THE PRIME PROPERTY MARKET

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HAMPTONS INTERNATIONAL

THE WEALTH PARTNERSHIP

Why London?

What does 2018 look like for London's prime property market?

The approach of Brexit has led to many uncertainties about the future performance of the UK economy and its housing markets. However, there are many reasons to believe that the UK will ride the storm and that its property markets will continue to perform well. London is and will continue to be a desirable city to live in and to visit.

The cachet of owning one of the best addresses in the capital is not tied to its membership of the European Union, but to the opportunities for wealth creation in a global economy, along with its enduring desirability as one of the world's most historic cities.

While there may be some uncertain times to ride through and bumps along the way, there is still confidence in the UK's long-term economic prospects and investing in its property markets continues to be an attractive way to be a part of that.

The Appeals of Investing in UK Property

- Residential property performs well in the UK, but prime property outperforms across the whole nation
- Prime London property significantly outperforms other assets over the long term and the most exclusive property benefits from the largest returns
- Prime London markets have grown to accommodate demand for luxury city living, but the most exclusive areas retain their edge
- Taxation has altered some of the returns, but the UK remains well placed relative to other global cities
- Transition from the EU causes uncertainty, but the effective currency discounts compensate handsomely for the risks
- The outlook for capital growth in London's prime market is positive, supported by the lack of supply and rising competition for the best addresses
- Despite concerns about the effect of Brexit in the UK economy, London continues to outperform many competitor cities on the characteristics most important to wealthy investors and families

Market Overview

The most exclusive property has delivered the best returns over the long term

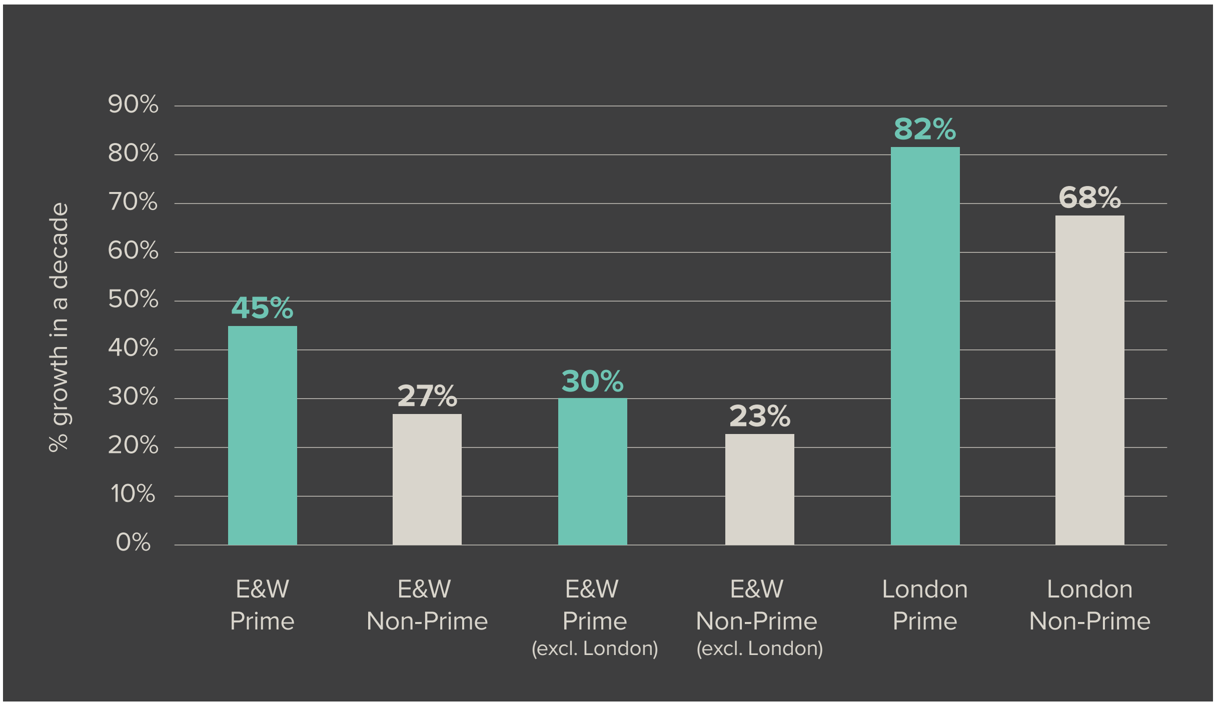
Residential property has long been a favoured investment, particularly in the UK. In the last fifteen years, the number of buy-to-let mortgages has increased tenfold as access to finance opened opportunities for more people. Residential property has remained a popular investment despite the credit crunch, which led to tighter affordability restrictions on bank finance and changes in tax policy. Low interest rates and low yields on other investments have helped to support this demand and indeed helped to support prices.

