RWC

WESTERN SYDNEY INSIGHTS

Parramatta CBD Office Forecast

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Executive Summary

The office market nationwide faces ongoing challenges due to low uptake, leading to increased vacancies and downward pressure on rents and asset values in CBDs and non-CBDs alike.

Supply and withdrawals remain a key indicator which has been influencing vacancies in both a positive and negative way however the underlying lack of leasing demand has shown little improvement.

The rise of remote and hybrid work arrangements has contributed significantly to declining occupied stock, as businesses reassess their accommodation needs amid rising operational costs. Many are downsizing or relocating to save on expenses, leading to a decline in net absorption levels across most office markets, however **Parramatta may be a shining light.**

For Parramatta, this acceptance of hybrid working has had an impact on the vibrancy of the CBD affecting the attraction of new businesses as well as existing tenants. High quality office accommodation, break out areas, end of trip facilities, on site cafes and fun activities have all tried to grow this vibrancy however it is a slow grind to improvement. Encouragingly, Parramatta was the eighth highest market regarding net absorption (across all 23 major Australian office markets), this result was of stability, while other cities saw another period of major losses in tenancies. This coupled with withdrawal of stock saw total vacancy levels decline to 22.0%, **an outstanding result particularly compared to other NSW markets.**

Population gains and infrastructure improvements in and around the city centre of Parramatta signal this market is likely to grow ahead of other major office markets. Affordability is high compared to Sydney CBD and North Shore markets for assets which can compete on quality, grandeur as well as ESG standards suitable from the small to large corporate needs with incentives rivalling those of CBD markets across Australia.

This uncertainty in occupancy has led to limited sales activity, some vendors are reluctant to list, while those on the market are having to meet the reduced capital values and increased yields in which purchasers are prepared to pay. Activity across the smaller end of both strata and freehold secondary assets have continued and some with outstanding results as opportunistic buyers look for possible uplift and redevelopment or repositioning potential of an asset.

If you'd like to discuss this report in more detail or to learn more about the Parramatta CBD Office market, we would be delighted to engage in a conversation with you.

PETER VINES
Managing Director,
RWC Western Sydney
0449 857 100

TOTAL OFFICE STOCK:	**963,386 SQM**
NEW SUPPLY:	**0 SQM**
WITHDRAWALS:	**17,449 SQM**

VACANCY BY QUALITY GRADE

A GRADE:	18.4% ↓
B GRADE:	40.0% ↓
C GRADE:	19.8% ↔
D GRADE:	7.0% ↓

NET FACE RENTS

PRIME	↘ **$590/SQM**
SECONDARY	↘ **$465/SQM**

INVESTMENT YIELDS

PRIME	↑ **6.00%**
SECONDARY	↑ **7.00%**

TOTAL VACANCY: 22.0% ↓

6-MONTH NET ABSORPTION	**-75 SQM**
12-MONTH NET ABSORPTION	**-35,098 SQM**

FORECAST NET SUPPLY

2024	**20,266 SQM**
2025	**1,000 SQM**

Refurbished projects have been deferred with building owners considering all options for their existing buildings.

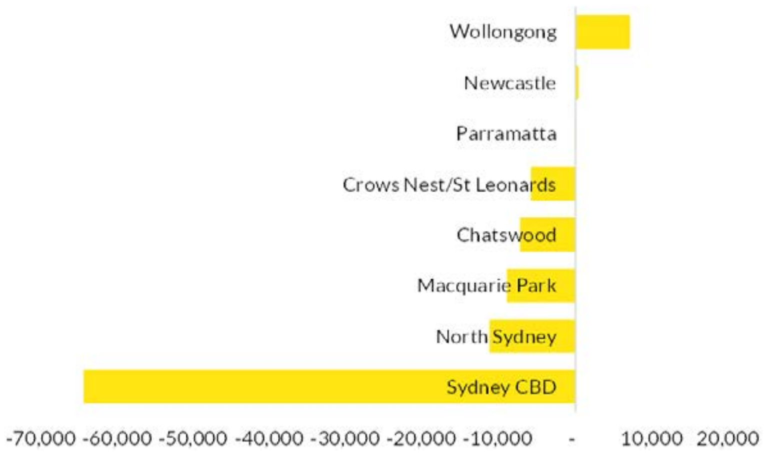
SOURCE: PROPERTY COUNCIL OF AUSTRALIA, RWCWS

Sub-lease space has increased slightly to **1.0%** as hybrid working conditions overtake the return-to-work push.

With over **100,000sqm** in vacancy of prime stock, incentives have exceeded **45%**. While across secondary markets, vacancy levels are similar, yet the fragmented private ownership has seen lessors sit firm at lower incentive rates.

NSW Office Market *Absorption*

6MONTHLY (SQM), SIX MONTHS TO JAN 2024



SOURCE: PROPERTY COUNCIL OF AUSTRALIA, RWCWS

The movement toward hybrid working styles, coupled with staff reluctance to return to the office, is pressuring employers to reconsider their accommodation needs during this time of higher finance costs.

