IPF Investment Property Forum

BPF BRITISH PROPERTY FEDERATION

RICS

INVESTMENT PROPERTY FORUM Educational Trust

Opening the Door to Property

Assessing the needs of small investors in property

Full report

September 2004

This research was jointly commissioned by the IPF, BPF and RICS

Opening the Door to Property

Research Findings

Working Paper One:
Market Sizing

Working Paper Two:
Individual Investor Profiles/Purchasing Behaviour

Working Paper Three:
Advisers to individual investors, pension funds and charities

Working Paper Four:
Small Pension Funds & Charities

Working Paper Five:
Commmercial Property Product Review & Evaluation

Working Paper Six:
Findings and Recommendations

September 2004

The IPF Educational Trust and IPF Joint Research Programme

The contribution from the IPF was funded under the auspices of the IPF Educational Trust and IPF Joint Research Programme.

The three-year programme supports the IPF's wider goals of enhancing the knowledge, understanding and efficiency of property as an investment class. The initiative provides the UK property investment market with the ability to deliver substantial, objective, and high quality analysis on a structured basis. It will enable the whole industry to engage with the other financial markets, the wider business community and government on a range of complementary issues.

The programme is funded by a cross-section of 16 businesses, representing key market participants. The IPF Educational Trust and the IPF gratefully acknowledge the contributing organisations:

Capital & Regional, Donaldsons, Grosvenor, GVA Grimley, Investment Property Databank, KPMG, LaSalle Investment Management, Land Securities, Lovells, Morley Fund Management, Nabarro Nathanson, Prudential Property Investment Managers, Quintain Estates & Development, Scottish Widows Investment Partnership, SJ Berwin and Strutt & Parker.

Opening the Door to Property Research Team

This research was undertaken by a joint research team from three companies.

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+ Experian Business Strategies
# Oxford Property Consultants

The research team was lead by Stephen Palmer of Seven Dials Consulting.

The IPF Project Steering Group

The IPF, BPF and RICS appointed a project steering group to guide and assist the research team. They gratefully acknowledges the contribution from:

Stuart Beevor – Chairman - (Grosvenor), Richard Auterac (Jones Lang LaSalle), Philip Ingman (SPREFS), Palmyra Kownack (BPF), and Charles Follows (IPF).

Preface

The Investment Property Forum (IPF), British Property Federation (BPF) and Royal Institution of Chartered Surveyors (RICS) commissioned this research to:

- Quantify the universe of smaller investors (defined as private individuals, Pensions Funds and Charities with total assets of less than £30 million),
- Determine the extent of their current exposure to commercial property,
- Assess the extent to which existing vehicles meet their needs, and
- To gauge the potential demand from these investors for tax transparent securitised real estate investment vehicles.

Background

Current equity market conditions and issues in the pension industry have combined to produce widespread interest from private investors in property as an investment. This interest has become manifest in several ways:

- There have been significant equity inflows into commercial property from private investors over the last two years. The commercial auction market in particular has seen a substantial increase in transaction levels. Also, private buyers are increasingly using Self Invested Pension Schemes (SIPPS) to acquire commercial property investments.
- The growing number of commercial property investment vehicles targeted on this market that have been brought forward by financial institutions and other product providers.

The industry is currently in dialogue with the HM Treasury concerning the introduction of a tax transparent REIT-like vehicle. A key tenet of the arguments being put forward is that such a vehicle would help alleviate some of the current problems in the pensions industry by meeting demand from smaller pension funds and private individuals for exposure to commercial property. Charities could also benefit from the stable income return and diversifying effects of investing in such vehicles.

However, this argument has been difficult to substantiate because little information is available in the public domain about the depth of the private investor market, current types of exposure and levels of investment in real estate, nor about the scale of latent demand for tax transparent securitised property vehicles amongst private investors, smaller pension funds, and charities.

Preface

Findings and Recommendations

This report comprises the full working papers for the project, and provide the detailed research findings.

The IPF, BPF and RICS congratulate the Research Team on an excellent project that lays the foundation for a deeper understanding of the needs of small investors in property. It provides an important contribution to the ongoing debate about the potential for a tax transparent investment vehicle in the UK.

The research shows that smaller investors are attracted to commercial property as an investment class. However, existing investment structures and vehicles do not offer smaller investors simple or tax efficient access to the commercial property investment market.

The Findings and Recommendations (Working Paper six) was submitted to HM Treasury in response to the consultation paper *Promoting More Flexible Investment in Property*.

The IPF, BPF and RICS invite comments on the findings and the recommendations for future research. Please address comments or suggestions to Charles Follows, Research Director, Investment Property Forum 3 Cadogan Gate, London SWIX 0AS. E-mail cfollows@ipf.org.uk; Telephone 020 7695 1649; Fax 020 7334 3872.

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Working Paper One

Market Size

This report summarises the findings of a desk-based research exercise to estimate the number of individual investors and the amount invested by individuals in terms of both pension and non-pension related savings.

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Brett Robinson

Assessing the Needs of Small Investors Research Team:

Andrew Baum#, Jane Fear#, Hannah Lord#, Stephen Palmer*, Brett Robinson*, Clive Shore+ and Adam Swash+

* Seven Dials Consulting
+ Experian Business Strategies
\# Oxford Property Consultants

1. Summary

This report documents the findings of research to estimate the quantum of individual investors and the value of their savings in both pension and non-pension forms, segmented by asset type.

Understanding the activities of individual investors requires assimilation of data from a variety of sources, which inevitably give rise to some overlaps and consequent uncertainty over accuracy. Despite these logistical challenges, we can describe in some detail the activities of UK individual investors in aggregate.

Investors save money in a variety of ways, utilising a range of product types:

- unit-trusts and OEICs
- life insurance savings products
- pensions
- direct shares
- direct property
- cash, including bank and building society deposits

Also, there are pools of money that are not covered by the above categories and where there is little data available. These include money invested offshore, direct private equity and venture capital, money invested in various tax saving schemes, such as film partnerships, and less mainstream investment assets such as art, wine and whisky.

1.1 Unit-trusts and OEICs

- There are an estimated 19.3m unit trust accounts, of which 8.3m are ISA accounts and 6.8m are PEP accounts. After adjusting for multiple account holdings, it is estimated that there are around 4.8m unit trust and OEIC investors.
- Net sales of unit trusts and OEICs to retail investors totalled £7.9bn in 2003, up from the previous year by £0.3bn. This is still substantially below net sales to retail investors of £17.7bn in 2000.
- The total value of invested assets owned by private investors is estimated at around £138bn at Feb 2004. Institutional investors own another £108 bn in unit trusts and OEICs, giving a total value of £246bn, which roughly equates to the size of the commercial property investment market.
- However, only a very small proportion (0.4%) of unit trust assets are property assets, reflecting the very small number of funds available. Over 80% of assets are estimated to be invested in equities.

1.2 Life products

- Life insurance products remain an important savings medium for many people in the UK. Over 732,000 single premium life insurance investment contracts were sold in 2003. Of these, 384,000 were unit-linked contracts, where the investor has some choice over where the funds are invested. In terms of premium value, £9.2 bn was invested in unit-linked contracts (excluding distribution bonds). Several major life insurers have seen rapid growth in their property funds as a significant amount of this premium income has been targeted at property funds.
- Desktop research indicates that there is approximately £62.4 bn in total invested in unit linked life funds. Around 13% of this is estimated to be in property funds.

1.3 Pensions

- Private pension provision is undergoing an important shift as employers move away from defined benefit schemes and take up defined contribution schemes. This analysis only covers assets invested in personal pension or defined contribution schemes, where the individual usually has discretion over the investment of the assets and bears the investment risk.
- Almost 950,000 new regular or single unit-linked premium pension contracts were written in 2003, with a premium value totalling £8.9bn.
- The total value of unit linked pension fund assets is estimated at £164bn, although this figure is subject to significant error owing to the existence of many closed and duplicate funds.
- Approximately 6% is estimated to be invested in property funds. The lower figure as compared to life funds reflects the equity culture that has been so prevalent in the UK.

1.4 Direct shares

- There is substantial private client wealth invested directly in shares and other securities. At the end of 2003, it is estimated that stockbrokers, banks and fund managers had some 4.8m private clients, although only 423,000 were discretionary portfolio management clients.
- Assets of private clients totalled £239 bn at the end of 2003, of which £142bn was in discretionary portfolios. It is significant that only a small proportion of these assets are invested in commercial property related securities. In large part this reflects the small size of the quoted property sector.
- Despite the limited overall exposure to property, there is clear indication of appetite for securitised vehicles. Private client brokers have played a significant role in placing funds for recent property trust offerings from, Standard Life and SWIP.

1.5 Direct property

- In addition to the investment activities analysed above, many investors have invested directly in either residential or commercial property.
- In the case of residential property, there are 408,000 buy-to-let loans outstanding, with a gross value of £39bn. Assuming an average LTV ratio of 50%, the equity invested in residential housing is around £40 bn, excluding investors' primary residences.
- Over the last three years, private individuals have been significant investors in commercial property via private treaty. Taking into consideration both purchases and sales of assets in the last three years, the total value of net investment has been £6.25bn.
- In 2003, £1.25bn was invested in commercial properties via auction room sales according to JLL/IPD ARAS figures. Over the last five years auction turnover has increased steadily, with a total of £4.7bn being invested over this period.
- Some private investors have also been investing in commercial property by investing in limited partnerships, syndicates and other unquoted vehicles marketed to high net worth clients. However, there is no readily available source of data on how much money is invested by individuals via these products.

Table 1: **Summary - Individual Investor Assets**

	Asset Value (end 2003 £bn)	% in Property	Property Asset Value (£bn)
Indirect Property Exposure			
Unit trusts & OEICS, of which	138	0.4%	0.6
- PEPs/ISAs	66		
Unit linked life funds	62	13.0%	8.1
Unit linked pension funds	164	6.0%	9.8
Direct share ownership	239	2.0%*	4.8
Total	603	3.9%	23.3
Direct Property Exposure			
Direct property, of which	51.0	100.0%	51.0
- buy-to-let residential	40.0	100.0%	40.0
- commercial acquired by private treaty	6.3	100.0%	6.3
- commercial acquired by auction	4.7	100.0%	4.7
Total Property Exposure			
Total, including direct property	**654.0**	**11.3%**	**74.2**

Sources: IMA, ABI, ONS, ComPeer, Standard & Poors, Lipper, CML, JLL/IPD, PropertyData
*estimate

However, there are real issues surrounding this level of direct investment in property by individual investors, who are often seeking to augment their pensions:

- *Risk concentration* - by acquiring a single asset investors are taking on disproportionate exposure to a single sector and usually to a single tenant.
- *Debt exposure* - in order to acquire these assets individuals are taking on debt, but there is widespread inexperience of the risks associated with doing so. Moreover, investors are attracted to direct property ownership by the relatively high income return, but through the need to pay interest on the debt, investors are placing much greater emphasis on receiving a capital return on sale of the asset.
- *Management* - few individual investors have the time and expertise to efficiently manage the property assets that they have acquired, and fewer still own a sufficient number of assets to achieve economies of scale that reduce costs.
- *Depreciation and obsolescence* - few individual investors are building these factors into their appraisals prior to acquisition.

The key question for the industry that requires further investigation centres on the reasons why so little is invested indirectly in property, particularly at a time when interest in investing in the asset class has never been higher amongst individual investors. This issue is addressed further by other workstreams in this project, but these are likely to be preliminary in nature and given its importance further exploration will be required.

1. Summary

Summary: Market Size

- The total value of invested in unit trusts and OEICs by private investors is circa £138bn, but only 0.4% is invested in property assets.
- There is circa £62.4bn invested in unit linked life funds and around 13% of this is estimated to be in property funds.
- Unit linked pension fund assets amount to £164bn, and circa 6% is invested in property funds.
- Private clients own £239bn of assets, but only a small proportion of these assets are invested in commercial property related securities.
- Private individuals have been significant direct investors in residential buy-to-let and to a lesser extent, commercial property. However, there is little appreciation by these often inexperienced investors of the risks that they are taking on.

2. Introduction

This report provides information on the savings activity of individuals. It covers money invested in unit trusts and OEICS and life and pensions products. It does not cover, except at aggregate level, money held by individuals in bank accounts or directly in commercial or residential property.

2.1 Scope and sources of data

The main sources of data are:

Association of British Insurers
Investment Management Association
National Statistics
ComPeer Ltd

2.2 Approach to sizing the market

We may think of an individual's savings spread across a number of distinct categories:

- **cash, including bank and building society accounts**
- **unit-trusts and OEICs**
- **life insurance savings products**
- **pensions**
- **direct shares**
- **direct property**
- **other**

An individual's pension assets may be rights from a defined benefit scheme, where the individual has no influence on the investment of the assets of the scheme. This analysis only covers assets invested in personal pension or defined contribution schemes, where the individual usually has discretion over the investment of the assets.

Subject to the comments in the preceding paragraph, this report analyses how many individuals invest in categories (excluding cash), how much is invested in aggregate and how much of the total is invested in commercial property. In addition, some data are provided on how much money is invested directly into property outside of home ownership.

Inevitably, there will be some overlap between the categories and some double counting; instances are highlighted where known. Also, there are some pools of money that are not covered by the above categories, where it is difficult to get data. These include money invested offshore, direct private equity and venture capital, money invested in various tax saving schemes, such as film partnerships, and less 'mainstream' investment assets such as art, wine and whisky. In the case of commercial property, there is also no readily available source of data on how money is invested indirectly by individuals via limited partnerships and other unquoted vehicles.

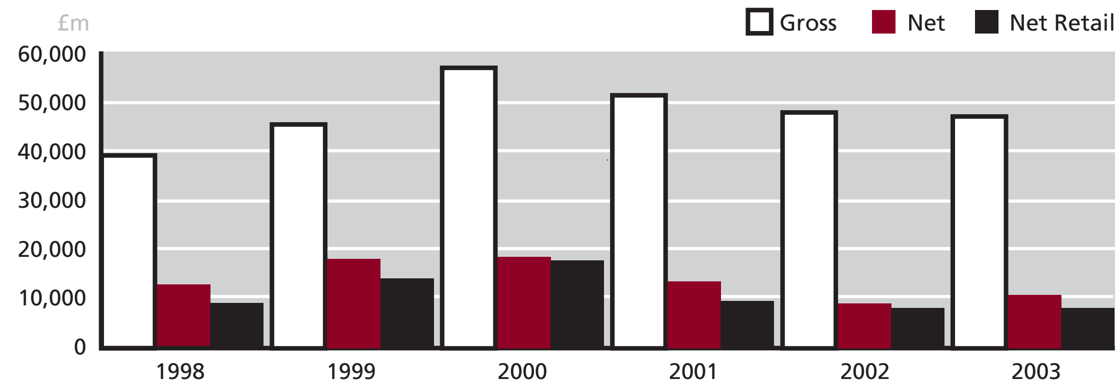
Whilst these exclusions detract from the completeness of the analysis, the activities of the vast majority of savers are included in the analysis and it is the activities of the general saving public that is of primary interest for this report.

3. Unit trusts and OEICs

All data on unit trusts and OEICS are sourced from the Investment Management Association unless otherwise stated. The data do not include unauthorised unit trusts.

Gross sales of unit trusts and OEICs have fallen over the last 3 years, to £46.9 bn in 2003. Net sales, calculated after deduction of redemptions, were £9.7 bn in 2003, up from £8.0 bn in 2002. Net retail sales, i.e. net sales to non-institutional investors, increased marginally in 2003 to £7.9 bn from £7.6 bn in 2002.

Chart 1: **Summary of Unit Trust & OEIC Sales**

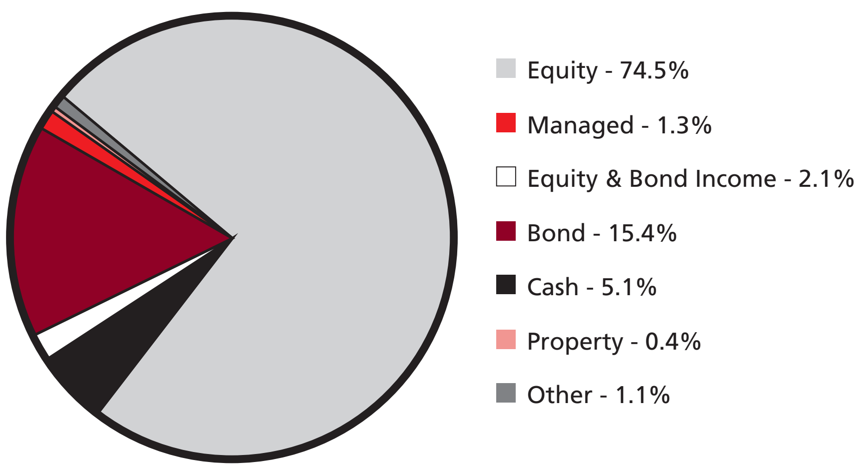


Source: IMA

3.1 Unit trust and OEIC assets

At the end of Feb 2004, the total amount invested in unit trusts and OEICs is estimated at £245.9 bn. In terms of the type of fund this was invested in, the split was as follows:

Chart 2: **Investment by fund category**



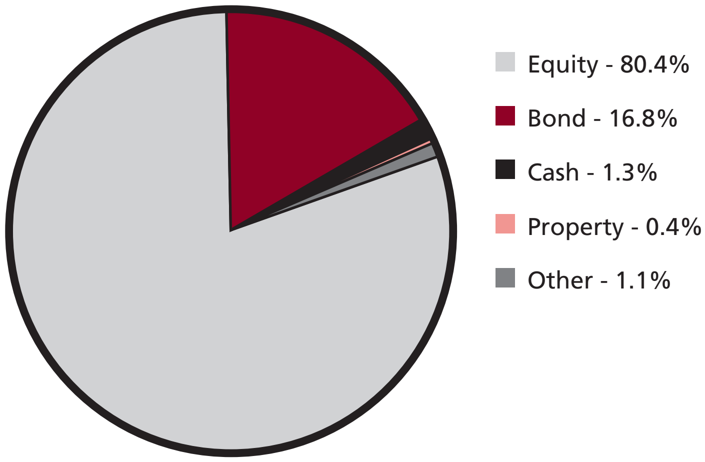
Source: IMA

3. Unit trusts and OEICs

Managed funds are those that invest in a mixture of equities, bonds and cash. (Institutional managed funds would also invest in property but few unit trust funds are able to and the amounts are immaterial for this analysis). If we make an assumption about the average asset allocation for each type of managed fund, then we can estimate the total aggregate asset allocation of unit trusts and OEICs.

After making adjustments for money invested in managed funds, it is estimated that 80.4% of the total assets was in equities, 16.8% in bonds, 1.3% in cash, 0.4% in property and 1.1% in other assets.

Chart 3: **Aggregate asset allocation**



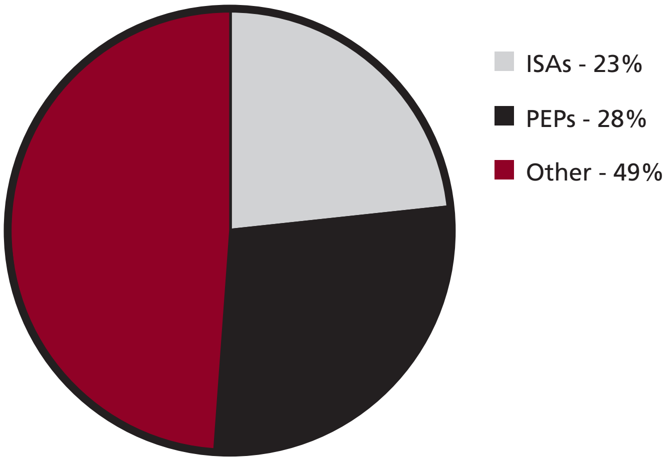
Source: IMA

Not all unit trusts and OEICs are owned by private investors. Institutional holdings of unit trusts and OEICS are estimated to total £108.2 bn, about 44% of the total, and 56% is in the hands of private investors. (Source: Office of National Statistics.)

Many private investors hold unit trusts and OEICs within PEPs and ISAs. Investment in ISAs totalled £28.7 bn and PEP investment totalled £38.2 bn, which together is about 51.1% of retail funds under management.

3. Unit trusts and OEICs

Chart 4: **Significance of PEPs and ISAs**



Source: IMA

3.2 Unit trust and OEIC investors

There are approximately 19.3 million unit trust and OEIC accounts, of which 8.2 million are ISA accounts and 6.8 million PEP accounts. It is estimated that an investor has on average 4 accounts, implying approximately 4.8 million unit trust and OEIC investors.

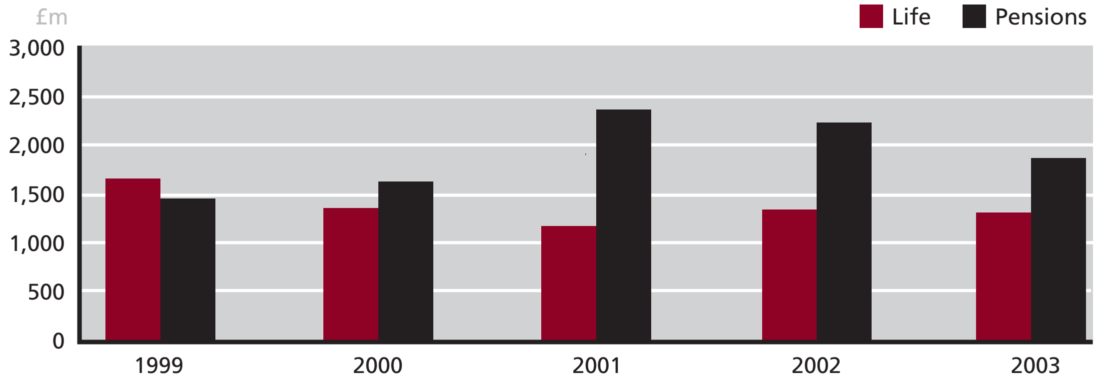
4. Life Insurance Business

Historically, a large proportion of mortgages were interest only and the mortgagor bought an endowment policy, with the expectation that the proceeds at maturity would pay off the outstanding loan. Sales of endowment policies have fallen dramatically but life insurance products are still used by many people for saving. For some investors there are tax advantages because up to 5% of the value of in investment can be withdrawn each year and treated as income for tax purposes.

All data on life insurance business has been sourced from the Association of British Insurers, of which all the major insurers are members, unless otherwise stated.

Life insurance business as a whole includes both life insurance and pension products. Only a life insurance company can sell a pension, although other types of company can manage or administer the assets. Life insurance savings products are either single premium or regular premium.

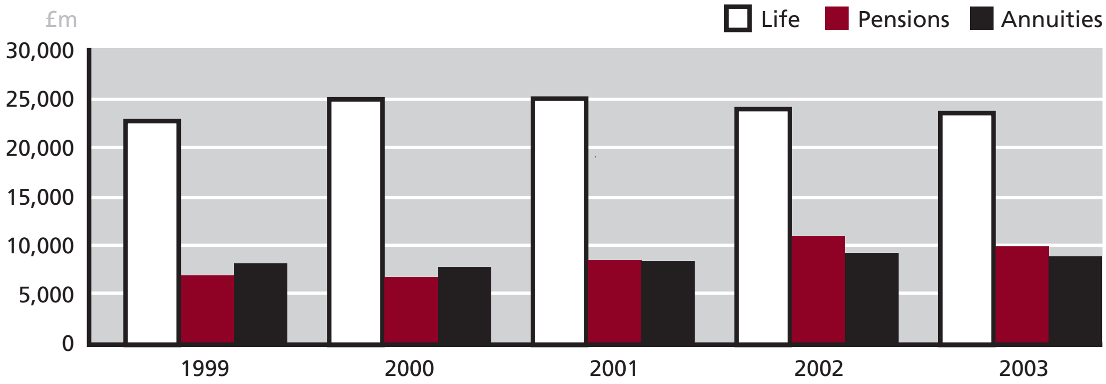
Chart 5: **New business: Individual regular premium**



Source: ABI

Single premium business is much larger in terms of amount invested.

Chart 6: **New business: Individual single premium**



Source: ABI

4. Life Insurance Business

4.1 Unit Linked Life Funds

In operation a unit linked fund is similar to a unit trust or OEIC: the units are priced and can be bought and sold. Legally, the position of the investor is different to that when investing in a unit trust. The investor has a contract with the insurance company, the value of which is linked to the underlying assets.

Many individuals make investments by buying what are technically life insurance contracts. Such contracts have tax advantages for some investors. These products are often referred to as investment bonds or life bonds, although they are not specifically related to fixed interest securities. The money invested in such products may flow into a with profits funds or more likely into unit-linked life funds.

It is important to realise that many of these products, which are discussed below, are referred to as Bonds of some sort, although they have no specific connection to fixed income securities.

Unit linked life fund investors

There were over 732,000 new investment-related single premium life insurance products sold in 2003. (This excludes annuities and unit trusts sold by life insurers.)

Table 2: **Sales of single premium life insurance investment products 2003**

Main investment catagories	No of contracts
Income & Growth Bonds	98,411
With Profit Bonds - Non-Linked	116,821
Guaranteed Equity Bonds	104,833
Unit-Linked Bonds	220,651
Distribution Bonds Linked	163,981
Other Insurance Bonds	27,306
Total number of new contracts	**732,003**

Source: ABI

Income & growth bonds are products whose payoffs are linked to the performance of some underlying financial assets or indexes, often manufactured through the use of derivatives. With-profit bonds are invested in the with-profits funds of life insurers. Guaranteed equity bonds offer fixed rates of return and are a form of fixed term deposit, wrapped up in a life insurance contract. Unit-linked bonds are invested in the unit-linked life funds of the product provider. Distribution bonds are a particular category of unit-linked bonds.

Of the above categories, only premiums for with-profit bonds, unit-linked bonds and distributions bonds are potentially invested in commercial property. In the case of with-profit bonds, the investor has no discretion over the investment of the assets. However, most long-term business funds, which are the funds that back with-profits bonds, include some allocation to property.

4. Life Insurance Business

Unit linked life fund assets

The amount of money invested in single premium life policies in 2003 totalled around £17.6 bn. Approximately £16 bn of this was attributable to the main categories described above.

Table 3: **Total investment in single premium life insurance investment products 2003**

Main investment catagories	£000s
Income & Growth Bonds	1,614,700
With Profit Bonds - Non-Linked	2,769,495
Guaranteed Equity Bonds	1,260,184
Unit-Linked Bonds	9,197,303
Distribution Bonds Linked	1,179,881
Other Insurance Bonds	49,235
Total number of new contracts	**16,070,798**

Source: ABI

The two categories of unit linked bonds made up over £10.6 bn in value, 64.5% of the total investment in the main product categories in 2003. Excluding Distribution bonds, unit linked bonds constituted 57% of the new single premium business in the main product categories. Where this amount is invested is at the discretion of the investor, i.e. he can choose which type of funds to invest in.

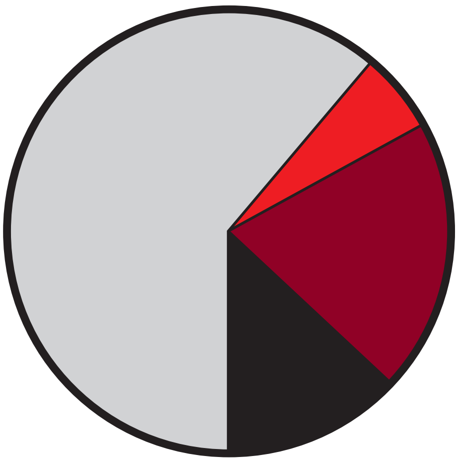
Unfortunately, there are no data available on which particular funds these premiums were invested in. However, estimates are given below for the allocation across the main asset categories of the aggregate total of all of the existing unit linked life funds.

The following estimates were derived by aggregating all of the individual unit linked life fund values listed in both Money Management and Investment Life & Pensions and taking the average. The original sources of the data in these magazines are Standard & Poor's and Lipper, respectively. There is inevitably some double counting in the aggregation.

The total value of investments in unit linked life funds is estimated at £62.4bn as February 2004. Unlike unit trusts and OEICs, a meaningful proportion of this is invested in property funds.

4. Life Insurance Business

Chart 7: **Unit linked life funds aggregate asset allocation (Feb 2004)**



Source: Money Management, Investment Life & Pensions, Seven Dials Consulting

4.2 Unit linked pension funds

Personal pension schemes are invested in unit-linked pension funds. Many new employer sponsored pension schemes are defined contribution schemes, in which the amount of contribution from the employer is determined rather than the pension at retirement. Money contributed into such schemes will flow into unit-linked pension funds.

Unit linked pension fund investors

Unlike life insurance investment products, there is a substantial amount of regular premium pension investment. This is to be expected given the long-term nature of pension saving.

Table 3: **Sales of regular premium pension products 2003**

Product	No of Contracts
Personal pensions	87,670
Stakeholder	199,923
SIPPs	196
FSAVCs	1,983
Group personal pensions	294,213
Employer sponsored stakeholders	253,813
Executive pension plans	18,554
SSASs	696

Source: ABI

Definitions: **SIPP:** Self Invested Personal Pension
FSAVC: Free Standing Additional Voluntary Contribution
SSAS: Small Self Administered Scheme

4. Life Insurance Business

The important message from this table and the one below is the quantity of premium pension contracts sold in 2003. The particular form of pension contract is not crucial for this analysis.

Table 4: **Sales of single premium pension products 2003**

Product	No of Contracts
Personal pensions	121,640
Stakeholder	84,458
SIPPs	6,265
FSAVCs	1,869
Group personal pensions	92,488
Employer sponsored stakeholders	21,335
Executive pension plans	11,357
SSASs	3,880

Source: ABI

Not all of these policies are unit-linked policies. In each category some of the contracts are based on with-profits funds and some are 'non-linked'. It is only unit linked policies where the investor has the possibility of electing where the money is invested.

Table 5: **Sales of unit linked regular premium pension products 2003**

Product	No of Contracts
Personal pensions	52,933
Stakeholder	158,900
SIPPs	196
FSAVCs	1,689
Group personal pensions	234,771
Employer sponsored stakeholders	221,983
Executive pension plans	16,822
SSASs	696

Source: ABI

Table 6: **Sales of unit linked single premium pension products 2003**

Product	No of Contracts
Personal pensions	52,933
Stakeholder	158,900
SIPPs	196
FSAVCs	1,689
Group personal pensions	234,771
Employer sponsored stakeholders	221,983
Executive pension plans	16,822
SSASs	696

Source: ABI

Unit linked contracts make up the majority of new contracts in every product category.

Unit linked pension fund assets

For regular premium contracts, the largest product category is Group personal pensions.

Table 7: **Value of unit linked regular premium pension products 2003**

Product	£000s
Personal pensions	182,115
Stakeholder	252,439
SIPPs	2,136
FSAVCs	6,904
Group personal pensions	532,412
Employer sponsored stakeholders	275,004
Executive pension plans	131,546
SSASs	12,043

Source: ABI

For single premium contracts, Personal pensions attract by far the largest investment total value.

Table 8: **Value of unit linked single premium pension products 2003**

Product	£000s
Personal pensions	4,349,125
Stakeholder	1,598,094
SIPPs	814,978
FSAVCs	16,358
Group personal pensions	655,741
Employer sponsored stakeholders	205,309
Executive pension plans	576,688
SSASs	244,166

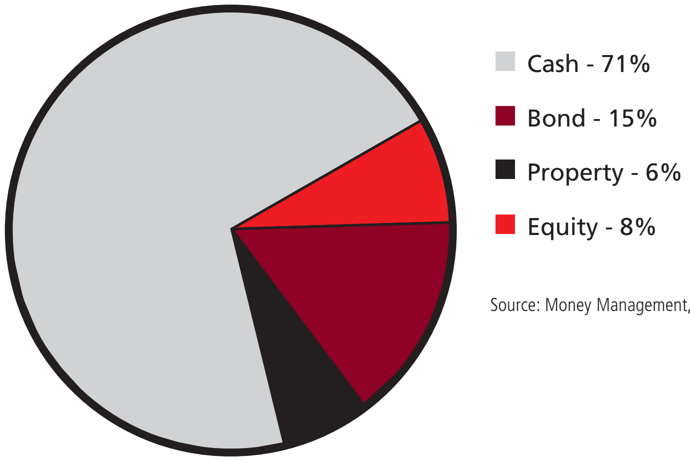
Source: ABI

As with linked life funds, there is no readily available data on which types of fund these premiums are being invested into. Once again we estimate the asset allocation of the aggregate total of all unit linked pension funds. The estimates were derived by aggregating all of the individual unit linked life fund values listed in both Money Management and Investment Life & Pensions and taking the average. The original sources of the data in these magazines are Standard & Poor's and Lipper, respectively.

The total value of unit linked pension funds is estimated at £125 bn from the Money Management data and £202 bn from the Investment Life & Pensions data. The large difference is troubling. It seems that there are a lot of closed funds that no longer accept new money. Some sources list these and some do not. In addition, some funds are duplicates of other funds with different names, e.g. XYZ Pension Equity Series 1 and XYZ Pension Equity Series 2 have different charging structures but the same underlying assets. Taking the average of the two estimated total values, gives total assets of £164bn.

4. Life Insurance Business

Chart 8: **Unit linked pension funds aggregate asset allocation (Feb 2004)**



Source: Money Management, Investment Life & Pensions, Seven Dials Consulting

In aggregate, unit linked pension funds are estimated to have 6% exposure to property. This is somewhat lower than the estimate for unit linked life funds at 13%.

5. Direct Share Ownership

The data in this section is taken from a report prepared by ComPeer Ltd based on its Private Client Stockbroking and Fund Management Survey unless otherwise stated.

This section describes the size of the market for dealing and fund management services to private clients. These services are provide by stockbrokers, clearing banks, building societies, specialist dealing firms, fund managers and private banks. Referring to the group as a whole as 'stockbrokers and fund managers', their clients may be classified as follows:

- Execution only
- Advisory dealing
- Advisory portfolio
- Discretionary

Execution only means that the client only trades through the stockbroker. Advisory dealing means that the client takes advice on his dealing and advisory portfolio means that the manager consults the client on dealing decisions but controls the overall portfolio. Discretionary means that the firm has discretionary control over the portfolio.

Table 9: **Number of private clients by type**

Client type '000s	2001	2002	2003
Execution only	3966	3690	3848
Advisory dealing	130	132	118
Advisory portfolio	401	346	337
Discretionary	429	452	423
Total	4926	4620	4726

Source: ComPeer

Assets of private clients of stockbrokers and fund managers

The total value of private client assets managed by UK based stockbrokers and fund managers, or managed by clients themselves through UK stockbrokers, is estimated at £239 bn as at the end of 2003. This is 9% up on 2002, mainly because of rises in share prices.

Table 10: **Assets held by private clients**

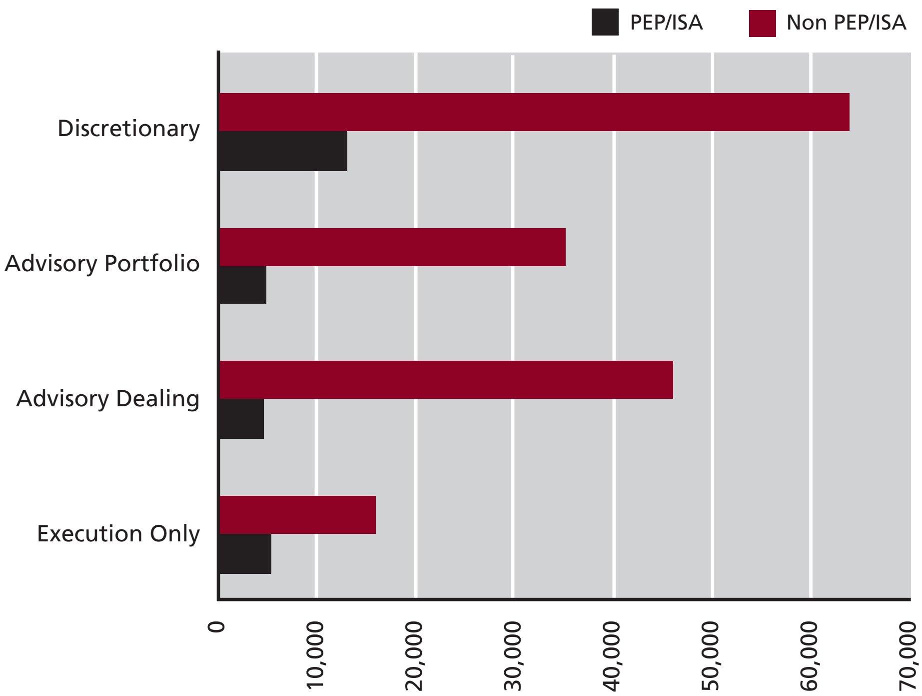
Client type '000s	2001	2002	2003
Execution only	42	34.8	41.6
Advisory dealing	17.7	13.2	10.8
Advisory portfolio	65	45.8	45
Discretionary	145.5	125.3	141.6
Total, £bn	270.2	219.1	239

Source: ComPeer

5. Direct Share Ownership

Some of these funds are held in PEPs or ISAs. The following table shows the relative importance of PEP/ISA money, based on the total funds excluding funds held in clients' own custody.

Chart 9: **Assets held by private clients by fund type**



Source: ComPeer

The data show that the PEP and ISA investments are a modest part of the total value of assets held by private clients. This is not surprising given the wealth profile of this group of investors.

Although no data are available on the breakdown of private client assets by investment type, the amount invested in commercial property related securities is inevitably very low, given the capitalisation of the quoted property sector even after allowing for the recent property investment trusts launched by Scottish Widows, ISIS and Standard Life.

6. Direct Property

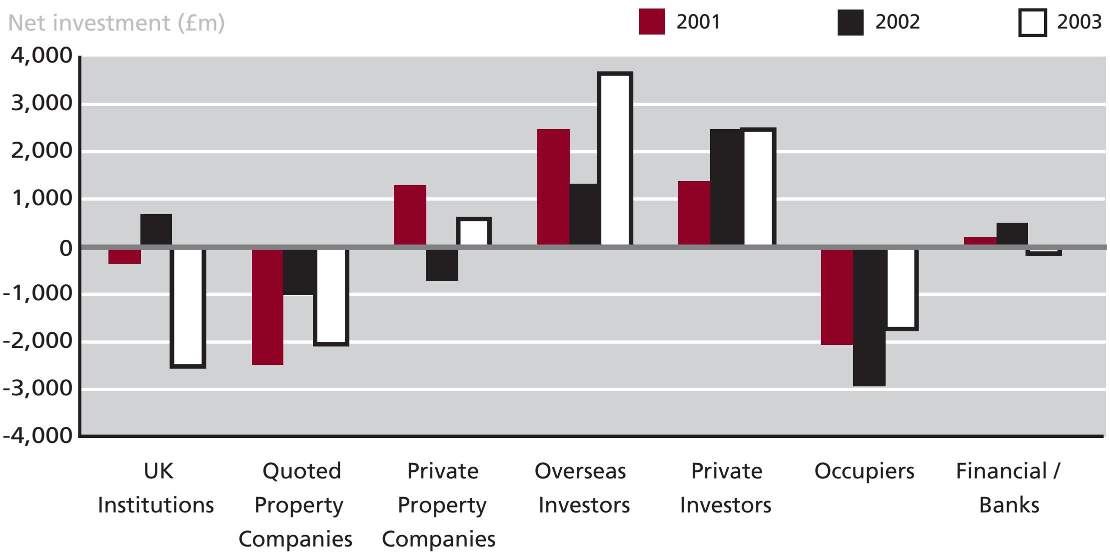
In addition to the investment activities analysed above, many investors have invested directly in either commercial or residential property. Although the available data is incomplete, the following analysis bears testimony to the considerable and growing appetite amongst small investors for exposure to real estate. Three different types of investment are considered:

- Private treaty
- Auctions
- Buy-to-let

6.1 Private treaty

Over the last three years, private individuals have been significant direct investors in commercial property. Private investors - as defined by PropertyData - acquired £3.26bn of commercial property assets via private treaty in 2003 and sold £800m. Taking into consideration both purchases and sales of assets in the last three years, the total value of net investment has been £6.25bn. The chart overleaf shows that alongside overseas investors, private buyers have been a dominant force in the market over the last three years as institutions and quoted property companies have been net sellers.

Chart 10: **Net investment by types of investor**



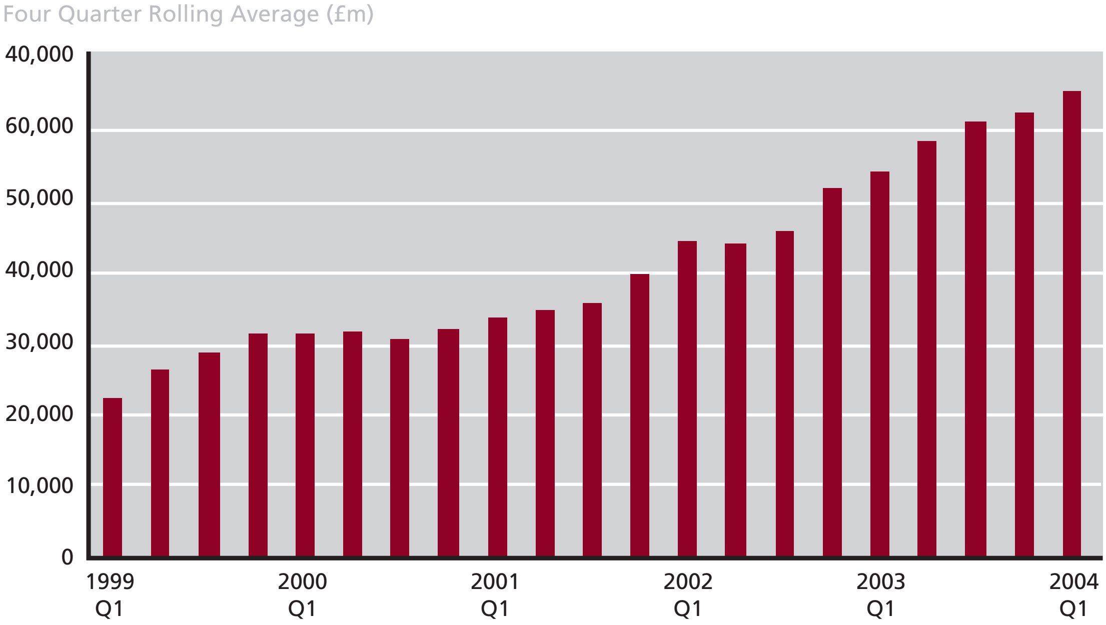
Source: PropertyData

6.2 Auctions

According to JLL/IPD ARAS figures, £1.25bn was invested in commercial properties via auction room sales in 2003. Over the last five years auction room turnover has increased steadily, with a total of £4.7bn being invested over this period.

6. Direct Property

Chart 10: **Auction Room Turnover**

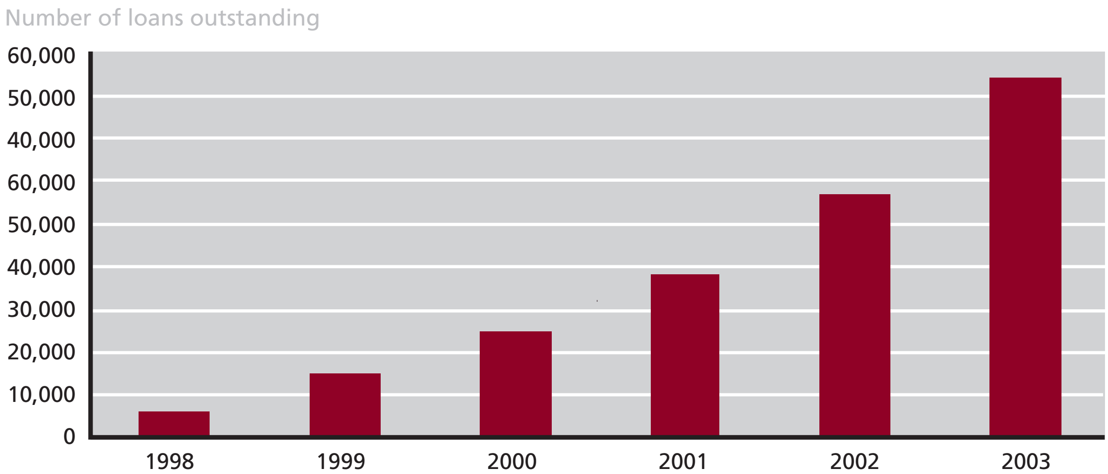


Source: Jones Lang LaSalle/IPD ARAS

6.3 Buy-to-let

There are approximately 408,000 buy-to-let loans outstanding, with a gross value of £39 bn. at the end of 2003. Some 178,000 new loans were made in 2003, and the average loan amount was £103,000. Assuming an average LTV ratio of 50%, the equity invested in residential housing, excluding people's primary home, is around £40 bn. Clearly, this estimate excludes outright ownership of buy-to-let properties.

