SPECIAL REPORT

Global Property Insight

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Prime time: market is divided between those who want to own buildings such as these in London's Canary Wharf and those who want to buy cheap Alamy

Investors learn to mind the gap

Polarisation provokes competition for best assets and opportunities in neglected areas **Page 2**

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Time arrives for different finance mix

Polarisation provokes competition for best assets and huge opportunities in neglected parts, says *Ed Hammond*

Banking on evolution: 'The property finance world is going through a huge structural change,' says William Newsom at Savills Bloomberg

The defining feature of the global real estate boom was the closing of the gap between good and bad quality buildings. Today, as the world turns into its sixth year of economic turmoil, the property market, increasingly, is defined by the widening of that gap.

The polarisation in value between a few well located buildings and vast tracts of property considered "secondary" shows no sign of slowing. This fissure has, for the majority of banks, property owners and developers, provoked ever sharper competition for the best assets. But, for investors with a little more appetite for risk, the flight to quality has created huge opportunities.

Across continents and asset classes, the market has separated into two distinct groups: those who want to own the best stock, be it sky-scrapers, shopping malls or town-houses, and those who see the crisis as a once-in-a-generation opportunity to buy cheap.

"Demand for large prime income producing assets from sovereign wealth funds, global institutions and North American pension funds has helped to sustain pricing in the likes of London, Paris, Stockholm, Munich and Frankfurt, where market fundamentals are stronger," says Anne Breen, head of real estate research and strategy at Standard Life Investments.

"On the periphery, a lack of investment has restricted price discovery and valuations are still deemed too high, relative to the risk investors are willing to take," she says.

"However, a handful of deals is beginning to be reported on the periphery and some visibility on pricing is starting to emerge in some markets."

One of the main drivers of the divergence in the market is finance. The banks that fuelled years of asset price inflation with the easy credit that precipitated the 2008 crash are still in retreat mode.

Save but a handful of mainstream lenders, the majority of banks on both sides of the Atlantic are prepared only to lend against the very safest property. This widespread retrenchment has opened the door for a wave of fresh sources for funding.

Insurers, pension funds, private equity groups and even sovereign wealth funds have moved in to fill the funding void left by the banks. But, even with a new source of debt capital being announced seemingly every week, the emergent shadow banking sector represents only a tiny fraction of the lending.

The shortfall has forced property companies to be more innovative in the way they address their funding needs, using a much broader range of capital market, non-bank and traditional finance.

This can be seen from the way some UK housing associations have flocked to the private placement market or the increasing relationship between large North American insurers and US and Canadian landlords.

William Newsom, senior director at Savills valuation team, says: "The property finance world is currently going through a huge structural change in terms of who will be issuing new property loans. The changes have been accelerated by regulatory issues facing traditional lenders, which have opened up opportunities for non-bank lenders."

"Banks have historically held a big market share in European property lending," says Robert Stassen, head of European capital market research at Jones Lang LaSalle. "Since the crisis, banks have actively reduced their exposure and new legislation is likely to increase the funding costs for banks as well as the equity charge for riskier property lending," he adds.

"The result is that banks as a sector will not only lend less, but also differently. This is a structural change. We believe that most banks which in the past have been lending to property will return when they have sorted out their non-performing loans, but not to the same extent as before. The resulting gap is likely to be closed by a mix of further write-downs, asset or loan sales and new entrants. A lot has been said about new debt market entrants in the European property market, but the fact is that they have arrived," says Mr Stassen.

"First, insurance companies like Allianz, AXA and Prupim have stepped up their lending programmes. Second, foreign banks have entered the market like Wells Fargo. Third, investment banks have returned. Finally, the rise of debt funds has been remarkable and we foresee further strong growth in 2013," he comments.

However, with most lenders still focused on writing loans secured against only the best assets, the industry has been forced to pull away from the second tier.

The upshot has been a steady decline in value in many buildings outside the core city markets. Many of the big landlords have stripped back their portfolios to specialise in prime assets, be they offices, shops, hotels or industrial property

In the past 18 months, though, the competition for this rarefied layer of top quality property has grown for one reason: sovereign wealth funds.

> In Ireland, Spain, Italy and Greece, funds are monitoring pressure on governments and banks to sell off vast portfolios

The rise of sovereign wealth funds from Asia, in particular, but also Norway and Canada, has changed the face of property investment.

They can buy assets and hold them not just for one or two cycles, but for 30 years or more; the focus is on rent, rather than total return. This fundamental difference in approach, combined with their deep pockets, means they can pay more and are outbidding traditional landlords on many of the world's most coveted buildings.

From a Central London real estate perspective, sovereign wealth funds are the driving force in pricing at the top end of the market and have become a key and distinctive purchaser type in the market. In 2012, sovereign wealth funds accounted for about 25 per cent of all transactions in the City market (£2.4bn out of £8.97bn), according to research from Knight Frank.

