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The Evolution of Property Investing

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Most history books agree that investing as we know it now kicked off in the 17th century, with the formation of the Amsterdam Stock Exchange in 1602. Others will argue that the invention of the investment market more rightly belongs to 16th century Antwerp's financial exchange system, or the futures markets of Medieval Britain and Renaissance Europe. Even Ancient Mesopotamia is said to have had a legal structure for investing.

The intrigues of the money markets pale by comparison to one of the oldest asset classes out there. Property was a source of wealth and trade far before we were minting coins and haggling over commodities. You could even say it started the rise of the rest.

Medieval Property Investors

Property was bought and traded centuries before the medieval period. The Roman Empire had well established property rights and strict ideas on how ownership could be transferred. But property investment as we know it today didn't emerge until the 14th and 15th centuries, where it took centre stage in Britain's developing commercial economy.

The feudal system introduced by William the Conqueror strictly regulated the transfer of land and meant that, prior to the 14th century, land ownership was the province of a very few lucky nobility and the church. But freeholders – lower gentry, craftsmen, clerics and merchants — were already starting to speculate at the lower end of the market and were beginning to successfully accumulate wealth.

In less than 100 years, this cohort became savvy property investors. In the 1380s, 14% of property transactions featured non-locals as either buyer or seller. Most interestingly of all, it was Londoners who made up the bulk of these out of town landlords, investing in the south of England, as well as Yorkshire and Northumberland. These properties ranged from small plots of land to entire manors.

But property investing wasn't limited to London and, by the early 1400s business partnerships or syndicates that brought property as a group rose in popularity to outnumber purchases by individuals or married couples. Towards the end of the 15th century, group investors began entering into either multiple partnerships or collectively bought more than one property[1]. Here we have portfolio diversification, and the beginnings of commercialisation of property in the UK. Not to mention the accumulation of wealth by a group that would dominate property ownership for the next 300 years.

Property and the Industrial Revolution

The Industrial Revolution of the late 18th and early 19th century shook up the investment markets globally. The invention of the steam engine and industrialisation also saw millions of people move from the countryside to the cities, abandoning the fields to seek work in the newly formed factories springing up in urban centers.

[1] Bell et al., 2019. Medieval Property Investors, Ca. 1300-1500. Available from: http://dx.doi.org/10.1017/eso.2018.92

For the first time in UK history, housing became a huge social issue. A limited number of dwellings within walking distance of the factories meant 'slums' were a common sight, with multiple families forced to share small and often run-down accommodation.

Property ownership was still limited to the gentry and upper classes, meaning ownership of land and capital were concentrated much as they had been in the 1400s. Now, with more workers than jobs and a desperate populous vying for space under every roof, the inequalities between the classes became more pronounced. Both commercial space and residential had never commanded such a premium, and property owners saw their income increase at pace.

Household budgets from this time show that there were only two groups with sufficient income to save, Landlords and Capitalists (those investing in trade and industry).

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The Growth of Home Ownership

Loans to buy property were not unheard of in the 12th century, although the structure and the obligations around the feudal system meant they were impractical and complicated. If a borrower or lender were to die before the debt was repaid, then the property was likely to be repossessed. As such, they fell out of favour in the 14th century and transactions were limited to cash-only buyers. It wasn't until the 1850s, with the emergence of the first building societies, that the concept of mortgages as we know them began to take shape[3]. Although at this point, borrowing money for property was still largely limited to the upper classes.

The end of the First World War and the 'Homes for Heroes' initiative sparked a social change towards homeownership in the working classes. By 1939, the number of people who owned their homes jumped to 27%, up from 10% in 1900.

The 1950s and 1960s was characterised by economic prosperity. Low interest rates and initiatives by the Tory government to reduce Stamp Duty, plus government lending to building societies to provide capital for mortgages saw home ownership jump from 29% in 1951 to 45% by 1964[3].

This established the underlying fundamentals of a long run, upwards trend in UK housing prices that stretched from 1955-1995. As incomes increased, people purchased more space. This not only pushed prices up as demand increased, but also made the supply of housing more difficult to predict and the market more volatile.

The 'Right to Buy' scheme introduced by Margert Thatcher in October 1980 gave council house occupants (the majority of UK tenants by this point) the option to purchase their home at a discount of 33-50%, with a guaranteed 100% mortgage. At its peak, nearly 250,000 homes were sold in just 12 months[4].

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This was the biggest shift in property ownership since the 1400s, when the freeholders banded together to buy property collectively and first established it as an asset class. Shifting attitudes and demand sparked four housing booms over

[2] Allen, 2005. Capital accumulation, technical change and the distribution of income during the British Industrial Revolution. Available from: http://www.ehs.org.uk/dotAsset/063f0b5e-0c2e-41b1-9492-5e24db75e861.pdf
[3] Henderson, 3017. The History of Mortgages in the UK. Available from: https://www.familymoney.co.uk/uk-mortgages/uk-mortgage-guide/history-mortgages-uk/
[4] Experience invest, 2017. History of UK Buy-to-Let. Available from: https://experienceinvest.com/history-of-uk-buy-to-let/

the next 40 years, in 1971-73, 1977-80, 1985-89, 1995-2007.

