Retail Renaissance 2025

Knight Frank

Lesson #1: Know your structural drivers

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The first of six papers exploring what other real estate sectors can learn from Retail's fall and unlikely rise again

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Lesson #1: Know your structural drivers

Embrace your sector's structural drivers, or get left behind when the market shifts.

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3 KEY LESSONS:

- Understand your sector's structural and cyclical drivers, or risk being caught off guard when the market inevitably turns.
- No sector or asset is immune. Change is constant and doesn't discriminate. Better to adapt early than deny what is inevitably coming.
- Structural disruption rarely means total collapse. The impact is usually more nuanced, and actually full of opportunity.

It sounds simple, but know what drives your sector. Too often, gaining that understanding gets sidelined by the noise of day-to-day deal-making. But when markets shift, as they inevitably do, a lack of structural awareness can be fatal.

Structural change doesn't arrive with a drumroll. It creeps in quietly, then reshapes everything all at once. Those who misread it, or ignore it entirely, end up reacting to symptoms rather than pre-emptively addressing causes. Retail learned that the hard way.

Online retail is often cast as the main disruptor, and while it has reshaped the sector, it didn't act alone. Retail was already buckling under the weight of at least nine other deeprooted structural flaws (see our 'Price of Change' report for more detail:

oversupply, historic overexpansion, bloated portfolios, rising rents, brand dilution, debt-laden balance sheets, chronic underinvestment, cost inflation, and – perhaps most damaging of all – complacency). Most of these challenges went unrecognised or worse, ignored. Such oversight proved costly.

Real progress only came once the sector and its advisors finally confronted those structural flaws head-on. From that reckoning came renewal, and ultimately, the beginnings of a more sustainable future (or 'Retail Renaissance').

STRUCTURAL VS. CYCLICAL

Structural change rewrites the rules of the game. Driven by forces such as technology, demographics or social shifts, impacts are often irreversible and unlike anything seen in recent history. Think ageing populations, the decoupling of work from place, or the emergence of e-commerce. For an analogy: structural change is akin to climate change, completely resetting the baseline.

Cyclical change, by contrast, is the market's familiar cycle of booms, busts and everything in between. It's what landlords and investors expect to see: demand rises, rents follow and yields compress. Then the cycle turns, and it all goes into reverse. To continue the analogy: these are weather events and seasonal shifts, playing out on top of a changing climate.

The two are not interchangeable, but they do interact. Structural decline can masquerade as cyclical softness. Investors bet on reversion, expecting the old model to return, "Online retail is often cast as the main disruptor, and while it has reshaped the sector, it didn't act alone. Retail was already buckling under the weight of at least nine other deep-rooted structural flaws."

only to discover that the baseline has shifted permanently. Retail was a case in point. Many landlords treated declining rents and rising voids as a temporary dip, and waited for demand to bounce back. It didn't. The model had already broken. Long-brewing structural weaknesses were simply laid bare.

The two forces can also compound each other. Take industrial. Its surge over the past decade driven by many genuine (and largely positive) structural tailwinds: e-commerce, just-in-time logistics, geopolitical risk spurring re-shoring. But structural strength has now met cyclical froth of overheating rents and overly tight yields.

Cycles can also obscure underlying structural shifts. During recoveries, rising tides lift all boats – but if a sector is in structural decline, some boats are sinking regardless. And during downturns, structural winners can get unfairly dragged down with the rest.

KNOW WHAT DRIVES YOUR MARKET

Most advisors claim to understand their sector's fundamentals. Few do in practice. Market knowledge often stops at the surface of rental levels, investment yields and take up. But true understanding means grappling with the structural mechanics underneath.

The ten structural issues we identified in 'The Price of Change' report were not obscure. Many were hiding in plain sight. But they were either dismissed as temporary, or, worse, deemed someone else's problem.

Those advising clients need to interrogate their sectors more rigorously. Are trends cyclical or structural? If the latter, what are their origins? Can they be mitigated, or should they be embraced? Failing to ask these questions leads to poor advice, and ultimately, capital misallocation. Hubris is also dangerous. Just because a sector is buoyant now doesn't make it immune. Office landlords may have once scoffed at retail's downfall. Now, they're having their own reckoning.

INDUSTRIAL - FROM DARLING TO DISRUPTED?

Industrial has been on a winning streak, benefiting from structural tailwinds that others envy. But the only constant is change, and change can be a double-edged sword. Take advances in autonomous vehicle technology. If logistics no longer require human drivers, 24/7 operations could soon become viable. Time constraints that once favoured centralised UK hub strongholds like the Midlands' Golden Triangle could be jeopardised, suddenly finding themselves oversupplied as demand shifts towards peripheral, lower-cost locations. Why pay a premium for centrality when the lorry ticker tape isn't watching anymore?

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A 'doomsday scenario'? Perhaps. But it's not entirely implausible. No sector is immune to its own structural shake-up, but it can build its defences. Vigilance, rather than dismissal of possible risk, is critical.

ONLINE RETAIL - THE MISUNDERSTOOD DISRUPTER?

