EMBARGOED UNTIL 11.30 AM THURSDAY 2 MAY 2019

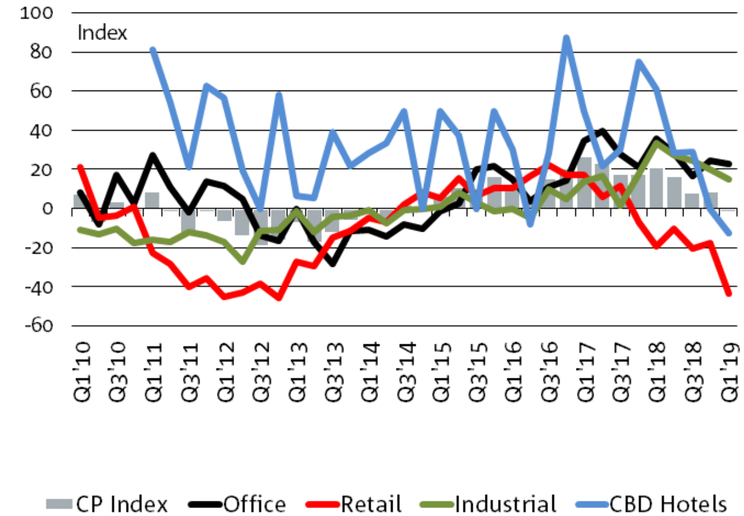
# NAB COMMERCIAL PROPERTY SURVEY Q1-2019

Date May 2019 | NAB Behavioural & Industry Economics

# KEY FINDINGS

- Overall market sentiment (measured by **NAB's Commercial Property Index**) fell 11 points to -2 in Q1 2019 - its first negative read in over 4 years.
- **Sentiment** led down by a sharp dip in Retail (negative in all states) and CBD Hotels (its first negative read since mid-2016). Office and Industrial sentiment also mildly softer, but still tracking well above long-term averages.
- **Confidence** dipped to new lows with outlook weaker in all sectors. Confidence weakest (and more negative) for Retail and CBD Hotels. It also fell below average for Office and Industrial (but still tipped to out-perform by a large margin).
- By **state**, sentiment moderated in VIC, NSW and QLD. It rose in SA/NT and was steady in WA (but both negative). Confidence in next 12 months also lower in VIC and NSW (and in all sectors). QLD steady with improved outlook for Office offsetting weaker Industrial and Retail. WA also lower with Retail very weak. QLD, WA and VIC most confident in next 2 years. NSW negative (first time), led by weak Retail outlook.
- **Capital growth** expectations for next year strongest for Office (1.1%), led by QLD (1.6%). Industrial values expected to grow (0.8%), led by SA/NT (3.8%). Outlook for Retail very weak (-2.3%), with values tipped to fall in all states. Industrial values expected to grow fastest in 2 years' time (1.3%), ahead of Office (1.2%). QLD (2.3%) and VIC (1.9%) the best states for Industrial property, and WA (2.4%) and QLD (2.3%) for Office. Retail values set to fall -2.5%, led by NSW (-2.7%).
- National office **vacancy** rose to 7.9% in Q1 (7.8% in Q4). It fell in NSW (4.7%) and QLD (10.1%), but rose in VIC (4.5%), SA/NT (12.6%) and WA (15.0%). Vacancy expected to remain steady at 8% over next 1-2 years, with rising vacancy in NSW and VIC (to still very low levels) offset by modest tightening in QLD, SA/NT and WA.
- Office **rents** tipped to grow fastest (1.1% & 1.6%) over next 1-2 years, led by VIC (2.1%) next year and QLD (3.2%) in 2 years' time. Industrial rents to grow (0.9% & 1.4%), with VIC (1.3% & 2.4%) providing highest returns. Retail rents negative (-2.7% & -2.9%) and expected to fall in all states, led by WA (-6.5% & -5.6%).
- The number of **developers** expecting to start new works over next 6 months fell to 41% in Q1 2019 (well below Survey average). The number of developers targeting residential projects also remains below average - reinforcing the view residential building activity has passed its peak.
- **Accessing credit** is still very difficult. In net terms, -40% of surveyed property professionals said it was harder to obtain debt in Q1 (second worst result on record) and a Survey low -32% to obtain equity. Property professionals also expect their funding conditions to worsen further in next 3-6 months.

## NAB COMMERCIAL PROPERTY INDEX




| | Q3 2018 | Q4 2018 | Q1 2019 | Next 12m | Next 2yrs |
|---|---|---|---|---|---|
| Office | 16 | 25 | 23 | 30 | 37 |
| Retail | -20 | -18 | -44 | -54 | -45 |
| Industrial | 25 | 20 | 15 | 27 | 36 |
| CBD Hotels | 29 | 0 | -13 | -38 | -31 |
| **CP Index** | **8** | **9** | **-2** | **-2** | **5** |

# MARKET OVERVIEW - NAB COMMERCIAL PROPERTY INDEX

Overall sentiment (measured by NAB's Commercial Property Index) fell 11 points to -2 in Q1 2019 - its first negative read in over 4 years. The Index has also fallen below long-term average levels (+3).

Weaker sentiment mainly reflected a sharp dip in Retail property (down 26 to -44), with sentiment deeply negative in all states. Sentiment in this sector is likely being influenced by the slowing in growth momentum into Q1 2019, with the situation in discretionary retail and consumption more generally deteriorating even further.

Sentiment in the CBD Hotels sector also fell quite sharply (down 13 to -13), posting its first negative read since mid-2016.

Sentiment in Office (down 2 to +23) and Industrial (down 5 to +15) markets also softened a little, but continued to out-perform the broader market with sentiment in both sectors still tracking well above their long-term averages.

