

RESEARCH



The Little Diner



MELBOURNE CBD

RETAIL MARKET BRIEF JUNE 2019

NEW PRECINCT EMERGES ON ELIZABETH ST NORTH

Key Facts

Vacancy in the Melbourne CBD retail core increased in June 2019 and now sits at **4.4%**.

As a percentage of shops, **clothing/footwear/soft goods** retailing has **declined** (27.3%, was 30.3%) while **food retailing** has **increased** (33.4%, was 31.4%).

Retail sales investment activity increased by **146%** from the prior 12 months. Sales volumes are now more in line with longer term trends.

One in every three **sales** in 2018-19 were by **private investors**.



FINN TREMBATH
Associate Director

Today's new generation—Millennials and Generation Z—are driving retail demand in Melbourne's CBD, and this has resulted in the emergence of a new retail precinct along the northern end of Elizabeth Street.

Retail Overview

Vacancy in Melbourne's CBD retail core has risen to 4.4%. The rise in vacancy has been driven by an increase in vacancy at shopping centres, in particular at Emporium. The lift in vacancy at Emporium however was in large part caused by the departure of Topshop which went into administration in 2017, and as such is not a reflection on Emporium which has historically enjoyed low levels of vacancy. Indeed, while total vacancy has risen in 2019, demand for retail is felt to remain strong due to Melbourne's strong economic fundamentals.

Moreover, the last few years has seen retail in the CBD evolve with adjustments to the retail mix ushering in a new-found market equilibrium. While E-Commerce has no doubt affected clothes retailing, in its place food retailing has flourished off the back of residential population and international student population growth. In essence, Melbourne's CBD retail market has responded to a shift in the CBD's demographic profile which has paved the

way for new consumer needs.

In response to this, in 2019 the Knight Frank CBD Retail Survey scope has been redefined, to include the area north along Elizabeth Street between La Trobe Street and Therry Street, which in the last few years has seen over 50 new retail stores set up shop, many of which are food retail businesses. The broadening of the survey scope reflects the recent transformation of retail in Melbourne's CBD, that has seen high density inner city living create a heightened appetite for food retailing.

Reflecting this, retail leasing activity in the CBD was driven by food retail, with much of this concentrated along Flinders Street and Elizabeth Street. The recent prominence of tech-enabled food delivery services such as Uber Eats, Easi and Deliveroo has helped fortify the CBD's many food retail businesses, by creating new revenue streams and in some instances dispensing with the need for large retail floor plates.

MELBOURNE CBD RETAIL CORE SURVEY

Melbourne's CBD displays resilience in the face of challenging retail headwinds

Set against the backdrop of continued slow wage growth, retail sales in Australia remain subdued with Australian Bureau of Statistics data revealing sales fell 0.1% during the first quarter of 2019 - the largest decline since the September quarter 2013 - while over the year retail turnover increased by 1.1%, the slowest increase recorded since 2011.

And yet despite this and the ongoing challenges presented by E-Commerce, retail in Melbourne's CBD remains healthy. Underpinned by record residential population growth and strong international student and tourism numbers, the city centre's premium location continues to draw tenant demand, and a recent upswing in food retail has offset declines in clothing retail.

Vacancy increases to 4.4%

Melbourne CBD's retail vacancy rate has risen to 4.4%. The rise has been driven by an increase in vacancy at shopping centres, in particular at Emporium where vacancy increased from 0.8% in 2018 to 6.5% in 2019. The lift in vacancy at Emporium was in part caused by Topshop which vacated 8 spaces across two floors.

While on the surface Emporium's 6.5% vacancy can appear high, it is worth remembering outside of its inaugural year

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

	Jun-18	Jun-19
Arcades/ Laneways	4.1	3.8
Street Frontages	4.0	4.8
Shopping Centres	1.7	4.3
Total Retail Vacancy	3.1	4.4

*For definition of Retail Core see back page

Source: Knight Frank Research

Emporium has never experienced vacancy higher than 1.6% (June 2016), and with other big fashion labels expanding their Melbourne footprint (H&M at Northland and The Glen, and Uniqlo at Docklands) Emporium's current vacancy can be interpreted as transitory with an expectation occupancy will increase in the next 12 months.

