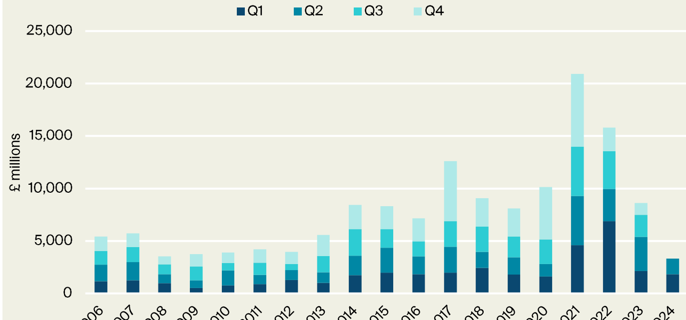
UK Logistics Market Dashboard

June 2024

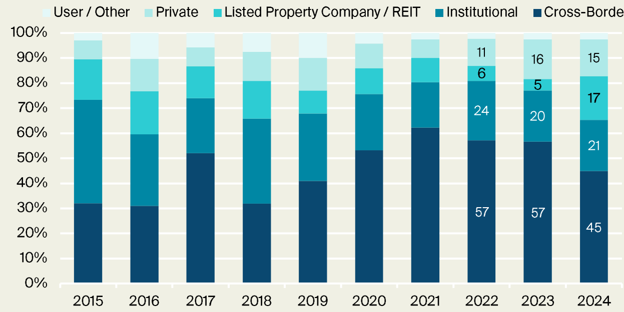
INTERNAL USE AND KEY CLIENTS ONLY

Investment market



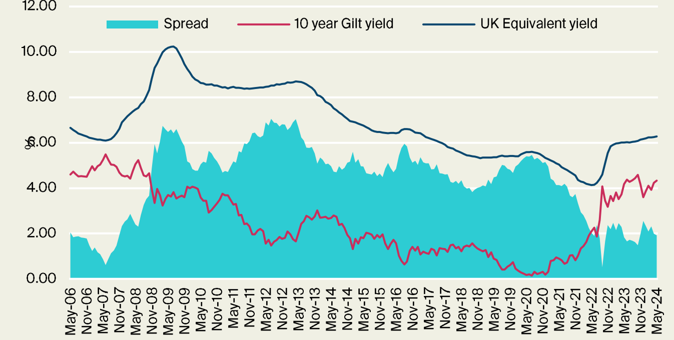
Source: Knight Frank Research, RCA

** Q2 2024 investment totals are not complete



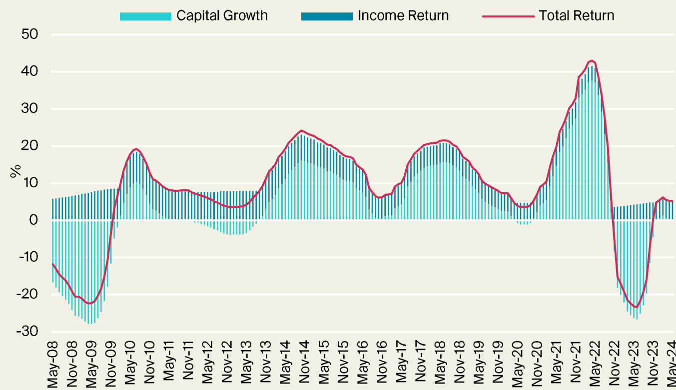
Source: Knight Frank Research, RCA

Yields



Source: Knight Frank Research, Macrobond, MSCI

Performance



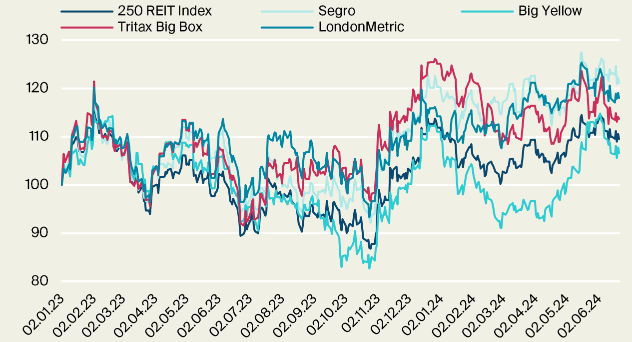
Source: Knight Frank Research, MSCI

Total Returns forecast (%) -Q1 2024

	2024	2025	2026	2027	2028	2024-28 CAGR
Industrial	8.4	9.3	8.6	7.6	6.9	8.1
Office	0.7	6.2	8.0	7.6	7.2	5.9
Retail	8.0	8.9	8.2	7.3	6.8	7.8
Other	5.9	8.1	7.9	7.5	7.1	7.3
All Property	5.8	8.2	8.3	7.5	6.9	7.4

