MIDDLETON®

ADVISORS

TAKING THE LONG VIEW

Why the right property is more important than the right timing.

Market Insights

2023 Vol. II

WELCOME

Our Market Insights reports investigate key trends and structural changes in UK housing markets.

As part of our ongoing collaboration with real estate researcher, Yolande Barnes, this volume considers a dilemma facing some current buyers: Is now a good time to buy? Should I wait for prices to fall more? How much might prices fall? An analysis of the last 70 years of UK housing market behaviour suggests that, for most people, such agony is unnecessary.

The research shows that bear markets can offer a great opportunity. For those looking to hold property over the long term it is more important to buy the right property than to obsess about timing, and – whilst supply remains tight, especially in prime markets – well-advised buyers may find they stand a better chance of acquiring their perfect home in a market where there are fewer home-hunters.

Mark Parkinson
Managing Director

+44 7920 770 747
mparkinson@middletonadvisors.com

EXECUTIVE SUMMARY

- Homeowners occupy their homes for much longer than renters and outright owners for longer than mortgagees. At current rates of sale and current stock levels, private-sector buyers of UK housing will likely hold their asset for longer than 20 years.
- People who buy flats and terraced properties will likely own them for less time than those buying detached and semi-detached houses. This has important implications for those trading ‘up the housing ladder’, usually in younger and more-indebted groups, because the variability of house price growth is much greater when property is held for shorter periods.
- Low average annual returns and higher variance in the range of returns means ‘flipping’ properties in the UK on the basis of market movements only is a bad idea. Gains on 3-month or 12-month holds are unlikely to be sufficient to cover costs and there is more than a 1 in 8 chance of loss on a 1-year hold and 22% chance of loss on a 3-month hold.
- According to the Nationwide building society, owners of ‘the average UK home’ have seen 117% growth in its capital value over the last 20 years, despite recent price falls and a major downturn in 2008 and 2009. This equates to 3.9% per annum compounded (pac).
- Over all the possible 20-year periods in every quarter since 1952, average UK housing has grown in value by between 3.9% and 14.4% per annum compounded (pac) in nominal terms and averages (median) 8.7%.
- This is a higher average rate of growth than the FTSE All-Share Index which averages 6.8% by the same measure and has much more volatile returns, ranging between 0.1% and 17.2% over the same 20-year holding periods.
- The optimum holding period for private housing is 9 years if losses are to be avoided; as there have been no falls recorded in all of the 246 quarters since December 1952 following a 9-year hold.
- Unlike equities and other markets, average annual housing returns increase with the length of holding period, while volatility reduces.
- For those looking to hold property for 9 years or more, it is more important to buy the right property than to obsess about timing. Bear markets can offer better opportunities than bull markets for the brave to get hold of a perfect home.
- Life doesn’t stop for bear markets and there are good reasons for some owners of prime properties to sell now or in the near future as they too will then be able to take advantage of motivated sellers and lower levels of competition for the best properties.

TAKING THE LONG VIEW

"The best time to plant a tree was 20 years ago, the second-best time is now"

This 500-year-old English saying might also be applied to homes. There are no 20-year periods over the last 70 years when average house prices have not grown but prospective home buyers still agonise over the timing of their transactions. Is now a good time to buy? Should I wait for prices to fall more? How much might prices fall? What is the likelihood that I will end up with a mortgage bigger than the value of my home (negative equity)?

Homeowners have a similar dilemma, if prices are falling should they be selling? If not, how long will they have to wait for things to improve? What is the right time to transact?

An analysis of 70 years of UK housing market behaviour suggests that, for most people, such agony is unnecessary. The average homeowner holds their property for over 20 years.

This is significant because an analysis of the Nationwide house price index, going back nearly 70 years to December 1952, shows that there were no 20-year falls in any quarter over that time.

TABLE 1: AVERAGE UK HOLDING PERIOD

Privately-owned dwellings in the UK	24.3m
Average annual home sales 2013-19	1.2m
Average period between sales	20.2 years

Source: ONS

There were no 9-year periods when prices fell in nominal terms over that time either. But the shorter the holding period, the greater the chance of experiencing price falls.

Some homeowners hold property for less than 20 years and some for longer. Older owners of prime, detached, properties are less likely to be sellers than mortgaged owners of apartments and terraced houses nearer the bottom rungs of the housing ladder.

