WESTERN SYDNEY INSIGHTS

NSW Block of Units

ISSUE 1

RWC WESTERN SYDNEY

NSW BLOCK OF UNITS

Executive Summary

NSW is starting to see strong pushes in population now immigration has recommenced, and this has caused a strong disconnect between demand and supply for housing across the Sydney.

With limited new stock entering the market over the past three years and future pipeline slow due to planning and construction costs the shortfall continues to grow between people and housing. As a result, there has been strong gains in median rents across the city causing affordability issues as more tenants move further afield to secure accommodation. Vacancy is now at an all time low and with the development pipeline shallow these fundamentals are expected to remain in play for the medium term.

For the block of unit market, this signals strength for income return and savvy investors have been quick to identify the opportunity. Furthermore, upward pressure on construction costs are seeing developers look to control their capital expenditure by refurbishing existing assets compared with the current escalating costs associated with new builds. However, limited stock is available to the market as vendors too do not want to lose this secure and growing income stream. As a result we have seen volumes down and yields show little movement despite the increased cost in financing. Recent discussions around the median house and unit prices in Sydney again gaining momentum upwards further signaling the potential for this asset class in the medium to long term.

SALES TRANSACTIONS

1Q 2023	$19.76M
1Q 2022	$70.20M
1Q 2021	$82.91M

AVERAGE TRANSACTION SIZE 2023 $3.95M

GROSS YIELD RANGE 2023 3.58% - 6.90%

TOTAL VACANCY

SYDNEY TOTAL VACANCY	**1.4%**
OUTER RING VACANCY	**1.5%**

SOURCE: REINSW (FEBRUARY 2023)

INVESTMENT INTEREST RATES
5.37% - 5.67%

SOURCE: RBA (FEBRUARY 2022)

% GROWTH IN AVERAGE OUTER RING UNIT RENTS

1 BEDROOM	**10.00%**
2 BEDROOMS	**11.11%**

SOURCE: FACS INSIGHTS (DECEMBER 2022)

% GROWTH IN AVERAGE MIDDLE RING UNIT RENTS

1 BEDROOM	**21.43%**
2 BEDROOMS	**24.44%**

SOURCE: FACS INSIGHTS (DECEMBER 2022)

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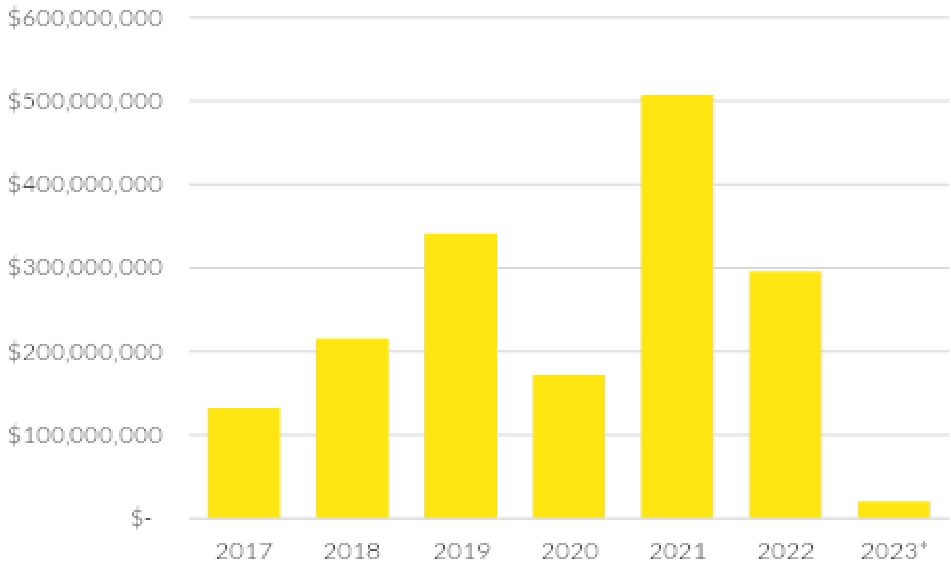
NSW Block of Unit Transactions

