08/08/2014

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RE: LORDS ROAD INDUSTRIAL PRECINCT

BACKGROUND

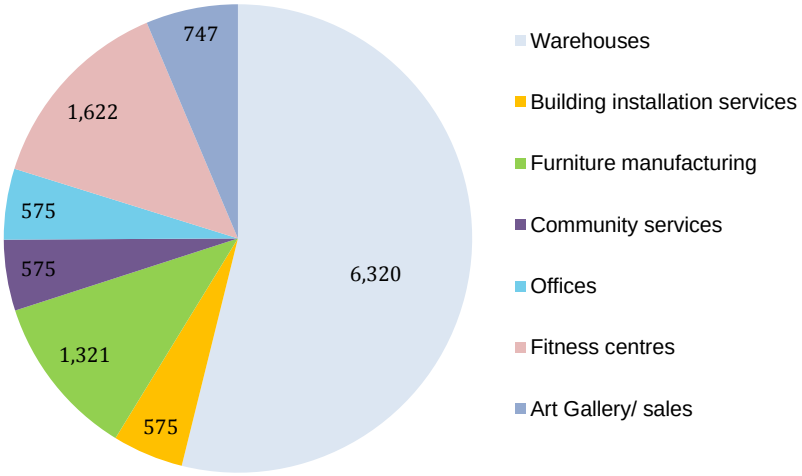
SGS has been invited to prepare a submission to report on the suitability of rezoning industrial land at 67-73 Lords Road, Leichhardt (the subject site). This exercise will run in tandem with the Leichhardt Industrial Lands Study (ILS), with outputs from the ILS directly addressing the Lords Rd economic analysis. The scope of the study is summarised as follows:

Task	Overlap with ILS	Estimated time for completion
1. Identify the role and function of the subject industrial precinct and its relative strategic positioning	Yes	Late July
2. Provide advice on the existing tenant mix, likely or potential rental return/ yield, locational and built form of the subject site in terms of its current economic viability	No	Late July
3. Review the subject industrial precinct against the Summary of the Strategic Assessment Checklist provided in Action E3.2 of the Metropolitan Plan; Criteria Table 1: Industrial Lands Strategic Assessment Checklist for rezoning of existing industrial land to other uses under objective 13 of the Draft Metropolitan Strategy to 2031; and Council's own criteria identified in the Leichhardt Employment and Economic Development Plan 2013-2023. Notwithstanding, the Consultant may also identify other issues that should be considered in the evaluation of the strategic importance of land for industrial uses in addition to the aforementioned criteria and checklists	Yes	Late August
4. Undertake risk analysis which considers the likely impact of not retaining the subject site as industrial zoned land	Yes	Late August
5. Consider the future industry dynamics for key sectors both currently in the subject precinct and those which could seek to benefit from locating in the area	In part, yes	Early August
6. Consider the potential impacts of WestConnex on the subject industrial land	Yes	Early August
7. If the site is found to be surplus to industrial requirements, its suitability against a range of alternative uses discussed in the EEDP is to be considered. For example, its potential for rezoning and use for creative industries, commercial office space or affordable housing	Yes	Early September
8. Have regard to relevant findings of the current Leichhardt Industrial Lands Study as they become available during July and August 2014	Yes	Early September

PRECINCT ROLE AND FUNCTION

- **Land use**. The Lords Rd precinct has a predominantly 'local service' industrial function. In terms of built form and land use the precinct can be classified as a small industrial park/ business park. The precinct is currently fully occupied with no vacant space. The majority of the GFA at the precinct is occupied by warehousing uses (54% of total GFA). Other (local service) industrial functions include furniture manufacture (11% of total GFA) and building installation service (5%). The remaining 30% of GFA at the precinct is occupied by non-industrial uses including a fitness centre, art auction room and offices.

  CURRENT GROSS FLOOR AREA PROFILE OF LORDS RD INDUSTRIAL PRECINCT



Source SGS: 2014

- **Development activity**. There has been very little development, or sales activity at the precinct in recent years. Leasing activity has been moderate. The latest leasing record at the precinct is for unit 2/ 71 Lords Rd which leased for $50,000 PA – around $138/ sqm[1]. This compares favourably with current on the market data for industrial properties at 151 Allen St (which is leased for $70/ sqm) and 2/ 57-61 John St (which is leased for $76/ sqm).
- **Existing tenant mix**. The existing tenant list at the Lords Rd precinct is as follows:
  - Lee Mathews Workroom
  - Country Road Clothing
  - Granville Smith Restorations
  - Art Est Pty Ltd
  - United Displays
  - James Lee-Warner Furniture
  - The Sports Pit

[1] Based on lot areas reported in RPData 2014

- Plex Pty Ltd
- CSR
- David Buckley
- John Cosco
- Isherwoods
- Showtime Production Services
- Gavin Clarke Building Services
- Compudrive / Storesafe
- Slabseal Australia
- Head Academy Kung Fu
- The Sports Pit
- Sydney Next Church
- Arthouse Auctions
- Ecocern Pty Ltd

INDUSTRY DYNAMICS

Industry trends and drivers

- **Slowing manufacturing jobs growth**. At a Greater Sydney Metropolitan level the proportion of jobs in the industrial sector is predicted to decline although the actual number of jobs is still expected to increase through to 2036. Job growth is not expected in traditional industrial sectors but rather the highly specialised and technological manufacturing (advanced manufacturing). As a consequence an increasingly skilled workforce will be required.

