IPF Investment Property Forum

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INVESTMENT PROPERTY FOCUS

In this issue:

The IPF has moved to New Broad Street House, 35 New Broad Street, London EC2M 1NH.

From the editor

This edition of **Investment Property Focus** reports on the progress of two key developments in the investment market, namely REITS and a property derivatives market, and considers where the market itself is heading over the next five or so years. This always assumes that property market forecasts are accurate! – a supposition considered by the research team commissioned by the IPF to look at the reliability of property forecasts. As Patrick McAllister of University of Reading explains, although there was a high level of agreement in the property forecasts analysed, the consensus forecast often contains high levels of uncertainty.

The IPF Consensus Forecast for February 2006 found that forecasters expect the yield falls seen throughout 2005 to continue and consolidate in 2006 but there is a significant divergence amongst forecasters as to the prospect for yields in 2007 and 2008, with a minority expecting yields to increase in 2008.

Sabina Kalyan of Capital Economics also suggests that yields are likely to move up in 2007 to 09, resulting in what she describes as, "a rather 'boring' period" where property produces real annual returns of around 5% through income rather than capital growth – poor compared with recent double-digit returns but in line with the 50-year average.

Charles Follows, the IPF Director of Research, outlines the findings of another other research project commissioned by the IPF, which seeks to determine why private sector sources of finance appear to shy away from regeneration projects. The research suggests that an appropriately structured regeneration investment vehicle may offer one solution.

If income is to be the key driver of investment performance over the next few years, the IPF November 2005 seminar on prospects for the retailing provided much for property investors to contemplate. Speakers Richard Boys-Stones of PricewaterhouseCoopers and Mark Teale of CB Richard Ellis highlighted the competitive pressures on high street retailers from the supermarket chains and, to a limited extent, the Internet. Mark Chivers of Boots Properties considered the benefits to retailers of restructuring their property holdings, given the current strong demand from property investors for product.

In the extensive interview with Jamie Ritblat of Delancy, he explains the Ritblat philosophy of buying quality assets with good underlying fundamentals. He believes the weight of money coming into the market has driven down secondary yields without true consideration to the underlying asset. Consequently when a correction occurs, secondary property is likely to suffer most. He is unlikely to turn Delancy into a REIT, although he considers REITs to be good for the market generally.

John Gellatly, of Merrill Lynch Investment Managers presents excellent news from the budget announcement in March on UK REIT legislation. John goes through the details of what the announcement means and where negotiations go from here.

In the October 2005 edition, Ian Reid, Chairman of the IPF's Property Derivatives Interest Group, outlined the need for a property derivatives market. Here, Rupert Clarke of Hermes explains the role of the Property Derivatives Trading Forum (PDTP). Set up by Hermes in September 2005, the PDTF already has nearly 60 participants and the first two trading days saw around £16bn of simulated trades completed.

IPF news and an update on the IPF research programme are included in the note of the Forum's activities at the back. If you are interested in contributing material to a forthcoming edition of **Investment Property Focus**, please contact Sabrina Wisner on swisner@ipf.org.uk – new ideas are always welcome.

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UK REITs – the long and winding road

STOP PRESS: At last!

Alongside this year's Budget, the government announced that it is bringing forward legislation to establish UK Real Estate Investment Trusts (UK REITs) in the 2006 Finance Bill with the objective of "improving access to UK commercial and residential property investment through more efficient and liquid markets" and enabling their launch from 1 January 2007.

Publication of this legislation is the culmination of several years work by government and the pan-industry working group (comprising the Investment Property Forum, British Property Federation and RICS) ever since the concept of the introduction of UK REITs was first alluded to in Gordon Brown's Budget Statement of April 2003. Since then, the industry worked with government through a series of consultation processes towards this end – the most recent of which was the publication of the draft legislation just prior to Christmas 2005.

These initial legislative proposals attracted considerable adverse comment with many believing that the proposed conditions – especially those pertaining to the income cover ratio test and shareholding restrictions – were too restrictive. In such an event, it was feared that the vehicle would be unworkable from a commercial perspective thereby ensuring that few, if any, property companies would seek to secure REIT status.

However, these proposals were draft in nature and the government was consistently accepting of the industry's arguments so long as they were backed by solid, well researched evidence and analysis. Indeed, it is this aspect of the industry's approach, led by the IPF research effort, which has been integral to the eventual successful announcement.

As a result, the subsequent conversations with government have been positive and constructive and have resulted in the publication of legislative proposals that took into account many of the industry's concerns and included a number of key changes that are a direct result of consultation with the pan-industry group. Specifically, these include:

- *A reduction of the income cover test to 1.25x on a pre-capital allowances basis (previously set at 2.50x on a post capital allowance basis). The implication of this change is that the implied gearing for UK REITs, which under the original proposals would have been restricted to a maximum of circa 35% on a loan-to-value basis, can now rise to just over 60%. It is unlikely that UK REITs will fully avail themselves of this scope (UK listed stocks are already more lowly geared) but it does provide a more feasible test in the context of the UK financing environment where the margin between financing rates and property yields is narrower than in any other market around the world. UK REITs can therefore now manage their affairs with a more appropriate level of gearing but without running the risk of breaching the test and thus compromising their REIT status.*
- *A reduction of the required distribution rate to 90% of net taxable profits from a provisional level of 95%. Such a high payout ratio will ensure that UKREITs distribute the vast majority of their underlying portfolio's cashflow – being the ultimate source of the asset class' long term, stable returns and the attraction to investors – while providing sufficient margin to ensure effective active management of the properties.*
- *The introduction of flexibility to allow industry to operate more easily within the 9.9% maximum shareholding restriction. This percentage level is a function of various tax treaties and, quite understandably, the government are keen to protect any potential loss of tax flowing from holdings beyond this level who might, under the various Double Tax Agreements, have a claim against HM Treasury for a reclamation of some (or all) of the withholding tax applied to UK REIT dividends. The government readily acknowledges the problems associated with this issue (for example ownerships already beyond this level, the efficient yet standard working of the corporate sector for M&A and rights issues) and will bring forward a series of "market solutions" as part of the guidance notes being developed in the coming months.*

John Gellatly, Merrill Lynch Investment Managers and IPF REITs spokesman

The one area where there was no dialogue, but which the industry knew was coming, related to the scale and basis of the conversion charge that would be levied on companies in exchange for their converting to tax transparent REITs. In the event, the conversion charge was set at 2% of the gross market value of the investment properties, payable either in whole at the outset or with the option to spread this payment over four years but at the slightly higher overall cost of 2.15% of value.

This proposal was met with much general approval as it provides a sensible, clear approach to the issue. Furthermore, it also appears relatively favorable to the industry as compared to the other possible approach of charging 50% of the embedded CGT liability (as was applied by the French government on the introduction of the SIIC regime in 2003) which analysts believe could have equated to as much as 3% of GAV.

Indeed, the whole body of the proposal met with wide ranging approval as evidenced by the fact that:

- *UK listed real estate sector share prices overall rose by 8.3% on Budget day, adding £3.4 billion to the sectors' market capitalisation;*
- *Land Securities, one of the stocks most widely tipped to convert, underwent its largest price rise in a single day for 18 years; and*
- *In the days immediately following the announcement a number of corporates with large property portfolios (e.g. Tesco) commented that they would consider spinning off their properties into specialist REITs.*

So what next? The dialogue between the pan-industry group and the government does not stop here by any means:

- *Firstly, the industry is fully engaged as the legislation passes through the Committee Stages towards gaining Royal Assent at the end of the Summer and also as the primary legislation is fleshed out with technical tax guidance notes in the coming months.*
- *Secondly, even then debate and revision of the legislation continues. The US REIT legislation has evolved for over 45 years while the French are already into the third revision of their SIIC rules. Inevitably, as the new rules are applied and as the market evolves the initial legislation will require change and amendment.*
- *Finally, with UK REITs now a reality (or at least well on course to become so) the industry needs more co-ordination in how it promotes these structures to the wider retail investor base and educates investors generally about the merits of such structures in the context of overall real estate allocations.*

Property derivatives take off – virtually

Rupert Clarke, Hermes Property Asset Management Ltd

In September 2005, Hermes announced the setting up of the Property Derivatives Trading Forum (PDTF). Since then the PDTF met twice, holding two 'trading days' and has two more planned.

Behind the scenes, the Investment Property Forum has liaised closely with Hermes on the development of the PDTF and was very pleased to see its success – not least because Hermes has pledged all the proceeds from the PDTF, expected to be over £100,000 (but somewhat less after tax), to the Investment Property Forum. With a watchful eye on this new source of income, Executive Director of the Investment Property Forum, Amanda Keane, met up with Rupert Clarke, Chief Executive of Hermes Real Estate to find out more about the PDTF.

Amanda Keane (AK): "Tell me, what exactly is the Property Derivatives Trading Forum?"

Rupert Clarke (RC): "The Property Derivatives Trading Forum is an opportunity for all those principals interested in the potential of property derivatives to explore how the market might work in practice by trading on a virtual basis. Hermes approached all the major potential market players and invited them to participate in the PDTF as principals. The result was that we now have 59 participants – 19 institutions, 12 investment managers, seven property companies, 16 investment banks and five derivatives specialists."

AK: "So, how does it work?"

RC: "The PDTF consists of four separate trading days spanning October 2005 to May 2006. On each of these days, the principals trade property swaps covering All Property and the seven main sub-sectors; City Offices, West End Offices, Regional Offices, Industrial and Distribution, Shopping Centres, Retail Warehouses and Retail Units. Contract terms are three year swaps against LIBOR, for sub sectors against All Property."

AK: "How does this compare with the real market?"

RC: "A key objective of the Trading Forum is to ensure that it operates in as similar a way to how the real market might operate once it is more established. Accordingly, each participant has been given a 'strategic' trading limit, depending on the size of their direct portfolio, to reflect a reasonable estimate of the likely level of trades they might commit to in the real market. In addition, all participants have a trading account which has a much lower limit. So, no one participant is able to unduly influence pricing or trading volume in a way that would give an unrealistic impression of the market consensus."

AK: "How does the trading actually operate?"

RC: "On each trading day there are two trading sessions where principals make bids for the contracts that are on offer declaring whether they are a buyer or a seller and at what price they are prepared to trade. The trading itself is managed by derivative specialists ICAP and GFI, with IPD acting as an independent monitor of proceedings. ICAP and GFI select the strike price by taking an average between the price where buyers and sellers overlap, also taking into account the unmatched buyers and sellers, who reflect wider market sentiment. No trade is executed unless there is sufficient interest from another principal in the room to take the counterparty position."

AK: "So, what are the results so far?"

RC: "When we went into the first trading day we thought that principals might be keen to sell retail and, similarly, keen to buy commercial and that very few would be prepared to take the counter positions. The actual outcome was remarkable and very reassuring for the future potential of property derivatives. On the first trading day some £8bn of trades were completed and on the second day a similar volume was transacted. For these transactions to have taken place there had to be sufficient principals in the room taking equal and opposite positions – if they hadn't the trades could not have been completed."

