CASTLEFORGE

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WHAT'S NEXT FOR THE LONDON OFFICE MARKET?

Things feel different in the office market as of late. After a long hiatus, institutional investors are coming back into the office sector, looking for opportunities in the prime end of the sector. State Street's acquisition of 100 New Bridge Street in April as well as the partnership between Aware Super and Delancey to invest £1 billion in London offices ring a bell. Blackstone, meanwhile, is making good on its earlier "game on" announcement for offices through its acquisitions of Tokyo Garden Terrace Kioicho and Centre d'Affaires Paris Trocadéro.

It's invigorating to see the change in mood from our perch in London. However, as the market reaches a new milestone in recovery, we also recognise this moment as an opportunity to think retrospectively and ponder what's next for the sector.

We emphasize the strong supply and demand story in the London office market as a key reason why large investors are returning to the space. A lot of the demand in recent years has been driven by a wave of occupiers in highly productive knowledge economy sectors.[1] Large multinational firms in fields such as law, finance, consulting, and professional services have been pushing their employees to spend more time working in-person despite the fact that much of their work can be done anywhere with an internet connection.

The apparent disconnect between being in an industry that is theoretically capable of working remotely and company culture pushing for more in-person time has led to the narrative that having a best-in-class office is the only way for firms to attract and retain talent. This was predicated on the assumption that workers could only be drawn out of their homes if the office became a destination. The effectiveness of this narrative is clear – the first wave of post-lockdown occupiers has pushed through rental barriers, driving up occupation costs even as fit-out and construction expenses mount throughout London. At the same time, offices have scrambled to enrol in WELL Programs and improve amenities.

We don't disagree with this narrative – we apply the same principles to our developments at 75 London Wall and 1 Golden Lane. We pat ourselves on the back for being among the first to highlight the bifurcation of the office market back in 2020, when we argued that the "bookends" of success in the office market would be both prime buildings and flexibly managed spaces.

However, our read on the short term situation is that the "prime or nothing" narrative might be quieting down as demand deepens. Global cities like London have settled into a hybrid equilibrium. Workers in the US and UK spend 1.6 and 1.8 days per week working from home, respectively.[2] While a substantial amount of American workers in the latest Survey of Working Attitudes and Arrangements report that they want full-time WFH, a *majority* of employees want to spend at least some of their time in person, suggesting that offices will remain a part of working culture for the time being.[3]

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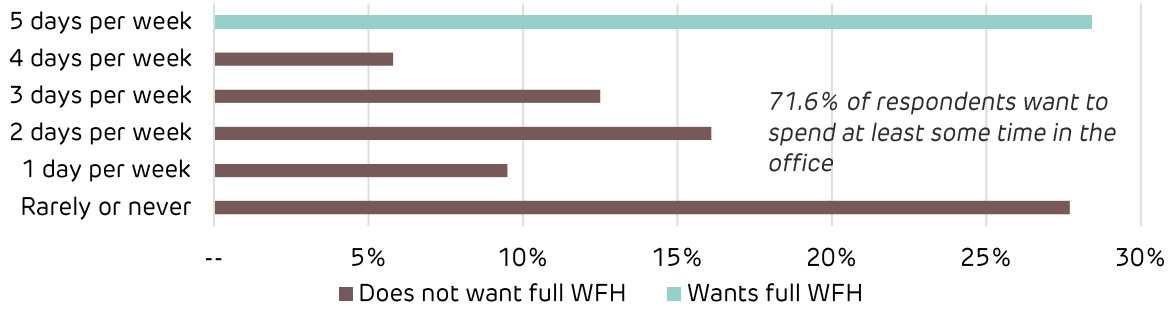
[1] Productivity as measured by average incomes for employees

[2] Working from Home in 2025: Five Key Facts | Stanford Institute for Economic Policy Research (SIEPR), Responses to the question "For each day last week, did you work 6 or more hours, and if so where?" N=16,422 college-educated workers in 40 countries surveyed in November 2024 – February 2025.

[3] Working from Home in 2025: Five Key Facts | Stanford Institute for Economic Policy Research (SIEPR) Survey conducted among American workers.

