WESTERN SYDNEY INSIGHTS

NSW Childcare

ISSUE 3 RWC WESTERN SYDNEY SEP 2024

Contents

NSW Childcare

Executive Summary

The childcare investment market in New South Wales has demonstrated remarkable resilience and adaptability in 2024, despite facing significant economic headwinds.

As of September 1st, transaction volumes have already reached $191.2 million, indicating strong investor confidence in this sector. This robust performance follows a record-breaking year in 2023, which saw a total turnover of $293.8 million, surpassing even the COVID-19-driven peak of 2021.

The sector appeals to a diverse range of investors, from first-time commercial buyers to experienced funds and developers, largely due to the accessible average price point of sub-$7 million per asset. Investment yields have shown particular stability, with metropolitan markets offering an average yield of 4.93%, ranging up to 5.75%. This represents only a modest increase of 83 basis points from the 2021 low, despite significant increases in the cash rate, highlighting the sector's unique position in the commercial property landscape.

DEVELOPMENT PIPELINE AND CHALLENGES

The development pipeline currently has 716 projects updated over the last six months across NSW. However, rising construction costs, labour shortages, and financing challenges have caused many projects to stall at the approval stage, leading developers to favour more cost-effective development projects such as single-level developments and avoiding basements.

Furthermore, project completion has also slowed as developers are increasingly cautious about the potential for oversupply in certain locations, detailed investigations are needed before committing to construction.

DEMOGRAPHIC TRENDS AND GOVERNMENT SUPPORT

Demographically, while NSW has experienced strong population growth of 2.2% in the past year, this hasn't directly translated to increased childcare demand. The number of children in centre-based day care has grown by an average of 2.3% per annum over the past decade, currently standing at 277,160 children from 224,800 families. Government support remains substantial, with $3.36billion spent on childcare subsidies in the March 2024 quarter alone across the country, further underpinning the sector's attractiveness as an investment.

FUTURE OUTLOOK

Looking ahead, the sector faces both opportunities and challenges. While population growth is expected to continue, particularly in Western Sydney, a declining birth rate may temper future demand growth.

Nevertheless, the childcare sector's essential service nature, coupled with strong government support and its potential for asset value growth, positions it as a compelling investment option in uncertain economic times, particularly when considering the land tax concessions and outgoings payable by the tenant. Investors and developers are adopting a more considered approach, focusing on location, quality, demographic projections, competition and long-term viability to navigate this evolving landscape.

If you'd like to discuss this report in more detail, we would be delighted to engage in a conversation with you.

PETER VINES
Managing Director
RWC Western Sydney
0449 857 100

A Snapshot of Childcare in NSW

459,040
CHILDREN IN CARE

324,350
FAMILIES USING CARE

5,246
APPROVED SERVICES

33.6 hours
AVERAGE WEEKLY USAGE

$13.25
AVERAGE HOURLY FEE

$3.36 billion
TOTAL SUBSIDIES
(AUSTRALIA-WIDE)

Source: Department of Education | March 2024

716 new childcare facilities are currently in the development pipeline across NSW

MORE THAN 80% IN METROPOLITAN AREAS

45 Projects Under Construction

362 Projects DA Approved

NSW CHILDCARE TURNOVER

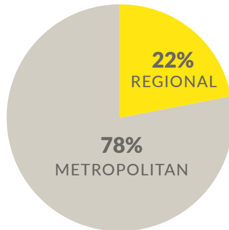
2024*	$191.2million
2023	$293.8million
2022	$175.9million