Furthermore, Melbourne CBD's retail vacancy has been incredibly stable over the past 12 years, and with Melbourne's economic fundamentals robust, there is no reason to believe demand for retail in Melbourne's heartland won't continue to be strong moving forwards. As evidence of this, rents for retail properties in the CBD have not declined in the last 12 months despite vacancy having risen.

Food and personal services retailing picks up the clothing slack

In saying this, there is no denying consumer tastes are changing, with a shift away from clothing retail towards food retail. ABS statistics tell us as a percentage of overall retail turnover, clothing/footwear/personal accessory retail turnover in Victoria has in recent years been in decline, while food retail has been increasing. And these trends are mirrored in the Knight Frank survey

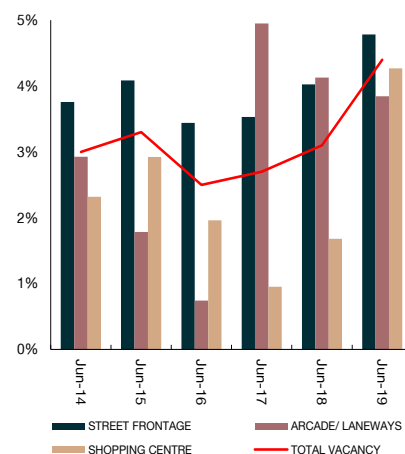
results—as a percentage of CBD retail, clothing/footwear/soft goods has declined (27.3% was 30.3% this time last year), while food retail has gone up (33.4% was 31.4%).

Tied to discretionary spending, clothes retailing is more likely to be affected by slow wage growth, and as a consequence is more likely to see a shift to online where prices tend to be cheaper (see the recent David Jones FRENZY sale that made news headlines). In contrast, those retailers who have an inherent need for physical bricks and mortar space, such as food and services retail, are more likely to thrive in today's retail landscape. Similar to food, in the Knight Frank survey, services retail as a percentage of all retail, has gone up (9.6% was 8.6%).

Elizabeth Street 'north' ushers in new Chinatown

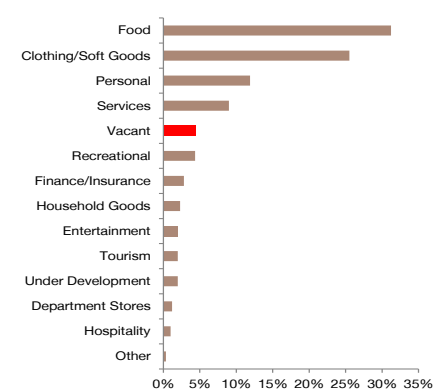
The ubiquity of food retailing is particularly noticeable along Elizabeth Street, especially along the northern end of the street where there has been a recent explosion of retailers satisfying the demands of the Asian market. Effectively the CBD's new 'Chinatown', this flourishing new retail pocket is a prime example of how the retail market has adjusted to meet the new tastes of Millennial and Generation Z consumers.

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



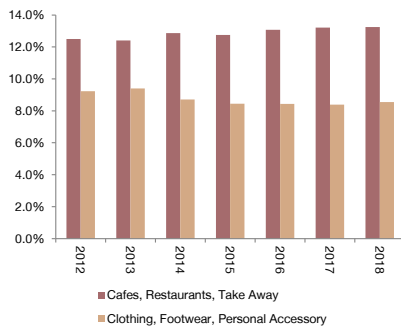
Source: Knight Frank Research

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



Source: Knight Frank Research

FIGURE 3
Food vs Clothes Retailing
% of total retail turnover (Vic)



Source: ABS

Driven by its close proximity to RMIT and several small private colleges, and populated with a number of new apartment buildings housing international students, the area north along Elizabeth between La Trobe Street and Therry Street is dotted with as many as 50 retail stores predominantly providing Asian food and beverage retail, personal services (beauty, electronics, travel) and Asian supermarkets/convenience stores. Demand along the north end of Elizabeth Street is so strong that vacancy is virtually non-existent (0.05%).

