A new era for Australian renters

First Sentier Investors

Background: The Residential for Rent Sector in Australia

There are marked changes occurring within global housing markets with a defined long-term trend from home ownership to rental accommodation, as housing affordability has become a major issue for younger generations and as the aspiration to own a home has waned with priorities shifting towards lifestyle and experiences. Another factor driving the greater propensity to rent is the quality of amenities. These trends have underpinned robust and growing demand for institutionally owned, purpose-built residential apartment buildings.

By global standards, the Australian Residential for Rent (RfR) market is in its mere infancy, with individual 'Mum and Dad' investors still owning the vast majority of rental properties. There are only a very limited number of institutionally owned rental projects publicly announced or under development in Australia, which lags considerably behind established markets like the United States, Germany, France, Finland and the Netherlands, and growing markets like Canada and the United Kingdom.

However, the landscape is now changing, which is positioning the domestic RfR sector for solid growth like other countries around the world have experienced. We believe the take-up of RfR buildings in Australia will be rapid in the future as institutionally owned, purpose-built rental buildings are developed and come on line to meet growing tenant demand for this type of product. The lifestyles of younger generations will be transformed, while the investment case for institutional investors is also compelling.

We recently visited the Mirvac Group's 'LIV Indigo' (LIV) project, which is Australia's first Build-To-Rent (BTR) development. The project represents a very exciting and significant milestone in the timeline of the Australian RfR sector.

LIV Indigo by Mirvac Group

LIV is a 315 unit project located adjacent to Mirvac's 'Pavilions' apartment project at Sydney Olympic Park. The development is being marketed as 'offering the security of ownership with the flexibility of renting'.

LIV Indigo. Source: Mirvac Group as at September 2020.

LIV officially opened for residents on September 1st, and to date, occupancy and underwriting metrics are on track, with 25% of the building already leased, while 16% of the apartments are now physically occupied.

The project was initially conceived as a Build-To-Sell project (BTS) but was converted to a BTR project as Mirvac saw the opportunity to launch this product in the Australian market. Mirvac currently has 1,700 BTR units under development and is targeting a 5,000 unit BTR portfolio.

The project comprises of 1, 2 and 3 bedroom units comprising 50%, 40% and 10% respectively of the total project. The unit sizes are 55-60m^2 (1 bedroom), 70-80m^2 (2 bedroom) and +90m^2 (3 bedroom units).

The tenants are currently drawn 50% from couples, with the balance split between single occupants (24%), families (15%), downsizers (6%) and share houses (4%).

Commencement base rental rates are $535 per week for 1 bedroom units, $630 per week for 2 bedroom units and $1,000 per week for 3 bedroom units. Additional charges apply for car parking and storage facilities.

Open Plan Living Area. Source: First Sentier Investors as at September 2020.

Mirvac believes that LIV has four key appealing elements: (a) the offer can be personalised for the prospective tenant, (b) the security of occupancy (tenants can extend leases at their option), (c) units are pet friendly and (d) no rental bond is required. Each unit comes supplied with white goods and furnishings such as blinds, a washer and dryer and fitted out wardrobes. The apartments have been designed with floor finishes that allows prospective tenants to fit out the apartment to their tastes.

Tenants can purchase the furnishing packages ranging from $10,000 for 1 bedroom units, $15,000 for 2 bedroom units and $20,000 for 3 bedroom units. The asset also offers tenants an amenity zone called 'The Deck', which includes a home theatre, group dining facilities, meeting rooms and casual dining facilities that can be booked by tenants for no additional charge. The building also has a gym and recreation area as well as a dedicated internal children's play area.

'The Deck'. Source: Mirvac Group as at September 2020.

Tenants can occupy the apartment on flexible terms starting at 12 months, but can opt for say 3 year leases if required with a perpetual occupation clause in the lease. After 12 months, the rent paid by tenants' will be reviewed based on market evidence although Mirvac will also evaluate any potential downtime impacts and recognise that the product is new for the Australian market. In any event market rent reviews will be capped at 4% per annum.

Mirvac expects the project will deliver an initial unlevered yield of 4.5% once stabilised, which would increase to 4.7% if the project was to be granted the land tax concessions recently announced by the New South Wales State Government for future BTR projects. Mirvac also expects operating margins to be ~79% once stabilised.

Disclosure: as of 30 September 2020 we are currently invested into Mirvac Group in our Australian and Global strategies.

To learn more about the sector globally, read our **'Evolution of Cities – Residential for Rent'** paper here.