research

from Hurford Salvi Carr

MIDTOWN, CITY AND EAST LONDON

RESIDENTIAL 1ST HALF 2020

“

Rents fall sharply as vacancy levels rise.

Sales continue at pre-lockdown levels.

”

HURFORD SALVI CARR

Market Overview

GLOBAL PANDEMIC STRIKES

This is the most difficult half year report that we have had to write in 25 years. At the end of June circa 6,000 people in London and 500,000 globally had lost their lives to coronavirus. It is against this sobering backdrop that we report on London's housing market.

The political certainty provided by the December 2019 election result boosted housing market confidence in January and February. The strength of buyer demand in this early period of 2020 secured more sales across central London than at any time since mid 2014. Owners remained reluctant to sell at what they perceived to be low values and there was an expectation that a shortage of properties offered for sale would lead to price rises. The optimism we had predicted in our 2019 year end report, had materialised.

This positive sentiment was widely expected to continue through 2020 as the market finally looked as though it was on the brink of staging a recovery in prices. That early momentum was soon haltered by the spread of coronavirus (Covid-19), first in the Far East, then Europe, the Americas and across the globe. There had never been such a stark contrast between Q1 and Q2 at a start to any year as GDP plunged 25% and London found itself in lockdown and closed for business.

On 23rd March Prime Minister Boris Johnson, in a broadcast to the nation, announced what amounted to a lockdown of the economy with emergency measures to restrict all non-essential movements and prioritise the health of the nation and protection of the NHS care and essential workers, over economic activity. Shops and restaurants closed and office-based employment shifted to homes. In the following days the government announced a series of measures to support business and the wider UK economy through a period of inactivity.

The impact on financial markets was immediate. The FTSE index plummeted 5% on March 23rd as companies issued profit warnings and slashed dividends. There were of course winners including workplace technology stocks and logistics companies. More than 800,000 employers in the UK went on to furlough 9.2 million jobs with the government covering 80% of earnings up to a cap equating to an annual salary of around £35,000 between April and July and tapering the support between August and October. An additional 2.3 million of the self-employed benefited from similar support. At one point, the government was supporting earnings for over 30% of the working population.

The housing market was, in effect, suspended as soon as official guidance said that anyone in the early stages of buying or selling a home should delay the transaction. Banks had expressed concerns about valuation accuracy and granting credit during the pandemic. On Thursday 26th March, the guidance was extended to a ban on visitors being allowed into properties, including estate agents, surveyors and potential buyers. Mortgage approvals fell to 56,161 in March, the lowest in seven years and down by 24 per cent from February's six-year high of 73,674. The ONS decided not to publish its House Price Index in April.

On Sunday 10th May, in another broadcast to the nation and after seven weeks, the Prime Minister announced that there would be some cautious lifting of restrictions and estate agents were amongst the first activities to benefit. From later that week and under strict hygiene conditions, it would be permissible to conduct viewings of homes for sale or rent.

When the market re-opened on 14th May, transactions that had been put on hold during lockdown, were able to complete, and there was a rebound in buyer enquiries, offers and new sales. By the end of June a new market had emerged at the same pricing level experienced pre lockdown. Our view rests on the enduring fact that there are few forced sellers in our markets. Experience tells us that homeowners will prefer not to sell, rather than discount prices. We believe that the positive beginning to the year has been crystallised in a 1% price uplift in Midtown, City and East London between January and June 2020. It may be modest but it is the first price rise we have reported since 2016.

The rental market, on the other hand, experienced sharp falls in value. Many private tenants left London, returning to family homes outside the city to work from home, some were furloughed employees, others were students from UK and overseas whose universities were closed. This created a significant rise in properties available to rent in central London and led to a 10% fall in the weekly rental values between January and June 2020. It was a simple case of supply outstripping demand.

London's leisure and hotel sector which relies on overseas visitors, tourism and business travellers, was one of the most severely hit by the lockdown. It had an almost immediate knock-on effect on the revenue of short term serviced rental operators. With little prospect of their market returning, operators in this segment of the rental market gave notice on hundreds of apartment across the City Midtown and East London, adding to the weight of available supply.

One of the legacies of this extraordinary period is likely to be a permanent increase in working from home. While many people missed the camaraderie and creative energy of the office, it has proven that remote working is viable and for many, convenient. This raises questions about the role of the office under social distancing rules and the longer term future of the office now that an alternative more flexible workplace model has proved workable. It also has implications for the housing market if commute times become less of a driver and space to work from home more important. For our markets, some might appreciate the remarkable peace on the streets of central London but most hanker for a return to the bustle and vitality of city living.

At the end of June, prices were broadly at the same level as pre-lockdown as buyers cautiously returned and prices being achieved continued at pre-lockdown levels. Circumstances are different in the rental market because landlords will generally prioritise income over headline values and the key is to avoid periods of vacancy. This means that prices tend to respond quickly to fluctuations in supply and demand, and since lockdown, rental values had fallen by around 10%.

Economic Overview

GOVERNMENT SUPPORTS BUSINESS

Any account of the UK economy written in summer 2020 is bound to be dominated by the hammer blow of the global Covid pandemic. The year had begun with the promise of a speedy resolution to Brexit and bold commitments, backed by investment, to energise the regional economies. By May it was hard to recall the optimistic glow of that recent past and at the end of June it was still too soon to know what will be the long term impact on the economy but the short term impact has been acute.

Infrastructure investment, which was central to the budget in March, when the priority was to 'level out' differences across the UK regions, has proved to be a consistent theme and has remained key to government policy to kick-start the economy after Covid.

CLERKENWELL GREEN EC1 - 3 BEDROOM APARTMENT, SOLD JUNE 2020 £1,175,000

By mid-April the IMF was warning of global economic contraction on a scale that the world had not seen since the Great Depression of the 1930s and which would 'dwarf' the financial crisis of 2008. In the UK, a quarter of businesses temporarily closed and most of those still operating reported a fall in turnover. The OBR mirrored the IMF sentiment in its own outlook, suggesting that output could plummet by 35% in Q2 if lockdown was not lifted.

Lockdown continued through Q2 with only cautious steps to lift the restrictions in June. While some commentators still hope for a sharp economic re-bound in early 2021, albeit from a lower base, many have real concerns about falling earnings and rising job losses once the government support is reduced.

The government was quick to implement an enormous package of measures to support businesses during the pandemic. The furlough scheme, designed to avoid widespread redundancies, allowed employers to reclaim the wages bill for anyone given a leave of absence while they were not needed for work as a direct result of Covid. The government would pay 80% of earnings, up to a cap of £2,500 per month. By the end of June 9.2 million people were being paid by the state under the furlough scheme and another 2.3 million under a separate scheme for the self-employed. Initially planned to last 3 months from April, the Chancellor extended it until October, albeit with a reduced contribution from August.

Other support came in the form of business interruption loans administered by the high street banks and one-off grants to small businesses via the business rates system. The scale of the support is one reason that it is hard to anticipate the long term impact of the pandemic. If, as is hoped, large parts of the economy can re-open by the Autumn, then spending and earnings can be re-started.

Businesses and households cut spending during lockdown, partly reflecting a desire to preserve cash and partly because there were fewer opportunities to spend and so demand fell across the economy. Consumer spending fell by 18% in April 2020, following a 5.2% fall in March. According to the Bank of England, the amount held in sterling by private sector companies and households rose by £57.4bn in March, the biggest increase on record and far above the £9bn average for the previous six month period.

