CLUTTONS
INVESTMENT MANAGEMENT

cluttonsim.com

Commercial property examiner

Q4 | 2025

Contents

1. Key takeaways

The UK economy is currently operating below potential, with stalled employment growth and cautious spending and investment from households and businesses. However, the outlook has improved, with strengthening PMI data. The annualised growth forecast has been revised up to 1.8% per annum over the next three years. Inflation is expected to return to the 2% target by the end of 2026, driven by declining energy and food prices and slower wage growth.

World financial markets remained positive in Q4, with the MSCI World Index rising by 4.1% in both USD and hedged GBP terms. However, concerns exist about the stretched valuations of AI stocks and the impact of President Trump's policies. UK gilts yields fell across all maturities in Q4, but the yield on 10-year Gilts remains at its highest level since the banking crisis of November 2008.

The UK commercial real estate market slowed in Q4, with MSCI Monthly Index total returns decreasing by 36 basis points to 1.42% quarter-on-quarter and 7.1% for the 12 months to 31st December 2025. Capital growth was limited in 2025. All Property equivalent yields have hardened by 10 bps in the 12 months to December but have made a negligible contribution to any change in valuations over the course of the last year. Meanwhile, market rental value growth remained resilient, particularly in the office and industrial sectors. Total returns remain largely driven by the income component.

The Investment Property Forum (IPF) lowered its 2026 projection for total returns to 8.3%. Forecasts for market segments show continuing support for Shopping Centres, Retail Warehouses, and West End Offices. Whilst we expect All Property market rental value growth to slow from its current annual rate of 3.4%, it will remain above the 2.0% post GFC annualised average. The outlook for yields will also improve should risk-free rates ease and UK real estate benefit from foreign direct investment originating in Europe and further afield. We now expect All Property total returns to reach 9.0% in 2026, and to average 8.0% annually through to 2028, though these forecasts are subject to risks stemming from ongoing global geopolitical instability.

2. The UK economy

- **Economic activity is currently below potential, the labour market shows stalled employment growth, whilst households and businesses remain cautious about spending and investment.**
- **But the outlook over the three-year forecast period has improved from an annualised growth rate of 1.5% to 1.8% and respondents to the PMI survey support the view of a strengthening outlook for the UK economy.**

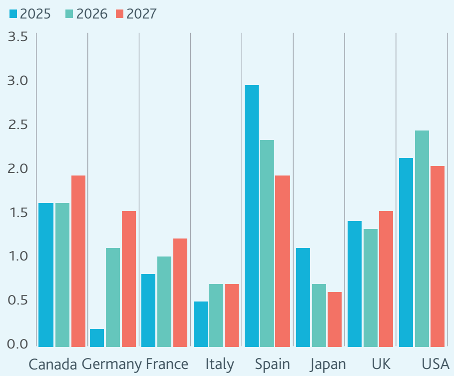
The recent moves by the US in Venezuela, and President Trump's threats of additional tariffs on European countries for resisting his purported annexation of Greenland reflect the current global risks facing countries and economies. Andrew Bailey, the Governor of the Bank of England, warned a Treasury Select Committee that there are "substantial risks" of spillovers to UK financial markets from President Trump's attacks on the independence of the Federal Reserve and his threat to annex Greenland.

Even so, the IMF's January World Economic Outlook (WEO) written before the latest events, predicts that global growth will remain resilient at 3.3% in 2026 and at 3.2% in 2027. These rates are similar to the estimated 3.3% outturn expected in 2025. The forecast represents a small upward revision for 2026 but no change for 2027 compared with that in the October's WEO. This steady performance reflects the balancing of the headwinds from shifting trade policies offset by tailwinds from surging investment related to technology, including artificial intelligence, more so in North America and Asia than in other regions.

Yet risks to the outlook remain tilted to the downside. Disappointment around current AI-related productivity growth expectations could lead to a decline in investment, and trigger an abrupt financial market correction, spreading from AI-linked companies to other segments and eroding household wealth. Trade and political tensions could also disrupt the global economy by affecting financial markets, supply chains, and commodity prices. In addition, policy uncertainty, although lower than it was in October, is still much higher than it was in January 2025.

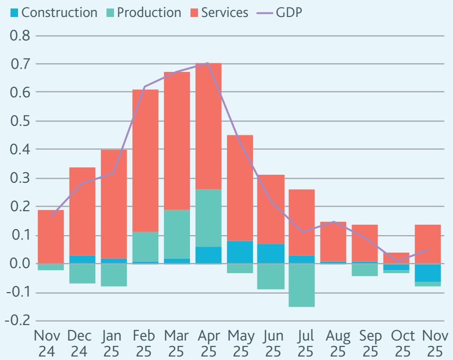
For advanced economies, growth is projected to be 1.8% in 2026 and 1.7% in 2027. Growth in the euro area is expected to pick up modestly to 1.3% in 2026 and 1.4% in 2027. In the UK, economic growth of 1.3% in 2026 is expected to rise to 1.5% in 2027. Inflation, which increased last year partly due to one-off regulated price changes, is expected to return

Global GDP forecasts (%)



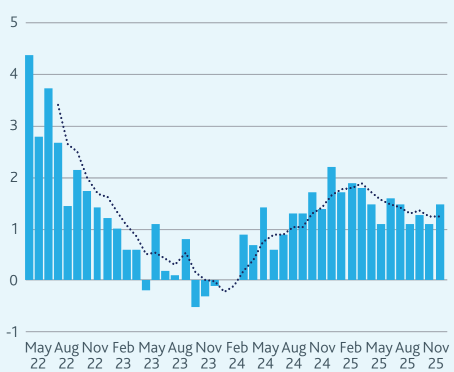
Source: IMF, Jan 2026

GVA% (quarterly growth)



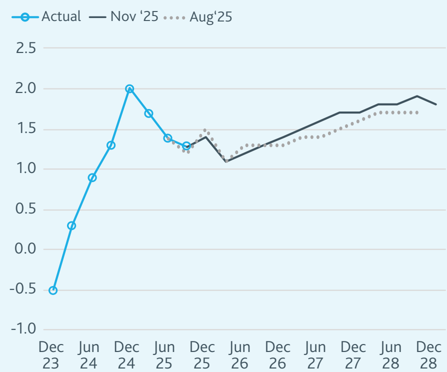
Source: ONS, Jan 2026

UK annual % economic growth



Source: ONS, Jan 2026

Actual GDP % growth and MPC forecasts



Source: ONS & Bank of England, Nov 2025 & Jan 2026 to target by the end of 2026 as a weakening labour market continues to exert downward pressure on wage growth.

UK GDP surprised on the upside and is estimated to have grown by 0.3% in November, following a fall of 0.1% in October 2025 and growth of 0.1% in September 2025. In the three months to November GDP is estimated to have grown by 0.1% compared to the previous three-month period, following no growth in the three months to October and 0.1% in the three months to September. The largest contribution to the three-month-on-three-month growth came from the services' sector. Within the production sector, there was a 18.9% fall in the manufacture of motor vehicles, trailers and semi-trailers resulting from the Jaguar Land Rover cyberattack. Over the longer term, GDP is estimated to have grown by 1.4% in the 12 months to November, compared with the same twelve months a year ago. Over this period, services grew by 1.7%, construction grew by 1.4%, and manufacturing rose by 0.3%.

