July/August 2017

MARKET INSIGHT

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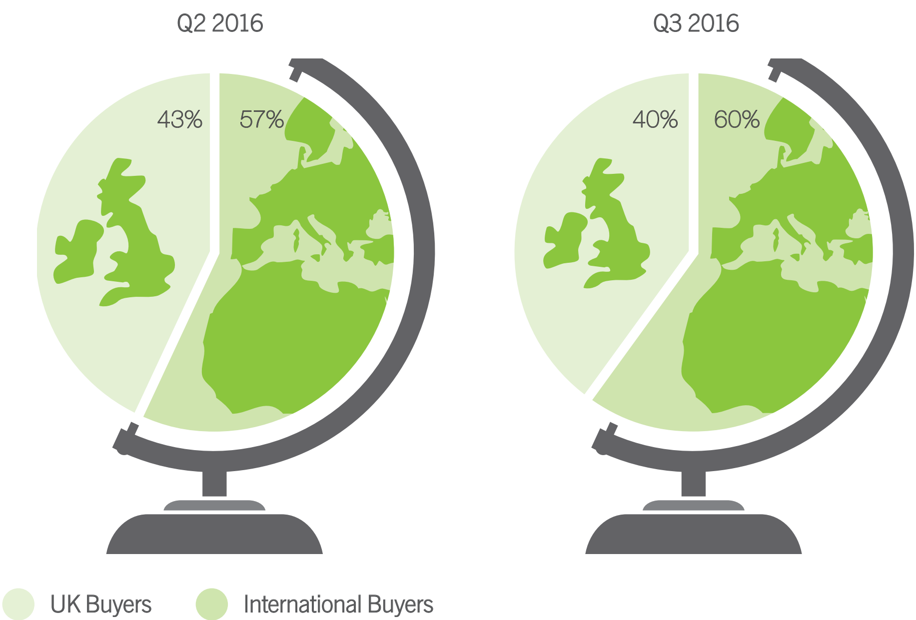
Focus

International buyers return to Prime Central London

The property market tends to reflect the overall health of the economy and sometimes its appeal is measured not by the interest of its nationals, but by foreign buyers. Over the last year swings in the housing market and uncertainty over the future of the economy have caused fluctuations in the currency. That affects the price of property and affects where international buyers decide to buy homes.

Historically Prime Central London (PCL) was where international buyers chose to invest. They accounted for nearly three out of five buyers in PCL in Q2 2016. However, a combination of the EU referendum, higher stamp duty rates and a generalised perception of prices peaking in London's most expensive parts has pushed international buyers to look further afield. The proportion of international buyers in PCL nearly halved between Q3 2016 and Q4 2016, from 60% of buyers to 33%.

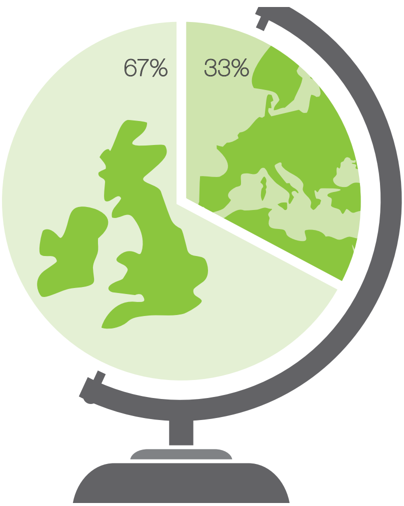
Proportion of international buyers in Prime Central London



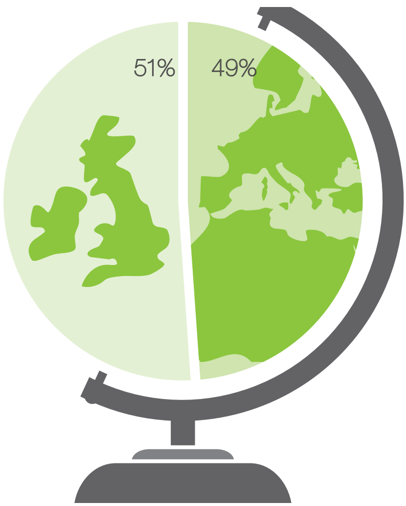
Instead, international buyers sought more affordable areas in the suburbs and 'super-burbs', including places like Hampstead, Richmond and Esher. Despite the currency advantage due to the depreciation of the pound, overseas buyers started looking for property where there was greater likelihood of price growth, rather than homes in the most expensive areas where prices are falling. This was particularly noticeable among European buyers who accounted for 11% of buyers in the suburbs and 'super-burbs' in Q3 2016, up from 6% in Q2 2016.

But after a year of uncertainty, international buyers are starting to return to Prime Central London. Their purchases accounted for one third of sales in the capital in Q1 2017 up from 22% in Q4 2016 – nearly reaching pre-referendum levels. This reflects a combination of vendors' price expectations getting more realistic and confidence in London as a popular and stable safe haven.

Q4 2016



Q1 2017



Source: Countrywide Research

Economy

Life is full of surprises

June is certainly a month of surprises. First the election result, which confounded the pollsters until the last moment. At 10pm on 8 June the exit polls predicted the government to lose its majority – a shock to most pundits and certainly to the politicians.