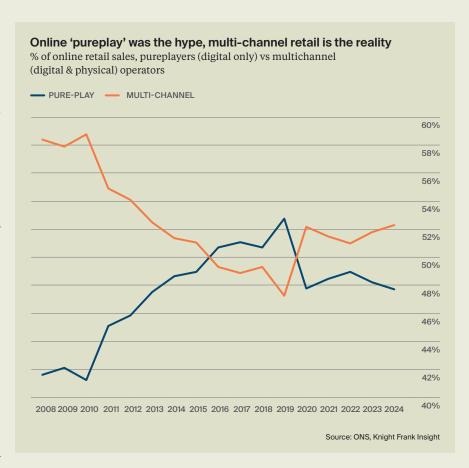
Structural change is rarely as straightforward as it first appears. E-commerce was never about replacing stores wholesale, it was about redefining their purpose. But initially, rising online penetration triggered panic. Investors feared a retail apocalypse, with stores rendered obsolete. Many retailers fed that narrative, diverting investment from physical formats and piling capital into online infrastructure. The digital 'space race' became the new holy grail, but that enthusiasm came at a cost. Online platforms were expensive to build, often low-margin, and during COVID, artificially inflated.

Online's share of retail spiked from 19.2% in 2019 to 37.8% in early 2021. Pureplay operators (those without a physical store) accounted for over

half (52.7%) of online retail sales, up from 41.1% a decade earlier. Triggering a wave of wildly optimistic extrapolations predicting online would account for 50% of all retail sales within years.

The reality proved more complex and more nuanced. Rather than replacing physical retail, online forced it to evolve. Not all retailers gave way to digital forces. Primark, Aldi and Lidl became standout examples of businesses that don't translate easily to the online model, yet continued to thrive.

The market began to recognise that stores and online weren't adversaries, they were symbiotic. One could succeed while the other grew. In many cases, they performed better together. Stores became essential cogs in a new multi-channel ecosystem, prompting fresh investment into bricks and mortar. From 2020 onwards, multi-channel retailers (those with both physical and digital presences) have consistently dominated online sales, accounting for an average 52% of the market versus 48% for pureplayers. But with that came a sharper edge.



Underperforming stores were cut with little hesitation as their contribution was scrutinised more closely than ever.

Online fundamentally reset the way store performance was measured. The question was no longer just about in-store sales, but about the broader 'halo effect' – how a store's presence boosted brand awareness and drove online transactions in the surrounding area. That shift helped rekindle appreciation for the role of physical space, not as a legacy cost, but as a strategic asset.

The market is now, arguably, out the other end of the tunnel. Online has matured, effectively treading water at 26% to 27% of total retail sales across 2024 and 2025. It no longer carries the existential threat it once seemed to pose. The frenzy has cooled. After its own 'bonfire of vanities', the market has come to accept that there's still a place for bricks and mortar – though only for space that's better, leaner and more relevant.

Next's CEO Lord Wolfson captured this shift in the company's March

2025 trading statement: "the worst of the retail-to-online structural shift [appears] to be behind us". For the first time in over five years, the retailer plans to increase its physical trading space by +0.4% this year. A small move maybe, but a highly symbolic one.

OFFICES - FACING THEIR OWN 'ONLINE MOMENT'?

Offices are starting to learn similar lessons: you can't pretend remote work isn't happening. But once you stop pretending, you can have a more nuanced, and frankly, grown-up, conversation about what it really means for the market.

The sector is now drawing its own conclusions from its structural disruptor (working from home). There's growing acceptance that the genie is out of the bottle, and it's not going back in. Instead of resisting change, the office market is beginning to adapt. Our 'YourSpace' research is tracking that shift in real time, moving past lazy assumptions about the 'death of the office' to uncover what

is actually happening and where the opportunities lie.

Five years on from the COVID-triggered 'great global workplace experiment', the tone has changed. Early fears of 'will anyone come back?' gave way to office-worker 'FOMO' (fear of missing out) once restrictions lifted. That's since evolved into 'FOBO' (fear of becoming obsolete) as AI accelerates, fuelling employee concerns about falling behind and losing relevance in a changing workplace.

While the disruption has been painful, it hasn't been directionless. It has forced the sector to confront uncomfortable truths, and in doing so, offered a loose blueprint for the future. One where floorspace has to earn the commute. Where buildings need to offer something the kitchen table can't. Where offices are shrinking overall, but becoming more purposeful, more intentional. More relevant, even.

Sound familiar? It should. Retail got there first.

THE AGENT VIEW

"Early fears of structural change now look overstated"

Sam Waterworth - Partner, Retail Capital Markets



"To say retail is 'back in fashion' might be an overstatement, but the market has come a long way from the wave of CVAs in the late 2010s, and the enforced closures of the pandemic. At the time, it felt like structural change had upended everything. Estimating rental values became guesswork, and the assumption was often that tenants would exit at lease expiry.

Today, the picture looks very different. In core towns, rents have

stabilised and there are now signs of modest growth. That comes off the back of significant rental rebasing – a painful but ultimately necessary adjustment. What we're now seeing is a more deliberate, selective approach from retailers. They're not chasing scale, but many are investing into stronger, more profitable markets. M&S's relocations to modern space in Liverpool, Bath, Bristol and Leeds are a good example. John Lewis, too, is back in investment mode. These aren't signs of a sector in retreat, they're signs of one redefining itself.

Yields remain elevated but are trending downward across all retail subsectors. On the High Street, prime yields sit at around 6.50%, compared with 4.00% in 2017. When you factor in rebased rents, capital values can

be less than half of their peak.
That repricing has started to bring investors back, especially in locations where the fundamentals are clearer.

Some of the early fears about structural change being terminal now look overstated. What we're seeing is a cyclical recovery playing out. Not everywhere, and not for every asset, but certainly in well-located, well-let stock. We recently advised on the successful (and profitable!) resale of a prime regional city High Street asset, bought just 18 months earlier. A strong result, and a reminder that in sectors that have already absorbed major structural change, opportunities do still exist. That might be a useful reference point for those navigating today's disruption in the office market."

We like questions, if you've got one about our research, or would like some property advice, we would love to hear from you.



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