



BRISBANE APARTMENT MARKET REVIEW

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Introduction

In this review, we provide the latest insights on the Brisbane Apartment Market, based on our ongoing research of the market over the past two years.

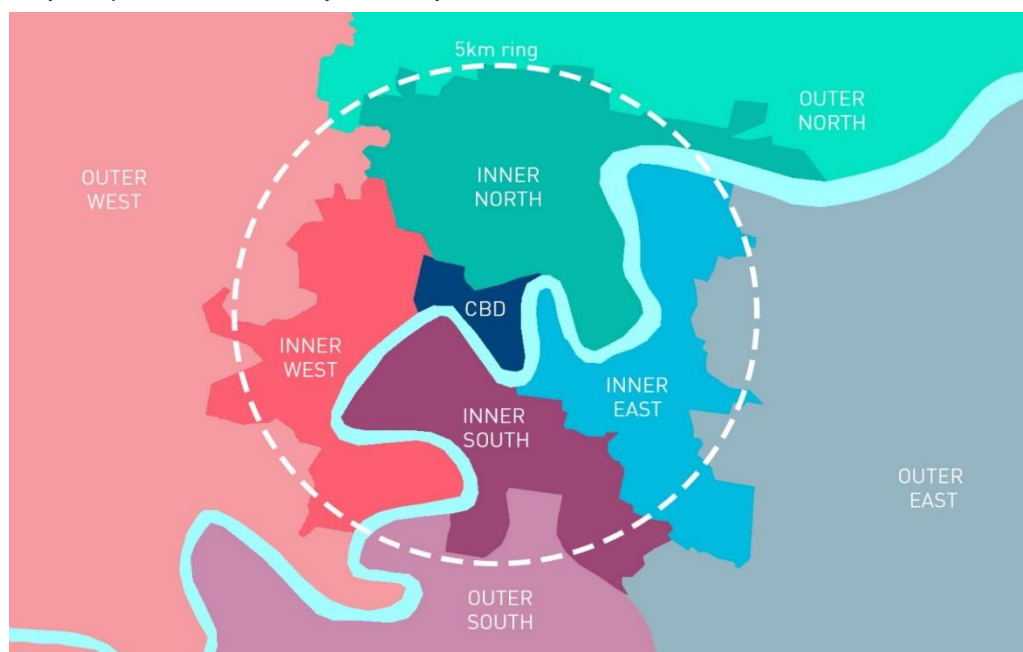
This research emanates from our database of 162 projects of greater than 25 apartments in size, and in turn 19,230 apartments, which are currently under construction or recently completed.

Methodology

In preparing this publication we have collated information from a variety of sources including Core Logic RP Data, Cordells, Queensland Titles Office, developer websites and kerbside inspections.

The data is for residential apartment projects completed during 2017 or under construction at 31 December 2017 with 25 or greater apartments situated in identified localities within 12 kilometres of the Brisbane CBD as shown in the map below. It does not take into consideration development approvals and projects awaiting commencement of construction.

Data has been collated over a period of time and therefore settlements in a number of projects may have subsequently completed or be currently underway.



Inner East

Balmoral, Bulimba, Cannon Hill, Coorparoo, East Brisbane, Kangaroo Point and Stones Corner.

Inner North

Albion, Bowen Hills, Fortitude Valley, Hamilton, Kelvin Grove, New Farm, Newmarket, Newstead, Spring Hill, Teneriffe and Windsor.

Inner West

Auchenflower, Bardon, Milton, Paddington, St Lucia and Toowong

Inner South

Dutton Park, Greenslopes, Highgate Hill, Norman Park, South Brisbane, West End and Woolloongabba.

Outer North

Alderley, Ascot, Aspley, Chermshire, Clayfield, Enoggera, Everton Hills, Everton Park, Gaythorne, Grange, Hendra, Kedron, Lutwyche, McDowall, Mitchelton, Northgate, Nundah, Woolloowin and Zillmere.

Outer South

Annerley, Archerfield, Coopers Plains, Eight Mile Plains, Moorooka, Sherwood, Sunnybank, Yeerongpilly and Yeronga.

Outer East

Carina, Carina Heights, Holland Park, Holland Park West, Morningside, Mount Gravatt, Mount Gravatt East, Murarrie, Seven Hills and Upper Mount Gravatt.

