Workshop and mooted redevelopment of the Southern Cross, HWT and Scots Church sites consolidating the concentration of new buildings from the early 1990s, particularly around the North-East CBD precinct. A further spine may emerge along the extension of Collins Street through to Docklands with 700 Collins Street being the first announced project.

Precommitments of more than 220,000 m^2 have already been announced with the State Government's 100,000 m^2 requirement still to be fulfilled …

In contrast to the early 1990s when there was considerable new construction in the Western Core of the CBD, there is only one new building and several major refurbishments in this precinct, despite the availability of several suitable sites. New development is expected to be a feature of the Eastern Core with the consolidation of Government (State and Local) accommodation needs expected to be a major driver as well as proximity to Collins Street (at much lower rents).

Whilst major office development has already been established on the south bank of the Yarra, Freshwater Place will consolidate it as a major commercial location given the quality of the expected tenant profile. The choices by NAB and Bureau of Meteorology to underpin new projects at Docklands are likely to encourage further corporate relocation to Docklands which offers the best opportunity to accommodate new office design concepts such as bigger, contiguous but flexible floorplates within planned, higher quality environments.

Collins Street has not lost its appeal

A legacy of the former central role of Melbourne in Australian industry and financial markets is the presence of some of Australia's largest companies along Collins Street …

Despite the failure of a number of proposals for redevelopment of Collins Street sites (due in part to non-market related factors), there remains a strong market preference for this location as indicated by the street's ability to attract higher rents. Only one new building of the current generation bears the marketable Collins Street address, however 700 Collins Street (31,000 m^2) will be outside of the CBD grid. Full refurbishment of 330 Collins Street (16,600 m^2) will be the only Collins Street address in the CBD with large contiguous floorspace available. A substitute in the present market for a Collins Street address is a near Collins Street location which has contributed to the attraction of tenants to 11 Exhibition Street and will likely benefit proposals for Southern Cross and Scots Church sites. The current situation is in contrast to the early 1990s when 336,000 m^2 across five buildings was delivered with a Collins Street address.

Is location driving corporate relocation?

Recent lease precommitments have been struck at net rents ranging primarily between $300 to $350 p.s.m.p.a. with some as low as the mid $200 p.s.m.p..a and as high as $380+ p.s.m.p.a. These rates compare extremely favourably with current market rents for Prime buildings of the early 1990s era that are now achieving average rents ranging from $260 - $330 p.s.m.p.a. in secondary locations through to a range of $400 (west end) - $480 (east end) p.s.m.p.a. for Collins Street properties.

Compared to corporate largesse of the late 1980s, today's corporate environment is characterised by much stronger regard for governance and shareholder value as reflected in more cost-effective and less embellished office fitouts and contraction of workspace ratios …

The advent of super floorplates (2,000+ m^2) is another factor driving development towards peripheral locations given the higher cost and difficulty of consolidating large development sites in prime precincts …

Whilst location remains a primary consideration, the opportunity to precommit to a new building in a non-prime location with all the latest technologies and design principles that is less expensive to occupy than, say, a 10+ year old building is certainly attractive. Therefore the importance of location is being reassessed, particularly as the financial equation overwhelmingly favours non-prime locations with lower land values. Furthermore, integrated redevelopments offer an opportunity to translate some of the amenities / attributes of the best commercial precincts to almost anywhere within, or outside, the CBD. New generation office projects will allow employees to enjoy a walk through an active retail environment, have access to an on-site child care facility, go to an on-site gym at any hour, and importantly, create an environment that assists in the retention of key personnel in an increasingly competitive environment for skilled workers. These facilities can be provided more cost-effectively within a mixed use setting because of cross-subsidies between different user groups.

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