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Residential Property Group Newsletter 2015

Happy New Year to you!

Predictions are only of use if the forecaster has a good track record of forecasting! So, as usual, we kick off reviewing how our predictions performed last year, before giving our forecasts for 2015.

Assessment of our 2014 predictions:

Our predictions in the past have been fairly good, so what about the predictions we made in January 2014 for the UK property market in 2014:

We are more positive on the market than we have been for over 5 years. The market is relatively buoyant and we expect this underlying strength to continue throughout 2014. Correct.
As per previous years, we repeat and reiterate that; residential property investment is a long term investment over a 5+year time horizon. Predictions over 12 months are provided for interest only, rather than any forecast of investment performance.

- **Capital values:** A national house price increase of 7%, or the equivalent of a real house price increase (after inflation of c2%) of 5%. The Help to Buy scheme will continue to support the market. Talk of a bubble is very London/South East centric; in the real world for the rest of the country, it is the first house price rise we have seen since 2007 and prices are still lower than 2007 levels. Correct, 7.2% according to Nationwide Building Society.
- **Regional variations in property prices:** As always, the market is highly fragmented. We stick with our views of last year that the South East, East Midlands and East of England will outperform. However, the north/south divide will not increase as much as in past years. Correct, strongest growth has been in South and East of England.
- **Rental growth:** Will be flat but part of a longer term upward trend. Correct.
- **Transaction levels:** Will continue to increase from 2013 levels. Help to Buy will assist this; phase 2 of help to buy only started at the end of 2013 and is still to impact. However, as house prices rise, albeit marginally, wages will not rise proportionately and housing will become more expensive. Correct, transaction levels were up 20% from 2013.
- **Interest rates:** base rate will remain at 0.5% throughout 2014. The subject of when interest rates should increase will be discussed at length throughout the year. We believe it is too early to raise rates, although there will be an increased possibility of a rate rise happening in 2015. Correct that rates would not move, and it would be discussed continuously in the press.
- **Mortgage availability**: Has improved dramatically since 2012. We expect this improving trend to continue. Availability is good, affordability (at present interest rates) is good, and Help to buy assists those struggling to raise their deposit needed to purchase a property. Correct, although with increased burden of due diligence.
- **House builders:** Had a fantastic 2013 and all indications are that they will have a good 2014. They surprised on the upside in 2013, growth will be less "surprising" in 2014. Share prices may begin to slip towards the end of the year as markets begin to worry about the impact of rate rises, and

the end of the Help to Buy scheme; regardless of how far away these events are. Correct, although prices are generally down at year end there would seem further to fall.

- **New housing starts:** will be higher still than the 2013 numbers. Correct; the figures for the first 3 quarters of 2014 are significantly above 2013 figures.
- **Prime Central London:** After another good year in 2013, one has to be wary of how long this outperformance can continue. There can be no denying London is now the globally most favoured city for residential property investment. Turmoil in the world drives capital to the safe haven of London property. Unease about tax implications on foreign investors and the outcome of the next general election in 2015 will weigh on the market; we expect 7% upside; in line with the rest of the UK market. Wrong, prices increased c16% in 2014, although we did predict prices would rise, we got the magnitude of the rise wrong.
- **A couple of other thoughts for 2014: Brazil win the football world cup Wrong it was Germany , Scotland will not vote for independence Correct, just, Euro problems will continue throughout the year Generally correct with now talk of a Greek exit, North Korea will cause concern to the global powers Correct, not until Sony was hacked but concerns linger, Prince Harry will get engaged Couldn't be more wrong!**

All in all we are very pleased with these predictions.
Importantly we got the direction and magnitude of movement of the wider market correct. That sentiment would be positive, interest rates unchanged and new supply increasing.
What we got wrong; we were again too conservative on the Prime Central London market; but who would have predicted the meteoric rise of the past 5 years? Otherwise sport and royalty we should steer clear of, but pleased with the calls on Scotland referendum and especially North Korea!

