MARKET INSIGHT
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After the storm: The tenth anniversary of Lehmans

PRESTON BENNETT

In association with HAMPTONS INTERNATIONAL

CONTENTS

HEALTH CHECK

With a mix of headlines regarding the state of the UK economy, where are we today?

Generally the UK economy is performing steadily, albeit unspectacularly. The headline numbers behind the UK economy are looking okay, but there are weaknesses behind some of those figures.

The latest data for UK economic growth beat expectations, with GDP rising 0.4% in Q2 this year. But looking ahead, the Bank of England expect the economy to grow around 1.75% over the next few years. Modest, but not exactly exciting, particularly compared to the United States whose economy is growing at over 4%.

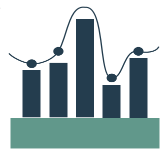
Inflation has been rising, but with incomes failing to keep pace, saving for many households has been a struggle. However, this changed last month when incomes grew 2.6% over the last three months, beating inflation at 2.4%.

Spare capacity in the UK's labour market is beginning to run out with unemployment at a 43-year record low, and this is finally putting pressure on wages to start rising. But despite that, productivity is still sluggish. According to the International Monetary Fund (IMF), by Thursday afternoon, the average US or German worker has produced as much as a UK worker manages by Friday afternoon. However, productivity is hard to improve without investment.

The good news is that despite two hikes over the last 12 months, interest rates are set to stay low. In September, the Bank of England voted to hold interest rates at 0.75% and the financial markets are forecasting just one, potentially two, further interest rate hikes by 2020. And this is good news for mortgaged households and should help support demand.

But the latest interest rate rise hasn't really had much of an immediate impact on the market. Around two-thirds of mortgaged households are on fixed rate mortgages according to UK Finance and haven't been directly impacted by any interest rate hikes. Additionally, it seems that most lenders had already priced in an interest rate rise, which has meant that mortgage interest rates have barely crept up.

So overall, the economy is looking steady, but Brexit uncertainty still looms large. Leaving the EU without a deal still poses the biggest risk to the future. But the good news is that the fundamentals supporting the economy and housing market are in a better place than they were ten years ago and this builds a firm foundation for growth in the future.



Over the next few years, the Bank of England expect the economy to grow around

1.75%

This is in comparison to the United States whose economy is growing at

4.2%

10 YEARS ON

The housing markets recovery following the 2008 financial crash.

On 15 September 2008, Lehman Brothers filed for bankruptcy, sparking what was to become one of the worst financial crisis in living memory.

In the 14 consecutive years leading up to the Lehman's crash house prices across England had been rising at an average annual rate of just over 10%. But in 2008, as homeowners struggled to repay their mortgages prices fell by 4.1% on the previous year and continued to fall throughout 2009. In 2008, 377,200 households went into arrears, forcing many to sell.

The recovery, when it came, was far from uniform. In London it took just two and a half years for house prices to return to their 2007 peak, but in the North East prices struggled to recover and today remain below their pre-Lehman's peak.

Prime Property led the recovery

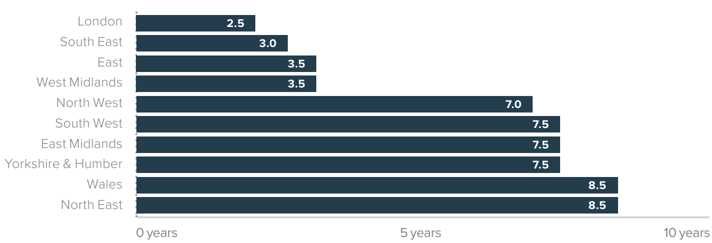
It's the most exclusive properties that have delivered the best returns. Across prime London the average price of a home has risen 80% since Q1 2008, compared with 65% across non-prime areas of the capital.

While the average cost of a prime country home has risen just 25% over the last 10 years, compared to 88% for prime city homes. But the tide is turning and for those leaving the capital, prime country now looks good value.

> *"Looking ahead we expect to see continued slow growth into 2019, with small price falls in London and some areas of the South."*

Time to Recover

Source: Land Registry & Hamptons International



In London, house prices returned to their 2007 peak in just

2.5 yrs

Until Stamp Duty put the brakes on
By 2014 such was the recovery in the housing market that George Osborne, then chancellor, introduced higher rates of taxation to slow growth at the top-end of the market. At the same time he made it cheaper for those buying homes under £1million. The net effect was to dampen sales over £1million, a market which continues to struggle today.

In April 2016 Osborne introduced further taxation in the form of a 3% stamp duty surcharge on second home purchases, which in turn led to a reduction in the number of properties bought by landlords. In fact, since April 2016 landlords have sold 103,000 more homes than they purchased.

