

research

from Hurford Salvi Carr

MIDTOWN, CITY AND DOCKLANDS
RESIDENTIAL REVIEW 1ST HALF 2008

Hurford Salvi Carr is an innovative firm of property advisors and development consultants who have become synonymous with urban living in central London. Our experience and expertise in both the residential and commercial markets, in the City, West End, Docklands and East London puts us at the forefront of property agency.

Since 1996 Hurford Salvi Carr has been a driving force of the 'city living' phenomenon having sold more than 3,000 new homes in over 175 developments, the majority created from former commercial premises, and we have played a pivotal role in the repopulation of Clerkenwell and the City fringes.

As real estate agents we are widely respected throughout London and are well known in property circles around the world. Our reputation is based on the accuracy of our advice, the quality of our marketing, and most importantly for achieving results.

The Company is divided into six divisions, specialising in Residential Sales, New Homes, Residential Lettings, Residential Investment, Commercial Agency, and Property Management. In many instances the skills of each division combine to provide our clients with best advice. Our fresh approach and award winning marketing expertise complements our service.

We are committed to providing a personal service to each of our clients and we maintain the highest standards in every aspect of our business.

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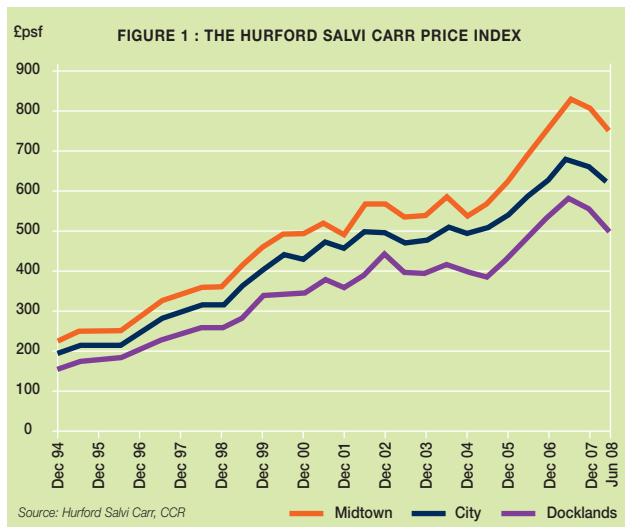
market overview

UK BANKS TRIGGER PRICE FALLS

The first half of 2008 was a difficult time for the London residential property market. The banking liquidity crisis led to the loss of 60% of new enquiries in the sales market, compared with the first half of 2007, and resulted in a downturn in transactions that was exacerbated by reports of consumer confidence hitting the lowest point since 1990.

With fewer enquiries vendors, including some developers, increasingly looked to the rental sector as part of a longer term strategy, rather than sell in a buyers' market. The private rental sector has provided a lifeline, unlike the last two major property corrections in the early 1970s and 1990s, when the rental market was not established as a viable alternative.

UK banks and building societies deserted the mainstream mortgage market as they came to terms with the consequences of their reckless lending policies of the past decade. The number of mortgage products available to borrowers sank from 28,400 in June 2007 to just 5,340 in June 2008, a reduction of over 80% (Source: moneysupermarket.com). As a result prices fell across the whole country, including London. In Midtown, City and Docklands prices fell by an average of 9% in the first six months of 2008 (Figure 1), a higher rate of loss than the 5% we predicted in our end of year report in December 2007.



- Secondary effects of the housing market downturn spread into the DIY stores sectors, furniture manufacturers and retailers, which are heavily dependent on business generated by house moves and re-mortgaging.
- On 2nd June Bradford & Bingley was forced to renegotiate the terms of its £300 million rights issue in the light of a surprise £8 million loss in the four months to April 2008 as a result of the housing market slowdown (especially in the buy-to-let sector where the bank was overweight) and the soaring cost of borrowing on the wholesale markets.

