

Reita monthly UK property market update – September 2008

Welcome to the first monthly Reita update on the UK REITs and Commercial Property market. We hope it will be the first of many such updates and that here you will find a useful concise overview of development and key news items. In these turbulent times we believe that there is a need for non-partisan information and this is at the heart of our mission. Reita is a not for profit organisation whose core objective is to raise awareness and understanding of property investment and REITs. Reita is supported by the British Property Federation, leading UK REITs, international fund management companies, corporate advisers, London Stock Exchange, EPRA and NAREIT.

Please visit our website www.reita.org for more information and to contact us about any of the items covered in this note. We would also be pleased to hear about any other areas that readers would like us to cover in the future.

Movements in the UK REITs market during September

September was a turbulent month for stock markets across the globe and UK REITs were not immune to these disturbances and during the month there was significant volatility with several daily movements of more than 7% up and down. However over the whole of September the FTSE / EPRA / NAREIT UK REITs index was down only 3.5% compared to the FTSE 100 which fell by 12% during the same period. By the end of September the biggest gains amongst the large REITs were recorded by Hammerson who were up 3% over the month and the biggest faller was Brixton whose shares were down 10%.

Between July 15th, which was called the bottom of the UK REITs market by several analysts and 30th September, the FTSE / EPRA/ NAREIT UK REITs index gained 13.5% whilst the FTSE 100 fell by 5%, however October as we are all aware has continued to be turbulent and the future prospects are once again uncertain.

The discount to Net Asset Values for major UK REITs as measured by EPRA averaged 35% at the start of September. Updated information will be available mid October and will be posted at http://www.reita.org/live/Databank/chart_nav.html as soon as it is available.

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Other REITs news

The major issue dominating the news towards the end of September was the impact of the traumas in the banking sector and whether or not short selling of property stocks should be banned in the UK as it has been for financial stocks. It appears that a ban is unlikely to be brought in for UK property stocks despite concerns raised by several sources. The problems of volatility have been highlighted by many industry leaders and indiscriminate short selling has been blamed for much of this volatility. However this concern has to be balanced by the recognition that short-selling is also an appropriate investment strategy when the future looks poor and as a legitimate means to hedge risks.

During September three UK REITs reported annual or half yearly results; Derwent London, Town Centre Securities and A&J Mucklow. Between them these companies cover all three core property sectors of Offices, Retail and Industrial properties respectively. They all described strong underlying performance but also reported losses before tax as a result of declines in the value of their property portfolios of between 9% and 15%, with the majority of these falls occurring in 2008. Full details can be found on the Reita web-site.

REITs going forward

Short-term uncertainty about UK REITs' pricing is inevitable given market volatility; however a number of positive signs long-term signs are also emerging. The greater volumes of commercial property coming to market as a result of increasing bank pressure and the need for liquidity amongst banks is thought likely to provide a significant opportunity for the well funded and relatively lowly geared UK REITs. Their financial strength according to some analysts is likely to play a valuable part in assisting the return to orderly markets over the next 18 months. In the meantime debate continues as to how far REITs share prices have already built-in future falls in the value of direct property investments. Future months are likely to prove both stressful and interesting for investors, shareholders and observers alike.

Movements in the UK direct property market in September.

The Investment Property Databank (IPD) Monthly index published in September which measures ungeared monthly returns for UK direct property investment showed all property total returns falling by -1.1% in August compared with -1.3% in July.

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Over the same period declines in capital growth on a month-on-month basis also slowed to -1.6% from -1.8% in July, with the retail sector faring best and falling by only 1.4% compared to falls of 1.8% for industrial and office property. More information about the IPD monthly index can be found at <http://www.ipd.com/OurProducts/Indices/UnitedKingdom/UKMonthly/tabid/921/Default.aspx>

The future movement of direct property returns and capital values is uncertain, with most commentators predicting further downward pressure both from weakening tenant demand as a recession takes hold and as a result of large volumes of property coming to market as forced sales. This is likely to be a particularly painful period for highly leveraged private property firms seeking to renegotiate financing.

Expectations of future movements in direct property prices

Property derivatives are a key source of information for any investor interested in the UK commercial property market. The UK derivatives market is one of the most developed in the world and it is anticipated that the value of derivatives trades will shortly exceed that of the real commercial property market.

At the end of September the UK IPD All property index was indicating a year on year fall of 21% in capital values between December 2007 and December 2008, with a further fall of 13% to December 2009. So far this year capital values have fallen by around 12%, implying that further falls of around 9% by the year end. On the basis of the IPD index, initial yields are also indicated to widen further to over 6% at the same time.

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