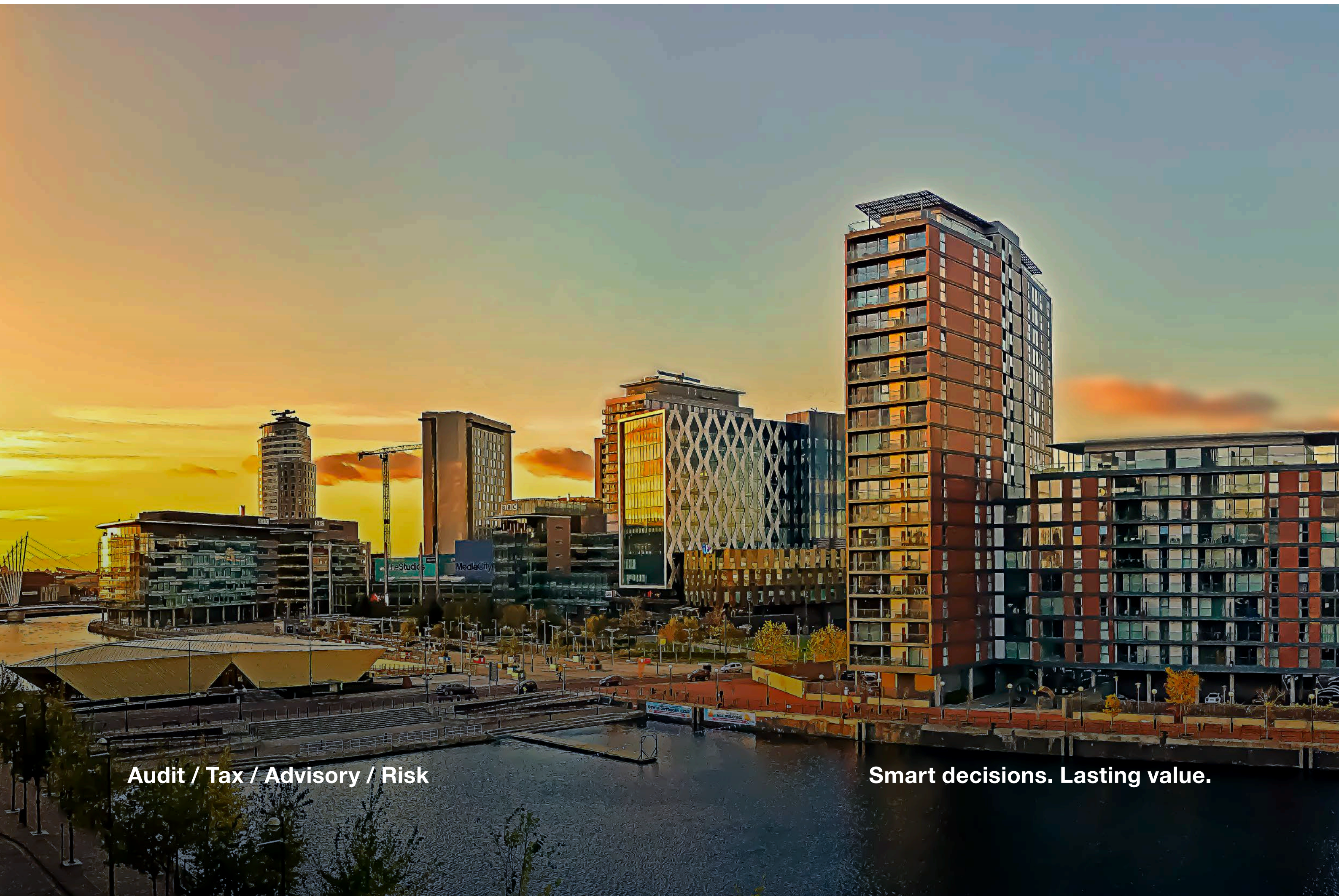
# 2018 Property and Construction Outlook Report



# Foreword

## The results of this year's report show that in the uncertain political and economic environment our respondents are wary of the outcome for the property and construction industry.

A number of key issues have developed over the past 12 months, which are having a real impact on the growth of the industry. Brexit negotiations and the outcome of Brexit is causing the most concern to businesses and the impact it will have on their operations, closely followed by economic and political uncertainty.

The respondents to our survey identified the current UK tax system as a key area for concern. Stamp Duty Land Tax (SDLT) has been continually seen by the industry as the biggest tax barrier to business growth. Respondents, unexpectedly, have also continued to state concerns over planning regulations.

This year's property and construction report has collected the opinions of those working in the industry, identifying the key challenges and opportunities they face. The results provide a unique snapshot into the sector's conditions and identifies ways in which the government can provide the support it needs.

**Stacy Eden,**
**Head of Property and Construction, Crowe**

# 01 Summary of Findings

# Brexit and UK economy

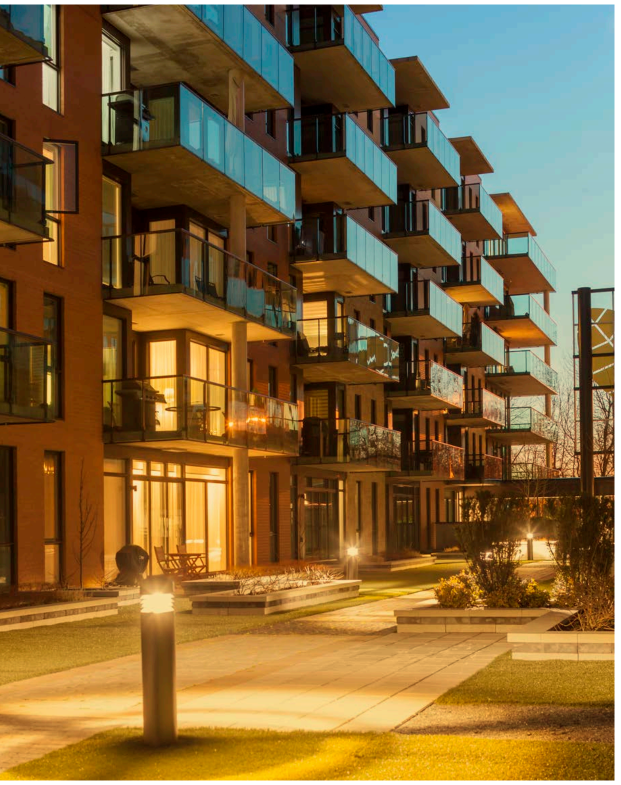
The United Kingdom (UK) will leave the European Union (EU) on 29 March 2019 and begin to chart a new course in the world. After a time-limited implementation period that is expected to conclude at the end of 2020, the UK and the EU will enter into a new relationship – one that must work for both sides, underpinning shared prosperity and security.

In the event of a deal there will be a transitional period until 31 December 2020, giving businesses more time to prepare for the new arrangements. If there is no deal the expectation is that the UK will leave the EU in March 2019, without any transitional provisions. In the event of a no deal Brexit, the UK government has released the first of 50 or more documents covering all aspects of trade with the EU, some of which cover many areas of tax.

The guidance is particularly useful as it may also reflect the expected position in a deal scenario but one where the UK sits outside the EU's VAT and Customs regimes, as is expected given the current stance of the government on this issue, at the time of writing.

