



JONES LANG  
LASALLE®

*Real value in a changing world*

on.point

August 2010

## UK Residential Market Forecasts

---

Annual capital growth in the mainstream UK market sits at 6.6% having dipped from a double-digit peak of 10.5% in April. The simultaneous impact of weakening buyer demand and the increased level of property for sale continues to affect pricing.

---

Our price forecast shows gains, year-to-date, being eroded during the remainder of the year. Sales volumes are likely to ebb rather sellers compromising on significant price reductions. 2010 will merely postpone the softening of prices we now expect through most of 2011.

---

The delayed impact of spending cuts will be felt as Budget measures are phased in. The government Spending Review for 2011-15 is due to be concluded in the autumn. This will have a bearing on the amount of public money available to sustain, limit or instigate new housing starts.

---

The longer term outlook implies a more upbeat economic picture; this adds further substance to our prediction of significant house price growth by 2012, with pricing gravitating towards the long-term average rate of price growth circa 7% pa.

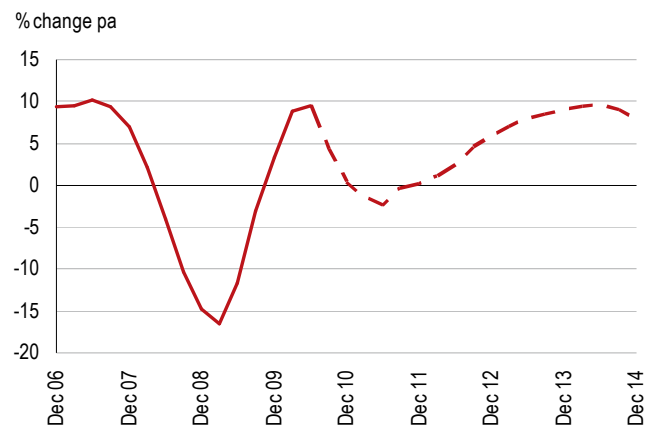


# UK Residential Market Forecast

## Summary

- While the recovery in the UK housing market has not been derailed completely, price growth shows distinct signs of slowing. Prices are up 3.6% year to date, with annual growth drifting from 10.5% in April to 6.6% in July.
- The abolition of HIPs in Q2 led to a rapid increase in stock on the market. Anecdotally, there has been a significant rise in “test marketing” of properties by speculative sellers looking to capitalise on pent-up demand for prime locations.
- Short-term metrics suggest the supply of resale properties will continue to increase. For every 10 sellers there are only 4 would-be buyers with an approved mortgage, according to new Rightmove statistics.
- Exchange volumes remained static over each month of Q2 at approximately 70,000 units per month according to HMRC. Transaction numbers are 26% higher than last year, yet continue to represent only 55% of the long-term average.
- The market outlook suggests that sellers will be forced to adopt less aggressive pricing strategies in forthcoming months. The balance of power is once again drifting in favour of the buyer for the latter part of 2010.
- Following the Budget in June, we await the government Spending Review in the autumn to assess the full impact of reduced public capital expenditure in the housing sector.
- Over the longer term, the economic picture looks brighter; this adds further substance to our prediction of significant house price growth by 2012. Prices are forecast to move towards the long-term average rate of growth circa 7% pa.