AVERAGE YIELD*

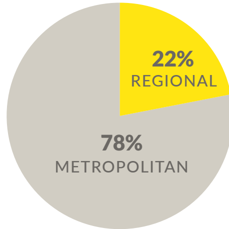
Metropolitan	4.93%
Regional	6.00%

Source: RWCWS *to 1 September

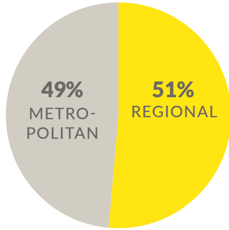
REGIONAL V METROPOLITAN SALES



2024*
METROPOLITAN
78%
REGIONAL
22%



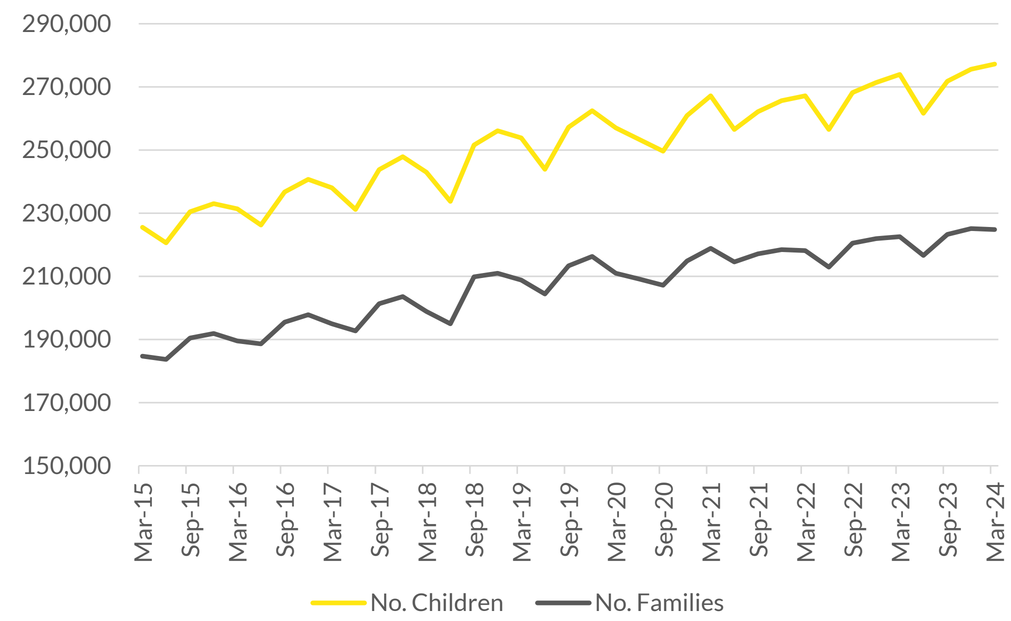
2023
METROPOLITAN
78%
REGIONAL
22%



2023
METROPOLITAN
49%
REGIONAL
51%

Need for childcare spaces continues to *grow*

NUMBER OF CHILDREN & FAMILIES UTILISING CHILDCARE
CENTRE BASED CHILDCARE, NEW SOUTH WALES



SOURCE: DEPARTMENT OF EDUCATION

In NSW, childcare offers great opportunity: with over a quarter-million children enrolled and billions in government subsidies, the sector's growth tells a story of changing family dynamics.

Over the past decade, New South Wales has witnessed a steady growth in childcare attendance. The number of children in "centre-based day care" has increased by an average of 2.3% per annum. As of 2024, this figure stands at 277,160 children from 224,800 families. Centre-based day care dominates the childcare landscape, accounting for 60.4% of all children in childcare across the state. The remaining children are split between family day care arrangements and before/after school care programs.

As of March 2024, New South Wales boasts 3,572 childcare centres. On average, children spend 33.6 hours per week in these facilities. The average cost of childcare stands at $13.25 per hour. However, this figure can be misleading, particularly in metropolitan areas where many centres charge up to $140 per day.

GOVERNMENT SUBSIDIES AND INVESTMENT

The Australian government's commitment to childcare is evident in its substantial financial support. In the March 2024 quarter alone, $3.36billion was spent on childcare subsidies nationwide. Notably, close to 85% of this funding was directed towards centre-based day care.

