



Find *the* Gap

UK Residential Forecasts
London focus

UK Residential Research | October 2018

Urban living, your way.





UK Residential Forecasts

The UK economic and political landscape has been dominated by Brexit over the past 2½ years. The next 2½ years are likely to be similar, albeit dealing with a different phase of the process.

Inevitably, the UK will collectively refocus attention on domestic policies as the sphere of influence from Brexit diminishes.

And there are plenty of housing issues that need addressing. These include affordability, taxation, regulation in the private rental sector, affordable homes, housing supply, lack of skilled labour and digital construction.

Our housing market forecasts for the next five years assume that a Brexit deal is hammered out over the coming months and that we have a transition period until the end of 2020.

During this time, greater political certainty will instil renewed confidence to UK businesses and consumers leading to improved housing markets.

But residential markets will take time to pick themselves up from current lows. Our housing market forecasts predict a steady recovery, with some London markets receiving an additional bounce-back boost.

Within this there will be geographical winners and losers. There will also be some sectors of the wider residential market that will present opportunities while others will look less inviting.

So, it will be important to 'Find the Gap' rather than to blindly back residential in its broadest sense.



Adam Challis
Residential Research



Neil Chegwiddden
Residential Research

“Won’t it be refreshing to focus on these key housing issues without Brexit poking its nose in every five minutes?”

Find the Gap

Reasons to be cheerful

It's easy to be cynical these days in the UK and no doubt many housing market participants have been spending a disproportionate amount of time this year modelling downside risk for the years ahead.

In a world of uncertainty, more so than normal, it would be easy to wallow with indecision and pull back on development programmes. So, credit where due, the housebuilding community has stepped up production. Net new additions in England increased by 15% in the year 2016-17. In London the increase was 30%.

However, the outlook for development is not as positive. Development starts in Greater London during Q3 2018, for example, slowed to their lowest level since 2012. This is bad news for just about everyone. But, rather than join the gloom it is worth taking a contrarian position for a moment. Not just because being optimistic is an agent's prerogative but because, when the mist clears, the market backdrop should present more positives than negatives.

Make no mistake, JLL sees every reason to expect a hard couple of years for the industry. The confluence of factors we noted in last year's forecast statement – with upward pressure on costs to both builders and buyers, and very little escape through rising prices or incomes – will plague the 'business as usual' approach to delivery. But land values will adjust, real incomes will nudge upwards and the majority of the industry will solemnly trudge forward.

Yet, there are also reasons to see a more optimistic picture, too.

Homes England

The Government's housing delivery unit is really beginning to ramp up activity. It is determined to help to build 300,000 homes a year by the mid-2020s while the majority of the £1bn initial short-term fund to assist SMEs has already been allocated. A further £1.5bn of short-term funding has been added to complement the £2bn long-term fund.

It will invariably be plagued by public criticisms for Help to Buy, but will have no choice other than to carry on with a more refined version of the programme.

The industry has an unhealthy addiction to 'Help to Buy induced demand', yet for all the criticism it has been undeniably successful in getting more homes built more quickly.

More importantly, Homes England has been retooled and is pushing on with the hugely ambitious supply programme that is underpinned by the three pillars of quality, quantity and pace.

It is more nimble and innovative with solutions, with an emerging track record of doing some big and creative deals.

This really is a golden age for the organisation and the industry should be beating down the doors at Windsor House to bring ideas forward.

Infrastructure

The UK is creeping towards a new era of infrastructure. HS2, HS3, Crossrail 1, Crossrail 2; these are all important catalysts for new housing sites and induced demand. Where tied to a structured housing delivery outcome, or linked to delayed/lower land payments, things will get done.

Despite their scale however, none of these will be as important to housing delivery as CaMkOx, or the Varsity Arc, that connects the UK's two great institutions of higher learning. Over one million homes are planned for this region, connected by both rail and dual carriageways. In truth, the arguments for connecting Oxford and Cambridge are weak, but the local and regional linkages with London will drive a wave of sustained community building for several decades.

Digital disruption

This is a bit of a catchall for the wave of 4th industrial revolution technologies that will gain both momentum and adoption over the next five years. Digital construction will mainstream. BIM will transform the relationship between supply chains, contractors and developers.

