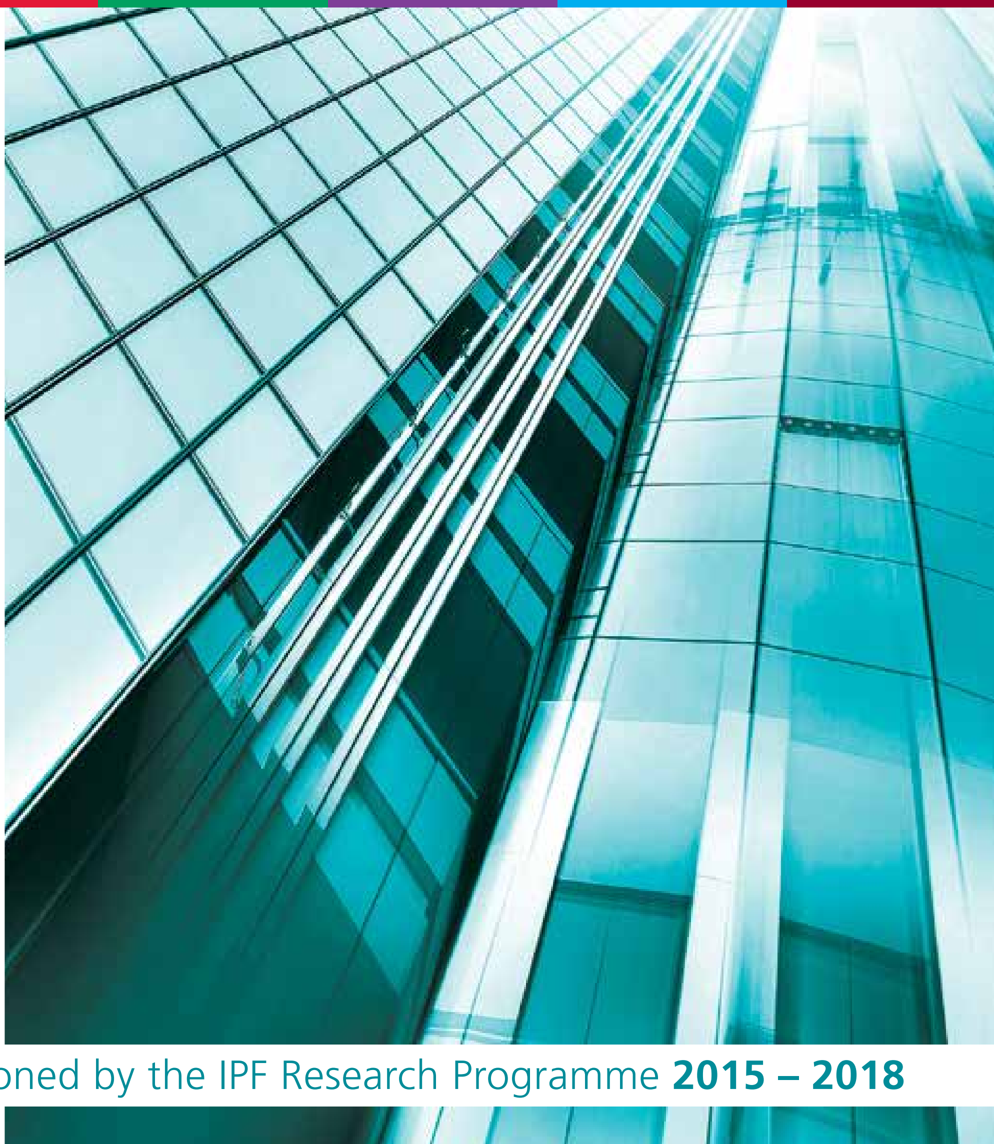
IPF Research

Investment Property Forum UK Consensus Forecasts

MAY 2016

SUMMARY REPORT



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This research was funded and commissioned through the IPF Research Programme 2015–2018.

This Programme supports the IPF's wider goals of enhancing the understanding and efficiency of property as an investment. The initiative provides the UK property investment market with the ability to deliver substantial, objective and high-quality analysis on a structured basis. It encourages the whole industry to engage with other financial markets, the wider business community and government on a range of complementary issues.

The Programme is funded by a cross-section of businesses, representing key market participants. The IPF gratefully acknowledges the support of these contributing organisations:

Survey of Independent Forecasts for UK Commercial Property Investment May 2016

Under the shadow of the forthcoming EU referendum in June, it is difficult to determine how much the slowdown in the property market is due to the uncertainty this has generated or whether this signals a cyclical correction or turning point. The second IPF survey of 2016 describes a pattern of declining growth and total returns for the majority of the forecast period, with only a modest recovery across all measures in 2020. The consensus for the 2016 All Property total return now stands at 7.1% (from 7.9% in February), primarily due to an 80 bps fall in the forecast of capital value growth (from 3.0% to 2.2% currently).