## Forecast of UK residential prices



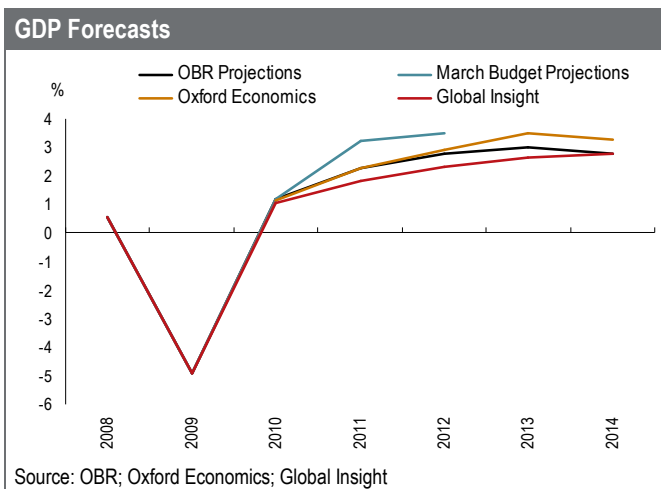
Source: Jones Lang LaSalle; Nationwide

Dec % Chg YoY	2009	2010	2011	2012	2013	2014
UK	3	0	0	6	9	8



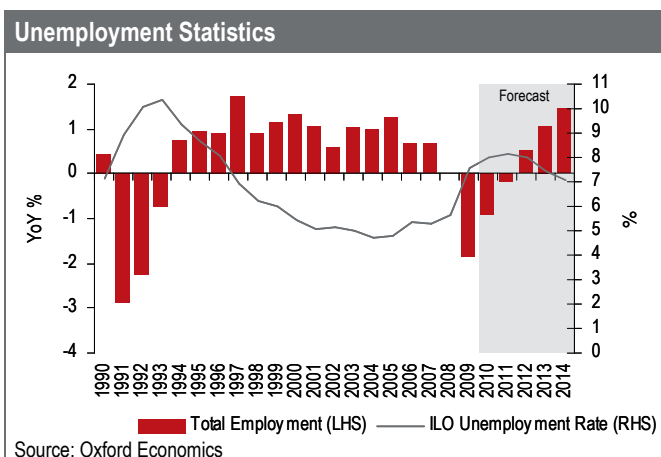
## Economic background

The economy grew at a faster pace than expected in Q2 at 1.1%, a significant improvement on the lacklustre 0.3% growth in the previous quarter. Growth was dominated by the construction industry which grew by a considerable 6.6% in Q2 compared with a decrease of 1.6% in Q1. The services sector also exceeded expectation growing by 0.9%. These numbers, however, are preliminary estimates and could be revised in future. The Bank of England recently spoke of a “choppy recovery” and downgraded its outlook on growth and consumer confidence. The key question is whether the recovery will be sustainable when the previously announced spending cuts are implemented.



## Unemployment rate the lowest in a year

The latest UK labour market data showed the number of people unemployed fell by 49,000 to 2.46 million in the three months to June, the biggest quarterly decrease for three years, bringing the unemployment rate down to 7.8%. The improvement, however, can be attributed to an increase in part-time employment as full-time employment declined. It is still too early to suggest that the worst is over for the labour market. A recent report by employment group the Chartered Institute of Personnel and Development (CIPD) suggested that unemployment could reach up to 3 million.



## Inflation fell again for the second consecutive month

UK inflation fell again for a second month in June to 3.2% from 3.4%. Although this is a positive sign, the inflation rate is still well above the government’s 2% target. The fall in prices can mainly be attributed to lower fuel prices and falling clothes prices. Similarly, the retail price index (RPI) inflation measure also fell to 5.0% in June from 5.1% a month earlier.

## Base rates and the impact on lending

Lower inflationary pressures will mean the Bank of England is likely to keep base rates at the current level of 0.50% over the next few months. If inflation does not fall, this will put pressure on the Bank of England to raise interest rates in the medium term, a move which would contradict the government’s favoured economic strategy.

## Forecasts for the UK Economy

	2009	2010	2011
GDP	-4.8	1.3	2.3
Household Consumption	-3.0	0.5	1.6
Inflation (CPI)	2.2	3.1	1.9
Short term interest rate*	0.7	0.8**	1.7***
10 year Gilt Yield	4.0	3.9**	4.4***

Source: Consensus Forecasts (Jun-10)

\* 3 month interbank rate

\*\* end Sept-10

\*\*\* end Jun-11



### Current UK housing market

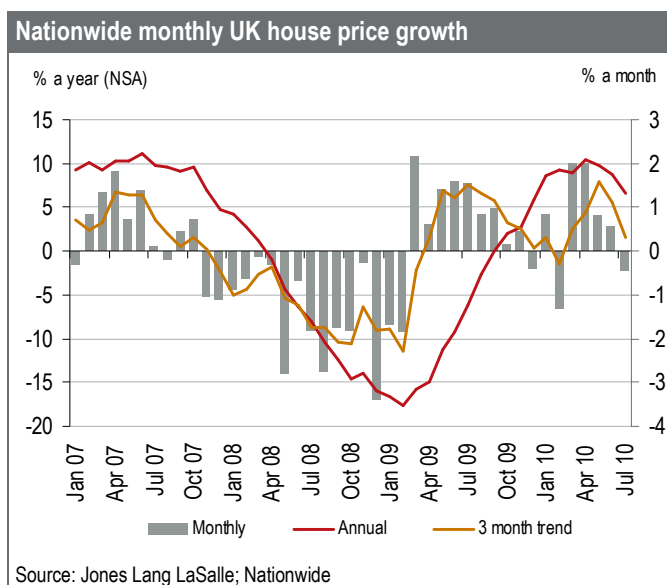
We are seeing definitive signs of a slowdown in capital growth across the UK housing market. In the last quarter, the quantity of stock available on the market increased, and in the last month we have started to see new applicant numbers reduce markedly for the first time in 2010. This shift in supply and demand dynamics coincides with the seasonal summer slow-down where historically the number of sales agreed is approximately one-tenth lower than the spring quarter.

