

ANNUAL WEALTH REPORT

PRIME RESIDENTIAL PROPERTY

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elcome to the 2008 Annual Wealth Report, a collaboration between Knight Frank and Citi Private Bank, market leaders in high-value property consultancy and wealth management respectively. In this report we have brought

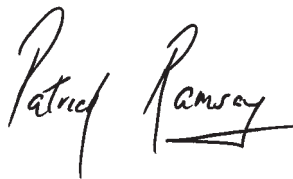
together our expertise in the property and financial sectors to provide insight into the wealthy and their relationship with the prime property sector.

It's been a roller-coaster 12 months. Prime property values rose 11% during 2007 as global capitals, emerging markets and prime sunbelt areas shone through the credit storm. Yet despite the spreading financial turmoil, emerging economies have maintained impressive growth. We provide a comprehensive analysis of the market, and investigate the growth of High Net Worth Individuals (HNWIs) around the world.

We look at the importance of residential property as an asset class, considering the role of second homes, investment properties and development opportunities in the wealth portfolio. We report on pricing trends across the global prime residential market and look forward, with the aid of market-leading thinkers and commentators, at the big trends set to impact on the property markets in the future.

While we have widened the scope and coverage of this year's report, once again our analysis is underpinned by three key questions: what do the wealthy expect from residential property? How has rising wealth influenced prime property performance over recent years? And where are trends pointing to in the future?

We hope you enjoy this unique publication.



Head of Residential, Knight Frank



Catherine Weir,
CEO, Citi Global Wealth Management, EMEA

Citi Private Bank



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CONTENTS

03

MONITOR

06 World view

Liam Bailey, Head of Residential Research at Knight Frank and author of the 2008 Annual Wealth Report, assesses the global property market

08 Global wealth survey

How many HNWLs are there and where do they live?

10 Wealth performance

Our experts discuss future financial trends

11 Design of the times

Ben van Berkel talks about intelligent design

12 Beyond the crunch

Donald Trump sees opportunities ahead

ATTITUDES

14 Decision makers

The factors HNWLs consider when they choose where to live

17 Good choices

David Lloyd picks his favourite markets for investment

18 Property as an investment

Where, why and how HNWLs invest in property

20 Property and the portfolio

Where bricks and mortar sit within the wider wealth portfolio

22 Back to nature

Architect Sou Fujimoto shares his vision for the future of housing

PERFORMANCE

24 Capital growth

Despite the credit crunch, London and Manhattan remain buoyant

25 Land rush

Agricultural land is a great investment, says financial expert Roger Orf

26 Prime numbers

Prime locations registering good growth, from Botswana to Australia

28 The future of luxury

Property entrepreneur Nick Candy says invest in the best

TRENDS

30 Residential design

At home with hotel detailing, bespoke interiors and iconic architecture

32 Environment and agriculture

Are HNWLs going green? Plus, the global squeeze on agricultural land

34 Hot locations

We tip 10 up and coming prime markets

36 Future horizons

James Waite of Globalegacy explains why social sustainability pays



NOTES AND DEFINITIONS

Wealth definitions

Knight Frank and Citi Private Bank place private wealth into three categories of net worth. Net worth is defined as being the sum of investible assets excluding the primary residence. Due to the nature of the subject matter contained in this report, we have included primary residences in our discussion regarding HNWI asset allocation.

Mass affluent	\$100,000 to \$1m
High Net Worth Individual (HNWI)	\$1m to \$10m
Ultra High Net Worth Individual (UHNWI)	\$10m to \$100m plus

In most instances, we use the acronym HNWI as shorthand for both HNWI and UHNWI.

Prime property

The term 'prime property' equates to the most desirable, and normally most expensive, property in a defined location. Commonly, but not exclusively, prime property markets are areas where demand has a significant international bias.

Research overview

Our research findings draw on three primary data sources produced exclusively for this report:

■ The Knight Frank High Net Worth Attitude Survey (Attitude Survey). We completed a first stage survey with 55 telephone and face-to-face interviews with private wealth managers and prime property specialists across the world. We followed this first stage process with a further 55 in-depth individual interviews with a similar range of asset and property management professionals.

■ The Knight Frank Prime International Residential Index (PIRI) comprises a basket of real properties that are valued throughout the year to provide the most accurate guide to prices and price movements in the prime global markets. All currency exchange rates used in this report are based on market rates on 31 December 2007.

■ The Scorpio Partnership's proprietary Wealth Distribution Model (WDM). This model combines

macro-economic and micro-economic data to estimate the 'true' distribution of wealth across different countries. The distribution data is based on parametric distributions of wealth, and builds in particular on the work of Vilfredo Pareto and subsequent academic developments in the fields of both economics and statistics. Parameterisation of the wealth distribution is validated against a number of statistical sources, including data from the IMF, UN, national household surveys, national balance sheets and rich lists. Growth figures are measured in both real terms and local currencies in order to allow for adjustment for inflation and exchange rate fluctuations.

For more information on the methodology employed in this report, please contact: Liam Bailey, Head of Residential Research at Knight Frank, at liam.bailey@knightfrank.com, or call +44 (0)20 7861 5133.

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- The prime property markets' performance over the last 12 months
- What next for the global investor?
- How many HNWIs are there and where are they?
- Investment trends ►

MONITOR

Market summary

Prosperous times?

It's been a tumultuous year for the global economy and property market. Liam Bailey assesses the market and gauges where it is heading next

The fate of plutonomy

This time last year plutonomy was a zeitgeist issue, but by early this year the atmosphere changed. The credit crunch seems sure to call a halt to asset price inflation and effectively stop access to the finance that fuelled it in the first place. However, the crunch has not yet signalled the end of wealth creation or accumulation around the world.

Last year we predicted that it was political rather than economic change that posed a risk to plutonomy – and in one country that prediction has partly been borne out. In the UK, a link has been made between private equity chiefs allegedly paying less tax than their office cleaners on the one hand, and wealthy non-domiciled residents apparently paying even less tax on the other.

The UK government responded with quick fixes to its capital taxes and advantageous non-domiciled rules, which led to speculation that London has lost some of its financial appeal. Eyeing the UK's share of world financial activity with envy, other countries have seen these tax changes as an opportunity to improve their share of global high value services.

Despite the uncertain economic and political climate, in almost all developed and emerging economies there were significant gains in the numbers of HNWIs, and the growth in their wealth has been similarly undimmed throughout 2007.

The credit crunch could turn nasty this year, with more than just the US economy at risk. Even so, it is too early to predict the end of plutonomy.

The credit crunch and the world economy

So far, the credit crunch has had its biggest impact in Europe and the US. Meanwhile, the rest of the world has seen economic growth power on. The crunch has proved that the rich are increasingly adept at protecting their wealth through substantial portfolio diversification and exposure to emerging economy and commodity investments.

The outlook, according to Robert Buckland, Chief Global Equity Strategist at Citi Investment Research, is mixed. He says: 'US housing and financial stresses will prove a drag on the global economy, and oil

prices have reached levels previously associated with recession.' But the picture is not entirely gloomy. Buckland adds: 'Economic leadership from the emerging economies and the continued easing of global monetary policy will remain resilient.'

The developed industrial economies will see GDP growth at 0.8% this year, but in the emerging economies real growth of close to 6% is predicted, so they should be able to cope with a slowdown in the West. A noticeable slowdown in the US economy is

Plutonomy defined

A plutonomy is an economy in which the richest 1% of households experience a more substantial and rapid increase in wealth than the general population. In the UK, for example, the wealthiest 1% has increased its share of national income from 6% in 1978 to 13% in recent years.

evident, though the reasonable inflation backdrop has given the Federal Reserve scope to ease monetary policy in order to support investor confidence. UK and European growth is also slowing, reflecting the impact of past policy tightening and the credit crisis. The Japanese economy remains static, with growth forecast at 1.8% for this year.

It's a different story among emerging economies. Asia will lead the way. China is forecast to enjoy a year of 11% economic growth. Latin America and emerging Europe are both forecast to see healthy growth this year, too, though not as strong as in 2007.

According to Buckland, the general picture is of a world economy 'at best muddling through'. The challenges remain considerable, most notably from US housing and the worsening global credit crunch, but support offered by emerging economies should buoy the market somewhat.

The bull market comes to an end

There is clear evidence that we are moving towards the end of the bull market in prime residential property – particularly in the developed economies. Over the past 12 months the number of locations where high price growth has been achieved has fallen. At the same time, the types of property and the price bands experiencing reasonable rates of growth have narrowed.

A classic bull market has developed and matured in London over recent years. The boom started in central London in September 2005 and continued through 2006, with annualised prime market price growth hitting 21% by July 2006. The boom gathered

There is evidence that we are moving towards the end of the bull market in prime residential properties

pace through early 2007, and by July of that year annualised growth reached 38%. At this point, annual growth for property priced under £1m had already peaked at just over 20%.

Price growth for properties priced up to £5m kept rising to hit 38% in August 2007. Annualised price growth in the £5-£10m band was next to peak at 44% in September, and by December price growth in the £10m-plus price band eventually peaked at over 50%.

This narrowing of growth to affect smaller and smaller market segments is characteristic of the end of a boom. Over the next 12 months, the London market will see much lower growth across all price bands as a bearish sentiment takes hold. By March the rate of annualised price growth in prime central London had fallen back to 24%, and we forecast that growth will continue to slow down into next year.

What next? And where?

Findings from our Wealth Report show that the rich are still getting richer. Over the medium and long term, super prime and prime markets will outperform as wealth accumulates around the world. Outside of these markets there are plenty of opportunities for investment in other locations.

The growing global mass-affluent population is worth serious consideration when formulating investment options. The expanding middle class in emerging economies in locations such as Warsaw, Guangzhou in China and Mumbai requires good quality, affordable accommodation, which is currently in short supply.

Rising affluence generates another market: second homes and holiday homes. A growing number of newly prosperous professionals in Moscow and other east European cities want second homes. Affordability constraints mean they are looking to buy in locations such as Bulgaria rather than more established markets like France. Buyers of developments on the Black Sea coast of Bulgaria have been 70% Russian, 20% Polish and only 10% northern European.

We have yet to see the full impact on demand for property from the rising mass affluent population of central and eastern Europe, let alone from China, India, South Korea and other Asian economies. The boom in second home ownership over the past decade will be as nothing compared with the growth we will see over the next decade.

The outlook

Residential markets have seen significant problems, including falling prices, restricted financing and declines in sale volumes. This began in the US and

is spreading to Europe, but it shouldn't colour the investor's view of the wider global property market. Prime locations have held their own: London, New York, Shanghai and others are proving that almost any residential market tied to the global economy maintains confidence among purchasers. Despite

Capital investment: the National Aquatics Centre, Beijing. China's economy is forecast for 11% growth



The boom in second home ownership over the past decade will be as nothing compared with the growth in the next

a weaker outlook for this year and next, we believe prime markets will remain worthy of attention over the long term.