The Bank also published figures showing that £7.4 billion of consumer credit had been repaid in April, the largest monthly repayment since records began in 1993. On credit cards alone, £5 billion was paid off, compared to a typical month when it's around £300 million. However, there remains £64 billion outstanding and there are obvious concerns about the financial conditions of those who have lost income during lockdown.

Amongst businesses, there was a steep rise in debt. Private sector businesses borrowed an additional £8.4 billion from the banks in April on top of a record £30.2 billion in March. Low demand from consumers translates directly into low revenue for businesses.

In its forecasts published on May 7th, the Bank of England expected the economy to contract by 30% in Q2, quarter on quarter and an annual contraction of 14% in 2020, broadly in line with the 13% suggested by the OBR a month earlier under its Coronavirus Reference Scenario. Figures published in June, confirmed that the UK economy had shrunk by 20.4% in April - the largest monthly contraction in output since records began while output from the construction sector fell by 43.6% as activity ground to a halt across the nation.

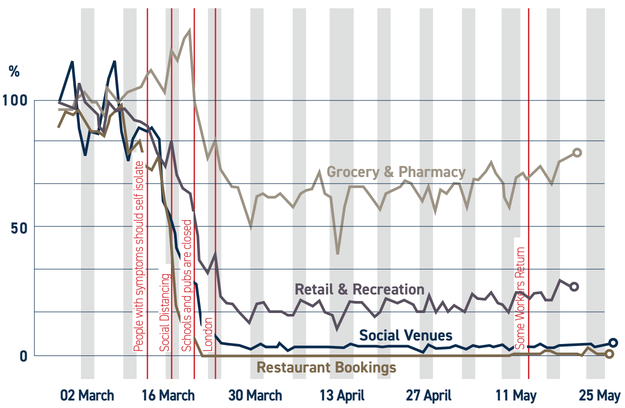
That meant that the UK economy lost 25% of its size. To set that in context, the peak to trough decline in the financial crisis of 2008 was just 6.8% and the largest monthly decline in September 2008 when Lehman Brothers went bankrupt, was around 1.25%.

LIMEHOUSE E14 - 2 BEDROOM APARTMENT, LET MAY 2020 £473 PW

The hospitality, travel and leisure sectors were hit harder and more completely than any others by the lockdown. Hotels, restaurants and visitor attractions closed their doors. Buses, trains and airports were reduced to essential skeleton services with very few passengers. Construction sites shut or slowed and all but essential shops closed too, although many had the alternative of online platforms and online retail was up by 18%. Supermarkets and home office equipment suppliers were coronavirus winners, able to increase sales while clothing sales dropped by over 50% in April following a 35% fall in March.

These sectors are major employers in London. The footfall figures show just how dramatically London changed in within the space of a few weeks.

FIGURE 1
RETAIL AND RECREATIONAL FOOTFALL ACTIVITY IN LONDON MARCH-MAY 2020



Source: Grocery and retail metrics from Google Mobility, social venues (bars, event spaces etc) from Purple public Wifi and restaurant bookings (national) from OpenTable

Note: Vertical red lines show changes in social distancing rules - Vertical grey bands show weekends and public holidays

However, much of the London economy is driven by well-paid office jobs in finance, professional services, consultancy, and tech, which can continue to function even under the work-from-home edict. That has meant that London is, in some ways, more protected than elsewhere in the UK. Almost one in two London jobs are office based and, in terms of earnings, the proportion is far higher. Nevertheless, three quarters (73%) of all London businesses applied for the Coronavirus Job Retention Scheme, and 63% for deferred business rates. Government support has been critical to the survival of London as elsewhere in the UK.

London also has particular challenges in returning to work posed by its reliance on public transport for commuting and the large number of businesses occupying tall buildings where the final leg of the journey to work is made in a lift - which is not conducive to social distancing. Before lockdown, over 40% of Londoners used to travel to work on public transport.

HIDE, HACKNEY ROAD E2 - 2 BEDROOM DUPLEX APARTMENT, SOLD MARCH 2020 £980,000

The passenger journey figures from London Transport are a stark indicator of how normal London life was put on hold. Less than 20 million journeys were registered in April, compared with over 183 million in March and 271 million in February.

The FTSE, which had attained record highs in February, plummeted during lockdown. While it has rallied in May after the restrictions of lockdown began to lift, the gloomy outlook for the economy has kept a lid on any significant rebound and investors remain wary of a second wave of coronavirus. In June, the OECD warned that the UK was likely to be one of the worst hit economies in the developed world and that most economies were at real risk of a second wave.

Inflation dropped from 1.5% in March to below 1% in April as commodity prices dropped, spending fell and savings rose. However, it is too soon to see the impact of non-essential shops re-opening in June. Given that production has reduced across the globe, it may be there will be some inflationary pressures in the shops over the summer. The government will certainly encourage an uplift in spending to boost the economy and, if that is not forthcoming, the Bank could consider negative inflation rates to prompt cautious consumers to spend some money.

In May, the Bank of England admitted that it was considering cutting the current 0.1% interest rate to below zero for the first time in its 324 year history but ultimately held rates at 0.1% in June. The banks have publicly objected to the idea, because it would reduce their profitability at a time that the sector is being expected to absorb coronavirus-related losses.

Fortunately, in addition to its long-established banking, finance, legal and insurance sectors, London also has a robust tech sector and a strong bio-tech and medical sciences cluster. These are both areas of the economy that have benefitted from lockdown and should help London to recover its economic health.


VOGUE
City Living
HOXTON NINE
waterside
City
avant-garde
SALE READY
SOLD
SHOREDITCH EXCHANGE
MAKERS
SHOREDITCH

Sales Market

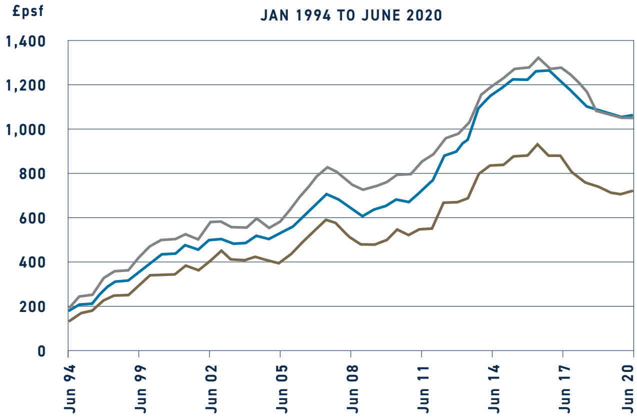
DEMAND BOUNCES BACK

In the first two and half months of 2020 a steady increase in demand helped secure more sales across central London than at any time since mid 2014. The combination of a newly elected majority government and greater certainty over Brexit, gave buyers the confidence to return to the market. Buyer enquiries at our London offices were 60% higher in Q1 2020 than in Q1 2019 and sales volumes began to increase. We even experienced a number of best bids situations in those early months, where offers exceeded the asking price.

Also welcome, was the return of the market for high end sales between £1.5m and £2m, especially in the West End which had taken the brunt of price falls over the previous 4 years. In short, the green shoots of recovery that we highlighted in our 2019 year-end report had started to mature.

Our experience seemed to be mirrored across London. The Evening Standard reported on 21st February that gazumping had returned to the London market for the first time in 5 years as buyers were desperate to snap up a bargain.

