UK Valuation Dashboard

February 2022

Capital value growth accelerates sharply across the UK Commercial Property Market

ECONOMICS

Economic Summary

Monetary policy tightening is now well underway in the UK, with the Bank of England sanctioning rate hikes in two consecutive meetings for the first time since 2004. What's more, the MPC mapped out their plans to increase rates several more times over the coming months, meaning the key policy rate is now expected to move above 1% by the middle of the year. Prompting this action, consumer price inflation hit 5.4% in December and is expected to move further above the 2% target through H1 (peaking above 7%). Although the economic hit from the rapid spread of the Omicron variant appears to have been relatively brief, a significant squeeze on households' spending power, reduced fiscal policy support and higher interest rates are all leading to GDP projections being trimmed. That said, the consensus forecasts at present still points to the UK economy expanding by close to 4% in 2022.

Commercial Property Market

Commentary

Commercial property ended 2021 on a strong note, with year-on-year rental growth accelerating to hit a five year high at the all-sector level. At the same time, the CBRE total returns index for Q4 points to commercial real estate investment producing a headline annual return of 17%. While the industrial sector remains the strongest performer by a clear margin, each of the three traditional sectors did in fact post positive annual returns. For retail, this marks the first such outcome in four years. Looking ahead, the latest RICS Commercial Survey feedback signals a relatively solid outlook for the year to come, with the prime office sector anticipated to see a progression in its recovery in rents and capital values. That said, growth rates in all-sector capital values are likely to ease to a certain extent compared with recent sharp increases.

Chart 1) Rent Expectations

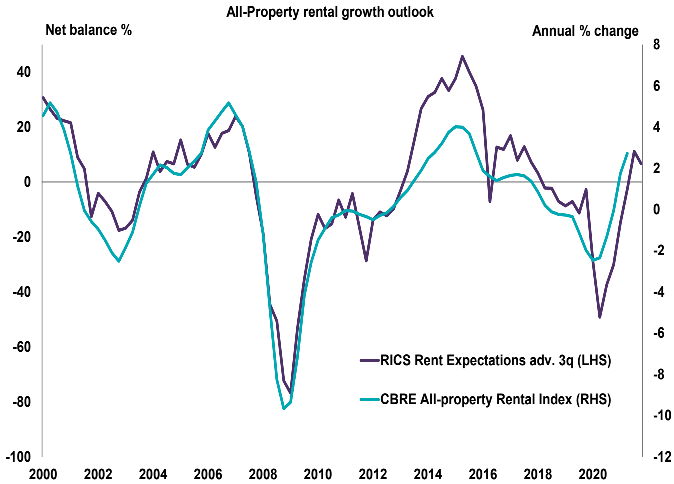

Chart 1 maps the RICS near-term rental expectations series against the annual change in the CBRE rental index. Advancing the former on by three qaurters enables us to gauge the likely outlook rents. As such, the latest headline reading for rent expectations suggests yoy rental growth is likely to settle at just over 2% through to Q3 2022.

Chart 2) Investment Enquiries

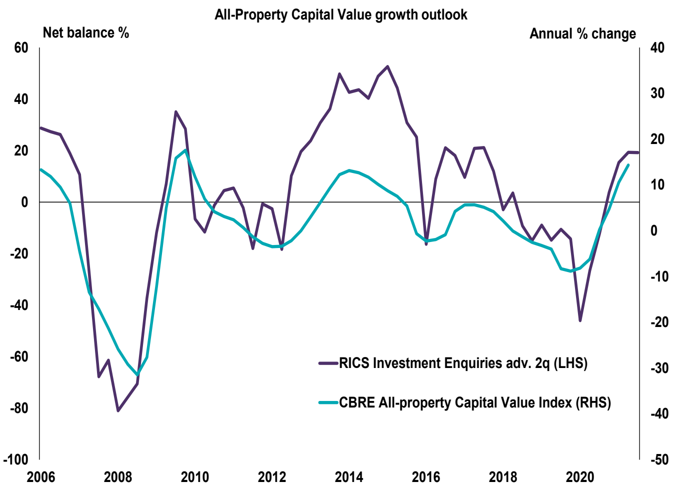

Chart 2 demonstrates the relationship between the RICS Investment Enquiries series and the yearly growth rate in the CBRE capital value index (with the RICS survey data pushed on two quarters). On the basis of this, it looks as if capital value growth will begin to steady, following the sharp acceleration reported in Q4, with a yoy pace of between 13-15% likely to being maintained through to H2.

