RESIDENTIAL RESEARCH

# RESIDENTIAL MARKET UPDATE

**Knight Frank**

FEBRUARY 2010

## GROWING CONCERNS

**"A renewed sense of concern seems to have settled over the housing market analysts and City economists I spent the past week interviewing. Sentiment amongst this group has darkened even as the market appears to have lightened, with rising prices and growing sales volumes. Concerns over affordability and the post-election world have created a new consensus regarding the likelihood of a weaker market later this year."**

**Liam Bailey,** Head of Residential Research, Knight Frank

**"Every 1% rise in house prices adds an additional £400 to the deposit required by a typical first time buyer."**

### Housing market update

**With prices continuing to grow in the first month of the year and sales continuing to pick up, there seems to be good reason to be cheerful about the housing market. The main concern of agents remains the lack of available stock, rather than a lack of would-be buyers.**

Despite this promising market overview, a degree of caution is advisable when we consider the market outlook against the backdrop of an insipid UK economic recovery, which will be unlikely to stave off further job losses this year. With consumer confidence and real incomes set to be undermined by rising taxes, there are considerable risks ahead for the market.

Latest results from the Nationwide confirm that price growth has continued into 2010, with prices rising 1.2% in January, representing the fastest rate for four months. The annual rate of growth has risen to 8.6%, up from 5.9% in December – the highest rate of growth for over two years.

The rapid bounce in prices is having an impact on market affordability. Despite the support offered by very low interest rates, and even setting aside the impact on mortgage repayment costs if interest rates rise later in the year, buyers are facing additional hurdles in accessing the market. Every 1% rise in house prices adds an additional £400 to the deposit required by a typical first time buyer, with wage inflation slowing to a standstill, at least in the private sector, the ability of buyers to continue building their deposit savings is weakening.

The Council of Mortgage Lenders confirmed last month that 'the main hurdle for first-time buyers continues to be finding a deposit, not the cost of regular monthly mortgage repayments'.

Data from the Land Registry confirm our experience that the market recovery is increasingly being felt in the more affluent parts of the UK. Stronger growth is more apparent in southern England compared to other regions. Prices in the more expensive parts of London, according to our Prime Central London Index, have risen by 15% since last March. Across the south east prices are up by 12% over a similar period – the UK as a whole saw an 8% uplift over this time.

There are indications that the supply and demand imbalance in the housing market is beginning to close. Data from the Royal Institution of Chartered Surveyors confirms that new buyer enquiries are rising at a much slower rate than they were in the autumn, even on a seasonally adjusted basis. On the flip side, supply of new property is at last beginning to rise and has been growing for over four months now.

The Bank of England confirmed that the number of loan approvals for house purchase in December (59,023) was lower than the

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November figure (60,045), the total was, however, well above the previous six-month average (55,004). Approvals for remortgaging (27,276) were higher than in November, but remained below the previous six-month average. While growth in the number of new mortgages seems to be slowing, the general path is still positive.

Turning to new supply from the house building industry, the market here has improved noticeably from the very difficult period 12 months ago. Housing starts in England hit a low of 16,000 in the final quarter of 2008, by Q3 2009 the figure climbed to 26,000, but remains at historically low levels. Undersupply of property will be a growing factor in the next one to two years.

When we consider the market outlook, the main issues remain the macro-economic fundamentals, namely will the Bank of England be able to hold the base rate at 0.5% in 2010, what will be the impact if it doesn’t, and, finally, what will be the market reaction to the post-election reality check caused by a dose of honesty on taxes and government spending? The need to exercise caution grows steadily.

## Economic update

With the UK economy limping into positive territory - it recorded 0.1% growth in Q4 2009 - the Bank of England’s Monetary Policy Committee (MPC) decided at its February meeting to halt, albeit temporarily, its quantitative easing policy. Despite the weak economic recovery, the recent rise in inflation has given the MPC a reason to avoid the risk of over stimulating the economy.

While the anniversary of the VAT cut was likely to push inflation higher in December, the rise to 2.9% was more than was anticipated.

The consensus view in the City is that the recent inflation spike will prove to be temporary and the ongoing weakness of the economy will lead to a continuation of quantitative easing in due course.

Rising inflation does not appear to be leading to increased pressure for higher pay settlements. In fact ONS data shows that wage growth hit a record low in the three months to November, with average pay in the private sector failing to rise at all.

Good news for the economy has been provided by the unemployment data. The total number of people unemployed fell by 7,000 to 2.45m in the three months to November. This was the first fall in 18 months. The number of people working rose by 99,000 – prompted by a rise in part-time work.

While the Q4 figures for economic growth were weak, there is the hope that the UK will see an eventual rapid recovery from this recession – as we did in the early 1980s and mid 1990s – however the parlous state of government finances puts a question mark over this prospect.

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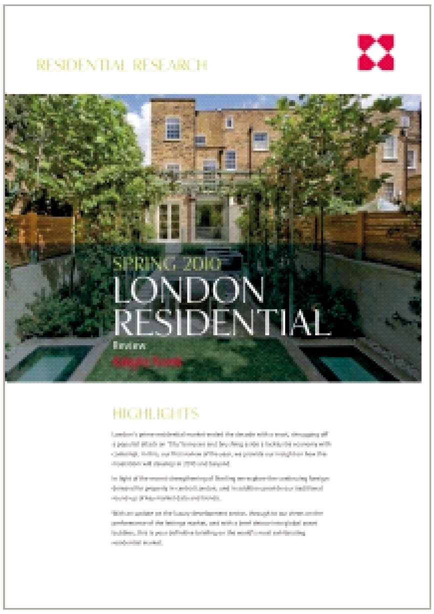
## Recent market leading research publications

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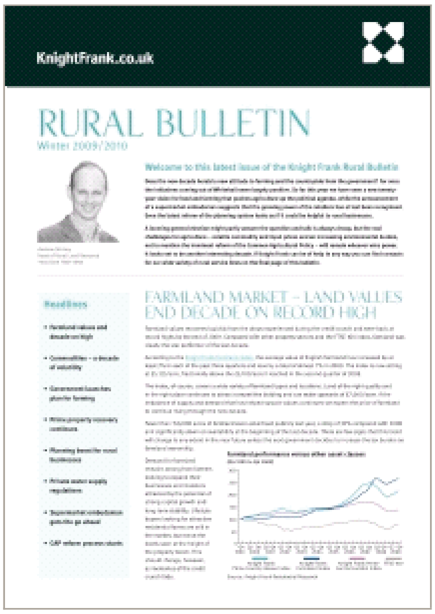


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