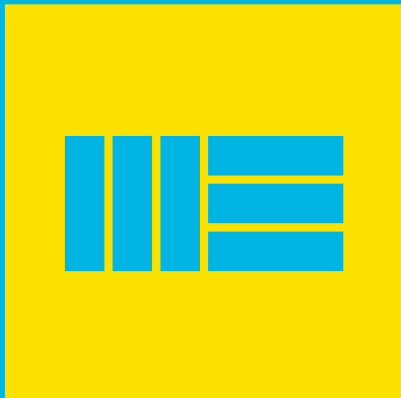


MARKET PULSE

UK PROPERTY INSIGHTS

Q2/Q3 2025



THIS QUARTER'S BRIEFING FOCUSSES ON THE RESIDENTIAL SECTOR: ONE OF HUGE IMPORTANCE TO THE UK BOTH SOCIALLY AND ECONOMICALLY, AND ONE WHICH IS CURRENTLY STRUGGLING, PARTICULARLY ON THE DEVELOPMENT SIDE.

What exactly is going on? Why is building homes proving so difficult, given the government's promise to deliver 1.5m new homes over its parliamentary term?

But as usual, before going into those details, there is a quick overview of the economy, the wider property landscape and the recent spending review – as well as some predictions as to what the implications of the Trump presidency might be for the property market.

QUICK SUMMARY

- The economy grew by an unexpectedly high figure of 0.7% in Q1 – but saw a 0.3% fall in April.
- Stockpiling caused by Donald Trump's tariff may have boosted the former figure, explaining the reversal the following month.
- Inflation came in higher than expected in April at 3.5%, but core inflation fell back, and the labour market is becoming less tight.
- Gilt yields have fallen by 20-25bps over the past month, which should provide some support for property investment and development.

THE ECONOMY

First off, the good news: the economy saw surprisingly strong growth over the first quarter of the year. GDP growth came in at 0.7% for Q1 – and output is now 1.3% higher than a year ago. The outturn was driven by expansion in both the services sector (0.7%) and production (1.1%), although construction was flat (perhaps unsurprising given the slowdown detailed in the second half of this briefing). This unexpected level of growth has led to Oxford Economics bumping up its forecast for the year from 1.0% to 1.2%, although 2026 and 2027 forecasts remain unchanged at 0.9% and 1.3%.

However, when announced, there were some concerns that these figures might be overstating the underlying strength of the economy. Business Investment picked up (following a fall in Q4 2024), and a big increase in exports might be related to companies stockpiling before Donald Trump's tariffs came into force. The weak reading for April (-0.3%) has been read by some as 'payback' for the factors behind the strong Q1 figure. The Purchasing Managers' Indices (PMIs) do now seem to point towards contraction, but this may reflect sentiment rather than actual conditions; their correlation with growth appears to have weakened recently.

Now, the more worrying news: inflation came in higher than expected in April at 3.5%, up from 2.6% in March. This was driven mainly by higher energy prices, as well as an increase in Vehicle Excise Duty. The unusually late Easter may have had an impact, pushing up demand for flights and thus airfares too. Together with wages and salaries still rising at above 5%, this probably explains why the Bank of England held rates at 4.25% this month. May's figure – just released at the time of writing – saw CPI growth fall back to 3.4%, however.

But with measures of core inflation falling back, and the data from the jobs market showing vacancies falling and unemployment slightly rising, the sentiment at the Monetary Policy Committee has become more doveish. So June's hold is a pause not a change of direction; all eyes will now be on August.

The 10-year gilt yield – all important for the property investment market – has fallen back quite strongly over the past month, by about 20-25bps, reflecting shifts in inflation and base rates. How it performs over the rest of the year will depend on inflation and base rates on one hand, but also on the UK Government's increasingly fragile fiscal position. Governments globally are borrowing more money – partly to fund increasing defence commitments – and this is increasing the supply of bonds generally, pushing prices down and yields up. This would obviously put upward pressure on debt rates and property yields, but this should be at least balanced out by inflation remaining low – if that does indeed turn out to be the case.

The big worry, of course, is the conflict between Iran and Israel and in particular what happens after the US's bombing raid, which had just occurred at the time of writing. Iran is threatening to close the straits of Hormuz, through which around a fifth of the world's oil is transported. As of Monday 23rd June, oil prices had spiked by 5.7%, reaching a five-month high, before losing some of those gains. Clearly, if oil prices increase, it will put some renewed upward pressure on inflation – and would have some wider economic impacts too.

