Intelligent Investment

Q2 2024

Residential Forecasts

REPORT — UK RESIDENTIAL

CBRE RESEARCH

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01

Economic Outlook

Economic Outlook

CBRE's UK Economic Outlook was last updated in May 2024.

CPI inflation fell to 3.2% in March 2024, the lowest rate since September 2021 and down from the peak of 11.1% in October 2022. We expect CPI to continue its downward trajectory towards the BoE target of 2% and stabilising in early 2025.

Given the continued fall in inflation, we anticipate rate cutting will begin in the summer. We expect 50bps of cuts by the end of 2024.

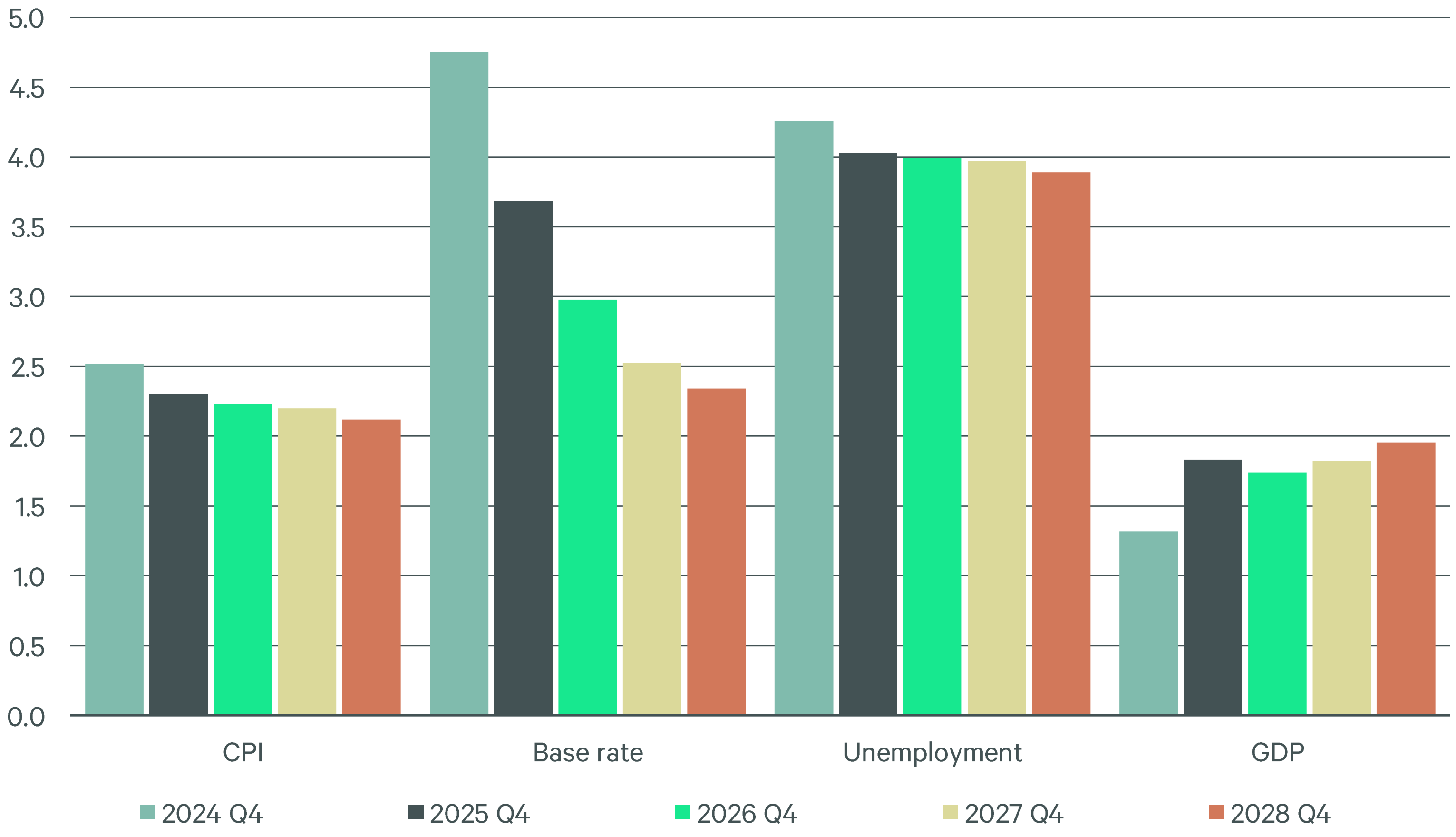
In light of falling inflation and the base rate being held for the last nine months, we expect the BoE to start reducing the rate in the second half of 2024.

One contributor to the stubbornness of inflation is that labour markets have remained tight, despite the weaker economic backdrop, and more recently due to increasing flows into inactivity. We expect the unemployment rate to decrease steadily given several labour supply constraints.

Despite recent weakness in the economy, falling inflation and tight labour markets should mean real incomes will continue to grow. This will act as a catalyst for consumption increasing in the second half of 2024, contributing to economic growth.

The outlook remains conditional mainly on the trajectory of inflation. Any destabilising factors domestically like stubborn wage growth, or globally such as the escalation of the Middle East conflict, could slow the return to target delaying rate cutting and dampening the recovery.

