exigere

Q2 2025 Market Update

In our Q4 2024 Market Update, the impacts and influence of the government's Autumn Budget were yet to fully set in.

A few months on, the new administration's plans are starting to play out, and tariffs have emerged as the next major challenge.

Last year, there was optimism that the UK could enjoy a strong recovery in 2025: a much longed-for outcome after a decade of tumult. However, as winter set in, poor GDP growth figures, the Bank of England's (BoE) slower-than-expected interest rate reductions and ongoing geopolitical instability dampened hopes. Now, tariffs have sent stock markets tumbling, creating turmoil with global growth forecasts likely to be hit hard.

The first quarter of 2025 brought daily waves of economic, trade and political wranglings. At a domestic level, CPI inflation rose 2.8% year-on-year in February; the BoE expects it to climb further to 3.7% in Q3 2025, driven in part by rising energy and water bills. Inflation was not expected to fall to the government's 2% target until 2026 at the earliest, subduing expectations of steady interest rate reductions this year.

UK gross domestic product (GDP) grew just 0.2% in the three months to January 2025, compared with the three months to October 2024, and dropped 0.1% month-on-month in January. The BoE therefore started the year feeling conservative, warning of a 'bumpy path' ahead, citing global tariff sparring that has now dramatically started to play out, and Middle East uncertainty as additional factors hampering confident projections.

In February, while the BoE cut the base rate to 4.5%, it also cut its 2025 GDP growth expectations, from 1.5% to 0.75%. As of March 2025, the base rate remains at 4.5%. Also in March, the Organisation for Economic Co-operation and Development (OECD) revised its UK growth forecast to 1.4% in 2025 and 1.2% in 2026, down from 1.7% and 1.3%, respectively.

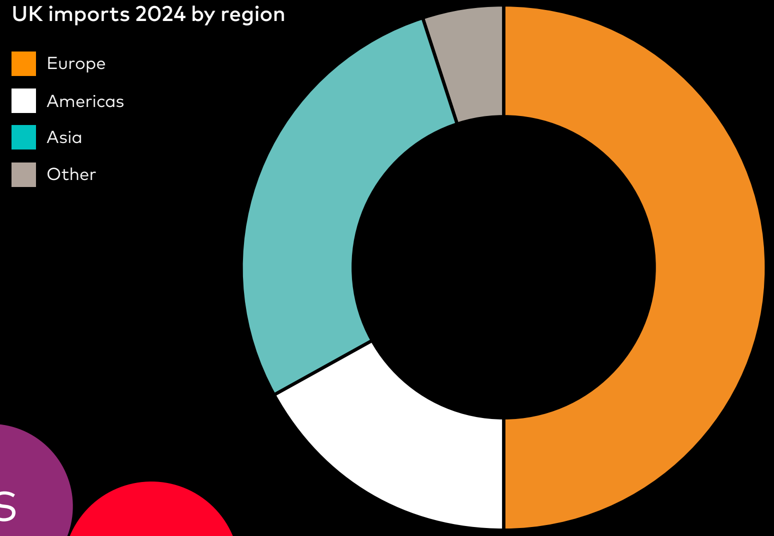
By the time of the Spring Statement in late March, the Office for Budget Responsibility had also tamped down expectations. It forecasts the economy to grow by just 1% in 2025, halving an earlier prediction and citing tariff uncertainty as a key reason for the revision. It now expects 1.9% growth in 2026.

The US's recent chaotic implication of tariffs will only serve to dampen any further growth, potentially impacting the demand for construction and it is likely to impact global supply chains in the short to medium term.

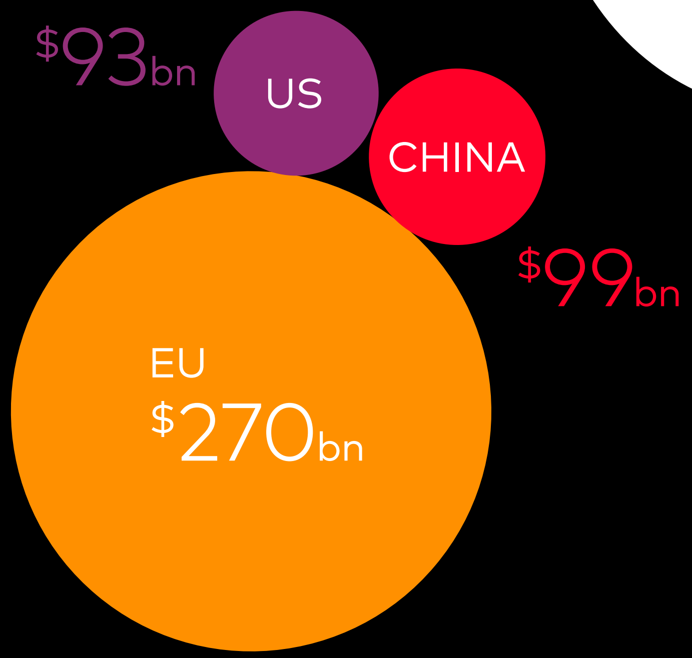
Proportionately, UK imports for construction-related materials and equipment comes mostly from Europe and China, although a significant proportion is produced domestically.

