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SPERI Global Political Economy Brief No. 2

International Capital Flows into London Property.

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Introduction

London has seen dramatic social and economic changes over the past decade, notably the increasing concentration of super-rich individuals and international investors buying property in the city. The influx of investment has been presented by some as a sign of the capital's success and a vote of confidence in the UK's stability, the financial system and London's cultural offering. Yet, these changes have also heralded a greater focus on the impact this wealth is having on London at a time when inequality is rising, and whilst those on low and moderate incomes are experiencing the effects of austerity, budget cuts and a general lack of affordable housing. Significant concerns have also been raised about the role of investment by the super-rich in reducing housing availability, the way in which investors often barely use the housing resources they purchase, and the extent to which money is being laundered through the property system.

This new SPERI Global Political Economy Brief assesses the relationship between international flows of capital into London's property market and the social impact on London and its neighbourhoods. It presents research findings from a project funded by the Economic and Social Research Council which involved using various data sources including property databases, census data and interviews with the super-rich in London and Hong Kong over a two-year period. It concludes by making a series of policy recommendations that could be implemented to address the city's housing crisis and the social impact of international flows of capital into London.

Part I - Global capital and local pressures

The super-rich in London

- London is a global epicentre of personal wealth. Capgemini and RBC Wealth Management calculated that globally in 2014 there were 14.6 million 'High Net Worth Individuals' (HNWIs) – each with \$1m (approximately £600,000) or more of investable assets (not including housing assets).
- Of this group of global HNWIs over half a million (550,000) reside in the UK - an increase of 13.3 per cent from 2012 - with the vast majority of them living in London.
- The 2015 Sunday Times 'rich-list' revealed that in 2014, there were 80 individuals with wealth of more than £1 billion resident in London. This is by far the highest number of billionaires of any city in the world. New York is home to 56 billionaires, followed by San Francisco (49), Moscow (45) and Hong Kong (43).
- The internationalisation of the London housing market has been a gradual, but accelerating process over the last two decades with dramatic rises in overseas buyers from 2007. In 2011 upwards of £5 billion invested in the London property market came from overseas.
- London and New York hold first and second place in the most recent survey of Ultra-HNWIs city investment preferences (Knight Frank Wealth Report, 2014).

Between June 2012 and 2013, 49% of all residential property sales in London with a value of over £1 million were to international buyers; 28% of these were to non-residents.

- Flows of international transactions have led to growing concerns about the rise of vacant or 'ghost' neighbourhoods with many homes left unoccupied for much of the year.
- London attracts wealthy residents from different parts of the world for multiple reasons including political stability, a high standard of living, a safe haven for their assets, as well as a world-renowned cultural infrastructure. Universities located in London, including a number of prestigious Russell Group universities, also attract large numbers of international students whose wealthy parents may buy them a property.

A domestic housing crisis

The background to these massive flows of international property investment is a domestic housing crisis which is particularly acute in London and can be indexed in various ways, including:

- A waiting list for public housing of a quarter of a million households in the capital (263,491).
- In most London boroughs a household would require an income of £100,000 to buy an average three-bed home.
- Homelessness figures for the capital (for the fourth quarter of 2013) revealed there were 42,430 households placed in temporary accommodation (pending assessment of their homelessness claim, or after being accepted as homeless). This compared to 14,500 households in the rest of England.
- Land Registry House Price Index data for February 2014 showed an annual increase of 5.3 per cent for house prices in England and Wales, with an average property price of £170,000. Yet, in Greater London the annual increase was 13.8 per cent, with an average property price of £414,356.
- Private rents in the mainstream lettings market in London are more than double that of most other English regions. A one-bed flat in Greater London had a median monthly rent of £1,000 in the 12 months to the third quarter of 2012, compared with £495 across the rest of England. For a two-bed flat the figure was £1250, compared with £570 for England.
- Analysis of the 2011 census reveals that the number of vacant homes (dwellings that did not have a usual resident on the night of the census) was 1 in 20 (5.4 per cent) in London's super-prime investment areas. This compared of a vacancy rate of 2.9 per cent for the rest of London. In the most transitory and international 'Alpha' areas the rate was far higher at 11.1 per cent of dwellings.
- The prevalence of London residents living in garden sheds and other illegal non-domestic dwellings has increased. One estimate for the borough of Ealing suggested there were around 60,000 people living in such dwellings.

