

The 2023 PropConnex Real Estate Case Competition

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2023 Campus Finals Case – Skyrack Tower, Sydney

Introduction

For the past 18 months, the strain felt by the commercial real estate market has been making headlines, particularly within major markets in the U.S. The combination of work-from-home and rapidly rising interest rates has put pressure on the entire commercial real estate industry, particularly impacting office properties. For a lot of investors, this is a time to re-evaluate the strategies of existing holdings and reconsider methods for deploying new funds. Many market participants are expecting commercial office valuations to decline.

In Australia, national office markets have observed a flight-to-quality over the last 2 years, with tenants prioritising building services, amenities and location against older/cheaper alternatives. This trend has been particularly noticeable within Premium Grade assets in Sydney CBD, where most of the vacancy has been concentrated in older / tired assets.

Obsolete Secondary Grade assets continue to be withdrawn from the market for redevelopment into Prime Grade offices or for alternative uses such as residential, student accommodation or hotels.

Silver Street Advantage - Investor Profile

Silver Street Advantage (SSA) is a leading investment firm focused on APAC with ~US\$60 billion in global AUM as of May 2023. Founded in 1987, SSA has invested US\$30bn across 6,300 properties in the APAC region, managing capital on behalf of nearly 200 institutional fund investors. SSA Real Assets is a vertically integrated investment manager, with a 35-year track record investing across Core, Core-Plus, Value-Add, and Opportunistic investments.

To date, SSA has raised several funds and SSA III is the most recent in the fund series with a mandate to generate total returns targeting 16% project-level (pre-tax) returns with allocation to Australia. SSA III looks to target Core-Plus / Value-Add assets in developed Gateway cities, with a particular focus on office, residential / student housing, hotels, and industrial sectors. SSA III typically will not leverage its investments above a 65% loan to cost.

Investment Overview

Through a personal relationship with a local real estate agent, SSA was presented with an off-market opportunity to acquire, Skyrack Tower (the “Property”), a Secondary Grade office building within Surry Hills on the fringe of the Sydney CBD. The agent has pitched the Skyrack Tower as a blank canvas Value-Add opportunity for redevelopment / adaptive re-use as it has been owned by a private family for the past 30 years who have invested limited capital. The Property has a short WALE (weighted average lease expiry) of 0.29 years.

You have been engaged by the SSA fund manager to review this opportunity and present your recommendation to the SSA investment committee. Your recommendation should include: 1) an acquisition price; and 2) a business plan for Skyrack Tower that will best realize its potential value.

Your presentation should not exceed 20 minutes and must include the following:

Property Analysis

- Current estimate of the asset value.
- Schedule of the sources and uses of any cash requirements.
- Analysis and discussion of relevant property and investment metrics for the business plan.
- Market research for the Property submarket.
- Risk management analysis, taking into account both property and market factors.

Strategic Plan and Objectives

Drawing on the above analysis, you are to devise and recommend a set of strategic objectives for the utilization of the asset.

