



"While New York has seen considerable 'safe haven' investment flows in recent years, the resilience of the dollar dampened what could have been a much bigger influx of foreign buyers."

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# HIGHS AND LOWS

Our experience of global prime residential markets confirms the fact that buyers are increasingly focussing on the opportunities offered by currency movements.

Knight Frank's international team often find that, for example, when the pound/ euro exchange rate reaches €1.20 enquiries from new buyers strengthen.

In figure 1 we examine whether a change in the pound/euro exchange rate appears to influence the number of properties in the Eurozone being viewed by UK based buyers on Knight Frank's <u>Global Property Search</u> Website, (figure 1).

The results show two key trends. Firstly, that the relationship between the exchange rate and property viewings (demand) was strong during two key periods; throughout 2010 and also between December 2011 and July 2013 (see shaded sections).

There were two key periods when the relationship between the two indicators weakened; during 2011 and from July 2013 to the present. In 2011 the Eurozone crisis was at its height with talk of Greece being the first country to exit the Eurozone. Viewings increased significantly despite the economic uncertainty but this was due to the fact that speculative buyers were seeking discounted properties.

Turning to the second period, although online viewings have slipped slightly since July 2013, sales have increased

(particularly in France and Spain), suggesting those British buyers that are actively looking for a second home in Europe are now potentially more committed purchasers.

## The magic number?

Analysis of figure 1 shows the €1.20 exchange rate is influential to buyer sentiment but not critical. The €1.20 exchange rate has been exceeded on four occasions since 2010 with mixed responses in terms of online viewing numbers. Although the first half of 2012 appears to show a fairly close relationship.

If the pound/euro exchange rate remains at its current 22-month high, it will be interesting to observe activity in September, following the summer break.

## London v New York post 2009

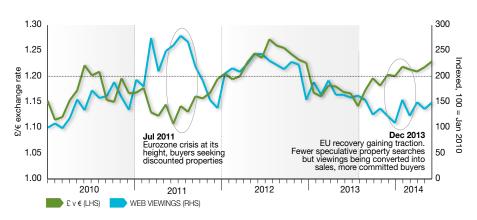
While currency matters to purchasers, it remains only one of many considerations, with investors weighing purchase costs, affordability and market transparency.

One of the most notable occasions when these factors aligned was in 2009 in London. Prime prices dipped by 24% in the year to March 2009 but a period of strong growth then ensued (prime prices jumped 20.7% in the year to April 2010). Buyers, both domestic and foreign, saw London's luxury bricks and mortar as a safe haven investment. In 2009 the pound had weakened significantly against key Asian currencies. This shift proved influential in attracting Asian interest in the UK capital.

The weakness of the pound meant that the number of Asian nationalities searching for properties in prime central London on Global Property Search website rose from 23 in 2009 to 31 in 2012.

During this time the US dollar remained relatively stable against the euro and key Asian currencies. While New York saw a flow of overseas investment into its residential market, the resilience of the dollar dampened what could potentially have been a bigger influx of foreign buyers.

£/€ rate v online viewings of Eurozone property by British-based buyers



Source: Knight Frank Residential Research / Macrobond

# **GLOBAL CURRENCY MONITOR**

To help gauge the real impact of currency movements worldwide, Knight Frank has created the Global Currency Monitor which calculates real investment returns for international investors by combining changes in prime prices with currency movements.

Our currency monitor not only looks at the performance of 30 prime residential city markets and 30 currencies but it allows different timeframes to be selected to see which buyer nationalities have seen the strongest and weakest returns.

### Some constants...

The standout performances of certain currencies in recent years means that regardless of whether you are comparing the performance of prime property in London, New York, Paris or Hong Kong buyers purchasing in certain currencies crop up time and again as the best or conversely worst positioned.

# Winners and losers ... or vice versa?

Below, we assess the currency monitor's results looking at two key time periods. Firstly, we assess the implications for those who purchased a year ago in prime central London. Next we consider the returns over a five year period using Hong Kong's prime market as an example.

There are two angles from which to consider the data. Firstly, from the perspective of those nationalities looking to buy today, and secondly from the perspective of those who purchased at the start of our two time periods.

An interesting example is provided if we consider a Turkish buyer looking to buy in central London in mid 2014, he is facing an effective 40% increase in prices compared to a year ago, which could well make a purchase less viable. However if the same buyer had bought 12 months ago, his investment returns have been super-charged by the combination of market and currency movements.

## Buying in: Prime London Time period: Last year

Due to the strengthening pound over the last 12 months – it is now at a six year high against the US dollar – there are few non-sterling buyers for whom prices in central London have appreciated at a slower rate than for local buyers (figure 2).

Prime prices rose by 7.5% in prime central London in the year to March 2014 in sterling terms. Only buyers from Iceland have an advantage compared to British buyers, with prices rising by only 6.6% over the 12 month period (figure 2).

Figure 2 also highlights the extent to which the currency advantage for Asian buyers looking to purchase in prime central London now has diminished compared to 2009 when the weakness of the pound gave them a significant advantage.

