

Urbanisation and BTR in a post-COVID-19 world



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COVID-19 and the disruption it has brought to global economies has made the process of urbanisation and the role of cities ripe for conjecture. Much of the commentary has speculated a decline in urban living because of the pandemic. But, we think the attributes of cities that support economic growth and foster a sense of community will abide after the immediate pressure of COVID-19 has receded.

Urbanisation and the build-up of cities have long been engines of economic growth since the industrial revolution. Urbanisation accelerated further in the 2000s and 84% of the UK population now live in urban areas. Humans are social creatures and there are powerful drivers behind the urge to congregate in cities.

Urban areas have grown to represent an outsized proportion of economic activity in the UK. They cover 9% of the UK land mass but account for 60% of jobs. This is particularly the case in city centres, which account for 0.08% of land but 14% of jobs.¹ Creativity and innovation thrive in cities, because when people live closely together, knowledge and ideas are more easily exchanged. Densely populated cities have allowed businesses and labour markets to flourish. This concentration has also facilitated more and greater diversity in leisure and cultural amenities and, in turn, driven an increasing proportion of the populace to live in cities.

COVID-19, which spreads more easily in areas of high density, has highlighted vulnerability in urban living. The spread of the virus has been heavily skewed to cities; 90% of cases have been in urban areas.² This is prompting a rethink of urban environments and how we live and work.

The immediate actions, to implement national lockdowns and social distancing measures to control the spread of the virus until a vaccine is distributed, will have implications for urban environments over the short-term.

The draw of cities is reduced while the pandemic persists. The risk of contracting the virus is heightened while the relatively seamless transition to home working in some occupations has reduced the need for many to commute into cities accentuating the positives of living in less densely populated locations. The lockdowns and social distancing guidelines in place have also limited many of the social and cultural amenities that drive many households' decisions to live in cities.

There is a risk that this may lead to migration out of large cities. In the past, we have seen such movement in cities following health or social crises and the population decline witnessed in London in the 1970s and 1980s demonstrates that urbanisation is not always one-way.

1. Centre for Cities/ONS
2. UN, Covid-19 in an Urban World

However, we believe that the COVID-19 crisis does not represent the beginning of a reversal in the urbanisation trend. Cities have always shown the capacity to endure, learn, adapt and reinvent. It is credible to expect the same to occur in the aftermath of this pandemic.

Already during the pandemic, we have seen this adaptive nature of cities. In only a few months we have witnessed hybrid working conditions where employees spend some time in the office to collaborate; the repurposing of public spaces and streets as pseudo piazzas to support restaurants, bars and pubs; increased pedestrianisation and more cycling infrastructure to reduce dependency on public transport; and the stronger focus on public parks and outside spaces.

We assume that a vaccine will be in place with distribution commencing in 2021³. Under that assumption, we believe that the attraction to cities will remain. Survey data through the pandemic is supportive of this view. That said, there are preferences being expressed in the surveys which, while supportive of city living on the whole, highlights risks; some aspects of cities have become less attractive to a minority. This may represent some shift in demand.

After the pandemic, there is a relatively small increase in the proportion of people who want to work from home all the time, increasing from 13% before the pandemic to 18% after.⁴ While people do currently state that they want to work from home more after the pandemic, they only want to do so some of the time. The survey also highlights that even if it became possible to work from home full-time, 12% would consider changing where they live.

A separate survey highlights that only 8% of those living in London say they are unlikely to still be living in the city in 12 months' time.⁵ On average, 6% of Londoners leave the city each year⁶ so this does not seem to suggest a substantial exodus from the city.

A survey on consumer spending after the pandemic shows that less than 20% of those surveyed expect to spend less on meals, going to gigs/events, cinemas and other cultural events. These are key pulls of city centre living, in comparison to suburban and rural locations. If that remains the case, it would seem likely that cities remain attractive to a large proportion of households, although we acknowledge the risk around a short term drop in spending. The breadth and variety of choice city centres offer isn't easily replicable in suburban or rural locations.

