# South Korea Real Estate Market Annual Report

**CRE capital values are expected to bottom out in 2025, with positive yield spreads anticipated from 2026.**

IN A NUTSHELL

- The short-lived martial law and impeachment of the incumbent president of South Korea in early December shocked the global market but highlighted the resilience of the country's democracy, with limited impact on the economy so far.
- The Bank of Korea lowered the base interest rate from 3.5% to 3.0% in late 2024 and is expected to reduce it further to 2.5% or lower by the end of 2025, amid concerns over a potential economic slowdown in the coming years.
- The negative spread between cap rates and lending rates has sharply declined throughout 2024 and is expected to settle from 2026. Valuation of office and logistics sectors has declined 8-20% in the last three years and could bottom out in 2025.
- In the Seoul office market, future supplies are limited and centered around fringe areas, keeping the office vacancy rate tight at least until 2028, with healthy rental growth expected to continue during this period.
- Despite short-term market disruptions, the Greater Seoul logistics market is expected to see a supply cliff from late 2025 due to rising construction and financing costs, leaving room for healthy rental growth for existing assets in the mid-term.

# 1 / Macro Economy and Capital Market

In early December, South Korea experienced a series of political events that captured global attention. Within 11 days, the country saw a brief 6-hour martial law and the impeachment of the president, who was midway through his five-year term. This sequence of events shocked global markets but also highlighted the resilience of South Korea's democracy, showcasing effective checks and balances between Congress and the administrative office. The most notable moment was Congress's unanimous vote to invalidate the martial law proclamation, which the president accepted without any attempt at a power grab. Although political uncertainty is likely to continue, it is expected to be manageable through established legislative and judicial processes.

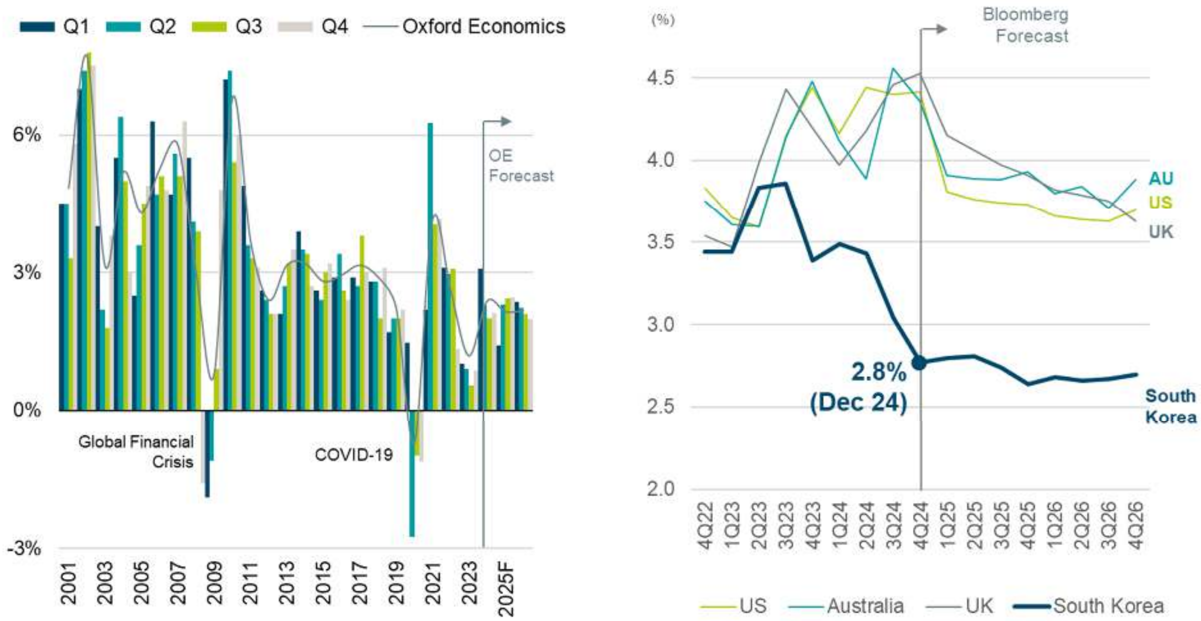
Despite short-term disruptions in the FOREX and stock futures markets, the Korean economy and capital market have remained relatively stable with only modest deprecation of KRW and KOSPI stock prices so far. However, it is important to monitor how the political vacuum might impact the country's economy, which heavily relies on export activities.

