SYDNEY CBD OFFICE MARKET REPORT

H2 2021

EXECUTIVE SUMMARY

As we pass the two-year mark since the start of the COVID-19 pandemic in Australia, there is strong evidence that office markets around the country are recovering at a promising pace, including that of the Sydney CBD, which continues to be a compelling and well-connected destination for businesses and employees.

Our latest Sydney CBD Office Market report explores the current state of the market and the macroeconomic factors and emerging trends that are shaping its journey to recovery.

There are many signs the CBD office market is rebounding to pre-pandemic levels, or at least that previous rises recorded in key fundamentals are slowing down. This includes the Sydney CBD Total Vacancy Rate recording an immaterial increase of eight (8) basis points (bps) in the second half of 2021 (2H 2021). While this remains above the 30-year historical average of 8.73 percent (%), the main contributor to this rise in vacancy was the listing of refurbished office stock back to the market without pre-commitments, such as the full refurbishment of 570 George Street and the partial refurbishment of 75 Pitt Street.

Furthermore, strong tenant demand led to positive net absorption recorded in this six-month period; a result of tenant expansion and relocations back into the CBD from suburban offices.

Pleasingly, sub-leasing vacancy fell below the historical average for the first time since the beginning of the pandemic as many businesses reclaimed sub-leasing spaces to allow for hybrid working arrangements for employees.

With the recommencement of international travel and the lifting of work from home (WFH) and office face mask requirements by the NSW Government earlier this year, we anticipate the CBD office market will attract increasing levels of cross-border and domestic capital as 2022 continues.

Furthermore, business confidence is poised to continue an upward trajectory, particularly as the influx of skilled overseas workers place further downward pressure on the already-low unemployment rate. This will boost tenant demand for office space and in turn, attract further investment into Sydney CBD and ensure it remains a market with rewarding yields.

If you would like to discuss this report or enquire about how a bespoke market analysis can help you achieve prosperity through property, we'd be delighted to speak with you.

ANDREW HUNTER

CHIEF EXECUTIVE OFFICER
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VACANCY

VACANCY BREAKDOWN

From July 2021, total vacancy increased by just eight basis points (bps) to 9.33% in the six months to December 2021.

Despite no major development completions in the six-month reporting period, net supply recorded a positive of 13,078 square metres (sqm). This can be entirely attributed to the completion of major refurbishments releasing stock with no pre-commitments back onto the market including 570 George Street (18,215 sqm) and 75 Pitt Street (2,100 sqm) contributing to a total 0.39% increase in vacancy.

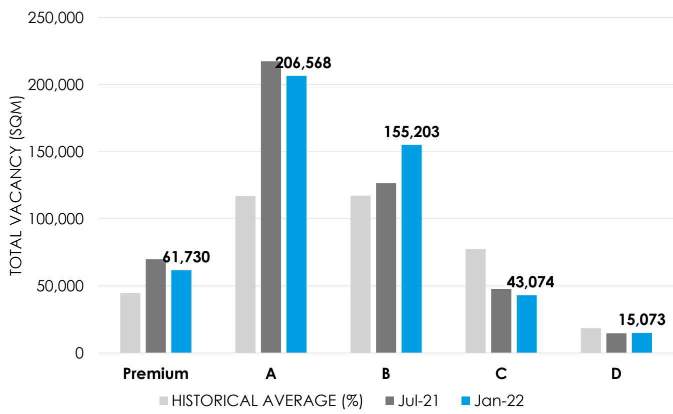
However, this was partially offset by solid tenant demand as many occupiers expanded their space commitments in the six months, resulting in the CBD recording positive net absorption (+7,812 sqm).

The largest contributor to this overall rise in total vacancy was observed within B-grade stock which experienced an additional vacancy of 1.9 bps (+28,746 sqm) to 11.3%. This equates to a staggering 3.3% above the B-grade historical average (8.0%) and is the highest quantity of vacant B-grade stock in Sydney CBD since December 2012.

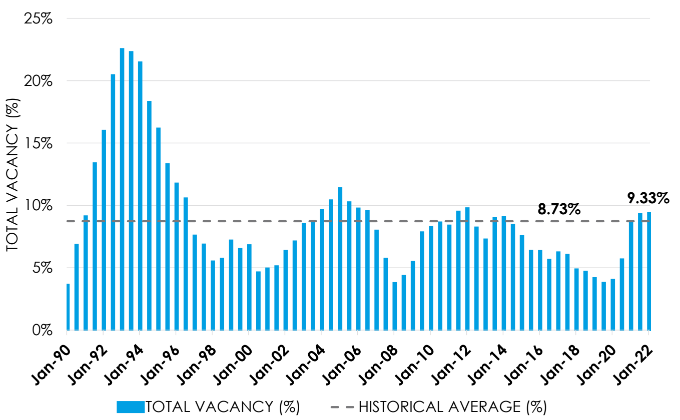
On the other hand, the rise in total vacancy was partially offset by the relatively large decreases in vacant Premium-grade and A-grade stock which both fell by -0.6 bps (-8,070 sqm and -10,942 sqm) to 4.9% and 10.8% respectively.

The largest portion of total vacant stock remains in the A-grade market (42.9%) equating to 206,568 sqm. However, A-grade stock has witnessed a sharp 5% decline in the six-month reporting period.

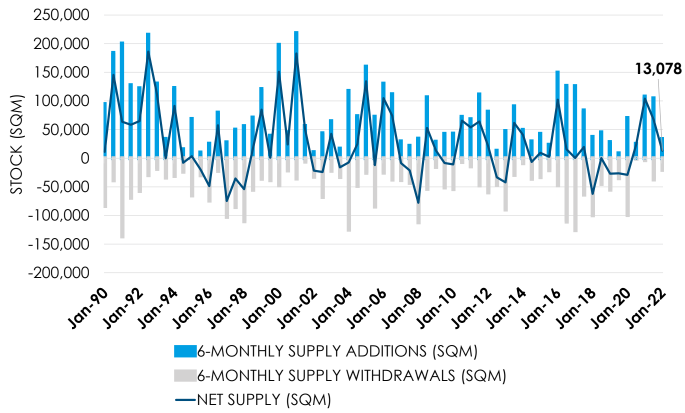
TOTAL VACANCY BY GRADE



TOTAL VACANCY VS HISTORICAL AVERAGE



SUPPLY ADDITIONS, WITHDRAWALS AND NET SUPPLY



SUB-LEASING

Sub-lease vacancy decreased by 30 bps to 0.95% in the six months to December, falling below the historical average of 1.0%.

BY PRECINCT:

The Midtown precinct remains the primary location of total vacant sub-leasing stock (44.9%) at 22,096 sqm despite also witnessing a substantial decline (19.1%).

The Western precinct has witnessed the most significant reduction in total sub-leasing space, which experienced a substantial fall of 63.3% to only 4,637 sqm, driven by a dramatic decline in A-grade sub-leasing space (currently 2,809 sqm).

