

Covid Contemplations



Never ones to be distracted by a crisis, Bull and Bear offer their own distinct advice for dealing with Covid-19

May 2020

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Bull and Bear shared a chance meeting (at always two metres apart, of course) in their local park. This publication records their discussion.

Bull: What a beautiful spring day for a constitutional.

Bear: Believe me, you won't be so jolly in a couple of months' time when reality has properly kicked in. We are all doomed, you know. Dooooomed!

Bull: I see the lock-down hasn't changed your approach to life has it Bear?

Bear: Absolutely not. We are heading for a deep recession, high unemployment and financial hardship everywhere. And, whilst I know the Bank of England's base case indicates a 'V' shape recovery, in my judgement, it's much more likely to be a 'U' or a 'Nike'.



Bull: But have you not seen just how much the Government has been chucking out in financial life-lines? Confetti doesn't come close. This is bound to hugely help.

Bear: Of course I have. I've never watched so much news in all my life. What with no sport on, there's nothing else to watch! QE has gone mad... again. How are we ever going to repay it all? Believe me, the GFC will look like a tiny blip compared with what is on the way. Yup. Doomed is exactly the right word if you ask me.

Bull: You are such a drama queen. The UK has the sixth largest economy in the world and, whilst it will obviously be challenging, I have every confidence that the economy will pick itself up over the coming months and start its comeback.

Bear: What makes you so sure?

Bull: Just trust me. I work in the City. And on that score, don't forget that our banks are significantly stronger now than they were and interest rates are dirt cheap. On top of that, my alumni friends at 'Ox'-ford (get it?) are pretty confident that they have come up with a vaccine.

Bear: That's ridiculously wishful thinking. Let's face it, the economy was at best treading water before the pandemic and if any cracks start to show in the Government's work-out plan, it will put interest rates and sterling under massive pressure. And the consequences of a second wave of the virus don't bear thinking about.

Bull: I can't disagree with that.

Bear: Plus, as if to add a huge dollop of salt into an already massive gaping wound, we have the prospects of a chaotic Brexit. Mark my words, all of this will bring rising crime, social unrest and misery upon misery.

Bull: Which makes it such a great time to be in the market whilst everyone is contemplating their navels. As in every downturn, there will be a bounce off the bottom... but you have to be prepared.

Bear: You just can't help yourself, can you? What makes you say that?

Bull: Firstly, property is now enjoying a huge yield gap over ten-year Government Securities which are currently priced at about 0.25% pa. Provided you are comfortable that your rental income is safe, the property sector represents really good (relative) value.

Bear: But this is exactly where your argument breaks down. Collecting rents this quarter has been a complete nightmare and, if the Government continues to give tenants protection from eviction, June's quarterly numbers will be even worse.



Bull: I doubt it. The last six weeks or so have been as tough as I can recall on the rent collection front.

Bear: Let's face it, businesses are falling over every day and property rental income is no longer the safe-haven it used to be. Corporates' long-term strategies have been forgotten and it is now all about cost savings. 'Right-sizing' has already re-entered the office occupier's vocabulary.

Bull: Right what?

Bear: Right-sizing. As sure as night follows day, there is bound to be a tsunami of vacant space coming onto the market.

Bull: So are you saying that rental values will take a big hit as a consequence?

Bear: Spot on and add to this generally weaker tenants' creditworthiness, and every signal indicates a severe negative impact on capital valuations. What sort of investor would want to catch a falling knife like that?

Bull: I get your drift, but you are missing the point. Firstly, before the lockdown, office vacancy rates were really low and there is hardly any speculative development in the pipeline. This will really help prop things up on the occupational front.

Bear: You'll need more than that to convince me.

Bull: Secondly, the UK is always the first country to mark down its property capital valuations and whilst this will be painful initially, at least buy/sell/hold decisions will then be able to be taken off realistic numbers.

Bear: Anything else?

Bull: Thirdly, yields on prime London office properties are already noticeably higher than in Europe which gives it a competitive advantage. And finally, London is still very much the Number 1 World City. Put all that into the melting pot and 'Bingo'...overseas money will come pouring back in.

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Bear: London! Don't you get it? No-one wants to commute on busy trains and buses any more. How can city centre offices prosper in an environment where the workforce is afraid of travelling?

