Sponsored by:

awh anderson wilde & harris EXPERTS IN PROPERTY

RICS

The downturn in the retail sector is far from over

UK Economy and Property Market Chart Book

Q4 2019

rics.org/economics

Contents

September saw the launch of the International Construction Measurement Standard (ICMS2) developed by a 50 strong global coalition of professional bodies including RICS. Its purpose is to bring greater transparency to construction costs. Click here to find out more

RICS Survey Release Dates

Frequency	Survey	Period covering	Release date
Monthly	RICS Hong Kong Residential Market Survey	October	21-Nov-19
Monthly	RICS Portuguese Housing Market Survey	October	29-Nov-19
Monthly	RICS UK Residential Market Survey	November	12-Dec-19
Monthly	RICS Hong Kong Residential Market Survey	November	12-Dec-19
Monthly	RICS Portuguese Housing Market Survey	November	20-Dec-19
Monthly	RICS UK Residential Market Survey	December	16-Jan-20
Monthly	RICS Hong Kong Residential Market Survey	December	16-Jan-20
Quarterly	RICS UK Construction Market Survey	Q4 2019	23-Jan-20
Quarterly	RICS Global Commercial Property Market Survey	Q4 2019	30-Jan-20
Quarterly	RICS UK Commercial Property Market Survey	Q4 2019	30-Jan-20
Monthly	RICS Portuguese Housing Market Survey	January	31-Jan-20
Quarterly	RICS Global Construction Survey	Q4 2019	06-Feb-20
Monthly	RICS UK Residential Market Survey	January	13-Feb-20

Economic outlook

The latest estimates by the ONS point to quarter-on-quarter GDP edging up by 0.3% in Q3 2019. Although this represents a pick-up in output following a modest decline in Q2, this result still came in below the consensus and the Bank of England's forecast of 0.4%. Significantly, there is little reason to anticipate a material pick-up in momentum in the run up to the end of the year with the drag from heightened economic and political uncertainty as well as a weakening global picture continuing to depress UK growth.

The picture remains particularly downbeat across the retail portion of the commercial property market

Furthermore, this year will go down as having been a particularly challenging one for the high street. Mainly on the back of the ongoing structural shift towards online shopping, there were almost 2,900 store closures in the first half of 2019 (estimated by PWC), the highest in over five years. Meanwhile, a whole host of household names including Marks & Spencer, Debenhams, Homebase and Mothercare are looking to scale back their footprint. This has been exerting significant pressure on the retail portion of the commercial property market with key indicators suggesting it is, if anything, becoming more pronounced. According to CBRE, retail rental values have declined in each the last four quarters.

Around a fifth of all retail sales are now made online compared to just 5% a decade ago. Retail landlords have had to bear the brunt of this enormous change in consumer spending habits.

These challenges are most clearly visible through the responses to the RICS UK Commercial Property Survey, which show that, in net balance terms, availability of vacant retail space has risen sharply in the past two years. In turn, landlord incentives provided to tenants, such as rent-free periods, have risen for ten straight quarters.

Against this backdrop, retail rental values are expected to fall further in the near term. RICS contributors expect prime rental values to drop by 4% over the next twelve months. Projections for secondary space are more downbeat in comparison, with rents envisaged to decline by around 7% over the same period.

Demand for industrial space is continuing to rise however

The counterpoint to this is the more positive feedback we are receiving on the industrial/logistics segment of the market. RICS indicators continue to point a pick-up in demand for well located industrial sites which should translate into an increase in rental values over the coming year particularly in prime locations.

The labour market is likely to remain tight

Significantly, retail spending is currently still growing at an annual clip of around 3% which bears out the perspective that the state of the high street may not be reflective of the health of the consumer. Indeed, it is likely that household demand will remain reasonably solid, at least in the coming months. The unemployment rate is still close to multi-decade lows at 3.8%. Moreover, this is now putting upward pressure on pay growth, wages increased by 3.5% on an annual basis in September 2019, a stronger trend relative to the last few years.

The continued lack of clarity around Brexit is likely to mean that businesses will want to continue to drive their existing capital stock harder in the near term rather than stepping up big-ticket investment programmes. This is likely to continue to support employment growth in the near term. Furthermore, inflationary pressures look set to remain soft for the foreseeable future; this should help support household purchasing power.

The MPC will keep rates on hold

A huge question mark hangs over any projections for the economy in 2020. One thing most forecasters seem to agree on is that a no-deal Brexit outcome will at least lead to a short term hiatus in the economy and, very probably, some form of recession. How extended this might prove to be would depend in part on the policy response but also on the speed with which new trade deals can be pulled together.

The lack of clarity on the outlook helps explain the current cautious approach from the Bank of England. At least for the coming months, we expect the MPC to sit on its hands and leave interest rates at 0.75%. Looking further out, it is conceivable that the Bank could follow the lead of the US Federal Reserve and the ECB and adopt a more accommodating monetary stance if conditions so warrant.

Uncertainty is causing buyers and vendors to hesitate

Key metrics capturing demand and supply in the RICS Housing Market Survey remain entrenched in negative territory with a raft of comments from contributors suggesting that the Brexit impasse is dissuading both buyers and vendors. This negative trend appears to be feeding through to the overall sales numbers, with the RICS agreed sales indicator consistent with a renewed fall in activity in the coming months, although so far the hard data (by HMRC) on transactions has remained relatively resilient.

In the lettings market, the latest set of results continue to point to a drop in new landlord instructions coming through to agents on the back of changes in the tax treatment of investment properties. It's unlikely there will be a material change in this trend over the coming months. With demand expected to continue outstripping supply, rent expectation remain positive for the coming year.

Pace of construction output growth has moderated

The headline RICS workloads series is pointing to a dip in momentum across the construction sector. In the latest set of results, growth in workloads slowed across all segments of the market including private housing which suggests that it is going to prove difficult to lift housing supply much above the current run-rate. It is also noteworthy that business enquiries for new projects or contracts in the past three months, which had averaged a net balance of 15% over the previous year are now reportedly flat.

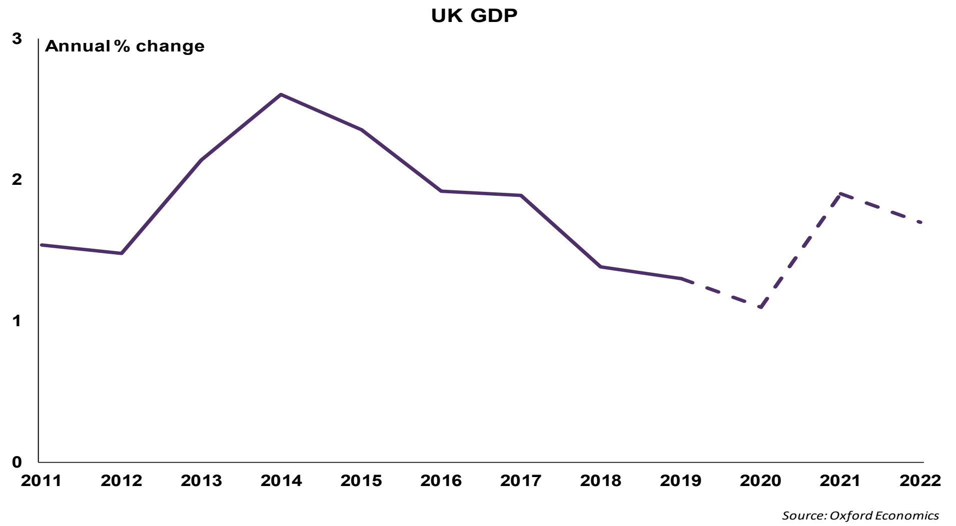
UK Economy

Following a decline in Q2, quarterly GDP growth edged up to 0.3% in Q3 2019. Persistently high Brexit uncertainties and a softening global economy are likely to depress momentum in the final quarter of this year. Forecasts by Oxford Economics suggest year-on-year GDP growth to be around 1.3% in 2019 and continued softening in 2020. Further ahead, Oxford Economics expects the government to implement an orderly Brexit, this should see a modest pick-up in growth in 2021 (Chart 1).