FIGURE 2
PRICE TRACKER - ONE BEDROOM APARTMENT
JAN 1994 TO JUNE 2020



Source: Hurford Salvi Carr *Data based on the value of a 500 sq ft one bed apartment in the re-sale market*

BLOOMSBURY WC1 - 2 BEDROOM APARTMENT, SHORT LEASE SOLD MARCH 2020 £550,000

By March there was a growing shortage of properties available and the market quickly tipped in favour of the seller. Buyers hoping to be able to negotiate on price were disappointed. Buyers who had delayed making offers in the hope that the Chancellor would announce a Stamp Duty cut in the Budget on 11th March were caught out when COVID-19 hit and London was plunged into lockdown.

The market slipped into hibernation on March 26th when ministers issued official guidance telling people in the early stages of buying or selling their home to delay the transaction and banning visitors to properties, including estate agents, surveyors and potential buyers.

Banks effectively closed their doors for new mortgage lending during lockdown and imposed a cap on the value of mortgageable properties for as long as surveyors were unable to visit homes. Their reasoning was that professional indemnity insurance, designed to protect surveyors against litigation, does not cover big loans for expensive homes which they have not visited in person. Meanwhile mortgage lenders were kept busy processing applications for mortgage holidays. By the end of May, over 1.86 million borrowers, or one in six mortgages, had been granted payment holidays.

Most of the stalled transactions proceeded to completion after the lifting of lockdown. We, like most agents, found that buyers who had wanted to move before lockdown, remained engaged and motivated to move this year.

One announcement the Chancellor did make in his pre-Covid budget was that there would be a 2% SDLT surcharge on non-UK residents purchasing residential property in England and Northern Ireland which would come into effect on 1 April 2021. This charge comes on top of an already punitive stamp duty regime for high value homes and a 3% surcharge for second homes. An overseas buyer could end up paying stamp duty of 17% cent on property values over £1.5m. When policy is given a future implementation date, it almost always fuels demand in the period running up to the deadline and it will encourage overseas buyers to complete on purchases before April 2021.

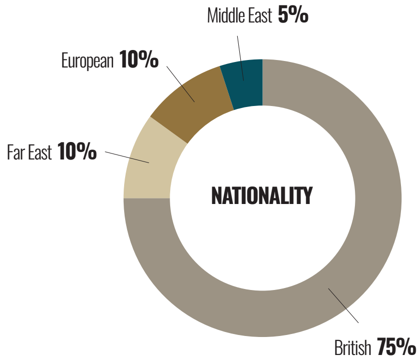
FARRINGDON EC1 - 3 BEDROOM APARTMENT, SOLD MAY 2020 £945,000

They will be joined by an influx of buyers for whom lockdown has prompted new life choices such as young adults keen to fly the nest and workers who have found that working from home could have a long term future and that they need more space to set up a home office, or at least a home workstation.

BUYER PROFILES MID 2020

Nationality

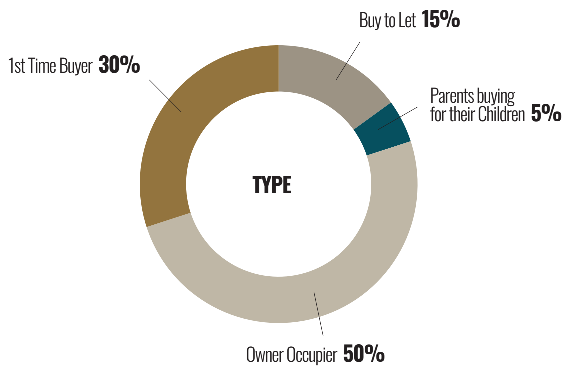
The volume of transactions in our markets was low in H1 2020 and this is reflected in the sample size for our buyer profile analysis. Nevertheless, the results for the first 6 months of 2020 highlight some changes that are noteworthy.



British buyers will always be a dominant group in our markets but this time they made up three quarters of all sales, compared to 62% in the same period last year. Overseas buyers remained active and we welcome the return of EU citizens in our markets who were absent in the same period of 2019. As we noted in the text, buyers from the Far East remained in evidence even during the Covid-19 period. The security laws in Hong Kong prompted investors to strengthen their ties with the UK, encouraged when the UK announced an intention to loosen visa restrictions.

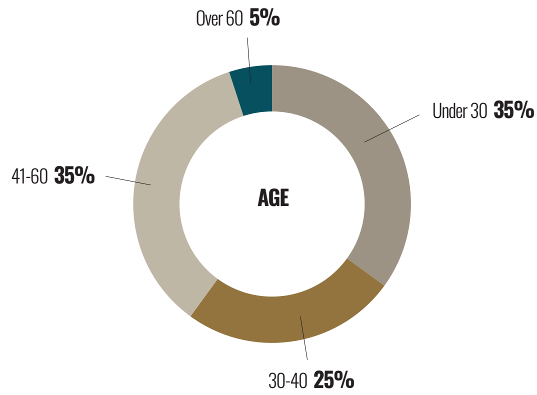
Buyer Type

There were far fewer parents buying for children in this period. It is a short period and sample sizes are low but this could presage a fall in the number of overseas students for the next academic year because they are often the key players in this category. It is too soon to call a trend and they may simply have delayed purchases until matters are clearer. We were pleased to note the presence of buy to let investors and first time buyers.



Age

There was a remarkably even distribution by age with the exception of the over 60 age group which are always a minority. Compared to the same period in 2019, there is a stronger shift to the younger age groups and it is surprising to see under 30s making up a third of buyers.



Funding

Almost a third of buyers borrowed more than 75% of the purchase price to acquire a property in our markets and 20% funded entirely with cash. This demonstrates the polarity of our markets where the presence of overseas buyers tends to elevate the number of cash buyers although we have had no purchases for use as a pied a terre so far this year.

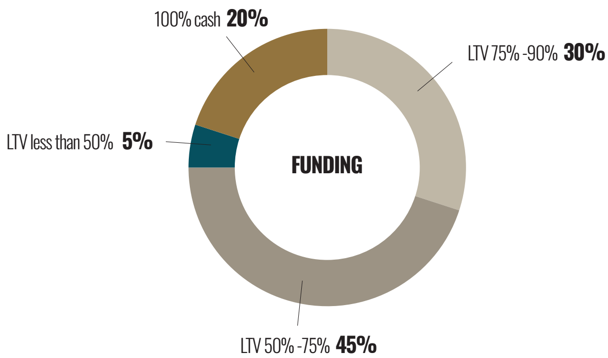


TABLE 1
PRICES AND ANNUAL GROWTH FOR ONE BEDROOM APARTMENTS IN THE RESALE MARKET AT H1 2020 : AVERAGE FOR MIDTOWN, CITY & EAST LONDON

Year	Annual Price Change %	Market Value £	Annual Change in Value £
1998	N/A	150,000	N/A
1999	26%	189,000	39,000
2000	11%	210,000	21,000
2001	10%	230,000	20,000
2002	13%	260,000	30,000
2003	-8%	245,000	-15,000
2004	0%	246,000	1,000
2005	10%	270,000	24,000
2006	26%	340,000	70,000
2007	9%	371,000	31,000
2008	-15%	318,000	-53,000
2009	8%	338,000	20,000
2010	4%	351,000	13,000
2011	10%	386,000	35,000
2012	5%	405,000	19,000
2013	20%	486,000	81,000
2014	8%	520,000	34,000
2015	6%	550,000	30,000
2016	1%	555,000	5,000
2017	-4.5%	530,000	-25,000
2018	-8.5%	485,000	-45,000
2019	3.1%	500,000	15,000
H1 2020	0%	500,000	0

Source: Hurford Salvi Carr

On May 10th, the Prime Minister gave a broadcast to the nation setting out plans for a gradual lifting of lockdown but conditional on monitoring infection rates, death rates and the 'R' number. Over the subsequent few days, details were clarified of business support packages and from Wednesday May 13th, people would be able to visit estate agents' offices, show homes and view properties for sale. This was a red letter day for the housing market and marked a turning point in the year.