AK: "What about pricing?"

RC: "The All Property derivative originally opened at 180bp which was about 30bp higher than the last reported trade in the real market and, after an extraordinary blip at the beginning of the second trading day, it has moved up to a mid pricing of 270bp over LIBOR which is also now the kind of price being quoted in the real market. Much of the discussion in the room on the first trading day was on low pricing of the All Property derivative and, although one cannot be entirely sure, we would not be surprised if the sentiment on pricing being reflected in the PDTF has now found its way into the pricing of the real market. Separately the sub sectors have gravitated as expected with the best performer being City Offices trading at All Property +220bp and the worst being Shopping Centres trading at All Property -160bp"

AK: "Why did you move from trading the sub sectors against LIBOR to against All Property?"

RC: "The first day trading reflected an approach which the investment banks were comfortable with since many other derivatives use LIBOR as the central reference point. However, it became clear that many institutions and property companies preferred to trade one sub sector against another i.e. buy West End Offices, sell Retail Units. In practice, it would be very difficult to achieve a liquid market in all the potential sub sector swaps because even if one fixed the maturity at a single point, the various combinations of sub sector swaps would result in 42 different contracts which would significantly decrease the chances of matching counterparties. Also investors are still struggling with the pricing of derivatives and how one factors in the arbitrage of a derivative versus the direct market or cash with regard to trading costs, valuation differences, performance of LIBOR etc. By trading the sub sectors against All Property,

Figure 1: Trading day results

	6th October trading day			23rd November trading day		
	Open (bp)	Close (bp)	Volume £m	Open (bp)	Close (bp)	Volume £m
All Property	Libor +180	Libor +220	£2,250m	Libor + 400	Libor + 270	£1,610m
Retail Units	Libor +40	Libor +20	£210m	All Property -150	All Property – 100	£540m
Shopping Centres	Libor +80	Libor +50	£870m	All Property -160	All Property – 160	£1,290m
Retail Warehouses	Libor +230	Libor +250	£900m	All Property +120	All Property +120	£710m
City Offices	Libor +450	Libor +450	£1,170m	All Property +230	All Property +220	£800m
West End Offices	Libor +350	Libor +400	£1,250m	All Property +270	All Property +200	£820m
Rest UK Offices	Libor +220	Libor +250	£410m	All Property +80	All Property +80	£480m
Industrial	Libor +210	Libor +210	£860m	All Property +0	All Property +20	£850m
		Total	**£7,920m**		**Total**	**£7,100m**

these pricing differentials evaporate and one is left with a simple projection of the relative performance of a specific sub sector against All Property – a calculation which all professional investors in real estate are considering all the time."

AK: "You have obviously been interested in property derivatives for some time. What have you learnt out of the experience of the PDTF?"

RC: "The PDTF is fascinating. The most exciting outcome has been the capacity for the market to trade amongst itself with no artificial stimulants which confirms to me that there is a very high probability that the property derivatives market will take off. Set against that finding is the realisation that of the 19 institutions in the room, only four of them had sufficient approvals and back office systems to actually go out and execute trades. So while the capacity is there for the market to develop, the reality is that unless the institutions get their act together, the development of the market could be very slow indeed."

AK: "Is there anything that can be done about 'readiness to trade' and what is the Hermes position?"

RC: "In order to accelerate the process and help participants through the back office maze, we worked with Phil Nicklin at Deloitte who put together a half-day workshop for the back office teams of the institutions to run through the practical issues involved in trading derivatives for real, and of course, there is the IPF one-day workshop in July which explores this area. For more information, refer to the IPF website. Hermes itself is currently in the process of obtaining approval from Trustees to trade derivatives for real. Assuming we receive their support, we would hope to be in a position to trade in the second quarter of 2006."

AK: "What do you believe is the most significant contribution that the PDTF may have made to the successful development of this market?"

RC: "There are a number of areas where the PDTF has undoubtedly added value. The least obvious but probably the most essential was to get all the key players to designate a team within their organisation to be responsible for the area – an essential first step to trading for real. After that most of what the PDTF has achieved is to reassure the principals involved that trading in derivatives was not too daunting and to grow their confidence levels to a point where they felt they could trade for real. In addition, for the wider market, the proof that there were sufficient parties prepared to take equal and opposite positions has dispelled the myth that investor behaviour was sufficiently herd-like to ensure that no trades would actually take place."

AK: "It all sounds very good for the market as a whole and for the participants, but how has Hermes benefited from its involvement and what triggered you to take on this challenge in the first place?"

RC: "I was convinced that while the majority of investors were interested in property derivatives, they would not actually trade until they had confidence in their own abilities and in the market. As a solution to this problem, I and my colleagues at Hermes conceived the PDTF. As to what have been the benefits to Hermes, clearly we now have a thorough understanding of the workings of the property derivatives market and have worked closely with derivative specialists, GFI and ICAP in formulating a credible market environment and trading platform. I would like to think that Hermes has always been prepared to take a leading position on market innovations in the past and the PDTF together with other initiatives in which Hermes have been involved, carries on that tradition."

AK: "Well, it's been absolutely fascinating to see the trading forum's progress so far. What have you got planned for the next trading sessions?"

RC: "Having traded three year All Property and sub sectors we are now introducing the concept of 'trading the curve' – that is not just trading three year contracts but one year, two year, five year and 10 year contracts. To simplify this process, we are only doing this at the All Property level otherwise we believe there would be significant dilution of liquidity. In addition, and in order to broaden the exposure of property derivatives, we have also invited the central asset allocators of the institutions who are participating in the trading forum to come and trade the All Property derivative to explore its potential use as a means of maintaining the appropriate portfolio mix at the central portfolio level. We believe that central asset allocators will be particularly interested in All Property derivatives against LIBOR and will be fascinated to see what impact they might have on the market. It is too early to say how many central asset allocators we can entice out of their natural habitat to come and join us. However, after initial marketing, five leading institutions have already signed up."

IPF Consensus Forecasts February 2006

Introduction

With an average total return forecast of 11.2% for 2006, up from the 8.6% reported in the November 2005 survey, it seems forecasters are expecting the yield falls seen throughout 2005 to continue and consolidate. The average forecast for 2007 is marginally up at 7.1% from the previous figure of 6.9%. For 2008, the consensus outlook is weaker with a total return of 6.2%. Over the five years of 2006 to 2010 the consensus is for a return of 7.7%, implying returns of about 7% in both 2009 and 2010. Thus, the outlook is for a further five years of real property returns.

We noted last time the divergence in views about the yield outlook for 2007 and 2008. This divergence is more evident in this survey, illustrated by the views on capital values shown in the scatter charts in the full report available on the IPF website. The capital value forecasts show that nine forecasters (25% of the sample) expect capital values to fall in 2008. A further 12 expect capital value growth of less than 1% in 2008. Given the rental value growth forecasts, the implication is that a large minority of forecasters expect yields to move up in 2008. For investors, capital value shifts only one component of total return. For the banks with lending secured against capital value, these yield shifts may be more of a concern.

Key points

Total return forecast for 2006 increased, with an outlook of real property returns for the next five years.

- Total return in 2006 forecasted at 11.2%, up from 8.6% since the last survey.
- The average total return forecast is 7.7% pa for the next five years.
- Average all property rental value growth is 2.8% pa for 2006 to 2010 (inclusive).
- Clear evidence that a minority of forecasters expect property yields to increase during 2008, with some expecting the yield increases to start in 2007.
- A significant minority of forecasters expect capital values to be under threat in 2008.
- A recovery in the London office market is widely forecasted, with rental value growth of over 6% pa in West End offices and City offices for the next five years.
- For 2006, retail warehouses are forecasted to show inflation beating rental value growth of 3.7%, matched only by the office sector on the back of strong rental value growth in central London.
- Retail warehouses rental value growth are maintained in 2007 and 2008.
- Some forecasters are bearish about the prospects in 2007 and 2008 for standard shops, shopping centres and industrial with some forecasting falls in rental values.
- Between 2006 and 2010 (inclusive), offices are forecasted to show strongest rental value growth at 4.6% pa, followed by retail warehouses at 3.7% pa. Standard shops, shopping centres and industrial continue to offer lower than inflation matching rental value growth on the five-year view.

Recovery in office returns to continue

- Sector total return forecasts place offices, driven by strong central London performance, as the top performer in 2006 giving 13.4% closely followed by retail warehouses at 11.7%. One forecaster believes that City offices will star in 2006, with returns of 27.7%, built off rising rents and falling yields.
- All sectors show lower returns in 2007 and 2008, with offices giving best returns. On the five-year view, offices are the best performing sector at an average total return of 9.3% pa.
- West End (10.3% pa) and City offices (10.6% pa) are expected to outperform all five of the main sectors on the five-year view. The City performance over the same period is forecasted to be ahead of the West End.
- The weakest sectors are likely to be standard shops and shopping centres, reflecting concerns about the strength of consumer expenditure. However, all sectors will give real returns for 2006 to 2010.

Rising yields in 2007 and 2008?

- Significant minority of forecasts imply that yields will rise in 2007 and 2008.
- The capital value forecasts show that nine forecasters (25% of the sample) expect capital values to fall in 2008. A further 12 expect capital value growth of less than 1% in 2008. Given the rental value growth forecasts, the implication is that a minority of forecasters expect yields to move up in 2008.
- One forecaster believes that the three retail market segments will give negative total returns in 2008.
- The diversity of views should add further impetus to the use of sector property derivative contracts for tactical asset shifts.

All property rental value growth forecasts

The average forecast is for 2.5% rental value growth in 2006, a slight increase on the November forecast of 2.4%.

Thereafter, the consensus is unchanged with rental value growth of 2.7% in 2007. The first figures for 2008 show a slight pick up in rental value growth to 3.0%. The annual average for the five years 2006 to 10 is 2.8% pa. Thus, the consensus outlook is for marginal real rental value growth for five years, when set against an inflation expectation of 2.5% pa.