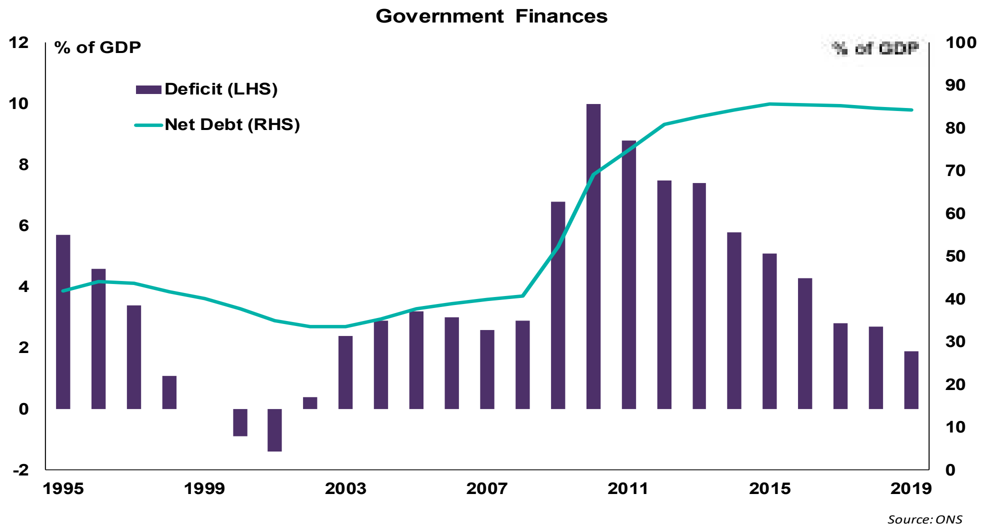
Both the Conservative and Labour parties have pledged to loosen fiscal policy though there may be little room for further giveaways. Although the budget deficit is now below pre-financial crisis levels, government debt remains close to record highs at 82% of national income (Chart 2).

In an orderly Brexit scenario, IFS expect government borrowing to exceed 2% of GDP in the next two years following the spending round in September 2019. This is notably higher than the OBR March 2019 projections. An additional fiscal giveaway of 1% of national income could see borrowing rising significantly over the next five years (Chart 3).

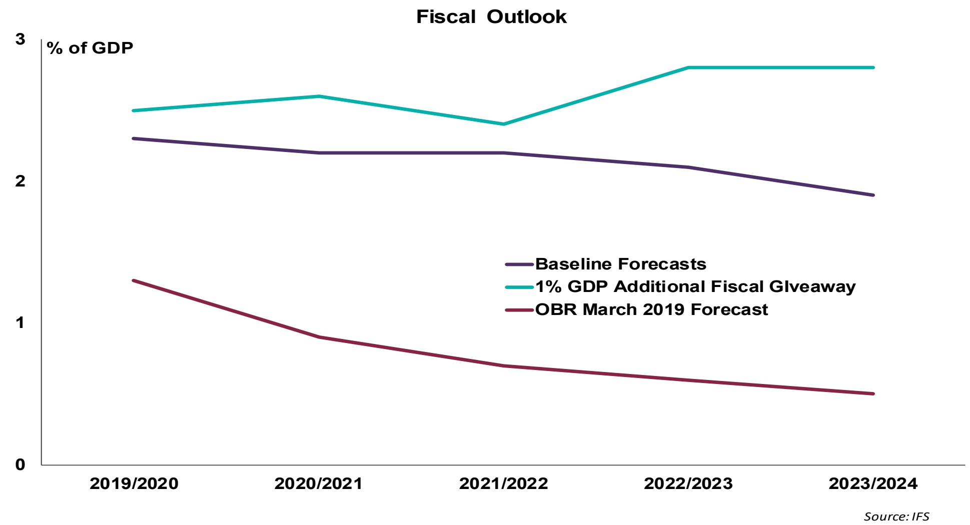
1. Current projections point to a sluggish picture for GDP growth



2. Government debt is still close to record highs



3. IFS expects borrowing to remain above 2% of GDP until 2022



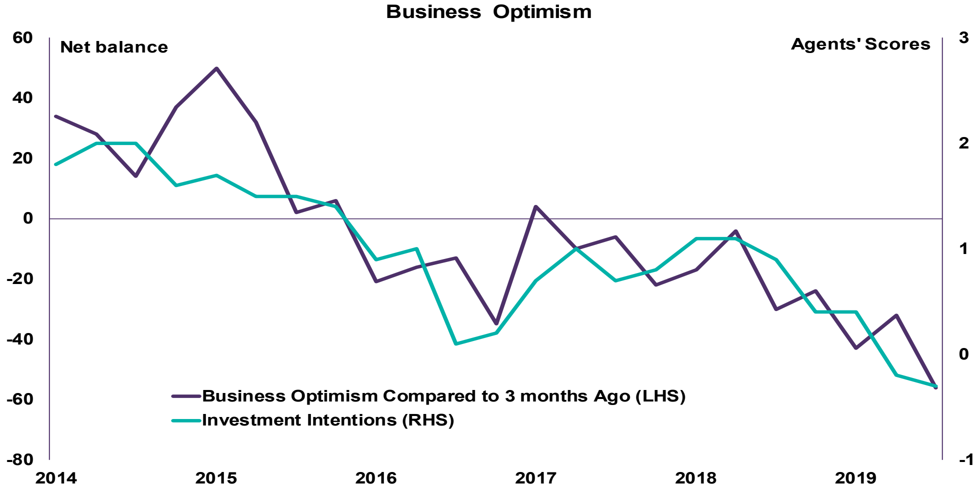
UK Economy

According to the Confederation of Business Industry's (CBI) Financial Services survey, overall business optimism has dipped significantly over the past year. Critically, confidence is now at the lowest level since 2014. Unsurprisingly, investment intentions according to the Bank of England's Q3 2019 Agents Survey have also weakened alongside this with investment plans now standing at a five-year low (Chart 4).

Indeed, Brexit uncertainties are continuing to dampen companies' appetite to invest. Chart 5 shows that in the Bank of England's Decision Maker Panel's September survey, more than 50% of firms said that Brexit is one of the current top three sources of uncertainty. The proportion of firms taking this view is now higher relative to the last three years.

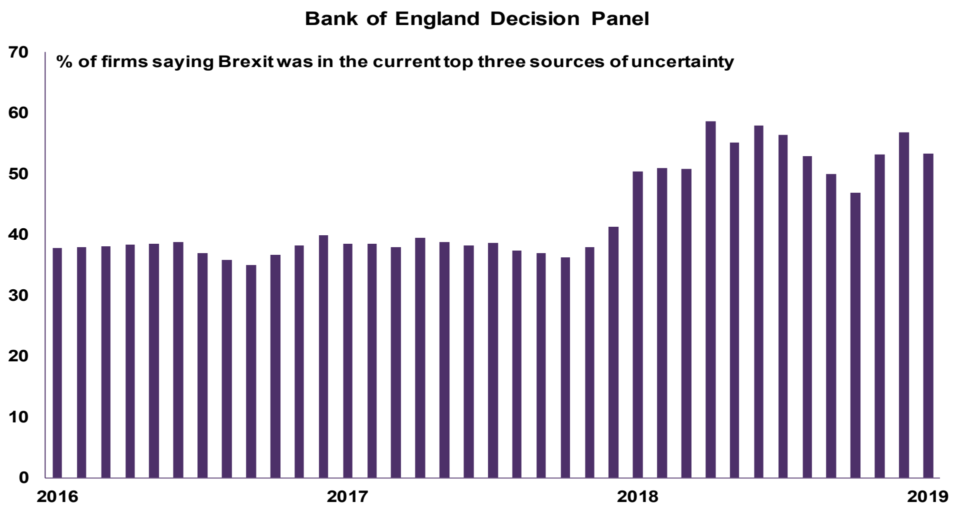
With businesses reluctant to commit to long term investment plans, it's likely that they will continue to take on more labour to meet demand. This is to some extent being reflected in the latest labour market data, which suggests that vacancies remain at record highs (Chart 6).