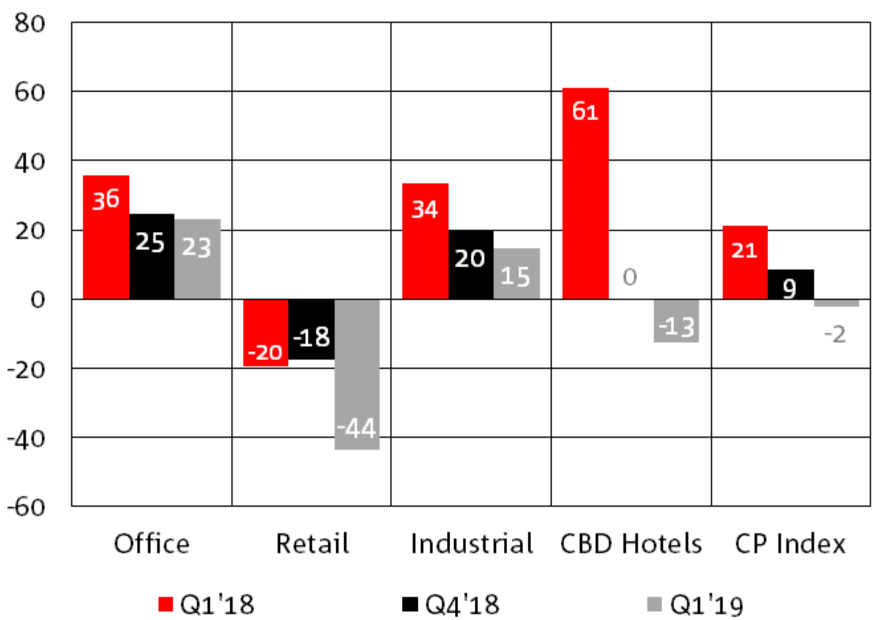
Overall confidence levels in commercial property markets fell to new Survey lows of +1 in the next 12 months (+16 in Q4) and +8 in 2 years' time (+20 in Q4), with the outlook scaled back in all market sectors.

Confidence is still weakest for Retail property and it dipped even further into negative territory to -54 in 12 months' time (-21 in Q4) and -45 in 2 years' time (-18 in Q4).

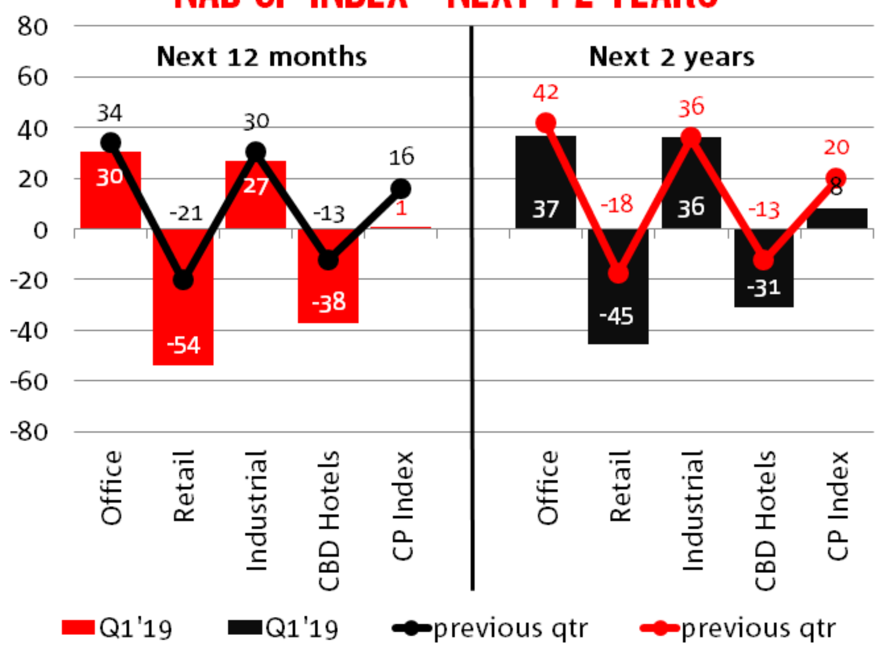
Confidence also slipped deeper into negative territory in the CBD Hotels sector on the back of negative expectations for both capital and revPar in the next 1-2 years.

Office and Industrial confidence held up better, but also fell little to below average levels. Both sectors are however still expected to be the best performing asset classes in the next 1-2 years by a considerable margin.

