

Industrial Market – Current State of Play

HMW Real Estate Insights

September 2023

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Industrial Market Overview

The industrial sector emerged from the COVID-19 pandemic as a popular asset class with investors. Whilst the pandemic softened demand fundamentals in the more traditional sectors of office and retail, the industrial sector benefited from heightened occupier demand, driven by numerous factors including strong e-commerce growth and a return to more localised manufacturing. More recently, strong population growth has been a major driver of continued strength in the occupier market.

As a result of strong occupier demand, coupled with construction delays, the industrial market has witnessed extremely low vacancy rates. The low vacancy rate has driven rental growth at levels not seen before, as well as a sharp reduction in incentives, over the past year.

Following record levels of investment activity over previous years, transaction values have been subdued during 2023. Investors have displayed heightened caution this year given the uncertain economic and pricing environment. These conditions have resulted in a softening of circa 100 basis points in both prime and secondary industrial yields across the South East Queensland market.

Greater Brisbane Industrial Rents and Yields – June Qtr. 2023

Net Face Rents

\$140/m²

Prime average
+11.3% y-o-y

\$120/m²

Secondary average
+20.1% y-o-y

Yields

5.55%

Prime average
+93 bp y-o-y

6.50%

Secondary average
+106 bp y-o-y

Industrial Indicators

The Industrial Sector's Contribution to the Economy

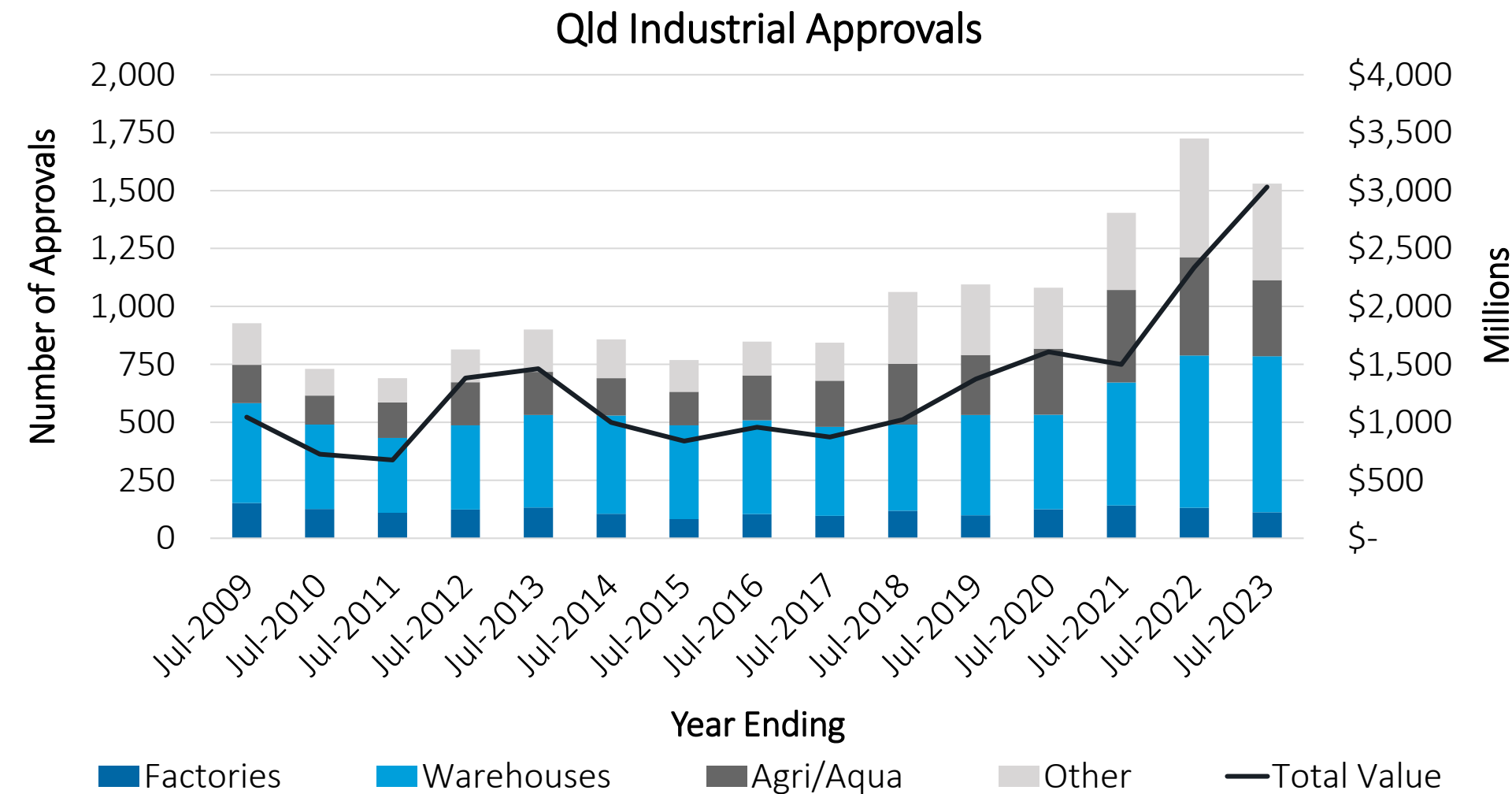
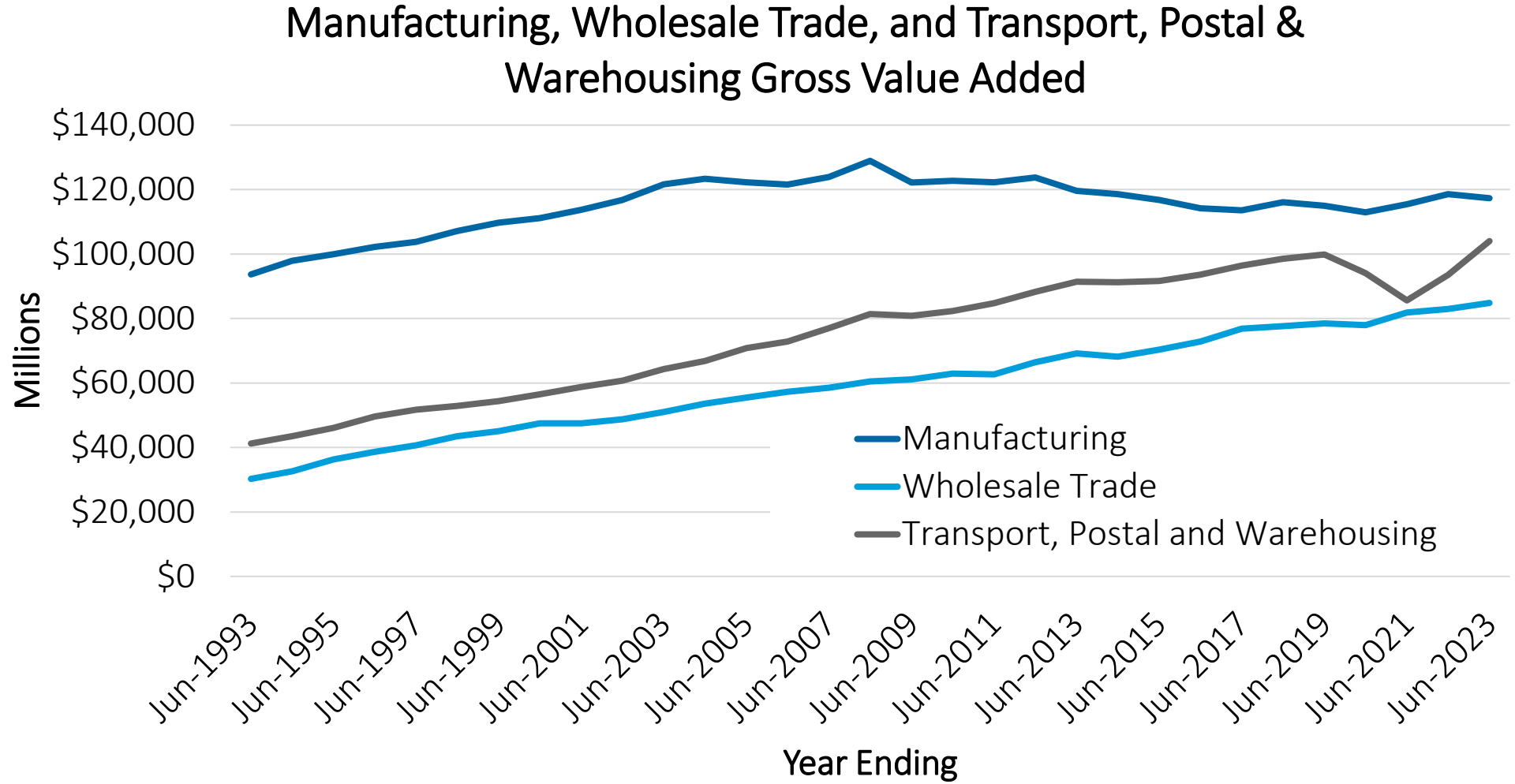
The manufacturing industry's contribution to the economy has broadly trended downwards since the 2007-08 financial year. Despite ticking up during the pandemic, it tapered back again during the 2022-23 financial year.

