Building slowdown to cut CBD office space

ELIZABETH REDMAN
VACANCIES

Australia's CBDs will see a substantial fall in the amount of new office space, with development halving over the next three years, according to a Property Council of Australia report.

The total amount of new supply due to come online between now and 2020 is 462,000sq m, only 50 per cent of that built over the last 18 months.

The effects of the construction slowdown will differ across the country, with pressure on rents more likely in Sydney and Melbourne while Perth is still feeling the impact of the weaker resources sector, the Property Council said.

"Going forward, there's not going to be many office buildings built in our CBDs," Property Council chief executive Ken Morrison told *The Australian*.

"That will certainly have an impact on the market dynamics of CBDs. But also a lower level of (office) construction when most forecasters are seeing a step down in housing construction — that is a potentially significant impact to the broader economy as well."

The council's latest office market report showed vacancies edged higher in Sydney, from 5.6 per cent to 6.2 per cent in the six months to January, although the city still has the lowest vacancy rate of all the capital cities.

Net demand in Melbourne and Brisbane was particularly strong, at more than three times its historical average in the six months to January, the PCA said.

Melbourne benefited from buoyant employment growth, with its office vacancy rate falling from 7 per cent to 6.4 per cent over the six months and future supply looking tight. Three of the five markets with the lowest vacancy rates in the country are now in Melbourne: East Melbourne, Southbank and the CBD.

Brisbane's office market had been affected by the mining slowdown and public service cuts under the previous state government, but got a boost from a pickup in the local economy as well as the government occupying more office space. The city's vacancy rate fell from 16.9 per cent, but remained higher than its other east coast counterparts at 15.3 per cent.

Canberra's vacancy rate also edged down from 13 per cent to 12.6 per cent, largely due to the withdrawal of some supply from the market.

On the west coast, by contrast, the vacancy rate continued to rise in mining-affected Perth, lifting from 21.8 per cent to 22.5 per cent. This is the highest rate in the country, alongside Darwin.

The Perth market is facing both the end of the mining construction boom and an overhang of new supply that was incentivised by the boom, although little new supply is expected over the next few years.

In Darwin, low growth in demand pushed vacancies from 20.7 per cent up to 22.5 per cent. In both Darwin and Perth, where vacancies are high, lower-quality office space has been worst hit as tenants can choose the best stock.

Vacancies also rose in Adelaide to the highest level in 18 years. The increase in the rate from 15.4 per cent to 16.2 per cent reflects a combination of negative demand and the addition of new supply.

The vacancy rate in Hobart was steady at 8.2 per cent, with new supply due this year from the completion of Parliament Square.

Tale of two cities as separate markets boom and bust

LEASING: Perth office towers still top the country for leasing incentives, agents say, while in the stronger market of Sydney limited supply is putting pressure on rents.

Figures from the Property Council of Australia show Perth has the highest office vacancy rate in the country, tied with Darwin, as the effects of the mining bust wash through the market. *The Australian* understands some tenants have been leasing space at incentive rates higher than 40 per cent in Perth, with other deals concluded at a lower level.

Perth also saw the strongest demand for premium grade properties, as tenants could afford to be choosy.

JLL head of office leasing Tim O'Connor said the office market in Perth had bottomed, but there were questions over how quickly it would recover.

"We haven't seen demand come back enough that incentives are starting to come down," Mr O'Connor said.

"Incentives in Sydney remained a lot higher for a lot longer than everyone thought."

Across Sydney and Melbourne, incentives to lure tenants have been falling "quite dramatically" over the last year amid strong demand and more scarce supply, Mr O'Connor said.

Sydney now has the lowest office vacancy rate in the country at 6.2 per cent, although this was a slight lift from six months earlier.

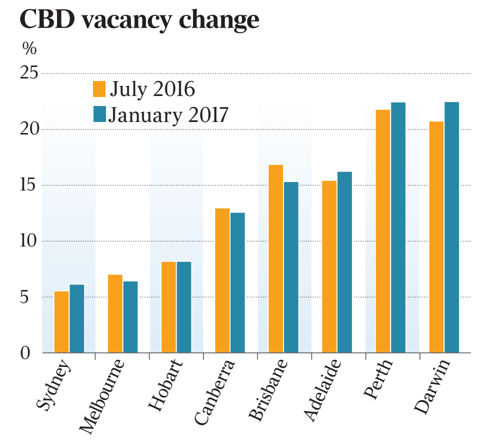
"Trading terms (in Sydney) will continue to tighten and we're anticipating a combination of rental growth and incentive contraction to continue in the years ahead," said CBRE senior director, advisory and transaction services — office, Jenine Cranston.

Tenants looking for 5000sq m of contiguous space in Sydney this year had a choice of fewer than 10 assets, Ms Cranston said.

