obbard
inspired property investment

2017?

February

In the immediate aftermath of the financial crisis it was often said the only certainty was uncertainty. As we head in to 2017, the degree of uncertainty across the globe can sometimes seem off the scale. My last missive made reference to the impossibility of avoiding any mention of Brexit, as we start the new year this looks like being trumped (apologies for that). By the second half of the year we may well be fixated on the Eurozone, or , God forbid, something bigger. Sometimes you feel like drawing the curtains and reading a good book or watching a movie, one of my favourite Sunday afternoon films is 'It's a mad, mad, mad, mad world'…..just saying.

Understanding, let alone predicting, the property market presents quite some challenge these days. This isn't to say the property market is any more uncertain than other markets or investment sectors. In fact it is perhaps a little easier to understand as I would argue history has shown us a couple of clear patterns over the past few decades. Firstly, when it comes to the broad domestic market, it is above all about interest rates and how the market responds accordingly as these rise or fall. Linked to this is the availability of credit which drives transaction volumes. Secondly, there is the prime market which is less mortgage dependent and far more discretionary. The lesson learnt here is that prime real estate is usually seen to be the last asset of choice to dispose of when times become tough or uncertain.

This is well illustrated in how the two sectors have performed over the past year. Data from HMRC shows that there were 1,231,120 residential transactions last year, ahead of the number of transactions in both 2014 (1,124,860) and 2015 (1,225,970). The distribution of transactions however was rather skewed last year, as many landlords bought properties before the higher rate of stamp duty on second homes came into effect at the beginning of April, creating a spike in March, the highest number of transactions made within a single month for the last ten years. However over the past three years as mortgage rates fell to reflect the reality of the 0.5%, now 0.25%, base rate, transaction volumes have been very robust and house prices on average have risen by around 4.5% pa.

By contrast, prime London has seen transaction volumes fall by an average 25%, rising to 50% in some areas/pricing brackets, and prices having come down by an average 10% since the high in late 2014. Over the course of the last three months there has been a very noticeable upturn in activity however, with many overseas buyers looking to capitalise on sterling's weakness as well as pent up demand being released, as we entered the post referendum era. However, aside from the oversupplied luxury new build sector which has a large pipeline still coming on stream, there is no surge of properties coming to the market as owners are not looking to exit or realise some of the substantial profits made since 2010. There are many who might indeed be tempted to realise their gains but the question then posed, where to invest the proceeds, is one that remains to be answered.

A reflection of the prime market can be seen by taking two example clients' experiences in 2016. One was after a good family house with a garden in Chelsea, Belgravia or Knightsbridge with a budget of around £7m. We started the search in mid 2015. Over the course of approx. 16 months we saw 11 houses (approx. a further 10 were dismissed out of hand) of which 5 were sensible possibilities. Of the 5, we pursued one but were out bid (over asking price) and agreed another at £6m on an asking price of £6.35m, reduced from £6.75m. Of the other three we had identified as possibilities, two remain on the market, one of which has the complication of a 20 year lease.

Another example was a brief to find a really good two bed flat on a prime garden square around Cadogan Square, Onslow Square etc. with a budget of £3m or so. This search started in late 2014. Over that period we viewed or had identified around a dozen properties, there were probably at least that number again of flats quickly dismissed. Of the 15, there were again only 4 or 5 worthy of serious consideration. All have since sold but we agreed one of them quite recently at £3.25m, having previously been under offer at over £4m at the end of 2014.

By contrast budgets such as these open up a world of choice in the luxury new build sector within the newly emerged areas, particularly stretching along the south of the Thames from Chelsea Bridge to Tower Bridge. With supply of development sites so constrained in the traditional prime areas, developer activity is being focused on emerging residential areas like Holborn, Kings Cross and Shoreditch as well as other historically more mixed resi/commercial locations like Victoria.

UNDERSTANDING BUYER MOTIVES

For quite some years now we have observed the bulk of buyer interest having a dual motivation. Firstly there is an underlying need of some sorts to acquire a property. This could be for immediate own use either as a principle or second home, for children's current or future needs (particularly in relation to foreign students) or as a future home for returning expats or overseas buyers with longer term plans to move to London. The other motivation is linked to investment and/or wealth preservation and despite the challenging market conditions with yields at an all time low, stubbornly high prices, Brexit uncertainty and an increasingly less favourable tax regime, the inherent long term confidence in London property appears to be undiminished.

Buyers are rightly wary of overpaying and therefore the well informed seek sellers who also have a need to transact, as opposed to those listing and hoping for a fool's offer. With prices looking weak and likely to remain flat for the next couple of years, there is little in terms of time pressure being applied to buyers, equally with interest rates at or around current levels, there is no pressure on sellers as well. Some overseas buyers may have switched in to sterling to lock in the lower rates and many are happy to take their time, often renting, as they become ever more selective. With the general view that prices are unlikely to appreciate for a while, off plan sales have lost much of their appeal and buyers are now more likely to want to physically stand in their potential purchase before committing. The result has meant that the market still remains reasonably active but transactions are more likely to take place where there are level heads on both sides of the equation.

THE FUTURE

There is a feeling that there is real change taking place in the UK residential property market. Home ownership as a percentage of the population is falling rapidly, to the extent that we now come close to matching France. Even the Germans, well known for their propensity for renting, are fast closing the gap. As a result, the nature of property investment is changing as well.

It was around 20 years ago that buy-to-let was born. This came about as the Housing Act 1988, which introduced the Assured Shorthold Tenancy, was significantly amended and improved in 1996, followed by the advent of specific buy-to-let finance. With access to high loan to value funding based on the property alone, buy-to-let became accessible to 'the man in the street'. Fast forward two decades and the Government has stepped in to reverse this by removing most of the key tax benefits such as mortgage finance offset and furniture depreciation and adding a penalty stamp duty levy. The rationale behind this new attitude is the belief that buy to let investors are competing too aggressively with owner occupiers in a market where there is a critical undersupply.