While surveys provide a guide to public preferences, it is important to note that these show preferences at particular point in time, during a pandemic where the awareness of health risks are heightened. Some of these preferences are likely to continue to evolve as we progress through the pandemic.

This is not to say that the pandemic will have no lasting impact on city living. As we return to something closer to pre-COVID-19 norms, cities will likely blend the positive changes to city living emerging from the pandemic with what worked and was appealing from before the pandemic. Rather than being a radical change, the pandemic's impact is more likely to be an accelerant for existing trends.

These trends include a further skewing of the demography of urban areas to younger age groups; preferences for locations with good local leisure and cultural amenities; more diversity in the way we move around urban areas; a preference for high quality office space which allow for better collaboration, health, and flexibility; and better designed homes with good digital connectivity and located in areas with attractive local amenities.

As investors, we need to look through the short-term disruption and take a longer-term view of the future of urban environments. What matters is how urban environments can transform and evolve to better minimise some of the vulnerabilities revealed by the pandemic and accommodate some of the accelerated behaviours and population trends.

What impact will this have on the BTR sector?

The impact of COVID-19 on macro-trends and consumer behaviour will have implications for many areas of real estate over the long-term with differing intensities. In the BTR sector, rather than new thematic trends emerging, we see the pandemic concentrating existing trends around broader themes of occupier demand and housing supply. We expect therefore that the demand and supply fundamentals of the sector is likely to remain supportive but with some relatively nuanced issues.

The most direct risk from the pandemic for BTR is the potential for it to reduce demand through notable shrinkage in city centre population; as households reassess living circumstances following their pandemic experiences. During the initial outbreak of the virus, we saw students and young workers choosing to leave cities and return home for example. The increased likelihood of more working from home, albeit not to the extent many currently suggest, may also contribute to shifting preferences from households as to where they live.

3. LGIM
4. YouGov, September 2 - 6 survey
5. Savanta/Centre for London
6. ONS

Data from estate agency enquiries highlight this risk. In July, across the 10 largest UK cities, there was a 126% increase in enquiries for homes in rural locations and a 68% increase for homes in towns compared with last year.⁷ Were the increased interest in rural and suburban living to materialise this may likely have a notable impact on cities. However, we would expect this to be driven by older age groups, who are typically more likely and financially able to be attracted to suburban and rural living, rather than the younger demographic found in BTR.

City centre demographics have increasingly been skewed to younger people. The number of 20 - 29 year olds in large UK city centres (excluding London) tripled in the first decade of the 21st century.⁸ Suburban locations in contrast are skewed towards older people and families.

