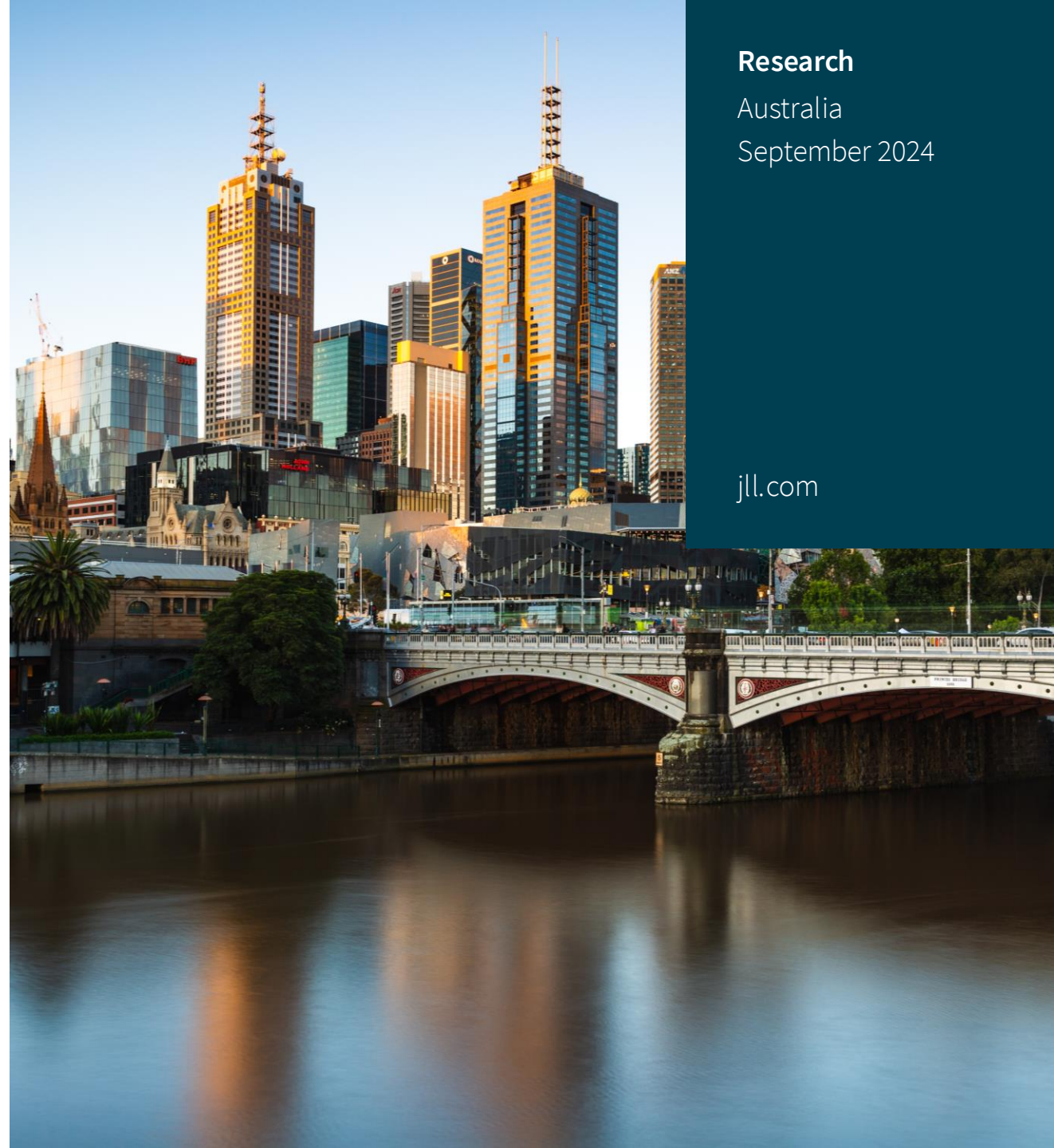


Report

The 'Real' Melbourne market narrative

Behind the headlines – understanding the nuances, the
opportunities and challenges

 **JLL** SEE A BRIGHTER WAY



Research

Australia

September 2024

jll.com

“

Kate Pilgrim

Market conditions have been tough, but opportunities and value are emerging. Melbourne’s underlying fundamentals are strong with liveability, affordability and population growth supporting demand.

Annabel McFarlane

The outlook for Melbourne is increasingly positive, and as the capital market value trough approaches, investors are looking to market growth fundamentals.

However, a nuanced approach and strategic thinking is required. Different real estate sectors – are being influenced by different supply and demand dynamics. Investor allocations to industrial and residential remain strong. However, Melbourne’s office and hotel markets completed significant supply cycles in recent years. Demand is selective and focused on the best spaces in the best places.

We are already seeing pricing tension for the best assets and the best locations, and this will support greater income growth and transaction liquidity in coming years.





Executive Summary

- **Melbourne is one of the most liveable cities in the world and has one of the strongest population and GDP growth projection combinations** of any city in a global top 15 economy. Melbourne's resident population is expected to increase by more than ½ million by 2028 i.e similar numbers to New York. For context Sydney and Brisbane are expected to increase by circa 300,000 sqm. Population growth could create 550,000 sqm of demand for office, 2.6 million sqm of industrial over the next five years and the need for more than 200,000 new dwellings.
- **Liquidity is starting to pick up, Melbourne has remained resilient despite VIC state tax changes.** Early movers, including Australian super funds, syndicators and private capital believe the market is bottoming out. For example, Bayley Stuart's acquisition of 628 Bourke Street with a 36% discount to previous acquisition price and PAG buying 367 Collins Street with a 27% discount to peak book value. Offshore investor pricing is less impacted by tax changes for office than industrial given other pricing metrics. Ultimately, it will be difficult to ignore Australia's largest industrial and CBD office markets.
- **Melbourne's CBD office market has had to absorb a 12.2% net increase in office stock since 2020.** No other CBD market has had to absorb such an increase through a pandemic. However, whilst vacancy is very high, good quality options are very limited, and a cohort of East End assets are achieving positive effective rental growth. Melbourne's office sector reset is largely complete with the largest 15 corporates having right-sized since 2020, although the VIC state government is yet to complete its right sizing process. Smaller groups (1,000 sqm to 5,000 sqm) are more likely to expand than contract. 10% (38) of assets account for 63% of vacancy. Structural vacancy is concentrated in assets built or refurbished before 2015 in Western Core and Docklands.
- **Melbourne's industrial market is Australia's largest but also its most affordable.** Melbourne's West prime net face rents are 34% lower than in Sydney's Outer Central West and are being considered by Sydney based 3PLs for their national distribution centres. Melbourne South- East industrial market has the lowest vacancy in the country with limited land availability restricting future supply. Melbourne has major road, rail transport infrastructure, Australia's largest port (Port of Melbourne) and airfreight hub (Melbourne Airport).
- **While there is more BTR stock under construction in Melbourne than other markets, it is not enough to offset the decline in BTS supply** and will likely provide only limited relief to the rental market. The residential rental market remains tight, and rents continue to grow. Further, most of the BTS pipeline remains focused on smaller premium stock for downsizers and will also provide little supply relief for renters. Despite the challenges the market still faces, developers are buoyed by Melbourne's strong population growth and are still optimistic about medium-term prospects.
- **Melbourne's hotel market has recovered ahead of expectations and hotel ADR accelerated beyond pre-COVID levels, as occupancy steadily recovers.** This is a significant achievement given Melbourne's hotel market has absorbed more than 5,000 new hotel rooms since 2020, a 24% increase in hotel stock through the pandemic. Ongoing recovery is being supported by improved inbound visitation and airlift capacity, recovering corporate/MICE (meetings, incentives, conferences and exhibitions) demand, as well as strong ongoing leisure demand for Melbourne's significant major events calendar.

Melbourne Fundamentals

1

Melbourne is one of the most liveable cities in the world. Supported by a world class health system and globally ranked hospitals and universities, Melbourne is known as Australia's cultural and sporting capital.

2

Melbourne's real estate is affordable relative to other capital city markets. Melbourne has lower dwelling prices than Sydney, Brisbane, Canberra, Perth and Adelaide. Office rents are lower than Sydney and Brisbane. Industrial rents are the most affordable in Australia.

3

Melbourne has one of the strongest population and GDP growth projection combinations of any city in a global top 15 economy. Greater Melbourne's population is expected to increase by over half a million people over the next five years and become Australia's largest city later this decade.

4

Victoria, like NSW and ACT is decarbonising rapidly. Victoria has made rapid emissions reductions, increasing to 40% renewable electricity generation by combining both emission reduction in non-renewable fuels and increases in renewable fuel production.





Melbourne market fundamentals

1

Melbourne is the world's 4th most liveable city (2024) according to the EIU's latest Global Liveability Index. Three European cities, Vienna, Copenhagen and Zurich are ranked ahead of Melbourne which is Australia's most liveable city ahead of Sydney (7th). Notably, Melbourne has **recovered its position from 9th and 10th in 2021 and 2022**, respectively.



2

..and is the 5th best student city in the world in the QS Best Student Cities 2025 QS World University Rankings. Melbourne is ranked behind London, Tokyo, Seoul and Munich and ahead of Sydney (6th). Paris, Zurich, Berlin and Montreal round out the top 10.



3

Two of Melbourne's universities are ranked in the global top 100. The University of Melbourne is ranked as Australia's best university (QS World Rankings: 13th and Times Higher Education: 37th). Monash University is Melbourne's 2nd ranked university and in the top 100 of global rankings, alongside University of Sydney, UNSW and UTS in NSW, ANU in Canberra, University of QLD, University of Adelaide and University of WA.





Melbourne market fundamentals

4

Melbourne is known as Australia's Cultural and Sporting Capital. A year-round calendar of events

- Australian Tennis Open
- Australian Grand Prix
- AFL football season
- Touring Broadway shows, and exhibitions
- Major Music Concerts
- The Melbourne Cup
- Ashes Cricket
- Events, festivals and Restaurant Culture
- Late night hospitality & all-night public transport



5

Three of Australia's six global top 250 ranked hospitals (2024) are in Melbourne.

The Royal Prince Alfred Hospital in Sydney (#56) and The Alfred in Melbourne (#97) are Australia's top ranked hospitals. The Royal Melbourne Hospital – Parkville (#102) and St Vincent's – Fitzroy (#189) are also in the global top 250. Source: Newsweek & Statista



6

Lower dwelling prices and unit rents than Sydney, Canberra and Brisbane. The average price of a Melbourne standalone house is below equivalent properties in Sydney and now in other states for the first time. Vic land tax increases for investment properties, in addition to the 425-basis point increase in the cash rate since May 2022 have made some mortgages unsustainable. However, affordability is a key driver of population growth and becomes an opportunity for new entrants.





Population and GDP growth is a driver of occupier demand for most real estate assets classes

Brisbane and Melbourne have the strongest population growth projections of cities in major global economies with growth rates of 2.1% and 1.9% y-y on average over next 5 years. Melbourne’s economic performance over the next 5 years is expected to be second only to Delhi in this cohort, with Brisbane and Sydney slightly behind Chinese cities.

Population growth is a key driver of residential and industrial markets and offsets weaker post-pandemic demand for office assets.

In terms of actual people, Melbourne is expected to accommodate an additional residential population of over 523,730 by 2028 (+9.7%). By 2029, Melbourne is expected to be Australia’s largest capital city at 5.9 million people.

The populations of Brisbane and Sydney are projected to increase by 318,910 (+5.7%) and 292,600 (+10.5%) respectively. For context New York’s will increase by 554,330 sqm (3.8%).

Selected global cities GDP and Population average annual change 2024 to 2028



Source: JLL Research, Oxford Economics



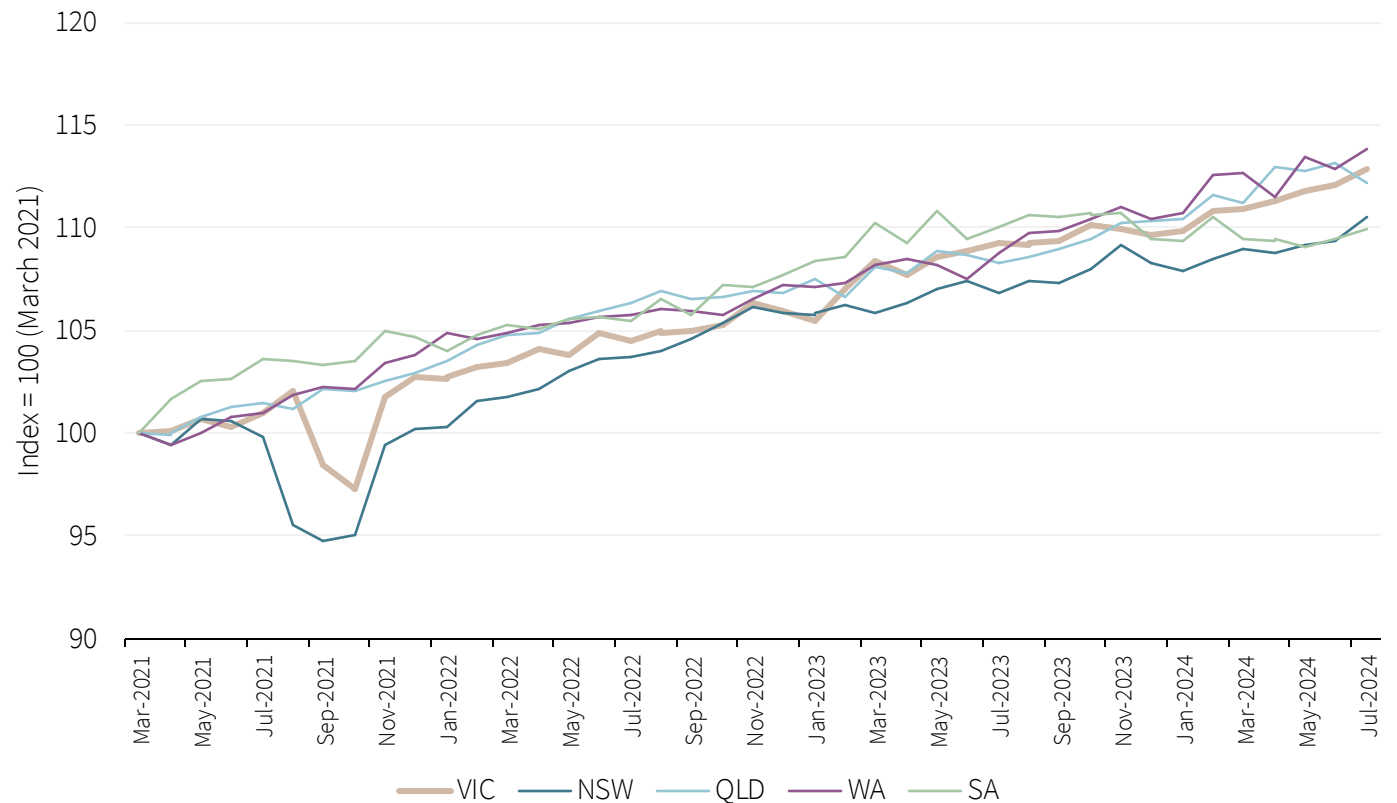
Victoria’s post-COVID-19 labour market recovery has outpaced most other states in Australia

Australian Bureau of Statistics (ABS) data shows that Victoria’s labour force growth has been one of the strongest nationally over the past three and a half years.