- **Manufacturing's role in the knowledge economy.** Manufacturing's decline in Australian cities over the last half century has been well documented, with the process of globalisation and the decoupling of the value chain resulting in many manufacturing processes relocating overseas to lower cost countries. In more recent times, the impact of this macroeconomic restructuring has been compounded by a high Australian dollar and globally soft economic conditions that have reduced aggregate demand (Adonis, 2013). However, the experience of other manufacturing nations has been that manufacturing can still play a relevant role in the economy if, much like other sectors of the economy, production moves up the value chain.

  In the global value chain, developing nations (for example China) initially utilise their relatively cheap labour to manufacture less sophisticated, more labour intensive products. Over time, as their manufacturing base expands there is a move towards robotics, intellectual property and other attributes to produce goods and services with a greater degree of sophistication (as witnessed in Germany, Japan and Korea). This specialisation in industries of comparative advantage is impacting all economies and industries, acting as a catalyst for them to evolve from their historical economic configuration into dynamic, adaptive and internationally competitive industries.

- **Supply-chain fragmentation.** Greater efficiencies of technology and mechanisation are changing the way that traditional industrial businesses operate. The global economy today consists of sophisticated linkages between businesses, which are designed to enable the efficient sharing of information and the delivery of goods through a global supply chain. Supply-chains have become more fragmented and business components are often scattered across wide areas – sometimes internationally. An example of this change can be seen in the motor

industry. Once concentrated in cities, the motor industry has evolved into a process where design, manufacture, and assembly occur in many different locations worldwide. All this has heightened time-based competition and flexibility, with implications for the functional characteristics and spatial disposition of industrial activity.

- **Growing service economy.** The decoupling of the value chain and movement of production activities across national borders has had a profound impact on the structure of Australia's economy. Australia's economic backbone has transitioned from one built on agriculture and manufacturing to one predominately supplying services. We used to produce much of what we consumed but this is no longer the case. In this transition, competitive advantage has increasingly been gained through specialising in activities higher up the value chain where high levels of innovation and creativity are central.

  This movement up the value chain has been most prominent (and indeed profitable) in the advanced business services sector, particularly in the Finance and insurance, and Professional, scientific and technical service industries. These advanced business services are therefore often dubbed 'knowledge industries' and the backbone of the 'knowledge economy'.

  In these high value-add sectors, competitive advantage is gained and maintained by offering environments that promote innovation and creativity, and are able to attract a sufficient supply of the highly skilled labour required to enable high productivity firms to flourish. These environments are known as agglomeration economies.

- **Agglomeration economies. '**Agglomeration economies' is a term used in spatial economics to describe the benefits that flow to firms from locating in areas that have a high density of economic activity. The benefits that arise from locating in a denser economy include:

  - **economics of scale and scope**: with a larger customer base firms are able to develop efficiencies through operating at a large scale. This also enables firms to focus the scope of their expertise in a particular field, gaining improved efficiencies through specialisation.
  - **deep and diverse pool of clients/employers/employees**: A competitive marketplace presents people and firms with a multitude of potential options. This frees them from reliance on a single (or limited) client or employer base, allowing firms to better align their specific skills, again improving productivity.
  - **technological spillovers**: With multiple firms located together there will be a higher level of technological and knowledge spillovers and transfers, which will help bolster innovation. This transfer occurs both directly, through stronger supply chain linkages and connections between local firms, and indirectly, when skilled labour moves between firms and transfers knowledge, as well as through incidental exchanges.

  These benefits, while experienced by all firms and residents, have particularly benefitted those in the advanced business services sectors, with macroeconomic conditions and Australia's position in the world economy allowing these sectors to be competitive in producing services higher up the global value chain.

- **Changing economic geography**. In response to the changing format of industrial activities and the growth of inner metropolitan land values, there has been a spatial redistribution of more traditional forms of industrial activity. Activities with rent sensitivities have relocated to less expensive land often on the urban periphery. Others have simply stopped operations in Sydney altogether.

  The ongoing trend is for new industries to favour a location with features that allow the development of large modern industrial facilities while maintaining low cost operations. The most sought after characteristics include:

- Undeveloped large vacant and unencumbered land for purpose built operations
- Low priced and serviced industrial zoned land
- Availability of an appropriately skilled local workforce
- Agglomeration or synergies with other industries in the area
- Good access to major arterial road and transport infrastructure

Land with these characteristics is largely found on the fringe of metropolitan Sydney, such as Eastern Creek and Erskine Park, where a large amount of recent industrial development has been occurring. This land is more affordable, developing in these areas is cheaper, and the large tracts of vacant land available provide a range of flexible subdivision options.

- **Growing need for space to house 'office' functions**. Research into business parks shows that in line with the increasingly advanced nature of manufacturing, the buildings housing these activities have moved from a split of 50/50 (office/warehousing) to 80/20. Another contributing factor to this shift was that office occupiers tend to be more reactive, only being attracted to a new location once it had been established and gained momentum. Ample car parking and good access to major road infrastructure were stated as key requirements.
- **Urban manufacturers.** With these underlying drivers, contemporary urban manufacturers derive competitive advantage from their focus on innovation and creativity, facilitated by their specific location within cities. Their location within dense urban networks allows them to capitalise on sophisticated design and local market insights, attract and retain valuable labour, and adjust quickly to shifts in local demand (Friedman and Byron, 2012). The urban manufacturing sector therefore appears to operate and prosper on many of the same attributes central to the success of advanced business services, namely the benefits gained through agglomeration.

  Taking advantage of these competitive edges, urban manufacturers tend to be: small (generally employing fewer than 20 people); provide a highly specialised or niche product; have fast turnarounds; and be horizontally integrated in networks of numerous clients, suppliers, distributors, and subcontractors (Pratt Centre, 2013). This embeds manufacturers in place, as does the nature of their work, which due to its often customised nature, requires frequent face-to-face contact.

