Market Commentary

Residential Analysts

Powered by BuiltPlace

United Kingdom – April 2021

- **Housing Bubble or New Normal**
- **Not So Special**
- **A Tax Cut For All**

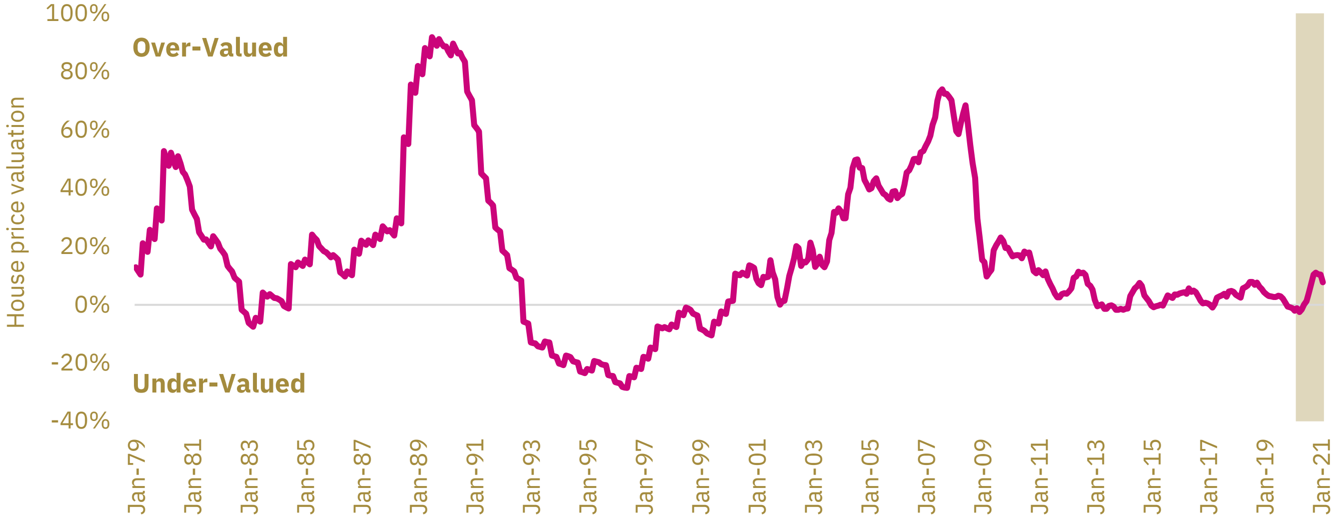
With house prices booming and transactions double their normal level, there are growing concerns that the housing market is in a bubble. It is also clear that there have been profound changes in the market since the pandemic hit, with many people reassessing what they want and need from housing. So, is this a house price bubble or are we seeing the start of a new normal created by the pandemic?

Housing Bubble or New Normal

The question of whether the UK housing market is in a bubble is not new. With the unaffordability of house prices, many may assume we were already experiencing a bubble before the pandemic hit. However, it was our view that house prices were priced appropriately when the pandemic hit, given underlying economic and mortgage lending conditions. Although house prices were high relative to incomes and access to the market was limited to those with large deposits, prices were at the level you might expect given existing wages and mortgage rates. Unlike previous bubbles, there were limited signs of stress in the market and mortgage borrowers were perhaps the safest they have ever been thanks to much tighter regulation since the financial crisis of 2007/08. It is possible that, if underlying economic or financial conditions had rapidly changed, we could quickly have found ourselves in a bubble as high prices and low mortgage rates make for a finely balanced market. However, despite all its failings, the housing market appeared to be priced appropriately. On this basis, if there is a bubble, it is one that has emerged since the pandemic hit.

Fig 1: Actual House Prices Compared To Modelled House Prices - UK

Source: ONS, Bank of England



Identifying an emerging bubble in real-time can be challenging for any asset, but it is especially difficult with housing due to the lack of timely and high-quality data. We know that house prices have risen rapidly since the market reopened last summer. However, the relative weight of the underlying drivers are still not clear. We will have to wait several months for Land Registry data to accurately reflect the location, type, and price of homes completing since the autumn though there are some early signs (see Fig 3). We will also have to wait for more data to find out who has been buying and selling during this period and their financial circumstances.

