



**Tuesday 17 January 2012**

Speakers

Ian McCafferty  
Chief Economic Adviser  
CBI

Stuart Morley  
Consultant Research  
GVA

**Looking for a land of plenty  
but still feeling the pinch?**

**Economic Property Market Review**

[gva.co.uk](http://gva.co.uk)

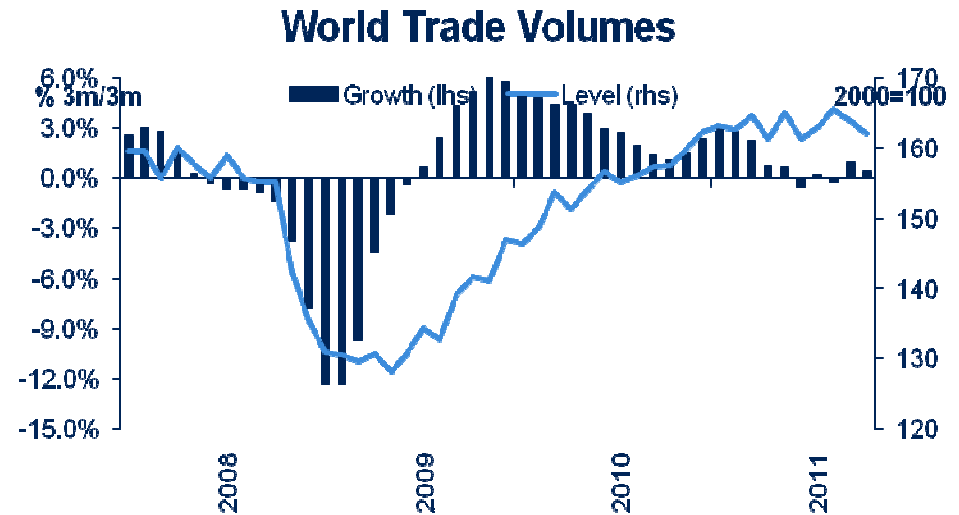
# Economic Outlook

## Challenges for business

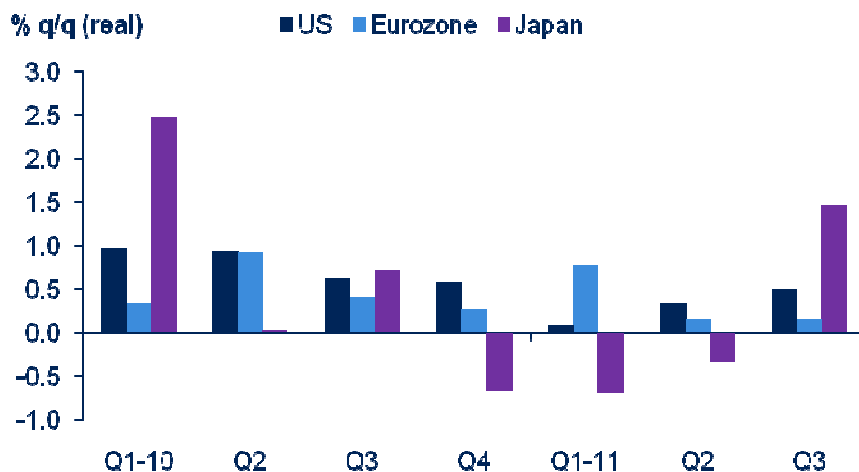
**Ian McCafferty**  
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# A divergent and uncertain global recovery

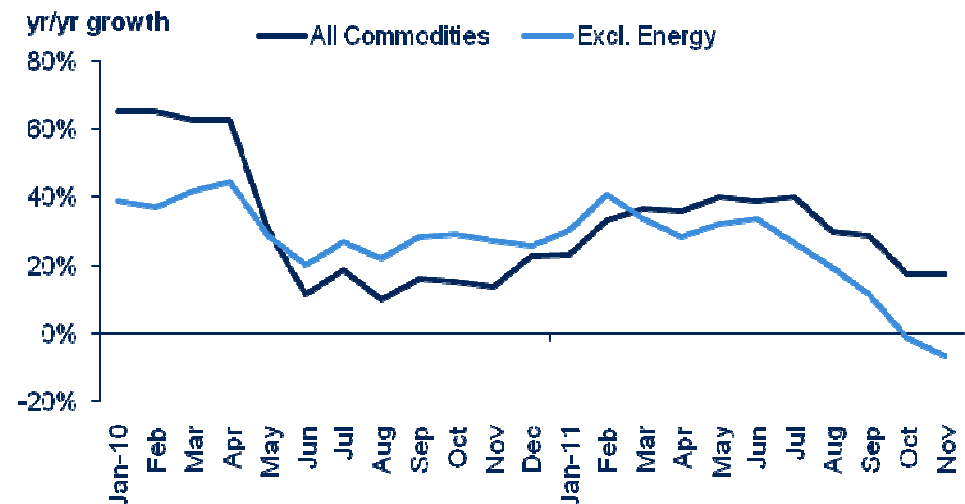
- **2011H1 Growth pause**
  - Commodity prices
  - Supply chain disruptions
  - China slowdown
- **2011H2 Improvement in US, Japan and EMEs, but Eurozone worsened**
- **The outlook for 2012**
  - A world of two halves
  - Critically dependent on the outcome of the Eurozone crisis



## Advanced Economy Growth Rates

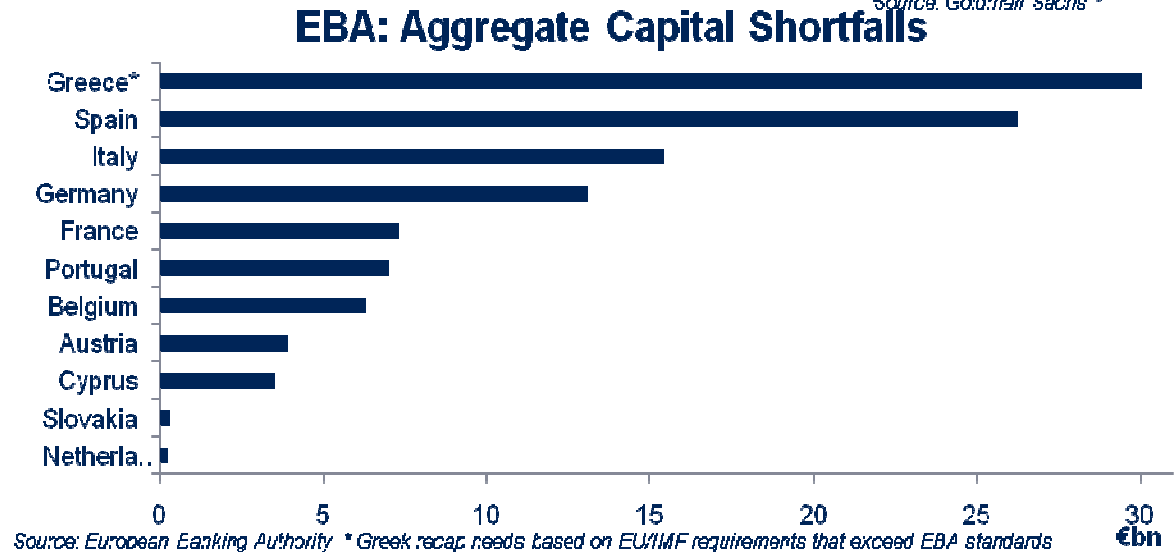
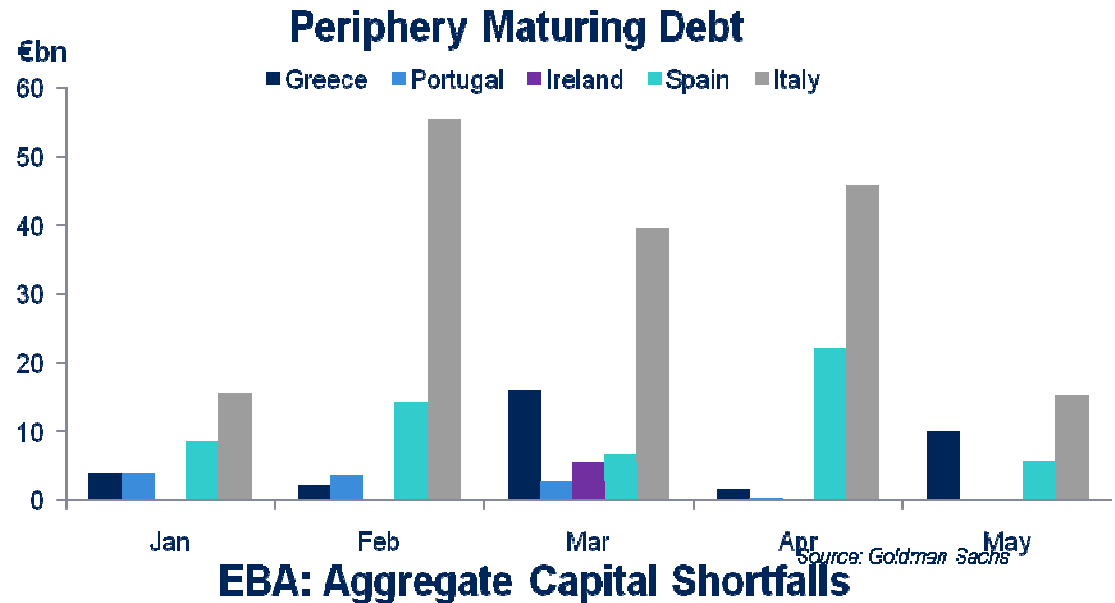


## HWWI Commodity Price Indices (\$)



# How will the Euro crisis play out?

- **Into the end-game**
  - Will EU leaders finally step up to the plate?
  - The immediate priority is to support sovereigns and provide liquidity
  - The cost of failure is enormous
- **Need for systemic solution**
- New & rigorous fiscal architecture
- Default arrangements
- Bank recapitalisation
- Joint debt responsibility
- Supply side reform
- Competitiveness imbalances
- Short to medium-term growth package
- **2012H1 a testing time**
- Sovereign debt rollover
- Bank refinancing
- Fiscal pressures
- The IMF and Greece



