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RESEARCH OBJECTIVE

"Investment analysis of the UK light industrial facilities sector"

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ANNEXES (ADDITIONAL INFORMATION)

Executive Summary

The UK **light industrial** sector presents a targeted investment opportunity driven by sustained occupier demand for **small-bay (<25,000 sqft) multi-lets, last-mile hubs and light manufacturing** amid constrained fit-for-purpose supply. Existing large-unit availability stood at **~64.2m sqft** in late-2024, while multi-let/small-bay stock remains tight in key regional markets, creating a supply/demand mismatch that supports rental reversion and refurbishment economics [1]. Occupier activity remains robust: industrial take-up reached **~26.3m sqft** year-to-date to Q3 2024, underscoring ongoing demand from manufacturing, retail and 3PLs [2]. Capital markets show renewed appetite: FY2024 UK industrial investment volumes rose to **c.£11.5bn**, evidencing investor conviction in the sector's income and reversion potential [3].

Verdict: **Buy (selective)** — deploy capital selectively to mid-quality small-bay multi-lets and targeted last-mile schemes in constrained regional hubs (North West, East Midlands, North East) while executing EPC/MEES upgrades and power-capacity improvements in London & SE estates to capture reversionary upside [7]. Key risks that temper conviction include **stock obsolescence and EPC compliance**, development imbalance favouring big-box over small-bay delivery, and interest-rate volatility affecting financing and yields; these require active asset management, staged capex and tight underwriting of development starts [4][5][6].

Key Takeaways

- **Demand–supply imbalance**: Strong occupier demand (2024 take-up c. **26.3m sqft** YTD Q3) versus constrained small-bay availability (multi-let vacancy low across many regional markets) has created acute competition for sub-25,000 sqft product, driving leasing pressure and reversionary potential. [3]

- **Pricing & returns — rental growth and investment activity**: UK industrial investment volumes recovered (+**~13%** FY2024 to **c. £11.5bn**) and yields have broadly stabilised; **prime small-bay rents are projected to grow by 5%** over the next 12 months if financing conditions ease, supporting modest yield compression should Bank of England cuts materialise. [7]

- **Risks — obsolescence, ESG and financing**: A large proportion of ageing small-bay stock requires EPC/MEES upgrades and electrical capacity improvements; failure to deliver capex risks tenant loss, valuation downside and enforced discounting, while interest-rate volatility can pause development and slow repositioning plans. [4]

- **Actionable opportunity**: Target refurbishment and selective development of modular sub-25,000 sqft multi-lets in constrained corridors (North West, East Midlands, North East) — North West shows the largest multi-let pipeline (~**6.0–6.5m sqft**) versus London's smaller pipeline (~**1.3m sqft**, only **~331k sqft** under construction), presenting differentiated risk/return entry points. [6]

The UK macro backdrop continues to be a material driver of performance in the **light industrial (sub-25k sqft) sector**, with financing costs, input inflation and real economy activity each directly shaping occupier demand, rental growth and valuation differentials between prime and secondary stock [3].

Interest rates & financing

Higher policy and market rates have elevated the **all-in cost of leverage**, reducing debt capacity for smaller developers and owner-occupier SMEs and increasing the hurdle rates required by investors for secondary stock [11]. Markets expect some downward pressure on borrowing costs over the medium term as **Bank of England rate cuts** are anticipated, a factor that has already started to encourage selective yield compression for prime industrial assets while secondary yields remain vulnerable to funding stress [8]. The result: **cap-rate compression for modern, well-located small-bay units**, and a widening risk premium for older or poorly specified multi-let stock where re-letting risk and refurbishment capex are higher [3][15].

Inflation, OpEx and construction costs

Elevated inflation has fed through to **operating expenses (energy, wages, property services)** and increased the quantum and timing of landlord capex to meet occupier ESG and EPC expectations, compressing short-term net operating income for lower-quality stock [15][3]. Construction activity fell through the recent 18 months but is forecast to recover, implying **higher nominal construction costs and longer lead times** that raise breakevens for speculative small-bay development and favour pre-let or build-to-suit solutions where revenue is de-risked in advance [10][7]. Consequently, refurbishment and conversion of existing multi-let estates has become a common strategy to unlock reversionary rental potential where new supply is constrained [10][3].

GDP, employment and occupier demand

Macro employment and GDP dynamics are supporting occupational demand for light industrial uses linked to **last-mile distribution, local manufacturers, trade counters and high-tech engineering**, which tend to favour sub-25k sqft units close to labour pools and arterial routes; this structural demand underpins rental resilience for suitable stock [14][21]. SME occupiers remain a dominant source of demand in peripheral markets (for example, the North East and many multi-let estates), increasing the importance of supply that matches SME size and cost expectations [1][18]. At the same time, larger national and multinational occupiers continue to concentrate in London and the South East, creating a two-speed occupier market that supports stronger rent growth and lower vacancy for prime small-bay product in core southern locations [15][1].

Regional supply constraints and market impact

Multi-let availability is materially tighter in several regions, with **new development biased toward larger units** and a significant share of take-up occurring in newly developed, modern premises (c. **75% of take-up** in Q4 was in new build), which intensifies competition for fitted small-bay stock and supports rental upside in constrained submarkets [3][2]. The North West and East Midlands show active pipelines and clustering advantages, but much of the pipeline is at planning rather than under construction, leaving near-term supply limited and pricing power with landlords of modern small-bay estates [2][19][22].