## NAB COMMERCIAL PROPERTY INDEX




## NAB CP INDEX - NEXT 1-2 YEARS



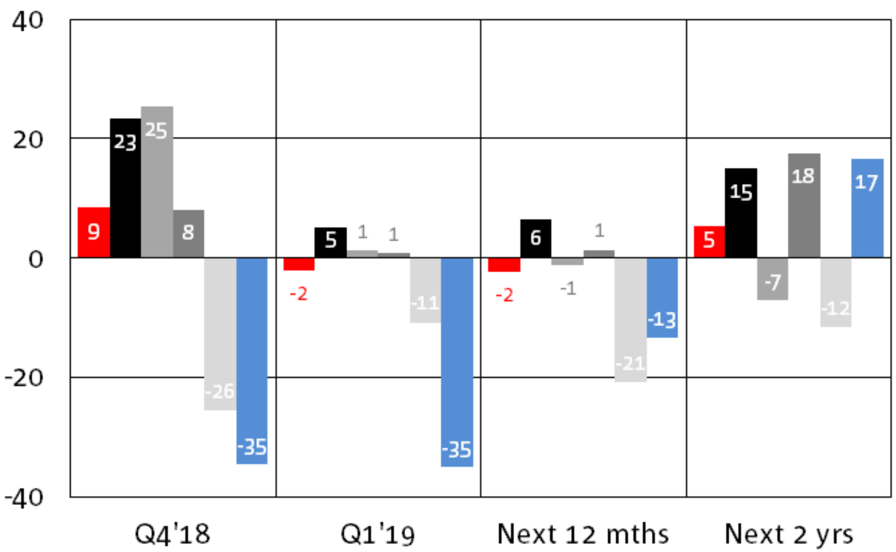
# MARKET OVERVIEW - INDEX BY STATE

Market sentiment in Q1 eased in VIC (down 18 to +5), NSW (down 24 to +1) and QLD (down 7 to +1). It rose in SA/NT (up 15 to -11) and was steady in WA (-35). VIC led the way for Office and Industrial property, with Retail sentiment negative in all states (see table on right).

Overall confidence levels for the next 12 months fell sharply in VIC (+6) and NSW (-1), and lower was in all sectors. QLD (+1) was broadly steady as an improved outlook for Office offset falls in Industrial and Retail. Overall confidence levels in WA fell further (-13), dragged down by a very weak Retail outlook.

QLD (+18), WA (+17) and VIC (+14) are the most optimistic states in 2 years' time. Long-term confidence in NSW (-7) turned negative for the first time, dragged down by mainly by a negative outlook for Retail, although confidence around Office and Industrial also softened.

## COMMERCIAL PROPERTY INDEX - STATE




## OFFICE PROPERTY MAKET INDEX – STATES

| | VIC | NSW | QLD | WA | SA/NT | AUS |
|---|---|---|---|---|---|---|
| Q1'19 | 35↓ | 30↓ | 29↑ | -8↑ | -8↑ | **23↓** |
| Q1'20 | 45↓ | 36↓ | 39↑ | 25↑ | -33↓ | **30↓** |
| Q4'21 | 50↓ | 28↓ | 64↑ | 42↓ | -17↓ | **37↓** |

## RETAIL PROPERTY MARKET INDEX – STATES

| | VIC | NSW | QLD | WA | SA/NT | AUS |
|---|---|---|---|---|---|---|
| Q1'19 | -45↓ | -29↓ | -50↓ | -100↓ | -33↑ | **-44↓** |
| Q1'20 | -58↓ | -32↓ | -67↓ | -100↓ | -33↑ | **-54↓** |
| Q4'21 | -45↓ | -43↓ | -50↓ | -50↓ | -33↑ | **-45↓** |

## INDUSTRIAL PROPERTY MARKET INDEX - STATES

| | VIC | NSW | QLD | WA | SA/NT | AUS |
|---|---|---|---|---|---|---|
| Q1'19 | 23↓ | 14↓ | 22↓ | -8↑ | 0↔ | **15↓** |
| Q1'20 | 41↓ | 20↓ | 28↓ | 33↑ | 0↑ | **27↓** |
| Q4'21 | 55↑ | 23↓ | 34↔ | 75↑ | 0↔ | **36↔** |

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

# MARKET OVERVIEW - CAPITAL & VACANCY EXPECTATIONS

On average, capital growth expectations in the next 12 months were lifted for Office (1.1% vs. 1.0% in Q4), with returns expected to be highest in QLD (1.6%) and lowest in SA/NT (flat). Industrial values are also expected to grow (0.8% vs. 0.9%), with SA/NT out-performing (3.8%) and WA under-performing (0.3%). Retail expectations were weaker (-2.3% vs. -1.1%), with capital values predicted to fall in all states. CBD Hotel values are tipped to fall -1.2%.

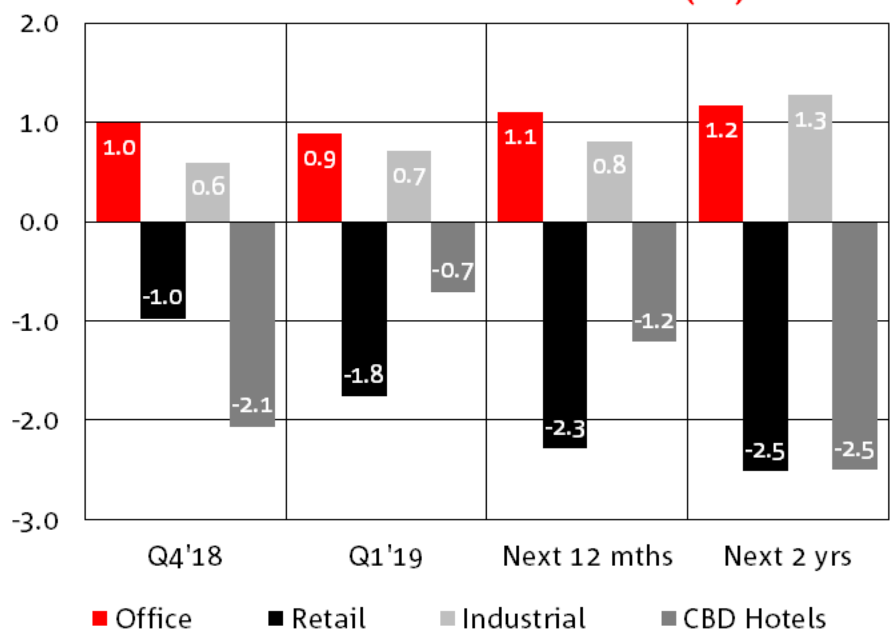
Capital growth is expected to be fastest for Industrial in 2 years' time (1.3%), just ahead of Office (1.2%). QLD (2.3%) and VIC (1.9%) lead the way for Industrial, and WA (2.4%) and QLD (2.3%) for Office. Overall Retail values are tipped to fall -2.5%, with the heaviest falls in NSW (-2.7%), VIC (-2.5%) and QLD (2.5%). CBD Hotels are also predicted to fall -2.5% in 2 years' time - **see page 10 for detail**.

