

RESEARCH & CONSULTING



WOLLONGONG

INSIGHT

SEPTEMBER 2018



GROWTH DRIVERS

DEMOGRAPHIC TRENDS

MARKET OUTLOOK

KEY FACTS

With a current population of 213,841 persons, the Wollongong LGA is expected to **grow to 244,800 persons by 2036**, an increase of 14.5% compared with June 2017.

Gross Regional Product (GRP) was estimated to be **\$13.38 billion** in 2017 for the **Wollongong LGA**, representing 59% of the Illawarra region's GRP.

Office market conditions continue to improve, owing to the **rise of the shared services sector** with tenants seeing Wollongong as an attractive place to do business. However, a lack of large contiguous A-grade leasing options in the market has placed a cap on demand. **Limited leasing options are causing rents to rise.**

Yield disparity between Sydney's metro markets and Wollongong is driving demand for quality stock across the office and industrial sectors.

Tenant migration from Sydney and increased demand from port related industries has seen a large improvement in Wollongong's industrial market.

Rising demand, led by first home buyers continues to drive residential prices across Wollongong which increased by 6.2% over the 12 months to June 2018.

WOLLONGONG IN CONTEXT

Following \$1 billion of investment over the past four years, and a further \$300 million investment in the pipeline, Wollongong is prime to continue its economic transformation. Alongside wider infrastructure improvements, these investments are collectively supporting the growth and transition of the major port City.

Strategically located 80 kilometres south of the Sydney CBD, Wollongong is continuing to show signs of a transition away from its historic heavy industrial roots, highlighted by increasing interest from national and international investors.

In recent years the City has benefitted from a \$200 million upgrade to the Wollongong Central Shopping Centre, a \$120 million redevelopment of Crown Street Mall and \$156 million in spending on expanding both the public and private hospitals. Further investment will flow from The University of Wollongong's (UOW) Strategic Plan which sets out capital expenditure plans which will release in excess of \$300 million within the next four years.

An uplift in the region's key employing industries of health care and education has meant that population growth has stemmed from incoming skilled workers. At the same time, resilient demand from domestic and overseas students attending The University has propelled population growth in younger age cohorts. As the UOW continues to maintain its upward performance within the annual ranking of the worlds universities, sitting in the top 2%,

demand and enrolments are projected to grow.

At an Illawarra regional level the NSW Government, through its final budget before the election, has committed \$101 million in 2018-19 to begin construction of the Berry to Bomaderry Princes Highway upgrade and \$65.6 million to begin construction of the Albion Park Rail bypass.

In addition to allocating millions more to other local transport projects, including \$648.2 million towards the modernisation of rail infrastructure to deliver improvements on the T4 Eastern Suburbs and Illawarra Line amongst other lines, Wollongong is well placed to benefit from improving accessibility.

Whilst these infrastructure projects will have significant implications on a broad mix of industries and the general population, for real estate markets, these projects will ultimately shape and determine the direction and magnitude of demand for expansion and additional space in key markets, be it office demand in the Wollongong CBD or industrial space across the Illawarra region.

FIGURE 1
Data Dashboard
Wollongong in Context



ECONOMY
\$13.38 Billion



POPULATION
213,841 persons



JOBS
79,222

Source: Knight Frank Research, ABS, REMPLAN

ILLAWARRA MIGRATION TRENDS

The Illawarra region has enjoyed solid population growth over the last decade, prompted largely by a pick-up in net overseas migration. Since 2007, population growth across the Illawarra region has averaged 1.1% per annum with 84 new residents moving into the region on average each week. Over the past 12 months, 67% of the region's population growth stemmed from Net Overseas Migration while a further 21% came from Net Interstate Migration (see Figure 2).

Given the region's natural beauty, close proximity to Sydney and access to a large labour market in its own right, the area has attracted significant inbound migration in recent years. Using the recently released 2016 Census, we are able to determine the location of where new residents of the Illawarra region moved from since the 2011 Census.