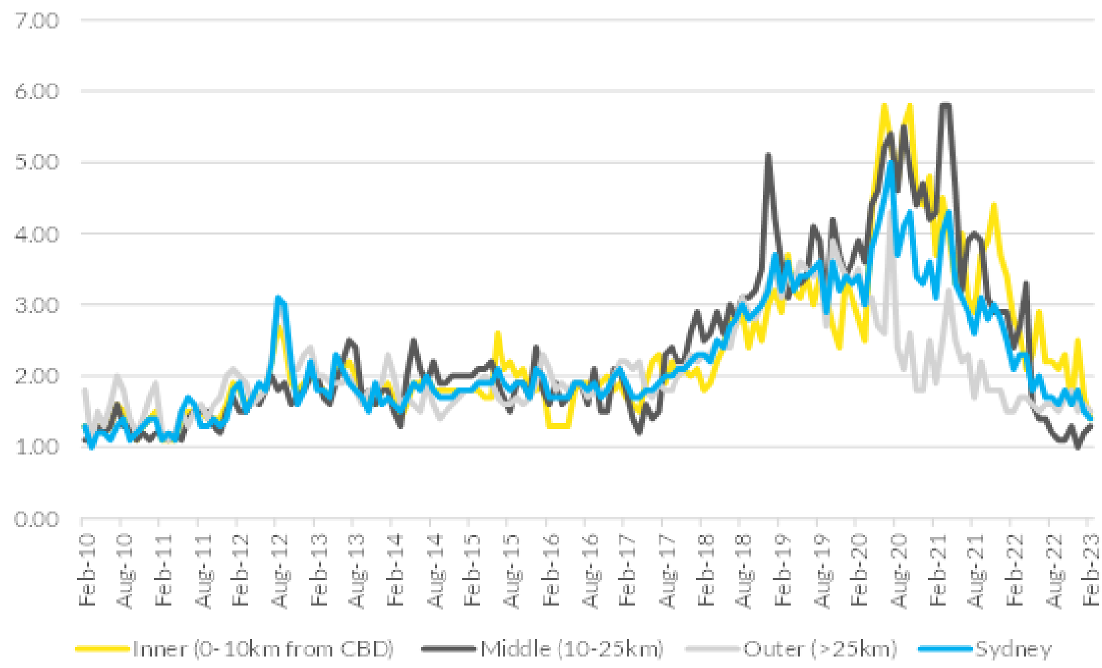


SOURCE: RWCWS *1Q

“A decline in sales activity from mid-2022 has been a reflection of limited stock coming to market as long-term investors continue to actively seek out these investments.”

The block of unit market has had a steady level of transaction historically, however, focus on it as a viable asset class had increased where volumes peaked in 2019 at $341.4million. Private investors looked to capitalize on stable returns as well as future median house and unit appreciation given the low interest rate environment while cash rich investors look to seek greater returning option as alternative to bank deposit. When COVID-19 hit, we saw hesitation in the market across all asset classes despite the rapidly declining interest rates, concern surrounding employment and rental delinquencies kept demand for this asset class subdued. However, as we pushed through into 2021 we saw significant increases in residential values and certainty in the marketplace surrounding tenancies while record low borrowing resulted in a total of $507.50million change hands. New investors emerged into the asset class looking to diversify and take advantage of cheap finance, as a result there was an increase in investment into secondary assets notably in regional markets. This high competition started to subside as interest rates started their journey upwards in May 2022 impacting the broader residential market. This was instrumental in reducing activity however as a reflection of limited stock coming to market as long term investors continue to actively seek out these investments.

