Is now the time to develop?

Q2 2025

Melbourne's CBD faces a tightening premium office market, as new supply slows and pre-commitments rise, creating an opportunity for future developers to fill the gap.

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- *Forecast supply has sharply declined since its 2020 peak*
- *Pre-commitments are limiting tenant access to new supply*
- *Premium-grade supply is highly constrained in coming years*
- *Only 3 major new CBD completions (>25,000 sqm) by 2029*

89k sqm
Total premium office space under construction between 2025-29 in Melbourne's CBD.

45.5% pre-comm
Amount of the forecast 5-year premium supply already pre-committed.

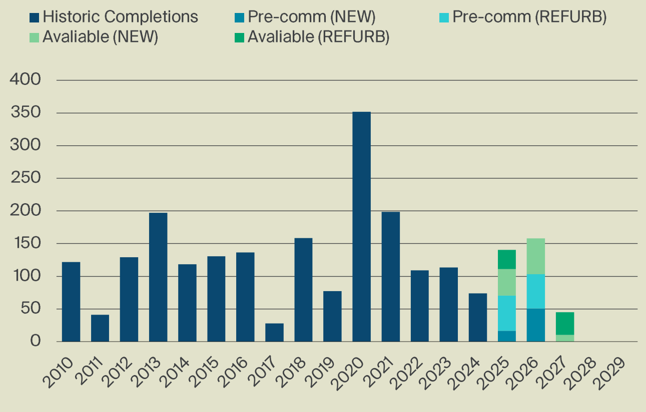
NEW SUPPLY IN THE CBD IS RUNNING LOW

Post GFC, Melbourne's CBD experienced a wave of new office supply, driven by historically low vacancy rates and robust economic growth. But with increasing global uncertainty development conditions are now brittle. As a result, the forecast pipeline has contracted significantly, with only three new office buildings larger than 25,000sqm currently expected to complete before the end of 2029. While headline figures suggest a robust delivery in the near term—140,000sqm in 2025 and a further 158,000 sqm in 2026—supply then dries up. High levels of pre-commitment and a growing share of refurbished or reintroduced stock limit the volume of truly new, uncommitted space entering the market. At present, only 48% of forecast total supply is from new developments with 34% of that pre-committed.

New premium office space is about to become scarce. Only two premium-grade developments are currently under construction in the CBD: 51 Flinders Ln (29,000sqm) and 435 Bourke St (60,000sqm). Initially viewed as speculative plays, both projects now appear well-positioned in the current market. 435 Bourke St, led by Cbus Property, has secured major pre-commitments from UniSuper and CBA, totalling 30,500sqm. This means less than half of the building's NLA is available with 12-18 months to go before completion. Meanwhile, 51 Flinders Ln, developed by GPT, has achieved a 34.5% pre-commitment (10,000sqm), most notably through WPP's 4,500sqm lease. Its boutique floorplates may limit appeal for larger occupiers, but early leasing momentum suggests strong ongoing interest.

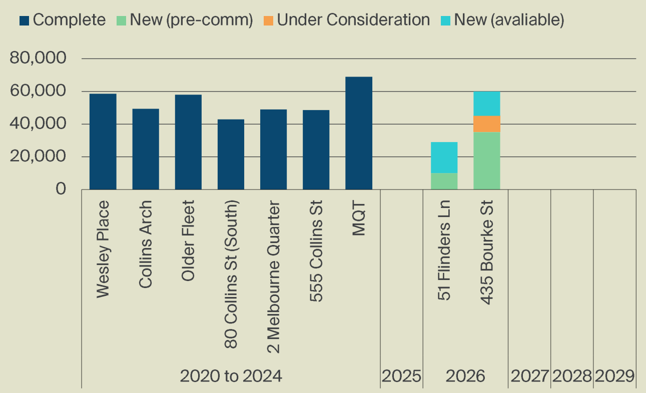
So, at the current time, just 40,500sqm of new premium office space is available for leasing in the CBD through to 2029. With a law firm recently looking at a 10,000sqm HOA at 435 Bourke St this falls to 30,500sqm if signed, pushing pre-commits from 45.5% to 56.7%. Combined with the solid letting performance of recent premium completions (see next section), this points to an emerging shortfall and presents a potential opportunity for developers to respond to a tightening segment of the market.

