May 2017

MARKET INSIGHT

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Focus

Quick on the Draw

Mrs May seems to have become a bit trigger happy! After the serving of Article 50 in March, she went on to call a snap General Election in April to be held on the 8th of June.

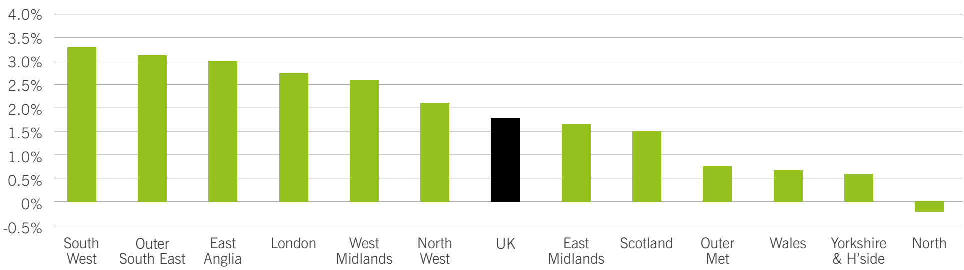
In previous elections, the housing market has been affected by the uncertainty. Analysis of nine general elections between 1979 to 2014 shows that there tends to be a slowdown in activity in the run up to election day followed by a bounce back afterwards. But this time there are less than 50 days until the vote, so there isn't enough time for political uncertainty to have a big impact on the housing market. Furthermore, it seems highly unlikely that the Conservative Party will lose power, indeed it is expected to increase its majority.

Speculation as to why Mrs May changed her mind seems to rest on giving her greater power in Parliament regarding policies on Brexit. If that is the case and she gains seats, that could actually reduce uncertainty – about the negotiations at least.

Whatever the outcome of the election, the effect of Brexit on the housing market is limited in the short term. Most demand is domestically driven and

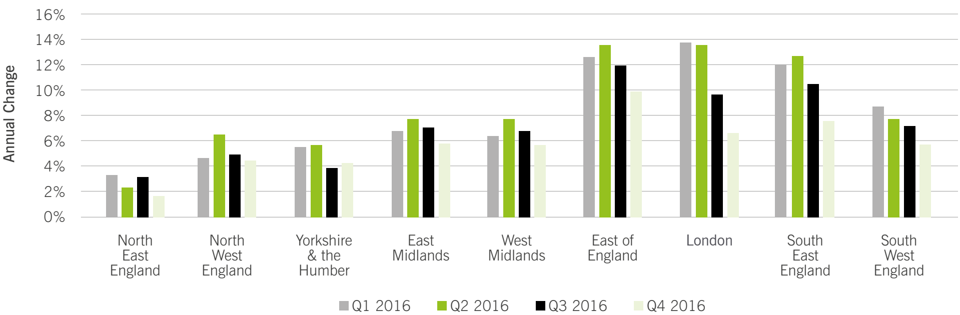
Price growth since referendum

Source: Nationwide



House prices still rising

Source: ONS



international buyers are still benefitting from a weaker sterling, which cushions them from any risk of a fall in prices.

So far, they've done quite well as prices have continued to rise since the referendum result – despite the previous Chancellor's warning that house prices could collapse by up to 18% over the next two years, which now seem very wide of the mark.

"Analysis of nine general elections between 1979 to 2014 shows that there tends to be a slowdown in activity in the run up to election day followed by a bounce back afterwards."

But looking ahead the picture could be different. How much will depend on how negotiations affect the UK's economic performance – particularly jobs. In the worst case scenario, investors could lose confidence in the UK's ability to thrive outside of the EU. That could hit sterling, which would help exports, but would make it more difficult for most households who would face higher prices.

Interest rates and the labour market are the most important drivers of the housing market's fortunes, so if uncertainty affects investment in jobs and interest rates increase, households will struggle to meet their mortgage payments causing an increase in forced sales and falls in house prices.

That is a worst-case scenario. If the economy is in the doldrums, it's unlikely that the BoE would consider an early rise in rates – that would be unsettling and could crush households and businesses at just the time we need them to spend and invest. The Bank has form on looking through inflation targets to the general health of the economy.

Investors too may take a longer-term view about the UK's performance. In the short term there may be uncomfortable adjustments, but in the medium to longer term the UK could become a less regulated and hence a more flexible economy, able to respond more swiftly to changing conditions. That would give it an advantage and help boost potential growth.

While we can be fairly sure of the result of the election, nobody yet knows how the Brexit negotiations will go. It seems most likely that in the short-term uncertainty and transition costs of leaving the EU will dampen the pace of the UK's economic growth and cause some wobbles in the financial markets. But in the medium to long term, the economy will find its way. It may ultimately be smaller than it would have been had the UK remained in the EU, but it does not mean that it will fall into recession. Nor that the UK, currently the fourth largest economy in the G7 will suddenly fall into the lower ranks of developed economies.

