INSIGHT

Housing Market Summary

Quarterly update of housing market activity

Q3 2021

AVISON YOUNG

Overview

- House price growth in the UK remained strong in Q3 despite the initial tapering of the Stamp Duty Land Tax (SDLT) holiday at the end of June. Nationwide reported 10.3% year on year growth in the quarter, the same as in Q2. This puts the average UK house price at £248,742, compared to £226,129 at the same time last year.
- Transactional activity has also remained strong, despite a dip in July following the tapering of the SDLT holiday. The most recent figures for August show 98,300 transactions, 20.8% higher than the same time last year and a 32% rebound from July's figures. 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 the final quarter of the year, the latest RICS Residential Market Survey and internet searches suggest buyer demand ticked up in September having receded over the previous two months. 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 0.1% month-on-month increase in September, down from 2.0% in August. This brought the annualised growth rate to 10%.

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 8% in July, down from 13.1% in June. Zoopla reported slightly lower but still strong figures, with annualised growth in September at 6.1% 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 be set against a limited and diminishing pool of supply, ensuring competition between buyers remains intense. This imbalance will help maintain upward pressure on pricing even as the stimulus of the Stamp Duty Holiday is tapered from the market.

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.

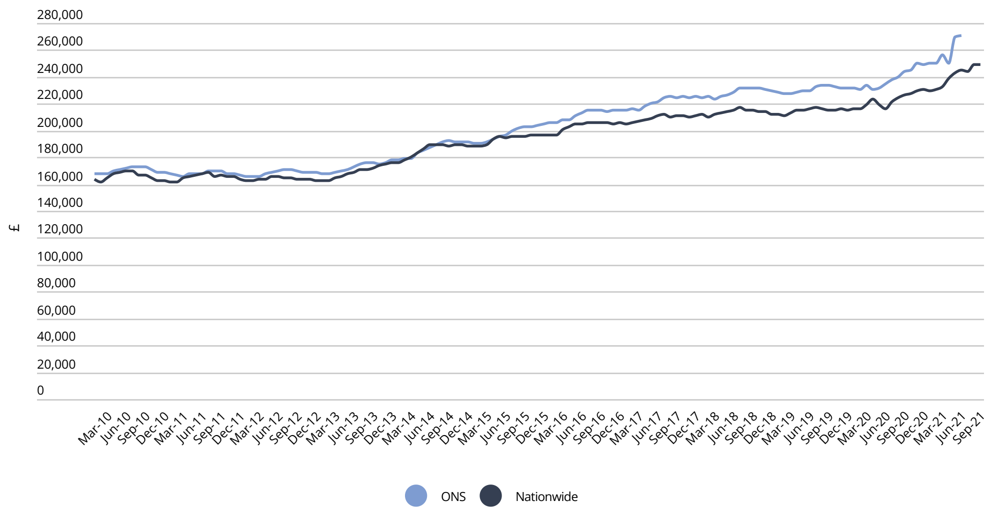
From April 2021, only first-time buyers will be eligible for the scheme rather than all home buyers. The previous price cap is being replaced by significantly lower regional price caps, defined as 1.5 times the average price of a first-time buyer property for each region. While the original version of 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.

> "
> **The economic backdrop, low mortgage rates and a continuation of demand resulting from reassessment of housing needs will support continued house price growth and transaction levels.**

