Market Commentary

Residential Analysts

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United Kingdom – September 2020

- **What Happens Next?**
- **The Politics of Planning**
- **First Time Buyers Crunched**

The housing market is booming, but how long can it last and will there be a crash? Last month we looked at what was driving the current housing boom. Now everyone is asking what happens next. The truth is no one knows given the widespread uncertainties. But you don't need to be a superforecaster to identify some of the important events coming up in the next six months and assess what they could mean for the housing market. This note looks at these and also at growing political challenges facing housing – namely planning and home-ownership.

What Happens Next?

The post-lockdown housing boom is continuing with rising house prices and record high activity levels. The big question is how long can the boom last and what happens next?

A Quick Recap

The current boom appears to be a mix of sales delayed by lockdown and a massive reassessment among buyers in the value of location versus space. While the first factor (delays) is significant, it will inevitable diminish in the months ahead, as they manage to buy or realise they can't. It is therefore the second factor that is more interesting to consider. There is emerging evidence from Rightmove (pdf) that the south of England has seen the biggest bounce-back in sales agreed. Meanwhile Zoopla are reporting that wealthier demographics are driving sales and there is higher demand from home movers (pdf) than first time buyers. This suggests the current boom is being propelled by buyers for whom the biggest impact of the pandemic has been to make them realise they want a garden, home office or can work from home more regularly. And the stamp duty holiday has encouraged some of those who weren't fully convinced of moving.

The Next Three Months (Oct-Dec)

The delays in transactions being completed and data being published means the current boom will continue to the end of the year, at least in the stats. It is likely that the high levels of sales agreed over the summer months will feed through into completions and hence HMRC data from September to December. Meanwhile the same transactions will also support house prices. It is therefore possible, in the absence of a further housing market shutdown this year, that when I'm looking back at annual housing statistics in my retirement, the lockdown is barely visible other than in a footnote. While this may appear to just be a statistical point, it suggests the data releases and resulting housing market news stories over the next three months will continue to support positive sentiment amongst potential home buyers and so we'll see continued interest and activity.

The housing market may look set for positive news over the next three months. The economy does not. The furlough scheme is due to end on the 31st October and the replacement launched last week was underwhelming. It now seems clear that the pandemic will lead to permanent economic damage with lost jobs and lower income for large numbers of people, even if a vaccine appears. However, due to their lower age and income profile, the immediate impact of the economic fallout is more likely to fall on renters than owners. For home owners that do lose their jobs, mortgage lenders will be under considerable pressure (internally and externally) to avoid repossessions. Therefore, we're more likely to see falling rents than prices or sales over the next three months.

The Three Months After That (Jan-Mar)

The first three months of 2021 could be the best quarter for sellers and estate agents since 2007 and possibly even 1988. The end of a stamp duty holiday always leads to a spike in transactions as buyers rush to beat the deadline and this time will be no different unless the holiday is extended. There will also be a rush as newbuild home buyers complete before the Help-to-Buy equity loan scheme is limited to first time buyers and under regional price caps. We might even see a flurry of activity from overseas buyers as they aim to beat the introduction of the 2% surcharge. It could be a big party for anyone that earns a living linked to selling houses.

However, 2021 might also be the year when we finally find out what Brexit actually means and what impact it will have on our lives and the economy. It is increasingly clear that any benefits (if they exist) will be realised over the long term. However, the costs could be immediate and significant. Therefore it's still far from certain what impact Brexit will have on the housing market. This is yet another large uncertainty that makes predicting the future particularly difficult if not near impossible at the moment.

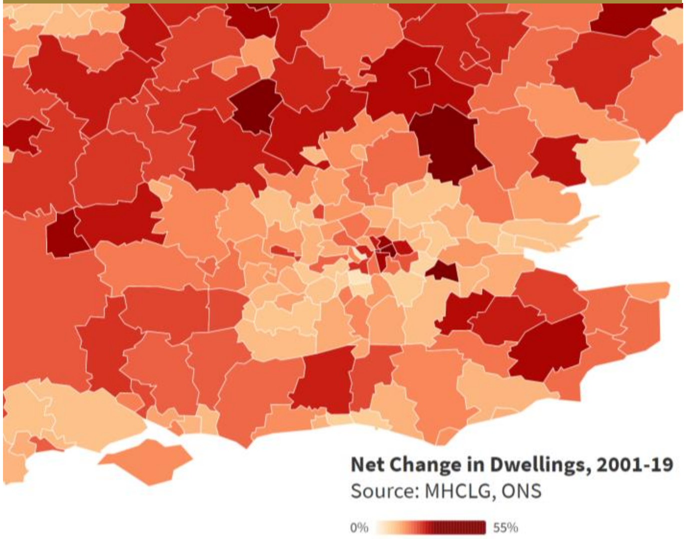
The Hangover? (April onwards)

If the stamp duty holiday does finish at the end of March then the following months could be dire for housing market activity. Any spike in transactions to beat a tax change consists of both truly additional buyers and buyers who would've bought in following months but chose to bring their purchase forward. As such, there is always a collapse in transactions when a tax comes to an end. This time will be no different. Turnover will be much lower in April and the months after. Unfortunately, low turnover increases the risk that a relatively low number of forced sales, whose impact might normally be contained, could have a bigger negative impact on the wider market.

