Australia Industrial – August 2023

SPOTLIGHT
Savills Research

Shed Briefing

savills

Low vacancy persists ● Rent growth eases ● Yields expand ● Investors still bullish on outlook

Tide beginning to turn?

Despite sticky inflation, the prospects for stability after two rate pauses might be the catalyst needed to lift activity.

Deals flow has slowed

The bid-ask spread between purchasers and vendors has widened further in recent months. Deal flow has slowed, and yields have moved out, with some repricing underway. While higher interest rates are making it harder for some transactions to move forward, particularly for investors with significant leverage or shorter-term mandates, opportunistic capital has started to return.

Macro drivers supporting demand

There has been a sharp rise in rental rates over the last two years, but there are very early signs that the pace of this growth is starting to ease. However, the strength in the occupational market is steadfast, with its historically low vacancy rate and rebound in some macro drivers, including the faster than expected recovery in Australia's population growth rates. This is sustaining investor interest and, notably, attracting new capital. The preference for global capital to increase exposure to Australia will play a significant role in unlocking investment activity later this year and into 2024.

Cushioning the impact

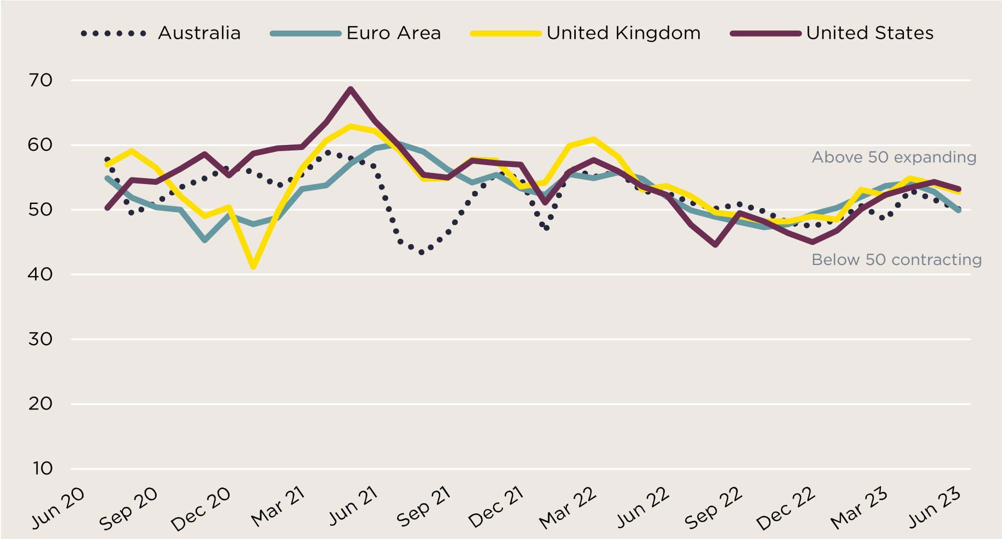
The household savings rate has fallen below its pre-pandemic level and is at its lowest level in 15 years, which suggests there will be increased caution in the coming months. However, the tight labour market, with an unemployment rate of 3.6% on average since April 2022, will continue to support wage growth and cushion the decline in savings. The rebound in the population growth rate and rise in wage growth will also provide support for future growth prospects and help fund household consumption, and ultimately the demand for industrial and logistics floorspace.

Prospects for rate stability after pause?

The RBA has left its cash rate at 4.10% for two straight months. The pause has triggered a shift in the outlook for Australia's current tightening cycle, with many economists now suggesting that the window for further tightening is closing. Consumer spending has slowed in recent months, with retail sales growth exclusively due to spending on food, dining out and takeaway, with spending being cut back everywhere else. Most economists and policymakers alike expect that the rate hiking cycle will end soon, and eventually policy rates will fall in the future. This will provide some relief to investors and likely boost investment activity going into 2024.

PMIs points to modest growth in 2023 as economy responds to rates

Purchasing Managers Indices (level above 50 denotes expansion)



Source Savills Research / IHS Markit

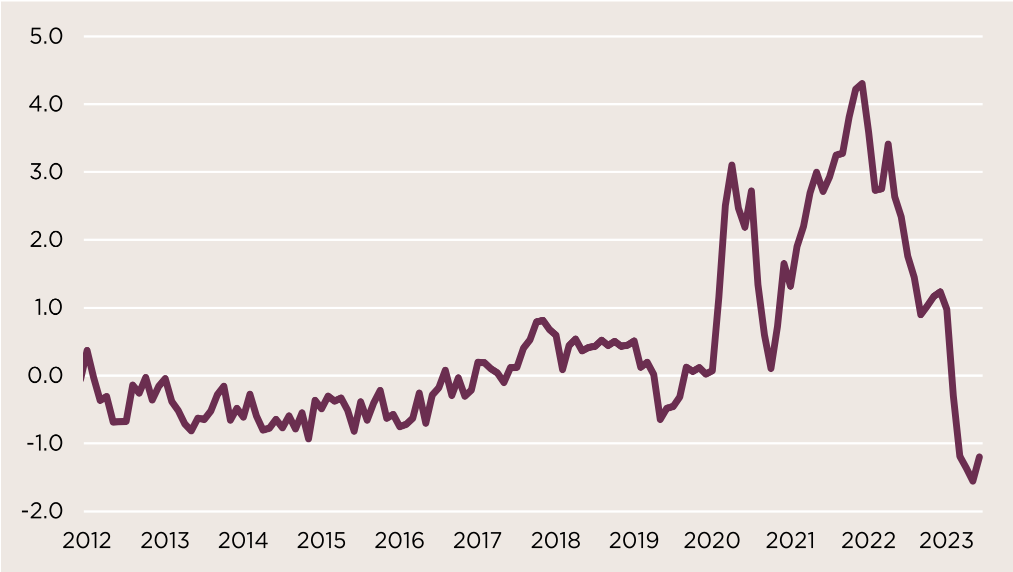
Katy Dean
Head of Research
Research & Consultancy
kadean@savills.com.au

Supply chains recover

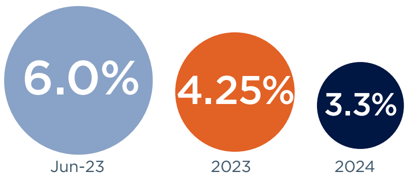
Survey activity, such as the purchasing managers indices (PMIs), which are strongly correlated with GDP growth, are pointing to modest growth in 2023. Supplier delivery times have shortened, effectively reversing the backlogs across the supply chain seen a year ago. This is contributing to a decline in inflation. The New York Fed's Global Supply Chain Pressure Index (GSCPI) on the right, shows the current state of the logistics industry and highlights the dramatic change over the last year.

The index has now declined to below the pre-pandemic stress levels, with every component of the global supply chain seeing improvement, including the price of shipping containers, air cargo, trucking and warehouse capacity. The pricing now favours retailers and manufacturers, with direct flow on effects to logistics. The shift in demand has allowed businesses to restock inventories back to desired levels, which for many industries is higher than they used to be, providing a buffer against future disruptions.