However, investment in prime property has been more lucrative, across the whole of the UK, not just the London markets. In the past decade, property prices in prime markets in England and Wales rose by 45% (30% excl. London), compared with 27% (23% excl. London) in non-prime markets. In London, prime property increased in value by 82% in the decade compared with 68% in the non-prime markets.

Property owners in London have seen very satisfying returns, but the amount depends on where the property is based. New, desirable areas of the city that are not quite classified as prime, but rather prime fringe, have seen strong returns over the period, but it's the most exclusive property that has delivered the best returns over the long term.

Over the past decade, property prices in the prime central area of London increased by 101%, but prices of the most exclusive properties in the super-prime areas of the capital increased by 116%. So, even within

Price Growth 2007 - 2017



Source: Hamptons International, HMLR

“The markets don’t expect rates to get above 1.25% within five years.”

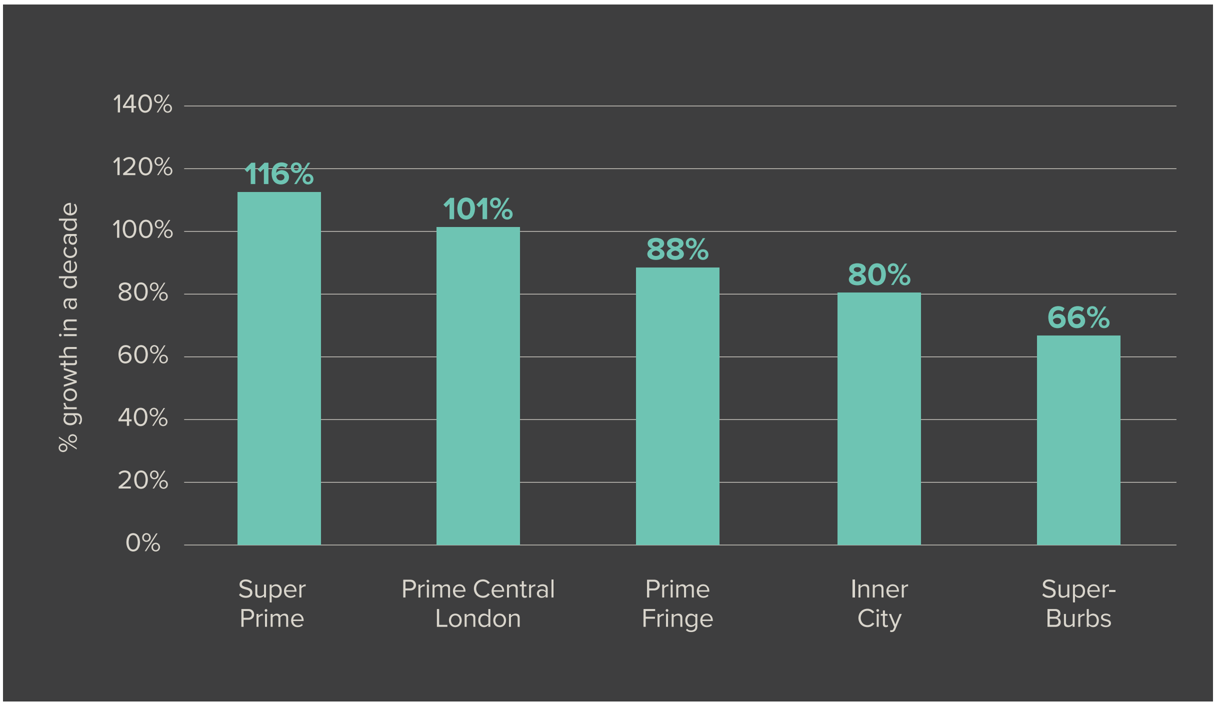
the prime sectors of the market the more exclusive the area, the more resilient prices are.

The obvious reason for this is the lack of available supply compared with demand. There has been an increase in the building of luxury property that has been difficult to achieve in the most exclusive locations. However, the most prestigious parts of London - overall a small geographic area - cannot accommodate demand from the growing number of wealthy households wishing to move into them. As a result, valuations have risen faster in the super-prime district and prime central markets have served as an overspill for those priced out of the most expensive areas.

