FULCRUM INSIGHTS

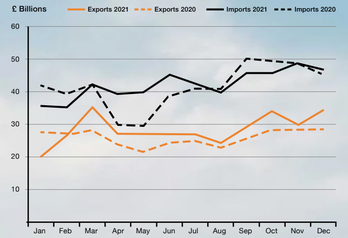
Fulcrum Global X Dr. Eddie Lam Analysis of Post-Brexit Residential Property Investment in the United Kingdom

The United Kingdom (UK) completed the transition period of the Brexit withdrawal agreement and as of 1 January 2021 was longer part of the European Union (EU) single market or the customs union. Will the UK economy be affected by Brexit after leaving the EU? The answer is surprising: rather than decline after Brexit, the British economy grew at its fastest pace in 80 years!

1 The UK economy rebounded by 7.5%, its strongest performance since 1941

According to official government data, the UK's gross domestic product grew by as much as 7.5% in 2021, which was the strongest economic growth since 1941. The total exports of goods reached £340.2 billion, up 9.4% from £311 billion in 2020. Except for January 2021 (the first month after the transition period), all other months in 2021 showed considerable year-on-year increases (Figure 1). Total imports of goods in 2021 were £504.7 billion, an increase of 1.7% compared to 2020. The jaws of some economic experts who had originally been bearish on Brexit surely dropped to the floor, and many had to admit that their predictions were wrong.

Figure 1: UK Total Exports and Imports of Goods[1] (2021 vs 2020)



What surprised the experts is that UK-EU exports did not plummet as expected. Total UK-EU exports increased by 4.2% from £148.9 billion in 2020 to £155.1 billion in 2021, while the UK's total non-EU exports grew by 14.2% (Figure 2).

Figure 2: UK Exports of Goods to EU / Non-EU[1] (2021 vs 2020)

	2021 (£ billions)	2020 (£ billions)	Change on 2020 (%)
EU	185.0	162.1	14.2
Non-EU	155.1	148.9	4.2
Total Exports	340.2	311.0	9.4

2 UK property investment: Anti-inflation, good rental income, value preservation and stable cash flow

Looking back on the concerns before Brexit, many people worried that the flow of goods to and from the EU would be subject to additional regulatory burdens. Import and export customs procedures and declaration documents were expected to be more cumbersome, raising enterprise costs and negatively impacting the overall export situation. But this has not been the case in reality! The value of UK-EU exports is increasing instead of falling – probably due to the free trade agreements of the UK with more than 70 countries. Moreover, the GBP/EUR exchange rate has also risen from 1.1 at the start of Brexit in January 2021 to the recent high of 1.2 (Figure 3). These are all evidence that the UK's post-Brexit economy growth momentum is indeed picking up.

Figure 3: GBP / EUR Exchange Rate Trend[2] (Jan 2021 – Apr 2022)

In addition to strong economic growth, another notable data point is the recent rapid rise in the UK inflation rate. According to data from the Office for National Statistics, the UK's consumer price index in March 2022 rose by as much as 7% compared to the same period last year, the highest in the past three decades. The Ukraine war has had a major impact on the surge in energy prices, pushing up the price of petrol by 12.6 pence a litre from February to March 2022.

As Ronald Reagan quipped, "Inflation is as violent as a mugger, as frightening as an armed robber and as deadly as a hit man". Inflation eats away the purchasing power of your savings. Moreover, it is believed that interest rate hikes in the UK should be slower than those in the United States in the coming future. In order to prevent bank deposits from being eroded by inflation, it is believed that many British investors will choose to buy properties in order to fight against inflation. Led by the impressive economic growth in the UK, there is strong demand for rental properties to push up the yield return. At the same time, the trend of rising inflation will also drive up property prices, allowing investors to obtain a stable cash flow from rental income.

3 Manchester, Birmingham and Leeds are new favourites for investors

If you want to buy a property for investment in the UK, it is recommended to consider central cities such as Birmingham and northern cities such as Manchester. Leeds is also an investment hotspot which cannot be ignored. Currently the average property price in these places is only 30%~50% that of London. In addition, the rental yield in those cities is much higher than that of London, and their future development prospects also have more potential. The British government has increased its focus on the development of northern cities with the Northern Powerhouse project, which aims to boost economic growth in the north of England, in order to avoid an excessive concentration of national development in the capital of London. This project has already attracted a large number of enterprises and young talent to England's northern cities. After the completion of the High Speed 2 (HS2) railway, it will take only 40 minutes to reach Birmingham from London and one hour to reach Manchester, which will greatly narrow the property price gap between London and northern cities.

According to a research report by the consultancy Capital Economics, the UK private rental market needs to increase by 227,000 homes a year to meet the demand for 1.8 million new households over the next decade. Leeds, one of the largest cities in the county of West Yorkshire, which is located to the east of Manchester, has also become a new favourite for investors in recent years. Savills expects rents in Leeds to increase by 18.8% over the next five years.

Some investors may ask the question: If I am not in the UK most of the time, will it be difficult to buy a property and collect rent from a distance?

If this is the case for you, you could consider entrusting a rental management company in the UK with the management of your property. According to current market prices, this type of company charges 10%~12% of the monthly rent and handles all the necessary work of renting a property. In addition to helping landlords find high-quality tenants, rental management companies will also arrange tenant screenings and conduct tenant credit checks. The scope of these background checks includes whether the tenant has a stable job, whether there is a record of non-payment of rent, utilities, broadband and credit cards, and whether there are bankruptcy and criminal records. After finding a suitable tenant, these companies will collect rent on behalf of the landlord and solve the tenant's problems, and then credit the rent to the landlord's bank account after deducting their fee and any expenses incurred.

Is it better to buy pre-construction versus a second-hand existing property? From an investment point of view, buying a second-hand existing home should be a better option. In the UK, the development period of a pre-construction property usually takes three years. If you purchase an existing property rather than a pre-construction building, you can enjoy an additional three years of rental income. Taking a return of 5.5%~6% per year after deducting the cost of the rental management company, three years of rental income is equal to 16%~18% of the property price – all in all a decent amount of money, and enough even to cover half of the down payment to buy an additional property! Moreover, you can visit the existing property on the spot, so there is no need to worry about not being able to complete construction. The average price per square foot is usually around 10%~20% lower than that of pre-construction buildings. In a nutshell, an investment in an existing property can allow you to get a higher rental return compared with an investment in a pre-construction property.

Source: 1) HM Revenue & Customs, overseas trade statistics 2) European Central Bank

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【About Dr. Eddie Lam】 Dr. Eddie Lam is a well-known celebrity and investor in Hong Kong, with previously experience of the vice chairman of a Hong Kong listed company with market value of USD40 billion, executive director of the investment banking industry and fund management. Over the years, he has been involved in various investment and speculation activities in the stock market, real estate market, futures, options and various business investments. His investments include Metaverse, online education platforms, publishing, education, real estate companies, game toys, medical supplies and sports. He is also the author of 40 books and 2 board games in Hong Kong, China and Taiwan.

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