



A substantial rise in unemployment
is likely towards the end of the year

UK Economy and Property Market Chart Book

Q3 2020

What's the forecast?



Anderson Wilde & Harris, Chartered Surveyors, have a practiced eye on the prevailing conditions in the property markets.

We are members of the RICS and we are experts in all aspects of real estate. But, just as important, we keep a weather eye open to ensure that our clients get the best advice available in changing economic times.



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RICS Forecasts

| | 2019 | 2020 | 2021 |
|---|------|------|------|
| GDP [average] | 1.5 | -9% | 7% |
| Bank Rate | 0.75 | 0.1 | 0.1 |
| Unemployment rate [average] | 3.9% | 8% | 6.5% |
| Construction Output (y/y average) | 1.3% | -9% | 6% |
| House price index (y/y average) | 0.9% | Zero | -1% |
| HMRC Real Estate Transactions | 1.2m | 0.9m | 1.1m |
| Commercial capital values (y/y average) | -2% | -12% | Zero |

RICS Survey Release Dates

| Frequency | Survey | Period covering | Release date |
|-----------|--|-----------------|--------------|
| Monthly | RICS Hong Kong Residential Market Survey | July | 19-Aug-20 |
| Monthly | RICS Portuguese Housing Market Survey | July | 29-Aug-20 |
| Monthly | RICS UK Residential Market Survey | August | 11-Sep-20 |
| Monthly | RICS Hong Kong Residential Market Survey | August | 22-Sep-20 |
| Monthly | RICS Portuguese Housing Market Survey | August | 25-Sep-20 |
| Monthly | RICS UK Residential Market Survey | September | 09-Oct-20 |
| Quarterly | RICS UK Facilities Management Survey | August | 17-09-20 |
| Monthly | RICS Hong Kong Residential Market Survey | September | 20-Oct-20 |
| Quarterly | RICS UK Commercial Property Monitor | Q3 2020 | 26-Oct-20 |
| Quarterly | RICS Global Commercial Property Monitor | Q3 2020 | 26-Oct-20 |
| Quarterly | RICS UK Construction Monitor Survey | Q3 2020 | 07-Nov-20 |
| Monthly | RICS Global Construction Monitor | Q3 2020 | 07-Nov-20 |

Economic Outlook

On the face of it, the UK is now in the recovery phase from what can only be put down as pretty much the worst quarter for GDP since records began. Looking closely at the latest labour market indicators however, it seems like challenging times still lie ahead. Flash estimates by HMRC for example suggest that employment through PAYE has already slipped by almost 750,000 in the last five months. What's more, experimental statistics by the ONS suggest that unemployment related universal credit claims have risen by 1.4 million since March. It is almost inevitable that these numbers will increase in the coming months as the government's job retention scheme is withdrawn. Predictably enough, the unemployment rate looks set to climb. It wouldn't come as a total surprise if the jobless rate rises from 3.9% currently to above the 8% mark in the last quarter of 2020.

GDP is set to fall sharply this year

Data compiled by Jefferies points to an initial revival in public transport usage, flight activity and UK visits to accommodation sites over the past few weeks. Most forecasters are anticipating a fairly significant pick-up in activity in the coming quarters. According to Oxford Economics, quarter-on-quarter GDP could rise by more than 14% in Q3 and by 6.5% in Q4. In spite of this recovery, we still envisage the economy to be down by around 9% this year.

The Office for Budget Responsibility

(OBR), reflecting some of the challenges in producing forecasts right now, has constructed three scenarios with different assumptions about the timeline for finding a vaccine, the pace of the recovery and the degree of long-term scarring. Significantly, double digit declines in GDP for this year are envisaged in all three scenarios, with estimates pointing to a drop of between 10.6% and 14.3%. A partial recovery is envisaged in 2021 however the OBR judges that output will not be back to where it was before the crisis hit until 2022. One thing to take away from the OBR's analysis is that the fiscal costs of this shock are enormous.

Government debt levels look set to rise substantially

The OBR's central scenario is that borrowing will reach 16.4% of GDP (the highest in peacetime history), taking government debt from 89% of GDP in 2019-2020 to around 104% this year. Debt is set to remain above 100% of GDP for the next five years. In the downside scenario (which assumes that a vaccine is not found and output recovers a much slower pace than in the central scenario) borrowing and debt levels could end up being a lot higher. Indeed, preventing a huge and permanent decline to output will be on top of the government's agenda for now, suggesting that a further loosening in fiscal policy is likely in the near term.

The OBR however has highlighted significant challenges around compounding long term pressures on public finances from an aging population and a rise in health and social care spending. This suggests that some adjustments in fiscal policy in the form of higher taxes is likely to be warranted further out.

However low interest rates could help to keep debt servicing costs manageable

One thing that could relieve some of the pressure on government finances is that ultra-low interest rates and the quantitative easing program can be used to help finance public borrowing at least for the foreseeable future. The Bank of England key policy rate is at record low of 0.1%. Financial market expectations are consistent with interest rates remaining close to zero in the coming years. Our projections are broadly similar. The topic of negative interest rates is being widely discussed but the Bank, at least for now, does seem reluctant to go down this road.

Housing sales are likely to recover in the coming months

Activity in the housing market has recovered somewhat with the latest HMRC data pointing to up-tick in the number of sales completed in June. Indicators to the latest RICS Residential Market Survey are consistent with a further pick-up in activity in the second half of this year. Whether this trend will be sustained is however open to question. Average twelve-month sales expectations

suggest that the recovery may run out of steam further out with unemployment looking likely to rise towards the end of year and the stamp duty holiday coming to an end.

Feedback to the RICS UK Q2 Commercial Property Survey suggests rents and capital values are likely to fall sharply across retail and office sectors in the coming year. Furthermore, the results indicate there could be significant changes for the office sector moving forward, with 93% of respondents to the Q2 survey anticipating businesses scaling back their office footprint to some extent over the next two years.

Infrastructure work could support activity in the construction sector

Following a broad-based decline in output in the second quarter of the year, the results to the RICS Q2 Construction and Infrastructure Monitor suggest that infrastructure workloads could help to support sector recovery over the next twelve months. This seems a response to the government's recent announcements regarding infrastructure spending. Reforms to the planning system, new residential permitted development rights, a stamp duty holiday and an extension to help to buy should all help to support activity in the private housing sector notwithstanding the macro uncertainty.

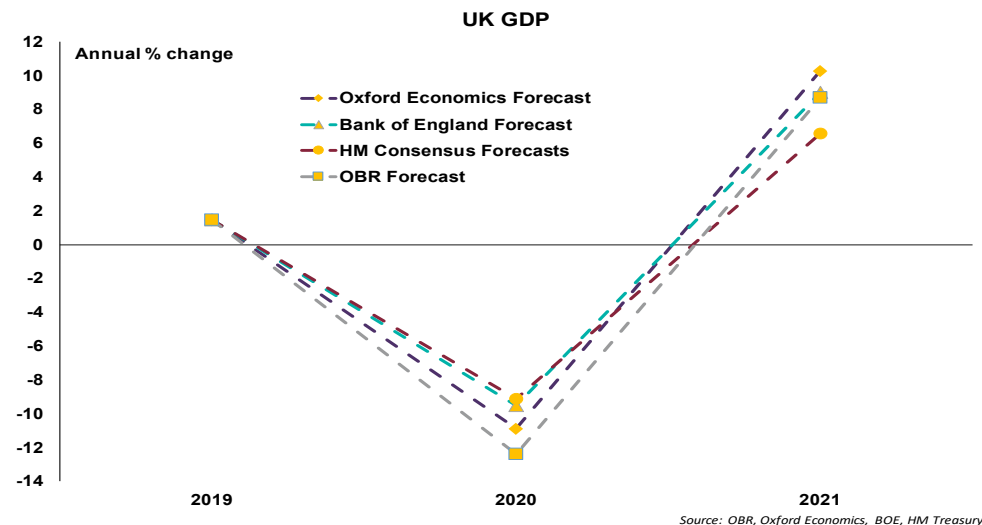
UK Economy

Following a sharp contraction in Q2, output is expected to recover somewhat in Q3 and Q4 on the back of a relaxation in government restrictions and a modest revival in consumer and business activity. In spite of this, forecasts are pointing to a substantial decline in GDP for the whole of 2020 (Chart 1). Our judgement is that, on an annual basis, output could slip by around 9% this year.