Chart 11: **Buy-to-let loans**



Source: Council of Mortgage Lenders

In addition to these forms of investment, individuals are investing in property through syndicates and limited partnership vehicles.

7. Conclusion

The value of investment assets owned by individuals is substantial, but only a relatively small proportion is invested in real estate. Assets owned by individual investors, excluding direct property, amounts to an estimated £603bn, almost twice the size of the commercial property investment market. However, most of these assets are investments in equities and just £23.3bn., or 3.9%, is invested indirectly in property assets.

Summary: **Individual Investor Assets**

	Asset Value (end 2003 £bn)	% in Property	Property Asset Value (£bn)
Indirect Property Exposure			
Unit trusts & OEICS, of which	138	0.4%	0.6
- PEPs/ISAs	66		
Unit linked life funds	62	13.0%	8.1
Unit linked pension funds	164	6.0%	9.8
Direct share ownership	239	2.0%*	4.8
Total	603	3.9%	23.3
Direct Property Exposure			
Direct property, of which	51.0	100.0%	51.0
- buy-to-let residential	40.0	100.0%	40.0
- commercial acquired by private treaty	6.3	100.0%	6.3
- commercial acquired by auction	4.7	100.0%	4.7
Total Property Exposure			
Total, including direct property	**654.0**	**11.3%**	**74.2**

Sources: IMA, ABI, ONS, ComPeer, Standard & Poors, Lipper, CML, JLL/IPD, PropertyData

*estimate

Over the last few years, considerable interest has been shown by individual investors in commercial property, and this is borne out by the considerable volumes of direct investment in residential but-to-let and commercial property both through private treaty and at auction. Together, these routes into direct ownership amount to £51bn, which equates to 8.1% of the total assets owned by individual investors.

7. Conclusion

However, there are real issues surrounding this level of direct investment by individual investors, who are often seeking to augment their pensions:

- *Risk concentration* - by acquiring a single asset investors are taking on disproportionate exposure to a single sector and usually to a single tenant
- *Debt exposure* - in order to acquire these assets individuals are taking on debt, but there is widespread inexperience of the risks associated with doing so. Moreover, investors are attracted to direct property ownership by the relatively high income return, but through the need to pay interest on the debt, investors are placing much greater emphasis on receiving a capital return on sale of the asset.
- *Management* - few individual investors have the time and expertise to efficiently manage the property assets that they have acquired, and fewer still own a sufficient number of assets to achieve economies of scale that reduce costs.
- *Depreciation and obsolescence* - few individual investors are building these factors into their appraisals prior to acquisition.

The key question for the industry that requires further investigation centres on the reasons why so little is invested indirectly in property, particularly at a time when interest in investing in the asset class has never been higher amongst individual investors. This issue is addressed further by other workstreams in this project, but these are likely to be preliminary in nature and given its importance further exploration will be required.

Working Paper Two

Individual Investor Profiles/Purchasing Behaviour

This report summarises the findings of quantitative and qualitative analysis of the investment behaviours of small investors. It draws on consumer surveys undertaken by MORI and estimates the total number of investors placing funds. It provides information on the profile of these investors and the strategies they employ to buy investment products. Drawing on these findings, estimates are made of the potential market for new retail commercial property funds.

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1. Summary

This report documents research to estimate the total number of individual investors, to profile these investors and the strategies they employ to buy investment products. It also provides insights on the attitudes of individuals to investing in commercial property. This involved three principal strands of work:

- Analysis of 46,000 interviews conducted for the MORI Financial Tracking Survey (FTS) during 2003, with people selected according to their demographics to ensure a representative sample is surveyed.
- Analysis of a MORI survey conducted on behalf of the BPF and CB Richard Ellis in December 2003, plus two additional questions that were inserted into MORI's wider omnibus survey of 2,000 people in April 2004.
- Three focus groups comprising active investors, aimed at gathering information on the investment strategies of smaller investors and their objectives and attitudes to commercial property investment.

The research undertaken during this workstream has provided three main benefits:

- An overview of personal investment penetration and behaviours in the UK, including a better understanding of the active investor population;
- Insights into the attitudes of small investors to commercial property investments and PIFs;
- A segmentation approach, which will help companies target select groups with differing commercial property investment products.

1.1 Market Overview

One of the key tasks was to estimate the size of the overall active investor market, as this is one measure of the number of people who may be interested in investing in commercial property and PIFs. We defined active investors as shareholders who held more than simply mutualisation or privatisation shares plus equity ISA, OEIC, unit trust and investment trust holders.

According to the MORI FTS survey, 43% of people surveyed had at least one investment product. Using Experian's Financial Strategy Segmentation (FSS) approach, we assessed the propensity to purchase investment products for each of the 31 specific FSS Types. It was clear that 17 of the 31 FSS Types are much more likely to purchase investment products compared with the wider population. Penetration indices of at least 50% above the national average are common.

The 17 FSS Types with the highest purchasing propensities were segmented into three groups, based on their anticipated risk appetite and investment strategies (eg growth vs income). This segmentation was intuitive and should be tested and refined as necessary by further market research.

Market size estimates for each of the three groupings were then made by comparing the investment penetration per product for each FSS Type with the number of adults in the UK of that Type. The results are shown in Table 1 below:

1. Summary

Table 1: **Estimated Size of the Active Investor Market**

Investment Group	Description	Estimated Market Size
Higher Risk Appetite	Sophisticated investors; More likely to be interested in property from a growth perspective and to have relatively high-risk threshold	1.8m – 2.1m
Medium Risk Appetite	Wealthy individuals, moderately attracted to property, with a mix of growth and income objectives	2.0m - 2.25m
Lower Risk Appetite	Investors attracted to regular savings schemes, who may be interested in commercial property from an income perspective. Relatively low risk threshold	2.75m – 3.0m
Total		**6.55 - 7.35**

Overall, this gives an estimated UK active investor market population of between 6.55m and 7.35m.

Detailed profiles of the relevant FSS Types in each segment are included within the powerpoint presentations that accompany this summary document.

1.2 Attractiveness of Commercial Property

Some caution is required in the interpretation of the survey undertaken on the BPF's behalf by MORI owing to the limited sample size(only 486 active investors). However, some general observations are possible and the focus group provide some further insights.

- About a third of active investors appear to be interested in commercial property investment products. After some prompting, this percentage increases to about 45%. In contrast, there is a hard-core of approx 40% of active investors who would need a lot of persuasion to invest in commercial property. This leaves a group of 15%- 25% who are fairly interested and may be converted over time.While a majority (nearly 60%) of active investors considered commercial property the best performing asset over the last 3 years, only a small proportion (10%) already had property based investment products.Similarly, there was a significant gap between those who said they were interested in commercial property investment (30% +) and those who stated they would definitely invest within the next 12 months period. Only 5% of active investors stated they would be interested in investing in commercial property within 12 months.
- It was apparent from the focus groups that there was little enthusiasm for the main commercial property investment products that are currently available. The management fees and transaction costs were thought to be high, particularly the five per cent initial fee for the unit trust products, and some remarked that the net returns were no higher than they would be from Premium Bonds.
- Different types of commercial property investment are likely to be attractive to different investor segments based on their risk appetite and investment objectives. Nevertheless, it is clear that there is some considerable investor uncertainty about how to invest, where to get appropriate information and associated investment risks. In addition, focus group members were concerned about the size of the sums required to invest, the long-term nature of the investment and the lack of liquidity.
- A major challenge for the industry is to determine how to persuade more people who are interested in commercial property investment to actually invest. The underlying investor interest appears to exist. The issue appears to be more about the products offered and investment information available. This should be a priority area for the industry to investigate further. What is required to close the gap between “performance awareness” and “investment decision”? Is there a sufficient understanding of the perceived constraints and the relative advantages and disadvantages of specific commercial property investment products?

1.3 Attitudes to PIFs

The main advantages of commercial property investment (from both the focus groups and MORI BPF/CB Richard Ellis survey) were identified as relatively stable income (resulting from longer leases than the residential sector), a perception that commercial rents rarely fall, and a view that the performance of the commercial property market will be aligned over time with that of the economy as a whole. Provided it was regarded as a long-term investment, the risk was thought to be fairly low, particularly compared to new residential property investment.

Property Investment Funds generated more enthusiasm than existing rival products and several focus group participants stated that they would consider investing in them. The main advantages were identified as the relatively high income yield, low fees, moderate risk, and low taxation within the fund.

The liquidity offered by PIFs was also regarded as a positive feature. Nevertheless, because of their perceptions of the commercial property market as offering steady rather than spectacular returns, most participants still regarded PIFs as a long-term investment.

The more active investors said the next thing they would want to know if looking into PIFs would be the exact type and location of the property. These participants were keen to exercise their own judgement about the prospects for the regions and sectors to which they would be exposed. Everybody said that they would carry out extensive research of their own before investing in such a product.

Participants felt that two types of investor would be attracted to PIFs: younger people could treat them as a long term investment to provide capital growth as part of a diversified portfolio, in an age where fewer people will be prepared to rely entirely on their pension fund; retired people with a lump sum at their disposal could look to PIFs to provide a reasonable and steady extra income.

For investors who had decided that they wished to include commercial property in their portfolio, PIFs were considered by participants to be an attractive and accessible way of doing so.

1.4 Next Steps

Several next steps are advisable to build on the analysis undertaken. However, it may be concluded that these should be left to individual investment companies to pursue as they wish.Validating the risk appetite and investment priorities of the 17 active investor FSS Types. Are the three identified risk segments accurate?

- Further focus groups to build on conclusions already identified and to understand the lower risk appetite group (owing to time and budget constraints, the focus groups concentrated on the high and medium risk groups).
- Developing prototype PIF products aimed at the differing FSS Types.
- Testing the designed prototype products with further focus groups and quantitative research.

2. Introduction

The purpose of this workstream was to research the needs of smaller investors who may be interested in investing in commercial property and to provide a more detailed understanding of the smaller investor market. Three specific pieces of analysis were undertaken:

- An overview of UK personal investment. Using the MORI Financial Tracking Survey, a quantitative summary was produced of people's financial behaviour. The MORI survey is based on approximately 4,000 face-to-face interviews each month, with people selected according to their demographics to ensure a representative sample is surveyed.
  The MORI survey responses were coded with Experian segmentation codes, such as Mosaic and Financial Strategy Segments (FSS). Combining the two approaches highlighted which customer segments tend to purchase what products. Estimating market size was then derived by extrapolating the survey responses across the whole of the UK.
- Quantitative market research, aimed at summarising the attractiveness of commercial property investment for small investors and their likely propensity to invest in new commercial property products. This analysis utilised both a MORI survey conducted on behalf of the BPF and CB Richard Ellis in December 2003 and two additional questions that were raised as part of MORI's April 2004 Financial Tracking Survey.
- Three focus groups comprising active investors, aimed at gathering information on the investment strategies of smaller investors and their objectives and attitudes to commercial property investment. This qualitative analysis included assessing the perceived advantages and disadvantages of investing in different types of commercial property, particularly proposed Property Investment Funds (PIFs), in order to gauge the extent to which existing vehicles meet investor requirements.

3. Overview of UK Personal Investment

3.1 Approach

The research information was collected from three sources:

- Mori FTS: A fortnightly survey, with approx 46,000 respondents during 2003;
- Experian's own proprietary segmentation analysis, using Mosaic and Financial Strategy Segments (FSS). In this instance, FSS was the primary segmentation method used;
- External desk research on overall UK investment product penetration. For example, Inland Revenue information.

FSS classifies all 46m adults in the UK into one of 31 distinct financial lifestyle types to describe their socio-economic and behavioural characteristics, their typical financial product holdings and likely future intentions. The core part of this analysis was to ascertain the attractiveness of various investments by FSS types and to gauge the size of the active investor market. This was taken to be a good proxy for the potential individual investor market for commercial property and Property Investment Funds.

Active investors were defined as those who held shares (other than via mutualization or privatisation shares), plus equity ISA, OEIC and unit trust and investment trust holders.

3.2 MORI FTS Overall UK Investment Penetration

The key points from an initial analysis of the MORI FTS results were as follows:

- 57% (25,806) of the Mori FTS sample had no investments at all. The remaining 43% had on average 1.9 investment products each.
- 45% of investors had stocks and shares, but only 5% had unit trusts
- Averaging these figures up to the national level implies there are 8.5mn individual shareholders in the UK. Separately, we identified that the Inland Revenue states there are 10.3 million shareholders in the UK. Consequently, it is likely that the MORI FTS sample is not fully representative of investors nationally and that the FSS market sizing estimates may err on the low side. Similarly, the Mori FTS estimate that 22% of ISA holders have equity ISAs is considerably lower than the Inland Revenue figure of 46%.
- This approach provides a low end range estimate for the number of active investors in the UK of 3.7m – being the Inland Revenue's estimate for the number of shareholders with more than mutualization or privatization stocks.

3.3 Investment Attractiveness by FSS Types

The attractiveness of seven investment products was assessed by Experian's FSS Type segmentation classifications. The products were Shares, ISAs, PEPs, Unit Trusts, Investment Trusts, OEICs and Company Pensions Schemes.

3. Overview of UK Personal Investment

Product penetration per FSS Type was compared with the percentage of people in that FSS Type within the overall MORI FTS sample. This resulted in a market penetration index number for every product per FSS Type. For example, if 2% of shareholders were FSS Type "Equity Rich Elders" and they were 2% of the sample, the index would be 100. However, if 3% of shareholders were "Equity Rich Elders", the index would be 150.

Product penetration indices for share ownership and unit trusts are shown in Tables 2 and 3 below. Market penetration indices for the other products are included in the Appendices.

Table 2: **Share Ownership by FFS Type**

FSS Segment		Distribution (%)	Index
A1	Aspirant Millionaires	0.51	247
A2	Women with Wealth	0.62	262
A3	Owner/Investors	1.64	216
A4	Higher Rate Salariat	0.93	262
B5	Capital Gainers	1.74	255
B6	Professional Heights	1.34	195
B7	Wealth from the Land	1.71	195
B8	Cusp of Retirement	3.83	236
B9	Upscale Middle Agers	5.48	192
B10	Ready for Retirement	7.39	129
C11	Equity Rich Elders	6.34	186
C12	On Private Pensions	6.73	114
C13	Greys Just Surviving	5.24	73
C14	Subsisting Elders	2.09	47
D15	Young Jobseekers	1.55	42
D16	Transient Lifestyles	1.39	31
D17	Lone Parents in Debt	0.70	24
D18	Hardened Cash Payers	3.31	61
D19	Cash Strapped Mums	3.12	49
E20	Anxious Breadwinners	3.12	61
E21	Aspiring Mid Market	9.27	117
E22	Wives on a Budget	5.91	84
E23	Prospering Flatmates	4.28	77
F24	Nest Forming Mothers	4.07	110
F25	Juggling Work & Home	3.10	149
F26	Women Flying High	1.59	199
F27	Men Behaving Well	4.16	172
F28	Urban Enterprise	3.30	149
G29	Rich Kids at Home	1.57	177
G30	Sons Still at Home	1.95	88
G31	Girls Still at Home	2.01	92
Formatted Sample Total		**100**	**100**

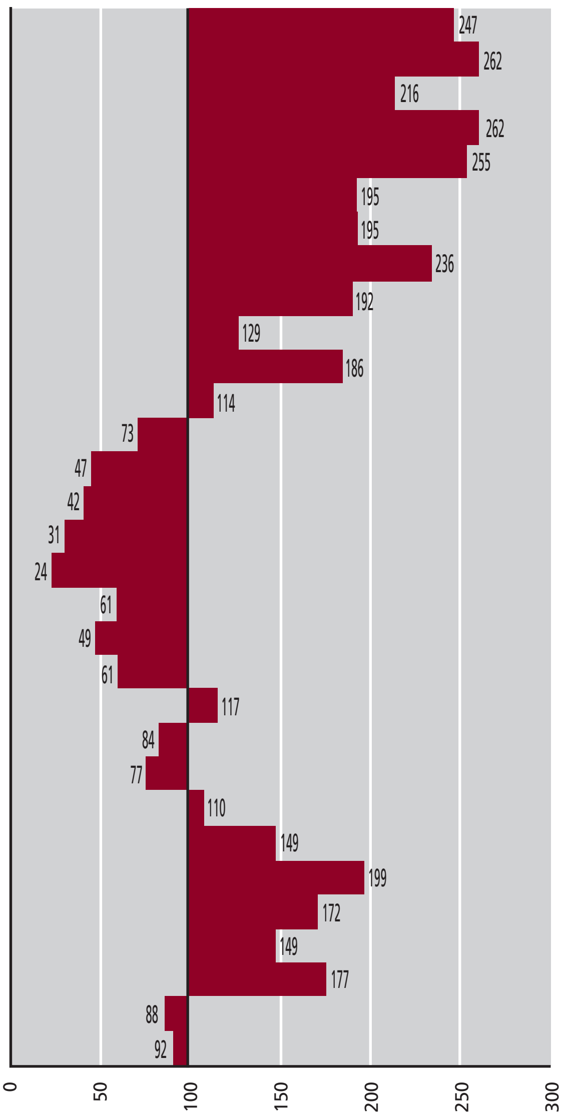
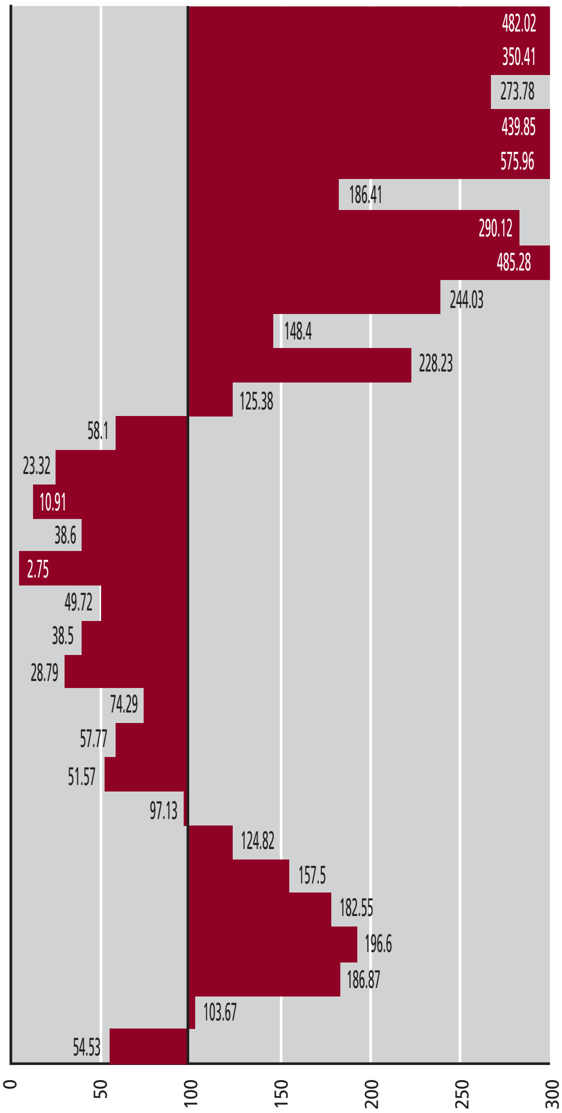


Table 3: **Unit Trust Holders by FSS Type**

FSS Segment		Distribution (%)	Index
A1	Aspirant Millionaires	0.99	482.02
A2	Women with Wealth	0.82	350.41
A3	Owner/Investors	2.08	273.78
A4	Higher Rate Salariat	1.56	439.86
B5	Capital Gainers	3.93	575.96
B6	Professional Heights	1.28	186.41
B7	Wealth from the Land	2.55	290.12
B8	Cusp of Retirement	7.88	485.28
B9	Upscale Middle Agers	6.96	244.03
B10	Ready for Retirement	8.53	148.4
C11	Equity Rich Elders	7.76	228.23
C12	On Private Pensions	7.39	125.38
C13	Greys Just Surviving	4.19	58.1
C14	Subsisting Elders	1.04	23.32
D15	Young Jobseekers	0.40	10.91
D16	Transient Lifestyles	1.71	38.6
D17	Lone Parents in Debt	0.08	2.75
D18	Hardened Cash Payers	2.71	49.72
D19	Cash Strapped Mums	2.46	38.5
E20	Anxious Breadwinners	1.46	28.79
E21	Aspiring Mid Market	5.91	74.29
E22	Wives on a Budget	4.08	57.77
E23	Prospering Flatmates	2.87	51.57
F24	Nest Forming Mothers	3.60	97.13
F25	Juggling Work & Home	2.59	124.82
F26	Women Flying High	1.26	157.5
F27	Men Behaving Well	4.41	182.55
F28	Urban Enterprise	4.34	196.6
G29	Rich Kids at Home	1.65	186.87
G30	Sons Still at Home	2.30	103.67
G31	Girls Still at Home	1.18	54.53
Formatted Sample Total		**100**	**100**



The results for all the 7 investment products investigated were broadly similar, with 3 of the 7 FSS Groups dominating and 17 FSS Types consistently being over-represented (indices over 100) as follows:

Dominant Groups

- *Group A* (All 4 FSS Types in the Group) – Money Worth Managing. The financial elite, likely to have highest incomes and most complex investment portfolios.
- *Group B* (All 6 FSS Types in the Group) – Asset Rich Families. Generally later middle age families. Generally invest in safe, conservative long-term financial products, with a focus on impending retirement.
- *Group F* (4 out of 5 FSS Types in the Group) – Equity Accumulation. Mostly 40-50 year olds, married, with good jobs who are able to add significantly to their net worth. Regular incomes and high tax liabilities make this Group a good target market for tax-exempt schemes, such as ISAs.

Secondary Groups

- *Group C* (2 FSS Types out of 4). Group is Grey Lifestyles, which covers most of the retired population. Specific sub-segments that were more likely to be active investors were "Equity Rich Elders" and "On Private Pensions". The former are in their early retirement years and tend to remain very active with substantial equity capital. Many will have occupational pensions and often they will use IFAs. The latter Type is older and tend to be women. Their savings are diminishing as they been retired some time and their focus is on careful management of their remaining savings. This includes tax-exempt schemes, while higher risk investments are not attractive.
- *Group G* (1 FSS Type out of 3). Group is Parental Dependency. Young adults who live at home or are financially dependent on their parents. In particular, "Rich Kids at Home" are young adults able to rely on wealthy parents. They are typically aged 18 to 25 and many will be starting to consider investment products, such as ISAs, and may welcome financial advice on their savings and investment strategies.

The 17 highlighted FSS Types were considered to be a good proxy for the active investor population. Ideally, we would have segmented the Types further according to their attitudes to risk and investment priorities (eg growth vs income). Unfortunately, no non-client confidential data that links FSS Types to risk profile was available and hence a working hypothesis was adopted to progress the analysis. Three risk-profile market segments were identified as follows:

- *Higher risk*: 6 Types likely to have a high risk appetite and be attracted to property investment for growth reasons;
- *Moderate risk*: 5 Types likely to be moderately attracted to property investment from both growth and income perspectives;
- *Lower risk*: 6 Types probably more attracted to the income attributes of property investment.

It is possible that some Types could be better placed in other segments. For example, G29 (Rich Kids at Home) may be more growth than income focused. It is recommended that the risk segments are validated and refined as necessary by further market research in due course.

3.4 Estimating Market Size by FSS Types

Market size estimates have been prepared by extrapolating the market penetration of investment products by FSS Types in the sample up to the wider UK population.

Overall investment product take-up within the "active investor" FSS Types is significantly higher than across the population as a whole. For example:

- Stocks/shares were owned by between 21% and 50% of the targeted FSS Types, compared with an average of 18.5% for the overall population.
- Equity ISAs were owned by 4% -15%, compared with 4.2% overall.Unit Trusts were owned by 2%-11%, compared with 2% overall.

National market size estimates were derived by extrapolating the market penetration rates of investment products per FSS Type against the total number of adults of that FSS Type in the UK. For example, 34% of "Equity Rich Elders" own shares and there are 1.8m "Equity Rich Elders" in the UK, giving a market size of 620,000. The estimated current market size per FSS Type for specific investment products is summarised in Table 4 overleaf:

3. Overview of UK Personal Investment

Table 4: **Summary Active Investor Market Size Estimates by FSS Type**

Catagory	FSS Type	Population Number	Stocks/Shares (%)	Stocks/Shares Number	Equity ISAs (%)	Equity ISAs Number	Unit Trusts (%)	Unit Trusts Number
High Risk								
A1	Aspirant Millionaires	250000	45	112248	15	38601	9	23179
A4	Higher Rate Salariat	260000	49	127726	11	28845	9	22791
B5	Capital Gainers	600000	47	283845	11	63931	11	68199
B6	Professional Heights	520000	36	186702	6	33185	4	18972
B9	Upscale Middle Agers	1700000	36	604330	10	177651	5	81650
F28	Urban Enterprise	1400000	28	386491	6	82923	4	54071
	Segment Total	**4730000**	**36**	**1701341**	**9**	**425135**	**6**	**268862**
Med Risk								
A2	Women with Wealth	350000	50	174430	10	34113	7	24541
A3	Owner/Investors	600000	40	239371	12	72371	5	32296
B7	Wealth from the Land	1100000	36	395181	9	96073	6	62689
C11	Equity Rich Elders	1800000	34	620544	7	130123	4	80797
F27	Men Behaving Well	1200000	32	381372	8	93691	4	43008
	Segment Total	**5050000**	**36**	**1810897**	**8**	**426371**	**5**	**243331**
Low Risk								
B8	Cusp of Retirement	910000	44	397754	10	93318	10	87055
B10	Ready for Retirement	2700000	24	641549	4	115225	3	78775
C12	On Private Pensions	2700000	21	570365	4	119459	2	66625
F25	Juggling Work & Home	1000000	28	275542	6	56197	2	24489
F26	Women Flying High	600000	37	220469	8	47136	3	18585
G29	Rich Kids at Home	1000000	33	329842	6	63685	4	36876
	Segment Total	**8910000**	**27**	**2435522**	**6**	**495020**	**4**	**312405**
	Overall Market Total	**18690000**	**32**	**5947760**	**7**	**1346525**	**4**	**824597**

Using this methodology, the total market sizes for the three risk segments were estimated as follows:

- The higher risk appetite segment is comprised of approximately 1.8m to 2.1m investors (40-45% of the 4.7m FSS population), broken down as follows:
  - 1.7 million shareholders
  - 425k equity ISA holders
  - 270k unit trust holders
- The medium risk appetite segment is comprised of approximately 2.0m to 2.25m investors (40-45% of the 5.1m FSS population), broken down as follows:
  - 1.8 million shareholders
  - 425k equity ISA holders
  - 245k unit trust holders
- The lower risk appetite segment is comprised of approximately 2.75m to 3.0m investors (30-35% of the 8.9m FSS population). While the percentage is lower, the segment nevertheless includes a large number of investors. This is broken down as follows:
  - 2.4 million shareholders
  - 495k equity ISA holders
  - 312k unit trust holders

Combined these three segments indicate that the active investor base across the 17 FSS Types lies between 6.55m and 7.35m. This provides an upper estimate to the size of the active investor market (compared to the Inland Revenue figure of 3.7m investors who own non-privatisation or mutualisation shares – see section 3.2).

4. Attractiveness of Commercial Property Investment

4.1 Approach

Both quantitative and qualitative research was undertaken into the attractiveness of existing commercial property investment products.

The quantitative market research was based on a MORI survey conducted on behalf of the BPF and CB Richard Ellis in December 2003 and some specific questions raised as part of MORI's April 2004 Financial Tracking Survey.

- In the December 2003 survey, MORI interviewed a representative quota sample of 2000 adults aged 16+ in the UK. The study focused on active investors only (equity or related product holders excluding mutualisation and privatisation) and was hence in practice limited to only 486 responses.
- The April 2004 MORI Financial Tracking Survey similarly targeted approximately 400 – 500 active investors.

The responses from both surveys were segmented using Experian's "MOSAIC" segmentation profiles. Use of more detailed classifications was not appropriate given the low sample of active investors.

The qualitative research took the form of three focus groups, which were conducted in London in early May 2004. In total there were 22 participants, who were recruited according to Experian's financial segmentation codes to help identify the risk profiles of investors. The groups were divided between people meeting the high and medium risk investor profile.

About half of the focus group participants described themselves as "active investors", by which they usually meant they took investment decisions at least every two or three months. All participants did so at least once a year (which met our own criteria for active investment).

The objective of the focus groups was to investigate attitudes to investing, to existing commercial property investment options and to PIFs.

4.2 Commercial Property Investment – Key Quantitative Research Findings

It was difficult to draw firm conclusions on the attractiveness of commercial property investment due to the limited size of the MORI samples (450 for each survey). Nevertheless some observations could be made:

- There was a significant difference between the number of active investors who thought commercial property was a top performing asset (60%) and those who had actually invested in commercial property (16%). This perhaps signifies some investor uncertainty about how to invest, where to get appropriate information and associated investment risks. This should be one area to investigate further – what is required to close the gap between "performance awareness" and "investment decision"?
- Approximately 30% of active investors would be interested in a new commercial property investment product. Similarly, it was apparent that there was a hard-core of approx 40% of active investors who would need a lot of persuasion to invest in commercial property. This leaves a group of approx 30% who would be fairly interested and could be converted over time.

4. Attractiveness of Commercial Property Investment

- The main constraints to commercial property investment were stated as affordability, risk and transparency. Different types of commercial property investment are likely to be attractive to different investor segments based on their risk appetite and investment objectives.
- There is a significant gap between those who say they are interested in commercial property investment (30% +) and those who state they will definitely invest within the next 12 months period. Only 5% of active investors stated they would be interested in investing in commercial property within 12 months.
- A major issue for the industry is how to persuade more people who are interested in commercial property investment to actually invest. The underlying investor interest appears to exist. The challenge appears to be more about the products offered and investment information available. Is there a sufficient understanding of the perceived constraints and the relative advantages and disadvantages of specific commercial property investment products?

4.3 Commercial Property Investment – Key Qualitative Research Findings

The main findings from the focus groups were as follows:

Attitudes to IFAs

- Attitudes to financial advisers varied according to how regularly participants took investment decisions, and how knowledgeable they considered themselves to be.
- The most active and best-informed investors were the least likely to seek the advice of financial advisers, often saying that they knew at least as much as a financial adviser could, and sometimes remarking that some of their biggest investment mistakes - usually pensions and endowment policies - had been as a result of advice taken from an IFA. However, while reluctant to turn to an IFA for investment advice, these people often said that they would seek professional advice on specialist areas such as taxation and estate planning.
- Less active and knowledgeable investors were more inclined to seek advice from an IFA, although they always said that they would conduct their own research and use their common sense.
- Newspapers were the most commonly used source of information about investments. Participants stressed, however, that they looked to newspapers for economic analysis and information about general trends and market conditions; they would treat "puffs" for particular financial products with scepticism.

Motivation for and attitudes towards investment

- Participants' motivation for investing varied according to their age. Those who were still working usually said they were seeking to provide a supplement to their pensions, or to accumulate capital to pass on to their children.
- Retired people were usually motivated by a desire to secure the capital they had accumulated over their lifetime, protect it from taxation, and earn as high a return as possible without exposing it to undue risk. Retired people of more comfortable means also engaged in fairly speculative investment, though only with limited sums that they could afford to lose.

4. Attractiveness of Commercial Property Investment

- When asked about their attitude to the current investment climate most of these investors said that they would advise small investors to keep their investments liquid, favouring bank savings accounts, cash ISAs or gilts rather than more 'speculative' investments.
- It was clear from remarks throughout the discussion that all investors recognised that the stock market had performed badly in recent years, with negative consequences for most investments linked to equities. Most noted that residential property was the asset that had gained the most value over the same period.
- The very active investors were most likely to take a detailed interest in the particular stocks or equities in which their funds were invested. As with financial advisers, many of these investors took the view that most fund managers were no more likely to make good investment decisions than they were (and consequently resented paying management fees). However, some said that they followed the careers of the best performing fund managers as they moved between institutions, and even that they moved their investments with them.
- All participants said that while a financial institution's track record was inevitably something they would take into account when making investment decisions, it is a factor they would treat with considerable caution. Several made the point that Equitable Life had once had a very respectable track record.

Attitudes to investment in property

- Many participants had current investments in residential property, or had made such investments in the past. Most of these put their returns – whether considerable or modest – down to timing and, to a significant degree, luck.
- Participants did not generally expect recent gains in residential property values to continue at the same rate (although most did not expect prices to fall). This factor, together with expected increases in interest rates and the inevitable problem of relatively short leases and frequent periods without tenants, combined to make new investments in buy-to-let residential property a relatively high-risk proposition.
- A small number of participants had looked into investing in commercial property (some of the very active and wealthy investors had done so) and aspired to do so, but most knew little about the subject compared to their knowledge of other fields of investment.
- The main advantages of commercial property investment were thought to be a relatively stable income (resulting from leases of 5-10 years, as opposed to 6 months to a year in the residential sector), a perception that commercial rents very rarely fall, and a view that the performance of the commercial property market will be aligned over time with that of the economy as a whole. Provided it was regarded as a long term investment, the risk was thought to be fairly low – particularly compared to new residential property investment.
- Although there was some limited knowledge of property investment products, the disadvantages of commercial property investment were thought to be the size of the sums required to invest, the long term nature of the investment and the lack of liquidity. For this reason, the main investors in commercial property were thought to be banks and financial institutions.

4. Attractiveness of Commercial Property Investment

- Of the three existing property investment products presented to participants (Authorised Unit Trusts, Unauthorised Unit Trusts and Offshore Property Investment Companies), the least risky – generally classed as low to medium risk - was thought to be the Authorised Unit Trust. Although it was acknowledged that regulation by the Financial Services Authority was no guarantee of performance (and even that compliance with regulations could restrict potential returns), FSA regulation provided a degree of reassurance to less active investors. The words "Unauthorised" and "Offshore" had connotations of risk for these people.
- There was little enthusiasm for any of these three products. The management fees and transaction costs were thought to be high – particularly the 5 per cent initial fee for the first two products – and some remarked that the net returns were no higher than they would be from Premium Bonds.
- There was some confusion, particularly among the less active investors, as to whether or when income or capital gains derived from offshore investments were liable to taxation.
- Nobody had heard of Norwich Property Trust or Edinburgh Property Trust, but several participants remarked that they had confidence in M&G. In general, the products were thought to carry roughly the same or slightly lower risk than a unit trust comprising blue chip equities.

5. Investor Attitudes to Property Investment Funds (PIFs)

5.1 Approach

Only the qualitative focus group research was appropriate for this section.

5.2 Attitudes to Property Investment Funds

The main findings on PIFs from the focus groups were as follows:

- Property Investment Funds generated more enthusiasm than the three other products – indeed several participants said that they themselves would consider investing in them. The main advantages were the relatively high income yield, relatively low fees, moderate risk, and low taxation within the fund.
- A few participants raised concerns about the involvement of HM Treasury, noting that ISAs operated under less favourable terms than TESSAs and PEPs, and fearing that the tax treatment of PIFs would equally become steadily less generous. Some also pointed out that the fees were similar to those for stakeholder pensions, and wondered whether they would be a sufficient incentive at that level for financial institutions to offer the product at all.
- The liquidity offered by PIFs was regarded as a positive feature. However, because of their perceptions of the commercial property market as offering steady rather than spectacular returns, most participants still regarded the product as a long term investment.
- The more active investors said the next thing they would want to know if looking into PIFs would be the exact type and location of the property. These participants were keen to exercise their own judgement about the prospects for the regions and sectors to which they would be exposed. Everybody said that they would carry out extensive research of their own before investing in such a product.
- The inevitable lack of a track record for PIFs would not put potential investors off. However, more active investors said they would consider investing a relatively small sum initially, and adding more after 6 months or a year if they had become confident about the product.
- Participants felt that two types of investor would be attracted to PIFs: younger people could treat them as a long term investment to provide capital growth as part of a diversified portfolio, in an age where fewer people will be prepared to rely entirely on their pension fund; retired people with a lump sum at their disposal could look to PIFs to provide a reasonable and steady extra income.
- For investors who had decided that they wished to include commercial property in their portfolio, PIFs were considered by participants to be an attractive and accessible way of doing so.

Appendix A:

An overview of UK personal investment

Assessing the needs of small investors

An overview of UK personal investment

July 2004

Contents

Objectives

- ❑ To summarise current investment patterns by private investors in order to place small commercial property investment within a wider investment context
- ❑ Analysis of current investment patterns to include information on:
  - Investment allocation
  - Market sizing
  - Customer segments
  - Customer behaviours

Approach

Information has been collected from three main sources:

1. Mori: The Mori Financial Tracking Survey (MFTS). Approx 48,000 respondents during 2003.
2. Experian: The UK's largest information company, with its proprietary customer segmentation analysis and a wide range of additional consumer information.
3. Desk based research.

MORI Financial Tracking Survey

- ❑ MORI FTS measures all significant developments in the retail financial services markets
- ❑ 4,000 face to face interviews conducted by MORI each month (representative sample)
- ❑ Use of MORI FTS to produce a comprehensive picture of personal financial behaviour in the UK
- ❑ We have taken all responses from 2003. A total annual sample size of 48,000
- ❑ Survey responses coded with Experian segmentation codes (Mosaic and Financial Survey Segments – FSS). This enables us to identify the profiles of investors who favour more sophisticated investment products and may be more interested in commercial property opportunities.

MORI FTS Survey Structure

- Introduction
- Awareness and consideration
- Future buyer preference
- General insurance
- Pet insurance
- Medical insurance
- Travel
- Life assurance
- Pensions
- Direct mail
- Financial sections →
  - Current accounts
  - Savings accounts
  - Investments
  - ISAs
  - Value of savings
  - Mortgages
  - Loans & credit
  - Credit cards
- Technology
- Miscellaneous
- Demographics

Experian information sources

Financial Strategy Segments

- A person level segmentation developed to help financial services companies target their financial services products and services.
- FSS classify all 46 million adults in the United Kingdom into a series 31 distinct financial lifestyle types to describe

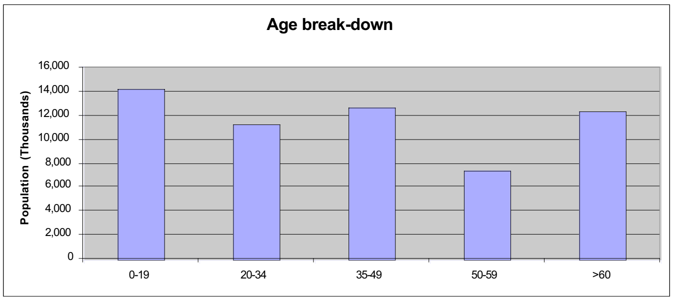
  - typical financial product holdings,
  - behavior and future intentions,
  - key socio-economic and demographic characteristics.

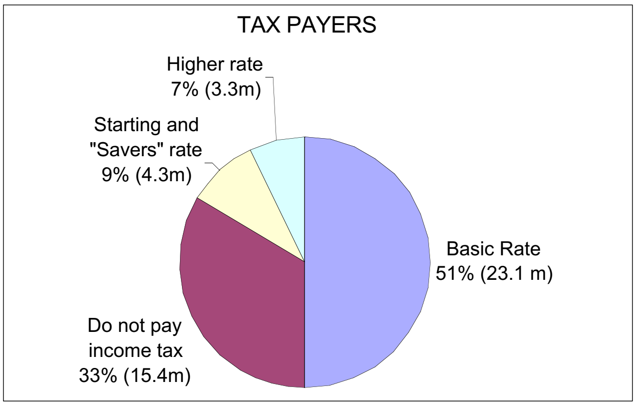
Lifestyle Survey Information

- Experian collects information from tailored consumer lifestyle surveys and has the benefit of data from over 16 million individual surveys.

National overview

2004 Population (Thousands)	
England	49,854
Scotland	5,046
Wales	2,933
GB	57,833





Source: Inland Revenue

- GB population is approx 57.8 mn.
- Adult population (aged 18+) is 44.8 mn.
- 34.4 mn adults aged 16 – 59
- Only 7% of tax payers pay tax at the higher rate

Types of investment – 43% have at least one investment product

Types of investment	number of people	% of respondents with product	% of investors with product
Premium Bonds	7780	17.4%	41.2%
National Savings	2177	4.9%	11.5%
Stocks and Shares	8498	19.0%	45.0%
ISA's	9473	21.2%	50.2%
PEPS	2070	4.6%	11.0%
Unit Trusts	904	2.0%	4.8%
Investment Trusts	481	1.1%	2.5%
GSMBS	308	0.7%	1.6%
Corporate Bonds	407	0.9%	2.2%
Investment Bonds	1241	2.8%	6.6%
OEICs	385	0.9%	2.0%
Savings Plan	1535	3.4%	8.1%
Total number of products	35259	100.0%	

Source: MORI FTS

- Mori asked 45,965 people about their investment in 2003, 44,675 responded
- Of these 25,806 (57%) had no investments
- The remaining 18,869 people had 35,259 investment products between them: an average of 1.9 each.
- The most popular investments were ISAs (50% of investors have an ISA; 45% had Stocks & Shares and 41% Premium Bonds)
- Only 5% of people questioned by MORI had unit trusts.

Equity investments - another view

Approx 10.3m Britons have shares. The vast majority of shareholders only hold privatisation shares

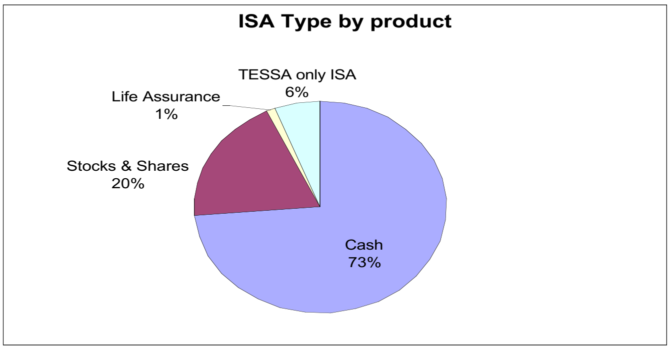
GB SHAREHOLDERS	
Total number of shareholders	**10.3m (23% of GB adult population)**
Shareholders with privatisation shares only	**9.45m (91.5% of shareholders)**
Shareholders with non-privatisation shares	**3.7m (36% of shareholders)**

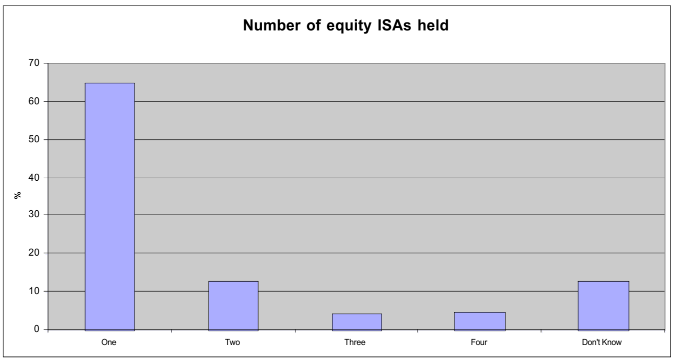
Note: Mori FTS implied 8.5 mn shareholders – 83% of the Inland Revenue total

SOURCE: Inland Revenue

ISAs – Cash ISAs Dominate

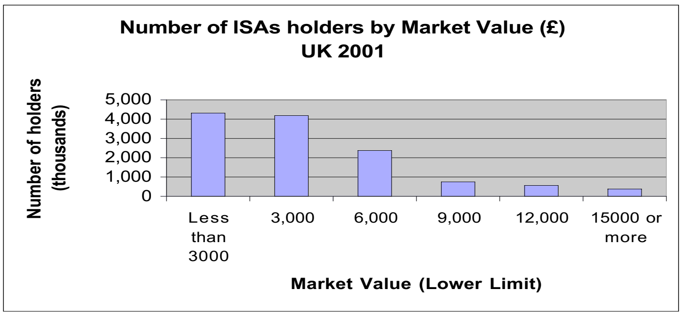
- Mori FTS (2003) asked 9,473 people about the type of ISAs they had. 937 did not know or refused to answer
- Of the remaining 8,536 investors, 81% (6,909) had cash ISAs, while only 22% (1,840) had equity ISAs
- Only 22% (398) of equity ISA investors had more than one equity ISA.

