THE CHANNEL ISLANDS OFFICE MARKET REVIEW 2025

D2 REAL ESTATE

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D2 REAL ESTATE THE CHANNEL ISLANDS OFFICE MARKET REVIEW **2025**

FOREWORD

2024 has been a good year for us here in the Channel Islands, and my hopes for 2025 are high. While unresolved geopolitical storylines may yet invite further economic turbulence, perhaps I have simply accepted this new normal, and grown 'comfortable being uncomfortable'. Regardless, there is growing evidence we are in much better shape than a year ago.

Commercial property is cyclical, making buying at the bottom and selling at the top a logical investment rationale. There has been much speculation this year of whether the UK market has reached the bottom. In the Channel Islands I am confident that we did so in 2023, with 2024 bringing clear evidence of yield compression for lot sizes below £20m and, in certain cases, competitive tension from several investors. I therefore believe the Channel Islands' cycle has drawn us into recovery slightly ahead of the UK market.

This investment demand has largely been driven by the compelling rental growth story that is underway, particularly in Jersey where we expect to see double digit growth coming through. Gaining clarity on this will require patience, as letting transactions are taking a significant time to complete, and thus to create a new rental benchmark. This issue is common to all jurisdictions. With a lack of economic certainty, it is a big commitment for an occupier, and the building has to be the right fit and worth the cost to invest in their fit outs. Build cost is another theme we will examine in this report.

And then of course, there are interest rates. Their impact on the sector has been profound, particularly for the larger lot sizes and where there are limited asset management opportunities. Once again, this year compares favourably to last. With two rate cuts in 2024, and narrowly missing out on a third, the expectation is for more of the same, hopefully reaching 3.75% by this time next year. That will again help the larger assets, and looking at the data yields are not far off where we were in 2008. As commercial property can bounce back quickly, I do see this period as a buying opportunity.

This is where professional guidance can prove decisive, as stock selection is crucial. In the UK some have discussed a 'K' shaped recovery, where the coveted 'best in class' assets perform, and those outside this bracket continue a downward trajectory. This is perhaps even more relevant in the Channel Islands. The market is small, each building's history can be established with a few calls, and people will know the occupiers, making asset selection a near-forensic process. As always, having a well-managed building is essential, and ensuring the phrase 'ready for sale' is not just a 'buzz word' will pay dividends when it comes to pricing.

PHIL DAWES
Managing Director | D2 Real Estate

"I THEREFORE BELIEVE THE CHANNEL ISLANDS' CYCLE HAS DRIVEN US INTO RECOVERY SLIGHTLY AHEAD OF THE UK MARKET"

LAST YEAR'S PREDICTIONS

With so much uncertainty, and several interdependent narratives shaping the global economy, forecasting has rarely been more challenging. However, looking back can provide some useful context and identify areas for further discussion.

2024 PROJECTIONS	**THE REALITY OF 2024**
2023 and 2024 to emerge as good times to have acquired stock.	**It's fair to conclude that the market bottomed out in 2023 and 2024. Evidence that some 2023 acquisitions are achieving 15%+ returns, due to rental growth and yield compression.**
Market Interest Rate Expectations: June 2024 **5%**; September 2024 **4.75%**; December 2024 **4.25%**	**Close. After 11 months on track, that final rate cut didn't materialize.**
'Anticipate muted GDP growth, a tapering of inflation, and a lowering of interest rates in 2024 triggering a potential recovery in commercial property values.'	**1% GDP growth in 2024. Inflation has fallen and values have bottomed out, with yield compression in the Channel Islands.**
'Could rents in Jersey achieve £50psf? ... tight supply etc. mean that answer could be 'yes''	**Whilst £50 psf proved optimistic, supply remained limited, and enquiries were strong. Evidence suggests rents in some second generation buildings will rise by more than 35% over a 12-month period.**
'New legislation that will be drafted in 2024 seeks to increase clarity around EPC's.'	**A Jersey Government U-turn meant the relevant legislation will not be adopted during the current term. However, EPC's are coming, with investors and banks already reacting.**

"EVIDENCE SUGGESTS THAT SOME 2023 ACQUISITIONS ARE ACHIEVING 15%+ RETURNS."