# UK overview 2011-13

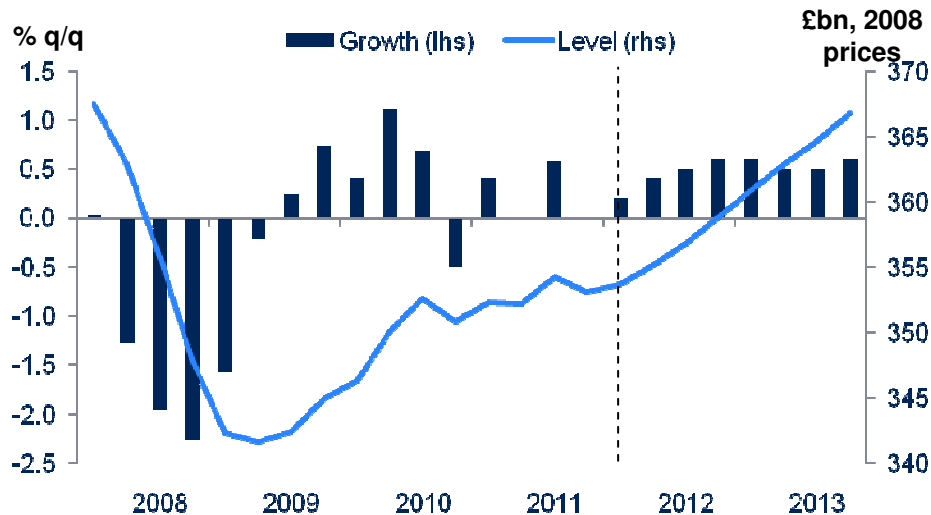
**2012 set to be another difficult year; some momentum building up through 2013**

- Growth is likely to have stagnated over the winter
- Recovery is crucially dependent on prospects for the Euro area – corporate confidence, trade and financial linkages
- 2012 will be sluggish – little support from households and drag from fiscal consolidation
- Inflation will fall, but unemployment will continue to rise

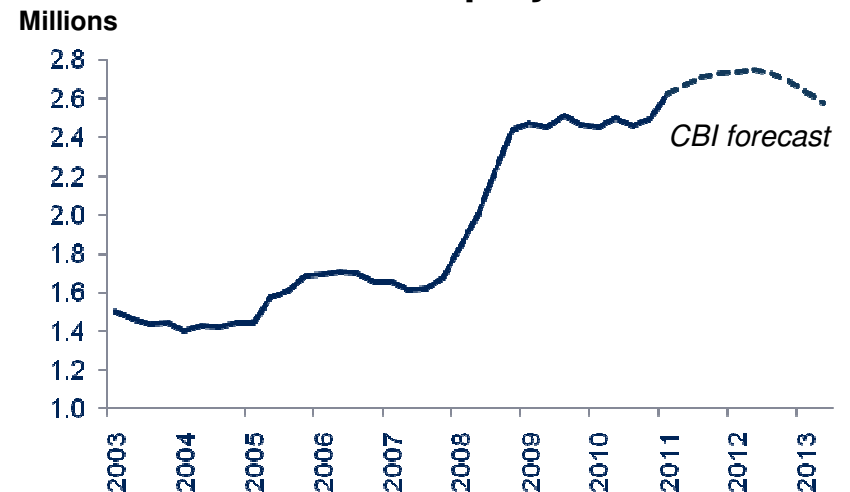
## Latest UK Forecast

	2011	2012	2013
GDP	0.9	1.2	2.2
Household Consumption	-1.2	0.0	1.7
Manufacturing output	2.8	0.6	1.5
Consumer Prices	4.5	2.9	2.1
Unemployment (%)	8.0	8.5	8.3

### CBI GDP forecast

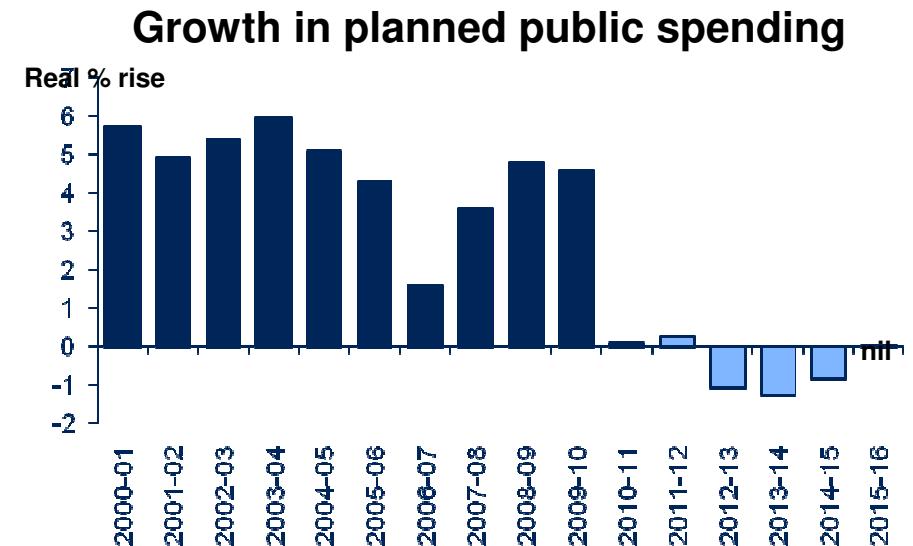
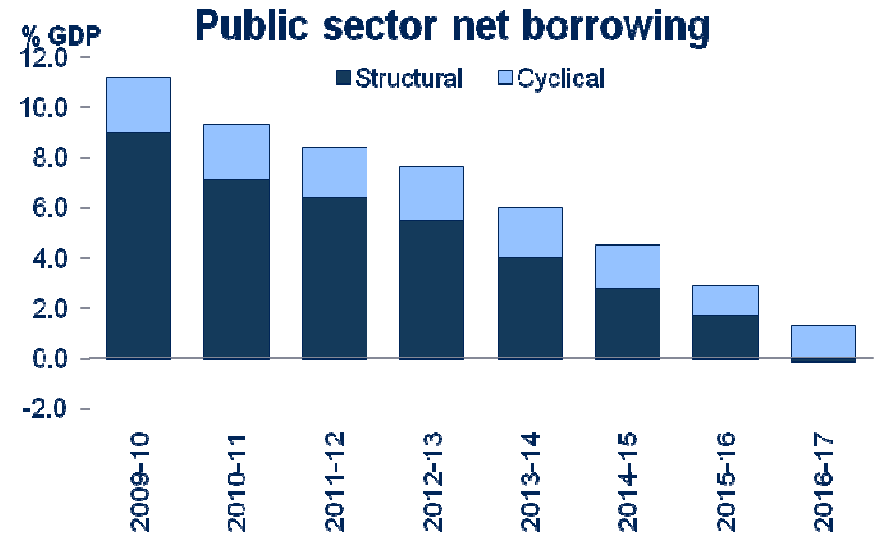


### ILO unemployment



# UK: fiscal and monetary policy

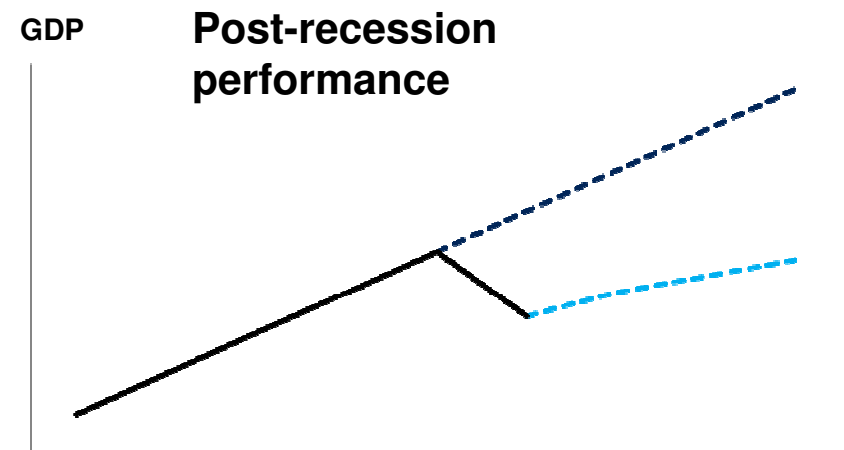
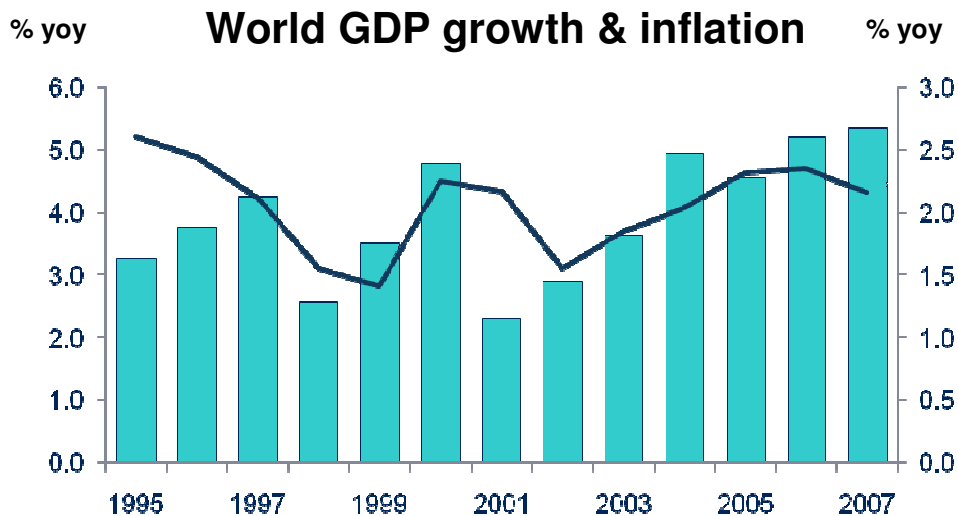
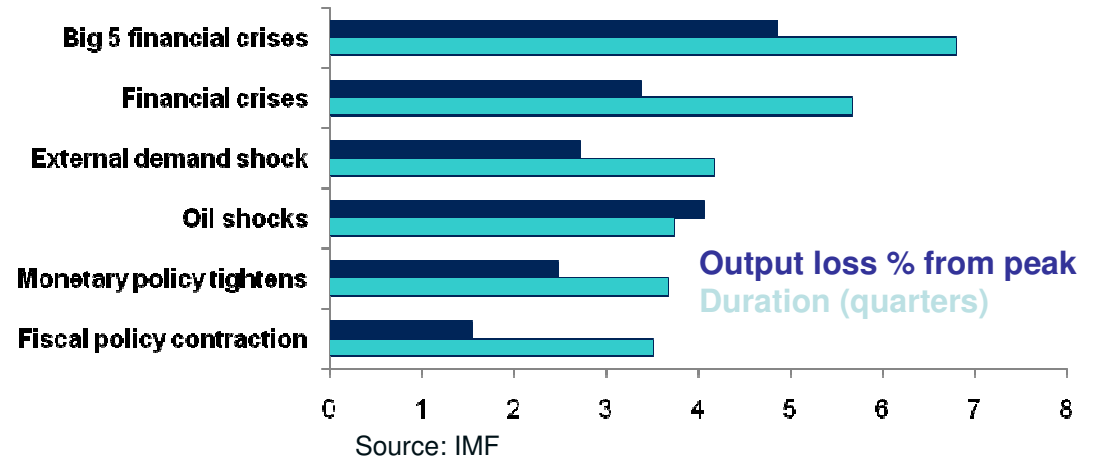
- **Austerity package under pressure**
  - Deficit elimination two years later
  - Debt peaks at 78%
- **Impact on economy**
  - Annual drag on GDP of ~0.5% points
  - Credibility premium delivers looser monetary policy
- **Monetary policy to remain accommodative**
  - Low rates into 2013
  - More QE?
- **Looking forward**
  - 2012 Budget
  - Plan B?