In this context, two further cuts in the Bank of England's base rate from 5.5% to 5% during the first half of 2008, as predicted in our 2007 year end report, had little impact on the mortgage market, where the UK banks typically responded by increasing their mortgage rates and lowering their loan to value ratios in response to wider commercial factors. A deeper cut in the base rate was hampered by the need for the Bank of England to maintain inflation

within the Government's target range, in spite of fears that the effect of the credit squeeze would spread from the financial markets to the wider economy.

The impact of the UK banks' lending policies on the housing market was a dramatic reduction in the volume of transactions resulting in price falls across the UK over the first half according to both the Nationwide and Halifax indices. At the end of May 2008, the Nationwide announced a monthly fall in UK house prices of 2.5%, the seventh consecutive monthly decline and the biggest monthly loss in the index's history. It also took the annual price fall to 4.4%. The Halifax House Price Index also recorded a 2.4% fall in May.

It was highly unusual for the national picture to be so in tune with market conditions in London. The convergence between the banks, however, to offer the least competitive products, in case they were inundated with mortgage applications, was not location specific. In short, the UK was in the grip of a "feel-bad" factor.

sales market

CASH IS KING

After a quiet final quarter to 2007, potential buyers returned to the Midtown, City and Docklands market in January and February 2008 in sufficient numbers to stabilise prices. The market was admittedly slow and the number of serious enquiries was less than normal, but sales were agreed. On 7th February, the Bank of England made a quarter point cut in the base rate to 5.5%, following its first reduction in this cycle of 25 basis points in December 2007. This cut, however, had no impact on the mortgage market, which remained illiquid.

Due to the vagaries of the lunar cycle, Good Friday fell on 21st March, creating a very early Easter. For many families this was a mere long weekend, to be followed in early April by the end of the school term. This extended period of holidays seems to have contributed to a further weakening of the market in London, at a time when it normally enjoys a spring boost. At a point when it seemed that banks were weathering the storm, on 17th March 2008 Bear Stearns collapsed in New York, precipitating a rescue by JP Morgan supported by regulatory authorities.

A further quarter point cut in the base rate to 5% by the Monetary Policy Committee on 10th April (a rate maintained in May and June) had no positive effect on the sales market whatsoever. In the wake of Bear Stearns and the continuing difficulties in the banking sector, rates and terms in the mortgage markets became more, not less onerous after the base rate fell. With banks struggling to access wholesale markets, the cost of more expensive funding was being passed on to customers in the form of higher rates and agreement fees. Buyers with lower deposits were paying a premium and competitive products were withdrawn to prevent lenders from being swamped with enquiries. In effect, higher interest rates were being used as a deterrent. Banks also became much more stringent, with less emphasis on the speed of the transaction and more on due diligence. This caused serious backlogs and delays resulting in a high failure rate, as while solicitors waited for underwriters to approve loans, buyers literally changed their minds.

The response on 21st April 2008 was the Bank of England's "Special Liquidity Scheme", where the Bank offered to swap difficult to sell mortgage-backed assets for Treasury bills. High quality AAA-rated mortgage backed securities that were already in place at the end of 2007 could be exchanged for Treasury bills for a one year period,



WENLOCK BUILDING, N1 - THREE BEDROOM APARTMENT SOLD JUNE 2008 £1.34 MILLION



LIMEHOUSE, E14 - THREE BEDROOM APARTMENT SOLD FEBRUARY 2008 £690,000

renewable for three years. The scheme has been taken up, but by the end of June 2008, lenders were still struggling to access funding and mortgage rates were still rising. An appreciable easing of credit terms is unlikely to occur before 2009.

The spring market would normally have led to an increase in enquiries and transactions, but this failed to materialise and enquiries were dramatically down by 60%. With fewer viewings, sellers either withdrew from the market (many transferring to the rental market) or dropped their prices. By May and June, buyers had the opportunity of better choice and were able to negotiate discounts off already reduced asking prices. Even where sales were agreed, they did not always progress to completion, either because solicitors were not happy to exchange contracts until every piece of information was in place in order to satisfy the banks, or because buyers that had negotiated a lower price pulled out, taking the view that price falls had further to go. As a result prices fell rapidly from the start of March to the end of June, typically down in the region of 9% on the end of 2007.