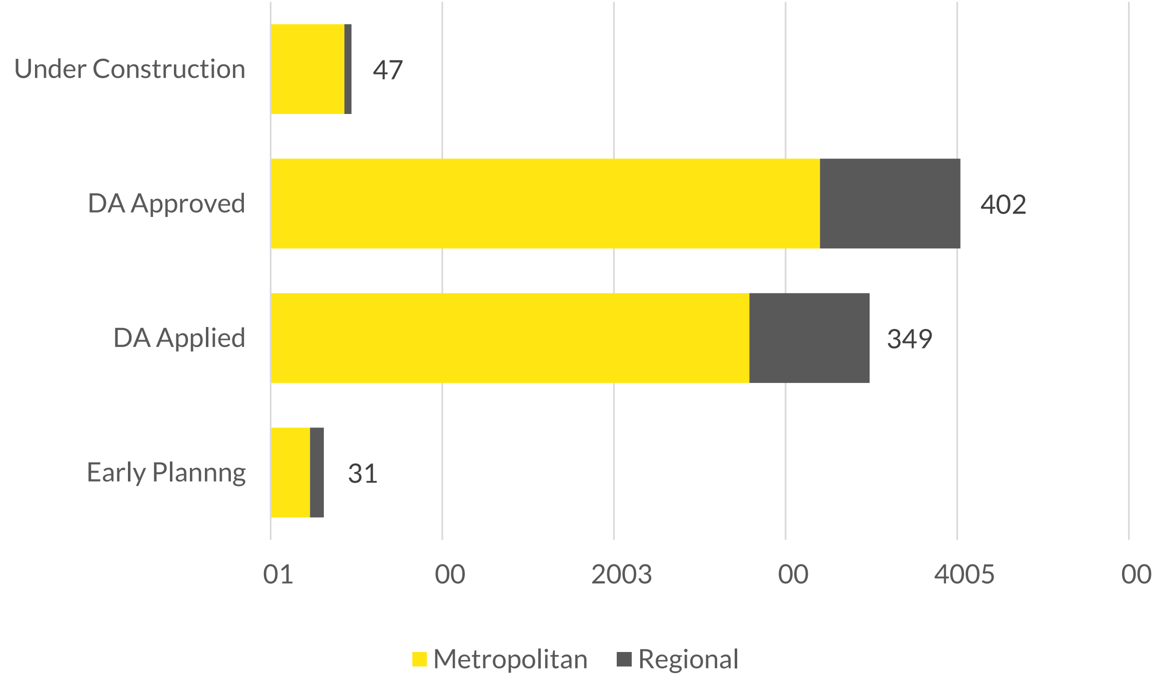
This significant government investment underscores the attractiveness of childcare as an asset class, offering a subsidised and growing income stream for investors.

The childcare sector experienced a dip in attendance during the COVID-19 pandemic. While numbers have since rebounded, the growth rate has slowed to 1.5% over the past year. This is in contrast to the substantial 2.2% increase in overall population during the 2023 calendar year.

Looking ahead, while population growth is expected to remain a key feature of the NSW economy, particularly in Western Sydney, this may not directly translate to increased childcare demand. The declining birth rate is a significant factor in this projection, suggesting that despite overall population gains, the childcare sector may not see proportional growth in demand.

Childcare pipeline remains ***large***, yet construction projects wane

NEW SOUTH WALES SUPPLY PIPELINE BY REGION
NO. OF PROJECTS



SOURCE: CORDELL CONNECT, RWCWS

With 716 childcare projects in the pipeline, NSW's childcare development sector is active—but the journey from approval to construction highlights uncertainties.

The childcare development sector in New South Wales continues to show significant activity, with 716 projects updated over the last six months. This impressive number encompasses both new centres and extensions to existing facilities, reflecting the robust development site sales activity observed over the past few years. The pipeline is particularly wide at the DA approved stage, indicating a surge in potential new childcare facilities.

CHALLENGES AND CONSTRUCTION TRENDS

The path from approval to construction has become increasingly complex. A combination of factors, including high construction costs and persistent labour shortages, has caused many projects to stall at the approval stage. Developers are grappling with the challenges of securing construction finance and ensuring project viability in this demanding economic climate. As a result, there's a noticeable preference for single-level developments, with developers steering clear of basement constructions to keep costs down, while focusing on areas where supply and demand are misaligned.

Looking ahead, there's cautious optimism in the sector. Anticipated interest rate cuts later this year and into the next are expected to inject renewed confidence into the market. This could potentially spur on the advancement of many currently stalled projects, breathing new life into the development pipeline. However, the viability of new development is increasingly location sensitive and rigorous investigations are needed to understand both demand and supply fundamentals to limit the potential for oversupply.

Currently, the construction phase echoes these sentiments, with only 47 projects actively under construction, marking a significant decrease from the previous year's figures. These projects are expected to reach completion within the next 18 to 24 months. This slowdown isn't solely attributed to financial uncertainties; it also reflects a shift in expectations surrounding demand.

WESTERN SYDNEY SUPPLY PROSPECTS

As population growth projections moderate, the location of new childcare facilities has become a critical consideration. Developers are now more meticulous in their analysis of supply, competition, and demographic projections for potential sites. This heightened scrutiny has resulted in a concentration of new projects within Sydney's metropolitan regions over regional markets, with Blacktown and Canterbury-Bankstown currently hosting the highest volume of construction activity.

