



MELBOURNE CBD

RETAIL MARKET BRIEF JUNE 2018

Key Facts

Vacancy in the Melbourne CBD retail core increased marginally since June 2017 however **vacancy at June 2018 remains low at 3.1%**.

New leasing activity in Melbourne's CBD was driven by **luxury brands and food retailers**.

Investment activity is down in 2018, due to a **scarcity of investment opportunities** presented to the market.

Private investors accounted for approaching half of total sales by value in the 12 months to June 2018.



FINN TREMBATH
Associate Director

The Melbourne CBD retail core continues to experience healthy demand, as the retail landscape evolves through changes to the retail mix.

Retail Overview

The vacancy rate in the Melbourne CBD retail core remains low albeit it is now slightly above the long term average having risen marginally compared to a year ago.

The increase in vacancy was driven, in part by Shopping Centres, and in particular St Collins Lane. Elsewhere, Arcades recorded the largest decrease, while vacancy for retail shops offering Street Frontages increased marginally.

The rise in overall vacancy can also be attributed to vacancy levels increasing along Street Frontages, especially Elizabeth Street, Flinders Lane and Little Collins Street. In contrast, vacancy in the super prime precinct of Bourke Street Mall remained at 0.0% for the fifth consecutive year.

In terms of composition, the tenancy mix in the Melbourne CBD retail core remains dominated by clothing and food retailing. Six in every ten shops fall into one of these two retail categories.

Delving deeper, Shopping Centres account for the majority of clothing, footwear & soft goods retailers, while food retailers are mainly found within Street Frontage retailers.

A notable observation from this year's survey is the changing nature of the retail landscape. International retailers continue to set up shop in the CBD, with the total number of international retail brands now more than double that recorded in 2010.

Moreover, leasing activity in the Melbourne CBD retail core was highlighted by luxury international retailers leasing along the sought-after Collins Street, and Melbourne CBD's growing residential and daytime population has resulted in numerous food retailers leasing space in the CBD.

While retail investment sales volumes fell considerably in the last 12 months, it should be remembered the previous year's volume was driven almost entirely by the St Collins Lane sale.

MELBOURNE CBD RETAIL CORE SURVEY

Population, employment & tourism growing

Population and employment growth in Melbourne's CBD, coupled with a burgeoning tourism industry provide a solid foundation for retail in Melbourne's CBD.

According to the Australian Bureau of Statistics (ABS), between June 2016 and June 2017 the CBD residential population increased by 11.2% to reach 46,104, while CBD white collar employment, as measured by Deloitte Access Economics increased by 6.0% to reach 301,825 in the three years to December 2017.

Furthermore, total inbound international tourism numbers for Victoria (Tourism Research Australia) increased by 16% to reach 2.9 million over the 12 months to December 2017, with Chinese tourists leading the influx.

In line with this, the ABS reports that retail trade in Victoria totalled \$6.5 billion for April 2018, up from \$6.3 billion in the previous year.

Vacancy still low despite recent increase

As at June 2018, the vacancy rate in the Melbourne CBD retail core remains low albeit slightly higher than 12 months earlier. The vacancy rate is now marginally above the historical average of 2.9%.

TABLE 1
Melbourne CBD Retail Core*
Vacancy by retail type (%)

	Jun-17	Jun-18
Arcades/ Laneways	4.9	4.1
Street Frontages	3.5	4.0
Shopping Centres	1.0	1.7
Total Retail Vacancy	2.7	3.1

For definition of Retail Core see back page

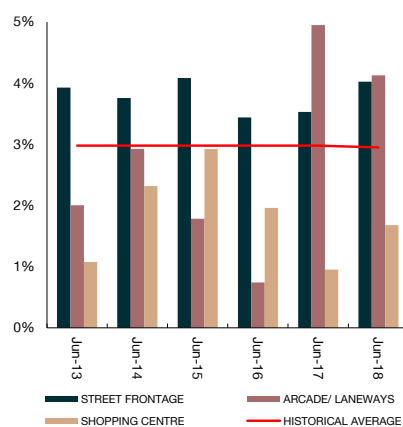
Source: Knight Frank Research

The largest increase in vacancy over the past 12 months was recorded in Shopping Centres, which increased from 1.0% to 1.7%, though vacancy is still below the long-term average of 2.9%. There are 14 shops available for lease compared with 8 a year ago. Vacancy in Shopping Centres is driven by and large by St Collins Lane (9.2% vacancy), with much of the vacant space here located in the food court (22.2%).