Demand for prime property from the wealthy has pushed the geographic boundaries

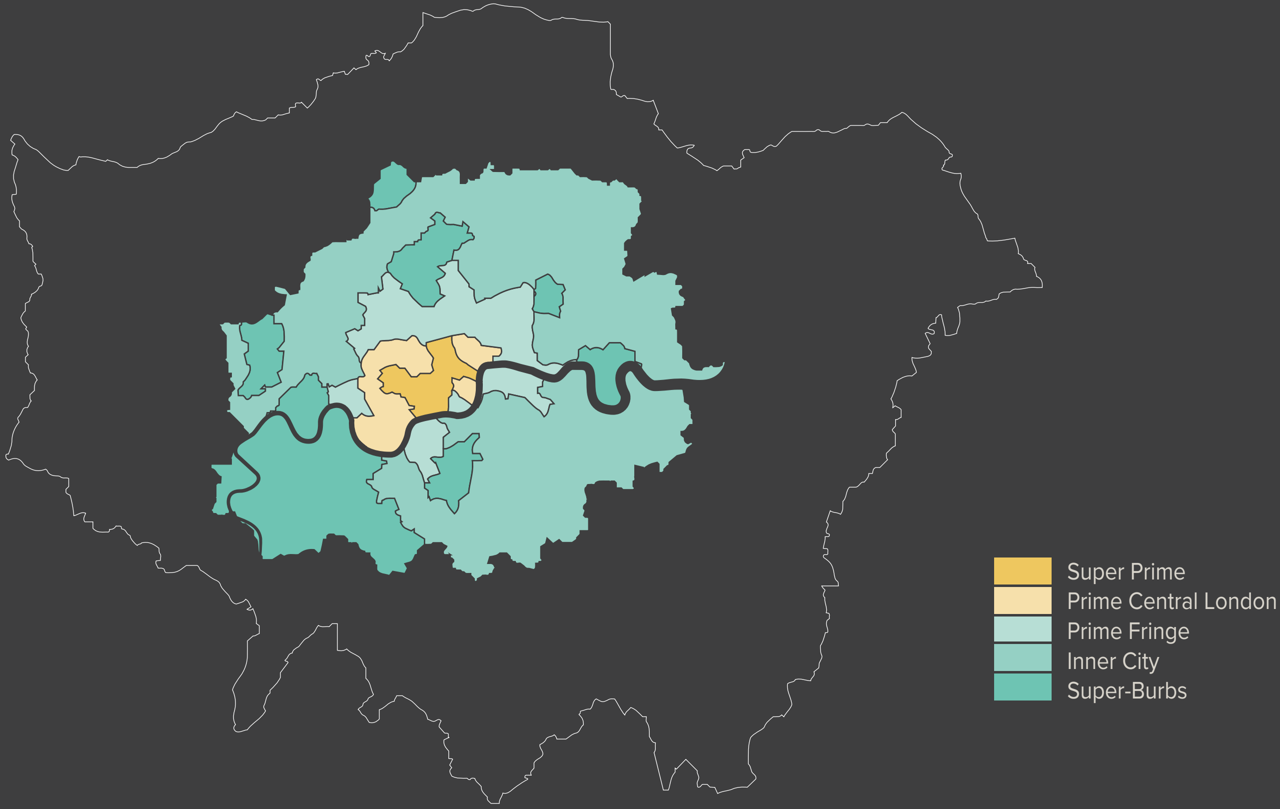
During the past couple of decades, prime London has doubled in size, growing from 10 to 20 square miles. Despite what has been a tough couple of years for the prime London market, there are few signs to suggest its structural growth is slowing. In similar fashion to almost every other world city, the appetite for luxury central living among the wealthy is growing. The success of developers in providing new luxury accommodation to satisfy demand in the higher price brackets is quite stunning. On average, the most expensive property in prime central London that was sold or refinanced in the past 12 months was built this century.