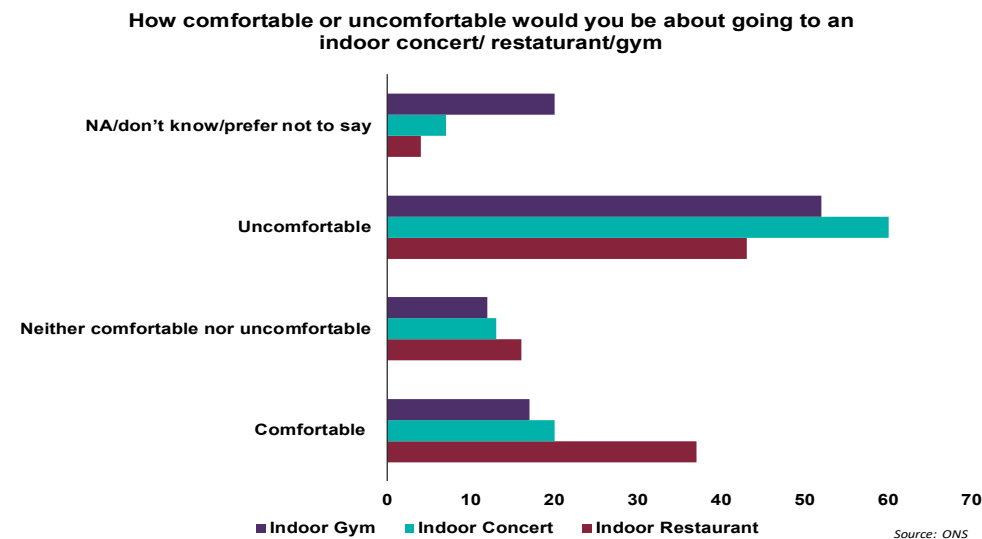
There is a risk that persistent uncertainty around the continuing health risks from Covid-19 could hold back a recovery in consumer spending in the coming months. A recent ONS survey (released on 7th August) around the social impacts of Covid-19 suggested that more than 50% of participants would feel uncomfortable attending an indoor concert or going to an indoor gym while 43% would feel uncomfortable about eating indoors at a restaurant (Chart 2).

Following a relaxation in government restrictions, retail sales rose by 13.9% on a month-on-month basis in June driven by a release of pent up demand (Chart 3). Meanwhile, non-store retailing has risen sharply in Q2, and is likely to remain strong in the coming months.

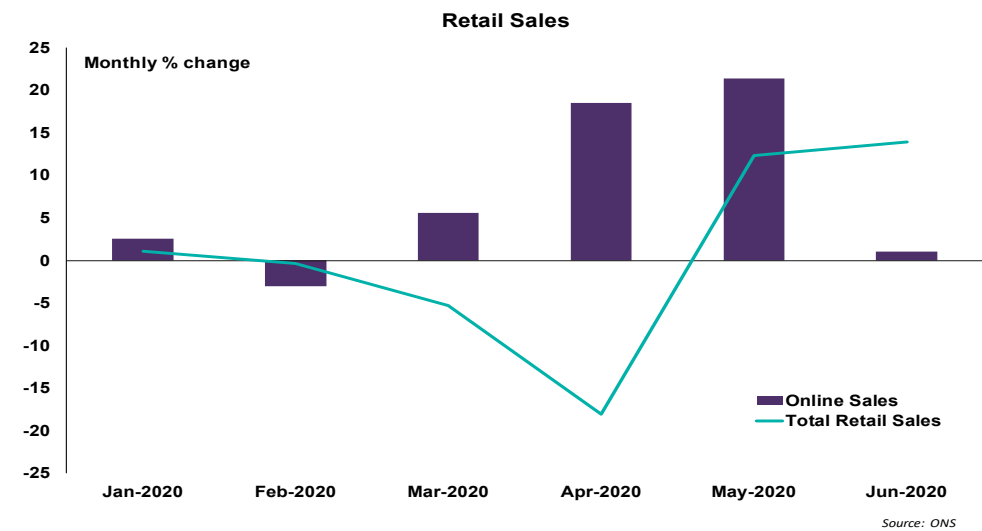
1. A double digit decline in GDP is likely this year



2. Consumers remain cautious



3. Retail sales rose in June as a result of pent-up demand



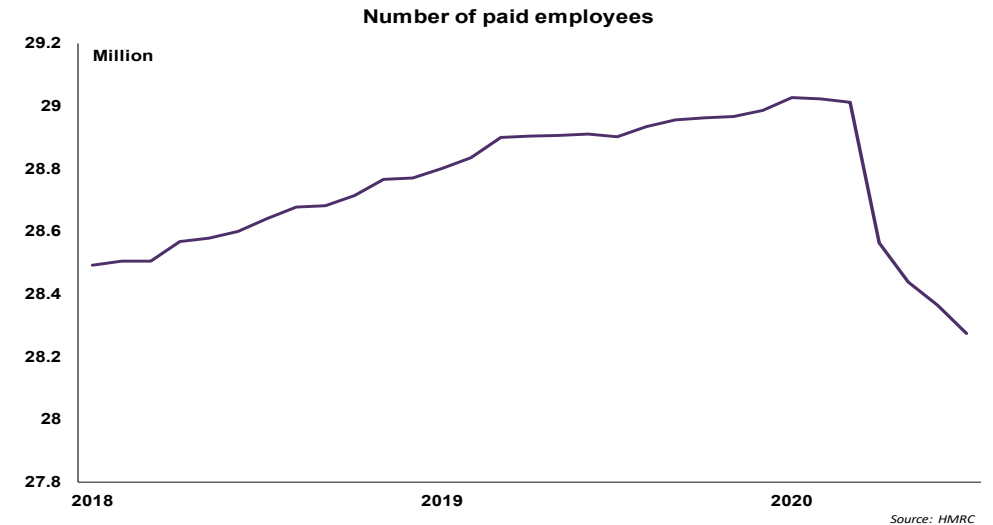
UK Economy

In spite of the support from the government through the Coronavirus Job Retention Scheme and the Self-Employment Income Support Scheme, employment appears to have fallen since the Covid-19 outbreak. Flash estimates by HMRC suggest that employment through PAYE has slipped by almost 750,000 since March (Chart 4). It is likely that this number will rise in the coming months as support schemes wind down.

