Australian Office – November 2024

SPOTLIGHT
Savills Research

Office Briefing

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Interest rate cuts globally • Investor confidence rebounding • Pricing nearing cyclical bottom

Interest rate cuts globally

Major central banks begin easing policy rates, but sticky inflation keeps RBA on hold for now

Policy easing gains momentum
Major central banks have moved decisively to ease monetary policy in response to moderating inflation. The US Federal Reserve, ECB, Swiss National Bank, and Reserve Bank of New Zealand have all cut interest rates by a cumulative 75bps this year, while the Bank of Canada has lowered its policy rate by 125bps.

RBA on hold for now
The RBA has ruled out cutting the cash rate in 2024 pointing to upside risks to inflation stemming from stronger than expected labour market conditions and government spending, as well as a forecast rebound in consumer spending as wage growth outpaces inflation and recently introduced tax cuts increase household disposable income.

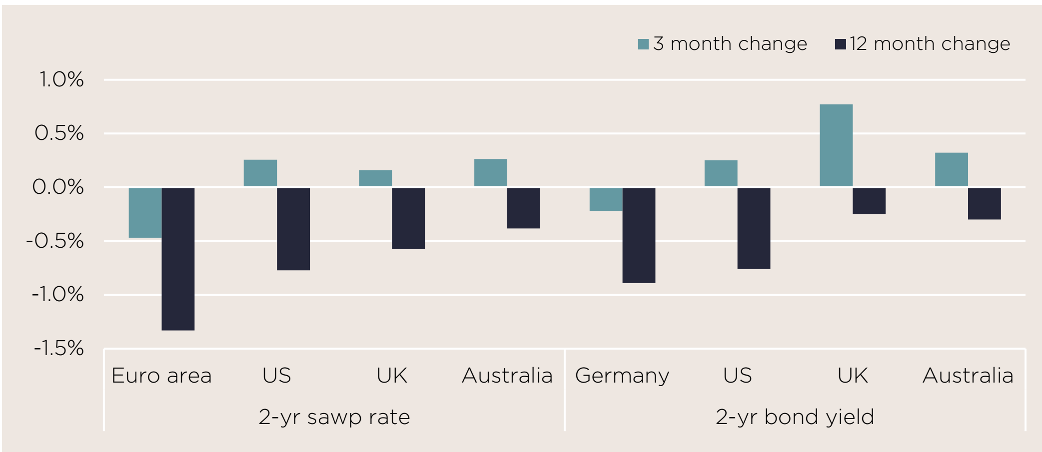
But inflation outlook is improving...for now
Inflation moderated further in the September quarter, with energy rebates driving headline inflation to 2.8% y/y, down from 3.8% in the June quarter, and to its lowest level in more than three years. Underlying inflation came in at 3.5%, down from 4.0% in the June quarter.

Bond yields move higher but are still lower over the year
Bond yields have generally moved higher in recent months as financial markets scale back the magnitude of the rate cutting cycle amid expectations of stronger growth and higher inflation following the US presidential election.

However, shorter-dated bond yields and swap rates in major advanced economies remain well below the levels prevailing a year ago. The Australian 2-year bond yield has declined by c.30bps from a year ago, and the 2-year swap rate is c.40bps lower. Meanwhile, in the US, the 2-year bond yield and 2-year swap rate are both c.75bps lower over the same period.

RBA rate cut expectations pushed back to Q2 2025
Financial markets are pricing in 50bps of cuts from the RBA in 2025, with the first 25bps expected mid-year rather than in Q1. Among market economists, the median expectation is for 75bps of cuts by the end of 2025.

