1 *Surging rental growth*

2 *Yields continue to soften*

3 *Transaction volumes ease*

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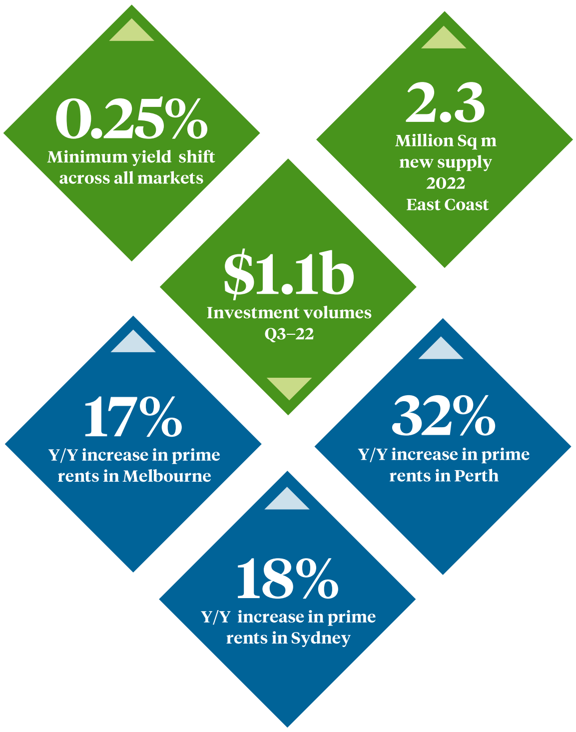
# Australian Industrial Review

**Q3-2022**

# KEY INSIGHTS




**The leasing market continues to be very strong**, driving widespread rental growth, but higher funding costs have seen a change in sentiment in the investment market, with yields rising by at least 25bps across all markets.

**In Sydney, vacancy has declined further**, and there is now under 40,000 sq m of prime space available across all precincts. Tenants are increasingly required to pre-commit to new stock due to the lack of available space to lease.

**Melbourne has the nation's largest development pipeline,** with over 1 million sq m expected to complete in 2022. and nearly a million expected in 2023. Over half of this stock is in the Western precinct.

**Brisbane saw strong take up in Q3,** with 219,000 sq m leased. This has resulted in a further fall in vacancy, with vacancy levels now at a decade low.

**In Sydney, land values have stabilised,** this follows consecutive periods of record growth in values.

**Perth is experiencing the fastest pace of rental growth nationally,** with prime rents up by 32% Y/Y as the market responds to strong tenant demand and rising construction costs.

**Key Indicators** Q3 2022

| 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 # | 187 | 157 | 3.75 – 4.25 | 2,013 | 1,724 |
| Brisbane | 130 | 115 | 4.25 – 4.85 | 531 | 497 |
| Melbourne * | 121 | 106 | 4.00 – 4.50 | 1,151 | 889 |
| Adelaide | 108 | 83 | 4.50 – 5.00 | 472 | 334 |
| Perth | 129 | 106 | 4.50 – 5.00 | 480 | 340 |

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 $141/sqm, secondary: $122/sqm; small lots: $1,269/sqm, 1-5ha lots: $1,180/sqm.*
**Melbourne (excluding the Fringe) prime net face rents average $111/sqm, secondary: $100/sqm; small lots: $889/sqm, 1-5ha lots: $686/sqm.*

# ECONOMY

*Retail spending continues to drive strong economic growth, but the global economy and capital markets provide a headwind into 2023.*

## Sustained growth momentum, on the back of domestic demand

Multiple interest rate rises and higher inflation may have impacted sentiment, but the average consumer is still spending freely, with retail sales rising further with 17.9% growth in the year to September (0.6% M/M). This is down on last month's 19.2%Y/Y but still strong. Spending remains buoyant across most of the major categories, led by clothing (up 2% last month and 70% Y/Y) and cafes & restaurants (up 1.3% and 53% Y/Y), although higher frequency data from the major banks is pointing to a slight slowing in recent weeks. The strength of the labour market is a key driver of this, with employment continuing to expand in recent months, aided by the return of inward migration.

## Deteriorating global outlook

While the economy has grown strongly during 2022, the outlook for 2023, is more subdued. The RBA's actions will ultimately act to curb household spending power and slow the pace of growth, with GDP growth forecast to halve from 3.8% in 2022 to 1.9% in 2023 according to the IMF. Despite this likely slowdown in 2023, Australia is still expected to out-perform other major advanced economies which are facing higher and more entrenched inflationary pressures. A number of major European economies – most notably Germany and the UK – and the US are at risk of recession in coming months, and while this poses a headwind for the growth outlook, it will bolster the investment case for Australian industrial and logistics assets as a relative safe haven.

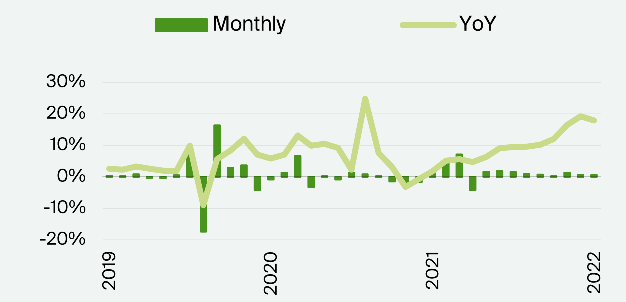
## Funding costs continue to edge upward on global uncertainty

The RBA continues to raise the official cash rate, to 2.85% at its November meeting. Further hikes are expected in coming months, but the pace has slowed back to more normal 25 bp increments and most commentators consider that the RBA will pause somewhere in the range of 3.10 – 3.60%. Their stance will be data-dependent and will evolve depending on the trajectory of inflation and growth in coming months.

Besides cash rate settings, global bond market pricing remains critical to the outlook for funding costs. Swap rates and bond yields have edged up during Q3 partly in response to shifts in the US and especially the UK, where long-dated bonds have struggled to get back from rates at 20-year highs. This uncertainty and shifting financial context is impacting pricing and will be a key driver of market performance in 2023. Consequently, availability of finance and its cost is becoming more of an issue as we head to the end of 2022.

