INSIGHT

Housing Market Summary

Quarterly update of housing market activity

Q4 2021

AVISON YOUNG

Overview

- House price growth in the UK remained strong in Q4 despite the initial tapering of the Stamp Duty Land Tax (SDLT) holiday at the end of June and the final tapering in September. Nationwide reported 10.4% growth for 2021, the highest level for a calendar year since 2006. This puts the average UK house price at £254,822, compared to £229,819 at the same time last year.
- Transactional activity also remained strong in the final quarter of the year, although it normalised relative to the very high levels that characterised the first three quarters of the year. There were 300,560 transactions in the UK in Q4, down 15% on Q3. Over the past 12 months, transaction levels have been the highest we have seen since the Global Financial Crisis and 25% above the 2019 total.
- Although we expect the market to cool somewhat in 2022, the latest RICS Residential Market Survey and internet searches suggest buyer demand ticked up in December, having receded over the previous two months (although still high). Zoopla have also reported higher than typical demand for the time of year.
- Another factor which will help support price growth is very limited supply. According to the RICS survey, the number of homes per surveyor at its lowest level on record except for the housing market shutdown in Q2 2020.

The Housing Market

The Nationwide House Price Index (HPI) showed a 1.0% month-on-month increase in December, up from 0.9% in November. This brought the annualised growth rate to 10.4%.

Other measures of house prices paint a similar picture of the market, the ONS House Price Index (HPI) which lags the Nationwide figures, recorded annualised growth of 10% in November, ahead of the previous month's 9.8%. Zoopla reported slightly lower but still strong figures, with annualised growth in November at 7.1% for the UK. They also reported that the market continues to move very quickly with the average time to sell a property averaging less than 30 days.

The RICS Residential Market Survey is one of the better leading indicators of market performance, and the most recent survey points to the continuation of solid levels of activity for housing transactions. Robust demand will continue be set against a limited pool of supply, ensuring competition between buyers remains intense. This imbalance will help maintain upward pressure on pricing even as interest rates rise over the course of 2022.

Help to Buy

The extended Help to Buy scheme expired on 31st March 2021 following an extension due to Covid-19. An adapted version will now continue with a more limited capacity through to 2023. Under the new iteration, the government will still provide an equity loan of up to 20% for the purchase of a new build home to enable buyers with only a 5% deposit to acquire the remaining 75% through a mortgage. The previous price cap was replaced by significantly lower regional price caps, defined as 1.5 times the average price of a first-time buyer property for each region. While the original version of the scheme was used by over 270,000 home buyers since its inception in 2013, there were questions around its efficacy – many of which have persisted with the new changes. The latest evolution also may disrupt the viability of some developments which were targeting the Help to Buy market at above the new regional price caps.

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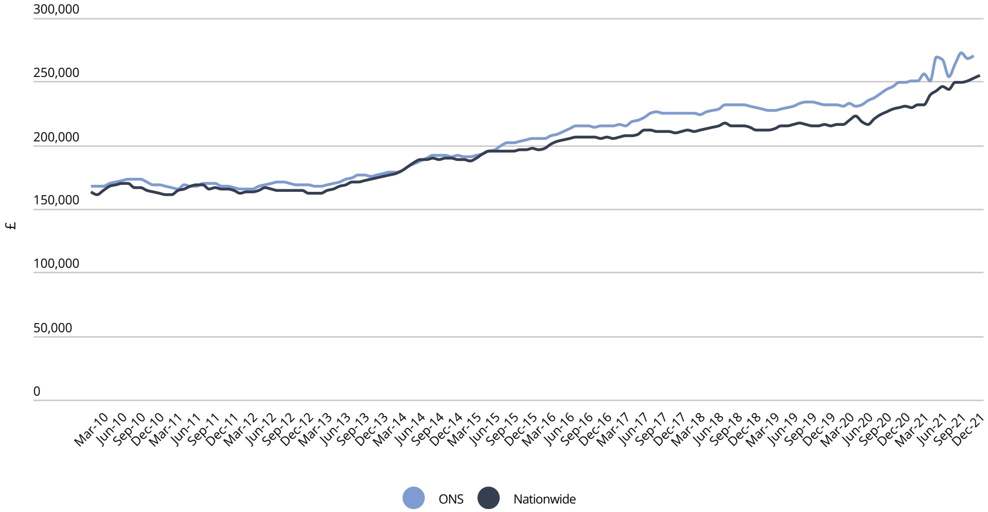
> **We expect the housing market to normalise somewhat this quarter, with wider macro-economic factors to return as the key drivers of the housing market. Our near-term economic outlook is broadly positive although supply chain pressures and inflation are posing an increasing risk.**