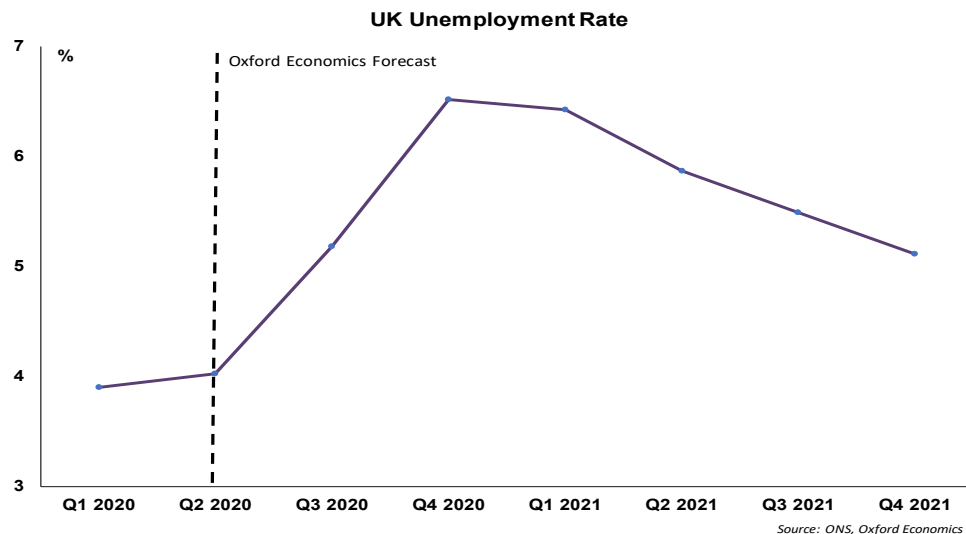
In turn, the unemployment rate is likely to increase significantly. As shown in Chart 5, forecasts by Oxford Economics indicate that the jobless rate could rise to 6.5% at the end of year (from 3.9% currently). Meanwhile, projections compiled by the Bank of England suggest that unemployment rate could, in fact, reach 7.5% in Q4 2020.

In addition, business investment looks likely to remain weak in the near term. In the most recent Agents Summary of Business Conditions survey, investment intentions have slipped materially in the past few months. Indeed, weaker sales and heightened uncertainty about the economic outlook are contributing factors behind this trend (Chart 6).

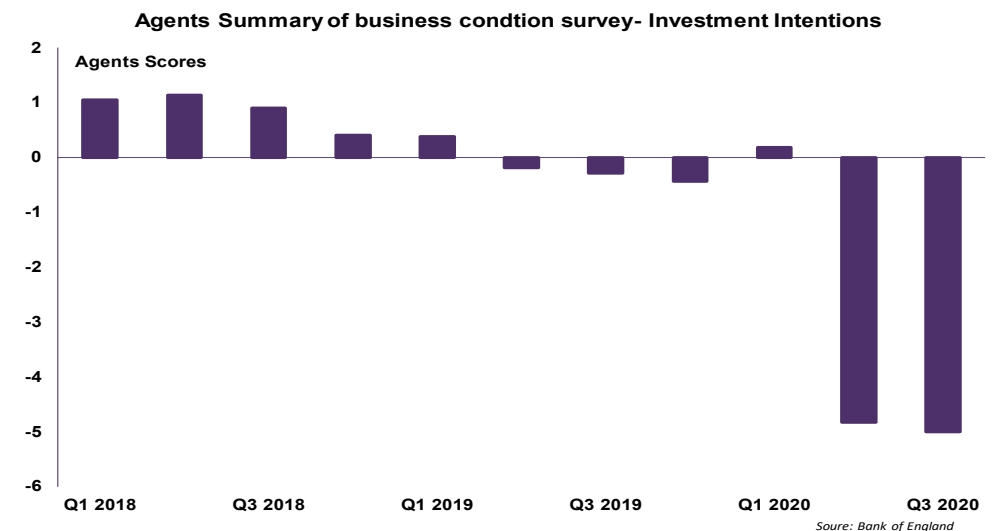
4. The number of employees has slipped sharply since March



5. The unemployment rate looks set to rise sharply



6. Investment intentions remain subdued



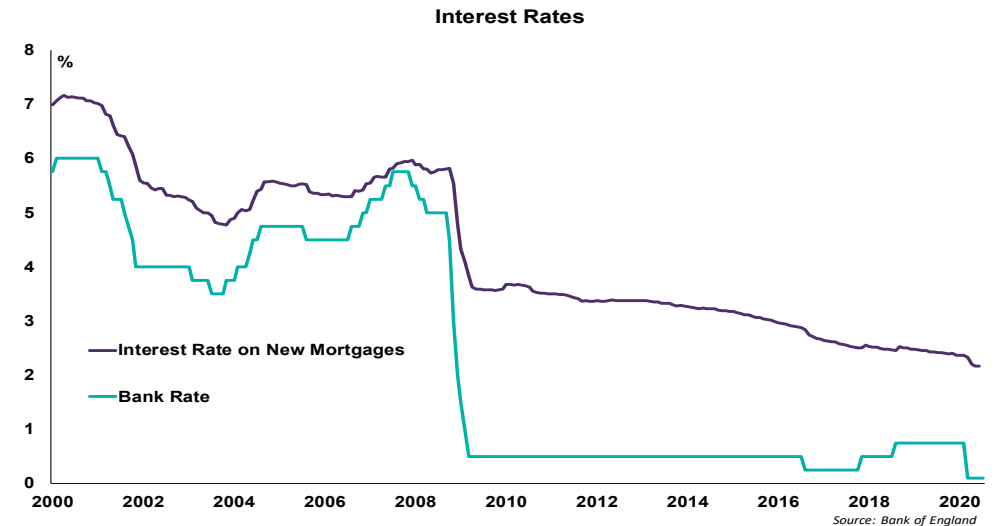
Housing Market

It is likely that government's policy interventions will provide some support to housing market activity in the coming months. For one, as the Bank of England cut its policy rate to 0.1% (the lowest in history), average interest rate on mortgages have also slipped, now standing close to 2% (Chart 7). This, combined with other policy measures such as the stamp duty holiday and the extension of help to buy could lead to a rise in housing transactions in the near term.

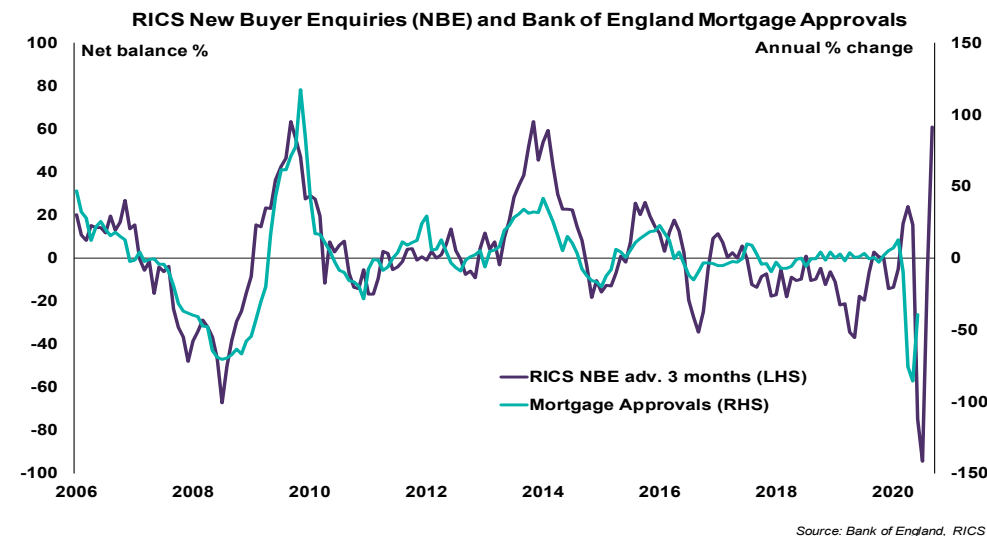
Notably, in the RICS Residential Market Survey, a net balance of +75% of respondents reported an increase in new buyer enquires in July. This suggests that mortgage approvals are likely to continue rising in the coming months (Chart 8).

That said, longer term expectations suggest that any uplift in housing market activity is unlikely to be sustained further ahead. Average twelve month sales expectations are entrenched in negative territory with concerns around higher unemployment levels towards the end of year once furlough schemes are phased out weighing heavily on the sales market outlook (Chart 9).