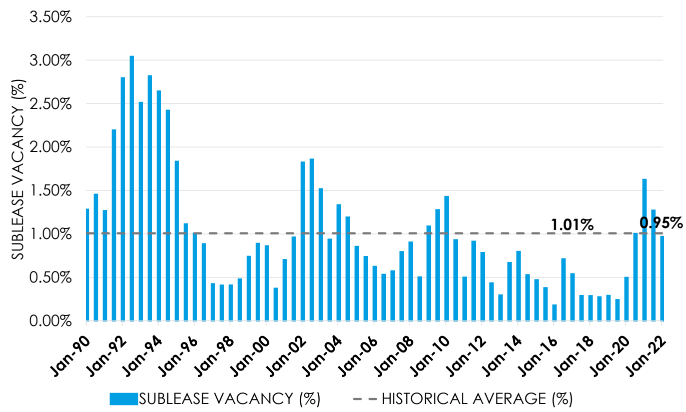
Recent leasing transactions involving significant take-up of Sub-lease space include:

- **RPS APP Consulting** has recently taken 1,539.5 sqm of A-grade Sub-lease space on Level 13 of 420 George Street for a five-year term beginning April 2022.
- **University Chambers** has taken 1,548 sqm of A-grade Sub-lease space on Levels 9 – 10 at 167 Macquarie Street for a 10-year term beginning February.
- **Mable Technologies** has expanded its existing A-grade Sub-lease space of 620 sqm to 1,474.8 sqm in Suites 12.01 – 12.02 at 255 Pitt Street for a two-year term beginning December 2021.
- **Armstrong Legal** has taken 946 sqm of A-grade Sub-lease space on Level 8 of 66 Goulburn Street for a five-year term beginning November 2021.
- **KordaMentha** has renewed its 1,228 sqm of Premium grade Sub-lease space in Suite 5.01 of 2 Chifley Square for a further seven-year term beginning August 2021.

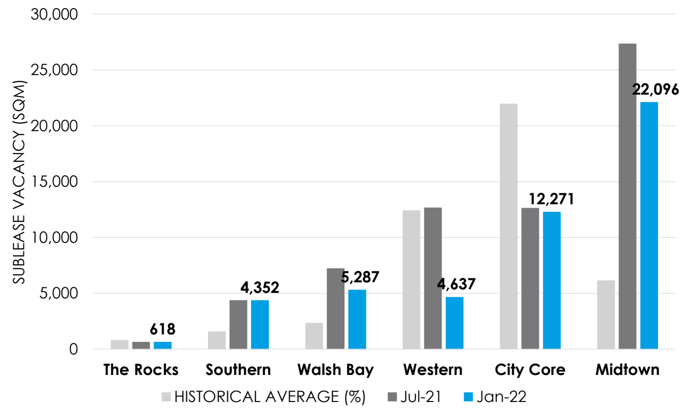
BY GRADE:

Total A-grade sub-leasing stock experienced the largest decrease (-43.4%). This can be attributed to many businesses continuing to reclaim the Sub-lease space they had placed on the market earlier in the pandemic, with a majority of this being prime stock (-33.9%).

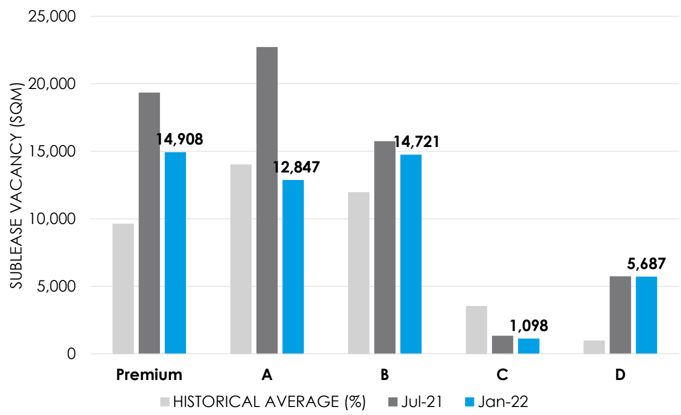
SUB-LEASE VACANCY VS HISTORICAL AVERAGE



SUB-LEASE VACANCY BY PRECINCT



SUB-LEASE VACANCY BY GRADE



OCCUPANCY
AND DEMAND

MAJOR OCCUPIERS UPDATE

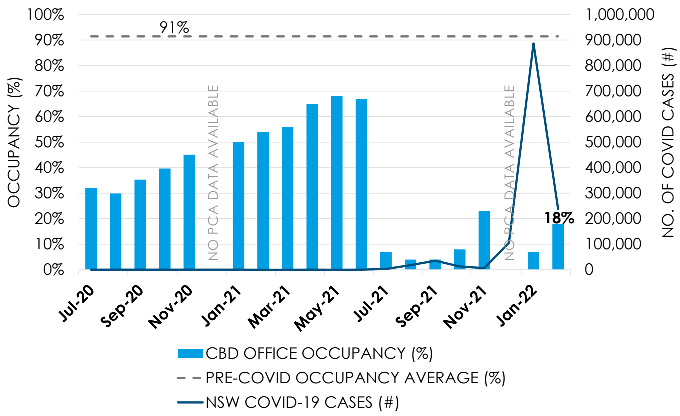
- **Football Federation Australia** has vacated 1,440 sqm of B-grade space at 1 Oxford Street, Darlinghurst and has relocated to 2,929 sqm of A-grade space at 1 Shelley Street.
- **The College of Law** has vacated 4,605 sqm of B-grade space at 12 Chandos Street, St Leonards to occupy approximately 5,000 sqm of B-grade space at 570 George Street which has recently undergone a full refurbishment.
- **Australian Taxation Office (ATO)** will be vacating 22,931 sqm of A-grade space at 680 George Street to take up approximately 13,000 sqm of A-grade space at 255 George Street in October 2022.
- **Bank of Queensland** has vacated approximately 3,900 sqm of Premium grade space at 2 Chifley Square to take up 7,255 sqm of A-grade space at 255 George Street.
- **Clifford Chance** will be relocating from 1,188 sqm of A-grade space at 1 O'Connell Street to 2,611 sqm of Premium space at Wynyard Place, 10 Carrington Street in July 2022.
- **International SOS** will be vacating 2,576 sqm of A-grade space at 4 Drake Avenue, Macquarie Park, to relocate to 1,100 sqm of A-grade space at 45 Clarence Street in June 2022.

OCCUPANCY

With NSW spending the majority of 2021's winter months in lockdown, Sydney CBD offices had an occupancy rate of only 4% occupied until November 2021 when occupancy gradually increased to 23%.

However, the emergence of the Omicron variant in early December 2021, has resulted in office occupancy in Sydney CBD to plunge once again at just 7% in Jan 22.

SYDNEY CBD OCCUPANCY VS NSW COVID-19 CASES



TENANT DEMAND

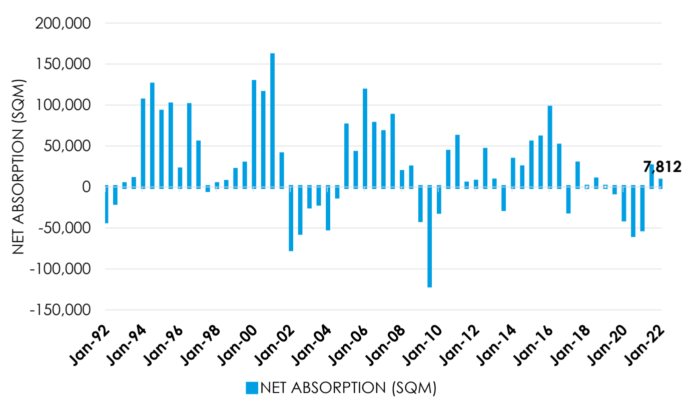
Despite an overall low occupancy level in Sydney CBD offices from July to December, Sydney CBD still experienced solid tenant demand with the six-monthly net absorption figure continuing to remain positive (+7,812 sqm).

