Considerations for the real estate industry

March 2020
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Considerations for the real estate industry
Context
UK Coronavirus Cases (Number)

Source: Worldometers/Deloitte Real Estate

Figure 1. Total coronavirus cases in the UK (Linear Scale)
The economic consequences of the coronavirus

Change in 2020 GDP Growth Forecasts

Figure 2: Change in 2020 GDP Growth Forecasts

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Sources: Refinitiv, Capital Economics
UK construction activity PMI index

- UK construction companies signalled a return to business activity growth during February, following a nine-month period of declining workloads.
- However, concerns around the coronavirus are expected to weigh on sentiment in the coming months.

**Figure 3: UK construction activity PMI index**

By 1st March, coronavirus cases had been detected in England, Wales, Northern Ireland and Scotland.
• The rapid spread of coronavirus is expected to hit global real estate investment in the short-term as travel and face to face meetings are restricted.

• The speed of the market rebound will depend on the period of the pandemic and the pace at which functionality returns coupled with investor confidence.

• Opportunistic purchasers are expected to seek to take advantage of the period of inevitably reduced liquidity.

• Equity fundraising likely to be impacted by reduced investor confidence in cash flow resilience - although debt markets may prove more accessible as policy makers seek to provide support.

• Funding issues due to falling values (covenant breaches) and the loss of income (covenant issues) as leading UK property funds have halted trading.

Figure 4: UK commercial property investment volumes (£millions)

Source: Property Data/Deloitte Real Estate

*Figures as of 20th March 2020
Offices
Office market

Short-term impact:
• Businesses unable to operate remotely, with lower IT resilience and reliant on static office models will be most affected by Covid-19

• Demand for short term office space to fall as workers stay away, impacting the co-working market. This will be mitigated by businesses which need to relocate temporarily as a result of the outbreak

• Occupiers to demand Covid-19 clauses in lease agreements.

Long-term impact:
• Enforced experience of agile working is likely to accelerate trend towards more flexible and remote working

• Businesses seeking new office accommodation are likely to require less desk-space per head, with office function shifting to a greater proportion of accommodation devoted to collaboration/meeting room space

• Occupiers to build provisions for community hygiene into their leasing agreement

• Greater adoption of proptech solutions such as robotics that can detect, sanitise and clean buildings

• Greater investment in IT resilience to promote alternative remote working arrangements

• Potential requirements for “multi-centre” disaster recovery accommodation as businesses seek to divide teams delivering essential/critical services.
UK retail footfall has plummeted by more than a fifth compared with 2019.

**Figure 5. UK footfall % change by day**

- Wednesday 18th March (YoY): -27.8%
- Wednesday 18th March (WoW): -23.7%

Source: Springboard
• Increased risk of **store closures**, in an already challenging UK retail market, impacting landlords’ rents

• March 2020 Barclaycard survey - more than a quarter of shoppers said they were **avoiding high streets** and other busy places because of virus

• **Food deliveries** and **e-commerce** are thriving but will be dependent upon resilient supply chain

• Rise in sales at supermarkets as shoppers are **stocking up** on essentials such as toilet rolls, hand sanitiser, dried pasta and tinned tomatoes

• Challenges to global supply chains as borders close with potential **move to more onshored models** on recovery.
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Impact on hospitality in Europe

Figure 6. Impact on hospitality in Europe, occupancy % change

Source: STR, Costar Realty Information
Hospitality

- A **significant reduction in demand**, with major conferences and high profile events around the world being cancelled or postponed

- Risks to **staff availability** may put a further strain on operators’ capacity to provide a service

- The magnitude of the impact will depend on the duration of the outbreak and counteracting measures

- A potential for a rapid rebound in the second half of 2020 as activity returns to normal level but the **return to normalcy could be protracted**

- We are waiting to see if Covid-19 triggers structural change in the industry.
Industrial & Logistics
Industrial & logistics

- **Disruption to global supply chains** causing supply shortages

- A shift towards **re-shoring or near sourcing of manufacturing**

- Warehousing firms specialising in providing short-term excess space is likely to see a drop in demand

- Increased use of **automation and robots** in warehousing

- Power to become a more important location factor than labour

- A surge in online grocery shopping during the outbreak could be more permanent, which will further **increase demand for logistics space**.
How could the real estate industry change post Covid-19?
How could the real estate industry change post Covid-19?

- **Remote working** to become a more permanent feature of our lives

- With high levels of working from home, **technology** across life and business is likely to be **more integrated**

- With **more online grocery shopping**, it will impact how retailers operate, with a higher demand for warehousing space

- With disruption of supply chains, businesses will **shift towards re-shoring or near-shoring**

- With travel restrictions and reduced air pollution, we are likely to see less demand for travel and **more emphasis on sustainability.**
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