# The shape of the recovery?

- End of the “Nice Decade”
- Legacy impacts from the financial crisis
  - Bank recapitalisation
  - Consumer deleveraging
  - Fiscal austerity
- Growth constrained for some time

## Shocks and Recessions



# Economic Outlook

## Challenges for business

GVA

January 2012

# Property Market Outlook

Stuart Morley

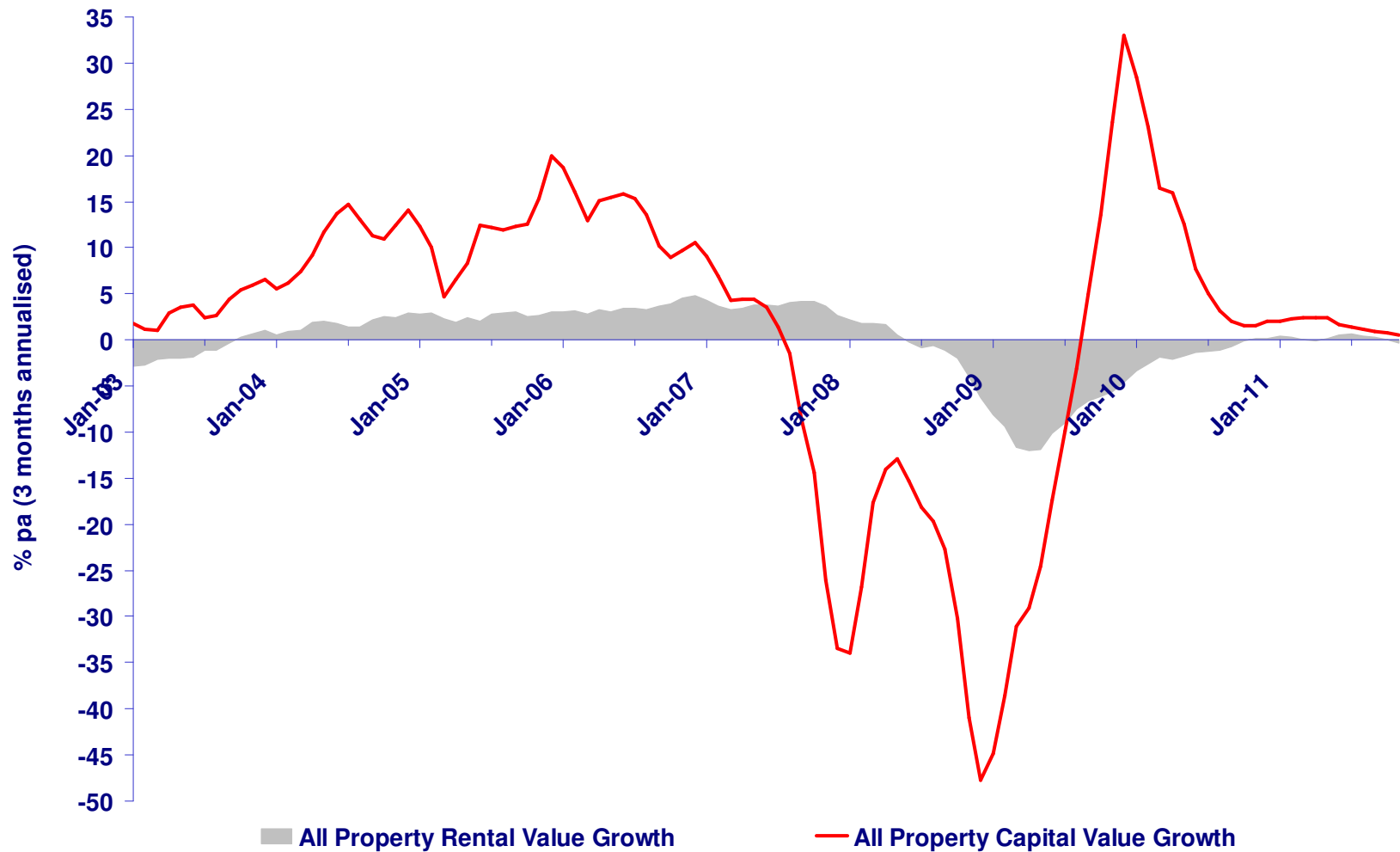




- **Where we are now**
- Demand drivers
- Supply – vacant property and new development
- Occupier markets and rental growth
- Capital value and investment return outlook
- Conclusions

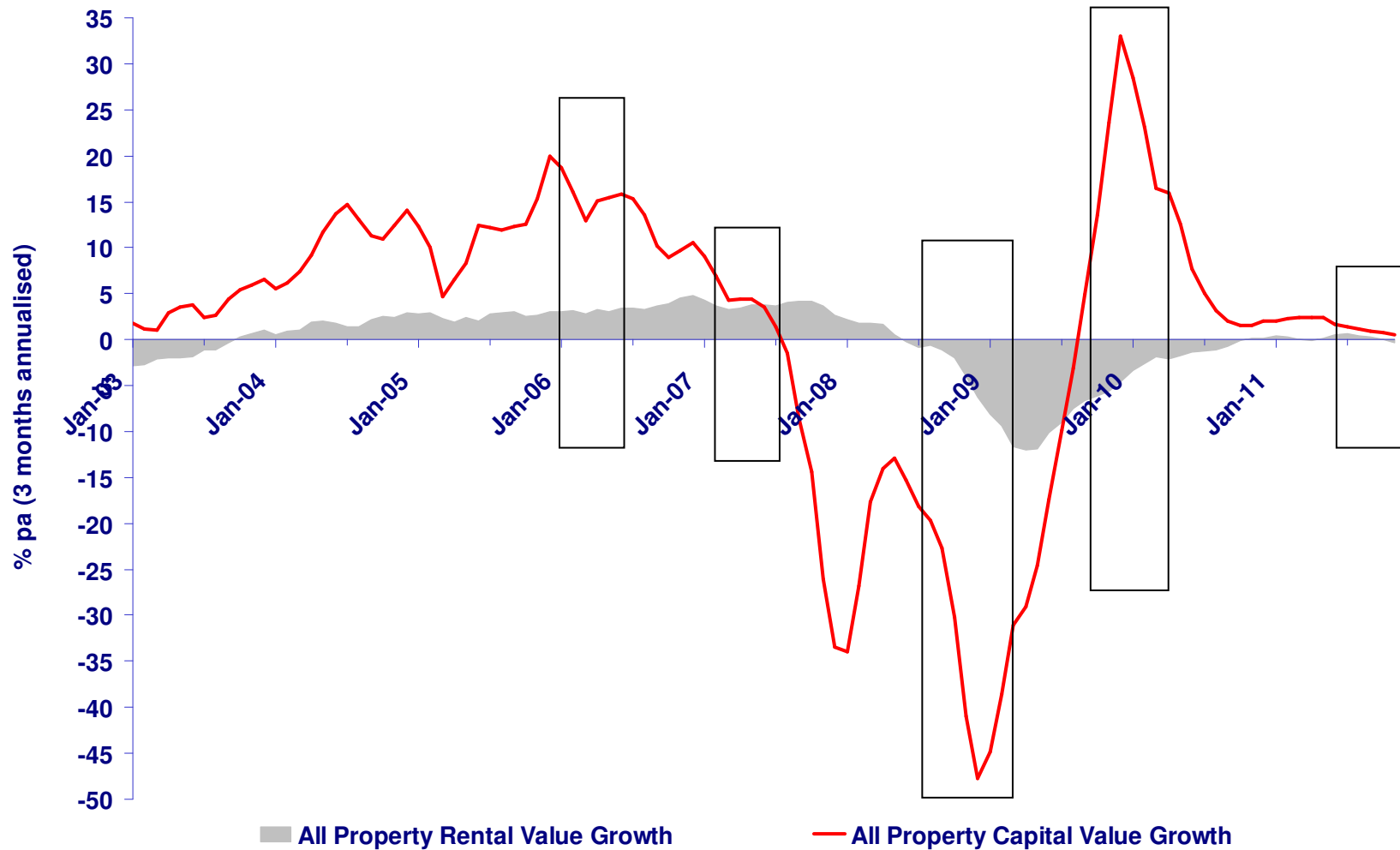
# Rental & Capital growth (3 month annualised)

- huge volatility in capital value growth (2007-2010), but rental value and capital value growth remarkably stable and flat over last twelve months



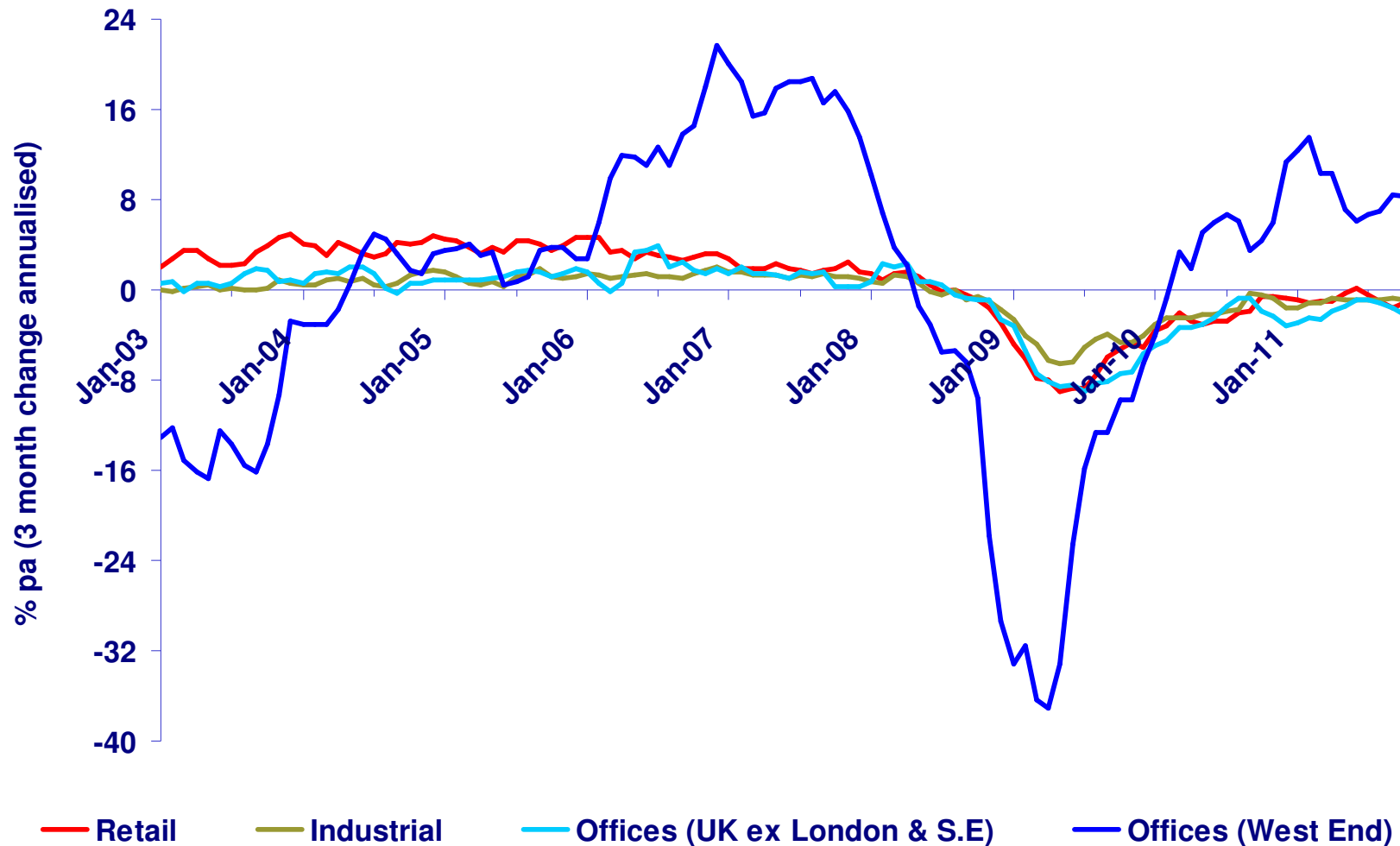
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# Rental Value Growth (3 month change annualised)

