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Crystal Ball Gazing

By Harvey M. Soning, FRICS

September 22, 2023



Harvey M. Soning, FRICS, Chairman – [James Andrew International Group of Companies](#)

Having recently been asked what the future is for commercial property in these challenging times, there is no simple answer to that because of the many factors that feed into this complex market.

The good news is, we have seen interest rates at this level before and the commercial property sector thrived then and it will again. What has changed is, we have become addicted to cheap money and the supply has dried up. What that means depends very much on whether you are a buyer, seller, or holder of property.

In simple terms, if interest rates rise the opportunity to earn greater interest elsewhere means property yields should also increase. If you are a buyer, the price you pay should be lower, and if you are a seller, you need to manage your expectations over the price you will receive. There are always exceptions but generally this will be the case.

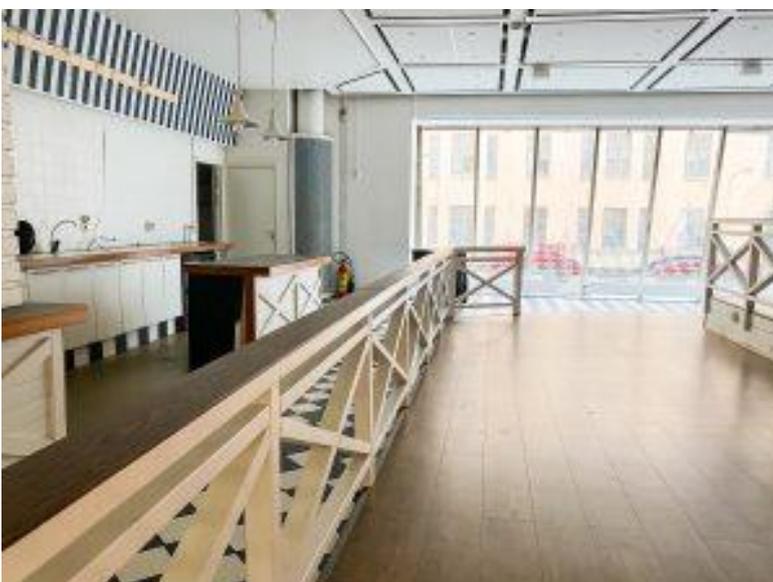


For the holder of property, if you have debt, it's about to become more expensive if it hasn't already. Capital Markets are factoring in another 0.5% before year end if, as we expect, inflation stubbornly fails to fall. On the face of it with banks having limited LTVs to 65%, they should not be under pressure to redeem loans.

However, rarely does a commercial mortgage not have a standard interest cover provision and interest rate rises could challenge this cover. In addition, there will be LTV provisions. Many banks will be carefully checking these, particularly if values fall swiftly. In short you may find the bank is seeking some further capital to close the gap.

In addition, if these economic pressures were not bad enough, there are the Statutory Compliance problems which face property investors from 2028. We are referring to the Minimum Energy Efficiency Standards (MEES).

These regulations are going to force owners to inject substantial capital into buildings to reduce carbon emissions. The government may well move the dates for compliance but our experience in the market today is that tenants are driving the standards required.



Compliance in some properties will be easier than others, but much like for electric vehicles, the UK's infrastructure is simply not ready to move everything to electricity. It is not clear how without electrification these MEES can be met. The key is to start planning early so you can budget for these costs. We were speaking to one lender recently who was making this another precondition of lending.

These are very general observations; all property types face different problems.

The problems with older office buildings usually involve the central cooling and heating systems, although cladding, windows and the roof also matter. In shops let as a shell, surely this is a tenant matter. We are not convinced. The legislation says you cannot collect rent if your property has an EPC of an F or above. If the EPC was renewed with a shop tenant in occupation, your EPC will reflect their fit out. We don't know the answer, but we fear the worst. Industrial property with large opening doors and super high eave heights are if heated unlikely to be very energy efficient.

Where to invest? High Street property must be at the bottom of its value range, with potential in the right High Street, especially as planners need to rethink their policies in the next few years. Definitely worth looking at if the tenant is good and the term lengthy. Logistics has, in our opinion, peaked and without higher yields looks expensive.



Offices remain a sound investment at the right price but in the right location, close to major transport hubs. If they need work doing, don't budget for the minimum, focus on what a tenant wants. Spend the right amount to ensure your property is one of the very best in the location. Do remember costs are rising and allow a contingency.

We, at James Andrew International, still believe in the opportunities for commercial real estate in the UK. Remember this is a small island. We cannot make any more land. Planning is more difficult than ever and we're still unique in the world, having FR&I leases.

Invest wisely and there will always be a good return in commercial real estate which seems to have beaten every index since the last war. For information on available commercial investment opportunities, do not hesitate to make contact.

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Overview:

- 63 years in the real estate industry*
- Ambassador and Founding Member of the Royal Air Force Museum Fundraising Board*
- Chair of the International Friends of the Natural History Museum London*
- Founding Member of the Natural History Museum Foundation*
- Trustee of JCoSS secondary school, Barnet, London*
- Court Member and Managing Trustee of The Worshipful Company of Chartered Surveyors*