ARCAPITA

UK Real Estate

After the Heatwave

September 2026

Overview

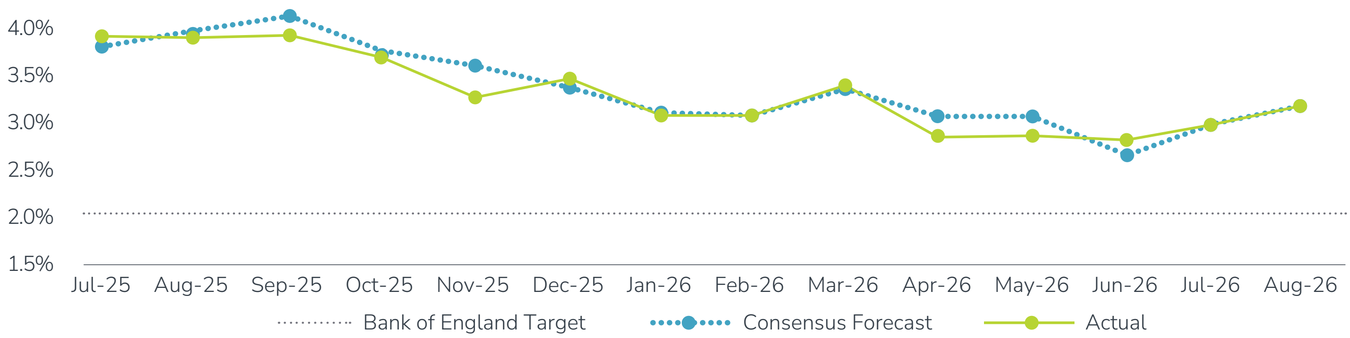
The summer of 2026 has been hot and dry, much like that of 2003. Coincidentally, the UK real estate market of 2026 also has similarities with that of 2003: underlying 5 year swap rates are in a similar range, the market feels nicely balanced between equity and debt providers in the same way as in 2003, and active management is again seen as the driver of investment performance. Of course, 2003 was followed by a real estate bull run up to 2008, driven by expanding and cheaper leverage; we are not suggesting that the next 5 years in UK real estate will necessarily follow a similar path, but it is enlightening to see how such accommodating market conditions are cyclical. In this note we outline the latest in the key macro factors that we pay attention to and update what we are seeing in the main UK property sectors.

What We're Paying Attention To

Inflation

UK inflation has gradually eased since last summer, from 3.8% in July to September 2025 to 3.1% in August 2026. We had anticipated that inflation could fluctuate between 2.5% and 3.25% through this period, similar to the path that UK inflation took following its peak in the early 1990s – in the end it has run slightly hotter but is now showing a broadly similar trajectory. Looking ahead, we are mindful that ongoing second order effects on energy markets from the Iran and Ukraine conflicts may see UK inflation oscillate rather than reduce towards the 2% target in the near term, but for now a disorderly increase seems unlikely. In our view, this inflation context remains a broadly neutral environment for real estate investment: as rental income tends to provide a relative inflation hedge, this inflation outlook should provide ongoing support to income growth, particularly with shorter or inflation-linked leases.

July 2025 to August 2026 inflation prints:
Consensus vs Actual Number



Source: Reuters; The Financial Times

What this means for real estate investors

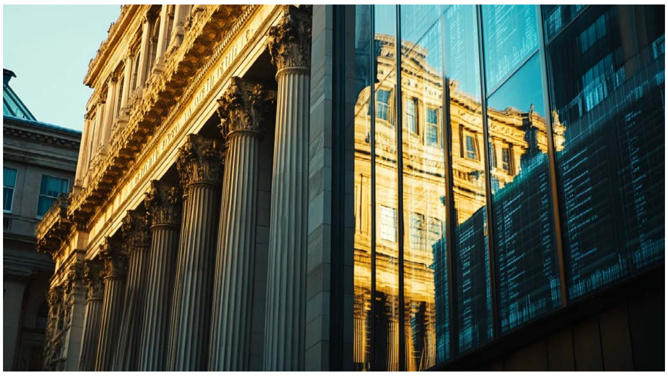
- We continue to favour explicit rent inflation linkage, or shorter unexpired lease terms, to hedge inflation exposure and capture inflation-led rental growth. While inflation probably won't reduce to 2% soon, and another inflation surge seems unlikely, retaining protection in this respect appears prudent.
- Sectors more exposed to inflation and overseas labour, such as hospitality or leisure, still appear less accommodating for income-focused investors.