Arcades recorded the largest decrease in vacancy, falling from 4.9% to 4.1%. This was driven in part by several beauty salon tenant commitments at Centreway Arcade, and numerous Asian food retailer tenant commitments at Mid City Arcade and Tivoli Court.

Vacancy for retail shops offering Street Frontages increased from 3.5% to 4.0% over the past year, brought on by an increase in vacancy levels on Little Collins Street (up from 2.7% to 10.9%), underpinned by Ted Baker and Calibre vacating their premises at Council House.

FIGURE 1
Melbourne CBD Retail Core Vacancy
% of total number of shops



Source: Knight Frank Research

In the last 12 months vacancy levels doubled along Elizabeth Street (up from 1.7% to 3.4%) and Flinders Lane (up from 2.4% to 5.0%). The Elizabeth St vacancies were driven by several food retailers vacating their premises.

The vacancy rate in the super prime

precinct of Bourke Street Mall remained at 0.0% for the fifth consecutive year. Key tenant commitments included Rebel Sports in the basement at 314-357 Bourke St Mall, and Pandora at 280-282.

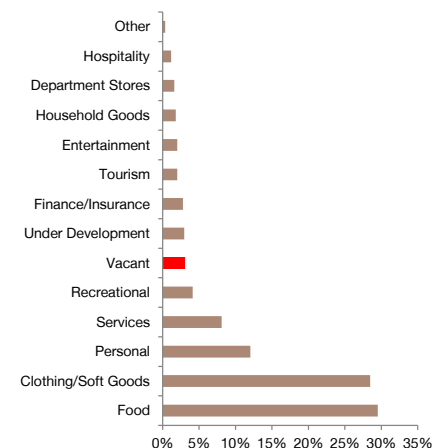
Looking forward, the Walk Arcade will be replaced by a mix use project including two hotels and new retail space.

Clothes & food dominate despite declines

The tenancy mix in the Melbourne CBD retail core remains dominated by clothing and food retailing, collectively accounting for 61.7% of the total number of shops. Despite a decline of 1.4% points compared to a year ago, food retailing is still the largest retail type at 31.4%.

Clothing retailing - the second largest retail type at 30.3% - also saw a decrease of 3.2% points. Footwear retailers (Mountfords on Bourke Street and Joanne Mercer on Elizabeth Street) and Unisex clothing (Godwin Charli at Emporium and Ted Baker on Little Collins Street) were notable vacancies.

FIGURE 2
CBD Retail Core Tenancy Mix
% of total number of shops



Source: Knight Frank Research

Shopping Centres account for the majority of clothing, footwear & soft goods retailers, while food retailers are mainly found within Street Frontage retailers.

TABLE 2

Distribution of Clothing and Food

	Clothing	Food
Arcades/ Laneways	11%	21%
Street Frontages	28%	44%
Shopping Centres	60%	36%

Source: Knight Frank Research

Notable additions to Melbourne's CBD retail landscape in the last 12 months were Hallmark Group's Emirates House and UK department store Debenhams, both of whom opened in the second half of 2017. Located between Collins Street and Flinders Lane, Emirates House has 2,000m² of retail space across two levels and three shops. Luxury retailers Burberry and The Hour Glass, and upmarket café Brunetti's have set up stores within the building. Around the corner, Debenhams has 4,000m² of flagship space at St Collins Lane, primarily in the basement.

International retailers on the rise

International retailers continue to set up shop in the CBD. The total number of unique international retail brands increased to 157, up from 137 in 2016-17 and now 2.4 times the 65 recorded in 2010. Clothing & footwear (53.5%) and personal goods retailers (25.5%) are the most dominant operators amongst international retailers. In response to Melbourne's burgeoning food scene, the past year has seen the arrival of a number of specialty food retailers such as Godiva (chocolates) and Uncle Tetsu's Cheesecake.

Leasing driven by rising population & luxury brands

Leasing activity in the Melbourne CBD retail core was highlighted by luxury international retailers Versace, Fendi and Bottega Veneta leasing along the sought-after Collins St. Other notable luxury brands, such as YSL and Hublot have been looking for space in the CBD's Paris-end, due to favourable conditions brought on by population and tourism growth.

Melbourne CBD's growing residential and daytime population has also resulted in numerous food retailers leasing space in the CBD, in particular Asian inspired eateries (such as Mr Crackles and Nong Tang Noodle House on Bourke Street).

Melbourne's appetite for coffee is also driving leasing activity with Starbucks expanding its Melbourne footprint leasing 168 Exhibition Street, and Coffee and Jaffles opening at The Causeway.

