Adelaide

Apartment Market

Australia Residential Research | August 2020

Overview

Like all major markets, the COVID-19 pandemic has dampened confidence within Inner Adelaide's apartment market. Nevertheless, prices for Adelaide residential have remained relatively steady through the initial months of the outbreak. Capital values and rental growth will be tested in the coming months as a moderating economy will likely soften demand during a period of elevated supply.

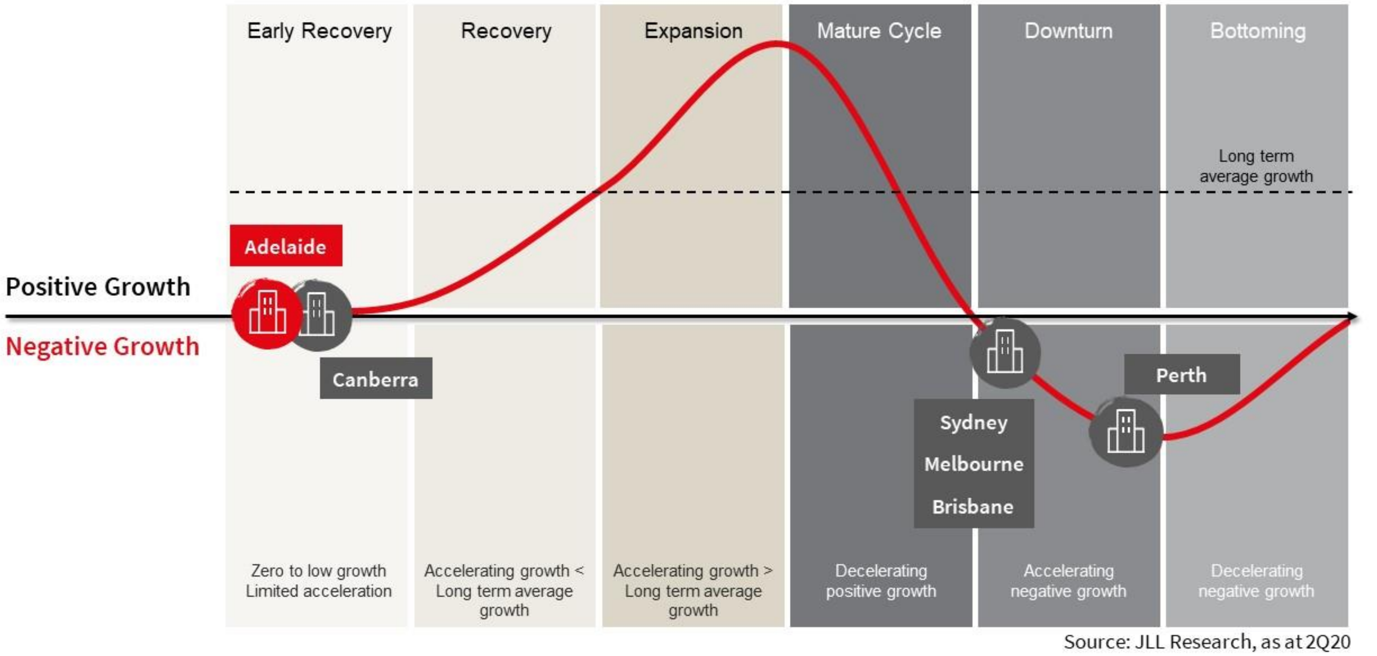
- Economic growth has taken a substantial hit in light of the pandemic, with Deloitte Access Economics (DAE) forecasting SFD growth of-4.1% in 2020. Nevertheless, the SA economy is expected to rebound, averaging 2.4% p.a. between 2021 and 2025.
- Demand for Inner Adelaide apartments recovered strongly from mid-2019 lows, with apartment sales increasing 15.3% over the year to Mar-20. Current sales data does not reflect the impact of COVID-19. As such, transaction volumes are expected to fall over the coming quarters.
- Supply within the Inner Adelaide apartment market is expected to pick up significantly over 2020, with more than 1,200 apartments due to complete by the end of the year, a 65% increase on 2019.
- CoreLogic's Hedonic Home Value Index data shows an increase of 2.9% for units and 2.4% for detached houses, over the year to Jul-20.
- We expect apartment price growth within Inner Adelaide to be limited through the second half of 2020 due to economic uncertainty surrounding COVID-19 and elevated levels of new supply.

