

It is time for us to write our end of year blurb reviewing the market, assessing the predictions we made last year for 2009, reviewing the market in 2009 and offering our predictions on the market for 2010 and some recommendations.

**So, most interestingly, were our “20 predictions for the UK property market in 2009” any good?!**

**Our 20 predictions for the UK Property Market in 2009:**

1. The recession will last throughout 2009, possibly with a glimmer of hope towards the end of the year, however, 2009 will be hard times. **Correct**
2. Unemployment will rise significantly, we have only just started to see some headlines on job losses; expect more. **Correct**
3. Unemployment in turn will lead to rises in the level of arrears for landlords, as tenants struggle to pay their monthly rents. **Not drastically so, but correct**
4. House prices will continue to fall throughout 2009; we expect a further 15% in the Halifax House Price Index. **Wrong!**
5. The proportionate fall in house prices will slow towards the end of 2009, we expect a small recovery into 2010. **Correct, but happened earlier and quicker than we thought**
6. Rental levels; These will remain steady in 2009; potential buyers renting at present, are offset by potential sellers waiting to sell. **Correct**
7. Macro: Housebuilders will build less than 80,000 homes in 2009, way short of the government target of 200,000 per year, or 2 million by 2016. (They cannot afford it, like the rest of us, and this target just shows how out of touch the Government is with reality). **Correct**
8. Mortgage funding will increase marginally, but only marginally, banks are reticent to lend to each other, let alone to us, the public, despite the Government's efforts to increase liquidity. Never in our life times will the days of 100% or 120% mortgage lending return. It was an absurd notion in the first place. **Correct**
9. Interest rates: Will fall to 1%, a full 50% less than where they are now (especially if oil prices remain at around \$50), as the UK tries to avoid the worst of the downturn. **They did fall, but even lower than we expected**
10. Libor rates: But as borrowers our rates are based off Libor not base rate, which still stand at a premium of 1.05% over base. This margin has been coming down slightly over the past few months and this is likely to continue, but banks like the rest of us are scared of lending to each other, and hence Libor will trade at a premium to base rate throughout 2009. **Correct but only marginally now**
11. Borrowing rates: So we can expect mortgage rates to come down, but to a significantly lesser extent than the equivalent fall in base rates. **Correct**
12. Loan to Value Ratios: One can still attain 80-90% loans but with punitive arrangement fees and expensive margins. The market for LTV ratios of 60-70% will generally improve, however, this does work off the basis that investors are putting down deposits of 30-40%, and therefore the Banks can take comfort in the fact that if the market does fall 30% more from present levels then the borrower (not the bank) will take the hit. **Correct**
13. London house prices will fall proportionately more than the rest of the UK, further exacerbated by stock market woes and financial job losses. **Wrong!**
14. Prime Central London: International investors who hold their funds in \$'s or Euros have seen the value of UK property fall in excess of 40% already. This will lead to some investment from overseas investors, however, mainly in prime Central London. However, overseas investors like the rest of us are also experiencing hard times; Middle Eastern investors are not as wealthy now as they were when oil was at \$140 per barrel, now \$50. US investors have their own problems,

- and Euro based investors have bargains in their own back yard. **Correct, but stronger investment than envisaged**
15. The belief that Housing Associations will wade in to rescue house builders and purchase their completed stock is ludicrous. Firstly, very few of the existing housing stock meet the strict criteria that Housing Associations need stick to in terms of space, energy efficiency and environmental design. Secondly, Housing Associations themselves must contribute towards purchases (it is not 100% Government funded), and Housing Associations cannot borrow any more freely than anyone else. **Correct**
  16. Repossessions: Will continue to rise throughout 2009 as the market continues to fall. There is some evidence that repossession agents will not simply dump stock, but will manage the sales; and this is a good thing. Forced sales get forced sales prices, which neither benefit the bank nor the homeowner. **Correct**
  17. Property Valuations: Valuers have been running scared ever since the overvaluation excesses of 2007; in which they were carried away with euphoria of the market. Now they are being more prudent, and possibly over-prudent and cautious in their valuations. This conservative approach is a positive for the market. **Correct**
  18. The London property market will be hit hardest by the recession; potentially 370K jobs to be shed according to Local Government Association. 7.9% of jobs in London are expected to be lost. As it led the market up, so it will lead the market down. **Correct, but subsequently it has already led the market back up!**
  19. Wretched HIPS: Housing Information packs are a damp squib. They serve little purpose and add even more to the cost of selling a property. The theory behind them may be good, but in practice, if anything HIPS have caused further unnecessary stress on the market. **Correct and potentially will be scrapped under new government**
  20. On a 5-10 year view; The downside to house prices is limited by pent up latent demand from buyers previously priced out of the market. UK house building will be at such a low level that supply will be sufficiently curtailed. **Correct**