  These modern manufacturers more closely resemble their productive counterparts prior to the industrial revolution, offering high-value add design orientated products. They produce a wide range of products, operating in fields of all types, from fashion textiles and jewellery to food and beverage, print and media, auto and bike customisation, musical equipment, and niche electronics, to name but a few.

  With these characteristics, small urban manufacturers typically operate in networks with other manufacturers. The flexibility of these networks and temporary partnerships/collaborations means small firms are not required to carry the large fixed overhead costs for all the equipment, space or labour required to produce an entire product. This networking is reflected in the preference of these enterprises to lease space in multi-tenant workspaces, with large traditional industrial premises often partitioned to create multiple smaller production spaces. This presents the possibility of developing high value-add manufacturing precincts at greater densities. Such an approach has been realised in Singapore, where lighter and cleaner manufacturing activities have been funnelled into medium-rise industrial complexes (Chan, 2011).
- **Traditional users of urban industrial zones.** In addition to these contemporary manufacturers, industrial zones house a raft of essential population servicing industries, including panel beaters, depots requiring an inner city

location to service construction sites, distribution centres, utilities provision, and facilities for concrete batching and waste management. In the more connected global economy, there are strategic industries (particularly logistics) deriving advantages from locating close to the port and airport. Furthermore, the placement of particular industries, firms and facilities (such as Council depots) on the fringe of the CBD is vital to providing essential support services to large population centres.

- **Threats and challenges to urban manufacturers.** Against the macroeconomic trends driving a resurgence in urban manufacturing relative to residential and commercial land users, manufacturers occupy a lower rung on the value add ladder and do not command the same rent. As such they are at significant risk of displacement from the locations that nurture them, most obviously through rezoning, but also through land speculation associated with possible rezoning and the erosion of industrial zones for non-industrial uses.

  These activities bid up rents and erode the productivity of the remaining industrial firms, not because firms become any less efficient, but because of the cost of their inputs (most notably the land upon which they produce) increases at a faster rate than their improvements in internal productivity. Furthermore, without a degree of certainty regarding the long-term zoning of industrial land the owners of such land may have a perverse incentive not to invest in their property in the hope that rezoning will occur in the imminent future.

Implication of macroeconomic trends and drivers on Leichhardt's industrial precincts

Leichhardt, situated close to the core of metropolitan Sydney, offers a dense urban environment, densely populated with a relatively affluent and highly skilled resident workforce, well served by major transport routes and within relatively close proximity to the economic hubs of the Sydney CBD, Sydney Airport, and Port Botany. In very basic terms, Leichhardt's character and position translate to high land values which make it difficult for some industrial activities to find suitable sites on which to operate.

Activity with declining demand for Leichhardt's industrial land:

- **Traditional manufacturing and open storage**. High land values threaten the existence of lower value traditional industrial activity (especially those requiring larger floor areas) which is increasingly looking further west for lower cost land.

Activity with persistent or growing demand for Leichhardt's industrial land

- **Population serving industry**. Leichhardt will need to maintain a stock of industrial land that is focussed on providing for the needs of the local resident population. These industrial areas are typically characterised as 'local service industrial' and include uses such as automotive repairs, trade supplies, household storage, etc. There may also be some demand from industries deriving advantage from locating close to the CBD, port, and airport. Although West Connex would improve accessibility of Leichhardt's industrial lands, we would suggest that port and airport related opportunities are still limited given the relative distance of Leichhardt's industrial lands compared with areas in Marrickville, Botany and the City of Sydney.
- **Urban manufacturers**. These are manufacturing firms for whom innovation and creativity are at the core of their business. These firms benefit greatly from the agglomeration benefits presented by Leichhardt's location and urban environment. Additionally, being in close proximity to residential areas is increasingly appealing to manufacturers when choosing where to locate, with the attraction and retention of quality staff of growing importance (Colliers, 2014).

- **Creative industries**. Creative industries in particular may look to start up in Leichhardt in some of the transitioning industrial areas or may be migrating there after being priced out of the longer established creative precincts on the city-fringe such as Surry Hills and Ultimo-Pyrmont.

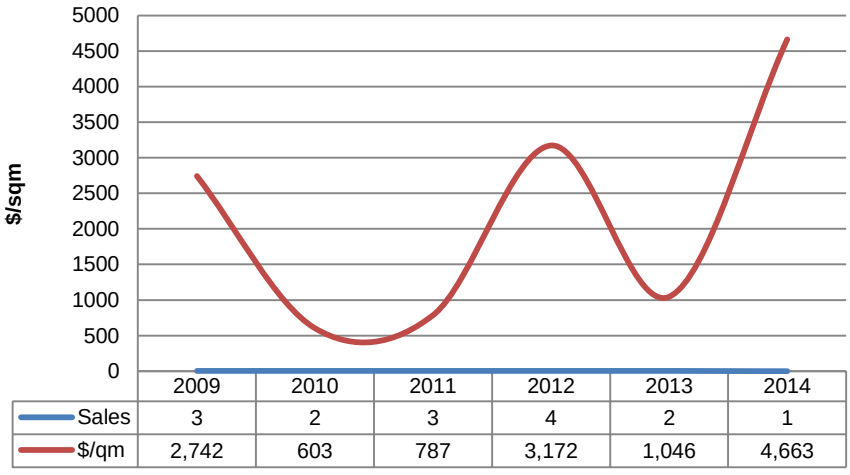
These activity types can be mostly accommodated within existing industrial precincts under current planning controls. However, perhaps the greatest pressure on Leichhardt's industrial land comes from non-industrial sectors – particularly residential development.