Interest Rates & Financing Costs

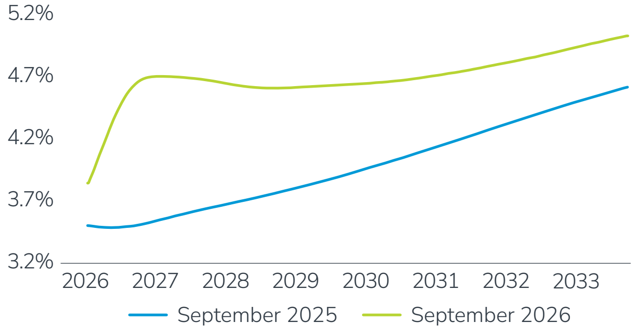
The Bank of England has kept interest rates at 3.75% since its last 25 basis point cut in December 2025, leaning towards holding steady rather than reacting quickly to more volatile geopolitical winds and seeing this decision bear out in a gradually decreasing inflation print. The market is now pricing almost three 25 basis point increases over the next 12 months, although this does fluctuate according to global oil prices and resulting inflation expectations, and the Bank's recent activity reminds us that this market pricing does not necessarily mean that UK interest rates will increase in the short term. Nevertheless the direction of travel indicates that UK rates are likely to remain relatively elevated over the medium term.

This compares to latest expectations of a similar increase by the US Fed over the next 12 months (beyond the 25 basis point increase in September 2026), and the market pricing in a further 75 basis point increase by the ECB over the same time frame (beyond its 25 basis point increase in September 2026), pointing to a market view of the UK base rate seeing a similar level to the US and c. 140 bps premium to the Eurozone over the medium term, providing further stability to the GBP exchange rate.

From a UK investment perspective, this means expectations remain for a higher-for-longer interest rate environment that gives a good runway to acquire UK real estate at attractive cap rates compared to some other geographies. In tandem, UK real estate financing costs should stay broadly stable, with healthy lender capacity, some widening of lender sector appetite and potentially improving margins and available loan-to-value ratios. Together this means that the UK continues to offer a largely predictable market environment, even if the prospect of a medium term easing in interest rates seems less likely at present.