Global supply chain pressures ease, index falls to record low
Global supply chain pressure index



Source Savills Research using Federal Reserve Bank of New York, Global Supply Chain Pressure Index https://www.newyorkfed.org/research/gscpi.html.
**index integrates transportation cost data and manufacturing indicators to provide a gauge of global supply chain conditions (includes Baltic Dry Index, Harpex, Airfreight cost indices, PMI surveys)



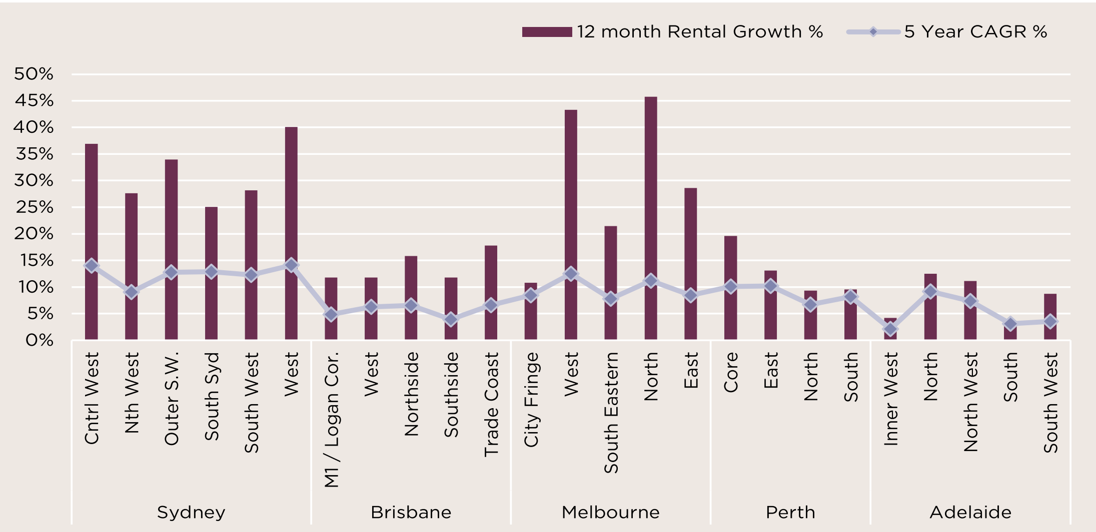
Source RBA inflation forecasts

Supply chain pressures have eased since the start of 2022. Further improvements could help reduce inflation to 3.25% in 2024.

Record rent growth easing

Despite a slowdown in some drivers behind demand, vacancy remains low as rent growth rates continues to surprise on the upside.

Rent growth is still running well above its average
Annual Prime Rental Growth Rates vs 5 Year CAGR % (by submarket)



Source Savills Research

Persistent low vacancy continues to benefit rental growth rates

As underlying fundamentals continue to cement the tailwinds for growth

Rent growth rates easing but still at historic levels

There has been minimal movement in the already record low vacancy rate over the quarter, which remains below 1.0% in some submarkets, and rents continue to rise.

Although growth rates are still above historic levels, with annual growth for prime rents averaging nearly 20% nationally, compared to its long-run average of 4.1%, there are early signs the pace of this growth is starting to ease.

Tale of the cities

Sydney prime net face rents grew 31.5% over the year, following a 5.9% push in Q2. Melbourne has been similarly strong, with rents growing on average 27.2% Y/Y, after a 6.3% rise in Q2. Brisbane grew 14% Y/Y and 3.7% in Q2, while Adelaide saw 8.0% average rise Y/Y and 2.7% in Q1. Perth rents rose 13.0% Y/Y but after averaging +5.3% growth in Q1, held in Q2.

Despite headwinds, income outlook positive

Compared to three years ago, prime rents have grown by 42% and secondary, nearly 50%, increasing the potential for rent reversion to market in most markets. This continues to support the outlook for income growth for investors and mitigate a large proportion of the yield expansion that has occurred.

Reflecting the tightness in the market, most major REITs are still reporting 99-100% occupancy rates. While the uptick in rents is supporting the development pipeline, economic headwinds may lead to delayed decision making and push out the timing on some development starts, as well as take-up activity on existing stock to later this year, into 2024.

Vacancy still at historically low levels

Vacancy is as low as 0.6% in some precincts, but on the east coast, vacancy now averages 1.6%. This is slightly up from 1.3% in April, according to SA1 Property. Of the sample tracked by Savills in Perth and Adelaide, vacancy is estimated to be less than 1.0% in core locations.

Demand and low vacancy driving rental growth

Take-up volumes increased during the quarter following an uptick in spec completions

+7.2%
Industrial job ads are up 7.2% Y/Y, with growth led by QLD (+15.5%), SA (+12.5%) and NSW (+9.2%).

+5.4%
Prime net face rents have increased on average 5.4% Q/Q on the east coast.

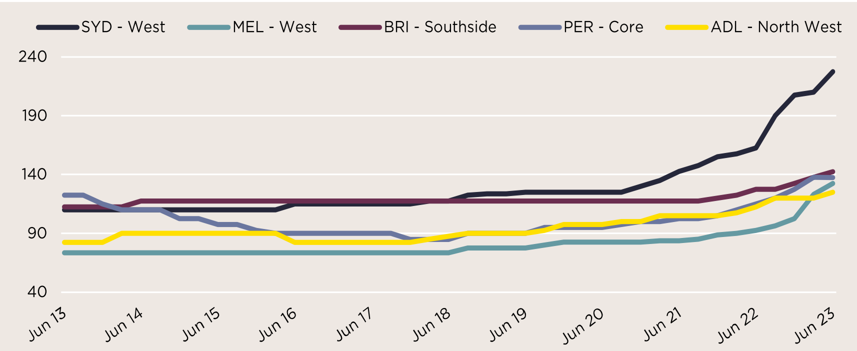
+5.0%
Secondary net face rents have increased on average 5.0% Q/Q on the east coast.

+34%
Industrial development approvals grew +34% Y/Y nationally, well above its 5.3% annual average.

Source Savills Research / ABS / LMIP

Prime net face rents

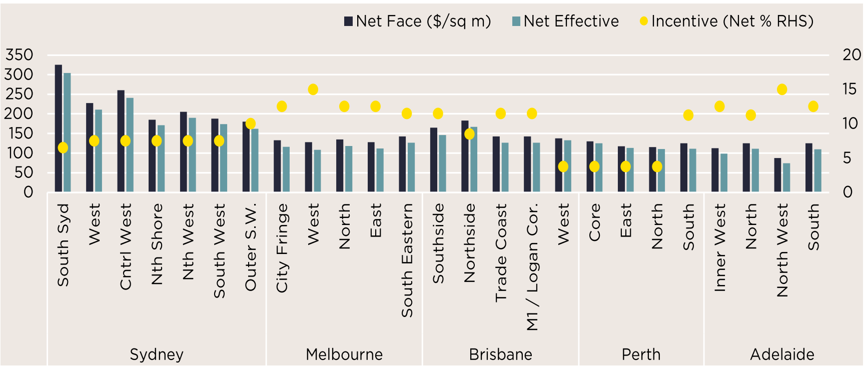
By key core market, $/sqm net face rent average