Data

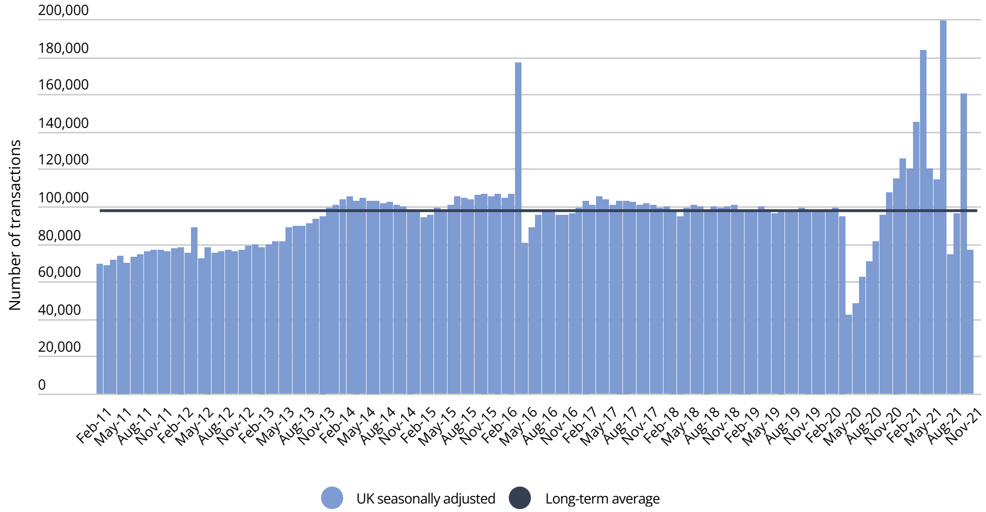
UK HOUSE PRICES

Source: Land Registry, Nationwide



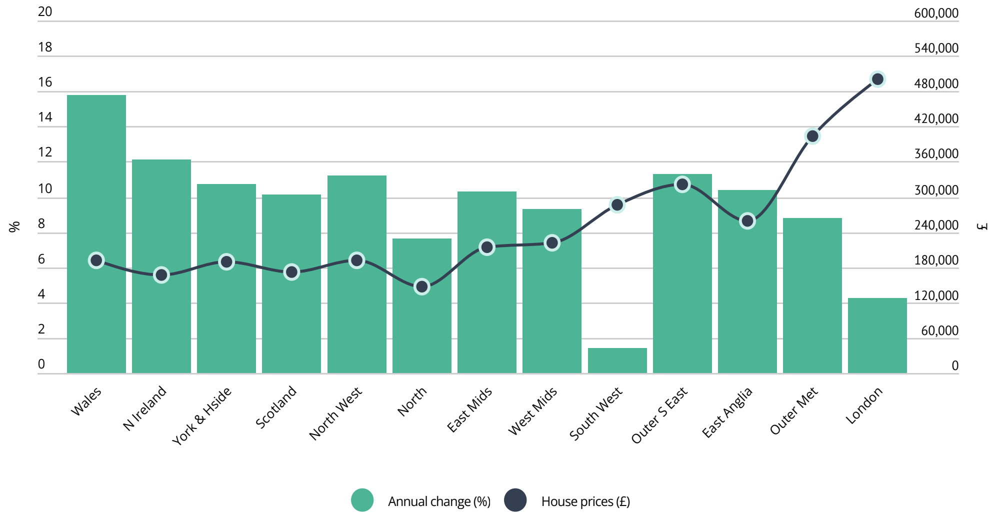
HOUSING TRANSACTIONS IN THE UK

Source: HMRC



REGIONAL HOUSE PRICES & ANNUAL GROWTH - Q4 2021

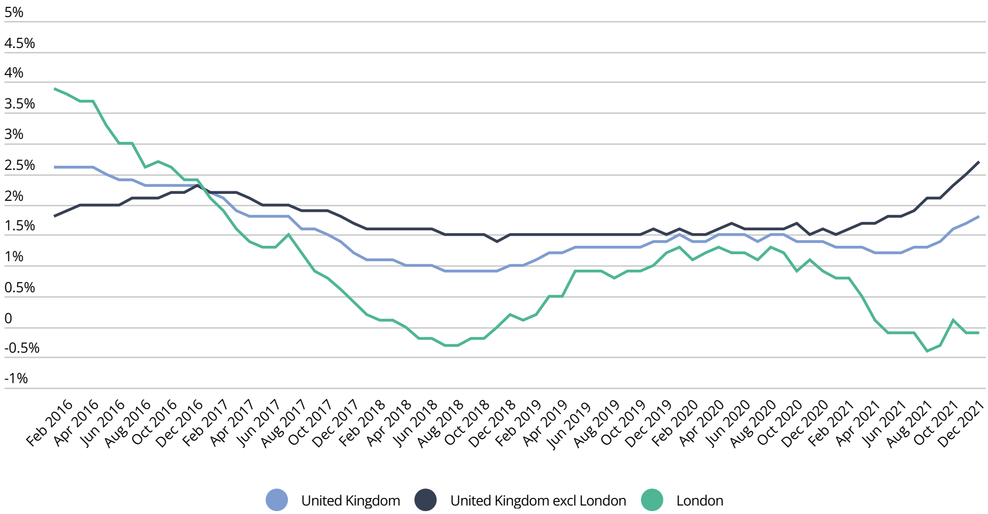