Over this period, the number of people employed in the state has risen 12.9%, compared to the national average of 11.7%. Victoria’s workforce participation rate reached a record high of 68.3% in July 2024, exceeding the national average and further demonstrating the strength of state’s labour force.

Post-COVID-19, employment growth in Victoria has seen a notable shift towards full-time and permanent positions. ABS data from July 2024 shows 68.8% of Victorian workers in full-time roles, a 1.3 percentage point increase from three years earlier. These figures underscore the robust recovery and evolution of Victoria's labour market.

Post-COVID-19 labour market growth – major Australian states



Source: JLL Research, ABS

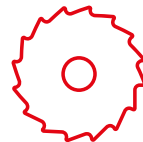


Victoria's workforce is one of the most educated in Australia, including being competitive across other APAC jurisdictions



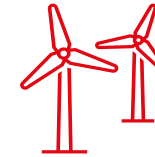
Digital technology

Victoria, along with New South Wales, stands at the forefront of Australia's digital technology landscape. The Department of Jobs, Skills, Industry and Regions' 2023 ICT Sector Fact Sheet reported 271,000 technology professionals employed statewide, including a third of the country's software engineers. The state surpasses other APAC jurisdictions, including Hong Kong, in terms of software development and cloud computing.



Manufacturing

Australia's manufacturing sector heavily relies on Victoria. Based on Australian Bureau of Statistics data, the state not only employs the highest number of manufacturing workers nationwide, but also has the strongest share of manufacturing employment (7.7% of total employment) among all major Australian states.



Renewable energy

Victoria's new energy sector talent pool is expanding rapidly. According to Victorian State Government investment attraction agency, Invest Victoria, the state ranks second in Australia for skilled professionals in renewable energy, sustainability, and agrifood technology.



Health and Life sciences

The Department of Jobs, Skills, Industry and Regions' August 2024 Health Technology update highlighted that Victoria's health and life sciences sector is rapidly growing, employing approximately 72,000 professionals statewide. Furthermore, health companies headquartered in Melbourne represent over 40% of Australia's publicly listed health technology businesses.



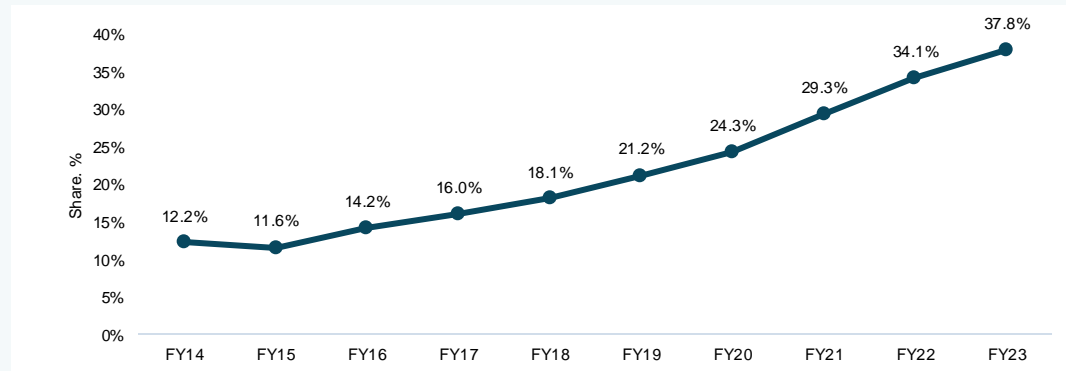
Victoria, like NSW and ACT is decarbonising rapidly

Decarbonisation of electricity grids is an indirect but important consideration for investors and occupiers of real estate markets. The availability of renewable energy from the grid is essential in the delivery of Net Zero Carbon Ready stock, particularly for assets that have limited space onsite to install solar PV, which is likely to be the case for most office assets.

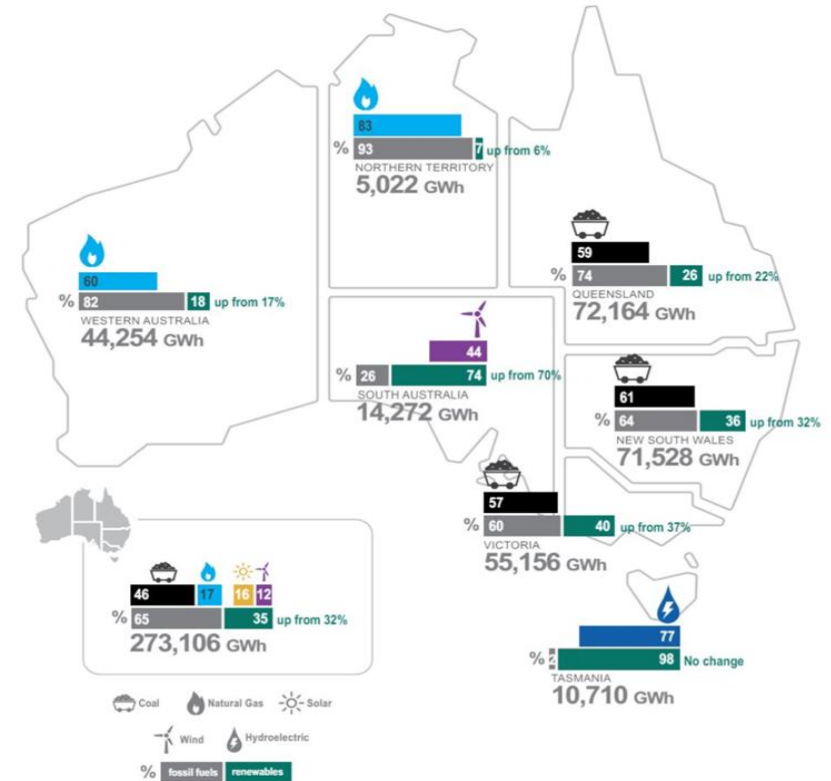
The Department of Climate Change Energy the Environment and Water (DCEEW) most recent update illustrates that Tasmania and

South Australia are leaders for their long-term emission reduction efforts. However, New South Wales and Victoria have made rapid emissions reductions, increasing to 36% and 40% renewable electricity generation by combining both emission reduction in non-renewable fuels and increases in renewable fuel production. Progress is also picking up in Queensland (26%), but since 2018, WA emission reduction efforts have been slow, and the NT's emissions have been rising.

Victorian renewable electricity generation share, 2013/14 to 2022/23



Australian Energy Statistics, Infographic April 2024



Source: JLL Research, Victoria State Government - Department of Energy Environment and Climate Action
 Australian Government - State and Department of Climate Change Energy the Environment and Water (DCEEW)

Capital market themes

1

Liquidity is starting to pick up.

Transaction volumes have totalled AUD 12.2 billion over the first six months of 2024, which is up on the first half of 2023 and indicative of improving volume for 2024. **Victoria has remained resilient**, attracting 18% of all volumes.

2

Have VIC State Government foreign owner and other tax changes already been priced in for office markets?

Since September 2023, the spread between Sydney and Melbourne Prime CBD office mid-point yields has widened by over 50 basis points, to 62.5 basis points in June 2024.

3

Despite the challenges associated with foreign owners' land tax, **foreign investors still deployed approximately AUD 500 million of capital into Victoria's industrial market** over the first six months of 2024.

4

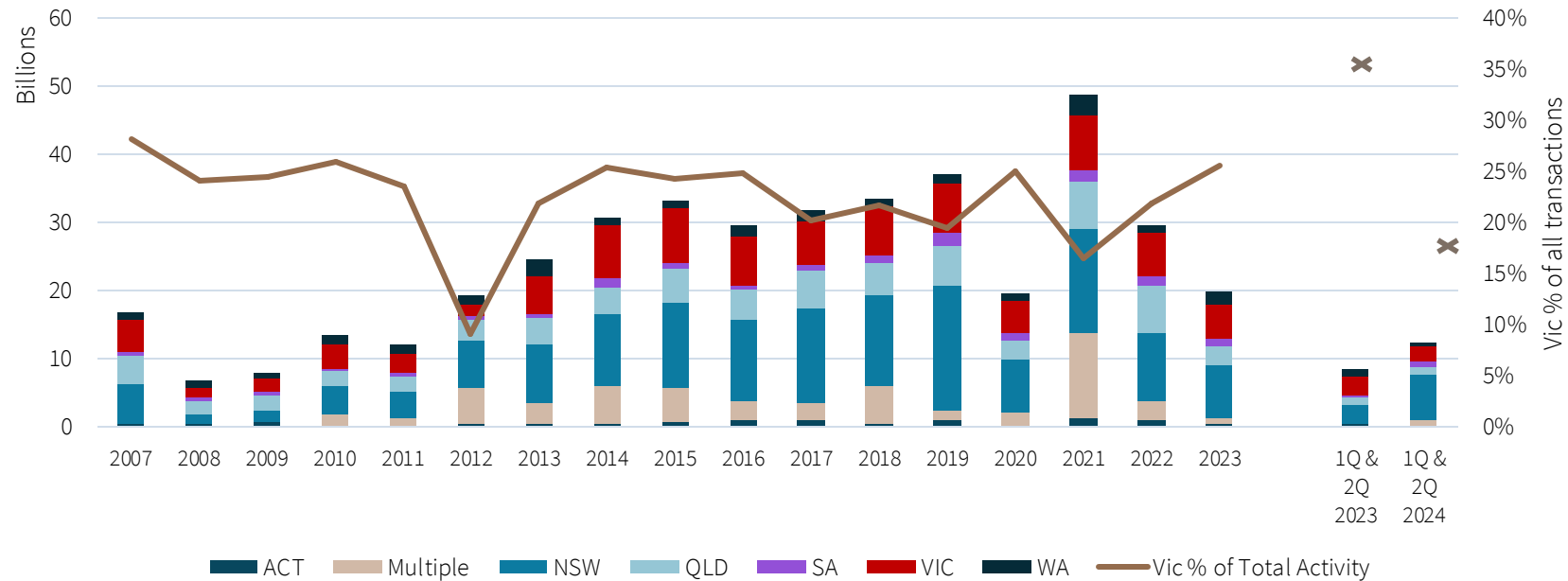
Catching the upswing: The cyclical upside. Previous cycles indicate that a period above average returns start the year after a correction. This bodes well for a **rebound in CBD office returns from 2025** as markets stabilise and confidence returns. Recent purchasers of Melbourne's CBD office assets indicate that early movers believe the market is bottoming out.



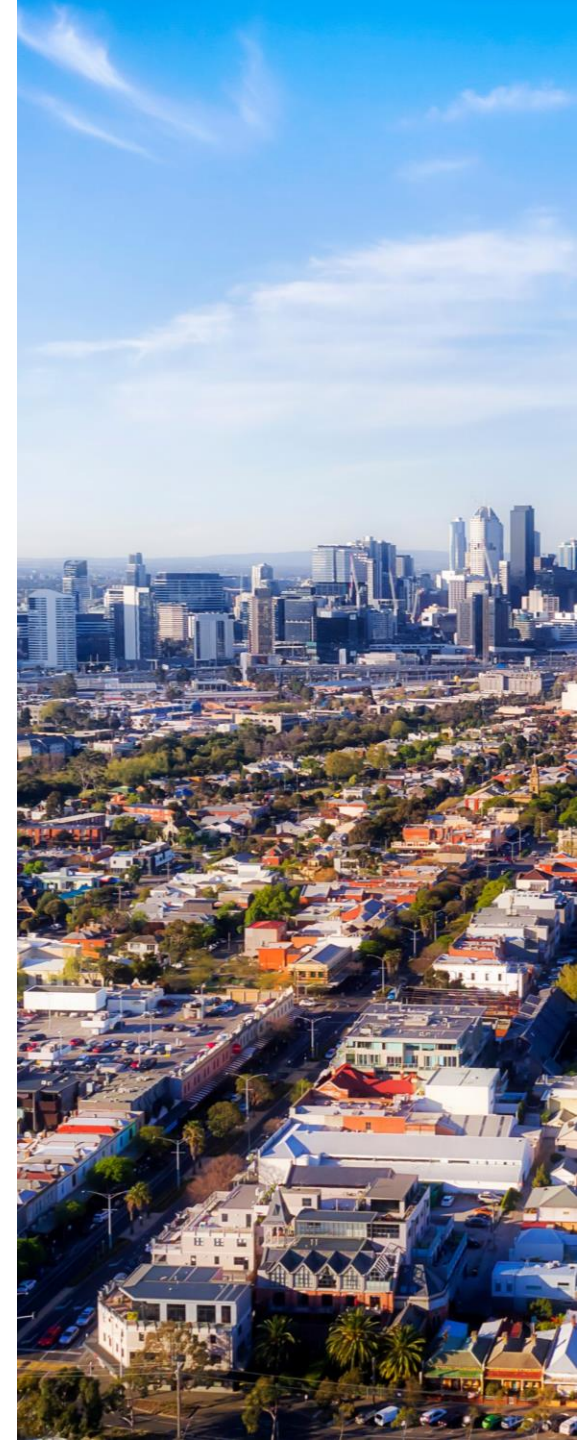
Transaction activity is starting to pick up

Australian real estate core sector transaction volumes totalled AUD 12.2 billion over the first six months of 2024, which is up on the first half of 2023 and indicative of improving volume for 2024. Victoria has remained resilient, attracting 18% of all volumes and 27% by count.