Source: Knight Frank Research, RealFor

Listed real estate



Source: Knight Frank Research, Macrobond

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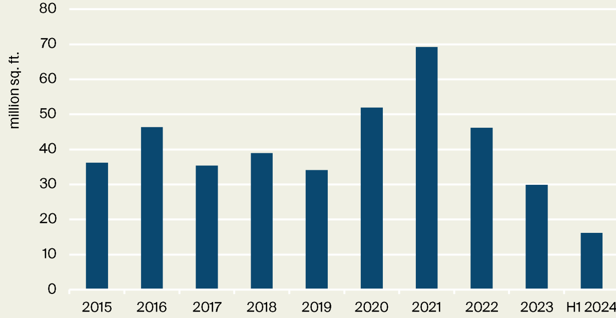
Occupier market

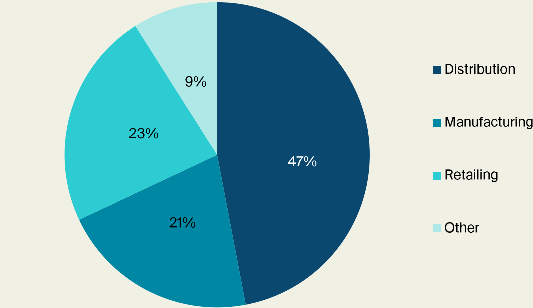
Take up (units over 50,000 sq. ft.)



Preliminary H1 2024 total

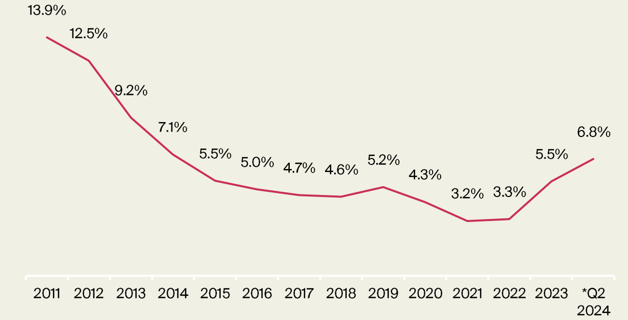
Source: Knight Frank Research

Take up by occupier type – last 4 quarters (to Q1 2024)
(units over 50,000 sq. ft.)



Source: Knight Frank Research

Vacancy Rate (%)

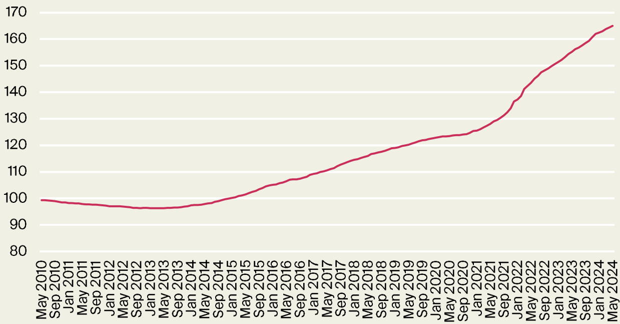


Preliminary Q2 2024 figure

Source: Knight Frank Research

Rents

Average market rental growth
Jan 2010 = 100



Source: Knight Frank Research, MSCI

Average rental growth forecast (%) -Q1 2024

	2024	2025	2026	2027	2028	2024-28 CAGR
UK	4.7	3.1	2.4	2.7	2.9	3.2
London	5.5	4.0	3.2	3.5	3.8	4.0
South East	5.1	3.5	2.7	2.8	3.1	3.4
South West	6.2	3.2	2.1	2.1	2.2	3.1
Eastern	3.7	3.2	2.7	3.0	3.1	3.1
East Midlands	4.4	2.4	1.9	2.3	2.6	2.7
West Midlands	4.2	2.4	2.1	2.6	2.9	2.9
North West	5.3	3.0	2.2	2.4	2.5	3.1
Yorks & Humber	4.7	2.5	1.8	2.0	2.3	2.6
North East	4.7	2.8	2.2	2.4	2.5	2.9
Scotland	4.1	2.2	1.7	1.9	2.0	2.3
Wales	3.6	1.6	1.2	1.9	2.4	2.1

Source: Knight Frank Research, RealFor

Development

Development completions (units over 50,000 sq. ft.)

