

EMBARGOED UNTIL 11.30 AM WEDNESDAY 18 APRIL 2018

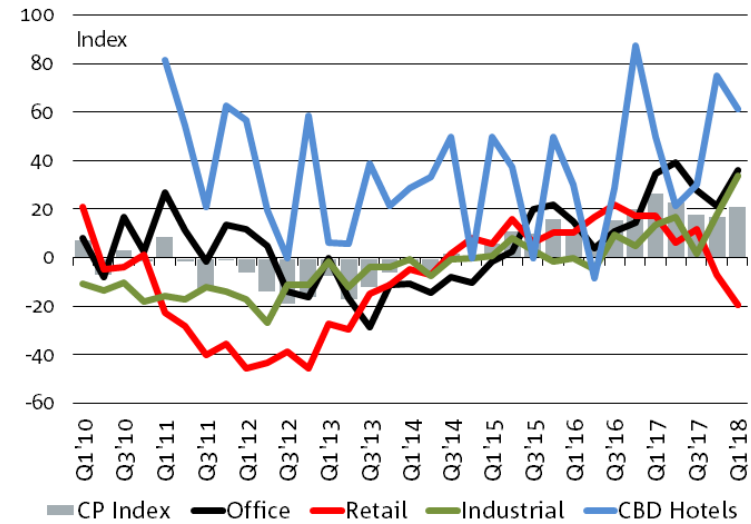


# NAB COMMERCIAL PROPERTY SURVEY Q1 2018

# KEY FINDINGS

- The **NAB Commercial Property Index** rose 4 points to +21 in Q1 and sits comfortably above its long-run average (+3).
- **By segment**, CBD Hotels still out-performing, aided by international tourism and global economic conditions. Industrial up again supported by transport & logistics firms and warehousing, fulfilment & distribution centres. Office also bounced back with healthy demand in key eastern states, strong business conditions and employment growth. Retail fell deeper negative as challenging retail trade conditions continued to bite.
- **Confidence** lifted in Industrial and Office. Retail down heavily and negative for the first time since mid-2013 - not surprising with NAB's Business Surveys also showing an under-performing retail sector and our own forecasts for subdued household spending in 2018 and 2019. Confidence was a little lower in CBD Hotels, but still highest overall.
- **By state**, big gains in WA (but negative). NSW and SA/NT also higher. Sentiment lower in QLD and unchanged in VIC. All states more confident about the market in next 1-2 years (bar QLD), with NSW and VIC most upbeat and WA least confident (but biggest improver).
- Expectations for **capital growth** in Office markets in next 1-2 years higher in all states bar QLD. Industrial also stronger. Retail scaled back with negative or slow growth in all states. Expectations still strongest for CBD Hotel property.
- Overall Office **vacancy** rose to 9.0% in Q1 with a small rise in NSW. But NSW along with VIC still the tightest markets for Office space (and set to remain so over outlook period). Office vacancy fell in WA, SA/NT and QLD and expected to keep tightening in next 1-2 years (but remain relatively high) with over-supply an issue in these states.
- Industrial (1.9% & 2.3%) & Office (1.8% & 2.3%) **rents** to grow fastest in next 1-2 years, with VIC & NSW out-performing. Experts see rents recovering in WA, especially Office. Retail outlook weak (-1.4% & -1.2%), with negative growth in all states bar NSW (flat).
- **Special Question** - Retail property experts assess strategy acquisitions of A-REIT and 'Other' investors for next 12 months. Most (over 1 in 2) think they will focus on acquisitions and holding assets. But 1 in 5 say 'Other' investors will divest (just 1 in 10 think A-REIT will). Strategies will be driven by concerns over economy, opportunities to buy traditionally tightly held assets, online retail and entry of new players, all time high cap rates and changing spending patterns. Most also think changes will impact landlords negatively, especially large neighbourhood, sub-regional and regional areas (*see page 7*).
- Fewer property **developers** looking to use land-banked stock for new projects and increasing numbers seeking new acquisitions, pointing to a period of stock rebuild. A higher than usual number of developers also seeking refurbishments, suggesting more developers are seeing this as a cost effective solution for their development needs.
- **Accessing funds** (both debt and equity) needed for their property business still a major challenge but less so than in Q4. But survey participants expect their debt funding and equity conditions to worsen again over the next 6-12 months.

## NAB COMMERCIAL PROPERTY INDEX



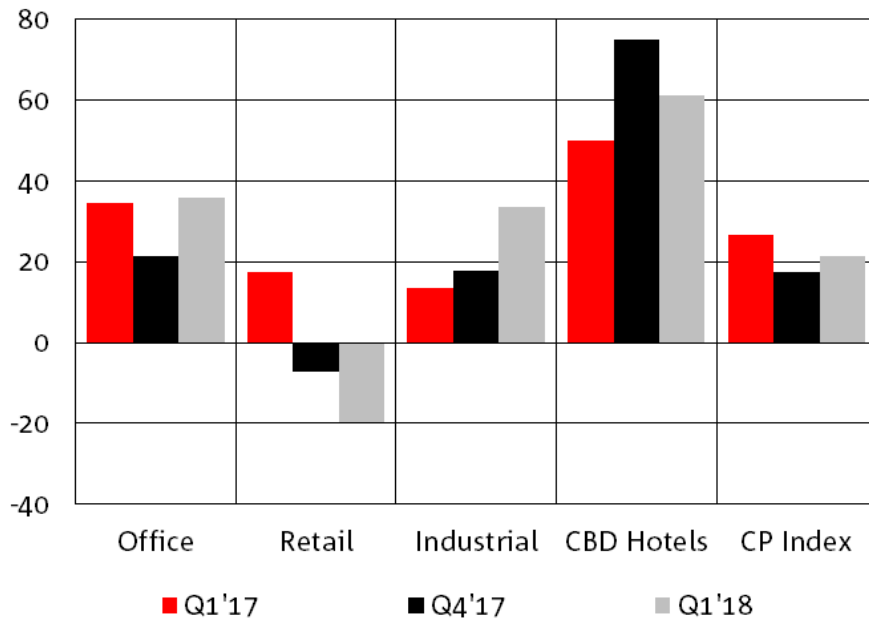
	Q3 2017	Q4 2017	Q1 2018	Next 12m	Next 2yrs
Office	28	21	36	42	44
Retail	12	-7	-20	-8	-10
Industrial	2	18	34	50	50
CBD Hotels	30	75	61	72	78
CP Index	18	17	21	32	33

