1 *Rental growth continues led by Sydney*

2 *Land values holding firm*

3 *Transaction volumes subdued*

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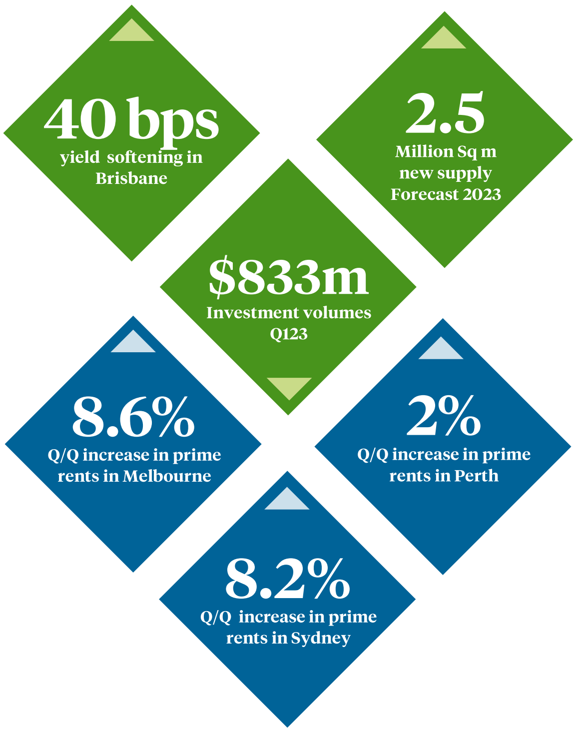
# Australian Industrial Review

**Q1-2023**

# KEY INSIGHTS




**Limited availability is driving widespread rental growth**, but higher funding costs have seen a change in sentiment in the investment market.

**Vacancy rates across the Eastern Seaboard continue to sit at record low levels with 444,681sqm,** a 18% drop in availability over the quarter.

**Investment activity levels was constrained in Q1**, dipping to $833 million nationally, well down from $4.2 billion in Q1 2022.

**2023 is forecast for a record year of new developments across the East Coast with 2.5m sqm expected** to be delivered, with Brisbane more than doubling its long term average.

**Land values have stabilised across all capital cities,** with some select precincts beginning to see a dip in value, this follows consecutive periods of record growth in values.

**Sydney has experienced the fastest pace of rental growth nationally,** with prime rents up by 38% y/y as the market responds to strong tenant demand and rising construction costs.

**Key Indicators** Q1 2023

| MARKET | PRIME NET FACE RENT $/SQM | SECONDARY NET FACE RENT $/SQM | SUPER* PRIME MARKET YIELD RANGE % | LAND <5,000sqm $/SQM | LAND 1-5 ha $/SQM |
|---|---|---|---|---|---|
| Sydney # | 227 | 187 | 4.25-4.75 | 2,005 | 1,716 |
| Brisbane | 149 | 132 | 4.75-5.25 | 521 | 488 |
| Melbourne * | 128 | 110 | 4.25-4.75 | 1,137 | 902 |
| Adelaide | 116 | 86 | 5.00-5.50 | 520 | 369 |
| Perth | 136 | 113 | 5.25-5.75 | 458 | 339 |

Source: Knight Frank Research *Yield range assumes a near new 10,000sqm+, non-specialised, institutional high-grade industrial asset with a of WALE 7.0 years +
Indicators are based on a blended average of the city precincts. *#Western Sydney prime net face rents average $182/sqm, secondary: $146/sqm; small lots: $1,269/sqm, 1-5ha lots: $1,180/sqm.*
**Melbourne (excluding the Fringe) prime net face rents average $115/sqm, secondary: $102/sqm; small lots: $872/sqm, 1-5ha lots: $678/sqm.*

# ECONOMY

*The moderation in retailing has continued into 2023 and further slowed as broader economic headwinds impact. Capital markets pose challenges, but the economy remains generally strong*

## The broader economy remains strong while retail moderates

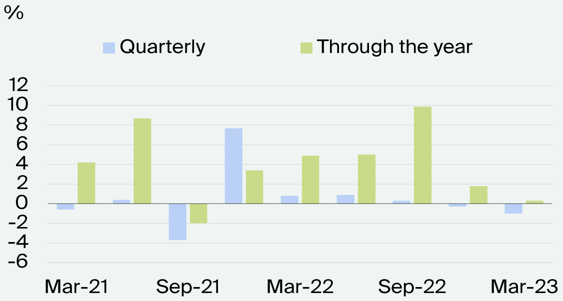
After a strong 2022 the headwinds for consumers have intensified and are negatively impacting retail turnover, with sales volumes declining by 0.6% in Q1. This followed from a minor (0.2%) contraction in turnover for Q4 2022. Amidst high inflation, growth in nominal sales turnover remains positive but the pace of growth has slowed substantially to 5.4% y/y. The slowdown in spending is most acute for the discretionary clothing and household goods categories, while food retailing remains resilient.

Outside of consumer spending, the broader economy remains strong with March employment data showing a stable unemployment level of 3.5% with a record high participation rate of 66.8% and the overall trend for employment increasing 0.2% in March. Coupled with rapid population growth and the sustained strength of the mining sector, this is supporting demand for industrial space despite the consumer slowdown.

## Inflation pressures ease marginally but remain

Cost-of-living pressures are pronounced, but the most recent CPI data is cause for optimism that the peak has now passed. Q1 data confirmed a decline in the headline rate to 7%, which, while still high, is a marked improvement on 7.8% in Q4 2022. Inflation is now moderating across parts of the economy, with goods inflation in decline, but remains high for other categories such as food (1.6% q/q) and housing (1.9%).

Quarterly turnover retail (in volume terms)




Source: Knight Frank Research, ABS

Construction costs increased again this quarter (+1.1%), but the annual rate of growth has moderated to 9.6% to March, as opposed to 11.9% over 2022.

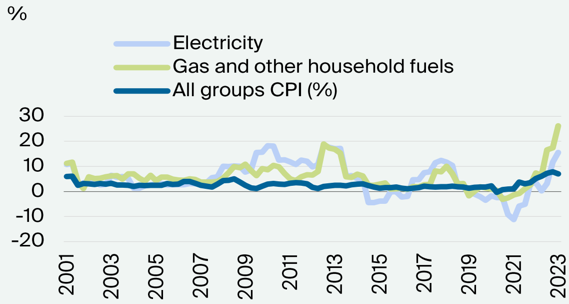
Rising energy costs are also of concern, with gas and electricity increasing sharply in Q1. These cost increases are impacting manufacturers and industrial occupiers more generally, and may also compound the negative sentiment among consumers when viewed in concert with the return to rising interest rates following April's pause.

## Unexpected May rate rise likely to put the brakes on

After a reprieve in April, when the RBA paused, interest rate increases resumed in May with the view that inflation remains too high. The RBA lifted the cash rate up 25bps to 3.85%. The door has been left open for further rate hikes in coming months, however the latest retails sales data demonstrates that cumulative rises are having the desired effect and will begin to force inflation down in Australia, thus allowing the RBA to undertake a pause and monitor the decline in inflation over the second half of the year.