Outer West

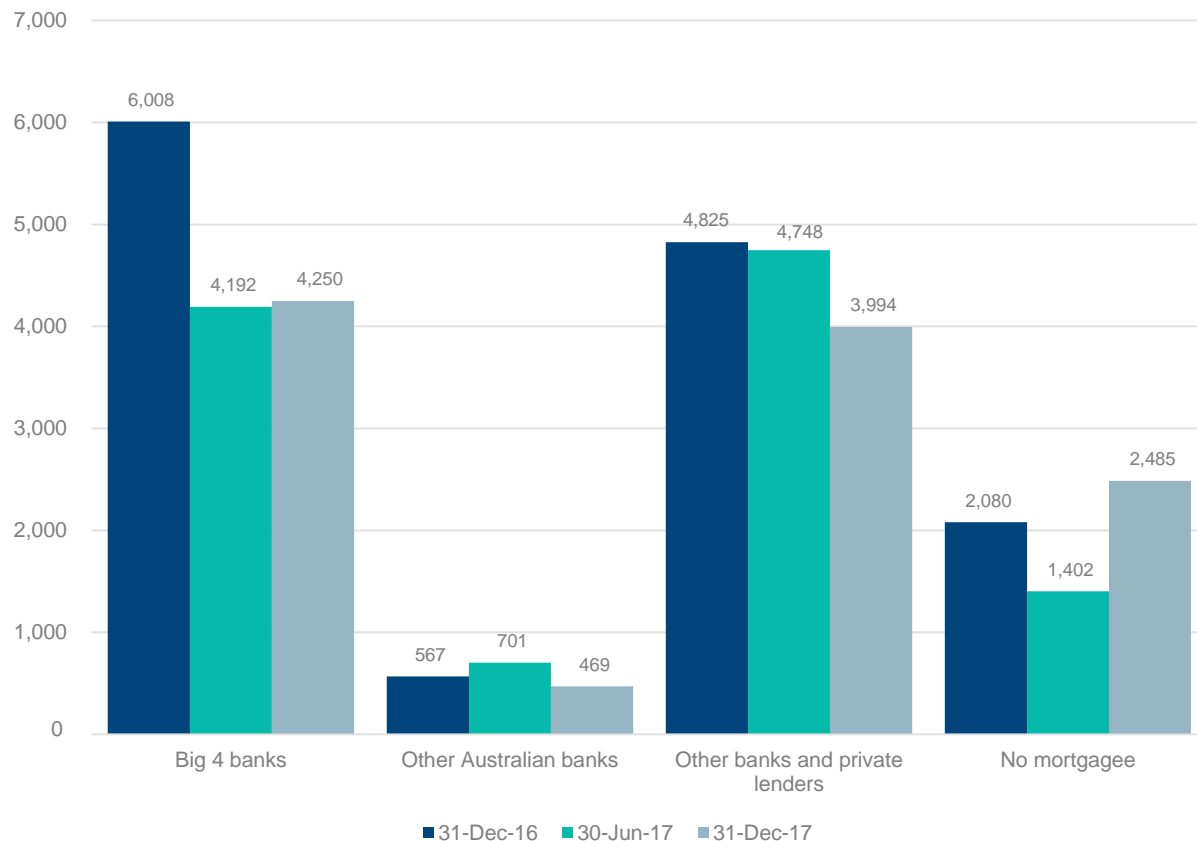
Ashgrove, Enoggera, Indooroopilly, Kenmore, Taringa and The Gap.

Summary

The key findings from our database of 19,230 apartments within 162 projects that were under construction as at 31 December 2017, or were completed during 2017, are:

- 8,032 apartments completed in 2017 with a number of settlements pending, compared to our forecast of 10,169 apartments to complete during 2017 in our report as at 31 December 2016. This decrease can be attributed to slower than expected construction progress across several projects.
- 11,198 apartments were under construction as at 31 December 2017, of which:
 - 7,750 are forecast to complete in 2018
 - 1,967 are forecast to complete in 2019
 - 1,481 are forecast to complete in 2020 and beyond.
- The market is awash with incentives for purchasers ranging from deferred settlement periods to price reductions and other arrangements including vendor finance, payment of stamp duty, furniture packages and rent guarantees.
- An increasing reliance on other financing arrangements with only 38% of financing coming from the big 4 banks. This contrasts to Sydney where our research shows 67% of all apartment projects are financed by the big 4 banks.
- There is a considerable number of projects with no mortgagee, further demonstrating that developers are pursuing alternative methods to fund their projects as the major banks have pulled back, due to highly publicised supply concerns.

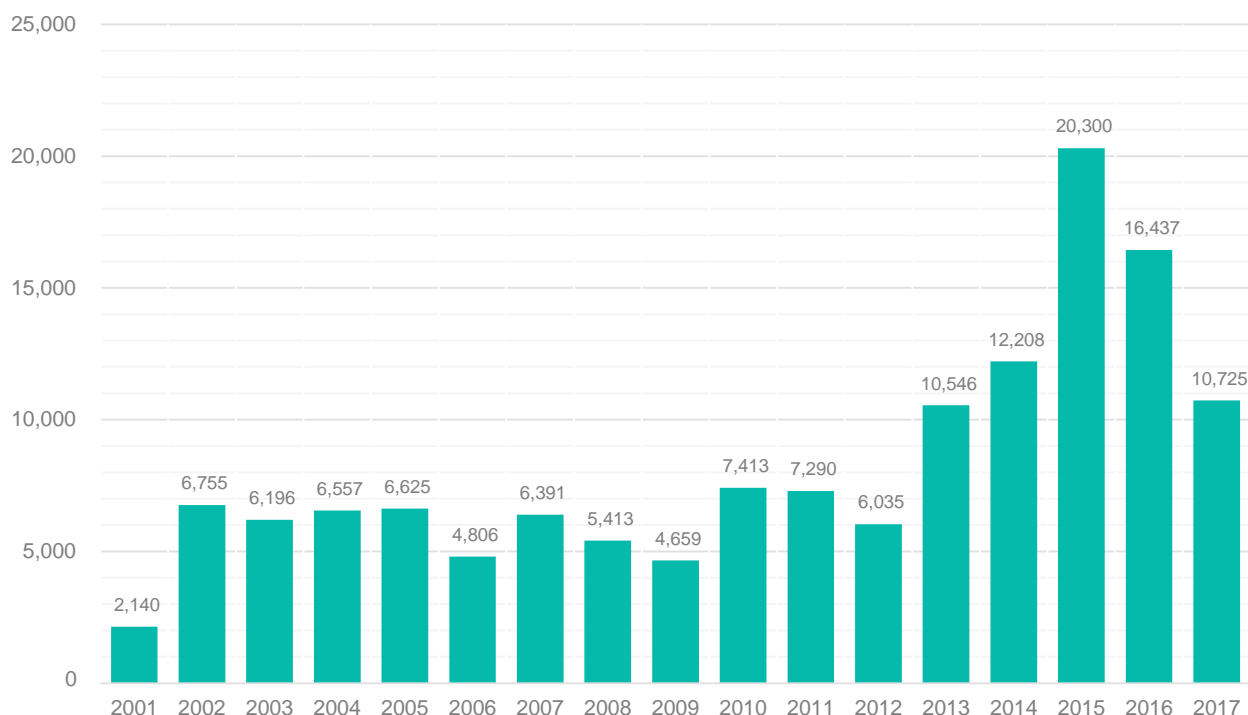
Number of apartments under construction – 12 month comparison by mortgagee



Supply

Building approvals for non-house residential construction in Brisbane decreased for the second year running during 2017, after the substantial increase between 2013 and 2015.