Regardless of the potential impacts of the political events, South Korean economic growth is expected to slow from 2.2% in 2024 to below 2% in 2025, amid increasing uncertainties in the global trade market following the U.S. election in November 2024. This casts a shadow particularly over exports of key national products such as semiconductors, automobiles, and secondary batteries to the U.S. The Bank of Korea lowered the base interest rate twice from 3.5% to 3.0% between October and November 2024 and is expected to reduce it further to 2.5% or lower by the end of 2025, amid concerns over long-term and structural pressures on the country's economic growth in the coming years.

**Exhibit 1: South Korea GDP Growth Outlook and Interest Rates Forecast**

South Korea GDP Growth Outlook by Country

10 Years-Long Sovereign Bond Yield Forecasts




Note: APAC Stock = MSCI AC APAC Index, US-REIT = FTSE EPRA/NAREIT United States, AUS-REIT = S&P/ASX 200 REIT, SIG-REIT = FTSE ST REIT Index, HK-REIT = Hang-Seng REIT Index, JPN-REIT = TSE REIT Index, KOR-REIT = Synthetic Index based on the weighted average of stock price change of all the listed REITs in South Korea
Note: Past performance is not a reliable indicator of future performance. Forecasts are not a reliable indicator of future returns. Forecasts are based on assumptions, estimates, views and hypothetical models or analyses, which might prove inaccurate or incorrect.
Sources: Korea REITs Information System, Korean Association of REITs, DWS. As of December 2024.

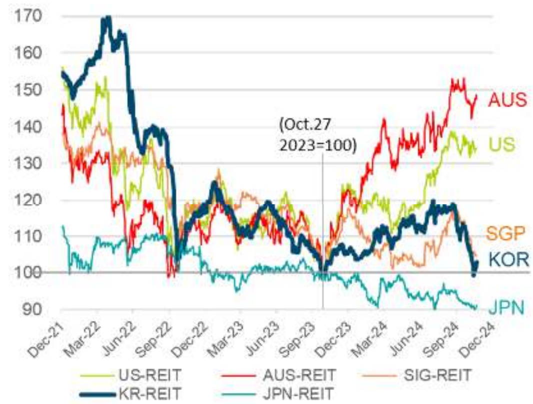
The valuation of the listed REIT market in advanced countries can be used as a leading indicator of the direct real estate market's valuation by about three to six months. This is based on the principle that the valuations of direct real estate and listed REITs converge to the same price in the long term. The REIT market in Korea still lacks the market size, liquidity, and institutional maturity to be used as a leading indicator. However, its rapid growth and increasing share in the transaction market are expected to incrementally enhance its utility in assessing overall real estate market developments.

Looking at the trends in REIT prices worldwide over the past 12 months to December 2024, REIT prices in the U.S. and Australia have shown a rapid recovery of 30-50%, following significant drops in their real estate valuations during the rapid interest rate hike cycle. In contrast, REIT prices in Korea and Singapore, where price adjustments were relatively smaller during the same period, have shown slower recovery. In Korea, this slower recovery is partly due to the unwelcome public offerings of some REITs, which made yield-dilutive acquisitions that lowered dividend yields.

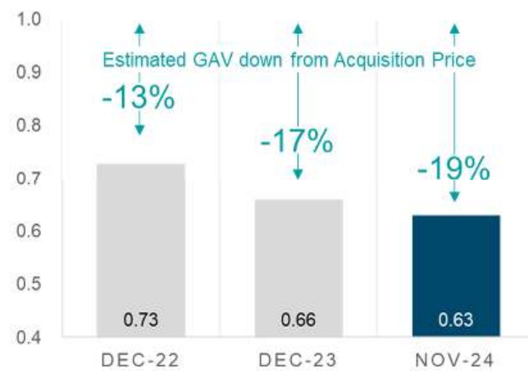
Nevertheless, the current Price-to-NAV (P/NAV) of listed REITs in South Korea is around 0.6x, implying an asset price adjustment of about 19% compared to the acquisition price if we take into account the average leverage of 50% at REITs. This can serve as another reference for investors to determine the timing of market re-entry in the direct real estate transaction market.