The RBA's updated inflation forecasts suggest that Australia will see a rapid reduction over the next 12-18 months with downward movements becoming more broad-based bringing inflation close to the top end of the target band of 2-3% by the end of 2024. Much hinges on the evolution of inflation and the extent which the labour market is able to retain its current momentum in the second half of the year.

CPI and energy cost inflation




Source: Knight Frank Research, ABS

# LEASING MARKET

*Constrained leasing activity amidst limited availability, has led to increased competition and continued rental growth*

## Limited availability underpinning the sustained rental growth

The tightening vacancy trend continued in Q1 2023, with vacant space at a record low of 444,681 sqm across the Eastern Seaboard capital cities. This reflects an 18% fall in availability over the quarter and 82% below the peak in late 2020. With a 51% contraction in vacancy over the quarter, Sydney remains the tightest market, with a mere 43,759 sqm of available space. Meanwhile, 51% of the remaining space available space across the Eastern Seaboard is in Brisbane (226,592 sqm), with 39% in Melbourne (174,330 sqm).

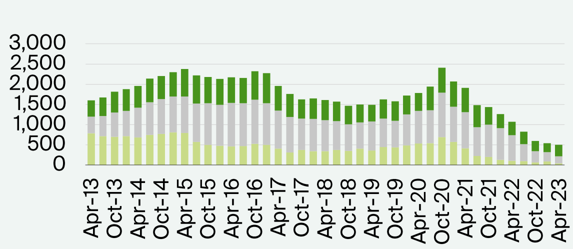
Impacted by the limited opportunities on the market, the Q1 take-up level across the Eastern Seaboard was 26% below the three year average, totalling 515,653 sqm. Existing prime and pre-committed deals accounted for 90% of leasing activity, highlighting the lack of existing space available to lease.

Intense competition among tenants for limited available space resulted in further rental growth across all capital cities. Brisbane led the quarterly rental growth by an 8.6% increase, followed by Sydney (8.2%). Adelaide and Perth reported 2.5% and 2.0% rental growth over the same period, while Melbourne saw moderate rental growth of 1.5% q/q on limited deals across most submarkets.

Incentives continued to decline in Q1 and currently average at 10% across the Eastern Seaboard, which stimulated stronger growth in effective rents over the quarter.

### Eastern Seaboard industrial vacancy

'000sqm, quarterly, 5,000sqm+




Source: Knight Frank Research

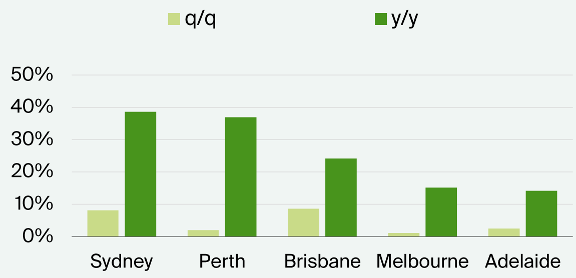
## Spec developments to provide some relief to undersupplied markets for 2023

Looking ahead, the gradual easing of material cost and supply chain pressures should aid the Eastern Seaboard supply pipeline, allowing it to reach a record of c.2.5 million sqm in 2023. However, 43% of the pipeline already pre-committed and 10% is owner-occupied, so it is unlikely that we will see a significant amount of speculative space entering the market and alleviating the current widespread undersupply.

Brisbane has a substantial development pipeline, with 843,573 sqm forecast to be delivered in 2023, compared to its long-term average of 357,940 sqm. In Sydney new developments are anticipated to reach 807,641 sqm. Whilst Melbourne will deliver approximately 900,748 sqm.

### Prime rent growth

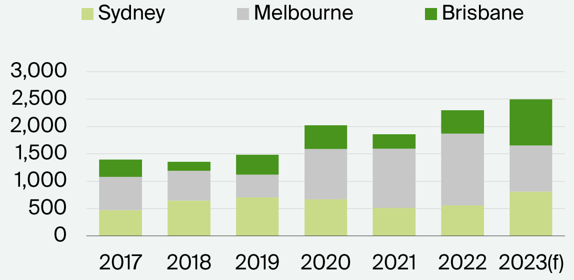
Average across major capital cities




Source: Knight Frank Research

### Eastern Seaboard industrial supply

'000sqm, completed 2017-2023(f)




Source: Knight Frank Research

# INVESTMENT

*Yields continue to shift up, but the impact on capital values is being offset by surging rental growth and varies by location and the structure and length of the lease*

## Subdued investment activity in Q1

Activity levels were muted in Q1, dipping to $833 million nationally, well down from $4.2 billion in Q1 2022. Underlying investor demand remains strong as the industrial sector is benefitting from much stronger rental growth than other property types. However, many investors are seeking greater clarity on the outlook before acquiring, while many vendors have opted to wait for conditions to improve before divesting.

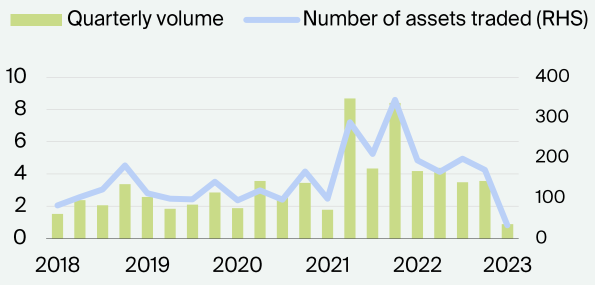
## Yield expansion continues but rental growth is a

Sydney saw the bulk of activity on Q1, with $571 million traded. Despite limited transactional evidence, prime yields are judged to have risen further in Q1, with the average prime yield shifting up in Sydney (to 4.8%), Melbourne (4.9%) and Brisbane (5.8%), while Adelaide (6.0%) and Perth (6.3%) held firm.

Despite continued yield shift, the outlook for capital values remains finely balanced because of surging rental growth and varies significantly by location and at asset level. Rapid rental growth in Sydney, Perth and Adelaide has out-stripped the impact of yield expansion resulting in further capital growth on average in Q1, whereas the picture is more finely balanced in Melbourne and Brisbane.

### Industrial investment volume

AUD billion



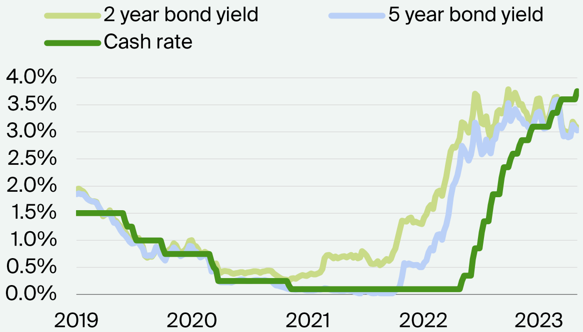

Source: Knight Frank Research, RCA

## Rates outlook looking clearer and more reassuring for investors

While debate continues over the level at which the cash rate will peak, funding costs have remained relatively stable in recent months, reflecting a balance between the potential for higher interest rates in the near term and market expectations that rates will be cut in 2024-25 once inflation eases.

If inflation subsides in coming quarters, the macro context will start to look more reassuring for investors in H2, so the trajectory of inflation overseas – and the extent to which services sector inflation persists – will bear close watching, alongside the actions of central banks in countries further along the path toward lower inflation.

