UK Property Predictions

2018

Economics & politics

Jon Neale
UK Head of Research
jon.neale@eu.jll.com
+44 (0)20 7087 5508

Brexit confusion will be the main theme of 2018
Negotiations will meet stumbling block after stumbling block; there will be walkouts, rumours and plenty of averse briefings; 'almost certainly' the mood music will get worse before it gets better. But with the EU, "nothing is agreed until everything is agreed" and it still seems likely that a deal will emerge late in 2018 or early in 2019 - even if it only covers transition.

While this is likely to mean – much to the annoyance of many Brexiteers – a continuation of the status quo for two or three years, it will come as a (temporary) relief to many in property. But it also means that the fog will remain impenetrable for most of the year ahead, with many hard choices postponed.

The economy will continue to slow – gradually
GDP growth looks set to be around 1.5% in 2018, roughly in line with 2017. This is a far better turnout than some of the more pessimistic forecasts produced at the time of the referendum – but will be somewhat behind France and Germany. On the other hand, inflation will fall back, base rates will remain unchanged and employment growth in the UK will remain solid, particularly in fast-growing sectors such as technology. There will be more negative headlines about job losses, but it is unlikely that they will have a noticeable impact on overall numbers, given growth elsewhere. But the risks of Brexit upsetting this relatively benign picture will increase as the year progresses.

Theresa May will cling on to Number 10, but her authority will be paper-thin by the end of the year
Very few in the Conservative party are happy with the Prime Minister – but they cannot think of an alternative that will not lead to a heating up of the "cold war" between the two wings of the party. The government is still refusing to make the necessary decisions around the trade-offs that Brexit involves. Even though it has said it wants to leave the Single Market and the Customs Union, it still pretends it can keep most of the benefits these bring. Once it is forced to chart a more definite course, May begins to risk the rebellion of those disenchanted with the route she has chosen. This sets the country up for an even more politically turbulent 2019.

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Industry themes

Alex Edds
Director of Innovation
alex.edds@eu.jll.com
+44 (0)20 7399 5333

Sophie Walker
UK Head of Sustainability
sophie.walker@eu.jll.com
+44 (0)20 7399 5050

2018 will be the year in which the industry finally takes technology seriously

Many other industries have already seen a complete re-shaping as a result of digital innovation – think music, TV, and photography – all of which look very different than 10 years ago. Our industry has as yet been relatively unaffected, but the change will come fast. We saw a number of new senior appointments by large real estate companies in 2017 to help drive this change, and it is likely that CTOs or CDOs will be commonplace on all real estate boards in the coming year(s). Additionally, the big agents and professional firms will invest more in R&D, and adopt more agile technology and innovation teams in order to respond more quickly to client demands and technological advancement.

Technology teams will expand with a particular emphasis on Data Scientists. These are among the most in-demand roles for any corporate right now so attracting them will be a challenge – not least because the industry won't just be competing within itself. This will become a key battleground in the war for talent in years to come. Alongside this, we will see the growing adoption of specific technology platforms to drive advisory, investment, management and development processes – thus supporting the continued growth of the 'PropTech' sector. Although at the moment it is confined to helping the existing industry work more efficiently – mainly through digitising analogue processes – it is bound to be more profoundly disruptive as technologists understand more about property and more VC money pours into this sector.

Space will increasingly be regarded as a service – and treated accordingly

Whether in retail, offices or industrial, occupiers are demanding more flexibility. The faster pace of growth, entrepreneurship and disruption means that long-term commitments, at least outside core functions will become rarer. Companies will gravitate towards locations where they can easily expand and contract, accessing different types of space where and when they need it. There will still be a need for highly-specified space, designed with a specific company's needs and brand in mind – but it may be a smaller part of the market. This even applies to warehouse space, where – notwithstanding supply shortages – space-on-demand may begin to emerge.

At the same time, there will be an ever-increasing focus on amenity and service - from concierges and programmed event space, to a curated F&B offer within shopping centres or large developments. It even extends to co-working space in hotels, the provision of co-living for mobile young talent or housing with care for older generations. Concepts from hospitality and retail are bleeding into every sector.

The property industry will focus on the need for a diverse workforce

All UK-based employers with 250 or more staff have up until April 2018 to publish data on the pay gap between their male and female employees. According to 2016 ONS data, the pay gap for all employees, both part time and full time, is 18.1%. There are likely to be even wider gaps for traditionally male oriented industries such as construction, real estate and finance.