Source Savills Research

Net face and effective rents v incentives

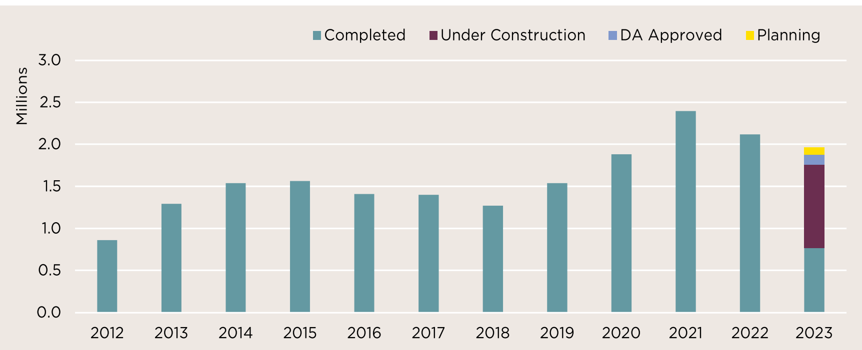
By submarket, prime average $/sqm and %



Source Savills Research

Development pipeline for east coast markets

Estimated sqm by development stage, in millions, sqm (NSW, QLD, VIC)



Source Savills Research

QUARTER HIGHLIGHTS

30% of deals are spec or pre-commitments
Low vacancy has previously limited the churn of existing space to lease, and this was reflected in take-up volumes in Q1, which dipped to c.700,000sqm on the east coast, below its average of about 1 million sqm.

While some companies are being more cautious about their leasing decisions, more than a third of the pipeline due to come online this year is already committed. Low vacancy has hastened some decision making and driven an uptick in spec and pre-commitment leasing activity.

Q2 take-up volumes normalising?
The slight uptick in the vacancy rate and relocation of some tenants during the quarter to new stock has freed up backfill allowing greater churn of existing space, leading to a rise in take-up volumes on the east coast in Q2 to c.1.03 million sqm. This is the busiest quarter since Q3-22. Notably, take up of existing space in Q2 was 60% more than its three year quarterly average. This suggests that the economic headwinds are being partially offset by an even sharper focus on securing supply chains and building in efficiencies to cope with rising costs, including increased labour, transport, and rental rates.

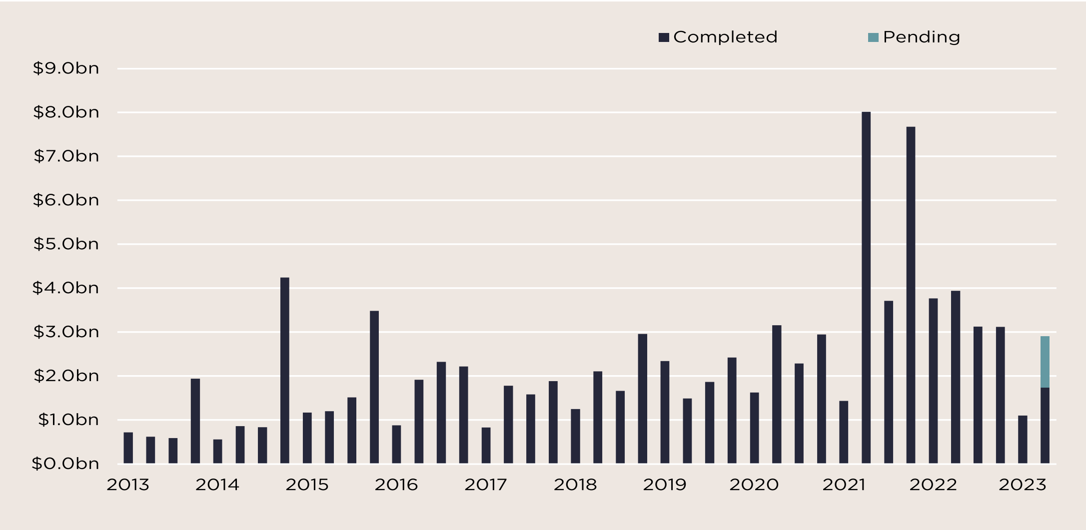
Pipeline still elevated
Savills has tracked c.2.0 million sqm in new developments on the east coast earmarked for completion in 2023, with c.770,000sqm of stock already delivered. This is trending slightly below the last two years, as the timing on some projects for 2022 were pushed into 2023 and 2024 due to higher construction costs, labour shortages and weather in some cases. This has impacted development feasibility and economic rents for new developments have increased, which is also contributing to rental growth.

Land price growth cools
Developers are increasingly focused on building out existing holdings to capture the market rental growth and are less focused on new land acquisitions. As a result, there continues to be signs that land values have peaked in most markets nationally, with small lot prices holding in Q2.

Capital markets adjust

Deal activity remains limited compared to this time last year, but there are a number of transactions in the pipeline, which should help advance any further repricing that's still to occur.

Investment volumes dip from the high of 2021 but still signs of liquidity
$10m+ industrial investment transactions quarter on quarter since 2013



Source Savills Research using MSCI RCA

Investors bullish on industrial, long game wins
Investors are largely positive on the sector, due to its strong underlying fundamentals

Lower volumes but deals still happening
The investment market has experienced a deceleration in transactions compared to previous years. Preliminary estimates for Q2 indicate c$2.4 billion has transacted (+$5m), which is about 30% less than the same quarter last year but notably this is 52% more than what transacted in Q1-23.

In FY annual terms, c.$9.9 billion has transacted. This is about 40% less than the 12 months prior, which was a record period for investment in industrial, however, included several portfolio transactions.

New capital emerging, as investors place all bets on industrial
The bid-ask spread between purchasers and vendors has widened further in recent months, with the cool down in investment volumes limiting sales evidence used to gauge current price levels. However, the strength in the occupational market, with its historically low vacancy rate, persistent rental growth and rebound in macro drivers, including the faster than expected recovery in Australia's population growth rates, is sustaining investor interest and, notably, attracting new capital. For example, Japan's Government Pension Investment Fund has committed $500 million to Blackstone's BREP X fund, which alongside the real estate arm of Ontario Teacher's Pension Plan (through Gateway Capital and Cadillac Fairview), is expected to begin deploying capital into the sector.

Investors remain positive
While deal activity is limited compared to this time last year, the RBA is nearing the end of its tightening cycle. This should unlock more transactional activity in the coming months. The rental growth outlook will be top of mind for investors, particularly those chasing assets with reversion upside potential.

Investors remain bullish on the long term outlook.

Rental growth still helping to offset yield expansion

+20bps
Average market yields for prime and secondary have expanded by 20bps in most markets.

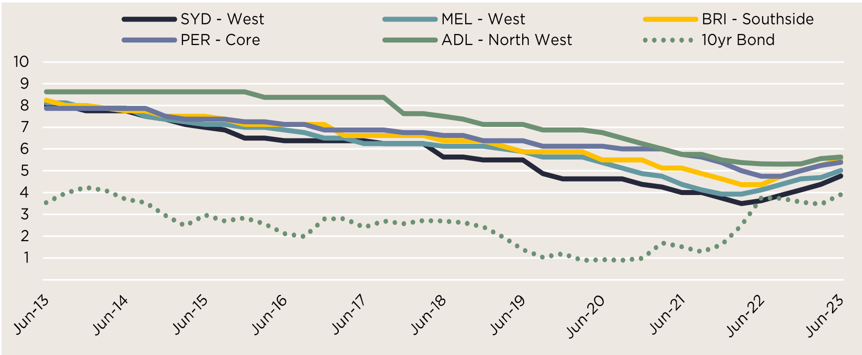
-40%
Transaction volumes have decreased to c.$10 billion in the year to June 2023, down 40% from the c.$16.7 billion rally in the 12 months to June 2022.