"The most interesting development, in our opinion, is the continued evolution of the requirements of the different sovereign wealth funds. As they become more familiar with the operating frameworks of the market, and more confident with letting and refurbishment risk in particular, there is evidence that some institutions are becoming more sophisticated and are now looking further up the risk curve," the estate agency says.

But, just as the bulk of capital is honing in on the top end of the market, private equity funds and more risk-hungry investors are preparing to pour billions into the the peripheral markets of Europe.

In Ireland, Spain, Italy and Greece, opportunistic funds are eyeing the growing pressure on governments and banks to sell off vast real estate portfolios. In 2012 and already this year, billions of euros of loans have traded in this market.

The gap between prime property and everything else has, perhaps, never been wider. Whether it starts to close this year depends a lot on the global economy. But, for now, extreme polarisation is the new norm.

Global Property Insight

Higher capital requirements raise cost of lending

Regulation

Many institutions are looking to reduce their exposure to real estate, reports *Brooke Masters*

The drive to make banks safer is proving to be a significant hurdle for property developers as it drives up loan costs and makes lenders more skittish about non-prime assets.

This year marks the beginning of the six-year phase-in period for Basel III, the bank reform package that requires institutions to hold more capital against unexpected losses.

As a result many lenders are reducing exposure to capital-intensive, potentially high-risk sectors such as commercial property.

"Higher capital requirements and troubled legacy loans continue to jeopardise the ability and appetite of banks for commercial real estate lending," says Natale Giostra, head of UK and Europe, Middle East and Africa debt advisory at CBRE's real estate finance team.

"There are fewer commercial banks open for business today because it has become too expensive."

At the same time, regulators are becoming increasingly sceptical about the models banks use to measure the risk attached to their holdings.

Andrew Bailey, head of bank supervision in the UK, has described commercial property models as "ropey" and studies by the Basel Committee on Banking Supervision and the European Banking Authority have each found wide variation in the way banks measure the riskiness of particular asset classes.

Since risk-weighted assets are the denominator for capital ratios, any change in the way risk is measured has profound implications for capital requirements and the cost of loans.

"It's clear regulators' concern about the appropriateness and differences between banks' internal capital allocation models is still the elephant in the room in Europe," says Jonathan Clayton of Venn Partners, a credit advisory service.

"This uncertainty and the potential increases, or at least challenges, to capital requirements continue to influence strategy on both legacy portfolios and new lending targets."

Some regulators are talking about imposing floors, or minimum capital requirements, to make sure banks do not tweak their models to make their holdings look artificially safe.

Sweden's bank supervisor has already done so for residential mortgage lending, effectively tripling the amount of capital the country's large banks have to hold against residential mortgages by setting a minimum risk weight of 15 per cent.

The authority says that, while credit losses on mortgages have been low over the past 20 years, it is concerned that rising household indebtedness and high loan-to-value loans might lead to a reversal of that trend.

Norway is heading the same way. In December the finance ministry asked its bank supervisors to look at raising the minimum risk weight to 35 per cent. A formal proposal is due this month.


Lord Adair Turner of the FSA

The UK has taken a somewhat different approach, telling its banks that they must move away from relying on their own risk models for commercial real estate and instead use an approach called "slotting" in which each loan is assigned to one of four categories and given a fixed risk weight, and therefore capital requirement.

The practical effect has been to increase the amount of capital banks have to hold against commercial real estate, particularly outside the prime London market

"We were allowing people to do commercial real estate lending on the existing models on too low a base," Lord Turner, chairman of the UK Financial Services Authority, has testified.

That shift has exacerbated the rise in finance costs, with the increases hitting smaller companies and those in the regions particularly hard, industry participants say.