Sydney Residential Vacancy Rates

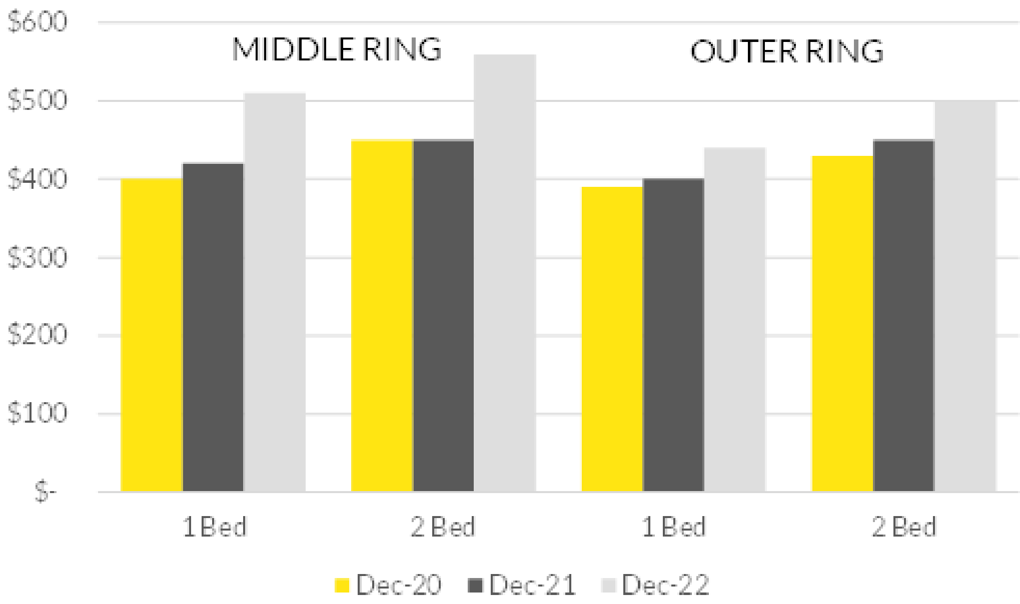


SOURCE: REINSW

Residential vacancies are at record low across the Greater Sydney area, a mismatch in supply and demand for stock causing strong declines in vacancies and significant upward movement in average rents. Limited new housing stock was added to the market throughout the COVID-19 period due to shutdowns, disruption to the supply chain, increases in raw materials and labour shortages which caused record increases to construction costs which continues to dampen building activity. Couple this with Australia's immigration tap being turned back on, has seen a quick increase in population during a time of limited residential supply. This has been highlighted by the current low residential vacancy rate averaging 1.4% across Sydney; the outer ring is anticipated to be the recipient of the greatest population gains has yielded a prolonged low averaging just 1.6% over the last year below the 1.8% annual Sydney average. Currently the middle ring vacancy has also seen compression as rising rents have seen tenants have to reconsider their relocation based on affordability moving to the middle and outer rings of Sydney. This trend is unlikely to dissipate as population is expected to continue to increase and construction starts remain low, making block of unit investments lucrative given their strong, growing returns anticipated.

> "Record low vacancies, particularly in the middle and outer rings will see block of unit investments continue to be a lucrative investment given their anticipated growing returns."

