

Portuguese housing market set to outperform Spain in 2010

“Spanish house prices are down by 7.8% y/y and Portuguese prices have fallen by just 1.3% y/y...”

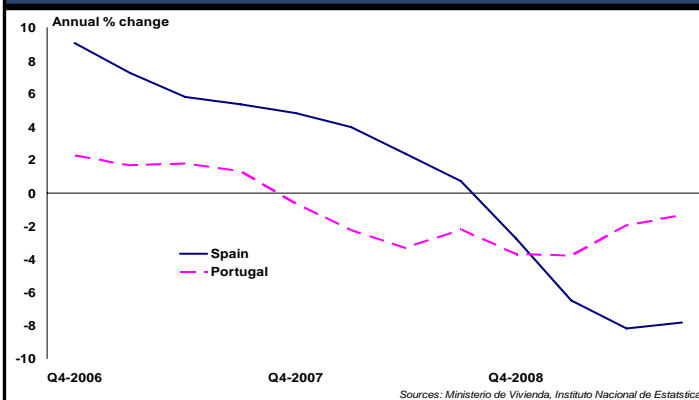
“...this is due to over supply in Spain and weaker demand”

- First estimates of third quarter GDP for the Euro area were released by Eurostat on Thursday 3rd. At the Euro area level, the recession has ended with GDP increasing by 0.4% on the quarter, but this still leaves output 4.1% below year ago levels. Focusing on Iberian neighbours Portugal and Spain, GDP increased by 0.9% on the quarter in former, whereas in the latter, GDP fell by 0.3%.
- In Portugal, house prices have been increasing for the last two quarters and are now only 1.3% below year ago levels (and 4.7% below their peak). However, the same cannot be said of Spain, where prices according to the Housing Ministry index continue to fall; they are now 7.8% below year ago levels and 9% below their peak (and about 13% below their peak according to TINSIA). The divergence can be explained, at least crudely, by differences on the demand and supply side. In terms of demand, the labour market has deteriorated far more sharply in Spain than in Portugal (due to a sharper contraction in the Spanish economy). Indeed, unemployment has only reached 10.2% in Portugal, compared to 19.3% in Spain. On the supply side, Spain has overbuilt, whereas Portugal has not. Residential investment as a percentage of GDP, a proxy for the degree of over/under building, exceeded the long run average in Spain (6.3% since 1995) between Q3 2001 and Q3 2008. By way of contrast, this measure has been below the long run average

(12.3% since 1995) in Portugal since Q4 2003.

- Looking forward, the Portuguese housing market is likely to continue outperforming the Spanish market throughout 2010. In light of the Q3 GDP figures, its labour market is likely to recover far earlier than Spain's. Meanwhile, Portugal has no excess inventory of new build to work off, whereas Spain, although making headway, still has its work cut out.

House prices have fallen less in Portugal than in Spain



Korean rates on hold as mixed data clouds outlook

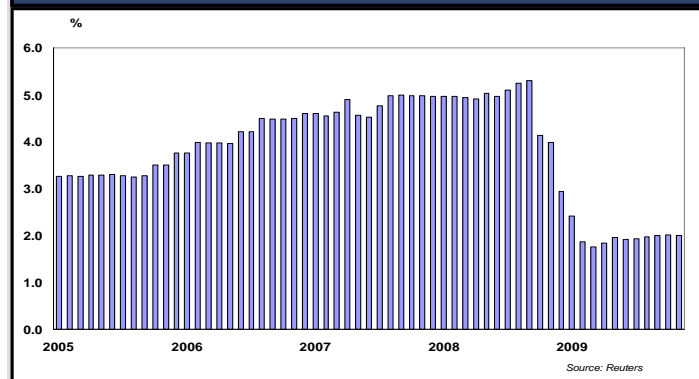
“The recovery in industrial activity appears to be moderating”

“..with rates set to remain on hold at next week's meeting”

- The Korean central bank meets on Thursday 10th to decide on interest rates amid some signs that the strength of the economic rebound in South Korea is moderating. Earlier talk of a rate hike to calm an acceleration in property prices has been toned down by central bankers in recent weeks as leading economic indicators have pared some of their earlier gains.
- The latest business survey of manufacturers has shown that sentiment toward the outlook for activity fell for the second consecutive month in November. Similarly, consumer confidence also fell back in November from a 7 year high in October despite the fact that house prices and employment have been on the mend for some months. The unemployment rate has fallen rapidly from a peak of 4% in June to 3.4% in October whilst in November house prices posted their first annual gain, since the downturn began. Minutes from the latest monetary policy meeting show that central bankers were unanimous in their decision to leave rates on hold at 2% during October. Of concern to policymakers remains growing uncertainty over the strength of the global recovery in 2010 as the effects of stimulus spending ease, and the current strength of the Korean won.
- One signal that central bankers are concerned over the volatility of growth during the recovery phase in the coming years has been a recent decision to widen the inflation target band. The Bank of Korea has widened its inflation target to between 2.0 %

and 4.0 % for 2010-2012 compared to 2.5 % and 3.5 % set for 2007-2009. The Bank of Korea stated that a widening of the band could help to give more emphasis to asset prices and economic conditions when setting monetary policy. RICS expect no change in interest rates next week although further measures to tighten mortgage lending criteria could be extended in the near term to prevent a renewed house price boom from destabilising the economy.