Figure 1: Average rental growth

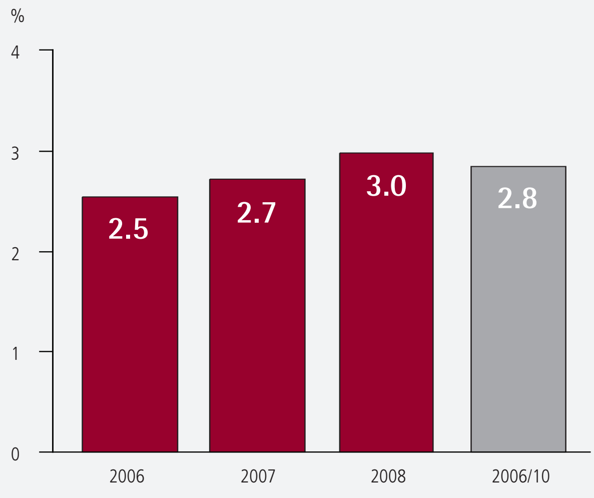
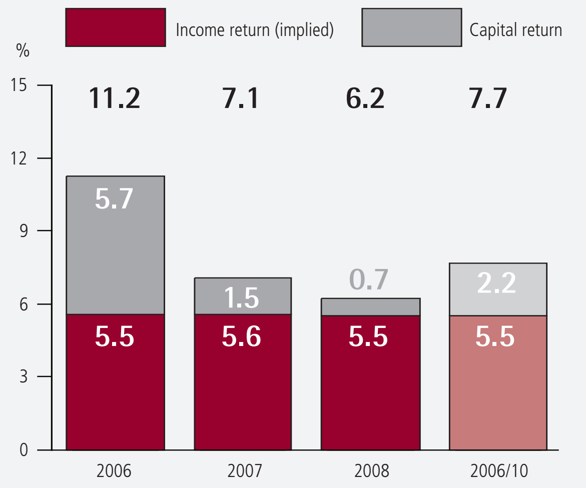


Figure 2: Average total returns



All Property total return forecasts

After the excellent performance in the last two years, the consensus still points to double-digit returns for 2006 at 11.2%.

Thereafter forecasters are looking for a slow down for 2007 and 2008, with just 7.1% and 6.2 % total returns in those two years respectively. Capital growth is expected to virtually disappear in 2008.

All Property survey results by contributor type
(Forecasts in brackets are November 2005 comparisons)

Figure 3: Property advisors and research consultancies (16 contributors)

	Rental value growth %						Capital value growth %						Total return %					
	2006		2007		2008		2006		2007		2008		2006		2007		2008	
Maximum	3.6	(3.7)	4.0	(3.7)	5.0	n/a	13.0	(7.2)	3.8	(2.9)	3.0	n/a	16.0	(12.7)	9.0	(8.9)	8.4	n/a
Minimum	2.1	(2.1)	1.9	(2.5)	2.0	n/a	2.7	(1.2)	-0.1	(-0.3)	-1.9	n/a	8.4	(6.6)	4.8	(5.2)	3.6	n/a
Range	1.5	(1.6)	2.1	(1.2)	3.0	n/a	10.3	(6.0)	3.9	(3.2)	4.9	n/a	7.6	(6.1)	4.2	(3.7)	4.8	n/a
Median	2.6	(2.6)	2.8	(2.8)	3.2	n/a	5.5	(1.8)	1.7	(1.3)	1.6	n/a	11.0	(8.0)	7.1	(7.7)	7.0	n/a
Average	**2.7**	**(2.6)**	**2.9**	**(3.0)**	**3.2**	**n/a**	**6.0**	**(2.5)**	**1.7**	**(1.5)**	**1.3**	**n/a**	**11.3**	**(8.3)**	**7.1**	**(7.4)**	**6.7**	**n/a**

Figure 4: Fund managers (16 contributors)

	Rental value growth %						Capital value growth %						Total return %					
	2006		2007		2008		2006		2007		2008		2006		2007		2008	
Maximum	3.1	(2.9)	3.4	(3.5)	4.4	n/a	9.4	(6.5)	5.1	(4.3)	3.9	n/a	15.1	(12.3)	10.1	(10.0)	8.7	n/a
Minimum	1.4	(0.6)	1.5	(1.4)	1.8	n/a	1.0	(-1.0)	-3.0	(-2.1)	-7.0	n/a	7.0	(5.0)	3.0	(3.6)	-1.0	n/a
Range	1.7	(2.3)	1.9	(2.1)	2.6	n/a	8.4	(7.5)	8.1	(6.4)	10.9	n/a	8.1	(7.3)	7.1	(6.4)	9.7	n/a
Median	2.4	(2.2)	2.7	(2.3)	2.7	n/a	5.2	(2.8)	1.1	(0.1)	0.0	n/a	10.6	(8.9)	6.5	(6.0)	5.4	n/a
Average	**2.3**	**(2.1)**	**2.5**	**(2.3)**	**2.6**	**n/a**	**5.4**	**(2.9)**	**0.9**	**(0.4)**	**-0.2**	**n/a**	**10.9**	**(8.8)**	**6.4**	**(6.3)**	**5.2**	**n/a**

Figure 5: Equity brokers (5 contributors)	Rental value growth %						Capital value growth %						Total return %					
	2006		2007		2008		2006		2007		2008		2006		2007		2008	
Maximum	3.7	(3.2)	3.9	(3.7)	4.8	n/a	9.0	(4.0)	5.0	(3.1)	3.8	n/a	17.0	(10.0)	14.0	(8.5)	10.0	n/a
Minimum	1.8	(1.9)	2.0	(2.9)	2.0	n/a	2.2	(1.8)	1.6	(1.4)	0.0	n/a	7.8	(7.5)	7.1	(6.9)	5.0	n/a
Range	1.9	(1.3)	1.9	(0.8)	2.8	n/a	6.8	(2.2)	3.4	(1.7)	3.8	n/a	9.2	(2.5)	6.9	(1.6)	5.0	n/a
Median	2.8	(3.0)	3.0	(3.0)	3.0	n/a	6.8	(3.5)	2.0	(2.3)	2.3	n/a	12.8	(9.2)	8.0	(8.3)	8.0	n/a
Average	**2.7**	**(2.8)**	**2.9**	**(3.2)**	**3.3**	**n/a**	**5.9**	**(3.2)**	**2.9**	**(2.3)**	**2.2**	**n/a**	**12.1**	**(9.0)**	**9.2**	**(8.0)**	**8.0**	**n/a**

Figure 6: All forecasters (37 Contributors)	Rental value growth %						Capital value growth %						Total return %					
	2006		2007		2008		2006		2007		2008		2006		2007		2008	
Maximum	3.7	(3.7)	4.0	(3.7)	5.0	n/a	13.0	(7.2)	5.1	(4.3)	3.9	n/a	17.0	(12.7)	14.0	(10.0)	10.0	n/a
Minimum	1.4	(0.6)	1.5	(1.4)	1.8	n/a	1.0	(-1.0)	-3.0	(-2.1)	-7.0	n/a	7.0	(5.0)	3.0	(3.6)	-1.0	n/a
Range	2.3	(3.1)	2.5	(2.3)	3.2	n/a	12.0	(8.2)	8.1	(6.4)	10.9	n/a	10.0	(7.7)	11.0	(6.4)	11.0	n/a
Std. Dev.	0.5	(0.6)	0.6	(0.6)	0.9	n/a	2.5	(1.4)	1.6	(1.4)	2.1	n/a	2.4	(1.4)	1.8	(1.4)	2.1	n/a
Median	2.5	(2.5)	2.8	(2.7)	3.0	n/a	5.2	(2.7)	1.5	(1.1)	1.0	n/a	10.7	(8.3)	7.0	(6.9)	6.4	n/a
Average	**2.5**	**(2.4)**	**2.7**	**(2.7)**	**3.0**	**n/a**	**5.7**	**(2.8)**	**1.5**	**(1.1)**	**0.7**	**n/a**	**11.2**	**(8.6)**	**7.1**	**(6.9)**	**6.2**	**n/a**

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. 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 three months prior to the survey.

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. Average – 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 forecasters' level only.

Survey results by sector

Figure 7: All Property	Rental value growth %				Capital value growth %				Total return %			
	2006	2007	2008	2006-10	2006	2007	2008	2006-10	2006	2007	2008	2006-10
Maximum	3.7	4.0	5.0	4.2	13.0	5.1	3.9	5.0	17.0	14.0	10.0	11.0
Minimum	1.4	1.5	1.8	1.9	1.0	-3.0	-7.0	-3.1	7.0	3.0	-1.0	2.9
Range	2.3	2.5	3.2	2.3	12.0	8.1	10.9	8.1	10.0	11.0	11.0	8.1
Standard deviation	0.5	0.6	0.9	0.7	2.5	1.6	2.1	1.4	2.4	1.8	2.1	1.3
Median	2.5	2.8	3.0	2.9	5.2	1.5	1.0	2.4	10.7	7.0	6.4	8.0
Average	**2.5**	**2.7**	**3.0**	**2.8**	**5.7**	**1.5**	**0.7**	**2.2**	**11.2**	**7.1**	**6.2**	**7.7**

Figure 8: Offices	Rental value growth %				Capital value growth %				Total return %			
	2006	2007	2008	2006-10	2006	2007	2008	2006-10	2006	2007	2008	2006-10
Maximum	8.7	8.1	7.7	6.5	13.7	8.1	7.1	7.0	20.3	13.8	12.1	11.9
Minimum	0.9	3.3	2.6	2.7	2.4	0.0	-5.0	-1.9	8.7	6.0	1.0	4.7
Range	7.8	4.8	5.1	3.8	11.3	8.1	12.1	8.9	11.6	7.8	11.1	7.2
Median	3.2	4.6	5.0	4.3	7.1	3.4	1.5	3.2	13.6	9.2	7.5	9.1
Average	**3.7**	**5.0**	**5.1**	**4.6**	**7.2**	**3.7**	**2.2**	**3.5**	**13.4**	**9.6**	**8.0**	**9.3**

Figure 9: West End Offices

	Rental value growth %				Capital value growth %				Total return %			
	2006	2007	2008	2006-10	2006	2007	2008	2006-10	2006	2007	2008	2006-10
Maximum	10.3	12.3	12.0	10.2	19.4	12.5	13.0	10.9	25.3	17.3	17.6	15.6
Minimum	3.9	3.9	4.1	3.0	3.0	-1.0	-8.0	-3.1	8.0	5.0	-3.0	2.7
Range	6.4	8.4	7.9	7.2	16.4	13.5	21.0	14.0	17.3	12.3	20.6	12.9
Median	5.8	6.8	6.0	6.3	11.3	6.1	3.1	4.8	16.6	11.3	9.0	10.2
Average	**6.0**	**7.1**	**7.1**	**6.3**	**10.6**	**5.7**	**4.3**	**5.3**	**16.0**	**10.8**	**9.3**	**10.3**

Figure 10: City Offices

	Rental value growth %				Capital value growth %				Total return %			
	2006	2007	2008	2006-10	2006	2007	2008	2006-10	2006	2007	2008	2006-10
Maximum	10.0	12.2	11.4	9.6	21.5	10.9	11.0	9.5	27.7	16.2	16.1	15.9
Minimum	1.5	4.5	4.6	3.5	2.2	1.0	-5.0	-1.5	8.2	7.0	1.0	4.6
Range	8.5	7.7	6.8	6.1	19.3	9.9	16.0	11.0	19.5	9.2	15.1	11.3
Median	4.1	6.6	6.0	5.9	8.2	6.0	3.6	5.4	14.1	10.8	9.0	10.6
Average	**4.6**	**7.0**	**7.5**	**6.0**	**8.5**	**5.5**	**4.1**	**4.9**	**14.5**	**11.0**	**9.6**	**10.6**

