We revisit the core themes from our 2020 London Report, examining their importance in the wake of COVID-19

COVID-19 SERIES

REVISITING THE 2020 LONDON REPORT

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REVISITING THE 2020 LONDON REPORT

Over the next few pages we reassesses the findings of our recently launched 2020 London Report and examine why the pandemic is set to hasten the city's evolution already occurring post-Brexit

This year's London Report was set against a backdrop of political stasis, precipitated by the seemingly never ending Brexit saga.

Despite the drag on economic confidence, London's commercial office market has demonstrated resilience. In part, this resilience boils down to basic market fundamentals: diverse and robust demand from businesses, led by finance and banking, professional services, tech and flexible office providers; and yields which outstrip most global bond offerings and, indeed, most major European gateway cities.

Still, while the UK may have formally Brexited on 31 January, a further test awaits UK plc in the lead up to the end of our transition period with EU, which is still due, Covid-19 notwithstanding, to terminate at the end of December.

It was against this backdrop that we coined the term reLondon. We defined this as a process that the British capital has undergone periodically in its near 1,000 year history, constantly reinventing and repositioning itself as a global magnet for businesses, investors and people. We felt this would be particularly apt for London in the new "twenties" as the city jostles for centre stage in our post-Brexit world.

And then the unthinkable happened. A crisis of epic proportions, stemming not from a faltering global financial system, but from an invisible threat. COVID-19 has disrupted humanity in a way that has not been seen for a generation and threatens to deliver the worst economic fall-out we have ever seen. Against this seemingly insurmountable battle, reLondon has never felt more apt.

Three of the four sub-themes we identified from the core reLondon concept almost feel like they've been elevated by the current situation and are now more relevant than ever:

- Reprioritising customers
- Reenergising demand
- Reimagining space

REPRIORITISING CUSTOMERS

The results of our 2020 London Landlord and Investor Survey can be distilled into three key areas of focus: services, amenities and experiences, all of which revolve around the way in which we are using office space. The office has a newly elevated status in the minds of businesses as a tool in the war for talent.

The traditional office has already transformed itself beyond recognition in the last decade. It has become a place that stimulates the mind, promoting mental wellbeing, a place where we come together to innovate and collaborate – all of which is unlikely to change.

We have come to develop very different expectations of our workplace. Landlords, developers and businesses have responded, delivering first class offices, with amenities including flexible meeting spaces, yoga terraces and end of trip facilities. The result? A happier workforce and a magnet for talent.

Best-in-class space

For a market like London where the office market has been supply starved for the better part of ten years, businesses have been racing to pre-let space to house future employees and to ensure they're in best-in-class space.

If the last few weeks have taught us anything, the much touted "death of the office" concept couldn't be further away from the truth. Granted that the daily commute may no longer appeal to all staff and occupational densities may need to be revisited once things normalise, but the need for a central hub and formal work environment has been overwhelmingly reconfirmed by our enforced remote working.

Furthermore, in the context of London, amenity rich locations such as the City and West End play a key role in helping make places attractive to businesses. In fact, in the West End, where 41% of floor plates are under 5,000 sq ft, businesses are often reliant on their surroundings to provide the amenities and experiences staff now seek, due to space limitations.

The traditional office has already transformed itself beyond recognition in the last decade.

Indeed, our Landlord and Investor Survey saw services and amenities being ranked as the second most significant real estate related consideration.

London's agglomeration benefits, hard to rival culture and a rich talent pool provides businesses with a strong platform for success, but it's the amenities and experiences available either within, or surrounding schemes that have become highly sought commodities that we all rely upon to enrich our working day; something that isn't necessarily available to all of us working remotely.

Thinking about this emergent and rapidly norming customer centric approach in the current climate, partnerships between landlords and businesses will be critical at this time as they work together to develop new rental payment plans and timelines.

Rent holidays

Cash flow pressures stemming from slowing economic growth have resulted in a rise in rent holiday requests, a trend picked up by our own sentiment indicators.

The COVID-19 pandemic happens at a time of record high London office rents, so this is perhaps unsurprising. The government's emergency Corona Virus Bill effectively grants a moratorium on forfeiture until 30 June, which offers some temporarily relief.

The Bill effectively means that tenants are not obliged to pay rent until the end of June. They are however still liable for the missed rental payments in the future. As a result of this and financial pressures, there have already been a number of instances of non-payment of rents in London's office market.

41%

OF FLOOR PLATES IN THE WEST END, ARE UNDER 5,000 SQ FT

REENERGISING DEMAND

Our second theme, re-energising demand, looks at how London is expected to resume its position as the world's most liquid and attractive investment market, after being usurped by Paris in the wake of the Brexit referendum.

With signs of long term investment strategies remaining in play, London appears to be assuming its position as a trusted global safe haven. The biggest challenge for investors of course will be the far reaching travel restrictions that has seen countries close their borders and ground airlines, which clearly will hamper property inspections. This is particularly important for London given that 75% of investment was from overseas in 2019.

Our Global Capital Tracker, launched at the beginning of February showed £48.4 billion waiting to deploy in London's office market from around the world (up 21% y/y). The volume of capital chasing assets in London may well become further supercharged, depending on the length and depth of COVID-19's impact on the global economy.

