

Private Markets

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Investing for Innovation: Life Sciences in Australia

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BlackRock Real Estate Research and Strategy - November 2024

Key Takeaways

- The life sciences sector plays a major role in **facilitating critical global outcomes**, namely through advancing biotech, pharmaceuticals and agri-food.
- Australia's life sciences real estate market is **entering its growth phase**, in our view, following established markets in the US and Europe.
- Key tailwinds include growing and ageing populations, increased healthcare expenditure, growing talent pools and rising public, corporate and venture capital investment.
- Limited real estate supply and deep pools of demand create a clear **early mover advantage** in Australia's life sciences real estate market.
- Moreover, there is an opportunity to provide **specialist management services** to support the sector and its occupiers beyond the provision of real estate, by facilitating access to a collaborative and vibrant community.

Capturing the APAC Lag Through Life Sciences

“The APAC lag” refers to winning global strategies that remain early in their development in APAC. Informed investors can build strategic conviction around such sectors and benefit from early-mover advantage in markets where these trends are yet to fully play out.

A key example of this is the life sciences sector, a well-established asset class in the UK, US, and Western Europe. Global focus on the sector is demonstrated by investor intention surveys which show that one third of investors are pursuing alternative real estate, with a focus on life sciences¹.

As the sector has matured, life sciences rents have settled at a ~40% premium to A-Grade office, underpinned by a supply demand imbalance and higher economic rents considering the higher construction costs for the specialized assets². In Europe and the US, investors who had conviction on the sector whilst it was in its relative nascency are now reaping the benefits.

Australia is a global leader in medical technologies and pharmaceuticals, ranking 11th globally for inward life sciences foreign direct investment with average annual growth of 75% between 2010-22³. Yet life sciences real estate is only now emerging in institutional portfolios, with a limited supply of commercial stock available to rent or purchase.

Figure 1: Global life sciences industry comparison of employment and companies

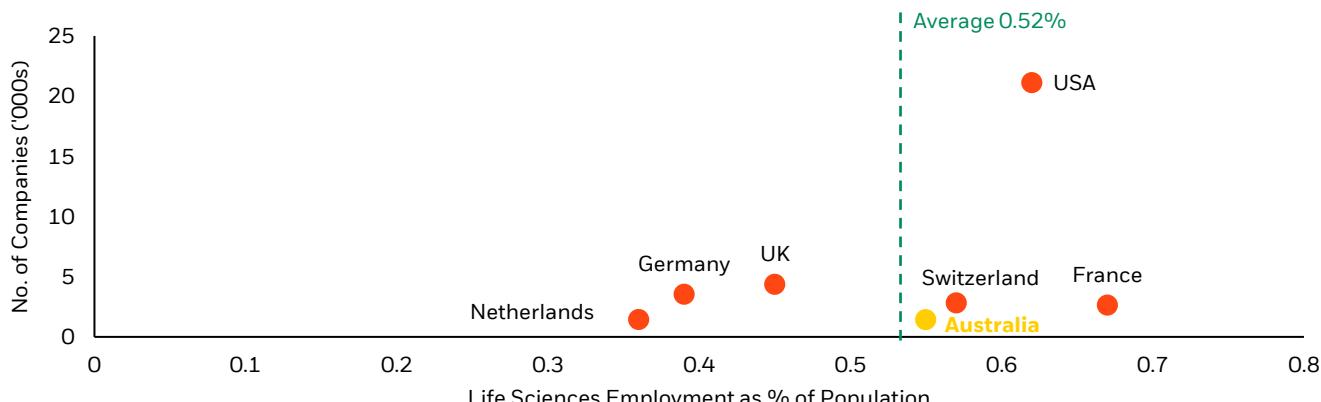


Chart Source: No. Companies: AusBiotech 2022 (Australia), Biotech Gate 2024 (USA, UK, Germany, France, Switzerland, Netherlands), No. Employees: 2023 U.S. Life Sciences Outlook (USA), UK Gov Office for Life Sciences Bioscience and health technology sector statistics 2021 to 2022 (UK), Panda International 2024 (Germany, France), interpharmaph Annual Report 2023 (Switzerland), Investment Monitor 2023 (Netherlands). Note: no. employees may not be reflective of current employment with variations for the date for each market's employment.

¹CBRE 2025 U.S. Investor Intentions Survey: Investment Activity Poised for Growth, ²BlackRock, Wentworth Capital, November 2024, ³BlackRock, Wentworth Capital, November 2024.

Demand for life sciences space continues to outstrip supply. The majority of existing life science real estate is owned & operated by universities or government. Competing established and privately-held stock of scale is minimal as development costs are prohibitive at prevailing rents (which are less than half of rents in the US & UK). Given the scarcity of existing life sciences assets, groups have had to pursue developments to gain exposure to the sector in Australia.

