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Real Estate


# Time out...

## London Office Crane Survey

Winter 2019

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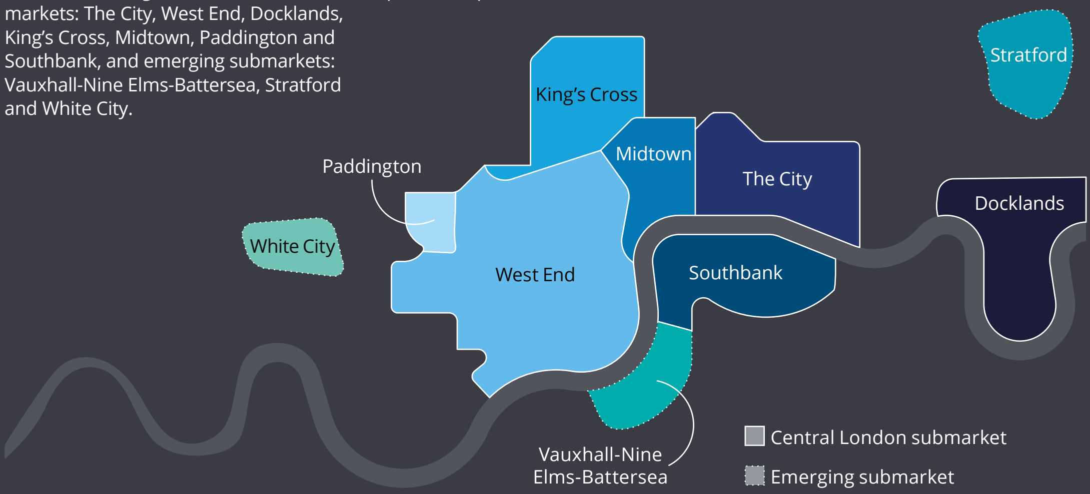
**What?**
A report that measures the volume of office development taking place across central London and emerging London submarkets.

**Where?**
London, covering the central office markets: The City, West End, Docklands, King's Cross, Midtown, Paddington and Southbank, and emerging submarkets: Vauxhall-Nine Elms-Battersea, Stratford and White City.

**Who?**
Developers building new offices or undertaking significant office refurbishment of 10,000 sq ft +.

**When?**
The survey covers the period from April and September 2019.

**How?**
Our team of researchers have walked the streets of central London and emerging London submarkets to monitor office construction. Our field research is then verified with direct industry links and in-house property experts.



# Foreword

## Welcome to Deloitte's Winter 2019 London Office Crane Survey – a barometer of business and developer sentiment as well as future workplace supply.

Within the report we track construction activity by area and leasing activity, by both submarket and business sector. After the financial crash in 2008 the property sector experienced a big drop in activity, but since 2015 successive Crane Surveys have reported strong leasing activity and above-average levels of construction. Bearing in mind the economic and political turbulence in the past few years this has been somewhat surprising – survey results have shown that actual activity has exceeded expectations.

Construction and leasing activity has traditionally been dominated by the City/financial sector. However in the past three to four years there has been a reduction in the amount of space being built in the City (although the City still remains much more active than other areas) and a corresponding increase in the space taken by the TMT sector (generally by technology, with major projects for Apple, Amazon, Google and Facebook). With the continuing growth of the FinTech sector we consider how this trend will evolve.

In the same period we have seen significant growth and disruption by co-worker/ flexible space offerings, which now account for around 10 per cent of all new leasing, generally in new-build offices.

Talent remains a key business driver. London's ability to attract talent is crucial for businesses and their decisions to locate in London. Occupiers are therefore keen to ensure that they have premises that attract and retain the best staff, operate efficiently and increasingly respect carbon emission and sustainability concerns.

In an effort to understand changes in office construction in central London, our team of researchers have once again walked the streets across all the established and emerging submarkets. We have spoken to London's established developers to understand their plans going forward, as well as their current concerns around the current market.

The lack of clarity due to Brexit continues, with Parliament failing to break the deadlock over the timing and nature of Britain's departure from the EU. The upcoming General Election is compounding concerns for investors.

Whilst leasing remains resilient, investment volumes have weakened considerably and the PMI construction index has reported a contraction in construction industry activity for the sixth month in a row.

Have the worsening market conditions started to impact London office construction levels? Our survey provides you with a detailed analysis.

In this edition we also discuss the growth of the TMT sector, the emergence of FinTech and whether we will see financial services firms relocate to other European cities. We also discuss issues facing the real estate industry as a result of disruption caused by co-working, environmental challenges, and why we think the current shortage of available Grade A space is likely to drive construction in the short term.

We would like to thank developers and contractors who assisted with the data and took part in our surveys. We hope you find our survey results and insights useful and thought-provoking, and we welcome your feedback.

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**Director**
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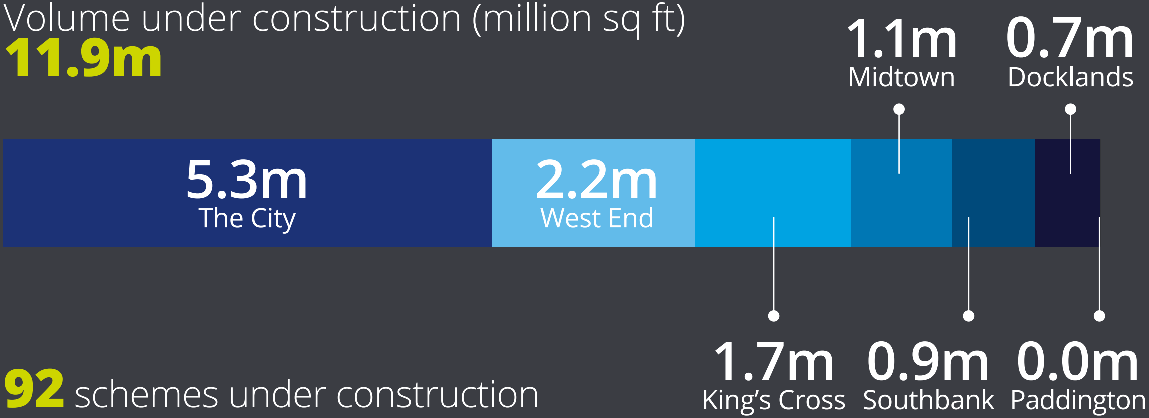
# London Office Crane Survey key findings


## Volume under construction (million sq ft)

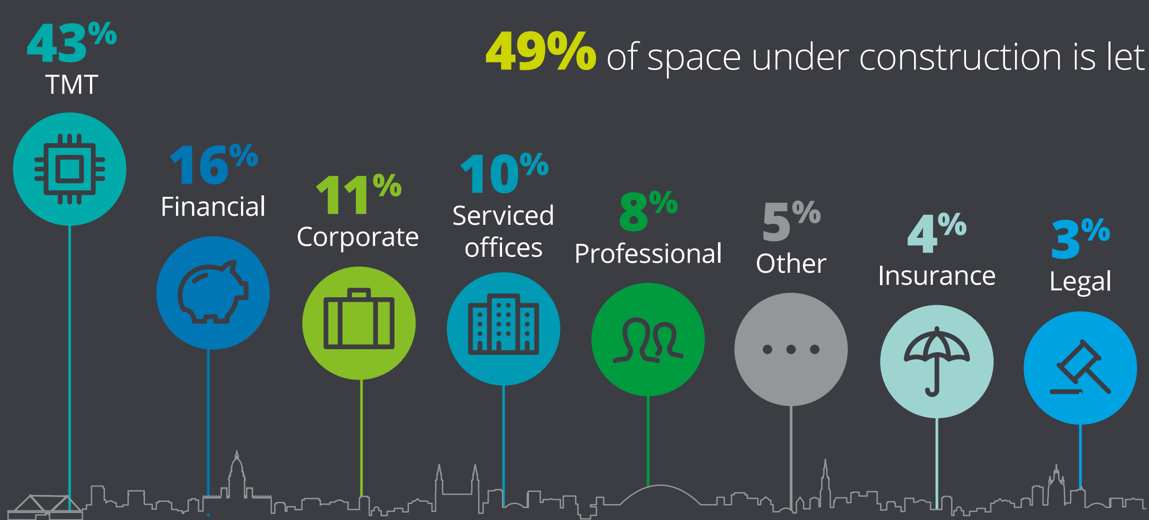
**11.9m**



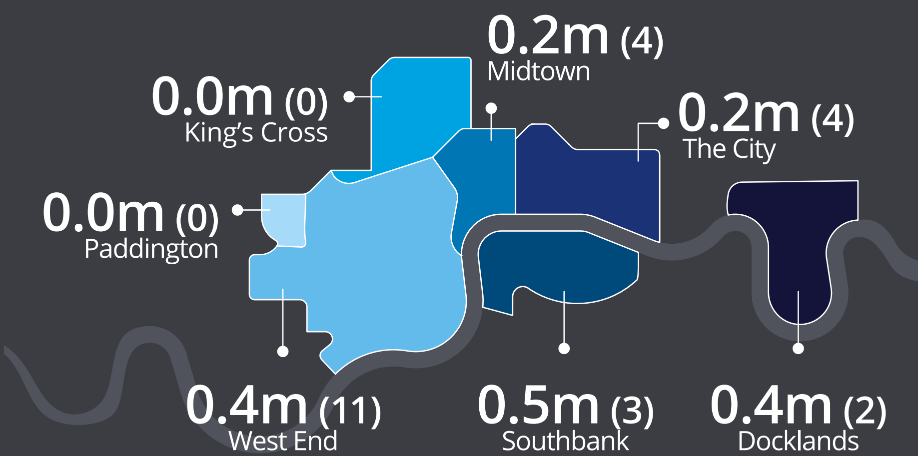

**92** schemes under construction

## Percentage of pre-completion space let by sector

**49%** of space under construction is let



## New construction starts: volume (million sq ft) and number




Total number of new starts
**24**

High (Q1 2016)
**51**

Average
**26**

Low (Q3 2010)
**4**

## Headline results

Office construction fell by **10%** on previous survey, to **11.9m sq ft**

**24** new schemes broke ground across **five submarkets**

**1.8m sq ft** of new schemes commenced, the **lowest volume** since Q1 2014

More new construction in the **West End** while **the City** slows

Completions surged by **44%** survey on survey, to **3m sq ft**

**43%** of space under construction is let to **TMT**

## Outlook

Slowing global growth adds to **recession risk**

Demand for **Grade A offices** will remain strong in order to attract the best talent

**Tech** will continue **expanding**, with FinTech emerging as one of the fastest growing sectors in London

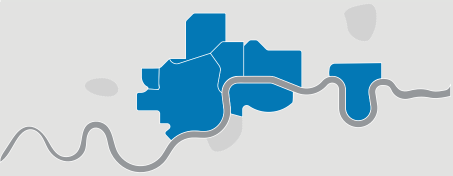
**'Plug & Play'** offices are here to stay

