

Australia Retail, Q2 2017

# Prime Sydney CBD leads the way in H117

 Retail Turnover  
3.1 y-o-y May

 Consumer Sentiment  
96.2 Jun

 CBD Prime Rent  
1.6% y-o-y Jun

 Regional Centre Yields  
5.4% Jun

**KEY POINTS**

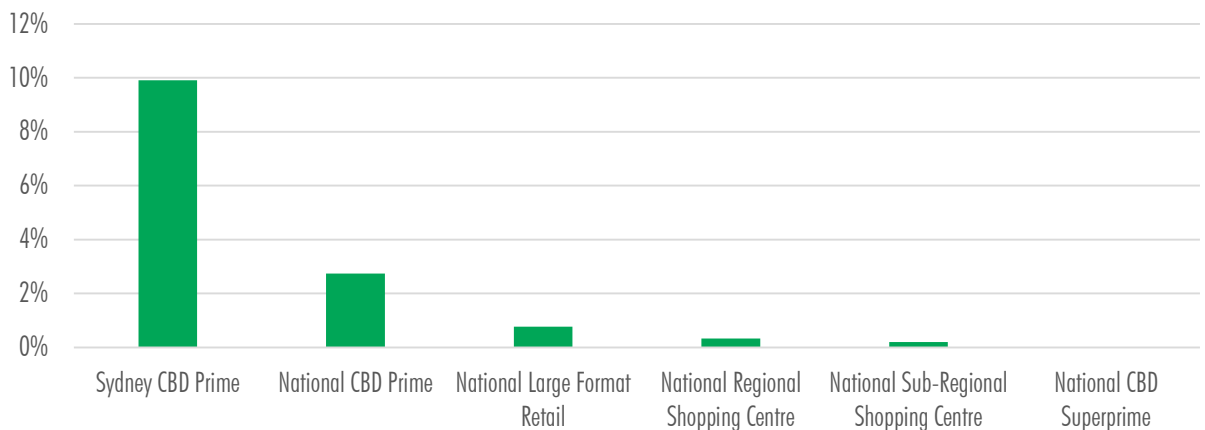
- Household goods sales improved in New South Wales with growth of 2.2% y-o-y (3mma) compared to 1.1% in April. Victoria and Queensland recorded strong growth between 4-6% y-o-y (3mma).
- Sydney CBD Prime rent that saw growth of ~10% in H12017, driven by demand spilling over from super prime rent and the low availability of quality space.
- Landlords continue to expand F&B offerings to attract foot traffic and generate higher sales productivity. Existing food businesses are becoming increasingly agitated on the dilution effect on sales by the increase in competition within F&B.
- We are close to the end of yield compression, as income growth moderates.

Retail trade stabilised in May driven by a pick up in household goods sales and Western Australia no longer a drag to growth in the quarter. National retail trade grew by 3.1% y-o-y (3mma) in the year to May, up from 2.7% in April. Household goods sales improved in New South Wales with growth of 2.2% y-o-y (3mma) compared to 1.1% in April. Victoria and Queensland recorded strong growth between 4-6% y-o-y (3mma).

Department store sales continue to decline in the quarter. Food retailing and cafes, restaurants and takeaway food services were the only two categories to outperform last year's performance, recording growth of 3.6% y-o-y (3mma) and 5.1% y-o-y (3mma) respectively.

Rent growth across all retail property types has been slower in H117 compared to H12016, with the exception of Sydney CBD prime rents, experiencing growth ~10% in first half, driven by demand spilling over from super prime rent and the low availability of quality space (figure 1).

Figure 1: Retail rent growth in H12017 – half yearly % change



Source: CBRE Research, Q2 2017.

**MORE CHANGES TO DEPARTMENT STORE FORMAT**

Innovation in retailing and the rise of online stores coupled with competition from international brands has adversely affected department stores sales. In a bid to reverse declining sales and differentiate from rivals, Myer and David Jones continue to explore new store formats.

Myer recently converted its second floor (4000sqm) department store in Frankston, Melbourne into a specialised clearance and sales outlet. This is a similar concept to the Nordstroms Rack branded clearance chain, which aims to keep surrounding flagship stores fresh by clearing unwanted excess stock. Myer is looking to roll one out in each state.

Towards the end of year, David Jones is planning on launching its new look food hall at Westfield Bondi Junction, which includes gourmet groceries to lure shoppers and boost sales across all categories. In addition, David Jones plans to offer smaller stand alone convenience stores (between 300 to 500sqm) that carry premium labels not stocked at the major supermarkets.

