FORCES FOR CHANGE

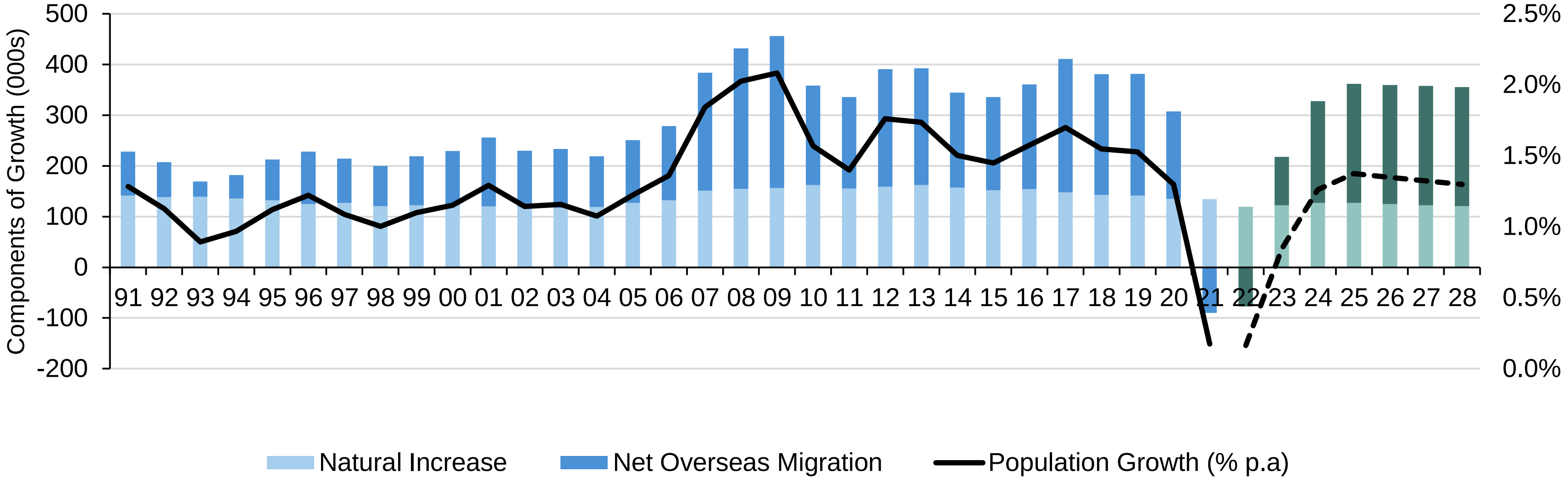
URBIS

Risk and recovery in the post-pandemic economy

Prepared for PFA

May 16th 2022

THE PANDEMIC HAS DISRUPTED AUSTRALIA'S NET OVERSEAS MIGRATION GROWTH DRIVER

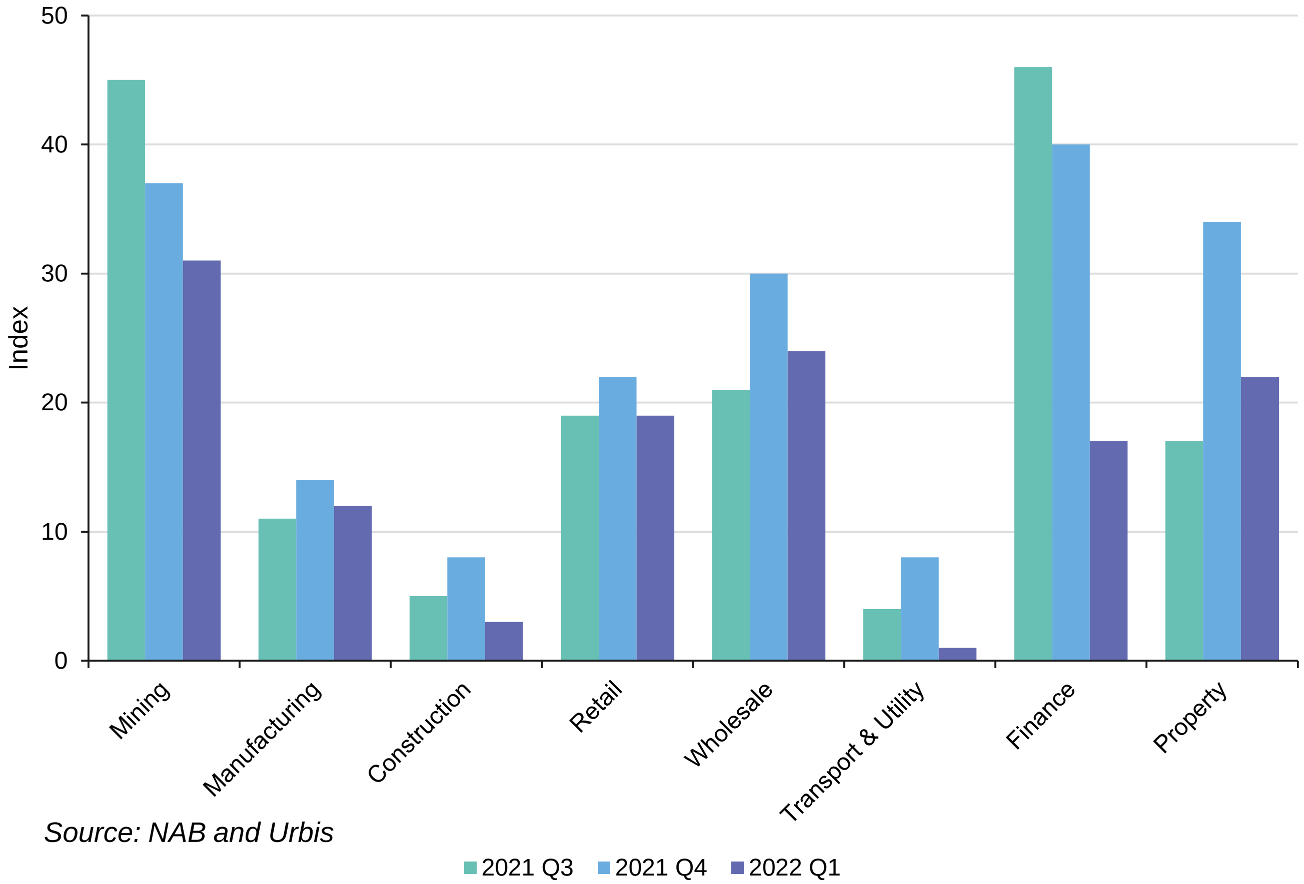


Source: ABS, Consensus and Urbis

The return of net overseas migration is likely to see increased demand for greenfield lots, driving up industrial land costs in outer-suburb spaces. Conversely, population and density increases are likely to flow through to demand for smaller, more flexible industrial spaces which can fulfil same-day fulfilment and/or multi-purpose use in inner-city locations.

Net overseas migration should re-emerge as a key driver of growth, with rises of 2% per annum from 2023-24.

THE PANDEMIC CONTINUES TO CAST A SHADOW OVER BUSINESS OPERATING CONDITIONS



Source: NAB and Urbis

Business conditions have declined overall from Q4 2021 to Q1 2022. While remaining positive, overall business conditions have fallen by 5 index points in Q1.

CAPACITY TO ADAPT TO THE POST-PANDEMIC WORLD VARIES ACROSS THE NATIONAL ECONOMY

STATE/TERRITORY	Output capacity	Business confidence & Investment intentions	Population growth	Financial position	Regulatory environment	Infrastructure pipeline
New South Wales	Contractionary	Neutral	Neutral	Neutral	Neutral	Expansionary
Victoria	Contractionary	Neutral	Neutral	Contractionary	Expansionary	Expansionary
Queensland	Contractionary	Expansionary	Expansionary	Contractionary	Expansionary	Expansionary
Western Australia	Contractionary	Neutral	Expansionary	Expansionary	Contractionary	Expansionary
South Australia	Neutral	Contractionary	Neutral	Expansionary	Neutral	Neutral
Tasmania	Expansionary	Neutral	Neutral	Neutral	Neutral	Contractionary
Northern Territory	Expansionary	Expansionary	Expansionary	Expansionary	Neutral	Expansionary
ACT	Neutral	Expansionary	Neutral	Neutral	Contractionary	Neutral

Source: Urbis

Expansionary Neutral Contractionary

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THE PANDEMIC HAS REVEALED UNDERLYING STRUCTURAL AND CYCLICAL CHALLENGES ACROSS THE SOCIO-ECONOMIC LANDSCAPE

Supply Chain bottlenecks

→ **Transmission channel/s:**

- Cost Pressures
- Output constraints

Energy market imbalances