We do import some materials, machinery, plant and equipment form the US, but we have minimal exposure in the main, so we expect minimal direct material price inflationary impacts, assuming no further knock-on impacts to the supply chain or further impacts of tariffs.

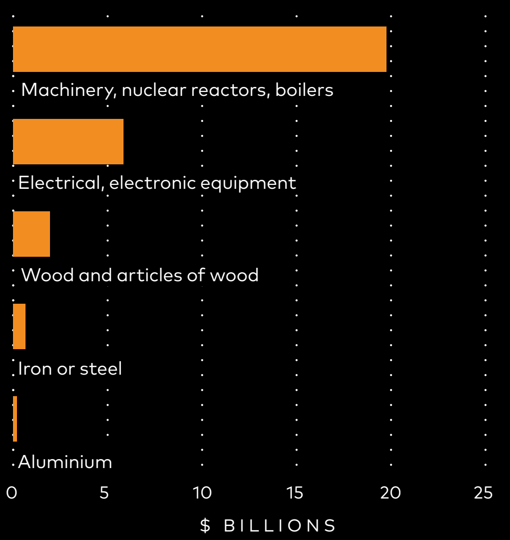
UK imports 2024 by region



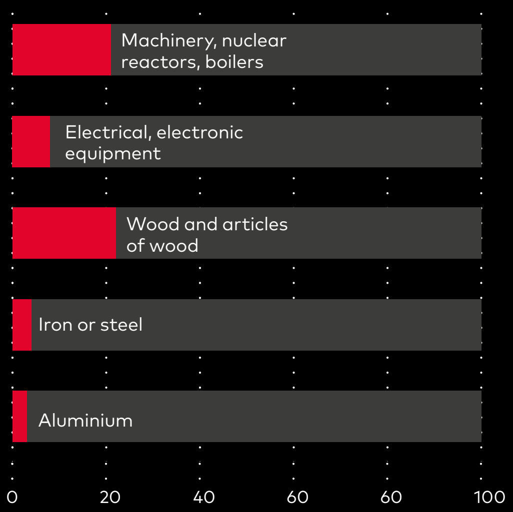
UK imports 2024 by value



Value of goods imported from the US (the biggest categories that might impact construction)



Proportion imported from the US (%)



Trump's 'Liberation Day', if not short-lived, will inevitably hit growth projections, and in conjunction with recent PMI figures, which are often considered a leading indicator, the possibility of a recession is back on the table. Indeed, with wider global uncertainty, disruption and the potential impacts on growth, this may cause further short to medium-term hesitancy in investment and dampen demand for construction. We may see inflation reduce, with further, faster interest rates cuts to follow.

That's not to suggest the UK's longer-term outlook is bleak. We still see a growth story over the longer term; however, the recovery is likely to be more subdued, and the impact on tariffs will take time to play out. A closer look at the underlying fundamentals and individual sector performance suggests that opportunities persist. The priority is to stay calm, identify the opportunities, and act on them through considered, targeted action with the right partners and behaviours.

CONTRACTOR SENTIMENT

Contractors feel the pinch amid wage hikes and insolvency shakeups

The central London market is particularly tough for contractors right now. Fingers were burnt in the past decade, with some contractors overstretching themselves in terms of their capacity and ability to deliver work. As a result, a number of poor performing projects were delivered, which further damaged balance sheets for businesses already fighting high inflation and insolvencies.

Industry insolvencies are not as acute as in 2023, when they were at their apparent peak. However, they continue to trouble the industry with their knock-on impacts on attitude to risk, cashflow and employment for associated businesses, and the need to get troubled projects back on track – exacerbating capacity constraints. In this environment, project delays and cost increases are often inevitable.

A cocktail of insolvencies, a fragmented, under-resourced industry, continued planning and regulatory change, evolving design driven by tenant demand, and growing pains adopting the Building Safety Act, are all impeding development and driving up construction sector costs.

All these factors contribute to a significant proportion of Tier 1 contractors continuing to feel risk-averse this spring. They want to consolidate, protecting their existing projects, specialisms, and partnerships, rather than experimenting and expanding. This is being reflected in the type and number of projects they will take on, as well as the risks they are prepared to take. They are generally only taking on projects in sectors which are a strong match for their skillsets and are achievable within their current capacities. Relationships, with both consultants and, more importantly, clients, are a material consideration for contractors.

Wage growth and NI increases are one of 2025's biggest industry cost pressures. Construction wages rose 6.7% in the year to January 2025, according to ONS data, having bottomed out in the first half of last year.

This month (April 2025) brings two more payroll hikes, both products of Labour's Autumn Budget. Employers' National Insurance contributions increase from 13.8% to 15%, and the National Living Wage rises 6.7%. Employers face a significant uplift to their costs this quarter.

