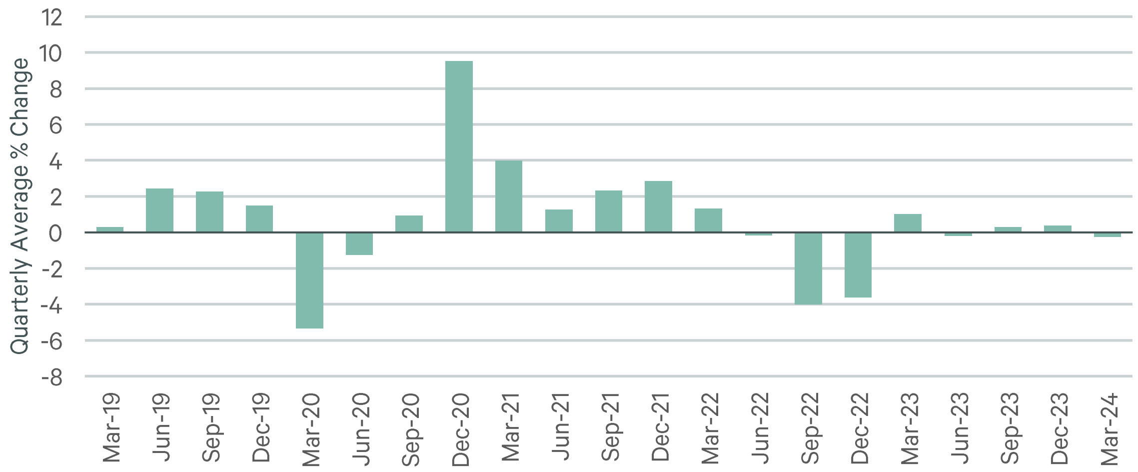
CBRE

Auckland Property Market Overview

INSIGHTS

- While our recent quarterly data indicates that the top of the yield cycle is close, we expect intensified selling pressure on some vendors in coming months. The resulting transactions will provide a clearer indication as to where the remaining gap between vendor and purchaser price expectations will settle.
- Flight to quality continues to characterise the office market. Despite ongoing occupier space rationalisation, expansion also remains a driver of new leasing activity. Due to differing impacts from new supply and occupier commitments, Prime office vacancy improved in the CBD but increased in the suburban markets.
- Retail centre rent growth is decelerating as the inflationary impetus wanes and trading conditions become more challenging, with sub regional centre rent trends tipping into negative territory this quarter.
- Industrial vacancy is under upward pressure due to an active supply pipeline and moderating demand. Industrial rent growth momentum has weakened, with market rents essentially stable during the past two quarters after a 35% to 45% increase, respectively, for the Secondary and Prime sectors.

Weighted Average Office, Retail, Industrial Capital Values – q-o-q % change



Market Indicators

Market Sector	Stock (sqm)	Vacancy (%)	Net Face Rent ($/sqm)	Incentives (%)	Yield (%)
Prime CBD Office	781,689	9.0	350 - 900	8 - 21	5.20 - 8.80
Secondary CBD Office	658,386	20.6	200 - 575	12 - 25	6.70 - 9.50
Prime Industrial	6,270,993	0.6	180 - 270	2 - 6	5.10 - 6.30
Secondary Industrial	7,462,018	0.5	110-220	2 - 6	5.20 - 7.00
Prime CBD Retail			1,100 - 5,000	1 - 3	5.70 – 7.30
Major Regional	301,473	1.6	700 - 2,850	4 - 6	6.80 - 7.30
LFR Centre	490,571	0.8	180 - 550	4 - 6	7.00 - 7.80

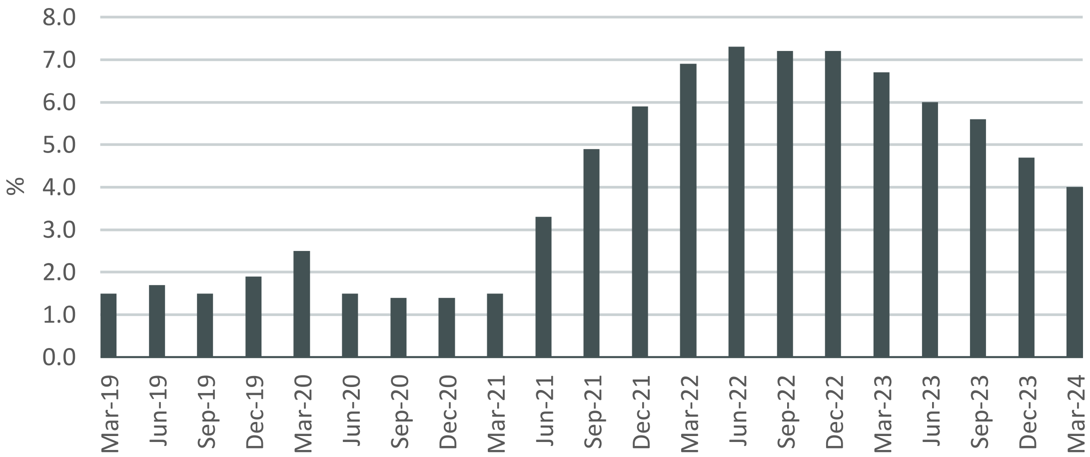
Economy

The RBNZ continues its fight against inflation. The diagnosis in the last two years was clear: mounting pressures were positioning the inflation rate way outside its desired target of 1%-3%. The medicine prescribed by the RBNZ was also obvious: monetary tightening via an aggressive dosage of high OCR to tackle a febrile economy and bring inflation down to non-threatening levels; especially domestic-generated inflation.

As with any prescribed medicine, there are also some side effects. One of them is recession. The New Zealand economy is clearly in recessionary territory. Out of the last five quarters, four registered negative GDP growth, clearly showing a double-dip recession. So far, headline inflation has been consistently slowing down and the unemployment rate has been rising. The inflation rate in Q1 2024 was 4.0%, coming down from 4.7% in Q4. However, the non-tradable inflation component remained highly sticky. Despite this, the medicine is revealing its effect, running slowly through the system, taking the excess steam out of the economy. The effects of the RBNZ's tightening monetary policy are having a clear impact on aggregate demand through weaker consumption by households and lacklustre private investment. Both the market and the RBNZ continue to forecast subdued economic conditions for the rest of 2024.

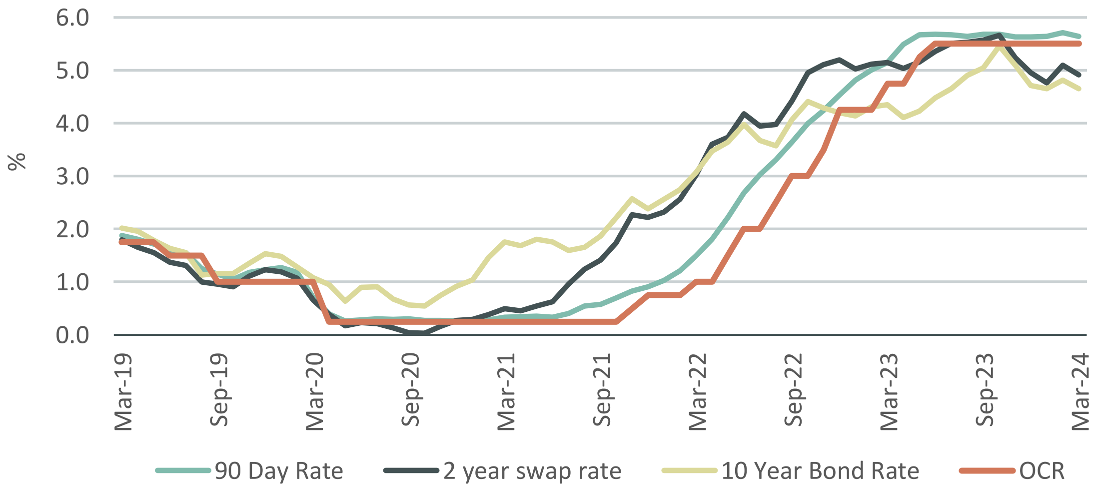
After increasing the OCR by 525 basis points from late 2021 up to May 2023, the RBNZ pivoted to a 'high for longer approach', letting the cycle run its course. Expectations of further OCR rises dissipated as Q1 2024 unfolded. However, the Q1 CPI data will be somewhat concerning for the RBNZ. Domestic inflation pressures remain acute, particularly concentrated in services sectors. The balance of risks is now tilted towards the RBNZ cutting OCR rates later than August, which until now has been the baseline consensus expectation for most economists. The RBNZ will likely await confirmation from the hard data before it pivots to looser policy, which means rate cuts may not be on the table until November.