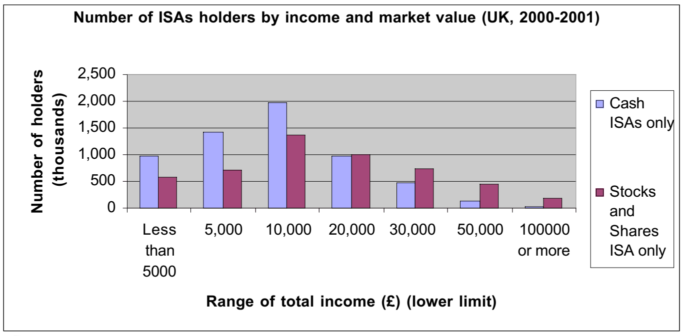




Source: MORI FTS

Profile of ISAs investors



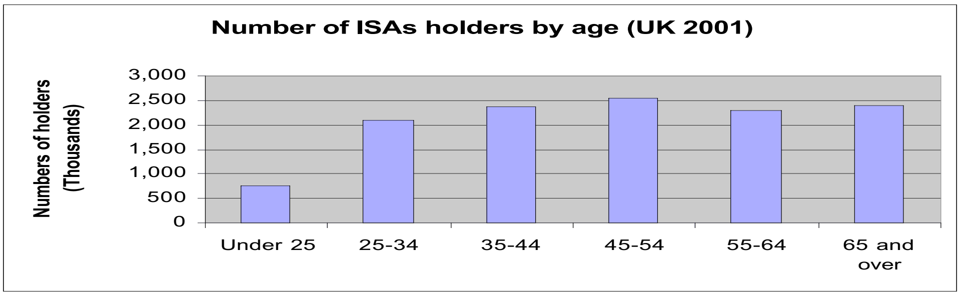


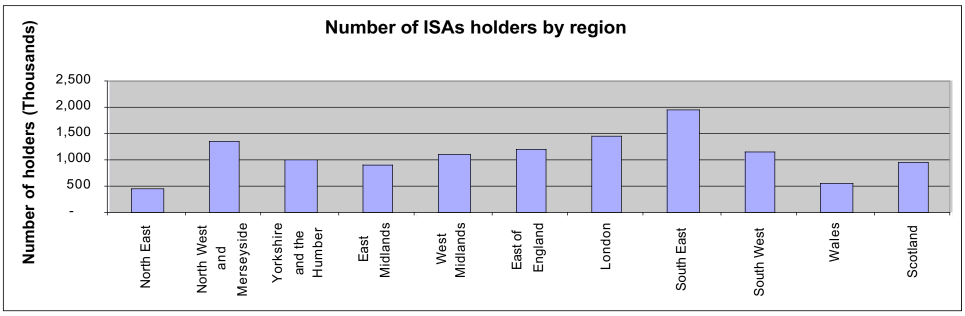
- Total number of cash ISAs holders is approx 5.9m
- The vast majority of ISAs holders hold less than £6,000 (market value)
- Total number of Stock and Shares ISAs only holders is approx 5m.
- The majority of cash ISAs only, and Stocks & Shares ISAs only holders are in the income range (£10,000 – £30,000)
- High income individuals are more likely to invest in equity ISAs

Source: Inland Revenue (UK, 2000-01)

Profile of ISAs investors

Number of individuals holding ISAs approx 12.2m in GB (2001)

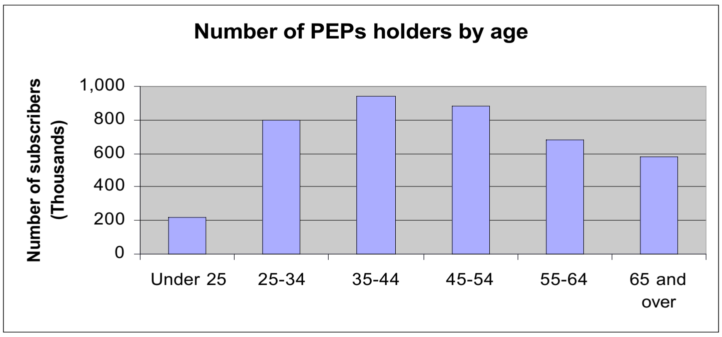




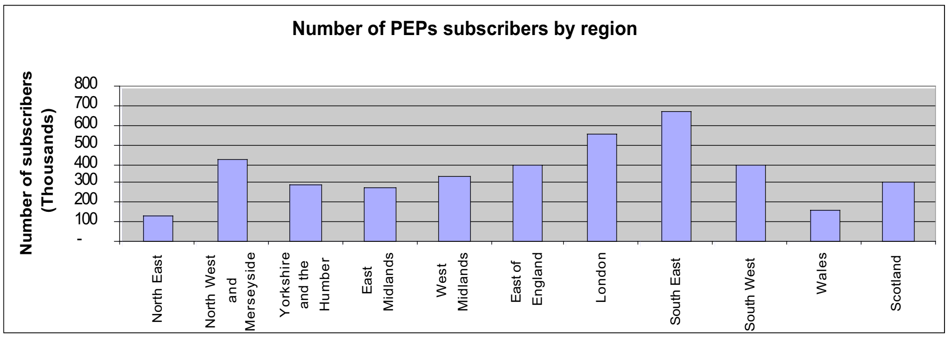
- ISAs holding uniformly distributed within the age range 25 – 65+
- ISAs holders concentrated in the South East, London, North West
- On the contrary, low concentration in the North East, Scotland and Wales

Source: Inland Revenue (2000-01)

PEPs



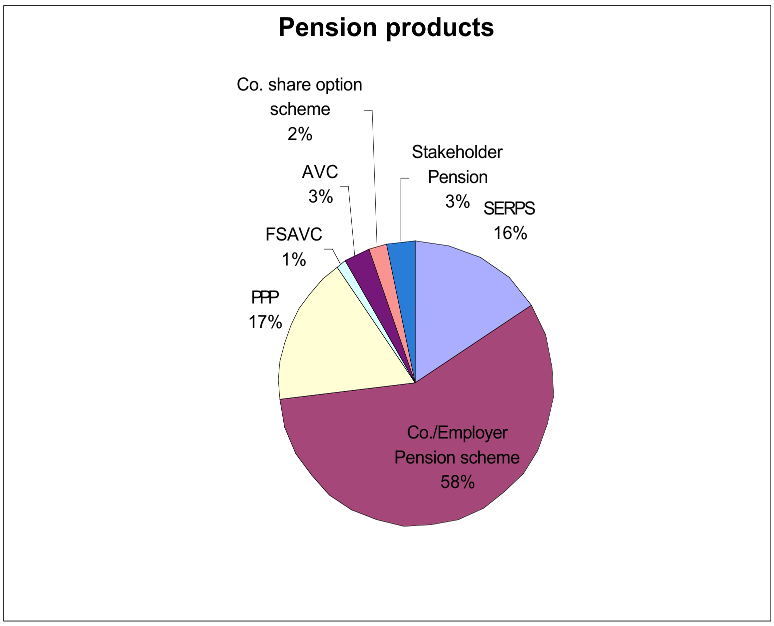
- Majority of PEPs subscribers are in the age range 25-64
- High propensity in investing in PEPs in the South East, London, the North West and East of England
- Low tendency in Wales and in the North East



Source: Inland Revenue 1998-99

Types of pension schemes

- Mori FTS (2003) asked 40,151 people about their pensions arrangements. 39,946 responded
- 25,964 (65%) were making no pension contribution
- Of the remaining (16,726), 9,585 had company pension scheme and 2,632 were in SERPS
- Sample appears to be over-representative of GB overall. Inland Revenue data suggests 1.8m employer pension members



Source: MORI FTS

Commercial property target market – sophisticated investors

- Initial market definition: individuals who own shares (other than privatisation shares), equity ISAs, unit trusts, investments trusts and/or OEICs
- Market Size:
  - Approx 10.5m accounts.
  - Estimated target market of sophisticated investors is 3.7m – 5m. (lower level being Inland Revenue non-privatisation shareholders).
- But:
  - Who are these investors?
  - How can they be segmented?

Introduction to Financial Strategy Segments (FSS)

- A segmentation system which places every GB consumer into one of 31 different categories
- Designed specifically for the financial services marketplace
- Categories based on the likelihood of consumers to hold various types of financial product according to their credit risk, net worth, equity held in housing and their preferred channel for undertaking financial services transactions.

Business Strategies from Experian

Experian's Financial Strategy Segments

FSS Segments	Proportion of UK adults	Outline description
A1 Aspirant Millionaires (Money Worth Managing)	0.55%	live in very expensive houses, to apply for very large mortgages and to have high holdings of stocks and shares
A2 Women with Wealth (Money Worth Managing)	0.75%	likely to be company directors and/or shareholders; better targets for investments in stocks and shares than for instant access savings
A3 Owner/Investors (Money Worth Managing)	1.26%	middle aged men that manage their own businesses; much of their capital value is locked up in illiquid assets; prefer lump sum long term investments.
A4 Higher Rate Salariat (Money Worth Managing)	0.57%	highly paid mid-career executives and managers; invest in a variety of savings schemes to minimise tax liability
B5 Capital Gainers (Money Worth Managing)	1.32%	have achieved high net worth through the appreciation of capital assets rather than from income; could be viewed as professional, as distinct from amateur, investors.
B6 Professional Heights (Asset Rich Families)	1.13%	middle aged and have reached the peak of their career; have significant net worth in financial products as well their home; invest in stocks, shares and unit trust, tax exempt savings.
B7 Wealth from the Land (Asset Rich Families)	2.54%	people who live in isolated rural locations where private finance is strongly intertwined with land and most financial assets are held in an illiquid form.
B8 Cusp of retirement (Asset Rich Families)	1.99%	crossing over from employment to retirement; have benefited from appreciating property prices, maturing life and endowment policies and inheritances.
B9 Upscale Middle Agers (Asset Rich Families)	3.68%	middle to upper middle income empty nesters; this group is busy adding to its existing pension provision through savings in tax exempt schemes.
B10 Ready for Retirement (Asset Rich Families)	5.88%	lower income empty nesters; thrifty group with modest tax free savings
C11 Equity Rich Elders (Grey Lifestyles)	4.02%	In early retirement with substantial capital; are not afraid to move funds around for better rates; often rely on Independent Financial Advisers
C12 On Private Pensions (Grey Lifestyles)	5.95%	Elderly people particularly anxious about the careful management of what savings
C13 Greys Just Surviving ((Grey Lifestyles)	5.91%	Little or no market for savings
C14 Subsisting Elders (Grey Lifestyles)	3.21%	no private income other than the state pension
D15 Young Jobsearchers (Welfare Borderline)	3.44%	Typically aged 18-25, who are still living with their parents
D16 Transient Lifestyles (Welfare Borderline)	2.40%	Welfare Borderline
D17 Lone Parents in Debt (Welfare Borderline)	1.17%	Welfare Borderline
D18 Hardened Cash Payers (Welfare Borderline)	4.18%	Welfare Borderline - very old fashioned attitudes towards financial services
D19 Cash Strapped Mums (Welfare Borderline)	4.74%	Welfare Borderline
E20 Anxious Breadwinners ((Small Time Borrowing)	3.73%	Low incomes working hard but still struggling to create an affluent lifestyle
E21 Aspiring Mid Market (Small Time Borrowing)	7.01%	on good incomes and who use a wide range of financial services products; the effectiveness with which they manage their money is an important part of their self esteem
E22 Wives on a Budget (Small Time Borrowing)	6.44%	married women typically in their 30s or 40s who have to manage carefully commitments in the form of mortgages, loans and pensions but have limited family incomes
E23 Prospering Flatmates (Small Time Borrowing)	5.04%	mostly of young singles, just out of college, who are at the start of what will probably become a well paid career.
F24 Nest Forming Mothers (Equity Accumulation)	3.98%	Few have substantial savings
F25 Juggling Work & Home (Equity Accumulation)	2.28%	married women, many with older children; they add to savings and investment accounts they have with mainstream financial services providers
F26 Women Flying High (Equity Accumulation)	1.25%	work in well paid professional and management positions; have above average usage across all savings instruments
F27 Men Behaving Well (Equity Accumulation)	2.72%	of middle income owner occupiers; beginning to see a significant equity margin in the homes and are building savings portfolios
F28 Urban Enterprise (Equity Accumulation)	3.04%	well educated young participating in new entrepreneurial service ventures in large cities; high earnings growth opportunities; early financial adopters.
G29 Rich Kids at Home (Parental Dependency)	2.07%	young adults who are able to rely on relatively wealthy parents
G30 Sons Still at Home (Parental Dependency)	3.69%	young males, typically aged 18 to 25, who with their parents. Many of them work in manual occupations, or are students.
G31 Girls Still at Home (Parental Dependency)	4.01%	mostly students, aged 18 to 25, existing on grants supplemented by part time work

Business Strategies from Experian

Group A – Money Worth Managing: 1.4m UK adults (3.13%)

- The financial elite of the country.
- Direct or own companies, enjoy the highest incomes.
- Can afford to speculate by investing in small enterprises or buying shares in large ones.
- Investments are carefully calculated and are undertaken with the help of professional advisors.
- Often find it convenient to borrow to finance investments.
- Complex portfolio of pension, life assurance and private insurance policies and tax-exempt savings accounts.

Group B – Asset Rich Families: 7.6m UK adults (16.55%)

- Later middle age whose families are grown up.
- Mortgages are close to being paid off.
- Financial concerns focused on impending retirement.
- Do not need or want to borrow, pay off credit card balances at end of every month.
- Invest mostly in safe, conservative, long-term financial services products.
- Prefer unit trusts and tax-exempt savings but extensive use of lump sum investments, stocks and shares, investment trusts and notice accounts.

Group C – Grey Lifestyles: 8.8m UK adults (19.09%)

- ❑ Covers majority of the retired population from the extremely comfortable to those supported entirely by state benefits.
- ❑ For significant numbers their home constitutes the majority of their equity.
- ❑ Many are juggling the need to preserve the value of their capital with the need to generate a reasonable flow of current income.
- ❑ Not the group to sell to for mortgages, overdraft facilities or personal loans.
- ❑ Insurance, particularly life and health, important to these people.
- ❑ Funeral insurance common for poorer pensioners

Group D – Welfare Borderline: 7.3m UK adults (15.93%)

- ❑ Virtually no net worth.
- ❑ Financial horizon are very short term, coping till end of week/month.
- ❑ Living on council estates, little formal education, difficulty finding and keeping full-time employment.
- ❑ Many reliant on state benefit, using the Post Office for transactions.
- ❑ Few savings other than National Savings or children’s accounts.
- ❑ Many accounts opened to save for specific events – Christmas/holidays.
- ❑ Unlikely to be accepted for credit.
- ❑ Many have neither car nor household insurance.

Group E – Small Time Borrowing: 10.2m UK adults (22.22%)

- ❑ Young singles and families at 'nestmaking' stage financial lifecycle.
- ❑ Limited earnings, children to support and mortgages to pay off.
- ❑ Heavily into overdrafts, personal loans and credit cards.
- ❑ Car finance is very important.
- ❑ Major concern is accidents that would affect their ability to repay loans so extended warranties and unemployment protection sell well.
- ❑ Few have substantial savings, just instant access accounts and children's savings book.
- ❑ Little interest in sophisticated investment products.

Group F – Equity Accumulation: 6.1m UK adults (13.27%)

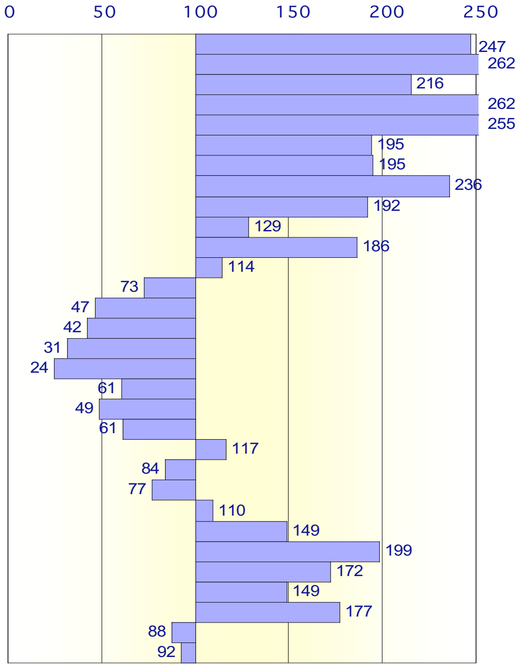
- ❑ People at the stage of their careers when they are able to add significantly to their net worth.
- ❑ Most are in their 40s–50s, married, good jobs and own their own homes
- ❑ However, some are personable young people and well educated who are gaining personal satisfaction from participating in new entrepreneurial ventures
- ❑ Often beneficiaries of deceased parents and their pension funds are now worth substantial amounts.
- ❑ Can consider outlay on home extensions or second homes from own capital resources.
- ❑ Wide variety of savings and investments but prefer low risk accounts such as fixed term bonds or unit trusts.
- ❑ Regular incomes and high tax liabilities make them good market for tax exempt schemes – PEPs & ISAs.

Group G – Parental Dependency: 4.5m UK adults (9.77%)

- ❑ Young adults who live at home, or depend on parents to finance their expenditure.
- ❑ Many use current accounts without cheque books and many get overdrawn regularly.
- ❑ Few financial services products except credit card.
- ❑ Little loyalty to existing suppliers.
- ❑ Lack of stable address or bank account are obstacles to obtaining the loans they would like to take out.

Stocks and Shares

FSS Segment	Distribution (%)	Index
A1 Aspirant Millionaires	0.51%	247
A2 Women with Wealth	0.62%	262
A3 Owner/Investors	1.64%	216
A4 Higher Rate Salariat	0.93%	262
B5 Capital Gainers	1.74%	255
B6 Professional Heights	1.34%	195
B7 Wealth from the Land	1.71%	195
B8 Cusp of retirement	3.83%	236
B9 Upscale Middle Agers	5.48%	192
B10 Ready for Retirement	7.39%	129
C11 Equity Rich Elders	6.34%	186
C12 On Private Pensions	6.73%	114
C13 Greys Just Surviving	5.24%	73
C14 Subsisting Elders	2.09%	47
D15 Young Jobsearchers	1.55%	42
D16 Transient Lifestyles	1.39%	31
D17 Lone Parents in Debt	0.70%	24
D18 Hardened Cash Payers	3.31%	61
D19 Cash Strapped Mums	3.12%	49
E20 Anxious Breadwinners	3.12%	61
E21 Aspiring Mid Market	9.27%	117
E22 Wives on a Budget	5.91%	84
E23 Prospering Flatmates	4.28%	77
F24 Nest Forming Mothers	4.07%	110
F25 Juggling Work & Home	3.10%	149
F26 Women Flying High	1.59%	199
F27 Men Behaving Well	4.16%	172
F28 Urban Enterprise	3.30%	149
G29 Rich Kids at Home	1.57%	177
G30 Sons Still at Home	1.95%	88
G31 Girls Still at Home	2.01%	92
Formatted Sample Total	100.00%	100

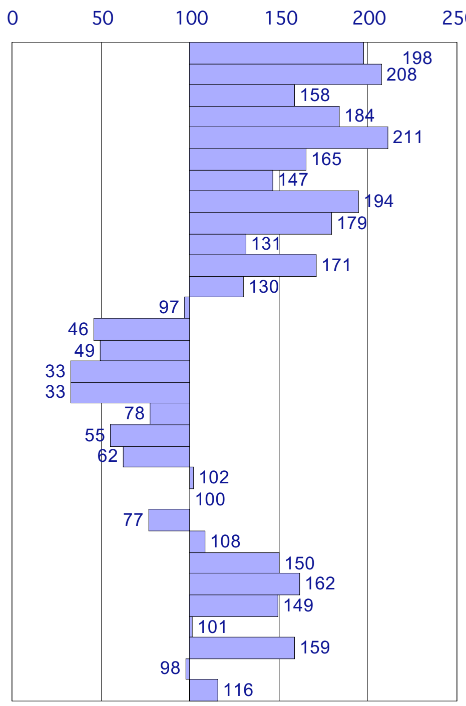


- ❑ 8,498 interviewees had stocks and shares.
- ❑ Significant market segments include:

1. (Group A) The financial elite.
2. (Group B) People in later middle age (families grown up, mortgages close to being paid off) with financial concerns about impending retirement
3. Group C11 – Equity rich elders; .Typically in early retirement years.
4. (Group F: 25-28) Equity Accumulation: People at the stage of their careers when able to add significantly to their net worth. Most of are in 40s & 50s, are in good jobs, are married and own their own homes.
5. Group G29 – Rich kids at home

ISAs

FSS Segment	Distribution (%)	Index
A1 Aspirant Millionaires	0.41%	197.66
A2 Women with Wealth	0.49%	207.54
A3 Owner/Investors	1.20%	158.41
A4 Higher Rate Salariat	0.65%	183.79
B5 Capital Gainers	1.44%	211.43
B6 Professional Heights	1.14%	165.02
B7 Wealth from the Land	1.29%	146.74
B8 Cusp of retirement	3.16%	194.47
B9 Upscale Middle Agers	5.11%	179.31
B10 Ready for Retirement	7.56%	131.46
C11 Equity Rich Elders	5.82%	171.11
C12 On Private Pensions	7.68%	130.37
C13 Greys Just Surviving	6.99%	96.8
C14 Subsisting Elders	2.06%	46.06
D15 Young Jobsearchers	1.81%	49.24
D16 Transient Lifestyles	1.45%	32.75
D17 Lone Parents in Debt	0.95%	32.81
D18 Hardened Cash Payers	4.23%	77.64
D19 Cash Strapped Mums	3.54%	55.35
E20 Anxious Breadwinners	3.17%	62.3
E21 Aspiring Mid Market	8.13%	102.16
E22 Wives on a Budget	7.07%	100.17
E23 Prospering Flatmates	4.28%	76.92
F24 Nest Forming Mothers	4.02%	108.28
F25 Juggling Work & Home	3.12%	150.42
F26 Women Flying High	1.30%	161.61
F27 Men Behaving Well	3.60%	149.25
F28 Urban Enterprise	2.24%	101.48
G29 Rich Kids at Home	1.41%	159.08
G30 Sons Still at Home	2.17%	97.85
G31 Girls Still at Home	2.51%	115.7
Formatted Sample Total	100.00%	100



- ❑ 9,473 interviewees had ISAs
- ❑ Significant market segments include:

1. (Group A) The financial elite.
2. (Group B) People in later middle age (families grown up, mortgages close to being paid off) with financial concerns about impending retirement
3. Group C11& C12 – Equity rich elders and on private pensions (longer retired).
4. (Group F: 25-27) Equity Accumulation: People at the stage of their careers when able to add significantly to their net worth. Most of are in 40s & 50s, are in good jobs, are married and own their own homes.
5. Group G29 – Rich kids at home

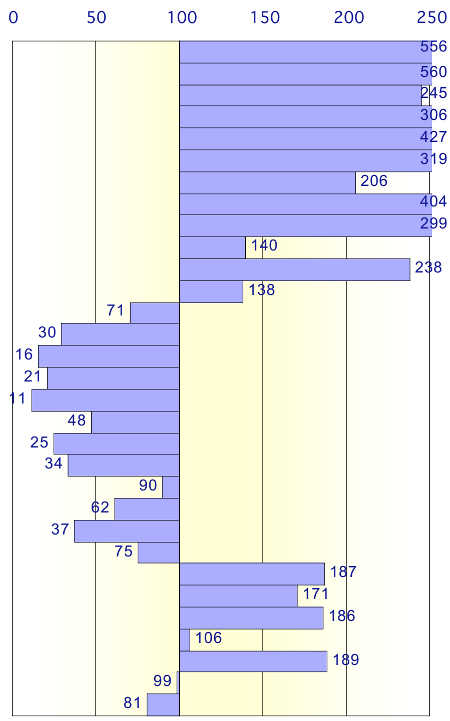
Profile of ISAs investors

FSS	Cash		Stocks & Shares	
	%	Index	%	Index
A1 Aspirant Millionaires	0.32%	78.2	0.81%	199.0
A2 Women with Wealth	0.35%	71.9	0.56%	115.7
A3 Owner/Investors	0.99%	82.6	2.29%	190.6
A4 Higher Rate Salariat	0.52%	80.5	0.97%	148.4
B5 Capital Gainers	1.24%	85.9	1.81%	125.4
B6 Professional Heights	1.16%	101.7	1.10%	97.2
B7 Wealth from the Land	1.16%	90.0	1.92%	149.3
B8 Cusp of retirement	2.86%	90.5	4.15%	131.5
B9 Upscale Middle Agers	5.01%	98.1	7.44%	145.5
B10 Ready for Retirement	7.65%	101.2	6.13%	81.2
C11 Equity Rich Elders	5.68%	97.6	6.14%	105.5
C12 On Private Pensions	7.75%	100.9	6.51%	84.8
C13 Greys Just Surviving	7.24%	103.6	4.56%	65.3
C14 Subsisting Elders	1.93%	93.8	1.33%	64.4
D15 Young Jobsearchers	2.07%	114.4	0.92%	51.0
D16 Transient Lifestyles	1.39%	96.0	1.83%	126.1
D17 Lone Parents in Debt	0.95%	100.6	0.66%	69.3
D18 Hardened Cash Payers	4.14%	97.9	3.29%	77.7
D19 Cash Strapped Mums	3.82%	108.0	2.50%	70.5
E20 Anxious Breadwinners	3.20%	101.1	3.31%	104.5
E21 Aspiring Mid Market	8.30%	102.1	8.80%	108.2
E22 Wives on a Budget	7.40%	104.7	6.71%	94.9
E23 Prospering Flatmates	3.95%	92.3	5.11%	119.3
F24 Nest Forming Mothers	4.18%	104.0	3.17%	78.9
F25 Juggling Work & Home	3.26%	104.3	2.92%	93.4
F26 Women Flying High	1.21%	93.3	1.57%	120.9
F27 Men Behaving Well	3.60%	99.8	4.72%	130.9
F28 Urban Enterprise	2.10%	93.6	3.27%	146.0
G29 Rich Kids at Home	1.36%	97.0	1.40%	99.6
G30 Sons Still at Home	2.35%	108.0	2.03%	93.3
G31 Girls Still at Home	2.85%	113.3	2.07%	82.2
Formatted Sample Total	100% (6909)	100	100% (1840)	100

- ❑ Propensity to Invest in cash ISAs is uniformly distributed, with the only exception of the financial elite which is less inclined
- ❑ Propensity to Invest in Equity ISAs has great variations
  - The most inclined are:
    - the financial elite (Group A)
    - the asset rich families (Group B)
    - people in their 40s and 50s in good jobs (Group F)
  - The least inclined are:
    - pensioners (group C) with the exception of equity rich elders.
    - people who have virtually no net worth, with short term financial horizons (Group D), with the exception of the transient lyfestyle group.

PEPs - Similar profile to ISAs

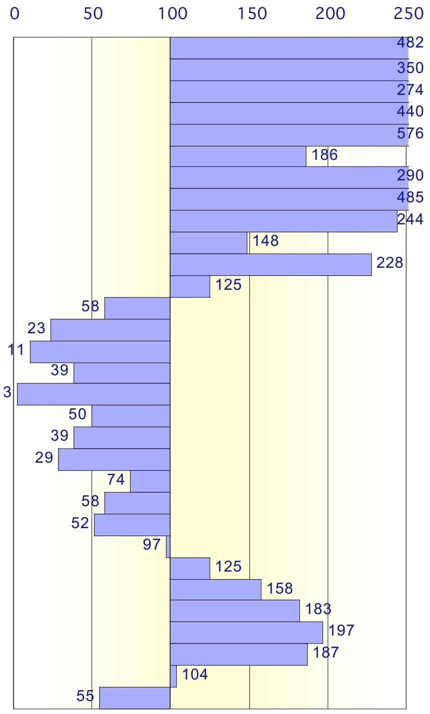
FSS Segment	Distribution (%)	Index
A1 Aspirant Millionaires	1.14%	556.01
A2 Women with Wealth	1.32%	560.39
A3 Owner/Investors	1.86%	245.09
A4 Higher Rate Salariat	1.09%	306.39
B5 Capital Gainers	2.91%	426.84
B6 Professional Heights	2.19%	318.74
B7 Wealth from the Land	1.81%	205.8
B8 Cusp of retirement	6.56%	403.77
B9 Upscale Middle Agers	8.53%	299.28
B10 Ready for Retirement	8.05%	140.01
C11 Equity Rich Elders	8.10%	238.13
C12 On Private Pensions	8.14%	138.19
C13 Greys Just Surviving	5.13%	71.01
C14 Subsisting Elders	1.33%	29.77
D15 Young Jobsearchers	0.58%	15.91
D16 Transient Lifestyles	0.92%	20.85
D17 Lone Parents in Debt	0.33%	11.39
D18 Hardened Cash Payers	2.59%	47.57
D19 Cash Strapped Mums	1.60%	25.04
E20 Anxious Breadwinners	1.72%	33.77
E21 Aspiring Mid Market	7.17%	90.16
E22 Wives on a Budget	4.35%	61.59
E23 Prospering Flatmates	2.07%	37.09
F24 Nest Forming Mothers	2.80%	75.39
F25 Juggling Work & Home	3.88%	186.93
F26 Women Flying High	1.37%	170.78
F27 Men Behaving Well	4.50%	186.42
F28 Urban Enterprise	2.35%	106.31
G29 Rich Kids at Home	1.67%	188.52
G30 Sons Still at Home	2.19%	98.56
G31 Girls Still at Home	1.75%	80.63
Formatted Sample Total	100.00%	100



- ❑ 2,070 interviewees had PEPs.
- ❑ Significant market segments include:
  1. (Group A) The financial elite.
  2. (Group B) People in later middle age (families grown up, mortgages close to being paid off) with financial concerns about impending retirement
  3. Group C11& C12 – Equity rich elders and on private pensions (longer retired).
  4. (Group F: 25-27) Equity Accumulation: People at the stage of their careers when able to add significantly to their net worth. Most of are in 40s & 50s, are in good jobs, are married and own their own homes.
  5. Group G29 – Rich kids at home

Unit Trusts

FSS Segment	Distribution (%)	Index
A1 Aspirant Millionaires	0.99%	482.02
A2 Women with Wealth	0.82%	350.41
A3 Owner/Investors	2.08%	273.78
A4 Higher Rate Salariat	1.56%	439.86
B5 Capital Gainers	3.93%	575.96
B6 Professional Heights	1.28%	186.41
B7 Wealth from the Land	2.55%	290.12
B8 Cusp of retirement	7.88%	485.28
B9 Upscale Middle Agers	6.96%	244.03
B10 Ready for Retirement	8.53%	148.4
C11 Equity Rich Elders	7.76%	228.23
C12 On Private Pensions	7.39%	125.38
C13 Greys Just Surviving	4.19%	58.01
C14 Subsisting Elders	1.04%	23.32
D15 Young Jobsearchers	0.40%	10.91
D16 Transient Lifestyles	1.71%	38.6
D17 Lone Parents in Debt	0.08%	2.75
D18 Hardened Cash Payers	2.71%	49.72
D19 Cash Strapped Mums	2.46%	38.5
E20 Anxious Breadwinners	1.46%	28.79
E21 Aspiring Mid Market	5.91%	74.29
E22 Wives on a Budget	4.08%	57.77
E23 Prospering Flatmates	2.87%	51.57
F24 Nest Forming Mothers	3.60%	97.13
F25 Juggling Work & Home	2.59%	124.82
F26 Women Flying High	1.26%	157.5
F27 Men Behaving Well	4.41%	182.55
F28 Urban Enterprise	4.34%	196.6
G29 Rich Kids at Home	1.65%	186.87
G30 Sons Still at Home	2.30%	103.67
G31 Girls Still at Home	1.18%	54.53
Formatted Sample Total	100.00%	100

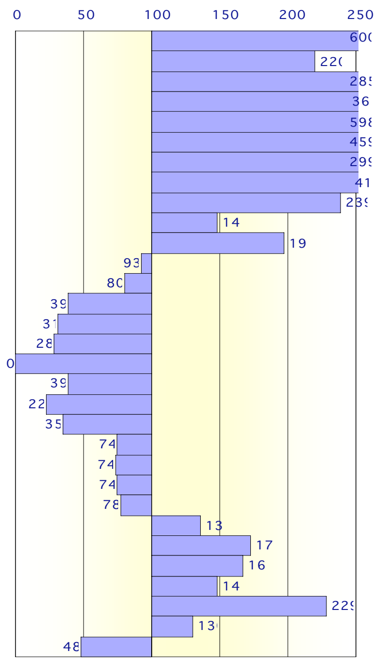


- 904 interviewees had Unit Trusts
- Significant market segments include:
  1. (Group A) The financial elite.
  2. (Group B) People in later middle age (families grown up, mortgages close to being paid off) with financial concerns about impending retirement
  3. Group C11& C12 – Equity rich elders and on private pensions (longer retired).
  4. (Group F: 25-28) Equity Accumulation: People at the stage of their careers when able to add significantly to their net worth. Most of are in 40s & 50s, are in good jobs, are married and own their own homes.
  5. Group G29 – Rich kids at home

Investment Trusts

- 481 interviewed had Investment Trusts

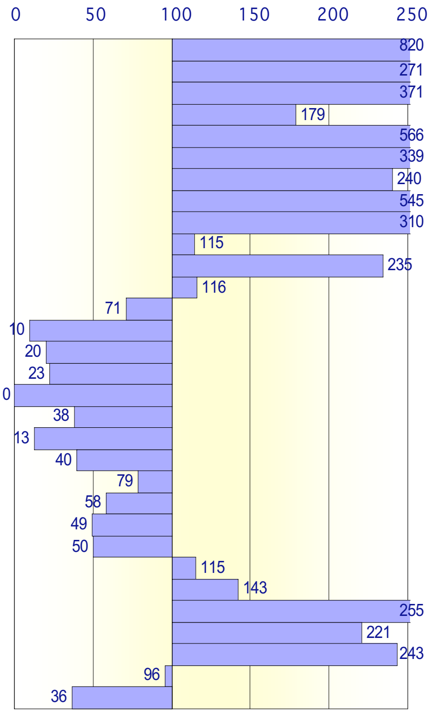
FSS Segment	Distribution (%)	Index
A1 Aspirant Millionaires	1.23%	600
A2 Women with Wealth	0.52%	220
A3 Owner/Investors	2.16%	285
A4 Higher Rate Salariat	1.28%	361
B5 Capital Gainers	4.08%	598
B6 Professional Heights	3.16%	459
B7 Wealth from the Land	2.62%	299
B8 Cusp of retirement	6.67%	411
B9 Upscale Middle Agers	6.81%	239
B10 Ready for Retirement	8.52%	148
C11 Equity Rich Elders	6.70%	197
C12 On Private Pensions	5.47%	93
C13 Greys Just Surviving	5.77%	80
C14 Subsisting Elders	1.73%	39
D15 Young Jobsearchers	1.15%	31
D16 Transient Lifestyles	1.25%	28
D17 Lone Parents in Debt	0.00%	0
D18 Hardened Cash Payers	2.11%	39
D19 Cash Strapped Mums	1.42%	22
E20 Anxious Breadwinners	1.76%	35
E21 Aspiring Mid Market	5.90%	74
E22 Wives on a Budget	5.19%	74
E23 Prospering Flatmates	4.14%	74
F24 Nest Forming Mothers	2.88%	78
F25 Juggling Work & Home	2.82%	136
F26 Women Flying High	1.38%	172
F27 Men Behaving Well	4.03%	167
F28 Urban Enterprise	3.27%	148
G29 Rich Kids at Home	2.02%	229
G30 Sons Still at Home	2.90%	130
G31 Girls Still at Home	1.05%	48
Formatted Sample Total	100.00%	100



- *Group B, Asset Rich Families* is the largest purchaser, accounting for almost 30% of all Investment Trusts.
- *Group A* also display high propensity to invest, between two and five times above average.
- *Welfare Borderline* class again showing extremely low actual (5.93%) and propensity (indexes 0-39) to buy investment trusts.
- Large difference between propensity of *Sons Still at Home* (index 130) and *Girls Still at Home* (index 48) to purchase I.T.s shows gender bias amongst the young for this type of investment.

OEICs

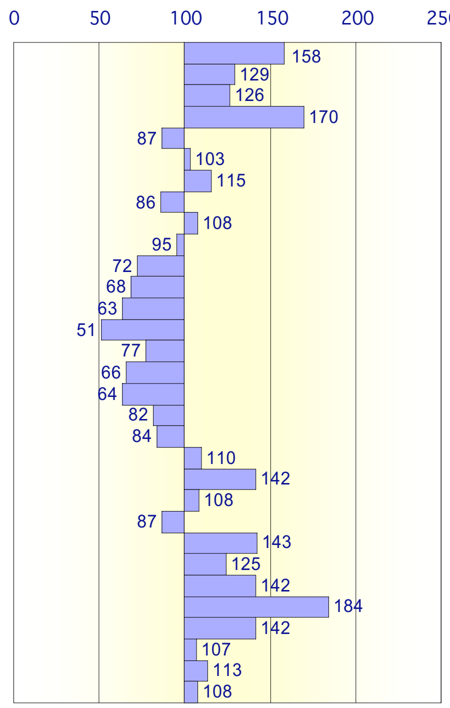
FSS Segment	Distribution (%)	Index
A1 Aspirant Millionaires	1.68%	819.92
A2 Women with Wealth	0.64%	270.85
A3 Owner/Investors	2.81%	370.57
A4 Higher Rate Salariat	0.63%	178.65
B5 Capital Gainers	3.86%	565.78
B6 Professional Heights	2.33%	338.89
B7 Wealth from the Land	2.11%	239.99
B8 Cusp of retirement	8.85%	545.18
B9 Upscale Middle Agers	8.83%	309.63
B10 Ready for Retirement	6.59%	114.59
C11 Equity Rich Elders	7.98%	234.64
C12 On Private Pensions	6.82%	115.76
C13 Greys Just Surviving	5.11%	70.85
C14 Subsisting Elders	0.44%	9.8
D15 Young Jobsearchers	0.74%	20.26
D16 Transient Lifestyles	1.00%	22.66
D17 Lone Parents in Debt	0.00%	0
D18 Hardened Cash Payers	2.09%	38.38
D19 Cash Strapped Mums	0.81%	12.59
E20 Anxious Breadwinners	2.03%	39.97
E21 Aspiring Mid Market	6.25%	78.61
E22 Wives on a Budget	4.13%	58.47
E23 Prospering Flatmates	2.75%	49.46
F24 Nest Forming Mothers	1.85%	49.98
F25 Juggling Work & Home	2.40%	115.36
F26 Women Flying High	1.14%	142.55
F27 Men Behaving Well	6.15%	254.5
F28 Urban Enterprise	4.89%	221.17
G29 Rich Kids at Home	2.15%	242.97
G30 Sons Still at Home	2.13%	96.02
G31 Girls Still at Home	0.79%	36.41
Formatted Sample Total	100.00%	100



- 385 interviewed had OEICs
- Combined *Group B* (33%) and *Group C* (20%) account for over half of all OEICs.
- Highest propensity to take OEICs found in *Groups A & B*, especially *Aspirant Millionaires* at 7 times the average.
- *Men Behaving Well*, *Urban Enterprise* & *Rich Kids at Home* all double the average.
- *Groups D & E* showing low investment level and below average propensity to buy.

Company pension scheme – FSS profile

FSS Segment	Distribution (%)	Index
A1 Aspirant Millionaires	0.37%	158.28
A2 Women with Wealth	0.33%	129.22
A3 Owner/Investors	1.06%	126.27
A4 Higher Rate Salariat	0.64%	169.66
B5 Capital Gainers	0.52%	86.64
B6 Professional Heights	0.79%	103.32
B7 Wealth from the Land	1.07%	115.32
B8 Cusp of retirement	0.97%	85.69
B9 Upscale Middle Agers	3.13%	107.82
B10 Ready for Retirement	5.75%	95.41
C11 Equity Rich Elders	1.72%	72.25
C12 On Private Pensions	2.76%	68.4
C13 Greys Just Surviving	3.08%	63.35
C14 Subsisting Elders	1.64%	51.11
D15 Young Jobsearchers	3.14%	77.42
D16 Transient Lifestyles	3.17%	65.95
D17 Lone Parents in Debt	2.03%	63.9
D18 Hardened Cash Payers	4.68%	81.85
D19 Cash Strapped Mums	5.90%	83.8
E20 Anxious Breadwinners	6.23%	110.14
E21 Aspiring Mid Market	12.41%	141.65
E22 Wives on a Budget	8.45%	108.1
E23 Prospering Flatmates	5.32%	86.83
F24 Nest Forming Mothers	5.88%	142.53
F25 Juggling Work & Home	2.88%	124.63
F26 Women Flying High	1.29%	141.57
F27 Men Behaving Well	4.90%	184.1
F28 Urban Enterprise	3.48%	141.5
G29 Rich Kids at Home	1.04%	107.1
G30 Sons Still at Home	2.81%	113.25
G31 Girls Still at Home	2.56%	107.83
Formatted Sample Total	100.00%	100



- 9,585 interviewed were enrolled in a company pension, making this the most popular form of investment.
- Propensity to invest in a company pension is closer to average in all groups than any other type of investment.
- Highest propensity to fund a company pension found in *Groups A & F*.
- *Aspiring Mid Market* (12.41%) alone account for almost an eighth of the market.
- *Groups C & D* showing lower investment levels but generally still close to average.

Commercial property target market – some sophisticated segments likely to be more attracted to property investment

- ❑ **High risk**: these segments (A1, A4, B5, B6, B9, F28) are likely to have a high risk appetite and be attracted to property investment from a growth perspective
- ❑ **Moderate risk**: these segments (A2, A3, B7, C11, F27) are likely to be moderately attracted to property investment from both growth and income perspectives
- ❑ **Low risk**: these segments (B8, B10, C12, F25, F26, G29) would probably be more attracted to the income attributes of property investment

- **High risk**: these segments (A1, A4, B5, B6, B9, F28) are likely to have a high risk appetite and be attracted to property investment from a growth perspective

Type A1 – Aspirant Millionaires: approx 250,000 UK adults (0.55%)

- Aspirant Millionaires are people whose earnings and assets way exceed what could be earned from a salaried position. Most of these people are in later middle age and are either owners of their own companies or directors or partners in professional practices. But this group also increasingly includes the younger rich, such as city high fliers and media and sports personalities.

- Assets take the form of illiquid assets, such as private companies, as well as stocks and shares in publicly quoted companies, investment trusts and residential property. These people outsource the management of their wealth to financial advisers, a key part of whose role is to minimise tax liabilities.

- Mostly men, these people are precisely the types of customer that most financial services organisation would like to recruit – they use a wide range of different personal financial services, they use them in a large way and they constitute good credit risks.