The legislation will encourage businesses to understand the root cause for such differences and to invest in solutions to promote gender equality. Companies like Lendlease and Landsec have already published and are taking proactive measures to addressing the gap. We expect many to follow suit, committing to active investment, inclusive recruitment rules and engagement campaigns to address unconscious bias. Some forward thinking businesses will use this opportunity to go beyond gender inequality and to focus on ethnic minorities and other marginalised groups as well. Our industry will start to realise that recruiting from a diverse pool of candidates will become a critical success factor as the war for talent intensifies.

Capital Markets

Alistair Meadows
Head of Capital Markets
alistair.meadows@eu.jll.com
+44 (0)20 7852 4092

Jon Neale
UK Head of Research
jon.neale@eu.jll.com
+44 (0)20 7087 5508

The prospect of capital gains tax on overseas investors will not deter them from the UK

The government announced at its budget on 22 November that it would be removing the capital gains tax exemption for overseas investors in UK commercial property from April 2019. This is likely to have a temporary impact on the market as it transitions to the new regime, particularly in London offices, where over 80% of investment has come from overseas in 2017. Consequently, we expect 2018 volumes to total around £55bn, only slightly down on the circa £60bn now expected for last year. For the rest of the market, the figure is much lower at 41% – but this is still very significant.

Undoubtedly there will be investors who are dissuaded by the changes. But the change only aligns the UK with most other developed countries. Meanwhile, the major reasons for investing in UK property remain – liquidity, lot sizes, landlord-favourable leases, the strong economic and leasing fundamentals, and at present, relatively high yields and a weak currency. Consequently, we expect 2018 volumes to total around £55bn, only slightly down on the £60bn estimated for 2017.

In the longer term, it may lead to some structural changes in the market. As it levels the playing field between overseas and domestic investors, it could allow UK REITs, institutions and propcos to compete more effectively in areas such as London offices. It may also make investors prioritise income over shorter-term capital gains. Much will depend on the extent to which the government makes exceptions for certain types of investor or areas such as development and refurbishment.

Total returns will be down on 2017, but industrial and logistics will outperform

Total returns as measured by the IPD All Property Index will hit 6.4% in 2018, slightly down on the level achieved in 2017 – currently expected to be close to 10%. The industrial sector will continue to lead the way with a total return of 9.9%, with retail and offices seeing more subdued returns of 5.7% and 5.5% respectively. Returns will be driven almost entirely by rents over the year, with yields generally flat, except perhaps in areas such as regional offices and multi-let industrial. The trophy end of the London market - a small part of the overall picture - will undoubtedly remain a law unto itself when it comes to pricing.

Industrial's outperformance will be a result of ongoing rental growth produced by low levels of development and supply, particularly in the South East, and the need for both large-scale and city logistics as more retail shifts online. While some developers have real ambitions for the UK in the longer-term, this is unlikely to impact in 2018. Industrial vacancy rates will hover around their current low level, supporting another year of solid rental growth – around 3.5% in 2018, with stronger growth in London, where the pressure on industrial land remains intense.

Arrival of Japanese and Korean capital

In April 2017, the Japanese Government Pension Investment Fund (GPIF), one of the world's largest pension funds ($1.3trn AUM) issued its first ever call for private equity, infrastructure and real estate managers interested in competing for global and domestic alternatives allocations. This followed an announcement that it would start investing 5% of its portfolio in real estate and infrastructure, amounting to $65 billion. Led by GPIF, other Japanese investors (particularly other pension funds) will follow in the same direction, adding substantially to demand for global real estate. The UK, and London in particular, is likely to be a key destination for this capital, as other major Japanese investors such as Mitsubishi Real Estate, Mitsui Fudosan and NTT are already active.

Korean investors are also expected to add weight to the broader push from Asia. While they have held back from adding to their UK exposure in the aftermath of the referendum, we expect a return in 2018, attracted by the market's resilient performance and high pricing in other global markets.

Sustained global demand and pricing in the listed sector will drive more platform deals

Rising capital allocations to real estate, the emergence of new investors, and the tendency for much of this growing demand to focus on core markets in the major developed economies is making it more difficult to access stock through traditional direct investment. These pressures are not new, and have spurred the search for different routes to deploy capital including debt strategies, the rise of alternative asset classes, and, increasingly, platform deals that marry equity with expertise and provide an efficient means to invest at large scale. This global trend is likely to accelerate in 2018, and with the UK listed sector priced at a discount to NAV, investors will be attracted to the UK in particular.

