



MELBOURNE CBD

RETAIL MARKET BRIEF JULY 2016

Key Facts

The vacancy rate in the Melbourne CBD retail Core **declined to a five year low of 2.4%.**

Clothing and food retailers account for the majority of occupied CBD retail Core shops at 64.8%.

Investment activity totalled \$357.1 million in the 12 months to July 2016.

Prime CBD retail yields have firmed by 37.5 bps for freehold and 12.5 bps for strata shops over the past 12 months



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The vacancy rate in the Melbourne CBD retail Core declined to a five year low as at July 2016, underpinned by strong growth in the resident and working population.

Retail Overview

Following the May interest rate cut, combined with higher employment levels and an improved long term economic outlook, consumer sentiment has increased by 7.4% over the past 12 months to July 2016.

Retail turnover in Victoria grew by 3.9% in the 12 months to May 2016, compared to 4.0% in the preceding 12 months. Lower interest rates combined with strong growth in house prices has contributed to the solid turnover levels, both of which have increased household spending and wealth confidence.

Retail trade in Victoria totalled \$60.4 billion, up from \$58.1 billion the previous year. All sectors recorded positive year-on-year growth, with the exception of electrical and electronic goods (-1.2%). The clothing, footwear and personal accessory sector grew from 0.8% a year ago to 1.7%, Department stores rose from 2.7% to 6.6% while cafes and restaurants grew by 9.3% from 3% growth a year ago. The NAB online

sales index showed annual growth of 13.2% in the 12 months to May 2016, up from 9% in May 2015. Nevertheless, the share of online retailing at \$19.9 billion has fallen modestly, accounting for 6.7% of total retail spending compared to its 7% share 12 months ago.

Internationally recognised as the world's most liveable city (EIU), Melbourne CBD-based employment and residential population growth continues to underpin demand for CBD retail space from both domestic and international retailers. Over the past three years white collar employment has grown by 13,751 workers in the CBD, while the residential population has increased by 21,455 over the same period. Total inbound tourism numbers into Melbourne grew by 13.3% to 2.4 million over the 12 months to May 2016, with Chinese tourists underpinning this growth.

Knight Frank Research has completed its 2016 Prime Melbourne CBD Retail Core survey which highlights vacancy and tenancy mix trends across the precinct.

MELBOURNE CBD RETAIL CORE SURVEY

Vacancy

As at July 2016, the vacancy rate in the Melbourne CBD retail Core declined to 2.4%, down from 3.2% at the equivalent period in 2015. Total vacancy is now at the lowest level since December 2011.

The largest reduction in the vacancy rate over the past 12 months was recorded in Arcades/Laneways, falling from 1.8% to 0.7%. There are just three shops available for lease compared with six as at July 2015, with the vacancy rate well below the long term average of 2.2%.

Vacancy for retail shops offering Street Frontage decreased from 4.1% to 3.3% over the past 12 months, driven by absorption of shops at prime locations. Collins Street saw prime vacancy levels decrease from 6.5% to 1.8%, with just two shops vacant compared with seven 12 months earlier. This has largely been underpinned by fashion retailers with the likes of Wittner and Rhodes & Beckett occupying space. Tenant interest for Swanston Street space also saw the prime vacancy rate fall, with the street vacancy declining from 3.4% to 1.3% with a number of food retailers occupying space.

While churn has occurred, the vacancy rate in the super prime precinct of the Bourke Street Mall remained at 0%. New tenant commitments include Chemist Warehouse, Cotton On and Michael Hill Jeweller, albeit with the latter two opening later in the year.

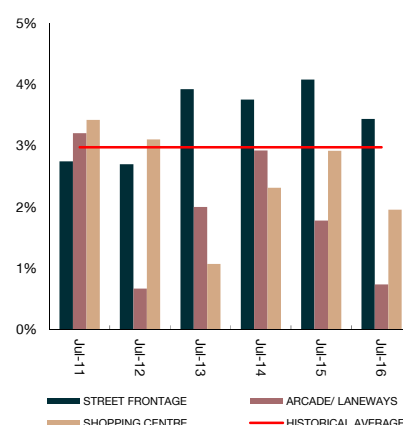
TABLE 1
Melbourne CBD Retail Core*
Vacancy by retail type (%)

	Jul-15	Jul-16
Arcades/ Laneways	1.8	0.7
Street Frontages	4.1	3.3
Shopping Centres	2.9	2.2
Total Retail Vacancy	3.2	2.4

Source: Knight Frank Research

*For definition of Retail Core see back page

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



Source: Knight Frank Research

Elsewhere, vacancy levels in Elizabeth Street increased from 1.3% to 1.9% impacted in part by outgoing tenants Laura Ashley and Bendigo Bank vacating their premises.