For our illustrated one bedroom flat this reduction has taken the price from around £370,000 to £340,000 in the first half of 2008, reducing Midtown, City and Docklands prices to the level seen at the end of 2006, effectively wiping out the gains made in the first nine months of 2007 (Table 1). As the acceptance of further price falls became widespread across the market, and mortgage providers in any case reluctant to loan, buyers adopted a "wait-and-see" attitude, which was still apparent at the end of June.

In the midst of gloom, some property types in Midtown, City and Docklands have fared better than others. The top end of the market, for penthouses and larger units with good outside space, has been maintained by the proportion of buyers with high equity stakes. The market for studios and one bedroom units has been supported by the pied-a-terre market and parents buying for children at university. Mid-range two bedroom apartments have seen the greatest fall in prices due to the over-supply on offer in the marketplace.

The sales market has been broadly supported by the proportion of buyers with high equity stakes and hence lower borrowing requirements. The majority of purchasers who bought through our agency in the first half of 2008 had a minimum of a 60% cash deposit and many purchased with 100% cash, and hence were not overly dependent on mortgage finance. It can be reasonably assumed that the 60% of enquiries that evaporated from the market were from buyers requiring 80%-95% mortgage finance. We were not surprised to learn that private banks such as Coutts are reported to have completed 30% more mortgage lending in the first half of 2008, given their clients' financial position.

TABLE 1: ILLUSTRATED PRICE CHANGES FOR ONE-BEDROOM FLAT 1998-2008 IN MIDTOWN, CITY AND DOCKLANDS

Year End	Price Change %	One bedroom Illustration	
		Market Value (£)	Change in Value (£)
1998	N/A	150,000	N/A
1999	+26%	189,000	+39,000
2000	+11%	210,000	+21,000
2001	+10%	230,000	+20,000
2002	+13%	260,000	+30,000
2003	-6%	245,000	-15,000
2004	+0.4%	246,000	+1,000
2005	+10%	270,000	+24,000
2006	+26%	340,000	+70,000
2007	+9%	371,000	+31,000
2008 1st Half	-9%	338,000	-33,000

Source: Hurford Salvi Carr, OCR

There was a geographical dimension to price changes across the market with a gradient from west to east, with lower rates of price falls in the west, while lower demand in Docklands led to higher rates of reduction in the east (Table 2). The pricing gradient reflected both supply and demand factors. The supply of homes for sale in areas such as Bloomsbury, Covent Garden and Marylebone was not extensive; there was a limited pipeline of new homes and less dependency on demand from the financial sector. Reduced demand, however, led prices to fall in the order of 6%.

TABLE 2: PRICES FOR TYPICAL ONE-BEDROOM FLATS (500 SQ FT) FIRST HALF 2008

Sub-Market	December 2007	June 2008	Reduction (%)
Bloomsbury (WC1)	£420,000	£395,000	-£25,000 (-6%)
City (EC)	£395,000	£365,000	-£30,000 (-7%)
Docklands (E14)	£340,000	£302,500	-£37,500 (-11%)

Source: Hurford Salvi Carr

In the City, although supply was higher and the demand side more dependent on confidence and employment prospects, there was still a reasonable supply of cash-rich buyers. Exceptional homes and attractive loft-style apartments continue to sell, but prices fell by 7% in the first half of 2008.

In Docklands, the imbalance between supply and demand was magnified by very high dependency on banking and finance jobs at Canary Wharf and an over-supply of very similar types of units in large blocks derived from the buy-to-let sector. As a result, Docklands prices fell sharply by 11% during the first half of 2008.

To put these falls into context, prices in Midtown, City and Docklands rose by 10% in 2005, 26% in 2006 and 9% in 2007 – a compound increase of 51% over three years. Average prices in June 2008, therefore, have fallen back to the level last seen 18 months earlier in January 2007.