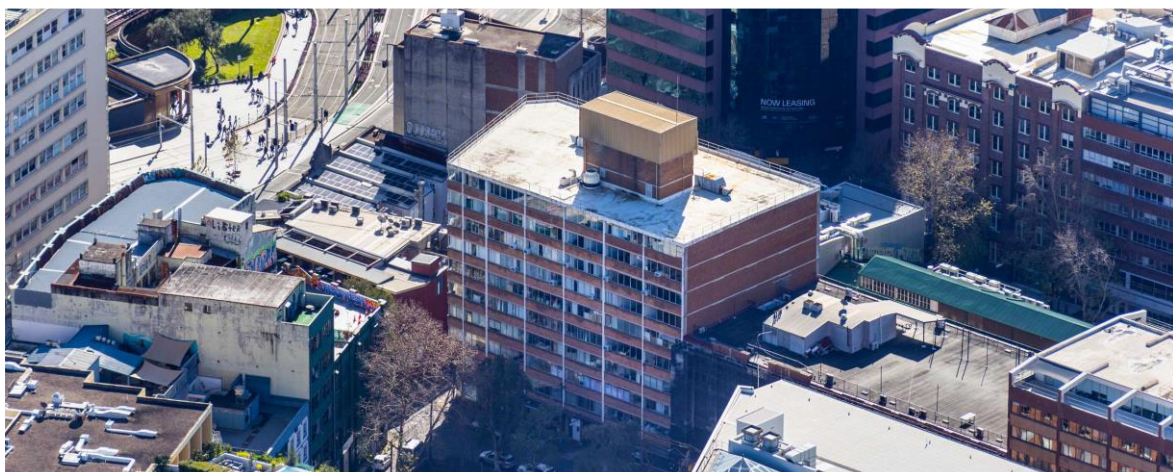
Your recommendation should be supported by detailed property and market forecasts and analysis backing the decision as well as an eventual exit strategy and investment time horizon. You may wish to address whether you intend to sell the asset (including to whom you might sell the asset) or pursue a strategy to hold the asset longer term to build additional equity value in the asset. Be sure to also discuss the debt financing required for any business plan that is recommended and provide an evaluation of the potential risks involved with your business plan and a means to mitigate them.

Rules and Guidelines

When in doubt about a particular issue, feel free to make an assumption, document it, and move on. Please use relevant market research and information to support your presentation as you see fit. Information provided within this case study should be supplemented with your own research. Please note this case is fictional and that the properties and companies in this case study may not exist. You may assume the current date is 1 July 2023 and your analysis should be completed on a pre-tax basis.