# MARKET OVERVIEW - NAB COMMERCIAL PROPERTY INDEX

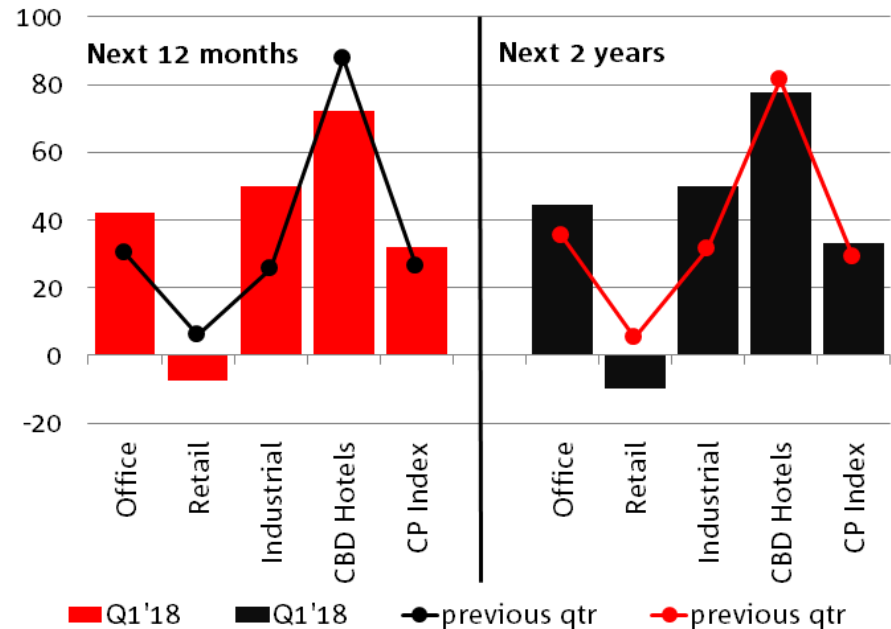
Overall sentiment (measured by NAB's Commercial Property Index) rose 4 points to +21 in Q1. It has however fallen compared to Q1 2017 (+27) but remains above its long-term average (+3). CBD Hotels eased 14 points to a still healthy +61, and continues to out-perform all other property classes supported by growth in international tourism and favourable global economic conditions. Industrial property rose for the third straight quarter (up 16 points to a new survey high +34) and is benefitting from the requirements of transport and logistics firms and growth of warehousing, fulfilment and distribution centres. Office also bounced back (up 15 to +36), amid healthy demand in key eastern states, strong business conditions and white collar employment growth. But Retail market sentiment sank deeper into negative territory (down 13 points to a 4½ year low -20) as challenging retail trade conditions impacted the outlook for capital and rental growth for Retail property.

Overall confidence lifted in Q1 - with NAB's Commercial Property Index expected to rise to +32 in the next 12 months (+28 in Q4) and +33 in 2 years' time (+30 in Q4). Confidence has lifted sharply in the Industrial space. We suspect a number of factors are supporting this optimism, including new entrants to the e-commerce sector, automation and population growth (particularly on the eastern seaboard). Confidence in Office markets also picked up amid continued strong demand for office space in Sydney and Melbourne. In contrast, Retail market confidence fell heavily and was negative for the first time since mid-2013. This result is not surprising with recent NAB's Business Surveys also continuing to highlight an under-performing retail sector, and our own forecasts for subdued household spending in 2018 and 2019. Confidence also slipped a little in the CBD Hotels sector, but is still the highest among all property sectors.

## NAB COMMERCIAL PROPERTY INDEX



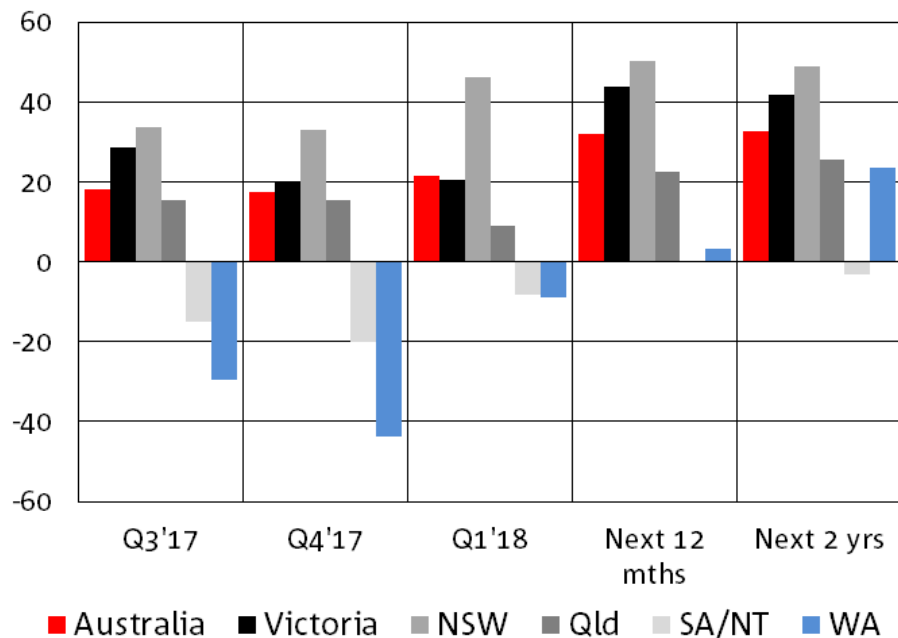
## NAB CP INDEX - NEXT 1-2 YEARS



# MARKET OVERVIEW - INDEX BY STATE

Higher sentiment nationwide reflected gains in WA (up 35 to -9), NSW (up 13 to +46) and SA/NT (up 12 to -8). QLD was down 6 to +9 and VIC unchanged (+20). Office sentiment improved in all states, led by NSW (+73). WA (-7) was negative but continued to taper. Retail sentiment was negative in all states, led by SA/NT (-50) and VIC (-27). Industrial sentiment was highest in the Eastern seaboard states, despite some easing in VIC (+35) and QLD (+22) to still relatively high levels. Property experts in all states are more confident about the overall commercial property market in the next 1-2 years, except in QLD because of lower confidence around Office and Retail. NSW and VIC are the most upbeat states and WA the least confident (but the biggest improver). Of note, property experts in all states are more confident around Industrial property except in SA/NT (unchanged).