SECTOR OUTLOOK

In offices, green shoots emerge

In the hybrid and home working years of 2020-2024, office developers had to adapt and adjust their ambitions, and speculative development was tempered. There are signs, however, of green shoots in the sector.

Post-pandemic, a four-days-in, one-day-out model is common, and expectations for full-time office attendance are increasing. This return to the office, coupled with a shortage of new provision over the past five years is driving up Grade A rents for prime, low-carbon office spaces.

In London, its tallest tower, AXA's 22 Bishopsgate, is now fully let after four years, with rents at the highest level ever achieved in the City. Real estate investor Derwent London posted growth in rental values of 4.3% in 2024, the highest levels since 2016.

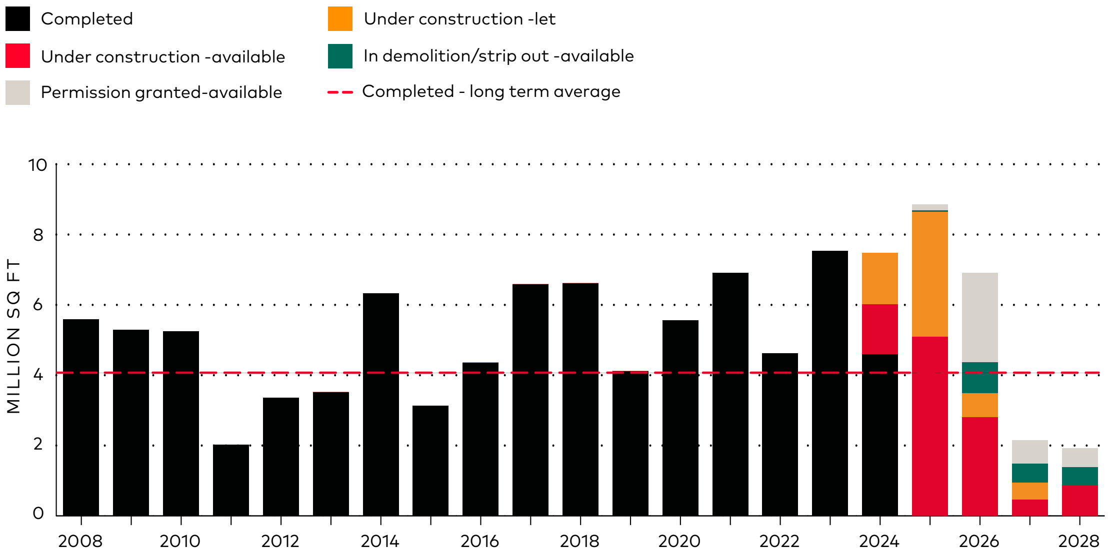
Outside of the capital, Savills reports prime office rental growth in key cities has been strong for three years, particularly in Bristol, Edinburgh, and Leeds. Investment has by no means ground to a halt. Offices attracted the third-highest levels of UK real estate investment in 2024, at £9.2 billion, the CBRE reports (living was the first, at £10.4 billion).

Over the longer term, demand for office space is set to increase as more blue-chip employers mandate full-time office attendance.


80 Goswell Road - Derwent London - office refurbishment

Central London: future office development pipeline

Source: Source: Deloitte, January 2025



As of March, JP Morgan employees are expected to be at their desks five days a week. Amazon, Goldman Sachs and Morgan Stanley have outlined the same expectation.

Offices need to be in prime strategic locations rich in amenities and boasting high sustainability credentials to meet blue-chip tenant client needs, and to attract and retain high quality staff. It could become a buyer's market for secondary or sub-prime office spaces that have laid dormant or under-utilised.

A shortage of supply could be further driven by falling new construction activity, which Deloitte said declined 12% in the six months to September 2024. Furthermore, it seems large-scale life science developments were propping up overall new build office volumes. They made up over a third of the new construction volume and were the sole drivers of new activity in the King's Cross and Docklands submarkets.

