Market Commentary

Residential Analysts

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United Kingdom – September 2023

- **Short-Term Volatility**
- **High-Rate Fallout**
- **Half-Year Transaction Update**

Mortgage rates may be falling from their summer highs but interest rates look set to stay higher for longer than many expected earlier in the year. Despite the downwards trend, there will inevitably be short-term volatility as markets react to new data and lenders adjust to changing conditions. As base rate rises ease, our attention will increasingly focus on the wider economy. Will we get a "soft landing" or will the economic stress created by higher rates lead to rising unemployment and forced sales. We also review sales data for the first half of the year.

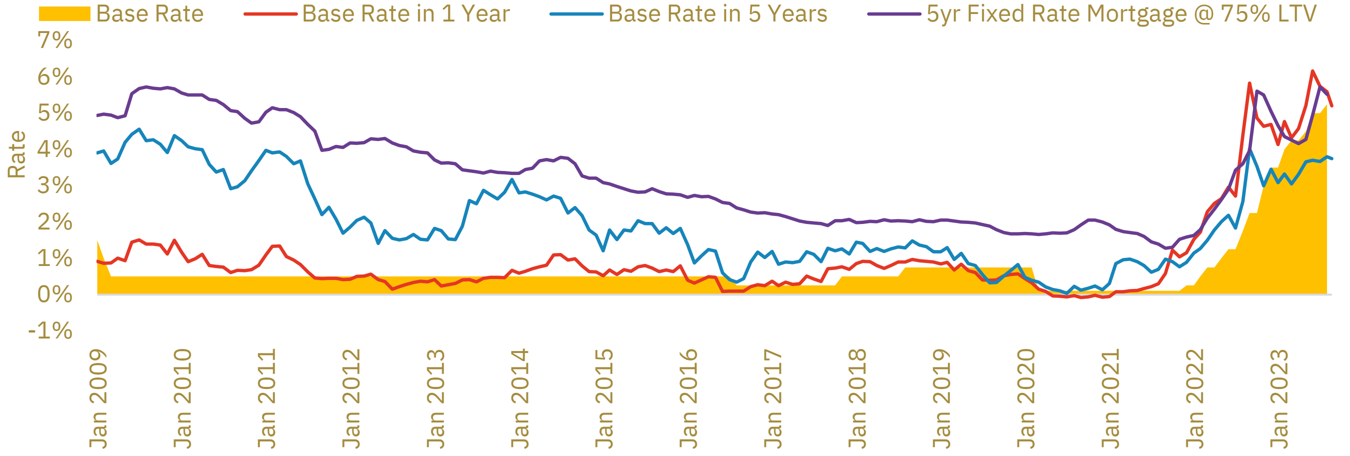
Short-Term Volatility

As the Bank of England took a pause from increasing Bank Rate this month, financial markets had already signalled their expectations that rates would be lower in the future than they had expected over the summer. As interest rate expectations have fallen, mortgage rates have also begun to ease, though at a slower rate. While they are still higher than in the spring, this will provide some relief for those reaching the end of their fixed rate period or the buyers that must move. But it appears rates look set to stay higher for longer than many expected and there will be more short-term volatility as financial markets react to new data – as seen in recent days.

We're yet to see the full impact of the summer mortgage rate highs in the data but, similarly to last winter, they look to have dampened activity more than prices. Rightmove recently reported sales agreed in August were 18% lower than the same month in 2019 and Bank of England mortgage approvals for house purchase in August were 37% below last year's figure. We're now into the autumn selling season when activity tends to pick up. But, with rates still elevated and little prospect for a return to record lows, there has been a weakening in both consumer and corporate sentiment towards the prospects for the housing market in recent months. This is reinforcing the stagnation already seen across many parts of the housing market as both people sit tight, waiting for prices to move or activity to improve. But, while rates remain high, the latter is unlikely without the former.

Fig 1: Mortgage Rates, Base Rate, & Market Expectations for Base Rate

Source: Bank of England – At Month End



High-Rate Fallout

It has become clear over the last year that interest rates are not the powerful tool they once were in the housing market. Fewer mortgaged homeowners and more fixed rates have helped insulate many from the immediate impact of higher rates compared to previous periods. But the economic fallout will still be felt, albeit not equally. Many will remain unaffected while others will feel the full weight, each depending on their personal and financial circumstances. As rate rises ease, our attention is increasingly turning to the labour market. Has the Bank of England done enough to dampen inflation without causing too much damage to the wider economy – a "soft landing". Or will there be economic fallout from higher rates, with rising unemployment putting further pressure on household finances, leading to more motivated (if not forced) sellers. The next six months could be key for the housing market's prospects over the next few years. Will a weakening labour market be the trigger for prices to correct to levels more in line with higher rates, creating the conditions for a recovery in activity. Or will the market continue to stagnate and adjust much more slowly, with prices only improving in real terms. Both outcomes have their downsides, but both are an inevitable result of how the housing market has evolved over the last decade.