London’s Price Growth by Sector

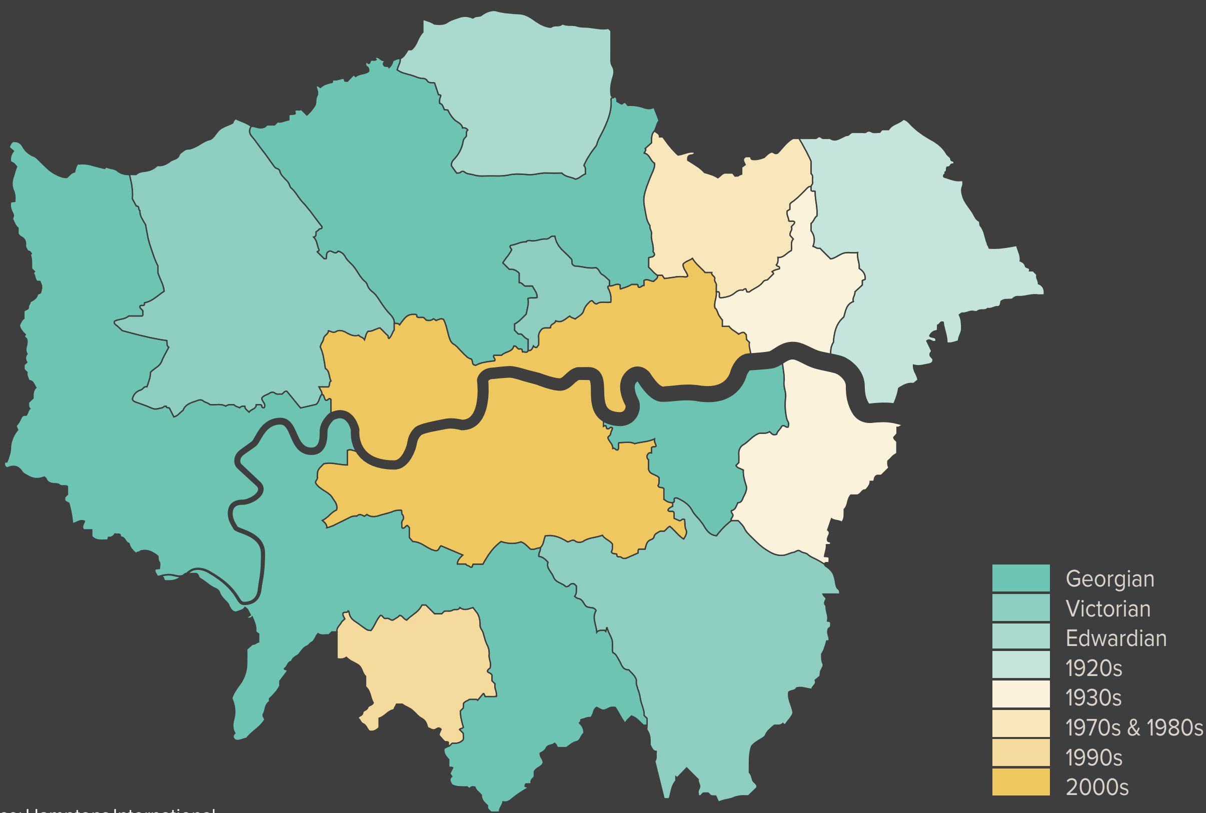


Source: Hamptons International, HMLR

Defining Prime London



Most Expensive Era Of Property



Source: Hamptons International

Relative Performance of London Property

Is property investment growth still possible?

Aside from the cachet of living in one of the world's most desirable cities, investment in London property still has to be attractive from a financial viewpoint. Low interest rates have had a negative impact on investment returns in many financial markets, pushing investors to search for yields in other asset classes. This appetite for higher returns has fuelled some of the capital growth in the property market. Transaction levels in the prime London market have been patchy in some periods but overall its price recovery has outpaced even gold – the ultimate safe-haven commodity.

Even though prime London property has outperformed other assets over time, price growth cannot accelerate forever. If it becomes detached from the underlying fundamentals of the economy, expectations of future growth will suffer and prices will adjust until they realign. Such rapid price growth in the Noughties was unsustainable, investors' expectations began to weaken from 2013 and so did the pace of price growth.

There are two reasons why this happens. First, as prices become detached from other housing markets the pool of potential buyers shrinks, meaning those who wish to sell quickly will face price negotiations. Second, as prices in the most exclusive areas become unaffordable to all but the wealthiest, buyers look to adjacent areas where there is better value for money – and more opportunity for future price growth. This has benefited both areas on the fringe of prime London and towns further afield.

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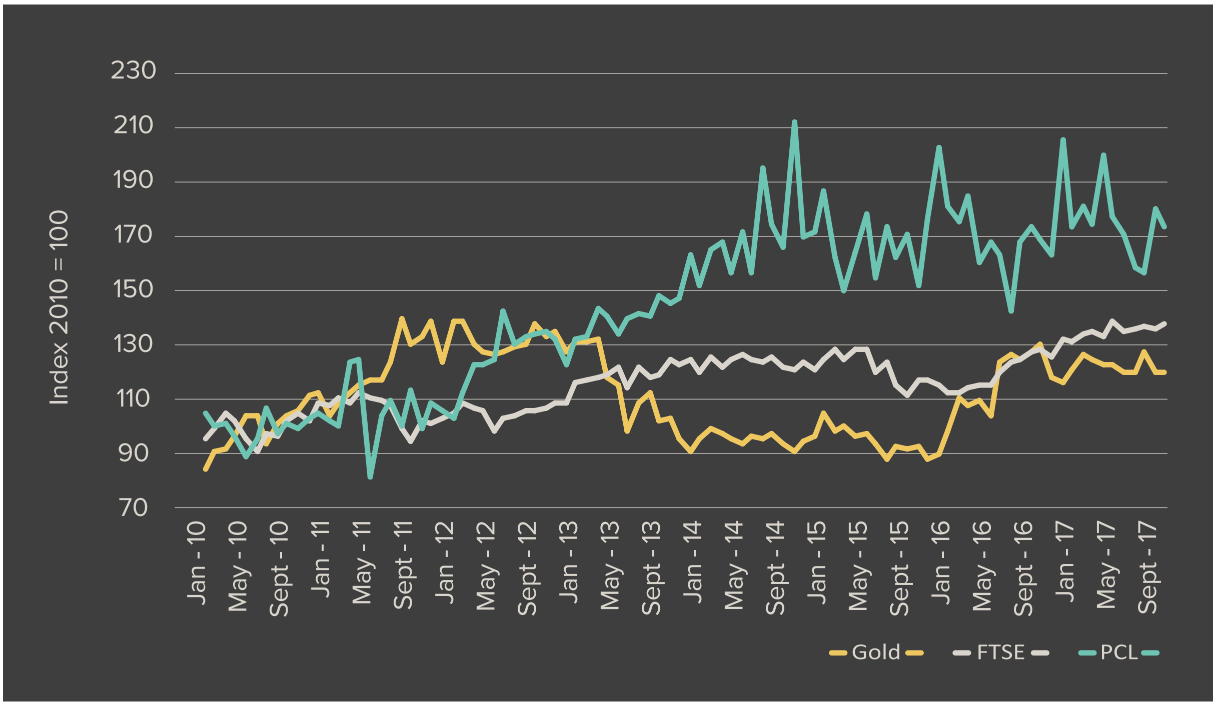
Prime London Property vs Other Assets