November's Monetary Policy Report from the Bank of England warns that economic activity in the UK is currently operating below its potential, reflecting weaker-than-expected US exports and temporary disruption caused by the Jaguar Land Rover cyberattack. Underlying GDP growth may have been marginally better than expected, but it still remains weak.

The labour market is softening. Employment growth has stalled, job vacancies have declined, and the unemployment rate has risen to 5.1% in the three months to November from 4.4% at the start of the year. Recent policy-driven cost increases, including higher employer National Insurance contributions and the National Living Wage, have weighed on hiring decisions. With demand remaining weak, businesses are unlikely to expand their workforce significantly, and spare capacity in the economy appears to be increasing.

Household demand also remains fragile. Although retail sales volumes reached their highest level since 2022 in September, they are still around 2% below their pre-pandemic level in late 2019. The household savings ratio which peaked at 27.4% in Q2 2020 during the Covid lockdown, and pre-pandemic was around 6.5%, has yet to return to historical norms. It decreased to 9.5% in Q3 2025 from 10.2% in Q2 2025.

Business confidence remains weak and investment intentions subdued. Global conditions provide only limited support. While the world economy has shown resilience to recent trade developments and benefitted from strong AI-related investment, particularly in the US, global growth has eased.

The MPC now expects annual UK GDP growth to dip below its current rate of 1.4% before recovering, supported by the lagged effects of recent interest rate cuts, gradually looser monetary policy, improved financial conditions, and stronger global demand. The annualised average forecast over the next three years has improved from 1.5% to 1.8%. However, the growing risks of weak demand and a softening labour market underline the importance of ensuring that policy remains sufficiently supportive to prevent an entrenched period of low growth and below-target inflation, suggesting that further cuts to base rate are in the pipeline so long as UK GDP growth remains subdued.

With the uncertainties caused by November's messy budget process ended, there is additional evidence that supports the view of a strengthening outlook for the UK economy. The S&P Global UK Composite PMI increased to 51.4 in December 2025 from 51.2 in November and 50.1 in September, reflecting the eighth consecutive period of expansion in British private sector activity with a slightly firmer expansion for services and an extension to the rebound for manufacturers who recorded their highest reading in over a year. The rise in new business was the strongest for 14 months reflecting improved service sector demand as client confidence improved. New overseas work increased in December, ending a 13-month period of decline but higher employment costs and uncertainty surrounding future demand drove down employment numbers.

3. Inflation and prices

- **Annual CPI inflation rose unexpectedly to 3.4% in December from 3.2% a month earlier, but is still down from 3.8% in September**
- **The MPC said market pricing indicates that CPI inflation will drop to around 3% in the coming months, mainly due to declining energy and food prices and slower wage growth, is expected to fall back to the 2% target by the middle of next year.**

Annual CPI inflation growth remains above the MPC's 2% target. The latest CPI numbers disappointed as 12-month inflation rose by more than expected in December, climbing by 3.4% compared to a 3.2% rise in the 12 months to November. Alcohol and tobacco, and transport, made the largest upward contributions to the monthly change in annual CPI rates.

Core inflation excluding energy, food, alcohol and tobacco has fallen steadily over the last year, reaching 3.2% in December, but this remains above the 2.7% average registered between 2011 and the pandemic. Service sector CPI inflation decreased to 4.5% in December from 4.7% in September. Annual wage growth excluding bonuses is also slowing, down to 4.5% in the three months to November, compared to 4.7% in the three months to August.

External factors have also modestly supported disinflation. Higher global tariffs have slightly reduced UK-weighted global export prices, partly through trade diversion away from the US towards the UK and euro area, particularly from China. Together with a small appreciation in sterling, this has contributed to subdued UK import price inflation.

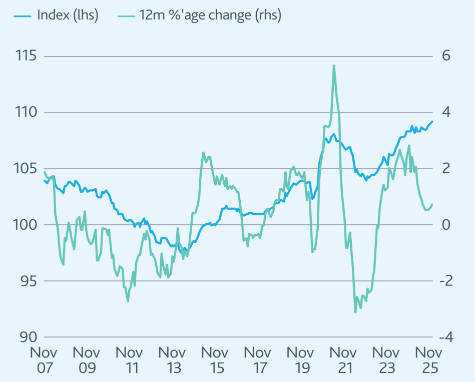
The MPC's November forecast indicates that CPI inflation is projected to fall below 3% this year, driven by lower contributions from energy and then fall towards 2% target next year, as economic slack continues and food prices and a further easing in services inflation as wage growth slows. Inflation is then expected to return gradually to the 2% target over the medium term, as economic slack continues to weigh on domestic price and wage-setting.

Wage growth is forecast to slow significantly, with private sector regular earnings growth falling from around 4.4% in mid-2024 to about 3% by mid-2027, reflecting weaker labour market conditions and lower inflation expectations.

The MPC has reduced Bank Rate from 5.25% to 3.75% since August 2024, lowering the degree of monetary restriction. However, with inflation still above target, policy must remain sufficiently tight to ensure inflation returns to and remains at 2%. Further rate cuts are therefore likely to be gradual .

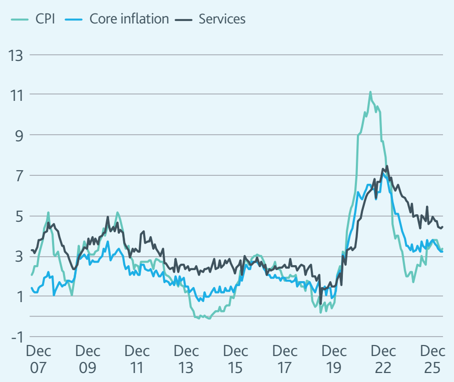
The market-implied path for interest rates underpinning November's MPC forecasts indicates that a further reduction in base rates from 3.75% to 3.5% could be expected by the end of H1 2026. However, as we commented in our last report, a continuation of the UK's weak economic growth could make a reduction in Base Rate to 3.25% or 3.00% in H2 2026 possible.

Real pay index, sa (May 2005=100)



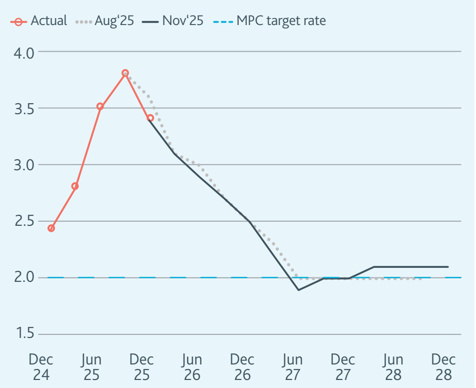
Source: ONS, Jan 2026

CPI inflation (%pa)



Source: ONS, Jan 2026

Annual CPI and MPC forecasts May '25



Source: ONS & Bank of England, Nov 2025 & Jan 2026

4. Stock markets, interest rates & asset yields

- **World financial markets remained positive in Q4, with the MSCI World Index rising by 4.1%. But threats to stability exist from the stretched valuations of AI and the intemperate policy decisions of President Trump.**
- **UK gilts yields fell across all maturities in Q4 but the yield on 10-year Gilts of 4.57% at the end of Q4 was still at the highest since the banking crisis of November 2008.**

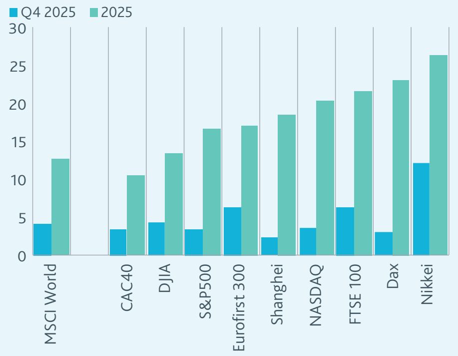
Over the course of Q4, the number of warnings that US tech – especially AI-linked – stocks look richly valued and vulnerable to a correction has grown. Following cautions issued by Investment Banks, asset managers as well as the IMF and Bank of England, the European Central Bank has warned that investors are being driven by the “fear of missing out”. Stretched valuations and the risk that disappointment on earnings, interest rates, or macro data could trigger a sharp pullback. AI may very well be a transformative technology justifying long-term gains, but markets often overshoot first.