The abolition of HIPs in Q2 led to an increase in property on the market. Average stock on agents books rose 8.1% in the last month, according to the RICS. Anecdotally, removing the HIPs barrier led to a marked rise in “test marketing” of properties by speculative sellers looking to capitalise on a buyer willing to pay “over the odds” to acquire in sought-after locations. In the first week of abandoning HIPs, Countrywide the UK’s biggest estate agency said it had seen a 68% increase in vendor enquiries against the same week last year.

### Price Changes

Residential property prices rose, on average, 2.9% during in the opening six months of 2010 when seasonally adjusted. Q1 contributed 1.3% of the growth with Q2 adding 1.6%. Annually the rate of growth has started to trend down, from a high-point of 10.5% in April; it reached its lowest growth rate in July this year at 6.6%. While we are not expecting prices to fall dramatically we do expect a degree of pricing stagnation in the short-term until the economic picture brightens.

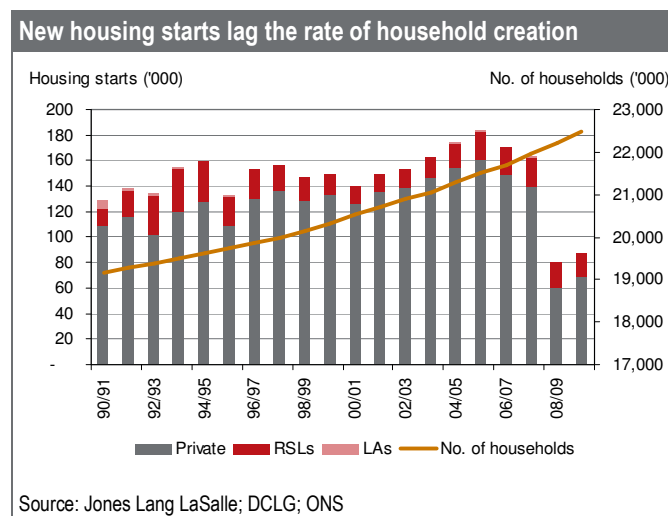
Prices have now risen 14.6% from their February 2009 trough, and sit 8.9% below the previous peak in capital values in October 2007.



### Housing Starts

The shortfall of newly constructed housing in areas of high-demand is likely to become increasingly acute. While NHBC figures show Q2 starts were up 42% against last year, this is building from a very depressed base. Following the new governments shake-up of the housing and planning system, applications for new starts were down 15% in June compared to May. It remains to be seen if this is a temporary blip, or a very rapid reaction to the austerity measures announced by the government.

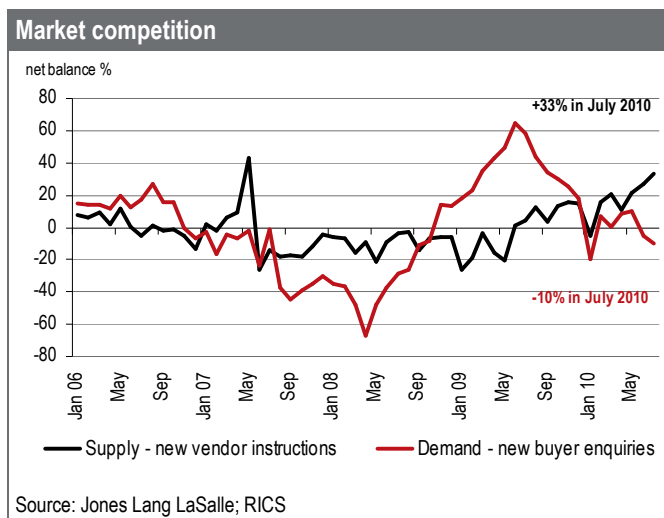
Private sector developers are also being hit as Local Authorities defer capital spending projects on housing and associated infrastructure something very likely to continue. The knock-on effect is a rise in social housing waiting lists, with the existing 4.5 million people currently on a waiting list projected to rise by 570,000 inside the next decade according to recent research from the NHF. A potential 40% cut in the affordable housing budget could lead to 230,000 fewer affordable homes being constructed between now and 2020.



