

Polish commercial property market outlook is subdued

“Falling core inflation and high level of spare capacity in the economy...”

The National Bank of Poland (NBP) announces its next interest rate decision on August 24th. At its last meeting in June, the NBP left the reference rate unchanged at 3.5%, where it has been since June 2009. The three main factors behind this decision were: 1) headline inflation (2.2% in May) running below the target rate of 2.5%, 2) continuing falls in core inflation and 3) partly as a result, downward revisions to the NBP’s medium term inflation outlook (2.2% to 3.7% in 2012 vs. 2.6% to 4.6% in the February projection).

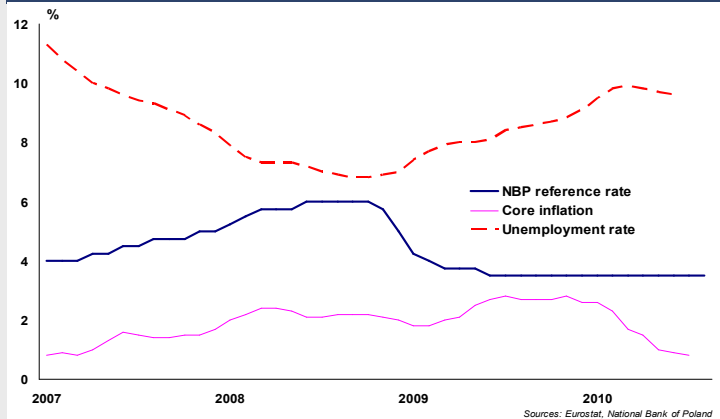
Key reasons for this cited by the NBP at its last meeting were relatively low levels of industrial capacity utilisation and a high degree of labour market slack. Since then, conditions have improved slightly; industrial capacity utilisation has picked up a touch (73.2% in Q2 from 72.4% in Q1) and the unemployment rate has edged down (9.6% in June from its post crisis peak of 9.9% in March). However, spare capacity within the economy remains abundant and significantly, it continues to bear down on core inflation (0.8% in July from 0.9% in June).

Relatively high, albeit falling, levels of spare capacity combined with falling (and relatively low) core inflation imply two outcomes that are likely to play out over the medium term. Firstly, high levels of spare capacity are likely to deter business investment and this means commercial property development is likely to fall further. Indeed, the latest results from the RICS Global Commercial Property Survey (GCPS) show development starts are already falling across all sectors

of the market. Secondly, low core inflation almost certainly means that the NBP will remain on hold for longer and may even cut rates if core prices continue to fall. The current disinflationary environment is unlikely to support asset prices and this includes commercial property. Indeed, RICS GCPS results show yields across all sectors of the market are falling (likely reflective of the medium term rental outlook), whilst momentum in capital values has almost come to a complete halt.

“...suggest that commercial property development is likely to fall and capital values may come under pressure”

There is abundant slack in the Polish economy



HKMA measures aimed at curtailing speculative buying in residential sector

“Occupiers appear to be taking advantage of the low interest rate environment”

The latest update on the Hong Kong residential property market is made available next week when the Hong Kong Monetary Authority (HKMA) releases its mortgage survey results for July. The June survey showed occupiers appear to be taking advantage of the low interest rate environment as demand for mortgages increased; the number of new applications picked up in the month by 8.2% from 20,283 to 21,947. Meanwhile, there was a modest decline of 5.1% in the number of new

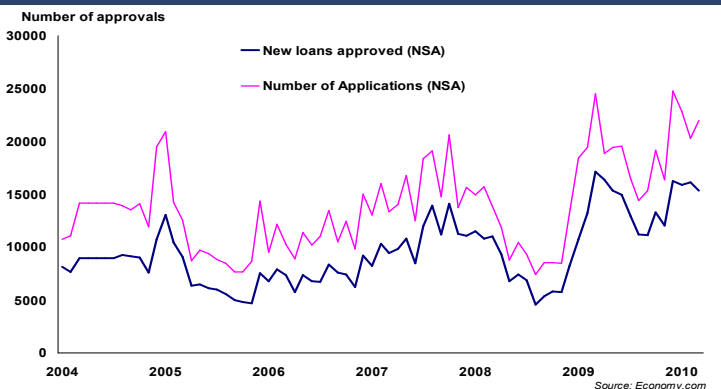
loans approved, while refinancing loans showed a greater decline as the number fell by 19.6% from May.

Interestingly, the HKMA announced a series of measures as recently as August 13th aimed at cooling upward momentum in the residential property market. The new proposals, ratified by the Financial Secretary, show the government’s improved resolve to curtail speculative purchasing and prevent an asset bubble. The measures will see a tightening of control over mortgage lending and mortgage insurance, which could reduce demand from speculators and in turn dampen further price increases. The key points of the measures are 1) that the LTV ratio has been lowered from 70% to 60% for all properties that are not owner occupied, and banks should require applicants to state whether they intend to occupy 2) the LTV ratio has also been reduced for all properties with a value at or above HK\$12mn; for properties valued below this, the 70% LTV guideline will continue to apply.

The measures are similar to those taken by the Chinese government in April, but lack clarity on the restriction of purchasers from outside Hong Kong; this allows foreign investors to take advantage of loose monetary policy and exploit Hong Kong’s attractive rental yields. The effects of these measures will not surface in the July survey results and could take some time to have the desired effects wanted by the government and HKMA.

