



## Pundits expecting house price collapse will look like turkeys by next Christmas, unless the pound really fowls up

In January of this year, one of the gloomiest months of this recession, cebr released a house price forecast which said something which seemed to us quite obvious – that the outlook for house prices in 2009 would be fundamentally affected by the volume of mortgage lending. At the time, mortgage approvals had hit rock bottom and were skirting along at about 30,000 per month according to the Bank of England statistics – this compares with an average of around 92,000 per month over the last fifteen years.

Our house price forecast predicted that if mortgage approvals improved fairly quickly to around 55,000 per month – still much lower than the long run average – prices would fall in the first half of the year but would then start to rise such that by the end of 2009 average house prices would be roughly the same as they were at the end of 2008. Now I am first to admit that this wasn't cebr's central scenario, but this particular scenario that was published in our January 2009 edition of *Consumer and Housing Prospects* turned out to be pretty much spot on. What this demonstrates is that house price forecasts must take account of not only broad macro-economic factors, but also micro factors such as mortgage lending and the supply side of the market.

Some house price experts only take account of macro factors, and some would even have us believe that there is some fundamental long term ratio between average incomes and house prices, that virtually rules out every other factor.

The same experts have for years been telling us that house prices are set to fall by over 30 per cent, a prediction that gets recycled over and over again, thus getting further and further from being right. Even during this – the housing market crash to end all crashes – prices fell by 22 per cent from peak-to-trough, but now stand just fifteen per cent lower than the end of 2007 peak. These experts are also telling us that next year house prices will fall back significantly. **We think this is an unlikely outcome for a number of reasons, despite our predictions for a weak economic recovery and unemployment rising further.**

Firstly, mortgage lending will continue to improve slowly but steadily as banks continue to rebuild their balance sheets. In addition we expect the price of mortgages to remain relatively low as the MPC keeps interest rates on hold at 0.5 per cent, **unless the precarious public finances lead to a sterling crisis which forces the MPC's hand.**

Another factor is the supply side. Many experts are pointing to the current shortage of supply on the market as a reason for the recent bounce in house prices, but most seem to think that this is a temporary issue. **However, they conveniently forget that possibly the biggest victim of the credit crunch was the housebuilding sector.**

DCLG statistics show that housing completions fell by eighteen per cent in 2008, and are likely to fall a further nineteen per cent in 2009 to just 115,000 completions. This compares with government targets of 240,000 housing completions per year to keep pace with demand – the closest we got to this figure in the last 20 years was 175,000 in 2007. As long as housebuilding does not keep up with household formation, **the supply side imbalance will continue to act as a driving force for house price growth. The dramatic collapse in housebuilding in the last two years will feed through into prices over the next five years.**

Taking all of these important factors into account, **our central prediction is that house price growth will moderate in 2010**, with prices at the end of the year being **between two and four per cent higher than today**. Over the longer term, the weak recovery will continue to hold growth back, **but we still expect house prices to be around fifteen per cent higher at the end of 2012 than they are today.**

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