Our Predictions for 2015:

We are "cautiously optimistic" about the residential property market in 2015. It is difficult to be too excited for there are too many unknowns lurking on the horizon, and we can't help feeling marginally more subdued going into 2015 than we felt going into 2014.
The market has strong, solid foundations, prices have increased slowly over 2014 and we continue to expect prices to rise over 2015 albeit at a slower rate.
As per previous years, we repeat and reiterate that; residential property investment is a long term investment over a 5+ year time horizon. Predictions over 12 months are provided for interest only, rather than any forecast of investment performance.

- **Capital values:** Direction: upwards, Magnitude: 4.5%.
  A national house price increase of 4.5%, or the equivalent of a real house price increase (after inflation of c1%) of 3.5%. Boring, I know, but there would seem too many headwinds to make the market, as a whole, move further up than this.
- **Regional variations in property prices:** As always, the market is highly fragmented. We stick with our views of last year that the South East, East Midlands and East of England will outperform. Areas with strong economic activity and stronger job prospects will outperform and we are big believers in the East of England and Cambridge being the driver for increased activity.
- **Rental growth:** Will be 2%, marginally above inflation, but part of a longer term upward trend. The demand from Generation Rent will continue to grow.
- **Transaction levels:** Will decrease marginally from 2014 levels. As house prices rise, wages are not rising proportionately as fast and housing therefore becomes more expensive. Combine this with the effects of a general election, a possible mansion tax and increased uncertainty and liquidity quickly evaporates from the market.(transaction levels in 2014 were 28% below the 25yr average prior to the credit crunch)
- **Interest rates:** base rates will remain at 0.5% throughout 2015. There is a small chance of a 0.25% rise in the final quarter of 2015. This is a huge unknown, and will likely be affected by whatever form the next Government takes post-election. There will be constant "chatter" in the press of rate rises throughout the year. Inflation, or deflation, is the factor to watch.

- **Mortgage availability**: Will be flat on 2014 levels. The longer term mortgage market has a far stronger base now; lending is prudent and executed on sensible metrics. Whilst affordability and availability is good, the "hoops to jump through" to attain a mortgage will prevent excessive lending. (MMR limits the number of borrowers and the amount they borrow)
- **House builders:** Share prices will fall c20% from their levels in December 2014. This will be driven by a slower market than 2014 and the problems with Government changes, policy changes and planning changes of different political parties.
- **New housing starts:** will be the same as, or small down on the 2014 numbers. However to put this in perspective, there were c112,000 new homes completed in year to March 2014 in England, this is still well below the 170,000 achieved in 2008 and hugely below the 240,000 needed to meet household growth.
- **Prime Central London:** For the first time in 5 years the market will be subdued and we expect price rises in line with the national average ie. 4.5% over the year. Now a Global city it attracts wealth from around the world, but even the wealthy are concerned about the impact of changes to taxes and especially mansion taxes. Political uncertainty will further subdue the market.
- **A couple of other brave predictions for 2015:** Greece will leave the Euro, North Korea will increasingly worry the world, oil prices will hit a low of $30, the Tories will form a majority government in May, our stock pick for the year is NCC Group; a world leader in cyber security. Our recommended short is BP (oil price and exposure to Russia). John F Kennedy to win the Derby.
- What we do predict is that predictions will not be as good as in 2014; there are just too many external factors that could come into play to affect the market.

Our Recommendations for 2015:

Given our predictions for 2015 above, property aint going to be a particularly exciting asset class for investment, but more importantly is HOW will property compare RELATIVE to the other asset classes of gold, equities, bonds and commodities?

This is a huge unknown; there are a lot of economic forces at play; euro woes, the winding down of QE programs, political elections, a low and volatile oil price, Russian sanctions and rouble devaluation, Cuban liberalisation; I would not like to be forecasting stockmarkets for the year, all we can say is that the historical attractions of "property" remain as strong today as of past years; less volatility, a tangible asset, a real asset with real tenants, an investment that is easily understood, and in an environment of limited supply and increasing demand.
In an increasingly unstable world, we believe the lower risk returns of residential property will prove attractive to many investors.

