Election Result 2017: What will it mean for UK property?

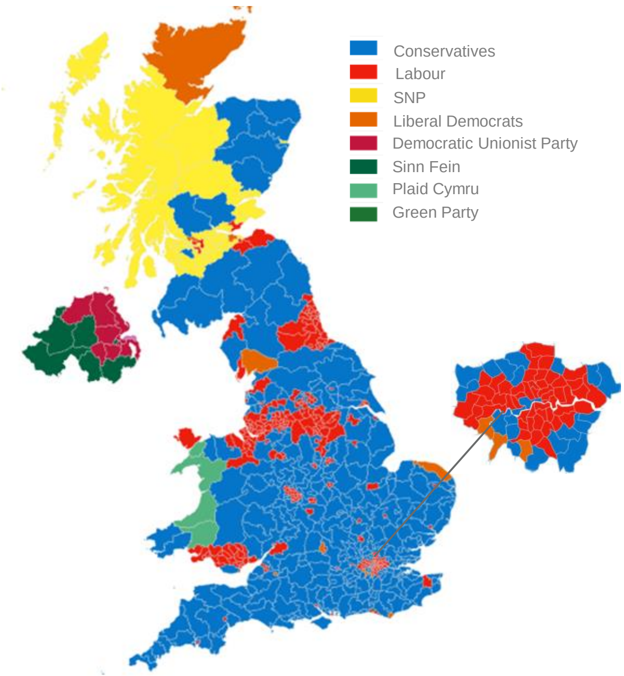
June 2017

DTZ INVESTORS

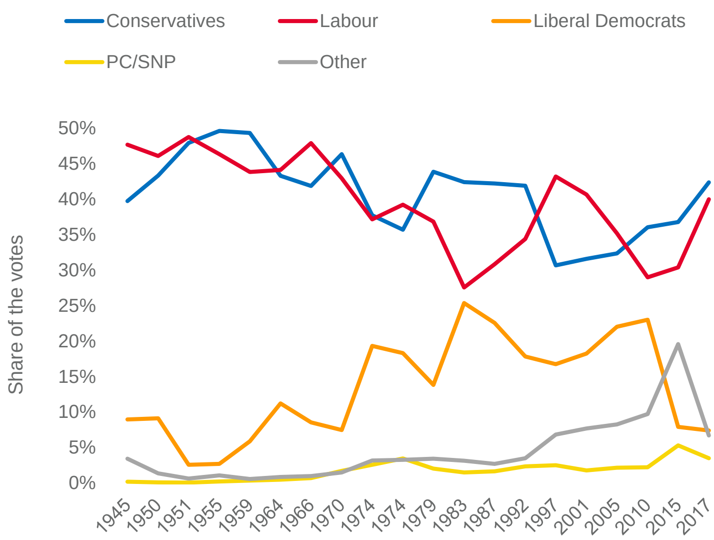
Just when the Prime Minister was on the cusp of seizing control and proceeding with her version of Brexit the electorate fought back, as the outcome of the surprise snap election, intended to strengthen Theresa May's Brexit negotiating hand, embarrassingly backfired.

In total, the Conservative Party received the highest share of the votes. At 42.4%, only the 'landslide' victories of Blair in 1997 and Thatcher in 1979 have surpassed this share since the early 1970's, however, the strong resurgence of the Labour Party vote and the UK electoral system resulted in the Conservatives losing their parliamentary majority. The result seems less of a surprise when one considers Theresa May's lack lustre performance during the election campaign. The key soundbite to May's campaign, 'a strong and stable' leadership came under question when the PM u-turned on key pledges in her manifesto, while the path envisioned for the UK economy, continued austerity and the lack of clarity on what was to be expected from a Hard Brexit were enough to persuade the electorate to vote differently. And so pro-business and pro-European voters, the young and the majority of London, looking for an alternate vision for the future placed their votes elsewhere.

2017 General Election Results by Geography



UK Vote Share by Party



Source: BBC, www.parliament.uk

The financial market's response to the election result was reasonably modest. The pound slipped to €1.13 and $1.27, still well above the post referendum lows, bond markets posted small losses, while equity markets gained. The FTSE 100 was up 1% by close of play Friday, as multi-national firms with foreign generated revenues benefited from the fall in the pound and even the domestically based FTSE 250 marginally increased. The effects of the political chaos on the economy remains unclear and will take time to feed through, but the fragility of the minority government and the scale of the Brexit task ahead will certainly test business and economic sentiment.

Are we heading for a 'coalition of chaos?

Despite May's failed gamble, the Prime Minister has vowed to press on, relying on Northern Ireland's right-wing Democratic Unionist Party (DUP) to support confidence motions and Conservative budgets. The newly formed leadership makes for uncertain times ahead. Doubts have been cast over the 'informal alliance,' and whether the new government will even last; and the strategic move is not without its issues, with the Conservatives likely to have to compromise on some measures to maintain the support of the DUP.

But the political upheaval could also be the catalyst for change. An enforced dependence on the DUP could mean the UK maintains some aspects of EU membership to allow a soft border with Ireland, and possibly a continued participation in the customs union. This was firmly ruled out in May's idealistic view of Brexit', but would be essential to the future prospects of Northern Ireland's economy. Alternatively, if a breakdown in negotiations between conservatives and the DUP occurs, the PM may have to resort to a cross-party approach to Brexit negotiations. Either way, the prospect of a softer stance to Brexit and a more relaxed type of austerity that better suits the short term interests of the economy seems more probable than it did days before.

How will UK property fare?

For the time being, we believe it will be business as usual for the UK property market, and do not foresee any short-term turmoil such as what followed last year's Referendum. The time lapse in property valuations relative to more frequently valued asset classes should provide enough of a pause for financial markets to seek some normality, minimising the effects on asset values. Short term movements in financial markets could also be favourable to UK property. The weaker pound is likely to boost demand from overseas property investors, while any near term declines in bond yields, given its safe haven status, could widen the property-gilt yield gap, increasing the attractiveness of property relative to other asset classes.

As for occupier prospects, it is hard to envisage any major short term changes due to the election results. Business and economic sentiment may weaken, but it was hardly upbeat before the vote was cast. The retail sector may be more vulnerable from cost push inflationary pressures that could stem from the short term fluctuations in the pound. The same factors are also likely to impact manufacturers and producers of goods in the industrial space, although the segment's healthy demand-supply balance should offset these pressures, enabling the sector to deliver above average rental growth for the rest of the year.

The sector that could see the biggest gains from the recent political developments is the office sector (London offices in particular). If a soft Brexit becomes a reality and the UK takes a more business-friendly exit from the EU, then this could result in a more optimistic outlook than we are currently forecasting. On the whole, we foresee a continuing shift towards more defensive stock as the prospects for rental growth remain generally muted.

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