**STRONG COMPRESSION IN LARGE FORMAT RETAIL**

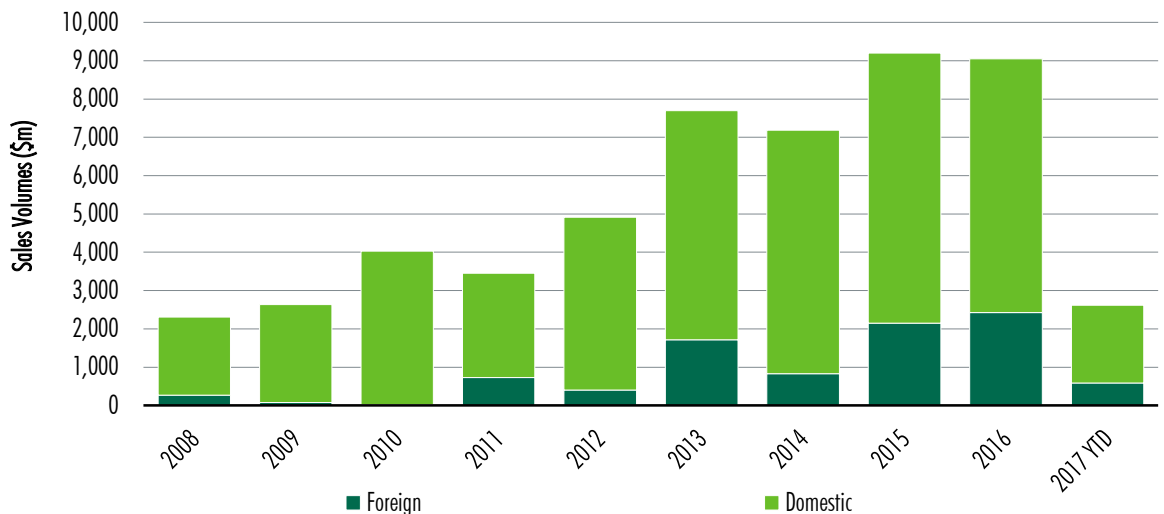
National retail yields compressed on average by 5bps in Q2, with the largest compression in large format retail (15bps) as investors move up the yield curve in search of higher returns.

Retail property transactions totalled ~\$1.1b in Q2, down from the \$1.6b recorded in Q1, of which 22% were purchased by foreign investors. Foreign investment has more than doubled from 8.2% of transactions recorded in 2012, indicating that Australia continues to be viewed as a strong destination for cross border investment in the Asia Pacific Region.

**LOWER YIELD COMPRESSION GOING FORWARD**

Retail yields are at record low for all sectors. We believe there is very little room left for compression in this cycle. The heat in the housing sector is slowly coming off as have dwelling approvals (which fell by 20% y-o-y in May). The retail environment in 2017 is expected to be weaker than two years ago, evidenced by slower rent so far this year. We expect the retail total return to be lower in 2017 than 2016.

Figure 2: National Buyer Origin Profile 2017 YTD



Source: CBRE Research, Q2 2017.

# CBD Retail

## RENTS REMAIN STABLE

After experiencing robust growth of above 5% in both 2015 and 2016, clothing, footwear and personal accessory retailing slowed to 1.5% y-o-y (3mma) to May 2017. With household budgets under pressure and consumer confidence below average in Q2, discretionary spending is expected to remain subdued for the remainder of the year.

Rent growth in the CBD has remained relatively flat in Q2 except for Sydney prime rents. Demand for super prime space in Pitt St mall has spilled over to surrounding buildings, with prime rent rising ~10% in H1, expanding the small super prime strip. Demand for CBD space remains strong from international brands as well as the F&B and health & fitness segments. However, conscious of rising occupancy costs, retailers are conducting more

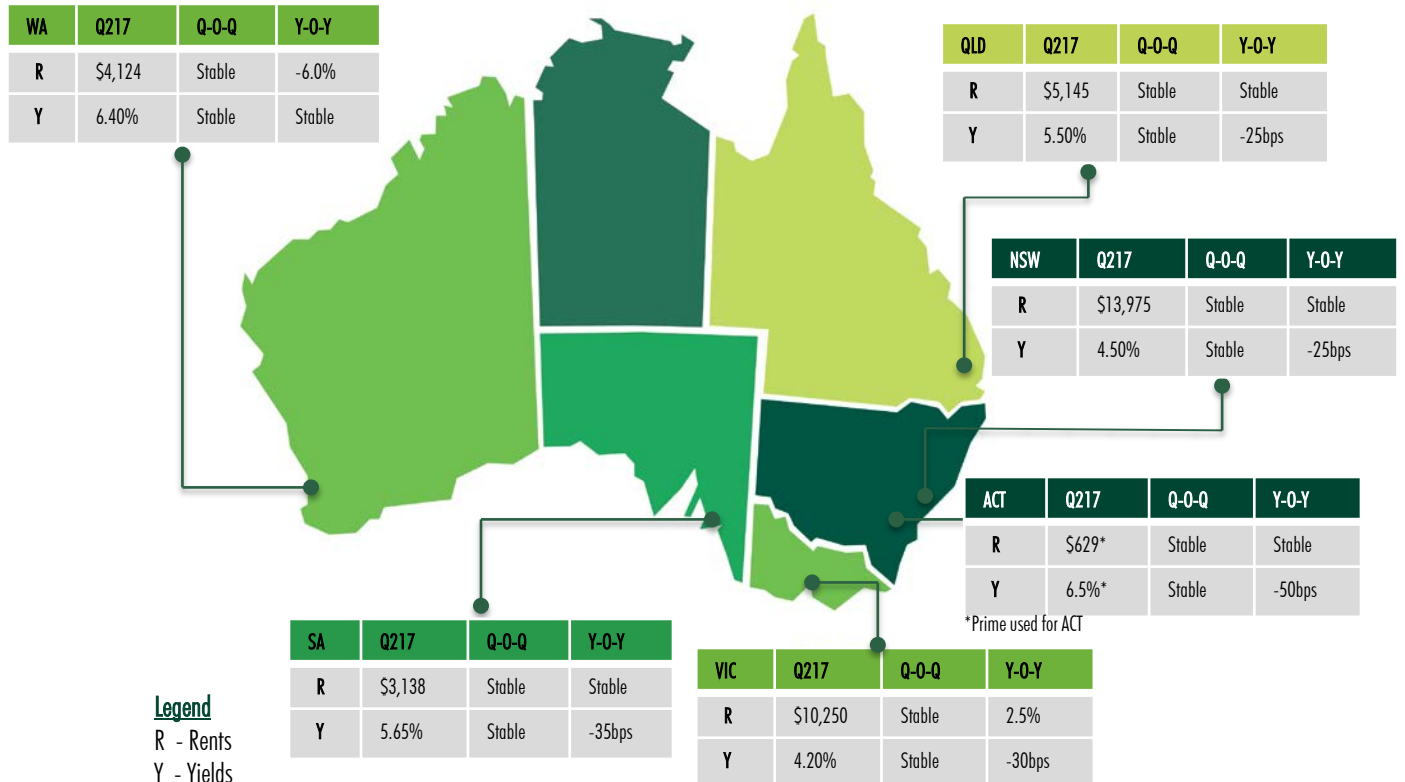
due diligence to ensure that they find the right site to meet their requirements, with the onus shifting to landlords to perform upgrades or reposition their assets in order to attract tenants.

