After Brexit: What Now?

It's the End of the World as We Know it... Or Do We Feel Fine?

By Russ Colchamiro

One thing we can all agree upon is that the United Kingdom's June 23rd referendum on whether to remain in or exit ("Brexit") the European Union got the world's attention.

Many feared a vote in favor of exiting, and the chaos that might ensue, but the prevailing sentiment was that, ultimately, U.K. voters would choose to stay in the E.U. Indeed, on the night of the referendum, betting markets pegged the odds of a Brexit vote at less than 10 percent.

Turns out the betting markets — and global pundits generally — were wrong.

There was the initial shock and some panic following the vote, with share prices of companies with significant exposure to the London market down as much as 33 percent. There were even predictions that Brexit would kick off a global recession, or worse. Dismantling a key member from a global, economic/political alliance is sure to be felt on multiple levels.

We are still in the early days after the vote — and the U.K. has not yet officially left the E.U. — but as time passes and the mania subsides, just how severe has the impact actually been, and how disruptive and intense will it become?

"While initially it looked as if the predictions of doom and gloom post-Brexit would come to pass, the reality has proved to be somewhat different," said SIOR member Paul Danks, an Executive Managing Director in the London offices of Newmark Grubb Knight Frank's Global Corporate Services division. "The short-term and potentially damaging impact of Brexit appears to have been contained by swift action."

That 'swift' action was the appointment of Theresa May as the new leader of the Conservative Party and thus the UK's new Prime Minister. "What could have been a protracted eight-week leadership contest and political vacuum was resolved in a matter of days," Danks said. "May immediately demonstrated her steely resolve carrying out the most ruthless Cabinet cull in living memory."

Others concur that the proverbial sky has not fallen. "So far the rest of the European Union is holding together," said Solly Gubbay, BSc (Econ) Hons MRICS SIOR, Associé Gérant / Managing Partner, Paris. He added, however, that a fully informed assessment will have to wait until the Brexit negotiation is complete and the U.K.'s status with the E.U. regarding free trade has been made clear.

Patricia LeMarechal, SIOR, BSc (Hons), MRICS, Partner, Gerald Eve, London, also reasoned that "while there is still no definitive indication of what Brexit means for the U.K. economy, to date, we have yet to see a mass exodus of U.K. occupiers." She also noted that the financial services sector, in particular, seems committed to London, a city rich with specialists and talent. This is evidenced by Wells Fargo's decision to take 33 Central in London with 227,000 square feet since the referendum decision.

But not all SIORs are optimistic. "We have to realize that our worst imaginations have become real," said Hans-Ulrich Berendes, Dipl.-oec, FRICS, SIOR, CRE Berendes & Partner Consulting GmbH in Hamburg, Germany. "A torn country, even a torn nation. How long will the UK exist? The irresponsible demagogues have left the sinking ship and a new Iron Lady, Theresa May, has to find a solution."

Geoffrey Kasselman went even further. "Brexit reverberations are being felt like seismic waves in the U.K., across the E.U., and around the globe, with stakeholders and bystanders alike rethinking which is better: the frying pan or the fire?" said the Chicago-based Executive Managing Director, National Industrial Practice Leader, and 2015-2016 SIOR Global President-Elect.

"It's a nightmare scenario for Prime Minister May," Kasselman added, noting that her options, all unpleasant, are to lead the U.K. out of the E.U. and risk global chaos, or back off and alienate the U.K. majority who voted in favor of Brexit, while Scotland and Northern Ireland grapple with the possibility of leaving the U.K to pursue independent self-interest. "Regardless of the scenario, it is in effect political suicide."

Boom from the Bust?

Though Brexit opinions run the gamut, some industry leaders believe there may, in fact, be a silver lining despite initial pains caused by the vote.

"Other European capitals will relish the thought of luring fleet-of-foot occupiers away from London, although the U.K. could see a response in the form of incentives such as reduced corporate taxes," LeMarechal said, although in a sign of confidence, most corporate occupiers have thus far eschewed a knee-jerk reaction in favor of a more considered approach. "We are beginning to see deals happening since Brexit," with GSK committing to invest £275 million in the U.K., while Amazon leased another 80,000 square feet in Principle Place.

Yet the investment market may get an unexpected boost. LeMarechal explained that the devaluation of Sterling has the potential to serve as a de facto stimulus, with U.S. funds such as Madison International Realty planning to deploy 30 percent of capital raised in the U.K. In addition, rumors are circulating that the new U.K. government may prioritize public investments and prime the economy via major infrastructure projects.

Danks agrees that Brexit has initiated activity, with countries such as China, Canada, and Australia already responding to the U.K. government's initial approaches to commence negotiations of new international trade deals. He also predicts that share prices for leading U.K. property companies and funds will not only recover, but find more rational investment levels following the intense run-up on values over the past half dozen years.

"Many commentators," Danks said, "have long predicted that an adjustment in pricing at the top end of the investment market, particular in Central London — across all property sectors — was long overdue."

In addition, given the low interest rate environment that is likely to endure for the foreseeable future, Danks expects an increase in merger and acquisition activity from major international companies. He further pointed to Marillyn A. Hewson, Lockheed Martin's chief executive, who recently commented that exporting from the U.K. could become more attractive, with Lockheed already seeking the U.K. as a place to invest.

Consumer Confidence is Key

These real and significant economic scenarios notwithstanding, LeMarechal contends that consumer confidence will be the ultimate barometer of U.K. stabilization. She posits that the change in currency rates post-Brexit will likely make the U.K. more accessible and thus attract visitors, with hotels and eateries in tourist areas seeing the benefit, which in turn, could boost real estate values. "But it remains too early to tell how consumers and businesses will feel about their long-term prospects," she said.

With copious sources of capital globally seeking a place to land as the U.K. market reconfigures, industry leaders anticipate an even greater investment emphasis into the U.S. real estate markets. The Brexit impact is extending to other countries as well.

"On the positive for the German real estate professional, our industry will profit," said Thorsten Wolf, SIOR, Prokurist, Berendes & Partner Consulting GmbH, Hamburg. "Cities like Berlin and Frankfurt are likely to see a higher influx of foreign companies making investments, pushing up rents and demand in the German office and industrial markets. The first clear indications are already emerging."

Time, indeed, will provide more clarity. But with the summer months coming to a close, the industry consensus is that starting in September, we will start to see whether the dire predictions of Brexit will come to pass.

Danks, for one, sees reason for optimism, pointing to the £67 billion invested last year in the U.K., one of the world's most stable, highly developed, and best regarded property markets. "It is therefore highly unlikely to collapse," he said. "Adjustments will be made for sure, but perhaps that is not such a bad thing."

However events unfold, it's clear that the Brexit vote has forced significant issues to the forefront, presenting both challenges and opportunities. As LeMarechal said, "it's too early to call," but given the inherent nature of real estate markets — and the nearly unprecedented amount of global investment capital looking for a place to land — the U.K.'s decision to leave the E.U. may slow some activity in the short term, but trigger new deals and agreements far sooner, and with more efficiency, than the pundits initially expected.