Core sector mid-point yields and real bond rates



Source: JLL Research





However, Victorian State Government recent tax changes create an additional investment headwind

From the 2024 land tax year, an **absentee owner land tax surcharge of 4% applies** to Victorian land owned by an absentee owner. The surcharge was 2% for the 2020 to 2023 land tax years, 1.5% for the 2017 to 2019 land tax years, and 0.5% for the 2016 land tax year.

VIC Commercial and Industrial Property Tax (CIPT) transition - **Stamp duty to be abolished**. From the 1 July 2024 Stamp duty will be paid one final time on the property if and when it is transacted. CIPT will be set at a flat 1% of land value ten years after the transaction. This strategy is unique to Victoria and the timing of transaction could positively or negatively impact returns depending on investment horizon.

In addition, Victoria introduced the COVID-19 Debt levy from 1 January 2024 for 10 years, a fixed charge up to \$975 for landholdings valued at less than \$300,000 and an additional 0.1% increase land tax rate for landholdings valued at more than \$300,000. (included in the max land tax rate of 2.65%). This follows the introduction of the Windfall Gains Tax in July 2023 applicable to value increases from government rezoning decisions.

Whilst most states have an absentee owner land tax surcharge applicable to residential land holdings, Queensland is the only other state where it is also applicable to all property types, and this was recently increased to +3% with effect from 30 June 2024.

Back of envelope calculations suggest a **significant negative impact on bid pricing from offshore investors** and capital sources at the revised 4% surcharge rate. The CIPT and COVID-19 levy adds a further layer of complexity and pricing uncertainty.

Office bid price impact

-6.8%

**38 basis points
softer yield**

Industrial bid price impact

-13.0%

**75 basis points
softer yield**



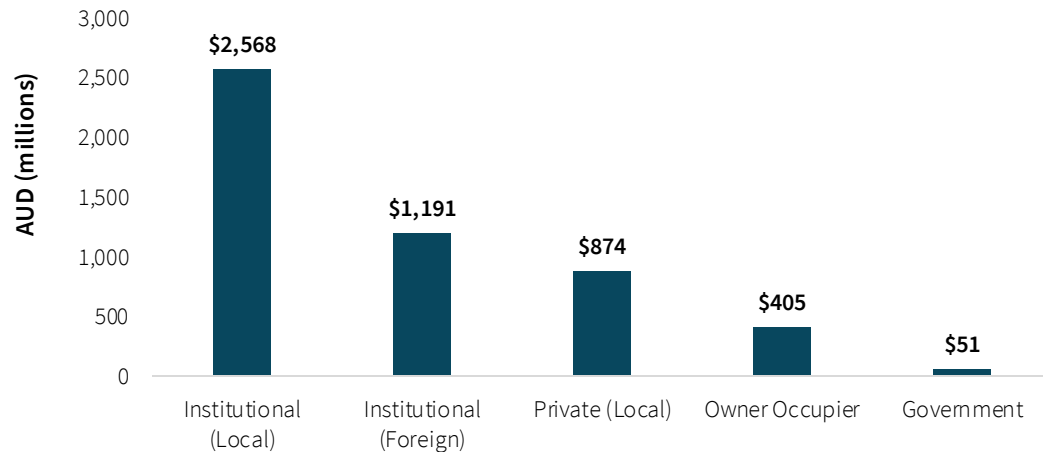
Victoria is still an investment destination, with over AUD \$2.2bn invested, and 66% weighting to logistics and industrial

Local buyers of industrial and logistics are the most active buyer in Victoria, led by Australian Superannuation Funds and locally domiciled private investors YTD 2024. Of the \$2.5bn sold by foreign investors nationally, a large portion of that (60%) originated in Victoria, indicating an ongoing rebalancing of portfolios and reduction of exposure to the market.

Despite the challenges associated with foreign owners' land tax, foreign owners still deployed approximately \$500mn of capital into Victoria, which is on par with the entire Queensland industrial volumes.

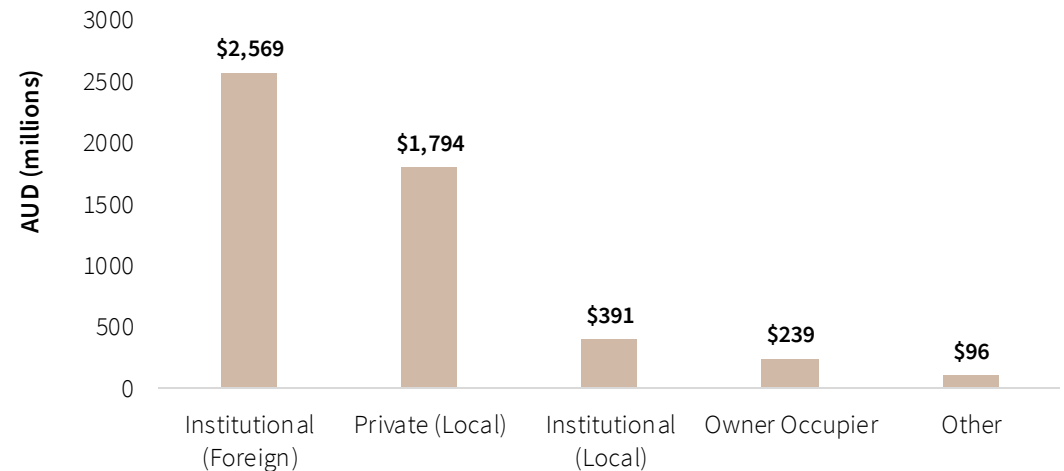
Rebalancing is underway

Top Logistics and Industrial Buyers YTD 2024



Source: JLL Research

Top Logistics and Industrial Sellers YTD 2024



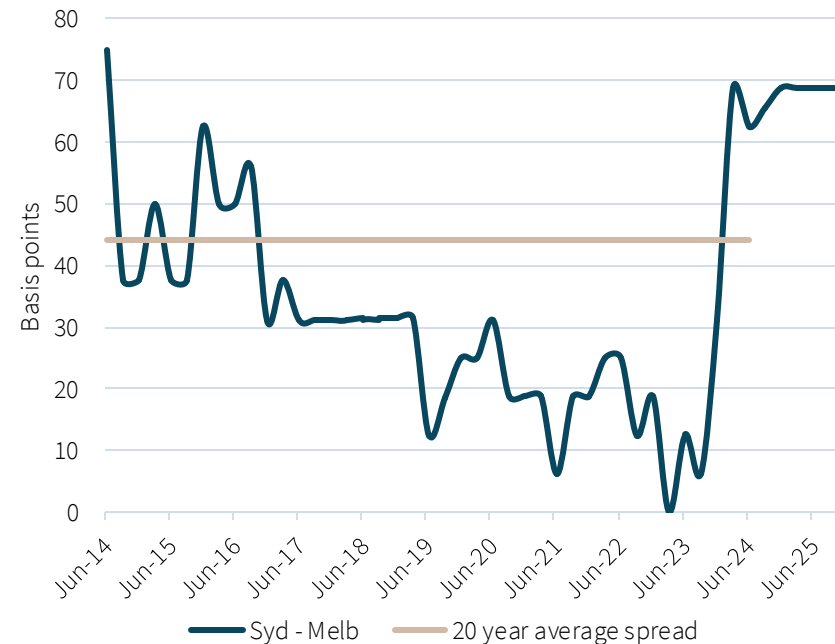
Have Victorian State Gov foreign owner and other tax changes already been priced in for office markets?

JLL research has tracked property market yields since the 1970's. Since September 2023, the spread between Sydney and Melbourne Prime CBD office mid-point yields has widened by over 50 basis points, to 62.5 basis points in June 2024. This is wider than the difference indicated by analysis of the foreign owner surcharge (38 basis – points) and suggests that other factors are at play.

In the past, offshore buyers have been able to accommodate the Victorian government foreign owner surcharges in pricing models for the right assets. This is illustrated by analysis of transaction buyer profiles through a period where a 2% Victorian absentee owner surcharge was applicable in 2020 to 2023 and compared to Sydney where the absentee owner surcharge applies to residential only. The % volume of offshore buyers for office assets in Melbourne was slightly higher at 41% than the 20-year average and the spread between Sydney CBD and Melbourne CBD office asset yields was 26 basis points narrower than the 20-year average, 44 basis points. However, recent activity suggests, in a challenging office investment landscape, the additional surcharge and other Victorian tax changes are having an impact, for offshore groups wishing to deploy capital in Victoria's real estate markets.

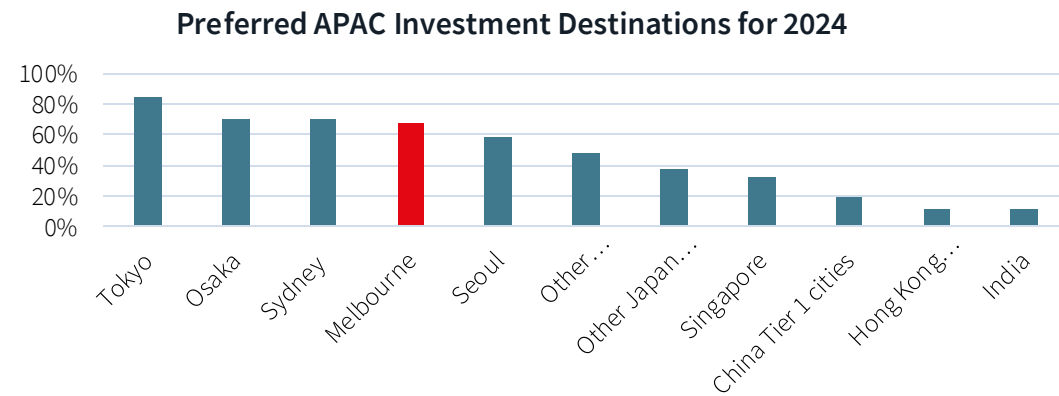
Source: JLL Research, ANREV

Sydney to Melbourne CBD Prime office mid-point yield spread



This presents as short-term opportunity for domestic capital and private investors

In early 2024 the ANREV survey of investor destinations again ranked Melbourne as a top 5 destination for global capital in the APAC region. Transparent real estate markets put the largest markets within Japan and Australia at the top of the list. Offshore groups are unlikely to stay out of Australia's largest /second largest real estate market depending on sector for long.



Source: JLL Research, ANREV





The cyclical upside.

Over 10 years and 15 years, Melbourne CBD office markets have outperformed with 8.8 total return CAGR compared to 8.1 and 7.8 respectively for all CBD office markets but has been more negatively impacted in this cycle.

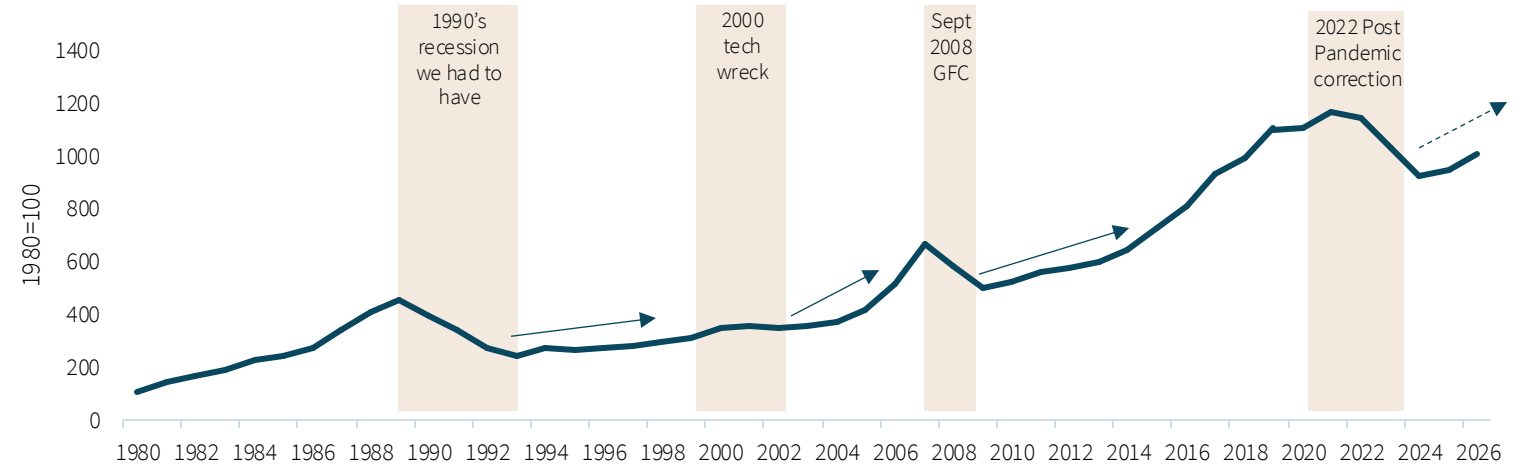
Previous cycles indicate that a period above average returns start the year after a correction. This was observed post GFC (2008) and post tech wreck (2000 to 2002).

11.5% and 9.7% total returns were achieved in the 5 years from December 2009 and December 2003 for Melbourne CBD office markets outperforming 10-yr and 15-yr returns. This bodes well for a rebound in CBD office returns from 2025 as markets stabilise and confidence returns.