Source: WGC, HMLR, FT

"The proposed exit from the European Union has influenced the pace of capital growth."

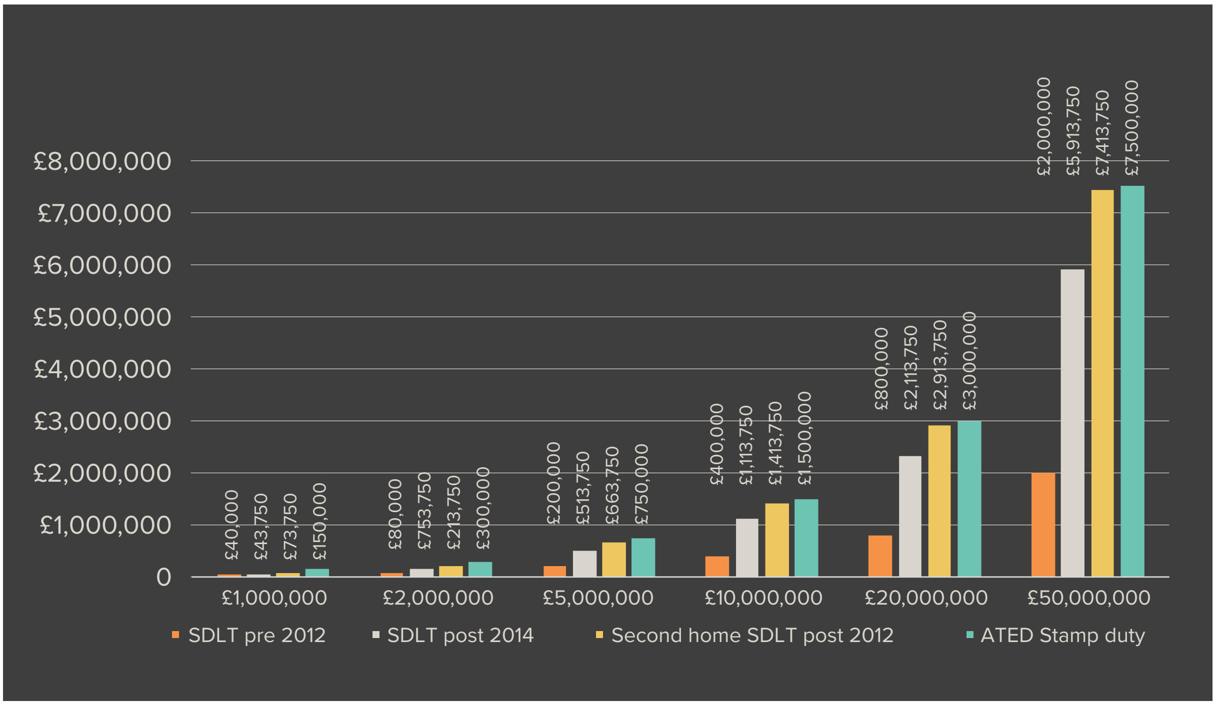
Recent changes to UK property taxes and the prospects for the UK economy as it negotiates its exit from the EU have also influenced the pace of capital growth in the prime areas of the capital. And, they are also affecting expectations of future capital gains.

The raft of tax changes that hit the most expensive homes and company purchases hardest changed the investment sums, too. Additional costs of buying have been factored into purchase price negotiations. On top of that, the new supply of luxury property coming on stream added to weakening expectations and price negotiation. The below chart shows how the amount of transaction tax paid by buyers has increased over time and by property value and ownership.

While it is true that overall property taxes in the UK rank highly in the Organisation for Economic Co-operation and Development averages, the comparison is not straightforward since the structures of tax in different counties make like-for-like comparisons almost impossible. Most UK property tax is raised from sales of property, while annual property taxes are very low. In other countries they are much higher and wealth taxes can also play a large part in the cost of investing in and owning property.

Comparing costs similar to stamp duty, i.e. up-front purchase taxes and fees to the government, shows the UK is relatively highly taxed but its annual charges are much lower. In Hong Kong, annual property charges are as high as 15%, while

Change in Stamp Duty Charges



Source: Hamptons Research, HMRC

in the UK these add up to less than 2%. New York and Paris also charge significantly higher annual property taxes. This is important to bear in mind when investing for the longer term.

