01 02 A NEW ERA OF OFFICE DEMAND

The Future of Office Series

SEP 2024

Introduction

Over the last four years, Office has experienced one of the most significant impacts to the sector in the modern era, driven by change in worker preferences and a heightened focus on space utilisation stemming from the pandemic period.

However, change is inevitable and although conditions over the past few years have supercharged many evolving trends, it is time to acknowledge the structural shifts that are now occurring within the sector. Office is experiencing a period much like the retail sector has already endured as online retail trends heightened the focus of retailers on how to adapt their physical space to changing consumer preferences. The result has not been the demise of physical retail but led to a period of adaptation that has resulted in a hybrid approach to physical retail and e-commerce and a shift to more experience-based retailing. The office sector is now at the forefront of its own period of adaptation and many new trends are shaping the sector for the future.

In this five-part series, we aim to explore these trends bringing together both our research expertise and business expertise to explore the future of office.

Part 2 - A new era of office demand

The future of office demand has been grappled with by occupiers and investors alike, as changing workforce patterns and a reassessment of space requirements has begged the question – how much office space will be needed into the future. The evolution of office has now been galvanised by a shift in values, ensuring that an asset originally designed as a space for shared resources in the 1900s, now emphasises employee health and wellbeing, fulfilment, productivity and much more.

While the conversation is still evolving, new themes and considerations are re-shaping the occupier decision making process and ushering in a new era of office demand.

01

Occupier preferences – the new, the old and everything in between.

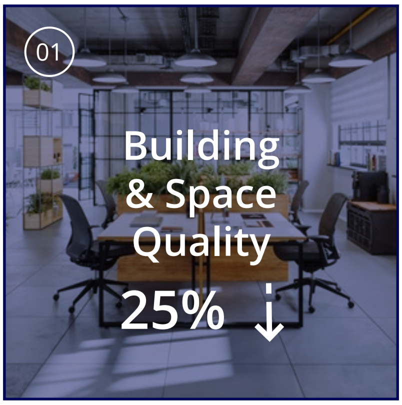
Before delving into the future drivers of office demand, it is crucial to address one fundamental aspect: the occupier. The key question is whether occupiers are rethinking their approach to office space. The evolving dynamics of how we physically work, perceptions of work and interactions within the workplace are reshaping the key criteria that occupiers consider in their decision-making process.

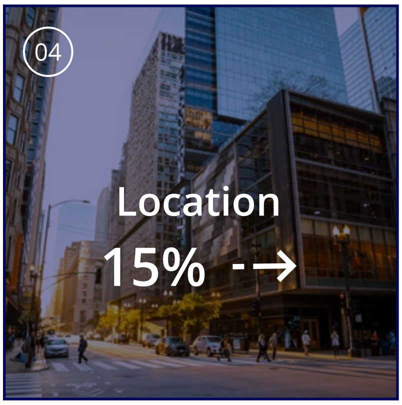
According to recent insights from the Colliers tenant representation team, the most significant shift in occupier decision-making has been an increased focus on employee experience emerging over the past 12-24 months. This shift has been mostly influenced by the immediate impacts of flexible working arrangements and efforts to bring employees back to the office. It also reflects a broader, long-term shift in societal values, which now places greater emphasis on employee health, well-being, and fulfilment. While factors such as the quality of the office building, office space, and cost still constitute about half of the decision-making process, their relative importance has decreased as more weight is given to employee experience.

Considerations related to Environmental, Social, and Governance (ESG) factors have also gained more prominence, now accounting for around 15% of the decision-making process. In 2019, financial considerations for tenants primarily focused on cost per seat. Today, tenants are increasingly considering the cost impact of how well a building supports their ESG commitments, alongside overall experience requirements. Colliers will explore the impact of ESG in greater detail in Part 3 of the Future of Office series.

What is driving occupier decisions

Occupier Weightings Towards Key Decision Making Criteria for Office Space





Note: Arrows represent if the weighting towards this component of decision making has increased, decreased or remained the same over the last 12 months.

“

The Employee experience has become central to the occupier decision making process with the shift to a flexible workforce meaning the focus is not on 100% of the workforce being in the office 100% of the time, but on how the office brings the workforce together to collaborate and promote company culture. The location of the asset is a critical component to achieving this goal and supporting office as a core workplace destination, and not just a place to work.

