dexus

Australian Real Asset Review

Q1 2025

ASCEND Industrial Estate at Jandakot Airport, WA

Inside

Key trends for 2025

Better times ahead for real assets

The start of 2025 is likely to be a turning point for real assets as the interest rate cycle moves to an easing phase. The re-pricing which has occurred to date has reset values and lifted yields, making real assets more attractive to investors. Deal flow is expected to improve significantly in 2025 assuming stable to falling interest rates. However, there is uncertainty around the outlook for inflation, global growth and interest rates given a change of administration in the US and the recent mini-spike in bond yields.

Key trends to watch in 2025 are:

1. **Phase shift for interest rates**: Interest rates are expected to decline in 2025, improving the relative yield for real assets and leading to increased real asset transaction volumes. Transaction volumes for real estate in 2024 were up 6% on the previous year and for infrastructure they more than doubled.
2. **Yields now look more attractive**: Two years ago, A grade office buildings in Sydney were yielding 4.8%. Now they're yielding around 6.3%. Industrial, retail and healthcare assets are also producing higher yields. Within the real asset universe, yield spreads between different investments have widened, creating an expanded opportunity set for investors.
3. **Bottoming of the value cycle:** Valuations appear to be stabilising for most real estate sectors and are lifting for some, like super-regional retail. History has shown that such periods typically lead to above average returns. For example, in the decade following the GFC, office values grew by 75%.
4. **Social infrastructure and emerging real estate sectors look appealing**: Deal flow in the infrastructure sector is expected to increase significantly due to a narrowing of the gap between buyers and sellers and an undersupply of capacity in sub-sectors like healthcare, student accommodation, aged care and social housing. Data centres and cold storage will also be in demand. Each of these sub-sectors offers a strong growth thematic.
5. **The retail sector will surprise on the upside**: The retail sector will see a lift in investment demand. Both discretionary and non-discretionary spending are on the rise. Limited new construction is keeping vacancy rates low. Over the past decade a shift in shopping centre category mixes to include more services and experiences has made cash flows more secure.
6. **Office cycle turning the corner**: The factors needed for a recovery in office markets are now in place – namely a fall in the supply pipeline and growth in services employment. The adjustment to hybrid working models is now well advanced and the merits of offices for collaboration are well understood. High quality buildings in core central locations are set to outperform.
7. **Ecommerce returns as a growth driver for industrial**: Ecommerce should return to being a steady growth driver for industrial demand after a period of consolidation post the pandemic. Asset selection will be key as occupiers focus on strategic locations, efficiency and automation. The industrial sector is expected to see a recalibration of growth expectations after a period of high growth.
8. **Demographic shifts**: Australia's population growth is among fastest of the advanced economies. Within that overall bright picture, the trend of interstate migration towards QLD and WA giving those states an extra boost which will drive demand for housing and infrastructure.
9. **Increasing urban density:** The housing affordability issue and the imperative to supply more housing will drive government programs to encourage residential investment in urban hubs as well as in infrastructure such as the Metro rail in Sydney. Higher population density will be good for shopping centres and warehousing in metropolitan areas.

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Investment climate

Inflation pressures easing

Australia's GDP grew by just 0.8% in the year to Q3 2024, however the subdued growth is consistent with tight monetary policy settings that appear to be successfully reducing inflation. The next phase of the economic cycle is expected to be a period of easing interest rates and firming private sector growth.

Economic growth has been driven by public spending rather than the private sector. The business sector had a relatively weak quarter, with the NAB Business Confidence Index falling 8pts to -3 index points in November. However, the labour market remains strong, with the unemployment rate at 4.0% in December. GDP growth is forecast to improve to 2.4% p.a. in 2025, supported by consumer spending, an improvement in residential construction and infrastructure projects.

The headline annual inflation rate fell to 2.8% in Q3 2024, down from 3.8% in Q2 2024, largely due to weaker goods inflation and electricity rebates. Services inflation remains persistent. Accordingly, the Reserve Bank held the official cash rate steady at 4.35% in December 2024, making it a year since the cash rate last changed. The market consensus forecast is that official cash rates will decline in H1 2025 (possibly as early as February) given a further easing in inflation pressures.

The 10-year government bond yield recently lifted by 30 bps to 4.5%, leading to speculation about a 'higher for longer' scenario which could slow the anticipated recovery in real asset deal flow. On the other hand, any falls in either the cash rate or bond yields through 2025 is likely to be positive for deal flow. The consensus forecast is for bond yields to trade in the range 4.0%-4.5% in the short term.

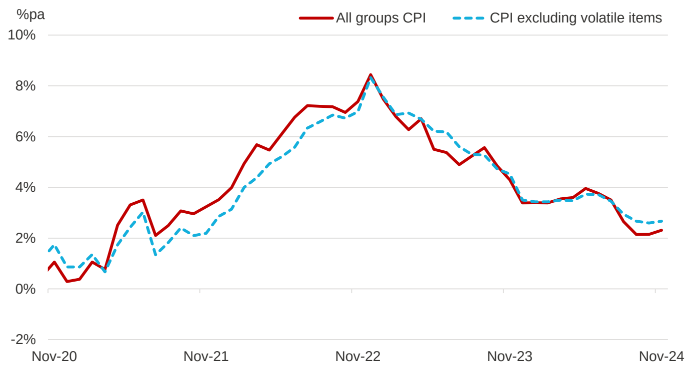
The demand outlook for real asset sectors will be supported by population growth. However, after running at circa 2.5% p.a. in FY23, population growth is forecast to ease back to more normal levels of 1.2% p.a. in 2025 as the net migration surge wanes.

Australian economic forecasts

	Dec-24	Dec-25	Dec-26
Real GDP %p.a.	1.1%	2.4%	2.7%
Employment %p.a.	2.6%	1.3%	1.6%
Unemployment %	4.0%	4.4%	4.4%
Business investment %p.a.	-1.2%	1.4%	4.1%
Dwelling investment %p.a.	2.9%	1.5%	6.5%
Population %p.a.	1.8%	1.2%	1.1%
Retail sales %p.a.	2.8%	3.0%	3.1%
CPI %p.a.	2.9%	3.4%	2.5%
Cash rate %	4.3%	3.6%	3.4%
10yr Bond %	4.5%	4.2%	4.2%