Data

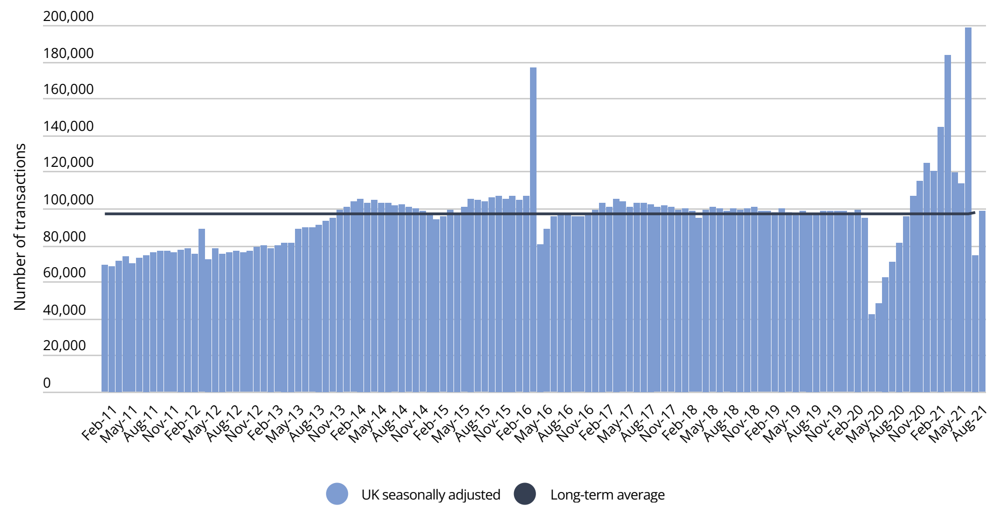
UK HOUSE PRICES INDICES

Source: Land Registry, Nationwide



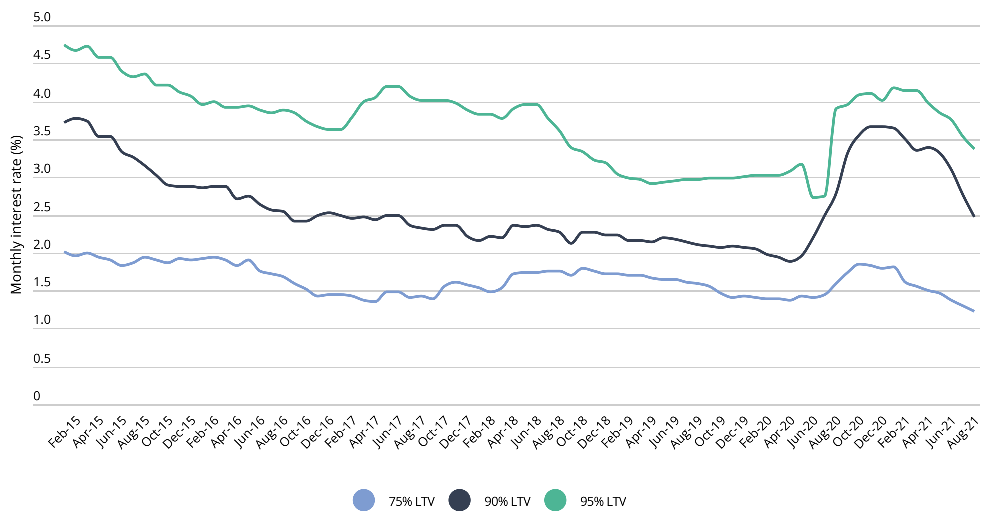
HOUSING TRANSACTIONS IN THE UK

Source: HMRC



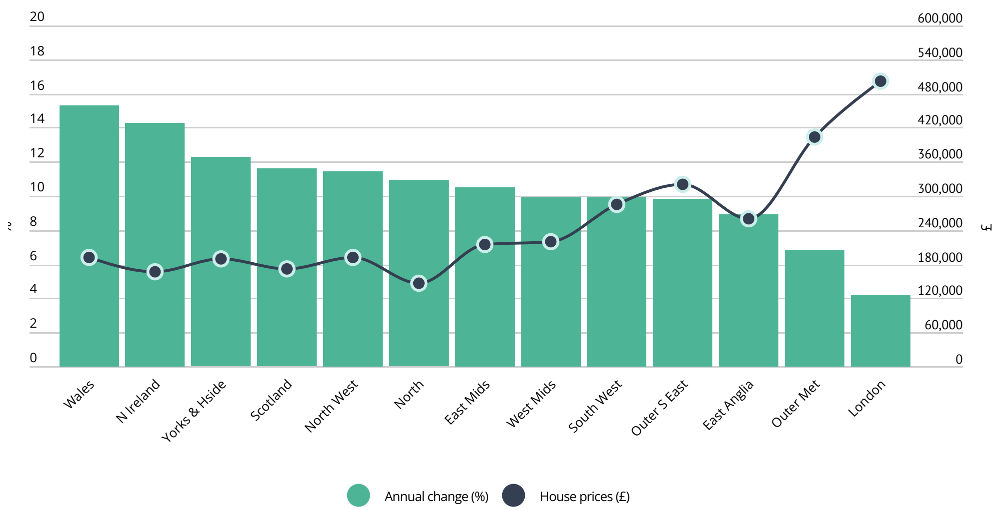
INTEREST RATE ON 2-YEAR FIXED MORTGAGES

Source: Bank of England



REGIONAL HOUSE PRICES & ANNUAL GROWTH - Q3 2021

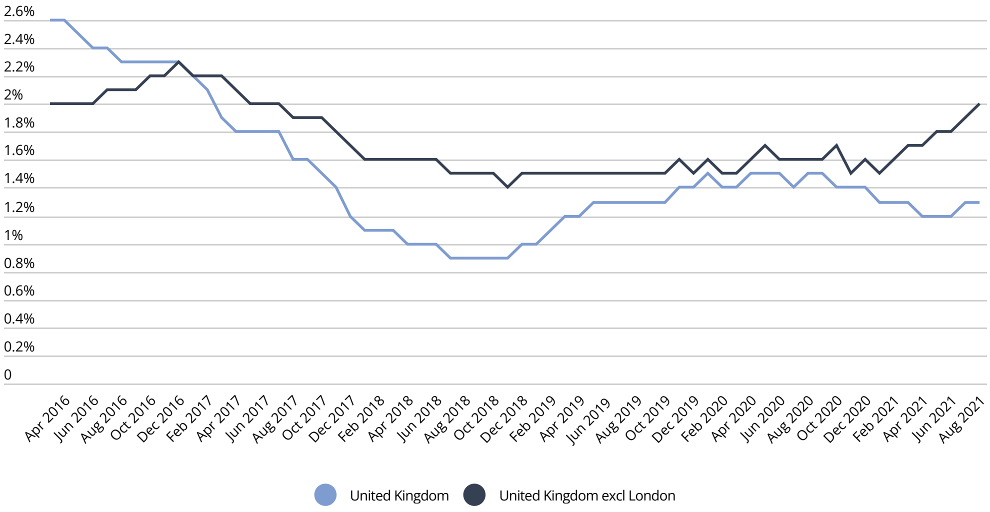
Source: Nationwide



Data

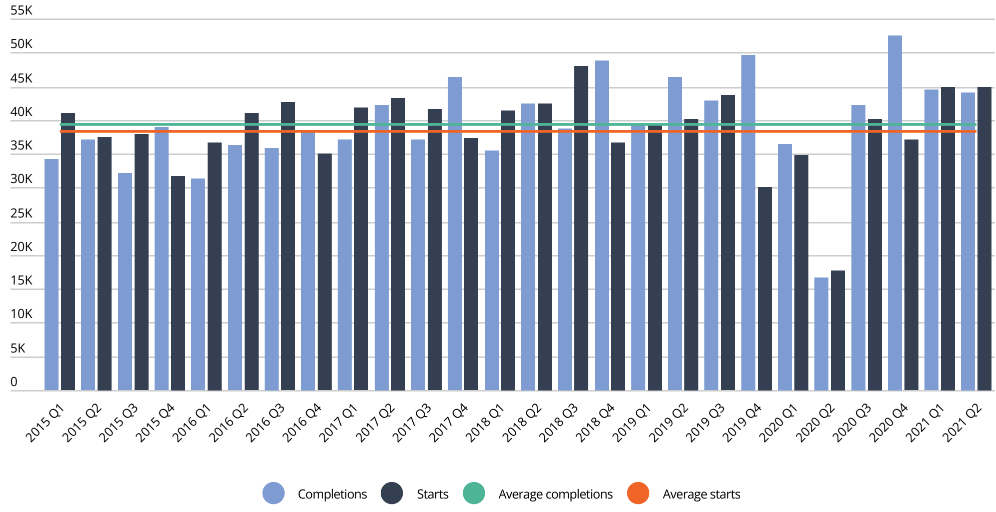
ANNUAL PRIVATE RENTAL GROWTH

Source: ONS



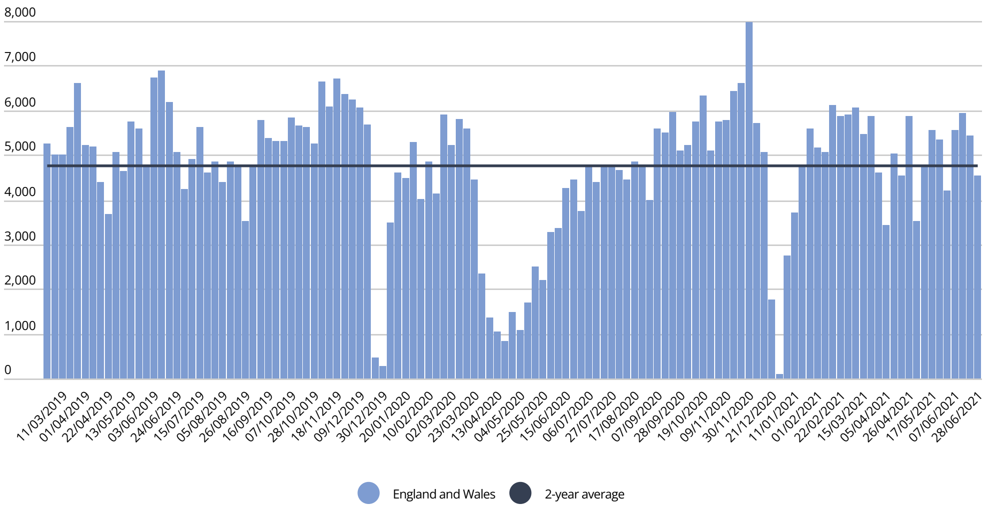
QUARTERLY PERMENANT DWELLING STARTS AND COMPLETIONS IN ENGLAND

Source: MHCLG



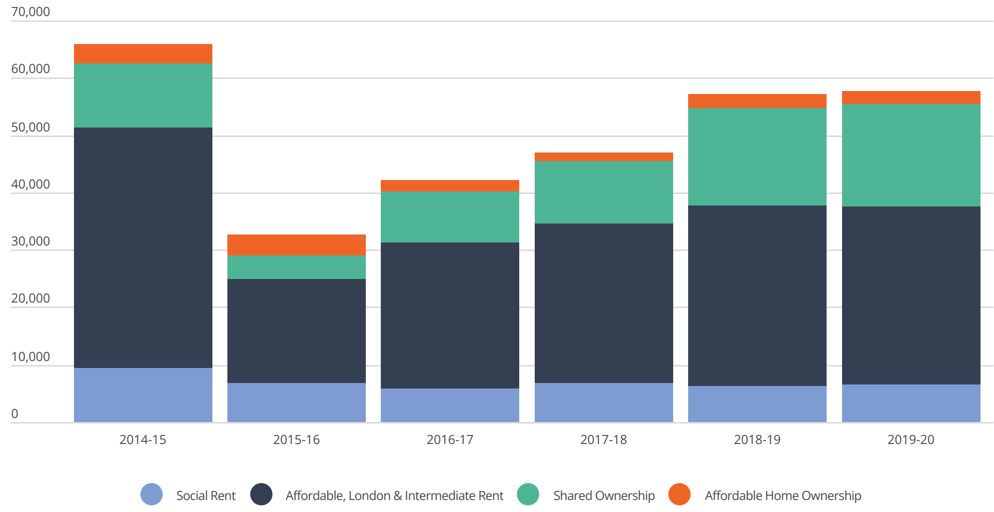
WEEKLY EPC LODGEMENTS FOR NEW DWELLINGS IN ENGLAND AND WALES

Source: MHCLG



AFFORDABLE HOME COMPLETIONS BY TENURE IN ENGLAND

Source: MHCLG



INTEREST ON 2-YEAR FIXED RATE MORTGAGES

August 2021

Mortgages