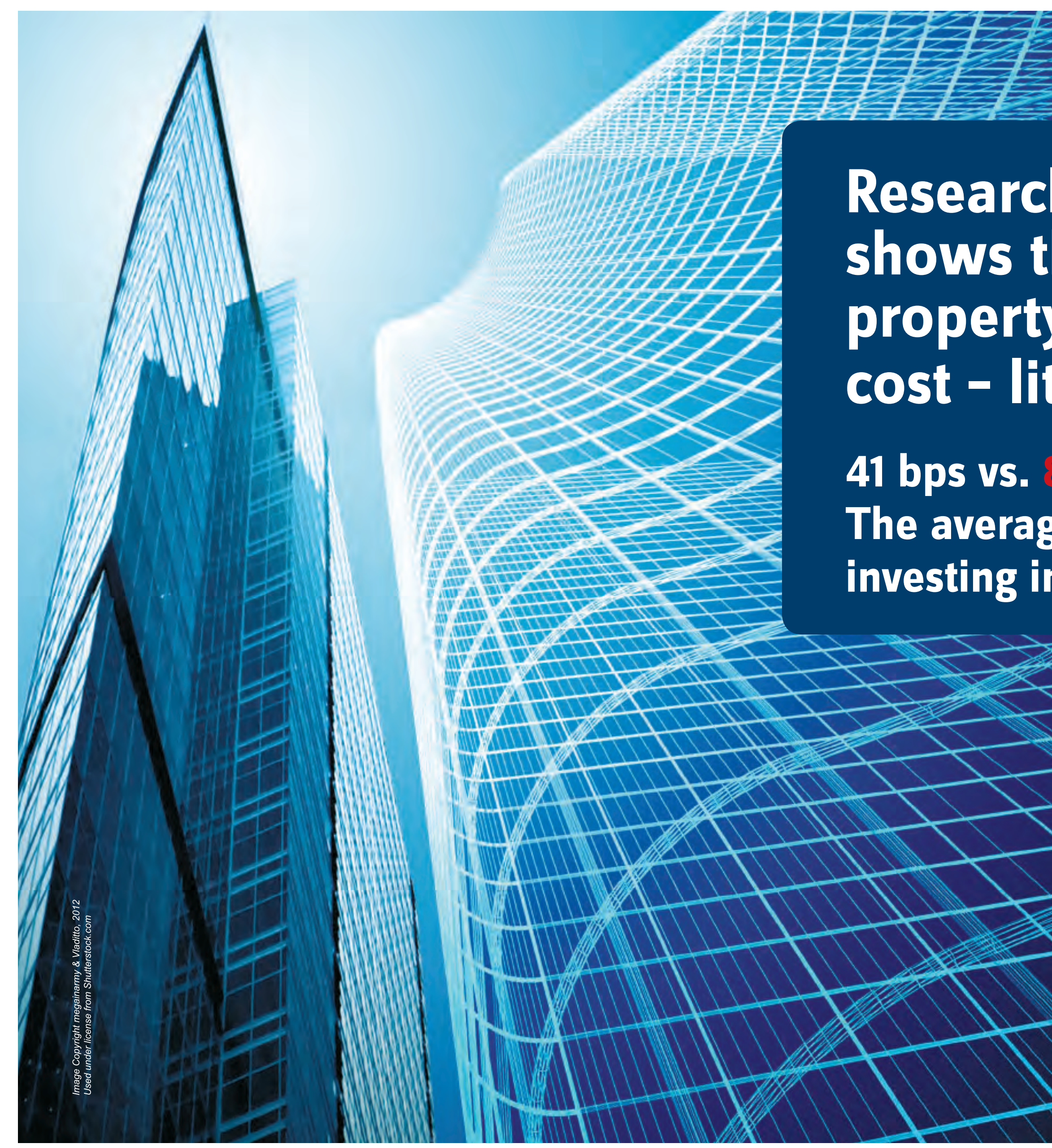
While the UK has been particularly explicit about its concerns over commercial property loans, other countries are also beginning to take action to ensure banks do not go overboard in a new bubble.

In February, the Hong Kong Monetary Authority took action with a suite of changes to its rules for mortgage lending, taking in both commercial and residential loans.

Among the changes, it set new loan-to-value caps on a wide variety of commercial property categories, dropping the maximum ratio by 10 per cent across the board.

At the same time, the HKMA increased the minimum risk weight for residential mortgages from 10 to 15 per cent, effectively increasing the capital requirements for such lending by 50 per cent.

Norman Chan, chief executive, said at the time: "The risk of overheating in the property sector to financial stability in Hong Kong is no smaller than that seen in 1997," when much of Asia was hit by a financial crisis.



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Prime assets stay central to demand

Secondary meltdown Recovery in peripheral markets is a long way off, writes *Ed Hammond*

In the dying embers of 2012, one of the largest office properties in London was put on the market for close to £800m. The sprawling complex at Chiswick Park attracted a flutter of interest from sovereign wealth funds and other deep-pocketed investors.

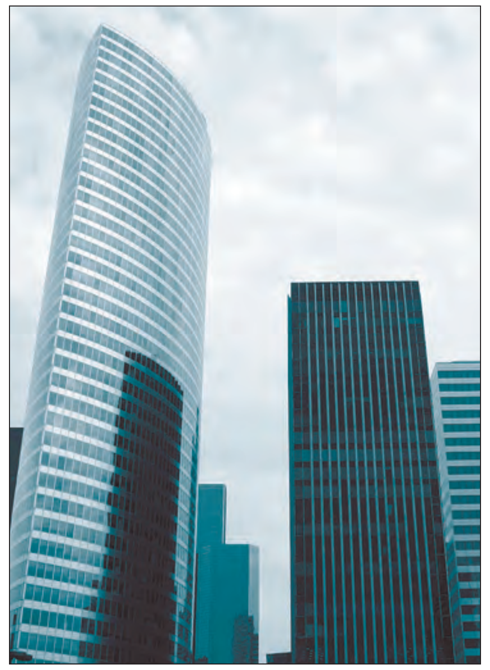
Chiswick Park was the latest – and biggest – in a string of large office deals to hit the London market during the year. Only it was different, in one respect at least: the 1.1m square foot property, less than 10 miles west along the Thames of the City of London, was considered to be in a secondary location.

Europe can be neatly divided into two markets: a few big business centres, such as London, Paris and Frankfurt, and everything else. It is a crude demarcation, but one that investors are increasingly using to define what is prime and what is not.