**Retail sales**

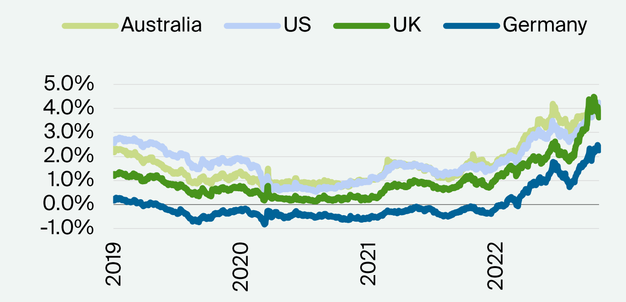
Per cent change




Source: Knight Frank Research, ABS

**10-year government bond yields**

Per cent




Source: Knight Frank Research, Macrobond

# LEASING MARKET

*Vacancy rates continue to fall and rents rise; with demand continuing to outstrip supply, the leasing market remains very tight.*

## Record supply hits record demand to continue to put pressure on availability

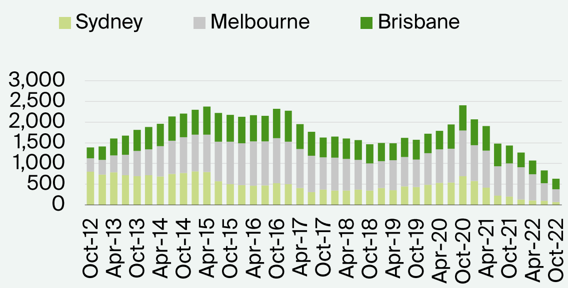
Vacancy rates fell to record lows as availability continued to fall in all the main markets. Across the Eastern Seaboard vacant space fell by 33% in Melbourne (to 276, 913 sqm) and Sydney (to only 66,648 sqm) and 18% in Brisbane. Overall total vacant space on the Eastern Seaboard fell below 600k sqm at 598,158 sqm, the lowest on record. This despite a record delivery of new space, with Melbourne on track to deliver its forecast 1.3m sqm in 2022. Elsewhere, only Adelaide has a sizeable amount of vacant space left (c550,000 sqm), with just c.77,000sqm in Perth.

Whilst there has been a record amount of supply coming onboard, there has also been continued high levels of take-up, which rose 24% across the Eastern Seaboard to 679,194 sqm, with Sydney the lowest of the three main markets at 170,677 sqm, mainly limited by supply-side issues.

As a result of the very tight market rents continued to rise strongly. Perth showed the highest growth rates; and both Perth (14.4% Q/Q and 34.1% Y/Y) and Sydney (9.9% Q/Q and 18.1% Y/Y) had sharply increasing rates as lack of supply really starts to show in pricing. Some sub-markets in Perth are seeing 50% rises Y/Y and 28.6% in the last quarter. Rents continue to show strong growth in Melbourne and Brisbane, where limited availability means that secondary rents are now growing more rapidly than prime ones as tenants scramble for what space is amiable. Adelaide remains better supplied and has more steady growth, up 1.5% Q/Q and 7.4%Y/Y.

### Eastern Seaboard Industrial Vacancy

'000sqm, quarterly, 5,000sqm+




Source: Knight Frank Research

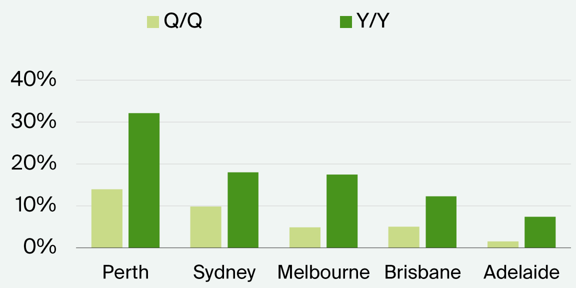
## Substantial development pipeline in Melbourne and Brisbane

2023 is looking like it will again provide substantial extra space for the market as pipelines continue being developed out. The major space coming through will be from Melbourne and Brisbane, both with close to 1m sqm. Brisbane is expected to produce 1,081,644 sqm, particularly in the South and South East, though part of this is delayed delivery from 2022 due to supply and weather issues. Melbourne is presently down to bring 927,160 sqm on-line, with half of this in the West.

Continued construction and material/labour supply issues may continue to cause delays. On top of this, financing costs are putting pressure on development feasibility and feeding in to pricing for both tenants and land values, whose growth paused in many places as investors work to make developments add up.

### Prime Rent Growth

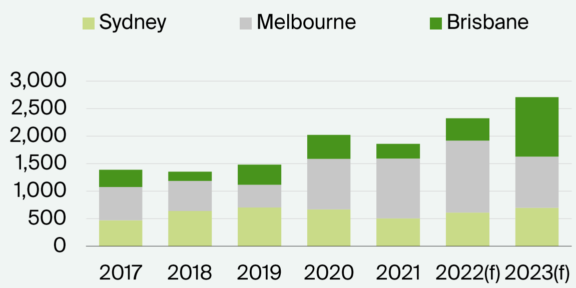
Average across major precincts




Source: Knight Frank Research

### Eastern Seaboard Industrial Supply

'000sqm, completed 2017-2023(f)




Source: Knight Frank Research

# INVESTMENT

*After a decade of compression, yields edged upward in Q2 in response to the higher cost of debt, but land values continued their ascent.*

## Sustained demand for industrial assets, but deals taking longer to settle

Uncertainty over the outlook for inflation and interest rates both globally and locally continue to weigh on market sentiment and investors are closely scrutinising real-time data for signs of slowing inflationary pressures. The underlying questions of how high rates will rise and whether they will persist at higher levels or drop back down in 2023-24 are critical to the outlook, and in this environment many asset owners and investors are pausing to allow conditions to settle.

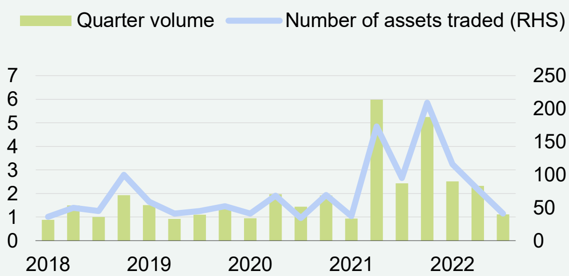
Reflecting this shift, deal volumes have been relatively subdued recently although the industrial market has felt less impact than other markets. Total market turnover reached $1.1bn in Q3, down from $2.4bn a year ago but in line with the trend seen in 2019-20. Underlying investor demand for industrial and logistics assets continues to be strong, but heightened uncertainty over the outlook is resulting in deals taking longer to transact.

## Yields adjust upwards to reflect higher rates

As the market continues to adapt to the higher cost of debt, yields shifted out further in Q3. Prime yields rose by a further 25 basis points in Perth, Brisbane and Adelaide, 40 basis points in Melbourne, and by 50 basis points in Sydney after not having adjusted in Q2. Notwithstanding this yield shift, the impact on capital values remains finely balanced because of the strength of rental growth. The aggregate impact and near-term outlook for capital growth is dependent on the balance of these competing forces and varies significantly at asset level.

### Industrial Investment Volume

AUD billion, covering deals over 10m




Source: Knight Frank Research, RCA

On average, rental performance has so far been strong enough to offset the outward yield shift with the 20% y/y uplift enough to offset the 50 bp movement across the market on average.