Mortgage approvals continued to cool in July, falling from 80,272 to 75,152, although they remain higher than the 2019 average of 65,000.

There are some nuances in the mortgage market between different types of products. The economic fallout from Covid-19 spurred lenders into placing greater scrutiny on mortgage requirements, including reducing the availability of high Loan to Value (LTV) mortgages. Analysis of interest rates on 2-year fixed mortgages show that high LTV borrowers also experienced a disproportionate rise in borrowing costs over 2020 as lenders became more risk averse.

High LTV mortgages are most common among first-time buyers and are a crucial product for helping people get on the housing ladder. While FCA data shows mortgage completions by first time buyers had recovered at a similar rate to mortgaged movers in the summer and autumn of 2020, since Nov 2020, their numbers have stayed high but not experienced the further growth seen by mortgage movers.

Analysis of average quoted rates in September shows that this situation is beginning to improve with rates falling across all high LTV mortgages, reflecting the improved economic environment and increased risk tolerance from lenders.

> **"Analysis of average quoted rates in September shows that this situation is beginning to improve with rates falling across all high LTV mortgages, reflecting the improved economic environment and increased risk tolerance from lenders.**

QUARTERLY ANNUALISED HOUSE PRICE GROWTH LONDON

Q3 2021
4.2%

Q2 2021
7.3%

Q1 2021
4.8%

Q4 2020
6.2%

Source: Nationwide

The London Market

London was the weakest performing region in Q3, with annual growth slowing to 4.2% from 7.3% last quarter. It is important to point out that this level of growth remains strong and much higher than pre-pandemic levels. Homes in the capital remain by far the most expensive in the UK, roughly 60% above the outer South East – the next highest region.

