Balham **Battersea** Battersea Park Chelsea Clapham East Putney Fulham Gloucester Road
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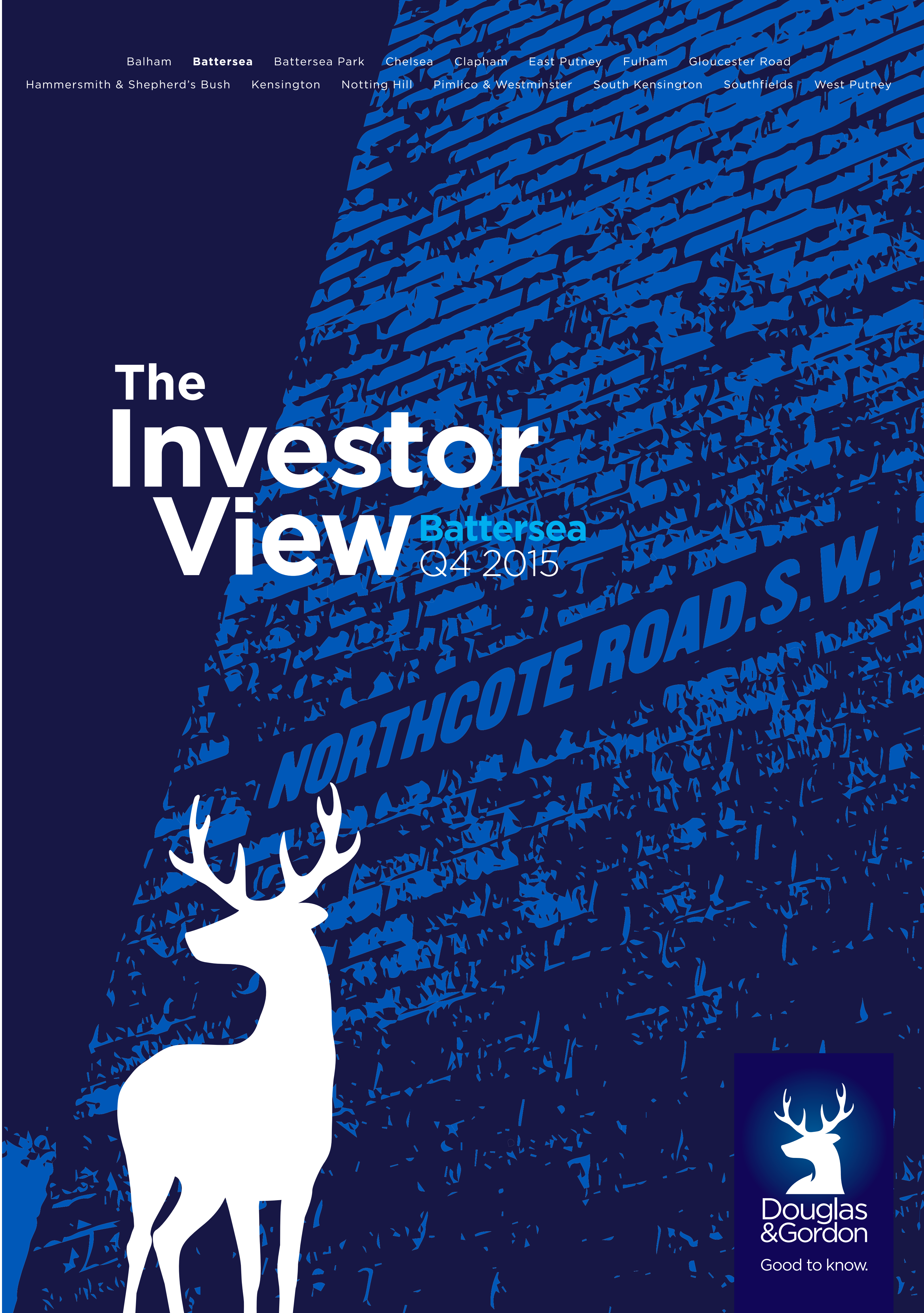
The Investor View

Battersea
Q4 2015



Douglas &Gordon
Good to know.

Introduction

Anyone who owns a property in London is a property investor. Our lives and plans often depend on the performance of what is likely to be the largest asset we own. So perhaps it will be helpful to take more of an investor's view of the market.

To produce this report we worked closely with D&G Asset Management, a company we co-founded in 2005. They deploy money into London residential property all the time, so they are constantly analysing different areas and the assets within those areas, seeking to maximise returns.

As well as publicly available sources, we have used the proprietary data that we have been capturing since 1996 to help us make decisions and provide advice and guidance to our clients.

D&GAM has helped us focus on the data that counts and we think the results make fascinating reading.