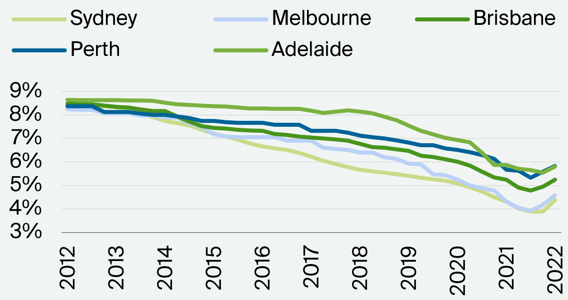
## Land values stabalise in Q3

With capital growth having slowed and construction costs continuing to rise, land values have stabilised after a sustained run of strong growth over the past couple of years. Melbourne saw a slight contraction in Q3, but most markets saw values unchanged, with several markets showing continued growth.

Desirable locations with good access to transport infrastructure remain in demand, but market performance is likely to be more dependent on local market factors now that the uniform surge in capital value growth has abated.

### Average Prime Yields - Major Cities

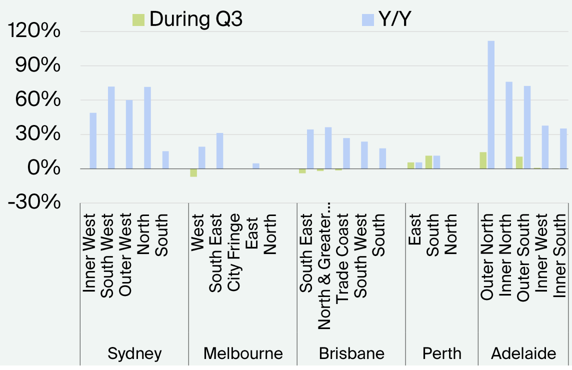
Average across precincts (5,000 sqm assests, 5 year WALE)




Source: Knight Frank Research

### Land Value Growth by Precinct

Annual growth for medium lots (1-5 ha) to Q3 2022



# SYDNEY

*Competition among occupiers and limited available stock promotes unprecedented rental growth across the board.*

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

## Logistics and manufacturing occupiers drive demand

Demand for industrial and logistics space continues, supported by a sustained uptick in e-commerce and supply chain challenges. Logistics operators and manufactures thus have been at the forefront of this demand over the quarter as they strategically revaluate their supply chains model to avoid future disruption.

Compared to Q2, take-up in Q3 slightly dipped to 170,677 sqm, among which, Outer West and South West precincts were aggressive as always, accounting for 77% of total take-up this quarter. Transport/logistics and manufacturing occupiers dominate the industrial leasing market, accounting for 75% of activity this quarter.

More strikingly, while transport/logistics operators seek large facilities to meet the future expansion potential, retailers and manufacturers prefer to lock in medium to long-term leases, with 89% of the manufacturing and retail trade leasing activity recorded this quarter having over 5-years leases.

## Vacancy hits another record low

The solid occupier demand promotes another record low vacancy level in Q3. Vacancy in Q3 now measures 66,648sqm, which indicates a 33% decline Q/Q and a 67% plummet Y/Y.

Looking at different precincts, Outer West and Inner West experienced significant vacancy reduction, with the available spaces down 55% quarterly to 14,434 sqm and 61% to 21,810 sqm respectively. On the other hand, no vacancies have been recorded in the South for over 12 months. Warehouses with upcoming vacancies are generally being renewed or even leased well ahead of lease expiries.

The tight vacancy market is presumably to last for the foreseeable future, as occupiers continue to strengthen the efficiency and resilience of their supply chains by seeking more space. Furthermore the limited speculative space available on the market will also hinder vacancy levels.

## Rents rise at an unprecedented rate

The historical low vacancy level has piled significant pressure on rents. Continuous supply disruption and limited supply encourage intense competition among logistics operators, online retailers and manufacturers for scarce industrial space available on market, which is driving the rents to an unprecedented level.

On a blended basis, average prime and secondary net face rents increased by 9.9% and 6.8% Q/Q. In Y/Y terms, average prime and secondary net face rents surged 18.1% and 15.8% accordingly. In comparison with different precincts, South experienced substantial rental growth over the quarter, with a recorded prime net face rent growth rate of 18.0%, followed by Inner West (+9.0%) and Outer West (+8.4%). Given the facts of stock limitation and the continuous inflationary pressures, further rental growth is expected over the near term.

## Pre-commitment development dominates the construction pipeline till year-end

Notwithstanding the escalation in construction material costs caused by supply constraints, the development completions by the end of 2022 are anticipated to arrive at c. 615,000 sqm, with 93% of the under-construction development being pre-committed. Outer West precinct accounts for the most development activity, with 76% of total development activity by the end of this year.

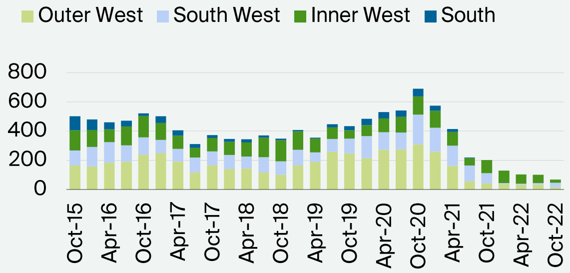
After continuous growth in land values over the last two years, values this quarter remained steady across all precincts, with 1 -5 ha lots averaging $1,260/sqm in Western precincts, whilst land in South Sydney averages over $3,000/sqm.

## Yields soften across all precincts

Over the quarter there was 50bps softening in yields across all precincts, with the average prime yield now 4.4% and secondary yields at 4.8%. It is the first time in over a decade that an upward trend for industrial yields has been recorded. With the rise of funding costs and market uncertainty playing out, yields are likely to soften further.

