

## Chinese property prices under increasing scrutiny following interest rate hike

**“September saw house prices rise for the first time since May...”**

September compared with a month earlier which was actually the first month-on-month rise since May. On an annual comparison, prices now stand 9.1% higher than a year earlier; the recent high point was 14% in April. A pick-up in capital inflows into China in recent weeks has, however, fuelled the suspicion that prices are set to resume an upward path over the coming months.

This assessment of the outlook for real estate is broadly consistent with the results of the RICS Q3 Global Commercial Property Survey which was released earlier this week. Responses to the questionnaire suggest that, both from an occupier and investment perspective, the pricing environment is firm. A net balance of 58% more respondents anticipate commercial rents moving higher in the near term while a broadly similar percentage project capital values continuing to be pushed upwards. Significantly, investment activity also remains firm with the average number of bidders per property climbing once again.

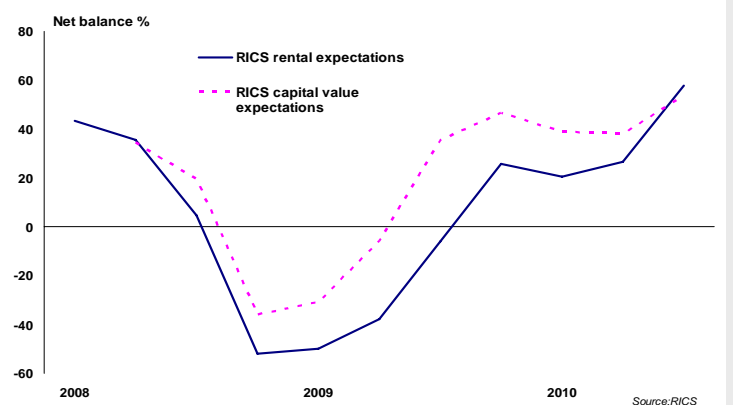
It is not entirely surprising against this backdrop that the Chinese central bank recently announced an interest rate hike and the government instructed lenders to request a 30% down-payment from

An update on the state of the Chinese residential market will be provided on Wednesday 10<sup>th</sup> with the release of October data on urban property prices. This will be followed on Thursday 11<sup>th</sup> with the publications of numbers charting the trend in fixed asset investment. Official data indicates that property prices were up by 0.5% in

mortgage applicants (for second home owners it is now 50%). The higher deposits required by the typical buyer of property should have some impact on demand but it is more questionable whether it will be felt at the upper end of the market. Ultimately more measures may still be required to prevent a real estate bubble developing although this could prove unnecessary if the steps already taken are rigorously applied.

**“...while the Q3 RICS global survey shows sentiment towards commercial real estate to still be upbeat”**

### Sentiment towards Chinese real estate remains positive



## Canadian house price gains look to moderate

**“Economy and housing market is starting to slow after three consecutive rate hikes...”**

The Canadian Mortgage and Housing Corporation (CMHC) releases the October figures for housing starts on Monday 8<sup>th</sup>, while StatsCanada releases its September house price index for new homes the following day. Housing starts peaked in April at 205,000 and have generally been trending downwards, reaching 186,000 in September but they are still above their long run average of

178,000. Meanwhile, new home prices resumed their upward crawl in August, gaining 0.1 percent on the month but the annual growth rate

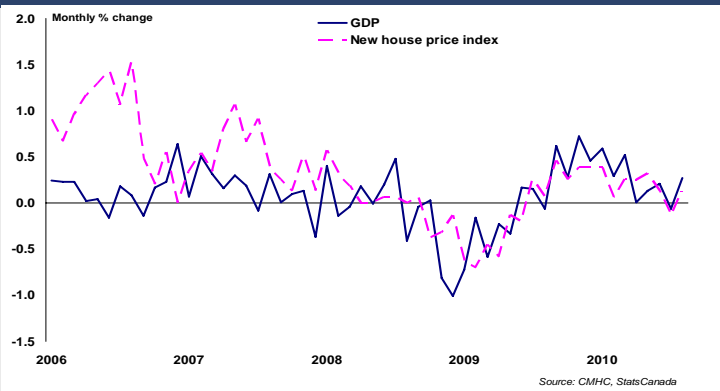
still fell to 3% due to base effects.

House prices have shown modest but consistent increases over the last year, against a strong macroeconomic backdrop, but both the economy and the housing market are now slowing. This follows the Bank of Canada's (BoC) three consecutive interest rate hikes from June to August as they start to normalise monetary policy. The BoC has made it clear that they would carefully consider the patchy recovery before hiking rates a fourth time, which is now not expected till early next year. Another factor that influenced the BoC's decision to pause monetary tightening is the economic woes of Canada's largest trading partner, the US.

Looking ahead, the decline in residential investment and softer house price picture is likely to continue, as past interest rate increases continue to filter through the economy. However, given the proximity of Canada to the US, this week's announcement by the US Federal Reserve to implement a second round of large scale asset purchases, may gradually provide some support to the Canadian economy, possibly limiting the overall downside facing the housing market and construction sector. However, the effects of such actions are unlikely to be felt in Canada over the near term, during which the current weakening trend is likely to persist.

