January 2012

RESIDENTIAL RESEARCH

RESIDENTIAL MARKET UPDATE

Knight Frank

Wait and see... to what happens in the Eurozone

The UK housing market holds its own in 2011, while prime central London shines. But as 2012 gets underway, all eyes are on the Eurozone.

Key figures

House prices fell by 0.2% in December but were up 1% year-on-year

House price sentiment dipped again in December, with the Knight Frank/Markit sentiment index indicating further price falls this year

Prime central London prices rose by 0.8% in December, taking annual growth to 12.1%

Prime country house prices dipped by 1.7% in Q4 2011, and are down 3.1% on the year

Libor rates tick up despite bank base rate remaining at record low

To find out the latest news, views and analysis from the world of prime property, visit Globalbriefing

Gráinne Gilmore
Head of UK Residential Research
+44 (0)20 7861 5102
grainne.gilmore@knightfrank.com

UK housing market and economic overview

There was some cheer in the New Year as Nationwide's measure of national house prices showed that values held their own in 2011, rising by an average of 1%. Of course, this figure masks wide regional variations – highlighted by the continued strength of the prime central London market which is chalking up growth that puts it streets ahead of any other region. The wider London market is also outperforming the rest of the UK.

The difference in property performance across the UK was further underlined by the most recent House Price Sentiment Index (HPSI), produced by Knight Frank and Markit, a leading economics consultancy. This index, which monitors sentiment across the mainstream housing market, shows that while households in London, the East Midlands, the East of England and the West Midlands expect their house prices to rise this year, households in the other seven regions expect prices to fall, with those in the North East expecting the biggest declines.

The downbeat assessment was echoed by the most recent monthly survey from RICS , which indicated that there was no real sign of the market picking up in the coming months.

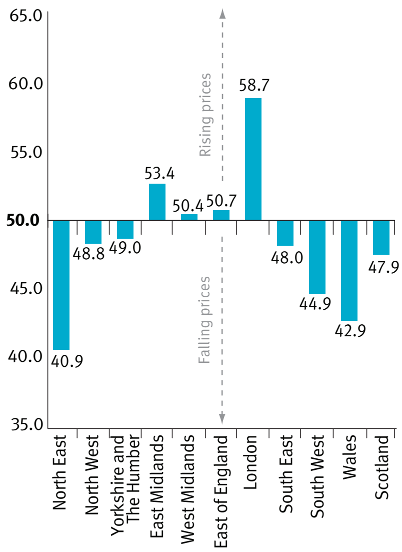
There is a sense of 'wait and see' as the UK, and the world, looks to the Eurozone to see if it can overcome the fiscal crisis gripping the single-currency area.

The Eurozone is now entering a critical phase as several countries will be forced to raise billions more for their coffers by selling government bonds. This is because many of their current tranche of bonds are coming to maturity, meaning they must repay investors the original capital. Drumming up an appetite among investors for new bonds will be a litmus test as to the markets' view on the future of the Eurozone, and its likelihood of survival in its current form.

Figure 1

House price expectations over next 12 months

Future House Price Sentiment Index (HPSI)



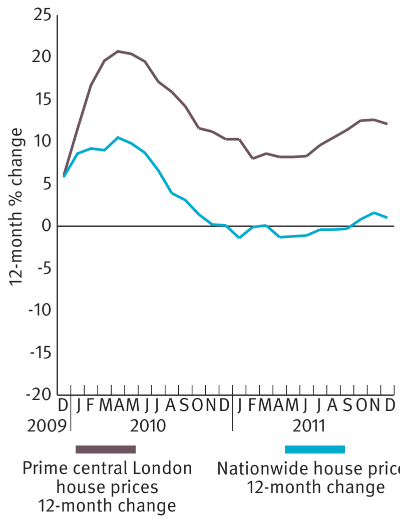
Source: Knight Frank/Markit

NB: A score of 50 equates to no change, above or below representing growth or decline respectively.

Figure 2

12-month price change

London versus Nationwide average residential price change



Source: Knight Frank Residential Research

RESIDENTIAL MARKET UPDATE

Knight Frank

> "LONDON'S LUXURY PROPERTY IS SEEN AS A SAFE HAVEN, AND THERE IS AN ARGUMENT THAT THIS WILL CONTINUE TO BE THE CASE EVEN IF THE SITUATION IN THE EUROZONE DETERIORATES."

Back at home, the economy is struggling to grow. We may avoid a recession, but the economy is stalling. Any shock from the Eurozone would lead to a contraction however. Rising job losses, muted wage growth, on-going public sector spending cuts and difficult access to mortgage finance means that the mainstream housing market faces stiff headwinds this year, as explained in our forecast.

But there is good news for homeowners as interest rates are expected to remain low, so those with a home loan pegged to the base rate will benefit from reduced rates. The Libor rate – the rate of interbank lending which determines the pricing of some mortgage deals – continues to tick up however, meaning that mortgages for new borrowers and re-mortgagers are creeping up despite the low base rate.

Prime market performance

While the wider UK housing market is largely treading water, the prime central London market continues to go from strength to strength. Prices rose for the 14th consecutive month in December, starting the year up 12.1% compared to the same time last year. Activity has been robust, with a 10% rise in applicants over 2011, and a 31% rise in exchanges. London's luxury property is seen as a safe haven, and there is an argument that this will continue to be the case even if the situation in the Eurozone deteriorates.

Activity in the prime country market has been more muted, with sales in Q4 2011 remaining unchanged from levels seen in Q4 2010. But applicant volumes have risen by 11% over the same period. Nevertheless, prices fell by 1.7% in the final quarter of the year, resulting in a 3.1% annual fall.

The picture was broadly similar in the prime country house market in Scotland, with prices down 3.2% on the year. Values in Edinburgh have slipped by 2.8% this year, although activity picked up towards the end of the year, with increased interest from overseas, and especially Russian, buyers.

Rental market

Average rents across the UK slipped slightly in November, the first fall in 10 months, according to the latest data from LSL. But rents are still 3.5% higher year-on-year, and are expected to maintain this uplift, and possibly rise further, as the lack of activity in the sales market forces more people into the rented sector.

In prime central London rents have also slipped in recent months, but are still up 6.7% year-on-year. Rental growth is strongest in the sub-£1,500 a week sector at 7.3%, but demand remains strong across all sectors, suggesting more growth in the pipeline, albeit at a more sustainable level of around 4% to 5%.

Residential Research

Gráinne Gilmore
Head of UK Residential Research
+44(0)20 7861 5102
grainne.gilmore@knightfrank.com

Press Office

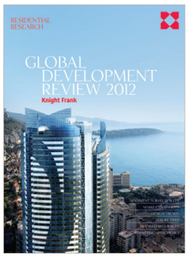
Daisy Ziegler
+44 (0)20 7861 1031
daisy.ziegler@knightfrank.com

Recent market-leading research publications

Prime Central London Sales Index Dec 2011

Super-prime London Report 2011

Prime London expands 2011/2012



Global Development Review 2012

Knight Frank Research Reports are available at **www.KnightFrank.com/Research**