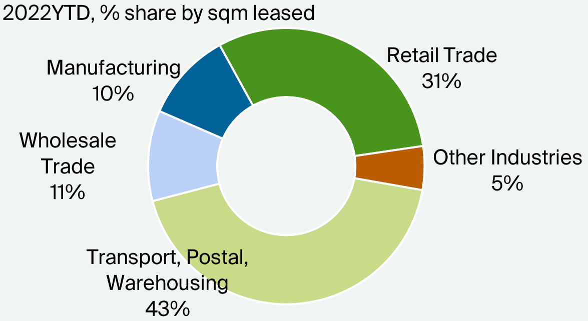
| TAKE-UP (SQM) Q3 | MOST ACTIVE SECTOR Q3-22 | VACANCY (SQM) Q3 | NEW DEVELOPMENT (SQM) |
|---|---|---|---|
| **170,677** | **58%** | **66,648** | **614,825** |
| -7% Q/Q | TRANSPORT, POSTAL, WAREHOUSING | -33% Q/Q | Estimated 2022 (f) |

### Sydney vacancy
By precinct, '000sqm



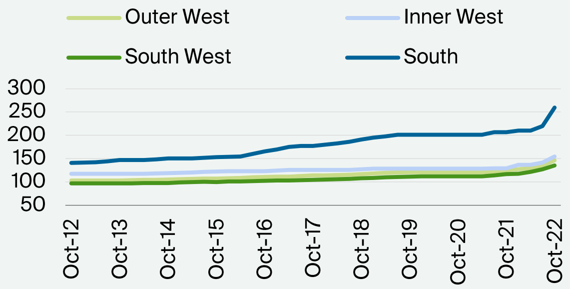

Source: Knight Frank Research

### Sydney Leasing Take-up by Industry
2022YTD, % share by sqm leased



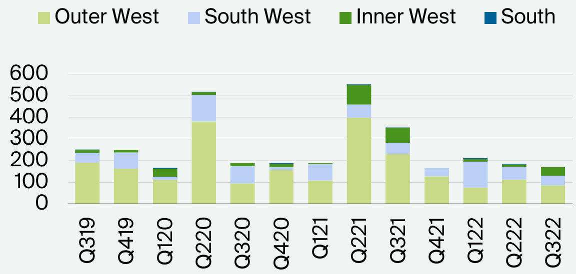

Source: Knight Frank Research

### 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) |
|---|---|---|---|---|---|
| **Go Logistics~** | 11 Grand Ave, Camellia | Inner West | 29,499 | 138 | 10 |
| **National Products** | 1B Raffles Glade, Eastern Creek | Outer West | 13,255 | 142 | 5 |
| **XL Express~** | 26 Pavesi Street, Smithfield | Outer West | 12,770 | 134 | 5 |
| **Brandlink~** | 52 Holbeche Road, Arndell Park | Outer West | 9,628 | 170 | 2 |
| **CSR^** | WH 1A, 52-66 Glendenning Road, | Outer West | 7,463 | 150 | 6 |

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

# MELBOURNE

*Vacancy falls to the lowest in a decade as limited supply and high demand continues to push up rents; yields rise as investors respond to financial markets.*

**By Tony McGough**

## Vacant space drops by a quarter to the lowest since 2012

Demand for industrial space continues to outstrip new supply as vacant space fell to its lowest since April 2012. Overall vacant space fell to 276,913 sqm, down 33.3 % on the quarter. 46.5% of the remaining space is in the South East (128,842 sqm). In the West only 60,479 sqm remains vacant—this is the first time we have recorded vacant space in the West down to a 5-figure number. There are record low vacancy figures in the North (24,313 sqm ) and East (15,531 sqm), highlighting the extremely tight market at present.

## Manufacturing continues to increase its share of activity in the sector

Q3 again showed manufacturing as the most active sector in the market, taking up 57% of let space in the quarter. For the year as a whole, logistics maintains its lead, just, at 38% of take-up versus 35% for manufacturing. This continued trend highlights a new vibrancy in the sector and that it is not just a one-trick pony which has been driven in the last few years by logistics requirements. Other trends in the global economy, such as back sourcing, are now clearly impacting on demand for industrial space. Overall take-up remained similar to last quarter, and off its highs, due to lack of space.

## Most 2022 supply delivered. 2023 already getting pre-committed

Despite delays due to well known supply pipeline issues etc. most of 2022's record expected delivery of new space has arrived already, however there is still 213,386 sqm left to be delivered but this is now arriving at a rapid rate. Of this space, the majority (68.1%), is dropping in the West with most of the remainder (24.9%) in the South East, and over half is also pre-committed. Consequently, there is little relief on pressure for space in the other precincts. People are now considering supply in 2023, which is looking like it will provide a sub-million, 927,160 sqm at present. Of this space, 20% has already been pre-committed. The split for new space in 2023 is roughly 50:30:20 to the West, North and South East, with only a small amount expected in the East.

## Rents continue to rise as there is a search for space

Outside of the Fringe (where rents again remained flat), rents again increased across all precincts and within both prime and secondary. In the markets still to have some space left, prime rents rose quickest, and at an increasing pace compared to the annual figure. In the South East, prime rents were up 7.1% in the quarter (23.5% Y/Y), whilst in the West rents rose 8.1% in the quarter compared to 21.6% Y/Y. In further signs of the scurrying for space, secondary rents in the East, where availability is now very limited, increased by 11.1%, more than double the rate of prime space (4.5%). The North was a similar, if less dramatic story, with secondary rents up 8.2% while prime rose 7.4% . The gap between prime and secondary continues to tighten as tenants look for space.

## Land values stall as investors pause

Whilst the leasing side of the market is very much in favour of the landlord, in terms of land sales, purchasers have paused, and so have land values, following several years of rapid growth. The extra finance and construction costs have brought some reality to the market. Q3 saw land values generally flat in the Fringe, North and East of the city. Larger (10 ha+) lot sizes increased in value in the South East (13.9% to $410/sqm) as evidence of pricing came about with several deals in the quarter. In the West prices fell back. Small lot sizes saw the biggest fall, down 8.9% (to $895/sqm) in Q3, but having risen rapidly, are still up 36.5% Y/Y. This is seen as the market settling at sensible rates rather than the start of major falls.

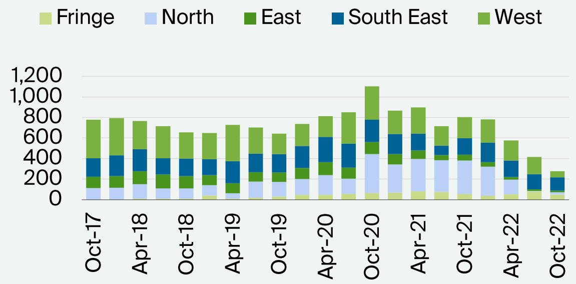
## Yields continue their steady rise

Unsurprisingly, given the present environment in the capital markets, yields continued to move out in a generally orderly manor. Having risen 25bps last quarter, Q3 saw the pace increase as interest rate rises picked up speed and regularity. Q3 saw average yields rise 40bps to 4.58% (41bps to 4.63% excl. the Fringe). Secondary rates rose over 5% to 5.38% (up 47bps) excl. the Fringe and 5.33% (up 38bps) inclusive. The movement out has been less extreme than interest rates, as rental growth still underpins pricing and attracts investors.