The emerging market sector should be on every investor's radar – the likes of Brazil, China and India are seeing tremendous GDP growth and wealth creation. The spectacular capital price growth seen in these countries is due largely to a lack of supply of quality product in many cities.

■ Liam Bailey is Head of Residential Research at Knight Frank and the author of the 2008 Annual Wealth Report.

MONITOR

Global wealth survey

The big picture

Emerging economies such as China and India are experiencing rapid growth in the number of HNWLs

Data for 2007 provided by Scorpio Partnership reveals that wealth creation, and the allied rise in number of HNWLs and UHNWLs, has been dominated by the emerging market economies. The biggest high net worth population growth rates for 2007 were recorded by China (14%) and India (9%), while Kazakhstan, Singapore, Argentina and United Arab Emirates all achieved 8%.

In absolute terms the most significant growth was seen in the US, where the number of HNWLs grew by almost 120,000 to 3.1m. China saw the second largest increase, with the figure rising by nearly 46,000 in one year. China's HNWL population is now 373,000, which is almost as many as in Germany (375,000). The absolute growth in HNWL populations exceeded 20,000 in both Japan and the UK, which with 765,000 and 557,000 HNWLs respectively have the second and third largest populations in absolute terms.

Commodity price rises have brought wealth and created a significant number of additional new HNWLs in countries that benefit from a high level of natural resources – Brazil, Canada, Australia and Russia, which each added more than 8,500 additional wealthy residents in 2007.

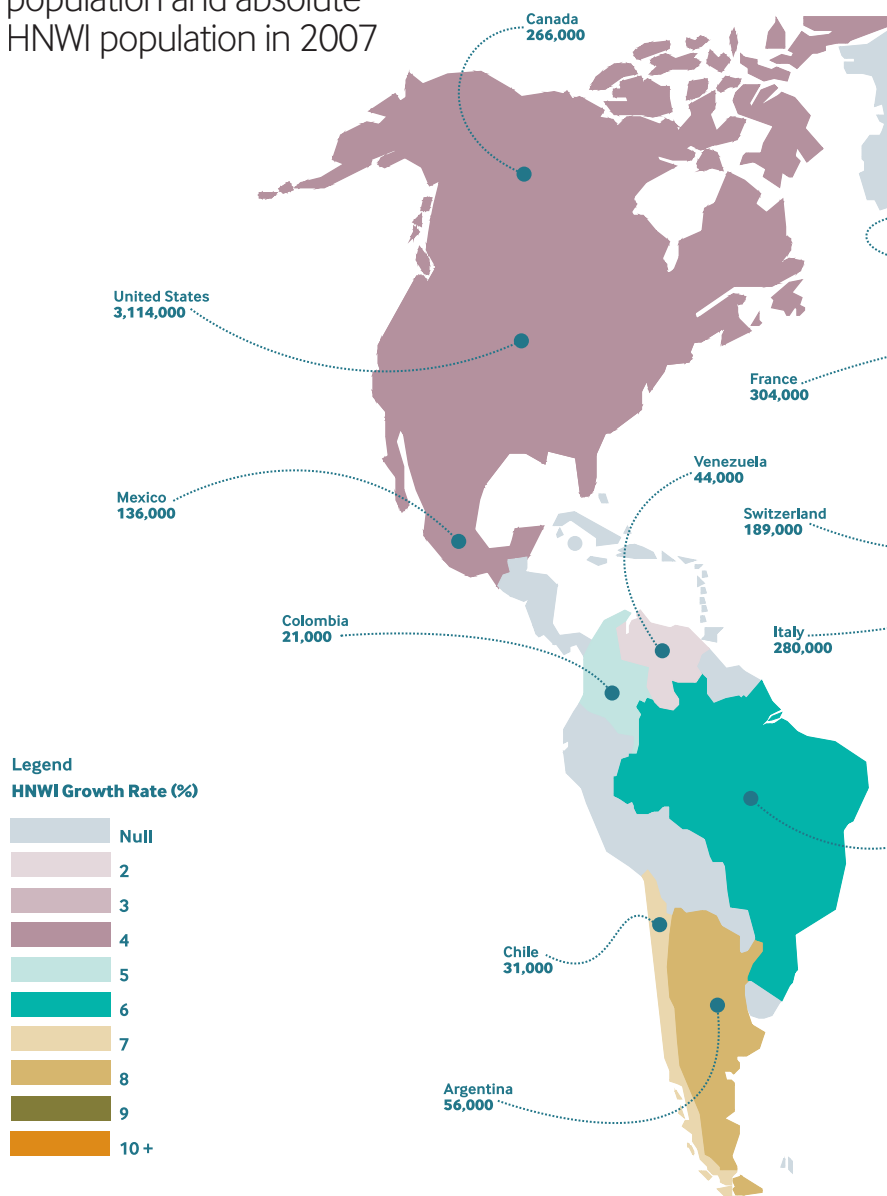
One constant across almost all the countries surveyed by Scorpio Partnership is that the rate of HNWL growth has outpaced growth in both GDP and GDP per head. This is not a perfect measure of relative wealth growth across income levels, but there is an indication here that the plutonomy model retained its strength through 2007 and is in rude health.

The number of UHNWLs and dollar billionaires has a close to linear relation to HNWL populations. The US has the largest number of dollar billionaires (460), followed by Russia (82). The UK has 49, although only 35 have British nationality. Switzerland is an even bigger importer of billionaires: 16 out of its 25 are from abroad.

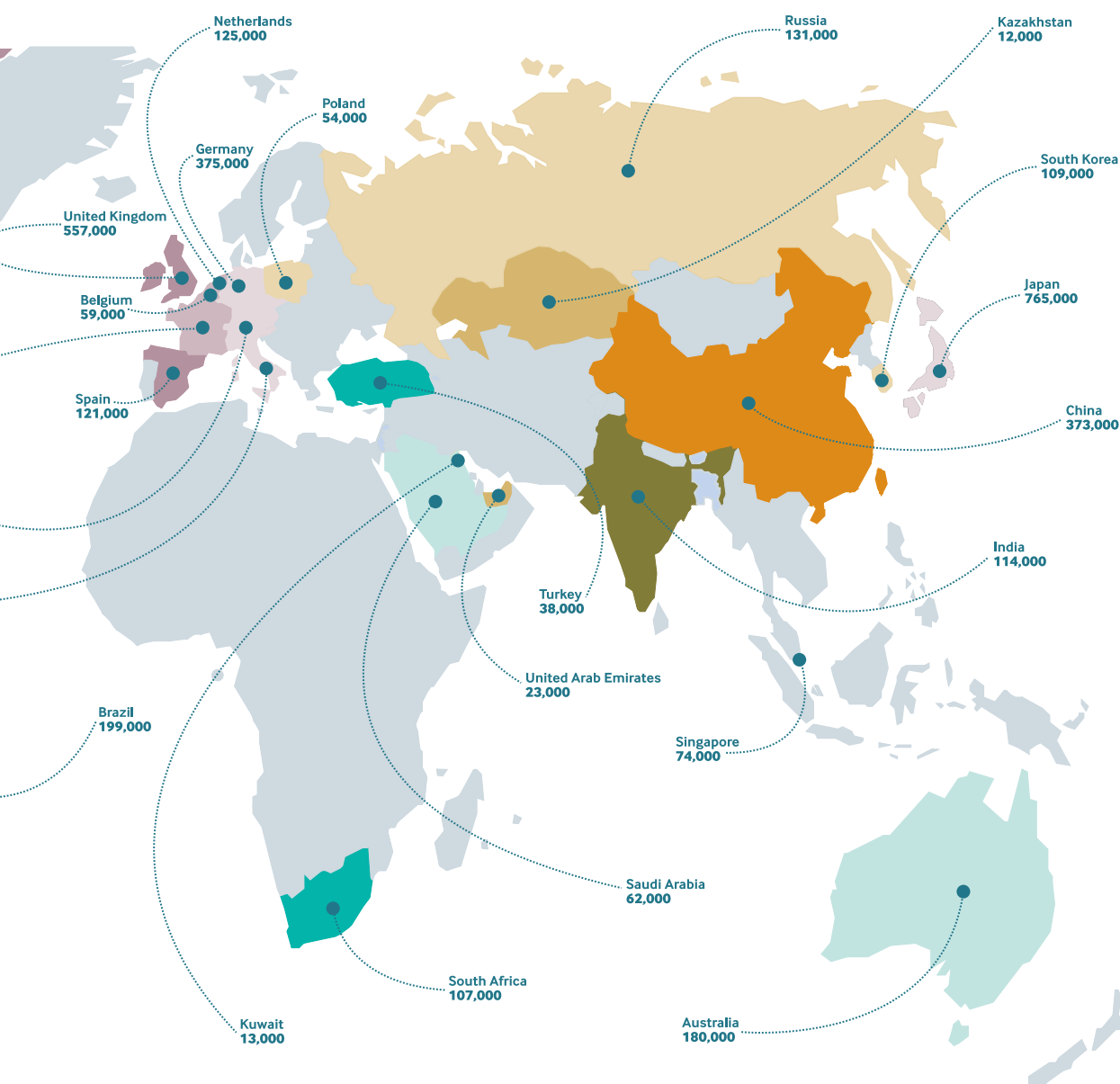
Future growth in HNWL and UHNWL numbers will centre on locations that have huge reserves of existing wealth and innovation (the US), places that are financial and high-value service specialists (UK and Hong Kong), commodity-rich economies (Brazil, Russia and Canada), emerging market powerhouses (China and India) and low tax jurisdictions (Switzerland and Monaco, among many others).

Where is the wealth?

Growth rate in HNWL population and absolute HNWL population in 2007



Source: Scorpio Partnership



Methodology employed

The data in our global wealth survey has been provided by Scorpio Partnership and comes from its proprietary Wealth Distribution Model. This model combines macro-economic and micro-economic data to estimate the true distribution of wealth across different countries. For more information about the methodology, please see the Notes and Definitions section on page 4.

MONITOR

Wealth performance

The shape of things to come

Liam Bailey talks to Catherine Tillotson, Head of Research at Scorpio Partnership, about global wealth trends

LB: Are the BRIC nations (Brazil, Russia, India and China) the future for wealth creation?

CT: Based on current economic forecasts and the outlook for the global economy, these countries are set to hold a dominant position among the emerging economies. They are increasingly important in terms of wealth generation, investment and spending decisions. China is experiencing a diversification in its economic base, and over time HNWIs from China will be a more noticeable force in the world economy.

LB: Will we come to see as many wealthy Chinese and Indians in London or New York as we do Russians?