The Transport, Postal and Warehousing industry's contribution to the economy declined sharply at the start of the pandemic, before re-bounding over the past two fiscal years, driven by growth in e-commerce, business's focus on supply-chain efficiencies, and higher inventory levels ("just in case" inventory management). This trend has been reflected in industrial space absorption, with users from the Transport, Postal and Warehousing industry accounting for a significant proportion of leasing demand.

Industrial Building Approvals

The number of industrial building approvals declined over the year ending July 2023, compared with the previous 12-month period; however, the total value of industrial approvals rose to over \$3 billion.

By value, the \$20 to \$50 million bracket has seen exceptionally strong growth in the number and value of approvals over the past two years, driven by growth in warehouse approvals, low vacancy rates and increased demand from e-commerce and associated logistics demand.



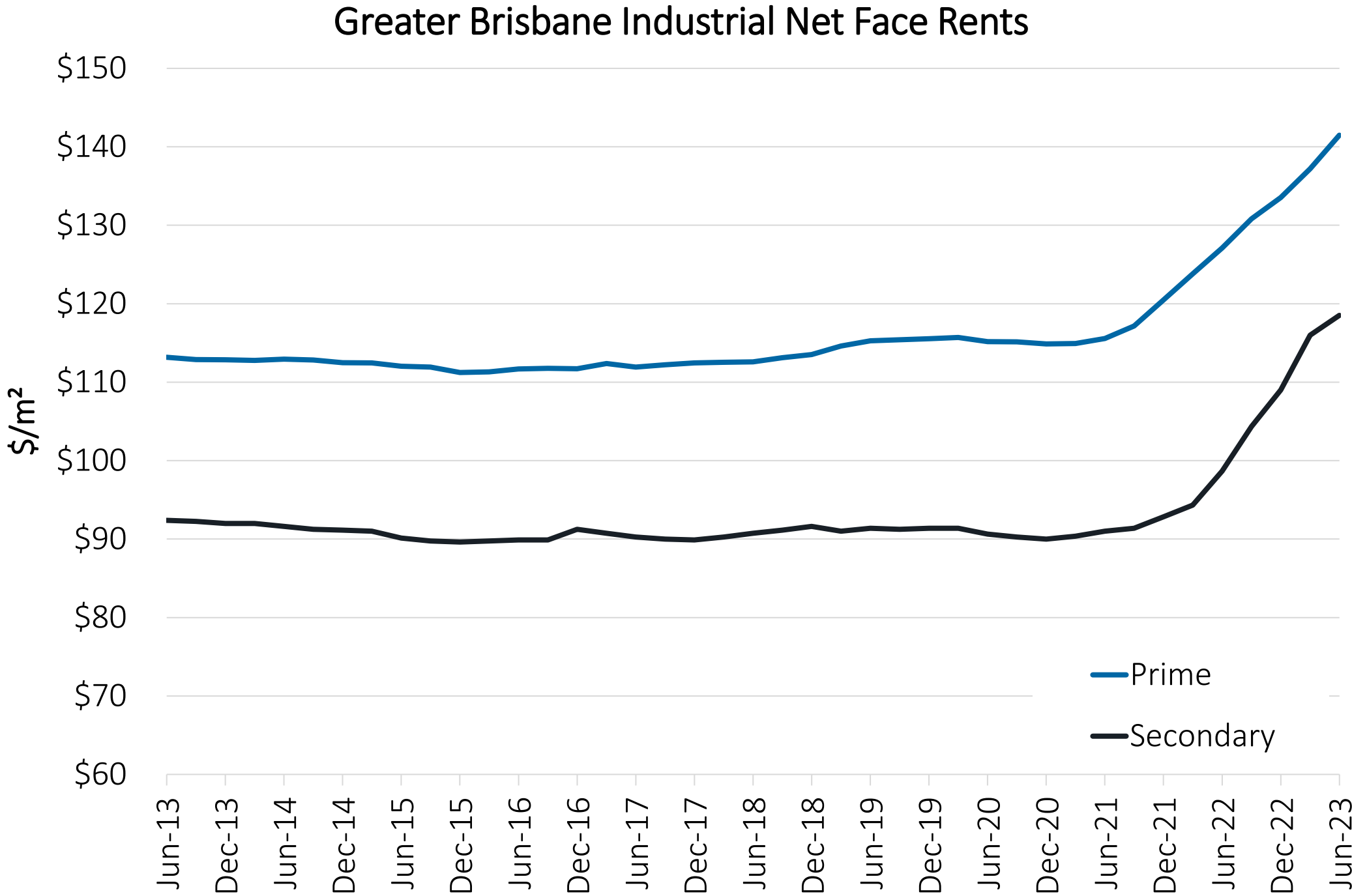
Source: ABS, HMW Real Estate Advisory
 Note: Building approvals \$250,000 +

Rental Market

Prime net face rents currently average circa \$140 per square metre and secondary net face rents average circa \$120 per square metre. The Australia Trade Coast continues to attract a premium to the remaining sub-markets. The spread between prime and secondary rents has narrowed over recent years due to the tight vacancy rate.

