SPOTLIGHT
Savills Research

Mainstream Residential Property Forecasts

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2021 will be a complex year, with competing forces having different impacts on the housing market over the course of the year. But government support, the easing of social distancing restrictions, and low interest rates underpin our forecast for 4.0% price growth.

It's safe to say that most people spent much more time at home last year than they may have been expecting. As a result, the housing market saw incredible strength as those households with the financial security to do so sought homes that could act as workplaces and schools, as well as places to live.

Despite the economy contracting by -10%, house prices rose by 7.3% over the year, as the stamp duty holiday added a sense of urgency to a market that was driven more by behavioural change than underlying economics.

Remarkably, transaction levels ended the year just 11% below those of 2019. Our calculations show that home buyers spent a record £120.5bn in the fourth quarter of the year, some 22% above the previous high in the third quarter of 2007.

But as we look forward, a number of questions hang over the market. The answers to these will determine levels of market activity and future price growth.

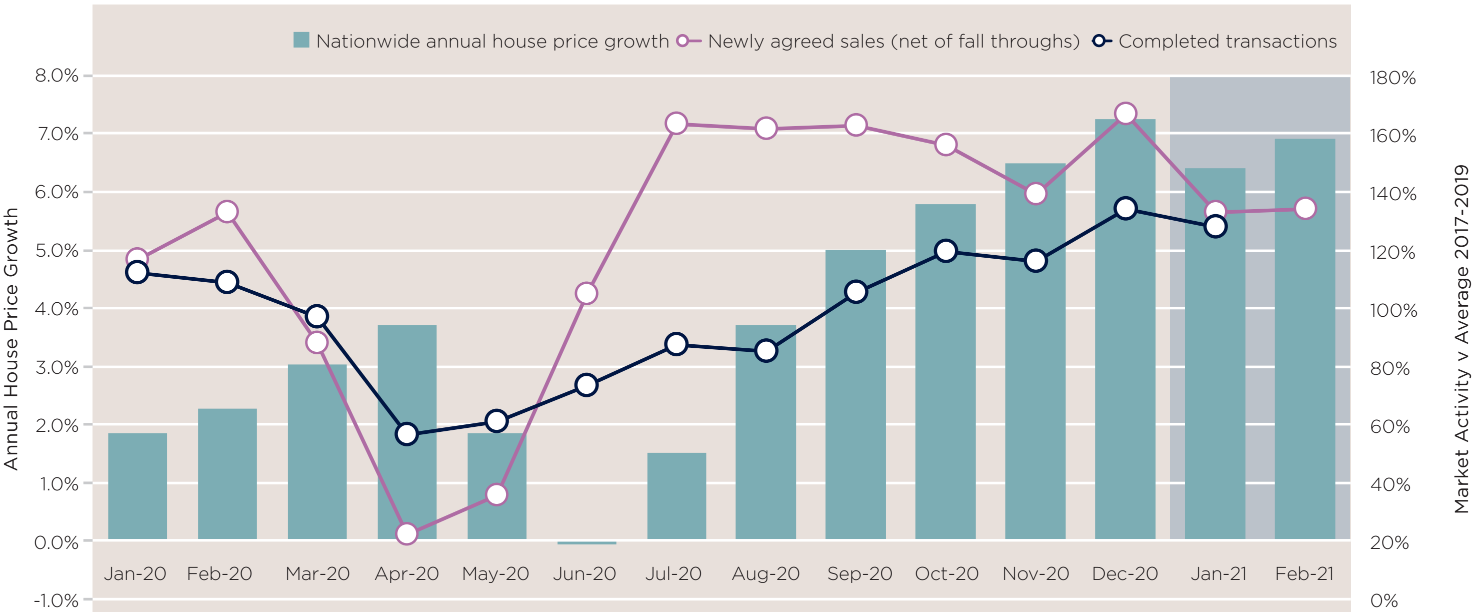
- What impact has the most recent lockdown had on people's desire and ability to get onto or trade up the housing ladder?
- How important have various stamp duty holidays really been to the strength of demand? What happens when they come to an end?
- What impact will the vaccination programme have on buyer sentiment as it is rolled out?
- What has the price growth of 2020 done to the underlying capacity for price growth over the remainder of our five-year period?
- What does that mean at a regional level, given where we were in the housing market cycle prior to the pandemic? And how will this play alongside the Government's levelling up agenda?

Table 1 Forecasts and economic assumptions

	2020 Actual	2021 Forecast	2022 Forecast	2023 Forecast	2024 Forecast	2025 Forecast	5 years to 2025 forecast
UK House price growth	**+7.3%**	**+4.0%**	**+5.0%**	**+4.0%**	**+3.5%**	**+3.0%**	**+21.1%**
Transactions (millions)	1.04	1.40	1.25	1.20	1.20	1.20	n/a
GDP Growth (whole year)*	-9.9%	+5.5%	+6.0%	+2.2%	+2.0%	1.8%	+18.6%
Unemployment (at Q4)*	5.1%	5.8%	4.8%	4.3%	4.1%	4.0%	n/a
Bank Base Rate (at Q4)*	0.10%	0.10%	0.10%	0.10%	0.25%	0.5%	n/a

Source: Savills Research, *Oxford Economics

Figure 1 Prices and activity in the UK housing market



Source: Savills Research using Nationwide, TwentyCi, HMRC

“Our analysis suggests average UK price growth of 20% is sustainable over the next five years without unduly depleting mortgage affordability”

The year ahead

2021 will be a complex year, with competing forces having different impacts over the course of the year. With the country back in lockdown in the early part of the year, the economy is predicted to contract by 4.4% in the first quarter.