The major contributor to this positive outcome was a result of tenants moving into Sydney CBD offices from other suburbs including the **Australian Institute of Music** vacating 5,700 sqm of B-grade space at 1 Foveaux Street in Surry Hills and relocating to 4,000 sqm of C-grade space at Foreshore House, 66 Harrington Street.

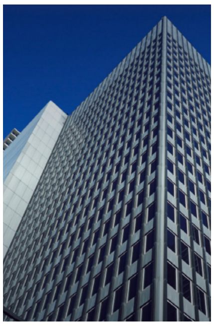
On the other hand, some large tenants exited the CBD for suburban offices such as **Caltex Australia** vacating 7,220 sqm of A-grade space at 2 Market Street to occupy 4,750 sqm at 29 Bourke Road, Alexandria. **Link Market Services** also vacated 4,896 sqm of A-grade space at 680 George Street to take up 22,000 sqm of A-grade space at 6-8 Parramatta Square, Parramatta.

Observing these tenant movements, it is clear that after months of economic and business uncertainty and impacts, commercial tenants are determining their office locations, quality and sizes for the future with confidence.

SYDNEY CBD OFFICE NET ABSORPTION



SUPPLY AND DEVELOPMENT



570 George Street

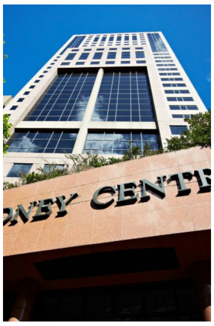
(Full Refurbishment)

570 George Street has undergone a full building refurbishment as of Q2 2021. From basement, ground level and mezzanine up to Levels 1 - 23, the 18,100 sqm A-grade office tower has upgraded its lift lobby, internal lift cars, office fit-out and building services at a total cost of $31.8 million.

Munich RE House

(Full Refurbishment)

143 Macquarie Street is currently undergoing a full refurbishment of its 3,670 sqm NLA, estimated to be completed by Q2 2022. The 13-storey B-grade building was recently refurbished with new end-of-trip amenities and a new lobby in 2020.



Sydney Central

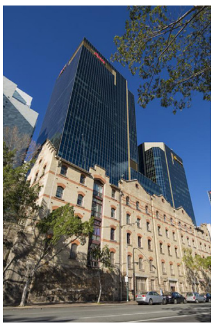
(Partial Refurbishment)

477 Pitt Street is currently undergoing a partial refurbishment of 6,700 sqm Net Lettable Area (NLA) of its A-grade office space. This refurbishment accounts for approximately 13.9% of its 48,092 sqm of total NLA.

National Australia Bank House

(Partial Refurbishment)

255 George Street is currently undergoing a partial refurbishment of 19,000 sqm of its 39,981 sqm NLA of A-grade office space, estimated for completion by Q2 2022.



AON Tower

(Partial Refurbishment)

Similarly, 201 Kent Street is currently undergoing a partial refurbishment of 2,650 sqm of its 39,932 sqm NLA of B-grade office space.

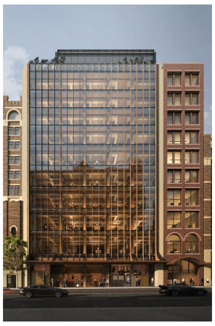
Quay Quarter Tower

(New Development)

Located at 50 Bridge Street in Circular Quay, Quay Quarter Tower has recently been completed. The new Premium-grade 50-storey office building is over 90% pre-committed to tenants such as AMP Capital, Deloitte, Corrs Chambers Westgarth and Barrenjoey.

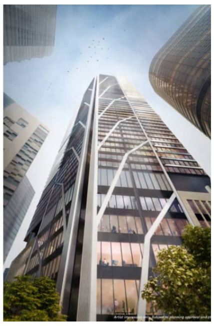
AMP Building
(Full Refurbishment)

AMP Capital will also be undertaking a full internal and external refurbishment of the existing 27-storey commercial office building known as the AMP Building. To be completed by Q1 2025, this will include renewal of the 50-year-old building's ground and Level 1 lobby, as well as all retail tenancies, the end-of-trip facilities and reinstatement of the tower walls and facade.



King York House
(New Development)

Expected to be completed by Q1 2023, 32-36 York Street is currently under construction for 7,772 sqm NLA of space spanning 11 storeys.



Salesforce Tower
(New Development)

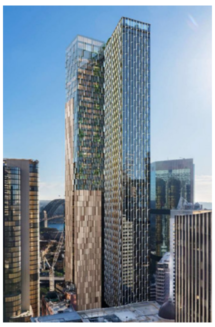
Lendlease is currently in the process of constructing the 56-storey office tower at 180 George Street at an estimated cost of $590.7 million. Dubbed the "Salesforce Tower" after its anchor tenant Salesforce which has pre-committed to the top 24 floors, the building - which spans over 55,000 sqm in Net Lettable Area (NLA) is due for completion in Q3 2022.

Darling Park (Tower 4)
(New Development)

GPT Group, AMP Capital and Brookfield have partnered to develop a 40-storey commercial office tower. The building is currently under at DA stage and will offer 65,000 sqm of NLA with 12,000 sqm of retail space and is estimated for completion by 2026.

Poly Centre
(New Development)

Construction is currently in progress for Poly Centre at 210 George Street for a 28-storey commercial office tower with ground and first-floor retail. Due for completion in Q3 2022, the office tower will span 16,500 sqm of NLA office space across 26 levels.



37 - 55 Pitt Street
(New Development)

Mirvac is currently undertaking site works for 63,000 sqm NLA of office and retail space. Estimated to be completed in 2027, the tower will cost $1.5 billion with a stage 2 DA being being lodged and currently under assessment.

SYDNEY CBD CURRENT DEVELOPMENTS

1 **570 George Street**
GFA 21,930 sqm

2 **183-185 Clarence Street**
GFA 9,603 sqm

3 **10 Carrington Street**
GFA 75,000 sqm

4 **275-281 George Street**
GFA 8,023 sqm

5 **65 Martin Place**
GFA 29,168 sqm

6 **50 Bridge Street**
GFA 102,133 sqm

7 **180 George Street**
GFA 61,894 sqm

8 **210-232 George Street**
GFA 20,148 sqm

9 **32-36 York Street**
GFA 8,595 sqm

10 **65-77 Market Street**
GFA 36,391 sqm

11 **4-6 York St and 341 George Street**
GFA 6,128 sqm

12 **50 Martin Place,**
5-19 Elizabeth Street
8-12 Castlereagh Street
and 55 Hunter Street
GFA 75,498 sqm