Key Market Indicators: Inner Adelaide

Indicator	Latest	Y-o-Y % Change
Apartment Approvals (12 months to May-20)	953	18.7%
Sales Volumes – Units* (12 months to Mar-20)	1,371	15.3%
Median Unit Price*^ (as at Jul-20)	$332,975	2.9%
Median Rent – 1 bed (as at Mar-20)	$329	7.9%
Median Rent – 2 bed (as at Mar-20)	$350	1.4%
Median Rent – 3 bed (as at Mar-20)	$455	-1.1%
Gross Yields^ (as at Mar-20)	5.1%	16 bps

* New and Existing
^ Greater Adelaide
Source: JLL Research, ABS, CoreLogic, REIA

Australian Apartment Market: Capital Value Cycle



Source: JLL Research, as at 2Q20

Economic Overview

The SA economy will be challenged as Australia enters its first recession in nearly 30 years

The SA economy was operating below trend prior to the COVID-19 pandemic, recording SFD growth of -1.0% over the year to Mar-20, below national Gross Domestic Product (GDP) growth of 1.4% over the same time period. Economic conditions will deteriorate further due to the pandemic, with Deloitte Access Economics (DAE) forecasting SFD growth of -4.1% in 2020. Nevertheless, the downturn should be short with the SA economy expected to rebound in 2021 and average 2.4% p.a. between 2021 and 2025.

The South Australian unemployment rate sat at 8.8% in Jun-20, 1.7 percentage points (pps) higher than Jun-19. National unemployment reached 7.4% in June. More than 37,000 South Australian jobs have been lost since lockdown measures were implemented in March. The Federal Government announced in July that the JobKeeper payment will be extended to 28 March 2021, with a tiered system to be implemented from 27 September 2020. The Government also announced an AUD 25,000 HomeBuilder grant for eligible owner-occupiers to build a new home or substantially renovate an existing home to assist the residential construction industry.

SA retail turnover fell 14.5% m-o-m in April at the depths of the lockdown period. Spending rebounded 16.1% month-on-month (m-o-m) in May 2020, as lockdown restrictions eased and retailers recommenced trading. Retail spending has since stabilised with a 1.3% m-o-m increase in June. Annual turnover growth was 2.8% in June, just below the national rate of 2.9%.

The state's population growth, coming largely from overseas migration, was just 0.9% over the year to Dec-19, compared to the national average of 1.4%. Indefinite border closures will bring a temporary halt to immigration. This will test the rental market, which is heavily dependant on the influx of international students for the university semester.

The RBA cut the cash rate by 25 bps at its March 2020 meeting before a further 25 bps rate cut was announced following an emergency meeting on March 19th in response to the COVID-19 outbreak. The cash rate now sits at a historical low of 0.25%, 125 bps lower than May 2019. With interest rates now likely at their lower bound, the RBA has also commenced quantitative easing measures for the first time to support the economy and financial market liquidity. In total, the Federal Government and RBA has delivered around AUD 320 billion in stimulus packages, equating to 16.4% of annual GDP.

Key Economic Indicators - South Australia

State Final Demand Growth
-1.0% **Year Ended Mar-20**

Population Growth
0.9% **Year Ended Dec-19**

Retail Turnover Growth
2.8% **Year-on-Year Jun-20**

Employment Growth
-4.4% **Year Ended Jun-20**

Demand

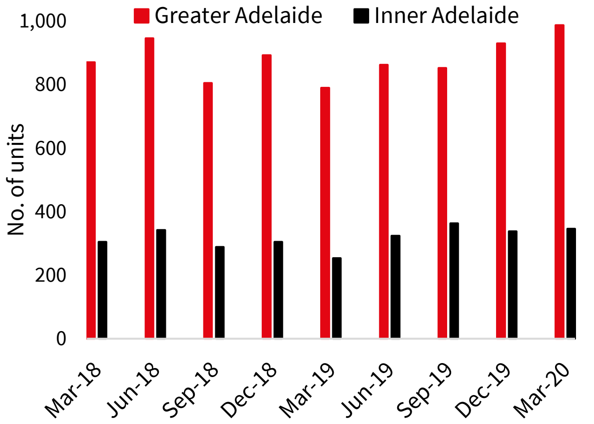
Apartment demand will likely soften over the short-term

Current data does not yet reflect the impact of COVID-19 on sales activity. As such, transaction volumes are expected to fall over the coming quarters.

