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Savills World Research
UK Residential

Briefing Note
The Budget: How Help to Buy will affect the market

May 2013

Help to Buy initiatives in the 2013 Budget seek to assist home buyers, stimulate the market and boost house building. What will be their impact?

Overview

New Government measures, designed to help credit worthy buyers on and up the housing ladder, will stimulate the property market and boost house building.

The Help to Buy initiatives, which comprises of an equity loan scheme and a mortgage guarantee announced in the 2013 Budget, should have a much bigger impact on the number of property transactions and help more people to buy than previous schemes such as FirstBuy and NewBuy.

Although the Government expects the new two part initiative will help over 500,000 home buyers, Savills research estimates the move is more likely to help up to 400,000 buyers. As the equity loan part of the deal only applies to England, this figure could be higher if Welsh and Scottish versions were to be launched.

The take up will be limited by buyers' affordability constraints and lenders' take up of the initiative. For both schemes, borrowers will need to meet their chosen lender's credit and affordability checks.

Although in theory, the scheme aims to allow buyers with deposits of 5% to purchase, in practice buyers with 10% deposits will be more likely to get a favourable response from lenders. About a third of the mortgage guarantee element is likely to be diverted to homeowners remortgaging.

Equity Loan
How will it work?

From 1 April 2013, up to £3.5 billion of Equity Loans worth up to 20% of the value of a property was made available from the Homes and Communities Agency (HCA) for those buying new build homes with a minimum deposit of 5%. The scheme will run for three years in England.

Buyers will still be required to secure a mortgage worth up to 75% of the property's value. The new version is open to all buyers, not just first-time buyers, purchasing new build homes worth up to £600,000, provided the property is their only residence. Unlike FirstBuy, which required house builders to make up half of the equity loan, Help to Buy is fully funded by the Government.

This is how it breaks down:

Minimum 5% Borrower Deposit / Equity
Maximum 20% Equity Loan from the HCA secured through a second charge
Maximum 75% Mortgage from Third Party Lender secured though a first charge

For the first five years the equity loan will be interest free, after which you will pay a 'fee' of 1.75% rising annually by the increase in the Retail Price Index, plus 1%.

Key Points

Help to Buy at a glance

Property Purchases: The mortgage guarantee element of Help to Buy could facilitate up to 325,000 purchases over the next three years, assuming mortgage lenders have a moderate appetite for the scheme. This is the equivalent to an average of 110,000 purchases a year, an increase of 12% on 2012 levels.

New Build: The equity loan part of the scheme could support 75,000 sales of new build homes over the next three years. The extra demand, together with the mortgage guarantee, could increase private sector building by 30%. That said, the speed of the increase will be limited by builders' capital and physical ability to manage that growth.

First-time Buyers: Both parts of the scheme together could help 160,000 first-time buyers get on the property ladder over the next three years. This represents a 25% increase on current levels.

Price Growth: Better access to homeownership and cheaper mortgages as a result of Funding for Lending is likely to push up property values in the short to medium term. However, the scheme is likely to have a bigger impact on transactions and house building than prices. Growth will be tempered by affordability constraints and underlying economic weakness. Assuming a successful take up of the scheme we could see house prices rise by 15.3% over the next five years, rather than 11.5% as forecast.

Private Rented Sector: The scheme will not halt the growth of the private rented sector, although they may temper it. Population growth in London will continue to support high demand for rental homes. But we may see slower growth in rental demand in areas where property prices are more affordable. The private rented sector is still likely to grow at a pre-credit crunch rate of about 210,000 households a year in the next three years. This compares with a growth of around 245,000 households a year in 2011.

The loan will be repayable on sale of the property at which point the HCA will recover its equity share in the value of the property. As a backstop, the equity loan must be repaid after 25 years though early repayments of the equity loan are possible.

> "The equity loan element of Help to Buy is effectively a more generous extension of the existing FirstBuy scheme" Lucian Cook, Savills Research

What is the likely take up and impact on the market?

The equity loan element of Help to Buy is effectively a more generous extension of the existing FirstBuy scheme which was introduced in 2011. Potentially it can provide funding for 75,000 extra equity loans in England between 2013 and 2016.

The fact that it is fully funded by the Government will open up the programme to smaller developers whose balance sheets did not allow for the extra loan commitment in the past. As a result there should be more widespread take up among house builders. The £600,000 ceiling also makes it attractive in London where prices are higher.

There is also established demand for equity loans among prospective homeowners. Over 2012/13 FirstBuy is likely to have supported an estimated 14,000 sales, in addition to around 2,000 supported by NewBuy (a mortgage indemnity scheme launched in 2012). These deals have accounted for between 20% and 25% of sales among major volume house builders.

We anticipate the equity loan element of Help to Buy could build up the numbers of supported sales to more than 44,000 in 2015/16, particularly given its application beyond the first time buyer market.

On this basis we believe Help to Buy could increase levels of private sector house building by around 30% assuming that lenders are prepared to advance mortgages on the remaining 75% value of the property on competitive terms.

Mortgage Guarantee: How will it work?