Source: Knight Frank Research, Glenigan

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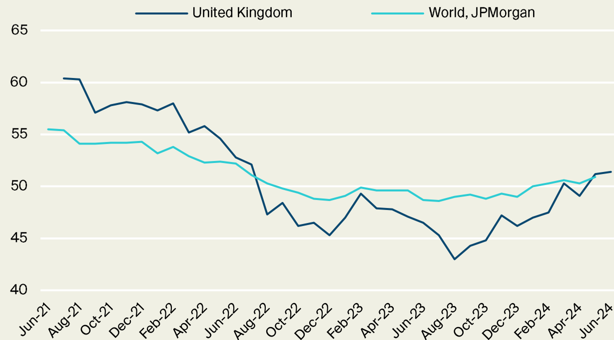
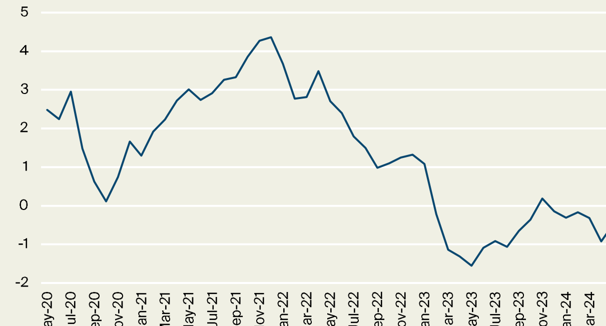
Industry, trade and manufacturing

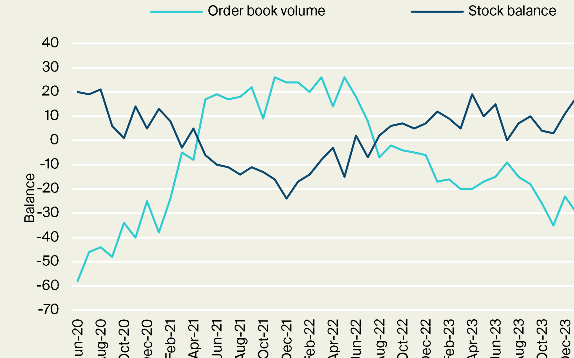
Manufacturing PMI Index



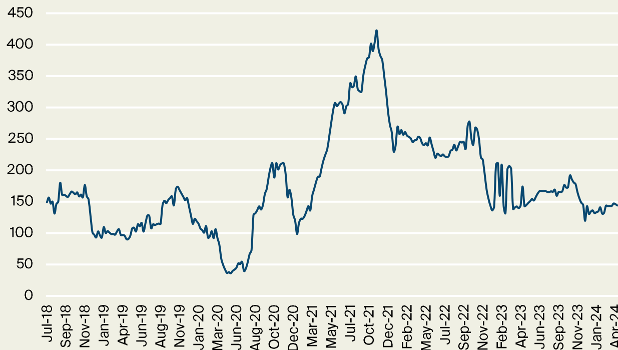
Global Supply Chain Pressure Index (GSCPI)
Standard deviations from average value



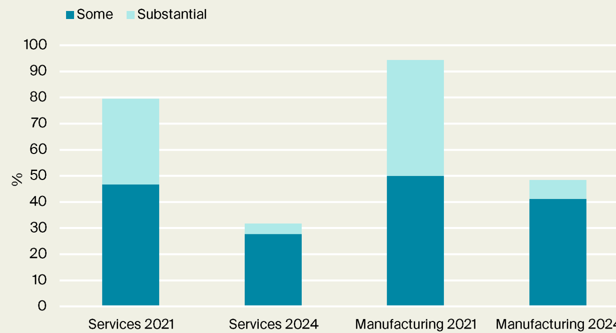
Order Books, Stocks Balance and Output Prices
CBI Industrial Trends Monthly Survey



Job Vacancies Index - Transport/Logistics/Warehouse



Supply Availability Indexes



Key comments

- The Flash Manufacturing PMI edged higher to 51.4 in June from 51.2 in May and its highest reading since June 2022. Despite a fall in demand from export markets, new orders rose.
- Supply chain disruptions have eased, but remain a concern. The GSCPI rose to -0.48 in May, up from -0.92 in April (revised down from an initial reading of -0.85). Easing supply chain pressures have contributed to the slowdown in inflation.
- According to the CBI Industrial Trends survey, manufacturers reported order book volumes below "normal" in June but sharply improved relative to last month (-18% from -33%). Stock levels remain "more than adequate" standing at +14%, the same as in May.
- Job vacancies in the transport, logistics and warehouse sector have remained broadly stable over the past three months but a year-on-year comparison shows a slight decline in vacancies, with the last four weeks showing job vacancies at around 6.6% lower than a year ago.
- Online retail penetration rates (excl. auto fuel) rose to 27.2% in May, from 26.7% in April 2024. The value of online sales also rose, up 7% month on month and 5% higher than May last year.
- Online grocery retail penetration rates are up slightly month-on-month, with 9.1% recorded in May, the same penetration rate as May last year. This compares with a monthly peak reading of 12.4% recorded in January 2021.
- However, indications for June figures are less positive. The latest CBI Distributive Trades Survey shows internet sales declined heavily, and at a faster pace than expected in the year to June (-45% from -6% in May). Online sales are expected to fall again next month.

