WMG

WMG Advisors LLP

REAL ESTATE NEWSLETTER

2020 Year Ahead

WMG Real Estate

Objective:

WMG, acting as principle together with its investors invest in London Real Estate, for capital appreciation as well as yield. It aims to return more than 15% IRR.

Dear Investor,

The Real Estate sector, specifically London Real Estate, has been revived following the election results. London is in a far better shape this year than the previous three years. The conservatives, led by Boris Johnston, won a clear majority, allowing the government to finally pass Brexit as law. The European Parliament has voted and supported the Bill. The devil is of course in the detail and that is to come over the next twelve months. Negotiating a new commercial relationship with Europe will not be easy and there is still the question of the Irish Border. The sterling is going to fluctuate as sentiment changes one way or another, trading between 126 and 140 against the dollar. Spite these difficulties there is optimism in the current economic climate. One thing for sure, Britain did not vote in a Labour government, especially one led by Jeremy Corbyn; who would have attacked the property market with wide ranging reforms to taxation and changes to laws for landlords.

Confidence is back, with forecast of house prices rising from one percent to as much as ten percent in 2020. Chinese investors have broken the highest paid price for a UK property, paying 200million pounds for a mansion on Rutland Gate in Knightsbridge. This is seen by many as evidence that London's prime property market is recovering. In previous newsletters we have argued that the London residential market fell into two categories, prime and affordable. We have for the last two years been focused on the latter and stayed away from the former. Conservative majority, Brexit done, we are now beginning to feel more comfortable with the prime market.

Election results and Brexit are not the only reason why London is looking at recovery. They are the catalysts. Boris Johnston's tenure could see the beginning of a rejuvenated London, with economic growth back on track, low interest rate and an attractive entry level for foreigners investing into sterling assets. For US dollar investors; London residential prices represent a discount of 38 percent, from its peak in 2014. That's depreciation and sterling weakness together. In addition to these two factors, you have a scenario where the interest rates will remain low. In fact, Bank of England is under pressure to lower when in November we saw the UK economy contract by more than expected. With low interest rates and the pound trading below 1.30 against the US dollar, London residential estate offers real value.

The IMF forecast's a modest pickup in global growth from 3% to 3.4%. There are many global factors which could affect this forecast, with the USA/China dispute in the forefront and the impact of the Coronavirus still unknown. Here in the UK, Bank of England cut its forecast as recently as 30 January, predicting 0.8 percent for 2020, 1.5 percent for 2021, and 1.75 percent for 2022. Clarity on political decision making, Brexit finally done, low interest rates, and economic growth has changed the appetite for London real estate from one of pessimism to optimism. The biggest beneficiary of the macro picture improvements is the London office space, which is particularly "…sensitive to underlying economic growth…driven by pick-up in business investment and major fiscal easing.

"London office stocks have already rallied…as demand for UK assets recovers, and where our economists see a return to two percent GDP growth by 2011." A recent report (28 November 2019) by Morgan Stanley wrote. This prediction is based on expectation that the economic growth will continue to accelerate. Real estate investment is still attractive both on a global basis and more specifically in London, for all the reasons we discussed above. Office space and residential has had the biggest growth in terms of volume in 2019. Savills recently, in January declared "there is pent up demand waiting to invest in real estate – in many cases beyond the core assets.

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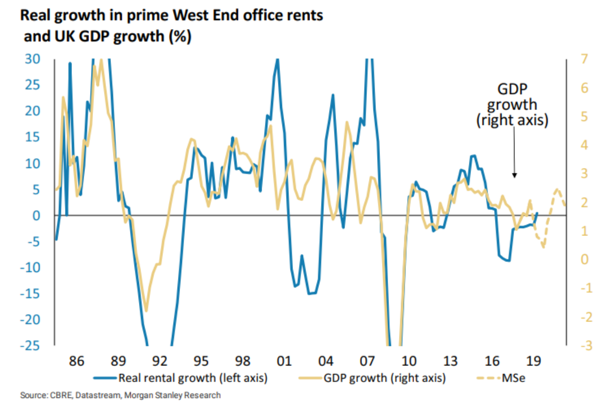
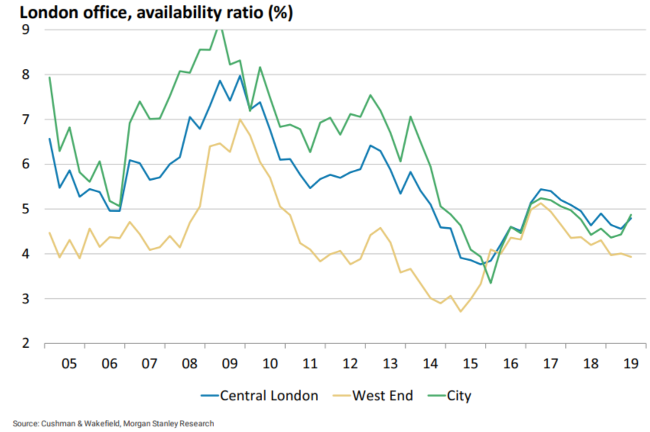
Sources: *ONS, **Avison Young, +CBRE and ++JLL

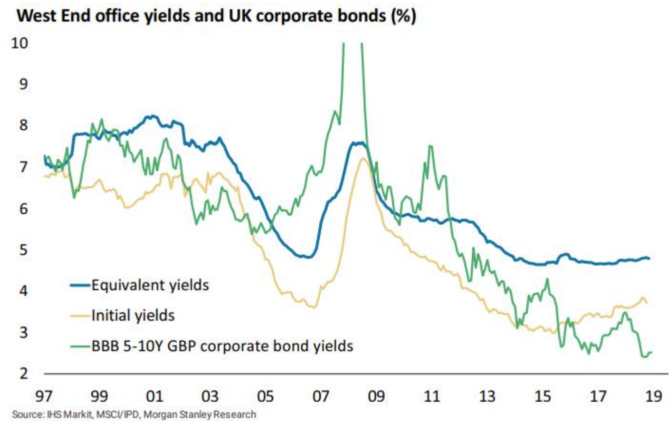
UK GDP growth is a key macro factor when forcasting Londonrental value growth. Our economists see a return to trend growth from mid-2020, driven by a pick-up in business investment and fiscal easing.



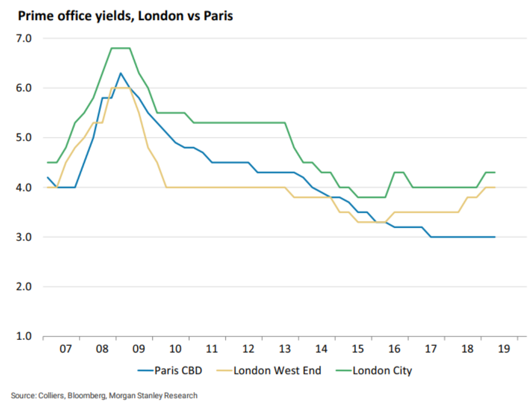
But low availability is supporting rental market pricing.



Low bond yields likely to keep downward pressure on property yields



Prime office yields in London's West End have moved out around 100bps relative to Paris in the last 5 years.



Source Savills Research using RCA, Note 2019 data year to November

In summary, London Real Estate once again looks attractive to investors. Our recommendation is to invest in office space, residential, logistics and avoid retail. With tenants demanding shorter leases and rents falling, retail will continue to be a challenge.

If you would like to discuss, or receive further information on either of these opportunities, please email: property@wmgfunds.com

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