The distinction has caused a dramatic concentration of the flow of global capital into property. In the fourth quarter of 2012, about 72 per cent of the €38.2bn invested in European real estate markets was focused on the UK, Germany and France, according to latest capital flows data from Real Capital Analytics. Only 3 per cent of capital invested in real estate found its way into the third and fourth biggest economies in Europe – Italy and Spain.

Olaf Schmidt, a partner at DLA Piper, the law firm, says those properties located outside the big cities will continue to fall in value for some time. "Institutional money will not be interested in such assets and banks will refrain from financing them. Transactions will occur only between local players and will be based on local relationships. No international investment will be seen.

"The market for secondary and tertiary assets will be the last to return to normal trading, most likely not before the end of the economic crisis in Europe. The few transactions that will happen on a local level will be done at yields that show a substantial discount to reflect the investment risk related to the almost complete lack of liquidity in this market," he says.


Location, location: prime Paris office space

Anne Breen, head of real estate research and strategy at Standard Life Investments, agrees. "Investors are still keenly differentiating between core and periphery and prime and secondary, and are averse to any substantial risk to the income stream or to their ability to refinance assets," she says.

The problem with much of the secondary property is that the market for which it was built has long since gone. During the boom, trillions of euros were lent by European banks to finance offices, shops, hotels and industrial properties in edge-of-town clusters, secondary cities or rural outposts. The picture was similar in the US. In simple terms, so great was the expectation of continued demand for real estate that the risk of developing outside the big cities was not priced effectively by either the developer or the banks funding it.

The turnround has meant that vast tracts of that property will attract finance only if it can be used as something else – the demand for commercial property of all types had diminished with the contracting western economies and labour markets. At its worst, some secondary property is valueless, worth only the land under it less the cost of dismantling.

Matt Richards, head of international capital Europe at Jones Lang LaSalle, the property consultancy, says the growing gap between primary and secondary property is causing another level of furcation. "With a restricted debt market and an abundance of capital chasing prime assets, the gap between prime and secondary has widened further. This means we have moved from a bipolar to tri-polar market. For the past two years, the market was black and white. Put simply, people wanted to invest in prime and avoid the greater risk of secondary assets.

"For 2013, we expect prime assets to remain in strong demand, but we see a grey area arising from a split within secondary between those assets that have the potential to become prime through investment or repositioning and those that don't."

Money makers see the benefits of more risk

Institutions

David Oakley finds some pension funds starting to switch out of government bonds

Neil Cable, head of European real estate at Fidelity Worldwide Investment, does not pull his punches. As a property investor for a quarter of a century, he sees value in buying non-prime real estate in the UK and continental Europe.

"There really hasn't been a better time to buy this kind of property since the late 1980s," he says. "Just take a look at the yields, which are often as high as 11 per cent and in many instances as much as 4.5 percentage points more than the yields on prime property."

Although not everyone agrees, the market does look likely to benefit from increasing risk appetite and rallying equity markets. Certainly pension funds and insurance companies are starting to switch more money out of so-called risk-free government bonds, which yield as little as 2 per cent, and into higher yield assets.

Even prime property, the safest investments in the sector, offer yields of about 5 per cent, a significant improvement over government bonds. Higher yields in property are starting to help pension funds tackle the problems of deficits, partly brought about by low government bond yields that do not give them enough of a return to match their liabilities.

Standard Life Investments, property fund managers in the UK and continental Europe, runs a number of funds that offer investments ranging from office blocks to warehouses and retail parks.

It mainly favours prime property over non prime, advising clients to opt for real estate in places such as London, southeast England, Germany and France.

In contrast, Fidelity, which runs funds in the UK and the eurozone, only invests in non-prime property, although it favours the UK, excluding London.

Mr Cable backs non prime because of the yield spread over prime, which is wider than at any time he has seen in the past 25 years. Non prime trades at about 4.5 percentage points above prime compared with about 0.5 percentage points before the financial crisis.

However, some pension funds remain reluctant to move out of government bonds. Adrian Benedict, investment director at Fidelity, says it is the fear factor that is holding back some investors.

"Some investors were burnt in the property market five years ago and they do not want to get burnt again," he says. "They are reticent to invest in non-


Neil Cable: non-prime focus

Innovative financing set to fill lending vacuum

Banks

Ed Hammond reports on alternatives to traditional sources of capital

The boulevards of London's Mayfair are an unlikely locale for the sharpening tip of real estate finance. The expensive buildings, cossetted from the road by double-width pavement and the heavy coachwork of parked Rolls-Royces, are in no apparent need of new kinds of funding.

But it was here, at the end of 2012, that Blackstone pulled together a financing package for three of the neighbourhood's most exclusive hotels that illustrated the distance the UK's property market has travelled from its long-standing dependency on domestic clearing banks.

In a £547m deal, backed by Royal Bank of Canada, Bank of America and Wells Fargo, the US private equity giant refinanced the Maybourne Hotel Group.