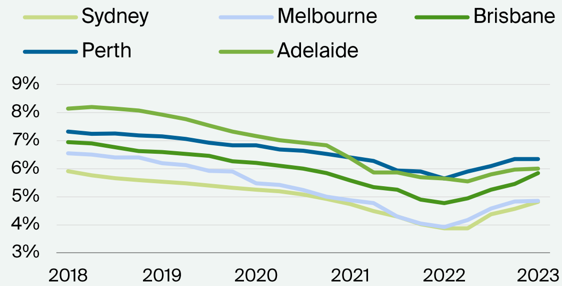
### Australian interest rates




Source: Knight Frank Research, Macrobond

### Average prime yields - major cities

Average across precincts (5,000 sqm assests, 5 yr WALE)




Source: Knight Frank Research

# SYDNEY

*Acute supply shortage and availability constraints have resulted in a landlord market; Tenants scramble for limited lease options driving rents to a new high*

**Marco Mascitelli** | Associate Director | **Naki Dai** | Research Analyst

## Subdued leasing activities resulted from availability constraints

The Q1 take-up number, recorded at 50,898 sqm, is well below the long-term average, highlighting the acute availability constraint across all precincts in Sydney. The most active precinct in Q1 is Outer West, with 63% of leasing activity.

By occupier type, transport/logistics (27%) and wholesale trade (22%) dominated the leasing market in Q1. Meanwhile, 90% of take-up activities were derived from existing facilities, given the rising construction cost and materials shortage delaying the development progress.

Take-up in Q1 was underpinned by Air Road Logistics securing 13,925 sqm of existing warehouse in Wetherill Park, Best Bar signing a lease 6 months before moving to the existing space in Ingleburn, and Hitachi Construction Materials committing to a 5,326 sqm speculative development in Marsden Park.

## The highest quarterly vacancy drop in Q1 leaves scarcity of space across all precincts

Vacancy tightened further by 51% in Q1 to 43,759 sqm, sitting at another record low. Among different precincts, Inner West and South West led the vacancy drop over the quarter, with available space down 60% and 59% respectively. South, as the tightest market, has no lease options available since Q3 2021.

The tightening vacancy has left tenants no choice but to negotiate the lease for any possible space 3-12 months in advance. Since 2022, almost all spec-built facilities were leased prior to completion, with an average of 6 months ahead of practical completion. The robust leasing market further supports significant rental growth and record rental rates.

## Rental growth continues with chronic undersupply fuelling the landlord market

The unprecedented rental growth momentum continues in Q1 as tenants compete intensely for space regardless of the ever-tightening market. On a Q/Q basis, average prime and secondary net face rent increased by 8.2% to $227/sqm and 8.6% to $187/sqm, accordingly. The Outer West precinct recorded the highest quarterly growth rate of 13.3% on prime facilities, while Inner West outperformed the other markets by its 15.6% growth in the secondary market.

Limited availability is driving a landlord market across all precincts in Sydney. Average incentives fell to 8.5% for prime and 9.2% for secondary over the quarter. As a result, the net effective rents climbed 11% on both prime and secondary assets in the same period. Looking ahead, further rental growth is expected, where a stronger rental escalation in spec-built and pre-committed facilities than in the existing prime market could be observed in the following months.

## Pre-committed developments to lead the supply pipeline in 2023

The forecast pipeline in 2023 is anticipated to reach 807,641 sqm, with rising material costs and delayed planning approvals pushing out project deliveries in 2022. More than 67,000 sqm of the space has been completed in Q1, with 41% being pre-committed and 30% being owner-occupied.

Pre-commit activity continue sustaining the supply pipeline throughout the year, with over 73% of the development in 2023 already being committed. When comparing different precincts, Outer West and South West will remain the most active submarkets this year, contributing 82% of total development pipeline.

Major developments this year include The Yards Industrial Precincts (c.100,000 sqm), Switchyard Industrial Estate (c.65,000 sqm) and ESR Horsley Drive Business Park (c. 50,000 sqm).

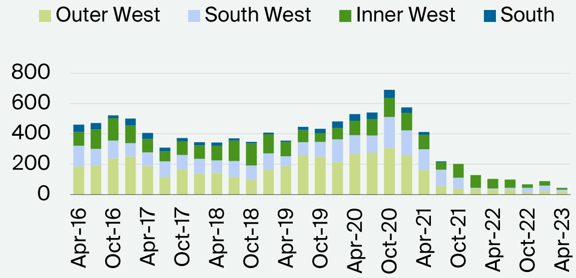
## Yields soften across all precincts again in Q4

The Sydney average prime and secondary yields softened again by 25bps Q/Q to 4.8% and 5.3% respectively. Since the lowest position in yields in mid-2022, average yields have expanded by 95 bps. Further yield expansion is expected in the year ahead considering the relatively high funding cost environment.

| TAKE-UP (SQM) Q1-23 | MOST ACTIVE SECTOR Q1-23 | VACANCY (SQM) Q1-23 | NEW DEVELOPMENT (SQM) |
|---|---|---|---|
| **50,898** | **27%** | **43,759** | **807,641** |
| -49% Y/Y | TRANSPORT, POSTAL, WAREHOUSING | -51% Q/Q | Estimated 2023 (f) |

### Sydney vacancy

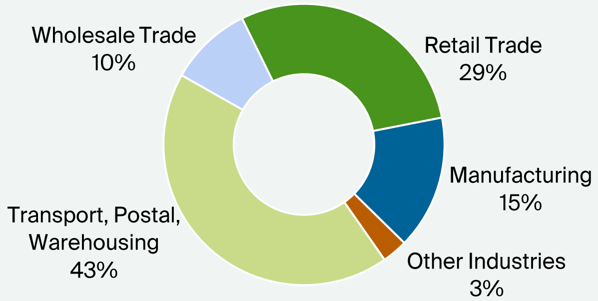
By precincts, '000sqm




Source: Knight Frank Research

### Sydney leasing take up by industry

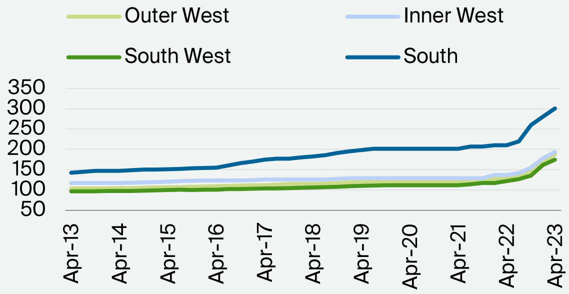
2022-2023YTD, % share by sqm leased




Source: Knight Frank Research

### Sydney industrial rents by precinct

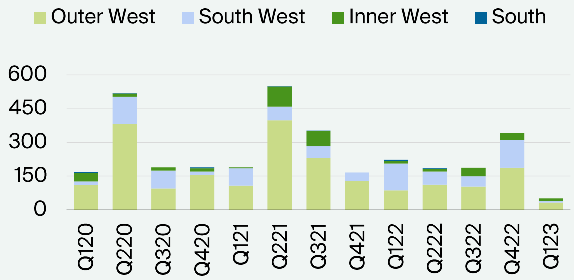
Average prime net face rent, $/sqm




Source: Knight Frank Research

### Sydney leasing take-up by precinct

By quarter, '000sqm




Source: Knight Frank Research

## Recent significant tenant commitments

| OCCUPIER | PROPERTY | PRECINCT | SIZE SQM | NET RENT $/SQM | TERM (yrs) |
|---|---|---|---|---|---|
| **Air Road Logistics ~** | 495 Victoria Street, Wetherill Park | Outer West | 13,925 | 175 | 5 |
| **Best Bar~** | Tenancy 2, 7 Williamson Road, Ingleburn | South West | 7,111 | 155 | 10 |
| **Harry the Hirer~** | Part Building, 11-13 Berry Street, Clyde | Inner West | 7,000 | 230 | 3 |
| **Hitachi Construction Materials#** | 168 Hollinsworth Road, Marsden Park | Outer West | 5,326 | 200 | 7 |
| **Freedom Tyres~** | 18-20 Bowmans Road, Kings Park | Outer West | 4,227 | 165 | 5 |