Figure 2: CBRE Economic House View, April 2024



Source: CBRE Research

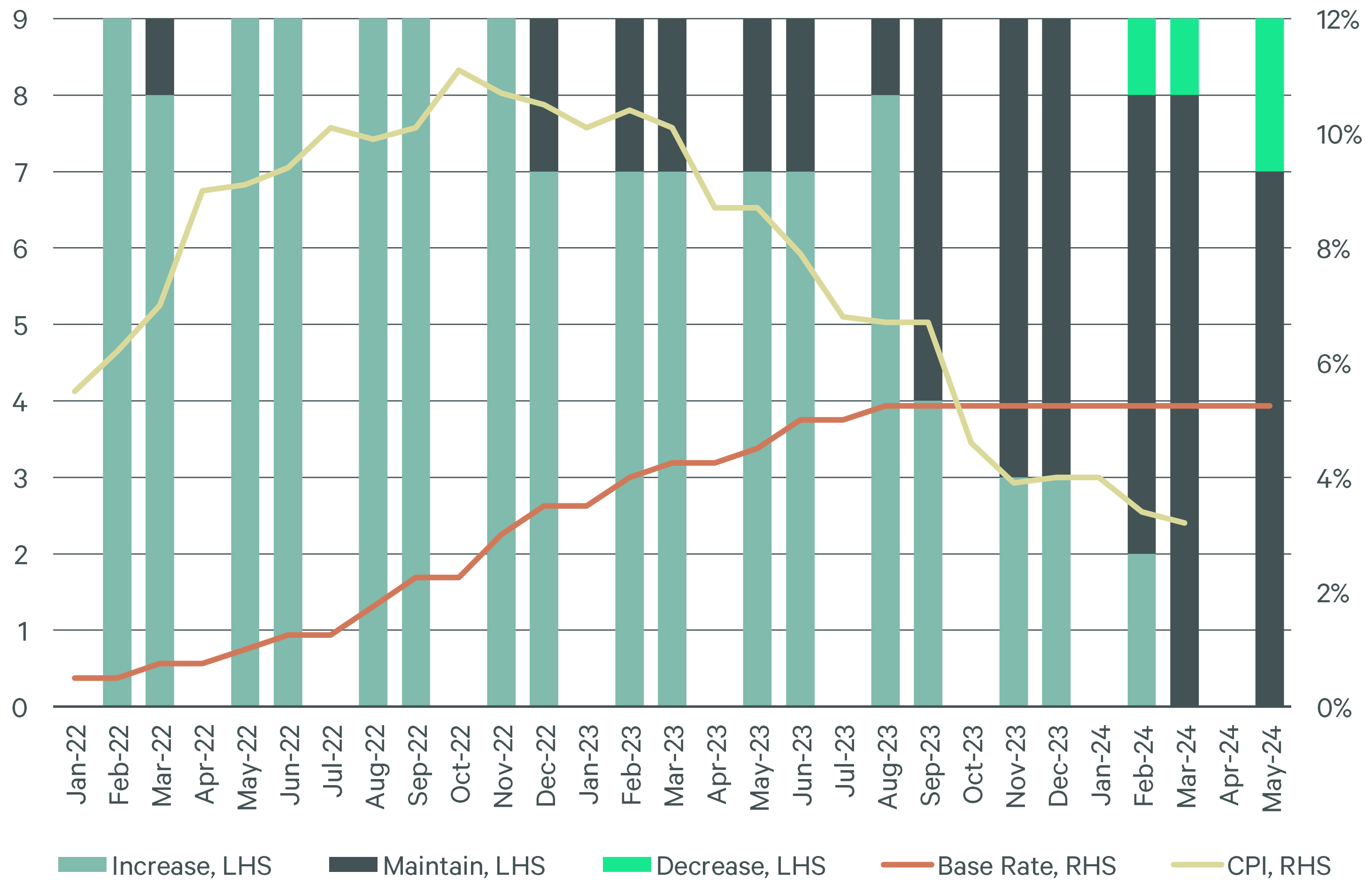
Monetary Policy

The Bank of England (BoE) reached the end of its interest rate tightening cycle in the second half of 2023, with the base rate now having peaked at 5.25%. This has put inflation firmly on a downwards trajectory. Headline inflation was 3.2% in March 2024, continuing its fall since its peak of 11.1% in October 2022.

As a result, the first three Monetary Policy Committee (MPC) meetings of 2024 have shown some appetite to begin cutting the base rate. There have been votes to decrease the base rate in each of the first three MPC meetings in 2024. This is the first time this has happened since the COVID-19 pandemic. March's meeting was also the first with no votes to increase the base rate since September 2021. This indicates that an initial base rate cut is imminent.

As inflation continues to move towards its 2% target, there will be greater ability for the BoE to begin loosening monetary policy. This will provide a boost to consumer spending power and could also be a significant turning point for demand in the housing market.

Figure 1: MPC Committee voting history, base rate, and CPI



Source: CBRE Research

02

House Prices

House Price Overview 2023

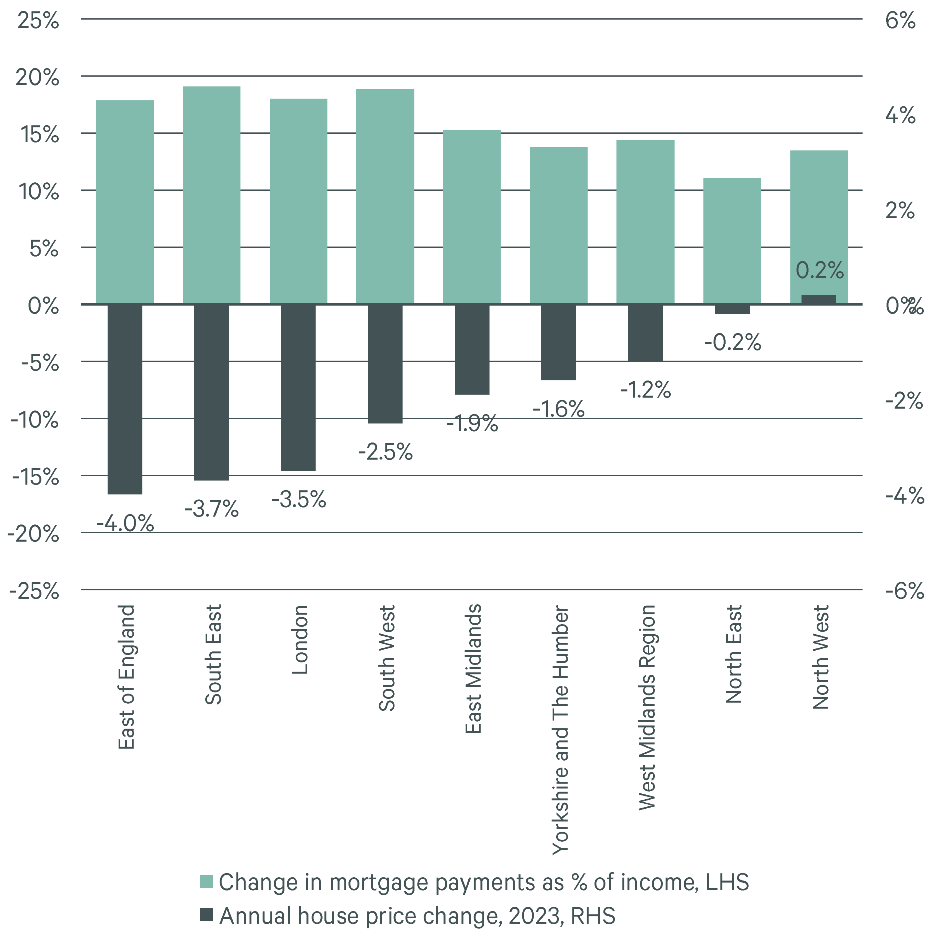
Mortgage affordability dictated house price movement

Across the UK, house prices fell by 1.6% in 2023, according to the ONS. The largest falls were recorded in the East of England and London, whereas prices remained broadly static in the North. Similarly, the Nationwide House Price Index recorded prices falling by 1.8% across the UK in 2023, with the same regions registering the greatest drops.