Chart 3) Industrial Capital Values

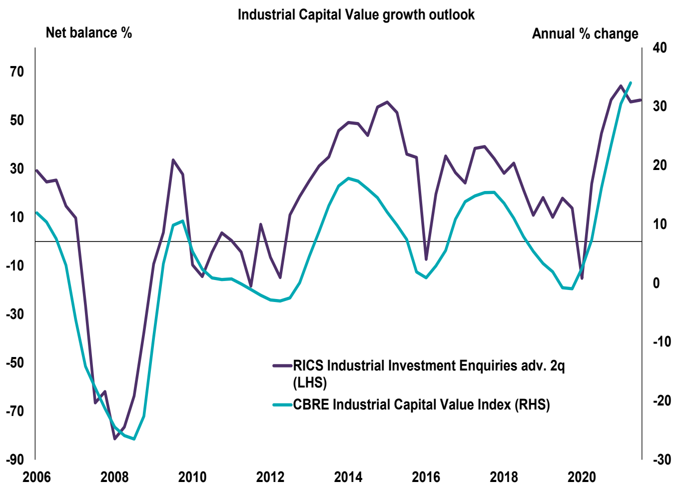

Chart 3 shows this same relationship, but focuses specifically on the industrial sector. It points to industrial capital value growth beginning to ease marginally going forward, albeit from a record pace of over 30% yoy as of January 2021.

Residential Property Market

Commentary

The residential property market remains characterised by still solid demand being met by a lack of stock available for sale. This is resulting in continued upward pressure on house prices which, for the time being, shows no sign of abating. Indeed, house price indices produced by Nationwide, Halifax and the Land Registry all estimate growth is running at close to (or above) 10% yoy currently. Moreover, the RICS Residential Market Survey feedback indicates prices are set to rise sharply through the first half of the year, with metrics capturing the balance between supply and demand suggesting price growth will cool only gradually through H2. That said, with the Bank of England outlining their intention to raise rates several more times over the coming months, this could begin to weigh on housing market activity more significantly in due course.

Chart 1) House prices

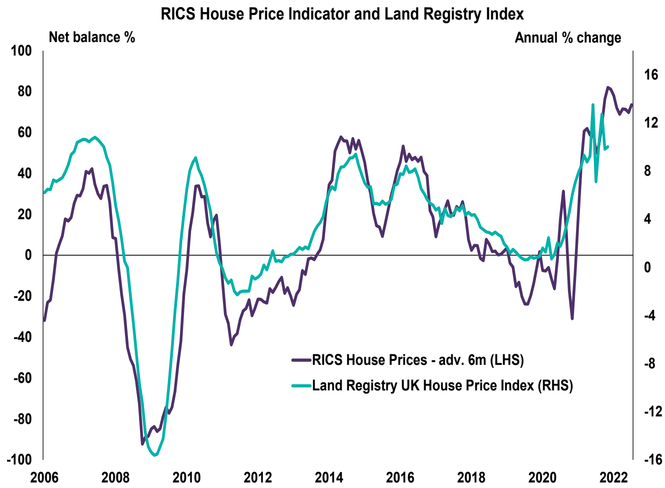

Chart 1 looks at the RICS Price net balance against the official house price index from the Land Registry. The RICS series provides a six month lead and has been pushed forward accordingly. From this, given the minimal easing in the survey feedback on price growth of late, it looks likely that a near double digit pace of house price inflation will be maintained through to the mid point of 2022.