Consumer Price Index



Source: : Statistics New Zealand

Interest rates (% pa)



Source: Reserve Bank of New Zealand

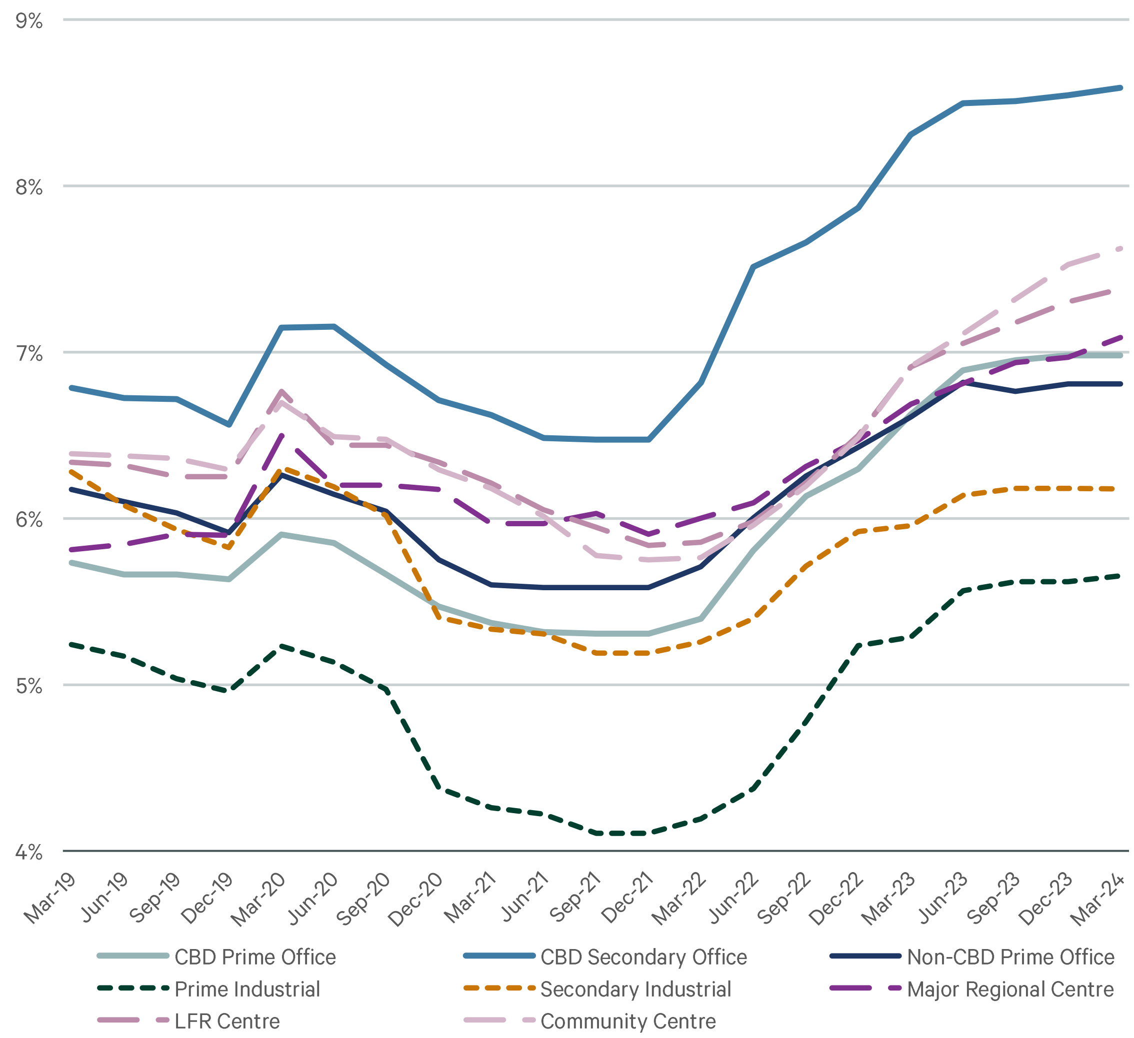
Investment Market

Our Q1 assessments reinforce the view that cap rates are stabilising. Similarly to Q4 2023, we kept market yields unchanged for half of the 18 property sectors we monitor. While our recent quarterly data indicates that we are close to the top of the current yield cycle, we expect selling pressure on some vendors to intensify in the coming months. The resulting transactions will provide a clearer indication as to where the remaining gap between vendor and purchaser price expectations will settle.

In both Q4 and Q1, retail centres were the most affected, with yields across the category pushing out by an average of 8 bps in Q1 following a 13 bps increase in Q4. To an extent this represents a catch up, with retail centre yields moving relatively little during 2022/23 when office and industrial yields moved out more substantially. It also represents the generally thin market for the asset class, compounded by some concerns around seismic issues whose pricing impact can be difficult to untangle. With several centres on, or expected to come on, the market this year, yield levels are likely to clarify in the next few months.

Outside of retail centres, there were some adjustments which show modest movements reflecting specific adverse underlying operating performance issues (occupancy and rent) for some asset classes. This includes Prime CBD retail where we increased yields for less well located spots given ongoing occupancy issues, and C grade office where we sought to increase the yield discount to B grade, especially in the CBD.

Auckland Indicative Yields by Sector



Note: Non-CBD Grade A office yields firmed in Q3 2023 due to some non-market changes including introducing a new building in Newmarket. The market trend in Q3 was still softening in this submarket.

CBD Office Vacancy

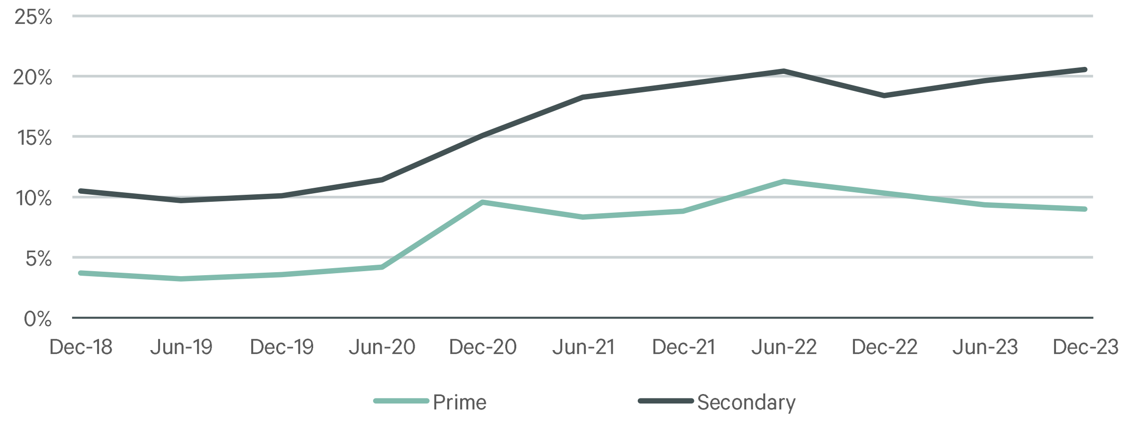
As in the first half of the year, in H2 2023, Prime grade buildings drew occupiers seeking high quality amenities and public transport, leading to a reduction in their vacancy levels from 9.3% to 9.0%.

