Housing market trends and recent policies

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Context

• Strong upturn in the housing market in 2013

• Very active area for government policy

• Concerns raised about:
  – House price ‘bubble’
  – Affordability
Outline

1. What has been happening to house prices?
   - What do recent trends suggest about a potential ‘bubble’?

2. What impact will Help to Buy have?
What is a ‘bubble’ and how can we identify one?

• A ‘bubble’ is when rising prices are driven by expectations of future price increases
• Differs from a ‘boom’, where prices are driven by economic ‘fundamentals’, i.e. supply and demand for housing
• Characteristic features of a ‘bubble’
  – Speculative buying for capital gain
  – Speculative mortgage lending
  – Rising prices followed by decline or collapse
• A ‘bubble’ and a ‘boom’ might indicate different problems, and require different solutions
• How can we identify a bubble?
  – Compare with historical peaks and trends
  – Look directly at supply and demand (why is London different?)
UK house prices since 1988

Notes and sources: see Figure 5.1 of The IFS Green Budget: February 2014
UK house prices since 1988

Notes and sources: see Figure 5.1 of *The IFS Green Budget: February 2014*
House prices in London

Notes and sources: see Figure 5.1 of *The IFS Green Budget: February 2014*
Real house prices in the UK and London

Notes and sources: see Figure 5.6 of *The IFS Green Budget: February 2014*
Why are prices growing faster in London?

• Short run
  – London’s economy has performed better than UK average since 2007 on some measures e.g. total output, employment
  – Large flows of foreign investment, increased since 2007

• Long run
  – Population growing faster than housing stock in London (in contrast to England as a whole)
Prices growing significantly faster than earnings in London

Nominal house-price-to-earnings ratio for first-time buyers

- UK
- London
- UK trend
- London trend

Prices growing significantly faster than earnings in London

Notes and sources: see Figure 5.7 of *The IFS Green Budget: February 2014*
Help to Buy - overview

• Aim: describe two components, explain rationale and objectives, initial assessment of impact

• Equity loan: loans of up to 20% on newly built homes (launched Apr 2013)
  – No interest for first five years; govt shares in capital gains and losses
  – £3.5bn over 3 years; 74,000 properties

• Mortgage guarantee: provides mortgage lenders the option of govt-backed insurance on high LTV loans (launched Oct 2013)
  – Lenders pay a fee calculated to cover expected costs
  – £12bn contingent liability to fund £130bn or loans over 3 years

• Eligibility is very broad for both schemes
  – Properties worth <£600k
  – Residential only, no second homes
  – Borrowers have to pass mortgage ‘affordability’ checks
Help to Buy - objectives

• **Increase affordability of homeownership**
  – Address deposit constraint (enable purchase with 5% deposit)
  – Major reduction in availability of high LTV loans
  – Equity loan: top-up ‘deposit’
  – Mortgage guarantee: increase availability of high LTV loans, correcting perceived ‘market failure’ in market for high LTV lending

• **Stimulate housing supply**
  – Equity loan: direct stimulate spending on and demand for new builds
  – Mortgage guarantee: no direct link; potential indirect impact via increase in demand/activity
Help to Buy: equity loan, assessment

• Impact on affordability
  – Concerns policy not targeted at those who need help to get on property ladder (FTBs, low-income households/‘starter’ homes)
  – Available data suggests this is not major issue:
    • 92% of loans made to FTBs
    • Above average incomes, but lower than typical house purchaser
    • Average purchase price of £195k, close national average (£170k)

• Impact on supply
  – Will the scheme generate ‘additional’ demand?
  – How will supply respond?
    • Supply historically not very responsive
    • But may be spare capacity in short term
  – So far: increase in construction, but hard to isolate impact
Help to Buy: mortgage guarantee, assessment

• Impact on affordability
  – Has the scheme increased availability or reduced costs of high LTV mortgages?
  – Bank of England survey reports increased availability, linked to policy
  – Reduction in interest rates, though impact of policy less clear

• Impact on supply
  – No direct link to supply of new homes, has caused concern
  – Short term upward pressure on prices is likely (given rel fixed supply)
  – Eventual impact depends on additional demand and supply response
  – Given supply concerns, could target purchases of new builds only
Summary

• Strong growth in house prices in 2013

• No clear evidence of ‘bubble’ based on comparisons of real prices with previous peak and trends

• Faster growth in London partially explained by strong economy, foreign investment and population growth, though prices growing faster than earnings is potential source for concern

• Help to Buy is likely to improve affordability in the short term

• Uncertainty around impact on supply (and prices)