At the same time, the rate of new household creation continues to rise unabated (as illustrated in the chart). Comparing the most recent annual figures with those a decade earlier, the number of households in England has risen 11%, while over the same timescale the number of housing starts sits at a level 42% below the prior decade. This situation is not being aided by the existing difficulty in funding new development so will accumulate greater demand for UK housing in future years.

### Supply and demand dynamics

A weight of evidence is building to show housing supply is increasing far faster than demand at present. Alongside the rise in stock levels reported by the RICS, recent figures show that sale instructions grew three times faster than the rate of new buyer registrations across the last quarter, according to Hometrack. Demand has been slowing in comparison to supply throughout the last quarter with consumer confidence knocked by the austerity measures and taxation implications of the Budget.



The shifting competitive dynamic was even more marked this quarter as data illustrates rising supply and falling demand. The net balance of supply increased from +27 in June to +33 in July. At the same time demand fell from -5 in June to -10 in July on the RICS measure of net balances.

The length of time an average property spends 'for sale' increased to 85 days in July, rising from an average of 60 days in June. This is reflected across the country as marketing a property becomes more challenging in the face of reduced demand.

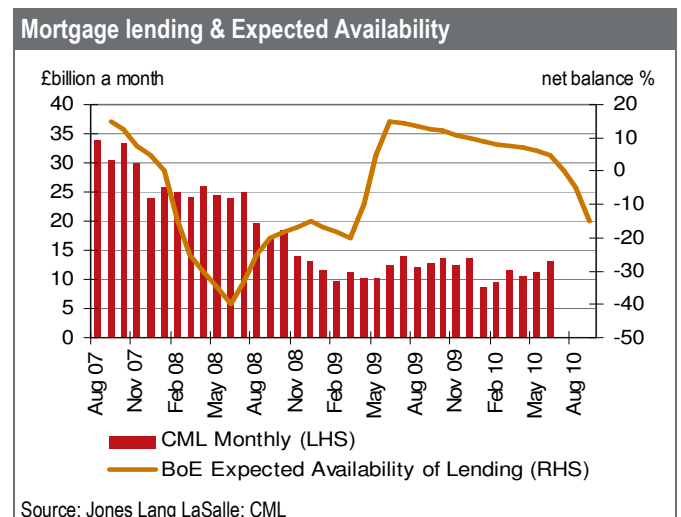
### Government Spending Review

The government review of public expenditure for 2011-2015 is currently underway. This will formalise the proposed public spending cuts proposed in the June Budget. The 2010 Spending Review will run until the autumn, and will set spending limits for all government departments for the period. In effect, this is where the market should learn more about the budgetary constraints for the Department for Communities and Local Government (DCLG), the Homes and Communities Agency (HCA) and other public bodies with a significant influence on the housing market.

### Mortgage lending and credit expectations

Gross mortgage lending was an estimated £13.1 billion in June, up from £11.4 billion in May, and 7% higher than this time last year, according to the CML. The results of the Bank of England's Credit Conditions Survey (Q2-10) show that overall demand for secured lending for house purchase reduced somewhat in the past three months.

Availability of secured credit is expected to decrease in the next quarter. The associated chart illustrates the continued historical weakness in gross mortgage lending according to the CML, allied to this; it shows the results of the aforementioned Bank of England survey. In part, reflective of lenders' expectations that wholesale funding market conditions might tighten in coming months. Thus liquidity constraints show no sign of easing.



