AUSTRALIAN
HORIZON

Knight Frank

Will 2024 yield a superior vintage?

Your guide to the future of the Australian property market

1st edition	2024

knightfrank.com.au/horizonreport

The *Horizon Report* sets out our views on Australian real estate, taking you on a journey through the macro context underpinning investment performance, with sector specific insights across office, industrial, alternatives and residential markets that shed light on the path to performance in 2024 and beyond.

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How we chose our cover

In our quest to forecast the future of the real estate market in 2024, we posed a provocative question: Does this year show any signs of improvement? Our discussions revolved around the rich tapestry of history and progress. We drew parallels between the evolution of real estate and the venerable art of winemaking, likening each year to a unique vintage remembered for its distinct character and quality.

Collaborating with our creative agency, Studio Riz, they were inspired by our report's title, 'Will 2024 Yield a Superior Vintage.' Embarking on a creative journey, they visualised cities as if captured in the timeless elegance of a wine bottle. This imaginative leap took us from the concept of wine ageing in bottles to the romantic imagery of pirate ships carrying treasured old wines. It eventually led to the whimsical idea of miniature ships meticulously crafted inside a bottle. In this spirit, Studio Riz envisioned a collection of miniature buildings from Australian cities, encapsulated within glass bottles, symbolising both preservation and timelessness.

Employing the latest in AI image generation tools, Studio Riz brought this concept and the other images in the report to life. We also extend our gratitude to them for their role in shaping the new *Horizon Report* branding and designing this inaugural report. Their work not only captures our vision but also propels us into a future where each year is cherished, like a vintage, for its unique contribution to the evolving narrative of real estate.

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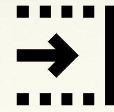
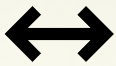
Key highlights

Based on our research here are the *Horizon* top 7 insights for 2024...



End of the NICE era has important implications for investment strategy

Low inflation and low interest rates prevailed in Australia for many years, but these conditions have now changed with the prospect of more volatility going forward. Lower rates may yet return, but this is far from assured, and investors will need to strategise for multiple scenarios.

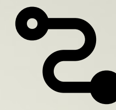


Wide divergence in yield impact depending on perception of risk and rental growth prospects

With higher risk-free rates available to investors, pricing is being reset. However, average movements conceal divergent impacts on pricing which will widen the gap between prime and secondary and between assets with and without strong security of income.

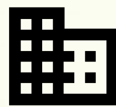
A better vintage awaits: 2024 will be a better year to acquire assets

After a tumultuous period in 2022-23, better value is now emerging for investors. Higher yields will act to reset the market and provide a more attractive entry point, generating the prospect of higher returns.



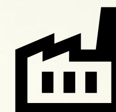
Tilt to core strategies to drive sustained living sectors expansion

Across all regions, investors are seeking greater exposure to alternative sectors and the residential living sectors are at the front of the queue, reflecting a search for greater diversification and more defensive strategies in response to a more uncertain global economic outlook.



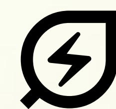
Slowdown in office development to create conditions for future shortages of new supply

Several factors are pushing against new office commencements, and even at this early stage it is possible to identify a potential shortage of prime space later in the decade that will bring tenants to market earlier and drive up the face rents on new developments, aiding market recovery.



Global comparisons show that industrial rents have further to rise

While rents and other operating costs for industrial occupiers have escalated dramatically over the past two years, rents in Australia are by no means out of line with the level of rents in comparable cities globally. Amidst rapid population growth and ongoing supply shortages, rents can be expected to continue to grow.



New sustainability reporting requirements will raise the bar for real estate

New reporting standards mark a huge shift in requirements to directly address emissions across the full spectrum of activities. Businesses will need a report with audit-ready data, requiring them to get on the front foot now with improved processes for capturing and storing information.

Economy

Rates peak nears as population surge boosts growth outlook

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The economy remains on the 'narrow path'

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Rates are now peaking but rapid declines are unlikely

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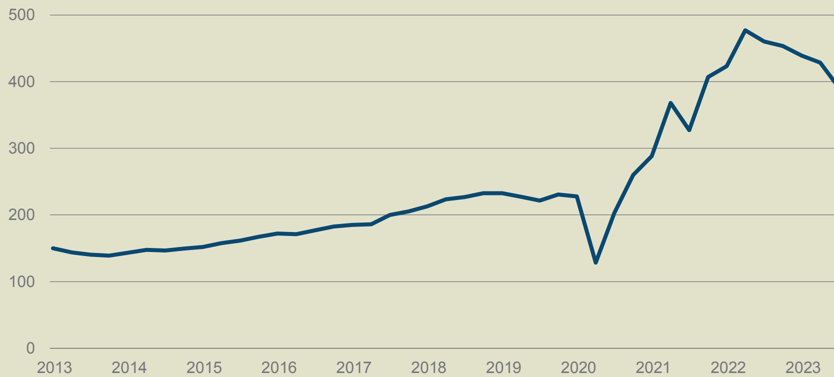
On track for a soft landing

The economy remains on the ‘narrow path’

Job vacancies

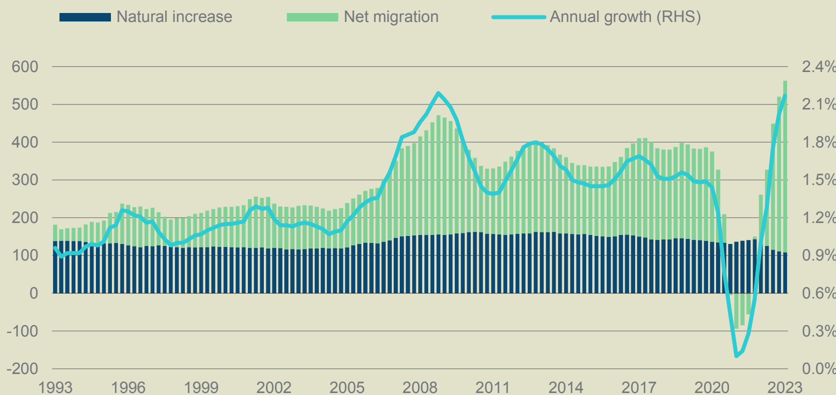
Estimated number of vacancies nationally



Source: Knight Frank Research, ABS

Population growth

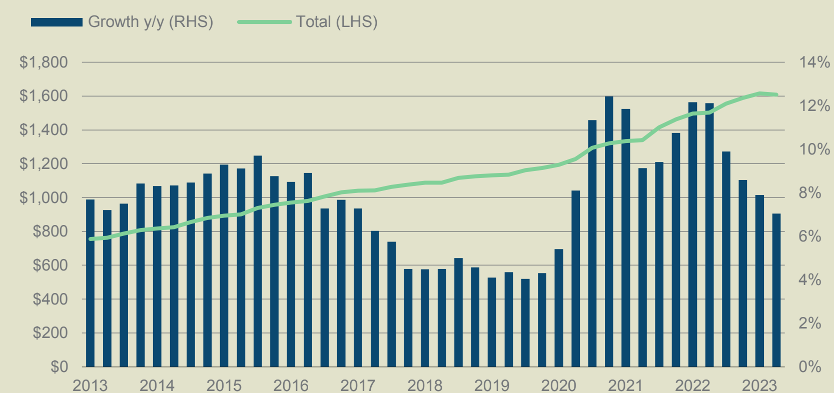
Annual change (thousands) and growth rate (%)



Source: Knight Frank Research, ABS

Rise in household savings

Currency & deposits of the household sector, AUD billions



Source: Knight Frank Research, ABS

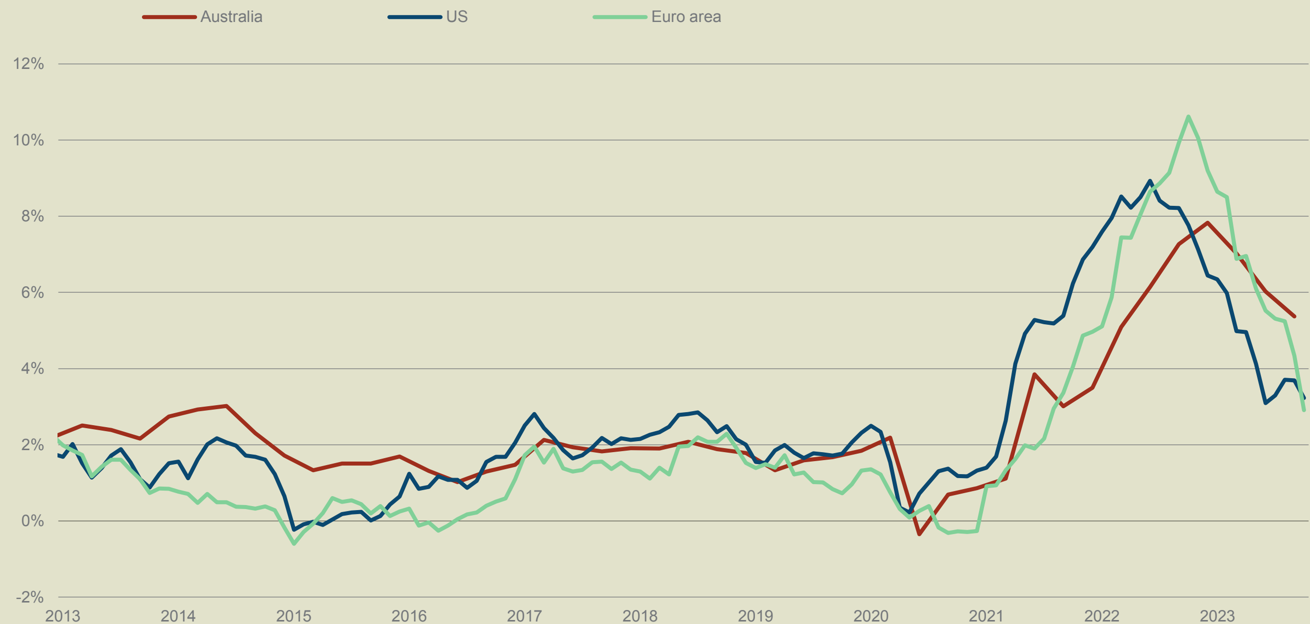
After a sustained period of monetary tightening since mid-2022, markets have been watching for signals of economic slowdown as higher interest rates fed through to cool consumer spending and business investment. The headline GDP growth rate has clearly slowed, with the annual pace of growth slowing to 2.1% in Q2 from 3.1% in mid-2022 and the quarterly pace of growth suggesting a further slowing is imminent. Retail sales have been an obvious weak point, with three consecutive quarters of decline in volume terms.

However, the slowdown has not been as bad as many feared, and the economy remains on the RBA's 'narrow path' to a soft landing. Moreover, multiple indicators point to resilience. Firstly, the labour market remains very tight, with the unemployment rate still close to record lows and job vacancies still at very high levels across most industries and well above the pre-pandemic trend.

Related to this, surging population growth, driven by record levels of net migration, is clearly supporting the economy and underpinning Australia's long-term expansion, with clear consequences for property across all sectors. ABS figures to the end of the March quarter point to an annual increase of 563,000, reflecting growth of 2.2%, with subsequent data releases expected to show that the pace of growth has accelerated even further to record levels.

Separately, on the household front, the aggregate level of savings has held up in the face of the steep escalation in mortgage costs. While many households are clearly feeling the pinch and that pain is being felt unevely, the overall level of cash deposits remains elevated, which attests to substantial savings buffers still on hand for the economy on the whole.

All of this points to sustained growth in 2024, even if the overall pace remains below trend. Australia is better placed than many other countries to experience not only a soft landing, but a stronger take-off once the pressures the rate hiking cycle abate.



Matterhorn or Table Mountain?

Rates are now peaking but rapid declines are unlikely

While the resilience of the economy is welcome, the flipside is that is still generating significant inflationary pressure.

The initial wave of inflation that had its genesis in supply chain disruption and sharp rises in the cost of goods has now passed, but the global economy is now dealing with persistent inflation across service industries, propelled by rising wages and rising inflation expectations, particularly in the short term.

Inflation rates are coming down globally, but there remains concern that progress will stall with inflation in the 3-4% range and that it will prove difficult to get CPI all the way back to the target range. This is also true of Australia, with the latest data for Q3 pointing to stubborn core inflation and ongoing cost pressures in key areas such as housing rents, fuel and utilities.

After such a disruptive period it is difficult to predict the speed of the downward trajectory for inflation, with central banks wanting to do enough to make sure the pressures abate but not so much as to drive a hard landing.

