Appendix C – Market Analysis For Quarter 2

Market Summaries:

HOUSING MARKET

UK house prices fell by 0.2% in March, after taking account of seasonal effects. Nevertheless, the annual rate of house price growth edged higher to 1.6% in March from 12% in February. House prices rose by 0.7% in September, taking annual growth to 3.2%, according to Nationwide. This represents the strongest annual house price growth figure since November 2022.

Activity has picked up from the weak levels prevailing towards to the end of 2023, however, remains relatively subdued by historic standards. For example, the number of mortgages approved for house purchase in January was around 15% below pre-pandemic levels. This largely reflects the impact of higher interest rates on affordability. While mortgage rates are below the peaks seen in mid-2023, they remain well above the lows prevailing in the wake of the pandemic.

With cost-of-living pressures easing as inflation moves back towards target, consumer sentiment is improving. Surveyors are reporting a pickup in new buyer enquiries and new instructions to sell in recent months, with all regions seeing an improvement in the annual rate of change in the first quarter of 2024. London has remained the best performing southern region with annual price growth recovering to 1.6%.

Moreover, with income growth continuing to outpace house price growth by a healthy margin, affordability is improving, albeit gradually. If these trends are maintained, activity is likely to gain momentum, though the pace of the recovery is still likely to be heavily influenced by the trajectory of interest rates.

The RICS has been engaging with stakeholders in relation to leasehold reform matters contained in the 7 November Kings Speech and the subsequent Government consultation: Modern leasehold: restricting ground rent for existing leases.

High mortgage rates caused by inflation have caused the market to cool. Buyer affordability is constrained as average mortgage rates hover around 6% which is unaffordable for many. Many first-time buyers have been discouraged from entering the market due to the high interest rates and are therefore opting to rent instead, the rental market remains exceptionally strong because of this.

RESIDENTIAL GROUND LEASES

For the avoidance of doubt, due to the functioning nature of the market, our valuation is reported as being subject to ‘material valuation uncertainty’ as defined by VPS 3 and VPGA 10 of the RICS Valuation – Global Standards. This declaration reflects VPS 3 and VPGA 10 of the RICS Valuation – Global Standards (“the Red Book”) and may be considered to be an unprecedented set of circumstances on which to base a judgement. Consequently, less certainty, and a higher degree of caution may be attached to these valuations than would normally be the case. Given the unknown future impact that the consultation might have on the ground rent investment market valuers are, where appropriate, advising that the valuation of residential ground rent investment assets be kept under frequent review. The inclusion of a material valuation uncertainty declaration does not mean that the valuation cannot be relied upon.

SOUTH EAST OFFICE MARKET

In October take-up across the Greater London & South East market at the end of Q3 2024 reached 2.1 million sq ft, which was 38% above Q1–Q3 2023 and 5% above the five-year average. Take-up levels have grown incrementally each quarter this year, with Q3 take-up amounting 756,000 sq ft, 10% above the previous quarter.

Prime and Grade A office space continues to be occupiers preference, accounting for 80% of take-up in Q1–Q3 2024, which is driving rental growth across the market. However, only 13% of supply across the Greater London and South East market is classified as Prime.

Southeast office space has seen a 0.75% increase in prime yeilds up from 7.00% in October 2023 to 7.75% in October 2024.

SOUTH EAST INDUSTRIAL MARKET

In recent years, demand in the South East has favoured distribution logistics over B1 manufacturing space, with firms seeking locations in proximity to good transport connections. Rental growth has remained strong in the South East industrial market through 2023. In many industrial hotspot locations, including Croydon, Crawley, Gatwick, and Slough, there has been particularly strong take up and robust rental growth observed as demand for good quality space continues to outstrip supply. Whereas locations with supply constraints, where good quality stock is limited, are suffering from lower take up levels and static rental growth. Yields stabilised at pre-pandemic levels of around 4.4% in the South East in 2023.

Take-up of Logistics and Industrial properties in the United Kingdom totalled 6.2m sq ft during Q3 2024 across 43 deals, the lowest quarterly volume since Q1 2020. Despite a markedly slow quarter with volumes impacted by ongoing uncertainty in the UK economy, take-up during 2024 is both 18% higher than at this point in 2023 and is 5% above the 5-year Q1-Q3 pre-pandemic average. Industrial prime yields are down 0.25% from 5.25% in October 2023 to 5% in October 2024.

SOUTH EAST RETAIL MARKET

Increasing business costs, rising interest rates and cautious consumer sentiment have created a challenging economic climate for the recovery of the high street retail sector in recent years. As a result, several large tenants including Wilkos have fallen into administration. This has contributed to rising vacancy rates in many high street locations. Prime high street rents have either remained stable or declined across the South East retail market, with take up remaining subdued. Declining rental values since 2017 still persist with new supply being limited, with most development in these areas concentrated around the repurposing of retail property for other uses. This will reduce the overall retail stock and help ease vacancy rates in towns across the South East.

Similar to the wider UK market, the UK retail warehousing market has been the favoured part of the retail sector in the South East over recent years. The popularity of discount retailers, such as Poundland and B&M has driven expansion amongst this sector, mostly choosing to take space in out-of-town retail parks. High demand and low supply have kept vacancy rates in the South East amongst the lowest in the UK.

In terms of transaction activity, the market has outpaced last year's performance for the same period. According to data from RCA, investment volumes reached £24.1 billion for the first three quarters of 2024, compared to £22.3 billion in 2023. However, sector performance varies. Office (-17.7%) and industrial (-7.5%) volumes remain low, while retail (-0.3%) is essentially flat. Although vacancy rates have not yet reached levels that inspire widespread investor confidence in the strength of the 'in-town' occupational market, the stability of both this market and consumer footfall, alongside consistent demand from operators seeking new space, offers a positive outlook. LDC reports that high street vacancy currently stands at 14.0% and has been stable for the past four quarters, while shopping centre vacancy is at 17.6%, showing minimal fluctuation since early 2023.

Further, rents for new leases on high streets and within shopping centres continue to show modest growth, according to Savills' internal data. As of September, headline rents averaged £27.77 per square foot over the past four quarters, representing a 0.4% increase over Q2. This marks continued positive quarterly growth for five consecutive quarters, the first sustained improvement since the cost of living crisis caused a brief dip in rents. This trend indicates a growing competitive tension among operators looking to expand, particularly in well-occupied areas, which are well-represented in Savills' new transaction portfolio.

High street retail prime yields are down from last year by 0.25% from 6.75% in October 2023 to 6.5% in October 2024.

Commercial Office Market Summary

In the commercial property sector high borrowing costs have dampened activity, one market being hit significantly is office space partially because remote work trends continue to limit the demand for it. Retail properties remain to be affected by decreased consumer spending due to the cost-of-living crisis, decreasing footfall on high streets significantly. There has been an increase in commercial to residential conversion projects as developers pivot in response to the decreased demand for traditional office and retail space and invest in residential space.