| TAKE-UP (SQM) Q3 | MOST ACTIVE SECTOR Q3 | VACANCY (SQM) Q3 | NEW DEVELOPMENT (SQM) |
|---|---|---|---|
| **241,044** | **57%** | **276,913** | **1,308,018** |
| +4% Q/Q | MANUFACTURING | -33% Q/Q | Estimated 2022 (f) |

### Melbourne Industrial Vacancy

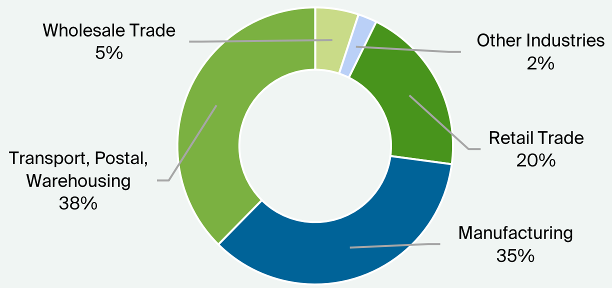
'000sqm by precinct (excl. Design & Construct)




Source: Knight Frank Research

### Melbourne Leasing Take-up by Industry

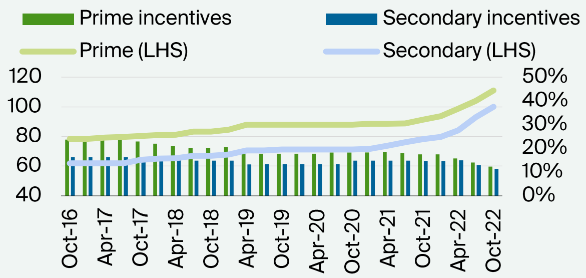
2022YTD, % share by sqm leased




Source: Knight Frank Research

### Melbourne Industrial Rents & Incentives

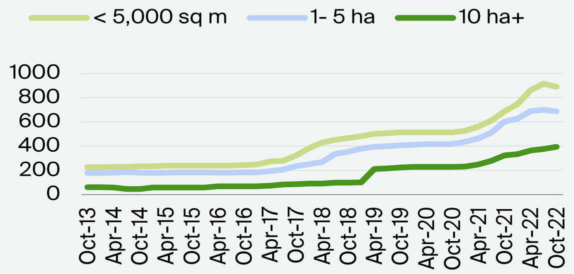
$/ sqm net rents, % incentives; excl. fringe




Source: Knight Frank Research

### Melbourne Industrial Land Values

$/sqm by precinct, excl. fringe




Source: Knight Frank Research

## Recent significant tenant commitments

| OCCUPIER | PROPERTY | PRECINCT | SIZE SQM | NET RENT $/SQM | TERM (yrs) |
|---|---|---|---|---|---|
| **Techtronic Industries#** | Melbourne Airport Business Park, Tullamarine | North | 74,200 | 90 | 10+ |
| **Kitchen Warehouse ^** | Spec 1A, 410 Cooper Street, Epping | North | 17,010 | U/D | 10 |
| **ACFS^** | 97 Australis Drive, Derrimut | West | 24,610 | 100 | 5 |
| **Linfox^** | 101 Castro Way, Derrimut | West | 17,140 | 95 | 10 |
| **Interior Secrets ^** | 143 Foundation Road, Truganina | West | 10,170 | 88 | 7 |
| **Kings Group#** | 143 Portlink Drive, Dandenong South | South East | 15,138 | U/D | 5 |

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

# BRISBANE

*Tenant demand and associated rental growth dominates the market with limited existing vacancy. Investment market remains stalled.*

**By Jennelle Wilson**

## Q3 take-up remains elevated with annual take-up running at just over 1 million square metres

Leasing activity in Q3 was down somewhat from Q2, but remains in line with the elevated levels seen since early 2021. This has seen the rolling 12 months reach 1.05 million square metres, record levels. Take-up was strongest in the South West (92,008sqm), Trade Coast (49,353sqm) and South (48,706sqm) during the quarter. On an annual basis the South remains the strongest with 30% of the market activity, closely followed by TradeCoast at 27% and South West with 25%.

## Inventory upscaling and distribution network expansion dominates activity

Transport, postal and warehouse users with 30% of take-up have overtaken retail tenants (28%) as the most active sector over the past 12 months. Given the limited suitable existing space most relocations are into speculative space (Dutt Transport, Aus Post, TSS) and pre-lease (Wallenius Wilhelmsen. Tasfreight). Pre-commitment activity was lower in Brisbane for Q3 (down to 47,000sqm from 177,000sqm in Q2) although there are a number of requirements remaining.

## Vacancy fell a further 18% in Q3 to 10-year lows as more than half of the availability is in spec space

Vacant space fell a further 18% in Q3 to be 41% lower than a year ago. Absorption of vacant space was down by 12% in Q3 as opportunities were more limited. Take-up of 128,099sqm was dominated by spec absorption of 81,569sqm as existing space only made up 48% of all vacancy. Immediate requirements continue to dominate the landscape with grade becoming less of an issue than location and availability.

Secondary vacancy continues to contract, down by 10% in Q3 and 46% over the past year to 81,722sqm a new low. To put the sustained fall in secondary space into context, there is now 270,738sqm less space available than there was two years ago (October 20), the recent high point. Prime available space fell by 22% in Q3 and is 46% down y/y. Of the 173,235sqm of prime vacancy only 42,025sqm is currently available with the remainder speculative developments still under construction.

## Rental growth accelerating across the market, but secondary rents have been outpacing prime

Average prime face rents increased by 12.3% y/y to $130/sqm net, average incentives have ticked down across existing stock to 13.2% although incentives achieved now range from 0% - 17% depending on tenant/landlord. The secondary market has jumped by 23.4% y/y to $115/sqm net setting new record highs. Economic rents continue to be pushed by high land prices and construction cost and timeframe blowouts and softer yields.

## Supply pipeline remains robust but delays impacting delivery for 2022

New supply has accelerated in 2022 but weather impacts and materials/labour shortages continue to delay completions. Over 226,000sqm has been completed in 2022 to date with a further 178,000sqm under construction and expected to be completed this year. A further 410,000sqm is under construction with completion expected in 2023, some of which will complete early in the year. Underpinned by pre-commitments of 466,000sqm supply in 2023 may exceed 1 million square metres, a new record high.

## Investment volumes reduce as purchasers eye debt cost increases

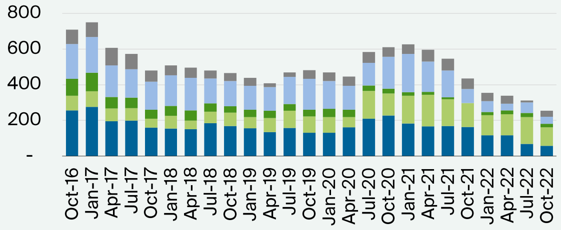
Land values remain high, however prices have begun to moderate as impacts on development feasibility has softened appetite for further price increases. Prices remain elevated on an annual basis with smaller lots (<5,000sqm) up by 18.5% y/y and medium lots (1-5ha) up 27.4% y/y.

