Review of Office Demand within Rhodes

Prepared for NSW Department of Planning, Industry and Environment

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Contents

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Executive Summary

Background & Scope

Background & Scope

In 2015 the City of Canada Bay Council (Council) nominated Rhodes as an area for potential renewal and has been collaborating with the NSW Department of Planning, Industry and Environment (DPIE) and state agencies on plans for the area. Over the last four years, draft Precinct Plans have been prepared and exhibited. Most recently, DPIE prepared and released the draft Rhodes place strategy which:

'…outlines how the precinct will provide opportunities for residential and other uses supported by infrastructure and public benefits.'

The draft Rhodes place strategy was exhibited for feedback between 31 August and 9 October 2020, through this exhibition receiving about 3,000 submissions. We have been advised by DPIE that a key theme within the submissions relates to the potential over supply / provision of commercial floor space.

Based on the above, DPIE requires an understanding of the potential demand for commercial office within the Rhodes Precinct, as this may inform whether any changes to the draft Rhodes place strategy should occur. JLL have been engaged to undertake analysis to understand the demand for new office in the Rhodes Precinct over the short, medium, and long-term.

Historic & Current Economic Context

Historic & Current Economic Context

Overview of Key Economic Indicators

We set out an overview of key economic indicators below for reference. With this data being released in December 2020 it now reflects a better understanding of the impact of COVID-19, notwithstanding, we are currently in unprecedented circumstances and forecasts are prepared with the latest information available. We have over the next few pages looked further into the impact of COVID-19 on property markets, particularly the office market.

Table: Historic, Current and Forecast Economic Conditions (Average % or % p.a. CAGR)

National	Historic	Current	Forecast	Observations
Standard bank variable mortgage rate (average)	7.4% (CY91-CY20) 5.8% (CY11-CY20)	4.6% (CY20)	5.2% (CY21-CY30)	Interest rates to slightly increase after recent compression
Treasury Bonds (10 year) (average)	5.5% (CY91-CY20) 2.9% (CY11-CY20)	0.9% (CY20)	1.6% (CY21-CY30)	Risk free rates to stabilise in the short term and expected to revert to slightly higher levels
CPI (average)	2.3% (CY91-CY20) 1.9% (CY11-CY20)	1.3% (CY20)	2.0% (CY21-CY30)	CPI to revert to slightly higher levels than current, akin to historic
NSW	**Historic**	**Current**	**Forecast**	**Observations**
Gross State Product (CAGR)	2.4% (CY90-CY20) 2.1% (CY10-CY20)	-2.4% (CY20)	2.7% (CY20-CY30)	GSP growth to expected to moderate over the next 10 years to historic levels after recent decline
Private housing investment (CAGR)	2.0% (CY90-CY20) 1.9% (CY10-CY20)	-10.2% (CY20)	1.8% (CY20-CY30)	Negative private housing investment growth in the short term and expected to moderate over next 10 years
Retail turnover (CAGR)	3.1% (CY90-CY20) 2.8% (CY10-CY20)	2.7% (CY20)	3.0% (CY20-CY30)	Retail growth moderating to long term average over next 10 years
Total population (CAGR)	1.1% (CY90-CY20) 1.3% (CY10-CY20)	0.8% (CY20)	0.9% (CY20-CY30)	Population growth to decline over the short term and expected to moderate over next 10 years
Employment growth (Sydney GCCSA) (CAGR)	1.4% (CY90-CY20) 1.5% (CY10-CY20)	-2.4% (CY20)	1.5% (CY20-CY30)	Employment growth moderating to long term average over next 10 years

Source: Australian Bureau of Statistics, Deloitte Access Economics, NSW Department of Planning & Environment, JLL Notes: CAGR – Compound Annual Growth Rate; GCCSA – Greater Capital City Statistical Area

COVID-19 Impact

Overview

The World Health Organisation declared the Coronavirus (COVID-19) a global pandemic on 11 March 2020. The outbreak of COVID-19 has spread globally and is continuing to spread. Countries across the world are implementing protective policy measures designed to slow the spread of COVID-19, including travel and border restrictions, closure of non-essential businesses and services, social distancing, self-isolation and other measures

Consequently, COVID-19 has caused global economic uncertainty which is having a significant impact on the financial markets, investment, business and consumer confidence. Whilst Governments are responding with fiscal policy measures, including the Australian Government, economic volatility is likely to continue given the current uncertainty as to the length and severity of the pandemic.

Property Markets

Economic uncertainty has consequences for property markets. Factors affecting value could include reduced investor and occupier confidence, softening investment yields, reduced occupier demand, lower rental values and higher vacancy rates. In addition, reduced transaction and development activity across all sectors is likely as decision making could be delayed in light of the current economic uncertainty.

Overview of Key Economic Indicators

- Australian Gross Domestic Product (GDP) numbers show that Australia had an unprecedented 27 years without recession, the only country in the developed world with such an extended period of uninterrupted economic growth. However, the economic shock caused by the COVID-19 pandemic impacted growth, particularly early in 2020 with contractions in GDP in both the March (0.3%) and June (7%) quarters, resulting in Australia entering its first recession since the 1990s.
- However, Australian GDP bounced back in the second half of 2020 with a 3.4% increase in the September quarter and a 3.1% increase in the December quarter.
- Despite the historic strength of the Australian and NSW economies, there was considered to be a risk of future moderation before the onset of the COVID-19 pandemic. The outlook for the NSW economy was for a slowdown of growth in State Final Demand (SFD) and Gross State Product (GSP). A decline in residential construction activity was also expected, after a period of extraordinary growth, which was accelerated due to the economic impacts of the COVID-19 pandemic.
- The Reserve Bank lowered the cash rate twice in March 2020 from 0.75% to 0.50% on 3 March 2020 and again to 0.25% on 19 March 2020 in response to the impacts of the COVID-19 pandemic. As of 3 November, the cash rate has remained at 0.10%.

COVID-19 Impact on Office

Some of the key impacts and observations to the office sector include:

- Most Australian office sectors were operating with low prime grade vacancy prior to the outbreak – risk is concentrated for secondary grade assets where vacancy is elevated. In the short term, the flexible / co-working space sector is likely to undergo significant consolidation.
- Over the longer term, the outbreak will fast track structural changes of remote working and investment in collaborative technologies. Despite the current switch to mass remote working, the physical office will maintain its importance for facilitating interaction, collaboration and employee health, wellbeing and productivity.

Sydney Office Market

Office Market Definitions

Office uses broadly fit into three category types, these are:

1. Investment grade office assets. These are generally defined as large floor plate office buildings within 'defined' office precincts. Within Sydney these include Sydney CBD, Sydney Fringe, Chatswood, Macquarie Park and Parramatta, as well as others identified within this report.
2. Support office uses. These uses generally provide localised services to the community and share some characteristics to retail uses. They often benefit from access to the public and therefore public transport, car parking and exposure are important considerations. Examples include real estate agents, accountants and local solicitors' offices. These are often provided in smaller office type accommodation.
3. Office uses that support another primary land use e.g. a small amount of office within an industrial facility or medical facility. This is not considered in significant detail in this report as the nature of this type of product is generally found outside commercial centres. Note, for the purposes of definition we have assumed the small amount of office that supports retail uses within the 'support office uses' above.

Our observation of the opportunity for office uses in the Rhodes Precinct generally fall into the first two categories, with greater risk in achieving the new investment grade assets, whereas, the second category will be driven by growth in local and catchment population.