Tackling **climate change** moves up real estate agenda

**Long term pipeline softens**, while construction is increasingly driven by **pre-lets**

Source: Deloitte Real Estate

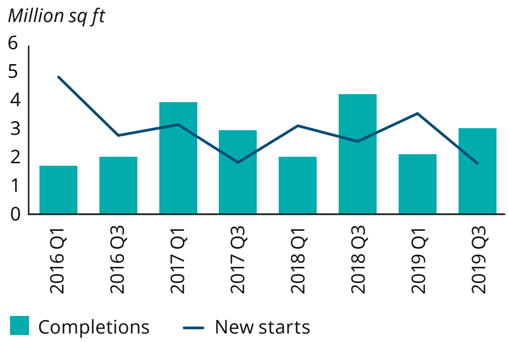
# Central London Crane Survey results



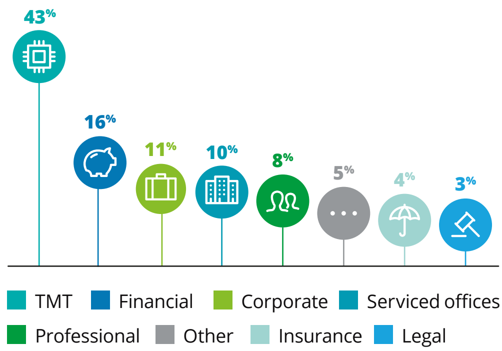
# Overview
# Central London

## Central London office pipeline

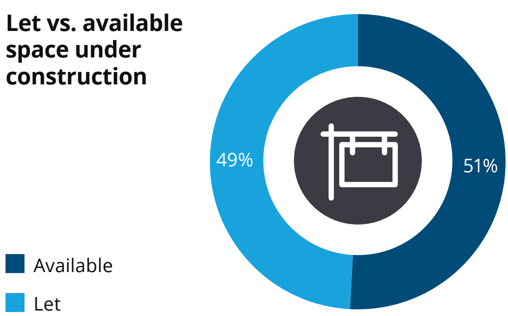

## Volume of new starts and completions



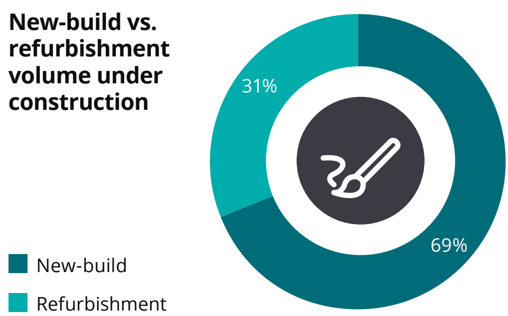

## What sector is taking the most space?




## Let vs. available space under construction




## New-build vs. refurbishment volume under construction




Source: Deloitte Real Estate

# Crane Survey Winter 2019 – findings

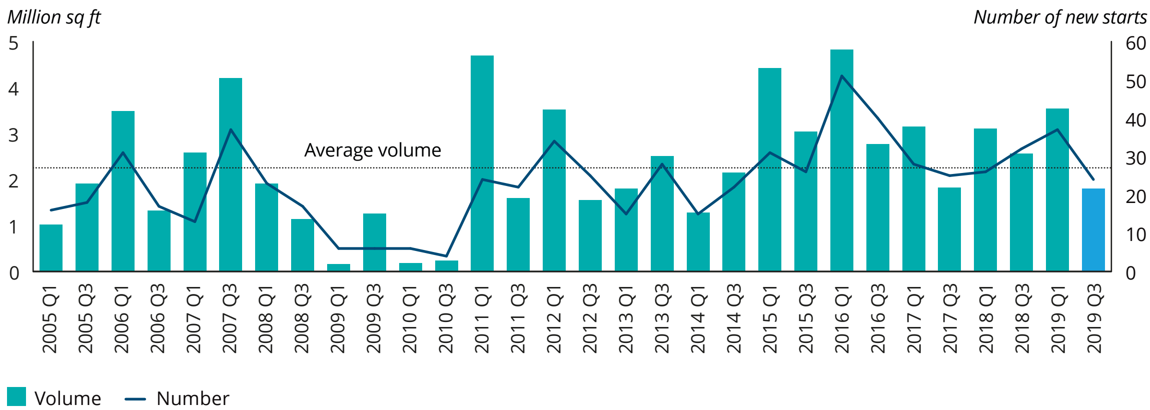
The London Office Crane Survey has long been regarded as a barometer of London's commercial property market and the wider economy. Against a backdrop of heightened Brexit uncertainty, we are now also facing the prospect of a global economic slowdown and unease created by the US-China trade war. Technical recession in the UK that many feared after the contraction in GDP in the second quarter will be avoided this year. On the upside, the labour market continues to support the economy through household spending, despite weak consumer confidence and slowing house price growth.

In the commercial property market, occupational demand has largely weathered recent political uncertainty, with office take-up in London remaining resilient. Investment volumes, however, have weakened considerably as the availability of stock has dried up. Whilst some prospective investors have adopted a 'wait and see' approach during this period of political uncertainty, many overseas investor groups remain keen to deploy capital.

The October PMI construction index, produced by IHS Markit, reported contraction in industry activity for the sixth month in a row due to client hesitancy and weaker demand, resulting in ongoing stagnation.

At 1.8 million sq ft, the volume of new starts falls almost 15% short of the long term six-monthly average of 2.1 million sq ft.

**Central London: Volume and number of new starts per survey**




Source: Deloitte Real Estate

## Lowest volume of new starts in over five years

Following the three-year high in construction starts reported in our previous Q1 report for the period between October 2018 and March 2019, this survey shows a 49% drop in volume between April and September for schemes over 10,000 sq ft.

At 1.8 million sq ft, the volume of new starts falls almost 15% short of the long term six-monthly average of 2.1 million sq ft, it is also the lowest figure since Q1 2014.

24 new schemes broke ground during this survey period, which is down from 37 in the previous report. The typical size of a new development also shrank by 22%, to an average of 75,000 sq ft.

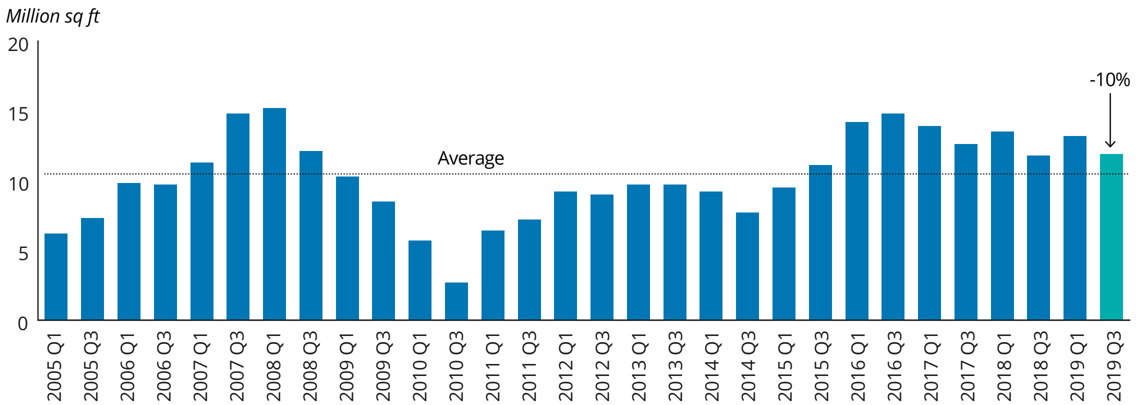
Several schemes were not included in the survey as 'new starts' because they were still in the demolition stage at the end of September. There is currently up to 3 million sq ft in demolition, which suggests that the next survey could see an uptick in new starts, albeit at a modest rate.

## The City's new construction tumbles

New construction activity varied across submarkets. **West End** led the way with 11 new starts, including seven refurbishments, followed by the City and Midtown, each with four new schemes breaking ground. **The City** was notably quiet, with only one new-build product and three small refurbishments, totalling a mere 200,000 sq ft. This is down significantly from the 1.2 million sq ft in 11 schemes reported in the previous survey.

On the other side of the river, **Southbank** witnessed an uptick in construction activity, with work starting on three new office buildings, including the biggest in the survey – the Bankside Yards 220,000 sq ft office development. This is the first phase of a 1.4 million sq ft mixed-use project that will redevelop the south side of the river between Tate Modern and Blackfriars Bridge.

**Central London: Total volume under construction per survey**




Source: Deloitte Real Estate

**Docklands** also experienced a rise in new activity, in two schemes totalling 400,000 sq ft, both of them new-build. There were no new starts in **Paddington** during this survey period, but three sizeable schemes are currently in demolition and are likely to feature in the next survey, including the Paddington Square development, which will comprise 360,000 sq ft of office space.

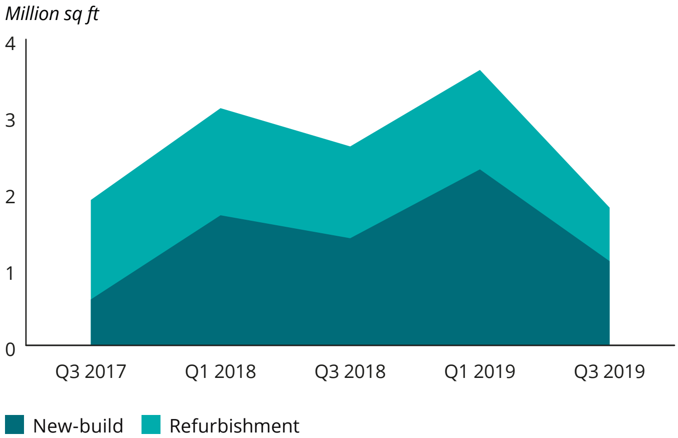
Both new-build and refurbished construction declined sharply (see graph). New-build starts fell by 54% compared to the previous survey, while refurbishments were 41% lower across central London. The proportion of new-build versus refurbishments remains broadly in line with our three previous surveys: just over half were new developments.

### Overall construction volume is down but remains above long-term average

The overall volume of office space under construction in London totalled 11.9 million sq ft across 92 schemes as at the end of September. While this figure is down by 10% from the previous survey, it remains above the long term average of 10.6 million sq ft. The average size of schemes under development is currently 130,000 sq ft, down by 12% from the previous survey average.

Construction levels in **the City** have been declining gradually over the past few years. In this survey, there were 5.3 million sq ft under construction in the City, representing 45% of activity in central London. However, this is considerably lower than the 8.8 million sq ft and 59% of the total construction volume reported in Q3 2016. An even lower volume had been expected in this survey due to the anticipated completion of the 1.3 million sq ft 22 Bishopsgate during Q3 2019, but this has been delayed until Q1 2020.

**Central London: New starts – new-build vs. refurbished**




Source: Deloitte Real Estate

In contrast, the **West End** has been experiencing a steady rise in construction activity over the same period. There were 35 separate office buildings under construction that will add 2.2 million sq ft of new and refurbished office stock. Key schemes currently under development in the area include 321,000 sq ft 80 Charlotte Street in Fitzrovia, and 312,000 sq ft Regent's Place, near Euston Station, which is fully pre-let to Dentsu Aegis Network.

The levels of office development remained relatively unchanged in Midtown and King's Cross. Paddington recorded no active schemes under construction; however this submarket is expected to see a number of new starts in the coming months.

The overall volume of office space under construction in London totalled 11.9 million sq ft across 92 schemes as at the end of September.