The supply pipeline remains at a moderate level in comparison to its historic average, with New South Wales and Victoria accounting for ~75% of the national pipeline over the next three years.

## YIELDS CONTINUE TO TIGHTEN

Despite a limited amount of stock for sale, strong investor interest continues to push prime and secondary yields down. Sydney CBD prime yields may compress a little further as higher rent growth drives income. In other markets, yields are probably near the bottom for this cycle given they have remained steady over the past three quarters.

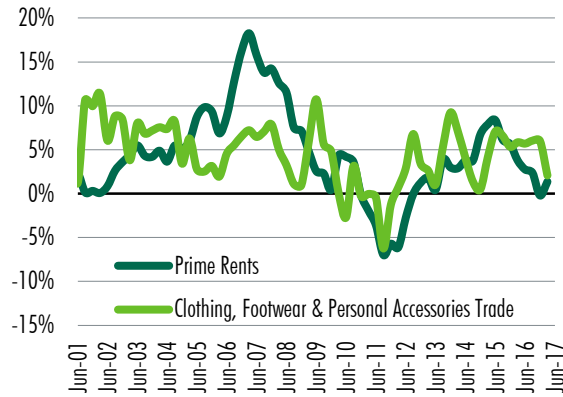
Figure 3: Super prime CBD retail key metrics



Source: CBRE Research, Q2 2017.

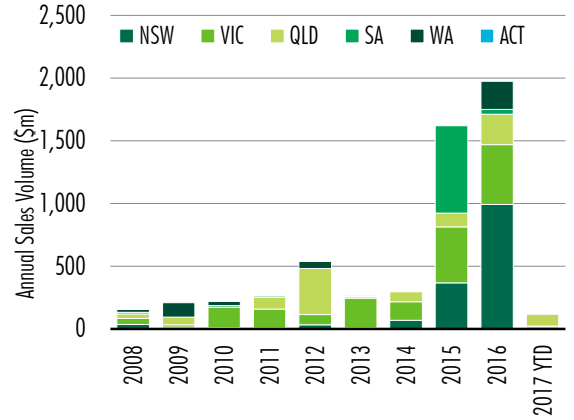
# CBD Retail Dashboard

Figure 4: Retail Sales and Prime CBD Rents Index



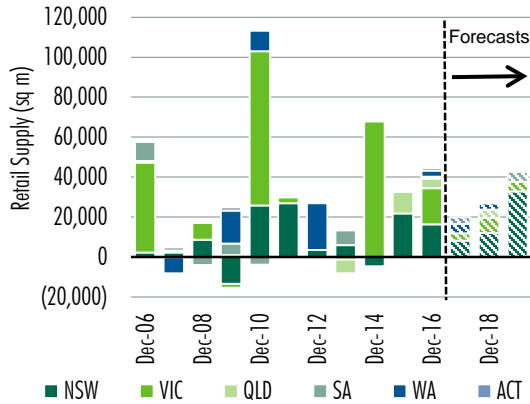
Source: ABS, CBRE Research, Q2 2017.

Figure 6: CBD Retail Transactions by State



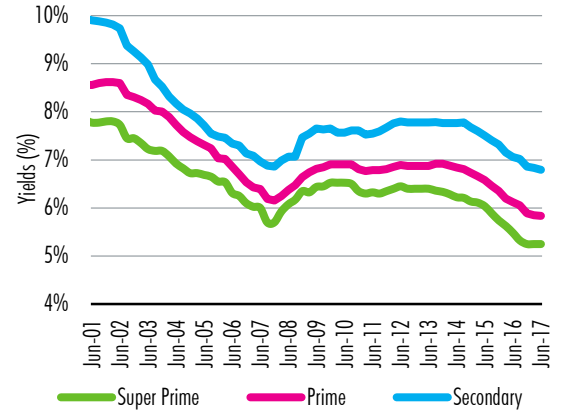
Source: CBRE Research, Q2 2017.

