

# Executive Analysis

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**London's Prime Residential  
Property Report - Quarter 3**

## Safe as Houses?

With strong returns in the first half of 2010 yet falls in August and September, what is happening with London's prime residential property market?

Although the record low interest rates have made mortgages cheaper in the UK, the continuing lack of credit has meant domestic buyers have still struggled in the market and mortgage approvals remain relatively low. This has pushed domestic buyers towards the rental sector, which had a buoyant first half as a result.

The increased demand for rental properties coupled with discounted property prices has pushed yields for prime London properties up, making them attractive for foreign investors compared more volatile stocks and lower yielding government bonds.

At the same time the surge in the wealth of ultra high net worth individuals, (rising 21% in 2009) with the rebounding of commodity prices, has played into with London's prime residential hands. It's reputation as a safe haven for wealth has attracted strong interest for the most exclusive properties, pushing prices up 8.9% year on year in Q1 and Q2.

To further fuel investor demand the pound sterling remained weak (25% lower than peak) making investment in the UK cheaper. These factors, along with the illiquidity of the market, appear to explain why the prime property saw this strong rise.

*London's reputation as a safe haven for wealth has attracted strong interest for the most exclusive properties*

As a result half of all £2 million plus luxury properties sold in central London go to foreign buyers, rising to 60 percent in Knightsbridge, Mayfair and Hampstead, and on up to 70 per cent of all homes over £5 million. This summer also saw the first residential property sold in London for over £100 million (One Hyde Park), again to a foreign buyer.

The 2nd half of the year remains a different story. For the time being the short term market indices, although volatile because of low volumes (20% lower than the Q3 2009), recorded a 2.8% monthly drop. Estate Agents have noticed a reduced interest in August as the Middle East market cooled down during Ramadan.

In addition the Euro's uncertainties over the summer took its toll on its exchange rate lowering the purchasing power of the bloc. As a result prices suffered a dip in August and September. Yet, despite this fall, prices still remain well above the September 2009 mark, leaving investors with their net rental yields and a modest capital gain.

With these two factors alleviating, demand should return to levels seen earlier in the summer along with property prices. The fortunes of London remain more globally intertwined than ever, with a crash only likely should another global crisis strike again ■

Fig. 1



Fig. 2



Fig 1. Highlights the continuing weakness of the sterling against the Euro, Dollar and Asian currencies linked to the dollar. This Provides properties at a discount to overseas investors. With Government austerity measures in the pipeline this seems likely to remain.

Fig 2. Shows the volatility of stocks against London's prime housing market for the last year. Total returns for the period October 2009 to end of August 2010 (excluding dividends, rents and exchange movements) were 10 times larger for Prime properties at 14.18% compared to a 1.38% return on stocks.



## A Longer View

### Can London's prime residential property continue its ascent?

Since our parent company, Octagon Properties, was formed in 1968 residential property values have increased 60 fold and that's without net rental income taken into consideration. Its strong performance is a function both of the desirability of London Central property and its relative illiquidity, which helps smooth over the peaks and troughs of other asset classes. This is what makes it such a valuable component in a balanced investment portfolio and with capital flowing into emerging markets at record levels, London's prime market seems to be a safe hedge to offset these riskier assets.

As long as London retains its status as a centre of culture, business and history, which other cities struggle to imitate, this global demand will remain. And with the Olympics coming in 2012, a Football World Cup bid being prepared for 2018 and threats of regulatory onslaught on financial services not materialising, it looks like London's reputation is here to stay.

Other threats to the market include a rise in interest rates, that may indeed pull money

out of property as well as stocks. However with strict planning laws and a near halt to new building in 2008 and 2009, properties remain in short supply. And with the number of ultra high net worth individuals (with wealth of over £30 million) set to soar as emerging markets grow, demand is set to increase too.

***the strong performance is a function both of the desirability of prime London property and its relative illiquidity***

Nevertheless, in the medium term, doom mongers are quick to predict another crash in property values; citing the continuing lack of credit in the domestic economy, a rise in interest rates and a high house price to earnings ratio. However the global nature of the prime London market means properties are now a vital part of an investment portfolio, not just a house. With strong returns over the past year and healthy net rental yields of 4.6%, they will retain their home within the books of investors for some time to come.

Fig. 3 HNWI Population

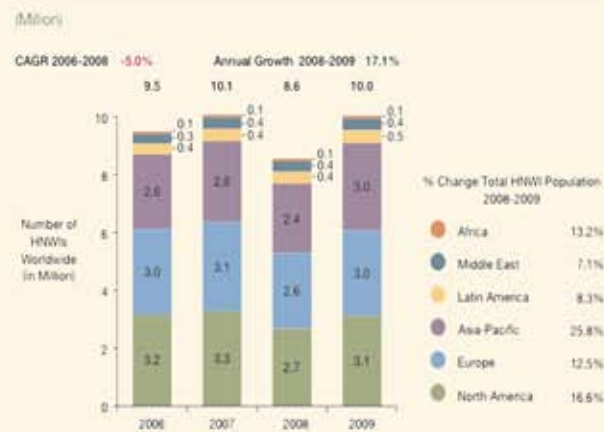


Fig 3. Shows the quick rebound of the number of High Net Worth Individuals following 2008's slump. Asia continues to be the main driver of wealth creation.

Fig 4. Prime London vs Equity Return



Fig 4. Shows the vast returns that prime London property (The Royal Borough of Kensington and Chelsea) has achieved in comparison to the FTSE 100 over the same period.

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