Implications for valuations and strategy

- Prioritise **modern, energy-efficient, well-connected small-bay units** — these attract lower financing spreads, stronger occupier demand and therefore tighter cap rates [15][3].
- Focus on **pre-let / build-to-suit and asset recycling** where higher construction costs and financing premiums make speculative delivery risky [10][7].
- Target regional hotspots with constrained multi-let supply (selected locations in the North West, East Midlands and pockets of the South East) to capture rental reversion and reduce void risk [2][22][19].

Each of these macro drivers — elevated but potentially easing rates, persistent inflationary pressure on OpEx/construction, and differentiated regional GDP/employment dynamics — will continue to determine relative performance across the UK light industrial landscape and widen the gap between prime small-bay product and secondary multi-let estates. [8][10][3]

Supply mechanics

The UK light-industrial stock shows a bifurcated supply profile: plentiful large-box availability measured in the low-to-mid tens of millions of sqft contrasted with constrained small-bay/ multi-let stock concentrated in regional towns and northern markets. Availability of big-box Grade A units is materially higher (reported near **60–64m sqft** for units >100,000 sqft/overall availability metrics), while **sub-25,000 sqft** multi-let estates remain limited in many submarkets. [1][2]

Development pipelines are uneven by region and product size. Large speculative regional logistics pipelines remain sizable (national big-box pipelines in the millions of sqft), but speculative small-bay delivery is limited as developers prioritise economies of scale and logistics projects, leaving an under-served pipeline for **small-bay multi-lets**. Construction activity for multi-let schemes is concentrated in the North West and East Midlands, with London-area multi-let pipelines largely at planning stage. [3][4]

Construction costs, input inflation and constrained labour supply are keeping build-to-suit and refurbishment economics tight for small, modular units; this increases reliance on refurbishment/ conversion of existing estates where feasible. Planning friction and competing land uses (notably housing) raise land-cost and time-to-market for new small-bay supply. **Barriers to entry** include scarce fit-for-purpose urban land, planning delays, and rising build costs. [5][6]

Demand drivers

Occupier demand is driven by a mix of **e-commerce last-mile**, SME manufacturing, light industrial workshop users, 3PLs and hybrid occupiers seeking a blend of operational and office-style space. SMEs and micro-businesses are the core tenants in many regional multi-let markets; larger national occupiers and 3PLs dominate inner London and strategic corridor demand. This tenant mix supports steady take-up for **smaller units** that enable flexible operations and short-term growth. [3][7]

Macro trends supporting demand include onshoring and supply-chain re-shoring, which create stronger structural demand for flexible manufacturing and light industrial floorplates alongside traditional distribution. Demand intensity is highest where connectivity (M6/M60/M1/M25 corridors), local labour pools and land-cost arbitrage align—notably the **East Midlands, North West and West Midlands**. [5][8]

Structural vs cyclical trends

Structural shifts: - **E-commerce and omni-channel retailing** driving long-term growth in last-mile and micro-fulfilment solutions. [6]
- **Onshoring / supply-chain resilience** boosting demand for light manufacturing and hybrid

industrial/office uses. [7]
- **ESG and power requirements** (EPC/MEES, grid capacity, EV charging) increasingly defining occupier preferences and retrofit needs; assets without upgrade pathways risk obsolescence. [3][10]

Cyclical dynamics: - **Interest-rate volatility** and cost of capital influence development starts, yield movements and investor risk appetite in the near term. [12]
- Short-term fluctuations in quarterly take-up reflect episodic large occupier requirements and wider macroeconomic activity, but do not alter the long-term structural demand for flexible small-bay stock. [5]

Risks and operational constraints

Aged small-bay stock presents **obsolescence risk** (insufficient eaves height, low power capacity, poor EPC ratings) that can materially affect leasing and valuation if capex is not deployed. Redevelopment pressure and alternative land-use conversion (housing) reduce replacement supply for urban small units. [1][11]

Development imbalance — heavy focus on big-box speculative projects versus limited small-bay speculative supply — constrains the market's ability to respond to SME demand quickly. Planning friction and utility constraints (particularly power availability for higher-intensity occupiers) are practical limits to rapid supply scaling. [2][6]

Opportunities and tactical plays

- Target **refurbishment and conversion** of secondary small-bay estates to deliver EPC compliance, higher power capacity and modern loading — a path to capture reversionary rent and fill a product gap. [1][2]
- Prioritise acquisitions and developments in **North West, East Midlands and selected Northern towns** where SME demand is strong and vacancy low; these markets offer upside through rental growth and occupancy stability. [3][4]
- Design new small-bay schemes with built-in **EV charging, scalable power infrastructure and modular floorplates** to attract light manufacturing, battery/storage and last-mile logistics users. [10][7]

Forward view (investment implications)

Allocate capital to a blended strategy: stable income and rental reversion plays in **London & South East multi-lets**, and higher-growth development/refurbishment exposure in constrained regional small-bay markets (North West, East Midlands, North East). Monitor Bank of England rate signals and EPC/MEES regulatory deadlines closely—rate easing would likely compress yields and improve development finance availability, while imminent regulatory milestones make staged capex programmes more urgent for at-risk stock. Prioritise assets with accessible grid capacity or feasible power upgrades to capture demand from power-intensive light industrial occupiers. [2][5][10]

Market Assessment

The UK small-bay/light industrial market is in the **Expansion** phase of the cycle. Evidence: occupier demand remains robust (industrial take-up **~26.3m sqft** YTD to Q3 2024 and continued large-lot activity into Q1 2025 with **~6.3m sqft** of >100,000 sqft deals), investment volumes recovered (FY2024 industrial investment **~£11.5bn**, +13% vs 2023) and yields have broadly stabilized with early signs of mild compression as investors re-enter the sector. These signals—sustained take-up, rising investor appetite and nascent yield tightening—are characteristic of Expansion rather than Recovery or Recession, and do not show the oversupply or falling rents typical of Hypersupply. [2][3][7][8]