CT: There is a feeling that the wealthy Chinese will concentrate on Asia in terms of travel and investment. The Indian experience is different – the historic links with the UK mean that London is an obvious first port of call for so many wealthy Indians.

LB: Could Brazil be the country that ends up surprising us? It has a young and growing population, unlike Russia and soon China, and significant mineral and natural resources. Brazil and the wider Latin American economy look very interesting as locations supporting considerable growth in personal wealth.

CT: Yes, I am positive about Brazil. There is a degree of reliance on the commodity market, but it supports significant innovation in IT and biotechnology, which should aid widening local economic strength over time.

LB: Do discussions of wealth creation and the emergence of HNWIs tend to discount the US? It has more seriously wealthy people than anywhere else and seems uniquely able to translate innovation into wealth creation.

CT: Experience from the private banking arena shows that US banks are very innovative and rank with Swiss institutions in terms of development of new services for the large and very demanding US HNW population. US banks have had to introduce elements such as financial education weekends for younger, soon-to-inherit HNWIs, and family office development

has been led by the US. The reason the US is often not fully recognised in global wealth discussions is that there is a more parochial outlook for US HNWIs

there are so many options and opportunities for investment and spending decisions within the US and a less outward or global mindset.

LB: Is the rapid emergence of wealth in the UK in recent years merely a product of low interest rates and high house price appreciation?

CT: Some of it, yes, but we shouldn't understate the achievement the UK has made in grabbing market share in high value added areas of the financial services sector. Despite the credit crunch and a downturn in some areas of finance activity, the UK continues to be a leader in financial services.

LB: Will the focus on non-domicile rules affect the performance of UK wealth creation?

CT: Complex issues of equity and fairness always need to be addressed at a political level. However, in terms of the UK's economic position the presence of non-doms has been a significant benefit. London in particular has benefited over the past decade with innovation in services being undertaken here that could easily have taken place elsewhere. The real concern for the UK is that other countries are desperately working to take a share of the UK's financial services industry. Monaco, Switzerland and Dubai among other locations are spending a lot on infrastructure and services to attract the hedge funds and other players. It is not all to do with non-dom legislation – the UK has been very adept in creating the right framework for financial services to flourish. Despite recent criticism, the UK Financial Services Authority has been a serious force for good across the market.

LB: Are there lessons to be learnt from the Singapore model?

CT: Singapore has worked very hard to attract the most talented Asian financial employees and to create a centre of excellence in financial services. Its government looked at the Swiss model and has created the conditions for the development of the Asian centre for private banking and niche high value service provision. It has been so

On the rise: São Paulo, Brazil. The country may yet support enormous growth in personal wealth



successful that there are now significant shortages of private bankers. The real lesson is that you have to create the right conditions for wealth to flourish.

LB: Do the new investigations into alleged tax avoidance activity in Liechtenstein have wider bearing on off-shore or low tax jurisdictions?

CT: It is likely to force greater clarity and transparency across not just Liechtenstein but also Monaco, Andorra and several Caribbean centres. There is a place for low tax centres in the global economy, and the EU and the US have learnt to work with them. But the tide of public opinion has definitely turned against illegal tax avoidance activity. There is a much bigger market for tax minimisation, rather than avoidance.

LB: How have HNWIs reacted to the crunch?

CT: There has been little change in their activity, other than a shift away from structured finance. They already had significant diversity in their portfolios across property, equities and funds. In fact, the HNW population is weathering the crunch much better than larger institutional investors.

LB: Is there a global HNW outlook – a similarity of behaviour or aspiration across the world?

CT: The fundamental question is less about national characteristic and more about maturity of wealth. First and second generation HNWs tend to concentrate on protection of their wealth, investing heavily in education and skills for the next generation – think of Indian, Russian and Chinese students applying to UK private schools and US universities. The temptation for later generations of HNWs to spend rather than invest is a feature of European, American and Asian HNWs, and the risk of going from rags to riches and back again in three generations seems to be universal.

LB: What will influence the activities of HNWs over the next few years, especially in relation to property purchase or investment?

CT: The biggest trend is a shift to a greater emphasis on legacy issues. There are some fabulous fortunes that have been made in recent years and as wealth becomes more 'normal' the search for luxury becomes a given. HNWs have become far more interested in philanthropic issues and property is a key area here. The ability to 'give something back' through the enhancement of a local or international environment is a real objective for an increasing number of HNWs. Environmental issues are an area where they can see their wealth, their skills and their network really making an impact.

'Singapore has worked very hard to attract the most talented Asian financial employees and to create a centre of excellence in financial services'

INSIDER INTERVIEW



BEN VAN BERKEL
Co-founder and Director,
UNStudio, Amsterdam

What will be the key themes for the future in residential property?

The emergence of the millennium generation will be interesting over the next decade. They care about good design and put increasing emphasis on iconographic design to help them stand out from the crowd. Architects are learning from the likes of Calvin Klein, who has taken a high-end luxury product to the mass market. People are also thinking differently about the purpose of spaces within the home. The living room, for example, is no longer the most commonly used space and this impacts on its design.

What is the most positive trend at the moment? And the most negative?

Sustainability is rising in importance and with it intelligent design, as clients demand their properties have a lighter environmental impact. But over-reliance on new design technology can restrict the imagination and lead to a formulaic approach.

What is the biggest missed opportunity?

Opportunities missed tend to be those where we are not brave enough to break the normal conventions. They can also be where we don't open our minds to the views of those from other cultural backgrounds.

If we gave you some money to invest, where would you put it?

We ought to rethink Europe and try to make people appreciate landscapes and cultures closer to home. There is so much scope to improve the urban environment and create places where we can enjoy the simple pleasures of life that lift the soul.

Photo: Getty images. Illustration: Hai Knafo



DONALD TRUMP **Chairman and President,** **The Trump Organization,** **New York**

What will be the key themes for the future?

Luxury residential properties in New York City have seen record-breaking sales of late. This sector has carried the market in New York, and I think this trend will continue. For the future in general, I am very optimistic. Real estate always evens itself out in time.

What is the most positive trend at the moment?

The condominium market in Manhattan is doing very well and the momentum is there. There's a certain part of the market that remains immune to the highs and lows of the economy. As an example, I recently sold a \$34m apartment in Trump World Tower at United Nations Plaza.

And the most negative?

The foreclosure situation throughout the country has been a major problem, but it will resolve itself. There was a bubble for a while, and history has shown us that these trends come and go and repeat themselves. But the market will even out and once again be strong on many levels.

What is the biggest missed opportunity?

Not seeing the opportunity in the first place is the biggest missed opportunity. I always tell people that there are opportunities everywhere. When I



'For the future in general, I am very optimistic. Real estate always evens itself out in time'

first started out in real estate in Manhattan, I was repeatedly told that it was a terrible time to be doing so. If I'd listened to those people, I never would have started. So I reiterate: there are always opportunities, especially in bad markets.

If we gave you some money to invest, where would you put it?

I know real estate, so I'd invest it that way, probably in one of my Trump International Hotel and Tower condominiums in Las Vegas (above), Chicago or Dubai. Depending on how much you gave me, maybe all three.

High life: the Trump International Hotel and Tower opened in Las Vegas in March 2008

- How HNWI's decide where to live
- Why invest in property?
- Prime property and the wealth portfolio
- HNWI's and debt
- Agricultural land becomes a lifestyle choice ➤

ATTITUDES

Choosing residences

Decisions, decisions

How do HNWLs choose where to buy residential properties?

Researchers suffer from a love of order and a desire to segment markets and activities. HNWLs, however, tend to be more relaxed in their outlook. Our attempt to separate responses relating to second homes and primary residences struggled against the reality of property usage. In general, HNWLs do not differentiate between properties, and are especially flexible regarding prime and second home designations. For this reason, we have assessed both property types together in our Attitude Survey to understand the choices that HNWLs make when buying property.

A classic example that emerged from our survey was the case of a Brazilian/Russian family who owned apartments in New York, Geneva, Ibiza and, until recently, Singapore. They spend equal periods in each of their properties, with business and social ties meaning they find it possible to shift location for a long or short period with ease. In many ways, none of their properties was regarded as either a primary or secondary residence – in fact they feel equally at home in all of them.

Another reason for ambiguity between primary and secondary residences is due to significantly improved communications technology and the ease and speed of access to more remote locations. It is becoming increasingly difficult to tell the difference between a London resident director and another director who is taking care of business matters at his villa in Tuscany and flying to London weekly for key meetings.

Access options

The single most important factor influencing the location of primary and secondary residences for HNWLs is accessibility: 76% of interviewees identified this as one of main factors that determines HNWL choice of location for primary residences, and 71% named it as a main factor for second homes. Main determinants for accessibility were ease of access between their property and work or leisure time (59% primary, 35% secondary) and access to international airports (41% primary, 53% secondary).

HNWLs tend to measure accessibility in terms of travel time. An additional related factor that was mentioned is ease of crossing borders. One interviewee noted that 'if governments want to attract HNWLs they should make customs and immigration procedures efficient and at least mildly bearable'.

Security and stability

As we might expect, physical or property security, and politically related stability factors, also contribute to location choice (68% primary, 65% secondary). The main concern is personal security (53% primary, 47% secondary). Political, financial and economic stability were also frequently mentioned. One third of interviewees identified political safety as a concern for HNWLs. This was especially so for some emerging markets, pushing HNWLs to look to buy second homes in more secure foreign markets.

The importance placed on security features such as gated developments, electronic surveillance, concierge and security services for both primary and secondary residences was highlighted for properties in Latin America, eastern Europe and Russia in particular, but these features are growing in prominence across most global markets.

The notable decline in US purchase activity in European markets following the attack in September 2001 on the World Trade Center was felt to be a classic example of security concerns having an immediate and tangible impact on prime property markets. Interestingly, our interviewees noted one location, Australia, that had seen a noticeable upswing in interest from HNWLs. The location and size of this country is seen as somehow offering a secure location for second homes.

Staying connected

The importance of maintaining social networks is the fourth most important factor informing the choice of primary and secondary residences mentioned in our survey (38% primary, 35% secondary). HNWLs have a

Weekend retreat: the second home belt of Cape Cod is easily accessible from New York



How many residences do HNWLs own?

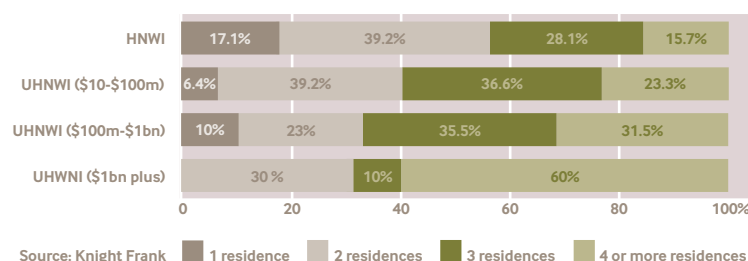


Photo: Alamy



It is increasingly difficult to tell the difference between a London resident director and another who is taking care of business at his villa in Tuscany and flying to London for key meetings

strong desire to live in an environment where, even if they are not close to immediate friends and family, they are at least close to social, economic, national or linguistic peer groups.