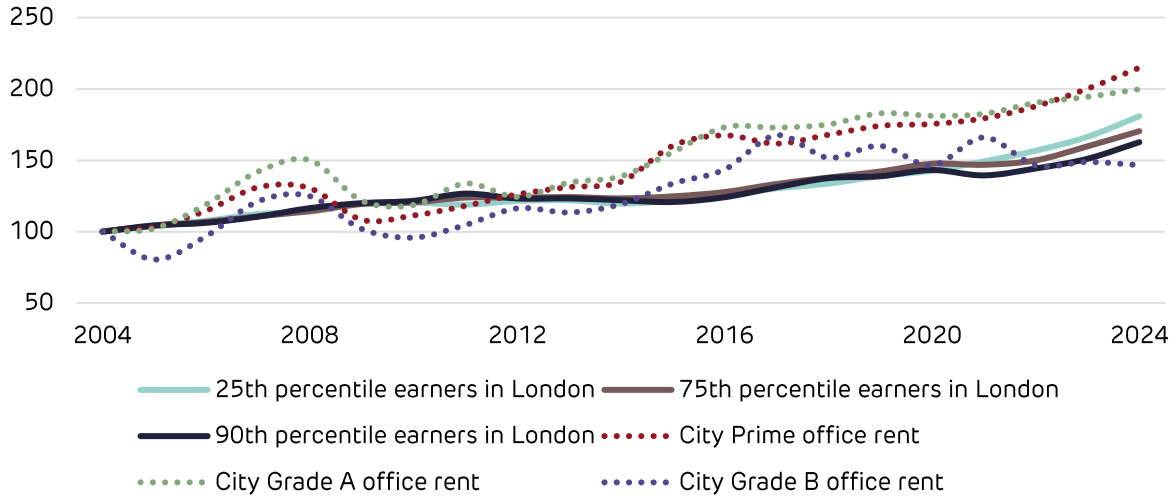
Figure 1: Number of days per week US workers want to spend working remotely[4]



While many employers were unwilling to commit to office leases in the past few years, we think the mounting data in favour of in-person time might convince the hesitant to make their move. This second wave of occupiers will likely be driven by firms outside of the white-shoe, "at any cost" profile that defined the first. These firms are likely not looking to spend £80-100 per foot on an office (and that's before accounting for elevated fitout costs and business rates), even if that price tag comes with trendy features like pickleball courts or custom fragrances.

What they will be looking for, however, is convenient transit access in dense urban areas. Easy access to multiple train stations, for example, essentially represents a reduced cost of commuting for employees and benefits employers by giving them a larger catchment area for potential new hires. Transit-dense areas also tend to be in highly urbanised settings, which can help allay the lack of amenities in an office building. An older building in EC2 might not have an artisanal coffeeshop in its lobby, but it probably isn't a long walk from one either!

Figure 2: Indexed growth of office rents vs salaries in London[5]



[4] Responses to the question: "Looking one year ahead, how often would you like to have paid workdays at home?" Data from the Oct-24 to Sep-25 SWAA waves. The sample includes full-time wage and salary employees (i.e. who worked 5 or more days during the survey reference week) who have work-from-home experience during the pandemic and pass the attention-check questions. N = 36,405.
[5] ONS, Savills. Income growth refers to income excluding overtime.

Since around 2015, office rents for Prime and Grade A spaces have generally moved in the same direction as income growth, meaning that the relative shares of office occupancy and employee salaries were the same on a cost sheet.

Lately, however, we see that Grade A and B rental growth has slowed relative to income growth. As the previous figure shows, rental growth between 2022 and 2024 reached +6.5%, as opposed to wage growth of around +13.9%. If trends hold, an occupier paying market rents on a Grade A/B building in the City might find that the rising cost of rent are less impactful to their P&L than the cost of labour. This divergence creates an opening for the second wave of occupiers we've been discussing – firms that want quality and location but don't need best-in-class amenities.

If demand deepens as we expect it to, it will be crucial to position ahead of where the next wave of occupiers will emerge. Grade A buildings in transit-rich locations offer precisely this opportunity. They sit at the intersection of genuine occupier need and relative value, which is a far more sustainable foundation than speculation on which building will win the amenities arms race. After all, most employees would probably trade the office fragrance consultant for a Tube station that actually gets them to work on time.

LIFE SCIENCE REAL ESTATE: THE SOLUTION THAT WASN'T

A few years ago, we considered expanding Clockwise by developing a turnkey flexible lab space platform for startups and small teams in the life science sector. This would be done by converting underutilised offices into lab space – a trend that garnered plenty of coverage among property sector commentators at the time.