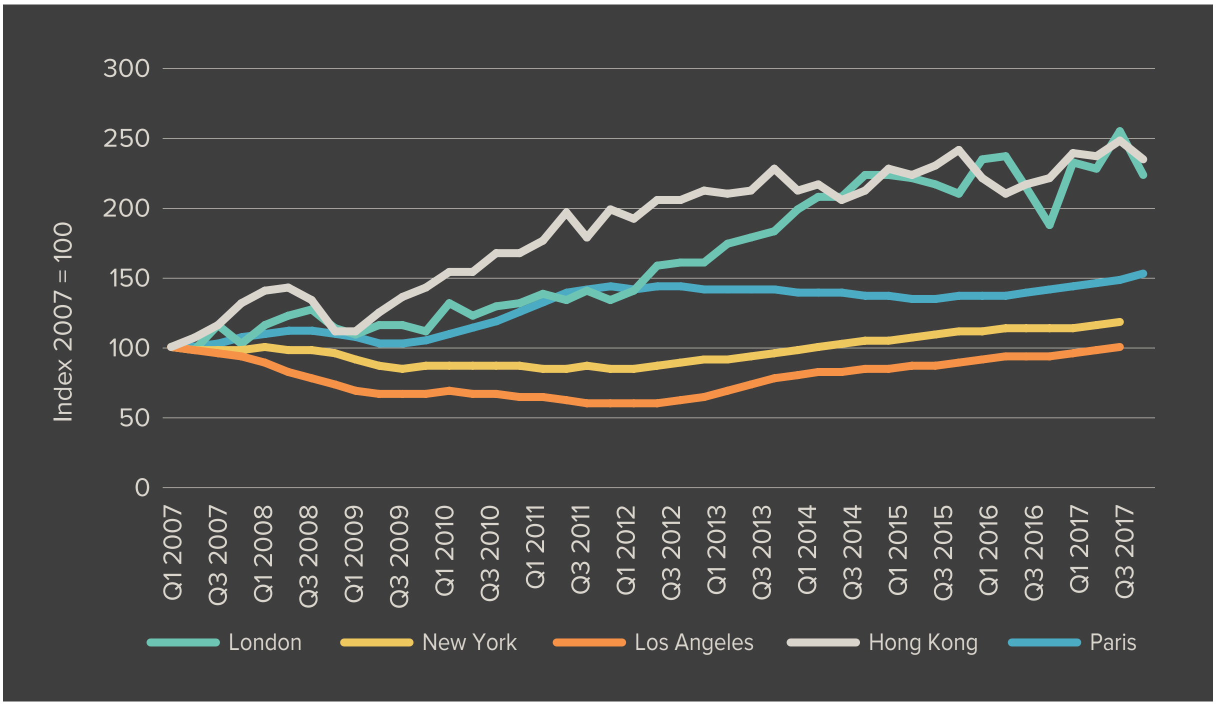
Even taking tax changes into account, property price growth in London's prime markets compares very favourably with other attractive 'global' cities.

Government Tax on Equivalent £5,000,000 Purchase

	HK	UK	Paris	New York
Purchase Price	HK$53,000,000	£5,000,000	€5,654,765	$6,700,000
Government Tax	HK$20,405,000	£663,750	€340,140	$189,275
	39%	13%	6%	3%