The national office market vacancy rate rose a little in Q1 to 7.9% (7.8% in Q4). Whereas lower vacancy was reported in NSW (4.7%) and QLD (10.1%), it rose to 4.5% in VIC (still lowest overall), SA/NT (12.6%) and WA (15.0%). Office vacancy is expected to remain steady at 8% in the next 1-2 years, with rising vacancy NSW and VIC (to still very low levels) offset by modest tightening in QLD, SA/NT and WA.

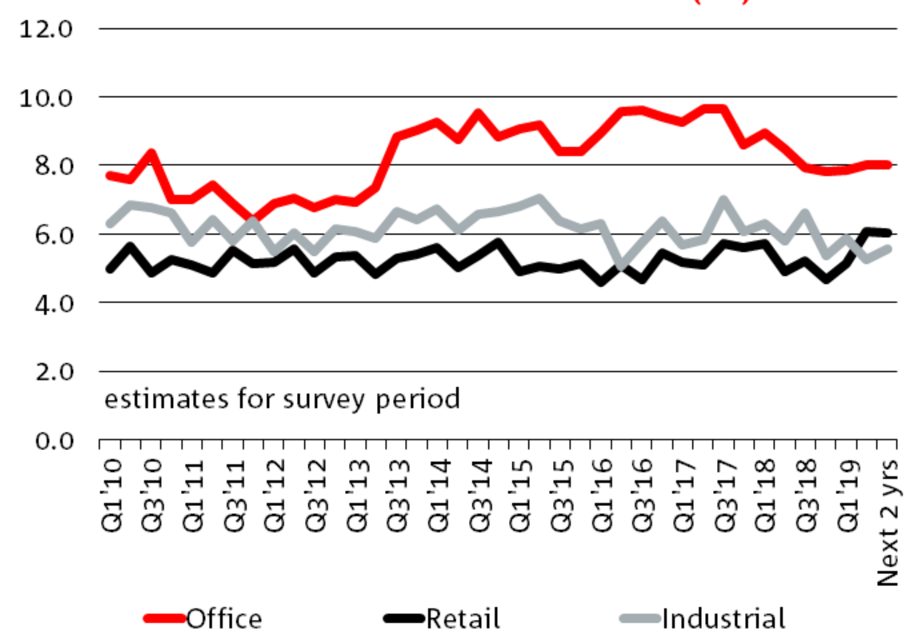
Overall Retail vacancy climbed to 6.1% in Q1 after having fallen to 4.7% in Q4 on the back of higher uptake typically seen before Xmas. Retail vacancy rose in all states except QLD and WA (unchanged).

In the Industrial sector, national vacancy rose to 5.9% (5.4% in Q4), led by sharply higher vacancies in WA (11.8%) and SA/NT (9.0%). The national market is however expected to remain relatively tight over the next 1-2 years - **see page 11 for detail**.

## CAPITAL VALUE EXPECTATIONS (%)




## VACANCY RATE EXPECTATIONS (%)



# MARKET OVERVIEW - RENTS & SUPPLY

Office property is expected to lead the way for rental growth over the next 1 -2 years, growing by 1.1% in 12 months time and by 1.6% in the following year. Expectations in the next 12 months are strongest in VIC (2.1%) and weakest in SA/NT (-1.8%), but QLD (3.2%) leads the way in 2 years' time, followed by VIC (2.2%).

Industrial rents are tipped to grow 0.9% nationally over the next 12 months and 1.4% in the following year. VIC (1.3% & 2.4%) is expected to generate the highest income returns, followed by WA (1.2% & 2.1%).

The outlook for Retail rents remains negative (-2.7% & -2.9%) and has been pared back significantly since the last survey (-0.9% & -0.8%). Retail rents are expected to fall in all states over this period, led by WA (-6.5% & -5.6%) - **see page 10 for detail**.

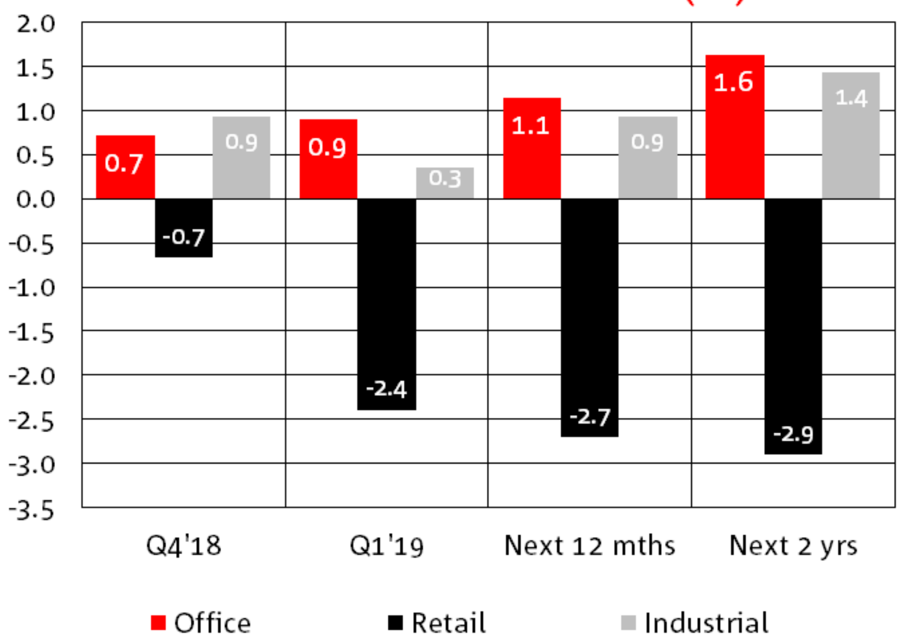
Property professionals said supply conditions in the Office, Industrial and CBD Hotels sector were 'neutral' in Q1. Office and Industrial markets are expected to remain that way in the next 1-5 years, but some over-supply in the CBD Hotels market is anticipated in the next 1-5 years. Retail markets are expected to be 'somewhat' over-supplied in the next 1-3 years, but return to balance in 5 years' time.

