

# Brexit: the UK referendum on EU membership

## Risks, possible outcomes and potential real estate market impacts

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Focused on the future of real estate

# Brexit: what's known

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- On 21 February David Cameron, the UK Prime Minister, announced that a referendum on EU membership will be held on 23 June
- In the event of a 'no' vote, the UK government would have to apply to leave the EU in accordance with Article 50 of the Treaty of the European Union. This gives the UK and the EU two years from the date of the application to negotiate an exit deal
- To investors, a crucial aspect of these negotiations would be the degree of access the UK retains to EU markets, and what trade agreements and treaties can be negotiated with non-EU countries
- A number of risks for investors have emerged following the referendum announcement:
  - Uncertainty over the referendum outcome
  - Uncertainty over the process for exit
  - Uncertainty over the substantive effects of exit
- The Conservatives: the Conservative government will campaign to remain in the EU, but cabinet members are permitted to support either side. Conservative Mayor of London, Boris Johnson, together with a materially significant number of Conservative MPs, are campaigning to leave the EU
- UKIP, DUP, and the rest: The seeds of the referendum were sowed by the formation of UKIP in the nearly nineties. UKIP and the DUP are the only notable political parties officially campaigning for exit. The Liberal Democrats and Labour both support remaining in the EU

# Upsides and downsides

## Sources of possible gains and losses from Brexit

Possible gains	Possible losses
Less regulation	Possible tariffs on exports to the European Union
Savings on European Union contributions	Loss of access to the single market
Ability to strike new trade deals	Damage to the City
Skills-based migration policy	Drop in investment caused by uncertainty

Source: Capital Economics, AEW Europe

# The Cameron deal: useful, but not decisive

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Concessions David Cameron was able to secure from the EU prior to the referendum announcement:

- The UK's "Special Status"
- The new unilateral "safeguard"
- Detachment from "ever closer union"
- Migrant benefits "emergency brake"

# Prior form

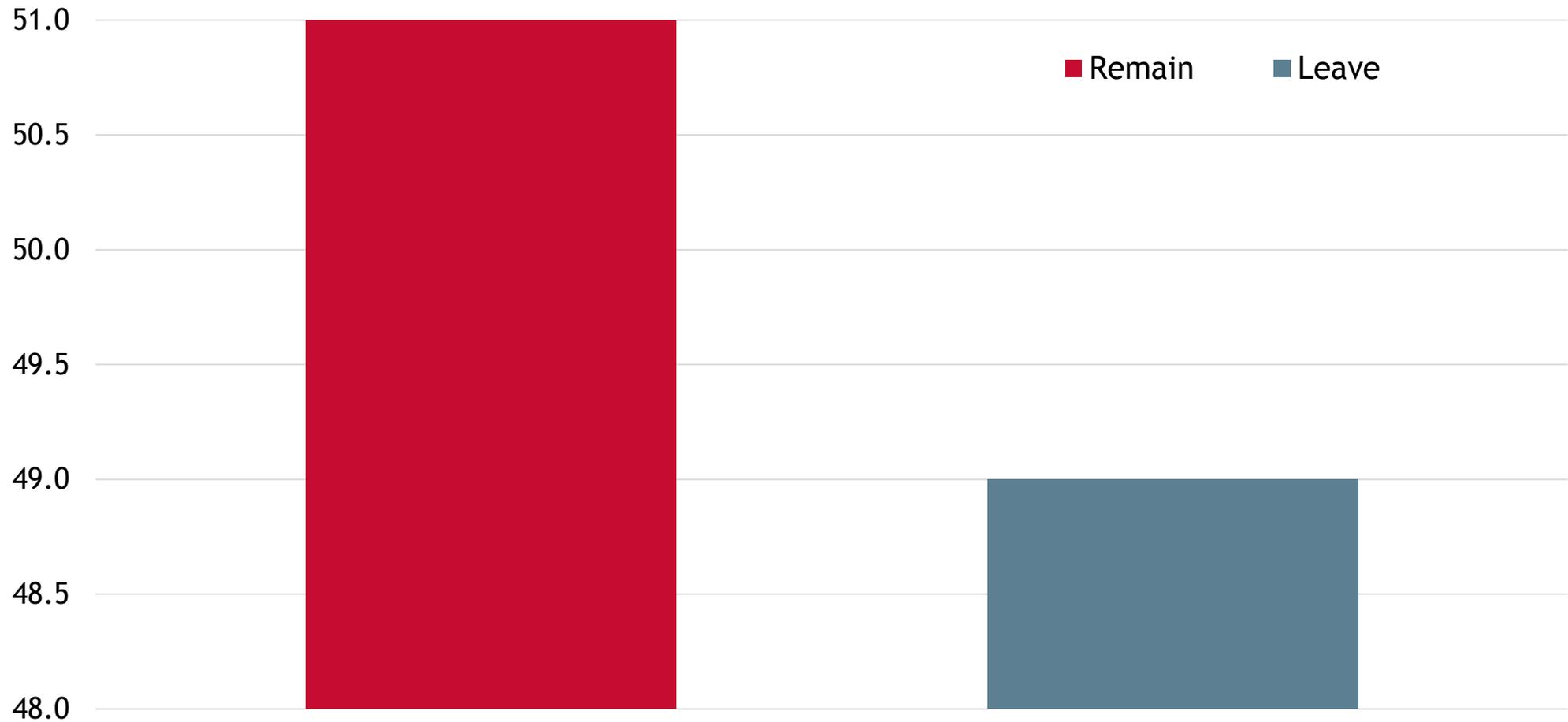
## Outcome of other comparable UK referendums

Question	Yes	No	Turnout
1975: UK to stay in the European Community?	67%	33%	65%
2014: Scotland to become independent?	45%	55%	85%

Source: BBC

# Too close to call ?

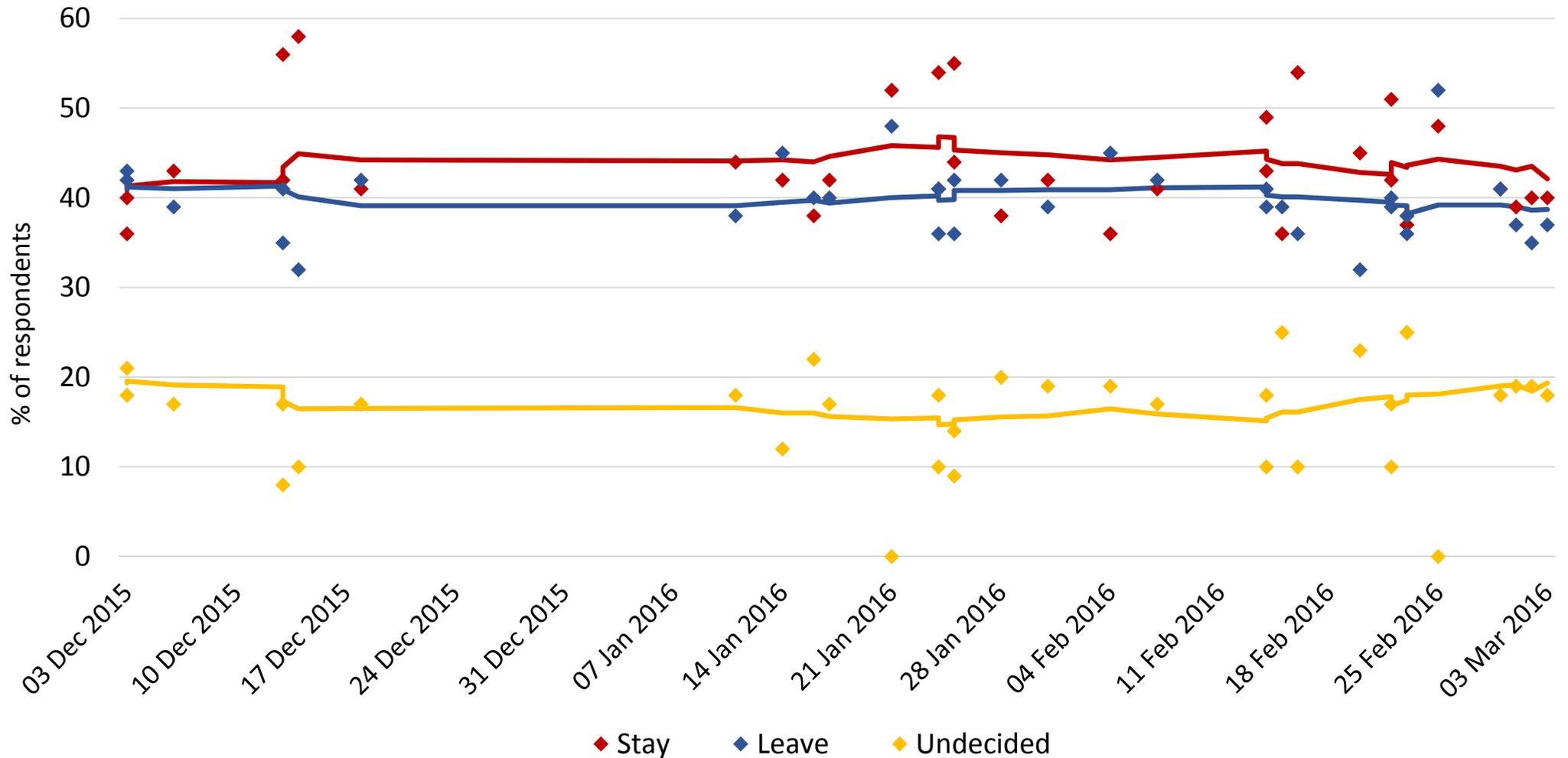
Should the UK remain in the EU ? (Poll of polls, as at 09 March, 2016)



