

FEAR AND NESTING

THE EMOTIONAL AND ECONOMIC DRIVERS OF THE HOUSING MARKET IN LONDON AND THE SOUTH EAST

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In summary

Housing prices in London and the South East now sit ahead of their former peak. As London's international economy continues to draw in highly skilled workers, the pressure on housing in the capital will intensify and, in the absence of step change in residential development in the wider region, rents and capital values will move further ahead of incomes. These conclusions were set out in research undertaken on behalf of Cluttons by Professor Ball (2012, 2013), which highlighted the economic implications for London as the cost and quality of housing dampen the capital's ability to compete for the best workforce.

This paper, based on a large-scale survey of a cross-section of tenure and socio-economic segments of the population in September 2013, looks at the individual stories that make up the market. It seeks to understand the drivers of behaviour in the London and South East housing market.

Practical lifestyle issues, in particular buying a first home as a couple and having more housing control, are the primary drivers for buying amongst those who do not already own a home. But, the desire to save on rent and get on the housing ladder before prices rise any further were equally important.

Tenant buyers depend on financial help to purchase a home. Help to Buy is influential amongst this group, but other strategies such as buying with another person, not as a couple, in order to get on the ladder are also being employed. However, familial financial assistances are commonplace with a third of buyers dependent on this help. Downsizing and equity release accounted for 20% of purchases over the last 12 months, suggesting a degree of equity transfer between generations to facilitate the acquisition of a first home.

Existing homeowners in the region are also struggling to afford the next rung in the ladder, with lower earners in particular still dependent on family financial assistance. However, at the other end of the scale, a significant proportion looking to buy does not require a mortgage, reflecting moves out of London and downsizing.

Tenants who are not actively looking to buy generally aspire to be homeowners (66%), but 53% do not think they will be able to afford to, at least in the next five years. While a segment of social tenants are very content with renting and the flexibility and security the sector offers, tenants generally look to home ownership to provide greater control over their housing situation and aspire to make their home their own. There is an opportunity for an alternative rental model that meets these basic human responses.

However, the view predominately held across all tenure groups and housing situations is that residential in London and the South East is a good investment and will rise in value ahead of salaries over the next decade. This is the overwhelming driver of behaviour and aspiration in the market, with implications for individuals and the economy.

The context

We are on the eve of the six year anniversary of the peak of the market prior to the financial crisis that has defined so many aspects of our lives. However, despite the magnitude of this event, prime Central London house prices have shown a remarkable improvement, now standing 13.4% ahead of that peak (Cluttons). This recovery is

evident beyond the central prime markets, with prices in Greater London and its Outer Metropolitan areas standing 5% and 2% ahead of their former peaks respectively (Nationwide) (Figure 1).

The rental market has shown a more rocky recovery, with a bubble of growth during 2010 and 2011 giving way to rental adjustments. However, rents across the capital have now stabilised and have returned to their trend trajectory. Over the summer we saw a sharp increase in demand across prime Central London driven in large part by a recovery in recruitment in the financial services sector. With signs of a sustainable pattern of economic growth not only in London but across the UK, the challenge of living in and around London will become a growing issue.

The housing challenge

This issue was considered in detailed research undertaken for Cluttons by Professor Michael Ball of Henley Business School, University of Reading. The results of this work were detailed in two papers published by Cluttons: One size does not fit all: diverse opportunities in London's rental market and Renting in London: the coming boom. The research considered the drivers of housing demand in and around London over the next decade. In analysing the prospects for employment and business growth trends in the capital, Professor Ball identified two key factors that will frame price pressures going forward.

Firstly, from a demand perspective, there will be an increase in higher skilled workers sought by the range of global businesses that will continue to agglomerate in London. These workers will be more international, footloose, younger and importantly, wealthier. This will add to demand pressures in London, with higher incomes and a younger, more international population impacting on housing expectations in terms of size, quality and location. Secondly, the supply capacity of London and the South East is highly restricted physically and politically, with development contained by both the greenbelt and aversion to development in many areas of the Home Counties that provide the potential residential spill-over land for London. The inevitable result of these dual pressures on demand and supply is a housing shortage, which Professor Ball concluded will have the effect of accelerated house price growth in London and a dampening impact on the capital's economic growth. This will occur as a result of internationally footloose staff, and therefore businesses, opting for alternative global locations where the simple function of living is less of a grind.

Looking beyond the short to medium term forecasts that are commonplace in the market, Professor Ball's research drew the conclusion that residential values in the capital will grow well ahead of incomes over the next decade. Aligned to this the research also surmised that as a result of the expected escalation in residential values in the capital, an expanding segment of the population will be excluded from home ownership within its sphere of market influence; that is within much of the south east commuter belt. This will inevitably result in greater demand for rental accommodation in and around the capital, not just the younger cohorts, but in a growing number of instances throughout a person's full housing life cycle.

