INVESTING IN UK PROPERTY IN 2016

WHY FORTUNE FAVOURS THE WELL-INFORMED

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Britain's property market is facing some of the biggest changes it has seen in a decade, with a raft of new rules set to impact second home and buy-to-let buyers. Yet amid the overhaul, there are opportunities aplenty for astute investors.

This report sets out what you need to know to keep one step ahead of the changes – and how to make well informed property investment decisions in 2016.

Jonathan Hopper – Managing Director

There is already evidence of buying activity in the first quarter as both buy-to-let investors and second homebuyers rush to complete before April's Stamp Duty increase.

Thereafter the field will increasingly be left to the more sophisticated buyers or institutional investors who have the resources, expertise and ability to take the changes in their stride.

For investors who equip themselves with the right intelligent and advice, 2016 and beyond promise to offer great opportunity.

VIEW FROM THE FRONT LINE

British investors have long regarded residential property as not just the most tangible asset class, but also one of the most consistent.

2015 reinforced this popular appeal – with average house prices rising across the UK, and annual rates of price growth in hotspots like London, Oxford and Cambridge reaching double figures.

Hundreds of thousands of property investors have reaped the rewards of rising prices, and there has been a boom in buy-to-let investing. The government's latest Housing Survey revealed that in England alone, buy-to-let landlords own 4.4 million homes – enjoying not just capital appreciation but rental income too.

But the buy-to-let bandwagon could stop in its tracks in 2016. Major changes announced late last year by the government are already altering the shape of both the buy-to-let and second-home markets. They are summarised in the following table:

With as many as two million Britons now owning a buy-to-let property, the Bank of England is warning that the sector's size could "amplify" a housing boom or bust. These measures, announced in quick succession, have prompted some to see the government as being anti-buy-to-let.

Certainly buy-to-let investors will be hit much harder than buyers of second homes – for whom the changes are likely to be an awkward speed bump rather than a gamechanger.

But for the buy-to-let sector it will be a different matter. It's likely that many small investors, and especially those who are highly leveraged, will exit the market.

This in turn should create substantial opportunities for more sophisticated investors. With many tenanted properties likely to come up for sale just as competition from small landlords wanes conditions will be ripe for wealthier, less credit-reliant investors to increase their rental portfolio.

CHANGE	WHO WILL BE AFFECTED	TIME FRAME
3% increase in Stamp Duty on purchases of "additional residential properties"	Buyers of second homes or buy-to-let property	Effective 1st April 2016
Cut in tax relief on buy-to-let landlords' mortgage interest payments	Higher rate taxpayers who own a mortgaged buy-to-let property – the tax relief they can claim on their mortgage interest payments will be limited to 20%	Phased in from 2017 to 2020
Bank of England to be given broader powers to restrict buy-to-let mortgage lending	Buy-to-let buyers seeking a mortgage would face greater scrutiny of their finances, and lenders may be limited to lending less	Public consultation is due to complete in March 2016
Capital Gains Tax will have to be paid within 30 days of the sale of a residential property, down from the current window of up to 22 months	Those selling a property that is not their primary residence	Effective April 2019

BUY-TO-LET WINNERS & LOSERS

With buy-to-let landlords facing both a stamp duty levy, loss of mortgage interest tax relief and restrictions on mortgages in 2016, a series of alternative ownership structures is emerging to allow the financially astute to continue to enjoy the market's robust returns.

Buy-to-let property investors might be forgiven for feeling under siege following the government's most recent Autumn Statement.

Though the slew of measures impacting property investors was presented by the Chancellor as a "levelling of the playing field" between those buying a home and BTL buyers, the slashing of the tax relief landlords can claim on their mortgage interest payments is also astute politics.

For the Exchequer it will be both a substantial revenue raiser, and a tax grab on landlords for whom many voters may feel little sympathy.

Together with April's 3% hike in the Stamp Duty levied on buy-to-let properties, it will hit smaller, highly-leveraged landlords hard. The resulting reduction in yield, plus the looming prospect of a rise in interest rates, will force many amateur and highly-leveraged landlords to exit the market.

Would-be buy-to-let owners seeking a mortgage may also face tougher borrowing criteria following a public consultation on whether to give the Bank of England new powers to rein in lending.