4. Business optimism has dipped significantly



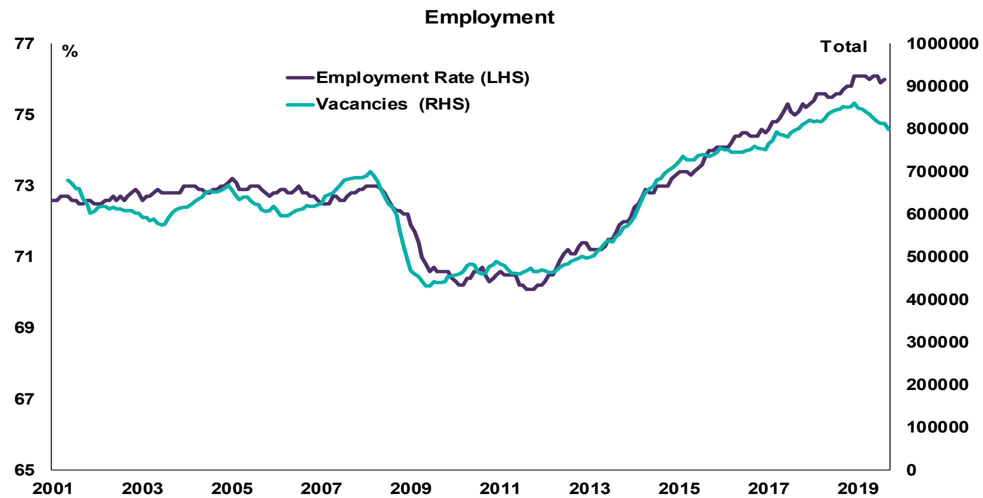
Source: CBI, Bank of England

5. Brexit remains one of top three sources of uncertainty



Source: CBI, Bank of England

6. The labour market is likely to remain tight in the near term



Source: ONS

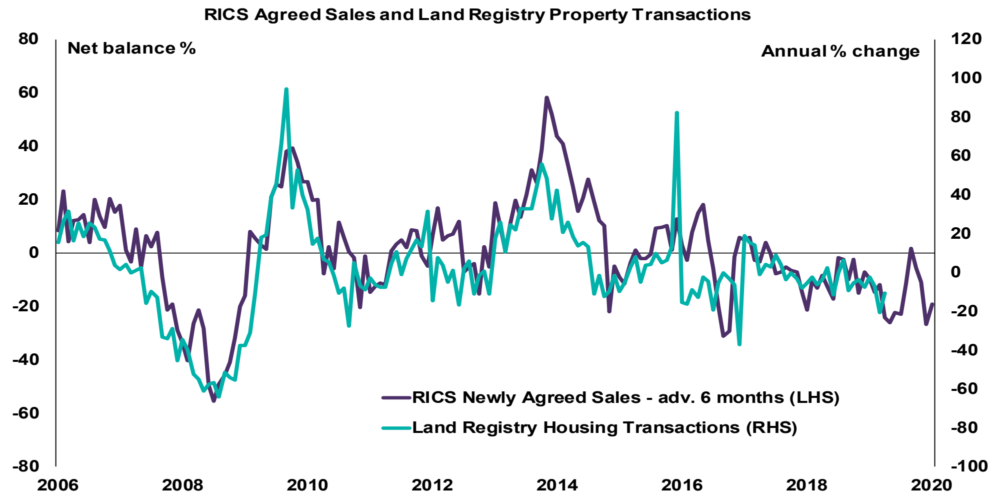
Housing Market

Housing transactions according to HMRC edged above the 100,000 mark in September for the first time in ten months. However, there is a tendency for initial readings of this series to be revised in subsequent releases. Indeed, other metrics suggest that the housing market is continuing to struggle for momentum. In particular, Land Registry data (covering England and Wales) point to a material decline in housing sales this year. Significantly, the RICS Newly Agreed Sales net balance remains entrenched in negative territory signalling that activity is likely to remain subdued in the coming months (Chart 7).

Lack of suitable supply remains a contributing factor to the sluggish picture. Anecdotal evidence to the RICS survey suggests that Brexit uncertainty seems to be dissuading vendors. Furthermore, appraisals are reportedly down compared to a year earlier in all regions suggesting there is little prospect of a pick-up in listings in the immediate future (Chart 8).

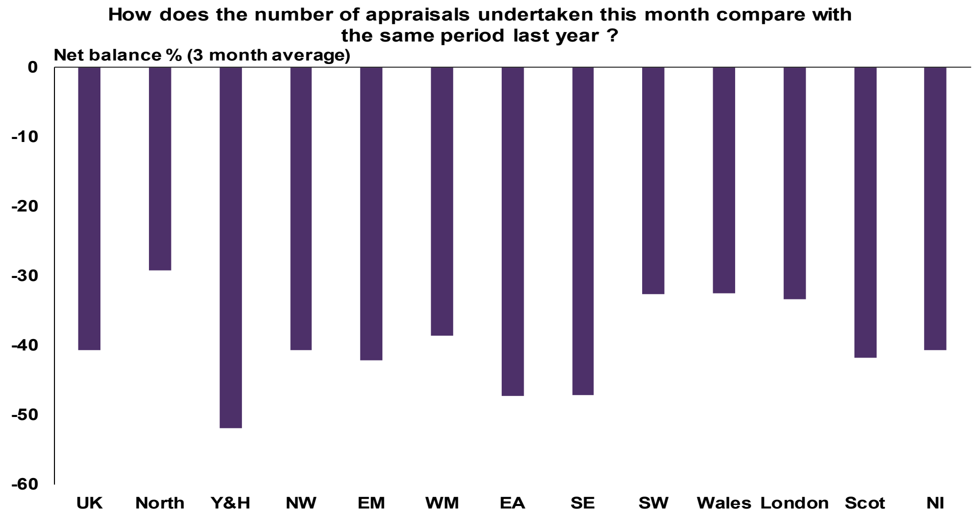
On the back of a softer trend in buyer appetite, the mortgage market remains highly competitive. Average interest rates on new mortgages are close to historic lows as lenders continue to compete for market share (Chart 9).

