Rents continue to increase despite a strong supply pipeline pushing up vacancy

▲ 19.3%
Overall Vacancy Rate (+230 bps)

▲ 615 AUD/sqm
CBD Prime Gross Face Rents (+2.5% q-o-q)

▼ 35.2%
CBD Prime Incentives (-17 bps q-o-q)

▼ 673 sqm
6-month net absorption

▼ AUD 18m
Sales volume Q1 2024

Note: Arrows indicate change from previous quarter / year.

Key Points

- The Adelaide CBD continued to see steady demand for office space over Q1 2024, with leasing enquiries higher than those seen in 2020.
- The Adelaide CBD overall vacancy rate ended 2023 at 19.3% as per the most recent PCA data. The vacancy rate within newer prime Gen3 assets sat at 10.5% this quarter, owing to the recent completions of two CBD office buildings. These buildings comprise nearly half of the vacant space amongst Gen3 assets.
- Prime gross rental rates ended Q1 2024 at 615 AUD/sqm. This represented a quarter-on-quarter increase of 2.5%. Prime incentives decreased slightly by 17 bps to 35.2% as of this quarter.
- Office sales volume totalled AUD 18 million in Q1 2024. Investment activity remains subdued due to the continued mismatch between buyer and vendor pricing expectations.
- Average prime office yields softened to 7.5%, while secondary yields saw a sharper rise to 9.4%. These values represented quarter-on-quarter increases of +7 bps and +24 bps respectively.

FIGURE 1a: Adelaide CBD Office | Vacancy Rate Summary

Adelaide CBD	January 2024	July 2023	January 2023	H-o-H Change	Y-o-Y Change
Vacancy Rate	**19.3%**	17.0%	16.1%	+230 bps	+320 bps

FIGURE 1b: Adelaide CBD Office | Summary of Prime Market Indicators

Adelaide CBD	Q1 2024	Q4 2023	Q1 2023	Q-o-Q Change	Y-o-Y Change
GFR	**$615/sqm**	$600/sqm	$583/sqm	+2.5%	+5.5%
NFR	**$470/sqm**	$455/sqm	$462/sqm	+3.3%	+1.8%
Incentives	**35.2%**	35.3%	34.5%	-17 bps	+67 bps
Yield	**7.5%**	7.4%	6.5%	+7 bps	+92 bps

$ = Australian Dollar AUD
CBD = Core & Frame markets
Source: CBRE Research

Office Demand

Leasing demand remains positive albeit at subdued levels

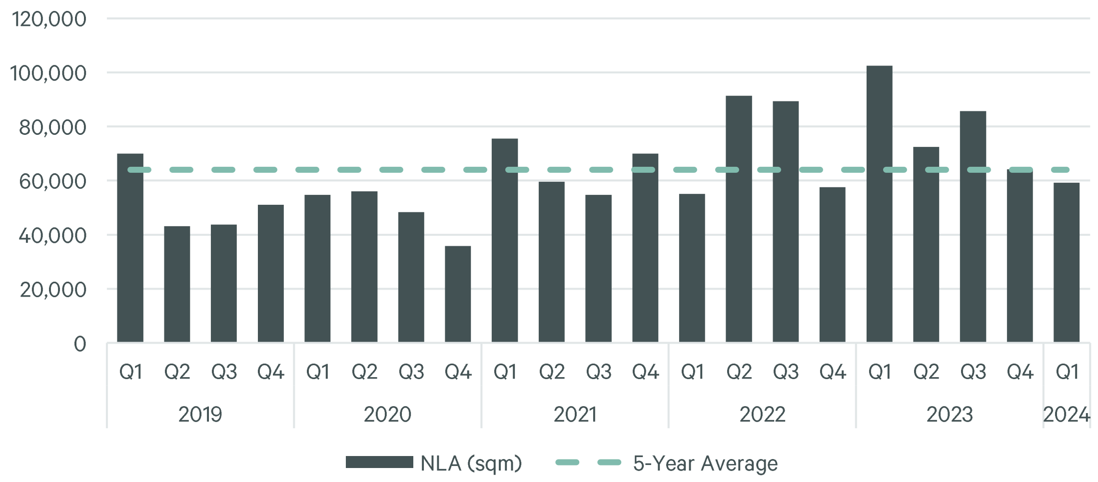
Demand for office space within the Adelaide CBD was strong over 2023, with full-year enquiry levels outpacing 2022. Large enquiry volumes continued in the first quarter of 2024, with enquiries totalling c.59,200 sqm of net lettable area. These levels were higher than those seen in 2020.