Source: HMRC, Notaires de France, Homenet HK, RealDirect

Major Global City Prime Growth, 2007 - 2017



Source: Hamptons International, HMLR, Insee, USFHA, HK Govt

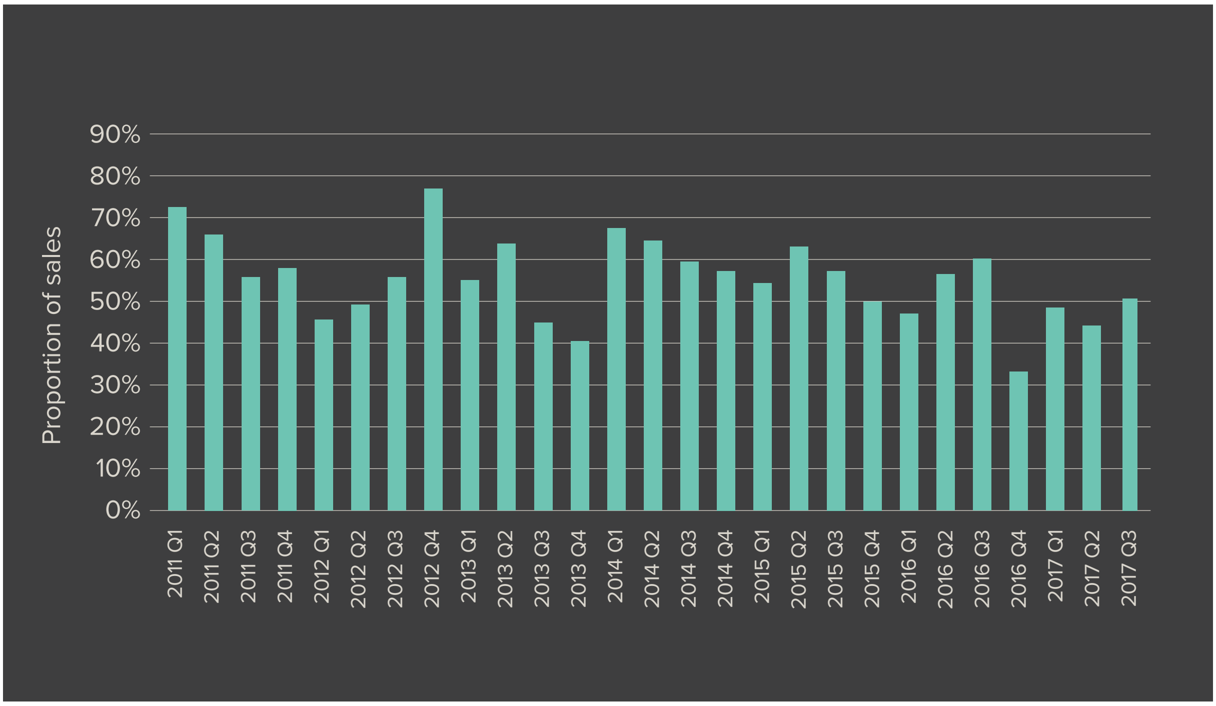
Uncertain Times

Where is the risk and what are the opportunities?

Looking ahead there are a number of risks and opportunities for prime property. Leaving the EU brings uncertainties about the UK's economic performance and the impact on property values, but also the effect of changes in the currency on the value of overseas investments. Yet the exclusivity of the best addresses in London and its place as one of the world's most prestigious cities are still big draws. This helps prime property to hold its value better in tough times and to increase in bull markets, which are big attractions for investors. Furthermore, just as London's property markets experienced significantly increased interest during the euro currency crisis in 2012, leaving the EU may once again cause investors to see the UK as an alternative and attractive haven for funds.

Uncertainty about the UK leaving the EU is adding to nerves but our latest data from Hamptons International reveals the proportion of prime central London property bought by international buyers still accounts for over half of all sales, despite concerns about Brexit and higher taxes. In Q3 2017, the proportion of prime central London property bought by international buyers reached its second highest level since the EU referendum. International buyers accounted for 51% purchases in London, up from 44%

International Buyers in Prime Central London (%)



Source: Hamptons International Research

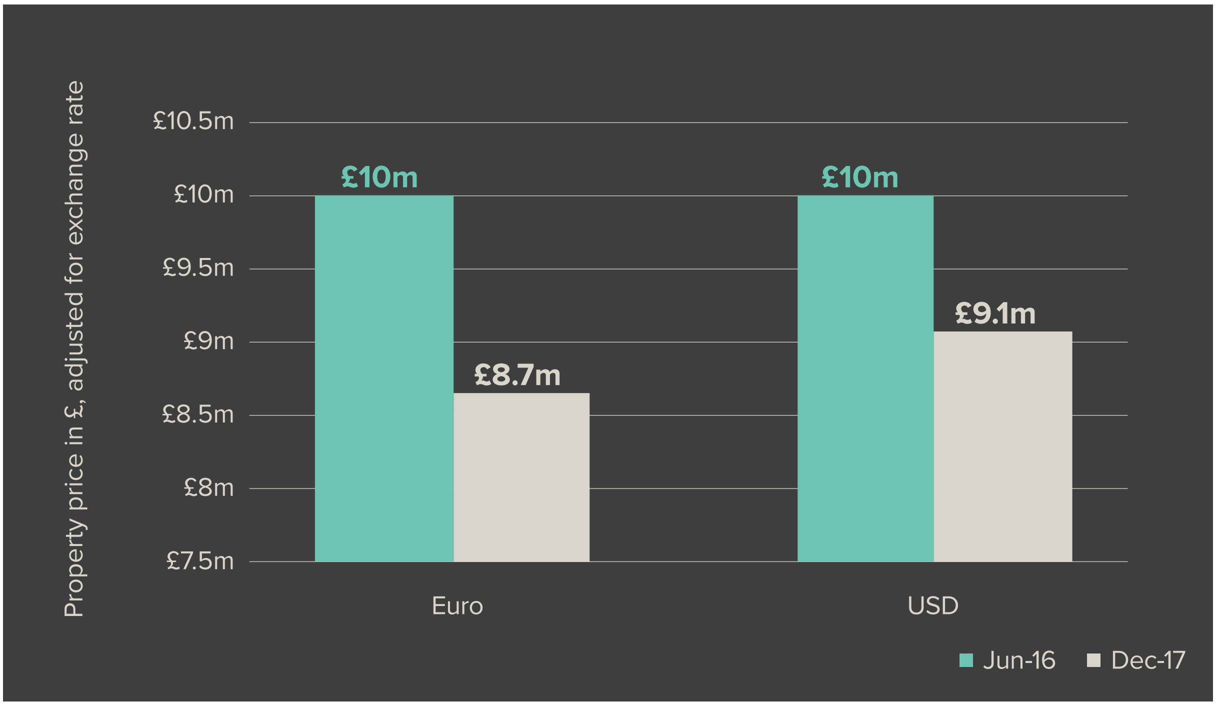
> "The fall in sterling has neutralised the effects of higher stamp duty."

