



Output is likely to drop again in the last quarter of the year

UK Economy and Property Market Chart Book

Q4 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 Survey Release Dates			
Frequency	Survey	Period covering	Release date
Monthly	RICS Hong Kong Residential Market Survey	October	18-Nov-20
Monthly	RICS Portuguese Housing Market Survey	October	27-Nov-20
Quarterly	RICS UK Facilities Management Survey	November	03-Dec-20
Monthly	RICS UK Residential Market Survey	November	10-Dec-20
Monthly	RICS Hong Kong Residential Market Survey	November	17-Dec-20
Monthly	RICS Portuguese Housing Market Survey	November	24-Dec-20
Monthly	RICS UK Residential Market Survey	December	21-Jan-21
Monthly	RICS Hong Kong Residential Market Survey	December	21-Jan-21
Quarterly	RICS UK Commercial Property Monitor	Q4 2020	28-Jan-21
Quarterly	RICS Global Commercial Property Monitor	Q4 2020	28-Jan-21
Quarterly	RICS UK Construction Monitor	Q4 2020	04-Feb-21
Quarterly	RICS Global Construction Monitor	Q4 2020	04-Feb-21

Economic Outlook

Following a pick-up in Q3, GDP is likely to drop again in Q4

Output across the UK economy recovered by 15.5% in Q3 according to the latest estimates from the Office for National Statistics. Despite this being a record quarterly increase in GDP, aided by an easing of lockdown measures over the summer, it still leaves the total level of output 8.2% below where it stood prior to the pandemic back in February. Moreover, with England entering a second lockdown at the start of November, the economy will undoubtedly suffer a further setback on its road to recovery this month. That being said, current restrictions are not quite as stringent as those imposed back in March (schools will remain open for instance), meaning the contraction in economic activity this time round is expected to be much smaller than that seen during Q2.

To soften the blow, the Bank has launched further stimulus

Policy support has been bolstered in a bid to contain some of the economic fallout arising from the new four-week lockdown. On the monetary policy side, the MPC voted to raise the level of quantitative easing by another £150bn, with these extra asset purchases beginning in January and set to run until the end of next year. This announcement was accompanied by a downgrading of the MPC's forecasts for economic growth.

Indeed, the committee now sees the economy shrinking by 11% during 2020 as a whole (weaker than their previous projection of -9.5%). Meanwhile, the recovery next year is also envisaged to be slightly weaker than earlier expectations, with forecasts for GDP growth being revised down from 9% to just over 7%. Given the ultra-loose monetary policy stance already in place, coupled with the MPC's reservations over the potential effectiveness of negative interest rates, fiscal policy will be all the more critical in supporting the UK's recovery from here.

While fiscal support has also risen

On that front, Chancellor Rishi Sunak announced the furlough scheme has been extended until March 2021. In addition, the requirement that firms must be temporarily closed due to government restrictions to access the scheme was relaxed, although businesses will still need to pay national insurance and pension contributions of any furloughed workers. Alongside this, the self-employed income support grant was raised from 55% to 80% of average profits, while the Chancellor also announced an increase in the upfront guarantee of funding for the devolved administrations (from £14 to £16 billion).

Still, unemployment is likely to

rise further

As it stands, labour market data shows unemployment has already risen from a low of 3.8% pre-crisis to 4.8%, with a record 314,000 redundancies reported in July to September alone. Going forward, although the extension of the furlough scheme will help to protect some jobs, forecasts from Oxford Economics still point to the rate of unemployment peaking at just over 7% by the mid-point of 2021. If this comes to fruition, it would mean that more than 1 million jobs will have been lost across the UK throughout the pandemic.

As far as Brexit is concerned, the coming weeks could be critical in defining the UK and EU's trading relationship next year. Striking a free-trade agreement still looks possible although the window is short. On the other hand, failure to reach agreement will most likely lead to a short term hit to GDP next year.

Recovery in the housing market will run out of steam further ahead

Activity across the UK housing market remain firm which appears to be at-odds with the subdued economic picture. Housing transactions have continued to rebound while mortgage approvals in September reached their highest level in thirteen years. However feedback to the RICS UK Residential Market Survey suggests that this trend is unlikely to be sustained further ahead. Average twelve-

month sales expectations point to momentum slowing with the difficult economic backdrop expected to weigh on activity next year as the Stamp Duty holiday comes to end.

Meanwhile, the Q3 results for the RICS UK Commercial Property Market Survey suggest that the office and retail segments of the market are continuing to struggle against the challenges posed by the ongoing pandemic while activity across the industrial sector seems to be relatively more resilient. Over the course of the next twelve months, rents are envisaged to decline sharply in both the retail and office sectors. In contrast, contributors envisage industrial rental values rising by around 1.5% in the coming year.

Government policies are likely to support activity in the construction sector

Turning to the construction sector, the government's commitment to increase infrastructure spending is likely to help support activity across the industry in the coming years. A net balance of +35% of respondents to the RICS Q3 2020 survey anticipate workloads rising in the infrastructure sector over the course of the next twelve months. Output is also seen rising across the private housing sector supported by new permitted residential development rights and reforms to England's planning system.

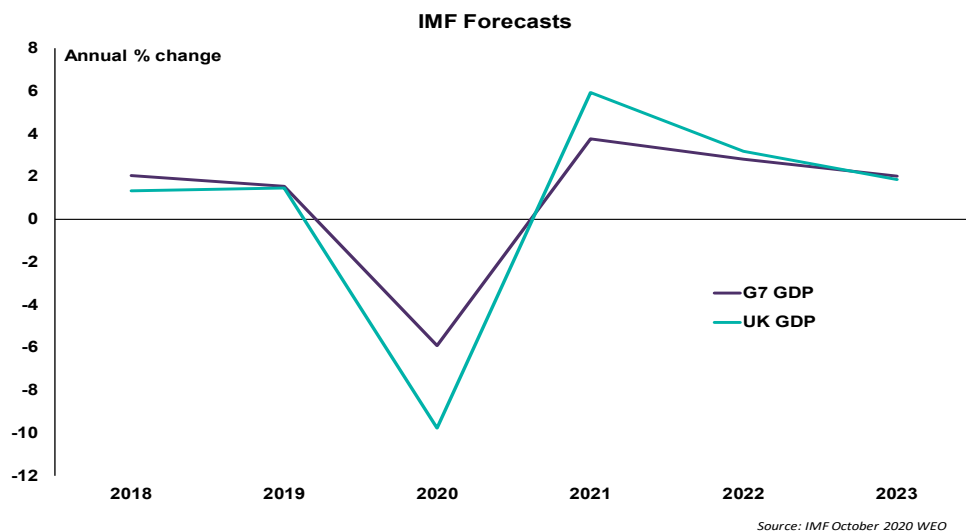
UK Economy

Estimates by ONS suggest that quarter-on-quarter GDP rose by around 15.5% in Q3 2020 following a decline of around 19.8% in Q2. It seems that just over half of the loss in output in the first two quarters of 2020 has been recovered. However, with England entering a second lockdown in November, GDP looks set to drop again in Q4. According to projections by Oxford Economics, UK output is unlikely to be back to where it was before the crisis hit until the end of 2022 (Chart 1).