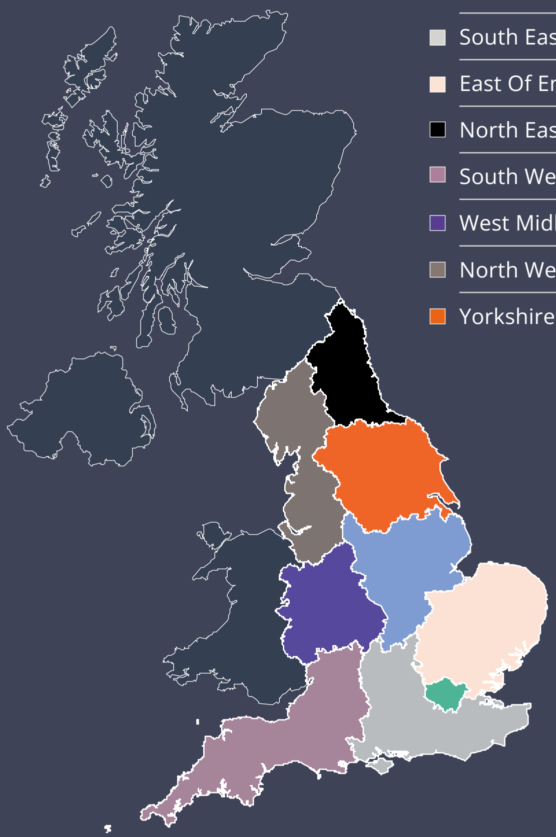
In the September RICS Residential Market Survey, new buyer enquiries in London were the third highest of all regions and sales expectations from surveyors were the second highest. This suggests that with more people returning to the office and London having been fully 're-open' for a sustained period, it maybe experiencing an uptick in demand relative to other areas. As with the wider nation, there are signs a significant shortfall of supply relative to demand has emerged in London. The net balance for new instructions remains low and has seen six months of decline. This imbalance will help support pricing in London, even if demand were to moderate.

> "In the September RICS Residential Market Survey, new buyer enquiries in London were the third highest of all regions and sales expectations from surveyors were the second highest.

The Regional Market

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

In Q3 2021, Nationwide data showed continued strength in house price growth across all the UK regions, although all regions other than Wales, Northern Ireland and Scotland recorded a slowdown. Wales and Northern Ireland were the strongest performing regions at 15.3% and 14.3% respectively.

In England, Yorkshire & Humberside was the strongest performing region for the second quarter running, with price growth at 12.3% year-on-year. This was followed by the North West at 11.4%, the East and West Midlands saw 10.5% and 9.9% respectively. London was the weakest performing English region with its surrounding areas all also seeing slowdowns.

The RICS residential survey shows that all regions except the North have falling vendor instructions which suggests the supply and demand imbalance we referred to previously will continue. The survey also reported that over the next three months, surveyors in all regions anticipate growth in house prices.

Changes to the Help to Buy scheme may result in challenges in some regional markets as the new regional price caps will have the greatest impact in high value regional markets. This is because the caps reflects average prices across regions, so markets such as Bath, Cambridge, Winchester and York where average prices are much higher than regional levels are exposed. Housebuilders in these markets will have to adapt their product/pricing to be able to viably deliver homes eligible for the scheme.

The Lettings Market

The ONS UK private housing rental index showed that the price paid by tenants increased by 1.3% in the 12 months to August 2021, a similar level to the previous month. The East Midlands saw the highest annual growth in private rental prices (2.7%), while London saw the lowest (-0.4%).

Supply and demand pressures can take time to feed through to this index as it reflects price changes for all private rental properties rather than only newly advertised rental properties. Other measures, which track newly advertised properties have reported much sharper price movements.

Zoopla's Rental Index is one of these and their most recent report (Q2) reported that UK rents (excluding London) were up 5% year on year and that London rents were down 3.8%.

Leading indicators suggest that London rents have now snapped firmly into recovery mode. Responses to the RICS survey show London has had the third highest level of tenant demand over the last three months with the net balance of new landlord instructions remaining negative. Surveyors also reported positive rental growth expectations over the three and 12 month horizons.

Respondents for all other regions reported positive rental growth expectations for the next quarter with a consistent theme of strong new tenant demand but weak levels of new landlord instructions.

The above sentiment indicators suggest that demand is outweighing supply in most of the UK markets, placing upward pressure on rents. This narrative is echoed in the 12-month outlook for rents in the RICS survey, with all regions anticipating growth.