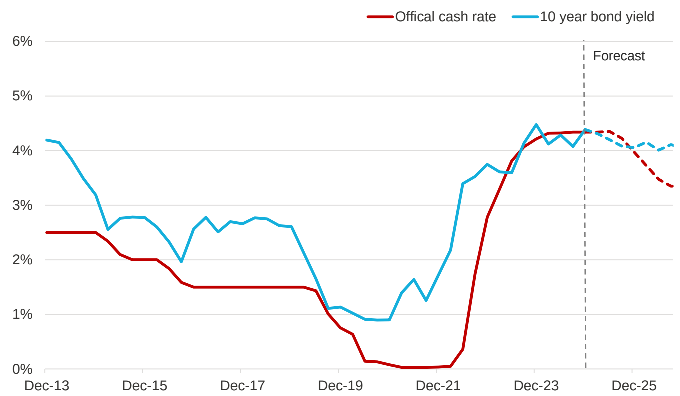
Source: Oxford Economics, December 2024

Australia's inflation rate (monthly)



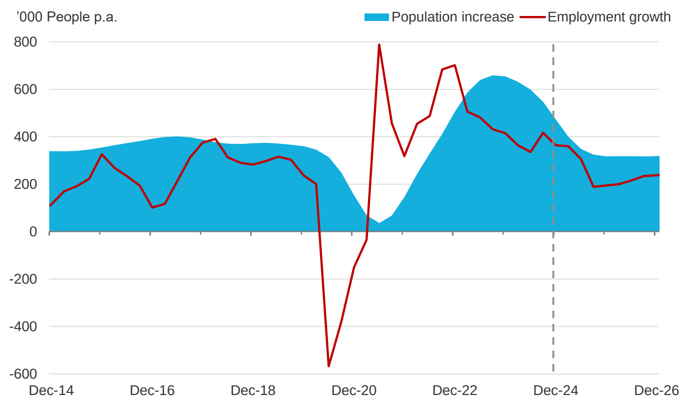
Source: ABS, Dexus Research

Australia's interest rate forecasts



Source: Bloomberg, Oxford Economics

Population and employment growth forecasts



Source: Oxford Economics

Market performance

Fund performance beginning to improve

After a period of weak returns driven largely by an easing of capital values, returns have shown signs of improvement. In particular, the retail sector, which remained flat quarter-on-quarter (q-o-q). All sectors had a higher quarterly return in November than they did three months prior. This improving trend is expected to continue through 2025. Diversified wholesale total returns were down 0.4% q-o-q, but this still represents the strongest result in a year, hinting at a potential turnaround in the year ahead.

Listed real estate had a weak quarter, down 6.0%, but was up 18.5% through the year. Listed pricing, which is sensitive to movements in bond yields, stands to benefit further in 2025 should bond yields fall or the discount to underlying asset values close, or more likely, both.

Capital markets unlocking

After a quiet 2023 characterised by rising interest rates and easing valuations, transaction volumes are showing signs of life. As 2024 progressed, real asset capital markets began to unlock.

Real estate transaction volumes firmed by 6% in 2024 and there are further transactions in the pipeline. The office sector, which faced elevated uncertainty in 2023, saw transaction volumes surge 16% higher in 2024. This uptick signals improving liquidity and a growing confidence in valuations.

Foreign buyers are increasingly active in Australia. CBRE are reporting that offshore investment in real estate increased by 37% in 2024, totalling $8.3 billion. The largest share of investors came from the United States, Japan and Singapore.

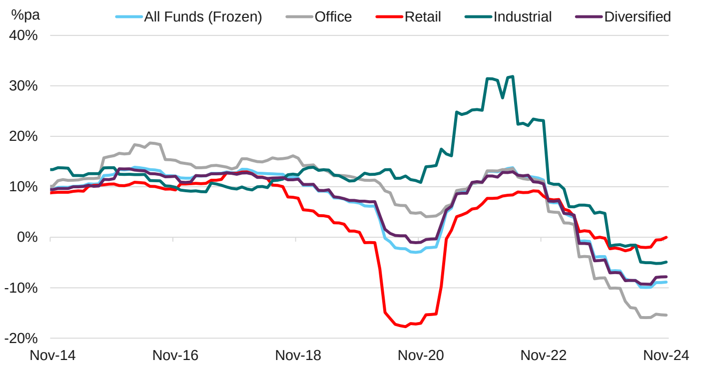
Uncertainty around interest rates is diminishing. Investors are increasingly confident that we are at the peak of the tightening cycle, with the next move more likely down this calendar year. 2025 is likely to be an even more active year for commercial real estate transactions.

Asset class performance to Dec 2024

	Qtr. %	1 yr % p.a.	3 yr % p.a.
AREITs[1]	-6.0%	18.5%	3.5%
Australian shares[2]	-0.8%	11.4%	7.4%
Infrastructure[3]	8.6%	21.1%	8.0%
Australian cash[4]	1.1%	4.5%	3.2%
Australian fixed interest[5]	-0.3%	2.9%	-0.8%
Unlisted property[6]	0.3%	0.0%	-2.7%

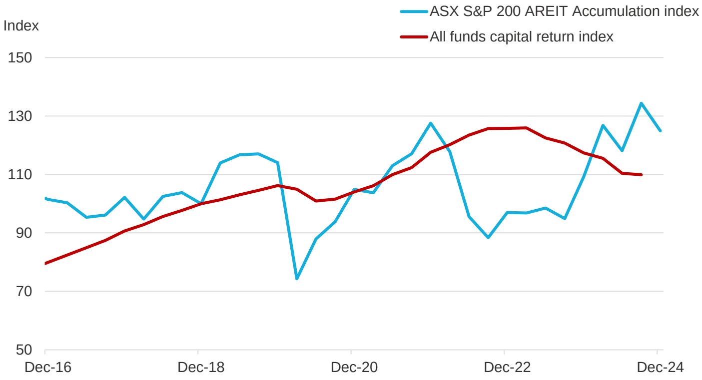
Source 1: S&P/ASX 200 A-REIT Accumulation Index
Source 2: S&P/ASX 200 Accumulation Index
Source 3: Dow Jones Brookfield Global Infrastructure Total Return Index
Source 4: Bloomberg BAUBIL Index
Source 5: Bloomberg BACM0 Index
Source 6: MSCI/Mercer Australian Core Wholesale Monthly PFI (Nov -24)

