"We decide on something, leave it lying around and wait and see what happens. If no-one kicks up a fuss, because most people don't understand what has been decided, we continue step by step until there is no turning back." **Jean Claude Juncker**

"When it becomes serious, you have to lie." **Jean Claude Juncker** addressing a meeting of the federalist European Movement on 9th May 2011

"We all know what to do, we just don't know how to get re-elected after we've done it." **Jean Claude Juncker**

Am I picking on Jean Claude? Yes but only because I read these quotes recently. I am sure if I wanted to waste a few hours of my life, I could find similar quotes from numerous other major political figures.

Anyway, before I lambast the most recent spate of political gerrymandering by our beloved leaders and wannabe emperors a few titbits of information for you:

- British Land plc announced their results on the sale process of their new development Clarges Mayfair overlooking Green Park. It has exchanged on the sale of 18 apartments with an average value of £4,750 p.s.f. as well as setting new records for Mayfair of over £5000 per square foot

- The number of billionaires living in the UK has risen to 104 with a combined wealth of more than £301bn - Sunday Times Rich List, 2014

– Overseas’ buyers purchasing property as rental investments only account for c. 7% of all greater London residential transactions. The percentage seems much larger due to high investor activity in the new build sector which accounts for less than 10% of all London transactions (Savills)

– Lenders provided £2.2 billion of private-landlord mortgages in April, a 57 percent increase from a year earlier, according to the Council for Mortgage Lenders. Gross mortgage lending increased 36 percent to 16.6 billion pounds and loans to first-time buyers gained 47 percent to 3.5 billion pounds in the same period. (Bloomberg)

– More than 34 houses worth in excess of £1 million are sold every day according to figures released by the Land Registry.

– There were 478 sales in Chelsea over the 12 months - with 57 of those homes costing in excess of £5 million. This outstripped Knightsbridge, Mayfair & Belgravia (Land Registry)

– The UK’s population has increased by 4.4 million over the last decade, yet just 2 million new homes have been built (CBRE)

– The super-prime market of London is a very small part of the overall market; 5.5% of sales in 2013 were priced over £5 million with just 1.4% priced over £10 million. (Lonres)

– In SW8 alone there are 16,233 units being built across 15 developments, the largest of which are Embassy Gardens, Battersea Power Station, Nine Elms Parkside and New Covent Garden Market.

– New World Wealth report titled 'The Multi-Millionaire Phenomenon: Second Home Hotspots'. London tops the list with 22,300 multi-millionaires with second homes in the city. This is in addition to the 9,700 resident multi-millionaires living there.

– Stamp Duty revenue has increased by 34% in the last year. SDLT raised £9.273 billion compared to £3.108 billion collected in Stamp Duty on shares. 70% of the SDLT revenue was raised on residential transactions

- The highest proportion of SDLT came from the London area, where buyers in Kensington & Chelsea paid £444m – 6.9% of the total.

- SDLT raised £1.01 billion from purchases of residential properties worth more than £2m by individuals – a rise of 26%.

**Politics, Politics, Politics**

Imagine you are a doctor. In front of you is a patient with multiple wounds. What do you do?

A. Administer a lethal injection as the patient will continue to deteriorate without extensive surgery, which will be difficult, expensive and with no guarantee of success.
B. Take a cursory glance at the wounds, but decide that it is too much effort/too costly to repair the damage in just a few operations. However, you sustain the patient with expensive blood transfusions until an indeterminate time in the future when the patient's deteriorating condition and death will be someone else's problem.
C. Risk your career and reputation by administering extensive surgery over a sustained period. You risk objections, reputational damage and the loss of your job, but in the long run it will save the patient's life, return him to health and ultimately save money.

Politicians will invariably choose option B if they can – see Ol' Juncker's third quote above. In the UK, Comrade Miliband wants to increase blood infusions into the NHS rather than fixing the problems which is rather like continuously pouring water into a bucket riddled with holes rather fixing the bucket.