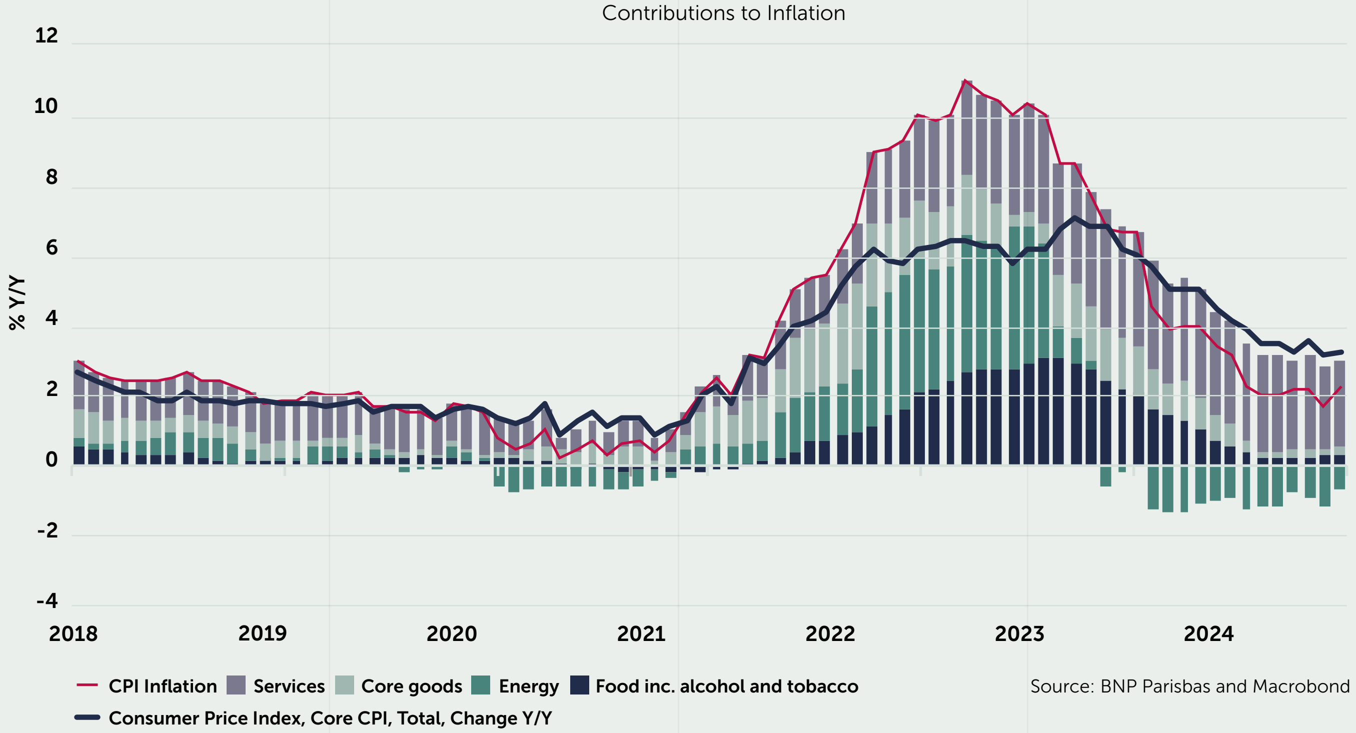
ECONOMIC OVERVIEW

If the 20's have taught us anything, it is that stability is a relative concept. However, after the extraordinary events of recent years, 2024's encouraging GDP and inflation data both suggest that a recovery is finally underway. Andrew Bailey's recent hint that a base rate of 3.75% may be within reach by the end of 2025 also bodes well for the property market.

The picture, though, has been nuanced. Labour's historic landslide in July did little to boost business confidence and investment, despite August's interest rate cut. The subsequent Reeves budget in October pulled few punches, ushering in over £40bn in tax changes and positioning itself as the necessarily tough medicine that Britain must swallow. Growth in public borrowing has already led to increased gilt yields which in turn have impacted property yields, albeit these are a blip compared to the fallout from Liz Truss' mini budget of 2022.

Adding further to the need to temper optimism with caution, the combined effects of the higher cost base for businesses arising from Employer National Insurance changes and the increased minimum wage, plus the extent of promised public investment, may all impact inflation in 2025.

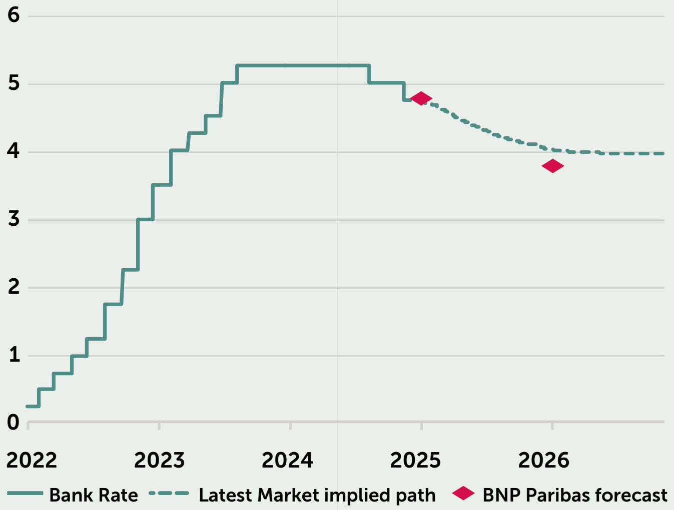
INFLATION



Source: BNP Parisbas and Macrobond

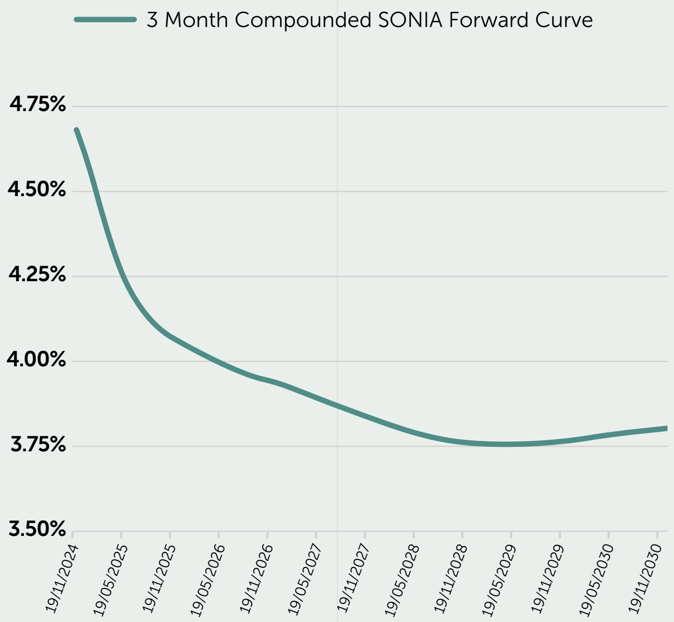
Further afield, the second Trump term is likely to re-shape foreign, fiscal and trade policy, all of which could exacerbate inflation risk. However, while many believe the Trump administration is more likely to target net exporters as opposed to countries like the UK where trade in goods with the US is broadly balanced, the President elect is nothing if not difficult to second-guess.

RECENT INTEREST RATE HISTORY & MARKET IMPLIED FORECAST



Source: BNP Paribas & Macrobond

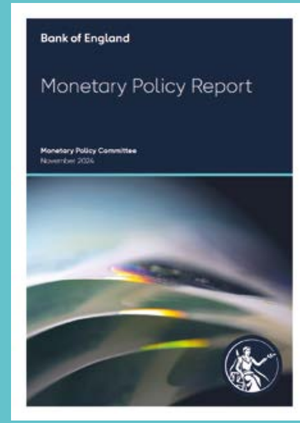
3-MONTH SONIA COMPOUNDED FORWARD CURVE



Source: Chatham Financial (Jan 2025)

Reflecting on 12 months ago, we are unquestionably in a better place. With greater political certainty (in increasingly sharp contrast to leading Eurozone nations), there is growing likelihood of a gradual increase in business and investor confidence, and a return to sustainable economic growth.