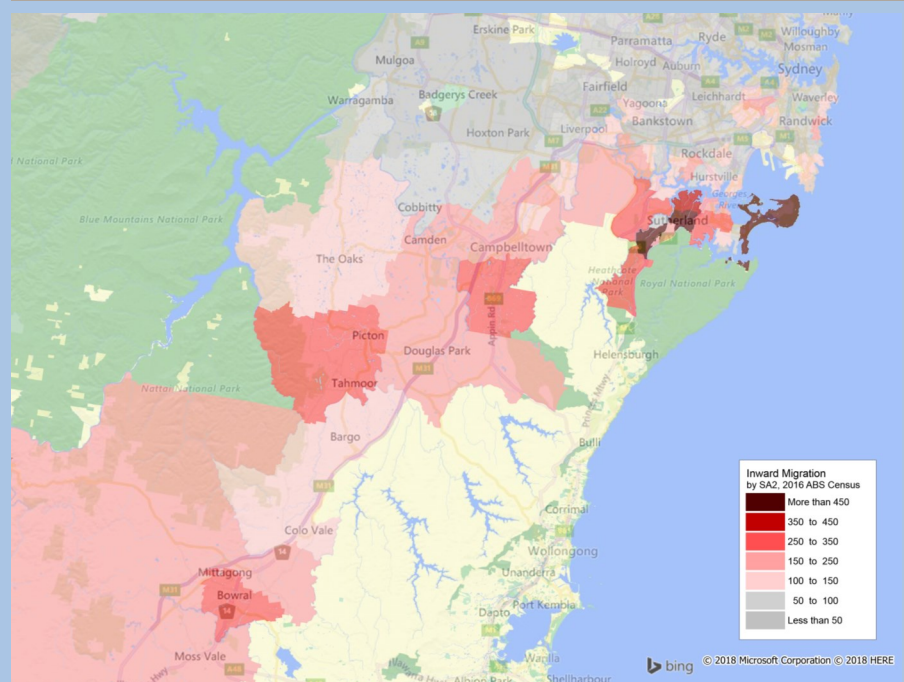
Excluding internal movements within the Illawarra, almost 51,000 persons moved to the Illawarra region between the 2011 and 2016 Census period (gross), 22% of which came from persons moving from overseas.

With median house prices in Sydney approaching \$1 million, Sydney residents are increasingly looking to relocate to the Illawarra region. Despite the Illawarra recording similar house price growth to Sydney, the price differential between the two is \$316,000 (see Figure 3), which is close to historical highs. Driven by

MAP 1

Illawarra Inward Migration

Where New Residents Have Moved From, 2011-2016 Census



Source: Knight Frank Research, ABS

affordability, 22,381 persons (or 44%) moved from Sydney to the Illawarra between the 2011 and 2016 Census, underpinned by movements from the Sutherland Shire, Campbelltown, Canterbury-Bankstown and the Inner West (see Map 1). Elsewhere, 3,064 persons

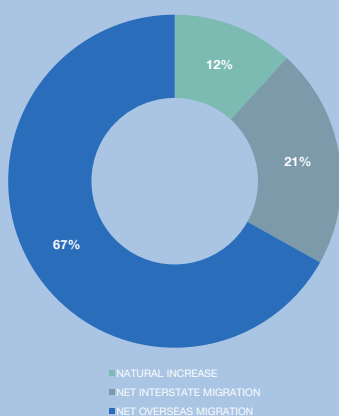
moved from Queensland, 1,594 from the ACT and 1,575 from Victoria.

Taking into account outward migration (persons who left the Illawarra), net migration into the Illawarra totalled 20,740 persons over the five years to 2016.

FIGURE 2

Components of Population Growth

Illawarra Region, 2017

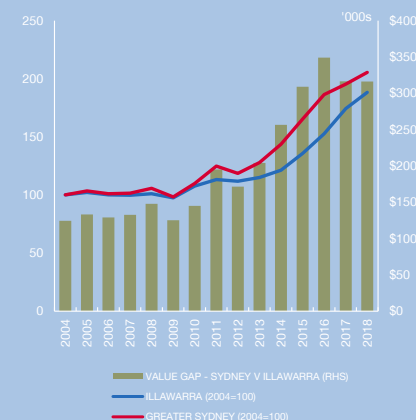


Source: Knight Frank Research, ABS

FIGURE 3

Illawarra v Sydney House Price Index

2004-2018 (2004=100)



Source: Knight Frank Research, APM

FIGURE 4

Top Areas Where People Moved to*

2011-2016 Census

1. Wollongong - East
2. Woonona - Bulli - Russell Vale
3. Balgownie - Fairy Meadow
4. Wollongong - West
5. Figtree - Keirville