Exhibit 2: Listed REIT Trends in South Korea

APAC REIT Price Trends




P/NAV* of 18 Listed REITs in South Korea (Compared to Acqusition Price)




* The NAV of listed REITs in South Korea is calculated based on the acquisition price. This is because there is no regulatory requirement for regular updates of appraisal valuations for the assets owned and managed by listed REITs in the country.
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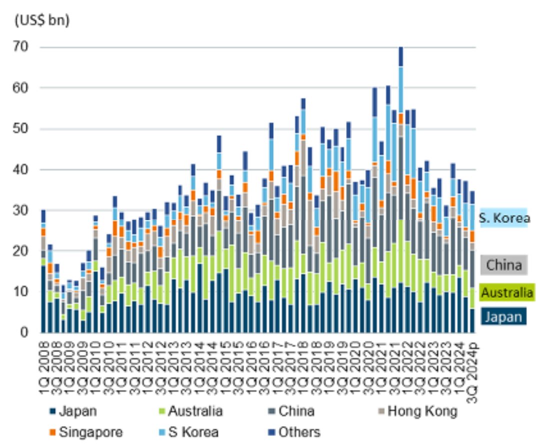
Sources: Korea REITs Information System, Korean Association of REITs, DWS. As of December 2024.

Across the Asia-Pacific region, the quarterly real estate transaction volumes in the third quarter of 2024 have decreased to about half of the previous peak of three years ago. This trend was similar across all the markets including China, Japan, Australia, and Korea with their quarterly transaction volume decreased by 40-60% in the same period. Especially In South Korea, the transaction volume from January to September 2024 was approximately 9 trillion KRW, which is a modest increase compared to KRW 7 trillion in the same period of 2023, showing the early signal of recovery. However, it still remains at about half the average of the past five years, making it difficult to say that investment sentiment has fully recovered.

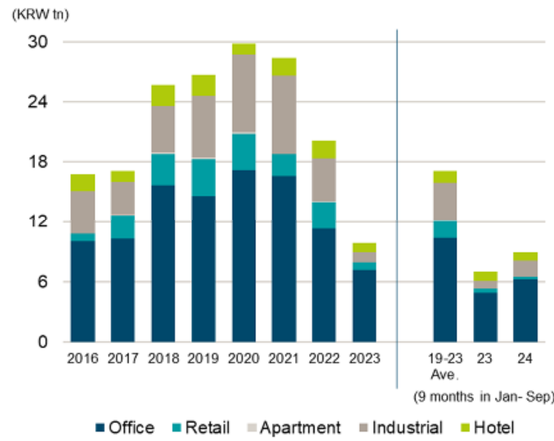
Nevertheless, since the latter half of 2024, a notable number of global investors freed from the denominator effect, have begun to resume equity investments. Domestic investors are also starting to show renewed interest in real estate equity investments, particularly in preferred stocks, moving away from a focus solely on real estate debt investments. This suggests that there is a possibility of a significant revival in direct real estate transactions from mid-2025, when the negative carry between cap rates and lending rates is expected to be resolved.

**Exhibit 3: Commerical Real Estate Transaction Volume in APAC and South Korea**

**APAC Commercial RE Transaction Volume by Country**




**CRE Transaction Volume in South Korea**

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Sources: Real Capital Analytics, DWS. As of December 2024.

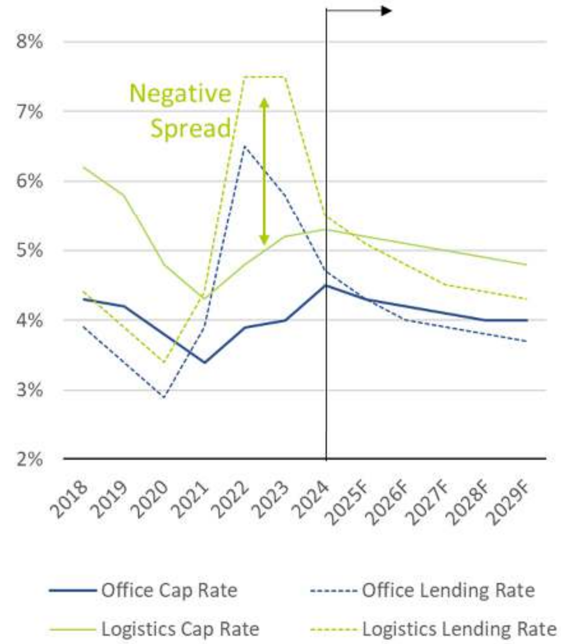
The negative spread between the market cap rate and the lending rate, which once expanded to 250-300 basis points, has sharply declined throughout 2024. This is due to a modest decrease in long-term bond yields and a recovery in lending sentiment towards stabilized assets. In the latter half of 2024, some prime office transactions secured lending rates in the low 4% range, nearly matching their market cap rates. Similarly, prime logistics transactions had lending rates around 5.0-5.5%, with a small negative spread of 20-30 basis points against their market cap rates, showing a rapid narrowing of the negative spread seen between 2021 and 2024.