World financial markets maintained their positive momentum through Q4. The MSCI World Index has large and mid-cap representation across 23 developed markets. It also has 72% exposure to the US markets and 27% to IT with a 24% exposure to the so called “Magnificent 7”. It grew by 4.1% both in USD terms and on a hedged GBP basis, as the dollar and pound maintained parity over the last three months and ended the year 12.6% higher in USD terms and 17.2% on a hedged GBP basis as the currency appreciated by 7.7%.

In the USA, the tech-focused NASDAQ delivered growth of 20.2% in 2024 while the broader based Dow Jones and S&P 500 grew by 13.4% and 16.7% respectively. Eurozone shares benefitted from investor rotation away from highly tech concentrated US indices. The broad-based Eurofirst 300 index gained 6.4% in Q4 and 17.1% over the year. The UK’s FTSE 100 rose by a further 6.2% in Q4 and ended the year 21.5% higher, representing its best year since 2009. This momentum has carried into 2026 as the index passed through the 10,000 mark. Performance was driven by internationally – focused businesses benefitting from a resilient global economy and a weak British pound. Investors were also attracted by a high dividend yield that provided a stable income return in a year marked by volatility and risk aversion.

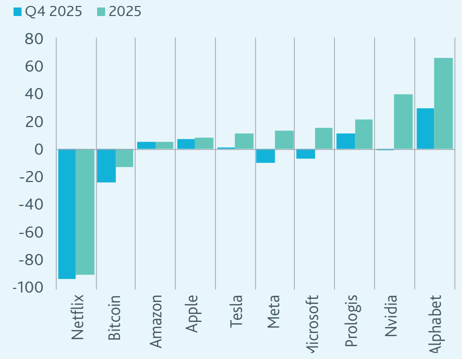
Markets remain reactive to the changeable actions of President Trump. The most recent escalation of the Greenland crisis wiped out

World stock markets in 2025 (%'age growth)



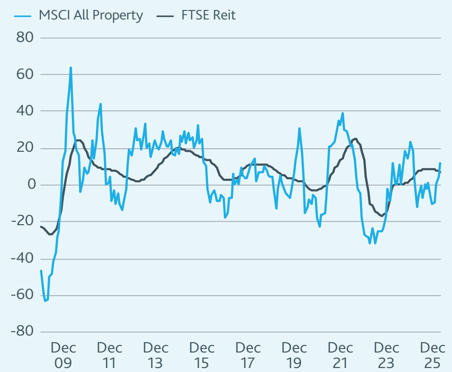
Source: Yahoo Finance, Jan 2026

Tech & other selected stocks in 2025 (%'age growth)



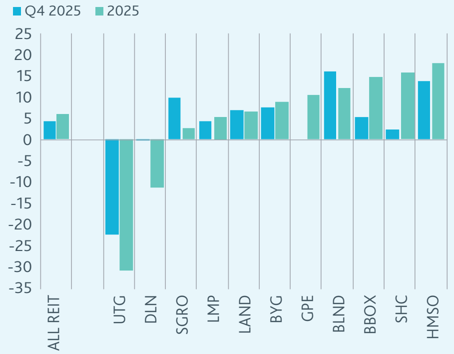
Source: Yahoo Finance, Jan 2026

Long-term 12m total returns



Source: Yahoo Finance & MSCI, Jan 2026

UK REIT price movement in 2025 (%'age growth)



Source: Yahoo Finance, Jan 2026

all market gains so far in January. But when Trump backed down on European tariffs he had earlier threatened, bond yields fell and stocks rose.

The performance of the FTSE REIT index improved in Q4, registering 4.4% growth, compared to a -6.7% fall in Q3. The index ended the year 6.0% higher. The average annualised rate of growth is -1.8% over three years and -4.8% over five years. However, the high dividend yield of 5.5% offered by the sector boosted 2025's total return to 11.9%.

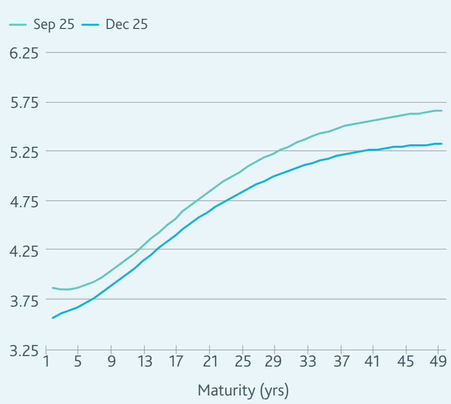
Retail specialists Hammerson and Shaftesbury Capital were the best performers of 2025 delivering growth of 18.0% and 15.5% respectively. Hammerson the owner of the ten largest retail and leisure city destinations across the UK, Ireland and France undertook a program of consolidation in 2025 by acquiring outstanding minority stakes in North London's Brent Cross Shopping Centre, Birmingham's Bullring & Grand Central and the Oracle in Reading. In its half year results, the company reported like-for-like gross rental income up 5.0%, total gross rental income up 11.0% after acquisitions and portfolio valuation up 11.0%. Hammerson's trailing dividend yield amounted to 4.9% in 2025 but its shares traded at a 30% discount to NAV.

Shaftesbury Capital has a £5.2 billion portfolio with 2.7 million sq ft of retail, food and beverage, office and residential assets across Covent Garden, Soho and Carnaby Street and Chinatown. In April the company completed the sale of a 25% interest in its £2.7 billion Covent Garden Estate to Norges Bank Investment Management, Norway's sovereign wealth fund. In its half year results it reported 193 leasing transactions, representing £19.2 million of contracted rent, 9.0% ahead of December 2024 ERV and 16.3% ahead of previous passing rents. The portfolio valuation increased by 3.1%. Shaftesbury's trailing dividend yield amounted to 2.3% in 2025 and its shares traded at a 22% discount to NAV.

Key developments across other companies in the sector over the course of 2025 have included Segro's plans for a 2.3GW+ land-enabled power bank and joint venture to develop its first fully fitted data centre; the acquisition by Tritax Big Box from Blackstone of a £1.04bn logistics portfolio; London Metric's takeover of Urban Logistics REIT; Blackstone's takeover of Warehouse REIT and in the alternative sector, Primary Healthcare Properties takeover of Assura Plc. Additionally, Land Securities announced plans to sell £2bn worth of office buildings and scale back office developments as it aims to reduce the allocation to offices from about 65% to a third by 2030, while boosting retail and housing to roughly a further third each.

