



Debt Advisory

Real Estate Report

Spring 2025

We see things
differently.

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Headline views

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Macro factors point to a stabilisation in house prices

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Planning changes in progress but yet to be reflected in actions

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Rising build costs lead to challenging profit margins on land acquired in recent years

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Widening gap between lender's panel valuers and developers' 'valuation'

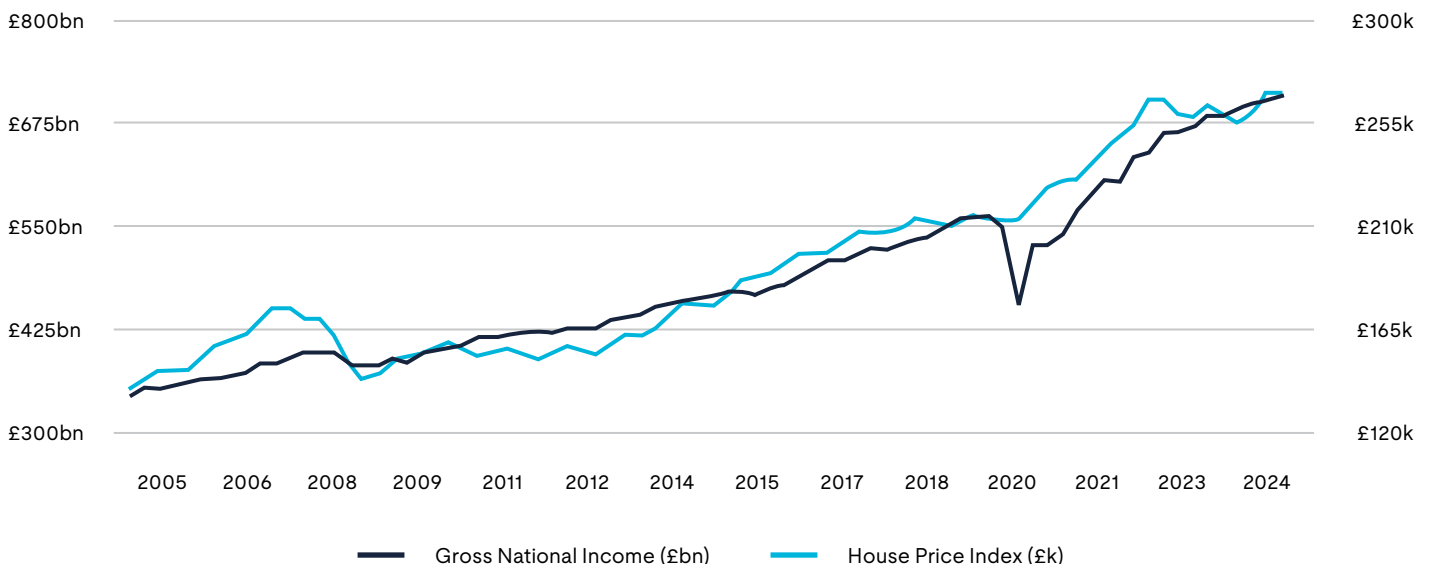
Recent macroeconomic environment

Indicators

The restrictive monetary policy environment of 2022/23, to which the property sector is particularly sensitive, has kept house price growth subdued. However, with limited housing stock, expected interest rate cuts, and additional fiscal support, prices are likely to revert to their long-term trend. We anticipate a rise of at least 3% over the next year.

As of November 2024, the average UK house price stood at £268,000, reflecting a 4.6% increase over the past year.

Fig.1 UK House Prices



Wage growth averaged a strong pace 6.1% year-on-year in January 2025, slightly higher in the construction sector at 6.7% year-on-year. Rising labour costs, along with increases in National Insurance and the minimum wage, are squeezing margins.

Persimmon, for example, projects a £15 million increase in direct costs due to NI hikes, with an additional £10 million impact across its supply chain. However, developers retain some pricing power, which could drive further inflation in house prices. The unemployment rate currently stands at 4.4%.

