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Mirvac's long-term rental future

Mirvac has prospered under the leadership of chief executive Susan Lloyd-Hurwitz. **Jessica Hromas**

by **Su-Lin Tan**

Hundreds of homebuyers squeezed into Mirvac's display suite in Sydney Olympic Park six weeks ago in the hope of snapping up apartments at its latest project, Pavilions.

People queuing to buy homes in Sydney is not a new phenomenon. And especially when Mirvac was offering first home buyers first dibs to buy 60 apartments at a time when the city is struggling with a housing affordability crisis.

But there's something else attracting buyers. "First dibs or not, the reason why I am here is because it's Mirvac," one Chinese-Australian buyer told *The Australian Financial Review*. "Even if the housing market wobbles, you can't go wrong with a Mirvac product."
Mirvac's may have a good reputation for quality in the residential space, but this does not mean the developer is resting on its laurels.

Major contributors to Mirvac EBIT

	FY17 lot target	Secured (%)
Apartments		
Moreton Bondi, NSW	190	100
Unison Waterfront, Qld (Stage 1 & 2)	252	100
Forge, Yarra's Edge, Vic (Tower 10)	143	100
Green Square, NSW (Ebsworth)	174	100
Harold Park, NSW (Precinct 4)	67	100
Masterplanned communities		
Tullamore, Vic	164	100
Brighton Lakes, NSW	130	100
Gainsborough Greens, Qld	365	100
Woodlea, Vic	670	100
Gledswood Hills, NSW	140	100

Mirvac share price, daily ($)

SOURCE: MIRVAC, BLOOMBERG

Chief executive Susan Lloyd-Hurwitz is a proponent of affordable housing and wants to contribute solutions to the problem. This is most acute in Sydney, where the median house price is now about $1.1 million, according to Domain Group's latest release.

Lloyd-Hurwitz says Mirvac is looking beyond the staples of apartments and houses and venturing into the realm of housing innovation such as 'build-to-rent' projects, where Mirvac owns entire projects and leases them out to tenants on long-term tenures.

Its boldness in taking on the never-tried build-to-rent product may feed Lloyd-Hurwitz's passions. But can she pull it off?
CLSA's head of Australia real estate Sholto Maconochie says the numbers do not stack up for any developer wanting to make a decent return. "We have looked at this but it is not that simple," Maconochie says.

"It requires a combination of state and Commonwealth government support and/or legislation changes as currently the yields do not stack up relative to other real estate asset classes."

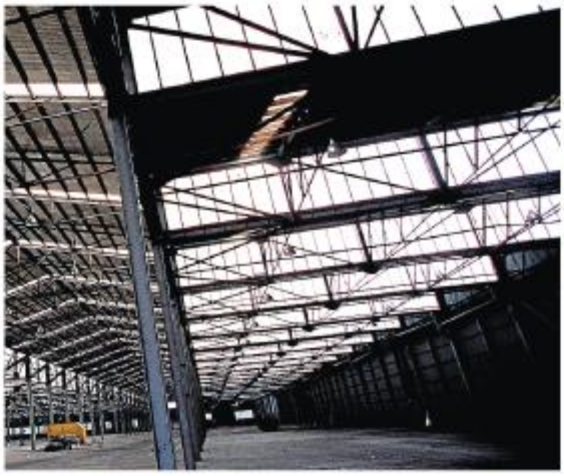
Mirvac's $5.5b portfolio

OFFICE

Occupancy (%)	97.6
Cap rate (%)	6.0
Weighted to Syd, Melb (%)	81.0
WALE (yrs)	6.7
Average age (yrs)	12.7
Prime or A-grade (%)	95.0

INDUSTRIAL

Occupancy (%)	99.5
Cap rate (%)	6.4
Weighted to Syd, Melb (%)	93.0
WALE (yrs)	7.1



SOURCE: MACQUARIE

So why is Mirvac, or any other residential developer or investor, considering the build-to-rent space?

For starters, yield in other property asset classes – like commercial – has shrunk so much that it is now close to being on par with the lower yield of potential build-to-rent projects, which is about 3.5 per cent to 4 per cent, Lloyd-Hurwitz says.

Additionally, build-to-rent, or "multifamily" as it is known in the US, provides steady long-term cash flows through residential leases.

Beyond financials, Lloyd-Hurwitz looks at housing in a way that is more than just about returns, a 'get-rich' commodity or a way to foolproof retirement.

"Why do we think we have a chance to make institutional [build-to-rent] work? Because renting in Australia is generally a very miserable customer experience ... the whole industry is set up to serve the owner, not the tenant," she tells *The Australian Financial Review*.
"Housing is not just about houses. It defines how we can experience our sense of place, our comfort, our last step, our next step," she recently explained at CEDA's NSW property market outlook event.