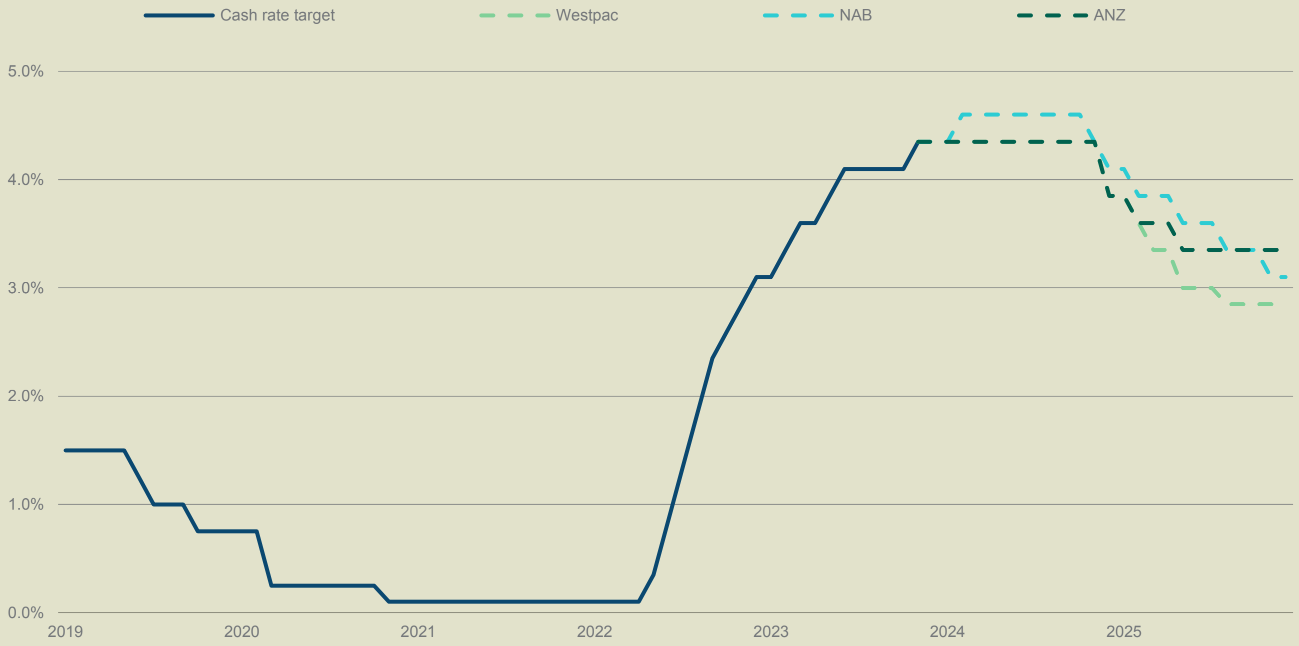
Across the board, they have had to push rates higher than initially expected to drive inflation down, and from these higher levels the interest rate outlook remains highly uncertain. To paraphrase a recent comment from Huw Pill, Chief Economist at the Bank of England, will the outlook for rates look more like the Matterhorn – with a high peak for rates followed by rate cuts – or Table Mountain, implying a lower peak but a longer period at a high level?

Market expectations for the US arguably point to a 'Matterhorn' profile, while Australia looks set to experience a lower peak with the RBA arguably showing more patience to allow time for inflation to come back to target.

Regardless of the peak level for the cash rate, economists are almost universally of the view that we will see rate cuts in 2024-25, with most expecting this to occur from late 2024. As such, the macro outlook is gradually becoming more favourable and by mid-2024 we expect a clearer picture on the peak for property investors, even if there remains uncertainty as to the timing and extent of future rate cuts.

Cash rate target

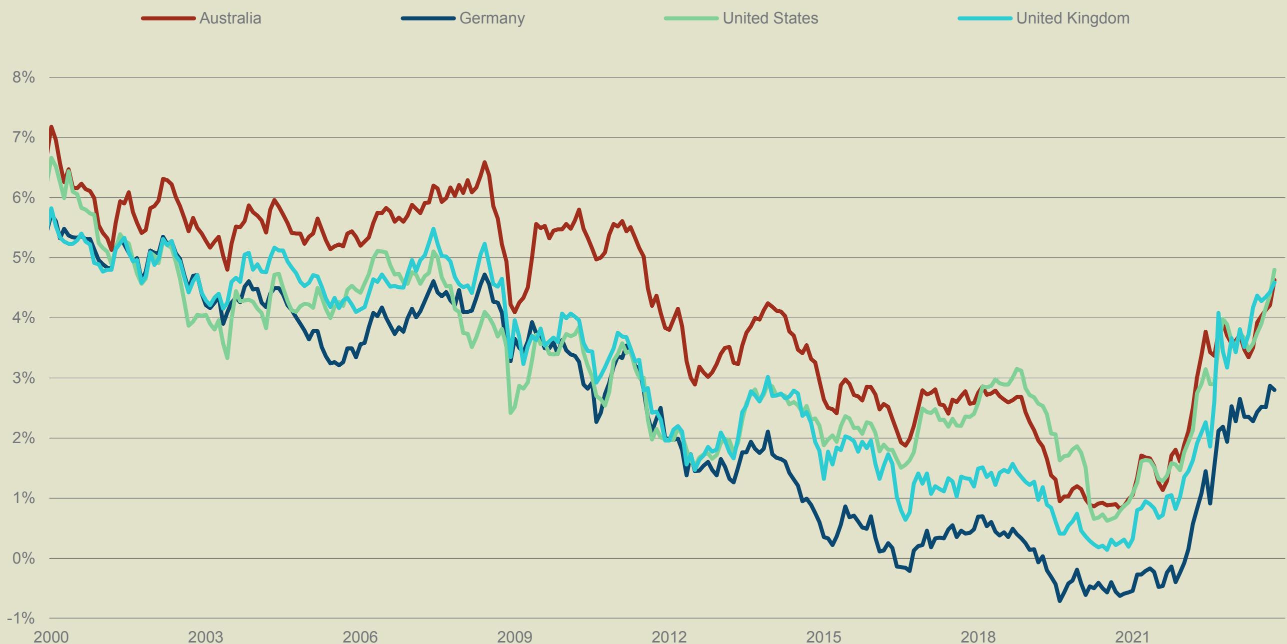
Historic rates and latest forecasts



Source: Knight Frank Research, NAB, Rate City

The end of the NICE era

The potential for more variable inflation has big implications for real estate



Source: Knight Frank Research, Macrobond

Among the valedictory remarks from outgoing RBA governor Phillip Lowe was an observation that the recent experience of higher and more volatile inflation could be a sign of things to come. Lowe commented that inflation is likely to be more variable looking ahead, owing to multiple pressures including climate change, the associated energy transition and demographic shifts.

His comment calls to mind the NICE analogy from another former central banker – Mervyn King – when referring to the end of global macroeconomic conditions that have driven a 'non-inflationary consistent expansion' (NICE). NICE conditions have prevailed in Australia for many years, with inflation barely registering as a concern for investors since the early 1990s. Now however, we see evidence that expectations are shifting, with higher bond yields globally signalling the expectation that rates will not swiftly return to the low levels that prevailed in 2016-21.

Again, this is partly due to Australia's strong fundamentals, with a strong long-term growth outlook once we get through the current hiking cycle. However, this growth may come alongside a more variable outlook for inflation and interest rates over the next decade, as significant investments in infrastructure, housing and the energy transition alter the balance between savings and investment, and test the capacity constraints of the economy. Lower rates may yet return, but this is far from assured, and investors will need to strategise for multiple scenarios.

> "It will be difficult to return to the earlier world in which inflation tracked in a very narrow range. The increased prevalence of supply shocks, deglobalisation, climate change, the energy transition and shifts in demographics mean either steeper supply curves or more variable supply curves."
>
> **PHILLIP LOWE**
> Former Governor
> of the Reserve Bank of Australia
> September 2023

Capital Markets

A better vintage awaits investors in 2024

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IRRs will rise to restore the spread over bonds

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Extent of yield shift depends on risk perception and rental growth outlook

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Required returns have risen

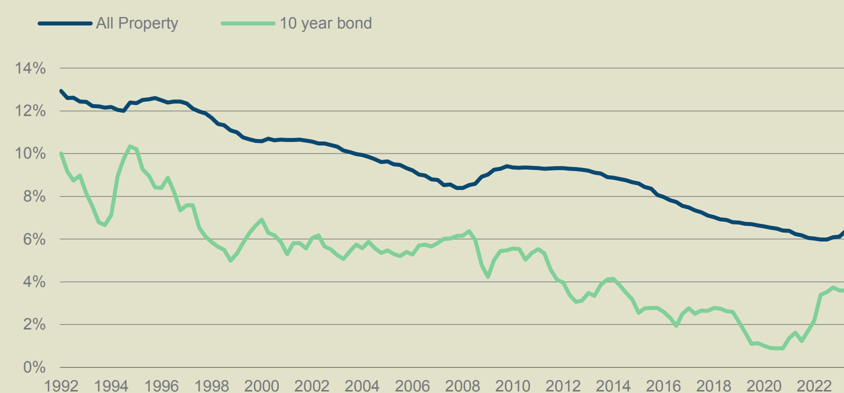
IRRs will rise to restore the spread over bonds

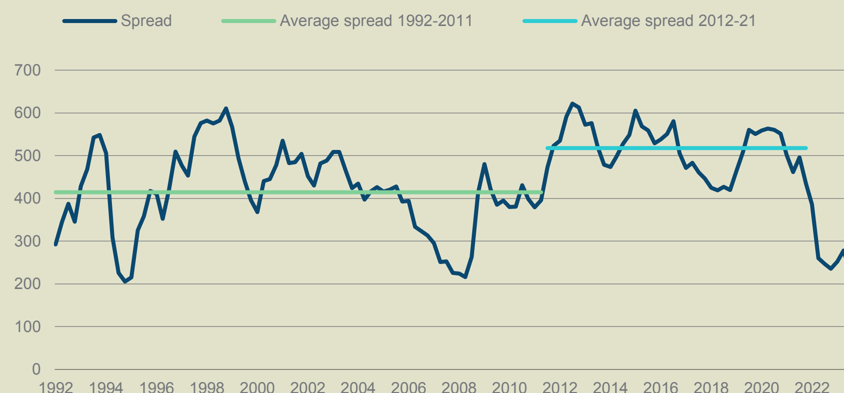
With long-term bond yields standing at over 4.5% in Q4 2023, financial assets across the spectrum are having to adjust to a much higher risk-free benchmark. Required returns are rising and the extent of the resulting yield shift is being hotly debated.

However, an important pre-cursor to an assessment of the impact on yield is the impact on required returns, and while this return hurdle will naturally differ from investor to investor, some aggregate conclusions can be drawn from a historic analysis of reported discount rates (IRRs). The average IRR across the Australian fell gradually over the past decade and reached 6.0% in 2021. This was much lower than in years past, but by no means low when compared to government bond yields which fell even more dramatically. Indeed, despite low IRRs, the spread over government bonds was consistently high from 2011-21, averaging 510 basis points over this period compared to 410 basis points over the 20 years prior.

Evidently, property investors did not expect interest rates to remain at such low levels forever, and pricing ensured that property returns retained a substantial buffer over risk free rates. Arguably, the earlier period from 1992-2011 when interest rates were substantially higher is a better guide to the sort of spread we might reasonably expect going forward.

With a bond yield ranging from 4.4-4.9% in October 2023, this may be seen as implying that IRRs need to rise substantially to 8.5-9.0%. But just as investors perceived in 2011-21 that long term yields were unlikely to remain at such low levels, it is unlikely that the current market perception has shifted equally far in the other direction. It is more likely that longer-term expectations for risk-free rates still hover in the 3.0-4.0% range, implying IRRs of 7.0-8.0% and a more modest shift upwards from current levels.





Wide divergence in yield impact

Extent of yield shift depends on risk perception and rental growth outlook

Regardless of the shift in IRR required for different markets on average, it is clear that there will be divergent impacts on pricing owing to the very different ways in which higher return targets will be achieved by different property types. Core assets that are perceived to offer better income security will trade at tighter IRRs, and for those that also come with strong income growth prospects, this will imply that a given return target can be achieved with a lower yield. On the other hand, weaker quality stock is likely to be perceived as higher risk and also offering less income growth potential, so yields will need to be significantly higher to achieve a given return target.

This will play relatively well for industrial assets, which are benefitting from strong rental growth and tight supply that is starting to appear structural rather than purely cyclical. The perception of risk in different sectors has undoubtedly changed over time, and while industrial assets have traditionally attracted higher risk premia, it is expected that the recent trend toward slightly lower IRRs in industrial compared to office and retail will continue over the forecast horizon. This will limit the potential for a further softening of industrial yields beyond that already experienced to date, as the outlook for strong income growth means that target returns can be achieved at a lower initial yield.

For office and retail assets, there will be a sharp divergence depending on asset quality and perceived growth potential. Prime assets that are the demonstrated preference of tenants and consumers within their local market and are experiencing rental growth associated with the recognised flight to quality, will also see a smaller shift in required return targets and hence reduced yield shift. However, assets facing heightened vacancy risk and without the prospect of seeing effective rents rise in the near term will see investors demand a higher premium for risk. In these cases, the yield shift experienced will also be larger because investors will perceive that a higher proportion of the return over the medium term will need to be achieved via income as opposed to future growth.

Higher Quality

- Lower IRR adjustment
- Stronger rental outlook
- Smaller yield shift

Lower Quality

- Larger IRR adjustment
- Weaker rental outlook
- Larger yield shift

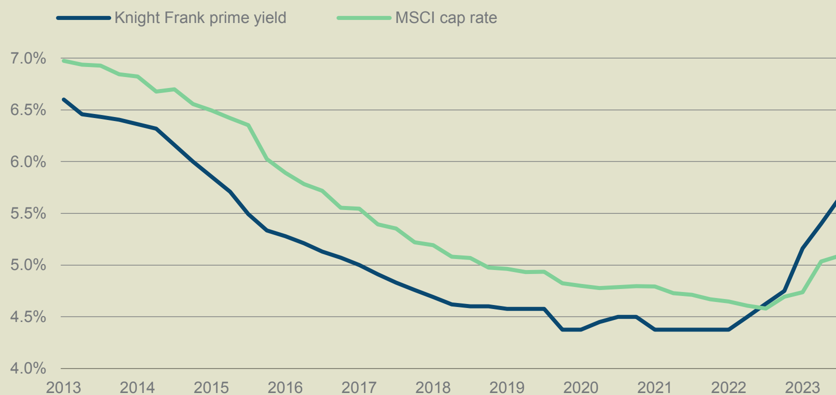
A better vintage awaits...