But if smaller buy-to-let investors are the losers of this double-whammy of tax revisions and lending restrictions, more sophisticated investors could be big winners.

The exit of smaller BTL investors from the market will create an unprecedented opportunity for wealthier investors – as a spike in the supply of tenanted properties for sale coincides with less competition from inexperienced buyers.

Far from creating a rental crisis, this will allow institutional and sophisticated investors to step in and take up the slack left by smaller players forced out of the market.

Family offices and HNW investors are at the vanguard of this change, and are already using a range of ownership structures to limit their tax exposure, such as:

LIMITED COMPANIES – this is likely to become the new norm for sophisticated investors buying property. Properties held in a corporate vehicle will continue to benefit from full tax relief on mortgage interest payments and from 2017 enjoy lower rates of corporation tax.

PROPERTY SYNDICATES – these allow a group of investors to combine their funds to make a collective investment in property. Investors pay income tax on their net rental income, and CGT if the property is sold for a profit.

PROPERTY CROWDFUNDING – a new breed of crowdfunding platforms allows investors to buy shares in individual BTL properties. Shareholders get a portion of the rental income and can sell their stake if they want to realise the value of their asset. There is no Stamp Duty to pay when investing, but investors must pay income tax on the rental income, and CGT on any gain made when the property is sold.

The government is keen to get more owner-occupiers onto the housing ladder, and is doing so at the expense of the amateur buy-to-let sector.

So it's ironic that the moves it has unveiled to discourage smaller buy-to-let investors won't just create a gap for more sophisticated investors, they will also magnify their potential returns.

The Royal Institution of Chartered Surveyors predicts that over the next five years, rents will rise by an average of 5% a year – outpacing average price rises of 4.7% a year.

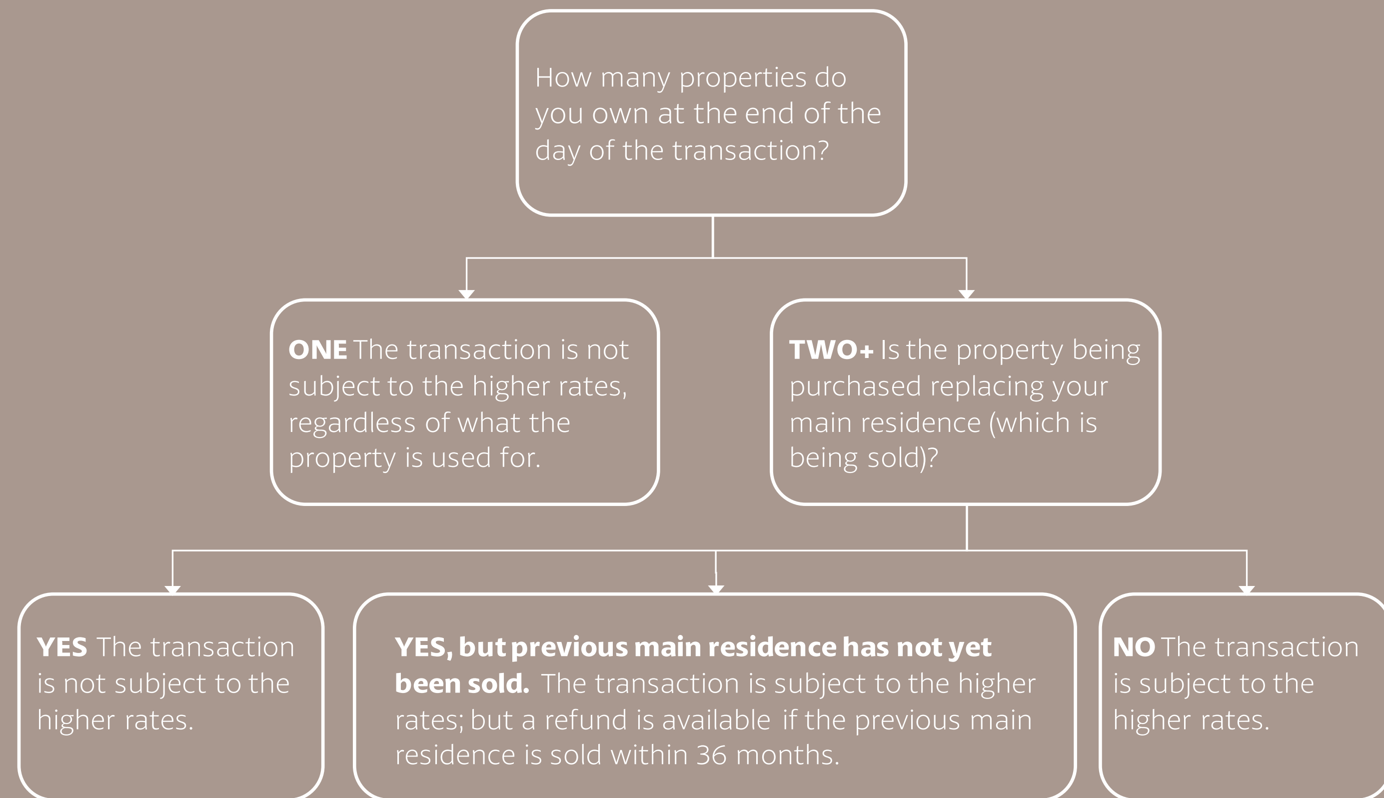
Against this backdrop, 2016 is likely to offer exceptional opportunities for astute buy-to-let investors. But the challenges posed by tax rises and lending restrictions will also raise the stakes for those making critical investment decisions.