Net face rents have seen strong growth over the past year, offsetting, to some degree, the effect of softening yields on industrial property values. Prior to this recent growth, rents across Brisbane had been largely stable for a number of years. Effective rents have seen even stronger growth due to declining incentives. Incentives averaged circa 10% for prime buildings during the June 2023 quarter.

The industrial market remains a landlord's market. Tight vacancy rates have limited the number of lease deals that have occurred over recent years and contributed to strong rental growth. Activity has been strongest in the south and southwestern markets, which is where most of the new supply has been completed. However, we note that landlords that signed long-term leases with tenants without the provision for market reviews will be unable to take advantage of the strong rental growth environment and are possibly locked in on long remaining lease terms with passing income that is substantially lower than market income.



Source: HMW Real Estate Advisory

Investment Market

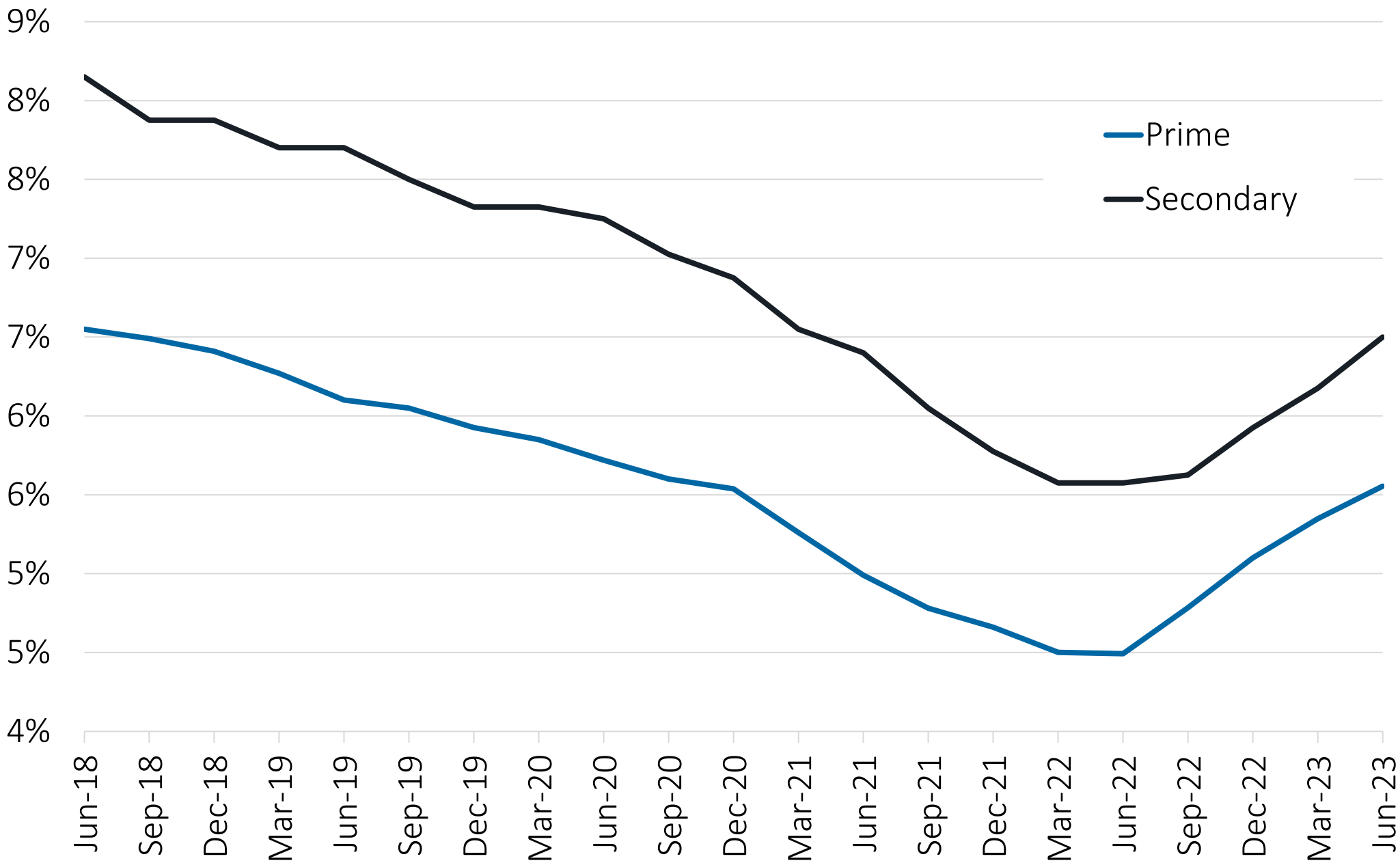
Sales volumes have declined considerably during 2023 due to the higher interest rate environment and the disconnect being vendor and vendee expectations.