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Half-Year Transaction Update

Fig 2: Estimated Transactions by Region
Source: HM Land Registry Price Paid

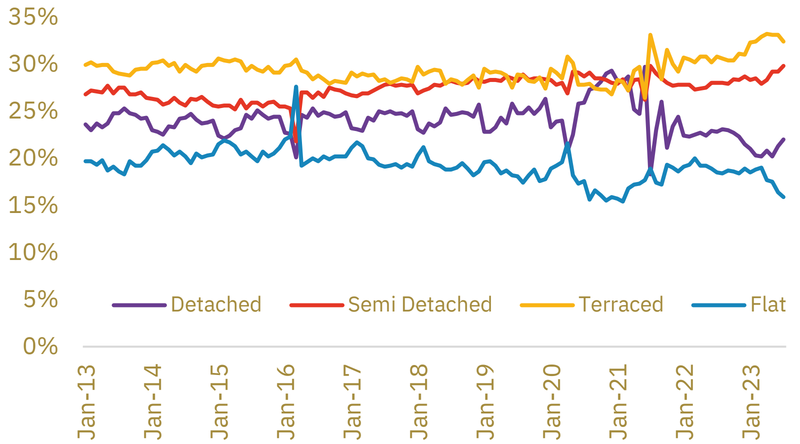
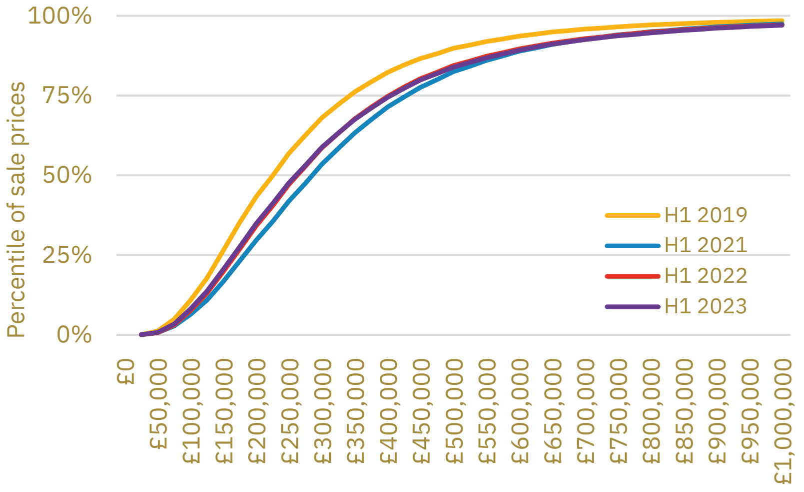


Fig 3: Estimated Transactions by Region
Source: HM Land Registry Price Paid

Fig 4: Cumulative Price Distribution
Source: Calculated using HM Land Registry Price Paid & HMRC



Today's HMRC release provides a timely estimate for national housing transactions but little in the way of detail on what is being sold or where. Instead, we need to use the Land Registry price paid data. Unfortunately, it has a lag in when transactions are registered but the delay appears to have improved since the pandemic. Therefore, while we don't yet have every sale in the first half of 2023, we do now have enough of a sample for doing some analysis.

Perhaps the most important message that emerges from the Land Registry data is the change in the mix of property types that have been selling (Fig 2) – both during the pandemic and over the last year. There has been significant volatility in this mix and it will have had an impact on some house price measures. It also highlights how higher rates are affecting different markets, with the share of flats falling from 19% to 16% since the beginning of the year.

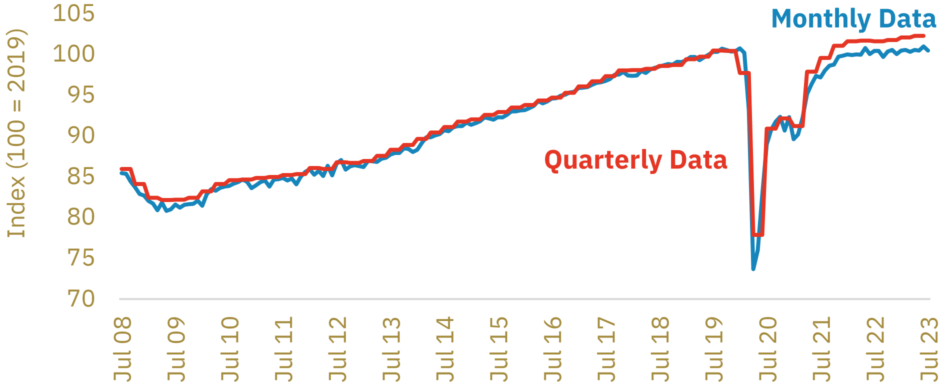
Using a combination of the Land Registry and HMRC transactions, we have also estimated the total number of regional transactions in the first half of 2023. As Fig 3 shows, all regions have seen a fall in activity compared to the same period last year. However, the comparisons with both 2019 and 2014 are more interesting. Again, most regions have seen lower numbers than 2019 except for the North East where they are broadly similar. The other exception is London where transactions are lower but not to the same extent as most other regions. The reason for this is highlighted by the figure for H1 2014, with London sales down 32% compared to this period – prior to all the SDLT tax changes. Meanwhile, sales in the North East were 15% higher this year when compared to 2014.

