SPOTLIGHT
Savills Research

Mainstream Residential Property Forecasts

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More growth to come in 2021 and a soft landing in 2022

UK mainstream house price growth forecast +9.0% in 2021…

The average UK house price has continued to rise strongly in 2021, increasing by +5.6% in the first six months of the year according to the Nationwide index. Despite the rush of activity prior to the stamp duty deadlines of March and June, we are continuing to see elevated levels of demand against the backdrop of limited supply.

This imbalance looks set to maintain growth for the second half of the year meaning we expect annual house price growth across the UK as a whole to end 2021 at 9.0%.

…and transactions to exceed 1.6m for the first time since the credit crunch

We expect transaction levels to diminish gradually over the remainder of this year as government support for both the housing market and the wider economy is withdrawn. However, the pace at which sales continue to be agreed suggests that national transaction levels will still end the year at circa 1.62m.

That is roughly 35% higher than the average for the five years prior to the pandemic, despite an acknowledged shortfall of available supply to meet demand.

Reduced capacity for price growth post-2021

The recent strong price growth, combined with an expectation that interest rates start to rise a little earlier than previously anticipated, leaves much less capacity for price growth post-2021.

Affordability limits have become embedded by the stress testing of mortgage affordability at a borrower level and the caps on lending at high loan-to-income ratios that were introduced by regulators to ensure responsible lending.

They are one of the key reasons behind our expectation that price growth in the period 2022 to 2025 will be in the order of 11%-12%. They also indicate limited capacity for further price growth at the end of this period, without substantially affecting who is able to buy and the number of potential transactions.

A soft landing seems likely

But those limits are an equally important reason why we are expecting a soft landing, rather than a dramatic correction in values in the short term.

There are five further reasons for this:

1. The pace of economic recovery means unemployment levels have been contained and are forecast to progressively return to pre-pandemic levels
2. The price growth seen since the housing market reopened last year has partly been driven by a change in buyer profile: one more weighted to equity-rich home-movers (as opposed to first time buyers) meaning less reliance on mortgage debt
3. This, combined with more activity from higher earners, has meant that average loan-to-income ratios have not moved dramatically. As a consequence, buyers active in the market have been able to operate within the bounds of existing mortgage regulation without unduly stretching their mortgage requirements
4. More of those buyers have been able to lock into low-cost fixed rate mortgages for longer periods, protecting them against the risk of rising interest rates
5. Interest rate rises are still expected to be gradual and modest, meaning a progressive squeeze on affordability.

Together this means there does not appear to be a trigger for a major house price correction.

….though the pattern is difficult to determine

Ultimately, the pattern of growth over the period 2022-2025 depends on the extent to which the market normalises and what this means for price growth next year. ➤

London: a market divided between flats and houses

London has performed better than we might have expected, given its affordability pressures and reduced demand for urban life during successive lockdowns. The city still saw growth of 4.8% in the first half of the year and we are expecting it to finish the year up 7.0%.

The bulk of growth has been driven by family houses, given the demand for more space. Flats have performed less strongly and, with cladding issues also holding back this part of the market, we expect them to continue to underperform the London average in the immediate future.

Forecast house price growth and economic measures

	2021	2022	2023	2024	2025	5-year total
UK house price growth	9.0%	3.5%	3.0%	2.5%	2.0%	21.5%
London house price growth	7.0%	2.0%	1.5%	1.0%	0.5%	12.4%
Transactions (millions)	1.62	1.23	1.20	1.20	1.20	-
Bank Base Rate (at Q4*)	0.10%	0.10%	0.25%	0.50%	0.75%	-
Unemployment rate (at Q4*)	5.0%	4.5%	4.2%	4.0%	3.8%	-
Real GDP growth (whole year*)	7.6%	6.3%	2.1%	1.5%	1.5%	20.4%

Source: Savills Research, *Oxford Economics

> “A recovery in First Time Buyer activity relies on government support or more help from the Bank of Mum and Dad”

➤ While at this point, we are forecasting price growth of 3.5% next year, we could still see some of the growth generated by the extraordinary market conditions of 2020 and 2021 unwind at times during 2022.

This is by no means a certainty, given the difficulty in predicting how embedded the changed housing priorities and requirements for more space will be in the market. Not only will this be critical to the level and composition of transactions, but it will determine the capacity for further price growth as the prospect of interest rate rises appear on the horizon.

But risks remain

The path of interest rates remains crucial to our house price forecasts. A steeper-than-anticipated jump in rates would severely restrict growth, although it would have to be severe to lead to actual falls in values – an outside risk in our view.

The regional view

Regionally we continue to expect the markets of the Midlands and the North of England to show the strongest price growth as has occurred historically at this point in the housing market cycle, due to greater capacity for growth before hitting affordability ceilings.