- These people are particularly likely to live in very expensive houses, to apply for very large mortgages and to have high holdings of stocks and shares. They are particularly likely to use Amex and Diners cards, to take out health insurance and to pay heavy premia for both home and car insurance. Very few have County Court Judgements.

- People in this group pay their bills by post and are enthusiasts for telephone banking.
  You would find many of these people in the MOSAIC type Clever Capitalists.

Type A4 – Higher Rate Salariat: approx 260,000 UK adults (0.57%)

- Higher Rate Salariat contains highly paid mid-career executives and managers whose financial interest in the company they work for is restricted to annual bonuses and profit related pay rather than the appreciation of equity shares.
- As a result these people use their job security and high salaries to build up significant capital investments both in residential property and in stocks and shares. They live in fairly expensive but not outrageously luxurious homes on which they still have a mortgage which is now low in relation to the house value. Surplus income is invested in a variety of savings schemes in such a way as to minimise tax liability, for example through children's accounts, personal pensions, Peps, Tessas and Isas.
- This is not a particularly good market for personal loans whilst most credit card balances are paid off at the end of the month.
- Brand loyalty counts less than convenience and competitive rates for these people who are enthusiasts for internet and telephone banking and who are also particularly like to have current accounts with supermarket chains.
- The MOSAIC group High Income Families is one where you will find many of this type of person living.

Type B5 – Capital Gainers: approx 600,000 UK adults (1.32%)

•Capital Gainers are people who have been fortunate, or perhaps prudent, in achieving high net worth through the appreciation of capital assets rather than from income from employment or the development of their own businesses. These could be viewed as professional, as distinct from amateur, investors.

•Including both men and women, this group is typically in their 50s and 60s. They deal regularly in shares and have assembled formidable portfolios of investment and unit trusts. These people are considered risk takers who would prefer speculative to fixed interest investments and who take care with the tax efficiency of their investment spreads. To them the term 'bed and breakfast' would mean more than holiday accommodation.

•This group is a barren market for overdrafts and personal loans and would feel disgrace were their liquidity to be so mismanaged that they had to pay bank interest rates on credit card balances. Their next car would be paid for in cash and for them there will be no problem in ensuring their income in retirement is adequate.

•Managing their own personal finances efficiently is one of the great pleasures of life for this group, which has the lowest incidence of bad debt of any financial MOSAIC segment.

•Capital Gainers can be found in the MOSAIC types Clever Capitalists and Gentrified Villages.

Type B6 – Professional Heights: approx 520,000 UK adults (1.13%)

- Professional Heights consists of middle aged men who have reached the peak of their career in professional or public service positions. Rewarded over the years with increments on official salary scales and with children often at university or beyond and mortgages largely paid off, this group now experiences what might be described as a positive cash flow and look for savings instruments that minimise tax and maximise retirement income.
- It is at this stage of the life cycle that the family is likely to inherit substantial lump sums from deceased parents or to benefit from the maturity of life insurance or mortgage endowment policies.
- As a result this group has very significant net worth in financial products as well as hidden assets in the form of house price appreciation. It is in bureaux in these homes that you will find investment certificates in stocks, shares and unit trust, all available forms of tax exempt savings scheme and life insurance policies.
- Although many people use Gold cards, these are invariably paid off in full at the end of the month and mailings offering loans or overdrafts are considered an unwelcome intrusion rather than a lifeline to the purchase of some otherwise unaffordable necessity.
- The MOSAIC type Gentrified Villages is the one where Professional Heights is most likely to choose to live.

Type B9 – Upscale Middle Agers: 1.7m UK adults (3.68%)

- Upscale Middle Agers are typically middle to upper middle income empty nesters whose children are off their hands and whose mortgages are now fully paid off. With fewer outgoings and with retirement impending, this group is busy adding to its existing pension provision through savings in tax exempt schemes.
- Lump sum investments, Tessas, unit trusts, Peps and Isas have all sold well to these people. Privatisation issues have also proved popular in the past. By contrast this is not a good target group for selling children's accounts.
- Conservative in outlook, these people are particularly loyal to their existing bank and tend not to question the objectivity of the advice they get from it. To them the convenience of 24 hour telephone banking is not a material benefit and they are less likely than others to consider switching to a different supplier. They pay bills through the branch and, though they like advice face-to-face, they would look to a branch manager rather than an independent financial adviser to provide it.
- In common with other people approaching retirement they have no need for instruments of credit and though they hold a lot of credit cards these are used for convenience rather than for finance.
- These people are believers in self provision and have an above average likelihood to hold private pensions and private health care policies.

Type F28 – Urban Enterprise: 1.4m UK adults (3.04%)

- Urban Enterprise consists mostly of well educated and personable young people who are gaining personal satisfaction from participating in new entrepreneurial ventures, many of them in innovative service companies in large cities.

- Working with enthusiastic young colleagues in pioneering companies, these people find it difficult to separate their work and leisure lives and are happy to postpone marriage, family and home ownership to later so that they have more time to build up their skill base and enjoy the excitement of developing small service businesses.

- This group is a good market for financial services companies to sell to as most of their members have high earnings growth opportunities. At present their choice of financial services is motivated more by convenience than by value. They are too busy with their work to avoid getting their account overdrawn, credit cards are a convenience method of payment at smart restaurants, telephone banking is convenient for people too busy to visit the bank in the lunch hour. The internet registers a high level of interest among this group as a transaction channel.

- Though many of this group are single or have partners, many more are starting families and in the market for a mortgage. They set demanding standards of their financial services provider and are well aware of the innovations introduced by each of the mainstream financial services suppliers.

- **Moderate risk**: these segments (A2, A3, B7, C11, F27) are likely to be moderately attracted to property investment from both growth and income perspectives

Type A2 – Women with Wealth: approx 350,000 UK adults (0.75%)

- Women with Wealth contains very high proportions of wealthy women, although this segment is not comprised exclusively of females. Women with Wealth is a particularly important market for luxury goods, for home improvement products and for upmarket fashion chains and department stores and many of these individuals have awesome spending power.
- Some of those within the Women with Wealth segment achieve their wealth through their marriage to captains of industry, others play an important role as directors in family owned businesses whilst many have their own distinct careers in business and other professions. Today little of their wealth is inherited.
- Individuals in this group are particularly likely to be company directors and/or shareholders and to live in houses with high valuations and which have appreciated significantly in value in recent years. Despite high net worth, many use their homes as collateral for loans. For the savings company they are better targets for investments in stocks and shares than for instant access savings schemes and gold card and store card operators find many of their best customers among this group.
- Individuals in this group are particularly likely to have private health insurance and to send their children to private schools.
- They find it convenient to bank with Tesco or Sainsbury and they may well operate a current account through a telephone bank.
- You would find many of these women living in the MOSAIC types Clever Capitalists, Chattering Classes and Gentrified Villages.

Type A3 – Owner/Investors: nearly 600,000 UK adults (1.26%)

- Owner / Investors is a group of middle aged men whose financial behaviour is focussed on the financial needs of the business that they both own and manage.
- Although they are worth a lot of money, much of the capital value is locked up in illiquid assets against which they often want to borrow. For example they have loans secured against their houses, they seldom pay off their balances on their credit cards at the end of each month and many have a personal loan. It is not surprising that this group should have a high incidence of County Court Judgements.
- The group use their business to purchase health insurance for themselves and to lease the cars that they drive. By contrast they don't bother about the tax saving opportunities of Tessas and Isas and prefer lump sum long term investments to regular monthly payments.
- These people are particularly strong users of Amex and Diners Club cards and tend to have a large number of different credit cards.

Type B7 – Wealth from the land: 1.1m UK adults (2.54%)

- Wealth from the Land describes people who live in isolated rural locations where agriculture and tourism remain bedrocks of the local economy. In these areas of small, family businesses business and private finance are strongly intertwined and most financial assets are held in an illiquid form.
- Calculating family incomes in these areas is quite hard since they vary from season to season and reflect return on the capital value of the land as well as labour input.
- Loans may be secured as a charge against property or taken in the form of an arranged overdraft. Credit cards too are an important line of credit and new vehicles are more likely to be leased than among other Financial MOSAIC segments.
- This is also a fertile area for the sale of private pensions and private health and disability insurance. Nonetheless many people in this category are worried about the adequacy of their incomes in retirement.
- With increasingly poor access to local banking services it is hardly surprising that people are very interested in the possibility of internet and phone based banking and that most bills are paid through the post rather than over the counter.

Type C11 – Equity Rich Elders: 1.8m UK adults (4.02%)

- Equity Rich Elders are typically in their early retirement years. Their good health allows them to live an active lifestyle and to continue to manage a large house and an extensive garden. These people tend to have the security of substantial equity capital. Their houses, when they come to sell them, will also provide a second tranche of capital. Meanwhile many of them benefit from occupational pensions which are either final salary based or index linked.
- These people often rely on Independent Financial Advisers to organise the conversion of equity capital into current income. They are not afraid to move funds around as better rates materialise.
- Given their age many people in this group are content to tie up money in long term investments such as unit trusts or tracker funds – their anxieties are that inflation erodes the long term value of their capital.
- Today a more serious anxiety is the reduction of annuity rates offered against lump sum investments
- Among these people there is no need for credit so credit cards are used as a convenient payment method rather than a line of credit. These are not people to whom you would want to promote a mortgage, a personal loan or an overdraft.
- By contrast a key advisory need is for taxation planning. This may involve the selection of tax exempt savings schemes, the management of capital gains tax liabilities, inheritance tax planning and the use of offshore funds.
- In general these people are keen to access this advice face to face and to use people of their own background and generation that they can trust.

Type F27 – Men Behaving well: 1.2m UK adults (2.72%)

- Men Behaving Well is a group of middle income owner occupiers, most of whom are now beginning to see a significant equity margin in the homes they may have bought ten to fifteen years previously.
- Typically married and with two, three or more children, they are moving across the lifestage divide that separates borrowers from savers. Heavy users of credit cards, personal loans and overdrafts, they are nevertheless adding savings and investment accounts to their portfolio of savings products. They are particularly confident that their own personal financial circumstances will improve.
- This midmarket group is attracted by well known financial brands selling straightforward financial services products. People compare notes with friends and neighbours but have confidence to buy products over the phone and through the post as well as face to face. They register particular interest in internet banking

- **Low risk**: these segments (B8, B10, C12, F25, F26, G29) would probably be more attracted to the income attributes of property investment

Type B8 – Cusp of Retirement: approx 910,000 UK adults (1.99%)

- Cusp of Retirement describes a group of people who are crossing the big divide between the employed and the retired. In their fifties and sixties these people have benefitted from appreciating property prices, from the maturity of life and endowment policies, from inheritances and from the appreciating value of the privatisation issues they may have purchased.
- With children off their hands and mortgage repayments now completed, these people have been able to supplement private or company pension schemes with substantial additional investments.
- On retirement many of these people are looking to downsize their accommodation in order to release more equity.
- Cusp of Retirement, whilst good for savings products, provides few opportunities to the credit grantor, who will nonetheless target a lot of his direct mail at these people on account of their exemplary credit record.

Type B10 – Ready for Retirement: 2.7m UK adults (5.88%)

- Ready for Retirement consists of lower income empty nesters most of whom are approaching retirement age. Mostly in their fifties and sixties and in manual jobs on moderate incomes, these are nevertheless owner occupiers who now tend to own their homes outright.
- With children off their hands and mortgage repayments completed, this thrifty group has been able to make modest savings in the form of tax exempt savings, unit trusts and lump sum investments. Some are members of company schemes, some have provided privately whilst others have no pension provision other than the basic state scheme. Overall however the majority feel they are adequately provided for when they retire.
- This, like other types of thrifty empty nesters, is a poor market for credit products, particularly personal loans. The use of credit cards is quite widespread but one suspects that average transaction values are low and that the typical month end balance is not substantial. Debt levels are low.
- With its elderly, blue collar profile, this group is rooted in the mindset of face to face banking and there is little interest in newfangled channels such as the telephone and the internet for transaction processing.

Type C12 – On Private Pensions: 2.7m UK adults (5.95%)

- On Private Pensions are elderly people, mostly but not all women, who typically have been retired for some time. For this reason their original equity is losing its value and inflation is undermining the value of fixed income annuities based on private or company pension schemes.
- This group are therefore particularly anxious about the careful management of what savings they still have, about equity withdrawal from their houses and about the impact on their financial circumstances of long term illness and disability.
- Here you will find careful use of tax exempt schemes but a greater reluctance to invest in higher risk shares and in limited access investments that would be the case among the younger and fitter elderly.
- This is not a good group to sell mortgages, loans and credit cards to.

Type F25 – Juggling Work & Home:1m UK adults (2.28%)

- Juggling Home & Work describes married women, many with older children, whose qualifications did not allow them to earn enough when their children were younger to pay for professional child care. Their careers interrupted by children they have now returned to work in part time or routine full time administrative jobs and are comfortably off as they approach retirement and as grown up children contribute to the family income.
- These people tend to live in mid value houses on which they still have a small mortgage. They are currently adding to the value of their savings and investment accounts which they have taken out with mainstream financial services providers.
- They are particularly keen on tax exempt savings schemes and on opening accounts for their children. They enjoy visiting the banking parlour on a monthly basis to add to their savings account and they will have good knowledge of the interest rates they can obtain from rival suppliers. For these people banking is a face to face activity and they welcome advice from people they trust.
- Most people in this group are satisfied that they will be adequately provided for in their retirement.

Type F26 – Women Flying High: approx 600,000 UK adults (1.25%)

- Women Flying High include a number who work in well paid professional and management positions and who can afford from their incomes to pay others to help with looking after homes and children.
- Typically well educated, this group consists mostly of career women with professional or managerial partners and whose earnings make significant contributions to the household income.
- These women tend to have above average usage across all savings instruments but are a particularly good market for regular savings schemes, for children's accounts and for life cover. But they are also extensive users of personal credit, whether in the form of overdrafts, personal loans and outstanding credit card balances. They don't use a large number of different credit cards but their wallets do bulge with storecard plastic.
- Many of these women live in the MOSAIC type Rising Materialists.

Type G29 – Rich Kids at Home: nearly 1m UK adults (2.07%)

- Rich Kids at Home are young adults who have the privilege of being able to rely on relatively wealthy parents whilst they live at home or attend college.
- These 'kids', typically aged 18 to 25, have a much wider range of financial accounts than their contemporaries from poorer backgrounds. They are more likely to have access to an Amex or Diners Club card and to storecards and credit cards generally.
- With greater access to cars and to telephones, they are extremely interested in internet and telephone banking and are the most likely of all groups to consider changing to a new supplier. They are also much more likely than poorer students to bank with Tesco or Sainsburys and to pay bills through the post rather than at a Post Office.
- These children are well enough off for many to be considering taking out an Isa. Many claim that they would welcome financial advice on their savings and investment strategy.

Estimating market size - Approach

- Stage 1: Breaking Mori FTS sample into Financial Strategy Segments and active investors. For example there are 2,707 “On Private Pensions” individuals in the survey and 572 own shares.
- Stage 2: Number of people per FSS Type divided by investment responses to give product penetration rates. For example, 21% of “On Private Pensions” individuals own shares
- Stage 3: Divide FSS profiles by estimated risk appetite and apply product penetration percentages to total FSS market size. For example, there are 2.7m “On Private Pensions” individuals in the UK. Assuming a 21% product penetration rate implies that 570,000 own shares.

Mori FTS Active Investors by FSS Type

		Mori Sample %	Sample Number	Stock/Shares Number	Equity ISAs Number	Unit Trusts Number
A1	Aspirant Millionaires	0.21%	97	43	15	9
A1	Women with Wealth	0.23%	106	53	10	7
A3	Owner/Investors	0.76%	349	139	42	19
A4	Higher Rate Salariat	0.35%	161	79	18	14
B5	Capital Gainers	0.68%	313	148	33	36
B6	Professional Heights	0.69%	317	114	20	12
B7	Wealth from the Land	0.88%	404	145	35	23
B8	Cusp of Retirement	1.62%	745	325	76	71
B9	Upscale Middle Agers	2.85%	1310	466	137	63
B10	Ready for Retirement	5.75%	2643	628	113	77
C11	Equity Rich Elders	3.40%	1563	539	113	70
C12	On Private Pensions	5.89%	2707	572	120	67
C13	Greys Just Surviving	7.22%	3319	445	84	38
C14	Subsisting Elders	4.47%	2055	178	24	9
D15	Young Jobsearchers	3.67%	1687	132	17	4
D16	Transient Lifestyles	4.43%	2036	118	34	15
D17	Lone Parents in Debt	2.88%	1324	59	12	1
D18	Hardened Cash Payers	5.45%	2505	281	61	24
D19	Cash Strapped Mums	6.40%	2942	265	46	22
E20	Anxious Breadwinners	5.09%	2340	265	61	13
E21	Aspiring Mid Market	7.96%	3659	788	162	53
E22	Wives on a Budget	7.06%	3245	502	123	37
E23	Prospering Flatmates	5.57%	2560	364	94	26
F24	Nest Forming Mothers	3.71%	1705	346	58	33
F25	Juggling Work & Home	2.08%	956	263	54	23
F26	Women Flying High	0.80%	368	135	29	11
F27	Men Behaving Well	2.42%	1112	354	87	40
F28	Urban Enterprise	2.21%	1016	280	60	39
G29	Rich Kids at Home	0.88%	404	133	26	15
G30	Sons Still at Home	2.22%	1020	166	37	21
G31	Girls Still at Home	2.17%	997	171	38	11
	TOTAL	1.00	45965	8497	1840	904

- Survey total was 45,965 people
- 8,497 of these had stocks/ shares (18.5%)
- 1,940 had Equity ISAs (4.2%)
- 904 had Unit trusts (2%)
- Some would have had more than one product.

Active Investors – FSS Penetration Rates

		Sample %	Sample Number	Stock/Shares Number	Stock/Shares %	Equity ISAs Number	Equity ISAs %	Unit Trusts Number	Unit Trusts %
A1	Aspirant Millionaires	0.21%	97	43	45	15	15	9	9
A1	Women with Wealth	0.23%	106	53	50	10	10	7	7
A3	Owner/Investors	0.76%	349	139	40	42	12	19	5
A4	Higher Rate Salariat	0.35%	161	79	49	18	11	14	9
B5	Capital Gainers	0.68%	313	148	47	33	11	36	11
B6	Professional Heights	0.69%	317	114	36	20	6	12	4
B7	Wealth from the Land	0.88%	404	145	36	35	9	23	6
B8	Cusp of Retirement	1.62%	745	325	44	76	10	71	10
B9	Upscale Middle Agers	2.85%	1310	466	36	137	10	63	5
B10	Ready for Retirement	5.75%	2643	628	24	113	4	77	3
C11	Equity Rich Elders	3.40%	1563	539	34	113	7	70	4
C12	On Private Pensions	5.89%	2707	572	21	120	4	67	2
F25	Juggling Work & Home	2.08%	956	263	28	54	6	23	2
F26	Women Flying High	0.80%	368	135	37	29	8	11	3
F27	Men Behaving Well	2.42%	1112	354	32	87	8	40	4
F28	Urban Enterprise	2.21%	1016	280	28	60	6	39	4
G29	Rich Kids at Home	0.88%	404	133	33	26	6	15	4
	TOTAL	0.32	14571	4417	30	988	7	596	4

- Number of people per FSS Type in the survey has been divided by investment responses to give penetration rates.
- Stocks/shares are owned by 21-50% of targeted FSS Types; Equity ISAs by 4% -15% and Unit Trusts by 2%-11% - significantly higher percentages than for the total sample (see previous slide - sample averages 18.5%, 4.2% and 2% respectively)

Segment 1: Higher risk appetite

Category	FSS Type	Population Number	Stock/Shares %	Stock/Shares Number	Equity ISAs %	Equity ISAs Number	Unit Trusts %	Unit Trusts Number
High Risk								
A1	Aspirant Millionaires	250000	45	112248	15	38601	9	23179
A4	Higher Rate Salariat	260000	49	127726	11	28845	9	22791
B5	Capital Gainers	600000	47	283845	11	63931	11	68199
B6	Professional Heights	520000	36	186702	6	33185	4	18972
B9	Upscale Middle Agers	1700000	36	604330	10	177651	5	81650
F28	Urban Enterprise	1400000	28	386491	6	82923	4	54071
	SEGMENT TOTAL	**4730000**	**36**	**1701341**	**9**	**425135**	**6**	**268862**

- High risk appetite segment (approx 4.7m people) is estimated to consist of:
  - 1.7 million shareholders
  - 425k equity ISA holders
  - 270k unit trust holders
- Overall market size likely to be 40-45% of the relevant FSS population

Segment 2: Medium risk appetite

Category	FSS Type	Population Number	Stock/Shares %	Stock/Shares Number	Equity ISAs %	Equity ISAs Number	Unit Trusts %	Unit Trusts Number
Med Risk								
A2	Women with Wealth	350000	50	174430	10	34113	7	24541
A3	Owner/Investors	600000	40	239371	12	72371	5	32296
B7	Wealth from the Land	1100000	36	395181	9	96073	6	62689
C11	Equity Rich Elders	1800000	34	620544	7	130123	4	80797
F27	Men Behaving Well	1200000	32	381372	8	93691	4	43008
	SEGMENT TOTAL	**5050000**	**36**	**1810897**	**8**	**426371**	**5**	**243331**

- Medium risk appetite segment (approx 5.1m people) is estimated to consist of:
  - 1.8 million shareholders
  - 425k equity ISA holders
  - 245k unit trust holders
- Overall market size likely to be 40-45% of the relevant FSS population
- Very similar penetration results to the Higher risk segment

Segment 3: Lower risk appetite

Category	FSS Type	Population Number	Stock/Shares %	Stock/Shares Number	Equity ISAs %	Equity ISAs Number	Unit Trusts %	Unit Trusts Number
Low Risk								
B8	Cusp of Retirement	910000	44	397754	10	93318	10	87055
B10	Ready for Retirement	2700000	24	641549	4	115225	3	78775
C12	On Private Pensions	2700000	21	570365	4	119459	2	66625
F25	Juggling Work & Home	1000000	28	275542	6	56197	2	24489
F26	Women Flying High	600000	37	220469	8	47136	3	18585
G29	Rich Kids at Home	1000000	33	329842	6	63685	4	36876
	SEGMENT TOTAL	**8910000**	**27**	**2435522**	**6**	**495020**	**4**	**312405**

- Lower risk appetite segment (approx 8.9m people) is estimated to consist of:
  - 2.4 million shareholders
  - 495k equity ISA holders
  - 312k unit trust holders
- Overall market size likely to be less than the others – at approx 30-35%, but still significant.

Segment 3: Lower risk appetite

Category	FSS Type	Population Number	Stock/Shares %	Stock/Shares Number	Equity ISAs %	Equity ISAs Number	Unit Trusts %	Unit Trusts Number
High Risk								
A1	Aspirant Millionaires	250000	45	112248	15	38601	9	23179
A4	Higher Rate Salariat	260000	49	127726	11	28845	9	22791
B5	Capital Gainers	600000	47	283845	11	63931	11	68199
B6	Professional Heights	520000	36	186702	6	33185	4	18972
B9	Upscale Middle Agers	1700000	36	604330	10	177651	5	81650
F28	Urban Enterprise	1400000	28	386491	6	82923	4	54071
	SEGMENT TOTAL	**4730000**	**36**	**1701341**	**9**	**425135**	**6**	**268862**
Med Risk								
A2	Women with Wealth	350000	50	174430	10	34113	7	24541
A3	Owner/Investors	600000	40	239371	12	72371	5	32296
B7	Wealth from the Land	1100000	36	395181	9	96073	6	62689
C11	Equity Rich Elders	1800000	34	620544	7	130123	4	80797
F27	Men Behaving Well	1200000	32	381372	8	93691	4	43008
	SEGMENT TOTAL	**5050000**	**36**	**1810897**	**8**	**426371**	**5**	**243331**
Low Risk								
B8	Cusp of Retirement	910000	44	397754	10	93318	10	87055
B10	Ready for Retirement	2700000	24	641549	4	115225	3	78775
C12	On Private Pensions	2700000	21	570365	4	119459	2	66625
F25	Juggling Work & Home	1000000	28	275542	6	56197	2	24489
F26	Women Flying High	600000	37	220469	8	47136	3	18585
G29	Rich Kids at Home	1000000	33	329842	6	63685	4	36876
	SEGMENT TOTAL	**8910000**	**27**	**2435522**	**6**	**495020**	**4**	**312405**
	OVERALL MARKET TOTAL	**18690000**	**32**	**5947760**	**7**	**1346525**	**4**	**824597**

- Very similar penetration percentages across the three risk categories
- However, some quite significant differences across FSS types within each segment.
- Warrants further investigation. Could be flawed category allocation or simply people still buying shares or unit trusts, but different types for different purposes (growth vs income).
- Overall, indicates likely market sizes of:

  - Higher risk: 1.75- 2 mn

  - Medium risk: 1.8 – 2mn

  - Lower risk: 2.4 – 2.75mn

Touchpoint channel preferences

Experian uses Touchpoint analysis to asses the channel preferences of consumers.

- Touchpoint Segments classify all 46 million adults in the United Kingdom into a series of nineteen distinct types which comprehensively describe their channel preferences and promotional orientation, as well as summarising their key socio-economic and demographic characteristics.
- Taking the 17 FSS types that we have identified (1 to 12 & 25 to 29) it is possible to cross-match the UK population in each of these FSS types by their Touchpoints Type.
- There are 19 Touchpoint Types, but 64% of our target market by FSS types falls into one of only four Touchpoint Types.

Touchpoint channel preferences

Type 18 - Principles and Prejudices

- 10.54% of UK population,but 26% of the target market
- NB almost all are from FSS Types 11&12
- Description: Principles and Prejudices have firm and fixed opinions, often rooted in the values of a bygone age. They resist consumerism, reject lifestyle imagery and value quality and personal service. As they are not time pressured they have the opportunity to consider their options carefully.

Type 14 - Contented Conservatives

- 7.17% of UK population, but 19% of our target
- Description:Contented Conservatives see little reason to adopt new products and neither rely on mainstream advertising for information or for entertainment. They like personal service, disdain mass consumerism and will pay a premium for quality and personalisation.

Touchpoint channel preferences

Type 10 - Value Driven Switchers

- 5.85% of UK population, but 10% of our target
- Description: Value Driven Switchers by and large do not buy into the brand experience and take a particularly hard-nosed attitude towards what they buy. They compare product prices and performance closely, buy from sales and from discount operators, and will respond readily to price based promotions. They rely on advertisements for information rather than for emotion.

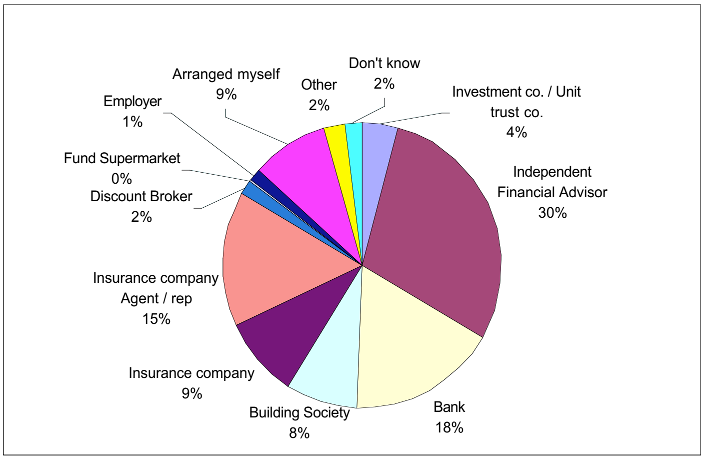
Type 16 - Mr and Mrs Mainstream

- 6.48% of UK population, but 10% of our target
- Description:Mr and Mrs Mainstream are mostly consumers of mainstream brands advertised on mainstream, mass circulation and coverage media. These people are not particularly resistant to change, but have neither the emotional need nor the material resources to do more than occasionally experiment with anything new.

Types of investment

When you bought your most recent investment who arranged it for you?

	number	% of all answers
Investment co. / Unit trust co.	98	**4.22%**
Independent Financial Advisor	679	**29.22%**
Bank	398	**17.13%**
Building Society	196	**8.43%**
Insurance company	210	**9.04%**
Insurance company Agent / rep	353	**15.19%**
Discount Broker	42	**1.81%**
Fund Supermarket	5	**0.22%**
Employer	30	**1.29%**
Arranged myself	208	**8.95%**
Other	57	**2.45%**
Don't know	48	**2.07%**
Total Number of answers	2324	
Formatted Sample Total	1888	

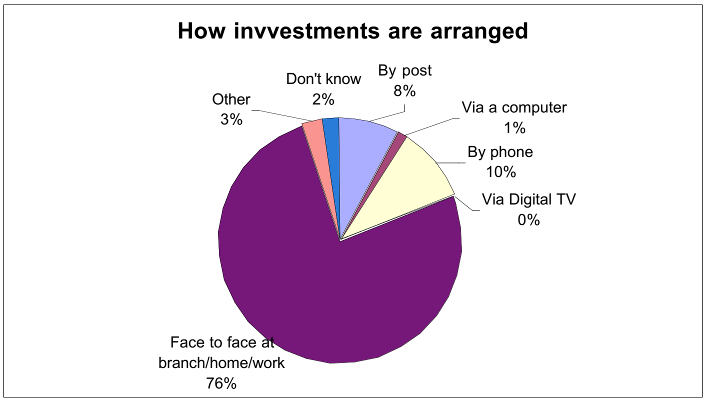


SOURCE: MORI FTS

Types of investment – Awareness & Consideration

When you actually arrange an investment, which one of these methods would you be most likely to use?

	Number	% of all answers
By post	283	8.19%
Via a computer	41	1.19%
By phone	334	9.66%
Via Digital TV	1	0.03%
Face to face at branch/home/work	2628	76.02%
Other	94	2.72%
Don't know	76	2.20%
Total Numbers of answers	3457	100.00%
Formatted Sample Total	2832	



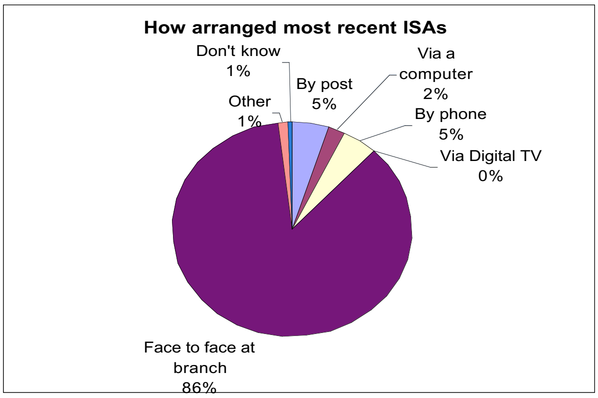
SOURCE: MORI FTS

Business Strategies

ISAs

How did you initially arrange your ISA?

	Number	% of all answers
By post	467	5.14%
Via a computer	195	2.14%
By phone	415	4.56%
Via Digital TV	9	0.10%
Face to face at branch	7835	86.17%
Other	110	1.21%
Don't know	61	0.67%
Total Numbers of answers	9092	100.00%
Formatted Sample Total	8258	



SOURCE: MORI FTS

Business Strategies

Appendix B:

Attractiveness of commercial property investment

Assessing the needs of small investors

Attractiveness of commercial property investment

July 2004

Contents

- ❑ Objectives and approach
- ❑ Existing property market investment
- ❑ Potential investment
- ❑ Conclusions
- ❑ Appendix

Objectives

Utilising quantitative market research

- to summarise current small investors investment patterns in commercial property
- to assess the propensity to invest in new commercial property investment products.

Approach

Information has been collected from two surveys conducted by MORI Financial Services

1. Survey conducted in December 2003 on behalf of the British Property Federation (BPF) and CB Richard Ellis
   - Interviewed representative quota sample of 2000 adults aged 16+ in GB.
   - Study focused on active investors only (equity or related product holders excluding mutualisation and privatisation) – 486 people.
2. Two specific property investment questions included with the April 2004 MORI Financial Tracking Survey (target 400 – 500 active investors from sample of 2000).

Experian has segmented the responses from both surveys using its "MOSAIC" segmentation profiles. Use of more detailed classifications was not appropriate given the low sample of active investors.

Approach – MOSAIC overview

Mosaic UK classifies all UK consumers into 61 distinct lifestyle types and 11 groups which comprehensively describe their socio-economic and socio-cultural behaviour.

•Data Components

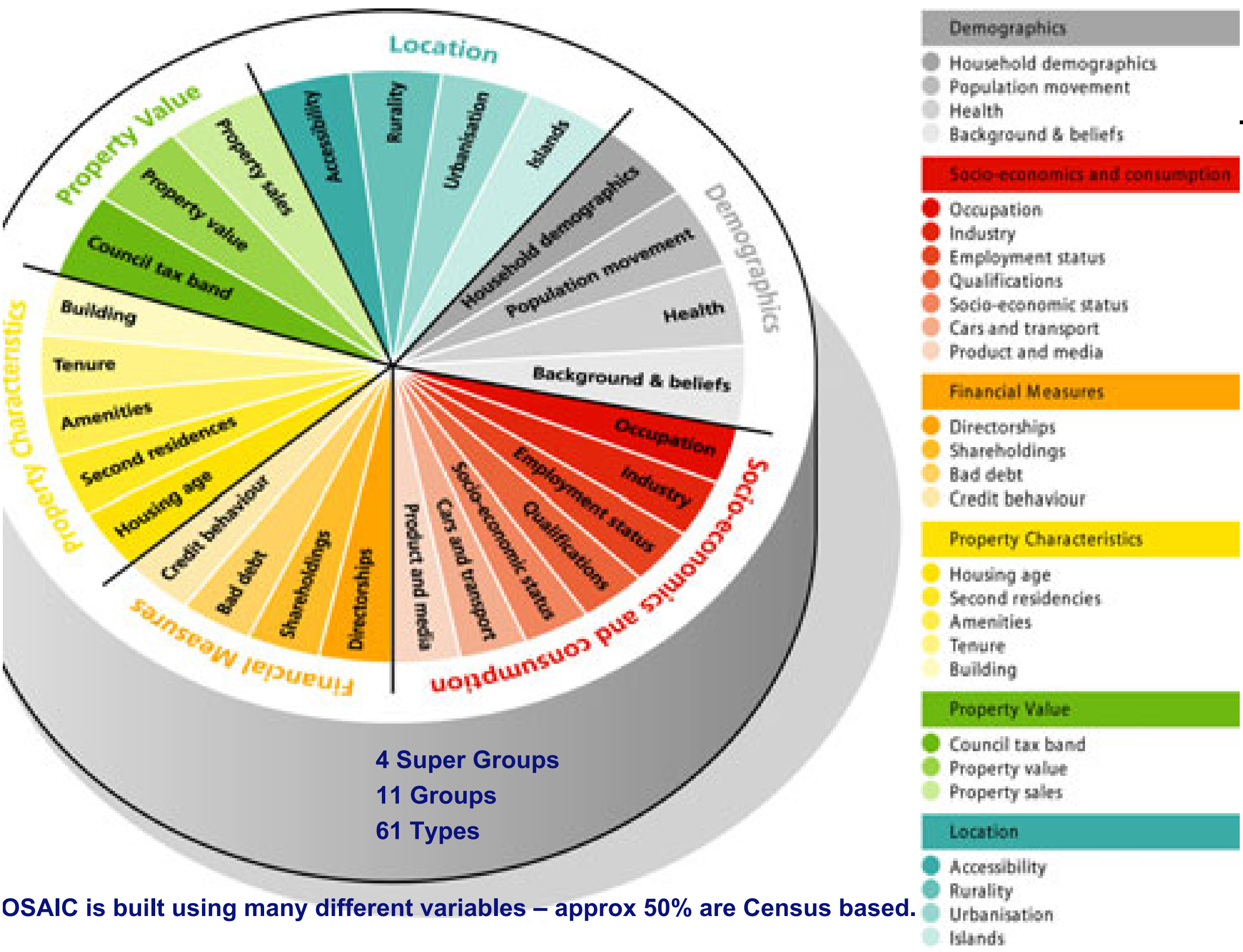
Quantitative Data

- Over 400 data variables have been used to build Mosaic UK. These have been selected as inputs to the classification on the basis of their volume, quality, consistency and sustainability..
- 54 per cent of the data used to build Mosaic UK is sourced from the 2001 Census. The remaining 46 per cent is derived from our Consumer Segmentation Database.

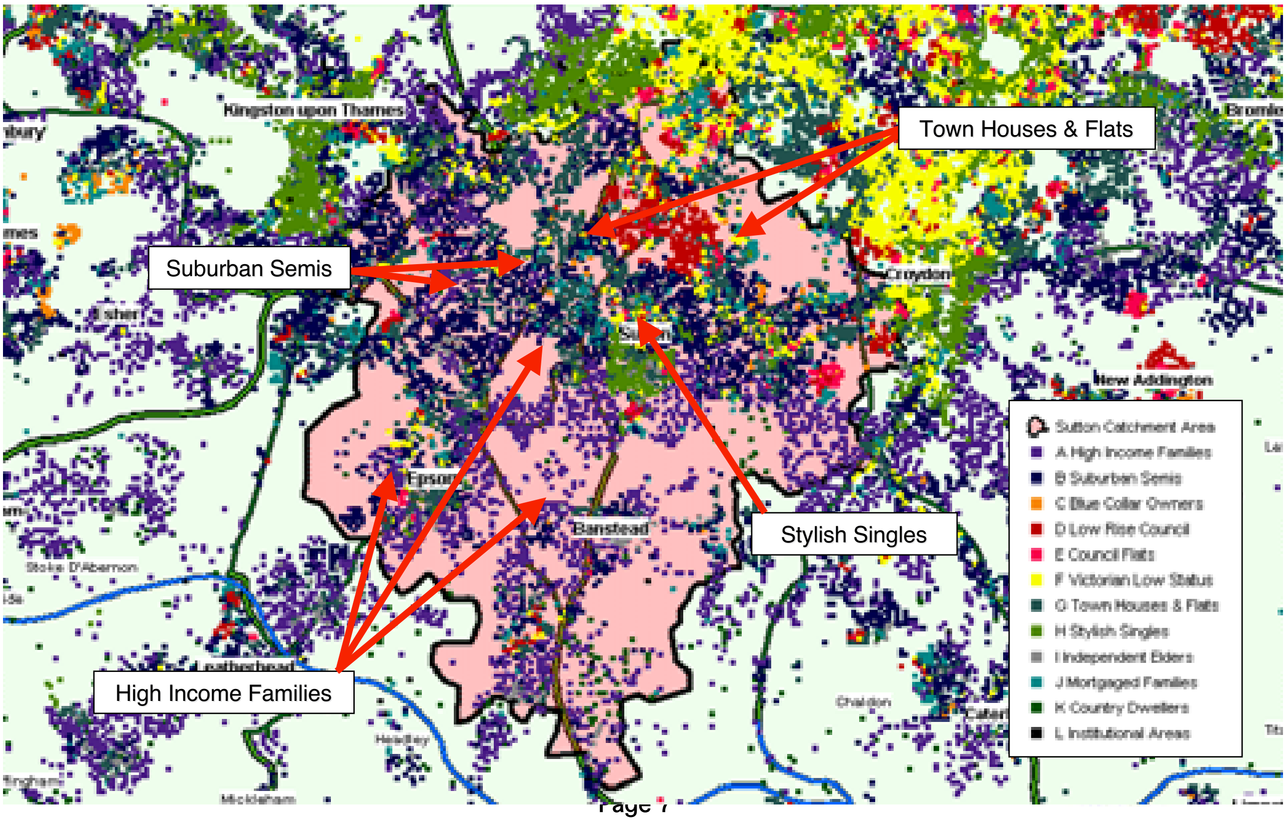
Qualitative Research

- A programme of fieldwork and observational research covering the whole of the UK supports Experian's quantitative data.
- A number of the UK's leading experts in the fields of consumer psychology, human geography and economics to interpret the classification and provide a detailed understanding of the behaviour of each of the Mosaic groups and types.

•*Clustering.* Mosaic UK is designed to identify groupings of consumer behaviour for households and postcodes.



OSAIC is built using many different variables – approx 50% are Census based.



Town Houses & Flats
Suburban Semis
Stylish Singles
High Income Families
Kingston upon Thames
Croydon
New Addington
Epsom
Banstead
Stoke D'Abernon
Chaldon
Headley
Mickleham
Sutton Catchment Area
A High Income Families
B Suburban Semis
C Blue Collar Owners
D Low Rise Council
E Council Flats
F Victorian Low Status
G Town Houses & Flats
H Stylish Singles
I Independent Elders
J Mortgaged Families
K Country Dwellers
L Institutional Areas

Contents

MORI BPF active investors by Mosaic groups

GROUP	Number of people	%
A Symbol of Success	70	14.4%
B Happy Families	56	11.5%
C Suburban Comfort	133	27.4%
D Ties of Community	60	12.3%
E Urban Intelligence	18	3.7%
F Welfare Borderline	10	2.1%
G Municipal Dependency	11	2.3%
H Blue Collar Enterprise	34	7.0%
I Twilight Subsistence	4	0.8%
J Grey Perspectives	39	8.0%
K Rural Isolation	31	6.4%
Unclassified	20	4.1%
TOTAL	486	100.0%

•Over a quarter of the survey were "Suburban Comfort" – which comprises people who have successfully established themselves and their families in comfortable homes in mature suburbs.

•Top 4 groups (A-D) include two-third of the survey (65.6%).

Objectives and approach

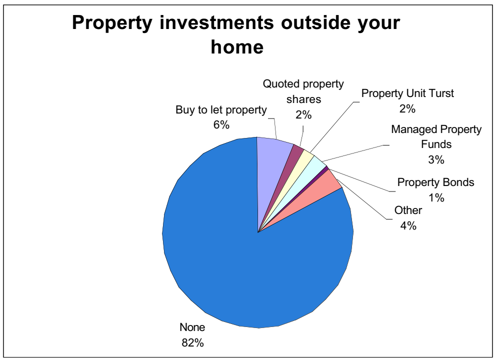
MORI BPF active investors by Mosaic group

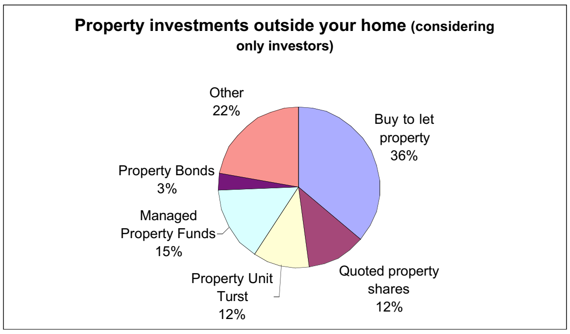
The MORI FTS survey included more active investors.

The MOSAIC profile was similar to the BPF sample.