Source: Knight Frank Research, ABS
*Excludes internal movements

LOCAL MARKET DEMOGRAPHICS

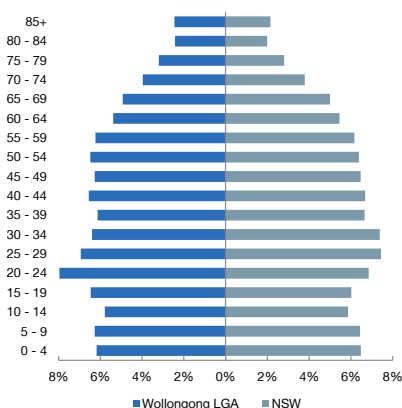
In response to strong local economic conditions and Wollongong's attractiveness as a place to live, population growth in the Wollongong LGA is currently running at its highest level since 2010. Over the 12 months to June 2017, population growth across the Wollongong LGA measured 1.2%, almost double the 0.7% recorded for Regional NSW (NSW excluding Sydney) over the same period. As a result of recent growth, the Wollongong LGA has a total population of 213,841 persons, making it the most populous LGA in NSW outside of Sydney.

Although classed as a regional city Wollongong is seen as the main city and capital of the wider Illawarra region, which has a resident population larger than the ACT and NT states, of over 410,130, as at June 2017.

Given a strong labour market and its affordability, population growth has been aided by Sydney residents relocating south to Wollongong. Over the two most recent Census periods (2011-2016), 10,909 persons moved to the Wollongong LGA from Sydney, up from 8,342 persons over the five years prior (2006-2011).

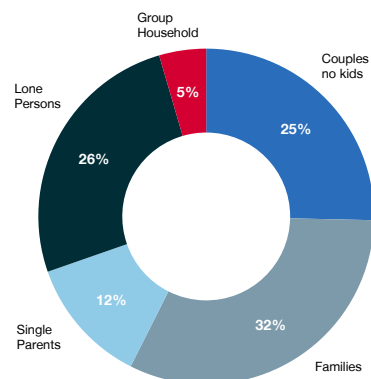
By area, population growth in the Wollongong LGA has been concentrated in a select few pockets, underpinned by land subdivisions in the West Dapto/ Horsley precinct (see Map 2). Elsewhere,

FIGURE 5
Population by Age, 2016
Wollongong LGA v NSW



Source: Knight Frank Research, ABS

FIGURE 6
Household Composition
2016, Wollongong LGA

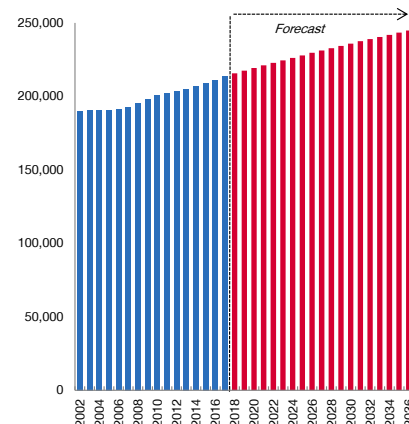


Source: Knight Frank Research, ABS

solid population growth has been recorded at Howards Bay (land subdivisions) and the Wollongong CBD where numerous apartment projects have been launched in recent years.

Looking ahead, strong population growth is expected to continue. Although house price growth in Sydney is showing signs of moderation, wages growth nationally