Due to the limited stock (<200,000 sqm), in Premium Grade new supply can affect the vacancy rate more than they would in grades with larger stock, which occurred in H2 2023. Premium grade vacancy increased from 3.0% to 3.6%, despite strong take-up of 11,553 sqm. In late 2023 Precinct's mixed-use development at 1 Queen was finished, adding 13,900 sqm to supply. The development had strong precommitment, with only 1,500 sqm still available. Deloitte are in, with 7,500 sqm (and naming rights), along with PAG, Mitsubishi and Buffer. Bell Gully have committed to over 4,000sqm and will shift in mid-2024.

Grade A performed well in H2 2023, with positive absorption of ~2,500 sqm. Over 3,000 sqm was taken up in the character building at 131 Queen St. New occupiers here include business consultants Accenture and arts consultants Cultural Partners, who have each taken up a floor, and Montarne Capital Partners, who have taken 500 sqm. 66 Wyndham St has also had a positive second half year, with ICIB taking up over 1,000 sqm, along with Fairway Resolution Trust. This contrasts with the wind-down of FIFA's Women's World Cup operations at 45 Queen St, which generated almost 2,000 sqm of new vacancy, however the football organisation will keep their office on L39 of the ANZ Centre.

Secondary grade vacancy rose in H2 2023, continuing the flight to quality trend, such as lawyers Haigh Lyon, who shifted from B to A Grade while staying on Shortland St and occupying a similar size space. The return of international students that we saw green shoots of in our H1 2023 occupancy survey, has sprouted in H2. NZ Language Centre having taken up ~4,200 sqm across 214-220 and 238-242 and Queen St, while still using their ~1,800 sqm Viaduct Basin premises.

Auckland CBD Office Vacancy



Auckland CBD Office Vacancy Change by Grade

		PREMIUM	GRADE A	GRADE B	GRADE C	GRADE D	TOTAL
Vacancy at December 2023	%	3.6%	10.8%	18.1%	19.8%	33.5%	14.3%
	sqm	6,965	63,435	50,096	60,263	25,070	205,829
Vacancy at June 2023	%	3.0%	11.3%	17.9%	18.4%	31.8%	14.1%
	sqm	5,405	66,200	49,053	58,030	24,268	202,956

CBD Office Rents

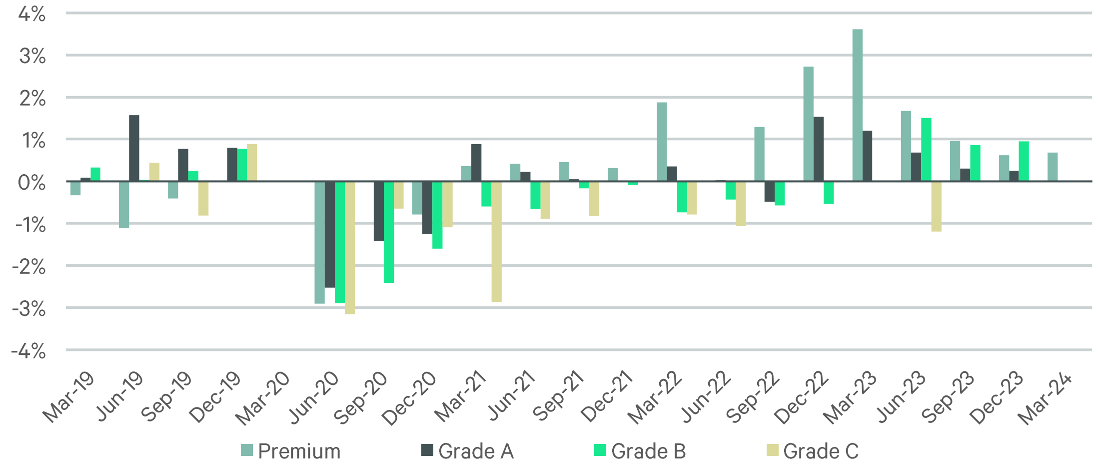
Office rent growth is patchy across the CBD. A couple of Premium grade CBD buildings are showing face rent growth, leading to an uplift of 0.7% in Q1, but for the remainder both rents and incentives remained steady. Grade A rents also remained steady, resulting in Prime rental stability for the third consecutive quarter. Net effective indicative rent for Prime is currently sitting at $477 sqm, up $18 since Q1 2023.

As the cost of fit-out has increased, occupiers have become more hesitant to commit to the CAPEX involved, and this is placing pressure on landlords to come to the party with higher incentives. This is benefiting landlords who are able/willing to contribute, both for new tenants and those re-signing new leases for existing premises.

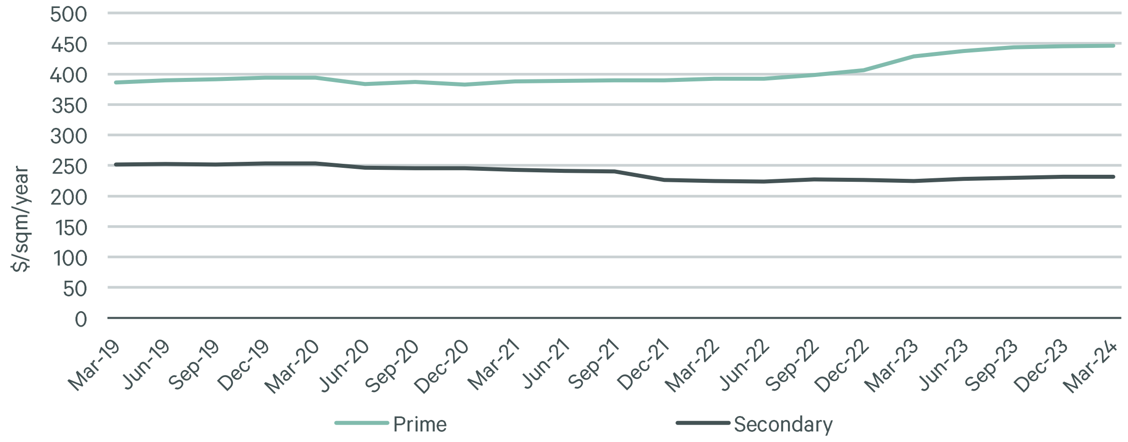
Occupiers are exhibiting a strong preference towards modern workplace fitouts with collaborative workspaces, focus rooms, and large meeting rooms offsetting any increase in staff to desk ratios.

Within Secondary grades rents remained stable, indicating equilibrium between demand and supply. Net effective indicative rent remains at $231 sqm for the second consecutive quarter, having risen $6 psm since Q1 2023.

Auckland CBD Net Effective Office Rents by Grade – Quarterly Change



Auckland CBD Net Effective Office Rents



CBD Office Market Outlook

Vacancy

The occupier flight to quality trend is unlikely to abate over the forecast period, with occupiers focused on getting the best quality space in the right area. As recent trends indicate this can also encompass flight to quality within the Secondary market, not just Secondary to Prime. The vacancy increase forecast for Prime stock is due to the introduction of new developments such as the recently completed 1 Queen, the soon to be completed 50 Albert St, and in 2025, 123 Beaumont St. The strong actual and expected occupier precommitment for these developments will be creating backfill vacancy in existing Prime buildings and draws additional occupiers to those spaces over time. Therefore, we expect the rise in Prime vacancy will wane from late 2025 as supply moderates and occupier moves consume the backfill vacancies.