1 Knightsbridge Green - BEAM - office new build

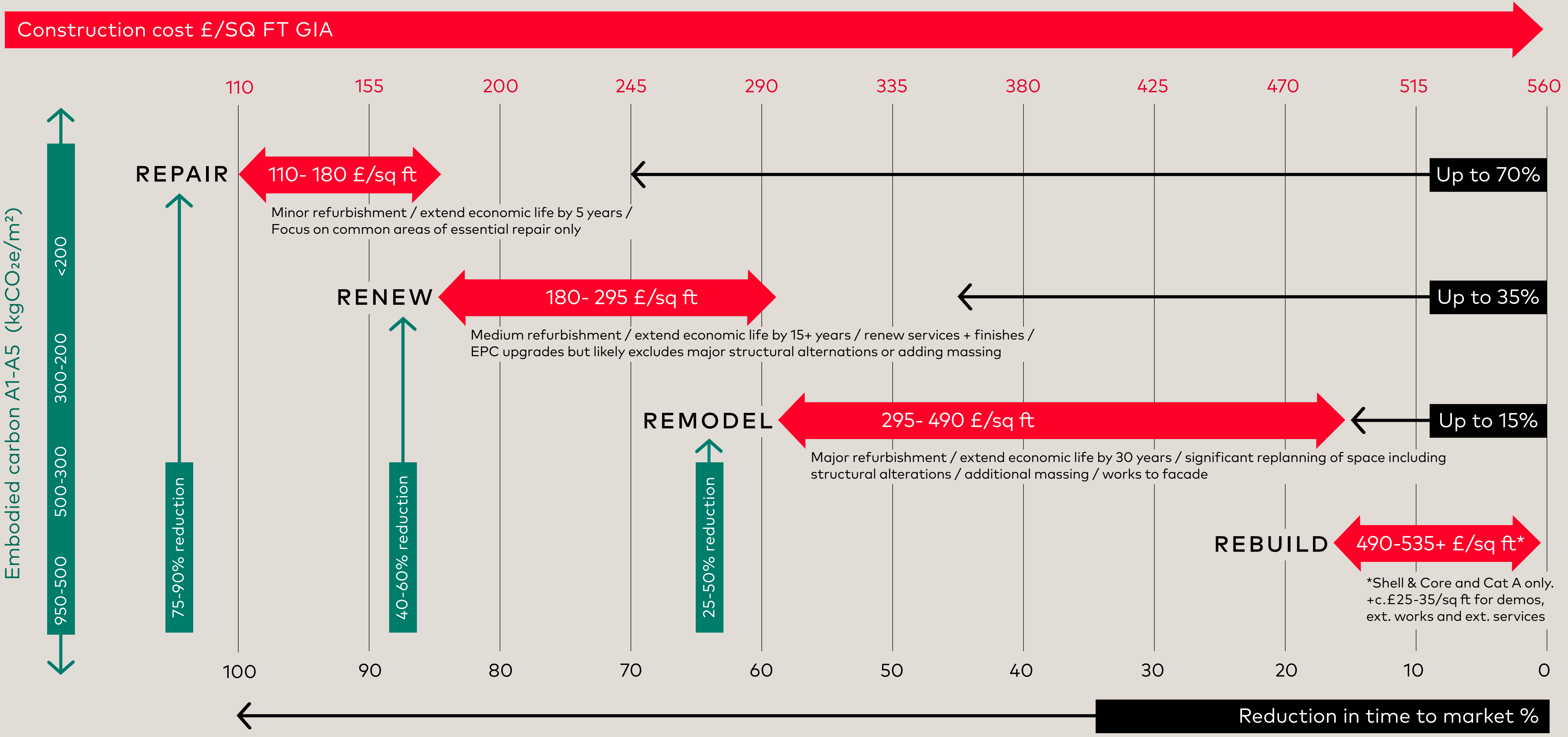
In contrast to falling new starts, 2023 and 2024 delivered good levels of completions, with 2025 set to deliver similar levels. There is sufficient tenant appetite to absorb all of this prime space. Annual completions for 2024 are anticipated to reach 7.5 million sq ft. According to their latest market estimated completion dates, Deloitte expects 8.9 million sq ft to be completed in 2025 and 6.9 million sq ft in 2026.

In the Square Mile, a strong pipeline of proposed and approved new build tower projects is being established, which should see spades in the ground from next year. Developer Brookfield Properties' 99 Bishopsgate tower is expected to begin construction in 2026. Meanwhile, AXA's all-electric 50 Fenchurch Street building is due to be completed by 2028, targeting BREEAM Outstanding accreditation and net zero operations. AXA also applied in March to build a 46-storey office project at 63 St Mary Axe, indicating a bullish attitude to the City's long-term office prospects.

For the office sector, viability and continued uncertainty remains an issue, and this is having a dampening effect on investment the number of schemes moving forward, even with relatively strong tenant demand for prime space.

The uncertainty caused by recent events could mean further delays to schemes moving forward; this remains to be seen. Capacity constraints and the hard lessons learnt over the last five years will mean that contractors will continue to be risk averse and selective in this sector.

exigere cost vs time office benchmarking Q2 2025



SECTOR OUTLOOK

Return to the office, consolidation and flight to quality support resilient central London workspace market

The outlook for the workplace market in central London appears generally positive, with a healthy pipeline of projects planned for 2025.

In terms of leasing activity, the central London office market has shown resilience, with continued strong demand for Grade A office space. In 2024, overall take-up totalled circa 10 million sq ft – a slight increase from 2023. This trend is expected to continue in 2025, driven in part by the ongoing push toward a return to the office. This is set against a backdrop of stable vacancy rates in both the City and West End. The finance and professional services sectors were the most active over the past 12 months – a trend expected to continue.