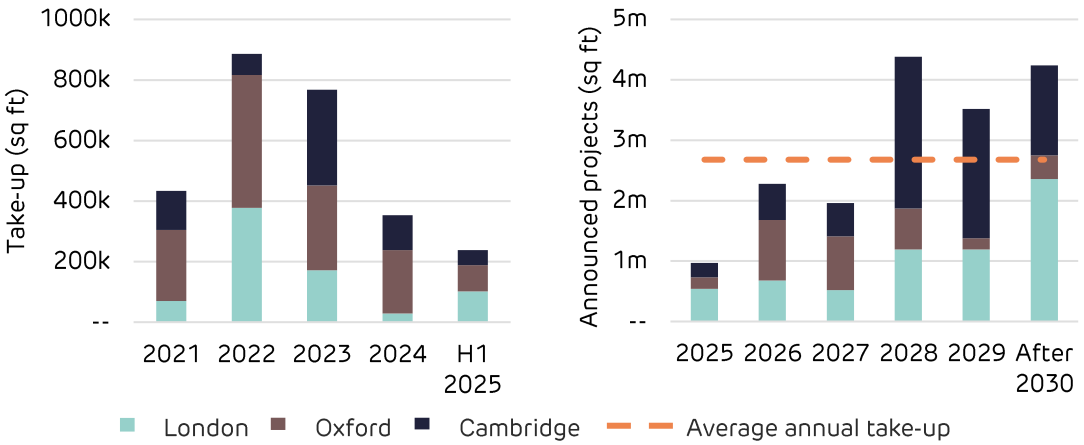
From our perspective, such an expansion would have made a lot of sense. An ongoing funding boom for life sciences at the time was creating demand for fitted labs for startups. Additionally, around 40% of a laboratory tends to be traditional office space, so we'd have some transferrable skills. Another advantage was that most of the UK's demand for lab space is concentrated in the "Golden Triangle" between Oxford, Cambridge, and London, which means that we would be working in familiar territory.

So, why isn't there a "labs" page on the Clockwise website?

As we examined the office-to-lab conversion strategy, we raised several concerns in an internal note. One key issue was that we weren't convinced the UK faced a structural undersupply of relevant space. The data was too limited to make a credible argument, and many analyses merely pointed out that the UK had less available lab space relative to the US. We also weren't certain that there would be enough credit tenants to support a buildout of new, premium space. Turnkey lab space offerings would largely go to pre-revenue startups engaging in highly speculative work for years due to lengthy safety and approval processes. As a result, we decided not to proceed with the project, believing that the drivers at the time were unsuitable for a long-term strategic pivot.

In the years since, we think we made the right decision. Data from CBRE shows that there has been a growing supply-demand imbalance in the sector, as investor capital piled in to convert offices and build out new lab space – even as take-up declined year after year since 2022.

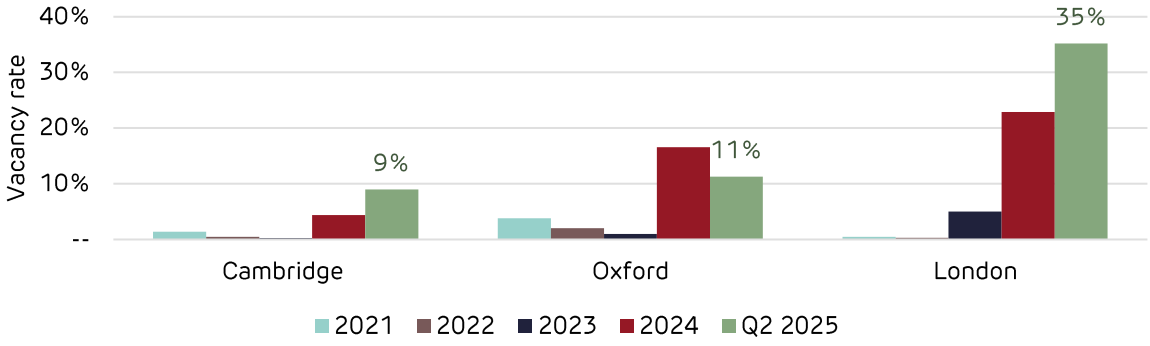
Figure 3: Falling demand, rising supply in the UK life science sector[6]



The supply/demand issue is likely to worsen, as around 9.6 million square feet of space is expected to be delivered by 2028 – which equates to around 16 years' worth of average take up in the Golden Triangle. Unless many of these projects are scrapped, such oversupply is likely to hinder effective rental growth and improvements to vacancy rates, which sit at 9% in Cambridge, 11% in Oxford, and 35% in London.