13 **125 Bathurst Street**
GFA 47,800 sqm

14 **39-49 Martin Place**
GFA 37,553 sqm

15 **189-197 Kent Street**
GFA 14,408 sqm

16 **3 Hosking Place**
GFA 3,093 sqm

17 **33 Alfred Street**
GFA 41,510 sqm

18 **133-145 Castlereagh Street**
GFA 100,000 sqm

19 **8-10 Lee Street**
GFA 70,256 sqm

20 **133-141 Liverpool Street**
GFA 24,042 sqm

21 **55 Pitt Street**
GFA 55,743 sqm

22 **200-202 Sussex Street**
GFA 6,530 sqm

23 **333-337 Kent Street**
GFA 15,061 sqm

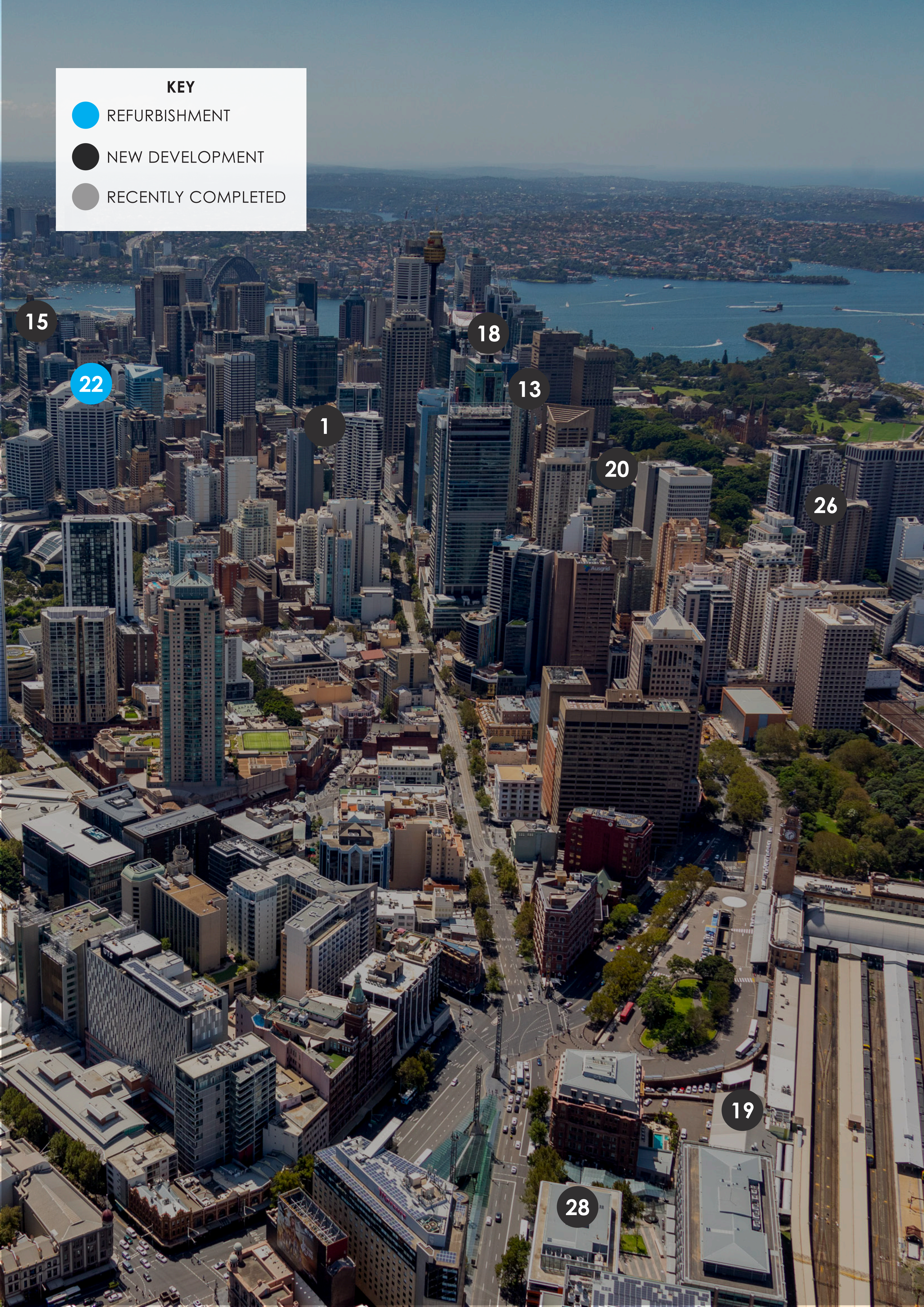
24 **37-55 Pitt Street**
GFA 72,307 sqm

25 **317 & 319-321 George Street**
GFA 5,570 sqm

26 **169-183 Liverpool Street**
GFA 51,168 sqm

27 **458-472 George Street**
GFA 57,989 sqm

28 **24 Lee Street**
GFA 155,000 sqm


KEY
REFURBISHMENT
NEW DEVELOPMENT
RECENTLY COMPLETED
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22
18
13
1
20
26
19
28

MARKET OUTLOOK

Over the next six years, 391,753 sqm NLA (+7.6% of total stock) of new Prime-grade office stock is expected to enter the Sydney CBD office market.

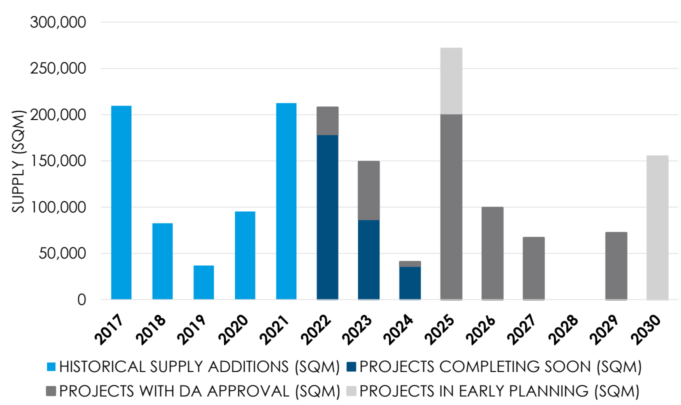
Over 2022, we see vacancy rising a further 0.5% and peaking at 9.8%, as an additional 146,740 sqm (+2.9% of total current stock) of new office space will be added to the market from new developments, of which an aggregate 66% is currently pre-committed. The flow-on effects of anchor tenants such as Salesforce, Deloitte and Corrs Chambers Westgarth relocating from their current premises in the CBD into the new developments at 180 George Street and Quay Quarter Tower will place an additional 41,300sqm (0.79%) of vacant stock back on the market.

> ***"While the pandemic triggered a sudden shift towards flexible working arrangements, it's clear they have given birth to a more significant structural shift in Australian workplaces about flexible working desires and are here to stay. However, this isn't bad news for the office market vacancy rate. With the nation's unemployment rate at almost record low levels (4.2%) despite over 390,000 vacant jobs in the market, signals a positive outlook for office vacancy levels in the near future."***
>
> **SHIRLEY FAN,**
> HEAD OF ASIA DESK

Tenants who have more recently signed pre-commitments for the remaining vacant suites in these upcoming developments include:

- **Greenhouse by Investible**, a soon-to-be launched growth and innovation hub for climate tech startups, will be taking up circa 3,711 sqm at 180 George Street.
- **JLL**, currently occupying 3,660 sqm of A-grade space at 420 George Street, will also be taking up 3,532 sqm over three levels at 180 George Street.
- **Johnson Winter & Slattery**, currently occupying 2,617 sqm of A-grade space at 20 Bond Street, will be taking up 3,056 sqm over two floors at Quay Quarter Tower at 50 Bridge Street in July 2023.
- **Barrenjoey**, currently occupying 3,250 sqm of Premium grade space at 161 Castlereagh Street, will also be taking up circa 5,000 sqm at 50 Bridge Street in December 2023.