Policy response

This clearly presents challenges for central and local government, as well as housebuilders and other providers in the private and social rented sector. There have been initiatives to address the challenge, both on the demand and supply sides of the equation. The Help to Buy scheme and its planned extension, combined with financial support directly from homebuilders, including New Buy, have facilitated first home purchases and moves further down the chain. An easing in mortgage conditions and continued historically low rates have also had a major impact (Figure 2).

However, the well intentioned support to households looking to move on with their lives following a five year market demand impasse will have the inevitable side effect of driving further price growth, unless supply at least keeps pace. Measures have been introduced in this respect, ranging from an easing in domestic permitted development rights, financial incentives for local communities who support housing development, to a London wide strategic housing plan driven by the Mayor of London. We have seen a sharp upturn in housing starts over the last year, albeit on the back of an historical low base of activity

Figure 1. Average residential values, 2007-2013

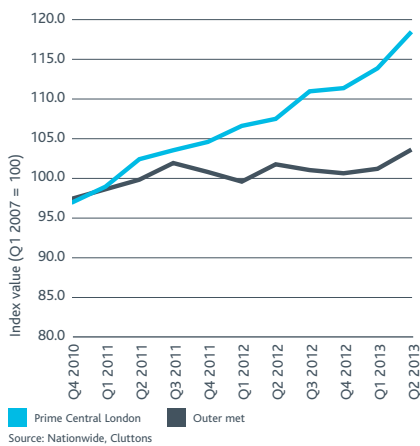
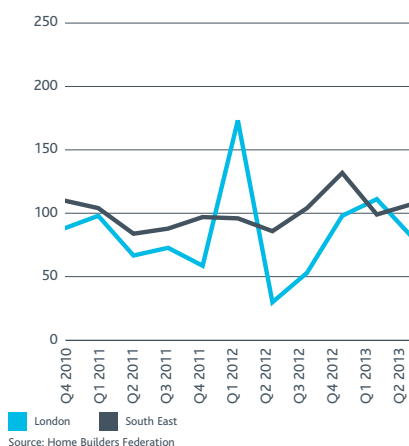


Figure 2. Number of housing projects securing detailed planning approval



as well as relaxation in traditional planning laws governing the conversion of commercial buildings to residential usage. However, despite this, the pace of building in London and the south east remains critically short of that needed to sustain London’s economic growth. Increasingly, supply is inevitably a greater challenge for both practical and political issues and therefore households in the region are facing a mounting housing challenge, in the short to medium term at the very least.

Understanding the multiplicity of housing stories we call the market

Given this intractable backdrop, we have taken forward our programme of research on the future housing story for London by turning our attention to the drivers of individual decisions to buy, rent and move. Establishing the individual narratives that make up the market enables us to more effectively understand the overall trends, challenges and the opportunities presented by specific market segments.

In order to achieve this, we surveyed nearly 1,800 persons, achieving a sample representative of age, gender and socio-economic group in each of the geographical areas included in the study. The respondents comprised a range of housing situations; living at home with parents, renting in the private or social sector and owner occupation. We included sub-samples of those currently looking to purchase a home and those who purchased within the last 12 months. Geographically, we covered London and the Home Counties. The online survey was undertaken on our behalf by Morar Consulting during September 2013.

Coupling up and getting on the ladder

London and the South East is quite unlike the rest of the country in terms of its tenure makeup. Inner London comprises a significantly higher proportion of private and social renters relative to the national average, while in the South East region nearly 70% of households are owner occupiers, with almost half this number owning their home outright (ONS) (Figure 3). As a result, across the London and South East region as a whole, for most people, the home in which they live is their largest financial asset. There is inevitably a non-monetary or emotional element to decision making about purchasing a home. However, unlike a pension or other financial investment, the emotional and investment imperatives are intertwined. Figure 4 presents the reasons why buyers who do not currently own a property are buying a home. The size reflects frequency of mention.

Figure 4.



Our research clearly demonstrates this complexity. The survey found that for buyers in the market who do not already own a home, practical lifestyle issues combined with financial factors are the most important reasons for buying. This is demonstrated by the points noted by respondents, but brought out in more detail in the analysis of their views. Tenants looking to buy were asked about the most important reason for buying a home. Issues surrounding life changes were found to be a key driver as is to be expected. Buying a home as a couple and the need for more space were noted by 22% and 12% of respondents respectively. This reflects the profile of the respondents, with 57% buying as a couple. Notably, buying a first home as a couple was noted as the prime driver of 30% of those currently living at home with parents, highlighting the importance of the family home in providing accommodation of young adults up until they 'settle down' and purchase with a partner. Aligned to this, the survey also brought out the desire for greater control over housing situations, which was noted as a top three driver by over half of tenants currently looking to purchase a home, with little difference between those currently living in the social and private rented sectors.

