RESIDENTIAL MARKET UPDATE

Mixed start to 2013

The initial weeks of the New Year have been a mixed bag, with gloomy economic news being alleviated by evidence of falling mortgage rates and a striking pick up in transactions in prime central London.

Key facts

UK house prices fell by 0.1% in December, and are down 1% year-on-year

Prime central London prices rose by 0.2% in December, and ended 2012 up 8.7%

Prime country house prices declined by 1.2% in Q4 2012, leading to an annual decline of 3.8%

Prime Scottish country house prices fell by 2.7% in 2012

Knight Frank forecasts a 2% drop in mainstream UK prices this year

For the latest news, views and analysis on the world of prime property, visit Global Briefing or @kfglobalbrief

UK housing market and economic overview

Hopes that early 2013 would mark the start of a sustained economic recovery were dampened this week by independent data showing that economic output fell in the final quarter of 2012, raising the spectre of a 'triple dip' recession. The respected National Institute of Economic and Social Affairs (NIESR) said that the economy shrank by 0.3% between October and December. All eyes will be on the official GDP data for Q4, published at the end of January, to give a clearer indication of how the economy is faring.

There are some small signs of optimism in the housing market however. December's Knight Frank/Markit house price sentiment index showed that more respondents expected the price of their property to rise rather than fall in 2013. But in a market with low levels of transactions, the picture is increasingly localised.

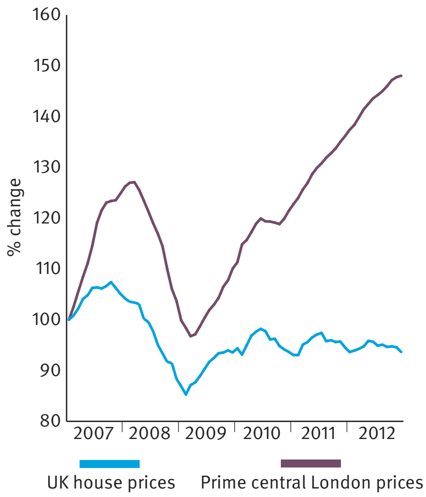
The mortgage market has also shown some green shoots over the last couple of months, with average rates for the handful of mortgages available for those with a deposit of 10% starting to recede.

On the other hand, expectations that the Bank of England's multi-billion Funding for Lending scheme would boost overall mortgage lending have yet to be met.

The central bank said that the real effects from the scheme, launched in August 2012, would not be felt until this year. Analysts will monitor mortgage approval rates closely in the coming months to get a steer on whether activity in the housing market is being spurred on by the Bank's cheap loans scheme. At present, the number of mortgage approvals each month remains near the lows hit in the wake of the financial crisis.

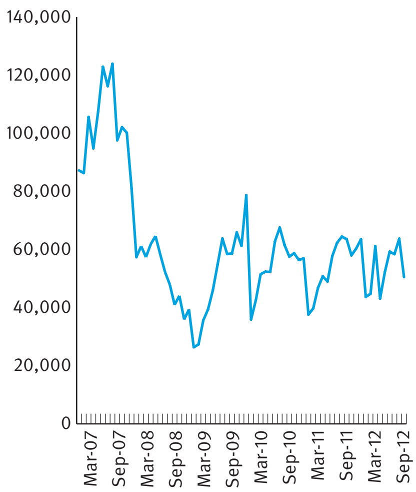
Meanwhile new analysis of house price data once again highlighted the full effect of the financial crisis on property values. It showed that in real terms – stripping out inflation –

Figure 1
How house prices compare: UK vs prime central London
Indexed Jan 2007



Source: Knight Frank Residential Research

Figure 2
House sales in England and Wales
Monthly transactions



Source: Knight Frank Residential Research, Land Registry

Follow Gráinne on twitter at @ggilmorekf

"Expectations that the Bank of England's multi-billion Funding for Lending scheme would boost overall mortgage lending have yet to be met."

Gráinne Gilmore, Head of UK Residential Research average UK house prices are down 22% from the highs seen in 2007. Knight Frank forecasts that mainstream UK house prices are unlikely to hit 2007 levels again until 2031 once CPI inflation has discounted.

Average UK prices remained broadly steady in 2012, falling by 1% throughout the year, according to figures from Nationwide. Knight Frank forecasts a further moderate 2% decline in prices this year, as prices come further back into line with average earnings.

Prime market performance

Prices in prime central London climbed by 0.2% in December, taking the annual rise in property prices to 8.7%. This follows a 12.1% rise in 2011, and a 10.3% increase in 2010. Prices are now 53% higher than the post-crisis slump in early 2009.

There was a noticeable pick-up in transactions in the market after the announcement of draft legislation for additional property taxes on £2m+ homes owned through company structures in December last year – a result of the pent-up demand as potential buyers waited to see how the new rules might affect them. Most of these transactions were by purchasers buying in their own name, the number buying through company structures has fallen sharply year-on-year, and is expected to remain relatively muted in 2013.

More evidence of how tax policy can affect market dynamics comes when examining trends in the country house market.

Average prices for prime country homes continued to fall in the final quarter 2012, ending the year down 3.8% compared with December 2011. But prices of homes worth £2m and £3m, fell more sharply, by 5.6%, which can be directly linked to the increase in stamp duty from 5% to 7% introduced in March 2012. Prices overall were more buoyant in 'hotspots' such as Esher, Oxford and Guildford.

Prices of prime property in Scotland ended the year down 2.7%, but Edinburgh bucked the trend, with a 0.6% annual rise amid a sharp uplift in activity.

Rental market

Average UK rents rose by 3.4% in the year to November as the constrained mortgage market prompts more people to move into rented property. In contrast, rents in prime central London, which are more closely aligned with employment in financial sector in the capital, have been falling for a year, and ended 2012 down 3.2%.

"PRICES IN PRIME CENTRAL LONDON CLIMBED BY 0.2% IN DECEMBER, TAKING THE ANNUAL RISE IN PROPERTY PRICES TO 8.7%."

Residential Research

Gráinne Gilmore
Head of UK Residential Research
+44 20 7861 5102
grainne.gilmore@knightfrank.com

Press Office

Daisy Ziegler
+44 20 7861 1031
daisy.ziegler@knightfrank.com

Recent market-leading research publications

The Wealth Report 2012

Taxation of Prime Property Dec 2012

The London Review Autumn 2012

UK Housing Market Forecast

Knight Frank Research Reports are available at www.KnightFrank.com/Research