SYDNEY CBD - HISTORICAL AND FORECAST SUPPLY



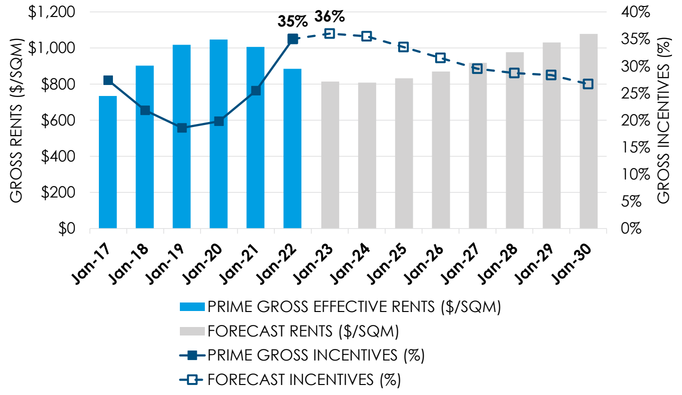
RENTS AND INCENTIVES

Average prime face rents continue to hold steady while gross prime incentives have risen by 9.5% from 32% over the last year to December 2021, currently sitting at an average of 35%. As a result, prime gross effective rents have witnessed a decline of 4.7% over the same period. This is unsurprising given the rise in current vacancy levels, leaving 481,648 sqm of vacant office stock on the market.

On a more positive note, office market fundamentals are experiencing solid growth, with the national unemployment rate at its lowest since 2008 at 4.2%, bolstered by a rise in job numbers of over 700,000 in the last year to December 2021. More specifically, white-collar employment growth in NSW increased by 4.2% year-on-year (YoY) to February 2022 (Australian Bureau of Statistics – ABS) and is forecast to continue growing at a steady rate of 1.8% per annum over the next decade.

Over 2022, we forecast prime gross effective rents to reach the bottom of the market as average incentives rise a further 1.0% from 35% to 36% and face rents hold steady.

SYDNEY CBD - HISTORICAL AND FORECAST RENTS AND INCENTIVES



Studies of the last three major economic downturns indicate similar patterns of recovery, wherein the full effect of the downturn on the office market is staggered over a lagged flow-through of two to three years. With a full supply pipeline of new large-scale developments due to hit the market over the next year and our subsequent forecast rise in vacancy, it is unlikely that the effective rents will recover until 2023.

A gradual recovery has been modelled thereafter, with prime gross effective rents returning to similar peak levels witnessed in 2019 by late 2027 to 2028. This is led by incentives steadily decreasing as the market recovers, while face rents begin to rise again, bolstered by new prime developments such as the various above-station integrated Metro office hubs over the next six years.

LEASING
TREND WATCH

The current leasing enquiries in the CBD office market have reflected the growing trend of tenant preferences for spaces with fit-outs included or newly refurbished speculative (spec) fit-outs, triggered by rising fit-out costs due to pandemic-related supply chain disruptions and labor shortages. On average, the cost of fit-out per sqm in the CBD increased by 22.1% YoY between 2020 and 2021 (Asia-Pacific Fit-out Cost Guide, JLL).

At CI, the majority (83.6%) of leasing enquiries from tenants over H2 2021 have been for spaces with existing fit-outs or refurbished spec fit-outs, with 13.9% having no preference for fitted or unfitted spaces and just 2.4% only considering spaces with no fit-outs.

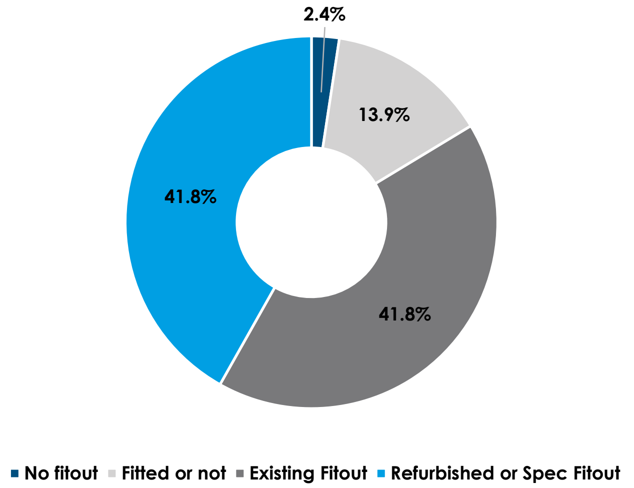
With rents still relatively high in Sydney CBD, many tenants have opted for spaces with fit-outs over spaces without in order to use incentives such as rent abatements to offset their rent over the term of the lease.

Examples of recent transactions at CI with tenants preferring fitted spaces are outlined below:

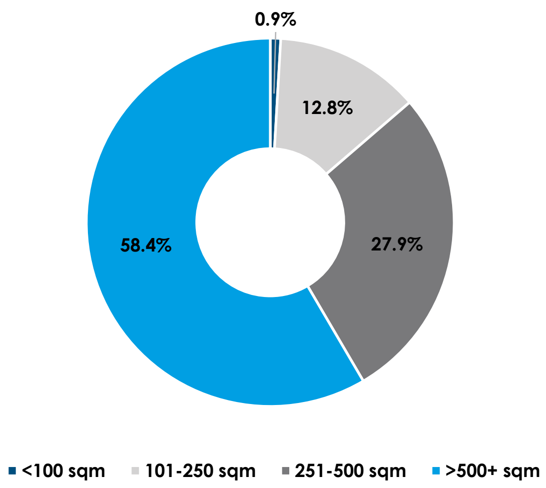
- **Stanton Road Partners** has moved into 310 sqm of Premium-grade space in Suite 10.02 of 126 Phillip Street, where the suite had recently undergone a full speculative fit-out.
- **Aston Chace Group** has taken up 222 sqm of A-grade space in Suite 13.02 of 35 Clarence Street. The space was offered with an existing fit-out, allowing the tenant an easy relocation.
- **Varga Brothers Investments** has taken up 144 sqm of B-grade space with a newly completed speculative fit-out in Suite 4.04 of 4 Martin Place.
- **Wybenga Partners** has moved into 424 sqm of B-grade space on Level 9 of 37 York Street, where the space had also recently undergone a full speculative fit-out.

> ***"The majority of our clients are focused on acquiring premises that are either partially fitted or fully fitted or can be done so by an external party. This in being driven by the ongoing impacts of COVID-19, the recently announced Federal Election and general global instability. We see this trend continuing for some time."***
>
> **BEAU STEWART,**
> HEAD OF TENANT REPRESENTATION SERVICES

CI LEASING ENQUIRY BREAKDOWN BY FITOUT



CI TENANT LEASING ENQUIRY BY NLA



"Tenant demand in the market reflects the want for a fit-out, be it existing or new spec fit-outs. While this is driving many landlords to speculatively fit-out anything below 500 sqm, we are also seeing whole floor spec fit-outs in the circa 1,000 sqm range based on enquiries.

This is impacting negotiations for open plan refurbished spaces, as landlords view the fit-out for a period longer than the initial term when negotiating terms for a speculative fit-out. Therefore, no make good is associated with the initial lease term and as the landlord is investing in the fit-out and no Incentive Guarantee is sought for upfront cash contribution provided to the tenant."

BEN KARDACHI,
DIRECTOR OF COMMERCIAL LEASING

CAPITAL TRANSACTIONS

VOLUME

As of H2 2021, the Sydney CBD office market experienced a total sales volume of $2.40 billion (Real Capital Analytics – RCA) in the six months to December 2021, a significant 54.5% increase against total transacted volumes in H1 2021 ($1.55 billion).