3 New Street Square - Landsec Myo - workspace

As previously highlighted, prime locations within central London saw strong rental growth in 2024, partly driven by a limited supply of high-quality office space. This growth is expected to persist, particularly for sustainable buildings, amid a diminishing development pipeline. Overall, the central London occupier market is poised for a robust year, with continued demand for high-quality office space and stable vacancy rates; all subject to investment decisions which may fall out from the current turmoil.

Fears of major supply chain impacts following the demise of ISG have, so far, not materialised, with others able and willing to step in. Clients have also played their part in supporting the supply chain where possible.

LONG-TERM TREND

Population growth is a key growth and productivity indicator

In our Q4 2024 update, we flagged the UK's rising population as a core growth factor to watch. New figures released by the Office for National Statistics (ONS) in January bore this out: the ONS expects a 7.3% population increase between 2022 and 2032. This is largely driven by migration, with 9.91 million people set to immigrate to the UK in this period.

The UK government responded by saying it wants to bring down such 'staggeringly high' levels of migration, but we also foresee significant long-term upsides to this trend.

With migration comes people available to work and spend in the UK, cementing the UK's reputation as a good place to study, live and work on the global stage. The construction market suffered deeply from the labour exodus sparked by Brexit; a return to accessible, skilled international labour can only be a good thing, given a lack of domestic appetite to enter the industry.

London will be the centre of this population growth and as such, faces significant challenges in terms of homes, healthcare, and education provision – but also the biggest opportunity for productivity gains.

As of Q1 2025, jumpstarting productivity is a priority for the capital. Between 2008 and 2022, productivity ground to an almost-halt, at 0.12% per year. In contrast, productivity expanded on average 3.16% a year in the period 1998-2007, according to the London Councils.

In February 2025, the Mayor of London launched the London Growth Plan, which targets restoring London's productivity growth to 3% per year – making London's economy £107 billion larger by 2035. This may be further bolstered by the fact that the UK seems to have faired better than most from the imposition of tariffs, which could make the UK an attractive proposition for many.

SECTOR OUTLOOK

Hotels and retail benefit from increased town and city centre footfall

A rising tide lifts all boats, and a return to the office also helps the UK's retail sector. After a string of blows over the past decade, as of Q3 2024, UK retail investment volumes were up 8% year-on-year, according to Savills, pushing up rental yields and drawing the attention of international institutional investors. This reflects good retail growth in other European markets.

Deals such as December 2024's Landsec acquisition of a £490 million, 92% stake in shopping centre Liverpool ONE evidence this trend. Landsec said retail sales at the destination grew 5% in 2024, with new leases signed 10% above ERV, and relettings and renewals 5% above previous passing rent. It also highlighted a trend for consumers wanting physical retail to deliver 'fewer, bigger and better stores from key brands' as fuelling its decision to rebalance its portfolio and divert investment into retail.

Ruby Stella - RE Capital - hotel new build

The UK hotel sector is a strong performer, with investment activity returning to pre-pandemic levels. Savills says 2024 investment in the sector topped £5.8 billion, concentrated in London, which saw an impressive 91% year-on-year increase on investment. London was named the most attractive European city for hotel investment in 2025, according to Deloitte's 2024 poll of European senior hospitality figures and investors.

Hotel occupancy volumes are strong across the UK: London and regional hotels are now back to pre-pandemic levels of occupancy. Last year also saw over £400 million of former office buildings being converted into hotels, a trend that shows no signs of abating.

Knight Frank research found full-service hotels with strong meeting, conference and events provision were the biggest winners in 2024 – reinforcing the sense that travel, and doing business in person, is back.

SECTOR OUTLOOK

Life sciences hoped to jumpstart productivity, as the UK seeks to build Europe's Silicon Valley

While it remains to be seen whether full-time office work will fully return, the underlying fundamentals of the UK's business culture are strong.

No other country in the world offers highly developed political, legal, education, life science and finance sectors in such proximity to each other. This advantage is being capitalised upon. In January, Chancellor Rachel Reeves outlined her ambitions to create 'Europe's Silicon Valley' in the 'golden triangle' of Oxford, Cambridge and London.

Life sciences and AI are the two sectors expected to power the 'Oxford-Cambridge Growth Corridor', which the government hopes will boost the UK economy by up to £78 billion by 2035. The three cities will be better integrated and able to collaborate, so the plan goes, by relaxing planning to stimulate new housing, rail, water, roads and rail infrastructure in the triangle.

These are punchy, ambitious plans, but it will take time to see what they will translate to in reality. The life sciences and AI sectors are characterised by speculative, fast, and scrappy growth. There are major winners, but also many players that fail to scale. This makes for unpredictable tenants, making it difficult for developers to base their returns (and lease terms) on them with confidence. It is undoubtedly an exciting opportunity, but the market is still learning how it is going to turn this promise into steady growth and performance.

Office and life sciences demand in the region slowed in 2024, most significantly in the life sciences sector. This was due to slowed global venture capital activity, hindered by a challenging economy. Despite this, overall demand still outstrips supply. Early signs in 2025 are positive, with uptake in January alone exceeding Q4 2024.