Brisbane building approvals, dwellings excluding houses



Source: ABS

Building approvals peaked in 2015 following the introduction of Brisbane City Plan 2014 which allowed higher density development in areas close to the Brisbane CBD and public transport hubs coupled with increased risk appetite from developers and investors in a low interest rate environment.

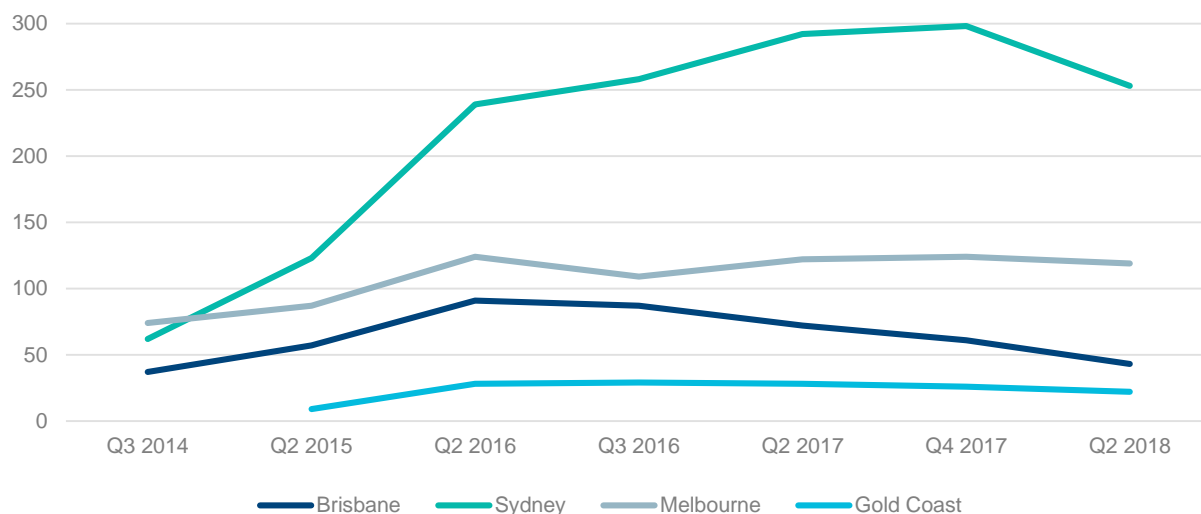
However, as shown above, 2016 and 2017 have demonstrated a steady decrease in approvals. Factors working to constrain future supply, include:

- Oversupply concerns, as evidenced by the level of recent completions with residual unsettled (developer owned) stock
- Increased construction costs
- Expectations for price discounts, following increased provision of marketing incentives.

Based upon available 2018 data we project that building approvals will plateau in the short to medium term. However, given the significant lag time between approvals and apartment completion there remains some time to go before the Brisbane apartment market returns to sustainable levels.

The most recent RLB Crane Index reflects the decrease in activity with the number of cranes used in apartment construction in Brisbane decreasing from 91 (Q2 2016) to 43 (Q2 2018).

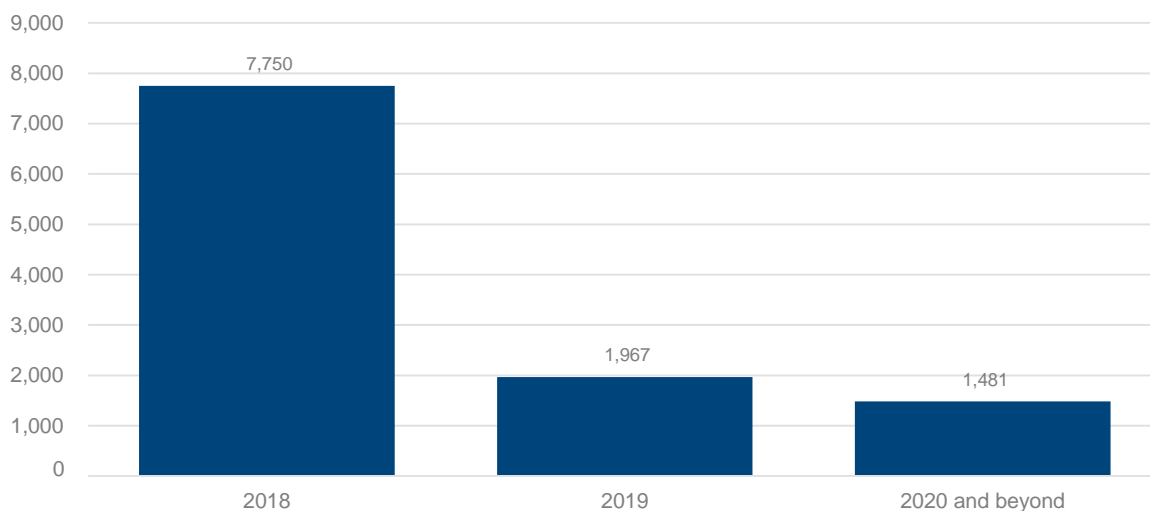
Number of cranes used in residential sector



Source: RLB

While there has been a slow down in approvals, there are still 11,198 apartments within 12km of the Brisbane CBD currently under construction due for completion between 2018 to 2020.