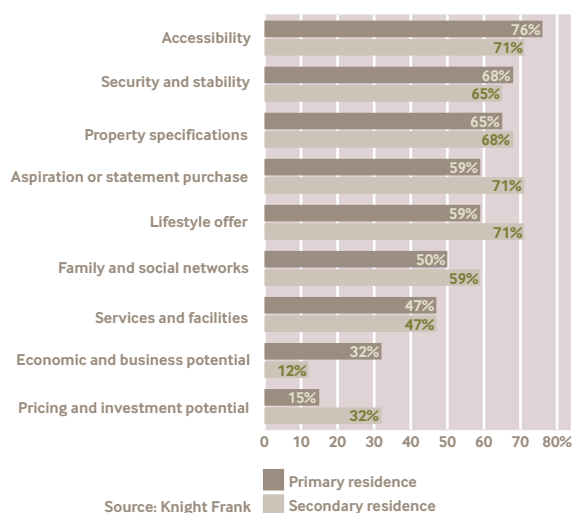
Good examples of this trend are the Russians who buy second homes and holiday homes in central and eastern European countries – locations with a shared cultural and historic heritage. Similarly, in the Greek islands there is some evidence of HNWI clustering by nationality, with Greek HNWIs concentrating in Mykonos, Germans in Crete and British buyers in Cyprus.

A fascinating microcosm of this trend is currently being seen in London, with the clustering of European buyers in Chelsea and Kensington, Russians and Middle Eastern buyers in Belgravia and Knightsbridge, and buyers from the US in Mayfair. We need to accept that micro-market concentrations of buyers are less fixed than, say, a desire to be on one island

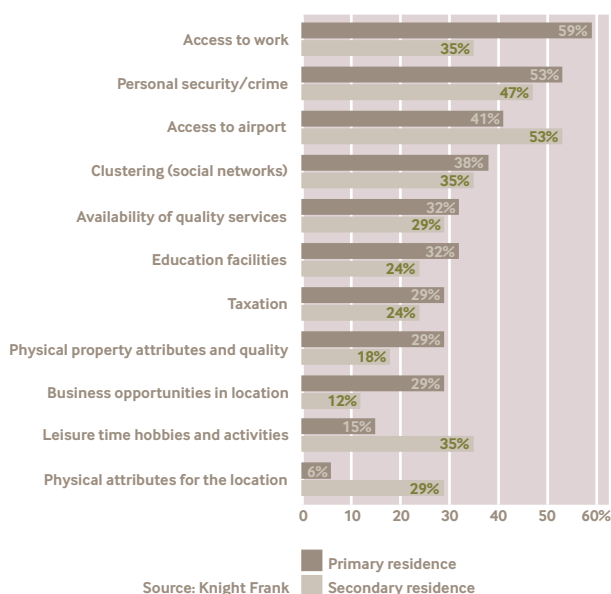
ATTITUDES

Choosing residences

What are the most important factors influencing the location of a primary residence or a second home?



What are the most important individual factors influencing the location of a primary residence or a second home?



or another. At this end of the market, HNWIs tend to live wherever it is that they want to within certain constraints. What they require are well-connected places close to the facilities and people they need to be in contact with.

Education proximity

A significant driver for buyers with school or university age children is education. University or college cities in the UK, US and Europe are particular targets, especially Ivy League institutions in the US, and Cambridge and Oxford in the UK. The desire to provide an English language education places a premium on Anglosphere locations. Almost a third of respondents referred to educational facilities as being one of the main factors driving location decisions for HNWIs.

The popularity of these Western educational centres is now rivalled by a growing number of institutions offering MBA and other business

Northern Europeans, especially the Irish and British, place a high degree of importance on the ownership of a second home

courses in the Middle East and Asia. INSEAD, CASS, Rutgers and the London Business School now offer business courses in these regions.

Several local Asian and Middle Eastern universities have also started their own MBAs and are working hard to raise their profile. These efforts are already yielding results. In 2007, 11 Asian MBA programmes were included in the Economist Intelligence Unit's top 100 MBAs.

Wealth display

Second homes often need to fulfil additional requirements, such as the provision of an aspirational or statement purchase. They allow purchasers to display their achievements, according to 71% of our interviewees in relation to second homes. There is a degree of cultural difference in the importance placed on second home ownership.

Northern Europeans, especially the Irish and British, place a high degree of importance on the ownership of a second home, and the need for a

home in the sun is very high for HNWIs from colder climes in general. However, even in locations such as Brazil where there is no rationing of good weather, the cultural drive for second homes ownership still remains strong. Many second home purchases are viewed as prestige or trophy properties.

Our interviewees identified that HNWIs expect to have access to excellent leisure services, either in their own residences or at least in the immediate vicinity (32% primary, 29% secondary).

What constitutes accessibility?

Accessibility is generally viewed as a combination of travel time and ease of access. Ease of access was variously described as including time spent changing transport – from, say, car to plane – and in navigating customs, security and immigration. Our survey showed that for a primary residence to be accessible, a maximum daily journey time to a place of work should be between one and one and a half hours.

Other accessibility requirements are placed on homes. Assuming they are not boarding, children should be able to reach school within 15 to 20 minutes, and even rural homes should be within a 20- to 30-minute drive of a decent selection of restaurants and bars.

Second homes were divided into frequent stay, or weekend homes, and longer haul homes used seasonally, such as summer residences. For the former, our interviewees reported that these homes should be no further than two hours from the office and/or primary residence. For the longer haul property, travel time still rules. Our survey suggested that for HNWIs, the usually accepted travel time to more distant second home locations is around four hours.

Further than this and the use of the property declines sharply.

However, there are exceptions. A third tier of second homes was also identified. These require an ultra long-haul journey, with 10 hours being the accepted travel time limit. Such properties are likely to be used only occasionally but for longer time periods – think of island locations in the Indian Ocean.

Assuming they are not boarding, children should be able to reach school within 15 to 20 minutes

INSIDER INTERVIEW



DAVID LLOYD
Chairman, David Lloyd
Ownership Resorts

What are the key themes for the future?

Over the next seven to eight years, people will be looking to emerging markets such as Brazil, Grenada, Mexico and Thailand for property investment. These are locations that haven't been fully exploited so far. They have stable economic and political environments, and they compare very favourably with the high prices demanded in the UK, Europe and US.

What is the most positive current trend?

The vast improvements that have been made to international infrastructure, and the welcoming attitude of local and national governments in emerging countries to approaches from high-end developers.

And the most negative?

Everything is getting so expensive today – not just property but everyday consumer goods, too.

What is the biggest missed opportunity?

I think China is a growing opportunity that could be missed. However, you need to develop a good relationship with a Chinese business partner on the ground to provide advice and direction.

If we gave you some money to invest, where would you put it?

I'd buy and develop in Grenada and Asia, as they offer the greatest opportunities for growth, are unspoilt and have wonderful climates.

ATTITUDES

Property investments



The property picture

What positions are HNWLs taking on the market?

HNWLs have a high regard for property-led investments, according to our Attitude Survey. With its proven performance and the belief that it is a good hedge against inflation, property is seen as an investment for which performance can be influenced directly through management and improvements unlike equities or gilts, which are regarded as passive investments.

More than 50% of HNWLs invest in property to some degree. The main aim is strong capital growth. Reflecting weaker conditions in many residential markets, target rates of capital growth were variously placed at between 7% and 12% per annum, which represents a slight reduction from last year's results when the range was 8% to 15%.

Rental returns were again regarded as being less significant for most HNWI investors when compared with capital growth. Last year we noted that the main objective was that rents should allow for investments

to cover costs. This sentiment was again repeated, although there was a shift, with investors beginning to plan for lower capital growth and to look at means of enhancing rental income. Despite a long-term investment strategy, portfolio liquidity is key for most HNWLs, with considerable importance placed on planning for market exit strategies.

Last year's UK-based survey revealed a notable local investment pattern when it came to direct investments. This reflects a desire for easy access to properties for inspection, and also a belief that investors should pick areas they know well. The results of this year's survey are similar. Most HNWLs (67%) around the world hold direct investments in their main country of residence. However, there is a more confident outlook from Asian, Australian and African investors, around 40% of whom have bought a direct investment outside their own country – in particular in the US, UK and Middle East.

Over recent years, there has been increasing availability of information regarding global residential market performance. Despite this improvement in market transparency, there is still a long way to go for this sector to match the ease of analysis available

Growing interest: a plantation in Argentina, where agricultural land is attracting attention

in, for example, the equity markets. HNWLs commonly will avoid direct investment in markets with which they are unfamiliar. This applies not only to residential but also commercial and agricultural markets.

Outside of direct investment purchases, our survey results revealed that only 25% of second-home purchases and 10% of primary-home purchases had investment potential (generally through capital growth) as the lead driver for purchase.

Identifying trends

The general perception was that most HNWLs were relatively well-informed regarding broad housing market trends. The recent US housing market downturn offered little surprise for most investors. There was some acceptance that there were several other markets – Ireland and parts of Spain were mentioned – where prices had run too far ahead and would experience a market slowdown.

In terms of location and stock picking, most HNWLs have confidence in their ability to stay ahead of market trends. There is a general belief that while low inflation and interest rates cannot be taken for granted, there is little danger of a return to a high interest rate environment, and a related knock on asset prices. There is a noticeable desire in the US, Europe and the Middle East for more information about investment opportunities in Asia, where the limited market information currently available appears to point to significant future growth potential.

Prime preference

We noted in last year's study that there was a bias among HNWL investors towards prime market exposure. This is confirmed again this year, with most respondents (59%) noting that in their experience HNWLs tend to target established prime or super prime markets as opposed to emerging markets.

The attitudes of HNWLs towards investment risk varies considerably. Respondents were asked to grade attitudes to investment risk, and the response was that 32% of HNWLs were described as having aggressive investment strategies. Their objective is to maintain very thin strips of equity and to achieve highly leveraged returns from residential property: 40% were described as holding a medium risk outlook, and 28% as having a low or very low risk tolerance. Many among this group held no investment properties.

Commercial considerations

The generally positive attitude towards residential investments was repeated for commercial property.