This reflected surveyor sentiment as recorded by the RICS, with buyer enquiries and sales instructions firmly negative for most of 2023. This resulted in a subdued sales market throughout last year, with mortgage approvals 20% below the long-term average.

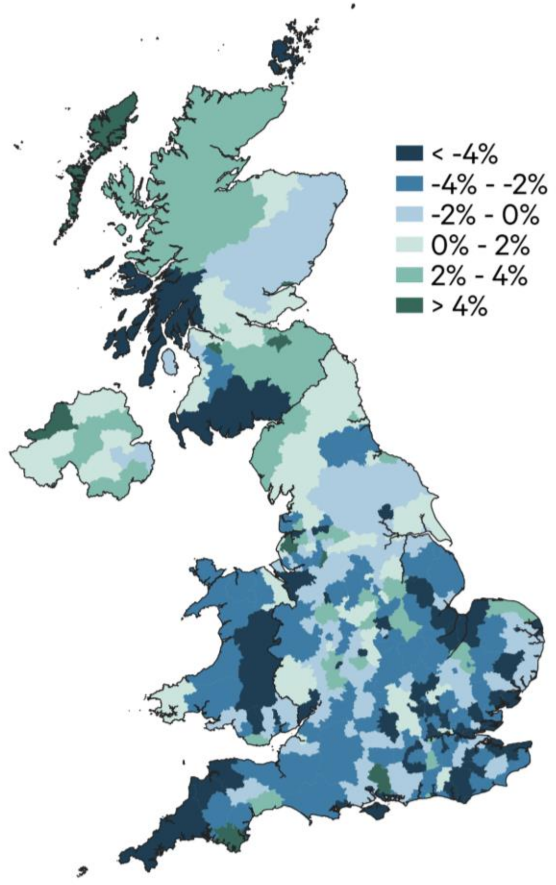
This trend was largely dictated by mortgage affordability. The sharp increase in mortgage rates throughout 2023 meant housing affordability came under increasing pressure. As a result, the steepest price falls were in regions where affordability became most stretched. For example, in London, the increase in monthly mortgage payments on the average property equated to 18% of the average income, compared with only 14% in the North West.

Figure 3: Annual change in house prices, mortgage affordability (%)



Source: ONS, Bank of England. CBRE Research

Figure 4: Annual house price change, 2023



Source: ONS

House Price Overview 2024

Falling mortgage rates boost sentiment

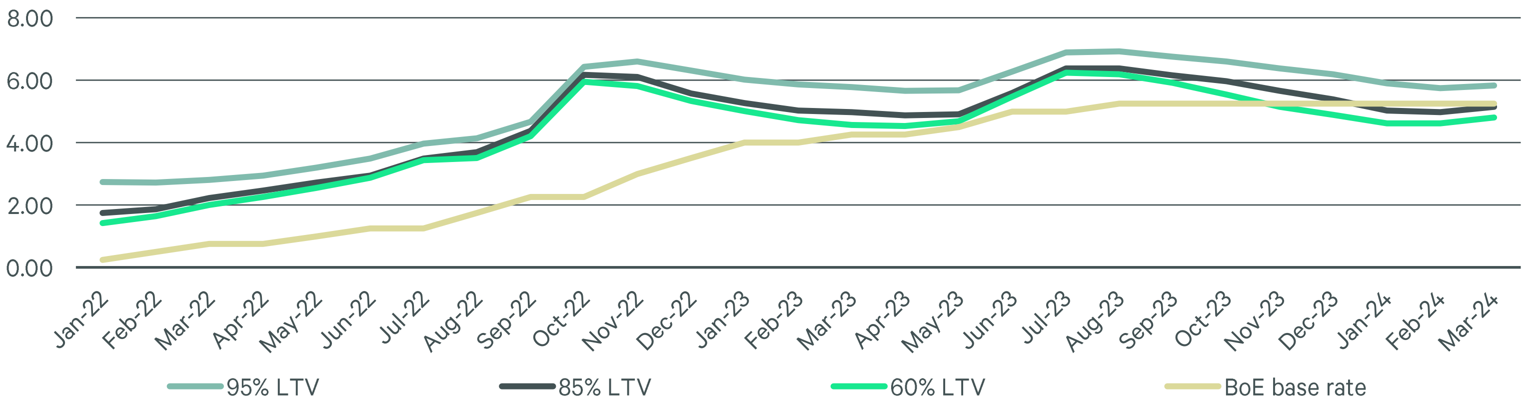
Mortgage rates have now gradually fallen since peaking in August 2023. Average mortgage rates increased slightly in March but are still lower than at the end of last year. As a result, the mortgage payment on the average UK home (on a 75% LTV product) has dropped by £240 per month since August.

This improvement in affordability has boosted sentiment at the start of 2024. The RICS monthly survey reported a positive balance of buyer enquiries in the first three months of the year for the first time since April 2022. Similarly, new sales instructions were positive over the last four months to March 2024. Prior to this, it had been negative in all but one of the preceding 20 months.

The return of buyers and sellers to the market has resulted in positive sales expectations for five consecutive months. This has underpinned a recovery in mortgage approvals and sales volumes. There were 60,383 mortgage approvals in February 2024, marking the fifth consecutive monthly rise and the highest level since September 2022.