## COMMERCIAL PROPERTY INDEX - STATE



## OFFICE PROPERTY MARKET INDEX - STATES

	VIC	NSW	QLD	WA	SA/NT	AUS
Q4'17	29↑	73↑	20↑	-7↑	0↑	36↑
Q4'18	57↑	73↑	20↓	14↑	17↑	42↑
Q4'19	57↑	67↑	24↓	50↑	8↑	44↑

## RETAIL PROPERTY MARKET INDEX - STATES

	VIC	NSW	QLD	WA	SA/NT	AUS
Q3'17	-27↓	-5↑	-12↓	-20↑	-50↓	-20↓
Q3'18	0↑	5↑	0↓	-30↓	-50↓	-8↓
Q3'19	-4↑	10↑	-15↓	-10↑	-50↓	-10↓

## INDUSTRIAL PROPERTY MARKET INDEX - STATES

	VIC	NSW	QLD	WA	SA/NT	AUS
Q3'17	35↓	61↑	22↓	0↑	0↔	34↑
Q3'18	55↑	66↑	47↑	33↑	0↔	50↑
Q3'19	50↑	63↑	53↑	33↑	0↔	50↑

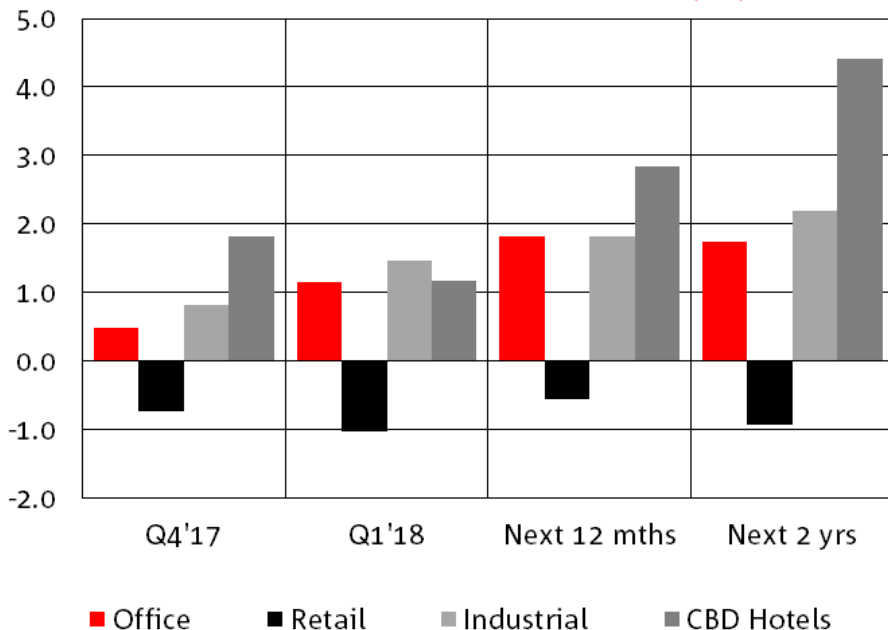
LEGEND: ↑ up since last survey ↓ down since last survey ↔ unchanged

# MARKET OVERVIEW - CAPITAL & VACANCY EXPECTATIONS

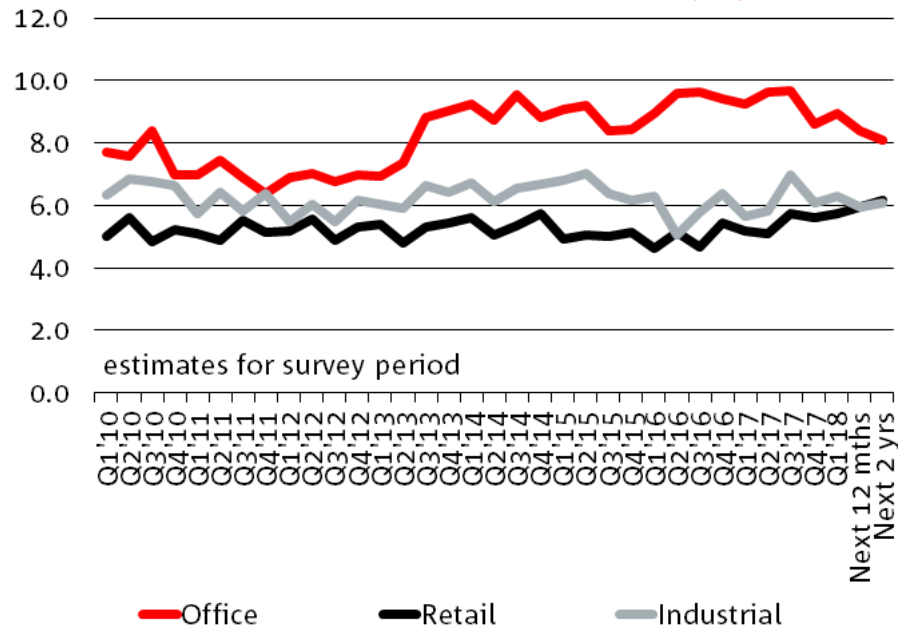
On average, property experts have raised their expectations for capital growth in Office markets over the next 1-2 years (1.8% & 1.7%). Expectations were higher in all states except QLD (unchanged for the next year but lower in 2 years' time). NSW (3.3% & 3.1%) and VIC (2.4% & 2.9%) are expected to provide the highest returns and SA/NT (0.6% in both years) and WA (-0.4% & 0.8%) the lowest. Capital growth expectations for industrial property also improved (1.8% & 2.2%), with returns expected to be highest in NSW (3.4% & 3.6%) and lowest in SA/NT (-0.5% in both years). In the Retail segment however, expectations were cut further (-0.6% & -0.9%) with negative or very slow growth predicted in all states. Capital growth expectations remain strongest for CBD Hotel property (2.8% & 4.4%).