By June the level of new enquires were encouraging, with many buyers increasing their budgets to secure larger properties that are better suited to working from home. We do not underestimate the attraction of apartments in Midtown, City and East London as cost effective alternatives to serviced offices or co-worker spaces for small businesses and consultants.

Buyers who had intended to act pre-COVID-19 resumed their searches in May and June. Chinese investors, who are accustomed to buying remotely from exhibition rooms started to reappear, initially facilitated by the use of virtual viewings. There was also a notable increase in interest from Hong Kong buyers following the Chinese imposition of new security laws in Hong Kong and particularly after the British government responded in late May with an offer of extended visa rights to Hong Kong citizens.

Prices edged up by 1% in the first three months of 2020 the first time we have reported an overall increase since 2016. Early indications from the post-lockdown market, are that asking prices are unchanged and, while buyers are initially cautious and inclined to test the market with low offers, there is no appetite from vendors until offers are raised.

Low transaction volumes inevitably translate into low stamp duty receipts, an increasingly important revenue source as the tax has risen steadily in recent years. Calls for a stamp duty relief to reignite the housing market seem likely to fall on deaf ears. The 3% additional Stamp Duty surcharge on additional properties, introduced in 2016, had raised £6.6 billion by the end of 2019 according to HMRC figures, against a target of £2.9 billion set by the then Chancellor George Osborne for the end of the tax year 2019-2020. In April, Stamp Duty revenue fell 40% across the UK as the number of property sales halved during lockdown.

TABLE 2
PRICES & PRICE CHANGES FOR 1,2 & 3 BEDROOM APARTMENTS IN THE RESALE MARKET AT H1 2020

		2019 £	H1 2020 £	£ per sq ft	Change % 2019 - H1 2020	Change % from 2015
Midtown	**1 Bed**	550,000	550,000	1,100	0%	-15%
	2 Bed	850,000	850,000	1,133	0%	-15%
	3 Bed	1,650,000	1,700,000	1,133	3%	-38%
City	**1 Bed**	560,000	560,000	1,120	0%	-11%
	2 Bed	765,000	785,000	1,047	3%	-9%
	3 Bed	1,400,000	1,500,000	1,000	7%	-26%
East London	**1 Bed**	390,000	390,000	780	0%	-13%
	2 Bed	525,000	525,000	700	0%	-16%
	3 Bed	900,000	900,000	600	0%	-28%

Source: Hurford Salvi Carr *1 Bed is 500 sq ft, 2 Bed is 750 sq ft with 2 Baths, 3 Bed is 1,500 sq ft*

Stamp duty has cast a shadow over prime markets for several years and the levy on additional homes was particularly problematic in our areas where so many properties are second homes or where people may be left temporarily with a second home while they combine resources to buy together. The government recognised that these 'accidental' second home owners could be caught out by the hiatus in the market during lockdown and so they announced in June that there would be an extension to the three-year window to sell a previous home in order to claim a refund of the 3% stamp duty surcharge. The three-year rule was intended to protect accidental second home owners while ensuring that owners of investment or holiday homes paid additional stamp duty.

SHOREDITCH N1 - 2 BEDROOM APARTMENT, SOLD JUNE 2020 £750,000

TABLE 3
LONG RUN PRICE CHANGES FOR A 1 BEDROOM APARTMENT IN THE RESALE MARKET

Submarket	1994 - H1 2020	2000 - H1 2020	2007 - H1 2020	2008 - H1 2020
Midtown	458%	112%	28%	40%
City	512%	146%	52%	67%
East London	458%	114%	23%	42%

Source: Hurford Salvi Carr

THE BUILDING SAFETY FUND AND FIRE PREVENTION

The issue of unsafe cladding on tall buildings has been a growing concern since the terrible risks were exposed by the fire at Grenfell Tower in 2017. Soon after the fire, new fire safety guidance was introduced for residential buildings taller than 60ft / 18m – typically six storeys. In January 2020 the guidance was extended to buildings of all heights and now applies to all apartment blocks with any type of cladding.

The government initially allocated £600 million for the removal of ACM cladding (Aluminium Composite Material) of the type used on Grenfell Tower, divided between £400 million for the social sector, and £200 million for the private sector. Subsequent investigations revealed that ACM was not the only unsafe material or building cladding system and the problem went far wider.

In March 2020, only one private sector building had applied for funds. Many leaseholders had been unable to sell their homes because mortgage companies are not willing to lend against buildings that cannot prove they have no combustible materials on or between their walls. Many sales fell through or were put on hold with no end date.

In the March 2020 budget, the Chancellor set aside an additional £1 billion for the express purpose of: 'stripping combustible cladding from homes in private ownership in buildings taller than 18 metres'. The Building Safety Fund is intended to help leaseholders who are responsible for the costs of the remediation works.

However, critics have pointed out that the fund will not go far enough. It does not cover the interim costs of buildings' insurance and walking fire patrols that are essential until the work has been completed and which costs will be recouped from residents via the service charge. It does not cover other safety defects that represent a fire risk such as flammable insulation. It also excludes the many buildings under 18 metres in height which have the same issue. A parliamentary inquiry has warned that the £1 billion fund will cover only a third of the 1,700 most dangerous high-rise blocks, and that there may be almost 10,000 other blocks with problems. Lobbying group 'the UK Cladding Action Group', have surveyed residents and gathered many stories of resulting hardship.

Estimates of the number of properties affected vary, According to the Association of Residential Managing Agents, there are up to 550,000 people, living in 1,375 buildings, which have wall systems at risk of fire. Remediation work had been started (but not completed) on 116 buildings in the period leading up to lockdown and that accounted for the homes of around 20,000 people, according to government data.

The scheme is intended to protect leaseholders from the costs of remediation but it is the building owner, freeholder or managing agent responsible for the maintenance of the building who make the application for funds to undertake the works. There is a process for leaseholders to provide feedback to the relevant government department 'if they are concerned that the owner is not taking sufficient action to remediate unsafe cladding or is passing remediation costs onto leaseholders.'

The total cost of remediation work is substantially higher than the fund. Social landlords alone have estimated that the cost to make their non-ACM fire safety measures will exceed £10 billion. The fund is not intended to relieve building owners of the responsibility.

The problem still lacks clarity and many flats seem to be unfairly refused mortgages by banks. Mortgage lenders are increasingly reluctant to lend on any property with a balcony or cladding of any type. Fire Safety Reports frequently now recommend further investigations should be carried out by specialist façade engineering consultants including intrusive exploratory work to both the external materials and also internal walls/insulation. It is only once these additional reports have been completed that freeholders and managing agents can organise the remedial work.

Since Grenfell, fire assessors and other suitably qualified professionals have been in great demand and the lead times for testing, inspections and design solutions have caused long delays. Without information from the original developer, or follow up reports, it is often not possible for a Fire Consultant to certify a building as safe or complete the new standard EWS1 form produced by the Royal Institute of Chartered Surveyors.