Forecast completion dates



Source: Cordell Connect, Azurium Real Estate

A total of 8,032 apartments were completed during 2017 which compares to our estimate of 10,169 made at the beginning of the year. This decrease is largely the result of slower than expected construction progress on a number of projects.

Project funding

From our research across the Brisbane, Gold Coast and Sydney apartment markets, we have identified the following bank and other financier exposures.

Percentage of apartments under construction – as at 31 December 2017 by mortgagee

Mortgagee	Brisbane	Sydney	Gold Coast
Big 4 bank	38%	67%	28%
Non-Big 4 bank	40%	22%	41%
No mortgagee	22%	11%	31%

Source: Azurium

There is an increasing reliance on other financing arrangements with only 38% of financing coming from the Big 4 banks in Brisbane. This contrasts to Sydney where our research indicates 67% of all major projects (over 50 apartments) are financed by the Big 4 banks.

There is also a considerable number of projects with no mortgagee, further demonstrating developers are pursuing alternative methods to fund their projects as the major banks have pulled back, due to highly publicised supply concerns.

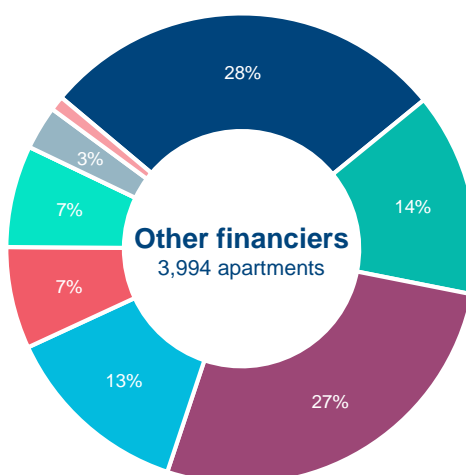
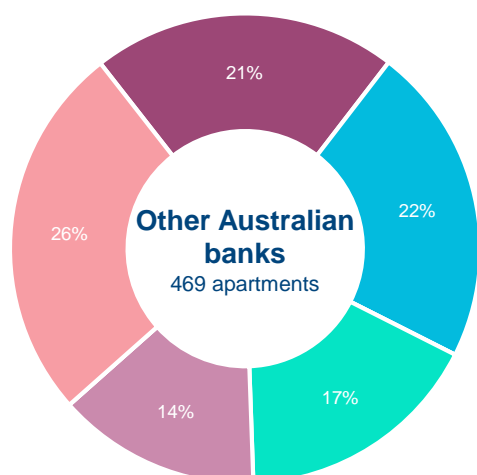
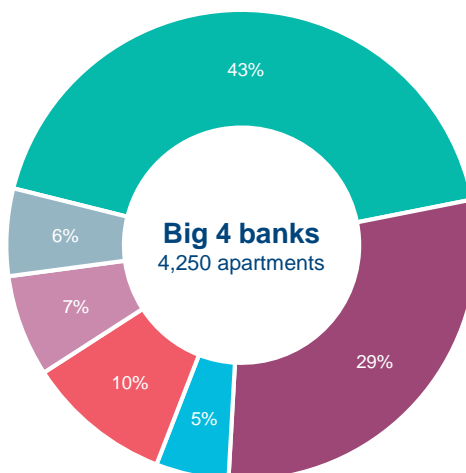
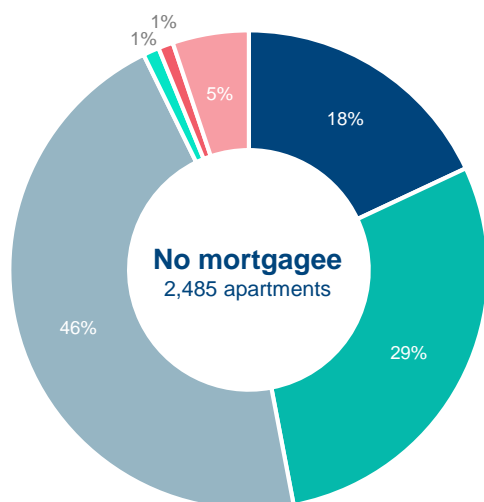
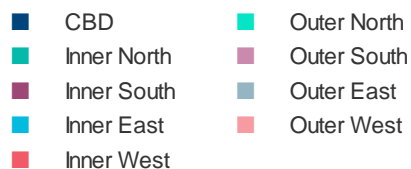
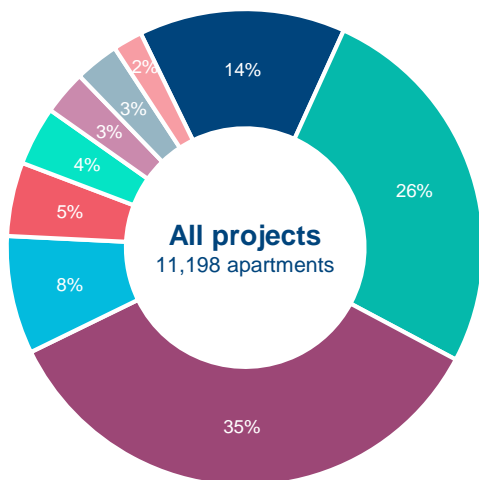
Financier exposure by locality

The charts opposite show the percentage of all apartments under construction by locality.

