

Green Shoots of Recovery Expected by the End of 2023 for UK Real Estate, Says CBRE

4 years ago



Real estate investment markets are expected to emerge from a period of uncertainty and pricing will likely stabilise towards the end of 2023, with a continued flight to quality and ESG being key drivers of activity across all asset classes, according to the UK Real Estate Market Outlook 2023 published today by [CBRE](#).

In the near term, a moderate recession is expected, with high inflation and rising interest rates putting downward pressure on economic activity. Income returns, rather than capital growth, will likely drive commercial real estate returns in 2023 - heightening the importance of asset management and the financial performance of occupiers.

On the investment side, CBRE's Head of UK Research, Jennet Siebrits, anticipates further inbound investment into the UK market. "While we forecast investment volumes will drop somewhat, the UK real estate market benefits from a diverse investor base. The realignment of prices towards the end of 2022 means that 2023 may provide opportunities for private capital to enter the UK market."

Siebrits added: "We face an undoubtably challenging start to 2023, but the clouds will begin to break later in the year. Logistics and purpose-built student accommodation sectors have robust rental growth prospects and life sciences, build-to-rent and healthcare sectors have strong fundamentals that remain attractive to investors."

"The performance of the listed sector in 2023 will also be of interest. In 2022, the share prices of UK REITs fell well before the change in the private property market. Investors will therefore be watching for signs in listed property prices that indicate improved confidence in UK real estate. Green shoots of recovery will materialise."

Overview of sectors:

Sustainability

The implementation of more mandatory disclosure requirements and high energy prices will accelerate sustainability action within the real estate market, from both investors and occupiers. CBRE expects buildings with greater energy efficiency or using onsite renewables to be insulated from the worst of the energy price shock.

Landlords and investors will be better informed as to the cost and benefits of sustainability and green features, as better quality and more substantiated data is cemented into the valuations process. More 'net zero' buildings are anticipated to enter the market in 2023 and the increased demand from occupiers will prompt further scrutiny as to what qualifies as a 'net zero building'.

Office

In the office market, leasing activity will be constrained due to a fall in office-based employment in 2023. CBRE expects continued strong demand for the best quality space and as a result, appetite for properties that are newly developed or refurbished will remain high.

Yields will expand further during the first half of 2023 in most UK office markets. Pricing will stabilise during 2023 and this should stimulate more investment activity. CBRE forecasts office investment volumes to be down 20% year-on-year in 2023, with the majority of transactions likely to take place in the second half of the year.

Logistics

CBRE anticipates occupational activity levels will remain above long-term averages in the logistics sector. Third-party logistics providers are expected to continue leading the take-up due to the ongoing search for flexibility in supply chains.

The market faces challenges including critically low levels of supply, increasing construction costs, rising exit costs and higher exit yields. However, CBRE asserts that logistics assets will remain attractive to investors with continued rental growth expected.

Retail

CBRE expects retail to be less affected by repricing than other sectors, yet it will not be immune to the wider economic headwinds in 2023. The physical store will play a key role, with modest expansion anticipated for well positioned occupiers. Furthermore, the volume of business casualties is expected to be less severe than during the pandemic.

Residential

While activity in the housing market will reduce in 2023, CBRE forecasts investment appetite for build-to-rent and co-living to remain strong.

The challenges faced in the for-sale market should boost the already strong occupier demand for rental housing, including build-to-rent, co-living and single-family homes. The rental sector will remain resilient

against recession, and there is likely to be strong rental growth of 4% in 2023 and 5% in 2024.

CBRE anticipates the sector will experience a strong bounce-back as the economy recovers and lower inflation allows interest rates to fall.

The affordable housing sector will also remain resilient, supported by its strong ESG credentials and appeal to investors. Social and affordable housing funds account for the largest segment of social impact investment in the UK, valued at £3.8 billion.

Purpose-Built Student Accommodation (PBSA)

In 2023, the PBSA sector will be characterised by undersupply, slowing development and record-high demand for available beds due to a growing student population. Even with a backdrop of high inflation and rising interest rates, the prospect of high total returns led by strong rental growth will drive PBSA investment.

Hospitality

For the hospitality and leisure industry, operators across the sub-markets are at various stages of recovery and confidence is growing. The sector generally offers highly attractive inflation protection and there is a wall of capital targeting the sector, with demand for operational platforms exceeding supply.

In the hotel sector, demand will remain strong. As the debt market stabilises, the operating fundamentals will prove attractive to investors, with CBRE predicting growing investment volumes during the year.

Healthcare

CBRE anticipates investment activity in the healthcare market to remain robust in 2023, with investors attracted to strong occupier demand, long lease terms, index-linked reviews and the ability to deliver on ESG strategies.

The current lending environment is creating opportunities for property investors that can work with operating businesses to create flexible, long-term partnerships. CBRE expects this to be an area of increased activity in 2023, particularly where refinancing has become more challenging.

Data Centres

Despite the challenging wider economic backdrop, demand for data centres remains near all-time highs, as the largest cloud service providers look to expand their presence in London.

CBRE forecasts high levels of M&A activity in the data centre market. Providers need to expand to meet the needs of their largest customers and the cost to do so has soared. As a result, new combinations will be created.

Life Sciences

The life sciences sector continues to grow, in part driven by companies in this sector seeking to de-risk supply chains by capitalising on the nearshoring, onshoring and reshoring trend which countries across Europe are benefitting from. The 'golden triangle' locations - Cambridge, London and Oxford remain a

particular focus, with a majority of funding allocated to these areas. However, this is broadening into other regional locations and with Government ambitions to make the UK a “Science Superpower” by 2030, the sector is likely to benefit from continued research and development funding as part of a package to deliver this.