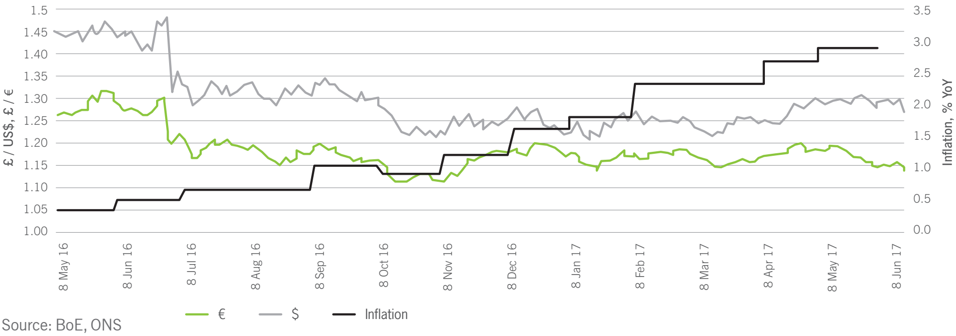
However, the markets took the news relatively well. Sterling fell by 2% but the FTSE was largely unmoved. The first is not good news for the UK economy – a further fall in the currency means that the cost of imported goods increases. The UK is a very open economy and much of our household spending is on imported goods. In addition manufacturers can't cut back on overseas components for their goods and home builders need to import bricks and raw materials too. The upside is that UK exporters are having a field day since their prices can be lower abroad, hence boosting competitiveness or, even if they stay the same, earnings in sterling are higher.

The impact of the falling pound on inflation cannot be ignored. The latest data shows inflation rose to 2.9% in May, the highest level for nearly four years. As the pound has fallen, the inflation rate has picked up – though it's picking up across the Eurozone too.

The usual outcome would be for interest rates to begin to rise, after all inflation is now almost one percentage point above its target. But at the latest Monetary Policy Committee meeting there was still little appetite to begin to increase interest rates. Three members voted for an increase, beaten by the remaining five content to continue to look through this increase in inflation because it is led by currency issues rather than over exuberant demand. But this could change next month given Andy Haldane's, the Bank's Chief Economist, remark that he nearly opposed the Governor by voting for a rise in June.

Negotiations on the UK's terms for leaving the EU have now got underway. The change in the balance of power in Parliament may mean that Brexit will turn out to be softer than it would have been. That would be welcomed by the business community, and boost confidence. There are hurdles and undoubtedly more surprises ahead, but beginning to take the Brexit path with a more flexible approach might mean a shorter and less painful period of adjustment to a life outside the EU for the UK economy.

Inflation and exchange rates



Source: BoE, ONS

Sales

Hanging around

The election left us with a hung parliament, but politicians aren't the only ones hanging around. While activity in the UK housing market has picked up since the financial crash, more buyers and sellers are choosing to stay put than in the years before 2007.

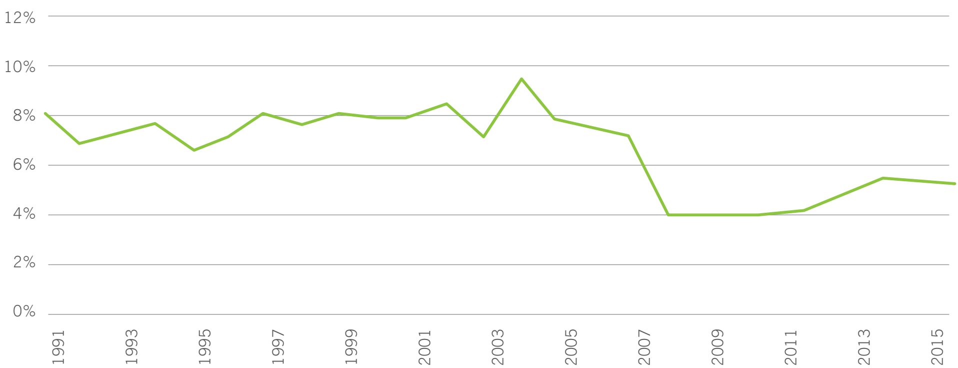
The turnover rate (homes sold as a proportion of the total housing stock) is close to two thirds of its long run average of 8%. This collapse in activity was initially driven by a lack of credit, but as conditions have improved activity has not followed. Affordability has been an issue for first time buyers, but the real key is the absence of movers combined with the growth of the private rented sector. First time buyers are the biggest pool of potential buyers by far – and the ones that can just hang around.

But are things going to change? It seems likely that the levels of activity we are experiencing now and expect to see in the next one to two years is the baseline level of activity reflecting a need rather than a desire to move. On the upside, the longer that movers have stayed out of the market, the greater the potential for pent up demand, which could begin to flow through.

Weaker house price growth could also be a catalyst for both buyers and sellers to come to market. Expectations of house price growth have weakened in almost every part of the country, which should encourage more negotiation and hence more deals to be struck.

