RIO Property posted a gain of 2.16% during the third quarter of the year. The investment is yet another RIO product which has performed above expectation, with net returns year to date of 6.23%. For those invested I am sure that is a welcome relief, as it's a far cry from the negative returns suffered by mainstream equity markets, many of which have seen severe losses in 2022. Many members have continually commented that this investment has performed very well relative to stock markets and mainstream investments.

It must be said, that despite economic headwinds gathering strength and speed throughout 2022, the RIO Property team have managed operations with skill and fortitude. I personally visited all four projects during July and can confirm that they are all firmly back on target. I would comment that the performance of the prime UK housing markets in the first nine months of the year has been nothing short of remarkable. Bolstering the positive result, our illustrious team has continued to deliver what can only be described as a herculean effort to overcome these issues and ensure that projects remain on schedule.

Looking forward, I do not foresee any disruptions to ongoing works at any of the sites, but with interest rates and the rising cost of living, a change of mood is beginning to brew in this market. And as always, RIO are well prepared, having correctly forecasted this change.

Residential Property

The new Chancellor announced a range of changes to SDLT to promote the Government's commitment to the housing market. The threshold from when SDLT becomes payable (England and Northern Ireland) has been doubled from £125,000 to £250,000 with immediate effect as of 23 September 2022.

The biggest beneficiaries of the stamp duty changes are likely to be first-time buyers, where the savings on offer will make their deposit requirements seem less daunting. But the counterbalance will be a combination of recent house price growth and current rate raises, so in short, the Government actions will not result in a surge of first-time buyer home-buying activity.

Even the maximum upfront stamp duty saving of £2,500 for other buyers is a drop in the ocean with the additional annual mortgage costs that have plagued this market from the beginning of the year. The cut is permanent, so unlikely to bring a repeat of the urgency that the property market experienced in the previous stamp duty holiday.

The changes are, I am sure, welcomed by those buying. But in the short term, my experience in the UK Property market would lead me to forecast that these announcements will not positively affect house price growth but are more likely to temper the effect of the broader economic headwinds facing the housing market.

One reason for my pessimism is that new buyers today already face a significant increase in interest rates. This will, in turn, limit the level of debt they are prepared to take on or be able to secure from their lender. That being so, I would not expect many potential buyers, particularly those reliant on high loans, to consider borrowing in this market. They will likely adopt a wait-and-see attitude, given the general levels of uncertainty in the mortgage markets. After that, a lot depends on the impact and

the extent to which policymakers and lenders seek to mitigate the potential impact of a sharp increase in interest rates.
Another influencing factor is the fact that during the last 12 months, residential construction costs have skyrocketed. Following years where cost inflation averaged between 1% and 2.5% pa, prices are now between 10% and 14% higher than they were only a year ago.

Both pandemic-driven supply chain issues and increasing energy costs are driving this and, as a result, have paused consideration of new developments. This is a positive as one of RIO's projects is now seeing an increased appetite because operational and nearly completed sites carry less risk.

Looking further forward, I predict that many property investment companies will remain on the sidelines, and this will likely remain the case until rates return to a more accessible level. As such, I fully expect to see a period of lower transaction levels during other periods of uncertainty in the housing market; this has certainly been the case in the past.

It is also clear that interest rate hikes will negatively impact the transaction levels, and considerable financial strain will be placed on existing borrowers, especially those who do not have a fixed rate deal and are on a variable rate. Banks and building societies will have little choice but to pass any bank base rate increase to their customers; although they may be keen to avoid a significant rise in repossessions, these will be on the rise without aid. The only saving would be action to offer full-scale mortgage holidays. Delaying capital repayments might be something some banks will consider as an example.

As for the Government, they are well aware of the negative effect the fortunes of the housing market have on consumer confidence. If their intervention in the energy markets is anything to go by, we might see the powers implementing time-limited measures to support homeowners during elevated interest rates, which would mitigate the impact on the market. Still, without such action, the property market will suffer. For this reason, this market is exposed to potential downside risks.

In conclusion, I am confident that we will see some downward pressure on prices and lower transaction levels during 2023. The first-time buyers and buy-to-let landlords are those most reliant on mortgage debt and thus will be negatively impacted. This will likely drive many in a difficult position to list their properties for sale and the additional properties coming on the market for sale, and mortgage defaults, will certainly add extra downward pressure on property values.

All of the above is an opportunity for property experts such as RIO; we are always ready and prepared. During August, I took steps to position RIO to be able to potentially capture prime distressed property, should it become available. Importantly RIO would only be buying at a substantial discount to the market value, that is, if and when the dominos fall.

William Gray
The RIO Club