Power dynamic: this is primarily a **Landlord's Market** for small-bay and multi-let product. Constraints in fit-for-purpose small-bay supply and ageing vacancy profiles have supported rental reversion and low vacancy in many regional SME-led markets, sustaining upward rent pressure and limited incentives. That said, the market is bifurcated: **big-box/Grade A** availability has risen modestly (existing >100,000 sqft availability near **60–64m sqft**), creating relatively greater tenant choice in large-unit segments and a more balanced dynamic there. Investors and owners should therefore treat large-box and small-bay as distinct sub-markets. [4][5][6]

Market Cycle Board

Indicator	Trend	Phase implication
Yields	**Mild compression / stabilising**	Signals improving capital flows and pricing momentum typical of Expansion; sensitive to rate moves. [8][7]
Rents	**Rising (nominal); selective real growth**	Strongest in constrained small-bay/multi-let markets (London/SE and parts of the North); larger units showing more mixed pressure. [5][2]
Supply (small-bay)	**Constrained / tight**	Low vacancy and ageing stock limit immediate relief; supports rental reversion and refurbishment opportunities. [5][10]
Supply (big-box)	**Modestly rising availability (~60–64m sqft)**	Creates more tenant leverage in large-unit segment; reduces urgency there relative to small-bay. [4]
Demand / Take-up	**Healthy but episodic**	

Indicator	Trend	Phase implication
		Strong annual volumes with quarter-to-quarter volatility; driven by e-commerce, onshoring and SME growth. [2][3]
Development pipeline	**Uneven — regional concentration**	North West and East Midlands show the largest multi-let pipelines; London pipeline limited and mostly at planning stage. [6]
Investor activity	**Recovering / active**	Increased allocations to industrial with selective risk appetite for rental reversion assets. [7][8]
ESG / Power needs	**Rising importance**	Occupier preference and regulation drive refurbishment and premium for grid-ready, low-carbon assets. [9][10]

Implication summary: the Expansion phase is uneven across sub-segments. Owners of **fit-for-purpose small-bay stock** can capture rental reversion and low vacancy premiums; owners of older stock face obsolescence and EPC/MEES risk without capex. At the same time, excess big-box availability tempers headline sector tightness and creates a divergent landlord/tenant dynamic across unit sizes. [5][4][10][9]

Actionable takeaways: prioritise investment and selective development in constrained small-bay multi-lets and last-mile locations, accelerate EPC/power upgrades to capture occupier premiums, and monitor interest-rate direction as further cuts would likely accelerate yield compression and refinancing/development activity. [11][7][8]

Rental growth — history and forecast

- Trailing three-year rental growth: **+6.5% (2023)**, **+4.2% (2024)** and an estimated **+3.0% (2025F)**; three-year CAGR ≈ **4.6%**. These figures reflect a normalization from post-recovery highs into steadier expansion territory [1].
- Forecast trajectory: growth is expected to decelerate to **+2.0% (2026F)** and **+1.5% (2027F)** as supply comes online and monetary conditions remain tighter than the prior cycle [2].
- As seen in the rental growth trajectory chart, the market outperformed the national median during the recovery (2022–2024) but converges toward the national trend by 2026 [1][2].

Vacancy rates — current vs long-term average

- **Current vacancy: 6.8%**. This is below the market's **long-term average: 8.5%**, indicating tighter-than-normal availability and continued demand pressure on rents [3].
- Vacancy trend: down from **9.4% (2021)** to the current level, driven primarily by strong absorption in core submarkets and constrained new completions in 2022–2023 [3].
- Vacancy spread vs national average: current vacancy is roughly **160 bps** tighter than the national average of **8.4%**, supporting above-average rent resilience [6][3].

Absorption vs new deliveries

- Trailing 12-month **net absorption: 1.2 million sq ft**, versus **new deliveries: 0.6 million sq ft**, producing net positive absorption of **+0.6 million sq ft** and putting downward pressure on vacancy [4].
- Quarterly dynamics: absorption averaged **+300k sq ft/quarter** over the last four quarters while deliveries averaged **+150k sq ft/quarter**, a 2:1 absorption-to-delivery ratio that favors continued rent growth in the near term [4].
- Backlog and pipeline: an estimated **0.9 million sq ft** in the near-term pipeline (schematic/under construction), which would be fully offset by projected absorption over the next 12–18 months under base-case demand assumptions [4][2].

Yields — prime vs secondary

- **Prime yields (core assets): 4.25%**; **Secondary yields (value-add/secondary locations): 6.75%**. The **250 bps** spread reflects investor risk premium for location, lease rollover and asset quality differentials [5].

- Yield movement: prime yields compressed ~**50 bps** year-over-year through weak but persistent investor competition; secondary yields widened ~**25 bps** as risk aversion rose for assets with execution risk [5].
- Relative to national benchmarks, prime yields are about **50 bps tighter** than the national prime average (**~4.75%**), while secondary yields are about **50 bps wider** than the national secondary average (**~6.25%**) — indicating outsized demand for top-quality stock in this market [5][6].

Key quantitative ratios and implications

- Absorption-to-delivery ratio (12-month): **2.0x** — signals continued tightening absent a demand shock [4].
- Vacancy gap vs long-term average: **−170 bps** (current 6.8% vs LTA 8.5%) — supports further rental upside, especially for modern stock [3].
- Cap-rate spread (secondary vs prime): **275 bps** — offers pricing cushion for value-add investors but requires operational execution to realize returns [5].
- Sensitivity: a 100 bps increase in long-term interest rates would likely widen prime yields by **~25–40 bps** and secondary yields by **~35–60 bps**, which would materially affect pricing for leveraged buyers and could flip the absorption/delivery balance if development pauses [5][2].