In the Mar-20 quarter, 346 new and existing apartments were transacted within Inner Adelaide, up 2.4% from the previous quarter. Around a third of sales occurred in the CBD, down from 50% in Sep-19. Across Greater Adelaide, 987 apartments were sold in the Mar-20 quarter, an increase of 6.1% q-o-q.

Rolling annual data shows an upward trend in Inner Adelaide sale volumes since mid-2019. A total of 1,371 units were transacted over the year to Mar-20. This figure is about 15.3% higher than the year prior. For the Greater Adelaide area, 3,632 units were transacted in the year to Mar-20, up 5.8% from the prior year.

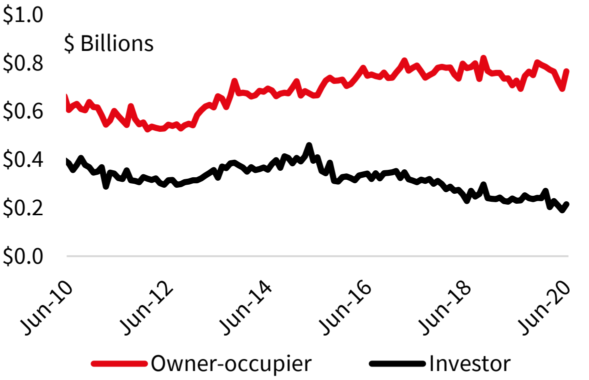
Figure 1: Quarterly Sales Volumes (New and Existing)



Source: CoreLogic, JLL Research as at Mar-20

The value of housing finance commitments is a leading indicator for housing demand and provides a more timely picture of the current climate. South Australian housing finance commitments reveal a brief softening in demand in the initial months of the pandemic. The value of approvals for owner-occupiers fell in April (-5.1% m-o-m) and May (-4.5% m-o-m), before rebounding in June (10.6% m-o-m). The value of owner-occupier approvals are 5.4% higher than Jun-19. Similarly, the value of approvals for investors fell in April (-8.1% m-o-m) and May (-9.3% m-o-m), before a strong recovery in June (12.8% m-o-m). The value of investor approvals are 6.6% lower than Jun-19.

Figure 2: South Australia Housing Finance Commitments



Source: ABS, JLL Research

Supply

Supply levels remain elevated, but will moderate in 2021

More than 700 new apartments have been completed in the Inner Adelaide apartment market over the first half of 2020, on par with the number of completions over the entirety of 2019. A further 530 units are expected before the end of 2020, bringing the annual total to just under 1,250 units.

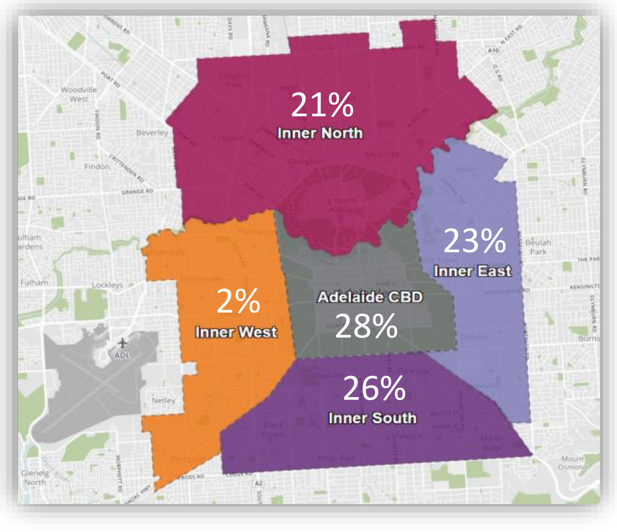
Development activity has been concentrated within the Adelaide CBD, accounting for 77% of new completions in 1H20, followed by the Inner East (19%) and Inner North (4%) precincts. Conversely, there is an even spread of the 1,200 units currently under construction (see Figure 3).

