Carter Jonas

RESIDENTIAL BRIEFING NOTE

July 2020

Market Overview

Many parts of the economy have now moved into the recovery phase of the downturn, albeit in some cases the rebound might be slower than most had hoped. May's GDP growth was lacklustre but let us recall that May's Purchasing Managers Indices were also disappointing before showing strong resilience in this month's (June) data. Retail sales however are now very close to their pre-pandemic levels with a 13.9% rise in June following May's (upwardly revised) 12.3% increase, both of which defied market expectations.

In the residential market our own Carter Jonas offices have seen a very strong return in demand over the last eight weeks, even before the stamp duty holiday was announced, and the wider housing market generally reports enquiry levels and new instructions at rates well above last year, and much greater than what would normally be seen at this time of year.

Executive Summary

- *May's GDP growth of 1.8% was hardly the start to a 'V-shaped' recovery that many had hoped. But parts of the economy only reopened halfway through the month so there will hopefully be a more notable rise in June as even more industries reopen.*
- *June's Purchasing Managers Indices are perhaps the first to show a stronger recovery, all three of which increased by larger-than-expected numbers.*
- *Consumers are slowly but surely regaining confidence in the market, although this is from a record low base. At -27 the GfK consumer confidence index is up nearly ten points compared with four weeks prior.*
- *Retail sales volumes rebounded again in June, increasing by 13.9% over May, as sales in household goods and clothing rose by an astonishing 67% and 70%, respectively.*
- *Inflation edged up slightly during June but with a VAT cut in the hospitality industry, and government-backed schemes to get people to eat out in August, the coming months might begin to see deflationary figures.*
- *The government's furlough scheme is heavily influencing both the unemployment rate, and earnings growth. The former is being artificially propped up by those on furlough and not technically unemployed, while the latter shows very low levels, if any, annual growth right now.*
- *Both Nationwide and Halifax indicated monthly house price declines during June of -1.4% and -0.1%, respectively. The government's stamp duty holiday however should heavily pique the interest of both buyers and sellers, adding some upward pressure on prices as a result.*
- *RICS' residential market survey showed some downward pressure on house prices during June, but encouragingly reported that activity rose at its fastest rate in several years, even before the stamp duty holiday was announced.*

UK economic backdrop

- Although **May's GDP figure showed growth of 1.8% during the month, this was a disappointingly slow start to the recovery**, following April's record-breaking contraction of over 20%. May marked the beginning of the end of lockdown for some areas of the economy, with the construction industry, in particular, encouraged to go back to site that month. Nevertheless, that sector grew by 'only' 8.2% and industrial production rose by only 6%. This lacklustre rebound means that the economy was still over 25% smaller in May than in February, before the effects of the pandemic.

- **Retail sales during June rose by a staggering 13.9%** month on month, well above consensus expectations of a 10.0% rise. Following May's 12.3% increase this means that **retail sales volumes are very nearly at pre-pandemic levels**. Consumers were clearly in a mood to spend following weeks of avoiding discretionary spending, with non-food stores seeing their sales volumes rise by 45.5%, with household goods up 66.8% and clothing sales up by a mammoth 70.2%, month on month.

- GfK continued their flash reports every two weeks during June with the result showing a slow but gradual increase in consumer confidence over the weeks. Early June recorded the near-historic low of -36 which gradually moved to -30 and then -27 by late June. **Consumers appear to be gaining slightly more confidence as lockdown loosened across parts of the UK**. The Major Purchase Index gained traction moving from a low of -47 to -25, even before yet more shops and services could reopen in early and mid-July.

- Visa's UK Consumer Spending Index **showed that spending, on a month on month basis, rose by a record 16.6% in June**, following the 11.2% increase seen in May. Of course taken out of context this looks very encouraging however on an annual basis the index shows that spending was down again in June (albeit at a much slower rate than the previous two months), with a year on year decline of -6.5% this month, up from -19.9% in May. **Ecommerce spending in June increased at the quickest rate since the series began 11 years** ago, rising 15% compared with the same time last year, while face to face spending continued to decline (-20.1%) but at a much slower rate than during April (-44.9%) and May (-32.9%).