Figure 3. Tenure profile in London and the South East, 2012

	Own outright	Buying with mortgage	Social rented	Rented from employer or other	Rented from private landlord
Inner London	15.1%	22.2%	33.1%	2.4%	27.1%
Outer London	26.7%	34.1%	17.0%	1.9%	20.4%
South East	33.3%	35.4%	13.5%	2.3%	14.5%
UK	31.7%	32.4%	18.0%	2.0%	15.4%

Source: ONS, 2013

Financial issues are equally high on the agenda amongst tenants currently looking to purchase a home. 54% noted the desire to save on rent in their top three drivers, although this was particularly the case amongst those renting privately. Anxiety over rising prices and a desire to get on the property investment ladder are also primary drivers of the decision to buy now. Amongst tenants actively looking to buy, 35% noted a concern about buying before prices rose any further within their top three reasons for buying, again with little variation between the tenant type. This anxiety is consistent across the region, with no difference with those living within Zones 1 and 2 and those living in the Home Counties. Aligned with this, the major concerns expressed by tenants planning to buy were found to be overwhelmingly focused on affordability and cost (Figure 5).

Figure 5.



Bank of Mum, Dad, Gran, Granddad and others

Just over 90% of tenants actively looking to buy a property are first time buyers and are employing various strategies in order to get on the housing ladder in order to pre-empt further price rises. 17% of tenants actively looking to buy a home stated the desire to take advantage of the Help to Buy scheme as a top three driver, while 5% of tenants actively looking to buy were planning to purchase with another person, other than a partner (Figure 6).

More significantly however, 36% of tenants actively looking to buy a home will receive financial help with their purchase, with parents providing support in three-quarters of cases, but grandparents and others also playing an important role. Even for older purchasers (over 45 years) financial assistance from family will be provided in over a quarter of cases. The results suggest that this may in part be viewed as an investment by those family members providing the financial support since amongst those buyers not taking out a mortgage, family financial help will be provided in 43% of cases.

The role of financial help from family in the operation of the current housing market in London and South East can also be considered against a small, but notable proportion of downsizing activity which may be linked in part to funding home purchases for children and grandchildren. Of the survey respondents who bought a home in the last 12 months, 10% stated that downsizing was one of main factors driving their buying decision. Of those currently looking to buy a new property, the release of equity from their home, or downsizing were major drivers of the decision in 20% of cases. In fact, 12% of respondents stated one or other of these issues was their primary driver. That said, respondent comments also documented cases where more space was needed to accommodate aging family members, highlighting the duplicity of space and financial pressures across generations.

Those on the ladder still need strategies to move

However, it is not just first time buyers and those moving from the rental market into owner-occupation who expressed anxiety about the market. The majority of this group, as would be expected, are purchasing as a couple (66%), with 33% on their own and the remainder "coupling up" with another party. When unprompted, buyers in this category stated the main reason for their purchase is a need to change their physical space, whether larger, or indeed smaller (Figure 7). The need for more space was noted as the most important driver of the decision to move by 34% of respondent home owners. Relocation was also a key driver, with 23% of respondents stating this as their most important motivator. This was particularly the case amongst respondents in the outer London commuter zones and in the Home Counties.

Figure 6. Family financial help received by current home buyers

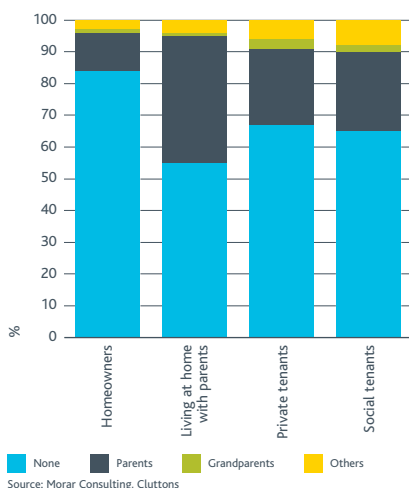


Figure 7.



The majority of existing home owners looking to purchase a new property intend to do so with the help of a mortgage (65%), although a significant number will be cash buyers. However, family support still plays an important role amongst this group, with 16% receiving financial help with their purchase from family, predominately parents, or others. Notably, those buying with a mortgage are also taking greater help from family, when compared to cash buyers. A higher proportion of those on lower incomes are, as would be expected, beneficiaries of this financial help. Specifically, 21% of those on a household income of less than £40,000 per annum received help from family.