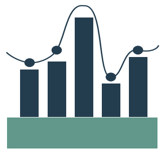
Outlook
The future of the UK's housing market will be dictated by the future path of the economy, which in turn depends on the terms of the UK's exit from the EU.

But the economy is performing steadily. A pickup in wage growth, which is now rising faster than inflation, is good news for households. This combined with low interest rates and healthy availability of mortgage lending provides upside. However affordability is still biting and this combined with Brexit woes will continue to impact on sentiment in the months' ahead.

Across the UK, house prices are rising at a modest 3.0%. Looking ahead we expect to see continued slow growth into 2019, with small price falls in London and some areas of the South.

However, in prime central London we expect to see price rises next year, although most of this is just correcting from previous falls. Meanwhile first-time buyers benefitting from stamp duty relief are expected to keep the lower end of the market active too.

But unlike ten years ago, the challenge today isn't about getting prices to recover, it's about getting people moving again.

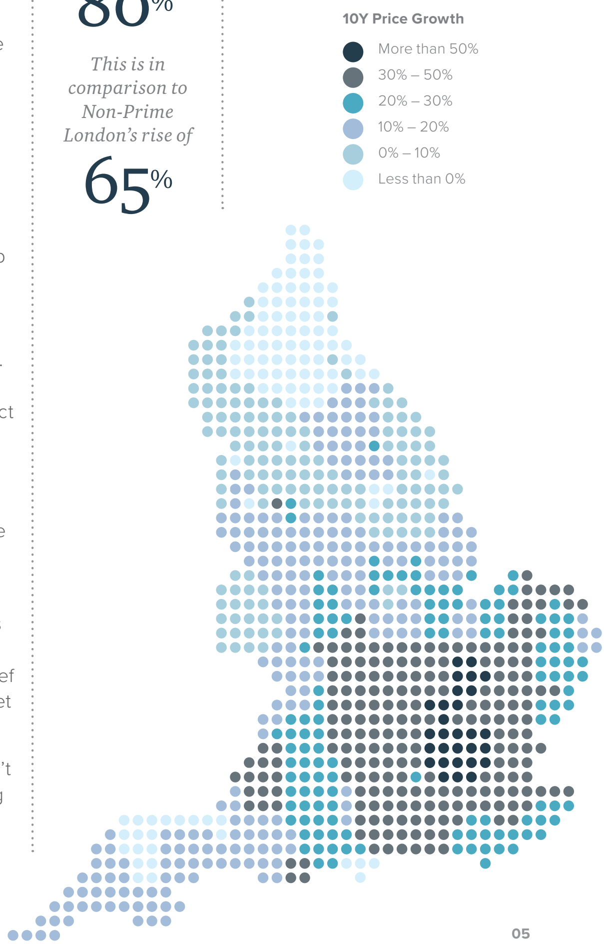


Since Q1 2008, Prime London has seen the average price of a home rise by

80%

This is in comparison to Non-Prime London's rise of

65%



MARKET METRICS

Transactions (HMRC)

Transactions in England, Scotland and Wales were flat year-on-year in August. But during the first eight months of the year, completions are 8.0% lower than during the same period last year. This chimes with other data showing a softening in the market.

0.0% YOY

-8.0% YTD

Mortgage Approvals

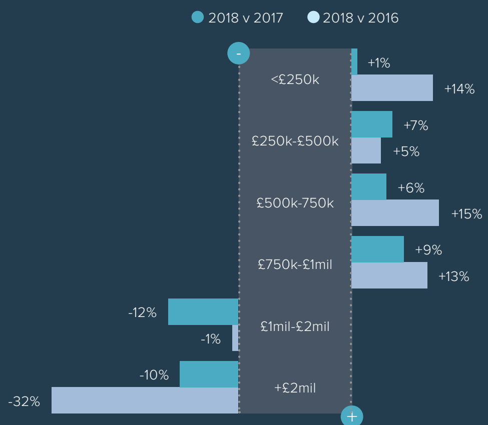
Bank of England mortgage approvals are a good indicator of future transactions, but suffered a poor month in July. Approvals fell -6.0% year-on-year in July. But year-to-date mortgage approvals are relatively flat. Remortgaging activity continues to drive growth, whereas house purchase approvals are weaker.