“New measures will see a tightening of control over mortgage lending and mortgage insurance”

Mortgage applications are approaching high watermark



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US home sales outlook dependant on labour market

“Existing home sales fall 5% in June”

The National Association of Realtors (NAR) release their July existing home sales figures on Tuesday 24th while the Census Bureau publishes their July new homes sales the following day. Existing home sales have been falling in the last two months, declining 5.1% m/m in June. With the extension of the tax credits till September (to settle pre-May sales), this will give existing home sales

a slight boost in the coming months. Reflecting the amount of distressed properties coming onto the market, the month's supply of existing homes edged up to 8.9 months with distressed properties making up nearly a third of total sales. But prices are holding steady, with the median price of an existing home standing at \$183,700, 1% higher than a year ago.

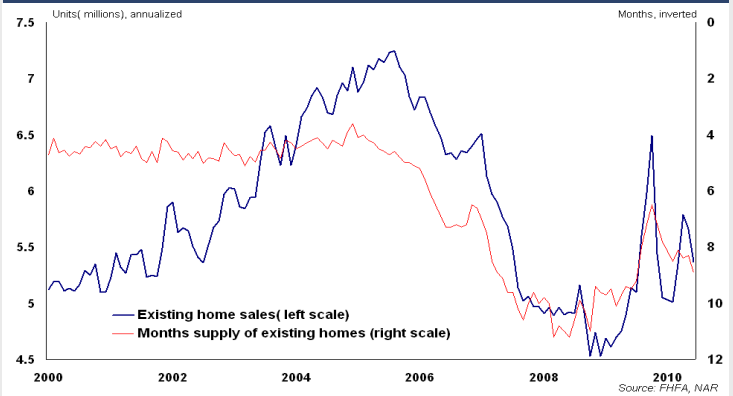
New home sales have been quite volatile recently, with the latest June figure rising 23% m/m. The monthly rise marks a solid rebound from May, when sales plunged by more than 30 per cent to a record low after the first-time homebuyer tax credit expired. In spite of the increase, sales remain depressed with June's tally representing the second-lowest on record. With new home sales 17% below June 2009 levels, housing starts continue to decline, with single family housing starts contracting 5% in June.

The outlook for home sales is heavily dependent on the state of the labour market. In this regard, the picture is quite weak, but there are grounds for cautious optimism. Job growth remains anaemic with the

latest non farm payrolls figure for July showing 71,000 private sector jobs created. This is still well below the 150,000 needed on a monthly basis to bring down the high unemployment rate (9.5%). However, the Federal Reserve's recent commitment to rates remaining 'low for long' and general change in bias towards more easing has brought down long term interest rates. This should in turn provide additional stimulus to economic activity and job creation over the medium term.

“The labour market remains weak but there are grounds for optimism”

Existing home sales fall in June



Outlook for UK residential market and construction sector has turned bleaker

“Buyer interest in the residential market is waning due to economic uncertainty”

The July lending figures from the British Bankers' Association (BBA) are released on Tuesday 24th and will be particularly closely watched for the mortgage approvals data. The data is seasonally adjusted and has been broadly flat since the beginning of the year; 34,813 mortgages were approved in June for new house purchase compared with 35,877 in January.

These numbers are some way below what was seen at the back end of

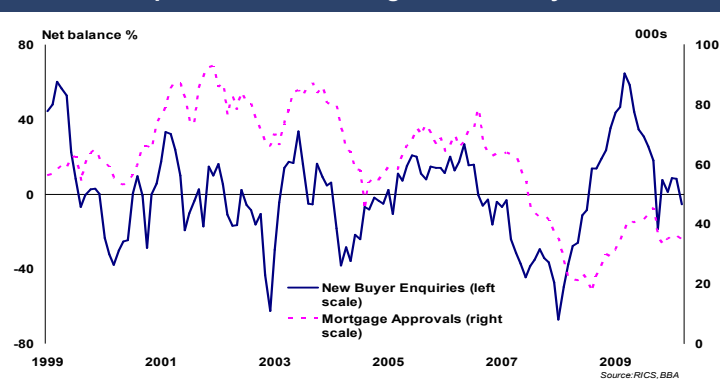
last year when purchasers rushed to take advantage of the stamp duty holiday that expired at the end of December.

Significantly, the most recent RICS Housing Market Survey suggests that buyer interest is waning in the face of the more uncertain economic outlook. The net balance on the new buyer enquiries series was negative in July for the second consecutive month, the first time this has been the case since the summer of 2008. This is broadly consistent with latest Bank of England Credit Conditions Survey which noted that demand for secured loans fell in the second quarter although the availability of funds actually increased.

The other interesting element of the BBA report relates to corporate lending. In June, net borrowing by the construction sector actually turned positive to the tune of £170m although lenders are continuing to scale back their commitment to the real estate sector. The latest RICS Construction Survey suggests that the recovery in workloads earlier in the year is already beginning to falter in the light of forthcoming public spending cuts. Private development plans are proving a little more resilient but concerns over the availability of bank funding is still an issue being raised by respondents to the report notwithstanding the slightly more positive tone to the BBA figures.

“Workloads in the construction sector are faltering”

Rental expectations now rising as availability moderates



RICS UK
T +44 (0) 20 7695 1682
pressoffice@rics.org

RICS Europe
T +32 2 733 1019
rics europe@rics.org

RICS Americas
T +1 212 847 7400
ricsamericas@rics.org

RICS Oceania
T +61 2 92162333
ricsoceania@rics.org

RICS Middle East & Africa
T +971 4 375 3074
ricsmiddleeast@rics.org

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