SONIA Forward Curve:
September 2025 vs September 2026

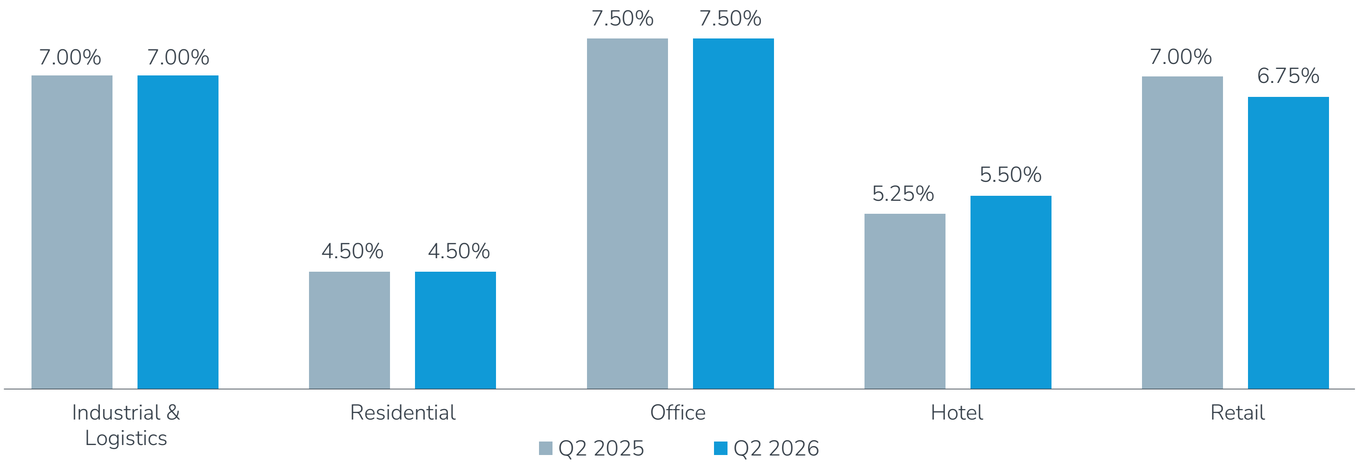


Source: Chatham Financial

What this means fo real estate investors

- Financing costs are largely stable and we expect capital market conditions to stay consistent for the foreseeable future.
- Lender pressure on legacy properties continues, although with less market disruption than we originally anticipated as 2020-22 era low-cost loans come up for refinancing.
- We continue to favour higher cap rate sectors where current financing costs are accretive
- Lenders continue to emphasise energy efficiency, whether through borrower upgrade plans or existing certifications, as they still face pressure to improve their loan book's energy profile notwithstanding new policies seen in the US.

UK RE Capitalization Rates by Sector

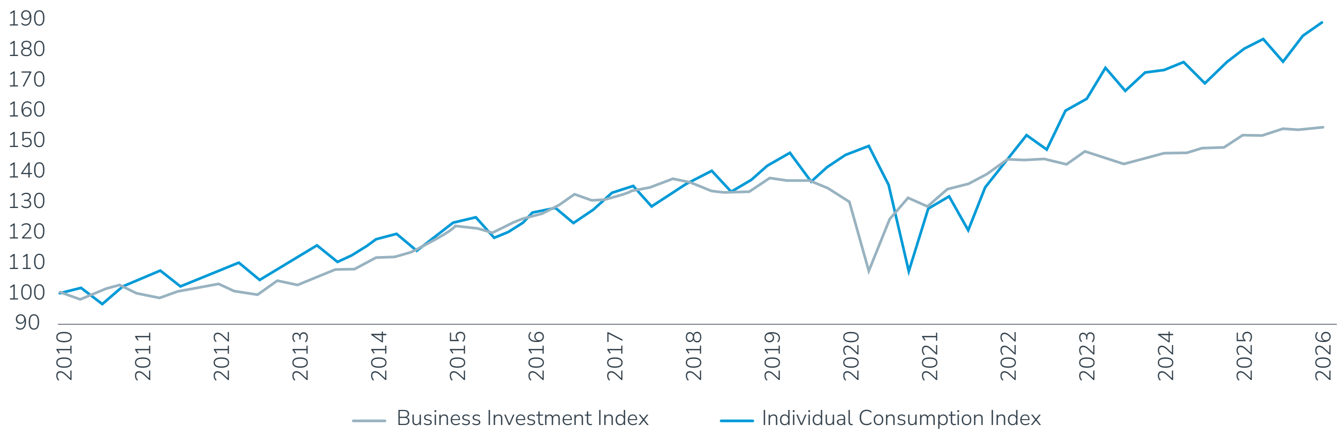


Source: Knight Frank Investment Yield Guide; Knight Frank UK Living Sectors Yield Guide

UK Economy

UK GDP growth, at 1.2% year-on-year in August 2026, has continued to be surprisingly robust over recent months given the global geopolitical uncertainty and UK political changes. Partly this seems due to underlying resilience in the UK services sector, and partly to UK consumer confidence reaching a 2-year high notwithstanding some media headlines, driven by significant UK household deleveraging over recent years. Indeed, the Bank for International Settlements now notes that the UK's combined private and public debt-to-GDP ratio (221%) is now lower than the US at 251%, making the UK actually one of the least indebted countries in the western world. On top of this, the UK houses the world's third-largest AI industry with an economy geared towards services and technology that is arguably well placed to benefit from AI productivity gains. Whisper it quietly, but after a decade of steady progress through various headwinds, the UK is now looking relatively well placed for the next global economic chapter.

UK Consumption & Investment Index



Source: ONS

What this means for real estate investors

- We continue to prefer income diversification and sectors making up the backbone of the UK economy, while being cautious on subsectors highly dependent on international capital flows
- We are starting to become more positive on sectors serving UK consumers rather than businesses, as consumer confidence gradually improves
- We favour real estate with affordable rents and offering value-for-money, irrespective of occupiers' business models
- We are also positive on investments around AI, although these tend to be more growth equity transactions rather than real estate (as UK data centres present a narrower opportunity than in the US, given planning and power constraints in the UK)

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UK Politics

In contrast, UK politics has been rather noisy over recent weeks. Keir Starmer has resigned as leader of the Labour party and therefore as Prime Minister, and has been replaced by Andy Burnham, the former mayor of Manchester. At the same time, Rachel Reeves has been replaced as Chancellor by John Healey, who was formerly the Defence Secretary.

