Market Commentary

Residential Analysts

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United Kingdom – June 2023

- **Everything But The Price**
- **Buying Less While Paying More**
- **Rising Arrears But Not Repossessions**

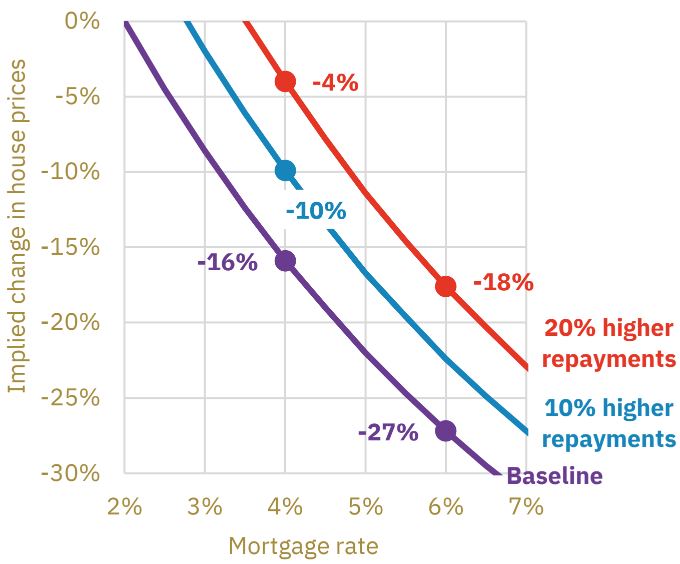
Mortgage dependent buyers are stretching every variable they can to afford still high house prices. As a result, they are ending up getting less while paying more than even just one year ago. Meanwhile, as more existing borrowers roll off their fixed rates, mortgage arrears are likely to increase but don't expect repossessions to follow. We also look at the number of first time buyers amidst claims they are at a twenty year high.

Everything But The Price

House price falls have been limited so far but the rapid increase in mortgage rates has hit the market hard, if you look beyond the headline price indices. When assessing the possible impact of higher mortgage rates last year, we suggested a rise to 4% could lead to a 16% fall in buying capacity and hence house prices for the typical borrower (purple line in Fig 1). However, we warned that previous periods like this have seen mortgaged buyers increase their repayments as a proportion of their income. We suggested that a 10% increase could be possible, with that implying 10% fall in house prices (blue line). In reality, typical repayments have increased by 20% and, as per our model, only led to a 4% fall in house prices (red line). Analysis of non-public UK Finance data on actual mortgaged buyers confirms this outcome. The rise in mortgage rates would've led to a big fall in buying capacity and house prices if not offset by higher repayments and, to a much lesser extent, longer terms and bigger deposits.

Fig 1: House Prices & Mortgage Rates

Source: BuiltPlace calculations using ONS RMS

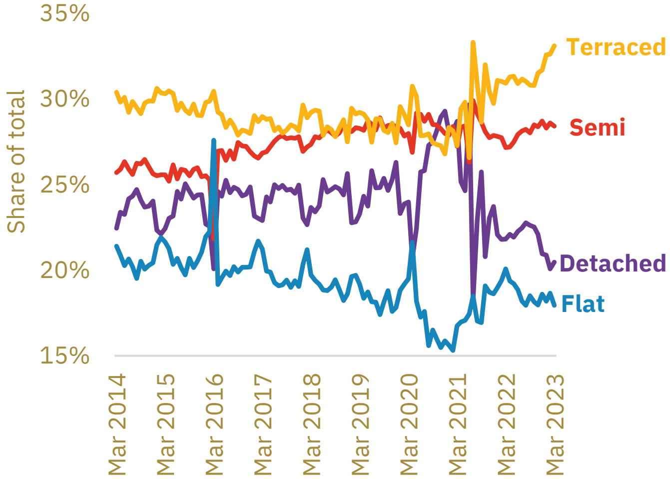


Buying Less While Paying More

Despite stretching themselves, many mortgage dependent buyers are still finding there's still a big shortfall in their budget relative to what they might've been able to afford last year and compared to the current still high expectations of vendors. As a result, it appears there have been some big changes in the mix and price of properties transacting over the last few months. The data is still provisional due to the Land Reg lag so we can't make any conclusions in terms of absolute numbers, However, it is clear, as per Fig 2, that there has been a proportional increase in the number of terraced houses and decrease in detached houses sold since last autumn.