Figure 11: Standard Shops

	Rental value growth %				Capital value growth %				Total return %			
	2006	2007	2008	2006-10	2006	2007	2008	2006-10	2006	2007	2008	2006-10
Maximum	2.5	2.9	3.0	2.7	10.4	2.0	3.0	3.0	15.1	7.0	7.2	8.0
Minimum	-1.0	-1.0	-0.2	0.0	-1.9	-4.8	-6.4	-1.6	2.8	0.5	-2.0	3.0
Range	3.5	3.9	3.2	2.7	12.3	6.8	9.4	4.6	12.3	6.5	9.2	5.0
Median	1.4	1.3	1.4	1.5	3.4	0.1	-0.2	1.4	8.6	5.0	4.8	6.2
Average	**1.3**	**1.2**	**1.4**	**1.5**	**3.3**	**-0.5**	**-0.5**	**1.0**	**8.4**	**4.4**	**4.4**	**6.0**

Figure 12: Shopping Centres

	Rental value growth %				Capital value growth %				Total return %			
	2006	2007	2008	2006-10	2006	2007	2008	2006-10	2006	2007	2008	2006-10
Maximum	4.7	4.0	4.1	3.9	9.7	4.3	3.1	3.8	14.2	9.1	8.5	8.7
Minimum	0.0	-1.0	0.0	0.3	-1.0	-6.0	-9.0	-5.0	4.6	0.0	-3.0	1.2
Range	4.7	5.0	4.1	3.6	10.7	10.3	12.1	8.8	9.6	9.1	11.5	7.5
Median	2.0	2.0	1.9	2.0	4.0	0.5	0.4	1.6	9.5	5.7	5.5	6.7
Average	**2.1**	**1.7**	**1.8**	**2.0**	**3.7**	**-0.1**	**-0.1**	**1.2**	**9.0**	**5.1**	**5.2**	**6.4**

Figure 13: Retail Warehouses

	Rental value growth %				Capital value growth %				Total return %			
	2006	2007	2008	2006-10	2006	2007	2008	2006-10	2006	2007	2008	2006-10
Maximum	5.8	5.1	5.3	5.8	13.9	7.3	5.3	5.6	18.3	12.1	9.5	10.0
Minimum	2.0	1.8	1.8	1.9	2.6	-6.0	-11.0	-4.5	7.5	-1.0	-5.0	1.0
Range	3.8	3.3	3.5	3.9	11.3	13.3	16.3	10.1	10.8	13.1	14.5	9.0
Median	3.4	3.4	3.5	3.7	7.1	2.2	0.9	3.5	11.8	6.9	5.8	7.6
Average	**3.7**	**3.4**	**3.5**	**3.7**	**6.9**	**2.1**	**0.9**	**3.2**	**11.7**	**6.9**	**5.7**	**7.7**

Figure 14: Industrial

	Rental value growth %				Capital value growth %				Total return %			
	2006	2007	2008	2006-10	2006	2007	2008	2006-10	2006	2007	2008	2006-10
Maximum	2.2	3.0	4.3	3.0	10.5	6.3	3.1	4.0	16.6	11.7	9.6	9.4
Minimum	-0.2	-0.4	-0.4	0.3	1.0	-4.9	-4.0	-2.5	7.5	1.7	2.0	4.3
Range	2.4	3.4	4.7	2.7	9.5	11.2	7.1	6.5	9.1	10.0	7.6	5.1
Median	1.4	1.5	2.0	2.0	4.3	1.0	0.4	2.0	10.0	6.9	6.4	7.8
Average	**1.3**	**1.6**	**1.9**	**1.8**	**4.3**	**0.8**	**0.3**	**1.5**	**10.6**	**7.0**	**6.5**	**7.6**

Investment returns: how much longer can the party last?

Sabina Kalyan, Capital Economics

The property industry is currently celebrating yet another year of fantastic total returns, driven by rapidly falling yields and double-digit capital value growth. But for how much longer can the party last? Have falling yields left property looking so over-valued that an early-1990s style correction is on the cards? Following a presentation at a recent IPF lecture Sabina Kalyan expanded her views. This was prepared before publication of the IPD results for 2005.

At Capital Economics, we have long been bullish on commercial property. Indeed, at the start of 2005, when the IPF Consensus Forecast predicted year-end capital value growth of 4.3% year on year, we penciled in a relatively bullish 7.6% year on year. Our view was based on a three-pronged method of assessing fair value in the commercial property market – look at historic pricing; decide how much of it we can trust; and take into account any short-term cyclical and structural factors that could influence the market.

The lessons from history

To begin with, we do not hold with the scaremongering "yields at historic lows" headlines. While we concede that nominal yields are falling rapidly, once you strip out the impact of changes in the level of inflation, real property yields actually look remarkably stable between 1994 and 2005. This suggests to us that the dramatic falls in nominal yields over the past three years are partly a long over-due adjustment to the UK's new low-inflation/low interest-rate environment. Indeed, if we look back further, we see the current real property yield is slightly higher than the long-run average (see Figure 1).

Having established that real property yields are not, in fact, historically low, the next step is to look at how property has been priced relative to long bonds and equities over the past 80 years. Once again, the current property-gilt yield gap of around 1% is higher than the long-run average gap of 0.5% – suggesting that property is more attractively priced today than has been common over the long run. Even if we look at the property-equity dividend yield gap since 1920, while property does not look cheap, it certainly does not look wildly over-valued.

So why are some investors getting cold feet? For a start, few people look back to 1920 in assessing fair value! Indeed, we suspect that many investors became accustomed to the incredibly attractive relative pricing available in the late 1990s and the early part of this decade. Between 1998 and 2003 the gap between the initial property yield and 10-year gilt yield was fairly stable at around 2%. Similarly, between 1993 and 2004, the property-equity dividend yield gap was a stunning 4.5%. With these gaps now standing at 'just' 1% and 2% respectively, property certainly feels less attractive than at any time in recent memory. However, as we said before, relative to the long-run, property looks, if anything, undervalued relative to bonds, and only marginally over-valued against equities.

But is historic pricing really a reliable guide to the current valuation?

Just how far should we trust the sanguine picture painted by the long-run pricing information? Our approach has been to be highly selective, given the massive changes in both the economy and the UK property market over the last 80 years. For a start, between 1920 and 1945 the UK economy was 'freaky' for all sorts of reasons. We saw a short, sharp period of deflation in the 1920s, the Great Depression in the 1930s, the spike in economic growth in the run up to World War Two, and then another recession during the war. So we probably do not want to take any pricing information from that period as a benchmark for current valuations.

We also think we should ignore pricing information from the 1970s and 1980s. During this period, the UK experienced double-digit inflation combined with three major recessions. As inflation sky-rocketed, real bond yields became negative.

Since the early 1990s, we reverted to a more benign economic environment. Inflation has fallen beneath the Bank of England's target range and, given the change to an inflation-targeting monetary policy regime, is set to stay there. In addition, economic growth has been stable and positive since 1993. And looking ahead, we remain positive about the long-run structural position of the UK economy. The introduction of new technologies, supply-side reforms in the 1980s and improved macroeconomic policy regimes suggest to us that growth should be less volatile than in previous decades.

Given that economic conditions going forward are likely to be diametrically opposed to those in the 1970s and 1980s, using pricing information from those decades to assess current and future valuations looks perverse. In fact, the period 1946 to 1970 more closely approximates current economic conditions. During this period, the UK experienced a 'golden age' characterised by a relatively low level of inflation and uninterrupted, positive economic growth. We would argue that average yields during this period are a better benchmark for valuation in the current cycle.

In other words, we think that investors should look for, at minimum, a positive gap of around 0.5% between the property initial yields and the long-run gilt yield, and a gap of around 2.9% between the property yield and the equity dividend yield. On this basis, property no longer looks cheap against gilts, and looks over-valued against equities (see Figure 2).

So, does this mean the party is over?

So, after years of proclaiming how attractive commercial property was compared to other asset classes, we now feel that there is little value left in the sector. Having said this, we do not expect the party to come to an end just yet.

For a start, there are strong structural reasons why capital flows are likely to hold up in the near term. While some investors are selling at what they perceive to be the top of the market, this net disinvestment has been more than offset by demand from institutions, overseas investors and some quoted companies. We expect this to continue well into 2006 as institutions continue to

