November 2015

Stats, Facts & Points of Interest

- Knight Frank reported £443.1m revenue for the year ending March 31 – a 13% rise.

- Property Partner has so far attracted nearly 4,000 investors who have crowdfunded over £8.5m in buying properties. (Property Industry Eye)

- Data from Equifax Touchstone found investment buys across London in August of this year were up 71.7 per cent year-on-year. (The Times)

- Home says new inventory in London was down by 74% compared with September 2007… the lowest number of properties entered the market in London since before the financial crisis. (Property Industry Eye)

- Home sales in the £2m to £5m bracket were down by 16.9 per cent during the quarter…Homes above £5m appear to be less affected: sales in this bracket were up 23.5 per cent in the third quarter from a year earlier. (FT)

- At the top end of the prime London market, properties worth £5m+ saw average values fall -4.7% over the past year. The most expensive properties valued £20m+ saw transaction levels 26% lower. (Savills)

- 70% of the UK's homes worth £1m or more are in London, yet they constitute just 8% of all London households and 10% of all privately owned housing stock in the capital. (Savills)

- Planning application statistics indicate 220,000 people in England extended their home in the year to June 2015, adding an estimated £6.6bn to the value of their homes. (Savills)

- In 2014 19,000 properties sold for in excess of £1m accounting for 1.6% of all transactions.

- Residential Property made up just over one third of the value of all assets held at death by those paying IHT. Just 0.67% of estates notified to HMRC held net assets of more than £2m in 2011-12. The average value of residential property held in those estates was £1.3m. (Savills)

- Office availability in central London fell to a 15-year low during the third quarter of the year (Property Week)

- The Centre For Economic & Business Research said house prices will increase 22% by 2020

The World’s Biggest House Price Bubble

“The London housing market has formed the world's biggest house price bubble, according to analysts at UBS… And it warned that London house prices have become more "decoupled" from household earnings than anywhere else in the world.” City A.M.

I couldn’t agree more: household earnings have become completely decoupled from house prices.

However, this completely misses the point!

McGivern have you gone mad? If people’s earnings aren’t high enough to pay for mortgages then it is impossible for prices to go higher and prices must at least plateau if not fall. This is basic maths, you imbecile.

And again this is true (not the imbecile part, although feel free to disagree; my wife does…).

EXCEPT:

Haven't we all read articles bemoaning the fact that the streets of Mayfair, Belgravia and Knightsbridge are a desolate wasteland after 8pm because London is now owned by people who don't live here?

And what about all those nasty developers who have the effrontery to try to sell their properties for the highest price possible, so sell them abroad?

Would this suggest that using household earnings might give a slightly inaccurate picture?

Household income is the wrong figure for three main reasons:

1. It does not take into account the international profile of some buyers
2. It does not take into account the effect of Q.E.
3. It ignores how unevenly wealth is spread in the UK

Now imagine your family is worth £5bn (don't if you're worth £10bn). Your wealth grows at a modest 2% p.a. = £100m p.a. Now say your family decided to buy 50 apartments in Nine Elms. Do household earnings have any relevance? Of course not.

This is actually happening and I expect I have severely underestimated their wealth. Admittedly an extreme example but we can extrapolate:

There were "nearly a million (920,000) new millionaires globally in 2014, as High Net Worth Individuals grew in both number and wealth to 14.6 million and US$56.4 trillion, respectively." (Source: Cap Gemini)

The UBS study does not take into account the massive gulf between the UHNWI's, HNWI's and the rest. Nor does it take into account the fact that there are a handful of global super cities that are the target of an enormous amount of investment from across the globe.

QE has changed the game (I am not saying this is fair, these are just the facts). The wealth is also spread unevenly between generations. Those over 50 own over 40% of the housing wealth in this country. They also have a sizeable pension pot which can now be accessed more easily and a large percentage of it will end up in the property market (which is possibly one of the reasons for the extraordinary increase in the BTL figures noted in the Stats section).

This is incredibly bullish for house prices if not beleaguered first time buyers (unless their parents can act as the bank of mum and dad).

Furthermore, incomes are increasing while corporation tax will be decreasing over the next few years. This will attract even more investment into the UK which can only have one effect on land and house prices.

Then there is the advent of crowd-funding in property. This is tiny at the moment. It is early days, but it allows people who could not otherwise access the property market the opportunity to invest.

For example, the smallest investment is £100. This will allow money to be invested into the property market that could never have done so before. This again has to drive prices higher (although will end disastrously for many invested in these schemes).

These are just a few brief examples of the reasons to be optimistic about London property, but it also pays to look at history something which few mainstream economists and analysts seem to do.

In every property cycle there is a crash. This time will be no different and I expect the eventual bust to be calamitous. Likewise in every cycle the length of the boom confounds economists. Here are a few exerts from newspaper articles during the last cycle:

2000 – "Housing-market experts, from estate agents on the ground to analysts in the high-rise city banks, are agreed on one thing: this is more than the annual summer slowdown. House-price inflation has dropped considerably and, in some pockets of the capital - usually areas on the fringes of more fashionable addresses - where people were paying silly prices for bad houses, properties are indeed worth up to 10 to 15 per cent less than they were six months ago." **The Daily Telegraph**

2001 – "The house price indices are for once agreed: prices are slipping as the effects of recession take hold. Suddenly, the telephone-number price-tags of rather ordinary two-bedroom flats are beginning to look ridiculous." **The Daily Telegraph**

2002 – "The top of the property market has been in trouble for some time… Property in some outer London boroughs now changes hands at phenomenal multiples of average local earnings - the prices being pushed up by a relatively small number of people driven out of expensive parts of the city.