From January 2014, the Government will also make £12 billion of guarantees available to lenders to encourage more lending at relatively high loan to values. Government figures suggest that this will support mortgage lending of up to £130 billion for those with deposits of between 5% and 20%. The scheme will run for three years.

Crucially, it will be available to existing homeowners as well as first-time buyers purchasing any home worth up to £600,000. It will apply to existing as well as new build stock and for re-mortgaging (where there is a change of lender) as well as house purchases. Qualifying loans will be on a capital repayment basis.

In the event of a repossession, the Government will compensate the lender for a portion of the net losses down to 80% of the purchase value of the property. Lenders will also take up 5% of the net losses above this 80% threshold. The guarantee lasts for seven years after the mortgage is originated. Lenders will also pay the Government a fee for each mortgage. Help to Buy excludes buy-to-let investors and second home buyers.

What is the likely take up?

Given that the full details of the new guarantee scheme have yet to be announced, it is difficult to assess its likely impact on the housing market and the extent to which it may stimulate demand.

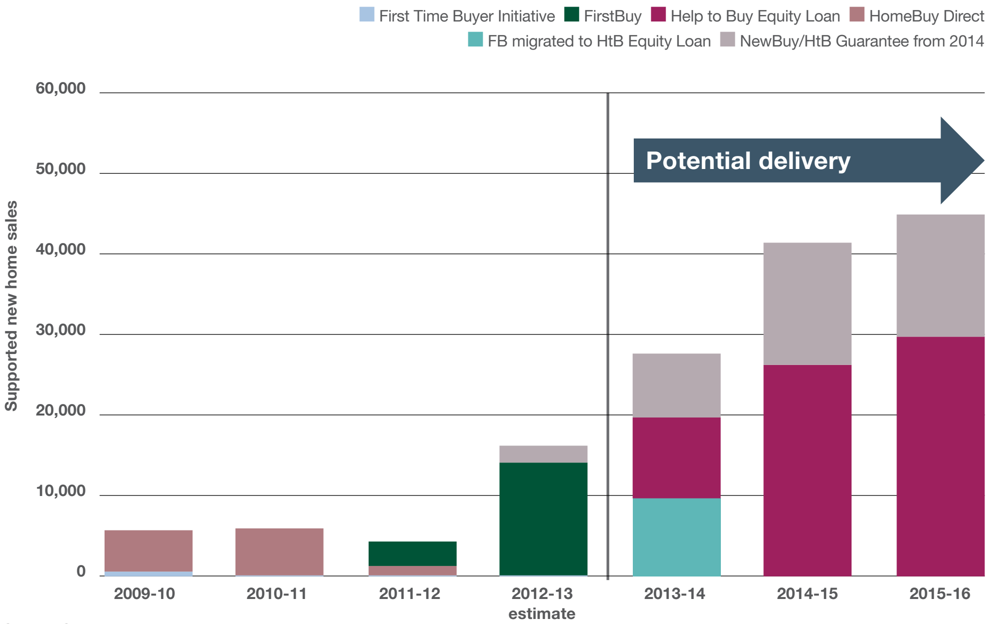
Our research indicates that, if the full £130 billion of mortgage lending is achieved the Help to Buy mortgage indemnity guaranteed could support up to 870,000 loans over a three year period from the beginning of 2014.

However, full take up is unlikely. The final number and value of new housing transactions facilitated by the scheme will be dependent on:

- Take up from lenders who will be constrained by the wholesale lending markets
- Appetite from borrowers and the mortgage rates they are offered
- Borrowers' ability to meet the conditions for the guarantee
- The extent to which the scheme is used to remortgage rather than to purchase. We think that about a third of the funds will be used to refinance existing loans.

GRAPH 1

Effect of Government schemes on house building in England



Source: Savills Research

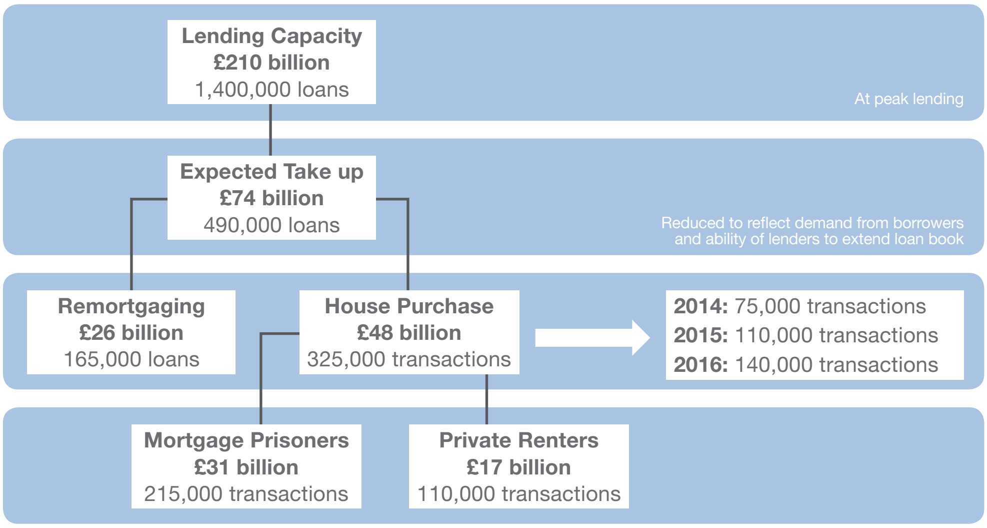
Few Help to Buy loans are likely to be at 95% loan-to-values. Judging from previous lending levels, there is much greater capacity for lending at between 80% and 90% LTV than above 90% LTV. We would also expect lenders to be more willing to lend in this band as it reduces their exposure to risk.

