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Residential Property Group Newsletter 2014

Predictions are only interesting if the writer has a good track record of forecasting.
So, as usual, we kick off reviewing how we performed last year, before giving our predictions for 2014.

Assessment of our 2013 predictions:

Our predictions in the past have been fairly good, so what about the predictions we made in January 2013 for the UK property market in 2013:

We cannot help feeling more positive about the residential market. Strangely upbeat, mildly and quietly confident, cautiously optimistic; call it what you will, but there is a glimmer of good news and a belief that the residential property market over 2013 will be a positive experience. Correct!

- **Capital values:** Boringly we stick with the figure we went for last year; that national prices will fall circa 2% over the year, or in real terms (after inflation of 3%), a 5% fall. We expect ongoing inertia with no significant drivers either for house price falls or house price rises at a national level. We expect prices in 2014 to increase moderately. Wrong! Too conservative, the UK market as a whole was up c7% or 3% excluding London and the South East (only slightly above inflation and hardly a bubble!).
- **Regional variations in property prices:** As always, the market is highly fragmented. We expect the South East and East of England to outperform, the North to underperform, the north/south divide will thus grow not shrink. Correct. London market rose c12% whilst the market in East Yorkshire, for example, increased only 1%. The average home in the capital now costs nearly three times the price of a comparable property in the North East.
- **Rental growth:** Will be flat. Rents have risen over the past 24months and will plateau this year. Longer term we do believe rents will continue to rise further. Correct-ish, regional variations meant rents were flat to +4%.
- **Transaction levels:** Will increase marginally from 2012 assisted by the Government funding for lending scheme and the increasing availability of mortgages. However, the average house costs over 5 times the average wage so there will be no dramatic increase. Correct, but levels increased more than marginally to exceed one million, still far below the 1.6million figure for the boom year of 2007.
- **Interest rates:** base rate will remain at 0.5% throughout 2013. Correct.
- **Mortgage availability**: will continue to remain constrained, but will improve from 2012 assisted by the funding for lending scheme. Affordability is not the constraint, but the amount of deposit needed by the average buyer to purchase a property. Correct it improved, these predictions were given before the "help to buy" scheme was announced, which hugely assisted mortgage funding. Gross mortgage lending ended 2013 at its highest level for 5 years.
- **House builders:** Had a good 2012, land bought in the market dip and revision of valuations downwards meant they reported strong profits for the calendar year 2012. We expect this to continue, and they will continue to be able to sell units with the assistance of the Governments "first buy" initiative. Correct, their share prices are now up c5x over the past 5 years.

- **New housing starts:** will be marginally higher than 2012. There is a long term imbalance between the demand for, and the supply of housing in the UK and this will remain the case. Correct, again may be a bit conservative, there were 125,000 housing starts.
- **First time buyers:** the real drivers of the market will increase. There were 216000 first time buyers in 2012; the most since 2007 and up 12% on 2011, expect this to increase further. Correct. The number of loans advanced to first-time buyers rose to 26,800 mortgages in October – 33% higher than the same time last year and the highest number of loans in a monthly period since November 2007.
- **Level of repossessions**: Will remain low, as a result of the low interest rate environment. Correct.
- **Prime central London:** Had another strong year in 2012 driven by the flight of capital to the safe haven of London property. Whilst there is turmoil elsewhere in the world, funds will continue to flow into the London market. The profile of London has been further strengthened on the back of the success of the Olympic games and the Jubilee celebrations. The Prime central market will remain resilient but not strengthen, we expect a flat market in 2013. Wrong, too conservative, it continued to power ahead rising c12%.
- **Private rental sector:** This sector will continue to grow in importance. By 2020 we expect more people to be renting than owning homes. Correct.
- **A couple of other thoughts for 2013: the US economy will strengthen correct, the Euro woes will continue to be a theme throughout the year correct, William and Kate will produce a male heir to the throne called George correct, amazing!**

All in all we think these predictions were OK, and a good result on the new royal heir; odds of at least 10:1 would have been given at the start of 2013!
We were slightly conservative in our predictions, and there were probably 2 reasons for this;

- having experienced a sluggish property market for the past 5 years it was hard to be too upbeat
- more importantly, we did not foresee the help to buy scheme and the impact this would have on the market as a whole.