CLERKENWELL GREEN, EC1 - PENTHOUSE SOLD MAY 2008 £1.5 MILLION

new homes market

OFF-PLAN LAUNCHES POSTPONED

Almost without exception developers responded to the new reality of the market by altering their marketing strategies in the first half of 2008. Evidence of prices falling across the Midtown, City and Docklands market deterred investment buyers, many of whom took the view that they were better off waiting until house prices stabilise at a new level before committing to purchase. In any case, even willing buyers had greater difficulty raising the necessary loan finance than in the past. This was particularly true for investors, especially in the buy-to-let market, to whom around two thirds of new homes were being sold prior to the credit squeeze and who have now disappeared from the market (see Investment Market, page 6).

Developers in Midtown, City and Docklands accepted in the first half of 2008 that off-plan volume sales were no longer viable in the current market and that they would instead target owner-occupiers. This inevitably led to scheme launches being put back until practical completion, when apartments could be seen and appreciated. In effect, therefore, the level of prices in the new homes market remained largely untested in the first half of 2008. We expect to see a number of significant launches from September 2008 onwards, which will provide important evidence on demand and pricing for new homes and the wider market. Our own view is that average prices for new homes are between £800-900psf in Midtown and the City and £500-700psf in Docklands (E14).

Bézier, a 17 storey development of 126 private apartments by Tudorvale on the south east corner of Old Street roundabout, was launched in March 2008 with a marketing suite in Leonard Street, EC2, with an anticipated completion date of 2010. In May 2008 a decision was made to close the marketing suite, even in a market with little competition from other major schemes, with the notable exception of Berkeley's City Quarter, Leman Street, E1. Bézier is an innovative residential development that will attract serious interest from Shoreditch, Clerkenwell and City buyers when it is complete, so it is a sensible strategy to concentrate the marketing spend when market conditions are more favourable.

There is also some limited evidence of schemes not yet started being "mothballed" until market conditions improve. In May 2008, for example, Grainger announced that it had frozen its housing development pipeline in London in response to the market slowdown.

In these conditions, "boutique" developments in established locations are likely to fare better than larger, anonymous blocks in pioneering regeneration areas. Hurford Salvi Carr is acting agent on a number of such schemes in the City and City Fringes, where lists of potential purchasers remain encouraging.

Bowling Green Lane, EC1 – A new three storey mixed-use building on the corner of Bowling Green Lane and Clerkenwell Close with 13 apartments on the 1st and 2nd floors above offices on ground and basement. The development by Marldon is due for completion in November 2008.

44 Hatton Garden, EC1 – A now rare office to residential conversion in Hatton Garden, on the corner with St Cross Street. The former Kinetic House, with its art deco facade, is being converted to 10 apartments with completion due by the end of 2008.

84 Fetter Lane, EC4 – A niche residential development on the west side of Fetter Lane, south of High Holborn, converted from

offices, comprises studios, one bedroom flats and a two bedroom penthouse on 4th and 5th, set for completion in August 2008.

Chamber Street, E1 – This is a new nine unit "build-to-let" development of one and two bedroom apartments close to Tower Hill, where gpad architects has again come up with an innovative response to an urban setting. The scheme includes a 1,746 sq ft three bedroom duplex penthouse and is due for completion in September 2008.

The Wenlock Building, Wharf Road, N1 – The second phase launch by developers London & Newcastle and United House of 15 apartments and penthouses in an 55 unit scheme, will officially begin in October 2008. Sales have successfully continued quietly off-plan during summer 2008, at prices in excess of £900 psf, proving that quality is selling.

43-47 Vallance Road, E1 – A new development of 14 one and two bedroom units in Whitechapel, priced from £265,000 with an average price of £550 psf, due for completion in October 2008.