Of course this is fine when you have a limitless supply of blood. Not so good if donors find that they do not want to actually give more blood and disappear. Of course the decision often differs if the person making the decision has to donate their own blood and more of it than they think fair/are capable of donating…

To be fair to Miliband, he is not alone. Pretty much every politician is too scared to suggest sweeping changes to the NHS. Miliband and the Lib Dems, however, have decided to go for the populist vote. They have proposed a Mansion Tax justifying it by saying that the increased revenue will be used for the NHS.

What will the tax entail? Well we don't know as there are no details. In fact they are being purposefully vague. Ed Balls said: "those with properties worth tens of millions of pounds… make a significantly bigger contribution than those in houses just above the limit", that limit being £2m. There will also be some form of protection for people who are asset rich but cash poor.

The goal is to allegedly raise £1.2bn or an average of £12k if 100,000 homes fall into this bracket. There is some confusion about the number of homes worth over £2m in the U.K. Some say there are c. 70,000 others estimate c. 110,000. Everyone agrees that the vast majority of these, c.90%, are in London.

Ultimately this is a very easy political play for Labour. It targets a tiny percentage of the <u>voting</u> population (in addition to the raw numbers a significant percentage will be owned by international buyers who have no vote) very few of whom are Labour supporters.

The tax is idiotic and unfair. For example, as Baker Tilly pointed out, a person whose home is a £1.5m flat , has an investment property worth £500k and a £1m place in the country would avoid the tax while someone with the same level of property, but in just one asset would get hammered.

The fact that it is unfair is, of course, irrelevant. If they get elected then it will happen although I would venture that the tax itself will not be quite as onerous as people suggest. However, one cannot be sure.

But what effect will it have? Well proponents of the tax will be hoping that as it is a tiny percentage of the market, it will have minimal effect.

Research by W.A. Ellis shows that between January and August 2013 there were 1,288 transactions and in the same period in 2014, 1,242 – a reduction of only 3.5%. The figures suggest that the threat of a Mansion Tax has not had an impact… yet.

Indeed, sales between £2,000,000 and £5,000,000 have increased by 11.7% this year. However sales of properties over £5,000,000 have diminished by

5.5%.  The reduction in activity over £5,000,000 is perhaps indicative that the foreign investor may tolerate a tax of £15,000 per annum (based on the current ATED charges) but not the more punitive £35,000 charge per annum currently applied to properties held in company names with values in excess of £5,000,000.

Research by Savills also notes that "At the extreme, properties under 1,000 sq ft have risen in value by 22% since mid-2012, while at the other end of the scale, those over 7,000 sq ft, where the tax burden is greatest, have grown in value by just 3.3%. Whereas those between 1,000 and 2,000 sq ft have seen a two year price growth of 18% on average, those between 5,000 and 7,000 sq ft have risen in value by under 7%.

The tax situation will certainly have had an effect. However, I think that the demographic shifts taking place are the bigger driver of this. If you have suffered these reports for any length of time, you will know that I think the typical, narrow London townhouse will continue to underperform despite an increase in the number of people moving to London.

Estates Gazette recently reported: "Historically growing families left London seeking more space and light but that process is reversing and at some pace: "Between 2001 and 2011, the population of Greater London and Greater Manchester grew by 18% & 14% respectively – more than twice as fast as nationally".

The problem is that households are growing in number but there are less people per household which is why we are seeing pressure on the housing stock. This should bode well for smaller flats and small houses in general (it should also be noted that the undersupply of housing is misunderstood and poorly reported. There is a lack of supply of smaller, cheaper properties to buy rather than to rent. This is because of the inherent advantages that buy-to-let investors have over first-time buyers - another unintended consequence of previous political meddling. Unfortunately I do not have time to go into this in more detail now).

As you will see, **I am not suggesting that you should rush out and buy lots of small new build apartments!**

What will be the unintended consequences of a Mansion Tax (if it ever happens)?