## Completions are up but the 2019 total will fall short of 2018

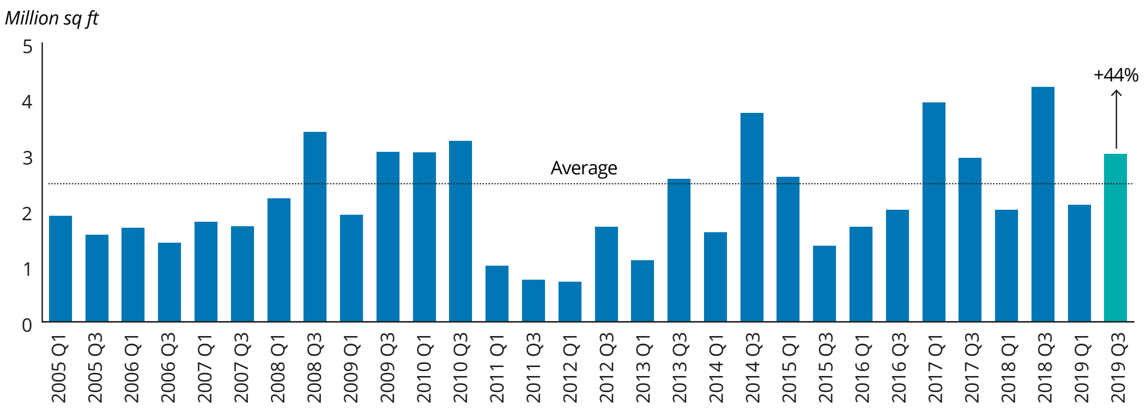
As we forecast in the previous report, completion volumes surged between April and September, by 44% to 3 million sq ft. The largest completion was the 870,000 sq ft 100 Bishopsgate in the heart of the City of London. This 37-storey office tower stands 181 metres tall and is 90% let to a range of tenants, ranging from financial and legal firms to serviced office providers. Another sizeable completion was the 27-storey One Bank Street in Docklands. This 690,000 sq ft office building is now fully let to Société Générale and the European Bank for Reconstruction and Development.

Despite our expectations earlier this year, the total completion volume for 2019 is set to fall short of the 2018 figure, by 23%. This is largely because of a delay in some large schemes, including 22 Bishopsgate. As shown in the graph on page 5, 2020 is now likely to reach just over 6 million sq ft, which is in line with the 2017 and 2018 figures.

In **the City**, 2.4 million sq ft of office space is expected to complete in 2019, down from the 2018 total by just under a third. However 2020 will see around 3.3 million sq ft delivered to the City office market, matching the 2018 total. The pipeline in the City includes the 'Gotham City' development at 40 Leadenhall Street, which has recently attracted £875 million of investment. It will consist of 34-storey skyscraper and a smaller tower of 14 storeys, providing up to 905,000 sq ft of space in total.

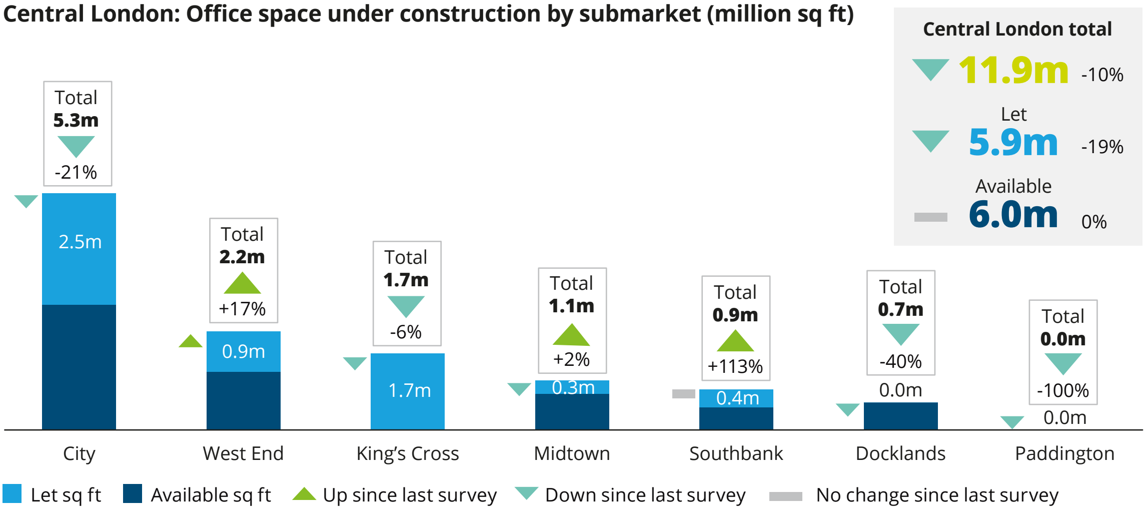
Office completions in the **West End** this year are forecast to reach a level similar to 2018. The recent surge in construction activity in the area will translate into 1.5 million sq ft of new and refurbished stock in 2020, the highest level of completions since 2013 (see page 16).

**Central London: Total volume of space completed per survey**




Source: Deloitte Real Estate

**Central London: Office space under construction by submarket (million sq ft)**




Source: Deloitte Real Estate

## Pre-letting is driving office demand

Ensuring the best quality office space is of growing importance for businesses wanting to attract and retain talent, with buildings increasingly seen as an integral reflection of an organisation's brand. In order to secure their preferred options, businesses are having to launch their searches at least two years in advance of the expiry of current leases.

As in previous surveys, the pre-letting market continues to be strong, driven by the scarcity of 'ready to occupy' Grade A accommodation, especially for larger requirements. Space currently under construction is 49% let and for size ranges of above 100,000 sq ft, the proportion edges close to 60%.

Pre-let rates vary widely by sub-market. In relatively new office sub-markets, like King's Cross, the large scale construction and re-development undertaken has been conditional on pre-letting. By contrast, the West End sees fewer pre-commitments. This is because the scale of development is much smaller and, as an established area with high rents, the risk associated with speculative development is lower.

As in previous surveys, the pre-letting market continues to be strong, driven by the scarcity of 'ready to occupy' Grade A accommodation, especially for larger requirements.

### Tech continues to expand

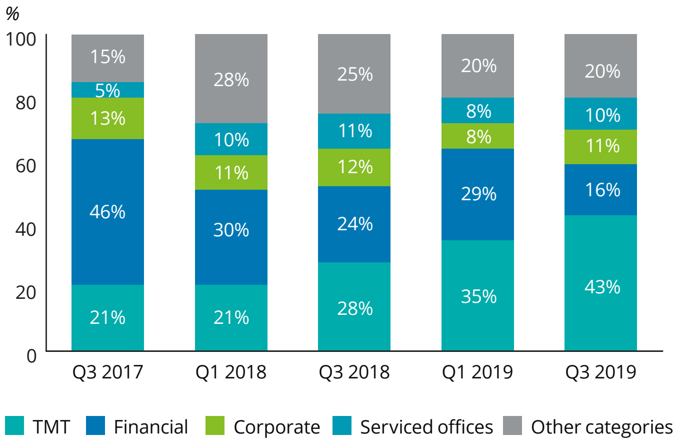
Technology, media and telecoms (TMT) has further increased its share of pre-let space under construction, from 35% to 43%. Submarkets that have traditionally competed for financial workers, such as the City and Canary Wharf, are now looking increasingly to lure TMT tenants from other areas. This confirms the continuing importance of the TMT sector in the London leasing market: we explore why this sector will continue to expand in the *Key Themes and Outlook* section of this report.

Serviced office providers' appetite for London offices has remained steady, amounting to 10% of the space under construction. Given recent announcements, we are likely to see a dialling down in the coming months in letting activity from WeWork, which is currently committed to 4.1 million sq ft across London. Read more on flexible office providers in the *Key Themes and Outlook* section.

### Developers less optimistic than six months ago about leasing demand

The past three years have seen strong and sustained demand for new and refurbished office space in London. In fact, London office take-up in both 2017 and 2018 comfortably exceeded long-term averages. This has been somewhat counter to expectations, given ongoing uncertainties around whether, when and on what terms the UK might leave the European Union. The take-up in the first three-quarters of this year softened but remained above average, suggesting healthy demand for office space.

**Central London: Percentage of pre-completion lettings by sector**

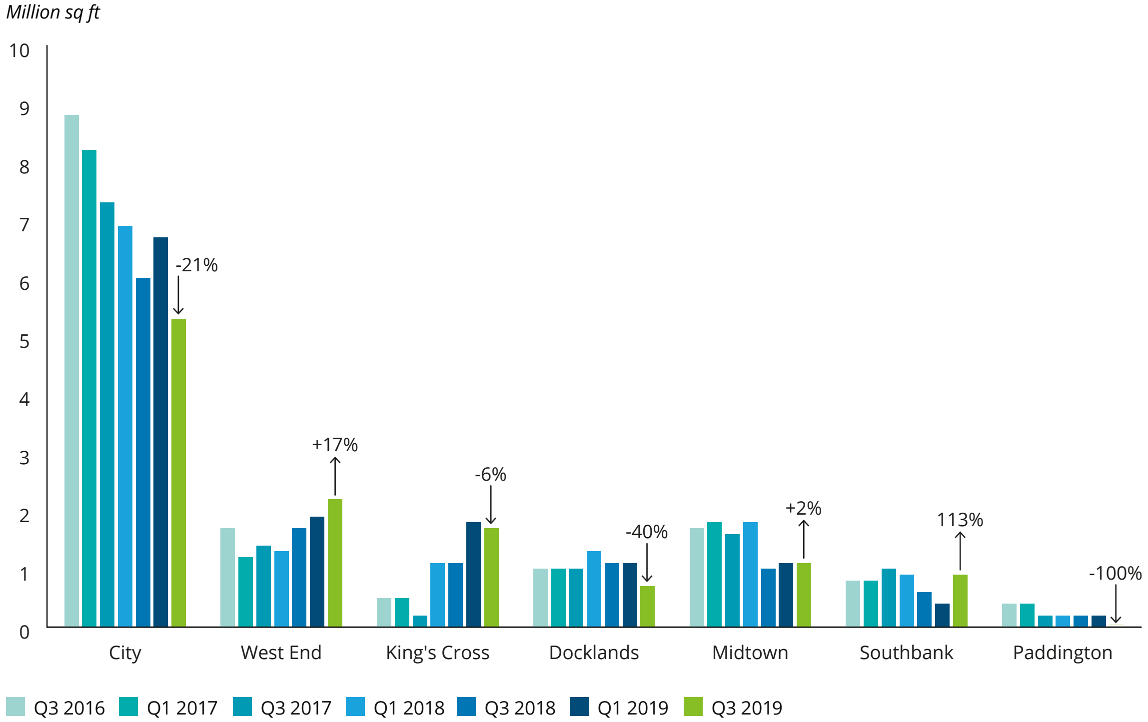



Source: Deloitte Real Estate

Serviced office providers' appetite for London offices has remained steady, amounting to 10% of the space under construction.

However, developers we interviewed for this survey were more pessimistic about the leasing market than six months ago. 40% indicated an appetite for office space that was 'a little worse', up from 27% in Q1 2019. 42% expressed 'no change' in sentiment, down from 56% in the previous survey. Less than a fifth (18%) expect the leasing market to be 'better'. No one thought that leasing conditions will be either 'very good' or 'very bad'.

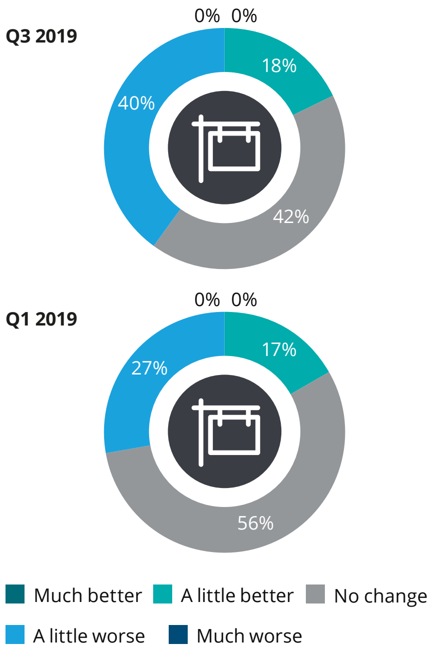
**Central London: Total volume under construction per survey**




Source: Deloitte Real Estate

Construction levels in the City have been declining gradually over the past few years. In this survey, there were 5.3 million sq ft under construction in the City, representing 45% of activity in central London.

