

Only modest rise in housing starts likely in England in third quarter

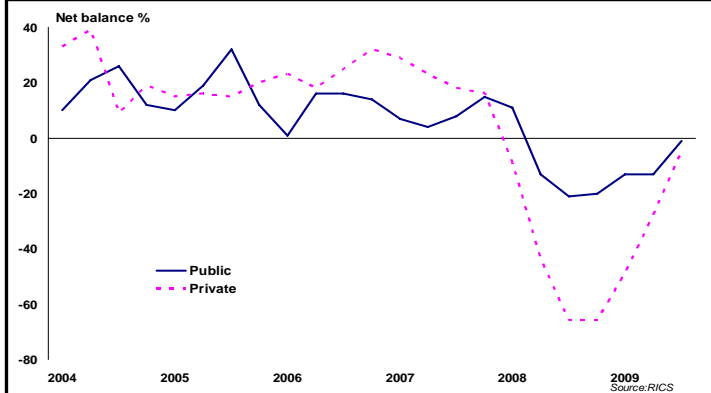
“The pick-up in activity in the third quarter is likely to have been modest...”

“...led by a bigger contribution from RSLs”

- Thursday 19th sees the release of the Q3 numbers on house building in England. Second quarter data showed starts of just 21,580 which, while up on the previous three month period, was way down on the 33,310 residential properties that were begun in the same period of 2008. The recent peak in this series was in the first three months of 2006 when 47,840 properties were started. With the trend in the number of housing completions naturally lagging starts, it is not surprising that the former are currently still coming in close to 30,000. However this picture will worsen over the coming quarters.
- The forthcoming data could show a bigger contribution to new build being made by Registered Social Landlords who have been beneficiaries of increased grant allocation from the Homes and Communities Agency. However, the pick-up in activity in the private sector is likely to have remained relatively modest. A number of house builders have reported good sales of existing inventory and have successfully attracted funding from the capital markets (which has in part been used to address balance sheet issues). However there continues to be significant problems relating to the availability of development finance. A recent RICS survey of members suggested only 10% had found it any easier to obtain development finance in the past three month period.

- Meanwhile, the latest RICS Construction Survey found that more respondents were still seeing private sector housing workloads fall (than increase) in the third quarter. More positively, the picture in the public sector appears to be stabilising. The pick-up in residential building activity over the next few years is likely to be very gradual. This will leave the headline figure way short of the target set out in the Comprehensive Spending Review of 2007, which was to raise the number of net additional homes per annum by 240,000 by 2016.

Housing workloads—change against previous quarter



German house price outlook highly uncertain

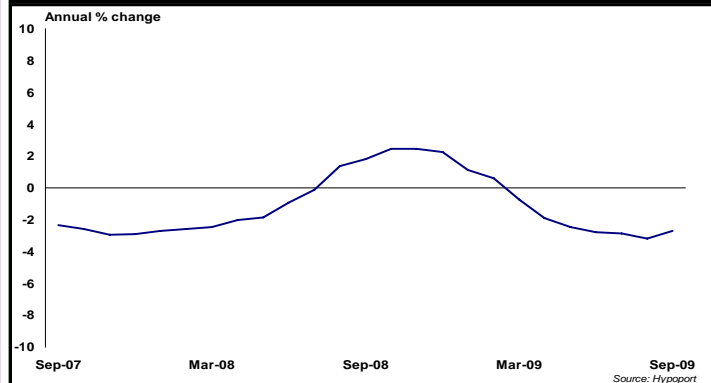
“German house prices have been relatively stable...”

“...but the outlook is very uncertain”

- German house price data for October is due from Hypoport next week. The headline index is down by 2.7% from year ago levels but prices are currently rising at 2.4% (three month on three month annualised basis). In contrast to the relative stability of German house prices, house prices in Spain fell by 7.8% in the year to September according to the Spanish Housing Ministry while other sources point to even larger falls.
- There are several factors that help shed light on this divergence in performance. First, on the supply side, the degree of over building in Spain has been huge, whereas in Germany, there has been a major lack of building. In Spain, residential investment as a share of GDP (currently 5.3%) remained consistently above the long run average (6.3% since 1995) between Q3 2001 to Q3 2008. However, in Germany, this figure (currently 5.5%) has remained consistently below the long run average (6.3% since 1995) since Q2 2001. Second, on the demand side, Spanish unemployment has surged from a trough of 7.9% in May 2007 to a peak of 19.3% in September. But in Germany, the unemployment rate has only edged up slightly from a trough 7.1% in December 2008 to 7.6% presently (and it has been at this level since July).
- Looking forward, uncertainties in the outlook for the German labour market could pose a risk to house prices. The short time workers scheme is limiting the rise in unemployment (by as

much as 1.4m workers as estimated by the OECD). The scheme involves full time workers agreeing to work part time rather than being made redundant, with the government compensating the shortfall in their earnings. However, this initiative is due to expire at the end of this year and that may have an adverse impact on the labour market. On the other hand, consistent with the pick up in manufacturing activity (industrial orders have surged in recent months), unemployment expectations have subsided, although they still remain above the long run average.