Unlisted wholesale fund returns by sector



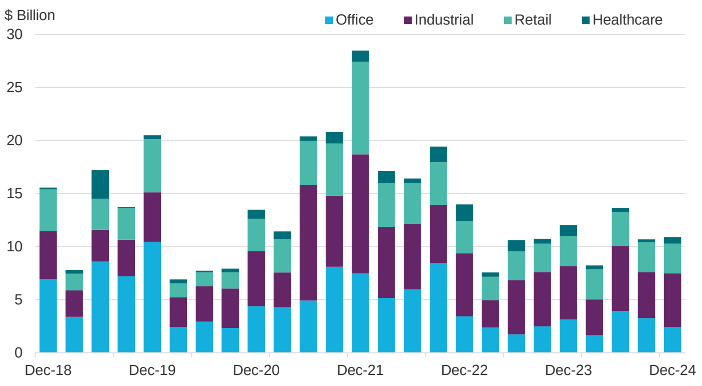
Source: MSCI, Dexus Research

AREIT price and unlisted capital return indexes



Source: Bloomberg, MSCI Core Wholesale Fund Capital Return Index

Yearly investment volumes – real estate



Source: MSCI Real Assets

Infrastructure

Deal flow gathering pace

Global infrastructure deal value rose 1.5% in calendar 2024 to US$352.3 billion, showing a clear firming trend over the past six months. The number of deals declined, consistent with a trend towards larger deals. The improvement in deal flow was particularly notable in Australia, where total infrastructure M&A deal value more than doubled in 2024 to US$27.8 billion. Australia's number was heavily influenced by the US$15.0 billion AirTrunk deal in Q4 2024, but after stripping this out, deal flow still increased significantly by 45% in the year.

In Q4 2024 there were significant transactions across the transport, energy and digital infrastructure sectors. Major transactions in the digital space in Q4 2024 included Infratil's injection of US$268 million of equity into CDC Data Centres and HMC Capital's acquisition of Australian co-location data centre operating platform iSeek for US$264 million as well as Global Switch's Australian data centres for US$1,199 million. The implied EV/EBITDA multiples for these transactions were 19x and 22.5x respectively. Renewable energy transactions included the acquisition of Neoen's Victorian renewables assets for A$950 million and Wild Cattle Hill Wind windfarm in Tasmania for US$185 million.

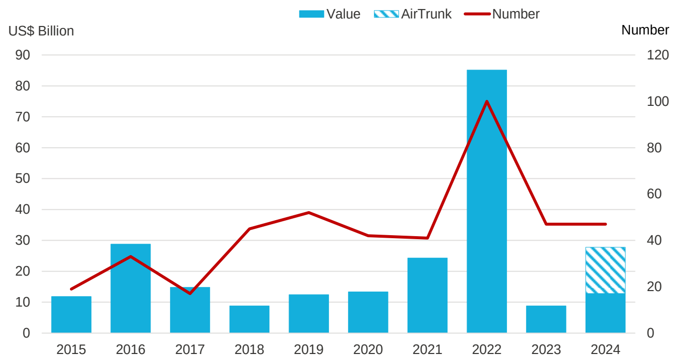
The Australian Government continues to advance its $213 billion five-year Major Public Infrastructure Pipeline with a focus on addressing the housing crisis and supporting the energy transition. Activity in this space included:

- Awarding the first national Capacity Investment Scheme (CIS) tender to 19 projects in different states, with a collective capacity of 6.4 GW of renewable energy and power storage;
- Approving the (US$3 billion) HumeLink project, which will construct 365 km of 500-kilovolt high-voltage transmission infrastructure in NSW; and
- Announcing a new partnership with the states to deliver up to 5,000 new social homes under a fast-track Round 2 of the Housing Australia Future Fund.

Looking ahead, transaction activity in 2025 is expected to be supported by falling interest rates, which enhances the relative yield of infrastructure investments, and an undersupply of student accommodation, aged care, healthcare and transport.

Australian unlisted infrastructure funds returned a creditable 7.3% in the year to September 2024 (latest available data), outperforming the Australian listed infrastructure funds (4.5%). Global listed infrastructure benefited from general strength in equity markets to return 23.7%.

Australian M&A infrastructure transaction volumes



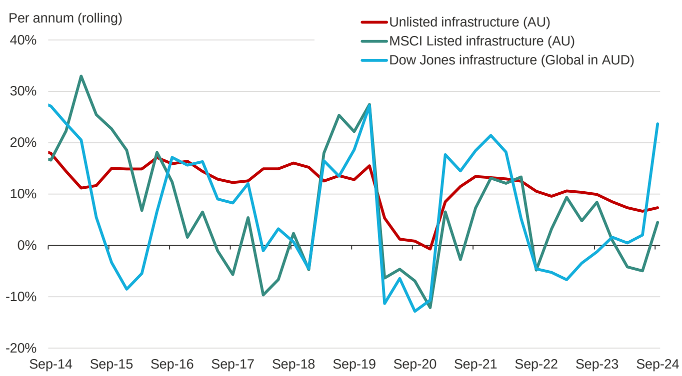
Source: Infralogic (closed transactions)

Major infrastructure transactions Q4 2024

Date	Asset	Buyer	Value (US$ million)
Nov-24	Rail First	CVC DIF	n.a.
Nov-24	Global Switch	HMC Capital	$1,199
Nov-24	iSeek	HMC Capital	$264
Dec-24	CDC	Infratil	$268
Dec-24	Spark Mobile towers	CDPQ	$509
Dec-24	Wild Cattle Hill Wind	Igneo Infrastructure	$185
Dec-24	Neoen Renewables	HMC Capital	$588

Source: Infralogic, Dexus, *includes closed and pending transactions

Australian and global infrastructure returns



Source: MSCI Australia Quarterly Private, Infrastructure Fund Index Australia Listed Infrastructure MSCI Index, Dow Jones Brookfield Global Infrastructure Total Return Australian Dollar Index

Office

Office sector turning the corner in 2025

The office sector is expected to improve in 2025, with demand increasing, most notably in Sydney. Much of the uncertainty around hybrid working seems to be behind us and the vacancy cycle at its peak. However, signals are still mixed from market to market.

Sydney CBD had its second consecutive quarter of positive net absorption at 9,300sqm in Q4 2024, taking total demand for the year to 86,400sqm. Prime incentives fell to 34.3% and net effective rents grew 4.0% over the year. Brisbane CBD is the standout performer with the strongest net absorption of all the markets at 16,300sqm in Q4 2024. Brisbane has the lowest vacancy among the CBDs at 9.8% and saw strong net effective rent growth of 11.9% in the year.

Meanwhile, Perth CBD had a mildly weak quarter with net absorption of negative 2,300sqm, with vacancy increasing to 15.8%. Melbourne CBD is lagging the other CBD markets with soft demand, no change in the vacancy rate at 19.8%, and a 3.2% fall in net effective rents in Q4 2024.

Australian office tenants across the market are engaged in both a flight to quality (high quality assets) and a flight to value (affordable space). Decision making continues to lack urgency. Sub-500sqm requirements are still the most active and most of these tenants are seeking fitted out space.

