The untapped potential of growth markets

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At Dexus we have brought together alternative investments, healthcare and infrastructure under a single growth markets banner. Why? Because of their shared potential to deliver scale, growth and importantly, drive investment performance.

From the well-established sector capabilities and asset scale in our $2 billion healthcare and $11 billion infrastructure portfolios to the breadth of existing and new opportunity in our $1 billion alternatives business – the common factor across all three is growth.

Through this lens of untapped potential, let's look at each sector in turn, supported by case studies that demonstrate the unique capabilities needed to capture the value on offer.

Our experience shows that picking trends like decarbonisation, connectivity, urbanisation and an ageing demographic early is key to achieving outsized returns.

Bridging healthcare and infrastructure, our investment in aged care provider Opal Healthcare is an example of this approach. Nineteen years ago, AMP Capital purchased it as a real estate investment. With investors and partners prepared to back us, we subsequently merged the real estate and operational units.

It was a transformational move confirmed by the ensuing returns. Over 19 years, the internal rate of return (IRR) was about 14%. Over the last five years, the IRR was over 20%.

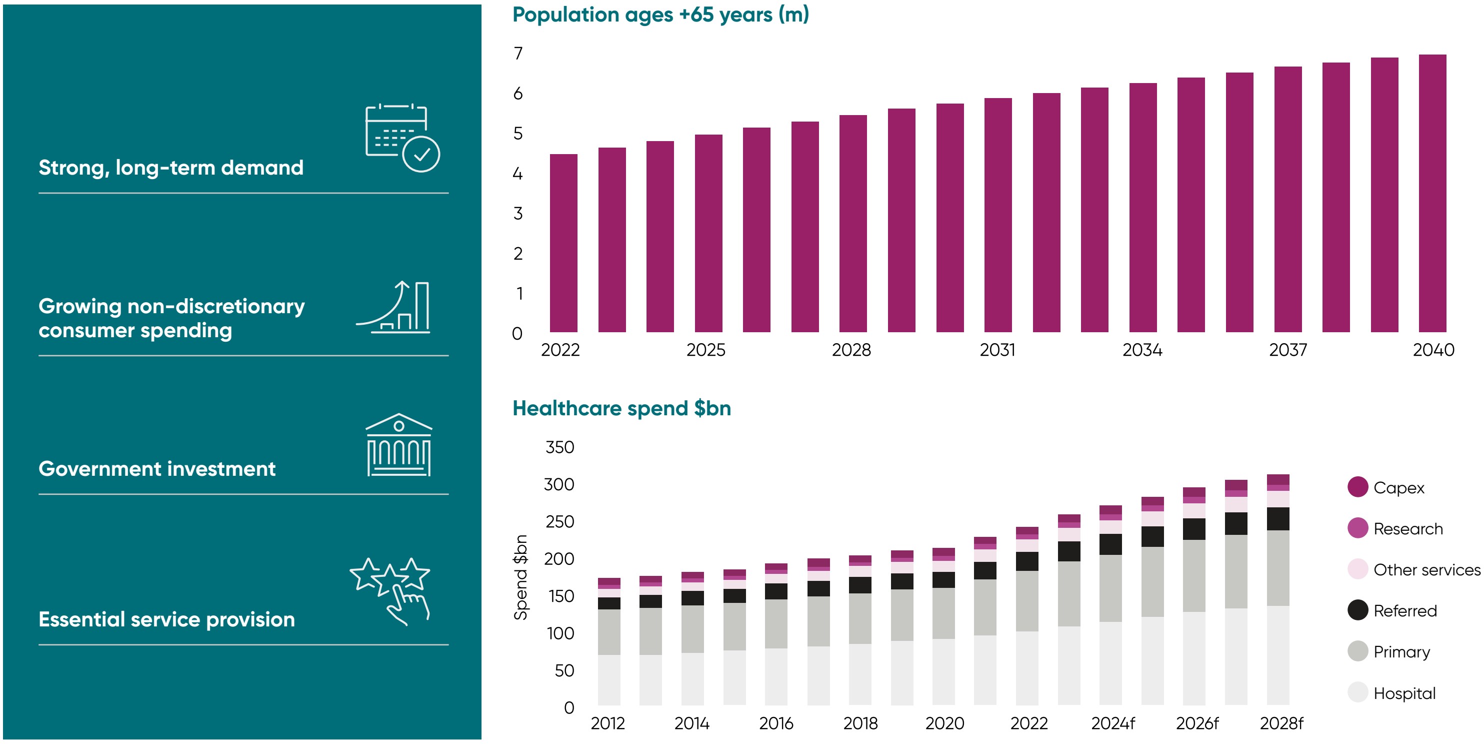
There are two broad explanations for this performance. The first is capability. By merging the real estate and operational functions, installing a new CEO and then building greater depth in the senior management team, Opal Healthcare has become the largest for-profit aged healthcare provider in the country. Strengthening management allowed the company to then invest heavily in systems and processes to drive the performance of the business.

