WHITE PAPER

Curate to Accumulate

Back in 1983, when Property Vision was founded, 25-year leases were still very much the norm in the UK commercial sector. By the first half of last year, according to MSCI's research[1], the average new lease had shrunk to just 6.3 years—and had dropped by 5 months since 2018. Why are we seeing this tightening, and what are the implications for investors?

A flight from commitment

The first and most obvious culprit is economic uncertainty. Companies have focused on maximising their financial elbow-room ever since the Crisis of 2007–08. Agility is all, with long-term commitments being pared back wherever possible.

This has been exacerbated by the 'dither and delay' of Brexit; and we still don't know how that story will end, despite the Withdrawal Agreement Bill having finally passed through Parliament. But just as important is the tidal wave of disruption sweeping through business and society at large.

The last decade has seen significant and accelerating changes in:

How people shop
With the partial exception of groceries, e-commerce has had a profound impact across all retail categories. Feet and wallets have deserted the high street for the laptop and smartphone. 16 stores are closing every day as companies restructure their operations[2]...or cease trading altogether.

How people work
Technology may not have cut the strings entirely, but it's certainly loosened the bonds that tie people to the office. Combined with the rise in self-employment, freelancing and 'slashies' (people who have multiple part-time jobs), today's workforce is increasingly mobile and home or cafe-based. ▶

FEBRUARY 2020

PROPERTY *vision*

How people live
Since the mid-1980s, the number of households living in private rented accommodation has doubled to nearly 20%. Even more dramatically, the percentage of 25–34 year-olds who own a home has halved to just over a quarter. Plus, of course, there has been an explosion in the size of the student population. For many members of this generation, renting may not simply be a rite of passage; it's likely to be a permanent way of life.

In combination, these factors have created occupier demand that's more fluid and volatile than ever before.

The emergence of 'space as a service'

As people's lifestyles become less fixed, and business shifts to more agile models, the commercial property market is necessarily evolving. Out go long-term fixed leases. In comes a much more nimble and proactive approach that has been called 'space as a service'.

'Space as a service' puts curation at the very top of the agenda. Curation has two key dimensions. First, it maximises demand for individual properties by ensuring they're ahead of the curve in terms of use, configuration, technological fit-out and environmental performance. Second, it involves the dynamic management of property portfolios; with an appropriate weighting being allocated to sectors where short-leased property can help increase income returns. Both aspects are critical to success.

The hottest commercial sectors for investment right now are those where curation matters most: spaces which have to be fit for purpose and desirable on an annual, monthly—or even nightly basis. These include the Private Rented Sector, logistics, leisure and (in particular) hotels and student accommodation.

'Space as a service' is about much more than WeWork, although Adam Neumann & co have certainly been running at the leading (or bleeding) edge of the trend. It reflects a fundamental, over-arching re-set in the relationship between landlords and tenants characterised by more flexible legal relationships, the emergence of 'all inclusive' rents, less rigid control of the physical space and more fluidity in the balance of uses.

Implications for investors

Commercial property is increasingly a front-foot game. Investors need to be closely engaged and forward-looking in how they manage and maintain their assets.

Whilst the long-term view remains important, passivity is high risk. Any building can fade quickly into obsolescence and paying a premium for long-leased properties only makes economic sense if those leases can be replicated in the future. Indeed, in response to occupier demand for flexibility, contrarian investors are currently focused on acquiring shorter-leased properties.

They believe this is where better returns can be found. It's a smart strategy, but it requires effective curation. Eyes and hands must be constantly on, which can place a heavy burden on time and resources. Many investors would benefit from an outsourced Family Office function, appointing partners with the experience, know-how and contacts to ensure their portfolio of commercial assets remains on-trend and in high demand.

In today's environment, curation is the key to accumulating the highest possible returns. Finding specialist help may be one of the smartest decisions any investor can make. ■

[1] MSCI, "UK Lease Events Review", November 2019
[2] PwC and the Local Data Company, September 2019