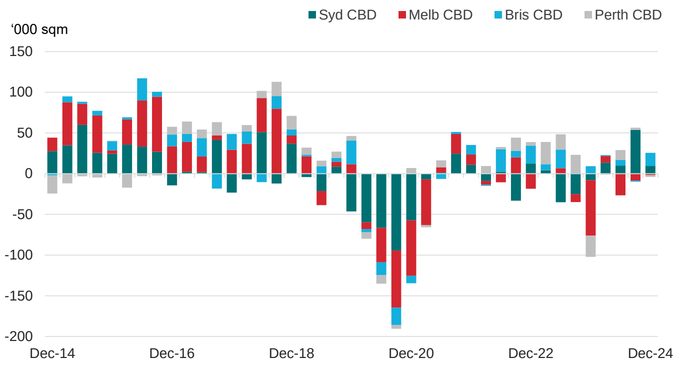
The supply pipeline has significantly contracted, with forecast commencements for FY25-27 down 32% compared to the five-year average. Supply is being deferred due to both weak market conditions and high construction costs. New supply requires rents higher than the current market to support new feasibilities. This deferral of supply which will help to protect existing stock from oversupply and support rent growth through the cycle. In addition the gap between market rent and the economic rent for a new build, which in Sydney is estimated to be in the order of 20%, implies a growth phase in market rents as the catch-up occurs.

Office snapshot

	Total Vacancy	Q4 Rent growth* (% p.a.)	Projected Net supply FY25-27 (%p.a.)
Sydney CBD	15.5%	4.0%	1.5%
North Sydney	21.0%	-3.9%	2.0%
Sydney Fringe	14.1%	-5.7%	0.3%
Parramatta	24.6%	-4.9%	2.4%
SOP / Rhodes	20.2%	-4.5%	0.0%
Melbourne CBD	19.8%	-7.2%	1.3%
Brisbane CBD	9.8%	11.9%	1.2%
Perth CBD	15.8%	1.4%	1.8%

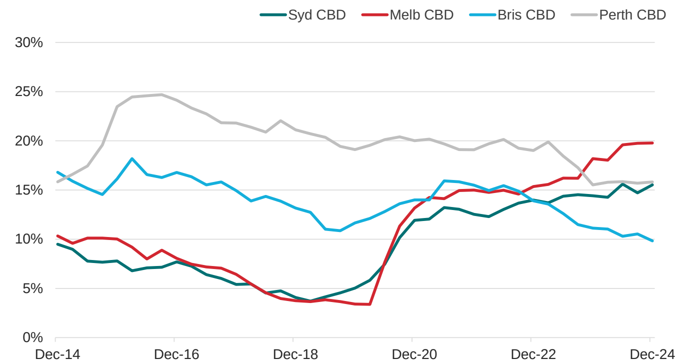
Source: JLL Research, Dexus Research, *Rent growth is net effective

Quarterly net absorption by CBD market



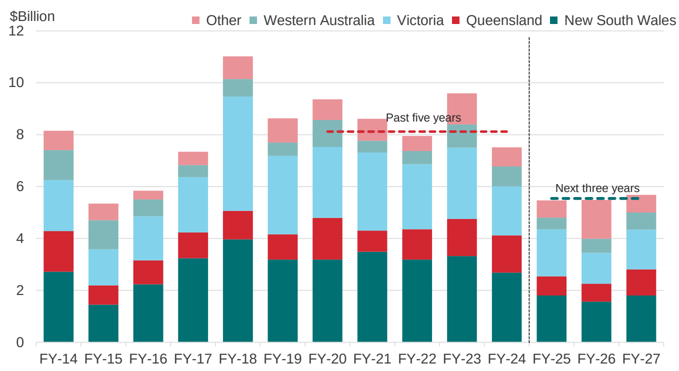
Source: JLL Research, Dexus Research

Vacancy rates by CBD market



Source: JLL Research

Office commencements



Source: Oxford Economics

Office market wrap

Market	Comments	Direction of trend for next 12 months	
Sydney CBD	Sydney CBD demand showed improvement this quarter, with positive net absorption of 12,000sqm. Despite this, vacancy rates increased by 0.8% to 15.5% mainly due to the completion of several new buildings. Prime gross face rents increased 0.9%, while effective rents saw a rise of 1.1%. Tenants are paying a premium for buildings in sought after locations, near public transport and amenity for their staff. The addition of ASX's sublease space at 20 Bridge Street (11,108sqm) to the market led to a slight increase in sublease availability however sublease space has fallen significantly in the year and signs are positive as Westpac will now re-occupy their remaining sublease space in Barangaroo. Prime incentives decreased to 34.3%, and yields remained stable at 6.3%.	Vacancy	↓
		Rents	↑
		Incentives	↓
		Yields	→
North Sydney	North Sydney demand showed positive momentum over the quarter with net absorption of 8,600sqm. The vacancy rate decreased 1ppt to 21%, driven by deals at 177 Pacific Highway, 2 Blue Street, and 100 Arthur Street. The opening of the Victoria Cross metro station has seen a significant increase in commuter and pedestrian activity in the area. The preference by tenants for fitted spaces remains strong, with 94% of transactions in 2024 being for fitted-out spaces. Sublease vacancy shrank 53% in 2024, reflective improving market conditions. Victoria Cross tower will reach completion in 2025, which is likely to lead to a spike in vacancy as tenants move from other North Sydney assets into the building. Yields increased 0.2ppts to 7.2% and incentives remained the same at 39.4%.	Vacancy	↑
		Rents	→
		Incentives	→
		Yields	↑
Parramatta	Vacancy in Parramatta rose to 24.6% due to a lack of large deals in 2024. Demand remains subdued and tenants that are prepared to consider Parramatta also consider options in other metropolitan markets, like Rhodes and Norwest. The Government remains the predominant tenant in Parramatta, which is unlikely to change in the foreseeable future. Incentives increased to 46.9% and yields rose to 8.1%.	Vacancy	→
		Rents	→
		Incentives	↑
		Yields	↑
Melbourne CBD	Melbourne CBD demand remained weak this quarter, with public administration continuing its consolidation across the market. However, prime grade net absorption remained positive for the second consecutive quarter. Vacancy remained steady over the quarter at 19.8%, prime grade incentives increased 1.5ppts to 46%. Preference for fitted space sub-500sqm remains the common trend, with limited interest in unfitted space. Coles committed to moving to 720 Bourke Street from Hawthorn East for over 40,000sqm which will improve sentiment in Docklands. Effective rents decreased -3.2%, and yields increased to 7.1% over the quarter.	Vacancy	→
		Rents	→
		Incentives	↑
		Yields	↑
Brisbane CBD	Brisbane CBD recorded positive net absorption of 16,300sqm this quarter. Vacancy decreased to 9.8%, with prime vacancy at 7.4%. Demand predominantly came from Public Administration and Financial Services, including Queensland Health and Senex Energy, expanding or relocating. The completion of developments at 360 Queen and North Quay will place upward pressure on market vacancy as pre-commitment tenants relocate from within the market. Effective rents continue to grow primarily due to falls in incentives. While new leasing volumes are lower y-o-y, the decision of most organisations to renew in their existing premises is creating a strong environment.	Vacancy	→
		Rents	↑
		Incentives	↓
		Yields	→
Perth CBD	Perth CBD recorded negative net absorption of 2,300sqm over the quarter. However, upward trends over the past 3 years in commodity prices and mining activity has supported tenant demand, especially in prime grade assets with good quality fitouts. The overall vacancy rate has increased to 15.8% with prime grade vacancy sitting at 13.5%. Face rents have increased during the quarter, but incentives remain stubbornly high at 47.7%. Incentives in the market are likely to remain elevated in 2025. Yields remain unchanged at 7.4%.	Vacancy	↓
		Rents	↑
		Incentives	→
		Yields	↑