The national Office vacancy rate rose slightly to 9.0% in Q1 (8.6% in Q4). This was due to a small rise in NSW to 5.6%. However, it remains along with VIC (4.6%) the tightest market for Office space, with both markets also expected to remain very tight over the outlook period. Encouragingly, office vacancy fell in WA (13%), SA/NT (12.3%) and QLD (10.6%), and is expected to continue tightening in the next 1-2 years (but still relatively high). The overall vacancy rate in the Retail property market rose slightly to 5.7% in Q1 (5.6% in Q4), but ranged from 5.3% in NSW to 7.8% in SA/NT. In the Industrial sector, overall vacancy also rose slightly to 6.3% (6.1% in Q4). By state, vacancy was lowest in VIC (4.5%) and NSW (4.7%) and highest in WA (10.2%) and QLD (7.8%).

## CAPITAL VALUE EXPECTATIONS (%)



## VACANCY RATE EXPECTATIONS (%)

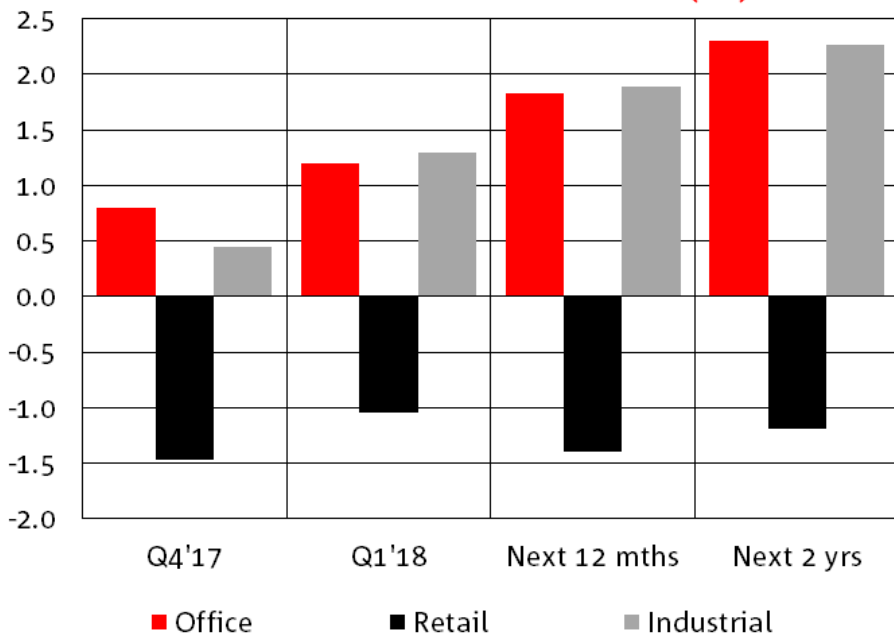


# MARKET OVERVIEW - RENTS & SUPPLY

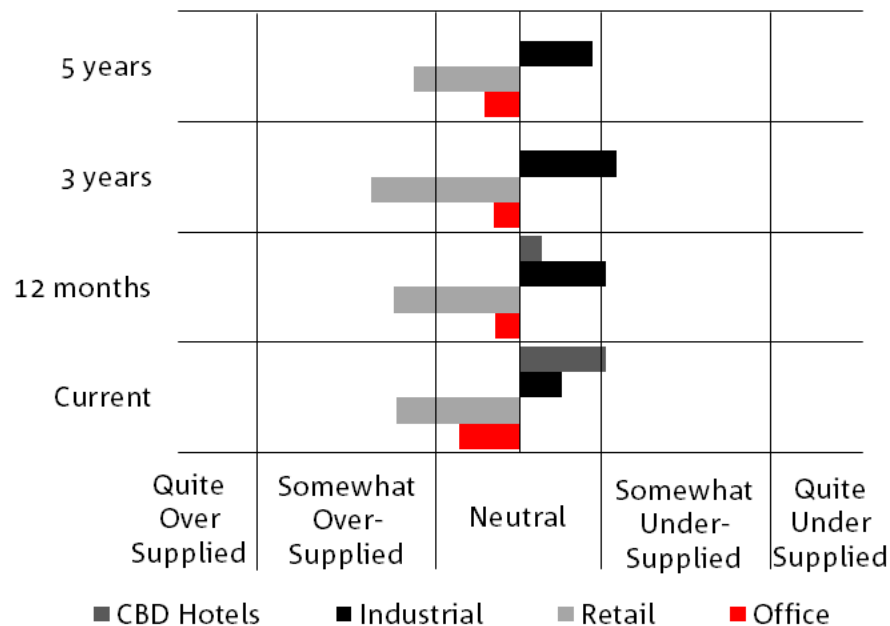
Industrial property (1.3%) overtook Office (1.2%) for the fastest rental growth in Q1, led mainly by stronger returns in NSW (3.1%) and VIC (1.4%). Office rents were also largely supported by higher returns in VIC (3.7%) and NSW (2.7%) as elevated vacancy rates continued to limit rental growth in other states. Rental growth for Retail property fell a further -1.0% in Q1, with negative returns reported in all states. Looking ahead, property experts think Industrial (1.9% & 2.3%) and Office (1.8% & 2.3%) rents will grow fastest in the next 1-2 years, with VIC and NSW out-performing in both sectors. There were also encouraging signs of a rental recovery in WA, particularly in Office markets. In contrast, the outlook for Retail rents remains very challenging (-1.4% & -1.2%), with negative returns forecasts in all states except NSW (flat).

Property experts believe Retail markets are currently “somewhat” over-supplied and will remain so in the next 1-5 years. Over-supply is expected to persist in NSW and VIC, with all other markets “neutral”. Office markets overall were assessed as “neutral” and also tipped to remain so over the outlook horizon. But big differences remain evident across states. Over-supply is still a major issue in WA and to a lesser SA/NT and QLD, but NSW is “somewhat” under-supplied (and will remain so in the next 1-3 years) and VIC “neutral” through the outlook period. Industrial markets overall are also balanced, but shortages in NSW and VIC are being offset by over-supply in WA and SA/NT. CBD Hotels market are “somewhat” over-supplied now but will balance in 1-5 years as new supply comes on stream.