Historic supply constraints in the Oxford-Cambridge region are gradually easing, with 4.3m sq ft of laboratories under construction as of Q4 2024 and due to complete by 2027, with a further 5.2m sq ft with planning permission. This will support the region to be able to react to demand requirements proactively, and boost growth in the region.

Vitrum - Breakthrough Properties - life science new build

Investment activity in the Oxford-Cambridge region remains robust, with improving economic conditions, stable yields, and growth in rents, but US tariffs will potentially impact the pharmaceutical and tech industries more than many, and it remains to be seen how this impacts investment in the sector.

SECTOR OUTLOOK

Bold state housing targets have been set, but industry barriers remain

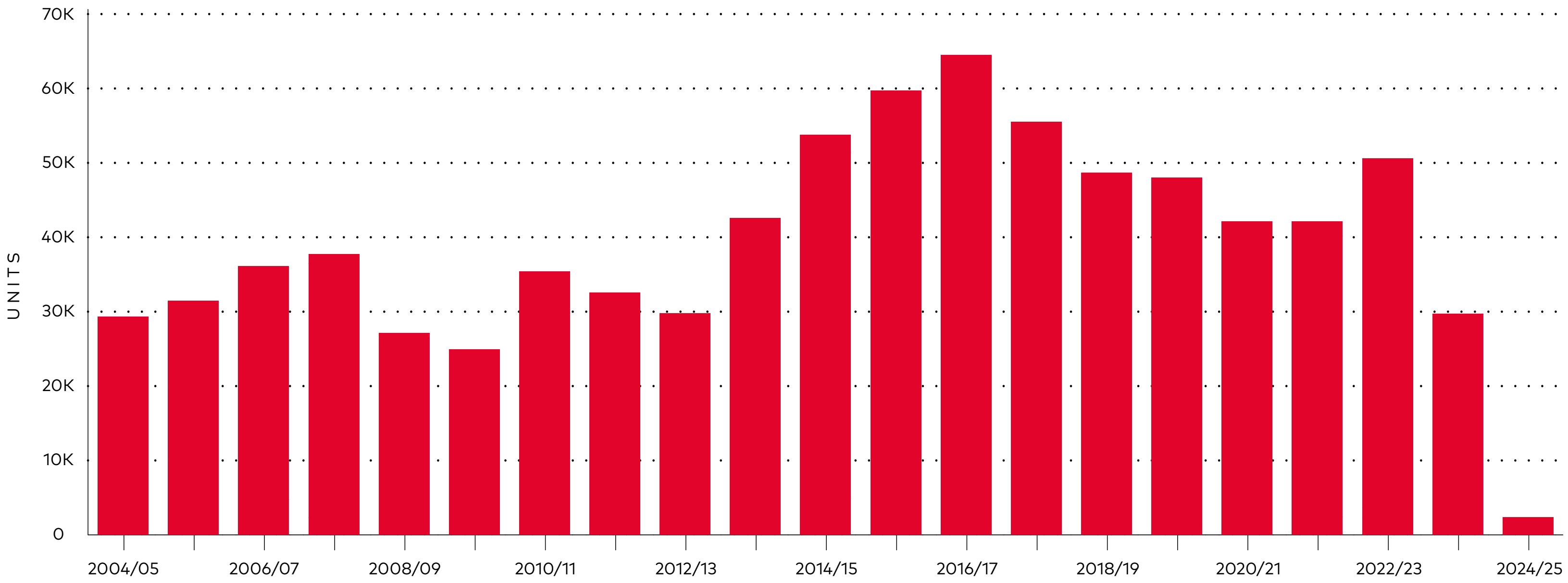
Housing was a Labour manifesto headliner, promising the construction of 1.5 million new homes in England by 2030.

This is unlikely to happen. Even if we take the systemic lack of supply chain skills and capacity out of the equation, well-documented bottlenecks in the Building Safety Regulator's (BSA) gateway approval process for new developments are heavily impacting projects, damaging the entire supply chain.

In late March, the OBR injected some reality into the government's 1.5 million target, stating it anticipated that, in a best-case scenario, 1.3 million new UK homes could be built by 2030 – falling short of the 1.5 million homes for England alone.

Residential starts

Source: GLA Residential starts dashboard



In March, Construction Leadership Council head Mark Reynolds warned the government's Housing Committee that approvals delays are forcing construction industry layoffs and spiralling costs, making it hard to build.

Reynolds cited two London and Leeds-based projects that have jumped in cost due to approvals delays. Gateway 2 approvals are intended to take 12 weeks: Reynolds reported 40 to 48-week approval processes for some projects. A lack of multidisciplinary teams able to carry out the required fire safety assessments, and a reported staffing shortage in 2024 at the regulator itself, are other issues.

Furthermore, surveyors are now required to register as building control approvers under the BSA.