- all sectors have improved over last 2 years, particularly central London offices, but improvement is slow and outside London has been flat over last 12 months

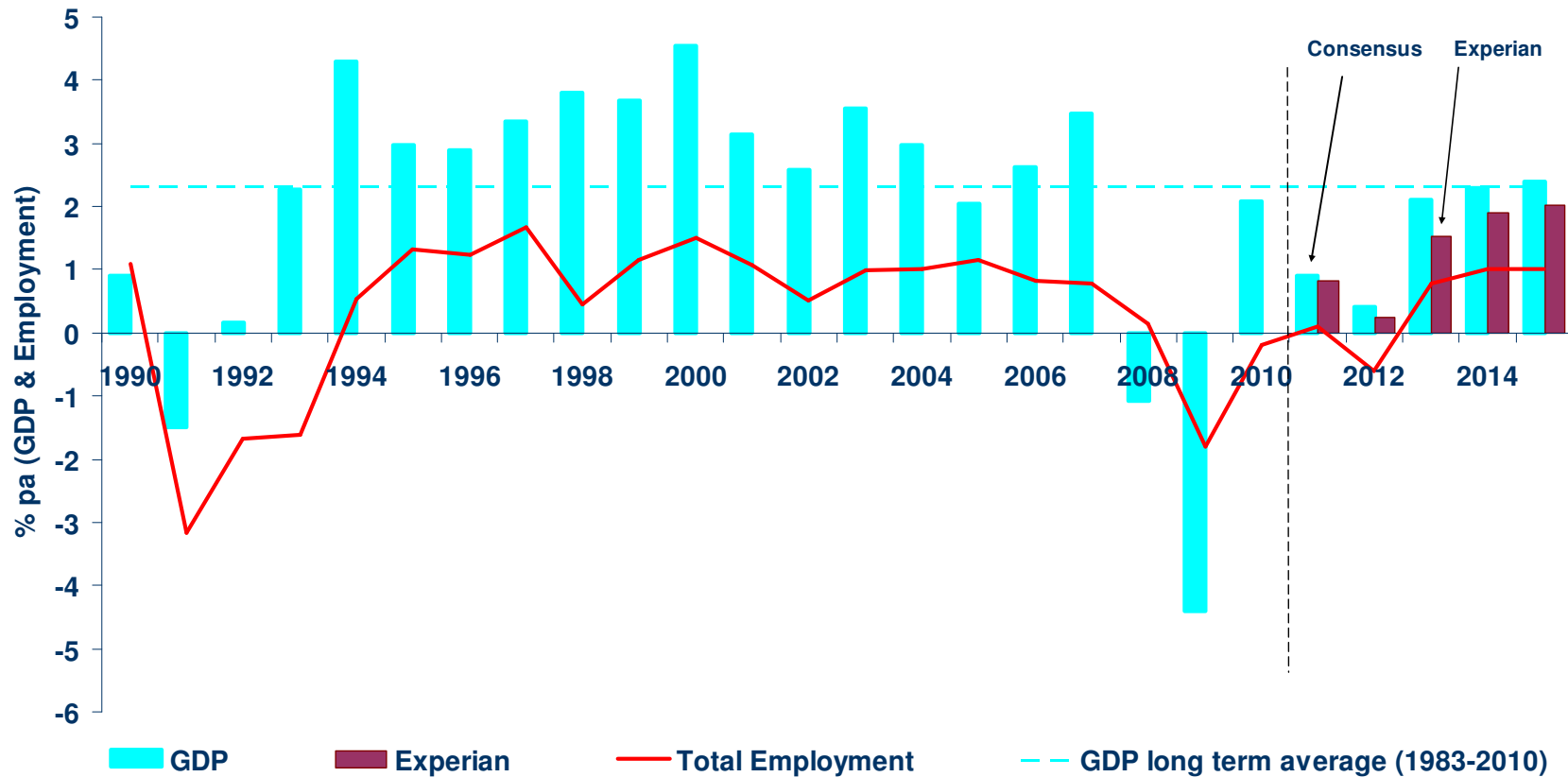




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# Economic Output & Employment Growth

- much weaker upturn than after 1990s recession





# Economic Outlook Summary

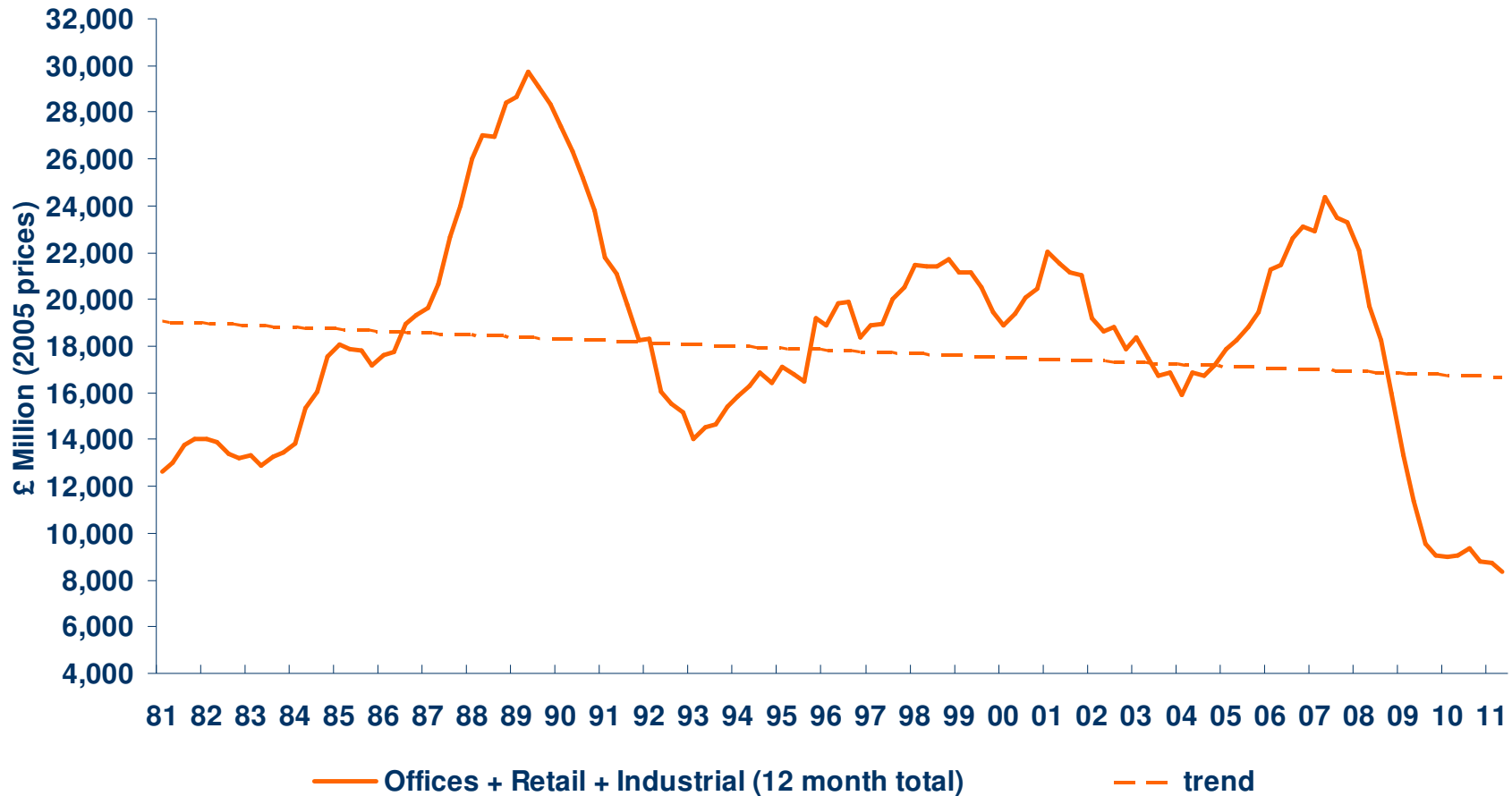
- Severe austerity package and growing eurozone crisis means very weak economy in 2012.
- Export led recovery impeded by weak economic growth in Europe.
- Inflation, although high, is falling and will fall further in 2012; real income growth will become much less negative. Base rate could remain at 0.5% throughout 2012 due to very weak economy.
- Bank lending remains limited and will only slowly increase.
- Property Occupier demand will remain muted and only improve slowly.