Bull: Oh come on! Have you never heard of the saying that every cloud has a silver lining? Some of the lessons learned from our current locked-down life-style will be translated into better long-term working space, better attention to well-being, and better working practices. That's good, isn't it?

Bear: I suppose so.

Bull: And it's about time we had a change, anyway. Architects and space planners are just rubbing their (sanitised) hands with the prospects of all the lovely office make-overs that will be coming their way. And if everyone has to keep two metres apart, businesses are going to need even more space to accommodate!

Bear: I agree with the necessity to modify office layouts but home working is now part of the 'new normal'. It's here to stay.

Bull: For some maybe, but to tell you the truth, I am all zoomed out and the quality of my broadband at home is rubbish. I am always having to wander around the house with my laptop just to pick up a signal.

Bear: Who's fault is that?

Bull: No comment but the sooner I can get back into the office the better. And... I really miss the banter.

Bear: I don't miss the commute one little bit though. In fact, I can't believe we have all put up with it for so long. Delays, poor excuses, regular price hikes. It's been so refreshing to start the day with a ten second stroll to the study.

Bull: Too right. But I've bought a bike so that I can avoid the crush on the tube.

Bear: Crickey. When Boris said that we needed to keep alert, perhaps he should have added 'in particular, watch out for wobbly cyclists!'



Bull: Ha Ha. Very funny Bear. Anyway, by the time we are all back in the office no doubt they will have abolished the concept of hot-desking. Good riddance to it, I say. I never liked it.

Bear: That's because you are not prepared to embrace change. I bet you still wear your tie when you are working at home.

Bull: Standards Bear, standards! Well, I hope you have finally found your way to the kitchen and used your time at home to learn how to make a decent sandwich.

Bear: Absolutely I have, because when we do finally get back into the office, there won't be anywhere to buy our lunch. The sandwich retailers will have all gone bust. An already weak retail sector has been completely decimated by Covid-19.

Bull: There's no denying that. Don't take this the wrong way though, but let's face it, there are far too many shops and take-aways anyway. A lot of them have been destined to fail for ages. And, maybe the ones that do survive will come back with a stronger, more compelling 'offer'.

Bear: Can't you see that it's a national catastrophe. The MSCI results last week were terrible.

Bull: Terrible is a tad harsh. I'd rather use the word 'disappointing'.

Bear: Did you miss the fact that the capital value of shopping centres crashed by 23.1% over the twelve months to the end of March 2020? And everyone knows that there is plenty more bad news to come. You can't just sweep it under the carpet.

Bull: You are conveniently focusing on the worst-hit sector.

Bear: For good reason though. The retail sector employs 2.9 million people and retail sales last year were £394 billion. Moreover, luxury shopping in London is a major draw for international tourists. What on earth will the state of the sector be in a year's time if incoming overseas visitors have to self-isolate for fourteen days... just in time to fly home?



Bull: I know. It's a complete car-crash. But at least there may be some safety in the industrials/logistics sector. Believe it or not, capital values there nudged up slightly over the year by 1.3%. Even so, I accept that it's going to be a really rough ride for millions of people, not only in retail, but right across the economy. Which is why I have come up with my own roadmap for UK property investors:

- Be alert. Keep a cool head. Embrace the challenge.
- Examine the road-worthiness of your existing strategies and adjust them accordingly.
- Manage the present intensely but never lose sight of the future. Take great care of what you already own... not only your investments but also your relationships. Once lost... they would be hard to replace.
- If you are in buying-mode, don't be rash. Be patient.
- In the spirit of 'we are all in this together', re-balance the appropriate 'returns' to all your stakeholders... investors, shareholders, tenants, service providers and employees alike. Chasing financial benchmarks alone is no longer enough.
- Impact investment has been a keen topic at seminars lately. It's now time for the action.

Bear: By heck, Bull. Well spoken.

Bull: Thank you, Bear. It's all that self-isolation I have been doing. Notwithstanding all the uncertainty and anxiety, it has been a great time to reflect on what really matters. I need to be getting on, but now that Boris has eased some of the lock-down restrictions, how about a round of golf sometime soon?

Bear: Sounds good. Stay safe.



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