Homeowners who are currently unable to remortgage will be able take advantage of the scheme to refinance. Over the past four years, remortgages have accounted for 32% of all mortgage lending compared to 41% in the previous six.

We envisage lenders may favour such remortgaging over new lending for house purchase (even though it requires a change of lender) as they seek to limit their exposure to the property market. This will reduce the number of new housing transactions and in turn house building facilitated by the scheme.

GRAPH 2

Mortgage Guarantee take up



Source: Savills Research

Limits to take up:
The requirement of the Mortgage Guarantee scheme for mortgages to be on a capital repayment basis is likely to limit demand, restricting the risk of creating a price bubble. In the mortgage markets of 2004-2007, some 16% of first time buyer mortgages and 20% of home mover mortgages were on an interest-only basis. This has fallen to 1% for first time buyers and 8% for existing home movers.
It is possible that the interest rate offered by lenders will be less competitive than open market deals.

There is also a requirement for an assessment of the borrower's ability to pay the mortgage, for example by way of a loan-to-income and credit score test. This is certainly likely to constrain take up in the 90% to 95% LTV range.

The requirement that mortgages are on a capital repayment basis, is also likely to have a bearing on the affordability of home ownership for many prospective buyers and the ability to pass tests regarding their means to service a mortgage.

Impact on the market:
Taking all these constraints into account and assuming 35% of loans are accounted for by remortgaging, we estimate that a maximum of 325,000 house purchases could be facilitated by the mortgage guarantee element of Help to Buy over three years.

It is worth remembering that lenders have increased volumes under the NewBuy scheme, to a level of supported reservations consistent with around 2,000 sales per annum. It remains to be seen whether there is appetite for the much larger numbers envisaged under Help to Buy.

House Building

Given that Mortgage Guarantees will be available for the purchase of existing as well as new build purchases, we believe it could result in additional house building of approximately 12,000 units a year (beyond those unlocked by Equity Loans) within three years.

The speed of increase in house building will be limited by the capacity of the house building industry to increase output having regard to skills, capital and management. Precedents from previous periods of expansion suggest that, at best, building output could expand to about 130,000 a year within five years. Over the last 25 years building by private sector house builders has not exceeded 150,000 homes a year.

Growth in Private Renting

We do not believe that the provisions are likely to halt the growth of the private rented sector although they may temper it.

DCLG figures indicate that in the period from 2003 to 2007, during which time mortgage finance was readily available, the number of households in the private rented sector rose by 1.1 million households in the UK at an average of 217,000 households per annum. The same data indicates that the annual growth in private renting increased by closer to 245,000 households in 2011.

This reflects the fact that even prior to the credit crunch there

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> Lucian Cook, Savills Research

were issues of deposit and mortgage affordability. Though both will be eased by the proposed measures neither will be eliminated.

It is likely that lenders will still be looking for average deposits of around 10% of purchase price from those benefiting from the scheme. This would mean an average deposit £17,000 across the UK.

Accordingly, we believe that levels of private renting are still likely to grow by at least 210,000 households per annum over the next three years.

Help to Buy scenario

Increased access to home ownership, combined with a potential reduction in the cost of mortgage debt because of the continuation of Funding for Lending, is likely to result in an increase in rates of projected house price growth in the short to medium term.

However, this is likely to be limited by underlying affordability constraints and the weakness of the underlying economic recovery.

Accordingly, we have devised a Help to Buy scenario which we have compared to our adopted five year forecasts for UK mainstream house price growth (see Table 1 below).

Build to Rent

Vital to meet housing need

Of greater importance to meeting housing need in the long term is to increase the size of the Government Build to Rent scheme five-fold, taking the total amount allocated to £1 billion.

A first round of 45 projects are set to receive a share of £700 million, with a second round of bids for the remaining funds set to open later this year. The projects have the potential to deliver between 8,000 and 10,000 new homes.

The fund promises to play a key part in establishing residential property as an institutional investment asset class, providing proof of concept which we believe will lead to rapid expansion of institutional investor activity, at scale.

TABLE 1

Successful Help to Buy scenario vs five-year house price forecast

	2013	2014	2015	2016	2017	Total compound
Forecast	0.5%	1.5%	2.0%	3.5%	3.5%	11.5%
Scenario	0.5%	2.0%	3.5%	4.5%	3.5%	15.3%

Source: Savills Research

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