BE NEWS

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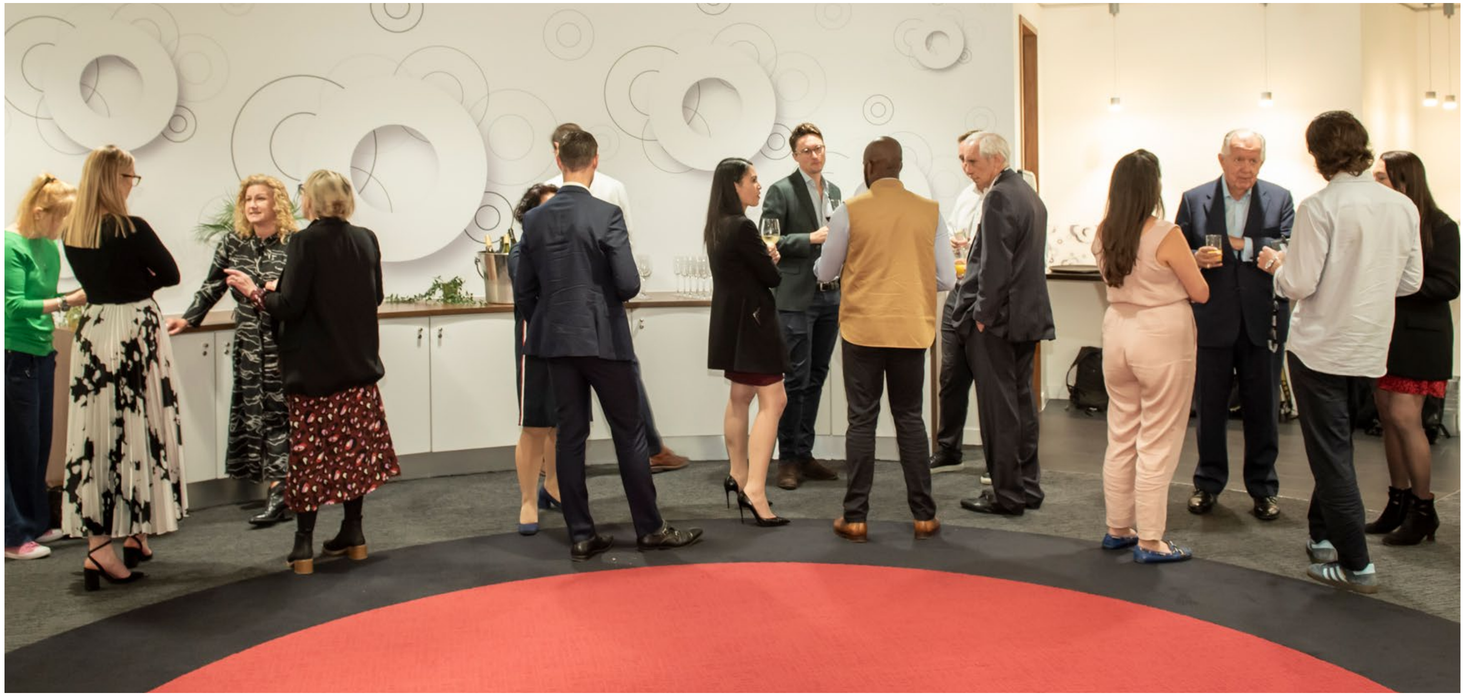
STATE OF THE MARKET: WHERE ARE WE NOW AND WHERE ARE WE HEADING?