Investment market activity has remained constrained with most institutional buyers out of the market until yields stabilise. To date there have been few distressed vendors which means that if the sales campaign does not meet pricing expectations the asset is withdrawn from the market. Sales which have occurred are generally under $20 million with private investors still active while institutional and syndicator buyers are sidelined. Yields softened a further 30-35 points in the quarter with limited direction from sales. This may change in Q4 with greater transactions and steeper softening.

| TAKE-UP (SQM) Q3 | MOST ACTIVE SECTOR RTM | VACANCY (SQM) | NEW DEVELOPMENT (SQM) |
|---|---|---|---|
| **219,903** | **30%** | **254,957** | **404,895** |
| 33% ABOVE THE 5Y-AVG | TRANSPORT, POSTAL & WAREHOUSING | -18% Q/Q | Estimated 2022 (f) |

### Brisbane Industrial Vacancy

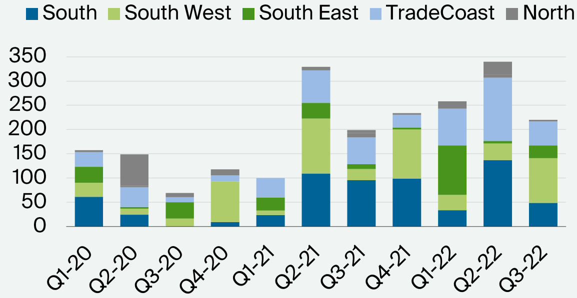
'000sqm available space by precinct




Source: Knight Frank Research

### Brisbane Leasing Take-up

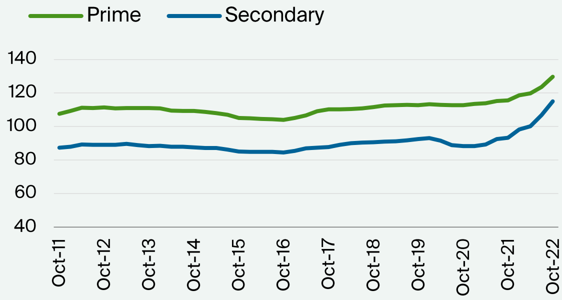
'000sqm by precinct




Source: Knight Frank Research

### Brisbane Industrial Rents

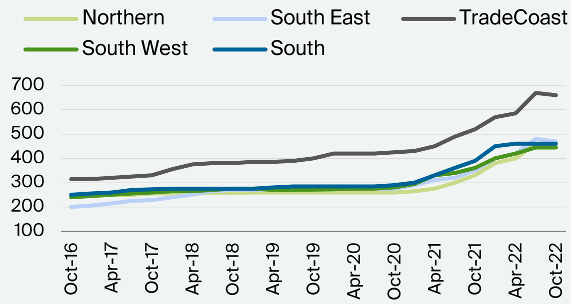
$/sqm average net face




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 |
|---|---|---|---|---|---|
| **Tony Immano Transport~** | 92 Sandstone Pl, Parkinson | South | 13,738 | 100 | 2 |
| **Ausdeck#** | 72 Banderra St, Richlands | South West | 12,915 | 140 | 10 |
| **Trenton^** | 1/500 Green Rd, Crestmead | South | 12,709 | 111 | 5 |
| **Evolution Precast~** | 30 Peterkin St, Acacia Ridge | South | 11,735 | 118 | 7 |
| **Sime Darby^** | 6 Litsea St, Eagle Farm | TradeCoast | 10,000 | 130 | 7 |

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

# ADELAIDE

*Transition from sellers to buyers market in the industrial and logistics sector; as cost of debt increases, land and rental values hold steady*

**By Amanda Azariah**

## Demand continues for strategically located land

The development market has slowed during the second half of 2022, impacted by the cost of debt and rising construction costs, however demand for industrial assets has continued. Parcel delivery, transport and logistics sectors in particular, have shown interest in land located in and around the Adelaide Airport. Two ground leases signed to developers for the construction of new facilities for DHL and Fedex at Transport Avenue, Adelaide Airport highlight this.

Land values for both smaller and larger sized lots have increased in the past twelve months with growth ranging from 30-108% between the precincts. The Outer North observed the greatest increase of 108.4% and is the only precinct in Q3 to have experienced an increase in land values, of 8.8%. This is highlighted by the recent resale of Lot 302 Hercules Drive, Direk, which realised a $718,020 (47.8%) increase in sale price within a three month period.

The Outer North currently accounts for approximately 45.9% of forecasted development to be completed by 2025. It has grown in popularity amongst investors and tenants, along with the Outer South, as these are the regions with the most available land.

## Rental growth due to imbalance of supply compared to demand

Continued rises in construction costs and supply chain issues has hindered production of new supply of industrial space, which, with rising demand levels, is pushing up rental levels for existing stock. A large amount of forecast supply has also been pre-committed to, such as the Nexus North Industrial Estate which sold partially pre-leased to Maxispan.

The net rental rates across all grades for prime and secondary assets have risen by 1.50% to $108/sqm and 2.45% to $83/sqm respectively. Furthermore, record low vacancy rates within the industrial sector have continued, resulting in a decrease in average incentives for prime stock from 7.50% to 7.00% over the past quarter.

We are beginning to notice tenants straying from long-wale opportunities as a way to minimise risk given the current market uncertainty. In addition, we have also noticed tenants opt for smaller units and business parks as vacancy has grown slightly over the last quarter for industrial assets above 5,000sqm.

## Yields have softened while sale and leaseback market slows

Prime yields have softened from 5.55% to 5.80% in Q3. Secondary yields have moved out by roughly the same amount, from 6.65% to 6.89%. In addition, the sale and leaseback market has fallen, with the last sale evidence occurring in August 2022 at 265-273 Cormack Road, Wingfield. The four fully leased office/warehouses sold for $9.5 million reflecting a market yield of 5.89% and a GLA rate of $1,592/sqm.

The current investment volume for industrial assets as at October 2022 is $359.33 million, with approximately $170.7 million or 47.5% occurring within the Outer North industrial precincts with a number of addition sites yet to settle.