# Pre-commitment ^ Lease of speculatively developed space ~Existing space U/D=Undisclosed

# MELBOURNE

*Market starts 2023 hunting for space, as vacancy levels fall below 200,000 sqm, limiting take-up*

**By Tony McGough**

## Vacant space levels continue to tumble as some precincts have no space left

A further fall in vacant space of 25% saw a new record low of just 174,330 sqm available across Melbourne for Q1 2023. The end-March deal on Reid Way in the North precinct removed the last 18,000 sqm of space from the district leaving vacant space at zero. With the East only having a single 7,242 sqm building available, available space is now concentrated in the West (67,259 sqm) half of which is a lot which is still being constructed, the South East (58,197 sqm), mainly around Cranbourne West with a few new buildings nearing completion and the City Fringe (41,632 sqm) where 2 of the 3 available lots are C grade. Vacant space remains super tight; the number of free buildings in Melbourne can be counted on your hands.

## Take-up falls to new low level, limited by supply

With such limited space available, it is not surprising that take-up is falling markedly with only 203,190 sqm in Q1 2023. This is around half  the pre-Covid take-up levels and 25% of the peak in Q2 2021. New space is being snapped up before completion and the odd vacant lot still available is being snapped up, as highlighted above. The South East had the highest take-up with 96,577 sqm (47.5%) followed by the West (33.5%) in line with where space is still to be found. This quarter was dominated by transport demand (45%) showing there is still growth in this area, although 29% is still undisclosed as we go to press.

## Supply arrives but gets absorbed immediately

Supply for 2023 has been revised down slightly to 900,748 sqm, of which 176,969 sqm (20%) has already been delivered as Q1 finishes and a further 681,848 sqm is under construction. However, vacant space numbers highlight how this is absorbed as it arrives, given the pent up demand. The West still dominates 2023 supply with nearly 400,000 sqm  this year and the South East will be getting 231,145 sqm. The North is expected to see nearly 260,465 sqm this  year, more than half of which is already committed. With sub 20,000 sqm in the Fringe that is this years deliveries, so space is expected to remain limited.

## Rental growth continues but is limited on fewer deals

Average prime net rents continued to rise now standing at $115/sqm (exc. The Fringe) up 1.7% on the previous quarter and 16.5% y/y. Secondary rents remained flat though are still up 21.1% y/y. In most precincts rents saw little change on a limited number of deals, but the West saw prime rents rise 5.5% to $115/sqm. This puts rents in the West on a par with rents in the East, though still below the South East. There is some evidence in recent deals that this may move markedly higher in the next quarter as space issues rise. Incentives remain around about the 10-12% mark for prime and secondary space with secondary remaining slightly lower. However there is continued pressure on incentives and in the West prime incentives are more like 5-10%, with secondary at 10% outside of the Avalon/Gelong and Melton areas.

## Land values fall back from 2022 highs, as developers impacted by costs

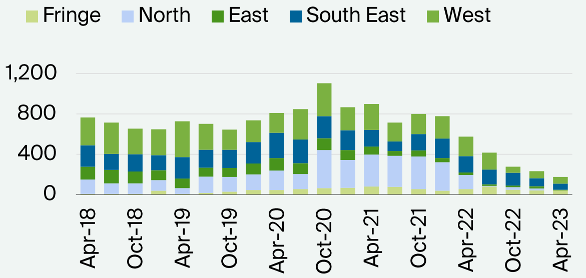
Land values dropped from their highs in 2022, showing there is a limit to prices that can be paid, even with rents continuing to rise as costs of construction, finance costs and uncertainty continue. Land values fell slightly across all size categories down 0.7% for <5000 sqm, 1.2% for 1-5 ha and 2.7% for 10 ha+. Values are now down 4-6% from last years highs. With demand for space still strong this is more a step back  and a removal of froth, rather than the start of a crash. This is apparent as the fall was concentrated in the West which has been flying as of late.

## Yields  show signs of stabilising

Yields remained virtually flat last quarter with only a slight upward movement. Prime yields went from  4.88% to 4.91%, so hidden by rounding, whilst secondary rose from 5.63% to 5.66%. Both prime and secondary markets are now 100bps higher than their historic lows in Q1 2022. Sales activity was lower as the market re-prices, but there were several deals in the West on Strzelecki Avenue totalling $18.75m, as well as an $18.5m deal in the South East.  The market remains open and attractive to investors.

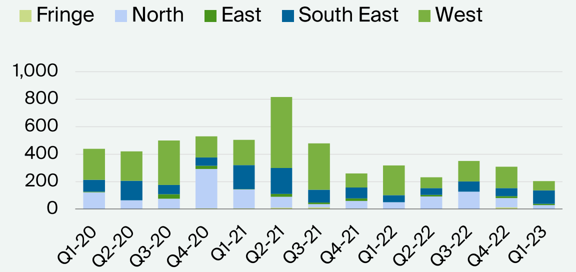
| TAKE-UP (SQM) Q1 | MOST ACTIVE SECTOR Q1 | VACANCY (SQM) Q1 | NEW DEVELOPMENT (SQM) |
|---|---|---|---|
| **203,190** | **45%** | **174,330** | **900,748** |
| -34% Q/Q | TRANSPORT, POSTAL, WAREHOUSING | -25% Q/Q | Estimated 2023 (f) |

