

Spotlight

# The Global Financial Crisis

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10

YEARS ON

How the credit crunch transformed  
the UK housing market



# Credit. Crunched

The effects of the Global Financial Crisis, which began in 2007, are still being felt a decade later, and will continue to influence the housing market in the years ahead

“ The first of March this year marked the 10th anniversary of my career switch to a housing market analyst. Back then, the housing market was roaring, but within six months of my arrival it had been turned on its head as prices and transactions went into reverse. Fortunately, these two things were not connected. There were much bigger forces at play, forces which continue to shape the market today.

For many, the first-hand experience of the once-in-a-generation events of 2007 and 2008 will be etched into their memory. For twenty-somethings – who’ll be more reliant on the 2015 film *The Big Short* to understand the cause and impact of subprime lending – the legacy of these events will nonetheless be all too real.

As we discuss in our lead article (p4), what has since been named the Global Financial Crisis (GFC) has fundamentally changed the nature of the UK housing market. It’s made getting on the housing ladder heavily dependent on the Bank of Mum and Dad or Help to Buy, has meant homeowners trade up the housing market less often and has placed much greater demands on the private rented sector.

It has also meant that in just over 10 years, I’ve seen virtually every aspect of a housing market cycle. First, I witnessed unsustainable house price growth which preceded a rapid market correction. This was followed by a temporary bounce-back in values. Not long after came a second slip in prices as the realities of the changed availability of mortgage debt and the impact of austerity kicked in. Then came a more sustained housing market recovery that led to measures aimed at cooling parts of the market through mortgage regulation and taxation.

During the decade, there’s also been a wide variation in the performance of regional and local housing

markets. For a long time, it looked as if London was dislocated from the rest of the country, but now it appears to be hitting up against the borrowing constraints imposed through mortgage regulation.

What of the future? The longer-term impacts of the GFC are likely to be masked in the short term by the effects of political (and associated economic) uncertainty. House price growth is slowing and lead indicators suggest that market activity will weaken. During the next two years, sentiment looks set to be the main determinant of the market. However,

## The Global Financial Crisis has fundamentally changed the UK housing market

as the uncertainty gradually starts to clear, we can be sure that the fundamentals will come back into play.

The events of 2007 were the catalyst for the ultra-low interest rates which have persisted for a period few would have predicted when I was new to the joys of London commuting. When interest rates rise, we’ll see another side to the measures put in place to prevent a repeat of the GFC events. Stress-testing of mortgage affordability will take on a different dimension, acting as a more noticeable drag on UK house price growth.

You can bet that the events of the last decade will still impact the housing market in the next. ”

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### The Global Financial Crisis timeline

#### August 2007

BNP Paribas refers to a ‘complete evaporation of liquidity’, preventing investors from removing money from three of its funds



#### September 2007

Investors withdraw more than £1 billion from Northern Rock in just one day

# Side effects: four ways the GFC continues to impact the housing market

**F**or the UK property market, the short-term effects of the Global Financial Crisis (GFC) were dramatic and swift. The average UK house price fell by 20% in 16 months. Transaction levels, which had averaged 1.65 million a year in the previous 10 years, fell to 730,000 in the 12 months to the end of June 2009.

Ten years on, the crisis and its consequences have dramatically changed the property landscape. It was not until May 2014, for example, that the average UK house price recovered to its pre-credit crunch level, while transactions have only once risen above 1.3 million.

And, as we explore here, those events continue to have four significant impacts on the market and will shape it for many years to come.

## 1 There's been a dramatic slump in spending and transactions

In the year to the end of March 2017, the total spend on house purchases was £312 billion. Given persistently reduced transaction levels and changes in how they are made up, this is £30 billion less than was seen 10 years ago.

The amount funded by debt has fallen by even more, some £47 billion (see graphic, facing page). Now, debt accounts for just 43% of house purchase funding, with cash and accumulated equity the dominant source of funding.

This largely reflects the mortgage regulation measures that were introduced because of the credit crunch with the aim of preventing another debt-driven housing market boom.