GROUP	BPF		FTS	
	Number of people	%	Number of people	%
A Symbol of success	70	14.4%	64	10.5%
B Happy Families	56	11.5%	69	11.4%
C Suburban Comfort	133	27.4%	119	19.6%
D Ties of Community	60	12.3%	119	19.6%
E Urban Intelligence	18	3.7%	24	4.0%
F Welfare Borderline	10	2.1%	12	2.0%
G Municipal Dependency	11	2.3%	32	5.3%
H Blue Collar Enterprise	34	7.0%	63	10.4%
I Twilight Subsistence	4	0.8%	10	1.6%
J Grey Perspectives	39	8.0%	48	7.9%
K Rural Isolation	31	6.4%	20	3.3%
Unclassified	20	4.1%	27	4.4%
TOTAL	486	100.00%	607	100.00%

Non-household investment - Which, if any, property investments do you have outside of your own home? (Question 3 MORI BPF)

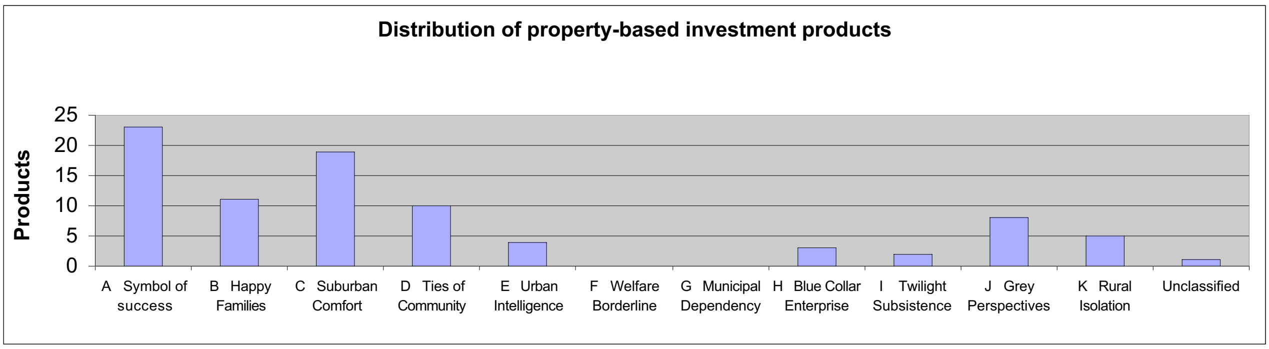




- MORI asked 486 people about investments outside their home.
- Of all the interviewees, 408 (84%), had no property investment outside their home
- Only 78 investors (16%) have property investments outside their home.
- Buy to let property was the leading investment

Property based investment distribution

- 78 people have bought 86 property based investment products.
- 26.7% of investment products were purchased by Group A (Symbol of Success). Nearly doubled the weight in the sample.
- Groups A, B, C and D account for 73% of investment product sold.
- Small sample size means conclusions are only indicative.



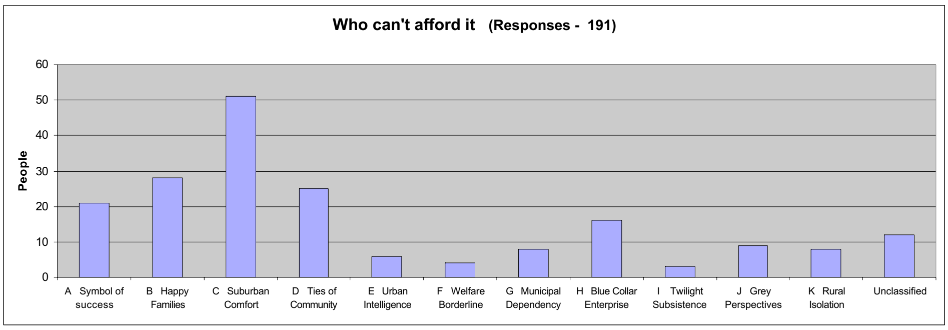
	A	B	C	D	E	F	G	H	I	J	K	Unclassified
% of Active Investors	14.4%	11.5%	27.4%	12.3%	3.7%	2.1%	2.3%	7.0%	0.8%	8.0%	6.4%	4.1%
% of Investment Products	26.7%	12.8%	22.1%	11.6%	4.7%	0.0%	0.0%	3.5%	2.3%	9.3%	5.8%	1.2%
Net difference	12.3%	1.3%	-5.3%	-0.7%	0.9%	-2.1%	-2.3%	-3.5%	1.5%	1.3%	-0.6%	-3.0%

Why have you chosen not to hold any property investment outside your own home? (Question 4 MORI BPF)

Reasons	Number of responses	%
Can't afford it	191	47%
Too risky	45	11%
Not easy to invest in property	10	2%
Don't understand enough about property to invest	30	7%
Don't know how to invest	15	4%
Property ties up money for too long/not easy to get at money	16	4%
Cost of entry (stamp duty, legal fees etc) is too high	3	1%
Size of investment required	13	3%
Other	9	2%
Too old	9	2%
Property overvalued	2	0%
Not interested	16	4%
Never considered	17	4%
Drop in the market	5	1%
Invest/use money elsewhere	7	2%
Just starting with first property	3	1%
Lack of opportunity	3	1%
Too much work/hassle	8	2%
Not advised to/advised not to	2	0%
Poor returns	2	0%
Total answers	406	

- MORI asked 486 people about their reasons for not holding property investment outside their home. 361 responded.
- Multiple answers were allowed, resulting in 406 responses from the 361 who replied
- 191 (47% of responses) stated affordability as the main reason for not holding any property investment
- However, risk (45 people, 11%) and the lack of understanding about property (30 people, 7%) also play a role.

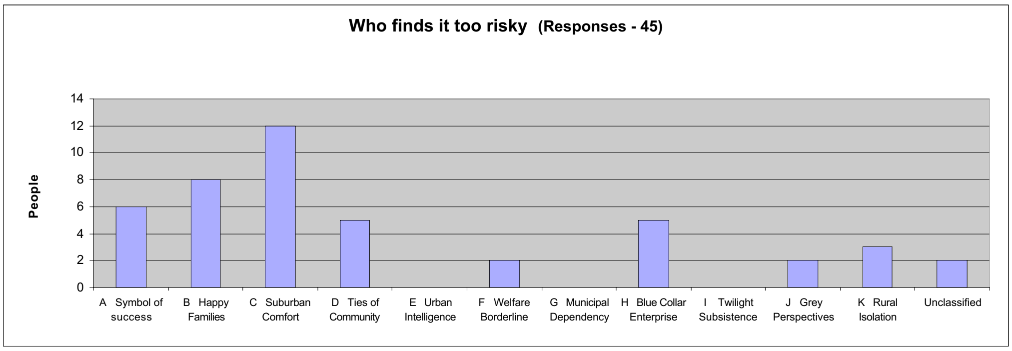
Who can't afford it – MOSAIC segmentation



- Affordability clearly less of an issue for wealthier segments (eg. Group A) – also apparently for Group J (Grey Perspectives)
- 104 of the 191 responses were from MOSAIC groups B, C and D (54%).
- Affordability may be more of a relative issue for Happy Families (14.7% versus sample representation of 11.5%)

	A	B	C	D	E	F	G	H	I	J	K	Unclassified
% of Active Investors	14.4%	11.5%	27.4%	12.3%	3.7%	2.1%	2.3%	7.0%	0.8%	8.0%	6.4%	4.1%
% of people who can't afford it	11.0%	14.7%	26.7%	13.1%	3.1%	2.1%	4.2%	8.4%	1.6%	4.7%	4.2%	6.3%
Net difference	-3.4%	3.1%	-0.7%	0.7%	-0.6%	0.0%	1.9%	1.4%	0.7%	-3.3%	-2.2%	2.2%

Who finds it too risky – MOSAIC segmentation

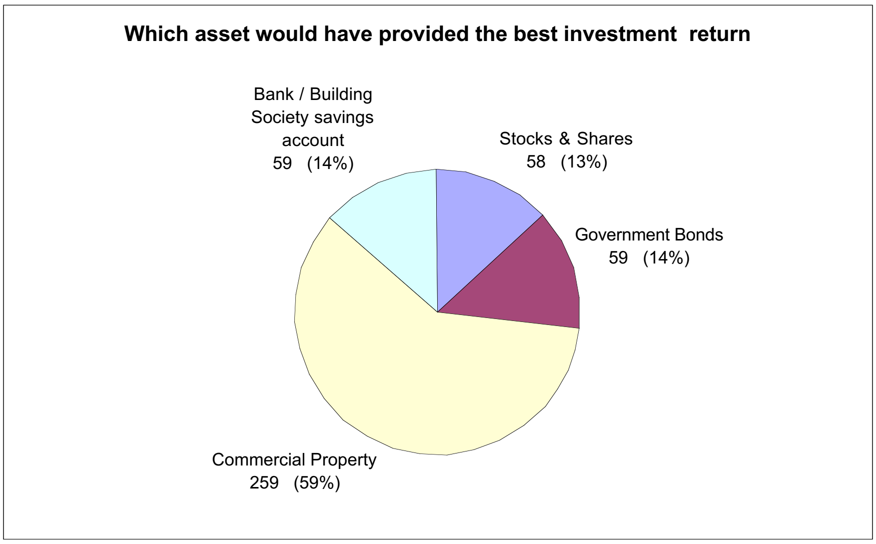


- Sample size very small, but:
  - Over a quarter of replies were from group C (Suburban Comfort).
  - Group B's may be more concerned about risk.
  - Are J's (Grey Perspectives) less concerned about risk?
- More research required to confirm hypothesis

	A	B	C	D	E	F	G	H	I	J	K	Unclassified
% of Active Investors	14.4%	11.5%	27.4%	12.3%	3.7%	2.1%	2.3%	7.0%	0.8%	8.0%	6.4%	4.1%
% of people who finds it too risky	13.3%	17.8%	26.7%	11.1%	0.0%	4.4%	0.0%	11.1%	0.0%	4.4%	6.7%	4.4%
Net difference	-1.1%	6.3%	-0.7%	-1.2%	-3.7%	2.4%	-2.3%	4.1%	-0.8%	-3.6%	0.3%	0.3%

Investor's perception of return

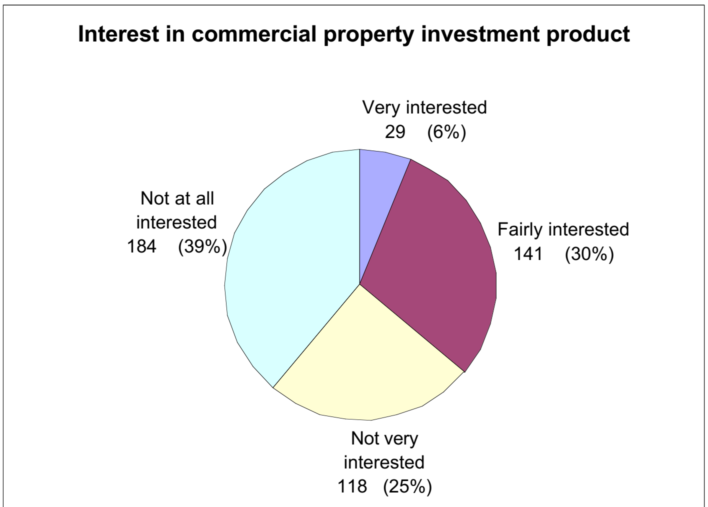
If you had invested money in each of the following assets three years ago, which one do you think would, by now, have provided you with the best return? (Question 1 MORI BPF)



- MORI asked 486 people which asset would have provided the best investment return. 435 responded.
- The majority, 259 (59%), believe that commercial property would have given the best return

Interest in a new commercial property investment product (MORI BPF Survey)

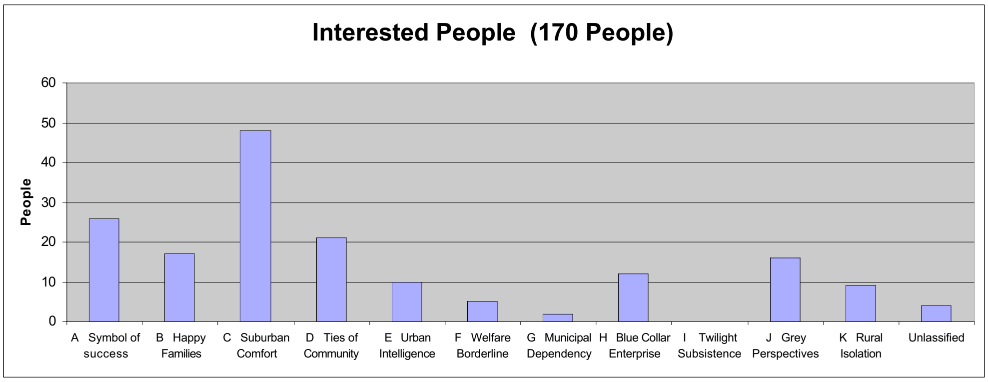
If there was an investment product available that allowed you to invest directly in commercial property e.g. giving you a 'stake' in a range of office developments, shopping centres, industrial parks etc how interested might you be in such a product? (Question 2 MORI BPF)



- MORI asked 486 people about their interest in this new product. 472 responded.
- Of these only 29 (6%) were very interested, while 141 (30%) were fairly interested – giving a total interest level of 36% (170 people)
- 184 (39%) wouldn't be interested at all, while a further 118 (25%) were not very interested.

One third of active investors appear interested in commercial property investments

Who is interested - MOSAIC Segmentation

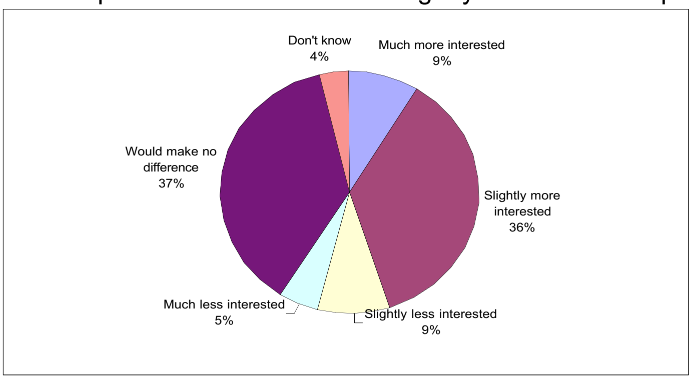


- Over a quarter of replies were from group C (Suburban Comfort)
- Groups A, B, C and D account for approx 66%.
- Group A (15.3%) and J (9.4%) show a level of interest with exceed their weight in the sample of active investors

	A	B	C	D	E	F	G	H	I	J	K	Unclassified
% of active investors	14.4%	11.5%	27.4%	12.3%	3.7%	2.1%	2.3%	7.0%	0.8%	8.0%	6.4%	4.1%
% of people interested	15.3%	10.0%	28.2%	12.4%	5.9%	2.9%	1.2%	7.1%	0.0%	9.4%	5.3%	2.4%
Net Difference	0.9%	-1.5%	0.9%	0.0%	2.2%	0.9%	-1.1%	0.1%	-0.8%	1.4%	-1.1%	-1.8%

Prompted **(Commercial property is the best performing asset over the last 3 / 5 / 10 / 15 years, and second only to equities over the last 30 years)**

Would you be more or less interested in an investment product that allowed you invest directly in commercial property e.g. giving you a 'stake' in a range of office developments, new shopping centres, industrial parks etc how interested might you be in such a product? (Question 8 MORI BPF)



		% of total answers
Much more interested	43	9
Slightly more interested	176	36
Slightly less interested	43	9
Much less interested	24	5
Would make no differen	182	37
Don't know	18	4
Grand Total	486	100

- Mori asked 486 people about their interest in commercial property. After being prompted, 468 responded.
- Overall 219 people (45% of all interviewees) would be interested in this new investment product (an increase of 49 people)
- 43 (9%) would be much more interested
- However, 182 (37%) believe that it would not make any difference

After prompting, the % of people interested increased from 36% to 45%

Pension fund investment

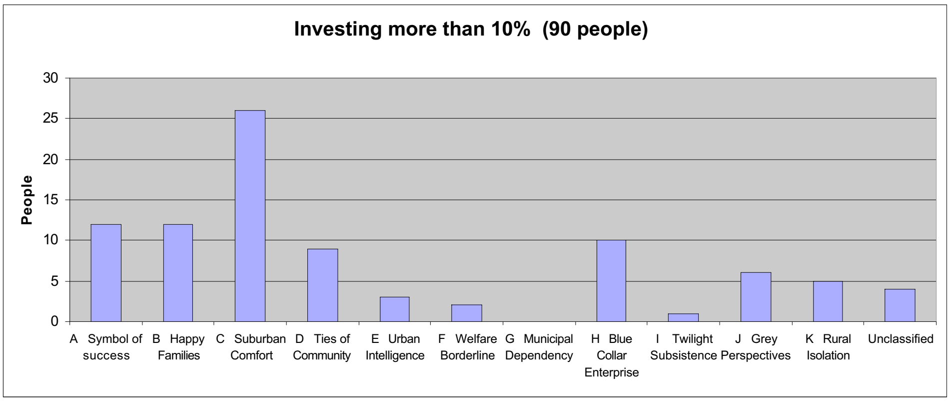
Thinking now for a moment about commercial property, what percentage of your pension fund would you expect to be invested in this? (Question 6 MORI BPS)

% of pension expected to be invested in commercial property	number of people	% People
0%	196	59%
1-10%	44	13%
11 - 20%	29	9%
21-30%	25	8%
31-40%	11	4%
41-50%	16	5%
51-60%	4	1%
61-70%	4	1%
71-80%	1	0%
81-90%	0	0%
91-100%	0	0%
Don't know	156	

- MORI asked 486 people about what % of pension they would expect to invest in commercial property. 330 responded.
- 90 people (28%) would invest more than 10%
- 240 people (72%) would invest nothing or very little (not more than 10%).
- Interested market share is again approx 1/3 of active investors

Investing more than 10% in commercial property – MOSAIC Segmentation

- Groups A, B, C and D account for nearly two-third.
- Groups B (13.3%) and C (28.9%) show a propensity to invest more than 10% which exceeds their sample weights.
- Group J shows a propensity to invest more than 10% which is lower than sample weight.



	A	B	C	D	E	F	G	H	I	J	K	Unclassified
% of active investors	14.4%	11.5%	27.4%	12.3%	3.7%	2.1%	2.3%	7.0%	0.8%	8.0%	6.4%	4.1%
Propensity to invest more than 10% (%)	13.3%	13.3%	28.9%	10.0%	3.3%	2.2%	0.0%	11.1%	1.1%	6.7%	5.6%	4.4%
Net difference	-1.1%	1.8%	1.5%	-2.3%	-0.4%	0.2%	-2.3%	4.1%	0.3%	-1.4%	-0.8%	0.3%

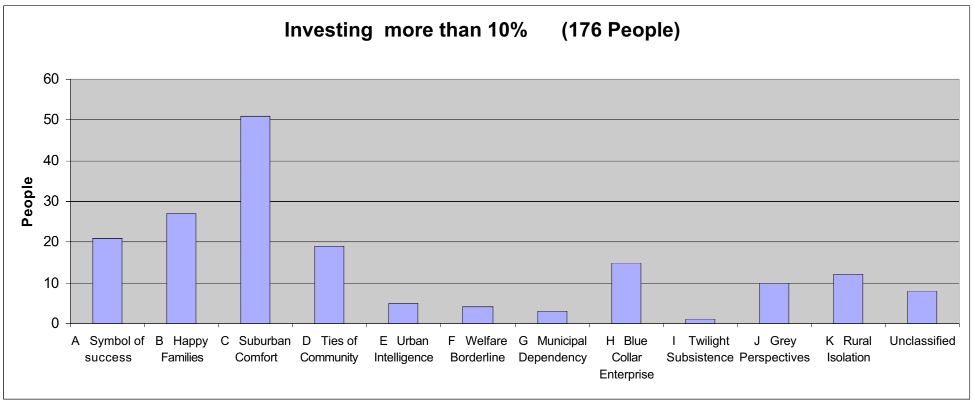
Prompted **(Commercial property is the best performing asset over the last 3 / 5 / 10 / 15 years, and second only to equities over the last 30 years)**

What percentage of your pension would you expect to be invested in commercial property? **(Question 7 MORI BPF)**

% of pension expected to be invested in commercial property	**number of people**	**% People**
0%	196	51%
1-10%	16	4%
11 - 20%	31	8%
21-30%	42	11%
31-40%	21	5%
41-50%	43	11%
51-60%	9	2%
61-70%	8	2%
71-80%	14	4%
81-90%	3	1%
91-100%	5	1%
Don't know	98	

- MORI asked 486 people about what % of pension they would expect to invest in commercial property. After being prompted 388 responded.
- After prompting, the percentage of people who would like to invest nothing or very little (not more than 10%) declined from 72% to 55%.
- The percentage of people who would like to invest more than 10% increased from 28% to 45%.

Prompted



- Groups A, B, C and D account for over two-third.
- Groups B (15.3%) and C (29.0%) show a propensity to invest more than 10% which exceeds their sample weights.
- Group J shows a propensity to invest more than 10% which is lower than sample weight.
- Similar to the non-prompted scenario.

	A	B	C	D	E	F	G	H	I	J	K	Unclassified
% of active investors	14.4%	11.5%	27.4%	12.3%	3.7%	2.1%	2.3%	7.0%	0.8%	8.0%	6.4%	4.1%
Propensity to invest more than 10% (%)	11.9%	15.3%	29.0%	10.8%	2.8%	2.3%	1.7%	8.5%	0.6%	5.7%	6.8%	4.5%
Net difference	-2.5%	3.8%	1.6%	-1.6%	-0.9%	0.2%	-0.6%	1.5%	-0.3%	-2.3%	0.4%	0.4%

Quantitative analysis was enhanced by two specific questions in the April MORI FTS omnibus survey of 2000 adults aged 16+ in GB

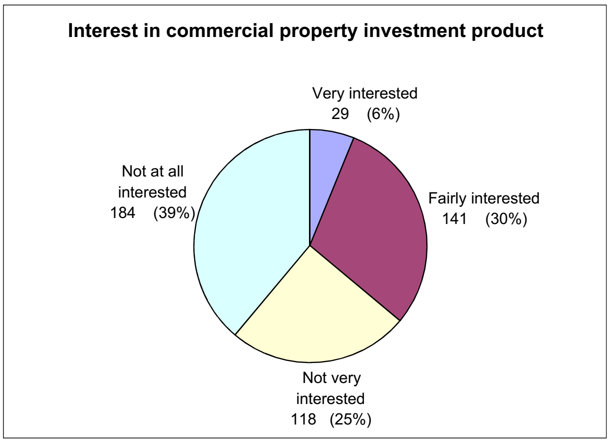
Question 1:
New regulations are making it easier for individuals to invest in commercial property via shares in a new type of investment product listed on the Stock Exchange.
How likely do you think you might be to invest in commercial property by this route over the next 12 months?

Question 2:
How much do you think you might invest in a listed commercial property investment product over the next 12 months?

Substantial difference in consumer response if asked whether interested in investing in commercial property compared to making a commitment to invest within 12 months.

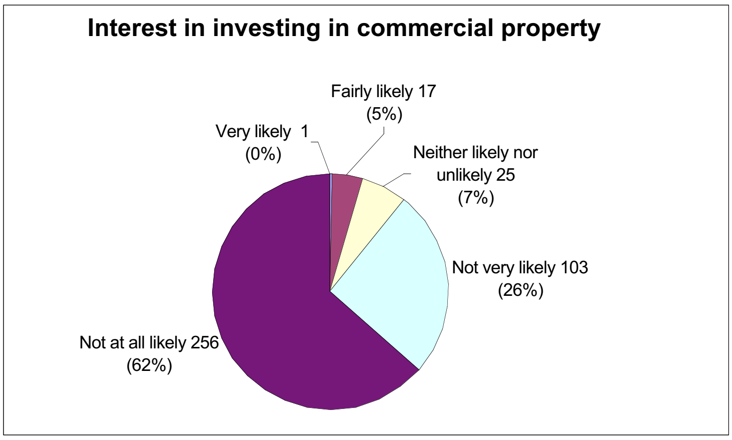
1. BPF questions (486 active investors)

One third of active investors appear interested in commercial property investments



2. MORI FTS questions (607 active investors)

Only 5% would be interested in investing in commercial property within 12 months



le interested in commercial property

~~18 likely~~ to invest within 12 months

Very low response from first MORI FTS question, effectively made the second question redundant

Question 2 - How much do you think you might invest in a listed commercial property investment product over the next 12 months?

Amount	Number	%
£1 - £4,999	3	17%
£5,000 - £9,999	2	11%
£10,000 - £19,999	5	28%
£20,000 - £49,999	1	6%
Over £50,000	2	11%
Don't know	5	28%

- Further quantitative research should be more focused on specific investment products. Testing:
  - Product features.
  - Target market.
  - Customer value proposition.
  - Level of likely investment.

Conclusions

It is difficult to draw firm conclusions due to the size of the sample. However, some general insights are possible.

- Paradox that while a majority (nearly 60%) of active investors considered commercial property the best performing asset over the last 3 years, only a small proportion (16%) already had property based investment products.
- 84% of active investors have no investment outside their home. The main constraints being affordability, risk and transparency.
- Apparent that about a third of active investors are interested in a new commercial property investment product which would offer a 'stake' in a range of property developments. After prompting, the percentage increased to 45%
- Similarly apparent there is a hard-core of approx 40% of active investors who would need a lot of persuasion to invest in commercial property. This leaves a group of approx 25% who are fairly interested and may be converted over time.

Conclusions – Market Size

MOSAIC Group	Number of adults (16 and over)	Commercial Property Interest (%)	Potential Market Size
A Symbol of success	5,155,826	15.3%	788,538
B Happy Families	4,651,251	10.0%	465,125
C Suburban Comfort	7,748,123	28.2%	2,187,705
D Ties of Community	7,755,019	12.4%	957,973
J Grey Perspectives	3,723,801	9.4%	350,475
Total	29,034,020		4,749,817

- These 5 MOSAIC groups seem to be the most interested in commercial property
- Nearly 30m adults, with a potential market size of nearly 5m
- Group C Suburban Comfort accounts for approx 45%

APPENDIX

Mosaic UK Group A

Objectives and approach

Group A: Symbols of Success (5.15m adults, 10.87%)

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Summary

Symbols of Success contains people whose lives are 'successful' by whatever yardsticks society commonly uses to measure success. These are people who have rewarding careers rather than jobs, who live in sought after locations, who drive the more modern and expensive cars and who indulge in the most exotic leisure pursuits. Most, though not all, appear to enjoy stable household arrangements.

•**Type A01: Global Connections.** *Global Connections* contains extremely expensive housing, mostly in central London, occupied by rich people from abroad and by childless older people on extremely high incomes.

•**Type A02: Cultural Leadership.** *Cultural Leadership* contains very well educated professionals, many of whom work in the liberal professions, government or the arts, who mostly live in very expensive middle ring London suburbs.

•**Type A03: Corporate Chieftains.** *Corporate Chieftains* contains very wealthy people, many of whom are senior business managers, living in large detached houses in outer metropolitan suburbs.

•**Type A04: Golden Empty Nesters.** *Golden Empty Nesters* contains wealthy older people living in large detached houses, often in choice residential locations in semi rural settings.

•**Type A05: Provincial Privilege.** *Provincial Privilege* contains well educated older professionals who work in senior, often public sector, positions in the centres of large provincial cities and who live in their older established suburbs.

•**Type A06: High Technologists.** *High Technologists* are found in areas of modern, high specification family housing, mostly in outer metropolitan areas, which attract well paid executives working in large corporations.

•**Type A07: Semi-Rural Seclusion**. *Semi-Rural Seclusion* contains people living in environmentally attractive villages and small towns where highly paid long distance commuters mix with a more locally oriented older population.

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Group B: Happy Families (4.65m adults, 9.80%)

Summary

Happy Families contains people whose focus is on career, home and family. These are mostly younger age groups who are married, or at least in a permanent relationship, and are now raising children in post war family houses, often in areas of the country with rapidly growing populations. The focus of expenditure is on equipment for the home and garden, and the immediate family unit is the principal focus of leisure activities.

•T**ype B08: Just Moving In**. *Just Moving In* contains people living in houses built since 2001, the date of the last census. Most of these identify new residential areas.

•**Type B09: Fledgling Nurseries.** *Fledgling Nurseries* contains very young couples, mostly working in intermediate level jobs in areas of new employment, who have bought homes on new housing estates built in the last ten years.

•**Type B10: Upscale New Owners**. *Upscale New Owners* contains younger professionals and managers who have bought expensive, modern, detached houses in rapidly expanding outer metropolitan areas.

•**Type B11: Families Making Good.** *Families Making Good* contains upper middle-income families living in estates of detached houses many of which are now around twenty years old.

•**Type B12: Middle Rung Families.** *Middle Rung Families* is found in the modern suburbs of mortgaged owner-occupiers which are affordable to middle income groups. Many are located in smaller towns with modern light manufacturing industries.

•**Type B13: Burdened Optimists.** *Burdened Optimists* contains confident, but not very well educated, co-habiting and married couples who live in mortgaged properties in areas of good employment opportunities.

•**Type B14: In Military Quarters**. *In Military Quarters* contains servicemen and their families who live in military accommodation.

Group C: Suburban Comfort (7.75m adults, 16.33%)

Summary

Suburban Comfort comprises people who have successfully established themselves and their families in comfortable homes in mature suburbs. Children are becoming more independent, work is becoming less of a challenge and interest payments on homes and other loans are becoming less burdensome. With more time and money on their hands, people can relax and focus on activities that they find intrinsically rewarding.

•**Type C15: Close to Retirement.** *Close to Retirement* contains many people in older working age groups, who own homes that were built during the 1970s, in areas of the country where planners were happy to allow rapid urbanisation.

•**Type C16: Conservative Values.** *Conservative Values* comprises people of older working ages who live on owner occupied estates built since the war on the outskirts of manufacturing towns. Many of the dwellings are bungalows.

Type C17: Small Time Business. *Small Time Business* lives in quiet small estates, mostly built since 1945 in market towns that have some industrial employment. These estates will typically be home to local professionals and small business proprietors.

•**Type C18: Sprawling Subtopia.** *Sprawling Subtopia* contains middle aged, middle income owner occupiers living on very large developments of 1930s suburban semi-detached housing.

•**Type C19: Original Suburbs.** *Original Suburbs* comprises a mixed social profile, but with a bias towards young professionals, residing in interwar semi-detached houses.

•**Type C20: Asian Enterprise.** *Asian Enterprise* contains well-qualified minorities, mostly from Asia, who have settled in suburban semi-detached houses in inter war suburbs.

Mosaic UK Group D

Objectives and approach

Group D: Ties of Community **(7.75m adults, 16.34%)**

Summary

Ties of Community is comprised of people whose lives are mostly played out within the confines of close knit communities. Living mostly in older houses in inner city neighbourhoods or in small industrial towns, most of these people own their homes, drive their own cars and hold down responsible jobs. Community norms rather than individual material ambitions shape the pattern of most residents' consumption.

•**Type D21: Respectable Rows.** *Respectable Rows* are found in areas of small, but not unattractive, terraced housing most of which was built just before or just after the First World War and which now displays a population profile surprisingly similar to the national average.

•**Type D22: Affluent Blue Collar.** *Affluent Blue Collar* comprises older manual workers, many of them employees of manufacturing industries such as steel and chemical plants, who have traditionally enjoyed a high standard of living and who own the spacious post war semi-detached houses that they live in.

•**Type D23: Industrial Grit.** *Industrial Grit* contains owners of older, comfortable but unpretentious houses, often in ex-mining areas, who work in manufacturing and assembly plants.

•**Type D24: Coronation Street.** *Coronation Street* contains poor, mostly white families, who own or privately rent, cheap terraced houses close to the centres of less prosperous provincial cities.

•**Type D25: Town Centre Refuge**.*Town Centre Refuge* contains young unattached people who live in small flats above shops or in the less prestigious side streets bordering the centres of small market towns and declining seaside resorts.

•**Type D26: South Asian Industry.** *South Asian Industry* contains extremely poor people, many of them of Bangladeshi origin, who live in very low quality 19th century terraced housing in the inner areas of industrial towns.

•**Type D27: Settled Minorities.** *Settled Minorities* contains areas of Victorian and Edwardian two storey houses which are attractive to young second generation black British and other ethnic minorities as they move out from the inner city in search of affordable family accommodation.

I

Mosaic UK Group E

Objectives and approach

Group E: Urban Intelligence **(3.35m adults, 7.07%)**

Summary

Urban *Intelligence* mostly contains young and well educated people who are open to new ideas and influences. Young and single, and few encumbered with children, these people tend to be avid explorers of new ideas and fashions, cosmopolitan in their tastes and liberal in their social attitudes. Whilst eager consumers of the media and with a sophisticated understanding of brand values, they like to be treated as individuals, and value authenticity over veneer.

•**Type E28: Counter Cultural Mix.** *Counter Cultural Mix* comprises a mixture of young professionals in rented flats, ethnic minorities sharing large old houses and poor tenants in council flats, that characterises many of the less well off areas surrounding the centre of London.

•**Type E29: City Adventurers*City.*** *Adventurers* contains twenty-something singles who command extremely high salaries working in high pressure jobs in central London. Most spend very small amounts of time in their smart, studio flats that are located in the inner suburbs.

•**Type E30: New Urban Colonists.** *New Urban Colonists* contains areas, mostly in London, which have been gentrified since the 1960s by a new generation of young professionals quite content to trade access to the city for a higher density of population.

•**Type E31: Caring Professionals.** *Caring Professionals* contains large numbers of young professionals, many working in the public sector, who live in socially mixed, inner areas of historic regional centres.

•**Type E32: Dinky Developments.** *Dinky Developments* contains a mixture of singles, co-habiting partners, couples with just one child and separated people who live in compact new starter homes, often built on brownfield sites amidst areas of older housing.

•**Type E33: Town Gown Transition.** *Town Gown Transition* is found in the older areas of provincial cities which are sufficiently close to universities to have large populations of students and recent graduates.

•**Type E34: University Challenge.** *University Challenge* is found in the areas of provincial cities which contain university halls of residences and where the surrounding streets are rented out to undergraduate students.

I

Group F: Welfare Borderline **(2.72m adults, 5.74%)**

Summary

*Welfare Borderline*is comprised of many people who are struggling to achieve the material and personal rewards that are assumed to be open to all in an affluent society. Few hold down rewarding or well paying jobs and, as a result, most rely on the council for their accommodation, on public transport to get around and on state benefits to fund even the bare essentials. The lack of stability in many family formations undermines social networks and leads to high levels of anti social behaviour among local children.

•**Type F35: Bedsit Beneficiaries.** *Bedsit Beneficiaries* contains people who live in the centres of cities and larger towns, mostly in mid rise rented flats in tenement blocks or above shops.

•**Type F36: Metro Multiculture.** *Metro Multiculture* contains people who rent public housing in the inner areas of London where a particularly high proportion of the population belongs to minority communities.

•**Type F37: Upper Floor Families.** *Upper Floor Families* contains low income young couples with children who rent homes in purpose built flats from local councils in England's larger cities.

•**Type F38: Tower Block Living**.*Tower Block Living* contains areas where the majority of the population live in high rise flats and suffer from very high levels of social and economic deprivation.

•**Type F39: Dignified Dependency.** *Dignified Dependency* contains areas, mostly in England, where small inner city flats and maisonettes are occupied by low income couples and pensioners whose children are now independent.

•**Type F40: Sharing a Staircase.** *Sharing a Staircase* contains households with young children, renting very small flats in mid rise walk up flats on large council schemes. These neighbourhoods are mostly in Scotland.

Group G: Municipal Dependency **(2.95m adults, 6.23%)**

Summary

Municipal Dependency mostly contains families on lower incomes who live on large municipal council estates where few of the tenants have exercised their right to buy. Often isolated in the outer suburbs of large provincial cities, *Municipal Dependency* is characterised as much by low aspirations as by low incomes. Here people watch a lot of television and buy trusted mainstream brands from shops that focus on price rather than range or service.

•**Type G41: Families on Benefits.** *Families on Benefits* contains large numbers of young families on very low incomes who live in extensive areas of low rise public housing on the outskirts of major provincial cities where few people have exercised their right to buy.

•**Type G42: Low Horizons.** *Low Horizons* contains large numbers of people in large provincial cities, who are on low incomes and are particularly dependent on city councils for housing and for transport.

•**Type G43: Ex-Industrial Legacy.** *Ex-Industrial Legacy* is found in parts of declining industrial areas, where a poor but relatively stable, elderly population lives in low rise council owned properties typically forty or more years old.

Mosaic UK Group H

Objectives and approach

Group H: Blue Collar Enterprise (5.27m adults, 11.12%)

Summary

Blue Collar Enterprise comprises people who, though not necessarily very well educated, are practical and enterprising in their orientation. Many of these people live in what were once council estates but where tenants have exercised their right to buy. They own their cars, provide a reliable source of labour to local employers and are streetwise consumers. Tastes are mass market rather than individualistic and focus on providing comfort and value to family members.

•**Type H44: Rustbelt Resilience.** *Rustbelt Resilience* neighbourhoods are mostly found in traditional mining communities, which are still intensely dependent on manufacturing employment. Though these are mostly very poor communities it does not cost much to own the terraced houses in which most people live.

•**Type H45: Older Right to Buy.** *Older Right to Buy* contains people of older working age, working in manufacturing industries and living in mixed areas of older council housing and owner occupied terraces.

•**Type H46: White Van Culture.** *White Van Culture* contains young couples who have exercised the right to buy their council houses, encouraged by high house prices and booming economies. They are found mostly around the M25.

•**Type H47: New Town Materialism.** *New Town Materialism* contains families with young children who live on recently built council estates in planned communities, built around new light industrial estates and assembly plants.

Mosaic UK Group I

Objectives and approach

Group I: Twilight Subsistence (1.56m adults, 3.30%)

Summary

Twilight Subsistence consists of elderly people who are mostly reliant on state benefits, and live in housing designed by local authorities and housing associations. Some live in old people’s homes or sheltered accommodation, while others live in small bungalows, set in small enclaves within larger council estates. Most of these people spend money only on the basic necessities of life.

•**Type I48 :Old People in Flats.** *Old People in Flats* are found in areas of small, publicly rented flats, often in larger towns, which are better suited to the needs of single people and pensioners than they are to the needs of families with children.

•**Type I49: Low Income Elderly.** *Low Income Elderly* is found in the bigger Scottish cities, where large numbers of empty nesters and pensioners live in ‘better’ council estates, though often in cramped conditions and on low incomes.

•**Type I50: Cared for Pensioners.** *Cared for Pensioners* contains old age pensioners who live in small pockets of specially built bungalows and flats, typically within more extensive estates of public sector housing.

Group J: Grey Perspectives (3.72m adults, 7.85%)

Summary

Grey Perspectives consists mostly of pensioners who own their homes and who have some source of income beyond the basic state pension. Many of these people have, on retirement, moved to the seaside or the countryside to live among people similar to themselves. Today many of these people have quite active lifestyles and are considered in their purchasing decisions.

•**Type J51: Sepia Memories.** *Sepia Memories* contains large numbers of pensioners who, on account of old age, ill health or bereavement, have exchanged a house with a garden for a modest apartment in a small block of purpose built flats, usually close to the sea.

•**Type J52: Childfree Serenity.** *Childfree Serenity* consists of well educated couples, who for various reasons don't have children, and wealthy older people, who can no long manage the responsibility of homes with gardens. They live in small modern purpose built apartments and attractive but compact older town houses in historic settings.

•**Type J53: High Spending Elders.** *High Spending Elders* contains well educated, early retirees and pensioner couples who see no contradiction between retirement and the enjoyment of an active lifestyle. Such people live not just on the coast but increasingly in attractive country villages.

•**Type J54: Bungalow Retirement.** *Bungalow Retirement* is found mostly by the seaside, where elderly couples have retired to enjoy a pleasant climate in the company of people of a similar age and similar values.

•**Type J55: Small Town Seniors.** *Small Town Seniors* contains mixed populations of lower income pensioners and middle income workers who live in second tier seaside resorts and in small, semi rural communities.

•**Type J56: Tourist Attendants.** *Tourist Attendants* contains people living in seaside resorts and small inland towns who cater for the needs of day trippers and summer holiday makers.

Group K: Rural Isolation (2.54m adults, 5.35%)

Summary

Rural Isolation contains people whose pattern of living is distinctively rural. They live not just outside major population centres but also deep in the countryside, in small communities which have been little influenced by the influx of urban commuters. These are places where people with different levels of income share attachments to local communities, and where engagement with the community and with the natural environment are more important to most residents than material consumption.

•**Type K57: Summer Playgrounds**. *Summer Playgrounds* is found in rural areas, where urban people own many second homes and where bed and breakfasts and other agro-tourism enterprises provide important sources of seasonal income.

•**Type K58: Greenbelt Guardians.** *Greenbelt Guardians* contains farming communities set in areas of high landscape value which, on account of their accessibility to towns, attract a minority of very wealthy households.

•**Type K59: Parochial Villagers.** *Parochial Villagers* is found in lowland Britain, in communities that have been relatively unaffected by the attentions of urban commuters, wealthy pensioners, weekenders or summer holidaymakers.

•**Type K60: Pastoral Symphony.** *Pastoral Symphony* contains populations of scattered farmers most of whom are owner managers of medium sized operations with a bias towards dairying rather than cereals or intensive agribusiness.

•**Type K61: Upland Hill Farmers.** *Upland Hill Farmers* mostly contains farmers who manage small farm holdings without the assistance of paid labour, in isolated areas of upland agriculture.

Working Paper Three

Advisers to individual investors, pension funds and charities

This report summarises the findings of structured discussions with advisers to individual investors, pension funds and charities.

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1. Summary

Financial advisers have an important role in advising their clients on whether to allocate funds to commercial property and on the suitability of the different commercial property products. This report summarises the findings of structured discussions with 30 advisers to individual investors, pension funds and charities. The key findings of this report are as follows:

1.1 Individual Investors

- Almost £22bn. of regulated financial products was sold in 2001 and independent financial advisers accounted for two-thirds of these sales. The remainder are sold by product provider owned sales teams and by direct marketing, telesales and the Internet. Life and pensions products dominated sales by value with less than 6% being invested in collective investment schemes.
- The FSA put the total number of financial advisers at 77,000, but market sources suggest that only 25,000 of these are active authorised individuals. In view of the promotional restrictions imposed under FSMA on unregulated collective investment schemes, these advisers are critical to the distribution of property investment products.
- Establishing risk preferences is an important first step taken by most advisers in determining an investment strategy for a client. The proportion of equities in the asset allocation is the key variable that alters with risk preference. Hence, Cautious investors (low risk) tend to have lower recommended weightings in equities than (medium risk) and Adventurous (higher risk).
- Commercial property figures strongly in the asset allocation advisers recommend to their clients. The average allocation to property for a Cautious investor was surprisingly high at 21%, but this allocation falls as the weighting in equities rises for investors who have greater preference for risk.
- Small IFAs tend to use proprietary software packages to determine asset allocation, according to risk preference. However, these packages do not include property, so it is left to the adviser to allocate.
- To help identify suitable products small independent firms of advisers also often use product selection software, such as Synaptic, and other sources, such as S&P Micropal and fund fact sheets. Property products are not well covered, making the decision-making process more difficult.
- Consequently, a number of advisers noted that a key stage in the product sales process was their own due diligence on the product, which required their 'buy-in' before it would offers to clients. This approach applied particularly to property where there is little comparative product analysis available.
- For many financial advisers, their clients are inherently risk averse, so the principal property products sold are insurance company unit linked life products and authorised unit trusts. Principal attractions included: diversified ungeared portfolios, reliable brands and competitive charging structures.
- Unauthorised unit trusts were favoured because the clients readily understand them.
- Also, offshore property investment companies were seen as being advantageous for the tax efficiencies that they offer. However, there were also concerns that pricing reflects market sentiment not the performance of the underlying assets, and the charges are considered to be relatively high.
- Limited partnerships are seen as appropriate for more sophisticated clients because these offer identifiable properties, gearing and the availability of capital allowances. However, the costs and illiquidity of these products were seen as being their principal disadvantages.

1. Summary

- The actions needed to broaden the access of investors to commercial property included: the need to simplify the product offering and reduce costs. Others would like to see more ISA-able property products as a way of getting smaller investors into property. However, concerns were also expressed about the pricing of listed products.
- Advisers' observations on PIFs are summarised as follows:
  - PIFs would need to be made available by mainstream provider to appeal to the more risk averse because it would be an 'easier sell' for advisers as the well known brand names would be more readily acceptable to clients.
  - Listing PIFs was seen as being attractive to less sophisticated investors, but concerns were expressed that pricing would reflect market sentiment rather than the prospects of the underlying assets.
  - PIFs would most likely appeal to those investors seeking exposure to property but without lump sums to invest.
  - PIFs would be attractive if the transactions costs were lower and the structure was straightforward to understand.
  - The high-income distributions associated with PIFs will not prove attractive to all investors. Many of the financial advisers consulted raised concerns about the associated tax liability, particularly for higher tax payers.

