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First-time buyers: their changing presence in the housing market and predictions for the future

Home ownership in Britain – a quick overview

In 1920s Britain home ownership was the preserve of the few. More than 20% of households were owner-occupiers while nearly all other households rented from private landlords. But over successive decades the combination of huge structural changes in the economy, changes in government policy and a steady growth in the affluence of individuals resulted in increased home ownership as more people could afford to buy their own home and aspired to do so. By the end of the 1960s Britain had as many owner-occupiers as renters.

Right to Buy

Legislation introducing 'Right to Buy' (RTB) was passed by Margaret Thatcher's government in the Housing Act 1980. Following this, council houses were bought by their existing tenants at substantial discounts. Most such council tenants were first-time buyers (FTBs) and had until then always lived in rented accommodation. The wave of council tenants buying under the RTB scheme helped to further fuel the nation's drive towards home ownership, especially among poorer families.

According to the Office of National Statistics (ONS) the number of households in the UK that owned their own home (owner-occupiers) finally peaked at 70.9% in 2003. Since then there has been a gradual decline in owner-occupation year on year so that by 2015-16 owner occupiers represented 62.9% of the entire housing market in the UK.

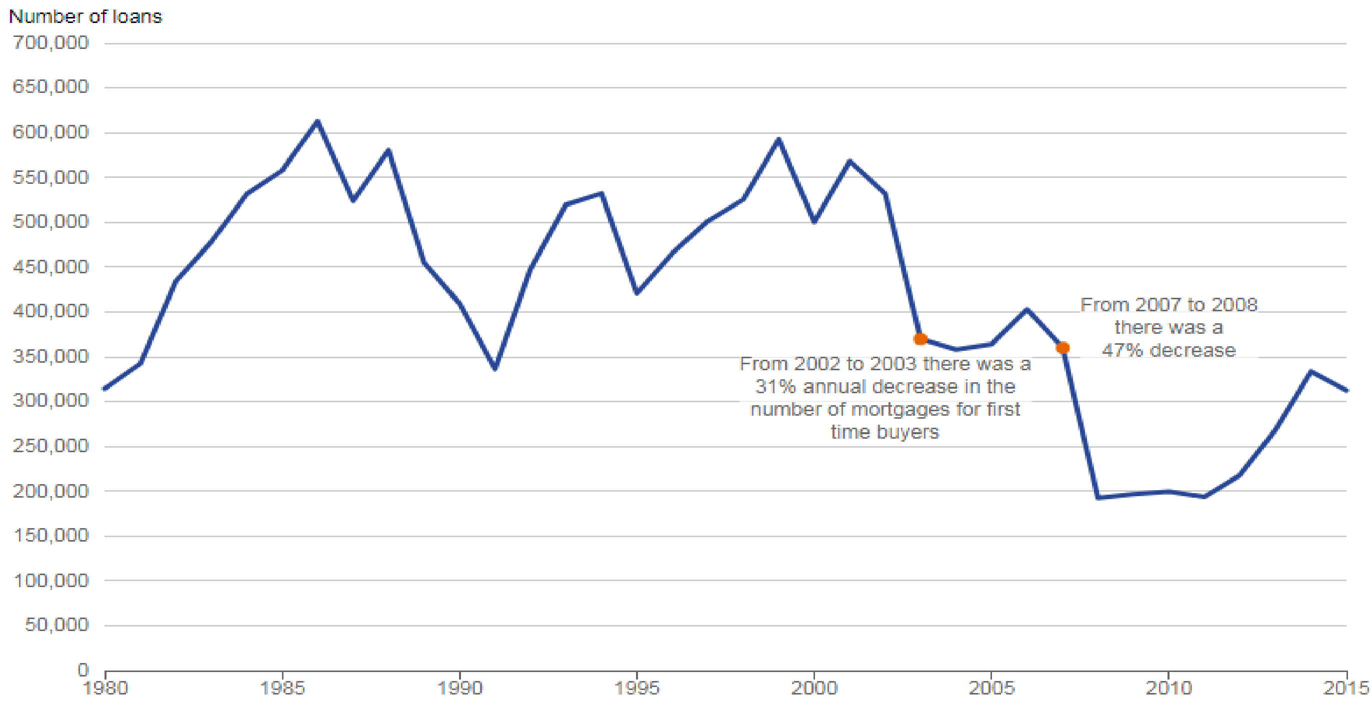
The importance of first-time buyers

FTBs play a vital role in the housing market. Whenever they enter the market by buying the homes of existing homeowner's they create 'chains'. They enable the sellers to then move another rung up the property ladder. This is because most homeowners need to sell their existing property to buy their next home. So FTBs help to bring 'liquidity' to the housing market. In addition, their presence helps stimulate the wider economy by, for example, providing work for surveyors, estate agents, conveyancers, housebuilders and tradesmen.

Clearly, the importance of FTB's to the housing market and to the nation's general economy cannot be ignored. Therefore, it is helpful to assess their role within home ownership in Britain.