New Homes

CONSTRUCTION CONTINUES

When the UK went into lockdown, work on construction sites was slowed or suspended. In London it affected the delivery of almost 30,000 new homes. The GLA launched 'The Covid-19 Housing Delivery Taskforce' in April made up of leaders from London's councils, construction companies and other interested parties. Their concern is that the current crisis and expected recession will slow the delivery of new homes in the medium to long term and the purpose of the Taskforce is to look for ways to maintain the delivery of new homes. Public sector is seen as having a key role in maintaining delivery as the private sector is widely expected to reduce activity.

The construction sector is recognised as a key driver of the economy and in London it employs 330,000 people so government at all levels is keen to keep momentum. In early March, before the scale of dislocation caused by Covid had become clear, Housing Secretary, Robert Jenrick announced a consultation called 'Planning for the Future' which recommended an expansion of permitted development rights (automatic permission). One suggestion was the right to add additional storeys to existing residential blocks. The new initiatives were also intended to promote activity amongst SME builders alongside the powerful quoted housebuilders who dominate delivery.

WHITECROSS STREET EC1 - 9 APARTMENTS, SOLD H1 2020

The experience of Covid has created greater urgency and in June The Prime Mininster set up an advisory panel which includes the chair of the Building Better Building Beautiful Commission, as well as developer Stuart Lipton and the national infrastructure commissioner. Robert Jenrick announced that 'the time has come to speed up and simplify this country's over-bureaucratic planning process' claiming that the government is thinking 'boldly and creatively' about a New Deal for planning. The reforms are seen as a key element to kick-starting the economy along with infrastructure spending. Ideas under consideration include zones where buildings that comply with the rules do not require special consideration from the authorities; change of use permissions for shops to homes, and development zones similar to the development corporations that enabled Canary Wharf to be realised in the 1980s. Under the Coronavirus Act 2020 the government has made a temporary amendment to the law to allow planning meetings to be held via video link until 31st May 2021.

The Help to Buy scheme has boosted private sector housing delivery since its launch in 2013. In its first year, it funded over 22,000 new home purchases and by 2019, the annual number had risen to almost 43,000. In London, the value cap and the percentage loan are both higher than in the rest of the country to reflect the difference in house prices. Government will lend up to 40% of purchase price on new build homes in London sold for up to £600,000 and the buyer need only contribute a 5% deposit as long as they can raise the rest with a mortgage. It has created liquidity in the new build market and encouraged developers to build. The government loan is repayable after 5 years with interest rates beginning at 1.75% in year one.

The government has built up significant exposure to the housing market since the scheme launch, estimated to be £15 billion. The Chancellor had announced that the scheme would be wound down by April 2023 and that from April next year (2021) it will be restricted to first time buyers only. However, given concerns over the economy and the expected contraction in housing delivery, there are now calls to extend the scheme. Shortly before lockdown, in February, the government announced a consultation on a new scheme to help first time buyers in the new build market. The 'First Homes Scheme' would give a 30% discount on new build homes to first time buyers in the local area. Critics suggested that it would come at the expense of affordable housing currently delivered under s106 agreements. The question of the housing crisis is an enduring one and there is no doubt that it will remain a key plank of government policy.

On Sunday, 10 May, when the prime minister announced some lifting of lockdown restrictions, he urged the construction industry to return to work. Developers were quick to make plans for safe distancing on sites, although there are particular challenges in London because so many construction workers rely on the underground to travel to work. The other key challenge to restoring the rate of delivery is the supply-chain. Materials shipped in from overseas have been held up and small developers in particular have suffered from difficulties with logistics.

The London plan target is to build 42,000 new home a year. That has always looked like an ambitious target and after Covid-19, it looks less achievable than ever.

On 30th June Boris Johnson announced his economic recovery plan that includes £5 billion of spending on infrastructure projects into 2020 – £1.5 billion for hospital maintenance, £1 billion for school building, £900 million for "shovel ready" projects, £100 million for road projects – and also promised the "most radical reforms of our planning system" since the Second World War in order to build more homes.

The government confirmed a £12 billion programme to support the building of up to 180,000 affordable homes over the coming eight years. These include a 1,500-unit pilot of First Homes, which will be sold to first-time buyers at a 30 per cent discount that "will remain in perpetuity, keeping them affordable for generations of families to own". Builders will no longer need a planning application to demolish vacant shops and build homes in their place, while people will also be given "fast-track approval" for loft conversions. He also announced plans to review the use of public sector land so that it could be used for housebuilding. This will though up new opportunities for developers and provide a potential boom for builders and the construction industry.

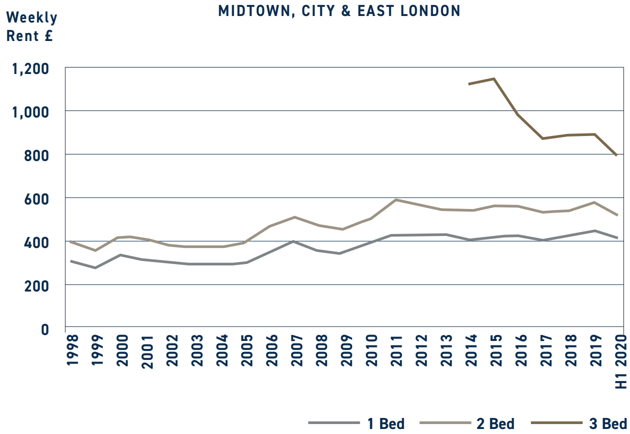
Lettings Market

SHORT LET MARKET COLLAPSES

2020 has been an extraordinary year. For anyone who announced that the decisive election victory in December 2019 had put an end to uncertainty in the UK, it soon proved that they had spoken too soon. In the rental market, the short term implications of coronavirus were dramatic and the long term remains to be seen.

Rental values dropped by around 10% in the lockdown months. The fall was fairly consistent across all property types, ranging from 9% for one bedroom apartments to 11% for 3 bedroom apartments. It has been a sharp interruption to the long term stability of our rental markets, certainly for one and two bed properties, which was still evident in the early months of the year.

FIGURE 3
WEEKLY RENTS FOR 1, 2 AND 3 BEDROOM APARTMENTS
MIDTOWN, CITY & EAST LONDON



Source: Hurford Salvi Carr *1 Bed is 500 sq ft, 2 Bed is 750 sq ft with 2 Baths, 3 Bed is 1,500 sq ft*

January and February performed very much in line with long term trends. It is, in any event, always a quiet time of year for the rental market but 'normal' ended in mid March.

Looking back, there were some threats on the horizon. The London Mayor, Sadiq Khan, announced early in March that he would be putting rent controls at the centre of his campaign for re-election, in a bid to secure tenants' votes in the London Mayoral election which was due in May. The impact of that latest swipe at landlords was never truly tested because the election was postponed when the enormity of the pandemic became clear.

As early as Janurary we began to receive cancellations from short term guests in our clients' serviced apartment blocks and, with little or no new demand to replace them, this quickly led to some of the larger short let operators applying to landlords for rent concessions. Around the same time, international students began to leave the city and head to their home countries. Many of those who had gone home for the spring break, would not return for the rest of the academic year.