Summary: Advisers to individual investors

- **Financial advisers are an important distribution channel selling two-thirds of regulated financial products and circa 25,000 advisers are authorised to sell unregulated collective investment schemes, including property products.**
- **Establishing a client's risk preferences is usually the first step in determining an investment strategy. The allocation to equities varies with risk preference.**
- **Commercial property figures strongly in asset allocation. The average allocation is surprisingly high at 21%, and the range is 10-25%.**
- **Software packages are often used in asset allocation and product selection; property is not well covered so advisers are reliant on their own due diligence and there is little comparative product analysis available.**
- **Reflecting clients' generally low risk preferences, the principal products sold are insurance company unit linked life products and authorised unit trusts.**
- **Unauthorised unit trusts and offshore property investment companies are seen as offering pros and cons. LPs are more appropriate for sophisticated investors.**

1.2 Small pension funds and charities

There are wide range of advisers to small pension funds and charities, including firms of independent financial advisers. Interviews were conducted with 10 advisers to small pension funds and charities.

- There is no typical asset allocation for small pension funds and charities from the adviser's point of view. Asset allocations depend solely on the needs and preferences of the client. However, it is significant that advisers were split about whether equities or property carried the most risk and this would condition their views on allocations.
- There is a consensus amongst the advisers that small pension funds and charities do not have sufficient funds available to invest directly into property. Nearly all advisers recommend indirect investments for these investors. The majority viewed property as a good diversifier, with access to specialist management and the relative ease of management also being attractions.
- Amongst those already invested, listed vehicles tend to be favoured together with unauthorised and exempt unit trusts.
- With the exception of pooled pensions products, the authorised products attract little interest from the advisers or their clients. Similarly, limited partnerships.
- Liquidity is perceived to be the principal disadvantage associated with indirect investment in property.
- Actions to improve access to the market include: relaxation of current regulation, the need for more tax transparent products and products that allow an easier exit than currently available. In this context, PIFs were seen as being beneficial.

Summary: Advisers to small pension funds and charities

- **There is no typical asset allocation as this depends solely on the needs and preferences of the client.**
- **There is a consensus amongst the advisers that small pension funds and charities do not have sufficient funds available to invest directly into property.**
- **Listed vehicles, unauthorised and exempt unit trusts tend to be favoured by advisers to small pension funds and charities whose clients are already invested indirectly.**
- **Liquidity is perceived to be the principal disadvantage associated with indirect investment in property.**

2. Introduction

Financial advisers have an important role in determining whether or not their clients allocate funds to commercial property and assessing on the suitability of the different commercial property products. This report summarises the findings of structured discussions with 30 advisers to individual investors, pension funds and charities.

These discussions have provided insights on the way investment strategies are developed, the asset allocation process and the relative perceptions of different asset classes. Specifically, views have been sought on commercial property as an investment, awareness of commercial property products and the perceived advantages/disadvantages of different categories of products.

A wide definition of financial advisers has been employed to include independent financial advisers, wealth managers, private client investment managers and pensions advisers. The rationale being that these organisations cover the full range of small investors as defined for the purposes of this study. However, it is important to note that there is no clear separation between the roles undertaken by these different groups. For example, all four groups may be expected to advise pension funds of different sizes.

3. Adviser market

To provide a broad basis for selecting interviewees, a brief analysis of the adviser 'market' was undertaken. What follows is by no means comprehensive but it provides some useful insights of the relative importance of different types of adviser, and in the case of the pensions funds, the dominance of several major firms of advisers.

3.1 Financial advisers to individual investors

Most financial products are sold face-to-face by financial advisers either directly or through independent financial advisers.

Direct sales predominantly take place via tied sales teams (owned by product providers), with a much smaller percentage via direct marketing, telesales and the Internet. The direct sales channel accounts for circa 20% of unit trust sales and a quarter of ISAs, but it is relatively unimportant for life and pensions products.

In contrast, independent financial advisers are the most important channel for selling pensions and life products. According to IFA Promotion[1], a non-profit organisation funded by 26 product provider sponsors, total new business in regulated products in 2001, excluding mortgages, was £21.87bn. Independent financial advisers sold 61% of these products by value, which equates to £13.31bn. Further detail is shown in the table overleaf.

Table 1: **IFA market share by product type**

Product type	Total New Busines 2001 APE[2] (£m)	IFA Market Share 2001 (%)
Long term insurance	10,939	62
Individual life	3,732	53
Individual pensions	3,300	76
Pension annuities	829	75
Collective investments	1,234	20
Group business	1,844	77
Total	**21,878**	**61**

Source: IFAP

There is no reliable source of the income this generated for IFAs in terms of fees and commissions, but in their report on the IFA market, Durlacher[3] employ an industry informed estimate of 4%. For regulated products this implies that the total value of IFA income in 2001 was £1.6bn. Note that Annual Premium Equivalent (APE) is the insurance industry's standard way of presenting data on the premiums for new insurance products sold. It is calculated as the sum of new annual premiums plus one tenth of single premiums. This means that the actual flow of money into insurance products in a given year is substantially higher than the APE figure.

It is also difficult to get up-to-date figures on the number of active financial advisers. In January 2002, the FSA put the total number at 77,000 of which 36,000 are authorised individuals. The principal market segments are shown in the table below and brief descriptions are provided overleaf.

[1] IFA Promotion (June 2002): Personal Financial Services New Business Report
[2] Annual Premium Equivalent is an insurance industry benchmark of Regular Premiums plus a tenth of Single Premiums
[3] Durlacher (2003) Independent Financial Anxiety

3. Adviser market

Table 2: **Financial advisers by segment**

Segment	Total No of RIs	(%)
Network	10,000	27.8
Nationals	2,800	7.8
Bank/building society	1,600	4.4
Independent	11,600	32.2
Professionals	10,000	27.8
Total	**36,000**	**100**

- Networks - most firms of advisers are small businesses with less than five registered individuals and there has been a growing trend for the businesses to join networks which centralise of non-core activities - research, administration, compliance and technology - and thereby achieve economies of scale that are passed on to the member firms. Durlacher estimate that 45% of IFA firms operate as part of 15 IFA networks.
- Nationals - these are integrated FSA-regulated firms with central management teams which set strategy, branding and provide training and development. The financial advisers are self-employed.
- Banks/building societies - some 26% of financial products are arranged through banks and building societies, but this figure includes mortgages. Driven by the regulatory changes that are restructuring the whole industry, several businesses in this category have acquired specialist firms of financial advisers to provide them with distribution.
- Independents - these are typically regional and local businesses, which in the latter case may comprise only one or two advisers.
- Professional - predominantly financial planners operating within or in close association with firms of solicitors and accountants

In light of the above, 20 interviews have been conducted with advisers drawn from all of the above categories, except banks/building societies due to the dominance of mortgage related business.

3.2 Advisers To Small Pension Funds and Charities

The advisers to small pension funds has been segmented by reference to the NAPF Yearbook, and specifically the subset of funds with total assets of less than £30m. Whilst a self-selecting sample of funds, the spread of advisers is considered to be relatively random. The table below shows the distribution of advisers to small pension funds ranked by the market value of assets within the funds advised. Interviews were conducted with a cross section of these advisers.

3. Adviser market

Table 3: **Adviser ranking by market value of funds**

Adviser	Market Value of Funds £m	% Total	Number of Funds
Mercer Human Resource Consulting	619.1	23.0	44
Hewitt Bacon & Woodrow	415.4	15.4	25
Watson Wyatt	174.9	6.5	33
Aon Consulting	117.3	4.4	12
SBJ Benefit Consultants	81.9	3.0	6
Jardine Lloyd Thompson	81.9	3.0	7
EB Consultants	81.3	3.0	3
Lane Clark & Peacock	73.9	2.7	5
Pricewaterhouse Coopers	66.4	2.5	3
Buck Consultants (now pt of Mellon)	65.1	2.4	3
Hymans Robertson	64.2	2.4	3
Towers Perrin	54.0	2.0	3
Heath Lambert Consulting	37.8	1.4	3
HSBC Actuarial Consultants	34.6	1.3	3
KPMG Actuaries & Pensions Consultants	33.1	1.2	3
Sun Life Assurance Society	16.3	0.6	2
Barnett Waddingham	15.7	0.6	3
Total Advisers To More Than One Fund	2,033.0	75.4%	161
Others	662.1	24.6%	32
Total NAPF Sample	**2,695.1**	**100.0%**	**187**

Source: NAPF Yearbook 2004

Ten advisers were interviewed. Seven of these advisers had a clientele that included both pension funds and charities, one advised only pension funds and two specialised in advice to charities.

4. Findings of Structured Interviews

The views of advisers to individual investors have been separated throughout from those of advisers to small pension funds and charities. However, as indicated above, to some degree, this separation is artificial.

4.1 Investment Process

Individual investors

Establishing risk preferences is an important first step taken by most advisers in determining an investment strategy for a client. Often this takes that form of a questionnaire, with some advisers relying upon proprietary software to assist them in categorising their clients. The common risk preference categories are: Cautious (low risk); Balanced (medium risk); and Adventurous (higher risk). These categories are then used to steer not only asset allocation, but also product selection (see below for further details).

Small pension funds and charities

There appear to be two principal points of entry for the adviser:

- The adviser establishes a strategic allocation with the client for all asset classes. In this instance, consideration is given to the maturity of the pension fund and profile of the membership. In the case of charities, there is more emphasis on matching current liabilities.
- The adviser starts client support after the strategic allocation has been established. In this case the strategic allocation is determined and only then is the discretionary mandate given to the adviser.

4.2. Asset Allocation

Individual investors

The proportion of equities is the key variable that alters with a client's risk preference. Hence, Cautious investors tend to have lower recommended weightings in equities than Balanced or Adventurous investors. Table 4 below shows that the average allocation is 29% but for Adventurous investors the equities weighting increases to 70%.

Similarly, Table 4 shows that the average allocation to property for a Cautious investor is 21%, but this allocation falls as the weighting in equities rises for investors who have greater preference for risk. Hence, the typical allocation for an Adventurous investor is just 15%.

Table 4: **Asset allocations - cautious investor (%)**

Asset	Average	Lowest	Highest
Equities	29	20	40
Bonds	23	5	40
Property	21	10	25
Cash	10	0	20
Other	17	0	30

The choice of products within those allocations is often guided by a review of the client's lifestyle profile covering factors such as life stage, preferences for income or capital, tax status and inheritance tax planning. Once asset allocation preferences are agreed with a client i.e. specific dislikes have been excluded, then the adviser typically moves on to consider product selection.

Several advisers mentioned that they sought initially to utilise available allowances, which led them to recommend ISAs and other tax efficient products ahead of others.

Investment in equities tends to take place via investment trusts and OEICs, rather than directly in the companies.

Small IFAs tend to use proprietary software packages to determine asset allocation, according to risk preference. However, these packages do not include property, so it is left to the adviser to allocate.

To help identify suitable products small independent firms of advisers also often use product selection software, such as Synaptic, and other sources, such as S&P Micropal and fund fact sheets. Property products are not well covered, making the decision-making process more difficult.

Consequently, a number of advisers noted that a key stage in the product sales process was their own due diligence on the product, which required their 'buy-in' before it would offers to clients. This approach applied particularly to property where there was little comparative analysis available.

Small pension funds and charities

There is no typical asset allocation for small pension funds and charities from the adviser's point of view. Asset allocations depend solely on the needs and preferences of the client.

Some advisers noted that mature pension funds are likely to have a higher allocation to bonds, in comparison to an immature fund. This shift in allocation is due mostly to the fixed income characteristics of bonds.

One adviser mentioned that the exposure to indirect property investment vehicles seems to be more popular with the immature pension funds.

In terms of risk ranking, five advisers thought that cash had the lowest risk, followed by bond investments.

Significantly, opinions were exactly split between equity or property as to which was the most risky asset class.

4.3. Risk

Individual investors

In terms of risk, property was placed in the middle of the ranking between equities which are seen as carrying the most risk and bonds with less and cash with the least.

Small pension funds and charities

Significantly, opinions amongst advisers to small pensions funds and charities were split between whether equity or property was the most risky asset class. In part, this may be a reflection of the expressed preference for listed vehicles (see below). Half the adviser consulted thought that cash had the lowest risk, followed by bond investments.

4.4. Portfolio Review

Individual investors

The frequency with which financial advisers review the structure of portfolios with their clients is conditioned by the value of the portfolio and by the asset allocation. On average, portfolios are reviewed annually, but high value portfolios and those with higher equity weightings tend to be reviewed more frequently.

Small pension funds and charities

Usually, there is an annual review of the portfolio structure with the client, but the reviews are predominantly driven by client request. Only two advisers recommended a three-year review. One adviser pointed out that this length of review would coincide with the valuation of the pension fund.

4.5. Commercial Property Investment

Individual investors

As indicated above, commercial property figures strongly in the asset allocation advisers recommend to their clients. Some direct investment in property assets is made when the client's portfolio is sufficiently large or there is pension related investment in business premises. In most instances, property is considered to be a longer-term investment i.e. five years plus.

Small pension funds and charities

There is a consensus amongst the advisers to small pension funds and charities that investors do not have sufficient funds available to invest directly into property. All advisers interviewed, except one, advise on indirect investments for smaller investors. The majority of advisers viewed property as a good diversifier and three said that they advise on indirect investment as both a tactical and a strategic investment.

4.6. Commercial Property Funds

All the advisers interviewed were asked for their preferences for different types of commercial property products and to explain the advantages/disadvantages as they saw them. Their responses are summarised below and include comments that are, in some cases, known to be misinformed.

Individual investors

For many financial advisers, their clients are inherently risk averse, so the principal property products taken are insurance company unit linked life products. The principal attractions of these funds are seen as being: the good range available, the diversified nature of the underlying assets, the competitive charging structures and the ability to withdraw 5% of their initial investment annually without tax penalty is seen positively.

However, some advisers were critical of these products citing the diversified nature of these portfolios as a positive disadvantage because this restricted the ability to be selective.

A number also place clients in authorised unit trusts because they provide a low risk (i.e. ungeared) entry into property, particularly for those with smaller portfolios; they are considered to have performed relatively well; they are associated with reliable brands; and they are relatively easy to track.

However, others commented that they did not favour AUTs because of the limited choice available, dilution of returns from the investment of an influx of new money, which was also pushing fund managers into becoming forced buyers. Others mentioned the drag on performance from cash holdings, particularly in light of recent inflows of new money.

Unauthorised unit trusts were favoured by several advisers because they are readily understood by the clients.

Offshore property investment companies were seen as being advantageous for the tax efficiencies that they offer but several mentioned that pricing reflects market sentiment not the performance of the underlying assets and the charges are relatively high.

A number of advisers interviewed mentioned that they generally look at the prospects for the underlying investment assets before recommending commercial property products to clients. Indeed, several commented that they had severe reservations about recommending 'blind' funds to clients.

More sophisticated clients often have views on the prospects for different locations, so limited partnerships are seen by some advisers as being attractive because these offer identifiable properties.

Moreover, the availability of capital allowances on some LP deals was considered to be a big plus by several advisers consulted. Although the view of others was summed up by one adviser who commented that the 'tax tail should not wag the investment dog'.

The costs and illiquidity of these products were seen as being their principal disadvantages. Although the relatively high minimum investment (£25,000) tends to mean that clients are more sophisticated and therefore accepting of the long-term nature of their investment in LPs. The level of gearing on some products was also mentioned as a disadvantage.

However, the complexity and unfamiliarity of the LP structure made these products harder for some advisers to understand and making them a harder 'sell', particularly to less financially educated clients.

A number of advisers mentioned the use of offshore bonds as a mechanism for tax-exempt route for investors into limited partnerships.

Small pension funds and charities

The authorised products do not seem to attract much interest from the advisers or respectively their clients. The exception to this rule seem to be the pooled pensions products, which were named several times by respondents.

All listed products (investment trusts, UK property companies and offshore property companies) were mentioned as the favoured structures for indirect property exposure. The most common form was investment in UK property companies.

Within the segment of unregulated products especially unauthorised or exempt unit trusts were mentioned. Limited partnerships and offshore property funds were not as popular but were also mentioned.

One of the key advantages for indirect property investment was the minimum investment amount required. Specialist management and the relative ease of management for the investment manager were also key attractions. Furthermore, the direct exposure to property returns, liquidity and the past performance record have been mentioned as a positive features of property.

However, the major disadvantage identified by most advisers was liquidity. The long time horizon for some property investments was also seen as a problem and this was linked indirectly with liquidity. The monitoring that property funds require was also seen as a disadvantage.

4.7. Broadening Access To Commercial Property and the Scope for PIFs

Advisers were asked for their views on the actions that need to be taken to broaden the access of investors to commercial property and whether PIFs would be of interest to their clients if such a vehicles were introduced.

Individual investors

There was no consensus of the actions that needed to be taken to broaden the access of investors to commercial property. A number mentioned the need to simplify the product offering and reduce costs. Others would like to see more ISA-able property products as a way of getting smaller investors into property.

The high-income distributions associated with PIFs will not prove attractive to all investors. Many of the financial advisers consulted raised concerns about the associated tax liability, particularly for higher tax payers. One adviser described high-income distributions as "a nuisance" as much of their activities are geared towards tax sheltering for their higher net worth client base.

PIFs would need to be made available by mainstream provider to appeal to the more risk averse because it would be an 'easier sell' for advisers as the well known brand names would be more readily acceptable to clients.

Listing PIFs was seen as being attractive to less sophisticated investors, but concerns were expressed that pricing would reflect market sentiment rather than the prospects of the underlying assets.

PIFs would most likely appeal to those investors seeking exposure to property but without lump sums to invest.

PIFs would be attractive if the transactions costs were lower and the structure was straightforward to understand.

Also seen as a possible tactical investment to gain exposure while awaiting the right direct investment opportunity.

Small pension funds and charities

There was no consensus amongst the advisers to small pension funds and charities about actions to be taken to improve access to the market. The interviewees mentioned a relaxation of current regulation, the need for more tax transparent products and products that allow an easier exit than currently available. The introduction of property investment funds was mentioned specifically as being beneficial.

Several advisers saw no need for action or were not sufficiently engaged enough in the sector to comment.

Working Paper Four

Small Pension Funds & Charities

This report summarises the findings of desk-based research to establish the universe of smaller pensions funds and charities, together with interview survey work with 23 pension funds and 18 charities with total assets of less than £30m.

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1. Summary

This report summarises the findings of desk-based research to establish the universe of smaller pensions funds and charities and details the findings of the survey into the investment activities of small pension funds and charities with total assets of less than £30 million

- There are no definitive statistics on the total value of assets held in UK pension funds. In 2003, UBS Asset Management estimated the market to be around £847bn, whereas Mercer Investment Consulting estimate it to be over £1,000bn.
- The large pension funds make up the vast majority of the pension fund universe by value, but the smaller funds, with assets of less than £30m, represent a large percentage of the universe by number. It has not been possible to quantify the exact number or value of their assets, but it is estimated that there are more than 98,700 'live' occupational pensions schemes that each have total assets of less than £30m. These schemes account for 98% of all occupational pension schemes, and together they own an estimated £61.1.2bn of assets.
- The quantification of the universe of UK charities has proved to be equally difficult. There are circa 163,000 registered charities, with an estimated total value of £70bn. The Charities Commission cannot provide a figure for the number of charities that fall into the £0-30m bracket. However, Caritas Data (the providers of data to the National Charities Database) holds data on 20,710 charities; 13,447 (65%) have a value of under £30m.
- Interviews were conducted with 23 pension funds and 18 charities with total assets of £317.4m and £292.2m respectively. The size range was £50,000 to £30m.
- Small pension fund investment is predominantly in equities - the weighted average allocation is 66%. Despite being categorised as being the highest risk asset class, equities are seen as the primary means of meeting long-term liabilities.
- However, there has been some structural changes over the last five years with downward adjustment in equities allocations in favour of bonds and respondents indicated that further shifts in this direction are likely. The average allocation to bonds is 28%.
- Small charities are less heavily exposed to equities (the weighted average allocation is 49%), and the rationale for holding these assets is more to do with income production than matching longer term liabilities. Their investment in bonds is also typically lower than small pension funds at 11%. However, at 24%, their cash weighting is also much higher than small pension funds (1%).
- A third of small pension funds and charities interviewed have commercial property investments, both direct and indirect. The average allocation to property by small pension funds and charities is 2% and 15% respectively. Property is held in small funds for many of the same reasons as it is held by large funds, namely, income production, capital growth, diversification, and long term liability matching. However, the much higher allocation by charities also reflects holdings in 'legacy type' assets and operational property.
- Small pension funds and charities invest in a wide range of indirect products. Diversification is the main driver for indirect investment, and according to those interviewed this is likely to remain so.
- The majority of investors were disinclined to invest in direct property in future because of its illiquidity, possible lack of diversification, high entry cost and the risk profile. Other reasons for not pursuing direct property investment include regulations, search costs, unsteady income stream and unfavourable returns.

1. Summary

Summary: Pension funds and charities

- Some 98% of all occupational pension schemes (98,700 schemes) have total assets of less than £30m. These schemes own an estimated £61.1bn of assets.
- There are circa 163,000 registered charities. Available data suggests that 65% have total assets of less than £30m.
- Small pension fund invest predominantly in equities (66%) as this is seen as the primary means of meeting long-term liabilities. Small charities hold less in equities (49%) to meet current liabilities.
- There has been a structural shift away from equities in favour of bonds (the average allocation by small pension funds is now 28%).
- A third of small pension funds and charities have commercial property assets, held either direct or indirect.
- Income, capital growth, long term liability matching and diversification are the main drivers for holding property. The latter is the key reason for holding indirect investments.

2. Background

The real estate investment strategies of large institutional investors are well documented. Allocation levels, high in the late 1970s and early 1980s, dropped consistently through the equity boom. In the mid-1990s allocations reached a low point, and it appeared possible that real estate would cease to be seen as the third asset class. At this point liquid and divisible listed real estate shares – simply a sector of the equities market - appeared likely to become the property vehicle of choice.

The equities crash of 2000-2002 coupled with an emerging out-performance record saw property recover its attractiveness and a rebound in institutional allocations followed. Supported by the absence in the UK of a tax-efficient listed property vehicle exemplified by REITs in the US, private pooled vehicles replaced listed property companies as the indirect vehicle of choice.

In the new millennium investment in property by private individuals (the retail market) became a growing business, represented by increasing interest by wealth managers, the creation of feeder funds which enable retail investors to access institutional products, and the launch of new pooled and unlisted vehicles designed by a range organisations (from Scottish Widows and Isis to Close Brothers and Matrix Securities) for the private investor.

However, in 2004 the exposure of the man or woman in the street to commercial property remained unmeasured. The appetite amongst retail investors for property was poorly understood, and the various ways in which the retail investor accessed the market was both complex and largely unrecorded.

Similarly, smaller charities and the smaller pension funds – including the SIPP and SSAS schemes which offer an alternative route into tax-efficient investment for the private investor – represented an under-researched component of the investment market.

In 2004 the UK government announced a consultation exercise designed to prepare the way for a UK REIT or PIF (property investment fund). Given the likely divisibility and liquidity of this instrument, a significant improvement in our understanding of the smaller investor is vital in developing an industry view of the necessary or preferred features of such a vehicle when it is launched.

This research is designed to contribute to this process of improving the knowledge and understanding of the investment decisions and procedures operated by the smaller pension funds and charities. In the report we address the following questions:

- How much exposure does the smaller investor have to property?
- How does property sit within the small investors' wider portfolio?
- What are the perceived advantages and disadvantages of the current routes into property investment for smaller investors?
- How do the smaller investors manage their portfolios and investment strategies?

3. Research background

This report details the findings of the survey into the investment activities of small pension funds and charities with total assets of less than £30 million.

Initial research was undertaken to examine in the first instance the total size of the pension fund and charity universe in the UK. The collection of reliable data in this area proved difficult because of the small size of the target organisations.

In their 2003 survey, Mercer Investment Consulting estimated the total UK pension fund market as being worth £1.04 trillion. The UBS Asset Management Survey (2004) estimated that the UK pension fund market had approximately £958bn of assets under management at the end of 2003, up from £847bn a year earlier. This latest estimate is made up of £708bn in occupational fund assets and £250bn in private pensions.

Large pension funds make up the lion's share of the pension fund universe by value. Although the smaller funds (those with a value of £100,000 or less) represent a large percentage of the universe by number, it is extremely difficult to estimate their exact value, as no organisation is responsible for the registration of all UK pension schemes and their value. The Occupational Pensions Regulatory Authority (OPRA) has a responsibility to record and supervise a range of legal requirements to protect citizens' occupational pensions. As part of this responsibility OPRA has built a database of pension funds but this information is not publicly available. The only publicly available data categorises pension funds by number of members, not by fund value.

OPRA data indicates that there were 100,500 occupational pension schemes in operation in the UK in 2003, so by using the UBS estimate of total asset value, it has been possible to estimate the total assets owned by schemes in each size band.

Table 1: **Estimates of Occupational Pension Schemes By Value (2003)**

Size bands	Number of scheme members	Total assets (£m estimate)	Number of schemes	Average scheme value (£m estimate)
2-11	241,431	6,807	80,649	0.1
12-99	450,546	12,703	12,113	1.0
100-999	1,887,245	53,209	5,990	8.9
1000-4999	2,630,537	74,165	1,234	60.1
5000-9999	1,597,427	45,038	227	198.4
10000+	18,304,667	516,079	323	1,597.8
Total	**25,111,853**	**708,000**	**100,536**	**7.0**

Sources: OPRA, UBS

Whilst not a substitute for reliable data, these estimates imply that at least 98% of schemes have total assets of less than £30m, and that the value of the smallest schemes is very small indeed.

In addition, more than 70% (72,400) of occupational pension schemes are money purchase schemes, where almost 1m individuals have some discretion over the choice of assets. Fewer than 300 of these schemes have total assets greater than £30m.

3. Research background

There are circa 102,000 self-invested pension plans in operation. Most, if not all, of these plans may be expected to hold total assets of less than £30m.

The NAPF year book 2004, which was the main source of contact information for the survey, comprises 194 member funds with total assets of less than £30m, which together total approximately £2.75bn.

The quantification of the universe of UK charities has proved to be equally difficult. The Charity Commission is established by law as the regulator and registrar for charities in England and Wales. As at March 2003 the Charity Commission estimated that there were 163,013 main charities on the register, with an estimated total value of £70 billion. The register cannot provide a figure for the number of charities which fall into the £0-30 million bracket. Caritas Data (the providers of data to the National Charities Database) holds data on 20,710 charities; some 65% of these have a value of under £30m.

The difficulty in finding data on the small investor universe of pension funds and charities has made the market sizing part of the research very difficult. The lack of information does illustrate quite clearly the potential problems for the dissemination of information to the small investor market, as there appears to be no clear idea how many there are and how to contact them.

A random sample from the available data was used for the purposes of the research reported below.

4. Research methodology

In order to achieve a cross section by value the survey population of pension funds and charities were split into six bands, each with a range of £5 million. The bands are as follows:

Band 1 - £0-5 million
Band 2 - £6-10 million
Band 3 - £11-15 million
Band 4 - £16- 20 million
Band 5 - £21-25 million
Band 6 - £26-30 million

In total 23 pension funds and 18 charities were interviewed giving a total of 41 responses. The size of funds interviewed ranged from £50,000 to £30 million.

Table 2: **Sample responses**

Band (£m)	Number of pension funds	Value of pension funds(£m)	Pension fund universe (%)	Number of charities	Value of charities (£m)	Charity universe (%)
£0-5	7	13.3	4.2	4	6.7	2.3
£6-10	3	22.0	6.9	2	14.7	4.9
£11-15	3	38.8	12.2	1	10.5	3.6
£16-20	2	32.7	10.3	3	59.9	20.5
£21-25	5	122.3	38.6	3	65.1	22.3
£26-30	3	88.3	27.8	5	135.3	46.4
Total	**23**	**317.4**	**100.0**	**18**	**292.2**	**100.0**

Of the pension funds interviewed 40% described themselves as being mature funds with short term liabilities to consider when making investment decisions. A further 40% described themselves as being immature and so had a very different set of longer term investment objectives. The maturity of the charities interviewed had little or no impact on their investment decisions.

5. Small investor profiles

Table 3: **Weighted average allocations to the various asset classes (by fund value)**

	Equities (%)	Bonds (%)	Property (%)	Cash (%)	Other (%)
Pension funds	66	28	2	1	2
Charities	49	11	15	24	2
All	**58**	**20**	**8**	**12**	**1**

Of the small investors interviewed, pension funds have a higher current and target allocation to equities and bonds and charities have a higher current and target allocation to property and cash.

Table 4: **Weighted average target allocations to the various asset classes (by fund value)**

	Equities (%)	Bonds (%)	Property (%)	Cash (%)	Other (%)
Pension funds	64	32	2	1	2
Charities	46	11	16	23	4
All	**55**	**22**	**8**	**11**	**3**

5.1 Equities

The vast majority of small investors invest in equities and they accounted for by far the highest allocation across all investment classes. The charities interviewed do have a lower percentage allocation to this asset class than the pension funds interviewed. Three pension funds and seven charities (24% of the total sample) did not have exposure to this asset class. One of the non-investors, a mature pension fund, explained that it did not have an exposure to equities because it needed to hold the majority of its fund in cash in order to meet its liabilities.

The investors surveyed (52% of pension funds and 22% of charities) regarded equities as being a good way of matching long-term liabilities. Other reasons for investing in equities were the potential for income delivery (13% of pension funds) and capital growth (22% of pension funds and 11% of charities). Investment in equities was also used as a means of diversifying portfolios.

Table 5: **Investment in equities**

	Pensions funds			Charities		
Band	Average allocation %	Lowest allocation (£m)	Highest allocation (£m)	Average allocation %	Lowest allocation (£m)	Highest allocation (£m)
£0-5 m	53	0.08	3.4	27	2.2	2.2
£6-10 m	50	2.5	4.4	65	5.8	5.8
£11-15 m	85	8.8	14.3	20	2.1	2.1
£16-20 m	63	9.1	11.3	74	12.7	16.7
£21-25 m	49	7.7	21.7	40.6	11.9	14.8
£26-30 m	75	21	23.4	43	18.7	26

Pension fund respondents acknowledged that there is likely to be a reduction in the percentage allocation to equities over the next five years. The target allocation figure fell from an average current allocation of 66% to a target of 64% over the next five years. The target allocation to equities within the charities sample also fell from 49% to a target of 46%. The move away from equities can be seen as a result of a number factors, including the riskiness of the asset class and poor performance over recent years.

5.2 Bonds

20 pension funds and nine charities invest in bonds with average allocations of 28% and 11% respectively. Like equities, bonds were identified as a good means of meeting long-term liabilities (by 56% of pension funds and 17% of charities). Income production (13% of pension funds and 28% of charities) and capital growth were also seen as advantages.

Table 6: **Investment in bonds**

	Pensions funds			Charities		
Band	Average allocation %	Lowest allocation (£m)	Highest allocation (£m)	Average allocation %	Lowest allocation (£m)	Highest allocation (£m)
£0-5 m	12	0.01	0.4	5	4.6	4.6
£6-10 m	43	0.6	5.8	20	2.3	8.2
£11-15 m	15	3.8	3.8	7	3	6.2
£16-20 m	38	4.8	7.5	15	0.7	0.7
£21-25 m	26	2.4	17.1	16.5	1.8	1.8
£26-30 m	21	4	9	4	0.4	0.4

Overall the pension funds interviewed indicated there was an increase of four per cent in the target allocation to bonds. There was no change in the target allocation to bonds by the charities interviewed.

5.3 Cash

Eight pension funds and 12 charities had some exposure to cash, with average allocations of 1% and 24% respectively. Three pension funds stated they held a proportion of their fund in cash in order to meet their liquidity requirements and short term liabilities. All of these were mature pension funds with current or short-term commitments to pensioners.

11% of charities interviewed recognised the value of holding cash for short term liability matching. Of those charities which held a high proportion of their portfolio in cash, one had only recently been established and was still deciding on an investment strategy. Another charity noted that it had a relatively secure income stream and therefore felt that there was no need to invest in other asset classes.

Table 7: **Investment in cash**

Band	Pensions funds			Charities		
	Average allocation %	Lowest allocation (£m)	Highest allocation (£m)	Average allocation %	Lowest allocation (£m)	Highest allocation (£m)
£0-5	12	0.01	0.1	68	0.1	3.9
£6-10	5	0.9	0.9	3	0.4	0.4
£11-15	-	-	-	3	0.3	0.3
£16-20	-	-	-	11	6.3	6.3
£21-25	2	0.8	1.2	35.5	0.3	21.4
£26-30	1	0.9	0.9	26	0.5	26.2

There was no change in the target allocation to cash by the pension funds interviewed. Charities, on the other hand, recorded a one per cent reduction in the target allocation to this asset class.

5.4 Investment in other asset classes

One pension fund and one charity invested in managed funds, investing 97% and 54% respectively. It was perceived that managed funds gave the investors a means of income production, long term liability matching and diversification. One charity invested about five per cent of its allocation in hedge funds. This was reported as a manager-driven decision.

The charities interviewed increased the target allocation to other asset classes by two per cent. The target allocation for pension funds did not change.

5.5 Investment in property

36% of the small investors surveyed invest in some form of property. Eight (35%) of the pension funds and seven (39%) of the charities invest in property with average allocations of 2% and 15% respectively.

Within the charities sample some of the respondents mentioned that they held 'legacy type' properties. It is likely that these will have had an impact on the reported allocations within this sector. One investor said that they held 98% of their portfolio in property, a large proportion of this being operational property. Holding property as an operational asset, or in one instance running a property-related charity was regarded as a disincentive to further property investment. The reasons given were to do with over-exposure of the fund to the sector.

5. Small investor profiles

Table 8: **Investment in property**

	Pensions funds			Charities		
Band	Average allocation %	Lowest allocation (£m)	Highest allocation (£m)	Average allocation %	Lowest allocation (£m)	Highest allocation (£m)
£0-5	8	0.07	0.3	-	-	-
£6-10	2	0.3	0.3	20	0.4	2.0
£11-15	-	-	-	60	6.3	6.3
£16-20	-	-	-	-	-	-
£21-25	4	1.2	2.4	7.5	0.5	4.5
£26-30	2	2.0	2.0	27	2.7	26.6

When the property investors were asked why they invested in property as an asset class they gave the following reasons. Income and capital growth were mentioned by 13% of pension funds and 16% of charities respectively. Diversification and long term liability matching were also cited. Despite these quoted attributes property still represents a relatively small proportion of the total asset allocation for pension funds and an even smaller proportion for charities. The average allocation to property, across all the small investors interviewed, is relatively low at 8%. This is in contrast to equities, bonds and cash which accounted for 58%, 20% and 12% respectively.

The pension funds interviewed did not foresee a change in their target allocation to property, in comparison, the charities were looking to increase their target allocations to this sector by one per cent.

6. Direct property investment

One pension fund and five charities invest in direct property. The allocation to property for four out of the five charities was historical, rather than based on recent investment decisions. The other charity invested in direct property for the good returns achieved.

The highest average allocation to property by the pension funds (perhaps surprisingly) came from band 1 (£0-5 million). This can be explained by tax efficient investment in occupational property by small pension funds. Unlike the pension funds interviewed, none of the very small charities in band 1 invested in property. Both pension funds and charities in band 4 did not undertake property investment in any form.

Pension funds and charities all identified diversification, good returns, inflation hedging, income production and capital growth opportunities as reasons for direct property investment. No single feature stood out as being the main driver for investment.

Illiquidity, high entry costs, high-risk profiles, the lack of diversification and management intensity were all cited as disadvantages of direct property investment. The latter two examples were the most frequently remarked upon. The management intensity associated with property investment is illustrated by the fact that over 80% of the investors had a role in the management of their property portfolio, with one charity relying on totally on external managers.

7. Indirect property investment

Table 9: **Indirect investments (total)**

Investment class	Number of investors
Investment trusts	3
UK property companies	4
Offshore property companies	1
Authorised property unit trusts	2
Unit linked life & pensions	2
Pooled pensions	1
Unauthorised and/or exempt property unit trusts	2
Common investment fund	1

Six pension funds and two charities invest indirectly in property. Diversification was quoted as the main driver for this. One pension fund invested in all forms of property in the range of listed and authorised products. Two pension funds from band 1 (£0-5 million) invested in unauthorised (exempt) property unit trusts, two pension funds from band 5 (£21-25 million) invested in listed products and one pension fund invested in an authorised property unit trust. These pension funds are spread throughout the bands indicating that indirect investments are accessible to pension funds of all sizes.

Of the two charities which invest in this sector, one invested 2.4% of its allocation indirectly in the Charities Property Fund. The other split its total commitment of five per cent between listed UK property companies and a pooled pension fund.

8. Non-Investors in Property

22 (just over half) of the small investor sample were not currently investing in property. Of these only four had a history of property investment. One pension fund and one charity previously invested directly and one pension fund had indirect exposure, in both listed as well as unlisted unitised funds. One pension fund knew that there was a history of property investment but did not know in what form.

When questioned why they no longer invest in property the interviewees reported that there had been reductions for liquidity reasons, and because of the risk and uncertainty of the income stream.

Of those four historic investors only the charity would reconsider investing in property – though moving from the direct to the indirect sector.

One charity did indicate that their investment managers had not promoted property as an asset class to invest in. A pension fund interviewee also mentioned that their manager did have a mandate to invest in property but had never exercised the option.

8.1 Future of property investment

If investment in property were to be considered in the future, the majority of funds stated they would use indirect structures. Four of the funds which were contemplating investing in property in the future named indirect investment exclusively; three entertained all alternatives and four would consider either indirect or listed exposure.

Two of these funds excluded direct because of their size.

Table 10: **Future property investment (total)**

	Direct (%)	Indirect (%)	Listed (%)
Yes	13	48	30
No	87	52	70

Portfolio diversification is the key driver for future property investment. The majority of investors were disinclined to invest in direct property because of its illiquidity, possible lack of diversification, high entry cost and the high risk profile. Other reasons for not pursuing property investment were the high search costs, unsteady income stream and unfavourable returns. One pension fund also mentioned that the new FRS17 accounting regulations would deter them from investing in property, probably because they believed the strict valuation requirements imposed on pension funds by the regulations were too onerous.

9. Risk profiles for different asset classes

Table 11: **The view of risk**

	Pensions funds				Charities			
Risk Factor	**Equities (%)**	**Bonds (%)**	**Property (%)**	**Cash (%)**	**Equities (%)**	**Bonds (%)**	**Property (%)**	**Cash (%)**
1 (highest)	89	-	11	-	45	-	-	37.5
2	5.5	55.5	67	-	33	50.0	33.3	-
3	5.5	39	22	29	11	37.5	50	-
4 (lowest)	-	5.5	-	71	11	12.5	16.7	62.5

Equities

Both pension funds and charities viewed equities as the riskiest asset class. 89% of pension funds took the view that equities carried the highest risk, while only 45% of charities rated equities as the riskiest asset class.

Bonds

Of those who responded to the survey 94% of pension funds and 87% of charities reported that they considered bonds to be the second and third most risky asset class.

Cash

Cash was seen by pension funds as the least risky asset. However, 37.5% of charities saw cash as a high-risk asset. This perception may be the result of a number of charities having a very high exposure as a percentage of their total asset allocation to the asset class.

Property

Pension fund respondents regarded property as the next most risky asset class after equities, with 11% of pension fund investors placing property as the riskiest asset class. The vast majority of pension funds (67%) saw property as the second most risky asset class. The charities provided a slightly different picture with regard to risk. For example, 37% of charities thought that property was a high risk asset.

10. Portfolio structure and management

The interviewees were questioned on a number of procedural matters in an attempt to understand their approach the management of their investments. Firstly interviewees were questioned regarding the management of their portfolios.

The majority (46%) of investors relied on portfolio strategy reviews being the responsibility of both internal and external teams. Only 14% of mandates for small investors were executed externally. If this is broken down within the two investor classes the majority (50%) of pension funds were managed internally. In contrast, only 27% of charities were solely internally managed. Charities favoured the combination of internal and external experts to manage their investments. Smaller charities are less likely to have investment professionals within their organisations than their pension fund counterparts.

Table 12: **Review frequency**

Review frequency	Pension funds (%)	Charities (%)	Total (%)
More than once a year	32	57	42
Annual	41	29	36
Less than once a year	27	14	22

The interviewees were asked how frequently they reviewed their portfolio. The majority (78%) reviewed their portfolios at least once a year. The actual review pattern varied from quarterly to annually. Over half, 57%, of charities undertook reviews with the greatest frequency (more than once a year on average), possibly reflecting the need to meet with their external advisors. The majority of pension funds conduct annual reviews.

10.1 Changes to portfolio structure

Over half the pension funds and almost 40% of charities interviewed said that they had made significant changes to their portfolio structure over the past five years. The most frequently cited change was a decrease in equities and a subsequent increase in investment in bonds. Individual investors made other comments, which are reported below:

Pension funds

- "We increased our allocation to cash but decreased our exposure to bonds"
- "We reduced our property allocation and increased the percentage allocation toward bond and equity"

Charities

- "We decided to move out of equities into bonds but are now considering a move back"
- "We would like to increase our investment in property"
- "We have decided to invest in property for the first time focussing on indirect property funds and also looking at hedge funds"

10. Portfolio structure and management

Table 13: **Asset allocation changes over the past five years**

	Decrease equities (%)	No change (%)	Other (%)
Pension funds	44	41	15
Charities	17	61	22
Total	33	50	17

There has been a noticeable move by smaller investors to gain a greater level of diversification within their portfolios.

When questioned about the future of the portfolio a large percentage of the respondents (68% of pension funds and 56% of charities) said they were expecting to change their portfolio allocations.

Table 14: **Expected portfolio changes in the next five years**

	Pension funds (%)	Charities (%)	Total (%)
Change	68	56	57.5
No change	32	44	42.5

Of the pension funds which were expecting significant changes in the future, nearly 40% were anticipating a decrease in their allocation to equities. One pension fund was considering moving into indirect property through a 'funds of funds' product, with another considering making a 10% allocation to a property unit trust. One pension fund was considering a move away from UK equities and bonds to global equities and bonds.

Table 15: **Asset allocation changes over the next five years**

	Decrease equities (%)	No change (%)	Other (%)
Pension funds	36	32	32
Charities	-	56	44
Total	20	43	37

The majority of charities were not expecting any significant changes in their portfolio structure over the next five years. Of those who did expect a change, 50% were considering some form of property investment.

11. Conclusions

A number of key points can be drawn from the research, including the need for improved information and a greater understanding of the operational nature of the investors and the investment requirements they have.

There is a need to educate the smaller investor in ways that they can access the property investment market: firstly, by improving the flow of information from product providers to the investors and /or their managers; and, secondly, a clearer picture of the small investor universe would prove invaluable for the managers and advisors who would naturally advise these investors.

Without a clear plan of how to disseminate information regarding the range of products available to the small investor, such as the existing private vehicles or the proposed PIF structure, the property industry will fail to attract a significant body of investors.

Differences in the way small investors operate in comparison to the larger institutional pension funds and charities should be taken into consideration in analysing their investment policies. For example, some smaller corporate pension funds are controlled by single families or by small groups of partners. It is a well known tax planning exercise for such businesses to include operational property in the assets of the corporate pension scheme and to lease it back, thereby reducing the risk of voids and accruing tax free capital gains. This may explain the higher allocations to property among the very small schemes.

The charities interviewed appear to have very varied allocations to property. This is less true of pension funds. One observation is that charities own operational property and other property which is bequeathed by donors. This skews the asset allocations away from those which may be produced by pure investment considerations.

In the UK government's consultation document on the introduction of a UK REIT or PIF (property investment fund) it identified the need to address the current lack of choice for smaller investors, and the poor liquidity associated with property investment. This report has highlighted the fact that many smaller investors are deterred from investing in property due to the illiquid nature of the asset class, the lack of potential diversification, high entry costs and the high-risk profile. A REIT type vehicle would address many of the disadvantages citied offering a potentially liquid and low cost way of accessing the asset class.