However it is still the Labour Party in government, so arguably less has changed than one might imagine. Burnham, like Starmer, is a pragmatist and has shifted positions over the years. He leans more left wing than Starmer or Blair, more like Gordon Brown in his 2007-2010 government and tending to focus on affordability, social care and public intervention in core infrastructure such as energy and transport. Having been out of government for the last two years (when he was Manchester mayor) he doesn't have a parliamentary voting record to review – or indeed, to prevent him being portrayed as a change within Labour. The direction of his government will only become clear over the coming months as new policies are rolled out, and particularly with the new Budget in mid-October.

Inflation	Interest Rates	UK Economy	UK Politics
3.1%	3.75%	221	
August 2026 down from 3.8% in summer 2025	base rate held steady since Dec 2025	Combined debt-to-GDP ratio	New PM (Burnham) & Chancellor (Healey)

UK Property Sectors

Arcapita's focus remains on the industrial sector, particularly multi-let industrial, where we think assets are attractive due to higher cap rates, diversified and sustainable income profile and value add initiatives through active asset management. We continue to monitor further opportunities and highlight our thoughts on the various sectors within the UK Real Estate Market below:

Central London Offices

What are we seeing:

- "Return to the Office": We continue to see companies requiring employees to be in the office at least 3 days a week and others are extending these mandates further. In parallel, we have seen a steady stream of big lettings to professional firms that were considered to be most impacted by Work From Home (such as Canary Wharf seeing lettings of 350,000 sq ft from PWC, 220,000 sq ft from Deutsche Bank and 210,000 sq ft from HSBC) and others such as Barclays buying their HQs to secure their occupational footprint – the London office is certainly going strong again
- Equally, large AI firms including Anthropic and OpenAI have been conspicuous by their activity, with AI firms leasing 700,000 sq ft in London in H1 2026, double the total for all of 2025
- We know that office tenants focus on best-quality space in new or refurbished buildings, as they bring employees back to in-person work. Two nuggets from Savills drive this home though: up to May 2026, 92% of central London offices leased were Grade A, and active office demand is at a record level of 15.9m sq ft.
- Consider also the fact that Avison Young report Grade A vacancy at only 1.9%, and you have the recipe for strong rental growth for the best buildings. Savills report that average Grade A rents in the City of London are now £70 psf with top rents at £155 psf – these were Mayfair rent levels pre-Covid. The West End has in turn seen increases to average Grade A rents of £116 psf with top rents at £180 psf (Savills data again) – will we see Mayfair and St James's rents at £200 psf on an increasing basis in the next year?

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Regional Offices

What are we seeing:

- The same dynamic is playing out in the major UK cities (Birmingham, Manchester, Leeds, Bristol, Edinburgh and Glasgow). Grade A take up has dominated activity, with occupiers looking for well-located space close to transport hubs with strong amenity provision and sustainability credentials, and rents have responded.
- What were prime rents in the £30s pre-Covid are now well in the £40s, and breaching £50 psf in Birmingham, Bristol and now Leeds. And with Grade A vacancy rates often below 2%, the stage is set for continued growth.
- This then outlines a specific investor question: if there is a new office development in a major UK city, and occupiers willing to pre-let it in the £50s or even £60s, the missing ingredient currently is investor capital to fund it. Will any investors take this opportunity over the coming months?

Industrial

What are we seeing:

- Demand for logistics space has steadied over recent months, as a combination of higher space availability and global supply chain disruption has drawn companies to redesign their logistics networks, some keeping them in-sourced and adjusting their locations/sizes, and others out-sourcing and leading to 3PL requirements. In addition, defence, food and energy self sufficiency impetus has led to further new demand.
- Speculative development remains constrained and focused on the most sought after locations and the largest developers, though the conditions may be starting to form for opportunistic projects at the start of the next cycle.
- Mid-box (50,000-100,000 sq ft) units have seen their development cycle peak later than the larger logistics units, with a focus on London and the South East, although this now seems to have peaked and we would expect constrained speculative development going forward.