50%
Private investors and owner occupiers accounted for 50% of total investment volumes in Q2, compared to its long run average of 30%.

Source Savills Research / MSCI

Key Markets - prime yield & 10yr bond rate

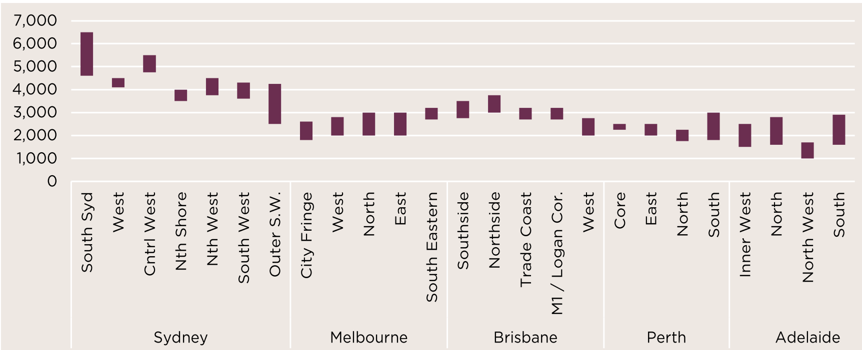
Average prime yield v 10yr bond rate, %



Source Savills Research / RBA

Typical capital value range

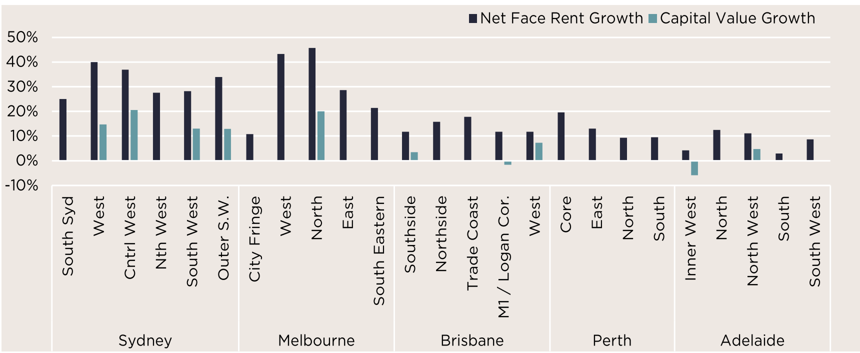
$/sqm prime average by submarket



Source Savills Research

Face rental and capital growth rates

12 month face rental and capital growth rate by submarket, prime averages, %



Source Savills Research

QUARTER HIGHLIGHTS

Yields expand

While there is a significant level of positivity, yields are still moving outwards, with Savills observing an average increase of 25bps for the east coast markets, and between 10-20bps for the southern states. However, values are generally holding with positive rental growth continuing to partially offset the impact yield expansion.

Of the major REITs (eg CHC, DXS, GOZ, CIP) that have revalued their portfolios, the movement in valuations has been relatively modest (-2.1% to +0.1%) from their December 2022 book values, despite their cap rates rising between +31 and +60bps over the same period.

Positive rent reversion

The potential for positive rental reversion across most markets continues to support investment demand. Demand for space still outstrips supply in most markets so rents are rising - prime is up +20% on average Y/Y. With a restricted supply pipeline expected to hold vacancy at low levels, even as some firms adjust inventory levels, the outlook for investment into the sector remains intact.

Privates and owner occupier activity rises

There has been an increase in owner occupier and private investor activity, with these buyers accounting for 50% of activity (by volume) in Q2 – up from its long-run average of 30%. The trend suggests that private capital and lower leveraged buyers are acting opportunistically.

Sale-leasebacks to unlock liquidity

During the quarter, there were two sale and leaseback transactions of scale, including the sale of the Bega Cheese (Vegemite) site in Melbourne to Charter Hall for $114.6m, and Allmex selling its Sydney site to ESR on a five year leaseback for $143m. Although ESR has long-term plans to redevelop the Sydney site into a multi-level building, the shift could signify that there is renewed interest in the sale and leaseback financial structure to help with cash flows.

City Highlights

Historically low levels of available space continue to support strong rental growth rates, highlighting investor focus on structural tailwinds to drive future returns.

Summary - Key Prime Averages

Q2-2023 indicators by sub-market

	Net Face Rent $/sqm	Market Yield (%)	IRR (%)	Capital Value $/sqm	Land Value $/sqm
SYD - South Syd	325 (+4.0%)	4.25 (n/c)	6.13 (n/c)	5,550 (n/c)	3,750 (n/c)
SYD - West	228 (+8.3%)	4.75 (+38 bps)	6.38 (+25 bps)	4,300 (n/c)	1,625 (n/c)
SYD - Cntrl West	260 (+6.1%)	4.25 (n/c)	6.13 (n/c)	5,125 (+4.6%)	2,250 (n/c)
SYD - Nth West	185 (n/c)	4.75 (+38 bps)	6.38 (+25 bps)	3,750 (n/c)	1,500 (n/c)
SYD - South West	205 (+3.8%)	4.75 (+25 bps)	6.13 (n/c)	4,125 (n/c)	1,778 (n/c)
SYD - Outer S.W.	188 (+15.4%)	4.75 (+25 bps)	6.38 (+25 bps)	3,950 (+4.6%)	1,318 (n/c)
MEL - City Fringe	180 (n/c)	4.81 (+31 bps)	6.13 (+25 bps)	3,375 (n/c)	2,625 (n/c)
MEL - West	133 (+7.7%)	5.00 (+31 bps)	6.13 (+25 bps)	2,200 (n/c)	950 (n/c)
MEL - North	128 (+8.1%)	5.13 (+25 bps)	6.25 (+25 bps)	2,400 (n/c)	900 (n/c)
MEL - East	135 (+10.2%)	5.00 (+31 bps)	6.13 (+25 bps)	2,500 (n/c)	975 (n/c)
MEL - South Eastern	128 (+8.5%)	5.00 (+31 bps)	6.13 (+25 bps)	2,500 (n/c)	850 (n/c)
BRI - Southside	143 (+3.6%)	5.50 (+25 bps)	6.25 (+13 bps)	2,950 (n/c)	525 (n/c)
BRI - Northside	165 (+3.1%)	5.50 (+25 bps)	6.25 (+13 bps)	3,125 (n/c)	675 (n/c)
BRI - Trade Coast	183 (+4.3%)	5.25 (+25 bps)	6.13 (+13 bps)	3,375 (n/c)	750 (n/c)
BRI - M1 / Logan Cor.	143 (+3.6%)	5.50 (+25 bps)	6.25 (+13 bps)	2,950 (n/c)	450 (n/c)
BRI - West	143 (+3.6%)	5.50 (+25 bps)	6.38 (+25 bps)	2,950 (n/c)	400 (n/c)
PER - Core	138 (n/c)	5.38 (+13 bps)	6.63 (+13 bps)	2,375 (n/c)	500 (n/c)
PER - East	130 (n/c)	5.38 (+13 bps)	6.63 (+13 bps)	2,375 (n/c)	500 (n/c)
PER - North	118 (n/c)	6.00 (n/c)	7.00 (-28 bps)	2,250 (n/c)	450 (n/c)
PER - South	115 (n/c)	5.88 (+13 bps)	7.00 (n/c)	2,000 (n/c)	350 (n/c)
ADL - Inner West	125 (n/c)	5.50 (+25 bps)	6.75 (+25 bps)	2,400 (-2.0%)	750 (n/c)
ADL - North	113 (+7.1%)	5.75 (+19 bps)	6.75 (+6 bps)	2,000 (n/c)	250 (n/c)
ADL - North West	125 (+4.2%)	5.63 (+6 bps)	6.75 (+6 bps)	2,200 (n/c)	350 (n/c)
ADL – South	88 (+2.9%)	6.75 (+19 bps)	7.63 (+6 bps)	1,350 (n/c)	213 (n/c)
ADL - South West	125 (n/c)	5.75 (+25 bps)	6.88 (+6 bps)	2,250 (n/c)	650 (n/c)