- **June's Manufacturing Purchasing Managers Index (PMI) rose again to 50.1 in June**, up ten points over May's figure and suggests a stabilisation in conditions following the sharp drop experienced during April and May, due to the coronavirus lockdown. Production rose slightly for the first time in four months and although new orders and employment both fell, the pace of decline is much softer. Encouragingly, business sentiment rose to a 21-month high in June as clients reopened and restrictions eased.

- Robust data from the construction sector as the industry appears to have begun a bounce back following the very low activity seen during April and May. **June's Construction sector PMI rose to 55.3, almost double May's figure of 28.9 and well above market expectations of 47.0. This also marks the sharpest increase in construction output in two years** as supply chains and businesses begin to reopen and construction activity starts up again in earnest. Residential work expanded by the most in almost five years (albeit from a very low base) with both commercial and civil engineering work also returning to growth.

- The IHS Markit / CIPS UK **Services PMI climbed to 47.0 in June, up from 29 in May and well above consensus expectation** of 40. Financial services and the transport services industries performed the best during the month following the gradual restarting of some activities across the economy during June. The sector however was held back due to closures in the hotel and restaurant category while the survey also showed a steep drop in staffing numbers during the month.

- **Inflation rose slightly to +0.6% in June**, up from 0.5% the previous month and ahead of consensus expectations of 0.4%. Inflation from recreation and culture (games, toys and hobbies, of which many will have been turning to during lockdown) contributed the largest overall upward contribution at 0.32 percentage points, while rising prices from clothing and footwear also contributed. On the other hand, prices for food and fuel fell. Looking ahead however and the VAT cut in the hospitality/tourism sector, coupled with the 'Eat Out and Help Out' scheme offering restaurant discounts in August, will put some heavy downward pressure on prices. So **in the short term we are probably headed for a period of deflation**, but it is just these schemes which are aimed at getting people to spend money and increase activity so it is **not something that the Bank of England will be particularly concerned with** if it lasts just a couple of months.

- The government's furlough scheme seems to be minimising any immediate damage to the labour market during the coronavirus crisis, as both the unemployment and employment rates remained unchanged in the three months to May, at 3.9% and 76.4% respectively. However, once again the indications for June payroll data suggest that **the number of employees in the UK on payrolls is down around 650,000 compared with March 2020. The largest falls in payroll data were reported at the start of the pandemic, and they have since slowed significantly.**
- The large number of people on the government's furlough scheme has impacted average pay growth data over the last three months. With many having taken a 20% pay cut on the scheme, this is dragging down pay growth rates, with total pay (including bonuses) falling by 0.3% in the three months to May, while **regular pay (excluding bonuses) slowed to just +0.7%**. The large difference in total versus regular pay will be due to minimal bonuses being paid during the crisis. Looking at wage growth across the different sectors of the economy it is clear that industries with the most furloughed employees (construction sector, hotel, restaurant and retail industries) are directly correlated to those with the lowest or declining pay growth.
- There is no Monetary Policy Committee meeting during July and therefore no change in interest rates and no new release of quantitative easing, although we expect there may be at the next meeting in early August.
- One of the country's biggest mortgage lenders, **Nationwide, pulled all of its 90% and 95% loan-to-value mortgage products from the market in late June.** According to Moneyfacts.com there were just 16 products for people borrowing 95% of their house value, down from 391 at the beginning of March. Lenders were clearly beginning to worry about the long-term impacts of the coronavirus crisis on the economy and employment. BUT, almost immediately **following the stamp duty holiday announcement on 8 July many lenders (including Nationwide) relaunched the 90% mortgages** as they anticipated a housing market boost and a flurry of activity as people look to move before next March.