By state large over-supply is expected to persist in Office markets in SA/NT and WA over the next year, but slowly work towards 'neutral' conditions in 5 years' time.

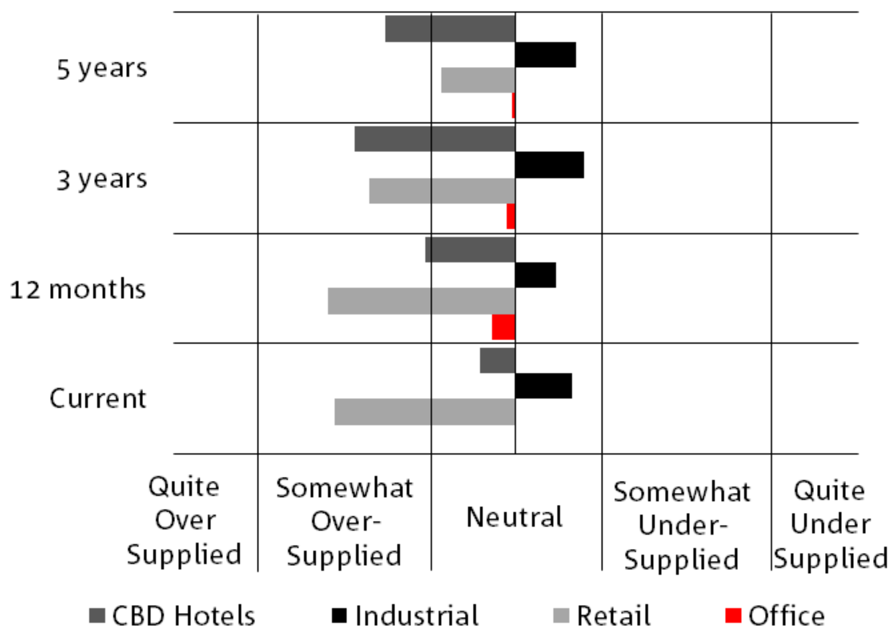
Retail markets also look set to remain over-supplied in most states over the next 1-3 years, and heavily in SA/NT and WA.

State industrial markets are mixed, with modest under-supply evident in NSW and QLD and some over-supply in WA next year and emerging in SA/NT in 3 years time.

## GROSS RENTAL EXPECTATIONS (%)




## SUPPLY CONDITIONS



# MARKET OVERVIEW - DEVELOPMENT INTENTIONS

Overall, the number of property developers expecting to begin new works in the next month fell to 6% (12% in Q4). The number planning to start in the next 1-6 months also fell to 35% (38% in Q4). Overall, 41% said they planned to start new works in the next 6 months (down from 49% in Q4) and well below the Survey average (50%).

The number of developers who said they planned to start new projects in the next 6-12 months also fell a little to 22% (23% in Q4), but the number planning to start in the next 12-18 months rose to 19% (10% in Q4).

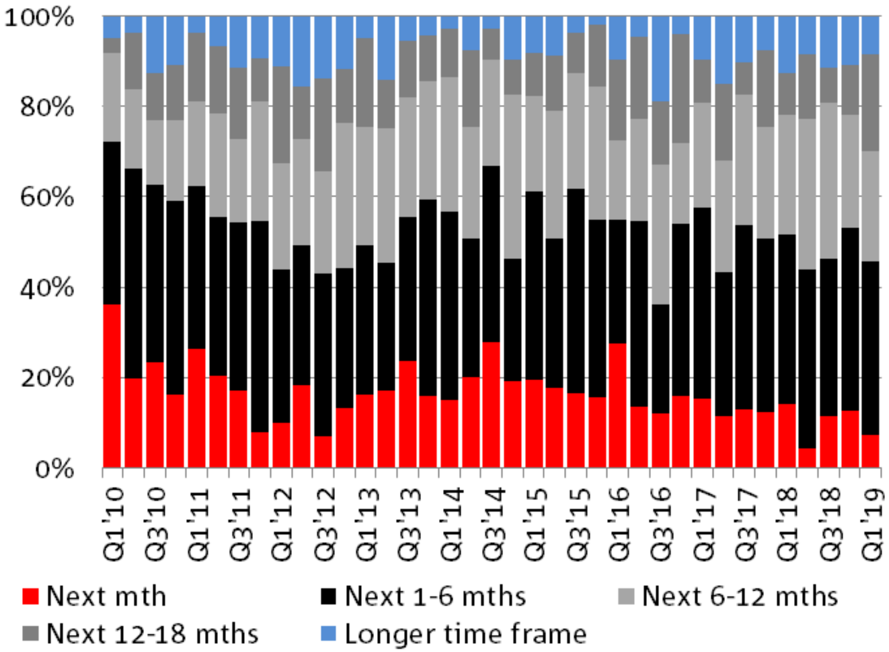
We continue to suspect that challenging funding conditions are making it harder to get new projects up and running, resulting in the shelving or delaying of some projects.