Figure 5: CBD Retail Supply by State



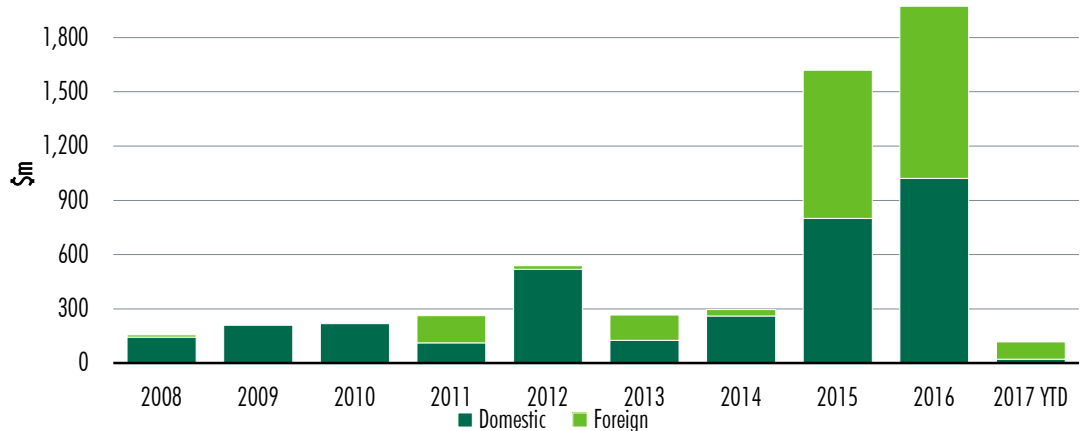
Source: CBRE Research, Q2 2017.

Figure 7: Average CBD Retail Yield



Source: CBRE Research, Q2 2017.

Figure 8: CBD Retail Buyer Profile



Source: CBRE Research, Q2 2017.

# Shopping Centres

## CHALLENGING TIMES AHEAD FOR RETAILERS

In the year to May 2017, clothing, footwear and personal accessory retailing (a key driver for speciality stores) recorded slower growth of 1.5% y-o-y (3mma), whilst traditional shopping centre tenants (supermarkets) grew by 3.7%.

National shopping centre rents were broadly stable in Q2. This is reflective of a more challenging trading environment, placing an increasing need on centres to optimise their tenancy mix and enhance customer experience, in order to increase MAT and rental performance.

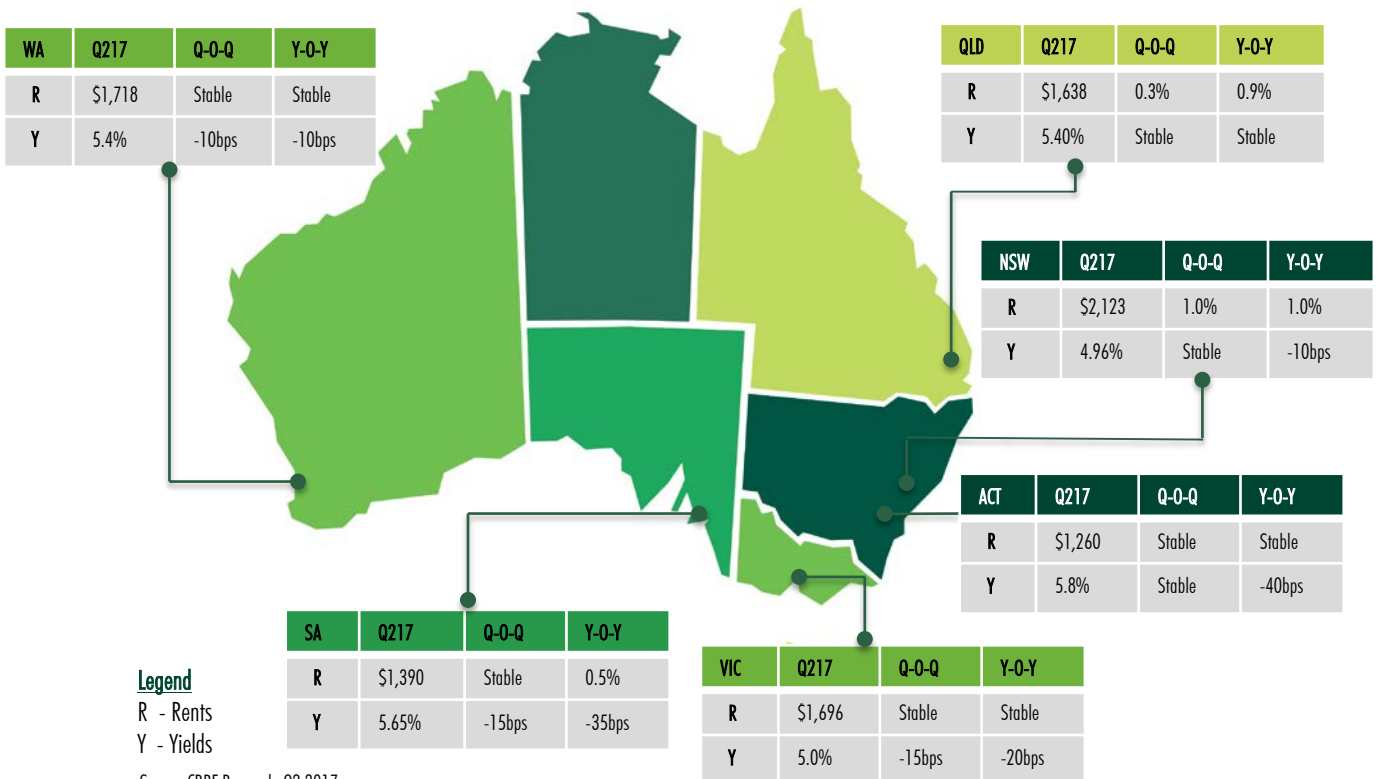
With landlords continuing to expand F&B offerings to attract foot traffic and generate higher sales productivity, existing food businesses are becoming increasingly agitated due to the dilution effect on their sales.