A key challenge for Leichhardt Council is to effectively and efficiently allow its employment locations to respond to industry and market trends and meet the ever changing requirements of occupiers. To achieve this, a significant degree of flexibility is important, both in terms of the design of the buildings and also the planning policy framework. This may include increasing the flexibility of industrial zones by increasing the range of mandatory permissible uses, allowing additional local uses in specialised locations.

Market dynamics

The number of industrial sales in Leichhardt has been very slow over the past 5 years (with just 15 sales recorded by RPData in that period). These numbers are predominantly a reflection of the small size of the LGA's industrial land market but also reflect a relatively slow industrial land market over the past 5 years.

INDUSTRIAL SALES 2009-2014



	2009	2010	2011	2012	2013	2014
Sales	3	2	3	4	2	1
$/qm	2,742	603	787	3,172	1,046	4,663

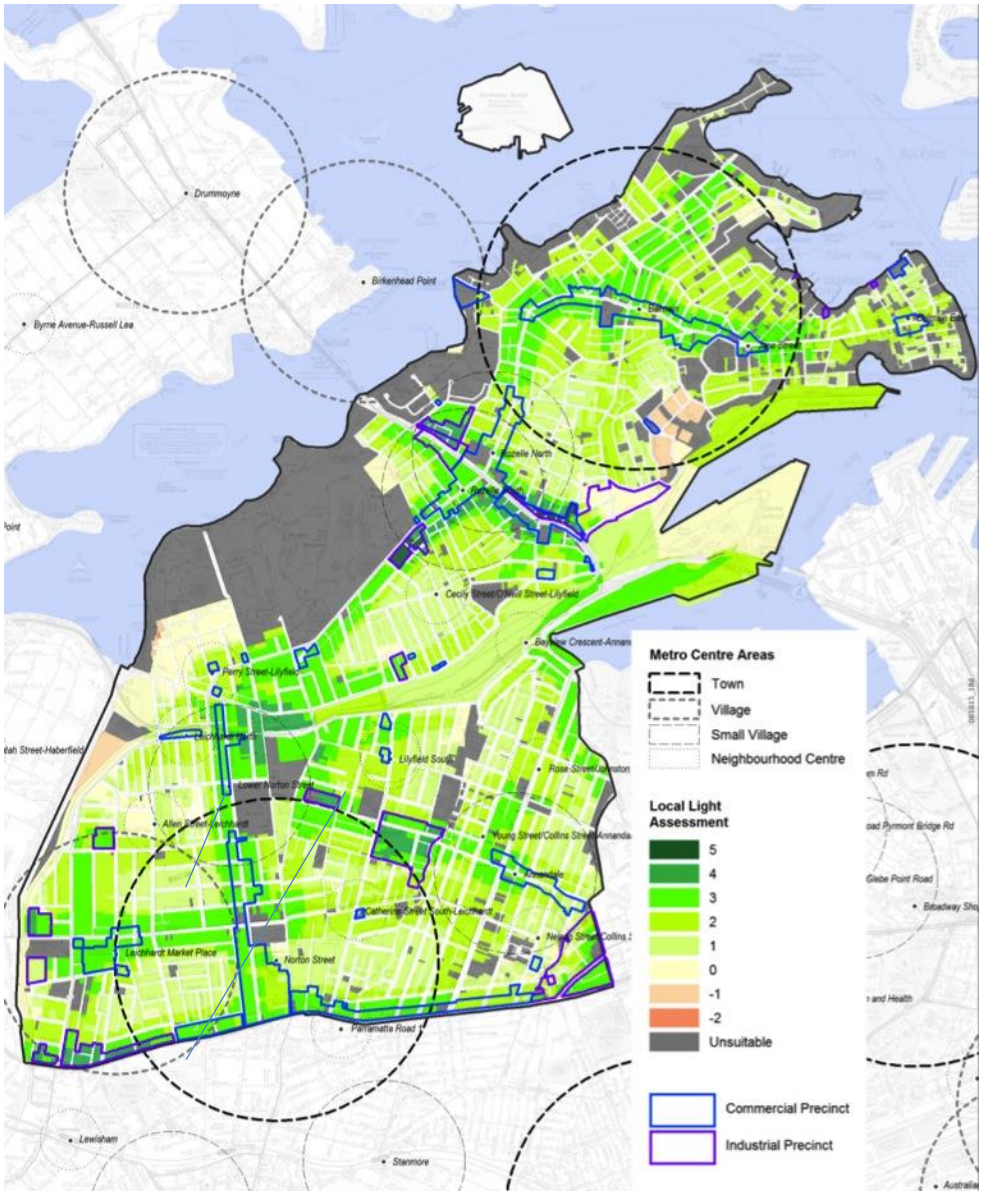
Source: RPData 2014

Suitability analysis

The map below shows the broad suitability of the Lords St precinct for light and local service industrial use. This assessment is based on a sieve mapping exercise which examines the suitability of each lot in the Leichhardt LGA for

local light industrial use2. This analysis shows that the Lords Rd precinct, although suitable for local light industrial, has a lower score than some other similarly zoned precincts in the LGA.

SUITABILITY FOR LIGHT INDUSTRIAL LAND USE



Source SGS 2007 and 2014

[2] The assessment for Local Light Industrial use takes into account: lot size, population density, proximity to existing centre, distance from major roads, distance from rail stations and bus routes, development constraints (acid sulphate soils, other contamination, flood, heritage).