### Melbourne industrial vacancy
'000sqm by precinct



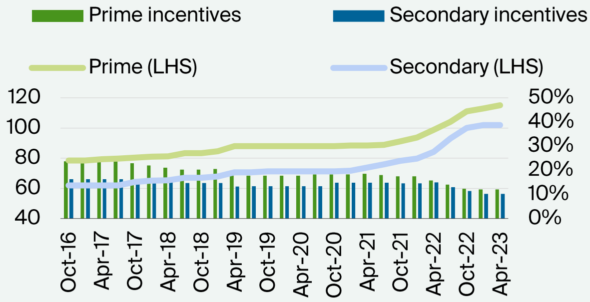

Source: Knight Frank Research

### Melbourne industrial take-up
'000 by precinct



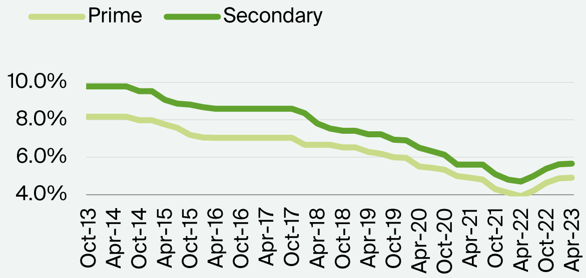

Source: Knight Frank Research

### Melbourne industrial rents
$/sqm net rents, % incentives; exc. fringe




Source: Knight Frank Research

### Melbourne industrial yields
% median core market yields




Source: Knight Frank Research

### Recent significant tenant commitments

| OCCUPIER | PROPERTY | PRECINCT | SIZE SQM | NET RENT $/SQM | TERM (yrs) |
|---|---|---|---|---|---|
| **PAC Trading^** | 10 Cargo Court, Dandenong South | South East | 9,627 | 115 | 5.0 |
| **Frucor~** | 67 Horsburgh Drive, Altona North | West | 10,000 | 125 | 5.0 |
| **Intercentral Logistics^** | W-1, 590-620 Western Port Highway | South East | 9,600 | 120 | 7.0 |
| **TW Logistics^** | W-2, 590-620 Western Port Highway | South East | 5,950 | 120 | 7.0 |
| **Effective Logistics~** | W-A, 2-30 Saintly Drive, Truganina | West | 10,630 | 120 | U/D |

# Pre-commitment ^ Lease of speculatively developed space ~Existing space U/D=Undisclosed

# BRISBANE

*Rental growth surges again as cost of new development is setting rental levels due to limited existing vacancy*

**By Jennelle Wilson** | Partner | Research & Consultancy

## Take-up remains at elevated levels with annual take-up remaining above 1 million square metres

Leasing activity in Q1 was 9% higher than for the previous quarter at 269,830sqm as the elevated levels of take-up since 2021 have been maintained. Annual take-up was 1.12 million square metres, the highest across the East Coast markets for the 12 months to Apr 23. During Q1 the strongest take-up was for pre-committed space, totalling 102,000sqm, followed by existing space with 69,963sqm and speculative developments at 97,218sqm. Take-up was highest in the South West with 46% of the quarterly activity.

## Transport and logistics users continue to seek additional and upgraded space

Transport, postal and warehouse users were the most active tenant type with 30% of take-up over the rolling 12 months, followed by manufacturers at 25% and 15% for retailers. Major leasing agreements in Q1 included Fantastic Furniture & Myer (38,562sqm) agreeing to terms on speculatively developed space, TI Transport (41,318sqm some 9 months before the building is available), Bradnam Glass (14,145sqm) and B-Dynamic (15,016sqm) into existing space. Recent pre-commitments have included two global occupiers who have reportedly agreed to (27,000sqm) and (21,000sqm) along with Moco Foods (18,032sqm).

## Vacancy increased for the first time in two years with significant new speculative starts

Vacant space increased for the first time in two years to be up 3% to be 226,592sqm, this remains 33% below that of a year ago. Existing prime vacancy fell by 9% to 41,443sqm but the increase in speculative space pushed total prime vacancy up by 20% in the quarter from recent lows, but remaining 30% down y/y. Speculative space now accounts for 40% of total vacancy, with the majority of this (37%) coming from speculative space still under construction.

Secondary vacancy fell by 20% in the quarter to 72,686sqm to be 39% below the levels of a year ago and reaching new record lows. Future quarters will begin to see significant secondary backfill space emerge (ie Coles at Heathwood).

## Rental growth accelerating further as new stock is setting rental thresholds

Average prime face rents increased by 24.2% y/y to $149/sqm net, with a further surge of 8.6% in the past quarter. Incentives have continued to contract at 10-12% on average, there have also been falls for pre-commitments and speculative space but the range remains wider depending on when negotiations commenced. The cost to deliver new space is currently the major driver of prime rents, given the lack of existing prime opportunities of scale. Secondary market rents increased by 7.7% in the quarter (31.7% y/y).

## Record supply expected for 2023 with at least 843,000sqm to be delivered

The new supply forecast for 2023 has been limited to projects already completed (190,144sqm) and those under construction (635,459sqm) to account for the current longer lead times. The final figure therefore may be higher than this should weather and supply issues improve. Economic rents for new development continue to increase, for assets of scale this is now at $140/sqm for the South and Western suburbs and $175/sqm+ for TradeCoast, this is driving prime rental growth.

## Vendor expectations are slow to match purchaser pricing levels, diminishing transaction volumes

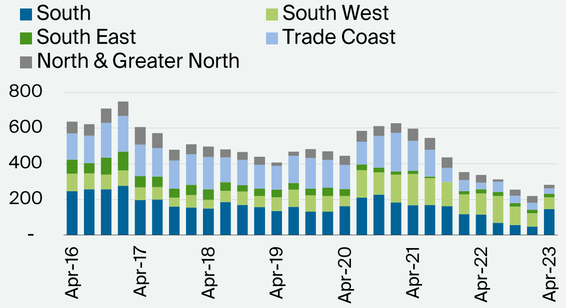
Land values were stable over the quarter at levels only slightly lower than the recent historical highs. Development feasibility has been hit by softer yields and high construction costs and timeframes. Owner occupiers have continued to buy, particularly smaller lots, but overall sales volume is lower.

Investment sales were sparse in Q1 with the gap between purchaser pricing and holding book values a hurdle to greater investment turnover, particularly for listed vendors. The largest recent sale is $32.75million at 80 Lomandra Dr, Brisbane Airport, a 24-year vendor leaseback at a yield of 5.2% on the leasehold asset. The lack of completed acquisitions indicates further yield softening of c40bps in Q1 and 100bps over the past year. Prime yields range 5.35% - 6.25% across Brisbane's precincts with a blended median of 5.85%.

| TAKE-UP (SQM) Q1 | MOST ACTIVE SECTOR RTM | VACANCY (SQM) | NEW DEVELOPMENT (SQM) |
|---|---|---|---|
| **261,565** | **30%** | **226,592** | **843,573** |
| 44% ABOVE THE 5Y-AVG | TRANSPORT, POSTAL & WAREHOUSING | +3% Q/Q | Estimated 2023 (f) |

