Market Commentary

Residential Analysts

Powered by BuiltPlace

United Kingdom – April 2024

- **On The Rise Again**
- **Peering Into The Affordability Black Box**

Everything is rising but something must give. House prices are up on last year, activity levels are recovering back to pre-pandemic levels, and interest rates are increasing. Unfortunately, the first two are incompatible with the third and, if interest rates stay high, it is likely that activity and house prices will weaken in coming months.

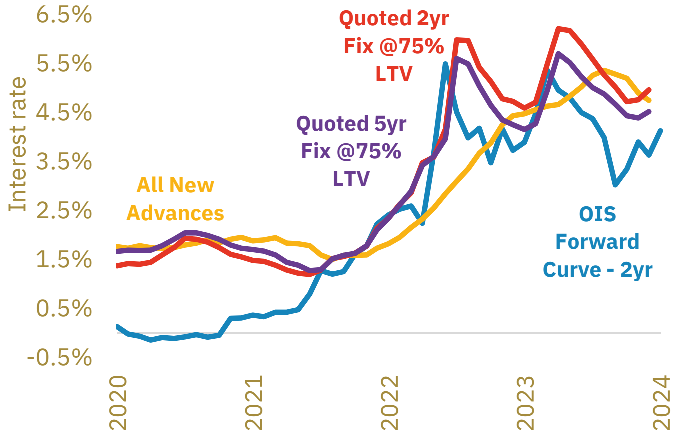
On The Rise Again

Most housing market measures are rising again. The latest house price indices are reporting prices slightly higher than last year, though the Nationwide index is rising less rapidly and there is significant regional variation. Meanwhile, there have been reports of robust sales agreed figures in recent months and these are now being reflected in the number of mortgage approvals for house purchase - just 7% below their pre-pandemic average. However, the total number of completed transactions is taking longer to recover and is still 15% below the pre-pandemic average, presumably due to the challenges in completing thanks to delays and fall throughs.

The recovery in market activity has also encouraged more people to list their homes for sale. With higher numbers of new listings, the total stock of homes available to buy has continued to increase, especially towards the upper end of the market. These higher levels of stock could be a challenge for the housing market if demand falters as rates rise and the economy weakens. The recent trend in interest rates has also been upwards since the beginning of the year (Fig 1) and there are growing reports of lenders increasing mortgage rates in response. These rate rises will dampen demand in the short-term but the prospects for the market over the rest of the year are still uncertain. Based on previous trends, the Nationwide index is on track for year-end growth of 3% but this could quickly rise or fall depending on what happens to rates.

Fig 1: Interest & Mortgage Rates

Source: Bank of England

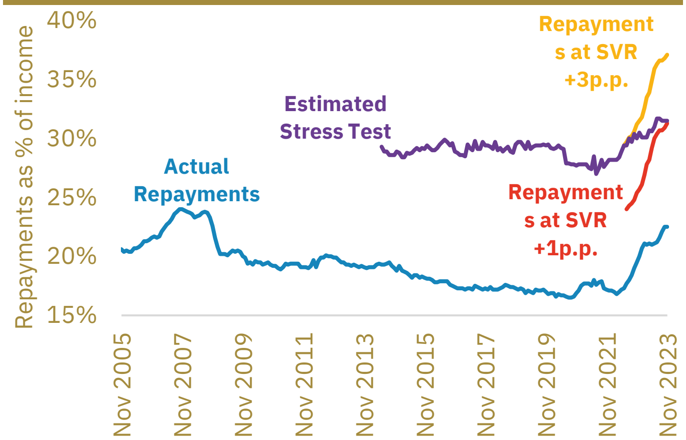


Peering Into The Affordability Black Box

Understanding how lenders apply affordability stress testing models is difficult given the lack of information available and the commercial sensitivity involved. However, we do know that lenders are reliant on ONS spending data and we can see the outputs of the models in terms of who is able to borrow and the conditions under which they do so from market data. As part of my recent report on first time buyers, I did some research using UK Finance and Bank of England data on mortgage repayments and stress test rates. This allowed us to assess the impact of the stress testing regime, including the impact of the shift from testing at +3p.p. to +1p.p.. More detail can be found in the report(PDF), but to summarise: We found, while low rates were largely priced into the market, they were not fully priced in. Loan-to-income ratios could have been around 10-15% higher in the absence of the stress testing regime. The analysis also shows that if the 3p.p. stress test was still in place, then the fall in average loan-to-income ratios since rates started rising could have been 25% rather than the 10% recorded. The analysis also highlights how lenders have been much more willing to allow borrowers to pay more than 30% of their gross income on repayments since the change in the stress testing regime. As our previous analysis has shown, this increase in repayments has almost fully offset the increase in mortgage rates and help avoid a bigger correction in house prices. The question looking ahead is whether mortgage rates or house prices will fall, or if these higher repayment levels will become a more permanent feature of the market.