Citing the cannibalisation effect of putting more competition in the same trade environment, Sumo Salad placed their leasing companies into voluntary administration attempting to force Scentre to renegotiate rents in lieu of the rapid expansion of F&B offerings in their centres.

## CAPITAL MARKET ACTIVITY SLOWS

With transaction volumes exceeding \$5b in 2015 and \$3.6b in 2016, capital market activity slowed to ~\$1b in H1, the lowest half year sales volume since 2012. With limited amount of stock available, regional, sub-regional and neighbourhood shopping centre yields compressed by ~7bps in Q2, with the largest transaction being Charter Hall Retail REITs purchase of Salamander Shopping Centre for \$174.5m at an initial yield of 6.0%.

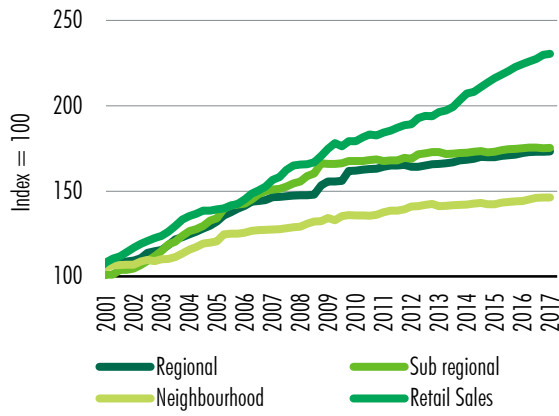
Figure 9: Regional Centre Key Metrics



Source: CBRE Research, Q2 2017.

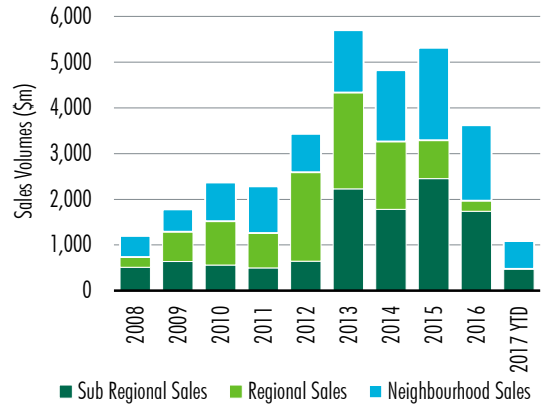
# Shopping Centres Dashboard

Figure 10: Retail Sales and Shopping Centre Rents Index



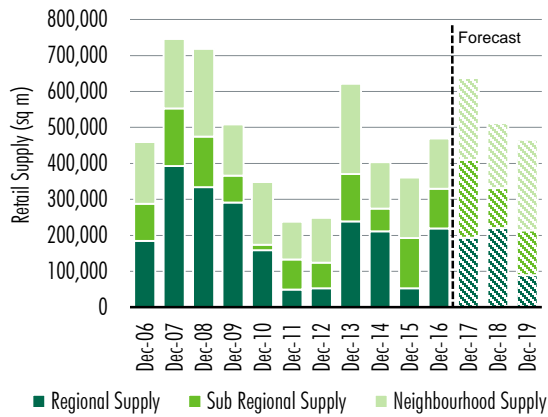
Source: ABS, CBRE Research, Q2 2017.

Figure 12: Shopping Centre Transactions by Type



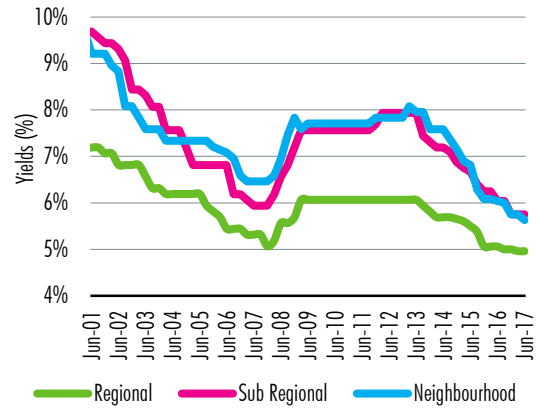
Source: CBRE Research, Q2 2017.

Figure 11: Shopping Centre Supply by Type



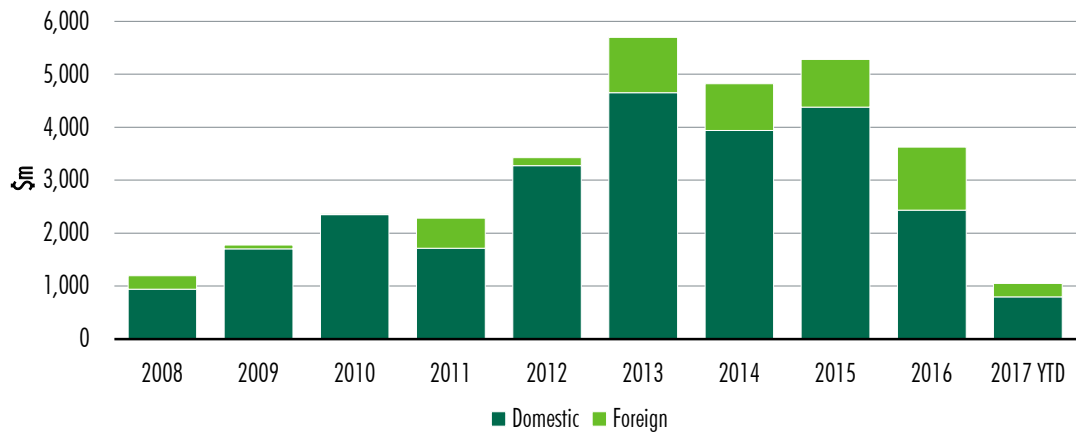
Source: CBRE Research, Q2 2017.

