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REAL ESTATE

Where next for UK residential transactions and prices?

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Eight-bedroom house for sale in Upper Phillimore Gardens, Kensington, London W8, price $39 million. Image courtesy of Knight Frank

By Liam Bailey

Our most recent forecast published April 6 assumed that a full lifting of the United Kingdom's COVID-19 lockdown would be achieved by the end of May.

The government's announcements this week has now confirmed the lifting of the lockdown will in actual fact run in stages through to at least July.

Our revised forecast published today adopts this latest advice from government and assumes that the U.K. will fully exit lockdown by the end of July.

In light of this change our view of residential transactions in 2020 remains unchanged, but we have made a downward revision for house prices.

Our view is that a decline of 7 percent in U.K. prices and 5 percent in prime London and prime regional prices will be experienced through 2020, with much of this decline already having taken place between March and May.

Context

There are some predictions of which we can be confident.

For example, we can be fairly certain that this year we will see one of the sharpest falls in economic growth in peacetime, both here in the U.K. and globally.

Equally, there are many predictions that are more uncertain.

While we know there will be a recovery, no one knows its shape or span. The key reason for this uncertainty is we just do not know the how economies will leave the current lockdowns.

If the U.K. appears to be struggling to navigate a way out, the lesson from Singapore, South Korea and even Germany confirms that almost everywhere is experiencing two steps forward and one step back when it comes to easing movement restrictions.

This uncertainly means that predictions for the housing market have to be read with extreme caution at a time when we cannot easily predict the ground rules under which the market is operating.

Current market activity

The lockdown, at least as far as the property market is concerned, has been very effective. Viewings are down 98 percent year-on-year, and the 2 percent that are taking place are virtual.

Alongside viewings: new buyer volumes are lower by 60 percent over the same period; new properties listed for sale are down 90 percent; offers made, down 80 percent; offers accepted, down 70 percent and exchanges are down the same amount.

To be fair, while all metrics are sharply lower, there is perhaps more activity than we initially anticipated back in late March.

Would-be vendors can take heart from the fact that, despite an effective lockdown of the market, a sizeable number of buyers are still registering their interest to purchase.

Facade of house for sale at Upper Phillimore Gardens, Kensington, London W8. Image courtesy of Knight Frank

Transactions

We last reviewed our forecast for the housing market in early April as the lockdown began to bite.

In terms of transactions, we noted that there were 1.18 million sales in the U.K. in 2019.

Prior to the arrival of COVID-19 we had assumed the "Boris Bounce" would lead to an increase this year to around 1.26 million.

During January and February, even this increase began to look modest.

However, with the arrival of COVID-19, we reduced our forecast to 728,000 sales for this year, a decline of 38 percent on 2019 levels. This new total represented around 500,000 missing sales compared to what we had initially expected.

Looking at the volume of activity that has occurred through lockdown, it might be that we were slightly pessimistic.

More sales have taken place, and fewer sales have failed to complete, compared to what we initially expected.

For now, we are content to leave our initial forecast unchanged as we discuss below there will be some additional challenges ahead for transactions from future pricing discussions.

Prices

Our previous forecast, which we published at the beginning of April, pointed to a 3 percent fall in U.K. house prices and no change in prime London prices.

This forecast assumed that the lockdown would be lifted in totality by the end of May, and also made the assumption that the 20 percent drop in prime London prices since 2014 would shield this market from further falls.

Since Sunday night (May 10) it has become clearer that some lockdown measures will remain in place into July and that social distancing rules governing day-to-day life, including property transactions, may remain in place beyond that.

It is challenging to get a handle on what is happening to pricing right now.

Published indices tend to be backward looking, and those that have been published since the crisis began have inevitably drawn on limited datapoints.

We can obtain some insight however from current activity in the market.

In late March residential exchanges were taking place at around 98 percent of asking price, an improvement on what had been experienced in 2019 when Brexit and electoral uncertainty weighed on the market. Right now, the ratio is around 95 percent.

So in very simplistic terms, and if we assume everything else remains equal, we might assume this represents a drop of 3 percent in prices in around six weeks from the start of the crisis. But many of these exchanges represent deals that were agreed four to six weeks ago.

We are however able to look at more timely data.

Of the offers being made by buyers, and which are being accepted, in late March, these averaged 98 percent of asking price. Right now, the average is around 94 percent, so representing a 4 percent drop.

If we allow for the fact that some asking prices have come down since March, then we might conclude that prices are off by 5 percent already since the beginning of the crisis.

Five percent seems like a reasonable starting point, and it is increasingly clear that prime London's five-year decline does not means it is immune from price falls.

However, I think it would be wrong to assume a continuation of the decline we have seen over recent weeks.

The key question is, will vendors accept discounts of more than 5 percent? Some will, but there is growing evidence from the widening spread between average offers and the offers that are being accepted that many simply will not.

If we add in to the mix the fact that we have low new-build rates coming through in 2020, low inventory and low interest rates, it becomes less likely we will see significant further falls from here.

OUR VIEW IS that as the market reopens in the next two months, the 5 percent fall in values we have seen since late March will be revealed in achieved pricing and while there could be some further downward pressure through to the summer it is likely to be limited and in prime London there is the potential for an uptick in the final two quarters of the year to offset some of the losses in the first half.

Our revised forecast for pricing during 2020 in the light of the longer lockdown is -7 percent for the U.K. and -5 percent for prime London.

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