Click to see the* ***latest market indicators* *at the end of document*

Residential property market

Sales Prices and Rents

- **June house price figures from Nationwide indicate negative growth for the first time since 2012 as prices edged down 0.1%** over the same time last year. On a monthly basis prices also declined, this time by 1.4%, following last month's fall of 1.7%. June's decline in prices will, in large part, reflect sales that were already in-progress before the virus hit and will therefore be pre-virus prices being negotiated down. It is also important to remember that **activity this June is at least less than a fifth of what we would normally see at this time of year (Bank of England data shows mortgage approvals at only 15% of their 'usual' numbers), and therefore pricing data and trajectory of growth must be taken with extreme caution.**
- In contrast, **Halifax's June house price index reported annual price growth of 2.5%** compared with the same month one year ago, although monthly prices are reported to have fallen by 0.1%. This is now the fourth month in a row that Halifax have registered monthly declines. Anecdotally however the Bank reports that new mortgage enquiries during the month of June were up 100% compared with May. **The disparity between the Nationwide figures and Halifax shows just how difficult it is right now to rely on the data during a time of so few transactions.**
- **The ONS took the decision to suspend the UK House Price Index publication from April 2020,** until further notice. The number of transactions has been greatly reduced during the COVID-19 crisis and the ONS felt it too difficult to produce an accurate measure of UK house prices that would be representative of true transaction activity and pricing.
- **House prices showed they were under some downward pressure during June, according to the latest RICS market survey.** A net balance of -15% of respondents saw some degree of decline over the survey period, marking the third consecutive negative monthly reading, but this month is decidedly less downbeat. At a regional level, the report found that London and the South East showed the weakest momentum with readings there of -58% and -33% respectively. In the short term the trajectory for house prices is becoming less negative as the net balance moved from -43% in May to -12% in June.

- More positive news comes out of Rightmove's latest house price index, suggesting that **the housing market was already headed for a 'mini boom' even before the Chancellor announced the stamp duty holiday.** Rightmove's July report finds that average asking prices were 2.4% higher than in March (pre-lockdown) and 3.7% higher than the same month last year, marking the highest increase in over four years.
- HomeLet's June report into the private rented sector found that, on average, **rents across the UK rose by around 1.1% annually, although when London is excluded this rises to 2.0%.** Regional variations are evident again this month as the North West recorded an average increase of 6.6% while the South East and Greater London posted annual rent declines of 1.3% and 1.7%, respectively. Current levels of uncertainty will clearly be affecting different areas of the country differently, particularly as demand levels vary with a high degree of ambiguity surrounding long-term employment levels and changes to living and working patterns going forward.
- Looking at the private rented sector and the RICS survey found that **tenant demand returned to growth in June for the first time in three months,** with a net balance of +24% of contributors seeing an increase. Landlord instructions were broadly steady, while rent expectations also turned positive both in the near term and the longer-term outlooks.

Activity

- Mortgage approvals fell sharply again in May, despite the housing market having reopened halfway through the month, according to **Bank of England data. At 9,273 approvals this is a hefty 41% below the already low volumes seen during April** and reflects an 85% drop compared with the same month one year ago. The **low approvals during the month will reflect the time lag between application to approval,** meaning that those that were approved during May will have submitted their application during the height of lockdown in April. We therefore expect a substantial rise in June as demand surged during the weeks following the reopening of the market.
- **Recorded property transactions edged up again in June, rising by over a third** compared with May's total, as all the UK nations have now reopened their housing markets following many weeks of lockdown. Despite this, on a seasonally adjusted basis transactions reached just 63,250 during the month, about 63% of the average figure for this time of year. Nevertheless, most analysts anticipate latent demand, the stamp duty holiday and a lag in recording to boost figures back to normal levels over the coming months.
- The latest RICS survey points to **activity increasing at its fastest rate for several years in June,** as new buyer enquiries leapt to 60% - only the second time this level has ever been reached. The **newly agreed sales balance also rose to 43%, while new instructions also rose sharply showing a balance of +42%**, up markedly from -22% last month. Looking ahead and a balance of +16% shows cautious optimism that sales will continue to rise in the coming three months. Further ahead though and participants were more pessimistic as the 12-month picture was more slightly negative. It must be remembered however that all these responses and the report itself were collected and drawn up before the Chancellor announced the stamp duty holiday. We therefore expect that next month's readings will again be different, and possibly even more positive.
- Both supply and demand in the sales market are recovering nicely with year-on-year **buyer enquiries up by 75% across the UK** at the start of July, according to Rightmove's latest house price index report. The report goes on to say that available supply continues to 'recover', with total stock now just 13% below where it was at the start of the lockdown in March.
- The RICS Residential Market Survey found that **tenant demand in June returned to growth for the first time in four months** with +24% of contributors witnessing a rise, compared with -12% in May. Meanwhile landlord instructions stayed broadly steady, the first time they have not shown a decline in recent months.