In Bromley, for example, house prices are now 10.4 times local earnings" **The Daily Telegraph**

2003 – "He [Roger Bootle] said: 'The message is clear. Houses are now so over-valued that a prolonged period of falling prices is on the cards.' … Some London 'hot spots' have already seen prices marked down in recent weeks, which has been attributed to lower City bonuses and Stock Market uncertainties." **The Daily Mail 1st March 2003**

2005 – "After five years of unstoppable price rises, the housing market has been showing signs of jitters." **BBC**

Which just goes to show that you do not want to rely on or be influenced by commentary in the press.

So we have been here before. Indeed look at the quote from 2002 – house prices were 10.4 times local earnings. Did property prices go significantly higher over the next 5 years? Indeed they did.

Now don't get me wrong. I am not saying that it is different this time and that prices can only go up. The exact opposite is true. This is exactly what happens in every property cycle:

- ✓ The market recovers after the previous crash
- ✓ The initial and biggest rises are in the wealthiest areas as these are the only people who have the means to buy or to whom the banks can/will lend
- ✓ Stock markets still seem volatile – city analysts, economists and journalists extrapolate this to house prices despite there being no historical evidence of correlation except during land price induced stock market crashes (not vice-versa)
- ✓ Headlines scream about house prices being too high
- ✓ House prices keep going up despite the press reporting the opposite or exaggerating the falls
- – A mid-cycle pause or even dip convinces the talking heads the market will crash
- – Lending criteria are slowly relaxed – house prices increase gently
- – Commentary in the press is still very cautious
- – House prices continue to increase and housing looks like the most solid investment

- Lending is relaxed further and prices begin to take off
- Commentary in the press becomes universally bullish – it really is different this time! House prices do only go up, we are in a "goldilocks economy", central bankers and politicians are demi-gods – blah, blah, blah. Prices rise 25%+ per annum
- Kaboom – surprise, surprise - it's not different this time. The new paradigm is shown to be a fraud. A major bank or two collapses "unexpectedly"; you know the story.
- The end of the world is nigh and the Four Horsemen of The Financial Apocalypse Will Be Riding Into Town – sell everything now
- The market recovers while the press reports continued problems and further imminent crashes
- The initial and biggest rises are in the wealthiest areas…

This is nothing new and it has been happening for centuries. If you don't believe me you can read the works of Fred Harrison, Philip J Anderson, Fred Foldvary, Homer Hoyt and others who have proven this.

Of course, complacency must be avoided. A seismic shift in government policy on property ownership could endanger the market but then that is true of anywhere.

But despite the seemingly high prices, the London property market is actually on an extraordinarily sound footing:

Savills in conjunction with Lloyds' Bank studied the purchases of properties over £1m since 2011. 50% were bought 100% cash and a further 25% were bought with mortgages of 50% or less. This is rock solid lending to individuals who are credit worthy – if you have applied for a mortgage recently you will know that the days of self-cert mortgages/liar loans are history (for now!).

The real concern is that people are being priced out and the papers regularly contain articles and letters complaining about gentrification. But this is nothing new. London will simply expand. This has happened in every property cycle going back hundreds of years.

I remember a talk at school during the dreaded "Business Week" given by an entrepreneur who mentioned that his great, great grandfather had once lost 200 acres of fields in a game of poker. Those fields are now called Wimbledon.

Indeed when I first rented a flat in Notting Hill in 1989 many houses off the Portobello Road were crack houses. Meanwhile, Northcote Road, the epicentre of what is now described as Nappy Valley (because of the number of baby shops and mothers with prams) was where one went to get stabbed on a Saturday night.

Hammersmith, Shoreditch, Kensal Rise, Maida Vale, Soho, Marylebone and Bloomsbury to name but a few were decidedly fourth rate and to be avoided only 20 years ago.

Gentrification is just the natural evolution of a thriving city. If you are making more money then you naturally want nicer things/surroundings. This is human nature. Of course, if have owned property in these areas for years then you will be sitting on a handsome asset. If you rent then you are in trouble.

What do you think the effect of Crossrail, HS1 and Crossrail 2 will be? It will make London bigger, more accessible and prices will increase where the stations are built. If the investment in the Northern Powerhouse happens then you will see the same there.

In the meantime expect to read many more articles expressing horror at house prices and tales of impending crashes. But remember this is a good thing, because it means that there is still plenty of money sitting on the side lines.

When the commentary becomes relentlessly bullish and you hear the words “It’s different this time” or the more pompous “It’s a new paradigm” then it will be time to head for the exits or reduce debt.

In the meantime, the wall of worry is distinctly good news.

Does this mean that you should run to your nearest estate agent and buy what you can? No. Certain properties will always outperform others and there are some severely mispriced properties on the market right now.

However, we have acquired a number of homes and investments for members recently as there are a number of good opportunities amongst the overpriced, average rubbish.

Interestingly, the number of applications for membership that we have received in the last two months would suggest that demand will be much higher next year as this year’s uncertainty fades.

Hopefully the press will not pick up on this and continue to rubbish the market as this is good for us.

Good luck with your search for a property in London.

Best regards,

Jeremy

p.s. If you have any questions or would like to discover how we can help you acquire your ideal home or investment on the best terms possible, please contact Veronika at veronika@mercuryhomesearch.com or call 0800 389 4280 (or +44 800 389 4280 from outside the UK).