

Real Estate Strategic Outlook: United Kingdom

Cautious optimism that the tide is turning

The UK economy is gaining momentum

First quarter growth exceeded expectations, business indicators are improving, inflation continues to fall and rate cuts could begin in August.¹ While recovery will likely be gradual, momentum should build over the year as improving household incomes pave the way for a consumer-led recovery. With that in mind, the medium to longer term outlook is more positive. GDP growth is forecast to outperform the Eurozone over a 10-year horizon, with London expected to remain a key driver of economic growth.²

Prices have largely stabilised for prime real estate

Prime yields expected to move in from next year

Recent indicators show stabilisation in prime property yields.³ At present, investment activity has yet to see any meaningful rebound, but much-anticipated rate cuts should stimulate liquidity over the second half of the year. In addition, a general election has been announced for July, yet this is not expected to deter a real estate recovery. On the contrary, a more certain political environment should reassure international investors and improve liquidity.

Logistics will likely be the first sector to see any notable price recovery, with prime yields forecast to compress over the coming six months. The other sectors should follow from 2025, with prime yields then expected to compress over a five-year horizon. At the same time, prime rent growth should further support robust returns, leading to UK outperformance.²

Residential: operational residential to offer the highest returns

Robust fundamentals should continue to support healthy rent growth in the UK build-to-rent sector and we maintain our positive view. However, operational residential, such as student housing and co-living, could outperform. Supported by the same demand-supply imbalance in many major cities, a higher entry yield should encourage more attractive risk-adjusted returns.

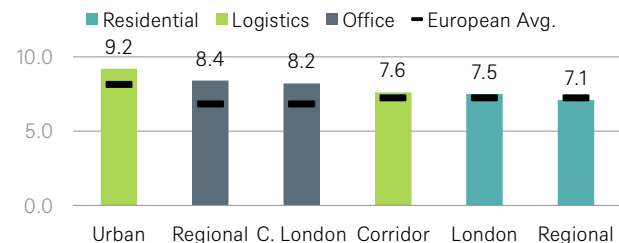
Logistics: a more selective approach to location

Overall, we maintain a positive outlook on UK logistics. However, national vacancy has increased sharply over the last 18 months to stand at 6.9% at end-2023, from a low of 2.2% in 2022, and is now back in line with pre-Covid levels.⁴ As such, location selection is important. Outperformance is most likely in the more supply-constrained urban and Last Hour markets around the UK's major cities. Within these locations, strong rental uplift and higher returns could be captured through the redevelopment of ageing stock into modern, energy-efficient logistics.

Office: trophy assets at reasonable prices?

Our positive outlook for best-in-class offices is unchanged. In the City of London, prime yields stand at 5.75%, a level last seen in the immediate aftermath of the global financial crisis and reflective of a 30% price correction. With that in mind, we see the opportunity to buy repriced trophy assets at attractive prices. In addition, office-to-best-use conversions remains a key strategy. In the West End, for example, the refurbishment of secondary office stock to Next Generation offices continues to stack up, whereas in locations outside of the CBD, but still within London, a residential or hotel conversion is likely to be more appropriate.

Prime Gross Total Return Forecast*, 2024f-2033f (% p.a.)



*Gross total returns minus capital costs
Source: DWS, June 2024

¹ DWS, Oxford Economics, May 2024

² DWS, June 2024

³ CBRE, Knight Frank, May 2024

⁴ Savills, January 2024

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Real Estate Research Team

Office Locations

Frankfurt

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

London

45 Cannon Street
London, EC4m 5SB
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
15th 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

Sydney

Level 16, Deutsche Bank Place
Corner of Hunter and Phillip Streets
Sydney NSW 2000
Australia
Tel: +61 2 8258 1234

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 & Retail Research

Ross Adams

Industrial Research

Sharim Sohail

Self-Storage 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

Matthew Persson

Property Market Research

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Autho



Rosie Hunt
Property Market Research

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