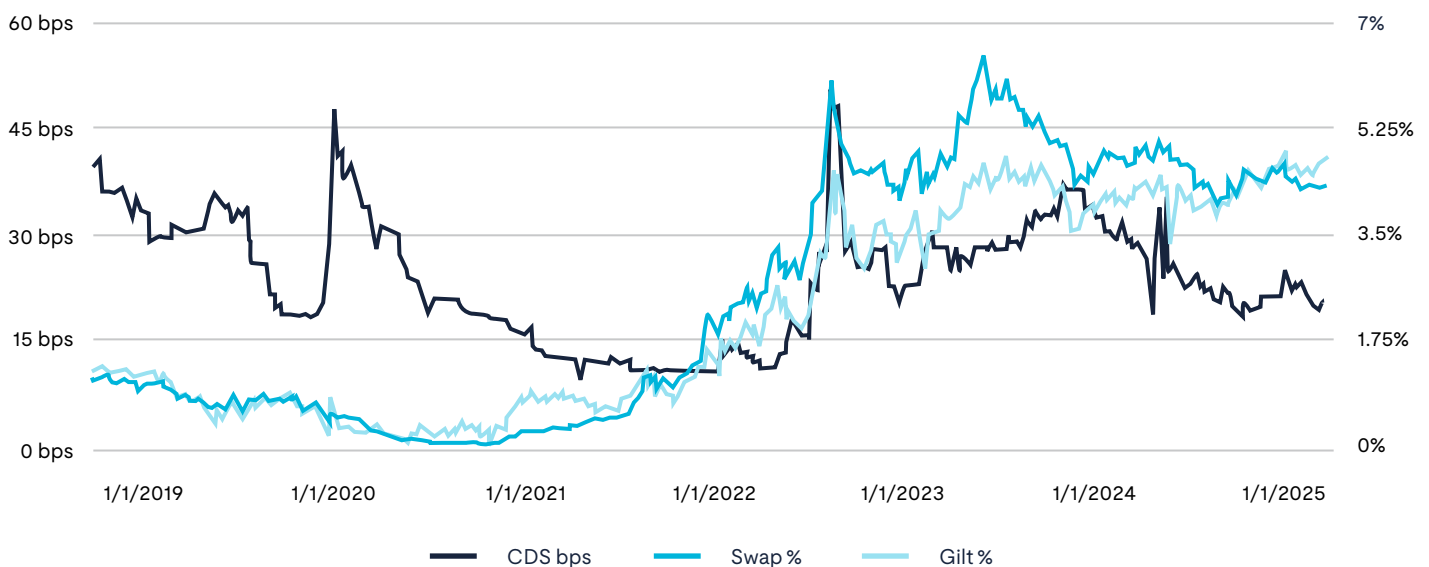
The Bank of England's base rate has been lowered from its peak of 5.25% in mid-2024 to 4.5%. Mortgage and development finance rates are influenced not just by the base rate but also by movements in medium-term sovereign gilt yields, swap rates, and credit default swap (CDS) indices, which are shaped by market sentiment on financial and fiscal stability, as well as geopolitical risks.

- **Bank rate** – Our wealth management team forecasts two further 25bps cuts in 2025, bringing total easing to 1.25% from peak levels.

- **CDS spreads** – These reflect financial sector creditworthiness. After spiking during COVID and the 2022 Mini-Budget, CDS rates rose again following weaker-than-expected growth data post the 2024 Autumn Budget.
- **Swap & gilt rates** – These remain sensitive to shifting short-term interest rate expectations.

Recent economic data has been mixed. GDP, retail sales, and services have outperformed expectations, but the manufacturing sector continues to struggle.

Fig.2 Key Lending Rate Drivers



The pound has appreciated by 1.9% over the past month against the dollar, but still is 2% below its 2024 peak, this has increased inflationary pressures on imported construction materials, though simultaneously making UK property more attractive to foreign investors. In the near term, anticipated interest rate dynamics should improve property lending conditions.