Chart 2) Regional prices

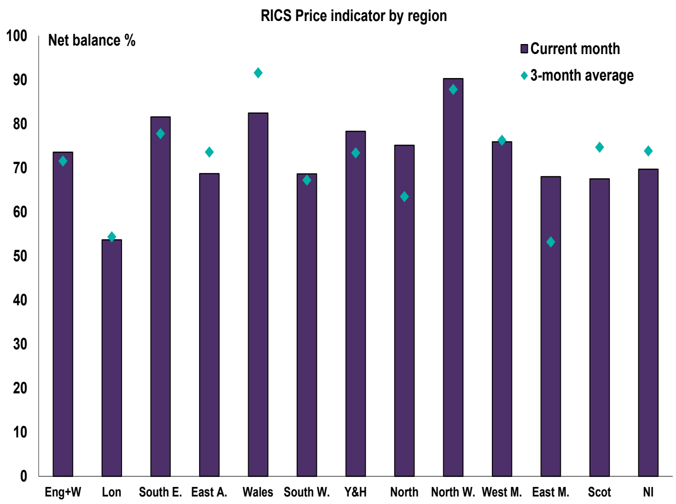

Chart 2 shows the RICS Price balance disaggregated at the regional/country level. All areas continue to return elevated readings, consistent with further strong price growth to come over the next six month. Even in London, where the price series has generally lagged the rest of the country over the past year, the latest net balance reading is above +50%, and therefore indicative of a sharp pace of house price growth.

Chart 3) Sales volumes

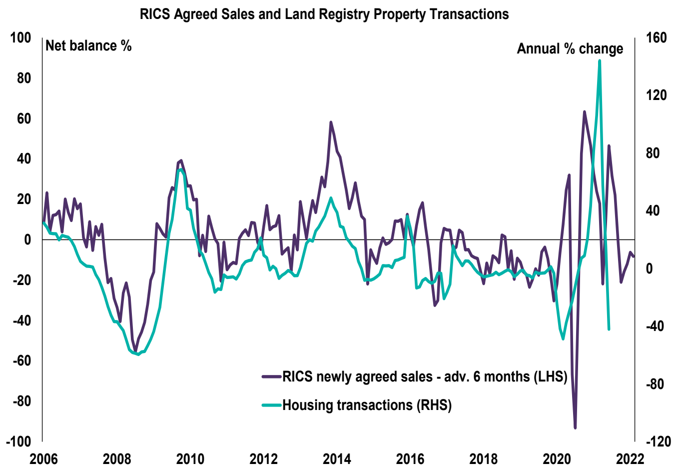

Chart 3 plots the RICS agreed sales net balaance alongside the residenital sales volume figures produced by the Land Registry. The stamp duty holiday inevitably cuased large fluctuations in sales numbers ahead of the tapering out of the tax break and the subsequent full removal. Nevertheless, the latest RICS survey data points to a positive yoy trend coming through over the first half of the year.

Real estate indicators

	Latest reading	2022 RICS Economics forecast	Commentary
All-property Index (annual growth rate)			
Capital values *Source: CBRE*	+14.7%	+6%	All-sector capital value growth is now running at an annual pace of nearly 15%, the sharpest rate of increase since 2014. The acceleration seen over the past six months has been dramatic, considering the yoy increase stood at just 3.1% back in July.
Rents *Source: CBRE*	+2.8%	+3%	Headline rental growth reached 2.8% yoy in January having accelerated markeldy during the final quarter of the year. As such, this represents the strongest rate of rental gains at the all-sector level since 2016.
Offices			
Capital values *Source: CBRE*	+4.8%	+4%	Office capital value growth turned positive in September last year, and has moved sharply higher since (leaving values 0.3% below Feb 2020 levels).
Rents *Source: CBRE*	+0.7%	+1.5%	Office rents have also edged up in recent months, with the annual rate of growth now at 0.7%.Compared with prior to the pandemic, office rental levels are now down just 0.1%
Industrial			
Capital values *Source: CBRE*	+36.4%	+12%	The extraordinary rise in indsutrial values continues, with the annual growth rate hitting a fresh record high of just over 36% in January according to the CBRE index.
Rents *Source: CBRE*	+9.4%	+6%	Industrial rents have risen by 9% over the past twevle months, marking the strongest growth on record by some margin (previous record was 5.7% in 2018).
Retail			
Capital values *Source: CBRE*	+7.6%	+3%	Retail capital values have now risen in each of the past nine months according to CBRE estimate. This leaves the annual gorwth rate at 7.6%. Nevertheless, retail values more than 10% below Jan 2020 levels.
Rents *Source: CBRE*	-1.5%	+0.5%	The annual growth rate in retail rents continues to turn less negative, with the current -1.5% yoy chance signficant less downbeat than -5.2% seen back in July.
Hotels			
Price index *Source: Costar*	-1%	no change	Having been hit hard by the pandemic, hotel transaction prices appear to have stabilsed of late.
Rents *Source: RICS GCPM*	no data	no change	RICS members are forecasting a generally flat trend in hotel rents for 2022.
Residential			
House price index *Source: Land registry*	+10%	+5%	House price inflation remains sharp, with 2022 likely to bring further strong growth. That said, with Bank rate now expected to hit at least 1% by May, this could take some sting out of the market.
Rents *Source: Zoopla*	+5%	+5%	The shortage of stock on the rental market looks set to drive rents firmly higher in 2022.