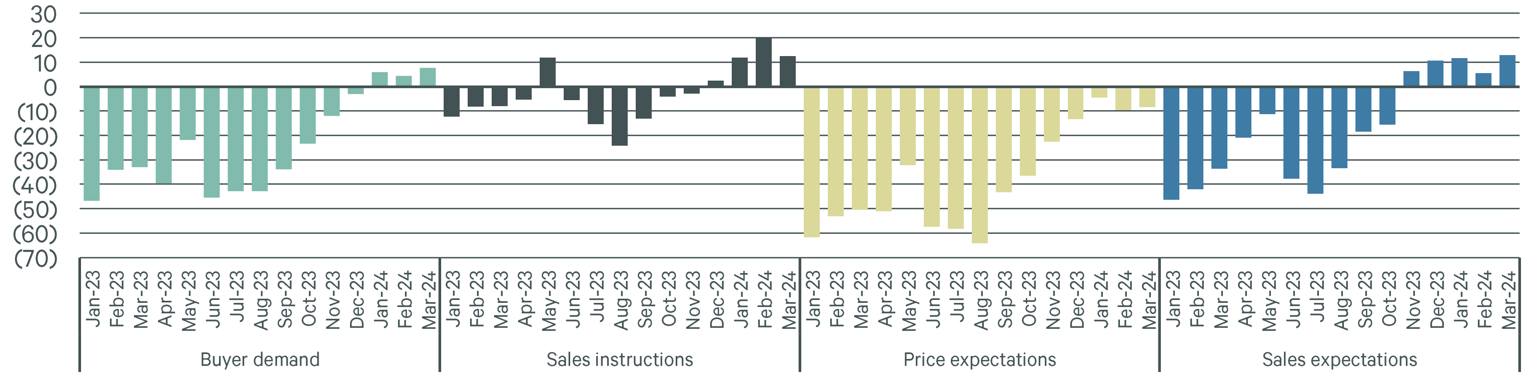
As a result, there have been tentative signs of house prices returning to growth. Nationwide and Halifax reported that the average UK house price has increased by 1.4% and 0.4%, respectively, in the first three months of 2024.

Figure 5: Average two-year fixed mortgage rate and BoE base rate



Source: Bank of England

Figure 6: RICS Residential Market Survey, net balance of respondents (%)



Source: RICS

House Price Forecasts

Our headline house price forecasts are based on Oxford Economics house price forecasts and adjusted to incorporate CBRE's macroeconomic house view.

The regional forecasts are calculated from the performance of each region relative to the UK, based on the **ONS House Price Index**. For 2024, this is overlaid with relative mortgage affordability across the regions.

Outlook

We forecast UK house prices will increase by 1.0% in 2024. This is an upgrade from the 0.9% fall we had previously forecast. Continued price falls are expected in the first half of the year but cancelled out by a recovery in the second half. We forecast five-year compound growth of 15.0% between 2024 and 2028.

At a regional level, mortgage affordability will remain the key driver of house price movement in 2024. Regions with higher house prices, like London and the South East, are expected to underperform the rest of the UK this year. London typically recovers faster after a downturn and the same is expected this time. Therefore, despite expected to see the lowest house price growth in 2024, it is still forecast to be the best performing region over the five-year period with growth of 18.6%.

Our forecasts for new build homes are the same as those for the broader market. Although new build homes will attract an initial premium, the ONS Index records that the performance is broadly in-line with the wider market.

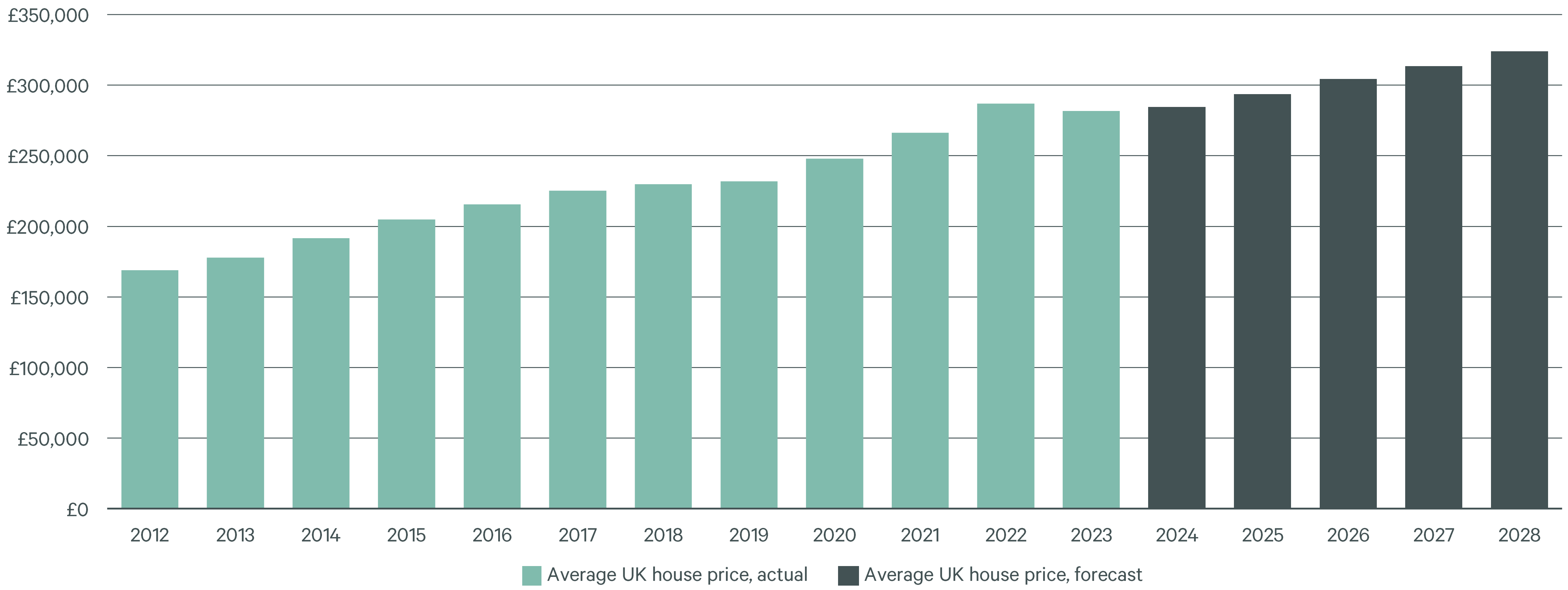
Figure 7: CBRE house price forecasts, annual % change