Carrington West reports this is leading to significant numbers of surveyors retiring, rather than take on the risk – and for those at the beginning of their career, changing course. As the building control talent pool shrinks, low staff availability is driving wage inflation.

Hackney New Homes Programme; Fellows Court - Hackney Council - residential new build (draft proposal at RIBA Stage 3)

In response to these pressures, we anticipate further standardisation of homes to avoid the risk of projects being sent back to the planning drawing board – which, sadly, risks associated losses of architectural, design and technical innovation. We are also witnessing schemes being designed under the BSA's referable height, to avoid the process entirely. Many housing developers are simply not building, adopting a wait-and-see approach.

Across all tenures, the UK's acute shortage of sustainable, affordable housing is likely to support long-term rental demand – but not necessarily sales. At present, planning, staffing and regulatory bottlenecks continue to stymie the sector.

Challenges adopting the Building Safety Act will resolve with time and practice. How long that will take to translate into a consistent pipeline of projects being rolled out on the ground is an issue the construction industry will have to manage this year from a fee, hiring, and planning perspective.

Over the longer term, the construction industry's skills shortage gap must be addressed. Even when developments are released from short-term impediments, without the people to build them, wage inflation will only increase.

Major house developers Persimmon and Taylor Wimpey are projecting single-digit housebuilding completions growth for 2025, between 3-8% for Persimmon and 4-8% (Taylor Wimpey). March commentary from the economics director of the Consumer Protection Association, Noble Francis, stresses security of supply – trades, materials, and product availability – will be just as important as the cost of supply for this projected growth to materialise, in 2025 and beyond.

As Francis stressed, construction skills investment, affordability support for first-time buyers hoping to enter the property market, and a commitment to social rather than 'affordable' housebuilding, are just a handful of the factors that would drive up housebuilding confidence. The government must couple its bold housebuilding targets with meaningful supporting action.

The Spring Statement offered indicators that the government is starting to listen to these industry requests. Chancellor Rachel Reeves announced a focus on planning reform, an additional £13 billion in capital infrastructure over the next five years, the launch of a £600 million construction skills package to train up to 60,000 more skilled workers, and an extra £2 billion investment in social and affordable housing.

SECTOR OUTLOOK

Purpose built student accommodation is an investment out performer, but student attitudes are evolving

There is one performance outlier in the UK housing market. The purpose-built student accommodation (PBSA) sector outperformed all other commercial property in the year to September 2024, providing returns of 9.8% (CBRE). Now a standard asset class for global institutional investors, its growth is fuelled by the UK's student population being at an all-time high, with record levels of international students coming to the UK.

However, reflecting the broader housing sector, PBSA development is not consistent across accommodation types. It is primarily mega-projects in active planning and construction – from the 1,672-bed Urbanest scheme next to London's Billingsgate Market (featuring a drive-thru McDonald's) to a 27-storey project in Nottingham, set to become the city's tallest structure.

As with the skyline-altering offices being greenlit in the Square Mile, the scale of these tower projects, alongside their self-contained nature, is raising questions about their future impact and integration in their local communities.

We also see early indicators of students beginning to move away from these highly serviced and expensive housing options. The cost of living and rental inflation is outstripping student maintenance loans, and PBSA rents are around 25-30% more expensive than off-street rents, higher education think tank HEPI reports. Students are therefore starting to seek accommodation in the private rented sector instead, which itself increased by 9.2% in cost in England in 2024.

If students begin to migrate back to traditional private rental houseshares, this will place further pressure on the already squeezed broader housing market.

Policy changes timeline 2023 – 2026

Interim update on BCO 2019 Specification Softening of requirements

Second staircase DLUCH announced second staircase would be mandatory in buildings over 18m

Building Safety Act – gateway points Gateway points for HRBs came into play

RICS whole life carbon assessment for the built environment Second edition extends professional body's existing standard to cover all buildings and infrastructure

Permitted development Significant legislative change introduced, expanding flexibilities for converting commercial properties to residential use

Skilled worker visas Minimum salary requirements via the Skilled Worker route will increase, plus shortage occupation list will be replaced and requirements under the spouse or partner visa will become more onerous

Building Safety Act – building control Requirement for all building control inspectors to register with Building Safety Regulator – an unachievable deadline according to industry representatives

Introduction of UKCA Government considering 58 recommendations made - including broadening the definition of HRBs

National Planning Policy Framework changes Consultation launched on proposed changes to planning policy

Grenfell inquiry Government announced intention to consult on plans for all social and privately rented homes to meet EPC C, or equivalent, by 2030

UK Net Zero Carbon Buildings Standard (The Standard) Pilot version launched

New consumer code for housebuilders Intention to introduce new code announced in response to CMA probe

Changes to Approved Document T (toilets) come into force Applying to non-domestic buildings and requiring provision on dedicated male and female facilities

Procurement Act 2023 Governing public sector procurement - delayed

Future Buildings Standard Due to come into play in 2025 but detail still lacking

Further changes to building safety regulation Real possibility following conclusion of the Grenfell Inquiry 2025

Leasehold and Commonhold Reform Bill Draft Bill promised in the King's Speech 2025

Approved Document B update Second staircase becomes mandatory - 30-month transition period ends

2023 2024 2025 2026

ON GOING **Net Zero Carbon Building Standard –unofficial 'Part Z'** Voluntary – industry-led – standard under development.