7. Activity is likely to remain subdued in the coming months



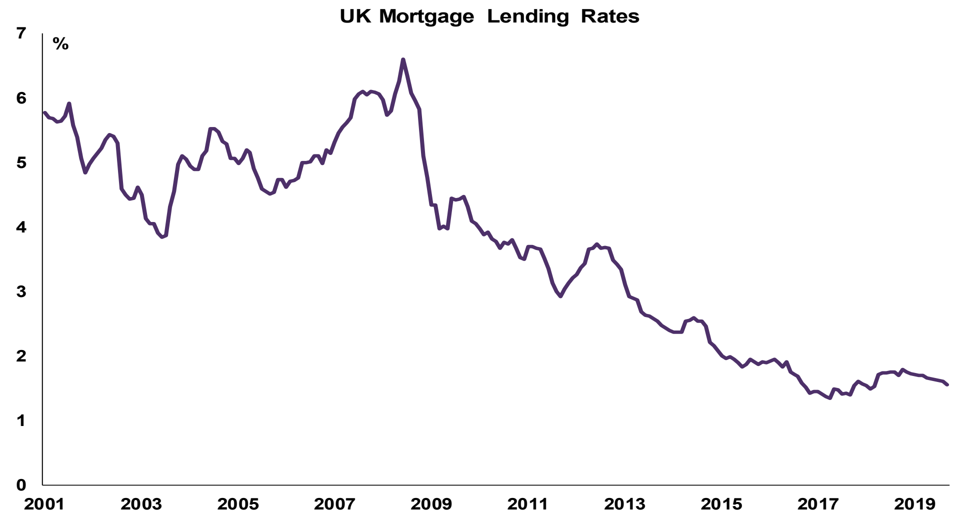
Source: Land Registry, RICS

8. Lack of supply is still a key issue



Source: RICS

9. The mortgage market remains highly competitive



Source: Bank of England

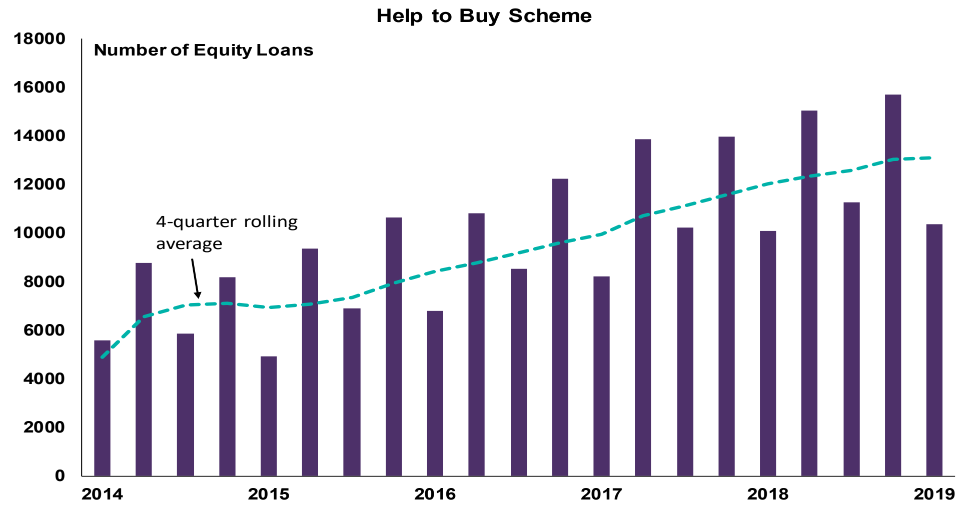
Housing Market

Independent evaluation by the Ministry of Housing, Communities and Local Government (MHCLG) show that the Help to Buy scheme has helped increase housing supply and accounted for 38% of new build property sales between 2013 and 2018. Chart 10 shows that the popularity of the scheme has risen over the past six years. Critically, there is a chance that momentum in the housing market could dip further ahead as the scheme is pared back in the medium term.

As far as house prices are concerned, the RICS headline price balance has remained close to zero in the past three reports consistent with a broadly flat trend in house price inflation over the coming months. Still, this headline gauge is continuing to be weighed down by negative momentum in London and the South East whilst results from Northern Ireland, Scotland and Wales are still consistent with further house price growth (Chart 11).

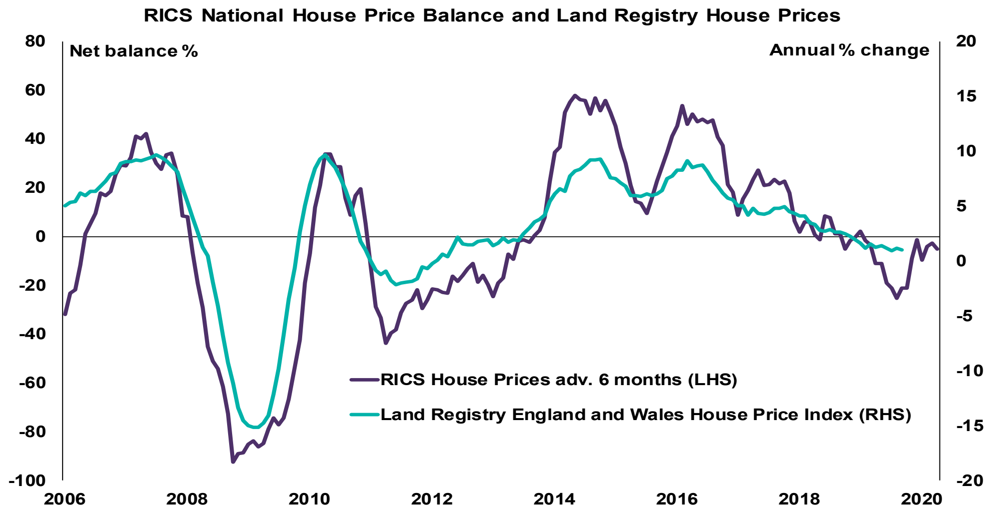
In the lettings market, RICS indicators suggest that fresh rental stock coming on to market is still falling as tax changes on investment properties continue to deter landlords. This is expected to drive further increases in rents across England in the coming year (Chart 12).

10. Help to buy has supported market activity



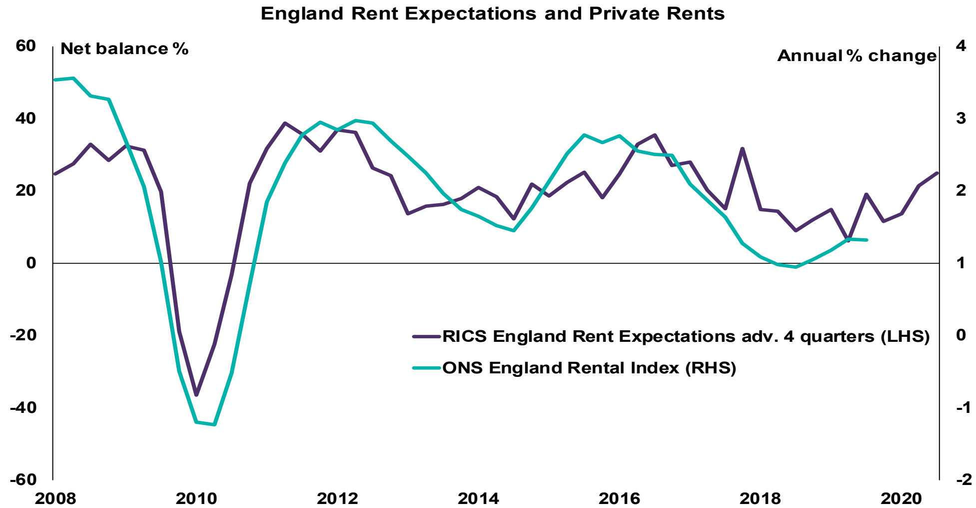
Source: MHCLG

11. House price growth is likely to remain broadly flat



Source: Land Registry, RICS

12. Rents are expected to rise further in the coming year



Source: ONS, RICS

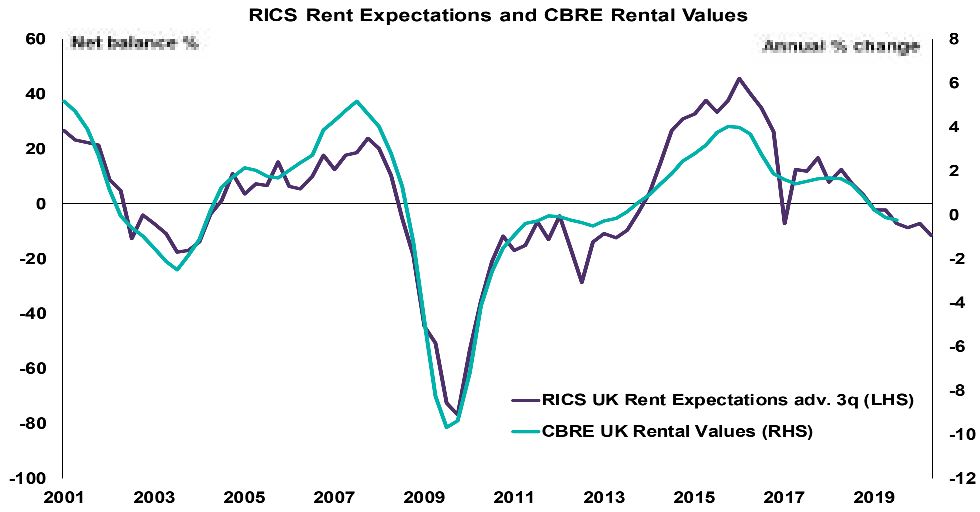
Commercial Property Sector

Sentiment has turned cautious in the UK commercial property market. In the latest RICS survey, the headline rent expectations net balance slipped to -11%, the weakest reading in six years. This indicator suggests that all sector rental value growth is likely to turn slightly negative in the coming quarters (Chart 13).