Note, these numbers are based on Real Capital Analytics' Trend Tracker. This accounts for the Hedonic Time Series of these figures (cap rates and pricing) to accurately represent the underlying trend and eliminate noise that often results from small data samples instead of a simple average of the transactions that have occurred in this reporting period.

While total 2021 sales volumes are also a 40.6% increase YoY compared to 2020, this represents only 63.5% of the pre-pandemic five-year average total sales volume between 2015 and 2019. This result indicates the steady, promising signs of recovery of commercial office assets in Sydney CBD, despite volumes not quite being at pre-COVID average levels.

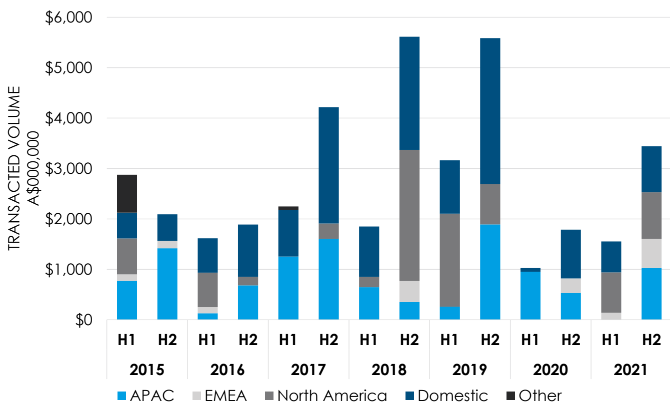
CROSS-BORDER ACTIVITY

H2 2021 recorded 73.5% of total sales volumes originating from cross-border investors ($2.53 billion). This is well above the average level of 58.3% based on the 2015 – 2019 volume breakdowns by cross-border activity, demonstrating Australia's strong underlying political and economic environment in navigating the pandemic with relatively high vaccination rates compared to other countries globally.

Over 2021, foreign capital accounted for 70.7% of total capital transaction volumes in the Sydney CBD with the most significant influx of investment flowing in from the United States and Canada.

The largest transaction recorded in the six-monthly period was US-based Blackstone's 50% purchase of Grosvenor Place, 225 George Street, for $925 million in December 2021.

CAPITAL TRANSACTIONS VOLUMES



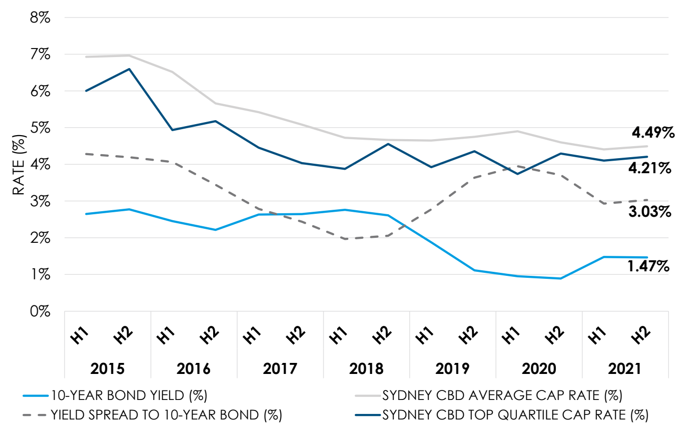
PRICING

Despite a higher total of transaction volumes in H2 2021, average capitalisation rates (cap rates) recorded a slight softening of +7.5 bps to 4.25%. However, average capital values across all transactions in the six months to December 2021 have risen to $21,356 per sqm (+14.3%). This can be attributed to the higher level of total vacancy in the CBD as well as the increasing risk-free rates following inflation and interest rate hikes to come in mid-2022, placing less pressure on cap rates.

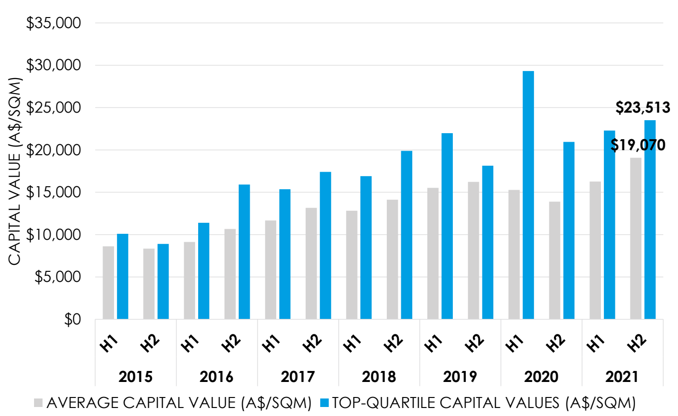
On the other hand, the lack of commercial assets for sale in the CBD continues to result in higher levels of demand, particularly from cross-border capital seeking a stable investment in the Sydney CBD office market. This can explain average capital values experiencing a rise in the six months to December 2021.

In the same reporting period, CBD prime assets saw top-quartile cap rates rise +11 bps to 4.21% and top-quartile capital values experience a slight increase (+5.47%) to average at $23,513 per sqm for prime grade office assets. This has been affected by the increase in face rents.

10-YEAR BOND TO YIELD SPREAD



AVERAGE & TOP-QUARTILE CAPITAL VALUES



RECENT NOTABLE TRANSACTIONS

- **Grosvenor Place** – Blackstone acquired a 50% stake in the Premium-grade asset at 225 George Street from Dexus and the Canadian investor CPP Investment Board for $925 million in December 2021. The sale represented a cap rate of 4.83% and a capital value of $21,635 per sqm. 225 George Street spans over 85,500 sqm NLA with key tenants including Deloitte which occupies 32.5% of the building.
- **309 – 321 Kent Street** – In December 2021, Ashe Morgan partnered with Liu Chong Hing Investment to acquire a 50% stake in the A-grade 309 – 321 Kent Street from Dexus. The $401 million transaction recorded a yield of 5.30% for the asset which spans over 47,700 sqm NLA.
- **77 Castlereagh Street** – Abacus Property Group purchased a 299-year leasehold from Blackstone at 77 Castlereagh Street for approximately $252 million in November 2021. This sale represents a core cap rate of 3.80% for the 13,161 sqm NLA A-grade building.
- **383 – 395 Kent Street** – Charter Hall acquired 383 – 395 Kent Street from Dexus in October 2021 for $385 million, representing a capital value of $21,411 per sqm for the A-grade asset with over 17,900 sqm NLA.
- **EY Centre, 200 George Street** – In a joint acquisition, Mirvac and British investor M&G Real Estate purchased a 50% stake in 200 George Street from AMP Capital in September 2021. This represents a reported yield of 4.30% and a capital value of $29,679 per sqm. The Premium-grade asset spans over 38,900 sqm NLA, occupied by key tenants such as EY, Mirvac and AGL Energy.

MARKET OUTLOOK

Macroeconomic Forecasts:

1. GDP, Unemployment Rate and Employment Growth

- In Q3 2021, Australia experienced a negative GDP growth rate of -1.9%. This was attributed to the Delta variant of COVID-19 resulting in lockdowns across the nation. However, Q4 2021, saw a positive result of +3.4% GDP growth as the less-severe Omicron variant saw a significantly smaller impact on Australian business operations. Overall, Australia recorded a positive GDP growth of 4.2% over the year of 2021 compared to 2020 results.
- As of February 2022, the Australian unemployment rate has fallen to the historical low of 4%, which was previously recorded in 2008 (ABS). The Reserve Bank of Australia (RBA) expects the unemployment rate to fall below full employment to 3.75% by the end of 2022 and anticipates this level to remain in the foreseeable future. Furthermore, employment growth has continued to improve into 2022, recording +3.1% growth YoY as of February, further supporting the growing tenant demand and anticipated business expansions.