Sarah Hughes
National Director,
Tenant Advisory, Occupier Services

02

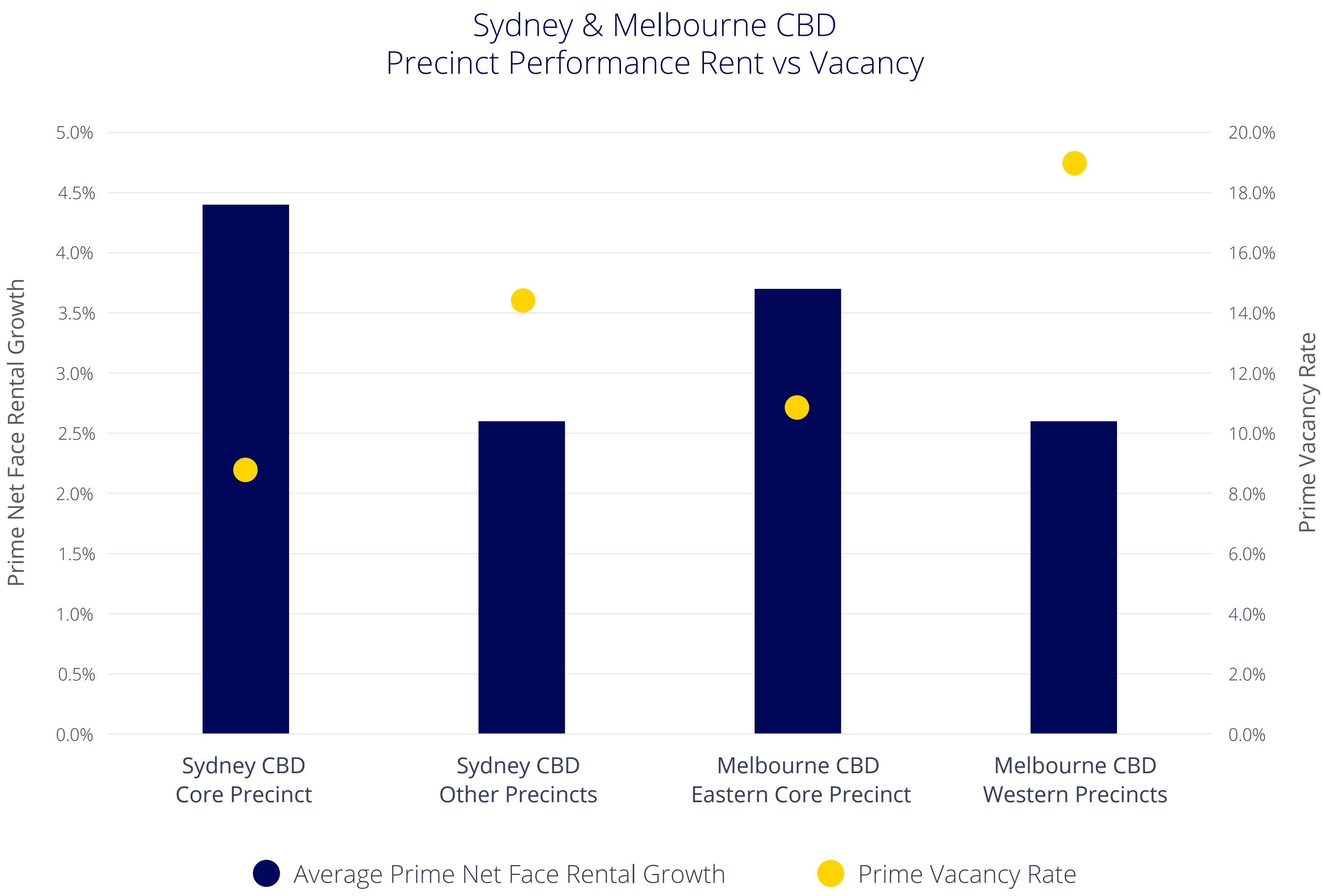
Location matters - widening the experience net to both asset and location

Location remains a crucial factor in the occupier decision-making process. Companies seek a location that supports their business operations by being close to both their client base and operational infrastructure, while also balancing the cost and commercial parameters available to them within that location. However, a new layer has emerged that is shifting the needle in the occupier decision making process: the role of the location in enhancing the overall experience of employees when they attend the office.

The location of an office asset has become integral to creating a vibrant workplace environment, transforming the office from merely a place to work into a core destination for employees. This shift represents an evolution from the traditional "flight to quality" trend, which focused primarily on the quality of the asset itself. Now, the emphasis has expanded to include the office's surrounding area and amenities, giving rise to a "pull-to-precinct" trend. This trend highlights the increasing importance of the broader precinct and its amenities in shaping office demand across Australia's office markets.

The concept of 'pull-to-precinct' has varied across Australia's office markets and has influenced leasing activity in different ways. Sydney and Melbourne's CBD's 'pull-to-precinct' has been more literal with shifting demand toward core hubs that offer greater vitality, as well as options and proximity of amenity such as cafés and restaurants, gyms, health facilities and essential retail services.

In the Sydney CBD this trend has led to increased leasing activity in the Core precinct over the past two years. Sydney's Core precinct net absorption has outperformed the wider market recording 33,400 sqm of positive net demand (according to latest PCA statistics as at July-24), whereas the remaining five office precincts recorded negative net absorption totaling 163,000 sqm. A similar pattern has been observed in the Melbourne CBD where despite negative net absorption in some precincts, the North-Eastern precinct recorded positive net absorption of 1,840 sqm over the last two years, with the adjacent Eastern Core precinct recording Melbourne's lowest vacancy rate at 10.8%. Both Sydney and Melbourne CBD occupiers have had to reassess their office strategies more extensively than in other markets over the last two years. They have increasingly focused on ensuring that both the office space and its location contribute to a comprehensive and engaging workplace environment for their employees, supporting a successful return to the office.