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# New Construction Orders (2005 prices)

- dramatic fall in new commercial development - worse than in each of the last two recessions; little sign of any improvement

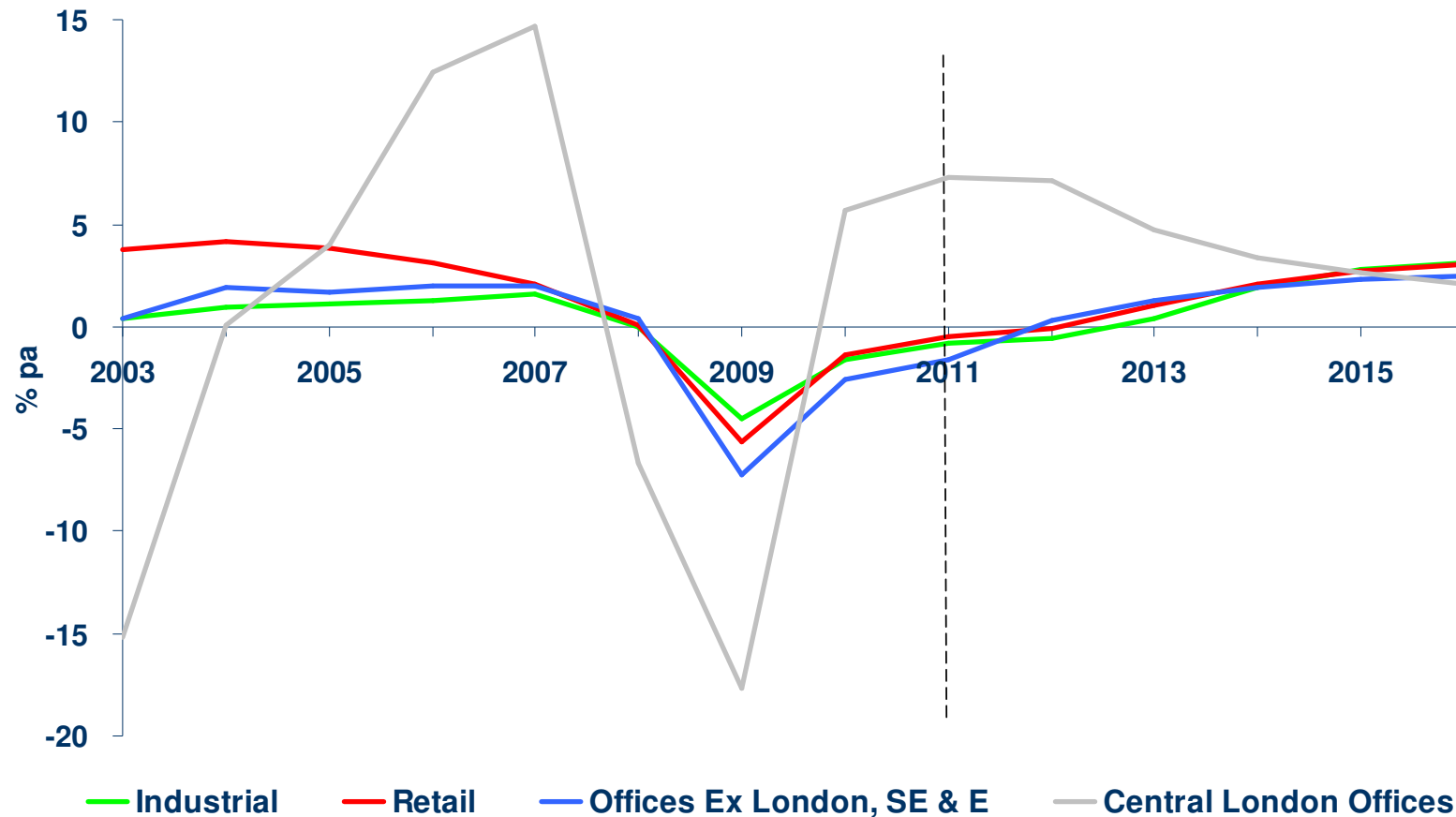




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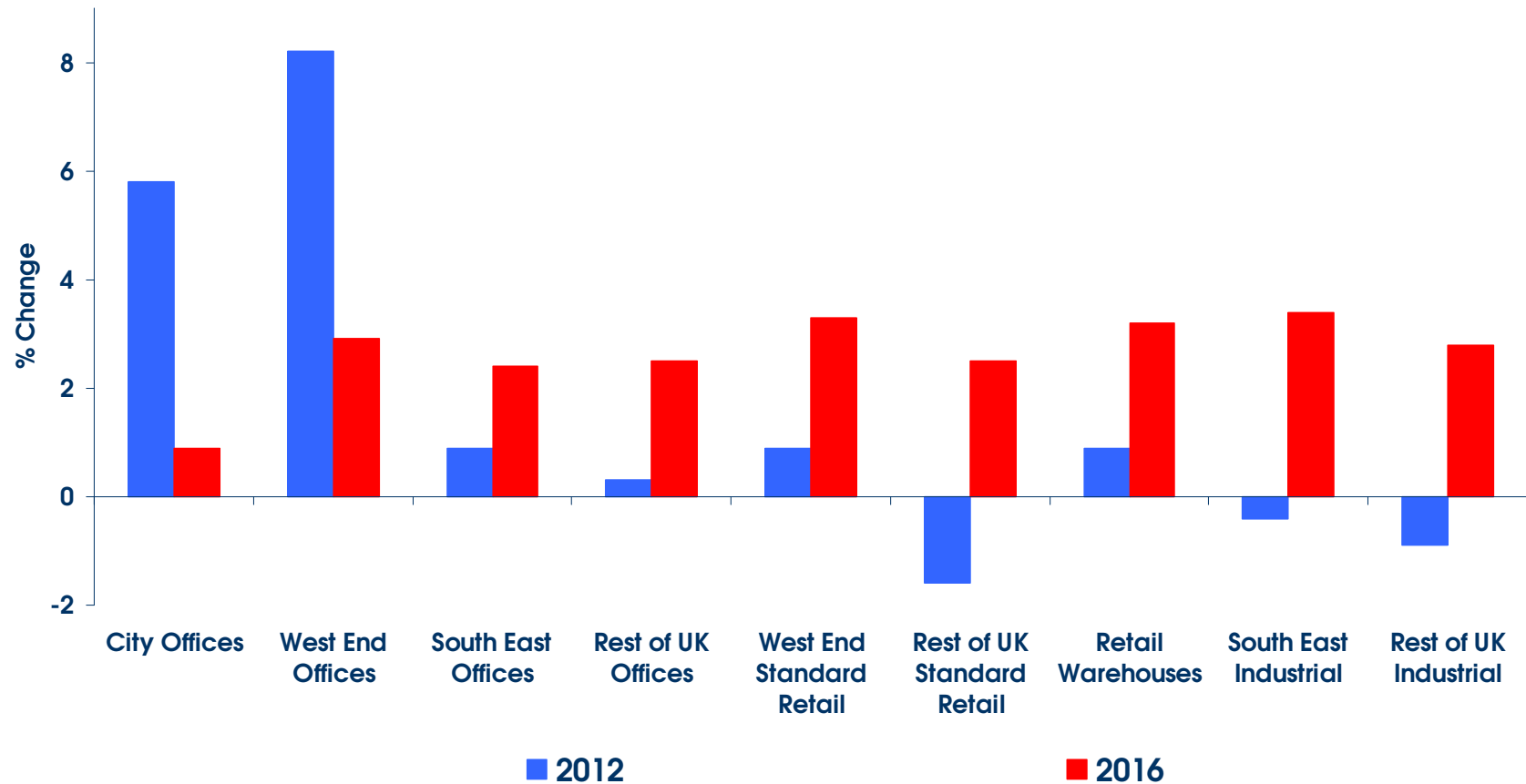
# Sector Rental Value growth

- strong upturn in central London, but not elsewhere; central London rental growth will weaken as new development completes from 2013 onwards



# Segment Rental Growth

-Large variation geographically in 2012 (central London dominant),  
but more similarity by 2016 when central London no longer dominant