Bond yields still lower over the year despite recent move higher
Change in 2-year swap rate and 2-year bond yield, per cent



Source Savills Research / Macrobond (pricing as at 8 November 2024)

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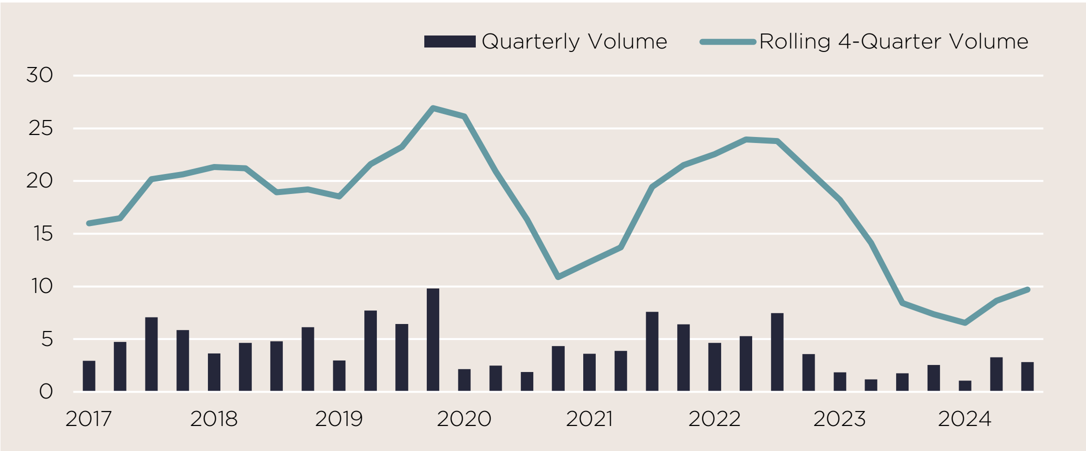
Investor sentiment rebounding

Q3 activity moderates after EOFY driven pick-up in Q2 but pipeline of deals points to growing investor confidence

Office investment volumes down c.13% in Q3 vs Q2
Quarterly and rolling 4-quarter investment volumes (deals $10m+), $bn



Source Savills Research / MSCI Real Assets

Liquidity improving but deal volume remains well below average

Deal pipeline points to activity gaining momentum

Deal activity stronger than 2023 lows but still well below average levels
According to MSCI Real Assets, total investment volume (for completed deals $10m+) reached c.$2.83 billion in Q3 2024, down 13% on Q2 when a string of major deals exchanged just before the end of the financial year.

Investment activity is now materially above 2023 lows, with transaction volume 61% higher than Q3 2023. However, deal volume remains subdued by historical standards, with activity in Q3 2024 41% below the 10-year Q3 average.

Sydney driving investment activity
Sydney remains a focal point for capital, with the city accounting for 63% of office acquisitions over the year to date, up from a 10-year average of 49%. Investors remain more cautious on Melbourne reflecting recent tax changes and lagging office occupancy.

Investment activity in Sydney has been driven by several major deals in Q2 (including 55 Pitt Street, 255 George Street, 5 Martin Place), as well as acquisitions in Q3 such as Deka's purchase of 333 George Street for $392 million, and Han Group's sale of 338 Pitt Street site and surrounding properties for c.$510 million.

Deal pipeline points to ongoing rebound in activity and confidence
Sydney also has a substantial deal pipeline, with several major transactions in train according to media reports.

Brookfield is set to sell its half stake in 388 George Street to United Overseas Land for $460 million. Meanwhile, Proprium Capital Partners is reportedly undertaking due diligence on 20 Bridge Street for c.$270 million, while BGO is interested in acquiring 10-20 Bond Street from Mirvac and Morgan Stanley according media reports.