-6.0% YOY

-0.3% YTD

Stock Levels

Source: Hamptons International



Interest Rates

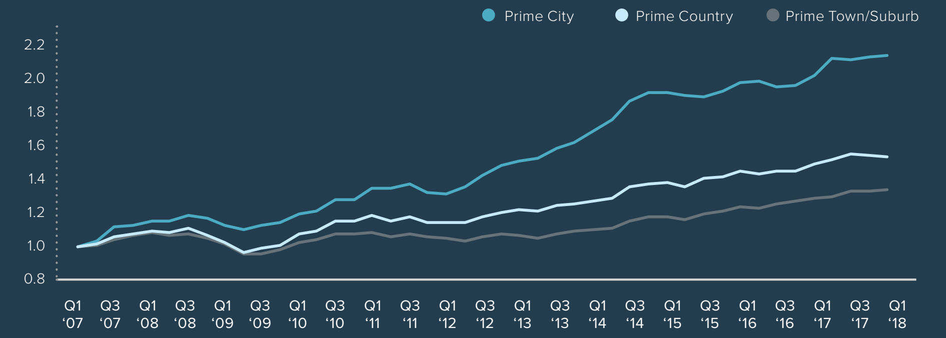
Source: Bank of England

Mortgage Interest Rates	Aug-18 Interest Rate	YoY Change
2Y Fix • 75% LTV	1.75%	0.32%
2Y Fix • 90% LTV	2.28%	-0.1
5Y Fix • 75% LTV	2.04%	0.1
2Y Variable • 75% LTV	1.71%	0.32%
Standard Variable (SVR)	4.33%	0.0
Buy to Let 75% • LTV Fixed	2.27%	-0.28%

Deposit Rates	Aug-18 Interest Rate	YoY Change
Instant Access Savings	0.22%	0.08%
1Y Fix Cash ISA	1.35%	0.24%
2Y Fix Cash ISA	1.22%	0.12%
1Y Fixed-Rate Bond	0.82%	-0.04%
2Y Fixed-Rate Bond	1.3%	0.14%

House Price Growth (Q1 2007 = 1.0)

Source: Hamptons International & Land Registry



Price Growth

Source: ONS

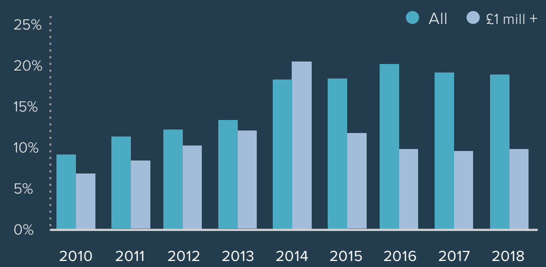
▲ 3.0% GB YOY

▼ -0.2% LONDON YOY

▲ 3.3% SE & SW YOY

Sold Above the Asking Price

Source: Hamptons International



Days to Sell

Source: Hamptons International

Instruction to Offer Accepted	GB	London
2012	54	40
2013	48	29
2014	38	25
2015	54	34
2016	34	29
2017	36	46
2018 YTD	36	45

NEW LETS VERSUS RENEWALS

Rental growth on new lets is slowing, despite low stock levels, but rents on renewals remain robust.

Rental growth across Great Britain has slowed this year, despite there being fewer homes available to rent on the market. The 3% stamp duty surcharge on second home purchases combined with the tapering of mortgage interest tax relief has reduced the number of homes available to rent. So far this year, there were 6% fewer homes available to rent in Great Britain than the same period last year. However, in London stock levels were down 21%.

> *It seems that uncertainty, affordability and the effects of various tax changes are hitting the rental market too.*

In fact, since April 2016 landlords have sold over 110,000 more homes than they've bought, with over 21,000 of those sold in London. But despite

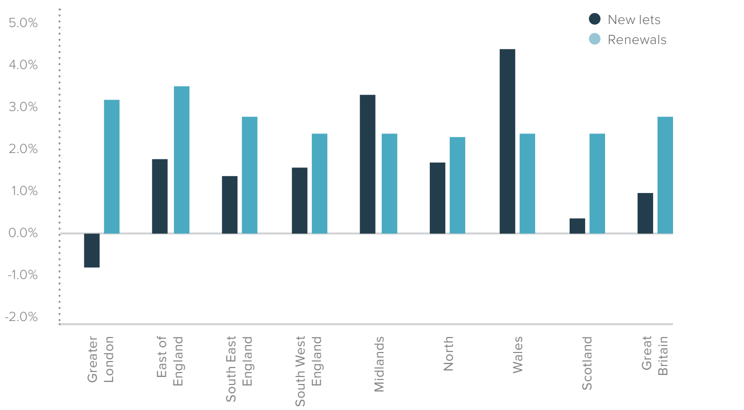
New Let rental growth compared with renewed tenancies rental growth (Aug 2018) Source: Hamptons International

1.0%

New Let Rental Growth

2.8%

Renewals Rental Growth



low stock levels, rental growth is still sluggish, so what's happening?