Meanwhile, tenants from start-ups to larger businesses are also increasingly seeking flexible space and flexible lease structures, according to Colliers International.

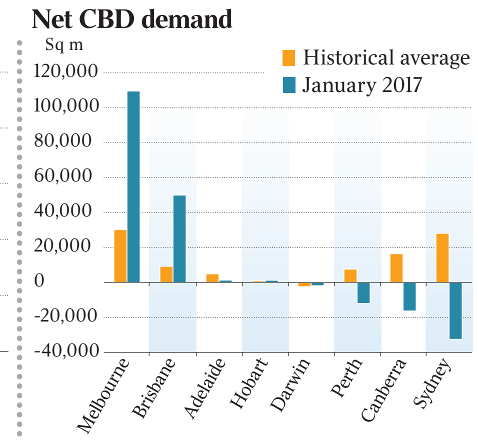
ELIZABETH REDMAN

CBD vacancy change

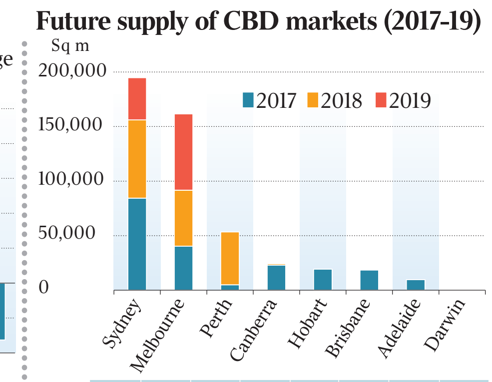


Source: Property Council of Australia

Net CBD demand



Future supply of CBD markets (2017-19)



	Sydney	Melbourne	Perth	Canberra	Hobart	Brisbane	Adelaide	Darwin
% of current stock	3.8	3.7	3	1	5.4	0.8	0.7	0
Pre-commitment (%)	46	31.3	0	42.2	84.4	0	0	0

% of current stock Pre-commitment (%)

GPT in swoop for $30m Salvos site

EXCLUSIVE

BEN WILMOT
DEVELOPMENT

GPT Group has signalled its determination to get back into office development by swooping on a $30 million-plus site in Parramatta being sold by the Salvation Army.

A purchase would give GPT Group control of a key property in Parramatta where developer Lang Walker and landlords including Dexus Property Group and Eureka Funds Management have been active.

The Salvation Army put its Parramatta office and church hall on the block last year as its long held site can sustain either a hotel or serviced apartment project or an office tower.

GPT will buy three buildings, on the corner of 93-95 Phillip Street and 32 Smith Street, that are in a prime area for redevelopment. The site could sustain a 28,037sqm project and GPT would likely seek to win a tenant precommitment before kicking off its work.

The sites attracted strong interest from office developers and groups interested in mixed use sites.

JLL's John Macree and Michael Binskin marketed the site with Raine & Horne's John Surian. The agents and parties declined to comment.

GPT has struck a series of office deals in recent months which aim to capitalise on its development and leasing savvy, which chief executive Bob Johnston has sought to emphasise.

The GPT Wholesale Office Fund last year boosted its stake in Brisbane office tower One One One Eagle Street that GPT developed.

The GPT-run fund also purchased Melbourne's landmark gothic-style tower from ANZ for $274.5m and will look to release the tower as the bank is preparing to move to a new complex in the city's Docklands.

While the deal with the Salvation Army is yet to be completed, it is part of the group's renewed focus on developing product at this heightened phase of the property cycle.

Some analysts have raised concerns about GPT's elevated share price and Goldman Sachs yesterday downgraded GPT to sell from neutral. "While we acknowledge GPT's high-quality diversified portfolio and solid balance sheet, we believe it is fully priced," Goldman Sachs said.

The analyst said that to become more positive on GPT it would need to see better-than-expected office demand and an improved retail sales environment.

"We would also look for above expectation development outcomes on management's identified pipeline," Goldman Sachs said.

Catalysts could include the three sites which GPT has identified as delivering upside — Camellia, near Parramatta, parcels at Sydney Olympic Park and surplus land around Rouse Hill in Sydney.

Holiday homes when only the best will do

RENEE NOWYTARGER

Contemporary Hotels managing director Matthew Fleming in the inner-Sydney suburb of Darlinghurst

TURI CONDON
TRADING ROOM

When Maserati launched its new SUV last year the luxury car brand didn't splash out on a five-star hotel, instead photographers rolled up to Baz Luhrmann's historic Italianate manor, Iona, in inner Sydney.

TV, advertising and film locations along with events have become an offshoot of the luxury home rentals sector, which also caters for a new generation of far more demanding travellers, according to Matthew Fleming, managing director of Contemporary Hotels. The boutique accommodation firm runs a 200-home stable, last year doubling its inventory after buying competitor Luxe Houses, and is considering a separate events division.