Region	2023 (actual)	2024	2025	2026	2027	2028	2024-28 average annual change	2024-28 compound total
South East	-3.7	0.8	3.5	4.0	3.3	3.7	3.1	16.2
London	-3.5	0.6	4.0	4.7	3.8	4.3	3.5	18.6
Inner London	-3.6	0.5	4.3	4.9	4.0	4.5	3.7	19.6
Outer London	-3.7	0.5	3.9	4.5	3.7	4.1	3.4	17.9
Eastern	-4.0	0.8	3.8	4.4	3.6	4.1	3.4	17.9
South West	-2.5	1.0	3.6	4.1	3.4	3.8	3.2	16.8
West Midlands	-1.2	1.1	3.5	4.1	3.3	3.7	3.1	16.6
East Midlands	-1.9	1.1	3.7	4.3	3.5	4.0	3.3	17.8
Yorkshire and Humber	-1.6	1.1	3.7	4.3	3.5	3.9	3.3	17.7
North West	0.2	1.2	3.6	4.2	3.4	3.8	3.2	17.3
North East	-0.2	1.2	3.1	3.6	3.0	3.3	2.8	15.0
Wales	-2.5	1.3	3.7	4.2	3.4	3.9	3.3	17.6
Scotland	2.3	1.2	3.3	3.8	3.1	3.5	3.0	15.8
Northern Ireland	1.4	1.2	2.6	3.0	2.4	2.7	2.4	12.4
UK	**-1.6**	**1.0**	**3.2**	**3.7**	**3.0**	**3.4**	**2.8**	**15.0**

Source: CBRE Research

House Price Forecasts

Figure 8: Average UK house price, end of year



Source: ONS, CBRE Research

03

Sales Volumes

Sales Volumes Forecast

Transaction values fell to a 12-year low in 2023. The one million transactions in 2023 were 19% lower than 2022 and 15% below the 10-year average.

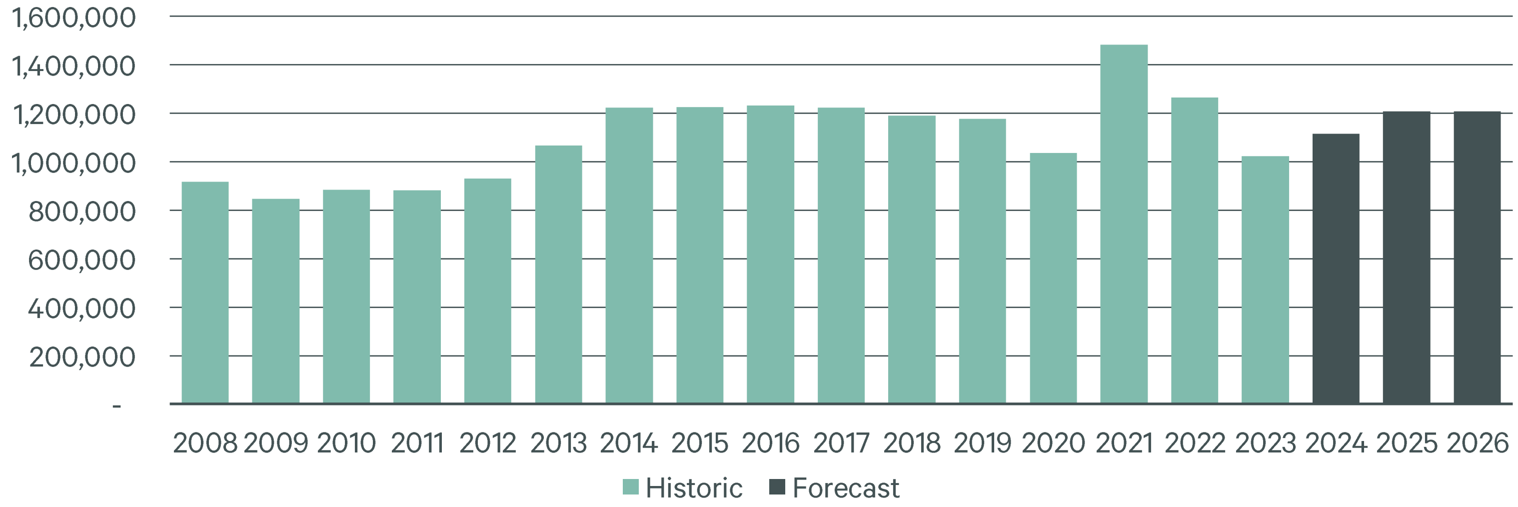
Increasing mortgage rates meant mortgaged sales fell the most. The number of first time buyers and home movers buying with a mortgage fell by 22% and 26%, respectively, in 2023. Buy-to-Let mortgaged sales recorded an even greater fall of 51%.

Cash buyers have been insulated from the increase in mortgage rates. Consequently, the volume of cash buyers in the market in 2023 has seen a much smaller decline, of just 4%. This partly offset falls from the other buyer segments in 2023.

However, mortgage approvals have now been continually rising since September 2023, although are still below the long-term average. The 60,400 mortgages approved in February 2024 were the highest since September 2022. As a result, 'sales expectations' from the RICS monthly survey have been positive in each of the last four months.

These positive forward-looking indicators point to a gradual recovery in sales volumes in 2024, which will be weighted towards the second half of the year. Overall, we are forecasting c.1.1 million transactions in 2024, an increase of 9% from 2023. This will be supported by an improving economic backdrop and lower mortgage rates. We then expect that transaction volumes will return to their long-term average of 1.2 million by 2025.

Figure 9: Total annual residential transactions



Source: HMRC, CBRE Research

Figure 10: Sales volumes by buyer type

Buyer type	2022	2023	% change
FTB mortgaged buyer	369,900	287,000	-22%
Home mover mortgaged buyer	338,800	250,900	-26%
BTL mortgaged buyer	106,800	52,500	-51%
Cash buyer	449,800	432,000	-4%

Sources: Bank of England, HMRC, UK Finance

Sales Volumes Forecast

Our London new build sales forecasts are based on Molior's new home statistics. Molior tracks development activity on all schemes with more than 20 private homes in London, which has accounted for around 60% of total development activity since 2020.

New home sales have historically moved in line with new construction starts, as developers match construction volume to their sales rates. We have analysed trends in new planning applications and permissions to forecast construction starts and subsequent sales volumes.