2. Cash and Interest Rates

- The cash rate has remained at a record low of 10 bps for the fourteenth consecutive month since November 2020, with the RBA discussing rate hikes likely to occur in June -2022 to see the year end at 1%, with significant increases by 2023 to 2%.
- The 10-year government bond yield closed in December 2021 at 1.61% before rising to 2.11% in February-2022. With inflation recording a 3.5% rise over 2021, the RBA will be raising interest rates in the latter half of 2022. This has resulted in the gradual increase in the long bond yield experienced since August 2021 (+1.12%). With risk-free rates rising, this could potentially see cap rates softening as the cost of capital for assets such as real estate increases. However, long Weighted Average Lease Expiry (WALE) assets will provide solid hedging against this inflation risk.

Given the looming interest rate hikes, we see this will place downward pressure on domestic investors. On the other hand, we anticipate a higher percentage of total sales transactions in 2022 to come from foreign investors with relatively less competition from Australian capital.

As the leasing market continues to recover from the effects of the pandemic, we expect 2022 to bring a more positive outlook on pricing with many tenants having now finalised their location, quality and space commitments. Meanwhile, we foresee the Sydney CBD office market continuing to regain momentum following the recent average cap rates and capital values which remained steady throughout 2021.

"While rising interest rates will see an increase in the cost of debt for incoming purchasers, there is still a large weight of equity and capital looking for investment, particularly from pension funds, insurance and sovereign wealth funds. Commercial real estate, particularly long-WALE assets, typically provide hedging against inflation risk, with leases increasing on either a purely fixed basis or fixed amounts above CPI."

MIKE STOKES,
DIRECTOR OF CAPITAL TRANSACTIONS

TREND WATCH

Strata in the CBD

Over the last five years, strata in Sydney CBD has evolved into a two-tiered market. Legislative and planning changes to certain areas of the CBD have formed an upper tier of strata units transacting at record prices on a rate per sqm, while office units that fall outside of planning boundaries continue to be priced according to traditional assumptions such as yield, demand and supply.

In 2016, the "Strata Schemes Development Regulation" was finalized, and the City of Sydney's "City Plan 2036" was released for public review for the first time. Legislative changes lowered the unit entitlement (UE) required for a party to undertake the redevelopment of a strata building from 100% to only 75%, whilst the new city plan outlined potential "Tower Cluster" sites throughout the CBD, wherein maximum height restrictions would be lifted from the current 237m to 330m.

As a result, by Q4 2019, the strata market saw units, both office and retail, transacting for inflated prices between $20,000 - $35,000 per sqm – the large variance depending on the UE held by each unit. Removing all sales of units located within known tower cluster sites, the average price of an office strata unit in the CBD dropped down to $10,000 - $15,000 per sqm (Q4 2019), depending on the quality, location, aspect and associated car parking.

Upon the onset of the pandemic in March 2020, the secondary - tier strata market saw average prices decline below the $10,000 per sqm mark, whilst purchases of units for strata amalgamation and redevelopment purposes remained at the same levels.

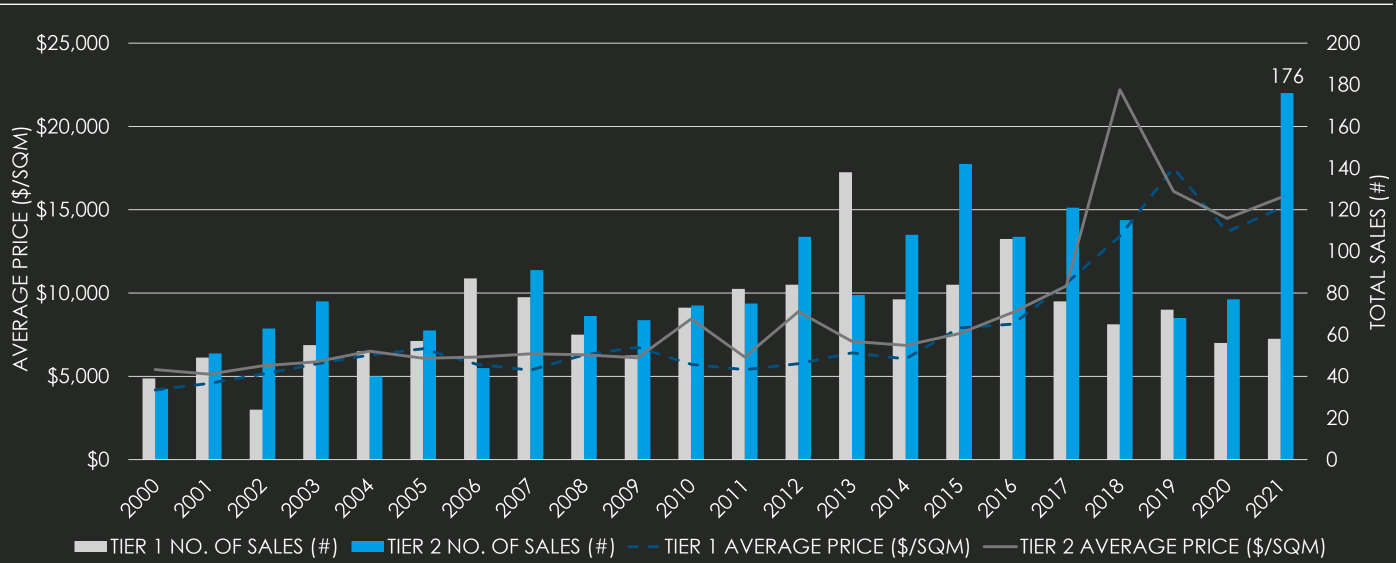
As 90% of strata units in the CBD are tenanted by small-to-medium businesses (CoreLogic, 2020) who were most likely eligible for COVID-19 rent relief during the pandemic, it is unsurprising that purchases made over 2020 from a pure investment standpoint struggled to maintain the inflated prices from 2019.

"As of H2 2021, the Sydney CBD strata office market has seen increased demand for secondary-tier strata suites, as tier 1 strata within the tower cluster zones continue to be withdrawn for large developments such as the Hunter Street Metro Station and the Kings Green supersite at 71-73 York Street. This subsequent diminishing supply of strata has driven higher demand for secondary- tier strata which has in turn resulted in a 129% YoY increase in the number of tier 2 strata sales from 2020 to 2021, with average tier 2 prices also increasing by 8.6% YoY. As of 2021, the average tier 2 strata price ($15,727 per sqm) has exceeded that of tier 1 strata, despite the latter being within the tower cluster zones. This can be attributed to the limited opportunities where a large enough site area (at least 2,000 sqm) is available for any development potential.

As a result, we anticipate the strata office market will continue trading strongly across both tiers, and upward pressure to be exerted on average prices due to the shrinking supply of this asset class."