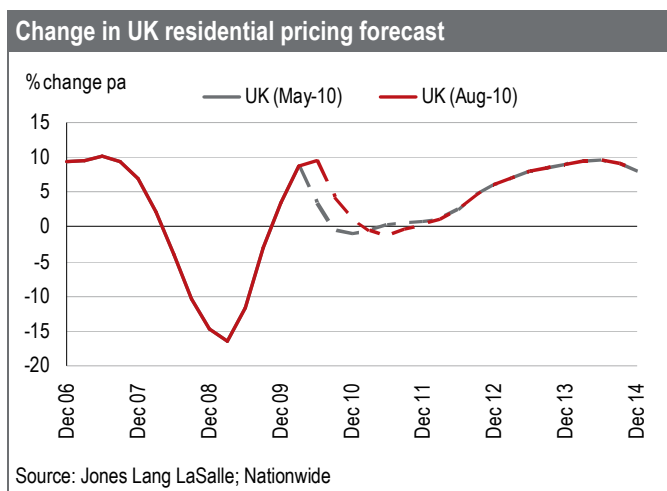
### UK house price forecasts

Short-term buyer/investor confidence remains fragile. The 3-month growth trend has fallen from 1.1% in June to 0.3% in July. We expect the tightened fiscal measures announced in the Budget to restrict UK spending, however the impact will continue to be phased in over forthcoming quarters.

The imbalance between increased supply and dwindling demand necessitated the current downward trend in house prices. The theme is substantiated by all the major housing indices to a greater or lesser degree. There remains no definitive evidence that prices are set for another wholesale correction, as witnessed in the 16 month period from late-2007 to early-2009.

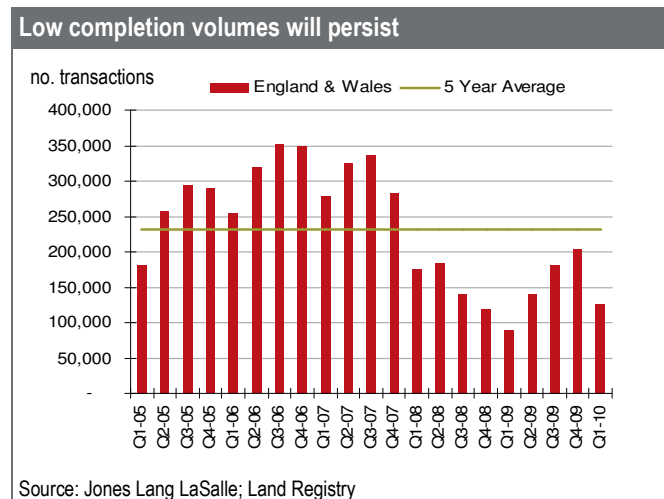
From current price levels, the outlook is for declines of 3.9% in the remaining five months of the year, in effect knocking more than £6,500 of the value of the average UK property.

Rather than 2011 leading to more solidity, we expect increased supply and spending cutbacks to lead to a further dip in Q1 and Q2. Rather than gaining 1% by the close of the year we expect prices to be flat.



The shape of the present dip in the market still takes the same form as previous forecasts, however the effect of public spending cuts and concerns around employment prospects are pushing out the recovery timescale. Our revised figures see virtually flat pricing at the close of 2010, up a marginal 0.5% on an annualised basis. We expect comparative exchange volumes to slow, rather than a huge price decline.

Comparative to the long-run average, the anaemic level of transactions persists in restraining capital gains (or losses). Recent exchange volumes, lagged the five-year first-quarter average by 31% in the opening quarter of 2010, as illustrated by Land Registry figures. Our forecast suggests little sign of a material pick-up in volumes in the short term.



Taking a strategic view of the impact, conditions stack-up in favour of renewed capital growth, at a level more consistent with the longer-term average. Metrics around the capital outlook from 2012 through 2014 remain positive with growth trending back in-line with the 10 year average, circa 7% per annum.

### Forecasts for the UK Housing

	Actual YoY %	Current	Short-term	Long-term
Average House Prices*	6.6%	↑	↓	↑
Transaction Volumes**	26%	↑	↑	↑
Housebuilding Starts***	60%	↑	↔	↑
Housebuilding Completions***	-16%	↓	↓	↑

Source: Jones Lang LaSalle; Land Registry; Nationwide; DCLG; NHBC

\* Quarterly prices (Q2-10)

\*\* Monthly volumes (Apr-10)