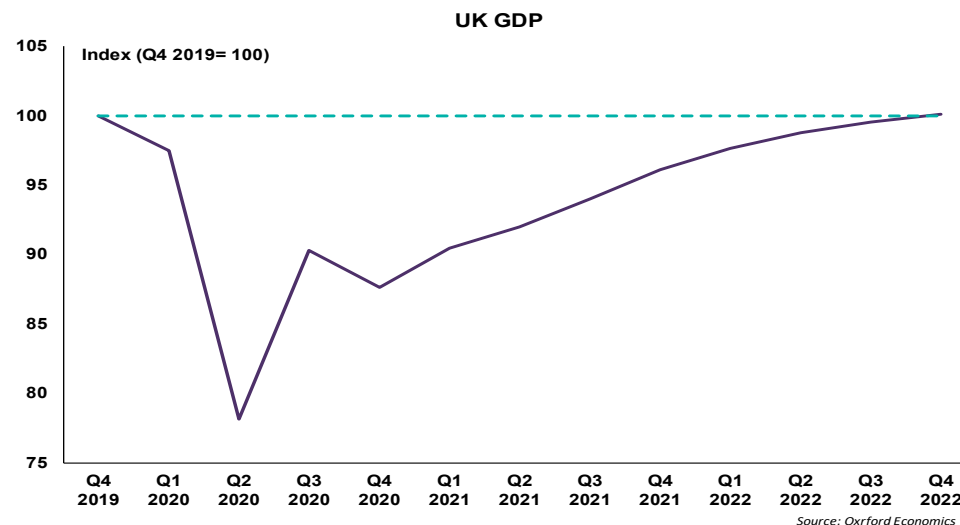
Meanwhile, forecasts compiled by the IMF imply that UK output could slip by almost 10% in 2020 on an annual basis, well below the average of all G7 economies (Chart 2). A significant pick-up in activity is envisaged in 2021, albeit a failure to reach a free trade agreement with the EU and a rise in unemployment could inhibit the recovery.

Chart 3 shows that the global trade picture has begun to improve somewhat in Q3. In spite of this, IMF forecasts imply that trade volumes are likely to come in around 10% lower in 2020 than in 2019. Trade is expected to recover firmly in 2021 which should support a reasonably favourable backdrop for UK exporters providing a no-deal Brexit is avoided.

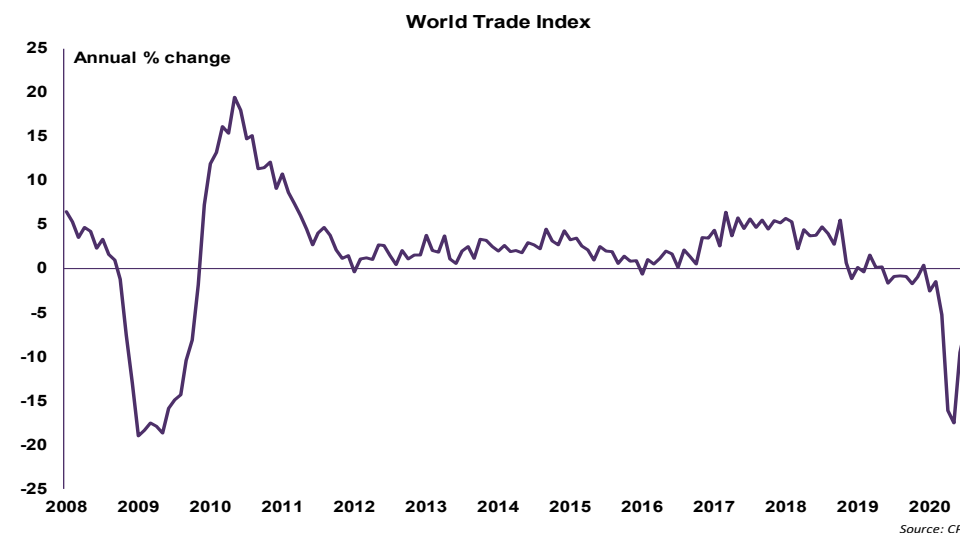
2. UK output could slip by almost 10% in 2020



1. Output is likely to drop again in Q4 2020



3. Trade volumes have begun to recover



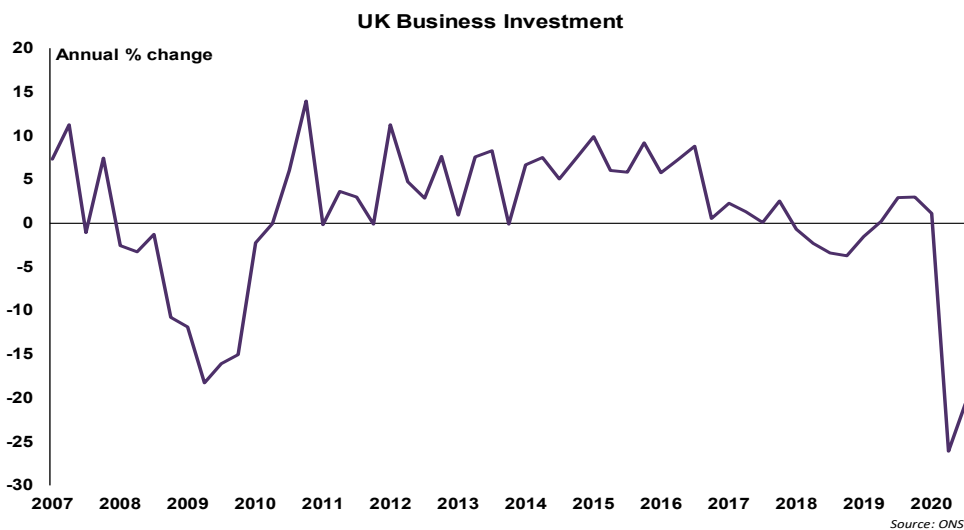
UK Economy

UK redundancies reached 314,000 between July and September, the highest since records began in 1995 (Chart 4). Alongside this, the unemployment rate edged up to a four-year high of 4.8% in Q3 from 4.1% in Q2. Although, the extension of the furlough scheme will help to support some jobs, it is unlikely to prevent unemployment from rising further in the coming months. Oxford Economics forecasts suggest that the unemployment rate could rise to around 6.3% by the end of the year and peak at around 7% in 2021.

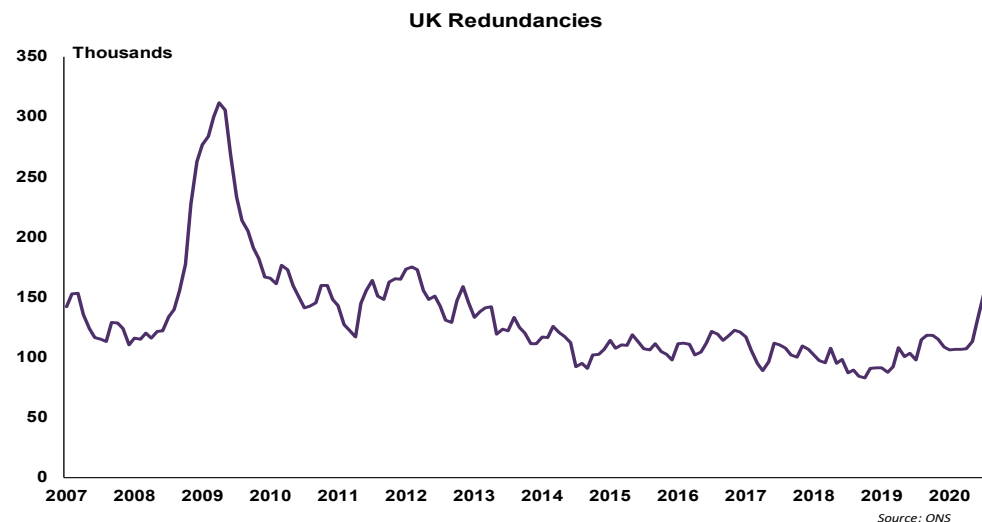
Meanwhile, ONS estimates show that business investment fell by more than 26% on a year-on-year basis in Q2 while Q3 data points to only a modest recovery (Chart 5). Looking ahead, it seems that investment will remain subdued in the near term with new Covid restrictions and lingering uncertainty over the UK's future trading relationship with the EU weighing on investment plans.