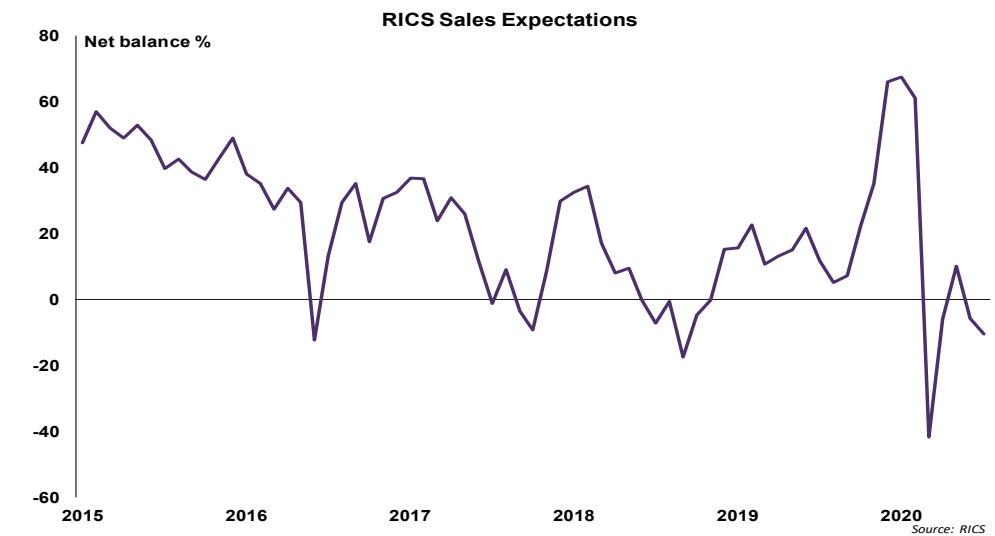
7. Interest rate on mortgages have slipped slightly



8. Mortgage approvals look likely to rise in the near term



9. The pick-up in activity is unlikely to be sustained further ahead



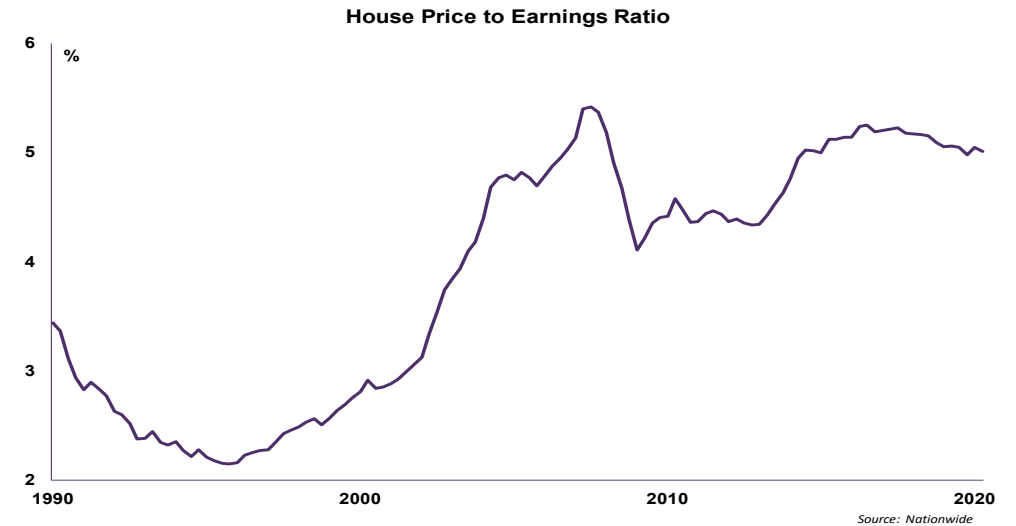
Housing Market

Nationwide data suggest that the ratio of house price to earnings has hovered around the 5% mark in the first half of this year, fairly close 2007's record high of 5.4% (Chart 10). It is likely that the stamp duty holiday and the extension of help to buy would support house prices at least in the near term, suggesting that affordability could remain stretched in many parts of the UK.

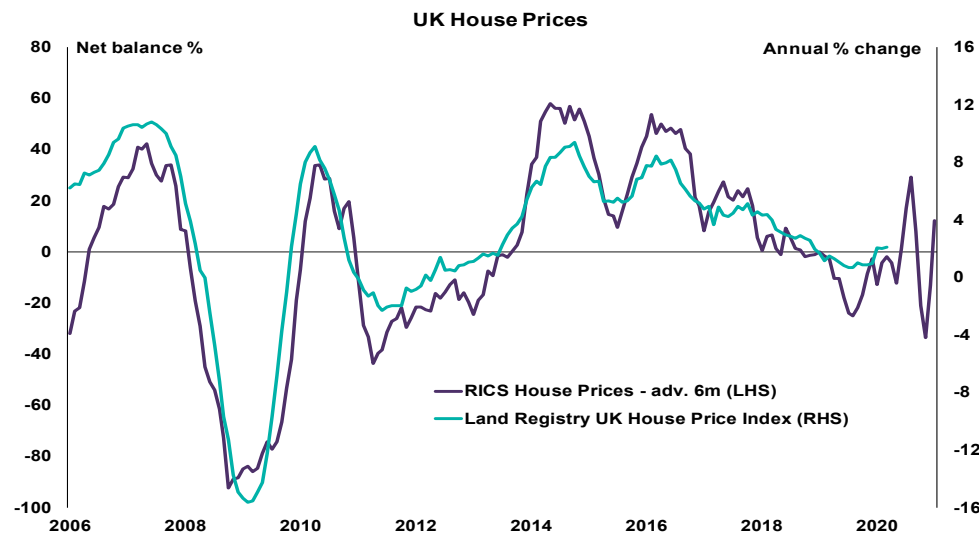
In the RICS survey, a net balance of +12% of respondents reported an increase in house prices in July. This series is good lead indicator of the official measure of house price growth and suggests that national price inflation could edge higher in the coming months (Chart 11).

Meanwhile, in the lettings market, headline near term rent expectations recovered noticeably in July with the net balance rising to +20% (from -35% in the last quarter). This points to a modest pick-up in private rents across the UK as a whole in the coming quarters (Chart 10). Average twelve month expectations suggest that rents are envisaged to rise in all regions apart from London where contributors are projecting rents to slip by 1% in the coming year.

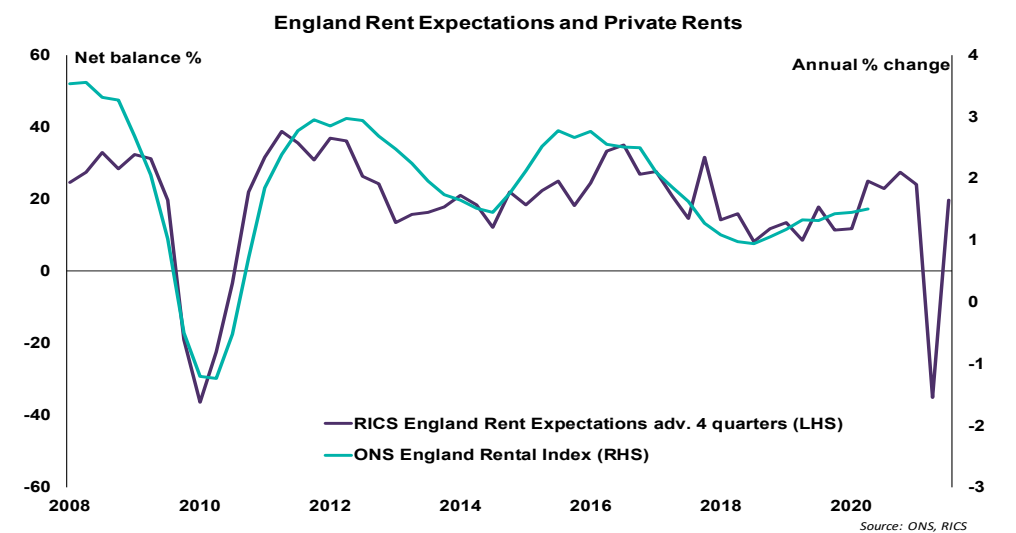
10. House prices to earnings ratio remains close to record highs