However, in the short term we do expect some of the buyer focus to shift back towards urban markets, including London, as social distancing restrictions and international travel restrictions ease.

This will see the ratios of regional to UK average values slowly converge over the next five years, as the lower value regions see stronger growth, ‘catching up’ with the rest of the country. This is what we’d consider typical late cycle behaviour.

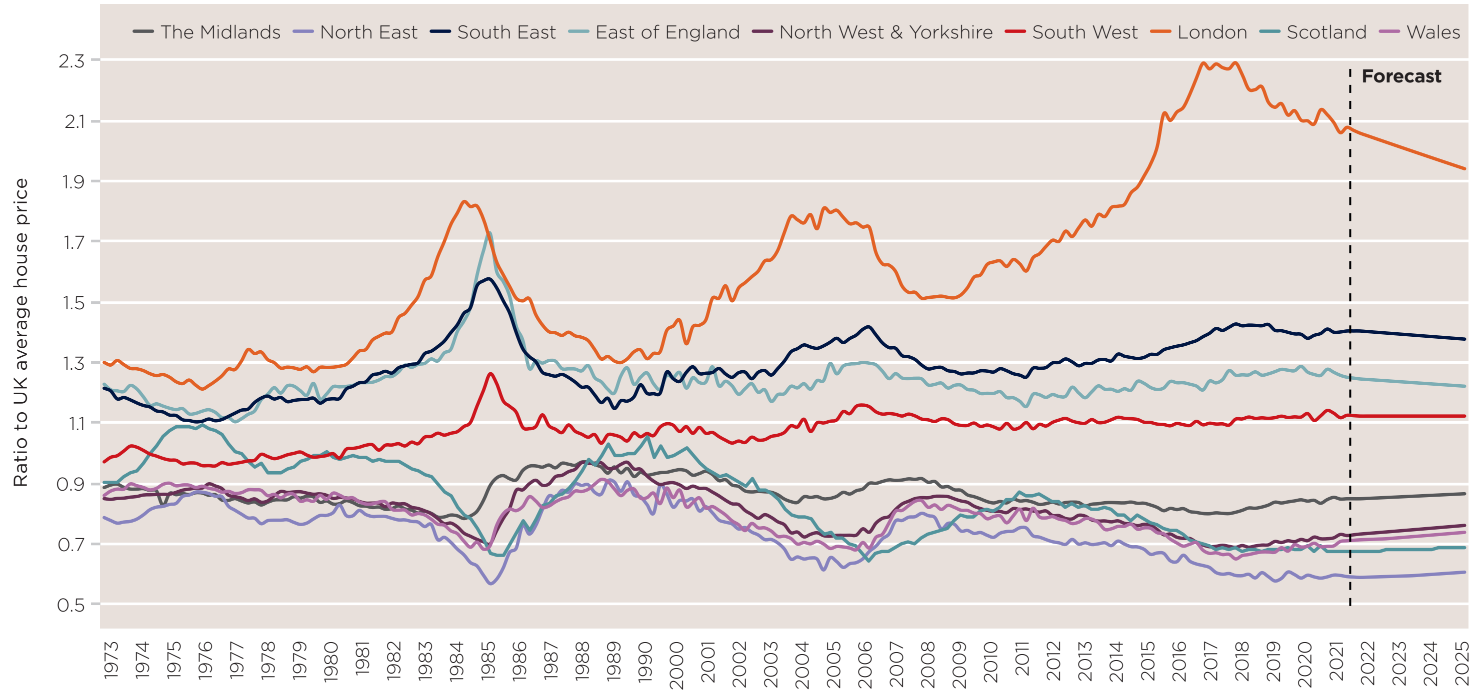
Mainstream residential property forecasts

	2021	2022	2023	2024	2025	5-year to 2025
North West	10.5%	4.5%	4.0%	3.5%	3.0%	28.0%
Yorkshire and The Humber	10.5%	4.5%	4.0%	3.5%	3.0%	28.0%
Wales	10.0%	4.0%	4.0%	3.5%	3.0%	26.8%
Scotland	9.5%	4.0%	3.5%	3.0%	2.5%	24.4%
North East	8.0%	4.0%	3.5%	3.5%	3.0%	23.9%
East Midlands	9.0%	4.0%	3.5%	3.0%	2.5%	23.9%
West Midlands	9.0%	4.0%	3.5%	3.0%	2.5%	23.9%
South West	8.5%	3.5%	3.0%	2.5%	2.0%	20.9%
South East	9.0%	3.0%	2.5%	2.0%	1.5%	19.1%
East of England	8.0%	3.0%	2.5%	2.0%	1.5%	18.0%
London	7.0%	2.0%	1.5%	1.0%	0.5%	12.4%
UK	9.0%	3.5%	3.0%	2.5%	2.0%	21.5%

N.B. These forecasts apply to average prices in the second hand market. New Build values may not move at the same rate.