Interest rates to remain on hold



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Canadian housing market to recover further during 2010

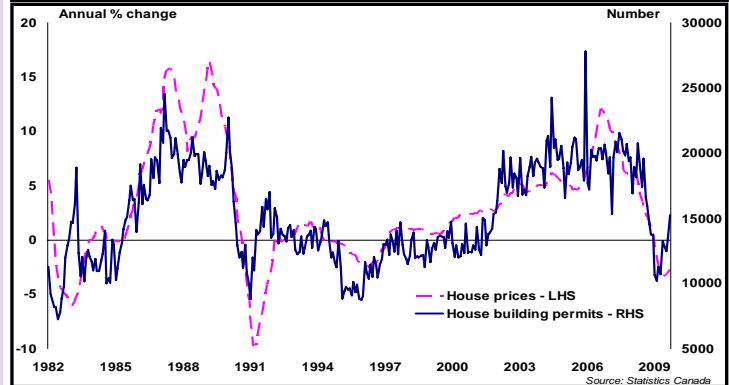
“Building permits are down by 4.1% y/y and house prices are down by 2.7% y/y”

“Improving economic fundamentals and low interest rates will boost building and prices”

- Canadian residential building permits data for October are due from Statistics Canada on Monday 7th and housing starts data for November are due on Tuesday 8th. In September, the number of permits issued totalled 15,250 (4.1% below year ago levels) and the number of annualised starts totalled 157,400. Permits are now 4.1% below year ago levels and starts are now 24.8% below year ago levels, but in both cases this reflects base effects. Indeed, building permits troughed in January (at 10,231) and starts troughed in April (at 118,500) and since then, both have recovered strongly. On the last reading, permits increased by 13.3% on the month, while starts increased by 5.4% on the month.
- At the end of the week on Friday 11th, house price data for October is due. In September, the national house price index was 2.7% below year ago levels, but over the last three months there has been a turnaround in momentum (measured on a 3 month on 3 month basis) and prices are now rising at a 1.1% annualised rate. However, this improvement in the national picture masks considerable regional variation.
- The rebound in house building and stabilisation of house prices reflects an improvement in a number of macro and financial indicators. GDP grew by 0.1% in Q3, marking the end of recession, and leading indicators of growth such as the Ivey PMI

survey have rebounded sharply in recent months. The labour market is also showing tentative signs of improvement, with the unemployment rate (currently 8.6%) now below its August peak (8.7%) and the unemployment sub component of the PMI index now in stable territory. On the financial side, mortgage rates have fallen to historically low levels thanks to the ultra low base rate (0.25%) and annual growth in mortgage lending (currently 7.5%) has accelerated in recent months. Against this context, the turnaround in house building and recent increases in house prices are likely to continue throughout 2010.

Canadian house prices have not fallen that far



Australian rate hikes adding to stretched housing affordability

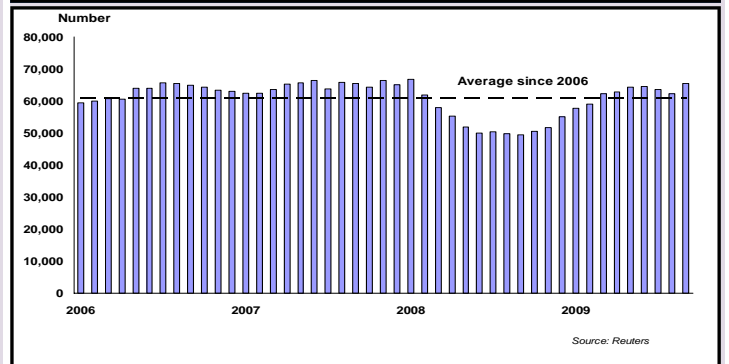
“Interest rates are at 50 year lows ...”

“...despite the fact that the economy hasn't entered into a recession”

- A raft of economic data is released in Australia next week critical to the near term outlook for the housing market. The state of the labour market will be gauged on Monday 7th with the latest release of the ANZ job advertisement figures. Typically, job advertising data tends to lead employment growth by between 6 – 9 months and will be closely watched for signs that the recovery in the jobs market is gaining momentum. Other key indicators next week include business and consumer confidence figures on Tuesday 8th and Wednesday 9th respectively. Housing finance is also released on Wednesday 9th with the latest unemployment figures due on Thursday 10th.
- The Reserve Bank of Australia raised interest rates by 0.25% for the third consecutive month this week, taking the level of interest rates to 3.75%. In a historical perspective, interest rates remain at an extremely accommodative level (still at 50 year lows). This is particularly significant given that the economy has not even fallen into recession and has suffered less structural scarring in the wake of the global economic downturn. Add into the mix, the lagged impact of a raft of government stimulus measures likely to add support to the housing sector in the coming months, then a case for raising interest rates aggressively back to more neutral levels appears to be mounting.

- Some measures have already been introduced to temper growth in house prices such as the halving in the government grant to first time homebuyers as of October 2009 and the phasing out of the “Boost Scheme”. For the coming months, however, the recent uptick in housing finance seems set to support further house price gains, which may add to concerns over stretched affordability.

Housing finance recovering adding support for prices



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