Source: Nationwide



Data

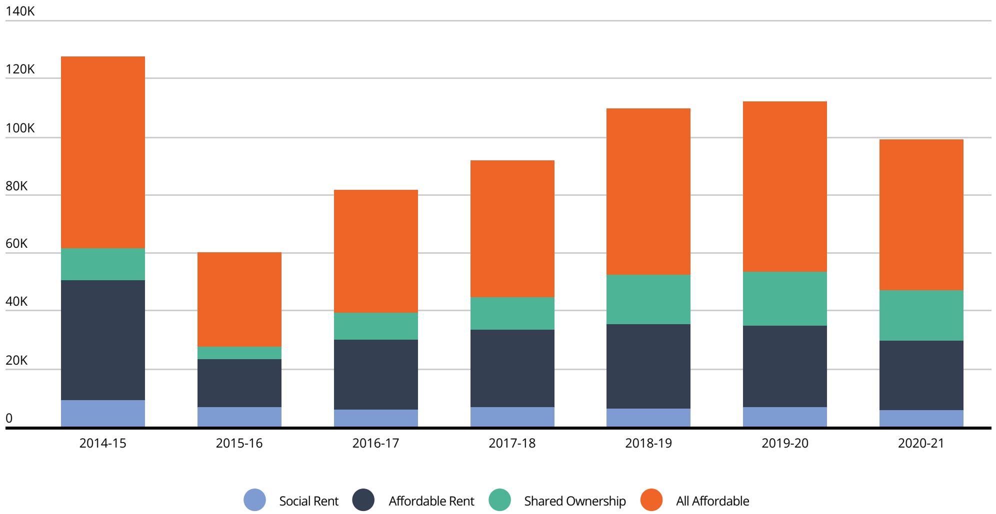
ANNUAL PRIVATE RENTAL GROWTH

Source: ONS



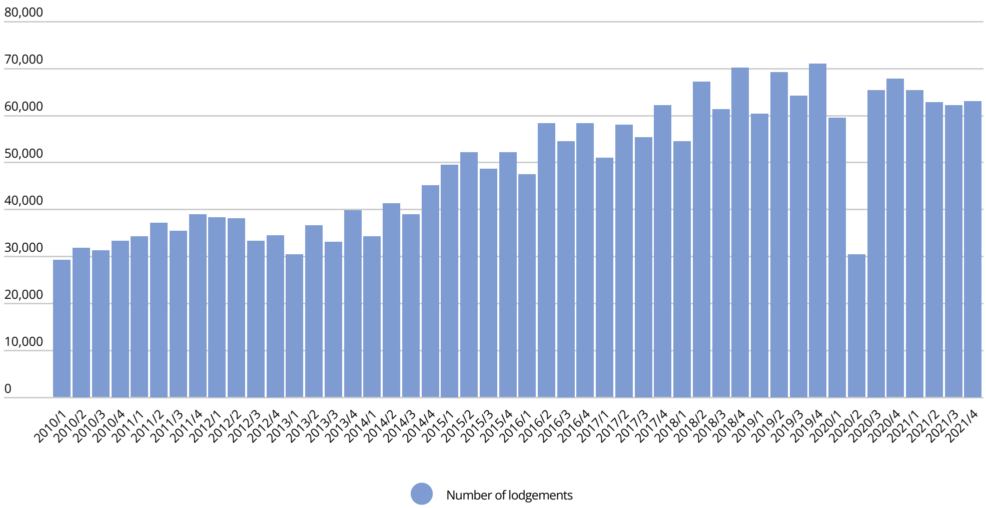
AFFORDABLE DELIVERY

Source: MHCLG



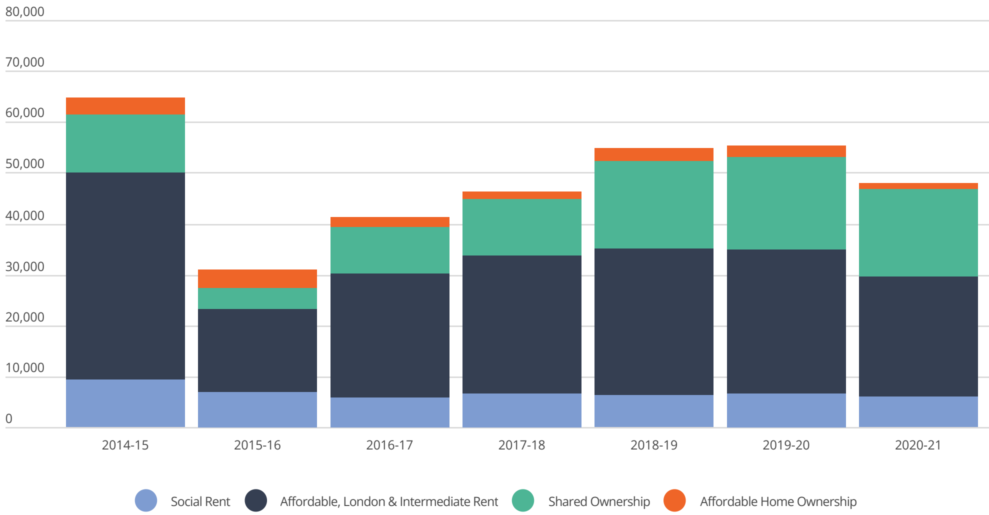
DOMESTIC EPC LODGEMENTS

Source: MHCLG



AFFORDABLE HOME COMPLETIONS BY TENURE IN ENGLAND

Source: MHCLG



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While mortgage interest rates remain low in a historical context, the rises will impact first-time buyers who tend to rely on higher loan to value mortgage products.