Office investment

There was £2.6bn of investment in London's office market in Q1 2020. This is down on the long-term average of £3.4bn. It was always going to be difficult for the market to top the £4.6bn registered in Q4 2019, when a surge followed the decisive result of the General Election.

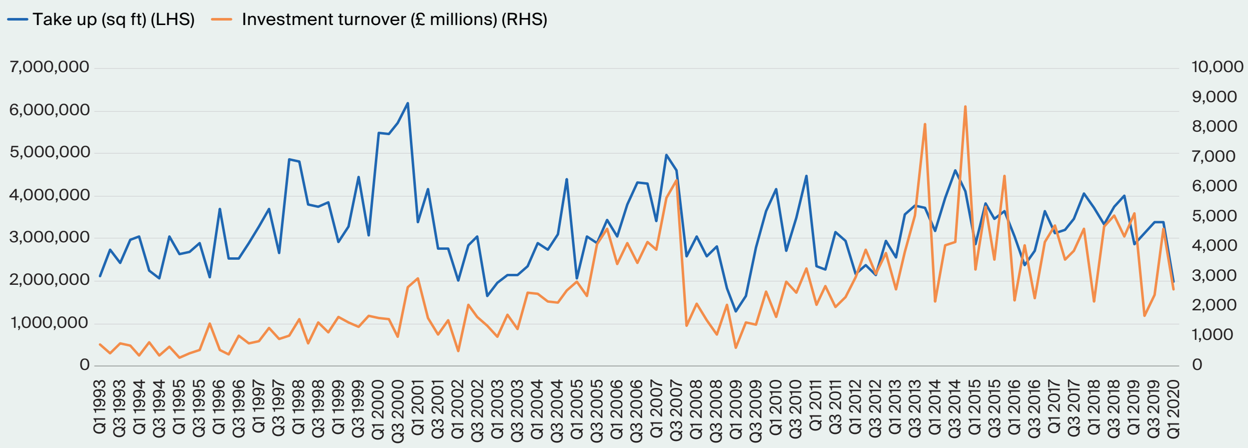
London appears to be assuming its position as a trusted global safe haven.

The decline in investment volumes in Q1 has in part been exacerbated by a distinct lack of investment grade stock, but weakened investor sentiment as the COVID-19 story plays out has also impacted on demand, particularly from international investors. Indeed our Agent Sentiment Survey has shown a rise in the number deals being aborted, or put on hold.

Certain investor groups are comfortable making off-plan purchases, particularly with residential property. Whether this extends to commercial office acquisitions remains to be seen and will, we suspect, depend on the need to deploy capital into safe havens like London in the wake of any economic contagion as a result of the COVID-19 pandemic.

£2.6bn
OF INVESTMENT IN LONDON'S OFFICE MARKET IN Q1 2020

London office market performance



Source: Knight Frank

REIMAGINING SPACE

Our third and final theme was inspired by the global "green" reawakening and here we investigated why the green agenda has risen up board room agendas so quickly.

Aside from legislative pressures that include consultations on making all commercial buildings in the UK EPC-rated by 2030 and plans for the UK to go carbon-neutral by 2050, the human element is also equally important.

The war for talent means businesses are turning to their green credentials and the green credentials of the space they occupy to differentiate themselves from the competition and as a way to appeal to the next generation of the workforce.

The biggest opportunity will lie in transforming 'ungreen' assets and saving them from inevitable obsolescence as businesses, talent and investors shy away from those that have the potential to hurt our environment.

Low-carbon future

Take BP for instance. Their new CEO, Bernard Looney recently announced sweeping changes to the 111-year-old petrochemical firm's business model, shifting its focus to lower-carbon energy.

Not only that, but there is a commitment for the business to go carbon neutral by 2050 as well and that includes emissions from vehicles buying fuel from BP forecourts around the world. Ambitious? Yes. Do-able? Tbc.

The main point here is around messaging. By greening the business ethos in such a way sends a very strong signal out to the workforce of tomorrow, who we all know are incredibly green conscious.

When it comes to green office space, we have 3,000 BREAAM buildings in London, creating rich pickings for those investors and businesses after something greener. The biggest opportunity however will lie in transforming 'ungreen' assets and saving them from inevitable obsolescence as businesses, talent and investors shy away from those that have the potential to hurt our environment.

Almost 65% of London's commercial buildings were completed prior to the year 2000. Notwithstanding refurbishments over the last 20 years, there will be plenty of rewarding 'greening' opportunities in London for landlords and investors.

3,000
BREAAM BUILDINGS IN LONDON

Together, these three themes represent issues that transcend short term economic and geopolitical challenges. Even the unprecedented COVID-19 crisis will not deflate the collective momentum that has been built around improving our wellbeing through the spaces we occupy, work from and live in.

FAISAL DURRANI - HEAD OF LONDON COMMERCIAL RESEARCH

To learn more about these themes and what they mean for the future of London, please visit **www.knightfrank.com/londonreport**

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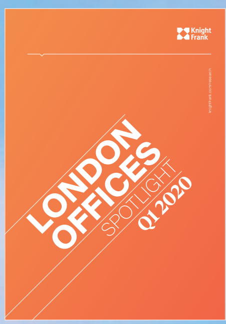

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