## Outlook for industrial sector remains positive despite current threats

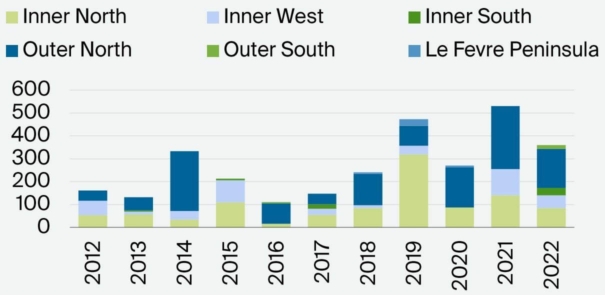
In the face of increasing inflation and recession risks, and the cost and paucity of debt, market activity is continuing, albeit at a slowing pace. Many market participants are currently taking a “wait and see approach” in their investment considerations until the outcomes that these factors may have on asset values becomes clearer.

The combination of high rental rates and low land values in Adelaide compared to the eastern states has highlighted SA as a prime location for all investor groups. Despite the continued rise in interest rates, increasing construction costs and supply chain issues which has caused the market to slow, industrial assets remain a secure investment with historically low vacancy rates and rising rental levels.

| TAKE-UP (SQM) YTD | VACANCY (SQM) | NEW DEVELOIPMENT ($) | NEW DEVELOPMENT SQM |
|---|---|---|---|
| **16,958** | **556,146** | **229.1 M** | **186,528** |
| (5,000SQM +) | (5,000SQM +) | Forecast completion by 2025 | Forecast completion by 2025 |

### Adelaide Industrial Sales

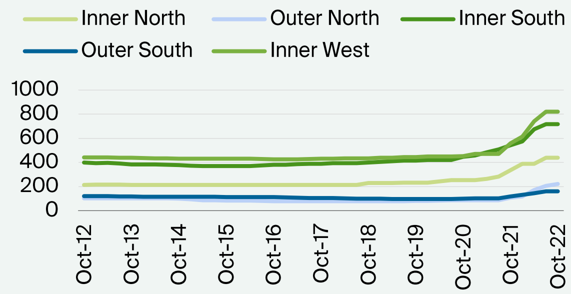
$5mil sales, 2012 to 2022




Source: Knight Frank Research

### Adelaide Industrial Land Values

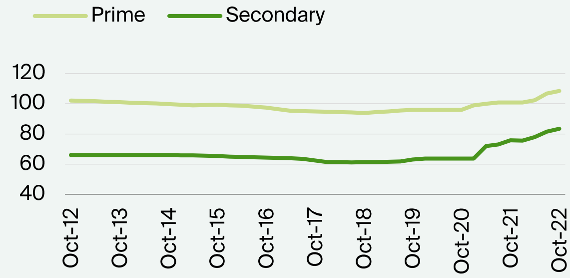
Average $/sqm by precincts for land <5,000 m²




Source: Knight Frank Research

### Adelaide Industrial Rents

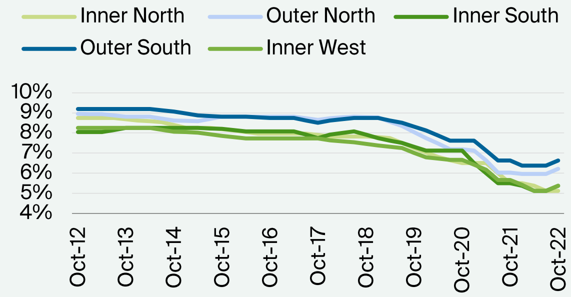
Average $/sqm p.a. net face by grade




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) |
|---|---|---|---|---|---|
| **Apex Steel** | 36 Caribou Drive, Direk | Outer North | 21,780 | 92 | 15 |
| **Cosentino Australia** | 6 Capelli Road, Wingfield | Inner North | 2,220 | 101 | 5 |
| **Industrial Fitting Sales** | 3 & 4/209 Cormack Road, Wingfield | Inner North | 1,174 | 125 | 5 |
| **Webb Haulage** | 36-36A Francis Street | Inner North | 3,467 | 75 | 3 |
| **Fraser Fire and Rescue** | 34 Cheltenham Parade, Woodville | Inner West | 3,482 | 89 | 5 |

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

# PERTH

*Robust occupier demand and limited availability fuels unprecedented rental growth*

**By Naki Dai**

## Strongest rental growth in the county

Strong occupier demand particularly from rising e-commerce activity keeps driving the leasing market. Q3 experienced another period of limited availability, with c.77,000sqm space sitting vacant across the market.

The substantial demand growth is also backed by the logistic business structure adjusting from 'just in time' to 'just in case', which encourages tenants to double their facility sizes with intense competition for limited available space on the market. This has resulted in the Perth market being the strongest performer nationally in terms of rental growth.

Perth prime industrial rents surged by 14% on average during Q3, reaching an unprecedented annual growth level of 32%. Additionally, 50% prime industrial rent growth (y/y) was recorded in the southern precinct which stood head and shoulders above the eastern and northern precincts where the annual growth rates recorded were 30% and 18% accordingly.

With the future container terminal in Kwinana planning in progress, the southern precinct will likely see further rental growth in the near term.

## Tight land supply

The relatively affordable industrial market and limited development opportunities on eastern seaboard capital cities has prompted developers to seek opportunities in Perth.

On the other hand, the active e-commerce and traditional manufacturing and mining industries have rapidly absorbed the existing zoned and serviced land, particularly in sought-after industrial locations including Kewdale, Welshpool and Canning Vale.

The tightening of land supply in eastern and southern precincts has not only added to the pressure on pricing in the land market but also brought the sub-prime and secondary areas now increasingly attractive for developers.

## Southern and eastern land values reach new highs

The robust demand and scarce supply has put upward pressure on land values. Land values for medium-sized lots rose by 5.6% on average during Q3 to be up by 22.1% over the year. Despite unvaried land value movements captured in the northern precinct, medium lots land values in eastern and southern precincts were up 5.4% and 11.5% in Q3 respectively.

Medium lot land values in eastern precincts take the lead of the region, with the highest land values reported in Belmont, Kewdale and Welshpool, achieving over $500/sqm. Meanwhile, land values in certain southern locations like O'Connor and Henderson have risen over 50% y/y.

It is worth noting that the erosion of the traditional discount for larger lots is another aspect of the tightening land market. The gap between the value per sqm of sub 5,000 sqm lots and 1 -5 lots has narrowed significantly, reflecting the tenants' large-scale requirements for holding stock in hands in the case of the next unforeseeable disruption and the greater confidence in the land market.

## Yield softening trend in line with other states

After a prolonged period of yield compression, the Perth market is beginning to see pricing adjust in response to the higher cost of debt. While transactional activity has been limited over the quarter, the attitude of buyers has clearly shifted and current sentiment points to softening of yields.