**Developer survey: "Compared to six months ago, how do you currently perceive the leasing market?"**




Source: Deloitte Real Estate

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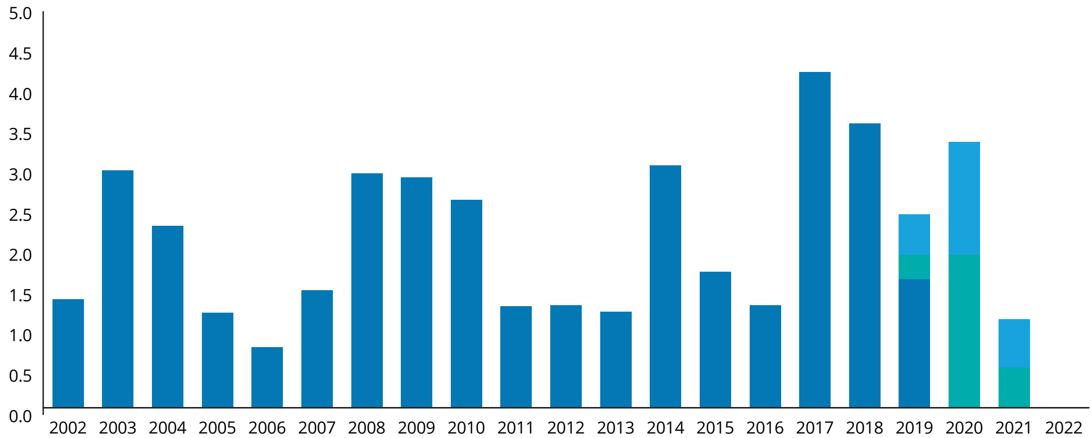
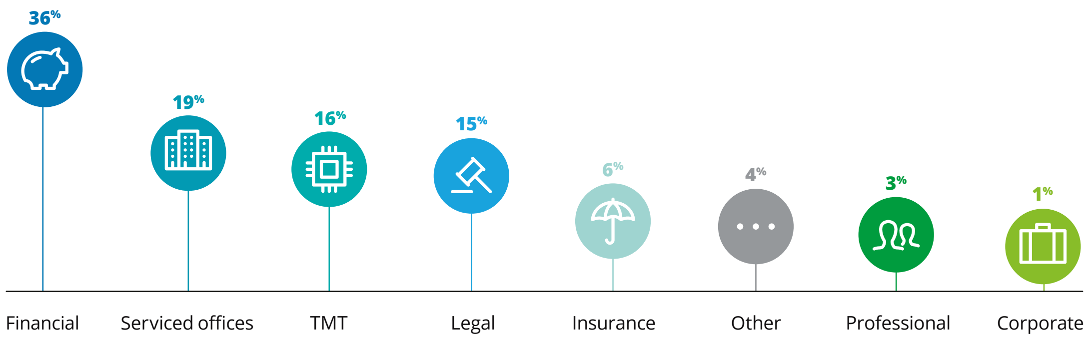
# Central London submarket snapshots