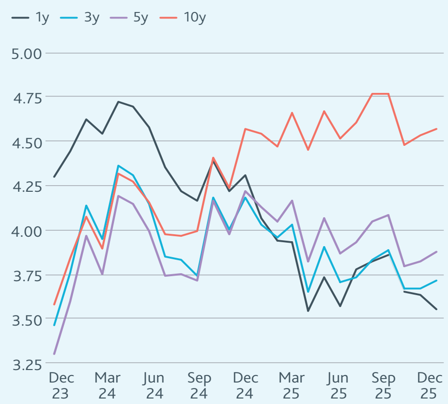
The yield on UK gilts fell across all maturities in Q4 by 30 bps for short-dated bonds and 20 bps or more for maturities of ten years and longer. Although, the gap between long-term and short-term yields remains

Gilt yield curve (%)



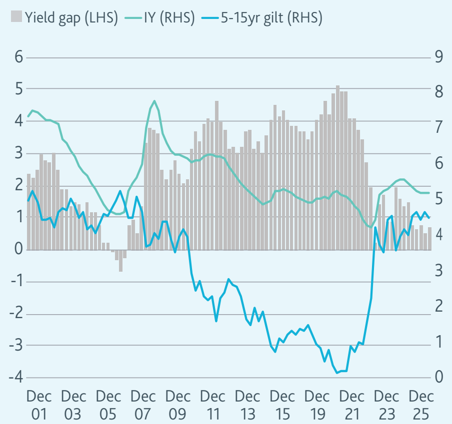
Source: Bank of England, Jan 2026

UK gilt yields (%)



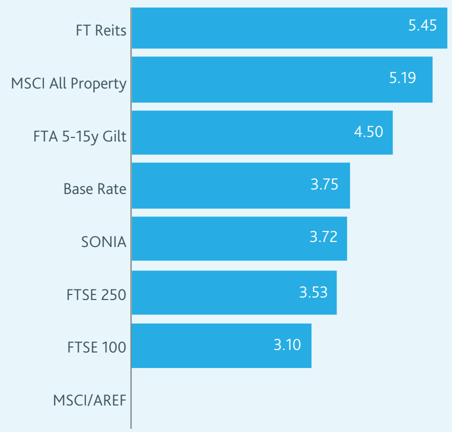
Source: Bank of England, Jan 2026

Property IY – Gilt yield gap (%)



Source: MSCI & Bank of England, Jan 2026

UK asset yields Q4 2025 (%)



Source: Yahoo Finance & MSCI, Jan 2026

steep by recent standards it was materially larger post-GFC. Nevertheless, for the reasons previously discussed in Q3 2025's "Commercial Property Examiner", the yield on 10-year gilts of 4.57% at the end of Q4 is the highest since November 2008 when it reached 4.70% as the UK Government was forced to support the banking system by re-structuring Northern Rock, HBOS, Lloyds and RBS / Nat West.

The yield on the 5-15 year gilt index hardened by 15 bps in the fourth quarter to 4.50%. This is reflected in the total return performance on the FTSE Actuaries 5-15 year gilt index in Q4 of 2.76%. Over the last 12 months, the gilt index has provided a total return of 5.87% as yields have decreased by 7 bps since December 2024. Changes in the risk-free rate are a key metric referenced in the valuation of commercial real estate.

After December's meeting of the MPC, the UK's base rate has been reduced by 25bps to 3.75%, and minutes from that meeting indicate that Bank Rate is likely to continue on a gradual downward path. However, the UK's long-term borrowing costs remain the highest across the G7.

5. Commercial property market performance

- **All Property total returns decreased to 7.1% year-on-year from 8.6% in September. Although this was only a 10 bp improvement on 2024's 7.0% it represented the best year-end result since December 2021.**
- **The Retail sector achieved the strongest total return performance at 8.8%, bolstered by Shopping Centres' impressive 11.9% performance. Offices were the weakest sector but their performance was lifted by the West End and Midtown office segment which delivered a total return of 8.2%.**

The MSCI Monthly Index is predominantly made up of core open ended non-listed real estate vehicles with some closed-ended and listed vehicles. As originally designed in December 1986, the constituent sectors of the index were 45% Retail, 42% Offices and 12% Industrial. Today Industrials dominate, representing 46% of the index, Retail 21%, and Offices 18%. Other property including Residential, Hotels, Healthcare and Leisure is now 14%.

As noted above, risk free rates hardened by 15 bps in Q4, and the All Property initial yield itself softened very slightly by just 1 bp. Consequently, the property initial / gilt yield gap has increased by 16 bps to 0.69% easing concerns of adjustments to pricing levels. However, market rental value growth across most segments of the market remains resilient, which may add support to the current risk premium.

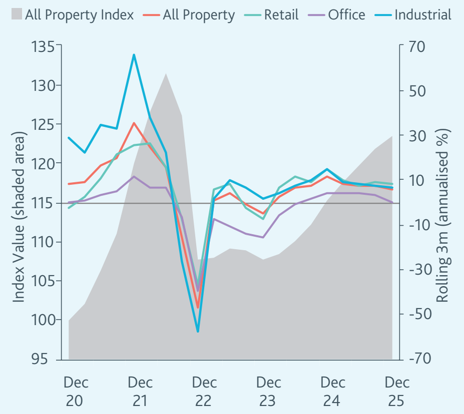
In Q4, the UK commercial real estate market slowed further as rolling 3-month total returns remained on a downward trajectory. All Property total returns, as recorded by the MSCI Monthly Index, decreased by 36 bps to 1.42% from 1.77% in Q3. Capital growth was limited to less than 4 bps after a rise of 0.4% (40 bps) three months earlier. Property equivalent yields softened by 3 bps but had no material contribution to changes in valuations. All Property market rental value growth in Q4 remained 0.9% as in Q3 but growth of 0.17% in December was the weakest monthly outcome of the year. Fourth quarter income returns remained at 1.4%.

The biggest surprise over the course of the fourth quarter in rental value growth came from the retail sector as MRV growth fell to near zero from 0.9% in Q3 after 11 consecutive quarters of growth. This appears to have been driven by a -5% quarterly decrease in Rest of UK standard retail units and more particularly a sharp -12.5% decline in Birmingham retail MRV's. Rents in the other two sectors exhibited more strength. Office rental growth increased to 1.3% from 0.6% and Industrial rental value growth increased to 1.6% from 1.0% a quarter earlier.

In the last three months, retail equivalent yields hardened by 15 bps and the office sector yields ended the quarter 19 bps lower. Equivalent yields in the dominant industrial sector rose 6 bps.

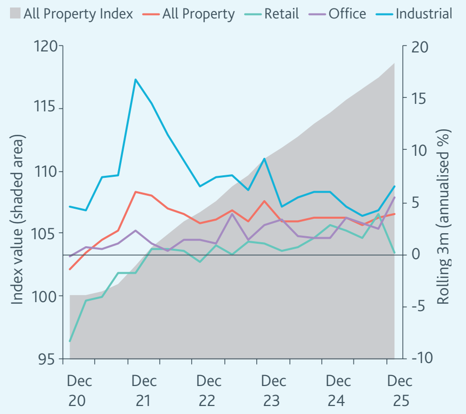
In the 12 months to the end of December, index performance has largely been driven by income returns with a modest contribution

Total returns (%) by sector



Source: MSCI, Jan 2026

MRV growth (%) by sector



Source: MSCI, Jan 2026

from capital growth. The limited capital growth was driven by MRV growth rather than yield compression.