Source: Colliers Research, PCA

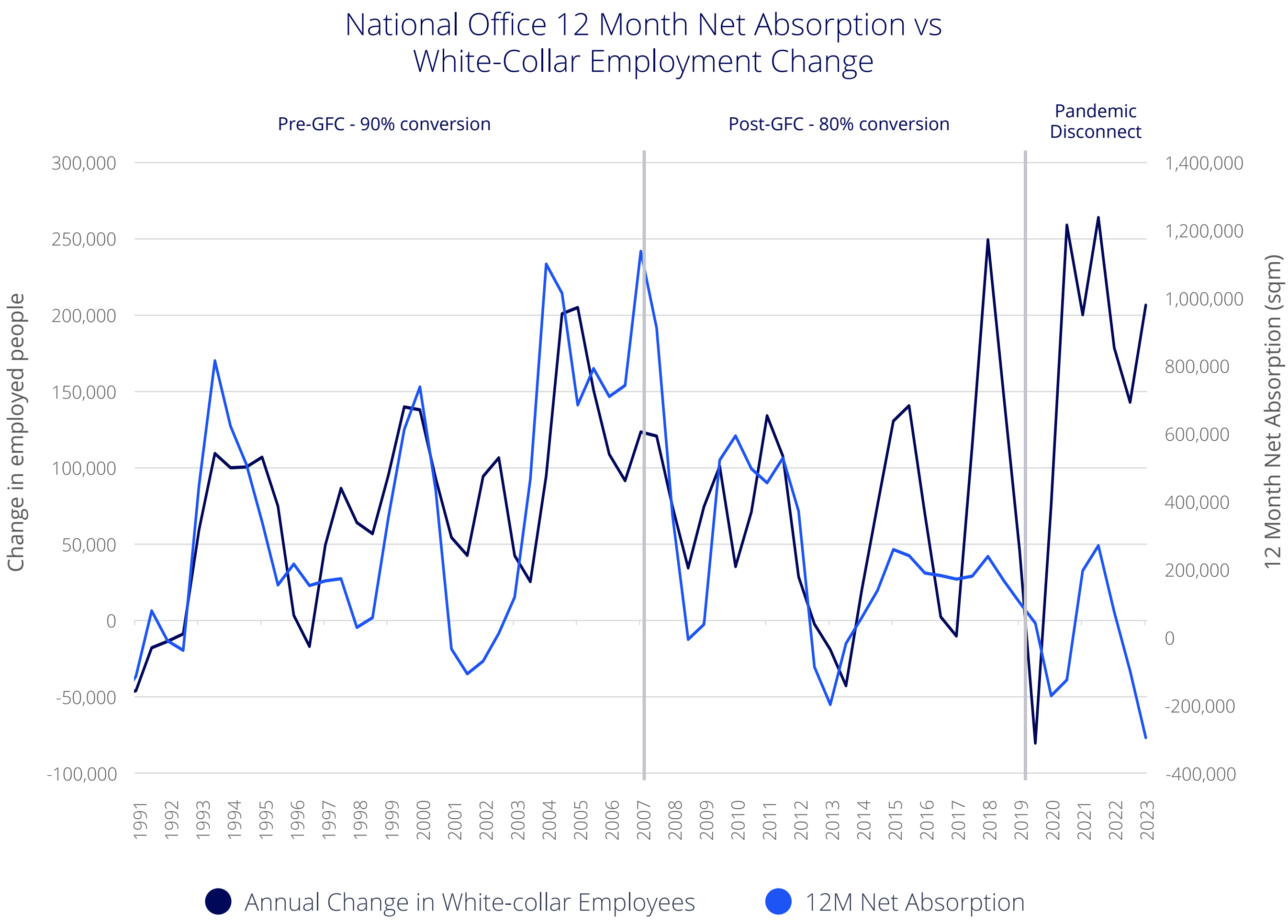
The thematic presents differently in the Brisbane, Perth and Adelaide CBD's as well as periphery CBD locations, with these markets not as geographically partitioned into precincts in the same way as Sydney and Melbourne. However, a strong flight to quality thematic by relocating tenants has led to lower vacancy rates in Premium or New-A grade space, while recent office developments have brought a new generation of office assets to these markets creating a destination in themselves. Brisbane CBD, in particular, has witnessed some of the strongest levels of leasing demand nationally with thriving economic conditions driven by strong population growth over the last two to three years. Brisbane CBD's Premium grade vacancy rate is the lowest nationally at just 6.5%.

03

A new shift is occurring in the conversion of employment growth to office space demand as the relationship adjusts to a new era of workforce flexibility – but it's not the first shift!

Historically, office demand patterns have followed a predictable trend. Typically, we have estimated office space demand based on forecasts of white-collar employment growth, which in Australia has been supported by strong population growth and economic resilience. Consequently, white-collar employment growth and office net absorption have historically been highly correlated, although the conversion rate of jobs growth to office sqm's has varied over time.