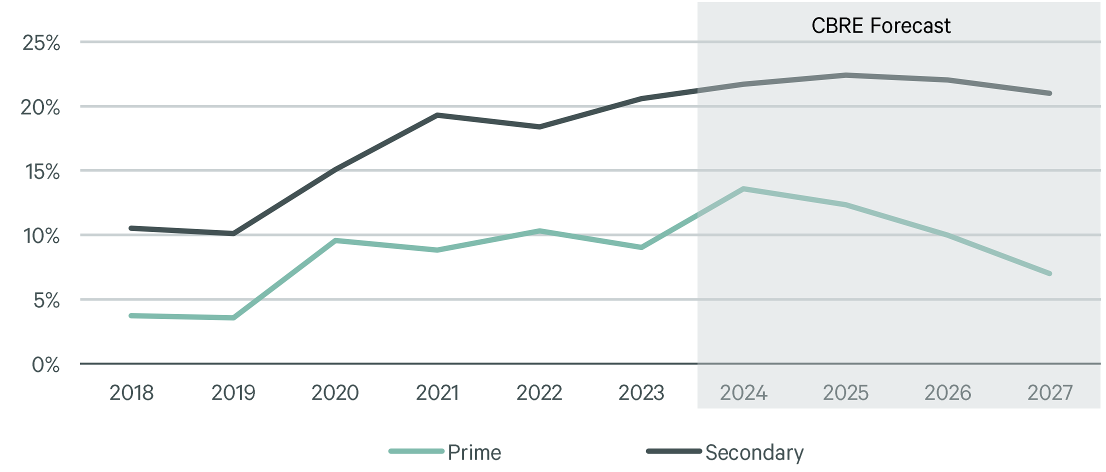
Demand for Secondary grade office stock is not sufficient to consume the available stock in the short term, and we anticipate vacancy levels remaining high, descending as owners remove stock for redevelopment, refurbishment, or re-purposing as residential apartments.

Rent

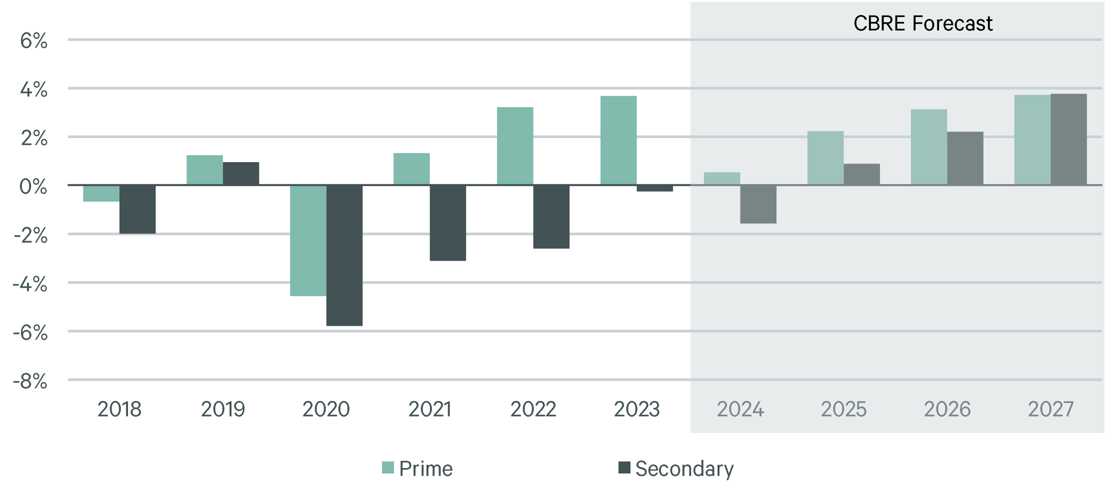
New stock completed in the next four years will meet continuing occupier demand for high quality space. While rents will not grow significantly for Prime grade in 2024, we expect them to recover gradually in the following three years.

In Secondary grade buildings for 2024, we anticipate a drop in net effective rents as occupiers negotiate favourable terms due to the large amount of vacant space available, and the cool economic environment. From 2025 onwards we anticipate stronger rental growth as demand grows on the back of a rising economy.

CBD Office Actual and Forecast Vacancy



CBD Office Actual and Forecast Annual Net Effective Rental Change



Non-CBD Office Vacancy

Prime (or Grade A) vacancies lifted slightly in the second half of 2023 by over 5,000 sqm to 35,000 sqm, or 0.9% to 9.6%. While Grade B kept stable at 9.4%, Grade C experienced a large increase of almost 9,000 sqm of new vacancy, lifting the vacancy rate from 6.8% to 8.1% over the half year. Grade D vacancy was relatively stable lifting only 0.6% to 7.7%.

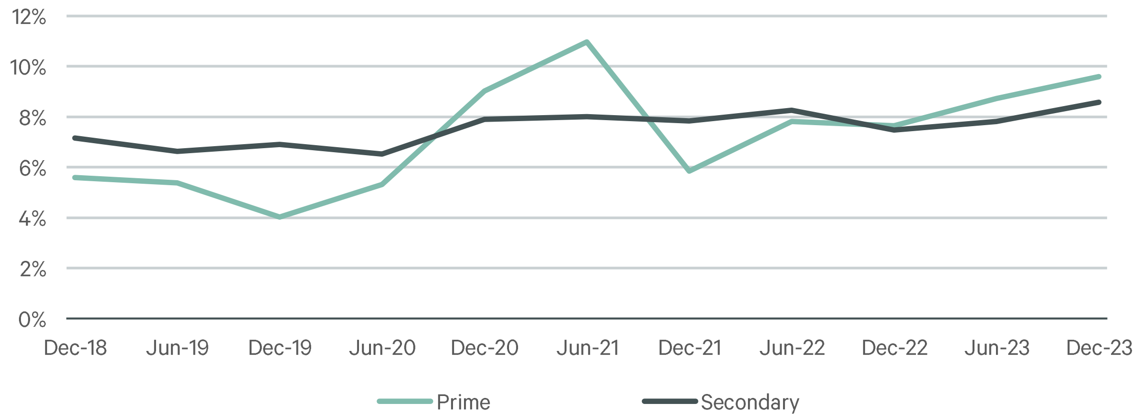
In A Grade, a major contributor to current vacancy is the new Munroe Lane building in Albany. Despite Auckland Council moving in, the building still has both direct- and sub-lease space available totalling 8,200 sqm, as local government looks to trim costs to balance its budget. Elsewhere on the North Shore, IRD took up 3,000 sqm, half of which was vacant, from One (Vodafone), at Smales Farm.

Within Ponsonby, the refurbishment and repositioning of previously Grade C stock into Grade B has worked well for 14 Maidstone St (1,140 sqm) and 202 Ponsonby Rd (1,580 sqm), both of which have been completely taken up in H2 2023.

A noticeable trend in H2 2023 was the shifting of predominantly digital media/advertising companies from the Eden Tce/Newton/Grafton area towards higher amenity precincts – destinations including lower Parnell, Ponsonby Rd, and the CBD – all of which are currently also less disrupted by the CRL project.

In Mt Wellington, backfill vacancies in Grade C increased as Geneva Finance left 1,500 sqm in Pacific Rise for the newly completed (and very striking) 3 Te Kehu Way. With the election over, the Electoral Commission has vacated their CBD and suburban locations, including 1,500 sqm in Greenlane's Millennium Centre.

