

UK Residential Property Review Report from Grant Stanley, Chartered Surveyors

In 1906 *The Estates Gazette* reported that the average price for a London house was about to top the princely sum of £350. By the beginning of 2006, the average price of a London home has topped £350 000. Although this seems to be a relatively modest increase over the period of a hundred years, it must be borne in mind that, in effect, a large proportion of this increase was spread over the last fifteen to twenty years.

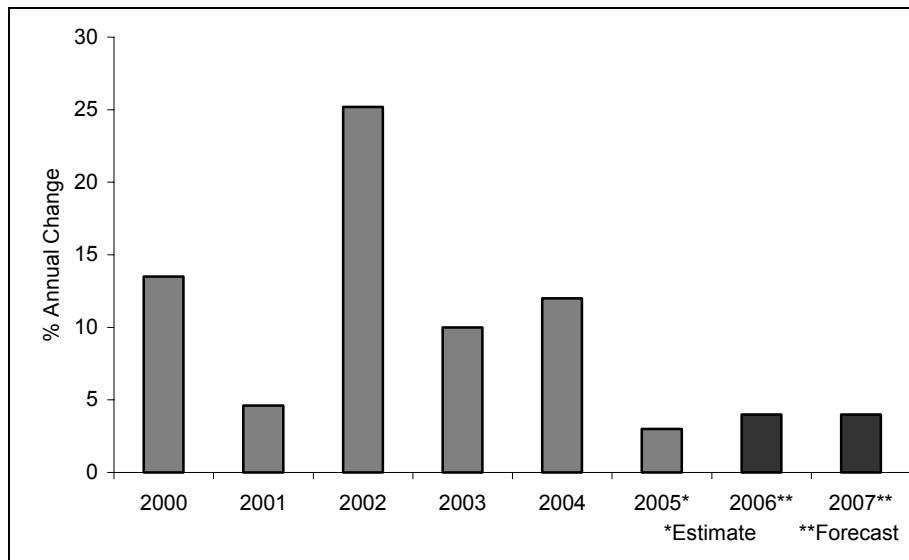
The UK housing market suffered its worst year in a decade in 2005, but there are signs that conditions have picked up a little after a sharp slowdown, data from the Nationwide Building Society shows. The mortgage lender said house prices rose by 0.5% in December and 1.4% in January, lifting the annual rate to 4.4% from 3% in December. Prices fall back only marginally over February, giving an annual rate of 3.7%. The last few months have witnessed 75% of the annual increase in prices.

2005 was still the weakest full-year performance since 1995 and follows several years of double-digit gains as a series of increases in interest rates took the wind out of the thriving market. Nationwide said that the national average home cost £157,250 in December, or up around £13 a day over 2005. That compared with gains of almost £50 a day in 2004. The average house price rose to £158,573 in February.

It also noted that this year was the first since 1999 that equity – market increases had outstripped house- price inflation. The FTSE -100 grew by 16% in 2005 compared to housing market growth of 3%. However, the FTSE still remains 10% below its 1999 level, whereas house prices are more than twice as high as those at the end of 1999.

But economists said fears of a housing crash, so widespread just a year ago, look to have been unfounded as evidence builds that the market is gently recovering, though a return to boom conditions seemed very unlikely.

They predict that the market is unlikely to tolerate any significant rises, as affordability still remained a key constraint for many buyers. If house prices start to accelerate markedly it is believed that buyer interest will diminish, thereby keeping prices down.



Year on Year House Price Growth (1997 – 2005)

Source: RICS Housing Market Review 2005.

A key reason for limited turnover is lower levels of market activity from first time buyers who now account for some 30% of house purchases compared with levels of around 50% during the 1980s and early 90s. More under 30 year olds are now choosing to rent rather than to buy, which for many, makes more sense at a time of life when moving house tends to happen frequently. Slow house price growth and relatively high cost of moving home act as a further break on transactions.

House prices have started to rise again for the first time in 15 months reports the latest RICS housing market survey published in December 2005. The three months to November saw 4% more chartered surveyors reporting rises in prices than falls. October's figures showed a balance of 8% reporting falls.

Buyer enquiries have consistently risen over the past six months and the market slowdown appears to have come to an end. Surveyor confidence is at its highest in 18 months

Market conditions are tightening as the level of property coming onto the market continues to fall, returning the bargaining initiative to the seller. Demand from new households has consistently outstripped supply. This has been a substantial factor in pushing average asking prices towards an all time high.