Source Savills Research
3 month change shown in brackets, land values reflect 'serviced & benched' sites (3,000 - 5,000 sqm).

Quarter Highlights

Demand and low vacancy driving rental growth as yields expand

+4.1%

Prime Rents
Average national increase prime net face rents Q2-2023

+4.3%

Secondary Rents
Average national increase secondary net face rents Q2-2023

+20bps

Prime Yields
Average change in blended prime yields Q2-2023

1.6%

Vacancy
Average vacancy on the east coast is 1.6% in Q2 2023 (SA1 Property).

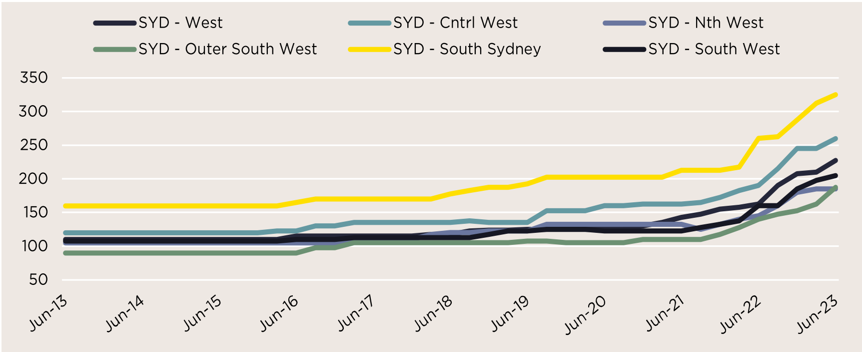
Source Savills Research / SA1 Property

Sydney

Yields expand but structural tailwinds continue to drive rental growth.

Prime net rents have increased on average 4.4% Q/Q

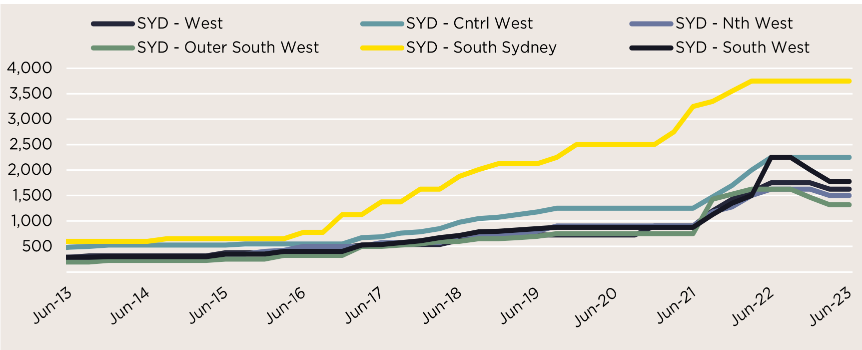
Prime Net Face Rents by Precinct, $/sqm average



Source Savills Research

Land prices start to fall

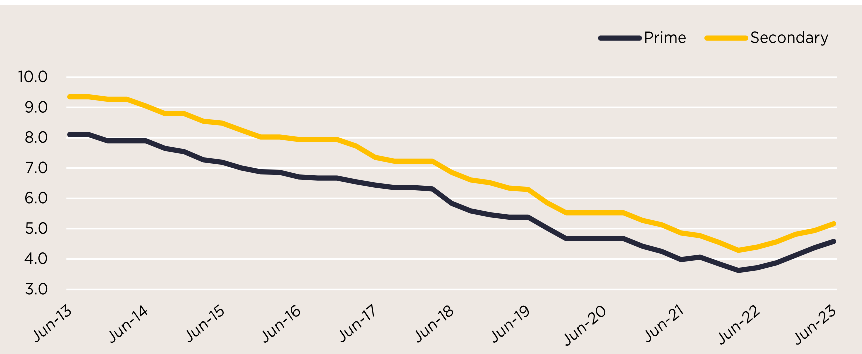
Land Values by Precinct, Small Lots, $/sqm, average



Source Savills Research

Prime and secondary yields still expanding

Prime vs secondary market yield, % average



Source Savills Research

QUARTER HIGHLIGHTS

Investment dip, but deals are still on
There remains some constraint on investment activity, with volumes down c.45% Y/Y. However, the persistent low vacancy rates and rental uplift narrative continue to drive demand from investors. The only limiting factor appears to be the reduced volume of available properties on the market. Despite this, property values remain steady even as yields show some outward movement.

Industrial still preferred
Investment volumes reached c.$903 million (+$5m) in Q2, up from c.$814 million in Q1. More than a third of these transactions were assets selling above $100 million. While there are lower investment volumes, as a share of total sales, this activity is trending above its average, 33% share vs its average 19% share, indicating that the market is still attracting buyers.

Prime yields expand but less in secondary
On average prime yields moved outwards 30-40bps. However, no change in yields was observed in the Central West or South Sydney, reflecting the robust nature of urban/last-mile locations and growth due to structural drivers, including the ongoing expansion of e-commerce. In secondary, yields expanded on average of 20bps in Q2.

Persistent rental growth
On a blended basis, prime net face rents are up 5.9% Q/Q (+31.5% Y/Y). There continues to be strong growth in the secondary market, which faces similarly low vacancies as the prime segment but its pace is slowing. On a blended basis, secondary face rents have increased 3.4% Q/Q and are up 32% on average over the year.

Vacancy near 1.0%
The average vacancy rate is estimated at 1.1% (+3,000sqm), according to SA1 Property, with some pockets across the precincts still averaging 0.5-0.6%.

c.300,000sqm has been leased in Q2, with spec and pre-commitment leasing activity accounting for c.40% by volume. Activity is trending close to the levels seen over the last two quarters but remains well below the peak periods in 2020 and 2021, with the historically low vacancy rate impacting direct leasing activity.

