SPR Newsletter
March 2011

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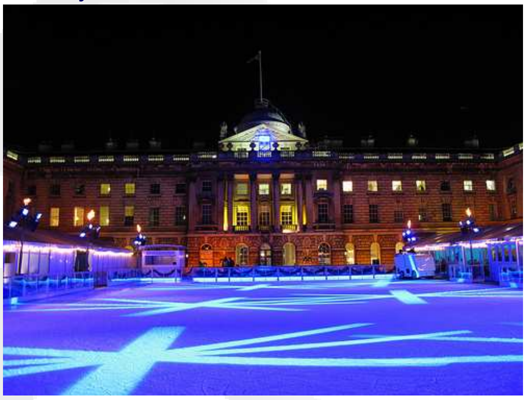
Coming Technical Events

Coming Social Events

This is already fully booked.

Save the date

Social Event Reports



Technical Event Reports

Ross Walker, UK Economist at RBS, explained his organisation's view of UK economic prospects, which anticipates GDP growth of 1.5-1.75% in 2011. This is based on a positive assessment of the prospects for UK business investment, given that balance sheets look relatively strong.
Full report on page 7.

Upcoming Technical Events

Peer Review Event - Real Options and Real Estate Development Decision Making
Wednesday 2 March 2011, 5.30–7.30pm
BNP Paribas Real Estate UK, 5 Aldermanbury Square, London, EC2V 7BP

Chair: Robert Fourt, Gerald Eve
Speaker: Gianluca Marcato, Henley Business School
Panellists: Tony Key, CASS Business School
Michael Lightbound, Argent Group

The seminar will explore Real Options and their application in real estate development – Gianluca Marcato will introduce the concept of optionalities and present a modelling framework that can be used strategically when faced with option choices, such as the choice between starting or delaying a project, or the choice between holding or selling land, demonstrating this with a development project valued using a real option model.
The panel will then discuss the practical applications of Real Options theory in real estate development and its potential role as a vital tool in the real estate industry.

Upcoming Social Events

SPR Quiz Night
Thursday 17 March 2011, 6.30-10.00pm
the CITY FLOGGER, a Davy's Wine Bar on Fen Court, 120 Fenchurch Street , EC3M 5BA
http://www.davy.co.uk/cityflogger

Come and compete for the prestigious SPR QUIZ TROPHY!

Buffet food will be provided.
This event is now fully booked

8th Annual SPR Golf Day
Thursday 26th May 2011, **Aldenham Golf and Country Club**

Sponsored by:

PROPERTY DATA
www.propertydata.com

It's time to dig those clubs out and dust them down, for the famous SPR Golf Day is just around the corner! After last year's scorcher, we're heading to cooler climates further north – near Watford - for this year's event. Aldenham Golf and Country Club is a tried and tested venue and has been the home of some excellent SPR golf days over the years.

The day will run as follows:
0800 Registration, bacon rolls and coffee
0900 First tee-offs on 9 hole warm up round
1200 Ploughmans and soup lunch
1245 First tee-offs on 18 hole competition
1800 Refreshments and prizes

The day has been kindly subsidised by the SPR and sponsored by Property Data, and comes at a bargain price of just £28 for SPR members.

Please don't delay booking, as the event is usually booked up very quickly!

Organisers: Michael Moran (07833 538 507) and Craig Wright (07919 074 094)

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Recent Social Events

SPR Annual Dinner & AGM, 11th November, 2010

1 Great George Street, London SW1

The Annual Dinner was well attended as always, with 120 members of the society present.

Professor Tony Key of Cass Business School was awarded an SPR fellowship in recognition of his contribution to property research. Before entering academia Tony Key played leading roles at PMA and IPD.

The raffle raised £1,045, which was donated to the National Autistic Society.

