October 2009

In this month's market update

- September sees another month of gains for UK residential property. Price rises are again paced by London and the South-East as the North/South divide grows.
- Key drivers to the recent rally are the continued lack of supply and fierce competition from cash and equity-rich buyers in a tight market – factors at their most pronounced in Prime Central London.
- International investor interest in Prime Central London remains strong as the long-term attractions of this unique asset class relative to equities and other risk assets find increasing favour.
- We believe that the worst of the market conditions are definitely behind us as central banks remain committed to maintaining low interest rates. However, the most likely outturn in the coming months is a slowdown in price rises. While the necessary conditions to a sustained recovery in prices are in place the recovery remains fragile. An increase in supply, though healthy for the overall market, will clearly temper recent rises – as will moves to curb City bonuses.
- Black Brick enquiry levels were extremely strong in September – aided by positive media coverage. Access to properties before they hit the open market and proven negotiating skills are proving to be hugely beneficial to buyers in an extremely tight Prime Central London market

Recovery in prices continues

For the many property industry commentators who forecast a protracted period in the doldrums for UK house prices following last year's sharp price declines, the recent buoyancy has proved somewhat of an embarrassment. The latest news from the many statistics and market indices has been universally positive as a broad if stuttering recovery in economic data, improving investor confidence and a shortage of supply helped UK residential property to post further gains in September.

The Royal Institution of Chartered Surveyors (RICS) showed a sharp improvement in the net balance of surveyors reporting rising rather than falling prices in its most recent survey. This measure turned positive for the first time since May 2007. Interestingly, the survey also provided signs that more positive sentiment is encouraging more sellers – an essential ingredient to a fully functioning market.

The RICS survey provided two other points worthy of note. First, while the survey undoubtedly supports the picture of an improving residential property market, the pace of improvement appears to be slowing with the net balance of surveyors reporting an increase in new buyer inquiries dropping sharply. Elsewhere, it is the huge regional price differences that leap off the page. Supported in no small measure by the return of City bonuses, the residential property markets of London, the South East and South West have all enjoyed strong rises while in the North the regions of Yorkshire, the West Midlands and Wales were among a number where a significant net balance of surveyors are still seeing prices decline.

The UK's two leading measures of residential property prices both posted solid gains in September. The Nationwide Building Society said prices rose 0.9% from August. Significantly, September's gain left house prices unchanged from a year earlier – the first time that prices have not declined on a twelve month basis since March 2008. Prices have now risen some 7.2% since the February low and sit 13.7% below their October 2007 peak. Meanwhile, rival Halifax reported house prices up 1.6% in September and some 2.8% for the calendar quarter. This was the first quarterly rise for two years and the biggest since the first quarter of 2007. According to Halifax, prices have risen 5.9% from their lows earlier in the year and are 18.1% below their high of August 2007.

Lehman Bros – twelve months after the fall

September also saw the passing of a landmark first birthday. As anniversaries go, it is hard to think of many less worthy of celebration, but the era-defining demise of US investment bank Lehman Brothers twelve months ago sent all risk assets into a sharp downward spiral. Much has happened in the interim, not least an unprecedented and co-ordinated response from the world's central banks and governments in a bid to halt the crisis that Lehman's demise accelerated.

It's no exaggeration to say that the repercussions of this event on prime London property were immediate and substantial. If the wheels of the banking system has been turning with increasing strain in the weeks prior to Lehman's failure, the decision to let Lehman fail saw the wheels fall off.

As credit markets ceased to function the availability of finance, even to the most credit worthy, dried up. For several months in the immediate aftermath transaction levels were almost non-existent as the strength and sustainability of the global financial system were called in to question. Where sales did occur, they were invariably forced sales at large discounts to the peak of the market. As the broader economic impact began to take root many international buyers also stepped back or withdrew from the market – either due to a desire to wait or because their own circumstances had worsened.

International investors first to seize the opportunity

But with the co-ordinated response of the world's central banks and governments confidence improved and in the early part of 2009 investors started to stick their heads above the parapet. It was international buyers who were the first movers, buoyed by the additional and material bonus of a weak pound which equalled savings of 50% from peak prices.

Contrary to many pundits who had forecast a protracted decline in prices, the UK residential housing market has continued to bounce strongly since the spring as the combination of a lack of supply and a large proportion of equity and cash-rich buyers has proven supportive. Indeed, those two factors have been at their most extreme in the South East in general and prime central London in particular.