Source: What UK Thinks

# The 'undecided' - kingmakers ?

## Opinion polls on Brexit

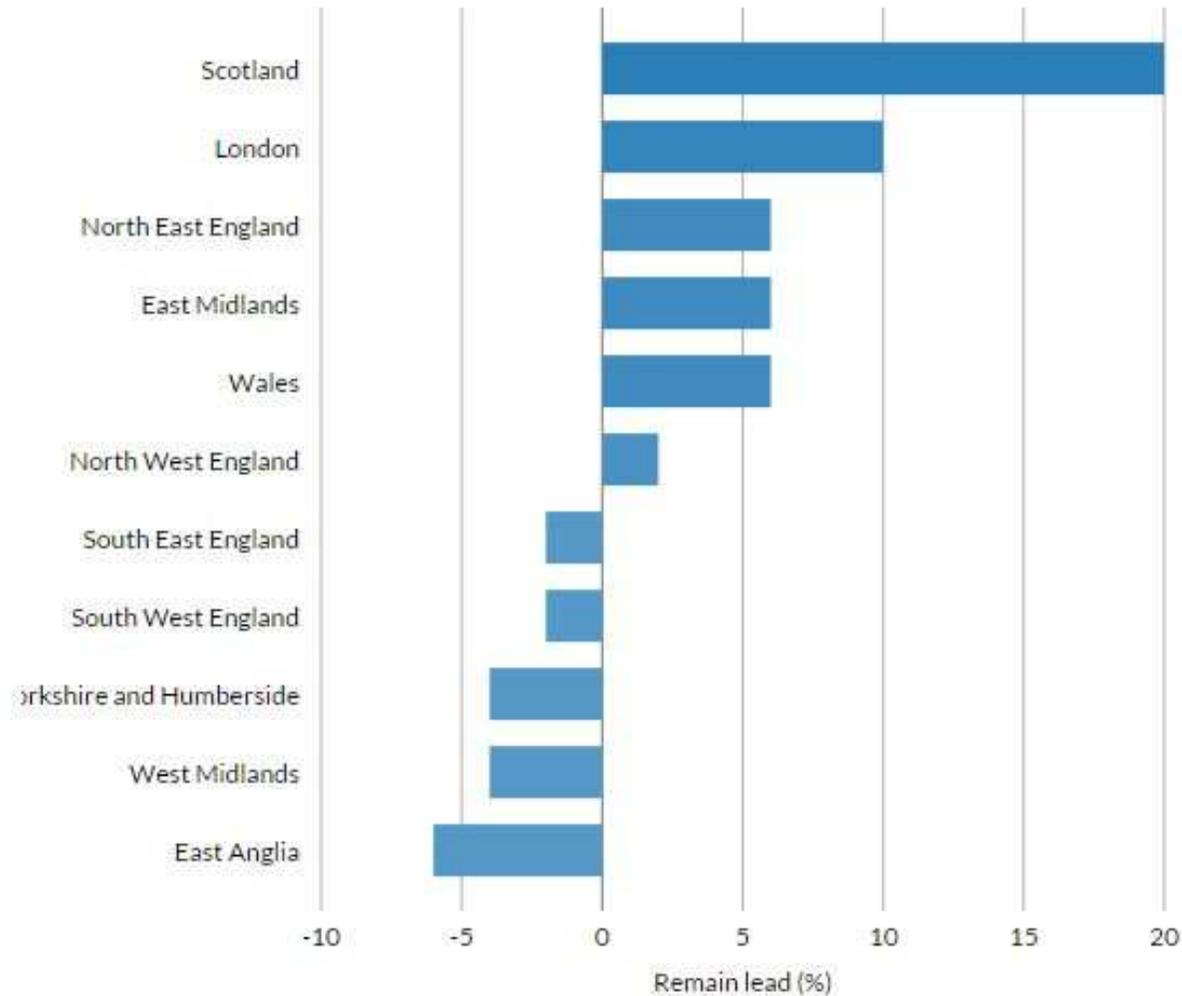


Source: Financial Times EU referendum poll of polls

\* Dots denote individual polls; lines show 10-poll moving average

# Geography matters

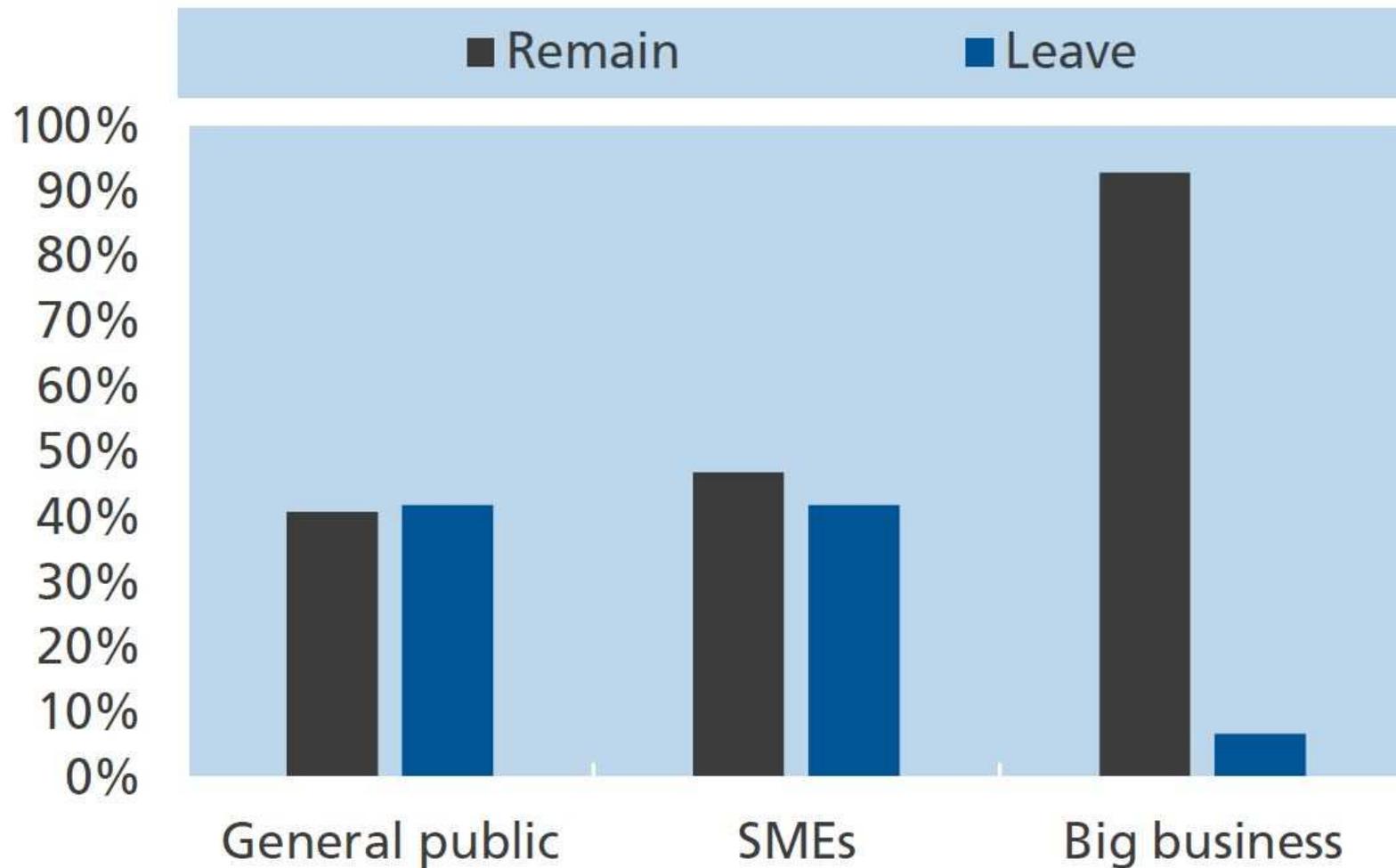
Lead of 'Yes' over 'No' among the regions



Source: *The Daily Telegraph*

# Size matters

Divergence of opinion between businesses and the public (January, 2016)



Source: LSR, YouGov

# Have the pollsters got it wrong ?

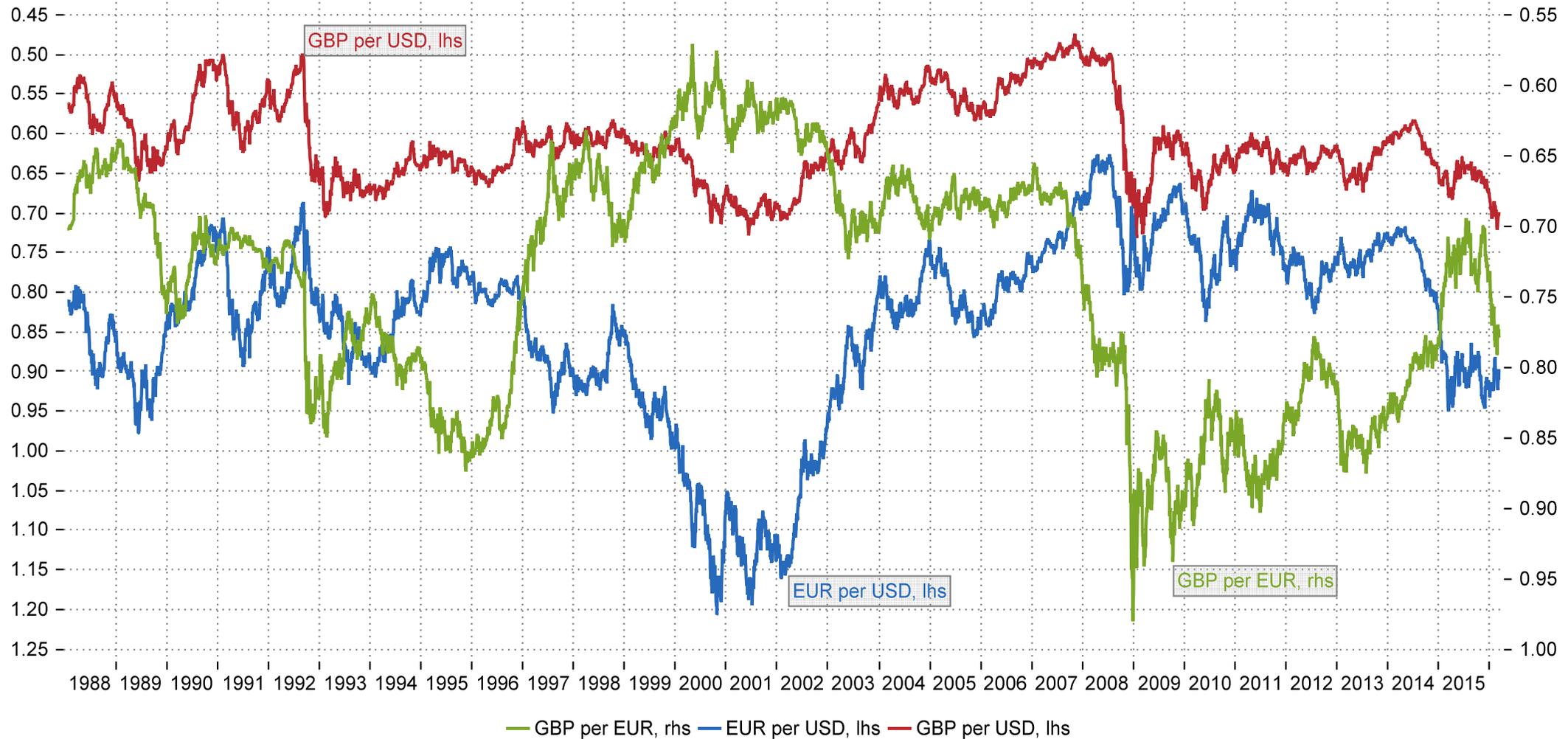
How the bookmakers see it: best odds

	1 December 2015		24 February 2016		9 March 2016	
Remain	<b>8/15</b>	65% probability	<b>2/5</b>	71% probability	<b>1/3</b>	75% probability
Leave	<b>7/4</b>	36% probability	<b>9/4</b>	31% probability	<b>12/5</b>	29% probability

Source: [oddschecker.com](http://oddschecker.com) \* Use of best odds from a variety of bookmakers means that probabilities do not add up to 100%

# Sterling first to suffer

EUR per GBP, EUR per USD and GBP per USD



Source: Macrobond

# Government bond yields still at very low levels

## Selected two year government bond redemption yields



Source: Macrobond

# Government bond yields still at very low levels

## Selected five year government bond redemption yields



Source: Macrobond

# Government bond yields still at very low levels

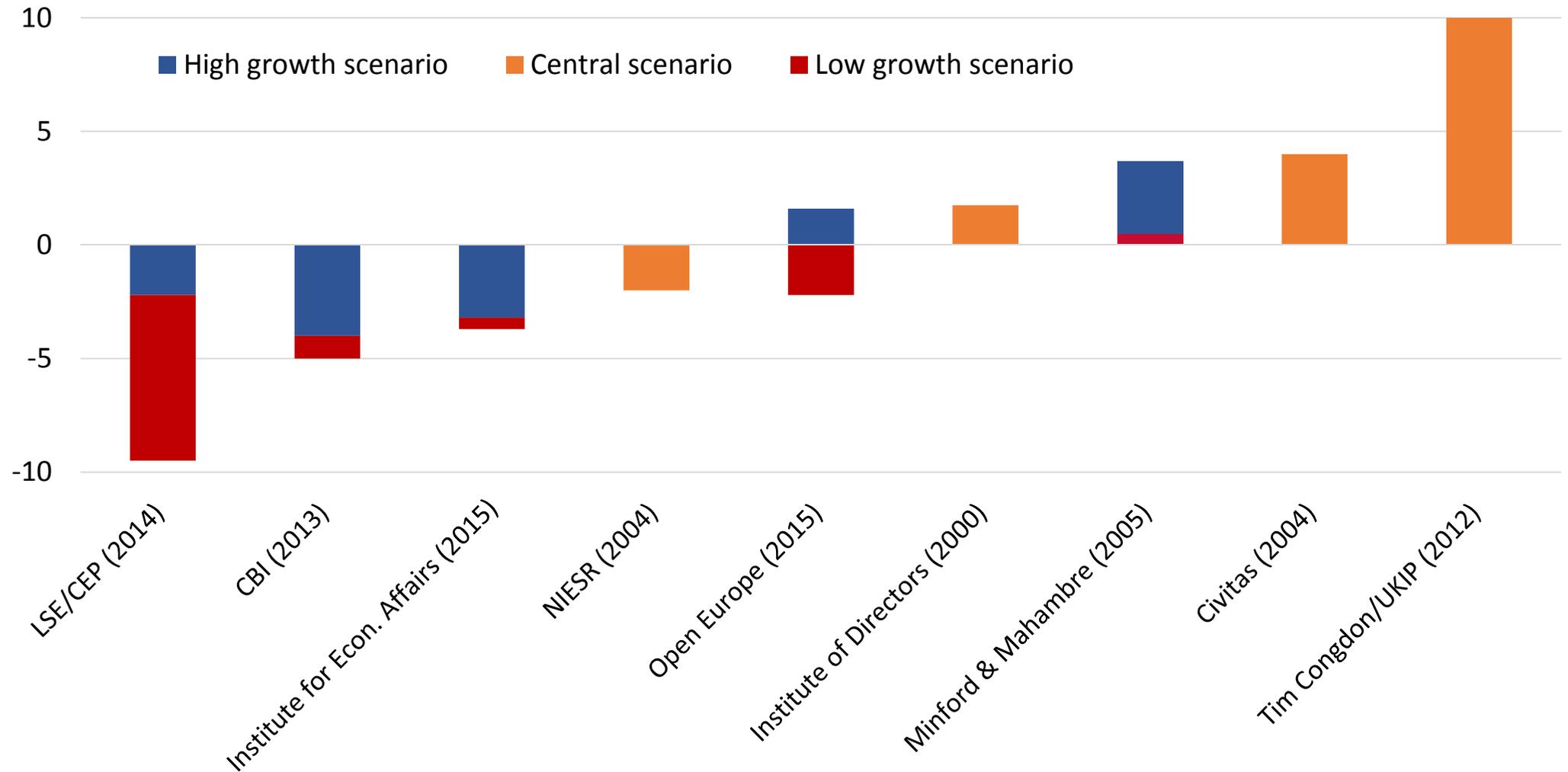
## Selected 10 year government bond redemption yields