Furthermore, quirks in the data mean there can be short-term divergences that reflect short-term problems or issues with the metrics rather than the emergence of an actual bubble. An example can be seen in our above measure of whether house prices are over-valued or not relative to underlying wages and mortgage rates. The line's rise above zero in recent months suggests house prices have become slightly over-valued. The technical reason for this over-valuation is higher quoted mortgage rates thanks to the credit crunch which has reduced the apparent borrowing capacity of new buyers. However, we know actual buyers during this period have had higher incomes and used larger deposits. With the mortgage market now returning to normal, the spike is more likely to reflect a short-term shock to the housing market than an emerging bubble.

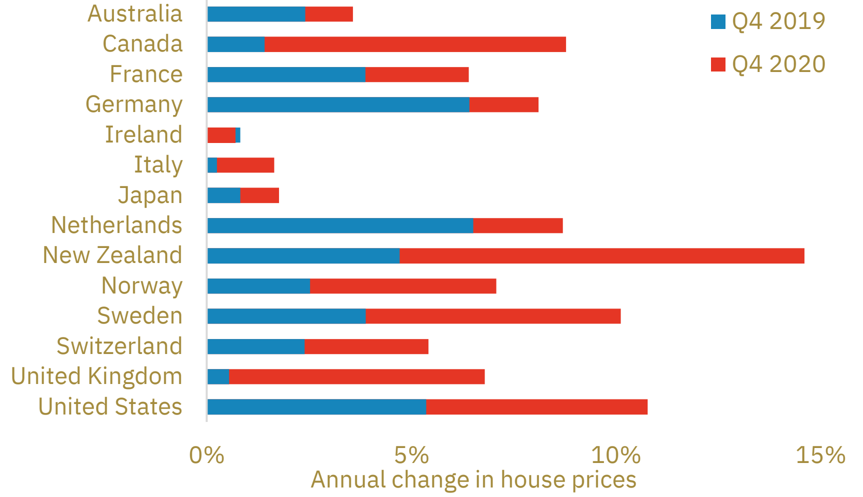
Not So Special

There are many drivers of the current housing market boom. Two stand out, the stamp duty holiday and the race for space. Of these, the stamp duty holiday is regularly considered the prime candidate. With the late extension, it is largely responsible for the enormous number of transactions completing in the first quarter of 2021. As a demand side subsidy, the holiday will also have contributed to higher prices and concerns that its end will lead to price falls. However, the current boom in house prices is not just a UK phenomenon. OECD data shows faster house price growth in numerous countries since the pandemic hit.

It appears the pandemic has led many people (certainly those who have the financial capacity and probably those that have saved more than normal during the pandemic) to reassess what they want and need from their housing and not just in the UK. While the race for space might be commonly characterised as wealthy Londoners looking to move to a large house in the country, it is more likely to be someone moving in the same town to an average priced home that offers an extra room or a larger garden. What is not clear is the extent that the stamp duty holiday has encouraged and enabled the race for space. The international data suggests this trend could continue when the holiday ends.