FIGURE 7
Wollongong LGA Population
Growth Projections 2002-2036

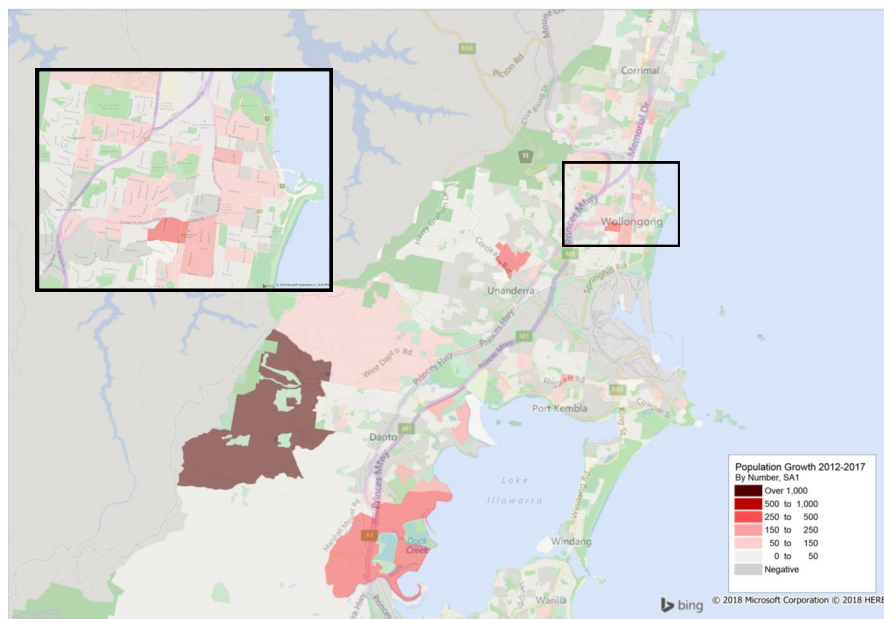


Source: Knight Frank Research, NSW DP&E, ABS

has been weak and it is expected that a greater volume of Sydneysiders will relocate to Wollongong driven by its affordability and proximity to Sydney. Drawing upon NSW Government projections, the population of Wollongong is expected to grow by 14.5% between 2017 and 2036, at which point 244,800 persons are expected to reside in the Wollongong LGA.

MAP 2
Illawarra Population Growth, 2012-2017

By SA1 Region



Source: Knight Frank Research, ABS

OFFICE MARKET

Office market fundamentals continue to improve

Office market conditions in Wollongong remain strong, supported by solid local economic fundamentals which has prompted growth in the number of businesses and local jobs. Over the 12 months to June 2017, an additional 76 white collar businesses begun trading in the Wollongong CBD (Wollongong East & West SA2 regions), representing growth of 3.5% over the period. The rise of the shared services sector is also becoming a significant user of office space across Wollongong, given the higher staff retention rates, lower salaries and lower leasing costs compared with Sydney.

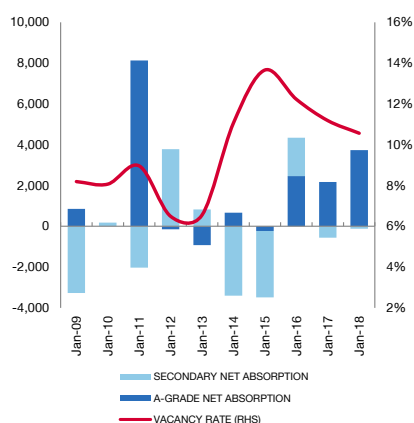
At 10.6%, Wollongong's office vacancy rate is currently at its lowest level in five years, having declined from 11.2% in January 2017. For the prime market, the vacancy rate is materially lower at 3.4% and reflects demand for higher quality buildings. A lack of large contiguous A-grade leasing options in the market has placed a cap on demand. As at January 2018, there were just two options in the A-grade market that were sized above 550 sq m.

Net absorption over the 12 months to January 2018 measured 3,608 sq m, the bulk of which stemmed from the prime market. Reflecting tenant preferences, tenant demand for B and C grade properties contracted over the same period

FIGURE 8

Wollongong Net Absorption

by Grade & Total Vacancy, 12 months to January, 2009-2018



Source: Knight Frank Research, PCA

by 1,134 sq m and 424 sq m respectively. Tenant demand over the past year was driven by SES's occupation of 93 Burelli Street (5,600 sq m), while their subsequent backfill space at 6-8 Regent Street (2,387 sq m) placed a floor on the overall vacancy rate. Given the level of recent tenant enquiries, we anticipate this space will be leased quickly, prompting the need for more office space in Wollongong to facilitate economic development.

Upward pressure on A-grade rents

An improvement in office market fundamentals and flow on effects from Sydney has begun to place upward pressure on rents, albeit grade specific. Given the low prime vacancy rate, prime gross face rents currently range from \$420-\$500/sq m (average of \$450/sq m) while a select number of buildings are achieving rents in excess of \$520/sq m (gross face). With incentive levels ranging from 5%-15% (across all grades), prime effective rents are closer to \$410/sq m. With prime rents pushing past \$500/sq m, new office developments start to become financially viable for developers. For secondary grade buildings, gross face rents currently range from \$300-\$380/sq m.

