RESEARCH

SYDNEY & BRISBANE CBD INSIGHT—OCTOBER 2016

October 2016

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SYDNEY AND BRISBANE—A TALE OF TWO CITIES

The cities of Sydney and Brisbane have experienced diverging fortunes over the past ten years as the timing and impact of economic drivers have been in play across these cities.

The Sydney CBD at 5.1 million square metres is more than double the size of the Brisbane CBD (2.3 million square metres) and as both are surrounded on three sides by water, this has shaped development and also pushed demand to non-CBD and increasingly fringe urban regeneration sites.

The Brisbane market has seen more decentralisation to immediately adjacent locations, whereas Sydney has many more suburban satellite markets of scale, which has pushed demand further afield. However, centralisation, driven by infrastructure investment, appears to be gaining traction in the Sydney CBD.

Shaping The Markets

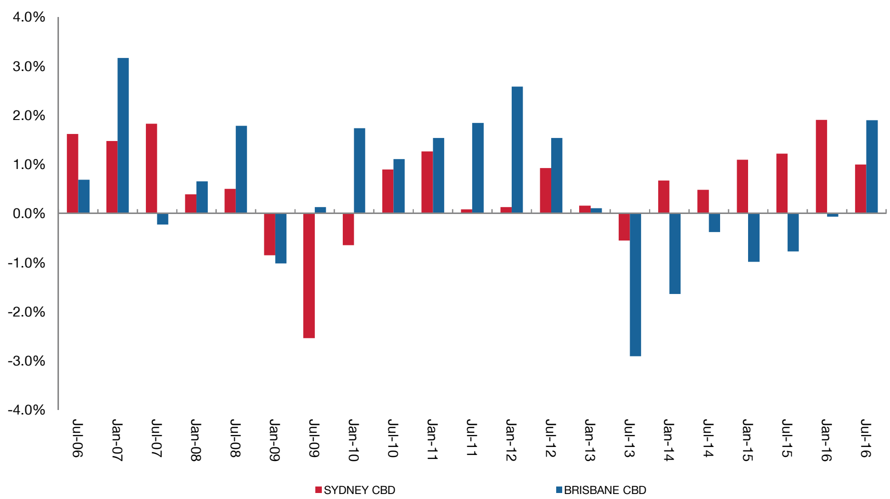
Shaped by the underlying economic drivers, the two markets have achieved periods of strong demand, however at differing speeds and timing. While both cities felt the initial impact of the GFC, Sydney's exposure to the Finance & Insurance sector led to a sharp fall in occupied space during late 2008 and into 2009.

In contrast the Brisbane CBD, boosted by strong conditions in the resources sector, was achieving strong take-up defying the broader national conditions. In 2013, the combined impact of a sudden downsizing in the State Government headcount, vacating circa 70,000 square metres of stock, and the loss of profitability in the resource sector, led to a sharp fall in demand within the Brisbane CBD.

FIGURE 1

Net Absorption Sydney CBD v Brisbane CBD

% Net Absorption as a percentage of total stock, per six month period



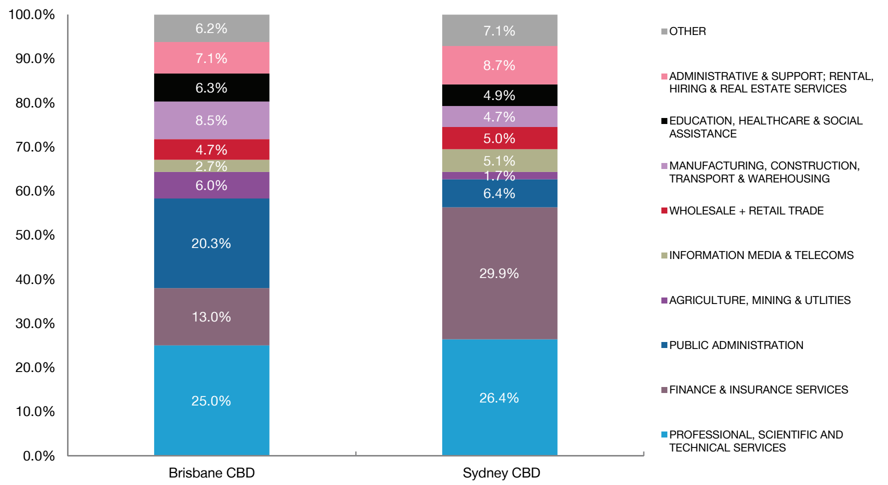
Source: Knight Frank Research/PCA

“CONSIDERING THE MAJOR OFFICE OCCUPIERS FOR THE TWO CITIES, IT IS EASY TO SEE WHY THIS DIVERGENCE HAS EMERGED.”