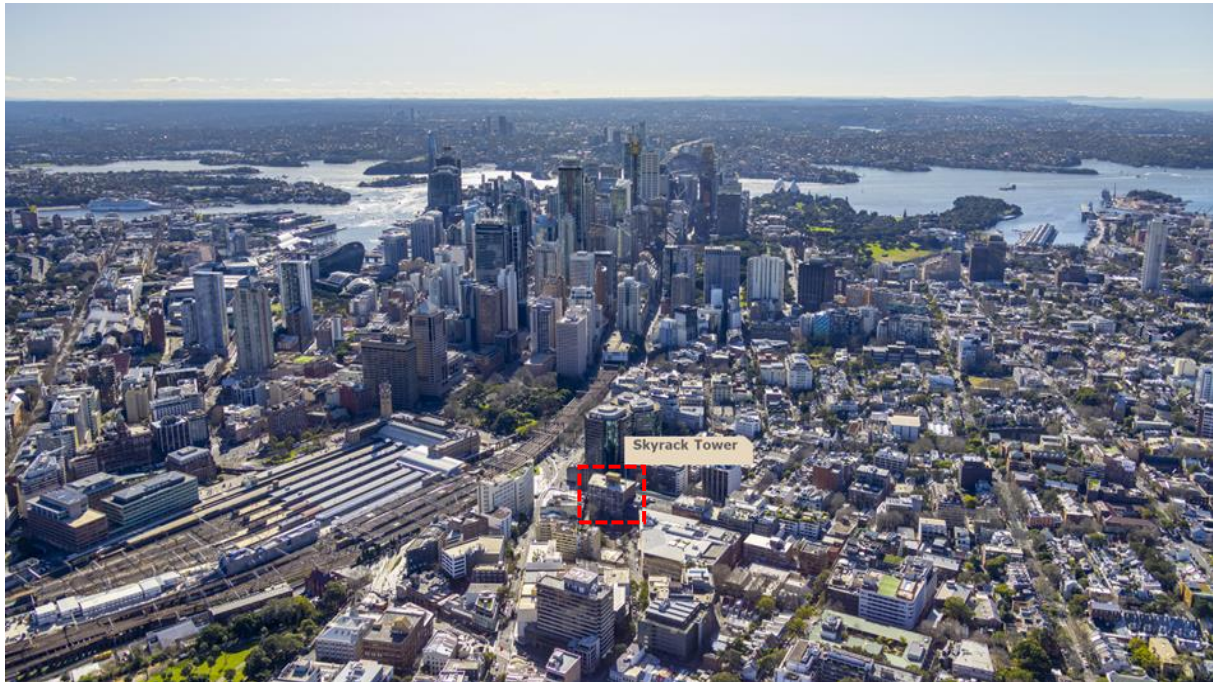
Asset Summary

Skyrack Tower is a C-Grade office tower located in the CBD fringe office market, Surry Hills. Built in the 1960s, the property is a 9-story, 8,400 sqm building that includes 7,700 sqm of office accommodation, 700 sqm of street-level retail and 52 basement parking bays. To the best of the team's knowledge, the building has not undergone renovations. The building is currently ~80% occupied and the NOI for 2023 is approximately \$2.3mm with all tenant leases expiring within the next 12 months. The property is currently charging well below the market's rent and is one of six investable assets with a NLA over 8,400 sqm and one of fifteen assets with floor plates over 875 sqm in Surry Hills.



Location Overview

Skyrack Tower is one of Sydney's most connected addresses. Central Station, Sydney's busiest station, connecting every train line except for one, is located just 250 metres West of the property. Further connectivity is provided by the various bus stations surrounding Central and the recent completion of the Sydney Light Rail. Central's status as Sydney's most connected station will be further enhanced from 2025, with direct access to the Sydney Metro to be completed.



Benefit from Tech Central

Tech Central is an NSW state government backed initiative to bring together three world class universities, a world leading hospital and over 100 research institutes and centres of excellence into one precinct.

Made up of six neighbourhoods; Surry Hills, Haymarket, Ultimo, Camperdown, South Everleigh, Darlingtown North Everleigh, it is envisaged to be Australia's innovation engine. Across the six designated suburbs, the NSW government has committed to providing affordable spaces for researchers, innovators, start-ups and entrepreneurs to incubate, test and scale their ideas. Tech Central will provide up to 250,000 square metres of space for technology companies, including 50,000 square metres at affordable rates for startups and scaleups, in a connected location brimming with heritage, culture and activity. Home to News Corp, Canva, SafteyCulture, new start-ups, arts and media firms, consultancies and professional services, Surry Hills is a vibrant creative cluster and cultural hub. The growing range of creative, digital, advertising and design agencies are the lifeblood of Surry Hills with businesses seeking out the converted older buildings the area has to offer.

Skyrack Tower provides potential investors with a unique opportunity to access the forecasted growth in Surry Hills given the significant investment in infrastructure, transportation and local amenities such as restaurants, creative workspace, and tech start-ups.

Zoning Information

The City of Sydney recently reviewed the zoning for the Central Precinct given the government's significant investment in upgrading Central Station and development of Tech Central. One key aspect that they amended was increasing the FSR (Floor-to-Space Ratio) from 9:1 to 12:1 and increasing the height limit to 45 meters to incentivise developers to consider new projects. Please see below the summary of planning restrictions for Skeyrack Tower.

Planning Overview:

Council City of Sydney

Zoning B4 - Mixed Use

Site Area 1,039 sqm

FSR 12:1

Current FSR 9:1

Height Limit 45m

ZONE B4 MIXED USE:

1 . Objectives of zone

- To provide a mixture of compatible land uses.
- To integrate suitable business, office, residential, retail and other development in accessible locations to maximise public transport patronage and encourage walking and cycling.
- To ensure uses support the viability of centres.

2. Permitted without consent

Home occupations.

3. Permitted with consent

Boarding houses; Centre-based child care facilities; Commercial premises; Community facilities; educational establishments; Entertainment facilities; Function centres; Hotel or motel accommodation; Information and education facilities; Medical centres; Oyster aquaculture; Passenger transport facilities; Recreation facilities (indoor); Registered clubs; Respite day care centres; Restricted premises; Roads; Seniors housing; Shop top housing; Tank-based aquaculture; Any other development not specified in item 2 or 4.