## GROSS RENTAL EXPECTATIONS (%)

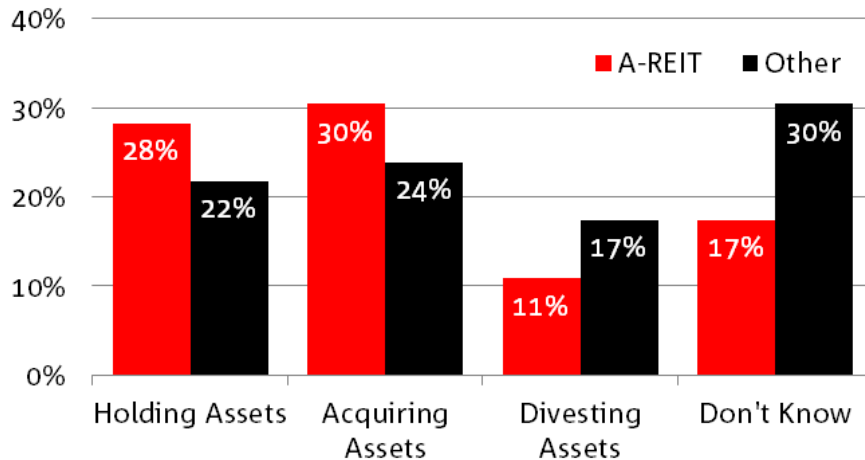


## SUPPLY CONDITIONS

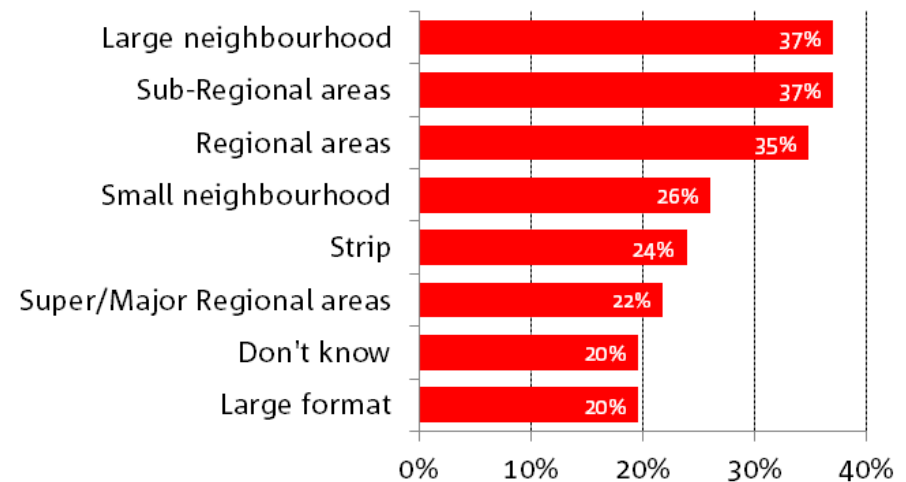


# SPECIAL QUESTION - RETAIL ACQUISITION STRATEGIES

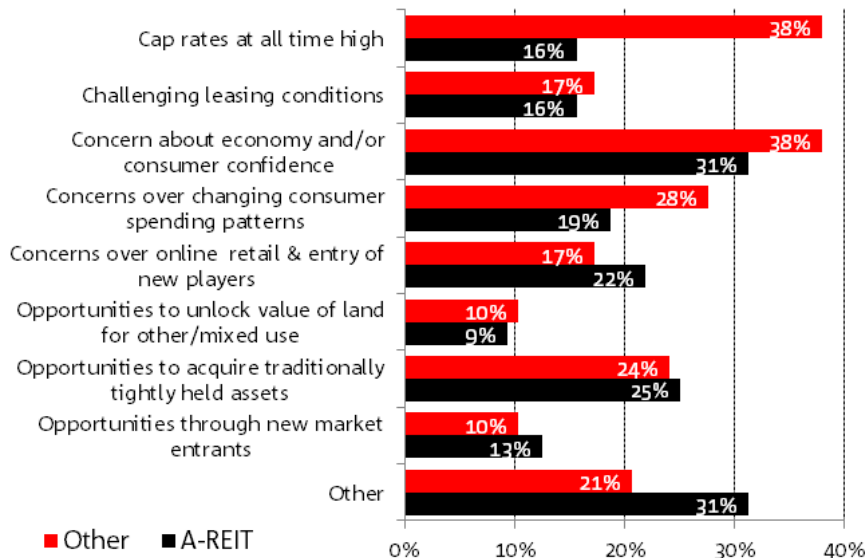
## ACQUISITION STRATEGIES



## ACQUISITION STRATEGIES - IMPACT BY MARKET



## FACTORS DRIVING ACQUISITION STRATEGIES



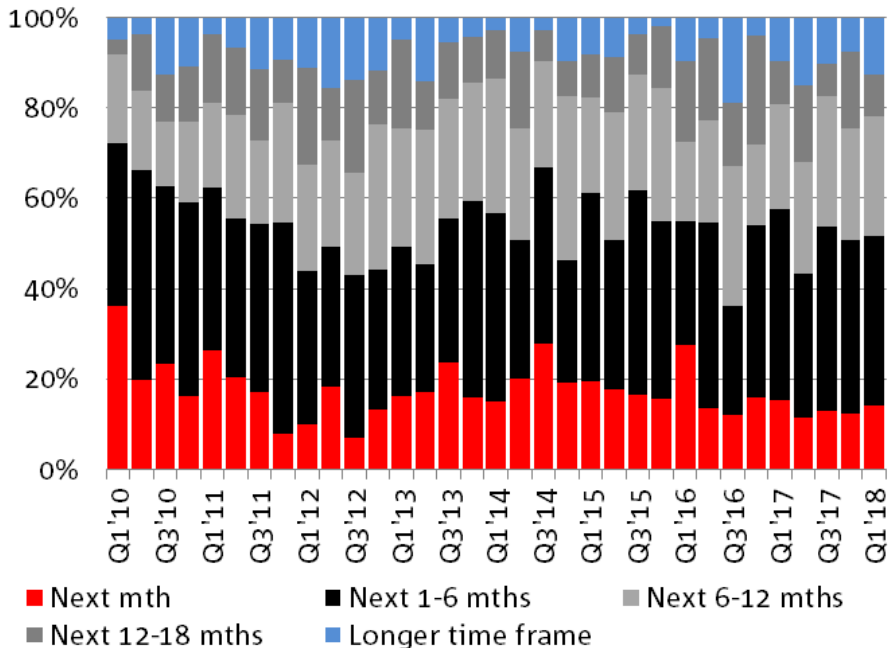
Retail property experts were asked to describe the Retail strategy acquisitions of A-REIT and 'Other' investors in the next 12 months. Around 30% believe A-REIT strategy will be driven by acquisition (24% for 'Other' investors), and 28% said A-REIT will focus on holding assets (22% for 'Other' investors). But 17% of 'Other' investors are expected to divest their assets (just 11% for A-REIT). Most property experts believe A-REIT strategy is being driven by concerns over the economy (31%), opportunities to buy traditionally tightly held assets (25%) and concerns over online retail and entry of new players like Amazon (22%). 'Other' investors were being influenced by all time high cap rates (38%), concerns over the economy (38%) and changing consumer spending patterns (28%). It was also apparent that a lot more property experts (~36% in net balance terms) expected these changes to impact landlords negatively. Moreover, the biggest impact of these changes are expected to be felt by large neighbourhood retail (37%), sub-regional (37%) and regional areas (35%). Large format (20%) and super/major regional areas (22%) are expected to be least affected.