The Help to Buy scheme started on 1st April 2013 and it has had a strong impact on the national property market. Few forecasters predicted the scheme, and even fewer would have forecast its impact on the market. Nonetheless it has been a very welcome boost to the sector.

Our Predictions for 2014:

We are more positive on the market than we have been for over 5 year. The market is relatively buoyant and we expect this underlying strength to continue throughout 2014.
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.
- **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.
- **Rental growth:** Will be flat but part of a longer term upward trend.
- **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.

- **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.
- **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.
- **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.
- **New housing starts:** will be higher still than the 2013 numbers.
- **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.
- **A couple of other thoughts for 2014: Brazil win the football world cup, Scotland will not vote for independence, Euro problems will continue throughout the year, North Korea will cause concern to the global powers, Prince Harry will get engaged.**

Our Recommendations for 2014:

Given our predictions for 2014 above, it is clear that we believe residential property will be a good performer over the year. However, it is increasingly difficult to predict the potential returns of other asset classes such as gold, equities, bonds or commodities. We are coming to the end of the (so far) successful quantitative easing strategies which have helped support all markets; what the impact of their unwinding will be is extremely difficult to foresee.

However, whilst there is uncertainty and wariness of other asset classes, we believe investors will be attracted to bricks and mortar due to its lower volatility and long term growth potential.

Where should one buy?

Whilst we predict national house price increases of 7% over 2014; there are many anomalies and opportunities within the market that will allow investors to make superior returns. We always recommend purchasing on a 5year + 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 a number of properties, and also source a number of properties for our retained clients.

- Example cities are Leicester, Nottingham, Peterborough and Northampton
- Prices are often 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
- Benefitting from recovering economies
- Benefitting from the ripple effect as wealth and jobs and business flows out from London
- Key commuter locations

Also, we are particularly active in the **City of Kingston upon Hull**, voted city of culture 2017, but also where we have our own property management team and a 10 year track record of property investment expertise.

- attractive rental yields; 8%
- prices still near their 10 year lows and at low absolute prices; from £40,000 upwards.

- high rental growth rates from a low level
- High yields help ensure that residential values do not fall.

We review a number of opportunities throughout the UK each year; we are not geographically constrained. Each is assessed on a project by project basis and on its individual merits. As always, due diligence of the unit(s) concerned is imperative.

The regions identified above we particularly like, but most importantly they meet the basic rules shown below that are imperative in property investment;

Capital values: Are considerably lower in all these areas than in London and the South East. Prices in many areas fell c50% from their 2007 highs, they have generally outperformed the wider national market in 2013, and we expect them to continue outperformance in 2014. These are areas that were hard hit from the property crash (unlike London and South East) but are benefiting from the stronger economy and wealth that flows from London. Talk of a "property bubble" in these areas is far fetched, prices are still c8% down from their peak in 2007.

Rental yields: Are typically 6% plus and rents are underpinned by strong underlying tenant demand. We have always believed that rental yields are an important part of total return and gross rental yields of 8%+, netting down (after running costs) to c6%, are an attractive income stream. Yields of half this amount are typically available in London.

Total returns: There are TWO key parts to the total return from residential property investment; capital appreciation AND rental yield. We have always focussed primarily on rental yield and secondly on capital appreciation. The market in London may rise the same as the national market, but the total return including the rental yield will be better in these target regions.

RPG Property Finding Service:

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.

Conclusion:
Property must be purchased well, and managed well.
We act as property finder for you the buyer (not an estate agent for the seller)
We act as property manager for you (ensuring a seamless hassle free service)
By using our services we considerably increase the chances of attaining a higher total return for your property investment.

We wish our clients and friends a very prosperous 2014
The Team at Residential Property Group Limited