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Is there really a property bubble?

It's the question everyone wants answered: is there a residential property bubble? If so, when will it all end and how bad will it be? If not, then how come everything I'd quite like to buy is too expensive?

These may be the questions needing an answer in London and highly specific parts of the Home Counties, but elsewhere in the UK there is no suggestion of a bubble, and property prices virtually everywhere outside this area continue to stagnate, with little sign of recovery. If there is a bubble, then it only truly exists in London.

Before we look more closely at the bubble question, let's consider what constitutes a bubble. Typically, it is when all common sense is lost, and people buy things, not for their intrinsic value, but simply with a view to selling it later at a higher price – the greater fool theory. This happened in the South Sea Bubble in 1720, the tulip mania in 1637, and the rather more recent dot.com bubble in 2000.

Is there any sign of this happening in the property market? Not in our view: the entry cost for properties in excess of £2m is a 7% stamp duty, plus likely estate agent buying and selling costs, and there is simply no evidence in London that buyers are seeking to make a quick buck. Quite the reverse, in fact. London property is increasingly seen, as suggested by the New York Times, as a sort of global reserve currency. In 2012 some £83bn worth of property was bought with no financing at all! Buyers are buying because prime property is seen as a store of value at a time when inflation is probably just around the corner, cash deposit accounts are a disaster, and not everyone wants all their money in the stockmarket. It helps that London is a simply amazing city to live in, which is why so many foreigners are buying.

This is all very well at the top end of the market, but it makes for a very tough environment for first time buyers. Entry level homes used to cost about 3.5x salaries. This figure is now closer to 5x or even 6x salaries. However, this fails to recognise that the actual cost of ownership has fallen dramatically. Mortgages in the 70s and 80s chewed up a huge proportion of net income, but now, mortgage servicing as a proportion of net income is well below its long term average. Finding a lump sum to get on the ladder remains a big hurdle, but increasingly this is where the so-called Bank of Mum & Dad step in.

So, will it end any time soon? Maybe, maybe not: if London remains the city of choice for foreigners seeking a safe haven for their capital, prices will probably rise even further. But if the landscape changes, perhaps after a general election, the imposition of mansion taxes and eventual higher interest rates could prompt a return to a less exuberant residential property market. Time will tell.



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