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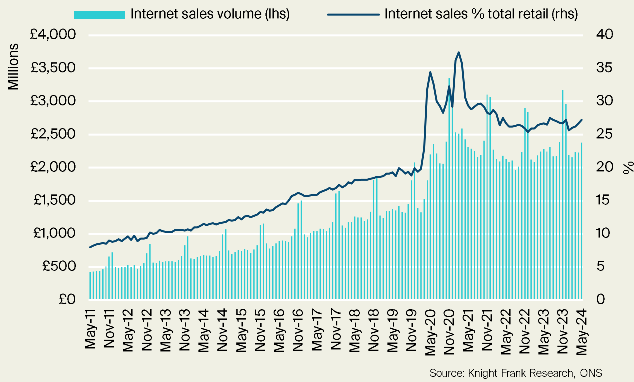
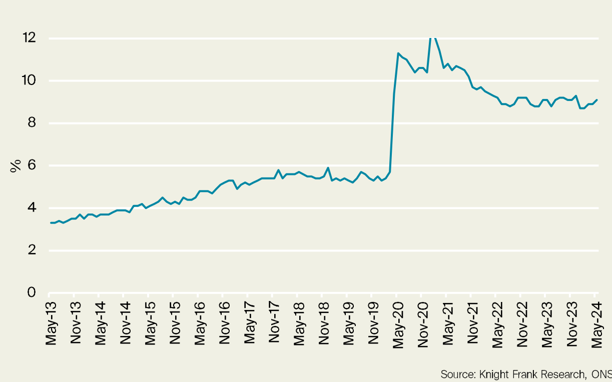
Online retail sales



Source: Knight Frank Research, ONS



Source: Knight Frank Research, ONS

Retail distribution

Source: Knight Frank Research, CBI

Market commentary

A new chapter awaits: What will the UK Election and the next phase of market growth mean for the industrial and logistics sector?

Polling stations and great expectations

With less than a week to go until the nation goes to the polls on 4th July, the industrial and logistics sector is paying close attention to the parties' manifesto promises and potential impacts. While specific details are still emerging, several policy areas could significantly impact the sector, particularly new policies on trade, transportation infrastructure, and environmental regulations.
Over the past five years, the industrial and logistics sector has seen four iterations of an Industrial Strategy, as well as a changing post-Brexit trade environment to adapt to. Both investors and operators within the industrial and logistics sector will be looking for a government and policies that promote growth and stability and support trade.

Business Rates reform?

A potential change in government may bring changes to tax regimes (such as business rates) or regulations around environmental standards, which could pose a risk to the sector. Such changes have the potential to impact business planning and be costly and operationally challenging, especially for small and medium-sized enterprises (SMEs).
All the main parties have looked at the potential for business rates reform. Indeed, the Conservative manifesto pledges to 'continue to ease the burden of business rates for high street, leisure and hospitality businesses by increasing the multiplier on distribution warehouses that support online shopping over time.'
The suggestion is to continue providing business rate relief for the retail sector and to fund it by increasing the cost of business rates for occupiers of distribution warehouses.
But is this needed? The 2023 Ratings Revaluation has already addressed the need for a rebalancing in business rates; the retail sector saw significant declines in Rateable Values, while those for distribution warehouses saw a considerable rise (averaging 32% across the UK).
It's also important to note that not all distribution warehouses are not exclusively used to support online shopping. Retail store networks also require a distribution warehouse, as do suppliers and business-to-business distribution firms. Furthermore, many retail businesses are now omnichannel, selling through brick-and-mortar stores and online. Therefore, it seems misguided to target a specific type of building to support high-street retail.