However, the negative margin between the passing yield of stabilized assets and lending rates is expected to be resolved only from 2026 or later, as many office assets are currently under rented compared to market rents due to the recent surge in office rents in key business districts of Seoul.

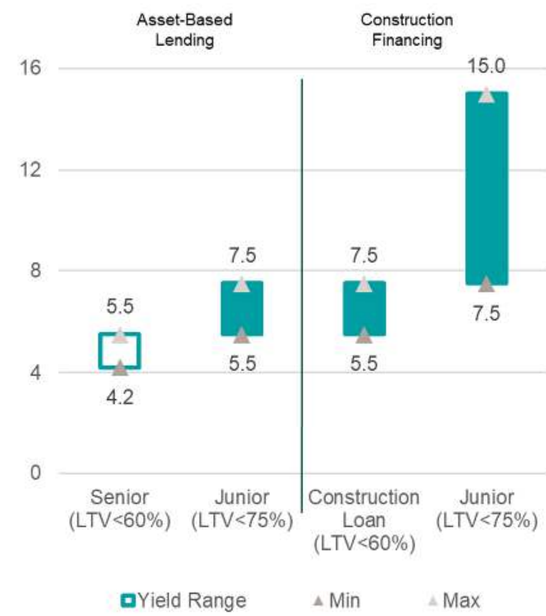
The valuation of the Seoul office market has declined by approximately 8-13% between 2021 and 2024, with a wide bid-ask spread due to subdued investment demand from financial investors. Logistics assets in the Greater Seoul market have seen a larger price drop of about 15-20% in the same period, due to weaker leasing fundamentals compared to the office market. A full recovery is expected around 2026, when the negative spread between market cap rates and lending rates is resolved and leverage starts to normalize.

Exhibit 4: Cap Rates and Lending Rates in South Korea

**Cap Rates and Lending Rates in Office and Logistics Sectors**




**CRE Lending Rates in South Korea**

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Sources: Avison Young, Cushman & Wakefield, DTZ, Real Capital Analytics, DWS. As of December 2024.

# 2 / Real Estate Market Fundamentals

## 2.1 Office

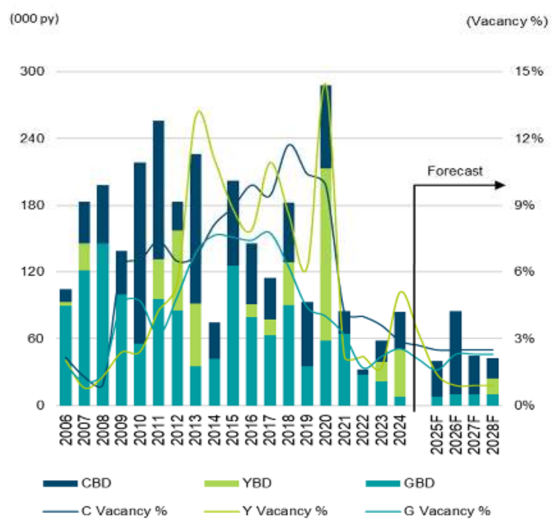
Looking back at past trends in office supply in the Seoul CBD area, there was a phase of rapid quantitative and qualitative growth in the office market due to large-scale supply in prime locations through the redevelopment of the Jongno Cheongjin-dong area. This led to a continuous increase in vacancy rates from around 2010 to 2020. Once the large-scale supply ended, vacancy rates quickly declined from 12% in 2020 to 3% in 2024, completing a 15-year redevelopment cycle.

Looking ahead, future development plans are centered on fringe areas such as the northern part of Seoul Station, Euljiro, and the Sewoon district, rather than the city center. From the perspectives of development cohesion, tenant preferences, and the impact on the surrounding environment, it is believed that the impact of these future supplies on the market will be relatively limited compared to the previous supply cycle. Additionally, due to rising construction costs and difficulties with project financing, the break-even rents for development are significantly higher than the market rents in these areas, likely keeping new office supply limited in Seoul CBD until at least 2028.