Fig 2: International Comparison of House Price Growth

Source: OECD, NZ updated using latest CoreLogic index via RBNZ



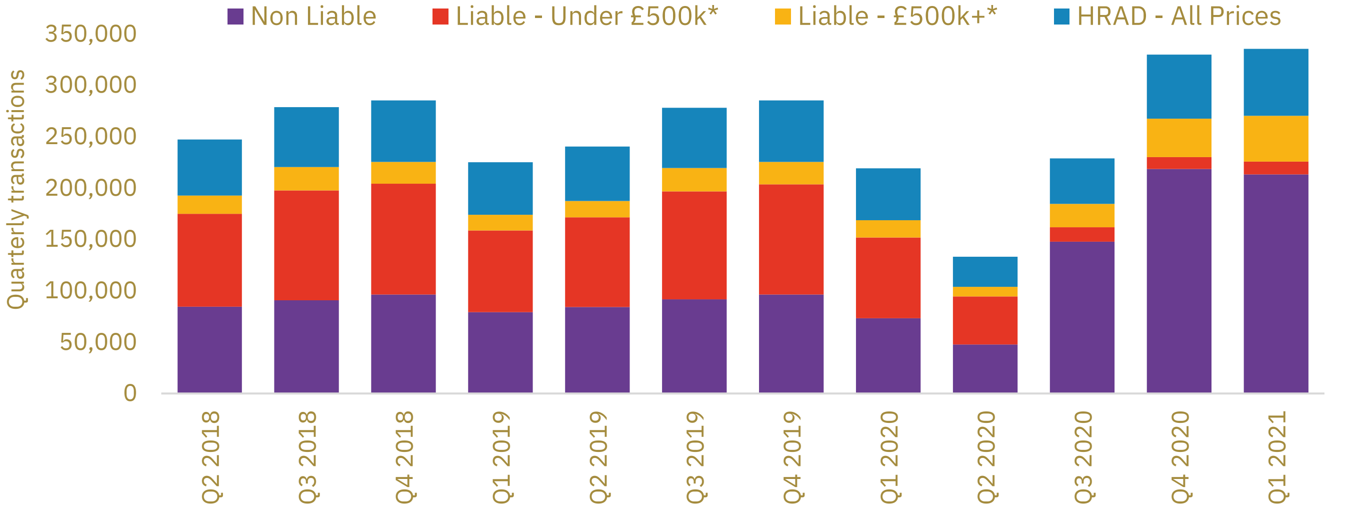
It is also not clear if the race for space is simply a one-off reaction to the pandemic that fades or reverses when life returns to normal, households' excess savings built up during the pandemic are all spent, or the widespread government support for the economy is removed. Alternatively, (I say this cautiously as someone who worked for an estate agent in 2007) we could be now in a new normal created by a unique event that leads to a permanent change in how we value housing and our built environment. The reality is that only time will tell us if this is the start of a bubble, short-term boom, or a new normal. It is too early to know. We will have to wait for future data that can help guide our understanding of the UK's housing market as we navigate these extraordinary times.

A Tax Cut For All

One useful data release is HMRC's quarterly stamp duty statistics for Q1 2021 data out today. The data reflects the boom in transactions completed as buyers rushed to beat the expected end of the stamp duty holiday. The data shows the majority of buyers paid no stamp duty as they were under the £500,000 threshold. But, in a sign of the wider role of both the stamp duty savings made by all buyers and the race for space, the biggest percentage increase in buyer numbers compared to Q1 2019 was amongst those paying £500,000 to £1 million.