# MARKET OVERVIEW - DEVELOPMENT INTENTIONS

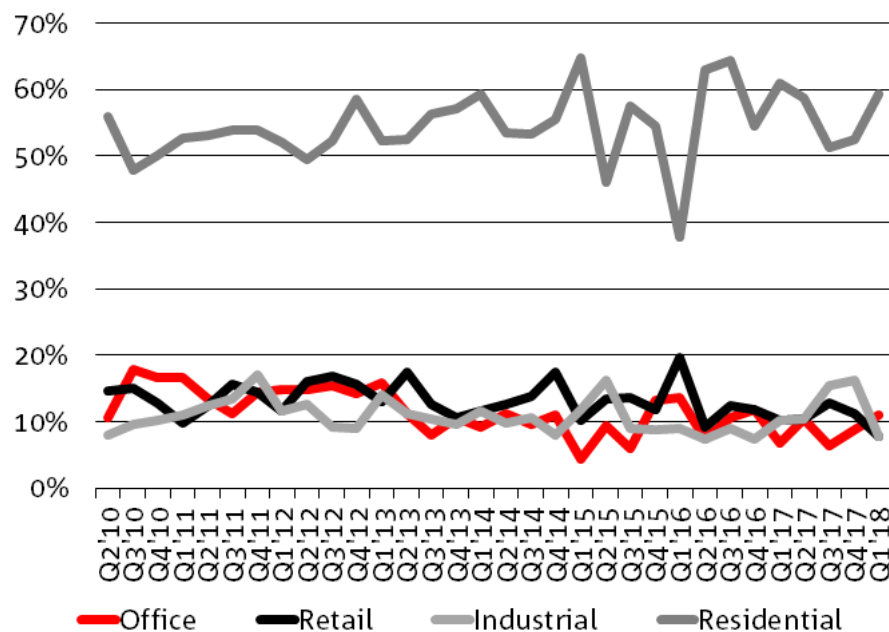
Despite a small improvement in Q1, fewer property developers plan to enter the market in the near future than historically. Australia wide, the number of surveyed property developers who said they were intending to commence new building works in the next 6 months rose to 49% (47% in Q4) - but remains below long-term average levels (51%). Around 1 in 4 (25%) plan to start new projects in the next 6-12 months (23% in Q4). However, just over 1 in 5 (21%) said they planned to start in the next 12 months or beyond - 9% said they would start in the next 12-18 months (16% in Q4) and 12% had a longer-time frame (7% in Q4).

The number of property developers planning to start new works and targeting residential development projects increased to 59% in Q1 (53% in Q4). This is now back above long-term average levels (55%), but still down from Survey high levels of around 64% in the second half of 2016. In commercial property markets, around 11% of developers said they were looking to start new works in the Office space (9% in Q4). In other sectors, around 8% were looking to start work on Industrial projects (16% in Q4) and 8% on Retail projects (11% in Q3).