Among developers planning to commence new works, the number targeting residential development projects increased to 51% in Q1 (48% in Q4) - but it remains below long-term average levels (54%), and reinforces the view that residential building activity has passed its peak.

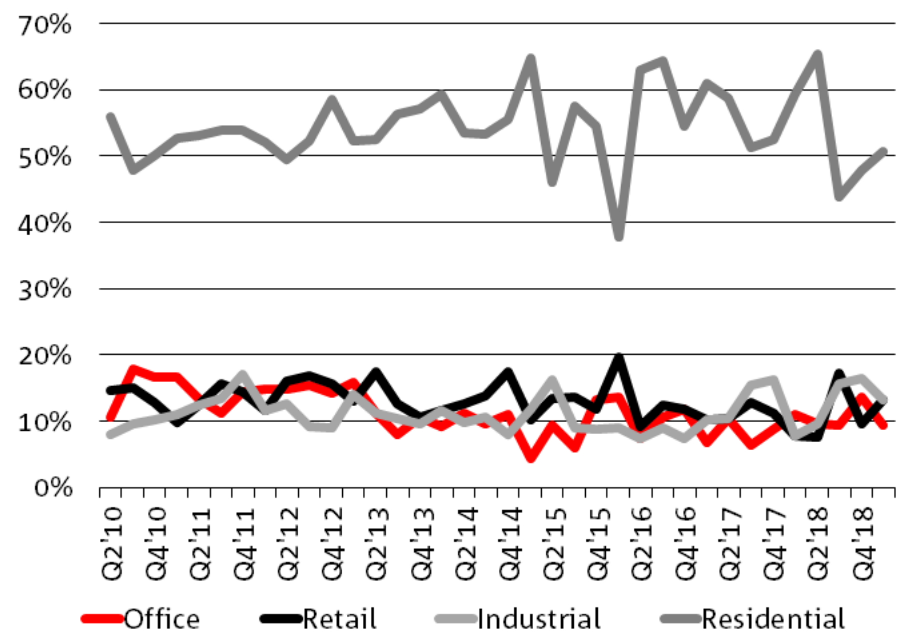
Surveyed property professionals also pointed below average numbers of developers targeting Office (9%) and Industrial property (13%) during the quarter.

The recently released national accounts number have also highlighted a turn down in the construction cycle - which appears to have continued (and indeed accelerated) into early-2019. This also reinforces NAB's view that over the next two years we are facing a pronounced residential construction cycle (a fall of around 20%).

## COMMENCEMENT INTENTIONS - TIME




## COMMENCEMENT INTENTIONS - SECTOR



# MARKET OVERVIEW - LAND SOURCES & CAPITAL INTENTIONS

The number of property developers looking to use land-banked stock for their new projects in Q1 2019 rose to 67% (61% in Q4),their highest level since Q3 2016 and well above long-term Survey average levels (59%).

The number who said they were seeking new acquisitions however fell to 20% (from 29% in Q4 and 30% at the same time last year).

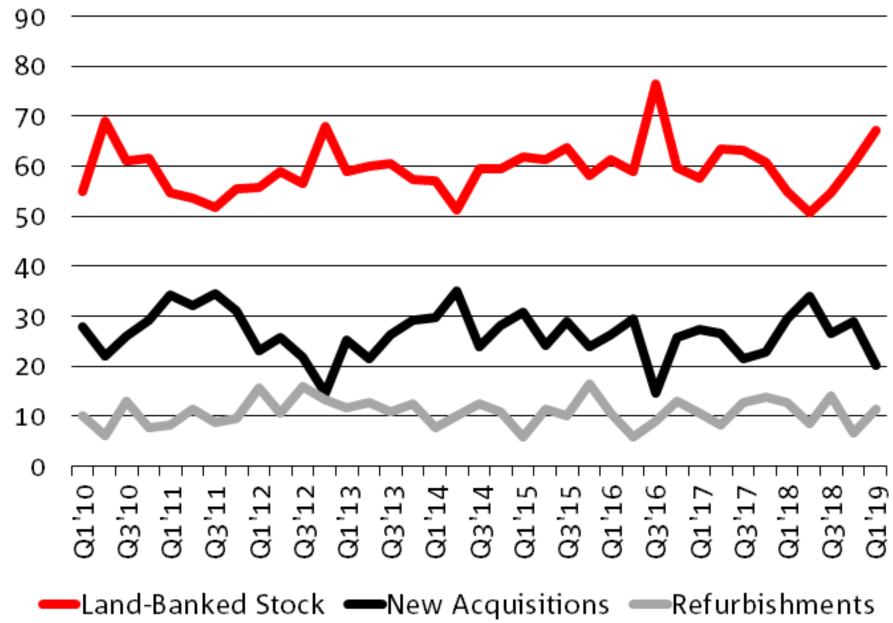
The number of developers looking at refurbishment opportunities rose to 11% in Q1 (7% in Q4).

The number of property developers planning to source more capital to fund their developments in the next 6 months was unchanged at 23% in Q1. Around 63% had no intention to source capital in the short-term (59% in Q4) and 14% were unsure (19% in Q4).