Indeed, in its recent Autumn 2009 London Residential Review, Knight Frank said prices in Prime Central London had risen 6.4% from end-March to end-August. The market backdrop was put into context by Hamptons' Head of Residential Sales Marc Goldberg's simple explanation for the sharp rise in prices: "*This summer we have registered 70% more buyers although there are 20% fewer properties for sale.*"

Sealed bids a common occurrence

At Black Brick we continue to see the impact of this lack of supply on a day-to-day basis. Sealed bids have become commonplace again, underlining the strength of competition and the importance of first mover advantage, something that our excellent contacts are able to facilitate.

There is increasing evidence that the wheels of the credit markets are, finally, beginning to turn. Net mortgage lending has returned to early 2008 levels, according to the British Bankers' Association. The difference between the rate that the Bank of England lends to banks and the level at which commercial banks then lend to each other is often quoted as a measure of the health of the all-important debt market. This rate is now back to its lowest level in seventeen months as confidence improves.

Black Brick enquiry levels strong

Transaction levels too are picking up, albeit from a low base. At Black Brick enquiry levels have been strong again in September as buyers seek the advantages of a specialist search company with access to properties before they hit the open market. Year-to-date we have bought some £50m of property for clients covering the full prime spectrum of buy-to-let flats right through to £10m+ superprime in the most exclusive addresses. Despite fierce competition and tight market conditions in recent months we have achieved an average 10.5% off the asking price, proving the value of skilled negotiators in all market conditions.

Camilla Dell, Black Brick Managing Partner, says demand from international buyers remains strong. "*Overseas buyers continue to take advantage of the weakness in sterling. While the pound has recovered a little of late, it remains well below levels of a year to eighteen months ago against almost all major currencies. We have also seen the geographical spread of investors widen yet further in recent weeks with a marked pick-up in interest from South Africa and Asia. Demand from the Middle East also remains strong. Most of these investors are sitting on cash that is looking for a home and many remain sceptical of equities and worried about future volatility. Investors are therefore turning towards real estate – an asset with intrinsic value – and when they do the focus is very much on quality. These savvy investors understand the importance of scarcity value in supporting long-term prices and rightly see prime London property as a unique asset somewhat insulated from the volatility and potential losses inherent in other asset classes.*"

The last month has also seen an increase in media coverage for Black Brick. As the largest independent buying consultancy in London our opinion is regularly sought by both trade and national press. Most recently we have been quoted in a number of articles on the luxury property market in London on leading newswire Bloomberg.

Two tier Prime Central London market developing

The surge in investor interest has been very much focused at the bottom end (£1m – £3m) of the Prime Central London market – leading to a clear divergence between conditions here and in the £10m+ superprime sector. At the lower end, not only is international interest is at its height, but competition from domestic buyers is also strong as City bonuses return. Meanwhile, dynamics in the superprime market are in stark contrast and continue to favour the buyer. On a relative basis supply is good and proportionately there is far less competition than in lower prime sectors. Given the demand/supply backdrop, prices have not enjoyed the bounce that other sectors have. At Black Brick we therefore believe now is an excellent time to be accessing this exclusive market.

City bonuses key to short term outlook

Looking forward, an increase in confidence may, ironically, serve to curb future rises in the wider market as more homeowners are encouraged to sell as they read about rising prices. Many industry pundits expect the army of 'forced' landlords who were unable to sell in the downturn to start putting properties back on the market.

While recent price rises are consistent with the broad pick-up in economic momentum over the corresponding period, we believe a degree of caution is still warranted despite the plethora of supportive data. The G20 group of leading nations' determination to cap City bonuses is clearly not simply political noise given the strength of public feeling against the financial sector.

Given the importance of City bonuses to Prime Central London property any legislation will inevitably cool prices. And while the latest figures from the British Bankers Association show an increase in net lending it comes from an extremely low base. The banks' appetite for a significant increase in property related debt is unlikely to be significant in the current environment.

Moreover we believe that while the necessary developments for a sustainable recovery are beginning to be in place, that recovery is still in its infancy. As such it remains fragile. But the fact that UK house prices are unchanged a year after the fall of Lehman Brothers shows just how quickly things can change – and over the long-term how resilient an asset prime London property remains.

We're ready when you are.
We would be delighted to hear from you to discuss your own property requirements and how we may be able to assist you. Should you wish to arrange for a non obligatory consultation, please contact us:

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