Figure 1: Real property yields 1920-2005

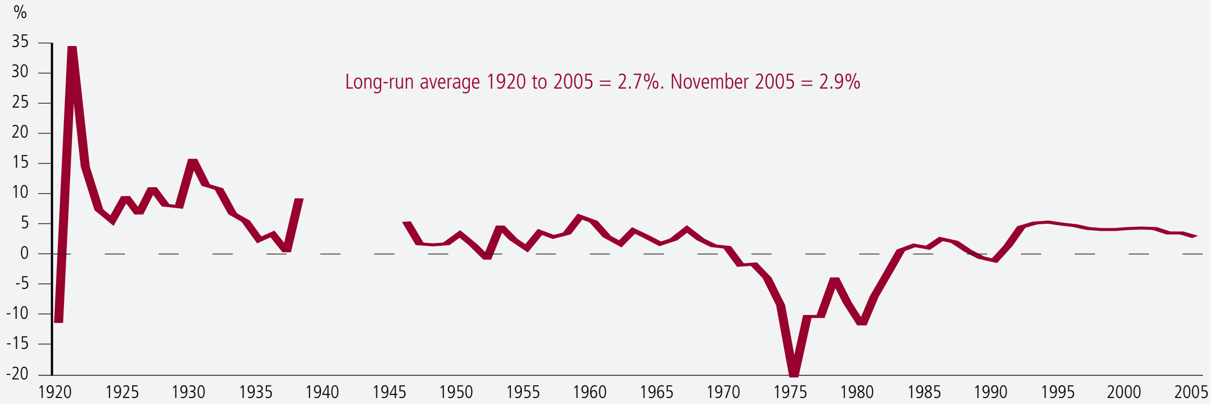


Figure 2: Real property yields 1990-2005

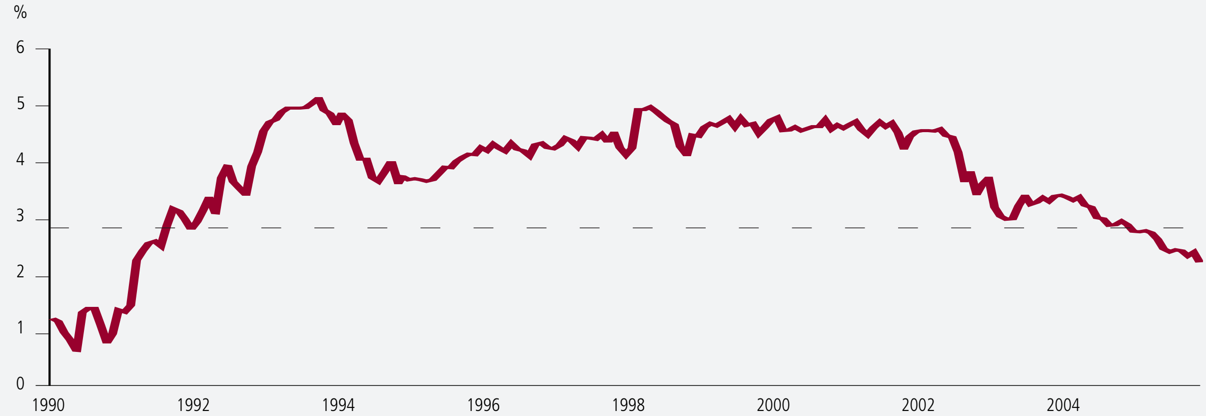
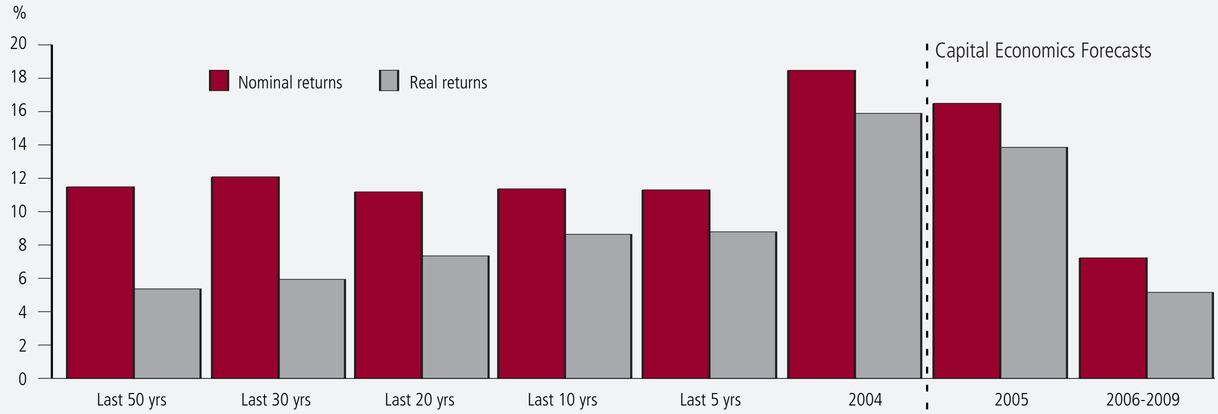


Figure 3: Annual property returns



spend increased allocations; overseas investors are attracted to Europe's largest and most liquid market; and some quoted companies re-shape their portfolios in anticipation of converting to specialised REITs.

The cyclical reason for our bullish investment market view for 2006 is that we think that bond yields will edge a little lower when the Bank of England cuts the repo rate to 4% by the end of 2006 to offset the deflationary impact of soft economic growth. Lower bond yields mean a lower cost of funding for debt-backed investors and also help keep property attractive relative to bonds throughout the forecast period.

The upshot is that while we think that property is currently modestly over-valued, and set to become more so, we expect nominal property prices to stabilise rather than fall, as yields creep back up in 2007, 2008 and 2009, bringing property valuations back in line with fundamentals. Is our happy ending scenario too optimistic? We think not, for two reasons. First, the magnitude of the over-valuation we are expecting is slight and requires only a minor correction. Second, it would be historically atypical, though not unprecedented, to see big falls in property prices when the economy was not in recession.

Overall, we think that the period when an investor could buy indiscriminately and rely on rapidly falling yields to drive super-normal returns will come to an end in 2006. However, in the absence of a full-blown UK recession or a sharp rise in bond yields, the chances of a 'hard landing' in the investment market are slim. Instead, we see a rather 'boring' period where property delivers real annual total returns of around 5% through income rather than capital growth. While this might seem dire compared with recent double-digit returns, it is actually bang in line with the 50-year average, not to mention the typical target return set by institutional investors (see Figure 3). So, while our medium-term forecasts might seem bearish, they represent nothing more than a somewhat over-due return to normality.

Education: Retail under threat – riding out the perfect storm

A recent IPF lecture looked at prospects for the retail market. Speakers included Richard Boys-Stones, Partner, Business Recovery Services, PricewaterhouseCoopers; Mark Teale, Director of Retail Research at CB Richard Ellis and Mark Chivers, Head of Location and Strategy Development, Boots Properties.

Boys-Stones said that 2005 was a bad year for UK retailers, reflected by the fall of over 5% in the FTSE General Retail share index compared with the rise in the all-share index. However the FTSE Food and Drug Index, dominated by Tesco, fared better, despite the poor performance of Morrisons. Since the end of 2004 both the volume and value of retail sales (in constant prices) declined with the slowdown in consumer spending.

Continuing reductions in the wholesale price of goods benefited consumers, particularly for audio-visual equipment and clothing. These trends should favour retailers, but increasing competition from supermarkets and the internet mean the advantages were eroded.

Meanwhile operational cost inflation is now around 5% per year due to the uniform business rate revaluation, rising fuel costs and the impact of minimum wage increases on labour costs. Retailers' profits were squeezed for some time, although value retailers like Primark thrive and are expanding their space occupation, and internet players such as Amazon suffered less cost pressure than their store rivals. Conversely electrical goods retailers, selling big discretionary items, and DIY operators, dependent on a healthy housing market, are suffering.

Retail property returns hold up because new tenants, e.g. H&M and Zara, expanded into premises vacated by the casualties of the last 12 months. Vacancy in prime locations is stable, although this may change. Secondary space may be more vulnerable. Out-of-town locations suffer from business failures, particularly in bulky goods, but strong demand remains for prime retail warehousing.

Rental growth for standard shops is bumping along the bottom, while retail warehouses are declining after strong growth. Property owners must look for warning signs amongst potentially vulnerable tenants. Key indicators include breaches of banking covenants, reductions in customer footfall and reduced conversions of store visits into purchases.

For strong operators this market offers opportunities to eclipse the competition, by improving operational efficiency, restructuring stock towards new product ranges, and reducing overheads.

Taking a longer-term perspective, Teale sees town centre shopping under further threat from out-of-town development. He presented findings from CBRE's National Survey of Local Shopping Patterns, which tracks consumer shopping destination preferences since 1995.

Maturing out-of-town shopping poses a threat to town centres, with improved accessibility, parking, range of outlets and security. This allies with the increased sale of non-food goods in supermarkets, which are moving increasingly out-of-town. Only town centres with new developments hold their own, while environmental issues and poor High Street management by most local authorities is undermining prime locations.

One answer may be business improvement districts (BIDs), but these are few. London is continuing to lose domestic shoppers, with congestion charging and pedestrian congestion increasing reliance on tourists – each spending 5% of a UK customer.

Tesco's domination of the grocery market means that 50% of the UK population do their main food shopping there or at Asda. In addition, they are making significant inroads into 'convenience goods', e.g. clothing.

Nearly half of retail parks now have grocery operators in their locality, providing an 'indirect anchoring' effect, with the grocery and other park operators drawing on the same core catchments. In this way, locations of 'everyday-type' comparison shopping is less distinguishable from that of convenience shopping.

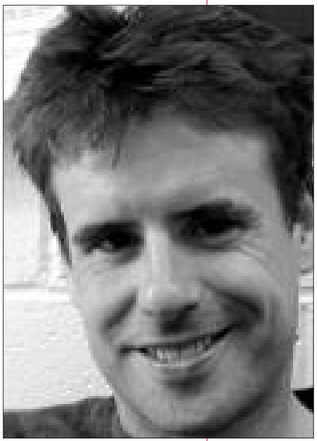
Fashion retailing is still mainly town centre based, with only 7% of clothing space out of town. But town centres are losing market share. Infrastructure factors are crucial to this trend: nearly a third of shoppers report that they abandon fashion shopping trips because of the misery of the experience – due mainly to road congestion. Congestion increases journey costs, to which consumers are now sensitive.

London is likely to see record levels of retail development activity over the next decade, with projects like White City, Elephant & Castle, Stratford City and Battersea. Combined with substantial transport improvements like Crossrail, this shifts the hierarchy of retail locations. Despite the efforts of the New West End Company BID, which seeks to raise the attractiveness of London's traditional retail locations, it is probable that suburbia will take a greater market share.

Chivers focused on the benefits of restructuring retail real estate in the current climate. The Boots sale and leaseback deal on 312 stores with REIT Asset Management in July 2005 released £300m of capital for the business. He emphasised the flexibility permitted within the contract, allowing Boots to vacate a proportion of the stores before the end of the initial 15-year lease period. Rent increases are fixed at 1.5% per year, and REIT is not permitted to break up the portfolio or securitise the assets.

Boots' strategy for holding property means that freehold ownership is preferred in key locations where they are committed to safeguarding their interests. In other locations, Boots is ambivalent about freehold or leasehold ownership, with the choice dependent on the property and occupational economics prevailing at the time. Freehold property is often cheaper over the longer term, especially if accompanied by significant capital appreciation. However this may be at the expense of balance sheet efficiency and the debt raising capacity of the company. Ultimately, the decision whether to own or lease is taken in the light of balance sheet strategy, and is thus partly dependent on non-property considerations.

Research: Disagreement and uncertainty in UK property market forecasts



Patrick McAllister, University of Reading

Additional contributions from: George Matysiak (University of Reading) and Graeme Newell (University of Western Sydney).

The IPF commissioned research to contribute to understanding the reliability of property forecasts.

This article is the executive summary from the research findings. A copy of the full research findings is available, price £150, and the order form is on the IPF website.

Background and objective

Property forecasts are an integral part of the property investment process at the strategic, tactical and stock selection levels. This study investigates the nature, extent and patterns of disagreement and uncertainty in the forecasts of UK property investors and their advisors. From the outset, it is important to be clear that uncertainty is inevitably associated with all forecasts and that a set of forecasts will contain some degree of disagreement. Market structures and relationships are never completely stable and even a perfect model could not account for (by definition) unforeseeable 'shocks'. Property market forecasts also rely upon forecasts of the market drivers which are typically obtained from macro-economic forecasting organisations. Different forecasting organisations then apply different model specifications to these inputs, interpret the information in different ways and, inevitably, produce different forecasts.

Data and approach

In order to examine uncertainty and disagreement in property market forecasts, we analysed the IPF's consensus forecasts from 1999 to 2004. The forecasts of individual property forecasting organisations were made available to the researchers on an anonymous basis. In addition, we compared the results from the property forecasters with non-property forecasters predicting an array of macro-economic and capital market variables. We then applied a range of standard measures of accuracy to the forecasts.