Indeed, the results to the latest Deloitte survey suggest that sentiment among the UK's largest firms remains downbeat. Around 80% of CFO's in Q2 and in Q3 report that their businesses are facing high levels of uncertainty (Chart 6). Moreover, around 86% believe that it is not a good time to take greater risk onto balance sheets.

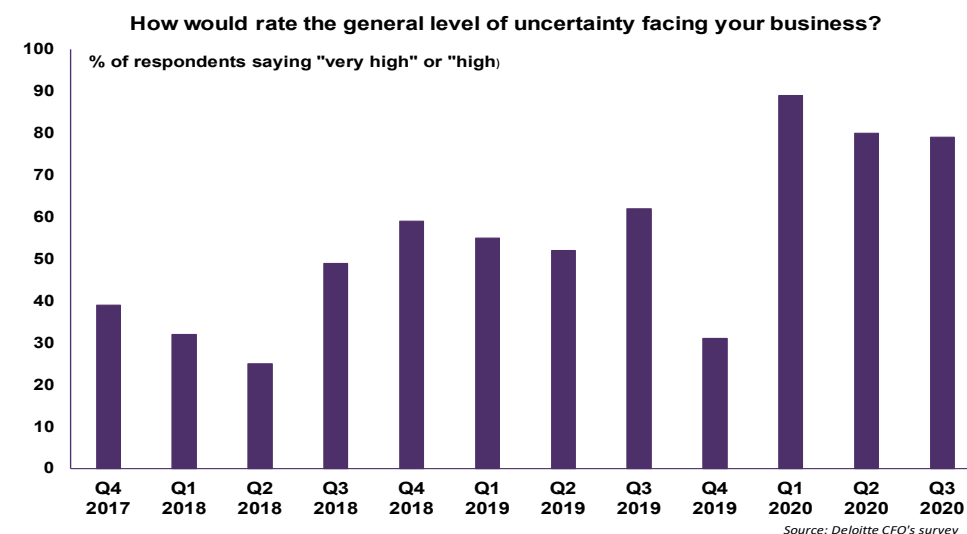
5. Business investment remains subdued



4. Redundancies have risen sharply



6. Firms are facing high levels of uncertainty



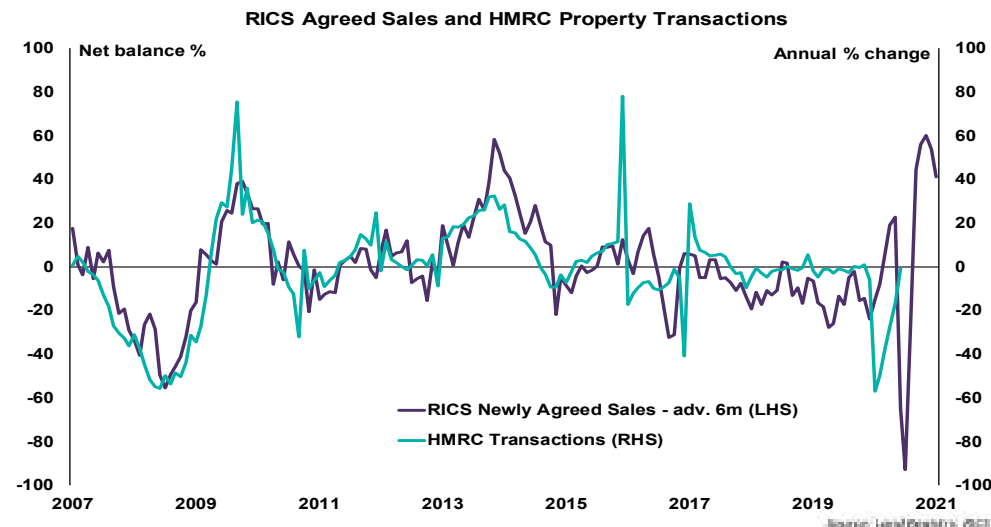
Housing Market

In spite of the subdued economic backdrop, activity in the housing market remains robust. The latest data from HMRC shows that transactions edged just above 98,000 in September, more than double than the number recorded in April and May. Furthermore, the RICS Newly Agreed Sales net balance is firmly positive, suggesting that transactions are likely to continue rising in the coming months (Chart 7).

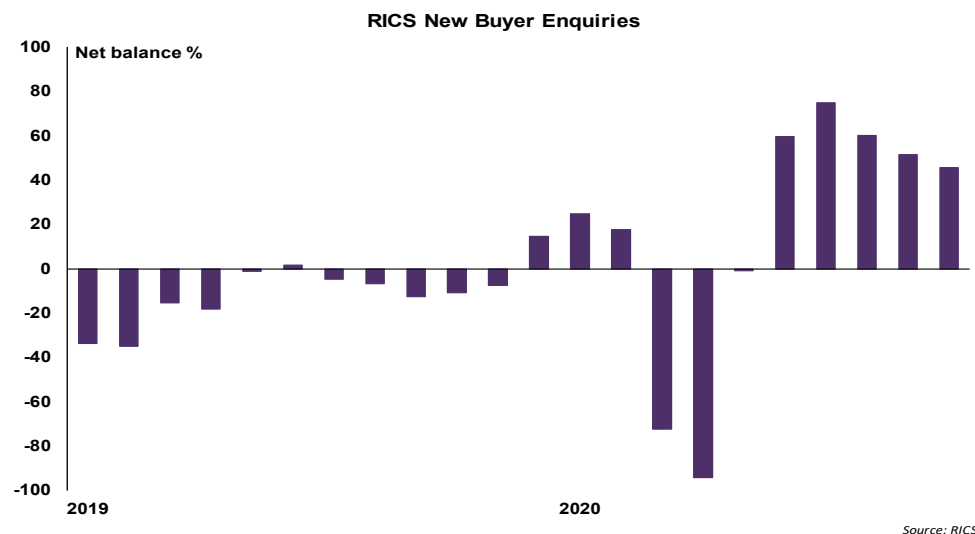
Strong buyer demand appears to be the main driving force behind the pick-up in the sales numbers. In the RICS survey, New Buyer Enquiries have risen firmly for five consecutive months supported by the temporary reduction in stamp duty (Chart 8).

It seems that the surge in demand has led to an increase in mortgage interest rates as lenders are trying to deter buyers due to a lack of capacity to progress mortgage applications. The latest data from the Bank of England shows that rates have risen particularly on high-risk home loans. The average interest rate on a 2-year fixed rate 95% loan to value mortgage has risen sharply to above 4%, meanwhile in the 90% loan to value category, the rate has jumped to around 3.55%, a five-year high (Chart 9).