That said, the retail sector is likely to be responsible for much of this decline. The ongoing shift towards online shopping still appears be negatively impacting retail occupiers. This is visible in the RICS available space indicator which shows that the supply of vacant retail space is continuing to rise sharply which will, in turn, put further downward pressures on retail rental values (Chart 14).

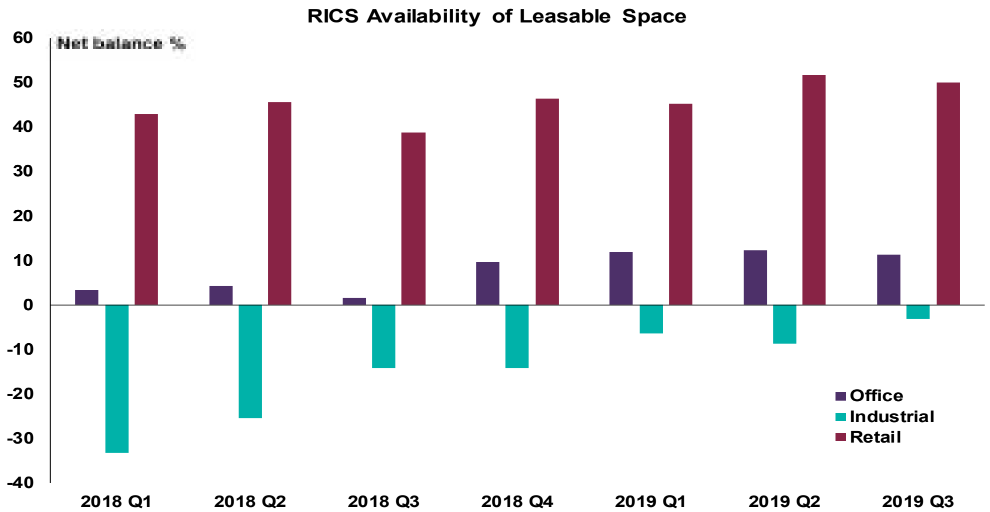
On the other hand, rent expectations are still solid for the industrial sector driven by strong tenant demand. The RICS series suggests industrial rents are likely to rise by around 3% on annual basis in the coming quarters (Chart 15). Moreover, average twelve-month rental value projections are also firm for industrials, particularly in prime locations.

13. Headline rental values look likely to slip in the near term



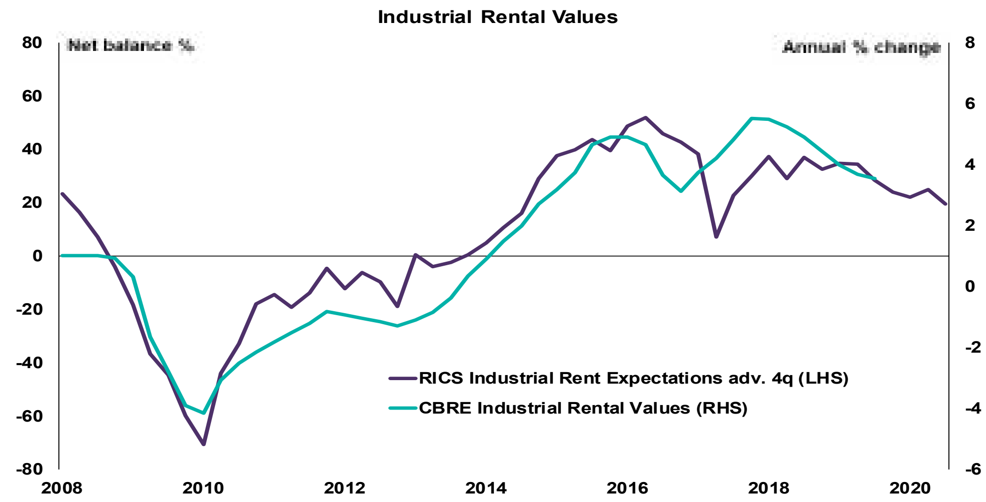
Source: CBRE, RICS

14. Much of the weakness is stemming from the retail sector



Source: RICS

15. Outlook for industrials is still solid



Source: CBRE, RICS

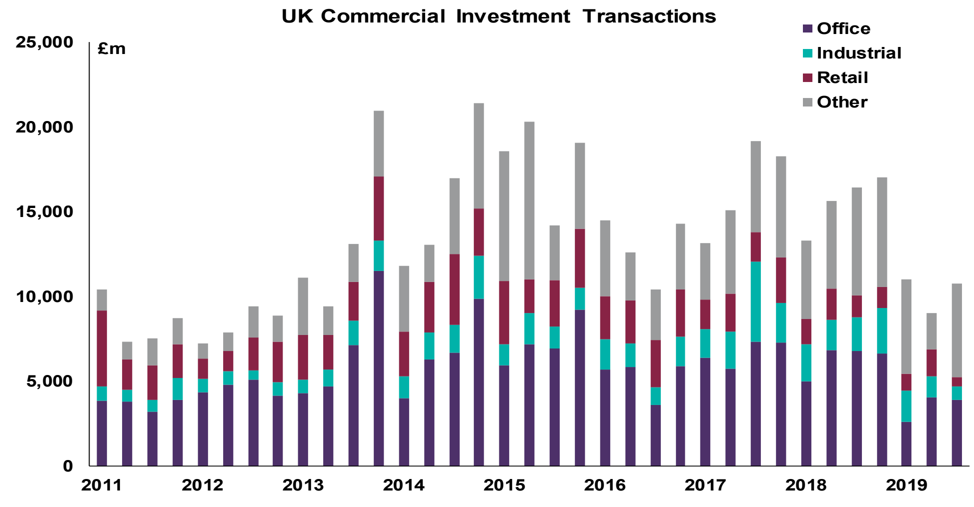
Commercial Property Sector

Ongoing uncertainty around Brexit has dampened transactional activity in the UK this year. According to Property Data, following five years of strong investment, transactions in the first three quarters of 2019 slowed to under £31 billion (Chart 16). This represents a 30% fall in comparison to a year earlier. It is unlikely that activity in Q4 will be much better as investment decisions continue to be put on hold.

Significantly, contributors to the RICS survey also a pull-back in both domestic and foreign investor demand. In line with this, near term capital value expectations slipped in Q3 2019, pointing to a modest drop in prices in the coming quarters (Chart 17). That said, the sector breakdown reveals that this is mainly driven by a particularly downbeat outlook for the retail sector while expectations for industrials are still positive.

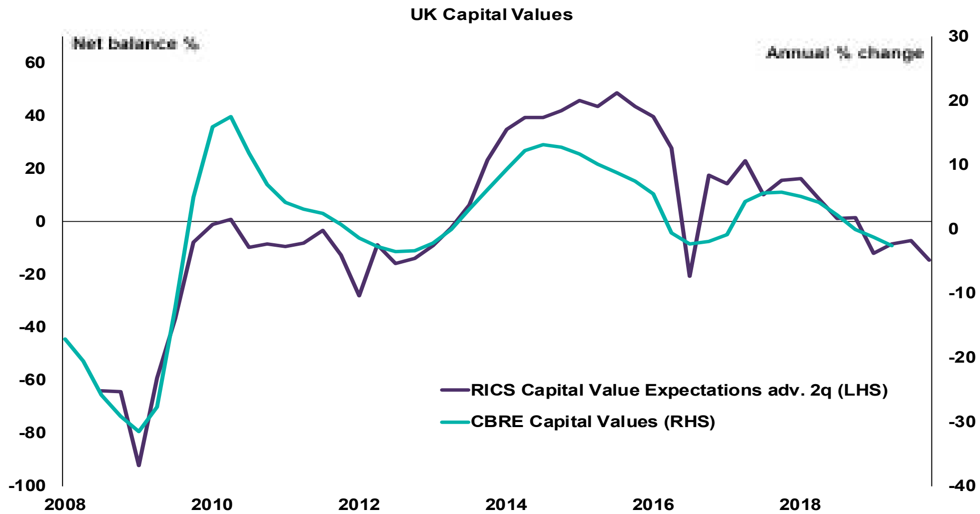
Chart 18 shows that on the back of heightened economic and political uncertainty and the structural challenges to the retail sector, overall market sentiment has turned slightly more cautious. 62% of RICS survey participants in Q3 2019 believe that the market is in the downturn phase of the property cycle, up from 53% in the previous quarter.