Smart technologies will enable better, more nuanced relationships with buying customers and renting residents. These are all statements of the obvious and if you are still a sceptic, just think back to what any of this meant to you only five years ago.

“It is less about stepping off onto the platform and more about stepping on board.”

But we believe the big changes will come towards the end of the forecast period, when off-site manufacturers achieve scale, when multi-family operators have built genuine brand-driven followings, and when consumers have normalised the benefits of these technologies. To get there, adoption and investment starts now.

The 52%

Lest it hasn't been said enough times, the end of the Article 50 period and beginning of the UK's brave new, independent world, will be welcomed by a majority of the population.

This is not just relief that the cross-channel tit for tat is over, but across major swathes of the UK and away from the London bubble, it will be welcomed

as a good thing. Do not underestimate that shift in sentiment. You don't need to like it to want to make the best of it and the implications remain at this stage, largely an unknown.

However, it is worth stating again – a majority of the population (or at least a large minority these days) is looking forward to independent Britain and this may well trickle into stronger consumer sentiment. Stranger things have happened.

Find the Gap

These are all big, structural changes for the housing industry. So, Find the Gap is a way of reframing the risks of a Mind the Gap perspective. The challenges are broad-based and well-known.

At the same time, there are several very large pillars to support new opportunities for the housing sector. They may require a shift out of traditional comfort zones to embrace new markets or new technologies, but they are undoubtedly there for the taking.



Brexit risks & assumptions

Battling through Brexit

With so much uncertainty, so many potential stumbling blocks and a myriad of possible outcomes, the economic and political outlook is not clear.

Here we set out the most likely outturns, discuss the hoops that need to be jumped through and settle on the Brexit assumptions we will make in our economic and housing market forecasts.

A deal most likely

While there are several potential scenarios and routes, as well as the possibility of a 'no deal', we believe that the most likely outcome is that the UK does agree a deal with the EU.

The main reasons for this are that it is in the interests of both the EU and the UK, and that the 'cliff-edge' or 'no deal' route is highly undesirable for all concerned, but particularly for the UK. Polls continue to suggest this is the most likely of the range of outcomes on the table.

What kind of deal?

The two most likely possibilities represent opposite ends of the deal scale.

The first is a soft Brexit whereby the UK accepts the four freedoms of the EU, continues to trade with the EU similar to today, but has no say in the regulations that it needs to abide by. The current Chequers plan would fall under the 'Brexit in Name Only' (BINO) heading, albeit a plan that the EU has rejected.

The other most likely scenario is that the UK and EU agree to trade under WTO (World Trade Organisation) rules after the transition process. Ultimately this is similar to a 'no deal' outcome, but in this scenario, there is a transition period during which many potential issues are ironed out, thereby avoiding a 'cliff-edge' situation.

Obstacles

There are many obstacles to overcome before any kind of decision can be made and agreed – deal or no deal.

Without contemplating exactly how each might arise, the hoops to jump through are Conservative Party approval, Parliamentary consent and EU agreement.

Depending on the outcome of each, other hoops and obstacles might arise. These could include a Conservative leadership contest, a General Election and a second referendum.

Timetable disruption

With all of these issues at play, and the lack of progress to date, it is quite likely that the current timetable will be disrupted.

This could be a postponing of the March 2019 exit, an altering of the length of the transition period or the EU delaying the approval of the proposed plan.

If any of these outcomes were to be realised, the prolonged uncertainty would drag on the UK's economic performance.

JLL assumptions

For the purpose of generating a base case housing market forecast, we assume that the UK will agree some kind of deal with the EU. The implications are that UK economic performance will recover reasonably well over the course of the next five years.

We also assume that UK economic weakness lasts for much of 2019, but is in recovery mode during 2020. This would arise as greater certainty returns, but does not necessarily mean there are no delays to the existing timetable.