Industrial

A slower year with growth tapering

The industrial sector has seen a year of slowing growth, with net face rent growth flattening in the past quarter and incentives rising. The ongoing cost of living pressures have constrained retail spending with flow-on effects for the warehouse leasing market.

Take-up in 2024 was a little higher than the previous year and slightly above pre-COVID levels. There were several large prelease deals that boosted take-up despite reduced demand overall. There are some positive signs for 2025, as retail spending has been firming in the past few months and online spending is rising again. These trends should lead to increasing demand from retailers and 3PLs.

Vacancy rates have continued to rise across the nation, albeit remain low in absolute terms. New supply brought to market and a preference by occupiers for newer premises has meant that solid pre-commitment take-up was accompanied by higher vacancy in older sheds. However, supply completion levels were lower in Q4 and going into 2025 it is likely that developers will reduce the level of speculative developments where possible as costs remain high and development margins are tight. Positive demand and lower levels of speculative supply should help limit vacancy levels.

Prime net face rents in the Outer West of Sydney rose 2.2% in the quarter and 5.3% over the year. Other markets were flat in the quarter such as Inner West and South Sydney, but still grew over the year with 3.8% and 11.7% respectively. Melbourne and Perth rents were mostly flat. In Brisbane, the Southern Brisbane and the Australian Trade Coast markets enjoyed positive face rent growth, growing 3.7% and 4.0% over the quarter. Incentives have risen in most markets through 2024, so effective rents fell in some of the outer markets.

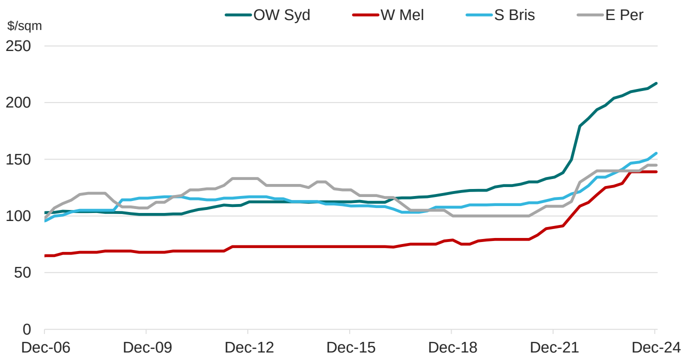
Average prime yields remained stable across most markets through Q4 and are forecast to see limited movement through 2025. Almost all markets, save West Melbourne which saw a 25-bps increase, saw no yield change over the quarter.

Industrial snapshot

	Prime cap rate change from Q2 2024 (bps)	Existing prime net face growth % y-o-y
Outer West Sydney	0 bps	5.3%
West Melbourne	25 bps	8.0%
East Perth	25 bps	3.6%
South Sydney	0 bps	11.7%
Inner West Syndey	0 bps	3.8%
Southern Brisbane	0 bps	10.1%

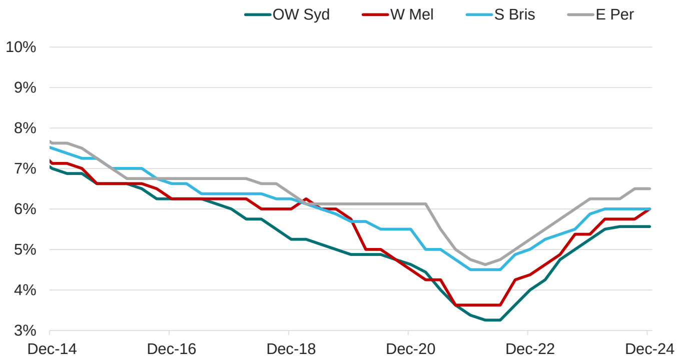
Source: JLL Research, Dexus Research

Industrial net face rents by precinct



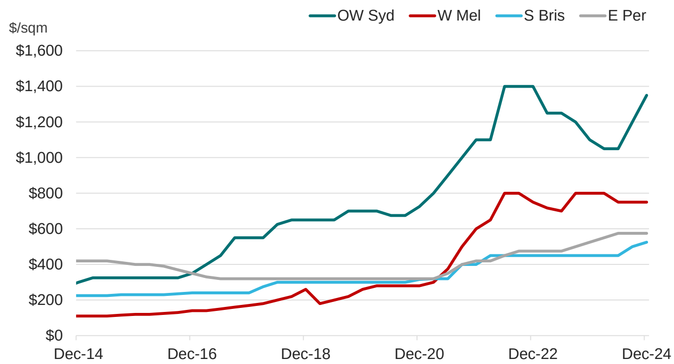
Source: JLL Research, Dexus Research

Industrial cap rates by precinct



Source: JLL Research (average prime), Dexus Research

Industrial land values by precinct



Source: JLL Research 2-5HA land values *East Perth = 1HA, Dexus Research

Industrial by region

Outer West Sydney

Take-up in Outer West Sydney increased over the 12 months to Q4 with 160,000sqm over the quarter and 494,000sqm over the year. A significant amount of this was sublease space taken up largely by manufacturing and transport companies. Alspec, a manufacturing company, alongside COPE a transport and warehousing company, have preleased 40,000 and 39,000sqm respectively at the Alspec Industrial Business Park located in Orchard Hills. Nippon Express, a postal and courier service, took up 17,000sqm in Kemps Creek. The vacancy rate is currently sitting at 3.2% (according to SA1 Property), which is up from 1.5% a year ago. Prime net face rents are sitting at $217/sqm.