Leasing activity continued to demonstrate resilience across Adelaide over 2023. The Adelaide CBD recorded overall net absorption of 673 sqm in H2 2023. This marked the sixth time that Adelaide has posted a positive 6-month net absorption total since COVID began in 2020. Despite absorption levels remaining positive, recorded net absorption was below the 10-year historical average of 2,700 sqm.

Demand across the Adelaide CBD continues to be driven by a flight-to-quality. High-quality stock completed since 2006 is seeing the greatest levels of demand at this time. Prime net absorption continues to outpace figures recorded for Secondary stock.

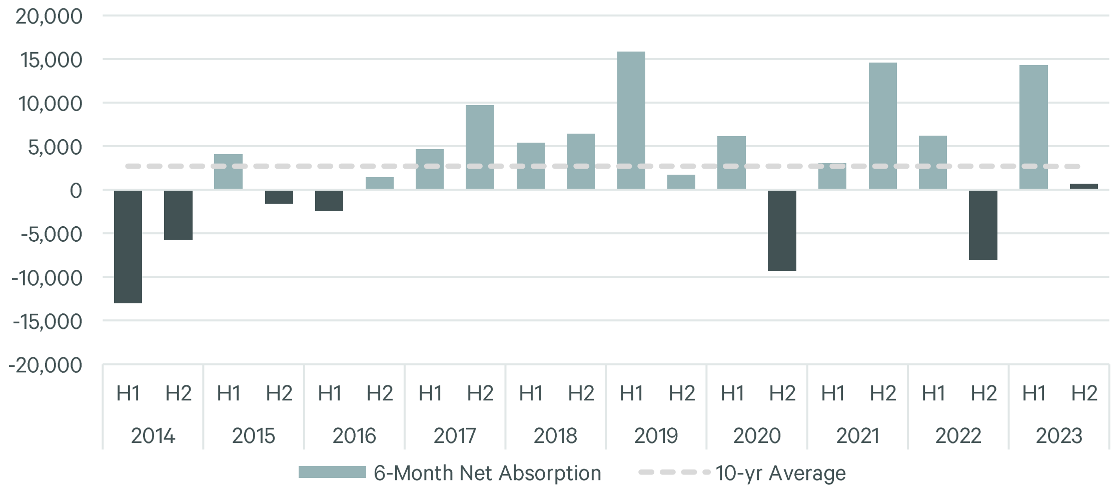
Given the significant levels of new supply delivered to the Adelaide CBD over the past two years and the development pipeline planned for the next five years, occupiers will continue to have opportunities to move into newer space going forward. Flight-to-quality will likely continue driving leasing activity in the Adelaide CBD over the near term and backfilling older vacated space will remain challenging.

FIGURE 2: Adelaide Office | Enquiry Volumes (sqm)



Source: CBRE Research

FIGURE 3: Adelaide CBD Office | 6-Month Net Absorption (sqm)



