

### UK Commercial Property

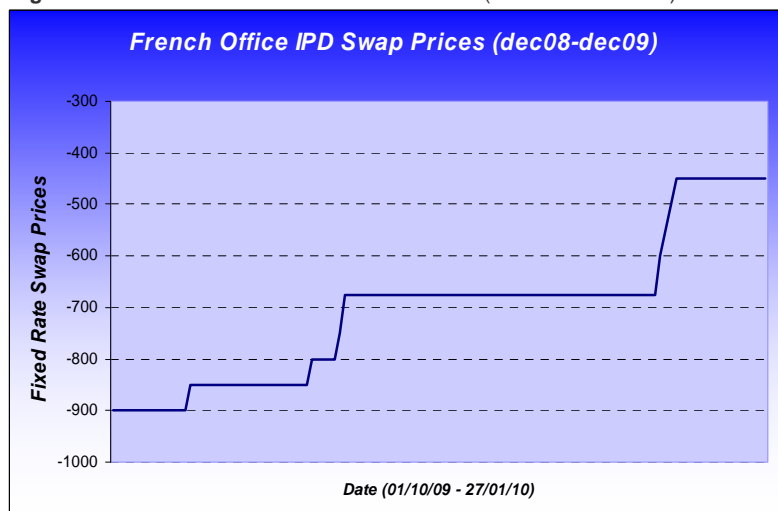
#### NEWSFLASH – Recession Ends. Time to Celebrate, but no ‘V’ for Victory.

- This week we received the long awaited news that Britain was finally out of the doldrums of recession. Early indicators from the Office of National Statistics suggest that the GDP soared like an (lame) eagle to post a positive growth figure in Q4 2009. Although the road to recovery will doubtless be potholed (and will definitely not be ‘V-shaped’), this below forecast figure of +0.1% is far better than say, -0.1%! So, before we concern ourselves with the effects of the latest inflation figures (CPI 2.9%), let’s savour this moment as we have just endured the longest post-war recession and come out the other side (for now)!
- Staying positive for the moment, this month the Royal institute of Chartered Surveyors declared that London office vacancy had decreased for the first time in two years, with rents having stabilised. Jones Lang La Salle currently quotes prime rents in the City and West End at £45sqft and £75sqft respectively, with prime yields at 5.75% and 4.75%.
- Savills boldly predict that 2010 will bring no ‘W-shape’ recession, in the London office market at least. They see rental increases in 2010, vacancy reduction and a “refurbishment and development boom” as London office space pipeline has been throttled. Estimated completions for the City in 2012 and the West End in 2011 each total 500,000sqft, well below long-term averages of 3.2m and 1.8m sqft respectively.
- According to IPD, the UK unlisted pooled property funds delivered total returns of 10.4% in Q4 2009, outperforming all other key property indices. Some of the top performers were Grosvenor, Standard Life and Aberdeen.
- Amongst this positivity lurks a sense of foreboding. The end of QE looms, interest rates can only increase, there will be post-election fiscal tightening and there’s the fear that GB PLC will slip back into the red. Commercial property occupancy markets are fragile, secondary investment markets are still weak and there exists the real threat of enforced sell-offs as yet more covenants are breached. The sector, after all, still owes £300bn to the credit market. So what shape will this recession be? We predict a ‘§-shape’!
- The property derivatives market was bolstered significantly this month with news that Britain’s largest real estate investment trust, Land Securities, is planning a move into derivative trading. It is believed to have approached two banks, including the Royal Bank of Scotland Group PLC (RBS), to set up their trading facilities. It will help the company balance its property portfolio and hedge its exposure to developments, in case property values fall again, as well as increase exposure to certain parts of the market.
- UK IPD swap prices have remained pretty static during the month. The dec09 contract unsurprisingly, is stuck at 200 mid, whilst the dec10, dec11 and dec12 contracts increased minimally by 15bps each. The biggest mover this month was in the French Office market, where the dec 09 contract shifted 200bps from -6.75% at the end of December to the current mid of -4.75% mid. Rather like the UK, French office swap prices have rallied strongly since September. See fig.2.

Contract Dec08	Mid Price (bps)
Dec 09 / 1y	200
Dec 10 / 2y	590
Dec 11 / 3y	625
Dec 12 / 4y	640
Dec 13 / 5y	650

Figure 1. UK IPD All property Swap Prices (27/01/10). Tullett Prebon.

Figure 2 French Office IPD Dec09 Contract Price (01/10/09- 27/01/10)



## UK Residential Property

### Sentiment survey shows significant swing. Halifax House Prices Post Positive 2009.

- Rightmove, the UK's largest property search engine, in their sentiment survey for 2010 revealed that 53% of the 33,000 consumers surveyed, predicted that house prices in the UK will rise during the year. This compares with a mere 10% at the beginning of 2009. This is in the face of negative news surrounding tax rises, spending cuts and rate hikes. Historically, positive sentiment has played a major roll in housing market recovery and has been a strong indicator of how prices might perform.
- Four of the UK's largest house builders are back in good shape. Taylor Wimpey have seen a 28% increase in sales and have been able to reduce debt by 50%, compared to January 2009. Bovis Homes have restructured their debt in order to make multiple development site acquisitions during Q1. Persimmon have reduced their debt by £600m and have acquired, or have under offer, £270m of sites currently and have seen their share price double from early 2009. Barratt Homes saw sales volumes up 43% in Q4, coupled with price rises of 4% in the same period.
- The Council of Mortgage Lenders announced that gross lending went mortgage lending reached an estimated £13.7 billion in December, a 14% rise from £12.1 billion in November and up 3% on December 2008. However, other than in 2008, this is still the lowest figure for December since 2001 (£13.4 billion). This unexpectedly high figure for December could be due to bunched completions resulting from individuals looking to best the end of the stamp duty holiday. In which case, we could feasibly see a reduction in loans agreed in the early part of 2010.
- The Halifax House Price Index posted the sixth successive month of house price rises. Dec 09 saw rises of 1.1% (seasonally adjusted), 0.99% (non-seasonal) and annual figure for 2009 of 5.56% (non-seasonal). The accompanying statement read, "The significant cut in interest rates has markedly reduced mortgage burden. This has helped to stimulate housing demand, albeit from a low base, as has an improvement in the labour market." Overall, their current view is that house prices will be flat during 2010.
- Since the release of the Halifax HPI figure in the first week of the year, and once market participants had rebased, derivative pricing has remained flat. Most traders' view for 2010 is for the market to remain flat, with any potential H1 gains to be chipped into during post-election H2. As such, the derivative price for the 1y contract (now 2009 start) is currently at 102 mid. There have been markets made in the Greater London index this month, suggesting that the residential derivatives market is to develop in the same way as UK IPD, as fund-managers require more a more specific tool to manage risk and gain exposure.
- At this point, as home owners groan at the thought of a flat year at best, let us again take stock, and analyse from where we have come. At the end of January 2009, the derivatives market was predicting implied values for 2010 of -16% (Tullett Prebon)! 0.1% GDP growth, a flat housing market - Great news! Come on, have we forgotten how to celebrate?

**Fig 3.** HPI forward contract prices and implied annual capital growth, 28/01/10. (Source Tullett Prebon)

Contract Dec09-	Fixed Rate Price (mid)	Annual Capital Growth (%)
Dec 10 / 1y	102	2.0
Dec 11 / 2y	103	1.50
Dec 12 / 3y	105	1.66
Dec 13 / 4y	107	1.75
Dec 14 / 5y	110	2.0
Dec 16 / 7y	114	2.0
Dec 19 / 10y	124	2.40

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