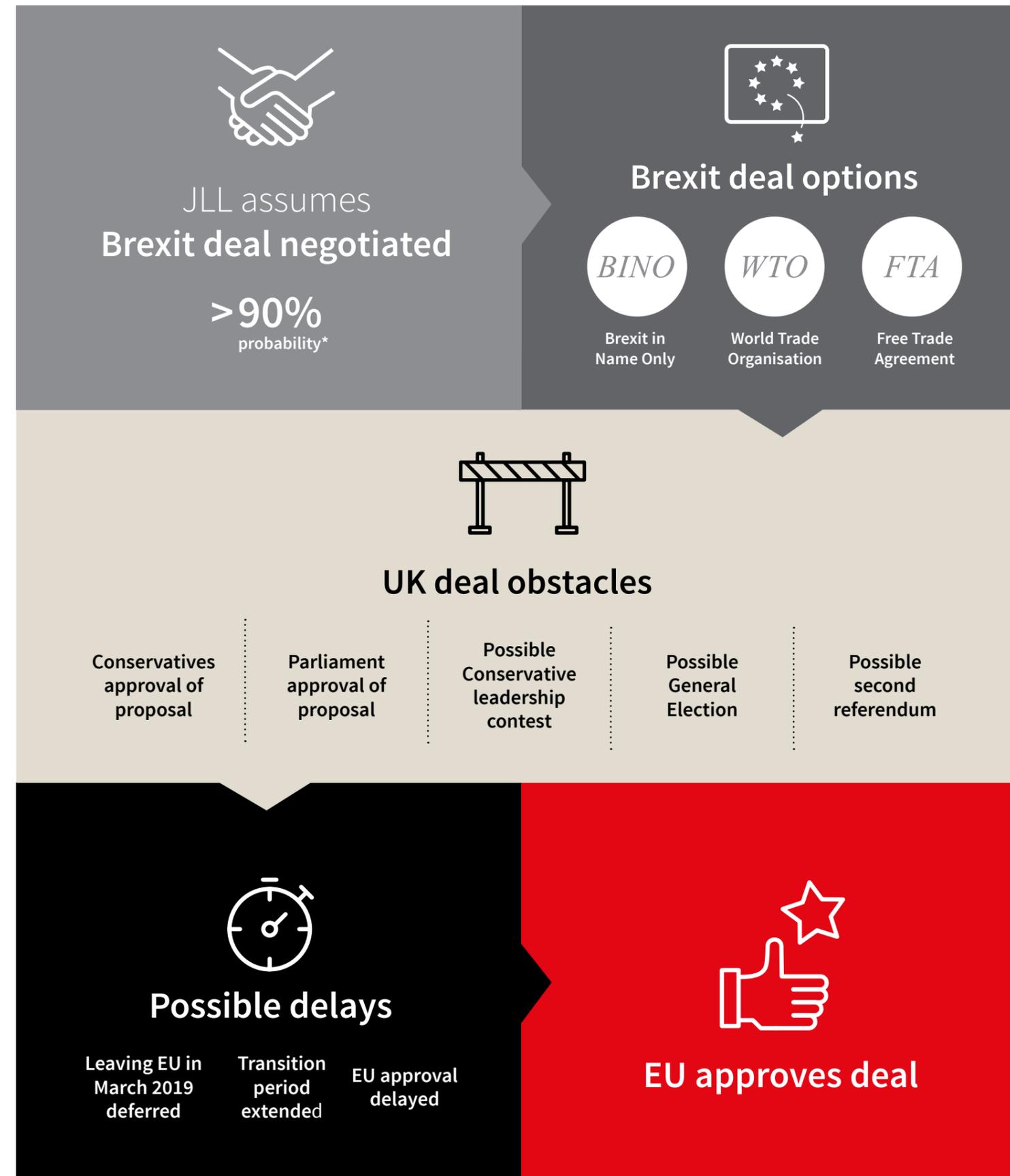
Forecast risks

The main risk to our assumptions is that UK economic weakness is prolonged by a year or two. This would result in lower UK GDP growth in 2020 and perhaps also in 2021. Sterling would also remain weaker for longer.

The second most likely risk is that the Brexit deal negotiated and approved is not as favourable for the UK as we assume. This would still result in an economic recovery, but a weaker upturn after 2019 compared with our base case assumptions.

The third risk is that the UK exits the EU with no deal. And whilst we deem this to have a probability of less than 10% at present, it would result in a far weaker UK economy over the next five years.