The three projects that reached completion in 2Q20 were:

- Realm Adelaide, Adelaide CBD – 310 units,
- Adelaidean, Adelaide CBD – 88 units; and
- Glenside Apartments, Glenside (Inner East) – 134 units.

Construction will cool off beyond 2020, with around 500 units in primarily smaller boutique developments on track for 2021 completion. Project timelines for around a third of developments previously set for 2021 completion have been pushed out, as COVID-19 economic uncertainty softens demand. Many projects that are in the early stages of marketing or at the development approval stage, could slip into later years or be abandoned if sufficient pre-sales are not achieved and economic conditions do not improve.

Figure 3: Inner Adelaide Apartment Market Precinct Map (% Under Construction, as at 2Q20)

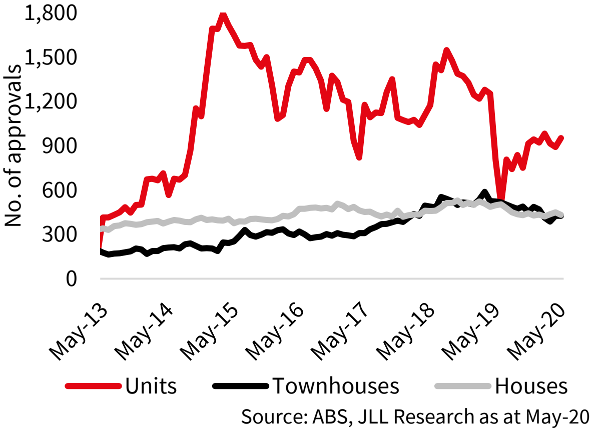


Across Inner Adelaide, there are more than 2,800 apartments in the pipeline (those under construction, currently marketing, with DA approval or plans submitted). Approximately 33% of those are located in Inner North precinct, followed by the Adelaide CBD (29%), Inner East (16%), Inner South (15%) and Inner West (7%).

Figure 4: Inner Adelaide Supply Pipeline by Status

Given the elevated levels of new stock coming to market, the number of building approvals plummeted over the first half of 2019, falling to just 507 units over the year to Jun-19. Since then, approval activity has trended upwards, with Inner Adelaide building approvals for the year to May-20 totalling 953 apartments, an 18.7% increase on the prior year. The Adelaide CBD and the Inner Eastern suburb of Norwood continue to attract the bulk of development interest, accounting for 51% of new approvals in the year to May-20.

Figure 5: Inner Adelaide Rolling Annual Building Approvals



Source: ABS, JLL Research as at May-20

Figure 4: Supply Pipeline by Stage and Precinct, 2020-2024 (Number of Apartments, as at 2Q20)

Stage	Adelaide CBD	Inner North	Inner East	Inner South	Inner West	Total
Completed (2020YTD)	548	27	134	-	-	709
Under Construction	347	267	284	329	28	1,255
Currently Marketing	98	-	-	-	-	98
Plans Approved	239	117	105	58	126	645
Plans Submitted	141	575	58	45	54	873
Total	1,373	986	581	432	208	3,580

Source: JLL Research, as at 2Q20

Pricing

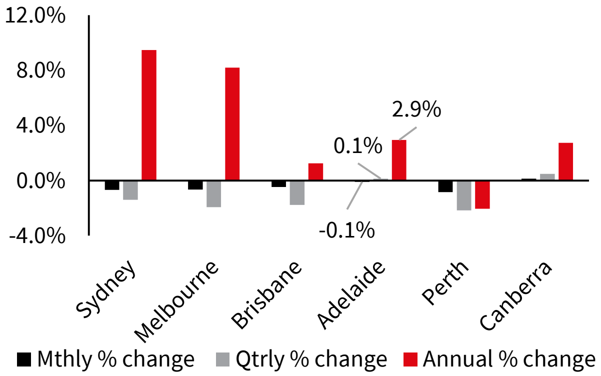
Positive price growth has stalled, but Adelaide's residential market has fared better than most other markets

Adelaide's residential market has held relatively steady through the initial outbreak of the COVID-19 pandemic, with apartments recording a 0.1% increase over the three months to July – outperforming the five main capitals. By comparison, Sydney (-1.4%), Melbourne (-1.9%), Brisbane (-1.8%) and Perth (-2.1%) all recorded price falls.