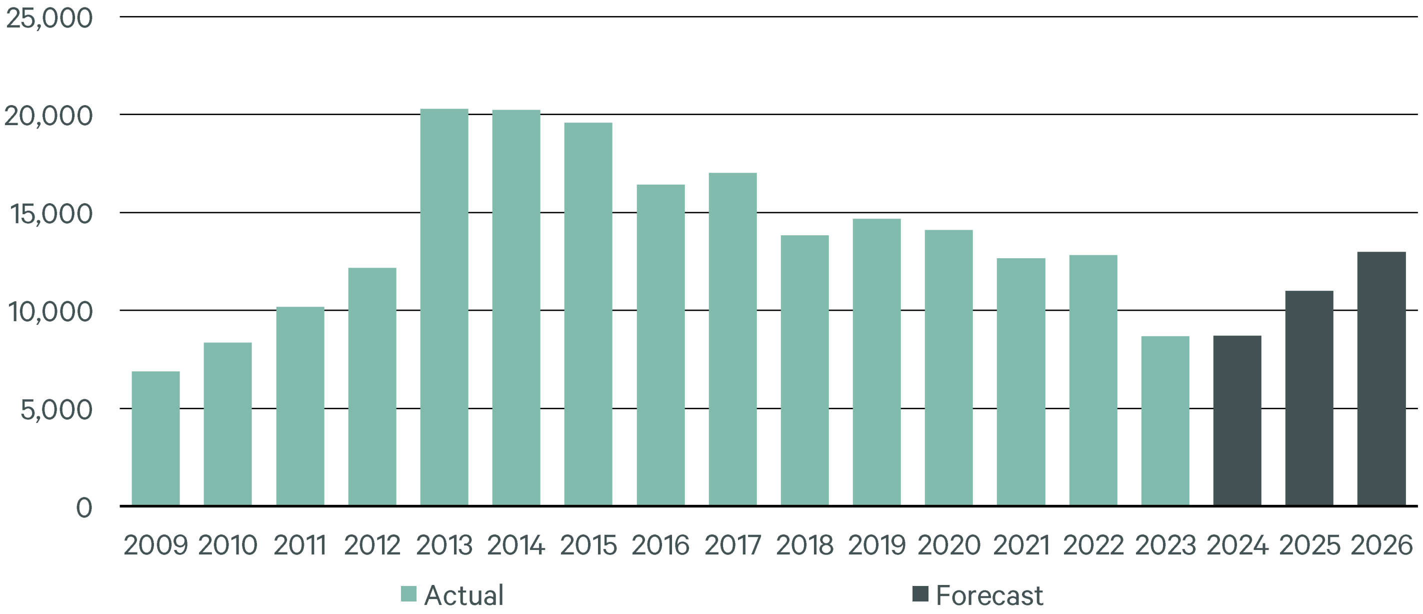
Outlook

London's residential development market slowed drastically last year. Applications submitted, permissions granted, and construction starts all fell by approximately 20 – 30% in 2023. This was driven by the loss of Help to Buy, higher interest rates, new planning regulations, and persistent planning delays. As a result, there were only around 8,800 new build sales in London in 2023. This was the lowest annual total since 2010 and a 32% fall from 2022.

Developers are unsure of future sales rates and viability of schemes, which has translated into a shrinking development pipeline. This muted development activity therefore continues to point to relatively low new build sales volumes in London.

A lot of the challenges from 2023 will continue into 2024, and we forecast new build sales to total 8,700 in 2024, broadly level to 2023. Thereafter, we expect a gradual recovery driven by a combination of a pricing correction and lower interest rates. This recovery broadly mirrors that following the previous downturn. However, much of the completed stock may have been absorbed by this time, so this recovery will be partly dependent on developers' ability to attract buyers to commit to off-plan sales.

Figure 11: Historic London new build sales volumes and forecasts



Source: Molior, CBRE Research

Figure 12: CBRE London new build sales forecasts

Region	2023 (actual)	2024	2025	2026
Sales volumes	8,673	8,700	11,000	13,000
Year-on-year change	-32%	0%	+26%	+18%

Source: Molior, CBRE Research

04

Rents

Rental Market Overview 2023

Record rental growth impacted affordability

Rental values increased by 8.3% across the UK in 2023, according to the ONS. London recorded the highest growth rate of all English regions, of 9.6%. These are the strongest growth rates ever recorded by the index. Rents on new lets increased by 8.0% across the UK, according to HomeLets.

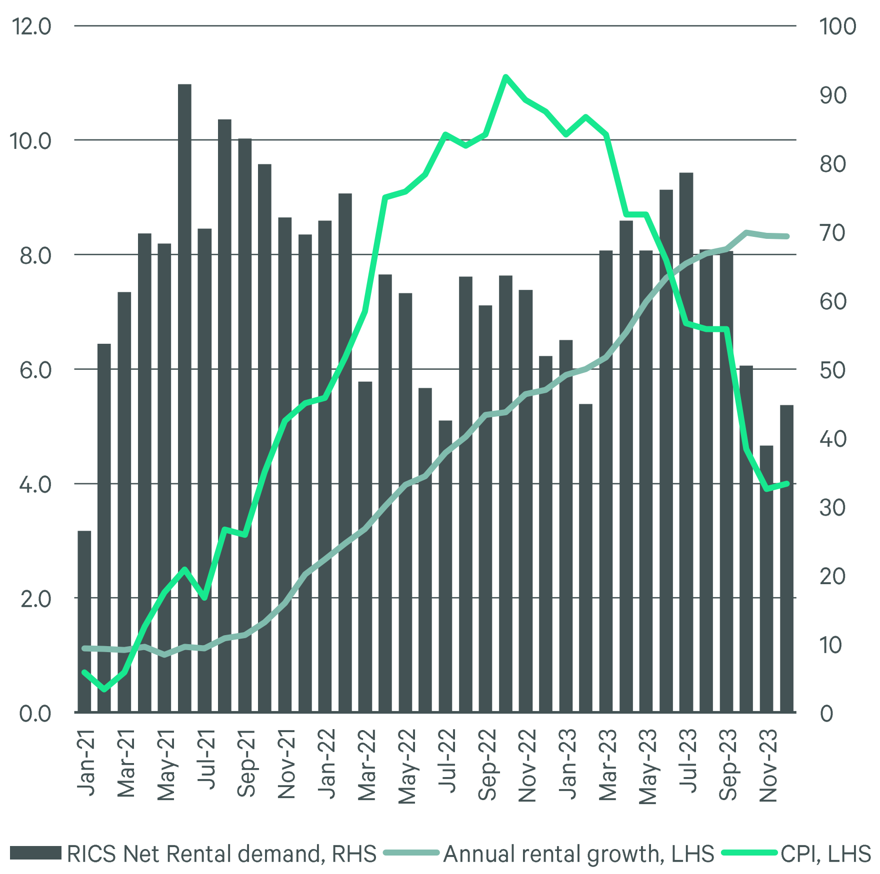
These high levels of growth were driven by an acute supply and demand imbalance, and the high inflation rate being passed through to tenants last year. The RICS monthly survey reported a negative balance of new landlord instructions in the last 19 months, while tenant demand has been consistently positive month-on-month.

