

Weaker German house price outlook for H2 and possibly beyond

“German economy is slowing”

In the light of recent turmoil in financial markets, RICS has revisited its outlook for the German housing market. The data shows that at the national level, price momentum eased during Q2. Indeed, the two main indices - Hypoport (monthly) and VdP (quarterly) - indicate that after a very modest rebound since mid-2009, annual price growth is currently

running between 2.3-2.8%, compared with 3.1-3.8% in Q1.

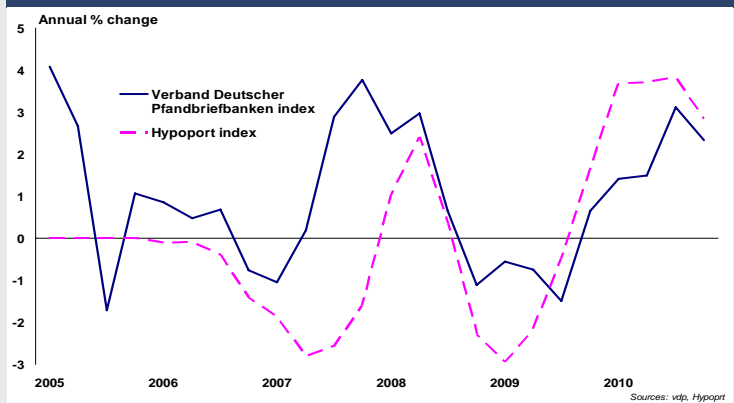
Although it is difficult to identify the cause of Q2's softer trend given the lack of detailed data, we nonetheless expect such weakness to persist through the remainder of 2011. Moreover, while it is not our central case at the moment, there is a growing risk of outright price falls. Were such falls to materialise, however, they are likely to be limited by the absence of any supply overhang. Indeed, future weakness in the German housing market is likely to stem from the demand side. Economic growth slowed sharply in Q2, but this was just one quarter's reading and average growth in H1 as a whole was still strong. More worrying than Q2's GDP reading is the deterioration in a host of leading indicators (PMI and IFO) which collectively suggest that the pace of activity is likely to be weaker in H2.

The weaker pace of activity signalled by the survey indicators – across the globe and not just in Germany - is likely to feed through to the labour market and knock consumer confidence. Currently the German labour market is incredibly strong; the unemployment rate is 6.1%, the lowest since April 1992. However, consumer confidence, as measured

by the European Commission's monthly sentiment survey, fell sharply in August. Moreover, unemployment expectations, a sub-component of consumer confidence turned positive for the first time in a year. In an environment where the pace of economic activity is slowing and consumers are turning fearful of losing their jobs, the housing market is unlikely to receive further near term impetus.

“ This is likely to feed through to the housing market”

German house price growth likely to slow further



Brazilian central bank cuts rates due to weakening economic outlook

“The BCB cut the key interest rate to 12% from 12.5%”

The Banco Central Do Brazil (BCB) surprised the market recently by cutting its main interest rate (Selic). The BCB said that a substantial deterioration in the global economic outlook was a key reason behind its decision to cut its overnight interest rate to 12%. The bank's monetary policy committee, voted five to two to lower the Selic rate from 12.5%, after five consecutive

increases this year. The statement accompanying the 50bp cut indicated that the BCB anticipates disinflationary pressures could arise from the current economic slowdown. In addition, the central bank