BE News and DWF recently assembled a panel of experts to discuss the current political landscape and what the future holds for the market ahead of next year's general election

THE PANEL

James Froud, partner, DWF
Natasha Guerra, chief executive, Runway East
Yohance Harper, partner, Quadrant Estates
Steve Norris, former MP and chairman of Soho Estates
Liz Peace CBE, adviser on property, politics and the built environment
Jamie Pearson, fund manager, HLIF (AlTi, Tiedemann Global)
Jon Quéré, director, CBRE Investment Management
Carla Revelo, real estate partner, DWF
James Scott, co-founder, Stories
Neil Sinclair, chairman, London Active Management
James Vivian, director, business space investment, Savills
Maria Wiedner, chief executive, Cambridge Real Estate Finance
Noella Pio Kivlehan, journalist, *BE News*
Liz Hamson, editor-in-chief, *BE News*



The property market is at a critical juncture. After one of the quietest summers most of us can recall, deal activity remains subdued. Funding is hard to raise. Even the industry golden children of life sciences and industrial are struggling. Next year, we have a general election to contend with and Labour is making all sorts of pledges relating to planning, housing and the green belt – while the Tories have rowed back on net zero policies. So, could things be looking up or will ongoing economic challenges put paid to any political clarity that might be emerging?

Some of the biggest names from across the built environment shared their views on the state of the market at a discussion chaired by *BE News* editor Liz Hamson and sponsored by law firm DWF.

QUESTION: Where are we right now and what did we make of the party conferences?

SINCLAIR: I'm disappointed with the Tories. They don't look competent; they look amateurish. They've been very poor with business, and I can't understand why they haven't got rid of the tourist tax. I haven't got the confidence that they can turn the country around. My fear with Keir Starmer is that he might be worse.

NORRIS: The biggest single difference between the parliament I joined in 1983 and the one MPs will join in 2024 is the advent of social media, and how appallingly corrosive it is. Before, if you disagreed with me, you might write to me, and I'd write back. It was very much you and me. It wasn't all on Twitter or Facebook. I was getting on average between four and 800 emails a day.

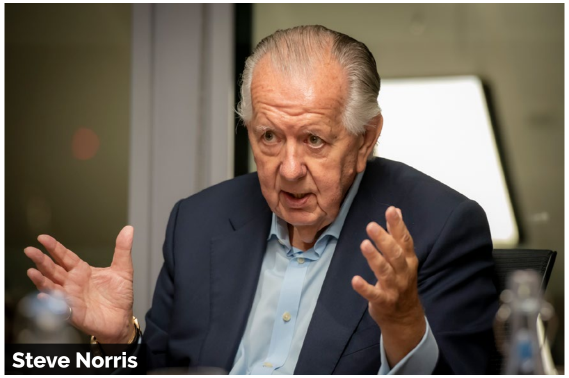
The pernicious impact of this is MPs in both parties tend to be more worried about what sort of media they're getting from their constituents than they do about loyalty, for example, in the party.

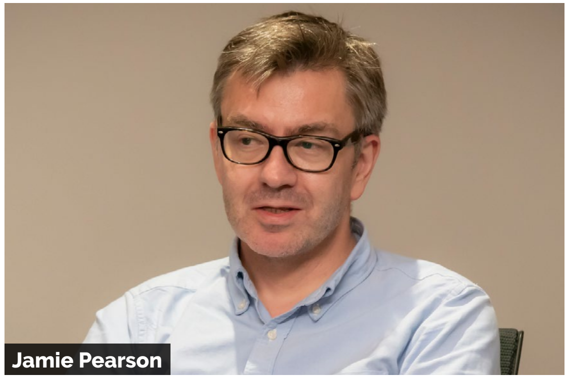
You are just a representative. And that means discipline has disappeared already in the ruling party, and I don't see it being any different for Labour.

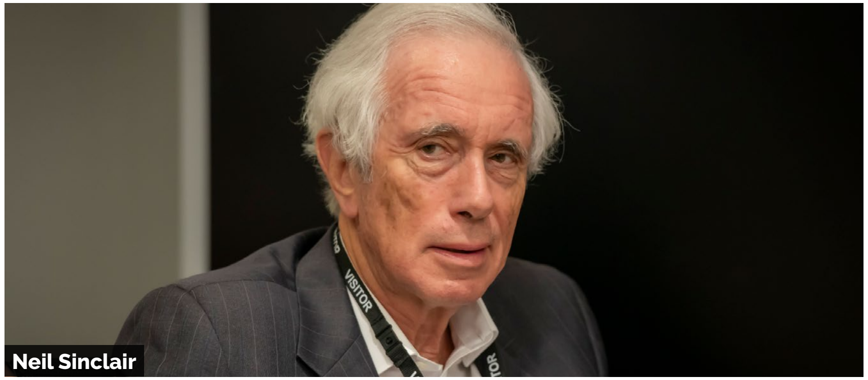
SCOTT: We're in a period of flux because of huge change. At a macro perspective, we have come out of a time of long-standing peace from the west's perspective. That's changed. We've also got a lot of new technology that is disrupting things. Social media is a massive external influence that needs to be worked out.