Figure 13: Average National Shopping Centre Yield



Source: CBRE Research, Q2 2017.

Figure 14: Shopping Centre Buyer Profile



Source: CBRE Research, Q2 2017.

# Large Format Retail

## HOUSEHOLD GOODS RETAILING FEELING EFFECT OF SLOWING HOUSING MARKET

Moderating housing and construction activity as well as rising bank investor lending rates are beginning to dampen household goods retailing. Total dwelling approvals in May 2017 were down 20% compared to a year ago and national investor housing finance contracted by -0.6% y-o-y. Household goods sales which had performed well in 2015 and 2016 with 6%+ growth is now experiencing growth below long term trend of just 2.2% y-o-y (3mma) in May. The correlation between the housing market and large format retail rent performance means that slower growth in median house prices will translate into lower large format retail capital values (Figure 20).

## YIELDS COMPRESSED BUT NEARING CYCLE PEAK

National large format yields compressed by ~15bps, reaching record lows in Sydney,

Melbourne and Adelaide. Investment activity slowed by 66% in H12017 compared H12016, but multiple sales achieved sub 6% yields. Major transactions include:

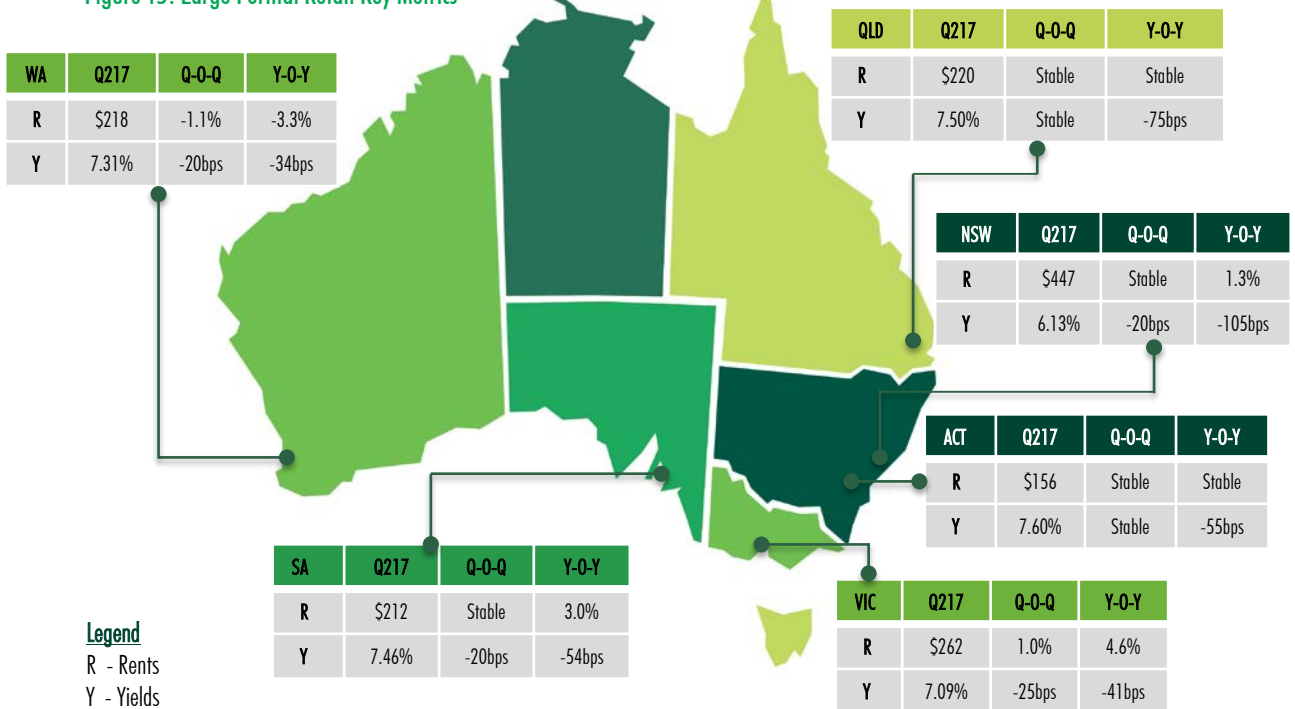
- Aventus Retail Property Fund’s purchase of Home Hub Marsden Park (NSW) for \$100m and Home Hub Castle Hills (NSW) for \$336m respectively. This represents initial yields of 6.0% and 5.5% respectively

## INCREASED SUPPLY TRIGGERING STORE ROLLOUT PROGRAMS

Supply created from vacated Masters stores is expected to be absorbed by both new entrants and established retailers. The reconfiguration of these centres into multi-tenanted stores is proving challenging due to the typical store depth of ~100m being well in excess of average requirements of around 50m x 20m.

Demand for big-box space by international tenants has not eased, with sporting goods retailer Decathlon announcing its first Australian store of 3,800sqm opening in Sydney’s inner west. There is also German supermarket Kaufland searching for a site up to 20,000sqm.