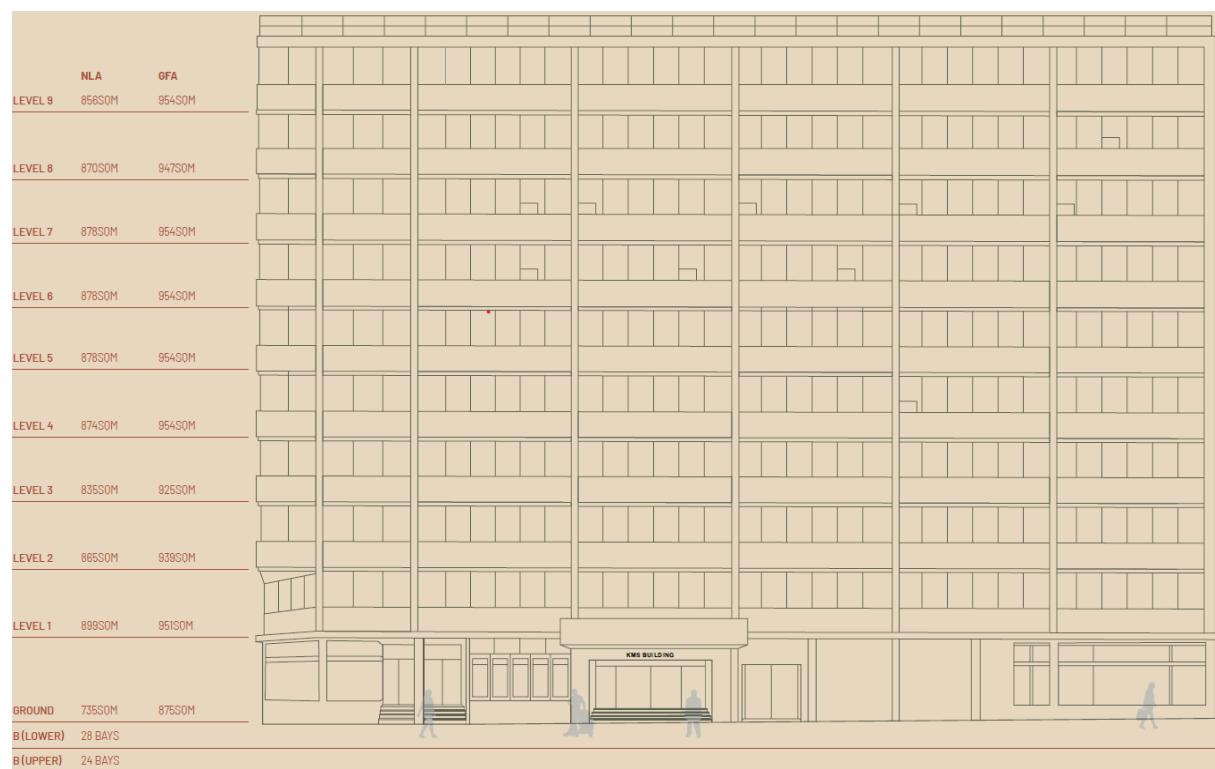
4. Prohibited

Extractive industries; Heavy industrial storage establishments; Heavy industries; Pond-based aquaculture.