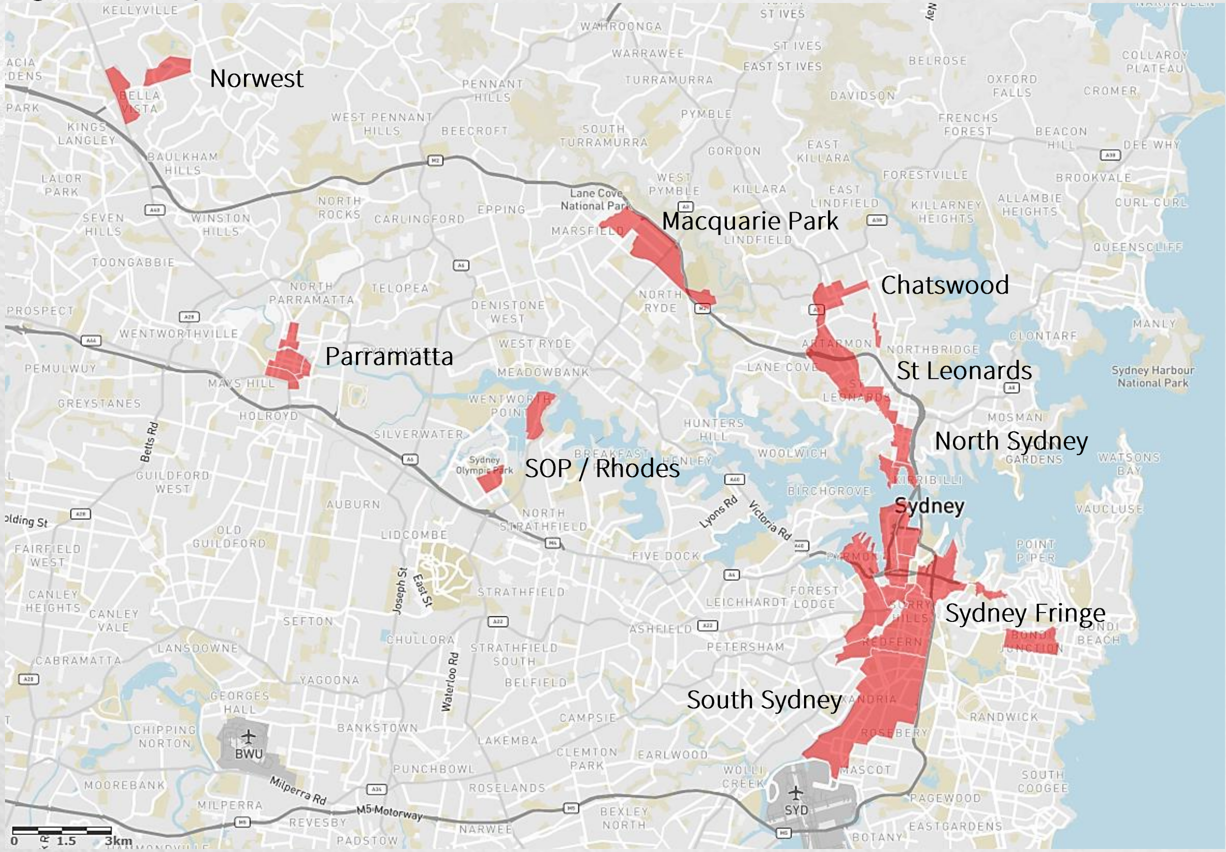
Overview of Sydney Office Markets

The Sydney office markets monitored by JLL comprise just over 10.1 million sqm of office space, 50.5% of which is located in the Sydney CBD market, and 49.5% located in the 9 major metropolitan office markets. The Sydney metropolitan markets monitored by JLL include the following:

- Sydney Fringe
- North Sydney
- Chatswood
- St Leonards
- Norwest
- Sydney Olympic Park/Rhodes (focus of this report)
- Sydney South
- Macquarie Park (including North Ryde)
- Parramatta

For the purposes of this report, we will be focusing our observations on the SOP/Rhodes commercial office market.

Figure: Sydney CBD and Metropolitan Office Market Locations



Source: JLL

Overview of Sydney Office Markets continued

The metropolitan markets comprise a mix of fringe CBD locations, major suburban CBDs such as Parramatta and Chatswood, inner suburban locations and business parks. Each of these locations has quite different characteristics that may attract different occupiers.

- The Sydney Fringe office market adjoins the CBD market and provides a viable near city alternative to the CBD. Typically, occupancy costs are lower (both rents and parking costs) and car parking provision is higher. The Fringe locations suit companies that desire an affordable, central location with better access to low cost parking for both workers and customers.
- Suburban CBDs include Parramatta, North Sydney and Chatswood. Some of these markets have attracted a large government workforce (e.g. Parramatta) with state government in particular decentralising some of their services to these locations. The markets generally have reasonable access to public transport and a good mix of support services. Rents are significantly lower than the CBD market.
- Business parks are typically lower density office locations providing modern, affordable accommodation with plentiful parking for workers and customers. Low rise buildings with large floor plates are common, providing greater flexibility and efficiency. Examples in Sydney include Norwest, Rhodes and Sydney Olympic Park.
- Other inner suburban locations are often an extension of fringe markets and have attracted office accommodation due largely to their relatively central location and good access to transport e.g. St. Leonards/Crow Nest. These markets have often been attractive due to their proximity to higher socio-economic residential areas which are where a high proportion of the employees reside.

Supply & Demand

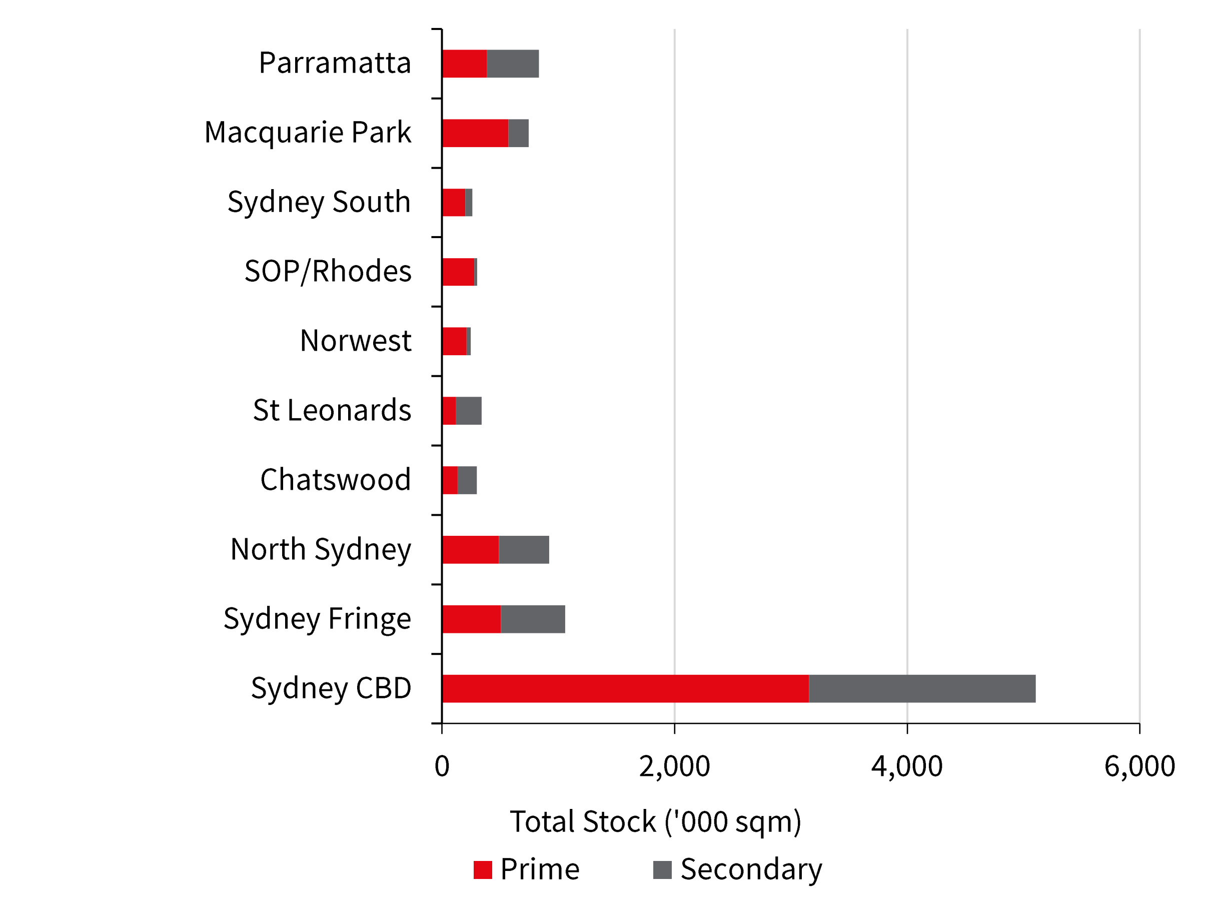
As at Q4 2020, the total stock across the nine monitored metropolitan markets was 5.007 million sqm. The largest Sydney metropolitan market is the Sydney Fringe and it comprises 1.060 million sqm of stock, accounting for 10.5% of the total Sydney office market, which includes Sydney CBD.

Table: Sydney Office Market Profile, Q4 2020

	Net Lettable Area	Prime Grade Stock	Secondary Grade Stock
	'000 sqm	% Total Stock	% Total Stock
CBD Markets			
Sydney CBD	5,106	61.8%	38.2%
Metropolitan Markets			
Sydney Fringe	1,060	47.8%	52.2%
North Sydney	921	53.2%	46.8%
Chatswood	298	44.9%	55.1%
St Leonards	341	34.4%	65.6%
Norwest	246	85.4%	14.6%
SOP/Rhodes	302	91.5%	8.5%
Sydney South	261	76.4%	23.6%
Macquarie Park	746	76.6%	23.4%
Parramatta	832	46.1%	53.9%

Source: JLL Research

Figure: Prime and Secondary Grade Stock by Metropolitan Market, Q4 2020



Source: JLL Research

Supply & Demand continued

We have recorded a slowdown in the Sydney office leasing market, with a negative net absorption in occupied stock in the 12 months to Q4 2020. The 10 Sydney markets overall contracted by -321,302 sqm over the last 12 months, which is mainly attributed to Sydney CBD, which experienced the largest contraction (-278,118 sqm). -57,329 sqm of net absorption was recorded in the Sydney CBD market over 4Q20, of which 78% was driven by large corporates (>1,000 sqm). The 2020 net absorption result exceeded the demand contraction during the GFC (80,700 sqm in 2009) as well as the demand contraction during the early 1990s economic recession (-110,000 sqm in 1991).

There was some considerable divergence between the best performing and worst performing, with the largest expansion coming from Sydney Fringe (45,040 sqm), driven primarily by The Commonwealth Bank's consolidation into Australia Technology Park. CBA pre-leased 50,951 sqm in the Foundry Building at 2 Locomotive Street, Eveleigh.