Leading market indicators are mixed. The RICS survey points to falls in new buyer enquiries and new instructions in the early part of the year. The Nationwide index showed a marginal fall in the average house price in January but a return to growth in February. Meanwhile, real-time data from TwentyCi indicates that the number of sales being agreed is still some way above the pre-pandemic norm, as were mortgage approvals for January.

This suggests the market will remain relatively strong through the first half of the year with the extension of the stamp duty holiday likely to prolong a period of robust market activity in England and Northern Ireland.

We have previously talked about the prospect of a lull in the market once the stamp duty holiday ends and the economic realities of lockdown are brought more sharply into focus as the unemployment rate peaks. A tapering of the stamp duty relief in the period to September, together with the introduction of a mortgage guarantee scheme across the UK as a whole, will provide support to transactions in this period, though we do expect the market to cool.

The roll-out of vaccines, the corresponding potential for the economy to rebound and the prospect that unemployment levels will start to fall in the second half of the year are all likely to gradually bolster consumer confidence. We expect this to support a return in activity and modest price growth later in the year in a period of continued low interest rates.

So, while there may be a brief lull in activity as people bring transactions forward to beat the stamp duty holiday deadline, the underlying drivers to move home will remain while the experience of lockdown remains fresh in the memory, supporting activity in the second half of the year.

As a result, we have revised our forecast for house price growth in 2021 up from 0% to +4% across the country as a whole, with a relatively strong start and end to the year sandwiching a more subdued middle.

Affordability underpinned by low interest rate expectations

As we look further into the future we gradually expect to see the fundamentals of mortgage affordability to determine levels of price growth and its regional distribution.

The price movements of 2020 will have made housing less affordable to the average household. Furthermore, given the disruption to the economy, income growth expectations over the next five years have softened.

However, because the outlook for interest rates has become much more benign, there remains capacity for further price growth. Pre-pandemic, Oxford Economics forecasts that Bank Base Rate would have risen to 2.25% by the end of 2025. Now they now are forecasting this figure will only have reached 0.5% at the end of our forecasting period, with the first interest rate rise not pencilled in until the third quarter of 2024.

Overall, our analysis suggests the average UK price growth of around 20% is sustainable over the next five years without unduly depleting mortgage affordability. If rates rise faster than anticipated, prospects for such price growth would be curtailed.

Return to stronger growth in 2022

With price growth of +4% forecast for 2021, we expect slightly stronger price growth in 2022 during a period of sustained economic recovery. Income growth is expected to peak and unemployment is expected to fall back to 5% by the end of the year. Social distancing will have largely, if not completely, eased away and international travel is expected to return restoring international demand. Together with government support for more higher loan to value lending, this should bring a broader range of buyers back into the market at a time when the 5-year cost of money will remain highly attractive for borrowers.

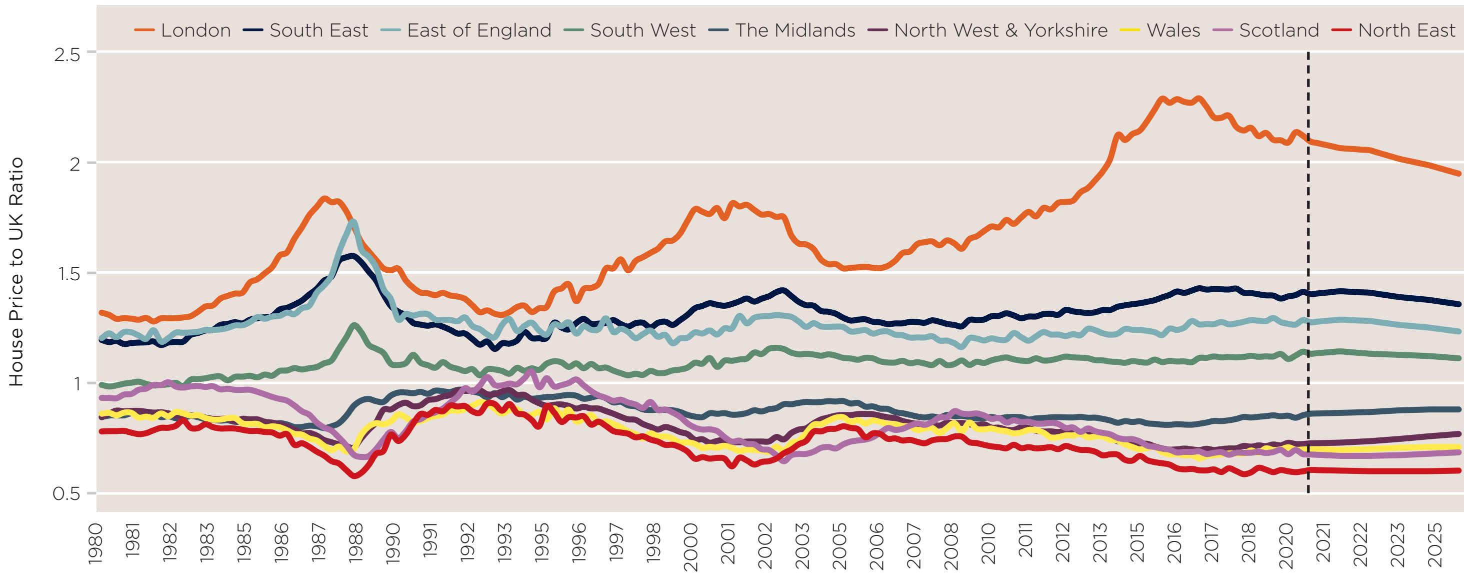
Thereafter, we expect levels of house price growth to ease back year on year, as rates of economic growth reduce, the prospect of rates rising comes closer and there is less urgency to move for lifestyle reasons.

