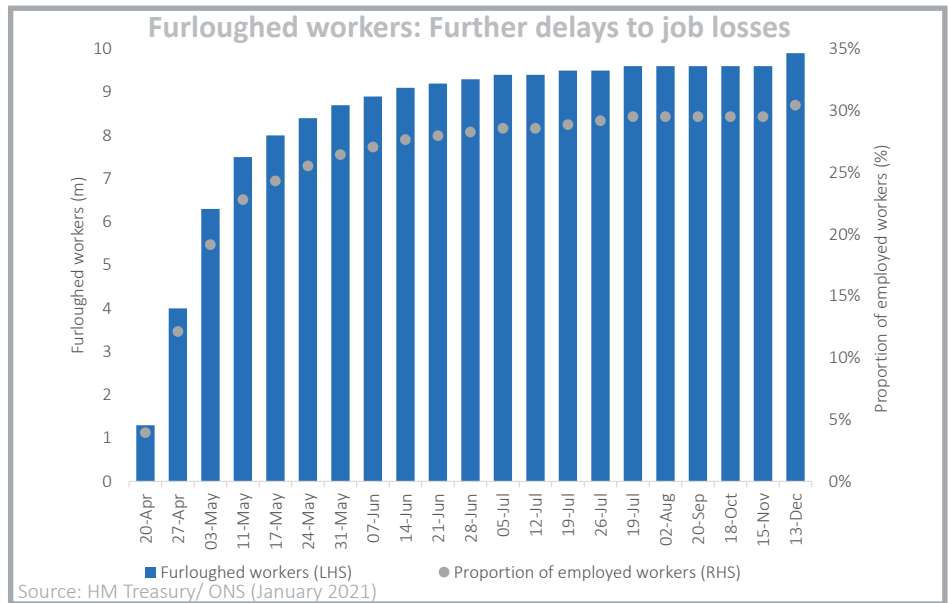


UK Economic Overview:

The pandemic had a strong negative impact on the UK economy last year. Despite a Q3 recovery, rising infections and new restrictions mean that we expect a regression of activity in Q4. We forecast GDP to contract -10.8% for 2020 overall. With stringent containment measures continuing into 2021, we expect a relatively weak Q1 but with widespread vaccination enabling a broader recovery towards the middle of the year. The UK seems well placed to achieve early herd immunity as vaccinations have commenced, public acceptance is high and the dosage order book is sufficient to cover the entire population. We predict UK GDP growth of 5.5% in 2021 meaning that the economy will not reach its pre-pandemic size until the second half of 2022.



In late December a narrow trade deal was agreed to avoid the UK exiting the EU on WTO terms. This prevented the sudden imposition of tariffs and quotas on most goods, averting major disruption. In the short-term, new border checks may still increase costs, cause delays and lead to supply shortages. This could weaken cross-border trade. There is currently no deal for services and until there is, the loss of automatic access rights to EU markets will create friction. Some financial activities have already been moved out of the UK, such as Euro-share trading. The longer it takes to sign a deal, the more cross-border services are likely to be lost.

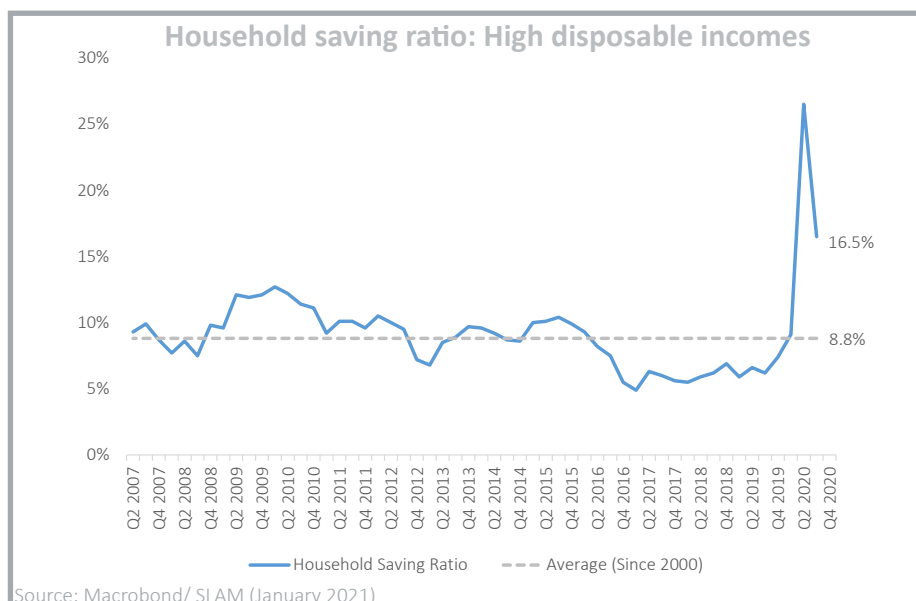
The UK's service sector recorded a PMI reading of 49.4 in December, indicating a marginal contraction. The manufacturing PMI rose to 57.5, a 3-year high, as UK manufac-