Melb CBD new supply pipeline
by commitment type and completion status, 000's sqm



Source: Knight Frank Research, PCA

Melb CBD premium office dev. pipeline
by completion status and precommitment level, sqm



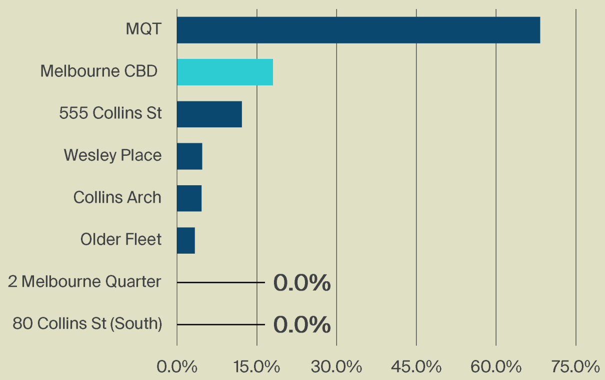
Source: Knight Frank Research, PCA

NEW PREMIUM IS A STRONG PERFORMER, BUT GET YOUR LOCATION RIGHT

The PCA numbers say there is 16.8% premium grade vacancy, but this is concentrated in older premium buildings. Over the past five years, seven premium-grade towers were added to Melbourne's CBD, with consistently strong leasing outcomes. Most of these assets reached sub-5.0% vacancy shortly after completion, with standout performers such as 80 Collins St South and 2 Melbourne Quarter achieving full occupancy. These outcomes are particularly compelling when benchmarked against the broader CBD vacancy rate, which remains elevated at 18.0%.

In a market with elevated incentives and vacancy rates; an access to services and excellent location is increasingly important in driving leasing outcomes. The performance of Melbourne's newest premium towers highlight the strength of demand for well-located, high-quality stock and offers a lower risk profile for developers' future premium office projects.

New premium buildings record low vacancy
Vacancy rate by premium building in Melbourne's CBD



Source: Knight Frank Research, PCA

WILL THE DEVELOPMENT DROP INTO RISING CAPITAL VALUES

Melbourne offices have faced price corrections and capital value falls before. However, when this has occurred there has been far more space coming on to the market (as a % of stock). Looking at what was delivered in the 3 years after capital values began to fall (so virtually unstoppable) 5.9% of stock was being delivered into the market following the dot.com crash and 3.8% was in development after the GFC. The latest fall in capital values began with 2.4% of additions expected and this is falling rapidly. This augurs well for the overall office market in Melbourne and the prospect of the return of rental growth. Previously, there was a high development pipeline as capital values fell, now there is not, particularly for premium.

RENTAL GROWTH DRIVES CAPITAL VALUES, NEW PREMIUM BUILDINGS WILL BE PERFECTLY PLACED

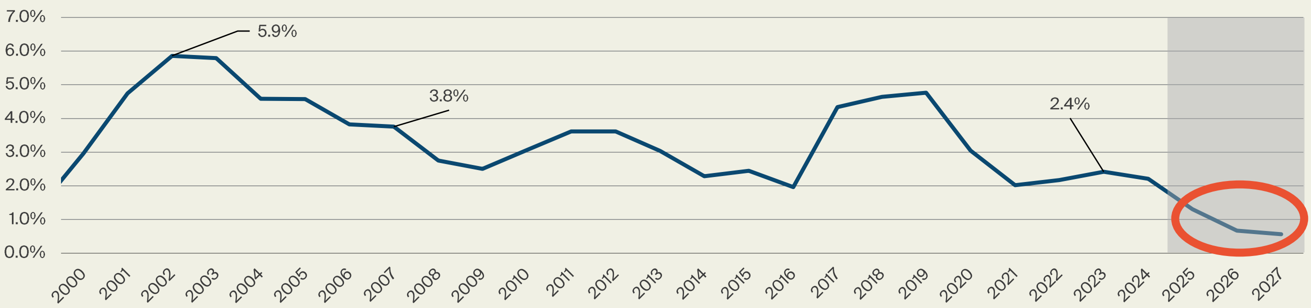
The table below also shows that capital value recovery is invariably driven by rental growth, yields do not need to get back down to their previous levels. Indeed, after the dot com crash yields did not return to their previous lows for 61 quarters (that's over 15 years and after the GFC!). They only stabilised and dropped back from their highs. The rental recovery pushed the capital values back to their previous highs and beyond.

