THE IMPACT OF INDEPENDENCE ON THE SCOTTISH PROPERTY MARKET

I should begin by providing a few credentials. I am Glasgow based but have a 35 year track record of working in the UK and Global property investment markets. Until 2005 I ran Aberdeen Asset Management’s property business, ultimately controlling £6bn of assets in the UK and Europe. I was president of the British Property Federation in 2004 and was instrumental in bringing the REIT structure to the UK.

I am now a director of various public and private companies in the UK and abroad: my website has more comprehensive information on my business – www.hunteradvisers.co.uk.

Throughout my career I have balanced living in Scotland with a job based in London or beyond. I thus have a unique perspective of the Scottish commercial property market, and have some very clear views as to what Independence would mean for investment values.

YIELDS

A starting point for property values is bond yields – so we need to address what would Government bond yields be in an independent Scotland? Small countries do not necessarily have high bond yields, but Scotland would begin its Independent life with high debts (taking its proportionate share of the UK’s debt) and will also be a largely oil based, and thus volatile, economy. That suggests to me that Scotland’s 10 year bond yield would be 1-2% above that of the UK – so I would estimate 4.5%, at current levels. Interestingly, subsequent to my coming up with this conclusion the National Institute of Economic and Social Research published an identical view.

If we accept the link between property yields and bond yields, Scottish property would need to yield 1.5% more than its English counterpart – not good news for valuations.

TRADE

Property performance is dependent on economic wellbeing. The Scottish economy currently exports around £11bn annually to the EU. However, it exports £45bn to the rest of the UK. It seems perverse to create fiscal, structural and possibly currency barriers between a country and its largest trading partner – but that will be a direct consequence of independence, with significant impact on the Scottish economy and its real estate market.

BREACH OF MANDATES

There are a number of compelling technical reasons why being outside the United Kingdom would have an immediate, and dramatic, impact on Scotland’s property investment market. First, most fund mandates are restricted to investment throughout the UK. The Republic of Ireland is excluded, and Scotland as an independent country would also automatically be excluded. As a consequence, fund
managers would be contractually obliged to exit their Scottish holdings over a short period, creating an investment vacuum and an inevitable steep fall in values.

RISK

Scottish property would fall into the “Overseas” category for London based Insurance and Pension Funds (the vast majority) and those who do have mandates to invest outside the UK would normally require a higher return to compensate for the higher risk of investing in a market with different tax and other fiscal arrangements and (possibly) a different currency. This would inevitably lead to higher yields and thus a fall in prices.

BENCHMARKING

Second, these same fund mandates are generally benchmarked against the Investment Property Databank. The main IPD index (£140bn, of which Scotland is 5.5%, or £7.7bn) covers only the UK and Scottish data will inevitably be excluded post Independence. There are various European indices which would incorporate Scotland. Investment managers tend to track closely the component parts of their benchmark, and when Scotland is excluded from the IPD UK Index, these managers will naturally wish to sell down their Scottish assets, and with few obvious replacement buyers investment values will plummet.

OCCUPATIONAL MARKETS

Moving to occupational markets, my inescapable view is that Scotland will lose a meaningful proportion of its office tenant base, with UK based businesses not wishing to be exposed to a different fiscal regime. I have heard it said that these occupiers will be replaced with more public sector occupiers, to replace Westminster functions. As a taxpayer, this prospect doesn’t fill me with cheer, and I also question whether this will stimulate development of high quality, high rent buildings.

CONCLUSIONS

Overall, for the reasons I have given, I think it is easy to demonstrate why Independence would have a dramatic negative impact on commercial property investment values. That this has not yet happened simply reflects optimism that Independence will not happen, and also a degree of heads in the sand over the impact.

Any of the above points can either be presented as a negative on Scotland departing the UK or a positive for Scotland remaining within the UK.

I would be happy to expand on these views, either in writing or in person.

David Hunter
January 2014