

Private Wealth Management

Deutsche Bank

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Investment Outlook - Glanmore Property Fund

UK commercial property valuers rely heavily on transactional evidence to help them value assets. However, as most of the activity taking place in the market at the moment is forced sales, this has temporarily distorted the data and left valuers little option but to continue to mark down the sector.

The recent cuts in the Bank of England's base rate are very welcome, and many forecasters expect it to fall to 1% in the coming months. This will help relieve pressure on many existing property owners, possibly reducing the number of forced sales that have driven down valuations.

For property transactions to recommence it is crucial that the banks start lending again. This may not happen immediately, as many are still in the process of repairing their own balance sheets and will be extremely risk-averse in the short term.

It is important that the money markets reflect the recent interest rate cuts, and, with three-month LIBOR at around 2.4% (when the Bank of England base rate is 1.5%), there is still a significant risk premium being charged by inter-bank lenders.

Global real estate specialist Jones Lang LaSalle has suggested the moment when UK opportunity and vulture funds perceive value and move into the market "cannot be too far away" and that the turnaround thereafter could be "fairly quick". However, the Royal Institution of Chartered Surveyors believes "rising defaults and credit spreads will prevent a near-term recovery, resulting in a sluggish investment market" and that capital values will continue to fall through 2009 and 2010.

Broadly, in the absence of any regular transactions, we expect valuations generally to drift further downwards through the first half of 2009. Assuming that banks start to lend again and base rates remain below 2%, we believe there could be a stabilising of values and activity slowly picking up later in the year.



Retail and London office space

It is clear that we are facing a deep and protracted recession in the UK, and recent difficulties for well-known High Street names highlight the pressure this will put on retail businesses. This will affect all retail property owners to some extent, although the national multiple retailers will want to retain their prime locations despite the current gloom.

One other specific sector worth mentioning is City of London office space. The shrinkage in the financial services industry in particular means rental values are under pressure and vacancy rates are likely to increase, causing capital values in this sector to fall for some time.

The Glanmore Property Fund

Amid the challenges faced by the UK commercial property market, it is worth reminding ourselves that the Glanmore Property Fund is a well-diversified collective investment fund, which currently comprises 95 buildings spread across 72 different towns and cities in the UK. It is also diversified in terms of building use, including offices, warehousing, retail and leisure. We have always had a consistently high tenant occupancy rate – currently around 96%. We expect this to move down a little further as the recession bites and if we see any further high-profile casualties in the High Street.

One of the reasons why we have such strong occupancy levels is the diverse nature our tenants and tenancy agreements. In addition, more than 80% of our tenants have contracts with more than five years to run; a third of them have leases with more than 10 years unexpired. This should ensure the continuation of a solid rental income stream in the medium term, assuming there are no more unforeseen shocks to come from the UK economy.

John Raff MRICS IRRV

Cardales UK Limited, Property Adviser to the Glanmore Property Fund

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