

# surveying trends

Issue 1 – 2007

## Capital allowances update

A major reform of the capital allowances regime was announced in the March 2007 Budget, including the phasing out of Industrial Buildings Allowances (IBAs) and Agricultural Buildings Allowances (ABAs), reductions in the rates of general writing down allowances (WDAs) for plant and machinery (P&M) and a new lower rate of WDAs for fixtures integral to a building.

Although the abolition of IBA/ABAs will be phased over the next 4 years some changes have already taken effect, notably the end of balancing charges or allowances on the sale of a qualifying building.

Phasing out will be achieved by reducing the annual writing down allowance from its current level of 4% by 1% each year over each of the financial years 2008/09 to 2011/12, by which

time the arithmetically astute will have worked out that the rate of WDA will be nil. Any unclaimed residue of allowances will be lost.

Similar proportionate reductions will apply to purchasers of second-hand buildings who may be claiming higher allowances based on the “residue after sale” and the remaining tax life of a building. Again, any unclaimed residue at the end of 2011/12 will be lost.

In the past purchasers may not have paid too much attention to the plant content of a building but the distinction now becomes crucial. It is no longer simply a question of the timing of allowances. Property owners will lose potential allowances on fixtures incorporated into buildings if they do not review future capital expenditure to identify that which can qualify for P&M allowances.

## Property finance review

Kingston Smith LLP recently acquired Blacktower Financial Advisers Ltd, one of the leading firms of Independent Financial Advisers in the South East to enhance the services we already provide to clients in this area. As well as advising on wealth management, Blacktower has experts in the field of raising finance for properties or capital loans. Kingston Smith LLP are now able to offer businesses and investors, in conjunction with Blacktower, a review of their existing commercial facilities, at no cost, to ascertain whether their current terms and conditions are competitive. This looks at factors such as interest rates, financial covenants, loan terms and security held. If this may be of interest please contact Julie Walsh on 020 7566 4000.

# Stagnant income puts pressure on profits

**Profitability maintained but increases in interest rates result in slowdown in the market**

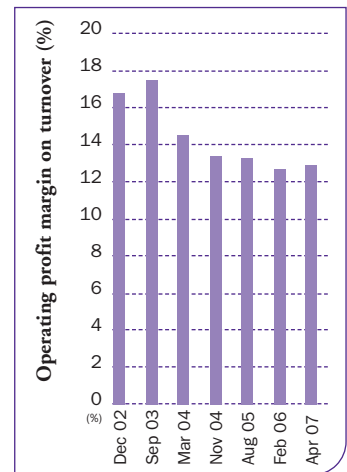
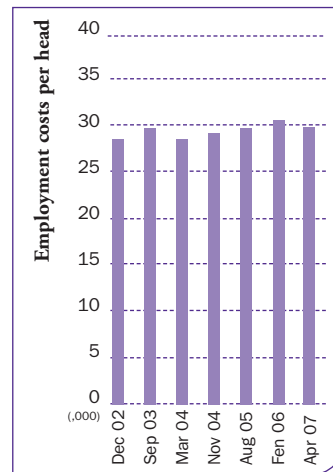
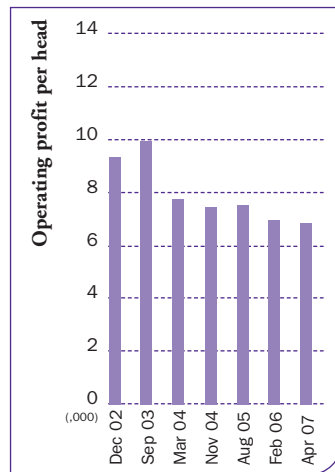
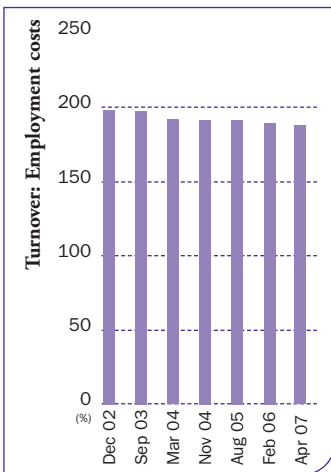
In recent months there has been significant price growth in the residential property market, which has not been matched with sales. The reduction in sales to stock has been influenced by the four interest rate rises in the past 12 months, but also the increase of property stock entering the market place. Surveyors reported a blip in the market with increased levels of new instructions throughout the country, as new property owners were keen to avoid the extra costs and uncertainties associated with the Home Information Packs (HIPs) proposed introduction on 1st June 2007. The profession has placed blame on the government for their role in implementing HIPs and their eagerness to achieve a rapid roll-out by the 1st June 2007 deadline. The Royal Institute of Chartered Surveyors (RICS) now see the delayed introduction of HIPs as vindicating their position that the market was not ready for the introduction of the legislation. RICS have started legal proceedings against the government to highlight how the changes of HIPs requirements and hastiness of the introduction has impacted on the industry's ability to cope with the change.