FROM THE BANK OF ENGLAND'S MONETARY POLICY REPORT – NOVEMBER 2024:



We have cut interest rates to 4.75%

2%

Inflation is close to the 2% target and we've been able to cut interest rates again

We need to ensure inflation stays low. So we will not cut rates too quickly or too much

If things evolve as expected, it's likely that interest rates will continue to fall gradually

KEY STATS 2024

4.75%
Base rate Jan 2025 v's **5.25%** Jan 2024 (Bank of England)

2.5%
CPI Dec 2024 v's **4%** Dec 2023 (ONS)

4.54%
UK 10-year Gilt rate Dec 2024 v's **3.97%** Dec 2023 (FT)

“REFLECTING ON 12 MONTHS AGO, WE ARE UNQUESTIONABLY IN A BETTER PLACE”

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1%
UK GDP growth Q4 2023 to Q4 2024 (ONS)

3.75%
Base Rate Prediction December 2025 (BNP Paribas Real Estate)

SONIA Forward Curves:
Jan 2025 **4.66%**
Jan 2026 **3.85%**
Jan 2027 **3.65%**
(Chatham Financial)

UK INVESTMENT OVERVIEW

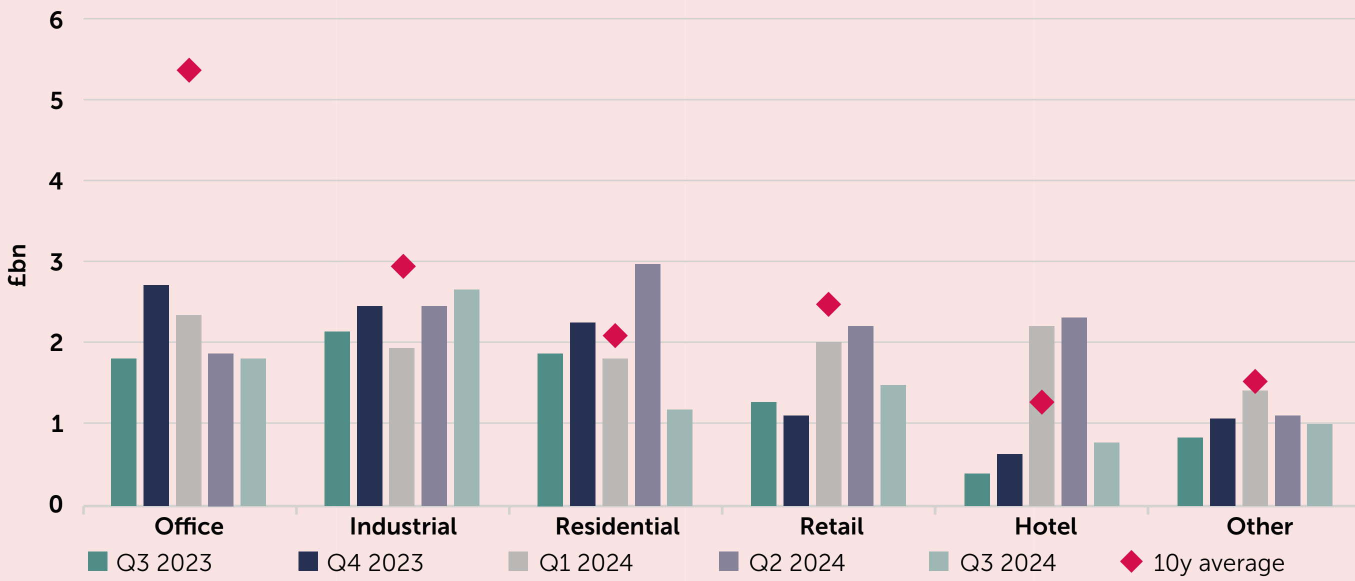
The global economy remains beset by a breadth of geopolitical issues, which have contributed to reduced investment volumes across all sectors of commercial property over the last two years. However commercial property not only has a well-established cyclical pattern, but it is often one of the first to benefit when wider economic fortunes improve.

A critical insight here is that the recent downturn has been caused not by an oversupply that has prompted lower occupancy, but by an interest rate spike which now appears to be reversing. With very little recent development across the sector, and few signs of this changing in the short term, high-quality stock remains limited, and demand strong. At the same time occupiers are increasingly prioritising the quality of the working environment, with those looking to expand facing limited options. Many believe this imbalance of occupational demand and supply may deliver one of the market's stronger performances over the next five years. Indeed, take up rose by 25% from 2023 to 2024 in the Big 6 cities.

Occupational Take Up Big 6	Total
2023 Total	**3,673,400**
2024 Total	**4,591,600 (25%)**
5-year average	**+13%**