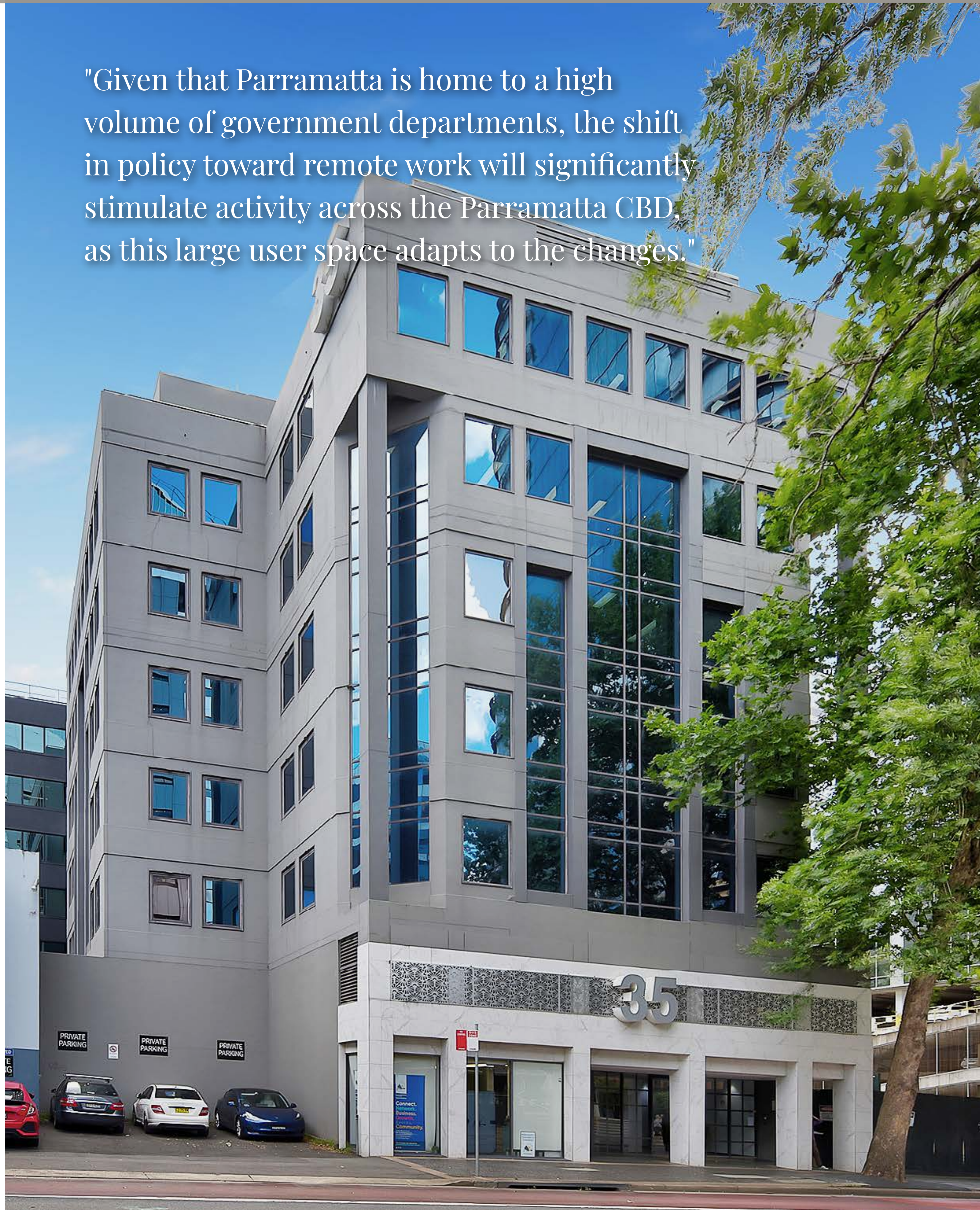
Queensland however has been the market leader in terms of improvement in occupied stock levels with the market benefitting fr om a growing population base, economic performance as well staff expectation surrounding working from home given the limited lockdowns Queenslanders endured during the pandemic. Looking to NSW, regional markets of Wollongong and Newcastle have been the only market to record a positive change in occupied stock, buoyed by population and business movements to the regions again borne out of COVID-19.

