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Joining the Dots...

Scottish Investment Market Quarterly Review: Q2 2025

Consistency of performance can be the most powerful differentiator of all...!

A quote most often used in a sporting context but one that can be just as relevant in the world of real estate. With so much uncertainty and volatility in recent times, investors are constantly looking for sectors that are delivering consistent performance.

Of the commercial sectors in Scotland, the Logistics sector has been one of the strongest (consistent) performers — a combination of healthy demand and virtually no supply has driven rental growth, along with some depth to the buyer pool (UK Funds, amongst others, are back investing in Scotland) has made for a compelling case.

As with most other regions in the UK, cost inflation has made speculative development particularly challenging. Tenants looking for new space are having to accept significantly higher rents and the drip down effect is helping to drive rents in slightly older stock. A good number of investors are happy to acquire this kind of stock with shorter leases (and potential void risk) on the assumption that capex is not significant and they will capture performance through re-letting at higher rents. With the Scottish market not subject to the constraints of the '54 L&T Act, it should place Landlords in a stronger position and make this kind of investment rationale even more compelling.

With this backdrop, in addition to our wider market analysis, our focus in this review will be looking at the Logistics market. How are investors perceiving their exposure to the sector, what is likely to happen to pricing in the foreseeable future and what drives investment decisions in the sector. To help form our view, we are pleased to include a guest contribution from Valentine Beresford and Hugh Chivers at LondonMetric Property Plc.

Taking consistency in a sporting context, as fans of Scottish rugby and football, this is term that is pretty alien to us...(unfortunately).

Market overview.

Key themes

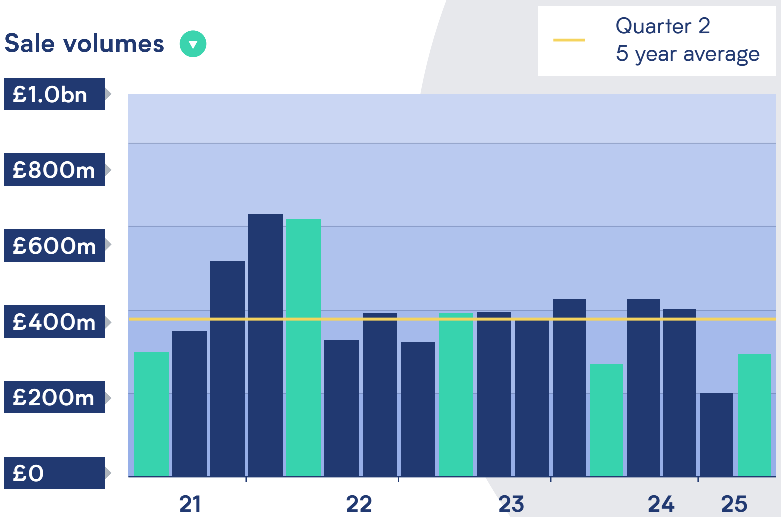
- **Glasgow offices** — after a particularly quiet start to 2025, there are currently 5 deals under offer, which should improve the volume stats and give some impetus to the market going into H2. While still trading at a particularly attractive discount to historic levels, the buyer pool seems to be deepening, as investors see value in fundamentally good buildings without the requirement for significant capex.
- **PBSA hiatus** — the potential inclusion of PBSA rent controls and 28-day notice periods in the draft Housing Bill has been met with dis-belief and frustration within the sector. Although most interested parties remain hopeful that the proposed amendments will be significantly watered down (or removed) to ensure an "investable" outcome, the knee-jerk inclusion has not helped liquidity and confidence in the sector.
- **Allez les bleus (toujeurs)** — the flurry of deals that we have seen being completed with the French SCPI's has continued. The slight nuance being that, in addition to targeting stock in the central belt, they are now turning their attention to assets in Aberdeen. Good buildings with strong covenants (and yields at 8%+) are proving attractive and a welcome addition to the active investors in the city.
- **Income rather than capital growth** — rental growth is being seen in some sectors (logistics, prime offices/retail and roadside) and with income expected to be the driver for returns over the next 6-12 months, it will be those investors focusing on asset management who are likely to see best performance.
- **Size isn't everything** — not what most agents want to hear but one of the most liquid parts of the market remains sub £10m. Private buyers with limited or no debt requirements are seeing the current market as ripe for picking up core plus assets, properly priced. We are seeing activity from a range of investors including, the UK, North America and the GCC.