Meanwhile, the undersupply of housing is such a concern that the Government is actively encouraging large scale investment in rented housing and looking to encourage institutional investment in this sector. It is clear for all to see that the issue of house prices being fundamentally unaffordable for so many is here to stay and therefore the future lies in building more rental stock. In effect that 'man in the street' who would chose to have faith in property as a long term investment/pension plan is being deliberately squeezed out. The result has seen the clock wound back to those days prior to buy-to-let funding, where ownership of second homes whether for investment, own use or children's futures, is once again the preserve of the very wealthy (more so foreign buyers than previously) where funding is an option and not a necessity.

Those buyers are likely to concentrate on established prime areas, a few emerging hot spots and a specific key university towns and cities. Meanwhile the primary players replacing the individual buy-to-let investor are now likely to be larger scale investors active in the build to rent sector and a few large institutions who will be growing very sizeable portfolios over the years ahead as generation rent becomes established.

A NEW LOOK AT OBBARD

We are excited about 2017 as we are undergoing a rebrand. We did this some 12 years ago and, just like the last time, the intention is to better reflect the business that we have evolved in to. We shall be announcing this within a few weeks.

Many clients know us for our 'day job' of finding good individual investments or homes in prime London and then adding value. Having now refurbished over 300 properties of varying size, budget and complexity, we have seen this side of our business really grow. The following is a snapshot of projects last year;

HOLLAND PARK - Refurbishment of 14,000 sq ft house with end value £55m Owner client

ST JAMES'S - Refurbishment of block of 5 flats with end value £25m Investor client

HAMPSTEAD - Refurbishment of 5,800 sq ft house with value circa £6.5m Investor client

HAMPSTEAD - Refurbishment of 1,100 sq ft flat with a value circa £1.25m Owner client

KENSINGTON - Redevelopment of 4,000 sq ft house with value circa £10m Investor/Developer client

KENSINGTON - Redevelopment of 2,300 sq ft flat with value circa £5m Owner client

KENSINGTON - Refurbishment of 1,300 sq ft flat with value circa £2.75m Owner client

SOUTH KENSINGTON - Redevelopment of 2,400 sq ft house with value circa £5.25m Investor/Developer client

SOUTH KENSINGTON - Refurbishment of 790 sq ft flat with value circa £1.75m Owner client

CHELSEA - Refurbishment of 1,500 sq ft flat with value circa £4.25m Owner client

CHELSEA - Refurbishment of 1,600 sq ft flat with value circa £3.25m Investor client

CHELSEA - Refurbishment of 1,824 sq ft flat with value circa £4.5m Investor/Developer client

CHELSEA - Refurbishment of 3,225 sq ft house with value circa £6.75m Owner client

KNIGHTSBRIDGE - Redevelopment of 2,750 sq ft house with value circa £7m Investor/Developer client

BELGRAVIA - Refurbishment of 1,150 sq ft flat with value circa £2.75m Owner client

HOLLAND PARK - Refurbishment of 14,000 sq ft house with end value £55m Owner client

ST JAMES'S - Refurbishment of block of 5 flats with end value £25m Investor client

In addition to the above, we have branched outwards, in terms of location, and sought investment opportunities well beyond London and the South East where we feel real value can be found, more on this to follow in future missives.

Future communications will have a new look and feel but for now, as before, here are a few opportunities that have caught our eye;

Herewith example opportunities;

KNIGHTSBRIDGE, SW3, **Target Price £5.75m** **Asking price £6.75m**

Eager seller

Originally listed at a far too ambitious £7.85m in late 2015, the vendor of this house is under pressure to sell. It is a very good family house just off a garden square extending to approx. 2,816 sq ft. In good condition but needing a cosmetic uplift.

SOUTH KENSINGTON, SW7 **Target**
Price £4.25m **Asking Price £4.25m**

Forced sale

A terrific first floor flat, approx. 2,600 sq ft, in a period building with a designated off street parking space. Due to health reasons the vendor needs a quick sale. This is a smart building with day porter, the first floor has tremendous volume and lateral space. The apartment needs modernising at a cost circa £650k.

KENSINGTON, W8 **Target**
Price £3.75m **Asking Price £3.95m**

Garden nirvana

A delightful period house in need of upgrading, with its own 55 foot garden (with summer house) and overlooking Kensington's prettiest garden square. Approx. 2,115 sq ft offering 4 bedrooms, 2 baths and 2 reception rooms.

CHELSEA, SW1 **Target**
price £1.3m **Asking Price £1.35m**

Rental investment

A 5th floor two bed flat overlooking a quiet lock. Let at £37,700pa until mid 2018. This apartment is within a development that we have regularly invested in and which we pick to outperform due to its unique situation lying between too of the most high profile regenerastion/development schemes currently.

BARNES, SW15 **Target**
Price £17.5m **List Price £24.3m**

Bank sale

This development was completed in July 2016. It consists of 9 town houses and 12 apartments, of which six apartments have sold. The investors (a family office and small syndicate) returned to their lending bank for an extension to their loan. A further loan was agreed subject to additional cash required by the investors but they were nor able or willing to provide this as the family office wanted its initial investment back. The investors and bank are working together to arrange an exit at a substantial discount to market value.

The project had a formal RICS valuation in November 2015. The target purchase price shows a 28% discount on red book valuation. On our own revised (down) values, the projected ROC after buying, selling and other expenses equates to 15%. The anticipated gross yield, based on projected rents at 15% below valuation, equates to 4.5%.