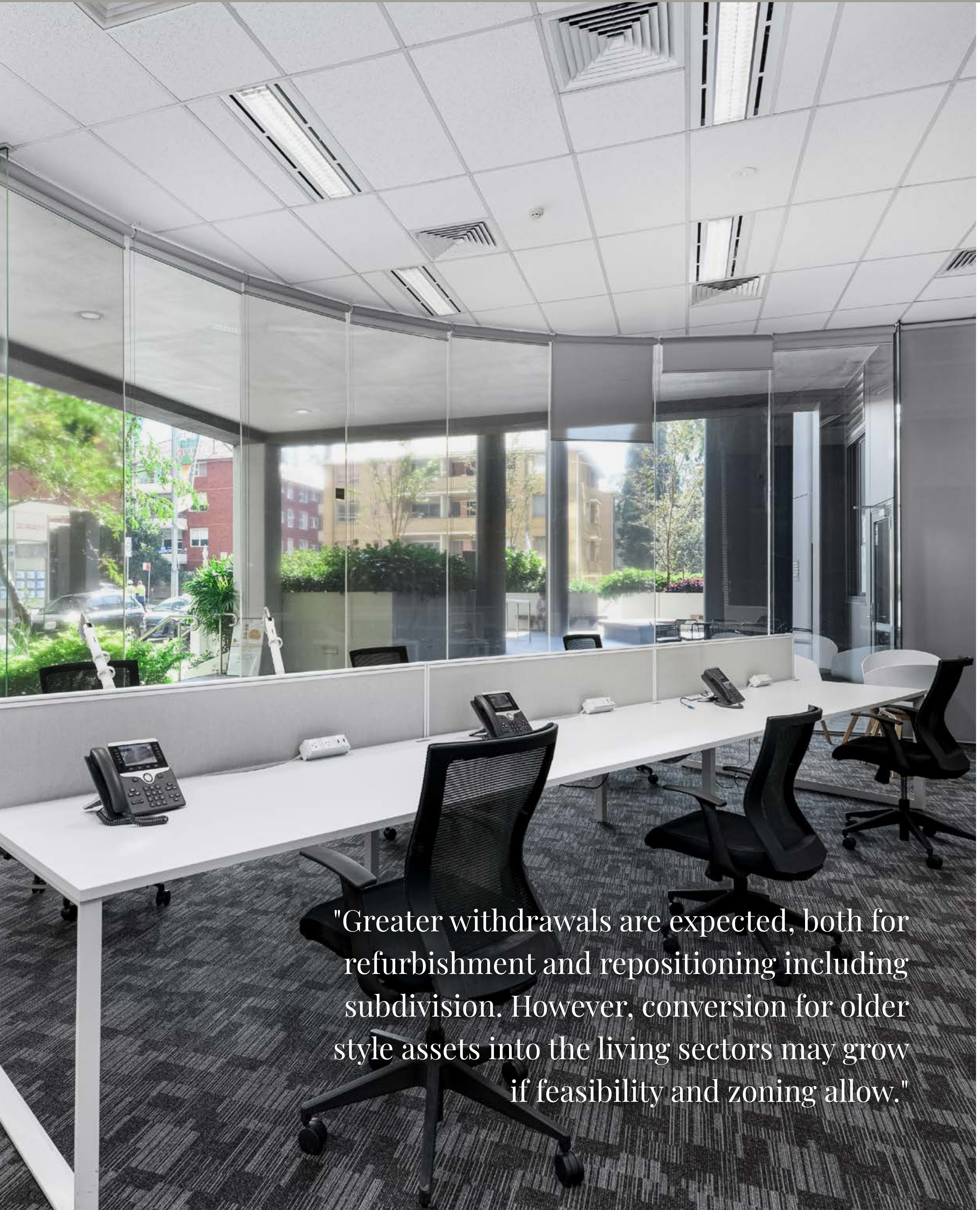
On the opposite spectrum, Sydney CBD continues to show leakages year on year, with businesses contracting or leaving the city, similarly the North Shore markets have been under the same pressures despite all markets being home to high quality, newly completed office accommodation options.

Considering these indicators, Parramatta is well poised to benefit from these losses.

The gateway to Western Sydney, this region is home to high population growth, improved accessibility via road and public transport enhancements as well as growing business innovation, couple this with high quality office assets available however with affordability in mind compared to other NSW markets.

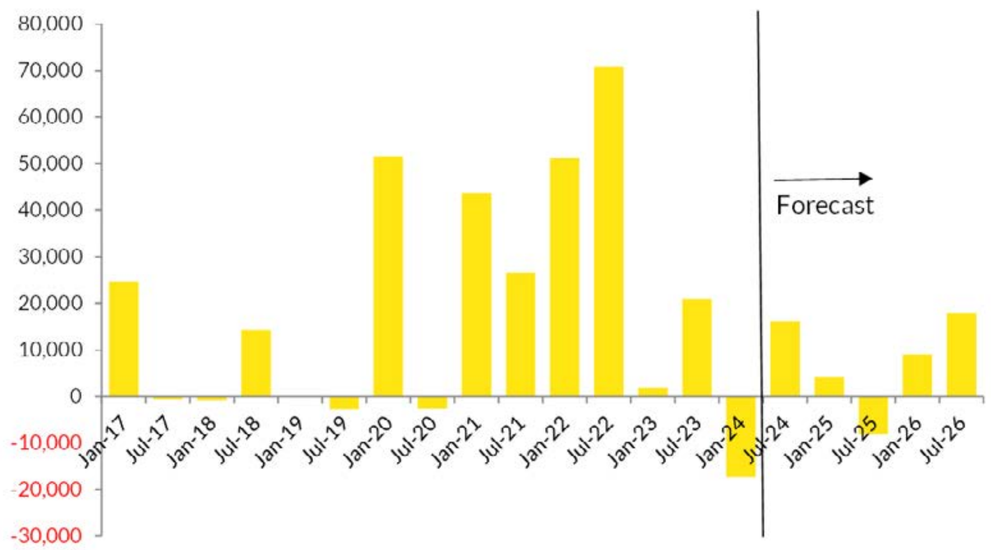
"Given that Parramatta is home to a high volume of government departments, the shift in policy toward remote work will significantly stimulate activity across the Parramatta CBD, as this large user space adapts to the changes."