West Melbourne

Take-up in West Melbourne in 2024 was higher than the previous year, but still below the two years prior. This demand was largely driven by manufacturing and logistics tenants. This quarter saw a large amount of take-up at 208,000sqm, making a total of 617,000sqm over the year. Essity, a global health and hygiene company, leased 40,000sqm and AGCO corporation, a manufacturer took up 30,000sqm, both in Truganina. Vacancy in Melbourne has been on the rise, and the West Melbourne vacancy rates are now at 3.9%, up from 2.2% a year ago. Prime net face rents are sitting at $139/sqm.

Brisbane (South and Australian Trade Coast)

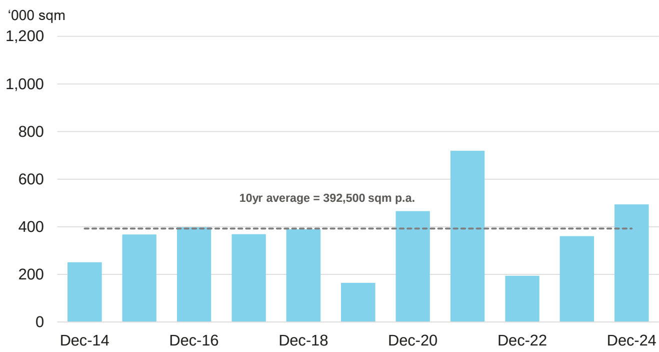
Demand tapered through 2024 and was below the ten-year average. The Australian Trade Coast saw a large pull back on demand over the year, and the only space taken during the quarter was from TNS logistics who leased 3,400sqm in Hemmant. The vacancy rate in Southern Brisbane rose in the quarter and is now 4.4%, up from 3.5% a year ago, one of the highest in the nation. The ATC vacancy rate also lifted and is now 3.2%, up from 1.5% in 2023. Net face prime rents are $155/sqm for South Brisbane and $197/sqm in the ATC.

Perth (East & South)

Perth has seen strong demand over the past twelve months. In the East, 81,800sqm was taken up over the quarter, with Blue Star Logistics taking up 9,000sqm in Hazelmere. In South Perth, 10,800sqm was taken up in Jandakot, one of the tenancies being Jaycar, a motor vehicle retailer, who leased 5,800sqm. Vacancy rates have remained quite low, due to the higher demand, but still increased slightly over the quarter. Prime net face rents are currently $145/sqm in East Perth and $135/sqm in South Perth.

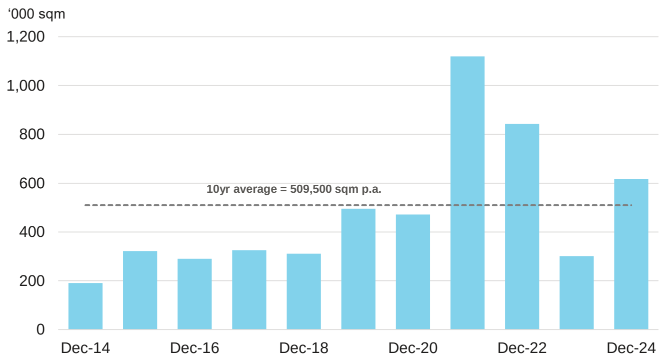
Note: Vacancy data for all markets is from SA1 property

Outer West Sydney gross take-up



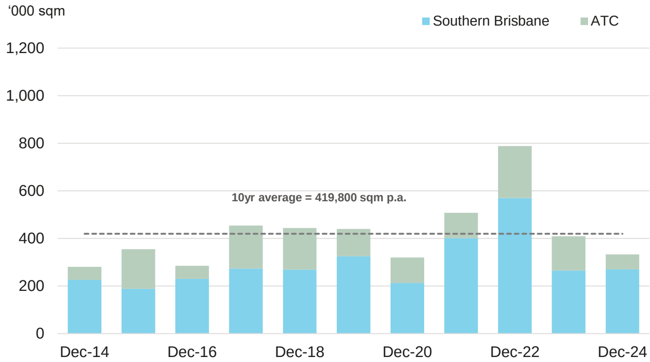
Source: JLL Research (gross take-up), Dexus Research.

West Melbourne gross take-up



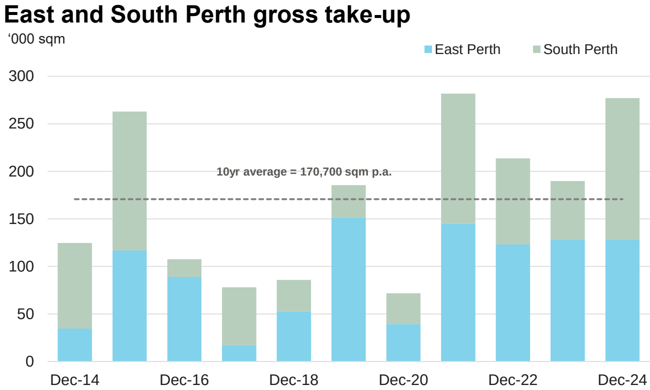
Source: JLL Research (gross take-up), Dexus Research

South Brisbane and ATC gross take-up



Source: JLL Research (gross take-up), Dexus Research

East and South Perth gross take-up



Source: JLL Research (gross take-up), Dexus Research

Retail indicators

Sales growth to improve through FY25

The Australian retail landscape was challenging through 2024 as the cumulative impact of interest rate hikes weighed on spending. However, over the past six months conditions have improved. Interest rates have remained stable, tax cuts boosted take home income and weaker goods inflation eased cost of living pressures to a degree.

A notable bright spot emerged during the Black Friday sales period. CommbankIQ data revealed a robust 7% increase in spending during the two weeks surrounding Black Friday compared to 2023. The strong performance in discretionary goods, which surged 11%, was encouraging. The Black Friday trading period set new spending records across many retail assets, suggesting consumers are reshaping their spending patterns to capitalise on major promotional periods.

Total retail spending grew by 3.0% in the year to November. Among the categories, pharmaceuticals were the leading category, growing by 8.9% y-o-y. Cafes & restaurants posted a 3.6% increase. Household goods sales remain subdued reflecting weak housing construction. Both liquor sales and department stores declined 1.2% compared to the previous year. After a post-pandemic lull, consumers are now spending more online. Online spending grew 8.7% y-o-y.