So the need for first-class market intelligence and expert counsel is now greater than ever.

HM Revenue & Customs

HIGHER RATES OF STAMP DUTY LAND TAX (SDLT) ON PURCHASES OF ADDITIONAL RESIDENTIAL PROPERTIES

From the 1st April 2016 liability to pay a higher rate of SDLT will be determined as follows:



Source: HM Treasury

HIGHER RATE SDLT

New rates applying to additional residential properties purchased in England, Wales and Northern Ireland after 1 April 2016.

Band	Old	New
£0 – £125k	0%	3%*
£125k – £250k	2%	5%
£250k – £925k	5%	8%
£925 – £1.5m	10%	13%
£1.5m +	12%	15%

Source: HM Treasury

*From £40,000

HOW TO MAKE THE SECOND HOME SUMS ADD UP

With the potential for double-digit rental yields, strong capital growth and the promise of blissful family holidays, the dream of a second home is as compelling as ever - but April's stamp duty hike means the dream will come with a higher financial cost.

Whether it's a bolthole in the heart of the Cotswolds, a seaside cottage in Devon or a city pied-a-terre, there are certain boxes that prospective buyers always seek to tick when searching for that dream second home.

Location, character, transport links, length of tourist season and resale potential are all checklist staples, as is a good sense of community. Even a picture postcard cottage may lose its lustre if it's in a 'second-home ghetto' – an area that's deserted out of season because the locals have all been priced out.

But if buyers' individual wishlists are infinitely varied, their motivations are often similar - a complex cocktail of head and heart.

For most, the genesis of wanting a second home is often a holiday, or a stay in a friend's house, in an area that they fall in love with. That initial, emotion-led idea – "wouldn't it be nice to have a place here?" – is then layered over with more practical and financial considerations.

For the right property in the right location, the financial case can be strong.

Second homes in desirable areas – especially those with limited supply - can enjoy strong capital growth, well beyond the county average.

If you are willing to let out your second home while you're not staying there, the rental yields in the most desirable locations can run into double-digits – more than double what a typical buy-to-let property might earn.

But second home purchases are never driven by purely financial factors. The most fundamental question buyers ask themselves tends to be "is this somewhere I will want to come back to regularly for my holidays?"

Some buyers will happily sacrifice a degree of rental yield in order to secure the dream property. The overarching vision that most will have is of a peaceful retreat that will both be a venue for many happy holidays, and a legacy they can leave their children.

Following the shake-up in stamp duty at the end of 2014, many buyers looking for their ideal second home 'away from it all' changed strategy – either scaling down in size or by looking beyond the traditional favourite locations.

Buyers are increasingly weighing up second home hotspots – such as the Lake District, Devon, Cornwall, the Norfolk and Suffolk Coasts, West Wales and West Sussex – against the better value available in North Yorkshire, Cumbria and the Scottish Highlands.

Yet the challenge for those trying to stay ahead of the geographic curve is to identify which areas still have the potential to show disproportionate growth – in other words, where might the next 'Rick Stein effect' be?