Before the Global Financial Crisis (GFC), workspace ratios generally ranged between 1:10 and 1:13 square meters per employee. During this period, occupiers often included additional space for future growth when relocating. As a result, the conversion rate of jobs to office space was high, estimated at around 90% of additional jobs translating into office sqm's. However, following the GFC, companies became more cost-conscious due to funding constraints. Workspace ratios tightened to improve floor space efficiency, and the need for additional space was less pronounced, with some excess space still lingering from the recession. Consequently, the conversion rate of jobs to office space decreased to around 80% in our estimates post-GFC.



Source: Colliers Research, PCA, DAE Employment Forecasts

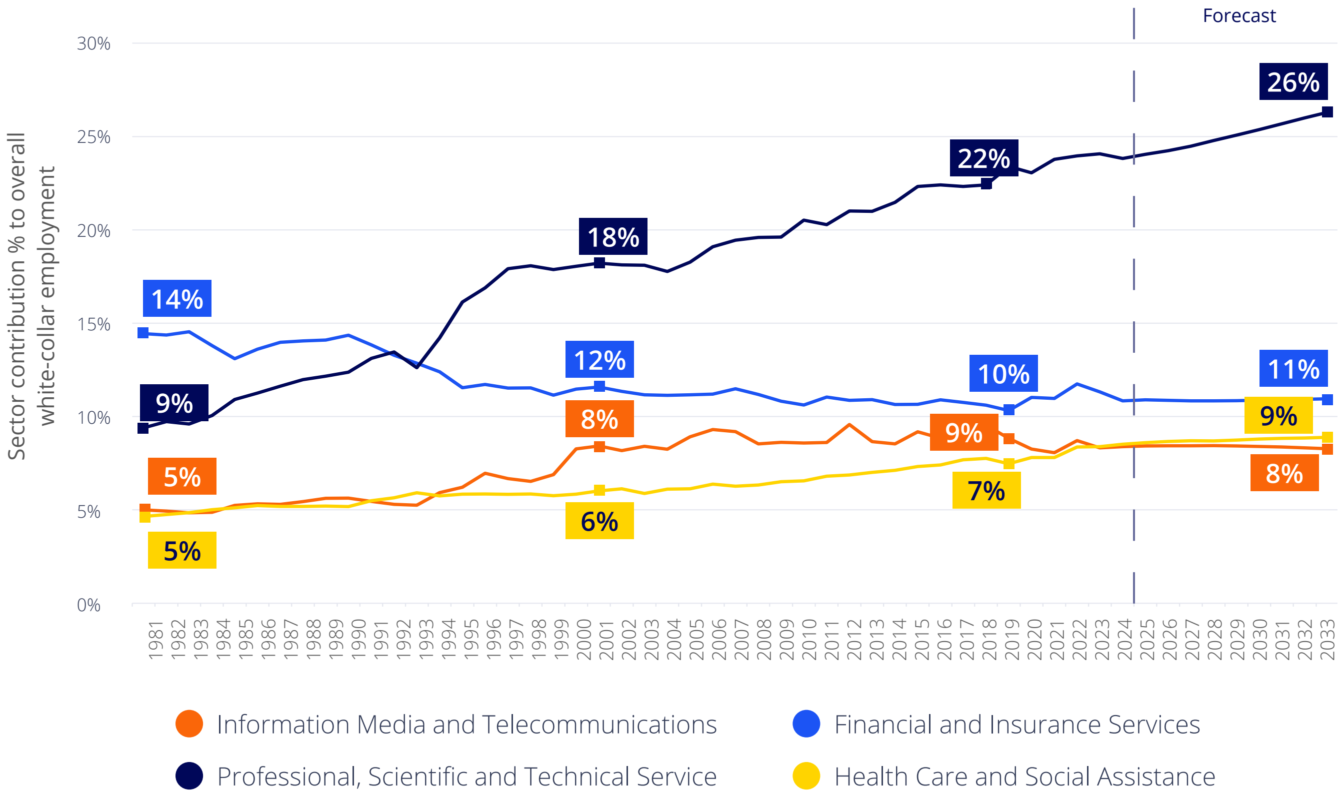
A third shift is now occurring as companies reconsider how they utilise their office space to ensure it caters to a flexible workforce and creates an environment that fosters collaboration and strengthens company culture in one destination. Flexibility is key, and additional space for future growth is being leased more strategically with flexible floor plans and adaptable third spaces becoming essential within current office space planning. The disconnect between employment growth and office net absorption, driven by the right sizing of companies over the last few years, will start to rebalance. As such, we expect that the relationship of jobs growth to office sqm's to return over the next 12 to 24 months with a new conversion rate of jobs growth to office sqm's moving forward of around 70% to cater for a new era of flexibility in both workforce dynamics and office space needs.

04

Although white-collar employment will continue to underpin office space growth, not all white-collar contributions to demand will be equal.