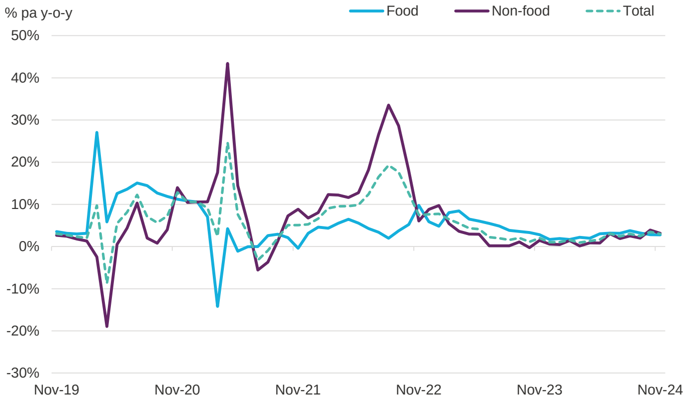
In 2025, population growth, a major contributor to retail sales growth, is expected to remain positive but ease from the high levels of last year. In addition, retail price inflation is expected to ease. Despite these influences, we do anticipate an increase in headline retail sales growth in 2025 due to a significant turnaround in real per capita spending (see chart). Per capita spending has been unusually negative in recent years but should return to more normal levels given falling mortgage rates, rising incomes and easing cost of living pressures.

Retail sales growth by category (November 2024)

	m-o-m	y-o-y	MAT
Cafes	1.5%	3.6%	1.7%
Clothing	1.6%	1.8%	0.8%
Department Stores	1.8%	-1.2%	0.6%
Food	0.5%	2.8%	2.6%
Other	0.3%	7.0%	4.8%
Household Goods	0.6%	1.2%	-0.2%
Total	**0.8%**	**3.0%**	**2.1%**
Online Sales	1.2%	8.7%	7.9%

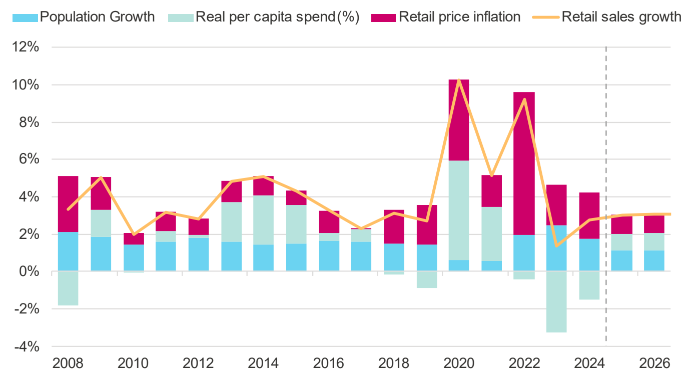
Source: ABS, Dexus Research

Discretionary vs non-discretionary spending growth



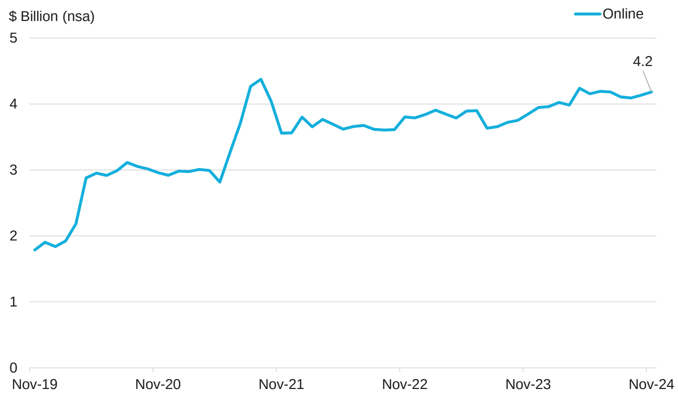
Source: ABS, Dexus Research

Components of retail sales



Source: Oxford Economics, Dexus Research

Level of ecommerce sales



Source: ABS, Dexus Research

Retail performance

Retail's improving value proposition

The retail property sector is showing encouraging signs of recovery, outperforming other commercial real estate sectors after a challenging period in recent years. While retail unlisted funds posted a modest total return of -0.5% in the year to November 2024, they significantly outperformed the broader market's -9.0% p.a. return.

On the occupancy side, leasing demand has been resilient in the face of generally subdued spending growth. Melbourne and Sydney regional shopping centres are experiencing declining vacancy rates. Occupancy costs are below pre-pandemic levels, creating a buffer for both tenants and landlords. The lower cost base provides runway for future rental growth without putting excessive pressure on retailers.

The supply side of the equation is looking particularly favourable for existing assets. Construction costs and planning restrictions are acting as natural handbrakes on new supply. Consequently, the new supply pipeline of subregional and regional space is running at just 70% of the 20-year average. There are no new regional shopping centres in development.

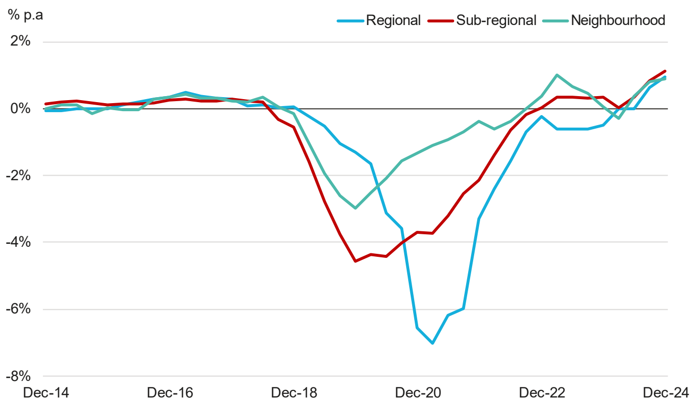
The investment case for retail property has strengthened considerably. Yields have been more stable than other sectors, and some sub-sectors, like Sydney neighbourhood centres, are even seeing yield compression. Over the past decade a shift in shopping centre category mixes to include more services and experiences has made cash flows more secure which may be leading to a re-evaluation of risk premiums.