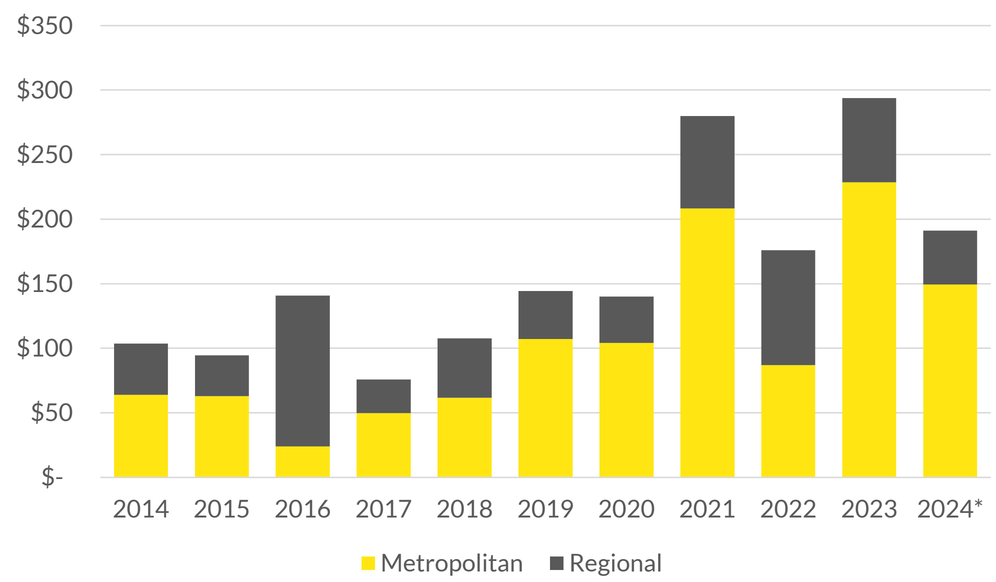
Across the total development pipeline, Sydney's western regions emerge as the epicentre of activity. Blacktown leads the charge with 84 projects in various stages of development, closely followed by Parramatta City Council area with 58 projects. The North West and South West growth corridors, benefiting from improved transport links and diverse housing options, are also seeing significant development. The Hills area boasts 46 projects in the pipeline, while the combined regions of Liverpool, Campbelltown, and Camden account for an additional 106 advancing projects.

As the childcare sector continues to evolve, it's clear that developers are adopting a more strategic, location-centric approach to ensure the long-term viability and success of their projects in the face of changing demographic and economic landscapes.

"As population growth projections moderate, the location of new childcare facilities has become a critical consideration. Developers are now more meticulous in their analysis of supply, competition, and demographic projections for potential sites."

Transaction activity ***robust***, after record 2023

NEW SOUTH WALES CHILDCARE TRANSACTION VOLUMES
$ MILLIONS



*SOURCE: RWCWS *2024 REPORTED TO 1 SEPTEMBER*

In a year of economic uncertainties, NSW's childcare sector stands as a pillar of strength, with $191.2 million in sales by September 2024 signalling unwavering investor confidence.

The childcare asset class has demonstrated remarkable resilience in 2024, with transaction volumes remaining robust despite economic uncertainties. As of September 1, sales have already reached an impressive $191.2 million, showcasing the sector's enduring appeal to investors. This strong performance comes in the wake of a record-breaking 2023, which saw a total turnover of $293.8 million, surpassing the COVID-19-driven peak of $279.8 million in 2021.

Private buyers have shown unwavering interest in childcare assets, undeterred by the tight returns on offer. The sector's attractiveness is partly due to the accessible average price point of sub-$7 million, which appeals to a diverse range of investors - from first-time commercial buyers to experienced developers, syndicates, and private funds.

2023'S RECORD-BREAKING ACTIVITY

2023 marked a significant milestone for the childcare asset market after a relatively subdued 2022. While the year began slowly, the latter half witnessed a surge in investment activity as confidence in the sector grew, this included investment into development projects as well as established centres. This resurgence was fuelled by several factors, including rapid population movements, with NSW benefiting from a significant influx of international migrants and reduced interstate losses to Queensland and Western Australia.