The average rent on a newly let property (i.e. a home advertised on the open market to let) stands at 1.0% in Great Britain. But in London, rents have fallen for the last three consecutive months, down -0.8% year-on-year in August. London remains the only region in the country where rents are falling, despite it being the worst affected region from the stamp duty surcharge because of its expensive property prices. Outside of the capital rents on new lets are still rising at 2.0%.

It seems that uncertainty, affordability and the effects of various tax changes are hitting the rental market too. This has resulted in a rise in the number of tenancies renewing. So far this year there were 2.5% more renewed tenancies than last year and this has meant that rental growth on renewed tenancies has risen 2.8%, the highest level in 10 months. This is particularly true in London.

> *London remains the only region in the country where rents are falling, despite it being the worst affected region from the stamp duty surcharge*

Renewal rents in London have risen for the last three months, reaching 3.2% year-on-year in August, despite rents on new lets in the capital falling. In fact, London has seen the second strongest renewals rental growth across the country.

Moving is costly for both tenants and landlords. In a period of uncertainty, with tenants' incomes and landlords' yields squeezed, more tenancies are being renewed instead. With affordability stretched and less choice available on the open-market, more tenants are choosing to stay put. And with landlord yields under pressure from high property prices and tax changes, fewer landlords want to run the risk of looking for a new tenant and suffering void periods.

Looking ahead, the shortage in lettings stock is unlikely to change anytime soon. August was the worst month on record for landlord purchases, with only 9.9% of homes being bought by an investor. But low stock levels, should support rental growth on new let properties in the future as incomes begin to pick up.

News let rents versus renewals

	Average New Lets Rent (pcm)	New Lets YoY Rental Growth	Renewals YoY Rental Growth
Greater London	£1,702	-0.8%	3.2%
Inner London	£2,609	0.4%	0.8%
Outer London	£1,530	-1.1%	4.0%
East of England	£957	1.8%	3.5%
South East England	£1,052	1.4%	2.8%
South West England	£807	1.6%	2.4%
Midlands	£689	3.3%	2.4%
North	£648	1.7%	2.3%
Wales	£683	4.4%	2.4%
Scotland	£658	0.4%	2.4%
Great Britain	£975	1.0%	2.8%
Great Britain (Excluding London)	£789	2.0%	2.6%

Source: Hamptons International

OUTMIGRATION

Londoners are on the move.

68%

of London Leavers purchased homes either in the South East or East of England.

In the first half of 2018, Londoners bought over 30,000 homes outside the capital; a 16% rise on the same period last year and 61% more than 10 years ago. In monetary terms this equates to £12.9 billion worth of homes – the highest level in four years.

While most London leavers head to the South East (38%) closely followed by the East of England (30%), an increasing proportion are moving further afield and setting up home in the North or Midlands. In the first half of 2018, one in five London leavers moved to the North or Midlands (21%), up from 6% a decade ago.

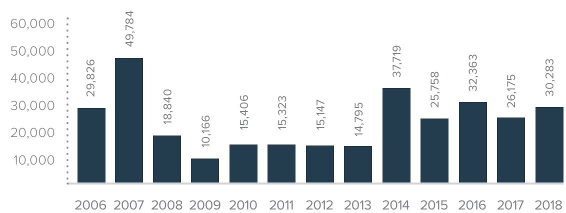
Quality of life, affordability and increased space remain the greatest drivers of these moves, but buyers are increasingly leapfrogging the more expensive areas of the South to buy a larger home sooner. By doing this they're able to future-proof additional costly moves while saving on stamp duty too. The average Londoner buying outside the capital spent £424,610 on their new home, more than 1.6 times more than a buyer from elsewhere.

London buyers are an important driver of local markets. Londoners bought more homes than existing residents in seven local authorities, most of which border Greater London. Broxbourne, Slough, Harlow, Thurrock, Brentwood, Dartford and Wokingham saw more homes bought by a London leaver than by a local resident this year. Other popular destinations further afield include Bath and North East Somerset where 42% of homes were bought by Londoners and East Dorset (25%).

However, not everyone is leaving the capital. In the first half of 2018, 31% of Londoners buying their first home moved out of the capital, but this represents a 2% fall on the same period last year. Stamp duty relief and Help to Buy have acted as a support to those first-time buyers wanting to stay and make London their home.

Number of homes bought by London leavers (H1 of each year)

Source: Hamptons International



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