All Property total returns decreased to 7.1% from 8.6% in the year to September. This represented the best year-end result since December 2021 when the performance reached 19.9% during post-COVID recovery. The strongest total return performance of 8.8% came from the Retail sector supported by the 11.9% performance of Shopping Centres. Offices were the weakest sector, but their performance was boosted by the West End and Midtown office segment which delivered total returns of 8.2%. Industrials delivered total returns of 8.0% as the Rest of UK segment outperformed London and the South East for the second consecutive year.

All Property capital growth decreased from 2.6% y-on-y in September to 1.3% y-on-y in December as office yields weakened further. All Property MRV growth was unchanged from Q3 at 3.4% y-on-y and the income return decreased very slightly from 5.8% in the year to September to 5.7% y-o-y in December.

At the segment level, a shift in momentum may be appearing. South East and Rest of UK Industrial MRV growth has decreased to 4.9% and 4.3% in 2025 from 5.7% and 5.1% in 2024 respectively. Meanwhile Retail Warehouse and Midtown & West End Office MRV growth has increased to 3.1% and 8.4% from 2.1% and 5.4%.

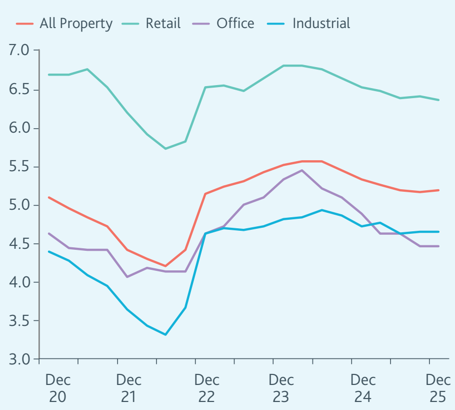
Property equivalent yields rose sharply in 2022 and 2023 as interest rates and bond yields spiked but yields have stabilised at this higher level in 2024 and 2025 albeit with some minor volatility. All Property equivalent yields have hardened by 10 bps in the 12 months to December but have made a negligible contribution to any change in valuations over the course of the last year.

In the last 12 months, Retail equivalent yields have hardened by 23 bps. Industrial equivalent yields increased by 5 bps y-o-y. Office sector yields re-rated by 20 bps in 2025 and y-o-y MRV growth increased to 3.5% in December from 2.6% in September. However, the rate of 12-month decline in capital values increased to -2.3% in December from -1.4% in September. This counter intuitive outcome is explained by higher office sector vacancy rates of more than 20% and the shortest weighted lease terms of just 5.2 years reducing net operating income by 7.3% y-on-y across the sector.

The recovery stage in the current cycle continues to disappoint compared to the vigorous bounce in capital growth enjoyed after previous downturns in both 1991-92 and 2008-09. Despite six consecutive reductions in Bank Rate from 5.25% to 3.75%, the market has not experienced a "V" shaped recovery reminiscent of the episodes in 1993-94 or 2009-10. Market uncertainties caused by tepid economic growth, persistent inflation and doubts over the future path of monetary policy continue to prevail.

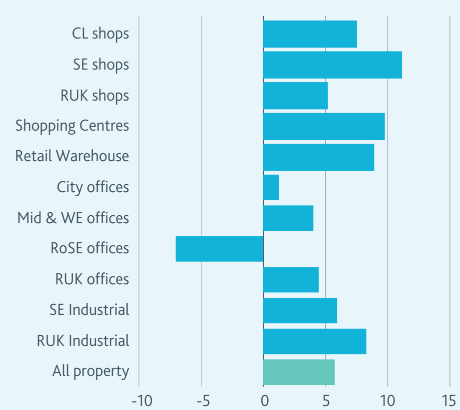
The tables included (page 12) contain further performance data for UK commercial real estate in Q4 2025.

Initial yield (%) by sector



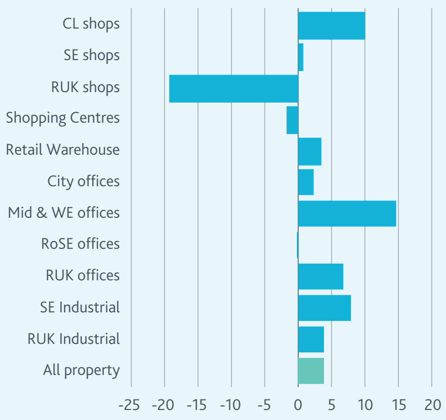
Source: MSCI, Jan 2026

Total returns (%) by segment – Q4 2025 annualised



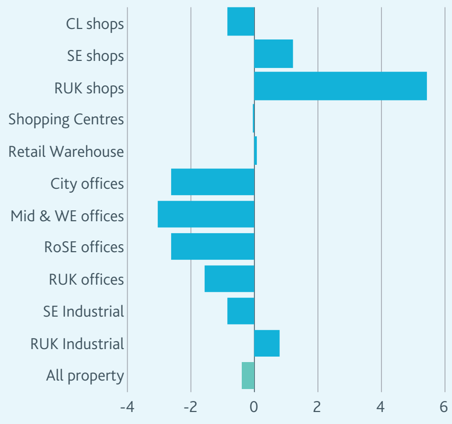
Source: MSCI, Jan 2026

MRV growth (%) by segment Q4 2025 annualised



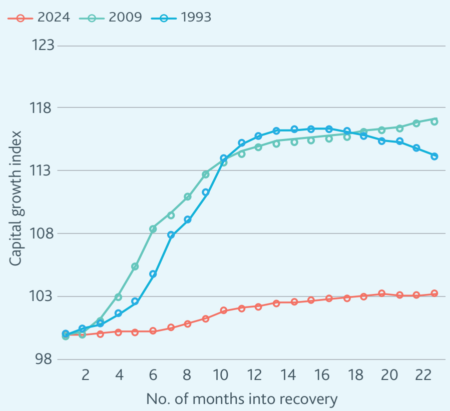
Source: MSCI, Jan 2026

Yield impact (%) – Q4 2025



Source: MSCI, Jan 2026

The pace of recovery from market downturn by quarter



Source: MSCI, Jan 2026

Total returns (%)

	Dec	3m	6m	12m
All Property	0.6	1.4	3.2	7.1
Retail	0.8	2.1	4.4	8.8
Office	0.4	0.1	0.9	3.0
Industrial	0.5	1.7	3.6	8.0
Annualised				
All Property	7.0	5.8	6.5	7.1
Retail	9.9	8.5	8.9	8.8
Office	5.0	0.5	1.8	3.0
Industrial	6.5	6.8	7.2	8.0

Source: MSCI, Jan 2026

Capital growth (%)

	Dec	3m	6m	12m
All Property	0.1	0.0	0.4	1.3
Retail	0.2	0.4	0.9	1.7
Office	0.0	-1.2	-1.7	-2.3
Industrial	0.1	0.5	1.1	3.0
Annualised				
All Property	1.4	0.2	0.8	1.3
Retail	2.9	1.5	1.9	1.7
Office	-0.3	-4.6	-3.4	-2.3
Industrial	1.7	1.8	2.3	3.0

Source: MSCI, Jan 2026

Income return (%)

	Dec	3m	6m	12m
All Property	0.5	1.4	2.8	5.7
Retail	0.5	1.7	3.4	7.0
Office	0.4	1.3	2.7	5.4
Industrial	0.4	1.2	2.4	4.9
Annualised				
All Property	5.5	5.6	5.7	5.7
Retail	6.8	6.9	7.0	7.0
Office	5.3	5.3	5.4	5.4
Industrial	4.7	4.9	4.8	4.9

Source: MSCI, Jan 2026

MRV growth (%)