→ **Transmission channel/s:**

- Oil and gas price spikes
- Transition to renewables

China growth slowdown

→ **Transmission channel/s:**

- Commodity price fluctuations
- Currency devaluation

Public Health systems pressured

→ **Transmission channel/s:**

- Health cost inflation
- Increased spending on health systems

Climate change & sustainability

→ **Transmission channel/s:**

- Increasing adoption of Sustainable Development Goals (SDGs)
- Decarbonisation targets (Paris Agreement)

Geopolitical tensions

→ **Transmission channel/s:**

- Regional instability in Europe & Asia
- Cyber threats
- IT 'Cold War'

Localisation vs Globalisation

→ **Transmission channel/s:**

- Focused and targeted micro infrastructure projects
- Connectivity and inclusion a focus

WITH SUPPLY-SIDE REALIGNMENT AND DISRUPTION IS A PROMINENT INFLUENCE ON BUSINESS CYCLES

International Supply Chain

Opportunity

Rapid post-COVID re-opening of economies with increased trade

Risk

Inflation due to continuing skills and supply shortages, and surging freight costs

International skills competition

Opportunity

Drawing of international talent due to Australia as an attractive place of work and lifestyle

Risk

Loss of skilled workers if affordability remains uncontrolled

Labour Force behavioural change

Opportunity

Improved productivity and participation from greater work-life balance, lower barriers to employment

Risk

Insufficient workplace structures to ensure social inclusion, collaboration and employee support

Indebtedness

Opportunity

Asset value improvements offset indebtedness, allowing a staged repayment of debt

Risk

A credit-crunch sees defaults on debts and asset values fall with mass sales

The Capital-labour gap

Opportunity

Capital is directed to productivity improvements, wages rise

Risk

Capital continues to dominate economic activity, wages and productivity lag

MACRO RISKS FOR THE PROPERTY SECTOR WILL SHIFT IN THE WAKE OF POST-PANDEMIC CHANGES

Risk Factor	1 – 3 Years Horizon	5 – 7 Years Horizon	+ 10 Years Horizon
Global business cycle	+4	+3	+2
Domestic demand conditions	+3	+3	+4
Inflation pressures	+4	+2	+2
Interest rates	+5	+3	+1
Employment and income growth	+3	+2	+3
Population growth	+2	+3	+3
Sustainability and resilience	+4	+4	+5