Part II – Insights from the world of London’s super-rich

As part of a large investigation into London’s super-rich over one hundred interviews were conducted with London-based wealthy residents, global investors, real estate operatives and a wide range of intermediaries who provide services to the super-rich.

The city of choice for the global super-rich

Our interviews highlighted how not all global investors display the same characteristics and that investors have multiple motivations for investing in London.

- Investors are mostly buy-to-let owners who are seeking properties that offer a good rate of return over the long-term, buy-to-leave investors remain a small number, but investors also include those who want to buy, live and engage with a particular community.
- London property investments often reflect broader global political crises and regional instabilities, and the perceived safety and non-interference of the British government.
- This trend is particularly acute for those from nation states where there is little protection for private property and where political conditions support summary seizure of private assets, such as Russia and China. London offers an immediate and future exit route from national and regional instabilities and we expect this to continue as future political, economic and military crises arise.
- A super-prime property dealer told us: *‘we have to remember that London is a global centre for trade, and finance, London is a global centre portrayed, and finance and services of culture, sport, a whole variety of different things, and one of the main things we’ve seen in the headlines for the past ten years, conflicts, civil unrest, global instability, and the United Kingdom is a clear beneficiary of all these problems around the world. In times of political and economic uncertainty London offers a safe harbour, strong rule of law, political stability, excellent service, excellent manufacturing sector, and incredibly high and advanced economy, and the market will provide for those people’.*
- Investors into London property have also taken advantage of investment vehicles that allow the concealment of investor identities. Property is often bought simply to ‘park’ money but concerns have also been raised about the extent to which property is used to hide money for illicit purposes.
- Prevailing property taxation levels are seen as less important than the wider locational and financial advantages of locating or buying in London. Domestic political and economic fears that taxing the wealthy will lead to people and money flowing overseas from the UK appear to be overstated. Many real estate personnel and the wealthy themselves told us that they want to be located in London above all other global destinations, or to have a residential base in London foremost and then additional homes in other world cities.

