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MARKET INSIGHT

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Focus

Ahoy there! Calm seas, choppy waters, but risk of storms

There is no doubt that the UK will launch into uncharted waters as it leaves EU membership. As it begins to navigate the open seas, there will be choppy times ahead as consumers and businesses try to assess the implications. Confidence will rise and fall along the way, but assuming a relatively smooth transition, the prospects for the economy and its housing market are respectable.

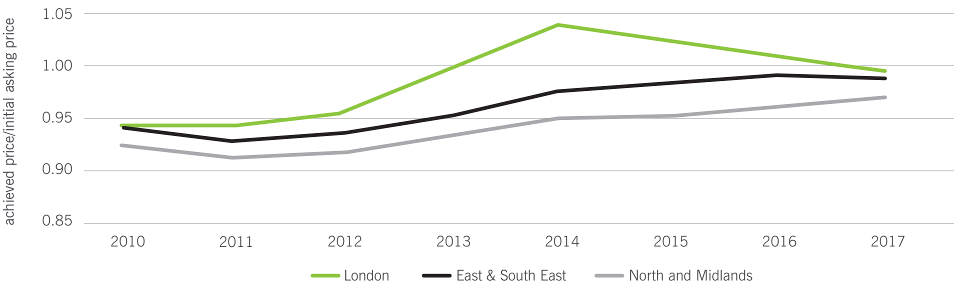
The biggest issue for home buyers and renters is the effect of currency driven inflation on their household budgets. With prices rising faster than earnings, spending power is falling. Inflation has risen to 2.9% and with wages growing at only 2%, the squeeze on household budgets is clear. The latest economic growth data shows that consumer spending is falling and that's important because consumer activity accounts for the biggest part of the economy.

In the short term this will dampen demand and with it, expectations of how quickly house prices will rise. Surveyors' expectations have been weakening in London for some time, but the sentiment has now spread into other parts of the south. This is also evident from the ratio of achieved sale prices to the initial asking price. London has been particularly affected since the change in stamp duty in 2014 made it more expensive for those buying property around £1m or more. This isn't a bad thing. Lower price growth is welcome as it makes home buying more affordable. Sellers also benefit from adjusting their expectations, achieving a realistic price more swiftly. And slower price growth is also welcome because it should lead to a more stable market.

After a decade without a rise, sentiment is moving towards a hike in interest rates – but not just yet. We expect a 0.25% rise in rates from spring/summer of 2018 followed by further hikes as economic growth starts to pick up, and wage growth accelerates, restoring households spending power and confidence.

Initial asking to achieved price

Source: Countrywide Research



As usual, the headline figure disguises the regional picture. London's market will slow the most, which entirely reflects the past levels of price growth and affordability. Expectations of future price growth potential are limited, which reduces some investor demand, especially from landlords. In addition, fewer landlord purchases, following the change in taxation. The end of year annual house price growth forecasts are positive throughout the forecast period, although there is likely to be some volatility, particularly in London.

In the prime areas of London, the outlook is a little more favourable. This sector of the market has already seen price falls and a revision of price growth expectations. We expect that to now adjust and for price growth to pick up. The rarefied nature of homes in this sector of the market means that supply is always a significant issue. The smaller market size can also make the price data volatile. But London still retains its place as one of the top world cities, which means that it should also benefit from a stronger global economy.

The long-standing issue with supply in the mainstream market will continue to be a support to house prices too. It is unlikely that there will be a significant boost from builders in a period where house price growth is low and input costs are rising. Even if the government meets its house building, it will do little to solve the previous undersupply. Leaving the EU single market will influence immigration and may help to reduce the rate of growth of households, but this is still some way off.

In the rental market, conditions are still favourable on the demand side. New taxation will bite harder over the next three years, eating into profit, which could increase sales by the most indebted landlords, reducing supply and boosting yields. However, tenants' budgets are also being squeezed so rental growth is likely to grow slightly less than average earnings – at about 2% in 2018 rising to 3.5% by 2019.