The analysts may have their doubts. But other players such as Salta Properties and Scape Student Living may have proved them wrong after laying claim, as recently as last week, to being Australia's pioneers in this new long-term rental movement.
And if Mirvac is up next, it will be the first listed group to take its shareholders on a new carpet ride.

Residential credentials
In the meantime, Mirvac has maintained performance in its usual residential portfolio. In its latest update in April, residential sales was up 18 per cent compared to a year ago. The group is on target to settle 3300 lots in 2017.

Settlements have progressed at projects like The Moreton in Sydney's Bondi and Ebsworth in Green Square, and defaults are tracking below 2 per cent, slightly higher than its historical 1 per cent average.

Their new launches at house-and-land sites in Olivine and Woodlea in Melbourne were 100 per cent pre-sold. Pavilions and Marrick & Co also in Sydney achieved at least 67 per cent in pre-sales.

But while Mirvac is known for apartments, it also has house-and-land projects, which have quietly flown under the radar, JP Morgan analyst Richard Jones says.

"They have done well with the Doncaster Eastern Golf Course, "Tullamore" ... they had strong sales there, which were way above expectations," he says.

Tullamore is a 42-hectare infill development with vacant land and integrated housing and Mirvac has more of those in growth areas of Moorebank, Gledswood Hills and Schofields, in southwest Sydney and in Canberra's latest township of Googong.

Housing risks

But the good times won't last forever and there are headwinds surging in the residential sector. The Australian Prudential Regulation Authority's recent clampdown on investor loans and major banks' rejection of all foreign lending for the last 18 months have ignited concerns about settlement risks, particularly around apartments.

Citi analysts have downgraded the outlook for dwelling investments, as the "economy now faces a second rebalancing challenge as the housing boom begins a protracted unwinding".

But agents and developers swear by a multi-speed housing market, where even in potentially softer markets like Melbourne and Brisbane, there are locations there will always sell and settle. The same goes for Sydney. Right now, Mirvac appears to be well-represented in those areas.

Off the back of defaulting foreign buyers, in its first quarter update in October last year, Mirvac sent a worry ripple around the industry when it announced there has been a "rise in the default rate for the settlement of off-the-plan residential sales, above its historic average of 1 per cent". It stressed however that all defaulted lots have been resold.
The consolation in the issue lies in the fact that Mirvac isn't the only developer facing these risks.

Credit Suisse analyst Hasan Tevfik says despite the lack of funding, Chinese demand – the biggest group of housing foreign buyers in Australia – will continue to grow.

Despite the lack of bank lending, these buyers have found alternative sources of finance to fund the purchases in Australia because demand is fairly inelastic, Tevfik says.

"The main reason why capital will continue to flow from China to Australia is because the middle-kingdom is huge. Not only is China an enormous economy, wealth creation is occurring at an impressive rate."

Office and Retail
Despite its reputation as an apartment developer, Mirvac's residential division is a lower proportion of its entire $8.7 billion portfolio, led by its two other strong suits, office and retail, Jones says. Residential property forms only a third of its property portfolio.

Using a development strategy with offices and an acquisition strategy with its retail assets, Mirvac reshaped its portfolio in 2015 and 2016.
It sold $885 million of "non-aligned" assets, selling all its suburban office buildings, all its offices in Canberra and its shopping centres in regional Queensland to focus on its higher-growth urban strategy.

At the same time, it invested $370 million in purchases "with the potential to unlock future value" and, over the past two years, developed $800 million of new office towers and industrial facilities.

All the heavy lifting that Lloyd-Hurwitz has done has paid off, Maconochie says.

Some of the strong office assets underpinned by long-weighted average lease expiry include the recently completed 200 George Street in which Mirvac houses its headquarters, the new premium-grade Sydney landmark 8 Chifley and the heavily refurbished 10-20 Bond Street, also in Sydney.

The group also has a long-term project business park project in the $1 billion Australian Technology Park redevelopment in inner-city Sydney, future home of the Commonwealth Bank of Australia.
Its Broadway shopping centre has the highest turnover by square metre in Australia.

But there are also headwinds for the retail sector with a likely entry by Amazon this year, CLSA says.

Capital diversification
The group has also started to diversity its capital usage, forming a 50:50 joint venture with Chinese insurance giant Ping An's property arm to develop residential projects in Australia.
Finding a capital partner for its 664 Collins Street and 477 Collins Street office towers could also be an advantage, Jones says.

Maconochie also credits Mirvac's strength to Lloyd-Hurwitz's leadership.

"She has done a good job, culturally [Mirvac] is better," he says.

With its house in order – strong diversified earnings, a careful eye on risks, and heavyweight capital partners – Mirvac may right now have just the right arsenal to make a push into more creative ventures like build-to-rent products and deliver much-needed innovative affordable housing solutions to the housing markets.