The Finance and Insurance industry sector has traditionally been the largest contributor to office demand, linked to its performance as one of the largest contributors to the gross value-added measure across Australia's economic growth profile. Although the Finance and Insurance sector is decreasing its share of jobs growth as a proportion of total jobs, and its weighting as a proportion of office demand, the sector still underpins one of the largest shares of leasing activity across Australia's office markets. Recent Colliers data shows that the Finance sector was responsible for the largest take-up of CBD office space transacted in H1 2024 equating to 21% of the total area leased. However, demand from the sector is now being driven by office requirements from small-to-mid sized finance and investment institutions, as opposed to the larger banks and finance institutions and we expect this trend to continue.

White-Collar Employment Industry Sectors
as a Proportion of Total White-Collar Employment



Source: Colliers Research, DAE Employment Forecasts

However, over recent years, Professional Services and Health sectors have overtaken the finance sector in contributions to the economy due to the rise in demand for essential services. In particular, demand in the health sector has been gathering pace and has been one of the most active industries during the first half of 2024. Non-CBD office markets are especially well-positioned to capture demand from the Health and Medical sector, with companies being close to population growth corridors and health infrastructure, while benefiting from the opportunity to lease more cost-effective space within key office locations. As such, the Health and Community Services sector was responsible for the largest area of space transacted across Australian metropolitan locations over H1 2024 comprising 16% of leasing activity.

Looking ahead, DAE Employment Forecast data shows that the weightings attributed to different white-collar sectors as a proportion of total jobs growth are shifting and is therefore expected to impact office demand moving forward. While the Finance and Insurance sector is expected to decrease from an average of around 12% (long-term average) to around 11% over the next 10-years, the Professional and Scientific Services (17% to 25%) and the Health Care sector (6% to 9%) will experience a greater shift over the forecast period, albeit noting that there will be a proportion of jobs within these sectors that are not traditionally office based. Many Professional, Scientific and Technical Services and Health Care jobs that are office-based in nature will be more geared toward in-person office attendance as opposed to hybrid office participation due to the higher face-to-face component to these industries. In contrast the finance and insurance sector will be more attuned to flexibility of the workforce.

For long-term growth, the TMT (Technology, Media and Telecommunications) sector holds significant potential and is expected to maintain a notable share of office demand, though at a more sustainable level compared to historical trends. The sector's contribution to white-collar employment growth is anticipated to remain relatively stable over the next decade, averaging around 8% per annum. down from a high of approximately 12% in the early 2000s. New jobs within the sector will be driven partly by the widespread adoption of artificial intelligence (AI) and emerging technologies, along with government initiatives aimed at expanding the technology sector. While the long-term impact of AI on overall jobs growth remains uncertain, historical trends suggest that technological advancements both displace some jobs and create new ones across different industries. These new roles may not always fall under the traditional TMT classifications, but could involve integrating AI with other skillsets such as marketing and design, data analytics, and administrative functions.

Although industry dynamics are shifting, we expect core business functions and core sectors such as finance, legal, and professional services to continue to underpin the majority of leasing activity within CBD markets and we anticipate non-CBD markets will see an increase in occupation from essential services occupiers such as the medical and health care sectors, technology and supporting business functions.