FIGURE 2

Distribution of White Collar Workers by Industry Type

% of total white collar employment



Source: Knight Frank Research/Deloitte Access Economics

Sydney CBD occupants are dominated by Finance & Insurance Services and has benefitted the most as this sector of the economy has recovered over the past five years

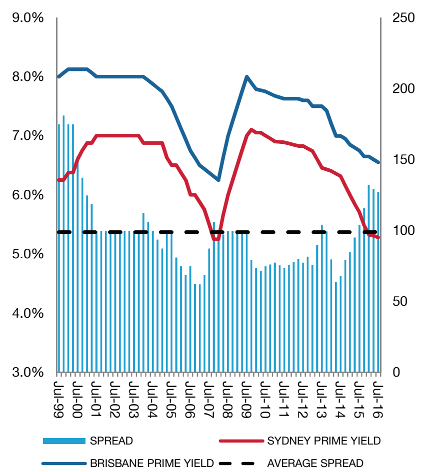
Spurred by a resurgent NSW economy, driven by a huge transport infrastructure pipeline, the Sydney CBD market has been on an improving trend since late 2013, accelerating since then.

Considering the major office occupiers for the two cities, it is easy to see why this divergence has emerged. The industry structure is very different, with 30% of Sydney CBD white collar workers in the Finance & Insurance sector while in Brisbane this is only 13%. In contrast in Brisbane 20% of workers are aligned with public administration compared to only 6% in Sydney, and the mining, manufacturing, construction and utilities sector is double the size in Brisbane. Importantly for Sydney over the past two years, has been the larger exposure to the IT sector, with the technology and creative services sector being a large contributor to growth.

The resources sector has a multiplier effect on office demand and the 8% exposure in Brisbane translates to a greater contribution to the office market; however compared with Perth (with 20% aligned to the mining sector) the Brisbane economy remains relatively broad based, with education and tourism occupiers also prominent.

The Brisbane CBD is constrained by the Brisbane River, concentrating development into a small area.

FIGURE 3
Prime Core Market Yields
Core Market Yield (LHS) & Spread bps (RHS)



Source: Knight Frank Research

Follow The Money

Investment in Australia, particularly office and hotel buildings, has been growing strongly, supported by the relatively higher yields still to be found in the market. In the office market, during 2015 over $9.12 billion worth of property changed hands in Sydney, 57% of Australia's total turnover for the year. Investors, particularly foreign, were attracted to this global city with an improving tenant market and strong Investment fundamentals.

In contrast Brisbane attracted 12% of total office investment at $1.96 billion. As yields for core assets continue to fall under the weight of money seeking a safe return and with the expectation of lower for longer interest rates, there is also a greater weight of funds seeking a relatively higher return.

"THE YIELD GAP BETWEEN SYDNEY AND BRISBANE REACHED ITS HIGHEST LEVEL IN 15 YEARS IN EARLY 2016."

Increasing interest in markets such as Brisbane is now in force, with indications that the negative influences in the tenant market have abated, and an expectation that the government sector is expanding once again.

The yield gap between Sydney and Brisbane reached its highest level in 15 years in early 2016, and there is the potential for this to narrow further in the near future, which is attracting value add buyers to the city and increasing the depth of offshore buyers.

The Future

The mining investment boom contribution to growth is reversing and there is a switch in drivers of the economy towards residential construction, transport infrastructure spending and the services sector including the technology and creative services industries. This is a clear positive for Sydney. However, Brisbane is a diversified economy and besides the large exposure to the business services sector, the government sector is on the cusp of an expansion, following sharp cuts in the preceding three years.

There continues to be divergence in the short term market conditions and rental growth performance in favour of Sydney, however we expect investment and occupier demand to pick up in Brisbane over the coming year, as investors begin to embrace more risk and seek higher relative returns.

This article first appeared in the Knight Frank's Global Cities: The 2017 Report. For more content from Global Cities download the full report at http://www.knightfrank.com/globalcities

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