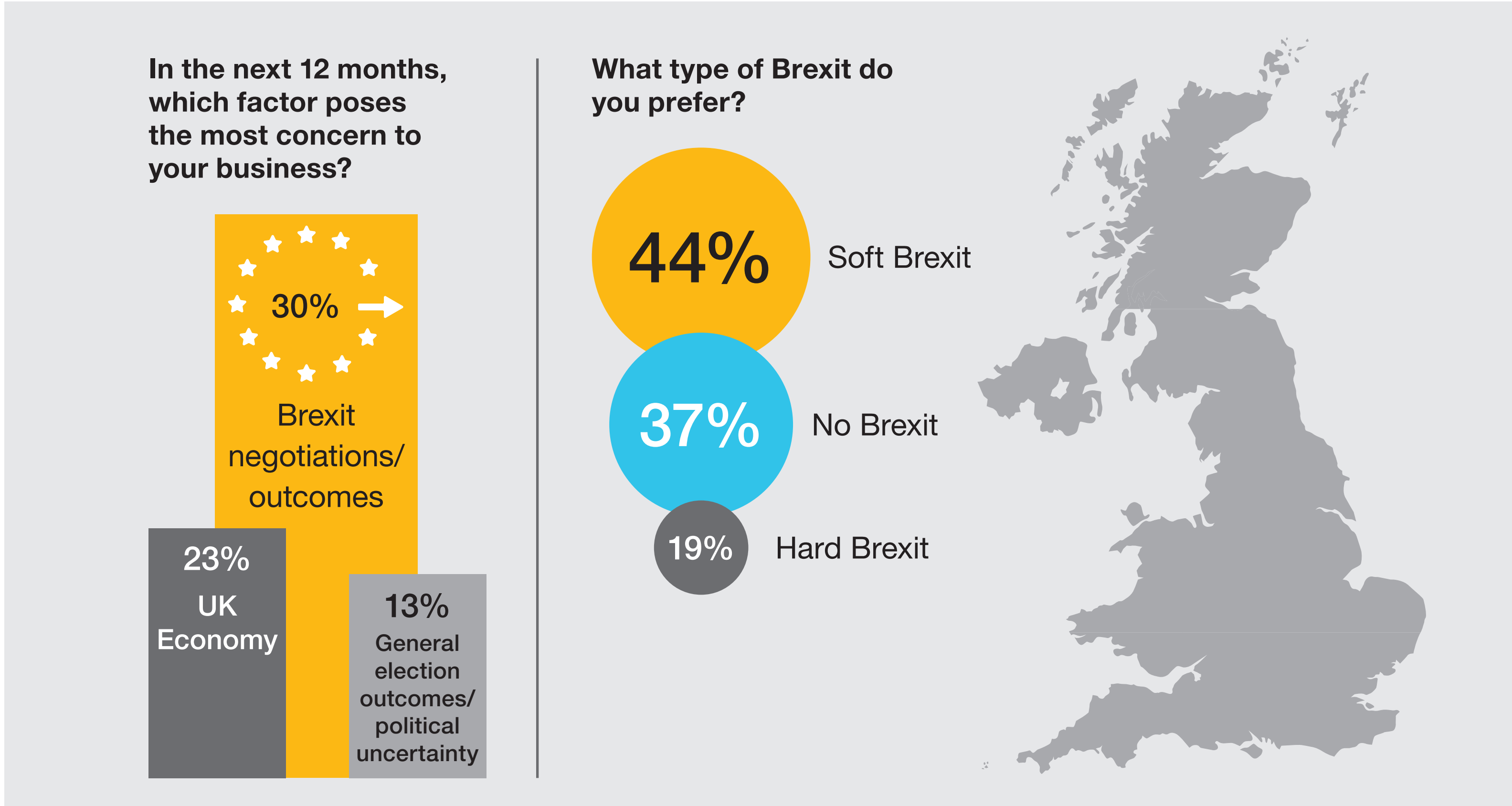
Even with the additional documents there are still many issues that cannot fully be covered, and remain as some of the Brexit fiscal unknowns. This also gives rise to whether there will be a 'hard' or 'soft' Brexit. 44% of our respondents would prefer a soft Brexit, with a similar number preferring no Brexit.

If Britain loses its free access to the single market, there is a worry that this could rapidly change the country's status as a commercial gateway to the rest of Europe, with adverse consequences for both occupier and property investment markets. If demand from overseas buyers did drop following Brexit, the impact on the market could be significant. After all, by value, overseas buyers have accounted for roughly half of all transactions in the British commercial property market over the past few years.



There is more reason for concern over the impact of Brexit on the City of London and, subsequently, the British property market. Brexit could damage the City, by forcing institutions to re-locate to the continent. In that scenario, vacancy rates could rise and the premium commanded by Central London office space could shrink.

It seems likely that leaving the EU without a deal would hit the health of the City and it is plausible that a number of overseas institutions would close or scale back their London operations, putting a dent in occupier demand.



# UK tax systems and government

## Unsurprisingly our respondents have highlighted that the tax system is not favourable for property developers and investors due to the property and construction industry being heavily taxed compared to many other OECD countries.

Making tax digital (MTD) will have an impact on the sector as we move towards the introduction of MTD for VAT in April 2019.

MTD is expected to be the most fundamental change to the tax administration system for at least 20 years and many property and construction businesses remain unaware of what is changing and when. From 1 April 2019 all organisations with a taxable turnover above the VAT registration threshold will have to:

- keep their VAT records digitally
- submit their VAT data to HMRC through compatible software
- stop using the HMRC online portal.

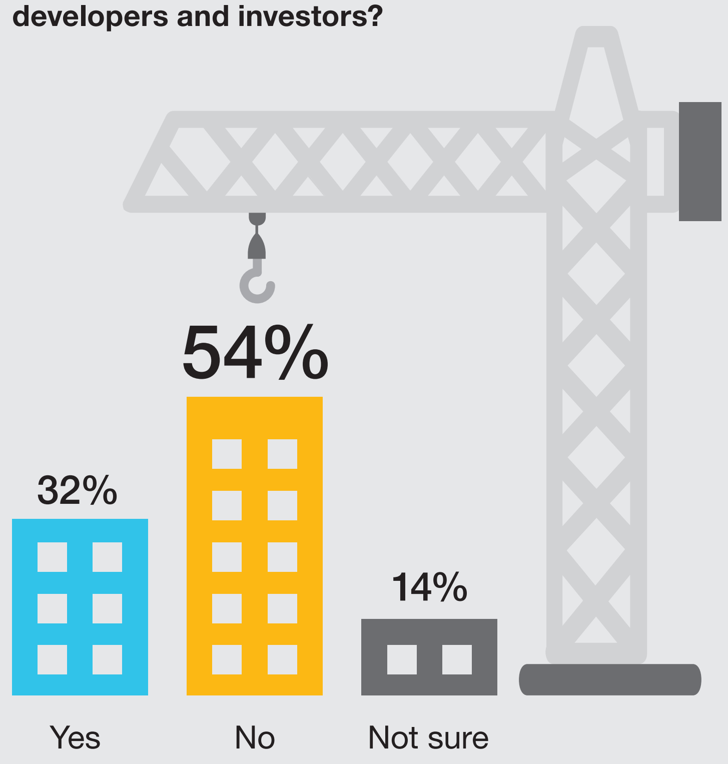
The requirements will be relevant to investors, developers, operators and construction service providers. In short, almost everyone in the sector that is registered for VAT.

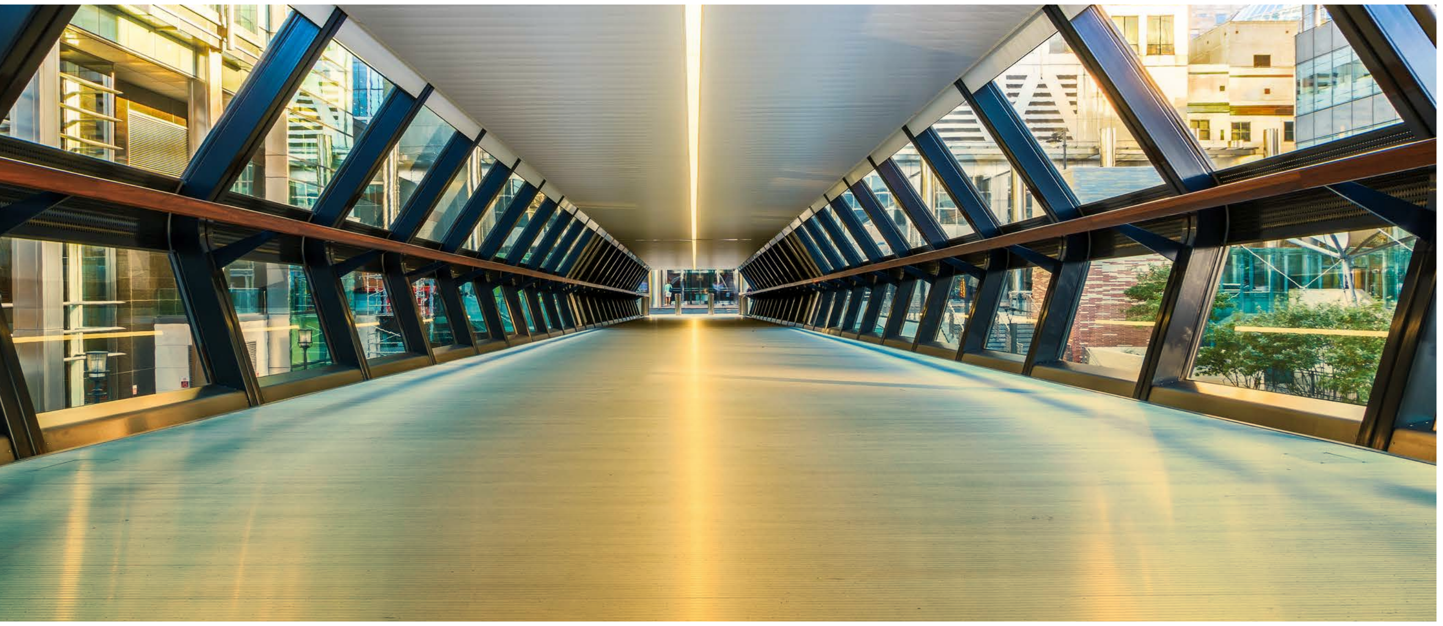
Additionally a number of changes to the way non-residents that hold UK land and property are taxed have been published in the draft legislation for the Finance Bill 2018/19.