Lower leveraged buyers such as private investors and owner occupiers have accounted for a larger proportion of sales this year than they have during previous years. Private investors have been acting more opportunistically whilst owner occupiers have likely been influenced to buy rather than rent due to the increasing costs associated with renting.

Yields have softened since mid-2022, with prime yields currently averaging circa 5.5% and secondary yields averaging circa 6.5%. Over the past 12 months, yields have softened by circa 100 basis points for both prime and secondary assets. However, strong rental growth has partially supported capital values despite this softening in yields.

After a period of rapid growth in land values, values have stabilised over the past year.

Greater Brisbane Industrial Yields



Source: HMW Real Estate Advisory

Draft SEQ Regional Plan 2023

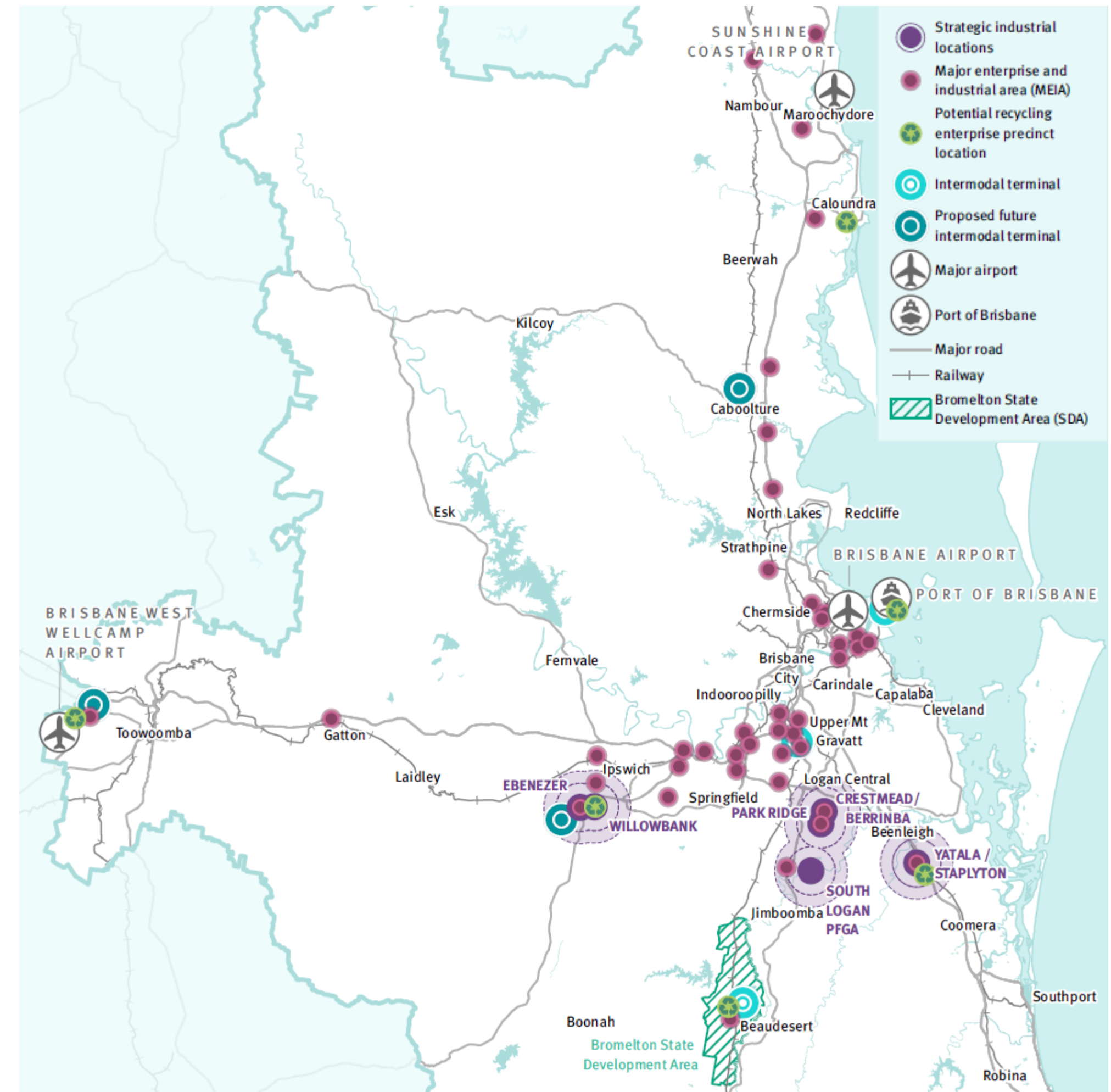
The Draft Shaping SEQ 2023 Update states that key areas of SEQ are approaching a critical shortfall of industrial land, with the Brisbane LGA having an estimated 10-15 years supply (with the impacts expected to be felt on land pricing in particularly within 5-10 years).