Over the last five years, bed numbers have grown by 12% a year on a compound basis. With 65% of revenue coming from the government, Opal excels in building strong stakeholder relationships and industry leading risk management and clinical practices.

The second factor concerns macroeconomic trends. As Chart 1 shows, Australia has an ageing population leading to large increases in healthcare spending.

North Shore Health Hub, Sydney

Chart 1 **Macroeconomic Trends**



Sources: L Healthcare Real Estate, CBRE Research, May 2024. R. AIHW Australia's hospitals at a glance, APH Budget 2023, CBRE Research

Put simply, Australia's healthcare sector and ageing population needs more beds. With the deepest development pipeline in the industry, Opal is set to deliver them.

In this sector we're focused on large-scale acquisitions underpinned by increasing preferences for out-of-hospital and shorter stay cares such as day hospitals, specialist hospitals and mixed-use clinical spaces, which will experience greater underlying growth. We prioritise partnerships with major operators to redevelop current facilities or build new ones, and we expand assets within our portfolio where there is strong underlying demand.

One such example is North Shore Health Hub (NSHH), owned by the Dexus Healthcare Property Fund (DHPF). Located in the North Shore Medical precinct, we bolstered the structure so that it had capacity to take additional floor space, allowing us to capitalise on the unmet leasing demand – now oversubscribed – and realise the potential of the site, market and sector. With DA-approved plans to add ~1,500sqm of space, the potential expansion ties into the existing structure.

To a conventional infrastructure asset with equally attractive potential. Melbourne Airport occupies 2,750 hectares of land, 400 of which has been allocated to a business park. Thus far, only half has been developed. Based on comparable Dexus analysis, the developed value of the undeveloped business park land is projected to be over $3 billion.

Unlocking the revenue potential in non-aeronautical assets at airport sites is a strategy we've previously deployed at Jandakot Airport in Perth, where Dexus is developing a large and profitable industrial estate. In Melbourne, the strategy is to accelerate the business park development, bring forward the cashflow and further diversify revenue.

By growing the airport's earnings base through business park expansion, the revenue mix is broadened, and risk is lowered, leading to a lower discount rate. Accelerating the development of the business park should also drive greater airport value.