c.AU$2.83 billion
transacted in Q3 2024

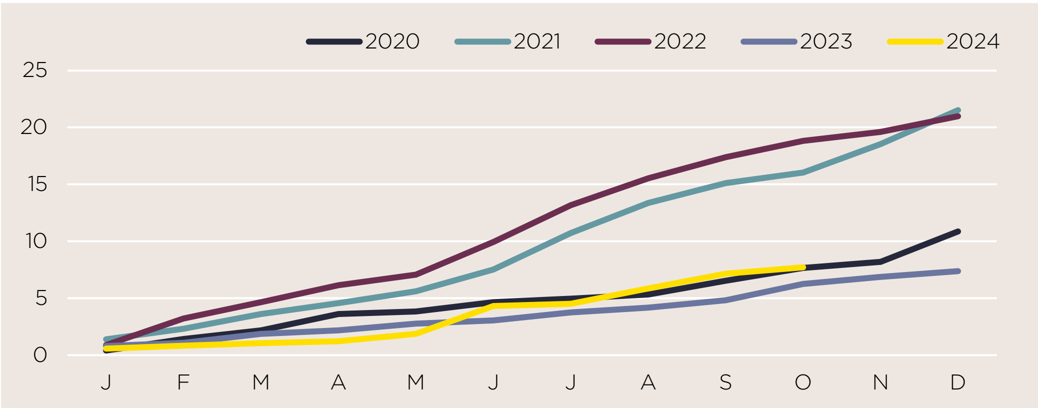
15%
Increase in 12-month rolling volume, year to Q3 2024

45%
Cross-border capital's share of total investment volume in 2024 YTD

-18.9%
Net capital growth, office specialist funds, year to Q3 2024

Deal activity gradually picking up after slow start to 2024

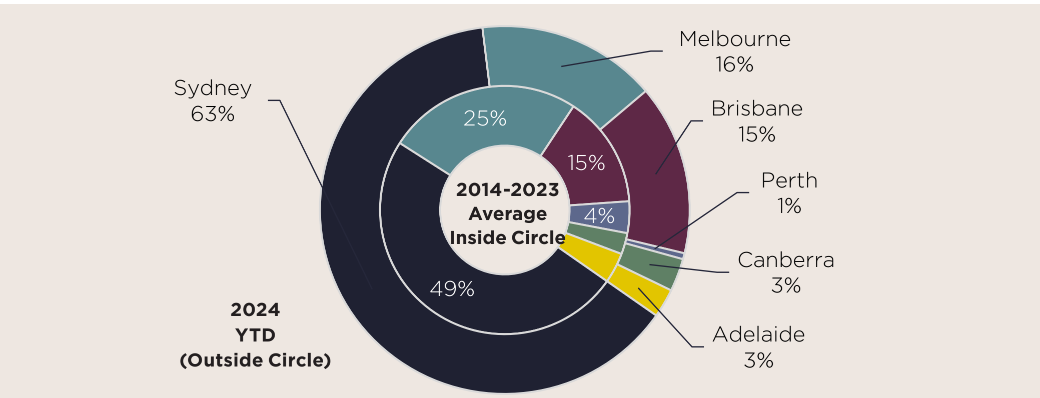
Monthly cumulative deal volume (deals $10m+), $bn



Source Savills Research / MSCI Real Assets

Sydney driving investment activity

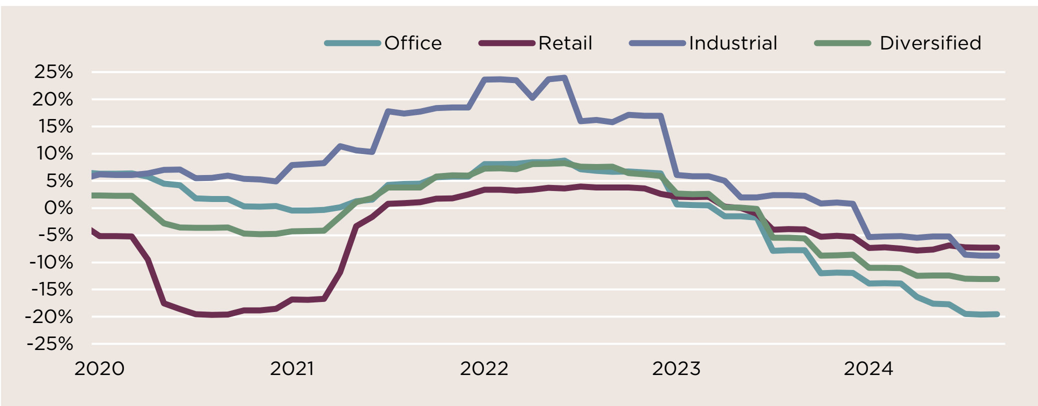
Share of office acquisitions by city, per cent