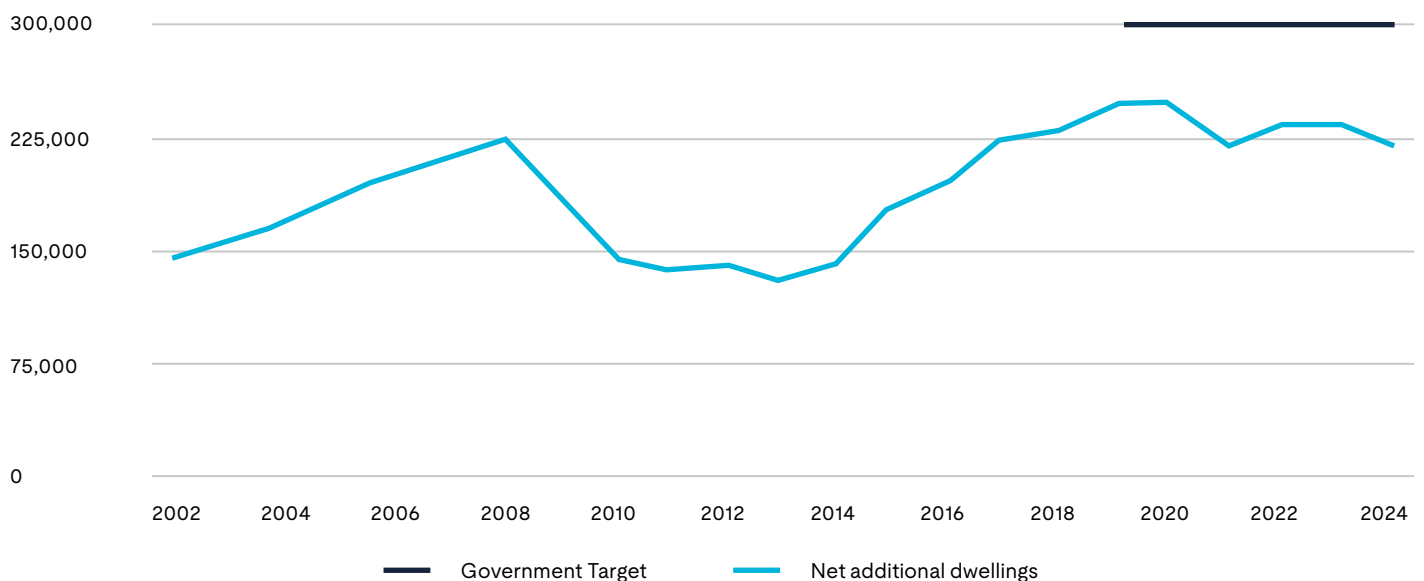
NIC increases has hit all levels of the supply chain and costs are being passed onto developers.

National market dynamics

We expect a surge in planning and development activity, likely to span an 18-month window.

The government's pledge to deliver 1.5 million new homes over its first term (300,000 per year) requires significant planning reform. Beyond new completions, conversions—such as splitting houses into flats or repurposing commercial buildings—could add around 20,000 homes annually.

Fig.3 UK Housing Stock



December 2024 saw the introduction of the Planning and Infrastructure Bill, decentralising land acquisition powers for affordable housing and reforming planning approval processes. Developers can now contribute to a Nature Restoration Fund instead of undertaking on-site environmental mitigation. The imposition of stamp duty on first-time buyers triggered a temporary sales surge, but demand is expected to cool as entrenched planning bureaucracy delays supply expansion.

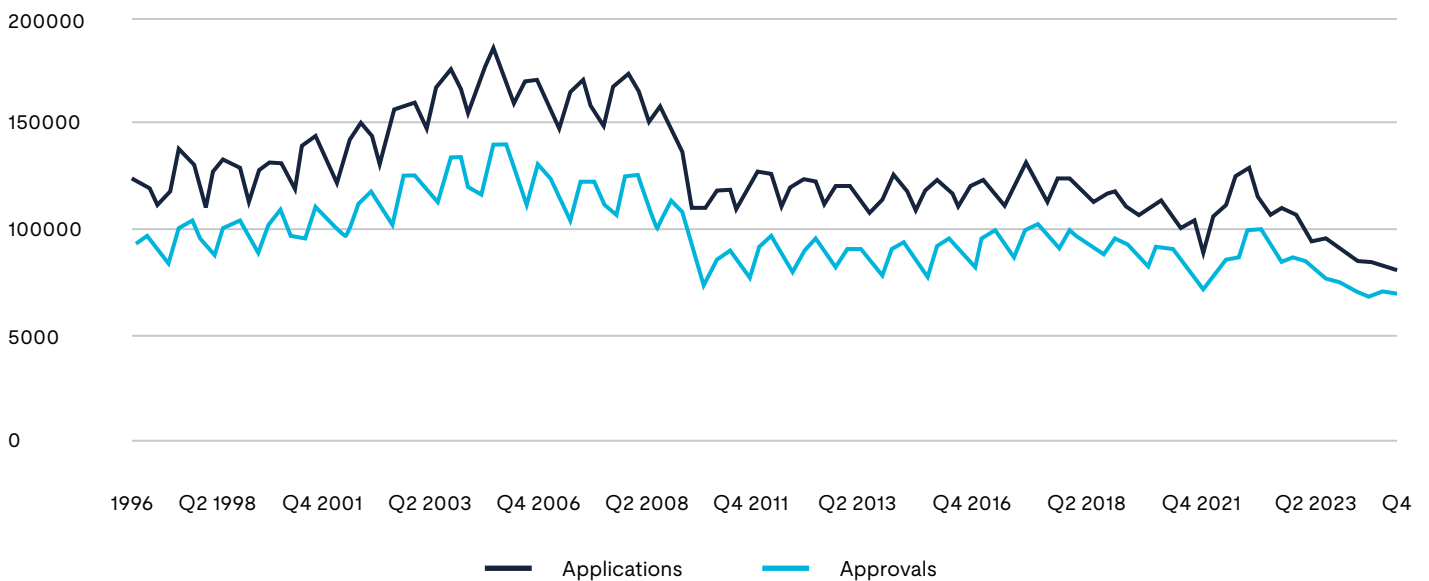
The national median price per square foot is £230, though this varies widely—London's new-builds average £325 per sqft, while the North averages £167 per sqft. Inflation was more pronounced outside London in 2024 due to weaker contractor pricing power. Going forward, analysts predict a 3–4% annual increase in building costs, with labour availability being the primary concern—only 13% of contractors in a Savills survey cited material costs as their biggest constraint.