Auckland Non-CBD Office Vacancy Change by Grade



Auckland Non-CBD Office Vacancy

		GRADE A	GRADE B	GRADE C	GRADE D	TOTAL
Vacancy at December 2023	%	9.6%	9.4%	8.1%	7.7%	8.8%
	sqm	34,717	51,583	54,188	12,586	153,074
Vacancy at June 2023	%	8.7%	9.4%	6.8%	7.1%	8.0%
	sqm	29,463	51,725	45,873	11,688	138,749

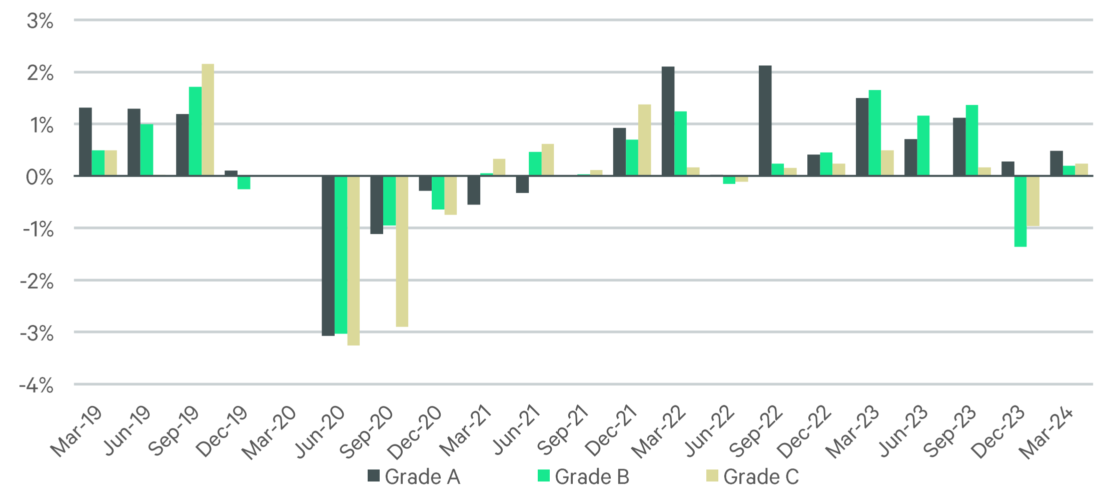
Non-CBD Office Rents

The quarterly change graph to the right paints a positive picture for Non-CBD office rents for Q1, with rents for A grade up 0.5%, B grade up 0.2% and C grade also up 02.%. However, these headline figures do not reflect the increasingly differentiated rent dynamics of suburban Auckland, as rents in broader precincts are influenced by supply, stock and demand conditions.

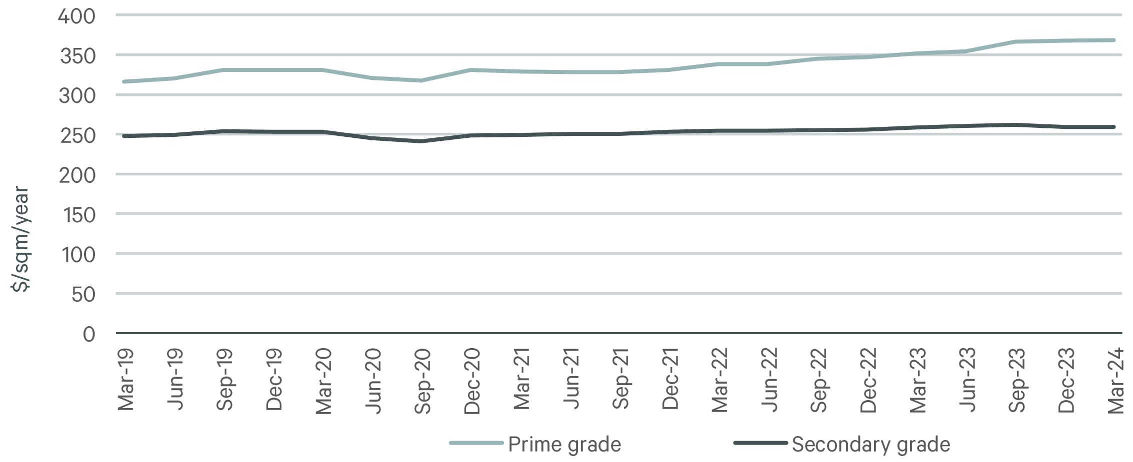
Near CBD and Southern Auckland precincts continue to show positive rental trends (through increasing face rents with incentives remaining stable). Net effective indicative rents for grade A space Newmarket are currently at $436 psm p.a., while grade B space is at $293 psm p.a. In comparison, other precincts close to the city (including Parnell, Ponsonby & Grafton) can command net effective indicative rents of $398 psm p.a. for grade A space, while grade B spaces are renting for $304 psm p.a. South Auckland rents for better quality buildings benefit from limited high quality stock, focusing occupier demand that is resulting in increases. Net effective indicative rents for grade A space are sitting at $339 psm p.a. in Q1 2024, while grade B space now commands $266.

Downward rental pressure is emerging on the North Shore with increasing vacancies due to both new supply and contracting occupier footprints. This is most evident at the higher quality end of the market with shrinking footprints from several corporate and government occupiers who have gravitated to the area (mainly to Albany) pre-Covid, as part of hub-and-spoke operating models that have lost some of their rationale post-Covid. Most of this rental pressure is emerging through higher incentives, and once this is priced in, net effective indicative rents for grade A space are currently at $328 psm p.a., while grade B space is at $250 psm p.a.

Auckland Non-CBD Net Effective Office Rents by Grade – Quarterly Change



Auckland non-CBD Net Effective Office Rents



Non-CBD Office Market Outlook

Vacancy

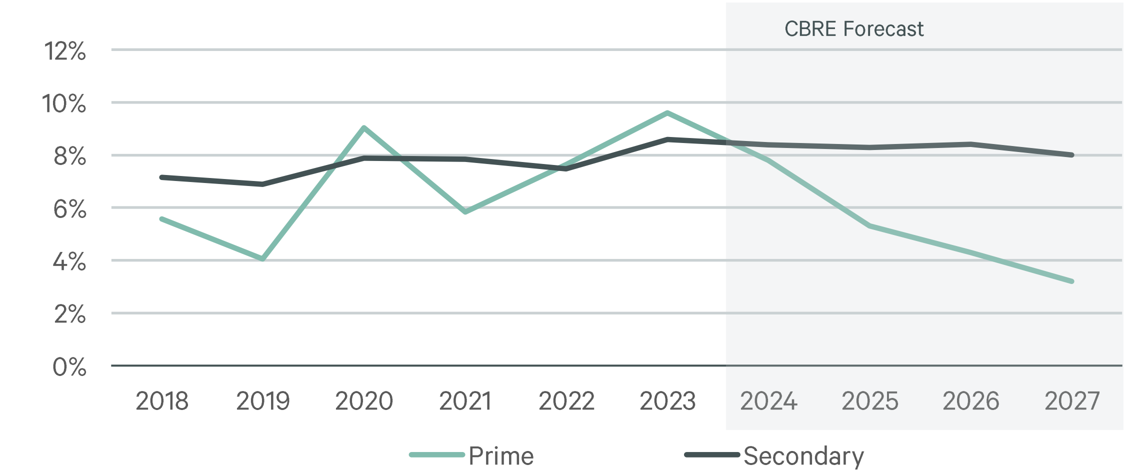
The timeframes of some of the projects in the suburban office supply pipeline continue to push out. Demand from healthcare remains a major factor in some projects such as those in Marewa Rd, Pacific Rise, and Manukau Station Road. Given the moderate supply pipeline, we expect Prime vacancy to improve steadily through to 2027.

Within Secondary grade stock, vacancy levels are expected to hover around the 8% mark, reflecting a mixture of negative absorption and stock losses with some periods benefitting from the interplay of low supply in the higher grades to drive tenant losses, combined with improving economic conditions.

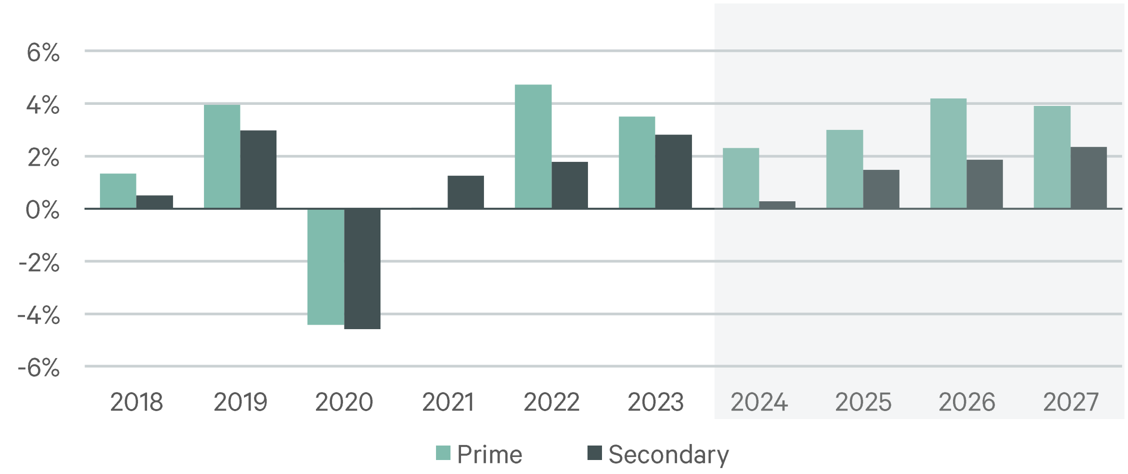
Rents

On the back of declining vacancy we anticipate Prime rents to increase by ~2% in 2024, then lift by 3% - 4% annually from 2025 - 2027. Secondary grade rental trends will be weak in 2024, and subsequent increases in rents are likely to lag behind Prime grade.