+1 = Low risk to +5 = Extreme risk

Source: Urbis

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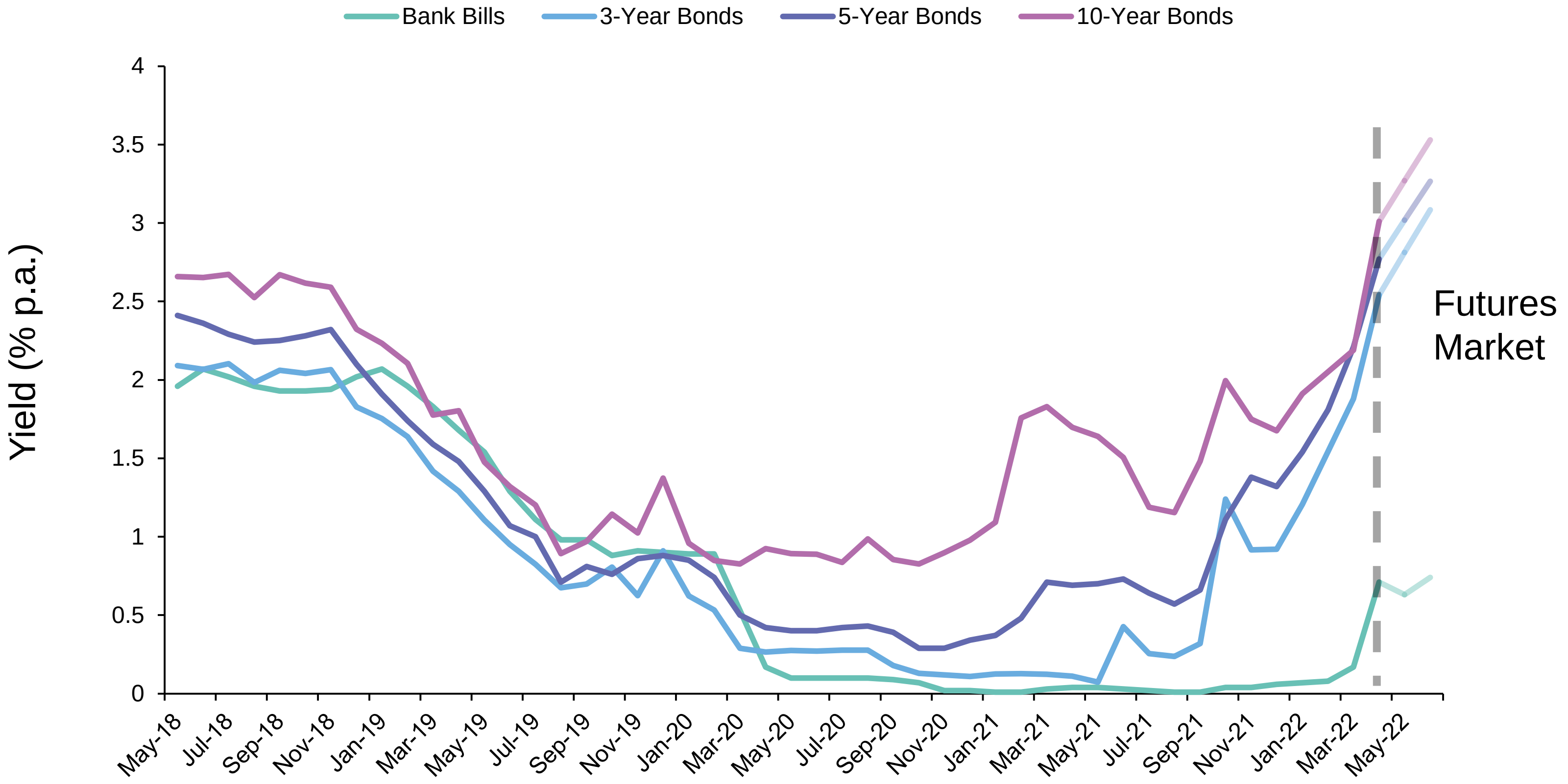
OFFICIAL INTEREST RATES ARE BEGINNING TO RISE AND MARKETS MUST RECALIBRATE THEIR CASH AND RISK-FREE RATES



Source: ASX, ABS and Urbis

With inflation and interest rates returning to long-term averages, the risk profile of assets will return to relying on the risk-free rate. This may see short term fluctuations in the opportunity cost of capital, however, conditions are likely to favour longer-term value assets that produce strong cash-flows.

The cash rate has risen for the first time in over a decade to 0.35%. The greatest risk is for mortgage holders, many of whom have never seen their loan repayments increase.