Leo Yard, EC1 – A twelve unit scheme of air-conditioned apartments with roof terraces on the 4th and 5th floors of a new office building on the south side of Great Sutton Street, being developed by Bee Bee Developments for the rental market and due for completion in September 2008.

There has been an inevitable knock-on effect on the land market, with a significant downturn in the bidding for residential development land and buildings by private developers. If the finance is available, developers are only prepared to buy at significant discounts, but vendors to date have been reluctant to sell. A much lower level of transactions for development land, combined with "ready to go" schemes with planning permission being put on hold, will reduce the rate of new homes completions in the medium-term. This should have a beneficial effect on the supply and demand balance in 2010-2011.

In the meantime, the major UK housebuilders announced significant job cuts, with the largest, Taylor Wimpey, closing 13 offices and making 600 staff redundant in May 2008, followed closely by Persimmon which announced "several hundred" job losses in June. Share prices of housebuilders had typically fallen by 60% in a year as a result of the credit squeeze.

One new factor for the new homes market is the election of Boris Johnson as Mayor of London in May 2008, replacing Ken Livingstone after eight years. Although the new planning policies to be followed by Mayor Johnson were far from clear during the election campaign, it seems likely that requirements for affordable housing will be eased in some cases. Individual boroughs, however, will continue to be the main drivers of affordable housing policy and variations between boroughs will remain. There was already evidence in May and June 2008 of developers submitting revised applications with lower proportions of affordable housing. Less stringent affordable housing requirements should enhance the viability of development in the tough market conditions which lie ahead.

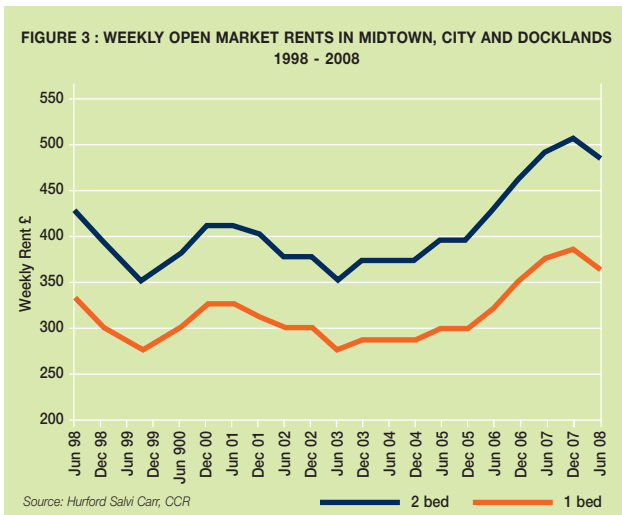
Over the past two years we have advised Housing Associations at competitive tender stage in a number of mixed private/affordable projects. This sector is likely to be increasingly significant in the future, given the availability of funding for Housing Associations which strengthens their buying power in the land market.

rental market

LOWER RENTS REFLECT INCREASED SUPPLY

Conditions in the sales market, where potential buyers either withdrew from the market or delayed purchases due to difficulty raising mortgage finance, had a beneficial effect on demand in the rental market in the first half of 2008. The volume of letting transactions across our Midtown, City and Docklands offices was up 6% compared to the first half of 2007. The weakening in the sales market also had the effect of increasing the stock of rental property, as potential sellers became landlords and the supply of homes to rent grew. Increased supply raised the level of availability in the lettings market by 25% during the first half of 2008.

With availability expanding at a faster rate than the growing demand for lettings, the effect was to bring down the level of market rents. Following an increase in rents in the second half of 2007 of 3%, rent levels fell by around 4% in the first half of 2008 (Figure 3). This is the first time rents have fallen in Midtown, City and Docklands since June 2003.



There was no diminution in demand from private tenants, but the corporate lettings market was hit by the slowdown in recruitment and activity in the City employment market. There were some signs of improved activity in the corporate market in June 2008, which gives some confidence that the traditionally strong summer market in this sector will materialise.