# Submarket snapshots
## The City

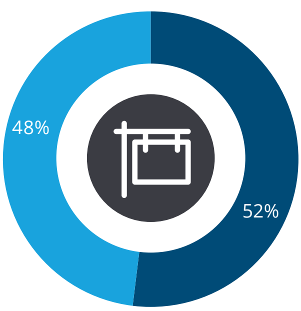
### The City office pipeline



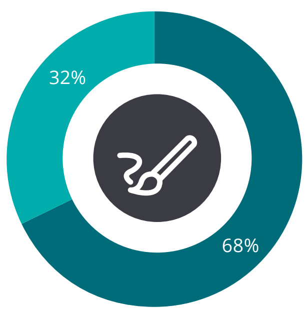

### What sector is taking the most space?




### Let vs. available space under construction




### New-build vs. refurbishment volume under construction

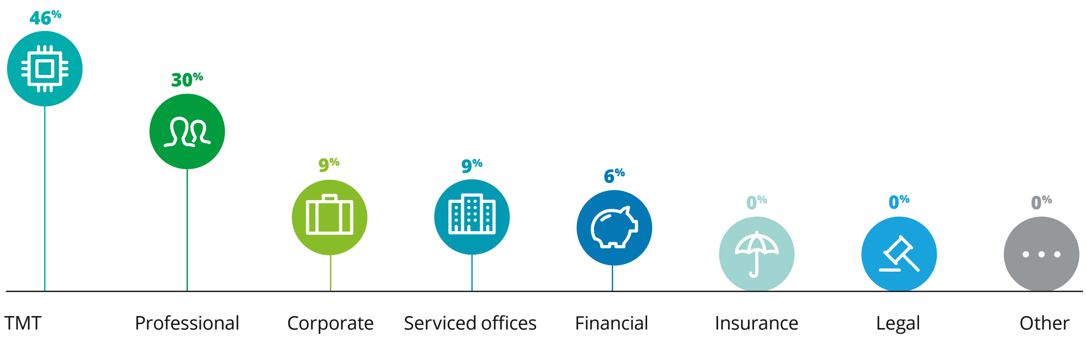



Source: Deloitte Real Estate

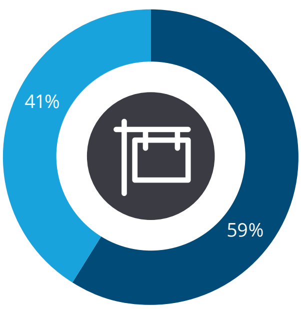
# Submarket snapshots
## West End

### West End office pipeline


### What sector is taking the most space?



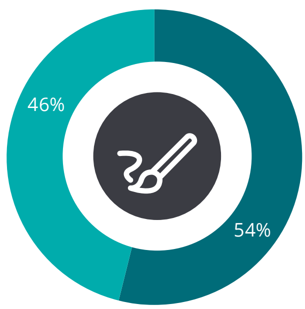

### Let vs. available space under construction




Available

Let

### New-build vs. refurbishment volume under construction



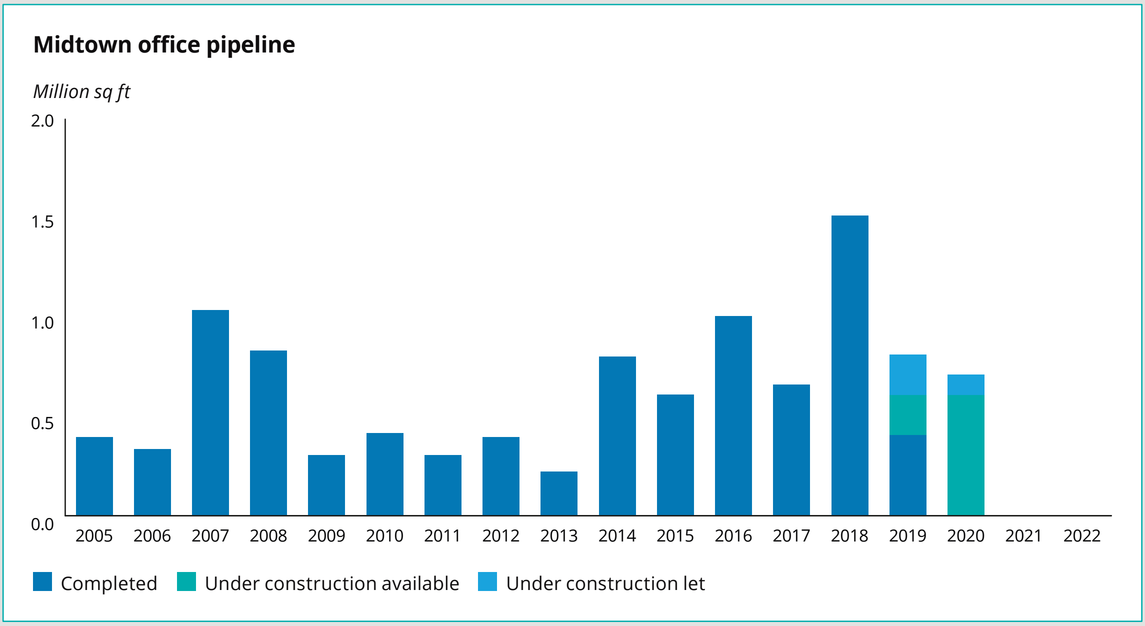

New-build

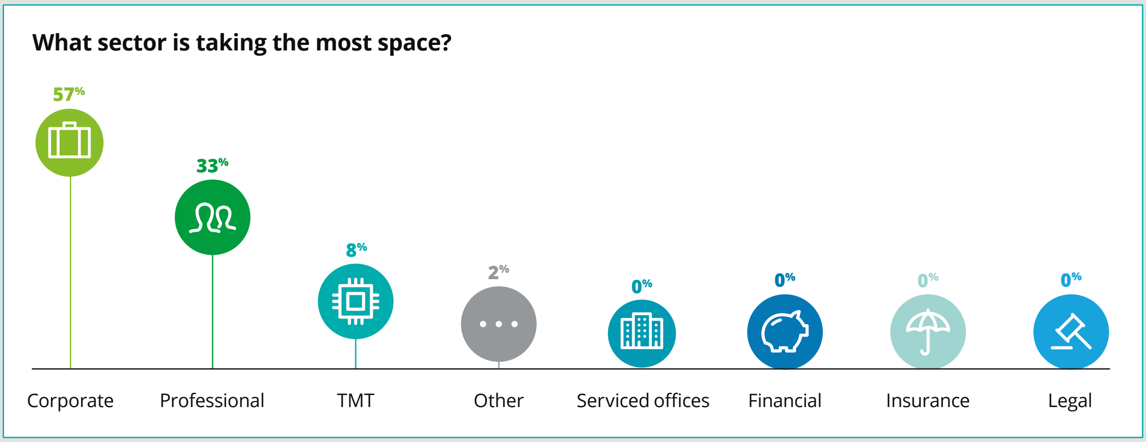
Refurbishment

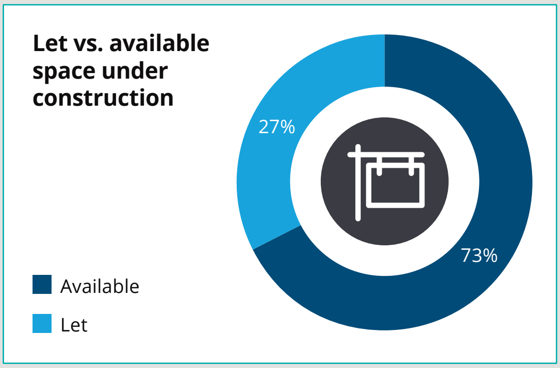


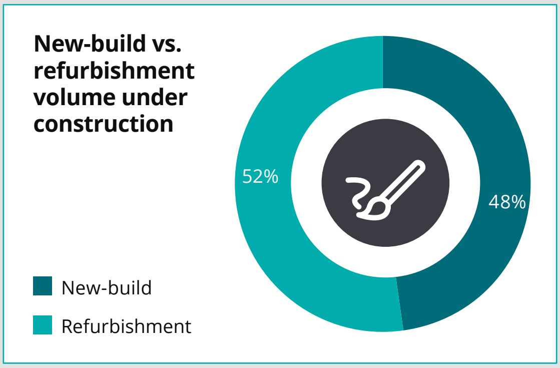
Source: Deloitte Real Estate

# Submarket snapshots
# Midtown



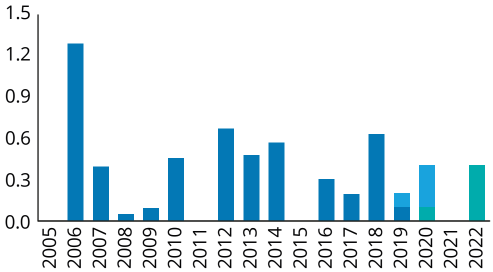




Source: Deloitte Real Estate

# Submarket snapshots
## Southbank and Docklands

### Southbank office pipeline

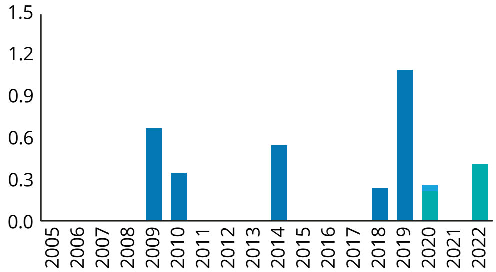
*Million sq ft*




Completed U/C available U/C let

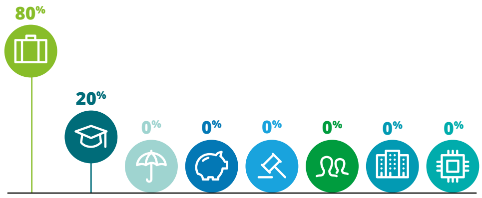
### Docklands office pipeline

*Million sq ft*



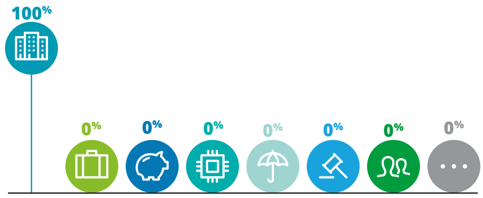

Completed U/C available U/C let

### What sector is taking the most space?



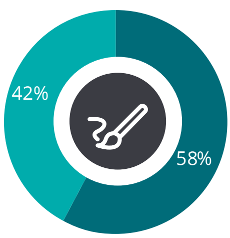

Corporate Education Insurance Financial
Legal Professional Serviced offices TMT

### What sector is taking the most space?




Serviced offices Corporate Financial
Insurance Legal Professional TMT Other

### New-build vs. refurbishment volume under construction

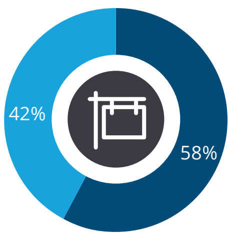



New-build
Refurbishment

### New-build vs. refurbishment volume under construction

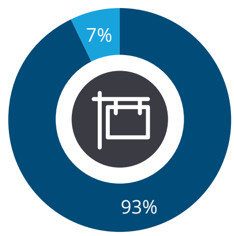

New-build
Refurbishment

### Let vs. available space under construction




Available
Let

### Let vs. available space under construction



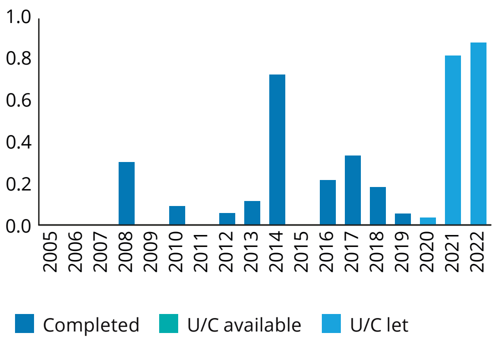

Available
Let



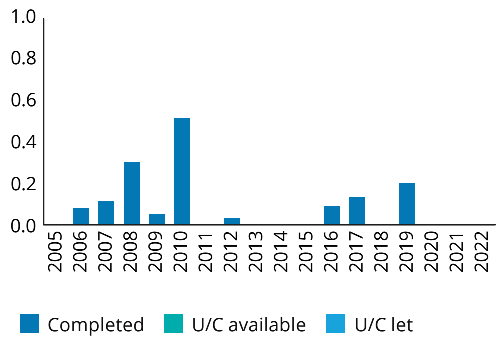
Source: Deloitte Real Estate

# Submarket snapshots
## King's Cross and Paddington

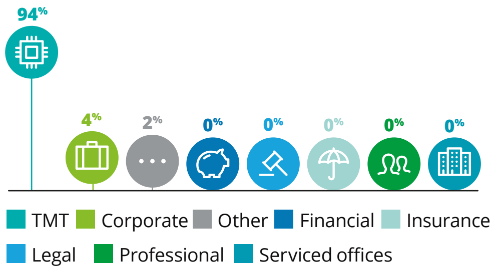
### King's Cross office pipeline




### Paddington office pipeline




### What sector is taking the most space?

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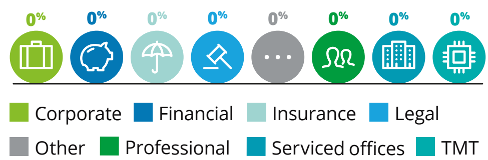
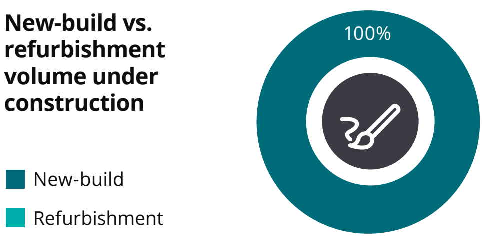
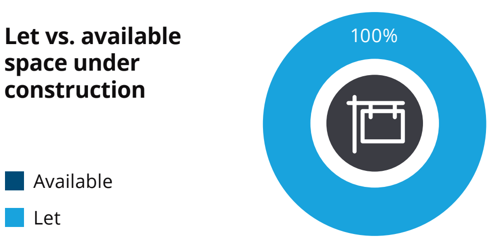



### New-build vs. refurbishment volume under construction




### New-build vs. refurbishment volume under construction


### Let vs. available space under construction




### Let vs. available space under construction


Source: Deloitte Real Estate

# Emerging submarkets Crane Survey results

# Emerging submarkets Crane Survey results

## Construction activity remains unchanged

Construction activity in emerging London submarkets (Stratford, Vauxhall-Nine Elms-Battersea, and White City) has remained unchanged for the third survey in a row: there were no new starts or completions. These three submarkets have a combined volume under construction of 1.3 million sq ft, with several large schemes due for completion in the next few months.

In **Stratford**, S9 – The International Quarter and 14 Westfield Avenue are both nearing completion. The 300,000 sq ft 14 Westfield Avenue is now fully pre-let to HMRC and will become its regional centre as part of the wider Government Hubs programme. The excellent transport links (Stratford will have a Crossrail station), and considerably lower rents and business rates for Grade A space, in comparison to central London, continue to provide a stimulus for relocating to the area.

In the **Vauxhall-Nine Elms-Battersea** submarket, the fully pre-let Battersea Power Station is scheduled to complete in Q4 2020, when it will deliver 520,000 sq ft. The 'next phase' of construction is expected in Q2 2021 when it will start developing 750,000 sq ft of office accommodation, due to be completed by the end of 2023. In Nine Elms, a planning application has been submitted for a 13-storey office building at the heart of the Embassy Gardens development, to be known as EG:HQ, close to the US Embassy which opened in January 2018. If approved, the building will provide 217,000 sq ft of office space and construction could begin early next year. The scheme will be next to One Embassy Gardens, which is currently under construction.

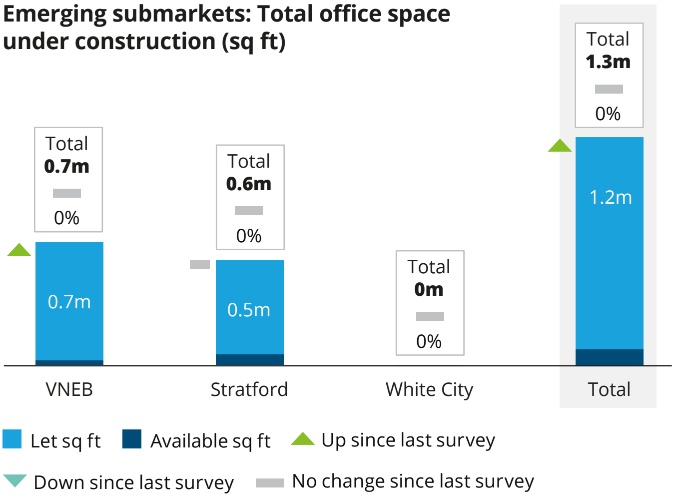
There is presently no construction activity in **White City**, but there are a number of schemes in the pipeline, including White City South. The Imperial College masterplan, which has recently been approved, will bring to the West London neighbourhood 1.9 million sq ft of space dedicated to research and business use.

## Pre-lets will trigger new construction

Construction activity in emerging submarkets is inevitably more volatile than in the more established and mature areas of central London. Development will often not start until there is a tenant in place, which will endorse the location and attract other businesses to the area. This occupier-led demand provides the stimulus for new construction, unless a developer steps in with a major 'bold play' proposition.

Of all the office space currently under construction in emerging submarkets, 93% is currently pre-let, leaving only 87,000 sq ft of available space across two schemes. These emerging submarkets have been attracting a diverse range of occupiers, from large tech firms, to serviced office providers, research charities and the public sector. The construction in new areas shows that businesses no longer restrict themselves to traditional business and financial zones, choosing locations with excellent transport links and local amenities.

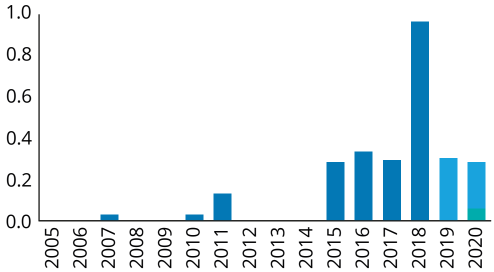
**Emerging submarkets: Total office space under construction (sq ft)**



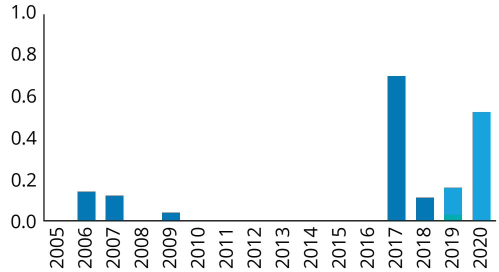

Source: Deloitte Real Estate

# Emerging submarket snapshots
## Stratford, VNEB and White City

### Stratford office pipeline




### VNEB office pipeline

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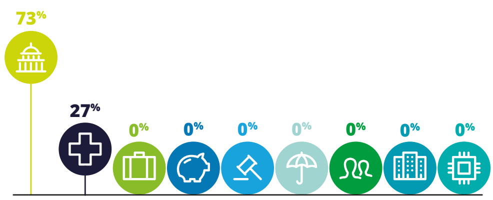


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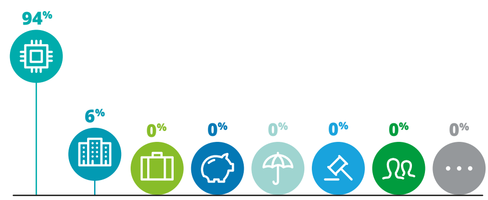


### New-build vs. refurbishment volume under construction

New-build
Refurbishment


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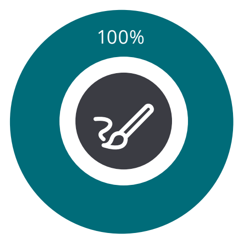
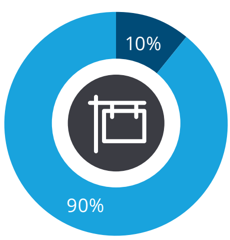
New-build
Refurbishment