Regional patterns of growth

The unique circumstances of the pandemic didn’t just break the historical relationship between recessions and housing market downturns. They also disrupted the normal geographical cycle of house price growth.

Since 2016 we had seen the London and South East markets underperform the rest of the country, having exhausted more of their capacity for house price growth because of their performance in the previous decade. Prices in London, in particular, had become more dislocated from the rest of the country than in previous cycles.

Figure 2 Ratio of Regional Values to UK



Source: Savills Research using Land Registry, Nationwide,

“ The Government’s levelling-up agenda is likely to support the patterns of regional price growth we would normally expect at this point in the cycle ”

With the exception of Scotland, where the market remained shut for longer than the rest of the country, price growth was far more uniform than in recent years. The perceived change in homeowners’ housing needs, brought about by the pandemic, was largely universal.

Though levels of activity varied between major cities, their suburban hinterland and more rural lifestyle-relocation markets, they increased right across the country.

As we look forward, the prospect of a prolonged period of low interest rates means there remains capacity for price growth across all markets.

In London and the South East, affordability has become less dictated by the finances of the average household over a number of years, as the market has become dominated by more affluent households. Such a change in buyer profile, combined with the increased role of equity as opposed to debt in house purchase, continues to deliver potential for price growth despite high average house price to household income ratios in these areas.

However, as lifestyle drivers increasingly give way to economic fundamentals, so we expect to return to the normal pattern of regional price growth that we would expect at this point in the housing market cycle. This is likely to be supported by the Government’s levelling up agenda, as shown in our regional price forecasts below.

Table 2 Regional house price forecasts

	2021	2022	2023	2024	2025	5 years to 2025
UK	**4.0%**	**5.0%**	**4.0%**	**3.5%**	**3.0%**	**21.1%**
North West	4.5%	6.0%	5.5%	5.5%	4.5%	28.8%
Yorkshire and the Humber	4.5%	6.0%	5.5%	5.0%	4.5%	28.2%
East Midlands	4.5%	5.5%	5.0%	4.0%	3.0%	24.0%
West Midlands	4.5%	5.5%	5.0%	4.0%	3.0%	24.0%
Scotland	3.0%	5.0%	4.5%	4.5%	4.0%	22.8%
Wales	3.5%	5.5%	5.0%	4.0%	3.0%	22.8%
North East	3.5%	4.5%	4.0%	3.5%	3.5%	20.5%
South West	5.0%	4.0%	3.5%	3.0%	2.0%	18.7%
South East	5.0%	4.5%	2.5%	2.5%	1.5%	17.0%
East of England	5.0%	4.5%	2.5%	2.5%	1.5%	17.0%
London	**2.5%**	**4.5%**	**2.0%**	**2.0%**	**1.0%**	**12.6%**

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

Source: Savills Research

Key forecast assumptions

- Unemployment peaks at about 6% over the summer
- Social distancing unwinds over the course of the year, in line with the Government’s plan
- The vaccination program continues as expected, and no significant disruption from new Covid-19 variants
- There is an economic bounce back in 2022
- Base Rate remains at 0.1% until 2024
- The stamp duty holiday in England and Northern Ireland tapers on 30th June and ends on 30th September. The furlough scheme ends on 30th September.

London in focus

For the first time since 1988, London is set for a fall in population, with residents seeking larger homes further out, and a number of overseas workers leaving the country.

While we expect to see an uptick in remote working, at this stage it is difficult to predict its scale. We expect accessibility to the workplace to remain a major consideration for most buyers, even if they are present in the office fewer days of the week. For many, such as those working in front-line healthcare or service jobs, working from home was never an option.

From a migration perspective, some overseas workers may find more hurdles to return, following the new immigration system with the EU. But we have already seen the fall in EU migrants offset by the rise in non-EU migrants at a national level. We expect this to continue. So, while the city’s population has taken a hit, this is likely to be temporary, and there will continue to be a significant demand for homes, driving growth.

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