Finally, we have looked at the distribution of sold prices in the first half of the year (Fig 4). At first glance, it might appear that we've missed off the figure for 2022. However, it's hidden behind this year's figure as, despite all the changes in mix, the overall price distribution is almost unchanged from last year. For example, the median price is just 0.9% lower this year and the upper quartile price is just 1.2% higher. Comparing to two years ago, the price distribution is much lower, when the SDLT holiday helped increase the number of higher value sales in the market – the median price in H1 2023 was 8.5% lower than in H1 2021 but it was still 16.2% higher than the H1 20219 figure.

Market At A Glance

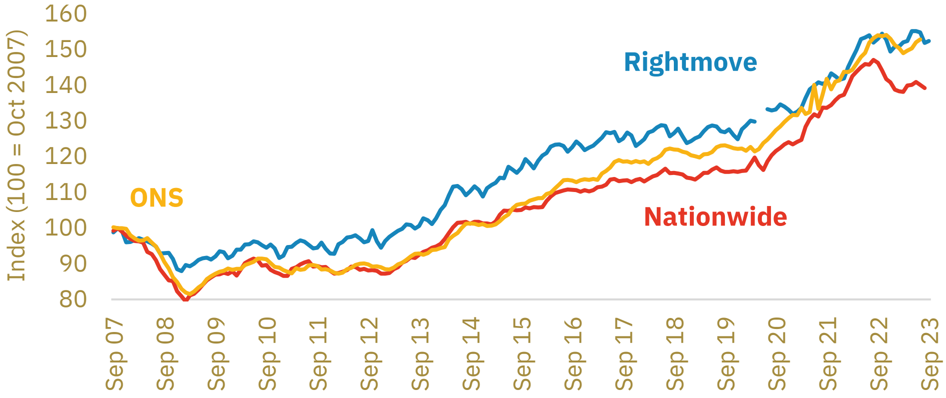
Economy – UK

The ONS estimated monthly GDP was unchanged in the year to July 2023. This left monthly GDP 0.3% below the pre-pandemic peak recorded in January 2020. However, this monthly data will be revised upwards in coming months to reflect the recent ONS Blue Book findings as per the latest quarterly data opposite.



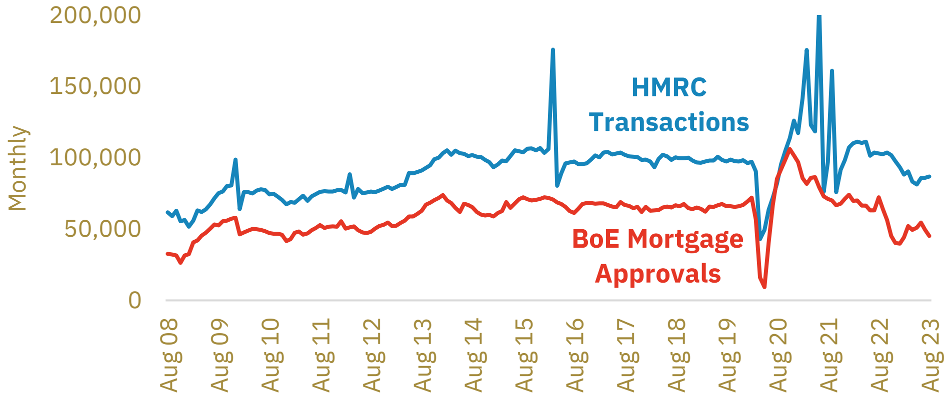
House Prices – UK

Rightmove reported a 0.4% annual fall in asking house prices in September 2023 while Nationwide reported a 5.3% annual fall in their mortgage approval based index in the year to August. Meanwhile, the ONS reported 0.6% annual growth in its sales agreed index for the year to July 2023.



Transactions – UK

HMRC provisionally reported 87,010 residential transactions in August. This was 11% lower than the same month in 2019. Meanwhile, the Bank of England reported mortgage approvals for house purchase were 32% lower in August 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 211,200 completions in the year to Q2 2023 while there were 239,300 new build Energy Performance Certificates in the year to Q2 2023 – a leading indicator for net housing supply.