In light of growing demand for commercial life sciences real estate, we believe the sector will follow similar growth to that observed elsewhere. This will enable investors to benefit from **early mover advantage**.

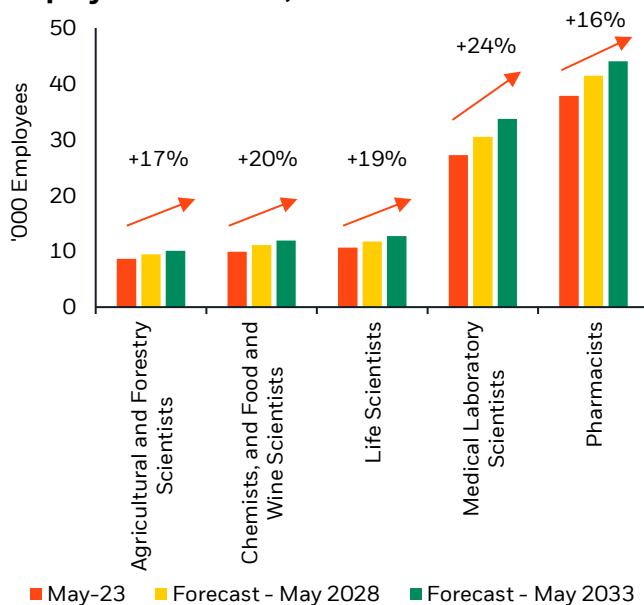
Our conviction leads us to believe the Australian market is mispricing life sciences assets from a both capital markets and rental perspective given the relative shortage of comparable trades in the domestic market when compared to other assets classes. Slowly, this trend is beginning to shift with several recent transactions creating a greater level of price transparency. This creates a **pricing arbitrage** opportunity for investors to capitalise on an early mover advantage in a relatively low-risk manner by purchasing existing high-quality assets, and to take advantage of the APAC lag as the market matures into an attractive core product.

Market Positioned for Growth

Despite its infancy compared to other global markets, Australia competes very strongly in terms of its relative number of employees and absolute number of life sciences businesses, (Figure 1). Australia represents an important location for multi-national organisations seeking geographical diversification in their revenue streams, diverse clinical trial locations and for those seeking to grow market share in the Asia Pacific region.

Whilst the life sciences real estate sector in Australia lags the US and UK, the underlying market is robust. There are 2,905 organizations in the Australian life sciences sector as of 2024, up 43% since 2019 and 60% since 2017.⁴

Figure 2: Australian Life Sciences Forecast Employment Growth, 2023-30

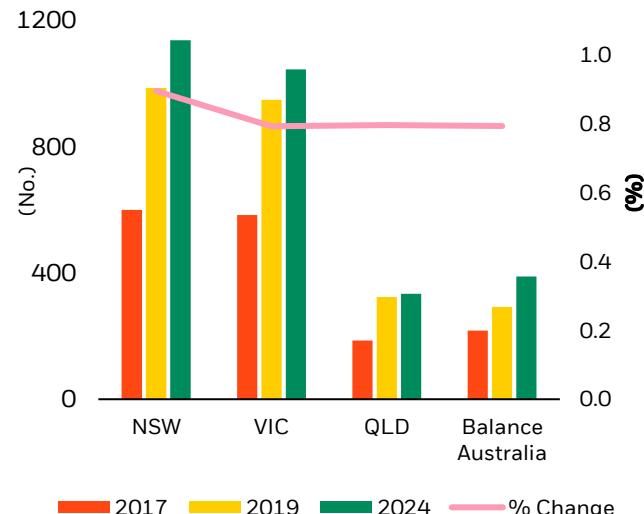


Source: Aus Biotech Sector Snapshot, 2022. Forecasts may not come to pass.

As the sector continues to grow, commercial real estate supporting its occupiers will need to do the same. With all life sciences employment categories forecast to experience strong growth, demand for increased accommodation will follow (Figure 2). Australian life sciences space requirements are expected to increase 19% from 2023 to 2033, with supply likely to lag demand considerably if existing delivery trends persist. This creates an opportunity for investors to become rental “market makers”⁵.

Growing healthcare spend underpinned by Australia's demographic story will naturally fuel demand for laboratory space.

Figure 3: Number of Australian Life Sciences Organizations



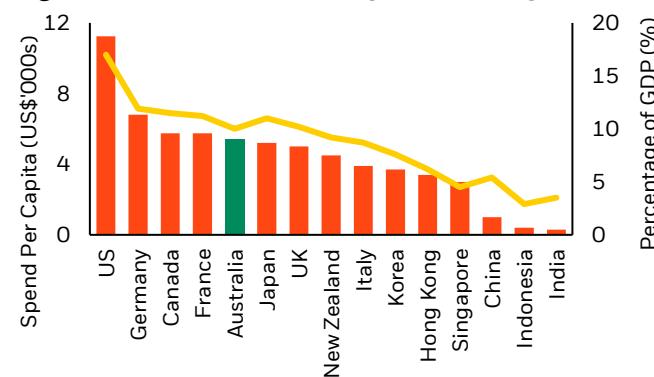
Source: BlackRock, Aus Biotech 2024.