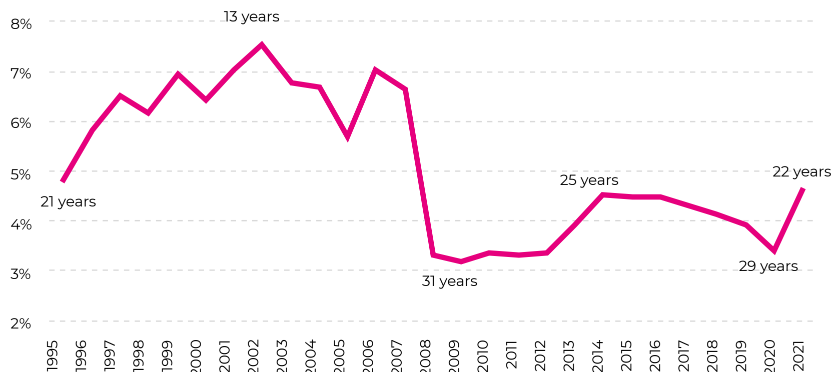
TABLE 2: SHARE BY PROPERTY TYPE YEAR TO SEPTEMBER 2022

	Detached	Semi-detached	Terraced	Flats
Percentage of all transactions	23%	29%	30%	19%
Percentage of all privately owned housing stock in England and Wales	27%	32%	23%	17%
Percentage of all owned outright stock	37%	34%	20%	7%
Percentage of all mortgaged stock	28%	37%	26%	9%

Source: 2021 Census, ONS

The 2020 Survey of English housing showed that the average time that outright owner-occupiers with no mortgage had lived in their homes was 23.8 years. Meanwhile, mortgagors tended to be resident for just 10 years.

GRAPH 1: TRANSACTIONS AS % OF ALL PRIVATE STOCK AND INFERRED HOLDING PERIOD 1995-2021 (ENGLAND ONLY)

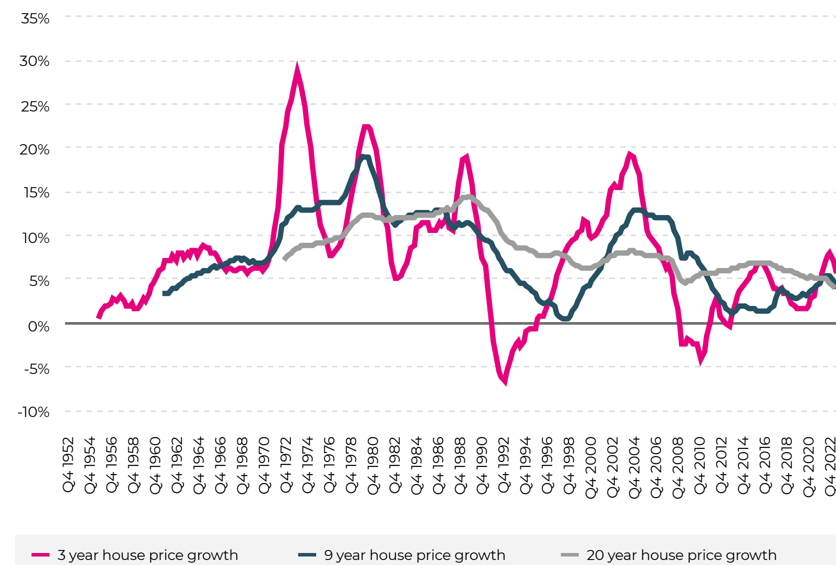


Source: ONS, YBC

This may be seen as something of a problem for younger and more mobile homeowners as there is greater risk associated with shorter holding periods as households work their way up the housing ladder. Not only does the likelihood of price falls increase with shorter ownership periods, but the volatility of those returns also increases.

If you bought one average property every quarter since December 1952 and March 2023 and held them all for 3 years before selling, there would have been 28 times out of 270 when you would have made a loss, ranging between -0.4% and -18.4%. Holding for longer periods would decrease your risk of loss from 10% for three-year holds to 3% for seven-year holds, 2% for eight-year holds and zero for nine-years-or-more holding periods.

GRAPH 2: AVERAGE ANNUAL COMPOUND GROWTH OVER DIFFERENT HOLDING PERIODS 1952 - 2022 (% PAC)



Source: Nationwide Building Society, FT, YBC

Your average return would be 22.3% or the equivalent of 6.9% per annum compounded (pac) but timing is critical to achieving this. The biggest gains would be made by those willing to ignore the fear in the market and buy in the depths of a downturn (just as the biggest losses would be made by those buying at exactly the time people were their most confident and the market has been rising rapidly to a peak). It is even more critical if you are looking for enhanced returns; for only 10% of all the quarterly time periods would you have seen total 3-year growth of between 64% (18% pac) and 113% (or 29% pac). Of course, spotting these opportunities is easier said than done, particularly in markets that are structurally different to those of the last 70 years.

