Market Commentary

Residential Analysts

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United Kingdom – October 2023

- **Teetering On The Edge**
- **But This Is No Precipice**

The housing market has been stagnating in recent months as the impact of high mortgage rates has been seen in much lower levels of activity. However, there are signs of weakening sentiment as rates stay higher for longer and the market is teetering on the edge of further prices. However, any further price falls should be relatively modest.

Teetering On The Edge

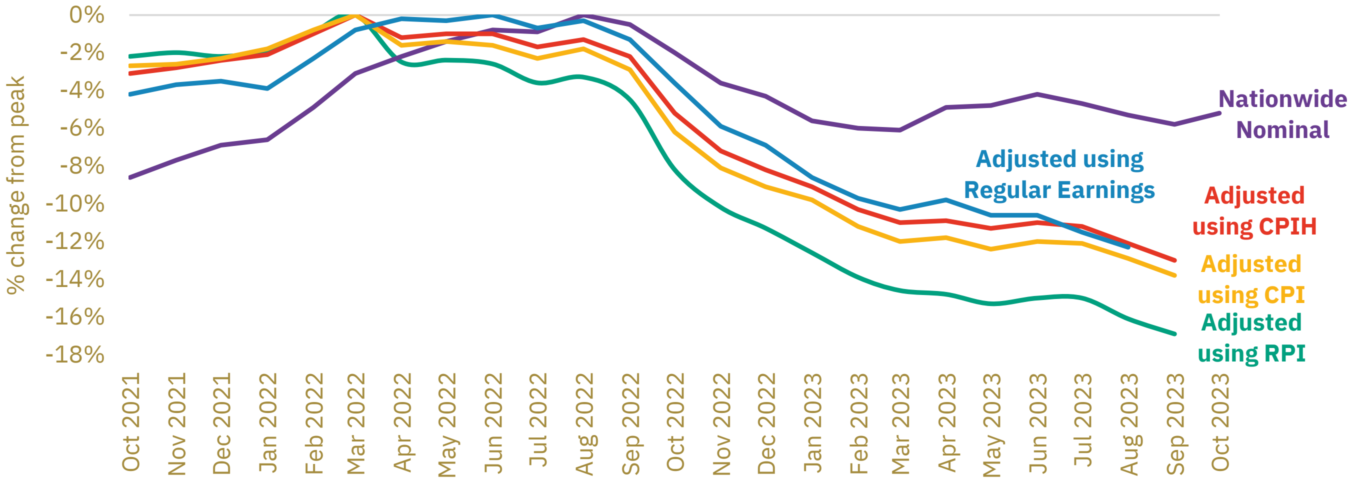
When recently asked to describe the state of the UK housing market, the word I arrived at was "teetering". So far, despite some price falls, most of the reaction to much higher mortgage rates has been lower activity: resulting in a stagnant market. But recently there has been a growing undercurrent of weakening sentiment and nervousness across the market as mortgage rates have stayed much higher for a lot longer than most people expected. The housing market may continue stagnating but, in this state, it wouldn't take much to push it into further price falls.

The latest mortgage data highlights the current market stagnation due to high rates. On Monday, the Bank of England released data showing the average mortgage rate on new lending hit 5.03% in September – the first time it's been over 5% since November 2008. As a result, the number of mortgage approvals for house purchase was 32% lower than last year and the worst month of September since 2008. The impact on total market activity has been less thanks to cash buyers but sales were still 17% lower in September when compared to last year.

As we've highlighted previously, those mortgage dependent buyers that are still active are facing all the pre-existing issues around the cost of buying (big deposits, higher incomes etc) but are now faced with higher mortgage repayments than just a year or two ago. However, with most rates above 5% and even higher stress-testing rates, the capacity to stretch repayments further is limited. Far fewer people are able or willing to buy at current price levels. Meanwhile, prices are down 5.2% from peak according to the Nationwide index and, while down more than double that when adjusted for rising earnings, this is still not enough to counter-act higher rates.

Fig 1: Change in Nominal and Real House Prices From Peak

Source: Nationwide, ONS



But This Is No Precipice

Nominal house price falls have been limited so far and the economic fallout from high rates has yet to really emerge - though poor data is hampering our understanding of the labour market. We have not seen a flood of forced sellers that would be required for a significant price correction and the number of homes being listed on the market appears to have continued at around normal levels. However, because of much lower transactions, there are now signs of rising stock levels - especially at certain price points (the £5 million plus market in central London is especially interesting!). These rising stock levels could contribute to further price falls in coming months if mortgage rates remain high and sentiment continues to weaken. Ultimately, it comes down to a question of balance. House prices are teetering on the edge. We could see them continue to plateau while activity stagnates. But it increasingly appears that the balance is shifting towards further price falls. However, if the market does tip over the edge and nominal prices start falling again, it is still unlikely that this will result in substantial price falls. Our modelling suggests, in the absence of mass unemployment, that this means another 5% to 10% off national prices from current levels rather than a crash that matches the scale of the late 2000s or early 1990s.