The combination of greater competition for the best value second homes and the cost implications of this April's stamp duty increase – which will see the duty on second homes rise by a further 3% – mean it is more important than ever for buyers to use their head more than their heart.

In short, the stakes are now far too high to impulse buy following a sunny weekend away. Wise buyers appreciate the need for the right intelligence to make the right decision.

And remember, the time of the year when you buy can be important, too. The canniest buyers often seek to purchase their second home during the less popular winter months – before the sun causes prices to bloom as much as the roses in that dream summer garden.

MAPPING THE ROUTE TO RETURNS

Smart investors are adapting their buying strategies in response to the changing property landscape, where enticing returns still remain available – however, identifying the right opportunity, more than ever, requires the right market intelligence.

2015 was the year that the remorselessly rising prices of super-prime London property finally took a breather. The introduction of punitive levels of stamp duty and a collapse in oil prices caused the global super-rich to reassess their approach to Britain's most expensive property. In most cases, demand and prices both fell.

But for most of the UK property market, the only way was up. According to the Halifax, average prices rose by a brisk 9.5% during the year. The Royal Institution of Chartered Surveyors is predicting the momentum will continue into 2016, with average prices rising by a further 6% nationwide.

Such robust price growth alone is enough to make property an attractive investment, but with the first weeks of 2016 being marked by tumbling stock markets and an admission from the Bank of England that interest rates will stay at rock bottom levels for much of the year, at present neither equities nor cash look likely to match the perennial lure of property as an investment.

Property investors typically seek either capital growth or rental yield – or a combination of the two. Research and market intelligence from Garrington has identified the following areas as having the greatest potential in these three investment categories.

Best for capital growth

Forest Hill – As the steady tide of unaffordability extends out from Prime Central London and past traditional fallback areas such as Battersea and Clapham, attractive but more affordable places such as East Dulwich and nearby Forest Hill are reaping the benefits. These areas have good transport links to London Victoria and London Bridge,, and terraced houses can still be acquired from £550,000 to £750,000.

Alexandra Palace – A combination of both the forthcoming 'Crossrail 2' and 'London Help to Buy' means that this quiet but beautiful part of North London is likely be a hotspot for buyers in the middle of the next decade. The average price of a 2-bed flat within Alexandra Palace is £375,000 but this could easily double in 10 years. Affordable housing will make up more than 50% of new-build homes in postcode N22, attracting buyers to an area that's set to have a very short commute to central London.

Kingston Upon Thames – This area is very well established, but currently suffers from a relatively poor commute time to central London, therefore 'Crossrail 2' should greatly enhance this. In fact schooling and recreational facilities are already strong and the percentage of affordable housing is set to be above 50% for new-build homes. The average price of flats in postcode KT2 is still only £475,000.

Best for yield

Streatham – Streatham has traditionally been an overspill for areas like Balham, Clapham and Brixton, however its popularity has risen steadily and recently we have seen many people migrating to the area. Factor in widespread regeneration, the direct train links to London Bridge, and continued value for money compared to neighbouring areas – when both buying and renting – and the appeal is clear. Yields over 5% can be achieved here.

Royal Victoria Dock – This location has good transport connections, with the new Custom House Crossrail station and London City Airport both close by. As well as this, there is a development being built in the brownfield sites, which could achieve yields of more than 5%. The area could also see some exciting future developments, and there are plans for 'floating luxury houses', offices, watersports faciilities, a Lido and even an ice rink.