We are not forecasting yields to return to their record lows any time soon (we expect them to stabilise and then compress slightly). But with very low supply and a growing economy, this will be enough, the implications are that capital value recovery will be fuelled by rental growth, not total yield recovery. Delivering a premium building, with limited competition for new premium space, strengthens the likelihood of obtaining this rental growth.

Even now the pre-commit on 51 Flinders Ln is achieving rent of circa $1,500/sqm on its top floor. This more than matches the standard upper floor pricing in the best towers in the Eastern Core, which have themselves been under less pressure than other buildings during the downturn.

	CV Peak	CV Trough	CV Recover	Rents Trough	Rents Recover	Yields Peak	Yields Recover
Dot Com Crash	Jul-01	11Q	19Q	7Q	18Q	11Q	61Q
GFC	Apr-06	6Q	15Q	5Q	13Q	8Q	31Q

3-year forward average annual gross supply additions as a % of stock
% of CBD stock



Source: Knight Frank Research

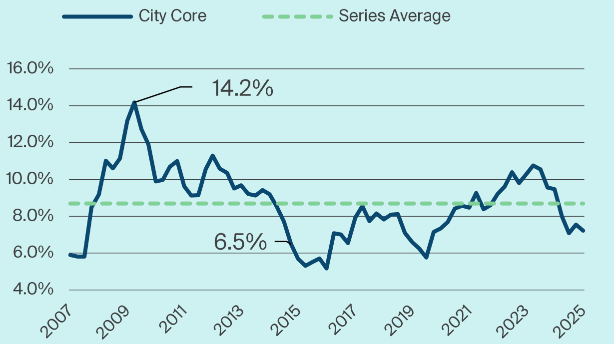
Fortune favours the brave...

The London market has faced similar cyclical volatility leaving developers in a quandary. For example, site clearance for the Shard began in 2008 and building began in 2009. With the GFC in full flow many projects faced financial problems. The Shard only continued due to strong backing from the State of Qatar. Their argument was little was being built so when complete it would lease well. They paid off a pre-commit from Transport for London (think PTV) to get better quality tenants. The aim, build when there is no premium building been built and let to high-end tenants. It completed in November 2014 and started taking tenants with vacancy rates in London near a low at 6.5%. It was fully let in 2017. The Cheesgrater then followed suit, building began in 2010, completed in 2014 and, being in the City, got fully let by 2015.

The Pinnacle also started in 2008 and was planned as the UK's tallest building. With no pre-let, and in the depth of a recession, construction stopped in 2011 with a 7 storey lift core all to show for £400m of prep work – it became the Stump. In 2013 it was re-designed but stalled again. AXA bought into the project in 2015, and it was redesigned as 22 Bishopsgate. The Stump was removed in December 2015 and building began at a low point for vacancies. However, it only got completed as 22 Bishopgate in 2020! With a lot of competition and vacancy rates rising, it was only finally fully let in Q1 2025 – that's this year.

London city core vacancy rate

The Shard project began as the vacancy rate peaked at 14.2%



Source: Knight Frank Research London

The Stump, London

14.2% vacancy rate as they built the Shard

" It is important to develop into where the market will be, not where it is."

- Dr. Tony McGough

The Shard, London

The Cheesegrater (122 Leadenhall St), London

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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