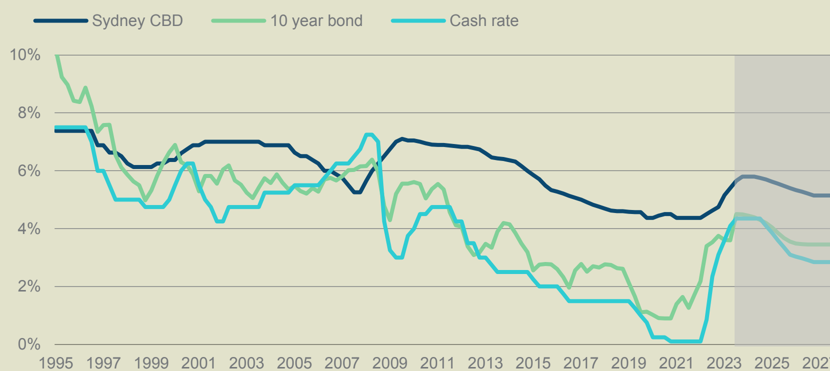
2024 will be a better year in which to acquire assets

After a tumultuous period in 2022-23, the market can look ahead to consolidation and to the prospect of recovery emerging in 2024. The sustained pressure of higher rates has put pressure on asset values and this is still playing out to varying degrees, with progress toward price discovery complicated by an acute lack of liquidity, particularly in the office market. Part of the uncertainty has been a disconnect between formal valuation metrics and market sentiment, as evidenced by the gap between the cap rates reported by MSCI and prime yield metrics reported by Knight Frank. For instance, MSCI data reflects an increase of 50 basis points for Sydney CBD offices whereas the Knight Frank series reflects an increase in prime yields of 125 basis points on average over the past 18 months.

The datasets are different and there are several reasons for the different pace of adjustment, but nonetheless this does indicate the lack of clarity on where formal metrics will end up and helps to illustrate the protracted bid-ask spread that is impacting market liquidity. With more deal evidence now coming through and formal valuations likely to be adjusted further in the December cycle, we expect the gap between sentiment and formal valuations to erode substantially over the next six months so that by mid-2024 the picture will be clearer for buyers and sellers alike, helping to restore confidence and liquidity.

While reductions in asset value are never welcomed by owners, the flipside is the reemergence of value looking forward. Higher yields act to reset the market and provide a more attractive entry point for investors, generating the prospect of higher returns. This is clearly illustrated when we assess historic market cycles and the performance achieved after pricing is reset in the aftermath of interest rate hiking cycles. The period immediately after the





conclusion of rate hike cycle ending in 1994, 2000 and 2010 was in each case a very attractive time to buy, achieving well above average returns over the following five years.

A key reason for this strong performance has been yield compression, which supported returns once interest rates were reduced from the peak – this occurred most decisively in 1996-98 after the 1995 peak and during the extended period of rate cuts that began in 2011. On both occasions, significant cuts in the overnight cash rate fed through to lower bond yields and also through to yield compression in Australian commercial markets, notably prime Sydney CBD offices.

In keeping with these long-term relationships, we expect that if rate cuts eventuate as anticipated in 2024-25, that this will also be accompanied by yield compression. Indeed, based on the current outlook for interest rates, we forecast average Sydney prime yields to peak in coming quarters, and then fall back by 50-75 basis points by 2026.

Of course, investors cannot take for granted that interest rates will fall exactly as anticipated. But careful asset selection will maximise the chances of strong performance whether it is achieved through income growth or boosted by a return to yield compression as interest rates revert.

This is not to say that history will repeat, and investors cannot take for granted that interest rates will fall exactly as anticipated. But careful asset selection will maximise the chances of strong performance whether it is achieved through income growth or boosted by a return to yield compression as interest rates revert in 2024-26.

Tilt to core strategies

Will drive sustained living sectors expansion

The sudden expansion of the build-to-rent (BTR) pipeline in Australia is emblematic of a wider shift in the global investment landscape. Across all regions, investors are seeking greater exposure to alternative sectors and the residential 'living' sectors are at the front of the queue, led by BTR but also encompassing student accommodation and retirement living. This was borne out in the most recent ANREV survey of global investor intentions, which highlighted that for the first time, residential is the most sought-after sector for global investors targeting the Asia Pacific region.

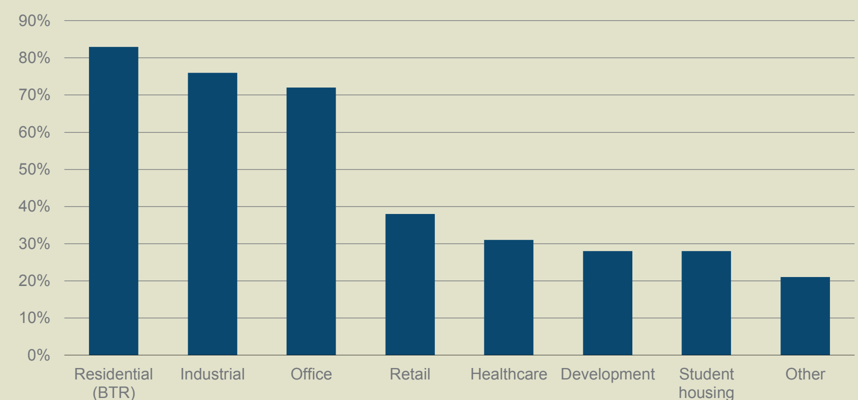
The shift to living sectors is part of a wider shift from major institutions globally to focus predominantly on core investment strategies as they seek greater diversification through exposure to the relative stability of the living sectors in response to a more uncertain global economic outlook.

Investors are also gravitating toward the living sectors because of structural under-supply in rental markets and because living sector assets offer the ability to adjust rental income streams more quickly than other sectors in response to high inflation. Historic experience certainly bears this out. Residential rents have consistently exceeded the pace of inflation over the long term, and also exhibited a high degree of correlation with fluctuations in inflation, in contrast with other major assets classes where the rental cycle has fluctuated more widely. An analysis of the relationship between annual rental growth rates in the residential sector and annual movements in inflation reveals a very high degree of correlation.

These drivers will remain in place in 2024, and we expect a further expansion of interest in BTR and other living sectors to be reflected in continued growth of the pipeline and additional capital partnerships being formed.

Preferred sectors for global investors

2023 ANREV investor survey - respondents targeting each sector (%)



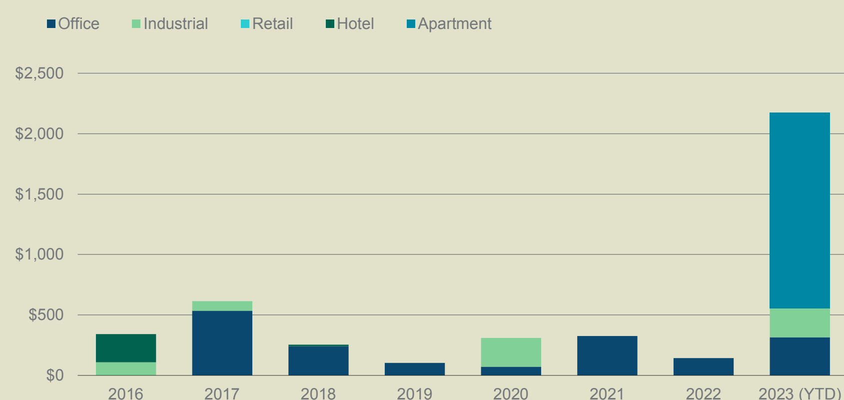
Source: Knight Frank Reseach, ANREV

Correlation - rent growth vs inflation

Correlation between rental growth rates and CPI since 1976

Source: Knight Frank Research, ABS

Acquisitions in Australia from Japanese investors
AUD millions



Source: Knight Frank Research, RCA

Japan emerging

Lower cost of capital sees Japan emerge as a key source of capital

With most major markets globally experiencing the impact of higher inflation and interest rates, global investment flows have reduced and many investors have chosen to wait until the macro picture settles. As a result, Australia has seen less inward investment from the usual sources of Singapore, the United States, Hong Kong SAR and Canada.

A clear exception to this has been investment flows from Japan, which have increased significantly in 2023, going against the wider market trend, with investors such as Mitsubishi Estate, Daibiru and Daiwa House all making large scale acquisitions. This has taken total acquisition volume from Japanese investors to a record $2.2 billion (Real Capital Analytics), encompassing large investments in BTR, offices and industrial assets.

While Japanese investors have long been active in Australia, the rise in funding costs globally has placed them at a competitive advantage given that funding costs remain far lower in Japan. And the advent of BTR in Australia has opened up new opportunities that fit the profile for Japanese investors, given extensive understanding of the sector within Japan where it is a well-established part of the institutional market. After a strong foray in 2023, we expect sustained interest from Japanese investors in 2024, focussing once again on capital partnering into develop-to-core opportunities.

Photography: Kishu-Kaido, Chuo Ward, Osaka, Japan by Rizwan Nawaz

Office

Tightening development pipeline sets the scene for prime market recovery

26 **Strong outlook for Brisbane and Perth**
Economic out-performance driving office market momentum

28 **Core CBD outperformance**
Strong performance in the core will broaden to neighbouring precincts

29 **Multiple pressures on feasibility**
Fewer development starts to tighten the prime market and widen the gap between prime and secondary rents

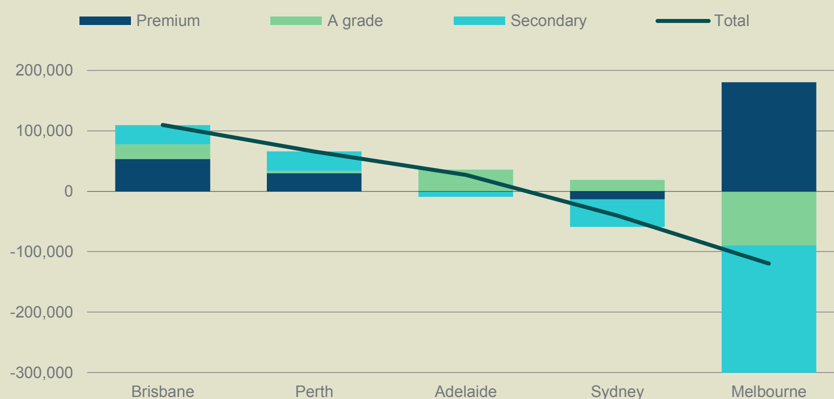
30 **Disruption will drive sustained demand**
Key themes from the (Y)our Space Australia & New Zealand survey results

Strong outlook for Brisbane and Perth

Economic out-performance driving office market momentum

Stronger office demand in Brisbane and Perth

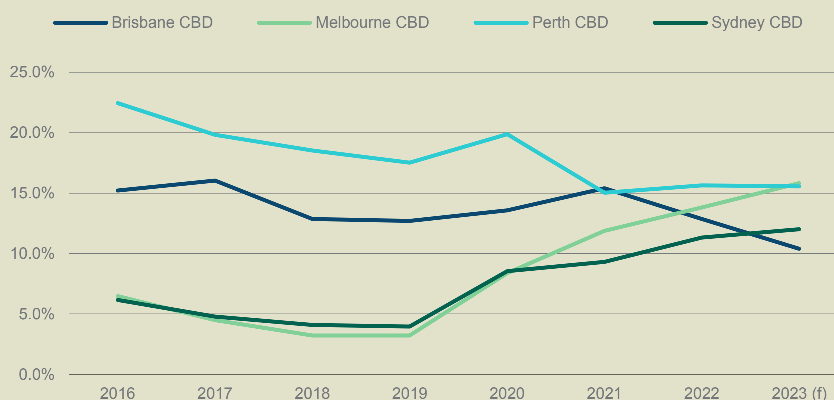
Sqm absorption by grade in major CBDs - total 2020-23



Source: Knight Frank Research, PCA

Change in the vacancy profile across cities

Historic and forecast vacancy rate, selected CBD markets



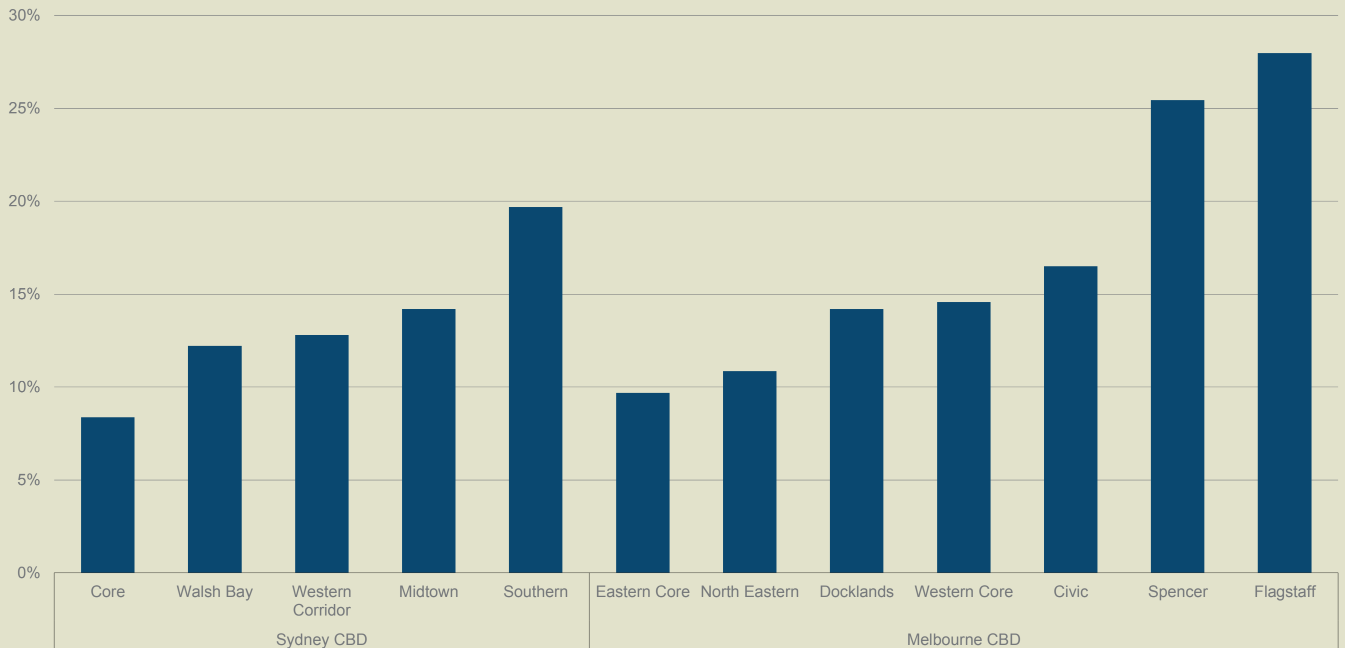
Source: Knight Frank Research, PCA

After lagging behind the larger markets of Sydney and Melbourne for much of the last decade, Brisbane and Perth have shifted back to a period of out-performance. Sustained tenant demand and minimal downsizing from major corporates have seen office demand expand substantially, as reflected in positive absorption of 110,000 sqm in Brisbane and 66,000 sqm in Perth since the advent of the pandemic. In contrast, Sydney and Melbourne have both experienced weaker tenant demand, as reflected in negative absorption over the same period, with sentiment remaining cautious.