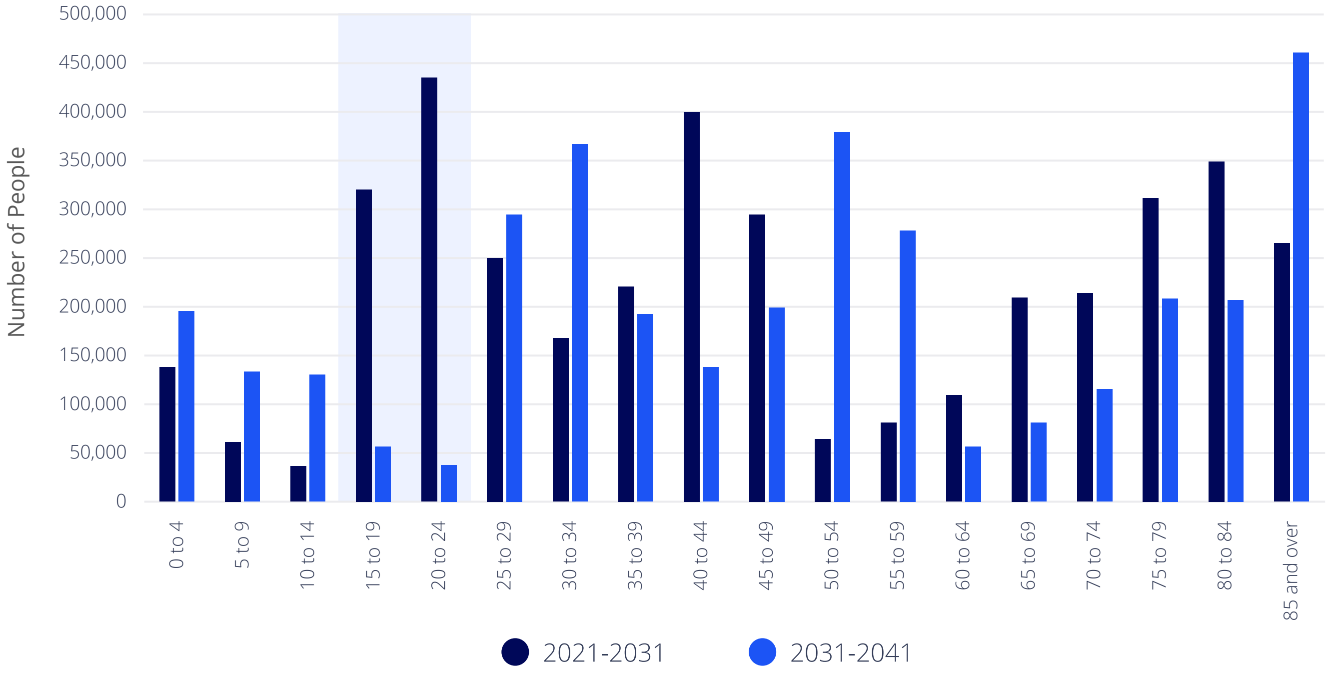
05

Experience will continue to matter into the future to align to future generational workforce shifts and diversity.

Australia is poised for significant demographic shifts in the coming years. The population is projected to increase by 3.3 million, reaching 30.4 million by 2031, largely driven by net overseas migration, contributing to an annual influx of 242,000 people. This growth will impact various age groups, with notable increases anticipated in the 15 to 24 age bracket, reflecting a rise in young professionals, typically with tertiary education and some degree of independence. Concurrently, there will be a growing number of parents and homebuilders in the 40 to 44s, a segment of the millennial generation seeking greater flexibility. Additionally, the ageing population is likely to work longer due to advances in health and longevity that will enable many people to keep working beyond what we perceive as retirement age today.

As Generation Alpha (born between 2010 and 2024) begins entering the workforce, they will bring advanced technological skills and high expectations for digital integration in the workplace. This generation will seek continuous learning and development opportunities. Meanwhile, Generation Z, known for their tech-savviness and comfort with remote work, will most likely favour flexible working arrangements. Millennials have already shaped the office environment with a focus on wellness, leading to the inclusion of amenities such as gyms, meditation rooms, and wellness programs. These generational preferences have driven the adoption of features such as open floor plans, breakout areas, and advanced communication technology to date. However, with an increasing number of workers approaching retirement, there may be a need to create spaces dedicated to knowledge transfer programs, as well as flexible working arrangements including part-time or phased retirement options.

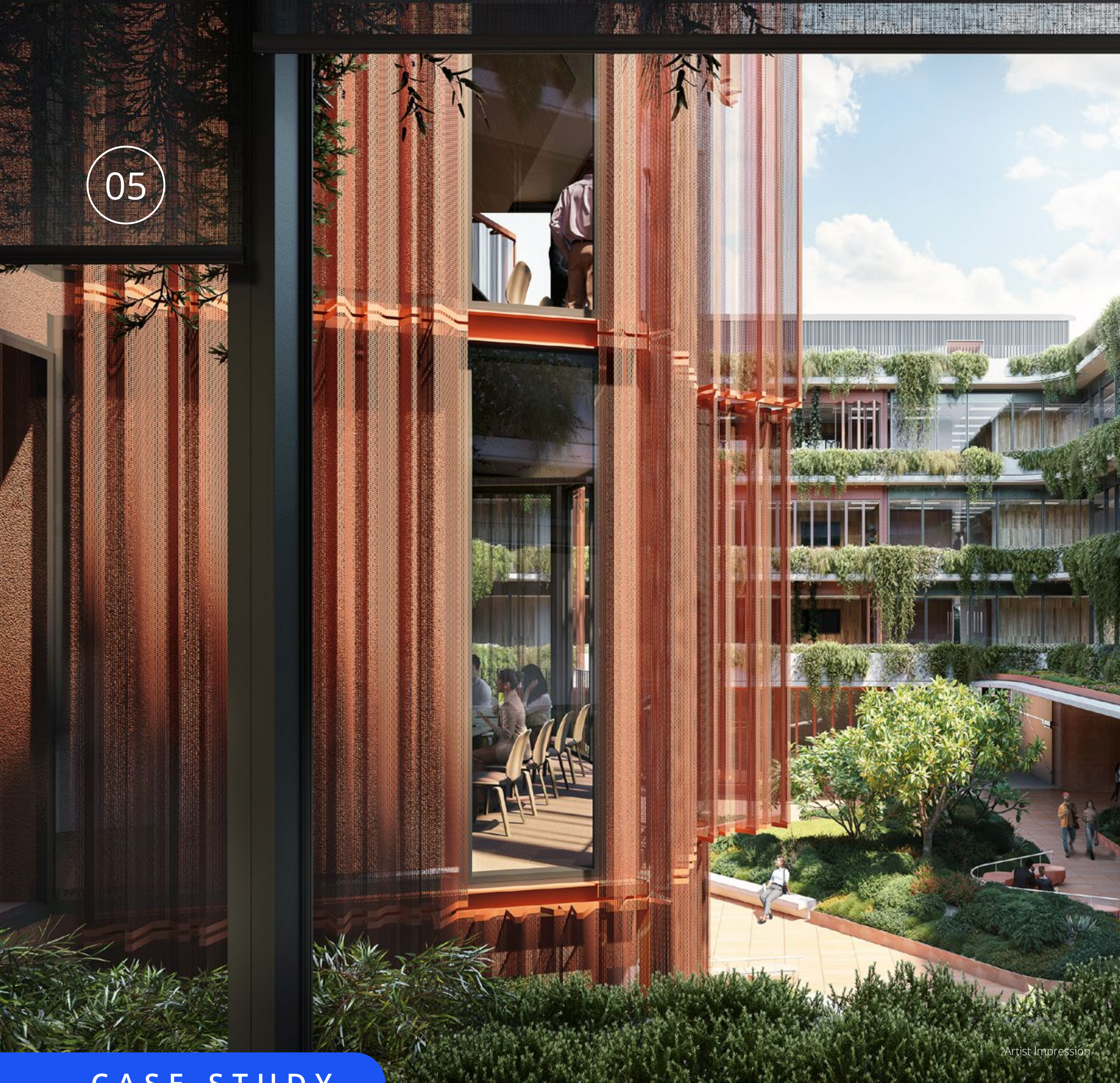
Rapid Growth Expected in the 15-24 Age bracket by 2031