Notable trends in both 2023 and 2024 include:

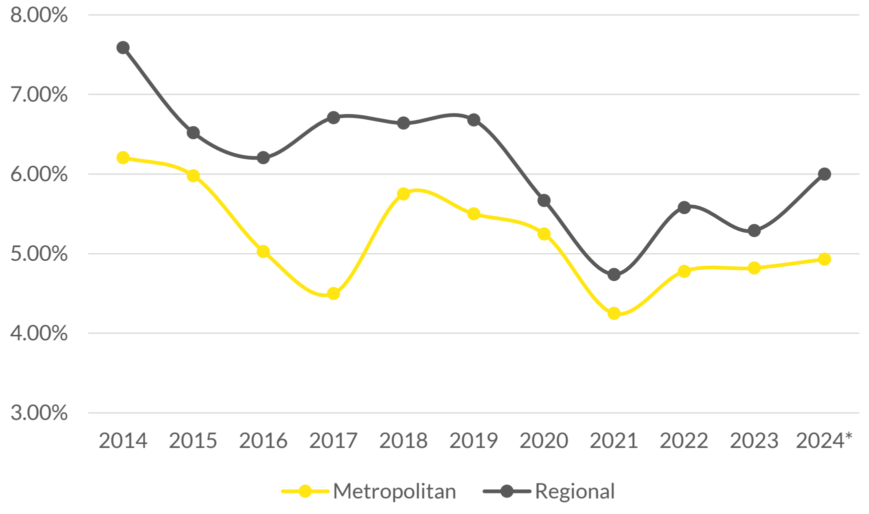
- A shift back to metropolitan investments, with over 77% of transactions occurring in these areas.
- Western Sydney emerging as a hotspot, accounting for approximately one-third of all NSW sales.
- Record-breaking transactions, such as Kids Academy Penrith & Regentville, this two-centre investment selling for just over $25 million, representing a yield of 5.6%.
- A return to fundamental analysis, with investors showing increased caution regarding local market conditions, competition, and long-term population growth projections.

While the childcare sector continues to attract substantial investment, there's a growing recognition that current population growth may not immediately translate to increased demand in the 0-4 age cohort. Investors are now taking a more refined approach, considering the potential lag between immigration and its impact on childcare needs in the coming years.

As the market evolves, the childcare asset class remains a compelling option for investors, balancing attractive returns with the essential service nature of the industry. However, success in this sector increasingly depends on strategic location selection and a thorough understanding of demographic trends and local market dynamics.

Yields remain ***tight*** in ***metropolitan markets*** while volatility ***grows*** in ***regional areas***

NEW SOUTH WALES CHILDCARE YIELDS
BY LOCATION



*SOURCE: RWCWS *2024 REPORTED TO 1 SEPTEMBER*

In a financial landscape marked by elevated interest rates and inflationary pressures, childcare investment yields show stability, defying market trends and offering investors steady returns.

Investment yields for childcare centres have demonstrated strength in the face of broader market fluctuations. Despite the cash rate's significant increase from early 2022 to its current 4.35%, childcare investment yields have not grown at the same pace as bond rates. This stability is particularly noteworthy given the challenging financial landscape, where ongoing high inflation has hindered the RBA's ability to reduce rates, although rate cuts are increasingly anticipated later this year.

The metropolitan childcare market currently offers an average yield of 4.93%, with yields ranging up to 5.75%. This represents a modest increase of 83 basis points from the 2021 low when the cash rate was just 0.1%. Regional markets have shown slightly more volatility, with yields increasing by approximately 125 basis points over the same period, though limited sales in these areas have led to some fluctuations in results. The relatively stronger performance of metropolitan assets reflects investors' preference for the longevity and security offered by urban locations.

FACTORS INFLUENCING YIELD MOVEMENT

The robust nature of childcare investments is underpinned by several factors. The strong residential market has resulted in many families relocating throughout the metropolitan area. Affordability concerns, both in buying and renting, have forced families into lower-cost housing, notably in Sydney's West. This shift has also fuelled the need for dual incomes, increasing the need for childcare in these regions, helping to maintain high occupancy rates. Government subsidies have also increased attractiveness for these establishments, making them a sought-after investment choice for buyers due to their stable and often growing income streams from quality tenants.

While population growth is strong across the state, the current influx may not directly impact childcare demand as it typically doesn't represent the relevant age cohort. However, this growth is expected to be an influencing factor in the years to come.

Childcare assets offer unique advantages for investors, which has driven strong demand and kept yields competitive. They are exempt from land tax, with net leases which see outgoings typically covered by tenants. This allows owners to benefit from income while also capitalising on potential growth in the underlying asset value, which may have future development potential or higher value uses.