Main findings

- An interesting finding of the analysis is the extent to which property forecasting organisations agree with each other. This may be caused by a combination of the use of common forecasting methods, obtaining 'driver' forecasts from similar sources and an element of herding among forecasting organisations.
- Although most property forecasting organisations tend to have similar expectations, the consensus forecast often contains significant forecasting uncertainty. This suggests that forecasting organisations should not draw too much comfort about being close to the consensus.
- Given high levels of agreement and high levels of uncertainty in the consensus forecast, uncertainty in the property forecasts of the individual organisations seem to be primarily generated by common factors rather than by the individual forecasting organisation itself. This is not a unique feature of property market forecasters and non-property forecasters display similar patterns.
- A key source of uncertainty in the property market forecasts of capital and total returns may have been due to problems of forecasting yield shifts. The fact that capital growth tended to 'mirror' rental growth indicated that forecasters' expectations of capital returns were generally a product of rental return expectations. This may reflect the generally acknowledged difficulties of modelling yield shifts rates relative to rental growth. Alternatively, it may result from the aggregation of individual sector and regional forecasts into a forecast of the index.
- The analysis suggests that there are inefficiencies in property market forecasts. When market performance was improving, total returns tended to be systematically underestimated. Conversely, when performance was deteriorating, total returns tended to be systematically overestimated.
- We find little evidence of consistent superior or inferior performance among individual forecasting organisations. When comparing the performance of individual forecasting organisations, very few stand out. Again this is true of both property and non-property forecasting organisations.
- At a group level, property advisors and fund managers tended to be marginally more accurate (in terms of absolute error) in their property forecasts than equity brokers.
- In specific years, across the three performance measures, the 'best' individual forecasters were property advisors (45% of years), fund managers (20% of years) and equity brokers (35% of years). However, most individual forecasters were generally unable to repeat the performance in other years. Most evidence of forecasters being able to repeat strong performance was for rental growth.

Acknowledgement

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Capital & Regional, Donaldsons, Grosvenor, GVA Grimley, Investment Property Databank, KPMG, LaSalle Investment Management, Land Securities, Lovells, Morley Fund Management, Nabarro Nathanson, Prudential Property Investment Managers, Quintain Estates & Development, Scottish Widows Investment Partnership, SJ Berwin and Strutt & Parker.

Research: Institutional investment in regeneration – necessary conditions for effective funding

Charles Follows, Investment Property Forum

The regeneration of communities and localities across the UK is a central part of government policy and local planning policy. To that end, government has introduced various policy initiatives, set up agencies and encouraged the re-use of brownfield sites, to stimulate urban regeneration. However, successful regeneration often relies on the private sector landowners and developers to bring forward sites and for banks and investors to provide finance at the various stages of specific projects. Ultimately all property requires an end owner/investor to provide long-term capital. Therefore, government policies will not be completely successful unless the interests of the private sector are harnessed, alongside the policy agenda.

Regeneration uses different sources and types of finance at the different stages of the process. Disparate funding sources have different return targets, assessment criteria, timescales and objectives. In addition, regeneration, particularly large-scale projects, is messy, management intensive, often complex, impacts on many stakeholders, can involve variety of landowners, and require public sector intervention.

The IPF and funding partners wish to more fully understand the reluctance of many institutional investors to engage in regeneration projects in order to encourage further dialogue between the policy makers in government and the sources of finance. So they jointly funded this research project, undertaken throughout 2005.

This project examines the requirements of the private sector sources of short-term funding and long-term capital. It looks at the main finance sources – banks, private equity, fixed interest and long-term property investors – to understand their needs and requirements. It will identify the necessary conditions that need to be in place to get the private sector to fully engage with government, national and local, and regeneration agencies. By explicitly identifying these necessary conditions, it is hoped the project will help to build a bridge and dialogue between the private sector and government policy.

Many sources of finance shy away from regeneration projects because of the perceived difficulties and protracted timescales. Financiers and investors perhaps over emphasise the risks and many projects are placed on the 'too difficult' pile. As a result, investors may forgo attractive returns. The research suggests that a regeneration investment vehicle with a mix of capital sources, and a portfolio of regeneration projects, would attract considerable interest across the sources of capital. Each participant would receive appropriate tranches of return reflecting their risk capital and objectives. The vehicle would hold a portfolio of projects at differing stages of the regeneration process to generate a diversified cash flow. The vehicle would provide management expertise and continuity for protracted projects.

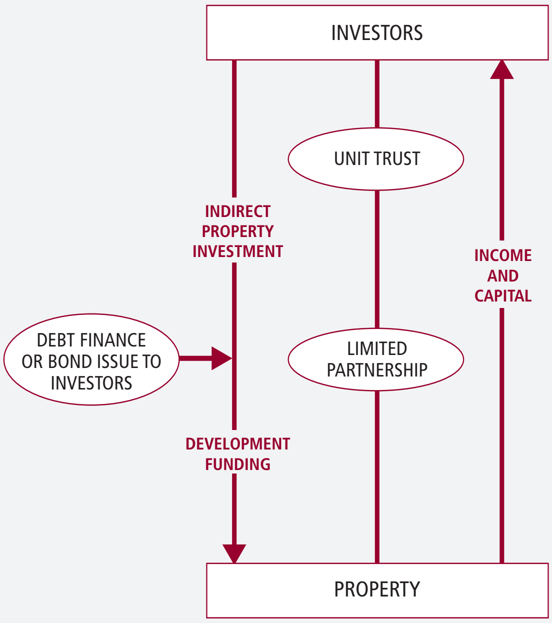
On 19 January 2006, nearly 200 people attended the launch conference for the initial findings of the project. The conference received the executive summary of the research findings from Professor Alastair Adair, the leader of the research team. This was followed by a number of speakers presenting their personal experiences in regeneration projects and commenting on the research findings. The conference was an opportunity for the research team to obtain market participant's reactions on the executive summary and overall thrust of their recommendations. They are now finalising the report, to be published shortly. The executive summary is available on the IPF website, together with the papers presented at the conference.

This article is a brief extract from the executive summary to set out the main findings. It is intended that this research will act as a catalyst for ongoing debate. Indeed the IPF has already started the debate with the ODPM and political parties. The suggested financing vehicle, from this research, is only one of many possible solutions. The property industry is encouraged to work to develop innovative structures to meet this challenge. If the industry is successful in attracting institutional investment funds to regeneration schemes not only will it help to alleviate pressing social and economic issues, but it will also widen the potential investment universe and perhaps satisfy the apparently insatiable demand for investment property.

Research findings

The central question at the heart of this research was to explore the conditions and type of vehicle that would attract more institutional investment into regeneration. The present regeneration funds are typically established using tiered limited partnership and unit trust structures. Figure 1 shows this structure in simplified form. In the structure, the institutional investment is made by way of subscription for units in a unit trust which in turn invests the subscription proceeds in a limited partnership. The limited partnership combines the equity subscriptions with bank debt or a bond issue to fund the development of the project. On completion of the development, net income arising from the property is distributed through the partnership and the unit trust to the investors. Net capital proceeds (arising from a disposal of the property) are distributed in the same way.

Figure 1: Traditional investment vehicle structure



The key characteristics of the most commonly used co-investment vehicles are shown in Figure 2. The need to combine the limited partnership with the unit trust arises because the UK limited partnership suffers from burdensome transfer tax treatment (which diminishes returns, hampers liquidity and ultimately affects project viability).

The key messages from our interviews have led us to propose a regeneration investment vehicle which, from a funding perspective, allows the combination of bond and indirect property investment/private equity elements (Figure 3) coupled with traditional bank debt. From a structural perspective the vehicle facilitates efficient management whilst offering tax efficiency, liquidity and flexibility to investors. The combined structure shown in Figure 1 has emerged as a viable fund model that can meet most of the funding and structural objectives. However, we consider that certain inefficiencies (in particular, the requirement to operate part of the combined vehicle offshore coupled with a sometimes cumbersome management framework arising from the fact that decision making takes place at various points in the structure) could be improved by the introduction of a new vehicle.

This structure may take the form of a REIT, but the full details of the legislation and regulations are needed, following the March budget announcement. Whilst removal of the 25% development restrictions is helpful, the interest cover test and income distribution requirements may mitigate against the use of a REIT for major regeneration projects.

As an alternative a new structure is proposed. The form of the vehicle could be in the nature of a UK-based investment trust (similar to a REIT) which would benefit from tax transparency (allowing investors to be taxed on income and capital gains as though they owned an interest in the underlying property directly) and transfer tax rates comparable to that applicable to equities to encourage investment and a liquid market. The scope of permitted activities of the vehicle would be sufficient so as to allow the development of and investment in 'qualifying' regeneration projects. The vehicle would secure finance from banks and investment from fixed income (bonds) and property institutions in order to invest across all phases of the regeneration process. In effect a number of regeneration investment vehicles should be set up operating on a project by project basis.

Figure 2: Typical co-investment vehicles used for regeneration projects

Investment vehicle	Tax treatment	Transfer tax	Listable	Open/closed ended	Investor restrictions
UK Limited Partnership	Tax transparent	4% on gross asset value of underlying UK property	No	Usually closed ended	Usually limited to institutional investors or high net worth individuals
UK Unauthorised Exempt Property Unit Trust	Effectively tax-free at vehicle level	0.5%	No	Either	Only available to UK tax exempt investors (i.e. pension funds and charities)
Jersey Property Unit Trust	Tax transparent. Can receive and distribute UK income gross. Not subject to UK capital gains tax	Nil	Yes, but unusual	Usually closed ended	Depends on regulatory approval obtained
Guernsey Property Investment Company	Not transparent but tax liabilities can be mitigated. No UK capital gains tax at property level.	Nil	Yes, in UK and Guernsey	Closed	Open to the public (including ISAs)

Figure 3: Elements and potential parameters of a regeneration investment fund

Bond element:	**Purpose of raising up front capital. Possibility of linking to PFI-type infrastructure projects**
Bond rating	Investment grade
Issuer/covenant strength	Various options including Govt backed/LA backed/ credit enhanced/insurance wrapper applied
Holding period	20+ years (to allow for development)
Pricing/risk premium	Gilts + 60 to 110bp
Liquidity	Tradeable
Payment of coupon	Fixed or variable coupon
Benchmarking	Against gilts
Fund size	Minimum £200m per issue
Gearing	Balance from private equity and bank borrowing
Return requirements projects gilts + 3%	Govt backed - LA gilts + 1-2%/PFI
Indirect property investment / private equity element:	**Purpose of funding development phase – capital gain & income Higher risk and higher return**
Holding period	Rolling three to five years in the case of private equity; longer in the case of indirect property investment
Fund size	Minimum £100m
Return requirement	Mid-teens +IRR
Possible structure	Combination of existing or new co-investment vehicles
Liquidity	Limited
Benchmarking	Absolute returns
Exit strategy	Sell to new investor
Long-term funding element:	**Comparable to direct property investment**
Pricing	NAV of scheme would dictate price
Exit strategy	Exit points at any time

The bonds component of the financing could take a number of forms, ranging from conventional issues (wrapped or unwrapped) secured on the schemes to government-backed issues funding infrastructure. There is also an opportunity to issue bonds with returns linked to an IPD index or to the value of the underlying scheme.

Our research shows that the various sources of finance would be likely to invest in a regeneration investment vehicle provided it is suitably structured to meet their differing demands for returns and appetites for risk. An essential requirement will be an expert and experienced management team.