Source: Savills Research

Ratio of Average Regional to Average UK House Prices



Source: Savills Research using Land Registry and Nationwide

What are the implications for First Time Buyers?

Since the inception of the pandemic we've seen a market increasingly weighted to equity rich home movers, at the expense of First Time Buyer (FTB) numbers. FTBs have struggled over the past year, with younger people facing higher rates of unemployment and furlough, house prices rising further out of reach, and withdrawal of high loan-to-value mortgages.

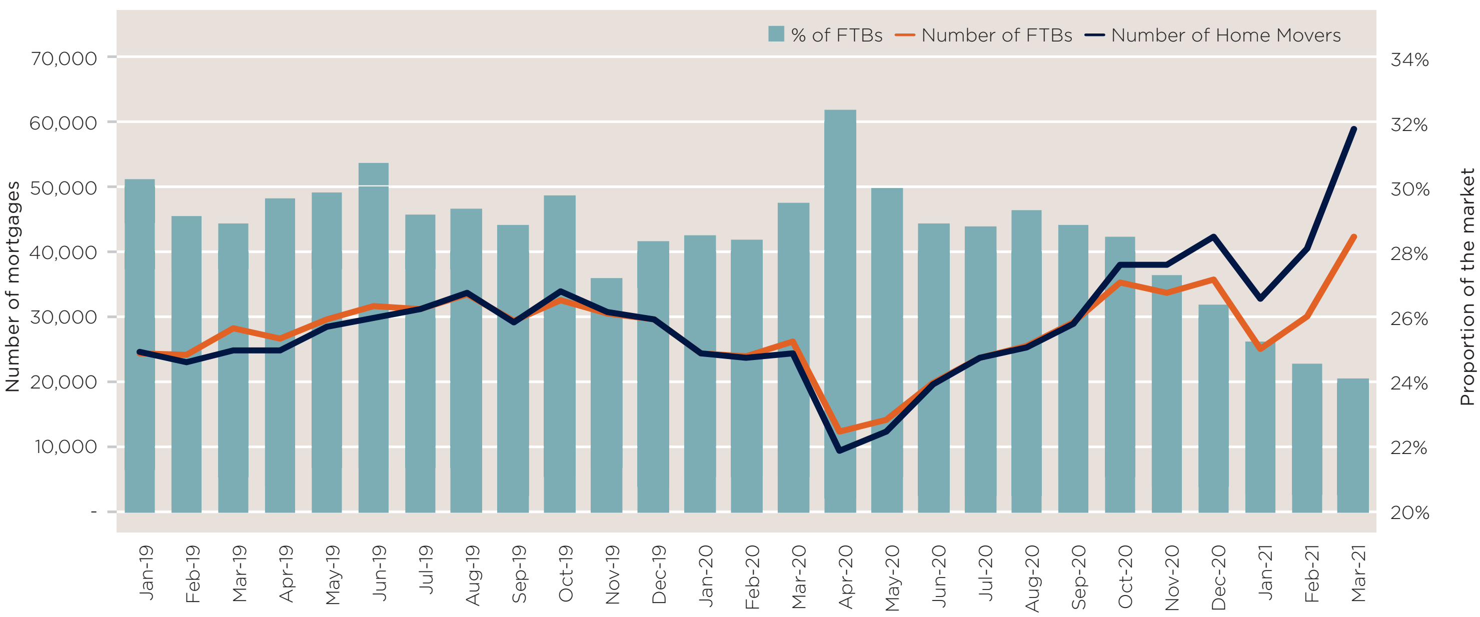
As a result, FTBs fell from 30% of mortgaged buyers in March 2020 to 24% by March 2021.

The Mortgage Guarantee scheme should go some way to boosting their numbers, perhaps by as many as 50,000 a year if the scheme's impact is on a similar scale to the previous mortgage guarantee scheme that ran between 2013 and 2017. The end of the stamp duty holiday will also see FTBs regaining a slight competitive advantage.

Looking further ahead, the end of Help to Buy (HtB) in 2023 will knock back FTB numbers, considering it supports around 40,000 FTB purchases a year. First Homes will soften some of this fall but is unlikely to compensate fully for the loss of HtB.

Any recovery in FTBs will have to be backed by various forms of government support, or by continued large contributions from the Bank of Mum and Dad.

First Time Buyers fall behind Home Movers



Source: Savills Research using UK Finance

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