The housing market has been relatively stable recently



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Recovery in US housebuilding sector

“House-builder sentiment has slipped back”

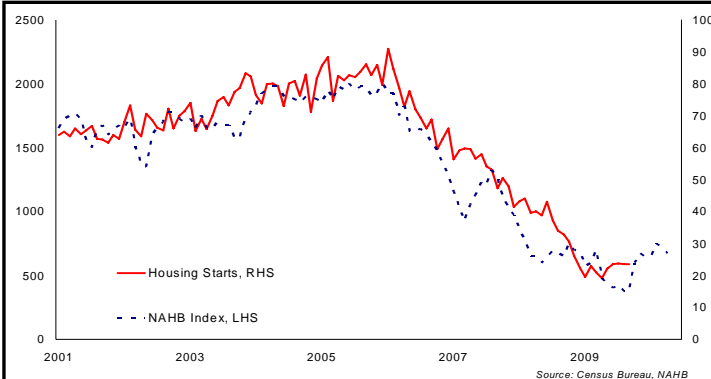
“Housebuilding activity is unlikely to improve much over the rest of the year”

- Next week, the NAHB survey of builders’ sentiment for November is due out on Tuesday 17th followed by housing starts data for October on Wednesday 18th. After some promising improvement in the middle of the year, the US housebuilding recovery has slowed to a crawl and, in some cases, even slipped back in the last month or so. A recovery in the housebuilding sector relies on expected increases in demand for new housing – and although recent positive news on the wider economy (such as a 3.4% annualised increase in GDP in Q3) and a small slowdown in foreclosures may have boosted consumer confidence, it will have been offset by the news that unemployment has risen to 10.2%, a 26 year high.

- Faltering confidence has also been evident in the most recent NAHB survey. All three key indicators – current sales activity, traffic of prospective buyers and expectations over the next six months – all slipped back in October’s survey. Present sales fell from 18 to 17, indicating that recent activity has slowed, and expectations are for more of the same. The buyer traffic indicator fell from 17 to 14 while expectations over the next six months slipped from 29 to 27. All in all, that took the headline indicator level from 19 back to 18. Although it’s unlikely that all the recent improvements will be unwound, housebuilders’ sentiment is likely to stay subdued over the winter so November’s numbers are likely to be relatively unchanged.

- It’s perhaps not surprising, then, that US housing starts data have also been sluggish and essentially unchanged at around 590,000 (seasonally adjusted and annualised) between June and September 2009. Admittedly, that’s a marked improvement from the 479,000 recorded in April 2009 but is still dramatically lower than the long run average (since 1959) of 1,520,000. Reflecting the fact that building permits actually slipped back in September, as well as the decidedly downbeat NAHB survey, housing starts are likely to hover around their current level over the remainder of this year.

Builders’ sentiment suggests slow recovery in housing starts



Japanese commercial property market starting to show some life

“GDP to show ongoing expansion”

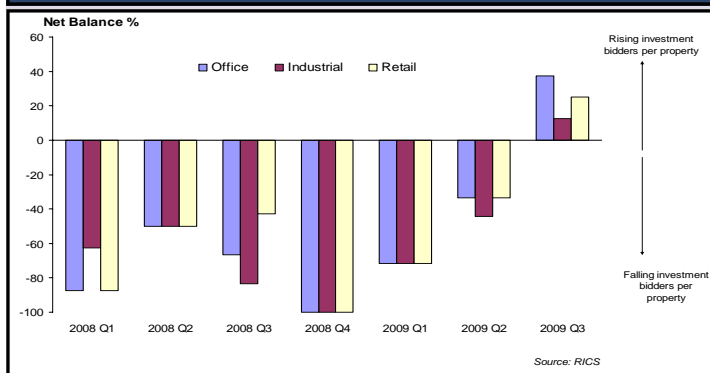
“although rates on hold as recovery remains fragile”

- Next week sees the release of several pieces of economic data in Japan key to property market developments. The provisional numbers for third quarter GDP will be released on Monday 16th whilst construction spending data is due on Tuesday 17th. On Thursday 19th, the Bank of Japan begins its two day monetary policy meeting with the announcement on interest rates due on Friday 20th.

- The upcoming GDP figure on Monday is expected to show that the economy continued to expand during the third quarter underpinned by the ongoing effects of government stimulus measures and a pick up in corporate capital spending. Leading economic indicators such as the manufacturing PMI, consumer confidence and the economy watchers survey moved higher during the third quarter signaling that a second successive quarter of positive growth is likely next week. The latest RICS survey of commercial property agents in Japan has revealed some modest improvements in the market since the second quarter. Lettings activity is no longer in decline and enquiries to occupy business property turned up for the first time in over 18 months during Q3. The improved conditions have lifted surveyor confidence towards the outlook for lettings activity into Q4 with the net balance indicator turning positive for the first time in a year.

- Rising availability continues to weigh on rental expectations, however, which have remained downbeat and virtually unchanged despite some modest improvements on the demand side. In the investment market, transaction activity has picked up with a rise in investment bidders per property most prominent in the office market during the third quarter. Amid a still fragile recovery, rates will remain on hold particularly as the outlook for activity in Q4 and early 2010 is less robust as the effect of stimulus measures wane.

Investment bidders per property now rising in Japan



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