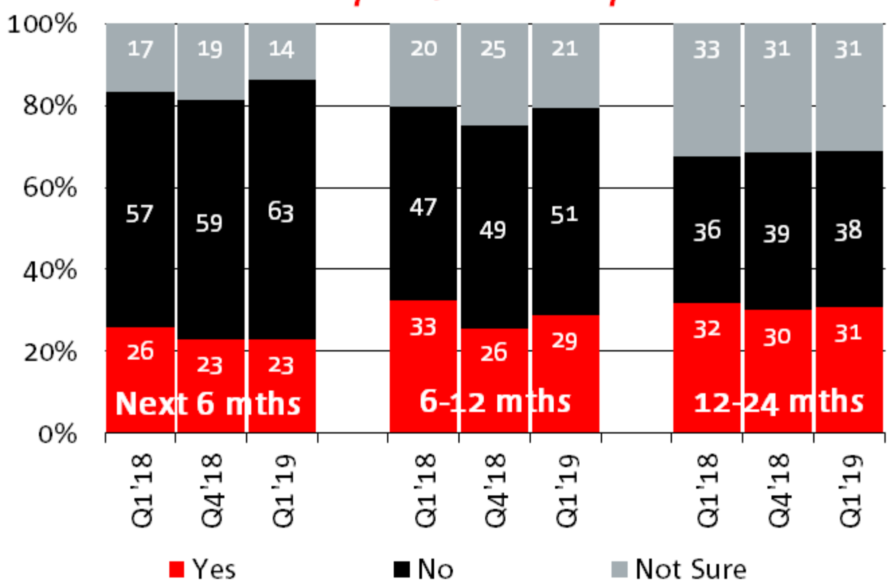
Although fewer developers said they were planning to commence new projects in the next 6-12 months, more developers planned to source capital in the next 6-12 months. The number who planned to do so rose to 29% in Q1 (26% in Q4), but 51% had no plans to do so (46% in Q4).

Slightly more developers also intended to source more capital in the longer-term (12-24 months) - 31% yes, 38% no and 31% unsure.

## SOURCES OF LAND DEVELOPMENT (%)




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



# MARKET OVERVIEW - FUNDING & PRE-COMMITMENTS

Accessing credit is still very difficult.

In net balance terms, -40% said it was harder to obtain borrowing or loans (debt) needed for their business in Q1 2019 (-41% in Q4) - the second worst result on record.

Equity funding was also assessed as being harder than it has been since the Survey started according to a net -32% of property professionals (-31 in Q4).

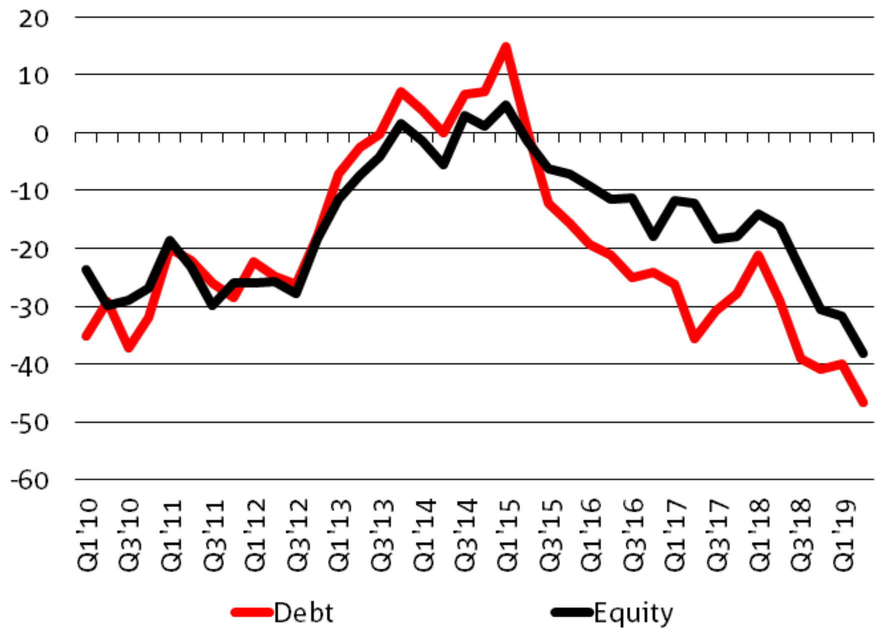
Looking ahead, property professionals expect funding conditions to worsen further over the next 3-6 months - a net -47% see debt funding conditions worsening and -38% said it will be harder to obtain equity financing.

Australia wide, the average pre-commitment to meet external debt funding requirements for new developments fell to 64.0% for residential property in Q1 (65.3% in Q4), but rose to 58.9% for commercial (56.9% in Q4).

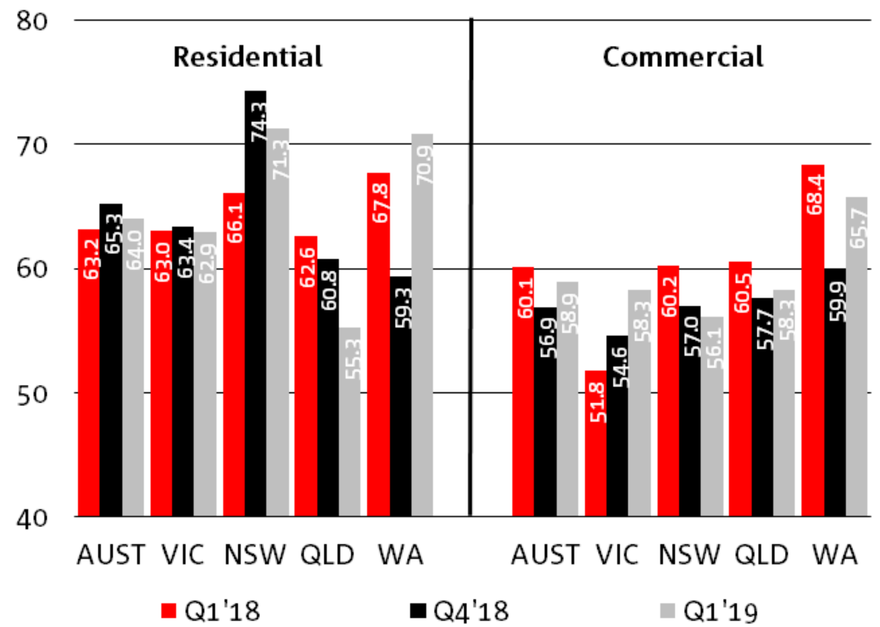
Residential requirements fell in VIC (62.9%), QLD (55.3%) and NSW (71.3%), but were noticeably higher in WA (70.9%). Commercial property pre-commitments fell in NSW (56.1%), but increased in VIC (58.3%), QLD (58.3%) and WA (65.7%).