Non-CBD Office Actual and Forecast Vacancy



Non-CBD Office Actual and Forecast Annual Net Effective Rental Change



Retail Vacancy

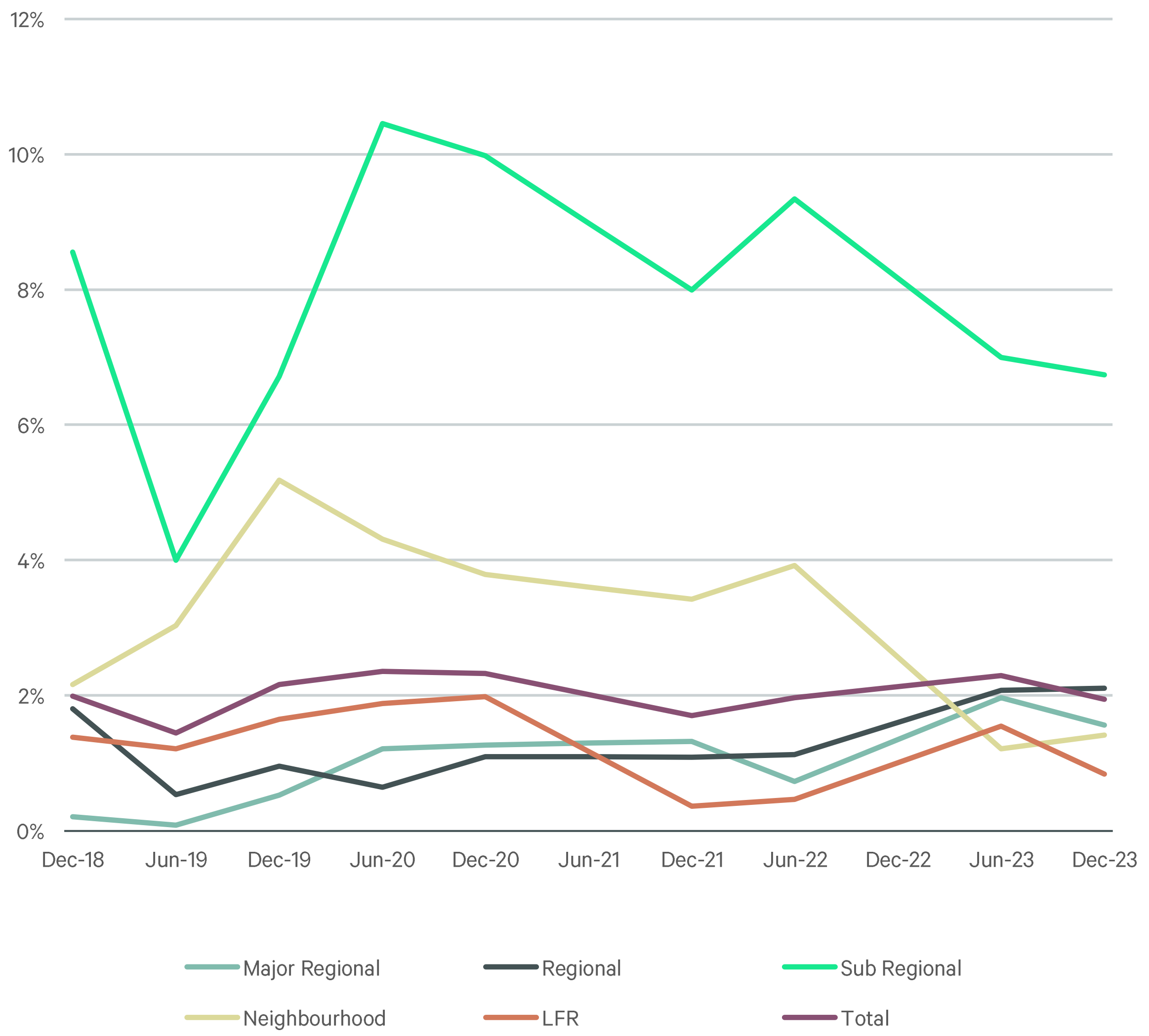
Vacancy levels have dropped for 4 of the 5 centre typologies we monitor, a good result during the current economic climate. The improvement in vacancy levels indicates that landlords are taking a pragmatic approach and working to ensure their centres are bright, lively, and positive.

Vacancy has tended to concentrate in a handful of locations under some significant competitive pressure in their catchments, centres with recent upgrades and activations performing better than those that need refurbishment.

Neighbourhood centres' vacancy levels rose to 1.4% in the second half of 2023; however, this figure is skewed by a small number of older centres having high vacancy levels. LFR centres returned to their usual position in H2 2023, with the lowest vacancy level of 0.8%, having recovered well from their pandemic peak of 2.0% in H2 2020. Major Regional centres also experienced a drop, their vacancy levels now sitting at 1.6% as landlords react to the current market conditions.

Looking forward, 2024 – 2025 will be a period of growth with expansion of Westgate's retail precinct which will include more LFR, an Asian supermarket, and multiple F&B offerings at the northern end of the precinct. In Mt Wellington IKEA's store is due to open in late 2025, with the promise of flatpacks and meatballs along with complimentary LFR offerings to link up the existing Major Regional centre. Auckland Airport's new outlet-focused shopping centre Manawa Bay (currently under construction) is due to open in late 2024 and is already promoting a dozen aspirational brands (including UnderArmour, Converse, Kate Spade, Swarovski, FILA, COACH, & Calvin Klein), which is likely to impact on occupancy rates and rents in other outlet centres in the Auckland region.

