Goodbye Piccadilly, hello Reading. Property speculators head west

Bargain hunters are homing in on industrial parks in the provinces, writes **Oliver Shah**

EVERY Friday and Saturday night, scores of wealthy youngsters queue along Derry Street in Kensington, west London. They wait excitedly to get into the Roof Gardens, on the sixth floor of an art deco building that was once a department store.

The grade II listed gardens have flamingos, fruit trees and a stream stocked with fish. Celebrity visitors have included Mick Jagger and Maria Sharapova.

Kensington Roof Gardens is one of the capital's most expensive nightspots — and one of its trophy properties. In January it was bought by the Conley family of Germany for £225m. The purchase marked the latest in a long line of swoops by foreign investors on prime property, all driven by London's reputation as a safe haven.

Last month, another overseas buyer struck a very different kind of deal. Oaktree Capital Management, the aggressive American asset manager, and the German investor Patrizia paid £245m for the IQ business park near Reading. Set beside the M4 motorway, it is the kind of drab campus where you would expect to find David Brent of The Office.

Yet Oaktree and Patrizia will probably make many times more money than the Conley family. Spurred by a resurgence in bank lending, the frenzied market in the capital and the lure of lower prices, investors are venturing back into the property outside London's prime postcodes.

The trend, led by opportunistic US funds and now being followed by the more conservative British pension funds, has sparked speculation about a long-awaited recovery in locations that have languished since the financial crisis.

"Over the past three years the demand for space from tenants was poor, and 18 months ago you couldn't get the debt to do deals," said Mike Brown of Prestbury Investments, which advises Max Property Group.

"Now we are reaching stabilisation in most occupational markets and debt is available again. In the short term it becomes self-fulfilling, anyway. With a limited amount of good stock, prices are rising simply because there are more buyers than sellers."

In 2009, the year after Lehman Brothers went under, it looked as if there was no way back for much of the regional property market. Values fell by half and the appetite for space evaporated as companies and the government cut staff. Lloyds Banking Group and Royal Bank of Scotland (RBS), which both lent billions of pounds on poor-quality property during the boom, collapsed into state control and turned off the supply of loans.

Values of shiny offices, shops and hotels in London have rallied since then but they are still 9% below the level in March 2008, according to Investment Property Databank, the analyst. Values of "secondary" properties — lower-quality buildings often located outside southeast England — are 43% lower.

Earlier this year, sentiment finally started to change. DTZ, the consultant, predicted that secondary property would prove a better investment than prime from next year. To start with, it said, this would be because of bargain-hunters switching their attention from London and pushing up prices elsewhere, rather than a surge of tenants seeking new space.

DTZ forecast that rents in the regions and weaker parts of the southeast would not turn positive until 2015. Occupier demand usually lags wider economic recovery by two years.

The push into the murky waters of riskier, less popular property started in late 2011 when Blackstone, the American private equity firm, bought into a £1.4bn portfolio of loans held by RBS. The loans in the deal, known as Project Isobel, were backed by buildings ranging from Pendragon car showrooms to Toys R Us megastores.

Lone Star, a distressed debt specialist, bought a pool of property loans from Lloyds in the same month. Other investors, such as Cerberus, Starwood Capital, Kennedy Wilson and even the bond fund Pimco, snapped up similar portfolios.

British pension investors have followed, priced out of London by Chinese, Malaysian and Singaporean money.

Lord Oakeshott, a long-time investor in property nationwide through his firm, Olim Investment Managers, said: "Values have been drifting down over the past 18 months, which is the ideal hunting ground for long-term investors. We've been buying hard since the start of last year. London is an overheated offshore island but there's been plenty of value in the provinces."

He added that mainstream pension fund managers had waited until now because "they prefer to move in a herd". "Some of them feel quite brave getting on a train to Bristol or Birmingham," Oakeshott said.

Simon Cooke of APAM, the asset manager, which last month created a joint venture with M7 Real Estate to buy out-of-favour offices, cautioned that many buildings outside London would remain empty and impossible to invest in.

In March, Cooke looked at a vacant business park in Peterlee, Co Durham, where warehouse rents had been cut to £1 a square foot.

"There are some parties that see this trend as the new beginning and the start of a recovery," he said. "There are others, like me, who say this is not about recovery, this is about liquidity.

"Because more money is coming in, everyone assumes pricing is going to go up. When you actually stand in front of a building in Peterlee with a £1 letting board, you realise there's no justification for that to go up in value."

Sky high prices: Kensington Roof Gardens, haunt of celebrities such as Daniela Hantuchova, sold for £225m