Just as the defining theme of the first five years of the financial crisis was the deterioration of the relationship between banks and the property world, the next five look set to be coloured by the emergence of fresh, more innovative, non-domestic sources of capital. Real estate companies are no longer looking to the banks as the only lenders of prime resort.

The alternative financing market is shedding its image of being just a provider to the parts of the capital structure deemed high risk or opaque, filling instead the lending vacuum left by the banks. This transition has been slow to take meaningful form but the use of non-bank finance is now a central part of the real estate funding model.

The question facing the property teams in many European banks, then, is what will their role be in the next cycle? Over zealous in fuelling it, the banking sector suffered financial excoriation from the brutal decline in asset values that accompanied the collapse of the property market.

The more recent imposition by Europe's regulators of higher capital requirements have had a less obvious but equally deleterious affect on the appetite to write loans secured by real estate.

"There are less commercial banks open for business today because it has become too expensive due to stringent capital constraints from incoming European banking regulations and, for the UK banks, the additional uncertainty over the impact of 'slotting' on new loans," says Natale Giostra, head of UK, Europe, Middle East and Africa debt advisory at CBRE, the property consultancy.

"For those that do decide to stay, the way they operate will be extremely different, with an obvious knock-on effect for borrowers. In the current climate there is simply no appetite for risk and the memory of what went wrong with property lending will take a long time to fade."

He adds that, while the lending targets of some banks have started to improve, "new lending will not be enough to cover the market demand, providing enormous opportunity for

> 'The memory of what went wrong with property lending will take a long time to fade'

insurers and other non-traditional bank lenders [for example, debt funds] to enter the market".

However, far from engendering uniform negativity in the continent's banks, the property crash has created opportunities for some lenders just as it has obliterated others. In the UK, where Lloyds and Royal Bank of Scotland – both taken under effective state control – are focused on shedding multi-billion pound property-loan books, HSBC and Barclays have stepped up their lending. Similarly, while Eurohypo, once among the most important forces in European real estate lending, has been mothballed by Commerzbank, its German parent company, other, non-European banks have stepped in.

In addition, the new-fangled sources of capital are helping bring back some banks. Perhaps encouraged by the stabilising effect new entrants have had on asset values, banks are starting to re-discover some of the lending appetite lost in the early years of the financial crisis.

Jane Hollingshead, head of property at Addleshaw Goddard, the law firm, says: "When one entity cuts back its lending, a vacuum is created, which naturally needs to be filled and, in this case, we're likely to see a variety of new institutions, combined with old players, operating in new ways."

Others in the industry suggest the decline in bank lending is only a temporary blip, rather than a more fundamental shift. "It is a property lending market that looks very different from what it was but I don't see a long term structural change," says William Newsom, senior director at Savills UK valuation team.

Evidently, the bank lending market across the continent is beginning to ease, albeit with a strong focus on high-quality, well- tenanted properties.

A recent survey of European lenders by Cushman & Wakefield, the consultancy, revealed that the expected amount of capital available for European real estate loans would be 22 per cent higher than in 2012.

While much of that will come from non-bank sources, the banks are slowly beginning to pick up where they were forced to leave off at the end of the last decade.

prime because of the perceived lack of liquidity, something that government bonds offer. They fear they will be stuck in a position as many were during the crises of 2007 and 2008, but the market is in a different place now.

"I do not think the lack of liquidity is as much of a hurdle any more and investors are starting to come around to this view."

Significantly, the fund focuses on the UK and core Europe. These markets look relatively safe, with many analysts expecting an upturn. Office and logistic real estate is considered safer than retail, but even retail parks can offer good value, say some investors.

> 'There really hasn't been a better time to buy this kind of property since the late 1980s'

Fidelity says there were flows into gilts in 2008-09, then a move into corporate bonds in 2010. The next move for some fixed income investors will be non-prime real estate, they believe. "The market is likely to reprice at some point, particularly with the talk of inflation coming back," Mr Cable says. "With non-prime real estate, you have an asset that gives you a high yield and protection against inflation as it is likely rise in value in an inflationary environment."

Another strong reason to invest in real estate is that it is simple to understand, which some pension funds like. It is a straightforward acquisition involving buying a freehold property, renting it out and putting the return from the yield in the bank.

However, despite the new mood of hope in the markets as the eurozone crisis appears to have faded, fund managers still warn against investing in the peripheral real estate markets of Spain and Italy.

As one strategist puts it: "We have seen a rotation out of low yields and into higher yielding assets, but we might well see a de-rotation back the other way."

The markets in the peripheral economies are, therefore, still considered a no-go area for many. They say a better bet is Europe's emerging markets in Poland and Hungary, although they are risky should the eurozone's problems over debt levels reignite. For many fund managers, therefore, the UK, Germany and France offer good value and relatively safe investments.

"Warehouses in Manchester, offices in Nottingham and retail in Berlin are the type of investments we like and recommend," says Mr Cable.