Transaction volumes

Q2 saw £296m traded up 9% on Q2 2024

Q2 volumes were 21% below the 5 year average

Q2 2025 Number of deals was 18



Our view.

- At face value, transaction volumes in Q2 appear relatively healthy, representing a modest increase of 9% against Q2 2024. However, delving into the numbers tells a somewhat different story, with two transactions representing 48% of the market in Q2. Were we to remove W Hotel and St Enoch Shopping Centre from our figures, total transactions would be down 48% against Q2 2024 representing a truer to life story of what has been another fairly slow quarter. With several significant transactions anticipated to complete in the coming quarter, we expect a notable uplift in transaction volumes across H2 2025.
- Edinburgh's hotel sector has been a shining light over the last few years, with operators competing with office specialists for redevelopment opportunities, resulting in over 200,000 sqft of prime office stock acquired for hotel conversion. With strong tourism and corporate demand, Edinburgh's impressive occupancy rate (85%) and RevPAR growth (+10% year on year) is sustaining activity, however redevelopment opportunities may be less prevalent going forward. Optimism in the sector was underscored in Q2 by Schroders' c.£100m acquisition of the W Hotel — a standout asset in the city — marking a successful exit for Nuveen.
- In the retail sector, prime high street remains compelling, with strong rental growth now being evidenced. Whilst George Street and Buchanan Street dominate investor focus, the case for the best surrounding streets, such as Princes Street and Argyle Street, is getting stronger. Constrained supply and an improving retail outlook, along with ongoing redevelopment, is leading to an increased focus on the best pitches of Princes Street and Argyle Street.
- The UK's macroeconomic outlook in mid 2025 remains cautiously optimistic, underpinned by cooling inflation, a stabilising labour market, and the Bank of England's gradual pivot towards rate cuts. Whilst the Monetary Policy Committee held the base rate at 4.25% in June, the direction of travel is expected to see further cuts in H2 2025. Whilst perhaps not moving the dial dramatically for investors this year, more attractive debt terms on the horizon give cause for optimism.

Key recent transactions.

Q2 saw some interesting themes and significant transactions which we have highlighted below:

W Hotel, St James Quarter, Edinburgh

"Landmark Edinburgh hotel trades"

- **Vendor:** Nuveen
- **Purchaser:** Schroders
- **Let to:** Marriott Hotels
- **Price:** c£100m
- **Date:** April 2025

St Enoch Shopping Centre, Glasgow

"Value add investor acquires centre for asset management"

- **Vendor:** Sovereign Centros
- **Purchaser:** Praxis
- **Let to:** Multi let
- **Price/Yield:** £54.4m / c12%
- **Date:** May 2025

Staycity West End, Edinburgh

"Aparthotel acquired by Allianz"

- **Vendor:** Associated British Foods
- **Purchaser:** DTZIM
- **Let to:** Stayedinburgh
- **Price/Yield:** £12m / 5.90%
- **Date:** June 2025

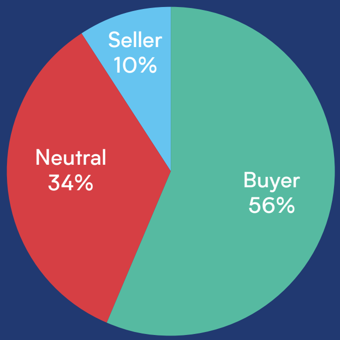
Beaverbank Place, Edinburgh & Firhill Court, Glasgow

"Two PBSA assets snapped up"

- **Vendor:** Mapletree
- **Purchaser:** CVC DIF
- **Let to:** Direct let
- **Price/Yield:** £55m/ 6.00%
- **Date:** April 2025

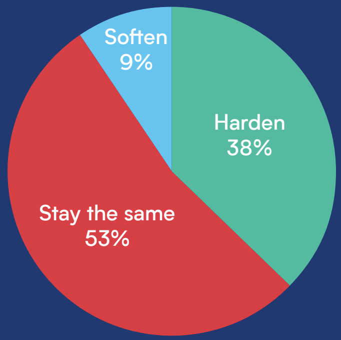
The Investor View on the logistics sector in Scotland...

