

London's bubbly housing market goes flat

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SINCE 1990 the price of the average house in London has tripled in real terms, easily outstripping the rest of the country. Millennials, many of whom have lost all hope of buying a home, have a morbid fascination with stories about

the capital's outrageous prices, including a recent one about a shabby, narrowboat-sized house in west London which went on sale for £600,000 (\$790,000). Yet the market may be turning. Lately the rate of house-price growth across Britain has slowed. But in London it has nosedived (see chart). Why has the capital lost its fizz?

One pocket of weakness is London's "prime" market, often defined as the priciest 5-10% of homes. According to a recent report by Savills, a property firm, prime prices in central London are 15% below their peak of three years ago. Back then estate agents in Mayfair and St James's would often sell homes for more than £50m. Data about such mansions are murky, yet they suggest that the maximum price in the area so far this year has been around £30m. In Kensington and Chelsea, the poshest borough, house prices have tumbled by 15% since January.

The travails of the prime market are partly due to worries about London's status after Brexit. Some plutocrats have already left; others want to rent, not buy. Yet other factors have played a bigger role. In 2014 the government made changes to stamp duty, a tax on homebuyers, which reduced it for most but raised it for those buying houses worth more than about £1m. Recently stamp duty became heavier still for those purchasing second homes. London is stuffed with luxury pads—it accounts for over half the houses sold in Britain for over £1m—so it is feeling these measures most keenly.

It is not just London's luxury market, however, that has cooled down. Figures from Hometrack, a consultancy, suggest that in all price brackets, prices are less bubbly than they were a few years ago.

One possible explanation is increased supply. Surprisingly enough for a city that feels so squashed, lately London's rate of house building has risen. Last year the stock of housing in the capital grew faster than it did elsewhere in England. Savills expects total net completions to peak at 46,500 this year, which is ahead of the target of at least 42,000 in the "London Plan", a blueprint from the mayor's office. Extra supply has added to downward pressure on prices.

However, changes to financial regulations may have had the biggest effect on the London market, by curbing demand. In recent years, many people have stepped onto the capital's housing ladder only with the help of a huge mortgage. In 2014 over 20% of buyers in the capital took out loans worth at least 4.5 times their income, up from around 5% a decade before and double the rate for Britain as a whole.

New rules to bolster Britain's financial stability, which were introduced in 2014, have dissuaded banks from doing too much lending at big multiples of income. Since then, the number of mortgages granted to first-time buyers has slumped by over a tenth in the capital, while rising elsewhere. With many potential buyers in effect forced out of the mortgage market altogether, demand has been dampened.

London's housing market may remain weak for a while yet. JLL, another property firm, expects annual house-price growth in the capital of around 2% over the next five years. Good news for the millennials, perhaps. Yet a period of softer prices will not make it much easier to get a foot on London's property ladder, especially since mortgage regulation will remain strict. If current trends persist, the ratio of London's house prices to household income will fall back to its long-run average only in 2040.