11. House prices look likely to edge higher



12. RICS data shows a rebound in rent expectations



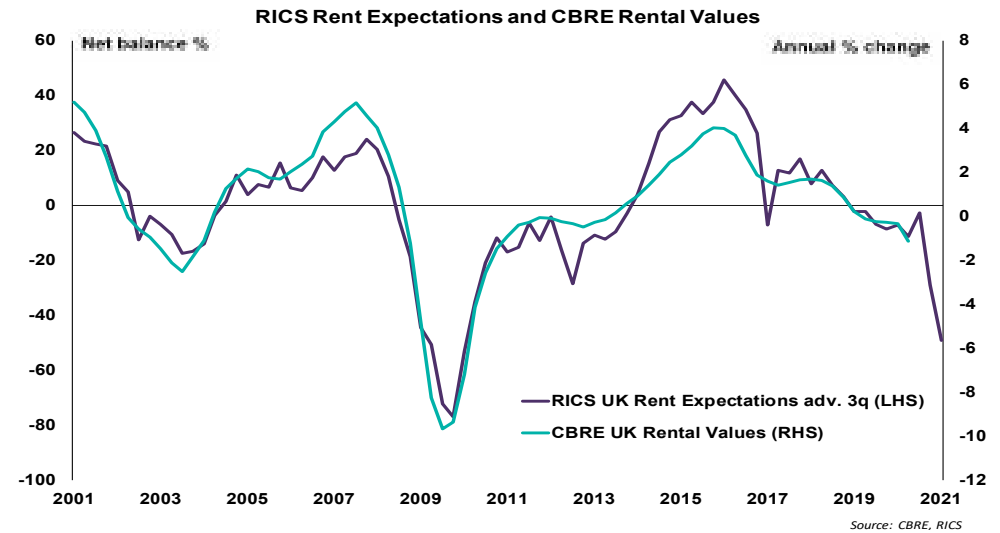
Commercial Property Sector

In the RICS UK Commercial Property Survey, the headline rent expectations net balance has declined in the past three reports slipping to -49% Q2 2020, from -29% in Q1 2020 and -3% in Q4 2019. This measure, as a lead indicator, in pointing a fall in UK rental values in the coming quarters (Chart 13).

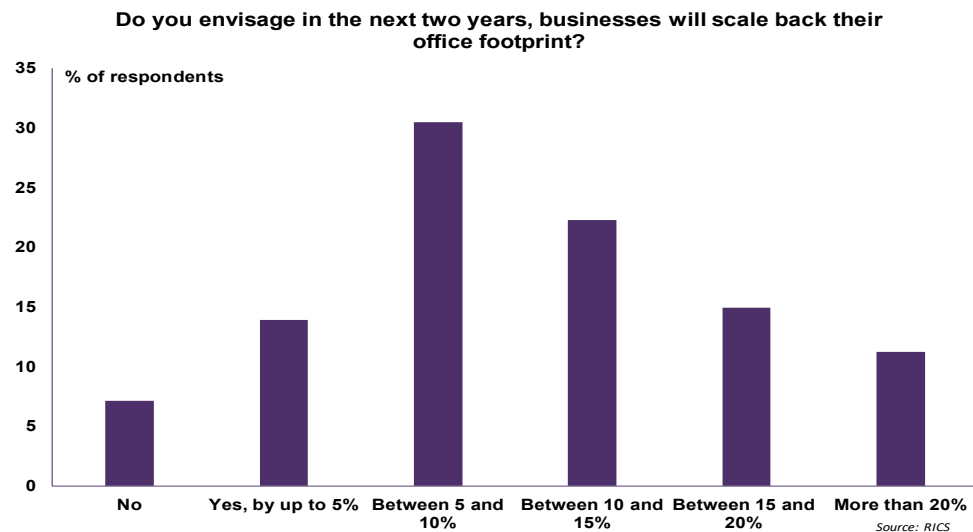
Research compiled by JLL on the future of global office demand suggests that in the long term, an increase in preferences for home-working could lead to a drop in demand for office space. Feedback to the RICS UK points to a similar trend, as 93% of respondents anticipate businesses will look to scale back their office space requirements to some extent in the coming two years. Furthermore, the largest share of contributors (30%) expect firms to scale back between 5 and 10% of their current footprint (Chart 14).

Meanwhile, it seems that the pandemic has accelerated the downturn in retail sector. This is highlighted by data from the Centre for Retail Research which shows that the number of retail stores affected by administration in the first half of 2020 is already above last year's total (Chart 15).

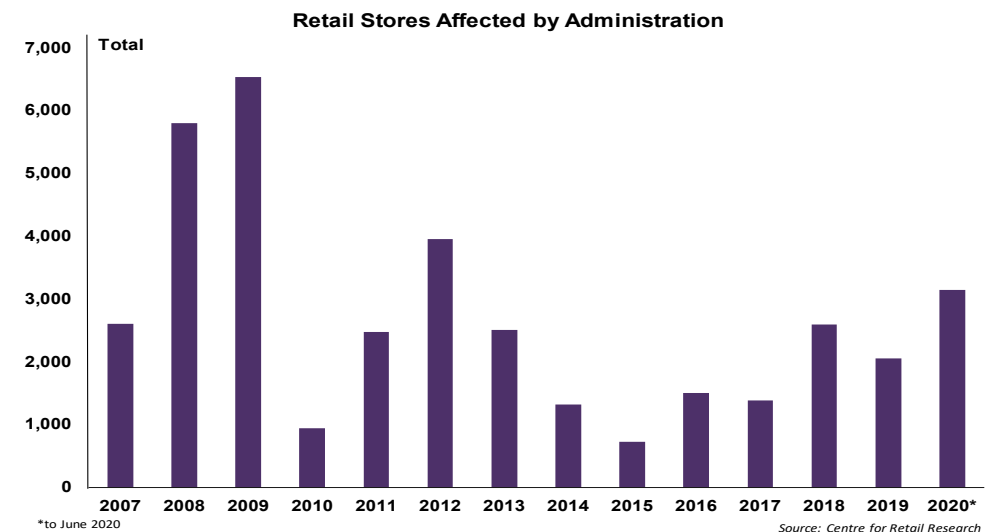
13. Rental values look likely to decline



14. Firms are expected to scale back their office footprint



15. Store closures so far in 2020 are already above those in 2019



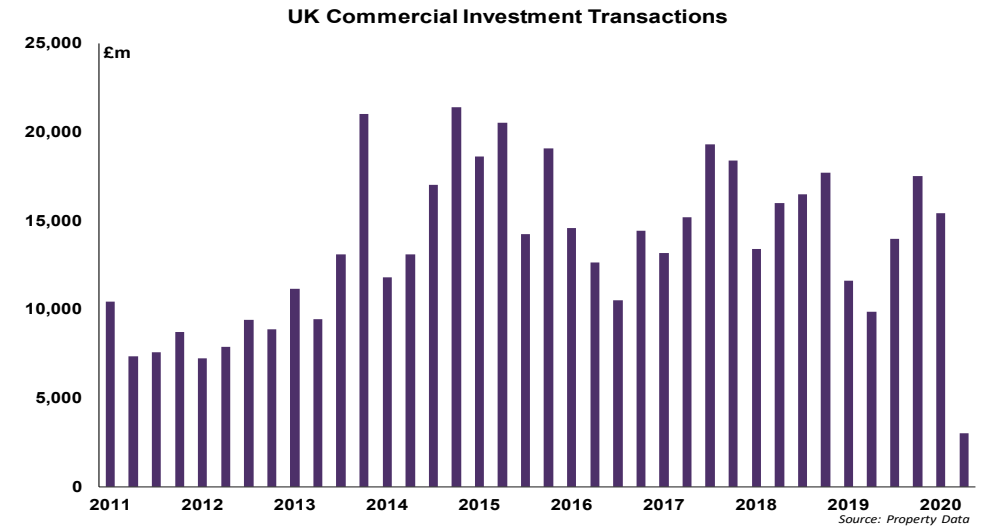
Commercial Property Sector

Investment market statistics compiled by Property Data suggest that UK commercial transactions predictably slipped very sharply in Q2. Still, it seems that this will prove to be a low point for investment transactions this year, and a gradual recovery in activity is likely in the coming months.