Office Net *Supply*

NET SUPPLY (SQM)



SOURCE: PROPERTY COUNCIL OF AUSTRALIA, RWCWS

Net supply levels across the Parramatta CBD experienced a surprising decline in the latest Australian Property Council office market report figures, with withdrawals totaling close to 17,500 square meters.

While 85 Macquarie Street was anticipated to contribute to stock levels during this period, its completion has been postponed to late 2024. Despite the withdrawal of 10 Valentine Street in late 2023, a swift refurbishment is anticipated with stock levels returning during the first half of 2024, bringing total new supply for the 2024 calendar year up to 30,000sqm however withdrawals will start to emerge and bring net levels down.

MEDIUM-TERM OUTLOOK

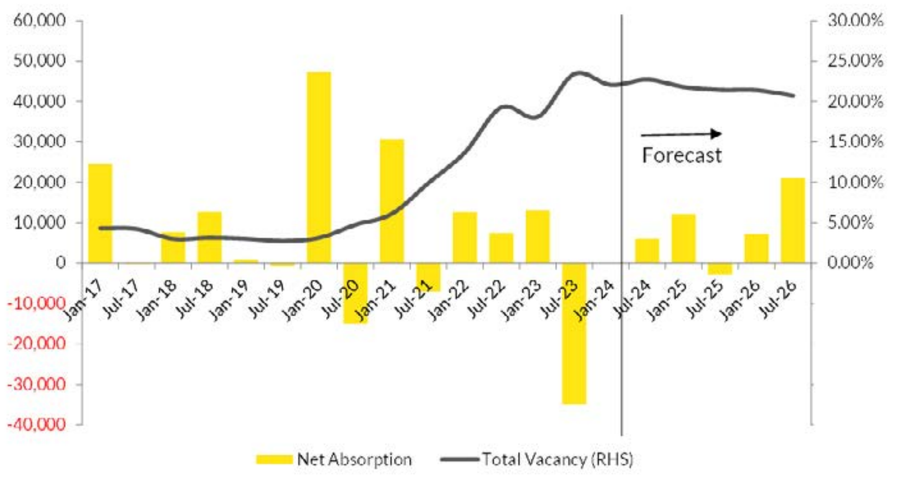
Over the medium term, refurbishments or redevelopments are anticipated to characterise the Parramatta office market. Assets like the Lang Centre, Octagon, 81 George Street, 27 Argyle Street, and Jessie Street Centre are all positioned for repositioning, potentially involving strata subdivision as tenant vacancies arise.

TRENDS IN PERMANENT WITHDRAWALS

Permanent withdrawals, particularly for older, smaller-style secondary assets, are anticipated to increase. These properties may offer greater ease of conversion into residential or hotel sectors due to features like higher ceiling heights and ample natural light. Despite the higher construction costs compared to newer office assets, these characteristics make their transformation more feasible.

Demand and *Trends*

NET ABSORPTION (SQM) & TOTAL VACANCY (%)



SOURCE: PROPERTY COUNCIL OF AUSTRALIA, RWCWS

Demand for office space is low across the country.