16. Investment activity has slowed in 2019



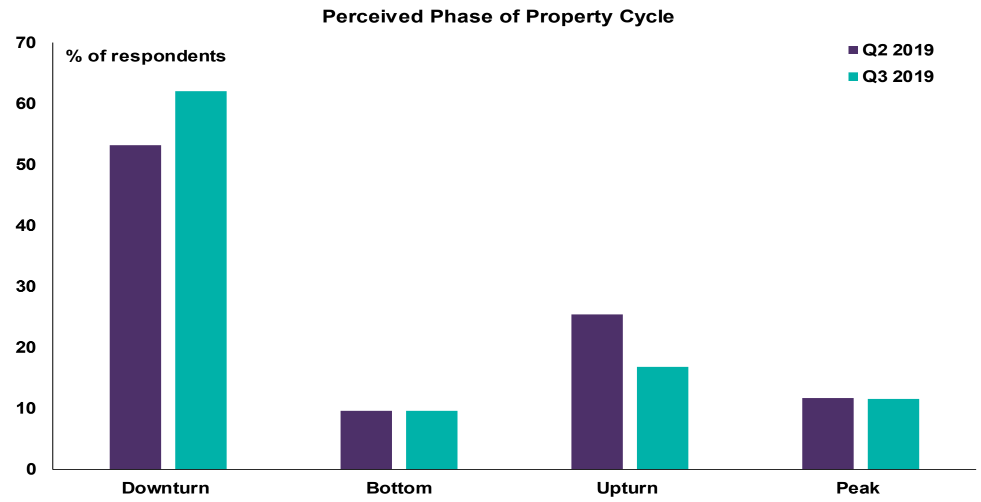
Source: Property Data

17. Capital values are likely to fall in the coming quarters



Source: CBRE, RICS

18. Majority view the market to be turning down



Source: RICS

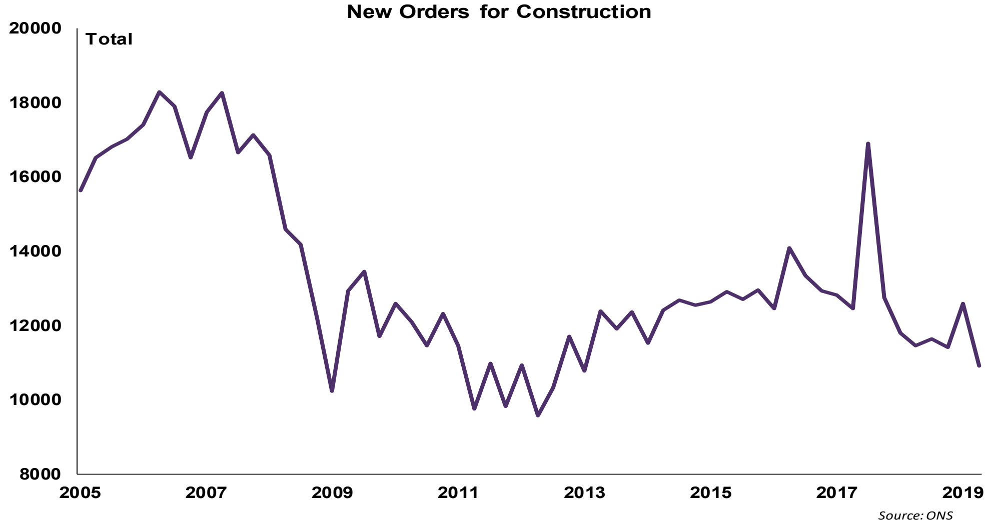
Construction Sector

Construction output has slipped in recent months. Anecdotal commentary to market surveys (conducted by the Bank of England, IHS Markit and RICS in particular) suggests that heightened economic and political uncertainty is one of the main reasons behind the fall in momentum. Significantly, new construction orders have edged lower in Q2 2019 suggesting a material pick-up in activity is unlikely, at least in the near term (Chart 19).

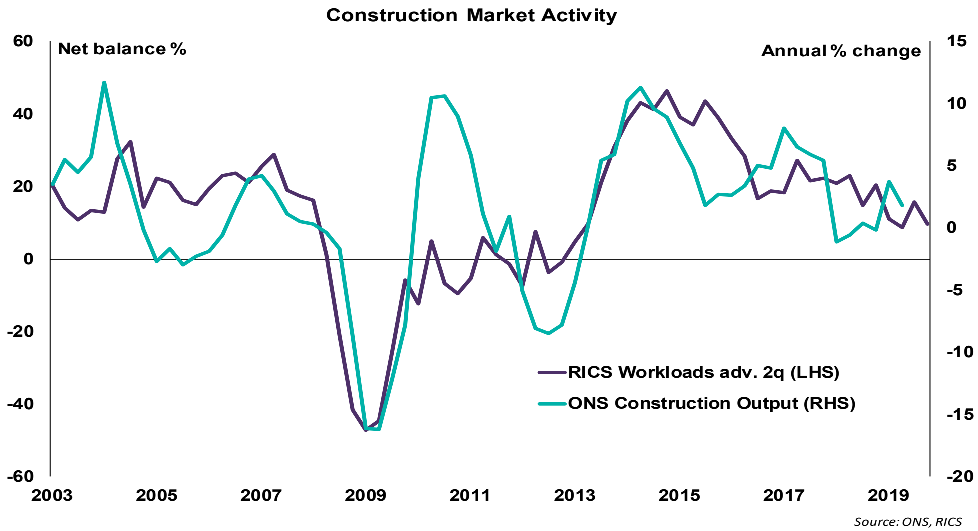
Key metrics from the RICS UK Construction Market Survey also point to a broad deceleration in output growth. The headline new workloads net balance edged down to +10% in Q3 2019 from an average of +19% over the past three years. This indicator is consistent with a moderation in construction output growth in the coming quarters (Chart 20).

The latest RICS survey results also point to a fall in optimism in the construction sector. The market confidence indicator, a composite measure of workloads, employment and profit margin expectations, slipped to +12%, a considerable drop relative to an average of +39% in the last five years (Chart 21).