TRUMP

The new world of unpredictable tariffs feels so familiar now, it is almost shocking to remember that “Liberation Day” was just 11 weeks ago. Even though the most excessively high rates have been trimmed back, they remain at levels that would be unimaginable a few years ago. The fickle and impulsive nature of decision making is also, to put it mildly, problematic.

The overall impact of the tariffs will be to reduce trade, particularly in manufactured goods. This will have a disproportionate impact on parts of the ‘pure’ industrial sector (not logistics so much), where tenants have already been struggling with higher rents, higher energy costs and a global economic slowdown. But overall, manufacturing is not as dominant a part of the UK economy as in some other countries, and services *should* be much less impacted by tariffs. In particular, the lion’s share of UK trade with the US is in services. This means that while the UK will be affected – both directly and indirectly through the global economic impacts – it should be less affected than some other developed countries.

According to modellers – and economic theory – the tariffs should be inflationary in the US and mildly disinflationary elsewhere, not least through the weakening dollar. This obviously supports the case, albeit perhaps marginally, for faster cuts in base rates. A final impact – and perhaps most important for our sector – is that the wider actions of the Trump administration have somewhat undermined the case for the US as an investment destination. The UK, and Europe generally, now look more attractive to investors in all sorts of asset classes, property included, but the shift will be slow.

Meanwhile, global business sentiment has improved somewhat on reduced tariffs and the *slightly* more cordial atmosphere between the US and China.

INVESTMENT

A WEAK QUARTER FOR UK INVESTMENT

Acquisitions of UK property amounted to just £7.8bn in Q1 2025, down from £14.7bn. This is the weakest quarter since Q3 2023 (£7.3bn), even though the general trend is still upwards.

All sectors saw declines, although it was less marked in the residential sector than elsewhere. Indeed, for the year to the end of March, residential was actually slightly above (11.9%) the 10-year annual average, while other sectors were below – notably offices (-49.3%). Even on quarterly basis (see below), the residential sector looks comparatively strong.

KEY POINTS

- The tariffs should be disinflationary outside the US
- The UK will be less hit than most owing to a smaller manufacturing sector
- The UK and Europe now look like more attractive investment destinations
- The market reaction to the tariffs has largely unwound, partly because of the lowering of the tariffs on China

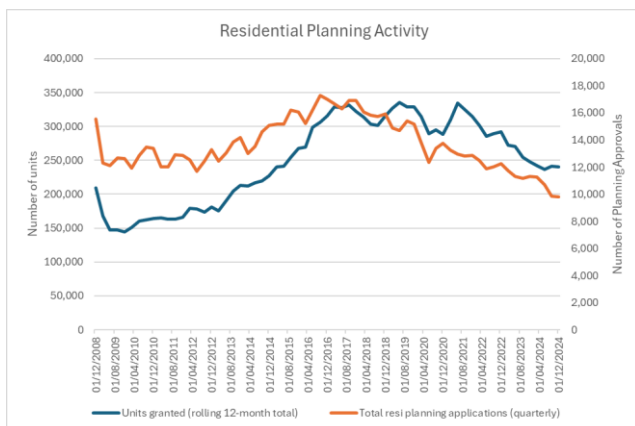
	C/TO PREV QTR	C/TO SAME QTR IN 2024
All Sectors	-46.8%	-25.2%
Office	-38.4%	-1.9%
Industrial	-57.6%	-19.9%
Retail	-59.2%	-34.9%
Residential	-17.0%	+7.3%
HOTEL	-72.1%	-80.6%

However, residential’s strength does not extend to overall returns, at least when measured by MSCI; it only managed 4.4% returns over the year to the end of March, a result of low yields and little space for more compression. Retail has overtaken industrial in total returns (9.6% vs 9.2%) but the drivers are totally different – income on one hand, capital growth on the other. Offices, meanwhile, languishes in last place with 1.5%.

RESIDENTIAL

The strength in residential *investment* is sadly not matched by residential development. The total number of starts in the final quarter of 2024 was 25,440, one of the lowest figures on record outside the pandemic and the Global Financial Crisis. Completions have not yet dipped dramatically, but this looks likely to change over the next year or so.

What is more worrying is the trend. Over 2024, work started on just over 100,000 homes – while the 10-year average is 150,000. Meanwhile, the number of homes with outstanding planning permission has been on a downward trend too and is currently at the lowest level since the financial crisis.