Our research confirms that the Inner South is the current hotspot for development with the suburbs of West End (742 apartments), South Brisbane (1,821 apartments) and Woolloongabba (991 apartments) seeing considerable new development.

As forecast in our report as at 31 December 2016, the number of apartments under construction in the Inner North has decreased from 32% (4,264 as at 31 December 2016) to 26% (2,926 as at 31 December 2017). This is in part due to the completion of high profile developments, FV – Valley House and Flatiron (combined 594 apartments), Newstead Central – St Tropez and Laguna (combined 420 apartments) and The Yards development (combined 390 apartments). The Big 4 banks in particular have been highly active in the Inner North with 43% of the Big 4 banks' exposure in the Inner North.

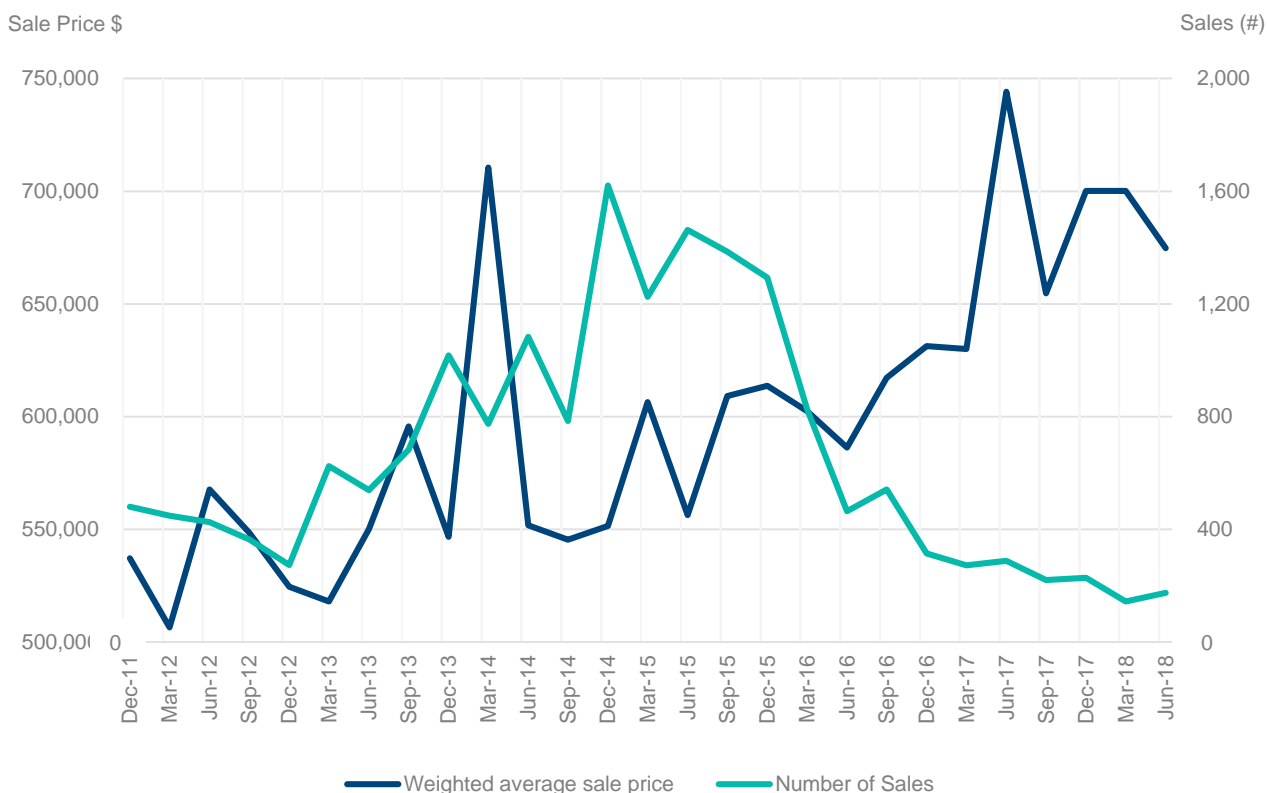
Contrastingly, whilst the number of apartments under construction in the Inner South has decreased from 4,215 (as at 31 December 2016) to 3,879 (as at 31 December 2017), this locality represents the highest percentage of stock under construction (35% as at 31 December 2017).



Demand

The graph below shows the volume of apartments sold from December 2011 to March 2018, together with the weighted average price of apartment sales within Inner Brisbane (0-6km).

Inner Brisbane apartment sales



Source: Place Projects

The weighted average sales price has fallen during the year whilst sales volumes have remained at record lows.

Owner occupier demand has continued relative to investor demand over the past year, noting the peak volume of sale contracts in late 2014 and early 2015, was driven primarily by interstate and foreign investors.

Many of these investors were sourced by investment marketeers who typically charge commissions of 5% to 8% per apartment.

The total cost to some of those developers is up to 14%, once seminar costs are paid and investors are offered various monetary / promotional incentives,

These rental incentives include free Wi-Fi, rent free periods and furniture packages amongst others.

Brisbane does however remain an attractive investment option due to its comparative affordability relative to both Sydney and Melbourne.

Increasing unsold developer stock

There has been increasing concern with regard to settlement risk over the past year.

In order to gain a deeper understanding of this risk for developers and financiers we investigated the number of apartments within completed projects that were yet to settle as at 31 December 2017.