Source: PCA, CBRE Research

Supply

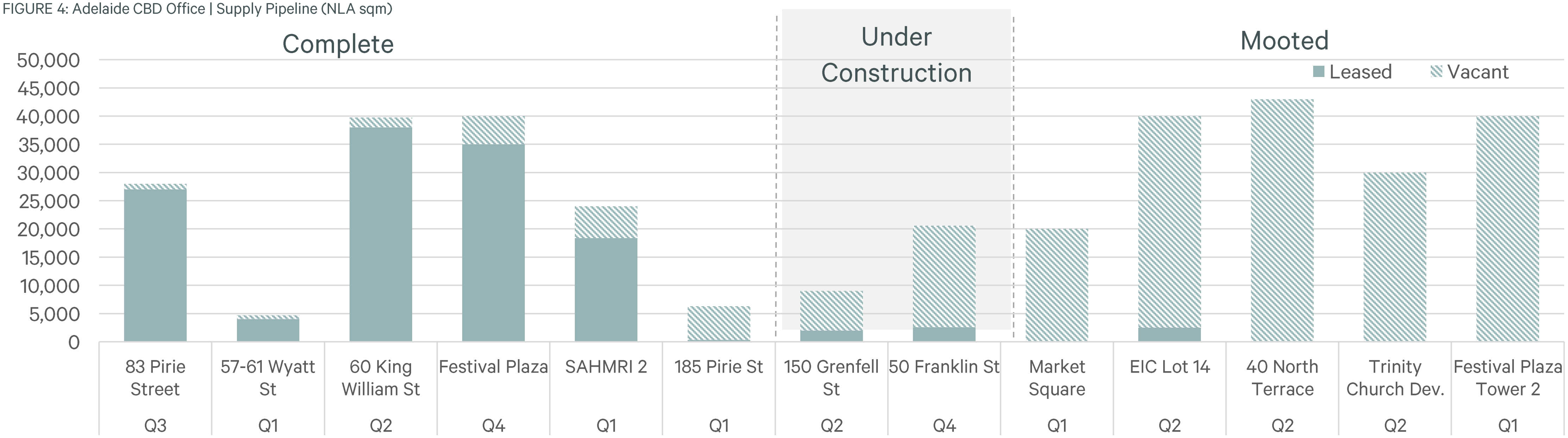
Adelaide's office supply pipeline remains robust

Major office developments delivered in Q1 2024 were SAHMRI 2 (21,300 sqm) and 185 Pirie Street (6,300 sqm). This brought the total supply for Q1 2024 to approximately 28,000 sqm. The SAHMRI 2 office development was delivered this quarter at 75% occupancy. Two new office developments are currently under construction in Adelaide totalling 30,000 sqm, with 150 Grenfell Street expected for completion next quarter. The largest development currently under construction includes 50 Franklin Street (21,000 sqm to be delivered in Q4 2025). As of the end of the current period, this development has 2,600sqm of leased space.

Leasing activity in new developments has been comprised primarily of existing Adelaide occupiers consolidating or expanding into higher quality space within the market. There have not been many new large scale corporate occupiers relocating to Adelaide over recent years. As a result of this trend, the Adelaide market will need to backfill a significant amount of space as new developments are delivered and existing occupiers move into their new tenancies.

Outside of the developments currently under construction, the outlook for future supply becomes more speculative due to challenging development conditions including elevated construction and financing costs. Any mooted projects will likely only begin construction once leasing pre-commitments are obtained.

FIGURE 4: Adelaide CBD Office | Supply Pipeline (NLA sqm)



Source: CBRE Research

Vacancy

Prime vacancy rises as new supply outstrips demand.

Adelaide's CBD vacancy, as per the most recent PCA Office Market Report, softened to 19.3% (direct and sublease), from 17.0% (July 2023).

Direct vacancy was reported at 18.4% and sublease at 0.9%, representing a +190 bps increase in direct vacancy and a +40 bps increase in sublease vacancy over the half. Vacancy for the Adelaide CBD is anticipated to increase further over the next few years due to the strong volumes of new supply currently under construction.

While headline vacancy rates are quite high, occupancy conditions varied greatly by building age. As of Q1 2024, vacancy in prime Gen3 assets (built since 2022) increased to 10.5% from 4.6% in Q4 2023. This was due to the completion of 185 Pirie Street and SAHMRI 2 bringing almost 10,000 sqm of vacant space. Gen2 assets (built from 2006 to 2021) saw the strongest occupancy as of the first quarter, with a vacancy rate of 8.9%. Tenant preferences continue to be concentrated in newer stock (Gen 2 and 3 assets), evidenced by lower vacancy rates recorded in these compared to Gen 1 assets.

The Adelaide sublease market has remained a minor component of the vacancy market with only 7,057 sqm available as per the PCA data. Resilient business performance, high occupancy in the public sector, fitted accommodation options being sought after, and continual increases of employees commuting to the CBD after the relaxation of COVID-19 restrictions are key drivers behind low sublease options.