All in all we think our predictions were pretty good! What we principally got wrong was the “pace” of change; the recession was shorter in time than and house prices started rising earlier than we envisaged. We also got the call on London and to a lesser extent Prime Central London (PCL) wrong; never underestimate the attractions of PCL to the international community.

### **The UK Property Market in 2009:**

- The stock markets bounced strongly off their March 09 lows to record circa 45% gains to date.
- QE flooded the markets with money, ensuring that all assets benefitted.
- Base rates were slashed to 0.5%, and the margin over base that Libor traded has fallen from circa 1% to only 0.1% now How many businesses (and mortgages) are being kept afloat by this low rate?
- Unemployment rises steadily throughout the year; Although not to the levels suggested by many commentators of 3m+; the rate of unemployment has slowed, due to part time working but shows no signs of peaking
- Contrary to commentators in the press; the UK residential property market is not a homogenous product. What happens in the Midlands and North is very different to the South East, and similarly very different to Prime Central London.
- Not only do prices vary according to regional location, but also dependent upon asset type etc. For example: prices in Prime Central London doubled between 2004 and 2007, fell some 30% peak to trough and now are back at their all-time highs. In Birmingham prices on some inner city flats are down circa 65% from peak to trough, and remain near their all time lows. In Hull the terraced property market has only fallen marginally, as the relatively high gross yields for investors and low absolute prices ensure there are limited forced sellers.

- Housebuilders share prices having fallen up to 95% in 2009, have rebounded strongly from their March lows; they have raised substantial amounts of new equity by way of rights issues in 2H09. They are once again starting work on new sites.
- The level of repossessions continued to grow throughout the year, but any deluge of repossessions that investors were expecting did not materialise. Banks have had to temper their aggression at repossessing and similarly low interest rates (and hence mortgage rates) have stopped many from hitting the wall.
- Mortgage availability has freed up a bit in 2009, but nothing like the previous number of products as 2007 and nothing like the LTV ratios of 100%plus. Although it was interesting to note that some new 90% mortgages have been made available.
- Housebuilders were forced to offer a wide range of discounting techniques to offload property. Along side shared equity schemes for first time buyers these discounts have, covered the whole spectrum from free carpets or free white goods, to stamp duty payments, to mortgage assistance, to part-financed deals, to discounts off list prices. The amount of discounting has reduced into 2H09, but still available.
- Regional Property Developers and Investors; many went into administration in 2009 and provided a decent flow of distressed stock to the vulture buyers circling.
- Valuers, having had their knuckles rapped due to overvaluing house prices, are now far more cautious and overly bearish in their valuations. No surprises, and in the bigger scheme of things this level of prudence is a sensible trait.
- As prices and transactions dwindled, housebuilders and developers hit the wall; a number of well known regional developers being forced into receivership.

Net/net it has been a fascinating year to watch and make selective purchases. The London market rally caught many unaware.

Whilst one reads that things are supposedly getting better in the economy, and bankers are getting paid their bonuses (who would have thought that 12 months ago!), it may be “grim” up north, but from where we are, in the “real world”, business is still pretty difficult, unemployment is rising, and owner managed businesses are still fairly pessimistic.

### **Predictions for the UK property Market in 2010:**

Our predictions for 2010 are best guesstimates, we are not economists, but we have tried to portray our thoughts;

Whilst it was more exciting (and potentially more dangerous) to make predictions for 2009, we believe that the outlook for the market in 2010 will be much less exciting and more sanguine. Property is not a racy commodity and its investment characteristics must be respected for this.