Economy

There may be trouble ahead...

The UK's labour market has been a real success story since the financial crash. Employment levels have risen and unemployment has fallen, despite more and more people becoming available for work[1]. That's all great news, so what's the trouble?

The answer is that while more people are in work, they aren't earning a lot. Average wage growth in 2006 was 4.7% but in 2016 it was just 2.6%. And on top of that inflation is beginning to eat into the amount that households have left to spend on themselves, or indeed on buying or saving up for a new home. For five years from 2009 to 2013, inflation adjusted earnings fell, before turning modestly positive in the last three years.

But the cost of essentials have risen faster than the general rate of inflation. Consumer price inflation reached 1.2% in Q4 2016, but inflation on transport was 2.9% and utilities 1.9%. Average annual wage growth was 2.6% in Q4 2016, higher than it has been, but not large enough to leave households better off in the face of the rising costs of essentials.

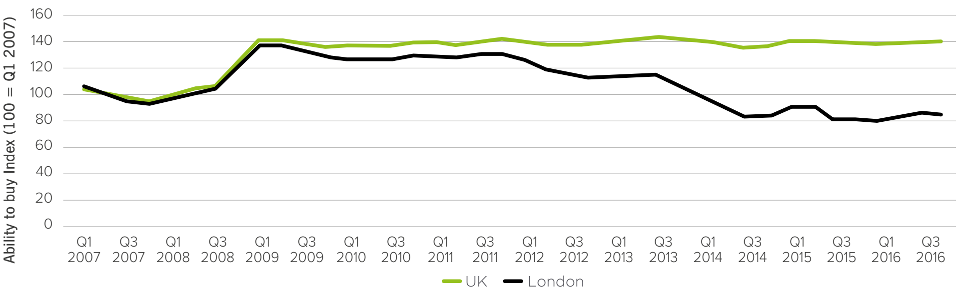
…but where there's slower price growth, low mortgage rates and keen lenders…

Combining the squeeze in incomes, the rise in the cost of living and higher house prices leaves households in a sticky place. But the big fall in mortgage rates is a relief meaning that average ability to buy has been fairly stable since 2009 – except in London where ability to buy now is worse than it was in 2007.

The upside is that mortgage lenders are keen to lend, mortgage rates are becoming more competitive and the pace of house price growth is waning. These add up to a less bad, if not rosy, scenario for ability to buy. So, we can face the music and dance.

Shifting affordability - ability to buy

Source: Countrywide Research



[1]Unemployment rates can change, not just because of the numbers of people who are out of work but also changes in the numbers of people who want to work. E.g. if the workforce was 100 and five people were out of work, the unemployment rates is 5%. But if 20 people come out of retirement, the workforce goes up to 120. With five people out of work, the unemployment rate falls to 4%

Sales

New build premium

The ability of a house builder to charge a premium for a house typically comes from a combination of three things; that it's ready to move into, carries a guarantee and has been designed and built for 21st century life. The size of the premium varies by the location of the home, who built it, how it was built and the specification of the development itself. Last year the average new home sold for 17% more than a comparable second-hand one, up from 15% a decade ago.

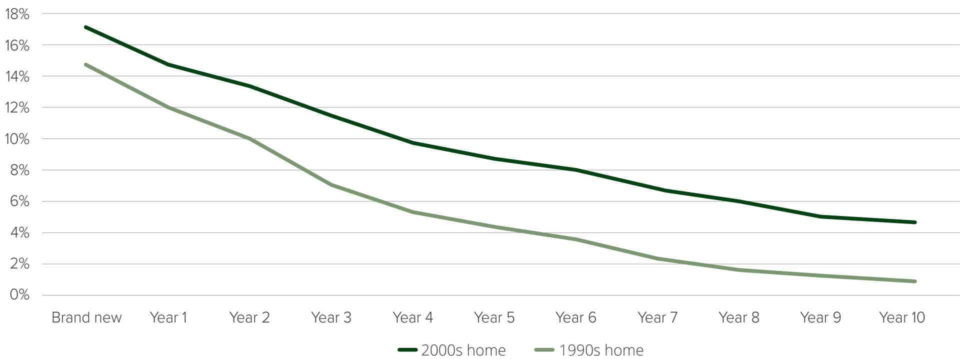
But what happens when a new home is no longer new? The average person who sold their new home for the first time in 2017 had bought it brand new from the developer seven years ago. How much of a premium the home can still command when it's no longer brand new depends on how both the property and the wider development have aged.