Price Growth Forecast

Region	2017(F)	2018 (F)	2019 (F)
Great Britain	1.5%	2.0%	3.0%
North East	0.0%	1.0%	2.5%
North West	2.5%	2.0%	3.0%
Yorkshire & Humber	2.0%	1.5%	2.5%
East Midlands	2.5%	2.0%	3.0%
West Midlands	2.5%	2.0%	3.0%
East	3.5%	2.0%	3.0%
South East	1.5%	2.5%	4.0%
South West	1.5%	2.0%	3.0%
Wales	0.5%	2.0%	2.0%
Scotland	0.5%	2.0%	3.0%
Greater London	0.0%	2.5%	4.0%
Prime London	2.0%	4.0%	5.0%
Central London	-1.5%	2.0%	4.0%

Source: Countrywide Research

Economy

Inflation?

We all know that inflation is rising – largely because sterling has fallen against other currencies, making imports more expensive. We import quite a lot so it adds a fair bit to the average inflation rate. But which inflation rate? There's RPI – the Retail Price Index; CPI the – Consumer Price Index and now a new one CPIH – Consumer Price Index which includes owner-occupiers' housing costs. What are they for and why do they differ? And which one is most accurate?

RPI is the oldest measure, but it doesn't capture the real inflation, that people feel, very well and reports a higher figure than the newer, more sophisticated measures. That benefits pensioners whose pensions are uprated at least in line with RPI. It's not so good for rail users though, as their fares are also linked to it.

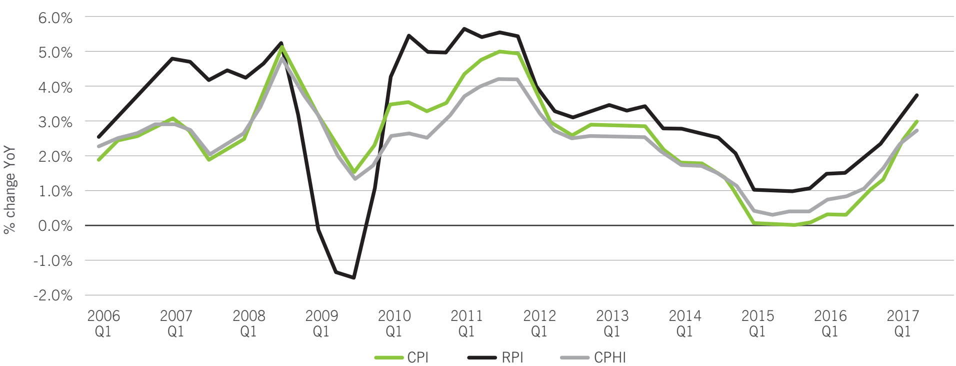
What about CPI then? This is the measure used by the Bank of England for inflation targeting.

The Monetary Policy Committee has a target of getting CPI to 2%. If it is more than 1% away from this – either way – the Governor of the Bank of England has to write to the Chancellor to explain why. But CPI has its flaws too because of housing. It includes rent in its calculations, but not ownership costs such as estate agents' fees or mortgages. These add up to over 15% of household spending are therefore quite a big thing to leave out. So that isn't the real feel of inflation either.

That leaves us with the newest measure CPIH, which does include the costs of owning a home and should be closer to the 'real feel' of price rises and could become the one to watch. In reality everyone has their own individual inflation rate, depending on how they spend their money. Therefore, without an individual series for everyone there will never be an exact measure of the rate of inflation for all – just an average for the whole of the country.

Measures of Inflation

Source:ONS



Sales

The top of the market

Just shy of 1.3 million people bought a home in 2007, a decade ago and the top of the last housing market cycle. Very soon after buying, these people saw the value of their home dip to below what they paid for it. For most, the fall in value was a paper loss as they sat tight, with no need to move on or sell up. But many of those who did sell in the first few years of the downturn, turned that paper loss into real money.

