

Is the Stick a Big Enough Carrot?



An Investor's View

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- What (else) can I get for my money?
 - Baseline investment – Risk Free Government Bond
- How much risk is there to my enjoyment of returns: how certain are my returns?
 - The higher the risk, the higher the Risk Premium, the lower the price
- How might the income from my investment change over time?
 - The greater the rate of increase over time, the higher the price
 - Markets rise and fall but all buildings depreciate

- Yield is the major pricing mechanism in the UK property market and links income and capital
 - Equals income received over capital expended
 - If yields change and income doesn't, then capital values change
- The Yield can be broken down into four elements, namely,
 - The Risk Free rate of return **plus**
 - The Risk Premium return **plus**
 - A rate of compensation for Depreciation **minus**
 - Payment for a rate of long run growth in market rents.
- If any of these factors change, the yield changes and (given income is essentially known), the capital value of an investment must change

- For assets that ‘score’ badly, it should:
 - Impact on the **liquidity** of assets, increasing opportunity costs and increasing the Risk Premium investors require
 - Impact on the **lettability** of assets, increasing uncertainties and void periods and increasing the Risk Premium investors require
 - **Lower the (future) rent payable** on the asset and thereby increase the Depreciation of that asset
 - **Increase the need to incur expenditure** and carry out retrospective works thus lowering net income flows to the investor
- Thus, there should be an upward movement on yields, and a related downward movement on prices.....
-but only if it is deemed ‘to matter’ .



- If owners and renters of property see sustainability issues as important and express this through their business preferences
 - This is beginning but still a long way to go
 - This should affect the price and performance of assets
- If others (Government, industry bodies, shareholders, activists, customers, etc.) make it matter, and can assemble information and evidence
 - Need for widespread, building-specific, environmental performance through which investment and occupational property portfolios can be reviewed, compared and ranked
- In these ways, the certificates will be a constant prompt through the operation of the market

- Pricing impacts will be greatest where ‘choice’ exists for the tenant and the investor
 - Impact greatest at the bottom of tenant and investment cycles
 - Probably greatest for offices and industrials :less so for retail
- Discounted Cash Flow dictates that this is a **current** rather than a future issue