



Melbourne Industrial Property Market Forecasts and Strategies 2011 – 2021



EXTRACT TO INDICATE THE GENERAL NATURE OF THE REPORT

COMMERCIAL PROPERTY

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1. INTRODUCTION

1.1 Introduction and major objectives of this report

Melbourne Industrial Property 2011 to 2021 is the twelfth comprehensive study of the Melbourne industrial market undertaken by BIS Shrapnel.

After starting to recover from the GFC-triggered downturn, underlying demand for industrial property in Melbourne has weakened this year, in line with the softening national and Victorian economies. Nonetheless, we estimate that the strength of demand has absorbed much of the excess capacity created during the downturn, particularly in warehouses. As a result, vacancy rates amongst prime stock (particularly larger than 5,000 square metres) are low.

On the supply side, industrial development work done has recovered moderately since the 2009–10 trough, but the recovery in activity has been sporadic, reflecting the commencement of a handful of large warehouse/distribution projects and a rebound in factory activity from very low levels. Even so, the value of work done remains some 40% below the 2006–07 peak level. Most activity this year has been concentrated in the west, with the south-east a distant second. New industrial supply is constrained because construction remains broadly unfeasible at current market rents, yields and land values, with pre-commitment rents well above rents for existing prime space in most regions. However, low land values and strong competition in the pre-lease market—particularly in the west—means the gap is very narrow here.

The combination of solid demand and limited supply has pushed down vacancies amongst prime properties, encouraging rental growth across all regions. In turn, a recovery in the investment markets has also been evident. Private investors have been the most dominant at the lower end of the market, with a number of portfolio sales and joint venture deals increasing the dominance of a handful of major A-REITs at the top end, but also reflecting foreign investor demand for institutional grade assets. Whilst the funding constraints on the major industrial and diversified A-REITs have eased, there are still many smaller players who remain under pressure to sell properties to reduce gearing.

Given the patchiness of the recovery to date, will the road to recovery continue along a bumpy path or start to smooth out?

Our study provides market players with vital information to better understand prospects for the market and tailor their business strategies to suit.

In our latest study, we assess the outlook for the Victorian economy and its impact on the demand for and supply of industrial space in Melbourne. In turn, we address the implications for rents, yields and investment returns for different grades of industrial property, looking beyond the current market uncertainty to assess prospects over the medium to long term.

We examine in detail the following questions:

- With negative business and consumer sentiment grabbing the headlines, are we about to enter another economic downturn?
- When will construction recover and what are the pre-conditions?
- Will the recent recovery in rents be sustained?
- What opportunities do the current market conditions present? Is now a good time to enter the market? Is land a good investment?
- How does Melbourne industrial property compare with other property investment opportunities?

1.2 Report outline

The **Executive Summary** provides a concise summary of our findings with respect to the industrial property market, together with our forecasts of rents, yields, values and investment returns.

In **Chapter 2** we examine demand issues within the Melbourne region relevant to industrial property. We provide an outlook for the Australian and Victorian economies over the coming 10 years before identifying and forecasting the principal drivers of demand for industrial space. Our conclusions determine aggregate demand for industrial space over the next decade.

Chapter 3 analyses supply issues within the Melbourne region. Supply issues focus on the impact of the building cycle on warehouse and factory construction, the current state of play and future outlook for new supply. In this chapter we also look at regional patterns of industrial land supply, planning influences and land values.

In **Chapter 4** we provide our forecasts for rents, yields and values within the individual regions. Prime, secondary and high tech rents and values are analysed over the last cycle in both current and constant price (inflation adjusted) terms and are forecast to 2021.

Finally, **Chapter 5** examines the prospects for investment returns from Melbourne industrial property and the implications for investment (both active and passive) and leasing strategies. We seek to answer the question: is Melbourne industrial property a good investment?



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