As a result of very strong rental growth, affordability within the sector has become more stretched than ever. At the end of 2023 tenants were spending a third of their income on rent, compared with a long-term average of 30%. This was more acute in London, with tenants having to spend almost 40% of their income on rent. This compares with the long-term average of 34%.

In addition, an estimated 120,000 Buy-to-Let homes were sold in 2023, bringing the total sold since 2016 to 483,000. This is exacerbating the supply shortage in the rental market and exerting upward pressure on rents.

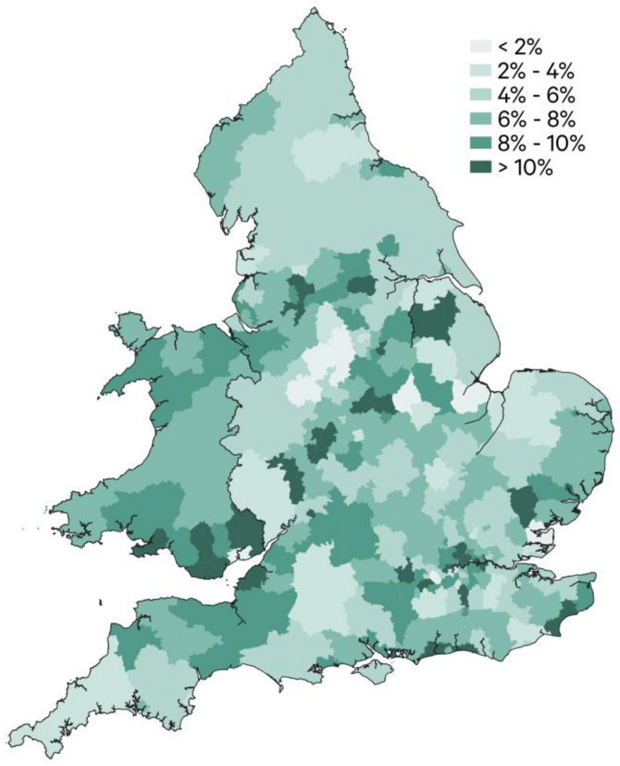
The Build-to-Rent sector has generally outperformed the wider market. Our Multifamily Index recorded that rents across the sector increased by 9.5% year-on-year to September 2023. This compares with 8.1% across the wider market over the same period.

Figure 13: Annual change in rents, net demand and inflation



Source: ONS, RICS

Figure 14: Annual rental change, 2023



Source: ONS

Rental Market Overview 2024

Lower inflation and stretched affordability dampening growth

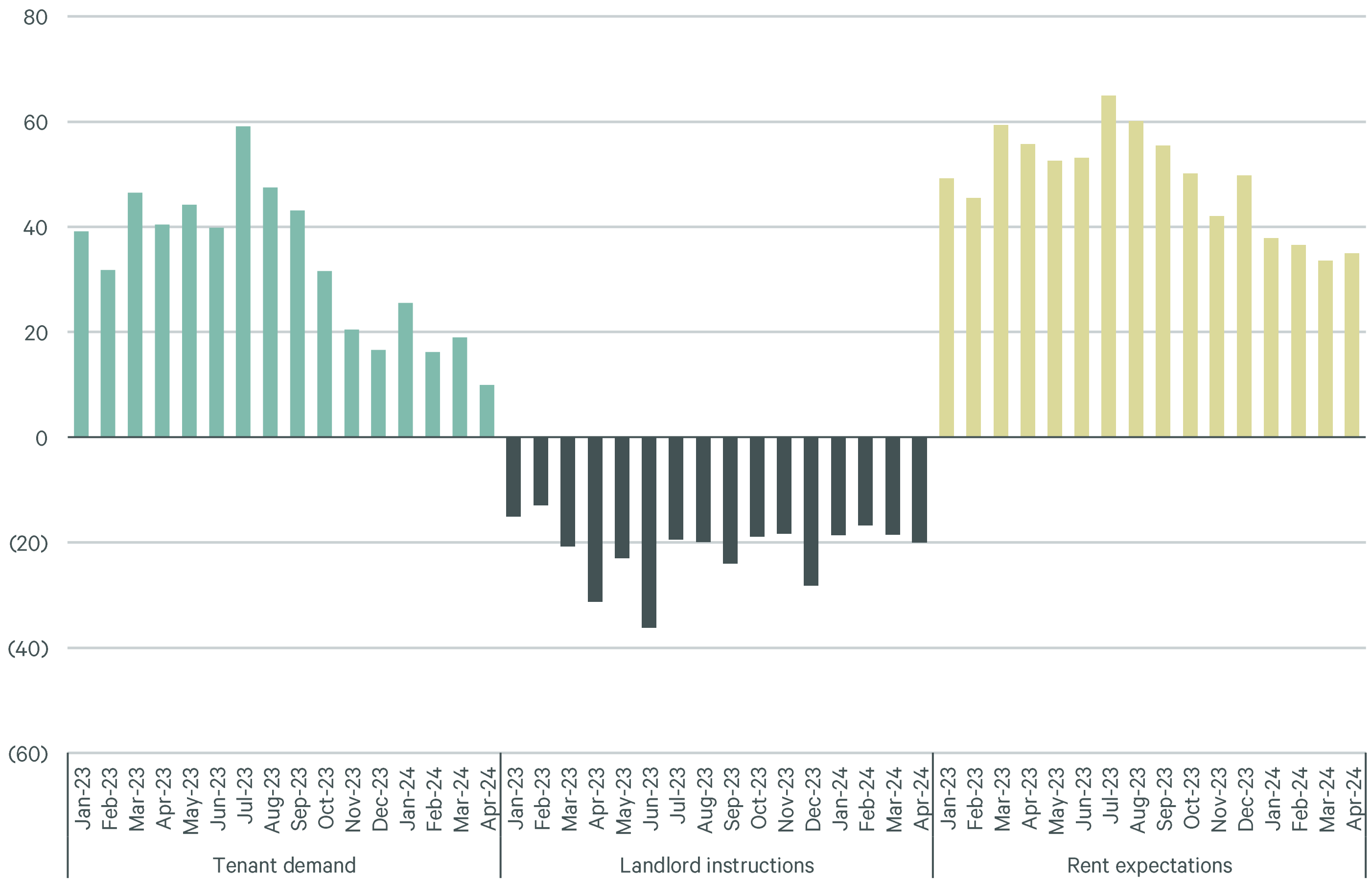
The net balance of tenant demand from the RICS remain positive but fell to the lowest level in over three years in April 2024. Sales expectations have also decreased at the start of the year. This indicates continuing, but lower, rental growth in 2024.