The vacancy rate in Shopping Centres fell from 2.9% to 2.2% over the past year. An increase in demand from clothing and service retailers in particular saw the vacancy rate decrease. New retailer additions into shopping centres included Sephora at Melbourne Central, Red Pearl at Emporium and Benjamin Baker at QV.

Tenancy Mix & New Supply

The retail tenancy mix in the Melbourne CBD retail core remains dominated by food and clothing retailing, collectively accounting for 64.8% of the total number of shops. Overall, clothing, footwear & soft goods retailing represents 33.3% of all retail shops within the CBD retail Core, largely in the form of other clothing retailing (11% of total) which incorporates unisex retailers like Zara and H&M, followed by women's clothing (9% of total). However, the weight of clothing, footwear & soft goods retailers is far greater within CBD shopping centres

specifically at 60.3%. Within other retail formats, the dominance is less pronounced, particularly Arcades/Laneways where clothing, footwear & soft goods retailers account for only 11.1%.

In line with Melbourne's popularity for its cafes and dining culture, food retailing is the second largest retail type (31.5%), followed by personal retailing (12.7%) and service retailing (8.1%), largely underpinned by hairdressing & beauty retailers.

Currently a number of centres and arcades are undergoing refurbishment or have recently completed in response to accommodate further international retailer expansions into the Melbourne CBD. Recent refurbishments include Emirates House, located between Swanston and Elizabeth Streets totalling 2,000m² over two levels. Anticipated to open later in the year, Emirates House will accommodate luxury retailer Burberry (1,000m²), Brunetti's cafe and watch specialist The Hour Glass.

St Collins Lane (9,000m²) which stretches between Little Collins and Collins Streets completed in May 2016 adds 59 specialty shops, four mini-majors and three kiosks to the Melbourne CBD retail Core survey. The refurbished shopping centre accommodates a mix of international, luxury, clothing and personal retailing with new international retailers such as REISS, Maje and Sandro making their first entry into Melbourne.

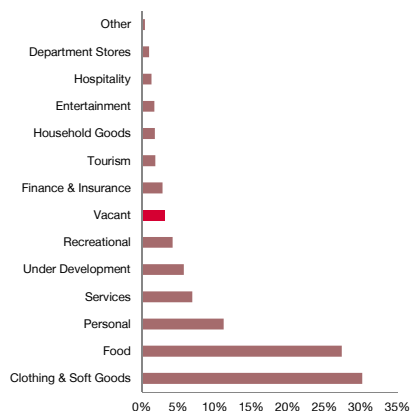
The total number of international retailers has increased to 121, up from 65 traders in July 2010. Clothing & footwear retailers (62%) and personal goods (22%) are the most dominant occupiers amongst international operators.

"CBD-based employment and residential population growth continues to underpin demand"

FIGURE 2

CBD Retail Core Tenancy Mix

% of total number of shops



Source: Knight Frank Research

Tenant Demand & Rents

Leasing activity in Melbourne's CBD continues to be underpinned by international retailers seeking prime space within the CBD retail Core. While demand is high, there is a lack of suitable leasing options to match their requirements. The growing residential and working population in Melbourne's CBD has encouraged supermarket chains and convenience stores to expand their exposure within the CBD market. Recently EzyMart opened at 520 Bourke Street while Woolworths Metro continued to expand its CBD footprint by opening a store in Melbourne Central. It is rumoured Woolworths has committed to a further two CBD sites.

Rental rates in the Melbourne CBD have remained relatively stable over the past 12 months, while moderate rental growth has occurred in the super prime retail Core. As at July 2016, gross retail rents in the super prime retail Core precinct of Bourke Street currently range from \$8,000/m² to \$12,000/m².