## Brisbane Industrial Vacancy

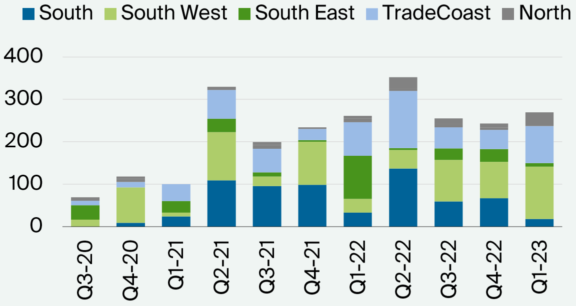
'000sqm available space by precinct




Source: Knight Frank Research

## Brisbane leasing take-up

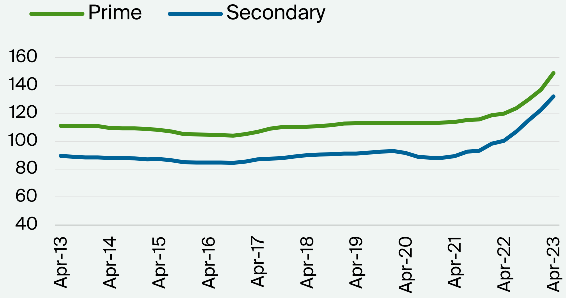
'000sqm by precinct




Source: Knight Frank Research

## Brisbane Industrial Rents

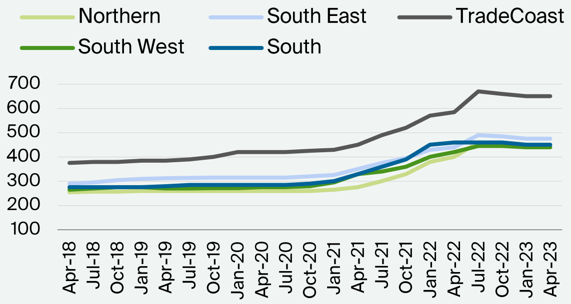
$/sqm average net face




Source: Knight Frank Research

## Brisbane Land Values

$/sqm average for sites 1-5ha




Source: Knight Frank Research

### Recent significant tenant commitments

| OCCUPIER | PROPERTY | PRECINCT | SIZE SQM | NET RENT $/SQM | TERM |
|---|---|---|---|---|---|
| **TI Transport~** | 56 Australand Dr, Berrinba | South | 41,318 | 125 | 7 |
| **Moco Foods#** | 55 Barracks Rd, Wacol | South West | 18,032 | 190 | 10 |
| **B-Dynamic~** | 30 Flint St, Richlands | South West | 15,016 | 120 | 7 |
| **Bradnam Glass~** | 62 Pineapple St, Zillmere | North | 14,145 | 140 | 8 |
| **Undisclosed tenant#** | 54 Monash Rd, Redbank | South West | 14,500 | 138 | 7 |

# Pre-commitment ^ Lease of speculatively developed space ~Existing space

# ADELAIDE

*Despite a stall in investment sales, land values continue to rise while demand from both tenants and owner occupiers remain strong.*

**By Bradley Tobiassen**

## Demand continues despite a shifting market

The industrial development market has faced a slowdown in growth over the past three quarters, primarily resulting from a marked increase in both debt and construction costs. Despite these challenges, however, demand for industrial assets persisted, specifically in the Inner and Outer Northern precincts.

Land values for both small (2,000-5,000 sqm) and medium (1-5 ha) sized allotments have increased over Q1 2023, with more impactful growth occurring among smaller allotments. At a precinct level, small allotments experienced growth in the Outer North, Inner North and Inner West precincts, while medium allotments saw growth in only the Outer North and Inner West.

According to Cordell Connect, around 72.4% of the expected development set to be finalized by 2025 will occur in the Inner or Outer Northern precincts, in contrast to 20.7% in the Inner and Outer Southern precincts. Both the Outer North and Outer Southern precincts have gained favour among investors and tenants. The Outer North, in particular, offers the most accessible and cost-effective land, as well as being attractive to developers due to improved accessibility resulting from the north/south connector. As a result, it is likely that these precincts will continue to experience an increase in investment and development activity in the coming years.

## Tenant needs adjust to rising rents

Persistent increases in construction costs and supply chain challenges have hindered the projected supply of industrial assets, leading to a supply-demand gap that has driven up rental growth rates for existing stock. Average prime net face rents have increased 2.56% over Q1 2023 and 7.29% over the six months to April 2023. Additionally, average incentive rates have remained stable at 7% during the quarter, the lowest they have been in 10 years, highlighting the strong ongoing demand for quality assets.

In Q1 2023, occupiers remained cautious and focused on cost control, with a growing preference for shorter leases, particularly among institutional tenants who have been more inclined to consider sub-7 year leases in the last six months. Furthermore, we have also observed an increase in demand for business parks as industrial asset vacancies above 5000 sqm have slightly grown from 493,097 sqm to 532,143 sqm over the last quarter.

## Yields continue to soften slightly, in selective

As we entered 2023 yields have continued to weaken but in a much more nuanced manner. Overall prime yields moved out 0.4% to 6.01% whilst secondary yields rose just 0.1% to 6.95%. Prime Inner North yields rose 25bps to 5.83% whilst Inner West rose 10bps to 5.73%. However Southern precincts saw no yield movement whilst yields came in by 13bps in the Inner North to 6.13%. Secondary yields remained stable except for slight movement in the Outer Northern precinct.

Q1 2023 saw sales volume for industrial assets above $5m of $133.63 million. The Inner North dominated sales with $84.11 million, followed by the Inner West and Outer North both with $20+million each . Sales were very limited in the South with zero registered for the Inner South over the quarter.

## Market fundamentals remain strong

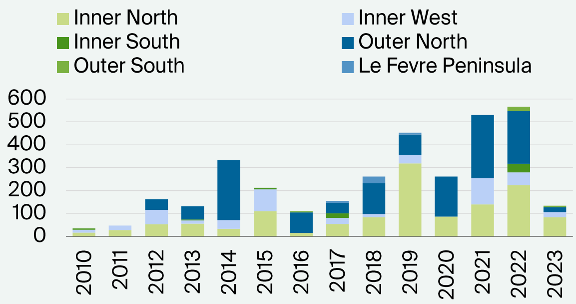
Commercial markets remain very cautious, both on the leasing and investment side, as economic and financial uncertainty continues. Throughout this period, the demand requirements for industrial space mean that the market has continued to trade, new developments have progressed and rental growth has continued to materialise. As a result, industrial assets in South Australia are still seen as a secure investment option, providing value for money with upside growth potential.

It is important to note that although yields have moved out, it is due to the fundamental issue of the cost of debt, and not weaknesses in the market itself. As clarity begins to return to financial markets and interest rates near their cyclical peak, the South Australian industrial market remains robust, with low vacancy rates and projected rental growth.

| TAKE-UP (SQM) Q1 | VACANCY (SQM) | NEW DEVELOPMENT ($) | NEW DEVELOPMENT (SQM) |
|---|---|---|---|
| **65,393** | **532,143** | **288.7M** | **198,749** |
| (5,000SQM +) | (5,000SQM +) | Forecast completion by 2025 | Forecast completion by 2025 |

## Adelaide industrial sales

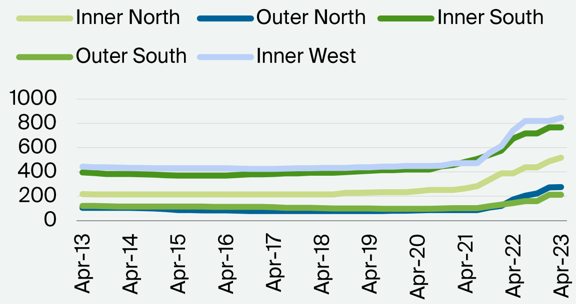
$5mil sales, 2013 to 2023YTD




Source: Knight Frank Research

## Adelaide industrial land values

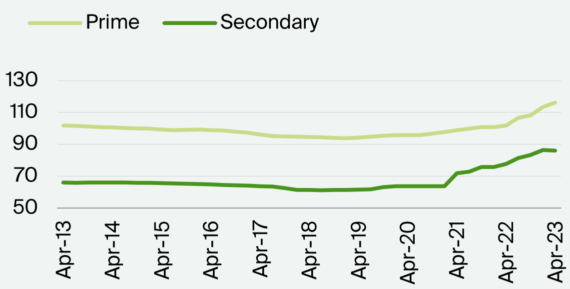
Average $/sqm by precinct for land <5000sqm