At the AGM the new committee was unveiled. The members are:

CHAIR: Kieran Farrelly, CBRE Investors
PAST CHAIR: Ruth Hollies
VICE CHAIRS: Henri Vuong, PRUPIM
Rebecca Shafran, Cordea Savills
HON.TREASURER
Andrew Marston, CB Richard Ellis
HON. SECRETARY
Kevin Mofid, BNP Paribas Real Estate
GENERAL COMMITTEE
Mark Clacy-Jones, IPD
Charles Conrath, JPMorgan Asset Management
John Danes, Aberdeen Property Investors
Simon Durkin, RREEF
Cleo Folkes, St Martin's Property Corporation
Oliver Gilmartin, RICS
Adelaide Gray, Legal & General
Richard Gwilliam, PRUPIM
Phil Hammond, Property Market Analysis
Marie Hickey, Savills
Fergus Hicks, DTZ
Anne Koeman, LaSalle Investment Management
Simon Marx, LaSalle Investment Management
Alex Milojevic, Cushman & Wakefield
Michael Moran, Moran RAC Ltd
Fotis Mouzakis, Cass Business School

Ice Skating & New Year Drinks, 12th January 2011

Somerset House, London WC2

This year's ice skating took place on a balmy January evening; but fortunately the ice was still frozen hard. Richard Gwilliam of PRUPIM took the plaudits as the most elegant SPR skater while Bob Thompson of RETRI deserved applause as the bravest beginner. Kevin Mofid (BNP Paribas) drew praise as the most stylish wearer of a duffel coat (see photo below).

After an hour on the ice, the skaters adjourned for a buffet supper and mulled wine at the Old Bank of England pub in Fleet Street.

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Recent Technical Events

Unless stated otherwise, meeting reports written by Tim Horsey

SPR Retail Research Briefing, 30th September, 2010

Grosvenor, 70 Grosvenor Street, London W1

Richard Barkham of Grosvenor chaired this meeting.

In his introductory presentation on European and Global retail trends, **Neville Moss** of CBRE emphasised that although retailing was now a very international business, global retailers are nevertheless pursuing a wide range of strategies on the type and range of locations they wish to occupy. And amongst those retailers aiming to globalise, some nationalities – in particular the US – are proving to be much more successful than others.

Europe's retailers have become more positive about business prospects over the last 12 months, suggested Moss, with those in the Northern countries generally more optimistic than those around the Mediterranean. International retail chains' expansion plans are focusing on traditional core European markets, but also on Central Europe, according to a recent CBRE survey of leading firms. Luxury retailers in particular are also targeting core markets in their expansion plans – France, Germany, Spain and Italy – rather than emerging locations where it may be difficult to find the right kind of High Street space.

Beatrice Guedj of Grosvenor's Paris office concentrated exclusively on high-end retail – that is properties occupied by luxury brands located in prime locations. These assets have remained in demand by institutional investors due to their secure long-term cash flows, and may well be a leading indicator of European retail property markets in general. UK luxury retail property is already bouncing back according to Guedj, while in Germany and France this part of the market, though more cautious, is likely to avoid the protracted downturn that looks possible in more secondary retail areas.

London and Paris see some of the highest rents for luxury retail in Europe due to the size and wealth of these capitals and their immediate regions, compared to Spain where there are two economic drivers, Madrid and Barcelona.

For Continental Europe at least, double figure rental growth belongs in the past. In Spain this is not only because demand has weakened but also due to a growing supply of stock in prime streets, often with financial organisations leaving these areas and freeing up large high quality premises. But through the crisis the purest of the luxury locations have not seen rental falls, although tenant concessions have increased. The worst affected locations have been Spain and Italy where some domestic luxury brands have been hard hit. Capital values of luxury retail have also held up relatively well in Continental Europe, though they have proved more volatile in UK, and have fallen significantly in Spain.

In the near future some expect that the Continent will follow the pattern of decline seen in UK, but Guedj believes that this may not be the case due to the rise of retailers in the space between volume fashion (eg Zara) and luxury fashion. Many of these have set up flagship stores in high-end streets, preferring to do this rather than take prime pitches in regional centres as they did in the past.

Hilary Atherton of JLL took a ten year perspective on the future of European retail – how consumer needs are changing, and how the retail market will have to react to these changes. This was based on a JLL survey of late 2010 undertaken in collaboration with a futurologist, which identified eight key trends.

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Of these Atherton emphasised advances in technology, which have made shopping much more convenient, and the widespread use of mobile phones which is making comparison between retailers much quicker, with images of alternative products visible on smart phone displays. Technology is also likely to speed up payment, while stores may be tempted to have less of their products on display. People may become less concerned about trying on fashion goods before purchasing, particularly as virtual shopping technology can allow a scanned body shape to be electronically recorded and the desired clothing to be displayed digitally in 3-d form.