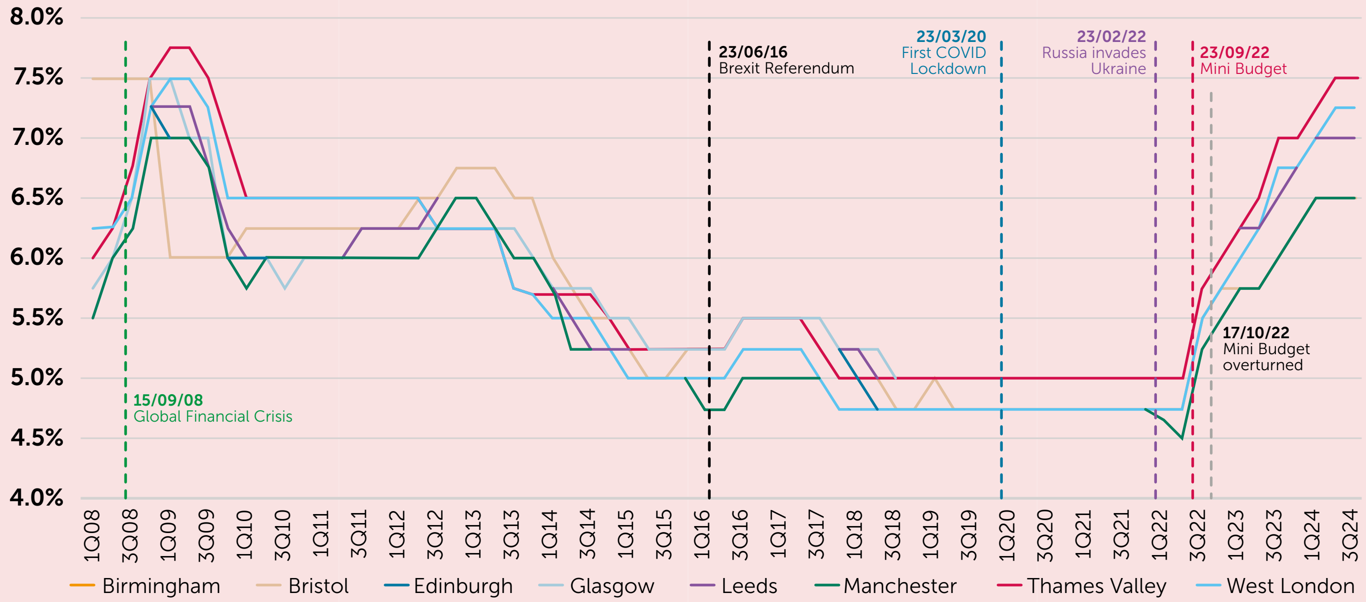
Source: 2025 Jones Lang LaSalle IP, Inc

QUARTERLY CRE INVESTMENT VOLUME BY SECTOR



BNP Paribas Real Estate, MSCI, data as at 22.10.2024

PRIME YIELDS



*Assuming a 15 year income and OMR

This in turn has propelled significant rental growth, for example Bristol is nearing £50 psf versus 2014's £28 psf benchmark. This rental growth has come at a time when yields are at their most attractive since 2008's financial crisis. The likelihood of yield compression is therefore very real, as rental growth drives market confidence, and investor competition for the most attractive assets intensifies.

Note that here we are referring to 'best in class' buildings, with less attractive assets destined to continue to decline, with a rising risk of obsolescence. We may see 'K' shaped property recovery, and a sharply bifurcated marketplace.

Another positive is that the rate cutting cycle is now underway, creating conditions for more larger lot sized transactions. The recent dearth of activity has naturally suppressed total investment volumes. Indeed, EQ Bristol - an office we have tracked for many years - has reportedly been sold to Melford Capital for circa £100m becoming the largest regional office sale to complete in the past few years. We have also seen increased activity in London, a trend we expect will continue as interest rates fall, shoring up investor confidence and investment volumes.

Where are UK prime office yields?

As with many 2023/4 themes, reduced investment volumes make it hard to tell. However, a well-located 'best in class' building, at lot size of up to £50m, let on a long lease (say 10 year+) might achieve a yield in the order of 6.5%

THE MINT, EDINBURGH

Acquired by Pontegadea, a Spanish cash buyer seeking a solid income return from one of Edinburgh's best buildings.

- 70,476 sq ft
- Prime office & ground floor leisure
- Completed in 2019
- WAULT 10.2 years to break and 11.7 years to expiry
- Fully electric
- Lot size £42.5m
- NIY blended 5.78% / 6.96% reversionary given imminent rent review

EQ, BRISTOL

- 194,426 sq ft
- Prime location and one of the best buildings in the UK regions
- Completed in 2023
- WAULT 8.9 years to break and 10 years to expiry
- EPC A / BREEAM Outstanding
- 17,000 sq ft dedicated to amenity – café, 509 seater auditorium, roof terrace, 32 showers etc.
- Fully electric
- Lot size circa £100m / 7.25%

One of the largest transactions to complete in 2024. The property was launched in early 2024 at £116,000,000 and a net initial yield of 6.35%.

Quantum has impacted pricing and whilst the price is confidential, we believe the yield reflected over 7%. As the debt market recovers and investor confidence returns, the coming years could reveal it to be an inspired purchase.

THE CHANNEL ISLANDS INVESTMENT MARKET

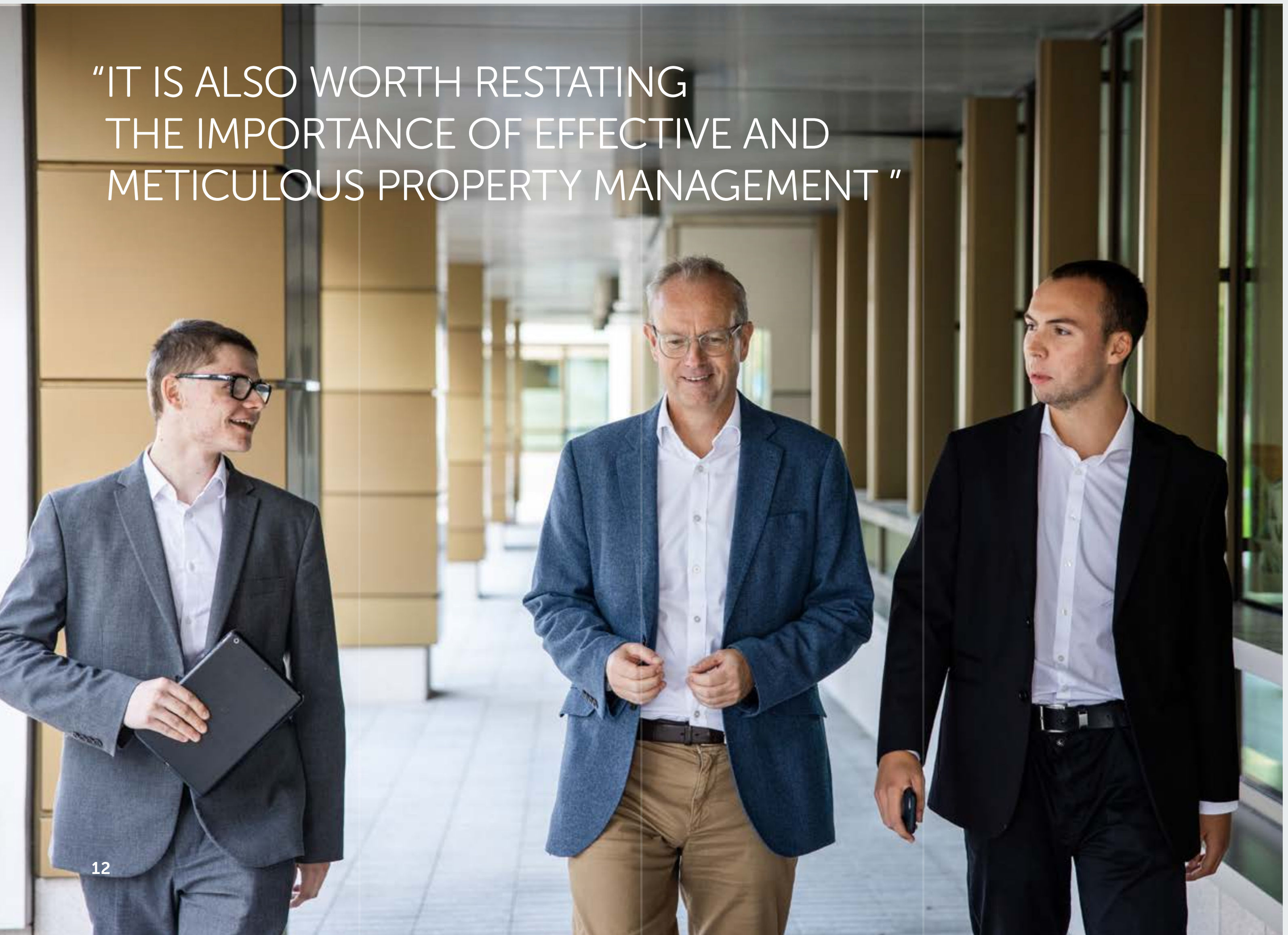
While many believe 2024 to be the year the UK market bottomed out, we believe that the Channel Islands reached that point in 2023, and has since been recovering. Yield compression and rising prices are evident, particularly in lot sizes of below £20m. As in the UK the data volume is limited, however the signs are very encouraging.