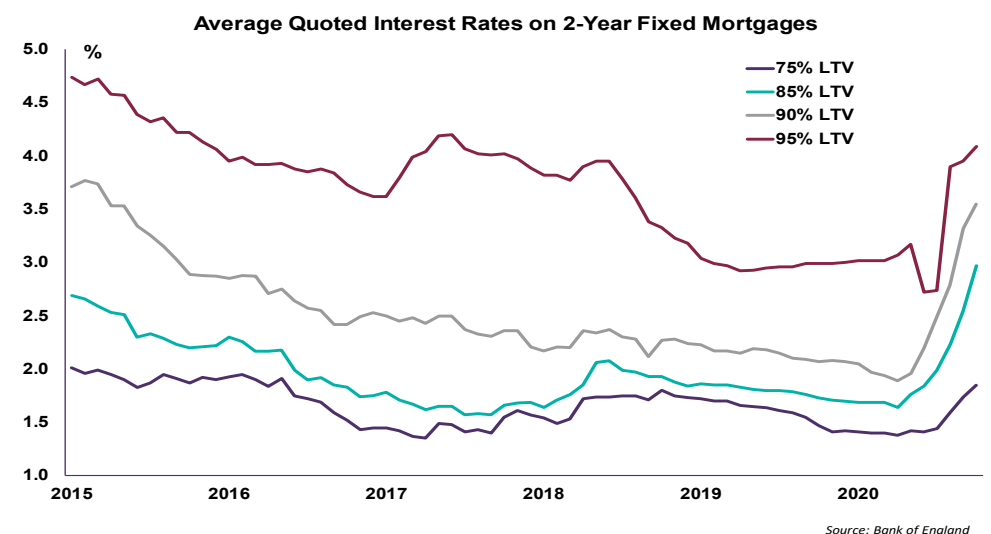
7. Housing transactions look set to rise further



8. Buyer demand has risen sharply..



9. ..leading to an increase in mortgage interest rates



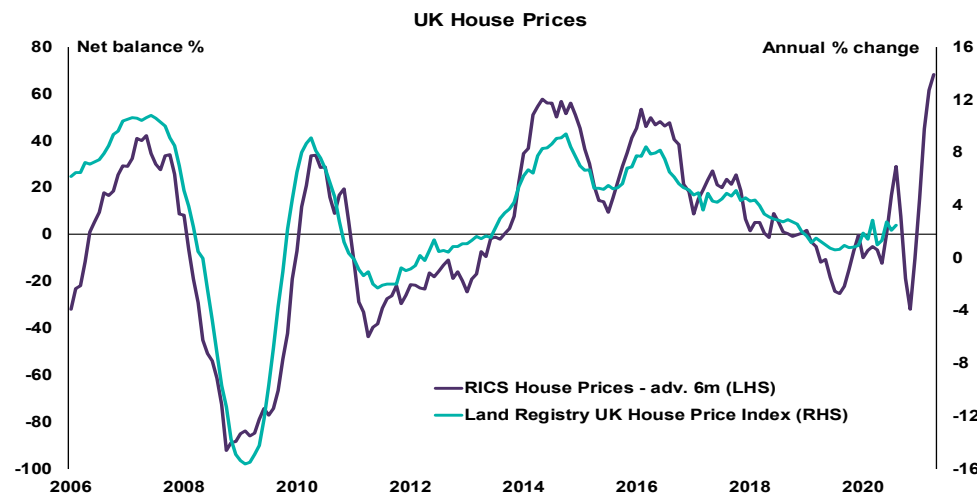
Housing Market

As far as house prices are concerned, the RICS headline House Price balance has risen firmly for four successive reports supported by an uplift in both buyer enquiries and new instructions. In October, a net balance of +68% of contributors noted an increase in house prices at the national level. This suggests that national house prices inflation is likely to rise further over the coming months (Chart 10).

In turn, affordability is likely to remain stretched in many parts of the country at least in the near term. Chart 11 shows that the national house price to earnings ratio remains at around 5%, very close to the high water mark of 5.4% in 2007.

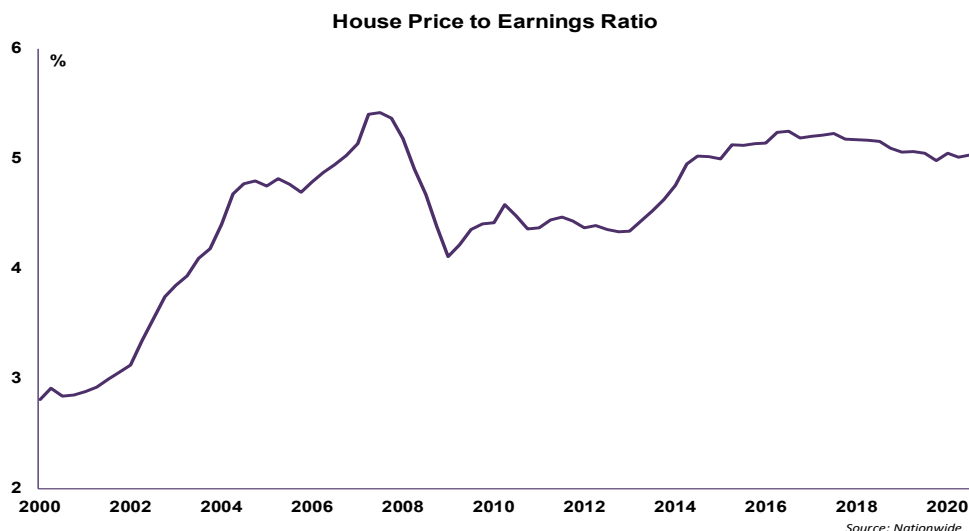
It seems improbable that the solid trend in prices and market activity will be sustained further ahead. A broadly flat trend in house prices is expected to emerge over the course of the next twelve months (Chart 12). Furthermore, average twelve months sales expectations are entrenched in negative territory as demand is looking likely to fade once the Stamp Duty holiday comes to an end.