1. Less money will come into the London market at the top end. This is already happening and is likely to continue. I expect there will be relatively few forced sellers and the market is likely to stagnate. **Result:** Less stamp duty revenues
2. Properties currently valued between £2m-£2.5m could quite easily be valued under £2m for mansion tax purposes if the time comes. There simply would not be a market for this price range (assuming a "slab" tax). This will greatly reduce the number of properties contributing and would also mean fewer forced sellers than you might anticipate. **Result:** A reduction in the expected revenue.
3. The tax will effectively "compress" the market so money that would otherwise have been used to buy properties over £2m will now focus on lower value properties. This in turn will price out people further down the property ladder. This is happening while every political party is saying we need to help people buy… Compressing the market while raising the taxes does not seem to be a good way of doing this. **Result:** Unhappy voters which will lead to yet more political interference and the unvirtuous circle will continue.

But, the real danger may actually attack from another angle. People who want to live in London will carry on buying and renting. Immigration is likely to continue and London will still be viewed as a safe haven. However, the continued attack on wealth and the anti-overseas buyer rhetoric is a cause for concern for international buyers. Therefore the part of the market that may see dramatic falls in price may not actually be the £2m+ market but the new build market where there is such a high percentage of international investors. They are far more sensitive to taxes and other costs.

The new build developments may well continue to sell well for now, but there is the possibility of significant price falls when they reach completion. Firstly, many of the buyers are speculators who do not really want to complete but want to assign their contracts before completion (known as flipping). This may prove harder than they anticipate and some are already realising this.

Secondly, the pressure on housing is really at the lower end of the market. These people will not be able to afford the rents in many of these developments. Consequently rental prices are likely to disappoint as there will not be sufficient demand for this type of property.

Now, many investors will not be bothered by this. However, a significant percentage will struggle if they cannot rent out their properties at the forecasted prices (which I think are unrealistic). Add in extended void periods and there could well be a significant number of forced sellers in the high density developments.

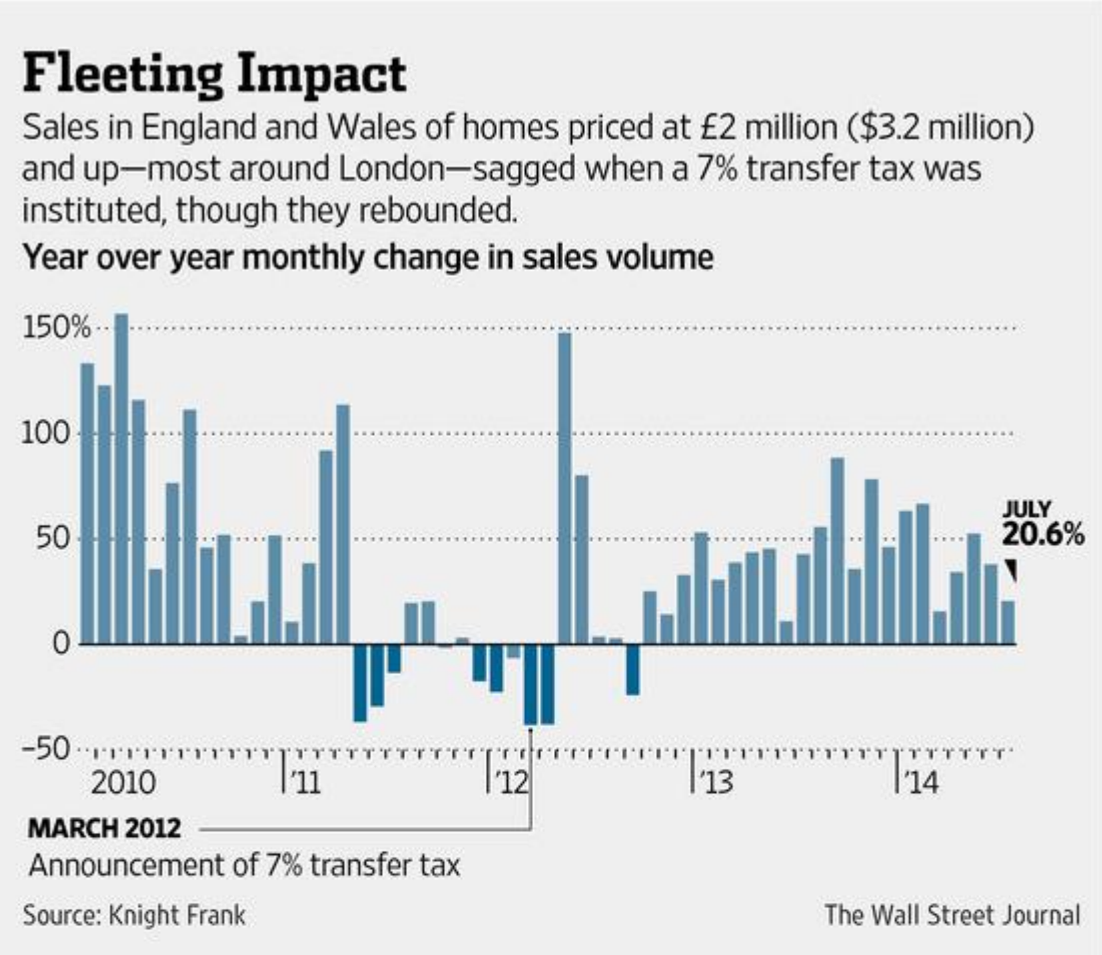
Basically you need to think very carefully about investing in areas where there is a high density of similar style apartments being developed – see SW8, for example.