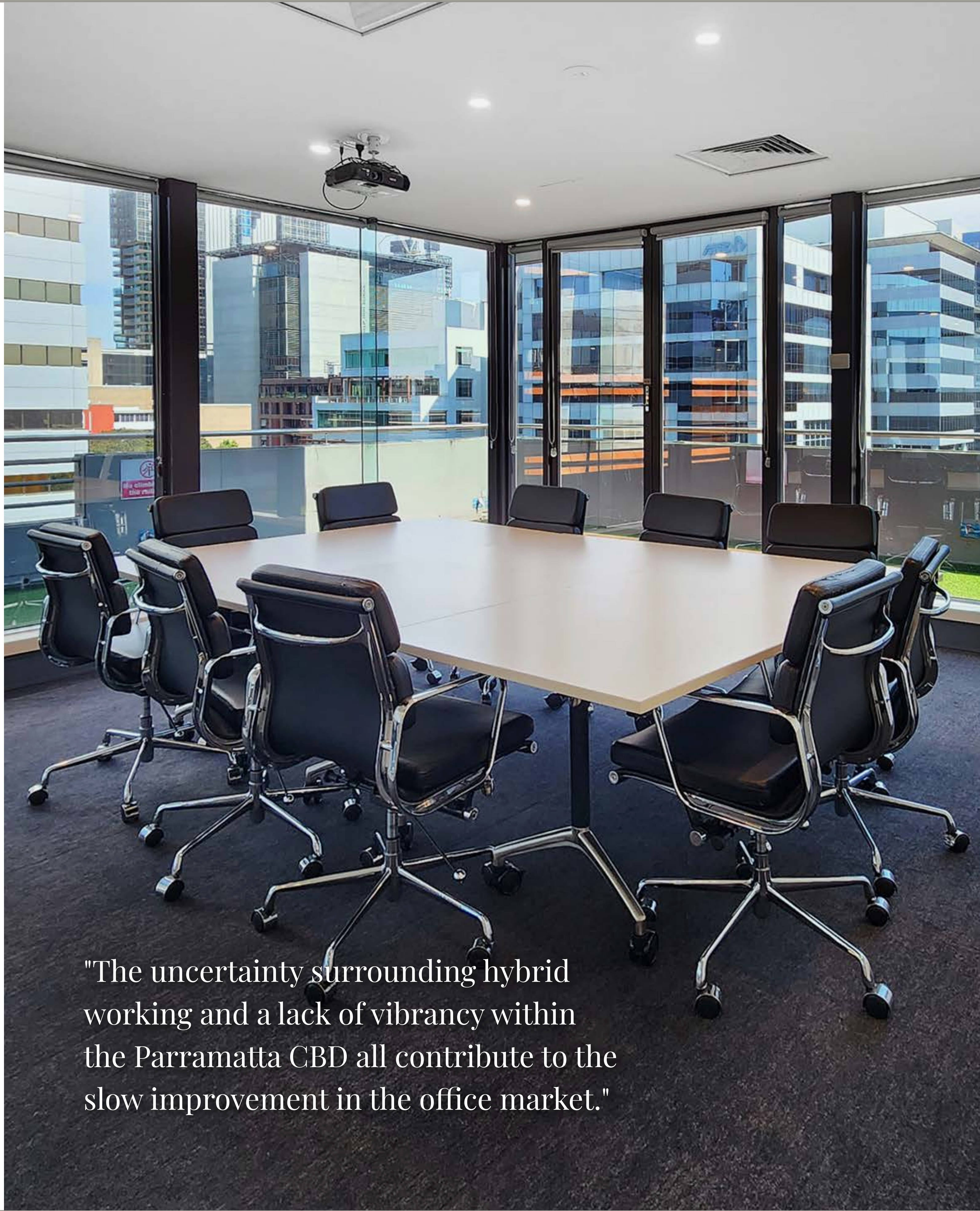
Results from the Australian Property Council's office market report have shown that major CBD markets have lost over 200,000 square meters of tenants in the past six months. In contrast, non-CBD markets present much more optimistic results, with positive take-up recorded. For Parramatta, the change in occupied stock remained stable at -75 square meters. This, coupled with the withdrawal of stock, led to a decline in total vacancy levels to 22.0% from the peak vacancy of 23.4% in the last period (July 2023).

PARRAMATTA'S DEMAND AND SUPPLY

- New supply additions in Parramatta CBD need to be demand-led to stabilise vacancy.
- Parramatta demonstrates the highest demand among non-CBD markets in Sydney.
- North Shore markets, including Macquarie Park, collectively lose over 84,000sqm of tenancies in the second half of 2023.
- Due to the supply pipeline, recovery in vacancies will be prolonged over the medium term, rates are expected to increase to 22.7% next period given the re-addition of space without full commitment before moving down to average 21.4% the following year.

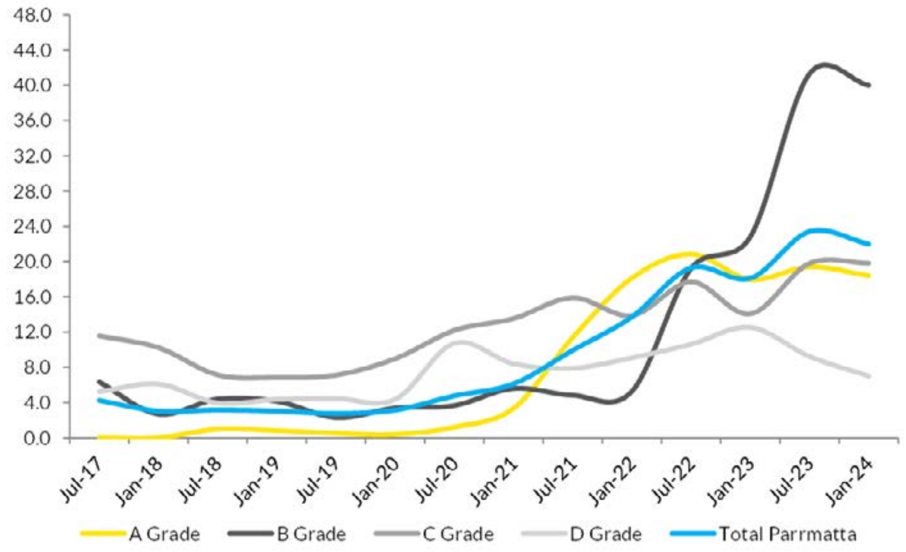
CONTRIBUTING FACTORS TO MARKET SLOWDOWN

The uncertainty surrounding hybrid working and a lack of vibrancy within the Parramatta CBD all contribute to the slow improvement in the office market. The growth in financing costs too has put pressure on businesses to cut costs, which has resulted in an increase in sublease vacancies to 1.0% this period. While unemployment levels remain low and employers support their staff working from home, a strong improvement in occupancy is unlikely to occur.



Office Vacancy *Levels*

BY QUALITY GRADE (%)



SOURCE: PROPERTY COUNCIL OF AUSTRALIA.

The Parramatta office market has enjoyed a recent history of high-quality office assets being added to the skyline, representing some of the best office assets in the country.