In the past few years, the upper end of the market has moved away from the traditional holiday rental "where little things could be forgiven", says Fleming. "Instead, there is a demand for perfection, similar to a stay at a five-star hotel."

Guests expect housekeeping that is perfect, a meet and greet on arrival, champagne, a fruit bowl and flowers, says Fleming.

"It's nothing like the old approach where the keys were under the door and linen was in the cupboard."

That "demand for perfection" will only become greater, he believes. "People travel more, people are more inclined to stay in a house rather than a resort and expect it to be better each time. The more you use it, the more you expect of the experience," he says.

The Contemporary Hotels business was founded by former model and creative director Terry Kaljo who, in the mid 1990s started with a letter box drop in Sydney's Palm Beach to see if owners would rent their homes.

In 1996, she bought Rockridge, a four-bedroom house above Palm Beach, later adding a home near Port Douglas and one on Bedarra Island. The family owns four homes and two apartments, with a farm stay near Berry to be added. "If I can prepare it in time," says Fleming, who is Kaljo's son.

"This (the farmstay) was my investment, we bought a 100 acre dairy farm on the south coast and it will be part of the letting pool at some stage, but the family are enjoying it too much."

The vast majority of the portfolio is managed on behalf of the homeowners, with many being full-time holiday rental properties where the calendar is managed on a weekly basis, rather than rented a few weeks or months a year when the owners are on holidays themselves.

At the top of the company's stable is Eclipse, a modern five-bedroom ocean front at Palm Beach on Sydney's northern beaches that rents for $35,000 a week in the high season.

There is also a batch of homes designed by high-profile architects including a Harry Seidler house in the NSW southern highlands and Peter Stutchbury's "Invisible House" in the Blue Mountains.

The family also own the 18-room Medusa hotel in Sydney's Darlinghurst and owned the 40-room Kirketon nearby until its sale in 2004.

"If another hotel opportunity presented itself, we would take it," says Fleming. "But the luxury holiday rental industry is growing at such a dramatic pace," he adds, noting that the immediate focus is on managing the up-market holiday homes.

Fleming started out at the Medusa and the Kirkton, "putting legs on beds and housekeeping", later working for the Commonwealth Bank for six years mostly in trading, and moving to Japan in 2009 managing holiday properties for a resort in Niseko.

"When I found my way back here, I found a market I had gained a passion for," he says.

Fleming only expects the holiday rental market to grow. "My generation and younger than me, they are not investing in property, they are investing in experiences," the 36-year-old says.

"With the price of real estate, owning a home is pretty much dead and buried ... for a little while at least."

Golden Age to offload 'Paris end' Sheraton

HOTELS: Developer Golden Age has put the Sheraton Hotel Melbourne on the block for up to $140 million as it looks to reshuffle its holdings after buying another major site in the city.

Golden Age, owned by Chinese-born Jeff Xu, last month snapped up an adjacent site in Melbourne's Spring Street from private developer Grocon for about $75m.

Selling the completed hotel will allow the company to cash in on the rising value of hotel assets and help it fund its new projects in Melbourne and Sydney.

The Sheraton is considered a prize of the city's hotel market and sits at the "Paris end" of Little Collins Street, near the city's celebrated laneways that house top shops, restaurants and the city's main theatres.

It has 174 rooms and also features an indoor heated pool, a fitness centre, a day spa and 660 square metres of function space.

The hotel is part of a larger 32-storey mixed use development that also houses 142 residential apartments, and a further 44 luxury residences and penthouses in the top six floors of the tower. JLL's Mark Durran is handling the hotel sale.

Golden Age's purchase of the adjacent site from Grocon could allow it to undertake a new $300m mixed use hotel and apartment project and was seen as a mark of its confidence in the city's unit market even as lenders and regulators take a more cautious stance.

Since 2006, Golden Age's property arm has amassed $3 billion in residential and commercial projects in Melbourne and Sydney. Projects include the Melbourne central business district's tallest residential tower, Victoria One, as well as the luxury Collins House on Collins Street, a 57-level, pencil thin tower.

Developments in Sydney include a site in Sydney's leafy Double Bay and towers in The Rocks and others at Waterloo and Macquarie Park.

Golden Age managing director Mr Xu said: "We're very pleased to be offering this exciting opportunity to purchase one of Melbourne's most prestigious and contemporary hotels," he said.

The Sheraton was the group's first major project and was developed on the old Naval and Military Club sites.

BEN WILMOT

Japanese buy Waldorf majority

DEALS: One of Japan's largest rental housing management outfits has acquired a majority stake in the privately owned Waldorf Australia and New Zealand in an off-market deal.

Japan's Daiwa Living Management, together with Cosmos Initia, bought 75 per cent of Waldorf for an undisclosed sum, despite the growing popularity of Airbnb in Australia.