Figure 1 overleaf shows the number of mortgage loans issued to FTBs each year from 1980 – 2015. The number of loans issued has experienced substantial rises and falls over this 35-year period. These peaks and troughs generally mirror major changes in both the housing market and the wider economy over that time. For example, years from the late 1980s through to the early 1990s saw a significant decline in mortgage loans issued to FTBs. Much can be attributed to the dramatic rise in house prices in 1987 (16.4%) and 1988 (25.6%) followed by the subsequent substantial increases in bank interest rates which finally peaked at 15% in October 1989 and stayed there until September 1990. The effect of these two factors served to price many FTBs out of the housing market from the late 1980s to the early 1990s, hence the fall in mortgage loans advanced to them during this period.

Figure 1: Number of mortgage loans to FTBs in the UK from 1980 – 2015



Source: Council of Mortgage Lenders

Figure 1 also shows the trend in mortgage loans to FTBs had generally been on a downward trajectory since the start of the new millenium, finally reaching an all-time low over this 35-year period of around 200,000 loans by early 2012. However, around the start of 2012 a surge in mortgage approvals for FTBs then commenced until it peaked at around 340,000 loans shortly before the end of 2014.

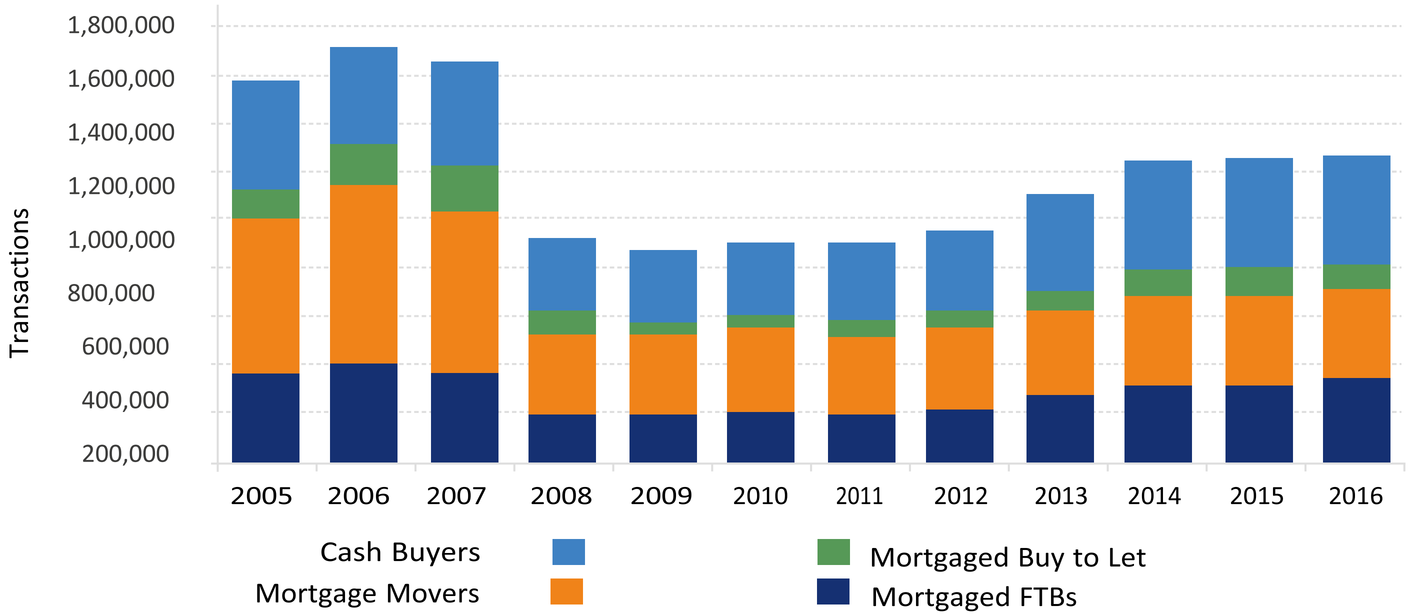
So what might have caused this recent surge? Well, part of it may be attributed simply to the cyclical nature of the residential housing market and it's endless peaks and troughs over successive years and decades. With this thought in mind, mortgage loans to FTBs plummeted in 2008 as the economy fell into a deep recession following the banking crisis. But due to the cyclical nature of the economy it was always going to come out of the recession at some point and in 2012 the first signs of recovery finally began to appear. Confidence in the economy then received a major boost when the Bank of England and HM Treasury launched the Funding for Lending scheme in July 2012. This scheme was designed to incentivise banks and building societies to boost their lending which of course included releasing loans for mortgages. The following year the Government introduced the Help To Buy scheme in April 2013 for FTBs and existing homeowners which was designed exclusively for the purchase of New Build properties. Consequently, as lenders became more willing (and able) to lend again confidence in the general economy and the housing market returned and with it a fresh wave of new FTBs entered the market, hence the surge in mortgage loans to FTBs around 2012 as illustrated in Figure 1.

