Charter Insight

Commercial Intelligence
Valuation Factors in 2017
Melbourne Market

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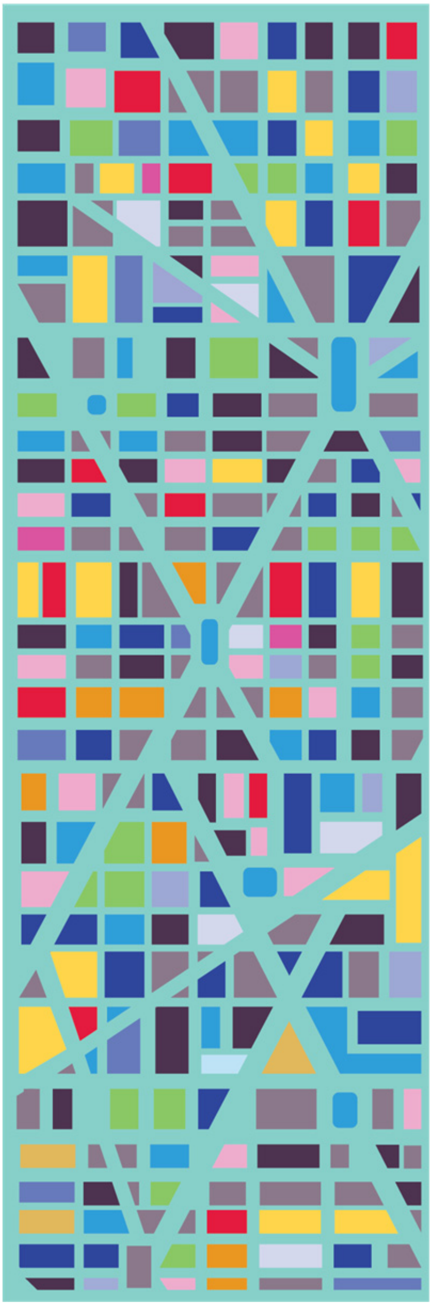
COMMERCIAL VALUATIONS



Office - CBD

OCCUPIER DEMAND

Strong tenant demand has seen the vacancy rate across the Melbourne CBD fall to 6.4% with net absorption for the six months to January 2017 being the strongest since 2006. The Melbourne CBD continues to be the prime focus for commercial occupiers taking advantage of relative affordable rentals and attractive incentives, together with the amenity that the CBD provides.

SUPPLY

Unprecedented levels of residential development have limited the availability of sites for commercial use and hence the supply of new office accommodation within the CBD. Only 40,000 sq.m. of accommodation is due to come on line in 2017, 65% of which is within a single building in Docklands.

RENTS & PRICES

Effective rents are gradually demonstrating growth as the tighter leasing market allows landlords to seek higher face rents and lower incentives. Whilst incentives are anticipated to remain in the market (in part to allow tenants to fund capital fit-out works), it is anticipated that effective rents will show growth over 2017.

There continues to be downward pressure on commercial office yields due in large part to the weight of money seeking to find a home. However, with bond rates starting to turn upwards, we anticipate yields will stabilise at their current levels.

2016 was a particularly strong year for the subdivided office market with 19 sales occurring of whole floors. Demand has been strongest from the owner occupier market, but with additional interest from investors, particularly for properties offering a remaining lease term of three years plus.

MARKET CONSIDERATIONS 2017

With office vacancy at 6.4%, the leasing market is starting to return to favour landlords, with tenants likely to have fewer future leasing options which should have a positive effect rental levels.

Chris Holroyd
Director - CBD Valuations

Office - Suburbs

OCCUPIER DEMAND

Stronger tenant demand in the inner suburban office market with vacancy rates decreasing. Hawthorn, Richmond, Collingwood, South Melbourne etc, are seen as an attractive and more affordable option than some CBD space. Conversion/demolition of existing office buildings to residential uses in the St Kilda Road and Southbank office precincts has also driven additional tenants to the inner suburban office market. Richmond (Cremorne) has proved popular for tenants in the media, advertising, marketing, design type fields.

SUPPLY

Similar to previous years there has been little activity in the city fringe, with most development sites being purchased for residential/mixed use purposes. Nevertheless, leasing opportunities have recently become available in some recently constructed office developments in Richmond and Collingwood. There are further office developments planned for the Richmond market to be available later in 2017 and 2018.

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RENTS & PRICES

City fringe rents are likely to gradually increase as a result of limited new stock. Outer suburban rents are likely to remain at a stable level. Given the continued low interest rate environment and increasing land values in inner suburban locations, together with a lack of quality stock, yields are likely to remain stable/compress further during 2017.

MARKET CONSIDERATIONS

The continued low interest rate environment is continuing to create interest in suburban office properties, particularly those which offer reasonable yields, occupy strong locations and/or benefit from medium to longer term redevelopment potential. Although very early into 2017, indications are that the suburban office market will continue at a steady/strong levels.

Sam Lipshut
Director - Office Valuations

Retail - CBD

OCCUPIER DEMAND

The Melbourne CBD continues to see a good level of demand from retail occupiers as a result of its significant daytime office population, visiting tourists (from both overseas and interstate), and increasing residential catchment. Notwithstanding, retail conditions more broadly are less strong with retail sales growth having fallen over 2016. Despite this, prime locations within the Melbourne CBD such as the Paris End and central Collins Street, together with Bourke Street Mall, continue to attract significant international retailers.

SUPPLY

Major developments at St Collins Lane and Emporium are now complete with no significant additions forecast. The Metro Rail Project will see a portion of retail space to the southern and northern ends of Swanston Street removed from the market whilst works occur, with occupiers already seeking alternate sites within nearby locations such as Elizabeth Street.