Ongoing developments

Planning approval slowdowns have been uneven. According to NHBC data, seven out of twelve UK regions saw increased housing registrations in 2024, particularly in the North and Scotland, while London saw a 48% drop due to financial difficulties among affordable

housing associations. Fewer permissions in London and the Southeast could exacerbate shortages in these areas, whereas the Northwest and Midlands may see a more robust supply pipeline.

Fig.4 UK Building Applications and Completions



Higher gilt yields have pushed up benchmark lending rates and equity return requirements, straining project viability. Development lenders have significantly repriced debt.

- Senior development loans range from 6.5% to 10%+ depending upon the size and credit profile of the borrower.
- Mezzanine and junior debt costs are even steeper, typically in the low teens.

- Bridging finance remains expensive, typically 0.7%-1% per month; (8-12%+ annualized).

Simultaneously, rising yields have compressed development margins by lowering Gross Development Value (GDV). Many developers have had to reassess project feasibility, particularly in commercial sectors, where financing has become harder to secure without pre-lets or public sector anchor tenants.

Impact on developers

Residential

The cost squeeze is most acute for small developers, while large housebuilders have benefited from locked-in lower-rate land and economies of scale. In addition, building costs are continually outpacing the increases in land values, making it difficult to acquire finance. The top ten housebuilders saw only a 4% drop in housing starts in 2024, while smaller developers saw a 36% decline. This year, construction business optimism has been similarly subdued due to delayed decision making and global economic uncertainty. Many are mitigating risks by phasing projects, shifting to build-to-rent models, or securing equity funding.



Commercial

Demand for office space is evolving with hybrid work models. Prime offices (Grade A, energy-efficient, well-located) remain in demand, while secondary offices face high vacancy rates. New speculative office developments are rare unless backed by pre-lets or public sector tenants.

Retail continues to struggle with e-commerce shifts. While post-COVID retail footfall rebounded in 2022–2023, structural challenges persist. Developers are focusing on mixed-use redevelopment rather than new retail schemes.

A hypothetical example: If a developer assumed a 5% exit yield (i.e., 20× annual rent in value) but yields rose to 6% (i.e., 16.7× rent), end values would drop ~17%. With rising construction costs, many commercial projects have lost profitability unless significant savings or additional equity were secured.

