

Market Dynamics— Solutions for the UK and Elsewhere



Laurence J. McCabe, SIOR, FIAVI, FRICS, FSCS, MIREF, Knight Frank, Dublin, Ireland has more than 40 years experience in the property business and has gained expertise in a wide variety of property areas. He is currently a consultant with Knight Frank.

By Laurence McCabe, SIOR, FIAVI, FRICS, FSCS, MIREF

The concerted response of leading world governments to both the global banking crisis and the downturn in international property markets should help alleviate some of the daunting challenges facing brokers/agents around the world. Nevertheless members of the profession and their clients will need to work a lot harder and smarter to ensure that they not only survive the downturn but are also well positioned for the recovery when it comes.

Reduction in Interest Rates Key

The key benefit of the concerted effort has been the reductions in international interest rates. These record, low rates make it less attractive to hoard cash and more rewarding to invest in properties that offer yields as much as 50 percent higher than the market peaks two years ago. Such prospects have generated not only the attention of vulture capitalists but also of respectable institutions. Some German funds have been exploring places where they would least have been expected to invest, including Ireland. Already in the UK, we have seen some pension funds buying regional retail park properties at yields of more than nine percent. For prime London offices, my Knight Frank colleagues negotiated deals

at yields of between 5.75 and 6.12 percent in the spring of this year.

Signs of Stabilization Seen

These are among the tentative signs of stabilization in parts of the UK, most notably the London market. Furthermore UK transaction volumes remained flat in the first quarter of this year at £3.5 billion, although across Europe as a whole, transaction volumes fell by 30 percent to £11 billion in the first quarter of 2009. This suggests that the UK may be at a more advanced stage of correction, thanks partly to the depreciation of sterling, which had increased the attractiveness of the UK market for European investors. In contrast, commercial property activity in France fell by 70 percent to £800 million and in Germany by 50 percent to £1.7 billion.

Nevertheless, more deals can be done if both the vendors and the purchasers are satisfied that they are achieving a reasonable price in the circumstances. One of the challenges is how to set the scene as to provide an assurance about the reasonableness of the price.

Not Simply Buying and Selling

If only the property market were as simple as just buying and selling.

The old catch phrase of location, location, location is being replaced by the phrase, position, position, position, referring mainly, though not solely, to the financial positions of the tenant, the landlord, and their bankers.

At present, the old catch phrase of location, location, location is being replaced by the phrase, position, position, position, referring mainly, though not solely, to the financial positions of the tenant, the landlord, and their bankers. For an industry that has focused so much on bricks and mortar built on solid foundations in prime locations, the key parties now find themselves on shifting sands as their “funding” is transferred onto governments and others. At the same time, their tenants are at the mercy of falling trends in consumer spending and salaries while unemployment continues to rise.

In such uncertain territory brokers/agents must not only adopt imaginative plans for thinking outside the box but also adopt new approaches for convincing their clients to join them in such imaginative thinking. For many clients “risk-related”

thinking may be the last thing they expect when all of the indicators are flashing caution signals. Not that all clients need to engage in such imaginative approaches. Those who have solid portfolios of performing assets may need to do little more than ensure that they retain good relations with those tenants. Nevertheless, they will need to ensure that prized tenants are not being enticed away by distressed competitors.

Making Concessions to Current Tenants

In the cases where tenants are finding it difficult to pay agreed rent increases, some landlords need to accept that some rent is better than none. It may also be necessary to reduce the periods for rent reviews from five years to one year.

Those brokers/agents who have solely concentrated on the prime sectors of the markets may need to consider advising their clients to look at other sectors, especially if their clients are developers. It may also be necessary to motivate target prospects with incentives such as rent-free periods or management support.

The key to many aspects of successful management of the recession, including relations with tenants who are considered blue-chip covenants, is to adopt a longer-term perspective.

A long view is also necessary when reviewing plans for new developments. For instance, in locations that are suffering from an over-supply of housing or hotel

accommodations, developers might consider the potential demand and economic viability for alternative uses such as healthcare facilities or nursing homes. In addition, one market sector that is often overlooked is that of religion. Although we are all familiar with the major landmark churches and schools that the major religious organizations have developed over the centuries, immigrant groups and others are not as concerned about competing in terms of trophy designs and are willing to consider alternatives. They may be willing to take upper floors in older city center locations, or even warehouses in industrial estates.

In addition, brokers/agents may find it necessary to counsel their seller clients advising them to accept offers that may be less than the prices at which the client acquired the property.

In such cases, brokers/agents may well feel pangs of guilt and may be reluctant to offer such advice when they were not at all hesitant in facilitating the purchase. Nevertheless, the brokers/agents now have to act in the client’s best interest, and an early sale may be more advisable when the funds raised from that sale can protect the creditworthiness of the client. Brokers/agents may find it easier to convince clients of the need to sell if they combine such advice with specific alternative investment opportunities for any residual equity.

Clients’ Best Interests Paramount

The key to convincing anyone to do anything in this current market is to undertake a comprehensive assessment of the client’s existing and future business prospects. This is the foundation for ensuring that brokers/agents do their best to protect and advance their clients’ best interests. 