FROUD: It's unfortunate that the government has pushed net zero policies further down


James Froud


Steve Norris


Jamie Pearson


Neil Sinclair

the agenda. As an industry we had to prepare for the changes to the MEES regulations that came into force earlier this year. There was a lot of time spent – not to mention hard work involved – in readying portfolios for that change and we've seen many of our clients already start to prepare for what they expect might be coming next.

That perhaps has now been thrown into doubt and we have, as yet, no clear guidance on what the EPC requirements may be in 2030. If the current government, or any new government, raises the bar for minimum EPC ratings in either 2027 and/or 2030, as many anticipate, clarity is needed now so clients can start to prepare.

QUESTION: Are we assuming the next government is going to be Labour?

SINCLAIR: I think the Conservatives are going to nick it. Rishi's lucky – his opponent is Keir Starmer. The problem is Britain's not working, particularly in the public sector. It's terrible. It's terrible with local authorities and with HMRC.

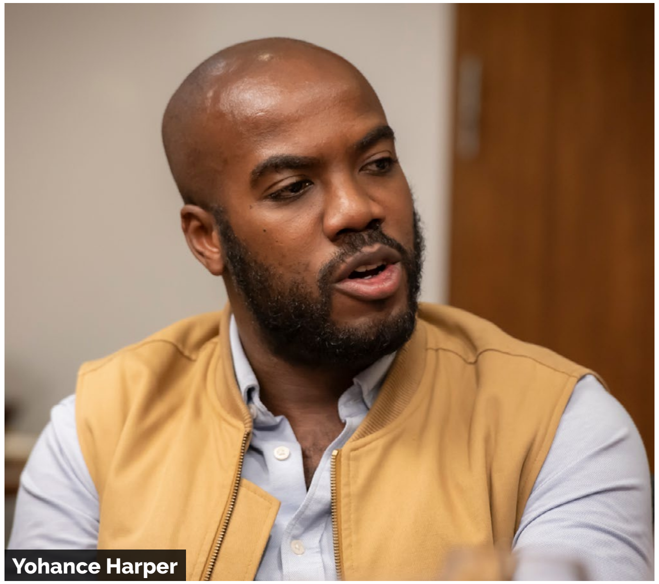
NORRIS: It is true that almost every part of government administration now takes about three times as long as it did 10-15 years ago. You must ask why. Why do planning consents take triple the time? There are some systemic problems, which Labour will inherit and have no answer to.

PEARSON: [On the Labour party's pledge to building 1.5 million homes over five years] it was mainly geared towards building more social housing. We could get to see more supply come through, but I'm not sure it's particularly different to anything we've seen before.

