Property – An Introduction

Property, like equities, is found forming part of many investments and savings, in that many life assurance and pension plans will have a proportion of their premiums invested by the life assurance company in commercial property. Property provides a return that is normally quite uncorrelated to the performance of stock markets and makes a good diversifier within a fund or portfolio.

Property for investment purposes is normally commercial property such as offices, shops, shopping centres, factories and industrial units. It is a highly specialised area of investment looked after by specialist property managers.

Investment in property should produce a long term hedge against inflation from growth in property prices. However, prices will not rise evenly and will have periods when they can fall. There are likely to be considerable differences in performance between different types of property such as offices and retail outlets as well as between regions of the UK. It is the managers job to position his fund to benefit from this.

The main purpose of investing in property is to benefit from the rental income. Managers will clearly try to obtain growth in rents. Their ability to do so will be affected by factors such as the rate of inflation and the state of the economy. The reinvestment or the payment of dividends from rental income will be the biggest source of return from a property fund.

The value of the properties will be based on the price investors are willing to pay for a given stream of rental income. There are times when that price will increase and times when it will fall. In selecting a property fund to invest in, one of the considerations is how much of the fund is invested in actual property and how much in the shares of property companies. It is also important to keep an eye on the amount of cash in a property fund. Too little and they may have difficulty in paying out investors quickly who want to take their money out. Too much and they will effect the performance of the fund as money on deposit does not earn rental income.

Real Estate Investment Trusts (REITS) and other closed ended property funds do not suffer from that problem as the shares and units are not bought from and sold to the fund’s mangers, but are traded on a stock market. They on the other hand, can have other issues to watch for, such as their share price being at a discount or premium to the value of the portfolio of properties and the level of borrowing the managers have taken on.

Common routes into property investments are through capital investment bonds, specialist property unit trusts, REITS, and, of course, pension plans. These avoid the problems of owning property directly, such as difficulty in taking out your money, taxation, obtaining tenants and managing the property. It should be noted that property may not always be readily saleable and under certain market conditions switches or encashment may need to be deferred for up to 6 months.

We consider property to be an important part of a portfolio properly diversified by asset type and, depending on market conditions, will normally feature in our recommendations. It is a normal part of The Nevis Fund portfolios.