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Everyone needs somewhere to live

Residential Institutions are considering a return to former role as landlords, writes *Ed Hammond*

Safe as houses: 'Residential [property] is a basic need providing for long-term cash flows' AP

Institutional investors in the UK fell out of love with housing a long time ago. Once some of the largest landlords in the country, the likes of Prudential, the pension fund, abandoned the residential market half a century ago; it was too clunky, fraught with the potential problems of dissatisfied tenants and, critically, not as profitable as owning offices.

The upshot is that residential property landlording in the UK has become the preserve of the small-time investor. Ever since 1988 and the introduction of the Housing Act – a game-changing piece of legislation that enshrined the right of landlords to charge a market rent – the proportion of rental properties in the hands of buy-to-let owners has grown steadily.

Today, two-thirds of residential investment properties are held by individuals, rather than companies, according to Jones Lang LaSalle, the property consultancy.

However, the institutional owners are eyeing a return to their former role. Carsten Loll, a partner at DLA Piper, the law firm, says investors should be looking carefully at the residential sector as an opportunity. "Residential is a basic need and a safe bet providing for stable long-term cash flows. Investments are compared with commercial property less dependent on tenants and their changing needs."

The view is echoed across the property sector, and not just in the UK. In Europe and the US residential is being taken a lot more seriously than it was in the boom years that led up to 2008.

The sentiment is supported by hard statistics. Far from just being a defensive alternative to the vast depths of the commercial market, residential has consistently outgunned nearly all other areas of the market.

On a direct comparison with the commercial market, residential has outperformed in each of the past three decades on both a total return and risk-adjusted return basis. It has also outperformed the equity and gilt markets over the 30-year period.

In real terms, the difference between residential and commercial property is even starker, with residential having produced an annual total return of 9.7 per cent, compared with commercial's 5 per cent, according to data from Prupim, a real estate analyst. The difference means that, since 1982, the inflation-adjusted outperformance of residential amounts to almost 300 per cent.

Similarly, the most recent data from IPD, the property value benchmarking group, showed returns from portfolios in the private rented sector were 8.9 per cent, outperforming the 2.7 per cent return from offices, shops and industrial units, and the 3.1 per cent inflation seen in the UK during 2012.

But, in spite of its demonstrably superior returns, the thing that is most often cited by long-term investors wanting to get into the sector is its stability.

The central thesis is that, during a downturn, demand for office space falls as companies shrink workforces or disappear altogether, but people, whatever their wage or employment situation, need places to live in.

This makes the likelihood of long-term vacancy much less likely, assuming the property is not in disrepair. The institutional approach to residential is in stark contrast to the buy-to-let market which depends heavily on capital growth to generate the returns needed to support its funding model.

According to James Mannix, head of Knight Frank residential investments, there are four main advantages for institutional investors: better capital growth prospects, greater liquidity, the ease with which the market can be understood and superior security of income.

On the last point, Mr Mannix explains that, "this may seem counterintuitive given the poor covenant strength associated with individual residential tenants; however, the security of income comes from the depth of the residential market's demand and the ability to re-let a vacant flat within a very short time period. For low and mid-market flats in central areas of London, a flat becoming vacant on a Friday can be cleaned or painted over the weekend and

> The likelihood of long-term vacancy is much less likely, assuming the property is not in disrepair

re-let at the beginning of the following week. This contrasts sharply with the months or years it can take to find a commercial tenant in even new grade-A office accommodation."

That the market is yet to flourish in the UK is something of a quirk.

Other European countries, notably Germany and Switzerland, have large, functioning institutional rental markets. The depth of demand for exposure in residential property was underlined in January by Goldman Sachs' decision to bring to the German stock market 57.5 per cent of the shares, valued at €1.4bn, of LEG Immobilien, a residential property company with 91,000 homes in North Rhine-Westphalia – Germany's most populous state.

The success of institutional investment in residential property elsewhere makes it all the more likely that a similar market will grow in the UK.

Thus far, however, much of the appetite has been in the form of statements of intent rather than actual deals.

Rule of law is central to London's safe haven status

Guest Column

Sir George Iacobescu

In these jittery post-recession times, it is not easy to cast your eyes on the other side of the current troubles. In the past few weeks, we have had a downgrade in the UK's credit rating, the introduction of new European banking regulations, a proposed cap on bankers' pay and the start of a process that will lead to a referendum on British membership of the EU.

Can London survive and thrive through this externally and internally contrived storm?

The fundamental attractions, the allure and indeed the magic of London have remained the same for hundreds of years. It is hard to beat 1,000 years of relatively peaceful development and layers of civilisation.

London in recent years has been in the middle of a renaissance. Some 40 years ago it was in economic decline, with a dwindling population and with vast tracts becoming derelict though deindustrialisation

Now, the population is rising again sharply. Step by step, infrastructure has been fixed, historic buildings have, in the main, been restored and returned to active use. Inner city locations such as Hoxton, Shoreditch and Brixton, seen as the least desirable places to live or work just 20 years ago, are now fashionable and thriving.