Source: Macrobond

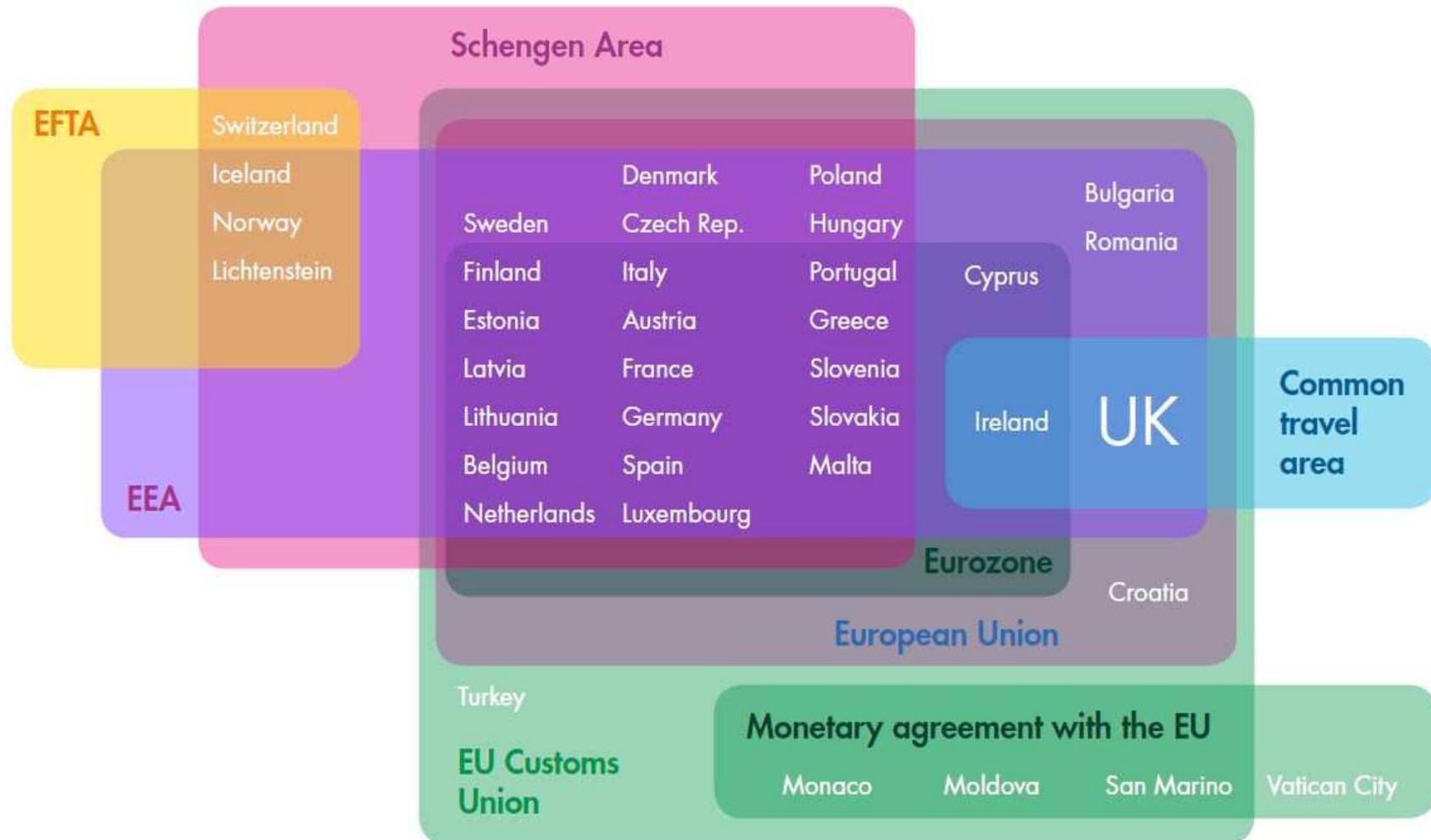
# Anyone's guess ?

Estimates of the impact of Brexit on the British economy (% GDP)



# Not just 'In' or 'Out' - other possible eventualities. . .

## Overlapping European relationships



Source: CBRE

# No free lunch

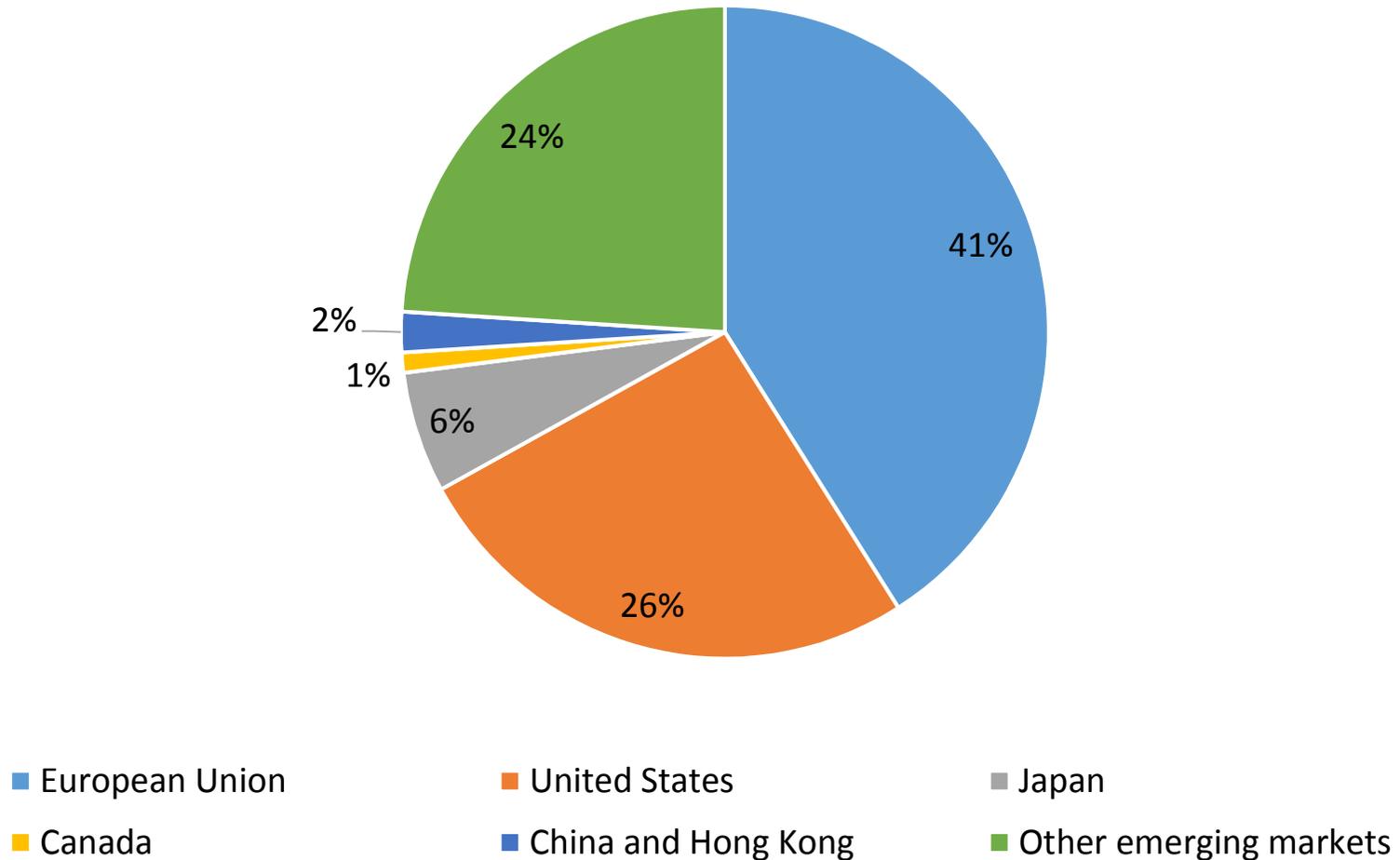
## Trade options: access or control - the trade-offs

	Tariffs on Goods	Full access to single market	Influence over EU Regulations Consultation, but No Voting rights	Control of EU migration	Contributions to EU Budget Yes - but a little smaller	Independent Trade Policy
EEA (e.g. Norway)	No	Yes		No		No
Bilateral Agreements (eg Switzerland)	No	No - Services excluded	No	No - but subject to Swiss Referendum	Yes - but significantly smaller	Yes - but subject to EU norms to access single market
FTA (e.g. Canada, South Africa)	No	No - Services excluded	No	Yes	No	Yes - but subject to EU norms to access single market
Customs Union (e.g. Turkey)	No	No - Services excluded	No	Yes	No	Yes - but subject to EU norms to access single market
WTO / Most Favoured Nation	Yes	No	No	Yes	No	Yes