Fig 2: Transactions by Property Type

Source: Land Registry Price Paid Data



In the absence of a house price correction, we have ended up with an even worse version of the already failing housing market we had last year. New buyers need even bigger deposits and have higher mortgage repayments that they will be stuck with for longer leading to higher total interest payments. And all this to buy a home that is probably smaller, further away, and less appropriate to their long term needs than the one they could've bought just last year.

With mortgage rates now rising again, it raises the question of whether this rate rise can be further offset by stretching everything but the price. My suspicion is not and if rates stay this high, we will see more of an impact on house prices. For example, the Fig 1 model suggests an 18% fall in prices with rates at 6% (red line). There is also the question of whether the rise in repayments is temporary – as it has been in the past – or a permanent adjustment in lending conditions.

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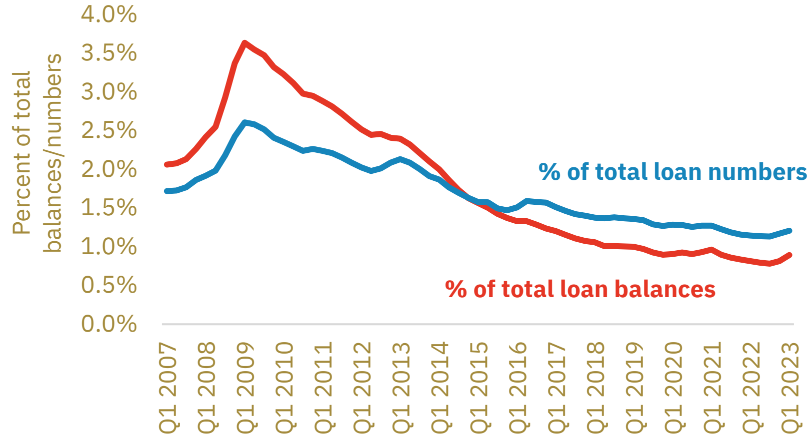
Arrears But Not Repossessions

With mortgage rates heading higher, the pressure on those rolling off record low fixed rates is increasing. Some will manage by paying more each month and cutting back on spending – the intended effect – while others with small remaining balances may even pay it off with savings. However, even with the available support such as extending terms and temporary interest only, there will be many who find themselves in financial difficulty. This is especially the case given the cost-of-living crisis. There will inevitably be an increase in arrears from their recent record lows (Fig 3) and lenders will have to focus their attention on their existing mortgage book rather than innovative new lending (100% LTVs anyone?!). However, despite the likely rise in arrears, it is much less likely that we will see repossessions hit the high numbers recorded during the last two downturns. Repossession is very much the last resort in this post financial crisis regulatory environment and lenders will be expected to do everything possible to avoid this outcome – even before the Chancellor announced his Mortgage Charter.