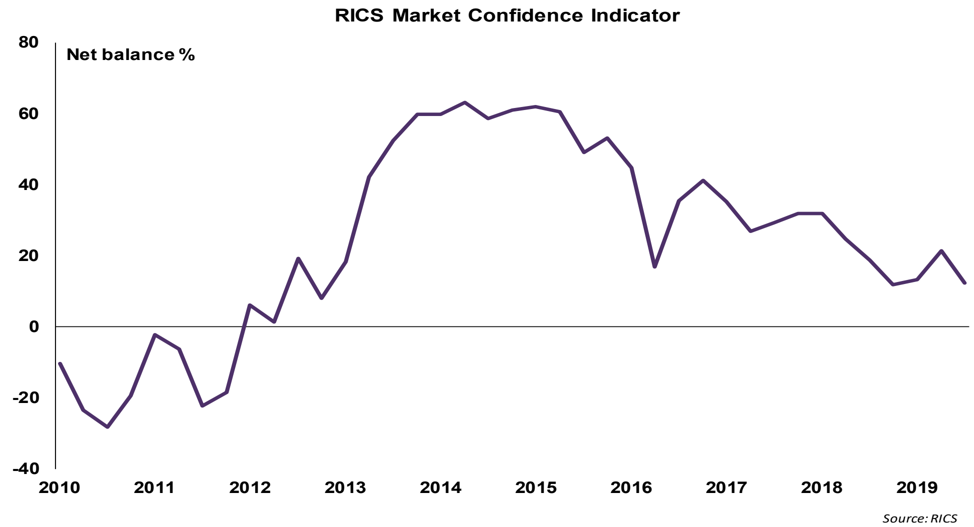
19. New orders have slipped again



20. RICS data points to a moderation in activity



21. Overall market confidence has dipped



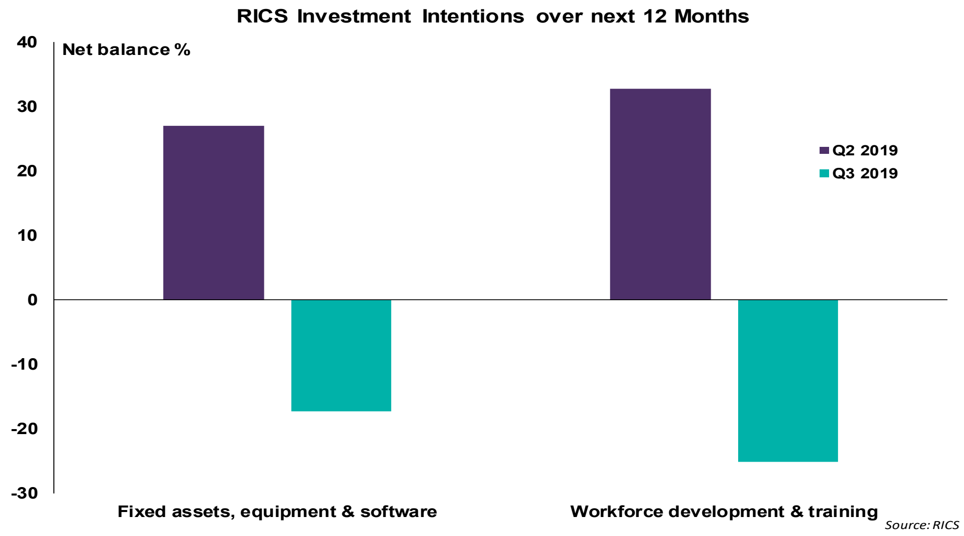
Construction Sector

Consistent with the dip in momentum across the sector, investment intentions for the next twelve months have also declined. Chart 22 shows that in the RICS Q3 2019 survey, 17% more respondents expressed the intention to decrease investment on fixed assets including equipment and software. Alongside this, 25% more surveyors expect to curb workforce training and development in the coming year.

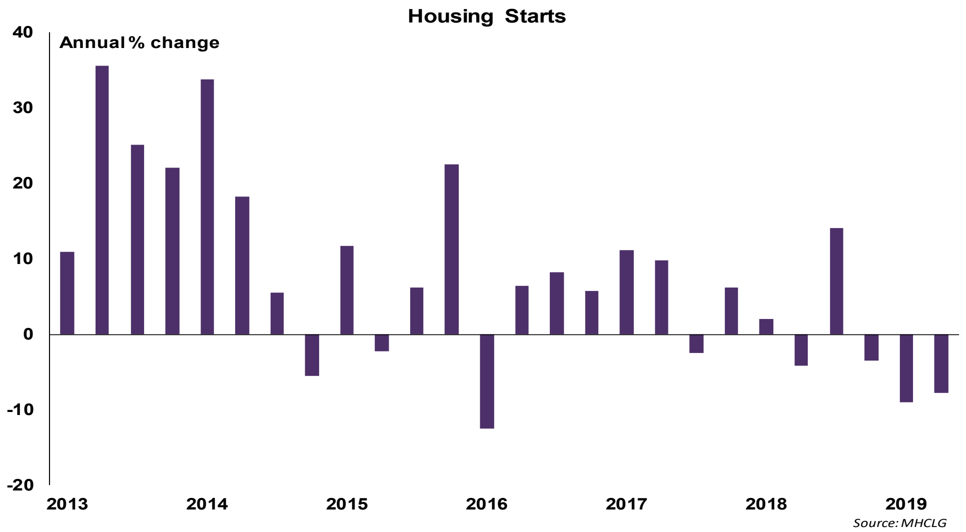
In view of a combination of subdued activity across the housing market and prolonged uncertainty engendered by Brexit, housebuilding across England in Q2 2019 has fallen to its lowest level in three years. Significantly, housing starts have declined on a year-on-year basis for three quarters in a row (Chart 23). It's improbable that there will be a material pick-up in construction activity in Q3 and Q4, suggesting that housebuilding is likely to see a sizeable decline this year.

In the latest RICS survey, more than 40% of contributors take the view that Built to Rent (BTR) could be a game changer in increasing housing supply over the next five years whilst around 30% believe it could be influential in the next ten to twenty years (Chart 24).

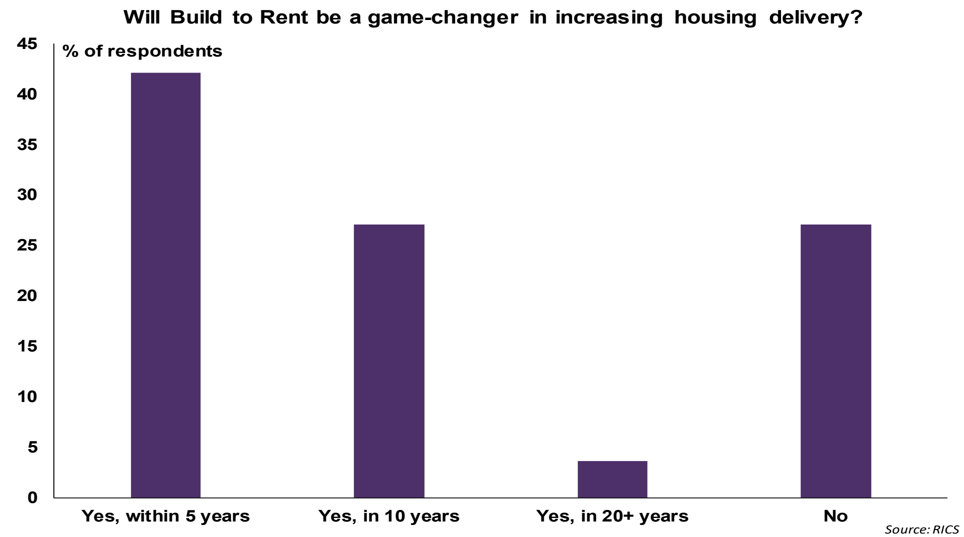
22. Investment intentions have declined



23. Housebuilding has fallen for three quarters in a row



24. BTR could be a game-changer in the medium term



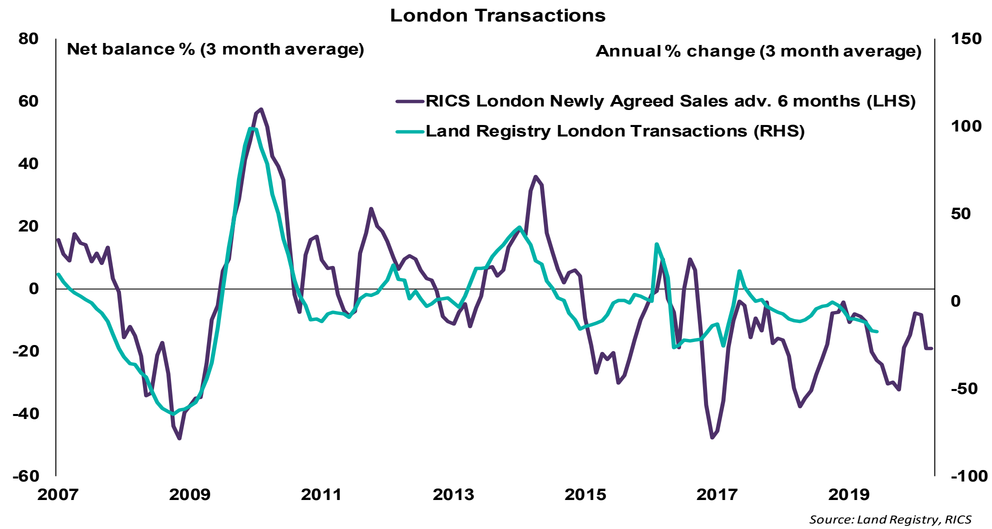
London

Housing transactions in London have consistently declined on a year-on-year basis in the last two years on the back of a combination of Brexit uncertainty, affordability constraints, as well as higher rates of Stamp Duty Land Tax levied on investment properties. The RICS London agreed sales balance remains firmly entrenched in negative territory suggesting that sales are likely to continue falling in the coming six months (Chart 25).