10. House prices are likely to rise further in the coming months



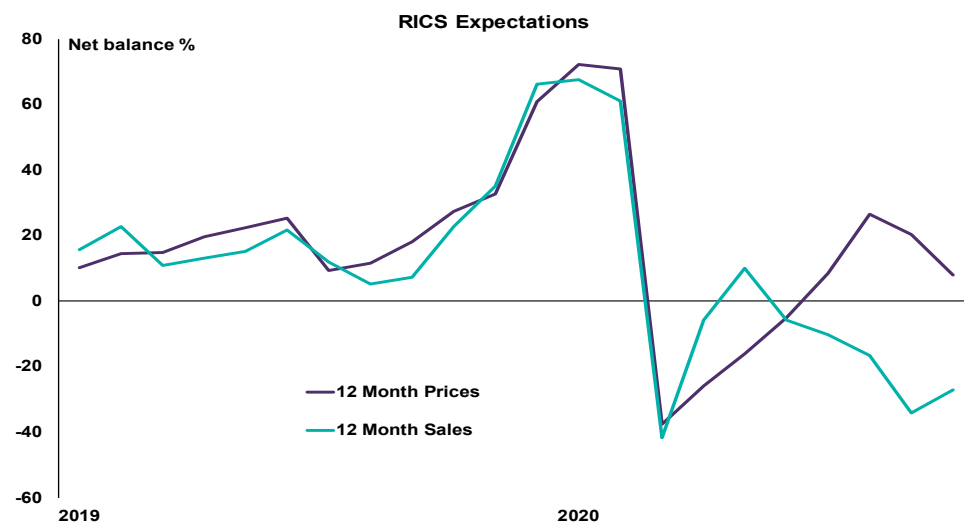
Source: RICS

11. Affordability is already a key issue for the market



Source: Nationwide

12. The recovery will run out of steam next year



Source: RICS

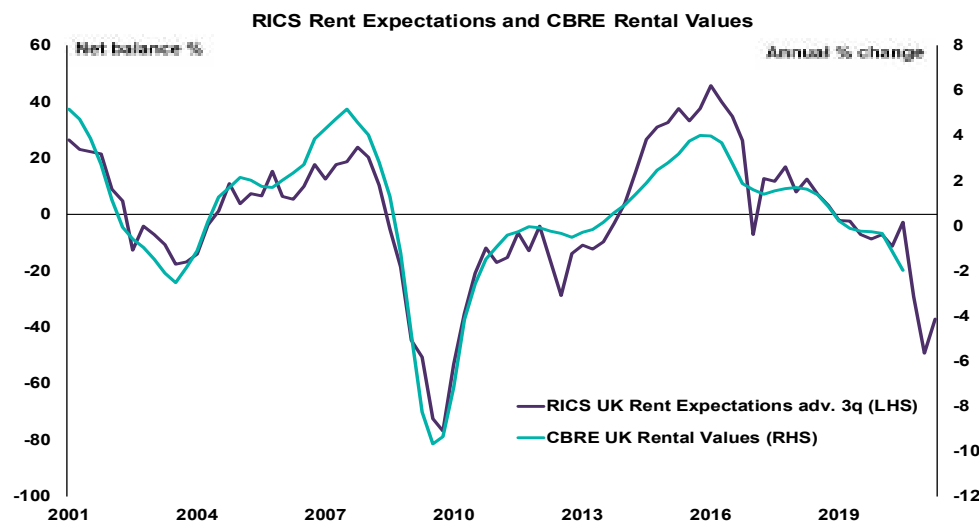
Commercial Property Sector

The picture across the commercial property market is still pretty much subdued. In the Q3 2020 RICS UK Commercial Property Market Survey, headline rent expectations net balance registered a reading of -37% suggesting that all-sector rental values could slip by as much as 6% on year-on-year basis in the coming quarters (Chart 13). That said, this is mainly a result of a sharp decline in rental values envisaged for the retail and office sectors. In contrast, industrial rents are seen rising over the coming months.

Government restrictions are likely to put further pressure on the retail portion of the commercial property market which was continuing to struggle against structural headwinds even before the onset of the pandemic. As shown in Chart 14, the Centre for Retail Research forecasts that more than 20,000 stores could close this year, significantly higher than in 2019 and 2018. This could take job losses in retail above the 200,000 mark.

Meanwhile the industrial sector is likely to benefit from the growing popularity of online shopping. The RICS series suggests that industrial rents could rise by around 2% on an annual basis in the coming year (Chart 15).

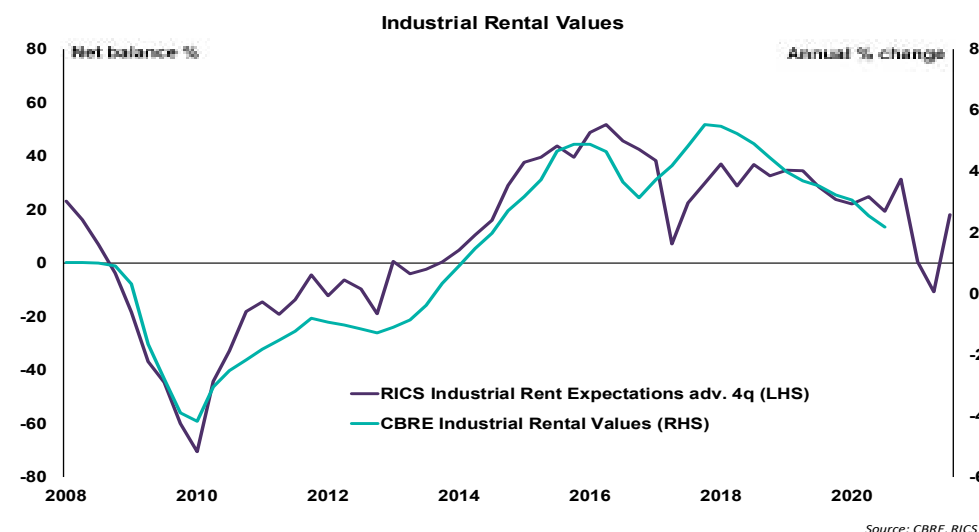
13. All-sector rental values are likely to slip further



14. More than 20,000 shops could close this year



15. Rent expectations are positive for the industrial segment



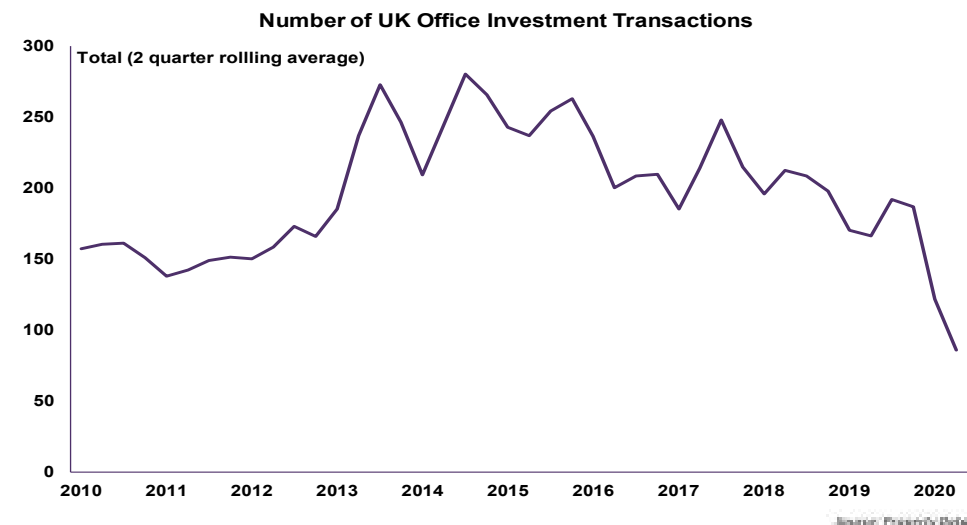
Commercial Property Sector

Estimates compiled by Property Data are consistent with momentum slowing significantly on the investment side of the market with the latest data suggesting that UK investment transactions have fallen sharply over the course of this year. A sizeable drop was also noted in the number of office transactions. It is likely that activity will remain subdued in the coming months as containment measures restrict trading (Chart 16).

