If the housing market has not bottomed out what are the positive attributes?

By Nicholas E. Ashton

I know people are on tender hooks, worrying about their jobs, putting food on the table and keeping a roof over their heads. Government has been more concerned with big business staying solvent whilst unemployment is spiraling out of control. Where is the sense in the politician's actions? It has been 9 months of government spending and increasing the American debt threefold!

So where are the positive aspects of this glum and discerning year?

Elizabeth Colman – Sunday Times stated:

"House prices look likely to end the year higher than they were in January, in defiance of dire predictions from industry experts. Prices have risen for five consecutive months, according to the Nationwide Building Society index, and are back where they stood in September 2008.

There has been a 4% rise over the year so far and on current trends, the gain could reach 6% by year-end. This is in sharp contrast to gloomy forecasts from the likes of the research consultancy Capital Economics, which predicted falls of 25% this year alone and 35% from peak to trough.

The strength of the rebound should come as no surprise to Sunday Times readers: in February, a panel of experts convened by Money said that the recovery, when it came, would be sharper and swifter than the leading forecasters were expecting. With the average house price now at £161,816 — only 13% off the October 2007 peak — we convened another panel to discuss whether the upturn could last."

This is Europe and is just about mirroring the USA.

Colman then stated:

“The panel raised concerns that the strength of the house price recovery could provoke the Bank into raising interest rates to contain inflation — precipitating a “double dip”. Last week, Halifax said property values increased 1.6% during September.

Rising unemployment was the other factor that would halt the recovery, potentially sending house prices into decline again in 2011, or 2012, the experts said.

Fitch, the credit ratings agency, forecast last week that prices could fall steeply next year. It believes they will fall 30% from peak to trough, suggesting another 17% decline next year.”

Not a pretty sight in anyone’s eyes!

Is government allowing the free fall for a reason? Do the politicians really understand the ramifications of the decline and the long term effects of a financially bankrupt America? How much do we owe the Chinese? What happens when they call in the massive loans?

How is this going to help you today? Can we derive a positive sense from this deluded economic world?

Of course we can, you’re not going to stop breathing, slit your wrists or blame the Mother-in-law! It is a positive time just like each and every depression or recession that has gone before. Lessons are taught and the facts can assist us to radically implement those traits that have been impressed upon us over time.

Short term wants and needs are not necessarily the answer. Some though will only respond in short term answers, let’s look at the question and the answers:

Kathryn Cooper, editor of Money: Why has the housing market enjoyed such a strong rebound?

George Buckley, Deutsche Bank: If we consider any measure of [housing] affordability — mortgage repayments as a proportion of income — it’s looking fairly good right now. Repayments are just 28% of average incomes. It’s no surprise that house prices are rising given that mortgage lending is starting to stabilize.

Simon Rubinsohn, RICS: There's also a global dimension. Central banks are pouring liquidity into the economy and pushing up asset prices, property in particular. It's not confined to Britain; other economies are fretting about the effect on prices. It wouldn't surprise me if we saw prices up on, say, Nationwide's index at peak levels.

Seema Shah, property economist at Capital Economics: In the short term, you could feasibly have another year of continuing price rises.

Ray Boulger, senior technical director at John Charcol: The sort of people who might have been repossessed in the late 1980s and early 1990s, when their interest rates doubled in 15 months, have this time seen their mortgage rates come way down because many are on trackers.

Government support is stopping lenders from repossessing, which will mean repossessions are not as bad as they were in previous downturns. Low interest rates are another key factor. For those reasons, we're going to see the market continue to improve in the short term.

Trevor Abrahmsohn, founder of Glentree International: The bottom of the market probably was in about April. Next year there will be a slow and progressive rise in prices. There's been a sea change in thinking among developers in the past six to eight weeks. I know a number that are taking quite a bullish view.

Lucian Cook, director of Savills Research: We have seen the bottom of the market, but that's not to say we won't get close to it again. I suspect there won't be the same demand in six or nine months that there is at the moment.

These are folks have a whole different aspect on the world economy and have maybe rose colored glasses.

So what do the long termers have to predict?

Cooper: Do you see this rally continuing?

Buckley: As soon as interest rates go back to normality or somewhere near normality, house prices will not look at their right level. If interest rates were at their long-run average — that's actually 7.1%, as opposed to Bank rate currently at 0.5% — mortgage repayments as a percentage of disposable income would be 37.2% now. That's where it was at the start of 2007.

There is probably more downwards adjustment to go. The decline we have seen in real terms is very similar to what we saw in the 1990s, when prices continued to fall.

Cook: There's still a big constraint, which is access to mortgage finance — particularly for those with small deposits. The market is being driven by the people who are in the market. Next year you may find it reflects much more the people who are still out of the market.

Rubinsohn: Looking at our surveys, we have had only two months in a row where we've had new instructions [from sellers]. The level of supply is way below that needed, given the sudden rush in demand, to hold prices stable. That is a short-term problem, though.

The ratio of sales to stock is key here. It is still at low levels but if we start to see more supply coming on tap, that could begin to shift the equation, particularly as mortgage supply remains a constraint on sales. I'm looking at that indicator particularly carefully at the moment.

Shah: There's going to be a second leg to this downturn. Timing is incredibly uncertain. Because interest rates have been so low, there just haven't been any forced sellers. But we're almost in a sweet spot at the moment with the economy, so either that recovery continues as it is, at which point the Bank of England will have to stop the quantitative easing programme and rates will go up, which means affordability goes down the toilet, or the economic recovery falters, in which case unemployment starts rising again. Neither seems to be very supportive for the housing market in the long term.

Boulger: Of the 10m residential mortgages in this country, 3m to 3.5m are held by people who can afford their mortgage but would not be able to get another if they wanted to move house — because they don't have enough equity in their property for the deposit needed or because they're subprime or self-certified and those deals have pretty much disappeared.