While it may be tempting to ascribe this outperformance as due to the stronger impact of the resource and commodity sector on the Brisbane and Perth markets, on closer inspection it is due to a much broader range of factors. Brisbane has seen strong take-up across both the State and Federal Governments, responding to the greater need for services as the population expands. Renewable energy and solar service providers and advisors have also been growing along with expansion across the professional services sector. Both cities also experienced less disruption during the pandemic and saw a quicker return to the office, and both have less reliance on large finance and insurance or technology tenants where tenant demand has been more subdued.

Looking ahead, the relative strength of the Queensland and Western Australian economies will remain supportive, as evidenced by strong population growth of 2.8% and 2.3% respectively over the past year. Both states are experiencing high levels of interstate migration and when coupled with strong employment prospects across multiple industries, they are also likely to attract a greater proportion of offshore migration in the coming years, all of which will help to diversify the talent pool and expand the office market over time.

Core CBD outperformance



Strong performance in the core will broaden to neighbouring precincts

While the Sydney and Melbourne markets are experiencing high overall vacancy rates, the aggregate picture masks significant variation in performance between different markets, both within the CBD and across the markets more broadly.

In Sydney, the core CBD is out-performing, as financial and professional services tenants take decisions to upgrade their space. New developments have also acted as a catalyst for significant tenant migration and created more opportunity for businesses to cluster around newly activated precincts.

In Melbourne, the Eastern core has likewise separated itself from surrounding precincts and is benefitting from rental growth while other precincts are experiencing much higher vacancy and negative sentiment.

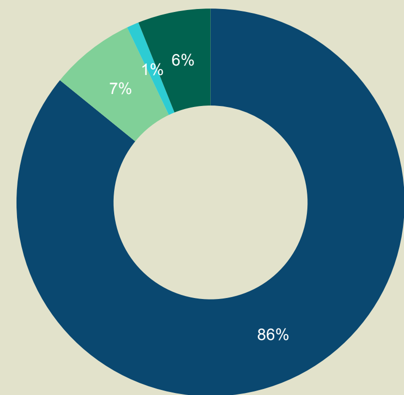
Looking ahead, we expect the respective core markets to build on this strength in 2024, and a gradual improvement in sentiment starting with neighbouring precincts. In Sydney, several markets including Midtown and North Sydney will benefit from the advent of the next phase of Sydney Metro, which will boost along the central corridor of the CBD off the back of several new overstation developments, while in Melbourne the Civic and Western Core markets will consolidate with the CBD market set to see fewer completions in 2024 and a slowdown in development activity over the forecast horizon.

Multiple pressures on feasibility

New developments in high demand

Let up timing of Sydney CBD new developments 2018-23

- Commitment Prior to PC
- Leased post completion (0-12 months)
- Leased post completion (12-24 months)
- Uncommitted (or still within 2 year period post PC)



Source: Knight Frank Research

Fewer development starts to tighten the prime market and widen the gap between prime and secondary rents

Several factors are pushing against new commencements in 2024, with developers likely to find it difficult to meet feasibility thresholds in the face of rising construction costs and elevated funding costs impacting project costs, while a backdrop of higher yields impacts asset values. In addition, higher vacancy rates and elevated incentives are traditional signals pointing to a need for caution.

However, a slowdown in commencements will impact the pipeline in 2027 and beyond, and even at this early stage it is possible to identify a risk of a shortage of prime space later in the decade.

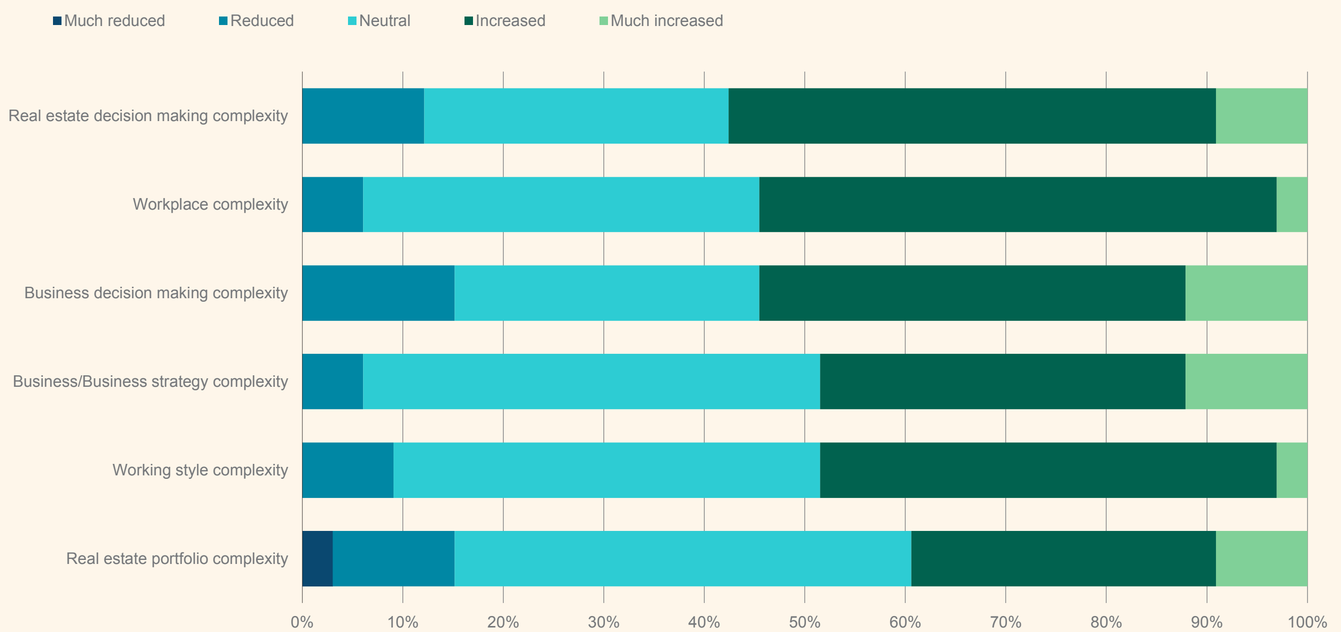
While overall market vacancy rates may remain elevated for some time, the demonstrated strength of tenant demand for newly built space will mean a potential shortage of new buildings at this time. This will bring tenants to market earlier, particularly those with larger requirements, and aid the overall market recovery. It will also act to drive up the face rents on new developments since this will be the only way to counter other pressures on feasibility. In turn, this will aid the prime market recovery and widen the gap between prime and secondary rents.

Disruption will drive sustained demand

Key themes from the (Y)our Space Australia & New Zealand survey results

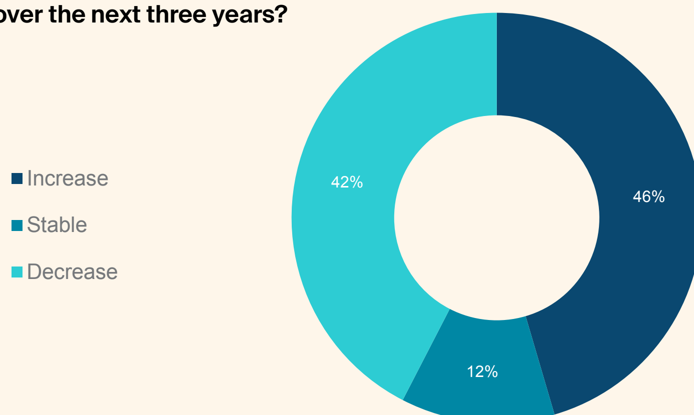
Q: How will decision making change over the next three years?

(Y)our Space global occupier survey - Australia / New Zealand based respondents



Source: Knight Frank Research, Y(our) Space

Q: How will your floorspace requirement change over the next three years?



Source: Knight Frank Research, (Y)our Space

Managing complexity

As businesses emerge from the pandemic a more complex operating environment is emerging across multiple dimensions of business transformation and real estate decision making.

One of the most significant disrupters is the rapid and widespread adoption of digital technologies and artificial intelligence, which enable new possibilities and challenges for working and collaborating across different locations, time zones, and cultures. Almost half of companies

surveyed expect to undertake a digital transformation strategy within the next three years.

At the same time, the legacy of the pandemic is reflected in continued workstyle experimentation and change and many companies are still experimenting on policies and styles which will be retained into the long term. More than half of survey respondents are anticipating a more complex workplace environment, indicating that the big questions raised over the past three years are far from being fully resolved.

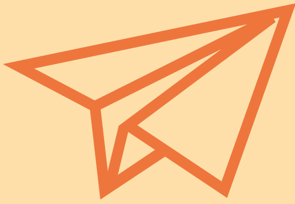
These and other structural shifts have profound implications for how organisations use real estate as a strategic tool to achieve their business goals. Survey respondents were evenly split between those planning to increase or decrease floorspace over the next three years, but what is clear is that regardless of the precise impact on floorspace requirements, complexity and disruption will drive sustained demand for office space that can meet the evolving needs and preferences of occupiers. Tenant mobility is set to rise even if the overall footprint is slower to grow.

(Y)OURSPACE

MANAGING COMPLEXITY

Knight Frank's flagship occupier research campaign investigating the future of work, workplace and corporate real estate. Our data analysis has been shaped by real-world perspectives from 640 worldwide companies set against ever-evolving real estate ambitions.

For more information, visit:
www.knightfrank.com/your-space



The flight to quality has 4 essential elements

‘Flight to quality’ is a well-worn phrase in office markets globally. It remains true but encompasses more than a simplistic drive to higher quality space. At its heart flight to quality embodies four different quests by tenants to enhance and future proof their real estate experience:

Flexibility

COWORKING

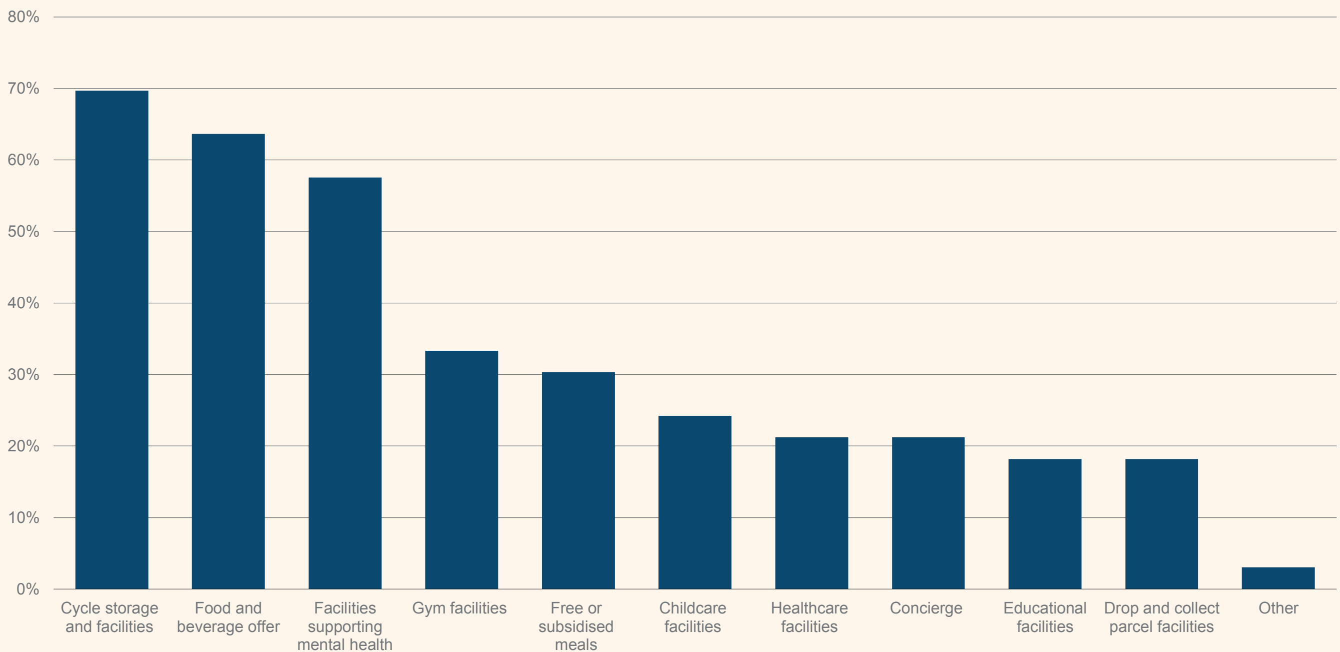
GROW/SHRINK

THIRD SPACES - MEETING ROOMS / AUDITORIUMS

With 65% of the Australian businesses surveyed indicating they expect to adopt a hybrid strategy in the long-term, planning around how to navigate peak days and all of company gatherings increasingly encompasses using flex space as part of the solution. Once the remit of only large companies, the expectation and adoption of flex space will increase, with a third or respondents expecting to increase the amount of flex space within their portfolio strategy, including through the use of third spaces to handle overflow, events or focussed collaboration.

Q: What amenities do you think staff will demand from their workplace over the next three years?