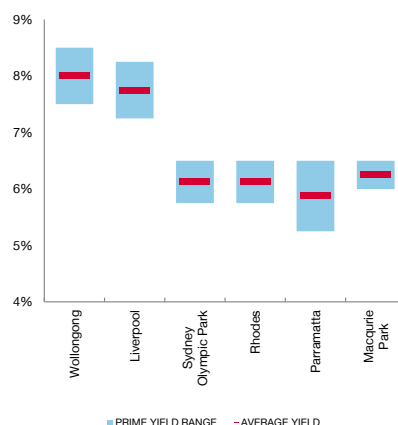
Office supply limited until 2020

In the year to January 2018, gross office

FIGURE 9

Average A-Grade Yields

Wollongong Vs Selected Major Non-CBD Sydney Office Markets, January 2018



Source: Knight Frank Research

supply in Wollongong totalled 3,417 sq m and stemmed largely from mixed use developments (14-18 Auburn Street and 31-41 Crown Street).

With prime rents supporting new development, a pick-up in office supply is anticipated. 47 Burelli Street will represent the next phase of office supply and will become the head office of IMB. The new project which has commenced construction will provide IMB with 6,695 sq m of office space. Beyond this 134-148 Keira Street (5,200 sq m) has also now commenced construction and is expected to complete in early 2020. Other mooted office projects include 29 Denison Street (20,000 sq m) and Langs Corner (Cnr Crown and Kembla Streets) which has recently received approval for a 10,000 sq m office tower. The timing of these projects is unknown and will be dependent on pre-commitments.

Yield disparity driving investment

Given its close proximity to Sydney, strong fundamentals and elevated yield metrics, Wollongong continues to attract interest from national and offshore investors. Recent office sales highlights continued confidence in the Wollongong market.

In 2017, investment volumes (\$5 million +) totalled \$79.4 million with two assets trading over the period. The largest sale to occur was the acquisition of 43 Burelli Street for \$46.1 million to an offshore investor. Sold by Folkstone, the 9,688 sq m building was sold with a 3.2 year WALE (73% of NLA occupied by government tenants) and reflected a core market yield of 7.31%.

The sale of 43 Burelli Street provided further clarity to yield metrics in Wollongong, particularly for upper A-grade assets. Average core market yields are now estimated to range from 7.3% to 8.0% for prime assets while patchy leasing conditions in the secondary market means investors continue to require an elevated risk premium where average core market yields currently range from 8.0% to 9.0%.

Given yield disparity between Sydney's metro markets, there remains headroom for further yield compression in Wollongong. A reduction in incentive levels, coupled with growth in face rents will aid the compression story for well located and quality assets.

INDUSTRIAL MARKET

Fuelled by positive economic conditions, solid market fundamentals in Sydney and Government led infrastructure projects, Wollongong's industrial market is performing well. There has been a measured improvement in leasing and sales activity across the Wollongong industrial market, some of which has stemmed from tenant migration from Sydney, while affordability continues to underpin investment demand.

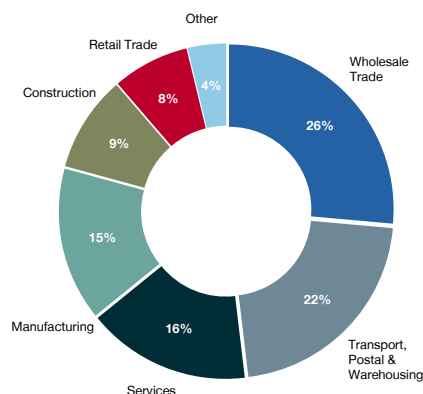
With industrial take-up and locational preferences for businesses heavily influenced by port related activities, industrial space in the Wollongong region is primarily located around Port Kembla, Unanderra and Wollongong (see Map 3). Outside of these areas, industrial activity is scattered, although with a focus along the Princes Highway, to the west and south west of Lake Illawarra.

Wholesale trade and transport dominate

To provide perspective on the types of industrial based businesses that are located in Wollongong, we have looked into the businesses that have amalgamated within the industrial precinct at Unanderra, immediately north-west of Port Kembla.