This will be underpinned by the continued supply and demand imbalance but constrained by lower inflation and tenant affordability.

This trend is starting to be reflected in HomeLet's index, which has shown annual growth slowing to 7.9% in April 2024, down from the 2023 peak of 10.4% recorded in June.

Conversely, the ONS index shows an increase of 2.5% in rental values in the first three months of 2024. However, this index includes all tenancies and is more lagged than HomeLet, so it will take longer to reflect current market conditions.

Figure 15: RICS Residential Market Survey, net balance of respondents (%)



Source: RICS

Rental Market Forecasts

Our rent forecasts are based on the Price Index of Private Rents produced by the ONS. These are forecasts for the whole of the private rented sector, including renewals. We use the historical data and incorporate our macroeconomic house view to forecast UK and London rents. We then calculate the performance of each UK region relative to the headline level to produce our regional level forecasts. These are the numbers in **bold** in figure 16.

We also include specific forecasts for new lets (in figure 16 in standard text). These are calculated based on the relative performance between the HomeLet and ONS indices.

Outlook

The latest indicators from the RICS survey continue to point to an acute supply and demand imbalance in the rental market, which will sustain rental growth in 2024. However, affordability constraints will mean growth will slow.

London is forecast to marginally outperform the UK this year. However, greater affordability constraints will lead to a larger slowdown in rental growth in London in comparison with 2023 growth.

From 2024 onwards, we expect growth to decelerate because of falling inflation and stretched affordability. Across the five-year period, we forecast a compound rental growth of 15.7% across the UK and 14.0% across London.

Our Scotland forecast does not currently account for the new proposals on rent control which will be confirmed later in the year.

Rental values on new tenancies are forecast to grow by 23.7% across the five-year period, at a faster pace than our whole-market forecast.

Figure 16: CBRE Private Residential Rent Forecasts, annual % change

Region	2023 (actual)	2024	2025	2026	2027	2028	2024-28 average annual change	2024-28 compound total
South East	**7.7** | 10.1	**5.8** | 7.7	**2.8** | 3.4	**1.6** | 2.2	**1.6** | 2.2	**2.0** | 2.6	**2.8** | 3.6	**14.6** | 19.3
London	**9.6** | 8.1	**6.6** | 3.0	**2.7** | 5.9	**1.3** | 4.5	**1.1** | 4.3	**1.7** | 4.8	**2.7** | 4.5	**14.0** | 24.5
Eastern	**6.3** | 10.4	**5.5** | 8.8	**2.3** | 2.6	**1.3** | 1.7	**1.3** | 1.6	**1.6** | 1.9	**2.4** | 3.3	**12.5** | 17.6
South West	**6.9** | 5.2	**5.6** | 4.1	**2.7** | 4.1	**1.6** | 3.0	**1.6** | 2.9	**1.9** | 3.3	**2.7** | 3.5	**14.2** | 18.6
West Midlands	**8.1** | 7.9	**6.0** | 5.8	**2.7** | 4.1	**1.6** | 3.0	**1.5** | 2.9	**1.9** | 3.3	**2.7** | 3.8	**14.4** | 20.5
East Midlands	**7.2** | 9.5	**6.3** | 8.8	**2.8** | 3.6	**1.7** | 2.5	**1.6** | 2.4	**2.0** | 2.8	**2.9** | 4.0	**15.1** | 21.8
Yorkshire and Humber	**7.6** | 10.1	**6.6** | 7.2	**2.8** | 4.0	**1.7** | 2.8	**1.6** | 2.8	**2.0** | 3.2	**3.0** | 4.0	**15.6** | 21.6
North West	**8.3** | 9.1	**6.7** | 5.9	**3.2** | 5.2	**1.9** | 3.9	**1.8** | 3.9	**2.3** | 4.3	**3.2** | 4.6	**16.9** | 25.4
North East	**5.2** | 6.1	**6.1** | 7.2	**2.2** | 3.2	**1.3** | 2.3	**1.2** | 2.2	**1.5** | 2.5	**2.4** | 3.5	**12.8** | 18.5
Wales	**9.4** | 7.7	**6.3** | 4.6	**3.2** | 5.4	**1.9** | 4.1	**1.9** | 4.0	**2.3** | 4.5	**3.1** | 4.5	**16.5** | 24.7
Scotland	**10.8** | 9.6	**7.8** | 5.4	**3.9** | 6.4	**2.3** | 4.8	**2.2** | 4.8	**2.7** | 5.3	**3.8** | 5.3	**20.3** | 29.7
Northern Ireland	**9.3** | 12.5	**7.5** | 9.5	**4.0** | 4.8	**2.4** | 3.2	**2.3** | 3.1	**2.8** | 3.7	**3.8** | 4.9	**20.4** | 26.7
UK	**8.3** | 8.9	**6.4** | 6.0	**3.0** | 4.8	**1.8** | 3.6	**1.7** | 3.5	**2.1** | 3.9	**3.0** | 4.4	**15.7** | 23.7

Source: CBRE Research

Contacts

UK Research

Jennet Siebrits
Head of UK Research
jen.siebrits@cbre.com

Scott Cabot
Head of Residential Research
scott.cabot@cbre.com

Michael McGill
Associate Director, Residential Research
michael.mcgill@cbre.com

Edward Franks
Analyst, Residential Research
ed.franks@cbre.com

CBRE