ANDREW BABICCI,
SALES EXECUTIVE

AVERAGE STRATA PRICES



H2 2021 FREEHOLD TRANSACTIONS

DATE	BUILDING NAME	ADDRESS	NLA (SQM)	TOTAL PRICE (A$, 100%)	% SHARE	ACTUAL PRICE (A$)
01-Dec-21	Grosvenor Place (Leasehold)	225 George Street	85,508.91	$1,850,000,000	50%	$925,000,000
01-Dec-21	309-321 Kent Street	309-321 Kent Street	47,700.84	$802,000,000	50%	$401,000,000
01-Nov-21	10 Barrack Street	10 Barrack Street	9,594.77	$199,000,000	100%	$199,000,000
01-Nov-21	77 Castlereagh Street	77 Castlereagh Street	13,160.68	$252,000,000	100%	$252,000,000
01-Oct-21	333 Kent Street	333 Kent Street	14,241.65	$130,000,000	25%	$32,500,000
01-Oct-21	383 Kent Street	383-395 Kent Street	17,981.56	$385,000,000	100%	$385,000,000
01-Sep-21	390-396 Pitt Street	390-396 Pitt Street	3,521.00	$70,100,000	100%	$70,100,000
01-Sep-21	7-9 Wilmot Street	7-9 Wilmot Street	724.00	$11,000,000	100%	$11,000,000
01-Sep-21	EY Centre	200 George Street	38,982.05	$1,156,957,000	50%	$578,478,500
01-Jul-21	Roy Morgan Building	230-232 Sussex Street	1,099.97	$20,000,000	100%	$20,000,000
01-Jul-21	1 Bligh Street	1 Bligh Street	43,417.94	$1,125,000,000	33%	$374,962,500

A$/SQM	REPORTED YIELD	GRADE	PURCHASER	VENDOR
$21,635.17	4.83%	Premium	Blackstone	CPP Investment Board, Dexus
$16,813.12	5.30%	A	Liu Chong Hing Inv, Ashe Morgan	Dexus Wholesale Property Fund
$20,740.47		B	Shayher Group	AEW Capital
$19,147.95	3.80%	A	Abacus Property Group	Blackstone
$9,128.15	N/A	B	Addenbrooke, Phoenix Property Investors	Glory Star
$21,410.82	5.30%	A	Charter Hall Group	Dexus
$19,909.12	4.42%		Teak Four Pty Ltd	Reserve Hotels Pty Limited
$15,193.37	N/A		Wilmot Street Pty Ltd	Yeh's Family Holdings Pty Ltd
$29,679.23	4.30%	Premium	Mirvac, M&G Real Estate	AMP Capital Investors
$18,182.26	VP		Ajmj Sussex Street Pty Ltd	Belvedere Enterprises Aust Pty Ltd
$25,910.95	4.38%	Premium	Dexus, Mercatus Co-operative Limited	Cbus Property

H2 2021 STRATA TRANSACTIONS

DATE	ADDRESS	UNIT #	NLA (SQM)	SALE PRICE (A$)	A$/SQM	LOCATED WITHIN TOWER CLUSTER
01-Jul-21	25 Lime Street	Unit 301	180.00	$3,350,000	$18,611.57	N
01-Jul-21	109 Pitt Street	Unit 1406	64.00	$1,168,000	$18,250.45	Y
02-Jul-21	235 Macquarie Street	Unit 12	104.00	$1,551,000	$14,913.83	N
02-Jul-21	95-99 York Street	Unit 15	164.00	$1,750,000	$10,670.73	Y
15-Jul-21	84 Pitt Street	Unit 1204	177.00	$2,170,000	$12,260.19	N
19-Jul-21	50-54 York Street	Unit 603	94.00	$1,130,000	$12,021.57	Y
26-Jul-21	104-118 Clarence Street	Unit 23	82.00	$1,271,000	$15,500.38	Y
30-Jul-21	33-35 York Street	Lot 21	534.00	$14,000,000	$26,217.23	N
30-Jul-21	127-131 Macquarie Street	Lot 13	522.99	$13,500,000	$25,813.25	N
02-Aug-21	74 Pitt Street	Lot 1	476.00	$18,000,000	$37,815.13	N
06-Aug-21	64-68 Castlereagh Street	Units 28,29,46 & 47	314.99	$5,500,000	$17,460.74	N
12-Aug-21	12-14 O'Connell Street	Unit 94	99.00	$1,395,698	$14,098.30	Y
12-Aug-21	82 Elizabeth Street	Unit 8	214.99	$2,970,000	$13,814.29	N
19-Aug-21	69-75 King Street	Unit 8	140.00	$1,910,000	$13,643.19	Y
27-Aug-21	309-313 Pitt Street	Unit 11	384.99	$3,591,330	$9,328.36	N
27-Aug-21	60-66 Hunter Street	Lot 64, 11FL	808.00	$14,750,000	$18,254.95	Y
31-Aug-21	301 Castlereagh Street	Unit 35	86.00	$785,000	$9,128.13	N
02-Sep-21	37 York Street	Unit 12, 29, & 45	445.99	$6,150,000	$13,789.57	N
07-Sep-21	650 George Street	Unit 2	153.00	$1,680,000	$10,980.66	Y
14-Sep-21	16 O'Connell Street	Unit 6	276.99	$4,986,000	$18,000.44	Y
15-Sep-21	95-99 York Street	Level 6	156.00	$1,930,000	$12,372.10	Y

H2 2021 STRATA TRANSACTIONS

DATE	ADDRESS	UNIT #	NLA (SQM)	SALE PRICE (A$)	A$/SQM	LOCATED WITHIN TOWER CLUSTER
17-Sep-21	26A Lime Street	Unit 4	119.00	$1,575,000	$13,235.62	N
07-Oct-21	51-53 Druitt Street	Lot 13, 17-22	1,301.97	$14,100,000	$10,829.76	N
12-Oct-21	50 Clarence Street	Unit 104	64.00	$1,230,000	$19,219.22	N
18-Oct-21	362-370 Pitt Street	Unit 203	290.99	$3,783,000	$13,000.32	Y
19-Oct-21	60-62 York Street	Unit 2	165.00	$2,345,000	$14,212.47	Y
26-Oct-21	209-211 Clarence Street	Unit 15	197.00	$2,585,000	$13,122.15	Y
01-Nov-21	229-231 Macquarie Street	Unit 10 & 11	130.00	$2,160,000	$16,615.38	N
01-Nov-21	60 Park Street	Unit 25	219.99	$4,800,000	$21,818.71	Y
04-Nov-21	109 Pitt Street	Unit 1307	116.00	$2,250,000	$19,397.03	N
05-Nov-21	60 Park Street	Unit 28	102.00	$2,600,000	$25,490.82	Y
05-Nov-21	82 Elizabeth Street	Unit 301	95.00	$1,300,000	$13,684.54	N
08-Nov-21	263-265 Castlereagh Street	Unit 803	121.00	$1,730,000	$14,297.87	Y
10-Nov-21	82 Elizabeth Street	Unit 5	216.99	$3,000,000	$13,825.22	N
16-Nov-21	45-47 York Street	Lots 1, 4-6, 9, 11, 21, 23-26 * 28	2,722.93	$38,800,000	$14,249.34	N
22-Nov-21	315-321 Pitt Street	Unit 612-613	79.00	$1,425,000	$18,038.41	N
23-Nov-21	45 York Street	Unit 28	84.00	$1,372,140	$16,335.40	N
23-Nov-21	45 York Street	Unit 23	115.00	$1,707,750	$14,850.36	N
23-Nov-21	45-47 York Street	Unit 21	115.00	$1,707,750	$14,850.36	N
14-Dec-21	650 George Street	Unit 61	80.00	$1,500,000	$18,750.46	Y
17-Dec-21	7-13 Hunter Street	Unit 16H	65.00	$5,000,000	$76,924.95	Y

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