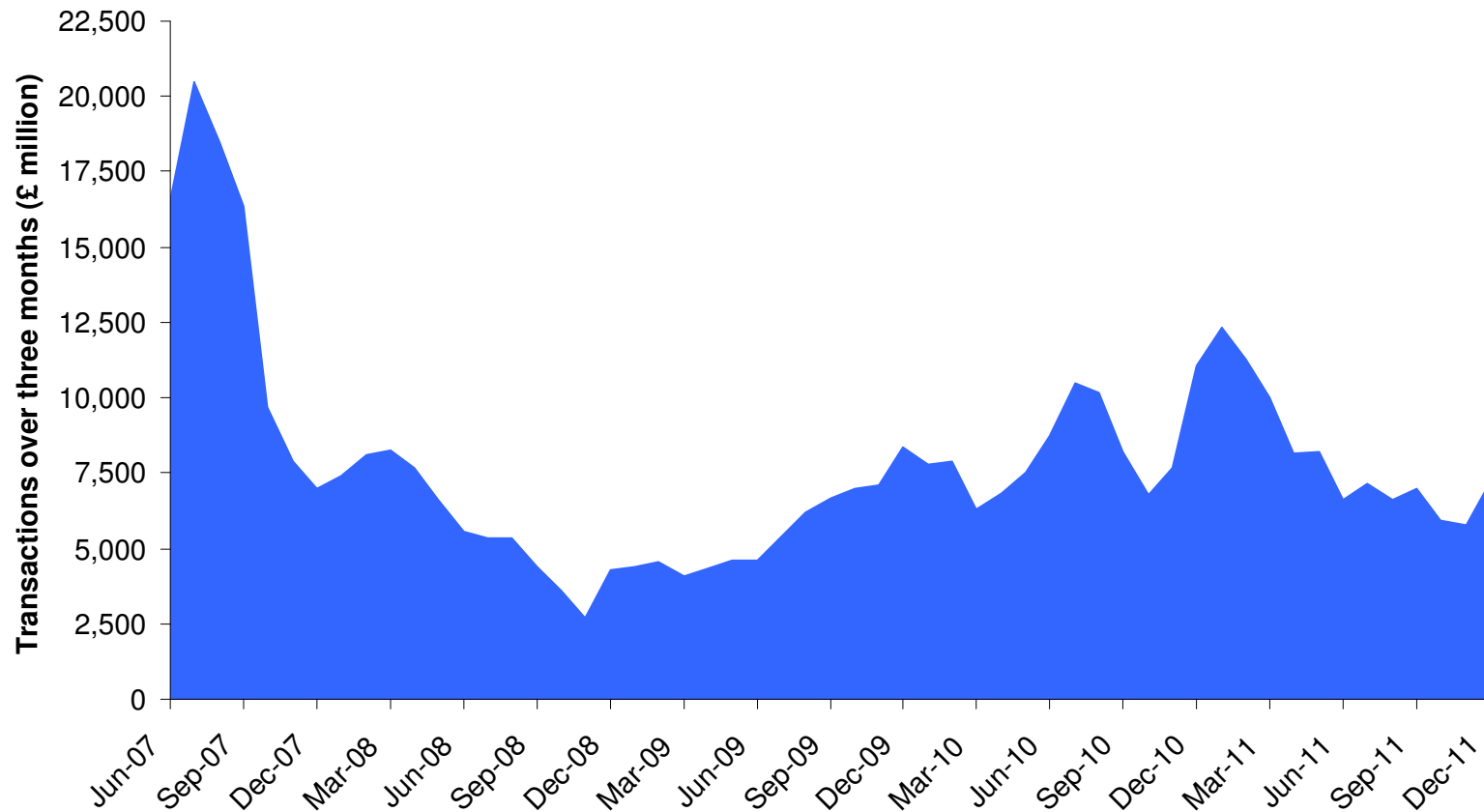
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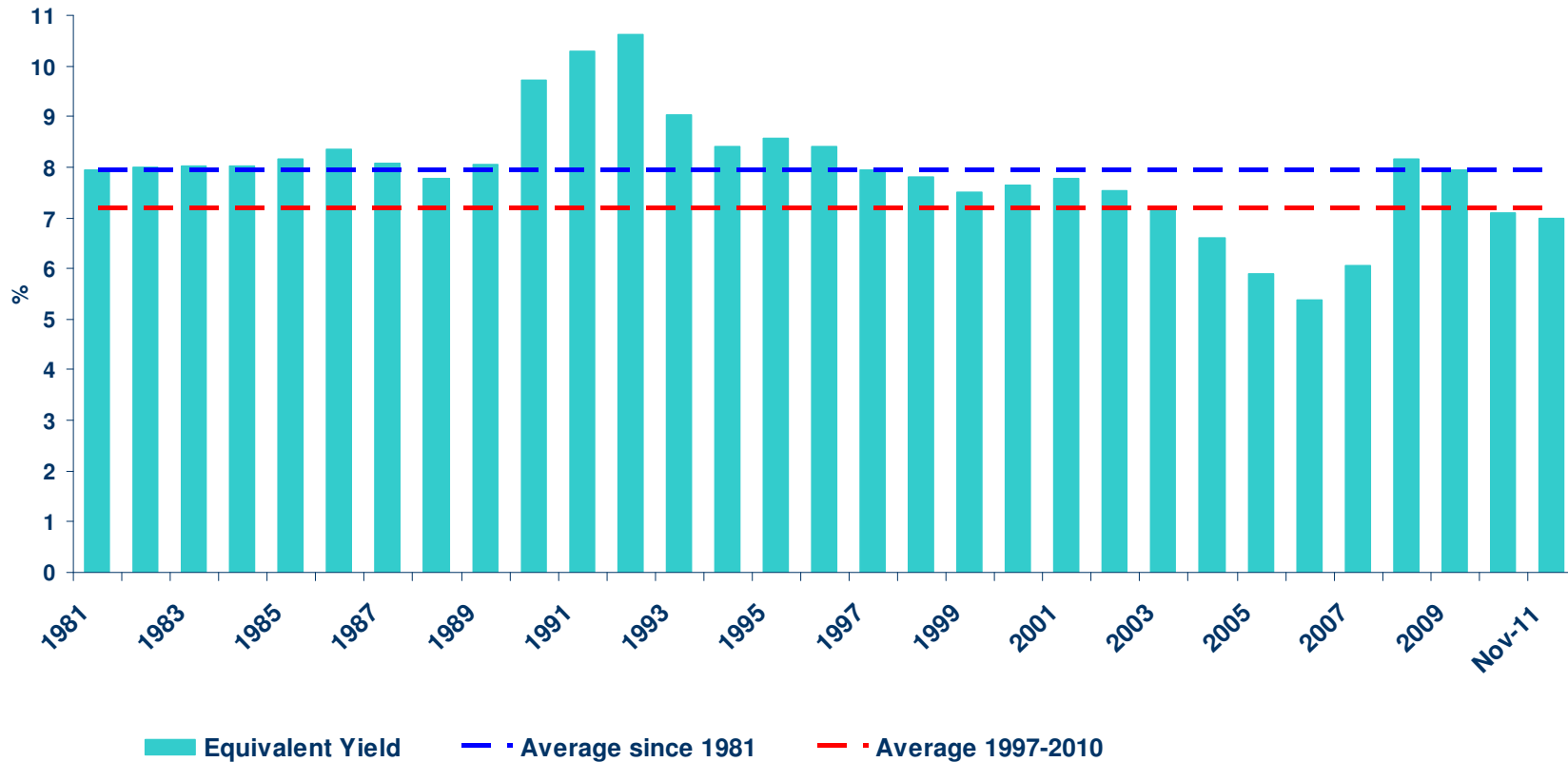
# Property Investment Transactions

-Volume of transactions has fallen back again in 2011



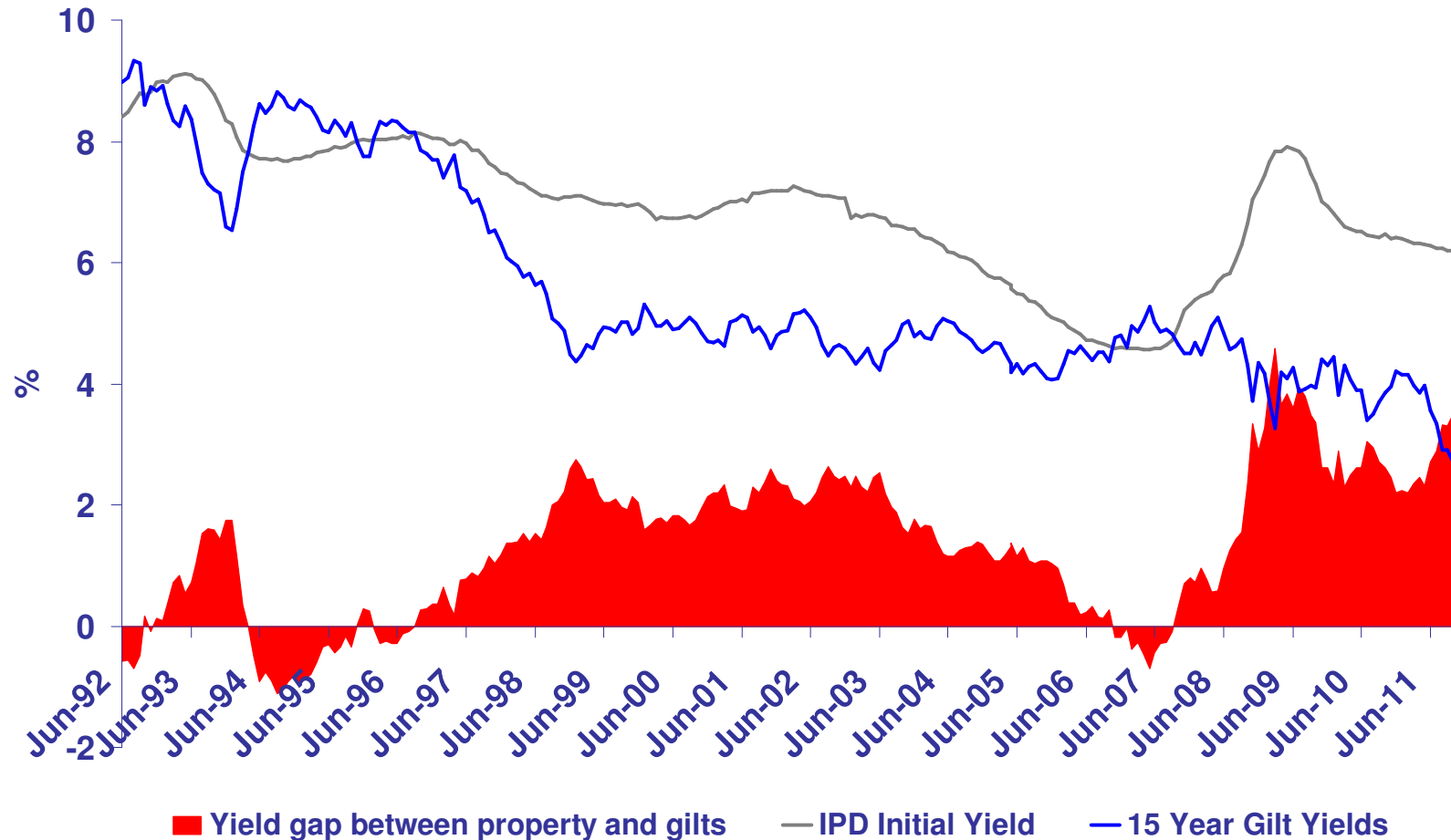
# Average Equivalent Yield

All Property nominal yields are now at or below long term average levels



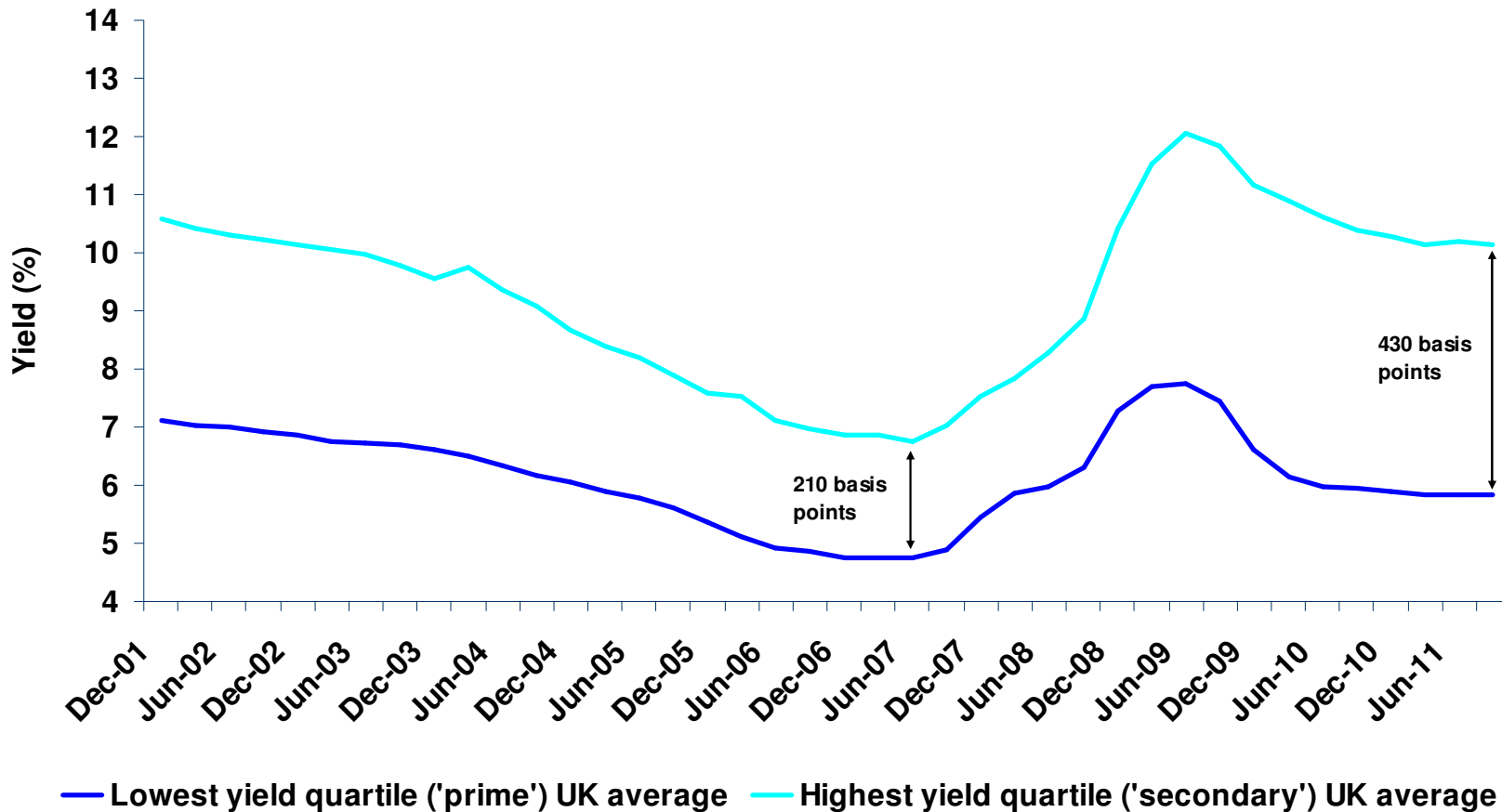
# Yields & interest rates (up to end Dec 2011)