Why does London have such an incredible attraction for foreign investment? In the commercial property sector, 2012 saw £8.8bn of investment, the highest volume since 2007. Overseas buyers continue to dominate demand, making 75 per cent of 2012 purchases. Will this change with the loss of our AAA rating? Probably not at all.

London is viewed as a safe haven because any investor can be sure that the legal system will safeguard properties under any political circumstances. Since the Domesday Book of Norman times, property rights have been protected. If you were to put side by side a virtual map of world wealth creation and a map of safe and stable cities, you would see that the former one grows exponentially while the other one remains, at best, unchanged.

The unfortunate truth is that economic trouble and political convulsion around the world have driven not only the rich but many ordinary people to seek refuge for their hard earned money and thus reinforced the value of London and the UK as a bastion of stability. There has been a lot of discussion about the role of the banks. A lot of the faults found in the financial system have been eradicated. Having come through this process, London's banking system should give international investors even more confidence.

If London were a country in its own right, it would be in the top 20 world economies, a little bigger than Sweden or Saudi Arabia. It is conveniently located between the established economic powers of the west and the new super powers in Asia, allowing people to talk to Beijing and Doha in the morning and New York and Los Angeles in the afternoon.

In business, London is the legal and insurance capital of the world, with a legal system used by international companies to write their contracts and settle their differences. London is still growing, too. The Greater London Authority estimates that, by 2031, London will need an additional 750,000 households and will be home to an extra 1m people.

Look at what has been achieved in the past 25 years. Canary Wharf, the company I work for, changed the face of the city's office market and led a regeneration of east London.

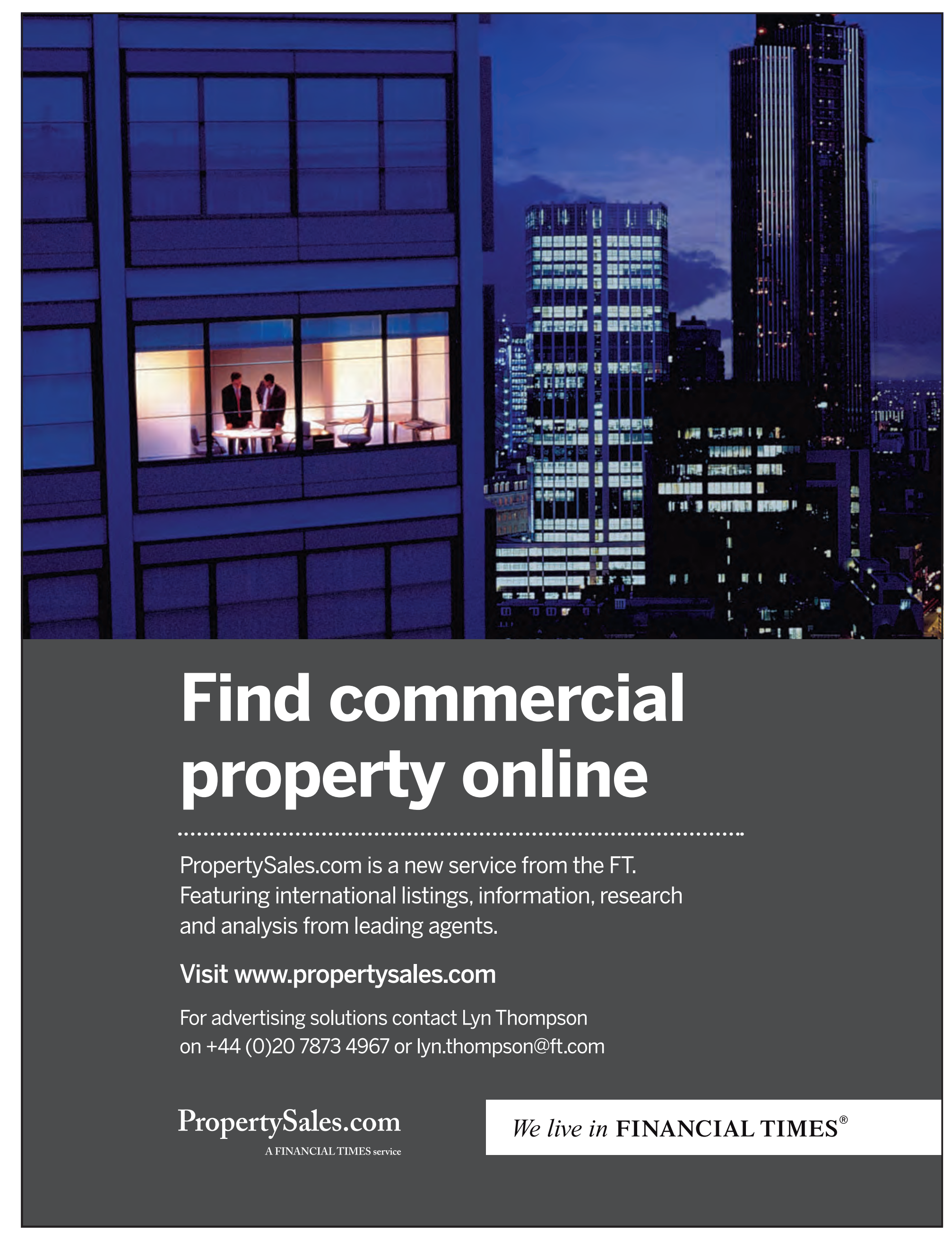
There will be difficulties, of course. The national economic situation means there is very little public money available for expanding services or infrastructure and new forms of funding will be needed for the next wave of investment. Britain also needs to stabilise its relationship with the EU, with calmer heads prevailing in European negotiations. We need to stop making it difficult for internationally mobile talent and business owners to come to the UK. Central government needs to recognise that London's needs are fundamentally different to those of Britain's regional cities.