**It’s not all bad news!**

The Mansion Tax is by no means a certainty. Firstly, Miliband has to actually remember to deliver entire speeches rather than omitting key points if he hopes to be elected. Secondly, a Mansion Tax will only happen if Labour win or form a coalition with the Lib Dems (assuming the Lib Dems actually get any votes). Thirdly, Labour’s proposal is so vague that it is highly likely to be watered down.

If, If, If…. and what do markets hate - uncertainty. Ironically prime London property has been the biggest beneficiary of global uncertainty. Now that we have our own worries, it is unsurprising that the market has “stalled” to use the latest euphemism.

However, as the chart below from Knight Frank shows, once the uncertainty over the 7% stamp duty (and later ATED) had passed, the London property market rebounded strongly.




The question this time is, if a Mansion Tax is ever introduced will it be the straw that breaks the camel's back?

Some very big players do not seem concerned. Reuters reports:

"Norway's $855 billion sovereign wealth fund, the world's largest, will focus its future real estate acquisitions on booming global cities, its deputy chief said on Thursday.

The fund invests 1.2 percent of its holdings in real estate but aims to increase that stake to 5 percent over time.

"We look for cities that are expected to see rising housing prices, that attract talent and people who are willing to pay to live in these cities," said Trond Grande, the fund's deputy chief.

“When we invest in England, we will not invest in Liverpool and Manchester. We will stick to London. Regent Street will be Regent Street, also in 50 years’ time.”

Indeed Savills are forecasting that all prime London property will see price rises of 23%.

Judging by the enquiries we are receiving there are many buyers who are not concerned by the threat of a Mansion Tax. However, there are certainly less buyers in the market than normal for this time of year. Consequently, there are opportunities to negotiate some good price reductions.

Do not be concerned about putting forward offers that may seem low compared to the asking price. We have recently bought an apartment for a client that was 18% under the asking price and 35% under the original asking price.

In fact only three days ago, an agent accused me of putting forward an “insulting” offer. When I pointed out to her that the property had been on the market for ages and that the offer letter included an in depth analysis of other properties that had sold in the area to justify our price, she simply started shouting. It is always a pleasure to deal with professionals! I assume she had already spent the imagined commission hence the reaction.

By the way, if this happens in a negotiation it is often better to then speak to the manager who is likely to be less emotional, than to continue trying to negotiate with someone who is simply not listening.

It is impossible for an offer to be insulting unless you actually include an insult in the offer letter. I have never tried this tactic as I expect it would be unsuccessful but perhaps I should give it a go. It is also strange that I have never heard an asking price being described as insulting, even though they are sometimes detached from reality. Go figure…

As ever, please do send me your thoughts and comments and if you know someone who would find this report helpful, please do forward it to them and ask them to contact us if they would like to receive future editions.

Best regards,

Jeremy