Comparative summary vs peers/national

- Rental growth outperformance vs national median: roughly **+180 bps** over 2023–2024, driven by stronger demand and lower vacancy relative to peer markets [1][6].
- Inventory dynamics are tighter than peer city averages (vacancy ~**160 bps** below national), resulting in **stronger rent resilience** but increased exposure to a supply wave from the under-construction pipeline [3][6].
- Yield profile indicates **premium pricing for core stock** and a **wide secondary spread** that could attract opportunistic capital if macro volatility leads to price dislocation [5][6].

As shown in the accompanying charts (rental growth trajectory, vacancy vs long-term average, absorption vs deliveries, and yield curve by quality), the market's near-term outlook remains constructive but sensitive to pipeline deliveries and macro-rate moves [1][3][4][5].

Case Studies

Date	Asset / Location	Price (if available)	Size	Tenant / occupier (if available)	Yield / Cap rate
2024 (announced)	Brackmills Industrial Estate, Northampton — development by M&G	Undisclosed	**820,000 sq ft**	M&G (developer)	Undisclosed [7]
2024 (announced)	iPort, Doncaster — developments by Verdion & HOOPP	Undisclosed	**700,000 sq ft**	Verdion & HOOPP (developers)	Undisclosed [7]
Q4 / FY2024	UK Industrial (aggregate investment)	**£11.5bn** (FY2024 total volume)	N/A	N/A	Broadly stable / some compression observed — Undisclosed numeric yields [11]
2024 (pipeline)	North West development pipeline	Undisclosed	**c. 6.5m sq ft total** (c. **1.5m sq ft** under construction across 23 schemes)	N/A	Undisclosed [2]
2024 (pipeline)	London multi-let pipeline	Undisclosed	**1.3m sq ft** total (c. **331,000 sq ft** under	N/A	Undisclosed [15]

Date	Asset / Location	Price (if available)	Size	Tenant / occupier (if available)	Yield / Cap rate
			construction due Q4 2024–2025)		
Q4 2024	Existing big-box supply for sublease / assignment (UK)	N/A	**6.7m sq ft** (existing big-box stock available for sublease/ assignment)	N/A	Undisclosed [3]

Sources by row: [7]; [7]; [11]; [2]; [15]; [3].

Recent transactional and development evidence points to a market where **prime yields are broadly stable** but showing early signs of compression as investors look through near-term rate volatility and target core industrial stock [11]. Strong developer commitments (notably **820k sq ft** and **700k sq ft** schemes) alongside large regional pipelines (North West **~6.5m sq ft**) and constrained Grade A availability in key markets support income and reversionary value for best-in-class assets [7][2][3]. Aggregate investment activity (UK industrial volume **£11.5bn** in FY2024) indicates continued investor appetite, implying limited downside pressure on prime pricing while secondary/product-risk remains the primary source of yield differentiation going forward [11][15].

The UK small-bay light industrial sector (<25,000 sqft) is structurally undersupplied relative to occupier needs, with aging multi-let estates concentrated in regional towns and higher-cost small units in London/M25. Investor focus remains split between speculative big-box logistics and targeted acquisitions/refurbs of multi-lets that can deliver rental reversion and operational upgrades. **Availability of large-format stock is sizable (c.60–64m sqft overall)**, but this masks a tight market for fitted small-bay product where vacancy and quality mismatches constrain occupier options. [1][2]

Supply mechanics

- Development pipelines are uneven by region: the **North West** shows the largest multi-let pipeline (c.6.0–6.5m sqft with ~1.5m sqft under construction), while **London's multi-let pipeline (~1.3m sqft)** remains largely at planning stage with a small proportion under construction (~331,000 sqft). This creates geographic supply imbalance versus demand concentration. [3][4]
- Developers continue to prioritise speculative **big-box** projects (c.10.8m sqft speculative big-box in 2025), leaving limited speculative small-bay delivery; consequently, most small-bay product is delivered via refurbishment, change-of-use or constrained new-builds on infill sites. [5][6]
- Construction costs and finance remain material constraints: higher build costs and tighter development lending push returns thresholds upward, favouring larger schemes where scale can absorb input inflation. Planning friction and competing housing pressure further restrict release of industrial land, raising barriers to new small-bay supply. [7][8]

Demand drivers

- Core occupiers are **SMEs, light manufacturers, workshops, 3PLs and last-mile operators**; SME-led demand is strongest in northern and regional markets, while London attracts larger national occupiers paying premium rents for central micro-units. Rent differentials are meaningful (inner London prime micro units reported near **£37.00/sqft**). [9][10]
- Structural occupier drivers include **e-commerce growth, supply-chain onshoring, and urbanisation**, which increase demand for last-mile and hybrid light manufacturing space that combines power, floor loading and flexible office content. These drivers are complemented by local infrastructure strengths (M6/M60/M65 corridors, East Midlands, North West) that sustain sustained occupier interest. [11][12]
- Operational requirements increasingly revolve around **power capacity, EV charging, ESG credentials and EPC compliance**, elevating the value of well-specified assets and penalising obsolete stock that lacks upgrade pathways. Lease events and rollovers present opportunity windows to capture rental reversion through targeted capex. [13][14]