That's going to constrain activity for quite some time because those people have either got to stay put or they've got to sell up and rent, which most probably won't be keen to do. I see activity increasing only relatively slowly.

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Buckley: This cannot go on forever. Look at the past six months: house prices are up 7.2% on the average of the Nationwide and Halifax indexes since February, so that's close to a 15% annualized rate of growth. That is a little bit worrying when you have an inflation target of 2%.

Cooper: It almost sounds like you are worried about another bubble.

Rubinsohn: What's going on is not indicative of a particularly healthy economy. It's not a testimony to a successful market.

Buckley: House prices rose 200% over 10 years; they've fallen by only 13%. If we were in a bubble before, we're probably still in a bubble.

Cook: Unemployment is another reason why we could see a softening in the market, because demand is essentially driven by the cash rich. Also, we don't think unemployment is going to peak until next year.

Rubinsohn: Arguably, you could say that 2011 is going to be a bigger story for unemployment, when the public spending cuts start to have a material impact. Our view was that prices would drop back next year, but I wonder whether if this run continues it will be the latter part of next year or even 2011 when we see the drop.

Shah: We can expect to see a tail-off [in house prices] in 2011 and 2012 because of unemployment.

The long term answers are still not giving us a full positive reflection. It seems that unemployment problems are going to be with us for a long time. That is no comfort to those without jobs!

So what is the long term?

Boulger: Interest rates are going to be the key, and if they go up too far, too quickly, that will bring down house prices again.

Abrahmsohn: Interest rates will start to rise toward the middle to the end of next year but some of the banks and building societies may cut a bit of their margins because at the moment those margins are obscene. That means the amount consumers actually pay may not be that different even if interest rates do rise a little.

Boulger: I'm not sure it is at all clear that rates will start rising in the middle of next year. It is a big unknown. The longer it takes the economy to improve, the longer interest rates are going to have to stay low.

Buckley: Mervyn King [governor of the Bank of England] has called this the "nice decade" — a great moderation, if you will. I worry that over the next 10 years we won't see this "nice" decade. We may see a period where there is exactly the opposite — where we need higher interest rates, and lower growth, to keep inflation at the 2% target. People do not think about that when rates are low. They just think "affordability is very good; I need to buy a house".

Shah: We could see the Bank reacting a lot sooner than anyone expects, considering we've had this run-up in house prices.

Rubinsohn: We don't think interest rates will rise until November next year, so quite late given what's going on in the housing market. I can't help but feel that if we continue to see strength in the market, it will filter into the way the Bank thinks. At the moment, I'm still saying November, but the risk is it's going to be brought forward.

There is no defined answer from the core group at all. It is all maybe this, maybe that!

Just what is the outlook for those that have mortgages or are contemplating obtaining a new mortgage?

Boulger: Gross margins [the price of new mortgages over the cost of funding] are the highest they've been for a long time. We are seeing a few signs of lenders beginning to get a bit more competitive. As Bank rate rises, those spreads will narrow. They won't narrow back to the levels we had before, but they will narrow.

Cook: There is a huge difference between mortgage credit being affordable and being available. At the moment, there is still extremely constrained access to finance.

Boulger: There are still no really long-term fixed-rate mortgages available. I don't think protecting yourself for even five years is long enough. If interest rates don't start to go up for three or four years, which is possible, then having a five-year fix could mean you come out of it at just the wrong time.

If you are a first time buyer what are your chances?

Cook: First-time buyers have got the rough end of the stick. They're clobbered by the requirement to raise a big deposit.

Shah: As a first-time buyer myself, it is impossible to put a deposit at the level required to get a good mortgage rate. That immediately puts me out of the market. The other thing is, is it a good time to buy? First-time buyers are the ones most at risk of losing their jobs in the next two years. I wouldn't expose myself to the market right now. I would want to see what happens over the next year; if it means that I missed the bottom of the market, so be it.

As all these experts are across the pond what do they feel about their own London market?

Cook: Prime London markets have come back much quicker than the rest of the country. Prime southwest London had second-quarter growth of 6.4% and third-quarter growth of 8.4%, although it is still something like 15% off its peak.

Abrahmsohn: I've seen London change since the early 1970s from a quaint historic city to somewhere diplomats and prime ministers want to have second homes. Then you've got the exchange rate, which is favoring anyone in Euros — and if you earn money in petrodollars, there is an incentive to buy in this country. With all this pressure on a finite market, plus people already in the London market considering buy-to-lets, there is a lot of positive pressure. I've always had this robust view of the London market; it almost defies gravity, somehow.

Cook: There is a big difference between the prime and equity-rich markets and the other end of the scale, where a lack of access to finance and unemployment could have a more prolonged impact. The difference between the equity "haves" and "have-nots" over the next five years is going to be quite significant.

The bottom line is what should you do if you want to enter the housing market and commit to a new roof over your head?

Boulger: Potential buyers should go ahead provided they can get finance at a rate they are confident they can afford. If prices rise another 6% next year, a buyer today will be in a better position even if they have to pay, say, an extra two percentage points on their rate than if they buy in a year's time, even if they then qualify for a slightly cheaper mortgage.

Cook: The big difference now, compared with early 2009 or 2008, is the realistic prospect of sale in a reasonable period. If you are putting the property up for sale now ... you have a reasonable degree of certainty. There is a real opportunity now, if you're an upsizer and you have a big deposit.

Thank you Elizabeth Colman! Some of the most down to earth research and bringing this great "real information" to the forefront and we appreciate.

From a sales perspective the message is go forward! Let nothing stand in your way; make sure you are selling for the right reason for the buying client.

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