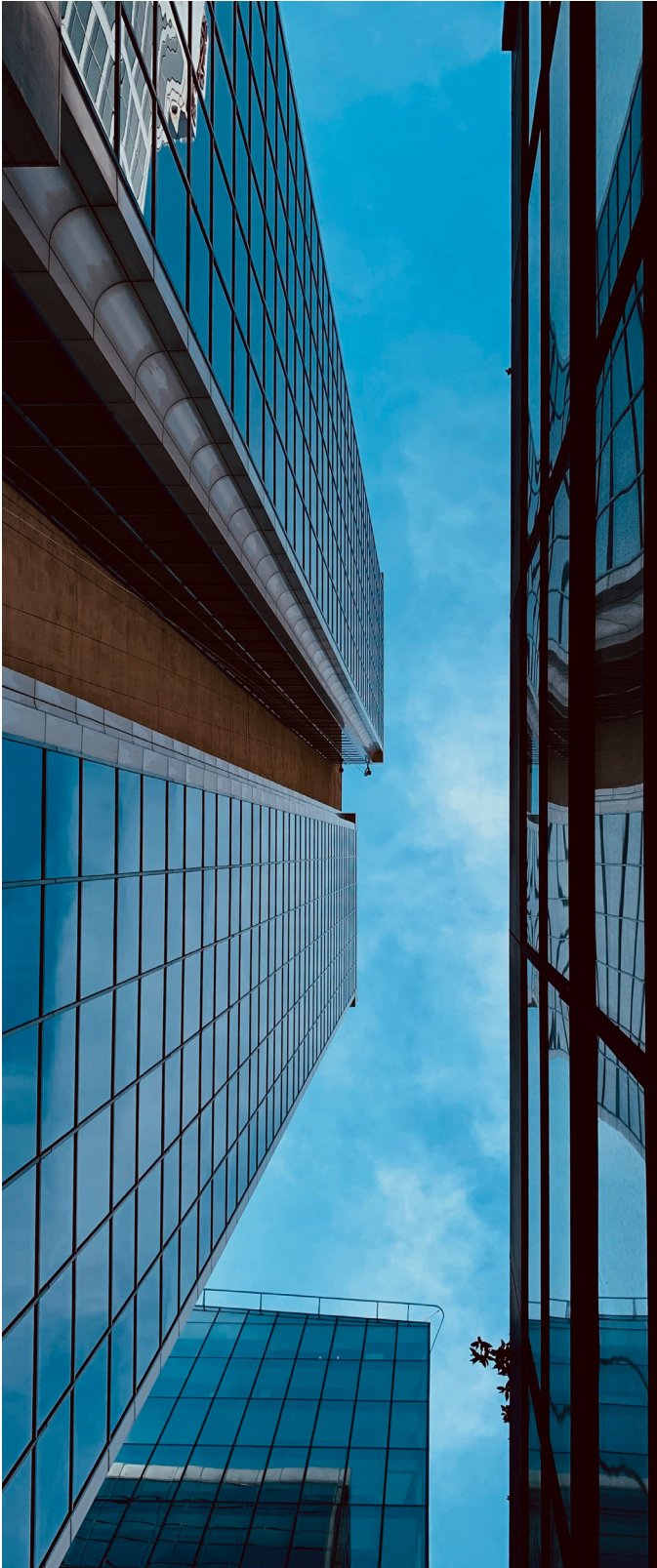
PBSA

The PBSA sector has expanded in university cities but faces challenges due to its reliance on forward funding. Given affordability constraints and rent caps, developers have turned to institutional investors rather than banks for financing, a higher-risk strategy in pursuit of better yields. This approach has facilitated developments in Manchester and Birmingham, alongside university partnerships that provide land and guarantees. PBSA remains in a growth phase, although growing valuer conservatism is starting to limit the quantum of lending available.



Across all sectors, a growing gap between lender panel valuations and developers' projections is slowing down deal flow. Lenders are taking a cautious, backward-looking approach, while developers' base valuations on future potential and market recovery. This disconnect is making it harder to secure funding, particularly for residential and regeneration schemes, pushing developers towards alternative finance and delaying project delivery.