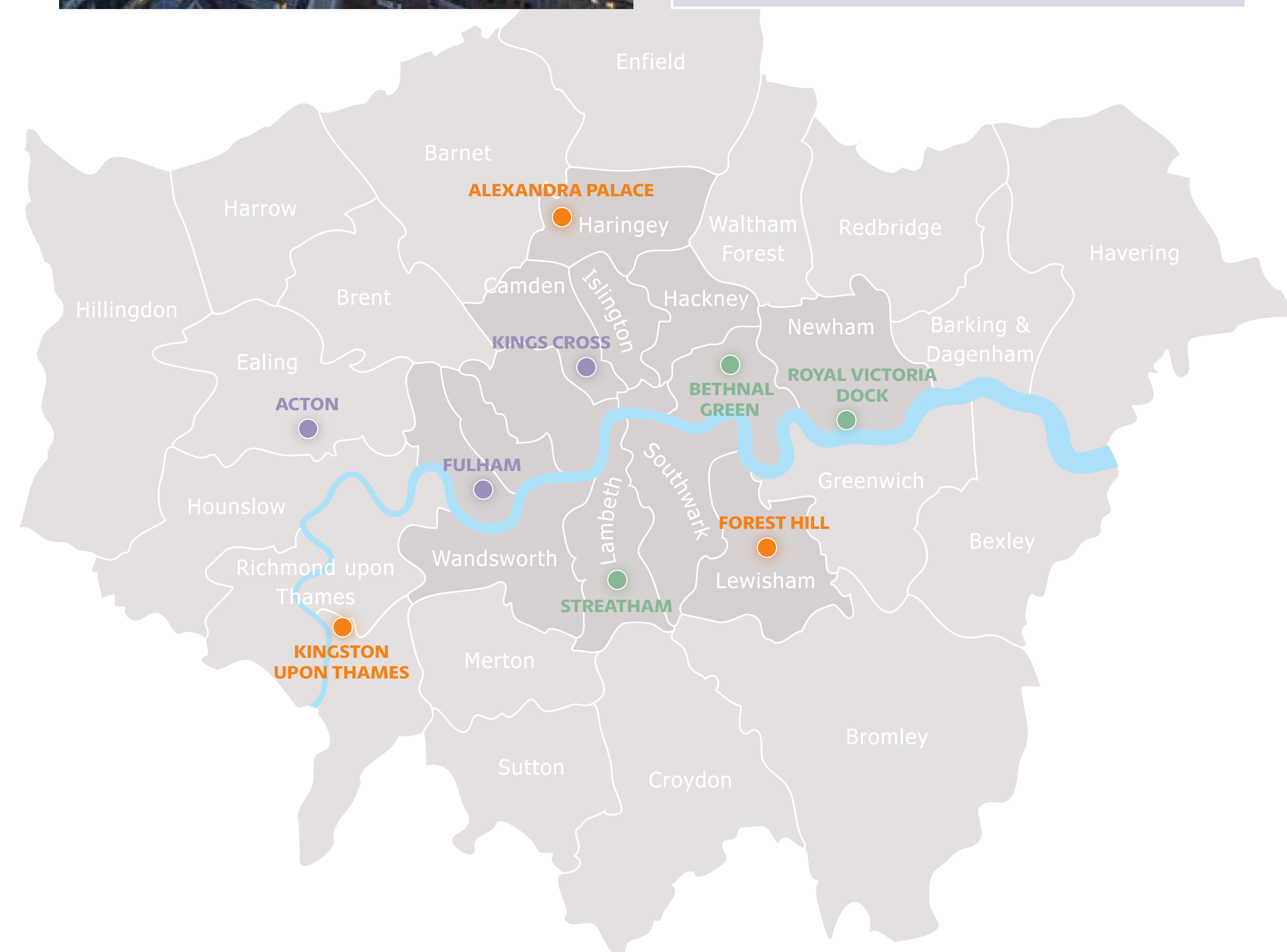
Bethnal Green – Bethnal Green is currently one of the few places in London to achieve approximately 5% in rental yields. The reason is that market values here are still quite low compared to Bethnal Green's more expensive neighbours. The demand for renting remains high as it is not far from the City, 2 stops from the Central Line to be precise, and is close to the green space of Victoria Park – attracting families across London. As well as this, there are three hospitals nearby, which greatly ensures that there is a steady flow of medical staff seeking accommodation.

Best for blended returns

Acton – While neighbouring areas benefit from 'Crossrail 1' (to become Elizabeth Line) may have peaked, Acton should continue to gain appeal, as it is the next station out from Paddington, and only two stops from Mayfair (Bond Street).

Fulham – A reliable location, both in terms of yield performance and capital uplift. The sheer density of houses will mean that there is a steady supply and the proximity to central London will ensure constant demand, particularly from those who cannot afford nearby locations.

Kings Cross – The new 67 acre development just north of the station will prove a Mecca for student buyers and tenants alike. There are superb transport links to across London and beyond, with the new development providing a new village in itself. The regeneration of this whole area will mean prices can only go one way in the long term. Some units in the new developments are already achieving £2,000 per square foot alone.



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