Student Housing

What are we seeing:

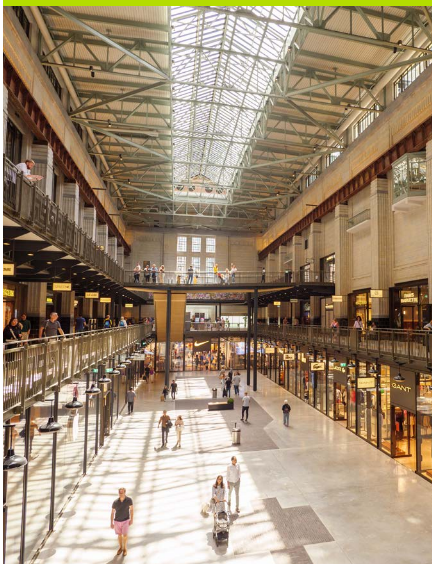
- As the new academic year approaches, there is decidedly mixed picture on student housing demand. On the one hand, UCAS figures show undergraduate applicants up 4.6% for 2026/27, however for many schemes the key audience are international students rather than the majority but cost conscious UK domestic students.
- For these international students, UCAS data show undergraduate applicants up 7.1% as at June. At the same time, Home Office data show that student visa applications as at end August fell 16% compared to the previous year. How to reconcile these? The main explanation seems to be that international students may now apply to universities in multiple countries (for example, the US, Canada or Australia as well as the UK, plus a growing appeal for some European countries), so an academic application may not lead to a visa application (and an actual international student in the UK) if say a Canadian university is eventually chosen.
- In addition, the key postgraduate data on international students comes out in September. The full picture, and the effect on student housing schemes, may not become evident until October.
- In the meantime, the investment market has entered a lull. There have been few transactions in recent months (Knight Frank estimate only £120m in Q2 2026) and there are reportedly c. £2bn of portfolio sales that have not progressed as the uncertain data feeds into differing seller and buyer expectations. Q4 may bring more clarity as the picture clears, but negative surprises may lead to an extended investment pause.

Residential

What are we seeing:

- The Renters' Rights Act came into force in May 2026, with the aim of providing tenants in private residential leases greater security of occupation and a more predictable regime for rent changes. Together with recent tax changes for residential properties, this is expected to extend the retreat of individual landlords from the residential letting market, and make institutional ownership more widespread.
- Single Family Housing remains the darling of this institutional residential market with Savills noting that the sub-sector's share of the residential market has grown from 6% in 2019 to 59% in 2025. There is now an increasing spread of buyers (from private equity to consolidating UK pension funds) and more consistent selling from the larger housebuilders.

Retail



What are we seeing:

- Quite surprisingly, the shopping centre investment market has been unlocked in recent months, with two of the UK's major centres (Metrocentre in the North East and a 50% share in Manchester's Arndale Centre) going under offer to listed REITs, and a pipeline of further deals that could lead to the strongest market since 2016. Shopping centres aren't for every investor's risk appetite (for example, Savills data shows 16% average vacancy rate and headline rents decreasing by 6.2% over the past year), but high cap rates on offer, the ability to place large equity cheques and the potential for active management to deliver value is drawing an increasing range of buyers.
- Retail Warehousing continues to show strong performance, underpinned by low vacancy rates and a clear core acquirer pool. However Cushman & Wakefield note that a downside of the low vacancy is that there are relatively few opportunities to demonstrate a reset of market rents through new lettings, such that headline rent growth has fallen from 3.5% at end 2024 to 1.2% in Q1 2026.

Arcapita's Focus

As we observed in 2025, there has been a lot of noise both politically and geo-politically, and indeed this has arguably increased over 2026. However the UK economy continues to impress with its resilience and its investment environment remains broadly unchanged, so that we still see the most attractive investment returns in higher income assets, active management strategies and a disciplined, targeted approach that can capitalize on these dynamics.

Within UK real estate, we maintain our highest conviction on domestically focused properties featuring affordable rents, diverse rent rolls and a value for money proposition. In particular, our preferred sector continues to be UK multi-let industrial, with its attractive combination of higher cap rates, sustainable income return, and capital growth through focused asset management.