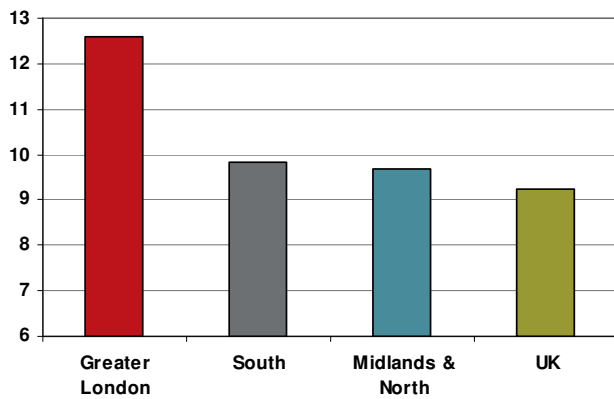
\*\*\* Quarterly housebuilding (Q1-10)

### London house price forecasts 2010-2014

Regionally performance in London leads the way, with annual growth across the last four quarters of 12.6%, more than 3% higher than the UK average. With levels of equity and disposable income far higher than average, London shows less likelihood of significant price falls than any other region. The wider UK figure is dragged down by sluggish performance in regions outside England.

#### Regional house price growth last 12 months

% change over Q3 & Q4 of '09, Q1 & Q2 of '10



Source: Jones Lang LaSalle; Nationwide

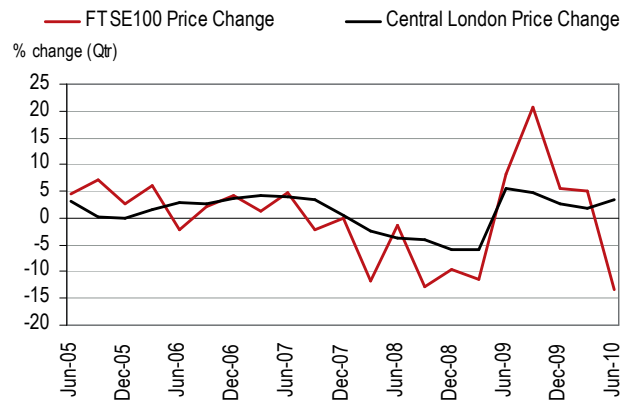
While there is increasing supply and decreased demand on the sales side, the reverse is true in the lettings market as rental property continues to perform strongly. Average asking prices in London rose 2.2% in the quarter, and are up 6% annually according to the Find-a-Property index. Rising demand and elevated asking rents are providing a welcome income boost for private landlords, despite the lack of short-term capital growth. Average gross rental yields in London are 4.71% up from 4.62% at the end of the opening quarter of 2010.

### London house price forecasts 2009-2014

Dec % Chg YoY	2009	2010	2011	2012	2013	2014
Greater London	7	1	1	7	12	9
Prime central London	8	2	2	9	13	10

The positive correlation between the performance of the FTSE 100 and central London house prices implies the market may be heading for a downward price correction in the short-term. This ties in with our forecast for price declines throughout the remainder of the year, followed by further marginal declines in the opening quarters of 2011 before prices stabilise and volumes increase.

### Central London pricing and stock market performance



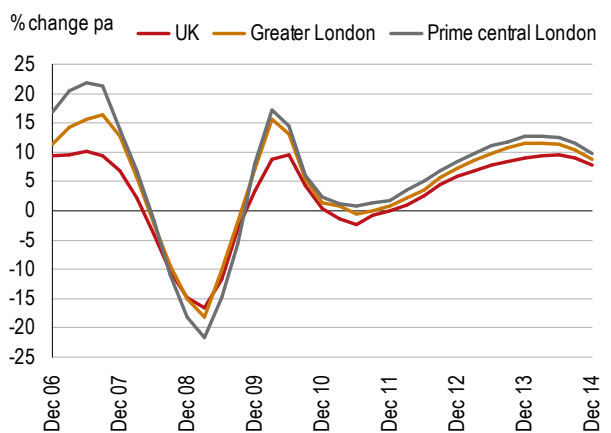
Source: Jones Lang LaSalle; Datastream

Changing government policy is having an impact on the London market. The emergency Budget was not as debilitating as first thought. With CGT capped at a flat rate of 28% the impact on investor sentiment was not as damaging as the 40-50% rate first mooted.

With no repeal to the proposed higher rate of stamp duty, at 5% for properties in excess of £1 million as of April 2011, the top-end of the London market is already feeling the impact of buyers and sellers spurred-on to secure a deal prior to the impending change. In effect, this will add a minimum of £10,000 to transaction costs.