Gen1: First generation assets built pre-2006 (formerly referred to as 'Old Gen'
Gen2: Second generation assets built 2006-2021 (formerly referred to as 'New Gen'
Gen3: Third generation assets completed within or after 2022 (formerly referred to as 'Next Gen'

FIGURE 5: Adelaide CBD Office | Leasing Market Summary

Market/ Grade	Inventory *Jan 24*	Vacant Space *Jan 24*	Vacancy Rate *Jan 24 (6month Diff)*	Net Absorption *6 months*
Prime	743,853 sqm	163,462 sqm	22.0% (+510 bps)	3,945 sqm
Secondary	819,712 sqm	138,818 sqm	16.9% (-21 bps)	-3,272 sqm
Total	1,563,565 sqm	302,280 sqm	19.3% (+230 bps)	673 sqm

Source: PCA (OMR Jan 2024)

FIGURE 6: Adelaide CBD Office | CBRE Vacancy Tracking

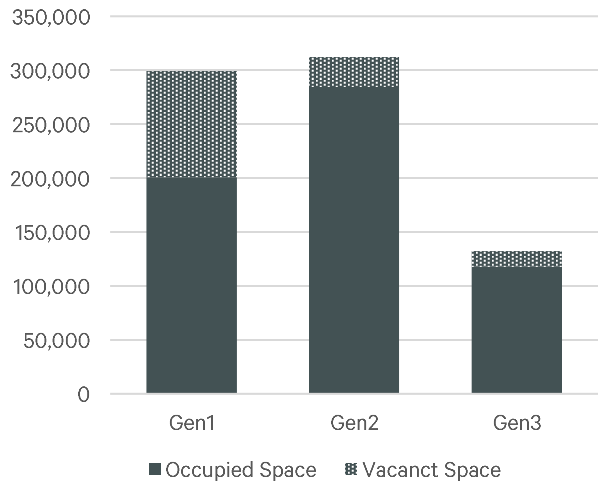
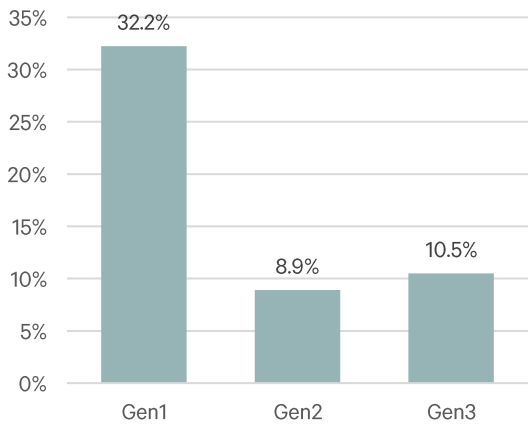


FIGURE 7: Adelaide CBD Office | CBRE Vacancy Rate



Sources: CBRE Research

Rental Performance

Modest rental growth despite rising vacancy

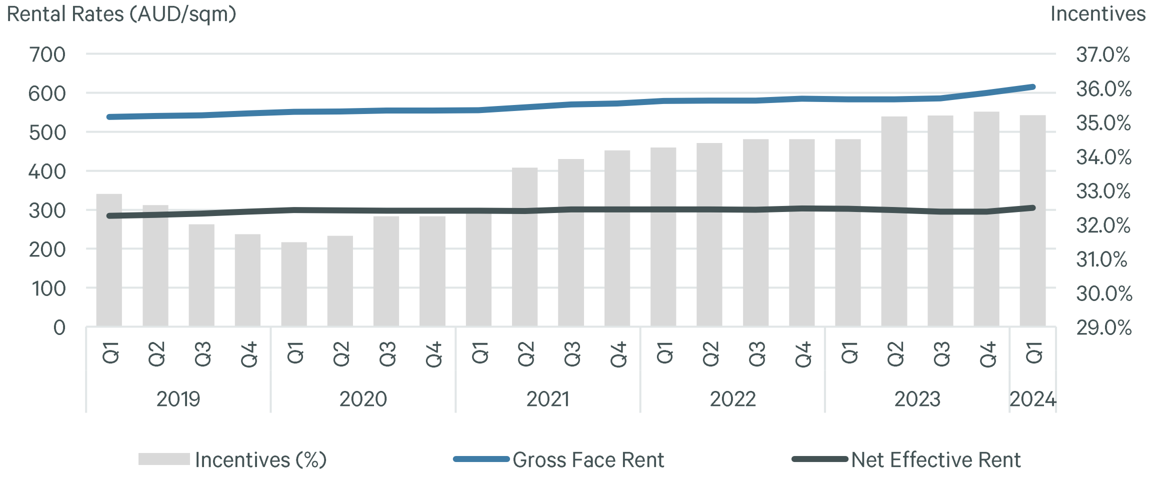
While rental conditions across the Adelaide CBD remained stable throughout the pandemic, this trend shifted in Q1 2024. The market saw some moderate increases to rents to start 2024, specifically in Prime stock.