HM Treasury Forecasts for the UK Economy, July 2020

	2020	2021	2022	2023	2024
Official Bank Rate (%)	0.10	0.20	0.99	1.34	1.55
House Price Growth (annual, %)	-3.0	2.7	3.6	3.1	3.2
CPI inflation rate (annual average, %)	0.5	1.7	1.9	2.0	2.0
Unemployment rate (%)	8.0	6.5	4.1	4.1	4.1
GDP (annual, %)	-9.1	6.6	1.7	1.8	1.7
Average earnings growth (annual, %)	-1.1	3.0	3.2	3.2	3.3

Sources: HM Treasury Consensus Forecasts (July 2020)

Select Market Indicators, latest versus previous data

	Current	Previous	Direction of change
GDP monthly (May, month-on-month)	1.8%	-20.4%	↑
Retail sales volumes (monthly % change)	13.9%	12.3%	↑
Visa's UK Consumer Spending Index (expenditure, y-o-y)	-6.5%	-19.9%	↑
GfK Consumer Confidence Index	-27	-36	↑
IHS Markit / CIPS Manufacturing PMI	50.1	40.7	↑
IHS Markit / CIPS Construction PMI	55.3	28.9	↑
IHS Markit / CIPS Services PMI	47.0	29.0	↑
Inflation rate	0.6%	0.5%	↑
Interest rate	0.10%	0.10%	↔
Employment rate (to April 2020)	76.4%	76.4%	↔
Unemployment rate (to April 2020)	3.9%	3.9%	↔
Weekly earnings growth, regular pay (excl bonuses)	0.7%	1.7%	↓
Nationwide annual house price inflation	-0.1%	1.8%	↓
Halifax annual house price inflation	2.5%	2.6%	↓
Official UK House Price inflation (suspended)	n/a	n/a	n/a
Rightmove House Price Index (annual, asking prices)	3.7%	n/a	n/a
HomeLet Rental Index (annual growth, UK)	2.0%	2.7%	↓
£ Sterling: $ USD	$1.26	$1.26	↔
£ Sterling: € Euro	€1.10	€1.12	↓
Brent Crude (USD)	$42.75	$41.38	↑
Gold (USD)	$1,816.99	$1,723.44	↑
FTSE 100	6,260.66	6,306.00	↓
UK 5 Year Gilt Yield	-0.084	0.013	↓

Sources: ONS (unless otherwise indicated) (final six indicators retrieved 20 July)

HomeLet Rental Index, June 2020

Source: HomeLet Rental Index

Region	Average Price	Monthly Change (%)	Annual Change (%)
North West	£758	0.0%	6.6%
Yorkshire & Humberside	£658	0.9%	3.8%
Scotland	£692	1.5%	3.1%
West Midlands	£714	-1.0%	2.7%
East Midlands	£651	-1.2%	2.5%
UK (excluding Greater London)	£797	-0.7%	2.0%
South West	£858	-1.4%	1.9%
Wales	£636	-1.9%	1.8%
UK Average	£951	-0.8%	1.1%
East of England	£917	-0.7%	0.0%
North East	£525	-0.4%	-0.9%
South East	£1,022	-1.4%	-1.3%
Greater London	£1,583	-0.9%	-1.7%
Northern Ireland	£659	1.2%	-1.8%

ABOUT **CARTER JONAS**

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