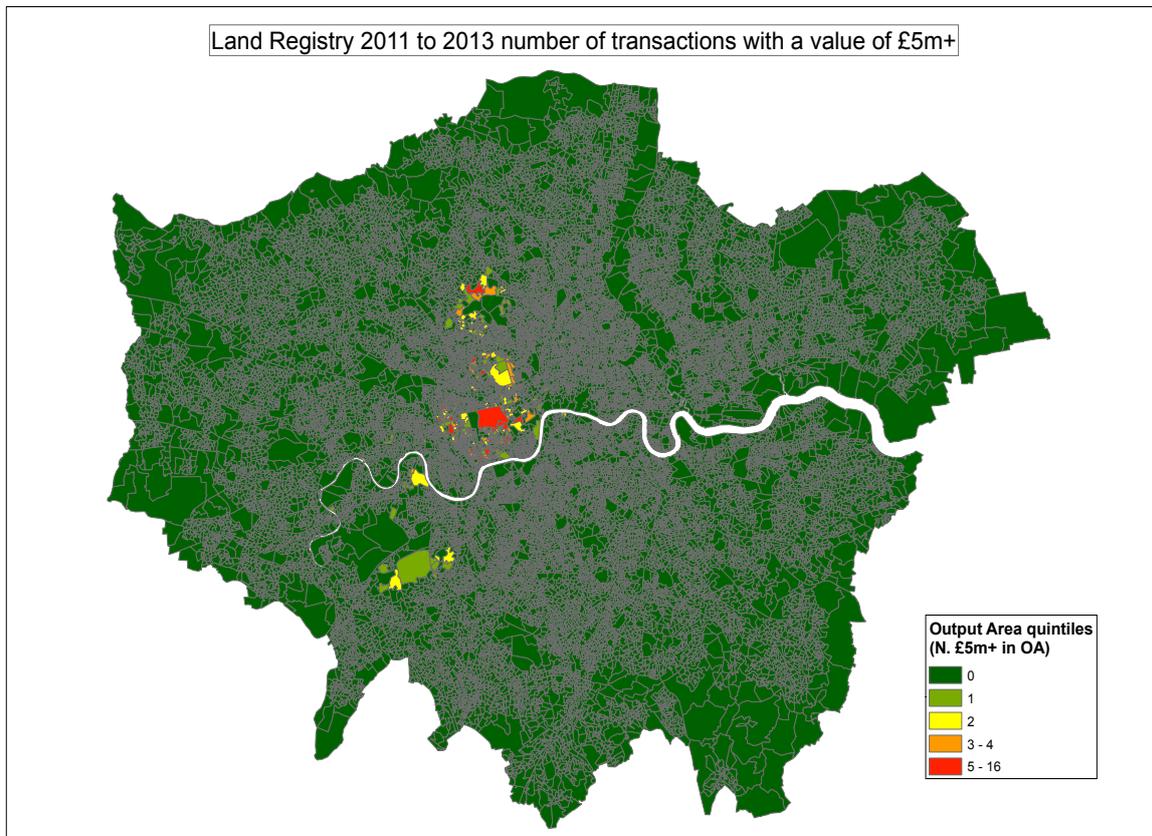
Lessons from Hong Kong

- Our research in Hong Kong and the UK regarding the flow of capital from Hong Kong into London's property market further explains why London property is attractive for Hongkongers and other wealthy foreign nationals.
- Interest rates at banks in Hong Kong yield nearly 0% interest which drives investment by cash-rich Hongkongers into other urban land markets. Global stock markets are deemed too risky to invest in. Many Hong Kong investors don't just invest in London properties but also buy properties in Australia, Japan, mainland China, Thailand, Canada and the US.
- Low interest rates means that investors from Hong Kong are keen to maximise rental income and so rarely leave properties unoccupied, compared to Chinese and Russian investors who tend to leave properties empty.
- Having a property in the West can be a status symbol for Hongkongers. As one interviewee told us, many investors *'don't mind their living conditions in Hong Kong, they might even be living in public housing, it's not about buying for how they would want to live, it's buying purely for investment. They want to use their money for something and a lot of investors don't really care about the look of the building or the location of it. They might care a little bit but what they're worried about is their numbers. As long as it rents out and they get a good net yield that's what they're looking for mainly'*.
- A London-based academic who has studied Hong Kong and mainland Chinese investors told us: *'There's two completely different markets. There's the mainland Chinese investors and the Hong Kong investors. The Chinese investors who I've met have been generally quite unfussy in terms of what they're buying because they're just looking for a safe home for their money. But the Hong Kong investors I think are much more sophisticated, more interested in capital growth and the relationship with rent and that type of thing'*.

Part III – Analysing the impact upon London

- Price displacement pressures, raising the cost of housing elsewhere and thereby forcing existing residents on lower incomes out of these areas, emanate from super-prime investment areas. These areas can be seen in Figure 1. New properties are also increasingly being snapped-up 'off-plan' by international investors (usually paid for in cash). These pressures are contributing to the capital's housing crisis, as outlined in Part One.

Figure 1



- Despite the long-established wealth of many central London neighbourhoods, such as Kensington and Chelsea, the increasing inflow of international investment is generating localised conflict within these neighbourhoods.
- Conflicts have arisen over new-build properties, conversions (such as large basement developments) and the extension of existing buildings. Many existing residents also dislike the increasingly securitised aesthetic of many homes, and the lack of a permanent resident population due to properties only being used for short periods of the year.
- Many developers are now designing and building properties in London specifically for international investors. Hong Kong, mainland Chinese, Singaporean and Malaysian investors work with UK developers to customise properties and to help decide what gets built, such as apartments with dedicated karaoke rooms.
- The trend at the top of the property market is also expressed in bespoke interiors by international clothes and interior designers and by a focus on high-specification security systems, including live-in and off-site staff, and built-in technology.

