

Real Estate Strategic Outlook: Australia

Short-term challenges, longer-term opportunity

Signs of economic slowdown amid rate hikes

With the Reserve Bank of Australia having raised the cash rate by a cumulative 425 basis points since May 2022, inflationary pressures have subsided from the peak of 8%, though the last CPI print in Q3 of 5.4% remains elevated.

Nonetheless, quarterly GDP growth have slowed while other economic indicators such as flat household consumption growth and increased unemployment rate suggest weakening aggregate demand. As such, implied futures¹ are currently pricing in a 60 basis rate cut by end-2024. On a longer-term horizon of 5-10 years, Australia's economic growth underpinned by positive migration inflows is expected to outpace most other developed nations

Ongoing repricing presents mid-term opportunities

Amid weaker transaction volumes and the standoff between buyers and sellers for most of 2022 and 2023, we have seen more advanced repricing occur towards late 2023 with office yields crossing the 6% level, 100-150 basis points higher compared to between 12 to 18 months ago.

While distressed sales opportunities do not appear widespread, higher financing costs and negative yield spreads continue to exert pressure on sellers with weaker balance sheets, presenting potential investment opportunities for discounted sales as we expect yields to correct further before peaking later this year.

Residential: Structural housing shortage driving low vacancy

The residential housing shortage in Australia has been well documented – Strong immigration inflow, low housing availability with record-low construction starts and escalating housing prices resulting in poor purchase affordability. Any turnaround would likely take years to materialize, which underpins the strong rental growth expectations in Built-to-Rent opportunities, on top of

expectations for higher cashflow stability and lower returns volatility.

Logistics: Market underpinned by limited supply and vacancy

Logistics fundamentals remain underpinned by record low vacancy rates, high pre-commitment levels and structural demand drivers including rising e-commerce, migration inflows and A\$230b of infrastructure spending over the next five years.

Prime logistics rents have set new benchmarks following sharp increases in the past two years. Tenant resistances are starting to emerge, but rental growth is likely to remain elevated in the near-term, particularly for prime warehouses with good transport connectivity near urban centers.

Office: Leasing challenges with flight-to-quality and core

With elevated vacancy rates and high incentive levels, office leasing has become increasingly challenging for landlords. Nonetheless, there is a strong divergence in leasing performance with newer premium grade buildings outperforming their aged counterparts in non-core locations. Low development pipeline over the next few years should support rental growth in the longer term, though any office investments should be highly selective and focused on repriced core assets.

Total Return Forecast in Australia, 2024-2033f, p.a.



Source: DWS, January 2024

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¹ ASX 30 Day interbank Cash Rate Futures, as of 18 December 2023

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Real Estate Research Team

Office Locations

Chicago

222 South Riverside Plaza
34th Floor
Chicago
IL 60606-1901
United States
Tel: +1 312 537 7000

Frankfurt

Mainzer Landstrasse 11-17
60329 Frankfurt am Main
Germany
Tel: +49 69 71909 0

London

Winchester House
1 Great Winchester Street
London EC2N 2DB
United Kingdom
Tel: +44 20 754 58000

New York

875 Third Avenue
26th Floor
New York
NY 10022-6225
United States
Tel: +1 212 454 3414

San Francisco

101 California Street
24th Floor
San Francisco
CA 94111
United States
Tel: +1 415 781 3300

Singapore

One Raffles Quay
South Tower
20th Floor
Singapore 048583
Tel: +65 6538 7011

Tokyo

Sanno Park Tower
2-11-1 Nagata-cho
Chiyoda-Ku
18th Floor
Tokyo
Japan
Tel: +81 3 5156 6000

Teams

Global

Kevin White, CFA

Global Co-Head of Real Estate Research

Simon Wallace

Global Co-Head of Real Estate Research

Americas

Brooks Wells

Head of Research, Americas

Liliana Diaconu, CFA

Office Research

Ross Adams

Industrial Research

Sharim Sohail

Property Market Research

Europe

Ruben Bos, CFA

Head of Real Estate Investment Strategy, Europe

Tom Francis

Property Market Research

Siena Golan

Property Market Research

Rosie Hunt

Property Market Research

Carsten Lieser

Property Market Research

Martin Lippmann

Head of Real Estate Research, Europe

Asia Pacific

Koichiro Obu

Head of Real Estate Research, Asia Pacific

Seng-Hong Teng

Property Market Research

Hyunwoo Kim

Property Market Research

AUTHORS



Koichiro Obu
Head of Real Estate Research, Asia Pacific



Seng-Hong Teng
Property Market Research

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