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Henderson Think/UK Series: Can the Surge in Pricing be Maintained in 2010?

2010 expected to produce double digit returns, with performance to plateau in 2011

In its latest Think research report, Henderson examines prospects for the UK real estate market for the year ahead. Henderson expects to see All Property total returns edged into double figures. This will be driven by the current pressure on fund managers to acquire assets, extending the recent pricing rally in the short term. However, concerns linger as to whether the UK can successfully transcend the period of government-backed support to a self-sustaining and growing economy. As such, changing fundamentals including rising vacancy rates, falling rents and insolvencies, coupled with a rise in supply as sellers take advantage of market conditions, suggest that the pace of the current rally will not be sustained in the second half of the year and that pricing will plateau in 2011.

Banks will have an important role to play in the pricing of assets in 2010 and, while the market turnaround may bring forward planned disposals and a more hard line approach is expected for more poorly performing managers, Henderson does not expect to see a flood of assets brought to the market, especially not of the quality stock currently in demand.

A lack of stock is expected to affect the two-tier market that developed in late 2009, driven by huge demand for prime, well-let stock with long and secure income streams. This is likely to give way to a three or even four tier market given the scarcity of investment stock, depending on how far investors are tempted up the risk curve. There is already evidence of risk-taking on shorter lease income provided the product is of high quality and well located.

The more aggressively that prices correct in the short term, the greater the concern over whether the UK market will experience a pricing wobble, as investor confidence, sparked by the rebound in equity markets, wanes reflecting the underlying weakness of the UK economy. As such, the economic backdrop will become increasingly critical, especially if the UK experiences anything other than an orderly rise in interest rates and bond yields. The ability of the government, whoever is in parliament post general election, to address the burgeoning current account deficit and restore investor confidence will be pivotal.

Mike Keogh, Research Manager at Henderson said: *“Over 2010, UK All Property returns are likely to hit double figures in 2010, largely driven by a continued rally in the first half caused by lack of investor stock and the weight of money entering the market. Barring a serious relapse in economic confidence, we expect the UK market to experience a pause in the medium term positive yield correction from the end of 2010. This stabilisation in yields, or even slight fall in values across non prime assets where occupier threats have materialised, is likely to produce relatively modest returns in 2011.*

“The principle of timing and the quality and volume of assets available in the market over 2010 is therefore key. The medium term picture however, remains healthy, supported by an improvement in the underlying economic picture. As such, UK property remains a good buy, and buoyed by a higher income return, we expect the market to deliver an annualised 5 year return of 10% pa between 2010 and 2014.”

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About Henderson Property

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Henderson is a leading property asset manager with around £8.8 billion (as at 30 September 2009) of property funds under management across Europe, Asia and the US. The property team comprises over 180 staff based in offices across Europe, Asia and the US. The company has offices in London, Frankfurt, Milan, Paris, Amsterdam, Vienna, Luxembourg, Madrid and Singapore and Chicago. It also has additional asset management capabilities through a joint venture in Hamburg.

The property business manages pooled and segregated accounts which invest in properties offering core and value-added returns. In addition to investing across all commercial sectors, the property business also manages funds with sector specialist and/or regional themes. Henderson's property business includes a market-leading research capability. Twice yearly the in-house research team carries out analysis and forecasts for over 800 local markets across Europe.

About Henderson Global Investors

Established in 1934, Henderson Global Investors is a leading independent global asset management firm. The company provides its institutional, retail and high net-worth clients with access to skilled investment professionals representing a broad range of asset classes, including equities, fixed income, property and private equity. Headquartered in London, Henderson is one of Europe's largest investment managers, with £57.7 billion assets under management (as at 30 September 2009) and employs around 940 people worldwide.