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The Impact of Brexit on the U.S. Real Estate Market

One month removed from the historic Brexit referendum on June 23, 2016, it is still too soon to tell the long-term impact of the decision on world markets. At this point in time, speculations from experts all contain similar messages, but only time will tell if they are correct. The one thing that is certain is the *uncertainty* the vote has created around the globe.

Background

When the British people went to the polls to vote on their *exit*—hence the moniker Brexit—from the European Union (EU) and ultimately chose to do so by a margin of 52% to 48%, they found themselves in uncharted territory.

As the first nation to decide to utilize Article 50 of the Lisbon Treaty, the escape clause, they will be the first to navigate the process required to withdrawal from the 28 member EU. First order of business for the United Kingdom was to elect a new Prime Minister following the resignation of David Cameron due to the outcome of the Brexit referendum. His successor, Theresa May, took office on July 13 and has to invoke Article 50 to trigger a two-year clock on withdrawal negotiations with the other EU nations. Prime Minister May has insisted that the people have spoken and there will be no second referendum on the matter. She says the exit talks triggered by Article 50 will begin no earlier than the end of 2016.

Until the terms of the UK's exit from the EU are completed, the nation must continue to abide by all EU treaties and laws but will do so without being able to provide input into the organization's decisions.

Long-term Impacts

Experts are anticipating the Brits' divorce from the EU will result in an exodus of technology and financial firms from the UK. Over the next two years they are stating there will be an 18% decrease in office rentals, with a 10% decrease in UK commercial property values.

If the technology and financial industries pull out of the UK, the United States is an obvious relocation destination. Our commercial real estate market should benefit from Brexit as those businesses secure space to lease or purchase for their operations. As international investors redirect resources towards large US cities and away from the UK amid the uncertainty of their economic future, there will be a flurry of real estate activity in urban centers.

Early estimates place the number of employees UK businesses would bring with them as high as 100 thousand, all of whom will need places to live. The increased demand on the housing market combined with the infusion of foreign money into US cities will cause a spike in real estate prices. In 2013, 75% of Central London's new homes had foreign buyers.

What if the exit of the UK causes the dissolution of the entire EU? Those who think it may trigger such a response warn of a global recession. That would have detrimental effects on the very slow-growing US economy still recovering from our own recent recession. History has shown us that the lower income and higher unemployment that comes with a recession has a negative impact on the housing market.

Short-term Impacts

How the Federal Reserve reacts to Brexit will have the largest and most immediate impact on the US housing market. In the weeks leading up to the Brexit vote the mortgage rate

plunged to its lowest level in three years. As compared to a rate of 4.06% a year prior, the week of the Brexit vote Freddie Mac showed loan rates at 3.54%; two weeks later it was 3.41%. The Mortgage Bankers Association is reporting a 17% increase in loan applications over the first quarter of 2016, and refinancing up by 10%.

The Federal Reserve announced in December 2015, that they were raising interest rates for the first time since the recession and indicated they would do so four more times in 2016. However, in June they voted to stay at current rates until fallout from the Brexit vote subsides. Once the uncertainty stabilizes they will revisit their decision.

What We Do Know

At \$700 billion annually, the European Union is the United States' largest trading partner; we engage in \$100 billion of trade annually with the UK, making them our seventh biggest partner. It may be manageable or it may be of crisis proportions but there is no way the US economy will be able to avoid the impact of the separation of the UK and the EU.

Until Prime Minister May invokes Article 50 and we begin to learn the details of exit negotiations, we can only speculate on the terms of the withdrawal of the UK from the EU. In the meantime we need to buckle our seatbelts and hold on for the ride.

See you at the settlement table!

HOW THE FEDERAL RESERVE REACTS TO BREXIT WILL HAVE THE LARGEST AND MOST IMMEDIATE IMPACT ON THE US HOUSING MARKET.