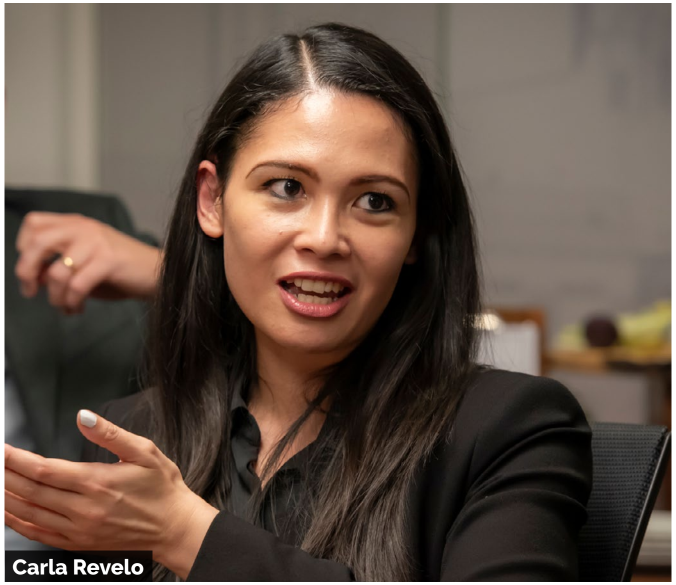
SCOTT: Three years ago, when the conversation around things like yields and gilts was more optimistic, that suggested an economic recovery, which would have tied in very well with next year. The fact that the latest forecast shows it's not going to get better as quickly as it was perhaps a few months ago plays against the Tories, because it will be very difficult to share any progress. [People are] fed up with what they've got. The overriding emotion is that a lot is not working; it's maybe time for change. That's what Labour are going to run on, and that's probably going to prevail.

QUESTION: How is ESG driving the market?

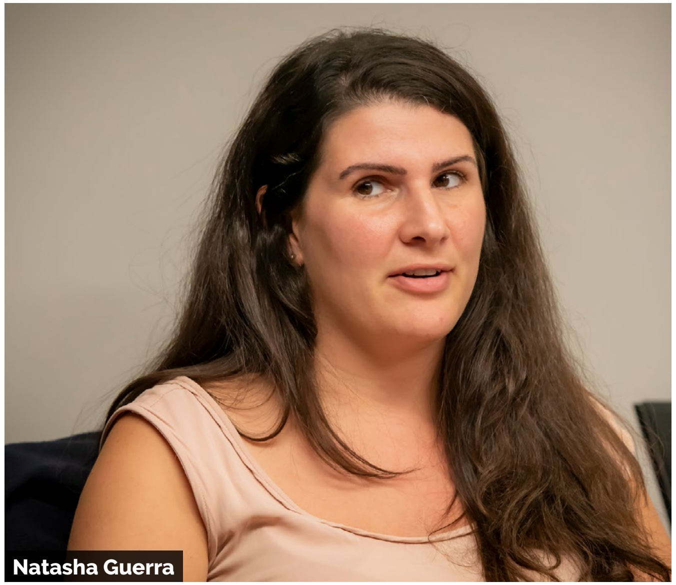
HARPER: As the gap between prime and super-prime increases, ESG is one of the defining factors. To achieve the highest ⊳



Yohance Harper



Carla Revelo



Natasha Guerra

rents, benchmarks like BREEAM 'Outstanding' are becoming standard. The real differentiator of value in the new generation of buildings will be in their operation, which will prove how sustainable they actually are.

Equally, it's easy to forget that ESG is more than sustainability; community and location are just as important. We couldn't be happier with the location of YY London, our new 415,000 sq ft refurbished former Reuters building at Canary Wharf.

So much is happening in the area to transform it into a thriving mixed-use destination and the new Elizabeth line is taking people there in record numbers. Occupiers are going to notice this and the buzz the area offers their employees.

REVELO: There are more tenants agreeing to include green lease provisions in leases. However, interestingly, when parties actually try to operate some those green lease provisions in practice, for example in relation to making improvements to increase energy efficiency, there is less appetite from either party to actually incur any costs in order to make the necessary improvements. As such, there is a danger that green lease clauses just become a tick-box exercise, enabling parties to report to their investors that leases contain these provisions without actually operating them in practice.

GUERRA: Pre-Covid, no one ever asked a single question about anything related to sustainability. Initially, it was landlords driving the conversation, who wanted their buildings upgraded to meet EPC targets. Now the conversation is being pushed by people coming into our buildings, and I genuinely don't think we will be selling space that wasn't meeting criteria. This has happened in a short space of time where it's gone from being on nobody's agenda to being on everyone's.

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>
> *Yohance Harper*

PEACE: Are we in danger of it being a two-tier market because there are people who want to do the right thing? I'm a non-executive of Howard de Walden, and we are looking at how we can turn our estate, of mostly very old buildings, into something that performs as well as possible with ESG credentials. And we are doing it because we don't want our estate to lose value.