News for the UK's life sciences sector has also taken a negative turn lately, with large companies like Sanofi, AstraZeneca, and Eli Lilly pausing UK investments and Merck backing out of its £1bn London Research Centre across from St Pancras Station. The Ellison Technology Institute, meanwhile, is scaling back on its earlier commitment to invest £10 billion in a science campus near Oxford.

Figure 4: Golden Triangle vacancy rates 2021-Q2 2025[7]



Overall, there seems to have been a misallocation of capital relative to the size of the life science market in recent years. For comparison's sake, take-up in the Central London office market is around 10 million square feet per year and has remained at that level for the past three years. Despite falling vacancy rates and shortages of relevant space, there's only around 21.3 million square feet of new stock in the pipeline to 2028 – equivalent to around two years of take-up.[8]

A few weeks ago, we joked in one of our research meetings that the narrative of life science saving the office market has reversed and that offices might end up rescuing lab space. Alexandria Real Estate

[6] CBRE
[7] Cushman & Wakefield
[8] Savills.

Equities, one of the largest life sciences REITs in the US, seems to agree. Deep in their 2024 10-K, we found a passage that we think reflects the absurd whiplash of market better than we can.[9]

> The increase in demand for premium office space in 2024, primarily driven by the tech sector, particularly companies focused on AI, absorbed some of the market's previously misguided office-to-lab conversions, which are now being repurposed back into modern office environments. High ceilings, improved ventilation systems, and abundant natural light have become highly desirable features, appealing to office tenants. This trend is expected to lead to the exit from the life science sector of inexperienced life science real estate developers and expedite the resolution of the oversupply.

"Misguided" is certainly one way to put it. As it turns out, converting offices with high ceilings, natural light, and good ventilation – which appeal to a broad tenant base across many business sectors – into highly specialised laboratory spaces has proven challenging in the long run. Who could have guessed?

LOCATION, LOCATION, COMPUTATION

The current arms race to build out data centre capacity is hard to ignore. Meta is planning to build a data centre the size of Manhattan, while xAI is raising $12 billion for a second "Colossus" facility near Memphis. While Europe is less exposed to the capex boom, there are still some large deals going on, such as Blackstone's partnership with QTS in Northumbria. In total, these eye-catching hyperscale projects amount to hundreds of billions of dollars in collective spending, drawing in investment capital from around the world. Yet while hyperscale data centres dominate headlines, smaller, strategically positioned facilities also offer worthwhile investment opportunities due to their proximity advantages, steady inference demand, and downside protection.

We use the term "urban edge" to refer to data centres that provide low-latency connections to end users while also providing enough power density to support AI inference and application training workflows (up to roughly 50 kW per rack). These urban-adjacent facilities typically offer tens of megawatts of total capacity and can host multiple tenants. For comparison, an AI training facility for larger, general-purpose LLMs may aim to provide hundreds or thousands of megawatts for end users such as Meta or OpenAI. What they sacrifice in scale, urban edge sites compensate through strategic positioning and low-latency connections to the populations that actually use AI models on a daily basis.

For enterprises seeking to deploy AI applications on their proprietary data, the calculus looks different from that of hyperscale training. These businesses rarely need the colossal power budgets required to train frontier models with hundreds of billions of parameters. Instead, they may prioritise secure, low-latency access to their own data and the ability to iterate locally within regulatory constraints. This makes smaller, urban-adjacent facilities particularly attractive, as they can support fine-tuning and inference workloads without the prohibitive costs or logistical complexity of remote hyperscale sites. In effect, proximity to data becomes a competitive advantage, enabling enterprises to integrate AI into production environments without sacrificing speed or compliance.