	Dec	3m	6m	12m
All Property	0.2	0.9	1.8	3.4
Retail	-0.4	0.0	0.9	1.9
Office	0.4	1.3	1.9	3.5
Industrial	0.4	1.6	2.6	4.7
Annualised				
All Property	2.0	3.8	3.7	3.4
Retail	-4.2	0.1	1.9	1.9
Office	4.3	5.4	3.9	3.5
Industrial	4.5	6.4	5.3	4.7

Source: MSCI, Jan 2026

Net initial yield (%)

	Dec	3m	6m	12m
All Property	5.2	5.2	5.2	5.3
Retail	6.4	6.4	6.4	6.5
Office	4.5	4.5	4.6	4.9
Industrial	4.7	4.6	4.6	4.7

Source: MSCI, Jan 2026

6. Investment in property

- **All Property investment volumes remain muted by historical measures of activity but investment volumes in Q4 have benefitted from a customary year-end bounce and increased by 30% quarter on quarter.**
- **Preliminary estimates for Q4 indicate that Central London office transaction volumes almost doubled quarter on quarter. Investment volumes so far recorded in 2025 are better than both 2024 and 2023.**

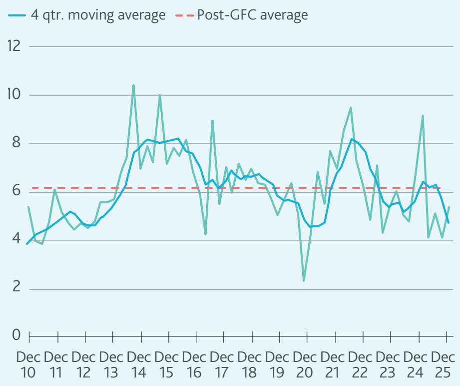
A rise in the overall value of transactions can be driven by a small group of deals struck at higher prices. The best gauge of market liquidity is the number of transactions which gives investors greater price transparency and proof of a deep and liquid market into which they can sell on the assets if needed. Therefore, we focus in this section on investment volumes represented by the current value of investment transactions adjusted for capital growth.

All Property investment volumes remain on a downward trend limiting any capital value uplift from yield compression. In the first half of 2025 investment volumes were lower than both 2023 and 2024. Investment volumes decreased by -20% in the third quarter and were a disappointing -33% below their long run post GFC average.

Preliminary estimates suggest that investment volumes in Q4 have benefitted from a customary year-end bounce and increased by 30% quarter on quarter but were still -41% below the level achieved in Q4 2024 and -13% below the long run average. As usual the latest numbers for Q4 are likely to be revised in the coming months. However, cumulative four quarter UK investment volumes so far recorded in 2025 are currently the lowest since September 2020 in the aftermath of the first pandemic lockdown.

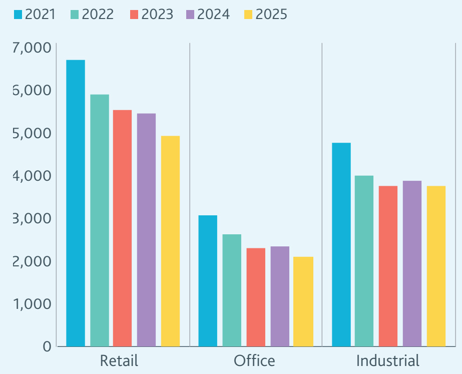
Retail made up 51% of investment volumes in Q3; offices represented a further 37% and industrials made up the remaining 12%. In the 12 months ending September 2025, the retail sector accounted for 47% of transactions. Offices represented 19% of transaction numbers and industrials a further 34%. The volume of Retail Park investment transactions has decreased since it peaked in Q4 2024. Similarly, the volume of Shopping Centre investment transactions fell away in early 2025 but has since recovered as investors have been boldened by the current total return outperformance of this segment. The declining number of transactions suggests that investors are

All property investment volumes (£bn)



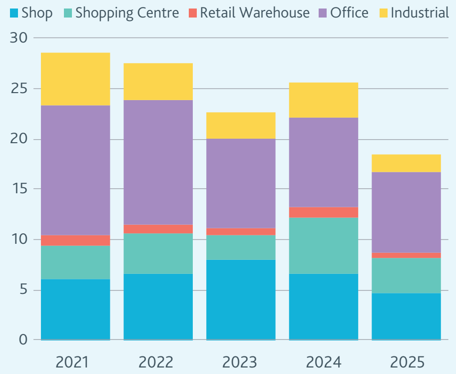
Source: CoStar, MSCI & APR, Jan 2026

UK investment transactions by year



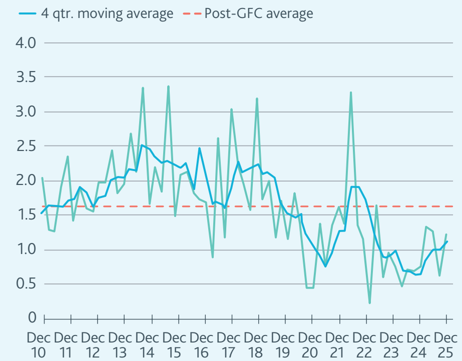
Source: CoStar, MSCI & APR, Jan 2026

UK investment volumes by year (£bn)



Source: CoStar, MSCI & APR, Jan 2026

Central London office investment volumes (£bn)



Source: CoStar, MSCI & APR, Jan 2026

making highly selective stock selection decisions rather than deploying capital through broader brush asset allocation approach.

Investment volumes in the UK's key Central London office market have been slowly recovering since March 2024 albeit in a volatile manner. Having improved in the first half of 2025, they decreased by -51% in the third quarter and were -61% below their long run average.

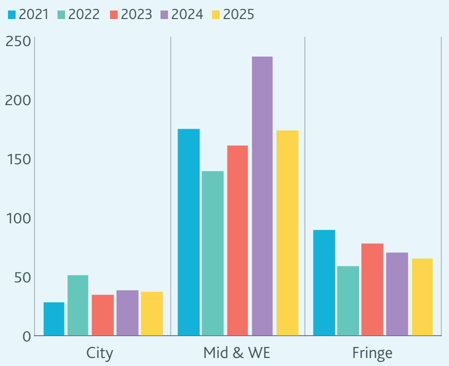
Preliminary estimates for Q4 indicate that there has been a dramatic improvement in investment market liquidity as Central London office transaction volumes almost doubled quarter on quarter. As usual the latest numbers for Q4 are likely to be revised in the coming months. Nevertheless, cumulative four quarter investment volumes so far recorded in 2025 are better than both 2024 and 2023. In 2025 Central London investment transactions numbered 272, down from 340 in 2024 but the average transaction value rose sharply to £16.4 million form £7.8 million in 2024 suggesting the market witnessed a smaller number transaction but with a higher value.

Throughout 2025 City investment volumes have surpassed those across the West End and Midtown and made up 63% of Central London office investment transactions in Q3; Midtown and West End offices represented 21% and Fringe offices made up the remaining 20%.

Outstanding loans from UK banks and financial institutions to real estate businesses grew 11.6% in the 12 months to November, to £142bn, according to Bank of England data. That was the fastest year-on-year growth rate since at least 2010. Earlier in the year London's Bayes Business School reported that banks have made significant progress in reducing their defaulted loan books, through refinancing and increased syndication. This has renewed their appetite for new lending, with loans now offered at highly competitive rates. Loan pricing has become increasingly competitive. with loan margins narrowing. Bayes confirmed that 74% of new lending has been deployed to refinance expiring debt. Consequently, transaction volumes remain low due to pricing uncertainty and a reluctance from investors to commit equity in the face of the current macro-economic uncertainties.

