CHARLOTTE SQUARE
INVESTMENT MANAGERS

A VIEW FROM THE SQUARE

July 2025

The Quiet Revival - REITs Re-awakening

Entering July brings to a close the first half of what has been an eventful year so far, with President Trump's return to the White House bringing a familiar blend of tax cuts, deregulation, and trade protectionism. The newly passed "One Big Beautiful Bill Act" has cemented the 2017 tax cuts, slashed Medicaid spending, and rolled back clean energy incentives in favour of fossil fuel expansion. Wall Street, for now, is cheering with the S&P 500 recently reaching new all-time highs in dollar terms, but for Sterling investors, those that continued with a high unhedged position remain in the red year to date.

Across the Atlantic, however, performance could be found in the real estate sector that suffered terribly in 2022 on the back of rising interest rates. The Bank of England (BoE) is navigating a delicate balancing act between persistent inflation and a weakening economic outlook. The central bank has already cut interest rates four times since their 2024 peak of 5.25%, bringing the current rate to 4.25%. Markets are now pricing in two more cuts this year, likely in August and November, which would bring the base rate down to 3.75% by year-end. While the BoE has signalled a "gradual and careful" approach to easing, several factors could force its hand, we see an opportunity for the BoE to cut rates further and quicker than what is priced in. Why?

GDP Growth: Grew at the start of this year, largely supported by tariff frontrunning, but this has started to turn, with April showing a 0.3% contraction. This, coupled with rental prices slowing, which generally means that housing inflation will soon begin to decline, could prompt cuts to stimulate.

Weakening Employment: While employment levels have been strong for the last couple of years, they are showing signs of weakening with payrolls stringing a run of 3 months of contraction. Any uptick in unemployment or wage stagnation could shift the BoE's focus more squarely toward supporting demand.

Inflation Normalisation: UK inflation, currently at 3.4%, is still above the 2% target, but is expected to fall steadily. If inflation drops faster than expected - especially due to falling energy prices or easing supply constraints - the BoE would have more room to cut.

While much of the market's attention has been fixated on AI, geopolitics, and macroeconomic policy, a quieter resurgence has been unfolding in the world of real estate investment trusts (REITs). After a turbulent few years marked by interest rate shocks and valuation resets, REITs are once again drawing investor interest - not just for their defensive qualities, but for their growth potential. Falling interest rates are a powerful tailwind for REITs.

Lower Financing Costs: REITs are often capital-intensive and rely on debt to fund acquisitions and development. Lower rates reduce borrowing costs, improving profitability, and enabling more aggressive expansion or M&A activity.

Higher Valuations: As base rates fall, the relative attractiveness of REIT dividend yields increases. This tends to drive capital inflow into the sector, pushing up share prices and narrowing discounts to NAV.

M&A Acceleration: This year, we have benefited from takeovers of Urban Logistics and Care REIT and with capital becoming cheaper and valuations still recovering, we could see further consolidation or at least, company boards putting a more strategic focus on enhancing shareholder value.

The Bottom Line
If the BoE cuts rates to 3.75% or lower by the end of 2025, we see REITs as one of the most attractive plays in the UK market. Investors seeking income, inflation protection, and exposure to growing assets may find this a compelling entry point, particularly in sectors like student living, logistics and healthcare.

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