Corporate Occupier

Sue Asprey Price
UK Head of Corporate Solutions
sue.aspreyprice@eu.jll.com
+44 (0)203 147 1941

Tom Carroll
Head of EMEA and UK Corporate Research
tom.carroll@eu.jll.com
+44 (0)20 3147 1207

The proportion of flexspace within occupier portfolios will continue to grow in 2018

2018 will see a continued focus on increasing flexibility in corporate portfolios. JLL's Human Experience research showed that UK employees are increasingly mobile both within and outside the office and the rise of the flexible office market is a natural response to a structural change in the way people are working. Traditional static portfolio concepts are being redesigned to incorporate new formats of space, co-working and a more fluid and diverse range of space options that support creativity, innovation and collaboration. A greater number of large organisations will explore flex space and co-working in 2018 for multiple objectives ranging from servicing a mobile workforce, supporting business development, to delivering swing space or driving innovation.

Smart real estate – growing adoption of technology will redefine buildings, workplaces and portfolios

Digital Technology continues to redefine real estate and 2018 will see further acceleration in this area. The adoption of smart building technologies will continue to grow as leading edge organisations focus on a seamless integration of Internet of Things technologies throughout their buildings. At a workplace level AI and machine learning are being deployed in various ways to improve utilisation, monitor employee experience and measure financial performance and operational excellence objectives. 2018 will see a deepening level of integration and adoption of digital technology across corporate real estate portfolios.

Time for decisions – 2018 will mark a year of decision for many businesses regarding Brexit

After 18 months of contingency and scenario planning, 2018 will be the year that companies decide whether to enact their plans. Amidst signs of continued corporate investment and focus in the UK from sectors as diverse as life sciences, technology and automotive; many international companies have been developing plans in parallel to provide a functional platform for business continuity in the event a disorderly brexit. For financial services in particular and ancillary professional services European leasing activity has been seen in Frankfurt, Paris, Dublin and other European hubs. As the CBI has vociferously indicated, without greater clarity for business on the nature of any transitional agreement some businesses will be forced to enact contingency plans in 2018.

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Alternatives

Ollie Saunders
Head of Alternatives
ollie.saunders@eu.jll.com
+44 (0)20 7087 5843

James Kingdom
Alternatives Research
james.kingdom@eu.jll.com
+44 (0)20 7087 5154

The birth of living and social infrastructure
Following a number of recent landmark deals, 2018 will see wider participation by institutions and pension funds in the alternative sectors, especially for direct let and operational platforms. This demonstrates that these sectors are now a key component of the property market. Concerns over exposure to increased risk outside of traditional markets will be offset by sound underlying market drivers. Appetite is being driven by a mix of long income opportunities linked to inflation, exposure to strong demographic trends and a number of sectors which benefit from a structural supply and demand imbalance. Alternatives also provide a defensive position against weakened economic sentiment which has a more direct impact on traditional commercial markets.

The rise of mixed-use alternatives
Rather than focusing on one specific sector, investors and operators will increasingly regard themselves as providers of living space and social infrastructure. The shortage of supply will result in established operators in one sector moving into a similar or complementary market. Apart from addressing one of the main challenges faced by investors, it will also deliver more mixed-use developments with supportive social infrastructure alongside accommodation.

Electric Vehicles gearing up to being the mainstream choice
Technology remains a key theme across alternatives and will increasingly improve margins in a number of sectors. A key example is automotive: Government policy and manufacturer-led innovation is supporting the growth of ultra-low emission vehicles (ULEVs) which is set to have a transformative effect on many locations and sectors. To enable this transition from petrol and diesel, there is an urgent need for investment in the supportive infrastructure. A recent survey of Local Authorities (LAs) carried out by JLL and the British Parking Association (BPA), revealed nearly one third of LAs have no EV charging points. And of the LAs with charging facilities, less than 20% of points are located 'On Street'. The situation is similar in strategic locations as well, with the average number of charging points per shopping centre standing at just 0.68. The good news is that the Government sees this as a priority and, as stipulated in the Clean Growth Strategy, is committed to developing one of the best electric vehicle charging networks in the world. The 2017 Autumn Budget saw Chancellor Philip Hammond pledge to establish a new £400m charging infrastructure fund. This should attract greater private sector investment in charging infrastructure within strategic locations as well as the much needed 'On Street' parking with Local Authorities.