Source: PMA, AEW Europe

# EU is a big market for the UK

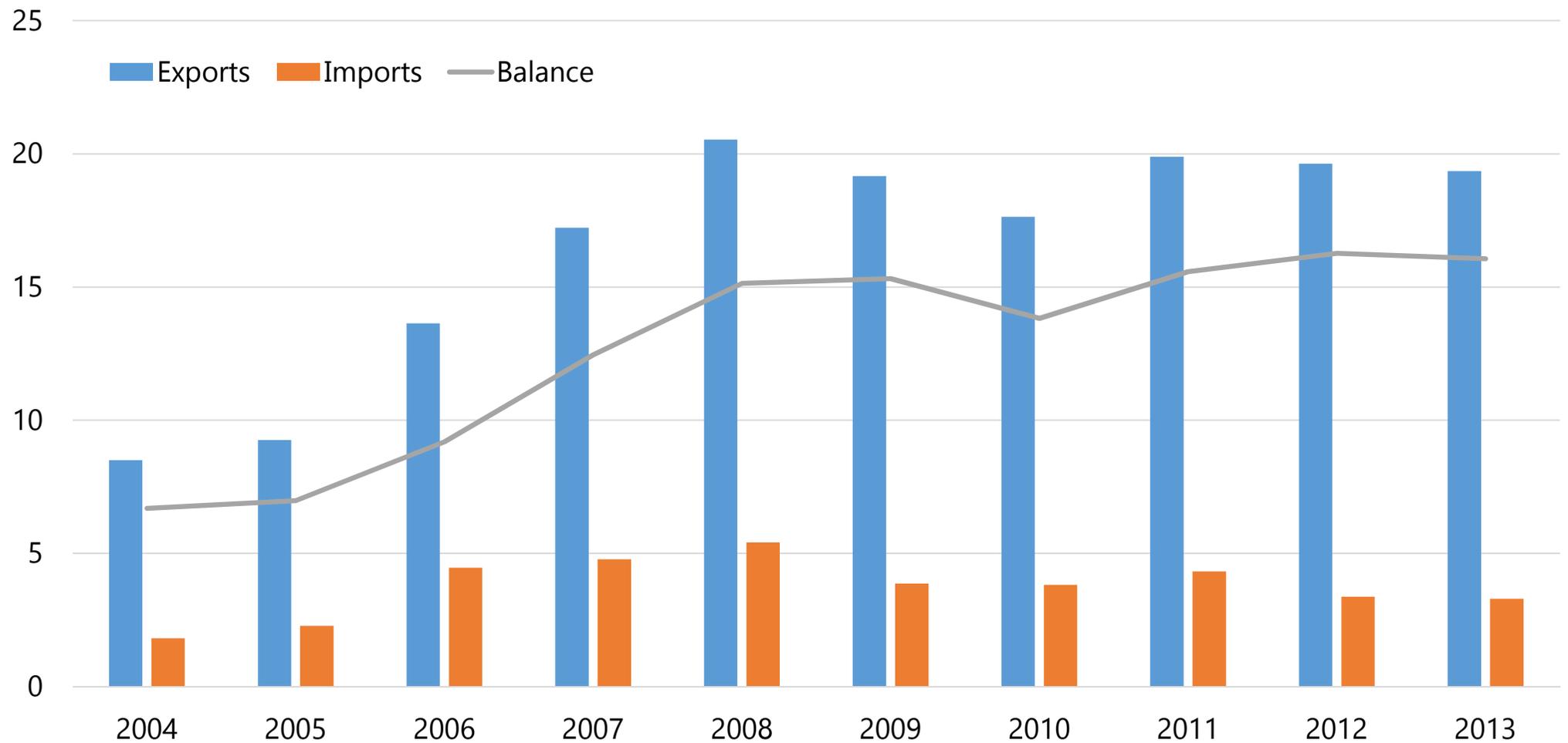
British financial services exports by destination (% share of total 2013)



Source: World Trade Organization, Capital Economics

# The imbalance that's a source of concern

British financial services trade with the EU (GBP billions)



Source: Thomson Datastream, Capital Economics

# Upsides and downsides

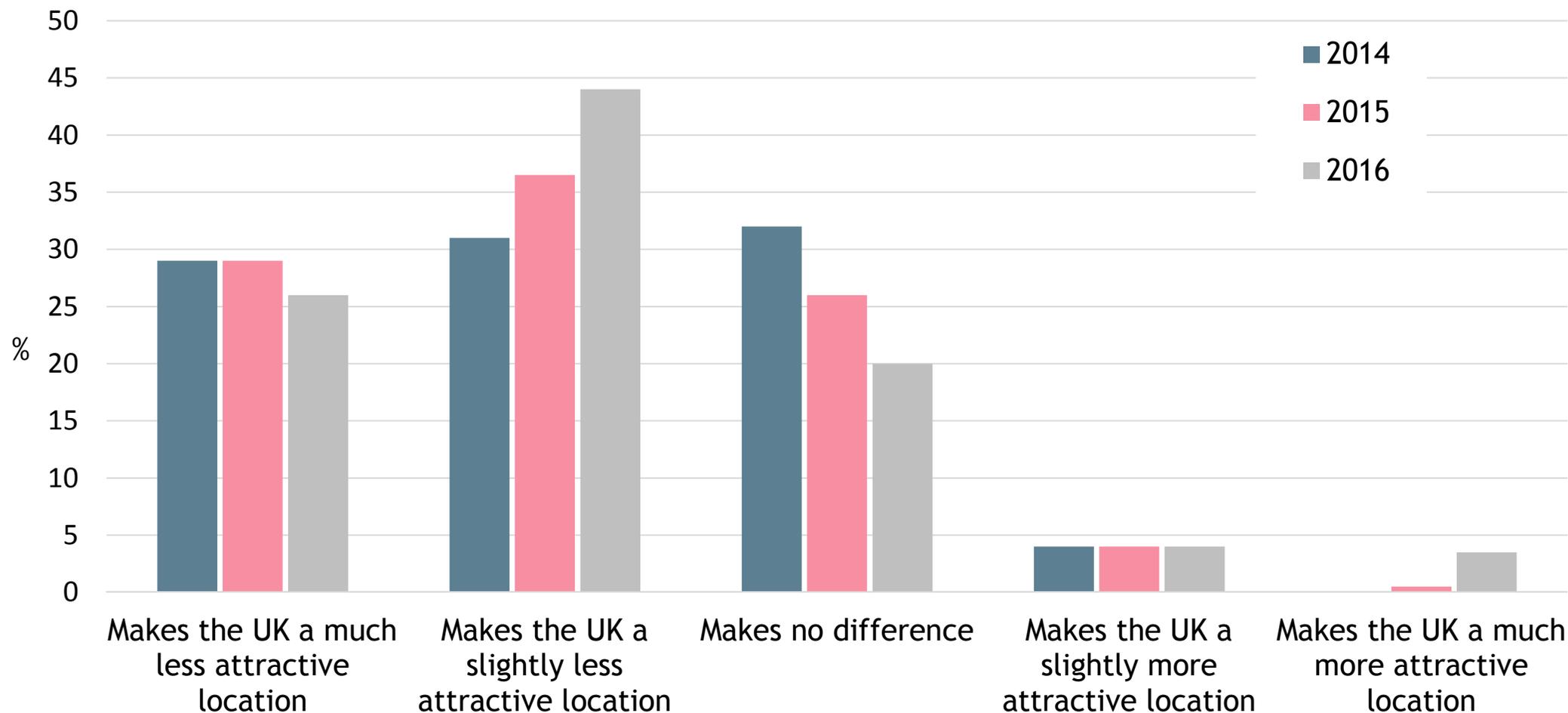
Main concerns of the financial services industry about leaving and staying in the EU

What are your main concerns for the future of the City if the UK decides to leave the EU?	What are your main concerns for the future of the City if the UK decides to remain part of the EU?
Loss of business to EU financial centres	Over regulation
Decline in international stature	EU becoming increasingly uncompetitive
Loss of influence on international policy	Declining influence of EU

Source: Survey of the Financial Services Sector's Views on Britain and the EU, CSFI, April 2015

# Perceptions over time

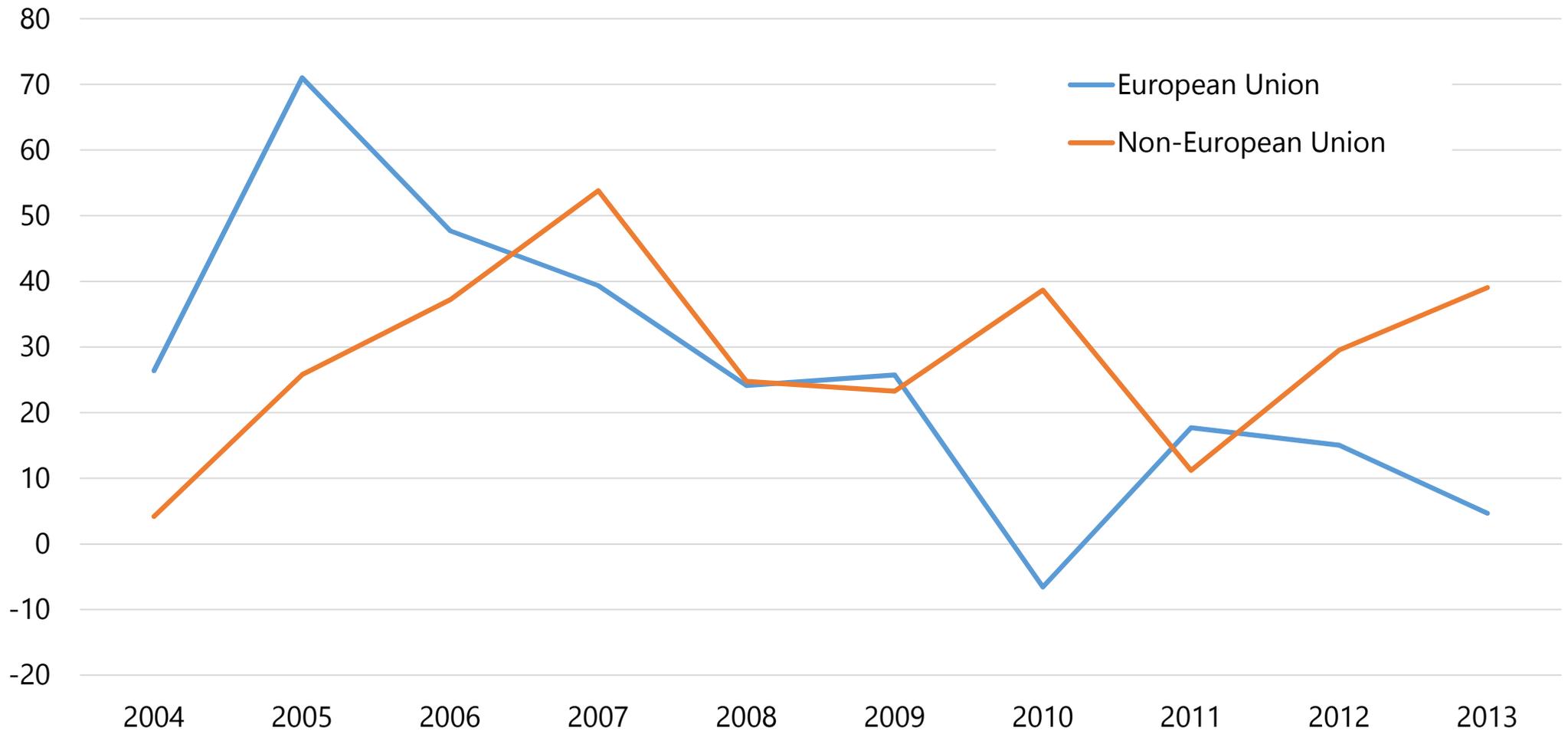
Property investor views on impact of exit on UK real estate investment (2014-2016)



Source: CBRE. The question asked was "How would it affect the attractiveness of property investment if the UK were to leave the EU" (2014: 385 respondents; 2015: 280 respondents; 2016: 191 respondents)

# How important is EU investment ?

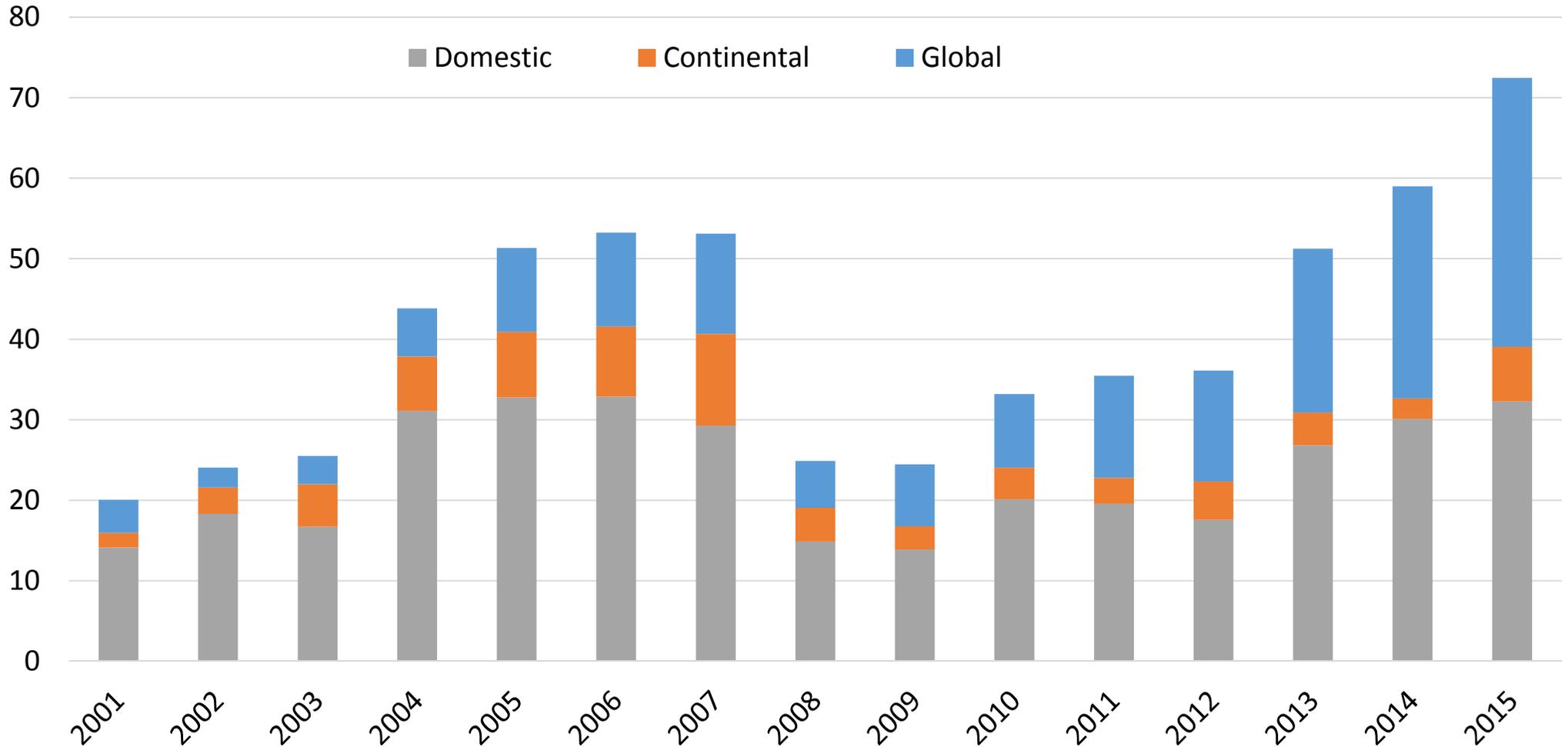
Foreign direct investment inflows into the UK (nominal, GBP billions)