Prime gross rental rates ended the period at 615 AUD/sqm, increasing by 2.5% quarter-on-quarter. Prime incentives decreased slightly by 17 bps to 35.2% over the first quarter. The combination of rising gross rents and declining incentives has resulted in a 3.5% rise in prime net effective rents over the quarter. Prime outgoings saw no change from the prior quarter, however, they remain 19% higher year-on-year. The yearly growth in outgoings was driven by elevated inflation and building operating costs. Outgoings are expected to increase for the remainder of 2024 which should slow net effective rental rate growth for the foreseeable future.

In the Secondary market these trends differed, where gross rents and net effective rents both declined by 1.0% quarter-on-quarter. A minor decline was also seen in secondary incentives which ended the quarter at 41.4% after falling by 8 bps.

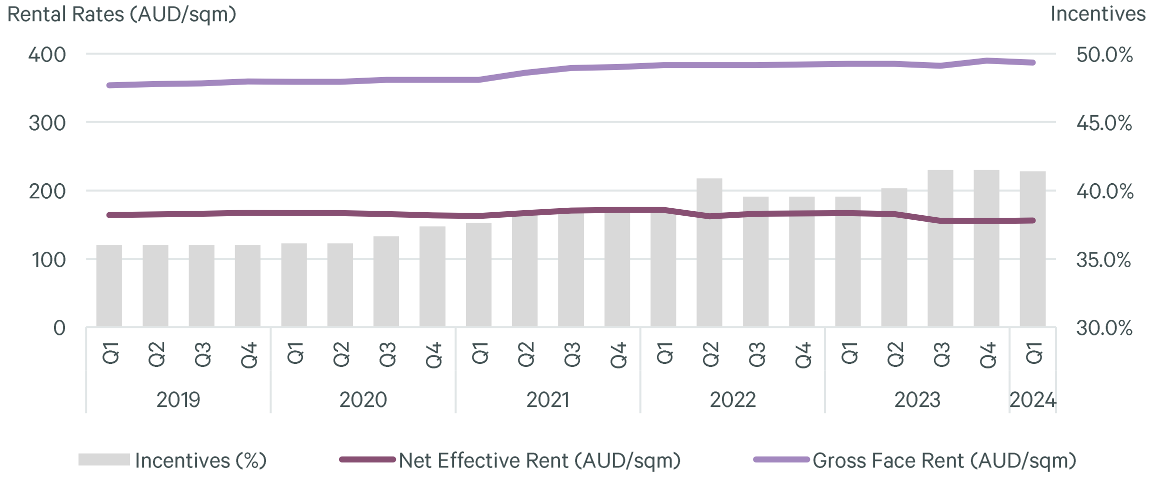
Looking forward, rental rates are expected to continue growing over the coming year. This will be driven by limited new supply coming to the market over 2024 and 2025 as well as nationwide pressures to increase rents in line with inflation. These impacts will be mostly felt in the prime market where demand is driven by flight-to-quality.

FIGURE 8: Adelaide CBD Office | Prime Gross Face Rents, Net Effective Rents, and Incentives



Source: CBRE Research

FIGURE 9: Adelaide CBD Office | Secondary Gross Face Rents, Net Effective Rents, and Incentives