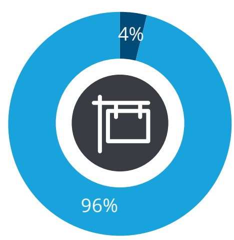

### Let vs. available space under construction

Available
Let




### Let vs. available space under construction

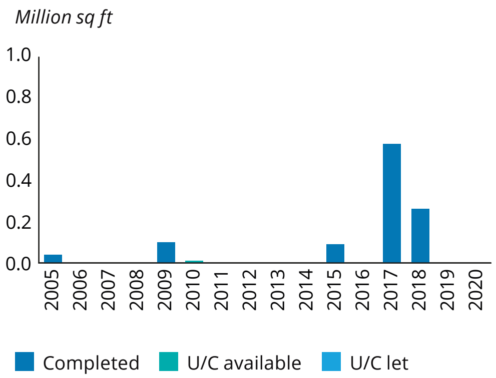
Available
Let






Source: Deloitte Real Estate

### White City office pipeline

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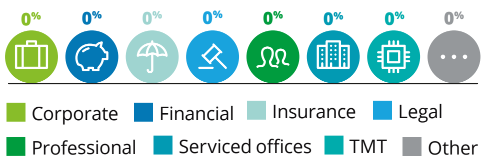


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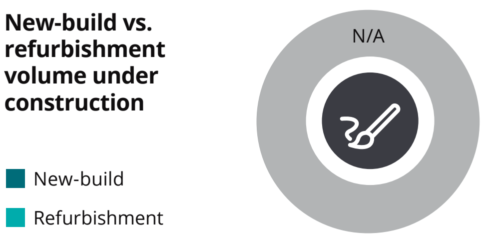


### Let vs. available space under construction


Source: Deloitte Real Estate

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# Key themes and the outlook

# Key themes and the outlook

## Slowing growth adds to recession risk

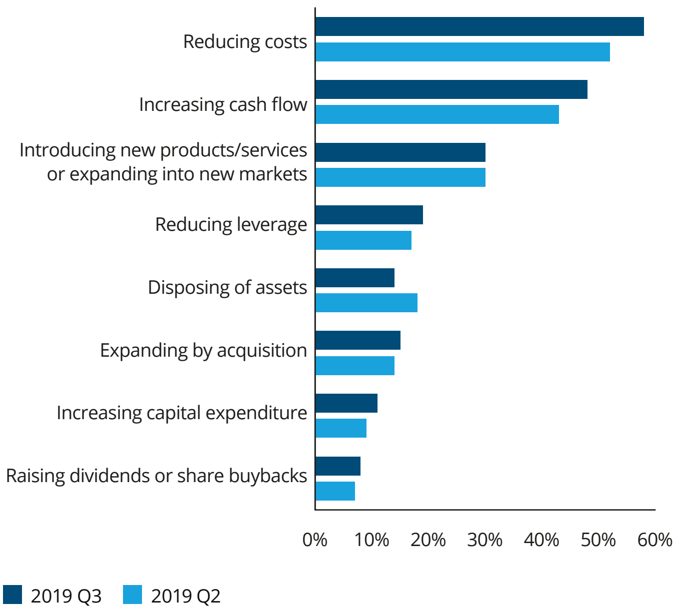
The lack of certainty around Brexit continues, with a hung Parliament failing to break the deadlock over the timing and nature of Britain's departure from the EU.

While the UK is likely to have avoided a technical recession in the third quarter, GDP growth remains soft following contraction in the second quarter.

The global economy has also been showing signs of weakness, with the OECD and IMF downgrading their growth forecasts for 2019. This is due in part to the ongoing US China trade war, with both countries announcing new tariffs. Downside risks are, therefore, continuing to mount, taking their toll on confidence and investment, and threatening already weak growth prospects.

Deloitte's *Q3 2019 UK CFO Survey* confirms that the slowing economic growth and ongoing uncertainty in the UK have affected corporates' strategies. The survey reported that 58% of CFOs rated cost reduction as their top priority, the highest level in ten years, and higher even than when the economy was emerging from financial crisis in late 2009. Brexit continues to be seen by corporates as their greatest risk. Over the past three months, CFOs have also become much more concerned about the headwinds caused by slowing growth in the UK and the EU.

**% of CFOs who rated each of the following as a strong priority for their business in the next 12 months**




Source: Deloitte *CFO Survey: Q3 2019*

Brexit continues to be seen by corporates as their greatest risk. Over the past three months, CFOs have also become much more concerned about the headwinds caused by slowing growth in the UK and the EU.

### Banks stay loyal to London, for now

The ability to recruit a young and highly-skilled workforce from the international labour market will be key to the UK's post-Brexit economy. However, with UK unemployment at historically low levels and accelerating wage growth, the UK could soon face recruitment difficulties.

The exodus of jobs from London's banking and finance sectors to other European financial centres such as Frankfurt, Paris and Dublin has been limited to date.

"The cost of relocation is significant, far bigger than originally expected. The relocation packages of moving experienced staff from London includes housing, schools and other perks to entice Londoners to move. Add legal and travel costs and staying in London becomes a cheaper option."

**Zahir Bokhari, Partner, Deloitte**

After the financial crisis, the UK government implemented new rules to protect the economy and taxpayers from problems in the banking system. These required large UK banks to 'ring-fence' their core banking services, which resulted in moving some operations into the regions. However this is not a Brexit-related change, and employment in financial services in London has remained relatively steady.

As banks automate more processes to cut costs, they are recruiting more in countries where they can find skilled workers, in areas such as technology and risk management, at a fraction of the cost seen in the main Western European financial centres. Poland for example has seen a surge in advertised jobs in financial services in recent years, suggesting that global banks are increasingly looking to reduce costs this way.

### Tech will continue expanding, with a possible arrival of Chinese firms

Tech expansion in London continues apace. According to a recent study from *London & Partners*, the official promotion agency for the UK capital, London is currently the top destination for international tech companies looking to expand or set up an operation outside their own country. In the past year, 91 international tech firms have chosen to open offices in London, with total investments worth £864 million, more than Singapore, Paris and New York. APSCo *(The Association of Professional Staffing Companies)* also confirms this trend, reporting that the tech sector recorded a 44% increase in hiring activity in the UK year-on-year. The TMT sector saw a 32% rise in demand for talent in the 12 months to mid-2019.

The international tech giants, which already have a presence in the capital, are also likely to diversify their offerings and expand into competitors' areas, such as advertising, TV and video. The mobile gaming industry, in particular, is likely see a rapid growth going forward, potentially increasing demand for London office space.

Furthermore, the UK has not yet seen arrival of large Chinese tech firms. With the current US-China trade war and restrictions introduced by the US government, more Chinese firms could possibly set up their foreign base in London. The slowdown in economic growth in China might also persuade them to choose expansion in Europe, including London.

## Paul Lee, Head of TMT Global Research, Deloitte

**Q. With the recent increase in their office footprint in London by some of the largest global tech firms, how much more growth can we expect in the coming years?**
All these large companies may need to continue to grow to justify their valuations (especially the multiples). They are going to diversify out of their core areas into other tech companies' territories. Mobile games also remains a growing industry. When you hit it big in games, rewards are significant. The challenge is to develop a scale a game that lasts for years and years.

**Q. China boasts nine of the world's 20 largest tech companies. Are any Chinese tech giants looking to increase their presence in London?**
There are a number of geopolitical headwinds at the moment, including the restrictions placed by the US government on certain Chinese companies from operating in the US. Furthermore, the Chinese domestic economy is now experiencing a lower level of growth than has been the norm over past the past decade. For both reasons, Chinese tech firms may increasingly look to Europe in order to deliver their expansion plans.

**Q. What impact will Brexit have on the UK's tech talent pool?**
Depending on the outcome, there may be less migration from Europe, but more from outside Europe to counterbalance this. The key reason tech companies are attracted to London is because of its deep talent pool. It is important that Brexit should not diminish London's attractiveness.

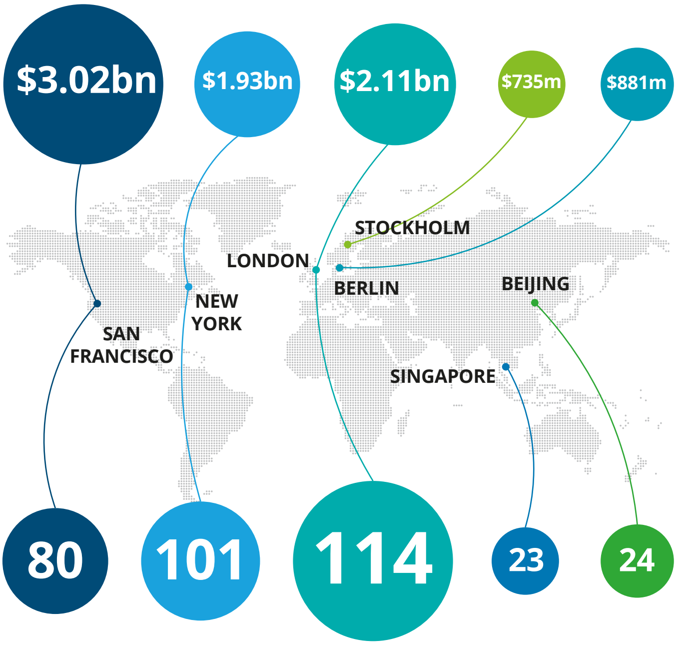
### FinTech is now one of the fastest growing sectors in London

Over the past decade, innovation has revolutionised financial services, with the rapid growth of FinTech. London in particular is being transformed into a leading hub of global FinTech innovation. The main reasons why London appeals to FinTech firms are because of the already-established financial markets and deep tech talent pool, as well as supportive regulation.

According to *Innovate Finance*, London has now overtaken New York for FinTech investment deals. London also leads overall FinTech investment in Europe by a large margin, attracting $2.11 billion investment between January and August 2019 in comparison to Berlin ($881 million), Stockholm ($735 million), Paris ($330 million) and Milan ($49 million).

**A city comparison of global FinTech investment in 2019**

**Top cities by deal value in 2019 (to August) ($) and deal count**




Source: A Fine Year for FinTech: Global Trends from a UK Perspective, London & Partners, Innovate Finance

There are currently 44,000 people who work specifically in FinTech roles in London – more than in Silicon Valley or New York. The number is likely to increase substantially over the next decade. FinTech thrives in ecosystems built around incubators and entrepreneurs, as well as universities. The recent proposal by the Home Office to extend the post-university visa to two years for those who have studied in the UK has been welcomed by the FinTech industry. Brexit therefore represents a challenge to the future FinTech talent pool.

"FinTech firms choose London over other cities for four main reasons: access to talent, and proximity to customers, investors, and the regulator. A London based FinTech founder can see a client or job candidate in the morning, an investor for lunch, and the regulators in the afternoon.
There are only a handful of cities in the world able to compete with that."

**Thomas Rees, Head of Business Development, Deloitte**

## HR is influencing real estate decisions

In a tight labour market, retaining staff is of the utmost concern. According to the *Deloitte Global Millennial Survey 2019*, 49% of individuals would, if they had a choice, quit their current jobs in the next two years, and about a quarter actually do so. Changing jobs is often seen as a way to broaden skills and experience, as well as advance careers with new employers. The high turnover in the competitive labour market is, however, very disruptive and costly for employers.

To address this concern, providing the best-quality office space has rapidly become an essential ingredient in recruitment and productivity strategies. Corporates are having to consult HR when choosing office accommodation and the fit-out. Wellbeing has gone from being a 'buzzword' to something that is now firmly on the workplace agenda. Office space with built-in wellness features, such as good acoustics, natural light, and high water and air quality, are seen as a way to lure talent, improve staff retention and increase productivity.