The Update establishes a regional approach to industrial land planning to complement Local Government planning and identifies future industrial land, particularly in the Redland, Sunshine Coast and Gold Coast LGAs. Furthermore, the LGAs of Gold Coast, Ipswich and Logan are expected to play key roles in meeting future demand, due to freight and logistics networks and freight volumes from the southern states.

The following actions have been prioritised in the draft Update:

- Identification of additional land within northern Gold Coast.
- Infrastructure investment within Logan for improved freight accessibility.
- Investigation of potential additional land within Logan.
- Infrastructure investment within Ipswich to service land at Ebenezer.

Consultation on the Draft Shaping SEQ 2023 Regional Plan closed on 20 September and the final Update is scheduled to be finalised in December.



Draft SEQ Regional Plan 2023

The draft Update states that detailed planning will be prioritised for the following future industrial areas:

Metro Sub Region

- Part of the land within the Southern Thornlands Urban Footprint expansion area
- Urban Footprint expansion area at Redland Bay
- Additional areas at Narangba East

Northern Sub Region

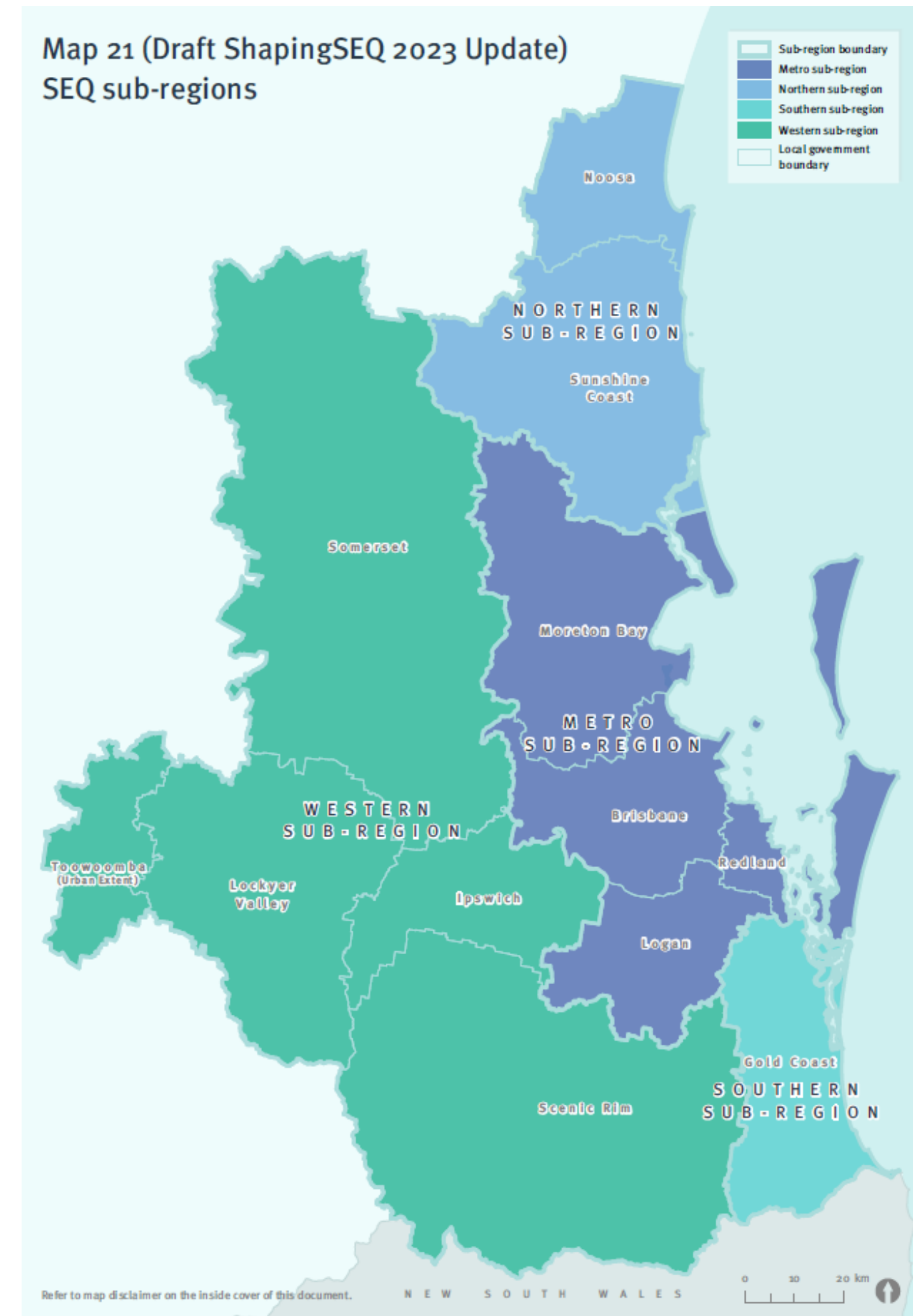
- Beerwah Further Investigation Area
- Part of the Beerwah East major development area
- Urban Footprint expansion area at Yandina
- Expansion of the Coolum MEIA
- Expansion of the Caloundra MEIA