Fig 3: Mortgage Arrears
Source: BoE/FCA

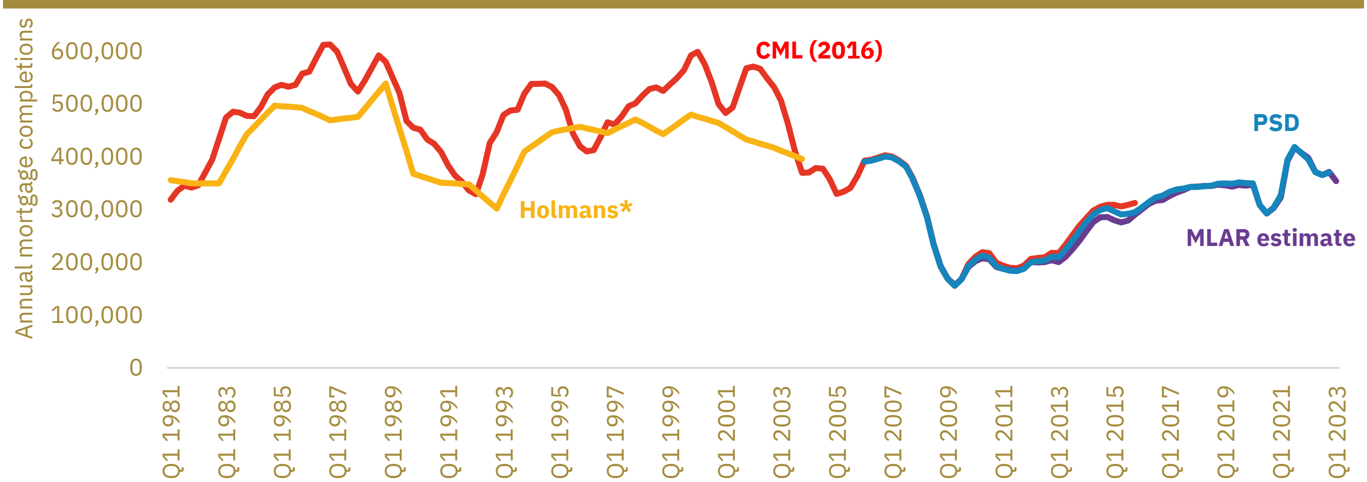


The priority for borrowers in difficulty is to get in touch with their lender as soon as possible. They are there to help and have duties of care - though they would probably benefit from a media campaign to highlight to the public how they have changed their behaviour since the late 2000s. Unfortunately, there will inevitably be some who fall through the gaps in processes and systems or for whom the available support just isn't sufficient. Even for those borrowers who end up facing repossession, the current constrained capacity of the legal system – already dealing with pandemic related backlogs – means there should be further pressure on lenders to avoid this route.

First Time Buyer Numbers

At Prime Minister's Questions this week, Rishi Sunak claimed "in the last year for which we have figures, we saw a 20-year high in the number of first-time buyers". This isn't totally wrong as data for 2021 does show there were over 400,000 mortgaged first time buyers during the year – actually peaking in September 2021 as the stamp duty holiday finally ended. And, as Fig 4 shows, this was probably the highest it has been in the last twenty years (since 2003). However, the prime minister's data was out of date as more recent data for 2022 suggests the number of first time buyers had already fallen back to around 370,000 per year and our estimates for Q1 2023 using MLAR data suggests the figure is still falling – down to 354,000. There is also the complexity of measuring first time buyers. There appears to be a disconnect between who the lenders report as a first time buyers and who the tax collectors think qualify for relief. This is not a new problem with "returners" regularly inflating numbers in previous decades – leading Alan Holmans to publish his own estimates for the true figures. It's quite possible that many of those helping push 2021's figure to a twenty year high were not actual first time buyers.

Fig 4: Annual First Time Buyer Numbers
Source: CML, Holmans, ONS, FCA (*annual data)*



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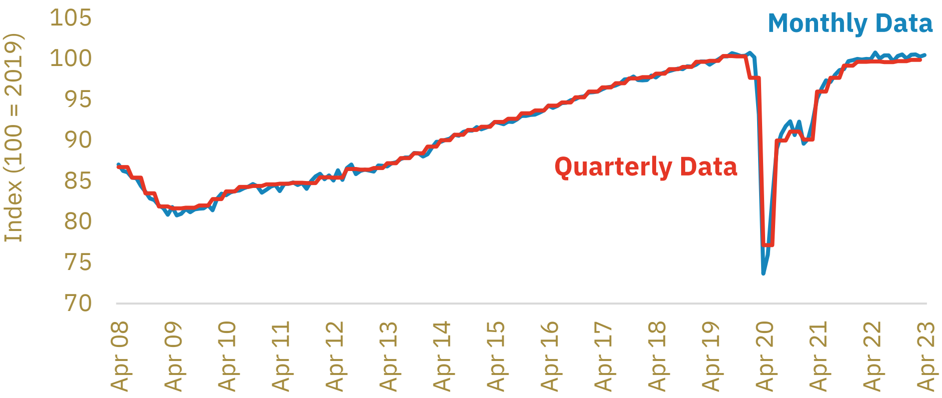
Market At A Glance