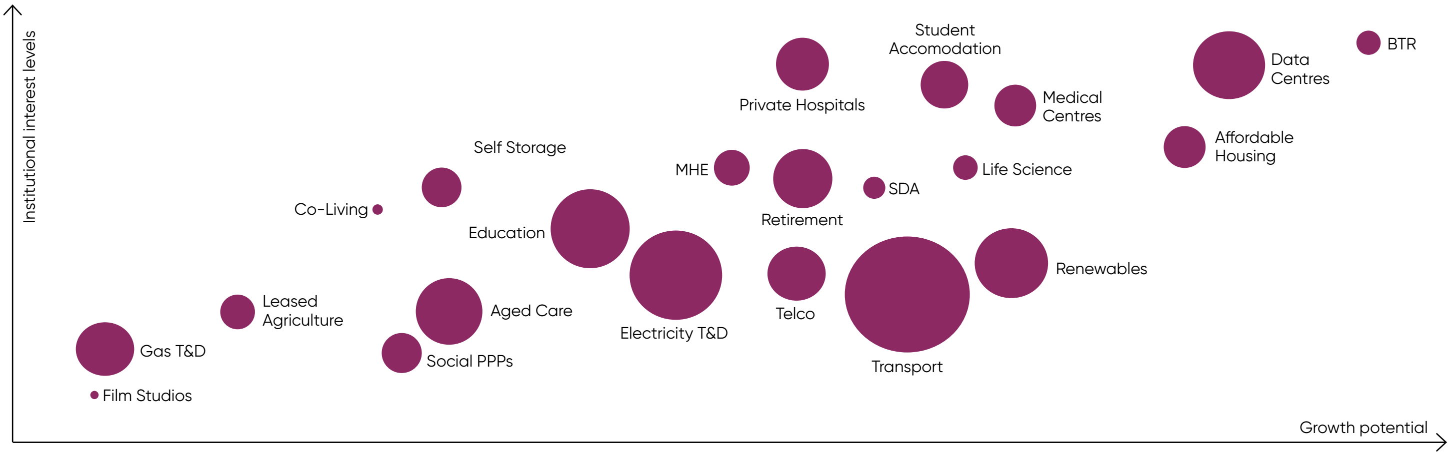
To the final leg of the growth markets stool. Alternative investments is an emerging sector characterised by its breadth. From alternative asset classes to different capital structures, return profiles, or investment profiles stretching from shorter term opportunistic plays to established, sustainable growth over the longer term.

In Australia, the alternative investment sector is less mature than in the US or UK but, as Chart 2 shows, the growth potential is huge and we are targeting sectors and asset classes where there is high growth potential, scale and adjacency to Dexus platform capability to drive performance.

With opportunities aplenty, we'll focus on adaptive reuse as an example. Imagine a 1970s office building close to two universities with good bones and a functional core. Whilst no longer suitable for its original purpose, viewed through the lens of untapped potential, could it be transformed to capitalise on market demand and tailwinds elsewhere?

Chart 2 **Alternative Investment Landscape**

Size of bubble = relative sector size



Sources: JLL Research, Cushman & Wakefield, Dexus, 2024

In this real-life example, the answer is 'yes'. Dexus's origination capability secured the financial sponsor and during due diligence, our experienced office development team scoped, designed, priced and established the delivery methodology to turn it into student accommodation.

We also contracted with a counterparty to mitigate the risks that might crop up in delivery. Our infrastructure colleagues, meanwhile, shared some key research and data that was valuable in underwriting rent, occupancy and operating costs on completion.

Early in October, Dexus and Marquette Properties made public their plans to repurpose a B Grade office building at 41 George Street, in Brisbane's CBD. The building is being acquired through Dexus's opportunistic Dexus Real Estate Partnership (DREP) fund series, with 5% of the economic interest held by Marquette Properties. Dexus and Marquette will be joint development managers.

On completion, the modern, purpose-built student accommodation (PBSA) facility will provide 1,200 beds and is expected to be valued at circa $500 million and generate a forecast levered IRR of ~20%[1].

The new development will feature three floors of resident amenities including gym, yoga, gaming and cinema rooms. At 27 storeys, the tower will be the closest purpose-built student housing to Queensland's second largest university campus, Queensland University of Technology, and two blocks from the Griffith University CBD campus, set to open in 2027. Many more adaptive reuse opportunities will be under consideration in the years ahead.

These examples across infrastructure, healthcare and alternatives, display the Dexus capability to identify and extract value out of any asset to drive investment outperformance from the untapped potential of growth markets, and, from hospitals to airports and student housing, the opportunity to meet community needs and create positive social impact.

[1] Represents an estimate as at September 2024 and is therefore subject to change over time. Investment level return – i.e. gross of fund costs/expenses and fees.

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