Where should one buy?

Whilst we predict national house price increases of 4.5% over 2015; there are opportunities within the diverse property market that will allow investors to make superior returns.
Please note we always recommend purchasing on a 5 year + investment horizon.

As many of you know, RPG cover the whole UK residential market, but we focus on the **East Midlands and East of England** where we manage c800 units, and also source a number of properties for our retained clients.

For 2015 we are recommending;
A: Peterborough/Kettering/Northampton

Why?

- We are massive fans of the economic growth happening in the East of England and in particular Cambridge. Whilst the city of Cambridge itself is relatively expensive, we recommend surrounding cities which will benefit from the improving economy and jobs market in the wider area.

- Prices are still below the national average and often at or below the stamp duty threshold of £125,000.
- These areas benefit from an active first time buyer market, where they can actually afford to buy
- The ripple effect of wealth flows out from London to these areas which are all within a 1hour commute of Prime Central London at a fraction of the price
- The blended returns of superior capital growth potential (4.5%+) accompanied by an attractive rental yield of c 6-7% make for an attractive total return of 10% +. (we would expect the total return in Prime Central London to be less).

B: City of Kingston upon Hull

Why?

- Regeneration; in 2003 Hull was voted the country's no 1 "crap" town in the Crap Town Book, but now voted city of culture for 2017! attractive rental yields; 8%
- Prices are still near their 10 year lows and at have low absolute prices; from £40,000 upwards for a two bed terraced house, and prices were flat last year.
- High yields provide a "floor" preventing further downside to prices.
- With these higher yielding properties it is imperative that properties are managed carefully and professionally, many cowboys abound. We are pleased that we have our own property management team based in Hull with a 10 + years track record of property investment expertise.
- The blended return of some capital growth potential (2-4.5%) accompanied by an attractive rental yield of c 7-9% make for an attractive total return of 10% +. (we would expect the total return in Prime Central London to be less).

RPG Property Finding Service:

We continuously review investment opportunities throughout the UK and we are not geographically constrained. Each opportunity is assessed on a project by project basis on its own merits. As always, due diligence of the unit(s) concerned is imperative.

The areas identified above we particularly like, but most importantly they meet the basic rules of a STABLE RECURRING BLENDED RETURN made up of capital appreciation and rental yield.

Capital values: In these areas are considerably lower than London and the South East. Prices are still sub 2007 levels, and have only recently started to move upwards in 2014. There is NO bubble here.

Rental yields: Are typically 6% plus and underpinned by strong underlying tenant demand. These are real yields that net down after running costs to c6%. Yields of half this amount are typically available in London.

It is imperative that you select the right area, the right location, the right development, and the right unit(s) in which to invest. A poor purchasing strategy (or indeed exit strategy) can have drastic effects upon the total return.

It always amazes us that people use stockbrokers to buy shares and use estate agents to sell houses but often do not use property finders to buy investment property. Many investors are not able to do this in depth research, nor are they familiar with the local market. This is why we offer our property finding service.

We have been active in these regions since 2001, we know the local markets, we have the contacts, and we manage properties throughout these regions and we are therefore able to advise and assist our existing as well as new landlords.

It means you are being hand-held in what can be a complex purchase procedure, it means being confident in the decisions you have made to invest, and it means that we do not just source a property then run, but once sourced we will manage the property, and that we hope to forge a long term relationship with all our clients, old and new.

RPG can act as property finder for you the buyer (not an estate agent acting for the seller). We can let and manage the property for you (ensuring a seamless hassle free service), and we aim to considerably increase the chances of you attaining a higher total return for your property investment.

We wish our clients and friends a very prosperous 2015 **The Team at Residential Property Group Limited**