FTBs as one of the four main buyer types

Figure 1 on the previous page was restricted soley to FTBs who had purchased their first home with the aid of a mortgage. However, of all property transactions undertaken each year FTBs only represent one of the four main buyer types in the housing transactions market. Consider Figure 2 below to get a clearer perspective of how FTBs fit within the market.

Of the four main buyer types, the one that has undergone the biggest change is unquestionably Mortgage Movers. At the height of the housing boom in 2006 they were by far the largest group, accounting for 43% of all UK housing transactions. However, ten years later in 2016 this share had fallen sharply to just 29%.

Figure 2: Transaction by buyer type in the UK from 2005 - 2016



Source: HMRC, CML

The most striking observation to be taken from Figure 2 is the dramatic collapse in housing transactions from 2007 to 2008. This was, of course, brought about when the housing boom abruptly ended due to the 2008 banking crisis and subsequent recession. However, beyond this it is important to consider what changes have taken place since 2008 to influence the current role of FTBs within the four buyer types.

This changed the share of housing transactions for the other three buyer types. In the case of FTBs, it meant that although there were 16% fewer FTBs in 2016 compared to 2006, their share of housing transactions saw a small rise from 24% in 2006 to 27% in 2016. Consequently, this modest rise may owe more to the collapse of the share of the market previously occupied by mortgage movers than it does to any government initiatives to help FTBs get a foot on the property ladder.

Mortgage repayment type and length of mortgage

According to UK Finance, in the UK in 2008 around 26% of mortgages for FTBs were interest-only mortgages. In London, this proportion was even higher at 45%. However, following the recession in 2008 and collapse in global stock market values the added risk presented by interest-only mortgages became very apparent and their appeal was lost among lenders and borrowers alike. Their fall in popularity was so sudden and complete that by 2012 only 2% of FTBs in the UK and 5% in London had an interest-only mortgage. In 2014 the introduction of new regulations further tightened up the rules surrounding interest-only mortgages with effect that by 2016 interest-only mortgages had become almost non-existent.