Compared to three months ago, sentiments for the different sectors vary in terms of the rate of slowdown in rental growth over 2016 and 2017, although the downward movement in capital growth rates in these two years has reduced slightly over the quarter. A general weakening in performance expectations is maintained until the final forecast year however. On an historic basis, property, by virtue of its income element, will remain competitive with equity and fixed income investment: one-year returns on equities and bonds to end-March 2016 being -5.8% and 3.8% against 11.1% for UK real estate, as reported by MSCI[1]. Average returns over 10 years, as at 31 December 2015, were 4.7%, 5.6% and 5.5% respectively.

With the outcome of the referendum on the UK's continued membership of the EU too difficult to call at this point, greater forecaster confidence may emerge following the 23 June vote. September's consensus report may therefore provide a better view of the market's prospects over both the short- and medium-term.

Key points

Near-term likely to deliver best performance over five years

- The **All Property rental growth** average forecast for 2016 has fallen by 8 bps over the last three months, to **3.1%**. Although the Industrial growth rate has improved marginally (to 3.7%), Offices are unchanged at 5.2%, whilst below average growth continues to dog retail markets.
- Average **capital growth** forecasts have declined across all sectors in the current year, as a consequence of which the **All Property** average has weakened to **2.2%** (from 3.0%) – falls of over 100 bps have been recorded in this quarter for Office, Shopping Centre and Retail Warehouse capital value growth rates.
- 2016 **total returns,** in turn, have deteriorated further, with the All Property average now 7.1% from 7.9% as reported in February.

Year-on-year declines should be arrested prior to the end of the survey period

- The pattern of average sector rental value growth forecasts shows a decline throughout the five years surveyed. The rates at which growth has weakened between sectors have fluctuated over the quarter, although the **five-year** annualised **All Property rental growth** rate of **2.1%** is unchanged from the February forecast.
- **Capital growth** rates are projected to weaken substantially in 2017, as a result of uncertainty over the UK's membership of the EU. The slowdown continues in later years, however, with the All Property average falling below zero in 2019 before a potentially flat year in 2020. Beyond the current year, the five-year **All Property** average of **0.6%** per annum appears vulnerable unless 2020 marks a turning point in the investment market.
- In parallel with capital growth prospects, **total return** forecasts weaken, from 5.7% in 2017 to 5.1% in 2020, (and potentially dipping below 5% in 2019). Supported by the 2016 forecast, the annualised five-year average for **All Property** remains **5.6%**. With the exception of the Office sector, all property types are projected to outperform the All Property average in each of the final three years of the survey period and on a five-year average basis also.

[1] MSCI/IPF UK Property Investment Seminar, Q1 2016, 4 May 2016

Economic background

The latest Office for National Statistics (ONS) release[2] recorded a preliminary estimate for gross domestic product (GDP) of 0.4% in the first quarter of 2016, compared to growth in the UK economy of 0.6% for the period between October and December 2015 (previously estimated to be 0.5%). Output increased in services by 0.6%, whilst the other main industrial groupings within the economy decreased: production falling by 0.4%, construction output by 0.9% and agriculture by 0.1%. Overall, GDP was 2.1% higher in Quarter 1 (January to March) 2016 compared with the same quarter a year ago.

In its March report[3], the Office for Budgetary Responsibility (OBR), noted that "economic developments have disappointed and the outlook for the economy and the public finances looks materially weaker" than a quarter earlier. A downward revision of productivity growth appears to have been the major contributor to a revision in the OBR's forecast of GDP growth over the remainder of the decade to around 2.1% per annum.

The ONS reported[4] that public sector net borrowing, excluding public sector banks, fell to £76 billion in the complete financial year ending March 2016 (or approximately 4% of GDP), a decreased of £15.7 billion on the previous financial year, although this represented a £2 billion increase to the initial estimate published in March. OBR estimates, based on current policy, the budget deficit should move into surplus by 2019-2020.

The Consumer Prices Index (CPI)[5] measure of inflation rose by 0.3% in the year to April 2016, down from 0.5% in the year to March, the main drivers being falls in air fares and prices for clothing, vehicles and social housing rent, partially countered by rises in motor fuel prices, some recreational goods and cultural services, as well as by static food prices (unchanged between March and April 2016 but having fallen in the same period a year earlier). The Bank of England's Monetary Policy Committee (MPC) voted unanimously at its May meeting to maintain both Bank Rate at 0.5% and the stock of purchased assets financed by the issuance of central bank reserves at £375 billion. The Bank's latest views on inflation[6] noted that CPI inflation increased to 0.5% per annum in March (but well below the target of 2%), due to "unusually large drags from energy and food prices" that should diminish over the next year.