### Average house price UK

2007: £181,180

2017: £209,971

### London

2007: £292,409

2017: £478,142

Source Nationwide

### % of lending at over 90% LTV

2007: 14.1%

2017: 3.9%

Source PRA/FCA

### Interest-only lending as a % of the whole market

2007: 32.5%

2017: 1.2%

Source CML

#### June 2008

The UK enters its deepest post-war recession. It lasts for five quarters



#### October 2008

Three Icelandic banks collapse. The UK Government announces a £50 billion rescue package for the UK banking industry



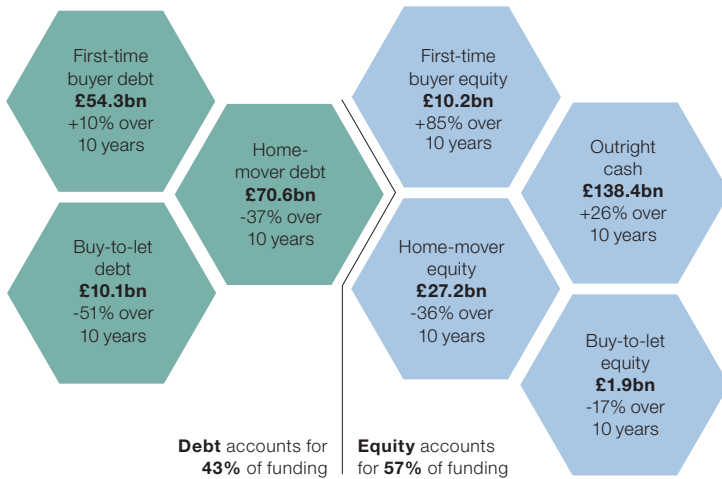
#### September 2008

Fannie Mae and Freddie Mac bailed out by the US Government. Lehman Brothers files for bankruptcy

#### February 2009

Average UK house prices bottom out, having fallen by 19.6% in just 16 months according to the Nationwide House Price Index

**Debt and equity** The source of funds for house purchase and the change over the last decade (10 years to March 2017)



Source Savills Research using CML and HMRC

## 2 The Bank of Mum and Dad has become a major player in lending

With limits on the amount people can borrow, the high deposit required by a first-time buyer presents a significant barrier to younger households buying their first home.

That said, the amount of equity put down by first-time buyers exceeded £10 billion in the year to the end of March 2017, an 85% increase on 10 years ago. A lot of that, some £4.2 billion in England alone, is provided by the Bank of Mum and Dad or Help to Buy. Parental funding and government support are now heavily relied upon to help younger generations to get on the housing ladder. It is unlikely to change.

Occasionally, we read about the return of the 95% or 100% mortgage. However, gross mortgage lending at loan to values above 90% is still less than one-fifth of the £52 billion it was in 2007. Now, it represents less than 5% of mortgage lending.

A further consequence of this has been continued growth in the private rented sector. More people, across an increasingly wide social spectrum, are renting for longer. The demands on that sector will continue to evolve. >

### Average first-time buyer deposit

UK

2007: £12,556

2017: £26,224

London

2007: £21,196

2017: £97,513

Source CML

### Average first-time buyer income

UK

2007: £34,200

2017: £40,002

London

2007: £51,681

2017: £64,263

Source CML

### UK housing transactions

Total in 2007: 1.7m

Total in 2017: 1.2m

Source HMRC



#### March 2009

Bank base rate is cut for the third month in a row to just 0.5%

#### June 2009

Annual housing transactions fall to 730,450 – dropping 58% from their August 2007 level

#### April 2009

The G20 agrees a global stimulus package of \$5 trillion. It equates to almost 70% of the total value of UK housing

#### September 2009

The UK economy returns to growth in the third quarter

## Average mortgage for home movers

UK

2007: £130,699

2017: £174,999

London

2007: £208,699

2017: £345,399

Source CML

## Existing mortgaged home owners moving house

2007: 1 in 15

2017: 1 in 27

Source CML

## Average mortgage rate for new lending

2007: 5.52%

2017: 2.07%

Source Bank of England

## Average mortgage interest as % of income

2007: 16.8%

2017: 7.4%

Source CML

## 3 There are now fewer rungs on the housing ladder

The debt taken on by home movers, which exceeded £112 billion 10 years ago, now stands at just £70 billion, a 37% decrease. This reflects a situation where people are trading up the housing ladder less frequently.

Compared to the preceding decade, when households could aggressively trade up the housing ladder, there have been 3.8 million fewer such moves by those needing a mortgage in the past 10 years. Any recovery in these numbers has been muted, suggesting this is likely to become a permanent feature of the market.