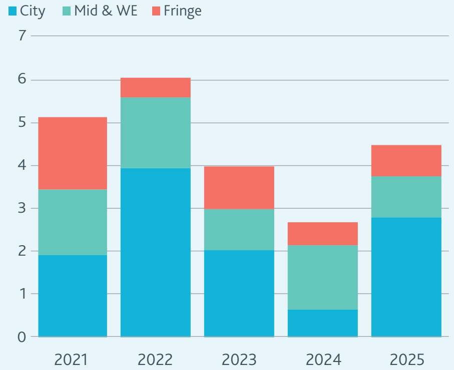
Better prospects for economic growth together with an improving inflation outlook may act as a catalyst for renewed inward investment into UK commercial real estate. INREV's 2026 Investment Intentions Survey indicates that the UK's residential and industrial / logistics sectors remain the preferred destinations for investment capital within Europe. In addition 93% of non-European real estate investors will be targeting the UK this year.

Central London office transactions by year



Source: CoStar, MSCI & APR, Jan 2026

Cumulative Central London office investment volumes by quarter (£bn)



Source: CoStar, MSCI & APR, Jan 2026

7. Outlook & house view

- **November's IPF consensus outlook shows that All Property commercial market performance is expected to improve from 7.1% to 8.3% in 2026.**
- **Market rental value growth is expected to slow in 2026 but, supported by some key segments, will remain above the 2% post GFC annualised average. Our house view is that All Property total returns will reach 9.0% in 2026, with a three-year annualised forecast of 8% through to 2028.**

Forecasters' confidence in a recovery of the UK's commercial property market weakened further as the end of the year approached. Consequently, November's Investment Property Forum (IPF) consensus forecasts for total returns in 2025 decreased to 6.9% from 7.6% in August. This final adjustment proved to more accurately reflect the eventual outcome for 2025 of 7.1%. At the start of the year the consensus All Property total return outlook was a more optimistic 9.0%.

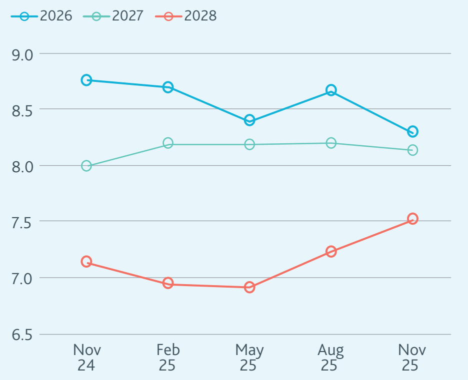
November's IPF consensus outlook for 2026 also weakened from 8.7% to 8.3%. However, 2026 is expected to mark the high point of the recovery and expectations slip back thereafter. The IPF's average annualised total return forecast over the next three years to the end of 2028 remains at 8.0% as it was in August.

Total return expectations for 2026 decreased across all segments in November's survey except Retail Warehouse and West End Offices. Expectations for 2026 are highest for Shopping Centres, Retail Warehouses and West End Offices although the performance of Shopping Centres is expected to decline from 11.9% in 2025 to 8.7%. The outlook continues to be weakest for Rest of UK offices.

The range of forecasts for 2026 narrowed in November, with the highest prediction at 9.8% and the lowest at 7.3%, a range of 2.5%, compared to 3.3% in August, suggesting the consensus view is narrowing in the face of the uncertain economic headwinds. The range of forecasts for 2027 has increased to 4.1% for 2027, ranging from 5.8% to 9.9% reflecting that uncertainty increases the further out the forecast horizon.

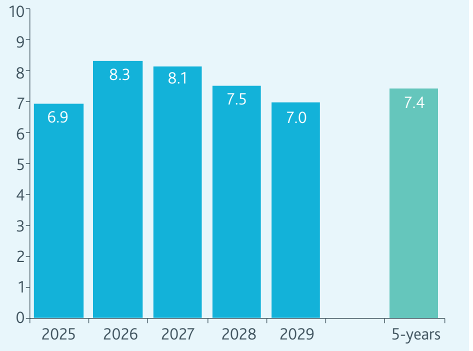
The Q4 2025 RICS UK Commercial Property Monitor results continue to reflect subdued market conditions, although there are some tentative signs of a more positive shift emerging. There has been an increase in the number of respondents that believe conditions are consistent with the early stages of an upturn across the market. Occupier sentiment has improved slightly although tenant demand

IPF Consensus forecast evolution (%)



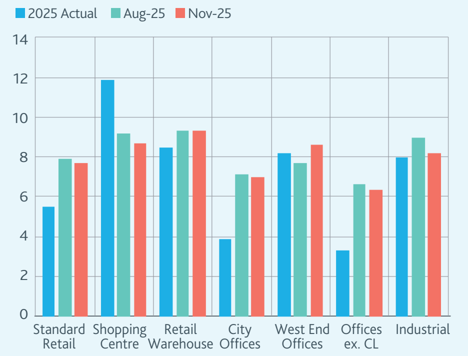
Source: IPF, Nov 2025

IPF All Property consensus forecasts y-by-y (%)



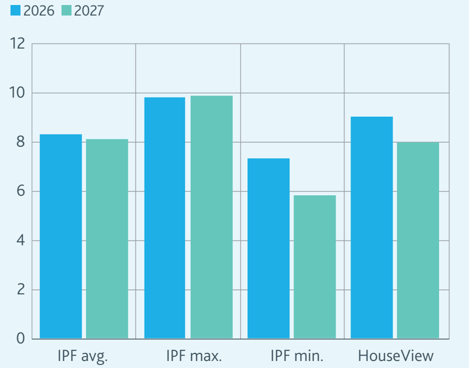
Source: IPF, Nov 2025

IPF 2026 total return forecasts by sector Nov 25 v Aug 25 (%)



Source: IPF, Nov 2025

UK commercial total return forecast range (%)



Source: IPF, APR & Cluttons, Nov 2025 & Jan 2026 continues to fall particularly in the retail sector. Rental projections for prime office and industrial sectors have improved, while prime retail rents remain flat and secondary office and retail rents are expected to decline. Investment market sentiment improved slightly in Q4. Capital value expectations were upgraded for prime industrial and office properties. However, the retail sector continues to reflect a divergence between the outlook for prime assets which are expected to benefit from capital growth and secondary assets characterised by negative expectations.

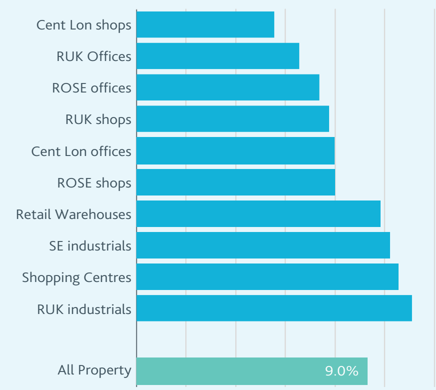
The central forecast from the House View model is revised on a quarterly basis to reflect the changing macro-economic outlook and the current performance of commercial real estate. We started last year believing that the momentum behind UK commercial real estate's recovery would continue and that All Property total returns of 7.0% in 2024 would grow to 10% in 2025. We soon realised that weak economic growth combined with a troublesome inflationary outlook and increasing risk free rates had created strong headwinds that would slow the recovery in commercial property values and reduced our guidance to 8.0% in March and 7.0% in June, close to the eventual outturn of 7.1%.