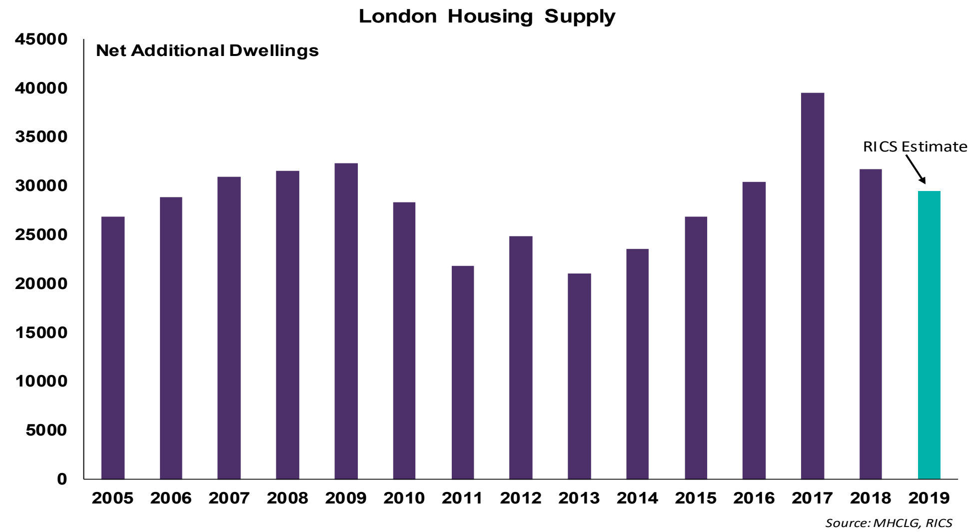
The drop in sales activity across London, together with Brexit uncertainty, has led to a fall in housebuilding in the capital. Indeed, Chart 26 shows that new housing supply slipped notably in 2018. With activity remaining broadly subdued this year, we expect housing starts to be down on an annual basis in 2019.

Momentum also appears to have slowed in the UK Commercial Property Market. In the RICS survey, the tenant demand indicator points to a decline in London enquiries over the last two years. At the same time, development starts across the capital have also reportedly fallen since 2016 limiting any potential supply overhang (Chart 27).

25. The London sales picture remains downbeat



26. In turn, housebuilding has slowed



27. Development starts are also continuing to fall


Which way is the wind blowing?
Anderson Wilde & Harris, Chartered Surveyors, are proud to sponsor this RICS Chart Book.
We give advice on any matter relating to property, we do so as established members of the RICS and because we keep in touch with the volatile economic environment in which the markets behave and may behave in the future.
awh
Anderson Wilde & Harris
Chartered Surveyors
12 Dorrington Street, London EC1N 7TB
Telephone: 0808 222 4811
Email: info@awh.co.uk
web: www.awh.co.uk
RICS

Market Surveys & Reports

Why the RICS surveys?

"The RICS poll - considered one of the most reliable guides to movements in house prices." **Financial Times**

"The RICS survey - the best short-term lead indicator of house prices and activity in our view." **Goldman Sachs**

"The RICS Survey has been a good leading indicator for the direction of and inflection points in the IPD index, and therefore the UK commercial property market overall." **Morgan Stanley**

"The RICS Commercial Property Survey is an excellent predictor of future IPD total returns." **North Row Capital**

Download RICS Economic market surveys and reports at www.rics.org/economics

- *UK Residential Market Survey (monthly)*
  www.rics.org/housingmarketsurvey
- *UK Construction Market Survey (quarterly)*
  www.rics.org/constructionmarketsurvey
- *UK Commercial Market Survey (quarterly)*
  www.rics.org/commercialmarketsurvey
- *UK Rural Market Survey (semi-annual)*
  www.rics.org/ruralmarketsurvey
- *Global Commercial Market Monitor (quarterly)*
  www.rics.org/globalpropertymonitor
- *RICS / Ci Portuguese Housing Market Survey (monthly)*
  www.rics.org/portuguesemarketsurvey
- *Hong Kong Residential Market Survey (monthly)*
  http://www.rics.org/hong-kong-residential-market-survey

The Economics Team

Kisa Zehra, Economist
kzehra@rics.org +44 (0)20 7695 1675

Simon Rubinsohn, Chief Economist
srubinsohn@rics.org +44 (0)20 7334 3774

Jeffrey Matsu, Senior Economist
jmatsu@rics.org +44 (0)20 76971644

Sean Ellison, Senior Economist
sellison@rics.org +65 68128179

Tarrant Parsons, Economist
tparsons@rics.org + 44 (0)20 7695 1585

Janet Guilfoyle, Surveys Administrator
jguilfoyle@rics.org +44 (0) 20 7334 3890

Confidence through professional standards

RICS promotes and enforces the highest professional qualifications and standards in the development and management of land, real estate, construction and infrastructure. Our name promises the consistent delivery of standards – bringing confidence to the markets we serve.

We accredit 118,000 professionals and any individual or firm registered with RICS is subject to our quality assurance. Their expertise covers property, asset valuation and real estate management; the costing and leadership of construction projects; the development of infrastructure; and the management of natural resources, such as mining, farms and woodland. From environmental assessments and building controls to negotiating land rights in an emerging economy; if our members are involved the same professional standards and ethics apply.

We believe that standards underpin effective markets. With up to seventy per cent of the world's wealth bound up in land and real estate, our sector is vital to economic development, helping to support stable, sustainable investment and growth around the globe.

With offices covering the major political and financial centres of the world, our market presence means we are ideally placed to influence policy and embed professional standards. We work at a cross-governmental level, delivering international standards that will support a safe and vibrant marketplace in land, real estate, construction and infrastructure, for the benefit of all.

We are proud of our reputation and we guard it fiercely, so clients who work with an RICS professional can have confidence in the quality and ethics of the services they receive.

United Kingdom RICS HQ
Parliament Square, London SW1P 3AD
United Kingdom
t +44 (0)24 7686 8555
f +44 (0)20 7334 3811
contactrics@rics.org
Media enquiries pressoffice@rics.org

Ireland
38 Merrion Square, Dublin 2,
Ireland
t +353 1 644 5500
f +353 1 661 1797
ricsireland@rics.org

Europe
(excluding UK and Ireland)
Rue Ducale 67,
1000 Brussels, Belgium
t +32 2 733 10 19
f +32 2 742 97 48
ricseurope@rics.org

Middle East
Office G14, Block 3,
Knowledge Village,
Dubai, United Arab Emirates
t +971 4 446 2808
f +971 4 427 2498
ricsmenea@rics.org

Africa
PO Box 3400, Witkoppen 2068,
South Africa
t +27 11 467 2857
f +27 86 514 0655
ricsafrica@rics.org

Americas
One Grand Central Place,
60 East 42nd Street, Suite 2810,
New York 10165 – 2811, USA
t +1 212 847 7400
f +1 212 847 7401
ricsamericas@rics.org

South America
Rua Maranhão, 584 – cj 104,
São Paulo – SP, Brasil
t +55 11 2925 0068
ricsbrasil@rics.org

Oceania
Suite 1, Level 9,
1 Castlereagh Street,
Sydney NSW 2000. Australia
t +61 2 9216 2333
f +61 2 9232 5591
info@rics.org

North Asia
3707 Hopewell Centre,
183 Queen's Road East
Wanchai, Hong Kong
t +852 2537 7117
f +852 2537 2756
ricsasia@rics.org

ASEAN
10 Anson Road,
#06-22 International Plaza,
Singapore 079903
t +65 6635 4242
f +65 6635 4244
ricssingapore@rics.org

Japan
Level 14 Hibiya Central Building,
1-2-9 Nishi Shimbashi Minato-Ku,
Tokyo 105-0003, Japan
t +81 3 5532 8813
f +81 3 5532 8814
ricsjapan@rics.org

South Asia
48 & 49 Centrum Plaza,
Sector Road, Sector 53,
Gurgaon – 122002, India
t +91 124 459 5400
f +91 124 459 5402
ricsindia@rics.org