From 1 April 2019 for companies, and from 6 April 2019 for other taxpayers, the UK Government proposes that all capital gains accruing on disposals of interests in UK property by non-residents will become taxable. This means that, as well as gains on commercial investment property being chargeable to tax, some previous exclusions in relation to residential property will be removed. In addition, there will be a charge on disposals of interests of 25% or more in companies and other entities that derive 75% or more of their gross asset value from land.

There are also changes to the tax rules around rental income from 6 April 2020. It is proposed that non-UK resident companies that carry on a UK property rental business or have other UK property income will be brought within the charge to corporation tax (17% from 1 April 2020), rather than paying income tax (currently 20%).

**Is the tax system favourable for property developers and investors?**





# Impact of technology

In 2017 the Mayor of London set out his ambition for London to be the world leading smart city, with digital technology and data at the heart of making London a better place to live, work and invest.

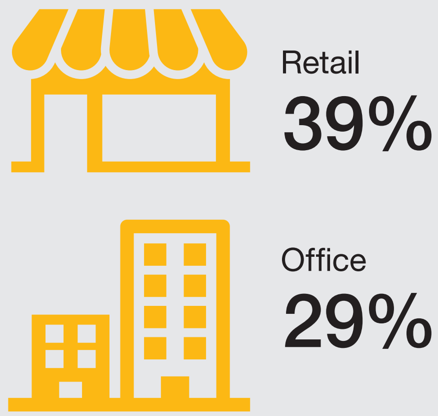
Improving our digital infrastructure is the core of ensuring London is comparable to other global and UK cities. City Hall announced plans to install half a million brick sized mobile masts on lamp posts and other public buildings to make London Europe's biggest 'gigabit city'.

Emerging technologies are reshaping the property and construction market, posing an opportunity and a threat to those within the industry. Our survey suggests that retail will be impacted the most. With the demand for customer experience and personalised service growing, the retail market is having to adapt to the need for convenience for the user. Click and collect and one hour delivery services have transformed the retail sector as time is becoming a precious commodity to the consumer.

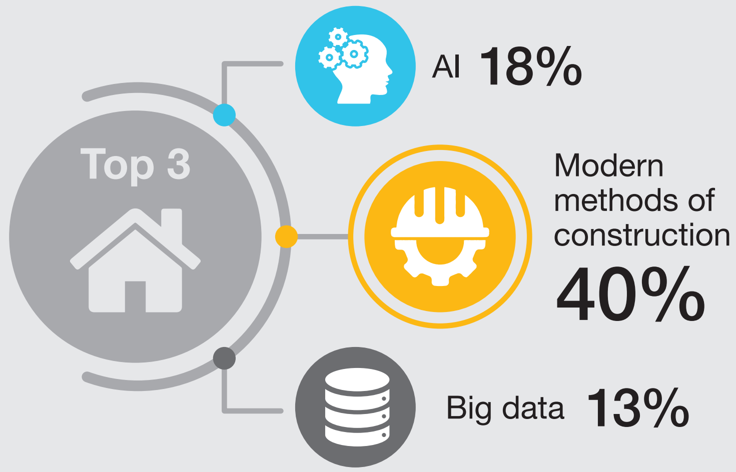
Robotic automation, machine intelligence and software robots are likely, over the coming years, to become a fundamental part of the working environment and will have an impact on space requirements.

Another change to office space is a growth of employees working remotely and new forms of work organised via online platforms. It is becoming clear with the rise of the 'we-work' co-working spaces that high growth firms, freelancers and entrepreneurs value the community feel of the office environment. This continued trend of flexible office space will cause more developers to take note of the demand and adapt.

**Which types of property are most likely to be impacted by technological trends?**




**What will be the next big thing to impact the property sector?**



# National versus London

## Findings from our survey, much like last year, show that the London market is still affected by low growth due to uncertainty and SDLT.

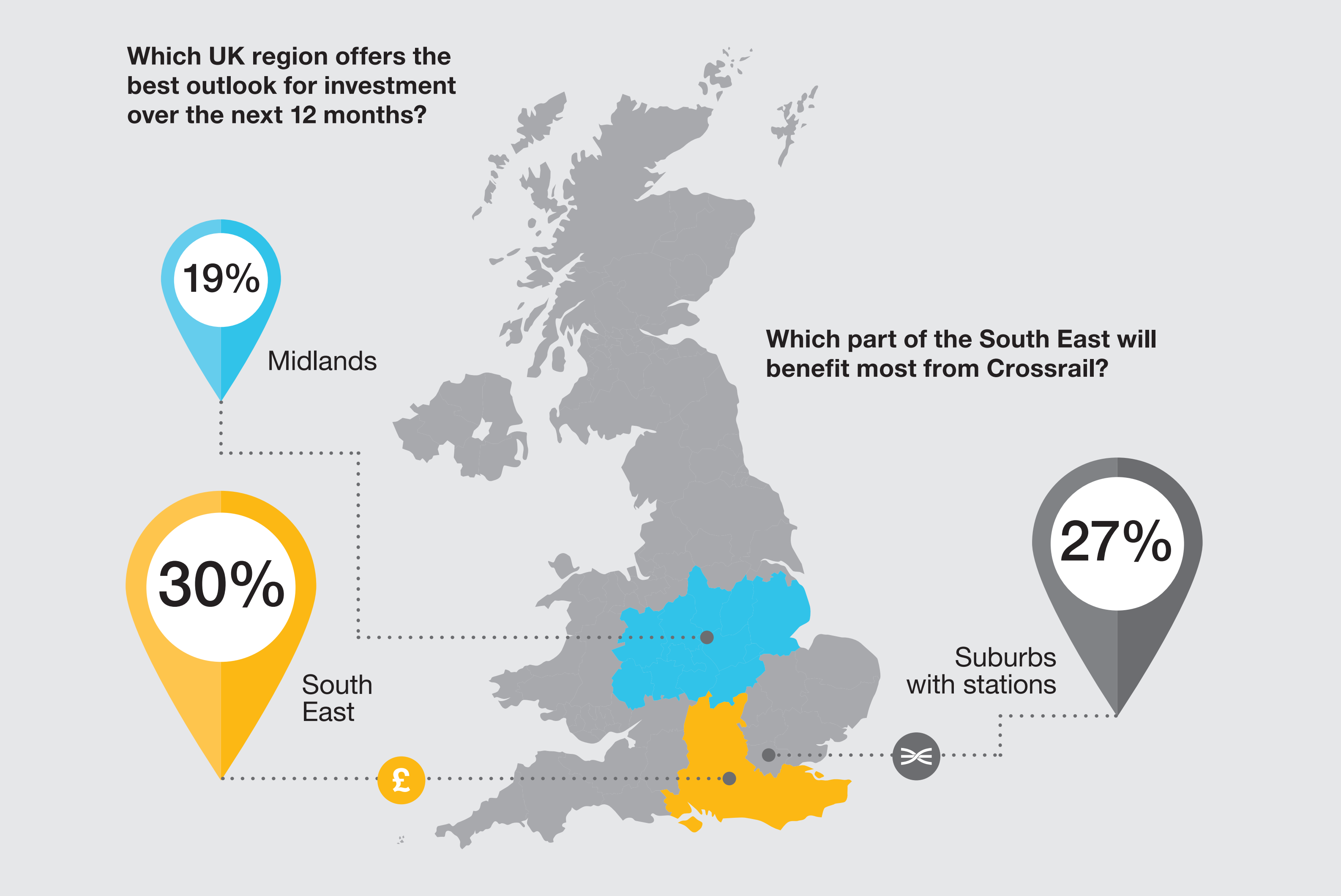
The South East is regarded by our respondents as having the highest potential for investment. This is partly due to Crossrail and buyers seeking cheaper alternatives to London.