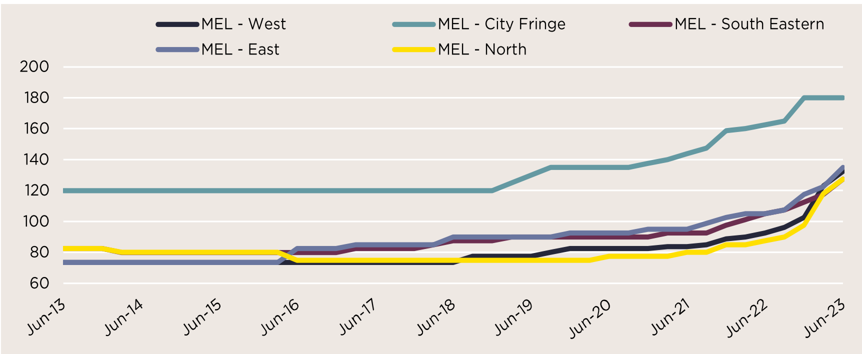
Land rates start to fall from their peak
By precinct, small lot prices in the South West and Outer South West have declined c.20% Y/Y, and c.7.0% in the North West and West. The prices for medium and larger lot sizes have started to shift slightly as transactions have cooled, suggesting appetite to acquire land at those peak prices is starting to wane.

Melbourne

Despite economic headwinds, rent growth rates are still accelerating as low vacancy persists, alongside an uptick in demand for spec space.

Prime net rents have increased on average 6.3% Q/Q

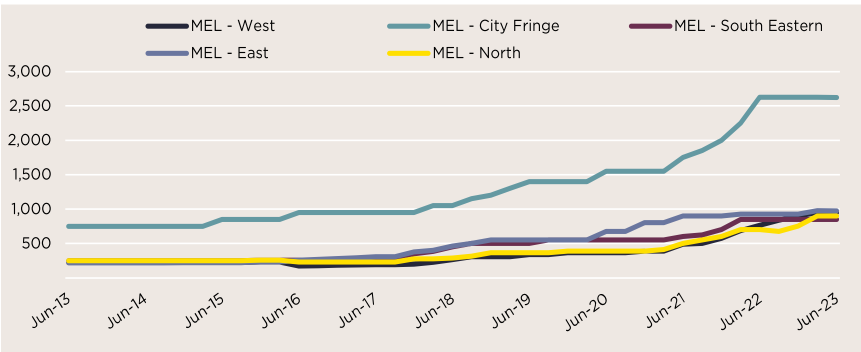
Prime Net Face Rents by Precinct, $/sqm average



Source Savills Research

Land price growth rates now holding

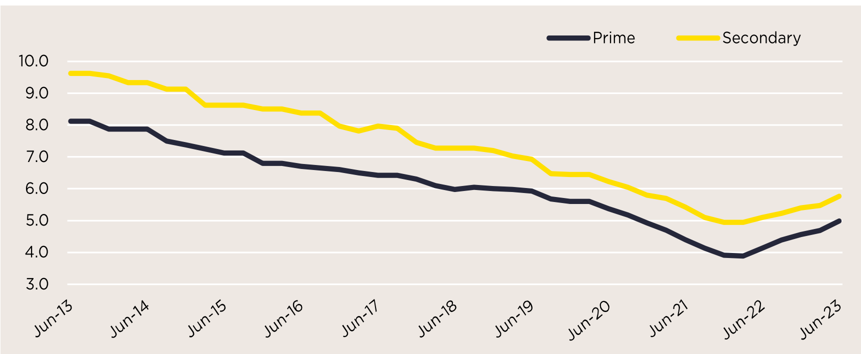
Land Values by Precinct, Small Lots, $/sqm, average



Source Savills Research

Yields expand across prime and secondary

Prime vs secondary market yield, % average



Source Savills Research

QUARTER HIGHLIGHTS

Big deals lift Q2 volumes
Despite a 20% dip in investment volumes Y/Y, deal activity in Q2 is above its quarterly average with c.$859m in transactions recorded (+$5m), up from $339m in Q1 and $655m in Q2-22.

The inflated Q2 volume follows the announcement that Bega Cheese had agreed to a 15-year sale and leaseback deal for the 100-year-old Melbourne factory with Charter Hall for $114.6m and that Gateway Capital and Cadillac Fairview have exchanged contracts for the acquisition of Axxess Corporate Park in Mount Waverly for $315m (less adjustments) from Dexus. While there remains some headwinds for select investors due to cost of debt, there is still appetite to deploy capital, particularly for assets in urban infill and last mile locations, as well as those that offer asset management or repositioning opportunities.

Higher interest rates see further yield shift
There has been further outward yield movement in Q2, with average market yields for prime and secondary softening 30bps. Industrial values seem to be more steadfast, with rental growth still doing its part to offset any significant movement here.

Rent growth persists
On a blended basis, prime net face rents are up 6.3% Q/Q (+27% Y/Y). There continues to be strong growth in secondary, which faces similarly low vacancies as prime, particularly in the West and Northern precincts. On a blended basis, secondary face rents have increased 8.5% Q/Q and are up 26% on average over the year, similar to the trend seen in prime. Land tax thresholds have changed, increasing outgoings in some markets.

Demand for spec
It is estimated that c.254,000sqm has been leased in Q2. While there has been a small amount of pre-commitment leasing activity, the majority of deals struck have been for existing space or spec deals, with transport/logistics and wholesale occupiers the most active takers of space. Vacancy is nearing 1.9% (+3,000sqm), according to SA1 Property, which is a slight increase on the previous quarter. A number of spec projects have been completed, contributing to the uptick, although some submarkets remain closer to 1.0%.

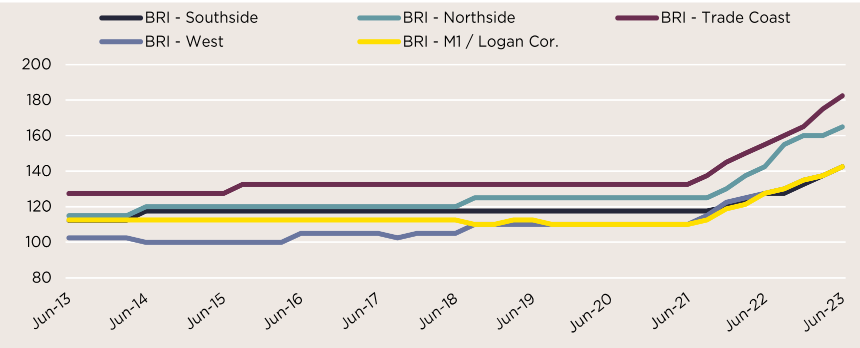
Land rates hold
Land sales have decelerated and there is limited evidence through the last two quarters to suggest there has been further growth in prices. In annual terms, small lots are showing an increase 7.5% and 1-5ha sites 8.6%.

Brisbane

Investors are maintaining their optimism, despite yields moving outwards with demand for pre-committed and spec space supporting the outlook for income growth.