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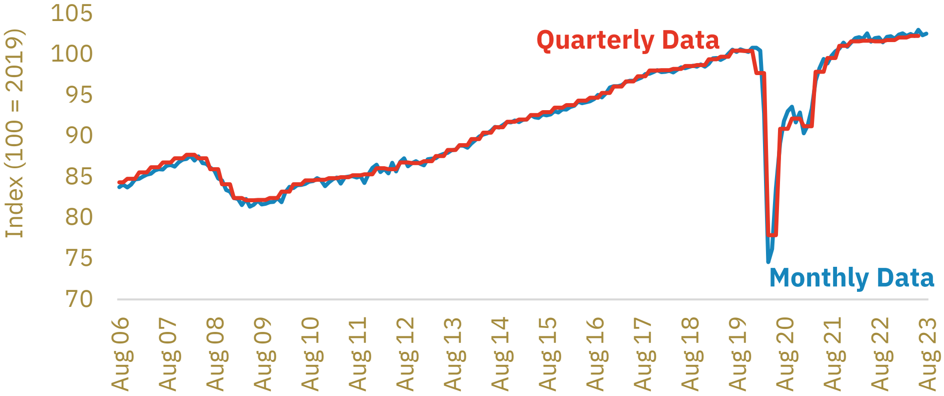
Market At A Glance

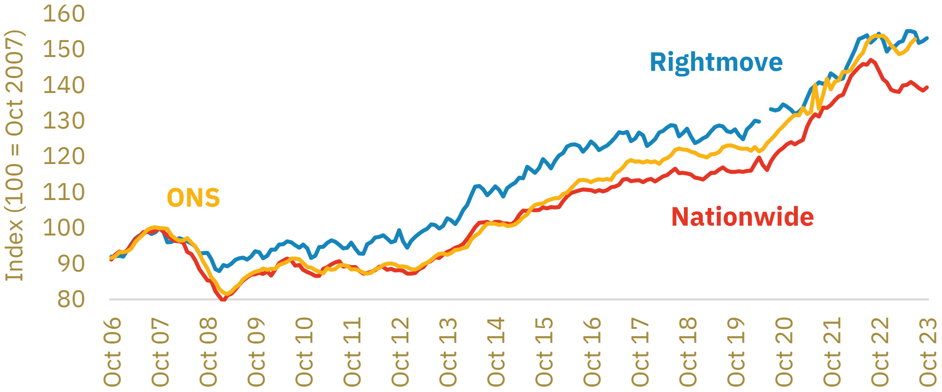
Economy – UK

The ONS estimated monthly GDP increased 0.5% in the year to August 2023. Thanks to recent revisions, monthly GDP was 1.7% above the pre-pandemic peak recorded in January 2020. However, this monthly data will continue to be revised in coming months.



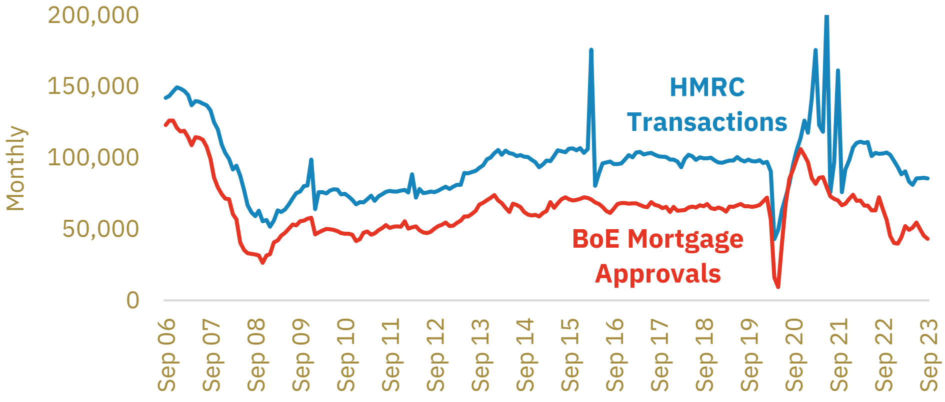
House Prices – UK

Rightmove reported a 0.8% annual fall in asking house prices in October 2023 while Nationwide reported a 3.3% annual fall in their mortgage approval based index in the year to October. Meanwhile, the ONS reported 0.2% annual growth in its sales agreed index for the year to August 2023.



Transactions – UK

HMRC provisionally reported 85,610 residential transactions in September. This was 13% lower than the same month in 2019. Meanwhile, the Bank of England reported mortgage approvals for house purchase were 34% lower in September 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 237,000 new build Energy Performance Certificates in the year to Q3 2023 – a leading indicator for net housing supply.