New supply in the 12 months to Q4 2020 totalled 300,282 sqm across the nine metropolitan office markets, equivalent to 6% of existing stock in this market. Of the nine metropolitan markets, three recorded no new supply in the 12 months to Q4 2020 – Chatswood, Norwest, and SOP/Rhodes. The stand out of contributors to new supply was North Sydney which contributed 98,439 sqm, equating to 10.7% of its existing stock. During this same period, Sydney CBD saw completions total 96,583 sqm, equivalent to 1.9% of existing stock.

Projects currently under construction across the nine metropolitan office markets as at Q4 2020 totalled 263,132 sqm, equivalent to 5.3% of existing stock. This is a relatively high level of construction activity when compared to CBD market, where 273,331 sqm, equivalent to 5.4% of CBD stock, is under construction. Most of the metropolitan projects under construction are attributed to the Parramatta and Sydney Fringe office markets, which together account for 83.1% of the total construction across the nine metropolitan office markets. SOP/Rhodes has recorded no new projects as currently under construction.

Table: Sydney Office Market Profile, Stock, Supply and Net Absorption, Q4 2020

	Net Lettable Area	Net Absorption 12 mths to Q4 2020	Completions 12 mths to Q4 2020	Completions 12 mths to Q4 2020	Under Construction	Under Construction
	'000 sqm	'000 sqm	'000 sqm	% of NLA	'000 sqm	% of NLA
CBD Markets						
Sydney CBD	5,106	-278.1	96.6	1.9%	273.3	5.4%
Metropolitan markets						
Sydney Fringe	1,060	45.0	75.2	7.1%	34.8	3.3%
North Sydney	921	-11.3	98.4	10.7%	13.0	1.4%
Chatswood	298	-29.1	0.0	0.0%	0.0	0.0%
St Leonards	341	10.2	32.3	9.5%	9.9	2.9%
Norwest	246	-2.0	0.0	0.0%	12.1	4.9%
SOP/Rhodes	302	-9.5	0.0	0.0%	0.0	0.0%
Sydney South	261	-33.7	1.0	0.4%	9.4	3.6%
Macquarie Park	746	3.4	49.4	6.6%	0.0	0.0%
Parramatta	832	-16.2	44.0	5.3%	183.9	22.1%

Source: JLL Research

Vacancy

As at Q4 2020, the total prime grade vacancy rate in the nine metropolitan markets was 13.9% compared to 12.5% for the Sydney CBD market. The total metropolitan markets' vacancy was 13.3% while the total vacancy for the Sydney CBD market was 11.9%. Norwest currently has the lowest overall vacancy rate of 7.7%, however, Sydney Fringe have the lowest prime grade vacancy of the Sydney markets at 5.7%. Historically the metropolitan and CBD markets have typically had higher vacancy rates in secondary stock, however, more recently this appears to not always be the case. Four of the nine metropolitan markets (North Sydney, Chatswood, Norwest and Sydney South) recorded a higher prime-grade vacancy than secondary-grade vacancy in Q4 2020.

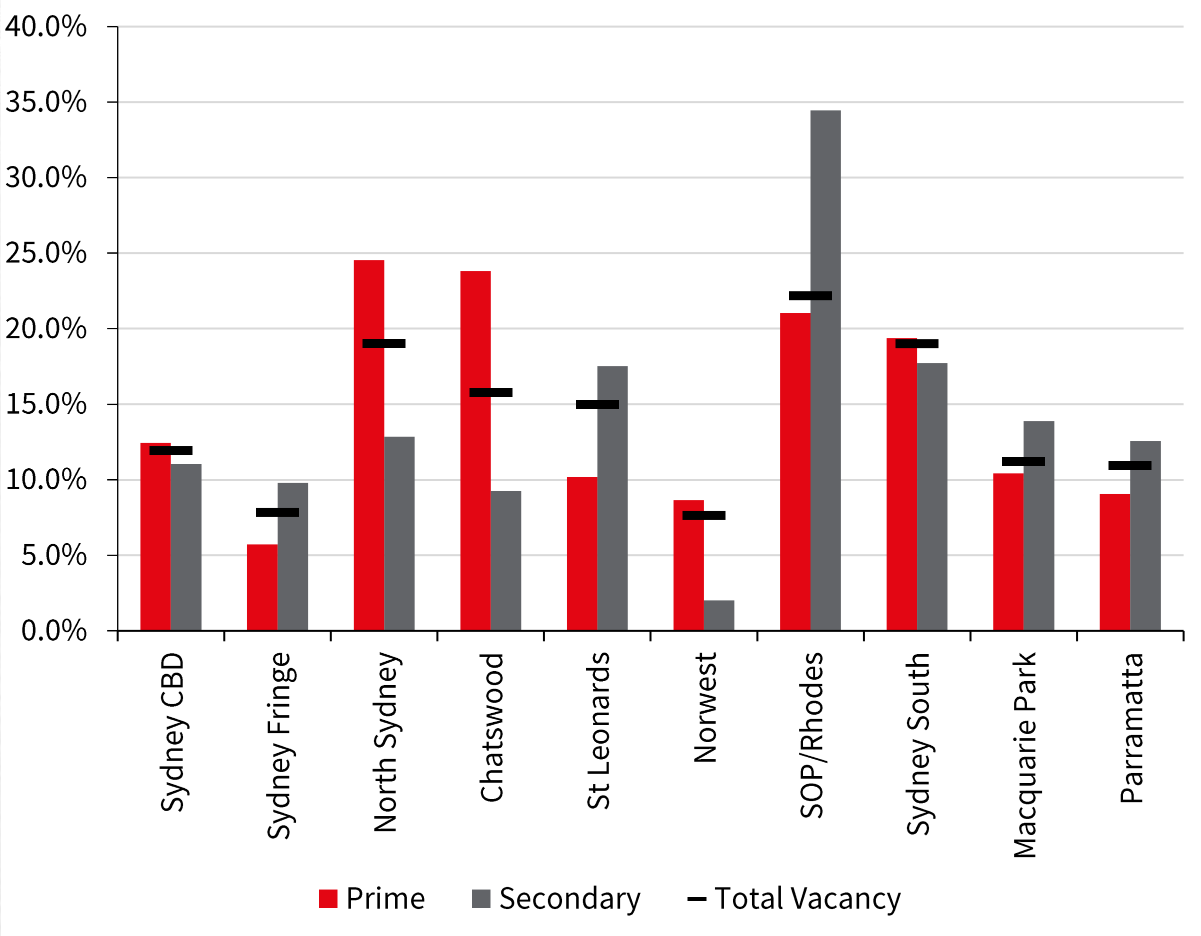
Within the Sydney office markets, Sydney Olympic Park/Rhodes has the highest total vacancy (22.2%) as well as the highest vacancy in secondary stock (34.4%), while North Sydney has the highest vacancy in prime stock (24.5%). There have been a few large occupier moves away from SOP/Rhodes in the last 12 months, including the Commonwealth Bank consolidating their office accommodation and vacating 20,000 sqm from 2 Dawn Fraser Avenue, along with the relocation of NAB from Building B1 Homebush Bay Drive to 3 Parramatta Square.

Table: Sydney Office Market Profile Vacancy, Q4 2020

	Vacancy % NLA	Prime Grade Vacancy % NLA	Secondary Grade Vacancy % NLA
CBD Markets			
Sydney CBD	11.9%	12.5%	11.0%
Metropolitan Markets			
Sydney Fringe	7.8%	5.7%	9.8%
North Sydney	19.1%	24.5%	12.8%
Chatswood	15.8%	23.8%	9.2%
St Leonards	15.0%	10.2%	17.5%
Norwest	7.7%	8.6%	2.0%
SOP/Rhodes	22.2%	21.0%	34.4%
Sydney South	19.0%	19.4%	17.7%
Macquarie Park	11.2%	10.4%	13.9%
Parramatta	10.9%	9.1%	12.5%