Competitive positioning[3]

Precinct	Role/ function
Tebbutt Street/ Parramatta Road Summary: Retail and trade supplies (Parramatta Road); Storage, local service industry (Tebbutt Street, George Street)	The precinct is at the western end of the Parramatta Road corridor and contains street frontage properties to Parramatta Road and properties with frontage to Tebbutt Street. The precinct is surrounded by residential areas to the north and some residential development has occurred within the industrial zoned area. Unlike the remainder of the corridor, this precinct is not affected by a heritage conservation overlay nor does it contain any heritage items. There is however, a heritage conservation area to the north of some of the Parramatta Road frontage properties. Tebbutt Street provides access to the Parramatta Road overpass located in this area and as such there are significant traffic movements generated. Back from Parramata Road, land uses are mostly 'local service industrial' in nature such as equipment hire, storage, automotive parts ,etc. Fronting Parramatta Rd, activities are more retail/ trade supplies focussed with uses such as electrical equipment supplies, DJ equipment supplies as well as automotive services.
Victoria Road south/ Robert Street Summary: Enterprise/ bulky goods corridor (Victoria Road) Local service industrial (Robert Street)	This precinct refers to the corridor between Roberts Road and Prosper Street and some properties with frontage to The Crescent. The Victoria Rd part of the precinct contains a mix of uses typical to a high traffic volume corridor including bulky goods retail, light industrial, and some mainstreet retail land uses. The setbacks along the corridor vary with some establishments having car parking in the front setback while others are built to the street. A heritage conservation area overlay affects some parts of the corridor with heritage items located at the corner of Gordon Street and Victoria Road. Industrial uses on Robert St are typical local service/ light industrial uses such as panel beaters, car repairs, automotive parts, etc Land uses surrounding the corridor include predominantly detached residential dwellings to the north (most located within a heritage conservation area) and south, the White Bay Industrial precinct and REP 26 lands to the east and Rozelle centre to the west
Moore Street Summary: Light manufacturing, printing (John Street)	Moore Street precinct is bound by White's Creek to the east, War Memorial Park on the corner of Catherine and Moore Street, and residential development predominately made up of workers cottages. The majority of Moore Street precinct currently contains a mixture of local light industrial, and light manufacturing. Smaller land uses include dispersed land uses and freight and logistics activities. Office uses and some detached residential are located on Moore Street. There are also residential properties located in the vicinity of Hill Street. The precinct has a diverse mix of office-based, industrial and bulky goods retail activities. Activities with high shares include Building and Construction Services, Motor Vehicle Retail and Warehousing.
Camperdown Summary: Bulky goods (Parramatta Road and Pyrmont Bridge Road); Storage, equipment hire (Booth Street); Small industrial complex (Chester Street)	The precinct is located on Parramatta Road, and is dissected by Pyrmont Bridge Road. The precinct is accessible by road or public transport and has high visibility along Parramatta Road. Parramatta Road is a congested road which experiences 60,000 AADT vehicle movements per day. The area is bounded by a canal to the North West, and Parramatta Road to the South and Booth and Mallet Streets to the east. This area is located in close proximity to Sydney University and is adjacent to new high-density housing developments south of Parramatta Road in Marrickville LGA. Fronting Bridge Rd and Parramatta Rd, land uses are predominantly bulky goods retail (kitchen showroom, furniture, etc) as well as automotive supplies.

[3] Based on incomplete land audit data as part of the 2014 Industrial Lands study

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Lilyfield Summary: Local light, some creative - plumbing supplies, textiles, car services (Lilyfield Road) ; Trade supplies, some creative industries (Balmain Road)	The Lilyfield industrial precincts are made up of two precincts – one on Balmain Road and the other on Lilyfield Road. Both sites are surrounded by residential development comprising of median density walk up flats and workers cottages. Both precincts are characterised as local service industrial – consisting of plumbing and other trade supplies, automotive services, textiles, with some creative industries (furniture manufacture, jewellery, glass, textiles, some small scale professional services)
Balmain East Summary: Port-related	This precinct contains existing port-related activity. Cooper St – 'Svitzer' marine salvage and towing.
Lords Rd Summary: Local services/ local light	This precinct is a small light industrial complex at the western end of Lords Rd. Current uses are predominantly local service industrial (warehousing, small scale manufacturing) with some 'dispersed' activities (such as a martial arts school, church, arts auction rooms).
Marion St Summary: Bulky goods, dispersed (Marion); Local light industry and some creative (Walter Rd)	This small precinct is at the western end of Marion St, with the Hawthorne Canal on the western boundary and Walter Rd on the northern boundary. The precinct is dominated by an aged care facility and motor showroom fronting Marion Street. There are some small scale creative businesses and light industrial businesses on the Walter St side.
Allen St Summary: Local service industrial	This small precinct is on the western end of Allen Street – bound by Allen St to the south, Flood Street to the east and Lyall Street to the north. The precinct is dominated by a warehousing/ distribution function.
White Bay Summary: Local light/ local service industry (Mullens Street)	The area is located in close proximity to Sydney's CBD, accessible via the Anzac Bridge. The area as a whole can be accessed via Victoria Road, which is often congested particularly during peak hours. Bus Services operating along Victoria Road connect this area with the CBD and Ryde. In addition, a cycleway runs along the Anzac Bridge. Port facilities at Glebe Island and White Bay are the primary adjacent land uses. Current and future operations at this location have the potential to impact upon amenity in the area, and previous proposals for widening the range of uses in this area have not been supported by State Government. Residential areas are located to the north and western of this employment land precinct. Businesses in this location are diverse and include a gym and film studio. There are numerous auto-repairers such as along Mullens Street, as well as show room uses along Victoria Road. This precinct will be affected by the White Bay revitalisation project which covers around 80 hectares of Government owned land including sites such as the heritage-listed White Bay Power Station, Glebe Island, White Bay, Rozelle Bay, Rozelle Rail Yards and Blackwattle Bay, including the Sydney Fish Market.