Auckland Retail Centre Vacancy

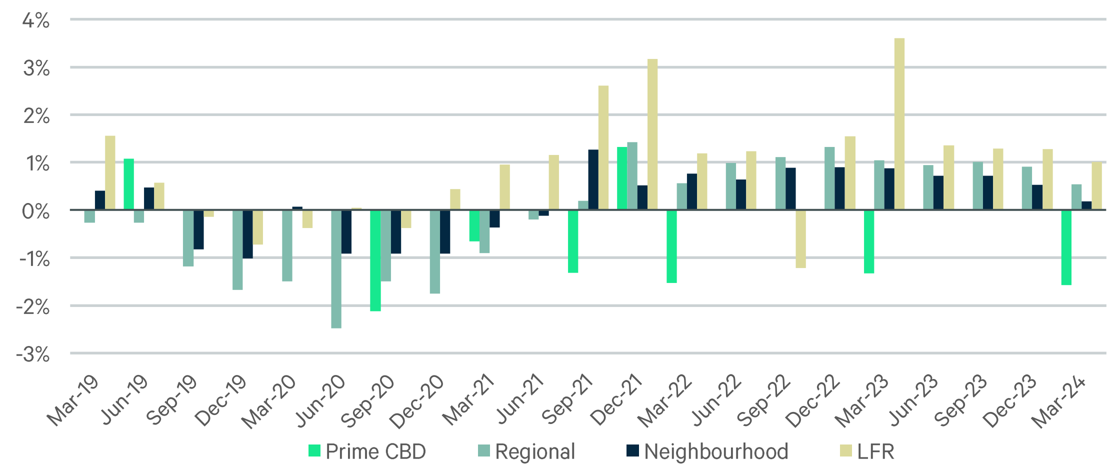


Retail Rents

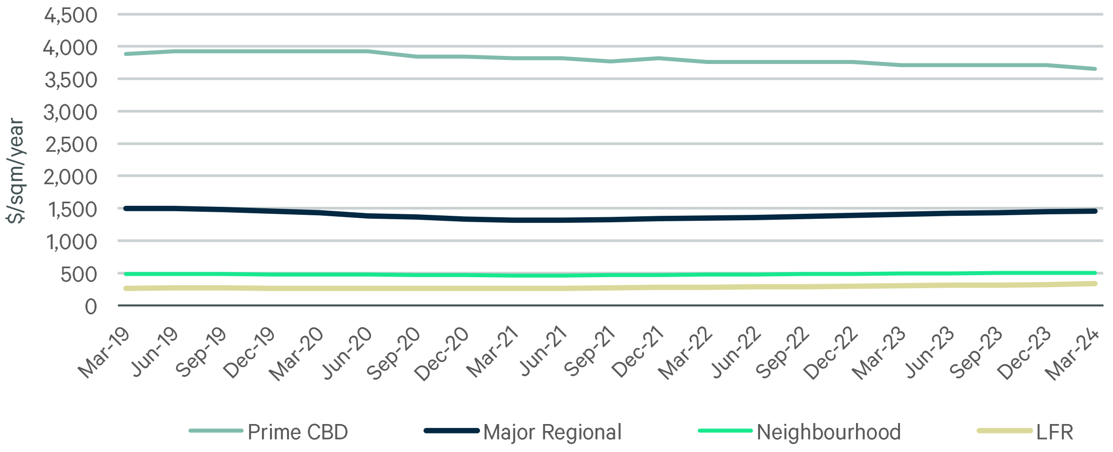
Retail rents show diverging trends. In strip retail, recent leasing in the CBD indicates further downward pressure; most evident in the Fort/Customs St area of the Secondary submarket. In contrast, rents in Newmarket appear to have reached a floor with well trading off Broadway locations (in and around Osborne St mainly) showing some growth.

Retail centre rent growth is also decelerating as the inflationary impetus wanes and trading conditions become more challenging, with sub regional centre rent trends tipping into negative territory this quarter.

Auckland Retail Rents – Quarterly Change



Auckland Retail Rents

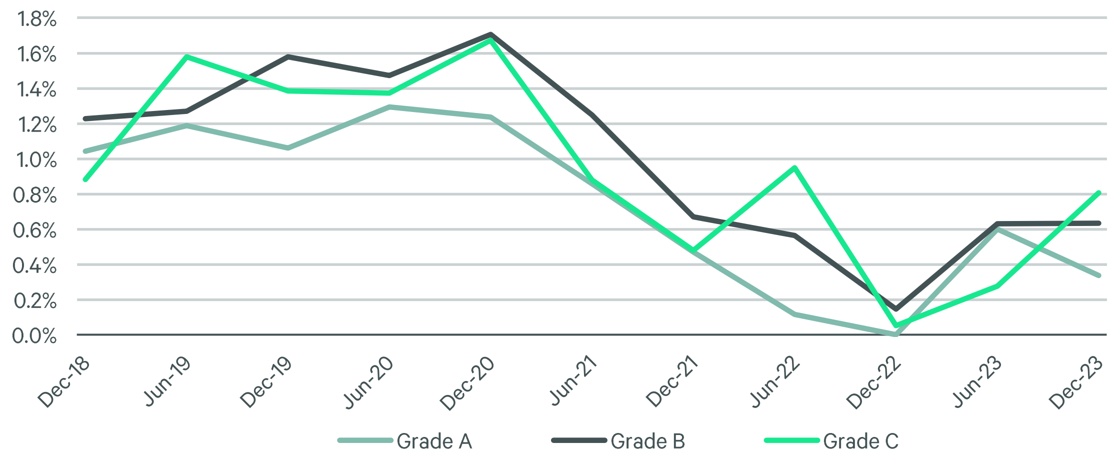


Industrial Vacancy

The vacancy rate remained stable at 0.5% in the second half of the year and total vacant space only increased by circa 3,000 sqm. Grade A shows some improvements since June 2023, vacancy dropping by 16,000 sqm or 0.3%. In contrast, Grade C/D vacancy increased by a much larger 19,000 sqm. This trend is expected to continue in 2024 with a sluggish economy exacerbating volatility in the Secondary market compared to Prime.

Demand remained robust but has moderated slightly from the Covid induced boost of the past three years. Total net absorption was 132,000 sqm in H2 2023, slightly lower than the average net absorption of 136,000 sqm between H1 2020 and H1 2023. The uptake of new developments was a major contributor to Grade A absorption. Although net absorption in the Secondary market was -26,000 sqm, this shows an improvement compared to H1 2023 where net absorption was -66,000 sqm. Turners & Growers' departure from their Monahan Road building contributed a large part of Grade C/D negative absorption and new vacancy.

Auckland Industrial Vacancy



Auckland Industrial Vacancy Change by Grade

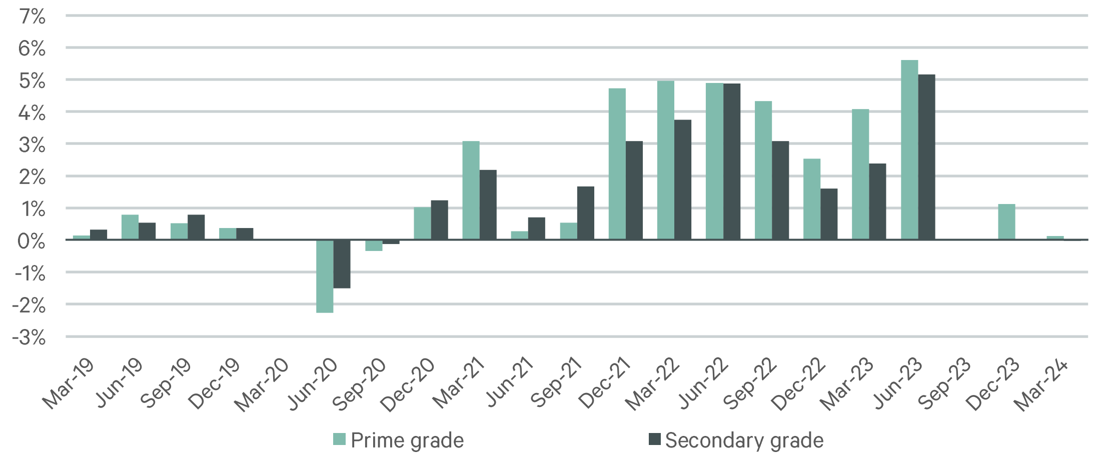
		GRADE A	GRADE B	GRADE C/D	TOTAL
Vacancy at December 2023	%	0.3%	0.6%	0.8%	0.5%
	sqm	21,758	24,647	28,729	75,134
Vacancy at June 2023	%	0.6%	0.6%	0.3%	0.5%
	sqm	37,785	24,589	9,823	72,197

Industrial Rents

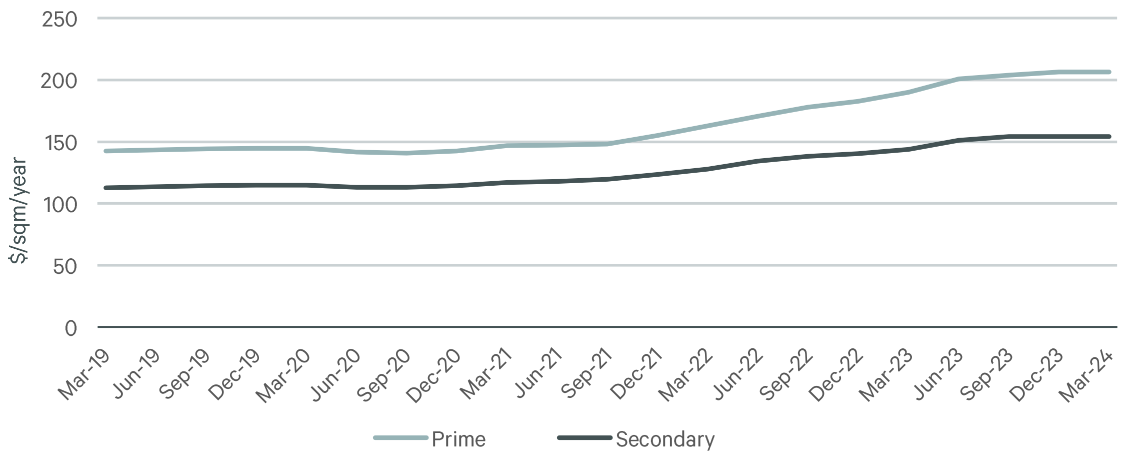
Industrial rents have been largely stable in the past three quarters, which reflects a slowing leasing market. Since Q3 2023, there has been an increase in available space, particularly in the Secondary submarket, even though most of it is not physically vacant. This has led to a more competitive leasing market for landlords compared to the previous two years.