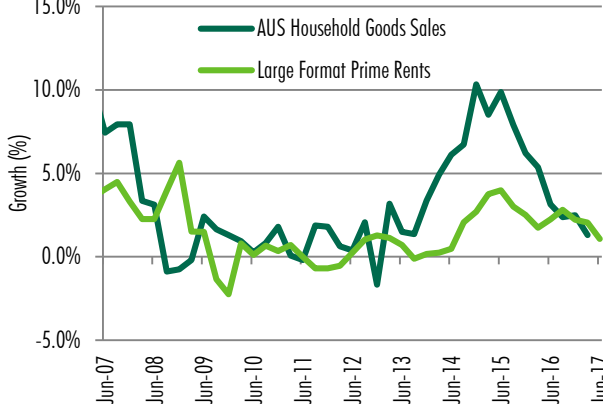
Figure 15: Large Format Retail Key Metrics



Source: CBRE Research, Q2 2017.

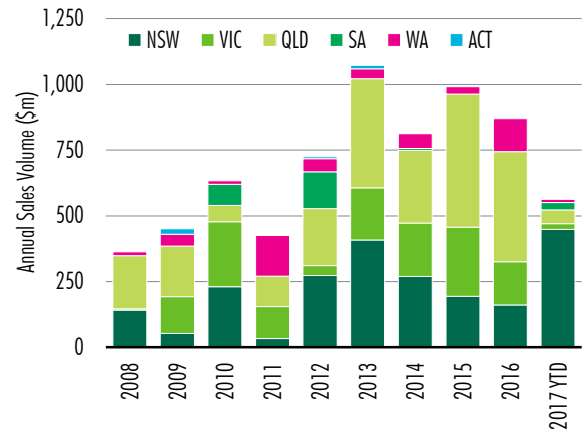
# Large Format Retail Dashboard

Figure 16: Large Format Retail Rents and Household Goods Sales



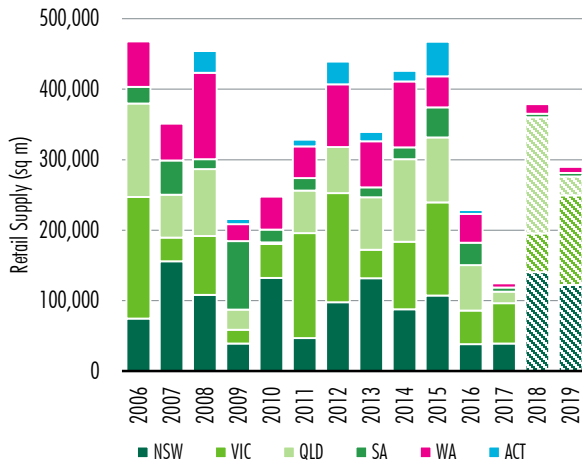
Source: ABS, CBRE Research, Q2 2017.

Figure 18: Large Format Retail Transactions by State



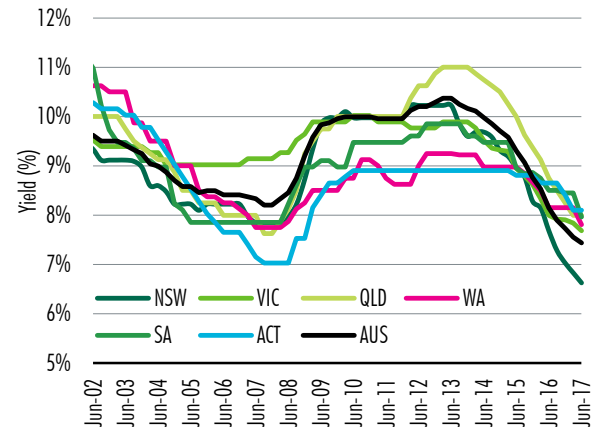
Source: CBRE Research, Q2 2017

Figure 17: Large Format Retail Supply by State



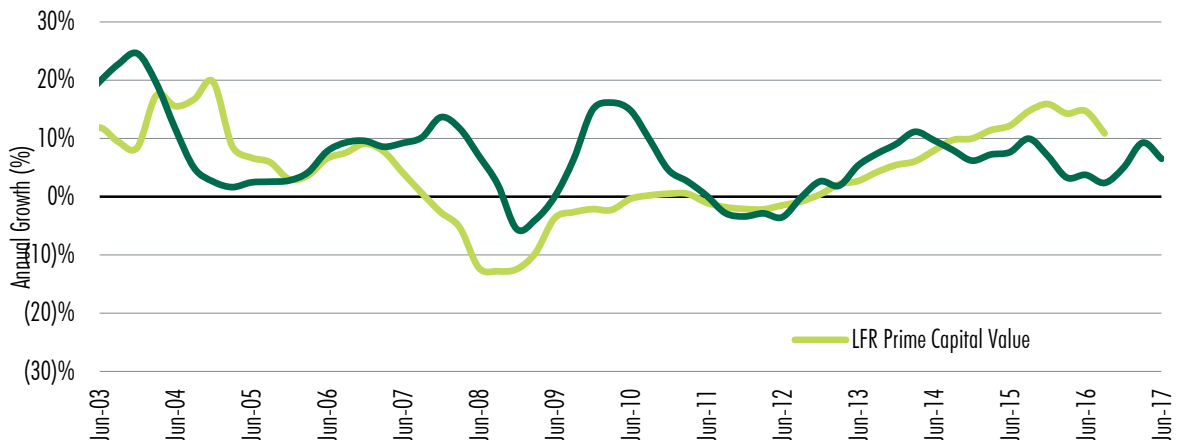
Source: CBRE Research, Q2 2017.