In terms
of location
and stock
picking,
most
HNWLs
have
confidence
in their
ability to
stay ahead
of the
market

HNWLs who are exposed to direct commercial property investments have a mix of long-term investment holdings based on a total investment return strategy, and short-term development opportunity-led options that are adhered to when circumstances and opportunities present themselves. Interviewees in Russia, Ukraine, China and Africa pointed to the opportunities afforded by a lack of quality office and other commercial space in these markets. HNWLs in these countries are often heavily involved directly in the property sector, or in business sectors exposed to property development. These HNWLs use their professional knowledge and acumen to aid the performance of their personal investments.

There is a lower tendency for HNWLs with no direct professional exposure to the commercial property sector to access this market in a personal capacity, compared to residential property. Residential property is viewed as more accessible by the amateur investor.

Agricultural interests

There has been a noticeable increase in interest in agricultural property investment in recent years. Aside from the obvious potential returns from record commodity prices, two clear drivers are encouraging HNWLs to access this market, according to our survey. Firstly, the available tax incentives in parts of Europe and Australia make investment in this sector attractive. Secondly, there are strong cultural reasons, especially for HNWLs from Argentina and Brazil, who historically have close links to land ownership.

As with commercial property, there are HNWLs who want to invest in this sector because they have a high level of technical market knowledge. However, there is a more common route for access. This is so-called lifestyle ownership, where agricultural or forestry land is purchased primarily for residential property enhancement rather than as a pure investment asset.

In the UK, this is a very mature market. Figures from the Knight Frank Farmland Index reveal that the single largest group of purchasers in 2007 were lifestyle buyers. In the UK, non-farming buyers account for 37% of all agricultural land sold.

Funds are the preferred route for investment in both commercial real estate and residential property in emerging economies. Managing agriculture and forestry land investments can be labour- and knowledge-intensive, so HNWLs widely use management companies and indirect investment routes. These have been used to access otherwise restricted property markets, such as China and Vietnam, where direct ownership by foreign HNWLs is extremely limited.

ATTITUDES

Wealth portfolio

A concrete investment

We assess how important property is to HNWIs as part of their investment portfolio

While there is no typical HNW portfolio, many HNWIs display an exuberant attitude towards property, with more than 80% of their wealth allocated to this asset class. At the other end of the scale, there are some HNWIs who would rather invest in their passion for art, and serial entrepreneurs whose portfolios are divided between speculative investments and their own business ventures, with only their primary residence as a solitary property asset.

Despite this, our Attitude Survey revealed some clear trends. Looking at HNW investment activity from the countries represented, property, including primary residences, accounts for approximately 38% of HNW asset allocation – and in the UK it is higher still at 41%. The UK HNW is not alone in his love of property – Irish, northern European and Israeli portfolios all displayed significantly higher than average exposure to property.

Further dissecting the property element of the portfolio, 13% of total asset value is held in the primary residence, 8% in secondary residences, 8% in residential investment properties, 7% in direct commercial, agricultural and other property, and 2% in indirect property investments.

HNWIs normally own their primary, secondary and holiday homes directly, although commonly offshore trusts or similar vehicles are used to optimise tax efficiencies. If a HNW is interested in property investment, they will often have a private property portfolio in addition to the properties managed by their asset managers.

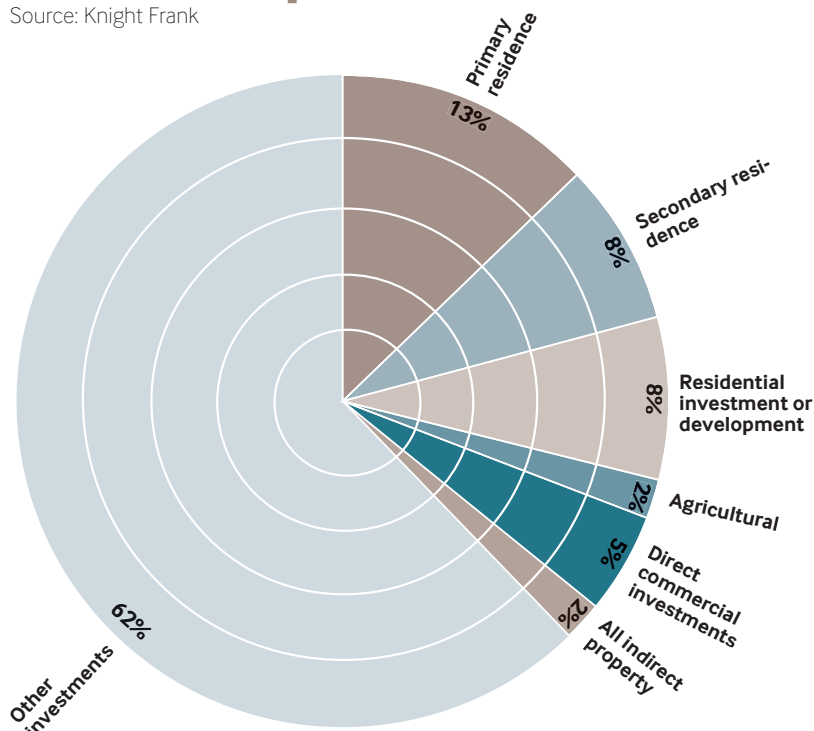
These shadow portfolios enable HNWIs to participate in markets, such as direct residential investments, which asset managers can't provide. Generally they will cover investments where the key incentive is personal, especially homes bought for children in higher education.

Positive attitude

HNWIs have retained their positive attitude to property investment over the past year. We stated in our 2007 report that there was a desire to increase their portfolio weighting in property, especially indirect investments. This desire to gain more exposure to commercial and residential property markets is especially noticeable in

Global HNWIs' property as a percentage of their wealth portfolio

Source: Knight Frank

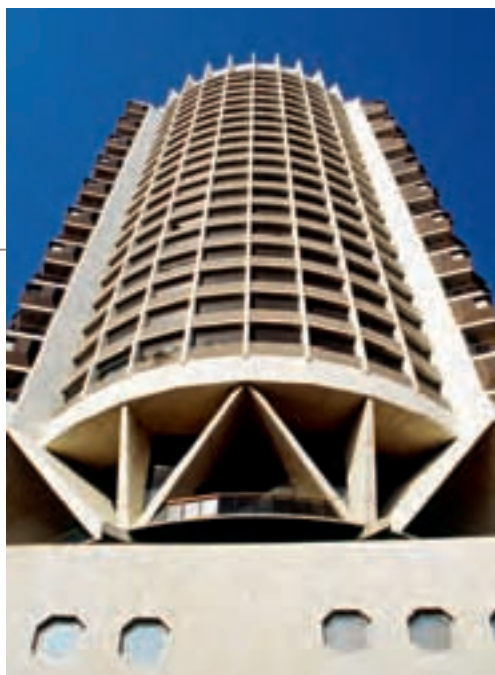


HNWIs' generally positive view of emerging economy opportunities. Our survey this year revealed that HNWIs will probably look to increase their exposure to property from 38% to closer to 40% of portfolio weighting over the next 12 to 18 months, partially due to a desire to reduce equity holdings.

Interestingly, the wealthier an individual the less significant property assets become as a share of the overall portfolio. UHNWIs with assets of more than \$1bn allocate only 15 to 20% of their assets to property, while HNWIs with assets of less than \$10m allocate over 40% to property. The value of primary residences accounts for a large part of the differential. It is easy for someone with \$10m to spend \$3m on their main house, but almost impossible for someone with \$1bn to spend \$300m on theirs.

Only 11% of HNWIs have a sole primary residence with no second home, 33% have one second home, 31% have two, and 25% have three or more. There are significant differences across the wealth spectrum, as we might expect, with greater wealth resulting in

HNWIs have retained their positive attitude to property investment over the last year



Building trust: the portfolios of HNWI's from the UK, Ireland, northern Europe and Israel all have far higher than average exposure to property



more second homes. UHNWIs with above \$100m rarely, if ever, have only a primary residence.

Mortgage manoeuvres

Surely UHNWIs don't need to get into debt to buy property, but it's surprising how many make use of a mortgage. In terms of the HNWI residential property portfolio, the split between debt and equity, including the primary residence, is 38% to 62% respectively. Primary residences are commonly less heavily leveraged, unless there is a significant opportunity for interest rate arbitrage or tax incentives. In approximately a third of all cases, primary residences are owned outright with no debt.

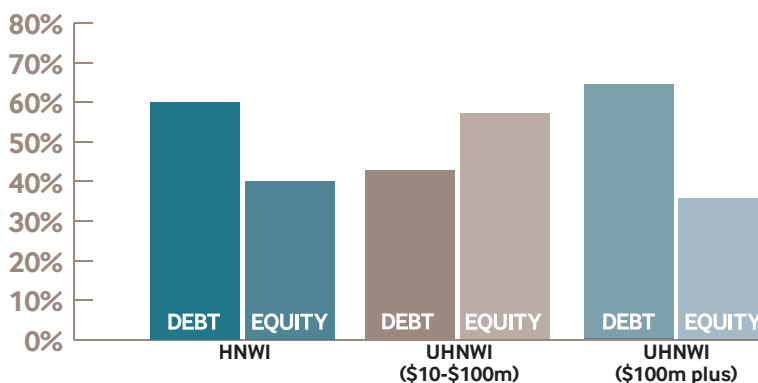
If we exclude the primary residence from the equation, the split between debt and equity in our 2008 Attitude Survey was 60% to 40%. For UHNWIs with wealth of more than \$100m, it was 64% to 36%.

Second homes and investments tend to be more highly geared, with the investor looking to exploit investment opportunities elsewhere in their portfolio.

The propensity to make use of debt is a function of HNWI professionalism in investment markets. This was uncovered in our survey by the observation that UHNWIs tend to have the most leverage, even though they obviously have less need for access to finance. In several emerging economies, mortgage markets are somewhat undeveloped, and it can be relatively expensive to make use of mortgage debt. The main reasons for using debt are the provision of alternative routes to investment, tax benefits and interest rate arbitrage.

How do HNWI's finance their property holdings?

Source: Knight Frank





SOU FUJIMOTO **Sou Fujimoto** **Architects, Tokyo**

What will be the key themes for the future in residential property?

To understand where innovative architecture is going, we need to reflect on primitive architecture. There are lessons for us to learn from the first built forms that emerged through human activity.

Consider the origins of the nest and cave. A nest is prepared according to inhabitants' sense of comfort and needs, while a cave exists regardless of convenience or otherwise for its inhabitants.

It is not organisation in the name of functionalism but place-making that encourages people to discover new opportunities. I search for an ideal condition of new architecture between artifice and nature. My Primitive Future house is full of promising projections.

What is the most positive trend at the moment? And the most negative?

These questions are two sides of the same coin. The most positive trend is the almost universal consensus that architecture must be part of a sustainable future. It must address issues of lower energy usage, pollution and so on, and also look again at the conditions in which humanity and nature can coexist. This will require current limitations of eco architecture to be transcended.