The good news for those Indonesian, Australian and Chinese buyers who bought in prime London a year ago is that their asset has appreciated rapidly, by 37.8%, 32.5% and 18% respectively. But for that same cohort of buyers looking to buy in 2014 the strengthening pound has made a London investment comparatively more expensive.

# Buying in: Prime Hong Kong Time period: Last 5 years

Prime prices in Hong Kong rose by 67.9% in the five years to March 2014 but buyers from New Zealand and Australia would only pay 10.2% and 25.6% more than in 2009 respectively due to the strength of their currencies.

In contrast, Japanese or Turkish property owners in Hong Kong may see the current confluence of prices and currency as an opportunity to sell.

The pegging of the Hong Kong Dollar to the US Dollar largely negates any currency play between the two, leaving buyers from either territory having to rely almost exclusively on price growth if looking to achieve their investment returns.

### The extremes

We have selected in figure 4 some key examples of the returns achieved based on common buyer trends around the world.

One common cross-border transaction, a Brazilian buying in Miami for example, would have paid, on average, 30.6% more in March 2014, than a year earlier, with only 17.2% of this growth due solely to price growth.

However, it's worth highlighting some of the less common buyer patterns which have reaped some of the largest rewards. In the year to March 2014, one of the largest uplifts would have been enjoyed by a Turkish buyer purchasing in Dublin, who would have seen a 58.3% return. The biggest loss over this period would have been an Icelandic buyer purchasing in Moscow, an admittedly rare combination.

# **BACK TO BASICS**

## What determines the strength of a currency?

Aside from global economic stability, interest rates, the supply and demand of a currency as well as a country's inflation rate all have a bearing. Tight fiscal discipline and anti-inflationary monetary policies will help strengthen a currency, along with a well-established rule of law and a history of constructive economic policies.

- If a currency is strong, the number of local buyers looking to purchase overseas will increase as they get more for their money
- If a currency is weak, property in the home country will be more appealing to foreign buyers with a stronger exchange rate.

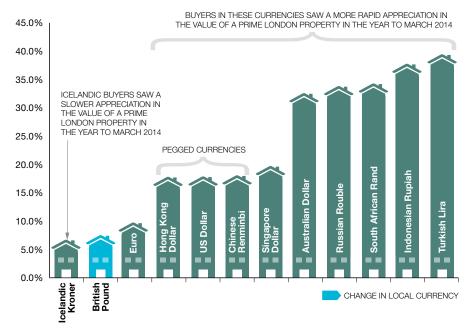


# THE REAL IMPACT: HOW INVESTORS HAVE FARED...

### FIGURE 2

### **Buying in: Prime London**

% change, taking account of price and currency movements (Mar 2013-Mar 2014)

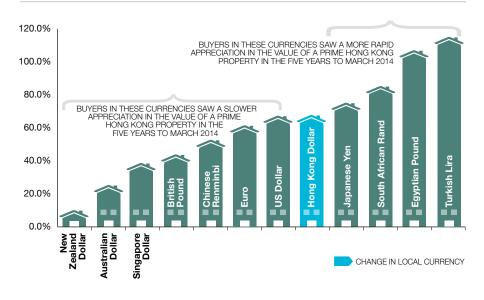


Source: Knight Frank Residential Research

FIGURE 3

### **Buying in: Prime Hong Kong**

% change, taking account of price and currency movements (Mar 2009-Mar 2014)



Source: Knight Frank Residential Research

For data on additional cities and currencies please see the **Data Digest** on the back page. Notes: All exchange rates are calculated as at 31 March 2014

### FIGURE 4

### **Premium and discounts**

Currency impact on common cross-border



-27.7%

Source: Knight Frank Residential Research



# **OUTLOOK**

The one statement we can be confident making about future currency movements, is that recent volatility is likely to remain a constant. The pound for example fell 20% from 2006 to 2010 but since 2010 it has outperformed nearly all its rival currencies apart from the Swiss franc.

On the world stage the biggest downside risks for global economic growth include the removal of market stimulus such as quantitative easing (QE) in the US, the slowdown in the Chinese economy, the expected rise in interest rates in the US and UK, as well as the geopolitical tension in Ukraine and the Middle East. Calculating the resulting impact of each of these events and the knock on effect on global currencies is highly complex.

There are, however, a few conclusions that can be drawn. Firstly, the Japanese Yen, the world's weakest performing major currency over recent years, is likely to strengthen, albeit slowly and from a low base.

Secondly, the currencies of key emerging markets have weakened significantly in recent years leading several to peg their currency against the US dollar or the euro to avoid further volatility. With stronger currencies, new wealth in these developing and influential markets is more likely to invest overseas.

At the start of 2013, and again at the start of 2014, the widely-held view was that the dollar would strengthen throughout the year and outpace the euro. This didn't occur. However, with the Federal Reserve likely to increase interest rates in 2015, and the ECB's move towards negative interest rates, the dollar is likely to rise.

The Yuan is still not currently fully exchangeable, but it is likely to be in five years-time. There are a growing number of observers expecting a devaluation – which would dampen investment outflows into global

residential property – especially property priced in currencies with a hard dollar link – Hong Kong in particular.