Prime Street Frontage retail rents range between \$1,500/m² and \$5,000/m². Rents in Arcades presently average \$1,600/m² while Shopping Centres attract rental rates between \$800/m² and \$2,000/m².

Investment Activity

Investor demand for retail investments has remained strong over the past 12 months. Transaction volumes in excess of \$1 million totalled \$357.1 million in the 12 months to July 2016, more than double the \$151.7 million recorded for the equivalent period in 2015. This was the highest annual total since 2007. Historically, CBD transaction volumes have averaged \$173 million per annum.

Volumes were underpinned by the sale of the Myer Centre (approximately \$150 million for a 30% share) and 206 Bourke Street (\$116.2 million). There have only been six transactions recorded above \$100 million since 1999.

Offshore buyers were the most active purchasers spending \$158.6 million, accounting for 44% of transaction volumes, the highest total recorded since 1999. Looking ahead, strong demand from offshore buyers is anticipated to continue with St Collins Lane reportedly in due diligence, with JP Morgan rumoured to be purchasing the asset for approximately \$250 million.

Prime yields for freehold retail (excluding shopping centres and arcades) compressed by 37.5 basis points to now range between 3.00% and 4.20%, whilst prime yields for strata retail assets recorded a firming of 12.5 basis points to now range between 4.00% and 5.50%.

TABLE 2

Recent Sales Activity Melbourne CBD Retail

Address	Price (\$ m)	Core Market Yield (%)	GLAR (m ²)	Rate of GLAR (\$/m ²)	Date
Myer Melbourne (30% share)	c.150	c.5.0*	39,923	c.11,272	May-16
206 Bourke Street	116.2	5.5*	11,969	9,715	Dec-15
168-174 Bourke Street	18.2	2.1*	737	24,708	Dec-15
59-63 Bourke Street	9.8	3.3	1,318	7,435	Dec-15
21-25 Hardware Lane	8.1	3.9	700	11,571	Oct-15
384-386 Bourke Street	15.0	3.0*	1,200	12,500	Sep-15
194 - 200 Bourke Street, MidCity Arcade and Chinatown Cinema	57.0	5.45	3,722	15,314	May-15

*initial yield

TABLE 3

Recent Leasing Activity Melbourne CBD Retail

Address	Tenant	Gross Rent (\$/m ²)	GLAR (m ²)	Term (yr)	Date
146 Swanston Street	Tsujiri Japanese	3,250	80	5	Jun-16
115 Collins Street	Philippe Mouchel	380	400	3	May-16
73 A'Beckett Street	Galaxy Technology	1,100	240	5	Mar-16
108 Bourke Street	Foodbase Korean	1,250	200	5	Jan-16
207 Lonsdale Street	Yi Australia	1,450	160	5	Dec-15
317 Swanston Street	Myeong Cosmetics	1,600	215	5	Dec-15
206 Bourke Street	Tim Ho Wan	1,318	330	5	Oct-15
555 Bourke Street	Sake Jr	900	500	10	Oct-15
349 Bourke Street	Cotton-On	U/D	1,200	U/D	Oct-15
221 Russell Street	Suttons UGG Australia	1,900	80	5	Jul-15

U/D undisclosed

Source: Knight Frank Research



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Outlook

Looking ahead, demand for retail space in the Melbourne CBD retail Core is expected to remain solid over the next 12 months. The forecast completion of several high-rise apartment developments in the CBD combined with strong population growth of 5.6% per annum over the next five years, will continue to support demand from retailers looking to expand their footprint in the CBD.

While there is no doubt that the vote in favour of Brexit will generate a period of renewed uncertainty it is unlikely this will have a big impact on Australian retailers going forward. The economic drivers of retail spending will remain fundamentally unchanged, with the outlook for retail

spending in Australia positive. There may be a slowdown in the number of international retailers looking to expand into the Australian market, with evidence of some requirements being put on hold during this period of uncertainty.

Transaction volumes are anticipated to remain elevated at above trend levels over the medium term as a number of offshore buyers continue to increase their Australian exposure.

As a result of continued investor interest for CBD retail assets, prime retail yields are expected to remain at current levels despite the constrained outlook for rents in the short term.

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.

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