To do this we undertook searches to identify which apartments in projects completed during 2017 were still recorded in the name of the developer as at 31 December 2017. We acknowledge that some of the apartments may be contracted with settlements yet to occur.

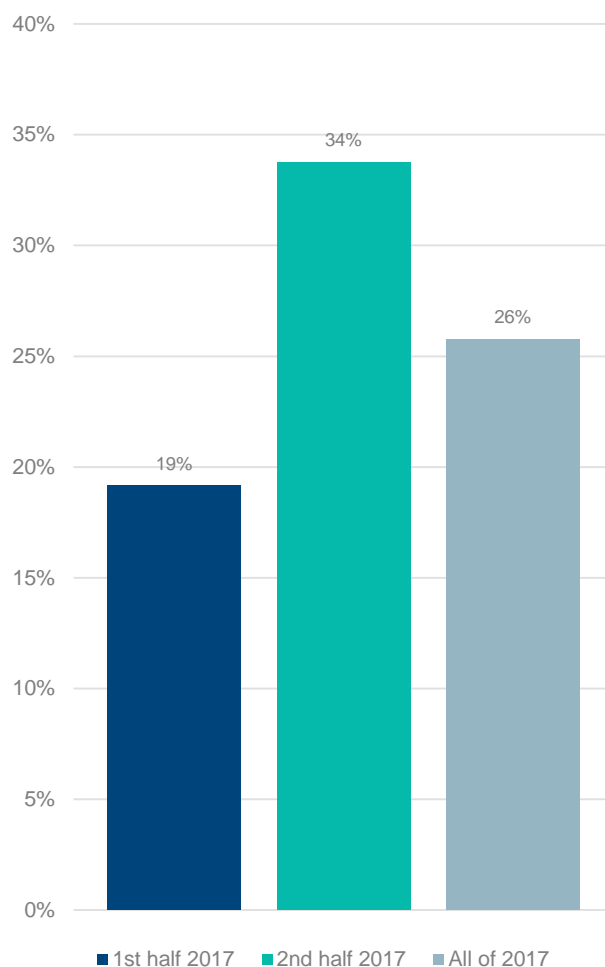
Our findings show that settlements are taking longer to finalise with 19% of apartments completed in the first half of 2017, 34% of apartments from the second half of 2017 and 26% of all apartments completed during the year remaining unsettled as at 31 December 2017.

These settlement delays, at a time of peak debt for the developer, add substantial interest costs, diminishing the return to mezzanine providers and eroding the developer's equity position. We are also aware of developers being charged roll over fees where their facility was not paid back on time.

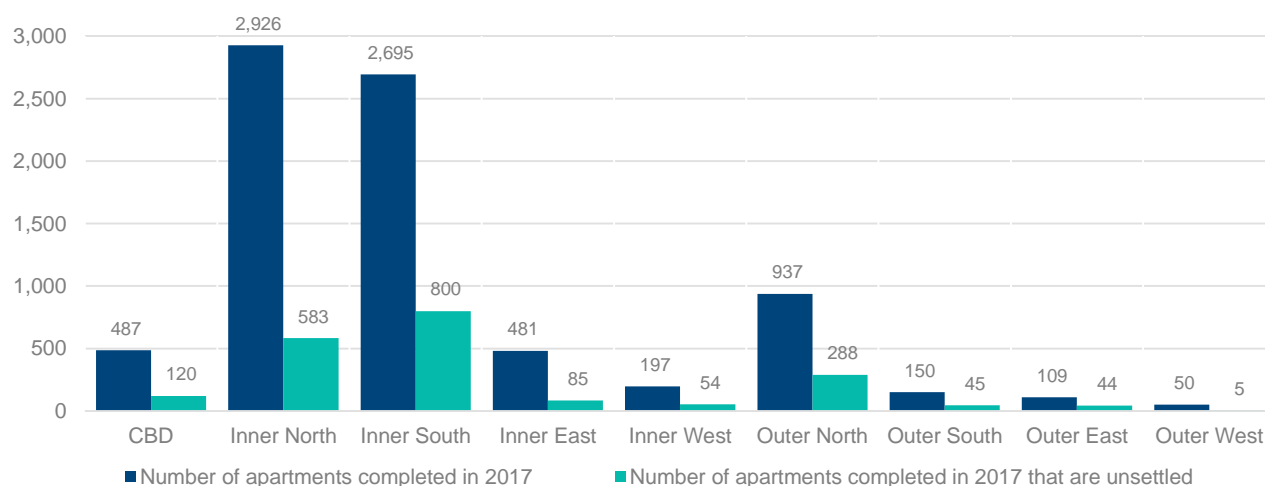
Our research demonstrates that some localities have a higher number of unsettled apartments. In particular, the following suburbs have the highest number of unsettled apartments as at 31 December 2017:

- South Brisbane (410 apartments)
- West End (280 apartments)
- Chermside (181 apartments)
- Albion (141 apartments)
- Bowen Hills (121 apartments)

Unsettled apartments as at 31 December 2017 as a percentage of total apartments completed