With prime price growth slowing in London, and falls being seen in Hong Kong and Singapore, buyers may start to identify profit-taking opportunities and look instead to low risk, tier two cities where capital appreciation may be strongest but in countries with weakening currencies.

Currency fluctuations can have a significant influence on investor returns or losses. But, as we have highlighted it is one of several considerations. The ease with which an investor can exit a market, tax changes, a market's transparency and stable political governance are also firmly on the radar of international investors.

### CURRENCY TRENDS TO WATCH



Chinese Yuan If the Yuan is devalued, Chinese buyers are unlikely to be as active in international property markets as they have been, particularly in markets such as London, New York, Sydney and Vancouver. Foreign interest in Chinese real estate would strengthen suggesting the cooling measures introduced to improve domestic affordability and deter foreign speculative investment would remain in place.



British Pound If sterling strengthens further (already at 18-month high against the euro) some foreign owners may take the opportunity for profit taking.



US Dollar If the US Dollar rises as expected, demand for prime residential property in those markets favoured by US buyers such as the Caribbean, Italy, Ireland, the UK and France may increase.



Euro

If the euro weakens, foreign buyers who retreated from many second home markets post 2008 may start to return motivated by the ECB's negative interest rate. Potential new stimulus in the form of QE by the ECB would support prices further.



Japanese Yen The Yen is increasingly viewed as a 'safe haven' currency, having fallen only 0.3% in the first half of 2014 against the pound. With property in Japan considered the most undervalued by the OECD when compared with rents and incomes, Tokyo may increasingly appear on the radar of international investors.

Source: Knight Frank Residential Research

# DATA DIGEST

The tables below show the aggregate effect of the change in prime prices and currency movements by city. For example, a property in prime central London purchased by a US buyer in March 2013 would have appreciated in value by 17.9% over a 12 month period. A British buyer, by comparison, would have seen growth of 7.5%.

### Year to Q1 2014

	LOCATION WHERE BUYING									
Currency of buyer	London	Paris	Miami	Hong Kong	S'pore	Toyko	Sydney	Dubai		
US Dollar	17.9%	7.5%	17.2%	-5.2%	-10.0%	6.3%	-5.2%	11.7%		
British Pound	7.5%	-2.0%	6.8%	-13.6%	-18.0%	-3.1%	-13.6%	1.8%		
Euro	9.7%	0.0%	9.0%	-11.8%	-16.3%	-1.2%	-11.8%	3.9%		
Russian Rouble	33.8%	22.0%	32.9%	7.6%	2.1%	20.5%	7.5%	26.7%		
Japanese Yen	29.0%	17.6%	28.1%	3.7%	-1.6%	16.2%	3.7%	22.2%		
Canadian Dollar	27.9%	16.7%	27.1%	2.9%	-2.4%	15.3%	2.8%	21.2%		
Australian Dollar	32.5%	20.8%	31.6%	6.5%	1.1%	19.4%	6.5%	25.5%		
Chinese Renminbi	18.0%	7.6%	17.2%	-5.2%	-10.0%	6.3%	-5.2%	11.7%		
Singapore Dollar	19.6%	9.0%	18.8%	-3.9%	-8.7%	7.7%	-3.9%	13.3%		
Hong Kong Dollar	17.8%	7.5%	17.1%	-5.2%	-10.1%	6.2%	-5.3%	11.6%		

Source: Knight Frank Residential Research

### 5 Years to Q1 2014

	LOCATION WHERE BUYING									
Currency of buyer	London	Paris	Rome	San Fran'co	Hong Kong	Shanghai	Tokyo	Dubai		
US Dollar	95.4%	33.8%	-4.2%	17.5%	67.7%	81.2%	-3.4%	57.0%		
British Pound	68.0%	15.0%	-17.6%	1.0%	44.2%	55.8%	-17.0%	35.0%		
Euro	88.2%	28.9%	-7.7%	13.2%	61.5%	74.6%	-7.0%	51.3%		
Russian Rouble	102.7%	38.8%	-0.6%	21.9%	74.0%	88.0%	0.2%	62.9%		
Japanese Yen	103.8%	39.5%	-0.1%	22.5%	74.9%	89.0%	0.7%	63.8%		
Canadian Dollar	71.5%	17.4%	-15.9%	3.1%	47.2%	59.0%	-15.2%	37.8%		
Australian Dollar	46.3%	0.2%	-28.2%	-12.0%	25.6%	35.7%	-27.7%	17.6%		
Chinese Renminbi	77.7%	21.7%	-12.8%	6.9%	52.5%	64.8%	-12.2%	42.9%		
Singapore Dollar	51.7%	10.7%	-20.7%	-2.8%	38.7%	49.9%	-20.1%	29.9%		
Hong Kong Dollar	95.6%	34.0%	-4.1%	17.6%	67.9%	81.4%	-3.3%	57.2%		

Source: Knight Frank Residential Research

For more information on the Global Currency Monitor contact Kate Everett-Allen

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