1. There is an “air” of confidence at the moment in not only the economic recovery and the high street, but also in residential property. We would temper this enthusiasm and agree there are opportunities for carefully researched property purchases, but there will not be any dramatic return of confidence to the residential market.
2. House prices in 2010 will continue to be held back by the lack of mortgage availability (whilst banks repair their balance sheets), the threat of a potential increase in interest rates and increasing unemployment.
3. First time buyers have been absent from the market for the past 12months (with deposits on property purchases needing to be circa 30% this is not surprising) and this is likely to continue into 2010. Until we see these buyers return we doubt we will see a significant and sustained price rally.

4. The UK will be distracted by the general election, and regardless of the results, there will undoubtedly be hardship to come in 2H2010 and 1H2011; as taxes rise and we try and repair our country's vast debt.
5. As QE (quantitative easing) comes to an end, commentators will increasingly consider the risk of rising interest rates. Although rates are unlikely to increase dramatically (if at all) in 2010, the "threat of increase" will dampen enthusiasm. (If you think there are homeowners and investors struggling with mortgage payments at the moment, consider what the effect will be in a rising interest rate environment).
6. The UK will officially come out of recession, however, only on paper, there will be plenty of hardship and unemployment to temper any great enthusiasm.

## **Our Recommendations for 2010:**

It would be only right for us to see what we forecast last year, and how successful we were! We said; **"In amongst all the gloom, we are going out on a limb and recommending that as a Long Term Buy (that is 5-10 years), and we are firmly of the belief that property should be a long term investment, that 2009 will offer unprecedented opportunities to acquire residential stock at discounted prices, which will show good gross yields, a net margin over financing costs, and in 5-10 years an appreciable price rise over 2009 acquisition costs. We would caveat this recommendation, with the advice that it is imperative to seek proper advice, and purchase the right investments. There will be many pitfalls along the way for the unwary investor."**

**We think the above recommendation was pretty good, and rather than coming up with any new, exciting recommendation the same recommendation applies for 2010;**

- a) Property must be viewed as a long term investment (5-10 years)
- b) There are good, selective, **well researched** buying opportunities now
- c) Debt management is imperative. Consider fixing into 5 year or longer fixed rates; swap rates are near all time lows. Be prudent/conservative
- d) Property Management: Residential investments must be pro-actively managed; any potential loss of income impacts returns
- e) Yield is important; the rental income less running costs must cover interest costs. Capital gains will be a bonus
- f) Location, Location; this is imperative as ever, and we believe in our chosen area of the Midlands and North, "right asset in right location"
- g) Diversification: A portfolio should be diversified both in type of property, and geographical location

For those with cash to invest it is a difficult choice; what will the stock market do in the next few years? Will China boom? Where are oil and gold prices heading? We would urge investors to consider the benefits of residential property investment in their asset allocation strategy.

We are not saying to charge into the market now, but by acquiring a diversified portfolio of quality properties over the next 12 months, a quality portfolio can be accumulated as a long term hold.

### **A: We recommend, as a property finding agent, specific investment opportunities;**

We believe areas outside of London and the South East will outperform in the longer term. Whilst inner city flats in Prime Central London are possibly now at the same price as their 2007 all time highs, in Birmingham, for example, properties can still be bought at 60% plus discounts to their original sale prices. We believe we will continue to see some deeply discounted stock being sold by developers and investors. We believe we will see some opportunities in areas of new build; the likes of Leicester, Leeds, Birmingham and Manchester that have seen huge oversupply of new build stock. A lot of the excess supply has been sold in 2009 but there will still be opportunities in 2010.

We will, as always, be yield driven in our property advice. We expect a minimum gross rental yield of 8%, netting after voids, insurance, maintenance and management fees, 6%. It is imperative that one attains a rental income to cover loan repayments.

We believe in regeneration areas as attractive long term investment opportunities. The likes of Hull and Corby have inflows of public and private money helping support and improve the quality of the cities.

We believe in purchasing property that is less than the average national house price.

**B: for those, who would prefer an indirect vehicle, then we would recommend reviewing the fund that our sister company Residential Property Asset Management (RPAM) is launching "Residential Property Recovery Fund". This will be invested in a diversified portfolio of residential properties throughout the Midlands and North of England. It will be managed by RPAM and follow the recommendations above. The minimum investment is £25,000 and the investment is allowable via SIPP or SSAS pension.**

Should you wish to receive information on the fund please email; [info@rpamfunds.co.uk](mailto:info@rpamfunds.co.uk).

We wish our clients and friends a very prosperous 2010

**The Team at Residential Property Group Limited**