Whether we will see large numbers of forced sales remains uncertain. Here, the approach of mortgage lenders will be key. As mentioned, they will be under considerably pressure to keep numbers down. However, even if they do, the housing market has changed significantly since previous recessions. There are large numbers of home owners and investors that sit outside the mainstream mortgage market, either because they own outright or they have used alternative financing. Even if mainstream lenders exhibit forbearance, these other parts of the market could be at risk from rising unemployment, falling incomes, and falling rents next year.

The coming months are peppered with uncertainties making it extremely tricky, if not unwise, to predict confidently what comes next for the housing market. There remains a large risk of a crash next year. We could see stagnation with low sales and static prices. Alternatively there might be a boom driven by home movers continuing to trade location for space or triggered by a Covid-19 vaccine. Whatever happens, there are clear political challenges facing government and housing.

Figure 1: Net Change in Homes, 2001-19
Source: MHCLG, ONS



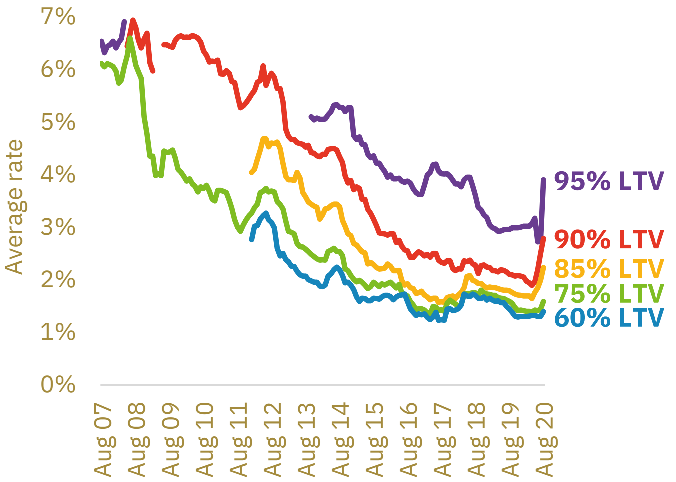
The Politics of Planning

The government's planning white paper has brought the politics of planning back into focus. Widespread references to the new standard method for calculating housing need as an algorithm may frustrate some, but reflect appropriate concerns over a one-size-fits all approach. Meanwhile, the political ramifications of shifting to a zonal system with everyone's home tagged in one of the three categories and easily visible online should not be brushed aside. The challenge for the government is highlighted by the map opposite showing the relative under-supply of new homes across the traditionally Conservative-voting Home Counties. In theory, the new standard method would go some way to correct for this (though still limited by green belt) but the political fallout is growing. Perhaps, given we're still figuring out the implications of the massive ongoing changes to how people live and work, now may be an appropriate time for some deeper strategic thinking and planning to establish what we want and need from housing and how best to deliver it.

First Time Buyers Crunched

Although planning might be getting more political attention, the ongoing plight of first time buyers (FTBs) excluded from the market due to the credit crunch looks set to rise up the agenda. Data on average mortgage rates (opposite) shows the spike in rates on the available higher loan-to-value mortgages typically used by FTBs. It's possible that around half of FTBs are now excluded from the housing market, though Help-to-Buy and reassessing budgets versus locations may reduce the net impact. However, once these factors are accounted for, it could be that FTB numbers are a third lower than normal while the credit crunch persists. If this is the case, it's worth noting that for every two months the credit crunch continues, the same number of buyers would be excluded from buying their first home as would be housed in a year by Affordable Homes Programme funded home-ownership homes.