These are important themes in architecture that address functional and pragmatic necessities, but they fall short of a more fundamental change in living



‘Architecture must look again at the conditions in which humanity and nature can coexist’

conditions that would make people want to live in harmony with nature.

I often say that obstacles make people aware of their environment, meaning that the notion of obstacles, or rather surfaces of discovery, makes possible ways in which people can reassess themselves, interpret the landscape, reorganise their life patterns accordingly, then come to a new level of existence that would have been unimaginable up to that point.

What is the biggest missed opportunity?

Every project that falls through is a big missed opportunity at the moment.

If we gave you some money to invest, where would you put it?

In people, places and papers – or, in other words, employees, locations, research and knowledge.

Living proof: Fujimoto's visionary housing design is evident from a model of his Tokyo Apartment project

- The world's best prime market performers
- Emerging locations
- London and Manhattan continue to stride ahead
- Hot spots in Africa, Asia and South America ➤

PERFORMANCE

Prime property

Location reports

How has prime residential property performed worldwide?

First introduced in last year's Wealth Report, the Knight Frank Prime International Residential Index (PIRI) is the only index that tracks prime residential property markets across the globe. The data used is based on a selection of residential properties in prime market locations, which are valued on a structured basis, capturing changes in capital values, rents and yields. A total of 100 locations are included in the index, which represents an increase from the 74 in last year's report. All prices are captured in local currencies to remove the impact of currency change on our calculation of price growth.

Average change in capital values of prime property on a global basis was 11% between Q4 2006 and Q4 2007. The first area of strong growth was in the emerging economies, especially China, and central and eastern Europe. The second main area of strong growth was in the global financial centres and key second-home hot spots in France, Italy and the Caribbean, helping to prove that plutonomy is alive and well (see page 6).

Beyond the world financial capitals, the developed economies delivered relatively lacklustre price growth in the prime residential markets, with North America (excluding Manhattan) seeing growth of only 2% overall and western Europe only 4-5%. As growth at this rate is at only a little above inflation, in real terms it was practically zero in many locations.

Emerging markets

Top locations for price growth were a mix of second home locations and key prime cities, with Antigua and St Jean Cap Ferrat in France leading the table. These top-performing sunbelt locations were closely followed by St Petersburg and Moscow, where the rate of growth was 38% and 35% respectively in 2007 (compared with 95% and 75% in 2006).

The fall in the rate of growth in the Russian centres reflects more sustainable market conditions. However, there remains a lack of prime residential properties in major Russian cities as a result of strong growth in private wealth. The supply and demand imbalance has shifted to the mass affluent market across the big cities, where one of the central problems is a lack of suitable construction opportunities.

Strong economic growth and an ongoing increase in industrial production and trade have helped near neighbours Guangzhou in China and Hong Kong to

Port of call: St Jean Cap Ferrat is a top-performing sunbelt location



▲
40%
Antigua achieved the highest growth

take eighth and fourteenth position on our growth ranking, with 28% and 21% growth being achieved respectively. Meanwhile, the rate of price appreciation has eased from 29% to 16% in Beijing, and 16% to 4% in Shanghai.

In Ukraine, as in Russia and China, the supply and demand imbalance has driven prices higher. In 2006, price growth hit 72% in Kiev, while in 2007 it fell to a

still respectable 17%. In the past – and to some extent even now – one of the major factors in capital value growth has been immaturity of other asset markets. Real estate has offered a way to invest and increase wealth meaningfully.

Prime city markets in Poland demonstrate trends in former Eastern Bloc countries. In Warsaw, increasing demand for higher quality residences means prices were pushed up 10% in 2007. In the middle-tier market, demand is likely to grow as Soviet-era buildings become increasingly obsolete.

Again in central and eastern Europe, there is growing interest in holiday-home and second-home locations. Not only western Europeans are buying, but also Russians and Poles. The prices of some new developments in the Bulgarian Black Sea region grew by 20%, although the typical rate of price growth in Bulgaria and Croatia was around 10%. In the Balkans, demand increasingly comes from Russia, Greece and northern Europe.

Affordability is key in these locations. In the Obzor region of Bulgaria, prices stand at around €1,220 per square metre.

Photo: Alamy. Illustration: Hai Knafo

PIRI top 10, average price growth for prime residential property, 12 months to December 2007

Location	Country	Capital value growth
Antigua	Antigua	40%
St Jean Cap Ferrat	France	39%
St Petersburg	Russia	38%
Moscow	Russia	35%
Singapore	Singapore	31%
London	UK	29%
Guangzhou	China	28%
New York	USA	25%
Monaco	Monaco	25%
Dubai	UAE	24%

Source: Knight Frank

PIRI bottom 10, average price growth for prime residential property, 12 months to December 2007

Location	Country	Capital value growth
Gascony	France	0%
Dar Es Salaam	Tanzania	0%
Helsinki	Finland	0%
Chianti	Italy	-1%
Krakow	Poland	-1%
San Diego	USA	-2%
Palm Beach	USA	-3%
Noosa Heads	Australia	-7%
Ibiza	Spain	-13%
Dublin	Ireland	-15%

Source: Knight Frank

▼
15%
Prices fell
by the
highest rate
in **Dublin**

INSIDER INTERVIEW



ROGER ORF
Head of International
Investment for Europe
and Asia, Citi Property
Investors, London

What will be the key themes for the future in residential property?

The credit crunch is having a major impact on world markets. There is no doubt the sub-prime mortgage crisis in the US has had a dramatic impact on value. I don't expect it to settle down until 2013.

What do you think is the most positive trend at the moment? And the most negative?

There is little to be optimistic about. The Federal Reserve is behind the curve. It may take a year or two for recent rate cuts to feed through the system to the point where we can see a significant positive impact on the market. The problem in Europe is led by the currency and the impact of the one-size-fits-all effect: not all countries have the same inflation rates, and the European Central Bank's interest rate is simply not flexible enough to accommodate this.

What is the biggest missed opportunity?

In Asia India and China in particular there is huge growth that will continue for some time. Investing rather than speculating in these locations will mean you will outperform the market in the West.

If we gave you some money to invest, where would you put it?

Agricultural land is the best bet, because of the rise in commodity prices and expanding populations.

PERFORMANCE

Prime property

Capital gains

Super prime residential properties in London and Manhattan continue to rise substantially in value

Capital value growth has been strong in the global financial centres and low tax jurisdictions. Five of the top 10 high growth locations in 2007 were in this group. The strongest performer was London, which saw 29% growth, with average prime values reaching €46,000 per square metre. Other financial centres in the top 10 include Singapore (31%), New York and Dubai (25% and 24% respectively).

Low tax jurisdictions were very successful in 2007. Monaco saw 25% price growth, meaning that prices now stand at almost €44,000 per square metre. Geneva saw 15% price growth and Barbados 12%.

In London, newbuild developments have continued to lead the market in terms of prices. Not only have developments in Belgravia and Knightsbridge broken the €60,000 per square metre barrier, but prices for some newbuild apartments have also nudged €80,000 per square metre. The credit crunch and world financial market turmoil meant that purchasers

Prices for prime Manhattan properties rose by 25% in the 12 months to December

Thriller villas: London's super prime market remains strong



held back from buying in September and October. By November, however, there was a return of confidence, with sales beginning again and volumes at a five-month high.

An example of the strength of the prime market in London is that the number of £10m-plus (€13m-plus) sales in Chelsea, Knightsbridge and Belgravia rose by 190% in the six months to January 2008 compared with the same period a year earlier. Whereas €38,000 per square metre represented the peak of the market in Knightsbridge in 2006, 18 months later €60,000 per square metre is not just achievable but expected for refurbished and newly developed properties in the super prime sector.

We all know that London has enjoyed a boom in top-end property in recent years. Since September, the prime and mainstream markets have slowed and activity and price growth should slow further into 2008, but at the top end of the market there has been no such slowdown. So why has this £10m-plus sector remained so strong?

Despite the credit crunch, extraordinary wealth creation has continued across the global oil and commodity sectors. Far from being dead, the financial market still provides huge rewards. Energy and commodity prices are under sustained upwards pressure and future wealth generation can be expected in these sectors through 2008.

In prime central London, prices rose by a total of 29% in the year to the end of December 2007 – a remarkable result – but prices for properties valued above £10m rose by more than 37% in the same period. In the final quarter of 2007, when price growth for all property slowed considerably and prime central London managed only 1.4%, prices for the £10m-plus bracket still managed 3.8%.

The dislocation of London's top-end market has been replicated in the other global super prime markets: Manhattan and Monaco. Whereas prices in the US fell by 4.5% over the past year, and by 4.2% in New York generally, prices for prime Manhattan properties rose by 25% in the year to December. In Monaco the same pattern has been seen, with prices overall rising by 25%, and properties priced at more than €10m rising by close to 30%.

With the UK market generally in a more sombre mood, the strong performance of the super prime market has been thrown into even sharper relief. Does the divergence of performance mean we are close to the peak of the super prime market? Our view is that fundamental economic arguments point to continued support for this sector. Demand is not going to evaporate, and wealth creation and

Top 35 PIRI average prices for residential property, December 2007 (source: Knight Frank)

Location	£ per sq ft	\$ per sq ft	€ per sq m
London, UK	3,025	6,191	46,000
Monaco	2,877	5,888	43,750
St Jean Cap Ferrat, France	2,860	5,853	43,490
Courchevel, France	2,302	4,710	35,000
Hong Kong, China	2,207	4,507	33,458
Manhattan, USA	2,111	4,320	32,100
Cortina d'Ampezzo, Italy	1,480	3,028	22,500
Portofino, Italy	1,315	2,692	20,000
Singapore	1,187	2,423	17,990
Tokyo, Japan	1,141	2,334	17,345
Verbier (new developments), Switzerland	1,136	2,325	17,273
Moscow, Russia	1,092	2,235	16,610
St Tropez, France	1,029	2,106	15,650
St Petersburg, Russia	946	1,937	14,390
Sydney, Australia	941	1,926	14,310
Paris, France	915	1,872	13,910
Verbier, Switzerland	884	1,809	13,440
Rome, Italy	859	1,758	13,060
Gstaad, Switzerland	792	1,622	12,050
Venice, Italy	753	1,541	11,450
Valais, Switzerland	671	1,373	10,200
Geneva, Switzerland	605	1,238	9,200
Florence, Italy	580	1,187	8,820
Barbados	562	1,151	8,550
Surrey, UK	560	1,147	8,520
Madrid, Spain	517	1,058	7,860
Côte d'Azur, France	510	1,044	7,760
Buckinghamshire, UK	500	1,023	7,600
Hampshire, UK	487	997	7,410
Mallorca, Spain	475	973	7,230
Bermuda	475	972	7,220
Edinburgh, UK	450	921	6,840
Milan, Italy	449	919	6,830
Berkshire, UK	434	888	6,600
Chianti, Italy	425	869	6,460

accumulation in emerging economies and high-end service sector activities will also continue.