On balance, more property professionals still expect pre-commitment requirements to worsen going forward - a net -28% for residential property in the next 6 months and -26% in 12 months, and -27% in 6 months and -20% in 12 months for commercial property.

## EASE OF ACQUIRING DEBT/EQUITY (NET)




## PRE-COMMITMENT REQUIREMENTS (%)



# SURVEY RESPONDENTS EXPECTATIONS (AVG) Q1-2019

## OFFICE CAPITAL VALUES (%)

| | VIC | NSW | QLD | WA | SA/NT | AUS |
|---|---|---|---|---|---|---|
| Q1'19 | 0.7 | 1.1 | 1.1 | 0.0 | 0.6 | 0.9 |
| Q1'20 | 0.8 | 1.2 | 1.6 | 1.1 | 0.0 | 1.1 |
| Q1'21 | 0.7 | 0.6 | 2.3 | 2.4 | 0.3 | 1.2 |

## OFFICE RENTS (%)

| | VIC | NSW | QLD | WA | SA/NT | AUS |
|---|---|---|---|---|---|---|
| Q1'19 | 2.9 | 1.1 | 1.0 | -0.6 | -2.0 | 0.9 |
| Q1'20 | 2.1 | 1.4 | 1.7 | 0.3 | -1.8 | 1.1 |
| Q1'21 | 2.2 | 1.3 | 3.2 | 1.7 | -1.3 | 1.6 |

## RETAIL CAPITAL VALUES (%)

| | VIC | NSW | QLD | WA | SA/NT | AUS |
|---|---|---|---|---|---|---|
| Q1'19 | -1.7 | -1.3 | -2.1 | -2.8 | -1.9 | -1.8 |
| Q1'20 | -2.3 | -2.0 | -2.5 | -2.8 | -1.9 | -2.3 |
| Q1'21 | -2.5 | -2.7 | -2.5 | -1.9 | -1.9 | -2.5 |

## RETAIL RENTS (%)

| | VIC | NSW | QLD | WA | SA/NT | AUS |
|---|---|---|---|---|---|---|
| Q1'19 | -2.6 | -1.2 | -2.6 | -7.5 | -2.3 | -2.4 |
| Q1'20 | -3.3 | -1.7 | -2.6 | -6.5 | -1.4 | -2.7 |
| Q1'21 | -3.9 | -2.0 | -2.3 | -5.6 | -1.4 | -2.9 |

## INDUSTRIAL CAPITAL VALUES (%)

| | VIC | NSW | QLD | WA | SA/NT | AUS |
|---|---|---|---|---|---|---|
| Q1'19 | 0.9 | 0.3 | 1.7 | -0.3 | -0.7 | 0.7 |
| Q1'20 | 1.3 | 0.4 | 1.6 | 0.3 | 3.8 | 0.8 |
| Q1'21 | 1.9 | 0.5 | 2.3 | 1.5 | -1.5 | 1.3 |

## INDUSTRIAL RENTS (%)

| | VIC | NSW | QLD | WA | SA/NT | AUS |
|---|---|---|---|---|---|---|
| Q1'19 | 0.6 | 0.4 | 0.5 | 0.0 | -0.7 | 0.3 |
| Q1'20 | 1.3 | 0.9 | 1.1 | 1.2 | -1.5 | 0.9 |
| Q1'21 | 2.4 | 1.0 | 1.7 | 2.1 | -1.5 | 1.4 |

# SURVEY RESPONDENTS EXPECTATIONS (AVG) Q1-2019

## OFFICE VACANCY RATE (%)

| | VIC | NSW | QLD | WA | SA/NT | AUS |
|---|---|---|---|---|---|---|
| Q1'19 | 4.5 | 4.7 | 10.1 | 15.0 | 12.6 | 7.9 |
| Q1'20 | 5.5 | 5.3 | 9.7 | 14.7 | 12.2 | 8.0 |
| Q1'21 | 6.0 | 6.0 | 9.3 | 13.7 | 10.6 | 8.0 |

## RETAIL VACANCY RATE (%)

| | VIC | NSW | QLD | WA | SA/NT | AUS |
|---|---|---|---|---|---|---|
| Q1'19 | 4.5 | 5.4 | 4.3 | 6.0 | 10.3 | 5.1 |
| Q1'20 | 5.6 | 6.6 | 4.8 | 6.0 | 11.0 | 6.1 |
| Q1'21 | 6.0 | 6.5 | 4.4 | 5.0 | 11.0 | 6.0 |

## INDUSTRIAL VACANCY RATE (%)

| | VIC | NSW | QLD | WA | SA/NT | AUS |
|---|---|---|---|---|---|---|
| Q1'19 | 4.8 | 3.9 | 6.4 | 11.8 | 9.0 | 5.9 |
| Q1'20 | 5.0 | 3.6 | 5.2 | 10.2 | 8.0 | 5.3 |
| Q1'21 | 6.0 | 4.0 | 5.3 | 9.4 | 8.0 | 5.6 |

## 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:

•annual growth to the current quarter
•annual growth in the next 12 months
•annual growth in the 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.
Over 300 property professionals participated in the Q1 2019 Survey.

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