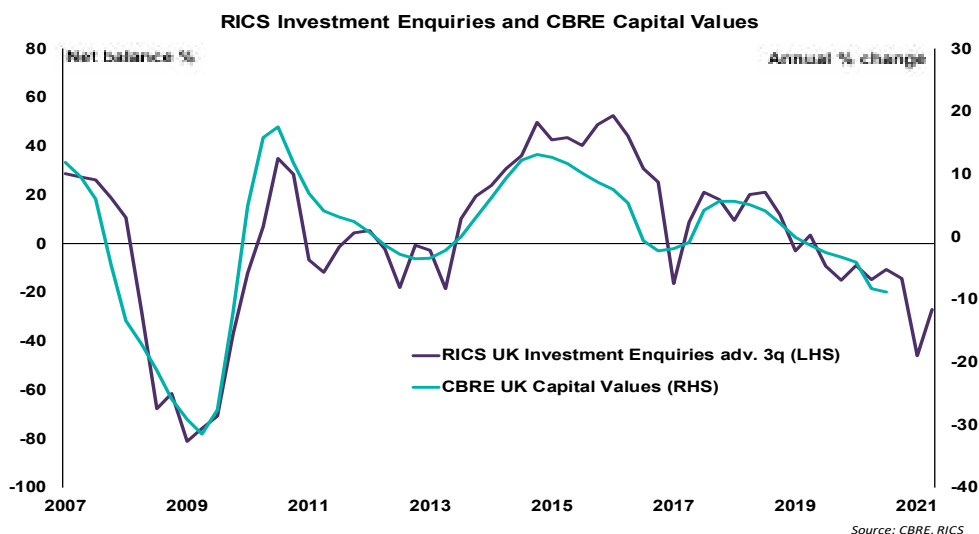
Similarly, feedback to the RICS survey indicates that investor demand has continued to pull-back in Q3 2020 with the net balance reading of -27% consistent with a decline in investment enquiries over the quarter. It is also suggestive of a further drop in commercial property prices in the coming months (as shown in Chart 17).

Meanwhile, the latest RICS survey results show a rise in investor appetite for sustainable buildings. A net balance of +43% of contributors reported that investor demand had risen for green certified buildings over the past twelve months (Chart 18). It seems that this trend is having an impact on prices, as more than one-third of contributors believe that green buildings receive a price premium over comparable non-green buildings.

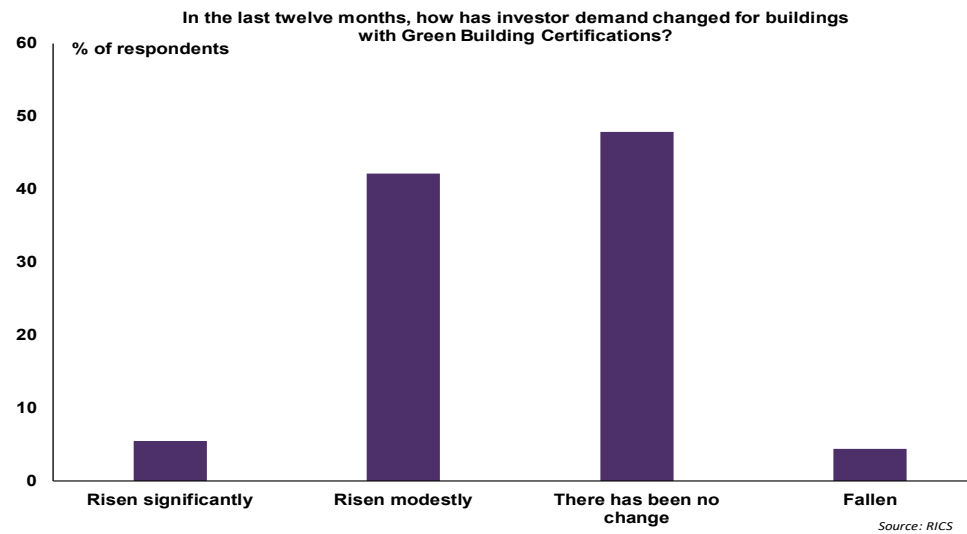
16. Office transactions have slipped significantly



17. Capital values are likely to slip further



18. Investor demand has risen for green buildings



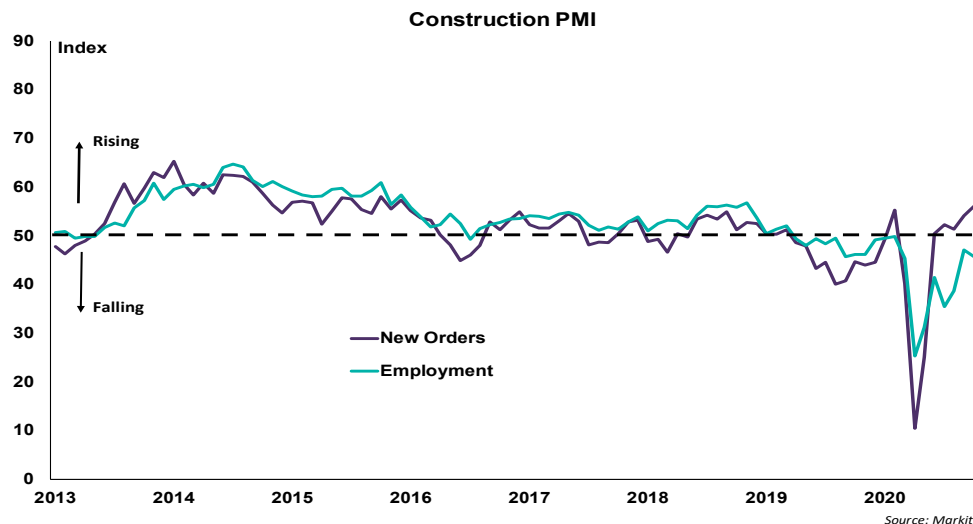
Construction Sector

The Markit Construction PMI came in at 53.1 in October consistent with output rising across the sector. As shown in Chart 19, new orders have recovered following a substantial decline in the second quarter of 2020. That said, the employment index remains below 50 showing that firms are continuing to lay off workers, suggesting that momentum could slow over the coming months.

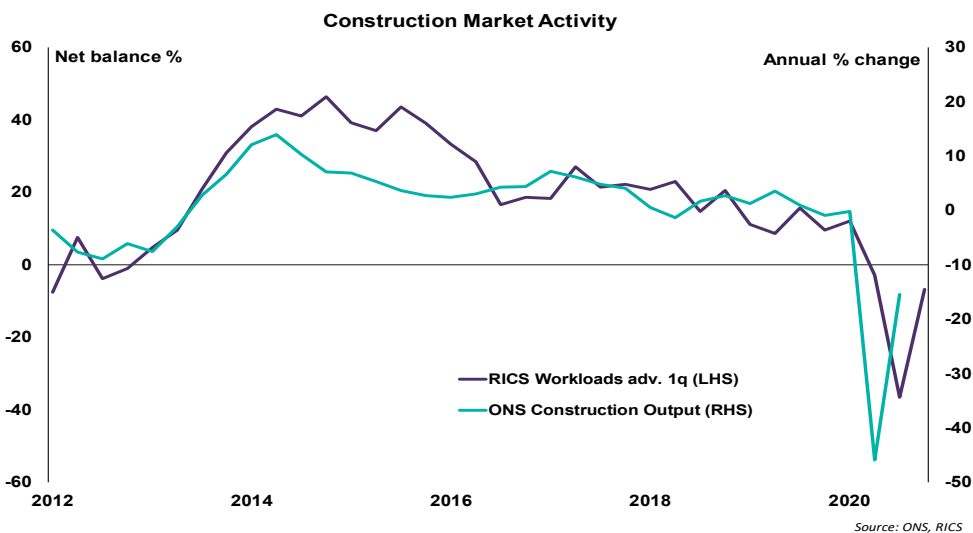
In the RICS UK Construction Market Survey, the headline workloads net balance registered a reading of -7% in Q3 2020 up from -37% in Q2. Although this suggests that activity is beginning to recover somewhat across the sector, it is probable that construction output will remain down on a year-on-year basis, at least in the near term (Chart 20).