A grade space quickly swelled from just 263,000sqm in early 2019 to 571,372sqm today, swiftly changing vacancy from 0.5% to 18.4%. While the impacts of the pandemic were felt during this period, a recovery in occupancy has yet to occur, keeping many of these assets sitting vacant. The flight to quality has certainly improved the prime sector over the last few years, with tenants taking the high incentives and flexible lease terms on offer resulting in B grade vacancies moving from 2.3% to 40.0% over the same period.

CURRENT VACANCY LEVELS

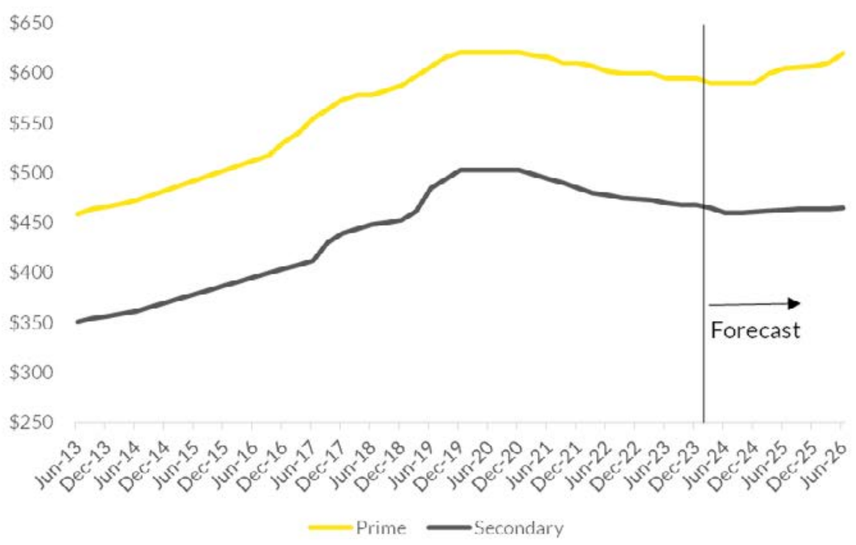
- Prime market vacancy stands at 104,856 sqm (18.4%).
- Secondary markets (B, C, D grade) have a similar level of vacancy at 107,560sqm (27.4%).
- Secondary assets may struggle to compete with A grade stock in the short to medium term.

STRATEGIES FOR FUTURE COMPETITIVENESS

The supply pipeline includes withdrawals and refurbishments to maintain competitiveness. Repositioning or conversion of low-grade stock to alternative uses should be considered to address limited demand for office space nationwide.

Office Rental *Insights*

NET FACE RENTS ($/SQM)



SOURCE: RWCWS

The office rental market across the country has been particularly challenging. The take-up of just -75sqm in Parramatta highlights the lack of activity across the marketplace.

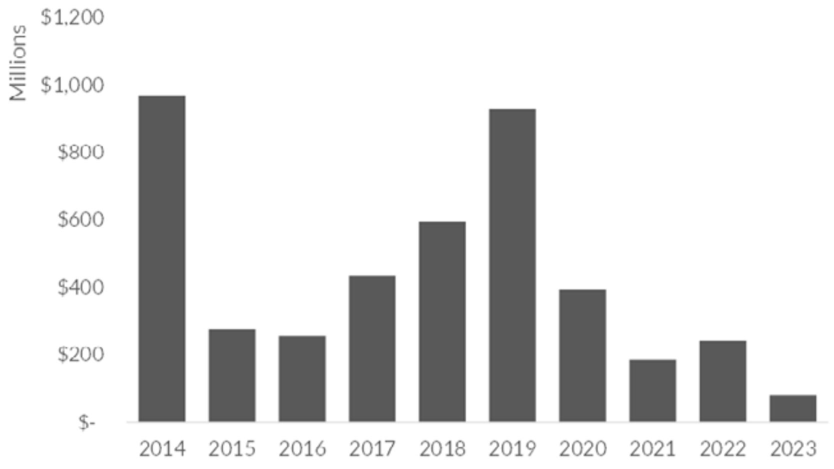
Despite limited overall volumes, tenants remain active in relocating within the Parramatta CBD. They seek to capitalise on the quality spaces available with attractive terms, including incentives, leading to a reduction in A grade vacancy. With many employers looking to encourage staff back into the office on a more permanent basis, they are seeking not only office space, but local amenity, funky foyers, attractive fit outs, and facilities to lure staff back in.

FACE RENT STABILITY AND INCENTIVES

- Net face rents across prime assets show little change.
- REIT and Fund owners maintain stable face rents but increase incentives up to 45%, pressuring effective rents downward.
- Secondary owners are a mix of both institutional and privates who prefer to keep incentives down, leading to some compression in face rents.
- Face rents range from $350 to $550/sqm, averaging $465/sqm, while prime rent averages $595/sqm, with rates up to $680/sqm available.

Parramatta CBD Office *Transactions*

VOLUME OF SALES



SOURCE: REAL CAPITAL ANALYTICS, RWCWS

The transaction market has been quiet across the country, with office sales falling year on year over the last three years in line with the increase in interest rates.

For Parramatta, few larger assets have to market, resulting in limited transaction volumes. Over the past few years, sales of smaller freehold secondary assets, together with strata units, have dominated the landscape, resulting in total sales for 2023 recorded at just $82.18 million, far from the highs of 2019 when close to $1 billion changed hands.