Measures were introduced to protect tenants who might get into difficulties meeting their rent payments. On 26th March 2020 the Coronavirus Act came into effect obliging landlords to give tenants three months' notice of an intention to seek possession. Under this law landlords cannot apply to start the court process until after the three month notice period. From 27th March, the court service suspended all

BLOOMSBURY WC1 - VIEW FROM THE ONE BEDROOM APARTMENT, LET MAY 2020 £600 PW

ongoing housing possession action – effectively suspending a landlord's rights to evict tenants during this period. On June 5th, the ban was extended for a further two months taking it out to August 23rd.

Landlords struggling as a direct result of coronavirus, could apply to their mortgage lender for a repayment holiday.

By April, lockdown had ended all possibility of business or leisure travel, and landlords who had been using short let platforms such as Airbnb and booking.com found that their properties were laying empty and not generating income. Many approached us to reassign their properties to the longer-term 12-month AST market.

As concern grew that the spread of the coronavirus in London would follow a similar course to Italy and other European neighbours, we received a rush of requests from tenants for rent holidays, rent reductions and notices to terminate their tenancies early. This continued until early May, by which time most tenants had adapted to lockdown, were working from home and the market seemed to settle.

The average weekly rent for apartments of all sizes fell but it was the City which bore the brunt of the steepest falls. In Midtown and East London, the weekly rent for a one bedroom apartment dropped by 4% and 7% respectively, whereas rents in the City lost 16% in a very short period. Of all our markets, it is the City that depends most heavily on short term rentals, business travel and overseas visitors, including students.

The market for two bedroom apartments was hit harder in Midtown, losing 12% of the rental value – much the same as the City at 13%. East London, where rentals are significantly lower than the other two areas of our market, fared much better losing, on average 6%. The most likely explanation is that the flood of stock that returned from the corporate let sector predominantly landed in the City and Midtown, rather than East London.

Renters pay a substantial premium to live in a central location. The annual rent for a 1 bed apartment in Midtown is around £8,000 more than the equivalent space in East London, a 44% premium. The Midtown one bedroom apartment costs the tenant £3,000 more than a two bedroom in East London.

TABLE 4
WEEKLY RENTS FOR 1, 2 & 3 BEDROOM APARTMENTS IN MIDTOWN, CITY & EAST LONDON AT H1 2020

Submarket		2017 £	2018 £	2019 £	H1 2020 £	% Change 2018 - H1 2020
Midtown	1 Bed	450	475	500	480	-4
	2 Bed	600	640	680	600	-12
	3 Bed	1,100	1,100	1,100	950	-14
City	1 Bed	450	450	490	410	-16
	2 Bed	560	560	600	525	-13
	3 Bed	925	950	975	850	-13
East London	1 Bed	320	340	350	325	-7
	2 Bed	425	425	440	420	-5
	3 Bed	575	575	575	540	-6

Source: Hurford Salvi Carr *1 Bed is 500 sq ft, 2 Bed is 750 sq ft with 2 Baths, 3 Bed is 1,500 sq ft*

Renting is the option that makes true city living possible for young professionals who can choose to commit a larger proportion of their earnings to rent for a period in return for access to the attractions of the city and the short commute to the workplace. While these benefits have been lost during the extraordinary circumstances of the pandemic, as the city begins to return to normal (whatever that will be), public transport will be one of its greatest challenges and the value of a central location will actually be reinforced. We also expect safe cycle routes to become a key determinant of demand.

TABLE 5
ANNUAL RENTS FOR 1, 2 & 3 BEDROOM APARTMENTS IN MIDTOWN, CITY & EAST LONDON H1 2020

Submarket		Weekly Rent £	Sq ft	Rent p.a.	Rent psf
Midtown	1 Bed	£480	500	£24,960	£50
	2 Bed	£600	750	£31,200	£42
	3 Bed	£950	1,500	£49,400	£33
City	1 Bed	£410	500	£21,320	£43
	2 Bed	£525	750	£27,300	£36
	3 Bed	£850	1,500	£44,200	£29
East London	1 Bed	£325	500	£16,900	£34
	2 Bed	£420	750	£21,840	£29
	3 Bed	£540	1,500	£28,080	£19

Source: Hurford Salvi Carr *1 Bed is 500 sq ft, 2 Bed is 750 sq ft with 2 Baths, 3 Bed is 1,500 sq ft*

It may be that the resilience of the rental market had not yet been fully tested by the end of June. In London the peak of activity for rental is always in Q3 when students start the new academic year and graduates normally start their first jobs. That sets a pattern for future lease anniversaries and a recurring peak in leases expiring. By Q3, there is a reasonable chance of some normality having returned to the market but we also expect a significant drop in overseas student numbers for the 2020/21 academic year and a decline in graduate recruitment. It seems likely that changes to lifestyles and working patterns, as well as the economic consequences of Covid-19, will have an impact on demand and pricing in the remainder 2020 and into 2021.

Most London renters are young. 51% of tenants are aged between 20 and 29, which is the demographic most likely to have retreated to a family home outside the city during Covid-19. If debts do mount in the rental sector then we would expect that the Bank of Mum and Dad will be the lender of choice for tenants under 30. However, with opportunities to spend their earnings in retail, restaurants and bars severely curtailed, the market is to some extent protected by the very conditions that could be a threat.

One unexpected by-product of lockdown was that it accelerated the widespread adoption of some new technologies. During the weeks from March 23rd to May 13th, both tenants and landlords embraced the use of video technology and virtual tours became commonplace. They proved to be an acceptable substitute for a physical viewing and, perhaps more surprisingly, were also widely accepted as enough on which to sign a rental agreement. A 'new normal' emerged and became mainstream across central London. Virtual tours work best when the property is vacant at the point of marketing, as is the case for the majority of our stock, but alternatively, outgoing tenants have taken the videos.

By June, the government was looking for ways to restart the domestic tourism market and set a target for the private holiday sector to reopen by July 4, with self-let properties like Airbnb likely to be among the first to be available. In London however, much of the influx of supply from the short term rental market is likely to stay in the conventional market for the rest of the year and beyond. Properties let on a 12 month lease, will not return to the short term market until mid 2021 at the earliest. On the other hand, the flow of new stock from development completions has been slowing for some time.

CITY EC2 - TWO BEDROOM APARTMENT, LET FEBRUARY 2020 £1,250 PW

It is always interesting to look at the long term changes in rental values in our markets. Rents are far more stable than the media would suggest. Over 20 years, the average rent for a 1 or 2 bed apartment in our markets, has risen by an average of 1.25% per annum, over shorter time periods, the average often hovers at between 0.3% and 1% per annum, depending on the period examined.

TABLE 6
LONG TERM RENTAL GROWTH

	2000 - H1 2020	2007 - H1 2020	2008 - H1 2020	2014 - H1 2020
1 Bed	25%	5%	16%	0%
2 Bed	26%	2%	12%	-5%
3 Bed	N/A	N/A	N/A	-30%
Inflation (CPI)				

Source: Hurford Salvi Carr *1 Bed is 500 sq ft, 2 Bed is 750 sq ft with 2 Baths, 3 Bed is 1,500 sq ft*

AIRBNB AND THE SHORT TERM RENTAL MARKET

Shortly before lockdown, the GLA published a report on short term and holiday rentals in London. The report was prompted by a concern that this type of short term letting had become so popular that it was sucking supply out from the mainstream rental market and exacerbating London's housing crisis.