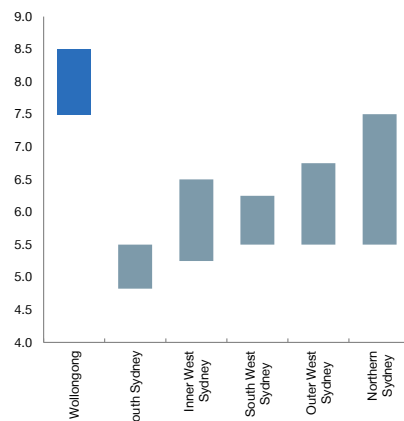
The largest share of businesses within the Unanderra industrial precinct (by

FIGURE 10
Unanderra Industrial Business Profile
By Number, July 2018



Source: Knight Frank Research

FIGURE 11
Average A-Grade Industrial Core Market Yields (%)
Wollongong Vs Sydney Regions, July 18



Source: Knight Frank Research

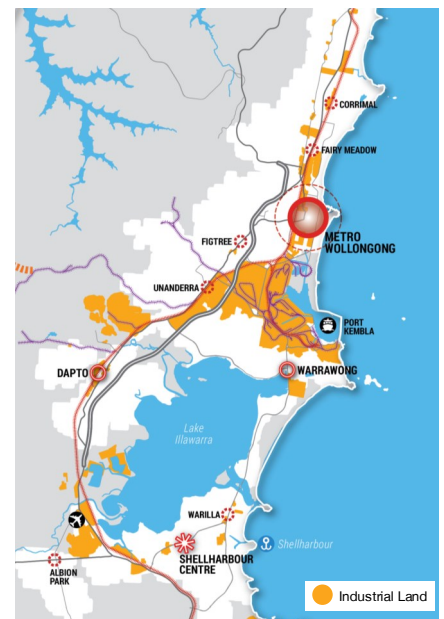
number) falls under wholesale trade and transport, postal and warehousing at 26% and 22% respectively. The presence of businesses such as WesTrac Wollongong, TNT Express, Toll Priority and Fastway Couriers has driven this composition as Unanderra allows businesses to service the southern and northern regions of the Illawarra. Services (17%) and Manufacturing (15%) were the next dominant industries by number in Unanderra.

With the rise of e-commerce coupled with growth in new vehicle transport through Port Kembla, it is expected that transport providers (3PL) will account for a growing share of demand going forward.

Rental growth slow and steady

Moderate industrial rental growth has been recorded over the past 12 months, albeit varying depending on location, access and quality. Broadly, industrial rents in the area range from \$110-\$140/sq m for A-Grade premises and \$85-\$115/sq m for secondary options. With rental growth starting to gather momentum in Sydney, we anticipate there will be flow on effects in Wollongong.

MAP 3
Wollongong Major Industrial Precincts



Source: Illawarra-Shoalhaven Regional Plan 2015

Investment & yields

Investment activity continues to see heightened demand, supported by low interest rates which have prompted owner occupiers into the market while investors including self managed super funds (SMSF) continue to chase the high yields on offer. Limited assets have been brought to the market over the past 12 months which has hampered investment volumes over the period.

With a large pool of buyers vying for a select number of assets, the tightening market has fuelled yield compression. Highlighting recent price growth was the sale of 185 Berkeley Road, Unanderra. The 4,484 sq m facility on a 1.65 ha site was sold in February 2018 for \$9.6 million and reflects a 25.5% premium from when it last sold in June 2016 for \$7.625 million. Anchored by StarTrack Express, the sale reflected a passing yield of 8.6% which represented significant firming from the 10.3% recorded in June 2016.

As at July 2018, average core market yields range from 7.5% to 8.5% for prime assets (assuming 5 year WALE). Prime assets with long term rental security are trading below this range. Secondary assets are trading in the 8.5% to 9.5% range with tenants increasingly favouring prime assets.

RESIDENTIAL MARKET

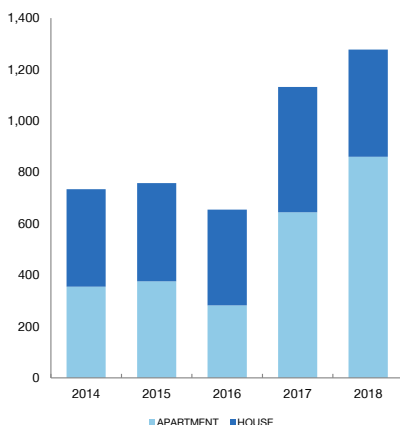
Strong population growth and historically low interest rates has fuelled the Wollongong housing market over the past four years. Since 2014, dwelling prices (house and apartments) across Wollongong have increased by 12.6% per annum on average, well above the 6.3% per annum recorded for Sydney over the same period. As a result of such strong growth Wollongong is now the third most expensive city in Australia

Due to regulatory changes to the banking system in Australia initiated by macroprudential controls imposed by the Australian Prudential Regulation Authority (APRA), dwelling price growth in Wollongong has slowed from recent highs. The largest impacts have come off the back of out of cycle interest rate hikes and increased serviceability requirements. In the 12 months to June 2018, dwelling prices increased 6.2% across Wollongong.