Perhaps surprisingly, given the decreasing variance of returns (volatility), average growth (% pac) also increases with the length of holding period.

It is perhaps worth noting that whilst other markets such as equities provide higher average returns over the short-term (the FTSE All-Share Index median return was 9.1% over all 1-year holding periods in every quarter since 1952), these returns can diminish over longer holding periods while housing growth increases over longer holding periods.

TABLE 3: HOUSING AND EQUITY GROWTH RATES BY HOLDING PERIOD 1952-2022 (% PAC)

Length of holding period since December 1952	Median rate of housing capital growth	Median rate of FTSE All-Share Index growth
3 years	7.7%	7.8%
9 years	8.0%	5.7%
20 years	8.7%	6.8%

Source: Nationwide Building Society, FT, YBC

At the same time, stock-market returns are significantly more volatile than housing markets. Table 4 shows a measure of volatility called standard deviation which shows how much returns in different years vary from the average. The higher the number, the more volatile the market.

TABLE 4: HOUSING AND EQUITY VOLATILITY BY HOLDING PERIOD 1952-2022 (% PAC)

Length of holding period since December 1952	StDev of housing capital growth	StDev of FTSE All-Share Index growth
1 Quarter	9.9%	39.4%
1 Year	8.8%	20%
3 years	6.8%	10%
9 years	4.6%	5.3%
20 years	2.7%	3.8%

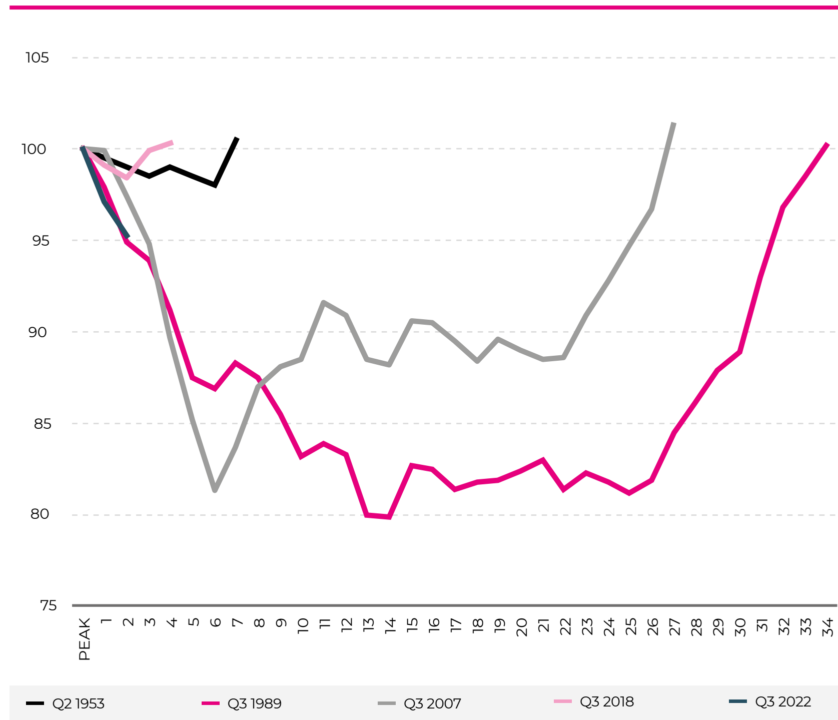
Source: Nationwide Building Society, FT, YBC

It really would appear that a responsible, long-term strategy has paid off in the British housing market over the last 70 years. There appears to have been virtually no advantage in betting on the UK housing market in the very short term as the average UK home price offers little for the pure 'flippers' that is, those buying to sell on within 3 months or a year. Over the last 70 years, the median rate of capital growth over three months has been just 1.6% and over a year, 7%. Neither return would cover the cost of transacting and would only be worthwhile if substantial amounts of value could be added to the property by alternative means than just market movements over such a short period.

Growth seen in holding periods of just 1-year has in exceptional years of high inflation during the 1970s reached an incredible 42% but 70% of the time was less than 10% and 40% of the time, less than 5%. Absolute losses would have been made at a rate of more than one in every eight quarters and range from -0.5% to an uncomfortable -16.5% (seen between the first quarter of 2008 and the 1st quarter of 2009).