Ironically, as the demand from travellers plummeted during lockdown, short term stock found its way back in to the mainstream rental market and, far from exacerbating shortage, it threatened to cause an oversupply.

Short term lettings are now an established feature of the rental market and play an important role by offering an alternative to hotel rooms and a source of additional income for households. There is a cap on the number of nights that a property can be used for short term rental of 90 days per annum which means it is not a commercially viable alternative to long term rental for investors but can be a valuable mechanism to plug voids, boost revenue and shift lease anniversaries. The GLA report calculated that, on average, a property would need to be let for 190 nights per annum for the income to outweigh a standard open market tenancy.

The average price per night ranged widely across London but in our areas, the average price per night was £128 in Camden, £108 in Islington and £90 in Hackney and Tower Hamlets. If any of those rates was translated into weekly rents it would dwarf normal rental income and that is one reason why the market is regulated, to minimise loss of private rental stock. The other key concern is that it would have a detrimental impact on community.

There are around 450 businesses in London with a portfolio of properties available for short term rental operating on Airbnb and other platforms with a similar operating model.

The GLA report found that the number of Airbnb listings in London had increased four-fold in four years and had grown in all boroughs.

There were 80,770 properties listed on Airbnb in in May 2019, of which 48,100 were 'active' and 45,000 were entire homes with the balance being rooms within a property. Of the active listings, 79% were in Inner London. That number had quadrupled since 2015. While Inner London accounted for the majority of listings, the number in Outer London grew much faster between 2015 and 2019. Unsurprisingly, Westminster topped the ranking by total number of properties listed with over 9,000, but Camden, Islington, Hackney and Kensington & Chelsea all had around 5,000 or more and Tower Hamlets had more than 7,700. Of those, around half were active in May 2019.

Most hosts have just one property listed but there were 280 who had more than 10 properties listed. The report assumes that these multiple listers were probably management companies acting as hosts and supervising guests.

In London, short term rentals are restricted to 90 nights a year but the report estimates that almost a quarter of properties exceeded that level and with multiple platforms available, it is difficult to monitor compliance.

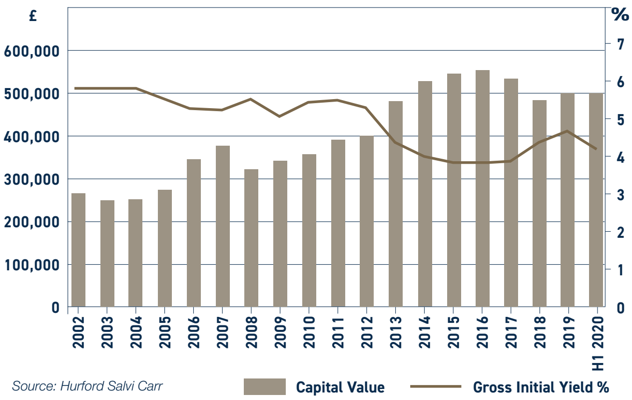
The Government has made it clear that it has no plans to ban the use of residential properties for short-term letting. It considers that further legislation would be overly bureaucratic and could act as a barrier to households letting out their properties on a short-term basis. Instead, the Government prefers a non-regulatory approach by encouraging the Short Term Accommodation Association to improve standards and promote best practice in the industry.

INVESTMENT MARKET

Just as supply constraints can protect investment values, the addition of new stock to the rental market can pose a threat to rental growth and therefore yields. In our markets, yields have been rising since 2017 as rents continued to rise even as capital values did not. That balance has reversed in 2020 because capital values rose while rents have fallen.

Gross returns for rented properties in midtown, City and East London fell back to 4.2% before costs for a typical one bedroom apartment, 3.5% for a two bedroom 2 bathroom apartment and 2.97% for a three bedroom penthouse. This returned yields to where they had been in early 2014.

FIGURE 4
CAPITAL VALUES AND YIELDS FOR ONE BEDROOM APARTMENTS
MIDTOWN, CITY & EAST LONDON



Source: Hurford Salvi Carr

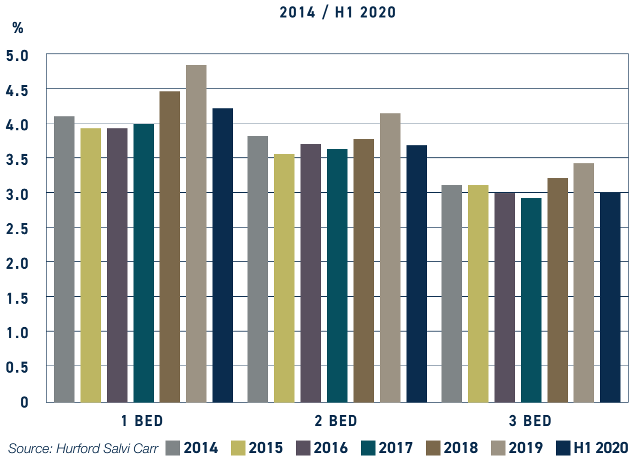
Returns remain substantially higher than interest rates and outperform the returns on many other investment options despite the changes to taxation and tax reliefs. At times of uncertainty bricks and mortar has always been seen as a safe haven. In this period, the intrinsic value of property has been particularly heightened by the focus on the home as a safe place.

It is also the case that the foundations are more secure than in previous recessions. When the Global Financial Crisis hit the housing market, prices had been rising strongly and

CITY EC1 - TWO BEDROOM APARTMENT, LET JUNE 2020 £700 PW

affordability was stretched. This current crisis has struck after a period of slow or negative price growth and at a time when affordability had been rebalanced to some extent. It means that sellers had already begun to adjust to new expectations and buyers are less likely to fear buying in a falling market.

FIGURE 5
CHANGE IN YIELDS FOR CITY, MIDTOWN & EAST LONDON
2014 / H1 2020



Source: Hurford Salvi Carr

TABLE 7
GROSS INVESTMENT RETURNS FOR ONE BEDROOM APARTMENTS
AVERAGE OF MIDTOWN, CITY AND EAST LONDON 2012 TO H1 2020

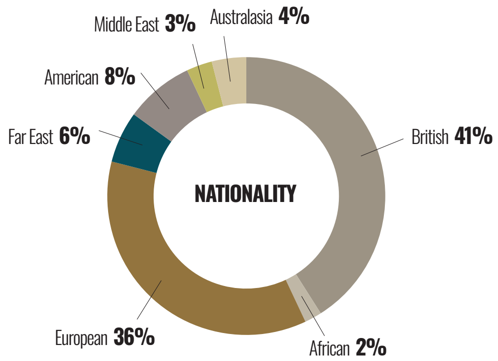
	2013	2014	2015	2016	2017	2018	2019	H1 2020
Gross Annual Income £	21,840	21,060	21,580	21,840	21,060	21,840	23,140	21,060
Capital Value £	486,000	520,000	550,000	555,000	530,000	485,000	500,000	500,000
Gross Initial Yield %	4.5	4.1	3.9	3.9	3.97	4.50	4.6	4.21

Source: Hurford Salvi Carr

Gross Yields - Gross to Net is typically depleted by 2.5%

Nationality

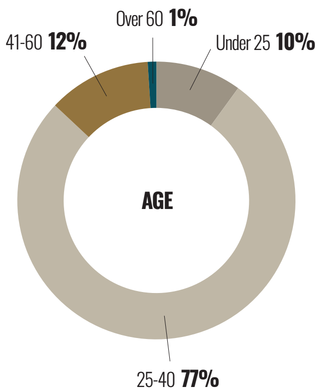
The number of new lettings was low compared to previous years but, unlike in the sales markets, we processed hundreds of transactions before, during and after lockdown. In the rental market there is a distinct difference between the profile of tenants in the two halves of the year. This is explained by the influx of students over the summer in time for the autumn term. It also means that these figures will not pick up the true extent of the impact on overseas student numbers in London until Half 2.