Source: CBRE Research

Investment Market

Sales activity expected to rebound over 2024

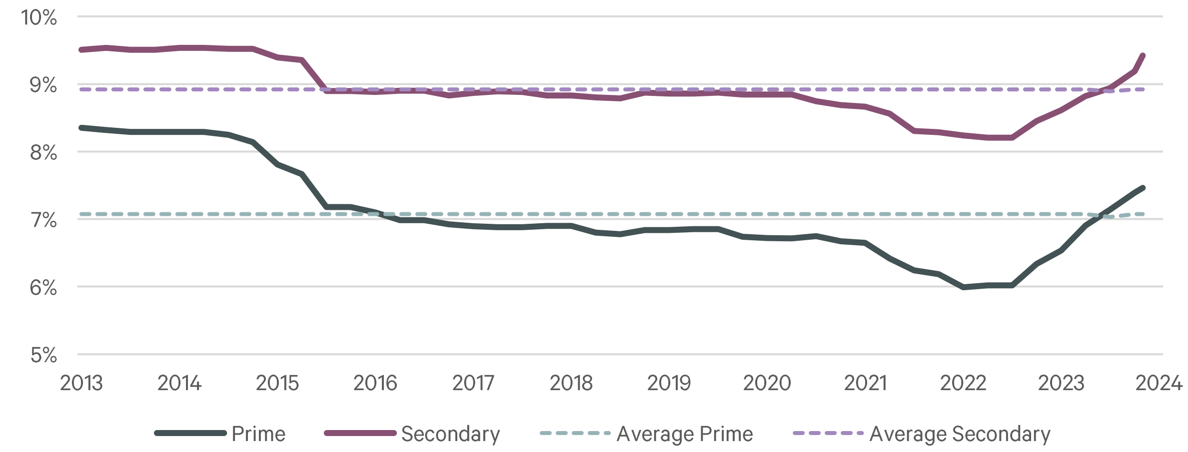
Average prime and secondary asset yields softened quarter-on-quarter to 7.5% and 9.4% respectively. There was a notable difference in yield movement amongst both office grades, whereby prime yields began to stabilise quarter-on-quarter (+7 bps), while secondary yields had a sharper rise by +24 bps.

Office investment sales in Adelaide totalled $18.2 million over Q1 2024. This total represented a decline by 65% compared to the same period in 2023. The assets sold this quarter comprised of 393-395 South Road and 6-10 Gibson Street, which transacted for $9.2 million and $9.0 million, respectively. Both sales were located in suburban geographies.

Despite muted sales activity, it is apparent that investors, namely privates, are willing to purchase office assets in Adelaide if the pricing is right. Regardless, there is a continued mismatch between buyer and vendor expectations at this time and this is preventing sales from closing.

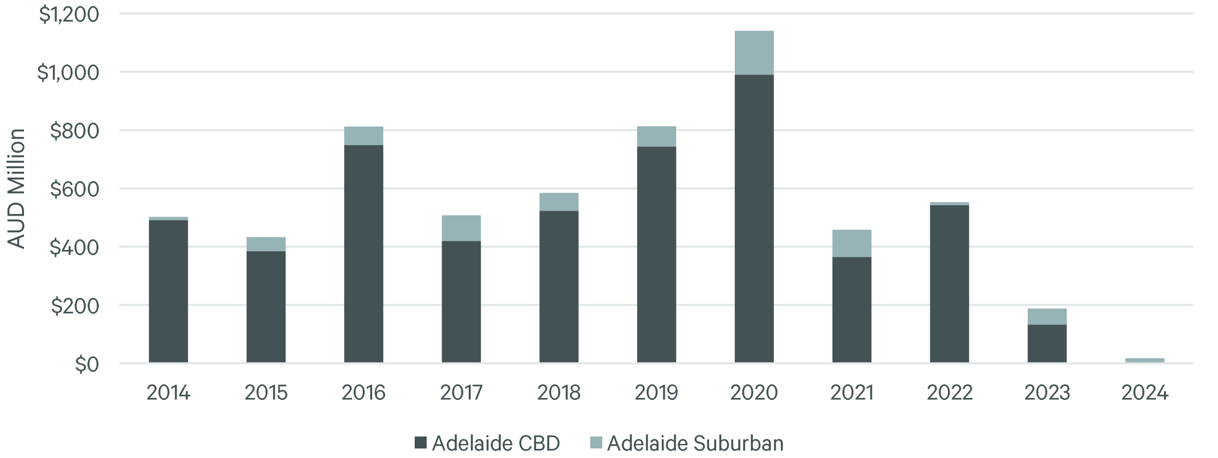
Given that current cash rates have been stable over the first quarter of the year and are forecasted to fall in the second half of the year, current expectations are that sales activity will increase towards the end of 2024 as investors regain confidence in the market.

FIGURE 10: Adelaide CBD Office | 10-year average Prime and Secondary Yields



Source: CBRE Research

FIGURE 11: Adelaide Office | Investment Sales by Submarket (AUD millions)



Source: CBRE Research, MSCI-RCA

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