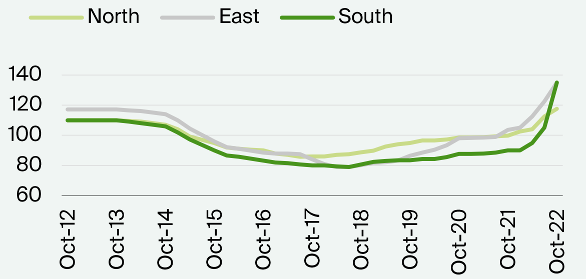
All precincts experienced a modest yield expansion of 25 bps over Q3, with the average prime yield at 5.83% and the average secondary yield at 6.88%. Yield is expected to soften further for adjusting to rising debt costs in the near future.

Notwithstanding the softening trend of yield keeping in step with the nation, buyer appetite for Perth industrial assets remains strong with several investors searching for the yield value that Perth offers compared to the eastern seaboard.

| PRIME RENTAL GROWTH | LAND VALUE GROWTH (<5,000SQM) | LAND VALUE GROWTH (1-5HA) | PRIME YIELD SHIFT |
|---|---|---|---|
| **14.0%** | **15.7%** | **22.1%** | **+25 BPS** |
| Q/Q AVERAGE ACROSS ALL PRECINCTS | Y/Y AVERAGE ACROSS ALL PRECINCTS | Y/Y AVERAGE ACROSS ALL PRECINCTS | YIELDS MOVE OUT IN Q3 |

### Prime Average Rents by Precinct

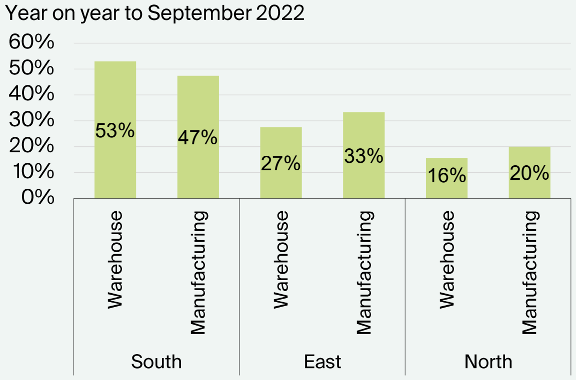
$/sqm net face




Source: Knight Frank Research

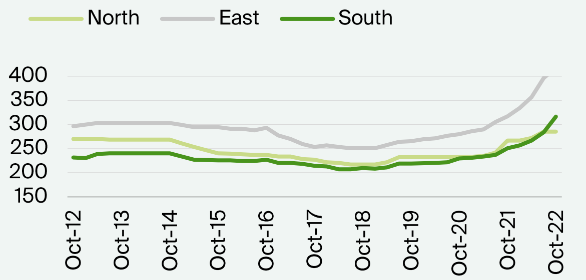
### Prime Rent Growth by Precinct

Year on year to September 2022




### Perth Land Values by Precinct

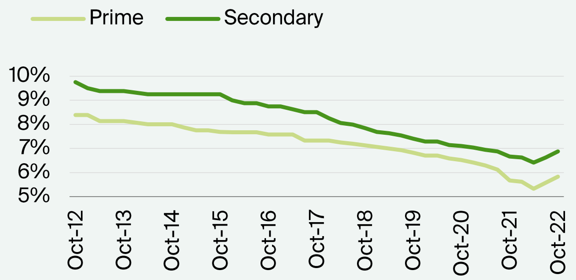
Average $/sqm, Medium Lots 1-5ha




Source: Knight Frank Research

### Perth Industrial Market Yields

Prime vs Secondary (Averages)




Source: Knight Frank Research

## Recent significant tenant commitments

| OCCUPIER | PROPERTY | PRECINCT | SIZE SQM | NET RENT $/SQM | TERM (yrs) |
|---|---|---|---|---|---|
| **AGC Industries~** | 15 Beach Street, Kwinana Beach | South | 11,670 | 86 | 10 |
| **AirGroup~** | 8 Gauge Circuit, Canning Vale | South | 6,698 | 140 | 5 |
| **Sinopec ~** | 21 Logistics Boulevard, Kenwick | East | 2,825 | 170 | 10 |

# 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 | 63-69 Pipe Road, Laverton North | 57.4 | 25,898 | 2,216 | ESR | Harmony | 4.5 | 4.6 |
| Melbourne | 1, 1A, 13 & 17 Magnesium Place, Truganina | 64.24 | 25,085 | 2,561 | Frasers Commercial Trust | Goodman | 3.67 | 6.49 |
| Melbourne | 147-153 Canterbury Road, Kilsyth | 22.25 | 11,882 | 1,872 | ESR | Dexus | 3.90 | 5.08 |
| Melbourne | 45-49 Vella Drive, Sunshine West | 11 | 5,350 | 2,056 | Centennial Industrial & Logistics | Australian Securities | 4.4 | 3.8 |
| Sydney | 30 Clay Place, Eastern Creek | 34.5 | 6,183 | 5,580 | FIFA Capital | Centuria | 3.48 | 3.4 |
| Sydney | 6 Shale Place, Eastern Creek | 16.25 | 3,933 | 4,132 | Pittwater Capital | Leda | 3.82 | 0.2 |
| Sydney | 5 Yarrawa Street, Prestons | 58.3 | 15,066 | 3,870 | Pittwater Industrial | Loftex Property | 3.3 | 7 |
| Brisbane | 34 Iris Place, Acacia Ridge | 13.6 | 6,867 | 1,980 | RF Corval | Pathway Sixteen Pty Ltd | 6.1 | 3.6 |
| Brisbane | 344 New Cleveland Rd, Tingalpa# | 17.5 | 6,149 | 2,852 | Trident Funds Mgt | Ferra Engineering | 5.25 | 20 |
| Brisbane | 97 Trade St, Lytton# | 16.0 | 6,600 | 2,424 | Private Investor | KWB Group | 5.16 | 10 |
| Adelaide | 27-30 Sharp Court, Cavan | 23.2 | 8,200 | 2,835 | Centuria | Harmony | 4.21 | 5.4 |
| Adelaide | 5 Talisman Ave, Edwardstown | 20.1 | 9,500 | 2,121 | MA Financial | Private | 4.56 | 6.6 |
| Adelaide | 300 Richmond Road Netley | 71.3 | 134,714 | 42,112 | Harmony Corporate | Charter Hall | 4.45 | 2.5 |
| Perth | 189 & Lot 59 Bushmead Road, Hazelmere | 23.5 | 6,160 | 3,815 | Altis | Private | 4.83 | 6.2 |
| Perth | 15 Beach Street, Kwinana Beach | 16.2# | 11,670 | 1,388 | Redhill | Leaseback | 6.17 | 9.9 |
| Perth | 23-29 Fargo Way, Welshpool | 11.98 | 7,670 | 1,563 | RF Corval | Prop & Pathways | 6.09 | 1.4 |

[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.

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