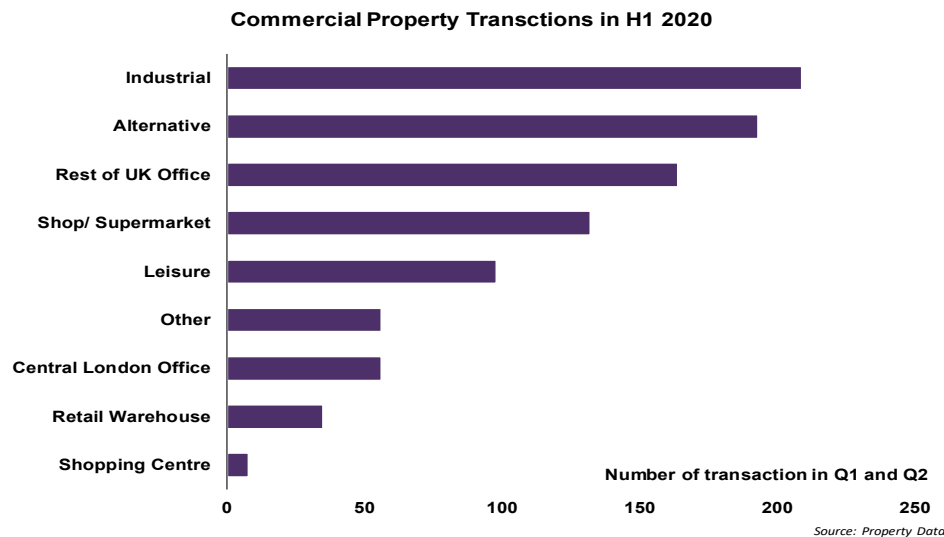
Indeed, the industrial segment of the commercial property market recorded in the highest number of commercial property transactions in the first half of 2020. At the other end of the spectrum, activity appeared to be particularly weak across the Shopping Centre, Retail Warehouse, and Central London office segments (as shown in Chart 17).

Average twelve month capital values projections in the RICS survey point to a sharp drop in capital values across the hotels sector, a result that is unsurprising given that travel restrictions remain in place across the globe due to the pandemic. Alongside this, projections indicate that a combination of cyclical weakness and structural change will continue to weigh on the retail sector. In comparison, capital values are envisaged to remain broadly stable in the industrial portion of the market in the coming year (Chart 18).

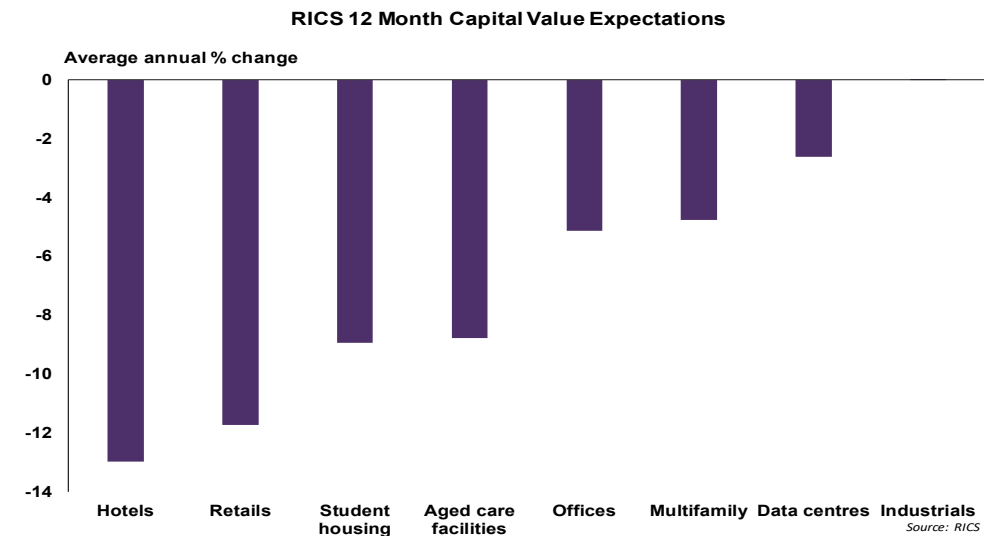
16. Investment transactions slipped significantly in Q2



17. Industrial sector continues to outperform



18. A significant drop in capital values is expected for hotels



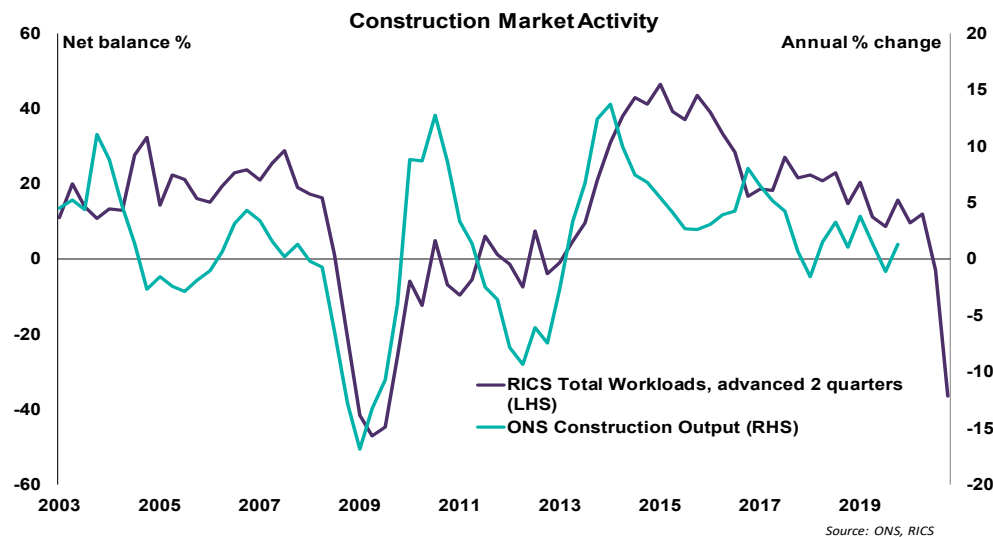
Construction Sector

With much of the industry required to close amidst the Covid related lockdown, survey data is consistent with a sharp drop in construction output in the first half of this year. This is visible in the latest results to the Bank of England Agents Summary of Business Conditions survey, where the Agent's score for construction output has slipped to a record low in the last two quarters (Chart 19).

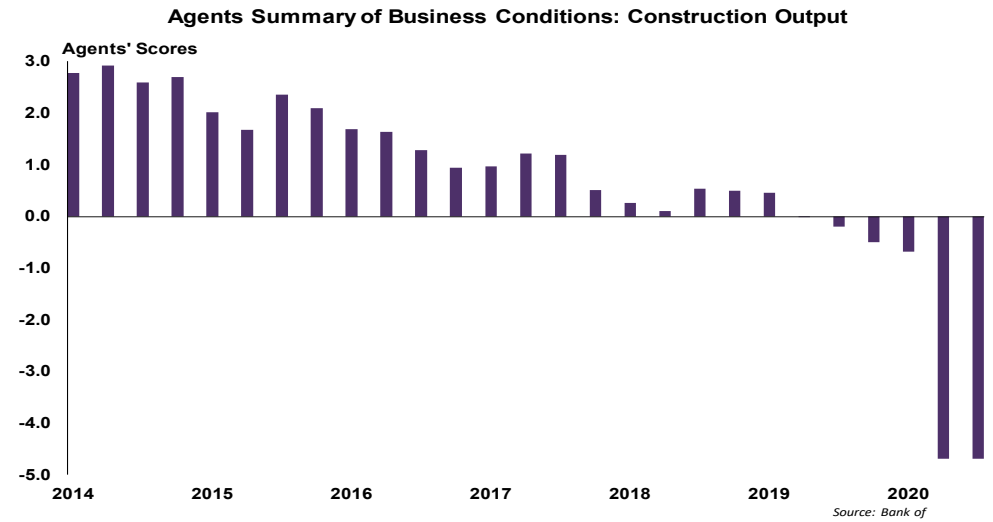
The Q2 2020 results to RICS UK Construction and Infrastructure Monitor are consistent with a deterioration in market sentiment with the headline workloads net balance slipping further into negative territory over the quarter (Chart 20).