Western Sub Region

- Urban Footprint expansion area at West Toowoomba
- Prioritising the delivery of Stage 1 of the Willowbank Industrial Area
- Delivery of key infrastructure projects to facilitate the long-term development of the Bromelton State Development Area

Southern Sub Region

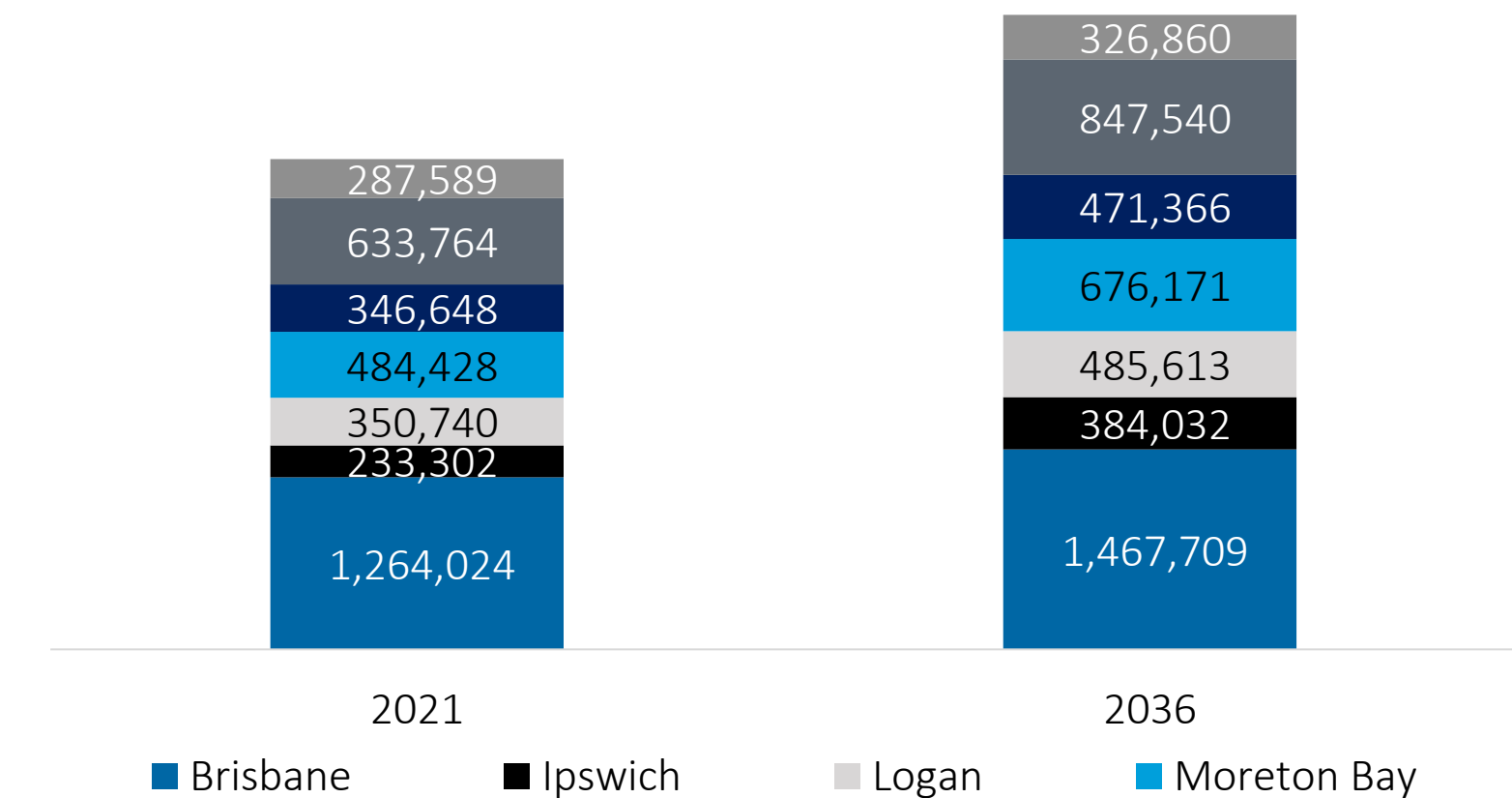
- Urban Footprint expansion area of Stapylton
- Expansion of the Yatala / Stapylton MEIA