RECALIBRATION WILL INEVITABLY RESULT IN ADJUSTMENT TO THE RISK-REWARD EQUATION

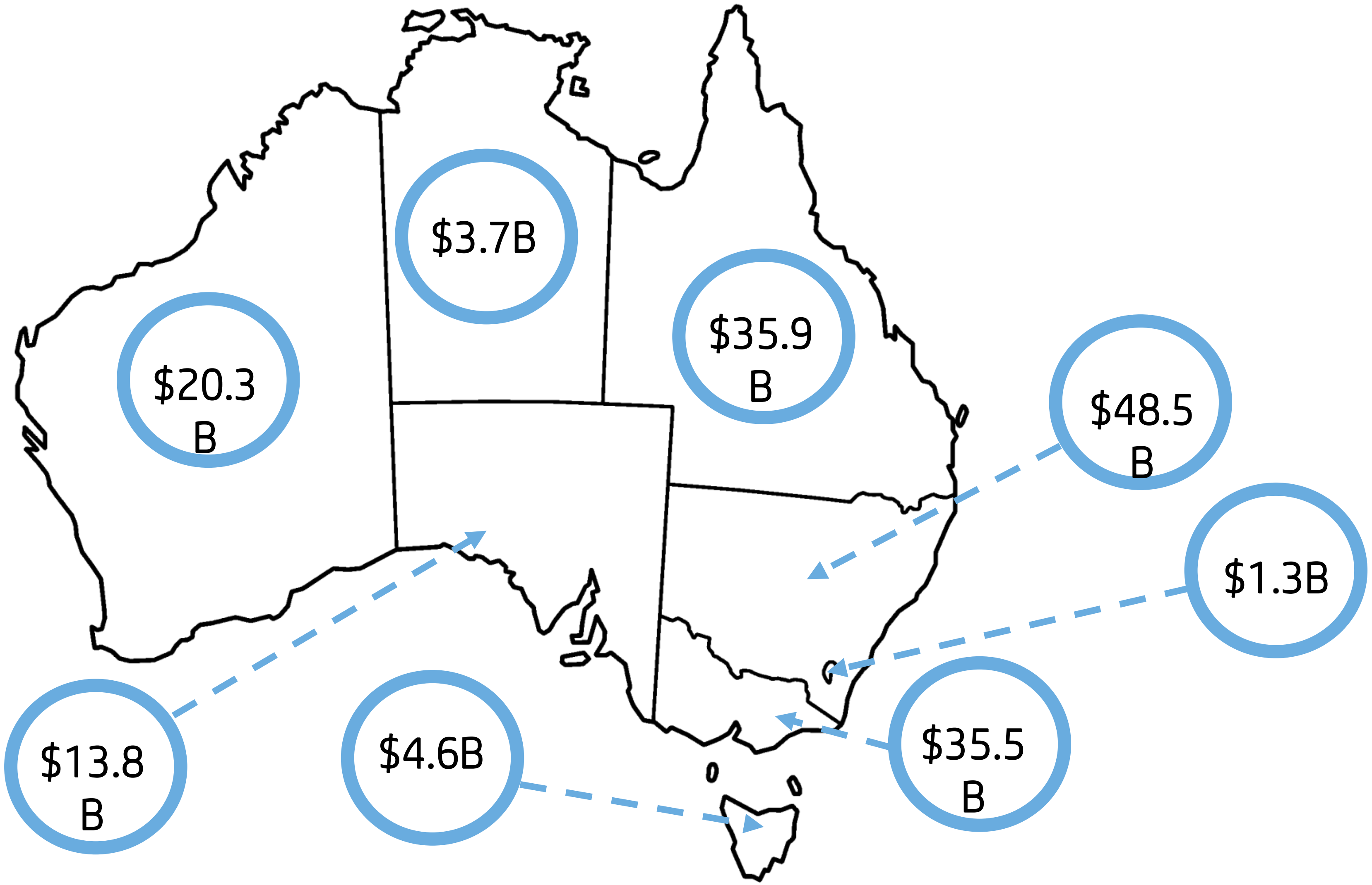
⇧ Business insolvency is at risk of rising due to lower revenue and higher costs.

⇧ Rising inflation and interest rates could make it difficult for borrowers to meet debt repayments.

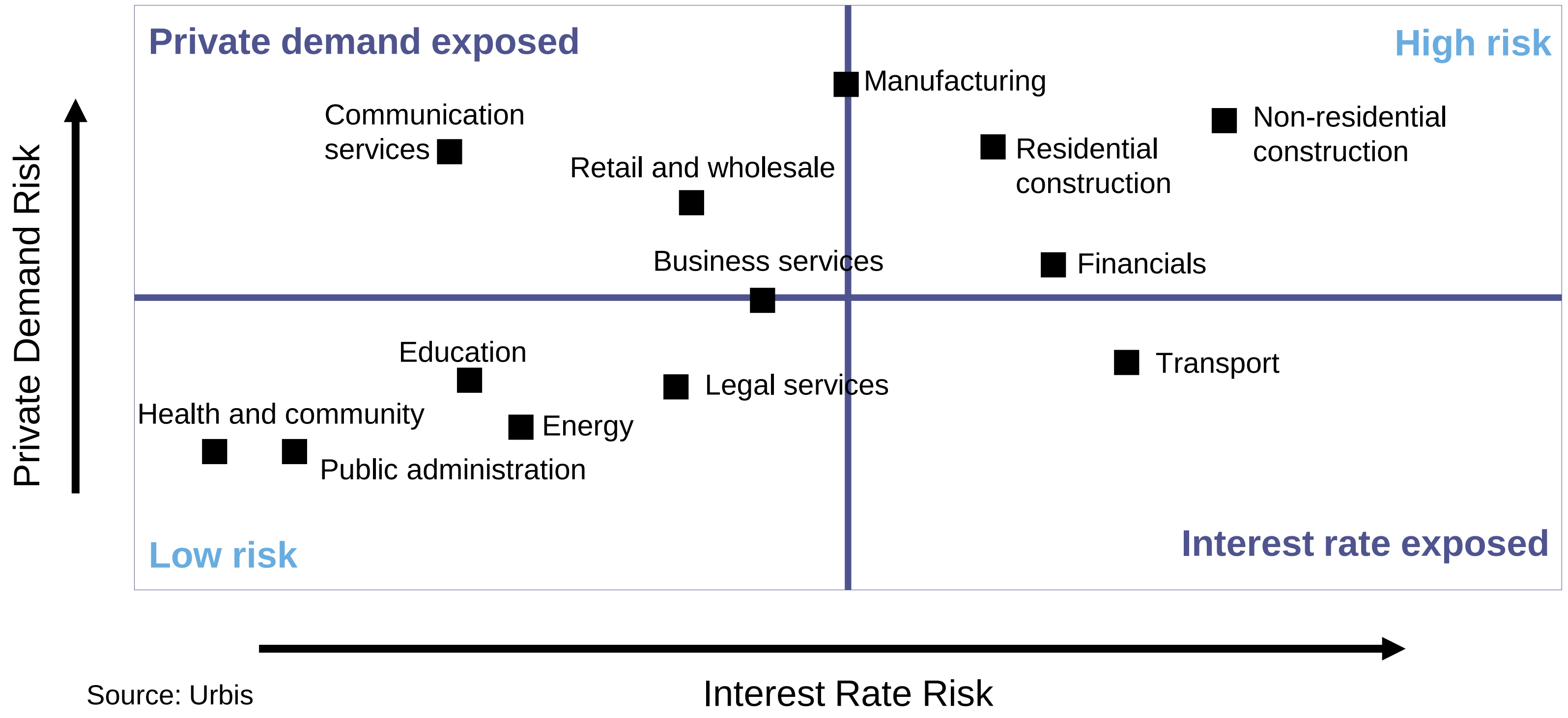
⇧ Interest rate increases are expected to impact commercial property valuations.