(Y)our Space global occupier survey (% of Australia / New Zealand based respondents)



Source: Knight Frank Research, (Y)our Space

Amenity

FOOD & BEVERAGE

CYCLE / END OF TRIP

MENTAL WELLBEING / SANCTUARY SPACE

EDUCATIONAL FACILITIES

The desire for amenity is long-standing but remains as important to tenants' decision making now as it has even been with 100% of respondents expecting to maintain or improve the level of amenity in their real estate portfolio. This encompasses physical amenity features which are increasingly regarded as core requirements, plus services and facilities supporting mental wellbeing, with the latter increasing in importance since the last (Y)our Space survey.

Location

TRANSPORT

RETAIL

OUTDOOR SPACES

As tenants have greater choice in the market the importance of location has returned to the forefront. The flight to location has demonstrated that buildings can borrow amenity from a well-curated precinct and not all amenity which attracts potential tenants needs to be located within the building. Attractive and well-connected streetscapes with ready access to entertainment, retail and outdoor spaces create a natural centre of gravity and businesses will gravitate to them.

ESG

GREEN ACCREDITATION

RECYCLING

GREEN ENERGY

Weak sustainability credentials will continue to be the major driver of obsolescence in office stock as the gap between stated ambitions of corporates and their real estate decisions is reduced. The (Y) our Space survey indicated that 79% of respondents expected their company's ESG strategy or commitments to have either a great or moderate influence on their real estate decisions in the next 3 years, reflecting the widespread desire to upgrade the level of accreditation across their portfolios.

Education to emerge as the next frontier of amenity provision

The past decade has seen a significant uplift in the breadth and quality of amenity provision, so where next in the ongoing evolution of offices? Globally, an emerging trend from corporates is an expanded focus on staff training, with widespread recognition that the pace of business transformation and the advent of new technologies including generative AI is proceeding at such a pace that there is a need to shape an internal education agenda rather than entirely rely on staff to upskill and reskill for themselves. This aims to ensure to that ensure new and existing staff are empowered to meet the specific needs of individual businesses and is potentially a win-win for employer and employee.

While education was not highlighted as a key requirement for occupiers in the recent (Y)our Space survey of Australian corporates, major investments in other global markets from the likes of Deloitte (Paris), KPMG (Florida) and Telefonica (Madrid) in dedicated education campuses point to a future where corporates take a stronger lead in ongoing staff training to boost productivity and staff retention. While we are unlikely to see similar campuses in Australia in the short term, the education imperative will still guide the form and function of future developments, with training and event spaces likely to be increasingly integrated as part of holistic service provision.

Industrial

Rental growth set to continue

36 **Global comparisons**
Evidence on business costs and global benchmarks indicates that industrial rents can rise further

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What can Vancouver tell us about the outlook for Sydney?

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Perceptions of reduced risk and strong long term growth prospects will reduce the required shift in IRRs

Global comparisons

Evidence on business costs and global benchmarks indicates that industrial rents can rise further

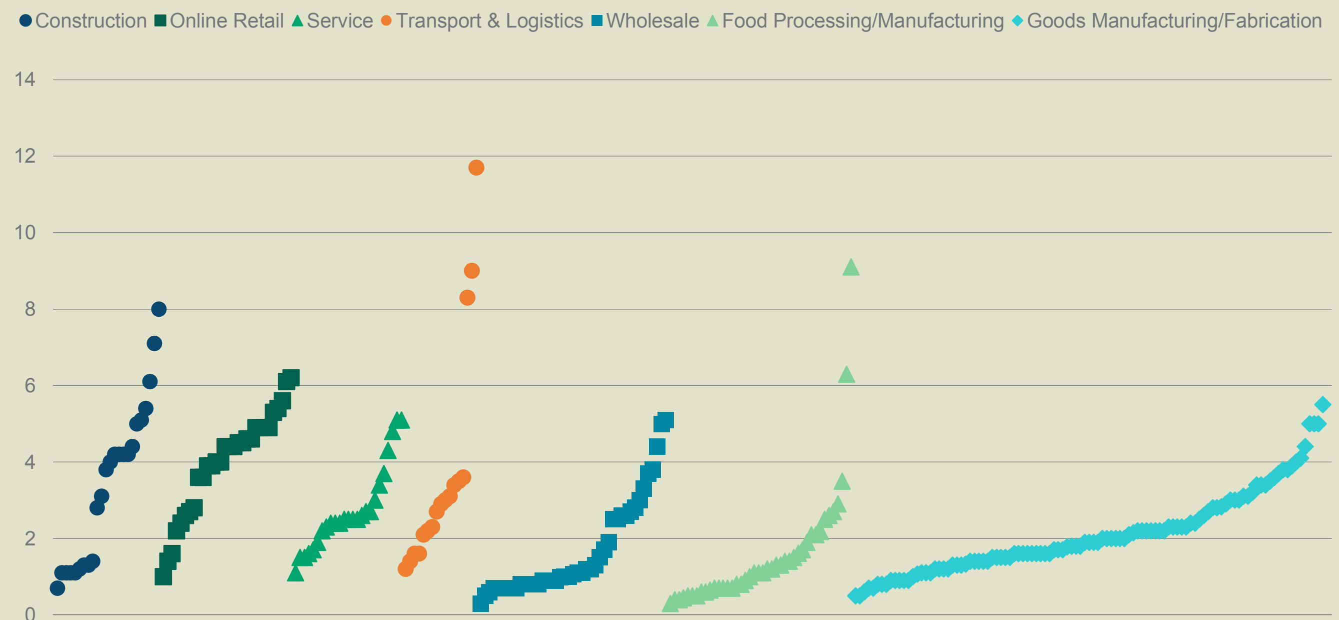
Does the current phase of rental growth have further to run? This is a key question among market participants as we head into 2024, off the back of sustained and substantial increases to industrial rents over the past three years across all markets.

Two considerations suggest that the answer is yes. Firstly, an assessment of rental costs as a proportion of total operational costs for a wide range of industrial space users suggest that rents are not presenting an unmanageable burden. Data from IBIS World indicates that rents represent less than 5% of total operational costs for 90% of selected, industrial property-exposed industries. In addition, anecdotal evidence from major industrial landlords indicates that tenants on new, or newly marked to market, leases are increasingly having rents constituting 7.5% - 10% of their total operational costs, although for some Sydney tenants it may be up to 15%.

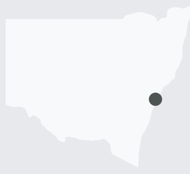
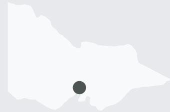
While rents and other operating costs are increasing, the data indicates that in most cases companies have been able to pass through the increases to end consumers, in keeping with the wider dynamic of a high inflation. Large companies appear to have the resources and business need to continue to absorb higher rental levels, although very tight supply levels in Sydney may drive longer term changes to the way companies allocate their holdings across the country.

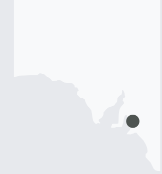
Secondly, rents in Australia are by no means out of line with the level of rents in comparable cities globally, most of which have also seen a sharp rise in rents in recent years. Comparing Australia's current prime industrial rents to other major economies indicates that the rent levels in our markets fall in the middle of the pack when compared on a like-for-like basis and the growth experienced has been in keeping with, rather than run substantially ahead of, the rise experienced in other major markets over the past five years.

Amidst rapid population growth and the ongoing need for new stock of a higher quality, rents can be expected to continue to grow, although going forward growth will be more closely linked to new supply rather than a scarcity of space across the entire market. The pace of growth will be more modest than in 2022-23 and there will be greater differentiation between the pace of growth for prime and secondary assets.



Forecast average prime rent growth in major Australian cities:

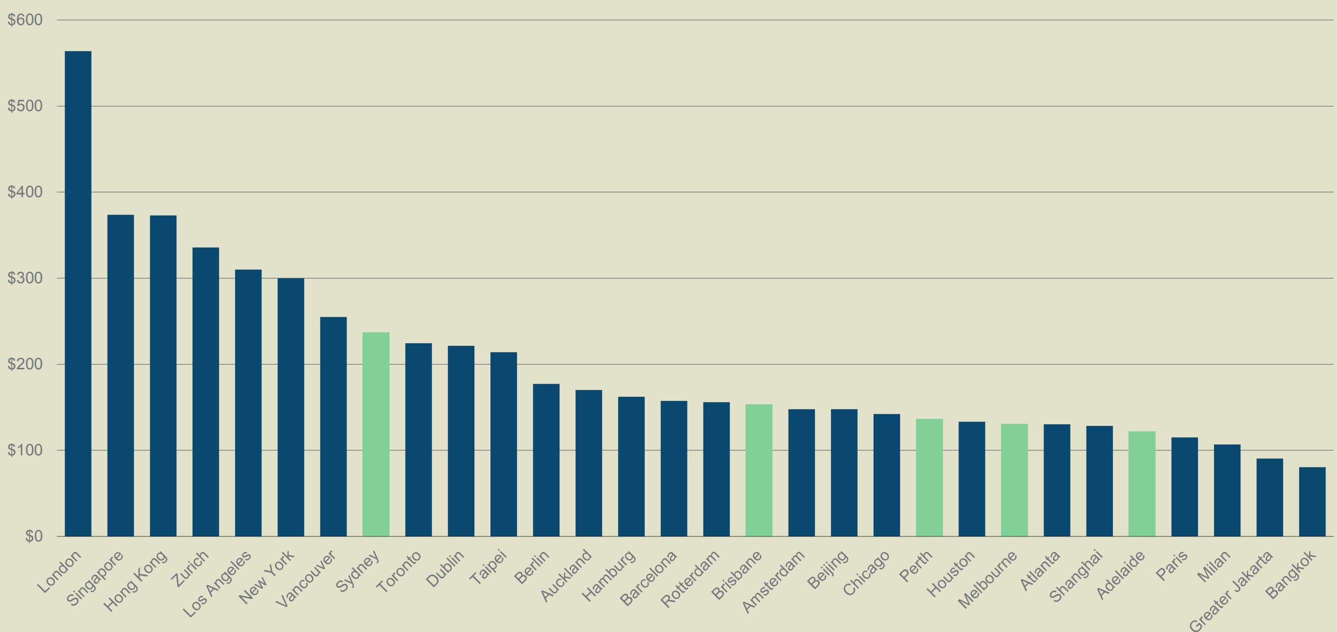





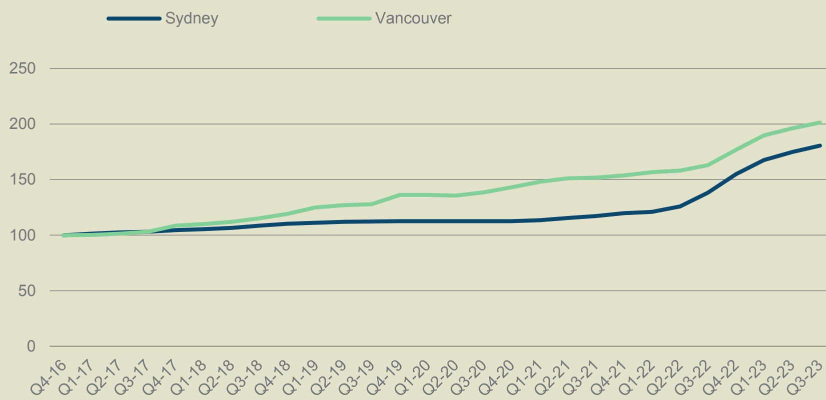
	Sydney	Melbourne	Brisbane	Perth	Adelaide
2022	29%	19%	16%	46%	14%
2023	20%	10%	16%	3%	10%
2024	6%	4%	6%	4%	3%
2025	4%	3%	4%	3%	3%

Comparing global prime industrial rents

A$/sqm/annum, as at Q2-23



Source: Knight Frank Research, Cresa



Source: Knight Frank Research

Understanding our Canadian twin

What can Vancouver tell us about the outlook for Sydney?

Sydney and Vancouver are often considered to be twin cities, with similar metrics and drivers within the residential, commercial and industrial markets. A comparison of the rate and shape of growth in the industrial markets between the cities indicates that after a period of stability both began to see sustained rental increases during 2018 which then accelerated from 2021.

Given North American markets are generally considered to be slightly ahead of Australia – what insights into 2024 can be gained from Vancouver?

- Tenants have slightly increased choice and in 2024 may no longer have to compete with multiple offers.
- Asking rents have been stable the past two quarters with vacancy increasing to 1.4% after being sub-1% a year ago.
- The availability of labour is a real challenge, so locating in close proximity to workers is paramount and larger companies will pay the necessary rent.
- Smaller tenants are finding it harder to absorb much higher rents, with some choosing to shrink their footprint.
- Warehouse users are expecting a further increase in space available to lease or purchase in 2024, but not to levels that could be describe as a tenant's market.

Source: Cresa Vancouver Industrial Q3 2023

Development to remain elevated

The ongoing drive for efficiency will sustain demand

It is a testament to the sustained strength of demand that the major Australian industrial markets have experienced unprecedented levels of new development over the past four years. Markets have been able to absorb the increase, and still been left seeking more supply.

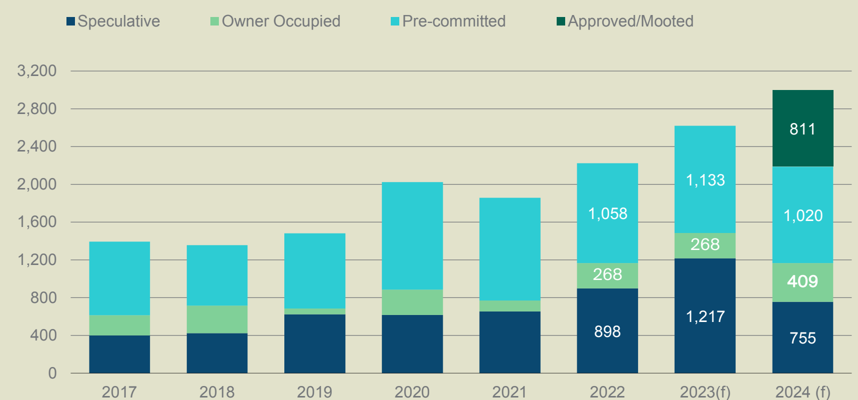
Looking ahead, the need for new industrial premises will continue to drive a high level of new development. For many tenants, advances in technology surrounding warehousing, distribution and stock tracking offer new opportunities to drive efficiencies but also act to make their existing premises functionally obsolete. For instance, many robotic systems favour deeper warehouse spaces with higher eaves, greater racking density and different fire suppression demands. Super-awnings, also fully sprinklered, are favoured to allow all-weather loading without internal docks reducing warehouse floorspace.