A fifth consecutive reduction in UK base rate to 3.75% was only announced in December and it may be too soon to detect any improved appetite from the UK's commercial real estate investors. As noted above, capital growth in 2025 remains limited, income is the main driver of performance and transaction numbers remain underwhelming. However, we are more optimistic this quarter that inflation will continue on a downward track allowing the MPC to further reduce base rate to boost the sub-par performance of the economy.

Macro-economic fundamentals suggest that market rental value growth may slow further from the current 3.4% y-on-y rate. But growth will nevertheless remain relatively strong in selected segments of the market. The outlook for yields is also improving. It is to be hoped that recent tax rises have re-assured the bond market. National Statistics has just reported that the UK borrowed less than expected in December. Public sector net borrowing totalled £11.6bn, below the £13bn forecast by economists polled by Reuters and 38% lower than in the same month a year earlier. A reduction in the risk free rate used to benchmark the capitalisation rate of property income could be one outcome. The favourable view of the UK from overseas investors highlighted by INREV's 2026 Investment Intentions Survey may also provide a welcome fillip to the investment market this year.

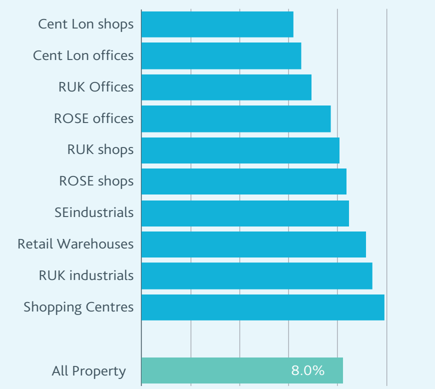
Accordingly, we now expect All Property total returns of 9.0% in 2026 and 8.0% annualised over the three years ending 2028. However, this forecast must come with a warning regarding the threats to financial markets from the prevailing geo-political instability.

Cluttons house view – 2025 relative total returns (%)



Source: IPF, APR & Cluttons, Jan 2026

Cluttons house view - 2026-2028 relative total returns (%)



Source: IPF, APR & Cluttons, Jan 2026

Uniform Business Rate update from

Commercial properties in England, Wales, and Scotland have been revalued. The Valuation Office Agency in England estimated the assessment based on the rent that would have been paid on 1st April 2024.

There have been some substantial increases in assessment, but other sectors have benefitted from a more conservative approach. In some cases, the Valuation Office may lack relevant evidence to support larger increases or decreases.

Large high bay distribution warehouses were expected to see large increases but seem to have been spared from this outcome. In some cases, assessments are at 2/3 of their potential value.

Conversely, we expected substantial decreases in assessments for secondary shopping centres, but this hasn't happened. Some centre assessments have remained the same or even increased despite evidence suggesting otherwise. The Valuation Office's cautious approach to increasing assessments may be due to concerns about challenges and reductions. They also seem to have avoided substantially reducing assessments, especially in struggling sectors like secondary retail centres.

We also have concerns regarding the multipliers announced in the Chancellor's budget speech. Though diminished, intricate reliefs still cause complications. In Retail, Hospitality & Leisure, a blanket 40% relief was replaced by three multipliers based on property rateable value. Strict rules determine ratepayer benefits, making liability calculations unique. Billing Authorities may struggle with accurate rate demands, leading to challenges.

Compounding matters, the Government introduced a transitional relief scheme limiting yearly liability increases based on rateable value to a preset percentage. While welcome, it represents a complication and any relief will be lost if the ratepayer changes. Moreover, if the property does not benefit from transitional relief there is a surcharge applicable to the multiplier from those who are benefiting from the relief.

The system may be falling into disrepute and is certainly becoming increasingly complex to administer. The public house sector has been particularly affected, with substantial increases in assessment that haven't been offset by a multiplier that provides the same level of relief as under the current scheme. The problem is that properties in this sector were last valued for the 2023 Revaluation with reference to trade as of 1st April 2021, at the height of the pandemic. The latest valuation date is 1st April 2024, by which time trade had recovered significantly. Consequently, properties in this sector have seen substantial increases in liability, leading to outcry from publicans and chain operators. The Government is looking at this and may reduce the multiplier for public houses to offset the substantial increases. Details are likely to be revealed to allow Billing Authorities to amend their records.

Upward only rent reviews update

The Government's proposed ban on upward-only rent reviews, part of the English Devolution and Community Empowerment Bill, has reached the House of Lords committee stage.

During the Public Bill Committee stage, some MPs raised concerns about the Government's proposal, warning it could deter commercial investment and create unintended consequences in sectors such as logistics. Mike Reader MP highlighted that Ireland introduced protections alongside bans, while David Simmonds MP argued the change could undermine contractual freedom and lead to complex workaround leasing structures. The Government pushed back, insisting the ban is overdue, internationally standard, and essential for fairer, more flexible leasing that supports small businesses and high streets, stressing that landlords still have viable alternative rent setting tools and that the existing system is illogical and harmful.

Intended to support small businesses and revive high streets, the ban has sparked wider debate and criticism due to limited consultation and potential impacts on investors. Upward-only rent reviews have long underpinned confidence in commercial leases, and their removal could have significant implications for landlords and their portfolios.

The ban will apply to all review mechanisms, and capture attempts to circumvent through methods such as side letters but will not be retrospective. It will only affect tenancies entered after the Bill's implementation. Stepped or fixed rental uplifts will remain permitted. Recent amendments to the draft Bill address inconsistencies between leases and subleases and clarify that tenancies where the tenant is not in physical occupation will also be captured.

Whilst revitalising town centres is a worthy aim, blanket legislation risks unintended consequences in a complex market. Former Treasury analyst Martin Beck estimates the removal of upward-only rent reviews could reduce commercial property values by 15%, equating to an £11bn loss across the sector. Beck also warns of reduced investor appetite for large-scale developments, such as data centres, where guaranteed returns are critical.

Potential knock-on effects are not just limited to the landlord community. A two-tier market may emerge, disadvantaging incumbent occupiers compared to new tenants until renewal. Although average lease lengths have fallen below seven years across all sectors segments of the market incurring significant fit-out costs often favour longer terms. These occupiers could remain outside the new regime for years, unable to align with evolving norms.

How might the market respond:

- Shorter lease terms and increased prevalence of contracted-out leases.
- Landlords having to balance guaranteed returns against maximising rental value for new developments, with potentially reduced investment and lending.
- Greater reliance on alternatives to market reviews, such as stepped rents, fixed increases, or index-linked mechanisms (e.g., CPI + 1%).

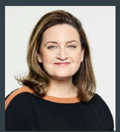
Supporting commercial occupiers is welcome, but investor and landlord needs must also be considered. More targeted relief would likely be a better solution than a one-size-fits-all approach, minimising uncertainty and disruption in the market at a time when confidence is paramount.

CLUTTONS
INVESTMENT MANAGEMENT

cluttonsim.com

For further details contact:

Jamie McCombe
Head of investment management
+44 (0)7958 207 027
jamie.mccombe@cluttonsim.com



Gráinne Gilmore
Director of research and insight
+44 (0) 7967 271 321
grainne.gilmore@cluttons.com

Researched on behalf of Cluttons Investment Management by Alexander Property Research.

RICS