Fig 2: First Time Buyer Stress Testing

Source: BuiltPlace analysis of UK Finance and BoE data



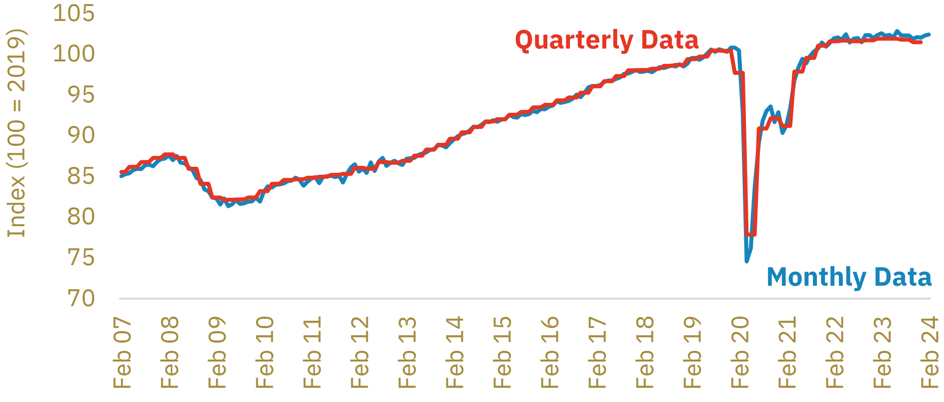
Market Commentary

Powered by BuiltPlace

Market At A Glance

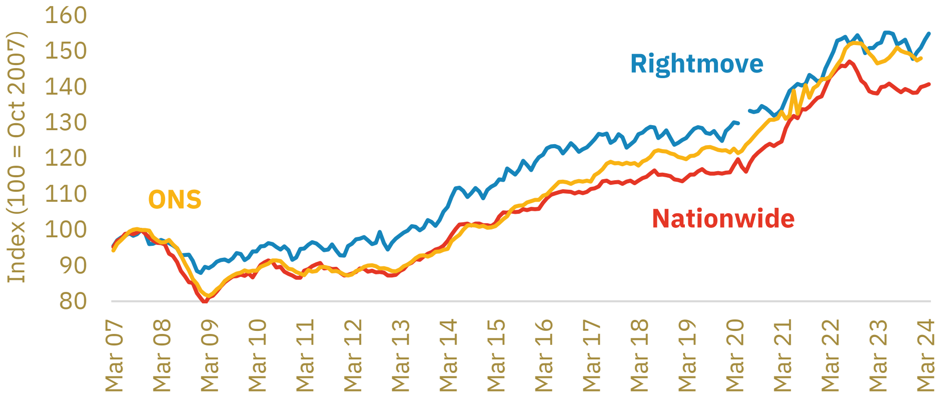
Economy – UK

The ONS estimated monthly GDP fell 0.2% in the year to February 2024. Monthly GDP was 1.6% above the pre-pandemic peak recorded in January 2020. However, this monthly data will continue to be revised in the future.



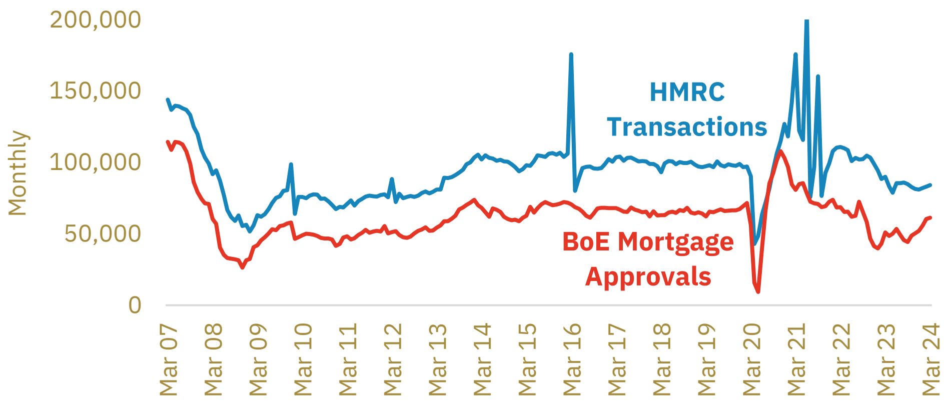
House Prices – UK

Rightmove reported a 1.7% annual rise in asking house prices in April 2024 while Nationwide reported a 0.6% annual rise in their mortgage approval-based index over the same period. Meanwhile, the ONS reported a 0.2% annual fall in its sales agreed index for the year to February 2024.



Transactions – UK

HMRC provisionally reported 84,200 residential transactions in March. This was 14% lower than the same month in 2019. Meanwhile, the Bank of England reported mortgage approvals for house purchase were just 1% lower in March 2024 than the same month in 2019.



New Supply – England

The latest net additions data for 2022/23 reported 234,400 net new homes in England with 212,600 new build completions. The latest quarterly house-building data suggests there were 193,000 completions in the year to Q4 2023 while there were 232,500 new build Energy Performance Certificates in the year to Q1 2024 – a leading indicator for net housing supply.