1) Do you expect to be a net buyer, seller or neutral on logistics over the next 6 months/H2 2025?



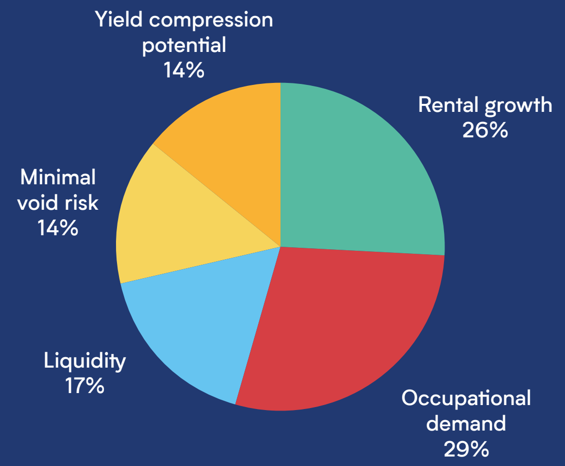
- Investor sentiment towards logistics remains broadly positive, with 56% of respondents indicating they expect to be net buyers over the coming six months. Only a small minority – just 10% – anticipate being net sellers, while 34% expect to remain neutral.
- This outlook is most pronounced among institutional funds, where 71% identified as net buyers, followed by investment managers at 53%. Only 7% of investment managers surveyed said they would be sellers – the lowest percentage among all respondent groups.
- Several respondents noted that while they expect to be acquisitive, this will depend on suitable opportunities becoming available. A number of responses highlighted the limited supply of good quality stock currently on the market as a factor influencing activity. While the appetite for logistics assets remains clear, availability of investable product may constrain transactional volumes in the near term.

2) Do you expect the prime logistics yield to harden, stay the same or soften?



- Responses to this question suggest a market edging toward stability, with 53% of investors expecting prime logistics yields to remain unchanged in the second half of 2025. This suggests that some of the volatility observed earlier in the year, driven by fluctuating gilt rates and international trade concerns such as US tariff announcements, may have settled.
- Notably, 38% of respondents anticipate yield hardening, with some responses highlighting the expectations of interest rate cuts later in the year.
- Among investor types, propcos were the most bullish, with 60% predicting yields would harden. Conversely, funds and investment managers showed a more cautious stance, with 86% and 60% respectively expecting yields to hold steady.

3) What do you believe are the most important drivers for logistics investment?



- Occupational demand was identified as the top driver for logistics investment, selected by 29% of respondents. This was closely followed by rental growth at 26%, suggesting that income performance remains a key focus. Liquidity (17%), minimal void risk (14%), and potential for yield compression (14%) were also cited as important factors.
- Among funds, minimal void risk was ranked ahead of liquidity, which may reflect differing priorities across investor types.
- In addition to the multiple-choice responses, several participants highlighted other factors, such as the volume of recently raised capital looking for deployment, and a view that logistics offers relative sector stability. Other themes mentioned included low obsolescence costs, a lack of new build supply, and the presence of US private equity activity.

“Expert view” on logistics...

Valentine Beresford

Investment Director
LondonMetric Property Plc

Hugh Chivers

Investment Executive
LondonMetric Property Plc

Logistics has been one of your favoured sectors for some time, why is this, and do you see any headwinds for the sector right now?

Logistics is the sector we like, for the tailwinds, as much as anything. We see strong growth drivers and solid demand. Supply is fundamentally constrained by land requirements, the planning system, construction costs, and build times – pressures that are tightening. At the same time, obsolescence is rising, and new occupiers want purpose-built facilities, meaning a long tail of secondary or tertiary space is becoming unfit for many users. We like all these factors.

There are always headwinds, right? The rising cost of debt has been a significant challenge in recent times but that is not just an industrial issue, it's a property issue. The biggest headwind right now is the shortage of investable assets. Stock is scarce, and when it does come up, there is competition from a range of investors, particularly the PE platforms.

Tariffs are another factor. Global trade barriers can be disruptive, though they also provide opportunities through onshoring and stockpiling. We've seen benefits from Freeports, like our site outside Felixstowe, where bonded status allows goods to be imported and stored without immediate tax.