Long gone are the days where an interest-only mortgage would facilitate a move to a bigger, better property. Interest-only mortgages – which accounted for one-third of all new loans in 2007 – now represent just 1.2% of all lending to home owners.

Not only must home movers factor in the cost of capital repayments when they consider the affordability of making their next move, they also need to have paid off more of their existing mortgage debt and spent longer accumulating equity in their current home.

## 4 Buy-to-let mortgages have been squeezed back to 2007 levels

The army of small buy-to-let investors are now also within the scope of mortgage regulation. Portfolio landlords will follow shortly. This has come on the back of more politically motivated increases in stamp duty charges and restrictions of tax relief on interest payments.

Some thought that the combined effect of these measures would result in an exodus from the sector, with landlords cashing in. Instead, it has curtailed buying activity of those needing a mortgage to fund their next (or first) investment.

In the year to March 2016, buy-to-let lending was effectively back to where it was in 2007. Now it is at half those levels. This effect is likely to become even more entrenched as the progressive reduction in tax relief combines with rising interest rates to squeeze affordability.

Much like the rest of the market, cash has become king. With the Bank of England recently acting to ensure that mortgage regulation will be consistently applied by all lenders, across all aspects of the market, that is likely to be the lasting legacy of the credit crunch. ■



### April 2010

UK house price growth exceeds 10% according to Nationwide, as the market temporarily bounces back. Greek debt is downgraded to junk

### June 2010

Prices in prime central London return to their pre-GFC peak, having risen 25% in a year

### December 2009

The average first-time buyer deposit peaks at more than £35,000 according to the CML, £22,000 more than in August 2007 and £11,000 more than today



### May 2010

A Conservative-Liberal Democrat coalition is formed following the 2010 general election

# House price growth: a dividing decade

House prices have risen in most UK regions during the last decade, but a closer look at the figures reveals wide divisions

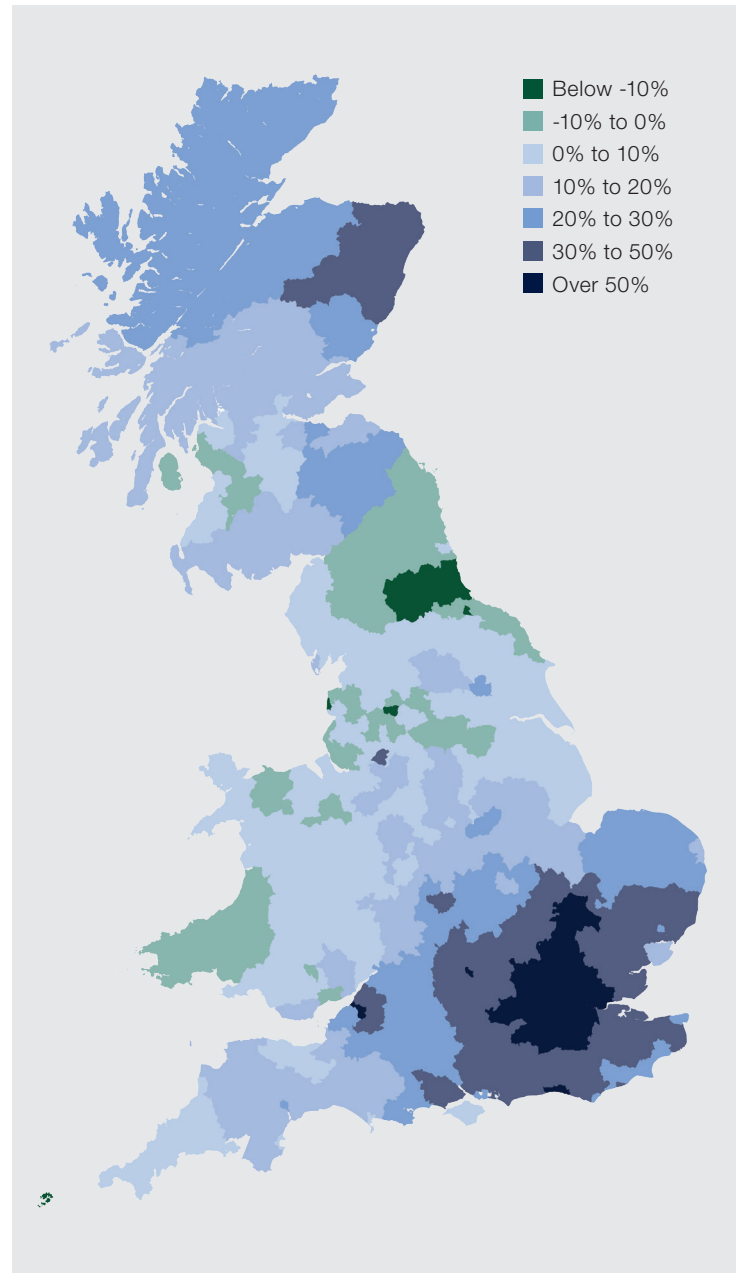
According to the Nationwide, the average UK house price is only 18% above where it was 10 years ago. On an inflation-adjusted basis, the effect of the Global Financial Crisis means the average UK house price is 11% below its 2007 level.