Conclusion and Outlook

- Occupier demand is expected to be more subdued over the near-term, due to weaker economic conditions. These conditions may lead some occupiers to scale back expansion plans or rationalise their existing footprint. Higher costs may encourage some occupiers to consider their supply chain, building and operational efficiencies. When combined with new supply coming to the market, these conditions have the potential to result in a slow-down in rental *growth* over the short-term.
- However, we expect that rental growth will be robust over the medium- to longer-term due to the solid outlook for occupier demand resulting from:
 - Improving economic conditions (particularly household spending, following weak conditions in the short-term);
 - Robust population growth forecast for South East Queensland;
 - Construction of infrastructure and facilities for the 2032 Olympic Games;
 - Demand from national occupiers without a Brisbane / SEQ presence;
 - Reducing land availability; and
 - Continued growth in online retailing.
- When compared with the office and retail sectors, which are still in many respects feeling the pain of COVID-19 induced demographic changes (i.e. working from home and shopping online), we are of the view that industrial properties remain a standout investment option, backed by sound longer-term fundamentals and increased certainty regarding occupier demand going forward.
- Investment demand is expected to increase from early next year following an expected stabilisation in interest rates and higher certainty regarding the cost of debt.

SEQ Forecast Population Growth (Persons)



Source: Queensland Government Statistician's Office, HMW Real Estate Advisory
 Note: SEQ Remainder includes the Redland Bay, Noosa, Somerset, and Scenic Rim LGAs.

HMW Real Estate Advisory Services

Property Valuation Services

- Commercial property (office, retail, industrial); specialised assets (self-storage, disabled housing, petrol stations, retirement villages etcetera); and health care assets.
- Non-mortgage, trust, asset (Government and private) and GST valuations.
- Pre-acquisition valuations and consultancy advice, in addition to disposal strategic solutions and advice.
- Tactical advice on portfolio balance and strategies.

Property Economic and Research Services

- Catchment analysis for proposed business and property ventures.
- Supply and Demand research for proposed business and property ventures.
- Property market research.

NDIS Disabled Housing Project Consultation and Advice

- Independent review and advice in relation to NDIS development and funding.

Property Portfolio Valuer/Valuation Management

- Valuation management services including obtaining quotes and selection.
- Preparation of a program for communication and deliverables.
- Provision of a structured reporting process.
- Review of valuation methodology, rationale and sales for appositeness.

Highest and Best Use Assessments

- Identification of potential uses of the property for either redevelopment, repositioning or refurbishment.
- Review town planning and zoning constraints impacting on future development and use the site.
- Supply and demand / needs analysis for the perceived highest and best uses of the site.

Project Feasibility Analysis

- Highest and best use of the site.
- Gross Realisable value of the project based on highest and best use.
- Residual analysis studies to establish Project Related Site value.
- Market value of the site on the basis of a third-party, independent of the proponent.

Rental Review, Determinations and Assessments

- Strategic advice on tenant lease Terms and Conditions and recommendations for negotiations of leases.
- Market analysis of rental transactions to assess the Current Market Rental value.
- Market rent assessment based on the proposed/existing lease terms and conditions.

Tenant Representation Activities

- Engagement of appropriate consultants for new leases and/or lease renewals.

Project and Investment Funding Sourcing

- *Quintessential Finance* overseen by Tony Rickards, Partner, HMW Group.
- Credit assessments or loan submissions to supplement internal resources and skills.
- Independent review and advice on loan submissions, credit assessments and underwriting policies, specialising in property development and investment finance.
- Genuine and considered insights into the performance and outlook of industry sectors.
- Hindsight reviews of loans to give opinion on the health of your loan exposures and underwriting practices.
- Loan portfolio impairment stress testing / modelling.
- Origination of lending opportunities (e.g. broking)

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