RESEARCH

JUNE 2013

MELBOURNE CBD

Retail Market Brief

HIGHLIGHTS

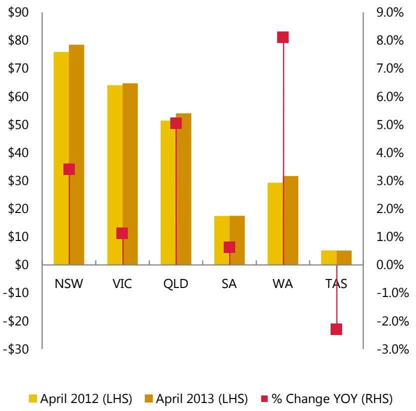
- The Knight Frank CBD retail survey comprises 1,646 shops within the CBD Core, of which 43 were recorded as vacant resulting in a vacancy rate of 2.61%, up from 2.47% recorded in June 2012. Over the year to June, vacancy within Street Front shops increased from 2.70% to 3.93%, its highest level in five years. The vacancy rate in Arcades rose from 0.67% to 2.00%, while in contrast, vacancy within Shopping Centres fell from 3.11% to 1.08%
- Clothing retailers and food retailers remain prevalent within the Melbourne CBD retail core, with Guzman Y Gomez, Mad Mex and Bonbons Bakery among some of the recent incoming tenants. Menswear retailers in particular became more prominent, underpinned by Bell & Barnett opening three stores over the past six months.
- CBD retail sales, greater than $1 million in the 12 months to June 2013 totalled $82.57 million across 16 properties. The transactions achieved yields ranging from 3.5% - 7.5%, with a median of 5.1%. Supported by the increased levels of transactional activity over the past year, yields are expected to firm slightly as investors continue to be drawn to prime retail investment opportunities.

Economic Snapshot

The Australian economy and its growth prospects remain hindered by the health of the global economy. The high $AUD has impacted the traditional "bricks and mortar" retail market adversely with consumers instead spending more on offshore travel and new cars. Despite the cash rate being at a 53-year low of 2.75%, recent cuts seem to have had little impact with retail sales only recording modest growth over the past year.

In April 2013, the ABS recorded 1.1% (year on year) growth in Victorian retail turnover. In contrast, Western Australia, Queensland and New South Wales recorded solid growth of retail sales with 8.1%, 5.1% and 3.4% respectively. Tasmania was the only state to record a fall in retail sales.

Figure 1
Retail Turnover by State
12 Months to April-13 ($ billion)

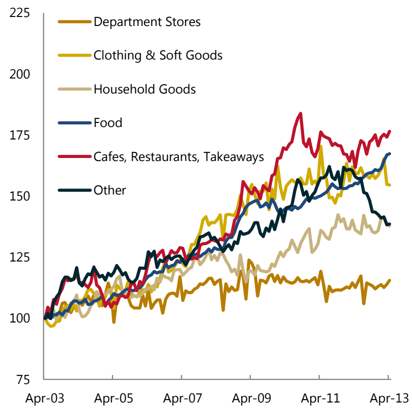


Source: ABS

Analysis of retail turnover by industry in the 12 months to April 2013 shows that in Victoria, with the exception of "Other" retailing, all sectors of retail turnover increased. The "Food" (supermarket, grocery and liquor) category experienced the largest increase at 4.8% (year on year) while "Café, Restaurant & Takeaway food" rose by 1.8% (year on year) and "Clothing, Footwear and Personal Goods" saw a 2.5% increase (year on year). The only drop in retail turnover came from "Other" (newspapers & books, recreational, and pharmaceutical, cosmetic & toiletry) falling by 8.1%.

Total retail trade in Victoria increased slightly during the 12 months to April 2013, to total $64.72 billion from $63.99 billion in the 12 months to April 2012. Despite this modest increase, challenges remain as retailers continue to be impacted by the strength of the $AUD and subdued business and consumer sentiment.

Figure 2
Retail Trade - Victoria
Index: April 2003 = 100



Source: ABS

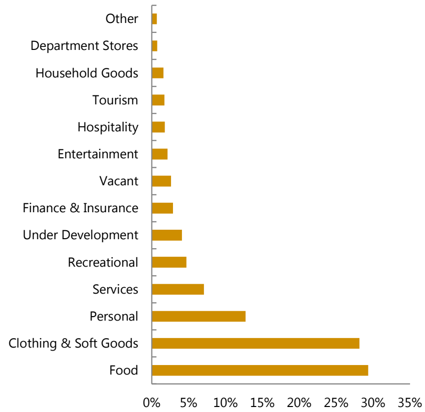
Current retail trade data demonstrates that consumers remain cautious, with discretionary spending still soft. Despite growth in disposable income, consumer spending remains weak as a result of an increase in the household savings rate which remains elevated at 10.6%. Moreover consumers are increasingly taking advantage of the historically high Australian dollar and shopping through online retail channels.