⇩ Underlying asset values will be negatively impacted by changing technological and logistical standards, as those that fail to adapt become obsolete.

AUSTRALIA'S $120 BILLION 10-YEAR INFRASTRUCTURE INVESTMENT PIPELINE IS A PILLAR OF THE ECONOMY'S COVID-19 RECOVERY



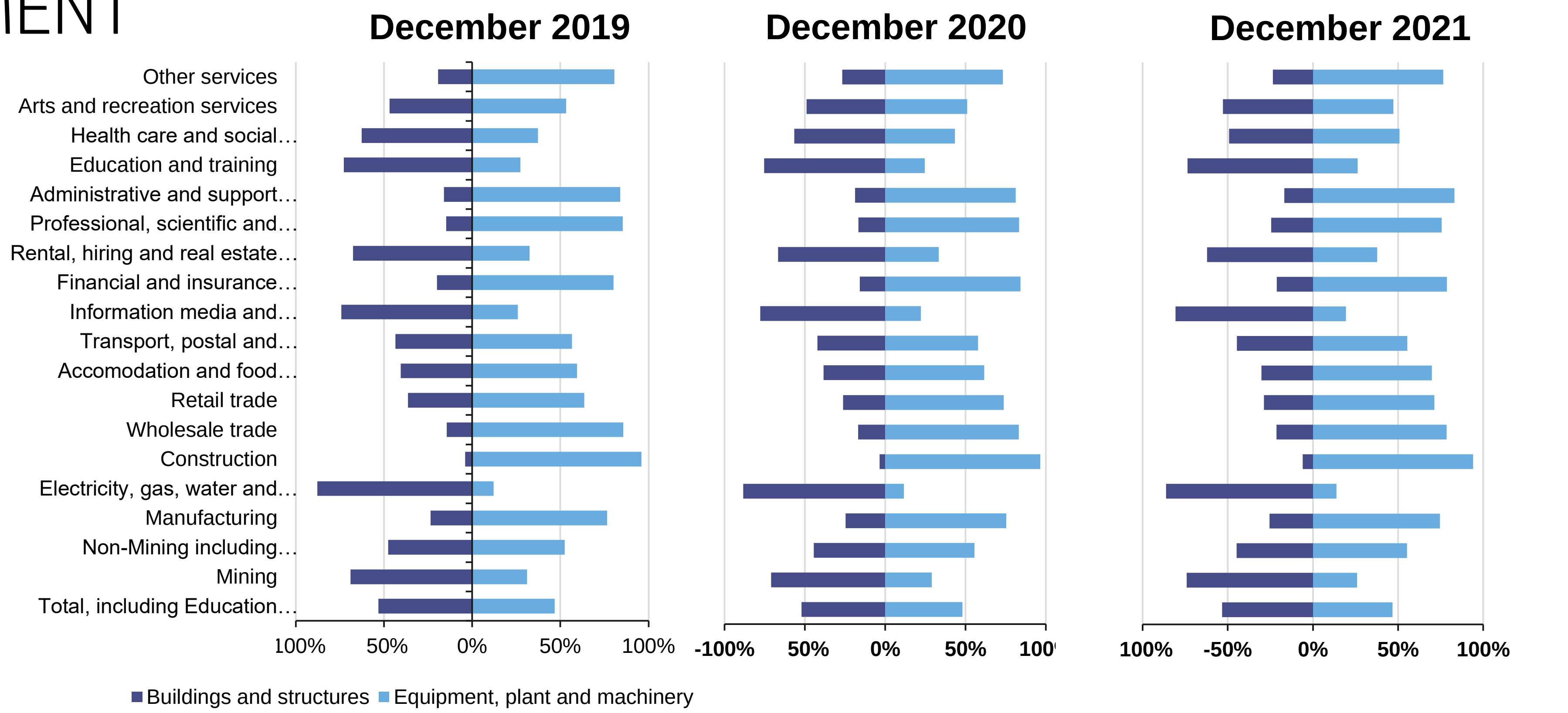
PRIVATE DEMAND AND INTEREST RATES REPRESENT CHALLENGES FOR THE KEY SECTORS OF THE ECONOMY



Source: Urbis

Industries more highly weighted in physical capital have a larger exposure to both private demand and interest rate risk overall.