Unsurprisingly, investors have typically had a strong knowledge of the local market, and are generally syndicates or high value residents (HVR). They understand where to invest and where occupiers want to be.

We will analyse the occupational market later in this report, but it is telling that this has influenced the investment market. With occupiers having 'right sized' now looking for new space in a market offering limited opportunities, landlords with large floor plates in older buildings who are in a position to invest and refurbish, are well positioned. The chances of securing a strong covenant on a long lease, say of 15 years with no breaks, is very real. It is also worth restating the importance of effective and meticulous property management. 'Ready for sale' should mean just that, backed up with relevant data and strategy to satisfy a diligent buyer.

50 / 100 BPS YIELD SHIFT? – THE EVIDENCE

Comparing 2023 and 2024 suggests a yield shift of 50 – 100 basis points. The transactions opposite are comparable in investment profile and location. They evidence clear yield compression, indicating values have risen by around 5% - 10% since mid-2023.



13-15 CASTLE STREET

- Sold: **April 2023**
- Price: **£14.53m**
- Yield: **8.33%** (purchaser's costs 6.5%)
- WAULT: **4.64 years to break**

CHARTER PLACE, SEATON PLACE

- Sold: **December 2024**
- Price: **£12.5m**
- Yield: **7.81%** (purchaser's costs 6.5%)
- WAULT: **8.3 years to expiry**
- Context: there were two parties bidding on this asset

1 SEATON PLACE

- Sold: **November 2024**
- Price: **£6.625m**
- Yield: **7.75%** (purchaser's costs 6%)
- WAULT: **3.4 years to expiry**

Each of the above had asset management angles to varying degrees and initial yields were all above 'all in' cost of debt. What hasn't been truly tested in the Channel Islands is a large, prime building let on long leases, where debt and interest rates can significantly influence performance and annual return on equity. If a prime building were marketed now, it may be too soon to move the yield from 6.5%, but that may occur as interest rates fall. For prime assets we believe the yield would match the UK and for second generation buildings, we believe there would be a Channel Islands premium.

COUNTING THE COST

Before exploring the occupational market, it is worth considering the symbiotic relationship between the construction sector and commercial real estate markets, and how this influences rents.

The challenges facing construction are well documented, with developers reluctant to commit to new builds or refurbishments without strong confidence in a quick and healthy return. The persistent skilled labour shortage also shows little sign of abating, posing significant industry risks as analysts warn of constrained future output and upward pressures on wages to meet any increased demand. This could undermine project efficiency and create delays through lower productivity.

Additionally, the improving but still compromised global supply chain, plus an uncertain economic environment, continue to drive increased build costs. The Q3 BCIS Forecast suggested a further rise of 15% over the next five years and tender prices potentially rising 20% over the same period.

The Channel Islands is arguably more exposed than most to these headwinds. As our previous reports have highlighted, build cost inflation has been consistently steeper than in the UK, with shipping costs and supply chain delays having a disproportionate impact. The situation is further compounded by a more limited local labour force, the risks associated with a reduced pool of larger-scale projects, and the widely acknowledged planning system deficiencies.

With a number of business failures, the pool of larger contractors has continued to reduce, particularly in Jersey, raising concerns over both deliverability and the need for adequate competition in restraining costs.

We stated in our 2024 report, the viability of any major new developments could only be opened up by a significant step change in rental levels which is not inconceivable given the focus of some occupiers on securing the highest quality office space with the best amenities and the latest fit-out in order to attract and retain the best talent.

Given where we are in the development cycle, any expenditure, from new-builds to refurbishments, poses difficult decisions for developers. They must assess a breadth of factors, including occupiers' ever increasing expectations, sustainability-driven improvements, placemaking and amenities and the limited economic life of the typical M&E equipment in larger buildings.

This highlights the importance of securing the best possible advice before investing in works, helping ensure more resilient, sustainable buildings that are both appealing to occupiers and deliver a healthy return on investment.

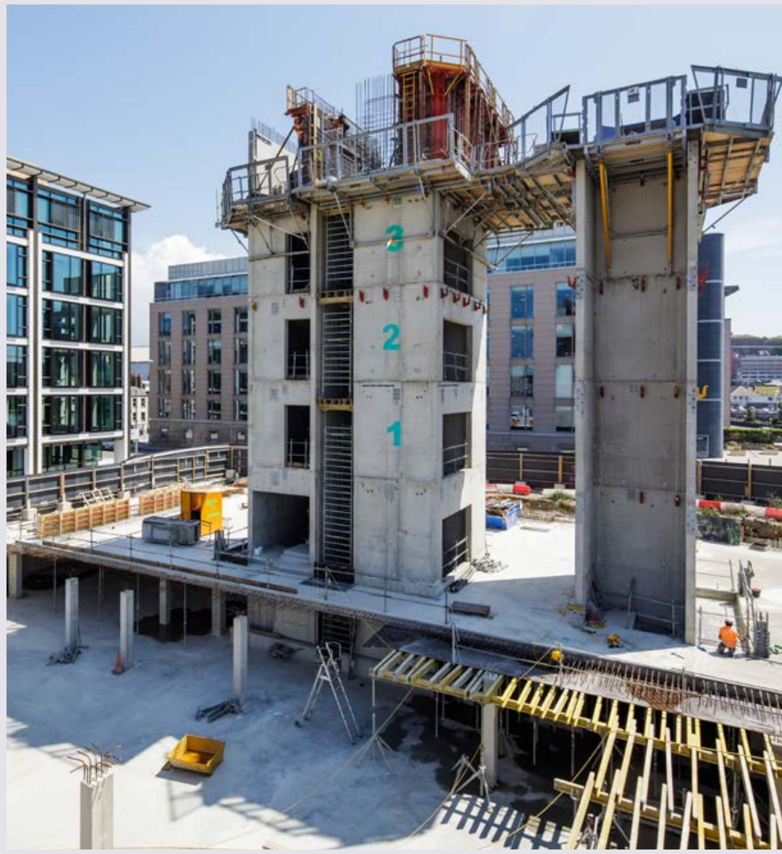
Whilst project costs vary hugely, here is a broad indication of the typical range:

	Channel Islands (sqft)	UK (sqft)
New Build Office	£475 - £525	£320 - £350
CAT A	£70 - £80	£40 - £50
CAT B	£120 - £140	£90 - £110

Source: AJK Consulting Limited

SUMMARY OF FORECASTS

Image © Bam Perspectives



CHANNEL ISLANDS OCCUPATIONAL MARKETS: **JERSEY**

Where next?

As we published our 2024 report, we expected the first £50 + psf office transaction in the Channel Islands within months. A year on, how close is this landmark figure?

Certainly, it is on the way. 2024's office take-up levels have remained consistent year-on-year, and occupiers' relocation activity remains driven by quality upgrades centred on the Esplanade / IFC / Castle Street location. Limited stock availability has led occupiers to consider larger office floorplates or temporary solutions until the right option comes along, strengthening demand for 'flex space'. There is an acute supply shortage, with many recent developments either prelet or built for owner occupiers (States of Jersey – circa 125,000 sq ft completed in 2024 and Aztec's IFC 6 completed in 2023). With the last development that offered significant vacant space completed in 2018, occupiers seeking a recently built building may have to be patient.

The result of these favourable supply / demand dynamics has seen further rental growth in the prime second generation building rental tone. Across several of these buildings we are seeing double digit growth, up from £28 psf to nearer £40 psf. The gap between the prime second generation buildings and new builds is narrowing. Once a new tone is established in second generation buildings this will make the jump to £50 psf+ for new builds more surmountable. But who will that occupier be?

We have identified around 200,000 sq ft of live enquiries from expanding corporates to new entrants seeking premium space, as well as over 80,000 sq ft now in advanced negotiations. A number of enquiries have been active for over 12 months, undergoing a size discovery exercise and refining their 'rightsized' need. We expect to see several commitments to identified options in 2025, which may ultimately carry us over the £50 psf threshold.

2024 Office take up:
110,000 sq ft

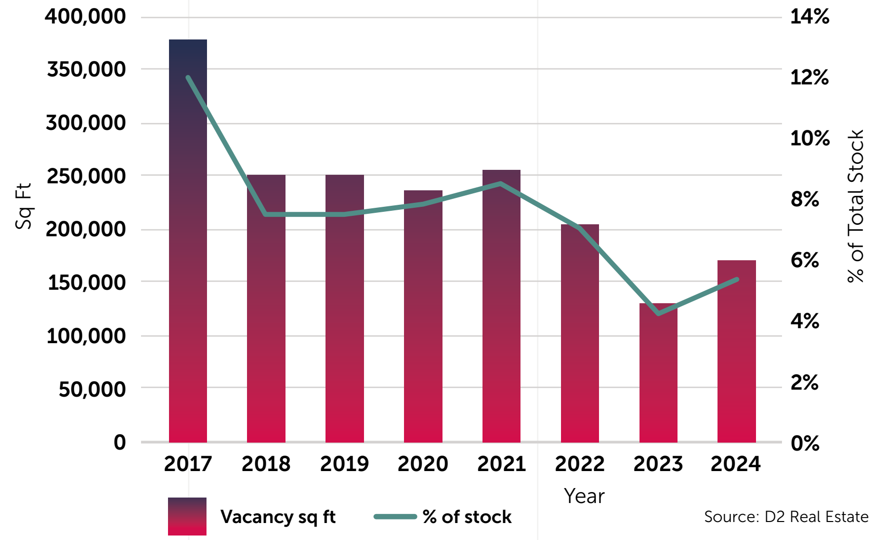
Total office stock vacancy rate:
5.31%*

Prime vacancy rate:
1.7%*

Number of live office enquiries:
200,000 sq ft

Typical rent-free incentive value:
1 month rent free per 1 year term certain

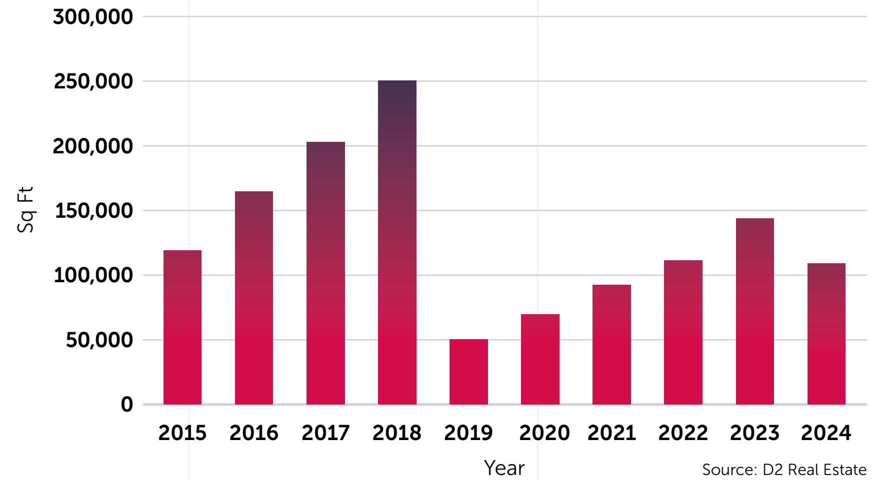
ST HELIER VACANCY RATE



Source: D2 Real Estate

The Vacancy Rate excludes 'grey space' (space that is let but the tenant seeking to downsize)