Western Europe

With the significant exception of London, the main Swiss centres and Monaco, most European locations saw price growth well below the global average. Dublin (-15%) and Ibiza (-13%) saw the biggest price declines overall. European markets have to some extent stagnated, due in part to high price growth in previous years squeezing affordability and also the slowdown in the Eurozone economy.

Africa, Asia and Australia

Capital values in Marrakech have increased by 12%. Low initial prices, together with rapid improvements in the local economy, have also yielded significant price growth in other African markets. In Botswana, for instance, growth was 25% in 2007 for prime landed properties. Prime markets in Asia are benefiting from significant economic growth. There are ripple effects in the local economy and this boosts local demand. Malaysia, for example, has seen growth at 22%.

Australian prime residential markets have seen a solid performance in recent years. After the market slowdown in 2004 and 2005, prime market locations in Sydney and elsewhere have seen fairly constant growth in demand. Prices rose by around 9% in both prime Sydney and prime Gold Coast locations.

The US and South America

With the notable exception of Manhattan, the prime markets in the US did not experience an especially strong performance in 2007. Pulled down by ongoing problems in the mainstream US market, the prime markets managed growth at or around only 2%. The weak dollar has increased the attractiveness of Caribbean destinations for non-American buyers. As a result, prices rose steadily in Barbados (12%) and the Cayman Islands (9%). The star performer was Antigua, which saw price growth at more than 40% through the year.

Brazil is seeing healthy growth in the prime residential markets. For example, São Paulo saw 8% growth in prices during 2007 following strong growth in 2005 and 2006. With prices for prime property standing at an average of only €1,520 per square metre, there is considerable room for growth over the next few years. So, although lenders have been widening access to mortgage finance and developers have increased newbuild supply over time, there now appears to be only a limited risk of a bubble developing in the prime city and coastal markets.



NICK CANDY
Director,
Candy & Candy,
London

What will be the key themes for the future in residential property?

To create something exceptional you need to take a layered approach, combining an elite team of iconic architects, interior designers, artists and luxury service providers with an outstanding location to make the ultimate luxury-living experience.

What do you think is the most positive trend at the moment?

People take comfort from knowing they own the best. Even if it is perceived that you are paying too much at the outset, if you buy quality I'm a firm believer that you will have made the best investment in the long term. In the current market there is a flight towards quality, as people look for long-term homes which they know they will enjoy living in.

And the most negative?

Dealing with public authorities in London can be frustrating. While local planning authorities are cooperative, other bodies often make things challenging, especially in relation to traffic organisation around Knightsbridge, where we are working hard to minimise disruption to the travelling public as we build One Hyde Park (see projection, right). This is only one

example of bureaucracy. If we're not careful, London will be overtaken by other global cities.

What is the biggest missed opportunity?

We spend our every waking moment making sure that we never miss an opportunity. Every step of the way our decisions are calculated and extensively researched. We don't do it on our own: we employ the best professionals across the design and development industry, and always have our finger on the pulse to make sure that we can move swiftly to take advantage of any relevant prospect.

If we gave you some money to invest, where would you put it?

It would have to be property in the golden postcodes of prime central London: Knightsbridge, Belgravia, Mayfair and Chelsea. I believe the capital has never stood on firmer bricks.

'I'm a firm believer that if you buy quality you will have made the best investment in the long term'



£959 million was paid for Chelsea Barracks, Britain's most expensive residential building site. Candy & Candy are its development managers and interior designers.

- Iconic architecture
- The home as a hotel
- Bespoke interiors
- The greening of HNWIs
- Farmland faces pressure
- New property hot spots ➤

TRENDS

Residential

Service providers

Hotel like facilities and striking architecture add to the desirability of a property

In an increasingly crowded marketplace, developers have had to find innovative ways to make their projects stand out. One way is by commissioning bold architecture. Selecting the right architect has become critical for some, and world-renowned practices such as Foster and Partners, Gehry Partners and Rogers Stirk Harbour and Partners have become synonymous with iconic projects. The so-called 'image transfer' from designers and architects to developments has become an increasingly important asset in the prime residential and hotel sectors.

A growing trend seen in London, New York and other key world centres is for residential development to borrow design statements from hotels, especially from boutique hotels. Modern hotel design is arguably more bold, imaginative and inventive than any other development genre.

Residential developers are learning a key lesson from hotels. In emerging or market-making locations where a prime scheme might be the first high-quality project, hotel developers understand the need to make the hotel or wider development act as the initial destination. To do this they provide bars, restaurants and other facilities to create the initial gentrification that encourages purchasers to develop a belief in an area. Expect to see more of this self-reliant gentrification in emerging locations in big cities including New York and Tokyo.

So long as they compete for business and wealth creation, cities will keep pushing for grandiose new statements. Two-fifths of the world's present stock of high-rise residential towers were built since 2000, and we can expect to see many more in the near future. Claims and counter claims for Europe's or Asia's or the world's tallest residential tower will be with us for some time.

The trend for residential developers to learn from hotels doesn't stop at design features. One of the biggest changes in prime market developments over recent years has been the inclusion of facilities and services that once would have been thought to belong only in a hotel. Our Attitude Survey shows that as the number of HNWIs with several homes grows, so too does a need for management and maintenance services. Residents in the best new developments are beginning to expect 24-hour concierge and security, biometric scans for access, private elevators from

Two-fifths of the world's present stock of high-rise residential towers were built since 2000



secure underground parking, rubber-coated parking sites for vehicle protection, laundry service, theatre and restaurant booking, and a shopping-ordering service. Some developments, especially in the US and Asia, even have individual 'white glove' butler services.

In many countries, HNWIs increasingly expect extensive leisure and health facilities, too. Levels of provision for health, relaxation and wellness are once again informed by the services on offer in the

Bold fashioned: the Frank Gehry-designed hotel at the Marqués de Riscal bodega in Rioja, Spain. Striking architecture is in fashion

best hotels. The blurring of the boundaries between hotel and residential development continues, with residential properties offering managed dining rooms, climate-controlled wine cellars, private screening and cinema rooms, swimming pools and saunas.

World of interiors

Lori Campbell identifies two key areas where the luxury market is seeing increased activity

Bespoke luxury and stealth purchases

Specialist bespoke design services have grown significantly over the past decade. A step up from an interior design service, this option allows for every element to be created afresh for each project.

There has been a notable widening in the range of HNWI purchasers willing to take up this option. It is difficult to escape the fact that luxury interior goods and furnishings have suffered from the impact of mass affluence. Even the most expensive off-the-peg interiors appear not to offer the necessary difference for some purchasers, and the bespoke route – already a favourite with boutique hotels and upscale brands such as Candy & Candy – is a growing trend.

The high-end consumer who takes up the bespoke option effectively exercises the opportunity to have a say in every detail of their home and interior purchase. There is a mix of honesty and secrecy to bespoke design. There is a desire to show more of your own ideas and character through the bespoke process, which is necessarily quite a revealing one, but for other purchasers, of course, there is a difficulty in replicating the overall look – the stealth element.

This trend is leading to a greater emphasis on craftsmanship and the longevity of furnishing – through the use of quality materials – and is also allowing for greater experimental production. The results are often very original.

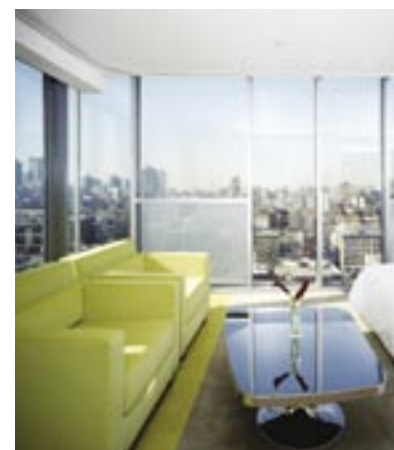
Rise of the flexible third space

The third space concept has been developing over recent years within the home – or at least next to, above or below it. There is a trend in luxury newbuilds and refurbishments towards the creation of a social space separate from the ubiquitous open-plan kitchen/dining area. Landscaped gardens with all-weather shelter suitable for socialising, including tree houses and garden retreats, will be more noticeable in the future.

For those purchasing high-end urban properties, this trend is to be seen in rooftop zones. There will be an increasing push towards the greening of roofscapes and the creation of rooftop gardens to offer third spaces in more confined circumstances.

■ Lori Campbell is Interior Designer and Space Planner at Knight Frank. She has been watching design trends for several years and publishes Interior Trends, an annual guide to the luxury marketplace.

Staying power: bespoke interiors, often influenced by boutique hotels, are becoming HNWI must-haves



‘The high-end consumer who takes up the bespoke option has a say in every detail of their home’

TRENDS

Environment and agriculture

Going green

Is climate change affecting the behaviour of HNWI's?

More than a third of respondents to our Attitude Survey said HNWI's have changed their behaviour as a result of climate change. Not surprisingly, the HNWI's most active in this regard live in areas with real and immediate environmental concerns. In California, Australia and Italy, residents are installing equipment to save energy and water. In two cases reported to us, HNWI's were remodelling properties to do so.

One of the biggest issues for HNWI's is how to maintain an existing high quality lifestyle while making environmentally aware choices. This is not the insoluble problem that it might seem. Meeting the challenge of reducing carbon usage, without producing a compromise on lifestyle, is one of the strongest incentives for innovation in design.

Over half of HNWI's are not yet making significant changes to their behaviour regarding climate change. When pushed for reasons, the respondents collectively said that climate change had yet to have a serious effect on the cost of living. Outside of locations suffering droughts or increased flood risk, it is still not affecting the ability of HNWI's to maintain their lifestyles.

Saving energy

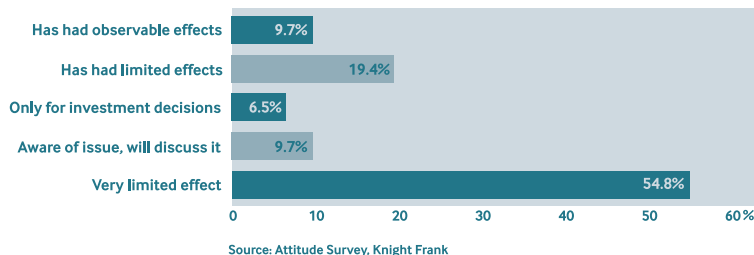
Developers are seeking to build greener second homes

Describing a second home as 'sustainable' is something of a misnomer, especially when you consider the extra travel required to visit a property. However, developers and architects are attempting to reduce the environmental impact of second homes. The simplest method is carbon offsetting

by planting trees for example. The more complex approach is to reduce overall use of energy and water.