Key statistics from the ONS May 2016 labour market release[7] include: 31.58 million people in work in the period January to March 2016 (44,000 more than for Q4 2015 and 409,000 more than for a year earlier), of whom, 23.12 million were working full-time and 8.46 million working part-time (328,000 and 81,000 more respectively than a year earlier). The employment rate was 74.2%, the highest since comparable records began in 1971, whilst 1.69 million, representing a rate of 5.1%, were unemployed (people not in work but seeking and available to work), 139,000 fewer than for a year earlier, when the unemployment rate was 5.6%. Average weekly earnings for employees in Great Britain increased by 2.0% including bonuses and by 2.1% excluding bonuses compared with a year earlier.

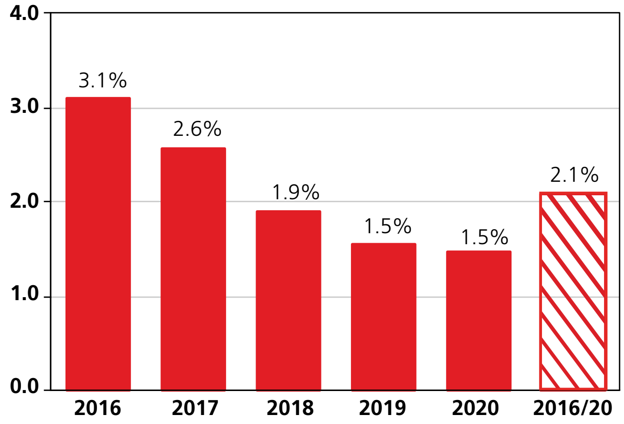
The ONS April 2016 retail sales release[8] estimated the volume of retail sales to have increased by 4.3% compared with April 2015, with an underlying 0.3% increase in the quarter-on-quarter movement in the quantity of goods bought whilst, compared with March, the amount purchased was estimated to have increased by 1.3%. An increase of 1.2% in the annual retail industry spend was reported, compared with April 2015, and a 1.0% increase compared with March 2016. Between April 2015 and April 2016, the value of online sales rose by 9.3% and by 1.7% between March and April 2016.

[2] ONS: Gross Domestic Product:, Q1 2016 Preliminary Release, 22 April 2016
[3] OBR Economic and Fiscal Outlook, March 2016
[4] ONS: Public sector finances: April 2016, 24 May 2016
[5] ONS: Consumer Price Inflation, April 2016, 17 May 2016
[6] Bank of England Monetary Policy Summary and minutes of the Monetary Policy Committee meeting ending on 11 May 2016, 12 May 2016
[7] ONS: UK Labour Market, May 2016 Release, 18 May 2016
[8] ONS: Retail Sales, April 2016 Release, 19 May 2016

All Property rental value growth forecasts

Since February, rental growth expectations for All Property have fallen marginally (by between 7 and 11 bps) for each of the first four years of the survey period but individual contributors demonstrate a range of opinion in their forecasts. This spread has increased in the current year (to 2.6% from 2.4%) whilst closing slightly in 2019 and 2020 as well as for the five-year average.

Despite the weakening in the rate of growth, the five-year average is virtually unchanged from three months ago (having reduced by 3 bps to the current 2.10%).



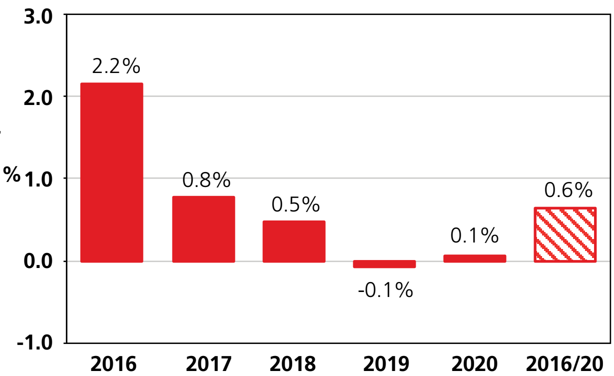
N.B. 2019 and 2020 averages differ by 6 bps but data labels are rounded to one decimal place.