Sir George: 'capital revival'

London needs to be given its head if it is to continue its remarkable success story. No renaissance would be complete without a renaissance man, and Boris Johnson, London's mayor, is the perfect embodiment of a city that is comfortable with both its past and its future.

One hugely overlooked advantage is that, empowered by technology, buyers worldwide have instantaneous access to London property. This is served by some of the best professionals in the world and a legal system that makes it relatively painless to buy and sell property.

Sir George Iacobescu is chairman and CEO of Canary Wharf Group.



Investors find real estate runes hard to read

Dubai spotlight

Camilla Hall reports on the emirate's rollercoaster property market

Dubai's real estate rebound is puzzling for investors trying to get a grip on the fundamentals of the emirate's rollercoaster property market, which created millionaires in the boom but sent others bankrupt in the bust.

Each local media report on the latest sale of a new luxury development in the city's centre sends tongues wagging. As with the pre-financial crisis property boom, everyone suddenly has an opinion on the real estate market.

But the publicity that surrounds a second real estate boom in Dubai is dividing opinion. There are those who reject the headlines of "phenomenal" demand for properties as nothing more than a public relations stunt.

> Dubai does not release regular economic data and official forecasts often do not tally with earlier statements

Others predict a second bursting of Dubai's bubble. Then there are the believers who are snapping up property so as not to miss out.

The confusion is in part down to the part-recovery in prices. "The rebound in the residential property market has been selective," says Jan Pawel Hasman, vice-president of equity research, at EFG-Hermes, the Arab investment bank. Prices at prime locations with good amenities accelerated the most last year, while increases in less desirable areas were less evident, he adds.

Property prices started to pick up in earnest last year. Apartment prices increased by 19 per cent and house prices rose 24 per cent in 2012, according to Jones Lang LaSalle, the property consultants.

But unlike more developed economies, Dubai does not release regular economic data – forecasts provided by officials are rarely given with context and often do not tally with earlier statements.

Investors look to proxy data, such as passenger traffic through the emirate, which is becoming an ever more popular tourist hub.

The signs look positive: passenger traffic through Dubai airport rose 14.6 per cent to 5.6m in January, up from 4.9m in the same month a year ago.

Many real estate investors go by what they can see and feel. With the city throbbing with activity, the roads jammed and the restaurants overflowing, the emirate feels very much as if it has returned to the heady days of before the financial crisis.

New project launches are also adding to the optimism. Last month, the emirate gave the go-ahead to plans for a $1.6bn island project, home to the world's largest Ferris wheel.

Alan Robertson, the Dubai-based regional chief executive at Jones Lang LaSalle, the property consultants, says the recovery in residential property prices is broadening beyond the city's most popular areas.

"As we move into 2013 we see the recovery as more widespread," says Mr Robertson. "There's something of a ripple effect coming out from the epicentre – if you're right out in the desert, things are still pretty quiet. If you're half a mile in, then things are getting better."

Emaar Properties, the government-backed developer, is behind some of the most recently launched popular projects. Ahmad Al Matrooshi, managing director, recently spoke of "phenomenal" customer interest in The Address Residence Sky View, a new off-plan development including 532 luxury serviced furnished apartments.

But while Emaar's sales announcements have prompted much excitement, analysts say few other developers have the ability to raise the financing for such projects.

"Just because Emaar is doing it doesn't mean the rest of the market is doing it," says Matthew Green, Dubai-based head of research at CBRE, the real estate investment firm. "They are leveraging their reputation for delivering good products."

He adds: "In 2006 or 2007, anyone could launch a product. Now that's just not the case."

From the glitzy areas of Downtown Dubai and the Palm Jumeirah, it is easy to forget the vast swaths of empty, ghostlike villa complexes outside the city centre.

Gargantuan projects such as The Waterfront, a city planned to be twice the size of Hong Kong, remain little more than boarded up desert lands.

Although house prices are increasing, banks are more cautious these days about lending to developers without a record and buyers are more wary about whom they will buy off-plan from.

The federal government has tried to stem the pace of price acceleration by raising the prospect of a 50 per cent mortgage cap. But analysts point to cash buyers as the main drivers of the fast rise in prices, meaning mortgage caps are unlikely to halt sales.

Castle in the air: the Address Residence Sky View