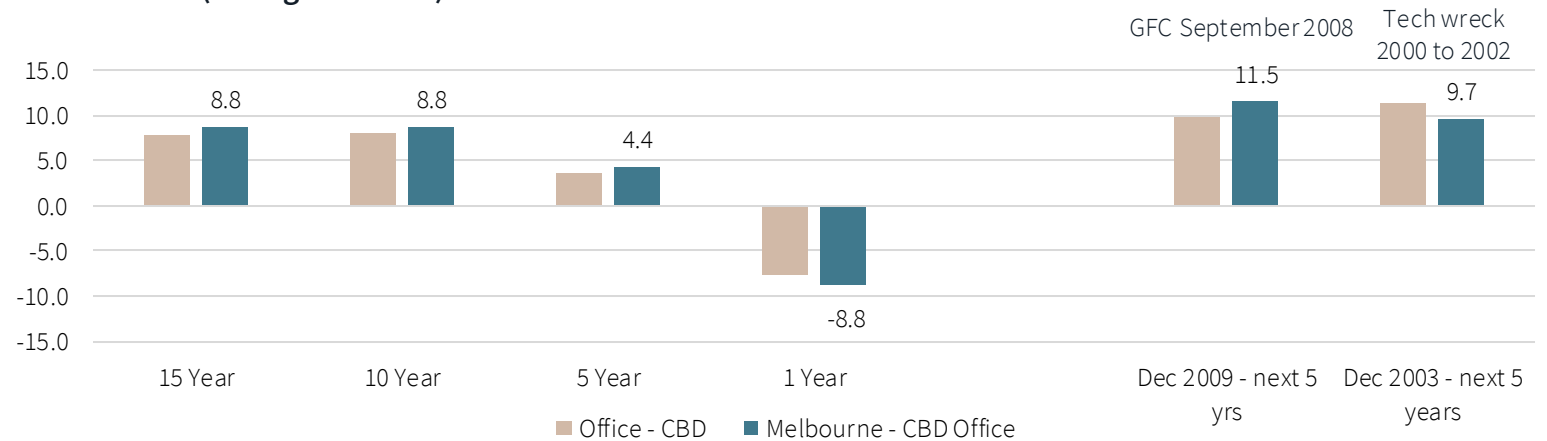
Catching the upswing: Recent purchasers of Melbourne’s CBD office assets indicate **early movers believe the market is bottoming out.** In June 2024, syndicator, Bayley Stuart bought 628 Bourke Street, Melbourne from AFIAA for \$115 million, a 36 per cent discount to the \$181 million the Swiss fund manager paid in 2017.

PAG (Singapore) buys 367 Collins subject to FIRB for \$300.0 million, a 27% discount to the December 2022 book value.

Australian CBD office capital value index



Total Returns (rolling annual %)



Office

1

Vacancy will remain at current high levels for the next 18 to 24 months. Melbourne's CBD office market has had to absorb a **12.2% net increase** in office stock since 2020. No other CBD market has had to absorb such an increase through a pandemic.

2

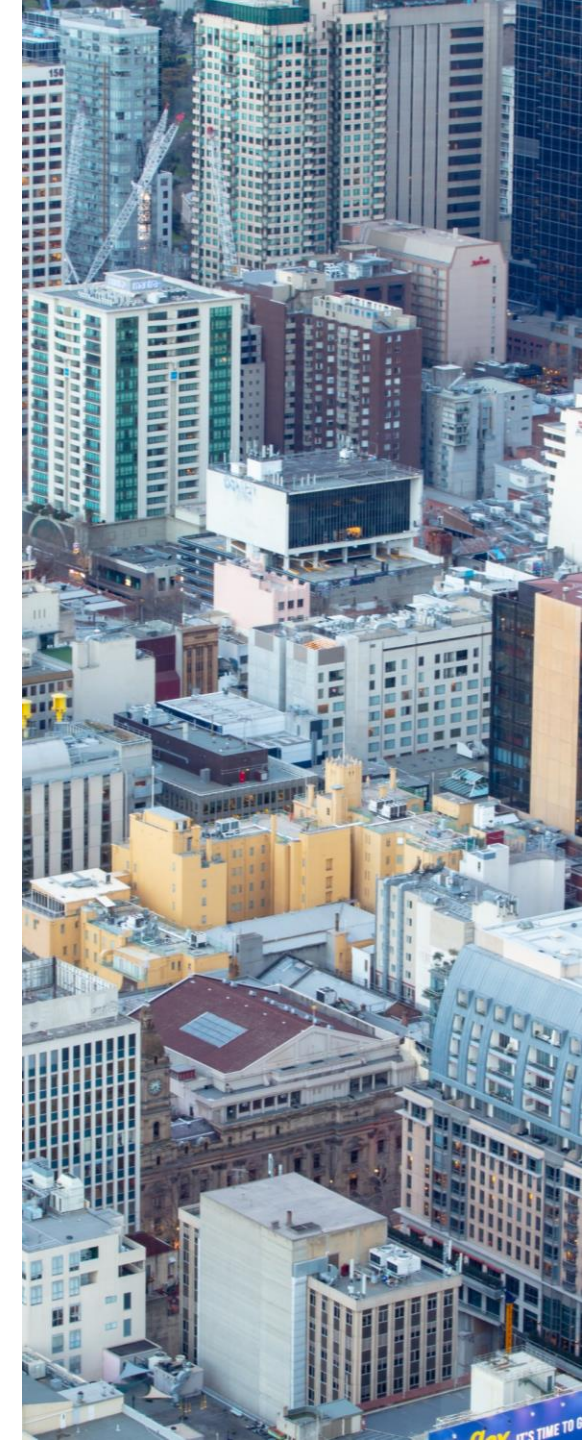
High vacancy but there are limited good quality options. 6 out of 12 current requirements in the market >5,000 sqm require strong sustainability credentials. There are **just 3 assets** in Melbourne's East end precincts with a NABERS 5.5* or 6* rating that can accommodate a >5,000 sqm tenant in current vacancy.

3

A cohort of prime grade assets are achieving **positive effective rental growth**. The **recovery is starting in Melbourne's Eastern Core** and rippling out to nearby precincts and down Collins Street.

4

The office occupier reset is largely complete. Population growth projections for Melbourne indicate potentially 550,000 sqm based on the current ratio of stock to population. **Over the last six months more tenants in the 1,000 to 5,000 sqm cohort have expanded than contracted.** However, the Victorian State Government is the last large occupier to review its occupancy.



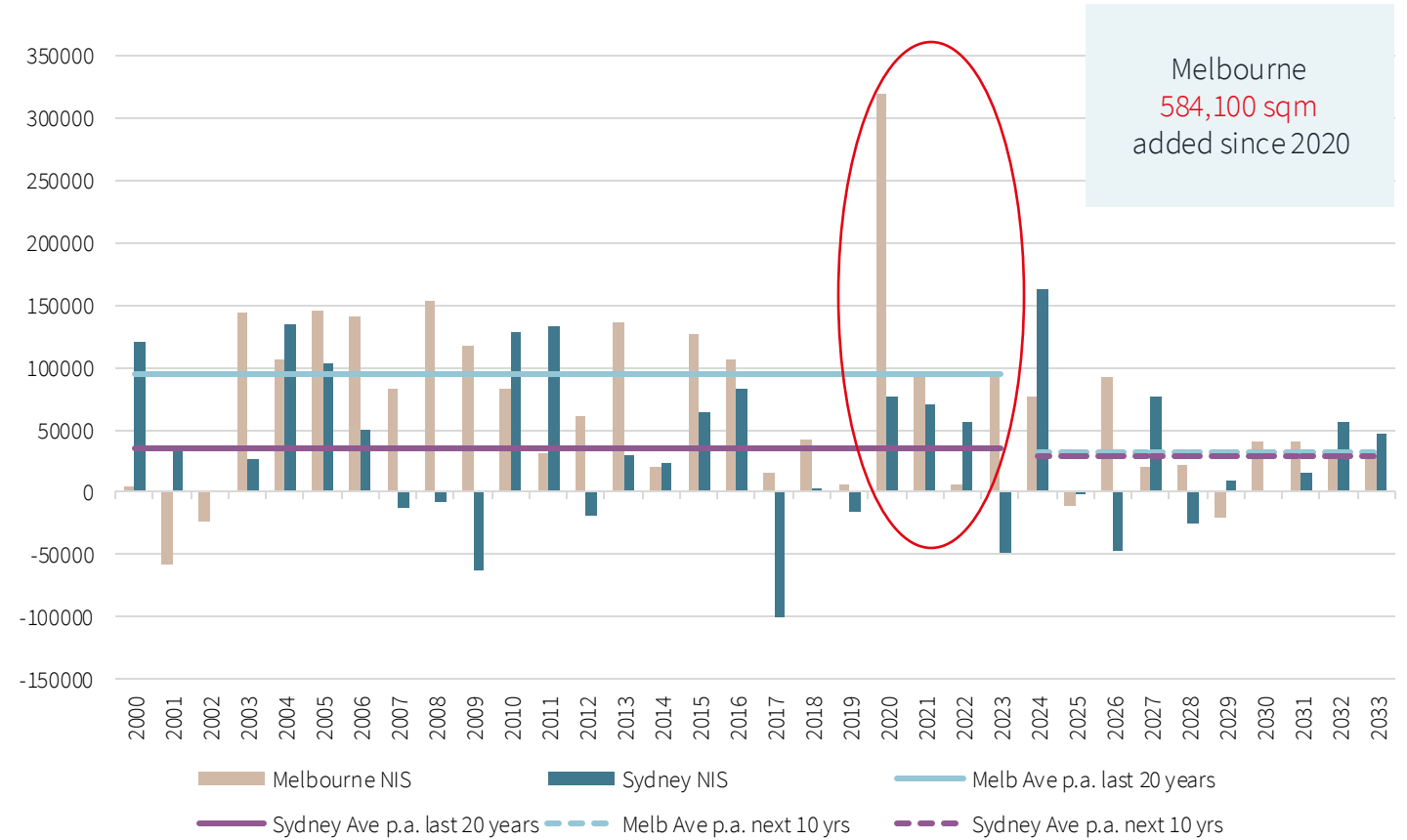
High vacancy in Melbourne’s office markets is not just a return to office story.

Melbourne CBD office market has added **584,100 sqm** in net increase in stock since 2020. That’s a **12.2%** increase in CBD stock since 2020.

No other market has had to absorb this level of supply activity through the pandemic. JLL research projects that Melbourne CBD office market vacancy (19.6%) will remain in the region **of current elevated levels through the next 18 months to two years** before contracting gradually from 2026.

From 2007 to 2019 Docklands accounted for 84% of Melbourne CBD Net increase in stock. However, key sites are largely built out and future development in the precinct will necessitate the withdrawal of office assets. Therefore, Melbourne’s supply profile is likely to be more like Sydney’s with increasing site amalgamations, office asset withdrawals and higher required economic rents are slowing future supply.

Figure 8:
Melbourne CBD and Sydney CBD office Net increase in stock 2000 to 2033



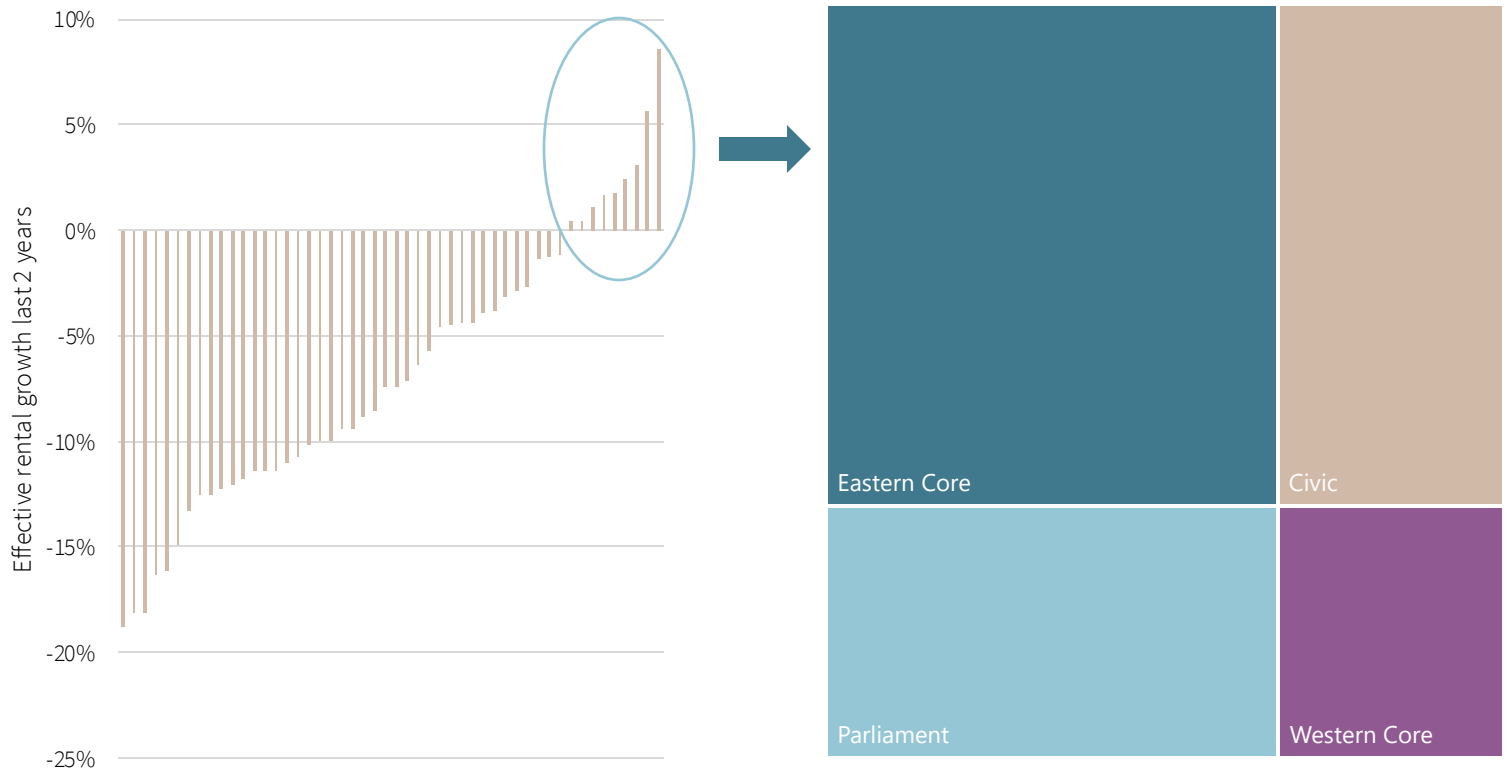
The office market recovery is starting in Melbourne's **Eastern Core**

18% of Melbourne's CBD Prime office assets achieved positive net effective rental growth over the last 2 years

Six of the nine assets in this cohort are on Collins Street with 101 Collins Street a notable example. There are more assets in Eastern Core that meet these requirements than any other precinct but there are examples rippling out to nearby precincts including Parliament and Civic with Olderfleet, 477 Collins Street the only Western Core example.