Despite the exponential spread of COVID-19 across Australia from mid-March, Adelaide unit prices maintained an upwards trajectory through to May. The first signs of a weakening market appeared in June with prices falling 0.3% m-o-m, followed by a 0.1% m-o-m fall in July. CoreLogic's Hedonic Home Value Index indicates Adelaide apartment prices have risen 2.9% over the year to Jul-20. Comparatively, house prices increased 2.4% over the same period. A softening economy, border closures and high levels of new supply are likely to put pressure on South Australian inner city apartment prices through the second half of 2020.

Adelaide's residential market continues to offer great value relative to other markets. Adelaide apartments are among the cheapest in the country, second only to Darwin. By comparison, in Jul-20, the median unit in Adelaide is valued at $332,980, compared to $747,240 in Sydney and $572,850 in Melbourne. A similar trend can be seen in the detached housing market with the median house price in Adelaide sitting around $478,180, compared to $1,002,100 in Sydney and $793,550 in Melbourne. This affordability, combined with SA's success in controlling the outbreak should help to limit downside pricing risk.

Figure 6: Annual Unit Price Growth (%)



Source: CoreLogic, JLL Research as at Jul-20

Rental Vacancy and Rents

Border closures will likely temper the tight Inner Adelaide rental market

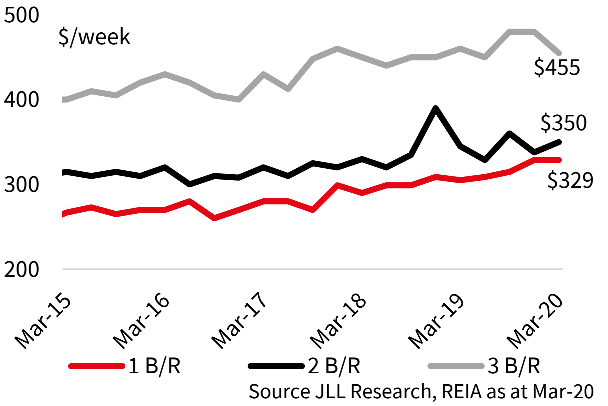
According to SQM research, the vacancy rate across Greater Adelaide sits at 1.0% as at Jun-20, down 0.2 percentage points from Jun-19. This is the lowest vacancy rate of all capital cities around the country. Generally, a vacancy rate of 3% is regarded as a balanced market, suggesting a supply shortage in the Greater Adelaide rental market.

Rental vacancy in the Adelaide CBD ebbs and flows with the tide of international students migrating to the city for the university semester. The influx of new supply, coupled with border closures due to the pandemic, has caused a spike in availabilities within the Adelaide CBD. According to SQM Research, the CBD vacancy rate sits at 6.2% as at Jun-20. By comparison, vacancy in Mar-20 was just 2.7%. In the two months following the border closures, the CBD vacancy rate spiked 4 pps to 6.7% (May-20).

Low vacancy rates and steady population growth has led to modest rental growth over the last few years. REIA data reveals the median rent for a 2-bedroom unit within Inner Adelaide rose 1.4% over the year to Mar-20. However, current REIA data does not reflect the impact of COVID-19 on the rental market. According to SQM research the spike in vacancy within the Adelaide CBD has led to a 2.9% decline in asking rents over the 3 months to Jun-20.

Vacancy rates in the Adelaide CBD will likely remain elevated until borders are re-opened to international students. This combined with relatively high levels of new supply, are expected to place downward pressure on rents.