This has occurred despite a prolonged period of abnormally low interest rates. In August 2007, the average interest rate for a new mortgage was 5.88%. Now, it stands at just 2.04%.

Of course, house price averages are misleading. The Savills Repeat Sales Index uses price-paid data from the Land Registry and Registers of Scotland. Across the country as a whole, it broadly concurs with the Nationwide figures. But it also shows wide regional and local variations in the nominal (non-inflation-adjusted) levels of house price growth reported below.

It suggests that prices in London have risen by 78% on average in the past 10 years. In the North East, though, they have fallen by 9%. The extremes are prices in Hackney, which have risen more than 120%, and Hartlepool, which have fallen by 24%. There is a north-south divide, but the picture is far more nuanced than that. >

House price growth 10 years to March 2017



Source Savills Research using HM Land Registry and Registers of Scotland



## July 2012

London hosts the Olympic Games. Mainstream house prices in the capital have recovered to within 1.4% of their 2007 peak, though annual house price growth in the capital slows to 1.1%

## September 2013

Annual housing transactions exceed one million for the first time since October 2008. That's still well below the 10-year pre-crunch average of 1.65 million

## January 2011

Annual UK house price growth slips back into negative territory according to the Nationwide

## March 2013

George Osborne launches Help to Buy in the budget. It provides for equity loans to buyers of new build property and mortgage guarantees for higher loan-to-value lending

## March 2014

The Help to Buy equity loan scheme is extended to 2020

**London as an island**

Price growth in London has far outstripped areas beyond the M25. Over 10 years, London price growth has essentially been twice that of the South East.

Consequently, London buyers appear to be hitting against the limits of mortgage regulation, with fewer buyers confined to more affluent households, stretching their borrowing to more than four times their household income and buying in areas they would not have considered pre-Global Financial Crisis.

Some urban markets such as Oxford, Cambridge and Brighton have parallels with London, both in terms of the price growth and the affordability issues they now face.

In addition to the usual suspects such as St Albans and Elmbridge, which have always attracted a flow of equity out of the capital, we have also seen prices in lower-value commuter towns such as Slough, Stevenage and Harlow rise 50% in the past decade, as investors and homeowners have looked to stretch their mortgage further.

But the gap between London and its hinterland has widened considerably and has only recently shown any sign of narrowing.

**The gap between debt and equity**

Moving away from London, the difference between equity-rich and more mortgage-dependent markets has been noticeable.

In Bristol and Bath, 10-year price growth of 48% and 41% respectively has not just been stronger than the average for the South West, but also the South East, while markets such as Gloucester and Great Yarmouth have prices that are no more than 15% higher than they were in 2007.

In the Midlands and the North, markets such as Trafford, Rushcliffe and York are poles apart from Blackpool, Blackburn and Burnley in relative terms, but here the differences are between a price growth of 20 and 30% for the former and net falls of 10 to 20% for the latter.

North of the border, price growth of 28% in Edinburgh has been twice that of Scotland as a whole. Fuelled by its local economy, Aberdeen had price growth of 44% between March 2007 and March 2015, but prices have fallen 9% since then with the oil price, so growth over the 10 years has been 35%. ■

**A focus on the future**

**Short term** The market is likely to be largely driven by sentiment with price growth suppressed by political and economic uncertainty. London is expected to be most exposed, given the sheer scale of the financial commitment which a mortgaged house purchase now represents in the capital.