It has been projected that the new line will support the delivery of over 57,000 new houses. Nearly half of planning applications within a kilometre of an Elizabeth line station have cited the new railway as a justification for the development proceeding, equating to around 5.3 million square feet of residential, commercial and retail space.

Respondents also highlighted West Midlands as an area for investment over the next 12 months. Birmingham is often affectionately known as Britain's second city having one of the largest populations outside of London. It also has one of the largest legal and financial services centres outside of London. Birmingham has a strategically advantageous position in the country, as 90% of the population can reach it in under four hours. As London gets more expensive to live in, it is reasonable for our big regional cities with large universities to be seen as a place for investment.

This region will benefit from the £55 million HS2 high-speed rail project, gaining new stations in the Birmingham area and one in the East Midlands at Toton. More people are likely to move to Birmingham with this new development and commute to London. HS2 journey times between Birmingham and London will take 49 minutes – the typical London journey to work is 45 minutes.





# Beyond British border

The majority of our respondents operate UK only businesses and 91% had no intention to expand overseas in the next 12 months. There were a variety of reasons cited including the tax burden for not investing in mainland Europe.

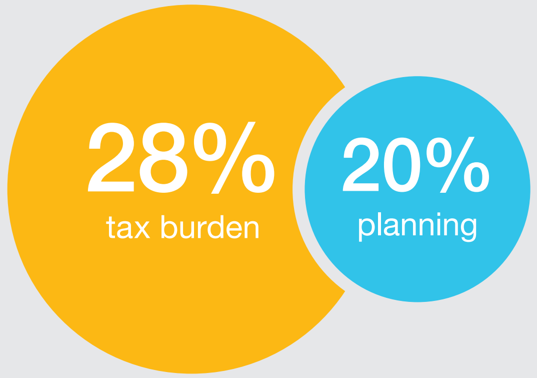
Access to finance and planning regulations were also cited as barriers to investing in Europe.

Germany appears as the most popular by 49% of our respondents as having the best potential for property investment. Given the European Central Bank's (ECB) zero interest rate policy, interest rates remain at a record low with financing conditions historically favourable. Furthermore, Berlin came top in Knight Frank's global ranking of 150 residential property markets. Three other German hot spots also appeared in the top 10: Hamburg, Munich and Frankfurt.

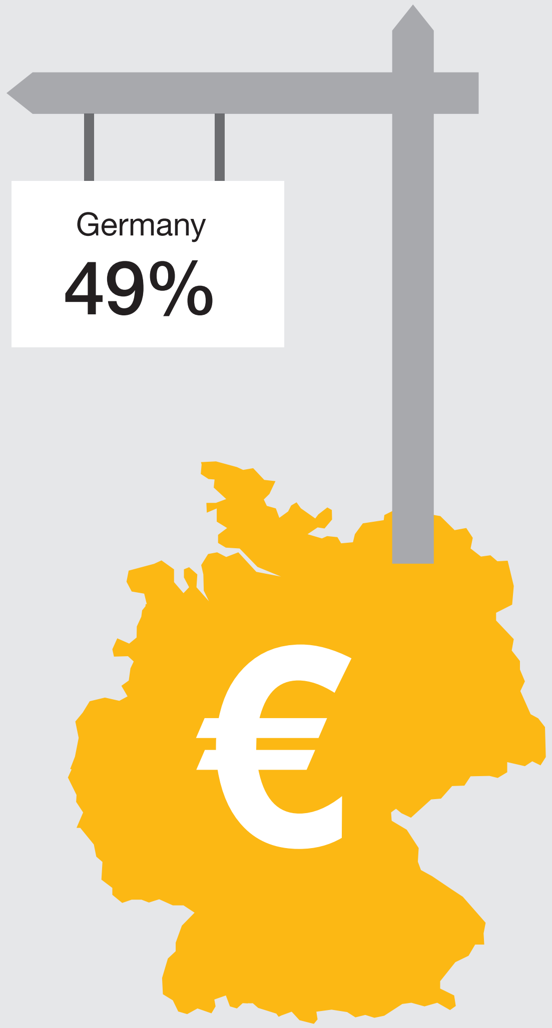
**In the next 12 months do you have plans to invest or expand overseas?**

91% of respondents **do not** plan to invest or expand overseas

**What are the biggest barriers for investing in property in Europe?**




**Which countries in Europe have the best potential for property investment?**

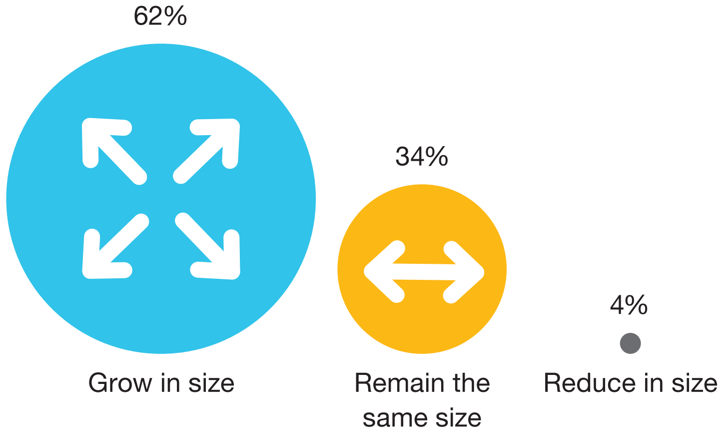


# 02
# The findings

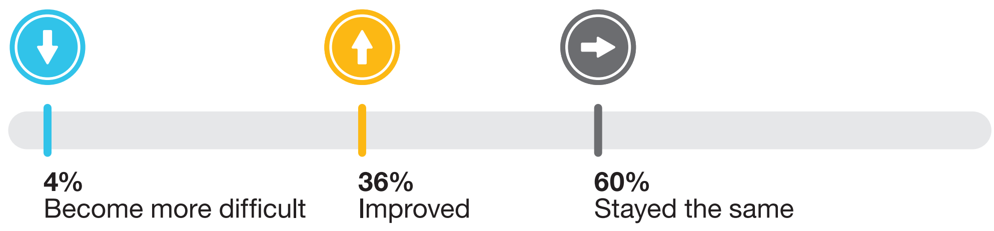
# Business operations and growth

In the next 12 months 62% of participants were positive about their business growth. Despite Brexit uncertainty, businesses are confident that their growth plans may continue. 60% of participants have little or no difficulty obtaining funding, with 36% suggesting access to funding has improved compared to the 24% last year. Banks still provide the majority of financing.

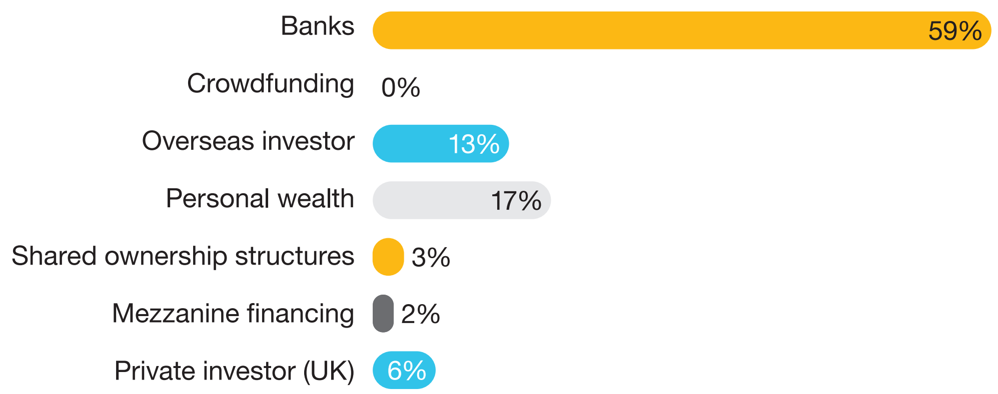
**In the next 12 months do you expect your business to...**




**How has the access to funding changed over the past 12 months?**




**In the past 12 months, where has the majority of your financing come from?**



# Valuations

## Low growth has been experienced in parts of the property market with our findings suggesting that the greatest impact will be felt in the retail regional market (30%). The residential London market was second highest (23%). Brexit uncertainty, the rise of e-commerce, business rates and national living wage could be attributed to this low growth.