The head and heart of home buying

The results of this survey demonstrate the understandable emotional aspect of the home and the buying decision. However, it also identifies the parallel issues of how those in the market, whether able to buy, or not, keep an eye on prices and their movement. There is a consistent view across all tenure groups, whether planning to buy, or not, that home ownership is a 'good investment for the future' with over 80% of respondents agreeing with this statement, with relatively little variation around this average. This is consistent with existing published research which has found that residential property is increasingly seen as an investment, rather than a consumption good, and contributes to a household's financial planning (Smith and Searle, 2006).

While the practical issues of space and life events are primary drivers of the 'why', anxiety over pricing appears to be underpinning the 'when'. The fear of house prices moving out of reach is a key driver of the London and South East housing market at present. The survey results identify a strongly held view that house prices in London and the South East will rise more than earnings over the next decade with 72% of respondents agreeing with this statement (Figure 8).

The Help to Buy scheme has, over a short period, become a notable incentive and aid to home purchases in the region, providing a particular incentive to social tenants, a quarter of whom are currently looking to buy and note this as an important driver, compared to 15% of private tenants and those living at home. However, the results of the survey suggest that without the financial support of family, even those on median incomes find themselves excluded from home ownership in many areas of the region. Unaffordable house prices are the overwhelming reason given by tenants as to why they do not intend to purchase a home, with the proportions in the private and social rented sectors, and those living at home, at 75%, 72% and 65% respectively. In fact of those that intend to buy in the future, private tenants believe it takes them an average of 8.5 years to be in a financial position to do so, while those in the social rented sector estimate over 10 years. A third of private tenants and two thirds of social tenants in the region never intend to purchase a home, although this group is dominated by those over 45 years of age.

Can new investment models provide homes for the excluded?

What are the implications for this cohort of unlikely, but aspirational homeowners? Certainly those with lower household incomes are the most likely group to consider moving to elsewhere in the country, if they were to buy. In fact, 53% of those who would like to become a home owner, but do not think they will manage to buy within the next five years, suggest that they would move away from the South East if they were to buy. However, this strategy must inevitably be set against employment opportunities and their accessibility, as well as family roots and the infrastructure they provide.

The survey finds that the current private rented sector (PRS) serves particular households well. Amongst private tenants not actively looking, particularly the young, there is less

Figure 8. Attitudes to home: the top 5 drivers

	% that strongly agree or agree with statement
Home ownership is a good investment for the future	77
Personalising my home is a benefit of owning a home	74
House prices in London and the SE will rise more than earnings over the next decade	72
Home ownership provides greater security over your housing situation	72
Paying rent is a waste of money	60

Source: Morar Consulting, Cluttons

anxiety over security of housing situation and a tendency to view renting as offering a more hassle free lifestyle. The growing professionalisation of the PRS over recent years amongst the new breed of investor landlords, has resulted in improved quality, services and security. This meets the needs of this cohort who generally view it as serving a purpose for a period of time. This ticks many of the boxes for the younger, more mobile renter, who has the desire and financial capacity, potentially aided by family help, to buy when they 'settle down'.

That said, there is a segment of social renters who do not intend to buy and significantly, are comfortable with their arrangements. They generally are less concerned about the need for home ownership to personalise their home, while considering the rented sector to offer a hassle free lifestyle and provide greater locational flexibility. This group also believe the cost of renting to be lower than buying and do not see rent as a waste of money.

However, with the exception of this particular segment of renters, the research finds that where the rental market will be a long term reality for a household, much of the current offer in the market is found to be lacking. The survey underlines the emotional aspect ascribed to home ownership: people of all profiles seek long term housing security and a place they can personalise to make their own. There are multiple implications of this. Shared ownership clearly offers one option, both within the social and the private housing markets. However there are also implications for private residential landlords in finding a model in which tenants can make their space home. The survey findings show that this is not simply a matter of offering a long lease on existing terms. A FRI (fully repairing and insuring) long leasehold model taken from the commercial market may present ideas for alternative models of tenure, offering a different risk return profile.

However, the distinction between emotional and investment drivers is important to the understanding of the housing market in London and the South East. The survey demonstrates an overwhelming desire for home ownership and it also highlights the importance of the fundamental human response in terms of wanting control over housing and ability to personalise one's space. But, consistent across all respondents, even those very comfortable and satisfied in the social rented sector, is the view that residential property in London and the South East is a good investment. The consistency and strength of this view suggests it eclipses the emotional factors, spurring home purchase decisions when perhaps the timing may not sometimes be right from a financial, or personal perspective. The market that is driving such behaviour does not of course only present dilemmas and compromises at the individual household level. From a wider economic standpoint, considerable research¹ points to the negative impact of home ownership on labour flexibility and as such, is an issue for the region and country as a whole.

¹ For example, the recent paper by Blanchflower and Oswald Does High Home-Ownership Impair the Labor Market?, May 2013.

Contacts
Sue Foxley
Research Director, Cluttons
sue.foxley@cluttons.com
+44 (0) 207 647 7023