However, there is debate about the ability of REIT type structures to offer direct property type returns. If we consider the US REIT or the Australian LPTs (listed property trusts) returns have mirrored those produced by the equity market eliminating some of the diversification benefits provided by property.

This research shows there is a strong preference among small pension funds and charities for indirect routes into the asset class. It is possible that a public PIF would meet this need, but it is also possible that private PIFs will be attractive to smaller institutional investors. The attraction of private indirect property vehicles is supported by a general reduction in the appeal of equities.

Working Paper Five

Commercial Property Product Review & Evaluation

This report presents an inventory of the main fund structures that are used to create property investment products sold to smaller investors. It provides a comparative analysis of the main features of each. It also provides a summary of the feedback from product providers received during interviews with them, and integrates comments on different products received from financial advisers.

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1. Summary

This report provides a description of each of the main types of fund structure used for commercial property investments targeted at smaller investors. For each fund type, the key features are given and an analysis is provided of the main advantages and disadvantages.

Fourteen different product structures have been reviewed against six key criteria:

- Marketability (legal & regulatory requirements)
- Accessibility (min investment level)
- Liquidity (time to transact, cost)
- Pricing mechanism (property valuation or market sentiment)
- Flexibility (constraints on gearing or investments)
- Tax treatment (leakage within the vehicle)

The following general conclusions can be drawn from this review:

- There appear to be a relatively large number of different structures available for small investors of different categories to gain indirect exposure to commercial property.
- However, there is often limited choice within each category. For example, there is only one investment trust that invests in direct property, there are currently only two common investment funds and only three authorised unit trusts.
- Moreover, certain types of investors may be excluded from investing due to their tax status, or by the minimum investment amount required. For example, many unregulated schemes have minimum investment requirements of £25,000+.

Taking a different perspective and evaluating the available array of products against the needs of different categories of small investors provided further insights. The needs of these investors have been derived from different project workstreams.

Small pension funds and charities have the widest range of product categories to choose from and their requirements can be summarised as:

- Liquidity
- Low transaction costs
- Small lot size

Sophisticated investors are currently much better served in terms of available products than those with smaller sums to invest. Defined as being those with more than £25,000 to invest at one time, these individuals may also be expected to have a greater appetite for risk have a better understanding of financial products. The potential market size exceeds 2.1m people. This group have a greater preference for unlisted vehicles that are a better proxy for direct investment.

1. Summary

Individual investors who have both a lower appetite for risk and less than £25,000 to invest have a limited range of products to choose from currently. The needs of this group, which potentially amounts to between 2.75m and 3.0m people, can be summarised as follows:

- Small minimum investment
- Liquidity
- Low transaction costs
- Listed/Authorised
- Onshore
- No/limited tax within the vehicle

Mapping these expressed requirements across the available product categories shows that no one product meets all investors' needs. Whilst UK listed property companies offer many of the desired features, together with a wide range of choice, investment in property company shares is not a good proxy for the underlying property assets and there is tax leakage from the vehicle. At the other end of the scale, offshore unit trusts are a better proxy for the underlying assets and have minimal tax leakage, but are neither domiciled nor listed/authorised in the UK. Moreover, there are few products that have investment minimum below £25,000 and often this is at the discretion of the manager.

The table below shows the main investment vehicles available to smaller individual investors, excluding unit linked pension funds. On the above 6 criteria, we have attempted to score each product as to how well it meets the needs of this group of investors.

Table 1: **Meeting the needs of individual investors**

	Small min investment	Liquid	Low dealing costs	Listed or Authorised	Onshore	Proxy for direct	Low tax leakage	No of products
UK property co	✔	✔	✔	✔	✔	✗	✗	50+
Investment trust	✔	✔	✔	✔	✔	✗	✗	1
Authorised unit trust	✔	✔	-	✔	-	-	✗	3
Unit linked life fund	✔	✗	✗	✔	✔	✔	✔	<20
Listed offshore property company	✔	-	✔	✔	✗	-	✔	<10
Offshore variable capital company	✔	-	✔	✔	✗	-	✔	1
Offshore unit trust	-	-	✗	✗	✗	✔	✔	<10

Key: ✔ = positive; - = neutral; ✗ = negative

The factor that has not been addressed in the above table is that of risk or volatility. Smaller individual investors tend to invest in packaged products rather than individual shares directly. Feedback from financial advisers suggests that individual investors are concerned about the pricing basis of any investment. Thus there is concern that the price of a listed property investment may be quite volatile, reflecting market sentiment rather than only the value of the underlying property assets.

1. Summary

Property companies rate highly on five of the six criteria but they are not great proxies for a direct investment in property because of the volatility of the share prices, which empirically are found to be more highly correlated with the equity market than direct property.

Conclusion

The property market has enjoyed a remarkable period of good returns and this, together with the unpleasant experience of investing in equities, has created a climate in which providers have been able to create and launch new products. But the existing constraints make product development difficult. Most of the new products that have emerged are unauthorised and therefore unavailable to the general public. Some of the existing investors in property funds would welcome access to a simpler product but many more potential investors, who do not currently invest, would be attracted to property investment if there was a simple product that could be marketed to them directly.

Summary: Product review and evaluation

- **There is a relatively large number of different structures available for small investors of different categories to gain indirect exposure to commercial property.**
- **But there is often limited choice within each category and some types of investors are excluded from investing due to their tax status, or by the minimum investment amount.**
- **Small pension funds and charities have the widest range of product categories that meet their needs.**
- **Sophisticated investors are currently much better served in terms of available products than those with smaller sums to invest.**
- **Individual investors who have both a lower appetite for risk and less than £25,000 to invest have a limited range of products to choose from currently and no one product fully meets their needs.**

2. Introduction

This report provides a description of each of the main types of fund structure used for commercial property investments targeted at smaller investors. For each fund type, the key features are given and an analysis is provided of the main advantages and disadvantages. Products are analysed according to the following key criteria:

- Marketability
- Accessibility
- Liquidity
- Pricing mechanism
- Flexibility
- Tax treatment

Marketability refers to the legal and regulatory requirements for marketing the product. A product's accessibility refers to the minimum investment threshold. Liquidity means the ease with which it is possible to sell the investment at a reasonable price. The pricing mechanism is the way in which a product is priced, which may be based directly on property valuations or may be subject to wider market influences. Flexibility refers to the requirements, if any, on the investments that may be held in the fund and the gearing that may be used. Finally, tax treatment covers both how tax is levied on the income flows within the vehicle and on the returns to the investor.

After the factual information for each product structure, there is a brief analysis of the advantages and disadvantages of the structure. This analysis includes the feedback received from product providers during interviews with them.

The following product types are analysed in this report:

- Authorised unit trust
- Unauthorised unit trust
- Unit linked life and pension funds
- Pooled pension fund
- Pension fund pooling scheme
- Common investment fund
- Investment trust
- UK domiciled and listed company
- Offshore domiciled and UK listed company
- UK Limited partnership
- Offshore limited partnership
- Variable capital investment company

3. Authorised unit trust

Following the introduction of a more flexible regulatory regime in April 2004, an authorised property unit trust can invest up to 100% of its assets in direct property and the manager is entitled to defer redemptions by up to six months. The previous rules required immediate redemption of units, so property unit trusts tended to hold higher levels of cash than most other unit trusts. Also, the funds can invest up to 20% of their assets in unregulated collective investment schemes, such as limited partnerships or unauthorised unit trusts.

Until the launch of the SWIP Property Trust in November 2004, there were only three authorised unit trusts. These were: New Star Property Unit Trust, Norwich Property Trust and Morley High Income Property Unit Trust 1 1

Marketability

An authorised unit trust may be marketed to the general public.

Accessibility

Small minimum investments. Fund is obliged to be open continuously.

Liquidity

Daily dealing. There will be a bid offer spread on the units, reflecting an initial charge of 5% typically.

Pricing mechanism

Based on NAV.

Flexibility

Flexibility has been limited hitherto by the need to hold 20% in liquid assets to facilitate redemptions. Gearing is allowed up to 10%.

Tax treatment

- The sale of units in a UK authorised unit trust is subject to capital gains tax with non-business asset taper relief available.
- Unit holders are taxed on distributions from the unit trust in the same way as a dividend from a company (i.e. a rate of 32.5% reduced to an effective rate of 25% by a 10% tax credit.)
- The unit trust itself is exempt from tax on capital gains but is subject to corporation tax at a special rate of 20% on its income profits (after deducting allowable expenses).
- Transfer of units is potentially subject to stamp duty (SDRT) at up to 0.5%.
- The sale of units in an authorised (and unauthorised) unit trust is exempt from VAT.

Analysis

The small number of authorised property unit trusts provides a strong statement as to the attractions of the structure from a provider's perspective. The regulatory framework that prevailed until April 2004 for authorised funds did not suit property investment. The need to provide daily dealing and the high liquidity holdings necessary to accommodate possible redemptions generated a considerable additional management challenge.

Several providers mentioned the introduction of a more flexible framework for authorised property funds following the implementation of a new rule book as a result of proposals put forward in CP 185. Despite the increased flexibility, we found little enthusiasm for launching new authorised funds in the near term. The main issues raised were:

- Ability to defer dealing only to next dealing day - this is not long enough
- Uncertainty around tax position and relationship to possible PIF

Unit trusts and OEICs are popular and familiar investment vehicles. For many smaller investors, in a wide variety of circumstances an authorised unit trust or OEIC is the most suitable investment vehicle. However, the lack of authorised unit trusts investing in property vividly demonstrates the lack of appeal from a product provider's perspective.

4. Unauthorised unit trust

Basics

Unauthorised property unit trusts exist predominantly to provide an efficient investment conduit for institutional investors. Some have tax-exempt status and are accessible only by gross investors (see next category description). Unauthorised unit trusts are usually based offshore, typically in the Channel Islands, to provide tax efficiency for investors. Some funds are open to individuals with sufficient money to invest.

Some unauthorised property unit trusts are open-ended, meaning that they are open to new investment on a regular basis, e.g. monthly. The unit trust structure can also be used to create closed-ended structures, i.e. where the promoter invites investment only at the launch of the fund and investment into the fund is not possible subsequently.

Marketability

Cannot be marketed directly to the general public.

Accessibility

Typically have high minimum investment thresholds, e.g. £25,000. Manager may decline to create units, i.e. allow new investment.

Liquidity

Fund will have specified dealing dates when units can be created and redeemed. Managers typically provide best efforts service to place units with other investors rather than redeem them. There is some secondary market activity by small number of investment banks. Costs of investing in property (e.g. 5.75%) will usually be reflected in the price of new units.

Pricing mechanism

Based on NAV.

Flexibility

Very flexible. Channel Island regulators fairly accommodating in terms of fund objectives, subject to competence of manager and suitable marketing restrictions.

4. Unauthorised unit trust

Tax treatment

- For unit holders the tax consequences are the same as for the Authorised unit trust, although this is not the case for the unit trust itself.
- The unit trust is taxable at 22% on gross income and, unless it falls within stated exemptions, is chargeable to capital gains tax on capital gains. Most expenses are not deductible in computing taxable income.
- As a result, the key difference between an Authorised and Unauthorised unit trust is the level of tax leakage in the vehicle itself, which affects the amounts available for distribution to unit holders.

Analysis

It's not attractive to run an onshore unauthorised unit trust unless the fund is specifically for exempt investors. If the fund is not for exempt investors, the fund faces capital gains tax. Consequently funds that are not exempt have migrated offshore, e.g. Merrill Lynch Property Fund was an unauthorised unit trust up to 31st January 2002 and became a Jersey Unit Trust from 1st February 2002.

Offshore unit trusts have become an accepted structure in the UK amongst institutional investors, although there are still some investors who have concerns about investing offshore. The process for getting a fund launched that is based in, say, the Channel Islands, is fairly quick and incurs moderate fees.

Offshore unit trust structures are attractive for managers because although they are open ended, managers are able to impose dealing restrictions to cope with unusually high cashflows, which would otherwise cause management difficulties. In an authorised fund, the manager would not have this discretion. The main disadvantage of such a fund is that the management has to take place offshore – it cannot be set up simply as 'rubber stamp' type operation, otherwise the fund's offshore status risks attack from the Inland Revenue.

In our interviews with advisers, a lack of information on unauthorised unit trusts was mentioned several times as an issue and barrier to investing. Transaction costs were also cited as a disincentive to invest. In this case, commentators were referring to the costs associated with the underlying property assets, rather than the fund related costs. Investors want to buy units on the secondary market rather than new units, which would attract stamp duty, but cannot necessarily buy what they want.

5. Unauthorised exempt unit trust

Basics

An exempt unit trust is an unauthorised unit trusts restricted to tax-exempt (gross) investors. Because it is restricted to gross investors, there is no need to domicile the fund offshore.

Marketability

Only marketable to gross investors.

Accessibility

Only accessible by gross investors.

Liquidity

Fund will have specified dealing dates when units can be created and redeemed. Managers typically provide best efforts service to place units with other investors rather than redeem them. There is some secondary market activity by small number of investment banks. Costs of investing in property (e.g. 5.75%) will usually be reflected in the price of new units.

Pricing mechanism

Based on NAV.

Flexibility

Wide flexibility for manager.

Tax treatment

- Fund income is subject to tax within the fund but this is reclaimable by gross investors.
- No capital gains tax payable if fund is restricted to gross investors.

Analysis

The comments above for unauthorised unit trusts also apply to exempt unauthorised unit trusts, which work satisfactorily for exempt investors. Main issues that were mentioned in interviews concerned the costs of trading, which reflect the transactions costs of the underlying assets, and the availability of units on the secondary market.

6. Unit linked life fund

Basics

Unit-linked life funds are accessible to individuals through either lump sum investment ('bonds') or regular savings products. The vast majority is lump sum investment. From the investor's perspective, unit-linked funds operate in a similar way to unit trusts although the legal structure is different. With unit linked funds the investor has a contract with the life insurance company, the value of which is linked to the underlying assets of the fund.

Because of the longer-term nature of these products, the funds are able to operate with less of their assets in cash compared to authorised unit trusts. However, the size of the funds varies considerably and even though some companies that have large property management teams, as a result of large property investments in their long-term business funds, have quite small unit-linked funds. The size of the fund is an important consideration because of the difficulty in achieving adequate diversification in a smaller fund.

Marketability

Life products are marketable to the general public.

Accessibility

Available to any private investor, subject to minimum investment levels set by the company. Owing to the intended medium to long term nature of any life bond investment, very small investments would not be acceptable.

Liquidity

Subject to the life company's terms and conditions, the units are liquid. However, the life insurance status of the product will inevitably result in penalties for early redemption. Manager may also impose restrictions on the creation and redemption of units in certain circumstances in order to manage extreme cashflows. Initial investment will attract initial charges, e.g. 5%.

Pricing mechanism

Based on NAV.

6. Unit linked life fund

Flexibility

Unit linked life funds have reasonable flexibility in terms of investment in direct property, although there are severe restrictions on holdings through some types of other collective vehicles.

Tax treatment

- The investor in a life insurance investment product (a 'bond') can generally withdraw 5% of his initial investment in the bond annually without any immediate charge to tax. This is only a deferral of tax as any intermediate withdrawals are taken into account when calculating the gain on the ultimate surrender of the policy.
- No stamp duty arises on issue or surrender for cash. Stamp duty can arise in other situations.
- No VAT should apply to the bond.

Analysis

Unit linked funds are well established and a known product type. However, unit linked life funds are a life product and therefore only suitable in certain situations. Investors for whom a life product is not suitable or desirable have no access to property through this structure. Also, they are long term products and will typically have hefty penalties for early redemption.

From a product provider's perspective, they carry hefty costs in terms of distribution. The open-ended nature also means that large cash inflows, as have been experienced recently, make management of the fund difficult both in terms of investing the cash and in making sure that existing investors are not unfairly diluted.

7. Unit linked pension fund

Basics

Unit-linked pension funds are accessible to individuals through either lump sum or regular savings pension contracts. From the investor's perspective, unit-linked funds operate in a similar way to unit trusts although the legal structure is different. With unit linked funds the investor has a contract with the life insurance company, the value of which is linked to the underlying assets of the fund.

Because of the longer-term nature of these products, the funds are able to operate with less of their assets in cash compared to authorised unit trusts. However, the size of the funds varies considerably and even though some companies that have large property management teams, as a result of large property investments in their long-term business funds, have quite small unit-linked funds. The size of the fund is an important consideration because of the difficulty in achieving adequate diversification in a smaller fund.

Marketability

Life products are marketable to the general public.

Accessibility

Available to any private investor, subject to minimum investment levels set by the company. Owing to the intended medium to long term nature of any life bond investment, very small investments would not be acceptable.

Liquidity

Subject to the life company's terms and conditions, the units are liquid. The investor would be able to sell the units, although because the funds are part of a pension savings scheme, the money would have to be re-invested in another fund. Managers may also impose restrictions on the creation and redemption of units in certain circumstances in order to manage extreme cashflows. Initial investment will normally attract an initial charge of the order of 5%.

Pricing mechanism

Based on NAV.

Flexibility

Unit linked life funds have reasonable flexibility in terms of investment in direct property, although there are severe restrictions on holdings through some types of other collective vehicles.

7. Unit linked pension fund

Tax treatment

Gross fund. No tax on income or capital gains, either within the fund or in the hands of the investor, who can normally only take the benefits as a pension.

Analysis

Unit linked funds are well established and a known product type. Unit linked pension funds are necessarily long term funds and the investor cannot access the investment until retirement when the most of the funds are used to purchase an annuity. These funds are restricted to those individuals who have a pension contract with the life company that runs them, i.e. you can't invest in them through another life company's pension contract.

8. Pooled pension fund

Basics

A pooled pension fund is the name commonly given to a fund set up to accommodate collective investment by pension funds. There is no such thing as a legal structure called a pooled pension fund. The legal structure may vary, but many are unauthorised unit trusts.

Marketability

Marketable to pension funds and their advisers.

Accessibility

Accessible only by pension funds.

Liquidity

Fund will have specified dealing dates when units can be created and redeemed. Managers typically provide best efforts service to place units with other investors rather than redeem them. There is some secondary market activity by small number of investment banks. Creation of units is likely to attract a charge to reflect the underlying property acquisition costs.

Pricing mechanism

Based on NAV.

Flexibility

The manager’s investment flexibility will be determined by the fund’s objectives but these should normally provide good investment flexibility.

Tax treatment

If constituted as a unit trust, fund income is subject to tax within the fund but this is reclaimable by gross investors.

Analysis

Pooled pension funds are successful products, which can take several legal forms, e.g. unauthorised unit trust. There are few disadvantages for eligible investors, other than perhaps costs. For product providers, they can be expensive to distribute, relying on traditional life company channels.

There is no stamp duty on secondary market transactions, which makes this a preferred way of investing but this, of course, relies upon the existence of a seller at the time of planned investment.

9. Pension funds pooling scheme

Basics

A pension funds pooling scheme is a particular type of unauthorised unit trust that is excepted from the definition of unit trust scheme given by section 99(2)(a) of the Taxation of Chargeable Gains Act 1992. It was introduced by the Government to facilitate the management of pension assets of companies with pension schemes for employees in multiple countries.

Marketability

Only marketable to pension funds.

Accessibility

Only marketable to pension funds.

Liquidity

No guaranteed liquidity. Fund will have specified dealing dates when units can be created and redeemed. Manager may provide best efforts service to place units with other investors rather than redeem them.

Pricing mechanism

Based on NAV.

Flexibility

The manager's investment flexibility will be determined by the fund's objectives but these should normally provide good investment flexibility.

Tax treatment

Because the fund is constituted as a unit trust, fund income is subject to tax within the fund but this is reclaimable by gross investors.

Analysis

Used infrequently at the moment. Notably used by ING for a new fund of funds scheme because it allows pension funds to transfer in existing unit holdings of other funds without triggering stamp duty payment.

As with other pension fund vehicles, it is only accessible to eligible investors.

10. Common Investment Fund

Basics

A common investment fund is a open ended pooled fund similar to a unit trust but is constituted under the Charities Act 1993. The key benefit is that charities are exempt from stamp duty as well as other taxes, unlike a pension fund which is not exempt from stamp duty. Investing in a common investment fund is the only way for a charity to retain this stamp duty exemption within a pooled fund.

Marketability

Funds are only marketable to charities.

Accessibility

Funds are only available to Charities. Minimum investment depends on fund objectives, which are set by the Manager, typically £25,000 for an initial investment, with no minimum threshold for additional investments.

Liquidity

A CIF is likely to have similar liquidity to an unauthorised unit trust. The fund will have specified dealing dates when units can be created and redeemed. Managers typically provide best efforts service to place units with other investors rather than redeem them. Costs of investing in property (e.g. 1.75%) may be reflected in the price of new units.

Pricing mechanism

Based on NAV.

Flexibility

Investment flexibility is determined by the fund's investment objectives, which are likely to be fairly conservative given the nature of the investors.

Tax treatment

Exempt from income and capital gains tax and from stamp duty. Distributions are paid gross.

Analysis

A CIF offers unique stamp duty saving benefits for charity investors who do not want to or cannot afford to own property directly. The structure works well for charities but is obviously inaccessible to any other type of investor.

Approval for launch of a CIF is given by the Charities Commissioner rather than the FSA.

11. Investment trust

Basics

A UK investment trust is an investment company listed on the Stock Exchange that is approved by the Inland Revenue. Approval means that the investment trust enjoys exemption from tax on capital gains. The rules require that the trust derive its income mainly from securities or from eligible property. However, in this case eligible property refers to let dwelling houses. In view of the restrictions on the source of income, investment trusts are not ideally suited as vehicles for investment in direct property.

There is one investment trust that holds a mixture of property company shares and direct property and that is TR Property Investment Trust PLC.

Marketability

Marketable to private investors, subject to normal FSA regulations.

Accessibility

Small minimum investment.

Liquidity

Traded on the UK stock exchange, and therefore very liquid compared to most other structures.

Pricing mechanism

As with other investment trusts, the shares can trade at a discount to the net asset value and, like listed property companies, the shares are more volatile than a direct investment in property.

Flexibility

Because of restrictions described above, this structure is not well suited to commercial property.

11. Investment trust

Tax treatment

- Disposal of a share in the Investment Trust is subject to capital gains tax with non-business asset taper relief available.
- Distributions from the Investment Trust are taxable as dividends i.e. at an effective rate of 25%.
- The Investment trust itself is charged to corporation tax on income at up to 30% but is exempt from tax on capital gains.
- Stamp duty applies at 0.5% on acquisition of the shares. No VAT should apply to the shares.

Analysis

Not surprisingly, this structure was not mentioned during product provider interviews. It is not suited to property investment, as currently construed.

Investment trusts are special purpose investment companies that offer investors many of the benefits in equity investing that a PIF could offer investors wanting to invest in property. Yet, investment trusts are not nearly as popular as unit trusts. One possible explanation is the additional volatility and pricing uncertainty that arises as a result of the vehicle being listed. Whether a similar assessment would be made about a new type of property investment trust is unknown. However, this has not been the case with the small number of offshore property investment trusts that have been launched. In fact these have traded at or above NAV for most of the time since launch.

12. UK domiciled and listed company

Basics

A property company is simply an ordinary UK company that specialises in property. Property companies suffer corporation tax on the rental income of their properties. Tax exempt investors cannot reclaim the tax paid. This is one of the reasons why institutional pension funds often prefer to invest in commercial property through buying property directly or investing in limited partnerships that are tax transparent funds that invest directly.

Marketability

Marketable to private investors, subject to normal FSA regulations.

Accessibility

Small minimum investment.

Liquidity

Traded on the UK stock exchange, and therefore very liquid compared to most other structures.

Pricing mechanism

Market based and therefore can diverge significantly from NAV.

Flexibility

Property companies have the advantage of being able to borrow money and therefore an investment in the equity of a property company is almost inevitably a geared investment. Also property company shares may offer access to specialist skills or sectors of the market. Despite these benefits, the number of quoted property companies, and the total capitalisation of the sector, has decreased and that trend is likely to continue.

Tax treatment

- A disposal of shares in the company should be subject to capital gains tax with non-business asset taper relief available. If the individual works for the company and various other conditions are met, the more favourable business asset taper relief may apply.
- Dividends are taxed at an effective rate of 25%.
- The company itself will be subject to tax on income and capital gains at 30%. Certain small and medium sized companies may benefit from lower rates.
- Tax exempt investors cannot reclaim the tax paid.
- Stamp duty applies at 0.5% on acquisition of the shares. No VAT should apply to the shares.

Analysis

The research project did not incorporate any direct assessment of property companies or interviews with their managers.

13. Offshore domiciled and UK listed company

Basics

Other legal jurisdictions offer the possibility of creating specialist investment companies that may be sold to UK investors. If the company is listed on recognised investment exchange (as defined by the FSA's rules), then it may sold to private investors. Typically, product providers form companies based in the Channel Islands, the Isle of Man and Ireland.

Often product providers will also obtain a UK stock market listing for such a company. This confers the benefit of greater comfort from the investor's perspective because of the UK market's listing requirements, and also should lead to greater liquidity. Securities so created are eligible for inclusion in ISAs.

Under current legislation, this is the only viable route to create an investment vehicle that is listed and that is highly tax-efficient.

Marketability

Marketable to private investors, subject to normal FSA regulations.

Accessibility

Initial investment may be set at a minimum level of a few thousand pounds, but secondary market transactions can be of even lower size.

Liquidity

The shares are traded on the UK stock exchange, and therefore very liquid compared to most other structures. How frequently the shares trade will depend on the level of interest shown by investors and market-makers.

Pricing mechanism

Market based and therefore can diverge significantly from NAV.

Flexibility

A UK listed property company is subject to the UK listing rules, which include minimum levels of diversification in terms of number of properties and exposure to tenant credit risk. Gearing is allowed up to 65%. However, the biggest management issue is that the fund must be properly managed offshore, and not just have decisions rubber stamped offshore.

13. Offshore domiciled and UK listed company

Tax treatment

- A disposal of shares in the company will be subject to capital gains tax, generally with non-business asset taper relief available.
- Dividend income will be taxable at 32.5%. A credit for tax suffered by the company in the overseas jurisdiction may be available depending on the terms of any double tax treaty in place. This assumes that the income within the company is not subject to income tax on the shareholder as it arises, under UK anti avoidance legislation.
- If the company is non-UK resident, it should not be subject to tax on capital gains on UK property provided it is a property "investor" rather than a "dealer" The company will be subject to UK income tax at 22% on rents (less allowable expenses) arising from UK properties. Other tax consequences may arise in the jurisdiction of residence.
- Anti-avoidance rules can apply to impute capital gains of the company to UK resident and domiciled shareholders if they have an interest in the company of more than 10% and if the company is controlled by 5 or fewer participants. These rules are complex and are designed to prevent individuals from realising profits free from tax by owning the assets in a corporate wrapper in a tax haven jurisdiction.
- Purchase of the shares is not subject to stamp duty unless the shares are registered in the UK.
- No VAT should apply to the shares.

Analysis

The key attraction of these structures is that it is possible to construct them so that the amount of tax paid within the vehicle is very low. This means it is possible to distribute a high gross income to investors in the form of dividends. In this way, investors are able to invest in property in listed form and get a dividend that is a substantial proportion of the underlying rental income. This type of structure is the nearest thing that currently exists to a listed PIF.

The funds that have been launched in this form have proved popular with investors. However, there are some difficulties in creating and managing these structures. First, the deals typically require readily accessible portfolios of property that attract low or no stamp duty on acquisition. If full costs were paid then the net asset value of the shares immediately after launch would be unacceptably low in the eyes of equity investors. Over time, this may change as understanding of property in the wider investment community increases. However, in the near term it means that the supply of new vehicles of this nature is likely to be very limited.

Operationally these structures also face some challenges. The companies have to be managed offshore and the low tax payable by the company relies upon inter-company loans from the parent to offshore subsidiaries. It is possible that these loan arrangements could be challenged by the Revenue if perceived as too aggressive, which could result in a higher tax charge.

In summary, these vehicles are popular but are not a viable long term substitute for a listed PIF type structure.

14. UK Limited partnership

Basics

Limited partnerships are popular vehicles for co-ownership of property because they offer tax transparency. This means that the investor in the limited partnership is treated as if he owned his share of the assets and liabilities directly. They are not tax-saving schemes.

Marketability

Limited partnerships are unregulated collective investment schemes and therefore may only be marketed to investment professionals and certain other high net worth companies, trusts and associations. In practice, products are marketed to IFAs. They may not be marketed to the general public.

Accessibility

Minimum investment levels are usually set at £25-50,000, although this is at the discretion of the product promoter.

Liquidity

There is not normally any liquidity in partnership interests. It may be possible to sell an interest before the planned wind up date but most promoters will endeavour to accommodate only on a best efforts basis.

Pricing mechanism

There is no set mechanism for pricing of a share prior to planned wind up, although it would likely be based upon NAV. However, lack of buying interest may result in a low price. Price on wind-up is based on NAV.

Flexibility

Limited partnerships are very flexible structure for the manager. High levels of gearing are possible and there are no specific regulations regarding the nature of the underlying assets, which may be a single building.

14. UK Limited partnership

Tax treatment

- The partnership agreement will determine a partner's entitlement to income and capital gains from the partnership. This will be taxed on the individual as though it were a direct investment in that share of the partnership assets.
- The partnership itself should be transparent for tax purposes so there should be no incidence of tax in the vehicle itself.
- Stamp duty at up to 4% can apply to the acquisition of a partnership share, although this would not normally affect an investor in a new fund.
- Following the introduction of Stamp Duty Land Tax, stamp duty may be charged on the sale on a partnership interest on the full underlying property value at up to 4%, even if the partnership is geared.
- The VAT treatment of the transfer of an interest in a partnership that owns property is not straight forward and will depend on the circumstances.

Analysis

Limited partnerships have been extremely popular as structures for co-ownership of property in recent years. In tax terms, the great benefit is that LPs are tax transparent. LPs are generally set up as closed ended structures, and normally will have a planned wind up date. In general, there is no liquidity in the partnership interests. LPs are not well suited for funds where there is expected to be changes in the investor base. This is because e.g. the redemption of one partner's interests creates a taxable event for all members of the partnership. Consequently, LPs are most commonly used in situations where the investor base is expected to remain constant.

The introduction of SDLT results in a tax disadvantage for LPs. On transfer of a partnership interest, stamp duty is payable on the full value of the partner's interest in the underlying property. Where the investment is geared, as is often the case, then stamp duty is chargeable on the ungeared value. Hence a partnership interest in a property financed 50% by equity and 50% by debt would attract stamp duty equivalent to 8% of the equity value. Whilst LPs are not set up with the intention of being traded, this situation is likely to diminish their appeal as suitable structures for property ownership.

15. Offshore limited partnership

Basics

An "offshore fund" is a term that can be used to describe many different types of offshore vehicle. Offshore property funds are often created as offshore limited partnerships ('LPs') if the unit trust structure is unsuitable for purpose. The issues for offshore LPs are similar to onshore LPs, with the added complication that control has to be exercised offshore.

Marketability

As with onshore LPs, offshore limited partnerships are unregulated collective investment schemes and therefore may only be marketed to investment professionals and certain other high net worth companies, trusts and associations. In practice, products are marketed to IFAs. They may not be marketed to the general public.

Accessibility

Minimum investment levels are usually set at £25-50,000, although this is at the discretion of the product promoter.

Liquidity

There is not normally any liquidity in partnership interests. It may be possible to sell an interest before the planned wind up date but most promoters will endeavour to accommodate only on a best efforts basis.

Pricing mechanism

There is no set mechanism for pricing of a share prior to planned wind up, although it would likely be based upon NAV. However, lack of buying interest may result in a low price. Price on wind-up is based on NAV.

Flexibility

Limited partnerships are very flexible structure for the manager. High levels of gearing are possible and there are no specific regulations regarding the nature of the underlying assets, which may be a single building.

15. Offshore limited partnership

Tax treatment

- The partnership agreement will determine a partner's entitlement to income and capital gains from the partnership. This will be taxed on the individual as though it were a direct investment in that share of the partnership assets.
- The partnership itself should be transparent for tax purposes so there should be no incidence of tax in the vehicle itself.
- Stamp duty at up to 4% can apply to the acquisition of a partnership share, although this would not normally affect an investor in a new fund.
- Following the introduction of Stamp Duty Land Tax, stamp duty may be charged on the sale on a partnership interest on the full underlying property value at up to 4%, even if the partnership is geared.
- The VAT treatment of the transfer of an interest in a partnership that owns property is not straight forward and will depend on the circumstances.

Analysis

The issues for offshore LPs are similar to onshore LPs, with the added complication that control has to be exercised offshore.

16. Closed ended investment company with variable capital incorporated in Ireland

Basics

A closed ended investment company with variable capital is a particular type of company authorised under Part XIII of the Companies Act, 1990. Such a company is an attractive structure for some funds because of the flexibility possible within the investment objectives and the appeal of Irish domicile. Many (general) investment funds have been set up within this framework.

The first property vehicle using this structure was launched by Strutt & Parker Real Estate Financial Services Ltd. Whilst this report address questions about the merits of various structures in general terms, this section refers extensively to the SPREFS fund because it is the only one in the market.

Marketability

Because the vehicle is a company listed on an approved exchange, the fund may be marketed to private individuals.

Accessibility

In the case of SPREFS, there is a minimum of £15,000 outside of an ISA, and £3,000 if within an ISA.

Liquidity

In the case of the SPREFS fund, a market maker has been appointed, although there is no guarantee that there will be a market price or what it will be. The company also has set up a discretionary facility to repurchase shares once a year, together with a firm commitment to provide a repurchase facility in 2008, 4 years after launch. This should provide a backstop to the market price of the shares relative to the underlying NAV and make it easier for the market maker to price the shares.

Pricing mechanism

Based on NAV of the underlying assets.

Flexibility

Investment flexibility will be determined by the articles of the company and the restrictions contained in the relevant Act under which the company was formed. However, these allow a wide range of investment approaches, although not high risk strategies that, for example, use high gearing.

16. Closed ended investment company with variable capital incorporated in Ireland

Tax treatment (for UK investors)

- Investors are liable for income tax or corporation tax, as applicable, in respect of dividends received from the fund.
- Because the fund is not for tax purposes a collective investment scheme, gains on disposal should normally be treated as capital gains.
- Although the underlying fund is obliged to deduct tax on distributions, these are reclaimed by the entity holding the units.

Analysis

The structure provides a vehicle that has many attractive features for the smaller investor. It is a hybrid structure that is available in small lot size, is likely to have some secondary market liquidity and gives access to a broadly diversified portfolio of property assets. These points are, in part, a result of the particular structure chosen by SPREFS but its fund does demonstrate what is possible.

However, the structure was not easy to create and involved working with three different regulatory bodies. Furthermore, the tax efficiency of the structure again relies upon the use of inter-company loans to generate an interest charge in the subsidiary company that owns the underlying assets that largely offsets the rental income.

Working Paper Six

Findings and Recommendations

To be supplied

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1. Key Findings, Conclusions and Recommendations

Anecdotal evidence suggests that individuals investing for the future are a growing segment of commercial property investors, but until now little data and information has been available in the public domain about this highly fragmented group. Similarly, our knowledge of small pension funds and charities is partial. As a consequence, there has been no real understanding about the needs of these smaller investors, making it difficult to assess their likely appetite for indirect investment products and, in particular, any new tax transparent securitised product.

Brief

In February 2004, a research team from Seven Dials Consulting, Oxford Property Consultants and Experian Business Strategies was commissioned by the three leading property industry bodies (IPF, BPF and RICS) to begin to address these issues. The principal objectives of the research project were:

- To quantify the current value of this market, and identify trends in the proportion of funds allocated to property and other assets.
- To gather information on the investment strategies of smaller investors, their objectives and, where appropriate, the liabilities they are seeking to match.
- To identify the perceived advantages and disadvantages of investing in commercial property, from the perspectives of the smaller investor.
- To provide insights about the level of knowledge and understanding of commercial property investment amongst smaller investors, and their advisers.
- To review and evaluate the range of commercial property investment products currently available to smaller pension funds, charities, and private individuals. In particular, assess the extent to which existing vehicles meet their needs.
- To assess the potential depth and value of the market for new tax transparent securitised vehicles.

1. Key Findings, Conclusions and Recommendations

Undertaken over four months and divided into seven inter-related workstreams, this study comprised a combination of desk-based analysis, structured interviews, focus groups and survey research. It has taken into consideration the different perspectives of individual investors and their advisers, small pension funds/charities and their advisers, and product providers.

The key findings and conclusions of this research are set out on the following pages. In light of these findings, conclusions are then drawn and recommendations are made with specific reference to the implications for proposals for Property Investment Funds (PIFs).

Key Messages

- **Small investors have an estimated £35bn of capital for property investment, but have limited knowledge of, or access to, the market.**
- **With at least 6.5m active individual investors and more than 200,000 pension funds, the small investor universe is significant.**
- **The value of assets that these investors have at their disposal exceeds £730bn, but only relatively small sums are held indirectly in commercial property.**
- **Existing indirect investment products do not meet the needs of small investors in commercial property, and for some, product choice is limited. Suitable new products are often complex and costly to manufacture.**
- **Individual investors with smaller sums to invest want a liquid vehicle that offers investor protection, stability and exposure to direct property returns. A simple product that could be marketed directly and which could be held in an ISA, and other "product wrappers", would be well received by these investors.**
- **Sophisticated investors with larger sums to invest, a better understanding of financial products and greater appetite for risk have a greater preference for unlisted vehicles that are a better proxy for direct investment.**
- **Small pension funds and charities are seeking indirect routes into the asset class. Unlisted products are more likely to appeal to these smaller institutions because they are diversifying their portfolios and shifting their asset allocations away from listed equities.**

1. Key Findings, Conclusions and Recommendations

Key Findings

- **The number of small investors is significant. Small investors are defined as active individual investors, who own holdings in shares (other than via mutualisation or privatisation), unit trusts, OEICs, or investment trusts together with small pension fund and charities that have total assets of less than £30m.**
  - There are at least 6.5m active individual investors in the UK, who on average own 1.9 investment products.
  - Some 98% of all occupational pension schemes (98,700 schemes) have total assets of less than £30m. These schemes have exceeding 2.5m members.
  - More than 70% (72,400) of occupational pension schemes are money purchase schemes, where almost 1m individuals have some discretion over the choice of assets. Fewer than 300 of these schemes have total assets greater than £30m.
  - There are circa 102,000 self-invested pension plans in operation. Most, if not all, of these plans may be expected to hold total assets of less than £30m.
  - There are circa 163,000 registered charities. Available data indicates 65% of these charities have total assets of less than £30m.

- **The value of the assets owned by small investors is substantial.**
  - Active individual investors own assets in excess of £654bn.
  - Occupational pension schemes with total assets of less than £30m own an estimated £61.1bn of assets.
  - Self-invested pension plans hold some £17.6bn in assets.

- **As an asset class, commercial property has outperformed equities and bonds over three, five and ten years, and in a portfolio context, commercial property acts as a diversifier, but small investors have limited exposure.**
  - Small pension fund investment is predominantly in equities - the weighted average allocation is 66%. Despite being categorised as the highest risk asset class, equities are seen as the primary means of meeting long-term liabilities.
  - However, there have been some structural changes over the last five years with downward adjustment in equities allocations in favour of bonds and respondents indicated that further shifts in this direction are likely. The average allocation to bonds is 28%.
  - Small charities are less heavily exposed to equities (the weighted average allocation is 49%), and the rationale for holding these assets is more to do with income production than matching longer term liabilities. Their investment in bonds is also typically lower than small pension funds at 11% and, at 24%, they typically have large cash holdings.

1. Key Findings, Conclusions and Recommendations

- The average allocation to property by small pension funds and charities is 2% and 15% respectively. The much higher allocation by charities also reflects holdings in 'legacy type' assets and operational property in addition to investment assets.
- Establishing risk preferences is an important first step taken by most advisers in determining an investment strategy for a client. The proportion of equities in the asset mix is the key variable that alters with risk preference. Hence, low risk investors tend to have lower recommended weightings in equities than medium and higher risk investors.
- Financial advisers usually see commercial property as having a role in their clients' investment portfolios. The average recommended allocation for a low risk investor is surprisingly high at 21%, with a range from 10% - 25%, but the allocation to property tends to fall as the weighting in equities rises for investors with higher risk preferences.
- There is widespread awareness of the strong performance record. Some 54% of active investors view commercial property as the top performing asset and a third of active investors say that they are interested in investing.
- However, a significant gap exists between awareness and investment decision-making. Substantial sums have been invested directly by individuals (residential buy-to-let properties amounts to £40bn), but less than 10% of active investors own commercial property investments via indirect means and their allocations amount to less than 4% of the total. Moreover, just 5% of active investors plan to invest in commercial property in the next 12 months.

Table 1: **Summary - Individual Investor Assets**

	Asset Value (end 2003 £bn)	% in Property	Property Asset Value (£bn)
Indirect Property Exposure			
Unit trusts & OEICS, of which	138	0.4%	0.6
- PEPs/ISAs	66		
Unit linked life funds	62	13.0%	8.1
Unit linked pension funds	164	6.0%	9.8
Direct share ownership	239	2.0%*	4.8
Total	603	3.9%	23.3
Direct Property Exposure			
Direct property, of which	51.0	100.0%	51.0
- buy-to-let residential	40.0	100.0%	40.0
- commercial acquired by private treaty	6.3	100.0%	6.3
- commercial acquired by auction	4.7	100.0%	4.7
Total Property Exposure			
Total, including direct property	**654.0**	**11.3%**	**74.2**

Sources: IMA, ABI, ONS, ComPeer, Standard & Poors, Lipper, CML, JLL/IPD, PropertyData
*estimate

1. Key Findings, Conclusions and Recommendations

- **Greater indirect investment in commercial property products by small investors is currently held back by the limitations of the available products:**
  - The existing property investment product structures are inflexible, complex and costly to manufacture.
  - At first sight, there would appear to be a considerable range of products available to meet the needs of small investors in commercial property. However, on closer inspection the choice within each category is often extremely limited. For example, there are currently only three authorised unit trusts that invest in direct property, only two Common Investment Funds and only one investment trust.
  - Illiquidity is perceived to be the principal disadvantage associated with indirect investment in property.
  - The relatively high initial entry costs (fees etc) of acquiring an interest in most property products.
  - Very small investors are excluded from securing indirect access to commercial property because few products meet Inland Revenue regulations for qualifying investment for PEPs and the stocks and shares element of ISAs. Units in both authorised and unauthorised property unit trusts are specifically excluded.
  - The unregulated nature of most property funds means that products cannot be marketed direct to the general public, and also that some advisers are not able to offer these products to their clients, either because they are not permitted to do so by their organisation or they lack the necessary professional indemnity insurance cover to do so.
  - The tax status of some types of investors means they are excluded from investing in certain categories of product.
  - The minimum investment levels excludes individual investors with only modest amounts to invest. The threshold for most unregulated products is £25,000. Some 46% of active investors with no property exposure cited affordability as the principal barrier.

- **There are a range of additional factors that contribute to the low level of take-up:**
  - Individual investors' risk preferences tend to be cautious and property products are perceived by many potential investors to be complex and "too risky".
  - The low level of knowledge and understanding amongst individual investors. Some 11% of active investors with no property exposure say they do not know enough about commercial property to invest or they do not understand about the ways of accessing the market.
  - The general lack of specialist knowledge amongst financial advisers. The number of products being targeted at private investors is growing. But most financial advisers do not have the time or expertise to evaluate these products and advise their clients on their relative merits. The array of products being offered to private investors - whether listed entities or unregulated collective investments - are often complex structures that are not easily understood.
  - Lengthy due diligence and decision-making by both large firms of financial advisers and pension fund trustees restricts their participation in products with limited offer periods.
  - Property and property products are not generally incorporated into the software packages used by many financial advisers to assist them with asset allocation and product selection. To some extent, this reflects the 'alternative' status of commercial property but it also reflects the unlisted character of most vehicles and the associated scarcity of pricing and performance data.