The prospect of falling property values has traditionally been of biggest concern to mortgaged owner-occupiers who have not yet paid off a significant proportion of equity on their home. For them, the prospect of negative equity, whereby the value of their asset is lower than the loan secured upon it, has negative consequences affecting their ability to move home or place of work or to be able to secure additional funding, for home-improvements or business ventures for example. Graph 3 shows that the sort of prolonged downturn which would lead to these sorts of problems is relatively rare and has only happened twice in the last 70 years, during the early and mid-1990s when nominal house prices took an extraordinarily long time - 34 quarters (or 8.5 years) - to return to their former peak levels and after the global financial crisis of 2007/8 when recovery to the former price peak took 27 quarters (6.25 years).

GRAPH 3: UK HOUSING MARKET DOWNTURNS: NO. OF QUARTERS AFTER PEAK



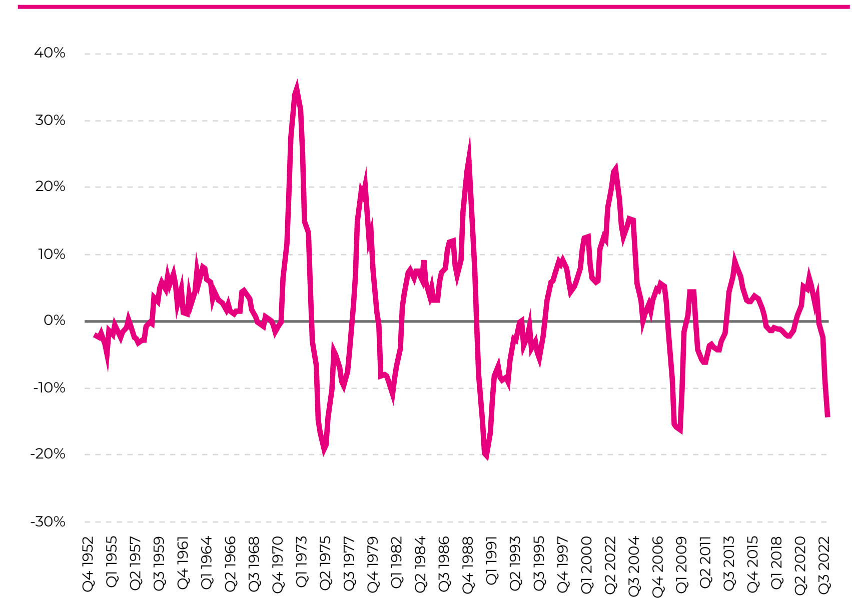
Source: Nationwide Building Society, FT, YBC

It can't be ignored and is perhaps sobering that current price falls are on a similar trajectory to those of late 1989. But there are reasons to believe that any housing market downturn now is likely to be dissimilar to the early 1990s. This is because levels of mortgage borrowing should be more sustainable than they were in 1989; loan-to-value ratios and income multiples are lower so there is more slack in the system before households get into either negative equity or payment difficulties. Although mortgage rates have risen substantially, they are not as high as in the early 1990s. A combination of lender forbearance and more equity-rich homeowners means repossessed stock and distressed sales are less likely to be a feature of the market, driving prices down over a long period, as they did in the 1990s.

The question then again arises as to how relevant these findings are for the future of the housing market in an age where even the cost of living crisis and rising interest rates do not begin to emulate the extremes of the 1970s.

Graph 4 shows inflation-adjusted house price growth and how the very high nominal house price rises of the 1970s were dramatically tempered by general price inflation (as measured by the retail price index). It means that, in real, inflation-adjusted terms, the housing market downturns of the mid-1970s and early 1980s were just as big as those that came later when inflation was lower – but were felt differently in the marketplace thanks to money illusion and continuing nominal rises. It also means that because currently inflation is high, we are seeing

GRAPH 4: REAL ANNUAL HOUSE PRICE GROWTH 1952-2022



Source: YBC

UK price falls on the same scale as 2008, 1990, 1980 and 1974.