Source: Office for National Statistics, Capital Economics

# UK investment activity now much higher than pre-GFC

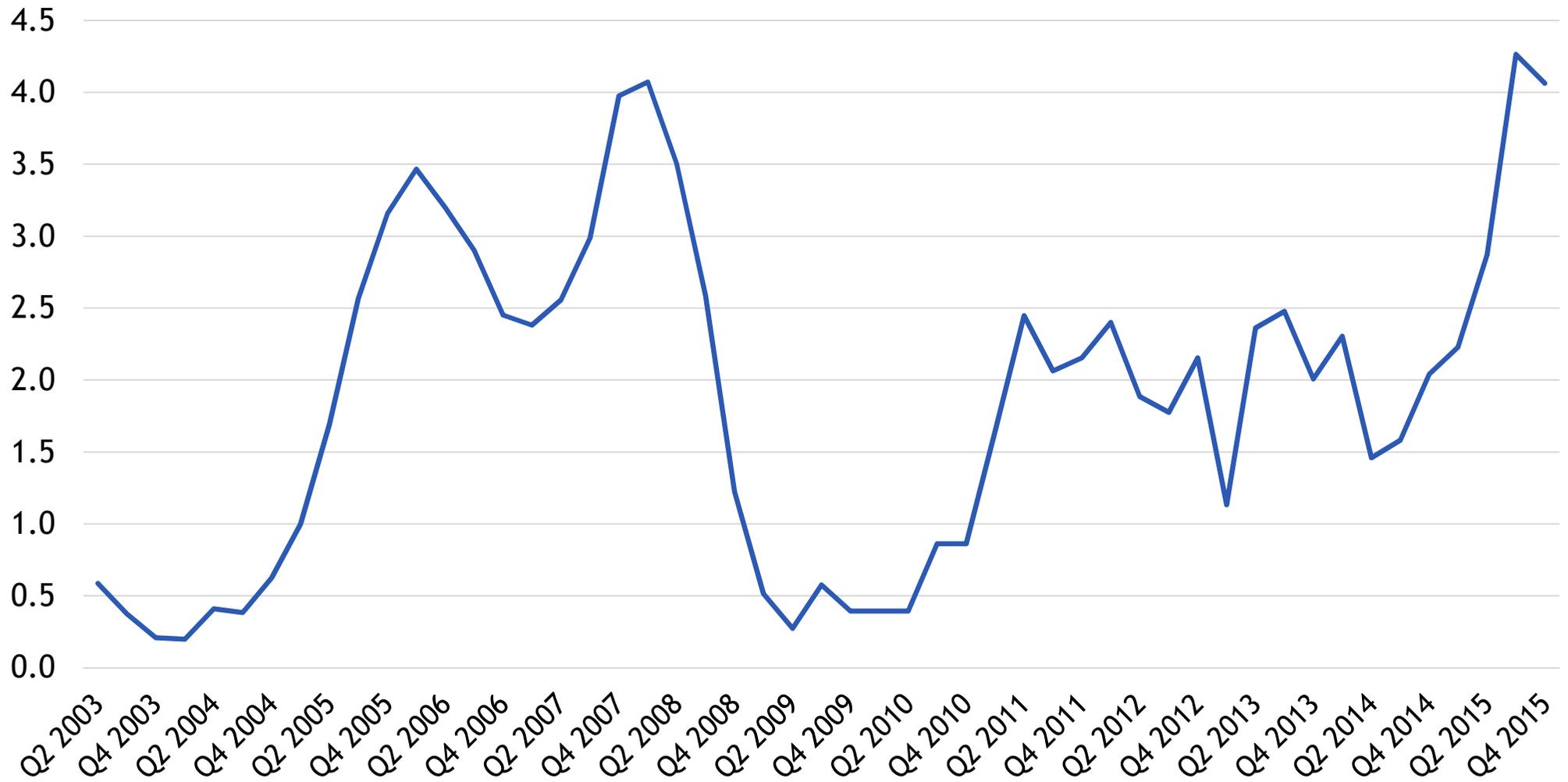
UK commercial real estate investment volumes (GBP billions)



Source: RCA

# Construction starts peaked ?

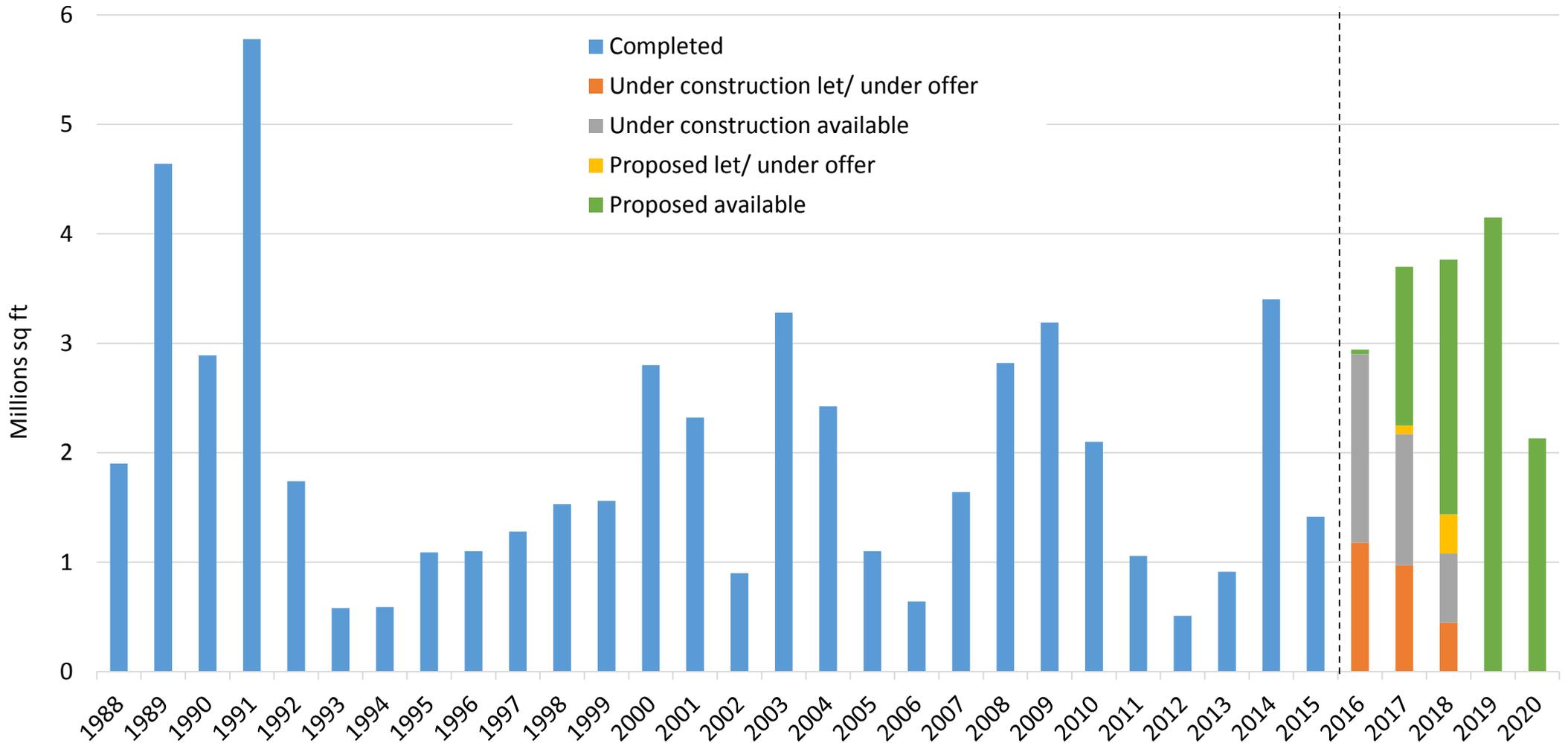
City office starts (millions sq ft)