In the coming year, RICS expects a rise in UK house prices of 4% in 2006 and 4% in 2007. RICS predicted an upturn of 3% for 2005 based upon the ODPM index and the actual figure was 2.9%. The Centre for Economics & Business Research (CEBR) is forecasting a rise of 4.4% in 2006. Nationwide is predicting 0 – 3% growth over 2006 and for N. Ireland and Scotland to outperform.

The modest pick-up in house price rises for next year reflects the impact of the August interest rate cut, as well as a lift from a further expected 0.25% interest rate cut in the first half of 2006. However, if wage data due out is particularly weak i.e. low wage increases, the Bank of England will be dissuaded from further cuts.

With the housing market showing signs of a recovery from a marked drop in activity in the latter half of 2004, purchases are also expected to rise firmly in 2006, having fallen for two successive years.

RICS expects mortgage approvals to rise from a five year low of 1.127m in 2005 to reach 1.336m in 2006. Indeed, January was a particularly strong month in this regard with a third more lent than at the same point last year. RICS spokesperson Ian Perry says: -

"All the numbers point to renewed price rises. There is a universal expectation from agents that interest rates are heading down again in the new year, which is providing the market with confidence.

"The biggest increases have been seen in London where city bonuses are expected to help the market along in the coming months."

The prime Central London market, which has started the year relatively strongly, benefits from the combination of city based employment and world city status, attracting a large core of high net worth buyers and tenants. This profile helps to cushion this market from the full impact of many of the negative factors weighing down the other markets across the UK. In the three months to the end of September we have seen a noticeable increase in purchasers from Asia. They have overtaken European purchasers for the first time since 2000. Evidence suggests that activity from Asian buyers will continue to rise. In line with the change in the global economy, the number of purchases and lettings completed by people from the developing countries has increased and should continue to do so.

Savills predict that prime areas of Central London are the places to watch. They predict above average rises this year in Docklands, Notting Hill, the West End and Mayfair. London has some of the largest concentrations of riverside residential property in the UK and this provides a link between many of the prime markets in London. Such is the demand for riverside locations, that premiums of between 18% and 25% can be achieved for properties with a view of the Thames. These may seem irrelevant to many people who cannot afford the capital's prices, but they could herald the start of a new cycle of property appreciation across the country.

The market doomsters would have us believe that high levels of household debt will trigger house price falls. Interest rates remain low and there are few signs of the debt trigger within residential mortgage lending. With no sign of a debt trigger and employment levels remaining strong, the key to future house price growth is affordability. At a national level, as the RICS has stated, a modest national average rise of around 4% is anticipated for 2006, but prime central London prices are anticipated to show a 5% increase next year.

The decision by Gordon Brown not to allow residential property to be included as part of a Self Invested Personal Pension (SIPP) has diminished property investment possibilities, though RICS does not expect this to have an impact on the market next year.

However, individuals may soon be able to take advantage of property investment tax breaks by using a Real Estate Investment Trust (REIT) to invest indirectly in residential property. REITs will provide a tax efficient method of investing in property without having physically to acquire the bricks and mortar. Though the technicalities have still not been finalized, the concept will provide enable an investment in the property market through a tax transparent vehicle. This will introduce a new pool of investors and inject fresh liquidity into the market.

Home information packs will become compulsory in mid-2007 although pilot schemes will start this summer. The packs, to be prepared by sellers, and likely to cost in excess of £500, must include search and survey information. Although they are likely to have some effect on the

number of properties coming onto the market, the general feeling is that they will not have any long-term detrimental effect on values.

The Knight Frank Prime Central London Letting Index showed an increase of 0.6% for 2005. Although there was a fall in some rents during the final quarter of 2005 prime areas such as Wimbledon, Wapping and within Kensington and Chelsea rents did show some modest increases. Strong capital growth during the year resulted in average yields dropping to 4.93% in the final quarter of the year. However in areas such as Chelsea, Canary Wharf and Wapping yields are still holding strong in excess of 5%. With a recovery of rents expected during the early part of 2006 average yields will exceed 5% again. The results seem to indicate that the slowdown in the letting market is primarily due to the underperformance of flats, whereas houses have continued to display consistent rental growth.

Despite the recent marginal fall in rents, indicators such as renewal rates and asking-to-achieved ratios, remain strong. It is clear that the general health of the lettings market is good with applicant activity continuing.

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Sources:-

RICS Housing Market Review – December 2005

Savills Residential Research Bulletin – December 2005

Knight Frank London Residential Review – Winter 2005

Flexible overseas property financing & refinancing available through the Lloyds TSB International Mortgage Service (IMS).

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