KEY POINTS

- Residential development and planning activity is at – or close to – an all-time low
- It is particularly marked in London where there were only 1,219 starts the first quarter compared to a government target of 22,000
- Building Safety Act issues and Gateway approval delays are causing problems for flat construction, which dominates London delivery
- The rise of Single-Family Housing (as a build-to-rent investment) is favouring more suburban or greenfield sites out of London
- Despite falling mortgage approvals, house price growth is still positive, and relatively strong in the North and Midlands
- Rental growth continues to fall back from the heights of a few years ago, notably in London.
- A connected solution could be the best method to navigate these complexities and unlock new opportunities.

There were approvals given for just 240,785 homes in 2024; that is admittedly higher than around the time of the GFC but is lower than the almost 300,000 that has been typical over the past ten years. As the chart below shows, it has also been on a downward trend – albeit one that stabilised in the second half of 2024. Total residential planning applications have also been falling, to stand at (pretty much) the lowest level on record.

The fall in actual construction activity is not evenly distributed around the country. Over 2024, starts in regions like the North West, the West Midlands and Yorkshire were 60-70% below the 10-year average, while the South performed better at 70%-80%. London, on the other hand, saw starts at just 38% of the long-term average.

REGION	2024	10-YEAR AVERAGE	2024 AS % OF 10-YEAR AVERAGE
North East	6,960	8,087	86%
East of England	16,650	19,971	83%
South East	22,010	27,779	79%
East Midlands	11,940	15,822	75%
South West	12,700	17,861	71%
Yorkshire and the Humber	8,550	12,395	69%
North West	11,820	18,060	65%
West Midlands	9,470	14,780	64%
London	6,330	16,828	38%

According to more timely data from the London resi data specialist Molior, there were just 1,210 starts across the whole of London in Q1 - compared to a quarterly government target of 22,000. While completions have not yet fallen back (owing to the historic pipeline), it is now expected that 2026/27 will see just 7,100 completions.

So, what is causing this slowdown? The main problems are viability: with construction and debt costs much higher, the appraisals projects were originally assessed with no longer make sense without some major changes. The affordable housing sector is also concentrating on improvements to its existing stock and is not looking to develop in any significant way (or acquire s106 stock). Sales volumes, particularly in London, have also fallen back; many people were buying at the limit for affordability and with increases in mortgage rates the pool of people able to acquire has diminished.

The other issue is the second staircase requirements for buildings of 18m or more and the related provisions in the Building Safety Act. The 'Gateway' process for approvals is very time-consuming and many projects are stuck in the queue. This particularly affects London as so many of its delivery has been in flats – typically over 80%, although this has risen to over 90% in recent years. This is in contrast to England overall, where the proportion has fallen from 20-35% in the early 2010s to only a little over 10%. This explains why the regions outside London have not seen the same drops – particularly as many of the flats delivered there are more likely to be low- or medium-rise and less affected by regulation.

What has also kept housing (as opposed to flat) delivery going is the rise of the Single-Family Rental sector. The impacts on flats have also extended to Build to Rent investors, who have increasingly moved away from “multi-family”. This has been assisted by the number of housebuilders looking to bulk dispose of stock. Lower operational costs have also made SFR more attractive. At the end of 2024 there were 14,142 completed homes in the sector (compared to 8,818 in 2021), 12,493 under construction (3,146) and 8,919 in planning (4,482). It's one of the few

property sectors that has seen an acceleration in activity and remains highly popular with investors. It is also one that largely contributes to development outside London or indeed the other big city cores.

This continued appetite exists alongside more subdued rental increases – as of January 2025, according to Hometrack, rents were 3.0% higher than a year before, compared to 7.4% at the same point in 2024. London is a notable outlier, with rents rising at just 1.1% in the year to January, compared to 5.1% a year earlier.

The wider housing and mortgage market remains *relatively* buoyant, with the Nationwide index pointing to a 3.5% y-o-y increase in May (and a 0.5% monthly increase). But again, this shows strong regional variation – 5-6% in the North and West Midlands, sub 4% in the South, and sub 2% in London – again reflecting how the more affordable parts of the country were better placed to absorb the shock of higher rates.

Transactions in the wider market have remained relatively robust at c. 70% of 10-year averages, although the increase in mortgage approvals seen for much of 2024 has reversed. Mortgage rates, though, continue to decline for floating-rate or short (2-year) fixed rates (now 5.02% and 4.54% on average respectively). They have risen for 5-year fixes (now 5.33% on average). This implies that the expectations for interest rates have declined in the short term but maybe risen slightly in the longer term. Nevertheless, activity should increase again over the year if interest rates continue falling – although a boom is a long way away.