That said, construction activity seems to have resumed somewhat after restrictions were lifted. Average twelve month expectation suggest that activity could continue to rise further ahead. Significantly, a net balance of +40% contributors expect infrastructure workloads to rise in the coming twelve months. This seems to be a response to the government's intention to boost infrastructure investment. Private housing workloads are also envisaged to rise, with new residential development rights, a stamp duty holiday, extension of help to buy and reforms to the planning systems likely to support activity in this sector in the year ahead (Chart 21).

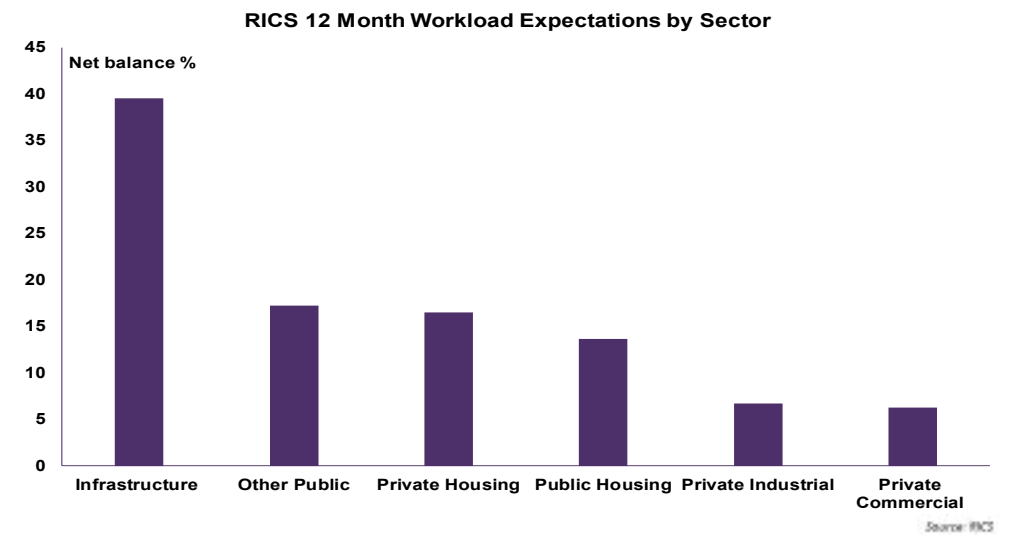
20. Output looks likely to fall in the coming months



19. Survey result point to a drop in construction activity



21. Infrastructure workloads could help support sector recovery



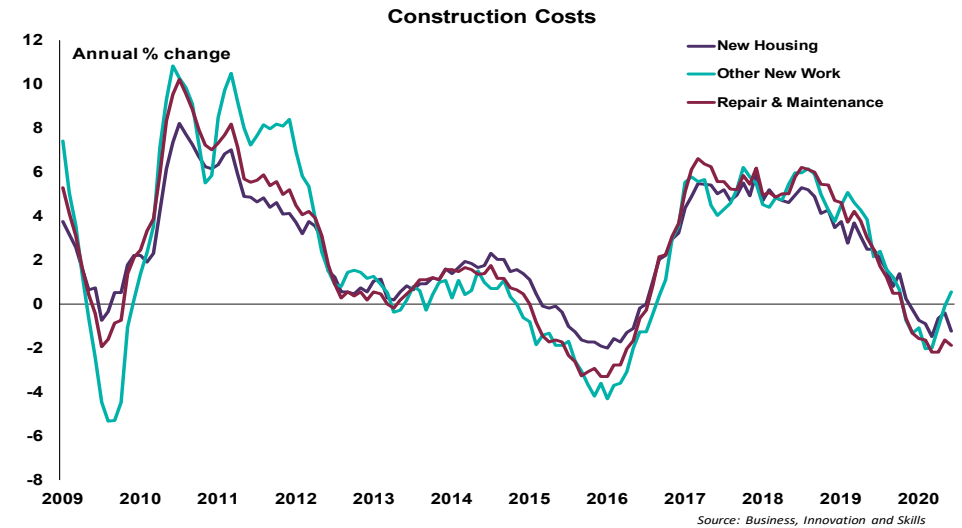
Construction Sector

Government statistics suggest that the price of building materials is falling on a year on year basis for now (Chart 22). However this trend could significantly reverse in the medium term if tariffs are put in place on imports from the EU once the transition period comes to an end. Furthermore, anecdotal commentary to the RICS UK Construction and Infrastructure Monitor suggests that global Covid-19 related lockdowns have led to problems in acquiring key materials.

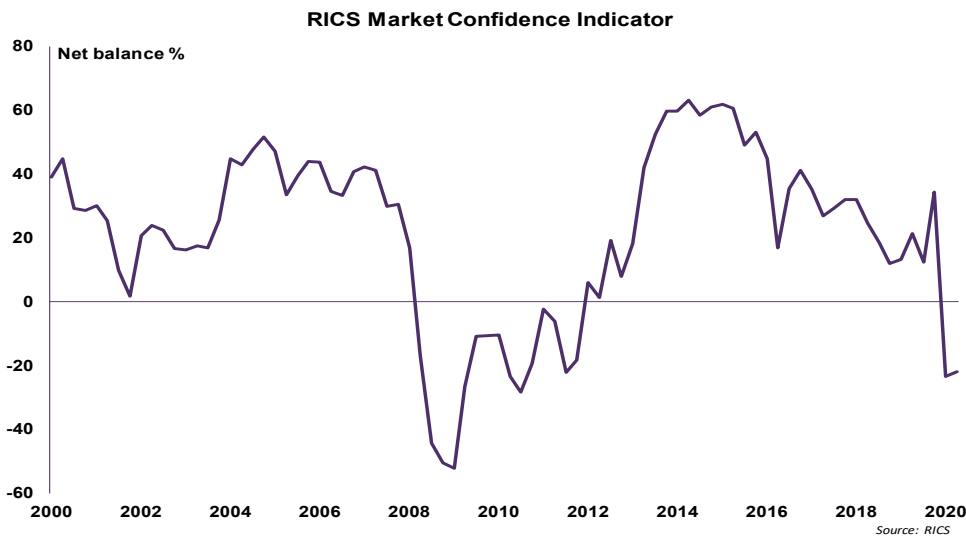
The RICS Market Confidence indicator, a composite measure of workloads, employment and profit margins expectations for the coming twelve months remained close to decade low in Q2 2020 (Chart 23). This is mainly as a result of downbeat outlook for profit margins and new hiring in the year ahead.

Meanwhile, onsite construction productivity, defined by as labour costs to produce the same level of output per month is expected to contract by the majority of participants to RICS Q2 2020 (as shown in Chart 24). The largest share of contributors (34%) estimate a loss of somewhere between 10 and 20%.