Financial constraints, shortage of materials and insufficient demand were cited as significant impediments to market activity at present in the RICS survey. In turn, investment intentions on fixed assets including equipment and software and on workforce development and training have slipped significantly over the course of the year (Chart 21).

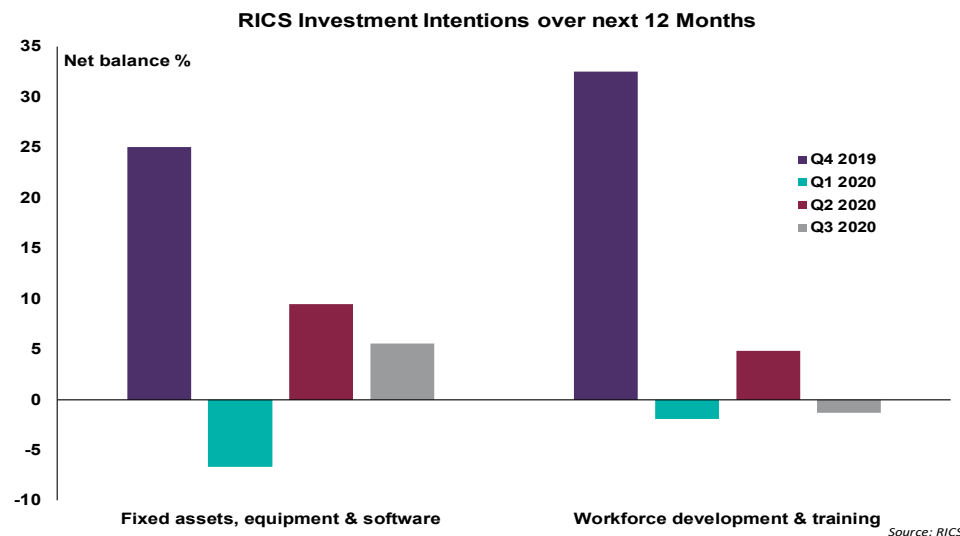
19. New orders are rising but employment seems to be falling



20. Output is unlikely to reach pre-covid levels in near term



21. Unsurprisingly, investment intentions have slipped



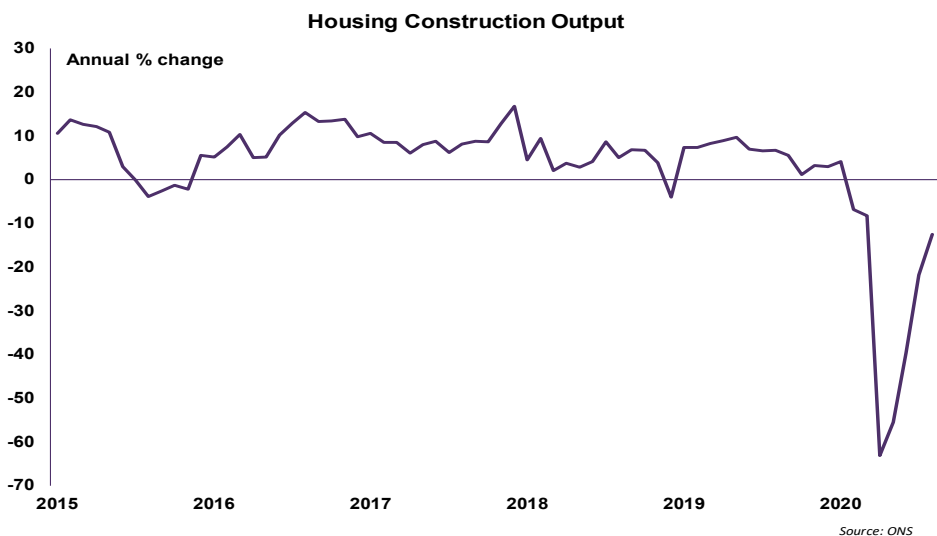
Construction Sector

A net balance of +13% of respondents in the RICS Q3 2020 survey expect workloads to rise in the coming twelve months (compared to -5% in Q2 2020). As shown in Chart 22, infrastructure and private housing workloads in particular are anticipated to be the key drivers of this. Indeed, the UK government's policies around further investment in infrastructure, reforms to the planning system and new permitted development rights are expected to support activity in both of these segments.

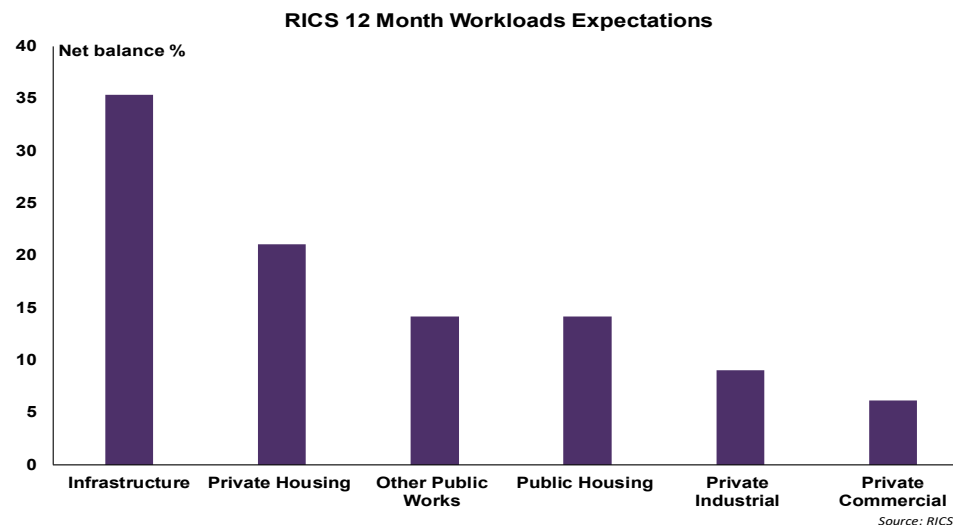
Private housing output appears to have regained momentum in Q3 following a steep fall in Q2. It is probable that activity will continue to rise in the near term on the back of the Stamp Duty holiday and the Help to Buy scheme (Chart 23)

The RICS Q3 survey results suggests that sustainable and green initiatives are being used across the construction sector. Around 62% of respondents stated that building resilience to extreme weather as a result of climate change is considered to be important when designing new projects. In comparison, for repair and retrofit work, this share was closer to 50%. However, the majority of contributors said these evaluations for now are limited to a very small number of projects (Chart 24).