Land market demand

Wollongong's land market has performed strongly in recent years, buoyed by a rise in first home buyer demand and improved lot affordability relative to local house prices. The bulk of Wollongong's land estates are located within the West Dapto Urban Release Area with pockets elsewhere at Howards Bay, Figtree and further north at Bulli. Further south there are significant land releases and developments in Albion Park and Shell Cove. With median house prices

FIGURE 12
Wollongong Dwelling Completions
House & Apartments, Wollongong LGA



Source: Knight Frank Research, ABS
Year to February - latest available data

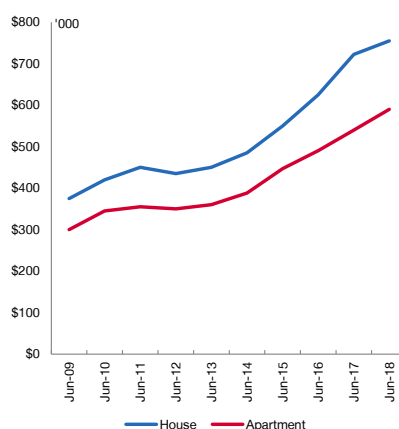
IMAGE 1
Wollongong Lifestyle



approaching \$1 million in Sydney, residents moving to Wollongong from Sydney have provided a key source of demand for new housing and has added to the region's population growth.

Over the past four years, land price growth has outstripped the broader housing market, increasing by 14.7% per annum over the period (APM). With anecdotal evidence suggesting upwards of 35% of land sales were sold to investors, recent regulatory controls has weakened sales volumes and subsequently the growth in lot prices. Over the 12 months to June 2018, land prices increased 5.1% to measure \$415,000.

FIGURE 13
Wollongong Houses v Apartments
Wollongong LGA Price Growth



Source: Knight Frank Research, APM

To highlight lot affordability, we have measured median land prices against median house prices. A ratio above 60% provides less motivation for buyers to purchase lots over established houses (and undertake a knock down rebuild). Despite rises in both vacant lots and house prices, the ratio sits at 55%, well below the 77% recorded in 2011 (APM) and highlights the relative affordability of lots compared to median house prices.

Apartment market continues to be strong

Over the past five years, apartment price growth has averaged 11.0% per annum across Wollongong, underpinned by solid investor demand. Despite house price growth in the area easing over the past 12 months, apartment prices have risen 9.3% over the year to June 2018, well above the 4.6% recorded for houses.

In response to increasing price growth and significant levels of pent-up demand, the number of apartment projects launched has surged in recent years. In the 12 months to February 2018, apartment completions reached record highs with 860 apartments added to the Wollongong LGA market. Despite a surge in supply, apartment rental values across the LGA have increased by 6.7% over the 12 months to December 2017 (latest data), underpinned by solid growth for three bedroom apartments (+9.6%).



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WOLLONGONG INDUSTRY AND LIFESTYLE



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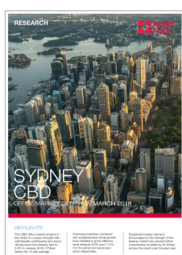
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The Illawarra region includes the four local government areas (LGAs) of Kiama, Shellharbour, Shoalhaven and Wollongong.

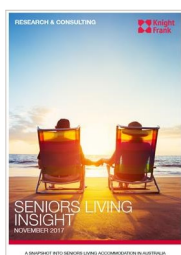
Abbreviations & Glossary:

Core Market Yield: The percentage return/yield analysed when the assessed fully leased net market income is divided by the adopted value/price which has been adjusted to account for property specific issues (i.e. rental reversions, rental downtime for imminent expiries, capital expenditure, current vacancies, incentives, etc.)

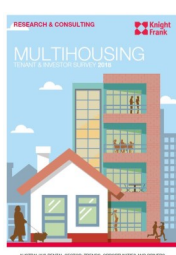
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