Figure 7: Median Rent – Inner Adelaide by No. of Bedrooms



Source JLL Research, REIA as at Mar-20

Recent completion: Realm Adelaide

Completed in mid-2020, Realm Adelaide becomes Adelaide's tallest residential building, at 132m above the Adelaide CBD skyline. Located on Austin Street, the 40-storey development includes 310 luxury apartments. One of the two penthouses sold for AUD 5.2 million, setting set a record for the most expensive apartment sale in Adelaide.

Gross Rental Yields

Rental yields increased over the year, but will come under pressure due to rental market headwinds

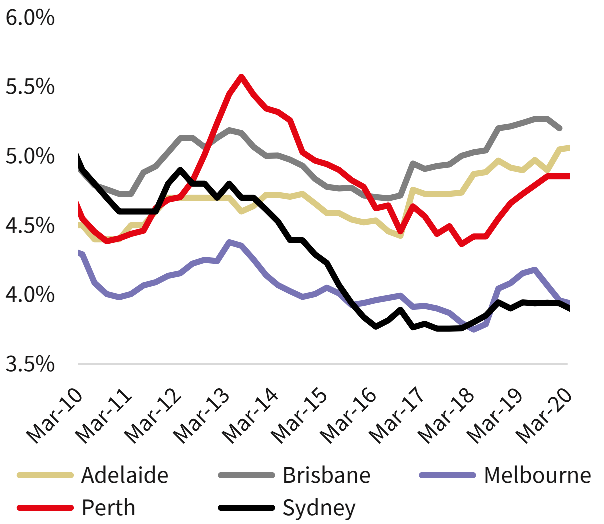
Gross rental yields for units across Greater Adelaide fell marginally (1 bps) over the Mar-20 quarter. Nevertheless, yields sit 16 basis points higher than this time last year at 5.1%. By comparison, gross rental yields declined in Sydney (-5 bps), Melbourne (-22 bps) and Brisbane (-4 bps) over the year to Mar-20. This has been a result of improving capital values through the turn of the year.

Yields in Adelaide remain above those in markets such as Sydney (3.9%), Melbourne (3.9%) and Perth (4.9%), but below Brisbane (5.2%) and Canberra (5.7%).

Lag in the data has not yet captured the impact of COVID-19 on residential markets over the June quarter. Looking forward, with rents anticipated to come under pressure due to elevated vacancies and high levels of new stock coming onto market, the gross rental yield in the Adelaide CBD is expected to fall. Comparatively, low vacancy across the Greater Adelaide area will likely result in fairly stable yields.

The yield spread between Adelaide residential and the Sydney (117 bps), Melbourne (113 bps) and to a lessor extent Perth (21 bps) markets present a value proposition for investors. This combined with Adelaide's relative affordability, may support investor demand through the recovery.

Figure 7: Gross Rental Yields – Units



Source: CoreLogic, JLL Research as at Mar-20

Site Sales

Inner Adelaide site sales remain limited

There remains a limited number of site sales due to the tightly held nature of the Inner Adelaide area. JLL Research recorded only one major site sales over 1H20, with 200-202 Anzac Highway, Plympton (Inner West) selling with DA approval. Demand for development land remains robust for the growing suburbs of Bowden, Norwood, Brompton, Prospect and Kent Town. These suburbs are attractive for both owner-occupiers and investors due to their close proximity to the CBD and the amenity services offered. Going forward, we expect Brompton and Bowden, and increasingly Kent Town to dominate demand for site sales in Inner Adelaide. However, the Inner Eastern and Southern suburbs, particularly Unley and Norwood, are still highly sought after by developers, albeit attracting a higher rate per square metre on average.

Hot Topic

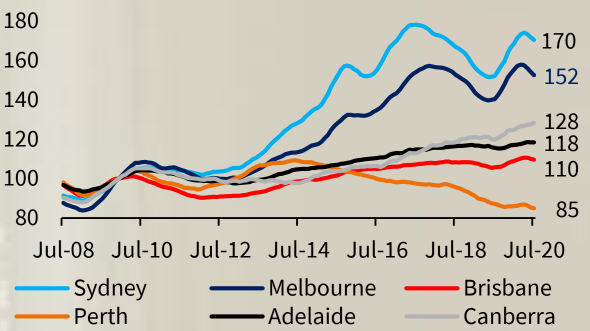
Is the shift to Apartment living over or just beginning?