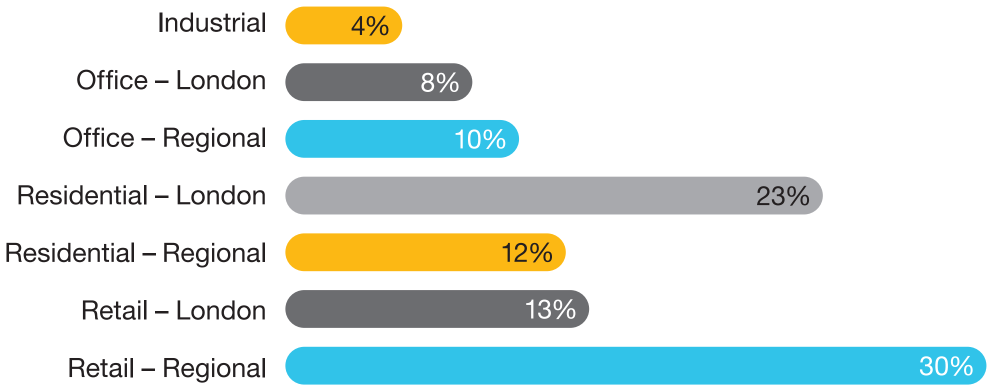
Business confidence data from the Institute of Chartered Accountants in England and Wales (ICAEW) suggests that sentiment in Q3 2018 has been hit by a number of disappointing economic and political events, such as weak GDP growth in Q1, store closures, house price declines and, of course, Brexit. The index fell to -0.2 in Q3, from +7.0 in Q2, but remains well above the post referendum average of -3.1.

The Bank of England raised the Bank Rate from 0.5% to 0.75% at the beginning of August; a decision that was unanimous. The rate rise did little to boost Sterling as the rise had already been priced in by financial markets.

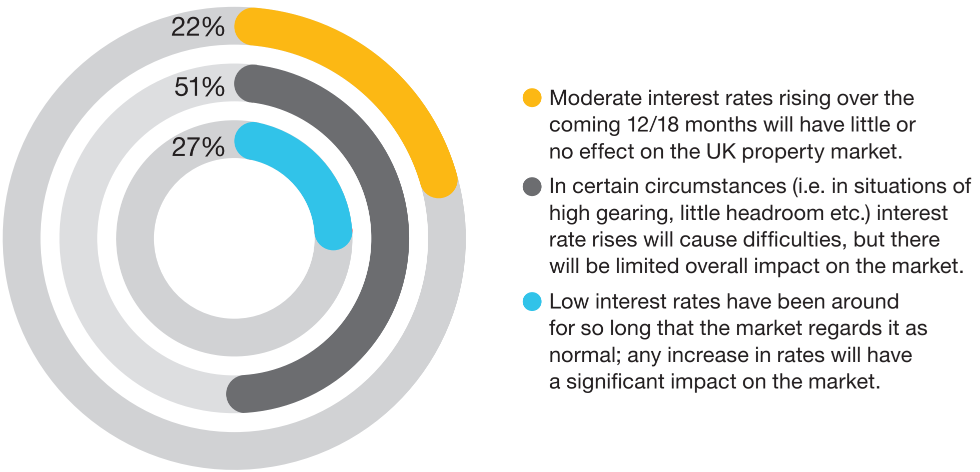
However, Oxford Economics expect the exchange rate to recover to £1/$1.38 by year end. CPI inflation is moving sideways and stands at 2.5% year on year in July, while there was a slight slowing in RPI inflation to 3.2% year on year.

Nationwide commercial and residential property prices were predicted by our respondents over the next six months to increase by less than 5%, highlighting the uncertainty in the market.

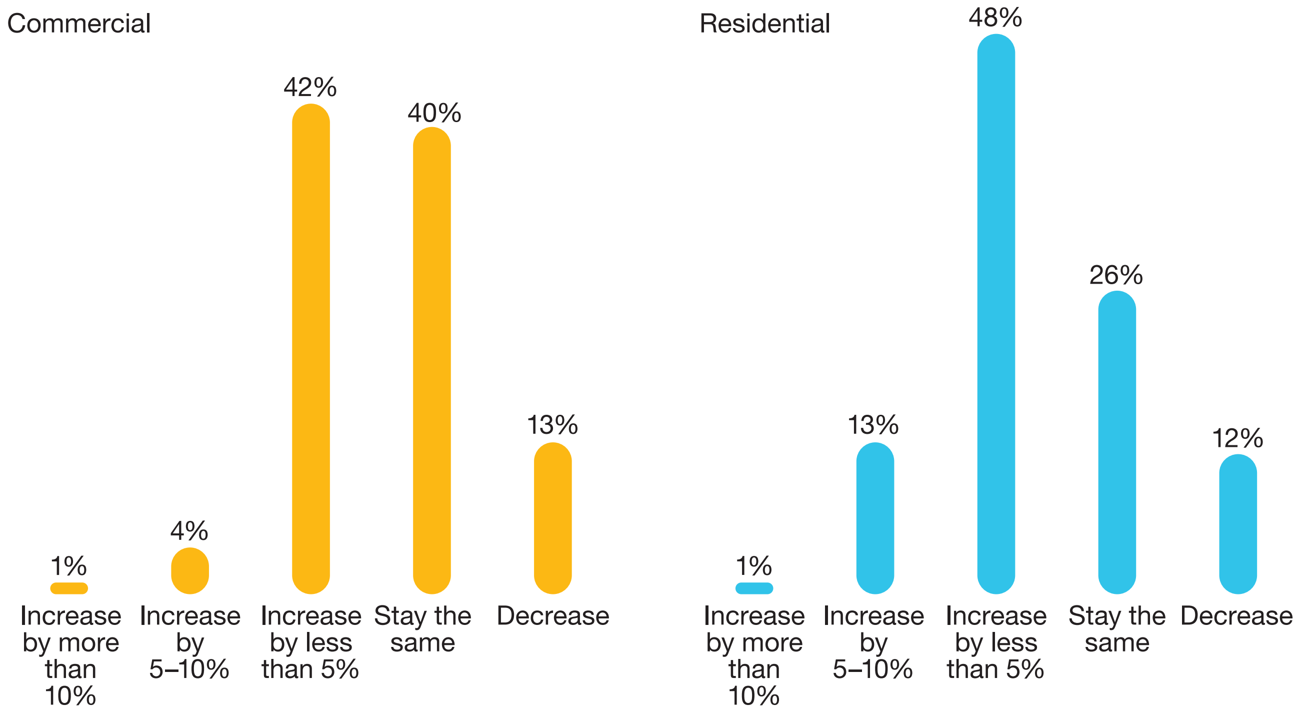
**With the property market experiencing low growth, which types of property are most impacted by this trend?**