WESTLAND PLACE, N1 - 11 APARTMENTS LET MARCH 2008

At the same time, the supply of rental property continued to increase, especially in Docklands where major new-build blocks that had mainly been sold to investors continued to flow into the rental market. Supply has also been enhanced by developers who have in some cases been forced to alter their strategies from “build-to-sell” to “build-to-let”. They take a view that rather than drip-feed sales into a falling market, it is better to put units on the rental market for between two to five years until both sales volumes and prices recover. At this point the units can be refreshed and launched on the sales market.

Whereas in early 2007 rental properties were quickly re-let, voids gradually increased in the first half of 2008. In Midtown and the City these periods remained fairly short at around 2 weeks, but in Docklands and East London void periods moved out significantly to 4-6 weeks. That said, renewal rates for rental property across Midtown, City and Docklands remain high.

In a competitive market, landlords have to be seen to be offering value for money for tenants as much as in the sales market. In March 2008, Hurford Salvi Carr let 11 apartments in the space of three weeks at a new development in Westland Place, N1, next door to Jamie Oliver’s restaurant “Fifteen”. All were let to individuals rather than companies, at negotiable rents and with attractive furniture packages. In the same month we let seven apartments in Bow Quarter, the former Bryant & May match factory in Bow, where tenants were also attracted by value for money, with rents for one bedroom apartments typically under £250 per week.

Inevitably, some renters are keeping a close eye on the sales market, with a view to entering the market when they consider that prices are at or close to the bottom of the current cycle. Given the state of the mortgage market, however, there will be more hurdles to overcome than in the past in successfully converting to a first-time buyer. We do not see the prospect of a significant shift from renting to owning until well into 2009, when mortgage markets should be more liquid and prices are likely to offer a more attractive proposition.

The prospects for the rental market look more positive for the second half of 2008. Late summer/early autumn is the traditional peak period of demand for rental property, with a combination of new recruitment, corporate letting and the annual influx of UK and overseas students. In our view, there will be a recovery in rent levels in the second half of 2008 of around the same proportion lost in the first half, leaving rents unchanged over the year.



BLOOMSBURY SQUARE, WC1 - 13 APARTMENTS LET SPRING 2008

investment market

BANKS CEASE TO SUPPLY INVESTORS

Residential investment in Midtown, City and Docklands ground to a halt in the first half of 2008. Two reductions in the base rate from 5.5% to 5%, which would normally have helped to stimulate investment, had no effect as stated earlier. Lending institutions altered their lending terms and policies and withdrew funds from the buy-to-let sector, effectively excluding many investors from the market. In June 2007 investors had a choice of 4,300 buy-to-let mortgage products, but in June 2008 the number was just 441, a reduction of 90%. Lenders that have remained open for business have increased interest rates, demand punitive arrangement fees and higher rental coverage, making it almost impossible for new investors to become landlords.

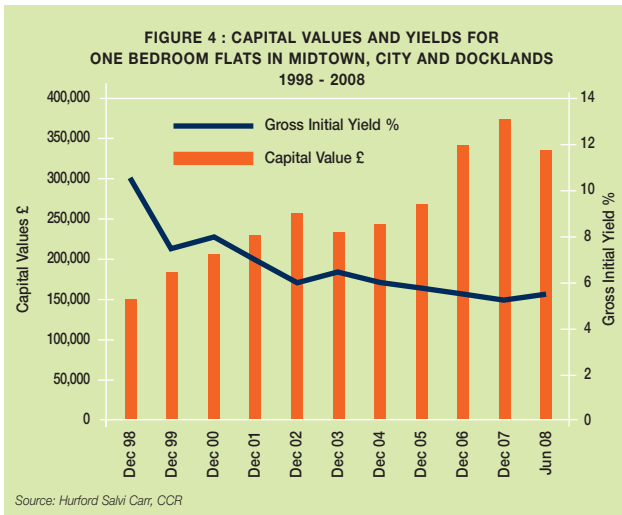
The impact of changes in values and rents can be seen in Figure 4 and Table 3, which plot capital values and residential investment yields in Midtown, City and Docklands. The 9% fall in capital values and 4% reduction in rents combined to produce a modest increase in gross initial yields from 5.4% to 5.7%. Investors are unlikely to be enticed back into the market in the short term given the expectation of falling prices, but even if they are, loan terms are so onerous as to form a barrier to participation in the market. Established investors tell us they will be returning to the market to add to their residential portfolios, but have moved their yield expectations out to 7-8%, given the prospect of the Bank of England raising the base rate above 5%.