ST HELIER TAKE-UP



Source: D2 Real Estate

CGI post refurbishment of 25/26 Esplanade

*excludes grey space

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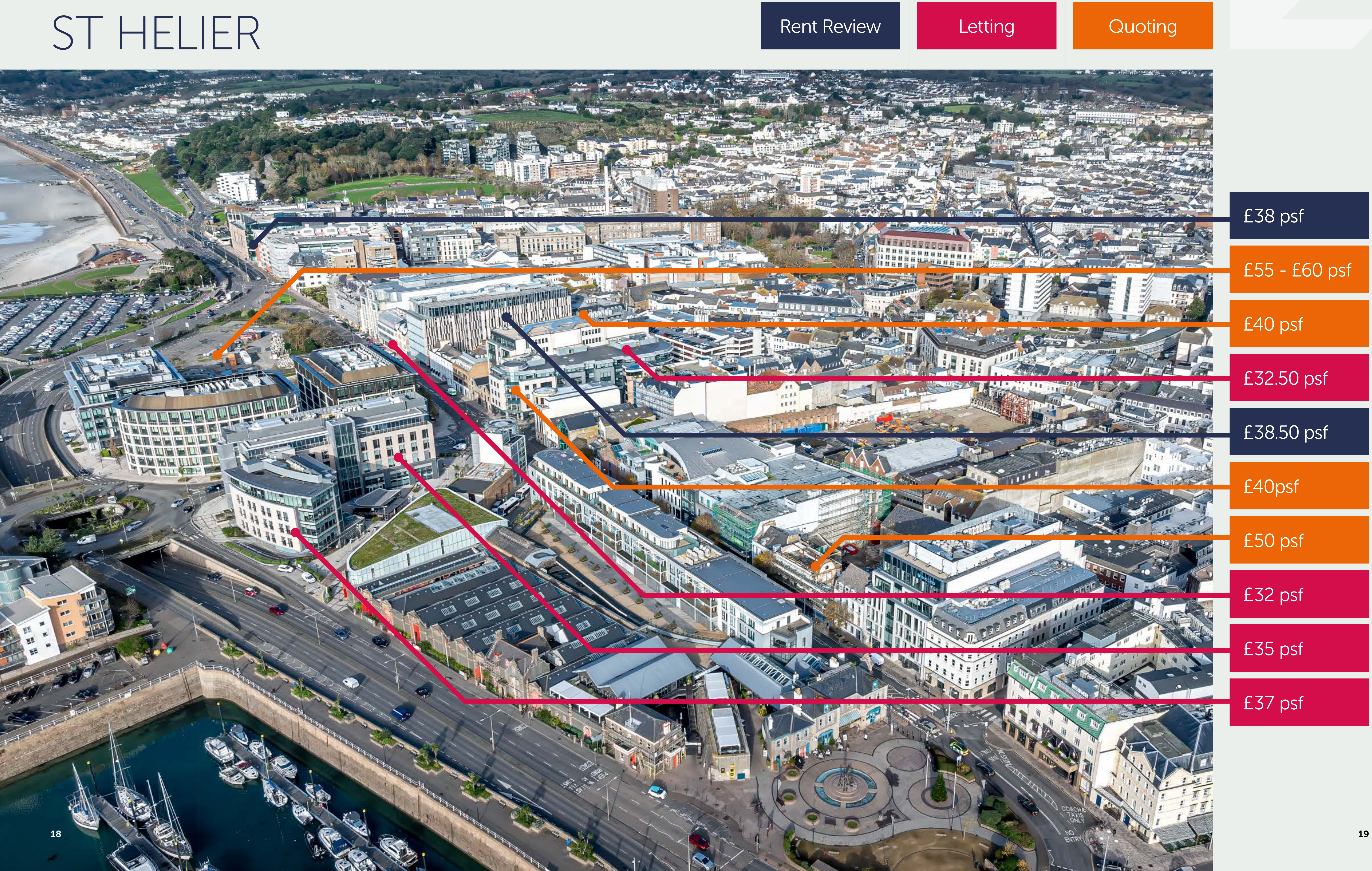
ST HELIER



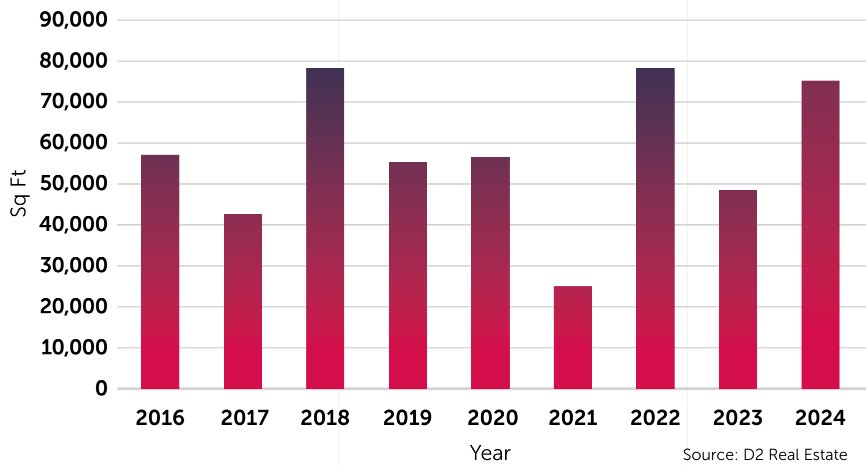
CHANNEL ISLANDS OCCUPATIONAL MARKETS: **GUERNSEY**

June's opening of Plaza House marked the completion of Guernsey's office development cycle. The BREEAM 'Very Good' office building has consolidated Admiral Park's success story with a plethora of quality occupiers, and the remaining vacant accommodation understood to be in advanced negotiations. The developer's confidence was evidenced by their decision to start on site without a prelet. Speculative development, carried out in the right environment, can prove to be an effective strategy. For example, a site acquired some time ago could offer developers the flexibility to offer more attractive rents to tenants while still achieving respectable profit margins. Where speculative development can introduce commercial risk for developers is when it creates a 'tenants' market', as this can lower the intensity of competition for space and impact the ability for the building to set a new rental tone.

As occupiers have relocated into 'best-in-class' space, others have been inspired to follow suit. After 2023's dip, 2024 take up has returned to the 2022 levels. Relocation activity continued to be driven by high quality office upgrades, with landlords reaping the rewards of their investments. Le Marchant House's comprehensive refurbishment has attracted a pre-let to Zedra and First National Bank, while extensive landlord works have delivered 100% occupancy at Royal Bank Place. Outside of leasing activity along Glategny Esplanade and at Admiral Park, significant lettings occurred across several town centre buildings, as well as the opening of Polygon's latest serviced office at Upper House on Smith Street, which has enjoyed strong occupier take up. Polygon will also open phase one of Town Mills, to be rebranded as Mill Place from Q2 2025, demonstrating the strength of the flexible occupational model in Guernsey.