CURRENT VIABILITY

The Lords Rd precinct is currently fully tenanted and has no vacant space. Rents at the precinct appear to be relatively high when compared with other industrial precincts such as Moore Street and Allen Street. Although assessment of market positioning and the subregional role is incomplete at this stage of the industrial lands study, at face value, the precinct seems to be functioning well as a local service/ light industrial precinct.

As stated in the industry dynamics section, there is considerable pressure on Leichardt's industrial precincts for other uses. The suitability analysis has shown that while Lords Rd is suitable for light industrial use, it is not one of the highest ranked precincts. With close proximity to Leichhardt marketplace, surrounding residential land use and the provision of the light rail service, the site would also appear to be a good prospect for residential or mixed use development.

We have tested the feasibility of three non-industrial redevelopment options at the subject site and compared the results of each redevelopment option with the current industrial operation as a base case. That is, the feasibility results test for the viability of each redevelopment option against a 'do nothing' or a 'base case' scenario. The current land value of the site is taken to be value of the site in its current use. As a fully tenanted light industrial/ local service precinct, the site is clearly viable in its current form. Based on recent sales data accessed from RPData, the current value of the site has been estimated at $15.9 million. The net profit under each redevelopment option has been compared with the current land value of site in its present form.

Results of this feasibility testing exercise are termed as the 'baseline model' results. Sensitivity testing was undertaken to test the robustness of baseline model feasibility results to changes in key underlying assumptions/ drivers.

- **Development parameters**. We have tested three development options against the base case. These are summarised as follows:

DEVELOPMENT OPTIONS

Option	1: Proponent's option at FSR of 2.4:1	2: Straight residential at 1.5:1 FSR	3: Mixed use at FSR of 1.5:1
Residential			
GFA	24,800	15,500	12,324
# of units	315, of which 16 affordable	211	168
Composition (1 bed, 2 bed, 3 bed)	75 (1 bed)	50 (1 bed)	40 (1 bed)
Number of storeys	8	3	3
Commercial			
GFA	-	-	3,518
Number of storeys	-	-	2
Other			
GFA	Childcare (750 sqm)	-	-
Number of storeys	-	-	-
Parking			
Number of spaces	253	167	168
Underground/at grade	230 Underground 23 at grade	Underground	133 Underground 35 at grade

Source SGS : 2014

Cells highlighted in green in the table above are derived using assumptions based on advice provided by Council, with the rest of the values provided directly by Council. These assumptions are as follows:

  - The total residential floorspace under Option 1 of 24,800 sqm was derived after applying the ratio of total floorspace and FSR ratio achieved under the straight residential option (i.e. 15,500 sqm with an

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FSR ratio of 1.5:1) to the FSR ratio envisaged for this option, i.e. 2.4. Hence, 24,800 sqm = 2.4 / (1.5 / 15,500)

- SGS assumed that under Option 1, the proposed café and childcare centre would occupy an area of 150 sqm and 750 sqm respectively. The café floorspace was assumed based on average floorspace occupied by cafes in similar locations. The assumed floorspace for a childcare facility was based on average floorspace size of childcare facilities hosting between 65 and 70 children, as assessed from previous SGS audits
- The total residential floorspace under Option 3 of 12,324 sqm was derived by assuming that business floorspace remains at current levels and the residual would be used for residential purposes after applying an FSR of 1.5:1 (based on Council advice). Presently, the total GFA occupied on site is 11,734 sqm, of which commercial uses occupy 3,518 sqm (based on SGS's land use audit), giving a residual of 8,216 sqm, which at an FSR of 1.5:1 equates to 12,324 sqm
- The number of units under Option 3 was derived after applying the ratio of total floorspace and number of units achieved under the straight residential option (i.e. 15,500 sqm with 211 units) to the FSR ratio envisaged for this option, i.e. 1.5. Hence, 168 units = 12,324 sqm / (15,500 sqm / 211 units)
- The typical minimum unit size was used in the analysis, i.e., 50 sqm for 1 bedroom, 70 sqm for 2 bedrooms and 90 sqm for a 3 bedroom apartment. SGS assumed that under each option, 24% of all units would be comprised of a 1 bedroom apartment, 47% comprised of a 2 bedroom and 29% comprised of a 3 bedroom apartment
- The number of storeys under Option 3 was assumed to be the same as that envisaged for the straight residential option as both options apply an FSR ratio of 1.5:1
- The total parking requirements of 168 spaces under Option 3 was derived after applying the parking ratio of 167 spaces for 211 residential units specified by Council for the straight residential option to the contextual option, and after accounting for minimum parking requirements stipulated by Council (as accessed using Council's Development Control Plan 2013, Part C (Section 1, c1.11) for other commercial uses specified under this Option. Hence, 168 parking spaces = 168 units * parking ratio (i.e. 167 spaces for 211 units as specified in Option 2) + minimum of 1 space for each 100 sqm of commercial *3,518 sqm of commercial space specified under this option,
- The composition of parking spaces into underground and at grade was assessed by SGS using its own professional judgment.

Other assumptions underpinning the feasibility model results are appended to this letter.