JLL base case forecast assumptions



* Probability of no deal estimated at <10%, JLL estimate

UK economic forecasts

Assumptions

Our base case Brexit assumptions are that some kind of deal is agreed with the EU, in principle at least, with transition arrangements lasting until the end of 2020. Given this relatively stable outcome, we expect the UK economy to steadily improve during 2019 from its current low, before strengthening further over the following four years.

UK economic growth

UK GDP growth is expected to be around 1.5% in 2019. Importantly, this will be a marked improvement on 2018 as the uncertainty that has sapped both business and consumer confidence dissipates on news that a Brexit deal has been reached.

The greater certainty delivered by the deal will fuel improved UK confidence. Economic output in the form of business output, expenditure and investment as well as higher consumer spending will all drive an economic revival.

However, because any deal will not be as favourable for the UK as the existing trading conditions, economic output growth will be slightly below the norm and lower than typical economic recovery growth rates.

Annual GDP growth is then expected to hit 2.0% in 2020 and 2.2% in the year after the managed transition period ends. GDP growth will then ease back to circa 2% pa in 2022 and 2023.

Jobs and earnings

UK earnings growth is forecast to return to a more normal rate of 4.0% pa following several years of subdued growth. The improved employment and wages outlook will be important for housing market confidence and affordability.

The heightened wage growth is predicted to be even more influential for the housing market over the next five years because CPI inflation is forecast to be around 1.6% pa during the next three years before rising to 1.9% pa by 2023. This will give households greater disposable income and spending power.

Employment levels are expected to remain high despite the current economic and political uncertainty, with the unemployment rate remaining at a record of just 4.0% of the workforce.

Interest rates

With the economy on the road to recovery over the next few years, the bank rate will increase steadily and incrementally.

No more bank rate rises are expected in 2018 but rates should rise to 1.00% by the end of 2019 once the Brexit outlook has become clearer.

By the end of our forecast period in 2023 the bank rate is still only expected to be at 2.75% as rate rises are contained in order to encourage and boost economic growth and stability.

Exchange rate

The strength of sterling will be keenly watched over the next five years as a bellwether to how the UK is viewed post-Brexit.

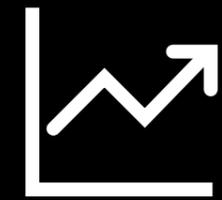
The pound is expected to strengthen to circa US\$1.41 by end-2019 before rising to US\$1.50 by end-2023. Against the Euro, the pound is forecast to strengthen and then remain at €1.20 through to end-2023.

Source: Oxford Economics



GDP growth (% pa)

2019	2020	2021	2022	2023
1.5%	2.0%	2.2%	2.1%	2.0%



CPI inflation (% pa)

2019	2020	2021	2022	2023
1.6%	1.6%	1.6%	1.8%	1.9%



Unemployment rate (%)

2019	2020	2021	2022	2023
4.0%	4.0%	4.0%	4.0%	4.0%



Earnings growth (% pa)

2019	2020	2021	2022	2023
3.2%	4.0%	4.1%	4.1%	3.9%



Bank rate (% pa)

2019	2020	2021	2022	2023
1.00%	1.50%	1.75%	2.25%	2.75%



Exchange rate (£/US\$)

2019	2020	2021	2022	2023
1.41	1.46	1.50	1.50	1.50

UK housing market forecasts

Forecast rationale

The assumptions used to generate our base case UK housing market forecasts are that the UK agrees a deal with the EU on Brexit and that the UK economy recovers to circa 2% pa GDP growth during 2020-2023.

Within this broad Brexit and economic environment there are several other factors that will influence the UK housing market.

Consumer confidence is key

Consumer confidence is a critical driver of the housing market. The uncertainty surrounding Brexit has dented consumer confidence while also casting a shadow over the job and personal financial prospects of millions of people. Such uncertainty is not conducive to big ticket purchases and has therefore impacted the UK housing market.

Other factors such as negligible real wage growth and, more recently, higher interest and mortgage rates are also not supportive of a thriving housing market. A lack of affordability, especially for first-time buyers, is also hampering transactions and house price growth, despite support from Help to Buy and the Bank of Mum and Dad.

Investor influence fading

Government initiatives to dampen the role that investors play in the housing market look to be working. Although only a part of the story, the number of loans to BTL landlords has fallen by 46% between the Referendum and July 2018.