- Small pension funds and charities have the widest range of product categories, which meet their needs and sophisticated investors are currently much better served in terms of available products than those with smaller sums to invest.
- However, as Table 2 shows, individual investors who have both a lower appetite for risk and less than £25,000 to invest have a limited range of products to choose from currently and no one product fully meets their needs.

Table 2: **Meeting the needs of individual investors**

	Small min investment	Liquid	Low dealing costs	Listed or Authorised	Onshore	Proxy for direct	Low tax leakage	No of products
UK property co	✔	✔	✔	✔	✔	✗	✗	50+
Investment trust	✔	✔	✔	✔	✔	✗	✗	1
Authorised unit trust	✔	✔	-	✔	-	-	✗	3
Unit linked life fund	✔	✗	✗	✔	✔	✔	✔	<20
Listed offshore property company	✔	-	✔	✔	✗	-	✔	<10
Offshore variable capital company	✔	-	✔	✔	✗	-	✔	1
Offshore unit trust	-	-	✗	✗	✗	✔	✔	<10

Key: ✔ = positive; - = neutral; ✗ = negative

- Our discussions with product providers indicate that the market is likely to remain supply-constrained and that investors' needs will remain unmet.
  - Most existing product providers are not attracted to the retail investor market, citing absence of suitable distribution channels, greater risk of mis-selling and administrative burden. Furthermore, most existing products have been developed for the institutional market and fee structures reflect this, so there is little scope for the introducers' initial fees associated with retail investors.
  - There is widespread concern amongst product providers that financial advisers and their clients are not fully conversant with the attributes and risks of different property investment products.
  - Authorised products are considered an easier 'sell' for financial advisers because they are seen as being less complicated, but the tax treatment of authorised property unit trusts remains an issue.
  - New offshore listed products are likely to be limited in number due to the practicalities and costs of bringing together portfolios of properties.

1. Key Findings, Conclusions and Recommendations

- For both small investors and product providers there is clear and continuing tension between onshore and offshore commercial property products:
  - From a tax perspective, most of the commercial property products that are acceptable to small investors are domiciled offshore. This applies as much to private individuals as to pension funds. The principal requirement is to ensure tax efficiency within the vehicle (i.e. minimise tax leakage). However, individual investors, in general and perhaps unfairly, prefer onshore vehicles because these are perceived to fall under a more stringent regulatory regime and so carry less risk.
  - For their part, promoters would like vehicles to be onshore as there is considerable cost – in terms of management time, fees and inconvenience - associated with manufacturing offshore domiciled products that are tax efficient and which also meet the differing requirements of investors and regulators in different jurisdictions. Moreover, the majority of offshore vehicles are unregulated collective investment schemes, which constrain the scope for marketing the product.

Conclusions and Recommendations

- There is significant interest in commercial property from individual investors, and smaller pension funds and charities want to invest indirectly in the asset class.

- Indirect investment in property by individuals is relatively small, but if allocations increased from current levels (less than 4% overall) to 10%, the minimum weighting advocated by financial advisers for low risk investors, then the property market would see capital inflows of £35bn. The associated impact would be significant, because this figure equates to 14% of the current size of the commercial investment market.

- However, it appears that private investor exposure to real estate may be supply-constrained and/or limited by the lack of specialist knowledge amongst financial advisers. Hence, the key challenges for the industry lie in the manufacture, marketing and distribution of attractive products that will convert 'performance awareness' into investment action.

- Property investment is perceived to be costly, risky and investing is not understood by individual investors or their advisers. Moreover, small pension funds, charities and their advisers view property as being high risk. Hence, education remains a major issue for the property industry. Without a clear plan, the property industry will fail to attract a significant body of these investors.

- The currently high level of direct investment in property by individual investors, and particularly buy-to-let residential is a cause of concern. Many of these investors are investing for the long term to augment their pensions. However, there is little appreciation of the risks that are being taken on by these inexperienced investors. Too few individuals know about or use professionally managed, diversified property funds as an alternative route into property investment.

- There is currently strong interest in commercial property but small investors are faced with limited choice of indirect property products, particularly those individual investors with relatively small sums to invest. Largely this reflects the inflexibility of existing product structures, and the complexity and cost of manufacturing new products that meet both regulatory requirements and investors' needs. Most new products are unauthorised and cannot be marketed to the general public.

1. Key Findings, Conclusions and Recommendations

The existing framework for authorised funds is cumbersome. Investors need and want a liquid vehicle that offers investor protection, stability and exposure to direct property returns. Hence, a simple product that could be marketed directly and which could be held in an ISA would be well received.

- In other markets, notably Australia and the US, the 'man in the street' invests significant amounts in LPTs, REITs and other liquid and regulated property investment products. It appears that the lack of a similar vehicle in the UK is greatly restricting public access to the asset class.
- There is a difference of view between smaller institutions and private individuals over the relative merits of listed and unlisted indirect property investment products. Listed products are more likely to appeal to individuals; unlisted products are more likely to appeal to smaller institutions.
- Private individuals place great importance over the brand, which is used to promote investment products. More leading brands need to offer property products for the retail market in order to meet demand.
- Financial advisers play a critical role in advising their clients on whether to allocate funds to commercial property and on the suitability of the different commercial property products. Commercial property is only now coming onto their radar screens, so their understanding of the asset class is still in its infancy.
- Evidence from other markets shows that many consumers are not well informed about financial products, and this research has shown this to be the case in relation to commercial property products.
- To achieve wider understanding and take-up of commercial property investment products the following steps should be taken by Government, the property industry and the financial advisory bodies:
    - Develop a co-ordinated programme of education and training, specifically tailored to the needs of small investors. Financial advisers to individual investors expect the product provider community to provide in this area. The need to educate is recognised widely but better communication and commitment is required to ensure better use is made of available resources.
    - Take steps to improve the provision of reliable data that will help small investors to make informed decisions.
    - Improve the availability of performance data on unquoted products. It is clear from other asset markets that performance drives product sales and there is a strong relationship between investment via intermediaries and five-year performance figures.
    - Encourage the development of independent quantitative ratings and analysis in order to make the indirect product market more transparent. There is evidence in other markets of close links between sales through intermediary channels and the availability of third party research and information.
    - Allow the market to develop as it has begun to do without damaging interference. The introduction of a tax efficient PIF in the appropriate form will be a positive impetus.

1. Key Findings, Conclusions and Recommendations

Property Investment Funds

The UK government's consultation document on the introduction of a Property Investment Fund, identifies the need to address the current lack of choice for smaller investors, and the poor liquidity associated with property investment. It also aims to put an investor in the same tax position as if they owned the assets directly, but with the benefit of diversification and professional management.

Few existing products comprehensively meet the expressed needs of individual investors who have both a lower appetite for risk and relatively small sums to invest. The findings of this research provide some pointers for structuring vehicles that would more closely meet the needs of this group, which potentially amounts to 3m people. Preferred products structures are likely to be those with the following characteristics:

- Listed/Authorised
- Onshore
- Minimal gearing
- Small minimum investment
- Low transaction costs
- No/limited tax leakage within the vehicle
- Well known brand

This research has also highlighted the fact that many small pension funds and charities are deterred from investing in property due to the illiquid nature of the asset class, high entry costs and the high-risk profile. A listed PIF would address many of these disadvantages by offering a potentially liquid and low cost way of accessing the asset class. However, there is also evidence of potential demand for unlisted PIFs.

Sophisticated investors have a better understanding of financial products and greater appetite for risk. This group amounts to between 1.8m and 2.1m individuals who may have a greater preference for unlisted vehicles that are a better proxy for direct investment.

Moreover, this research shows there is a strong preference among small pension funds and charities for indirect routes into the asset class. It is possible that a public PIF may meet expressed preferences for listed vehicles, but it is also possible that private PIFs will be attractive to smaller institutional investors. The attraction of private indirect property vehicles is supported by the trend for these investors to diversify their portfolios by shifting asset allocations away from listed equities.

One of the stated objectives of introducing a new PIF is to expand the opportunity for small investors to invest in a wider range of property. This research shows there to be a large number of existing types of indirect investment vehicles. However, in many categories of product, there is currently limited choice.

There are approaching 200,000 small pension schemes and potentially in excess of 100,000 charities with total assets of less than £30m. These organisations are likely to be attracted to tax transparent products with low entry costs, which allow an easier exit than those currently available. In this context, both listed and unlisted PIFs are seen as being beneficial.

1. Key Findings, Conclusions and Recommendations

Further Research

This project is the first systematic study of this topic and has identified many previously unknown issues and key findings. It provides a secure foundation for understanding and meeting the needs of smaller investors in property. To deepen this understanding, inevitably the study has highlighted the opportunities for further research in a number of key areas:

- More information is needed about the exposure of individuals to residential buy-to-let property. The Council of Mortgage Lenders[1] has also recently identified this need and plans to initiate further research, which suggests scope for a jointly funded project with the IPF, BPF and RICS.
- Some private investors have also been investing in commercial property by via limited partnerships, syndicates and other unquoted vehicles. More data is needed on the amounts of money invested by individuals in these products.
- Our estimates of market size require further investigation through an analysis of investors in existing commercial property products. An important step is to confirm the profile of investors and the amount invested by different investors groups. This will allow comparison to be drawn with the work reported here and thereby highlight whether any further analysis merited
- Further survey work is required to provide more detailed insights on the levels of current exposure by individuals to indirect investment in commercial property and on the attractiveness of commercial property investment.
- Building on the market segmentation analysis undertaken will develop our understanding of the risk appetite and investment priorities of the different groups of active investors identified.
- It is clear that there is considerable uncertainty amongst individual investors about how to invest, where to get appropriate information and associated investment risks. Further investigation is required to determine what is required to close the gap between the high awareness of commercial property performance and the decision to invest.
- Comparative studies of international markets would be helpful in comparing the UK situation with other G7 markets.
- Further investigation is required into the information needs of financial advisers, particularly in relation to risk assessment, and the most effective delivery mechanisms.
- The data on the universe of small pension funds and charities requires further investigation.
- Smaller pension funds, charities and their advisers view property as a more risky asset class than is the consensus view among investment professionals. Why is this? Is it a function of the products being marketed, memories of other crashes, the use of gearing or some other factor?

2. Introduction, Brief & Approach

Introduction

This remainder of the report brings together the findings from the seven separate workstreams of the research project commissioned The overall aim of the research was to provide a more detailed understanding of the needs of individual investors, small pension funds and charities. Each work stream examined a particular facet of this issue, relating to the six subsidiary objectives outlined previously.

Approach

The approach adopted was primarily driven by a desire to understand the needs of individuals and the various means by which these individuals save for the future in both pension and non-pension forms. Rather than define small investors in terms of their total investment assets, consideration was given to the circumstances where the risk and responsibility for investment decisions lie with the individual. Hence, the research project has centred on the different perspectives of individuals investors and the role of advisers and fiduciaries in decision-making. Individual investors were defined as those who own shares (other than privatisation shares), equity ISAs, unit trusts, OEICs, investments trusts and/or property.

Table 3: **The role of individuals, advisors and employers in decision-making**

Individuals	Decision maker or influencer		
Savings situation	**Individual**	**Advisor**	**Employer**
Non-pension	✔	✔	✗
Personal pension	✔	✔	✗
Company pension (defined contribution)	✔	✔	✔
Company pension (defined benefit)	✗	✗	✔

In addition, the needs of small pension funds and charities have also been considered. Small pension funds and charities have been defined as those with total assets of less than £30m. These investors are regarded as being a different category of small investor, with risk and decision-making lying with a combination of trustees, employers, fund managers and advisers. Also, a wide range of property investment products is already available to them. However, some of the issues that these investors face are comparable with those encountered by individual investors.

Seven different workstreams have been undertaken to address the aims and objectives of the study. These are outlined below.

1. Market Sizing By Asset Type

Essentially, this was a desk-based exercise that drew together data from disparate sources to determine the quantum of investment by individuals in different types of assets.

2. Individual Investors - profiles and purchasing behaviour

Drawing upon data from 46,000 interviews undertaken by MORI in 2003, the profiles of individual investors were determined and their investment purchasing behaviour was examined. In addition, this analysis enabled preliminary estimates of the potential market size for property investment products to be made.

[1] CML Market Briefing (May 2004)

3. Individual investors - survey research

Three work elements undertaken with each providing insights on the attitudes of individuals to investing in commercial property:

- The findings from a MORI survey of 2,000 individuals undertaken for the BPF were cross referenced with those of the larger MORI survey noted above;
- Two further questions were inserted into MORI's monthly omnibus survey in April 2004;
- Three focus groups were held in early May 2004 to help identify the risk preferences and attitudes of investors.

4. Smaller pension funds and charities

This workstream attempted to quantify the number of small pensions funds and charities with assets of less than £30m. Also, through structured discussions with 41 small pension funds and charities, the research team explored the role of property in investment portfolios, attitudes to indirect commercial property investment, and the relative attractions of different property investment vehicles.

5. Structured interviews - advisers

A combination of structured telephone discussions and face-to-face interviews were conducted with 20 financial advisers and 10 advisers to small pensions funds and charities. These interviews provided insights on the way investment strategies are developed and implemented, the different steps in the strategy formulation process, attitudes to commercial property as an investment, and perceived advantages/disadvantages of different commercial property products.

6. Structured interviews - product providers

There are an increasing number of institutions and other product providers that are targeting small investors with commercial property funds. Interviews were conducted with representatives from 10 organisations, which together covered many of the available product categories. These discussions contributed to the product reviews (see below) by providing insights on the sales process, the barriers encountered in marketing products to different categories of smaller investor, and the attitudes of intermediaries.

7. Product review and evaluation

Small investors are currently gaining access to real estate in a range of different ways - both direct and indirect. This workstream evaluated the full range of indirect property investment vehicles that are currently available to individuals, small pension funds and charities. This evaluation was based upon measures of marketability, accessibility and flexibility, together with the expressed needs of investors and their advisers. As such, this workstream drew upon the findings of several others, notably 3, 4, 5 and 6 above.

The detailed findings from these different workstreams have been brought together in five different reports, which will be available from the IPF:

- **Market Size**
- **Individual Investors and their Attitudes to Investing in Commercial Property**
- **Advisers to Individual Investors, Small Pension Funds and Charities**
- **Pension Funds & Charities**
- **Commercial Property Product Review and Evaluation**

The key findings of the research are set out on the following pages. The key points are summarised at the end of each section.

3. Market Size

The principal aim of this workstream was to estimate the quantum of individual investors and the value of their savings in both pension and non-pension forms, segmented by asset type.

Understanding the activities of individual investors requires assimilation of data from a variety of sources, which inevitably give rise to some overlaps and consequent uncertainty over accuracy. Despite these logistical challenges, we can describe in some detail the activities of UK individual investors in aggregate.

Investors save money in a variety of ways, utilising a range of product types:

- Unit-trusts and OEICs
- Life insurance savings products
- Pensions
- Direct shares
- Direct property
- Cash, including bank and building society deposits

Also, there are pools of money that are not covered by the above categories and where there is little data available. These include money invested offshore, direct private equity and venture capital, money invested in various tax saving schemes, such as film partnerships, and less mainstream investment assets such as art, wine and whisky.

Unit-trusts and OEICs

- There are an estimated 19.3m unit trust accounts, of which 8.3m are ISA accounts and 6.8m are PEP accounts. After adjusting for multiple account holdings, it is estimated that there are around 4.8m unit trust and OEIC investors.
- Net sales of unit trusts and OEICs to retail investors totalled £7.9bn in 2003, up from the previous year by £0.3bn. This is still substantially below net sales to retail investors of £17.7bn in 2000.
- The total value of invested assets owned by private investors is estimated at around £138 bn at 1 Feb 2004. Institutional investors own another £108 bn in unit trusts and OEICs, giving a total value of £246bn, which roughly equates to the size of the commercial property investment market.
- However, only a very small proportion (0.4%) of unit trust assets are property assets, reflecting the very small number of funds available. Over 80% of assets are estimated to be invest in equities.

3. Market Size

Life Products

- Life insurance products remain an important savings medium for many people in the UK. Over 732,000 single premium life insurance investment contracts were sold in 2003. Of these, 384,000 were unit-linked contracts, where the investor has some choice over where the funds are invested. In terms of premium value, £9.2 bn was invested in unit-linked contracts (excluding distribution bonds). Several major life insurers have seen rapid growth in their property funds as a significant amount of this premium income has been targeted at property funds.
- Desktop research indicates that there is approximately £62.4 bn in total invested in unit linked life funds. Around 13% of this is estimated to be in property funds.

Pensions

- Private pension provision is undergoing an important shift as employers move away from defined benefit schemes and take up defined contribution schemes. This analysis only covers assets invested in personal pension or defined contribution schemes, where the individual usually has discretion over the investment of the assets and bears the investment risk.
- Almost 950,000 new regular or single unit-linked premium pension contracts were written in 2003, with a premium value totalling £8.9bn.
- The total value of unit linked pension fund assets is estimated at £164bn, although this figure is subject to significant error owing to the existence of many closed and duplicate funds.
- Approximately 6% is estimated to be invested in property funds. The lower figure as compared to life funds reflects the equity culture that has been so prevalent in the UK.

Direct Shares

- There is substantial private client wealth invested directly in shares and other securities. At the end of 2003, it is estimated that stockbrokers, banks and fund managers had some 4.8m private clients, although only 423,000 were discretionary portfolio management clients.
- Assets of private clients totalled £239 bn at the end of 2003, of which £142bn was in discretionary portfolios. It is significant that only a small proportion of these assets are invested in commercial property related securities. In large part, this reflects the small size of the quoted property sector.
- Despite the limited overall exposure to property, there is clear indication of appetite for securitised vehicles. Private client brokers have played a significant role in placing funds for recent property trust offerings from, Standard Life and SWIP.

3. Market Size

Direct Property

- In addition to the investment activities analysed above, many investors have invested directly in either residential or commercial property.
- In the case of residential property, there are 408,000 buy-to-let loans outstanding, with a gross value of £39bn. Assuming an average LTV ratio of 50%, the equity invested in residential housing is around £40 bn, excluding investors' primary residences.
- Over the last three years, private individuals have been significant investors in commercial property. Taking into consideration both purchases and sales of assets in the last three years, the total value of net investment has been £6.25bn.
- In 2003, £1.25bn was invested in commercial properties via auction room sales according to JLL/IPD ARAS figures. Over the last five years, auction turnover has increased steadily, with a total of £4.7bn being invested over this period.
- Some private investors have also been investing in commercial property by investing in limited partnerships, syndicates and other unquoted vehicles marketed to high net worth clients. However, there is no readily available source of data on how much money is invested by individuals via these products.

Table 4: **Summary - Individual Investor Assets**

	Asset Value (end 2003 £bn)	% in Property	Property Asset Value (£bn)
Indirect Property Exposure			
Unit trusts & OEICS, of which	138	0.4%	0.6
- PEPs/ISAs	66		
Unit linked life funds	62	13.0%	8.1
Unit linked pension funds	164	6.0%	9.8
Direct share ownership	239	2.0%*	4.8
Total	603	3.9%	23.3
Direct Property Exposure			
Direct property, of which	51.0	100.0%	51.0
- buy-to-let residential	40.0	100.0%	40.0
- commercial acquired by private treaty	6.3	100.0%	6.3
- commercial acquired by auction	4.7	100.0%	4.7
Total Property Exposure			
Total, including direct property	**654.0**	**11.3%**	**74.2**

Sources: IMA, ABI, ONS, ComPeer, Standard & Poor, Lipper, CML, JLL/IPD, PropertyData
*estimate

However, there are real issues surrounding this level of direct investment in property by individual investors, who are often seeking to augment their pensions:

- Risk concentration - by acquiring a single asset investors are taking on disproportionate exposure to a single sector and usually to a single tenant.
- Debt exposure - in order to acquire these assets individuals are taking on debt, but there is widespread inexperience of the risks associated with doing so. Moreover, investors are attracted to direct property ownership by the relatively high income return, but through the need to pay interest on the debt, investors are placing much greater emphasis on receiving a capital return on sale of the asset.
- Management - few individual investors have the time and expertise to efficiently manage the property assets that they have acquired, and fewer still own a sufficient number of assets to achieve economies of scale that reduce costs.
- Depreciation and obsolescence - few individual investors are building these factors into their appraisals prior to acquisition.

The key question for the industry that requires further investigation centres on the reasons why so little is invested indirectly in property, particularly at a time when interest in investing in the asset class has never been higher amongst individual investors. This issue is addressed further by other workstreams in this project, but these are likely to be preliminary in nature and given its importance further exploration will be required.

Market Size – Summary

- **The total value of invested in unit trusts and OEICs by private investors is circa £138bn, but only 0.4% is invested in property assets.**
- **There is circa £62.4bn invested in unit linked life funds and around 13% of this is estimated to be in property funds.**
- **Unit linked pension fund assets amount to £164bn, and circa 6% is invested in property funds.**
- **Private clients own £212bn of assets, but only a small proportion of these assets are invested in commercial property related securities.**
- **Private individuals have been significant direct investors in residential buy-to-let and to a lesser extent, commercial property. However, there is little appreciation by these often inexperienced investors of the risks that they are taking on.**

4. Individual Investors: Profiles & Purchasing Behaviour

The aim of this workstream was to estimate the total number of individual investors, profile these investors and the strategies they employ to buy investment products. Primarily, this involved analysis of 46,000 interviews conducted for the MORI Financial Tracking Survey (FTS) during 2003, and Experian's own proprietary segmentation methods.

- According to the MORI FTS survey, 43% of people surveyed own at least one investment product (the average is 1.9 products each).
- The total number of active investors in the UK is estimated to be 6.5m. Active investors are defined as those with holdings in shares (other than via mutualization or privatization), unit trusts, OEICs or investment trusts.
- It is not appropriate to uniformly characterise the investment strategies of individual investors due to wide differences income, risk preferences, life stage and tax status. Hence, this research has identified seventeen different population types are much more likely to purchase investment products than the wider population and are therefore considered to be a good proxy for the active investor population. Penetration indices of at least 50% above the national average are common. These population types are drawn from five broad categories:
  - ***Money Worth Managing.*** The financial elite, likely to have highest incomes and most complex investment portfolios.
  - ***Asset Rich Families.*** Generally later middle age families. Generally invest in safe, conservative long-term financial products, with a focus on impending retirement.
  - ***Equity Accumulation.*** Mostly 40-50 year olds, married, with good jobs who are able to add significantly to their net worth.
  - ***Grey Lifestyles.*** Covers most of the retired population. Specific sub-segments that were more likely to be active investors were "Equity Rich Elders" in their early retirement years and tend to remain very active with substantial equity capital and older women "On Private Pensions". .
  - ***Parental Dependency.*** Young adults who live at home or are financially dependent on their parents. Typically aged 18 to 25 many will be starting to consider investment products.
- Taking into consideration their appetite for risk, the seventeen types have been divided into three broad groups:
  - Lower risk: Investors attracted to regular savings schemes, and who may be interested in commercial property from an income perspective. Relatively low risk threshold. Estimated market size: 2.75m - 3.0m
  - Moderate risk: Wealthy individuals, moderately attracted to property with a mix of income and growth objectives. The estimated market size is 2.0m - 2.25m people;
  - Higher risk: Sophisticated investors. More likely to be attracted to property investment from a growth perspective and to have a relatively high risk threshold. The estimated market size is 1.8m -2.1 m people;

4. Individual Investors: Profiles & Purchasing Behaviour

- Combined these three segments indicate that the active investor base across the 17 FSS Types lies between 6.55m and 7.35m. All these investors may be expected to have at least some interest in investing in commercial property products.

Profiles & Purchasing Behaviour – Summary

- **The total number of active investors in the UK is estimated to be at least 6.5m**
- **Seventeen different population types are much more likely to purchase investment products than the wider population**
- **Based on their appetite for risk, these seventeen types can be divided into three broad groups:**

  Lower risk: 2.75m–3.0m investors attracted to regular savings schemes, may be interested in commercial property from an income perspective.

  Moderate risk: 2.0m-2.25m wealthy individuals, moderately attracted to property, with a mix of growth and income objectives.

  Higher risk: 1.8m–2.1m sophisticated investors, more likely to be interested in property from a growth perspective.

5. Individual Investors: Attitudes to Investing in Commercial Property

There were two principal strands to this workstream with each providing insights on the attitudes of individuals to investing in commercial property:

- Quantitative analysis aimed at summarising the attractiveness of commercial property.
- Investment for small investors and their likely propensity to invest in new commercial property products. This analysis draws on a survey of 2,000 people undertaken by MORI on the BPF's behalf, and on specific questions inserted into MORI's wider omnibus survey of 2,000 people in April 2004.
- Three focus groups comprising active investors were held in early May 2004 to gathering information on the investment strategies of smaller investors, their objectives and attitudes to commercial property investment.

The key findings are as follows:

- Some caution is required in the interpretation of the survey undertaken on the BPF's behalf by MORI owing to the sample size. However, some general observations are possible and the focus group provide some further insights.
- It is paradoxical that 54% of the 486 active investors interviewed considered commercial property to be the best performing asset over the last three years, but only less than 10% had acquired property based investment products.
- Although 6% had invested directly in residential or commercial property, 84% of active investors have no investment in property outside their own home. The main constraints being affordability (46%), risk (11%) and knowledge; some 7% said they did not know enough about property to invest and a further 4% indicated that they did not know how to invest.
- These obstacles were reiterated during the focus groups where detailed knowledge about the commercial property market was confined to a few active investors who had either made investments in commercial property themselves, or had looked into doing so. Hence:
  - Most participants were not really aware of commercial property as a potential area for investment.
  - Those with no detailed knowledge were not sure whether commercial property would be a higher or lower risk venture than blue chip equities.
  - Participants thought the disadvantages of commercial property investment were the size of the sums required to invest, the long term nature of the investment and the lack of liquidity.
- The MORI survey for the BPF indicates that about a third of active investors are interested in a new commercial property investment product that would offer a 'stake' in a range of property developments.
- Conversely, there was a hard-core of approx 40% of active investors who would need a lot of persuasion to invest in commercial property. This leaves a group of approx 30% who are fairly interested and may be converted over time.
- However, there is a significant gap between those who say they are interested in commercial property investment (30% +) and those who state they will definitely invest. Only 5% of active investors stated they would be interested in investing in commercial property within 12 months.

5. Individual Investors: Attitudes to Investing in Commercial Property

- The focus group analysis helped to shed further light on the attitudes of prospective investors in commercial property products. There was limited knowledge of commercial property investment products, but some enlightening comments were made by focus group participants when presented with key feature summaries of three existing products (authorised unit trusts, offshore property investment companies and unauthorised unit trusts):
  - FSA regulation provided a degree of reassurance for participants who felt less knowledgeable about the commercial property market.
  - For these people, and less active investors, the words "Offshore" and "Unauthorised" had connotations of risk. The following comment sums up this perspective: "The word 'unauthorised' is an off-putter. Every time you read about a financier who has taken people down, 'Channel Islands' and 'offshore' are words that seem to figure".
  - Further, there was some confusion, particularly among the less active investors, as to whether or when income or capital gains derived from offshore investments were liable to taxation.
  - The management fees and transaction costs associated with these products were thought to be high.
- A similar summary of the likely features of Property Investment Funds generated more enthusiasm than the three other products. Several participants said that they themselves would consider investing in them. The main advantages were the relatively high income yield, moderate risk, and low taxation within the fund.
- The liquidity offered by listed PIFs was regarded as a positive feature. However, because of their perceptions of the commercial property market as offering steady rather than spectacular returns, most participants regarded the product as a long term investment.
- Participants felt that two types of investor would be attracted to PIFs: younger people could treat them as a long term investment to provide capital growth as part of a diversified portfolio, in an age where fewer people will be prepared to rely entirely on their pension fund; retired people with a lump sum at their disposal could look to PIFs to provide a reasonable and steady extra income.
- For investors who had decided that they wished to include commercial property in their portfolio, PIFs were considered by participants to be an attractive and accessible way of doing so.

Attitudes to Investing in Commercial Property – Summary

- **There is a significant gap between performance awareness and investment decision-making.**
- **54% of active investors consider commercial property to be the best performing asset, but less than 10% have acquired property products.**
- **A third of active investors say that they are interested in investing in commercial property, but only 5% are considering investing in the next 12 months.**
- **The main constraints on investment are affordability (46%), risk (11%) and lack of knowledge (11%).**
- **In contrast with some existing property products, the likely features of a PIF - high income yield, moderate risk, tax transparency - were seen as positive by focus group participants.**

6. Advisors to Individual Investors

Financial advisers have an important role in advising their clients on whether to allocate funds to commercial property and on the suitability of the different commercial property products. The financial adviser market was sized and structured interviews were conducted with 20 advisers to individual investors. The key findings are as follows:

- Almost £22bn. of regulated financial products were sold in 2001 and independent financial advisers accounted for two-thirds of these sales. The remainder are sold by product provider owned sales teams and by direct marketing, telesales and the Internet. Life and pensions products dominated sales by value with less than 6% being invested in collective investment schemes.
- The FSA put the total number of financial advisers at 77,000, but market sources suggest that only 25,000 of these are active authorised individuals. In view of the promotional restrictions imposed under FSMA on unregulated collective investment schemes, these advisers are a critical channel for the distribution of most existing property investment products.
- Establishing risk preferences is an important first step taken by most advisers in determining an investment strategy for a client. The proportion of equities in the asset allocation is the key variable that alters with risk preference. Hence, cautious investors (low risk) tend to have lower recommended weightings in equities than balanced (medium risk) and adventurous (higher risk).
- Commercial property figures strongly in the asset allocation advisers recommend to their clients. The average allocation to property for a cautious investor (low risk) was surprisingly high at 21%, but this allocation falls as the weighting in equities rises for investors who have greater preference for risk.
- Small IFAs tend to use proprietary software packages to determine asset allocation, according to risk preference. However, these packages do not include property, so it is left to the adviser to allocate.
- To help identify suitable products small independent firms of advisers also often use product selection software, such as Synaptic, and other sources, such as S&P Micropal and fund fact sheets. Property products are not well covered, making the decision-making process more difficult.
- Consequently, a number of advisers noted that a key stage in the product sales process was their own due diligence on the product, which required their 'buy-in' before it would be offered to clients. This approach applied particularly to property where there is little comparative product analysis available.
- For many financial advisers, their clients are inherently risk averse, so the principal property products sold are insurance company unit linked life products and authorised unit trusts. Principal attractions included: diversified ungeared portfolios, reliable brands and competitive charging structures.
- Unauthorised unit trusts were favoured by some because they are readily understood by the clients. Also, offshore property investment companies were seen as being advantageous for the tax efficiencies that they offer. However, there were also concerns that pricing reflects market sentiment not the performance of the underlying assets, and the charges are considered to be relatively high.

- Limited partnerships are seen as appropriate for more sophisticated clients because these offer identifiable properties, gearing and the availability of capital allowances. However, the costs and illiquidity of these products were seen as being their principal disadvantages.
- The actions needed to broaden the access of investors to commercial property included: the need to simplify the product offering and reduce costs. Others would like to see more ISA-able property products as a way of getting smaller investors into property. However, concerns were also expressed about the pricing of listed products.
- Advisers' observations on PIFs are summarised as follows:
  - PIFs would need to be made available by mainstream provider to appeal to the more risk averse because it would be an 'easier sell' for advisers as the well known brand names would be more readily acceptable to clients.
  - Listing PIFs were seen as being attractive to less sophisticated investors, but concerns were expressed that pricing would reflect market sentiment rather than the prospects of the underlying assets.
  - PIFs would most likely appeal to those investors seeking exposure to property but without lump sums to invest.
  - PIFs would be attractive if the transactions costs were kept low and the structure was straight-forward to understand.
  - The high-income distributions associated with PIFs will not prove attractive to all investors. Many of the financial advisers consulted raised concerns about the associated tax liability, particularly for higher tax payers.

Attitudes to Investing in Commercial Property – Summary

- **Financial advisers are an important distribution channel selling two-thirds of regulated financial products and circa 25,000 advisers are authorised to sell unregulated collective investment schemes, including property products.**
- **Establishing a client's risk preferences is usually the first step in determining an investment strategy. The allocation to equities varies with risk preference.**
- **Commercial property figures strongly in asset allocation. The average allocation is surprisingly high at 21%, and the range is 10-25%.**
- **Software packages are often used in asset allocation and product selection; property is not well covered so advisers are reliant on their own due diligence and there is little comparative product analysis available.**
- **Reflecting clients' generally low risk preferences, the principal products sold are insurance company unit linked life products and authorised unit trusts.**
- **Unauthorised unit trusts and offshore property investment companies are seen as offering pros and cons. LPs are more appropriate for sophisticated investors.**

7. Pension Funds and Charities

There are no definitive statistics on the total value of assets held in UK pension funds. In 2003, UBS Asset Management estimated the market to be around £847bn, whereas Mercer Investment Consulting estimate it to be over £1,000bn.

- The large pension funds make up the vast majority of the pension fund universe by value, but the smaller funds, with assets of less than £30m, represent a large percentage of the universe by number. It has not been possible to quantify the exact number or value of their assets, but it is estimated that there are more than 98,700 'live' occupational pensions schemes that each have total assets of less than £30m. These schemes account for 98% of all occupational pension schemes, and together they own an estimated £61.1bn of assets.
- The quantification of the universe of UK charities has proved to be equally difficult. There are circa 163,000 registered charities, with an estimated total value of £70bn. The Charities Commission cannot provide a figure for the number of charities that fall into the £0-30m bracket. However, Caritas Data (the providers of data to the National Charities Database) holds data on 20,710 charities; 13,447 (65%) have a value of under £30m.
- Interviews were conducted with 23 pension funds and 18 charities with total assets of £317.4m and £292.2m respectively. The size range was £50,000 to £30m.
- Small pension fund investment is predominantly in equities - the weighted average allocation is 66%. Despite being categorised as being the highest risk asset class, equities are seen as the primary means of meeting long-term liabilities.
- However, there has been some structural changes over the last five years with downward adjustment in equities allocations in favour of bonds and respondents indicated that further shifts in this direction are likely. The average allocation to bonds is 28%.
- Small charities are less heavily exposed to equities (the weighted average allocation is 49%), and the rationale for holding these assets is more to do with income production than matching longer term liabilities. Their investment in bonds is also typically lower than small pension funds at 11%. However, at 24%, their cash weighting is also much higher than small pension funds (1%).
- A third of small pension funds and charities interviewed have commercial property investments, both direct and indirect. The average allocation to property by small pension funds and charities is 2% and 15% respectively. Property is held in small funds for many of the same reasons as it is held by large funds, namely, income production, capital growth, diversification, and long term liability matching. However, the much higher allocation by charities also reflects holdings in 'legacy type' assets and operational property.
- Small pension funds and charities invest in a wide range of indirect products. Diversification is the main driver for indirect investment, and according to those interviewed this is likely to remain so.
- The majority of investors were disinclined to invest in direct property in future because of its illiquidity, possible lack of diversification, high entry cost and the risk profile. Other reasons for not pursuing direct property investment include regulations, search costs, unsteady income stream and unfavourable returns.

7. Pension Funds and Charities

Pension Funds and Charities – Summary

- Some 98% of all occupational pension schemes (98,700 schemes) have total assets of less than £30m. These schemes own an estimated £61.1bn of assets.
- There are circa 163,000 registered charities. Available data suggests that 65% have total assets of less than £30m.
- Small pension fund invest predominantly in equities (66%) as this is seen as the primary means of meeting long-term liabilities. Small charities hold less in equities (49%) to meet current liabilities.
- There has been a structural shift away from equities in favour of bonds (the average allocation by small pension funds is now 28%).
- A third of small pension funds and charities have commercial property assets, held either direct or indirect.
- Income, capital growth, long term liability matching and diversification are the main drivers for holding property. The latter is the key reason for holding indirect investments.

8. Advisers to Small Pension Funds and Charities

There are wide range of advisers to small pension funds and charities, including firms of independent financial advisers. Interviews were conducted with 10 advisers to small pension funds and charities.

- There is no typical asset allocation for small pension funds and charities from the adviser's point of view. Asset allocations depend solely on the needs and preferences of the client. However, it is significant that advisers were split about whether equities or property carried the most risk and this would condition their views on allocations.
- There is a consensus amongst the advisers that small pension funds and charities do not have sufficient funds available to invest directly into property. Nearly all advisers recommend indirect investments for these investors. The majority viewed property as a good diversifier, with access to specialist management and the relative ease of management also being attractions.
- Amongst those already invested, listed vehicles tend to be favoured together with unauthorised and exempt unit trusts.
- With the exception of pooled pensions products, the authorised products attract little interest from the advisers or their clients. Similarly, limited partnerships.
- Liquidity is perceived to be the principal disadvantage associated with indirect investment in property.
- Actions to improve access to the market include: relaxation of current regulation, the need for more tax transparent products and products that allow an easier exit than currently available. In this context, PIFs were seen as being beneficial.

Advisers to Small Pension Funds and Charities – Summary

- **There is no typical asset allocation as this depends solely on the needs and preferences of the client.**
- **There is a consensus amongst the advisers that small pension funds and charities do not have sufficient funds available to invest directly into property.**
- **Listed vehicles, unauthorised and exempt unit trusts tend to be favoured by advisers to small pension funds and charities whose clients are already invested indirectly.**
- **Liquidity is perceived to be the principal disadvantage associated with indirect investment in property.**

9. Product Providers' Perspectives

Face-to-face discussions were held with senior representatives of 10 organisations that promote and manage indirect property investment vehicles. These vehicles included: authorised unit trusts, unauthorised unit trusts, unauthorised exempt unit trusts, offshore domiciled/UK listed companies, limited partnerships, a common investment fund and a closed-ended investment company with variable capital.

In addition to the more product specific comments of the providers interviewed for this project, which are reflected in the product review (see below), a range of more general comments were made and these are summarised here:

- The existing property investment product structures are inflexible and complex to manufacture. To meet the needs of investors and those of regulatory bodies, often in different jurisdictions, providers are going to considerable lengths and incurring significant cost to structure products.
- Most existing products have been developed for the institutional market and fee structures reflect this position with little or no initial charge to pay fees to introducers. Where institutions and private individuals do co-invest, there is usually a different fee structure that applies to retail investors.
- The number of new offshore listed products is likely to be constrained by the practicalities and significant costs of bringing together portfolios of properties. For example, few organisations outside the major life companies own pools of assets that are exempt from Stamp Duty.
- There appears to be a growing understanding amongst intermediaries about property investment products. However, there is still widespread concern that financial advisers and their clients are neither fully conversant with the attributes and risks of different products nor appreciative of the impact that initial charges can have on their clients' equity investment.
- The slow reaction times associated with the vetting procedures adopted by some larger, national firms of financial advisers is seen as a constraint upon the take-up of products, particularly where the product offering period is limited.
- Similarly, the lengthy due diligence and decision-making processes of pension fund trustees tend to limit their participation in products that have limited offer periods.
- Authorised products are an easier 'sell' for financial advisers because they are considered to be relatively less complicated and many smaller financial advisers are not able to sell unregulated products because of these products are not covered by their professional indemnity insurance.

9. Product Providers’ Perspectives

- In general, the product providers consulted were not attracted by prospect of offering property investment vehicles to retail investors for the following reasons:
  - The absence of suitable distribution channels, which is seen as a pre-requisite for success. Even those organisation with developed distribution channels found themselves constrained in their marketing of property product to retail investor because unregulated collective investment schemes cannot be promoted directly to the public.
  - There is a greater risk of mis-selling. High net worth 'sophisticated' investors are presumed to know the pros and cons of the products that they are buying and be able to invest for the extended periods required by some products. The high minimum investment levels (£25k plus) that reflect the unregulated nature of many of the products reinforces this perception.
  - The considerable administrative burden associated with dealing with a large number of retail investors. For example, several product providers cited the inability of their existing (sophisticated) investors to complete application forms correctly.

Advisers to Small Pension Funds and Charities – Summary

- **The existing property investment product structures are inflexible and complex to manufacture.**
- **Most existing products have been developed for the institutional market and fee structures reflect this, so there are no scope for introducers' initial fees.**
- **New offshore listed products are likely to be limited in number due to the practicalities and costs of bringing together portfolios of properties.**
- **There is widespread concern that financial advisers and their clients are not fully conversant with the attributes and risks of different products**
- **Lengthy due diligence and decision-making by both large firms of financial advisers and pension fund trustees restricts their participation in products with limited offer periods.**
- **Authorised products are an easier 'sell' for financial advisers because they are considered to be less complicated.**
- **Existing product providers are currently not attracted to retail investors citing absence of suitable distribution channels, greater risk of mis-selling and administrative burden.**

10. Product Review and Evaluation

Fourteen different product structures have been reviewed against six key criteria:

- Marketability (legal & regulatory requirements)
- Accessibility (min investment level)
- Liquidity (time to transact, cost)
- Pricing mechanism (property valuation or market sentiment)
- Flexibility (constraints on gearing or investments)
- Tax treatment (leakage within the vehicle)

The following general conclusions can be drawn from this review:

- There appear to be a relatively large number of different structures available for small investors of different categories to gain indirect exposure to commercial property.
- However, there is often limited choice within each category. For example, there is only one investment trust that invests in direct property, there are currently only two common investment funds and only three authorised unit trusts.
- Moreover, certain types of investors may be excluded from investing due to their tax status, or by the minimum investment amount required. For example, many unregulated schemes have minimum investment requirements of £25,000+.

Taking a different perspective and evaluating the available array of products against the needs of different categories of small investors provided further insights. The needs of these investors have been derived from different project workstreams.

Small pension funds and charities have the widest range of product categories to choose from and their requirements can be summarised as:

- Liquidity
- Low transaction costs
- Small lot size

Sophisticated investors are currently much better served in terms of available products than those with smaller sums to invest. Defined as being those with more than £25,000 to invest at one time, these individuals may also be expected to have a greater appetite for risk have a better understanding of financial products. The potential market size exceeds 2.1m people. This group have a greater preference for unlisted vehicles that are a better proxy for direct investment.

Individual investors who have both a lower appetite for risk and less than £25,000 to invest have a limited range of products to choose from currently. The needs of this group, which potentially amounts to between 2.75m and 3.0m people, can be summarised as follows:

- Small minimum investment
- Liquidity
- Low transaction costs
- Listed/Authorised
- Onshore
- No/limited tax within the vehicle

10. Product Review and Evaluation

Mapping these expressed requirements across the available product categories shows that no one product meets all investors' needs. Whilst UK listed property companies offer many of the desired features, together with a wide range of choice, investment in property company shares is not a good proxy for the underlying property assets and there is tax leakage from the vehicle. At the other end of the scale, offshore unit trusts are a better proxy for the underlying assets and have minimal tax leakage, but are neither domiciled nor listed/authorised in the UK. Moreover, there are few products that have investment minimum below £25,000 and often this is at the discretion of the manager.

Table 5: **Meeting the needs of individual investors**

	Small min investment	Liquid	Low dealing costs	Listed or Authorised	Onshore	Proxy for direct	Low tax leakage	No of products
UK property co	✔	✔	✔	✔	✔	✗	✗	50+
Investment trust	✔	✔	✔	✔	✔	✗	✗	1
Authorised unit trust	✔	✔	-	✔	-	-	✗	3
Unit linked life fund	✔	✗	✗	✔	✔	✔	✔	<20
Listed offshore property company	✔	-	✔	✔	✗	-	✔	<10
Offshore variable capital company	✔	-	✔	✔	✗	-	✔	1
Offshore unit trust	-	-	✗	✗	✗	✔	✔	<10

Key: ✔ = positive; - = neutral; ✗ = negative

Product Review and Evaluation – Summary

- **There is a relatively large number of different structures available for small investors of different categories to gain indirect exposure to commercial property.**
- **But there is often limited choice within each category and some types of investors are excluded from investing due to their tax status, or by the minimum investment amount.**
- **Small pension funds and charities have the widest range of product categories that meet their needs.**
- **Sophisticated investors are currently much better served in terms of available products than those with smaller sums to invest.**
- **Individual investors who have both a lower appetite for risk and less than £25,000 to invest have a limited range of products to choose from currently and no one product fully meets their needs.**