Investors who purchased at the peak of the market between mid-2006 and mid-2007 are at some risk of negative equity. Most investors in the City and Docklands market, however, are in for the long-term and we have not yet seen any evidence of distressed sellers, although that may change over the next twelve months. Rental income continues to underpin the market, even if values have fallen.

More serious is the issue of the potential for investors who bought off-plan prior to the emergence of the credit squeeze being unable to complete their purchases. With loan to value ratios moving against them, some buy-to-let investors will be unable to complete and will be forced to drop their deposits. Developers will then have to decide whether to offer the units in the sales market or retain them as rental investments for the time being.

We understand from our own purchasers, that their 85% buy-to-let mortgage offers have been withdrawn and the best alternative being proposed by the lender is a 60% buy-to-let loan. We expect banks to suffer the consequences of restricted lending, which could lead to a higher number of repossessions in the next two years. This, in turn, could ultimately contribute to losses in the banking sector.

At the end of April came the news that Inside Track, the buy-to-let investment seminar operator, had gone into administration. Buying clubs which offered the novice investor the dream of making a fortune from the property market, played an important role in the off-plan sales market in London between 2003 and 2007, but it now looks likely that this new sector of the market will disappear as quickly as it arrived.



CLERKENWELL ROAD, EC1 - DEVELOPMENT OPPORTUNITY SOLD APRIL 2008 £3 MILLION

TABLE 3: ILLUSTRATED INITIAL YIELDS FOR ONE BEDROOM FLAT IN MIDTOWN, CITY AND DOCKLANDS 1998 TO 2008

	Dec 1998	Dec 1999	Dec 2000	Dec 2001	Dec 2002	Dec 2003	Dec 2004	Dec 2005	Dec 2006	Dec 2007	June 2008
Gross Annual Income £	15,600	14,300	16,900	16,120	15,600	14,820	14,820	15,340	18,200	20,020	19,220
Capital Value £	150,000	189,000	210,000	230,000	260,000	245,000	246,000	270,000	340,000	371,000	338,000
Gross Initial Yield %	10.4	7.6	8.0	7.0	6.0	6.0	6.0	5.7	5.4	5.4	5.7

Note : gross yields are typically reduced by 2.5% points by costs and voids

Source: Hurford Salvi Carr, CCR

market prospects

FORECASTS FOR 2008

The Sales Market

We know from the very high number of unique visitors to our website each day that Londoners have not lost interest in residential property. With the number of actual new enquiries at our offices down by 60% year-on-year in the first half of 2008, confidence in buying a home at this time has evaporated.

The current downturn in prices in Midtown, City and Docklands is, we consider, different in nature to previous episodes of volatility in the market, when prices recovered rapidly after a 10% fall, because the life-blood of the market, mortgage finance, has ceased to circulate.

Until the effects of the credit squeeze work their way through the banking system, there is no incentive for banks and building societies to undertake anything other than the least risky lending. This in a housing market where price rises had been fuelled over the past five years by ever-easier lending criteria by the self-same lenders. In any case, we do not expect to see lending institutions competing strongly in the market until they see evidence of a substantial reduction in prices at the national level. In effect, there is a danger of creating a self-fulfilling prophecy. For many of our clients under the age of 35, this is the first time they have experienced a serious economic downturn that has led to a significant adjustment in residential property prices.