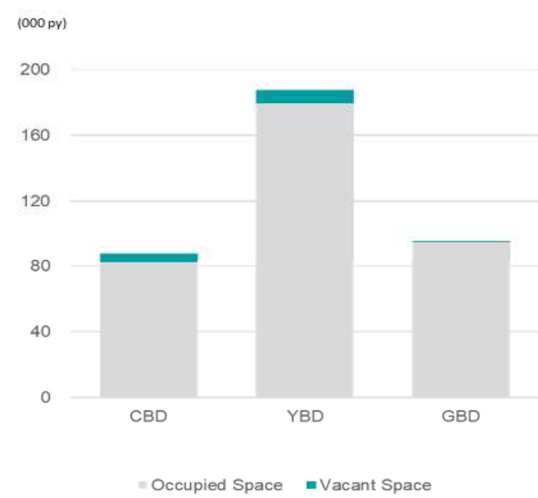
From a leasing fundamentals perspective, the average net absorption in the Seoul CBD office market was approximately 170,000-180,000 pyeong per year from 2010 to 2020. However, over the past five years, average net absorption has increased by 30% to 240,000 pyeong per year, driven by strong leasing demand from the country’s vibrant IT and tech industries as well as strong upgrade demands from "Flight-to-Quality." Despite concerns about economic recession and employment instability potentially affecting future office rental demand, limited vacancies in newly constructed buildings and stable long-term demand in Jongno suggest that the risk of a sharp increase in Seoul's office vacancy rates over the next five years is minimal.

**Exhibit 5: Office Vacancy Rates in Seoul by Submarket**

**Supply and Vacancy Rate of Seoul Office Market (3Q 2024)**




**Vacancy Rates of Buildings Completed after 2020**




*py (=pyeong) is a Korean unit of area. It is equivalent to 3.3 square metres (35.6 square feet).
Notes: GFA = gross floor area. sqm = square metres. Past performance is not indicative of future results. There is no guarantee the supply pipeline will materialize. Forecasts are not a reliable indicator of future returns. Forecasts are based on assumptions, estimates, views and hypothetical models or analyses, which might prove inaccurate or incorrect.
Sources: Avison Young, DWS. As of December 2024.

## 2.2 Industrial

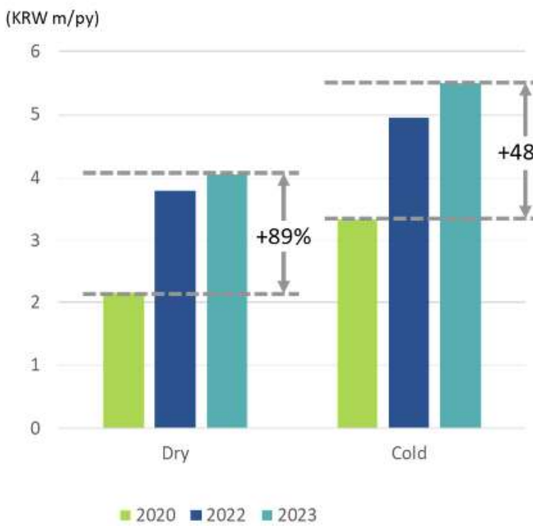
Despite discrepancies in logistics market data, there is consensus that the vacancy rate is notably high in the western submarket of Greater Seoul, where recent supply has been concentrated. The vacancy rate for dry logistics assets in Greater Seoul is estimated at around 9-10%, with continuous record supplies between 2021 and 2024 amounting to approximately 4.6 million pyeong, or about half of the entire logistics stock in the area. Despite this, the vacancy rate has remained stable at around 10%, demonstrating strong rental demand.