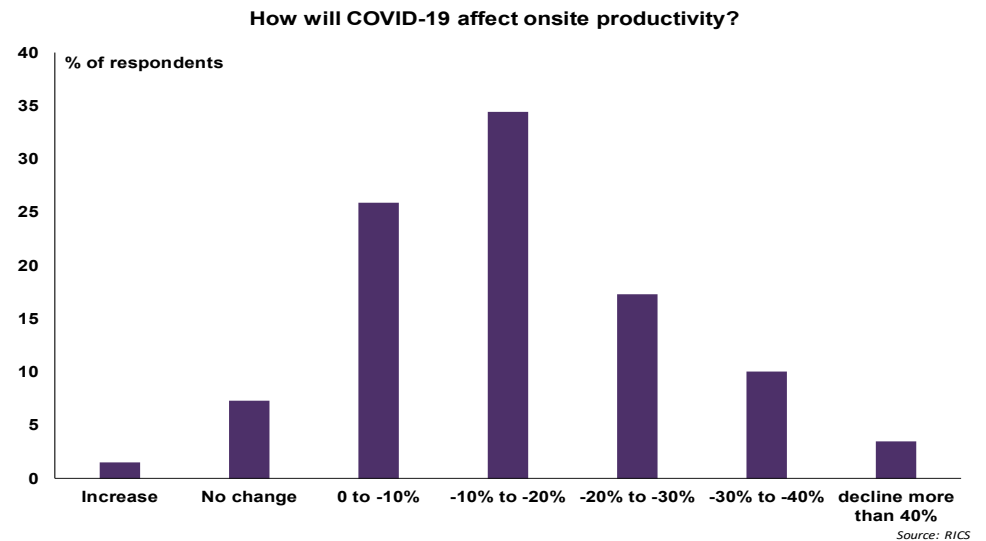
22. Material costs are falling on an annual basis for now



23. Market confidence remains close to decade low



24. Projects have been put on hold across the UK



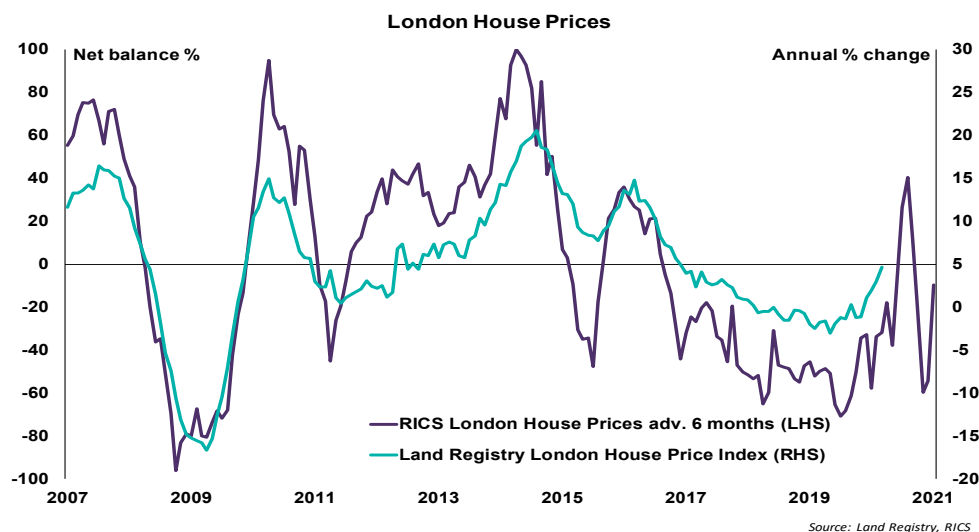
London

In the RICS UK Commercial Property survey, London office rents expectations fell sharply in Q2 2020 on the back of a drop in demand for office space and a rise in availability. This suggests that London office rental values are likely to fall in the coming months (Chart 26). Analysis by JLL suggests that in the long term, on the back of the Covid-19 pandemic, firms are likely to reconsider how they occupy office space with issues such as flexibility around working from home, workplace density, employee health and well-being likely to be taken into account. This could have a significant impact on city office demand and rental values in the medium term.

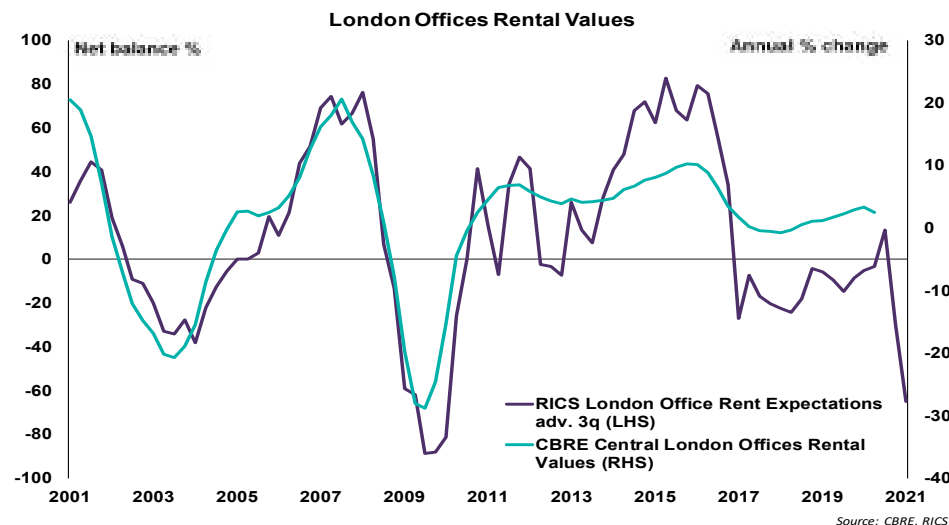
Turning to the residential market, in the RICS survey, the London house price balance picture looks relatively less downbeat in comparison to the couple of months with the house price net balance edging up to -10% in July from -54% in June (Chart 26).

Meanwhile in the lettings market, London rent expectation have slipped over the last two quarters suggesting that private rents across the capital are likely to dip over the course of the year (Chart 27).

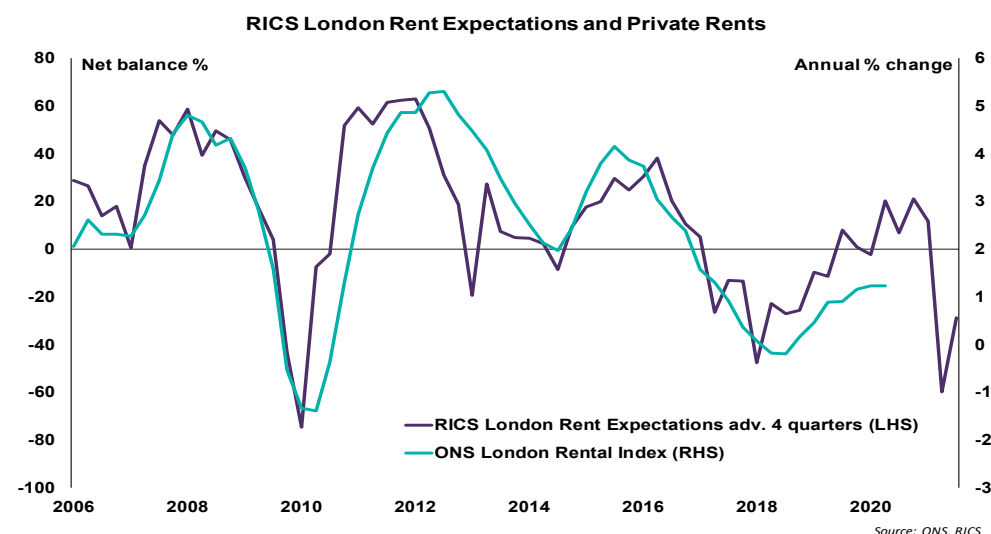
26. The London price picture has stabilised somewhat



25. London office rents are likely to fall in coming months



27. Rents look likely to fall across the capital in the coming year



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.

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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**

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- *UK Rural Market Survey (semi-annual)*
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- *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>

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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.

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