Deregulation of private rentals and shorter tenancies in the 1980s made buy-to-let a more enticing proposition for the everyday investor. Although slow to catch on, the sector grew steadily in prominence thanks to the introduction of Buy-to-Let mortgages in 1996. By 2013, buy-to-let mortgage lending had topped £20 billion a year and was growing YoY.

From 1950-1995, property market growth was been driven by income increases, low interest rates, government policy and limited borrowing criteria, which triggered an increase in demand and lack of supply.

But the property boom of 1995 to 2007 was the stuff dreams are made of. An expansion phase, characterised by rapid growth, low interest rates, and low unemployment, saw the value of the UK residential housing market grow by £3 trillion at its peak, making property the nation's biggest single asset.

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The 2008 global financial crash (GFC) put paid to that. UK housing values tumbled by -16.4% in just one year . As brutal as that sounds, the property market bore the brunt better than most. By December 2008, the FTSE had tumbled by -31.3% YoY and the Dow Jones fared even worse, charting -34% — its biggest loss since 1931[6].

The impact of the GFC and subsequent recession were wide reaching, but ultimately helped to boost the UK buy-to-let market long-term. Millennials, hit hard by lower wages, an increased cost of living and tighter lending criteria, formed 'Generation Rent'; a huge demographic of young renters who couldn't afford to buy. Increased demand in rental properties helped to buoy the buy-to-let investment market and sheltered investors to some degree from recent volatilities in property prices, with rents rising even as property values fall.

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Changes to tax and stamp duty by the current government, aimed at discouraging buy-to-let investors and freeing up stock for first-time buyers, has seen the volume of buy-to-let mortgages drop over the last two years.

A YoY fall in rental yields from 2015-2017 could also have played a part in discouraging would-be investors and encouraging established buy-to-let landlords to leave the market. However, rental yields are on the rise once again and averaged 5.9% in the last six months of 2018[7], the first time in four years that they have risen instead of falling.

In 2018, 59% of London-based landlords invested outside of the city. One trend that hasn't changed since 1380!

Property and Alternative Finance

The growth of the Alternative Finance (AltFi) sector was one of the most interesting changes to come out of 2008's GFC. High street lenders retrenched from 'high risk' loans to small business and lending criteria tightened.

At the same time, investors became disillusioned with traditional banking, a system whose failure to act responsibly was seen as the main cause of the crash. This environment nurtured the growth of crowdfunding and peer-to-peer (P2P)

[5] Halifax House Price Index. Data from 2005 – 2010.
[6] BBC, 2008. FTSE 100 index has its worse year.
[7] Pickford, 2019. Rising rents boost buy-to-let property yields. FT.

lending platforms, which enabled individuals to invest directly in small enterprise.

For property investors, this had two important outcomes. Firstly, it enabled investment in property beyond ownership, allowing individuals to invest in property development, for example, and share in the profit once a development was built and sold. Secondly, it allowed for participation in the market with very small amounts of capital for only the second time in history (the first being the 100% mortgages of the 1980s and early 1990s).

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By 2017, the UK online AlfFi industry had a market volume of £6.19 billion. While P2P business lending made up the largest segment of the market, property crowdfunding was the fastest growing. Investment volumes increased by 200% in 2017 to a total of £211m[8].

The Innovative Finance ISA

In April 2016, the government acknowledged the success of this market with the launch of the Innovative Finance ISA ('IFISA'), which allows savers to user their tax-free ISA wrapper to invest up to £20,000 a year in P2P lending or crowd bonds.

IFISAs are available across a number of different asset classes, with some providers offering property-based investment options. Returns vary between providers but can total 7.5% p.a.; the equivalent of 14% for a higher rate taxpayer[9]. Which is a higher than both buy-to-let rental and FSTE 100 yields for 2018[10].

The Evolution of Property Investment

UK Property investment over the centuries has been characterised by fast innovations that rocked the market, increased the number of people who could access it, and then settled down to become the status quo for hundreds of years.

From the introduction of the feudal system in the 12th century to the creation of property buying syndicates in the 14th, the accumulation of wealth by property owners during the Industrial Revolution to the introduction of mortgages in the 1850s. We've seen the pace of these innovations speed up, and the past three decades have given property investors more choice than ever; whether that's buy-to-let mortgages, crowdfunding property developments, or investing via IFISAs. Opportunities for UK property investors are materialising quicker than ever before, giving more and more people the chance to invest in a market that has outperformed equities over the last 15-years[11].

[8] Zeigler et al., 2018. The 5th UK Alternative Finance industry report. Available from: Cambridge Centre for Alternative Finance.
[9] Cogress in-house data, 2019.
[10] LSE, 2019. Data available from: https://www.londonstockexchange.com/exchange/prices-and-markets/stocks/indices/summary/summary-indices-chart.html?index=UKX
[11] Dan Woodruff, 2019. Available from: https://www.woodruff-fp.co.uk/property-vs-investment-portfolios/

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Total Investment Clarity