Source: JLL Research

Figure: Prime and Secondary Vacancy Rates, Q4 2020



Source: JLL Research

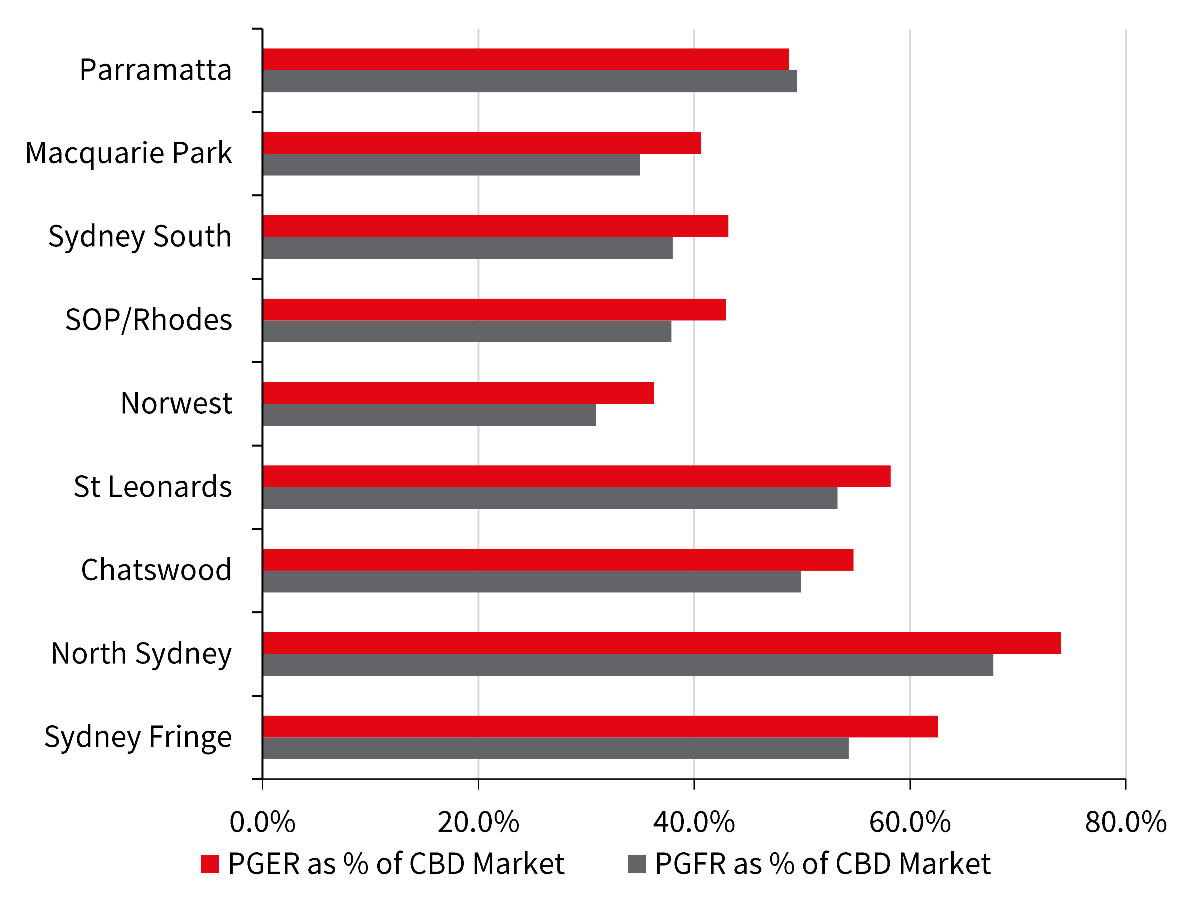
Rental Market

Metropolitan markets are more affordable than the CBD market. Generally, affordability is a key driver attracting occupiers to metropolitan markets, however, each market can also have alternative drivers e.g. proximity to demand driver i.e. university, hospital, etc. or clustering of certain industries.

Prime gross face rents in Sydney metropolitan markets range from an average of 30.9% of Sydney CBD rents in Norwest to 54.3% of CBD rents in Sydney Fringe, with other metropolitan markets in between these levels. The North Sydney market is comparatively much closer to Sydney CBD rents, with prime gross face rents averaging 67.7% of Sydney CBD rents.

However, when incentives are taken into account, the proportion of metropolitan to CBD rent increases for all Sydney metropolitan markets with the exception of Parramatta (as all metropolitan markets have a proportionally lower incentive, with the exception of this market) as evident to the right.

Figure: Prime Gross Face (PGFR) versus Effective Rents (PGER) Compared to Sydney CBD Market, Q4 2020



Source: JLL Research

Rental Market continued

Positive growth in prime gross face rents has occurred across all markets (Sydney CBD and metropolitan) in the 12 months to Q4 2020, this growth ranged from 0.0% in St Leonards to 9.1% in SOP/Rhodes, with the market overall averaging growth of 3.0%.

In all markets prime gross effective rents (rents adjusted for incentives) grew slower than prime gross face rents as incentives have increased.

We recorded prime effective rental decline across the majority of Sydney office markets over the quarter, which was mainly driven by an uptick in incentives due to the reduction in leasing activity caused by the COVID-19 outbreak. The largest decline in prime gross effective rents was recorded in Parramatta (-11.9%), resulting from a 13.3% increase in incentives in the last 12 months.

Table: Sydney Office Market Profile Rents, Q4 2020

	Prime Gross Face Rent	Annual Growth % Year to Q4 2020	Prime Gross Effective Rent	Annual Growth % Year to Q4 2020	Prime Incentives as at Q4 2020
	$/sqm p.a.	%	$/sqm p.a.	%	%
CBD Markets					
Sydney CBD	1,427	2.6%	930	-11.0%	23.3%
Metropolitan markets					
Sydney Fringe	775	1.9%	582	-7.0%	18.7%
North Sydney	967	1.7%	688	-5.6%	22.0%
Chatswood	712	1.4%	509	-7.3%	21.2%
St Leonards	761	0.0%	541	-8.4%	21.8%
Norwest	442	1.2%	337	-5.6%	23.0%
SOP/Rhodes	541	9.1%	399	-0.3%	25.7%
Sydney South	542	1.7%	401	-4.0%	33.5%
Macquarie Park	499	2.0%	378	-3.4%	24.9%
Parramatta	707	8.8%	454	-11.9%	24.5%

Yields & Capital Values

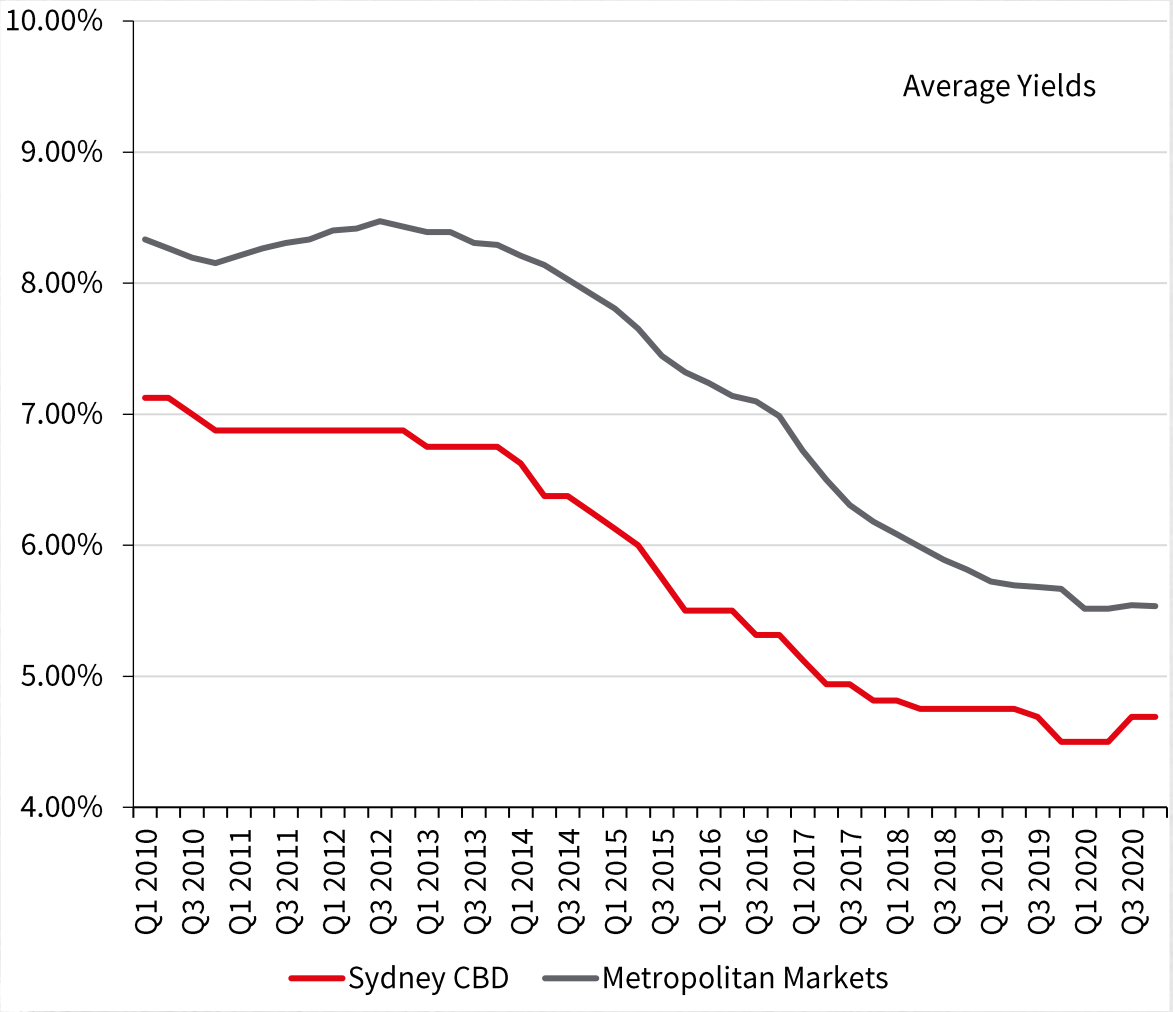
Nearly all Sydney metropolitan markets (except Sydney Fringe and Chatswood, which has experienced no change) have experienced at least some yield compression for prime grade assets over the 12 months to Q4 2020.