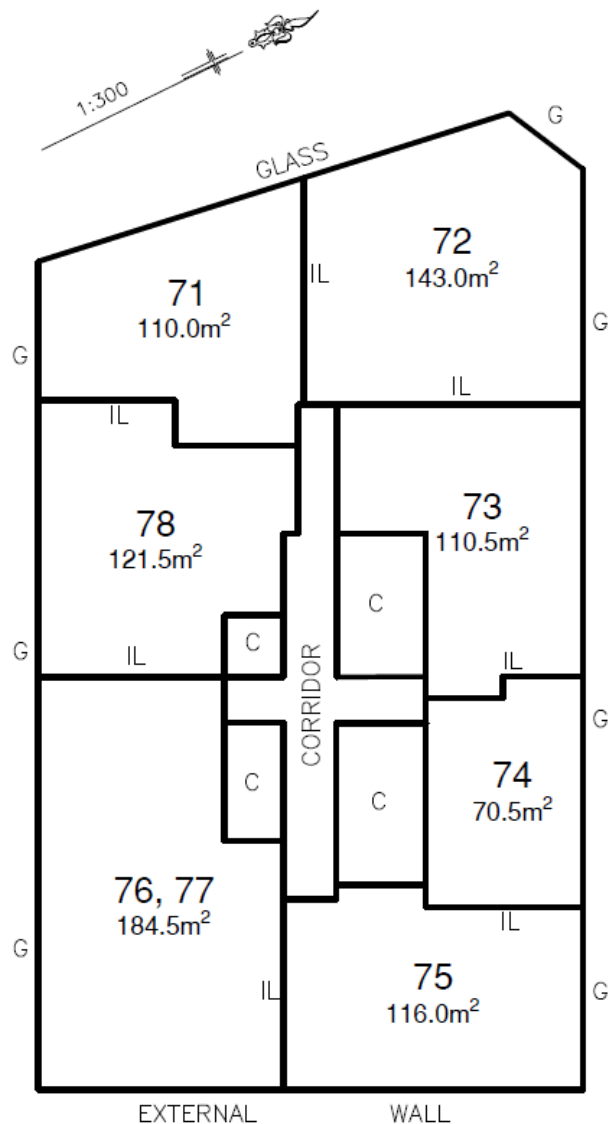
Recent New Office Leases – Surry Hills Precinct

Property	Level	Tenant	Leased Sqm	Lease Start	Lease End	Rent Gross/sqm	Annual Reviews	Gross Incentives
64 Kippax	3	Sony	750	Sep-19	Sep-25	\$978	3.50%	35%
64 Kippax	7	Audinate	750	Jul-19	Jul-24	\$1,029	3.50%	35%
64 Kippax	4-6	BioCeuticals	2,251	Jun-19	Jun-24	\$997	3.50%	35%
66 Goulburn St	11	TMF Corporate Services	545	Apr-22	Apr-25	\$1,031	3.50%	35%
66 Goulburn St	8	Go to Court Lawyers	946	Nov-21	Nov-26	\$1,065	3.50%	35%
280 Elizabeth St	7	Commonwealth of Australia	1,306	Jul-22	Jul-29	\$996	3.50%	35%
280 Elizabeth St	8	Department of Social Services	2,607	Apr-22	Apr-29	\$966	3.50%	35%
300 Elizabeth St	9	NDIA	1,300	Apr-23	May-25	\$973	3.50%	35%
300 Elizabeth St	16	ROKT	1,290	Aug-22	Aug-27	\$1,076	3.50%	35%
477 Pitt St	26	BRP Australia	965	Jan-23	Jan-30	\$1,078	3.50%	35%
477 Pitt St	27	Morlaw Holdings	2,895	Jul-22	Jul-32	\$1,041	3.50%	35%

Current Skyrack Tower Stacking Chart



Current Skyrack Floorplan



Construction Cost Assumptions

Build Efficiencies

GFA to Commercial Net Leasable Area	110%
GFA to Net Saleable Area	115%

Build Costs

Office GFA Build Rate (\$psm)	5,500
Residential GFA Build Rate (\$psm)	7,500
Student Accommodation / Hotel (\$ per bed)	300,000

Other Fees (% of Build Cost)

Development Management / Project Management	7.50%
Professional Fees	3.00%
Statutory Fees	2.50%
Project Contingency	5.00%