Regeneration is currently at the forefront of the government's priorities. At this time, our evidence shows there to be a substantial weight of institutional money that could be attracted into regeneration. This research is recommending a regeneration investment vehicle as an attractive means of delivering more institutional finance to meet the government's sustainable community targets. It is vitally important that a dialogue should commence among the interested parties to develop this idea and deliver institutional investment into regeneration.

Methodology

The research adopted a cross-asset class examination involving key institutional investors to determine the components of a model to encourage institutional investment into regeneration. This summary synthesises the key issues from matters discussed and evidence presented at the structured interviews with fund managers and debated at three workshops capturing public and private sector perspectives.

The IPF Educational Trust and IPF Joint Research Programme

This research was commissioned and partially funded under the auspices of the IPF Educational Trust and IPF Joint Research Programme. The programme is funded by a cross-section of 16 businesses, representing key market participants. The IPF Educational Trust and the IPF gratefully acknowledge the contributing organisations: Capital & Regional, Donaldsons, Grosvenor, GVA Grimley, Investment Property Databank, KPMG, LaSalle Investment Management, Land Securities, Lovells, Morley Fund Management, Nabarro Nathanson, Prudential Property Investment Managers, Quintain Estates & Development, Scottish Widows Investment Partnership, SJ Berwin and Strutt & Parker.

Joint funders of the research

The project was jointly funded by the British Property Federation (BPF), British Urban Regeneration Association (BURA) and English Partnerships. The IPF gratefully acknowledges their substantial financial support and the invaluable contributions from their representatives on the project steering group.

The research team

Professor Alastair Adair, Professor Jim Berry and Professor Stanley McGreal (all of the University of Ulster) and Professor Norman Hutchinson (University of Aberdeen). Suzanne Allan, (formerly of the University of Ulster, now PriceWaterhouseCoopers), was part of the research team in the first two thirds of the project. In addition, Deborah Lloyd, Justin Cornelius and James Dakin of Nabarro Nathanson (a donor to the IPF and IPFET Joint Research Programme) greatly assisted the research team towards the end of the project.

The project steering group

The IPF appointed a project steering group to guide and assist the Research team. They gratefully acknowledge the contribution from the Chairman – Phil Clarke (Morley) and David Shevill (observer from ODPM), Faraz Baber (BPF), Justine Lovatt (English Partnerships), Paul McNamara (Prudential), Peter Freeman (Argent), Rebecca Worthington (Quintain), Simon Burwood (BURA), Steve Carr (English Partnerships), Tom O'Grady (SJ Berwin) and Charles Follows (IPF).

Research Programme update

This edition of Investment Property Focus, reports the findings of the two recently completed projects funded under the IPF and IPF Educational Trust (IPFET) Joint Research Programme: Forecast disagreement in UK property markets; and Institutional investment and regeneration: necessary conditions for effective funding. There are a number of projects that will complete in the coming months, the Research Steering Group are developing ideas for commissioning more projects in the future.

The research projects are disseminated to IPF members, via the IPF website, and to others in the investment community in the UK and Europe. They are reported in the property and investment press, national press and discussed with government. The director and research teams present project results at conferences, lectures and workshops.

The IPF uses the research to build its relationship with government by developing its reputation as a rigorous and thoughtful organisation. Research output was presented in the submissions to government on REITS and upward only rent reviews. HM Treasury received a preview of the report on the size and structure of the UK investment market. The Bank of England uses the IPF Consensus Forecasts as part of its assessment of prospects for the UK economy. The IPF Consensus Forecasts are seen as important in the developing property derivatives market.

It is widely accepted that IPF research is rigorous, high quality and independent, with extremely positive feedback from practitioners, academia, government and the IPF membership. The IPF brand for high quality independent research is strong and internationally recognised. The IPF was awarded the International Real Estate Society (IRES) 2005 Award for Corporate Excellence in June 2005, in recognition of the Joint Research Programme role in leading research in the UK property investment market.

Projects reported to date:

- Liquidity of commercial property
- Opening the door to property
- Size and structure of the UK investment market
- Depreciation in UK markets
- Investment performance and lease structure change in the UK
- Sustainable property appraisal
- Institutional investment and regeneration: necessary conditions for effective funding
- Forecast disagreement in UK property markets

Ongoing projects:

- Behavioural influences on property stock selection decisions
- The investment performance of listed office buildings
- Index smoothing and the volatility of the UK commercial property market revisited
- Diversification in property portfolios
- Planning policy and retail property market performance in English towns and cities
- Property derivative pricing guidance note

The IPF and the IPFET are only able to deliver this series of high quality series of research initiatives through the IPF and IPF Educational Trust Joint Research Programme. The programme is funded by 16 businesses, representing key market participants.

The IPF Educational Trust and the IPF gratefully acknowledge the contributing organisations:

Capital & Regional, Donaldsons, Grosvenor, GVA Grimley, Investment Property Databank, KPMG, LaSalle Investment Management, Land Securities, Lovells, Morley Fund Management, Nabarro Nathanson, Prudential Property Investment Managers, Quintain Estates & Development, Scottish Widows Investment Partnership, SJ Berwin and Strutt & Parker.

Building on success: The IPF Research Programme 2006 to 2009

The IPF successfully raised its target of £1million to fund all of its research activities and research projects over the next three years, as the existing research funding is almost committed. Within the full range of research activities, the IPF will continue the acclaimed series of research projects.

The IPF invited organisations across the breadth of the property investment market to become a 'Supporter of IPF Research'. The target was for an exclusive group of 22 Supporters of IPF Research. The IPF ensured that the Supporters of IPF Research represent all aspects of the property investment market and include leading and visionary fund managers, property companies, banks, accountants and solicitors.

Future research ideas and volunteers needed.

If you have an idea for a topic or an issue that the IPF should research, please contact any member of the IPF Research Steering Group.

The Research Steering Group comprises of 11 members under the chairmanship of John Gellatly (MLIM) with Paul McNamara (PruPIM), Robin Goodchild (LaSalle Investment Management), Tony Key (City University), Stephen Palmer (Alecta Investment Management), Neil Turner (Schroder Property), Nick Tyrrell (JP Morgan Asset Management), Stuart Beevor (Grosvenor), Phillip Nelson (Trehaven Group Ltd), Amanda Keane (IPF) and Charles Follows (IPF).

For each research project the IPF appoints a project steering group of IPF members to work alongside the research team. If you are able to devote some time to helping the IPF by serving on a project steering group please contact Charles Follows, Research Director at cfollows@ipf.org.uk 020 7194 7925.

Forum news

IPF relocates to the City

The IPF recently moved to new offices. The accommodation, provided by serviced and managed office provider Stonemartin, is located at New Broad Street House (NBSH) beside Liverpool Street station. The building is owned by funds managed by Morley.

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The decision for the move was prompted by the RICS decision to surrender the lease on 3 Cadogan Gate, the IPF's former home, and release the building from the Institution's property portfolio. The RICS's accommodation rationalisation neatly coincided with the IPF Board's aspirations to secure its own office space. However, maintaining the close working relationship we have with the RICS will continue to be a top priority even though we are no longer under the same roof.

IPF executive

Sam Chappell left the IPF at the beginning of March to take up a post at the Audit Commission. She is replaced by Suleen Syn.

Subscriptions 2006-07

Each year the IPF Management Board reviews the subscription fee to ensure the financial stability of the IPF. Where possible any rise is kept to a minimum and in 2005/06, we avoided any increase by exploring other avenues such as some limited sponsorship of activities such as the Annual Lunch and Dinner.

In 2006/07 the subscription fee is set at £165pa. We hope you feel that this small increase continues to represent excellent value for money. At the same time we are expanding the number of free events to members and making access easier to our highly regarded research outputs.

The subscription notices go out shortly and, as ever, we greatly appreciate your prompt payment.

Regional boards

The success of the IPF regions is due largely to the hard work and dedication of a small group of members who form the regional boards. From time to time the composition of the boards changes and recently we have had some changes and new members join the boards. In the Midlands, David Allen of NAI Fuller Peiser has taken on the role of Regional Vice Chairman and will succeed Andrew Yates of Pinsent Masons as Chairman at the Midlands Dinner on 19 October. The board also welcomes two new members, Andrew Osbourne of Kenmore and Andrew Franck Steier of Colliers CRE. In the North, Andrew Quinlan of Pinsent Masons has taken over the role of Chairman from Andrew Hawkins of Jones Lang LaSalle. Ben Roberts of Kenmore has also joined the regional board. In Scotland, we also welcome Paul Findlay of Arlington to the regional board.

Education

Plans are well under way for a restructure of the IPF's Advanced Education Programme. Among a number of improvements, we are watching a new three-day indirect property investment module later this year as well as a new web based module introducing property as an asset class. For more information see www.ipf.org.uk. We are also applying for full course accreditation by Cambridge University – more news on that as soon as we hear – and at the same time we just accepted our 400th student on the programme.

Another set of IPF Diplomas were awarded in January to those who successfully completed the Advanced Education Programme in 2005. This year, they went to:

- Mark Powell – Chase & Partners
- Michael Cunningham – Scottish Widows Investment Partnership
- Michael Haddock – CB Richard Ellis
- Mark Meiklejon – Standard Life Investments
- Nigel Marsden – Warner Estate Holdings Plc
- James Mclean – Scottish Widows Investment Partnership
- Ben Gamble – King Sturge

- Gunnar Herm – UBS
- Victoria Fairhall – Savills plc
- Kerri Hunter – Scottish Widows Investment Partnership
- David Bannerman – ProLogis Management Sarl

Two prizes were also awarded for outstanding performance on the course. Michael Haddock of CB Richard Ellis was the winner of the IPF Educational Trust John Whalley prize for best overall performance and Keith Manning of BP Investment Management won the Module Prize for his performance in the assessment of the modules.

Our regular property derivatives workshops continue to run in London and more recently in Scotland and Sweden in partnership with IPD. We also introduced another specialist one day course, which explores the support processes for transactions involving property derivatives – for more information see www.ipf.org.uk. And of course, for those wanting access to property derivatives resources there's the www.propertyderivatives.co.uk site we have launched for IPF members.

At the time of going to press we are also planning the spring/summer season of events. Watch out for sessions on the EU Energy Directive and our regular slot covering the De Montfort bank lending survey.

Events

Birmingham Conference: January 06

The IPF's first major research launch occurred in January in Birmingham with over 160 people attending discussions on the findings for Institutional investment in regeneration. Many thanks once again to Locate Birmingham for its generous support which allowed the event to take place at the ICC. The summary is available in the IPF website in the research area.

Outlook for Property & the Economy members' event: January 06

January saw another sell out for this annual event with more than 200 members of IPF and SPR in attendance. We heard from Robert Houston of ING Real Estate Investment Management, who predicted that investors would again be happy with the returns on commercial property. ING is forecasting an overall return of 9.2% pa for the next four years. But Houston acknowledged that even within his own firm there was a much closer balance between bulls and bears, and that investors' expectations of property had been reined in after two years of returns in the high teens. The majority of those questioned in a survey carried out by ING in November 2005 would be happy with a property return of 8% this year. ING also believes that yields may have room to fall even further, with equivalent yields nudging down to an average of 5.8%. But Houston personally sees the implied breach of the 5% mark on initial yields as a psychological barrier for investors.