Fig 2: Average 2 Year Fixed Rate by LTV
Source: Bank of England



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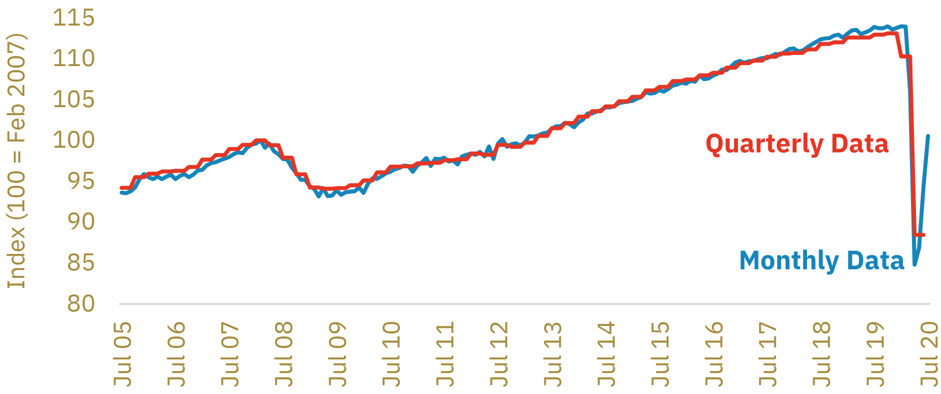
Market At A Glance

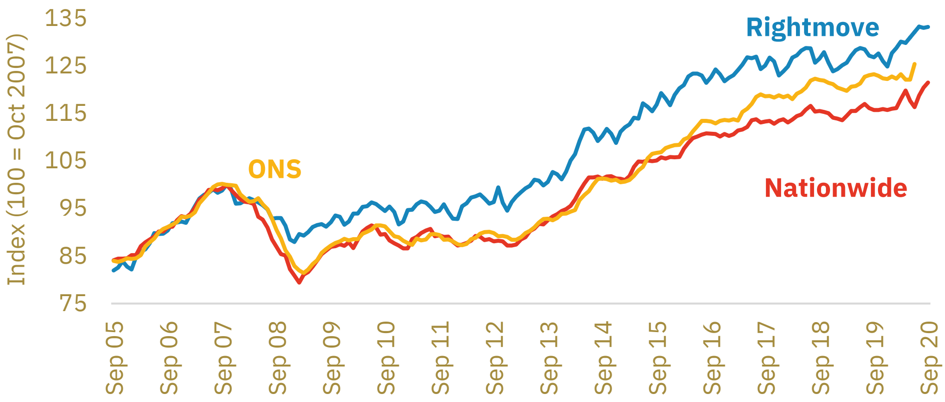
Economy - UK

The ONS's second estimate of GDP slightly revised the collapse in Q2 but it was still the biggest quarterly decline since quarterly data was first published in 1955. The quarterly data still highlights the trough but the monthly data shows the beginning of the recovery with GDP in July 11.8% below January's level (it was 17.2% below in June).



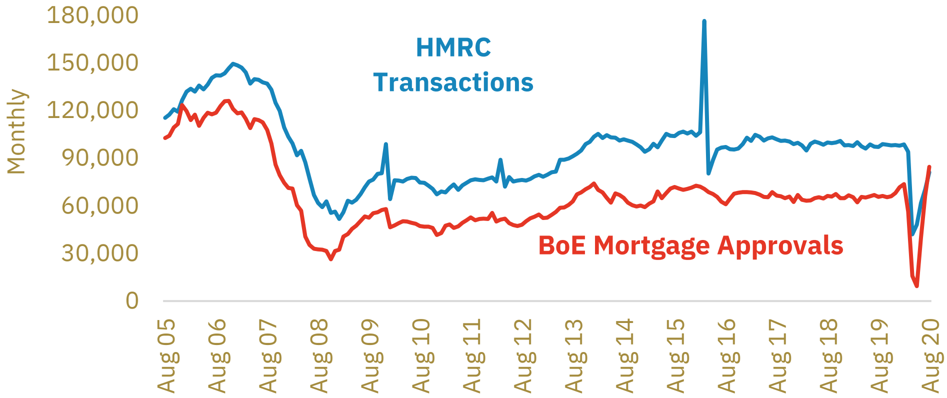
House Prices - UK

Both Rightmove and Nationwide reported a 5% annual increase in house prices during September. It looks increasingly likely that house prices will have risen by around that rate when year-end data is reported in Dec/Jan. Meanwhile the ONS index has caught up with its suspension during lockdown and it reported a 3.4% annual rise in June.



Transactions – UK

HMRC transactions have begun to recover but it will be the following months when we find out if the widely reported high numbers of sales agreed over the summer reach completion. The latest BoE mortgage approval data shows that, despite the crunch for riskier borrowers, there's still appetite for lending.



New Supply - England

There are issues with MHCLG's quarterly data though we have used it to suggest the potential path of completions opposite (dotted line). The best leading indicator for net additions is Energy Performance Certificates for new build homes. These suggest net supply fell to around 217,000 in the year to Q2 2020 but have recovered to normal levels in recent months.