Source Savills Research / MSCI Real Assets
Inner-circle : 2014-2023 Average , Outer-circle: 2024 YTD

Close to a cyclical bottom?

Annual capital growth for selected Australian wholesale property funds, per cent



Source Savills Research / MSCI Real Assets
As at Sept-24

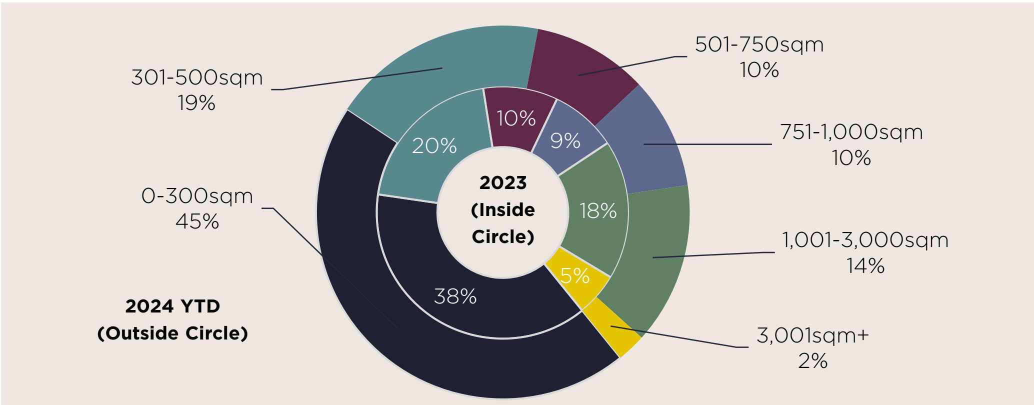
HIGHLIGHTS

Deal activity gradually picking up
Confidence is slowly returning to investment markets. After a slow start in this year, office investment volume reached $7.15 billion nationally over the nine months to September, outpacing the $4.82 billion during the same period last year, and roughly on par with 2020 levels. However, deal activity remains well below the high levels seen in 2021 and 2022.

Offshore investors returning
Cross-border investors are continuing to be more active in 2024, with net acquisitions of office property (for completed deals $10m+) nationally totalling around $1.4 billion YTD according to MSCI, up from -$50 million in 2023. Asset repricing is providing relative value investment opportunities, with investors from Asia and Europe deploying capital over the year to date.

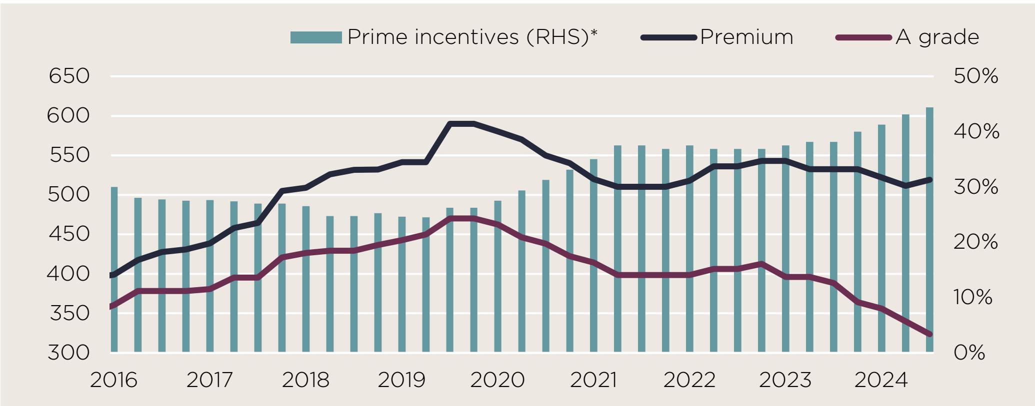
Asset performance stabilising
Property fund performance is showing signs of stabilisation. According to the MSCI/Mercer Australia Core Wholesale Monthly Property Fund Index, net capital growth for all funds declined by 13.0% over the year to September 2024, slightly higher than the -13.8% over the year to June. Office-specialist funds recorded -18.9% growth over the same period, up from -19.5% in the year to June.