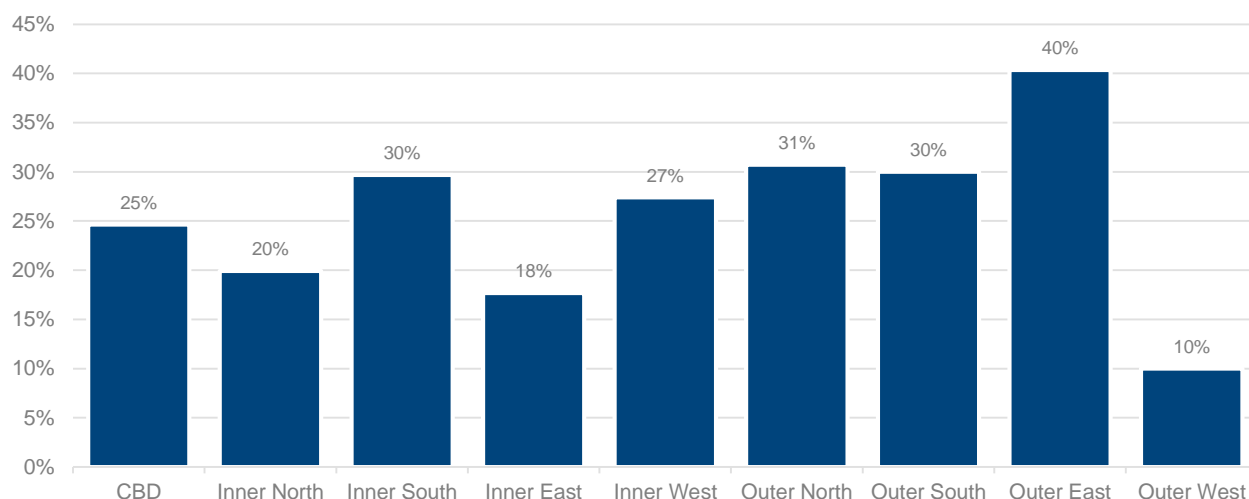
Number of apartments completed vs number of apartments unsettled in 2017 by locality



Despite fewer apartments being completed in the Inner South than the Inner North during 2017, the Inner South had a higher number of unsettled apartments as at 31 December 2017.

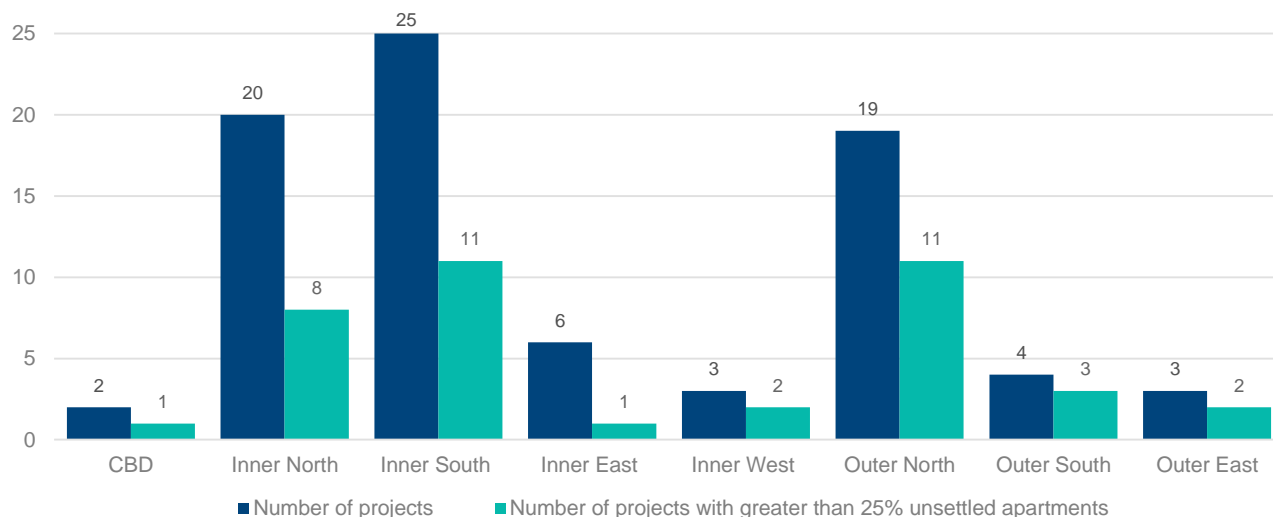
Further, while the number of apartments completed in the Outer North in 2017 was approximately a third of the number of apartments completed in the Inner North, the number of apartments unsettled in the Outer North was half of the number of apartments unsettled in the Inner North.

Unsettled apartments as a percentage of total apartments completed in each locality as at 31 December 2017



Settlement risk is certainly not confined to the Inner North, Inner South and Outer North. As the following graph shows, there were projects with greater than 25% of unsettled apartments in all localities.

Number of projects completed in 2017 vs number of projects completed in 2017 with greater than 25% of apartments unsettled as at 31 December 2017 by locality

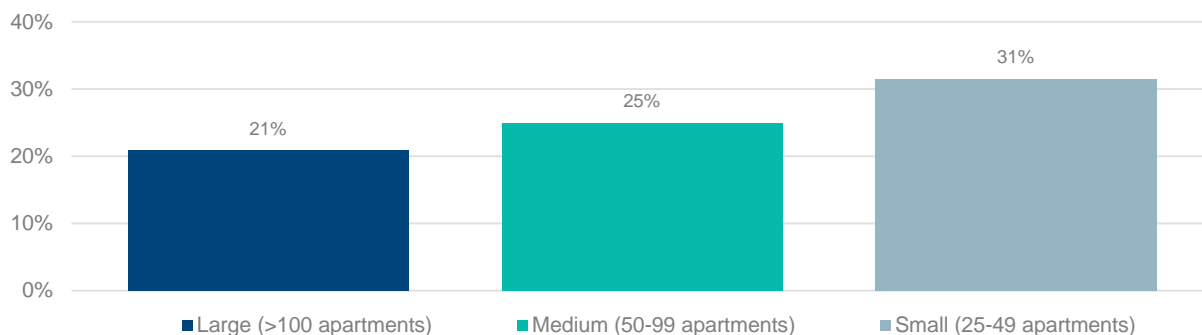


Although the Inner South had the highest number of apartments yet to settle as at 31 December 2017, the number of projects with greater than 25% of apartments unsettled was relatively low at 44% of all projects completed in the Inner South.