Housing Delivery

Seasonally adjusted new build dwelling starts in England are estimated at 42,900 for Q2 2021 (most recent data), this represents a 5% decrease on the previous quarter and the first quarterly fall since restrictions were lifted on building activity.

Compared to the same time this starts this quarter are up by 150% but this increase is an anomaly reflecting the restrictions on construction last year. The number of starts are 12% per cent below their 2007 peak and while they paint an encouraging picture of post Covid recovery are still well below where they would need to be if we are to continue to push toward the government's 300,000 homes a year target.

Completions have also recovered well and government figures put them at 43,660 (seasonally adjusted) for Q2 2021, a 10% fall on the previous quarter and 167% up on the same time last year. As with starts, this quarter represents the first time completions have fallen since restrictions on construction activity were lifted.

The total number of affordable homes completed for 2019-20 – the latest available figure – stands at circa 57,6400, a 0.8% increase on the previous year and the highest annual figure since 2014-15. Of these, the MHCLG reports that 6,570 socially rented homes, 30,950 affordable rented homes (including London and intermediate affordable rents), 18,000 shared ownership homes and 2,080 affordable ownership homes were completed.

The changes to the planning system introduced at the end of summer 2020 by the government will impact development trends, particularly relating to the conversions of vacant retail property into residential units. Such moves would no longer require planning permission from the local authority under the new changes which are likely to have significant repercussions across the whole UK property market, including the housing sector.

Changes to the Help to Buy scheme will also impact developments, particularly those specifically targeting first-time buyers. The regional price caps may mean that some potential developments may need to be considerably altered to either reduce the initial asking prices of properties or look at other arrangements such as moving to a build to rent model.

Build to Rent

Build to Rent (BTR) investments increased 30% year-on-year in 2020, totalling some £3.5 billion despite the pandemic. There are roughly 53,000 BTR units under construction with a further 89,000 in planning – a figure which continues to rise.

The growth in the sector is likely to continue, with BTR investors providing an attractive exit opportunity for house builders in the current market. We expect to see an increase of bulk sales to investors, bringing certainty and reducing risk for the vendor. In general, we expect the sector to see strong interest as its lower cyclical volatility and strong demand profile make it appealing to funds and institutions looking for long-run returns.

Evidence from the mortgage market suggests that it is going to remain challenging for would be first-time buyers to access mortgage finance. This is partly due to the sheer volume of mortgage applications which is having the effect that lenders are focussing on low-risk lending. This means people will remain in the rented sector longer, supporting demand. Once the stamp duty holiday finishes it is also very possible renters will delay buying a home in the face of economic uncertainty, as we have seen previously, lending further support to rents and the BTR market.

Further, house prices have shown considerable strength throughout the course of the pandemic while wages have been less robust. The affordability of homes has therefore fallen in the past year, compounding the appeal of the private rental sector and, by extension, the BTR market.

Outlook

As the pandemic set in last year, you would have been hard pressed to find anyone who thought it would set off a housing boom. However, the market has been remarkably strong and despite the end of the SDLT holiday, activity and price growth look like they will remain elevated relative to pre-pandemic levels.

Fundamentally, this will be underpinned by the economic backdrop, low mortgage rates and a continuation of some of the factors that have led to people re-evaluating their housing needs over the last year.

From the economic perspective, our successful vaccine rollout, opening-up of the economy and consumer spending has led to a faster and fuller recovery than most expected.

This means the outlook for people's ability and willingness to undertake buying a home is positive, it also feeds through to mortgage rates, encouraging banks to relax lending conditions.

Also, because interest rates are still very low, mortgage affordability remains good by long term standards. This means despite house prices being at all time highs relative to incomes, monthly mortgage payments remain affordable. The current level of inflation has attracted attention and may lead to sooner than previously expected interest rate rises but we do no expect this to substantially impact the cost of mortgage finance based on current predictions.

The other key driver in the market has been the reassessment of housing preferences, driven by the pandemic working and living experience. This is illustrated by the fact that the majority of house purchases over the last six months have been home-movers. Prior to the pandemic, first time buyers were the majority. As longer-term working arrangements become clear as we emerge from the pandemic, it is likely there will be a continuation of this theme which along with the economic factors will support robust market activity and pricing.

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

Joshua Rose-Nokes
Associate Director, UK Insight
+44 (0)20 7911 2566
joshua.rose-nokes@avisonyoung.com

Kiran Patel
Insight Analyst
+44 (0)20 7911 2625
kiran.patel@avisonyoung.com