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One Man's View Q3

By Harvey M. Soning, FRICS

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I have been asked to follow up on my previous commentary on the property industry and, of course, I am delighted to share my opinion. Last time I considered the drivers of the economy and how these affect the public's confidence, many of these have not changed dramatically, however, outside influences are again in the headlines.

My biggest fear for the next quarter, and the beginning of the New Year, is if the events in the Middle East spill over to a wider conflict. Unfortunately, I don't have the answers, any more than the UN or world leaders.

Overseas conflicts have been the driver of worldwide inflationary pressures for over 18 months, albeit the inflationary pressures of years of Quantative Easing had been overlooked by central governments for many years. The questions that concern me today are: have interest rates peaked, and is the use of interest rates a blunt instrument in the face of inflationary pressure caused by conflict?

Unfortunately, I suspect there will be one more rise in rates before the Bank of England takes a pause to see whether the rate rises have been effective. The new reality of 5.25%+ rates has yet to have its full effect on property but there is evidence emerging of the residential market stalling and if you look west to the USA, a storm is brewing.

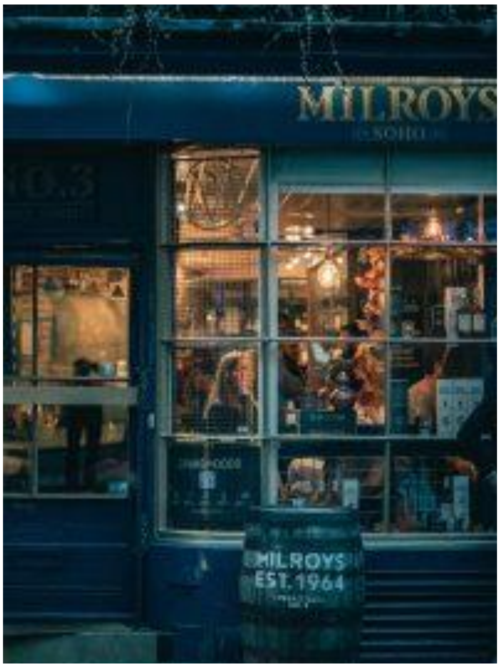
Oliver Shah, Editor of The Sunday Times, reported the collapse of the office property market with the destruction of billions of dollars in value. In the USA this has been brought about by work from home revolution and the drop in demand for aging office space. His report suggests “there are dozens and dozens of buildings that are going to change hands, get given back to the lender or restructured. On the other hand, there are buildings that are vibrant, strong, with good tenants.”

This is a familiar message we have been giving to clients since lockdown. To get staff back into the office you need the best offices, providing facilities we didn’t know existed just 5 years ago. The astute are already gearing up to take advantage of the collapse in values, and property owners with impending lease events that we know and advise, have already engaged consultants to report on the future.

This ensures they are ready to reposition their assets as the leases end. Many owners, however, will not have the resources to commit to the level of expenditure required, given loan to value and interest cover requirements on top of the increasing cost of building work.

This cycle will inevitably reach the UK and we need to be prepared. We are aware of a fire sale of an office asset in the City of London which was sold by a USA bank for under £200 per square foot. There are a multitude of factors that drove this, but the lot size and funds required to reposition the building where high on the list, not to mention an off-pitch location. Equally, there are good news stories.

Rents in the best buildings continue to rise. Clients of ours have been quoted £125 per sq ft in the new towers in the City. The City team at James Andrew International also advised Fidelity European Real Estate Climate Impact Fund on the purchase of 99 Queen Victoria Street from the ailing WeWork portfolio.



The property comprises an 88,000 sq ft building from which Fidelity intend to create a fit for purpose landmark office building in 2025. This will involve new MEP, terraces, and amenity space. We are very excited by the prospect of being involved in this high profile scheme and much of our efforts are now focussed on this and three similar repositioning projects across the City. Delivering the very best office buildings with amenities is, I believe, the key to enticing staff back into the office.

On this topic, I heard an original strategy by one employer, insisting the staff had to be in the office a minimum of 3 days a week with the proviso days at home could not be consecutive. Most employers appear to fear the backlash of staff if they impose a return to the office on employees.

The deepening economic crisis with looming redundancies could change attitudes. Long term for the majority of people, working in a collaborative fashion within an office environment has to be good for the business, but also the health and wellbeing of the staff.

Turning briefly to the residential sector, the interest rate rises since October 2022 have sharply increased the cost of mortgages for both landlords and owner occupiers. In the case of the former this has added to the woes of the Private landlord.

In 2016 when the Conservative government began the phasing out of mortgage interest relief, many landlords began to withdraw from the market. Relief ended in 2020 and the government seem intent on further ‘punishing’ these investors by removing the no fault termination, in effect removing the right to evict tenants. This measure with the increased mortgage costs is driving many small landlords out of the market.

For renters this can mean only one thing, greater demand than supply, thus rising rents. Of course, the contrary argument is a greater supply of property for sale, thus falling prices. These factors don't make property any more affordable, if you haven't got a sizeable deposit then you cannot get on the housing ladder.

For owners of leasehold property, the government have some new initiatives. Get rid of Leasehold houses and give apartment owners the right to extend to 999 years. I am not sure the developers have been told the buildings they erect have to last 1,000 years.

My residential management team can tell you, very few will last beyond 30 years and that's certainly true of the services. My recommendation is to ensure there is an adequate sinking fund. If there is one, have it checked periodically to ensure it covers everything and costs reflect reality.

My predictions for the next three months? Housing prices below £2 million to fall, sale volumes to contract and residential rents will continue to rise. In the office sector, rents of the best in class buildings will continue to grow. Values of existing stock will increasingly come under pressure. After all, if the costs rise and the end value is static, the only moving part is the value of the site. For retail property, the test will be the forthcoming period between now and Christmas.

That's it for now. May I wish you all Season's Greetings and wish you all well for the New Year.

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Overview:
- *63 years in the real estate industry*
- *Ambassador and Founding Member of the Royal Air Force Museum Fundraising Board*
- *Chair of the International Friends of the Natural History Museum London*
- *Founding Member of the Natural History Museum Foundation*
- *Trustee of JCoSS secondary school, Barnet, London*
- *Court Member and Managing Trustee of The Worshipful Company of Chartered Surveyors*