⁴Aus Biotech 2024, ⁵JLL for BlackRock November 2024

The BlackRock Investment Institute has identified demographics as one of the key mega forces which our Investment Teams seek to align strategies to. Given Australia's growing and ageing population, real estate is a sector expected to offer winning opportunities.

Australia's population is projected to average annual growth of up to 1.8% for the next 5 years and is ageing rapidly with the share of population aged over 65 set to double by 2060-61. A larger and older population leads to increased healthcare spend. At only 10% of GDP in 2019, this remains below other OECD countries and offers potential for further growth (Figure 4).

Figure 4: Global Health Expenditure Spend

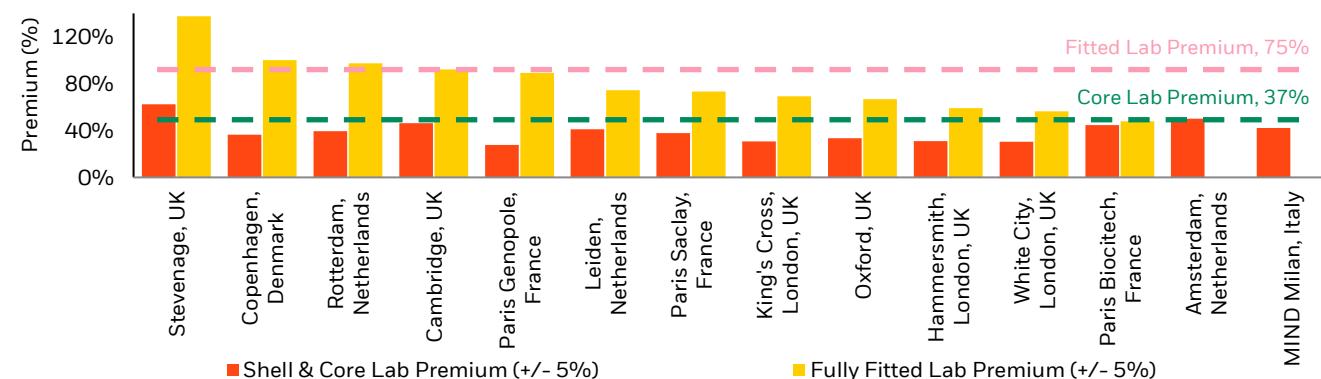


Source: BlackRock, CBRE Research, US National Health Expenditure Data, OECD Stat, Health Expenditure Australia 2018-19

These demand tailwinds in combination with the economic rents required to deliver fully fitted labs have lifted global life sciences rents for fitted space to circa 75% above premium office rents which is a trend beginning to emerge in Australia (Figure 5).

Australia is considered a highly supportive location for life sciences companies, with over A\$21bn in government funding to support research, manufacturing and commercialisation.⁶ The sector is also well-supported by rising domestic and offshore venture capital investment, corporate investment and IPO activity.

Figure 5: UK & European Office vs. Lab Rents



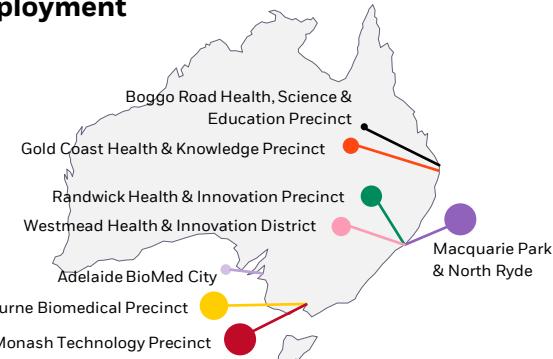
⁶ JLL research 2024, ⁷QS World University Ratings, 2024, ⁸Nature Index (Nov 2023- Oct 2024)

Finally, Australia benefits from high-quality research, workforce and industry growth. Australia is home to 9 of the world's top 100 universities, with 3 featuring in the top 20⁷, supporting strong sector employment and company growth. Moreover, Australia ranks 11th globally and 5th in APAC on Nature's index of high-quality scientific research output, reiterating its place in global life sciences circles⁸.

The Hunt for Scarcity

Life sciences occupiers prefer to 'cluster,' whereby they co-locate alongside similar groups around key universities, hospitals and transport infrastructure. The key Australian clusters are largely located in the country's South East, with many having been supported by Government investment in their development after recognising the value of key innovation precincts (Figure 6).

Figure 6 Life Sciences Precincts in Australia by Employment



Source: Employment in each of the precincts, JLL, ABS.