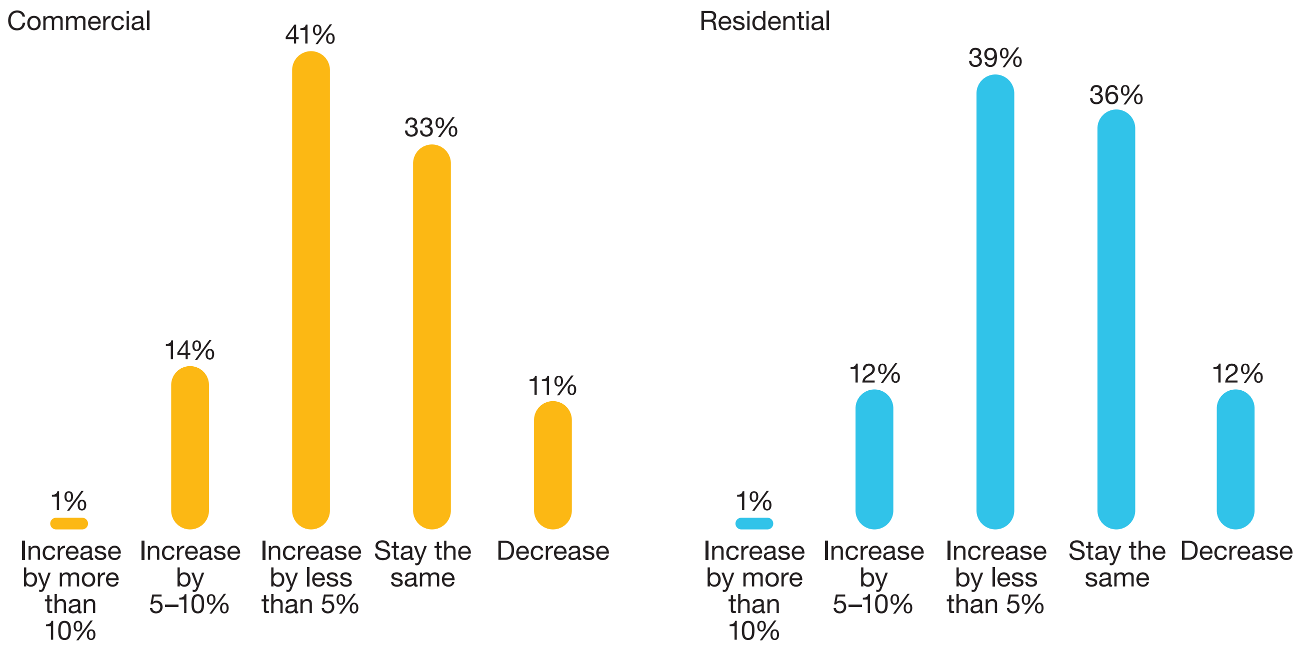

**How will the rising interest rates impact the property sector?**




**In the next six months, do you expect property prices nationwide to...**




**In the next six months, do you expect property prices in the South East to...**



# Government activity and priorities

Over two thirds of respondents agreed that the UK tax system is unfavourable to the property and construction industry, with over 82% attributing SDLT as the main fiscal barrier to business growth.

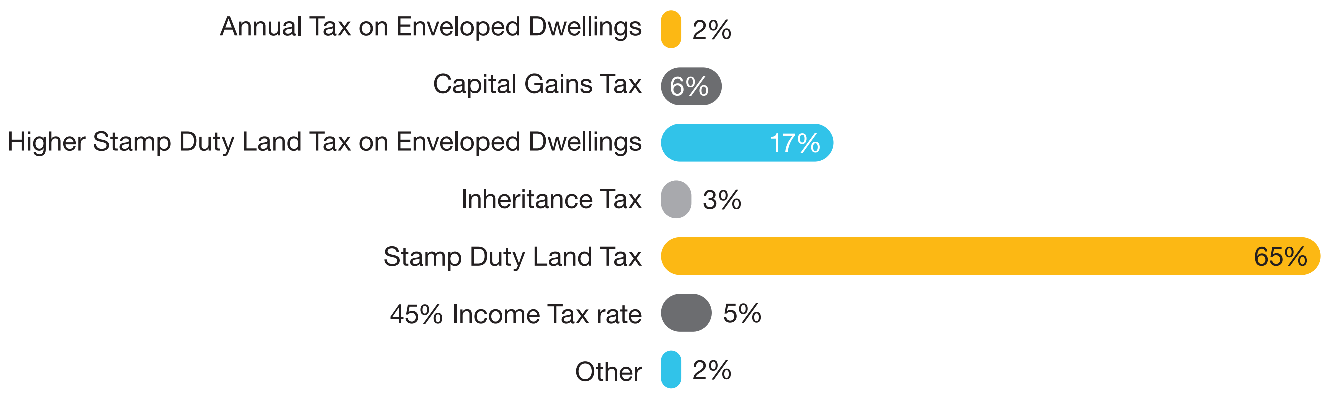
The high rates of SDLT have hugely reduced transactions in the residential market populating at the top end. This reduction in liquidity ultimately reduces government receipts and, more critically, our housing developments are reduced. In the residential market, the older generation often own large houses and high SDLT, and affordability may deter younger buyers therefore putting a brake on the market. However, Help to Buy has boosted transactions for first time buyers.

Retail stores experienced a negative impact from the 2017 rating revaluation, with the widespread closure of high profile retailers across the board, which could be a side effect of the 2017 rating revaluation.

The government has estimated that 510,000 businesses are set to see an increase in their business rates, 420,000 will stay the same and 920,000 will see a decrease. In the 2018 Spring Statement, The Chancellor, Philip Hammond announced the government will bring forward the next revaluation of business rates from 2022 to 2021.

Furthermore, 77% of respondent's highlighted that the Green Belt protections were not conducive to solving the housing crisis. The Government have set a bold target to build 300,000 homes a year by the mid 2020's and would require the current restrictions on Green Belt land to be relaxed to develop new homes.