SPR /IPF European Property Outlook
19th October, 2010

Freshfields Bruckhaus Deringer, 65 Fleet Street, London, EC4

Report by Anne Koeman, PRUPIM

On a rainy Tuesday evening in November, Freshfields Bruckhaus Deringer hosted the 2010 staging of this annual event. In collaboration with the Investment Property Forum (IPF), the SPR put together an impressive line-up of speakers, and a large number of members braved the weather to hear their views on prospects for the European economy and property investment markets.

Peter Hobbs, who has recently joined IPD as Senior Director after a number of years at RREEF, chaired the event, and opened proceedings by asking the audience for their an indication of their intentions on investing in European property: about 50% of the audience intended to invest more in Continental Europe in 2011 than in 2010, with only 30% of the audience intending to invest less.

Sabina Kalyan, Head of European Strategy at CBRE Investors gave the first formal presentation, setting out the economic context. She took the unconventional approach of dividing Europe into beer-drinking and wine-drinking countries, while placing the UK in a separate category of breezer-drinkers.

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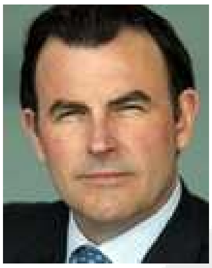
The beer-drinkers, comprising Northern European countries such as Germany, Netherlands, Austria and Scandinavia, are in a better shape – in terms of relative wealth, current accounts, costs of credit, and unit labour costs – than the wine-drinking countries, which are mainly in Southern Europe. For the future, however, Kalyan sees difficulties for both groups of European countries. With no means to devalue their currency, the wine drinking countries need to cut wages to improve their competitiveness. This may have very damaging effects, including deflation.

On the other hand, the beer drinkers are unlikely to see much growth as consumer spending remains weak and their export-led growth model is likely to falter if the Euro appreciates further. In the years ahead European banks will have an important role to play, stabilising their balance sheets and returning to an efficient allocation of capital. However Kalyan does not see that happening very quickly and expects economic growth to remain subdued with capital markets continuing to be volatile.

In an innovative section of this year's event, **Bill Dinning**, European Head of Investment Strategy & Economics at AEGON Asset Management, then placed the prospects for property across Europe in a multi-asset investment context. He explained that property is generally looked at in terms of its relative pricing against government bonds. Currently, returns from core European government bonds are very low, reflecting the low expectations in economic growth. Against this backdrop, the risk premium for property is high, making the asset class look attractive. But what about other asset classes? If you compare property with equities, you find that they are not too dissimilar. However, at the moment equities may look more attractive than property, as dividend yields across the world look extremely good value when compared to low bond yields.

Dinning also reminded the audience of the vast costs incurred by the world's advanced economies, including the European Union, in fighting the financial crisis – which dwarf those seen in all previous crises.

Governments are digging deep into their wallets out of a fear of deflation, producing the possibility of high-inflation scenarios for the future. If you believe in this possibility, Dinning concluded that you would be right to invest in property.



The final presentation, focusing on the implications for European property investment, was given by **Dennis Lopez**, Head of Global Fund Management, at AXA REIM. He outlined the main opportunities and threats facing the three main property sectors, as well as looking at the prospects for the different European regions, and argued that disparities in occupier markets will be key in the current recovery phase. Lopez also examined the State Street Investor Confidence Indicator, which shows that investor sentiment has become significantly more volatile over the past few years, accompanied by a trend towards greater risk aversion. Lopez closed with some insights into some recent development and investment deals undertaken by AXA, showing the transition from theory to practice.

After a question and answer session the audience moved outside to the bar area and enjoyed some networking drinks, kindly provided by Freshfields.

SPR Peer Review: Capital Market Expectations and the London Office Market, 6th December 2010

Report by Ruth Hollies, Alecta

Simon Stevenson, Professor of Real Estate Finance and Investment at Henley Business School, presented the working paper that he had co-authored with James Young of the University of Auckland.

Simon explained the motivation for looking at financial variables on rents in the City and West End combined with more "traditional" variables of economic growth, employment and so on. Within the vector error correction specification it is possible to investigate the size and magnitude of shocks to chosen variables in terms of the variance decomposition and impulse response function. The variance decomposition provides an idea of the size of a shock and the impulse response function gives an indication of how long the impact of the shock will be felt.