BUSINESS CAPEX REMAINS BALANCED BETWEEN BUILDINGS AND EQUIPMENT



Source: ABS, Urbis

Automation in industrial and commercial sectors has seen strong ongoing investment in plant and equipment. Furthermore, data analytics and storage are increasingly important for businesses which is similarly maintaining high plant and equipment spending.

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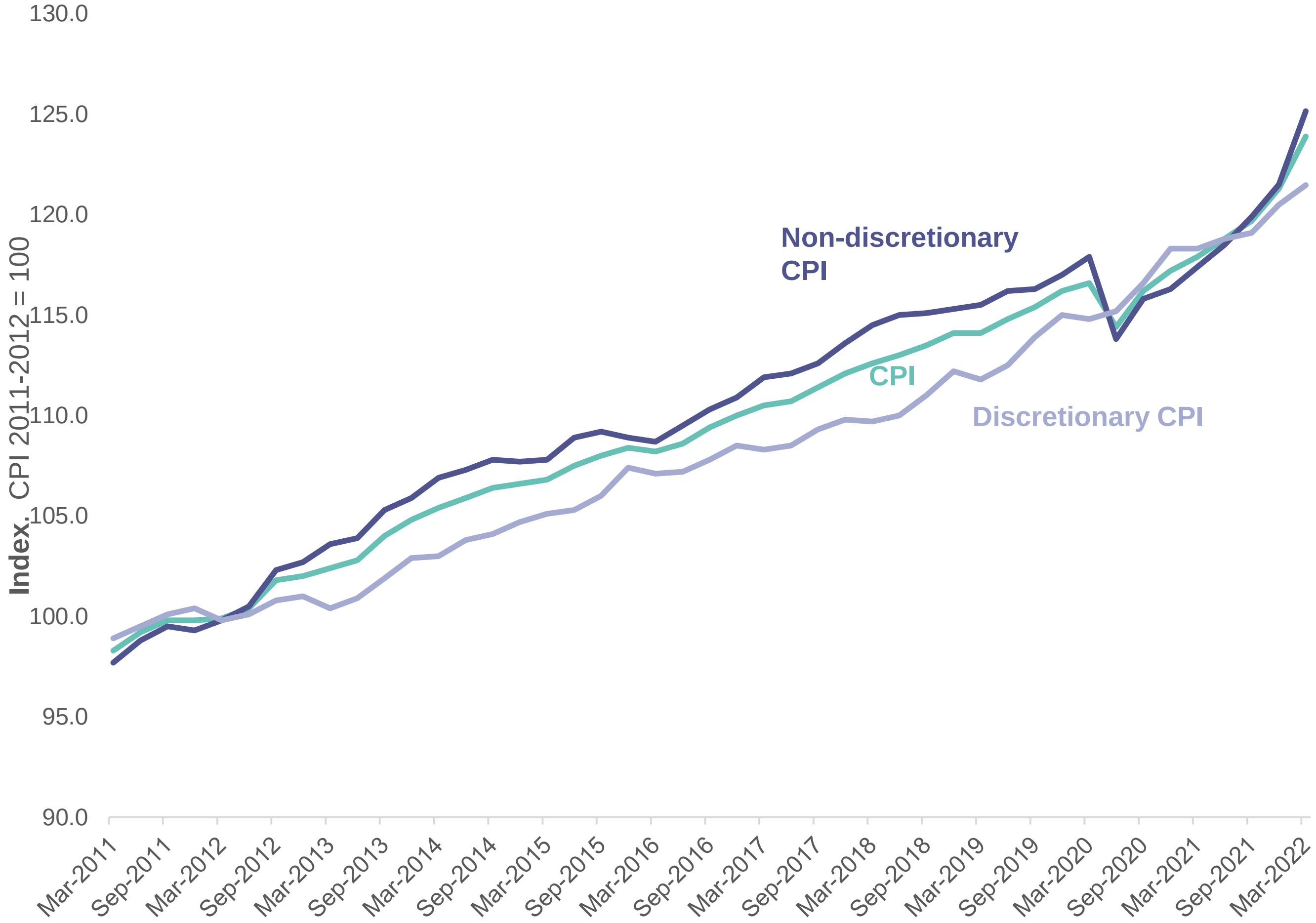
COST-PUSH INFLATION CONTINUES TO RISE REFLECTING ONGOING DISRUPTION TO GLOBAL SUPPLY CHAINS



Source: ABS

The continued growth of inflation will continue to cause strain on households, raising costs of living pressure and lowering the real growth of wages.

Producer costs are increasing at a higher rate than CPI, driving the need for efficient creation and delivery of goods and services.