**What do you perceive as the biggest tax barrier to business growth?**

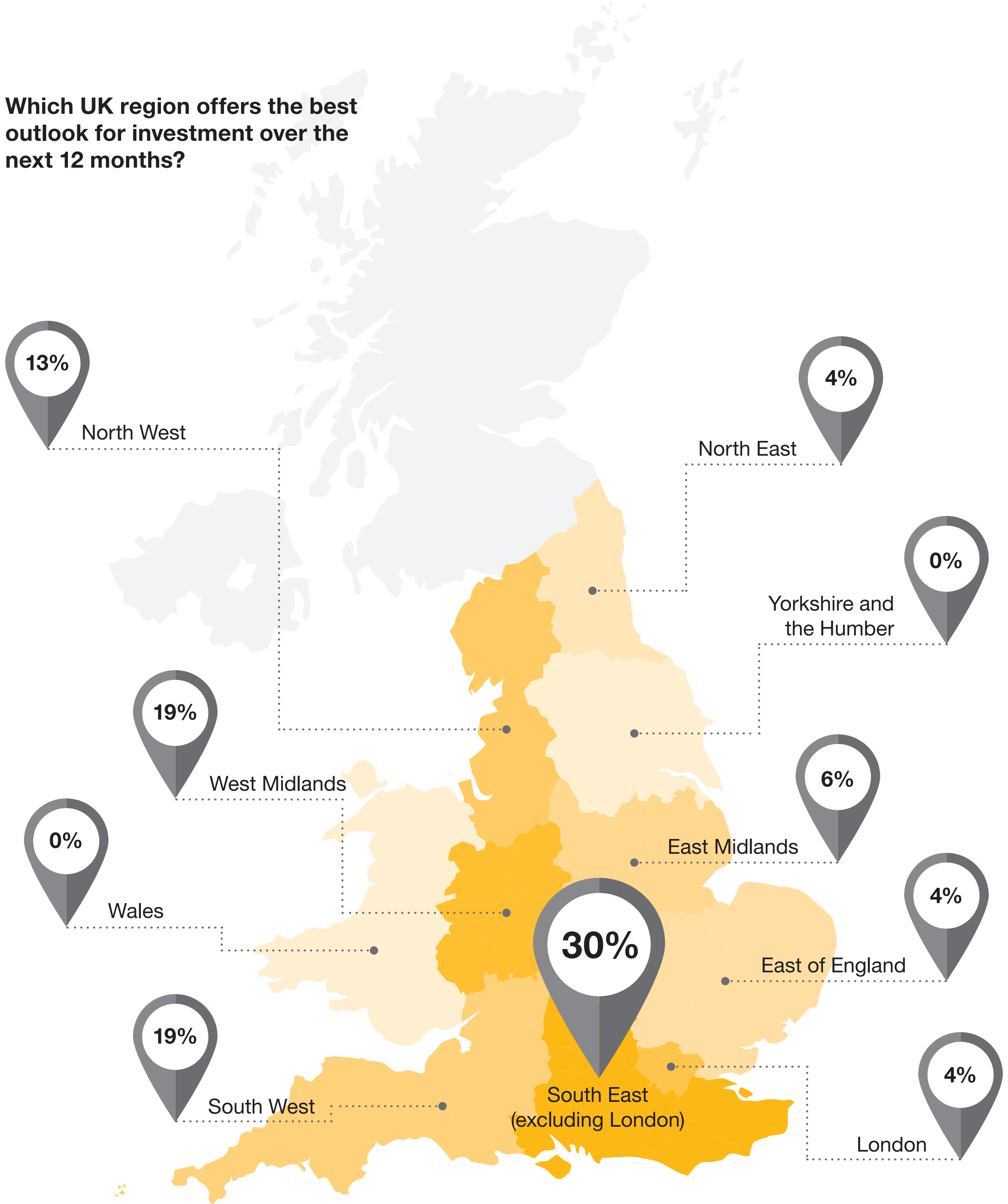



**Is current policy around Green Belt protections conductive to solving the housing crisis?**

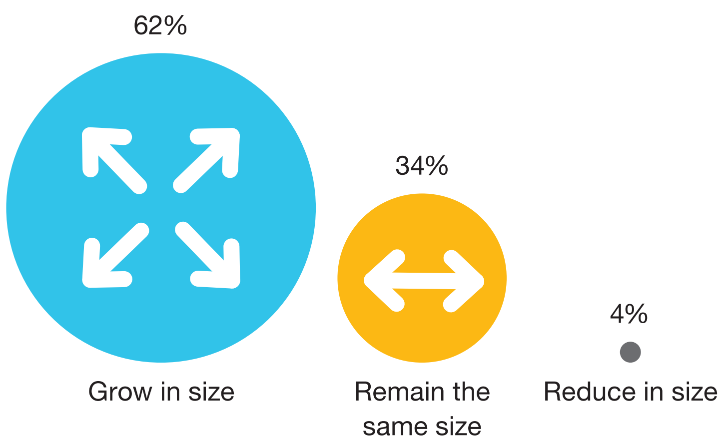
# UK outlook

With the flurry of government activity and almost daily headlines and speculation about the government's preferred vision for Brexit and strategy for the negotiations, it is no surprise that Brexit negotiations and its outcome is the greatest concern to those in the property and construction industry. This is followed by the UK economy, which has held the top spot for the last two years in our survey.

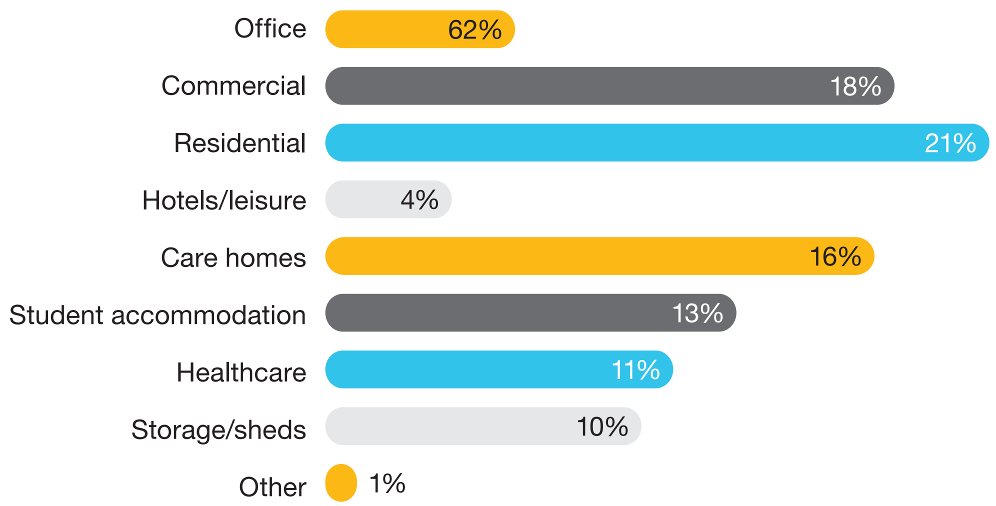
**Which UK region offers the best outlook for investment over the next 12 months?**



**In the next 12 months do you expect your business to...**




**In the next 12 months, what do you consider to be the most attractive asset class for investment?**



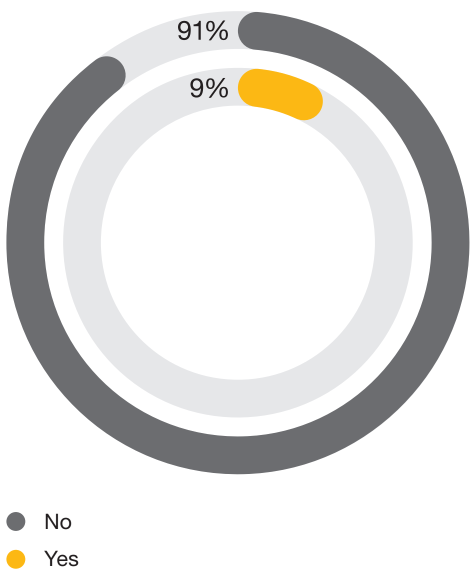

# International activity

Over 85% of respondents had operations focused in the UK; 91% did not have plans to invest or expand overseas.

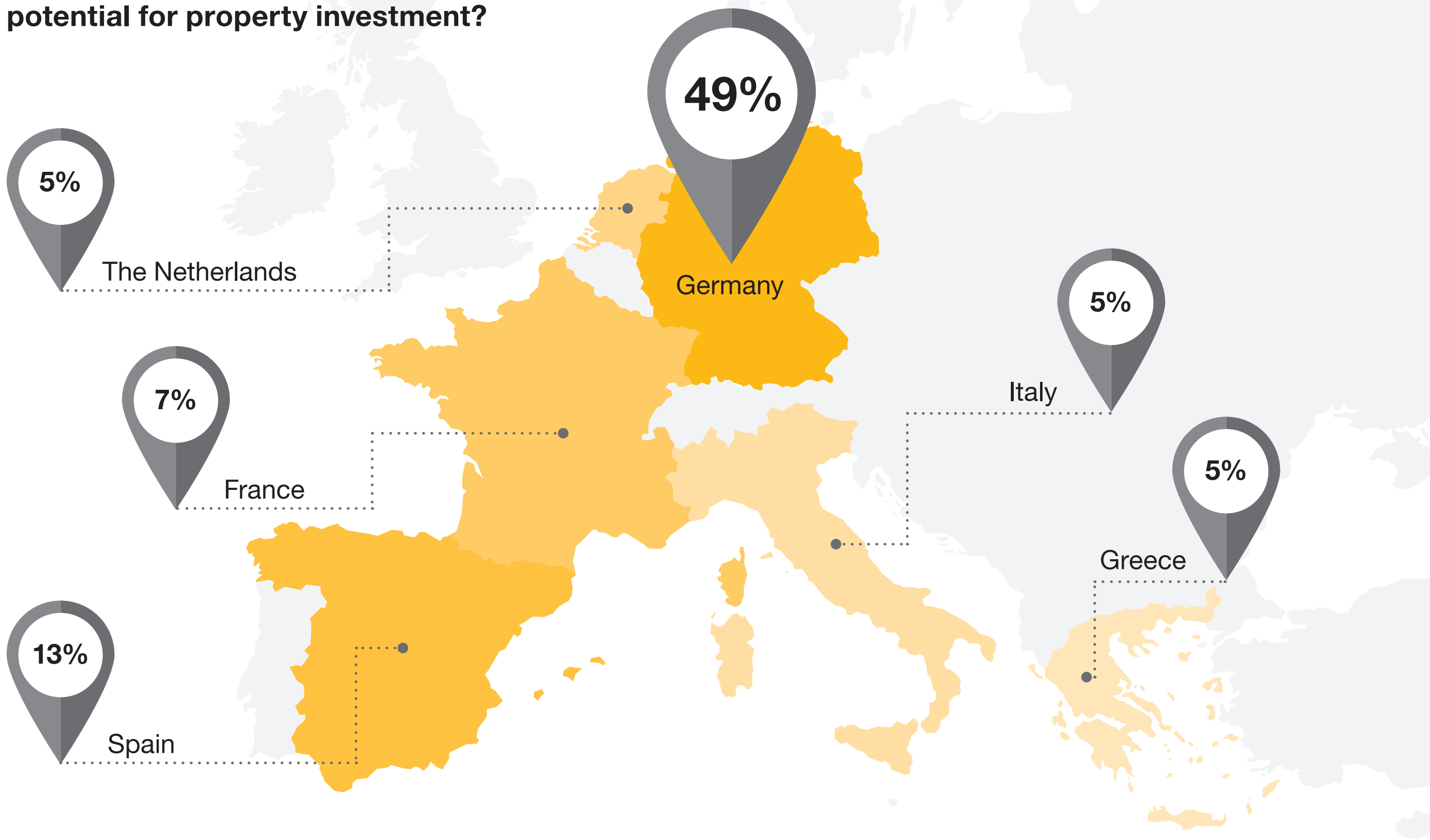
The majority of respondents named Germany as the best potential for property investment. Germany's robust economy, comparatively stable politics and continuing inward migration give overseas investors plenty of reasons to feel positive about investing.