Corporates are also increasingly required to report on their ESG programmes with older style facilities less able to demonstrate environmental credentials. Reducing embodied carbon through green steel and green concrete slabs are part of the answer- but also cross ventilation, LED lighting, flood mitigation and retention and bio-diversity on site are also required. Greater staff amenity in outdoor spaces, socialisation zones and other facilities are also increasingly required to meet modern standards.

For all of these reasons, plus the relentless pressure of population expansion, tenant demand will continue to support a high level of new development. Higher funding costs and elevated construction costs may slow the pipeline at the margin in 2024, but the ongoing need for new facilities and the willingness to pay higher rents to bring forward new product will ensure that we continue on the 2020-23 trend rather than revert to lower levels of supply.

Sustained growth in new suppy

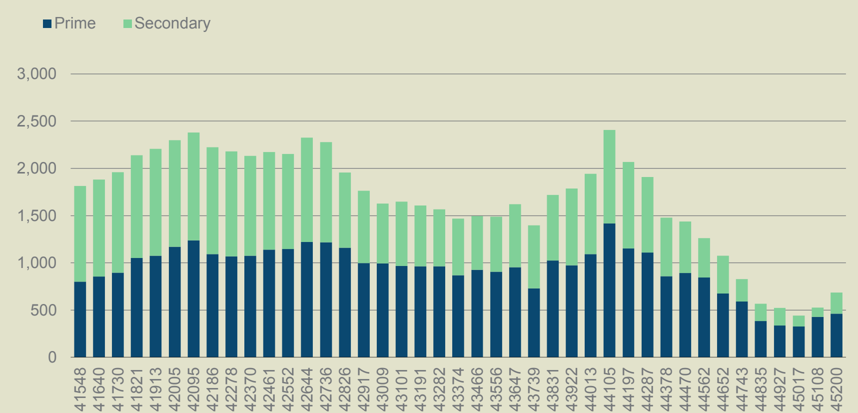
Eastern seaboard new supply, '000sqm, completed 2017-2024(f)



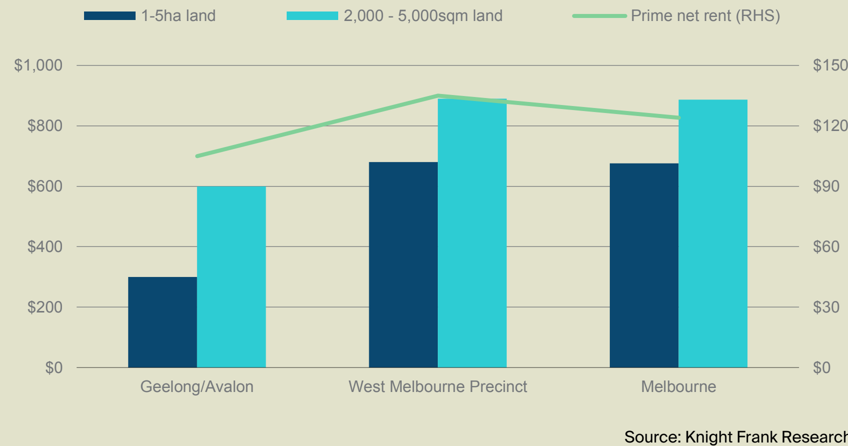
Source: Knight Frank Research

Vacancy remains very low

Eastern seaboard vacancy by grade, 5,000sqm+, '000sqm



Source: Knight Frank Research



Geelong opportunity

This regional city is emerging as an alternative to supply-constrained Melbourne

Australia's largest industrial market, Melbourne, has grown rapidly in recent years with substantial expansion, particularly to the West, and Geelong is now emerging as an option for further growth. Diminishing industrial land banks within Melbourne and tight feasibility on new development means that Geelong (including the Avalon precinct) is increasingly in focus for cost effective development.

The city and surrounds are benefitting from infrastructure investment as part of the expected Northern and Western Geelong growth areas, the largest urban growth project in regional Victoria aimed at strategic planning for population expansion, plus the Geelong Fast Rail project and the proposed Outer Metropolitan Ring/E6 Transport Corridor.

Meanwhile, Geelong Port remains the largest bulk port in Victoria with more than $7 billion in annual trade, leveraging road, rail and air links. The port recently launched the new Spirit of Tasmania terminal and is planning to develop a 25ha wind farm project cargo precinct and a new Geelong Hydrogen Hub.

This multi-faceted growth profile, combined with its proximity to the rapidly growing West of Melbourne makes Geelong an attractive location for industrial occupation and development. Land values across the Geelong/Avalon precinct sit at $300 per sqm for 1-5ha lots, a discount of 56% to the wider Melbourne level. Smaller lots have already shown strong recent price growth to $600/sqm, only 32% below the Melbourne average. Increasing occupier demand has driven Geelong prime net rents up by 17% since the start of 2023 to $105 per sqm. Though this is a steep rise, it is still 15% below the average Melbourne rents of $123 and given Geelong's potential for further expansion and faster transport links it is likely that rents and particularly englobo land values will continue to narrow the gap to Melbourne.

Changing risk perception

Perceptions of reduced risk and strong long term growth prospects will reduce the required shift in IRRs

Over the past decade the industrial market has undoubtedly benefitted from major behavioural shifts that have led to a reappraisal of the risk and growth outlook of the major property types. Firstly, changing consumer behaviour and the rise of online shopping saw investment divert from the retail sector and into industrial. Secondly, uncertainty over the extent of changing workstyles and the long-term impact on office occupation has further intensified the focus on industrial and alternative sectors such as the living sectors, healthcare and life sciences.

Coupled with the accompanying growth in scale of the industrial market, these shifts have had a significant impact on portfolio weighting and market liquidity. Between 2008 and the end of 2019, 43% of total Australian investment volumes were in the office sector, 22% in retail and only 13% in industrial. However, from January 2020 onwards the proportion of office has fallen to 34%, retail to 18% and industrial has increased to 24%.

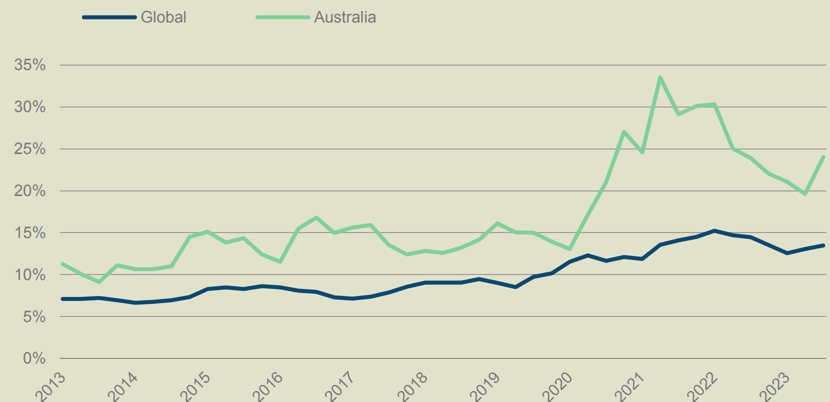
On a global scale this represents a high proportion of total investment directed towards the industrial market, however, this has been driven by a perceived undervaluation prior to 2020 and the ongoing lack of alternative assets of scale across the emerging sectors.

Related to this, perceptions of risk have also shifted, with required returns – as captured in average IRRs – in industrial now slightly lower than office and retail, having previously been significantly higher. It is no coincidence that the shift lower occurred in the early part of the pandemic.

Both of these trends are set to continue in 2024 and beyond, with the industrial market expected to continue to attract a high proportion of inbound investment, attracted by strong economic and population growth fundaments and ongoing rental growth expectations. It is also likely to experience a slightly smaller shift up in IRRs compared to other sectors due to the perception of less risk given its strong alignment with economic fundamentals, ongoing supply shortages and broad acceptance of a favourable growth outlook.

Rise of industrial share of market activity

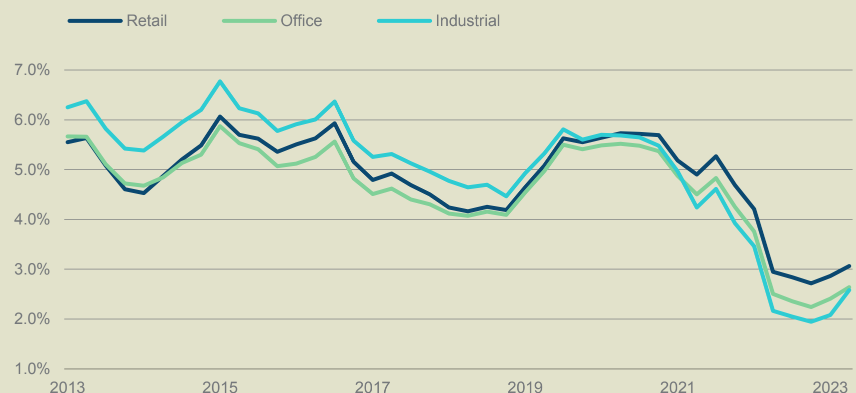
Proportion of total commercial deal volumes



Source: Knight Frank Research, RCA

Shift to lower IRRs in industrial vs other sectors

Average spread between IRR and 10 year bond



Source: Knight Frank Research, MSCI

Alternatives

Living sectors in vogue as new asset types emerge

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Higher cost of debt will shift the focus of different buyer types within living sectors

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Australian BTR expansion will mirror UK trajectory

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Attracting investors seeking living sectors exposure with higher return hurdles

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Driving new development beyond university precincts

48 **Capital recycling**
Will drive healthcare investment activity

Refining living sector strategies

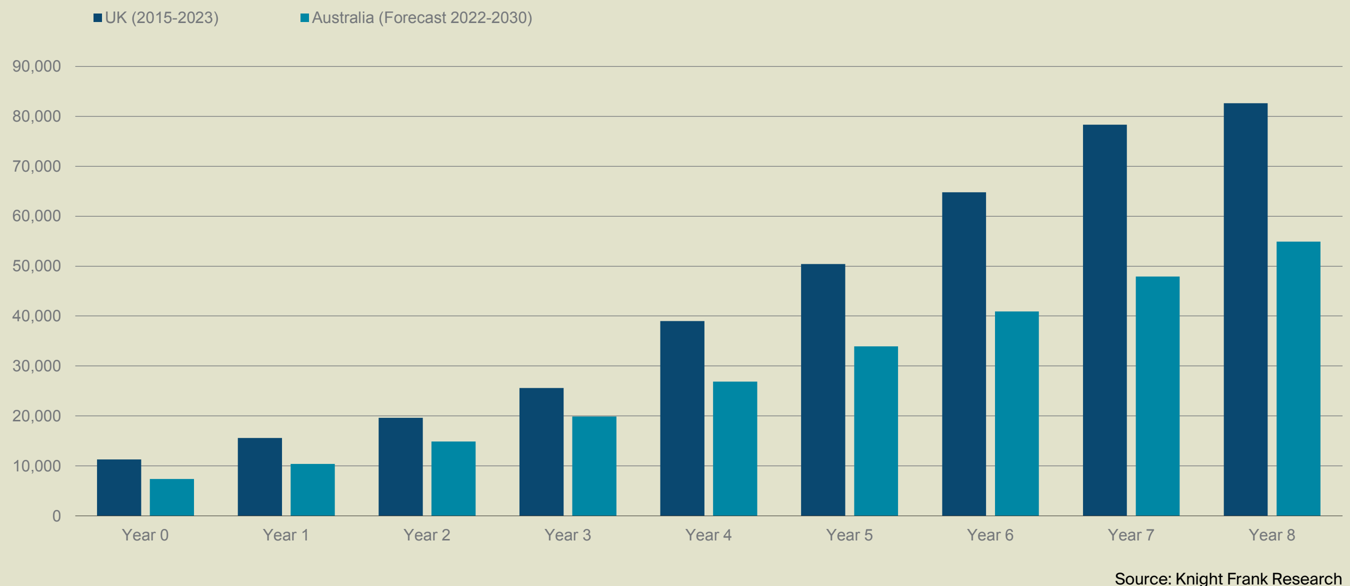
Higher cost of debt will shift the focus of different buyer types within living sectors

With living sectors emerging quickly in Australia and encompassing several distinct asset types, the challenge has shifted to execution as developers grapple with a higher cost of debt. Severe undersupply in residential markets and a thin development pipeline are providing fertile ground for the expansion of living sectors through a sustained supply-demand imbalance driving rental growth, but myriad cost pressures on developers are slowing the pace of delivery.

Build-to-rent has led the way and has the greatest potential to scale up, but higher funding costs, a lack clarity over the implementation of long-awaited MIT reform and uncertainty over potential changes to Thin Capitalisation rules are all making it more difficult to underwrite new developments.

In 2024 we expect sustained appetite for BTR but for this to be more concentrated among larger global investors seeking long term exposure through partnership arrangements with local developers. In the current climate, investors with a lower return hurdle will be best placed to meet more challenging feasibility criteria and deliver schemes at an appropriate yield on cost, while investors seeking higher returns will gravitate to other asset types within living sectors.

The surge in investment from Japanese investors is instructive in this regard, with Daiwa House and Mitsubishi Estate partnering with Lendlease and Mirvac/Clean Energy Finance Corporation respectively to invest in major BTR schemes in Melbourne.