Conclusion

Growing international investment in London property comes at a time of rising social inequality and significant distress in the capital's housing market. Central government's austerity measures continue to be felt via welfare cuts, and there is inertia on increasing the supply of affordable housing. With much new-build housing constructed to meet the desires of international investors and provide them with secure assets it seems that the private market, left to itself, is doing little to tackle housing need for middle and low-income households. The housing crisis has not appeared to affect the laissez-faire attitude of government to international investment patterns and the impact on the capital which have left many neighbourhoods with slender resident populations and homes used purely as investment vehicles.

If London is to remain a vibrant, creative and inclusive city it must find new ways to plan for substantial increases in affordable housing. Furthermore, it must find new ways of funding this provision by securing financial gains from the very wealthiest investors in the London property market. Our research leads us to make three recommendations that could help to tackle the policy challenges raised by international investment in London's housing market and alleviate the capital's housing crisis:

1. *The creation of an Inclusive City Fund*

To help address housing need, this fund would be generated by a levy on property sales by international buyers of homes with a value of £5m or more. Using land registry data we calculate this would generate around £85m per annum (this is based on a 10 per cent levy on the conservative estimate of 50% of £5m+ sales being to international buyers and having been bought for a combined sales total of £2.6bn over a three year period). The fund could also be used as an attractor for philanthropic funding given that the monies raised for this fund could be used to build social housing reserved for use by essential key workers and those on low-incomes, either administered by nominated housing associations, local authorities or a new body.

2. *Closure of taxation and investment vehicle loopholes*

There is a need for more creative thinking and interest in how the property system is used to shield monies made through illicit means globally. This requires investigating and finding ways of re-orienting the culture of the financial services sector to emphasise its role as a national, city and community wealth-creator. Global co-ordination will be required to develop effective international codes and rules regarding flows of capital. International rules are needed to assist national policymakers and financial institutions who will otherwise face the pernicious choice of seeking to unilaterally impose tighter controls while other countries may benefit from new competitive advantages. In addition, real estate and development control systems in the UK are not configured to identify money launderers. New measures are required to help identify the beneficial owners of those applying for new planning permissions and contesting planning decisions. Details of ownership should be made public and on this basis money laundering checks should be made by national and local authorities.

3. *Joining the dots*

Policymakers need to be held to account for the creation of a housing system that rewards landlordism and privileges homeownership, while overseeing the decline in fortunes of working renters and prospective owners who are forced to compete in a market that has been made even more expensive by speculative investors. Housing need in the capital should be understood as being the result of a failure of the market to provide sufficient and affordable housing for households, the increased 'tax' on households generated by inflated costs and subsequent price displacement pressures, and the sustained decline in funding for social housing occurring in tandem with welfare cuts. Future planning legislation should include more ambitious targets for affordable and housing association provisions in new developments, and policymakers should consider introducing a minimum affordable housing provision for each London borough. In addition higher rates of council tax could be imposed on homes left vacant for more than three months of the year.

Annex

Land Registry transactions within Greater London, 2011-2013

Price Cut-off	2011 £ sum	2011 Transactions	2012 £ sum	2012 Transactions	2013 £ sum	2013 Transactions	2011-2013 Total number of Transactions
All Greater London	3,7561,790,841	89,793	40,117,897,891	92,106	47,128,435,817	99,139	281,038
£1m+	9,038,010,728	4,745	10,358,615,190	5,127	13,911,335,655	6,843	16,175
£5m+	1,120,040,311	158	1,883,152,035	218	2,356,803,615	307	683
£10m+	223,475,000	17	753,993,589	47	756,084,295	55	119
£1,350,000+ (top 1%)	6,838,845,654	2,848	7,987,175,557	3,085	10,895,585,289	4,253	10,188



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