We have identified around 70,000 sq ft of live enquiries. With few available 'prime' office floor plates remaining, occupiers will need to think creatively, or consider more town centre / fringe buildings. However, for well-located buildings offering quality space, and taking into account the fundamental lack of future office development sites, we expect to see landlords firming up their rental aspirations, and a shift in the prime rental tone in 2025 to above £40 psf.

ST PETER PORT TAKE-UP



2024 Office take up:
75,000 sq ft

Total office stock vacancy rate:
9.95%*

Prime vacancy rate:
1.42%*

Number of live office enquiries:
70,000 sq ft

Typical rent-free incentive value:
1 month rent free per 1 year term certain

*excludes grey space

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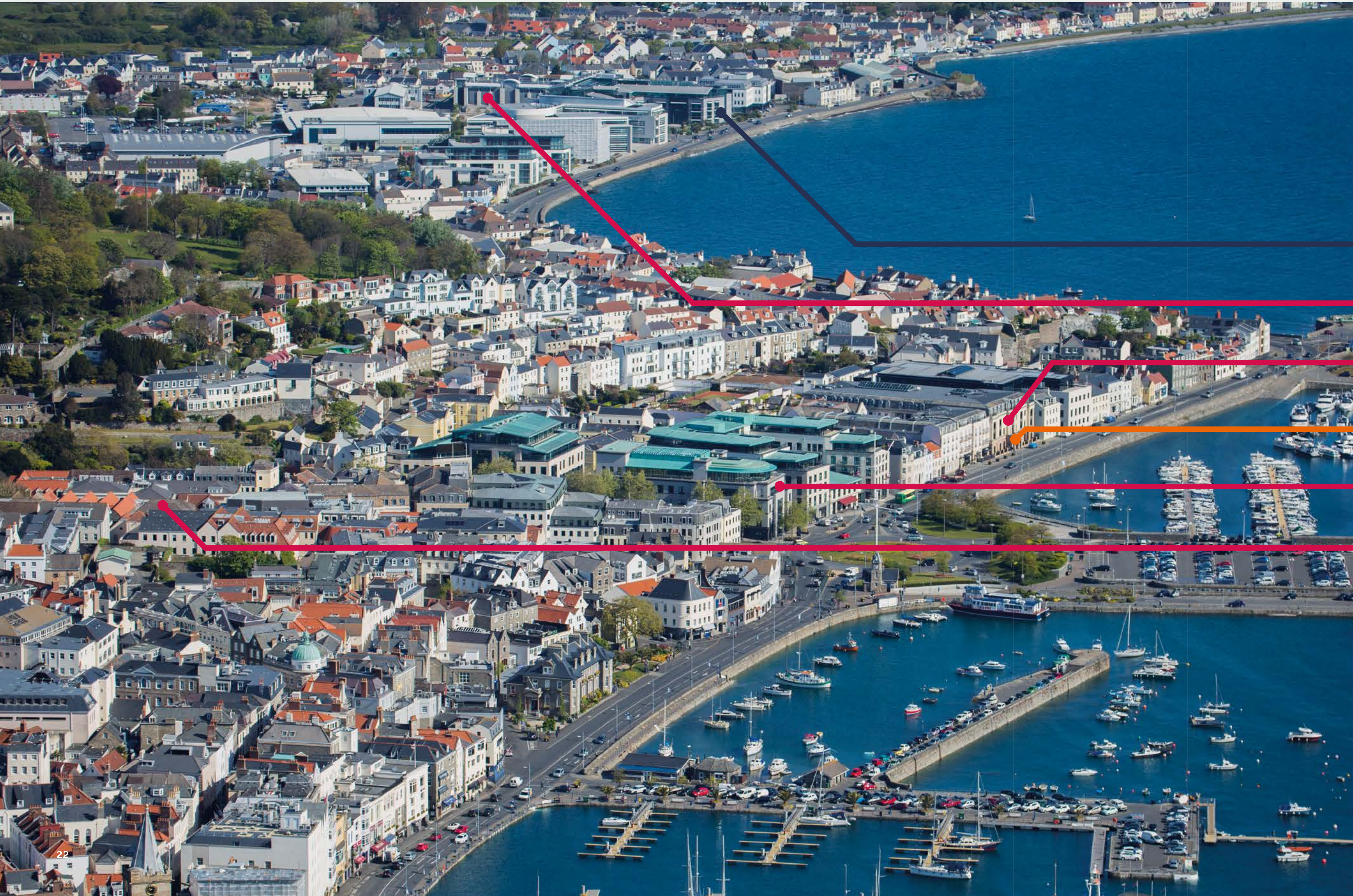
THE CHANNEL ISLANDS OFFICE MARKET REVIEW **2025**

ST PETER PORT

Rent Review | Letting | Quoting



£38 psf

£40 psf

£38.50 psf

£45 psf

£40psf

£35 psf

CONCLUSION

Reading this report, you may have noticed the conspicuous absence of Energy Performance Certificates (EPC's), a staple feature of our last two editions. EPC's have had a profound impact on the UK's commercial property market, and it had been expected that new legislation would be drafted in 2024. Ahead of this, D2 Real Estate and others had engaged heavily with Jersey's climate team surrounding the potential unintended consequences. The subject is complex, particularly when using a benchmark different to the UK's.

Following industry feedback Jersey will now focus on updating its building byelaws measures before drafting legislation relating to EPC's which is not expected in this government. It is not unreasonable to imagine that some form of legislation will be in place by 2030. However the 'when, not if' expectation means not only that the sales market is already adjusting, but that any refinance is likely to be influenced.

No doubt the cost of EPC compliance will come into the equation, albeit the Channel Islands generally score highly given its relative clean energy at source. Another jurisdictional advantage.

As mentioned in the opening of this report, I believe we are in much better shape than 12 months ago. Reducing interest rates – as ever, contingent on containing inflation – offer a strong platform for a sustained recovery. With increasing investment volumes will come rapidly gathering momentum. As I write, there is incontrovertible evidence of rising values here in the Channel Islands, and a strong tailwind of improving rental growth outlook and falling interest rates.

As ever stock selection is critical. We believe our experience, credentials, and track-record here are second to none. So if you are interested in future investment opportunities or want to hear how we can protect and enhance value through property management, we'd be delighted to talk to you.

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To find out how we can support your real estate strategy with research insights and strategic advice, please contact the team:

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