Also on the podium was Roger Bootle of Capital Economics who predicted commercial property returns of 6% to 7% for 2006, reflecting his view that the sector is now becoming over-priced, especially compared to equities which he sees as fairly-valued in the light of a UK economic growth forecast of 2%, held back by weak consumer confidence amid worries about pensions, the housing market and personal debt.

John Betteridge of M&G, responsible for asset allocation within the Prudential Group, sees property's attractiveness in the portfolio waning, due to far-reaching changes in regulation, accounting and actuarial practice. These changes mean that strategic allocation should place much more emphasis on limiting volatility through investment in fixed income assets, so that both pension funds and insurers are less likely to favour property than they were two years ago. And like Bootle, Betteridge also believes property yields have moved into the realm of price irrationality, while globally equities now appear much more solidly-based given recent levels of corporate profitability.

IPF Annual Lunch 2006: February 06

More than 1,100 members and their guests attended this year's Annual Lunch at the Grosvenor House. The event, which was sponsored by Chase & Partners and Jones Lang LaSalle, welcomed journalist and commentator John Plender as the after lunch speaker. John, who is a long-standing member of the IPF, provided an extremely thought provoking take on the UK property industry.

Future dates for your diary:

Midlands Hot Property Party 2006
3 May 2006 – Birmingham (Jam House)

Midlands Lunch 2006
8 June 2006 – Birmingham (Hyatt Regency)

AGM
June 2006 – London, date to be advised

IPF Annual Dinner 2006
29 June 2006 – London (Grosvenor House)

Scottish Conference 2006
14 September 2006 – Glasgow (Radisson SAS)

Midlands Dinner 2006
19 October 2006 – Birmingham (ICC)

IPD/IPF Annual Conference
30 November to 1 December – Brighton (The Grand Hotel)

IPF Annual Lunch 2007
31 January 2007 – London (Grosvenor House)

Interview with an IPF member: Jamie Ritblat

Jamie Ritblat, Delancey Estates

Interview by Alex Catalano

Jamie Ritblat is a fundamentalist. "My view on life is that if you don't start with fundamentals, you don't have a very strong deck of cards," he says.

Propertywise, life has dealt Ritblat a couple of high cards: son of John Ritblat, the creator of British Land, he trained under Elliott Bernerd at Morgan Grenfell Laurie and bought real estate for George Soros. But Ritblat is a skilled player in his own right and now, just turned 39, heads up his own property empire, Delancey Estates and its £2.5bn of assets.

Applied to real estate, the Ritblat philosophy means you buy quality assets. "They are not being bought for the benefit of yield enhancement, but have got good underlying fundamentals."

As Ritblat points out, most growth in real estate over the last two to three years has come from yield compression rather than rental growth. "We've had a terrific run and a re-rating of real estate, which I think was overdue, versus other forms of investment; with the exception of the West End where there's been clear rental growth," he says. "In Midtown we're seeing some growth now. In the City it's arguable there's a bit but it's pretty sporadic and the incentives still available are not inconsiderable. Outside London there's growth in some areas, though it's not consistent.

You haven't had a market built on fundamentals. The weight of money has driven secondary yields in, as people have sought income and yield without true consideration to the underlying asset – that's the issue," says Ritblat. However, he isn't calling the market, pointing out that it's nigh-impossible to forecast the turn or its trigger, "whether it's bird flu or rising interest rates.

But I do think that non-prime property is overpriced relative to prime property. When a correction occurs, it will be secondary property that will suffer the most. I don't think you will see a major correction in prime property, and some will continue to improve in yield terms," he predicts.

Hence, Delancey focuses on buying prime assets, or those that can be redeveloped, face-lifted, or primped into revealing their true quality. "Starting with the right rent, or close to it, and the ability to add value through doing things. It's easily talked about and hard-fought to achieve," Ritblat notes. "If you buy on that basis and finance it accordingly, you can afford to wait and keep the asset, even if the things you thought would occur, don't. We follow that line."

As an example, he points to MidCity Place, the 350,000 sq ft building in Holborn that Delancey bought in November 2004 for £215m.

"Terrific building, built five years ago, super floorplate, average rent £35 a foot, very nice tenants," he rattles off. "We paid about a 6% yield, which even by old-fashioned standards is not the wrong rate. There's potential to do things in the building – it's not single-let. If the cap rate goes down, terrific, but it's not part of the underwriting we took at the time.

It's about this philosophy of buying things that in the long term will out and are not subject to the vagaries of the shifting sands of the market, such as topical secondary shopping centres."

For those who complain that there's a shortage of deals, Ritblat has a simple answer. "They aren't really paying attention. I think there's the occasional myopic view about how you look at the market and find things. In the last couple of years we've done north of 20 transactions off the market, involving a couple of billion of pounds of real estate," he says. "Part of that is that we're not a passive investor, we don't sit at our desks and wait for an agent to ring. We're on the front foot, going out, we're trying to create a story."

A current storyline involves the former Dickins & Jones flagship department store in London's Regent Street. Last summer, Delancey took a 30-year assignment of the lease after the House of Fraser decided that it couldn't operate profitably when landlord Legal & General upped the rent.

With partner Shearer Property Group, Delancey plans to rejig the 120,000 sq ft building as ground-floor shops with flats and offices above. "That deal was pretty much done away from the market," notes Ritblat. "Taking on the operating liability is an unusual way to get access to an asset, but a very smart one in my opinion, based on work we did before going in with our partners. Fundamentally what you have is a terrific piece of real estate in a prime area of London."

As the D&J deal illustrates, Delancey's direct investments are skewed towards central London, which Ritblat feels he knows best and has the best long-term economic fundamentals. However, nothing is ruled out and the investment style is best described as knowledgeable opportunism. So where did Ritblat acquire the skills? "It's in the blood," he jokes, adding more seriously: "it's practice and a terrific team of people.

Property is not an emotional experience for us. It is a commodity," he elaborates. "Of course we develop and build things, and I'm very happy to do that. But it is a business. We like things – a lot, but we're not in love with them. We're in the business of generating returns. That helps in the discipline."

The corollary of this unemotional approach to bricks and mortar is open-mindedness. Delancey is a very broad church of assets and activities, which includes providing mezzanine finance and investing in companies, private equity funds, joint ventures and partnerships. The latter group range from a property unit trust (Radcliffe), a developer specialising in town centre regeneration (Centros Miller), a car park operator (Delancey Britannia) to a central London retail fund (Metro Shopping, with Land Securities).

"A very large part of our business is partnerships," acknowledges Ritblat. "There are people who are better at doing something. If you can harness that expertise in a way that is equitable, both on the downside and upside, what would hold you back?"

Ritblat cut his teeth working on British Land's joint ventures with Scottish & Newcastle and Tesco. He detects that others in the property industry are overcoming their traditional reluctance to team up.

"Generally speaking, institutions have become more open and more willing to participate. The willingness to gear has helped, because it's evened out the playing field in part," he says.

Ritblat seems a bit flummoxed when he's asked where he wants to take Delancey. His normal fluency dries up for a moment. "We started out 11 years ago as a fund manager and have ended up at the same place," he muses, pointing out that the journey involved a series of iterations including a "flirtation with public listing.

We've found a place we're very comfortable with. One of the good aspects is that it ensures and provides quite a disciplined approach to investment," he says, warming to his theme. "We run funds that over time dispose of their investments. They're not aggregators of assets. I don't think we want to be in that business."

He'd rather keep Delancey trim and punching over its weight. "To know that we can access significant amounts of capital when we need to, without necessarily sitting on a significant amount of capital and feeling the pressure to do something with it. That is the worst of all worlds. There's a lot to be said for not doing very much occasionally," he says.

For now, though, it is more of the same. "We can continue to expand. Will it change or impair the way we do things?" he asks. "Probably, because it's very hard not to get bigger and lose a certain something. We're a very tight team, quite nimble, with access to large amounts of money without cluttering ourselves up with noise in the system."

One road Ritblat is not remotely tempted to take is a public one. While generally enthusiastic about the prospect of REITs ('a good thing for the industry'), he won't be turning Delancey into one. Having experienced life in the quoted sector, Ritblat is clearly irritated by its constraints, "whether it's as simple as saying if you buy an asset above a certain size, you have to go to get shareholder approval and call an EGM."

That said, Ritblat thinks that some of Delancey's investments and funds could end up in the public domain. "Some of those could make very good REITs potentially, or public vehicles. That would be a way to realize value for our investors and we might continue to run those when they were quoted, if REITs can be externally managed," he says.

Longer term, he says, the big question is whether to go European. "That's a very hard thing to judge and one of the fortunate things about the business we have is that we don't have to pre-judge that. We can make that decision in very short order, if the opportunity arises to do something that is suitable and worth the effort."

Jamie Ritblat served his apprenticeship at Morgan Grenfell Laurie in the last half of the1980s, "under the tutelage of Mr Bernerd," as he wryly puts it. "It was a terrific stable, with a pretty phenomenal group of kids." At MGL he worked on both development and investment, moving over to British Land in 1990. There, he went in to grow the investment portfolio. During this time he also worked on the Quantum Fund, British Land's joint venture with George Soros' family trust.

Five years later, Ritblat left BL to set up Freehold Portfolios, joined by one of his friends from Morgan Grenfell Laurie, Paul Goswell (also the son of a well-know property man, Brian Goswell of Healey & Baker). Soros invested in this venture. "We'd forged a relationship, so when I left that was an obvious port of call," says Ritblat.

The Soros connection came back into play when Freehold Portfolios reversed into Delancey in 1998, investing some £128m in the venture. "In 2001 we took Delancey private and basically reverted back to where we were, pulling management apart from the assets and carried on with that," says Ritblat.

IPF Investment Property Forum

Thursday 29 June 2006

The Grosvenor House
Park Lane, London W1

18:30 Pre-dinner drinks
19:30 Dinner
Black Tie

Guest speaker:
Comedian Dara O'Briain

Ticket Price £120.00 (inclusive of VAT)
per person (excluding wine and liqueurs)

Annual Dinner 2006

Dara O'Briain – hailed as the "**best guest host of Have I Got News For You?**", the most polished of the new generation of Irish comedians, he is a natural storyteller with an unusual ability to appeal to all ages and levels of audience.

Please reserve tables by completing a booking form and returning it with payment, as soon as possible. Tables will be for ten or twelve (limited availability).

Individual bookings can be made and, in this case, please indicate if you wish to join a table with specific people. All business associates and colleagues are welcome.

Please note that wine orders, hosted bars and special dietary requirements must be arranged directly with The Grosvenor House, contact details will be supplied on confirmation of your booking together with tickets and place cards.

For more information or to book, contact Jenny Hooper on 020 7194 7923 or email Jenny on jhooper@ipf.org.uk

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