The nationality breakdown is similar to H1 2019 with a slight increase in the proportion of British renters and a fall in the proportion of EU renters from 46% in the same period last year to 36% in this latest set of data. All other nationalities are broadly similar in their contribution to the whole tenant pool.

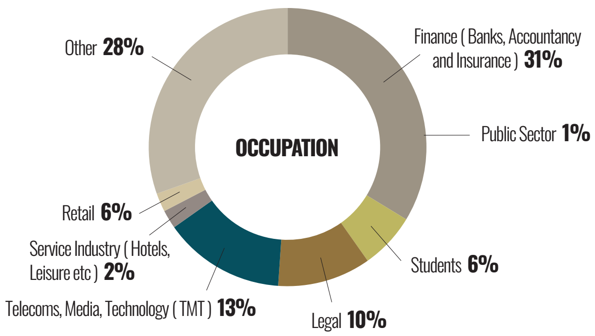
Age

The age distribution is unremarkable since it is little changed from the same period a year ago. We make the point in the text (page 11) that London renters are predominantly young and this breakdown confirms that with 87% under 40.



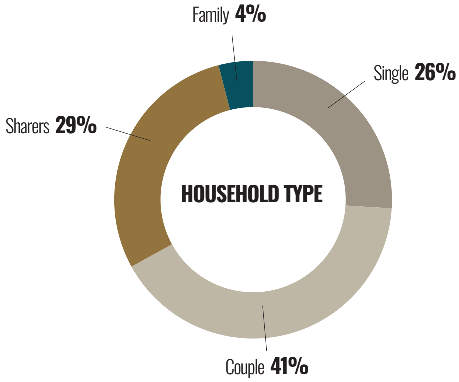
Occupation

Over the years that we have collected this data, the financial sector has consistently dominated the figures for tenants. This time 31% of all tenants were working in the sector and TMT has become a little more significant, accounting for 13% of the total. People working in retail and hospitality made up 11% in the same period last year and that has dropped to 6% in H1 2020. It will be interesting to see how this chart looks at the end of the year.



Household Type

The breakdown of household type is almost identical to the same period of 2019. This shifts for the whole year because of the importance of sharers to the student rental market which will impact the figures in Half 2.



Future Prospects

A NEW NORMAL

The London housing market, like much else, has been dealt a sideways blow in 2020, by the Covid-19 pandemic. Few can claim to have seen it coming. The scale of this dislocation could encourage people to reach for the security of home-ownership, or to crave the freedom of the rental market. In June 2020, it remains too soon to predict the outcome with any degree of certainty but we try here to sketch out some possible futures.

First, some reassurance. While clearly not immune to economic fallout, the London housing market in a much better place to withstand a recession than it was at the time of the Global Financial Crisis in 2008. The key difference today is that house price growth has been flat or negative in the period leading up to this crisis and the ratio between prices and earnings had been rebalanced.

Owners have been hardened by the long 5 year recession in central London property and, with prices already back to 2014 levels, there will be little motivation to sell in 2020. We do not expect any distressed or forced sellers as long as interest rates remain so low and because bank lending rules have been so tight since 2009. Based on our experience, owners will simply postpone plans to sell.

No one yet knows what the new normal will look like but some immediate changes are easier to predict. Safe viewing protocols are likely to persist for many months and some aspects will become permanent changes. It will be a long time before people feel entirely comfortable with strangers browsing through their homes.

Supply will be a significant constraint on sales activity in our markets. There are two major issues. The first is the lack of appetite from owners as prices stagnate for yet another year. The second is the backlog of investigative survey reports and structural repairs into apartment blocks that have become essential in the wake of the Grenfell Fire. Many properties cannot be brought to market, even if the owner wishes it.

There will be some compromise on the part of sellers but, in general, we foresee a return to the stand-off between cautious buyers and confident sellers, much as we experienced during the protracted Brexit negotiations.

COVID-19 will inevitably leave a lasting impact on the UK economy. It is not yet clear how deep that impact will be on the wider UK housing market but in the first weeks post-lockdown, agents across the country reported high levels of activity, some driven by a need for better home-working conditions.

The impact on corporate profits, employment, salaries and future investment decisions will be more marked in the Autumn once the furlough scheme has ended. Many agents expect the market to slow down at that point, especially as the next Brexit deadline looms.

To access the mortgage market in the next 6-12 months buyers will probably need larger cash deposits as lending criteria become more stringent. With price rises now off the agenda, our long held view that we will experience an unprecedented decade of no growth in property values across central London to 2023 is now looking increasingly valid. Indeed, our prediction may turn out to be an underestimate and stable prices could stretch out for 12 or even 15 years. Under those conditions, property will increasingly be viewed as a long term home rather than an appreciating asset.

The corollary to that is the huge increase in government debt could create inflationary pressures and if earnings rise with inflation, then house prices generally rise in parallel, especially if interest rates remain relatively low.

While the city rebuilds, and as long as public transport is seen as a barrier, we expect the popularity of cycling and walking to continue. Covid-19 could be the tipping point for the city to become a cycle-friendly city. That is certainly an ambition for City Hall. Apartments within a relatively easy cycle route of central London offices will have added appeal for buyers and renters. It could re-ignite the market for pied a terre properties.

In June, the Chancellor reiterated his commitment to infrastructure spending and supporting growth of new sectors such as green energy, although now the main policy driver is to kick-start the economy rather than level out the regions.

There have been calls for a stamp duty holiday to support a recovery in the housing market. Initial indications suggest that there is no need for a demand boost and the government will be reluctant to forego tax revenue in 2020. The argument rests on the secondary benefits for the wider economy as home moves prompt many other spending decisions.

As we write this report at the end of June we have no way of knowing how successful the measures to restart the economy will be or indeed if there is a chance that the virus returns in the autumn despite more widespread testing efforts and contact tracing. Lessons have been learnt and advances made but it could be early 2021 before the virus is fully under control. Many London office-based businesses are planning for only phased or partial returns in 2020.

Rental market pricing responds quickly to fluctuations in supply and demand. Most landlords will accept a reduced rent if it means avoiding a period of vacancy, in the knowledge that the rent level can be restored within 12 months if the market recovers.

Given that much of the short term rental stock was put back into the mainstream market, it is possible that some landlords will be tempted to plug that gap when it re-emerges and offer empty properties on platforms like Airbnb. There are already early moves to re-open for tourism and it is easier to social distance in properties without hosts than in many hospitality businesses.

For the rental market much hinges on demand from students and, in our markets, particularly from affluent overseas students. There are over 100,000 overseas students in London in a typical year – around 30% of the total in higher education. Student demand for rental property tends to peak in the summer and early autumn but it is likely to be delayed this summer as prospective students defer decisions about whether to come to London.

If the purpose built student housing providers have vacant rooms, it could impact on the wider private rental sector as they compete for tenants.

By October much should be clearer. The furlough scheme will end, all being well, travel for pleasure will have resumed and retail and leisure destinations will be welcoming visitors while continuing to observe social distancing.

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