What does Brexit and the new Conservative government mean for the London Property Market?

On 23rd. June Britain voted to leave the European Union. After joining over 40 years ago, the result of the referendum has delivered the most radical shake up in UK politics for a generation. Whilst the result itself was a shock to many, the speed with which the Conservative party machine has reacted will soon bring stability to the economy and property market. The new government, which has been in place for only a matter of days, has already given a strong steer that future economic policy will be reflationary, business-friendly and focused on growth.

Our view is that short-term market forces will be a strong buying signal for the UK residential market. By this autumn and throughout 2017, we forecast the UK will once again look like a 'safe haven' for overseas investors; The events of the last three weeks have led us to conclude that the window of opportunity to invest in UK residential property will be a lot shorter than expected.

The Conservative party united under Theresa May's leadership will provide a bullish backdrop for UK real estate

In the months leading up to the referendum uncertainty over the result has caused the London residential property market to slow down. The unexpected result has produced continued turbulence - but we see this calming significantly as political clarity unfolds. In particular the key players have already been very supportive, and will continue to be so going forward:

(1) The Governor of the Bank of England:

On the day of the referendum result the Governor of The Bank of England reassured the markets that he "would not hesitate to take additional measures required" to support the financial markets through "any period of uncertainty and adjustment".

That reassurance is shared by the Monetary Policy Committee. The minutes of last week's meeting (where interest rates were sensibly kept at 0.5%) indicated that many members expect to vote for a rate cut at the next meeting in August. The extent of their commitment to monetary easing can be summed up by the Bank's chief economist, Andy Haldane, who said in a speech delivered on Friday that: "I would rather run the risk of taking a sledgehammer to crack a nut than taking a miniature rock hammer to tunnel my way out of prison."

(2) The new Chancellor of the Exchequer:

"Markets do need signals of reassurance, they need to know that we will do whatever is necessary to keep the economy on track" (Philip Hammond: 14th July 2016).

In interviews with the press and media, the new chancellor, Philip Hammond (who reassuringly has a strong property background) has described the UK economy as entering a "new phase" and made clear that he understands investors "temporary loss of confidence". As a result, we believe;

- Deficit reduction targets will likely be scrapped.
- It is likely that infrastructure projects (a theme popular with the new Prime Minister) will be increased.
- Taxes (Corporation Tax and Capital Gains Tax) will be cut.
- A potential cut in the higher rates of SDLT might also be on the cards.

All of these measures will increase the attractiveness of the UK as a place to invest and do business.

There is an additional possibility that the Chancellor may well, and importantly for London as a major financial Centre, stress that the City will not be bound by any EU regulations on a Financial Transfer Tax (and bonuses).

The net result of a reflationary government policy, combined with a supportive central bank **will ignite growth in the UK economy.**

Medium term: Focus on UK 'special status' with the EU

The overriding priority for the new look government this autumn and beyond will be to secure access to the single market and special status for the UK within the EU.

Before the election we were deluged with scare stories focusing on the perils of the 'day after the night before'. This was mostly related to how European political leaders would react to a Brexit vote. Initial mutterings form EU national leaders, notably the German Chancellor, point towards a period of calm.

Our belief is that EU leaders will need to resolve the UK's status quickly and in a way that instils confidence back into sterling and UK assets. The last thing the French and Germans need is a weak sterling - adding to deflationary pressures in Euroland and taking export markets away from them.

Global economic headwinds will also provide a good backdrop to cutting a deal with the EU. We therefore think the UK will get a quick 'special' status, including full access to the single market.

Long term: The global backdrop will provide benefits for the UK residential property market

The great lesson of history is that the financial market 'circus' soon moves on to other distractions. The reaction of European markets after the vote has signaled this; and the elections of 2016 and 2017 will provide plenty of opportunity for continued disruption in other countries.

The US election in November looks set to undermine the whole basis of Global Free Trade orthodoxy. This will put doubt in the attitude of the USA, permitting unfettered access to its consumer market.

Brexit will encourage electorates in Spain, France and Germany to vote for change in the EU. In particular, we believe that next year's French Presidential elections will see the emergence of an anti-EU/Euro majority and this will have a seriously disruptive impact on Euroland.

Because of this we strongly feel that the UK will hold **safe haven status within six months**.

D&GAM research into past financial shocks – we are in <u>charted</u> territory

In the aftermath of the vote we circulated a presentation that we delivered to investors in the city of London last week. Our analysis revisited in detail two particular events considered by many at the time to be existential threats to the London property market:

- £ Sterling's exit from the ERM in September 1992; and
- The global financial crisis of 2008.

On both occasions sterling's weakness against the $US was followed by a reduction in interest and economic stimulus. The result: **a sharp increase in residential property prices**.

Conclusion

The swift clearing process of UK parliamentary democracy, doubted by some, has meant that there is only a limited window of opportunity for investors to snap up opportunities in the London residential market.

With prices having softened pre-Brexit and in the few weeks since, we are now entering a period of political certainty. This has happened a lot sooner than expected – David Cameron originally thought he would be lingering on as a caretaker Prime Minister until September/October.

It is likely that the pound will enter a period of stability against the dollar and strengthen further. With economic trouble likely on the continent, sentiment may well turn positive and the pound could strengthen. We strongly feel that the currency advantage for overseas buyers could also disappear in the next 2-3 months.

People 'sitting on the fence' currently need to act quickly. By September/October we could well see a normalization of the market and price stability. **Prepare for a V shaped recovery**.