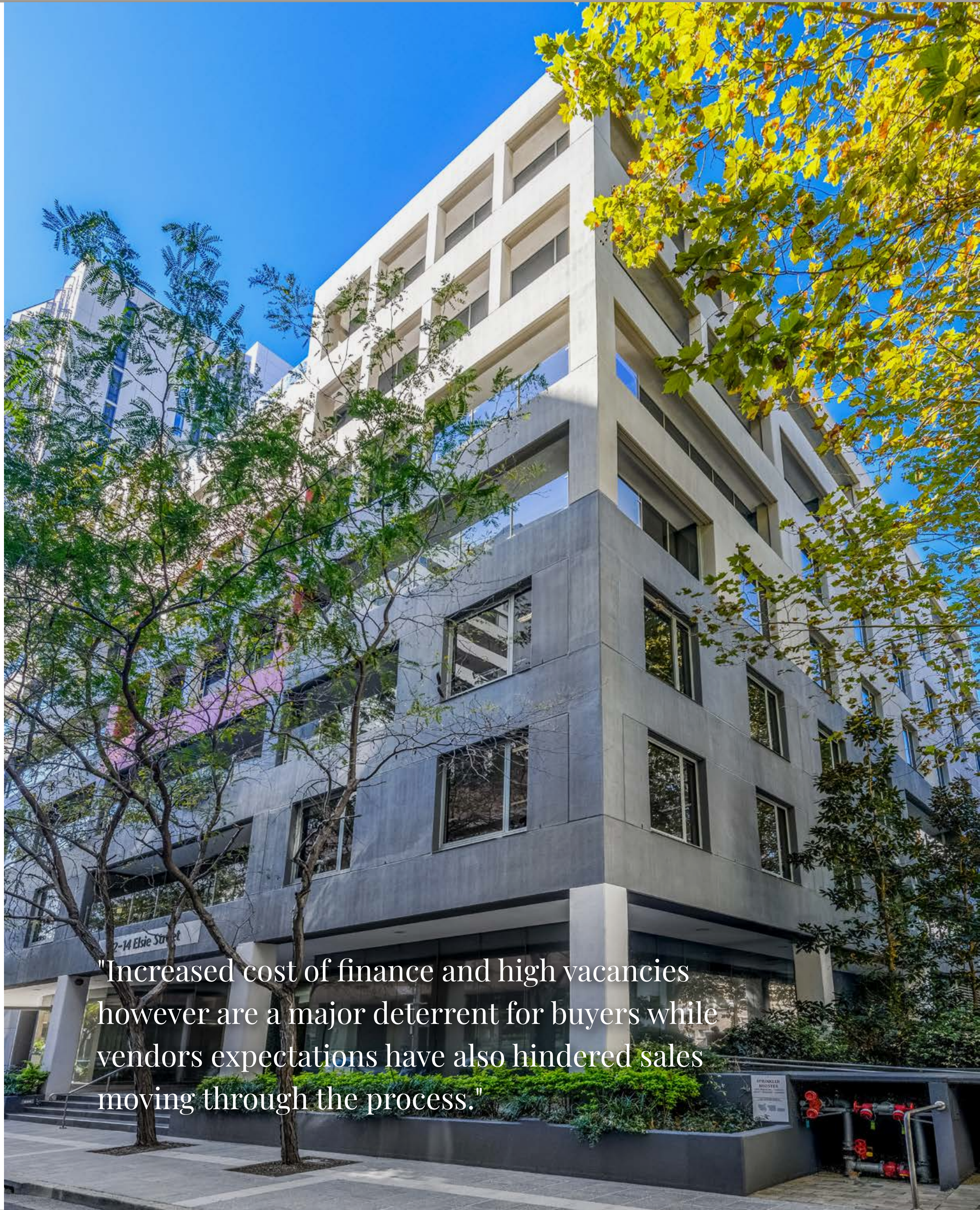
ENCOURAGING RESULTS FROM RECENT SALES

Some of these recent sales have yielded encouraging results with prospective buyers willing to speculate on the future of the asset class or reposition assets for future gains. Increased cost of finance and high vacancies however are a major stumbling block for buyers while vendors expectations have also hindered sales moving through the process.

DECLINE IN TOTAL RETURNS AND CAPITAL VALUES

- The latest MSCI/PCA Property Digest shows a decline in total returns for office assets, outpacing all other asset classes.
- December 2023 results for Parramatta CBD recorded office capital declines of 19.6%, while income returns remain positive.
- Uncertainty surrounding the asset class's future and the long road to recovery are expected to result in more assets coming to market, despite changes in capital values and achievable yields.

