

The Investor View

Clapham
Summer 2014



Douglas
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Good to know.

Introduction

Anyone who owns a property in London is a property investor and it's often useful to take an investor's view of the market before making big decisions. To produce this report we've worked closely with the experts at D&G Asset Management, a company we co-founded in 2005. They invest in London residential property all the time – so are constantly analysing different areas, and assets within those areas, seeking to maximise returns.

As well as publicly available sources, we've used proprietary data that we've been capturing since 1996, to help us make decisions and advise our clients. D&GAM has helped us focus on the data that counts, and we think the results make fascinating reading.

How an investor looks at the market

Residential property investors use two key measures to assess property – the capital value and the net

Property Values

Two bed flats performed well in Q1 but may have peaked in this cycle.

Q1 performance and outlook

Over the course of a full cycle, real annualised capital values normally rise in line with the real long term (10 year) trend. When, at a specific point in the cycle, real annualised growth is below the long term trend, rapid nominal growth is probable. Once the real annualised growth is aligned with the real long term trend, a pause is likely. Therefore, it's possible to forecast which assets might have further to run and those that are likely to stall.

Recent strong nominal growth in Clapham must be viewed in the context of long term and real annualised growth rates since the start of this latest market cycle in 2007 (when property prices last peaked).

In Clapham, only two bedroom flats have now reverted to their long term trend growth rates. All other unit sizes, though they are all rising in a uniform fashion, are still catching up and have not yet reverted to their long term trend.

Implications

Owners of two bedroom flats who are not looking to hold long term might find this the right time to sell.

We expect smaller flats and houses to start to outperform other unit sizes as the year unfolds. As discussed in our Q1 Investor View, we believe the impact of the unfolding credit cycle will be that these smaller (and less expensive) unit sizes will start to outperform larger units. As a result, buy-to-let investors who own two bedroom flats and are unwilling to maintain the property in line with tenant expectations (see Rental Growth & Yield section), might consider this the moment to sell. However, as a note of caution, the current market has started to

Clapham Property Values

	Real Annualised Growth		Nominal Growth
	10 year	This cycle	Q1 2014
1 Bed Flat	2.60%	-0.67%	6.67% ↑
2 Bed Flat	4.10%	3.12%	7.69% ↑
3 Bed House	6.00%	3.69%	4.35% ↑
4 Bed House	4.92%	2.83%	8.00% ↑

Source: D&G proprietary data, ONS

differentiate between good stock (in terms of location, space and finish) and lower-quality stock.

Many people do not have the luxury of picking their timing according to the cycle. These individuals can feel comforted that Clapham is benefiting from infrastructure and other demographic changes that should ensure continued capital growth rates of 4%-6%.

rental yield (the annual rent, less expenses, divided by the property's capital value).

Both of these measures are important, and are influenced by a number of factors including: supply of new properties, infrastructure projects, demographics of the area, the economy (in particular, interest and tax rates) and the wider geopolitical picture. It's the interplay of these factors that determines investment returns and makes property investment decisions so interesting.

The importance of market cycles

Successful investors will always maintain a keen awareness of market cycles and long term trends. It is therefore important to look at the recent growth trends of capital and rental values and in Clapham when managing your property assets.

We are recommending investors look at the year when property values last peaked (2007) and treat this as the start of the most recent cycle.

In Q1, rental values slowed, however indicators suggest a more positive end to the year.

Rental Growth & Yield

Q1 performance and outlook

Over the course of this lettings cycle, rents in Clapham have risen across all unit sizes. For example, between 2008 and the end of 2013, nominal rents rose from 20%+ for four bedroom houses to 30% for two bedroom flats and three bedroom house.

Rental values increased during the period of tight credit (2008-2012) as frustrated buyers were forced to rent. As credit has eased and confidence has returned so tenants have become owner/occupiers, leading to capital values rising and rents stabilising or even falling. This slowing down of rental growth has been evident during Q1 in Clapham (see table below).

Over the same period, employees/tenants experienced salaries stagnating in real terms meaning affordability was stretched. With earnings in the City now picking up and a general improvement in outlook, we believe that rents in Clapham will start to rise. Data from our offices in Prime Central London suggest this is already underway.