Source: JLL Research

Figure 8:
Melbourne CBD Office Prime Grade Effective Net Rental Growth by Individual Asset for the Past Two Years





High vacancy but how many good quality options?

Melbourne’s CBD vacancy is 19.6% as at 2Q24 and is the highest vacancy recorded in the CBD market since 1995. Prime grade vacancy is almost as high as secondary grade.

6 out of 12 current requirements in the market >5,000 sqm mentioned ‘**high sustainability** credentials’.

Tenants with requirements in the market are flooded with options but good choices are limited. There are 52 prime grade options in the CBD that can accommodate a 5,000sqm tenant requirement. However, just 11 options are in 5.5* & 6* CBD assets and only 3 of these are in East End (Parliament, E. Core & Civic precincts) Melbourne.

These assets few assets are all in the group recording positive effective rental growth.

Figure 3:
Space options are limited for good quality product in good locations

	Prime	5.5* & 6*	All Electric	East End (E.Core, Parliament Civic)	Collins Street Address	Number of Options	Comments
Number of Options >5,000 sqm	52	11	2	16	25		
Wish list 1	√	√	√	√	√	0	Only 2 completed CBD assets are electric base build, 500 Bourke Street and 101 Collins Street
Wish list 2	√	√		√		3	Only one on Collins Street
Wish list 3	√	√			√	5	Three are in Docklands
Wish list 4	√			√	√	7	Partnership with Landlord for sustainability upgrades

The only CBD assets to have completed the base build electrification process are 500 Bourke Street and the only asset in Melbourne’s East End precincts is 101 Collins Street and with very low vacancy, it’s unable to accommodate a requirement of this size.



The next tier down – where next for rental growth?

Rental pricing tension is driving a return to positive effective rental growth in the best assets. We have found that occupiers that miss out, need to decide between the best location amenity or the best building, guided by the following themes:

Human Centric Model – Cognisant of the appeal of location attributes to employees means that in most cases location will be preferred over building amenity when it's not possible to achieve both.

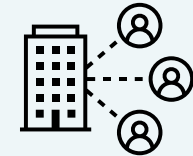
Partnership approach – The ability to work with a landlord on upgrades over time becomes very important and those developers and landlords with a track record of delivering agreed outcomes and timeframes will be favoured.

A more liberal approach to ESG – Whilst environmental sustainability remains increasingly important, with the absence of electrified or enough highly energy efficient stock in the market, tenants are working in partnership with landlords to achieve these aims over time rather than immediately, usually in conjunction with other building upgrades.



Best Core Location

OR



Best Building

Human Central Model

Tenant & Landlord Partnership

A more liberal approach to ESG



Melbourne’s office occupier reset is largely complete

The largest 15 CBD corporate occupiers have accounted for over -320,000 sqm net absorption since the start of 2020.

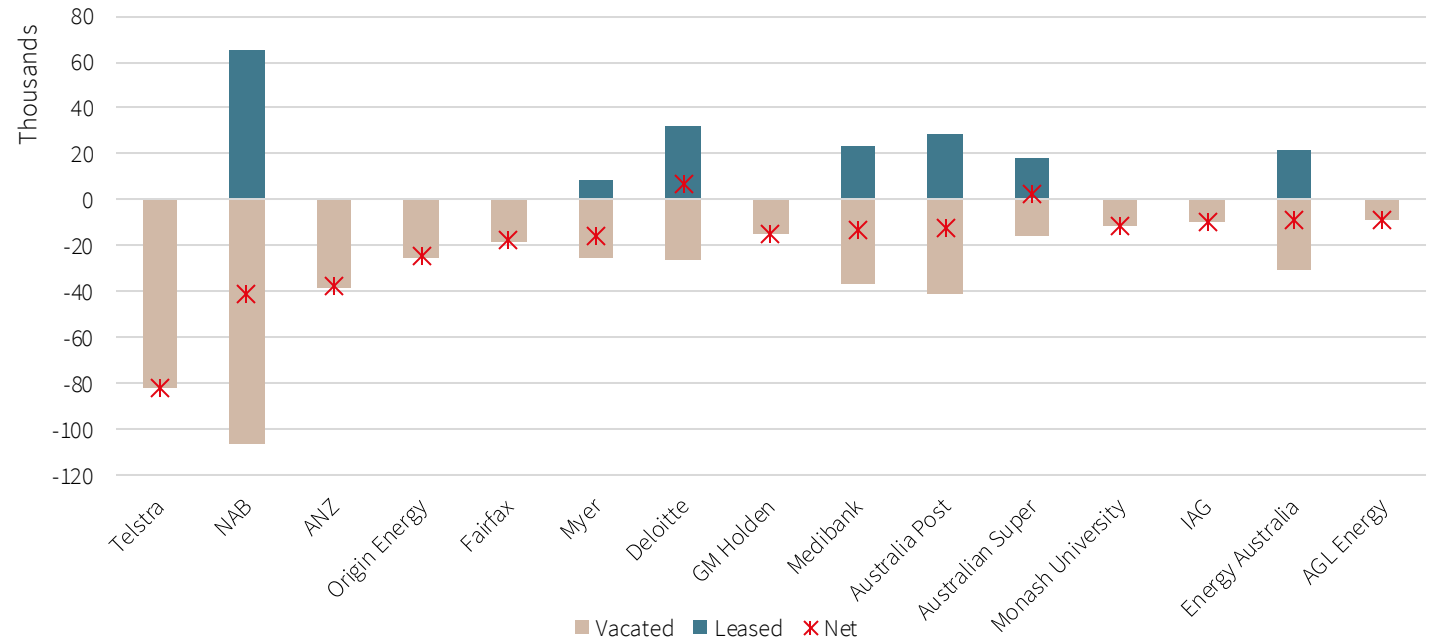
To put this in context, CBD net absorption for this period was -305,050 sqm, indicating that all other occupiers in the market had circa 15,000 sqm positive net absorption over this time.

Many of these groups have right sized with relocation, the decisions have been made and further moves are likely to be expansion or delayed until lease expiry. These include the following:

Right sizing with relocation

- Deloitte
- NAB
- Medibank
- Australia Post
- Energy Australia.

Figure 3:
Melbourne Largest 15 Occupiers – leasing activity 2020 to 2Q24

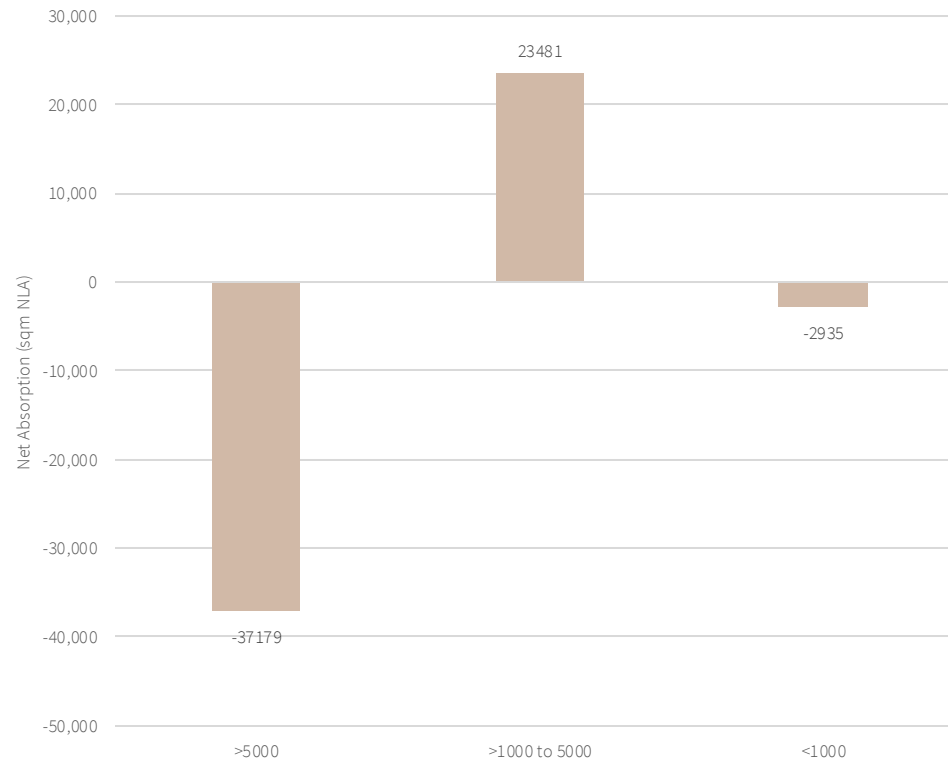


Which size cohorts are expanding?

Over the last 6 months 21 tenants in the **1,000 sqm to 5,000 sqm cohort expanded** and 19 contracted. The impact on net absorption was close to 23,500 sqm across Melbourne CBD, Fringe and Southeast Suburban (SES) office markets. While a few large tenants are having a greater impact on negative net absorption impact.

This bodes well for recovery in the market over the next 18 to 24 months.

Melbourne CBD, Fringe and SES Tenant activity 1Q & 2Q 2024 by size cohort (Net Absorption)

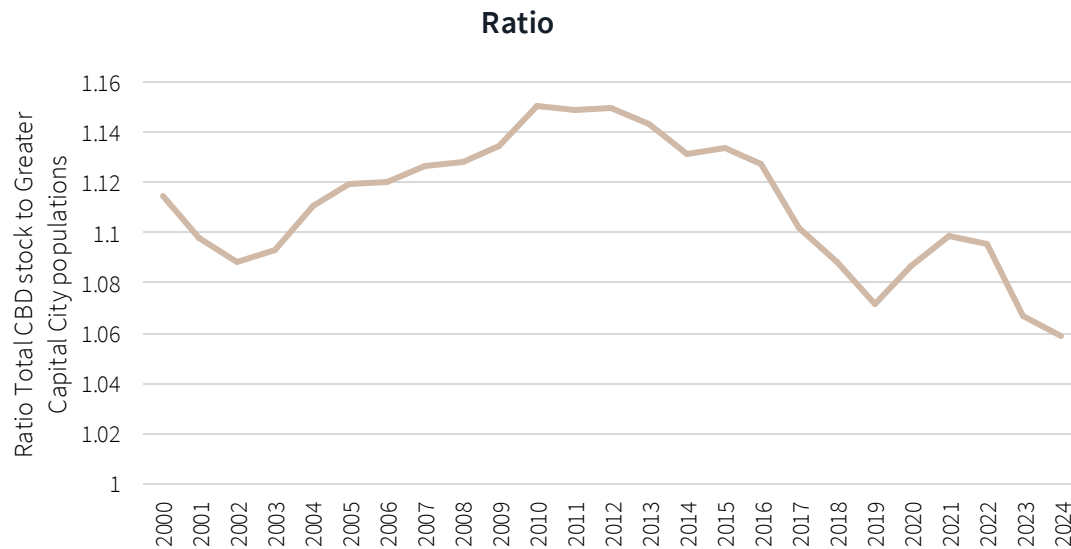




Population growth could drive demand return Melbourne’s CBD office market to equilibrium by 2028?

Equilibrium vacancy in Melbourne’s CBD office market is between 8.5% and 9.5%, 20-year and 15-year average vacancy is 8.8% and 9.4%, respectively. As at 2Q24 vacancy totals 1,052,600 sqm (19.6%). The ratio of greater capital city population to total office stock has reduced significantly over time as workplaces have changed moving from individual desks to activity-based working and more recently with the introduction of hybrid working.

As highlighted most corporates have completed their reset. If we assume the current ratio of 1.05 sqm of stock per person of total resident population Melbourne CBD office market could expect circa 550,000 sqm of demand over the next five years. Simple analysis shows that reducing current vacancy by 550,000 sqm would bring vacancy down to circa 502,600 sqm or 9.4% in line with long term average vacancy.



Source: JLL Research

Occupied stock, vacancy and population demand waterfall





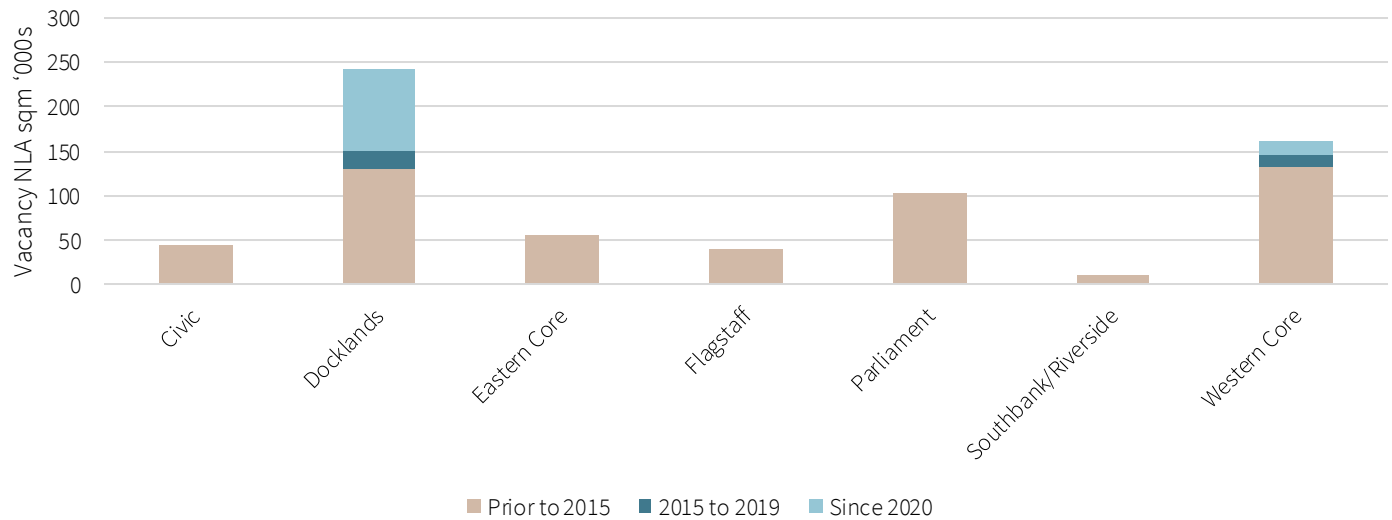
10% (38) of Melbourne CBD assets account for 63% of vacancy

These assets have the largest tranches of vacancy in them and therefore because of their scale, 33 of these 38 assets are prime grade office towers. 32 of them were built or refurbished prior to 2015. However, though these assets are represented across all Melbourne CBD precincts, there is also a clear weighting to Western Core and Docklands.