## COMMENCEMENT INTENTIONS - TIME



## COMMENCEMENT INTENTIONS - SECTOR



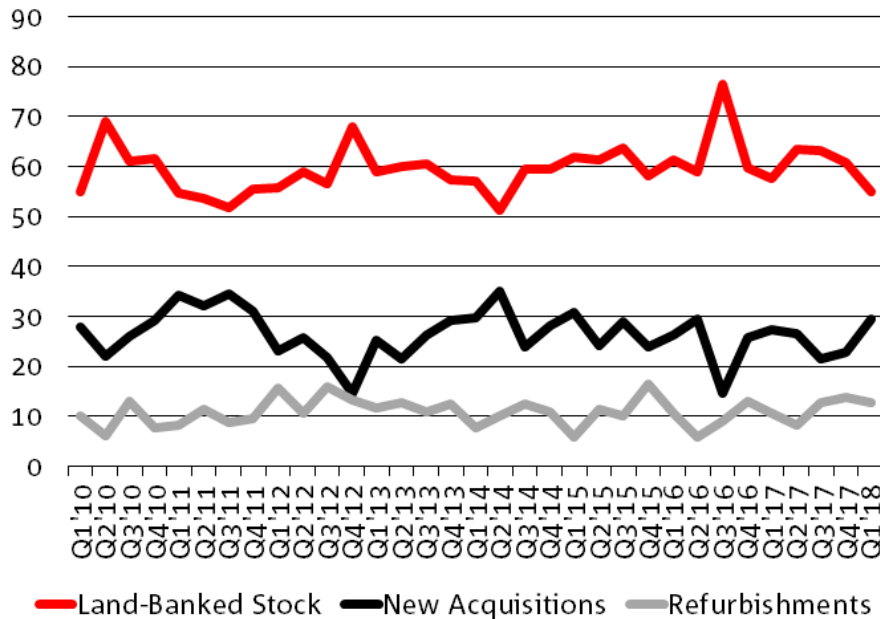


# MARKET OVERVIEW - LAND SOURCES & CAPITAL INTENTIONS

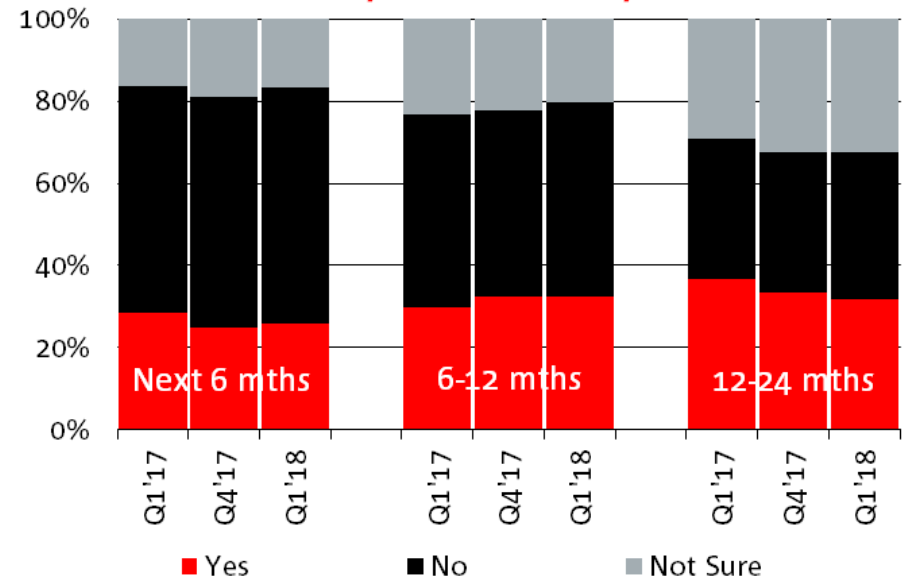
We have seen a noticeable drop in the number of property developers looking to use land-banked stock for their new projects in recent surveys. It fell to just 55% in Q1, down from 61% in Q4 and below long-term average levels (60%). At the same time, the number seeking new acquisitions rose to a 3 year high 30%. This has likely occurred because some developers have exhausted or drawn down their land stocks in this construction cycle and are looking to rebuild them. The number of developers looking at refurbishments was broadly unchanged at 13% (14% in Q4), but above long-term average levels (11%) perhaps suggesting more developers are also looking to refurbished property as a cost effective solution for their development intentions.

The number of property developers that were planning to source more capital to fund their developments in the next 6 months rose slightly to 26% in Q1 (25% in Q4). Around 57% had no intention to source capital in the short-term (unchanged) and 17% were unsure (18% in Q4). Medium-term sourcing intentions in the next 6-12 months were also broadly unchanged - 33% yes, 47% no and 20% unsure. Developers also continued to be evenly split about their longer-term intentions - 32% yes, 36% no and 33% unsure.