The NAB Online Retail Sales Index (April 2013) reported Australia's online retail spending totalled $13.5 billion and a growth rate of 23% (year on year), a solid result after recording a weaker rate in March of 15% (year on year). Growth within online retailing remains significantly higher than traditional "bricks and mortar" retailing, which grew by only 3.1% (year on year) to April 2013.

Tenancy Mix

The retail tenancy mix in Melbourne's CBD Core is dominated by Clothing & Soft Goods and Food retailers who together account for 57.5% of total occupants. By the number of shops, the next most prevalent categories of retailer in the CBD were Personal (i.e. pharmaceutical, cosmetic & toiletry) and Services (i.e. key cutting & shoe repairs, optometrists, hairdressing and beauty).

Figure 3
CBD Core Tenancy Mix
% of total number of shops (total 1,646)



Source: Knight Frank

Over the past 18 months, food retailers were the most active tenant types, boosting their already large presence in the CBD retail core, a trend that Knight Frank expects to continue. Guzman Y Gomez, Bonbons Bakery and Mad Mex have all recently opened stores, while The Candy Room, Konopizza and Wowcow are expected to open CBD stores later this year. Somewhat surprisingly, men's clothing retailers increased their presence over the past six months with Bell & Barnett opening three stores, whilst international menswear brand Peter Werth opened a pop-up store in Howey Place, testing the market with a view of adding a permanent presence outside of its in-store outlet at Myer.

Table 1
Melbourne CBD Retail Core*
Vacancy by Retail type

	Jun-12 (%)	Dec-12 (%)	Jun-13 (%)
Arcades	0.67	1.34	2.00
Street Frontages	2.70	3.67	3.93
Shopping Centres	3.11	1.61	1.08
Total Retail	**2.47**	**2.55**	**2.61**

Source: Knight Frank
* For definition of Retail Core see back page.

Vacancy & Tenant Demand

Melbourne's CBD retail Core vacancy rate increased over the 12 months to June 2013, rising to 2.61% from 2.47% in June 2012. Over the same period Street Front shop vacancy rose from 2.70% to 3.93%, the highest it's been in five years, whilst vacancies in Arcades rose from 0.67% to 2.00% and Shopping Centre vacancies fell from 3.11% to 1.08%.

The CBD retail market continues to evolve as food retailing becomes more prominent, with the majority of this within cafés and restaurants. Reiterating the ABS turnover data, the increased presence has been aided in the CBD by the increased population and workforce. Current City of Melbourne data reveals that both population and employment within the municipality is outpacing the broader metropolitan region. Over the four year period, population within the City of Melbourne grew by 19% while employment grew by 18.2% to reach around 428,000 workers.

The Westpac Melbourne Institute Index of Consumer Sentiment fell from 104.9 in April to 97.6 in May, representing a 7% drop and its lowest result since August 2012. Despite the recent rate cut, consumer sentiment is in pessimistic territory, which may have been exacerbated by the announcement of the Federal Budget, initiating renewed doubt over the state of the economy.

Rental Levels and Leasing Activity

Melbourne CBD retail rents have remained stable over the past 12 months with the highest rents being achieved within the 'super-prime' retail along the Bourke Street Mall where the rents range between $7,500/m^2 - $10,000/m^2. Prime retail rents range between $2,500/m^2 - $5,000/m^2, while Secondary retail properties achieve rents that range between $1,000/m^2 - $4,000/m^2. Over the past six months global menswear brand Peter Werth has leased a 33m^2 pop-up store at Howey Place on an approximate rate of $4,000/m^2. Meanwhile Dolce & Gabbana's 320m^2 store at the recently completed Mayfair Building at 171 Collins Street was reportedly leased at $4,000/m^2 for space spanning the ground and first floor. Guzman Y Gomez, a Mexican restaurant, leased the former IGA supermarket at 289 Swanston Street, comprising 300m^2 at $1,100/m^2.