Mortgages

Mortgage approvals remained strong by historical standards in Q4 2021. The latest December figures for approvals for house purchase showed a 4.7% rise on November's figure and were 7% higher than the 2014-19 average. Despite this, they were significantly below the very high levels seen in Q4 2020.

December saw The Bank of England raise the base rate from 0.10% - 0.25% and this was followed by a rise to 0.5% in the first week of February 2022. While mortgage interest rates remain low in a historical context, the rises will impact first-time buyers who tend to rely on higher loan to value mortgage products. This will be combined with the impact of inflation and cost of living increases which will impact their ability to save for a deposit.

The Bank of England's Q4 credit conditions survey suggests that, while credit conditions will remain loose, scope for lenders to absorb further increases in interest rates into their margins has run out.

The survey suggested an improvement in credit availability to buyers with smaller deposits and weaker credit scores. A balance of +30.7% of lenders reported that they expect to become more willing to lend to buyers with less than a 10% deposit, suggesting concerns about a drop in house prices have eased further. This improved access to credit for more stretched borrowers will go some way to alleviating the impact of the cost of living increases and interest rate rises.

However, the narrowing in lender's interest margins now appears to have run its course. A balance of +87.9% of lenders' reported that spreads tightened in Q4 but lenders don't expect any further narrowing. This means that rising interest rates this year will feed through to the mortgage market and push up the costs of borrowing.

The London Market

QUARTERLY ANNUALISED HOUSE PRICE GROWTH LONDON

Q4 2021
4.2%

Q3 2021
7.3%

Q2 2021
4.8%

Q1 2021
6.2%

Source: Nationwide

London was the weakest performing region in Q4, although growth remained very strong compared to pre-pandemic levels. Annual growth slowed to 4.2% in Q4, down from 7.3% in the previous quarter. Homes in the capital remain by far the most expensive in the UK, roughly 60% above the outer South East – the next highest region. This is one of the reasons that price growth is slower. House prices relative to incomes are so high that buyers reliant on mortgage finance are limited in how much they can stretch borrowing to put upward pressure on pricing.

Overall we expect activity in London to remain strong relative to pre-pandemic levels. In the December RICS Residential Market Survey, new buyer enquiries in London continued to significantly out pace vendor instructions. This imbalance will help support pricing in London, even if demand were to moderate. If anything, our expectation is that demand will strengthen in the capital. We expect a sustained return to the office this year which should boost demand for urban living and relaxation of travel restrictions which will help overseas demand. The prime central markets are particularly well placed to benefit from increased ease of travel as they have a more international buyer pool. They are also less reliant on buyers using mortgage finance which leaves them less exposed to interest rate rises. Consequently, we expect prime central London to outperform the wider London market.

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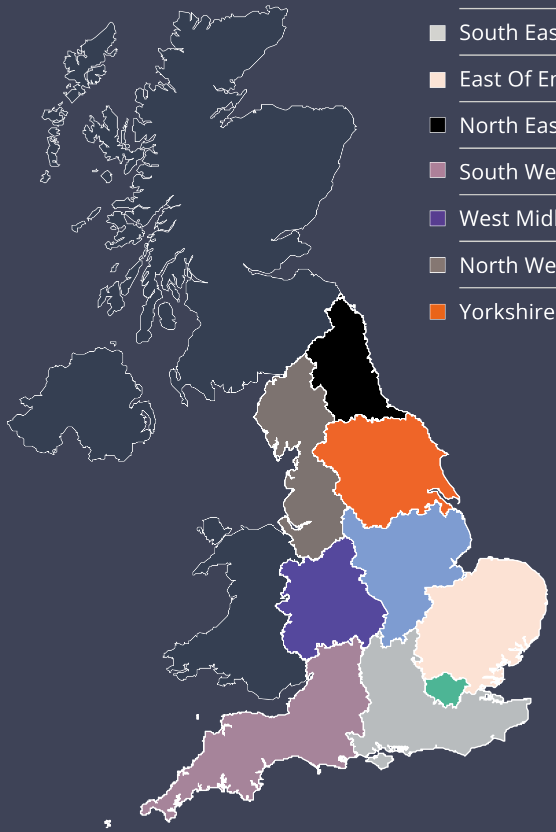
HELP TO BUY: EQUITY LOAN PRICE CAPS – APRIL 2021 TO MARCH 2023
Maximum property price