Yields for metropolitan assets are higher than CBD assets, however, this spread has declined significantly in recent years. The yield spread between average prime yields across the CBD market and average prime metropolitan yields was 84.50 basis points in Q4 2020. The yield spread has decreased over the last 12 months (from 116.72 basis points in Q4 2019), and is still considerably lower than the historic average over the last 10-year period of 142 basis points.

There are a number of reasons for this compression compared to historic averages, including that during an improving market the difference between superior and inferior assets reduces, which has been the case recently (with the exception of the last 12 months). In addition, this compression can also relate to the metropolitan markets becoming more attractive, including:

- In recent years investors with desire or requirement to invest in the Sydney office market have in some instances been priced out of the Sydney CBD, as such, they have looked to the metropolitan markets in order to enable exposure to the office market.
- Development of new, large office assets in the metropolitan markets provides both better quality assets and as these assets are normally pre-committed with majors tenants, they also often benefit from longer weighted average lease expires (WALE).
- In certain metropolitan locations, yields have also been influenced by acquisitions seeking development upside. This could either be for additional commercial floor area than currently allowable or seek to alter use i.e. a mixed-use, primarily residential development.

Figure: Yield Spread between Sydney CBD and Metro Markets, Q1 2010 to Q4 2020



Source: JLL Research

Yields & Capital Values continued

Specific yield ranges for each of the office markets as at Q4 2020 are provided below:

Table: Sydney Office Market Profile, Yields Q4 2020

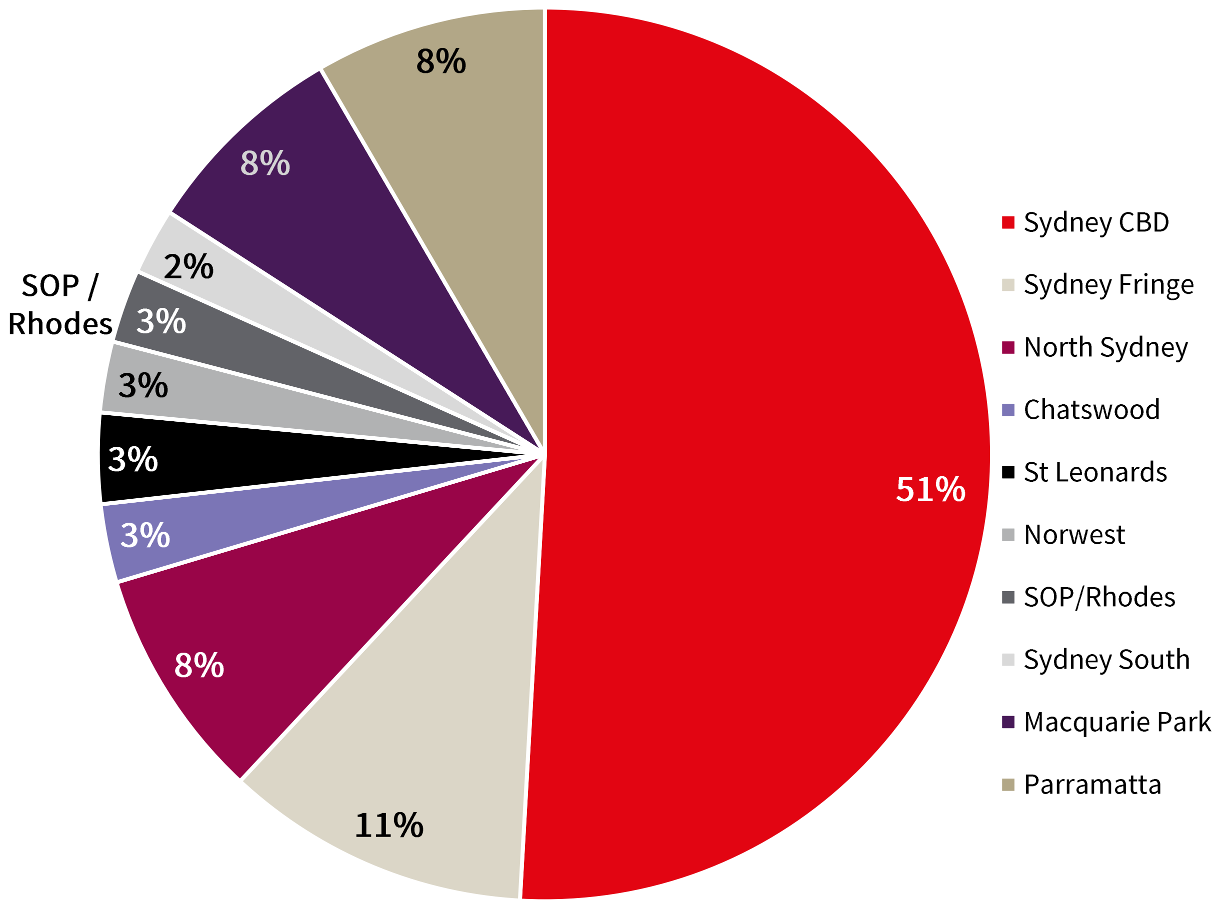
	Prime Yields as at Q4 2020
	%
CBD Markets	
Sydney CBD	4.38 – 5.00
Metropolitan markets	
Sydney Fringe	4.75 - 5.25
North Sydney	4.75 - 5.25
Chatswood	5.50 - 6.25
St Leonards	5.00 - 5.50
Norwest	5.75 - 6.75
SOP/Rhodes	5.50 - 6.50
Sydney South	5.25 – 5.75
Macquarie Park	5.00 - 6.00
Parramatta	4.88 - 6.00

Source: JLL Research

Sydney Occupied Office Stock

As at Q4 2020 the current occupied office space in the markets tracked by JLL totalled 8,836,916 sqm. The SOP/Rhodes office market as at this time equated to a total of 234,853 sqm in occupied stock, comprising approximately 2.7% of the total Sydney office market.

Figure: Sydney Office Markets – Current Occupied Stock Levels, Q4 2020



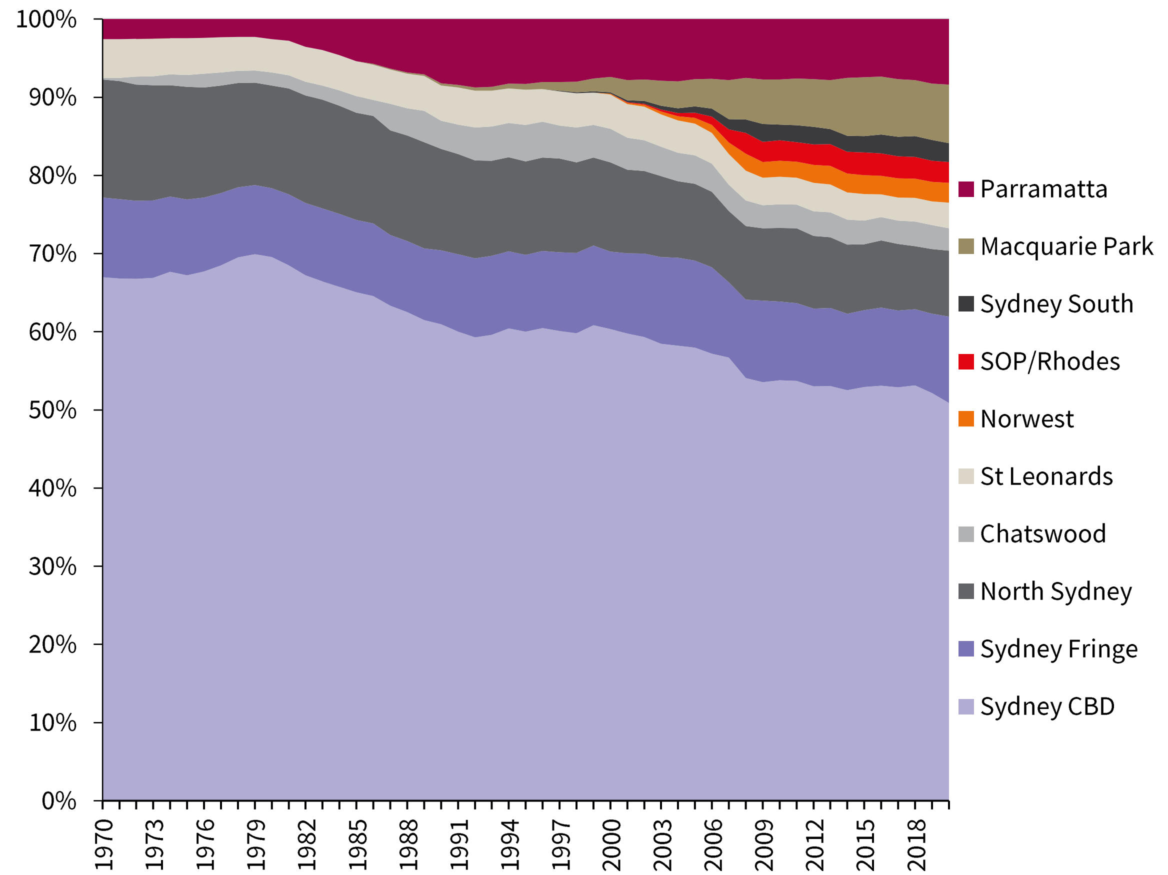
Source: JLL Research

Historic Growth of the Suburban Markets

Decentralisation of the Sydney Market

The below figures show the relative decentralisation of the Sydney office market. While the Sydney CBD has continued to grow in absolute terms it has shrunk as a proportion of the total market from 67% in 1970 to 51% by the end of 2020.