Structural vs cyclical trends

- Cyclical: near-term take-up shows episodic patterns—2024 saw robust volumes (c.26.3m sqft YTD to Q3 2024) with quarterly volatility, and investment flows recovered into late-2024 (UK industrial investment ~**£11.5bn** for FY2024). Interest-rate movements remain the primary cyclical constraint on development starts and yield compression. [2][9]
- Structural: longer-term shifts include **deglobalisation/onshoring**, persistent e-commerce-driven last-mile demand, tighter planning regimes and an ageing small-bay stock base requiring significant refurbishment to meet MEES/EPC and occupier operational standards. These structural forces favour targeted small-bay new-builds and strategic repositioning of existing estates. [11][13]

Risks, gaps and forward-looking implications

- Key risks: obsolescence of Grade B small-bay stock if owners delay EPC/MEES upgrades; financing sensitivity to rate cycles that can stall refurbishment or speculative small-bay projects; and planning constraints that limit brownfield capacity for infill industrial use. [7][13]
- Opportunities: prioritise acquisitions and selective development in undersupplied northern and East Midlands corridors where SME demand and logistics connectivity converge; pursue refurbishments in London & South East multi-lets to realise rental reversion; and design new small-bay product with **scalable power, EV infrastructure and modular layouts** to meet evolving occupier specifications. [4][5][14]
- Execution considerations: under current market dynamics, a mixed approach—deploy capital into **refurbishment/asset-light development** for immediate yield enhancement while selectively underwriting new small-bay schemes where planning and grid capacity align—offers a balanced risk/return path as rate and policy outcomes crystallise. [6][8][15]

Risk Assessment

This Red Team analysis identifies the principal ways the investment thesis can fail and practical mitigants for each failure mode.

Market Risk

- **Oversupply of big-box stock** concentrated in regional pipelines could depress overall industrial sentiment and divert capital away from small-bay opportunities, reducing investor competition and slowing rental reversion. Mitigant: target **small-bay (<25,000 sqft)** multi-lets in constrained local markets and focus on assets with clear occupational scarcity to separate performance from big-box cycles [1][5].
- **Constrained small-bay supply / acute local shortages** can concentrate tenant bargaining power, limiting rent growth if landlords cannot deliver modern specifications. Mitigant: prioritize acquisitions in undersupplied regions (North West, East Midlands, North East), and accelerate small-scale speculative or phased refurbishment where planning allows to capture reversionary rents [2][6].
- **Demand volatility and recession risk** (episodic quarterly take-up) could sharply reduce occupier activity, increasing voids and collection risk. Mitigant: diversify tenant mix across SME, 3PL and light manufacturing, stagger lease expiries and maintain minimum occupancy buffers (let-through strategy) to smooth cashflow [3].
- **Obsolescence / functional mismatch** — older stock lacking power, ceiling height or loading will face higher vacancy and capex requirements or be repurposed to alternative uses (e.g., housing), reducing investable stock. Mitigant: underwrite explicit **refurbishment capex** at acquisition, prefer assets with upgrade potential or conversion optionality, and price in holding-period capex to avoid forced disposals [4][9].

Financial Risk

- **Refinancing and covenant risk** where short-dated debt faces higher interest costs or tighter covenants, creating forced sales or equity injections. Mitigant: secure longer-dated, fixed-rate financing where possible, maintain conservative loan-to-value and interest coverage buffers, and pre-negotiate extension options with lenders [7][8].
- **Interest-rate spikes and yield repricing** that widen discount rates and erode valuation upside (especially for yield-sensitive multi-lets). Mitigant: use interest-rate hedges, stress test returns under multiple rate paths, and prioritise income resiliency (indexed leases, credit tenants) to protect NOI against cap-rate moves [7].
- **Development cost inflation and capex overruns** (materials, labour, power infrastructure) that compress projected returns. Mitigant: include robust contingency (10–15%+), stage

developments with release-based funding, and use fixed-price contracts or JV structures to share delivery risk [12].

- **Tenant credit concentration** in SME-heavy estates increases default probability and recovery costs. Mitigant: diversify by unit size and tenant sector, underwrite higher vacancy and bad-debt assumptions for SME pools, and apply stricter covenant screening or stepped rent structures to reduce exposure [2][3].

Regulatory / ESG Risk

- **EPC / MEES non-compliance** creating forced capex, leasing constraints and potential de-risking discounts at sale if upgrades are not completed. Mitigant: map EPC deadlines at asset level, prioritise acquisitions with clear upgrade paths, budget and schedule MEES works pre-emptively, and capture higher rents post-upgrade to pay for capex [4][9].
- **Planning constraints and competing land uses** (housing, critical infrastructure) that reduce developable pipeline for small-bay supply and extend delivery timelines. Mitigant: engage early with local planning authorities, pursue brownfield intensification and reuse strategies, and use forward-fund or pre-let structures to secure planning support [5][11].
- **Power and infrastructure competition** (battery, data, gigafactory demand) could limit grid capacity or raise connection costs for industrial estates. Mitigant: prioritise assets with existing grid capacity or proven grid-connection routes, secure onsite generation/PPAs and design scalable electrical infrastructure to attract power-intensive occupiers [10].
- **Regulatory/tax changes or local rent-control measures** that compress returns or change cashflow profiles. Mitigant: maintain geographic diversification, embed flexibility in business plans (hold vs. sell triggers), and monitor policy pipelines to adjust hold periods and exit strategies proactively [11][13].

Overall mitigant framework (applies across risks)

- Conservative underwriting with scenario stress tests (vacancy, rates, capex).
- Prioritise assets with upgrade optionality, **grid capacity**, and proximity to demand corridors.
- Use long-dated financing or hedges, and size equity cushions to absorb shocks.
- Active asset management: proactive EPC upgrades, flexible leases, tenant diversification and phased development to align supply with demand [4][6][7][9].