East Midlands	£261,900
Greater London	£600,000
South East	£437,600
East Of England	£407,400
North East	£186,100
South West	£349,000
West Midlands	£255,600
North West	£224,400
Yorkshire & Humber	£228,100



Source: Gov.uk

The Regional Market

In Q4 2021, Nationwide data showed continued strength in house price growth across all the UK regions. Wales saw the strongest growth of all regions at 15.8%, this marked the first time it has ended a year as the top performing UK region for house price growth.

The South West was the strongest performing English region, with annual growth of 11.5%. This was followed by the Outer South East and North West, both with growth over 11%. Growth slowed from Q3 in the North, Yorkshire & Humberside, East Midlands, West Midlands and London, although levels remained very high compared to pre-pandemic norms.

The RICS residential survey shows that surveyors in all parts of the UK expect to see continued rises in house prices over the year ahead, with expectations particularly elevated in Scotland and the South West of England (displaying net balance readings of +88% and +84% respectively). The survey also reported that surveyors in all regions apart from the North and North West saw falling vendor instructions in December, which will support pricing. Having said this, the Midlands, North West and Wales also falls in new buyer enquiries which will balance this out to some extent.

With the supply of homes coming to market so constrained, transactions volumes look set to be well below the highs seen in 2021 across all regions.

The Lettings Market

The ONS UK private housing rental index showed prices paid by tenants in the UK rose by 1.8% in the 12 months to December 2021, up from 1.7% in the 12 months to November 2021.

The East Midlands saw the highest annual growth in private rental prices (3.3%), while London saw the lowest (-0.1%). However, London saw a strong bounce back in Q4 from the rent falls seen earlier in 2021.

It is important to note that supply and demand pressures can take time to feed through to this index which reflects price changes for all private rental properties rather than only newly advertised rental properties, which may experience sharper movements.

Leading indicators, such as the RICS Residential Market Survey suggest solid growth in tenant demand right across the UK. Landlord instructions also remain thin on the ground, illustrated by 27% more respondents to the survey noting a decline compared to those citing an increase. This enduring disparity between demand and available supply on the means near term rental growth expectations rose further to post a net balance of +57% in December. Respondents to the survey expect rents to rise firmly across all parts of the UK, both at the three and twelve month horizons.

Housing Delivery

The latest figures for new housing supply were released in November 2021 which look back on the financial year 2020-21 and show that the number of net additional dwellings was 216,490, down 11% on the previous year.

It is the lowest level for 5 years and the decrease is due, in part, to the restrictions introduced during Spring 2020 in response to the COVID-19 pandemic.

Affordable homes comprised 52,100 of this figure and there were 57,417 starts on site in England in 2020-21, decreases of 12% and 16% respectively when compared to the previous year. The chart below shows the trend for different tenure components of affordable homes delivered (completions).

EPC' lodgements are one of the most timely indicators of new housing delivery and the most recent data shows that 243,775 EPCs were lodged for new homes in 2021. This represents a fall of -6.4% on the previous year but Q4 2021's figures of 61,112 was 3.3% up on Q3.