- significant downward movement in property yields, but now stabilising and large fall in gilts, so still a large positive yield gap



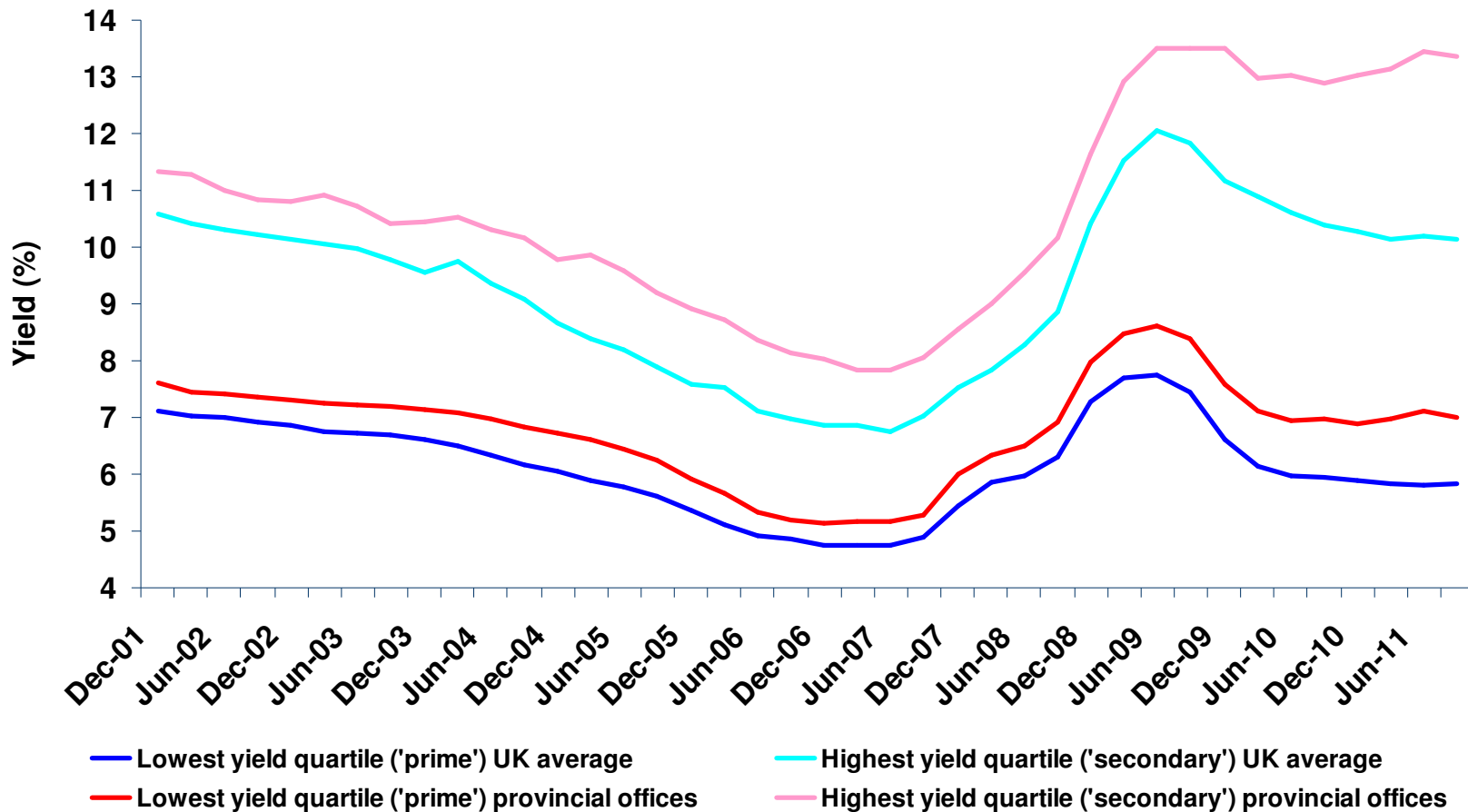
# Prime v secondary yields

-The gap between prime and secondary property yields has widened significantly



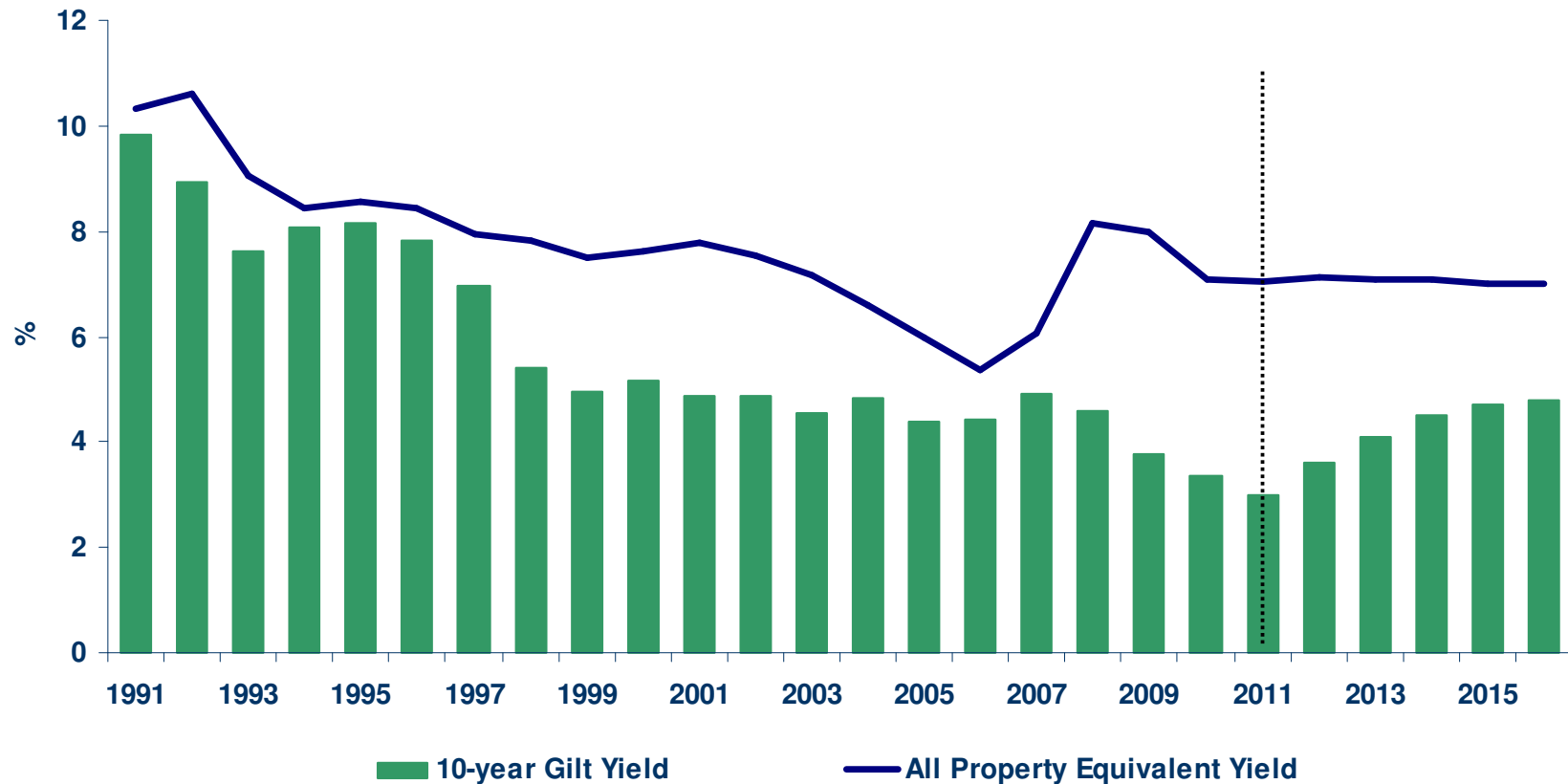
# Prime v secondary yields

-The gap between prime and secondary property yields has widened significantly, particularly for provincial offices