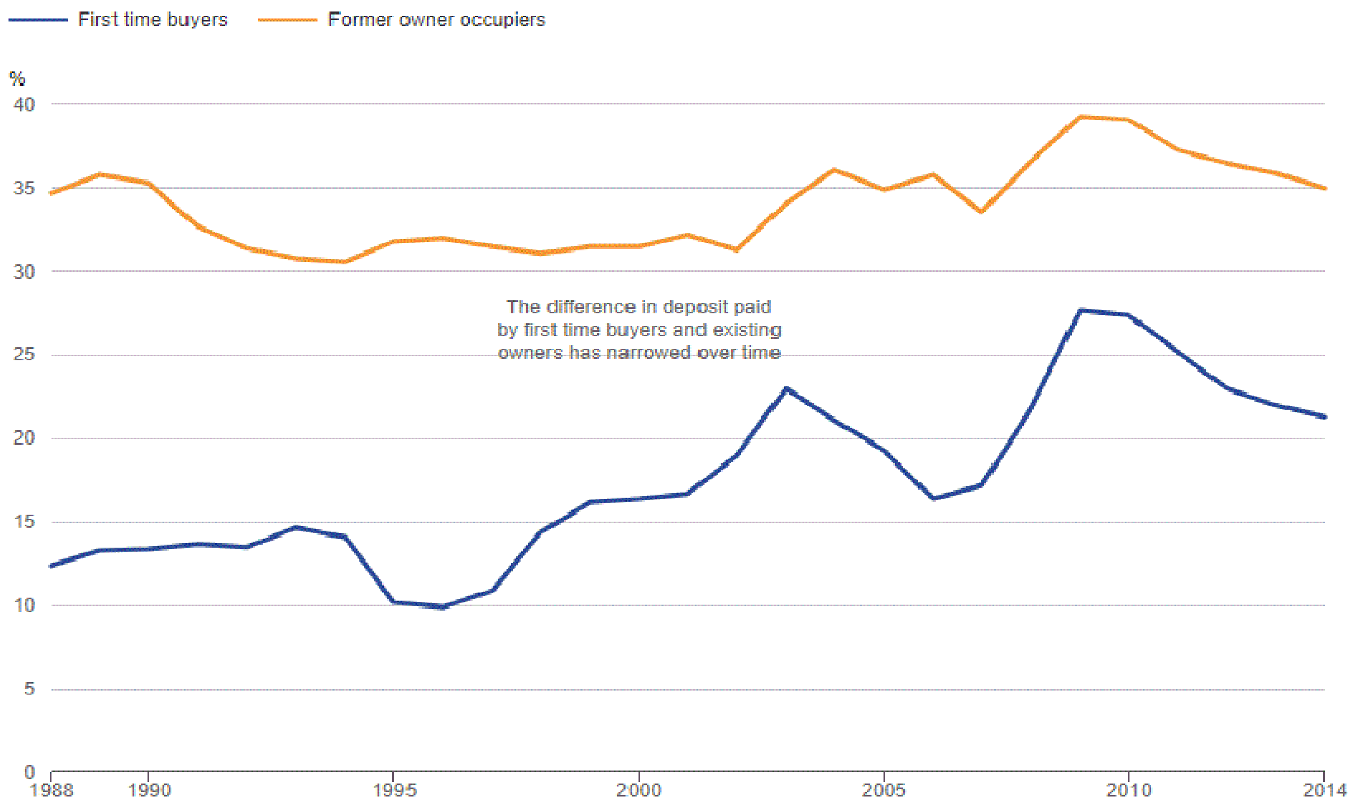
Historically, new mortgages taken out by FTBs were invariably for 20 or 25 years. However, evidence that the length of mortgage terms for FTBs are now on the increase were reported by The English Housing Survey in their Headline Report 2015-16. The report advised that 54% of FTBs in 2015-16 had taken out a mortgage of between 20 – 29 years but, more tellingly, the report also advised that 40% had taken out a mortgage of 30 years duration or more. Taking out a longer mortgage carries the disadvantage that ultimately the borrower will have to pay more money back in the form of interest to the lender. However, the advantage to the borrower is that monthly repayments will be lower. Therefore, because FTBs are now having to take on increasingly larger mortgages due to record house prices the only way many can make the monthly repayments manageable is to spread them over a longer mortgage term.

Deposits paid by UK first-time buyers as a percentage of purchase price

According to a report published by UK Finance in September 2017, the average Loan To Value (LTV) for a first-time buyer in August 2016 and August 2017 was 85.0%. Conversely, this means the average deposit provided by FTBs for these two periods was 15%. But how does this size of deposit compare with deposits over past decades?