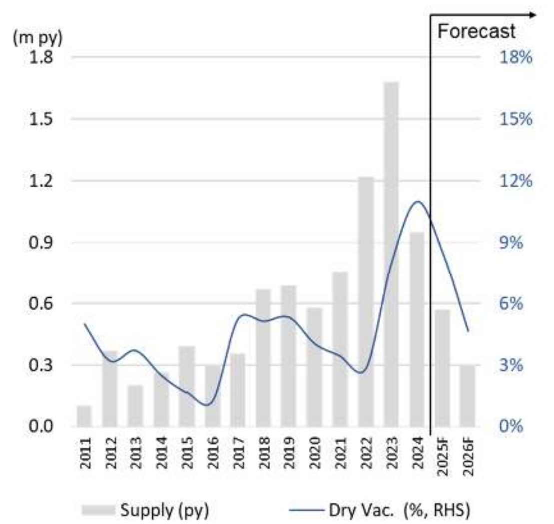
Looking ahead, future logistics supply is expected to be limited from 2026 due to an upcoming supply cliff driven by rising construction and financing costs since 2022. The logistics sector, having the largest building proportion in overall property valuation, is most affected by these rising costs among key sectors. Many development projects have been delayed or canceled over the past 2-3 years due to increased costs and tightened project financing. This impact has been evident since the second half of 2024, with supply levels dropping to the lowest in four years, and a supply cliff expected from the second half of 2025. Additionally, real estate trust companies are increasingly avoiding land trust guarantees due to the rising credit risk of construction companies, making completion guarantees difficult to obtain. The government is also recommending higher equity ratios for new projects, challenging the resumption of delayed projects even if interest rates decrease.

Considering future rent growth, the most noteworthy indicator is the approximately 30% difference between current rents and the rents required for new developments. If a supply cliff occurs and vacancy rates fall below the natural rate from 2026 onward, this gap could rapidly narrow over the next five years.

Exhibit 6: Logistics Supply and Vacancy Rate in Greater Seoul

**Logistics Market Rent and Breakeven Rent for Development** **Logistics Supply and Vacancy Rate in Greater Seoul**

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Sources: DTZ, CBRE, WeFunding, DWS. As of December 2024.

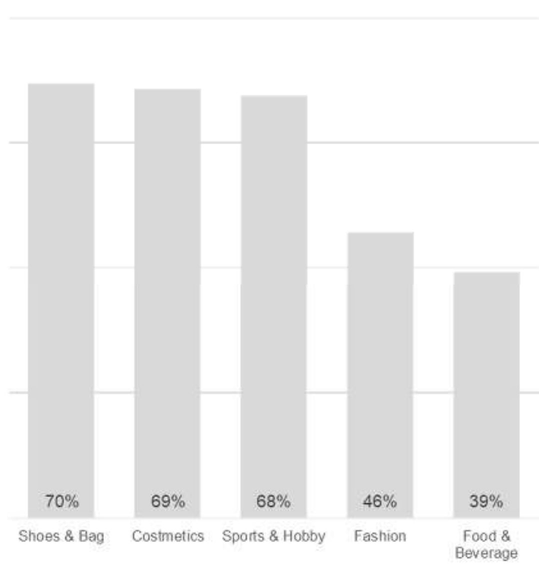
## 2.3 Retail

In the retail sector, sales performance varies significantly by subcategory compared to other markets. Hypermarkets continue to show poor recovery, while department stores focusing on luxury goods, cosmetics, and sports equipment have seen rapid sales growth due to revenge spending during the COVID-19 period. Additionally, retail vacancy rates in major high street retail areas are decreasing due to the increase in foreign tourists visiting Korea. This trend is more pronounced in areas popular with young domestic consumers, such as Hongdae, Hannam, Itaewon, and Seongsu. In contrast, Gangnam and Garosugil are showing slower recovery, with Gangnam experiencing a continuous outflow of retail population to Seongsu, and Garosugil clearly undergoing gentrification.

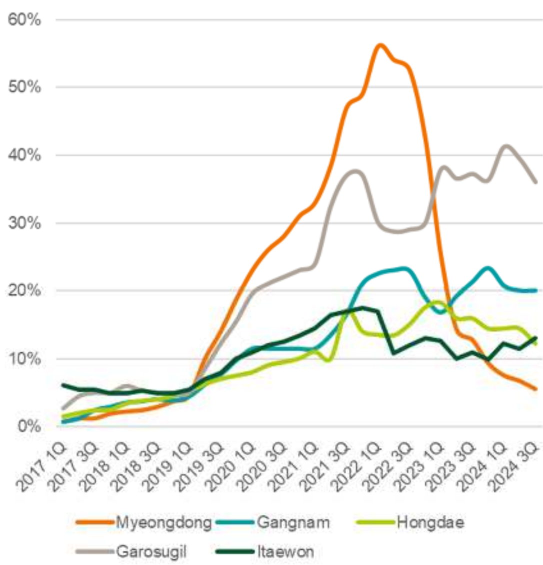
Looking at the characteristics of each high street retail area, Myeong-dong is popular with tourists for cosmetics and beauty products, Hongdae is expanding in medical fields such as dermatology, and Itaewon and Seongsu are notable for the growth of road shops and pop-up stores.