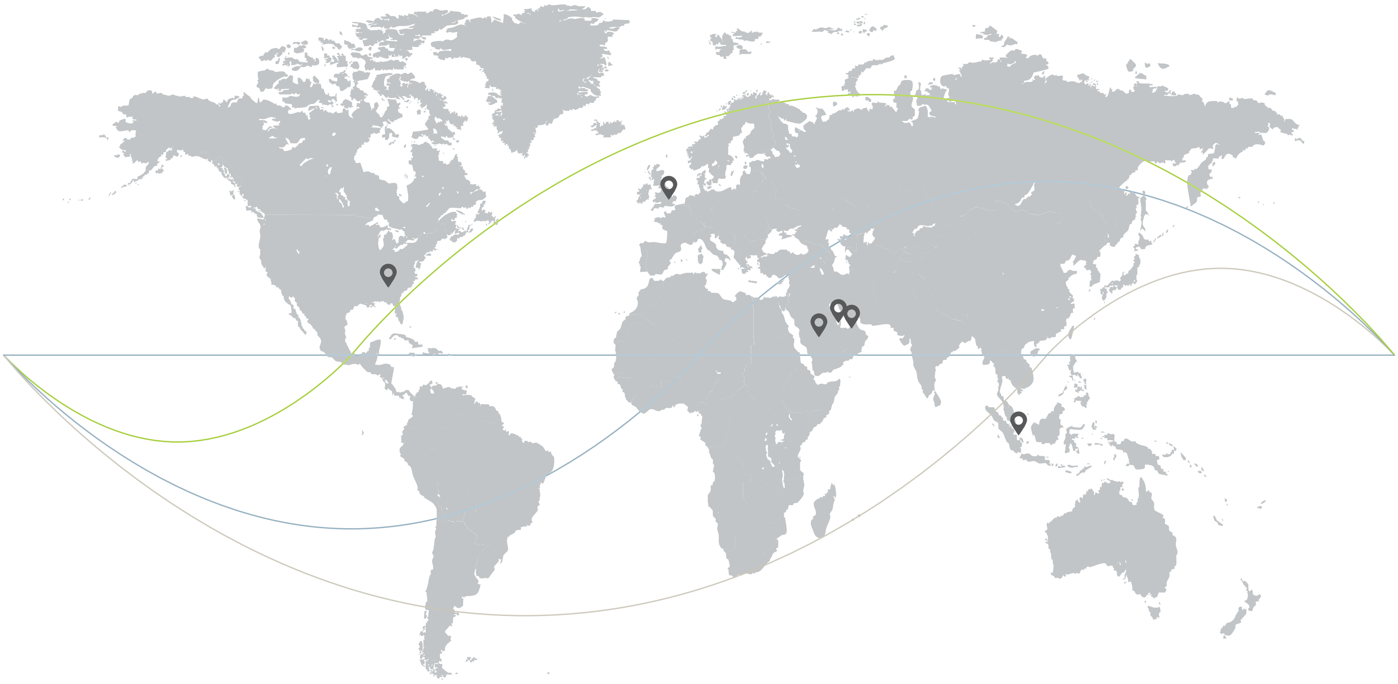
Anecdotally, we observe an increasing trend for companies to use AI to generate research and thought leadership reports. While we pursue thoughtful investment exposure to AI, rest assured that this report is, and will continue to be, fully human written. Any language or style quirks are the author's own.

ARCAPITA

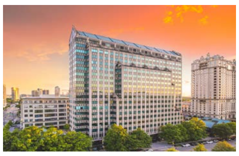
Overview

Arcapita is a premier asset manager offering diverse investment opportunities, focusing on private equity and real estate. At the center of one of the fastest growing wealth markets in the world, Arcapita's management has been serving an exclusive group of investors in the GCC region over the past two decades. With offices in Bahrain, US, UK, Saudi Arabia, UAE, and Singapore, Arcapita's management team has completed transactions worth a total value of approximately $30 billion and possesses a footprint to invest on a global scale. Arcapita focuses on defensive and counter-cyclical sectors supported by long-term macroeconomic and demographic trends.

With two decades of experience, Arcapita's management has built a global investment platform to access the opportunities that exist in our core markets of the US, Europe, Middle East and Asia.



United States



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