**“...but US QE2 could provide tailwinds further down the line”**

### GDP growth slows



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## Subdued outlook for European commercial property rents

**“Divergent GDP growth trends between core and periphery countries...”**

The flash estimate of Q3 Euro area GDP is due from eurostat on Thursday 11<sup>th</sup>. Two outcomes are likely: first, that overall growth will be slower albeit positive, largely owing to the continued robust performance from core German and French economies. Second, beneath the headline level, growth in the periphery will have flagged. Indeed,

leading indicators are signalling that that growth could range between 0.35% and 0.6% in Q3, which compares to actual growth of 1% in Q2. Meanwhile the national PMI surveys continue to paint a very divergent picture between the core and periphery countries through to September, with economic activity expanding in Germany and France, while contracting in Italy, Spain and Ireland.

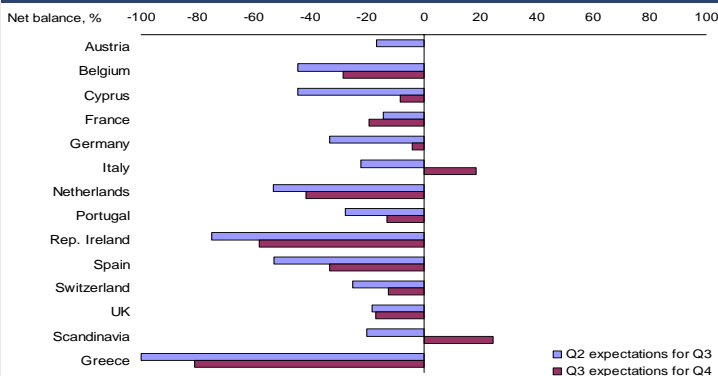
This divergent trend in economic activity is also largely being played out in the European commercial property sphere. Indeed, the Q3 results of the RICS Global Commercial Property Survey highlight continued growth in tenant demand in Germany and France. However, although tenant demand continued to weaken in Spain, Portugal and Greece, there were some notable exceptions with the results highlighting a more positive picture regarding tenant demand in Italy and Ireland. How much this is being driven by fundamentals is difficult to say, but we suspect, particularly in the case of Ireland, that this owes a lot to the elevated and increasing level of tenant inducements.

Beyond Q3, the leading indicators are not producing entirely consistent messages (the PMI fell while the Eurocoin edged up) but

overall they are signalling subdued GDP growth in the Euro area around the 0.3%-0.4% range for Q4. How this finally plays out in the commercial property sphere remains to be seen, but early indications from the RICS survey are that rents are still expected to fall in Q4 given the persistent supply overhang. Particularly large rental falls are still expected in the periphery countries Ireland, Greece and Spain.

**“...this is largely being played out in the European commercial property sphere, but there are some notable exceptions”**

### Rental expectations remain negative given supply overhang



## UK construction making strong contribution, or is it?

**“The first estimate of GDP indicated that construction output rose by a further 4% over the quarter”**

The surprisingly upbeat first estimate of Q3 GDP released last week indicated that construction output (based on provisional numbers) rose by a further 4 percent over the past three months, after contributing strongly to the Q2 rise in GDP. Indeed, over the past two quarters construction output has been responsible for almost half of the increase in GDP. Following on from this,

the more complete estimate for construction output for Q3 (including

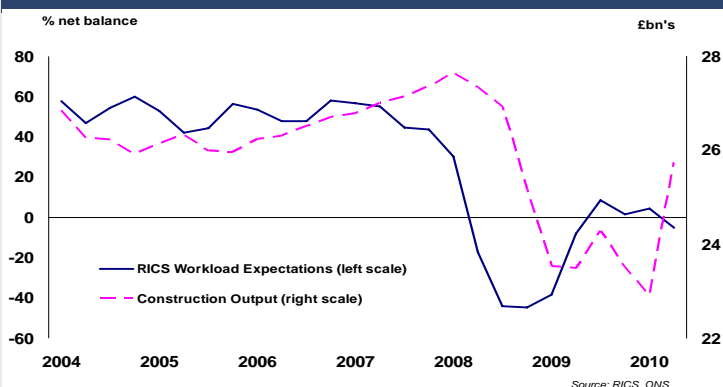
September data) is published by the ONS on Friday 12<sup>th</sup> and it will also provide a more detailed breakdown of underlying developments in the sector.

The recovery in construction output has been to date surprisingly broadly based given some of negative news stories doing the rounds about key parts of the industry. However, there is no doubt that the sector has been a beneficiary of the largesse of the previous government which, in the wake of the downturn in the economy, brought forward its planned capital spend sanctioning in the process a large number of new infrastructure projects. Unfortunately the construction orders data, which give an indication of future activity, is now only released on a quarterly basis. Nevertheless for what it worth, the last number showed a sharp drop in the value of orders placed from £13.5bn to £11.6bn. Alongside this, the more timely October CIPS Construction PMI survey is painting a slightly more downbeat picture; the headline reading of 51.6 was the lowest in the current eight-month sequence of expansion (where a result above 50 indicates positive growth). According to the survey, respondents are particularly concerned about the outlook.

Significantly, the third quarter RICS UK Construction Market Survey will be, released in the next fortnight. This should provide a little more clarity on the prospects not just for workloads and employment but also, critically, profit

**“Notwithstanding this, the provisional estimate for Q3 comes amidst more recent and downbeat dataflow”**

### Workload expectations have slipped



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