The wide range of asset prices makes childcare centres an accessible investment option for various commercial investors. These factors contribute to the sector's yield stability compared to other commercial investment classes, with expectations of continued stability looking forward.

"Despite the cash rate's significant increase from early 2022 to its current 4.35%, childcare investment yields have not grown at the same pace as bond rates, demonstrating remarkable resilience in the face of broader market fluctuations."

Conclusion

The childcare investment market in New South Wales has proven to be a beacon of stability and opportunity in an otherwise turbulent commercial property landscape. As we look to the future, several key factors suggest that this sector will continue to be an attractive proposition for investors, albeit with some important considerations and evolving dynamics.

RESILIENCE AND BROAD APPEAL

The sector's endurance is evident in its impressive transaction volumes and stable yields, even in the face of elevated interest rates and inflationary pressures. This performance underscores the essential nature of childcare services and the strong government support underpinning the industry. The diverse range of investors attracted to this market, from first-time buyers to experienced funds, speaks to its broad appeal and accessibility.

CHALLENGES AND SHIFTS IN THE DEVELOPMENT LANDSCAPE

However, the path ahead is not without challenges and potential shifts. The development pipeline, while robust, faces hurdles in the form of high construction costs and labour shortages, which has resulted in an uptick in sites coming to market. These factors have led to a more cautious approach from developers, with a preference for cost-effective projects and a sharper focus on location and long-term viability to limit potential oversupply.

DEMOGRAPHIC AND WORK PATTERN EVOLUTION

Demographic shifts and evolving work patterns present both opportunities and potential pitfalls:

- Strong population growth, particularly in Western Sydney
- Declining birth rates potentially tempering future demand
- Post-pandemic work arrangements reshaping childcare needs
- Potential shifts in geographic distribution of childcare demand

Investors and developers must navigate these trends carefully, with a keen eye on local market dynamics, future population projections, and emerging work patterns.

ENDURING STRENGTHS OF CHILDCARE INVESTMENT

Despite these challenges and changes, the fundamental strengths of childcare as an investment class remain compelling:

- Exemption from land tax
- Net leases with the majority of outgoings paid by the tenant
- Potential for asset value growth and minimal risk
- Essential nature providing buffer against economic downturns

These factors continue to attract investors and underscore the sector's resilience, as evident by its quick rebound following the COVID-19 pandemic.

PETER VINES
Managing Director
RWC Western Sydney
0449 857 100

OUR OFFICE

With a strong foundation of experience and expertise, we bring a winning combination of dynamism and operational rigour to the commercial agency space.

Our People are *Your Advantage.*

SALES


PETER VINES
Managing Director


JOSEPH ASSAF
Director


VICTOR SHEU
Director


JAI SETHI
Associate Director


TROY WANG
Sales Executive


OWEN WHITE
Sales Executive


DANNY SHI
Sales - AIS


TAO SHI
Sales - AIS


ANDREW SACCO
Sales Executive


VEE LI
Sales Executive


ALEX EL HAZOURI
Sales Associate


MARCUS AUDDINO
Sales Associate


JAYKY WU
Commercial Property Analyst


CHANTEL BRILLANTES
Marketing & Design


MONH LY
Campaign Manager

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

LEASING


ROBERT NAPOLI
Senior Leasing Executive


SAMUEL GONG
Senior Leasing Executive

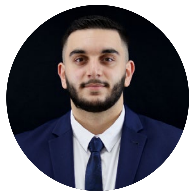
ASSET MANAGEMENT


JOYCE ELKOUBERCI
Director


CALLUM MCKAY
Asset Manager


SUZIE NIU
Asset Manager


AALIYAH CHAMI
Assistant


ADRIAN HARB
Assistant


MARCUS FUNG
Assistant


ANNIKA WARD
Assistant


ZEINA TAJIK
Accounts

OPERATIONS


RUBY ROZENTAL
Director of Strategy


HANNAH CARNEY
Director of Operations


PAULINE WATERFORD
Finance Manager


CHRISTIAN BRILLANTES
Office Assistant

PROJECTS


MARK BERNBERG
Managing Director


LIAM SIMPSON
Senior Sales Executive


NATASHA SANDERS
Sales Associate


SHANI FERDMAN
Sales Assistant


BETTY NGUYEN
Marketing Coordinator

RWC WESTERN SYDNEY

Level 1, 15-17 Argyle Street
Parramatta NSW 2150

(02) 8074 4884

rwcws.com