BTR expansion

Australian BTR expansion will mirror UK trajectory

Despite the challenges of higher interest rates, a BTR sector in Australia is now emerging with a wave of construction activity now underway. An estimated 8,350 dedicated BTR apartments are under construction nationally (September 2023) and a further 12,900 apartments are approved for development in the near term. The pipeline is most advanced in Melbourne and Brisbane, but activity is picking up across all major cities.

The acceleration in development that we have seen in 2023 mirrors the beginning of the expansion phase that occurred in the UK from 2015 onwards. Over the following eight years to 2023, total UK stock has expanded from 11,312 to 82,636 apartments, reflecting average growth in the total stock of BTR apartments of 30% per year, or 9,450 apartments.

Based on the current pipeline of BTR developments in Australia and the demonstrated growth trajectory in the UK, by 2030 we forecast that around 55,000 dedicated BTR apartments will have been completed. This would imply an annual delivery of 5,900 apartments as supply accelerates from 2024 onwards, slower than the UK in terms of annual delivery but a similarly rapid expansion in proportionate terms. Co-living will attract investors seeking living sectors exposure with higher return hurdles

The pressure on proving feasibility for large scale BTR schemes will motivate investors with higher return hurdles to consider other forms of exposure to living sectors, and in 2024 we expect the co-living market to expand.

Private investors, syndicates and other investors with opportunistic mandates will be attracted to ability to leverage off the same thematics driving BTR, but in an alternative form that offers greater flexibility, the ability to invest at smaller scale and within the commercial residential planning framework that avoids the GST and MIT complications that can impact the feasibility of BTR.

Co-living development sites need not be as large as sites for BTR or traditional build-to-sell site and the current market is small and fragmented, offering significant opportunity to capture latent demand for a new product type geared towards shorter stay rental accommodation.

The co-living opportunity highlights the different asset types on offer within the living sectors, each with a different tenant mix, tenure length and risk profile. Investors will generally choose to specialise in one area in the first instance, but are likely to want to gain exposure across several as they build their portfolio to take advantage of emerging opportunities and benefit from diversification.

Co-living investment

Attracting investors seeking living sectors exposure with higher return hurdles

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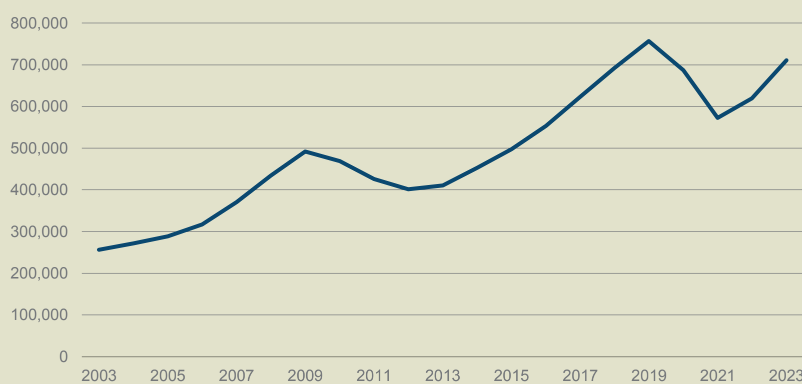
Acceleration in student demand

Driving new development beyond university precincts

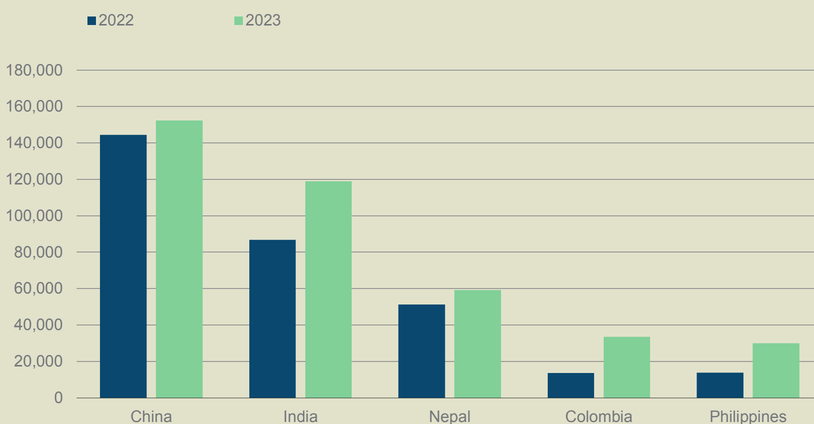
Number of intenational students in Australia

Total across all forms of education



Source: Knight Frank Research, Department of Education

Number of students - top five countries



Source: Knight Frank Research, Department of Education

The central driver of high population growth is surging inward migration, with an estimated 454,000 in net migration in the year to March accounting for 81% of total population growth.

Of these, a substantial proportion are international students, with the latest government data pointing to an increase in student numbers of 139,000 since the low point during the pandemic in 2021. Students numbers from China, India, Colombia, Nepal and the Philippines are all rising rapidly and this is creating shortages of supply for both purpose built student accommodation and also contributing to a tightening residential market more broadly.

After a period during the pandemic where the demand outlook was clearly at risk, new development has been limited, but looking ahead, we expect to see the sector reinvigorated in 2024 as momentum builds and attention shifts to how and where to boost supply.

However, site availability is becoming more restricted immediately adjacent to universities, given the expansion of the sector over the past decade. Going forward we expect to see some student schemes slightly further from universities and adjacent to other living sector hubs in well-connected urban locations such as Crows Nest and Queen Victoria Market in Melbourne. With a high degree of concentration in the sector, we expect the next phase of growth will encompass some smaller schemes as a broader range of investors seek exposure to student accommodation as part of a holistic living sectors strategy.

Capital recycling

Will drive healthcare investment activity

As investors look to increase their allocations towards alternatives, it is not only the living sectors attracting attention. Investors continue to seek greater exposure to the healthcare sector given its defensive characteristics and the long-term demographic tailwind associated with both the aging of the population and overall population growth driving consequent growth in demand.

The sector has performed strongly in recent years, with yield compression and capital growth second only to the industrial sector, and while all asset classes are facing headwinds from sharply higher funding costs, healthcare assets remain in favour as investors respond to a widening set of opportunities.

In 2024 we expect to see further turnover in sub-$20 million primary care and allied health assets, as established healthcare REIT managers seek to recycle capital to fund their development pipelines as their portfolios mature towards more sophisticated acute and day hospital-style assets. We also expect to see investors gravitating to large scale primary care and sub-acute care facilities, particularly those backed by government-funded programs such as Medicare Urgent Care Clinics, given strong security of income.

Residential

Ramping apartment supply in 2024

50 **Current developments**
Many new apartments remain grounded or in holding pattern despite tight supply

52 **Building pipeline**
New supply increasing in 2024 but not enough to push rental vacancy back above equilibrium

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Solid growth expected as higher construction costs pass through

Current developments

Many new apartments remain grounded or in holding pattern despite tight supply

The sparse number of new high-density apartment completions taking place across the country this year has resulted from the pandemic interruption three years ago which saw international and state border closures across Australia, supply chains become blocked, brakes on new apartment launches and a lack of urgency moving projects outside their early planning stage.

Despite elevated high-density site sales activity over the past couple of years, gaining building approval or turning soil on a new apartment project remains less buoyant given the challenges overhanging from inflated material and labour construction costs.

The collapse of several builders has encouraged more financiers to become actively involved in the pre-launch through to construction stages of a project, ensuring due diligence is sound for a successful completion. Once a development is approved, it now takes an average 3.3 years for an active developer to deliver a high-density apartment project to occupancy stage across Australia.

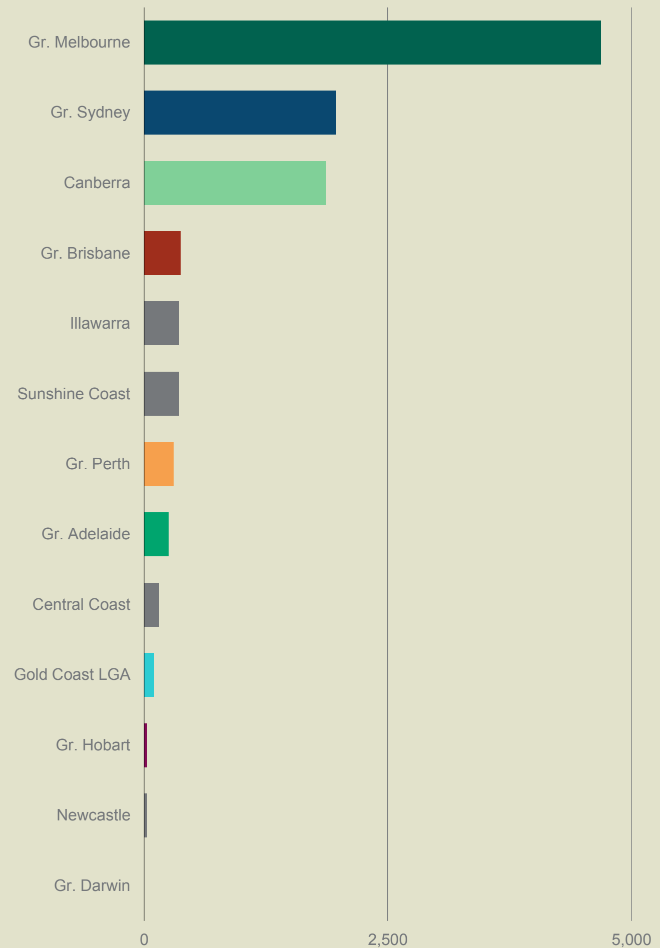
This means a fast-track solution to the lingering undersupply of affordable housing remains mostly unresolved, despite some state governments becoming more actively involved in the conversation to accelerate the planning approval process.

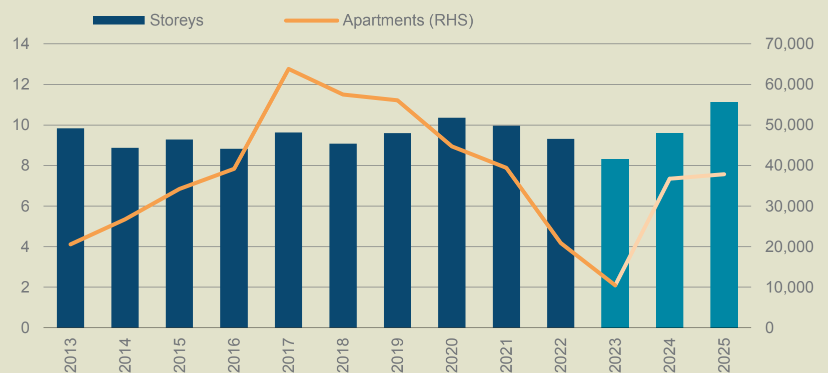
On top of this, uncertain times tend to encourage developers opting to stay in the game to kick-off their more low-risk developments. This has been no different over the past few years which has resulted in lower density apartment projects proceeding within the pipeline but has overall reduced the total amount of new apartments being built.

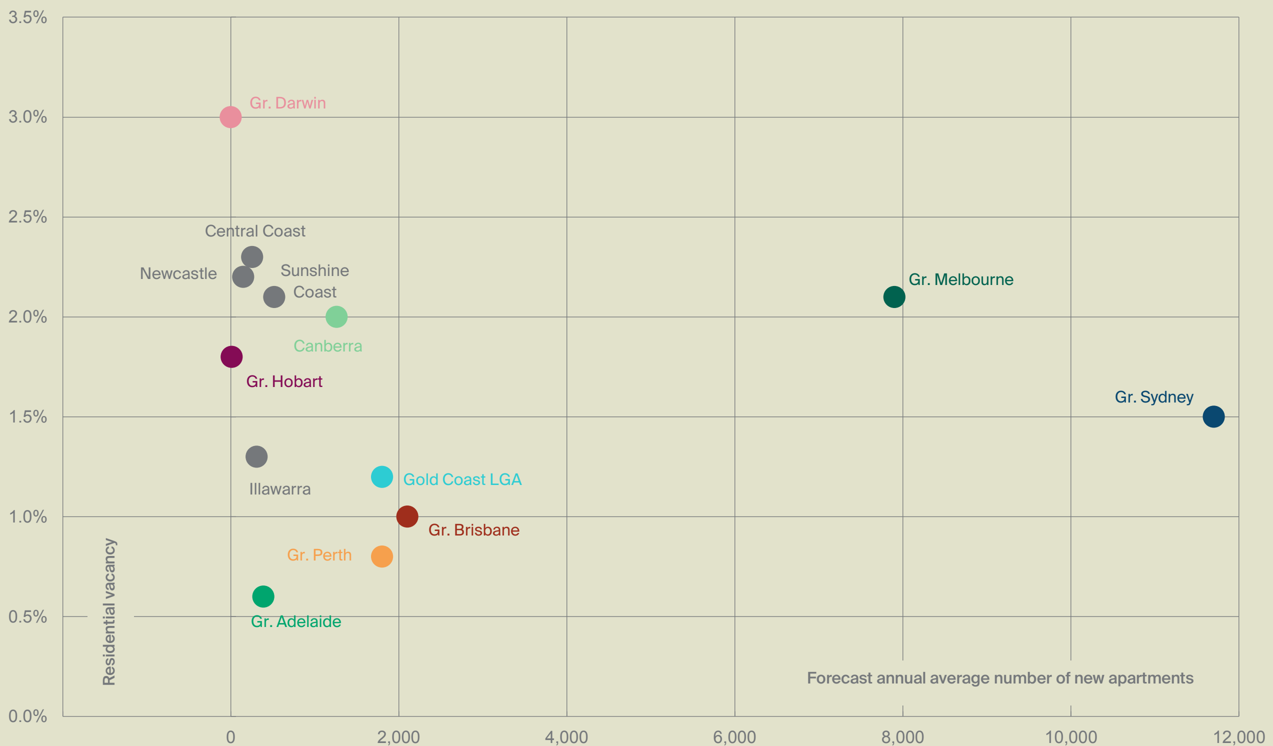
It's expected high-density apartment projects, being those with four or more storeys across the country, will average 8 storeys with a total of 10,460 new apartments in 2023, which is vastly below the 2017

average apartment tower built being at 10 storeys tall with a total 63,860 new apartments.