Figure: Sydney Office Market NLA (Proportion), 1970-2020



Source: JLL Research

Observable Trends

The Emergence of the Hub & Spoke Model

Factors attributing to the decentralisation of the Sydney office market include emergence of the Hub & Spoke Model

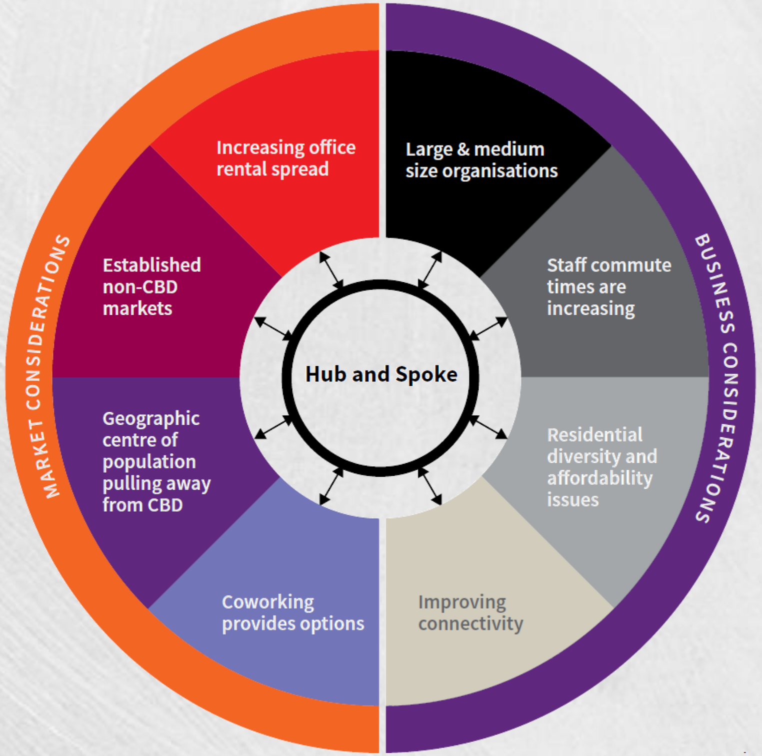
In Sydney we are seeing the emergence of a hub and spoke business model for some corporates, which in this context relates to office occupiers that are traditionally CBD based and that have reorganised their operations to have a major office presence in the CBD but also a significant but typically smaller secondary office location elsewhere. Examples are varied and can include major CBD tenants such as accounting firms (e.g. PWC – in the CBD and Parramatta) and law firms (e.g. Herbert Smith Freehills – in the CBD and Macquarie Park).

A hub and spoke business model has emerged in Sydney partly because of the office rental spread between CBD and non-CBD markets (discussed overleaf) but is also driven by a number of human factors including staff attraction and retention.

Low housing diversity, residential affordability issues in near CBD locations, increasing congestion and commute times for some staff may make attracting and retaining high quality staff difficult and this may be alleviated with the adoption of a hub and spoke business model.

Almost half of Greater Sydney's population is projected to be residing west of Parramatta by the time Greater Sydney has grown to a population of 8 million people (GSC). Over time staff will be increasingly passing through Parramatta and other metropolitan centres to get to work in the CBD. Having multiple office locations allows for staff flexibility and this is facilitated by improving video conferencing technology.

Figure: Reasons for the Adoption of the Hub & Spoke Model



Source: JLL Research

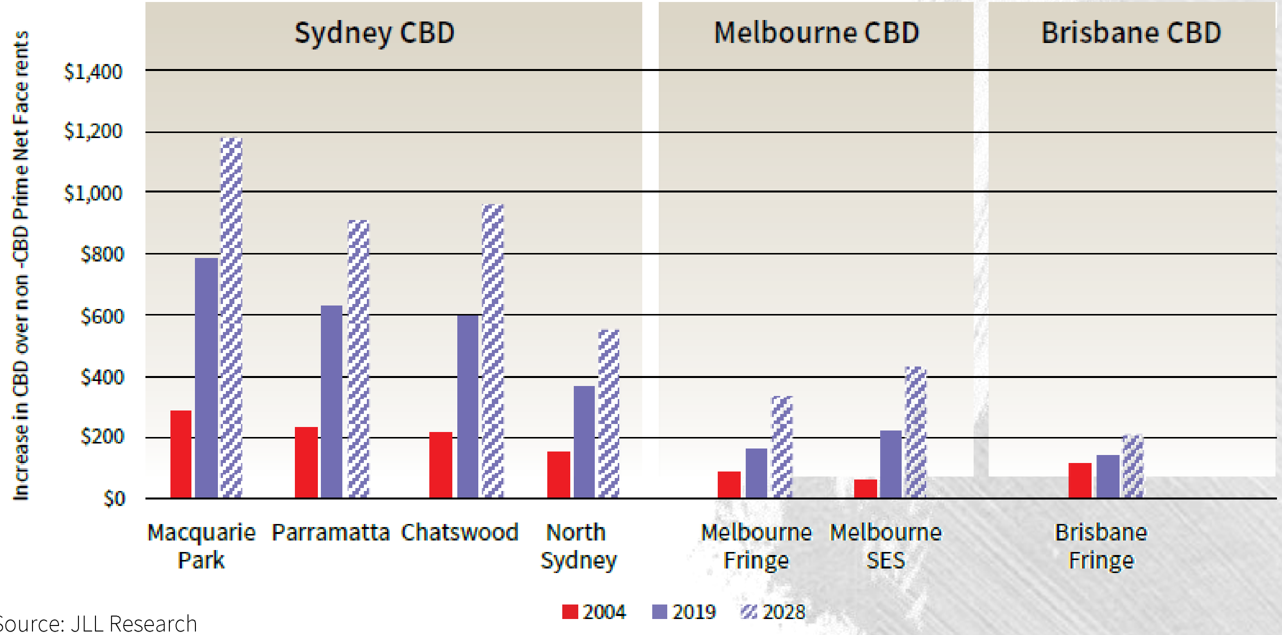
Observable Trends continued

Rental Divergence

In all Australian cities CBD office rents are on average higher than for equivalent space in non-CBD or metropolitan markets. However, the rental spread between CBD and non-CBD Sydney rents is wider than in other capital city markets and is likely to be a contributing factor in the emergence of a hub and spoke business model for some occupiers in Sydney's office market. The hub and spoke business model is not yet established in other Australian metropolitan markets.

The rental spread has widened over the last fifteen years as rental growth in Sydney's CBD market has accelerated away . The rental spread between Sydney's CBD and non-CBD markets has increased in both nominal and percentage terms since 2004 .

Figure: CBD to non-CBD market average prime net face rental spread ($)



Source: JLL Research

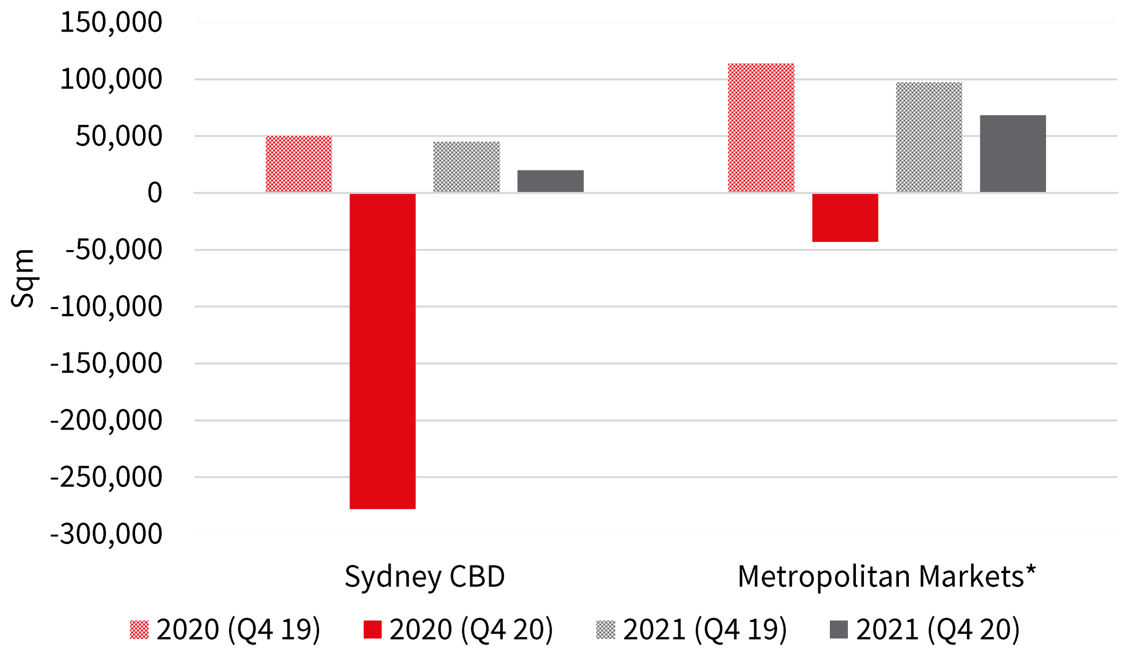
Short & Medium Term Considerations Impacting Office Demand

COVID-19 Impact on Office

JLL's Office Net Absorption Forecast

The office sector is highly sensitive to changes in the economy and employment expectations. As such, our house view of office net absorption for 2020 at the end of 2019 significantly differed from what occurred. We've also compared below our house view of 2021 as at the end of 2019 compared with the end of 2020. (see figure below).