Turnover remained fairly constant and agencies experienced a small decrease in the ratio of turnover to employment costs from 182%

to 181%, indicating that employment costs have risen slightly higher than income. However, agencies report a small increase in operating profit on turnover, up to 12.8% from 12.6%, indicating tight control over non-staff costs during the period. There may be further pressures to bear though as costs will undoubtedly increase as agencies have experienced costs in understanding and getting ready for the new government legislation regarding HIPs. The expected further rise in bank base rates will also reduce the level of transactions as buyers are priced out of the market, adding more pressure to profit margins.

The commercial property market continues to show an improvement, with reports that demand for commercial property accelerated at the fastest pace in seven years. Both the retail and industrial markets report a stabilising of demand, and these no longer act as a drag on overall demand in the commercial property market.

Average operating profits per head fell slightly from £6,965 to £6,939, with a corresponding decrease in the productivity of agency staff from turnover per head of £55,406 to £54,076. The challenge for agencies will be to increase turnover and productivity in this highly competitive market.



# Decrease in productivity and profit margins

## Staff costs rise faster than income which hits profit margins

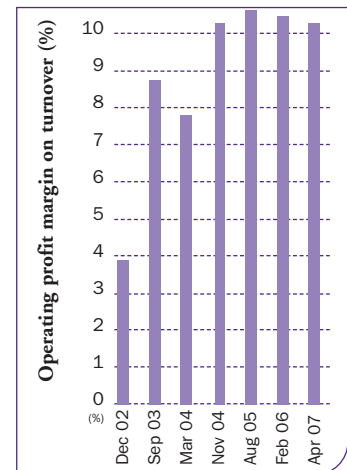
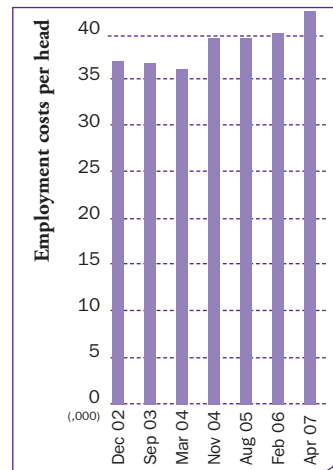
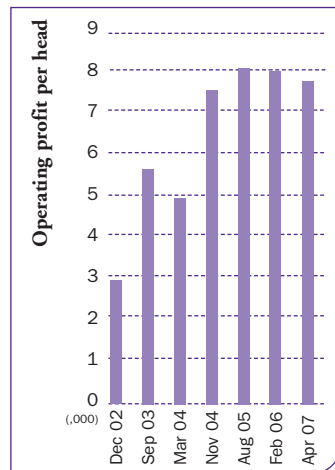
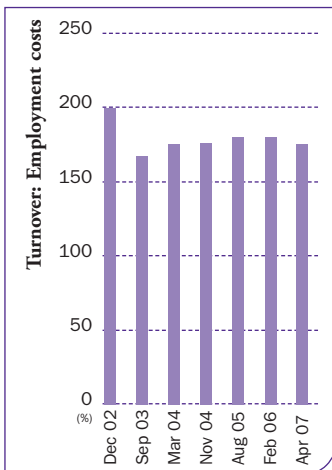
Turnover in the general practice sector has not increased at the same pace as in the recent past, and this together with an overall increase in costs has significantly reduced profitability for general practice surveyors.

The ratio of turnover to employment costs has decreased from 186% to 179%, indicating that staff costs have increased at a far higher rate than income. This now falls below the figures achieved by agencies and quantity surveyors – 181% and 183% respectively. This is a key margin as employment costs are by far the highest cost that surveyors incur within their businesses. A benchmark figure for the ratio of turnover to employment costs would be 200%, but some well run agencies comfortably exceed this target.

Rewarding and retaining staff remains a major issue for general practices within their highly competitive market and it appears that a shortage of suitably qualified staff has led to an increase in average salaries. These now stand at £40,999, compared with £40,155, as previously reported. It is likely that there will be further pressures on employment costs with growth in salaries currently exceeding 5% per annum.