Higher share of 0-300sqm tenant requirements in Sydney
Active tenant briefs by size of requirement, %



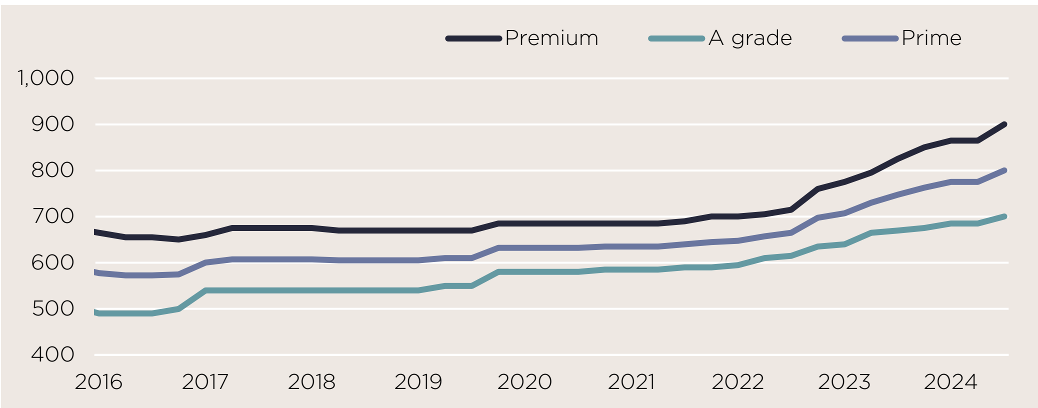
Source Savills Research

Widening gap between premium and A grade rents in Melbourne
Premium and A grade net effective rents ($/sqm), prime incentives* (%, RHS)