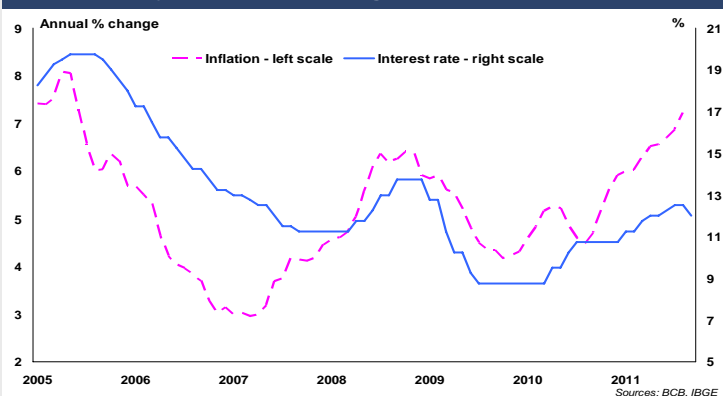
mentioned tighter fiscal policy as a contributing factor in favour of their interest rate cut. Interestingly, the decision goes against traditional monetary policy of generally not easing in periods of growing (and above target) inflation expectations and record low levels of unemployment.

While recognising that this pre-emptive move could help stabilise growth rates, the risks remain elevated. Indeed, inflation expectations have risen for 3 consecutive weeks and the IPCA (consumer price index) increased in August, from 6.9% to 7.2% (above the 6.5% upper limit of the inflation target). Therefore there is a real risk of inflation expectations becoming unanchored. Robust domestic demand (aided by ballooning credit growth) and high commodity prices still pose significant upside risks to rising inflation. Significantly, the cut in rates will lead to cheaper lending conditions. With credit rising 23% over the past year, a further acceleration in lending could 'overheat' an economy already suffering from severe supply bottlenecks.

We suspect that the recent cut was also biased by the fact that legislation relating to long term expenditure caps on government spending might finally pass through Congress. This, and other structural reforms aimed at government expenditure, should aid the central bank in bringing down the Selic rate to align it with international levels, as fiscal policy is tightened. That said, structural reforms have been languishing in Congress for several years, with lawmakers reluctant to curb their own spending powers.

“Inflation increased in August, rising from 6.9% to 7.2%”

Risky business...Cutting rates as inflation rises



RICS

the mark of
property
professionalism
worldwide

rics.org/economics

Higher UK unemployment poses a risk to the property market

“UK unemployment likely to rise further”

The coming week sees a slew of data published in the UK including the RICS Housing Market Survey and CPI inflation on Tuesday 13th, labour market figures on Wednesday 14th and retail sales numbers on Thursday 15th. Arguably the most significant of these is the labour market release which will give a further steer on how the softer trend in economic activity is effecting

recruitment. The claimant count measure of unemployment, which is the mostly timely indicator, is likely to record a sixth consecutive monthly increase in the jobless total. Meanwhile, the more broadly based ILO measure, reporting for the three months to July, should see the number of people actually looking for work moving back above 2.5 million for the first time since the early part of 2010. Consistent with this is a downturn in the vacancy to unemployment ratio which is effectively a demand - supply measure for labour.

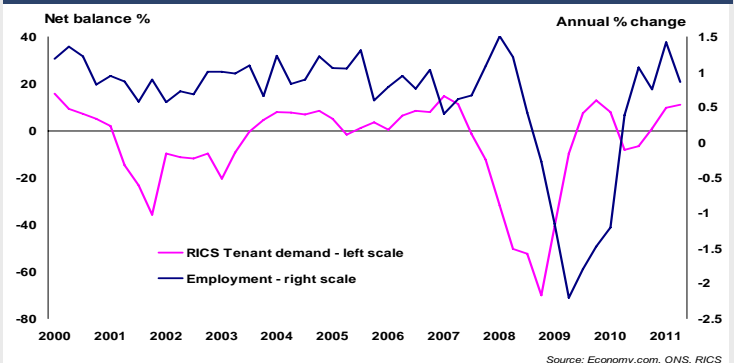
The official view as compiled by the Office for Budget Responsibility is for the ILO unemployment rate to edge up from 7.9% at present to a high of 8.3% before heading down again in 2012. Our suspicion is that the risks to the forecast are skewed on the upside with recruitment in the private sector falling short of expectations as over 300k jobs are lost in the public sector. The prospect of weaker growth through the course of next year and into 2013 strengthens the case for caution in this area.