But a lot of people holding property don't think like that and they will still find some occupiers for their space. So, the big problem is this bifurcation of the market, which is not helped by some of the responsible people who say 'well it's costing too much to improve that building so I'm going to sell it to somebody', and you can sell anything at the right price. But who buys it? What do they do with it?

VIVIAN: It's not that there is a danger of it becoming a two-tier market – it is a two-tier market. Post-Covid, all the big nine cities have achieved record rents – some may find that unbelievable. Tenants are generally taking 12% to 15% less space but paying the same overall rent.

We've got blue-chip companies that are in perfectly usable offices and are exploring turning them into net zero. That's great. But there needs to be a separation of best in class and carbon net zero because I think you can deliver carbon net zero without the building being best in class.

This is being driven by the tenants. A couple of years ago we were speaking with just the real estate teams but now the HR teams are more involved in real estate decisions. This is because businesses are under pressure to deliver on their carbon net zero targets at a corporate level and the buildings they occupy are a big part of that. Therefore, we are seeing tenants not legislation driving the conversation around delivering carbon net zero buildings.


James Vivian


Jon Quéré

QUESTION: What about the investment outlook?

QUÉRÉ: Where pricing currently sits, in the main, real estate doesn't provide a high enough risk-adjusted return versus a fixed-income investment. This suggests pricing across the real estate sector is still under pressure, more so in certain sectors like offices, which is undergoing a structural transition.

That said, there are, and will be, some interesting opportunities, for example in the living sector, which provides an inflationary income profile, and the underlying occupational market is very strong.

In the logistics sector we've seen significant and quick repricing. It provides an interesting income return from the outset with the prospect of potential yield compression in the medium term.

It feels as though a lack of stock, and a continued disparity between a purchaser's and vendor's expectations of pricing, will lead to a quiet Q4. Hopefully, as we move into 2024, there will be more clarity on inflation and the direction of travel of interest rates.

WIEDNER: Looking at how politics can help the real estate market, Boris Johnson – and I