All Property average capital value growth forecasts

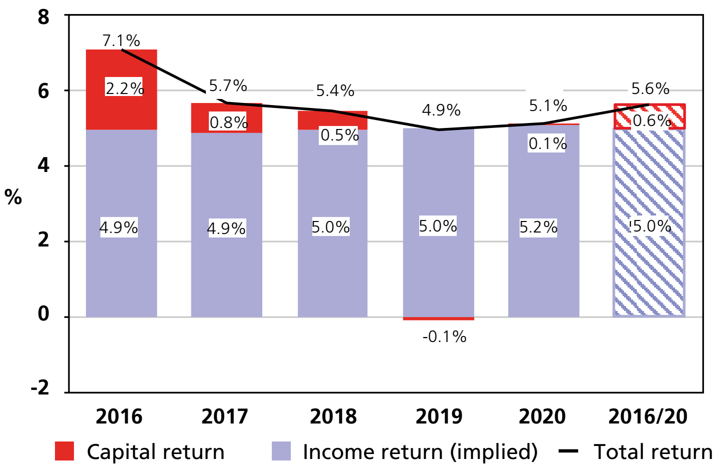
The average All Property capital value growth forecast for 2016 has fallen in the last three months from just below 3.0% to 2.2%, representing a further decline of 80 bps over the 100 bps fall recorded three months ago.

However, views on growth in 2017 and 2018 have improved slightly, rising from 0.5% and 0.2% respectively in February. 2019 potentially marks the nadir, although a return to positive growth in 2020 is uncertain with just over half of contributors projecting sub-zero rates for the final year of the survey period, as forecasts range from -1.6% to 2.8%.

With a weaker 2016 forecast, the five-year average has declined by 0.1% from February's projection.



All Property total return forecasts



The decline in the 2016 All Property total return forecast has continued, from an average of 7.9% in February as further weakening of capital value growth (from 3.0% previously) continues to affect this performance measure.

However, a slight recovery in the 2018 and 2019 forecasts (from 0.5% and 0.2% respectively three months ago) impacts the headline total return in each year.

The five-year average return remains broadly stable due to rounding, at just over 5.6% as the later improvements counter the lower near-term capital growth expectations.

All Property survey results by contributor type

(Forecasts in brackets are February 2016 comparisons)

Property Advisors and Research Consultancies

10 (10) contributors	Rental value growth (%)						Capital value growth (%)						Total return (%)					
	2016		2017		2016/20		2016		2017		2016/20		2016		2017		2016/20	
Maximum	3.9	(3.9)	3.7	(3.5)	3.3	(2.7)	4.7	(5.1)	4.4	(4.7)	2.8	(2.7)	9.5	(10.1)	9.5	(9.8)	7.6	(7.7)
Minimum	1.8	(2.6)	1.5	(1.4)	1.2	(1.3)	0.3	(2.1)	-7.6	(-7.5)	-0.8	(-0.6)	5.7	(7.1)	-2.2	(-2.7)	3.9	(4.7)
Range	2.1	(1.3)	2.2	(2.1)	2.1	(1.4)	4.3	(3.1)	12.0	(12.2)	3.6	(3.4)	3.8	(3.0)	11.7	(12.5)	3.7	(3.0)
Median	3.4	(3.4)	2.7	(2.7)	2.1	(2.1)	2.6	(4.1)	0.7	(0.7)	1.3	(1.4)	7.3	(8.9)	5.4	(5.4)	6.2	(6.4)
Mean	**3.3**	**(3.4)**	**2.6**	**(2.6)**	**2.2**	**(2.1)**	**2.7**	**(3.8)**	**0.3**	**(0.3)**	**1.0**	**(1.4)**	**7.6**	**(8.7)**	**5.2**	**(5.1)**	**6.0**	**(6.2)**

Fund Managers*

17 (14) contributors	Rental value growth (%)						Capital value growth (%)						Total return (%)					
	2016		2017		2016/20		2016		2017		2016/20		2016		2017		2016/20	
Maximum	4.4	(4.3)	4.0	(4.0)	3.0	(3.6)	5.2	(5.5)	5.3	(5.3)	2.2	(2.6)	10.1	(10.1)	10.4	(10.4)	8.0	(8.6)
Minimum	2.0	(1.9)	1.0	(1.0)	1.1	(1.0)	0.0	(-1.9)	-1.5	(-5.6)	-1.6	(-1.0)	5.0	(2.6)	3.1	(-0.9)	3.3	(3.6)
Range	2.4	(2.4)	3.0	(3.0)	1.9	(2.6)	5.2	(7.4)	6.8	(10.9)	3.8	(3.6)	5.1	(7.6)	7.3	(11.3)	4.7	(5.0)
Median	2.8	(3.0)	2.5	(2.8)	2.1	(2.4)	1.9	(2.3)	0.4	(0.9)	0.2	(0.3)	6.7	(7.0)	5.3	(5.4)	5.3	(5.0)
Mean	**3.0**	**(3.0)**	**2.6**	**(2.6)**	**2.1**	**(2.2)**	**1.9**	**(2.3)**	**1.1**	**(0.6)**	**0.4**	**(0.2)**	**6.8**	**(7.3)**	**6.0**	**(5.6)**	**5.4**	**(5.3)**