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Offices

Neil Prime
Head of Central London Markets
neil.prime@eu.jll.com
+44 (0)20 7399 5190

Jon Neale
UK Head of Research
jon.neale@eu.jll.com
+44 (0)20 7087 5508

London will remain resilient to Brexit pressures, but performance will vary by market

London office employment has continued to grow despite the uncertainty posed by Brexit, and this growth is forecast to continue during 2018. While negative sentiment will continue to cast a shadow, occupier demand will be robust and net absorption will remain positive, meaning there will be no jump in vacancy rates. However, performance will continue to vary by market, with amenity rich, supply constrained markets such as Southbank, Aldgate, Soho and Bloomsbury faring better than those where there is more supply and which rely on demand from the financial sector to a greater degree.

Flexible offices will continue to disrupt the leasing market and ripple out to the regions

The flexible office sector expanded rapidly in 2017, particularly in Central London. This will continue in 2018 and as the footprint of flexible office providers grows, they will increasingly be competing directly with traditional leasehold office space. Landlords will respond by accommodating flexible space in their buildings, providing more tenant amenity, and 'plug and play' office space – blurring the lines between traditional leasehold space and flexible/co-working options.

WeWork acquired their first two regional sites in Manchester during 2017, and flexible office acquisitions in other regional markets are expected during 2018.

A severe shortage of new supply in regional markets will drive rental growth and a local authority response

The level of new supply delivered in regional markets will drop substantially in 2018 and the availability of grade A space will be severely constrained. Speculative development is limited in most markets. Only circa 700,000 sq ft is on site and due to complete in 2018 with approximately 50% of this in Manchester. Glasgow and Leeds have no speculative space on site due to complete in 2018 and Bristol's new Grade A vacancy rate is zero. Occupiers will increasingly need to come to market earlier to look at pre-let options. While refurbishments could help to fill the gap in some markets, the shortage will help spur prime rental growth.

This shortage will also encourage local authorities to get more involved in facilitating office development, as part of wider urban development and regeneration strategies.

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Industrial & Logistics

Andy Harding
Head of Industrial & Logistics
andy.harding@eu.jll.com
+44 (0)20 7087 5310

Jon Sleeman
Head of UK & EMEA Industrial Research
jon.sleeman@eu.jll.com
+44 (0)20 7087 5515

Labour availability will become increasingly important for logistics occupiers

Given low unemployment and lower net migration from the EU, the supply of labour will become a critical location decision factor for companies requiring large logistics facilities, which often demand significant labour. This will increase the attractiveness of some less prominent logistics locations. Building design will be affected too: compliance with the WELL Building Standard will become more common as developers seek to make their buildings more attractive to employees – and labour-hungry occupiers.

Last mile – urban logistics – will continue to rise up the agenda for corporates, developers and investors

This is partly due to rising e-commerce and the need to reduce order lead times to customers – it also reflects much wider issues centred on improving logistics in cities and urban areas whilst minimising adverse impacts, such as emissions and congestion. This could generate interest in different types of buildings and operations, including multi-storey warehouses, to make best use of land. In large cities such as London there will increasingly be consolidation centres on the edge of the centre to reduce peak time traffic in the CBD.

Building specifications and the use of technology will continue to change

There will be a trend towards higher warehouses with higher floor loading to accommodate growing requirements for multiple mezzanine floors. Gazeley's new Altitude building at Magna Park, Milton Keynes which has a clear internal height of 21m, with floor loading of 80kN per sqm, has led the way in this respect and we expect others to follow.

Meanwhile, we expect to see more business interest in automation and the use of robots in large buildings. There will also be growing interest in accessing on-demand (or dynamic) warehouse space available through online platforms. Electric delivery vehicles will become more widespread – requiring more charging infrastructure. Autonomous or driverless cars and lorries are not on the near-term horizon but we expect more advances with both. All parties, developers, investors and corporates, will seek to gain advantage from greater connectivity (the Internet of Things) and big data.

Given high rates of employment, low unemployment and lower net migration from the EU, the supply of labour will become a critical location decision factor for companies requiring large logistics facilities, which often demand significant labour.

