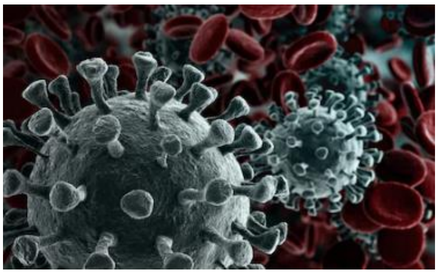
# OAK INVESTMENT MANAGEMENT GROUP



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# Is Real Estate a *'Risk On'* or *'Risk Off'* Asset Class?

*During these uncertain times basic assumptions are challenged and little can be taken for granted. Primary (medical and epidemiological) assertions are hard enough, let alone positing assertions about the secondary economic consequences of Covid-19 on the world. The OECD has suggested that Covid-19 could halve global economic output, but no one really knows whether the virus will lead to the break-down of the social order, or, will be a temporary and fleeting adjustment to higher death rates of certain sections of society.*

Real estate necessarily follows the behaviour of the economy. Clearly if the economy contracts, then real estate contracts and equally if the economy grows then real estate too grows (both after a time lag). Time lag is necessarily because of the large cost and time of producing new stock. However, general (or average) performance masks huge discrepancies.

Not all assets are not equal winners and losers. Over a set period, some capital values outperform (come into favour with investors) some capital values underperform (go out of favour with investors). Equally, over a set period, some rent levels (yield) decrease which, at a set price, makes rent relatively less expensive for occupiers and concomitantly some rent levels (yield) increase which, at a set price, makes rent more expensive for occupiers. Over a set period, some assets go completely out of fashion (redundancy) and some come into fashion (new stock).

To add to the 'noise' there is a downwards '*theta*' on value that, in itself, is dependent on the buoyancy of the market. The more robust the market the quicker the real-life depreciation of the asset, the less robust the slower the real-life depreciation of the asset. Finally, like all asset classes real estate is always priced by the most marginal vendor and the most marginal buyer – but importantly unlike lots of asset classes the distribution of these events from a statistical point of view is binomial rather than discrete, and based on a different time horizon.

Is real estate therefore a safe haven or a fool's haven? At the heart of real estate is the basic value of the property alongside a covenant (bond) by an occupier to pay for the use of the property. Generically property cannot be considered a haven from the ravages of the market. Specifically, some assets can be not only a diversifier but a safe haven in troubled times. Unlike stocks and shares the coupon is visible and reliable (and open to one's own assessment of risk). An investor is not reliant on management as well as analysts to understand the risk of a coupon which by definition is at the discretion of management. Clearly troubled times do challenge to the limits hypothetical covenant tests but within a range and well-chosen assets in real estate do provide the insulation, diversity that investors might crave.

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