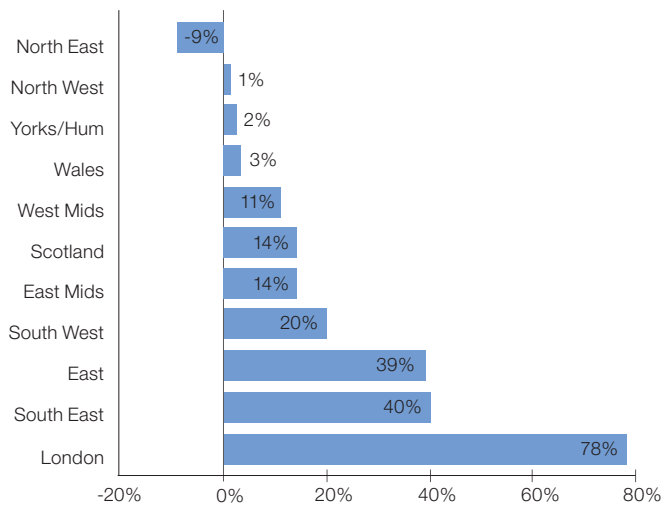
**Longer term** The cost of mortgage debt will be key even though the UK housing market has become increasingly driven by equity.

When rates rise, we expect a squeeze on affordability. Stress testing of household finances is expected to act as a drag on growth.

Recent evidence gives us clues as to the geographical distribution of that price growth. Those on the first rungs of the housing ladder are likely to want to stretch their money further, particularly in London and increasingly across the south of the country. In many cases, that will push them into the 'next-most-desirable' markets, that are more affordable and accessible than their first choice.

Equity generated in the London housing market among older households is likely to continue to be exported into the commuter zone. Across other parts of the country, we expect the legacy of the credit crunch to favour more valuable equity-rich markets, with lower-value areas dependent on the strength of the local economy.

**10-year house price growth to March 2017**



Source Savills Research using HM Land Registry and Registers of Scotland

**April 2014**

Mortgage Market Review brings in new lending regulations for home buyers. They include stress testing of affordability, as house price growth again moves back into double-digit territory

**December 2014**

Stamp Duty Land Tax is overhauled by removing the unpopular slab structure and reducing the liability for 98% of the market



**June 2014**

Annual house price growth across London stands at 25.8% according to the Nationwide



**May 2015**

The Conservative party secures an outright majority at the general election



# Approach with caution

As the effects of the Global Financial Crisis evolve, political and economic uncertainty has created a greater sense of caution in the UK housing market

**A**lthough this report chiefly focuses on the long-term impact of the Global Financial Crisis, recent economic and political uncertainty has contributed to a noticeable slowdown in rates of house price growth across the mainstream UK housing market.

According to the Nationwide Index, annual house price growth had fallen to just 3.1% by June 2017, from 5.1% a year earlier. Similarly, Halifax put it at 2.6%, down from 8.4% in June 2016.

The RICS Housing Market Survey suggests that numbers of both new buyer enquiries and properties being brought to the market are contracting as buyers and sellers become more cautious. That feeling has

been compounded by a slight squeeze on household finances, as inflation outstrips wage growth, and the increased tax burden faced by buy-to-let investors.

The unexpected result of the general election, which has resulted in a hung parliament just as Brexit negotiations commence, means there is little to suggest this picture will change in the short term.

Indications of an interest rate rise in the next six to 12 months will only add to this caution. However, underlying affordability of existing mortgage debt is unlikely to become an issue, so we expect price growth to continue to slow rather than go into reverse.

