AUSTRALIA'S
ROAD TO RECOVERY
INDUSTRIAL LAND VALUES

CUSHMAN & WAKEFIELD

Industrial land values surge across Australia

Industrial land values have surged over the past year, with many precincts reporting double-digit increases. This article will highlight some of the forces that are driving the increases in industrial land prices across Australia.

Over the last year, industrial land prices have risen sharply, more than what would be expected given the commiserate movement in rents. An unweighted average of Cushman & Wakefield data shows that land prices are up 37% over the past 12 months in Sydney, 35% in Melbourne and 21% in Brisbane.

In some sub-markets, such as Sydney's west and Brisbane's north, the price of land is up close to 50% over the past year. In Melbourne's west, the price of land is up 65% year on year (YoY). Rents have also risen over this period, but with few exceptions most markets have only experienced single-digit increases in net face rents. So, what has driven the spike in land prices if not rents?

Even prior to the COVID-19 pandemic, a structural shift was underway for the industrial sector, driven by the rise of e-commerce, increased technological adoption and growing integration of global supply chains. All of these factors, as well as the tsunami of yield-chasing capital that supported commercial real estate markets more widely, were a tailwind for industrial assets.

However, as are most structural phenomena, the change was relatively slow moving. According to data from Real Capital Analytics (RCA), between 2015-2019 industrial transaction volumes were fairly stable: the rolling four-quarter transaction volumes nationally held around $9 billion over this period. According to data from MSCI, average yields compressed by almost 200 basis points (bps) over the same period (from ~7.6% to ~5.7%), outpacing the office sector over the same period, which compressed 160 bps from 6.8% to 5.2%.

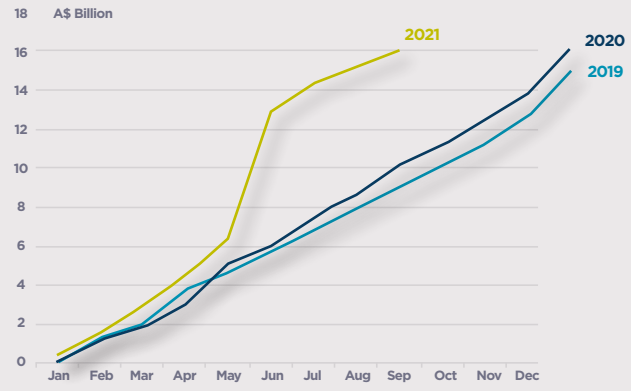
The pandemic abruptly changed this. Those that were slower to adopt online shopping were forced to during lockdowns; as a result, a change unlikely to be reversed for purchasing many goods. A forced shift to working from home highlighted the need for many businesses to increase investment in technology, especially those that had relatively low technological uptake in the days leading up to the pandemic. And risks to supply chains were apparent as demand for goods spiked. In short, the pandemic forced a gradual adjustment to happen all at once.

Markets recognised this.

"In 2019, monthly industrial investment volumes averaged $1.25 billion. This moved up to $1.37 billion in 2020, and has jumped to $2.0 billion in 2021."

Even excluding the $3.8 billion Blackstone portfolio sale to ESR, monthly investment volumes still average $1.5 billion in 2021.

Chart 1: Cumulative Australian industrial property investment volumes (A$, billions)

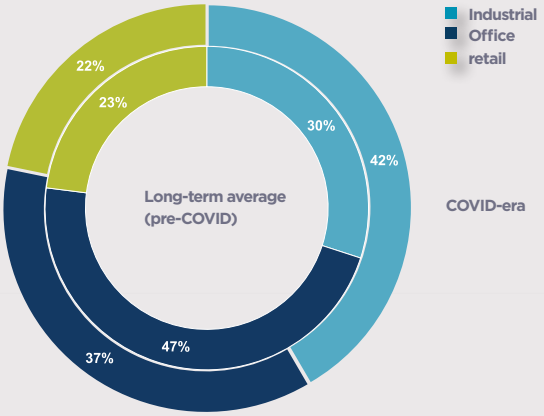


Source: Real Capital Analytics, Cushman & Wakefield

The greater interest in industrial assets is evident when looking at investment volumes. Chart 2 shows that prior to the pandemic, industrial transactions accounted for roughly 30% of investment volumes. Since the onset of COVID-19, this has jumped to 42%, mainly at the expense of office volumes.

“ The global weight of capital has survived the pandemic unscathed – it is just being aimed at different targets. ”

Chart 2: Share of investment volumes



Source: Real Capital Analytics, Cushman & Wakefield

There are flow-on effects from this type of investment. Consider the case of the Qantas portfolio sale in Sydney, which recently sold for $800 million. The portfolio attracted 18 bidders and was awarded to LOGOS. This leaves 17 bidders, with potentially hundreds of millions of dollars' worth of capital to allocate to the burgeoning industrial sector, left looking for other opportunities. In order to satisfy this uplift in demand, developers actively seek industrial land. However, the amount of land that has been made available for industrial development since COVID-19 has not been sufficient to absorb this spike in demand. The result is familiar to anyone who has taken Economics 101: when demand exceeds supply, prices rise.

This dynamic is currently driving industrial land markets across Australia. At some point, the higher cost of land will be passed on to tenants in the form of higher rents. This may happen more gradually but given the low level of industrial vacancy it is almost certainly going to occur. It is important to note that the COVID-19 pandemic has accelerated a structural change rather than being a one-time shock. Thus, it is unlikely that demand for industrial property will revert to pre-COVID levels, this is likely the 'new normal'. Until more supply is made available, the upward pressure on land prices will remain.

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