Residential

Andrew Frost
Head of Residential
andrew.frost@eu.jll.com
+44 (0)20 7087 5566

Adam Challis
Head of Residential Research
adam.challis@eu.jll.com
+44 (0)20 7399 5324

Flatter Pricing and Rents in 2018 and beyond

In an environment where GDP is weak, wage growth is subdued, and the political backdrop uncertain, it is unsurprising that JLL forecasts for prices and rents remain flat. The picture improves beyond 2020 as the post Brexit economy begins to improve and consumer confidence returns. But there are more profound structural changes underway.

In particular, the economic conditions that have driven house price growth of 6.9% pa over the past 20 years will recede. In 2017, we saw the first upward move in base rates for a decade, driving up the cost of mortgages. At the same time, unsecured consumer debt has now topped £200bn and quantitative easing has hit £432bn. The appetite for buy to let has lost steam as a result of policy changes that will mean 40,000 fewer investment property purchases in 2018 alone.

Combined with a few other factors, notably stretched affordability, house price growth will more closely align with real wage growth for the foreseeable future. This will ultimately be a good thing for the market, but has profound implications for the next wave of homeowners who will not enjoy anywhere near the same wealth-forming benefits from home ownership as their parents.

More diverse sources of housing supply

300,000 homes is a big number. So is £44bn. The scale of the housing supply challenge is daunting, but Chancellor Phillip Hammond has offered up a package of loan guarantees and investment that will give the industry a good run at this target by the mid-2020s. To have a hope of easing the affordability crisis, policy is rightly promoting a wider range of developers to grow. SMEs, Registered Providers and the creators of Build to Rent products will all become flavour of the year, enabled to build more homes with support from a more muscular and rejuvenated Homes England.

In London, the emphasis through the new London Plan will be on densification of well-connected areas of suburbia. Government will also release greater swathes of public land, which will be tethered to greater proportions of genuinely affordable housing. However, this will not be enough. As JLL has been saying for years, the construction industry simply does not have the capacity to meet ambition. Government has finally got that message, and through the Housing White Paper we now have explicit reference to the role that Digital Construction will play in housing delivery.

The rise of Digital Construction

Digital Construction – Building Information Modelling, Off-Site Manufacturing and the feedback loop providing the first dynamic learning for the industry – will transform housebuilding. The revolution will begin 2018. Legal & General's long-awaited factory will come on line. New innovators, domestic and international, suppliers and builders, will not just conceive of new models but deliver them too.

For the existing industry, there are some profound implications. The PLC house builders are dominant, with a well-refined cash flow driven model, and little imperative to move to a faster build process. But the IRR-driven approach of Registered Providers and Build to Rent-ers recognises the additional value that can be generated by an earlier income stream. Alongside SMEs that do not have supply chain pricing control, these groups will drive investment in digital construction and create greater housing delivery capacity.

JLL forecasts 2018 - 2022

House price growth % pa	2018	2019	2020	2021	2022	2018-22 *
Prime Central London	-1	½	2	3	4	8.7
Central London Developments	0	½	2	3	4	9.8
Greater London	0	1½	2	3½	4	11.4
South East	0	1½	2	3	3½	10.4
Eastern	½	1½	2½	3	4	12.0
South West	1	1½	2½	3	3½	12.0
East Midlands	2	2½	2½	3	3	13.7
West Midlands	2	2	3	3	3½	14.2
Yorkshire & The Humber	2	2½	3	3	3	14.2
North West	3	3	3	3	3½	16.5
North	1	1	2	2	3	9.3
Wales	1	1½	2	2½	3	10.4
Scotland	1	1½	2	2½	3	10.4
UK	1	2	2½	3	3½	12.6

Rental growth % pa	2018	2019	2020	2021	2022	2018-22 *
Prime Central London	-2	-½	1½	2	2	3.0
Central London Developments	0	1½	2	2½	2½	8.8
Greater London	1½	2	2	2½	2½	10.9
South East	2	2½	2½	2½	2½	12.6
UK	2	2½	2½	2½	2½	12.6

Activity and development	2018	2019	2020	2021	2022	2018-22 **
UK transactions (m)	1.18	1.19	1.21	1.26	1.30	1.23
UK housing starts (000s)	200	200	205	210	215	206
UK housing completions (000s)	180	185	200	200	205	194
London housing starts (000s)	24	24	25	26	27	25
London housing completions (000s)	24	24	24	24	25	24

** cumulative growth; ** average pa*

Retail

Tim Vallance
Head of UK Retail & Leisure
tim.vallance@eu.jll.com
+44 (0)20 7318 7838

Colin Burnet
UK Retail Research
colin.burnet@eu.jll.com
+44 (0)20 3147 1185

The retail market will be challenging but pockets of outperformance will emerge

Despite the ongoing economic and political uncertainty, the macro fundamentals supporting retail sales remain relatively robust, namely low unemployment and ongoing (if moderate) economic growth. It is the inflationary driven squeeze in household spending that represents the most notable headwind to retailer performance in early 2018.