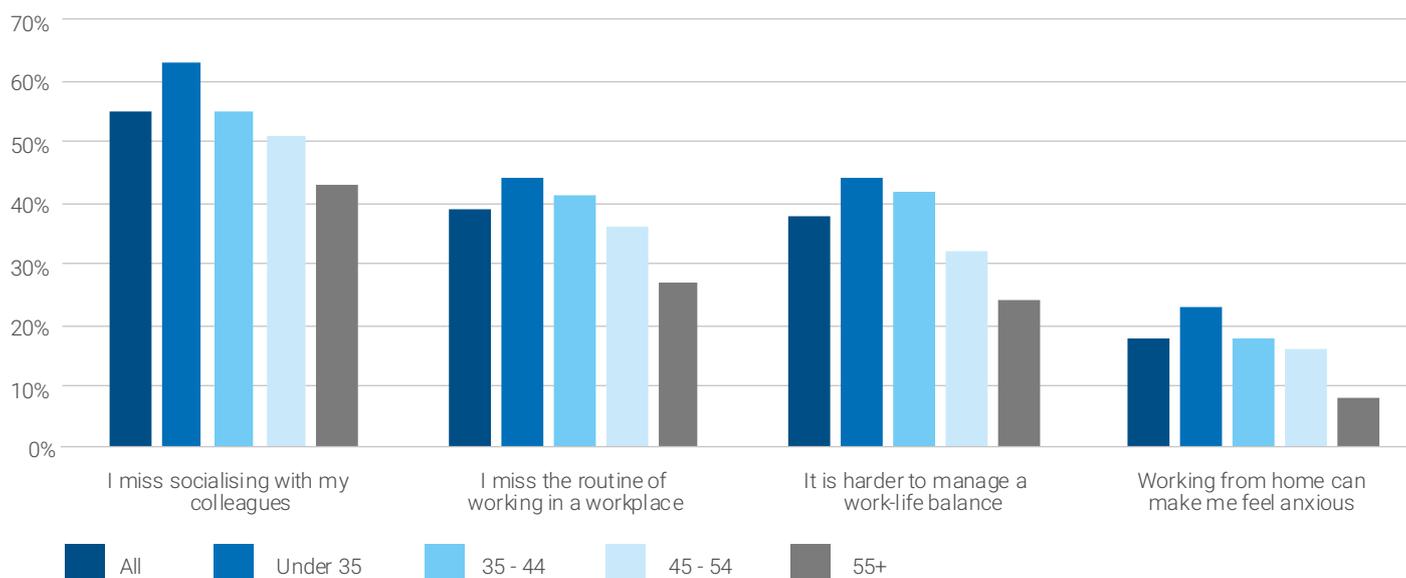
Survey data during the pandemic suggests this trend is likely to hold. On preferences for living in big cities, 45% of the 18 – 34

age group would choose to live in big cities, compared with 32% who wouldn't. However, 16% of the 35 – 54 age group surveyed would choose to live in big cities, compared with 61% who would not.⁹

Attitudes to working from home also provide some support for a demographic shift. We see potential for future working practice where older workers are more willing to accept longer commutes into the city as they spend less time in the office. Younger workers, spending relatively more time in the office, would likely continue to want to live close to their place of work.

Younger age groups are more likely to miss different aspects of working in the office, compared to other age groups. We believe the transition to working from home has been relatively easy for older workers, as they already have the expertise and relationships which can be leveraged to make it effective. This is not necessarily the case for younger employees.

Experiences of WFH (by Age Group)¹⁰



Source: Skillcast/YouGov

On the supply side, we see potential for the impact of the pandemic to facilitate increased level of residential supply in city centres. The Government has made housebuilding one key area of its post-pandemic recovery plans. Updated planning policy proposals, considered by many to be radical, place emphasis on reviving city and town centres by making it easier and quicker to repurpose commercial buildings to residential.¹¹