Source: PMA

# 2015 development in short supply

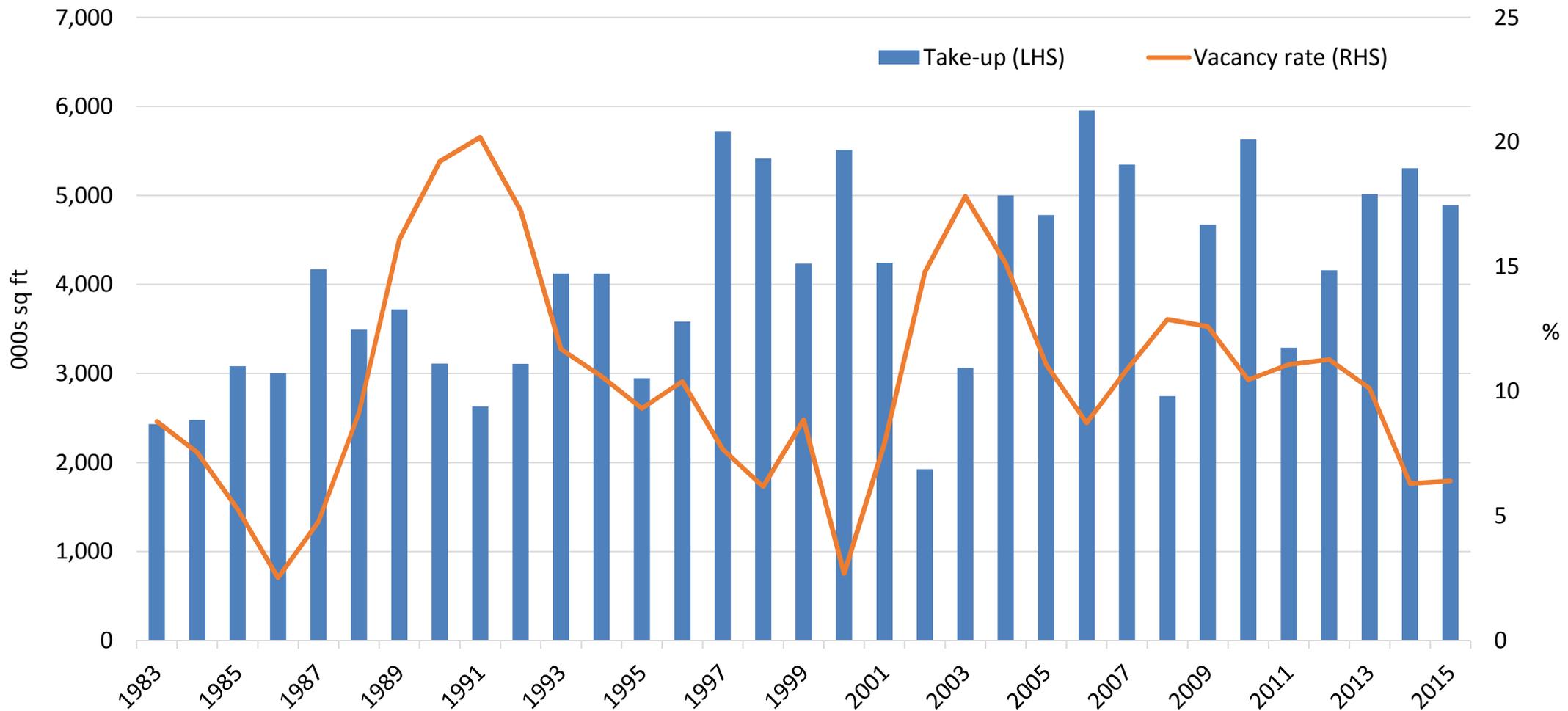
## City office development pipeline



Source: CBRE

# Vacancy rate at lowest level since 2000

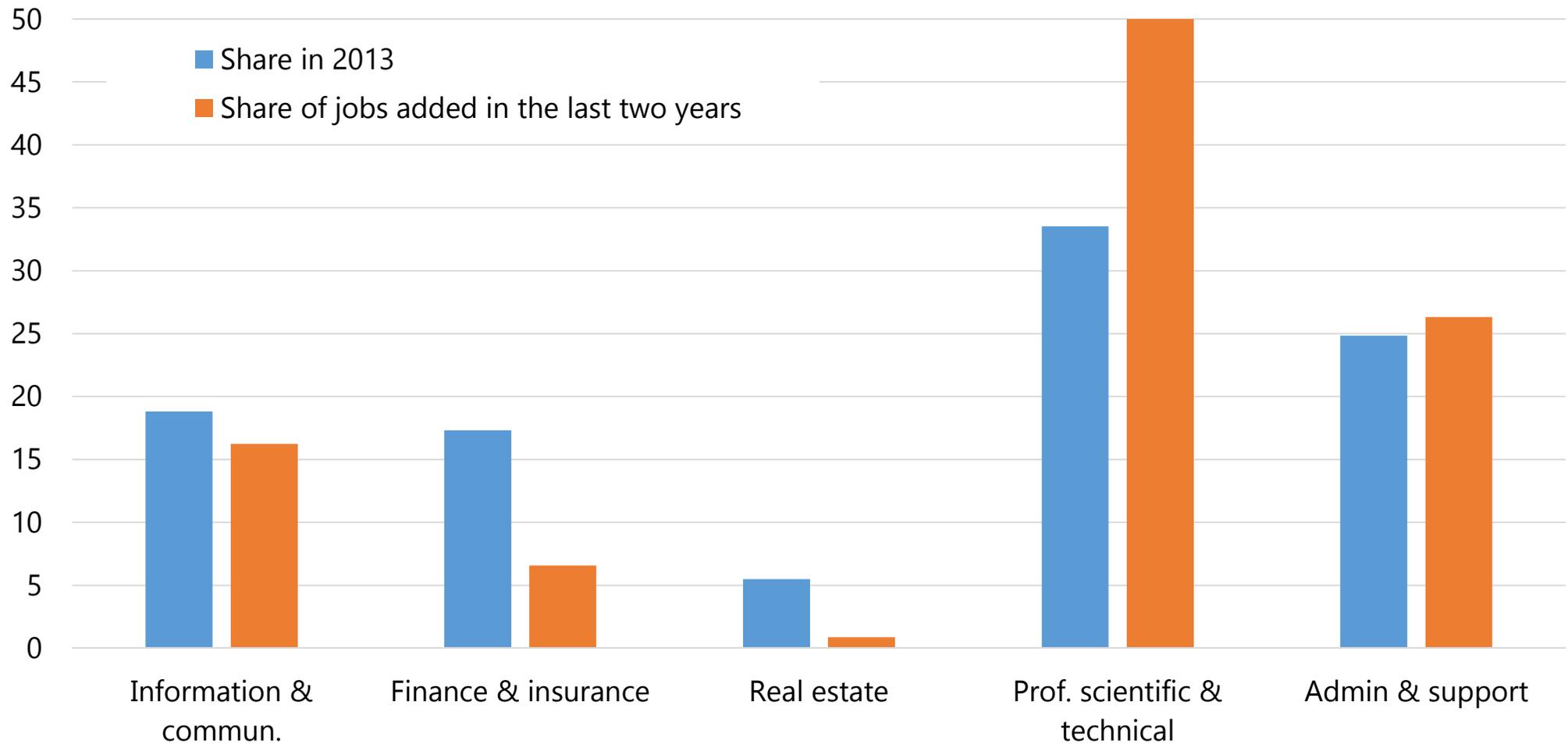
## City office take-up and vacancy rates



Source: PMA

# Financial services of lessening importance ?

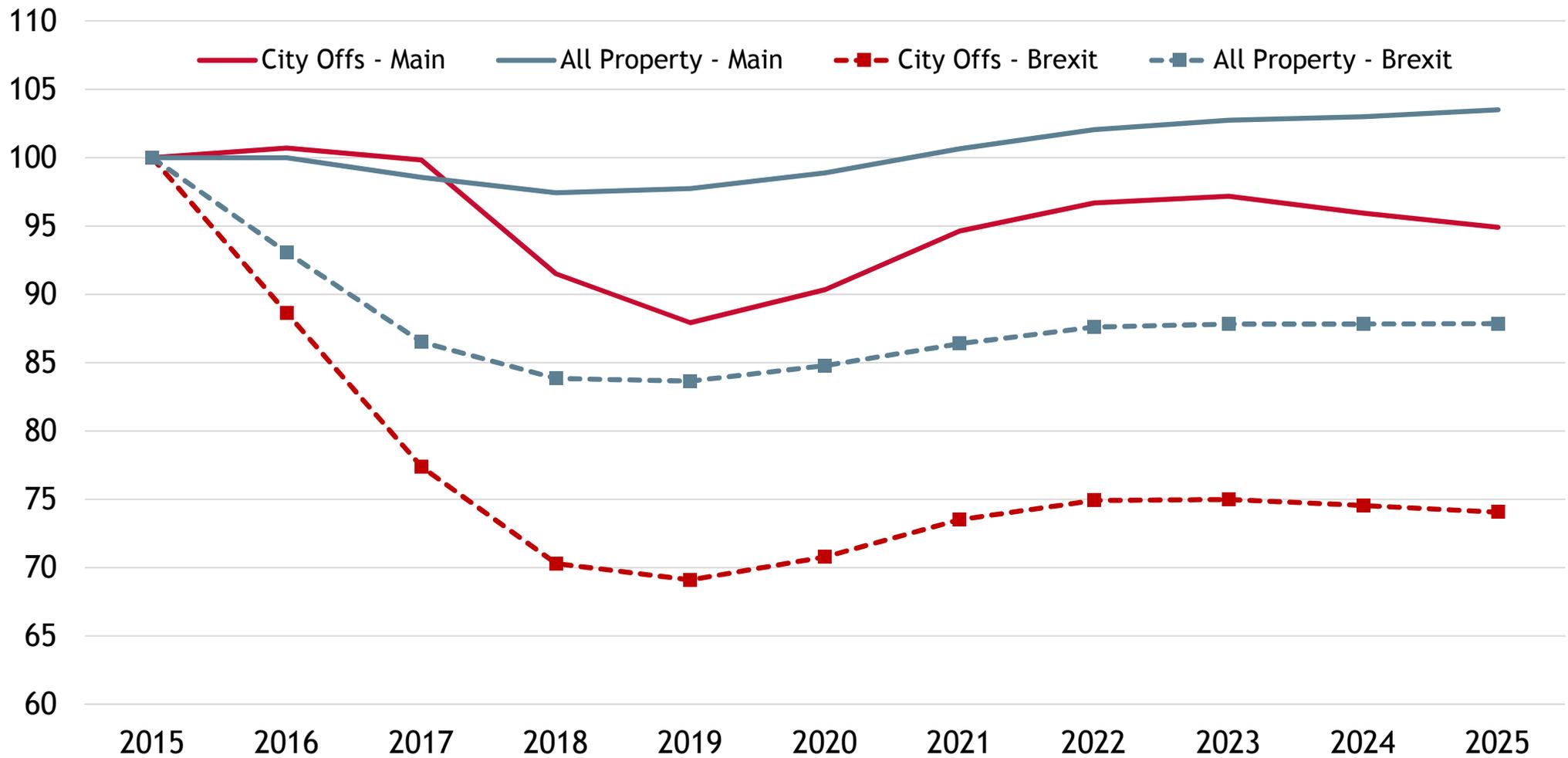
% of London office-based jobs by sub-sector (latest = Q2 2015)



Source: Office for National Statistics, Capital Economics

# London offices forecast to suffer most

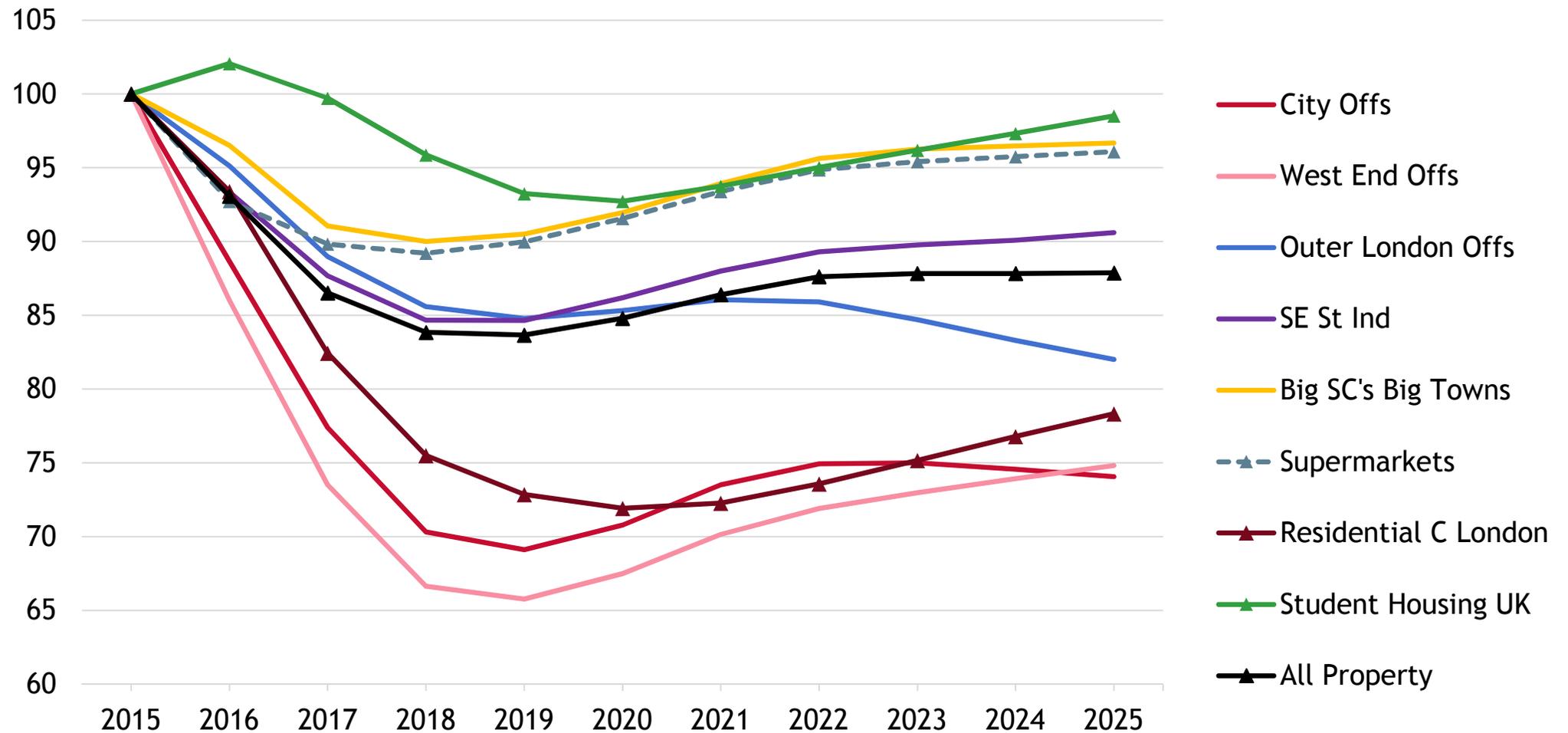
Brexit impact: capital values (base = 100)