Source: economy id/Colliers

These demographic changes are expected to drive significant transformations in office design to accommodate the diverse needs and preferences of a multigenerational workforce. As the workforce evolves, office environments are likely to incorporate ergonomic features and accessible facilities, including wheelchair accessibility, to support an aging population. At the same time, future generations will benefit from advanced technologies such as VR and drones. Flexibility and inclusive design will also become increasingly important.

With Australia's projected population growth largely fuelled by overseas migration, office designs are anticipated to become more inclusive, adaptable, and culturally sensitive. This trend is already visible in some workplaces, which have started to include amenities such as prayer rooms and meditation spaces. Over the next decade, as people work longer and generational diversity increases, offices will need to address varying skills and attributes brought by different age groups. This will require thoughtful consideration of how to best support each generation and their unique working styles within the office environment.



CASE STUDY

Bourke and Bowden
25 Bourke Road, Alexandria, NSW

Time and Place and Hickory have collaborated to challenge the convention of commercial workplaces with Bourke and Bowden. Located on the tech fringe, within the creative hub of Alexandria, Bourke and Bowden's 16,500 square meters of commercial and retail space across four levels represents the office experience from a neighbourhood perspective.

Shared areas and communal places for tenants beyond their footprint, push the boundaries for building an authentic community. Bourke and Bowden is also designed for work and life, raising the bar on building amenities.

Key Features

Three levels of flexible workspace, each with 4,500sqm NLA

1,000sqm central courtyard

Digital tenant portal

Three lookout meeting rooms on each level comprise the Treehouse, placing focused and team working spaces in a dedicated, nature-inspired environment

500sqm rooftop terrace, which is versatile enough to switch between a gathering space for speakers and entertainment, after-work drinks and one-off events

The lobby is designed to provide Sydney's first work hotel experience, eliminating boundaries between workplace and hospitality

Pre-commitment to a prominent wellness operator offering premium bath house facilities to the development

Luxury end-of-trip facilities also form part of the Club House including, 16 private showers, 115 bike stalls and 115 lockers

Environmental credentials including PCA A-grade, targeting 5.5 NABERS Energy Rating (6 Star with Green Power), as well as targeting 5 Star Green Star Design As Built rating.

Bourke and Bowden is located at the epicentre of a rapidly rejuvenating neighbourhood

172 car parking spaces within lower-level basement

10 Electric Vehicle (EV) charging stations and 3 GoGet Car Share vehicles

Leasing Agents

Michael Crombie
National Director, Property Sales & Leasing,
Director in Charge, South Sydney, Colliers

Jackson Wray
Associate Director, Property Sales & Leasing
South Sydney, Colliers

Justin Rosenberg
Associate Director of Office Leasing,
Sydney Fringe and South Sydney, Colliers

Developers

TIME& PLACE

hickory

Architect

Wardle

Interior Architect

FLACK

“

Designed by John Wardle Architects with interiors by Flack Studios, this is the most ambitious and future-forward building at the epicentre of a rapidly rejuvenating neighbourhood.

Tim Price
Director
Time & Place

“

We are passionate about the evolution of the South Sydney office precinct. We think Alexandria is the most exciting part of this market.

Peter Kazaglis
Head Of Commercial & General Manager - Development (NSW)
Time & Place

“

The design of Bourke and Bowden in Alexandria offers an experience beyond office floorspace, creating a flexible environment where workspace and wellness amenity are intertwined to build an authentic and creative community.

Edward Pearse
Director
Time & Place

“

Bourke and Bowden will set the benchmark for quality, next-generation offices and serve future communities for decades to come.