Source: Knight Frank Research

## Adelaide industrial rents

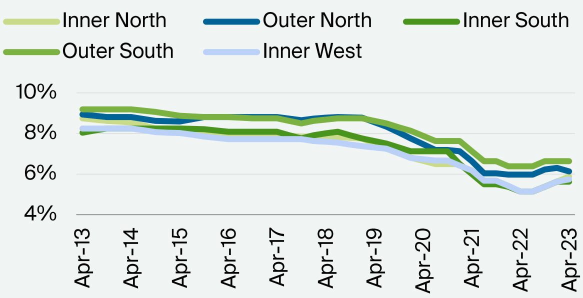
Average $/sqm p.a. net face by grade




Source: Knight Frank Research

## Adelaide industrial yields

% core market avg. yields by precinct




Source: Knight Frank Research

## Recent significant tenant commitments

| OCCUPIER | PROPERTY | PRECINCT | SIZE SQM | NET RENT $/SQM | TERM (yrs) |
|---|---|---|---|---|---|
| **Enerven Energy** | 2-8 Mirage Road, Direk | Outer North | 6,898 | 115 | 5 |
| **EC Carpets** | Lot 201 Sheriffs Road West, Lonsdale | Outer South | 15,313 | 86 | 10 |
| **AMA Group** | 80-92 Grand Junction Road, Kilburn | Inner North | 6,889 | 135 | 10 |
| **Confidential** | Western Suburbs | Inner West | 25,582 | 124 | 20 |
| **Confidential** | Outer Northern Suburbs | Outer North | 22,152 | 95 | 12 |

# PERTH

*After consecutive periods of strong growth Perth has moved to a position of stability*

**By Theodore Connell-Variy**

## Vacancy remains low, but rental growth has moderated

Perth's prime average market rents increased by 1.9% through Q1 2023 to reach $135.60, reflecting sustained market momentum in spite of slowing economic growth. This lifted the annual growth rate to 36.8%, putting growth in the Perth market on par with Sydney, where tight supply has resulted in rental growth of 38.7%. This is arguably as reflective of the slowdown in Perth as it is a strong, resurgent demand for high quality assets in Sydney. In the broader economic environment, a quarter punctuated by stability, small areas of growth, rather than decline, is a clear standout.

Q1 2023 showed a slowing of the growth that punctuated Q3 into Q4 of 2022. There remains a shortage of quality space and this leads to sustained strong demand across submarkets. Q1 showed more specific pockets of rental growth across markets – notably Inner South where both manufacturing and warehousing assets increased $5 and $10 per sqm respectively. Secondary markets have been dominated by flat line performance in a quarter of minimal activity.

Perth's industrial market has continually shown growth above the averages of the East Coast, however in the most recent quarter growth in the west has moderated while Sydney in particular has accelerated, up 7.8% y/y compared to the previous quarter.

## A tight market remains with limited availability

Prime land supply remains tight across Perth's industrial areas but has tightened most notably in the South Precinct. Increased demand for Inner South specifically has resulted in associated price increases – the average increased from $388 to $394 for large parcels.
Large lots in the East precinct have come back slightly (-0.7%) and appear to represent value to those still requiring significant space in a quality location. In a further sign that the heat is coming out of the Perth industrial market areas in the East have seen a drop of $25 sqm, both Kewdale and Welshpool coming back to $525 in the larger 1-5ha parcels. This came after consecutive periods of increases, followed by several periods of stability.

## Land prices remain firm

Offsetting these declines, however, was the increase in land value for Hazelmere where renewed demand has pushed prices up by $25 (again, for larger allotments). Continued strong demand in the South combined with limited supply has meant that land prices in the East have sustained the levels reached in Q4, but only larger lots in Canning Vale moved up ($25 sqm), which pushed the inner south average up 1.5%. Smaller, sub 5,000 sq land parcels were not in favour, and with limited activity prices remained stable across all market segments.

## Small yield movement, in-line with national trends

The Perth prime industrial property market has continued to experience a slight softening of yields almost uniformly across markets, but this would appear to be a movement to keep them in lockstep with other industrial markets. The continued pricing adjustments follow on from Q4 2022 where yields softened 25 bps. There was limited investment activity this quarter, however high-quality space in preferred locations were still sought out amid the changed perceptions on the market and shifting buyer sentiment.

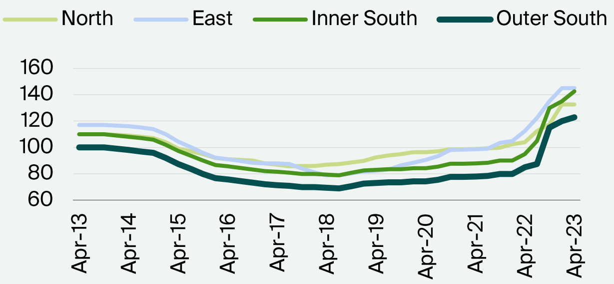
Most precincts experienced modest yield movement, well below the previous 25 bps over Q4, with the average prime yield moving out marginally (0.04%) to 6.38%, however the average secondary yield having moved out sharply, has come back a touch from 7.03% to 7.0%. The softer yields is resultant from rising debt costs and is expected to continue in the short-term. However, we note that Inner and Outer South precincts and secondary markets have almost universally remained static.

Yields are expected to remain above East Coast capitals, with Sydney rental growth this quarter suggesting a slight shift in demand with changing economic conditions.

| PRIME RENTAL GROWTH | LAND VALUE GROWTH (<5,000SQM) | LAND VALUE GROWTH (1-5HA) | PRIME YIELD SHIFT |
|---|---|---|---|
| **36.8%** | **14.01%** | **15.7%** | **+4 BPS** |
| Y/Y AVERAGE ACROSS ALL PRECINCTS | Y/Y AVERAGE ACROSS ALL PRECINCTS | Y/Y AVERAGE ACROSS ALL PRECINCTS | YIELDS MOVE OUT IN Q4 |

### Perth industrial rents by precinct

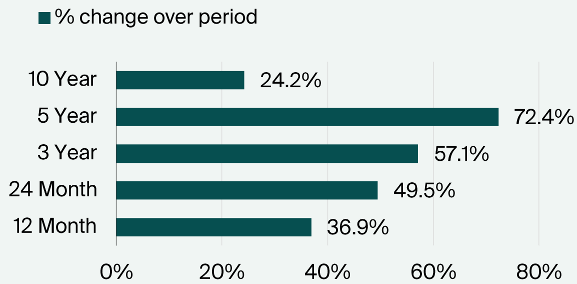
Average prime net face rent, $/sqm




Source: Knight Frank Research

### Perth % growth net face rent

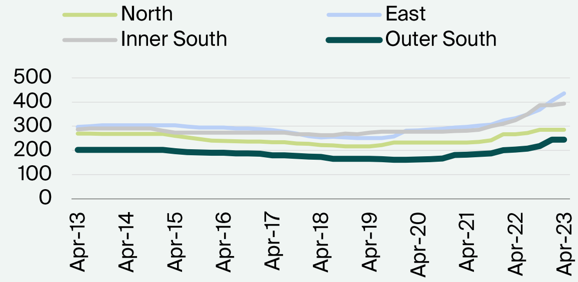
% Growth rate of $/sqm pa net face, blended rate