So how can the housing market – particularly the development side – be revived? The government has announced a new equity loan scheme in the Spending Review, and some of the problems are absolutely related to the end of help-to-buy, particularly in London and the South East. London Mayor Sadiq Khan has talked about opening up sites up the green belt and given the clear preference for family housing among both buyers and investors, this would smooth delivery. And, there is the liberalisation of planning as set out in the Planning and Development Bill.

There is a big question around whether this is enough, given the sharp slowdown in activity. It looks increasingly unlikely that the government will get anywhere near its target of 1.5m homes over its term. The Spending Review does, though, contain some interesting announcements which will certainly support delivery (if not changing the game entirely).

WHAT'S A SOLUTION?

Despite these challenges, the sector remains resilient, underpinned by strong demand fundamentals and ongoing opportunities for innovation and growth. The need for the right expertise and connected strategic approach is important to help landowners, investors, and developers successfully navigate this evolving landscape and capitalise on emerging market trends.

A connected approach to Residential could prove to be the answer, with the ability to navigate this complex landscape requiring deep understanding of market trends, emerging risks, and strategic opportunities in a connected way that is easy to navigate and find the needed expertise. Residential sector connectivity allows organisations to work closely with landowners, investors, developers, and local authorities to navigate these complexities, ensuring resilience and long-term success in an ever-changing market.

At Montagu Evans, we utilise this approach with “Residential:Connected”, which revolves around seamless integration of our experts, ensuring our clients can easily access the specific expertise they need; driving the creation of resilient and thriving Residential communities.

GET IN TOUCH TO HARNESS THE EXPERTISE OF OUR RESIDENTIAL:CONNECTED TEAM AND TO FIND OUT HOW WE CAN HELP.



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THE SPENDING REVIEW

THE MAIN THRUST OF THE SPENDING REVIEW WAS A REDUCTION IN THE FOREIGN AND HOME OFFICE BUDGETS ALONGSIDE AN INCREASE IN FUNDING FOR THE NHS, EDUCATION, INFRASTRUCTURE AND HOUSING. THE KEY HEADLINES WERE £39BN FOR NEW SOCIAL AND AFFORDABLE HOUSING AND A FURTHER £10BN FOR HOMES ENGLAND.

KEY ANNOUNCEMENTS

- £39bn for social and affordable housing
- A further £10bn for Homes England
- A new deal for social housing rents and more money and loans for upgrades to their stock
- Big increases in infrastructure funding, especially in the city-regions, the Northern Powerhouse and the Oxford-Cambridge arc

Given the difficulties Registered Providers are having with the upgrading of their existing stock, the deal of a CPI+1% increase in rents, £2.5bn of low-interest rate loans for RPs, and £1bn for stock remediation, will be very welcome. This index-linked income stream should prove highly attractive to institutional investors. The additional money for Homes England will also help it to unlock sites plagued by viability issues.

The other announcements of interest are ones that may help deliver more housing in cities; recently, building has been skewed to greenfield sites. The elected mayors of city-regions will see £1.56bn over the next five years for infrastructure projects (a more than doubling in spending), while there will also be £2.2bn of extra funding for TfL's capital renewal programmes. New infrastructure announced in the review includes metro extensions in Birmingham, Doncaster and Tyne & Wear.

More specifically, there will be £3.5bn to upgrade the Manchester-Leeds TransPennine route and £2.5bn to restore East-West or Oxford-Cambridge rail. Hopefully this can unlock more sites and push forward regeneration, which has stalled in many locations.

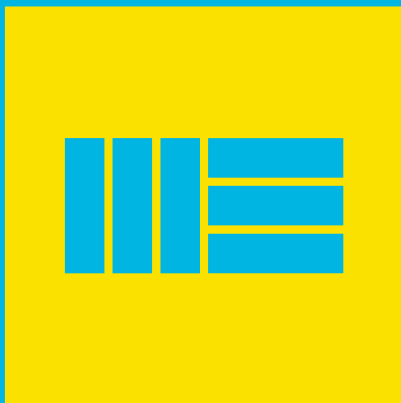
Finally, and not directly housing related, there were more announcements on pushing civil servants out of London to the regional hubs, and a further rationalisation of the London estate.

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