Rental rates across the Melbourne CBD retail core have remained stable over the past 12 months, however, moderate rental growth has occurred in the super prime retail core of Bourke Street Mall.

As at June 2018, gross rents in the Bourke Street Mall range between \$8,000/sq m to \$10,000/sq m. Prime Street Frontage rents range between \$1,500/sq m and \$5,000/sq m. Rents in Arcades average \$1,600/sq m while Shopping Centres attract rental rates between \$800/sq m and \$2,000/sq m.

Investment activity down

Retail investment sales volumes at June 2018 fell by 63% from the prior 12 months. Sales in excess of \$1M totalled \$100.6M from 19 properties in the 12 month period. While this is down on the \$274.8M recorded in the 12 months to June 2017, the 2016-17 volume was driven almost entirely by the St Collins Lane sale. Nevertheless, volumes were notably below the long-term average of \$177 million, and are back to levels last seen in 2012-13. These declines have been driven by a scarcity of investment opportunities presented to the market.

Approaching half of all sales were by private investors, the largest of which was 220 Bourke Street for \$15.2M. Offered for sale for the first time in 80 years, the property is home to tenants including Cotton On.

Prime yields for freehold street frontage retail assets range between 3.00% and 4.00% whilst prime yields for strata retail assets range between 3.50% and 4.50%.

TABLE 3

Recent Sales Activity Melbourne CBD Retail

Address	Price (\$ m)	Core Market Yield (%)	GLAR (sq m)	\$/sq m of GLAR	Date
220 Bourke St	15.20	3.00*	1,040	12,996	Apr-18
72-74 Bourke St	7.25	2.90*	254	28,543	May-18
185-187 Lonsdale St	10.15	3.94*	550	18,455	Mar-18
261 Franklin St	1.00	4.60*	82	12,195	May-18
321 La Trobe St	3.03	4.28*	108	27,778	Apr-18
21-23 Elizabeth St	9.62	2.54*	750	12,827	Mar-18
9-11 Hardware Lane	11.57	2.80*	506	22,866	Aug-17

* Initial Yield

TABLE 4

Recent Leasing Activity Melbourne CBD Retail

Address	Tenant	Gross Rent \$/sq m	GLAR (sq m)	Term (yr)	Date
168 Exhibition St	Starbucks	1,263	117	7	Apr-18
164 Bourke St	Mr Crackles	1,046	150	U/D	Mar-18
85 Collins St	Fendi	U/D	400	U/D	Oct-17
143-153 Collins St	Versace	U/D	307	10	Dec-17
19-25 Russell St	Culture Kings	1,213	600	10	Sep-17

U/D undisclosed.

Source: Knight Frank Research

Outlook

A number of factors indicate the Victorian economy is forecast to continue to strengthen over the medium term, which should have a positive flow-on effect on the retail sector.

By the end of 2018, 2,800 apartments are expected to be completed in the CBD. An additional 300 apartments are currently under construction, or being marketed, and due for completion by 2020. Reflecting this, the ABS predicts solid population growth of 4.1% between 2018-2020. Flowing from this, white collar employment is expected to grow by 4.0% during the two year period, and in line with this Knight Frank Research forecasts the office market to operate at near capacity with vacancy levels to hover around 4.6% to 4.1% between 2018-20.

Combined, these factors should continue to support demand from retailers looking to expand their footprint into the precinct. Indeed, retail turnover growth is forecast by Deloitte Access Economics to increase at an average of 3.0% between 2018-2021, and an expected increase in wages

Retail Core Definition:

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

should further support the retail industry.

Competition to bricks and mortar retail will come from online retail, which is growing and is tipped to reach 10% of all retail trade by 2020. The growth of online retail could potentially be accelerated by Amazon which launched in early 2018, and by tactical marketing initiatives such as eBay's 'eBay Plus' offer which provides for unlimited deliveries and returns. Electronics, clothes and books retailers are most likely to feel the impact of the rise in online retail.

Construction of the Melbourne Metro Tunnel will continue throughout 2017-18. While the project will result in some short-term disruption to retail trade (already the works have seen the demolition of Port Philip Arcade with its accompanying shops), longer term it is expected the addition of two new CBD rail stations will positively impact retail trade in Melbourne's CBD. The project is due to be completed by 2022.

As a result of continued investor interest for Melbourne CBD retail assets, prime yields are expected to remain firm.

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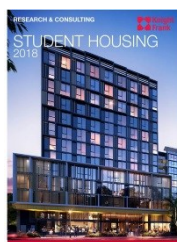
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