**Exhibit 7: Vacancy Rate and Average Rent of Ground Floor by Retail Area**

**Sales Growth of Department Stores by Product (2020-2023)**




**Vacancy Rates of Key High Street Retail Areas in Seoul**



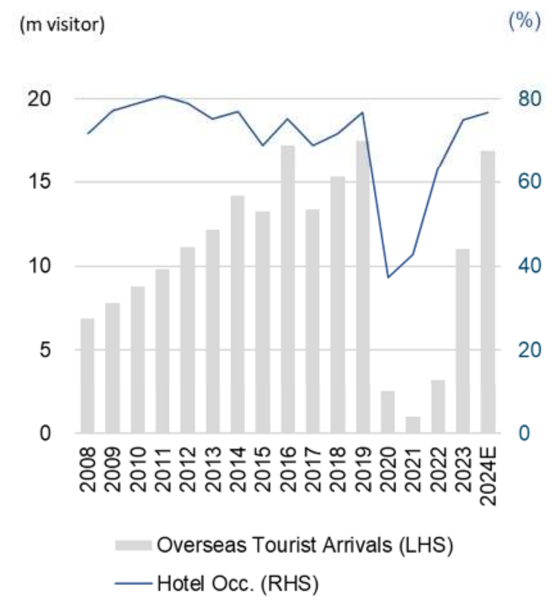

*Py (=Pyeong) is a Korean unit of area. It is equivalent to 3.3 square metres (35.6 square feet).
Notes: Past performance is not indicative of future results.
Sources: Korea Appraisal Board, Cushman & Wakefield, DWS. As of December 2024.

## 2.4 Hotel

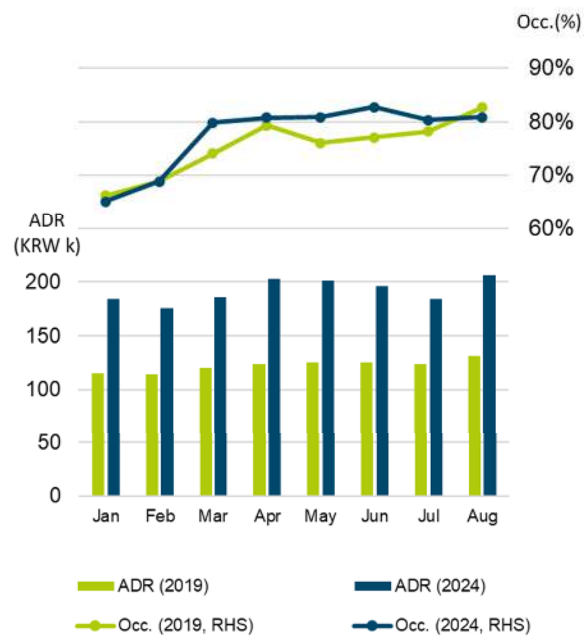
Driven by a rapid recovery of overseas tourist arrivals to South Korea, hotel occupancy rates in Seoul have already recovered to 2019 levels in the first 8 months of 2024, while their marketing strategy is focusing on increasing the Average Daily Rate (ADR) rather than further boosting occupancy rates for the operational efficiency. Average RevPAR once sank below 30% of pre-COVID-19 levels in mid-2020 but currently stands at around 70-90% higher than the 2019. Despite the short-term disruptions related to the political events, South Korea's hospitality market is expected to benefit from further recovery of inbound tourism in the coming quarters, supported by high tourism competitiveness and rising interest in the country's K-Pop or K-Drama culture.

Exhibit 8: Hotel Market Performances in Seoul

**Overseas Tourist and Hotel Occupancy Rate in Seoul**




**Hotel Performance in Seoul (2019 vs 2024)**




Notes: Past growth is not a reliable indicator of future growth. Forecasts are not a reliable indicator of future performance. Forecasts are based on assumptions, estimates, views and hypo-thetical models or analyses, which might prove inaccurate or incorrect.
Sources: Korea Hotel Association, Styleloft, DWS. As of December 2024.

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