

## Real Estate Strategic Outlook: Australia

### Australia's rate cut cycle to accelerate

#### Shorter, sharper rate cut cycle expected over 2025

The Reserve Bank of Australia (RBA) has begun policy easing, with back-to-back rate cuts from 4.35% to 3.85% over the past six months, US Tariff hikes look to weigh on short term economic growth expectations, with further rate cuts anticipated. Headline inflation remained stable at 2.4% (March 2025), with a notable improvement in the services segment. Economic growth has begun to improve, though reliant on public spend and population growth. The direct impact of US Tariffs on the Australian economy is expected to be limited, largely offset by a weaker AUD and positive Chinese policy, supporting export demand. However a slowdown in global economies has led economists to marginally revise down Australia's economic growth for 2025, noting a slower than anticipated rebound in private consumption. The market and major banks are now pricing in a further 50 basis points of rate cuts over the remainder of the year.

#### Capital markets to benefit from improved borrowing costs

Transaction activity continues to improve, with rate cuts to drive momentum. All sectors experienced year-on-year growth in transaction volumes over Q1 2025, with notable improvements in the retail and hotel sectors. Foreign capital has become increasingly interested in the office sector, particularly Sydney where attractive discounts to book value provides the potential for core+ returns at a core risk profile. Transaction yields have now stabilised in most office markets, presenting a buy opportunity, while industrial yields have begun to compress in Sydney and Brisbane. Lending conditions have improved, with short term swap rates 50 basis points lower than six months ago, though margins have slightly increased. Further declines in borrowing costs should support market liquidity and moderate yield compression.

#### Residential: Supportive legislation to underpin BTR growth

Australia's Build-To-Rent (BTR) sector has experienced growth, though broader supply challenges remain. The BTR sector has seen a doubling of its operational capacity to 10,276 units over the past year, however this remains a small portion of required supply, with dwelling completions lagging annual supply requirements by more than 60% (Dec 24). The government has become increasingly supportive of BTR, with recently legislated enhanced tax concessions to stimulate investment and development activity, while the national rental vacancy rate remains tight sub 2%. Interest rate declines have led to a re-acceleration of property prices, with an expansion of the 5% first home buyer scheme likely to widen the gap between the cost of servicing a mortgage vs rental payments. Personal tax cuts, minimum wage increases

and a boost to rental assistance payments should continue to support underlying growth in rents. We continue to favour 'essential living' BTR products, along key commuter rail lines and emerging CBD hubs, particularly in Western Sydney.

#### Logistics: Infill and Cold storage more favourable

A slowdown in the industrial market, places greater emphasis on asset and sub-market selection. Weaker household consumption continues to weigh on leasing demand, though lower interest rates should provide some relief to consumers. Vacancy remains elevated across most markets with higher incentives influencing effective growth, however more resilient within infill locations and the cold storage market. Infill locations remain crucial for reducing last mile transport costs, while the cold storage market benefits from its relative 'non-discretionary' nature with a preference for pre-commitment keeping vacancy low. The cold storage market remains under supplied at 3% of total stock, compared to more mature markets such as South Korea closer to 30%. We anticipate continued growth in online food, domestic consumption and Australia's role in global food production to drive underlying demand. The outlook for supply is largely concentrated in Greenfield locations, however a pivot towards pre-commitment will likely see project timing pushed out.

#### Office: Higher replacement costs to drive growth in rents

Occupier fundamentals have strengthened, while the supply outlook has moderated. Return to office continues to improve with 'office utilisation' rates sitting at 90% (peak day) of pre covid levels, with the largest improvements in the Sydney and Brisbane markets. Net absorption figures have been mixed, with a preference for newer prime grade assets in core locations, influencing vacancy, incentives & rental performance at a sub-market level. Growth in construction costs, incentive levels and an expansion in yields has led to a 30-40% gap between replacement costs and capital values, which look to weigh on future supply. While we anticipate moderate yield compression, a period of declining vacancy particularly in Sydney and Brisbane likely will warrant upwards pressure on rents to unlock future supply.

#### Total Return Forecast in Australia, 2025-2029f, p.a.



Source: DWS, June 2025

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