Can we define structural vacancy as assets **built / refurbished before 2015** in Docklands or Western Core?

Figure 3:

Location composition of 38 assets contributing to 63% of CBD vacancy



Vacancy in these 38 CBD assets

664,370 sqm

44.7% vacancy

Vacancy in remaining CBD assets

388,230 sqm

9.9% vacancy

What is the strategy for secondary or prime grade structurally vacant office assets?

Melbourne's CBD office market is expected to have vacancy at or around current elevated levels for the next 2 to 3 years. Market recovery has started with a cohort of assets in East end precincts and will broaden as the market recovers. However, some asset are at risk of structural vacancy, i.e unable to attract tenants even at very low rental levels.

There are several steps that owners of these assets can take to reduce risk, and strategies will vary for depending on location and physical attributes of the asset.

Valuation risk assessment

Obsolescence risk factors,
E.G current or approaching high vacancy and high % fossil fuel use, NABERS NR or <5.5 Stars

Leasing expiring assessment

E.G a lease expiring in 2025 /2026 in context with projected market conditions at time in terms of competing availabilities, forecast rents and incentives.

Upgrade cost assessment

Cost assessment for office upgrade including amenity and sustainability features. Assessment of development financing options including the opportunity to access green financing options for projects that include sustainably upgrades.

Adaptive reuse assessment

Hotels, Resi, BTR, Health & Education

Redevelopment and site amalgamation

Review site amalgamation opportunities. CBD sites that can deliver an office project of scale, with current set back rules typically need to be over 3,000 sqm, so additional value can be created by combining sites.

Sale potential

Melbourne's long term growth fundamentals are strong. Therefore, asset repositioning specialists may be a better ownership fit than a passive investor.

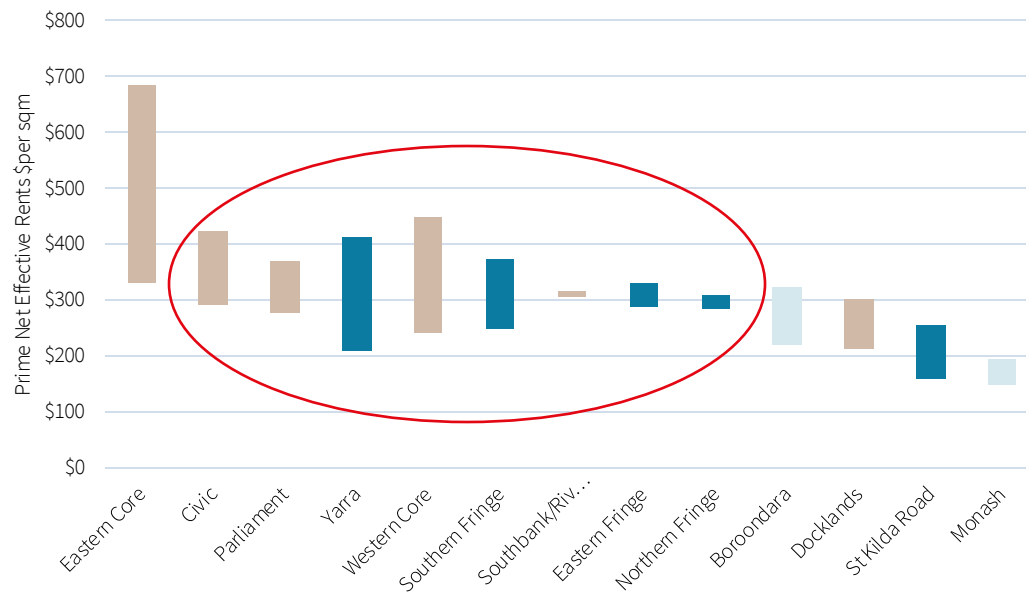


Centralisation is a continuing theme...but smaller occupiers are more likely to stay local

High CBD vacancy has resulted in CBD Prime Grade incentives increasing to average 43% at 2Q24. This compares to 38% and 35% in Fringe and SES markets respectively. Net effective rents in most CBD precincts are comparable to some fringe precincts. For example, a tenant in Melbourne’s Yarra precinct is now able to consider most CBD precincts except CBD Eastern

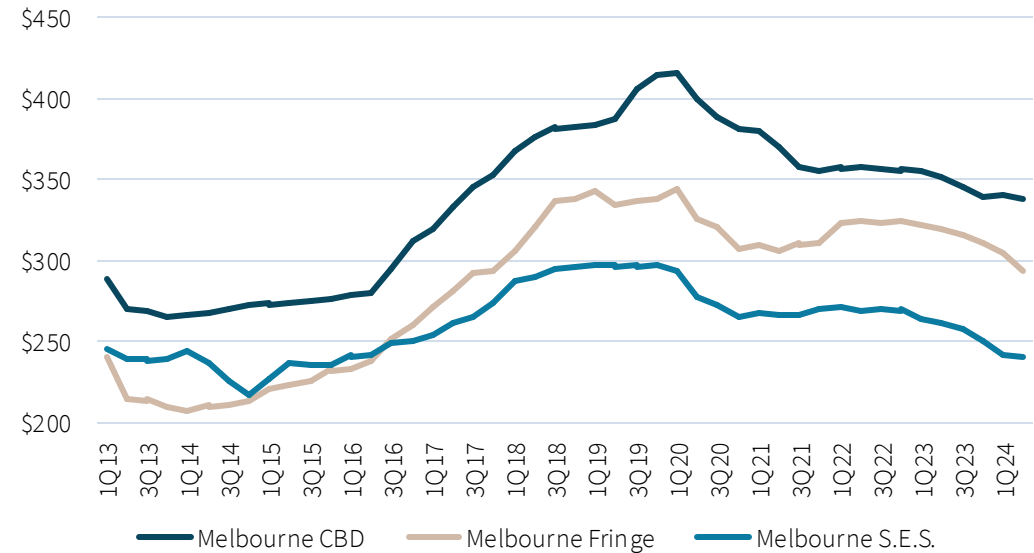
Core. Centralisation is likely to be a continuing theme for larger occupiers, enabling them tap into a wider pool of talent. Smaller groups have proven sticky in fringe and suburban precincts particularly in those assets with good car parking options.

Prime Net Effective Rents by Precinct



Source: JLL Research

Average Prime Net Effective Rents by market



Industrial

1

Melbourne is Australia's largest logistics and industrial market with 29.5 million sqm of total stock compared to Sydney with 23.1million sqm. Melbourne has leading transport infrastructure including Australia's largest port and biggest airfreight hub.

2

Vacancy is low at 3.03% (895, 245 sqm) and just 712, 500 sqm remains available in stock under construction and due for completion by 2026, suggesting a **shortfall of over 1 million sqm** of required stock by 2028.

3

JLL's population growth construction demand model suggests that Melbourne will need **a further 2.6 million sqm over the next five years** to support metropolitan Melbourne's growing population.

4

Affordability relative to other market. Strong rental growth across many precincts but rents remain affordable. Sydney Melbourne's West prime net face rents are 34% lower than in Sydney's Outer Central West and are being considered by Sydney based 3PLS for their National Distribution Centres.





Key transport infrastructure projects are in the pipeline to accommodate Melbourne’s growth

International, national and local industrial and logistics occupiers are attracted to Melbourne’s leading transport infrastructure.

The Port of Melbourne is Australia’s largest with highest volume of TEU volumes. The Port Development Strategy outlines plans to double container throughput to circa 6 million TEU each year by 2035.

Melbourne Airport is Australia’s biggest air freight hub. Expansion plans include a third runway with completion expected in 2026. Melbourne Airport has also given the green light to an above ground station for the proposed airport rail line to ensure the public transport link is in place as the airport expands.

Victoria’s Big Build program of infrastructure projects will deliver projects that will improve supply chain efficiency across metropolitan Melbourne.

Melbourne’s Infrastructure supports logistics and industrial sector growth



The **Port of Melbourne** is Australia’s largest, with 3.0 mn TEU compared to Sydney and Brisbane with 2.6 mn TEU and 1.3 mn TEU respectively



Melbourne Airport is Australia’s **biggest air freight hub**, with more than \$1.8 bn of locally made exports in first three months of 2024



The **Principal Freight Network (PFN)** identifies and protects Victoria’s key road and rail freight routes.



Westgate Tunnel
Total Investment **\$11.9bn**
Completion target: 2024
Improving drive times to Melbourne’s West



North-East Link
Total Investment **\$20.6bn**
Completion target: 2028
Allowing Melbourne’s most populous suburbs in the south-east to be services from Melbourne’s North



Level Crossing removal project
Total Investment **\$2.5bn**
Completion target: 2030
84 of 110 level crossings removals have been completed improving supply chain efficiency around Melbourne



Population projections suggest demand for circa **2.6 million sqm** of industrial over 5 years in Victoria

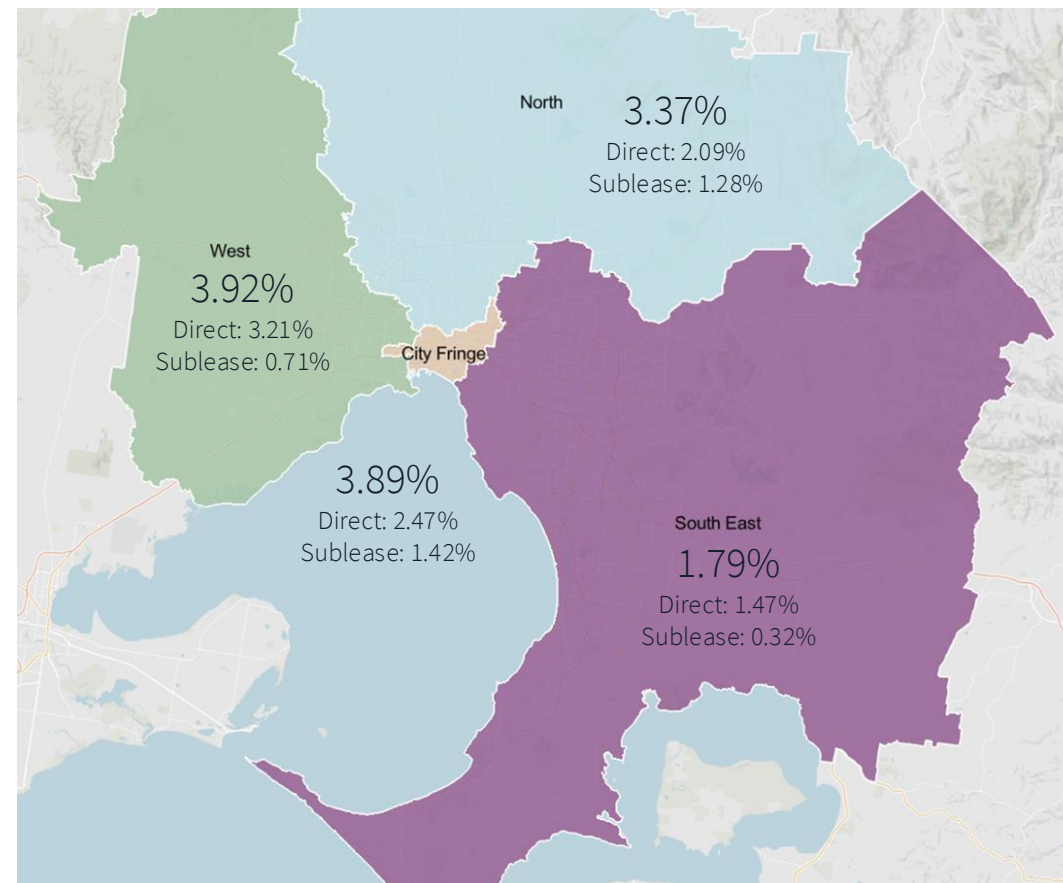
Melbourne is Australia’s largest logistics and industrial market with 29.5 million sqm of total stock compared to Sydney with 23.1million sqm.

Total market size is expected to expand further as population growth and continued growth in eCommerce.

Vacancy is low at 3.03% (895, 245 sqm) and just 712, 500 sqm remains available in stock under construction and due for completion by 2026, suggesting **a shortfall of over 1 million sqm** of required stock by 2028.

Melbourne South- East industrial market has the lowest vacancy in the country with limited land availability restricting future supply.