in Q2 2017.

Part of the reason why overseas buyers are more active in the market is the exchange rate. Sterling fell sharply against the US dollar and the euro when the UK voted to leave the EU. As of December 2017, sterling was still 9% down against the US dollar and 13% down against the euro.

Investors face higher stamp duty on more expensive property, a 3% surcharge on additional property and higher charges for property purchased through a corporate entity. The fall in sterling neutralises some of the effects. The total buying cost of a £10m home (excluding legal fees and assuming the purchase is by an individual rather than a company) would be about £1.5 million, assuming it is a second residence. However, the savings due to the currency mean an overseas buyer wanting to buy a property worth £10 million in London gets an effective discount of £938,000 if buying in US dollars or £1.34 million if buying in euros, compared with June 2016.

Effect of Currency on Price of £10m Home



Source: BoE, Hamptons International

Outlook

The outlook for London's prime markets is positive, although it may not be sparkling in the short term. However, the supply issues and continued desirability of the capital as a place to live and work as well as hold property will support its recovery over the long term.

Low and volatile sales volumes in prime markets make point forecasts particularly difficult, but we expect the official Land Registry data to show an average 1.5% increase in 2018 after an average expected fall of 3% this year. The average 1.5% increase, however, masks sharper falls in some sectors of the prime market. We expect the 'feel' to be of a continued downward adjustment over the next 18 months, but for recorded prices to rise in the order of 1.5% in 2018.

House Price Forecasts

	2016	2017 (F)	2018 (F)	2019 (F)	2020 (F)
GB	5.0%	2.8%	1.0%	2.3%	2.5%
Greater London	6.2%	1.5%	-1.0%	1.0%	2.5%
Prime London	3.0%	-3.0%	1.5%	2.5%	5.0%
Central London	6.0%	3.5%	0.5%	2.0%	3.0%

Source: Hamptons International

The Softer Factors

Choosing to invest or live in the more prime areas of the UK and London is not all about financial return. London has always been a city with international appeal. Its cosmopolitan nature and strong trade and cultural links with other parts of the world help to keep this strong. In addition, the country's clear and reliable legal system maintains business confidence in the UK. The political landscape may be more volatile than previously but the UK remains a stable democracy, which brings with it reassurance that there will not be a flight from the country.

Despite concerns about the UK's position after Brexit, the surveys of confidence in the UK remain strong. A recent attitude survey in the 2017 Wealth Report highlighted and ranked the factors most important to high net-worth individuals (HNWIs).

The UK performs well in each category and better than New York, Hong Kong and Paris in most areas. Indeed, Forbes rates the UK as number one in its assessment of the best countries for business despite the concerns about the implications of Brexit for the UK economy and the ability to do business here.

However, as security becomes more of a concern for citizens, it is unsurprising that it is highly valued by wealthy people. London scores well here too. The Economic Intelligence Unit rates the UK at number 15 overall – above Paris at 31 and New York at 25. London is in the top 20 of all cities in each of the categories of infrastructure, health and personal security.

Also, the UK is famous for the quality of its education, in its schools and its universities. UK independent schools appeal to parents around the world, not just for their academic achievements but for the range of creative and cultural opportunities available. The University of Oxford and The University of Cambridge are revered across the globe and many other UK universities are leading research institutions, with worldwide reputations for excellence. UK independent schools score more than twice as highly as the average for OECD countries with more than 24,000 children with parents overseas being schooled in the UK.

London has always scored well on its cultural and historic platform and continues to outpace other major global cities.

London performs well on transport, too. Getting around the world from its airports and rail terminals is relatively easy, while improvements to its transport infrastructure include the new Elizabeth Line and new trains and station refurbishments.

Most Important Factors for HNWIs

		Paris	**Hong Kong**	**New York**
	Rank (out of 10)	Ranking relative to London		
Lifestyle	8.2	–	+	+
Personal Security	8.2	–	+	–
Education	7.5	–	–	–
Healthcare	7.1	+	–	–
Transport Links	6.9	–	–	–
Business Reasons	6.8	–	–	–

Source: The Wealth Report Attitudes Survey; Forbes, Mercer, EIU, AT Kearney, NJ Med