The principal disincentive is the less favourable income tax regime, with higher stamp duty an added

financial deterrent. We expect investor appetite to remain muted while house price growth prospects remain both uncertain and relatively weak.

This shift is important because it means that owner-occupiers, and therefore fundamental affordability, are even more important than before.

The consequence of all these influences has been a slowdown in UK house price growth and housing transactions since the EU Referendum. Annual UK house price growth has eased from 8.2% to 3.1% by July 2018, while UK transactions have declined by 7.4% from 1.29m to 1.20m.

Supply boost easing

A further consequence of the uncertainty and the relatively weak economic and consumer confidence backdrop, is that new housing supply, which was in the midst of a five-year surge, has slipped back over the past year.

New housing starts in the UK were running at 196,000 pa in Q1 2017 but have dropped back to 179,000 by Q1 2018.

Base case housing forecasts

As a consequence of these combined factors, our base case forecasts are for UK house price growth to weaken further during 2019, fading towards 1% pa from 3% pa now. We expect transactions to slow too, down to around 1.12m pa from 1.20m today. Housing starts will also slow.

Assuming the Brexit process continues along the current proposed timetable, the economy and consumer confidence will improve during the second half of 2019 and into 2020. This greater certainty will

lead to a marginally improved UK housing market. We expect house price growth to rise to 1½% pa with London and south-eastern markets first to react. Housing starts will initially remain subdued.

From 2021 we expect greater certainty to lead to an economic recovery and improved business and consumer confidence. This will lead to a brighter UK housing market with house price growth and the number of transactions increasing – especially in London and south-eastern markets. Housebuilders should also feel more confident, increasing housing starts gradually.

Forecast risks

The main risk to our base case assumptions is that UK economic weakness is prolonged by a year or two. This would result in lower house price growth and transaction forecasts in the early years of our outlook, pushing the housing market recovery into 2022 or 2023.

The second most likely risk is that the Brexit deal negotiated and approved is not as favourable for the UK as we assume. In this scenario our house price growth and transaction forecasts will be slightly weaker over the forecast period.

The other risk is that the UK exits the EU with 'no deal'. This would result in a far weaker UK economy and housing market over the next five years.



Source: JLL

2019	1½%
2020	1%
2021	3%
2022	3½%
2023	3%

2019	1.15m
2020	1.18m
2021	1.23m
2022	1.28m
2023	1.32m



Source: JLL

2019	175k
2020	180k
2021	185k
2022	195k
2023	205k



Source: JLL

London housing market forecasts

Brexit impact

The influence of Brexit, poor affordability and stamp duty changes have exerted pressure on the London housing market over the past few years.

And although they have stabilised during the last 12 months, house prices have fallen in Prime Central London and in new build Central London Developments during the course of the past three years. Furthermore, prices are now declining on an annual basis across Greater London.

Dampening influences

Affordability in London continues to hamper the mainstream market. The average house price is now more than 13 times the average income. So first-time buyers continue to struggle to buy, despite help from the Bank of Mum and Dad and the Help to Buy scheme, which has aided more than 12,000 purchases in the last five years. Indeed, Help to Buy is proving crucial at many new London developments.

This is even more important now that owner-occupiers form a greater proportion of purchases. The investor market, both domestic and international, has slowed in the past three years, but there are still plenty of active buyers. Stamp duty and income tax changes, as well as Brexit, have taken their toll.

Further changes for overseas purchasers, as proposed by the Prime Minister, could undermine this key support for development activity. Importantly, the overseas buyer tax regime in London would still be favourable compared with many other global cities, thereby limiting the potential downside impact.

London supply

New housing completions have been as high as ever over the past couple of years. However, housing starts began

to slow after 2015 and the investor stamp duty tax was introduced, meaning that completions will also ease down over the next two years.

The prospect of an acceleration in private sector housebuilding is also being dampened by the affordable housing requirements introduced by Mayor Sadiq Khan. This is certainly impacting the land market, with developers conscious of the new regime.

Given all of these considerations, we expect new housing starts to remain around 20,000 units a year over the next three years, before rising towards 25,000 a year by 2023. Undersupply will continue to provide some support for house price growth.