As in Q4, the small increase in Prime rents represents the spread of recent rental benchmarks for new builds into a wider mix of geographic locations. As such, while our methodology shows this as market rent growth, it does not feel so given the higher rent does not represent the achievement of new benchmarks which has been the main growth driver of the past two years. Secondary industrial rental momentum has also dissipated. Prime industrial combined net effective reached $206/sqm/year and Secondary rent was $154.

Combined (office and warehouse) Net Effective Industrial Rents



Auckland Industrial Net Effective Rents – Quarterly Change

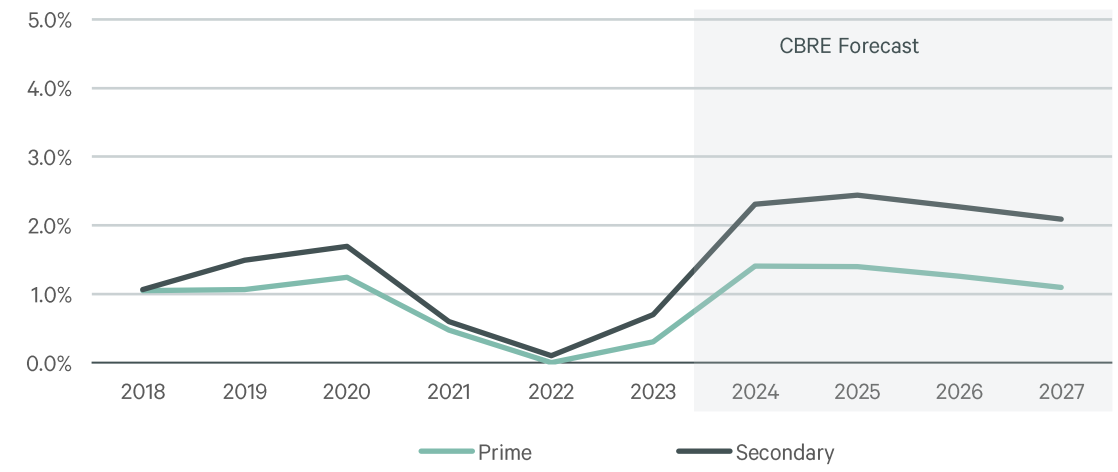


Industrial Market Outlook

Vacancy

After the completion of nearly 300,000 sqm in 2023, the anticipated new supply for 2024 is projected to exceed 400,000 sqm. Amongst the new stock there is not a huge amount of speculative supply with circa 80% pre-commitment. However, as supply chains normalise and economic conditions moderate, we expect that Prime vacancy will increase through to the end of 2024 and stabilise in 2025. The Secondary submarket, known for its historical volatility, is expected to be more adversely affected than Prime in 2024 as the economy weakens. Despite an overall increase in vacancy across the market, its peak is still expected to be lower than the 10-year average.

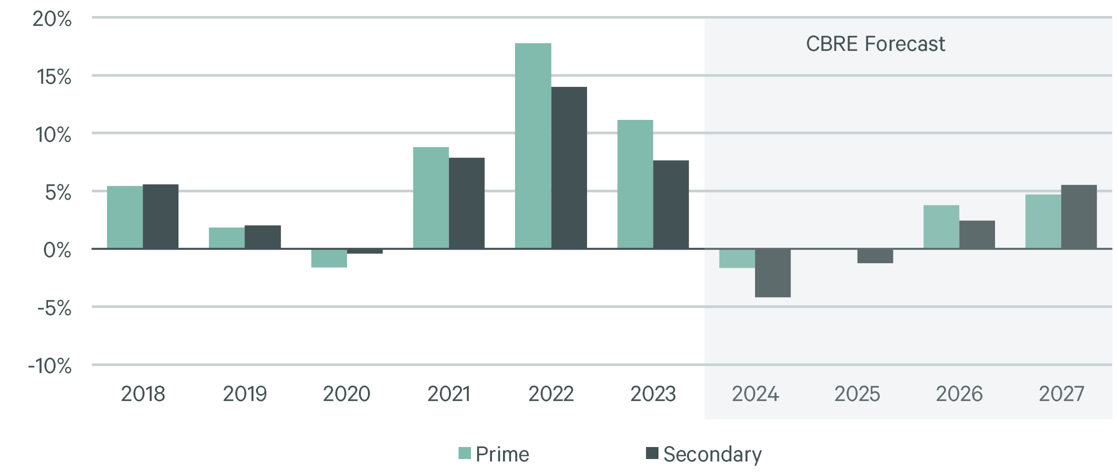
Auckland Industrial Actual and Forecast Vacancy



Rents

A circa 30% increase in Prime effective rents in the past two years to some extent sets up a fall as vacancy increases in the next two years. Recent market information indicates that some new or top-quality buildings can still achieve higher rent benchmarks, while the remaining Prime buildings' effective rents are likely to keep stable or experience slight drops due to higher incentives. However, historical data indicates that rents are more sensitive to economic weaknesses. The outlook for 2024 and 2025 indicates a less sharp but more sustained decline in Secondary rents compared to Prime rents.

Auckland Industrial Actual and Forecast Annual Net Effective Rental Change



Definitions

Office building grades

Premium: Top quality landmark space which is generally the pacesetter in establishing rents and includes the following general attributes: prestige lobby; high architectural merit; prominent location; prestigious occupiers; the latest or recent generation of building services; ample natural lighting; good views and outlook; quality access to and from an attractive street environment; large size - +20,000 sqm. **Grade A**: High-quality modern space including many but not all Premium features. **Grade B**: Good quality modern space with some but not all Grade A features and to a lower standard. **Grade C**: Average quality air-conditioned space. **Grade D**: Older style poor quality space. **Prime**: Combination of Premium and Grade A. **Secondary**: Combination of Grade B and C.

Industrial building grades

Prime: Industrial space used for general warehousing or logistics with stud heights of 9 metres or more, largely column free. Lettable area will exceed 1,500 sqm. The property will be of a high specification and well maintained. The grade encompasses properties from the current generation of design build premises to buildings built over the previous cycle. **Secondary**: Industrial space generally built prior to the mid 1990s, inferior to Prime space in terms of building quality and specifications being lower stud (generally between 6 and 9 metres) and in some cases lacking Capex and having deferred maintenance issues although still providing functional industrial accommodation. Lettable area will exceed 500 sqm.

Rents and yields

CBRE uses the "basket of buildings" methodology to determine market yields and rents. For each property sector covered, a group of representative buildings are nominated and a panel containing senior members of appropriate departments within CBRE convenes to assess the market level of yields and rents for these buildings. Based on this, CBRE's indicative average rental and yield figures reflect our view of the market after considering available appropriate evidence. Yields represent initial yields based on market rents. Rents are net effective. The industrial rents presented are a combined warehouse and office figure.

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