Source: Knight Frank Research

### Perth land values by precinct

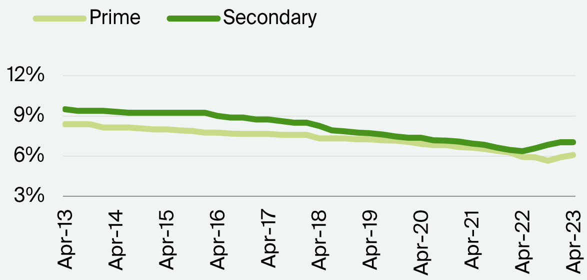
average $/sqm, medium lots 1-5 ha




Source: Knight Frank Research

### Perth industrial market yields

Prime vs secondary (averages)




Source: Knight Frank Research

| OCCUPIER | PROPERTY | PRECINCT | SIZE SQM | NET RENT $/SQM | TERM (yrs) |
|---|---|---|---|---|---|
| **Independence Australia** | 20 Aitken Way, Kewdale | East | 3,139 | 126 | 10 |
| **Sinopec ~** | 21 Logistics Boulevard, Kenwick | East | 2,825 | 170 | 10 |
| **U/D** | 8 Gauge Circuit, Canning Vale | South | 6,698 | 140 | 5 |

# Pre-commitment ^ Lease of speculatively developed space ~Existing space U/D=Undisclosed

# RECENT SALES

### Recent significant sales

| CITY | PROPERTY | PRICE $M | SIZE SQM | $/SQM | PURCHASER | VENDOR | YIELD %[1] | WALE |
|---|---|---|---|---|---|---|---|---|
| Melbourne | 41 Strzelecki Avenue, Sunshine West | 11.50 | 5,778 | 1,990 | Inotek Timber System | (Private Investor) | 4.40 | 2.5 |
| Melbourne | 152-158 South Gippsland Highway, Dandenong South | 12.5 | 4,367 | 2,862 | U/D | Cqr Property | 4.78 | 5.0 |
| Melbourne | 67 Gateway Boulevard, Epping | 8.9 | 3,970 | 2,259 | (Private Investor) | U/D | 4.24 | 4.8 |
| Sydney | 30 Clay Place, Eastern Creek | 34.5 | 6,183 | 5,580 | FIFA Capital | Centuria | 3.48 | 3.4 |
| Sydney | 137-147 McCredie Road, Smithfield | 30.3 | 10,210 | 2,963 | Madad Property | 3M Australia | 4.44 | U/D |
| Sydney | 13 Ferndell Street, South Granville | 57.0 | 15,320 | 3,725 | Hines | Pipeclay Lawson | 3.31 | 3.3 |
| Brisbane | 112 Cullen Ave, Eagle Farm | 32.3 | 12,034 | 2,680 | Altis Property Partners | Dexus | 5.63 | 1.5 |
| Brisbane | 63 Tile St, Wacol | 16.3 | 7,804 | 2,089 | Centennial Property Group | GM Property | 5.97 | 4.4 |
| Brisbane | 47 Acanthus St, Darra | 15.9 | 3,937 | 4,039 | (Private Investor) | Dexus | 5.52 | 4.3 |
| Adelaide | 1161-1171 Main North Road, Pooraka | 26.5 | 9,165 | 2,891 | (Private Investor) | Bricktop Group | 5.29 | 5.4 |
| Adelaide | 113 Ledger Road, Beverley | 14.2 | 8,194 | 1,736 | Leyton Funds | (Private Investor) | 6.19 | 1.7 |
| Adelaide | 300 Richmond Road Netley | 71.3 | 134,714 | 42,112 | Harmony Corporate | Charter Hall | 4.45 | 2.5 |
| Perth | 2-10 Kewdale Road, Welshpool | 20.0 | 11,449 | 1,747 | U/D | Bend-tech Group | 6.10 | 10.0 |
| Perth | 198-202 Bannister Road, Canning Vale | 14.7 | 7,808 | 1,883 | Harmony | Gianni Redolatti | 5.94 | 10.8 |
| Perth | 64 Great Eastern Highway, South Guildford | 16.0 | 4,593 | 3,484 | Westbridge | Acure Asset Management | 5.36 | 6.1 |

[1] Core Market Yield [2] Passing Yield [3] Land/Development Site [4]Specialised, purpose built shipping container storage yard with substantial concrete container rated hardstand [6] includes a service station component [7] reported #Sale & Leaseback ^Part of Portfolio +Fund Through ~includes cold Store/ambient temperature areas

## DATA DIGEST

**Prime Grade:** Asset with modern design, good condition & utility with an office component 10-30%. Located in an established industrial precinct with good access.
**Secondary Grade:** Asset with an older design, in reasonable/poor condition, inferior to prime stock, with an office component between 10-20%.
**Core Market Yield:** The percentage return/yield analysed when the assessed fully leased net market income is divided by the adopted value/price which has been adjusted to account for property specific issues (i.e. rental reversions, rental downtime for imminent expiries, capital expenditure, current vacancies, incentives, etc).
**WALE:** Weighted Average Lease Expiry
**Vacancy Methodology:**
This analysis collects and tabulates data detailing vacancies (5,000m$^2$+) within industrial properties across all of the Industrial Property Market. The buildings are categorised into 1) Existing Buildings – existing buildings for lease. 2) Speculative Buildings – buildings for lease which have been speculatively constructed and although have reached practical completion, still remain vacant. 3) Spec. Under Construction – buildings for lease which are being speculatively constructed and will be available for occupation within 12 months.

### We like questions, if you've got one about our research, or would like some property advice, we would love to hear from you.


**Research**
Ben Burston
+61 2 9036 6756
Ben.Burston@au.knightfrank.com

**Industrial Logistics NSW**
James Reeves
+61 2 9036 6728
James.Reeves@au.knightfrank.com

**Industrial Logistics, National**
James Templeton
+61 3 9604 4724
James.Templton@au.knightfrank.com

**Industrial Logistics– Investments**
Angus Klem
+61 2 9028 1110
Angus.Klem@au.knightfrank.com

**Industrial Logistics VIC**
Joel Davy
+61 3 9604 4674
Joel.Davy@au.knightfrank.com

**Industrial Logistics– Investments VIC**
Scott Braithwaite
+61 3 9604 4689
Scott.Braithwaite@au.knightfrank.com

**Industrial Logistics QLD**
Mark Clifford
+61 7 3246 8802
Mark.Clifford@au.knightfrank.com

**Industrial Logistics SA**
David Ludlow
+61 8 8233 5273
David.Ludlow@au.knightfrank.com

**Industrial Logistics WA**
Geoff Thomson
+61 8 9225 2436
Georff.Thomson@au.knightfrank.com

**Asset Management Services**
Lisa Atkins
+61 3 9604 4710
Lisa..Atkins@au.knightfrank.com

**Industrial Logistics TAS**
Tom Balcombe
+61 3 6220 6999
Tom.Balcombe@au.knightfrank.com

**Valuations National**
Alistair Carpenter
+61 2 9036 6662
Alistair.Carpenter@au.knightfrank.com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