turers stockpiled and EU-based companies brought forward purchases ahead of the Brexit deadline. This implies that there will be a weakening of activity in Q1 2021. The construction PMI remained expansionary at 53.1 as activity was permitted to continued during the lockdown. The end of the stamp duty cut in March and weaker demand from commercial developments may cause a contraction in construction during 2021.

Forced closures throughout the pandemic have damaged the retail, hospitality and leisure sector more than any other. Generous government support measures, including the recently announced £4.6 billion package for businesses, have had only limited success in preventing retail administrations and CVA's. More are expected. Rolling lockdowns will further entrench online spending habits which

accelerated to compose over a third of total retail sales in November.

Travel restrictions, forced business closures and worker support packages has led to a doubling of the household savings ratio in 2020 relative to the long-term average. Periods of looser lockdowns have been accompanied by large retail spending rises and the high savings rate suggests significant pent-up consumer demand to be unleashed once the virus is contained. Unemployment was 4.9% in the three months to October and is being kept artificially low by the furlough scheme. Furloughed workers currently represent almost a third of the total UK workforce. As the scheme is currently due to end in April, rising redundancies may serve to dampen the expected resurgence in consumer spending.



The UK inflation rate (CPIH) remained low at 0.6% in November, having risen slightly in September due to food and clothing price increases. The narrow EU trade deal has avoided the inflationary pressure that would have accompanied a no deal Brexit. We expect inflation to remain modest at 1.6% in 2021 as the economy slowly recovers.

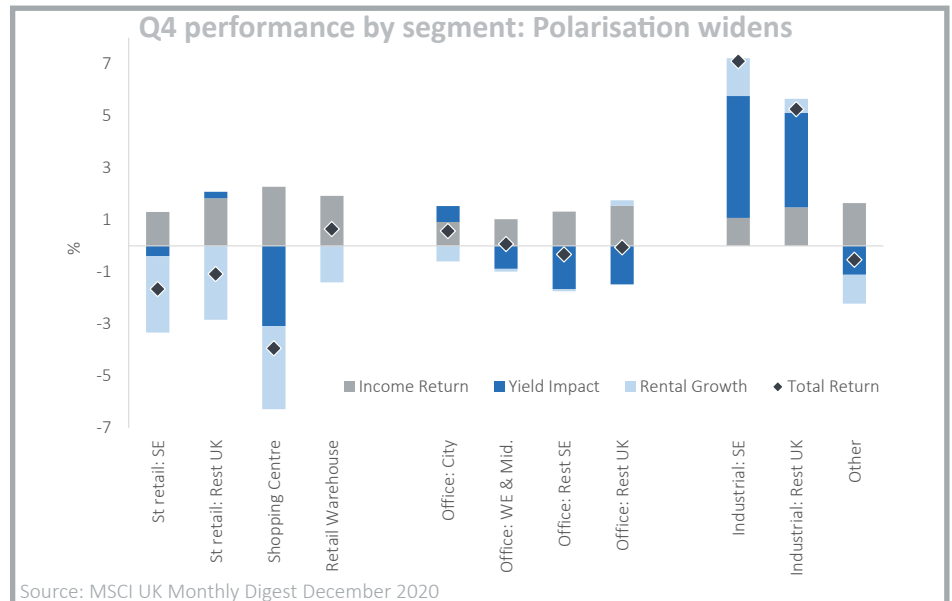
In the short-term, coronavirus restrictions and new EU trading agreements will hold-back the UK economy. The recovery will depend largely on how fast vaccines can be administered, the effectiveness of government support and the level of EU trading friction which emerges. Having avoided a no deal Brexit and with the vaccination program in full swing, we are optimistic that mid-2021 will herald the start of a broad-based economic recovery.

UK Property Market:

Preliminary data indicates that Q4 saw the largest quarterly transaction volumes of the year, amounting to some £12.6bn. This was still 29% below Q4 2019, largely due to weaker investment into offices and alternatives. Annual volumes in 2020 were 24% below the 10-year average and the weakest since 2012. Transactional activity is expected to remain constrained until the impact of the new EU trading agreement and coronavirus containment measures become clearer. Liquidity should improve towards the middle of 2021 in line with the wider economy.