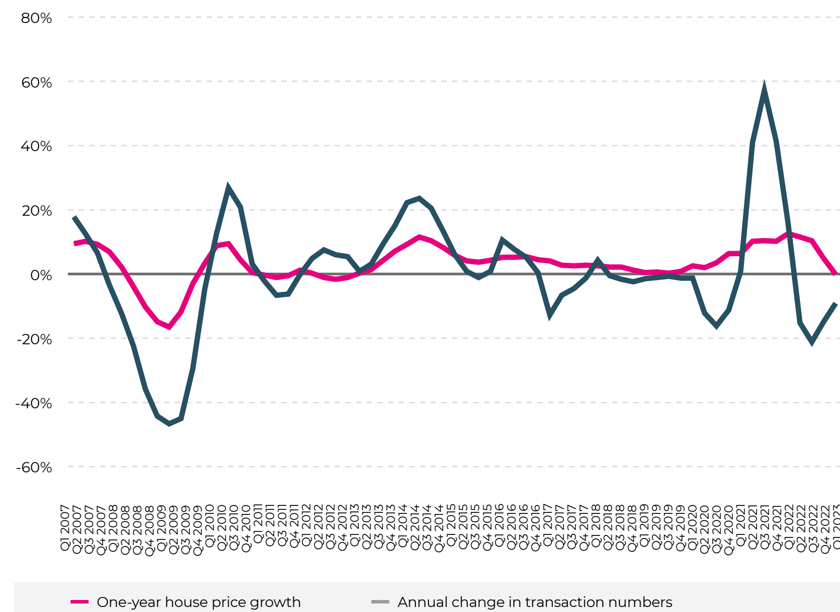
It may be possible that, even as inflation (hopefully) begins to abate, it has the potential to both drive nominal house prices upward, along with the price of other goods and services, and, at the same time, to devalue the debt secured on it in real (inflation adjusted) terms. Good news, in the longer term, for mortgaged owner-occupiers (provided household incomes keep pace), less auspicious for renters though.

Having said this, it does seem likely that transaction levels will be a major casualty of this downturn as buyers are discouraged from entering the market and available stock is limited by equally reluctant vendors exercising their discretion for a few years or until the market looks more buoyant. It is the resulting lack of quality stock which sows the seeds of the recovery, particularly in prime markets which tend to be the first to recover as soon as any interest resumes, driven by demand imbalance in a supply-starved marketplace.

Graph 5 shows how house price downturns often coincide with bigger downturns in the number of market transactions taking place. Although recent fluctuations were abnormal due to Covid-19 lockdowns, it seems likely that the downward trend in prices will be matched by much lower transaction levels.

This has important implications for both buyers and sellers in this bear market. Purchasers who are able to keep their nerve while fear stalks the market may find that they stand a far better chance of acquiring their dream home when they are not in competition with hoards of other home-hunters after the same opportunity. Properties may need to be searched out and motivated sellers found (death, divorce and debt are all motivators unimpeded by recession) but now really could be the best time for buyers to find the right property - rather than just any property.

GRAPH 5: HOUSE PRICE GROWTH AND TRANSACTION GROWTH COMPARED 2007 - 2023



Source: YBC

What about sellers? Why move now? Well, life doesn't stop for a downturn. You may want to change location, change lifestyle, release equity, trade up, have a family or downsize. The likelihood is that you are a buyer too and the choice of the best homes for your next move may be better now than in future. Despite the latest falls, if you've owned an average UK property for the last 20 years, it is still worth 117% more than when you bought it. Discretionary sellers have a lot of power in a bear market if they have a high-quality property which they don't have to sell but which will sell well to the right buyer. They are then a cash-rich purchaser in their next move and very attractive to a motivated seller.

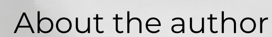
So while low levels of turnover will likely be a characteristic of the market for some time to come and inflation is the likely culprit devaluing our housing assets for a while, we gain value from our homes in other ways. It may be that most UK housing, and indeed other forms of real estate, have reached a 'high plateau' price-wise for the foreseeable future and may face further real falls. A fundamental shortage (which will probably always be with us) of the best properties in the best places will likely draw a threshold under the price of prime properties, even as some types of residential real estate, perhaps like recently built flats on the fringe of cities, for example, see a drop in demand and faster falling prices.

For most people, happy and content in their current home, able to afford its upkeep, there is nothing to be done except enjoy it. For these people, rises and falls are irrelevant, gains and losses are on paper only and far more important is living in a home you love.

NOTES:

About the author

YOLANDE BARNES



Yolande Barnes has been examining and analysing real estate markets for over 35 years. As Director of World Research at Savills, she provided evidence-based advice to clients and thought-leadership in real estate. She set up and ran their UK residential research department, pioneering and developing new techniques for measuring place potential, land values and sustainable urbanism.

DISCLAIMER

The views expressed in this article are those of the author. Every care has been taken to ensure that the information contained in this article is correct, the author does not assume responsibility for effects arising from its publication. No material may be used in whole or in part without the permission of the author. All rights reserved.

YOLANDE BARNES CONSULTING APRIL 2023

@**middleton**advisors #**middleton**advisors

middletonadvisors.com