The respondents cited tax burdens and planning restrictions as some of the biggest barriers when it came to them investing in property in Europe. Others highlighted currency movements, commercial uncertainty – Brexit etc. as barriers.

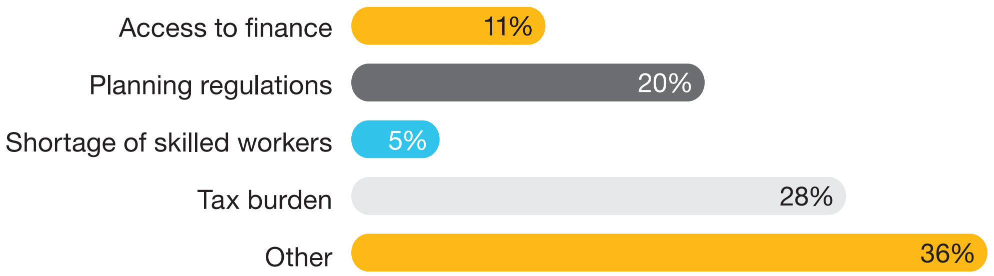
**In the next 12 months do you have plans to invest or expand overseas?**




**Which countries in Europe have the best potential for property investment?**




**What are the biggest barriers for investing in property in Europe?**

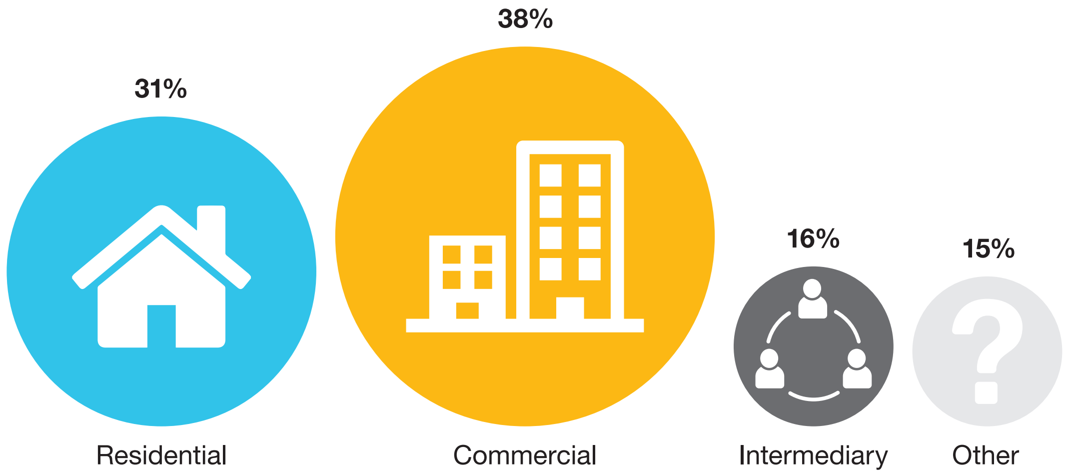


# A snapshot of the participants

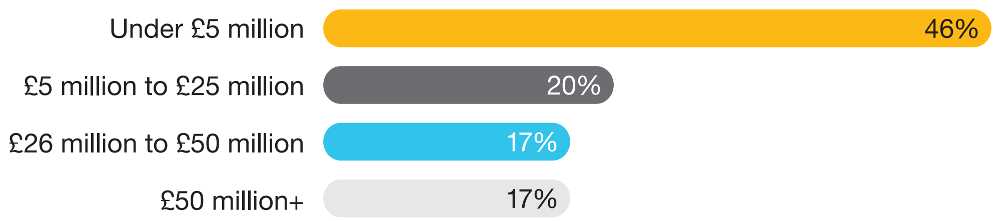
38% of participants work in commercial property businesses while 31% work in residential businesses. The remaining respondents work in organisations such as banks and legal firms or intermediary organisations such as brokers.

Out of all our respondents, the value of their property assets were varied, ranging from under £5 million, while others have assets valued over £50 million.

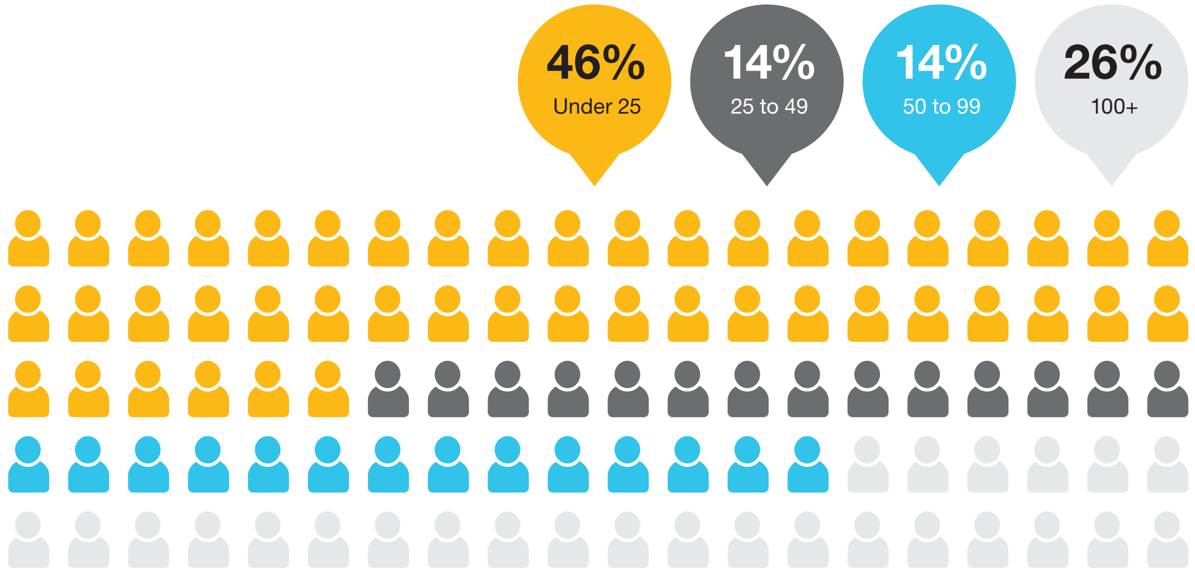
**Which description best fits your company's activity?**




**What is the value of your property assets?**




**How many people do you currently employ?**



# Our Property and Construction team

The property and construction industry has long been an indicator of the health of the UK. Our specialists are passionate about the industry and focused on your future and experience. By making smart decisions today we can create lasting value tomorrow.

**Your interests, our priority**
While the UK remains an attractive area for investment, the industry is changing. Businesses face new challenges including financing, imbalance in the market, and fallout from Brexit. Over recent years, the pressure from rising complexity and levels of taxes has become an added burden.

Our specialists can draw on many years' experience to help you navigate the changing landscape, mitigate risk and achieve your objectives.

**We help...**

- Listed companies
- Privately owned companies
- Limited partnerships
- Sole traders
- Funds
- Surveyors
- Architects
- Housing associations
- International groups

**Who are engaged in...**

- Property investment
- Property development
- Property trading
- Hotels
- Construction
- Care homes
- Student accommodation

**With...**

- Statutory audit and accounting
- Taxation compliance and advisory
- Financing
- Corporate finance
- Advice for shareholders and directors
- VAT
- International services
- Personal and exit planning
- Employer advisory
- Regulatory compliance
- A wide range of other financial services

**For more information on how we can help you please contact us to start the conversation.**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Crowe

## About Us

Crowe UK is a national audit, tax, advisory and risk firm with global reach and local expertise. We are an independent member of Crowe Global, the eighth largest accounting network in the world. With exceptional knowledge of the business environment, our professionals share one commitment, to deliver excellence.

We are trusted by thousands of clients for our specialist advice, our ability to make smart decisions and our readiness to provide lasting value. Our broad technical expertise and deep market knowledge means we are well placed to offer insight and pragmatic advice to all the organisations and individuals with whom we work. Close working relationships are at the heart of our effective service delivery.

### Start the conversation

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