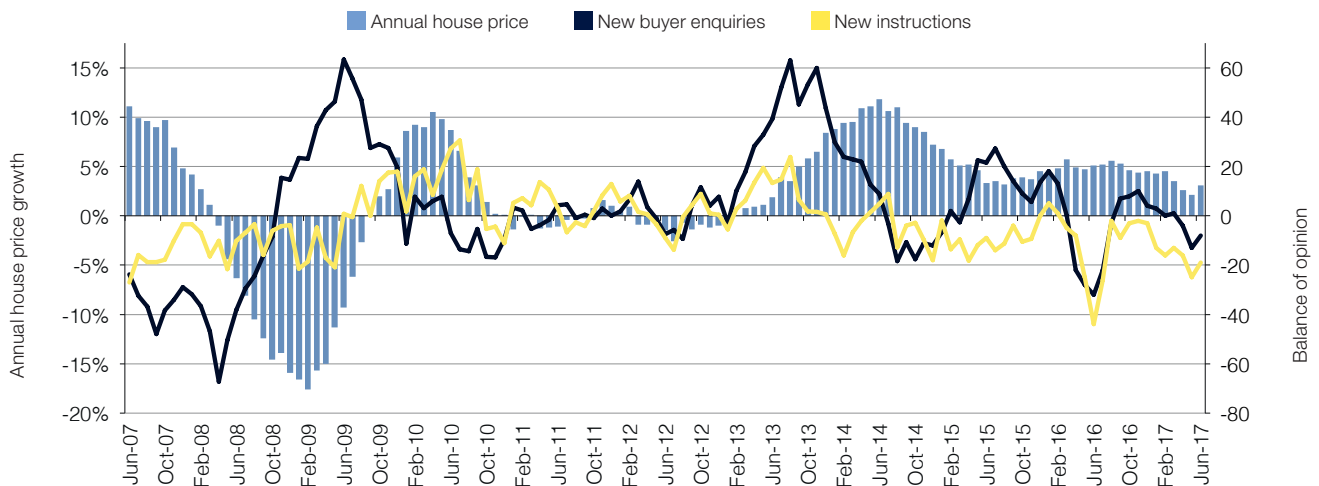
All of this suggests that we will return to more of a needs based market during the next two years.

## Mainstream house price growth (year to June)

UK 2016: 5.1% 2017: 3.1% London 2016: 10.0% 2017: 1.3%

Source Nationwide

### Market caution Annual UK house price growth, new buyer enquiries and instructions



Source RICS and Nationwide

#### August 2015

Annual UK house price growth falls back to 3.2% as mortgage regulation cools the market



#### June 2016

Britain votes to leave the EU

#### March 2016

Annual housing transactions reach a post-downturn peak of just over 1.3 million, boosted by a rush of investors seeking to avoid the 3% additional homes stamp duty surcharge

#### August 2016

UK bank base rate is cut to 0.25%

# Finding balance

Following a period of price adjustment and uncertainty in prime central London, values are starting to find a more balanced level

**S**ubdued buyer confidence in the mainstream housing market (see p9) has been compounded by high stamp duty costs at the top end. This is most evident in London, where prices peaked in September 2014 and have fallen by an average of 6.9% since.

In the prime central London market, the weakness of sterling has been offset by greater exposure to capital gains tax and inheritance tax for overseas buyers. Price adjustment has been greater and, with values having fallen by more than 14% in this area, they are now back at December 2011 levels.

From March to June 2017, prices slipped by 1.3%. Although not significant, it is reflective of the price-sensitive nature of demand that has become the norm.

Outside the capital, the effect of taxation has been less significant. Here, the incidence of stamp duty is less acute and there was also weaker growth in the run up to the tax changes of two and half years ago. Still, annual price growth only averages 0.9%.

The increased popularity in prime urban property throughout and beyond the London commuter zone means the price gap to prime rural homes remains wide. Consequently, farmhouses, rectories and manor houses all look good value.

Across the prime market, sellers are increasingly aware of the need to match asking prices with buyer expectation. So, even with a thinner seam of demand, the right property at the right price continues to sell.

**Role reversal** Prime house price movements in other regions of the UK have recently been outperforming London and its suburbs

	Quarterly	Annual	Since Sept 2014
Central London	-1.3%	-6.8%	-14.1%
Other London	-0.7%	-4.7%	-3.4%
Suburbs	-0.3%	-0.9%	0.7%
Inner commute	-0.4%	-0.5%	3.3%
Outer commute	-0.6%	1.0%	6.3%
Remainder of South	0.5%	2.3%	7.5%
Midlands and North	0.4%	1.9%	3.4%
Scotland	0.2%	1.1%	1.5%

Source Savills prime indices, Q2 2017

## January 2017

Tighter mortgage regulation is introduced for the buy-to-let sector



## June 2017

The Conservative party fails to win an outright majority in a snap general election. Annual UK house price growth stands at 3.1% according to Nationwide, while growth in London slows to 1.3%

## September 2016

Government announces that the mortgage guarantee element of Help to Buy will not be extended for 2017

## March 2017

The UK government triggers article 50





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