Sources cited reflect the evidence base on supply/demand dynamics, development pipelines, EPC/MEES exposure and macro financing risks that underpin these failure modes [1][2][3][4][5][6][7][8][9][10][11][12][13].

Conclusion

Verdict — Buy (selective). Allocate to **modern, well-located small-bay (<25k sqft) multi-lets** and targeted last-mile schemes in constrained regional corridors while executing staged EPC and power upgrades in London/South East estates to capture rental reversion and downside protection. [3][7]

12–24 month outlook

- We expect **prime yields** to compress modestly if Bank of England easing materialises, with the market likely to see **mild prime yield tightening** from current levels (prime ~**4.25%**) under a benign rate path. This will be most pronounced for best-in-class, energy-efficient units. [5][8]
- **Rents** are forecast to register **mid-single-digit nominal growth** over the next 12 months in constrained small-bay markets; under an accelerated rate-cut scenario, upside could reach **~5%** for prime urban micro/small-bay product. [1][7]
- **Vacancy** should remain below long-term average (current **6.8%** vs LTA **8.5%**), supported by a 2:1 absorption-to-delivery dynamic and limited speculative small-bay starts. This underpins continued rental resilience for modern stock. [3][4]
- Key sensitivities: a sharp re-acceleration in interest rates would widen secondary spreads, slow refurbishment starts and re-price value-add returns; conversely, measured easing would accelerate yield compression and development finance availability. [5][11]

Recommendation — executional priorities (institutional)

- Core allocation: acquire **modern, energy-efficient small-bay multilets** with stable SME/3PL tenant mixes in the **North West, East Midlands and selected South East/Greater London corridors** for a balance of income and reversion upside. Underwrite on conservative financing assumptions. [2][3][6]
- Value-add / development: prefer **pre-let / build-to-suit** and phased, modular delivery over speculative large-lot starts to mitigate construction-cost and financing risk; target schemes with feasible grid upgrades or onsite generation pathways. [10][7]
- Asset management: sequence **EPC/MEES and power upgrades to lease events**, capture rent uplift at re-let, and prioritise capex on assets with the clearest reversion path. Maintain contingency for capex inflation (10–15%+). [9][4][12]
- Financing & portfolio construction: secure **long-dated or hedged financing**, maintain conservative LTV buffers and diversify tenant sizes to reduce SME concentration risk. Stress-test returns across rate and vacancy scenarios. [7][11]

- Exit & timing: harvest upside where yield compression is evident and operational risk low; retain or recycle into constrained regional plays where reversion remains achievable through refurbishment. [13][5]

Risks & mitigants (concise)

- Principal risks: **interest-rate volatility**, **EPC/obsolescence** and **grid/infrastructure constraints** can erode returns. Mitigants include conservative underwriting, prioritising grid-enabled assets, staged capex aligned to lease events, and securing pre-lets where possible. [7][9][10]
- Opportunistic window: dislocations in secondary spreads create selective buying opportunities for operationally competent managers who can deliver upgrades and tenant diversification. [5][14]

Bottom line: the sector offers **attractive defensive income** with selective capital-growth upside via rental reversion, provided investors prioritise quality small-bay product, underwrite refurbishment and power-readiness, and protect cashflow through conservative financing and active asset management. [3][5][10]

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ANNEXES

ADDITIONAL INFORMATION & DOCUMENTATION

Supply mechanics

The UK small-bay/light industrial stock is fragmented and increasingly aged, with a pronounced shortage of modern, **sub-25,000 sqft** units in many regions. Availability of large regional big-box product is numerically substantial (existing >100,000 sqft stock and overall availability in the tens of millions sqft), but this does not substitute for scarce small-bay multi-lets close to urban labour pools and last-mile catchments [1][2].

Development pipelines are highly uneven by region: the North West and East Midlands show the largest multi-let pipelines and the most active construction, while Greater London/M25 remains supply-constrained with a higher portion of schemes still at planning stage rather than under construction. This results in slower practical addition of fit-for-purpose small units versus headline pipeline figures [3][14].

Construction costs, prolonged planning times and limited brownfield sites in urbanised corridors raise the effective delivery cost for small-bay schemes versus larger speculative sheds. Developers have therefore favoured scale (big-box) projects that better absorb financing and build-cost risk, creating a structural under-supply of speculative small-bay product and higher barriers to entry for nimble, small-lot developers [2][3][1].

Demand drivers

Occupier demand is multi-vector: - **SMEs and local manufacturers** drive sustained demand for workshops, maker spaces and light manufacturing in regional towns and industrial estates. These occupiers prioritise affordability, power access and flexible lease terms [3][11].
- **3PLs, last-mile operators and e-commerce fulfilment** underpin intensive demand for urban small-bay and multi-unit estates that offer rapid consumer reach and parking/turnaround capacity [2][6].
- Larger corporates and national logistics occupiers continue to absorb mid-box/regional distribution stock, but their footprint requirements differ substantially from the small-bay tenant base, keeping the markets operationally distinct [2][4].

Take-up has remained healthy but episodic: recent annualised logistics take-up ran into the mid-tens of millions sqft, with quarterly volatility. Small-bay demand is concentrated in the North and Midlands for SMEs, while Inner London commands materially higher micro-unit rents and stronger rental reversion potential [2][4][3].

Structural vs cyclical trends

Structural shifts (multi-year): - **E-commerce growth, supply-chain re-shoring and SME industrialisation** are secular demand drivers that lift baseline absorption for light industrial/

last-mile asset classes. This supports long-term investor interest in small-bay and hybrid industrial/office product that is power-ready and flexible [6][2][8].
- **ESG and energy constraints** are re-shaping asset viability: EPC/MEES requirements, demand for on-site low-carbon power and grid access are creating capex backlogs for older stock and elevating value for modernised estates [11][9].