Figure: Sydney Office Market Net Absorption



Source: JLL Research
*Only includes the forecast markets of North Sydney, St Leonards, Chatswood, Parramatta, Macquarie Park

Vacancy

Historically, office market slowdowns are accompanied by an increase in sublease availability. We are already seeing evidence of an increase in sublease availability, but it is unlikely to reach the levels experienced in the early 1990s. Organisations have been on a 30-year journey to increase density and reduce workspace ratios. We estimate that average workspace ratios are 20% to 25% lower today than the late 1980s. Headcount reductions, therefore, lead to less excess space than previous economic downturns.

We have analysed previous office market downturns (see table below). The large markets of Sydney and Melbourne entered this downturn with very low vacancy. It is important to note that for Sydney and Melbourne the expected vacancy rate trajectory pushes those markets above 12% – below the vacancy peaks recorded in the mid-1970s recession, early 1990s recession but higher than the post 2000 slowdown, GFC and early 1980s.

Table: CBD Office Market Vacancy Rate Peaks in Economic Downturns (Q4 2020)

Vacancy Rate Peaks						
Downturn	Sydney	Melbourne	Brisbane	Perth	Adelaide	Canberra
Mid-1970s	13.0%	18.3%	11.7%	-	-	-
Early 1980s	4.3%	7.8%	8.3%	15.1%	-	-
Early 1990s	22.5%	25.8%	14.3%	31.8%	20.7%	6.9%
Post 2000	11.9%	10.2%	7.0%	13.4%	13.0%	6.1%
Financial Crisis (2008/09)	8.0%	6.4%	10.2%	7.7%	8.2%	8.2%
Global Pandemic (Q1 2020)	9.6%	9.5%	12.5%	19.1%	15.7%	10.2%
Global Pandemic (Q4 2020)	12.6%	13.4%	15.4%	20.4%	16.6%	8.2%

Source: JLL Research

This report has been prepared based on information available at the time of writing which may not be reflective of current market conditions due to the evolving and unprecedented nature of the COVID-19 pandemic. The full impacts of the COVID-19 pandemic are yet to be known; however, current observations suggest a negative impact to the office market and office development, which will have implications for development within Rhodes.

Vacancy within the Rhodes Precinct

Overall, SOP/Rhodes at a vacancy rate of 22.2% has the high vacancy when compared to the rest of the Sydney office market. The market has been negatively impacted by the growth in size and recognition of other suburban markets, often with more cost-effective rentals.

Rhodes has a higher vacancy rate at 26.0%, with a higher amount of vacant space despite having less stock than that of SOP at 19.0%.

As mentioned earlier, there have been a few large occupier moves away from SOP/Rhodes in the last 12 months, contributing to the large amount of vacant space, including the Commonwealth Bank vacating 20,000 sqm from 2 Dawn Fraser Avenue (SOP), and with the relocation of NAB from Building B1 Homebush Bay Drive, Rhodes.

Table: SOP/Rhodes Vacancy by Precinct, Q4 2020

Precinct	Vacant Space	Stock	Occupied Stock	Vacancy rate (%)
Rhodes	35,375	135,948	100,573	26.0%
Sydney Olympic Park	31,580	165,860	134,280	19.0%
Total	66,955	301,808	234,853	22.2%

Source: JLL Research

Vacancy within the Rhodes Precinct Continued

As can be seen from the below figure, the SOP/Rhodes market has experienced a significantly inconsistent performance in terms of vacancy. This is largely attributed to major tenant relocations which significantly shift the vacancy of the relatively small market. Overall, the vacancy has remained relatively high with an average rate between the period Q1 2010 and Q2 2020 of 9.8%.

Figure: SOP/Rhodes Vacancy by Precinct, 2010-2020

Source: JLL Research

The current vacancy identified highlights challenges for office within the Rhodes Precinct within the short to medium term. Competition for office tenants will exist as building owners will try to secure these tenants to fill the current office vacancy.

Proposed Supply in Rhodes

The Rhodes Planned Precinct: Urban Design Report (August 2020) by Roberts Day, in collaboration with NSW DPIE and City of Canada Bay, provides the land use development summaries for the key precincts/character areas with proposed development GFAs of various land uses. We have summarised below the non-residential floor areas for each.

- Station Gateway West: 13,963 sqm of proposed non-residential GFA, which is in addition to the 12,820 sqm of proposed retail floor space
- Station Gateway East: 14,073 sqm of proposed non-residential GFA
- Leeds Street Foreshore: 4,726 sqm of proposed non-residential GFA
- Cavell Avenue Character Area: 382 sqm of proposed non-residential GFA

Based on the report by Roberts Day, there is a total of 45,964 sqm of non-residential GFA proposed within the Rhodes Planned Precinct (including current retail floor space proposed in SGW). The majority of this sits within the Station Gateway West and Station Gateway East, both sub-precincts benefiting from close proximity to the Rhodes Station.

While a large quantum of this non-residential floor space will likely relate to retail uses, we understand that some of this space will likely be office based in nature. Additionally, for more support office uses, these can locate within retail or office floor area e.g. accountants, solicitors, real estate agents, etc.

We understand that the office space, particularly in the Station Gateway West and Station Gateway East, will predominantly be located within the upper floors (first and second floor) with the retail likely residing on the ground floor. Additionally, all the non-residential floor space will be within mixed-use developments. The combination of the above two factors makes attracting larger office tenants more challenging as this offering is less appealing – compared to office only buildings.

As highlighted above, a large portion of this floor space will be retail in nature, notwithstanding, there is potential for significant supply of office within the Rhodes Precinct. For indicative purposes, we have assumed:

- 40% of the above floor space to be office in nature (including support office)
- A GFA to NLA efficiency assumption of 85%

These assumptions would equate to a potential office supply of ~15,600 sqm of NLA, representing just over 11% of the total office stock in Rhodes. This is a significant quantum of potential future office space, especially when considered in light of the relatively elevated office vacancy within Rhodes.

Future Supply of Competing Markets

Large tenant pre-commitments are typically required to enable office development to occur. These large tenants will often consider a range of suburban locations for their office accommodation needs.

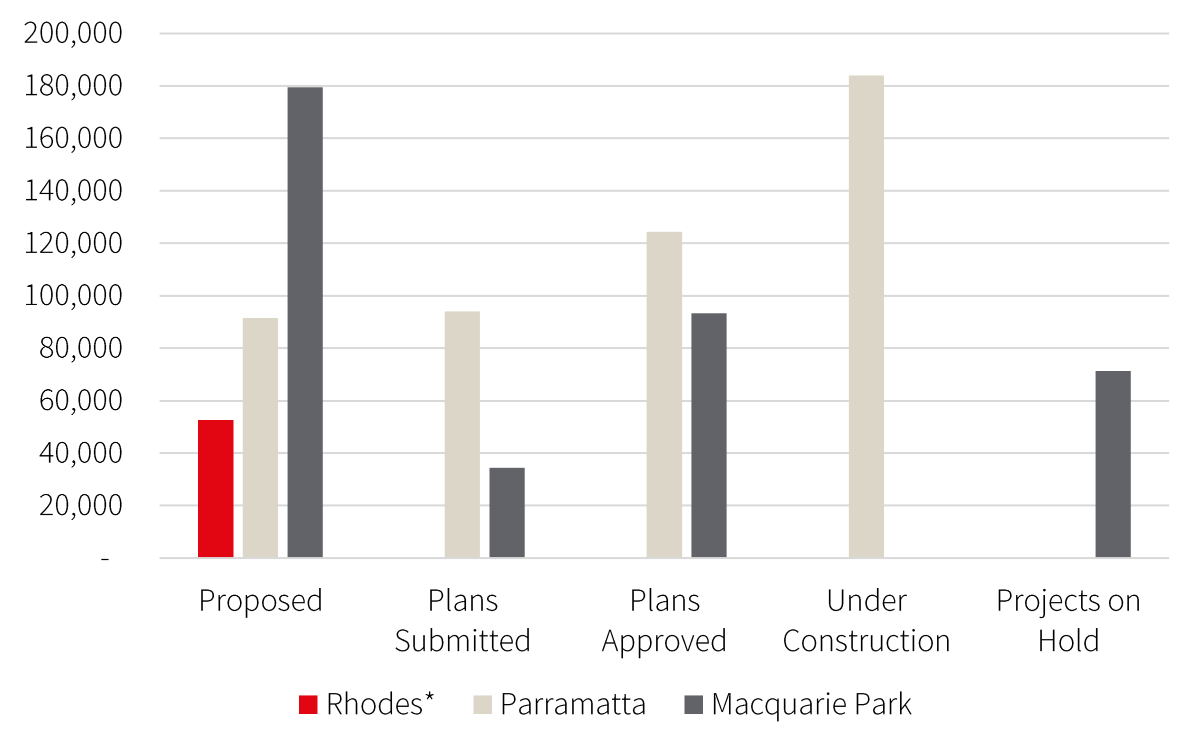
Rhodes competes with major markets of the Sydney Metropolitan area. The key competing precincts consist of Sydney Olympic Park, Parramatta and Macquarie Park.