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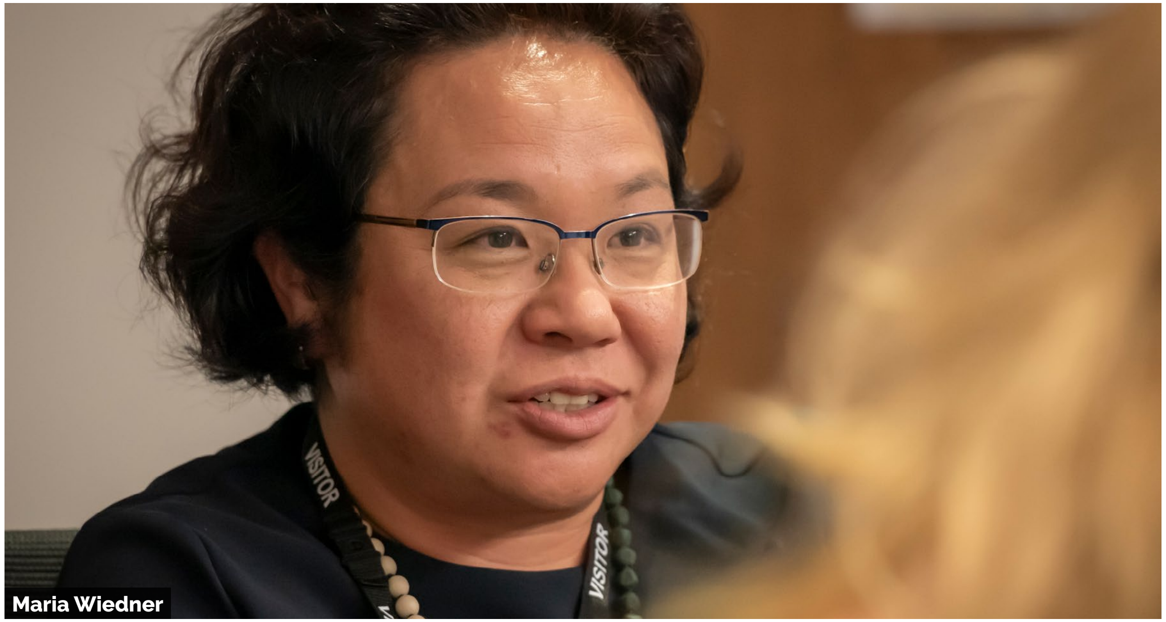
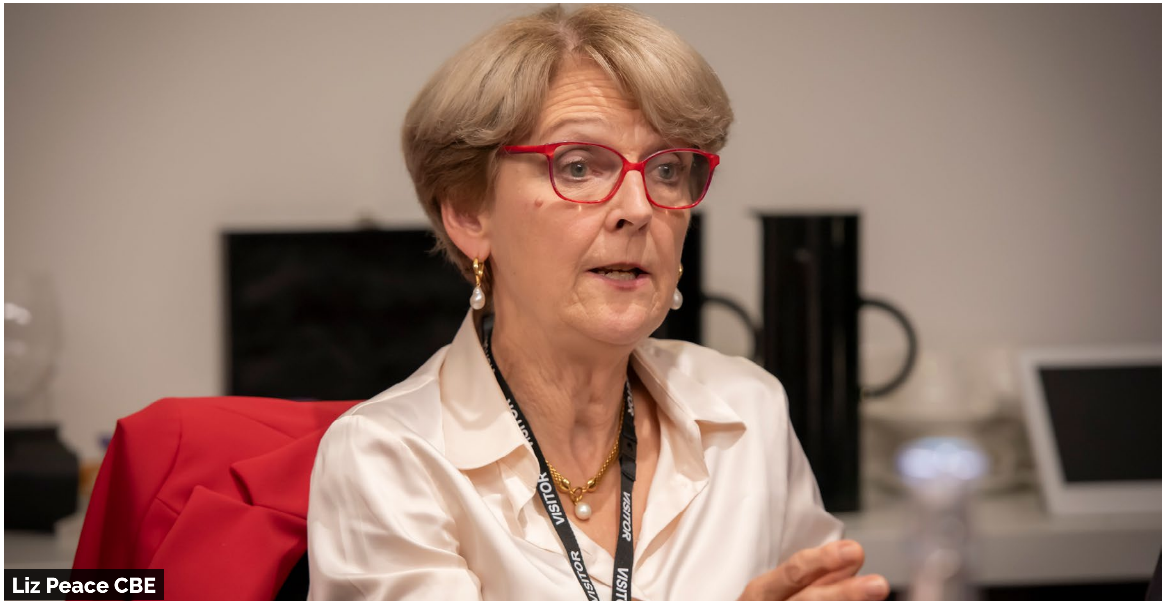

Maria Wiedner


Liz Peace CBE

One thing the property industry has always been very good at is finding opportunities

Liz Peace

am not his fan – for whatever reason managed to flex the regulation on offices. So it could help us to have less regulation on the change of use, and values would know what the best use is for it in that particular time, and would help us prevent large drops.