The retail market will become marginally more challenging in the short-term as these cyclical effects compound the long standing structural shifts. Pockets of the retail market will continue to deteriorate, particularly more secondary locations and less relevant centres that have been slow to respond to the ongoing challenges. But outperformance will emerge for those with expertise who can 'cut through the noise.' Major retail centres will continue to benefit from strong tourist spend, while convenience locations, where trading performance is robust and occupational costs more affordable, will also remain resilient.

Further casualties ahead, but the store will come back into focus

We must remember that poor retailers failed before the advent of e-commerce. That being said, UK retailers are arguably ahead of curve in terms of their response to the tech-driven structural change sweeping through the global retail market. The UK is certainly one of the most advanced e-commerce markets globally, evidenced by the slowing pace of online growth, which was down from 14.4% in 2012 to 7.9% in 2016. Despite this, the retail sector has not yet fully adjusted. Further casualties are an inevitability, and we also expect store closure programmes from some of the national multiples over the next 12 months. That's retail.

New types of retail occupiers and formats will emerge. The likes of Dyson, Tesla and Microsoft have already started to appear in high footfall locations - and more will follow. Unlike traditional 'brick and mortar' retailers, where the store is required solely for direct sales, these stores are principally a tool for raising brand awareness and improving customer engagement. The maturing online market is bringing the overall importance of the store back into focus – in particular its central role in the brand experience. The store can also drive online sales, particularly for categories where there is a preference to 'touch and feel' a product before purchase. Pure-play online will remain a marginal business; omni-channel is the future, but only if the product is relevant and the service is up to scratch.

F&B growth slowing – but strengthening links to leisure

In some areas there is a risk of oversupply of F&B, particularly where food has been used as an answer to rising vacancy. This is only an issue at a micro level, and will depend on the type of area and the competition present. But when viewed in conjunction with marginally slowing demand from F&B operators, which is certainly the case outside London, there is a danger of distress in pockets of this sector.

While there are undoubtedly challenges and headwinds ahead, there remain tangible reasons to be positive going into 2018. The growth of independent restaurant operators will fill some of the gaps, and take the opportunities left behind by some Private Equity backed chains. And demand for F&B will continue to grow from retailers themselves, as they increasingly see sublets to the sector as a differentiator. In addition, new formats will continue to emerge, driven in particular by the merging of retail and leisure. One to watch is Competitive Socialising (think Swingers, Flight Club and Putt Shack), where we expect to see demand rippling outwards from Central London.

Hotels

Will Duffey
Executive Vice President, Investment Sales
will.duffey@eu.jll.com
+44 (0)20 7087 5587

Jessica Jahns
Head of EMEA Hotels & Hospitality Research
jessica.jahns@eu.jll.com
+44 (0)20 7399 5821

Strong market fundamentals will continue to drive hotel growth during 2018, but it will be more muted than 2017
The weakening of the pound following the Brexit vote benefited hotels throughout the UK in 2017, with the number of inbound visitors expected to reach 40m, a 6% uplift compared to 2016. This influx enabled hoteliers to boost average rates by c. 5% in 2017. While we expect to see growth during 2018, the uncertainty over Brexit and slowdown in the UK economy may reduce business visits and dampen domestic spending, resulting in muted RevPAR growth. In London, the addition of 7,800 new hotel rooms poses pressure on hotel performance, however, it is hoped that the increase in tourism activity will counterbalance this.

Core+ capital funds being raised to invest into hotel real estate
We expect to see an increase in the amount of Core+ capital being raised across Europe in 2018. This will predominately come from private equity investors with a presence in Europe already, and with investments across all assets classes including hotels. This new capital will look for either single assets or portfolio opportunities across Europe and will target lower internal rates of return than typical opportunistic capital i.e. a 5.5-6% dividend yield. Leverage, or borrowing, is likely to be conservative at 50% of the fund.