Source: PMA

# Other sectors and markets do better

Brexit scenario: capital values (base = 100)



Source: PMA



# Appendix

# Research & Strategy platform



**Mike Acton**  
Head of Research  
AEW Capital  
Management

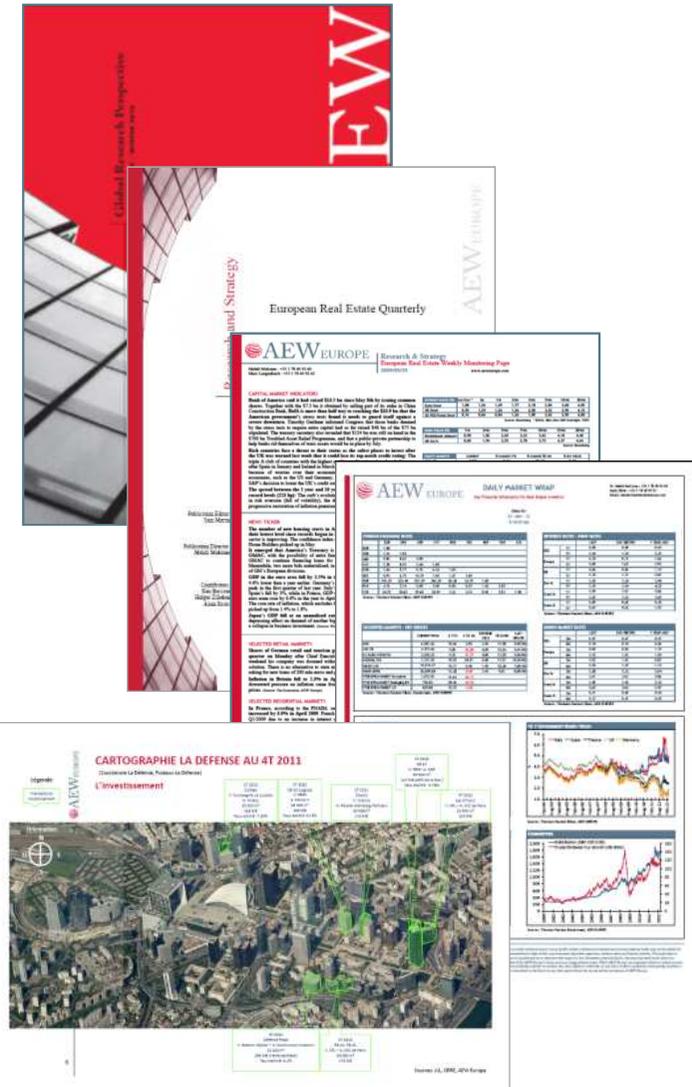


**Glyn Nelson**  
Director  
Research & Strategy  
AEW Asia



**Sam Martin**  
Head of Research  
AEW Europe

- 16 Research & Strategy professionals globally
  - 6 based in London and Paris
- London/Paris team provides seamless applied research support to Investment, Portfolio and Asset Management teams:
  - Production of proprietary Pan-European property market analysis, with a particular focus on core European and CEE markets covering logistics, retail, office and alternative sectors
  - Investment strategy formation
  - Investment underwriting
  - Input into the business planning and asset management processes
  - Regular publication writing
  - Global macroeconomic analysis with a particular focus on property market and investment strategy implications
- Research & Strategy produces regular and special topic research for internal and external clients on a weekly, quarterly and annual basis:
  - Real Estate Weekly Monitoring Page
  - European Real Estate Quarterly
  - Quarterly client market reports
  - Ad-hoc special topics and articles for the property press



# Research & Strategy platform

- We gather economic, financial and property markets intelligence from a wide variety of resources both internal and external
- Our main inputs include:
  - Macroeconomic:
    - Independent analysis and reporting challenging prevalent consensus views
    - Global, regional, country-level, city-level, and sub-city level data including independent forecasts
  - Real estate:
    - Independent and property consultants' commentary and analysis at market and sub-market level
    - Detailed fundamental data and independent forecasts at country, market and sub-market levels
    - Investment volume data and analysis
  - Capital markets:
    - Relative and absolute pricing of other asset classes
    - Real estate market implications
- Research & Strategy produces regular and special topic research for internal and external clients on a weekly, quarterly and annual basis:
  - Real Estate Weekly Monitoring Page
  - European Real Estate Quarterly
  - Quarterly client market reports
  - Ad-hoc special topics and articles for the property press

## Data and intelligence sources

### Macroeconomics

- Natixis
- Lombard Street Research
- Oxford Economics
- Capital Economics
- Economist Intelligence Unit
- Consensus Economics
- Société Générale
- Variant Perception

### Real estate

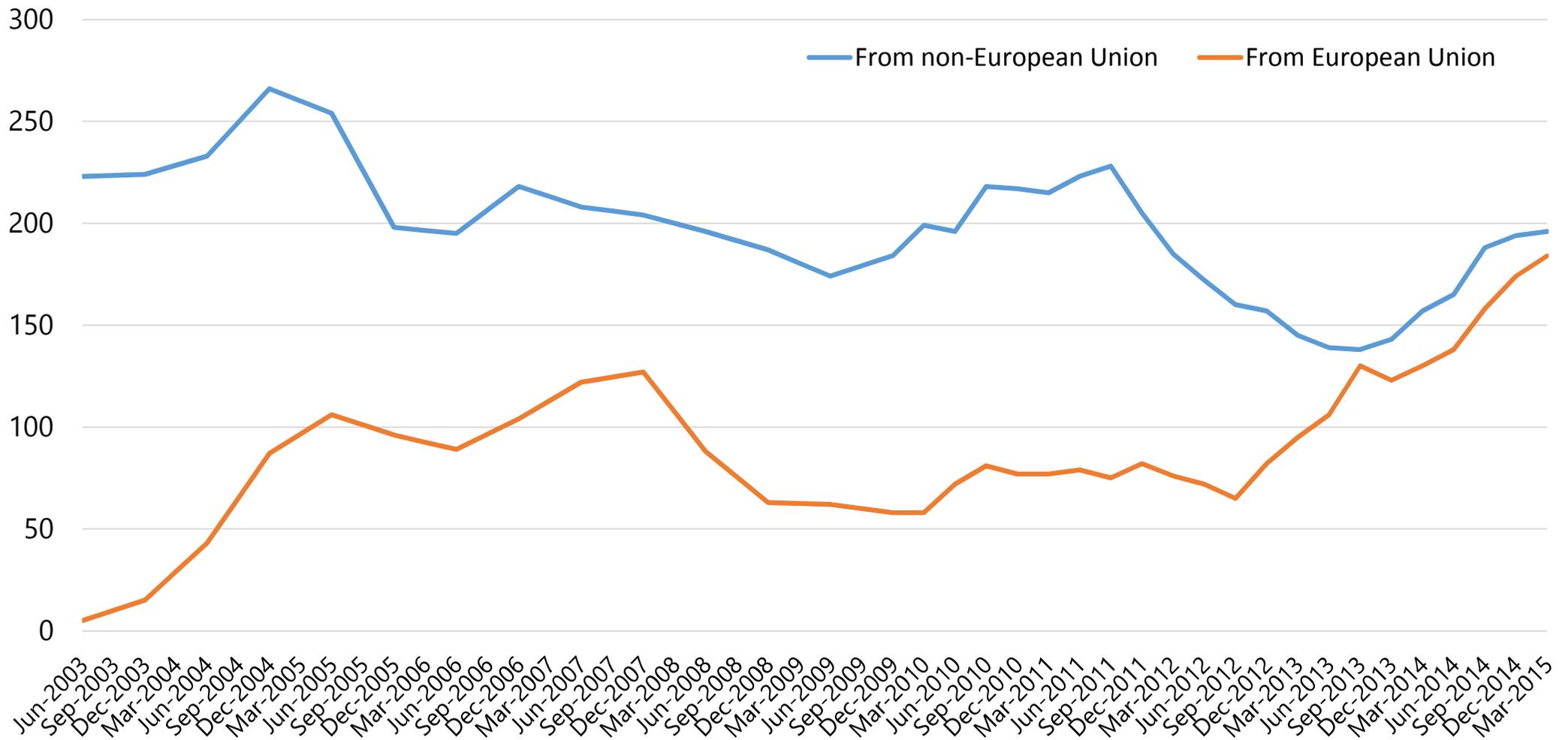
- Property Market Analysis
- Property consultants' data, commentary and analysis
- Annual valuation reports
- Investment Property Databank
- Investment Property Forum
- Society of Property Researchers

### Financial markets

- Bloomberg
- Macrobond
- Decision Economics
- The Economist
- The Financial Times
- Natixis Capital Markets
- Reuters Breaking Views

# Migration matters

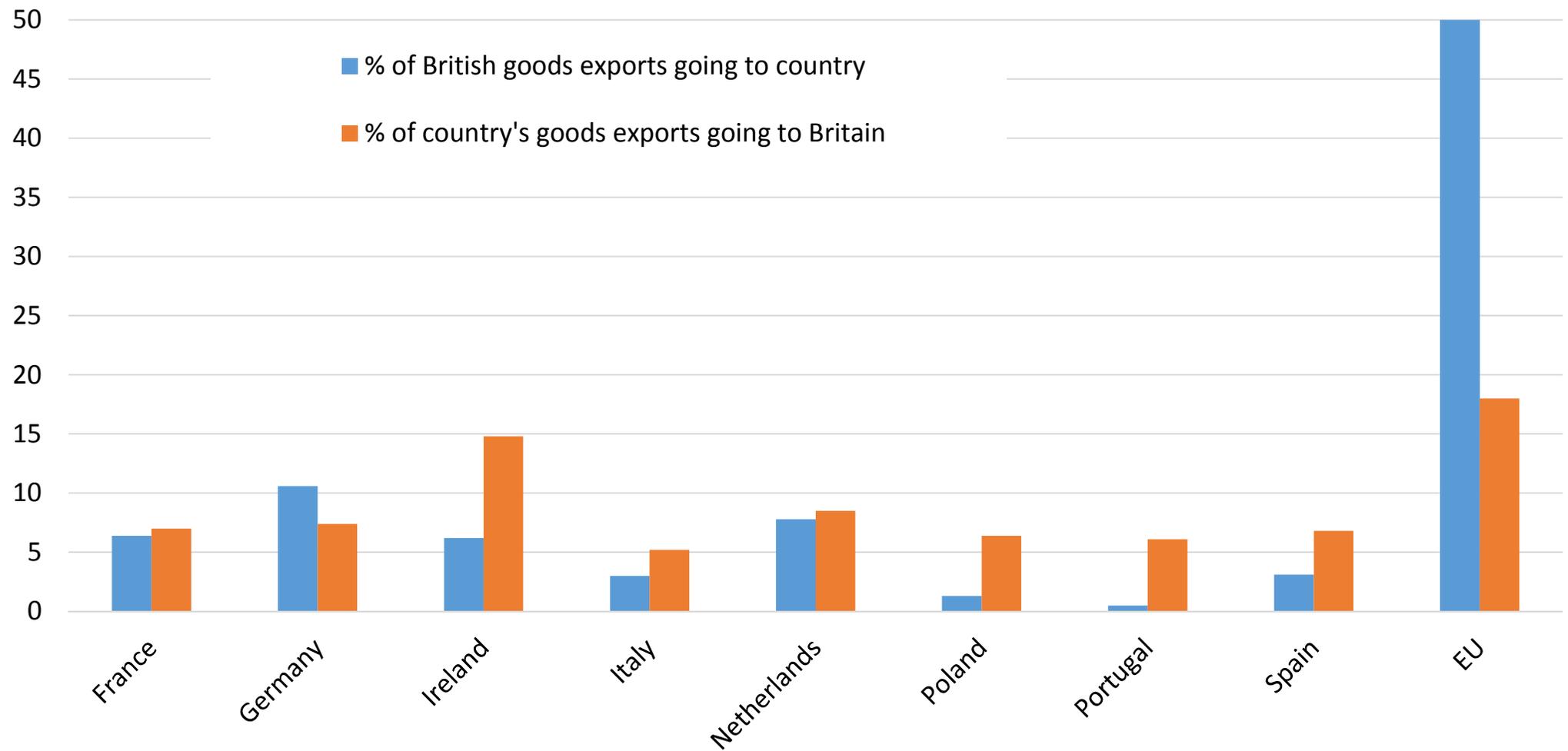
Net migration to the United Kingdom, thousands per annum