All Forecasters**

28 (24) contributors	Rental value growth (%)						Capital value growth (%)						Total return (%)					
	2016		2017		2016/20		2016		2017		2016/20		2016		2017		2016/20	
Maximum	4.4	(4.3)	4.0	(4.0)	3.3	(3.6)	5.2	(5.5)	5.3	(5.3)	2.8	(2.7)	10.1	(10.1)	10.4	(10.4)	8.0	(8.6)
Minimum	1.8	(1.9)	1.0	(1.0)	1.1	(1.0)	0.0	(-1.9)	-7.6	(-7.5)	-1.6	(-1.0)	5.0	(2.6)	-2.2	(-2.7)	3.3	(3.6)
Range	2.6	(2.4)	3.0	(3.0)	2.2	(2.6)	5.2	(7.4)	12.9	(12.7)	4.4	(3.7)	5.1	(7.6)	12.6	(13.1)	4.7	(5.0)
Std. Dev.	0.6	(0.6)	0.7	(0.7)	0.5	(0.6)	1.3	(1.7)	2.4	(2.7)	1.1	(1.1)	1.3	(1.8)	2.4	(2.9)	1.2	(1.2)
Median	3.1	(3.2)	2.6	(2.7)	2.1	(2.1)	2.3	(3.0)	0.4	(0.7)	0.9	(0.5)	7.0	(8.5)	5.2	(5.4)	5.8	(5.5)
Mean	**3.1**	**(3.2)**	**2.6**	**(2.6)**	**2.1**	**(2.1)**	**2.2**	**(3.0)**	**0.8**	**(0.5)**	**0.6**	**(0.7)**	**7.1**	**(7.9)**	**5.7**	**(5.4)**	**5.6**	**(5.6)**

*Includes one Fund Manager who provided rental growth forecasts only at the All Property and each sector level (including central London offices).
**Includes one Equity Broker.

Notes:

1. Figures are subject to rounding and are forecasts of All Property or relevant segment Annual Index measures published by the Investment Property Databank (IPD). These measures relate to standing investments only, meaning that the effects of transaction activity, developments and certain active management initiatives are specifically excluded.
2. To qualify, all forecasts were produced no more than 12 weeks prior to the survey date.
3. Maximum: The strongest growth or return forecast in the survey under each heading.
4. Minimum: The weakest growth or return forecast in the survey under each heading.
5. Range: The difference between the maximum and minimum figures in the survey.
6. Median: The middle forecast when all observations are ranked in order. The average of the middle two forecasts is taken where there is an even number of observations.
7. Mean: The arithmetic mean of all forecasts in the survey under each heading. All views carry equal weight.
8. Standard deviation: A statistical measure of the spread of forecasts around the mean. Calculated at the 'All forecaster' level only.
9. The sector figures are not analysed by contributor type; all figures are shown at the 'All forecaster' level.
10. In the charts and tables, 'All Property' figures were contributed by 28 participants for each performance measure (other than one Fund Manager who provided rental growth forecasts only). Full sector forecasts were received from reduced samples of 23/21 contributors.

Acknowledgements

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Property advisors (including research consultancies): Bilfinger GVA, BNP Paribas Real Estate, Capital Economics, CBRE, Colliers International, Cushman & Wakefield, Fletcher King, JLL, Real Estate Forecasting Limited, The Lazarus Partnership.

Fund managers: Aberdeen Asset Management, Aviva Investors, AXA IM Real Assets, BMO Real Estate Partners, CBRE Global Investors, Cornerstone Real Estate Advisers, Deutsche Asset Management, HSBC Global Asset Management, Kames Capital, Keills, Knight Frank Investment Management, LaSalle Investment Management, Legal & General Property, M&G Real Estate, Savills Investment Management, Standard Life Investment, TH Real Estate.

Note
Consensus forecasts further the objective of the IPF to enhance the efficiency of the real estate investment market. The IPF is extremely grateful for the continuing support of the contributors as noted above. This publication is only possible thanks to the provision of these individual forecasts.

If your organisation wishes to contribute to future surveys, please contact the IPF Research Director at pcraddock@ipf.org.uk.

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