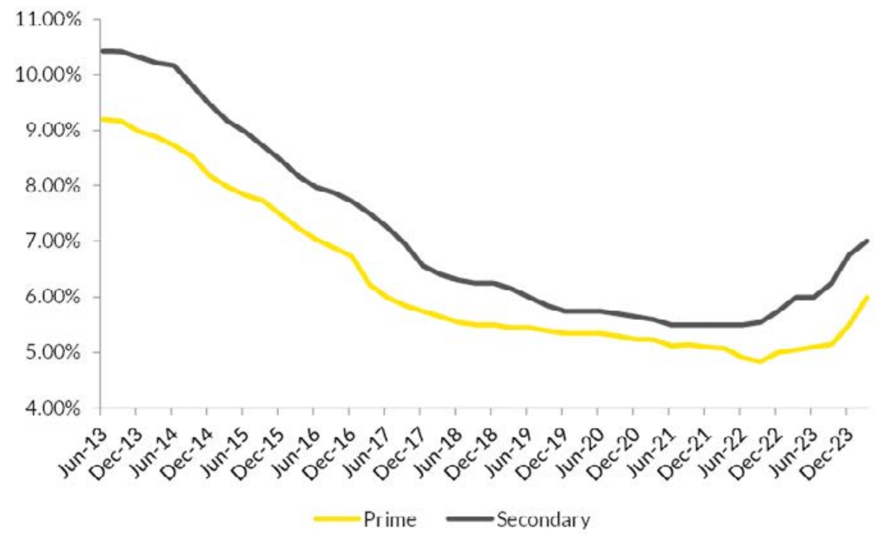
For many listed and institutional asset owners, the performance of their office assets may no longer align with fund objectives leading to more assets entering the marketplace.



" For the institutional-grade Parramatta office asset, a strong reduction in capital values has been felt, resulting in yield expectations shifting."

Parramatta CBD Office *Investment Yields*

BY QUALITY GRADE (%)



SOURCE: RWCWS

Sentiment surrounding interest rates have taken a turn this year after lower-than-expected inflation numbers were recorded in February, improving optimism surrounding a rate cut earlier than expected this year.

This will have a positive impact on confidence when looking to purchase, particularly for private investors examining smaller assets, including several strata units and freehold secondary properties currently on the market. However, for the institutional-grade Parramatta office asset, a reduction in capital values has been felt, resulting in yield expectations shifting.

YIELD TRENDS IN PRIME ASSETS

Data from MSCI shows prime yields in the vicinity of 6.0% at the conclusion of 2023 despite limited transactional evidence, with valuation rates highlighting this change in asset value.

PERFORMANCE OF SECONDARY ASSETS

For secondary assets there has been mixed results, with a number of smaller sales over the last 12 months recording yields below finance costs highlighting a long-term confidence in returns, value appreciation and redevelopment potential.

FACTORS INFLUENCING YIELDS LEVELS

The strong potential of Parramatta as the gateway to the west, high population and housing growth coupled with strong infrastructure spending improving accessibility not gone unnoticed by the private sector keeping yields possibly lower than anticipated.

Conclusion

The outlook for the Parramatta office market is optimistic, supported by the underlying growth in the greater Western Sydney region, indicating likely recovery ahead of other NSW regions.

Factors such as quality, affordability, and proximity are expected to drive increases in tenancy demand. Hybrid working and remote work dynamics will continue to evolve, with changes in unemployment likely to encourage staff back into office space on a more permanent basis. Government support to encourage employees back into the Parramatta CBD will enhance vibrancy.

Supply dynamics will shape the Parramatta office market in the medium to long term, with the withdrawal of stock and renovated re-entry influencing future vacancy rates. Repositioning smaller, older, secondary-grade stock into living accommodations may be viable, benefiting from greater ceiling height and light despite high construction costs. While uncertainty in demand persists, rents will remain stagnant, and the flight to quality will continue.

Parramatta's affordability and quality offerings will gradually reduce vacancy levels and increase effective rental rates. Corporate tenants' increasing focus on Environmental, Social, and Governance (ESG) requirements will make Parramatta's quality office options attractive for relocating businesses.

For the investment market, anticipated lowering of interest rates will do much to improve confidence. Despite limited sales turnover last year, investment yield levels have increased, institutional assets which no longer meet their funds objectives could start to come to market, setting a new benchmark for value and higher yield.

PETER VINES
Managing Director,
RWC Western Sydney
0449 857 100

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PETER VINES
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ANDREW SACCO
Sales Associate


VEE LI
Sales Associate


JAYKY WU
Commercial Property Analyst


CHANTEL BRILLANTES
Marketing & Design


MONH LY
Campaign Manager


SARA COPTIL
EA to Peter Vines

LEASING


ROBERT NAPOLI
Senior Leasing Executive


SAMUEL GONG
Sales & Leasing Executive


TERESA MULLINS
Leasing Executive

ASSET MANAGEMENT


JOYCE ELKOUBERCI
Director


JAMES CHEUNG
Asset Manager


CALLUM MCKAY
Asset Manager


SANDHYA SHARMA
Assistant


MONIQUE LEE
Assistant Asset Manager


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Accounts

OPERATIONS


RUBY ROZENTAL
Director of Strategy


SARAH RIZZOTTO
Settlement Officer


HANNAH CARNEY
Director of Operations


PAULINE WATERFORD
Finance Manager


CHRISTIAN BRILLANTES
Office Assistant

Who we are,
what we do,
why we do it

RWC WESTERN SYDNEY

Level 1, 15-17 Argyle Street
Parramatta NSW 2150

(02) 8074 4884

rwcws.com