# Property equivalent yields & gilt yields

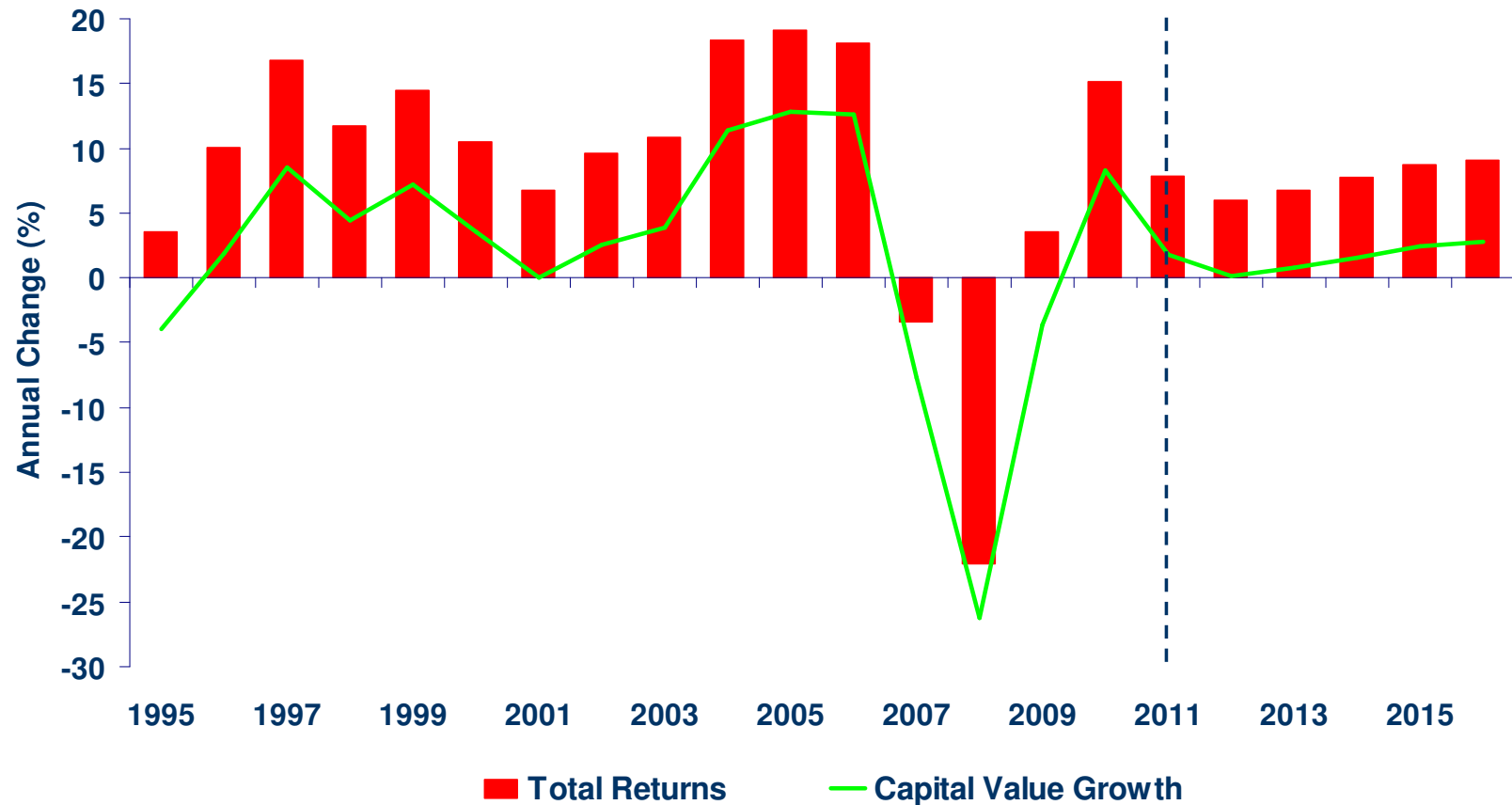
Current wide property yield gap over gilts could justify further property yield compression, but unlikely due to weak outlook for rental growth and likely increase in gilt yields



# Property returns & capital value growth

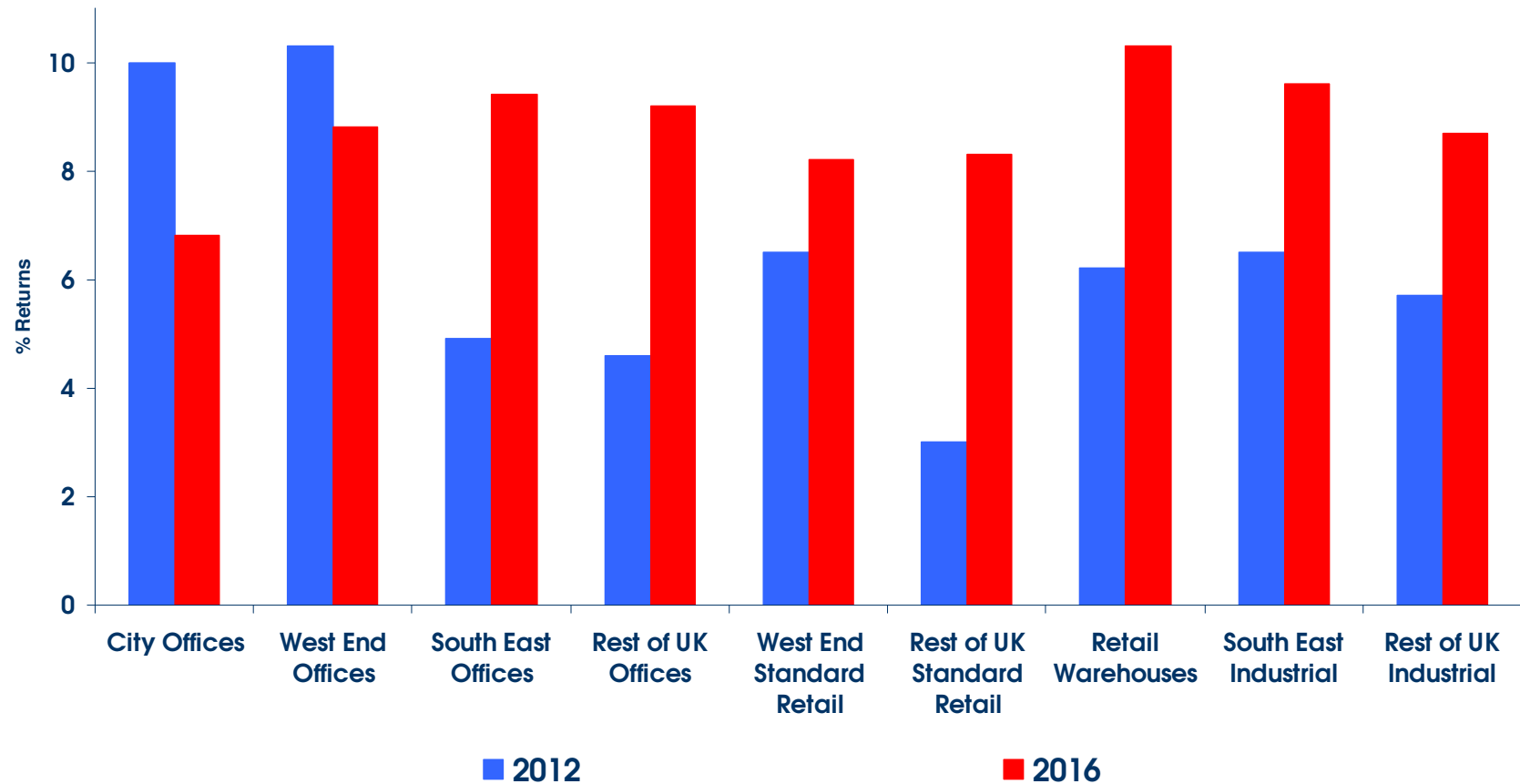


– Outlook is for 6-7% pa returns this year and next, rising to 8-9% pa in 2014-2016



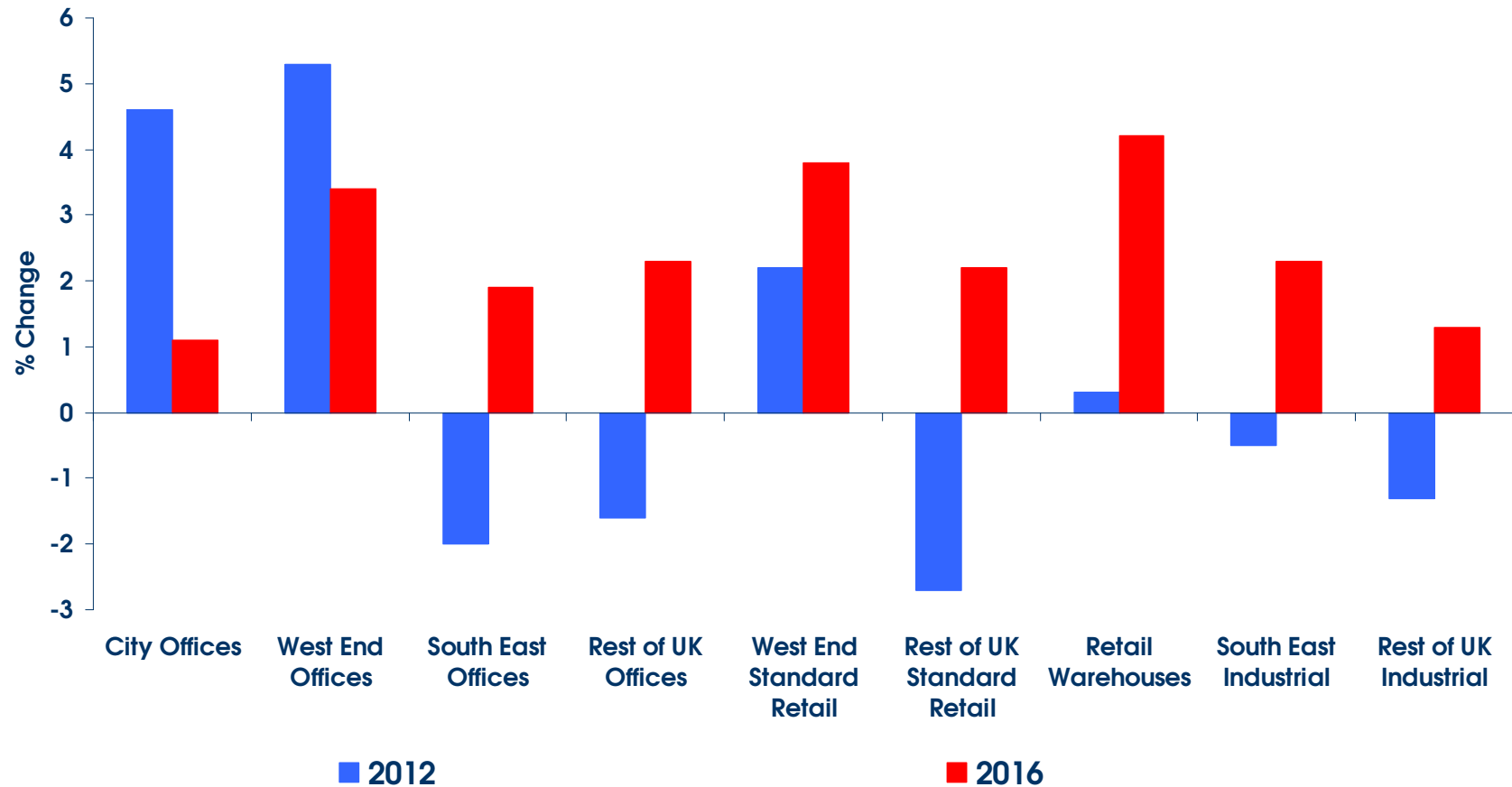
# Segment Returns

-Large variation geographically in 2012 (central London dominant),  
but more similarity by 2016 when central London no longer dominant



# Segment Capital Value Growth

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but more similarity by 2016 when central London no longer dominant





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## Conclusions – key points

- Rental growth little change in 2012
- Central London offices (& retail) slowing rental growth
- Capital values negative or close to zero growth in 2012.
- Widening difference between prime and poor secondary investments.
- Bank finance for property investment and development restricted for some years (but increased involvement by Funds)
- Long term outlook for property is fair
  - yields are historically lowish, but yield gap is large
  - capital values are close to trend levels
  - Lack of new development/supply
  - rental growth will slowly improve (after 2012)

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# Q & A

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