However, the demand from occupiers to locate within these clusters has created significant challenges in finding suitable space, particularly as their metro locations often mean there is low amounts of available developable land and very low tenant turnover. Hence, the purchase of existing assets in these clusters given the low to nil vacancy provides comfort of strong occupancy and rental growth as competitive tension emerges.

One of the key drivers of undersupply is the cost to develop labs. Depending on the physical containment level ("PC"), costs are estimated to be approximately 92% to 580% more expensive than typical office buildings. This drives the divide between economic rents for office and life sciences, as well as continuing to limit life sciences supply now and into the future.

As highlighted in Figure 7 the cost of delivering life sciences labs vs. standard office underpins the rental premium evidenced in global markets. As the complexity of the labs increases from PC1 to PC3, the associated increase in machinery, utilities, and infrastructure is significant.

The specialized knowledge required for development in combination with the difficulty in converting existing office assets to life sciences means we expect stock to remain highly constrained in the medium term.

This also creates an opportunity for specialist life sciences real estate operators to provide additional amenity and services to their tenants and portfolios. By deeply understanding life sciences occupier needs, a specialist manager could foster the acceleration and incubation of emerging technologies and companies within a collaborative ecosystem of like-minded tenants, further enhancing the utility of existing life sciences clusters across the country.

As the scarcity of life sciences stock persists due to challenges in delivering new stock, demand will continue to outstrip supply and drive life sciences rental growth – further evidencing the rental premium of life sciences to office in Australia.

The Investment Conviction

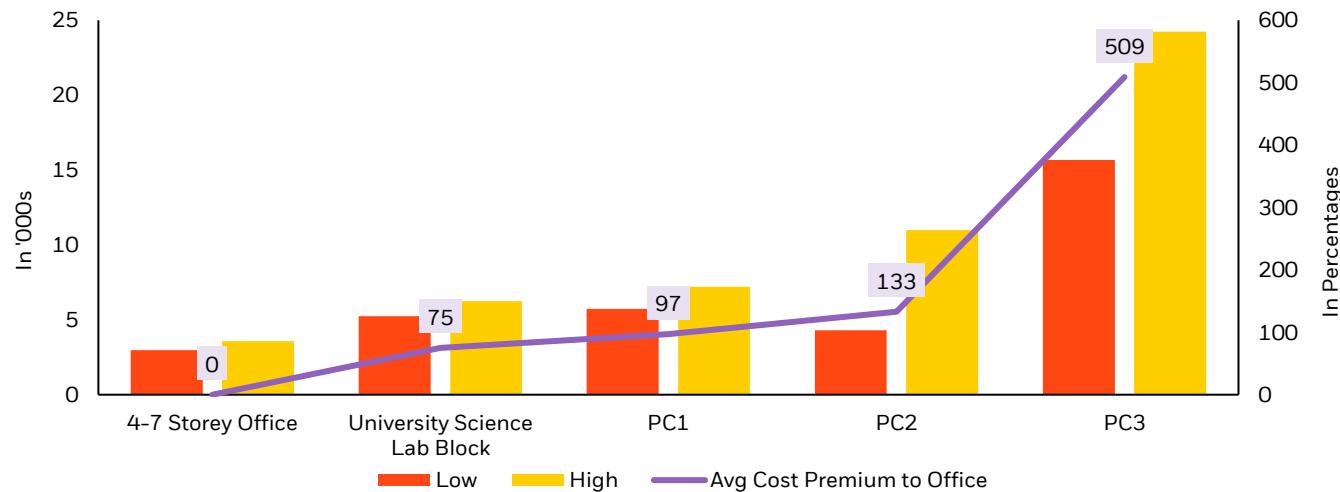
With life sciences operators providing critical infrastructure support to societies globally, we believe core investors will see the life sciences sector as a key component of their diversified property portfolios and look to the transparent and liquid market of Australia for these investments.

The most significant opportunity exists for those investors who can unlock the purchase of existing assets before the pricing arbitrage window from both a capital market and rental perspective is well noted, acted upon by a widespread pool of capital and therefore closed. The largest window of opportunity therefore exists now in Australia.

The existing capability of Australian universities, industry and innovation clusters in addition to the strong and growing private and public support for the sector, provides the talent, capital and support for life sciences industry growth. The final piece of the puzzle is readily available lab space for the industry to innovate, create and product their products.

- **PC1** – Low-risk dealings with minimal containment needed
- **PC2** – Designed for low to moderate-risk dealings with GMOs, with guidelines varying by facility type
- **PC3** – Used for moderate to high-risk dealings involving dangerous or genetically modified organisms
- **PC4** – Provides biocontainment for high-risk agents that may cause serious diseases, with facilities maintained under negative pressure

Figure 7: Construction Costs – Laboratory vs. Office



Source: JLL with BlackRock, November 2024.

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