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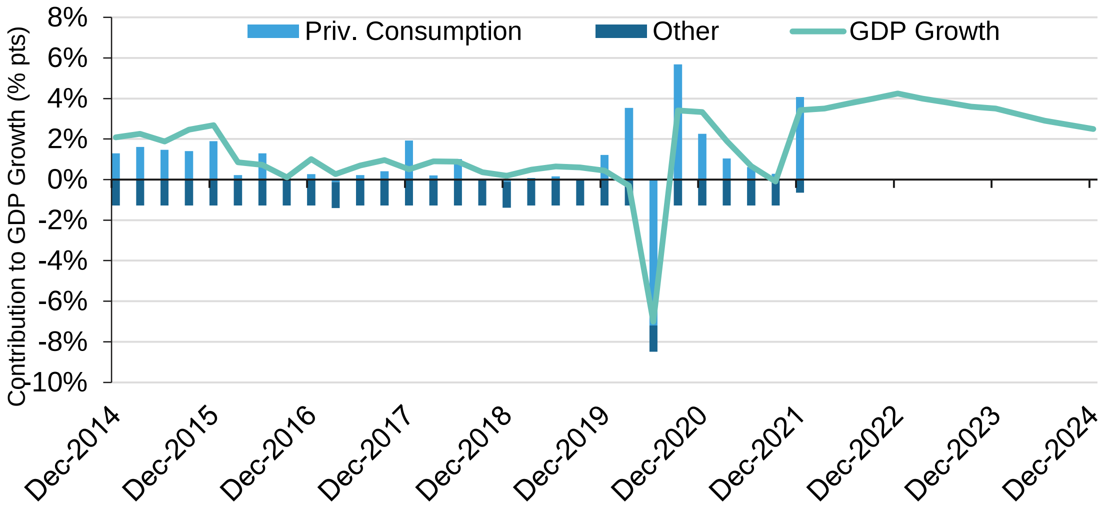
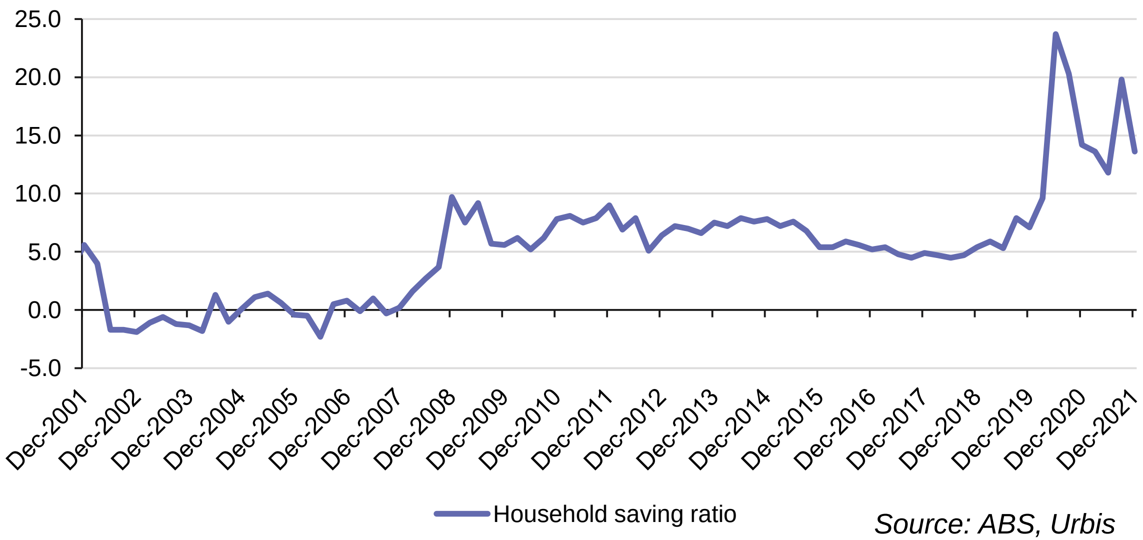
PENT UP STRENGTH OF PRIVATE CONSUMPTION WILL MODERATE AS THE 'WAR CHEST' OF SAVINGS IS SPENT



Source: ABS, Urbis



Source: ABS, Urbis

Private consumption will decrease as household savings diminish while concurrently facing growing cost of living pressures.

SUSTAINABILITY AND RESILIENCE ARE NOW THE HALLMARKS OF RESPONSIBLE INVESTMENT AND PRUDENT RISK MANAGEMENT

Social License to operate

- **Even though something is legal, is it ethical or socially acceptable?**
- **Resilience towards emerging social concerns such as post-COVID health practices, climate-related concerns**

Connection to country

- **Supporting the health and wellbeing of Country**
- **Respecting First Nations peoples and their cultural knowledge**
- **Sustained involvement of First Nations peoples**

Community benefits

- **Realising the positive externalities to the community that arise from best practices**
- **Considering the social frameworks of the communities where business is undertaken**

Working towards the United Nations SDG's

- **Transforming business models and systems for a sustainable future**
- **Implementing internal systems that support global environmental, economic and social objectives**

EU Taxonomy (in Australia's pipeline)

- **Encouraging sustainable financial investment**
- **Accelerating investment into low carbon and environmentally friendly business activity**
- **Already impacting current investment between Australia and the EU**

MOMENTUM IS BUILDING IN SUSTAINABLE FINANCING ACROSS ALL SECTORS

Sustainable Financing

- **Spurred by a combination of investor activism and regulatory and policy activity in the UK and Europe.**
- **Requirements are now flowing through to a wide range of sectors and deals, including real estate.**

Lenders

- **Increasingly offering facilities with ESG incentives – such as reduced margins – that are affecting the cost of capital.**
- **Ramping up due diligence on qualifying ESG claims.**