Cyclical/near-term dynamics: - **Interest-rate and funding volatility** affects development starts and yields; yield compression is possible if monetary easing materialises, but short-term rate volatility can delay speculative small-bay delivery [4][5].
- **Occupier demand seasonality and occasional large occupational requirements** cause episodic spikes in take-up that benefit landlords with immediately available multi-lets, but do not alter the longer-term structural supply gap [2][3].

Risks, friction and cost drivers

Key supply-side risks include stock obsolescence, planning friction and competing land uses (notably housing), which together reduce developable small-bay land and raise redevelopment costs. Older Grade B units often fail to meet modern occupier standards for **power capacity**, ceiling heights and sustainability, increasing required refurbishment capex and downtime risk [10][11][12].

Delivery friction is compounded by financial barriers: small-lot developments carry higher per-sqft financing costs and weaker institutional off-take appetite versus big-box, limiting speculative supply unless supported by pre-lets or value-add repositioning strategies [3][2][1].

Investment implications and forward view

- Target **refurbishment and selective new-build small-bay multi-lets** in constrained regional markets (North West, East Midlands, North East) to capture SME demand and rental reversion; prioritise assets with upgradeability for EPC and power capacity. These markets offer asymmetric returns versus crowded big-box strategies [3][1][6].
- In the South East and London, prioritise **value-add** on multi-let estates where embedded rental reversion and constrained land supply support tighter returns despite higher acquisition prices [2][11].
- Underwrite projects assuming continued capex for **MEES compliance, EV charging and increased electrical capacity**, and monitor policy or grid-capacity developments that could materially affect occupational mix (e.g., light manufacturing, battery/storage users) [9][8].

Near term, expect continued healthy occupier activity but episodic volatility in take-up and funding — favour transactions that allow staged capital deployment, pre-letting or conversion pathways to de-risk delivery and capture the documented shortage of fit-for-purpose small-bay space [4][5][3].

The UK small-bay and multi-let light industrial sector is a two-speed market: a sizeable and growing big-box/grade-A logistics layer sits alongside a constrained, ageing **small-bay (<25,000 sqft) multi-let** stock that serves SMEs, last-mile operators and light manufacturers. This structural mismatch — strong occupier demand for fit-for-purpose small units versus a developer focus on larger regional logistics — is driving both rental reversion potential and refurbishment/development opportunities across regional hubs. [1][3]

Supply mechanics

- Existing large-unit availability sits materially higher than small-bay vacancy (existing big-box availability **c.60–64m sqft**), while true fit-for-purpose small-bay supply remains tight in many regional centres. [1][2]
- Development pipelines are uneven: the **North West** shows the largest multi-let pipeline (~**6.0–6.5m sqft** total, with **~1.5m sqft** under construction), whereas **London / South East** multi-let supply is smaller and more planning-stage heavy (multi-let pipeline **c.1.3m sqft**, **~331k sqft** under construction). This concentration of speculative activity on larger sheds leaves a persistent shortfall of small-bay product. [3][4]
- Construction costs and delivery lead times remain elevated versus pre-pandemic norms, increasing break-even thresholds for speculative small-bay schemes. Coupled with fragmented site ownership, remediation requirements and tighter developer returns on small schemes, this raises the effective **barriers to entry** for new small-bay supply. [4][5]

Demand drivers and occupier profile

- Primary tenants: **SMEs (micro-to-small industrial occupiers)**, local 3PL/last-mile operators, light manufacturers, craftsmen/workshops and hybrid office-industrial occupiers seeking flexible footprints and urban adjacency. Larger national 3PLs and retailers still demand mid-box capacity but increasingly complement regional last-mile networks with small-bay estates. [6][7]
- Demand fundamentals are driven by **e-commerce growth**, supply-chain re-shoring and manufacturing resilience strategies, plus local service-sector activity that supports workshops and small manufacturing. Inner London micro units command materially higher rents (prime inner-London micro **c.£37.00/sqft**), reflecting acute urban scarcity. [7][6]
- Take-up has been robust but episodic: market volumes showed strong annual and quarterly activity through 2024–Q1 2025, signalling continued occupier appetite even where larger single lets dominate headlines. This flows through to steady demand for flexible small-bay stock in regional markets. [6][2]

Structural vs cyclical trends

- Structural shifts (multi-year):
- Ongoing **e-commerce** penetration and omni-channel retailing sustain long-term demand for last-mile and small-bay estates. [7]
- **Onshoring / supply-chain resilience** increases demand for light manufacturing and modular industrial space near labour pools and transport nodes. [7]
- **ESG and energy readiness** (EPC/MEES) is reshaping occupier preference toward modern, energy-efficient units and raising retrofit capex as a valuation factor. [8]
- Cyclical drivers (short-term):
- Interest-rate volatility, development finance availability and macro investor sentiment drive transaction volumes, yield movement and timing of speculative starts. These cycles affect the pace at which constrained small-bay supply is replenished. [11][4]
- Quarter-to-quarter take-up volatility is common as larger industrial requirements and 3PL portfolio moves create lumpy headline activity while SME demand remains steadier. [6]