Our central forecast continues to see property prices in all London markets outperform the UK average. Greater London house price growth is expected to be around 9% pa during 2012-2014.

### Forecast of London residential prices

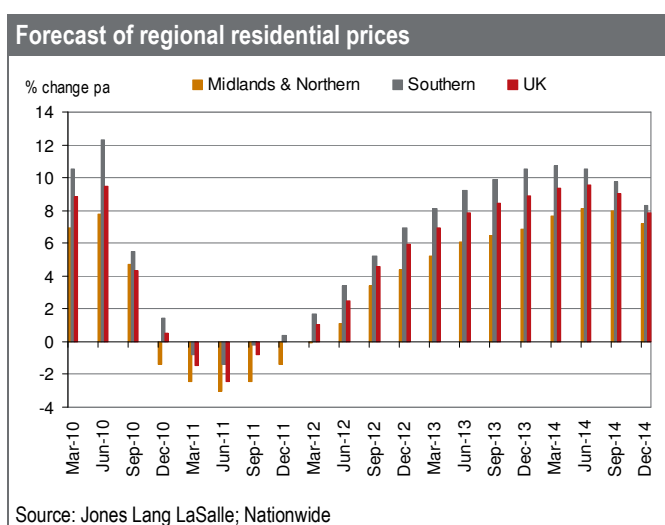


Source: Jones Lang LaSalle; Nationwide

### Regional house price forecasts 2009-2014

Regional prices in Southern areas of England outperformed the Midlands and Northern region, increasing 5.5% during the first half of 2010. In the Midlands and Northern market, growth remained subdued, rising, up 3.2%.

Having spent the best part of this year satisfying much of the pent-up demand garnered during the downturn, many of the would-be buyers have secured their new homes or investments. This is one of the factors behind the current dip in applicant numbers.



Demand is likely to become the real 'buzz word' across all regions of the UK, with many of the latest austerity measures taking hold. Employment, wage growth, disposable income and investable capital are all under pressure. One of the most direct impacts of the government cuts will be public sector employment.

Across the UK, public sector work accounts for an average 27% of all employment. However, this masks more than a dozen towns/cities where public sector employment accounts for over 40% of all jobs. The areas with the greatest dependence on public sector jobs will be most vulnerable to short-term house price declines as a result of the spending cuts alluded to in the Budget and set to be allocated via the Spending Review. In total 610,000 jobs are directly at risk and the weighted distribution of job cuts are shown in the following table.

Numerically urban districts and London Boroughs will be most affected, however they are better placed to absorb the impact through their private sector employment base. Nevertheless, research by Oxford Economics warns of the multiplier effect of reduced public services, with 2.3 million private sector jobs at risk as a result of spending cuts. Housing demand and pricing in peripheral areas are forecast to feel the greatest impact.

Rank	Top 10: Estimated public sector job losses by 2016	
1	Birmingham	13,205
2	Glasgow (City of)	10,942
3	Leeds	8,864
4	Westminster (City of)	8,672
5	Edinburgh (City of)	7,851
6	Manchester	7,628
7	Liverpool	7,523
8	Sheffield	7,014
9	Bristol	5,632
10	Newcastle-upon-Tyne	5,581

Source: ONS; OBR; Local Knowledge

Further ahead, and as the economy begins to improve house price rises will be more pronounced. London and the Southern market will head the recovery. We expect house prices to increase in the order of 8% pa in Southern locations during 2012-2014 and by 6% pa in the Midlands & Northern areas.

### Regional house price forecasts 2009-2014

Dec % Chg YoY	2009	2010	2011	2012	2013	2014
Southern	5	1	0	7	11	8
Midlands and Northern	1	-1	-1	4	7	7





*Real value in a changing world*

### Jones Lang LaSalle Contacts

**James Thomas**

Head of Residential  
Jones Lang LaSalle  
London  
+44 (0)20 7399 5584  
james.thomas@eu.jll.com

**Rob Bruce**

Head of Residential Research  
Jones Lang LaSalle  
London  
+44 (0)20 3147 1596  
rob.bruce@eu.jll.com

UK Residential Market Forecasts – August 2010

**OnPoint** reports from Jones Lang LaSalle include quarterly and annual highlights of real estate activity, performance and specialised surveys and forecasts that uncover emerging trends.

**[www.joneslanglasalle.co.uk](http://www.joneslanglasalle.co.uk)**