Delivery services fuel food retail growth

The recent prominence of food delivery services such as Uber Eats, Easi and Deliveroo is assisting the myriad small food retail businesses that have set up shop in the CBD in recent years. Largely driven by online booking systems, many food retailers in the CBD are choosing to take up small floor spaces in order to focus on delivery food in lieu of offering a dine in service.

Food retailers get resourceful with niche offerings

Indeed food retailers in the CBD are getting more and more resourceful, with some businesses focussed on very select offerings, again within small floor plates. On Swanston Street Hot Star Fried Chicken and Gong Cha share a single small retail space, and at Melbourne Central Chatime and Hudson Coffee share an island space between the food court and the train station entrance.

K-Culture continues to thrive at Melbourne Central

The popularity of Korean popular culture over the last few years has resulted in a number of Korean clothing brands setting up shop in the basement at Melbourne Central, and this trend has continued in the last 12 months with fashion label St Station opening in the basement and cosmetics behemoth Innisfree launching on Level 1.

Rents remain stable

Rental rates across the Melbourne CBD retail core have remained stable over the past 12 months, however incentives have increased marginally – whereas in 2017-18 many landlords would offer 2-3 months of incentives, in 2018-19 incentives are being offered for up to 4-5 months.

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 up

Retail investment sales volumes at June 2019 increased by 146% from the prior 12 months. Sales in excess of \$1M totalled \$248.1M from 25 properties in the 12 month period. Sales volume is on par with the longer term average of \$245.1M, and back to the levels seen in 2017.

One in every three sales were made by private investors, the largest of which was a well-located IGA supermarket at 620 Collins Street which sold for \$21.5M. Located at the bottom of Liberty Tower at the corner of Collins Street and Spencer Street and facing Southern Cross Station, the property at 620 Collins Street sold at a passing yield of 4.13%.

Prime yields for freehold street frontage retail assets sit within a range of 3.00% to 4.00% and for strata retail assets sit between 3.50% and 4.50%. Yields are expected to remain stagnant in the immediate short term.

TABLE 2
Recent Sales Activity Melbourne CBD Retail

Address	Price (\$ m)	Initial Passing Yield (%)	GLAR (sq m)	\$/sq m of GLAR	Date
187 King St	4.89	3.32	275	17,745	Jun-18
349 Elizabeth St	6.81	2.67	237	28,734	Aug-18
189-191 Bourke St	13.00	2.64	576	65,657	Oct-18
398 Elizabeth St	7.90	5.33	303	29,373	Oct-18
620 Collins St	21.55	4.13	639	33,725	Nov-18

Source: Knight Frank Research/RCA

TABLE 3
Recent Leasing Activity Melbourne CBD Retail

Address	Tenant	Net Rent \$/sq m	GLAR (sq m)	Term (yr)	Date
268 Flinders Lane	Tiffany Treloar	1,275	149	3	Jul-18
181 Collins St	Olga de Polga	2,432	37	4	Nov-18
220 Collins St	Koko Black	6,153*	65	5	Mar-19
200 Bourke St	Happy Lemon	5,800*	19	5	Jun-19
234 Collins St	KUNA Alpaca	3,800	113	5	Jun-19

* Gross rent
Source: Knight Frank Research

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 boundaries of La Trobe Street to the North, Flinders Street to the South, Spring Street to the East and Elizabeth Street to the West. In 2019 the core was expanded north along Elizabeth Street between La Trobe Street and Therry Street to reflect the emergence of a new retail precinct.

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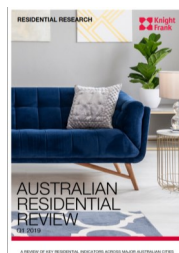
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