George Abraham
Managing Director
Hickory

“

The plethora of greenery and extensive integration of natural elements significantly shape the experience of Bourke and Bowden’s inhabitants and visitors. The vast central courtyard, treehouse meeting areas and expansive rooftop are examples of powerful nature-based interventions, which have been proven to enhance visual information processing speeds, attention and lower stress and cortisol levels. Renowned designer Frank Lloyd Wright articulated the purpose of biophilia well when stating; “I go to nature everyday for inspiration in the day’s work. I follow in building the principles that nature has used in its domain.”

Bourke and Bowden also represents the current trend of emphasising employee health and wellbeing, by supporting employees in a more holistic sense, with features such as extensive natural light and a luxurious wellness centre. Research shows that physical, mental and emotional health is linked to optimal performance and productivity, in addition to a better quality of life, lower risk of disease and injury, and greater likelihood of community contributions.

Workers at Bourke and Bowden are also encouraged to be their best selves with diverse single and team workspace options, which support neurodiversity. Tenants can choose from meeting rooms which open into the courtyard on the ground level or those ensconced in greenery on higher floors, to enclosed office areas and a range of communal spaces also enabled by the latest tech. Leading firms are increasingly endorsing catering for neurodiversity, encompassing ADD and autism in addition to introverts and extroverts, encouraging new and diverse ways of thinking and problem-solving, delivering innovation and a competitive edge.

The vibrant neighbourhood design also serves to benefit collaboration by providing numerous ‘bump spaces’ – no pressure environments for interaction, which traverse roles, divisions, and hierarchy, for knowledge sharing and enhanced personal rapport.

Bourke and Bowden truly sets a new benchmark for office design supporting employees holistically for productivity, wellbeing, innovation and a positive culture.

Karen Primmer
Head of Workplace and Transformation
Occupier Services, Colliers

*Artist Impression

“

Bourke and Bowden is a new generation building for the next generation of worker, rethinking the office experience from a neighbourhood perspective.

Justin Rosenberg
Associate Director of Office Leasing,
Sydney Fringe and South Sydney, Colliers

What does this mean for **tenants**?

- High demand for key locations and quality assets will see options start to diminish in these segments of the market, as well as higher rental growth than the market average. However, there is still opportunity to secure OpEx savings on an effective rent basis, particularly for tenants who entered leases at the height of the market end 2019/beg 2020. Ample lead time is needed before expiry to lock in desired locations and assets so compromises can be minimised.
- As key precincts and assets fill-up, a knock-on-effect to alternate precincts is expected to play out and as such more cost-effective options may be available over the next 12-24 months driving flight-to-value activity.
- Employee experience will continue to improve as landlord's explore new and exciting ways to stand out from the competition (e.g. wellness rooms at 333 Kent Street and 201 Kent Street). This will give tenants more choice of buildings that offer superior amenity and will be the most favoured assets by businesses as a way to give more to their employees.

What does this mean for **owners**?

- Tenant attraction and retention strategies are growing in importance and owners need to ensure they remain up to date with occupier preferences to ensure their asset remains competitive. Building amenity is now expected to be more hospitality like in its experience and is moving beyond basic end-of-trip facilities – constant innovation in this space is a must!
- Assets with experience central to any upgrade works will reap higher rental growth than the market average and shorter let-up periods.
- Asset positioning strategies to attract a wide range of tenant industry types will help to diversify tenant profiles and reduce leasing risk.
- When providing speculative fit-outs, the atheistic, design and flexibility is key to ensuring assets are shortlisted amongst a market with a larger pool of options for tenants. Carefully considered design that appeals to a diversified workforce will continue to grow in importance.

What does this mean for **office investment**?

- Early movers are following the occupier thematic as the recovery phase of the current investment cycle begins, with key CBD transactions occurring in key precincts such as the Sydney CBD Core.
- Value preservation through future proofing assets to meet changing occupier requirements will allow owners to benefit from stronger rental growth opportunity and higher occupancy levels.
- Investor confidence has returned, partly underpinned by positivity around the leasing thematic in core locations, as well the potential for interest rate cuts on the horizon. As such Core investors, both domestic and offshore, have returned to Core office precincts and will deepen the buyer pool moving forward creating increased competition for assets.
- Currently assets can be purchased at yields with comfortable clearance above all-in borrowing costs. Increased leasing momentum and forecast interest rate cuts will widen this delta.

Author

Jo Henderson
National Director,
Research

Office experts

Cameron Williams
Managing Director,
Office Leasing

Richard Garing
Managing Director,
Occupier Services

Karen Primmer
Head of Workplace Innovation
and Transformation,
Occupier Services

Adam Woodward
Head of Office,
Capital Markets

Dwight Hillier
Managing Director,
Valuation & Advisory Services,
Strategic Advisory & Healthcare
& Retirement Living

Matt Meynell
Managing Director,
Investment Services

Scott Jackman
Managing Director,
Project Leaders

Julia Batterley
Managing Director,
Real Estate Management
Services

Sarah Hughes
National Director,
Tenant Advisory,
Occupier Services

Simon Crouch
Head of Tenant Advisory,
Occupier Services