People might expect that financial variables would be relevant to the City market, given the occupier base, and less so for the West End. However, the modelling found that they were in fact significant for the West End, although smaller than in the City market. In part this may be explained by the term spread capturing expectations of future interest rates and the default spread providing some indication of expectations of economic performance; a widening of the spread would indicate lower corporate credit worthiness. The model had been run over different time periods to see if the financial crisis impacted on the results.

The work provides an understanding of the importance of lagged rents and other demand drivers on rental market dynamics. It also highlighted that capital market variables had an impact on West End rents and so provided evidence that expectations of economic activity are to some degree embedded in today's rents.

Sotiris Tsolacos, Director of European Research at PPR, one of the panellists, emphasised the usefulness of bringing this kind of academic work into real world forecasting and modelling procedures. The work also adds a new dynamic to the understanding of the London office market.

Martin Davis, Head of UK Research at DTZ, the other panellist, suggested that it was an interesting piece of work while observing that the supply side was missing in the equation specifications. This provoked some audience discussion of the impact that the omission of supply variables might have.

There was also a discussion around the availability of net effective rental information and other inducements to occupiers that may influence the estimated relationship, as the model was specified using headline rents from the CBRE prime index. This issue of the appropriate rent to use is not solely confined to this type of modelling but also applies to other analyses as there is a lack of long time series on net effective rents.

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SPR / IPF Outlook for UK Property meeting, 26th January 2011

Royal Bank of Scotland, 280 Bishopsgate, London EC2

At the start of the meeting, which was chaired by **John Stephens**, Ian Thurman of CACI paid tribute to his colleague Gordon Cousland, who was killed in the bombing of Moscow's Domodedovo Airport on 24th January. Gordon, an SPR member, was working to establish CACI's Eastern European retail research business. "He had tremendous energy and enthusiasm," said Thurman. "Now we all have to summon up the energy to carry on as Gordon would have wished."

Ross Walker, UK Economist at RBS began by explaining his organisation's view of UK economic prospects, which anticipates GDP growth of 1.5-1.75% in 2011. This is based on a positive assessment of the prospects for UK business investment, given that balance sheets look relatively strong. Whether this potential private sector demand can overcome the impact of public sector retrenchment will be largely down to business confidence, Walker suggested. Although household income is likely to be weak and eroded by inflation, with real growth only re-emerging in 2012, the strength of many manufacturing and other non-financial businesses should counteract this – particularly where they are more reliant on international rather than domestic demand. In terms of property demand, Walker noted that the retail sector looked vulnerable in the short term.

Tapan Datta, Global Asset Allocator at AON Hewitt provided a "bird's eye view of property investment assets", reflecting the underlying fundamentals for the various asset classes over the coming three years. Datta proposed that 2009-10 had been a very good period for risk assets, including property, but now prospects looked mixed. The big risk was that bond rates would be pushed higher with the threat of inflation increasing; property yields currently look good value as against gilts, but this is based on a long period of very low gilt yields which is now likely to end. Property and equities risk premia look healthy compared to their long-term averages, but equities growth is likely to be constrained by the fact that profits are already high and unlikely to go much higher.

Datta commented that property looks fairly priced compared to its main 'alternative' asset competitors, infrastructure and private equity, but not much more attractive than them. He sees a 'base case' property return of the order of 8.5% pa over a ten-year period, with a worst case scenario of 5.2% pa. One advantage for the asset class could well be a return of diversification benefits, since the last few years have seen an unusual degree of convergence with equities as a result of the financial crisis and the subsequent policy response. This is now likely to have run its course.

Andrew Jackson, Head of Wholesale and Listed Real Estate Funds at Standard Life Investments, focused on the property sector itself, predicting a return of 3-4% for 2011 with some marginal falls in value, while over the next three years performance should just about reflect the income return. Jackson warned against seeing the current weak market as similar to that of the 1990s, even if there might be some outward similarities. In particular the previous cycle was more inflation driven, and this time round rental markets should prove more solid as there has been less development activity.

Over recent months income returns have been rising with rising occupancy rates. Property income may well prove to be a better hedge for whatever inflation emerges in the coming months as there isn't the drag of oversupply seen in the previous downturn. But a lot will also depend on the particular locations of investments, as void rates are starting to vary dramatically between different parts of the UK.

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