Importantly, flexible working arrangements have become essential in recruitment strategies, but they also allow tenants to utilise space more efficiently. Thanks to these changing working patterns, office density has risen by a fifth over the past two decades, and this trend is likely to continue. By encouraging remote working, businesses are able to reduce costs by creating high quality space but occupying less space overall.

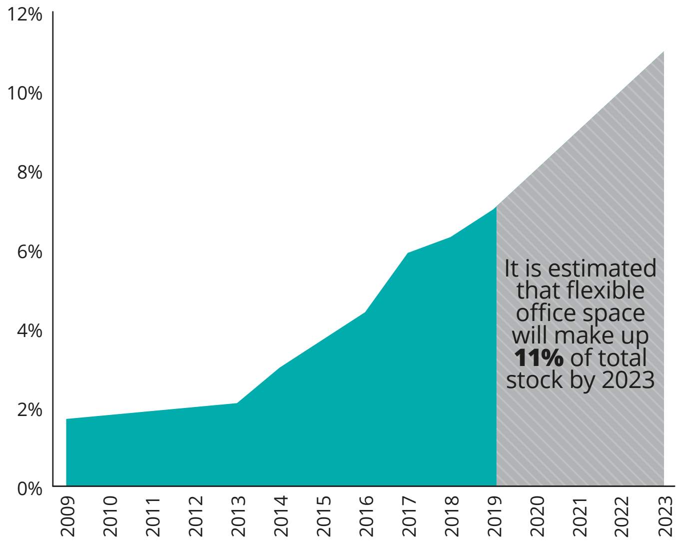
## ‘Plug & Play’ offices are here to stay

The rapid growth in co-working is well-documented and has fundamentally disrupted the commercial property market. Flexible workspace providers typically take long leases on properties, which they then refurbish/fit-out and let to occupiers on all-inclusive contracts for much shorter periods than traditional landlords.

Given the biggest vendor caters for only about one per cent of London's working population, and there are concerns over its future, co-working has gone mainstream. Although WeWork currently dominates the headlines, the London serviced offices market is highly fragmented. According to *Hubble*, there are more than 150 providers in London with some form of co-working space, in more than 650 separate locations. The flexible office and co-working markets have grown over the last five years to 6% of overall office stock in London, and *Hubble* forecasts this figure to increase to 11% by 2023.

As well as leasing space directly to serviced office firms, the more established landlords have now started to look for new ways to market their properties in order to meet the demand for office space on more flexible terms. Many have responded by forming their own flexible office platforms and offering a mid-point, where the landlord provides design features that make the space ready for occupation immediately. This ‘plug and play’ solution makes the office space more attractive to occupiers who want the flexibility, but not necessarily to share space, and who can do without the perks associated with the co-working model.

**The growth of flexible office space in central London as a percentage of the total office stock**




Source: 'Flex and the City 2019' Hubble

Traditional landlords are also beginning to recognise that they need to cater for small businesses, which have been avoiding conventional leases, as well as for larger organisations. Large companies have gradually been making more use of flexible workspace when seeking temporary accommodation for expansion or for specific projects. Recently, a large investment bank took over a co-working area for disaster recovery trading in the event of Brexit disruption. Another large bank secured 280,000 sq ft at WeWork’s Two Southbank Place.

## Is real estate doing enough to tackle climate change?

Real estate is estimated by the *United Nations* to consume 40% of energy globally and account for 20% of carbon dioxide emissions. With the current focus on changes to the earth's atmosphere and ecosystems, environmental issues have risen up the international political agenda and in the consciousness of employees. Businesses are beginning to recognise that to attract the talent, particularly among the younger generations, they must provide office accommodation that is energy-efficient, with low carbon dioxide emissions, and constructed from sustainable materials.

In September this year 23 property firms, with more than £300 billion of assets under management, signed up to the *Better Buildings Partnership* pledge to tackle the growing risk of climate change by delivering net zero carbon real estate portfolios by 2050. Signatories will also report annually on progress against their pathways and reveal the energy performance of their portfolios as a way to improve transparency within the market. This applies to both new and existing schemes, and covers both operational and embodied carbon for the whole building, including the energy consumed by tenants.

The pledge to reduce carbon dioxide emissions is however likely to affect landlords' profits, and it raises questions about the future of new-build development versus refurbishments. Adding the disruption caused by providers of flexible working space, including shorter flexible lease terms, together with rising construction costs, office development is looking increasingly costly. Equally, landlords who do not engage in this climate change agenda are exposed to related risks that may lead to accelerated obsolescence and falling property values.

## Property developers think long term

There is no denying that investor appetite has been tempered by Brexit uncertainty, and some investors will think long and hard before committing. Others are sitting on the sidelines waiting to see how Brexit plays out. In addition to uncertainty about whether and on what terms the UK leaves the EU, there is trepidation amongst investors regarding the outcome of the General Election.

It is clear that the drop in transaction volumes in the London office market this year has delayed or deterred some developers from pushing ahead with projects. However, property investors and developers tend to take a longer-term view, especially when locking into a large-scale office project. Unlike other types of investment, property development is an enterprise spanning years, from finding a suitable site and securing finance and planning consent, to construction and eventual sale of the asset. For example, the 'Gotham City' development has struggled to get off the ground since it obtained approval in 2014 and construction is only set to start in March 2020 with scheduled completion by the end of 2023.

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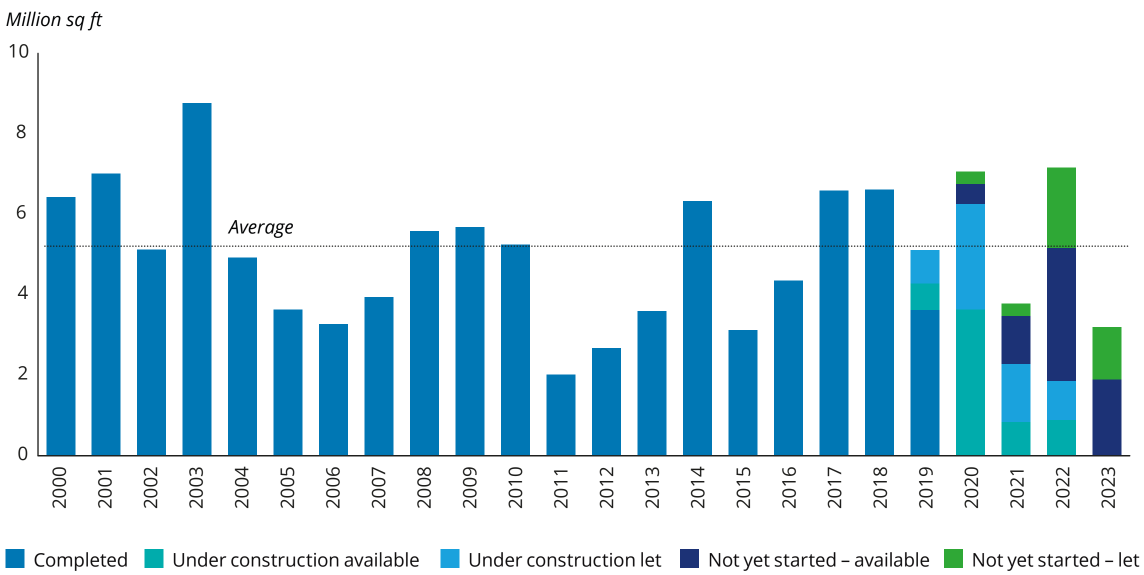
### The London skyline – not quite what it seems

To the casual observer the many tower cranes in the London skyline would suggest that there is a large amount of office accommodation for occupiers to choose from. In reality, however, much of the office space currently under construction is under offer or pre-let. In the four-year development pipeline, including schemes under construction and those yet to commence, 37% of space is already pre-let. Looking at 2020 alone, 41% of the space that is expected to be added to the market has already secured tenants.

London's existing office availability has also fallen in the last six months, with the vacancy rate hovering at just over 5%. The future pipeline also shows signs of softening, falling by 10% year on year to 26.5 million sq ft. This implies a declining appetite for speculation in the construction market as the requirement for pre-letting demand has accelerated.

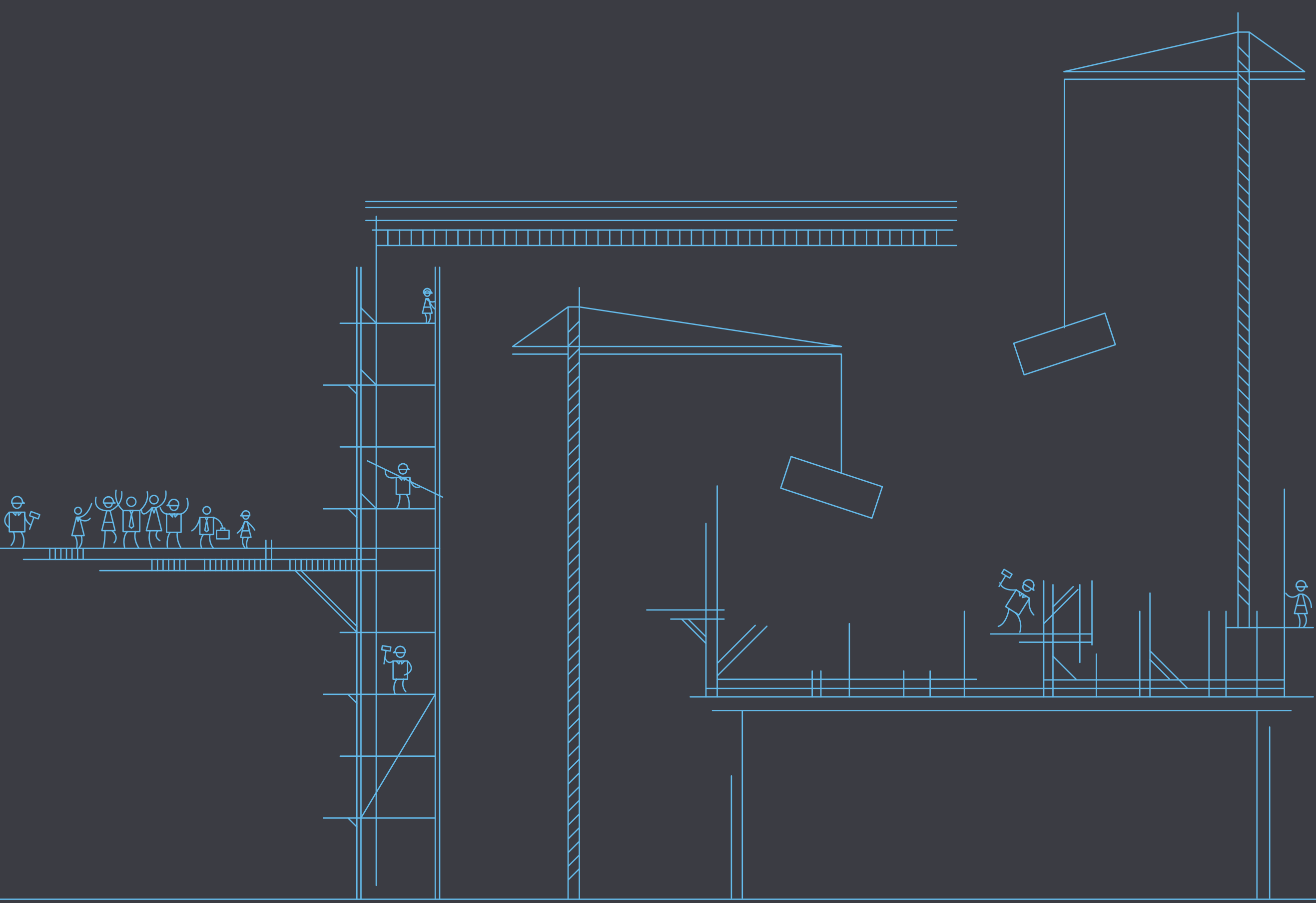
The importance of good-quality office buildings in attracting talent in the competitive labour market, coupled with further expansion by tech and FinTech, will continue to drive demand for office space. However current economic headwinds, and the impact of the rise of both co-working and environmental challenges, are all putting increasing pressure on traditional landlords and developers.