Build to Rent

Build to Rent (BTR) investment continues to be very strong, with total investment in 2021over £4.3 billion and more than half of this coming in the final quarter. There are now roughly 70,000 completed BTR units, with 42,000 under construction and about 100,000 in planning.

The relationship between the pipeline in London and the regions is increasingly changing. During the initial rise of BTR as a sector in the UK activity was very much concentrated in London. This picture has evolved and starts in London now look subdued in comparison to the regions and are failing to keep up with completions. London's pipeline has shrunk by 15% over the last year whereas the regional pipeline has risen by almost 30%. We are also seeing increased activity in the suburban single-family part of the market whereas previously the sector has been very much focussed on urban multifamily.

Overall, the growth in the sector is likely to continue to be strong, with affordability for would be first time buyers in the UK remaining stretched, meaning people are likely to stay in the rented sector longer. The investment characteristics of the sector remain attractive, particularly in an inflationary environment with rents having a long-term relationship with wage growth,

Outlook

While the 1.5m+ transactions of 2021 is very high, it still only means about 5% of our housing stock has changed hands. There is plenty of scope for additional households to take a view as longer-term work arrangements become clearer and would-be movers who held off making a decision may now be more confident.

This is one of the key reasons we expect transaction volumes and price growth to be ahead of pre-pandemic levels in 2022. Although, the shortage of homes coming to market is increasingly looking like it will act as a brake on activity. Along with this, we think there are other major factors which will help support a strong housing market.

The labour market continues to be robust and we expect inflation to peak in the first half of the year, with pressures that are driving it receding as the year progresses. This will support the economy, underpin consumer confidence and create a willingness to undertake house purchases.

Also, the market is still relatively well placed to absorb interest rate rises (based on The Bank of England's current trajectory) without significant disturbance . The monthly affordability of mortgage payments remains good by historic standards and mortgage rates would have to rise significantly to have enough of impact to derail house price growth. However, first-time buyers will be disproportionately affected as they tend to rely on higher LTV mortgages and cost of living increases will impact their ability to save for a deposit.

High house prices relative to incomes do present an obstacle for those looking to buy their first home or upsize but an alleviating factor is that the household savings build up during the pandemic has not been spent down. We expect people to continue to use savings to support larger deposits for house purchases, particularly as they are likely to be spending more time at home and therefore willing to spend more on their housing.

It is worth pointing out that it has disproportionately been more affluent households who have accrued savings, and therefore we are likely to see proportionately more activity from higher income groups. This has been one of the stories over the last year and while activity from all types of purchaser has increased, first time buyer activity has increased less than that of home movers or cash buyers. This will help support demand for rental property as would-be first time buyers remain in the sector longer to raise enough money for deposits

Upward pressure on prices from people being able to stretch mortgage lending is greatest in the regions where the house price to income ratio is lowest. These are the regions that have seen the strongest growth this year (Wales and the North) and we expect this trend to continue next year. This is typical of previous housing market cycles, where London recovers first and strongest and the regions recover later.

This has been particularly pronounced in this cycle and because house prices relative to incomes are now so high in London, this will act as constraint on growth in the capital next year. Although wage growth will go some way to alleviating this. Overall, we expect London to underperform relative to other regions, as it has this year, although it will experience some benefit from a return in appetite as people rediscover the agglomeration of benefits of the city.

As with house prices, rental growth has been very strong in 2021, with rental growth outside London is at its highest level since before the GFC. London had been the exception to the growth story but all indicators are now pointing a strong recovery in the capital and notably the RICS residential survey points to expectations of strong rental growth across all regions.

The strong rental market will help underpin confidence in the Build to Rent sector which has had a strong year in terms of investment volumes , despite the pandemic uncertainty and concerns about city centre living. There have also been a number of high profile new entrants to the sector with ambitious targets, including John Lewis and Lloyds. Along with the existing capital chasing the sector, this will mean opportunities are closely contested and we expect to see yield compression in London and prime regional locations.

Should you wish to discuss any details within this update please get in touch

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