Greater London

Assuming the UK agrees a deal with the EU before March 2019 and that the current timetable is adhered to, we expect confidence to begin to return to the Greater London housing market during the second half of 2019. However, house price growth and transactions are likely to remain quite weak in 2019.

Thereafter, we forecast that the London housing market will be the most responsive to the greater certainty of a Brexit deal. We expect house price growth to rise to 2% in 2020, before rebounding more strongly to 4% pa in 2021–2022.

Prime Central London

The Prime Central London market has struggled for the four years to end-2018. Stamp duty changes in December 2014 and again in 2016 have significantly increased transaction costs. And this, together with Brexit uncertainty, has led to sharply lower transactions and a notable decline in prices, especially at the upper-end of the market.

We anticipate a fillip to Prime Central London market confidence in 2019 once the EU deal is approved. The greater certainty will immediately boost demand from domestic and international buyers - the latter particularly keen to benefit from the short-term currency advantage.

Prices will begin to rise almost immediately, albeit gradually to start with, but it will take longer for transaction volumes to recover. Prime Central London price growth could rise to 1% in 2019 and 2½% in 2020 before accelerating to 4% in 2021. This growth profile could be dampened slightly if Conservative proposals to increase international buyer stamp duty are enacted.

Central London Development

We expect the Central London Development market to respond quite quickly to the changing UK/EU situation. Confirmation of a deal and a reasonable transition period will instil greater confidence into the market and will encourage both owner-occupiers and investors to buy. Prospects of sterling appreciation will be an additional driver for international purchasers in the near-term.

We expect prices to nudge up in 2019 as medium-term growth prospects improve, before price growth accelerates more quickly as confidence returns. An overhang of available units in current developments will initially temper price growth, but with supply set to slow, price growth could be as strong as 5% pa come 2021. These forecasts could be tempered slightly if new stamp duty levies are brought in for overseas buyers.

The London Help to Buy scheme will continue to provide positive impetus where and when appropriate. The market should be stronger and less in need of this initiative by the time it ceases.

2019	1½%
2020	3%
2021	5%
2022	4%
2023	3%



Source: JLL



2019	1%
2020	2½%
2021	4%
2022	4%
2023	3%

Source: JLL

2019	½%
2020	2%
2021	4%
2022	4%
2023	3½%



Source: JLL



2019	19k
2020	19k
2021	21k
2022	24k
2023	25k

Source: JLL

Our forecasts 2019 – 2023

House price growth (% pa)	2019	2020	2021	2022	2023	2019-23*
Prime Central London	1	2½	4	4	3	15.3
Central London Development	1½	3	5	4	3	17.6
Greater London	½	2	4	4	3½	14.8
South East	0	1	3	3½	3½	11.4
East of England	½	1	3½	4	3½	13.1
South West	1	½	2½	3½	3	10.9
East Midlands	0	½	2½	3½	3	9.8
West Midlands	1	½	1½	3	3	9.3
Yorkshire & The Humber	1	½	2	3½	3	10.4
North West	1	1	2½	3½	3½	12.0
North East	0	0	1	2½	3	6.6
Wales	1	0	1½	2½	3	8.2
Scotland	2	1	2½	3	2½	11.5
UK	½	1	3	3½	3	11.4

Rental growth	2019	2020	2021	2022	2023	2019-23*
Prime Central London	½	1½	2½	3	2½	10.4
Central London Development	2	2½	3	3	2½	13.7
Greater London	2	2½	3½	3½	3	14.2
South East	1½	2	2½	3	2½	12.0
UK	1½	2	2½	3	3	12.6

Activity and development	2019	2020	2021	2022	2023
UK transactions (m)	1.15	1.18	1.23	1.28	1.32
UK starts (000s)	175	180	185	195	205
UK completions (000s)	190	180	175	180	185
London starts (000s)	19	19	21	24	25
London completions (000s)	21	20	19	19	21

Source: JLL * cumulative growth

Residential services



Investment



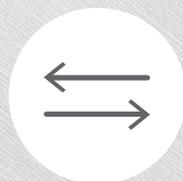
Affordable Housing



Estate Agency
& Lettings



Funding &
Corporate Finance



Land Sales &
Acquisitions



Research



Valuations



Mixed Use
Development



Planning



New Homes Sales



International
Agency



Development
Consultancy



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