RENTS & PRICES

Generally retail rents within the Melbourne CBD have remained relatively stable albeit with some minor growth. The trend towards micro tenancies of less than 50 sq.m. has seen higher rental rates being achieved on a rate p.s.m. basis, with tenants typically considering the rental on an annual sum of money basis.

Yields for freehold retail premises have remained stable at historically low levels, albeit with few transactions occurring during 2016 reflecting the tightly held nature of such assets. As a result purchasers have been drawn to subdivided retail properties which over the last 12 months have seen significant price growth through yield compression reflecting the lack of available freehold properties, a low interest rate environment, and the affordable nature of such assets.

MARKET CONSIDERATIONS 2017

Works for the Metro Rail Project have commenced to the northern end of the CBD with further works anticipated along Swanston Street this year. This will impact the retailing in those areas immediately affected, but also surrounding streets as tenants and shoppers alike seek alternative locations.

Net returns from freehold properties are likely to be eroded as a result of increased levels of land tax following Council's 2016 revaluation. Notably this is likely to have a lesser impact on subdivided properties which typically have a lower land tax impost.

Chris Holroyd
Director - CBD Valuations

Retail - Suburbs

OCCUPIER DEMAND

A continuing trend which is the result of increased retail spending in the food & beverage/convenience restaurant sector is that these type of operators are still demonstrating healthy demand for retail strip premises with the major brands also displaying preferences for stand-alone facilities in emerging residential growth zones. Some doubt is emerging about fashion retailers with recent announcements concerning the failure of Pumpkin Patch, Marcs, David Lawrence, Rhodes & Beckett and Herringbone.

SUPPLY

2017 is expected to demonstrate that most retail supply will be within Neighbourhood Activity Centres that are typically located within outer residential growth areas. A major driver of this is the tenant and owner occupier demand from major fast food restaurants, service stations and supermarket based shopping centres.

RENTS & PRICES

It was well documented in 2016 that overall yield compression was experienced for most retail asset classes. "Blue chip" investment holdings outperformed whilst secondary assets also benefited from widespread investor demand for retail investments. Leasing conditions for premises within highly regarded strip centres for food and beverage uses together with major fast food restaurants and service stations are expected to remain strong over the short term.

MARKET CONSIDERATIONS 2017

Vendors in general recorded significant capital gains through the disposal of assets in 2016 and the main driver of this favourable pricing was primarily attributable to yield compression. This trend is anticipated to continue in 2017 however can the same sale stock levels of 2016 be offered to the market in 2017? If not, will this cause further yield compression and even higher prices for assets offered to the market in 2017?

Bernard Cussen
Director - Retail Valuations

Industrial

OCCUPIER DEMAND

Steady level of demand with the majority of activity coming from businesses within the transport, logistics, as well as food and cold storage industries. Prime locations which are within proximity to major arterials are highly sought after.

SUPPLY

Increased supply placed downward pressure on rents in 2016. Vacancy rates marginally improved over the past six months. Incentives range between 10% - 25% depending on size, age and condition.

RENTS & PRICES

Limited rental growth anticipated in 2017. Low interest rate environment, as well as strong appetite from both local and offshore investors will continue to underpin yields remaining at historic lows.

MARKET CONSIDERATIONS 2017

There will be a significant number of newly constructed multi-unit industrial developments throughout 2017, with unit sizes typically ranging between 80 - 175 sq.m. Established developers are experiencing increased difficulty in obtaining development finance even for projects which have strong pre-sales.

Anthony Witton
Director - Industrial Valuations

Recent Transactions of Significance

PROPERTY / ADDRESS	SALE PRICE ($ MIL) / PASSING YIELD	VALUE RATE ($ P.S.M. BUILDING)	COMMENT
RETAIL			
125-131 Chapel Street **Windsor**	$14.96 / 3.90%	$16,170	A refurbished two storey retail/office building occupying a prominent corner location. Strong medium to long term redevelopment prospects.
KFC **Bacchus Marsh**	$2.82 / 4.35%	$13,756	A major fast food restaurant holding leased to a major KFC franchisee.
OFFICE			
301 Flinders Lane **Melbourne**	$34.20 / 3.88%	$7,398	Older style seven level building leased to Victoria University. Previously sold in September 2014 for $23,600,000 (45% increase) with no change to the building and a shorter remaining lease term.
114 William Street **Melbourne**	$161.50 / 5.92%	$7,698	23 level office tower located within the western core of the CBD. Again a sale demonstrating a significant uplift in value over a short period having sold in August 2015 for $125,000,000.
582 Swan Street **Richmond**	$10.01 / 6.26%	$6,198	Modern three level office building situated at the front of the Botanicca Business Park. Sold following an Expressions of Interest Campaign on a fully leased basis. WALE of approximately 39 months. Previously sold in September 2013 for $6,150,000.
391-393 Tooronga Road **Hawthorn East**	$13.50 / VP	$5,572	Two level commercial office building constructed in circa 1980 sold following an expressions of interest (EOI) campaign with vacant possession. Purchased by a local owner occupier.
INDUSTRIAL			
40-48 Howleys Road **Notting Hill**	$10.55 / VP	$939	1990s constructed industrial facility, incorporating a projected single level office, together with two high clearance warehouses. The property sold previously in October 2013 for $9,300,000 (exclusive of GST).
830 Wellington Road **Rowville**	$9.022 / 10.23%	$1,025	Purpose built (circa 1997) cold store facility. Leased until 28 February 2017 and purchased by Cold Xpress which will owner occupy the premises.
26-32 Evolution Drive **Dandenong South**	$5.38 / 6.82%	$1,245	Recently constructed industrial facility. Securely leased to AusStar Holdings International Pty Ltd for an initial five year term.

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