Investment Activity

According to the IPD Performance Index, for the 12 months to March 2013, Victorian retail property posted a total return of 8.7% with capital growth of 1.6%. Despite total returns being marginally lower when compared to returns of 12 months ago, Victorian retail returns are well above the five-year average returns of 6.3%. When comparing the total returns amongst states, only Western Australia retail assets recorded higher total returns with 11.2% over the past 12 months.

During the 12 months to June 2013 (sales greater than $1 million), Knight Frank recorded $82.57 million across 16 retail properties. This represented a 69% increase over the 12 months to June 2012, where $48.92 million worth was transacted across 11 retail properties. Private investors continue to dominate purchases accounting for 67% of all transactions, whilst off-shore buyers (17%) and owner occupiers (16%) made up the remainder. The largest sale was 43-53 Elizabeth Street to a private investor for $15.5 million comprising five ground level tenancies leased to tenants including 7-Eleven, Bakers Delight and UAE Exchange. At the time of sale the four office levels above were vacant, providing rental or development upside. The sales transacted over the past 12 months have achieved yields ranging from 3.5% - 7.5% with a median of 5.4%. With increased levels of investment activity anticipated, Knight Frank expects yields to firm slightly over the next 12 months with investors determined to secure prime CBD retail investments in locations with high levels of foot traffic and with blue-chip tenants.

Outlook

The new supply pipeline for the CBD retail market is buoyant, underpinned by the Myer Emporium development by Colonial First State and GIC which is scheduled for completion in late 2013. This development is expected to add approximately 240 tenancies within 46,000m^2 of retail floor space attracting renowned brands like Top Shop, Uniqlo, Sass & Bide and Salvatore Ferragamo among others. Elsewhere, as part of the Collins Square development in the Docklands, Walker Corporation is expected to bring 10,000m^2 of retail space to support the incoming workforce. In addition, several refurbishment projects are scheduled for completion over the next year such as at The Strand Arcade, GPO building and the former DFO development at Southern Cross station.

Although discretionary spending remains soft, a growing working and residential population coinciding with the cut in interest rates should mitigate against significant rises of vacancy in the Melbourne CBD retail market. However retail turnover figures and declining consumer confidence is likely to result in tenants remaining cautious in the short term.

Table 2
Recent Sales Activity Melbourne CBD Retail Market

Address	Price ($ mil)	Initial Yield (%)	NLA (m^2)	$/m^2 NLA	Sale Date
113 Lonsdale Street	2.80	4.34	460	6,087	May-13
21-25 Hardware Lane	6.00	5.00	800	7,499	Apr-13
43-53 Elizabeth Street ^	15.50	4.16	1,730	8,960	Mar-13
188 Little Collins Street	1.65	5.67	33	50,000	Feb-13
1 Queen Street *	11.00	VP	1,400	7,857	Nov-12

Source: Knight Frank
^ Retail component is 100% occupied and accounts for 28% of total NLA. Office component fully vacant at time of sale. * Offers large scope for residential development given its Capital City 1 zoning.

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Knight Frank Research

Rodney Wong
Research Analyst – VIC
+61 3 9604 4608
rodney.wong@au.knightfrank.com

Richard Jenkins
Director – Research VIC
+61 3 9604 4713
richard.jenkins@au.knightfrank.com

Matt Whitby
National Director, Head of Research & Consulting
+61 2 9036 6616
matt.whitby@au.knightfrank.com

Knight Frank Valuations

Joe Perillo
Joint Managing Director – Valuations
+61 3 9604 4617
jperillo@vic.knightfrankval.com.au

Michael Schuh
Director – Valuations
+61 3 9604 4726
mschuh@vic.knightfrankval.com.au

Agency Contacts

Gary Loo
Director – Retail Leasing
+61 3 9604 4743
gary.loo@au.knightfrank.com

Marcus Quinn
Director – Commercial Sales
+61 3 9604 4638
marcus.quinn@au.knightfrank.com

Langton McHarg
Director – Commercial Sales
+61 3 9604 4619
langton.mcharg@au.knightfrank.com

Sandra Wilson
State Director – Retail Management
+61 3 9650 4373
sandra.wilson@au.knightfrank.com

James Templeton
Managing Director – Victoria
+61 3 9604 4724
james.templeton@au.knightfrank.com

Retail Core Definition: Knight Frank's survey covers the key CBD retail precinct as defined as the Core. The CBD retail Core includes all retail premises within the broad boundaries of La Trobe Street to the North, Flinders Street to the South, Spring Street to the East and Elizabeth Street to West.

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