The deal was expected to be announced in Japan shortly.

Waldorf lets more than 1500 serviced apartments to holidaymakers and corporate travellers in Sydney, the NSW Central Coast, Canberra, Leura, Geraldton, Perth and Auckland.

Founding Waldorf director and chief executive Avi Rubinstein said he would retain 25 per cent of Waldorf, adding that Airbnb had no effect on the company's operations.

"Airbnb is not really having an effect. We are a serviced apartment and real estate company, which is slightly different from a hotel operation. In some complexes we are managing our Airbnb owners arrangements, it definitely does not affect us," Mr Rubinstein said.

DLM and Cosmos Initia are subsidiaries of Daiwa House Industry, Japan's largest publicly listed construction and development company, which manages about half a million rental properties in Japan.

"The sale to DLM group will bring forward our plans to further improve services and allow the business to expand significantly in the coming years," Mr Rubinstein said.

"We expect to grow our business to more than 5000 apartments in time and this will greatly enhance our brand awareness and increase our competitiveness."

DLM has been seeking an opportunity to enter the Australasian market for some time.

Mr Rubinstein will continue his involvement in the business with the main focus acquiring new properties.

LISA ALLEN

W Hotel adds more prestige to Collins Arch precinct

BEN WILMOT
LISA ALLEN
LEISURE

Global hotel chain Marriott International will add a funky W Hotel to Melbourne after striking a deal with developer Cbus Property to open a hotel in the $1 billion-plus mixed-use luxury Collins Arch precinct within three years.

The pre-sale of the W-branded hotel to Japan's Daisho group for more than $200 million is one of Melbourne's largest single hotel transactions. The deal significantly decreases risk for the project for Cbus and could spark presales of apartments in the complex and also add prestige to the office component of the project.

The acquisition of the deep-pocketed Japanese investor was flagged by *The Australian* last year and marks the second W hotel brand in Australia, with Brisbane to sport a new W by year end.

Cbus Property chief executive Adrian Pozzo said the W Hotels brand, together with Daisho Development Melbourne as hotel owner, befitted the project, which he believes will help transform Melbourne. "As a global symbol of style and luxury, W Melbourne will bring dining and function facilities benefits that will further enhance the precinct for not just hotel guests but residents, tenants and Melbourne locals," he said.

The W Melbourne will sport 294 rooms across 15 levels, including 40 suites, as well as a cocktail bar, restaurant, day spa, pool, gym, conferencing and ballroom facilities.

The hotel deal, brokered by Michael Simpson of Savills, was signed off last year. It will see Daisho, which also owns Sydney's Park Hyatt, commit to buying the completed property.

"This is a globally significant deal, bringing a world-class hotel brand in W Hotels to Melbourne's most ambitious architectural project, set to be a world-class destination for Melbourne visitors and locals alike," Mr Simpson said.

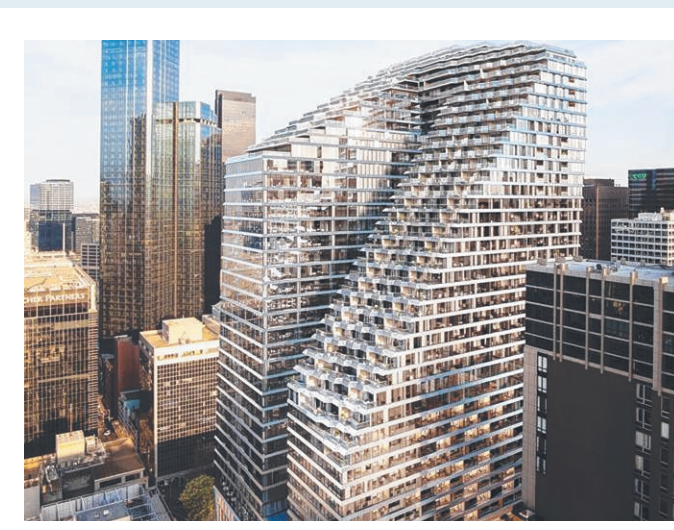
The Collins Arch hotel deal was hotly contested by investors, with several luxury brands also showing interest.

The W Melbourne at Collins Arch will be located in the eastern tower of the landmark dual tower project.

Marriott International vice-president Australia, New Zealand and Pacific Sean Hunt said the group was also talking with Grocon and Chinese-backed Greaton to bring a W Hotel to Darling Harbour in Sydney as part of the $700m The Ribbon project.

Mr Hunt said a group had signed a letter of intent to open a W, but he would not be drawn on further details.

"We're extremely excited to be working with Daisho Development Melbourne and Cbus Property to bring a second W Hotel to Australia," Mr Hunt said.



An artist's impression of the Collins Arch precinct in the Melbourne CBD that will include a new W Hotel