Future outlook

- **While the UK and Europe are currently leading the way, other regions are catching up.**
- **Sustainable financing is expected to be a fundamental driver of asset resilience in the future.**

Over the last 10 years the cost of capital between renewables and fossil fuel energy has diverged by nearly 60%

58% divergence in 10 years

Average loan spreads for coal power generation have increased by 38% globally

+38%

Meanwhile, average loan spreads solar PV have fallen by 20%

-20%

Source: Oxford University

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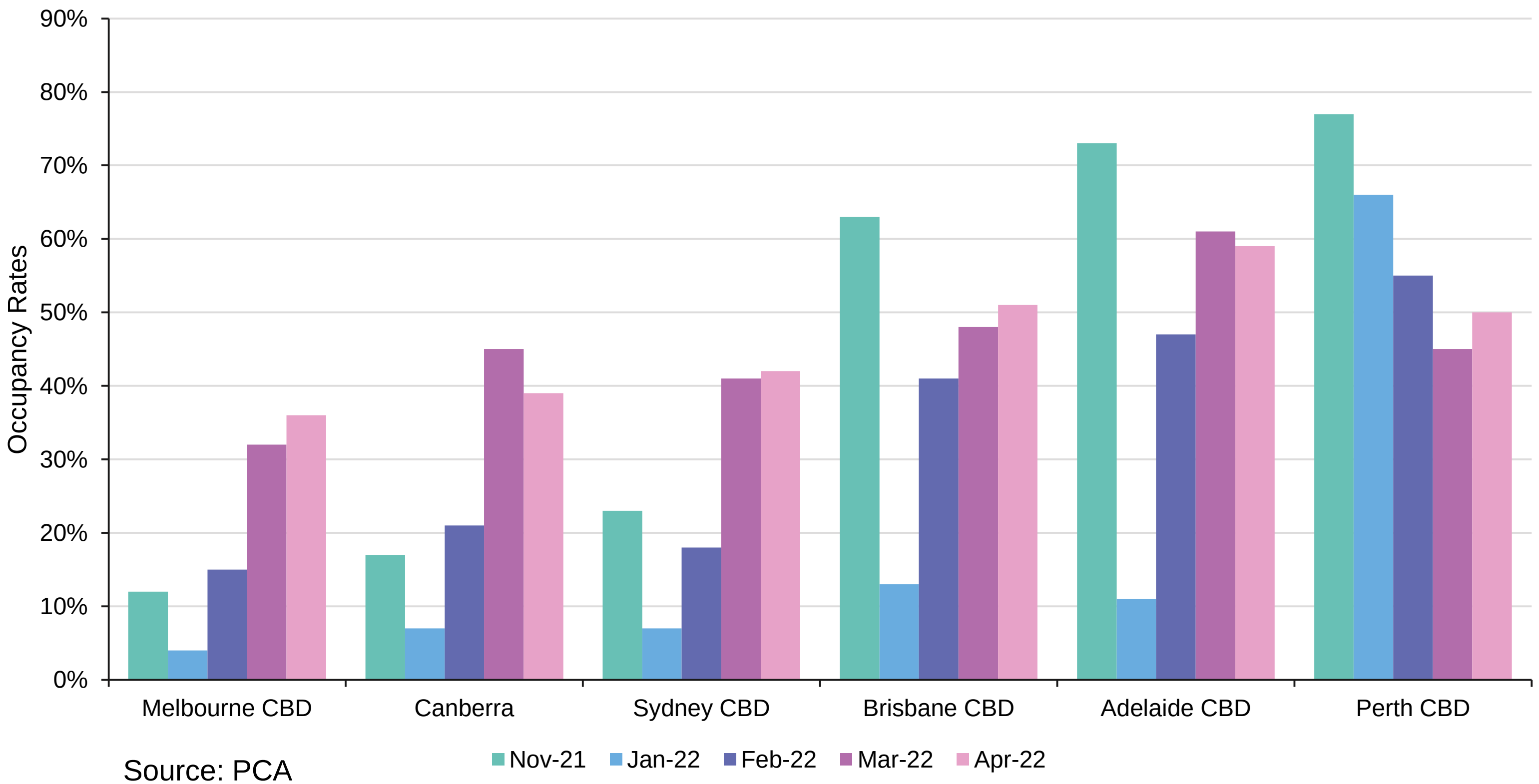
WORKPLACE OCCUPANCY IS BOUNCING BACK, BUT IN THE FACE OF NEW POST-PANDEMIC NORMS



Source: PCA

Increases in CBD occupancy rates suggest a return to at least hybridised workplace patterns. This is occurring following the cessation of lockdowns around Australia, and despite weather and transport disruptions on the east coast.

Despite strong returns to the workplace, employees are continuing to embrace the flexibility of hybridised work patterns to suit individual needs.

BALANCE OF RISKS FOR THE AUSTRALIAN ECONOMY IN 2022-23

BALANCE OF RISK PROBABILITY

Pent-up demand propelled growth — 50%

- Convergent but punctuated growth in the major economies
- Shifting business and consumer confidence
- Constrained asset markets with lower turnover
- Rising official interest rates
- Unstable commodity prices

Inflation-constrained activity — 35%

- Declining real growth rates
- Negative asset markets
- Subdued business and consumer confidence
- Rapidly rising interest rates
- Falling commodity prices

Global stagflation — 10%

- Negative real growth rates
- Weaker asset markets
- Depressed business and consumer confidence
- High interest rates and bond yields
- Accelerating commodity prices

Global financial crisis mark II — 5%

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