While sellers may be worried that the value of their home may fall, the context paints a much more optimistic picture. Prices today are 5.6% higher than this time last year – significantly more than inflation at 2.9%. In London they are 4.7% higher. Even if house prices in London fell by 1.5% in 2017 as we expect, they will still be about the same level as in April 2016. Since people typically move only every 15 years, that's a large increase in equity to help make the negotiation pill sweeter to swallow.

Turnover rate, England



Source: HMRC, DCLG

Lettings

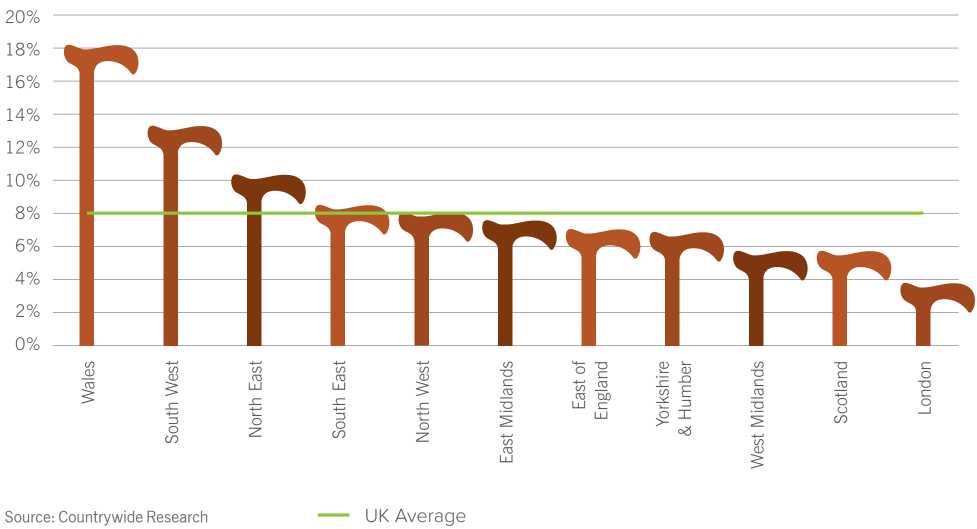
Retirees spend a record £3.7bn paying rent

The rental market can no longer be characterised by the image of carefree, young professionals. More than half of tenants are over 30 and the number of pensioners renting has reached record levels. Over the last 12 months people who have retired paid a total of £3.7bn in rent, up 216% from the £1.2bn they paid in 2007. This increase means that £1 in every £14 paid by tenants in Great Britain now comes from a pensioner. The total amount of rent paid by private tenants in Great Britain over the last 12 months stood at £50.6bn.

With younger generations growing up much less likely to be homeowners, tenants are getting older, increasing the size of the private rental sector. Retired people now account for 8.0% of all tenants, compared with 5.2% in 2007. The largest proportion is in Wales, where nearly one in five tenants are retired. The South West and North East have the second and third largest proportion of retired tenants respectively. London, where just 3.5% of tenants are retired, has the fewest. Across Great Britain as a whole 53% of tenant pensioners live alone and 81% are over the age of 65.

Retirees paid 12% less in rent than the typical tenant – an average of £810 a month in 2017. This is because they were more likely to rent a smaller home better suited to their needs. As a result, retirees tend to make up a greater proportion of tenants in the places where rents are lowest. With more of the younger generation unable to afford to buy a home, we are likely to see this trend continue.

Inflation and exchange rates



Source: Countrywide Research

Stat of the Month

Mortgage markets

Mortgage approvals in Q1 2017 were broadly stable compared with Q4 2016, and only 1% lower than a year earlier. The relatively small fall in approvals given the change in stamp duty is explained by timing and by the large proportion of cash sales to beat the SDLT surcharge.

The availability of credit is a positive factor for mortgage lending, but volumes are driven by demand, which will be affected by tighter household budgets.

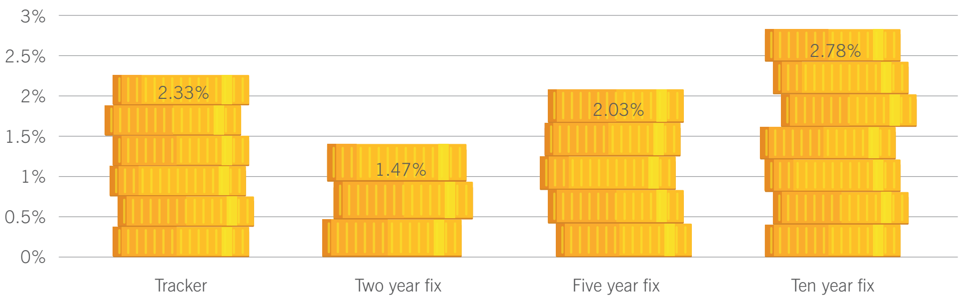
Mortgage Approvals

Source: Bank of England

The likelihood of an early increase in interest rates is small as the Bank of England are keen to keep the economy stable. We do not expect any change in the Bank of England base rate until 2018.

Current average mortgage interest rates

Source: CML



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