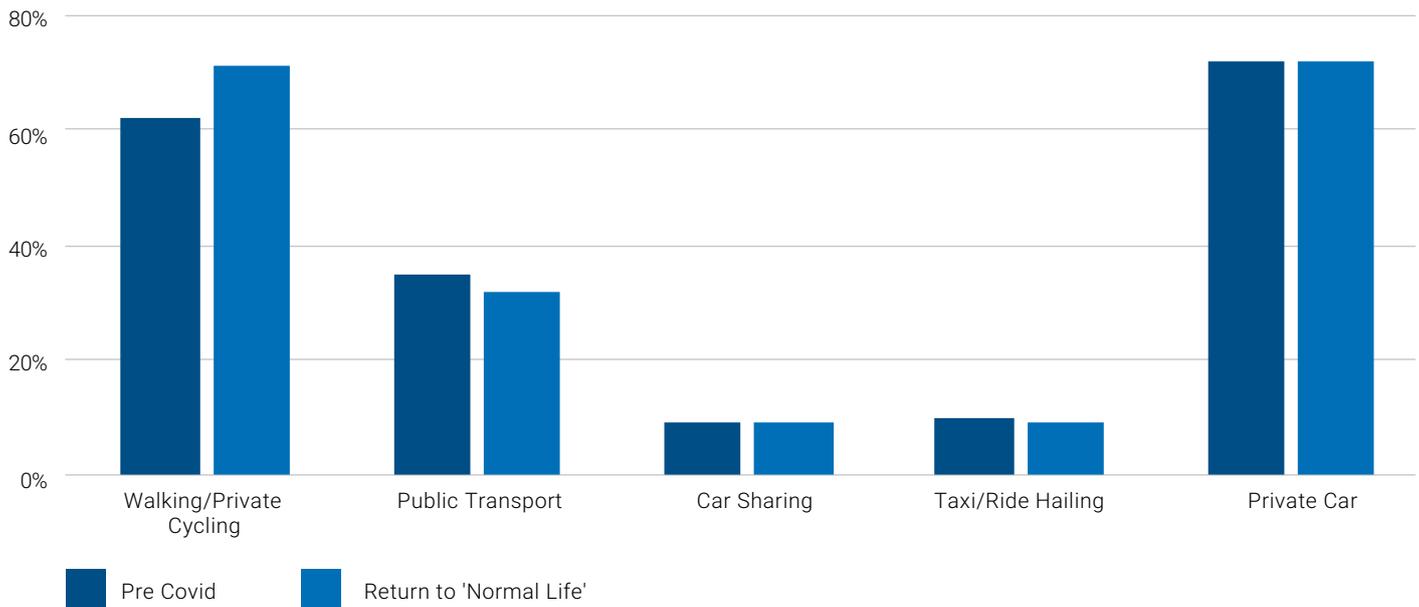
Increased residential choices in central locations will place further importance on selecting assets in the right location with attractive local amenities that improve the liveability of the area and its surrounds. Locations which have local attractions in their own right rather than, for instance, a conduit to more attractive location will likely see better performance in future.

7. Rightmove
 8. ONS/Centre for Cities
 9. Ipsos Mori
 10. Skillcast/YouGov
 11. MHCLG, Planning for the Future White Paper Aug 2020

Consumer preferences emerging through the pandemic also have additional implications for asset selection. There has been increased preference towards cycling and walking as a means of getting around through the pandemic. This shift in preference and the potential for it to be a lasting change is also boosted by supportive Government policy aiming to improve

cycle infrastructure nationally. Households in cities have typically prioritised public transport and the connectivity it brings. We believe this will still hold in future, but further importance may be placed in locations in shorter proximity to workplaces and leisure amenities.

How often did/do you expect to use the following modes of transportation (Often)¹²



Source: McKinsey

Changes in the way households live, driven by the pandemic, are likely to also necessitate additional consideration in the assets developed for BTR. These design choices can act as product differentiator.

As homes become more multifunctional spaces, rather than the typical unit mix and uniform sizes in many schemes, future schemes may necessitate differing unit sizes to provide optionality for those who may want dedicated working spaces in their homes. Increased working from home may also necessitate schemes having larger allocation for co-working spaces.

The move to working from home has also reinforced the need for high speed broadband connectivity in homes. Survey data highlights that 57% of millennials and 62% of Gen Z believe having fast and reliable internet connection has become more important to them than before the pandemic.¹³

Having some private outside green space has also become important for many households and there may be more

demand in future homes. There are limitations to incorporating this in dense urban developments and there has been acceptance of this in the past. This may continue to be acceptable but has potential to drive additional demand to assets in locations which already benefit from nearby public green spaces. Consideration can also be made to incorporate more green spaces or roof gardens in the masterplan of BTR schemes.

While there remains uncertainty, our view is that potential changes emerging from the pandemic do not impose a radical departure from existing thinking around BTR. The foundation for robust occupier demand in the BTR sector is to develop assets in attractive locations which have not seen adequate levels of supply. While occupier requirements may evolve, whether from an increase need for working from home amenities or access to green space - and strategies will need to adjust to meet this -, we believe that the core demand and supply fundamentals will continue to be supportive.

12. McKinsey
13. Ipsos Mori

Contact us

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