Increased investment from institutional investors into hotel sector
Leased hotels represent an attractive opportunity with a number of advantages over other commercial properties, from diversification to a long-term lease to a single tenant. The UK Institutional market has invested heavily in leased hotels throughout 2017 as they continue to allocate investment funds towards the alternative sectors. The result has seen a number of benchmark yields being achieved not only within Greater London but also regionally as demand continues to out strip supply. As we look to 2018, there is no sign of the demand falling. Although a number of investors may have filled their quota of specific covenant allocation, new money continues to be raised and new investment vehicles created. We expect yields to remain at current levels, although transaction levels may be slightly down.

The UK Institutional market has invested heavily in leased hotels throughout 2017 as they continue to allocate investment funds towards the alternative sectors.

Construction & Development

Helen Gough
Head of Building Consultancy
helen.gough@eu.jll.com
+44 (0)20 7087 5090

Jon Neale
UK Head of Research
jon.neale@eu.jll.com
+44 (0)20 7087 5508

Construction costs will rise above inflation and impact on viability

The impact on material costs caused by the depreciation of the pound will fade throughout the year, but two other factors will drive up costs: skills shortages and tightening building regulations.

There has been a significant decrease in construction workers in recent years. Despite overall employment rising by 2.2m since June 2008, construction has lost around 316,000 workers. Brexit could accelerate this trend – EU nationals are believed to make up 12% of the workforce (it is higher in London). Some house builders suggest that 30-50% of employees are from Europe. More workers may choose to relocate if other economies perform better (or offer higher rewards in their home currency). Any additional barriers imposed as a result of the UK withdrawal from the EU are likely to produce further strains. The ageing nature of the existing workforce is also a problem, given the limited incentives for young people to enter the sector. Naturally, this will push up labour costs.

Meanwhile, as a result of the upcoming Baroness Hackitt report on Building Regulations, changed standards may impact costs, planning programmes and design decisions. The Grenfell Tower disaster highlighted areas in which building standards require improvement, and we may see standards brought into line with those in the US. It is likely that as a result of any changes made, build costs will increase by a minimum of 1%, and possibly by as much as 4-5%. This will constrain development, particularly in locations such as the regional cities where there are already concerns around lack of space.

Off-site construction becomes mainstream

Off-site manufacturing promises greater efficiencies in cost, building standards, sustainability, reliability, health and safety, labour and build time – all very attractive to a country which desperately needs new homes and suffers from a construction labour shortage. Indeed, it helps address the skills problem by generating new multi-skilled specialists.

Globally, the industry is expected to expand by 6% by 2022, but the UK currently lags behind a number of other countries, particularly Scandinavia, where these technologies are well established. We have now seen examples of successful implementation in Britain. The use of 'flying factories' by Skanska and Costain for the first phase of the Battersea Power Station redevelopment resulted in a 44% cost saving, 73% less rework and a 60% reduction in build time.

The government's Transforming Construction strategy – part of the recently launched industrial strategy – will provide public money to stimulate this much-need transition. JLL estimates that there is currently capacity to build 20,000 modular homes in the UK each year, although we feel up to a third of all units could be constructed in this way within 10 years, representing a significant opportunity for developers.

Countdown to April 2018: the minimum energy efficiency standard kicks in

The property industry has been aware of the Minimum Energy Efficiency Standards (MEES) for a few years now. It will be unlawful to let commercial properties below an EPC rating of E from April 2018. Following timely action by the more prudent investors, there will be greater evidence of risk being priced into investment deals, of lease provisions being revised to enable compliance and of uptake of energy efficient refurbishments. A likely outcome of this will be better information on standardised costs of upgrades.

Despite the advance warning, many landlords have still not engaged with the regulations, leaving nearly one in six properties at the risk of being noncompliant. We expect to see a flurry of leasing activity by such landlords seeking to avoid penalty by finalising a new lease before April 2018. Tenants may seek to capitalise by pushing for more favourable terms.

Landlords should be aware of the 2023 compliance deadline when MEES would apply to all existing leases as well, requiring either lease breaks or in-situ upgrades. Also, over the year, the first set of commercial EPCs dating from 2008 will be up for renewal. Given the changes in the assessment methodology, it is expected that a significant proportion of D and E rated assets will fall below compliance, exposing landlords to a much bigger risk than anticipated.

There might be clarity on longer term trajectory of EPCs. The Clean Growth Strategy sets out proposal for majority of domestic properties to be EPC C by 2035 and we anticipate similar level for ambition for commercial properties.

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