Supply and demand

	Latest reading	12-months ago	Commentary
Offices			
Vacancy rate *Source: Costar*	6.6%	5.4%	Office vacancy rates appear to be flattening out according to CoStar data, albiet the current level is still well above the 4.8% low seen prior to the pandemic.
Occupier demand *Source: RICS GCPM*	-3% net balance	-63% net balance	The RICS occupier demand indicator appeared to be knocked back slightly in Q4, hampered by the surge in Omicron cases and subsequent work from home orders over the period. Nevertheless, expectations point to a modest recovery being resumed through the early part of 2022.
Investment enquiries *Source: RICS GCPM*	+5% net balance	-34% net balance	The RICS Investment Enquiries indicator has now been in marginally positive terrioty in each of the past two quarters across the office sector. This is indicative of a modest pace of recovery now underway.
Industrial			
Vacancy rate *Source: Costar*	3%	3.1%	Industrial vacancy rates remain at historically low levels, with the latest quarter seeing another fall in availability.
Occupier demand *Source: RICS GCPM*	+56% net balance	+22% net balance	Occupier demand continues to rise sharply for industrial space, with the latest reading across the RICS indicator remaining close to record-highs.
Investment enquiries *Source: RICS GCPM*	+58% net balance	+45% net balance	Investor demand for industrial assets remains robust, with the latest survey evidence continuing to singal a sharp uptick in enquiries.
Retail			
Vacancy rate *Source: BRC*	14.4%	13.7%	In Q4 2021, the BRC retail vacancy rate tracker fell (albiet by only 0.1%) for the first quarter since 2018. As such, it appears a turning point, or at least a plateu, may have finally been reached across the beleagured sector.
Occupier demand *Source: RICS GCPM*	-23% net balance	-78% net balance	The RICS occupier demand metric for the retail sector remained negative in Q4, not helped by pandemic developments over the period. That said, this is still significantly less downbeat than at the start of 2021.
Investment enquiries *Source: RICS GCPM*	-16% net balance	-63% net balance	The Q4 reading for retail investment enquiries from the RICS survey, while still subdued, was much less negative than at the start of the year, with greenshoots of recovery appearing to emerge.

Further reading:

RICS UK Economy and Property Update

RICS UK Commercial Property Market Survey

RICS UK Construction and Infastructure Survey

RICS UK Residential Market Survey

Net balance data:

- Net balance = Proportion of respondents reporting a rise in prices minus those reporting a fall (if 30% reported a rise and 5% reported a fall, the net balance will be 25%).

RICS Economics forecasts are formulated using forward looking indicators from the UK Commercial Property Market Survey. This includes both twelve month point estimates and net balance data.

Delivering confidence

We are RICS. Everything we do is designed to effect positive change in the built and natural environments. Through our respected global standards, leading professional progression and our trusted data and insight, we promote and enforce the highest professional standards in the development and management of land, real estate, construction and infrastructure. Our work with others provides a foundation for confident markets, pioneers better places to live and work and is a force for positive social impact.

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