	Population change next 5 years	Population change construction demand model (ratio)		
		4.5	5	5.5
Sydney	318,910	1,435,100	1,594,600	1,754,000
Melbourne	523,730	2,356,800	2,618,700	2,880,500
Brisbane	292,610	1,316,700	1,463,100	1,609,400
Perth	284,500	1,280,300	1,422,500	1,564,800
Adelaide	96,180	432,800	480,900	529,000
Total	1,515,930	6,821,700	7,579,800	8,337,700



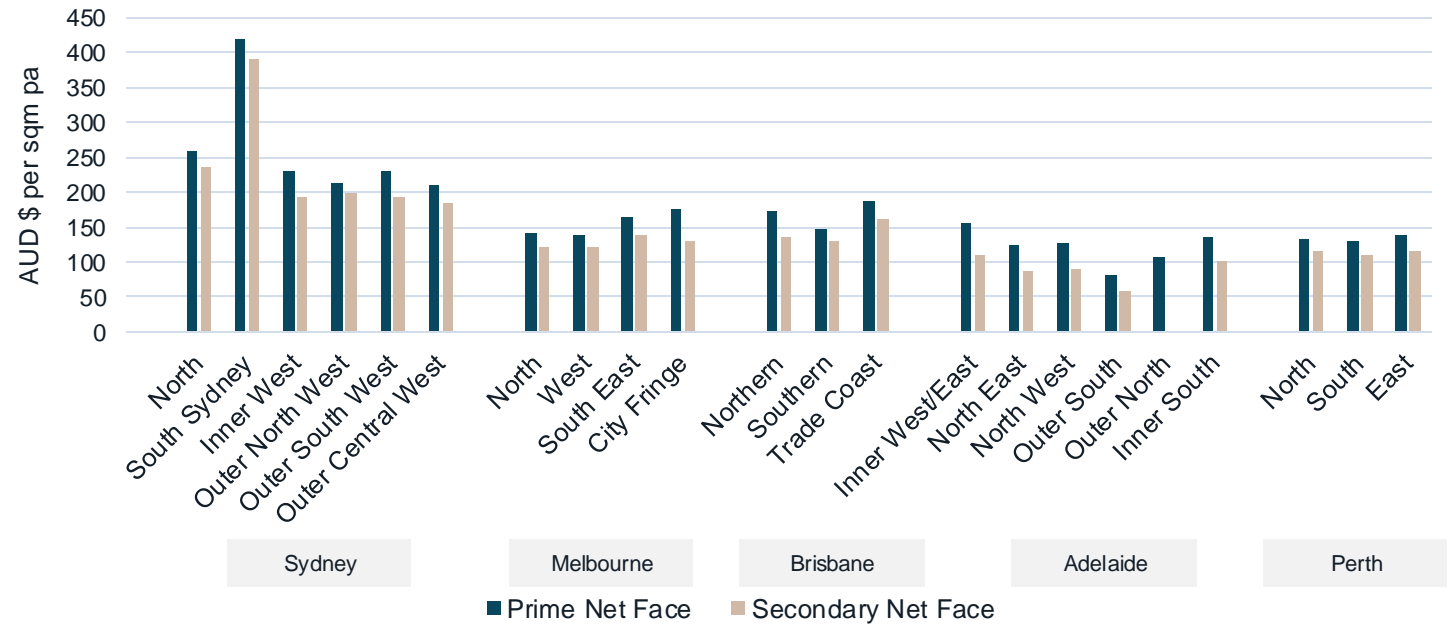
Source: JLL Research, Oxford Economics



Affordability relative to Sydney is proving a driver of potential demand for National Distribution Centres



Industrial Prime & Secondary Net Face rents by market



Melbourne's West prime net face rents are 34% lower than in Sydney's Outer Central West and are being considered by Sydney based 3PLS for their National Distribution Centres.

Living sectors

1

While there is more BTR stock under construction in Melbourne than other markets, it is not enough to offset the decline in BTS supply and will likely provide only limited relief to the rental market.

2

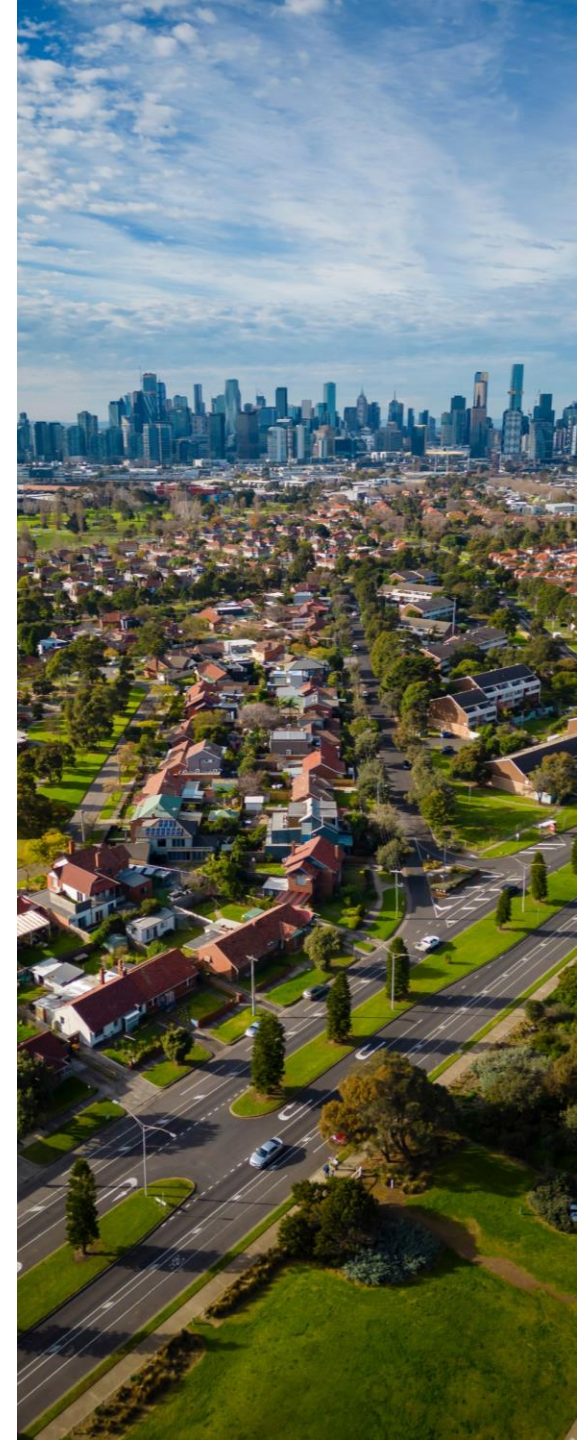
Overall, residential supply is not likely to keep pace with continued population growth. The improved affordability of Melbourne housing relative to other cities will also help support the inflow of migrants and students to city. As such, developers are looking beyond the current softer housing market conditions and remain optimistic about medium-term prospects for the city.

3

Melbourne's hotel market has absorbed **more than 5,000 new hotel rooms since 2020**, a 24% increase in hotel stock through the pandemic. An additional eight projects are currently under construction, which will result in a 33% increase in total stock over the current supply cycle.

4

Melbourne's hotel market has recovered ahead of expectations and hotel ADR accelerated beyond pre-COVID levels. Ongoing recovery being supported by improved inbound visitation and airlift capacity, recovering corporate/MICE (meetings, incentives, conferences and exhibitions) demand, as well as strong ongoing leisure demand for Melbourne's significant major events calendar.





Melbourne has the most BTR stock under construction, but not enough to offset the decline in BTS supply

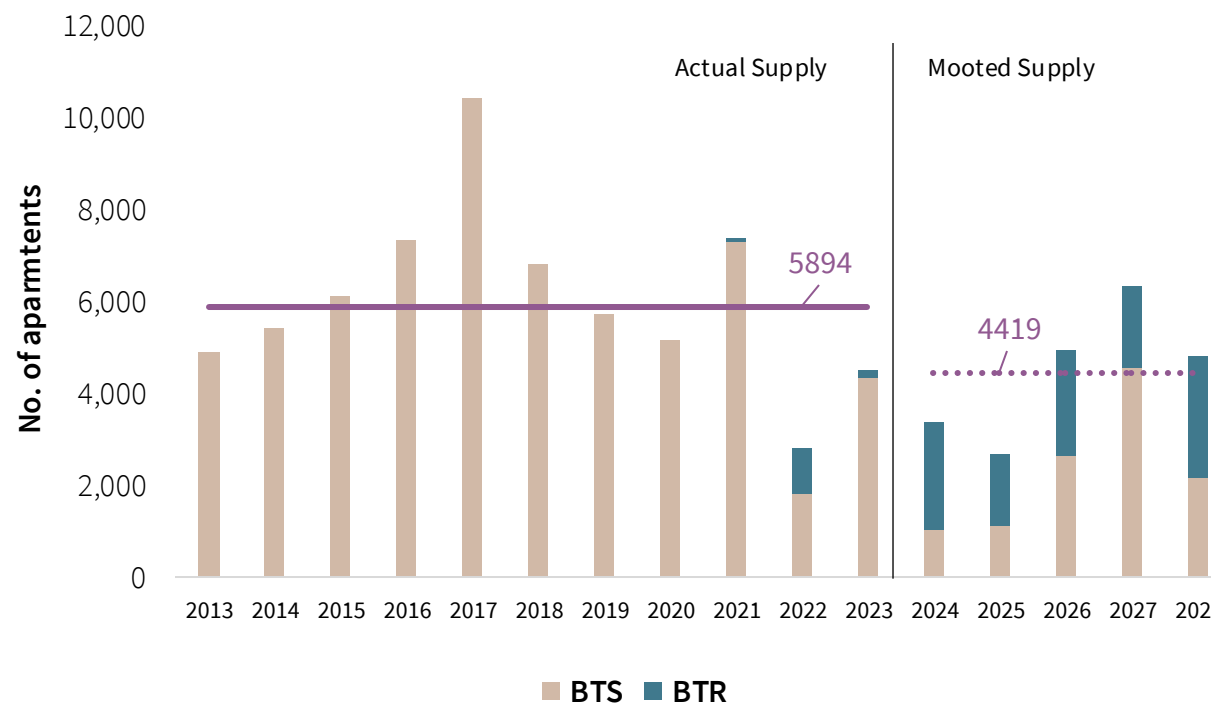
Melbourne has seen strong residential construction the past decade and the city is around 60% of all BTR supply JLL is monitoring nationally. However, there is very good reasons for this concentration in BTR towards Melbourne and it reflects a combination of the attraction of Melbourne’s very high migration and the availability of many well-located high-density sites in and around the CBD that are ideal for BTR and are much feasible than sites in other major cities.

Coming into 2024, Melbourne already had eight operational BTR assets totalling around 2,379 apartments. Already four projects have completed in 2024 and with another two due to complete before the end of the year around 2,179 would almost double that stock. Another six completions in 2025 are likely to add around 3,200 apartments. Completions over 2024 and 2025 include most of the sectors major players such as Mirvac, Greystar, Home, Local, Novus, GQ and Salta.

Despite these strong BTR completions and BTR being 48% of expected supply in Inner Melbourne from 2024 to 2028, it is not enough to offset the decline in build-to-sell (BTS) supply. Total supply over this period is expected to be only around 4,400 per annum and around 25% less than the period from 2013 to 2023.

Source: JLL Research

Inner Melbourne BTR and BTS Supply Pipeline



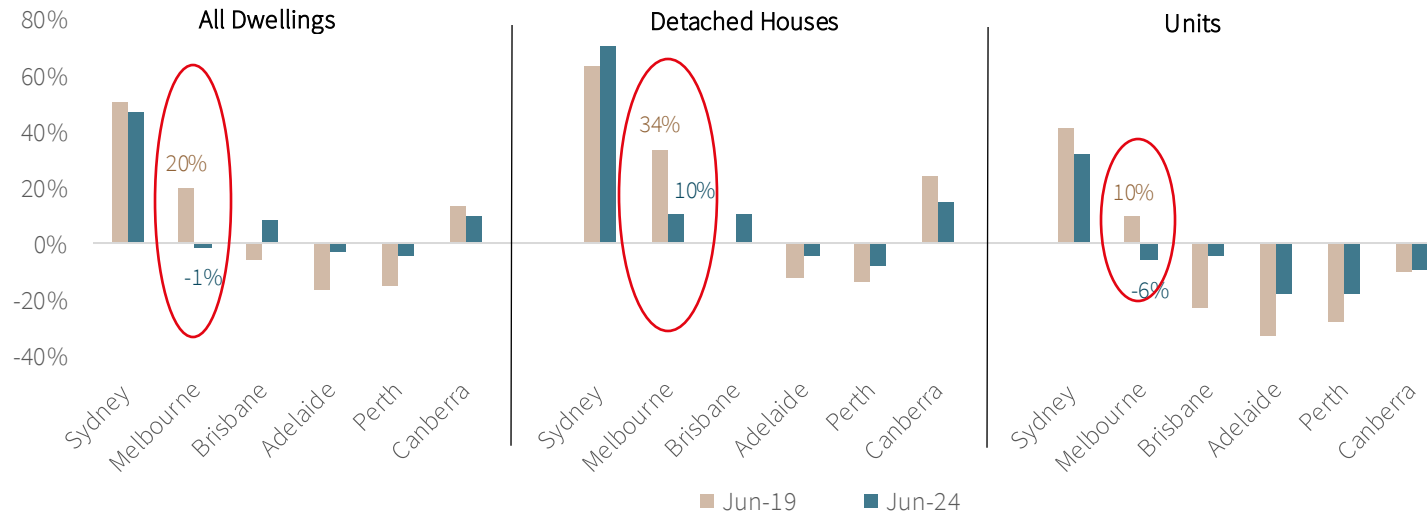


Improved relative affordability of Melbourne housing will help support continued high migration

Prior to COVID, Melbourne’s median dwelling prices were 20% higher than national average in Jun-19, but this had fallen to 1% below the national average in Jun-24. Melbourne dwelling prices have risen over the last five-years, but much less than other capital cities in part due to Victorian land tax increases for investment properties and second homes. Melbourne rental growth has been more subdued than other capitals since COVID and rental

prices are similarly affordable relative to other cities now. While conditions are likely to stay muted in near-term in a credit-constrained and high interest rate environment, this improvement in relative affordability is likely to put Melbourne in good stead in keep attracting a very large share of overseas migrants and students over the medium-term.

Price Differential to National Average (%)



Median Residential Rents (\$ per week)

	Median house rent	Median Unit rent
Sydney	\$750	\$700
Canberra	\$685	\$570
Perth	\$650	\$550
Darwin	\$650	\$550
Brisbane	\$620	\$590
Adelaide	\$590	\$460
Melbourne	\$570	\$550
Hobart	\$550	\$460
All capital cities	\$630	\$620

Source: CoreLogic, JLL Research



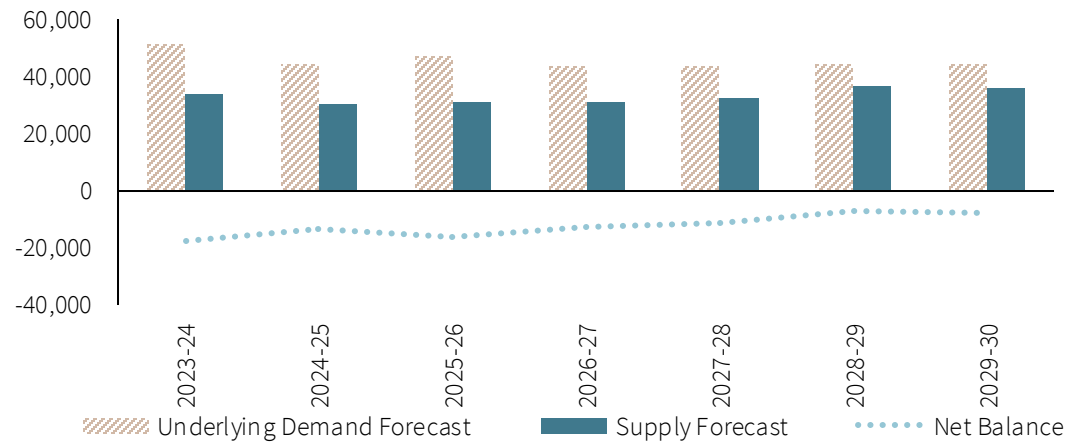
Supply will not keep pace with population growth, which supports the medium-term outlook

Despite likely further short-term headwinds for the housing market until interest rate cuts arrive, developers remain optimistic about the medium to longer-term prospects for Melbourne residential. This is evident in still strong investor demand for prime residential development sites. This optimism is rooted in the simple assumption that total housing supply is going to fall well short of underlying demand from strong population growth over the next five years or so.