Prime net rents have increased on average 3.7% Q/Q

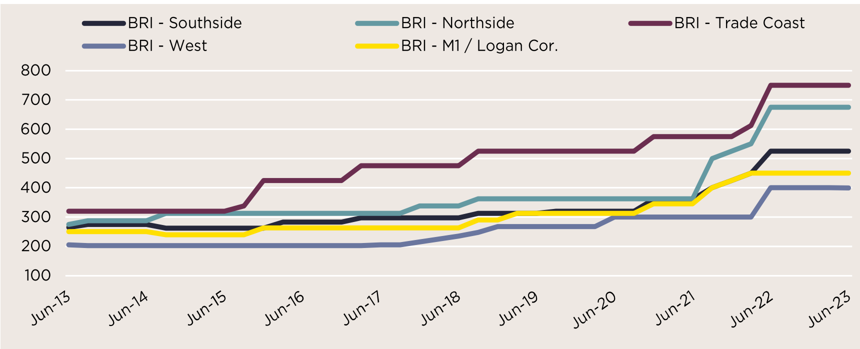
Prime Net Face Rents by Precinct, $/sqm average



Source Savills Research

Land price growth holding

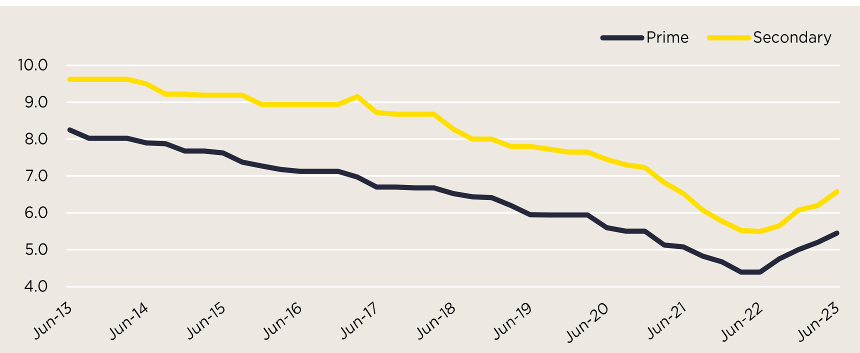
Land Values by Precinct, Small Lots, $/sqm, average



Source Savills Research

Yields move outwards, but values hold

Prime vs secondary market yield, % average



Source Savills Research

QUARTER HIGHLIGHTS

Deals still happening
The ongoing low vacancy and rental uplift story continues to sustain demand from investors that seem only to be held back by the lower volume of stock on the market. Values are holding despite yields moving outwards. A recent example includes Dexus selling their Woolworths leased asset in Stapylton for c.$67m* which is broadly in line with its previous valuation.

Privates and owner occupier activity rises
In Q2, investment volumes reached c.$338 million (+$5m), up from c.$259 million in Q1. Owner occupier and private investor activity in the sub $10m market has increased, accounting for 81% of activity (by volume) in Q2 – about double the long-run average. The trend suggests that private capital and lower leveraged buyers are acting opportunistically, and that some occupiers are transitioning to ownership.

Yields move outwards, but values hold
Prime market yields expanded in Q2, moving on average 25bps Q/Q to average 5.5%, while secondary rose 40bps to average 6.6%. Capital values are reacting less quickly, with rental growth still helping to offset this rise.

Sustained rental growth
On a blended basis, prime net face rents are up 3.7% Q/Q and secondary rents are unchanged. However, Y/Y, secondary rents have increased 14.4%, which is slightly more than prime (+13.9%), further demonstrating the low vacancy profile of the market, despite the uptick in the development pipeline.

Vacancy stays low
Vacancy sits around 1.9% (+3,000sqm), according to SA1 Property, with pockets in the South East, Southside and North still holding a rate closer to 1.0%. Land remains scarce in the Trade Coast, contributing to strong take-up rates in other precincts as they absorb overflow demand.

Spec/precom dominate
c.265,000sqm has been leased in Q2, driven by spec and pre-commitments deals. The uptick in spec development may lift vacancy rates later in the year, however, limited new supply in the more constrained markets will help to offset this as demand levels start to normalise from their recent robust pace.

Land rates still stable
After surging nearly 60% over the two years between June 2020 and June 2022, land values continue to hold. There have been few transactions compared to the previous two year period, with developers focused on building out existing pipeline.

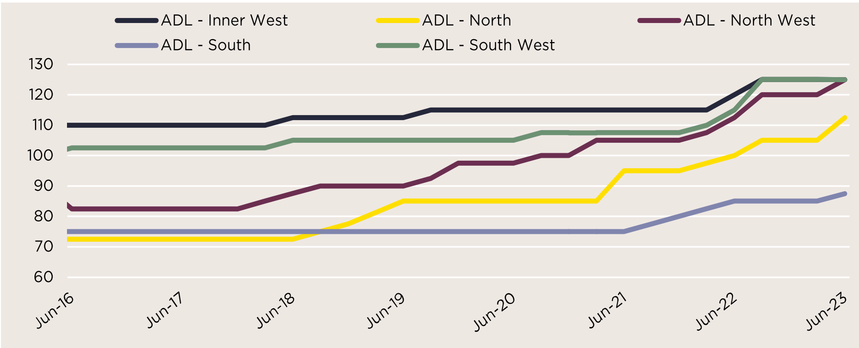
(*final price TBC upon settlement in October)

Adelaide

Capital adjusts to economic headwinds, resulting in a slowdown in investment activity but low vacancy is sustaining investor optimism for the outlook.

Rental growth rates start to ease in some markets

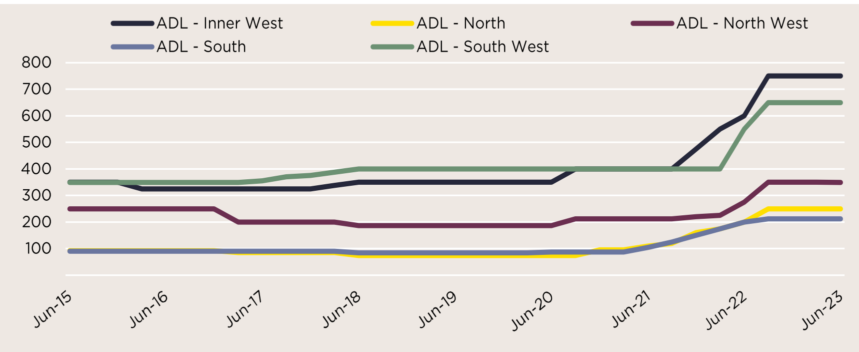
Prime Net Face Rents by Precinct, $/sqm average



Source Savills Research

Land price growth now stable

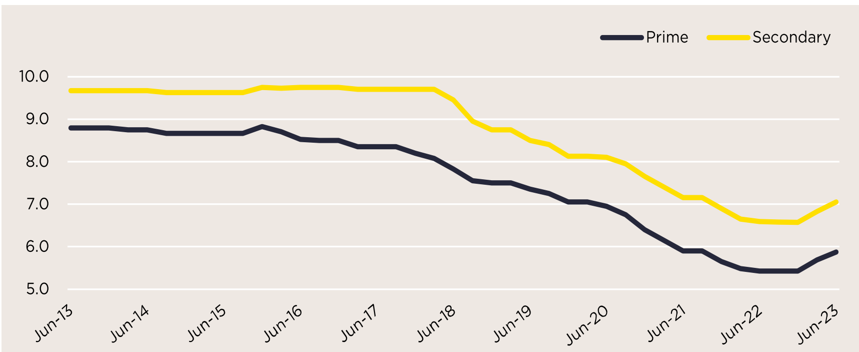
Land Values by Precinct, Small Lots, $/sqm, average



Source Savills Research

Yields continue to soften in prime and secondary

Prime vs secondary market yield, % average



Source Savills Research

QUARTER HIGHLIGHTS

Investment slows
Transaction volumes totalled c.$149 million (+$5m) in Q2, up from c.$68 million in Q1 and down from $217 million in Q2-2022. Despite the cooling of investment transactions over the last few quarters, activity is still running above its Q2 decade average of c.$115 million.