Figure 19: National Large Format Retail Prime Yield by State



Source: CBRE Research, Q2 2017.

Figure 20: National Prime LFR Capital Value Growth vs. National Median House Price Growth (nine month lag on capital values)



Source: CBRE Research, Q2 2017.



**Figure 21: Sales Transactions over \$5m in Q2 2017**

Building Name	Suburb	State	Retail Type	Sale Price (\$m)	Initial Yield (%)	Sale Date
Home Hub Castle Hill	Castle Hill	New South Wales	Large Format	\$ 336.0	5.50%	May-17
Salamander Shopping Centre	Salamander Bay	New South Wales	Sub Regional	\$ 174.5	6.00%	May-17
Home Hub Marsden Park	Blacktown	New South Wales	Large Format	\$ 100.0	6.00%	May-17
Arena Shopping Centre	Officer	Victoria	Neighbourhood	\$ 48.1	5.38%	Apr-17
Worongary Town Centre	Worongary	Queensland	Neighbourhood	\$ 46.3	6.00%	Jun-17
Century City Walk	Glen Waverley	Victoria	Neighbourhood	\$ 45.0	-	May-17
Wodonga Plaza	Wodonga	Victoria	Sub Regional	\$ 43.5	-	Jun-17
Highfields Village	Highfields	Queensland	Neighbourhood	\$ 41.0	6.00%	Jun-17
Mudgeeraba Market & Franklins Square	Mudgeeraba	Queensland	Neighbourhood	\$ 35.8	6.10%	May-17
Park Village Shopping Centre	Middle Park	Queensland	Neighbourhood	\$ 35.2	6.47%	Jun-17
Muswellbrook Marketplace	Muswellbrook	New South Wales	Sub Regional	\$ 34.3	6.70%	Apr-17
Terrace Central	Raymond Terrace	New South Wales	Neighbourhood	\$ 33.5	6.60%	Jun-17
Eli Waters Shopping Centre	Eli Waters	Queensland	Neighbourhood	\$ 33.2	6.30%	Jun-17
Hastings Central Shopping Centre	Hastings	Victoria	Sub Regional	\$ 32.1	6.20%	Apr-17
Gladstone Square	Gladstone	Queensland	Neighbourhood	\$ 31.5	7.25%	Jun-17
Renmark Square	Renmark	South Australia	Neighbourhood	\$ 30.1	-	May-17
Bunnings South Mackay	Paget	Queensland	Large Format	\$ 28.5	5.96%	May-17
Piazza on the Boulevard	Surfers Paradise	Queensland	Strip	\$ 22.0	5.00%	Jun-17
Lisarow Plaza	Lisarow	New South Wales	Neighbourhood	\$ 21.0	-	Apr-17
50 Hastings Street	Noosa Heads	Queensland	Strip	\$ 21.0	5.98%	Jun-17
19-21 Douglas Parade	Williamstown	Victoria	Strip	\$ 20.0	4.70%	Jun-17
Gunnedah Shopping Centre	Gunnedah	New South Wales	Neighbourhood	\$ 18.2	7.30%	Jun-17
Fitness First Bayside	Cheltenham	Victoria	Stand Alone	\$ 17.6	6.80%	Apr-17
Baxter Central Shopping Centre	Baxter	Victoria	Neighbourhood	\$ 16.6	5.60%	May-17
168 Willoughby Rd	Crows Nest	New South Wales	Strip	\$ 16.0	5.00%	Apr-17
Bunnings	Bendigo	Victoria	Stand Alone	\$ 14.5	6.00%	Apr-17
Rutherford Shopping Centre	Maitland	New South Wales	Neighbourhood	\$ 13.8	7.30%	Jun-17
Woolworths Brunswick	Brunswick	Victoria	Strip	\$ 13.5	4.80%	Apr-17
Woolworths Maryborough	Maryborough	Queensland	Stand Alone	\$ 13.0	5.90%	May-17
178-180 Bay Street	Port Melbourne	Victoria	Strip	\$ 13.0	5.73%	Jun-17
Tanilba Bay Shopping Centre	Tanilba Bay	New South Wales	Neighbourhood	\$ 12.6	7.30%	Jun-17
Woolworths Highton	Highton	Victoria	Stand Alone	\$ 12.4	4.70%	Apr-17
549-555 Gympie Road	Kedron	Queensland	Large Format	\$ 12.1	6.35%	May-17
137 George Street	Beenleigh	Queensland	Large Format	\$ 11.7	-	Jun-17
Walkerston Village Shopping Centre	Walkerston	Queensland	Neighbourhood	\$ 11.6	7.01%	Jun-17
Centrepoint Shopping Centre	Innisfail	Queensland	Neighbourhood	\$ 10.3	7.28%	Jun-17
Urban Village Cannon Hill	Cannon Hill	Queensland	Strip	\$ 9.1	5.66%	Apr-17
IGA Yarrabilba	Yarrabilba	Queensland	Strip	\$ 9.0	6.50%	Jun-17
38-42 Burns Bay Rd	Lane Cove	New South Wales	Strip	\$ 8.9	-	Jun-17

Source: CBRE, RCA, Q2 2017.

\* Note: Table sorted by sale price in descending order.

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