In Midtown, City and Docklands we had already reported price reductions starting earlier than in the national market in October 2007. Independent of the market, banks and other lending institutions will not lend freely again until the overall financial system has recovered and confidence is restored.

External factors suggest that recovery will come later rather than sooner.

- On 5th June the European Central Bank gave a signal that it could increase its main interest rate by a quarter point at its July meeting, in order to keep a lid on inflation caused by high oil and food prices.
- On 17th June the Governor of The Bank of England predicted that inflation would rise to more than 4% before the end of 2008. That announcement caused many City analysts to re-evaluate the short-term future for the UK base rate, with possible rate rises before the end of 2008.
- Job losses across London look increasingly likely in a variety of sectors – not just banking and finance with direct exposure to the global credit squeeze.
- In the political arena, the leadership of Gordon Brown is in question. The man who as Chancellor was seen as prudent and a “safe pair of hands” for the economy, knows he now has to prove himself as Prime Minister.

The likelihood that mortgage finance is going to be difficult to obtain for at least another year, if not longer, would seem to support the prognosis that prices do have further to fall before stabilising at a new level. As a result, we are forecasting a further reduction in sales prices in Midtown, City and Docklands in the second half of 2008 at a slower rate of decline of 5%, making an annual reduction of 14%. This implies a total cyclical reduction in values over the 15 months

from September 2007 to December 2008 of 17%, almost one-fifth. Bear in mind, however, that this reduction in values masks a range of falls from west to east, where the potential reduction in prices over 15 months is 14% in Midtown, 15% in the City and 19% in Docklands. We believe that this would support the level of correction that economists anticipate would be required before we can get back to a “normal” market.

Looking further ahead, we consider that three interrelated key factors could converge to kick-start the sales market. First, asking prices will fall to a level that attracts tenants to make the switch from renting to buying a new home, with two to three years potential demand from renters converging. Second, banks will, we hope, decide that they can lend again and become more realistic in their lending criteria. Third, the “feel-bad” factor that swept across the UK like a tornado in the first six months of 2008 will calm down and the outlook for the economy will show signs of improvement.

We lay the blame for the current problems in the housing market firmly at the door of the UK banks, but equally it is the banks that hold the keys to generating a recovery from the current uncomfortable position. Quite simply there is pent up demand to buy residential property in central London. If the banks do not recognise the opportunity that exists to generate profits for their own shareholders by offering competitive mortgage products, then they will leave the door open to new entrants to come in and fill the void and take market share.

The Rental Market

The central London rental market is highly seasonal, with a very pronounced peak in demand between July and October each year. As we saw in Figure 2, the upturn in demand for rental property actually began in May this year based on the interplay of factors between the sales and lettings markets. A proportion of the demand for rental property is coming from frustrated buyers. In normal circumstances they would be able to secure a mortgage, but in this exceptional funding environment, that is less of an option.

At the same time, there is likely to be a further increase in the stock of rental property in second half of 2008 from newly completed units entering the letting market, including a proportion that had previously been destined for owner-occupation. On balance, we consider that the seasonal uplift in demand for renting, augmented by frustrated buyers, will be sufficient to absorb the additional supply coming on to the lettings market. Indeed, we consider that demand will be sufficient to reverse the reduction in rents of 4% seen in the first half of 2008, leaving rents unchanged during 2008.

Although the latest output growth and employment data indicates that London continued to outperform the UK in the first half of 2008, the outlook for the London economy and employment is the worst since the early 1990s. According to GLA Economics’ May bulletin “London’s Economy Today”, the credit crunch means London is likely to grow below trend for the next few years. A slow down in the service sector is likely to lead to lower rates of recruitment in central London businesses, with a knock-on effect on demand for rental accommodation. With the supply of rental property set to continue to increase in the short to medium term, there is unlikely to be a return to rental growth in 2009.

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**HOLBORN, WC1 - 4 UPPER FLOORS SOLD WITH CONSENT FOR A SINGLE HOME
JUNE 2008 £1.25 MILLION**

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