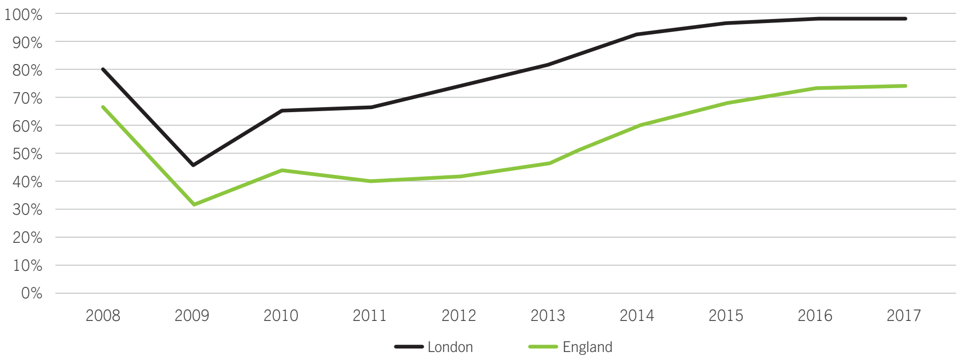
In the ten years since 2007, just over a third (34%) of those who bought a home at the top of the market have sold it. This is a much smaller proportion than those who bought in any of the previous five years. The '2007-ers' have been more likely to stay put, with many waiting for the value of their home to recover to allow them to move. Just 31% of those people who bought in 2007 and sold in 2009 got their money back. But 74% of those who waited for a decade sold for at least as much as they paid.

House prices in London have grown faster and to much higher levels than anywhere in the country and that allowed London sellers to be able to move sooner. Londoners who bought back in 2007 have proved the most likely to move on and have done so more quickly. Half of Londoners who bought in 2007 have now sold. During that decade, just 16% sold their home for less than they paid for it. And rather than waiting a full decade for prices to recover, the vast majority of this 16% sold between 2009 and 2012 when the market was at its lowest point.

For many homeowners, the late 2007 downturn is all but a distant memory. And since the crash there are some 2.4 million new owners. These people have only ever seen the value of their property go up. But a decade isn't such a long time and a significant minority of the people who bought in 2007, right at the very top of the market, know all too well that the value of their home can go down as well as up.

Proportion of 2007 buyers who've since sold for more than they paid

Source: Countrywide & Land Registry



Lettings

Rate of rental growth doubles

Countrywide's Monthly Letting Index shows how the run of eight consecutive months of falling rents in London ended abruptly in July. Rents in London ended the month 2.1% up on last year, as the number of properties available to rent in the capital fell sharply. Across Great Britain the rate of rental growth doubled from 1.1% in June to 2.2% in July. This comes as rental growth across the South of the country starts to pick up – three of the four English regions where rents rose fastest were in the South (South West, East of England and Greater London).

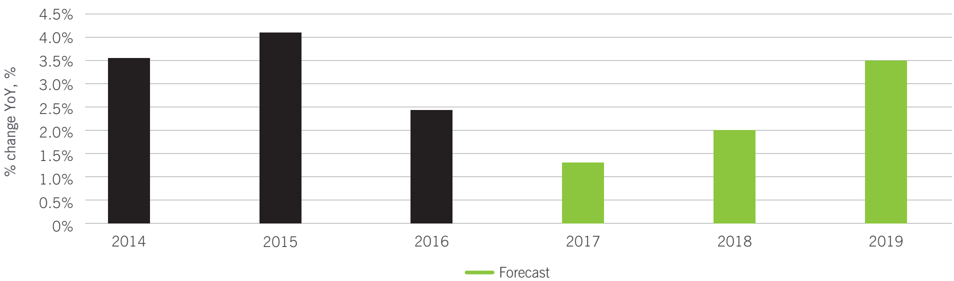
The number of homes on the market has remained high. That's because of the rush to beat the 3% stamp duty surcharge for investors in April 2016 caused a spike in the number of homes to rent. A month after the introduction of the surcharge, the number of homes on the market to rent in Great Britain was 14% higher than in the previous year. By July 2017 the number of homes to rent was 4% higher and the stock of homes to rent is now falling. That's because the change in taxation has reduced the flow of new landlords coming into the market. The effect is bigger in the more expensive parts of the country where the tax changes take a larger bite out of landlords' yields. In July the proportion of London homes bought by a landlord fell to 10.5%, its lowest level for seven years.

