

## **Investment**

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### **Headlines**

- **The current investment “bubble” will soften.** The current investment “bubble” for prime real estate is likely to soften in the first quarter. Fuelled by cash inflows from the public into the retail funds (the very funds which were undertaking sales to meet redemptions a short while ago) prime property has shown circa 20% value increase over last year. Investors are adopting a chartist approach – what goes down must go up – they are by definition optimists. However the impact of an end to quantitative easing, higher tax rates, election uncertainty, unemployment, Dubai, potentially Greece, and better savings rates will take the steam out of the market at the sharp end. Whether it is a VW, or a “corrugated” recovery, it is not a straight line up from here.
- **Secondary stock will continue to languish.** Those who anticipate a substantial rebound in poorer quality stock are mistaken. There is not a piece of strong elastic linking prime and secondary property, so that it is dragged up along with the quality stock. Buyers are focused on fundamentals of quality and income stream. The occupational markets are, and will remain, in a dire state for the next couple of years. Poorly located or elderly property, with short lease profiles exhibit risk that institutions and bank finance will continue to avoid. Landlords already suffering with empty secondary stock may be hoping for a gradual improvement in the occupier market, but the reality is that the impending rating revaluation and sustainability agenda will further devalue their buildings.
- **Core Central London offices a good prospect.** Central London offices in core locations will continue to find favour as quality vacant accommodation becomes more scarce and rents recover. As the UK lags other economies in recovery from recession, Sterling will remain low, and overseas investors will seize their opportunity to gain a foothold in the Capital. Outside of London the major provincial centres will see all but the most prime buildings suffer

from increasing investor awareness about the capital expenditure needed to offset depreciation, and take account of this in the returns they demand.

- **Second hand distribution affected by supply.** With the highest supply of industrial and warehouse stock in England and Wales recorded at 23.31 million m<sup>2</sup>, of which 3.42 million m<sup>2</sup> comprises new stock, investors in distribution warehousing will become more cautious. With the exception of those buildings exhibiting bond style characteristics with long leases, to strong tenants, the majority will be subject to short term leases in line with 3PL 5 year contracts and intermittent voids. Distributors will upgrade building with contract renewals, severely impacting on the lettability and ERV of second-hand buildings.
- **Post Christmas hangover, but gentle recovery for Retail investment.** After an upbeat Christmas period, retailers will find early 2010 much harder as the VAT rise bites, and consumers are affected by uncertainty over the election, higher taxes and reduced Government expenditure in the economy. Further CVAs will occur amongst mid market retailers, though the budget and “trusted” brands should fare better. In 2009 we recorded one retailer failure a week. 2010 will not repeat this level of attrition. Rental growth in this sector will be first to return though this will only be evident in the very best of towns. Unit shops will be most sought after by investors, though a slow return of institutional investors to shopping centres will occur.
- **Scarcity of Open A1 Retail warehousing will prove a positive.** Investors will continue to embrace the best quality retail parks, once again attracted by the value of limited Open A1 planning consents. There is a sense now that the occupiers who remain are likely to be survivors and that the scarcity of good parks is such that buying now for the medium term will not be regretted.
- **Operational premises with fixed growth sought after.** Increased interest will occur in fringe sectors such as student housing, medical, hotels and other occupational property. Such sectors offer the long leases, and often fixed or indexed rental increases, which are increasingly rare in the mainstream of retail office and industrial.

- **“Pretend and extend” will continue to be the prevailing bank policy.**  
Bank finance will slowly become increasingly available, but with £32.6 billion of debt due for redemption in 2010, refinancing this amount will prove impossible without a continuation of the “pretend and extend” policy the banks are exercising. Not wishing to write off significant debts to their balance sheets, toleration of all but the most serious breaches will be necessary, extending existing loan agreements. As balance sheets strengthen, the worst loans will be called in, but every opportunity to restructure with new equity will be taken, so the flood of distressed sales some are expecting may largely be averted.