**Central London: Office pipeline forecast**




Source: Deloitte Real Estate

# Construction cost and workload sentiment survey



# Construction cost and workload sentiment survey

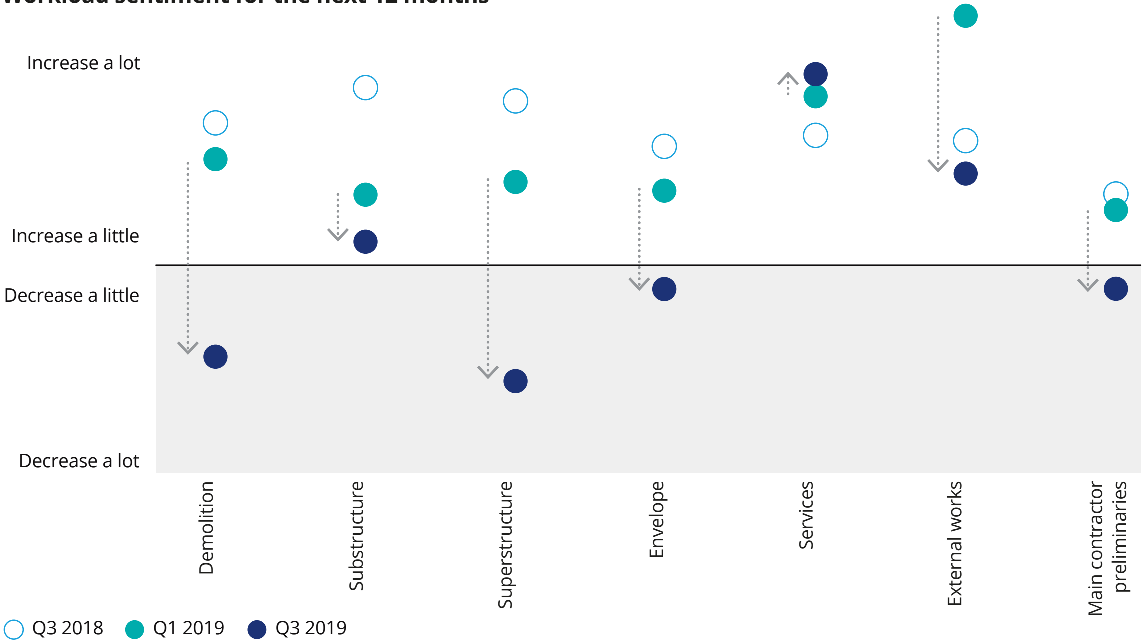
To complement the London Office Crane survey, Deloitte's cost consultancy team carry out a bi-annual construction market survey, capturing market sentiment on workload, price and industry issues. Our latest data marks the seventh survey in which main, trade and sub-contractors have responded with their thoughts on the market.

**A clear expectation of decreases in workload over the next 12 months**

Given the decrease in both construction volumes and new starts in the Crane Survey, it is perhaps not surprising that the construction sentiment survey shows a decline in workload sentiment for London projects in the next 12 months. The average response from most trade groups suggest that workload will "decrease a little" (a reduction of up to 10%).

The direction of the arrows on the workload graph shows the change in sentiment over the past sixth months. Almost all the arrows point downwards. The arrow lengths indicate that the change in sentiment is quite marked. Superstructure trade sentiment about future workload for example has gone from +4% to -4%. The only exceptions to the general downward trend are the Services trades. These results perhaps reflect trades completing current schemes rather than the more typical concern among other trades around the number of new schemes that are due to start.

**Workload sentiment for the next 12 months**



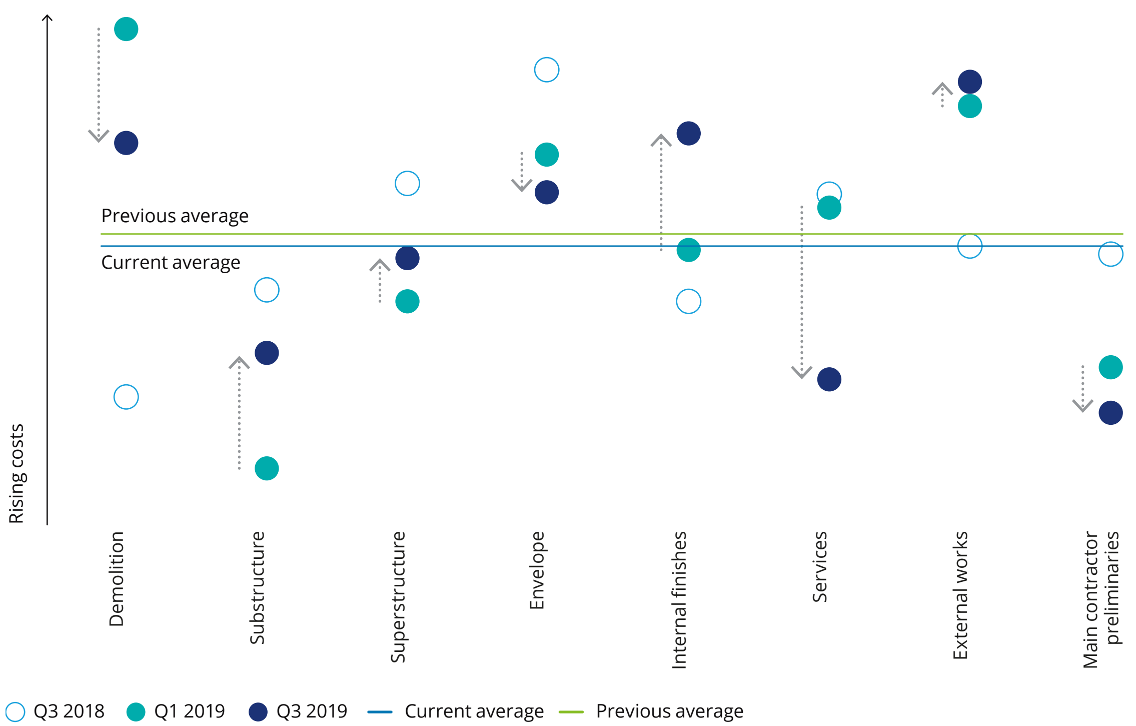

Source: Deloitte Real Estate

## Price sentiment inconsistent with workload expectations

With falling expectations around workload for the next 12 months it might reasonably be expected that sentiment around price would mirror this change. Sadly for developers that is not what our survey has found. The anticipated average price change for the next 12 months has dropped only slightly, from 3.8% in Q1 this year to 3.6% in Q3.

Our surveys tracks both cost and price changes and the latest results suggest that contractors are having to respond to tougher market conditions, and that for all but one trade group cost increases outstrip price increases, so that margins are being put under pressure. Survey respondents confirmed noticeable changes in overheads and profit margins in the past six months.

**Price change sentiment for the next 12 months**




Source: Deloitte Real Estate

As ever, the results are not entirely consistent across the trade groups. There have been some shifts from the sentiment expressed in Q1 this year. Previously demolition prices were expected to rise steeply, but the current survey results show prices still above average but rising less fast. In Q1, the substructure and superstructure trades suggested price growth would slow, but the Q3 figures suggest price growth is increasing and nearer to the overall average. Internal trades, such as partitioning, joinery and decorating, are suggesting increases on or above the average, which has been the case for a number of surveys: price and labour pressures are greater for these trades. Services trades both six and 12 months ago were suggesting price increases at or above the average, but the latest results indicate that services trades (with perhaps the exception of lift manufacturers) are now suggesting a slowdown in price increases.

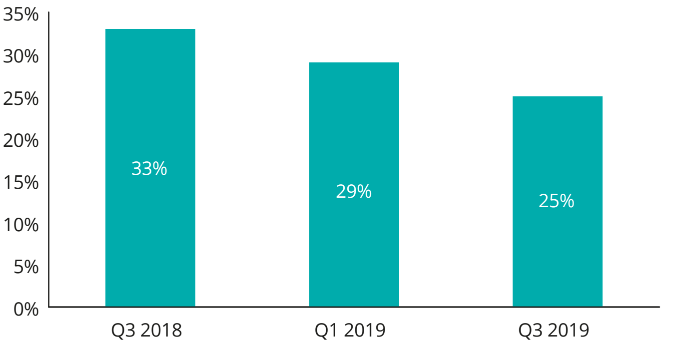
The key drivers of price increases remain the cost of labour and materials. The latest IHS Markit report noted that costs for almost all key materials were increasing.

Our survey for the past two years has been seeking to understand the impact of non-UK labour. With the UK industry failing to attract young construction workers at a pace to match retirement among older workers, contractors operating in the London market in particular have come to rely on a significant numbers of non-UK workers to supplement their UK workforce. The impact of Brexit as well as the attractiveness of other buoyant European centres may mean that labour once again becomes the dominant driver of construction prices.

Our survey found that contractors operating in London had on average 25% of non-UK labour in their workforce, down from 29% six months ago and 33% a year ago. This reduction may reflect the drop in workload but may also indicate that less labour is coming to the UK. A shortage of labour will inevitably drive up labour rates and hence overall labour costs.

Whilst the survey data overall suggests an average increase of over 3% in prices in the next 12 months, Deloitte believes as previously that price increases may turn out to be more subdued, due to the impact of reduced leasing and investment activity (reflecting Brexit and political uncertainties) as well as the smaller number of office starts due in the coming year.

**Non UK workforce**




Source: Deloitte Real Estate

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### Higher specifications for offices create further cost pressures

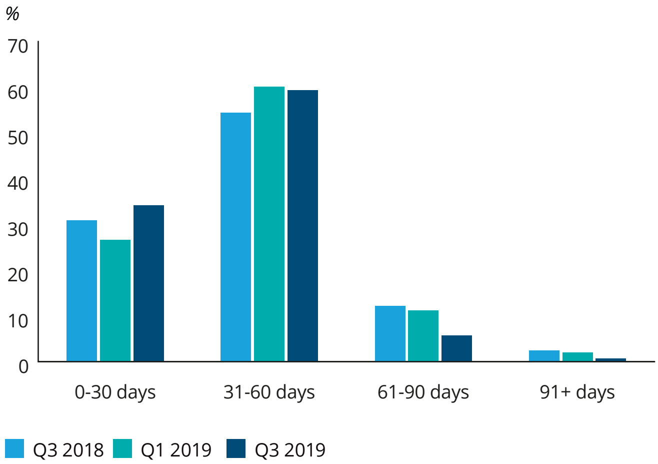
The cost of constructing a London office is a function of the price changes in the market described above. In recent years the strength of the property development market, as reported in previous Crane Surveys, has meant that tender prices for construction have risen consistently.

However developers are now facing further cost pressures from a need to respond to likely regulations around fire safety and also the occupier-driven desire for carbon neutral buildings. Both have the potential to drive specifications and hence costs higher.

### Payment periods decreasing

One piece of good news this time is around payment periods. Our survey suggests that fewer subcontractors are having to wait over 90 or 60 days for payment, and more are receiving payment within 30 days. This may be a result of Government pressure to make more information available about what Main Contractors' payment periods are.

**Payment terms**




Source: Deloitte Real Estate

In recent years the strength of the property development market, as reported in previous Crane Surveys, has meant that tender prices for construction have risen consistently.

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