As demonstrated above, the outer localities had a higher proportion of projects with greater than 25% of apartments unsettled as at 31 December 2017.

Unsettled apartments as at 31 December 2017 as a percentage of total apartments for projects completed in 2017 by development size

The following graph demonstrates an inverse relationship between a project's size and settlement risk. That is, as a project's size increases the percentage of apartments within the project that are unsettled decreases. While not within the scope of this report, we see this relationship extending to projects of less than 25 apartments.



While high profile developments in inner city areas such as Newstead and South Brisbane may attract the majority of attention, we retain our concerns for smaller projects located in the middle to outer ring suburbs.

It is here that the headwinds facing the apartment market will be felt most strongly as buyers become more discerning due to increased supply.

Other trends

Other noticeable trends include:

- Foreign (particularly Chinese) purchasers who are unable to obtain finance from Australian lenders rescinding contracts, with new contracts being entered into by local residents, usually family members.
- Early discounting of some projects to clear residual stock.
- Pre-sales on yet-to-commence projects are not meeting expectations resulting in project deferrals
- The quantity of new stock resulting in significant losses upon resale on recently purchased off-the plan prices of up to 30%.

Managing settlement risk

To manage settlement risk, it is critical to comprehend:

- Current market conditions and how buyers may be positioned
- The supply and demand for similar competing products
- The advantages and disadvantages of given product compared to the competition including other new stock and older stock
- Legal disputes such as the enforceability of pre-sale contracts relating to:
 - Building specification differences to marketing plans
 - Any looming sunset dates
 - Body corporate disclosure statement variances
- Level of deposit
- Buyer origin, being either local, interstate or foreign
- Nature of purchasing entity

Expectations for the future

The pressure on owners of older stock will continue to intensify as the choice for buyers and renters, who hold the higher ground in rental property negotiations, increases.

Anecdotally, owners are preferring to hold on to properties for a longer time period, rather than crystallise losses.

The longer this downward trend in apartment values continues, the greater the likelihood that off the plan purchasers simply elect to walk away.

If this eventuates, it will not only be the equity and mezzanine funders who will incur losses, but senior lenders may also be at risk, depending on their exposure.

Those developers with an effective and streamlined approach to managing settlements are faring better than those developers who do not have an appropriate strategy in place to work with purchasers.

With all the headwinds facing the residential apartment sector in Brisbane, we anticipate sales prices for new apartments will decline following decreases in sales volumes for off-the-plan apartments, with settlement risk being a significant concern.

While both inner city and middle ring suburban areas have large numbers of projects completing throughout 2018, we retain confidence in high quality projects.

Specifically, we consider the defining factors of successful projects to include:

- Location
- Building quality and visual appeal
- Number of apartments
- Size
- Layout
- Extent of allocated and unallocated parking
- Views
- Amenity
- Price point
- Purchase price compared to valuation

The flight to quality will pick up speed as buyers and renters begin leveraging their negotiating positions. This phenomenon will be felt the most in the middle ring suburban areas such as Albion, Nundah, Cannon Hill and Chermside.

Financiers exposed to the larger residential projects in this sector need to be prepared to work closely with developers to mitigate the risk of loss.

Snapshot of the market

From our research, we have formed the opinion that sale prices have fallen, the volume of sales has decreased, greater measures are being offered to motivate agents and buyers to act, and settlement periods are lengthening.



Our Queensland real estate team

In Queensland we have a team of experienced real estate professionals with extensive experience in the residential apartment sector. We can provide a detailed private briefing on the market, and where appropriate, advise developers and financiers on updated options analysis of any exit, hold or develop out strategies, project completion, mitigating settlement risk and project marketing.

To find out more, or for further information as to how we can assist, please contact one of our real estate team today.



Will Colwell
Queensland Practice Head
Ferrier Hodgson

+61 7 3834 9205
will.colwell@fh.com.au



Brett McAuliffe
Executive Director
Azurium Real Estate

+61 7 3834 9233
brett.mcauliffe@azurium.com.au



Tim Michael
Partner
Ferrier Hodgson

+61 7 3834 9228
tim.michael@fh.com.au



Peter Gumbley
Director – Sales & Project Marketing
Azurium Real Estate

+61 7 3834 9222
peter.gumbley@azurium.com.au



Sallyanne Pitt
Director
Ferrier Hodgson

+61 7 3834 9214
sallyanne.pitt@fh.com.au



Cameron Mana
Director – Development
Azurium Real Estate

+61 7 3834 9222
cameron.mana@azurium.com.au



Campbell Munro
Property Senior Analyst
Ferrier Hodgson

+61 7 3834 9235
campbell.munro@fh.com.au



Andrew Willsford
Valuation Specialist
Azurium Real Estate

+61 7 3834 9222
andrew.willsford@azurium.com.au



Jackson Adcock
Property Analyst
Ferrier Hodgson

+61 7 3834 9247
jackson.adcock@fh.com.au



Andrew Keeble
Retail Leasing Specialist
Azurium Real Estate

+61 7 3834 9222
andrew.keeble@azurium.com.au

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Ferrier
Hodgson

azurium
real estate

Level 7, 145 Eagle Street
Brisbane, QLD 4000

T +61 7 3831 4833