Walls & Futures

Is the UK property market in recovery?

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The endless talk of doom and gloom is now being replaced by that of recovery with the press replacing "Credit Crunch" with a new buzz word "Green Shoots". As always the UK property market remains tightly in focus and the debate now centres on the shape of the recovery?

In this edition we look at the possible shape of the recovery and strategies to protect the property investor should the market relapse.

Economic Overview

According to David Miles, one of the newest members of the Bank of England (BoE) monetary policy committee, the worst of the recession may be over. The combined actions of interest rate cuts, quantitative easing program (over £105 billion) with increases in government spending and VAT reduction, were likely to have a "substantial" impact on the economy in reviving demand.

Data from various parts of the economy back this point of view. The latest figures from the Purchasing Managers' Index (PMI) rose from 45.4 to 47, and although any figure below 50 shows contraction, this is the first positive move for 15 months.

The British Chamber of Commerce (BCC) survey of 5,600 businesses hailed that the "worst of the recession is over". The net balance for domestic sales in the manufacturing sector improved to -37pc in Q2 from -55pc in Q1 and the BCC said it was promising that sales confidence had improved dramatically, rising 40 points from -38pc to +2pc.

Although UK unemployment rose to 2.261 million in the three months to April, it was slightly below economists' forecasts. It is important to note that the unemployment rate is viewed as a lagging indicator, illustrating economic conditions that have passed. As such we will only see job growth reported once the economy is well into a recovery.

The Stock market is an example of a leading indicator and in Q2 2009 the FTSE 100 rose by 7.4% to 4249. Arguably the housing market is another lead indicator so have prices found their level?

Property Market Review

In our last review, we suggested that as property was one of the first sectors to enter recession, it would be one of the first out. The markets fall from grace has been well documented but in short, as credit evaporated, sales volumes fell by 61% leading prices to fall by up to 40%. Today however we now have a situation where affordability levels have been restored to the same levels of Q3 2005.

With interest rates at virtually zero, investors have been attracted to the yields and medium to long term capital returns now generated by property. The attraction is further bolstered by the fact that property as an asset class is something tangible; something that investors can touch and feel.

Estate agents have reported increased levels of demand and because of depleted stock levels, it is not uncommon for a property to have multiple bids or sell for over the asking price. According to Hamptons the current market is even better for sellers than the boom.

The anecdotal evidence is supported by the Nationwide who stated that UK average prices increased by 1.25% in May 2009, which was the third consecutive increase in four months. The recovery appears to be starting in London with the Land Registry reporting that while the UK property market fell by 0.3% in April 2009, London property prices actually increased by 1.4%.

Although prices have stabilised and the market appears to be rising, we do not believe this signals a medium/long term upward trend. One of the key reasons for these "Green Shoots" in the housing market has been the lack of supply as up until now, only forced/distressed sellers have put their properties onto the market. However as sentiment improves forced landlords may be tempted to put their properties onto the market leading to a possible fall in prices.

It is our belief that the market has found its level however will tread water for the next 12-18 months. The medium to long term view is healthy, especially for London which has a greater demand/supply imbalance than the rest of the country.

Is it time to dip your toes into the market?

Since the beginning of the year we have seen the deal flow of deeply discounted property turn from a flood to a trickle, especially in the new build sector. Developers are no longer under the same financial pressure they were under in Q4 2008 and the mantra has changed from "cash flow" to "profit". Several of the larger developers have sold the majority of their standing stock with the likes of Persimmon, the UK listed house builder, recently announcing they were ready to start working on 50 new sites. However this stock will take time to feed into the market so the short term lack of supply will help protect margins and support prices.

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We still believe the market is ripe for investment however investors should proceed with caution. There is a potential risk the market could destabilise if the substantial amounts of repossessed property held by banks are dumped onto the market.

The typical hands off buy-to-let model pursued by individual and institutional investors may not generate the same returns it once did. Therefore to mitigate this risk a thorough analysis of the market is required with a more involved and hands on strategy. To further protect your return it is important to remember that in today's market profits are made on the buy as well as the sell.

Quick Tips

- Location, Location, Location: Focus on established areas - If your budget can't stretch then target locations on the fringe which will benefit from the ripple effect.
- Target properties where you can add value, either through refurbishment or redevelopment. You are more likely to find these properties at auction.
- Build a diverse portfolio of property: Mixture of capital growth and yield producing assets.
- Base your offer price on the yield generated to ensure you don't overpay.

For many investors, especially those overseas pursuing this strategy may be challenging or impossible due to time, financial or knowledge constraints. Structured vehicles such as Funds offer a solution to investors who wish to benefit from the improved returns of this strategy without the day to day headaches of implementing the strategy.

In response to demand from clients and investors Walls & Futures will be launching a London residential property fund. For further information please register at www.wallsandftures.com/fund.html.

ABOUT WALLS & FUTURES

Walls & Futures is a London based property investment consultancy who specialises in providing tailor made solutions for individual and institutional clients.

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Finance

The availability of mortgage finance has gradually improved with banks starting to increase the number of competitive mortgage products. Data from the Bank of England (BoE) showed mortgage approvals at a 13 month high at 43,414. However it is still less than half the average monthly level of 95,000 reported by the BoE between 1993 and 2008.

First time buyers have started to return to the market, helped by the increase in the number of lower deposit mortgages, with Lloyds TSB leading the charge with a competitive 95% Loan to value (LTV) at a fixed rate at 4.99% until October 2012. You can save yourself 1.50% on this rate with First Direct however this is reserved for borrowers with a minimum 25% deposit. Nationwide caused an outcry by reintroducing 125% LTV mortgages however it is only available to existing Nationwide clients.

Investors requiring mortgage finance have a selection of new lenders to look at with NatWest and the Post Office topping the best buy tables. Those looking at purchasing new build properties would do well to double check lenders criteria as some treat this segment of the housing market as high risk, preferring to offer higher LTV's and more attractive rates on older properties.

While tracker rates look attractive, borrowers should look carefully at the spread between the bank base rate and the rate being offered. While the consensus on the direction of interest rates is up, the speed and timing is still up for debate. We would therefore recommend you check the length of the lock in period so as not to get caught out.

Our advice is to shop around for the most suitable product as the cheapest many not be the best so to look very carefully at lenders terms and conditions. Alternatively speak to an experienced mortgage broker.

Lending Table

Lender	Rate	Max LTV	Type
Lloyds TSB	4.99% (fixed Oct 2012)	95%	Residential
HSBC	5.99% (fixed Sept 2011)	95%	Residential
First Direct	3.49% (2 yr fixed)	75%	Residential
Royal Bank of Scotland	4.89% (2 yr fixed)	75%	Residential
NatWest	5.69% (fixed Aug 2011)	75%	Buy to let
Post Office	5.99% (fixed July 2014)	75%	Buy to let
Bank of Scotland Offshore	4.39% (2 yr fixed)	75%	Overseas Buy to let
Bank of Scotland Offshore	5.94% (2 yr fixed)	95%	Overseas Buy to let

Source: Moneysupermarket.com & Bank of Scotland