If you would like to learn more about the Battersea area, please do get in touch with our office on Northcote Road. Contact details can be found on the back page.

Property Values

Capital values in Battersea continued their steady uptick

In Q3 2015, capital values in Battersea continued their steady uptick. As you can see from the chart, however, prices of two bedroom flats and three and four bedroom houses remain below the peak in June 2014.

In the last quarter, capital values in Battersea outperformed many other Douglas & Gordon Emerging Prime offices, where prices fell on average by 0.56%.

Q3 2015 in more detail

- Property prices in the Emerging Prime residential market fall into three brackets; up to £1.1m, £1.1m-£1.7m and £1.7m+.
- The market below £1.1m continues to be firm. The top end of the market (£1.7m+) remains weighed down by the increases in SDLT rates.
- After the ups and downs of the last 18 months, Q3 2015 saw the return of a more normal market. Sensibly priced, well-located and well-presented properties, requiring little or no work, are achieving a good level of interest. Poorly located properties in bad condition are taking longer to sell.
- Q3 has seen a robust house market between £1.2m and £1.6m. Having fallen in H2 2014 this segment is now benefiting from a "reverse ripple effect". This is where potential buyers who have looked further afield are returning, after concluding that it is worth paying a premium to own in Battersea.
- The local French market has retracted due to a new French school opening in Wembley. We have, however, started to see some purchases associated with the US embassy, which opens in Nine Elms in 2017.

Background factors in play

- Homeowners across our Emerging Prime offices have large equity positions and are therefore discretionary sellers.

Battersea Nominal Property Values

Sales	Q3 2015	YTD	Since Q2 2014
1 Bed Flats	1.01% ↗	3.09% ↗	0.00% →
2 Bed Flats	0.72% ↗	2.19% ↗	-6.67% ↘
3 Bed Houses	0.36% ↗	1.82% ↗	-6.67% ↘
4 Bed Houses	0.66% ↗	2.33% ↗	-12.29% ↘

Source: D&G proprietary data

- Land registry data shows that between H1 and H2 2014, sales volumes in Battersea declined: flats -27%, terraced houses -44% and semi-detached houses -54%.

> In Q3 2015 buyers were price sensitive

- From a market perspective, these low volume sell-offs are a characteristic of "Prime" markets, where demand for property in an area always exists and buyers return after a short period of adjustment.
- Our research suggests that in Q3 2015 buyers were price sensitive as borrowers were wrongly guided to expect higher interest rates. See page 4 for our outlook on monetary policy.

Outlook

- Sellers should remain realistic and ignore headlines about UK national house price rises as they do not apply to London. The bull market in Battersea ended in April 2014.

How an investor looks at the market

Residential property investors use two key measures: the capital value of the property and its net rental yield.

You can make money from an increase in capital value and earn additional income by renting out a property you own. The net yield is the annual rent, less expenses, divided by the property's capital value.

Both are important and are influenced by many factors including: supply of new properties, infrastructure projects, demographics of the area, the economy (in particular, interest and tax rates) and the wider geopolitical picture.

The interplay of these factors is what determines investment returns and what makes property investment decisions so interesting. We hope this report provides some help as you assess your options.

Rental values in Battersea outperformed Emerging Prime

In Q3 2015, average rental values across D&G Land rose by 0.3%. Prime offices averaged a growth of 0.9% and Emerging Prime offices produced a very small increase of 0.03%. Against this background rental growth in Battersea averaged 0.9%. The breakdown of the numbers paints a complicated picture.

Corporate budgets are tightening - a message to house owners

- In our last report we described the Battersea house rental market as "subdued". As Q3 2015 unfolded, pockets of real weakness started to emerge and the higher up the chain one went, the more acute the problem became. One reason for this is that domestic renters are becoming increasingly cash strapped. Another reason is that Battersea is one of our "core" Emerging Prime offices that has recently experienced a decline in corporate relocation budgets.

Investors need to think ahead

- Over the past year we have written about the trend of corporate tenants looking for better value in lower-priced areas. We are now seeing more tightening of the belt, which will further impact the corporate rental market going forward. Investors need to think ahead.
- Fewer corporates means landlords will need to invest in upgrading their properties to appeal to the decreasing pool of prospective tenants, and/or consider the growing professional sharer market.
- Those house owners who have been averse to the sharers market will be interested to know that the demographics are shifting. Our internal data shows that 60% of our tenants in Battersea are over 30 – the new so called "generation rent": people who aspire to buy and want to maintain excellent credit records but have to remain in rental accommodation for longer.