Retail performance snapshot

	Q4 Specialty rent growth % y-o-y.	Cap rate change q-o-q (bps)
Sydney		
Regional	1.0%	0
Sub-regional	0.4%	-25
Neighbourhood	0.8%	-25
Melbourne		
Regional	1.0%	0
Sub-regional	0.4%	0
Neighbourhood	0.4%	0
SE QLD		
Regional	2.6%	0
Sub-regional	4.8%	0
Neighbourhood	3.2%	-12.5

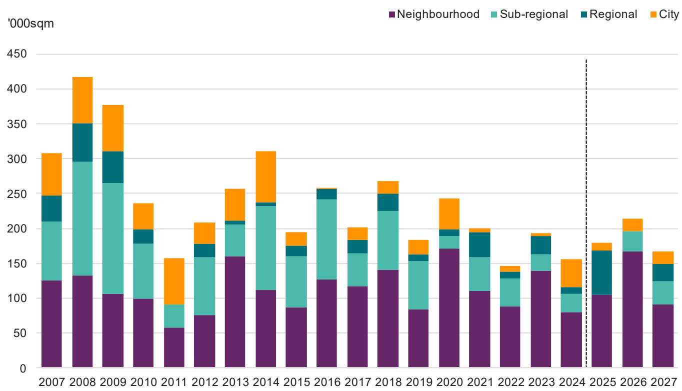
Source: JLL Research, Dexus Research

Shopping centre rent growth



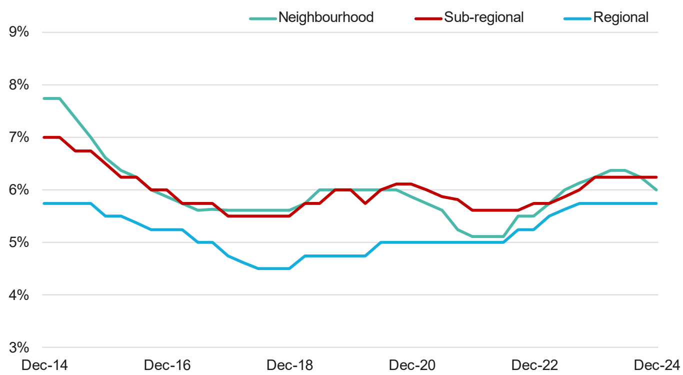
Source: JLL Research, Dexus Research

Australian enclosed shopping centre supply



Source: JLL Research

Yields by centre type



Source: JLL Research, Dexus Research

Healthcare

Returns trending positive in 2025

Healthcare returns are now turning the corner, helped by higher income returns and a tapering of the decline in capital values. The MSCI healthcare index is expected to return 0% in the year to December 2024. Returns are trending upwards and are expected to continue to strengthen through 2025. Deal flow is expected to improve due to the attractiveness of the higher yields on offer.

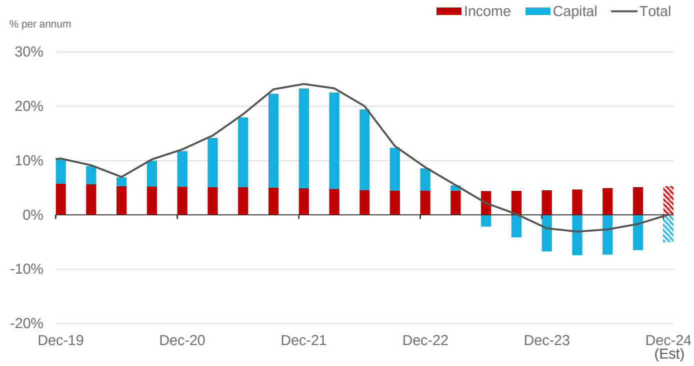
As demand for healthcare services grows, the sector is facing significant challenges such as workforce shortages and rising costs, albeit with variable effects depending on service type and location.

The overall workforce has been increasing as more students enter the workforce. However, it has become harder to fill roles given the expansion. From 2020-21 to 2022-23, the fill rate for medical professionals decreased from 62% to 44%. The number of applicants per vacancy has also decreased from 7.3 to 5.1 over the same time period. Impacts such as burnout, an ageing workforce and a fall in part-time participation are pressuring the already tight workforce. Over time, technological advances, addressing rates of pay and the skilled migration program are expected to help ease the pressure on staff within the industry.

Hospital separations (attendances) continue to grow, however there a significant shift from multi-day or overnight stays to same-day services. This shift benefits demand for day hospitals while increasing the pressures felt by private multi-day hospitals. The shift to shorter hospitalisations is driven by factors like cost pressures, technological advancements, and capacity constraints in the public system. Demand for same day services is increasing at a rate of 3.1% per year compared to 1.8% for multi-day services. In the 2022-23 period, 64% of private hospital separations were for same day services. Delivering services in day hospitals is more cost-effective than in multi-day facilities because day hospitals have lower overhead costs and don't have to sustain as many complex and technical services that a multi-day facility would provide.

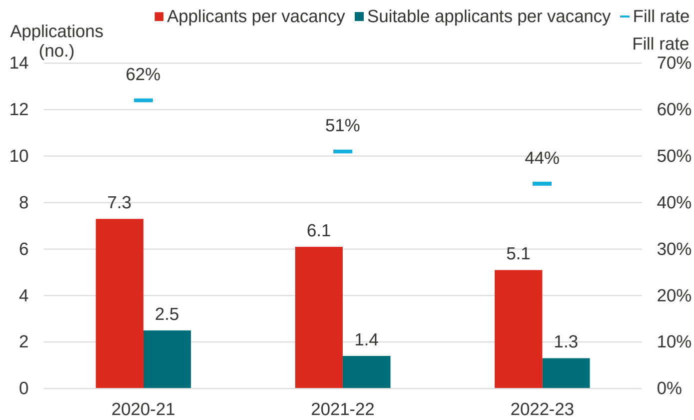
Rising out-of-pocket GP costs are a growing concern for consumers, impacting the affordability of healthcare services and leading to reduced GP attendances. Several factors are contributing to this including: increasing cost of services compared to the indexation of Medicare funding, gaps in private health insurance coverage and declining bulk billing rates. Out-of-pocket costs are now at the highest levels seen in the past decade. The situation should be helped by the FY24 budget where the Federal government announced changes to Medicare that provided a $1.5bn boost to Medicare indexation and tripled bulk billing incentives for GPs.

Healthcare performance – total return composition



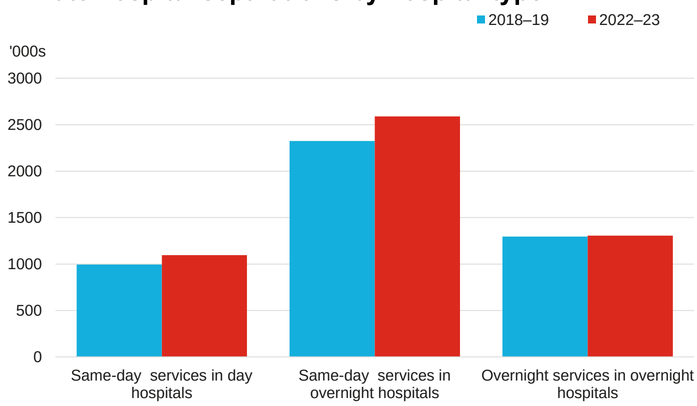
Source: MSCI (Dec 24 values are estimated)

Proportion of vacancies filled for health professionals



Source: Australian Institute of Health and Welfare

Private hospital separations by hospital type



Source: Australian Institute of Health and Welfare

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