Greater Sydney Median Weekly Unit Rents

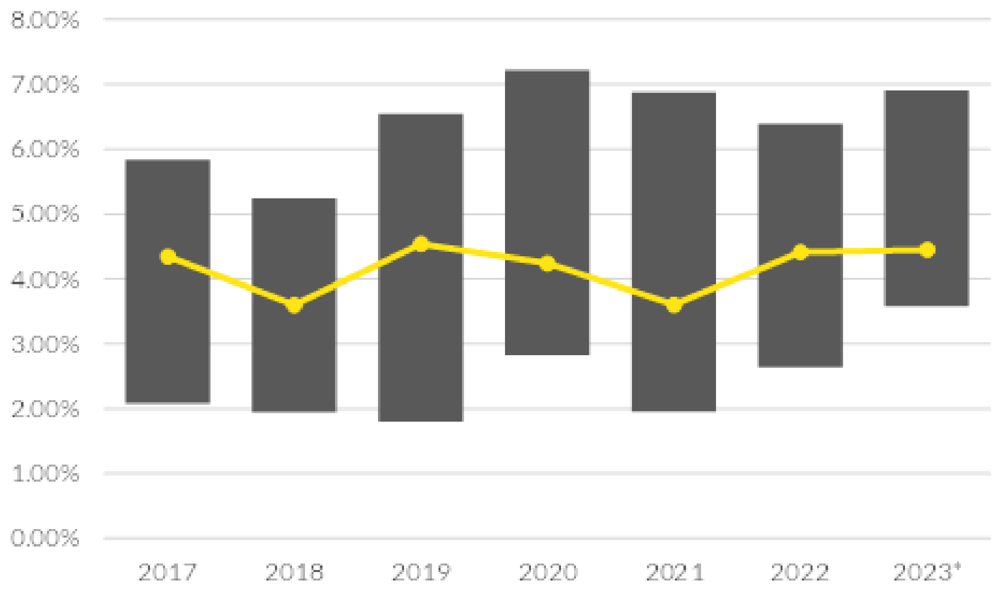


SOURCE: FAQS INSIGHTS

“Record low vacancies, particularly in the middle and outer rings will see block of unit investments continue to be a lucrative investment given their anticipated growing returns.”

Median rents have seen outstanding increases over the last year. During 2020 and 2021 we saw limited change in rents however during the 2022 calendar year trends have started to emerge across the various Sydney rings. Across the unit market we have witnessed significant changes to 1 bed and 2 bed assets growing over the 2022 year by 21.4% and 24.4% respectively in the middle ring, these results indicative of increased demand and tenants’ acceptance of moving further from the CBD in the quest to obtain affordable accommodation. Limited new starts and continued population growth is expected to maintain the pressure on the residential rental market which will keep vacancies low and rental growth projections high. Currently in the outer west, units have seen rental growth of 10.0% and 11.1% for 1 bedroom and 2 bedroom assets respectively, growing the divide between middle and outer ring rents. Despite these increases, the affordability for tenants in these outer markets coupled with the low vacancy and limited new stock additions will see continued rental appreciation. Its this continued growth in returns which makes the block of unit market attractive to savvy investors willing to purchase at low yield given the anticipated future rental increases.

Gross Yield Range



SOURCE: RWCWS *1Q

Investment yields have always maintained a low rate for block of unit assets as they are more aligned to residential returns. Private investors are the major purchasers of these assets who often already have a portfolio of residential assets and understand their potential as well as their stable, regular income returns. Developers are also key buyers for these assets looking to either redevelop, strata subdivide and on sell. During 2019 we saw strong investment into these assets, with a notable increase in cash buyers looking to earn increased returns, also activity in regional assets also grew and as a result average yields ranged substantially with an average at 4.54%. Despite limited activity in 2020, low interest rates and buyers willing to move up the risk curve saw this regional trend continue, again broadening the range up towards 7.00%. As interest rates bottomed in 2021, a range of new buyers entered the marketplace causing average yields to move below 4.00% averaging 3.60%, this indicative of the FOMO and first-time buyers entering the market. As interest rates increase and residential values fall, we saw a number of these less sophisticated investors exit the market; similarly, a lack of stock has come to market. Those assets however which have transacted continue to achieve quality yields as many buyers have a longer-term view on these assets particularly for their ongoing rental returns during this time of low vacancy.

"While the yield range has widened this year, the average continues at just 4.45% despite growing finance costs. Investors taking a longer-term view on strong gains continuing across the residential market given record low vacancies."

Conclusion

The NSW Block of unit market is bucking trends in 2023.

While volumes are down, this is a result of limited stock available to the market, not demand requirements. Despite the increased cost to financing, there is still depth in the investment market by private investors looking to capitalize on the current shortage of residential rental assets and developers keen to refurbish and hold existing assets during this time of high construction costs. The residential market in Sydney has now turned despite the increased interest rates with median house and unit prices no longer in decline but again improving. This is a symptom of the strong employment fundamentals of the state and the increases to population competing to secure suitable accommodation. This has also seen rental rates increase and growth has been considerable, moving from the inner to middle rings of the city and expected to move further west as affordability becomes a greater issue for the rental market.

As such, demand to purchase these residential assets as an investment has not dissipated with yields continuing to achieve robust results with buyers anticipating both capital and income return increases over the coming years. The limited supply pipeline of new residential stock further exacerbating this mismatch in supply and demand with construction costs still high and planning remaining an issue across NSW.

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what we do,
why we do it

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