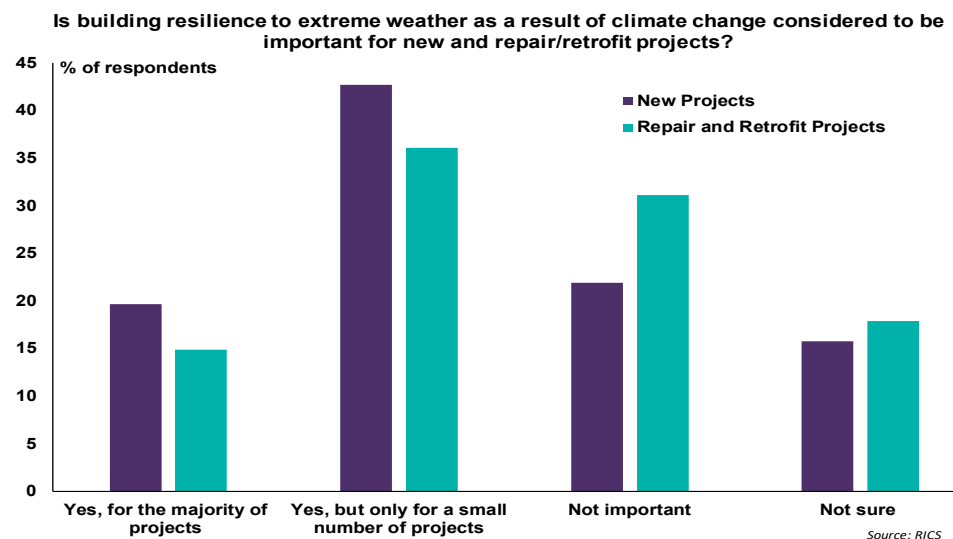
23. Housing output has recovered



22. Infrastructure and housing work is expected to rise firmly



24. Green initiatives are being used across the sector



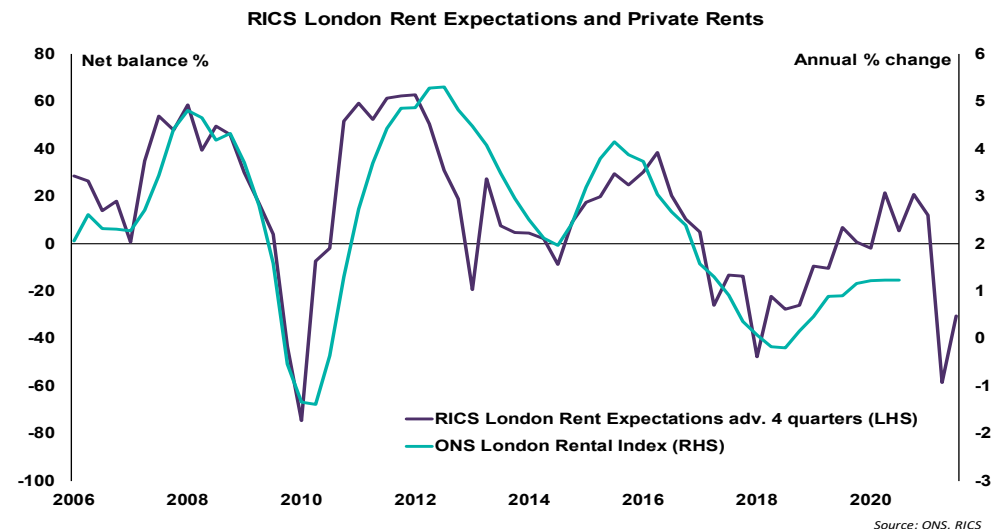
London

Feedback to the RICS surveys suggests that tenant demand has fallen sharply in London over the course of the year, at the same time, new landlord instructions have risen. On the back of this trend, short-term rental growth expectations have slipped, signalling that rents could fall across the capital in the coming year (Chart 25). This contrasts with the national picture, which shows that near term rent expectations have risen in recent months supported by a pick-up in tenant enquiries.

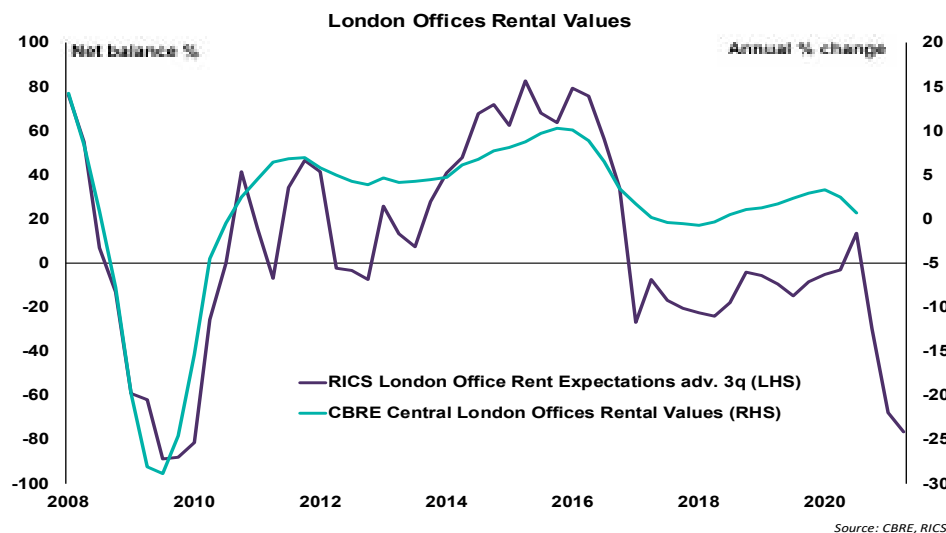
As far as the commercial property market is concerned, the RICS survey results suggest that the office and retail segments of the market are continue to struggle against the challenges posed by the ongoing pandemic. Furthermore, sentiment appears to be more downbeat across London in comparison to the national average. Occupier demand for London office space has declined over the course of the year pointing to a decline in office rental values across the capital in the coming quarters (Chart 26).

84% of the contributors to the Q3 2020 RICS survey see the London commercial property market to be in the downturn phase of the property cycle, a slightly higher proportion than in the Q2 survey (Chart 27).

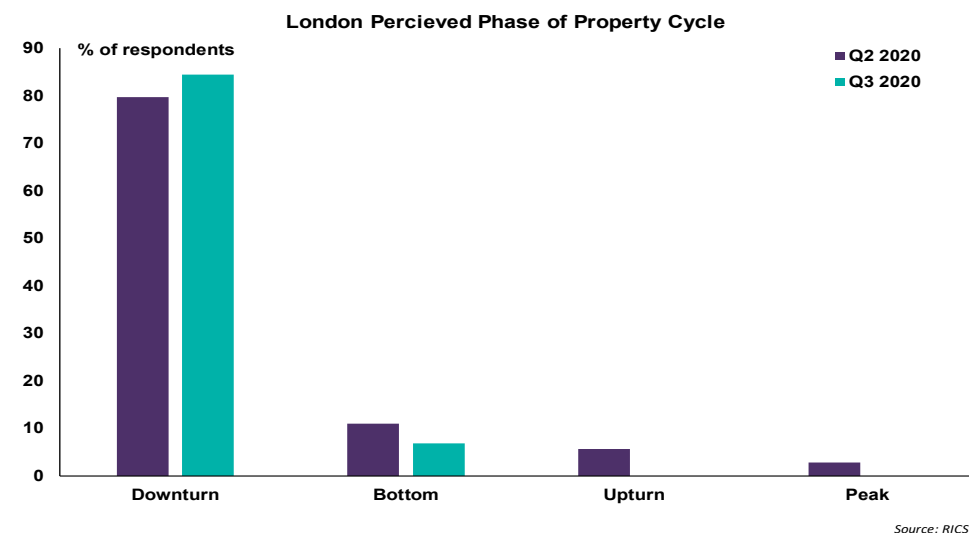
25. London rents could fall the coming year



26. Office rent expectations have slipped



27. Majority see the market to be in the downturn phase



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 Commercial Market Survey (quarterly)*
www.rics.org/commercialmarketsurvey
- *Global Commercial Market Monitor (quarterly)*
www.rics.org/globalpropertymonitor
- *RICS / Ci Portuguese Housing Market Survey (monthly)*
www.rics.org/portugueseemarketsurvey
- *Hong Kong Residential Market Survey (monthly)*
<http://www.rics.org/hong-kong-residential-market-survey>

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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.

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