Outlook and conclusion

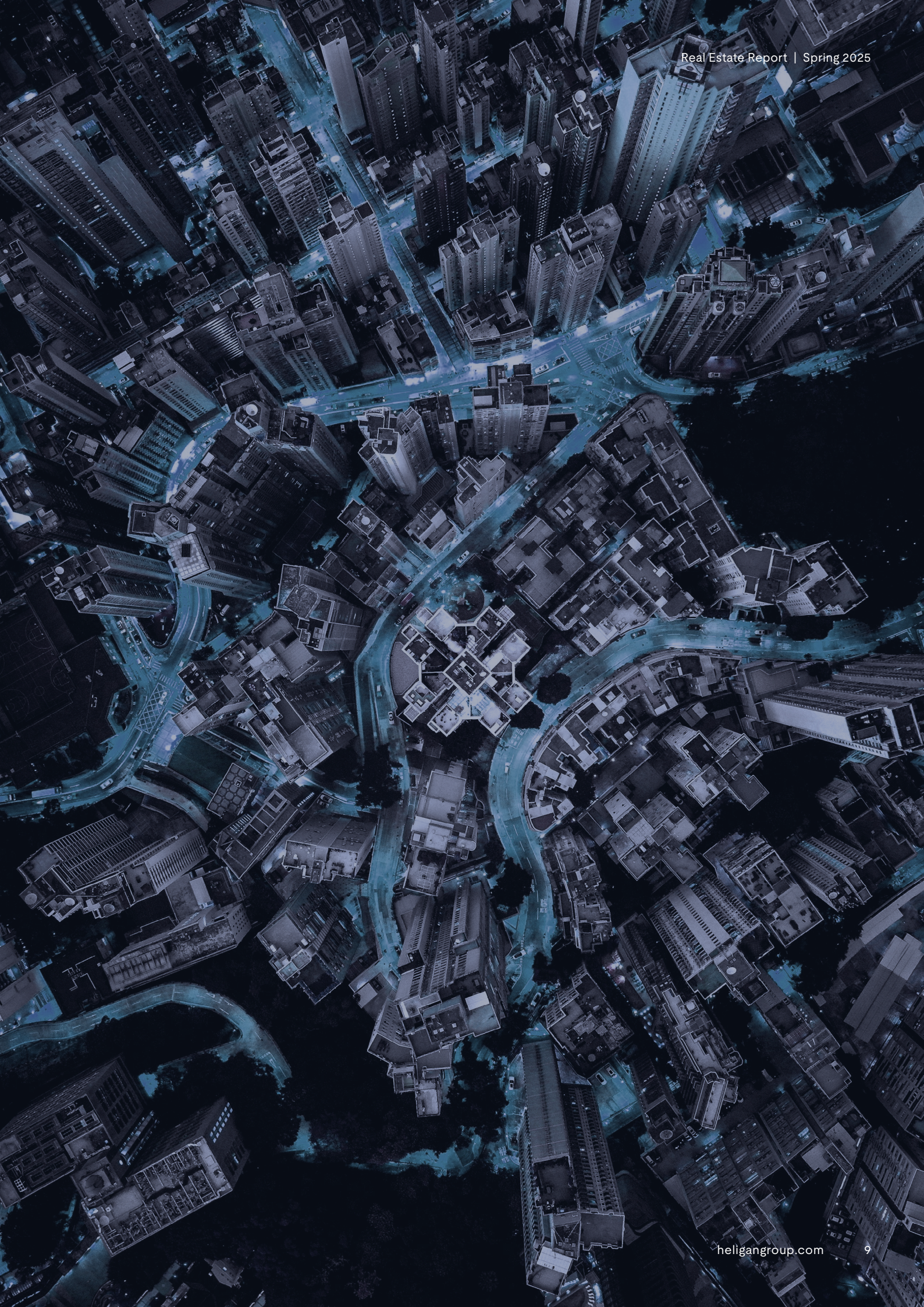


While property financing remains tight, the gradual easing of monetary policy should alleviate some pressure. However, stagnant GDP growth and cautious consumer sentiment pose risks. Housing completions in 2025 are expected to remain in the low 200,000s, with stronger growth anticipated in 2026. Inflation is moderating, with material costs stabilizing but labour constraints keeping overall inflation around 3% in 2025, dropping to 2% in 2026.

Regionally, the Midlands, North, and parts of Scotland should outperform in development. Meanwhile, London's housing supply remains constrained by financial uncertainty among housing associations. Commercial investment will focus on prime offices and life sciences hubs (Oxford, Cambridge, London), while secondary office markets and retail remain weak.

Key strategies for Developers

1. **Debt management:** Proactively refinance, engage lenders on covenant flexibility, and explore interest rate hedging.
2. **Alternative financing:** Consider mezzanine finance, private equity, and crowdfunding.
3. **Joint ventures:** Partner with landowners, major developers, or local authorities.
4. **Cash flow and phasing:** Prioritise early revenue generation and maintain liquidity.
5. **Value engineering:** Optimise design and renegotiate supplier contracts.
6. **Asset diversification:** Explore PRS, student housing, and senior living.
7. **Exit strategy:** Align with investors early and remain flexible on sales vs. rental plans.



About Heligan Debt Advisory

Heligan Debt Advisory specialises in structuring bespoke financing solutions for property development projects ranging from £10m to £100m. With deep expertise and an extensive network of lenders and private debt funds, we provide tailored guidance to clients navigating growth, restructuring, or fresh funding strategies.

Whether you are looking to secure capital for a new development or refinance an existing project, our team is here to support you with strategic, results-driven advice. If you are seeking funding solutions for your project, please do not hesitate to get in touch.



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