- **RLV performance measures**. Using the aforementioned inputs and assumptions, the feasibility ratio and the net profit (in addition to the 20 percent profit margin included in the development costs) were calculated for each redevelopment option using the RLV Model. The feasibility results, together with some calculations, are shown in the table below. The terms used in the table below can be explained briefly as follows:

  - Redevelopment costs include costs of demolition, construction costs and contingencies, site preparation and remediation costs, professional fees, developer's profit margin, infrastructure levies or contributions and other council fees

  - Land acquisition includes the cost of acquiring the land by the developer for redevelopment as well as any finance and stamp duty payable. This is over and above the redevelopment costs paid by the developer. Any change in the current land value affects land acquisition costs. As the current land value

goes up, so do land acquisition costs and vice versa. The current land value, and therefore, land acquisition cost is assumed constant for all redevelopment options in any given test (i.e. baseline and sensitivity tests)

- Net sales revenue including sales expenses include the sales revenue that the developer will likely accrue from sales of the product after accounting for expenses attributed to sales
- Residual land value is the difference between the redevelopment costs and net sales revenue. The development is considered feasible when the residual land value is greater than the cost to acquire the land. This is given as a ratio in the model where a feasibility ratio of greater than 1 translates to a feasible development
- Net profit is the difference between the residual land value and the cost to qcquire land. If this difference is positive, the development is indeed profitable. If the ratio of net profit to total land acquisition costs for the developer is higher than 1, then the redevelopment is considered feasible.

FEASIBILITY RESULTS OF REDEVELOPMENT OPTIONS – BASELINE MODEL

	Base Case Option, i.e. current land value	**Relative to base case, i.e. leaving site in its current use**		
		Option 1	**Option 2**	**Option 3**
Redevelopment cost (A)	-	$105 mn	$58 mn	$57 mn
Gross sales revenue	-	$223 mn	$147 mn	$149 mn
Net sales revenue inc'g sales expenses (B)	-	$215 mn	$142 mn	$143 mn
Residual land value (C=B-A)	-	$110 mn	$84 mn	$86 mn
Current land value	$15.9 mn	$15.9 mn	$15.9 mn	$15.9 mn
Total land acquisition cost for redevelopment (D)	-	$18.3 mn	$18.3 mn	$18.3 mn
Net profit from redevelopment (E=C-D)	-	$91 mn	$65 mn	$68 mn
Feasibility ratio (C/D)	-	5.96	4.55	4.67
Net profit / land purchase & finance cost (E/D), i.e. comparison with leaving the site as is	-	4.96	3.55	3.67

Source: SGS 2014

These results show that all suggested redevelopment options are feasible. The feasibility ratio on each option is higher than 1, and the development under each option delivers a net positive profit. As the ratio of the estimated net profit compared with the existing land value is higher than one, this suggests that each of these redevelopment options produces a greater return than the base case (the site in its current form).

It is also clear that suggested redevelopment options with a higher residential component achieve better returns. This is undoubtedly driven by the high anticipated sale prices for residential prices in the analysis.

The analysis undertaken in the next section sheds more light on the sensitivity of these results to underlying values, i.e. to test what happens when key assumptions used in the feasibility model are changed. Sensitivity testing is undertaken to assess the impact on results of situations which may arise, and which are different to what has been accounted for in the baseline model.

- **Sensitivity testing**. In order to undertake the sensitivity, two scenarios were conceptualised, both of which alter the following three key drivers or assumptions of the analysis:
  - The anticipated developer's margin
  - The assumed sale price for residential units, and
  - The underlying land value.

These two sensitivity scenarios differ in their scope as follows:

SENSITIVITY SCENARIOS

	Sensitivity Scenario 1	Sensitivity Scenario 2
Developer's profit margin	5% higher than baseline	10% higher than baseline
Revenue from apartment sales	10% lower than baseline	20% lower than baseline
Land cost	10% higher than baseline	20% higher than baseline

Source: SGS 2014

The developer's margin of 20% assumed in the baseline model is on par with industry standards. Consequently, the possibility of the developer's profit margin being higher than this ratio as assumed in both sensitivity scenarios is unlikely. However, revenue from apartments sales and land cost analysis was assessed by SGS based on recent sales data in the neighbourhood. Property market conditions could indeed change quickly, and consequently, it is somewhat probable that sales revenue could be lower and land cost higher than anticipated in the baseline. Consequently, both sensitivity scenarios seem plausible.

It is worth clarifying that both sensitivity scenarios conceptualise a situation worse than the estimated baseline. This acknowledges the rather robust feasibility estimates derived in the baseline. It was thought that any improvement in these suggested drivers would make the development even more feasible compared with the baseline. The results of the sensitivity are shown in the two tables below

FEASIBILITY RESULT: SENSITIVITY SCENARIO 1

	Base Case Option, i.e. current land value	Relative to base case, i.e. leaving site in its current use		
		Option 1	Option 2	Option 1
Redevelopment cost (A)	-	$109 mn	$60 mn	$59 mn
Gross sales revenue	-	$201 mn	$133 mn	$137 mn
Net sales revenue inc'g sales expenses (B)	-	$193 mn	$127 mn	$132 mn
Residual land value (C=B-A)	-	$84 mn	$67 mn	$72 mn
Current land value	$17.5 mn	$17.5 mn	$17.5 mn	$17.5 mn
Total land acquisition cost for redevelopment	-	$20.1 mn	$20.1 mn	$20.1 mn
Net profit from redevelopment (E=C-D)	-	$64 mn	$47 mn	$52 mn
Feasibility ratio (C/D)	-	4.18	3.34	3.59
Net profit / land purchase & finance cost (E/D), i.e. comparison with leaving the site as is	-	3.18	2.34	2.59