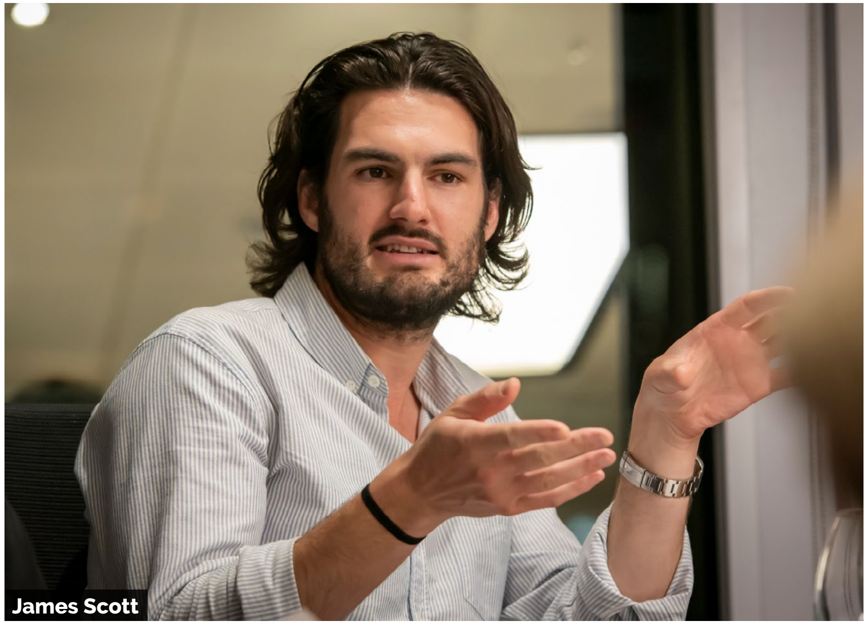
QUESTION: Where do you think we are in the property cycle right now, and what is the single biggest challenge and single biggest opportunity in the next 12 months?

NORRIS: We're near to the bottom. As planning is taking three times as long as it did 10 years ago, there's got to be something that can be improved to get developers into the market quicker. The biggest challenge is what happens with a change of government.

PEACE: We're hovering about the bottom of the market. The biggest challenge is politics in the next 12 months until the election. In the several projects I'm involved in we're worried about atrophy – nothing is going to move.

Biggest opportunities? There are clever people with real estate out there who can find interesting assets at the right price and do something very good with them. One thing the property industry has always been very good at is finding opportunities.

PEARSON: We're peering over the precipice, but we can't see the bottom yet – we've still got a long way to go. The challenges are in



James Scott

> ***Local councils know they just need to get things done and are working hard with private sector partners***
>
> *James Scott*

the commercial sector: it's related to demand, both tenant and investor, which is stagnant, and we're struggling to get out of that cycle. The opportunities are in the residential sector where you have clear and very defined demand that just needs meeting. [check]

GUERRA: Opportunities are converting space that's no longer suitable for other commercial use so flex can open a whole different market to customers and landlords. Challenges are managing growing operational costs, which are making it challenging to create margin.

SCOTT: There is optimism in the public sector at local council level. They know they just need to get things done and are working hard with private sector partners to find ways of doing that in spite of everything going on. Yes, the macro-political environment is a big challenge, but even going above that, the overall macro position, with everything happening in the world, is having an impact.

HARPER: There are opportunities with AI: it will change the way we work in the same way that email and mobile phones did. From a building perspective, technology is also making it easier than ever before to be sustainable. Both YY London and OSMO, our major new ESG-led 140,000 sq ft workspace scheme in Battersea, are smart buildings. Modern technology has been a major factor in enabling both buildings to achieve net zero in operation.

WIEDNER: We still have some way to go to the bottom – maybe a year. The biggest challenge in real estate in this country is planning reform. If you can sort that, it might be for the better, especially regarding building new houses.

SINCLAIR: I quote Nathan Rothschild: "The time to buy is when there's blood in the streets." And I think that will be the early part of 2024. The challenge is seeking out those opportunities and they will be there.

REVELO: Taking an optimistic view, we are probably looking at increased transaction volumes possibly in Q1, Q2 2024. We are seeing a few interesting deals being marketed now, which are attracting good levels of interest.

It is also largely dependent on the asset class – hotels, residential, logistics and life sciences remain attractive whereas other asset classes, such as offices in certain locations, are more challenging.

Opportunities can be found in pricing where investors may find opportunities at a historically low entry/price point. However, the challenge is parties agreeing on realistic pricing.

FROUD: I see the political landscape and the forthcoming general election as a potential opportunity. We've all said that things aren't working now and I don't think that can change until we have had an election. That will hopefully bring about a period of more stability, in the economy and more generally, which in turn might inject a bit of confidence into the market. We've been through an unprecedented period. We need some solid 'stable' government and perhaps things may settle down a bit. □

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