Yields expand
In blended terms, prime yields average 5.9% and secondary averages 7.1%. Both prime and secondary market yields expanded in Q2, moving outwards an average 20bps since Q1. Adelaide's North prime yields appear to be the most resilient to interest rate pressures, softening 6bps over the June quarter. As returns increase in a 'risk-on' environment, the focus shifts to leasing quality underpinned by high occupancy and extended lease terms, favouring income security.

Pace of rental growth picks up
On a blended basis, prime net face rents are up 2.7% Q/Q (+8.0% Y/Y). There has been a stronger growth rate of 7.2% Q/Q in the secondary market, with lower vacancy starting to limit the churn of stock, particularly in the Inner West and South West. Secondary rents are up 12% on average over the year, slightly above the trend seen in prime, suggesting demand is still outpacing supply.

Tenants renew early
Scarcity of assets and intricacy of planning and delivery of new supply has seen some tenants renew lease terms early to guarantee security of tenure.

Manufacturing to grow
According to the SA Government, manufacturing will remain the largest employer and will grow its market share by 2030. This will be primarily driven by jobs related to the future submarine programs across Adelaide's Outer North and West, earmarked as the city's next major employment centres.

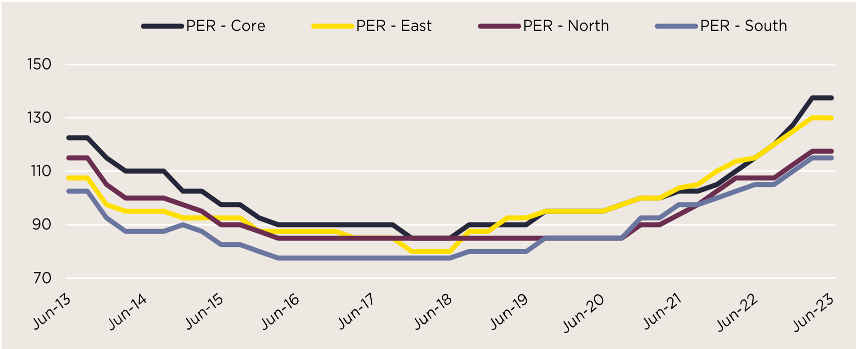
Land rates hold
On average, the value of small lots (<5,000sqm) remained unchanged over the quarter, however on an annual basis are up 21.3% Y/Y. Of the precincts, the North West experienced the largest growth rate of 27.3% Y/Y, with an average of $350/sqm, however, the Inner West and North have grown at near equal rates of 25% Y/Y to average $750/sqm and $250/sqm respectively.

Perth

After strong growth over the last three years, rental growth rates begin to stabilise, as capital adjusts to rising interest rates.

Prime net rent growth stabilises

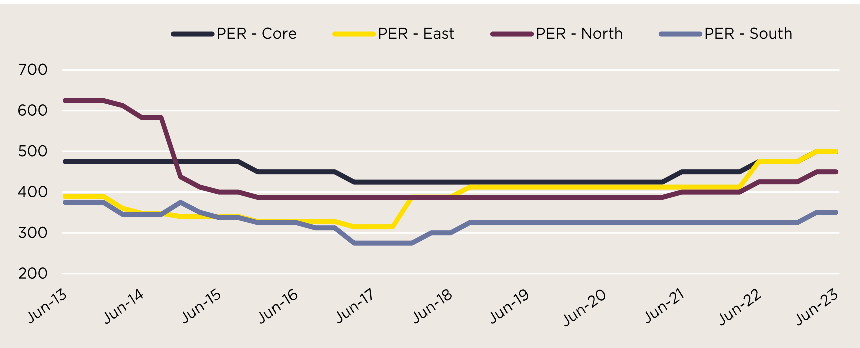
Prime Net Face Rents by Precinct, $/sqm average



Source Savills Research

Land value growth shows signs of easing

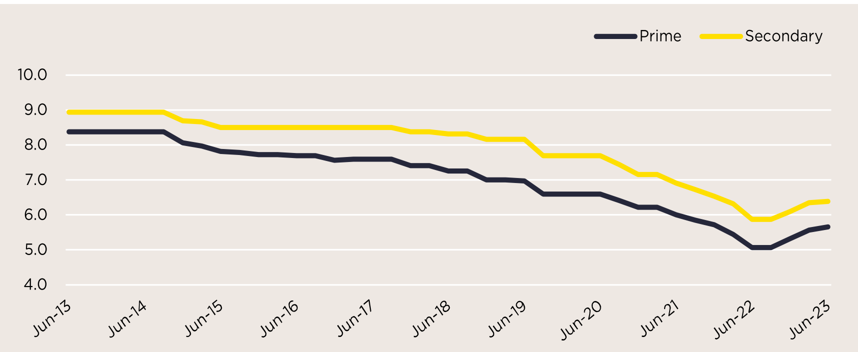
Land Values by Precinct, Small Lots, $/sqm, average



Source Savills Research

Yields soften but pace slows

Prime vs secondary market yield, % average



Source Savills Research

QUARTER HIGHLIGHTS

Investment volumes have been subdued
The tightening of the monetary policy and persistent inflation over the last year has seen some investors exercise more caution and take a 'wait and see' approach. Subsequently, the bid-to-ask spread has widened, resulting in subdued transaction activity in 2023 when compared to corresponding periods.

Sales volumes ($5m+) reached $69 million in Q2, this is down c.45% when compared to Q2 2022 ($126m), however, is slightly up on Q1 (+36%).

Yields soften 10bps, but pace slowing
Further yield movement was observed over the quarter, but the pace has begun to slow due to limited transactions. In Q2, average prime market yields softened 12.5bps to 5.7%, following two quarters of 25bps outward movement.

Secondary yields have held at 6.4% since Q1 and have expanded 50bps over the last 12 months.

Capital values held in Q2 with rental growth and limited transactional evidence helping justify the no change in values.

Annual rental growth offsets yield expansion
Average prime net face rents are holding stable following a 13% rise over the last 12 months and nearly 40% growth over the last three years. On a blended basis, prime net face rents average $125/sqm pa, up from an average of $113/sqm a year ago.

Land value growth rates stable
Rising construction costs at the same time as other economic headwinds, including labour shortages, inflation, and higher interest rates, have resulted in fewer transactions and new sites coming to the market. As a result, there's limited evidence to support any further uptick in land rates in Q2.

Annually, the price of small lots (>5,000sqm) has increased on average 5.9%, while medium lots (1-5ha) are up 6.9%. Further price stabilisation is likely to provide some confidence to developers looking at feasibility in the second half of the year.

Savills Research
For more information about this report, please contact us

Research & Consultancy

Katy Dean
Head of Research
+61 2 8215 6079
kadean@savills.com.au

Chris Naughtin
National Director
+61 2 8215 8832
chris.naughtin@savills.com.au

Barbara Cocca
Research Analyst
+61 2 8215 6078
barbara.cocca@savills.com.au

Harry Patchett
Research Analyst
+61 2 8215 8851
hpatchett@savills.com.au

Industrial & Logistics

Michael Wall
National Head
+61 415 057 637
mwall@savills.com.au