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Predicting the Unpredictable

The great thing in prediction is to get your timing right – because everyone is right at some point. Knight Frank predicted a slowdown in the London market in the late summer and autumn, only to have one of the strongest markets in recent memory as the actual outcome. Will the predicted slowdown occur in 2007 instead?

Not if our current client load is any proxy for the market. We have never been busier and have been turning away business on a daily basis throughout the autumn – not across the board, but particularly in central London and more particularly at the upper reaches of that market. None of these clients have come back from holiday any less keen to buy and it is unlikely that they are alone. Demand seems firm, at the very least, but supply might be easing a bit as there seem now to be some opportunistic sellers appearing who see this as a good chance to cash in or realign their lives to maximum advantage. Some of these are sellers of properties that may have some sort of problem which puts them in the second, rather than first, league; in this sort of market, buyers tend to be more blind (or deaf) to the busy road.

Some prices have been spectacular. Scarsdale Villas is a pleasant street of family houses in Kensington that we often cite as a ‘benchmark’ example of its type. A house has

just sold there for £4.35 million which we had under offer for £1.75 million in 1998. A larger house, also in Kensington, was sold for well over the asking price of £12 million with seven bidders. The corresponding house in the country is subject to the same misalignment of supply and demand and has risen by a similar amount which would suggest that the link between the Kensington family house and the Old Vicarage is still in place – but neither are remotely in reach of the ordinary family any more. The vicar was priced out a generation ago: as the old quip goes, he was a middle-class man, living in an upper-class house, on a working-class income.....

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Though it seems as if this boom at the top end of the market has been going up forever, it is actually a relatively recent phenomenon – about a year old, in fact. Prices in the UK overall have been on an upward trajectory for all of this decade, but between 2001 and 2005 London was pretty subdued with prices rising only about 10% over the period. There were a few exceptional properties that bucked the trend and made the headlines but the surge is a recent one, just as

the Mainstream Market has cooled. This emphasises again the differences in this ‘world market’, powered by very different economics and drivers – particularly petrodollars, of both the hot and cold climate variety, and the City.

The statistics on buyers make interesting reading, with overseas buyers now representing 50% of all buyers – and 60% at over £4 million. This compares with 34% for that other melting pot, New York, 22% in Paris and, surprisingly, only 13% in the Asian hub of Hong Kong. And it is very much focused on the evergreen areas, broadly the boroughs of Kensington and Chelsea and the City of Westminster. Docklands,

which intuitively you might think would have captured the City tailwind, rose on average only 2% between 2001 and 2006 reflecting the effect of an elastic supply of new developments as much as any lesser demand from overseas. Incidentally, Docklands itself is really two separate markets: of flats with a view of the river – and the rest. The rest can take some time to sell even in a good market, the exception being Butler's Wharf which is a micro-market all of its own.

What does seem to have happened over the last fifteen years is that there has been a passing of the baton from the Prime Market to the Mainstream and then back again; where London leads the rest follows, or something like that. What is difficult to see now is how the Mainstream Market, which has clearly been driven by much lower and more stable interest rates than in the past, can go much higher without resort to some dodgy lending – there are no million pound bonuses to support this market. Abbey, the UK's second largest mortgage provider, is now lending five times annual salaries. In itself, if interest rates stay low (and that is a big 'if'), this is only flirting with danger, but what it does show is that the search for new business by lenders is starting to look like scraping the bottom of the barrel. How about Kent Reliance, who are now pushing a so-called 'Inter-generational Mortgage', where the mortgage term is fifty years and interest only? This is being sold as a solution to Inheritance Tax: you do your heirs the great favour of handing them a debt for their lifetime as well as yours so that they can avoid paying Inheritance Tax.

Thanks Dad. Or Morgan Stanley who will lend you a higher multiple of your salary in return for a slice of any up-tick in the value of your property. Feels like something someone might regret in a few years' time. And we have been here before – in Japan in the 1980s.

In the Prime Market, however, the 'weight of money' argument currently seems unassailable and the natural tendency is to

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extrapolate this forward, and for developers to do this both in prices they think they can achieve and in areas they can pull off the same trick. The Candy Brothers, famous for their bells-and-whistles finishes and the eye-watering prices they achieve, are heavily long on some major projects – Bowater House (which we now apparently have to call One Hyde Park) and the old Middlesex Hospital in the area north of Oxford Street (which we now apparently have to call NoHo). By all accounts both the buildings' eventual asking prices will be

stretching today's not exactly fire-sale prices by about double. Which doesn't mean to say they won't get them – it is reported that some in One Hyde Park have already sold – but it is certainly a leap of faith.

However, being contrarian is not something to be practised every day as you will be right occasionally – but poor for life. To be successful, you need to identify extremes against which to go contrary and

you need to get your timing right. The Mainstream Market, unless there was a real surge in interest rates, is more likely to sag slowly, like a cooling soufflé, through lack of any further impetus rather than burst like a balloon. With the current liquidity in the Prime Market, you would have to be brave to bet against it and the thing that could derail it is an extraneous event that is, in its nature, unpredictable. Nothing goes up forever – but it looks pretty positive now.

LONDON OFFICE

Property Vision Limited
8 Cromwell Place
London SW7 2JN
Telephone +44 (0)20 7823 8388
Fax +44 (0)20 7823 8188

COUNTRY OFFICE

Property Vision Limited
Great Farm Barn, West Woodhay
Newbury, Berkshire RG20 0BP
Telephone +44 (0)1488 669900
Fax +44 (0)1488 668843

ASCOT OFFICE

Property Vision Limited
Old Boundary House
London Road, Sunningdale
Ascot, Berkshire SL5 0DJ
Telephone +44 (0)1344 651700
Fax +44 (0)1344 651777

SOUTH OF FRANCE OFFICE

Property Vision France SARL
Immeuble HSBC, 1 rue Gubernatis
06000 Nice
Telephone +33 (0)4 93 92 79 35
Fax +33 (0)4 93 92 79 39

mail@propertyvision.com
www.propertyvision.com