CONCLUSION

If cashflow is king in unstable times, protecting the supply chain serves us all

At the outset of Q2 2025, the UK is not enjoying the rebound in investor confidence many hoped for in 2024. There are multiple short-term factors making project viability hard.

While it is true that there are only so many changes, surprises and snags that can be absorbed, it is also true that the industry has managed to withstand a remarkable series of shocks and change over the past decade. Resiliency has been borne out of this. Now, further uncertainty and volatility due to Trump's 'Liberation Day' is the latest challenge to overcome.

There is a flight to quality taking place, driving good behaviour, and rewarding those taking a realistic approach to contract negotiations. Many successful industry players are characterised by their collaborative, flexible, and equitable behaviours.

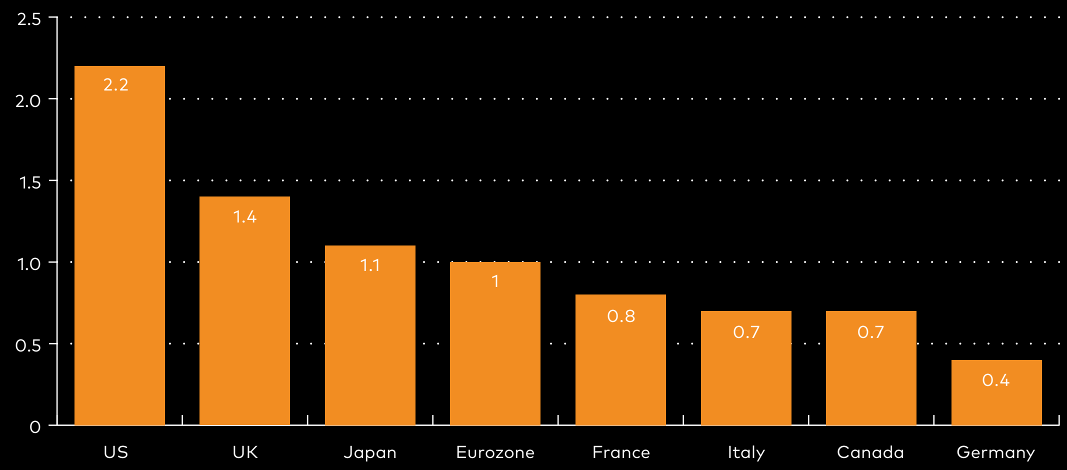
In practical terms, this looks like prioritising coordinated design, planning and early engagement to ensure high-quality teams and outcomes; strong relationships and appropriate workforce and materials availability; accurate and proportionate risk allocation; and where possible implementing measures to protect supply chain cashflow.

While the immediate outlook for the coming year now remains even more uncertain, reflecting an unpredictable global economic and geopolitical climate, we see positive indicators over the mid-and long term.

Interest rates are falling, albeit perhaps slower than had been anticipated. GDP growth, whilst minimal, was taking place, but this may now be further hampered. Demand is there for the right product. Longer term, the economics are slowly heading in the right direction to unlock the supply. While growth predictions have halved, it is worth pointing out that the OECD projects the UK to be the second fastest growing G7 economy this year and next, second only to the US. US tariffs imposed on the UK are not as fierce as those imposed on other nations', and are more likely to cause further indirect economic headwinds than direct consequences for construction prices, although we may see some short to medium term supply chain disruption on certain materials, plant and equipment.

OECD real GDP growth (%) 2025 forecasts for G7

Source: UK govt (forecasts published 17 March 2025)



While fears of a possible recession now loom, a muted upwards trajectory is probably the best we can hope for in the medium term. This slow-but-steady pace may in fact prove to be a boon over the longer term; in contrast to the volatility being experienced in other markets, the UK could benefit from being perceived as a safer, more stable place to land for global investors.

It is undoubtedly a very uncertain time, calling for high levels of perceptiveness, responsiveness, and flexibility. Calm heads will prevail.

Our TPI predictions

3.25%

for 2025 but there are drivers that may push our inflation forecast toward our low-end prediction, given the recent unpredictable and tumultuous events

Q2 2025 (%)

SENSITIVITY RANGE	2023	2024	2025	2026	2027
LOW			1.5%	2.0%	2.0%
BALANCED	**4.0%**	**2.5%**	**3.25%**	**3.75%**	**3.75%**
HIGH			4.5%	6.0%	6.0%

76 Southbank - Stanhope - office refurbishment

exigere

+making projects happen

Author

David Thornley
Partner

07834 257188
david.thornley@exigere.co.uk

exigere.co.uk