Implications

Clapham remains popular with tenants, but landlords must continue to invest in their properties to ensure tenants stay and/or pay more rent. "Accidental landlords" who during 2008-2012 rented properties out rather than sell, and are not keen to invest capital into their properties, might choose to take advantage of a strong sales market and sell.

Landlords must appreciate that those still opting to rent have more property to choose from and will be more demanding than a few years ago.

Note: When renting out a property, investors will look at current rental yield, (see below) however they also need to take a view on how much rents will grow. It's this "rental growth" that maintains real income and yield over time.

Clapham Nominal Rental Growth

	Dec 2008 - Dec 2013	Q1 2014
1 Bed Flat	27.27%	2.86%
2 Bed Flat	32.35%	2.22%
3 Bed House	31.58%	0%
4 Bed House	22.22%	0%

Source: D&G proprietary data

Current Rental Yields March 2014

One Bed Flats	3.9% - 5.0%
Two Bed Flats	3.0% - 4.5%
Three Bed Houses	2.7% - 4.0%
Four Bed Houses	2.7% - 4.0%
10 Yr UK Gilt Yield	2.7%
FTSE All Sh Yield	3.45%
UK Base Rate	0.5%

Never has the difference between London and regional property prices been so great.

Every Spring we co-host the 'Move to the Country Show' with The London Office. The show is held in Battersea and gives our clients and members of the public an opportunity to meet local independent estate agents from across our UK network.

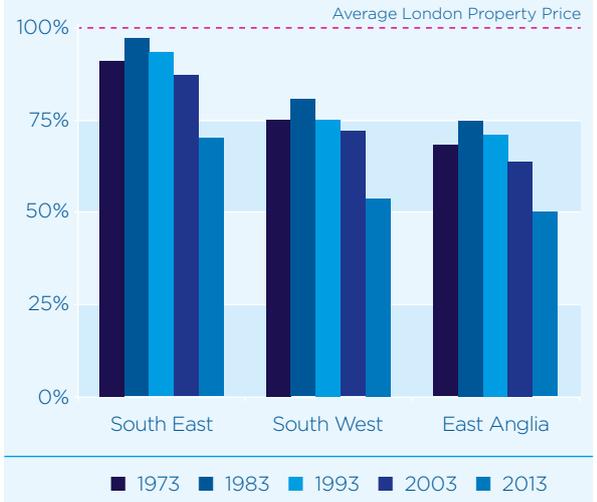
The show is an important date in our calendar as every year a proportion of our vendors sell up and leave London.

For many, the timing of that move involves a number of practical considerations such as schooling and space.

For others, it is an important investment decision where a London property is sold and part of the money deployed into a regional retirement property. The remainder often forms part of a pension pot, so the timing of the move is crucial.

Although we remain positive about London prices over the long term, the current relative gap between London and regional property prices may well provide an opportunity for those looking to move out of London and top up their savings/pension pots.

Regional property prices relative to London property prices



Source: ONS average property prices.

Clapham key facts & figures

Here are the key facts and figures anyone investing in the property market needs at their fingertips.

Nominal Rental Income Growth to Dec 2013

	2013	5 years	10 years
1 Bed Flats	0%	27%	52%
2 Bed Flats	0%	32%	61%
3 Bed Houses	1%	32%	62%
4 Bed Houses	-6%	22%	65%

Nominal Capital Returns to Dec 2013

	2013	5 years	10 years
1 Bed Flats	21%	50%	79%
2 Bed Flats	24%	67%	106%
3 Bed Houses	18%	92%	147%
4 Bed Houses	19%	67%	123%

Other Assets Capital Returns to Dec 2013

	2013	5 years	10 years
Nationwide HPI*	8%	15%	30%
Halifax HPI*	6%	8%	22%
FTSE100	14%	52%	51%
RPI	3%	19%	38%

*House Price Index

**Clapham 2014
Our view**

- Credit easing • Area re-rating to continue
- Capital values: Flats to outperform houses
- Rents to slowly pick up

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