Critically a flatter employment picture has ramifications both for the commercial and residential property sectors. The last RICS survey

covering the commercial market showed tenant demand edging upwards with a broadly similar trend visible in the office, retail and industrial segments. However, past relationships indicate that if recruitment were to begin to stall (and some surveys are suggesting that this may already be beginning to happen) tenant demand would turn negative once again. This would have inevitable consequences for the tentative recovery in rents that has recently become visible in some parts of the commercial property market.

“This will have inevitable consequences for property”

If recruitment stalls, tenant demand will follow



New Zealand housing market flattening as economy picks up

“The housing market had been sluggish over the past 12 months...”

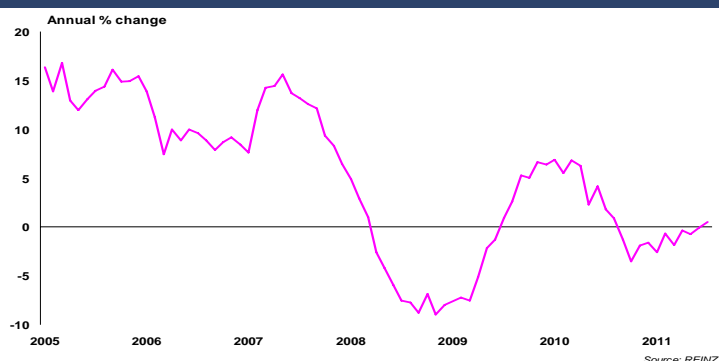
House price data for August is released in the coming week by the Real Estate Institute of New Zealand (REINZ). Meanwhile, the Reserve Bank of New Zealand (RBNZ) meet to decide the latest cash rate, with an announcement to be made on Thursday 15th. The cash rate is currently set at 2.5%, as it has been since March this year. Inflation

picked up above the target range (of between 1-3%) to 5.3% in Q2, increasing pressure on the bank to hike rates. However, the current fragility in global financial markets is clouding the outlook among major trading partners, who are cautious of a global slowdown. This is likely

to mean the RBNZ hold policy steady in the short term.

The latest reading of the REINZ house price index showed prices have broadly stabilised, growing by a modest 0.5% from a year ago. This reverses 10 months of falling prices as weak demand and 25 basis points of tightening in monetary policy held back the residential sales market. Indeed, the number of sales during July was 4,928; down by 301 from June and only 501 more than July last year, suggesting the market is largely flat. Supporting this is the latest reading from Quotable Value, which showed property values have steadied over the past month and are now only 0.4% below the same time last year. Furthermore, supply has remained relatively tight as permits to start work have yet to show a material improvement from the low point of 2009.

House prices are relatively stable



Slow wage growth and an uncertain economic outlook meant the housing market had been sluggish over the past 12 months, but is now beginning to stabilise as the economy gathers steam. The latest Business NZ PMI survey slowed a touch to 53.16, but remained above the mark of 50 which divides expansion from contraction. The employment component of the survey was particularly strong, rising to 56. If this continues in the August reading, which is released next Thursday, this could support a pick up in housing market activity.

“..but is beginning to stabilise as the economy gathers steam”

RICS UK T +44 (0) 20 7695 1682 pressoffice@rics.org | **RICS Europe** T +32 2 733 1019 ricseurope@rics.org | **RICS Americas** T +1 212 847 7400 ricsamericas@rics.org | **RICS Oceania** T +61 2 92162333 ricsoceania@rics.org | **RICS India** T +91 124 459 5400 ricsindia@rics.org | **RICS Middle East** T +971 4 375 3074 ricsmiddleeast@rics.org | **RICS Asia** T +852 2537 7117 ricsasia@rics.org

This newsletter contains economic and property news and analyses, edited by RICS. It should not be relied upon as professional advice and RICS accepts no liability for reliance on its contents.