Fig 3: Quarterly Residential Transactions by Stamp Duty Liability

*Source: HMRC - England & Northern Ireland - *excludes HRAD transactions*



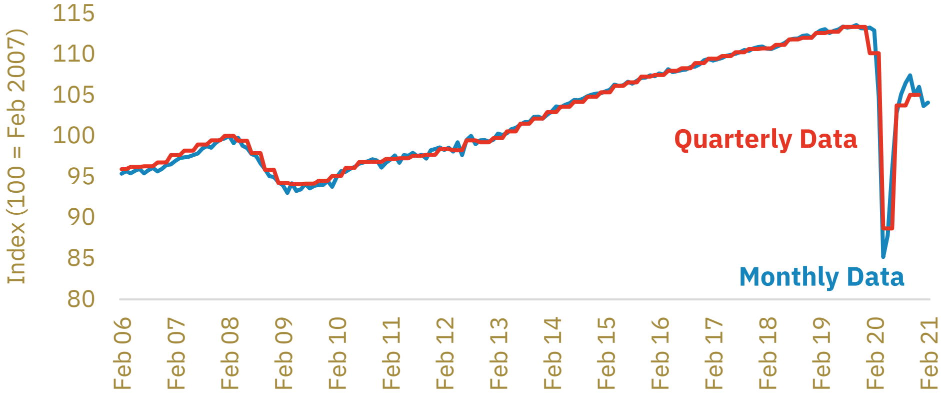
Market Commentary

Powered by BuiltPlace

Market At A Glance

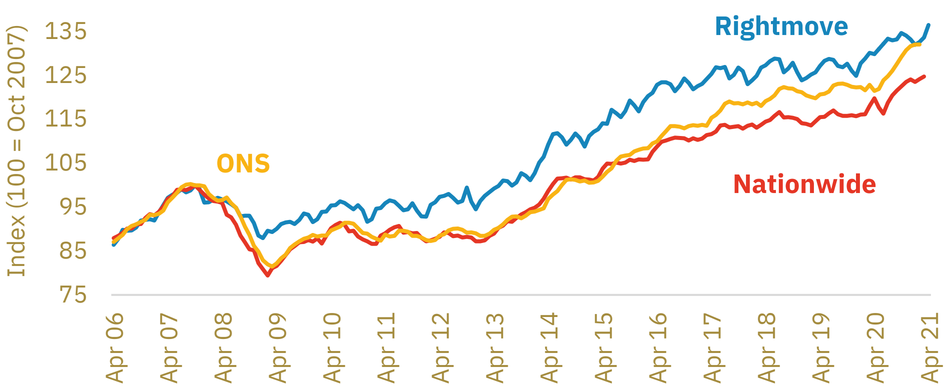
Economy - UK

The ONS reported a 0.4% monthly rise in GDP during February with the economy still 7.8% smaller than one year ago. The second estimate of GDP in the Quarterly National Accounts saw the total percentage fall in 2020 revised slightly from -9.9% to -9.8%. These figures are likely to be revised further in coming months and years.



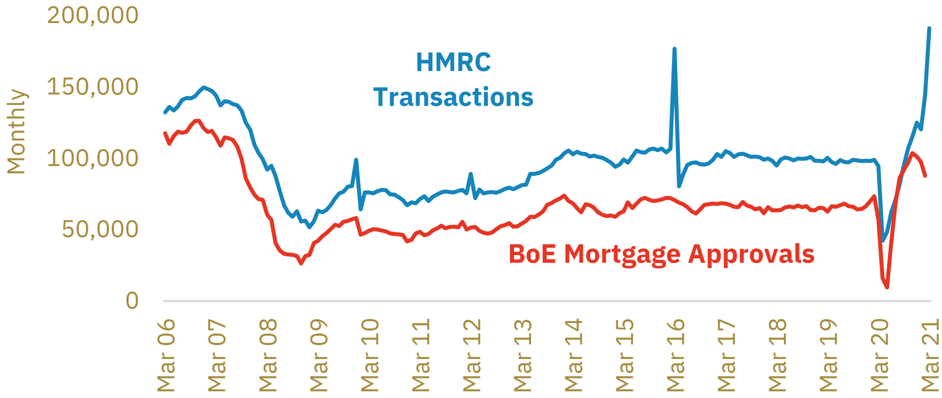
House Prices - UK

Rightmove reported a 5.1% rise in asking house prices in the year to April, rising from 2.7% the previous month. Meanwhile Nationwide reported a 7.1% annual rise in their mortgage approval based index over the same period and the ONS is now reporting very high growth in its sales agreed index with an 8.6% rise in the year to February 2021.



Transactions – UK

HMRC provisionally reported 191,000 transactions in March, 102% higher than the same month last year. Meanwhile, the Bank of England reported another fall in mortgage approvals for house purchase in February but they were still 19% higher than the same month last year. Approvals for remortgage were 34% lower than last year.



New Supply - England

There are issues with MHCLG's quarterly data though we have used it to suggest the potential path of completions (dotted line). The best leading indicator for supply is Energy Performance Certificates (EPCs) for new build homes with provisional data for Q4 2020 just 2.6% lower than the same quarter in 2019. Early estimates suggest net housing supply of 215,000 in 2020/21.