Source: SGS 2014

FEASIBILITY RESULTS: SENSITIVITY SCENARIO 2

	Base Case Option, i.e. current land value	Relative to base case, i.e. leaving site in its current use		
		Option 1	Option 2	Option 1
Redevelopment cost (A)	-	$114 mn	$63 mn	$62 mn
Gross sales revenue	-	$179 mn	$118 mn	$125 mn
Net sales revenue inc'g sales expenses (B)	-	$172 mn	$113 mn	$120 mn
Residual land value (C=B-A)	-	$59 mn	$51 mn	$59 mn
Current land value	$19.1 mn	$19.1 mn	$19.1 mn	$19.1 mn
Total land acquisition cost for redevelopment (D)	-	$21.9 mn	$21.9 mn	$21.9 mn
Net profit from redevelopment (E=C-D)	-	$37 mn	$29 mn	$37 mn
Feasibility ratio (C/D)	-	2.68	2.31	2.68
Net profit / land purchase & finance cost (E/D), i.e. comparison with leaving the site as is	-	1.68	1.31	1.68

Source SGS: 2014

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These results show that even with quite a pessimistic scenario compared with the estimated baseline (as conceptualised by Sensitivity Scenario 2), the development options remain feasible. Indeed the feasibility ratio remains quite healthy at above 2, even under such a scenario.

CONCLUDING REMARKS

This letter is aimed at assessing the value of rezoning industrial land at 67-73 Lords Road, Leichhardt given preliminary outputs from the Industrial Lands study. While some critical parts of the industrial lands study are still in progress (most notably the demand forecasts and supply-demand gap assessment), it is still possible to draw some initial conclusions from the work to date. These have been organised under the criteria for rezoning assessment established in the Leichhardt Employment and Economic Development Plan 2013-2023.

- Would the rezoning result in insufficient land industrial land being available for current and future demand for industrial land in the LGA, at a minimum?
  - Although a relatively small precinct, it functions well as local light industrial land. The loss of the land must also be seen in the context of both supply-side pressures. On the supply side, the LGA has relatively low stocks of industrial land that have continued to dwindle in recent years. On the demand-side, population growth, a likely increase in the 'competitive offer' of the precinct following West Connex completion, and the Bays precinct renewal are likely to place more pressure on industrial land availability in the LGA.
  - In the context of persistent demand and low supply, a rezoning would seem likely to dilute the ability of Council to provide sufficient land to accommodate demand. However, It is not possible to answer this question fully without completing a quantitative assessment of industrial floorspace demand and a local supply-demand gap assessment.
- Would the rezoning of the site result in the fragmentation of a larger industrial precinct or erode the viability of a locally or regionally significant industrial precinct?
  - Rezoning of the site would not result in the fragmentation or a larger industrial precinct or erode the viability of a locally or regionally significant precinct.
  - A rezoning would obviously remove this land from the supply of local service/ light industrial land in the LGA. The precinct is fully tenanted and is functioning well so the loss of this precinct as industrial space would be significant. Although having a local service/ light industrial character, the precinct also houses some non-industrial activity (martial arts centre, art auction rooms, church, etc.) as well as having a small office component (5% of GFA). In this light, the precinct may be a good example of a flexible industrial area and one that could be well positioned to attract creative businesses and/ or higher value light manufacturing activity if spaces are suitably configured. The provision of light rail service boosts attractiveness for these function (just as it boosts suitability for medium density residential and mixed use development)
- Would the rezoning be consistent with adopted Council and/or State Government Policy regarding the future role and demand for industrial land? What impact would it have to Council's employment targets?

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- According to Mecone data, the precinct currently employs 62 workers. The proposed residential development with childcare facility and café would produce few workers and would result in a net loss of jobs.
- At this stage it is not possible to quantify the effect of rezoning in terms of the ability of the LGA to meet job targets. However, given that there are no vacancies at the Lords Rd precinct, and there are relatively low stocks of industrial land elsewhere in the LGA coupled with some significant demand – side drivers (such as West Connex and the Bays Precinct renewal) we suggest that a rezoning would not be appropriate before a full supply-demand gap assessment is completed.

- Does the site(s) have characteristics required by light or high tech industrial uses and other uses permitted in the zone/seeking floorspace in the LGA or subregion (e.g. floorspace, access, proximity to economic infrastructure, parking, infrastructure, storage, building configuration and land value)?
  - Suitability mapping has shown that the Lords Rd precinct achieves a lower score than similarly zoned precincts elsewhere in the LGA. This is largely the result of other sites having better access to major roads. We acknowledge that these scores would likely change as a result of West Connex completion – further improving the competitive offer of the precinct It should also be noted that 'less suitable' certainly does not mean 'unsuitable' for local light industrial use. The site fulfils the requirements of local service/ light industrial business.
- Would it be economically viable to improve the site to attract new tenants or to adapt to changing industry requirements and to ensure that the land uses on the site address compatibility with surrounding uses?
  - The site is economically viable in its current form. Road accessibility is sufficient for local light industrial use and public transport accessibility is very good. There may be potential to reconfigure spaces on site to allow higher office components or more flexible space that would appeal to higher value and higher employment density uses (such as creative business).
- Would the retention of industrial uses on the site result in a positive net benefit to the community as a whole?
  - As the precinct is currently functioning well, rezoning would clearly have a negative impact in terms of the loss of jobs and the loss of population serving industrial land. Whether this is outweighed by the provision of housing (and affordable housing in particular) largely depends on whether the loss of this industrial precinct would affect the ability of the LGA to meet its employment targets and or whether it would result in insufficient supply of local service industrial land given the needs of the current and projected population. This question will be answered as part of the industrial lands study.

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