Source: Office for National Statistics, Capital Economics

# Germany's size matters

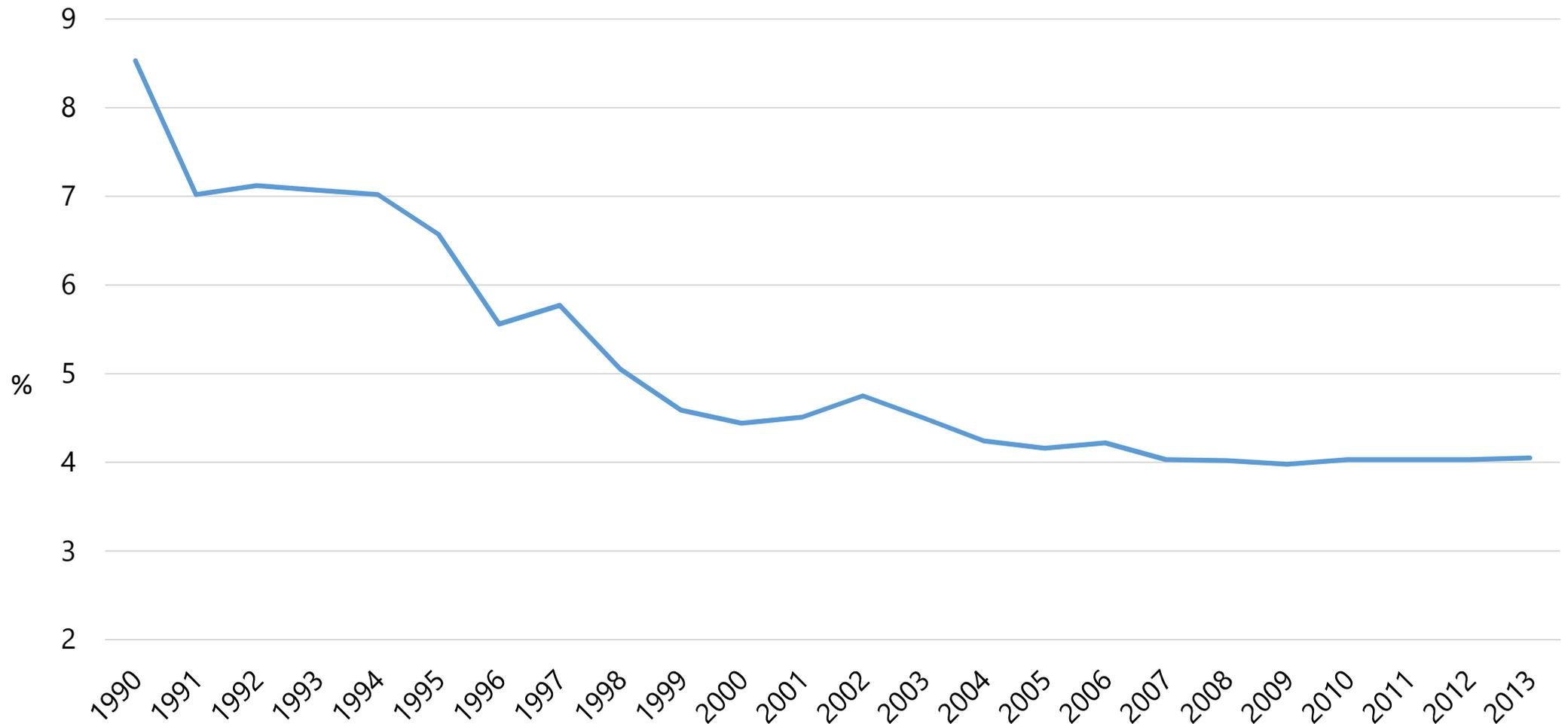
Exports of goods by destination (% of total 2014)



Source: Thomson Datastream, Capital Economics

# EU less important over time

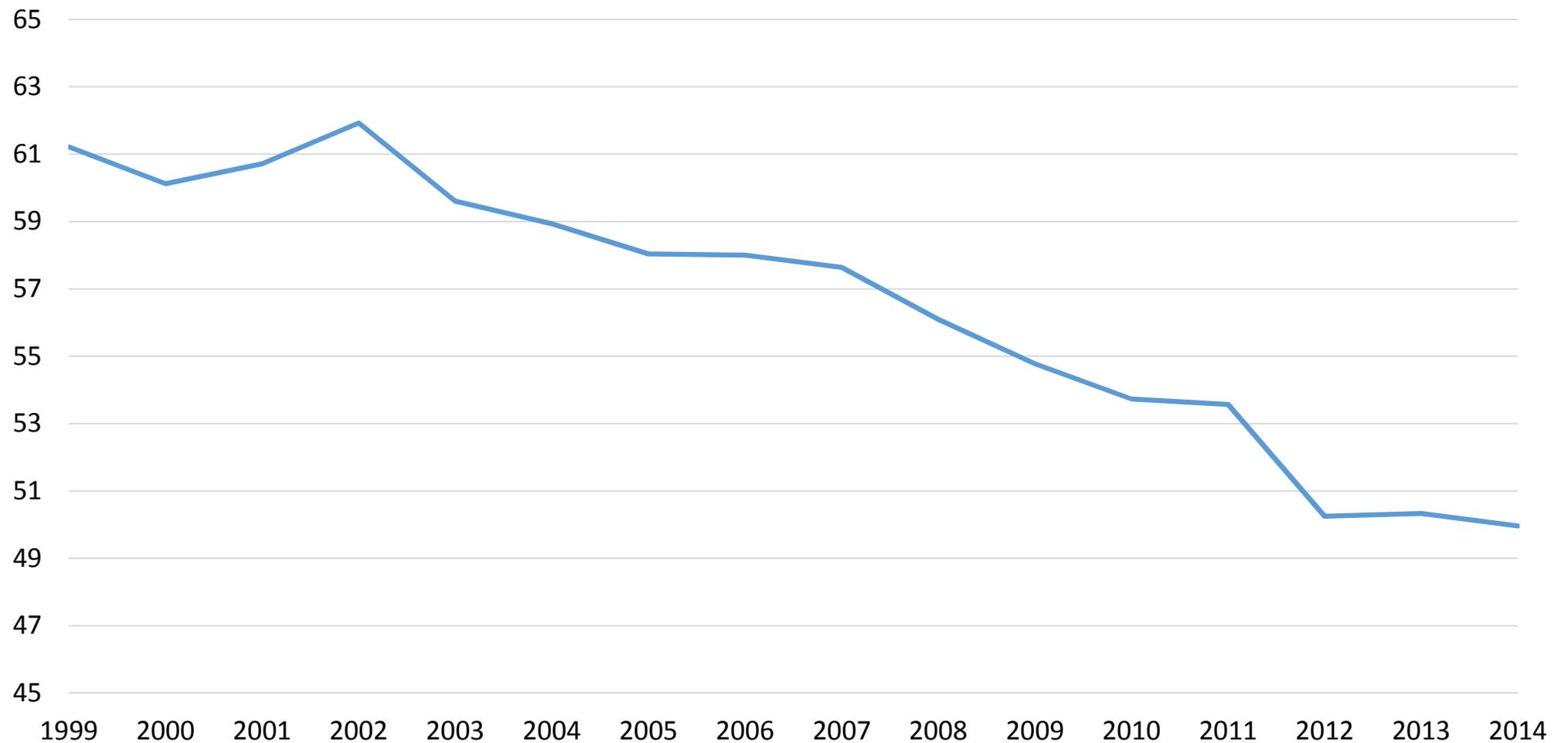
European Union most-favoured nation average tariff on manufactured goods (%)



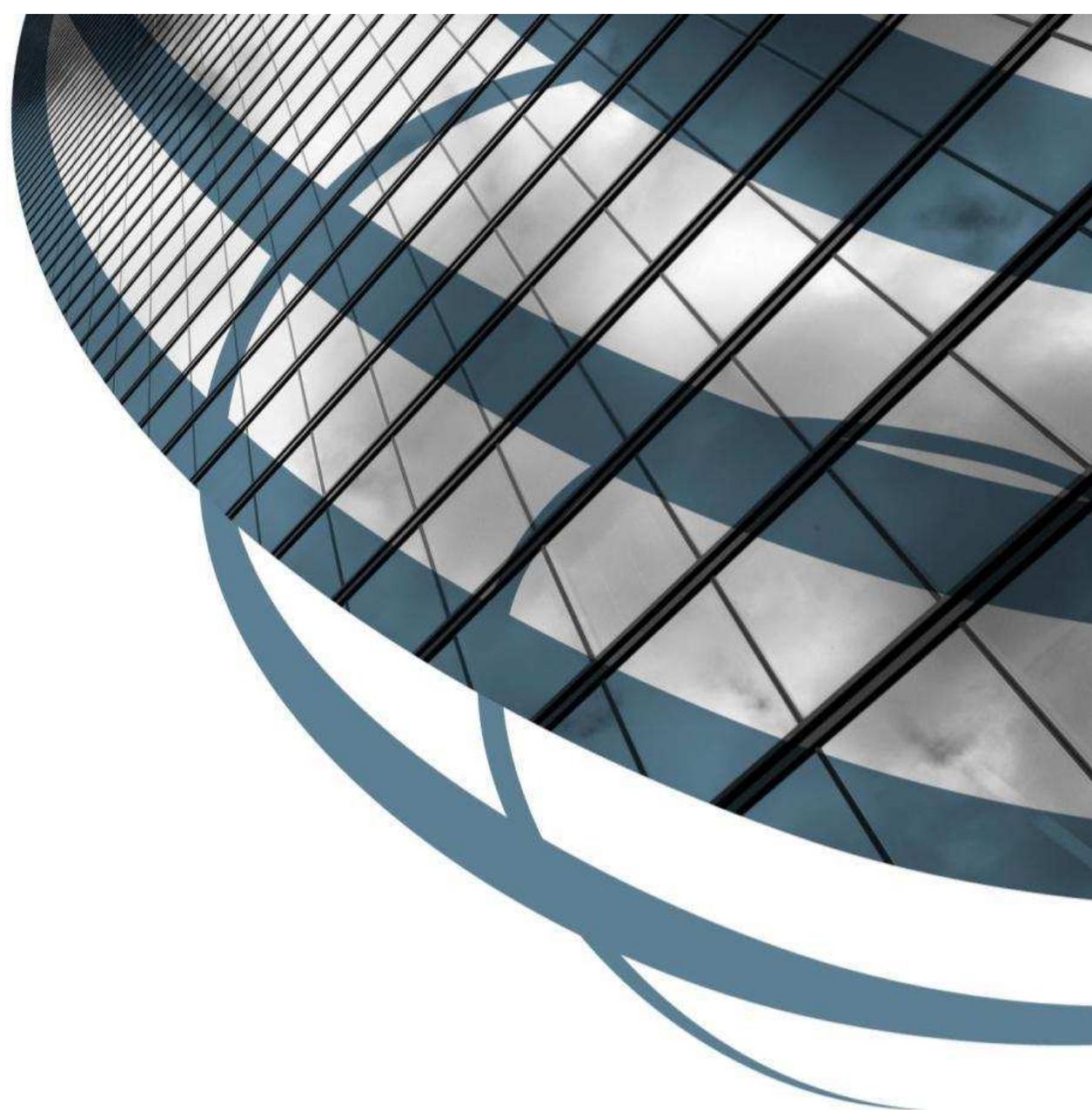
Source: World Bank, Capital Economics

# The cost of access

Exports of goods and services to the EU (% of UK total)



Source: Office for National Statistics, Capital Economics



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