The last decade has been a period of enormous growth in apartment supply in all Australian markets. This reflects the confluence of a number of economic, demographic and social trends that have seen apartment living accepted in Australia like never before.

This shift has been most evident in Sydney and Melbourne, but also smaller capital cities where there is less population and affordability pressures. The latter of which, many people would think has forced the shift.

However, the facts do not support that affordability is the only driver. Over the last decade, wages grew by around 31% across all major cites, while dwelling prices have grown by around 70% in Sydney and 52% in Melbourne, but by less than wage growth in all other capital cities (See Figure 8). So, given that apartment development has surged in all markets - even in Perth were prices are 15% lower than they were 10 years ago - there must be much more to the trend than just prices and affordability.

Figure 8: Dwelling Price Index (Dec 2009 = 100)



Source: CoreLogic, JLL Research as at Jul-20

Population growth and planning pressures have also undoubtedly also played a role. Australia's population has continued to grow at a very strong 1.6% p.a. over the past decade, faster than other comparable developed economies. Planning authorities have also responded to population pressures by encouraging greater infill density as opposed to greenfield development on the urban fringe.

So all these factors partially explain the shift to apartments, but the big intangible factor is the attitudinal shift among younger generations who have seemingly rejected living on the urban fringe. Instead, many are consciously deciding to maintain the inner-urban lifestyle they have come to enjoy and rent or buy apartments instead of other dwelling types. Older 'empty nester' Australians are also making conscious decisions to downsize into lower-maintenance apartments

The COVID-19 crisis may weaken attitudes to high-density living and disrupt the rise of apartments for a period. However, one potential silver lining is that the crisis may boost the prospects of build to rent (BTR) residential (which is institutionally owned and operated rental stock). With developers in the traditional build to sell market facing a challenging time getting projects going, it is a good time for BTR operators to get a foothold and acquire sites with less competition.

We firmly believe any softening sentiment towards apartment living resultant of the COVID-19 crisis will prove short-term, and that apartments will forevermore be a much greater share of new housing construction in Australia.

Outlook

Economic uncertainty, international border closures and relatively high levels of new apartment supply will challenge Adelaide's inner city apartment market going forward

Adelaide's residential market held steady through an otherwise tumultuous 2019 for most other capital cities. This trend has continued through the first half of 2020, which brought with it a global health and economic crisis leading to Australia's first recession in nearly 30 years.

Nevertheless, the first signs of price falls were seen in the month of June and dampened buyer confidence will likely continue while the SA economy slows, unemployment remains elevated and international borders remain shut. Land tax reform, COVID-19 relief schemes, State and Federal grants will provide some support to housing demand over the short-term and assist in limiting downside pricing risk.

The Greater Adelaide rental market should remain healthy, as low vacancy rates and steady demand support rental growth. A greater risk exists for the Inner Adelaide rental market, which relies on the migratory patterns of international students. Uncharacteristically high vacancy in the CBD will persist until borders are re-opened. The influx of new supply will place further pressure on the Inner Adelaide rental market, but the impacts will be limited due to the low volumes of existing stock in the Adelaide apartment market.

New supply within the Inner Adelaide apartment market will be relatively high over 2020, with around 1,250 apartments to be completed. Supply will moderate in 2021 as economic uncertainty following COVID-19 is likely to soften demand and push out project timelines. Residual stock, elevated CBD vacancy and lending requirements will likely dictate that new developments remain largely demand-led. Many projects that are in the early stages of marketing or at the development approval stage, could slip into later years or be abandoned if sufficient pre-sales are not achieved and economic conditions do not improve.

Adelaide's residential market continues to offer great value relative to other markets, with apartments among the cheapest available in this country. Strong yields compared to the major east coast markets may attract investors seeking to capitalise on investment opportunities as we emerge from the pandemic. This may attract external investor demand, which in turn will limit downside pricing risk, particularly with the state's success in controlling the outbreak.

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