Countless developers have adopted this second approach and are recycling materials and rainwater, implementing planting schemes to provide shade to naturally lower temperature, and creating on-site energy production, for instance. Innovations in this field hold out the hope for more significant gains in energy efficiency over future years. Designers and architects are increasingly motivated by the need to make developments fully sustainable, partially due to market demand, but in reality government policy imperatives are at least as important.

Has climate change affected HNWI behaviour?



Under pressure

As the supply of agricultural land declines, demand rises

It doesn't seem long since the biggest issue regarding farmland in the developed world was overproduction. Today there is far less concern about surpluses and more about the threat to supply. Two key themes emerge from our World Farmland Survey: first, the loss of productive land through development and degradation of quality; and second, rising demand for agricultural production for food and non-food crops.

The amount of available farmland is falling globally. In China, for example, over the five years to 2006, 26,000 square kilometres (10,000 square miles) of farmland were turned over to commercial and residential uses. The average area of farmland per capita in China is less than half the world average. Urban growth is covering some of the most fertile farmland in the Chinese coastal and river delta zones.

In the US, 2% of productive land was converted to urban uses over the eight-year period to 2005. In some areas the rate of loss has been immense – in Maryland nearly 8% of productive land was lost over the same period. This creates a problem: as land is lost, demands placed on the land that remains grow.

A combination of high oil prices and legislation designed to lower carbon emissions means that many public and private organisations are looking for fuel alternatives. The most favoured option is producing sugar for ethanol production. The viability of developing crop-based fuels depends on both high oil prices and the efficiency of converting crop energy into fuel energy.

A study by David Pimental, at Cornell University, published in 2001, calculated that ethanol uses up 70% more energy in its production than the energy that remains in it, and that 11 acres of farmland are needed to power an average US car for a year. Eleven

acres is the same area needed to grow a year's supply of food for seven people.

The UN's Food and Agriculture Organization expects the world population to continue rising from its current level of 6.4bn by 1.2% a year until 2015. This raises concerns about the ability of the world's population to feed itself, yet in similar situations in the past, agriculture has generally innovated its way out of danger.

But there is a new twist this time. Rapidly rising affluence in China, India and Brazil, among many other countries, means there is an increasing appetite for a high-protein diet, which needs significantly more land per calorie to service it. Demand is growing for meat, and the cereals and soya used as feed for cattle, pigs and poultry.

The net result is a build up of even more pressure on a shrinking world acreage. To some extent, a world land rush has started. Foreign investors have been active in South America, Australia, New Zealand and North America for more than a decade. In Europe, there has been a lot of demand for farmland in the recent and proposed EU accession states. In particular, there has been a clamour for land in Romania and Bulgaria, especially as it sells at a fraction of the price in the core EU states.

To some extent, a world land rush has started. Foreign investors have been active in South America, Australia and North America

Average global farmland prices

Netherlands	26,605
Spain	20,012
Denmark	17,712
Ireland	16,833
Belgium	16,631
UK	11,978
Italy	10,255
Greece	6,570
Germany	6,382
Malaysia	5,862
France	5,417
Finland	5,204
Sweden	2,846
US	2,591
Poland	1,556

Source: Knight Frank

INSIDER INTERVIEW



DR KEN YEANG
Director of Llewelyn
Davies Yeang,
London

What will be the key themes for the future in residential property?

Green issues will become increasingly crucial. Also, there will be a rise in resort-style living in city centres. These developments will not be part of the normal urban environment, but provide a form of escapism. I see the bedroom becoming probably the most important space in the dwelling unit, with the provision of a related or potentially separate audio-visual space for watching DVDs, sports, games and so on. This space will have excellent acoustics and AV systems.

What do you think is the most positive trend at the moment?

The reduction in energy costs associated with the construction, maintenance and running of buildings. Future purchasers will ask how much energy will be used in their homes or commercial spaces. It will be the same for water.

And the most negative?

Inflated prices.

What is the biggest missed opportunity?

We are still not making buildings green by design. At least 80% of the environmental impact of a building is determined at the design stage.

If we gave you some money to invest, where would you put it?

I would put it in land and property with the potential for future development.

TRENDS

Hot locations

Winning formula

We outline the five ingredients an area needs to be considered a prime global city location

There are no official criteria for what makes a prime city location. However, in our experience a neighbourhood has to have five characteristics in order to be thought of as part of the global luxury market. Firstly, it must be situated in a location tied in to the global economy, and be a national or global regional economic hub. This is why New York and London both have a world-class residential development market but Washington DC and Edinburgh do not.

Secondly, its property market must be open and transparent. International players need to be able to buy without difficulty. Thirdly, the built environment

needs to be highly attractive to the footloose global HNWI. Think London's Knightsbridge, Central Park in New York and Sydney Harbour.

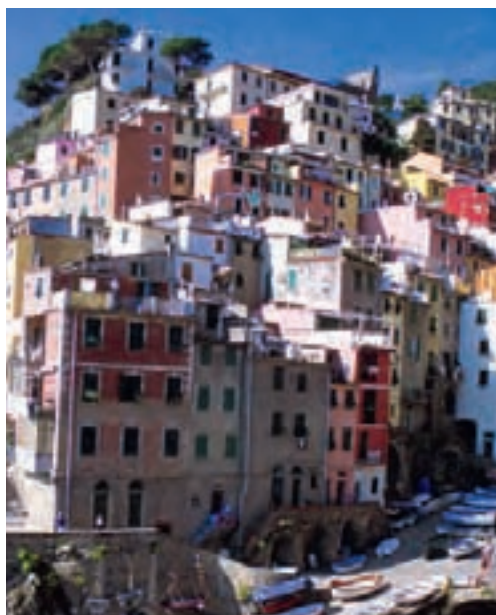
Fourthly, most prime markets are in well-defined locations. They can expand and develop, but extensions are almost always logical expansions of the original area. Recently, for example, Knight Frank officially recognised areas along London's South Bank as forming part of the prime central market in the capital. This is a natural extension from Westminster across the river.

Finally, local taxation law needs to create favourable conditions for international buyers. A world-class market needs its taxation status to be no more onerous than the OECD average. This is why we tend to see a clustering of world-class markets in the mid to lower tax economies of the US, UK, Asia and the broader Anglosphere, rather than in western or northern Europe.

Taxation laws no more onerous than the OECD average are needed to create a global market



Good looks: Sydney scores by having an attractive built environment



Land is already worth 10 times what it was five years ago in Trancoso and Itacaré in the northeast of Brazil



Prime suspects

Ten up and coming residential markets to keep an eye on

Portugal's Silver Coast

Saved from overdevelopment by strict local planning policies, the area enjoys a high level of seclusion unlikely to be broken by lower quality developments.

Singapore

Two areas are on the rise: Sentosa Cove and Marina Bay. The first offers a marina-orientated lifestyle in an integrated residential resort setting, while the second is being promoted as the city's new downtown area.

Bahia, Brazil

The northeast state of Bahia is attracting a lot of interest. Two areas in particular stand out: Trancoso and Itacaré, where land is already worth 10 times what it was five years ago.

Morocco

The coastal area lying close to El Jadida in the Doukkala-Abda region is proving increasingly popular. Advantages include easy access to Casablanca's Mohammed V Airport.

Seychelles

A strict planning regime limits development. Each island has its merits, but Félicité is particularly hot.

Croatia

The Istrian region represents a highly attractive investment opportunity. It has excellent transport links, and those seeking rental opportunities will be encouraged by its growing tourism market.

The Italian Riviera

Centred around San Remo, this area is well protected from overdevelopment and enjoys good connections to central Europe.

Grenada

Less developed than the larger Caribbean islands, Grenada has been attracting discerning buyers. Advantages include its location outside the traditional hurricane belt, and direct flights to the US and UK.

Mauritius

The island is attracting considerable interest, due to a government decision to relax planning restrictions and allow a handful of high-end luxury developments.

USA

Property in the States is of growing interest to purchasers with foreign currency. For something rural, secluded spots close to Savannah, Georgia – notably Hampton Island Preserve, The Ford Plantation and Spring Island – should be considered.



Golden opportunities: (clockwise from above) we tip Morocco, the Italian Riviera and Seychelles



Social awareness

James Waite on how social and environmental considerations have been built into plans for an independent financial centre in the Dominican Republic

How does sustainability fit into this project for the Independent Financial Centre of the Americas?

Any development of this scale will have both an environmental and a social impact. From hydrological considerations to choice of building materials and waste planning, long-term viability puts environmental integration at the heart of the business plan.

Socially, the project will bring obvious benefits to the wealthy international financiers who work there and to the wider Latin American region. Educational resources have been committed to provide specialised tertiary education, so that Dominican graduates can take professional employment at the centre.

There will also be a significant impact on the immediate community, many of whom were informally occupying the land. The decision to engage with the community rather than bulldozing it off the land, and to encourage its involvement as a stakeholder in the project, is a key ingredient of social sustainability.

Where does social sustainability begin?

Firstly, there's inevitably a pump-priming exercise – a credible and proactive charitable foundation is a good way to deliver resources. Funds are directed at primary health facilities for mothers to ensure they

raise healthy children and at primary teaching.

Secondly, there's the need to provide housing that nurtures the social and commercial potential of existing communities. Thirdly, there's the provision of training for adults and the creation of employment opportunities to support the project.

How does this evolve over time?

It's a generational process. While there's an immediate transformation in the quality of life for today's adults, the plan is to encourage the next generation to become entrepreneurs and start businesses to service this burgeoning urban environment.

Why should wealth creators be interested?

Put bluntly, there are two existential threats to established wealth around the world: the danger that the physical environment will no longer support it, and the mob, incensed at extreme and seemingly intractable inequality. In both cases, the remedy is more than a simple set of defensive measures.

Our experience is that the benefits of active engagement with the environmental and social impacts of wealth creation make a real contribution to all concerned. It opens up new possibilities for long-term economic activity and can bring millions of people into the mainstream global economy, where stability serves the interests of new participants as well as old.

■ James Waite is a founding partner of Globalegacy, an organisation working to establish entrepreneurial activities that accumulate and retain wealth in environments of endemic poverty. He is also a contributing strategist for the development of the Independent Financial Centre of the Americas.

Island life: local people and wealth creators alike should benefit from plans to build in the Dominican Republic

'There's the need to provide housing that nurtures the social and commercial potential of existing communities'

RESEARCH AND PRESS ENQUIRIES

Knight Frank Research provides strategic advice, forecasting and consultancy services to a wide range of commercial and residential clients, including developers, investors, and financial and corporate institutions.

For further details about information contained within the 2008 Annual Wealth Report, and for media requests, please contact **Liam Bailey, Head of Residential Research at Knight Frank on +44 (0)20 7861 5133, liam.bailey@knightfrank.com or visit www.knightfrank.com/research**