There has been an increase in the number of employees within the sector indicating that surplus capacity was not available to service new growth. This is reinforced by the fall in productivity, measured as income generated per member of staff, from £75,840 to £73,198. Consequently average operating profits per head now stand at £7,777, down from £7,999. The decline in productivity needs to be addressed if profit margins are to be improved.

The trend of a fall in operating margins reported in the last edition of Surveying Trends continues. Operating profit as a percentage of turnover fell to 10.4% from 10.7%. It is worth noting that this ratio does vary considerably between firms, with some practices achieving a 30% margin of operating profit on turnover, and others with negative operating profit margins. Clearly the main challenge for general practices is to improve the productivity of staff and control costs as the outlook in the commercial property market is positive with indications of rental growth and continued investment, although lower yields and higher borrowing costs are expected to tame the appetite of investors. There may also be signs of further consolidation as practices look to rationalise costs.



# Productivity and profitability up

## An increase in turnover and control of costs results in improved profitability

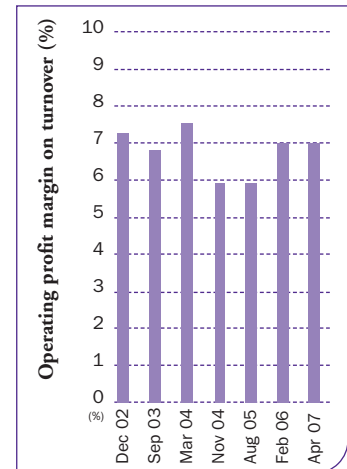
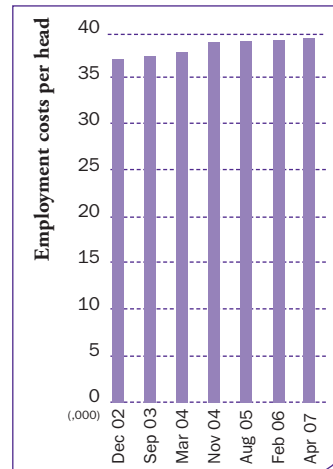
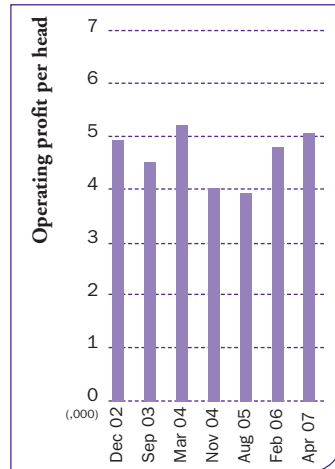
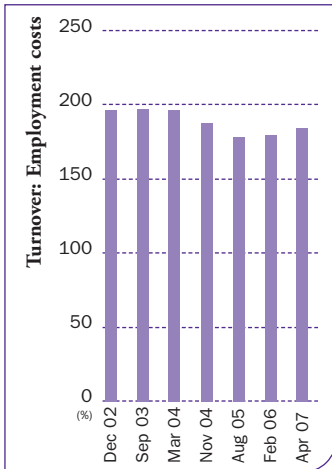
Quantity surveyors have reported significant growth in the period with a small increase in profitability. Part of the increased turnover can be attributed to acquisitions but there is underlying organic growth within the sector. There are also continued signs of increased activity in the commercial market, particularly office and industrial developments as well as private housing. There continues to be significant growth in project work and quantity surveyors report a good forward order book that should help maintain the current level of activity.

There was an impressive increase in turnover as a percentage of employment costs from 179% to 183%. This was particularly impressive as there continue to be reports of difficulties in retaining suitably qualified staff. The numbers of staff employed by quantity surveyors in our sample increased, and their average salaries rose from

£38,551 to £39,121, reinforcing this point. However, recent salary surveys indicate that salary costs are increasing in excess of 5% per annum. This will exert further pressure on profit margins, which means that quantity surveyors will need to increase productivity and tightly control other costs in order to maintain margins. Whether quantity surveyors can achieve this remains to be seen.

Productivity, measured as turnover generated per employee, rose on average from £67,361 to £71,577 per head. This is the highest level we have reported for quantity surveyors. This fed through to increased operating profits per head from £4,848 to £5,053.

Operating profit margin on turnover increased marginally from 7% to 7.1%. These still fall short of margins achieved by agencies and general practice of 12.8% and 10.4%, respectively.



**For further information on Kingston Smith LLP and our services please visit our website on [www.kingstonsmith.co.uk](http://www.kingstonsmith.co.uk) or call Julie Walsh at the City Office on 020 7566 3800 or Jonathan Seymour on 020 8848 5500.**

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