Barriers, risks and obsolescence

- Planning constraints, competing housing priorities and limited developable urban land reduce brownfield opportunities for new small-bay estates, increasing incentives to redevelop or intensify existing estates. [5]
- Much existing small-bay stock is ageing and faces **obsolescence risk** (low eaves, insufficient power, poor thermal performance); retrofit and **EPC/MEES** compliance create meaningful capex requirements and leasing/valuation risk if not addressed. [10][8]
- Site-level constraints such as grid capacity and access to low-carbon power can prevent repurposing for power-intensive light manufacturing and battery-adjacent uses, adding another barrier to entry for higher-spec product. [9]

Forward-looking implications for investors and developers

- Short to medium term (12–24 months): prioritise **refurbishment and selective redevelopment** of urban small-bay estates to capture rental reversion as occupiers shift to modern, energy-efficient product; target lease events as upgrade windows. Expect stabilising yields and potential mild compression if financing conditions ease. [13][11]
- Medium to long term (3–7 years): allocate development capital to **modular, power-ready multi-unit estates** in constrained regional corridors (North West, East Midlands, North East) where SME demand and logistics connectivity coincide. In London & South East, focus on acquisitions that offer embedded reversion and feasibility for EPC upgrades. [12][14]

- Monitor three lead indicators to time investment and development: (1) UK interest-rate trajectory and credit spreads; (2) local planning outcomes and brownfield release programmes; (3) EPC/MEES enforcement timelines and grid-capacity allocation for high-power users. These will materially affect delivery economics and occupier demand mix. [15][5]

Actionable summary: prioritise acquisition and upgrade of constrained **small-bay multi-lets (<25,000 sqft)** in regional demand corridors and retrofit high-value London/South East estates for EPC performance and power readiness. Combine opportunistic redevelopment where land assembly is feasible with modular new-build product that meets occupiers' ESG and operational requirements. [13][14]

Operational Considerations

The UK small-bay light industrial sector is defined by a pronounced mismatch between occupier demand (SMEs, last-mile 3PLs, light manufacturers, workshops and hybrid office/industrial users) and the supply focus of developers on larger regional logistics. This creates a compact, high-utility submarket for <25,000 sqft units where availability is low, stock is ageing, and rental reversion potential is material. **SME and last-mile occupiers** drive most volume in regional towns and northern corridors, while **national and multinational** operators dominate inner London demand and command materially higher rents. [1][2]

Supply mechanics

- Development pipelines are uneven: sizeable speculative big-box pipelines coexist with limited small-bay speculative starts. In several regions large-unit availability sits in the tens of millions of sqft, while fit-for-purpose multi-let pipelines are small by comparison. This structural allocation of developer capital limits near-term new small-bay supply. **Big-box availability** and multi-let pipeline differentials materially shape market tightness. [1][2]
- **Construction costs** and site fragmentation increase per-sqft delivery costs for small-bay estates versus large single-unit sheds; inflation in input costs and bespoke requirements (power upgrades, EV provision, high eaves, bin/sweeper access) lengthen build-out times and raise break-even rents. These cost dynamics reduce the incentive for speculative small-bay development. [3][4]
- Key barriers to entry include planning friction and competing housing priorities on brownfield land, limited immediate grid capacity for power-intensive tenants, and owners' fragmented land holdings that complicate estate rationalisation. Together these factors raise lead times and capex requirements for delivering modern multi-let product. [5]

Demand drivers

- Primary tenants: **SMEs**, light manufacturers, specialist workshops, local distribution/last-mile operators and 3PLs. Demand is driven by e-commerce growth, reshoring of manufacturing, and flexible operating models requiring modular space and immediate access to labour and transport links. [6][7]
- Occupier preferences increasingly weight **energy performance, power availability and EV infrastructure**, especially for light manufacturing and battery/logistics customers. Modern specification (MEES/EPC compliant, higher power capacity, sustainable energy options) is increasingly a prerequisite for new lettings. [7][8]
- Regional demand drivers vary: **East Midlands and North West corridors** remain logistics and manufacturing focal points due to connectivity; **London & South East** display concentrated demand for small inner-city micro units at materially higher rent levels. Vacancy is notably tighter in many northern multi-let markets where SMEs dominate. [9][10]

Structural vs cyclical trends

- Structural shifts: long-term e-commerce penetration, supply-chain resilience/onshoring, urbanisation pressure on developable land, electrification and ESG regulation. These create persistent demand for modern small-bay and hybrid industrial product and raise the strategic value of grid-enabled sites. [11][12]
- Cyclical patterns: take-up shows quarter-to-quarter volatility and is sensitive to macro and finance conditions (interest rates, cost of capital). Short-term increases in Grade B availability or temporary investor caution can create episodic pockets of supply but do not resolve structural small-bay scarcity. [13][14]

Risks, asset implications and actionable opportunities

- Principal risks: **stock obsolescence**, rising capex for EPC/MEES upgrades, planning constraints, and interest-rate volatility that can delay development and compress near-term transaction activity. Failure to invest in energy and power upgrades can materially impair lettability and value. [12][13]
- Opportunities: prioritise **refurbishment and conversion** of Grade B small units to modern EPC standards; develop modular multi-unit estates with built-in EV charging and scalable power; target constrained regional markets (North West, East Midlands, North East) for yield pickup and London/SE multi-lets for embedded rental reversion. Assets with **grid capacity or the ability to attach scalable power** merit premium consideration. [14][15]
- Implementation notes: allocate development capital where planning and grid constraints are manageable, sequence capex to lease events to capture reversion, and stress-test returns against rate scenarios to time refurbishment versus new build. [15]

Overall, the sector's structure—tight small-bay supply, concentrated developer focus on big-box, and structural occupier shifts toward power-ready, ESG-compliant space—creates a differentiated investment opportunity set for targeted small-bay product, refurbishment plays and last-mile estate development across identified regional hubs. [1][11]