Greater Melbourne is forecast to record the largest share of new apartments built (4,680) in 2023, followed by Greater Sydney (1,960) and Canberra (1,860). Less than 500 new apartments are due to be completed in each of the remaining capital cities and major regional cities including in Greater Brisbane (380), Illawarra (360), Sunshine Coast (350), Greater Perth (300), Greater Adelaide (250), NSW Central Coast (150) and on the Gold Coast (100) while less than 50 new apartments are due in Greater Hobart, Newcastle and Greater Darwin.







Building pipeline

New supply increasing in 2024 but not enough to push rental vacancy back above equilibrium

Although Greater Melbourne saw the highest number of new apartments delivered in the year to June 2023, Greater Sydney (11,700) is forecast to overtake Greater Melbourne (7,900) for the highest annual average number of new apartments to be built until the end of 2025. This coincides with total residential rental vacancy in June 2023, being at 1.5% and 2.1% respectively, with both cities trending well below the typical barometer of a balanced market of 3%.

In fact, all major Australian cities are experiencing vacancy or well below this level, including Greater Adelaide with 0.6% vacancy but only an average 390 new apartments forecast annually by the end of 2025). Greater Brisbane (1.0% vacancy) has an annual average of 2,100 new apartments due to be built in this time, Greater Perth has 1,800 (0.8%), the Gold Coast LGA has 1,800 (1.2%) and Canberra with 1,300 (2.0%).

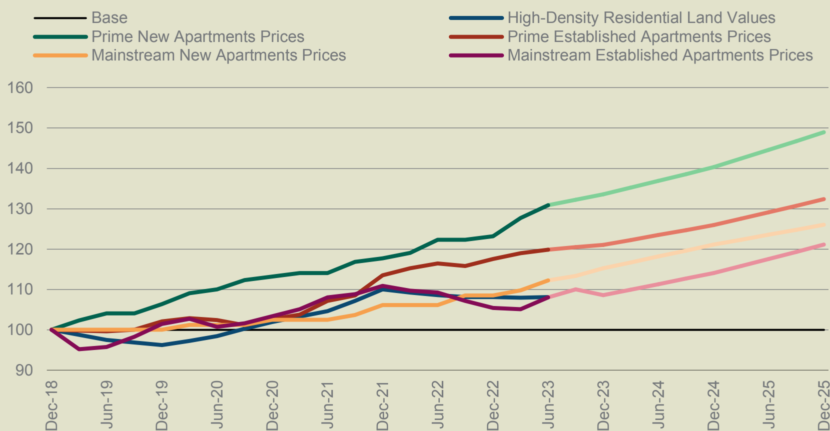
Developers not yet exploring the build-to-rent asset class continue to increasingly build more apartment product geared towards owner-occupiers. The modest group currently investing in the new apartment market and increasing the rental stock are mostly local investors, as international investors continue to face a high barrier of entry costs and keep at a distance, despite once being a solution to adding more homes to the local rental pool.

This highlights not enough private rental stock is being planned given the upward trending population growth and the current pause of investor demand following substantial mortgage rate rises over the past 18 months. This investment lull will continue to place further significant pressure on weekly rents and the availability of vacant homes in the rental pool.

Pricing outlook

Solid growth expected as higher construction costs pass through

Australian Apartments Price Performance & Forecast
Indexed, 100=Dec-18, price change



Source: Knight Frank Research

Whilst sales volume data over the past year shows a rapidly increasing share of high-density sites suitable for residential development being purchased, site values data for apartments demonstrates a decline in prices being achieved with many developers parting with sites off-market to regroup and rebalance their portfolios in preparation for better conditions ahead.

To recover higher construction costs, developers have begun lifting new apartment prices and although it's generally taking a considerably higher number of days on market to sell it than it would have taken five years ago, these prices are now being achieved from buyers who have time to consider their options.

Although there have been higher costs involved with mortgage lending, much of the activity in the apartment market has been derived from those not heavily reliant on finance and is driving up apartment prices in both the mainstream and prime markets.

The downsizing trend from the family home to a low maintenance apartment continues to take place across most parts of the country with the aging population commonly making a cash purchase given the relative comparison in value between an established standalone house and an apartment.

As a result, new mainstream apartment prices are forecast to rise annually by an average of 5% between 2023 and 2025, compared to established apartment prices rising by 4%. The limited number of new prime luxury apartments alongside the strong growth projected for the Australian wealthy populations, are further expected to achieve 6% annual price growth over the same time, while established prime apartments are more likely to average 4% annually.

Environment, Social & Governance

Winds of change as reporting requirements step up

56 **New reporting requirements**
More detailed reporting will require investment in data and processes

57 **Upgrading expectations**
Key findings from UK / European investor survey of ESG strategies

New reporting requirements

More detailed reporting will require investment in data and processes

Mandatory sustainability reporting is upon us. On 26 June, the International Sustainability Standards Board released its new sustainability standards and its impact on Australian real estate managers and investors is now clear. They will be required to provide detailed audit-ready reporting on their scope 1 and scope 2 emissions, and on scope 3 emissions from the second reporting year, with the new requirements commencing on a sequential basis from financial year 2024-25.

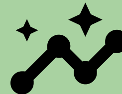
Consistent with international standards, climate-related financial information will be required to be disclosed following the four-pillar core content framework ,encompassing governance, strategy, risk management and targets.

The new standards mark a huge shift in reporting requirements to directly address emissions across the full spectrum of activities. Up until now there has not been a need to provide hard data, but now businesses will need a report with audit-ready data are and this will be transformational for property. It will require businesses to get on the front foot now with improved processes for capturing and storing data so they are not caught off guard when their reporting deadlines hit.

For many, scope 1 and scope 2 can be reported without major changes to existing processes but scope 3 presents a huge challenge and will have a cascading impact across the supply chain for all real estate managers.

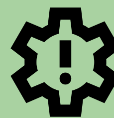
Governance

The processes and procedures used to monitor, manage and oversee sustainability-related risks and opportunities



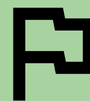
Strategy

The entity's strategy for managing sustainability-related risks and opportunities



Risk Management

The processes used to identify, assess, prioritise and monitor sustainability-related risks and opportunities



Metrics and targets

The entity's performance in relation to sustainability-related risks and opportunities, including progress towards any targets the entity has set or is required to meet

Upgrading expectations

Key findings from UK / European investor survey of ESG strategies

FLORA HARLEY
Head of ESG Research

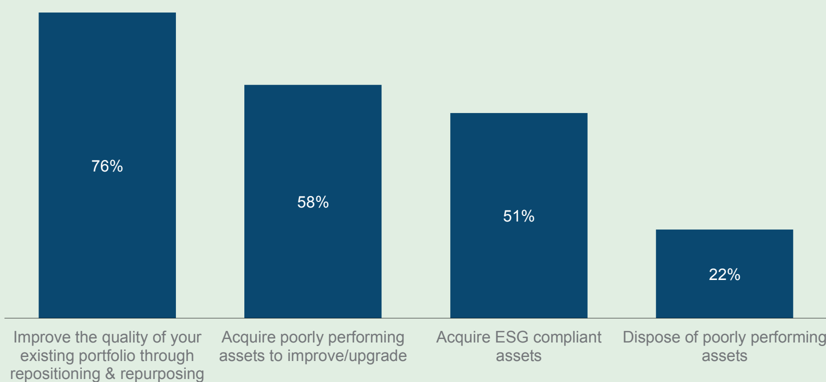
To gauge how ESG is influencing the decision making and long-term strategies of investors, in June 2023 we surveyed 45 investors about ESG and their property investments focusing on the UK and Europe. The survey participants represent nearly £300 billion of assets under management, and reflected a broad mix of investment managers, listed property companies, private investors, private equity groups, private property companies and local authorities. The results illustrate the critical influence of ESG issues and provide insight into how real estate managers are adapting to ongoing change globally and in Australia.

Photography: London, United Kingdom by Rizwan Nawaz

Improving property performance is the top focus

Improvement the top priority

Q: What is your focus on ESG in relation to property (select all that apply)

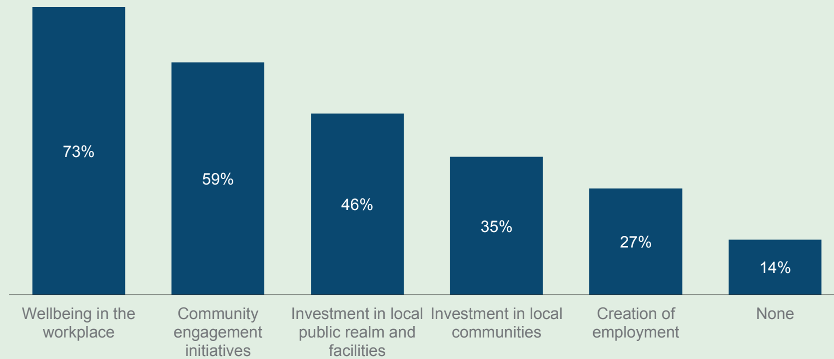


Source: Knight Frank Research

Three-quarters of surveyed investors say they want to improve the quality of their existing portfolios by refurbishing and repurposing. In addition, 58% are looking to acquire poor ESG-performing assets with the aim to improve and upgrade. Several investors have launched 'impact funds' to achieve exactly this. Knight Frank's capital markets teams are regularly working with investors to actively target the acquisition of such assets, often from asset owners who do not have the appetite, capability or funds to improve the ESG characteristics. Of those investors surveyed, fewer than a quarter are looking to dispose of poor-performing assets in favour of higher performing ESG assets – however among investors with a dedicated core focus this rises to 40%.

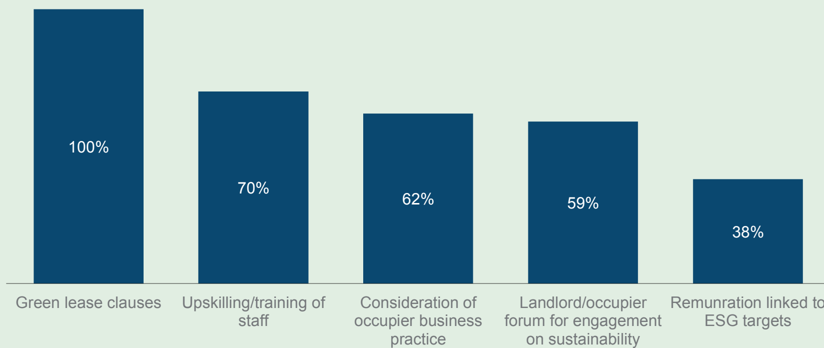
Of the investors who stated their company's net zero target, one has already reached this goal, 41% are committed to 2030, 15% look towards 2040, and the remainder are targeting 2050. We believe such aggressive short-term goals will only exacerbate the premium for the most sustainable core assets. Those targeting 2030 are seeking to get ahead given that three-quarters of countries globally have a pledge, proposal or law requiring net zero be reached by 2050, the UK and EU included. Real estate will play a pivotal role for organisations on their net zero journey which is evident in our survey findings.

Wellbeing a top social target
Q: Do you have social-based targets (select all that apply)



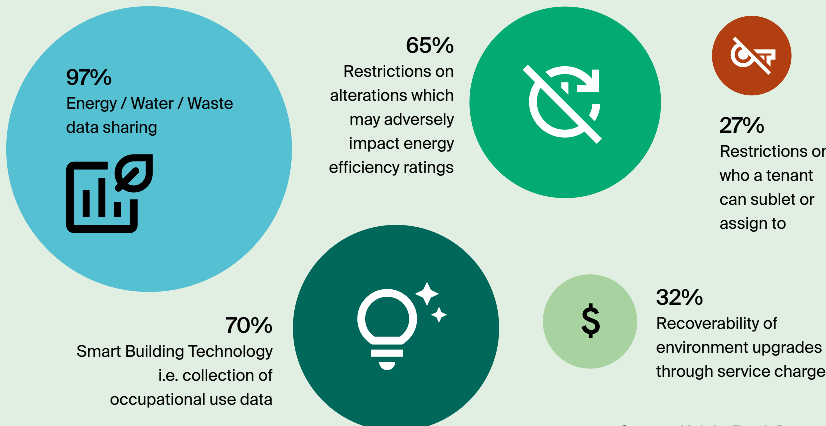
Source: Knight Frank Research

Supporting structures
Q: What structures do you have in place to realise your ESG targets (select all that apply)



Source: Knight Frank Research

Smart Sharing
Q: Regarding green / sustainability clauses in leases, which of the following do you include?



Source: Knight Frank Research

90% of respondents had social targets

Wellbeing in the workplace is a goal for 73% of the investors surveyed, whilst almost 60% target community engagement initiatives and 46% are pursuing investment into local public realm and facilities. These could include amenities for physical and mental wellbeing, such as cycle facilities and support networks, both are amenities which occupiers expect employees to require according to our latest (Y)our Space research.

87% of the investors surveyed stated that they have a dedicated in-house ESG team, with 44% saying that the team consists of five or more people. Size matters here, as all surveyed investors with £10 billion or more in AUM have an in-house ESG team, whereas only 77% of those with £500 million to £5 billion do. This level of expertise is likely to increase ESG due diligence on new acquisitions as well as reporting for disposals.

100% of surveyed investors stated they use green leases as a way to realise ESG targets

Investors feel that green leases are a vital in order to realise ESG goals, so we expect them to become even more commonplace and standard across the industry. When asked what provisions they include within these leases, 97% selected energy/ water/ waste data sharing, 70% look to have smart building technology that can aid data collection and maximise efficiency through, for example, monitoring and automated systems for heating, cooling and lighting. Almost two-thirds include restrictions on alterations which may adversely impact energy efficiency ratings.

Your partners in property