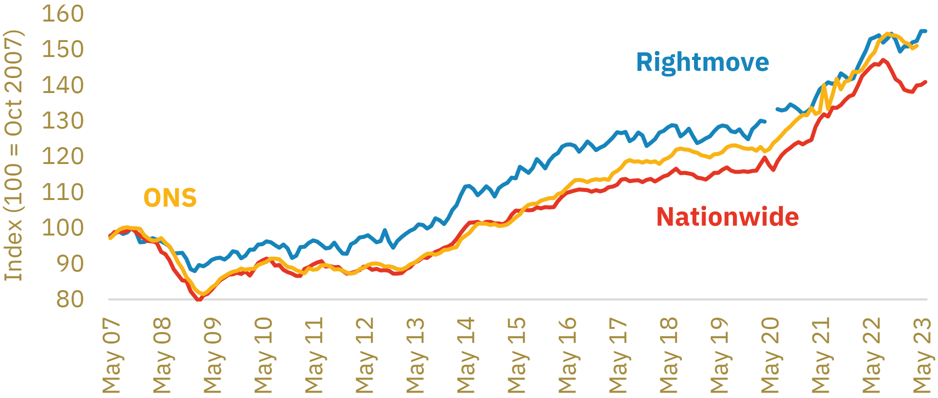
Economy – UK

The ONS monthly estimates reported GDP was 0.5% higher in April 2023 compared to the same month in 2022. This left monthly GDP 0.3% below the pre-pandemic peak recorded in January 2020. However, this data will inevitably be revised in coming months and years.



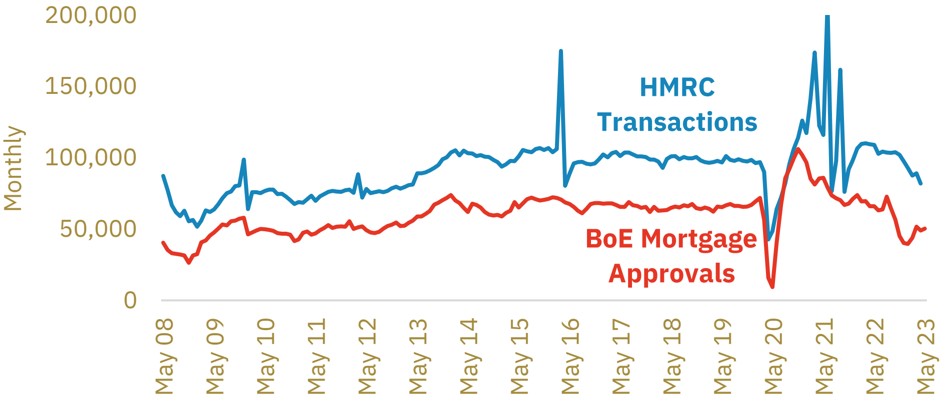
House Prices – UK

Rightmove reported a 1.1% annual rise in asking house prices in June 2023 while Nationwide reported a 3.5% annual fall in their mortgage approval based index in the same month. Meanwhile, the ONS reported 3.5% annual growth in its sales agreed index for the year to April 2023.



Transactions – UK

HMRC provisionally reported 82,120 residential transactions in April. This was 16.2% lower than the same month in 2019. Meanwhile, the Bank of England reported mortgage approvals for house purchase were 22.9% lower in May 2023 than the same month in 2019.



New Supply – England

The latest net additions data for 2021/22 reported 233,000 net new homes in England with 210,000 new build completions. The latest quarterly house-building data suggests there were 218,200 completions in the year to Q1 2023 while there were 246,800 new build Energy Performance Certificates in the year to Q1 2023 – a leading indicator for net housing supply.