Getting ahead of the curve

When the Bank of England's Monetary Policy Commission met on the 19th June, they voted to keep the Bank Rate at 5.25%. The decision was reached with a 7-2 majority, with two members voting for a 25bps cut.
Oxford Economics has revised its expectations around the timing of the first cut, which is now expected to come in August, with a total of 50bps cuts anticipated by year-end. However, as of Thursday, 27th June, Overnight Index Swaps suggest September may be the most likely date of the first rate cut, with an interest rate of 4.79% priced in for year-end.
Oxford Economics forecasts a further 100bps cuts in 2025, taking the policy rate to 3.75%. However, markets are pricing in fewer cuts for 2025, with 4.14% priced in for the end of 2025. While the forward curve should not be mistaken for a forecast, markets clearly expect interest rates to remain high for longer.
As interest rates fall, gilt yields are expected to sharpen, making current industrial and logistics real estate yields more attractive (relative to fixed-income investments) for investors. Ten-year government bonds are expected to be 4.03% in Q4 2024, reducing further throughout 2025, to reach 3.71 by Q4 2025 (Oxford Economics). This should boost investment market activity through the second half of 2024 and into 2025.

Higher for longer

The rise in interest rates has reduced the predictability of yields and real estate cash flows. This has upended investor strategies, resulting in a significant slowdown in development and investment transactions.
More active management will be needed to drive returns over the next 5-10 years. The burden of higher interest rates and cost of capital will mean that asset level or local market opportunities will be of heightened importance in generating growth. Assets that offer an opportunity for value-add returns will therefore, prove favourable.
Higher interest rates and inflation will mean that some investors/landlords may reexamine their preference for open-market rent reviews, with leases linked to inflation offering greater income certainty.
An extended high interest rate environment and ongoing inflationary pressures will continue to dampen construction activity into 2025, meaning good quality, new build stock will remain in short supply. Preliminary figures for Q2 indicate that vacancy is still rising, but at a slower pace than in previous quarters. Despite the uptick in vacancy rates in recent quarters, operators face limited options in many locations and across certain, particularly larger size bands.
The higher cost of capital may limit the growth opportunities for less-established companies or nascent sectors, which tend to rely on debt to finance expansion. Higher inflation and financing costs will drive many occupiers to focus on profit growth and managing their cost base rather than expansion. While this likely means that take up volumes will not return to the levels recorded in 2020/2021, it will also mean that companies exercising expansion plans tend to be well-capitalised, meaning greater income security for landlords.

History doesn't repeat itself, but it often rhymes

This market cycle is proving different from previous cycles, and thus challenging to draw parallels. While no two economic cycles are the same, as the American writer Mark Twain said, "history doesn't repeat itself, but it often rhymes".
Returns across all asset classes are unlikely to achieve those of previous cycles, and a smaller performance advantage for real estate over fixed-income gilts is expected.
Annual total returns of over 40% were recorded for UK industrial property in early 2022, far in excess of returns for other property sectors. Though forecast returns are lower than those reached during the previous cycle, they are still significantly higher than other asset classes and other property sectors, with 8.1% CAGR forecast 2024-2028 (RealFor).
Given this positive outlook for returns and the material repricing of logistics assets over the past couple of years, now presents an attractive opportunity to enter the market. Industrial and logistics assets have repriced faster than other sectors and faster than in previous market cycles. Valuations now appear to be stabilised, with the MSCI monthly index recording positive capital growth for the past two months (to May), and the equivalent yield softened by just 2bps in May (the same yield shift in April).

The industrial market has greater resilience than in previous cycles

In previous market cycles, the fortunes of the industrial and logistics sector were tied more closely to the manufacturing sector. While manufacturing remains an important driver of demand, the occupier base has broadened significantly over the past decade due to several factors, including the growth of e-commerce and the associated rise in demand for logistics and home delivery services.
In urban locations, the combined impact of rising urban populations, economic expansion, and increased demand for online retail and home deliveries have had a dual effect: constraining supply whilst increasing demand for industrial and logistics facilities. Much urban industrial land has been lost to housing over the past twenty years. The removal of large swathes of industrial land will mean that vacancy rates; particularly in urban areas; will not rise significantly or to the same levels seen during the previous market cycle.
Urban locations also have a far cleaner and more diverse occupier mix than they used to. Industrial and logistics facilities are increasingly used for courier services as well as offsite service-based activities such as laundry services, catering, coffee bean roasting etc. Alternative uses such as leisure have also sprung up, with climbing centres and trampoline parks occupying warehouse facilities.
Another source of demand stems from the rise in digitalisation. Rising data consumption and increased demand for content streaming platforms have driven demand for data centres and for film studios, which often locate on industrial land or adapt industrial facilities. These additional demand pressures will continue to fuel a demand-supply imbalance for the sector.

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