Source Savills Research
* Average net incentive
As at Sept-24

Premium grade leads Brisbane rental growth
Prime net face rents by grade, $/sqm



Source Savills Research
As at Sept-24

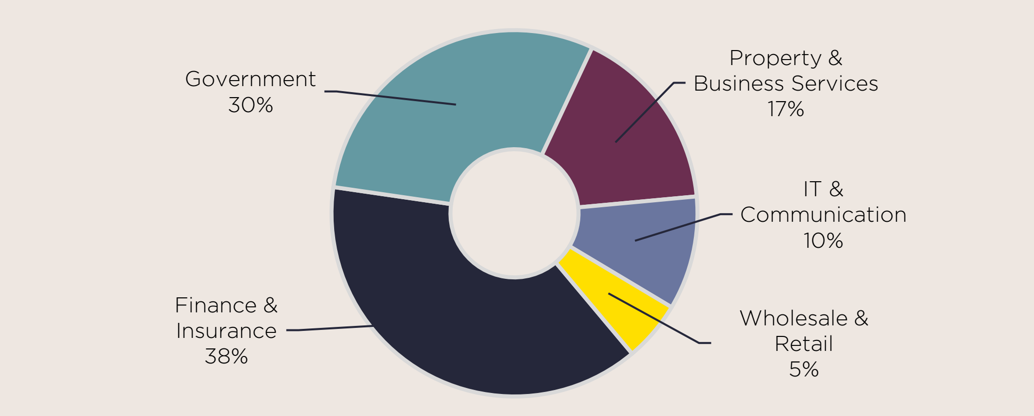
EAST COAST HIGHLIGHTS

Smaller size requirements increasingly driving tenant enquiry in Sydney
The number of active tenant briefs over the nine months to September 2024 is down slightly compared to the same period last year. However, the average size of tenant requirements YTD is significantly lower than 2023 levels. 0-300sqm size requirements have accounted for 45% of tenant briefs in 2024 to date compared with 38% in 2023.

Growing divergence between premium and A grade rents in Melbourne
Melbourne continues to see pronounced bifurcation in demand for space. Reflecting relatively solid demand in the premium market, premium CBD net face rents rose by 1.8% in Q3, the first increase in 18 months, while net effective rents returned to growth. By contrast, A grade face rents were flat, while higher average incentives in the A grade segment continue to drive effective rents lower.

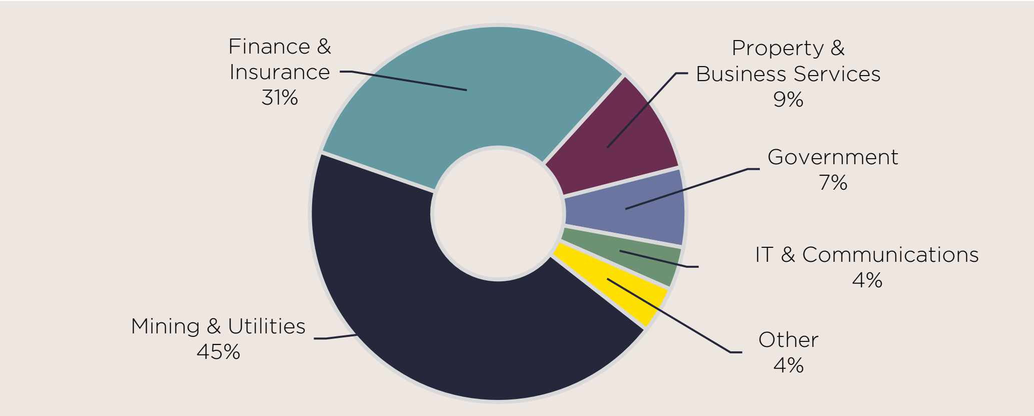
Brisbane rents power ahead
Brisbane continues see relatively strong rental growth compared to the other major CBD office markets. Prime average net face rents rose by 3.2% in Q3 to be 7.0% higher over year, led by the premium segment which recorded a 4.0% increase (+9.1%y/y). Lower average incentives at the premium end of the market also contributed to growth in effective rents.

Westpac deal boosts leasing activity in Adelaide
Adelaide CBD leasing volumes (1,000sqm+) by industry (%), year to Q3 2024



Source Savills Research

Mining and financial services tenants driving leasing activity in Perth
Perth CBD leasing volumes (1,000sqm+) by industry (%), year to Q3 2024



Source Savills Research

ADELAIDE AND PERTH HIGHLIGHTS

Westpac takes space at One Festival Plaza
Leasing activity in Adelaide has been boosted by Westpac signing a 9,000sqm tenancy deal across five floors at One Festival Plaza, one of the largest leasing deals in the city over the past decade. Financial services and government tenants accounted for a combined 68% of leasing activity over the year to Q3 2024.

Leasing activity picks up in Perth
Significant leasing deals in Q3 include AJ Gallagher and Suncorp, both taking space at 250 St Georges Terrace (QV1) (1,582sqm and 1,387sqm respectively), while McDermott Australia renewed 2,456sqm of space at 15-17 William Street. Mining and financial services have been the key industries driving leasing activity in Perth over the past 12 months, accounting for 45% and 31% of leasing volume respectively in the CBD over the year to Q3 2024.

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