When the average new home is sold on for the first time it commands around half of the premium it did when it was sold as new. The premium a new home can command five, ten or even twenty years after being built depends on the builder, the buyer and, in some cases, the managing agent. Around a quarter of new homes, generally the very best developments, are able to hold on to their premium for life. Other schemes however see their premium eroded within the first seven years, the average time someone owns a new build home. But for most new homes, the answer lies somewhere in the middle.

But while the length of time a premium lasts varies, in general developers are getting better at building homes that hold onto their premium for longer. The average noughties new build holds onto twice as much of its premium compared to a home built in the nineties. For someone wondering what their new home will look like when it's ten years old could do worse than looking at one built by the same builder ten years ago.

Erosion of new build premium

Source: Countrywide Research



Lettings

Company landlords reach record high

One in five homes let are owned by a company landlord. The proportion of homes let by a company landlord reached 20% in Q1 2017, the highest proportion since records began in 2010 according to the Countrywide Lettings Index. The numbers have been steadily rising since 2013, but Q1 2017 recorded the biggest annual jump (6%). Changes to tax relief on rental properties, announced by the former Chancellor in the 2015 Spring Budget may be behind the rise.

The changes, being tapered in over a four-year period beginning on 6th April 2017, reduce the tax relief landlords are able to claim to the basic tax rate of 20%. It's the landlords with a highly-mortgaged property portfolio who will be most affected by these changes.

Companies are generally taxed more favourably which means that landlords can typically save more by holding their buy to let properties in a company rather than as an individual.

Landlords letting homes in London are most likely to own their property using a company name. 27% of properties let in London are owned by a company, a larger proportion than anywhere else. Company landlord lets drive the top and bottom of the rental market with the most and least expensive homes likely to be owned by a company landlord. Over the last year, a quarter of homes let by a company landlord cost less than £500 PCM. Nearly one in ten homes (9%) let for between £1500 and £2000 PCM were owned by a company landlord, compared to 6% owned by non-company landlords.

Proportion of homes let by a company landlord by region - Jan 2016 – Mar 2017	
London	27%
Yorkshire and the Humber	17%
East of England	12%
East Midlands	12%
South East England	12%
South West England	10%
North East England	8%
West Midlands	7%
North West England	6%
Scotland	4%
Wales	3%

Source: Countrywide Research

Stat of the Month

Annual house price growth by local authority

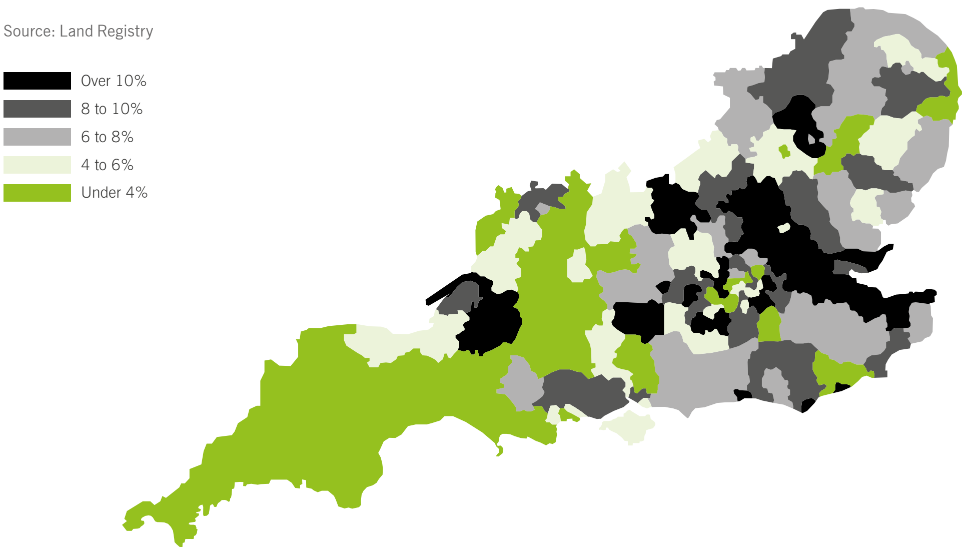
Top five for fastest price growth

Area	Region	Annual price growth	Average price
Hertsmere	East of England	19.5%	£561,610
Brentwood	East of England	18.6%	£486,620
Barking and Dagenham	London	17.7%	£285,610
Bexley	London	17.6%	£345,181
Basildon	East of England	17.1%	£307,836

Bottom five for fastest price growth

Area	Region	Annual price growth	Average price
Mid Devon	South West	-0.3%	£228,935
Tandridge	South East	-0.3%	£451,976
City of Westminster	London	-0.4%	£1,564,960
Hammersmith & Fulham	London	-1.5%	£992,158
Runnymede	South East	-3.3%	£445,483

Source: Land Registry



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