Battersea Nominal Rental Growth

Rents	Q3 2015	YTD	Since Q2 2014
1 Bed Flats	0.00% →	2.67% ↗	10.00% ↗
2 Bed Flats	2.06% ↗	7.61% ↗	12.50% ↗
3 Bed Houses	4.32% ↗	8.21% ↗	11.54% ↗
4 Bed Houses	-2.86% ↘	0.00% ↗	1.19% ↗

Source: D&G proprietary data

Current Rental Gross Yields October 2015

1 Bed Flats	3.70% – 4.50%
2 Bed Flats	3.20% – 4.00%
3 Bed Houses	2.20% – 3.60%%
4 Bed Houses	2.20% – 3.60%%
10 Yr UK Gilt Yield	1.76%
FTSE All Sh Yield	3.60%
UK Base Rate	0.50%

Source: D&G proprietary data

- On a brighter note for investors, rental values in the Battersea flats market were firm in Q3, as indeed they were across D&G Land. One explanation for this is that the sales market has not, as yet, taken off and people are staying put in rented accomodation.

Outlook

- In this low growth and low inflationary environment, we remain cautious on rental growth.

Market context

“Bad” news for the global economy equates to “good” news for UK real estate assets?

In Q3 the global economic backdrop to the London property market was challenging (see chart). Some commentators believe that the recent turmoil in emerging market economies is the third stage of the global financial crisis that began in 2008. The implications of this are:

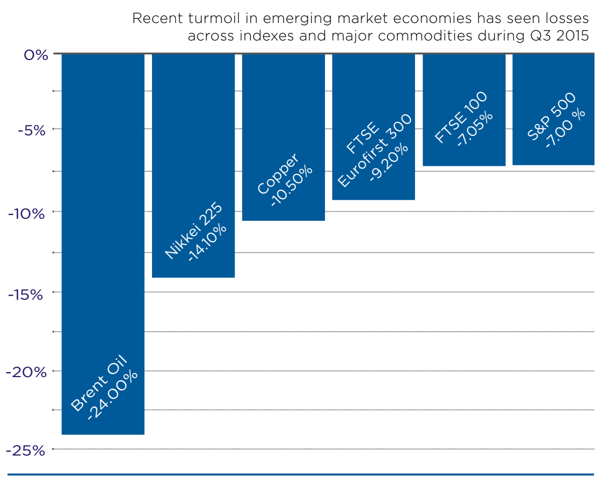
- Central banks across the world remain worried by no inflation:
  - In the USA: 2014 – 15 US median household income fell
  - In the Eurozone: Inflation turned negative in September 2015 (notwithstanding E 500 billion + of asset purchases by the ECB this year)
  - In Japan: The third quarter looks set to contract after the second quarter contracted 1.2% (notwithstanding $665 billion of asset purchases by BOJ over the last year)
- Capital flight from emerging market economies will pose a major threat to global growth (between 2010 and 2015, China was responsible for 50% of global growth)
- There will also be renewed threats to capital adequacy of US/UK/European major banks.

These global downside pressures will inevitably dampen UK growth, employment and inflation.

A lone voice holding this view has been Andrew Haldane, Chief Economist at The Bank of England.

On 18th September, the day after the FOMC kept US interest rates on hold, he said “In my view the balance of risks to UK growth and to UK inflation at the two year horizon is skewed squarely and significantly to the downside ... there could be a need to loosen rather than tighten the monetary reins as a next step to support UK growth and return inflation to target.”*

Global economic backdrop to Q3 2015



Since 2009 we have been arguing that the threat of deflation will overhang the global economy for many years and that there was no prospect of interest rate rises for years to come. We have also argued for the last two years that further QE and/or monetary loosening in the UK was likely, when others have been predicting rate rises and higher inflation.

Continuing and stablising low borrowing rates will lead to a pick up in mortgage approvals and this will have greater effect on some parts of the UK housing market than others.

** Speech to Portadown Chamber of Commerce 18th September 2015*

Battersea key facts & figures

Here are the key facts and figures anyone investing in the property market needs at their fingertips.

Nominal Rental Income Growth to Dec 2014

	2014	5 years	10 years
1 Bed Flats	9%	32%	56%
2 Bed Flats	8%	31%	53%
3 Bed Houses	3%	22%	68%
4 Bed Houses	1%	13%	48%

Nominal Capital Returns to Dec 2014

	2014	5 years	10 years
1 Bed Flats	15%	52%	120%
2 Bed Flats	-2%	61%	114%
3 Bed Houses	-5%	83%	155%
4 Bed Houses	-6%	58%	152%

Other Assets Capital Returns to Dec 2014

	2014	5 years	10 years
Nationwide HPI*	7.20%	16%	24%
Halifax HPI*	7.80%	12%	16%
FTSE100	-2.70%	21%	36%
RPI	1.6%	18%	36%

**House Price Index*

Douglas &Gordon

Good to know.

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To get an investor’s view of other areas in central, west and south-west London, visit douglasandgordon.com

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