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Supply/demand imbalance underpins the lower end of the Melbourne CBD commercial market

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The sub $10 million investment market in the Melbourne CBD has emerged as one of the most resilient sectors of the Victorian commercial sector according to a new market analysis from CB Richard Ellis.

CBRE Associate Director, City Sales & Retail Investment Properties, Mark Wizel said a supply/demand imbalance had emerged during 2009, with only a handful of sub $10 million assets listed for sale in the CBD.

One of the most notable properties was the Church of Scientology Building, located on the corner of Russell Street and Flinders Lane. Mr Wizel said the current sale campaign was expected to generate a price in excess of $7.5 million and there had been strong interest from investors.

“The lack of available stock is underpinning the CBD market, as owners opt to hold rather than sell,” Mr Wizel said.

“With very few cranes on the skyline, we see rising unemployment as the most serious threat to the CBD. However if the vacancy rate remains at a reasonable level, we assume that values will not drop significantly for properties in the sub $10 million bracket, given the current level of buyer demand.”

CBRE’s market analysis highlights two very different stock patterns in the CBD during 2009.

While very little stock has been offered at the lower end, there has been a considerable volume of larger stock offered by institutional owners.

Mr Wizel said the current low CBD vacancy rates for residential, retail and commercial properties were helping to underpin the lower end of the market.

“Whilst there is no doubt that increasing pressure is being applied to retailers ability to pay record rentals, the CBD retail market has been quite resilient, helped in part by the CBD’s growing residential market and rising student population,” Mr Wizel said.

Figures from Melbourne Council show the population in the City of Melbourne (referred to as “usual residents”) rose from 50,673 in 2001 to 85,800 in 2009.

“In recent years there has also been a noticeable increase in the number of international students calling the Melbourne CBD home,” Mr Wizel said.

“This has resulted in a groundswell of retail tenants wanting to either establish stores in the CBD or expand existing retail concepts into other city locations.”

Mr Wizel said the increased population and retail spend in the CBD had helped underpin strong results on the sale of a number of smaller retail properties during 2009.

”We have seen a number of properties sell on tight yields and at high rates per square metre,” Mr Wizel said.

“This was evidenced recently with the sale of two Flinders Lane retail outlets which transacted at $17,500 and $23,045 per square metre respectively.”

While CBRE’s market analysis acknowledges that tougher economic conditions will have an impact om the city market, Mr Wizel said the current cycle was fundamentally different to the early 90s downturn, given the lack of new construction occurring in the CBD.

“There is currently no speculative development occurring in the CBD, in direct comparison to the 1990-1993 recession when a staggering 200,000 square metres of speculative office space was under construction,” Mr Wizel said.

“At that time 101 Collins Street, 120 Collins Street, 530 Collins Street, 350 Elizabeth Street and 600 Bourke Street were all being built, with very limited tenant commitments. This fuelled a significant increase in the CBD vacancy rate to almost 27% and in turn we saw some secondary properties being sold at one-third of replacement cost, ultimatley for conversion to residential developments which in turn was the catalyst for CBD residential living.”

With very limited new office supply coming online between 2009 and 2011, CBRE’s market analysis highlight predicted rises in unemployment as well as an increased amount of sub lease spacing hitting the Melbourne CBD office market as the most obvious threats to the CBD property sector.

In terms of different market segments within the CBD, the analysis highlights the western sector as one of the most improved performing sectors as a result of major infrastructure developments such as the Southern Cross railway station and the ever evolving development of the Docklands precinct.

Mr Wizel said the vacancy rate in the western sector was circa 6.3%, with the Rialto building having a zero vacancy rate.

“Developers have recognised the emergence of the western sector, with APN and Leighton acquiring 567 Collins Street, Mirvac purchasing 664 Collins Street and ISPT/Pivot acquiring the former Age site to accommodate a mixed use development including retail, residential and office space and there is little doubt that users of such space agree.

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