Market Comment

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Matthews & Goodman

Property Advisers

BREXIT
WHAT IT MEANS FOR UK PROPERTY

In the immediate aftermath of the vote in the EU Referendum to leave the European Union, there is a great deal of uncertainty about the future course of all markets, including the stock market, property, and other forms of investment. It is likely to be several months before any clear trends become established. The short term uncertainties include political risk from forthcoming changes in the leadership of the major parties, a possible General Election, and near-term volatility in currency and stock markets, all of which will impact general investment sentiment.

Longer term uncertainties will centre on the nature of the UK's future relationship with the European Union, the potential decline in influence of the City of London, consequent loss of jobs and possible move off-shore of major high net worth employers. These trends are likely to become clearer after at least a year.

Putting it into perspective

Some markets have in any event been experiencing a cyclical peak. Following a period of increased trading volumes and yield hardening, Q4 2015 saw commercial property investment market activity calming down with a sense that the prospect of significant capital growth had receded. At the time, some commercial fund managers reported neutral capital flows and predictions of single digit total returns for commercial property in 2016.

With ongoing low interest rates and volatility in financial markets likely to be a feature for the balance of 2016, commercial property still provides a comparatively solid income return. Robust demand for properties with strong fundamentals, including good quality sustainable income streams, is likely to continue.

Rising confidence and sentiment

We should be watching out for rising confidence levels and sentiment over the coming days which, if managed well by our political leaders, will reassure overseas investors from whom early signs suggest an ongoing appetite for UK assets. Some overseas investors are expected to take advantage of currency movement, with a weaker sterling resulting in UK assets becoming nominally cheaper. Weaker sterling will also help exporters, although it may stoke inflation and in turn force higher interest rates next year.

We do however anticipate a cooling in prices for secondary assets and speculative developments, where occupier demand is unlikely to be robust in the light of economic uncertainty. In short there will be a general flight to quality, with reduced investment activity and outward drifting of average yields during the period of uncertainty whilst new terms of engagement with Europe are negotiated.

For many of our occupier clients, it is business as usual with uninterrupted engagement on regular property matters. However, large financial institutions will continue to sit on the fence and delay activity.

Structural Change in Central London?

We may well see a structural change in Central London market pricing, which could leave London out of step with other, potentially more stable, parts of the UK. As already reported, disruption of the Central London residential market is set to be exacerbated. Weekly analysis from LonRes highlights that capital transactions are down and we predict this will continue for some months, leading to pricing difficulties. Letting instructions are however sharply up, which is likely to result in rental levels edging down.

The Autumn Budget might see a further tightening of tax loopholes, which has already had an effect on high end residential values and the buy-to-let market.

FTSE indices provide reassurance

Overall, whilst there will be turbulence, we can already be reassured that the FTSE 100 and 250 indices are currently above February 2016 lows and arguably weathering the storm better than could have been anticipated. UK property remains a strong asset with global appeal, irrespective of EU membership.

For more information, please contact James Routledge
020 7747 3189 jroutledge@matthews-goodman.co.uk