## SOURCES OF LAND DEVELOPMENT (%)



## INTENT TO SOURCE MORE CAPITAL FOR DEVELOPMENT/ACQUISITIONS/PROJECTS

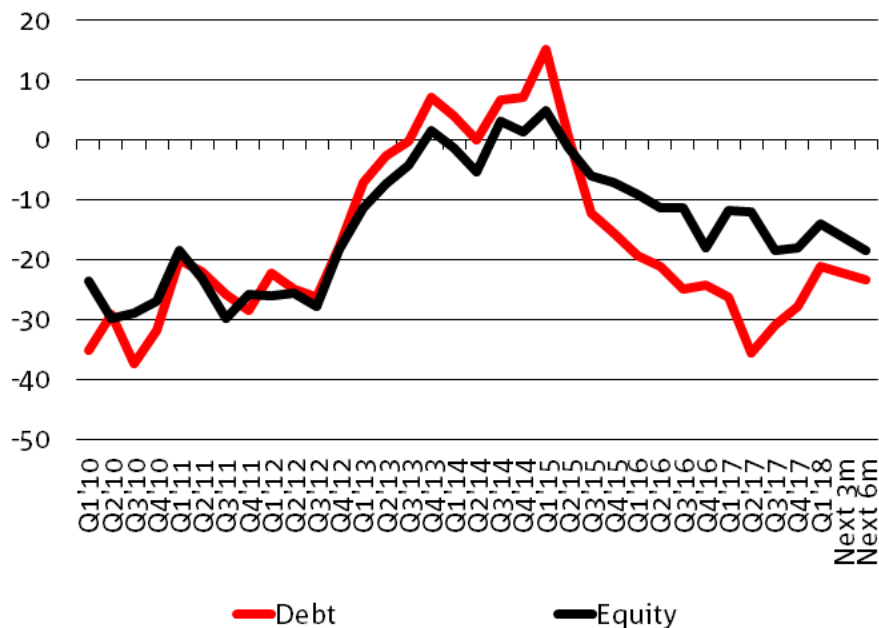


# MARKET OVERVIEW - FUNDING & PRE-COMMITMENTS

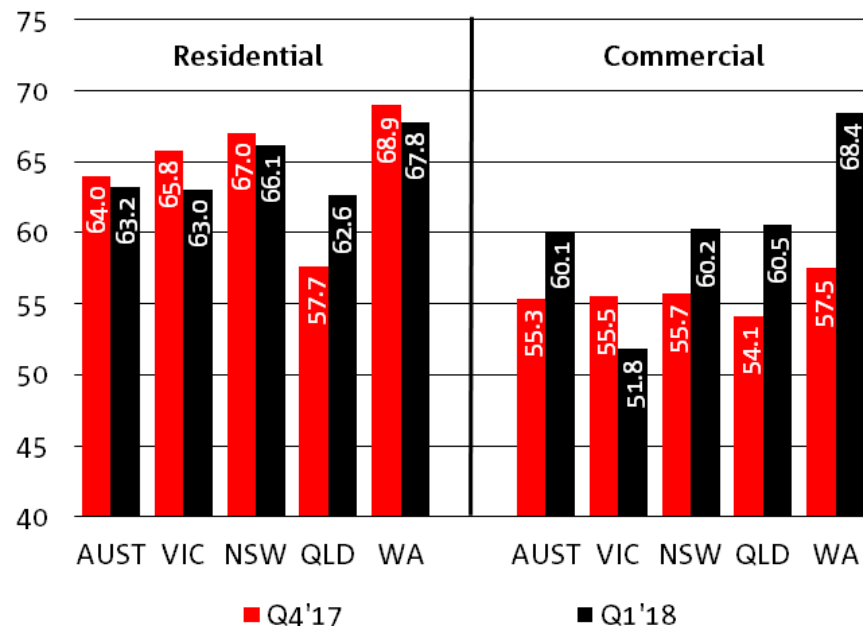
Accessing funds continues to be a major challenge, but has improved in recent surveys. In net balance terms, -21% of surveyed property experts said it was harder to obtain borrowing or loans (debt) needed for their business - an improvement from -28% in Q4. Equity funding conditions were also negative but a little easier according to a net -14% (-18% in Q4). Looking forward, however, more property experts on balance expect their funding conditions to worsen over the next 6-12 months - a net -23% see debt funding conditions worsening over the next 6-12 months while -19% think it will be harder to obtain equity financing.

Australia wide, the average pre-commitment required to meet external debt funding requirements for new developments was broadly unchanged at 63.2% for residential property (64.0% in Q4), but rose to 60.1% for commercial property (55.3% in Q4). Residential requirements fell in VIC (63.0%), NSW (66.1%) and WA (67.8%), but increased in QLD (62.6%). For commercial property, average pre-commitments rose in NSW (60.2%), QLD (60.5%) and WA (68.4%), and fell in VIC (51.8%). More property experts think their lending terms will worsen in the next 6-12 - although the number has fallen to a net -15% for residential property in 6 months (-20% in Q4) and -8% in 12 months (-20% in Q3) and to -14% in 6 months (-22% in Q4) and -9% in 12 months (-23% in Q4) for commercial property.

## EASE OF ACQUIRING DEBT/EQUITY (NET)



## PRE-COMMITMENT REQUIREMENTS (%)



# SURVEY RESPONDENTS EXPECTATIONS (AVG) Q1 2018

## OFFICE CAPITAL VALUES (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q1'18	0.4	2.8	0.3	-0.6	0.6	<b>1.2</b>
Q1'19	2.4	3.3	1.1	-0.4	0.6	<b>1.8</b>
Q1'20	2.9	3.1	0.7	0.8	0.6	<b>1.7</b>

## OFFICE RENTS (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q1'18	3.7	2.7	0.2	-0.9	-0.6	<b>1.2</b>
Q1'19	3.9	3.7	0.5	-0.1	-0.3	<b>1.8</b>
Q1'20	4.8	3.5	1.3	1.4	0.0	<b>2.3</b>

## RETAIL CAPITAL VALUES (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q1'18	-0.9	-1.6	-0.4	0.2	-2.9	<b>-0.7</b>
Q1'19	0.0	-1.4	0.4	-0.2	-2.9	<b>-0.6</b>
Q1'20	-1.0	-1.2	-0.6	0.2	-2.0	<b>-0.9</b>

## RETAIL RENTS (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q1'18	-0.6	-0.1	-1.0	-2.3	-2.9	<b>-1.0</b>
Q1'19	-1.0	0.0	-1.3	-2.3	-4.4	<b>-1.4</b>
Q1'20	-1.0	0.0	-1.6	-1.5	-2.5	<b>-1.2</b>

## INDUSTRIAL CAPITAL VALUES (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q1'18	0.4	3.6	0.6	0.0	0.5	<b>1.5</b>
Q1'19	1.0	3.4	1.7	0.9	3.8	<b>1.8</b>
Q1'20	1.3	3.6	2.7	0.6	-0.5	<b>2.2</b>

## INDUSTRIAL RENTS (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q1'18	1.4	3.1	0.4	0.0	-0.5	<b>1.3</b>
Q1'19	2.3	3.1	1.4	0.9	-0.5	<b>1.9</b>
Q1'20	2.4	3.5	2.1	1.2	-0.5	<b>2.3</b>

# SURVEY RESPONDENTS EXPECTATIONS (AVG) Q1 2018

## OFFICE VACANCY RATE (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q1'18	4.6	5.6	11.3	13.0	12.7	9.0
Q1'19	4.2	4.1	10.6	12.7	12.3	8.4
Q1'20	4.2	5.2	10.0	11.9	11.7	8.1

## RETAIL VACANCY RATE (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q1'18	5.4	5.3	5.5	5.8	7.8	5.7
Q1'19	5.7	5.5	5.2	6.2	8.6	6.0
Q1'20	6.1	5.5	5.9	5.0	9.0	6.2

## INDUSTRIAL VACANCY RATE (%)

	VIC	NSW	QLD	WA	SA/NT	AUS
Q1'18	4.5	4.7	7.8	10.2	6.0	6.3
Q1'19	4.4	4.7	6.7	9.4	6.5	6.0
Q1'20	4.3	5.8	6.2	8.6	6.5	6.1

## NOTES:

Survey participants are asked how they see:

- capital values;
- gross rents; and
- vacancy rates

In each of the commercial property markets for the following timeframes:

- current quarter
- next quarter
- next 12 months
- next 12-24 months

Average expectations for each state are presented in the accompanying tables.

*\*Results for SA/NT may be biased due to a smaller sample size.*

## ABOUT THE SURVEY

In April 2010, NAB launched the first NAB Quarterly Australian Commercial Property Survey with the aim of developing Australia's pre-eminent survey of market conditions in the commercial property market.

The large external panel of respondents consists of Real Estate Agents/Managers, Property Developers, Asset/Fund Managers and Owners/Investors.

Around 300 panellists participated in the Q1 2018 Survey.

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