We have analysed the short to medium term supply pipeline of these office markets to understand the level of office supply currently proposed and competing with the Rhodes office market. We note, JLL are currently not tracking any supply within the Sydney Olympic Park market, however, we understand plans are well to provide significant new office supply to leverage off the future Sydney Metro West connection (discussed further later in this report).

- Overall, Parramatta has the largest amount of future supply in office floor space at ~494,000 sqm. Of this, 183,940 sqm is office space currently under construction with 124,379 sqm with plans approved.
- This followed by Macquarie Park at ~378,551, however 71,290 sqm of this markets future supply is attributed to projects on hold. Almost half of the future supply of office floor space for Macquarie Park is attributed to proposed projects.

Rhodes' future success will depend on the markets ability to compete with these metropolitan markets that appear to currently be preferred by developers, particularly those which focus on office development, evident by their strong office development pipeline.

Figure: Future Supply of Competing Markets as of Q4 2020



Source: JLL Research

Note: For Rhodes we have utilised the office assumption tabled earlier, as well as, the proposed HP development (further details of this provided later in this report)

Long-term Considerations Impacting Office Demand

Future Supply in Rhodes

The future supply of office within Rhodes, excluding that identified in the Urban Design Report, is limited to the redevelopment of the Hewlett Packard site.

Hewlett Packard Headquarters – 410 Concord Road, Rhodes

The Hewlett Packard HQ, located at 410 Concord Road, Rhodes is a proposed office building on the eastern side of the railway line. The current site comprises of two commercial office buildings with a multi-level car park for 712 car spaces, across a 34,670 sqm parcel of land. The current GFA accounts for 19,800 sqm, resulting in an FSR of 0.5:1. underutilising the allowable FSR of 2.3:1.

A Development Application for the project was submitted in January 2021 for a 9-storey office building and 4 levels of basement car parking for 425 vehicles. The development application is for a 16,170 sqm GFA addition in A-Grade office space for the site, with potential for a further 27,480 sqm – amounting to a total proposed GFA for 43,650 sqm.

This first stage is set to commence in Q1 2022, DA approval pending, with Billbergia as the developer.

Figure: Hewlett Packard Headquarters Proposed Development

Source: Fitzpatrick + Partners – Architectural Plans for the Billbergia and Hewlett Packard Enterprises DA (Jan 2021)

Infrastructure Supporting the Growth of Competing Markets

As discussed earlier, suburban office markets in Sydney compete for tenants, especially larger tenant pre-commitments to underpin office developments. Supporting the future development of various Sydney suburban office markets are several infrastructure projects that have recently completed or are committed. These projects include:

- Sydney Metro North West
- Sydney Metro City & Southwest
- Sydney Metro Western Sydney Airport (previously Greater West)
- Sydney Metro West

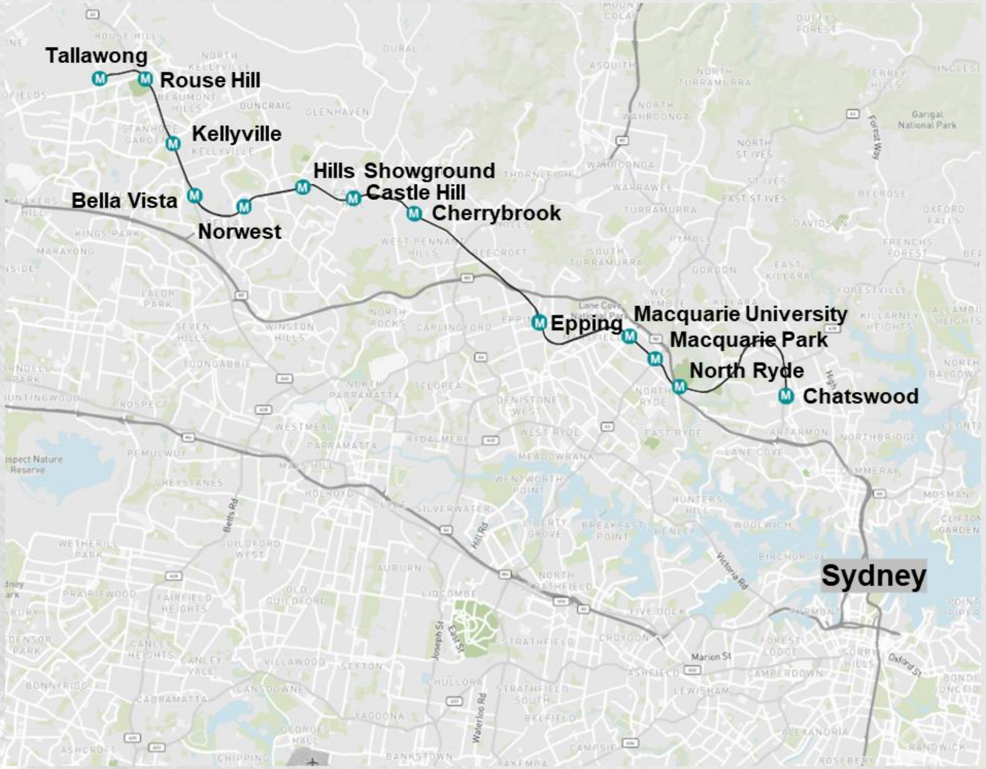
By improving the accessibility of existing office markets and supporting the creation of new office precincts over the medium to longer term, these projects will comparatively have a negative impact on the Rhodes office market.

Sydney Metro North West

Benefiting Macquarie Park and Norwest in particular, the Sydney Metro Northwest was opened in 2019, providing a driverless train service 13 railway stations between Tallawong and Chatswood.

The infrastructure will likely support future growth and opportunity at Macquarie Park, as well as growth of other markets along that corridor such as Norwest.

Figure: Sydney Metro North West Map



Source: JLL MapIT

Infrastructure Supporting the Growth of Competing Markets contd.

Sydney Metro City & Southwest

The 30-kilometre metro line will extend the Sydney Metro Northwest at Chatswood under Sydney Harbour, through new CBD stations and south west to Bankstown. The project is due to open in 2024

This will further support connectivity of established markets at Macquarie Park & Norwest, as well as the North Sydney and Sydney Fringe office markets. It will also support less established office precincts such as Bankstown.

Figure: Sydney Metro City & Southwest Map

Source: Sydney Metro

Sydney Metro Western Sydney Airport

The NSW government has committed to the new rail connection, the Sydney Metro Western Sydney Airport, connecting St Marys to the new Western Sydney Aerotropolis via the Western Sydney Airport. This commitment includes a delivery time in line with the opening of the new airport at 2026. This new infrastructure is expected to catalyse development of further office uses in western Sydney, with a particular focus across three levels of government driven by the Western Sydney City Deal to unlock new jobs within the Western Parkland City.

Figure: Sydney Metro Western Sydney Airport Map

Source: Sydney Metro

Infrastructure Supporting the Growth of Competing Markets contd.

Sydney Metro West

Anticipated to be opened in 2030, the new underground railway will connect Greater Parramatta and the Sydney CBD

The project will benefit the Parramatta office market, which already had been growing significantly and benefited from various government initiatives to support the Sydney's 2nd CBD. The project will also significantly benefit the neighbouring Sydney Olympic Park market, which has historically had poorer public transport access compared to Rhodes, as well as kick-start the creation of the Bays office Precinct.

Figure: Sydney Metro West Map

Source: Sydney Metro

Conclusions

Conclusions

Based on the analysis within this report, we believe there is potentially too much supply proposed for commercial office within the Rhodes Planned Precinct. We have provided below our rationale in forming this view:

- The **proposed product type**, being within mixed-use developments, will support demand from a subset of total office tenants. Larger office tenants are unlikely to find this offering appealing, especially in a suburban office market. **Support office users** will find still be attracted to this product, however, due to shared retail characteristics will have a preference for ground floor with foot-traffic and exposure benefits compared to upper floors. In order to assist the demand from both office or retail uses, we recommend **any conditions related to use types to be as non-prescriptive as possible** i.e. non-desirable uses should be clearly identified with all other uses being allowed.
- In the **short to medium-term** the current elevated vacancy of office in the Rhodes and adjoining Sydney Olympic Park market will need to be absorbed prior to significant supply, otherwise vacancy levels will likely continue to increase.
- While some **trends support broader suburban office growth**, Rhodes will need to **compete with other markets** for this growth. Over the **medium-term** significant supply is already proposed and further progressed in some of the key competing markets.
- In the **medium to long-term** a number of infrastructure and policy positions will continue to support the growth of other existing and new office markets that will compete with Rhodes.

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