UK All Property returns came under pressure last year but still held up better than had been expected at the start of the pandemic. Based on the MSCI monthly index to December, quarterly and annual total returns equated to 2.0% and -1.0% respectively. Polarisation between and within asset classes has become more pronounced. The rate of capital loss is slowing and monthly values returned to growth in November. Performance should improve this year. The latest IPF Consensus (November) predicts a total return of 1.5% in 2021 and 7.1% in 2022.

Industrial was the stand-out performer in 2020. On an annual basis the sector returned 8.7% and both yield compression and rental growth were evident. South East Industrial performed particularly well. Occupational activity in 2020 was the highest ever at over 50 m sq ft for “big box” (> 100,000 sq ft) warehouses according to Savills, fuelled largely by booming online sales. Online penetration rates will permanently settle at much higher levels

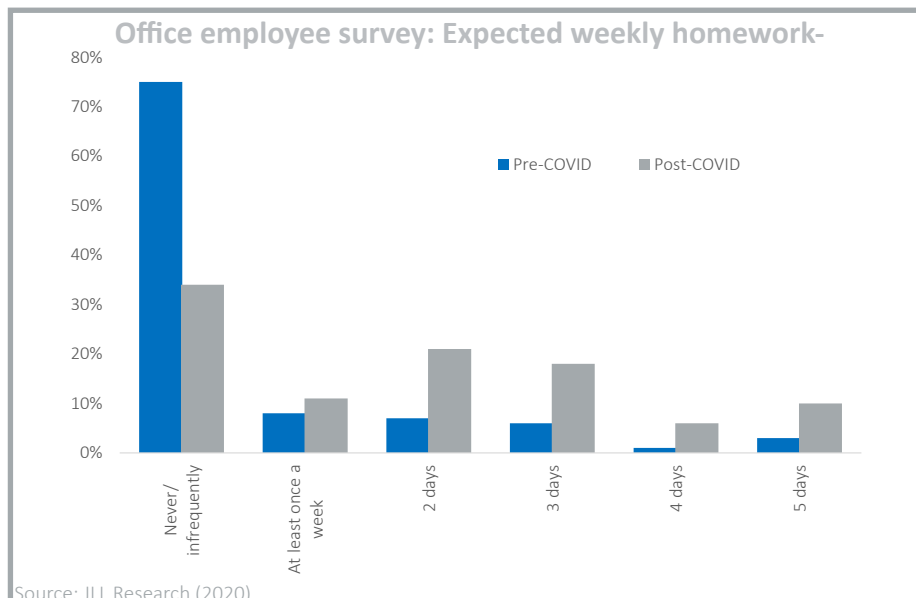


post-pandemic, which will maintain demand particularly in supply constrained locations within or adjacent to major conurbations. The impact of the new EU trading agreements remains to be seen. Whilst it is likely that more inventory will be stored domestically, more direct shipments between Ireland and Europe would curtail some demand.

Offices returned -0.9% during 2020 and capital values fell -5.7%. Take-up was weak and availability has risen, especially for sublet space. Occupiers are fundamentally altering their preferences which will only become fully visible on lease events. The future office will be a human-focused space for collaboration, socialising and creativity as well as a corporate showroom. Repeated surveys show that most employees expect a mix of office and home-based working post-pandemic. This is likely to

mean less demand for space per occupier but far greater emphasis on quality and service. We expect rapid performance polarisation with stable or rising rents and compressing yields for suitable stock and rental and capital loss for stock misaligned to modern occupier requirements.

Retail is at the epicentre of structural and cyclical trends. Food and discount retailers which remained open have traded strongly but others are under extreme pressure. Annual total returns for retail to December were -10.8% with capital loss of -16.9%. Shopping centres were worse affected with capital loss of -26.6% compared to -14.9% for retail warehousing. Given new lockdowns during the crucial Christmas trading period, more retailers without an online platform will permanently close stores or enter administration.



Resilient performance coupled with under-supply, consumer demand and a non-discretionary income profile implies that the living sector will remain a major investor focus in 2021. Accessing stock directly is challenging so investors must adopt more active and engaged strategies like forward-funding or developer/ operator partnerships.

Last year was extremely turbulent for UK real estate. Structural changes expected to materialise over 5 to 10 years were brought forward, rapidly creating winners and losers. We expect these trends to gather momentum in 2021 against a backdrop of improving market sentiment, rising liquidity and stronger occupier demand for winning assets and locations.