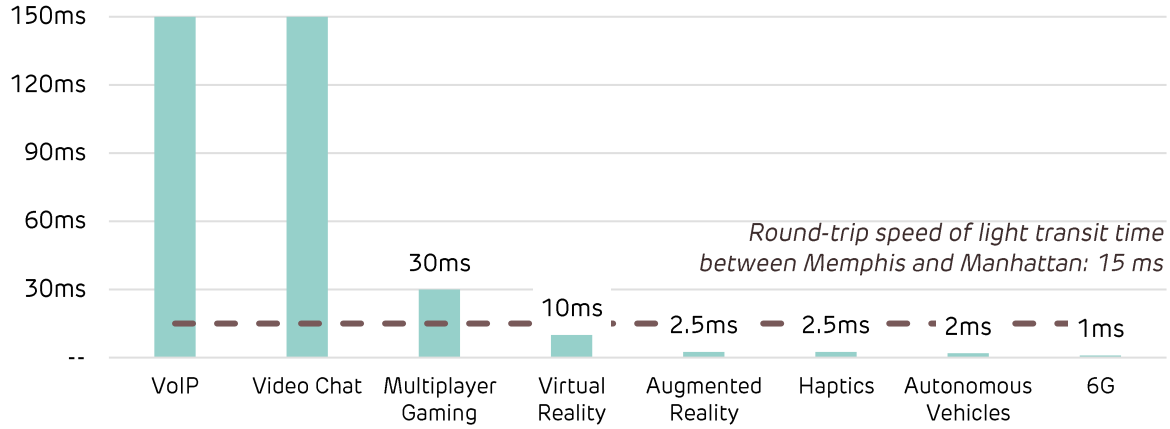
More generally, urban-edge facilities are critical to support growing demand for AI inference workloads. Unlike the one-off nature of model training, inference represents continuous demand. Tasks like ChatGPT queries, AI-enhanced web searches, and content generation for social media

[9] See also: WSJ: This Once Hot Real-Estate Type Is Now Being Offered as Office Space, PERE: Rethinking the Life Sciences Sector Beyond the Lab

aren't just done once. Rather, they require that models are inferenced millions of times a day, providing a steady driver of demand for inference-capable data centres.

Within the realm of inference work, we expect that there is significant scope for latency-dependent tasks to become more popular. Workloads that measure end-to-end latency in mere milliseconds include virtual reality, augmented reality, and autonomous vehicles. High frequency trading is even more stringent, with clients investing massive sums to shave microseconds off of trading times. Given that the speed of light is between 200 and 300 km per millisecond (depending on the medium of travel), there is a maximum limit for where servers can be located relative to their latency-sensitive end users, making far-off training data centres infeasible for some use cases. Indeed while the Colossus supercluster is able to train xAI's Grok models, inference is handled by cloud providers.

Figure 5: End-to-end latency requirements[10]



Another point to note is that while hyperscale data centres have larger power demands than urban edge sites, it may be less complicated to build out the power capacity needed for their operation. By siting in remote areas, hyperscale developers are able to create their own power infrastructure, leading to creative solutions. For example, xAI is importing a power plant from abroad to power its data centres, and Google is working with a nuclear power startup to develop small modular reactors (SMRs) to run alongside its data centres. Try getting *that* past a planning commission in London.

These simple (if heavy handed) solutions don't apply in urban environments. While data centres need large amounts of power concentrated in just one source, urban grids tend to be fragmented among many substations, often making available power capacity inadequate for use (if there's any power capacity in the first place). Moreover, the complexity of urban grids can drive up upgrade costs by orders of magnitude relative to rural locations, making it infeasible for data centre developers to fix these issues themselves. Stricter emissions regulations and noise ordinances in populated areas add further complexity to urban deployments. These challenges form a moat that can work in favour of successfully positioned urban facilities, potentially limiting competitive supply and supporting pricing power over time.

A final note for risk-conscious investors is the superior downside protection offered by core and edge facilities. The AI revolution, while impressive thus far, remains subject to the same boom-bust cycles that have characterized previous technological transitions. We saw that dynamic play out in China, where the market continues to deal with oversupplied compute resources, much of which is located in remote locations. The issue isn't necessarily limited to China, either. A former Meta executive

[10] Breaking the Latency Barrier - IEEE Spectrum, speed of light in fibre optic cable assumed to be 200 km/ms

recently noted the risk of assets becoming stranded as the industry progresses with its historic buildout of hyperscale capacity in places like Louisiana, Texas, and Ohio.

In contrast, we are more confident that urban-adjacent facilities possess inherent resilience. These locations were experiencing declining vacancy rates and rising rents before AI became a major source of demand, supported by traditional enterprise deployments and conventional data processing needs. Should LLMs go the way of the NFT, we expect that urban edge investors will benefit from the continued demand of non-AI computing tasks.

The investment calculus is becoming increasingly clear. While hyperscale facilities capture headlines and venture capital, core and edge data centres offer a more compelling risk-adjusted proposition for income-focused investors. They provide direct exposure to the inference economy – where AI's long-term value actually gets realised – while maintaining the diversification benefits of serving traditional enterprise demand.

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