So, while it's something to be mindful of, there are also opportunities in the tariff structure. That said, you can't plan around tariffs – especially with the unpredictability we've seen under Trump.

From your perspective, what is the key driver investors prioritise when evaluating a new opportunity?

Our criteria focuses on four key factors: building quality, location, lease length, and tenant credit. If at least three out of these four requirements are strong, we will likely review it.

But we won't pursue an asset just because it's an exceptional building if the other fundamentals don't stack up. Our priority is delivering an accretive income return to support dividend payments and enable progressive growth.

Expiring income gaps are a major issue for us, far more than for those using a total return model. Lease length and tenant strength are critical. We may even invest in weaker locations or lower-quality buildings if there's a long lease with strong credit.

Things become a little more complex when evaluating brand-new, high-quality urban logistics assets in an excellent location. In such cases, we may take a calculated view.

Do you expect recent strong rental growth to continue, and if so, what factors are driving it?

Rental growth has slowed at a macro level, but there are still pockets of strong growth driven by supply-demand imbalances in specific areas. Finding the right opportunities now simply requires careful selection of submarkets and asset types.

Rental growth across the industrial sector has slowed to around 2-3% annually. Brand new Grade A stock is seeing much stronger growth; however, it's the older secondary stock that is lagging – creating one of the widest rental gaps between prime and secondary assets.

There is growing alignment between occupiers and investors in targeting high-quality, prime assets, underpinned by common ESG and net-zero commitments.

The strongest rental growth is in pre-let, D&B space. Large bespoke requirements can't be met with off-the-shelf options; these facilities must be purpose-built. Developers, having been hit by land value erosion and yield compression, are recouping losses through the only means possible: pushing higher rents.

How much is the ESG agenda driving more frequent refurbishments? Is it raising specification standards in older properties, and are investors having to factor in higher CapEx as a result?

For older stock, a key issue is accurately assessing CapEx requirements. Historically, investors underestimated these costs relative to current cash flow modelling. This underestimation has led some to adopt more robust acquisition due diligence processes to better evaluate potential future CapEx exposure.

For older buildings, like those from the 1970s with asbestos roofs, refurbishment is often a one-time investment. Once the roof is replaced, the EPC improved and LED lighting installed, there's little left to upgrade. Unlike offices, which often require major upgrades every decade, once modernised, industrial buildings tend to stay functional for years – it's not like painting the Forth Bridge and having to start over every few years!

A challenge has been the gap between rent growth and CapEx investment. With rents rising regardless of upgrades, many landlords have avoided disrupting that cycle – strong demand has allowed this, but it can't last forever.

With potential interest rate cuts forecast later in 2025, how do you see this impacting investor appetite and pricing expectations?

Capital is available, and there's significant demand in the logistics space. The key difference is that buyers could likely absorb slightly higher pricing as interest rates adjust – rates come down, margins remain steady, and pricing naturally follows suit – that's just basic financial mechanics. The real issue is liquidity on the vendor side. Sellers need to see interest rates stabilise before their pricing expectations align with market realities, right now, that mismatch is creating a roadblock.

Ultimately, as interest rates shift, pricing will likely settle at a level more acceptable to vendors, helping to break the current deadlock.

With the Landlord & Tenant '54 Act not applying in Scotland, does this have a meaningful impact on investing in Scotland, particularly for shorter lease opportunities?

Absolutely, it should – but we tend to be cautious investors, particularly around potential income gaps. We rarely let an asset reach the end of a lease without securing an extension, as the risk of vacancy is unsettling for us.

Typically, we renew leases early, removing the need for Section 54 protection across our portfolio. Where early renewal isn't possible, we aim to sell with sufficient lease term remaining to maintain liquidity. In recent years, sub-five-year lease terms have worked well, giving buyers greater access to rental reversion.

Some investors take the opposite view: allowing leases to run close to expiry, staring down tenants, then negotiating to extract maximum reversion. We don't have that luxury, with portfolio occupancy at 99.9%, even a 2% vacancy would materially impact earnings. That's why minimising lease gaps is critical to our model.

So, while we are now more comfortable investing in Scotland, the lack of the '54 Act is not the primary driver for stock selection.

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