There were fewer homes available to rent in July compared with a year earlier. Then there was still a spike of new properties coming on to the rental market from landlords who had bought to beat the stamp duty rise. In London there were 18% fewer available while there were falls of 6% and 5% in the East of England and the South East respectively.

Fewer homes for rent when demand is still buoyant will lead to upward pressure on rents. That's already happening. In London, rents rose in the last two months after eight previous months of falls.

Rental Growth Forecasts

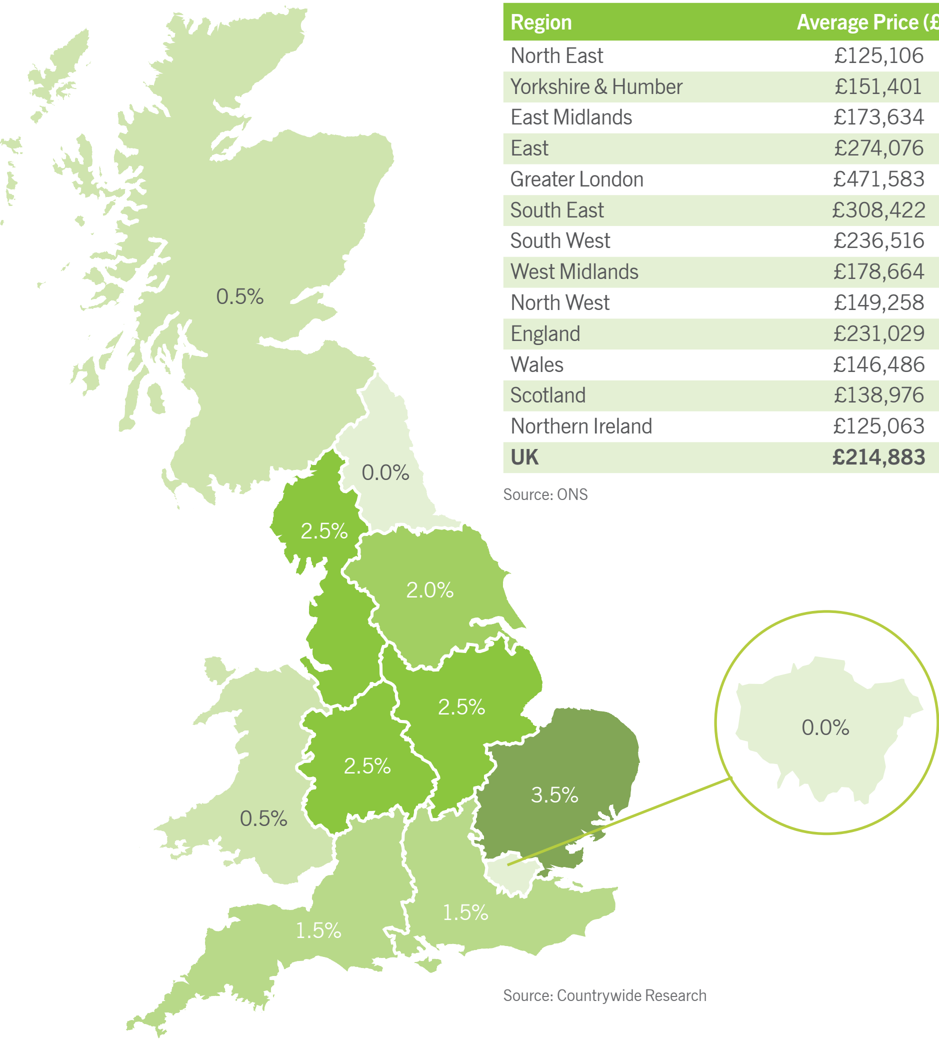
Source: Countrywide Research



Stat of the Month

House price forecasts

2017 Price Growth Forecast



Source: Countrywide Research

Average Price Q4 2016

Region	Average Price (£)
North East	£125,106
Yorkshire & Humber	£151,401
East Midlands	£173,634
East	£274,076
Greater London	£471,583
South East	£308,422
South West	£236,516
West Midlands	£178,664
North West	£149,258
England	£231,029
Wales	£146,486
Scotland	£138,976
Northern Ireland	£125,063
UK	**£214,883**

Source: ONS

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