Housing Australia (formerly NHFIC) released estimates of housing supply-demand balance in 2023 and JLL have updated these estimates using the latest (upwardly revised) population forecasts. While supply levels may well adjust to this outlook over the medium-term, it is difficult for this to happen quickly and particularly in what is a still difficult construction environment.

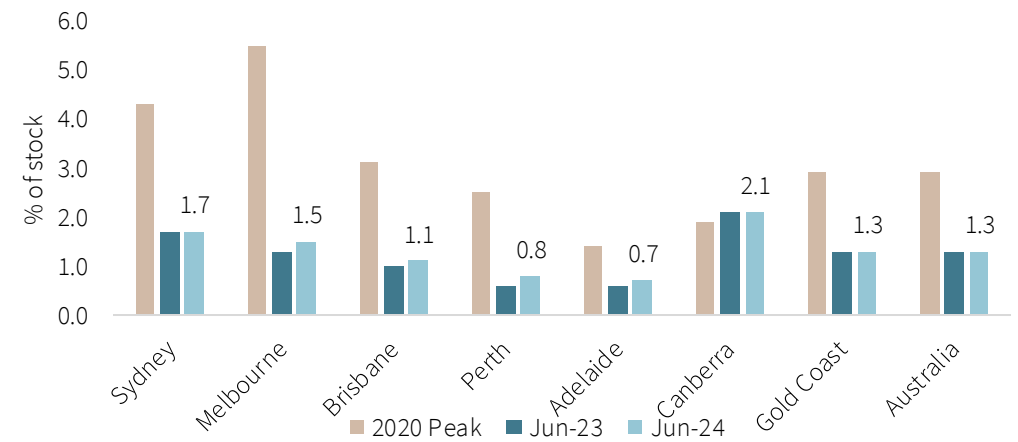
So despite the little bit of immediate supply relief the Melbourne market will get from some upcoming BTR completions, it will do little over the medium-term to address the overall housing supply shortages across the city and the already tight rental vacancy rate.

Melbourne Housing Supply-Demand Balance Estimates



Source: JLL Research, ABS, Housing Australia, SQM Research

Residential Vacancy Rate

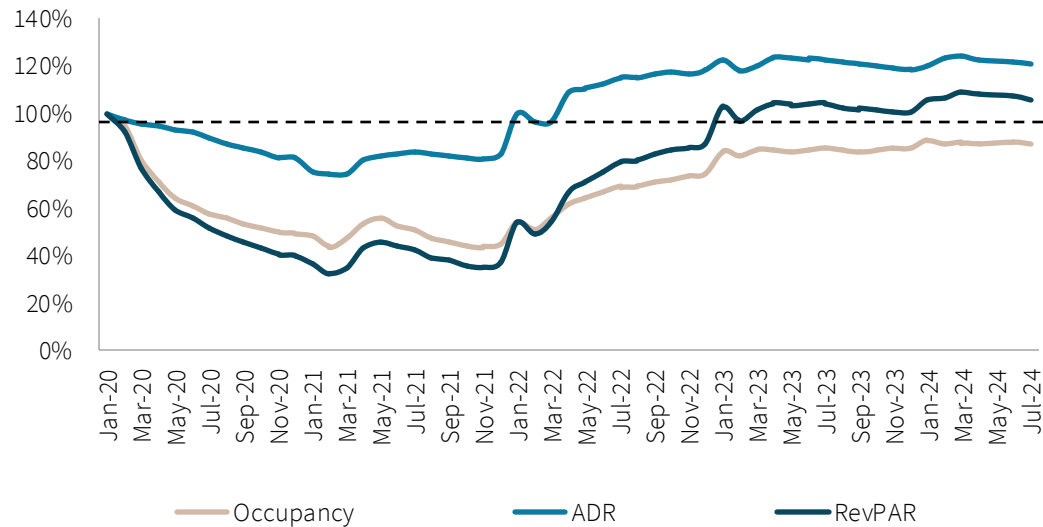




ADR accelerates beyond pre-COVID levels, as occupancy steadily recovers

Melbourne’s hotel market has recovered ahead of expectations with hotel ADR (average daily rate) accelerating beyond pre-COVID levels, as occupancy steadily recovers. Ongoing recovery being supported by improved inbound visitation and airlift capacity, recovering corporate/MICE (meetings, incentives, conferences and exhibitions) demand, as well as strong ongoing leisure demand for Melbourne’s significant major events calendar.

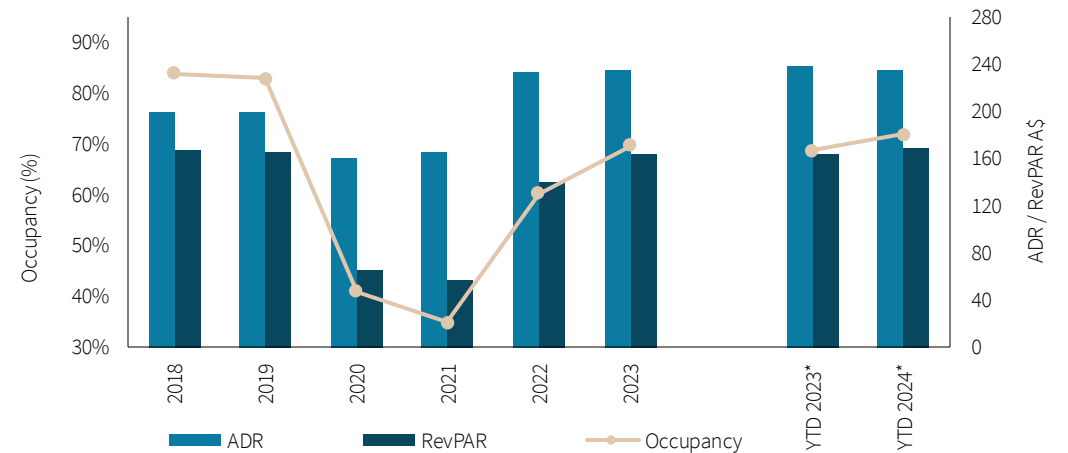
Melbourne Hotel Recovery to Pre-COVID Levels



Recent Performance

Melbourne (YTD July 2024)	vs 2023	vs 2019	
Occupancy	72.0%	+5%	-12%
ADR	\$236	-2%	+21%
RevPAR	\$170	+3%	+6%

Melbourne City Market Performance



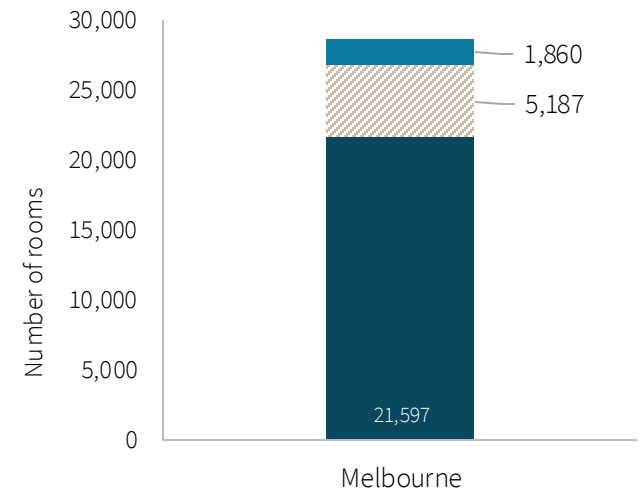
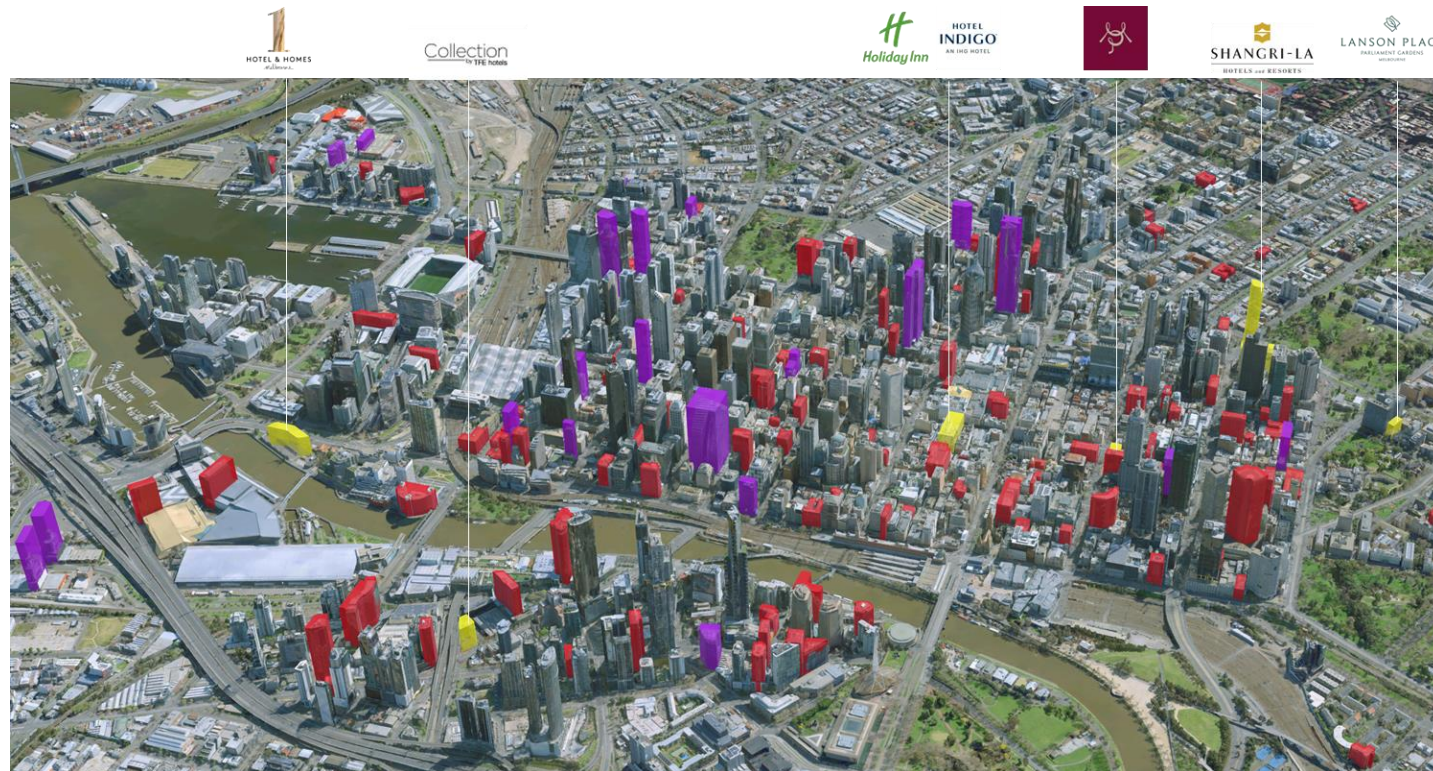
Source: JLL Research, STR



Melbourne hotels current supply and future pipeline

Melbourne’s hotel market has absorbed close to 5,200 new hotel rooms since 2020, a 24% increase in hotel stock through the pandemic. This included the addition of notable international brands such as the W, Ritz Carlton and Le Meridien. There remains eight properties currently under construction, which once complete will result in a net increase of

1,860 rooms. As a result, the current supply cycle will have delivered a significant 33% increase on total stock since 2020, and in doing so has become the largest hotel market in the country.



- No. of rooms under construction
- ▨ No. of rooms opened since 2020
- Total Average Rooms (Dec-19)

- Hotels – Existing Hotels
- Hotels – Opened since 2020
- Hotels – Under Construction

Source: JLL Hotels & Hospitality
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Outlook

Melbourne’s real estate markets have historically been consistent strong performers, driven by strong population, robust GDP growth and transparent real estate markets.

However, confidence in Melbourne’s growth parameters has also fuelled substantial supply waves in many sectors of the market. The 2020 supply peaks in office and hotels could not have come at a worse time with classic property cycles intersecting with changing occupier behaviours. No other Australian markets experienced these volumes of increased supply.

The Victorian state government tax changes have added increasing complexity to an already challenging investor landscape, but early movers, believe the market is bottoming out and are positioning to catch the cyclical upswing.

Strategic thinking and a more nuanced approach will be required in coming years. However, Melbourne’s growth fundamentals bode well for market recovery, as interest rates stabilise, and capital values reach their trough over the next six to 12 months.



Research authors

Annabel McFarlane

Head of Strategic Research, Australia
JLL Research
Australia
Annabel.mcfarlane@jll.com

Kyle Wheatley

Associate
Hotels
Australia
Kyle.wheatley@jll.com

Leigh Warner

Senior Director
JLL Research
Australia
Leigh.warner@jll.com

Ronak Bhimjiani

Director
JLL Research
Australia
Ronak.bhimjiani@jll.com

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To find out more about JLL services, contact:

Kate Pilgrim

Managing Director & Joint Head of Tenant Representation – Victoria
Australia
Kate.pilgrim@jll.com

Nick Drake

Joint Head of Office Leasing - Victoria
Australia
Nick.drake@jll.com

James Jorgenson

Head of Logistics & Industrial - Victoria
Australia
James.jorgenson@jll.com

Peter Harper

Managing Director, Head of Investment Sales
JLL Hotels & Hospitality Group
Australasia
Peter.harper@jll.com

Josh Rutman

Executive Director
Head of Capital Markets - Victoria
Australia
Josh.rutman@jll.com

Martin Reynolds

Head of Valuations Advisory
Australia
Martin.reynolds@jll.com

Jack Bergin

Head of Living, Capital Markets
Australia
Jack.bergin@jll.com

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