Figure 3 overleaf provides the answer.

Figure 3: Deposit as a percentage of purchase price by buyer type in UK 1988 – 2014



Source: House Price Index – February 2016 (Table 38), ONS

Figure 3 above illustrates how the average deposits provided by FTBs have risen and fallen as a percentage of the purchase price over the 26-year period from 1988 – 2014 (blue line). Since the low point in 1996 when the average FTBs' deposit was just 9.9% of the purchase price (giving a LTV of 90.1%) the general trend was upwards until the average deposit peaked around 2009 at 27.7%. Since then it can be seen from the chart that the trend has been on a downward trajectory ever since. Furthermore, based upon statistics referred to in the aforementioned UK Finance September 2017 report we know the trend has continued to fall since 2014 so the average deposit for a FTB is now 15% of the purchase price (giving an average LTV of 85%).

The orange line in Figure 3 clearly shows that homeowners generally provide a larger deposit than FTBs. This is undoubtedly made possible by an increase of the equity in their home as a result of house price inflation during their years of ownership.

Sources of deposits for FTBs

With few exceptions, a FTB's deposit will derive from one or more of the following sources: savings, parents (the so called Bank of Mum and Dad), government schemes and lender products. Considering how vital a deposit is, it's worth providing an overview of each of these sources.

Savings

This is the obvious source for a deposit for all FTBs. The English Housing Survey, 2014-15, concluded that in the recent 20-year period from 1994-95 – 2014-15 savings continued to be the single most important source of funds for a deposit. However, with increasing numbers of young adults now living in rented accommodation (the so called 'Generation Rent') many potential FTBs will find saving for a deposit very difficult when their priority is to pay the rent each month. This will, in turn, lead them to seek other sources to fund a deposit if they are ever to become homeowners.

Parents (the Bank of Mum and Dad)

As potential FTBs find it ever more difficult to afford to buy their first home increasing numbers are now receiving money or a loan from their parents to make their dream of home ownership come true. The Social Mobility Commission, in its State of the Nation Report 2016 - Social Mobility in Great Britain, reported that 31.1% of FTBs in England received money or a loan from their parents to help them buy their first home while 9.6% used inheritance money to help them. Interestingly, the same report also showed that FTBs who received a loan from their parents could buy their first home two years earlier than their counter-parts who received no such loan. In London this time difference increased to 4.6 years.

Government schemes

Housing has always been a very political issue and in recent years governments have introduced a variety of increasingly imaginative schemes and initiatives designed to help buyers (and house builders), to encourage and assist homeownership and boost the housing market. Although these schemes are not necessarily exclusive to FTBs they are generally designed with FTBs and those with particularly limited resources in mind. Such schemes include, but are not limited to, the Help to Buy schemes, namely Help to Buy: Equity Loan, Help to Buy: Shared Ownership, Help to Buy ISA's, together with schemes such as the First Steps London scheme, Co-Ownership in Northern Ireland scheme, Right to Buy / Right to Acquire schemes and The Starter Home scheme.

Lender products

Many lenders have mortgage products designed exclusively for FTBs. But in 2017 increasing numbers of lenders began offering mortgage products to FTBs that effectively allowed them to borrow 100% of the purchase price of the property. Such products are referred to as Guarantor Mortgages. They tend to vary slightly from lender to lender. But as an example, the guarantor (typically a parent) will place a sum equal to 10% (minimum) of the purchase price of the property into a savings account with the lender. This money will be at risk if the buyer defaults on their mortgage repayments. Alternatively, the guarantor might use their own home as security, meaning the lender would have a charge on the guarantor's home and could claim money from them or repossess their home if the mortgagee (i.e. the first-time buyer) fell too far behind with mortgage repayments. By contrast, a scheme offered by some lenders allows the buyer to take out a personal loan with the lender and use this as their deposit, effectively meaning that the buyer can borrow 100% of the purchase price of the property.

The fall in the number of young homeowners and the average age of today's first-time buyer

Since the beginning of the 1990s young adults have been finding it increasingly difficult to become homeowners. The following statistics provided by the English Housing Survey 2013 – 2014 clearly support this.

Percentage of each age group that were homeowners in the UK, 1981 – 2014

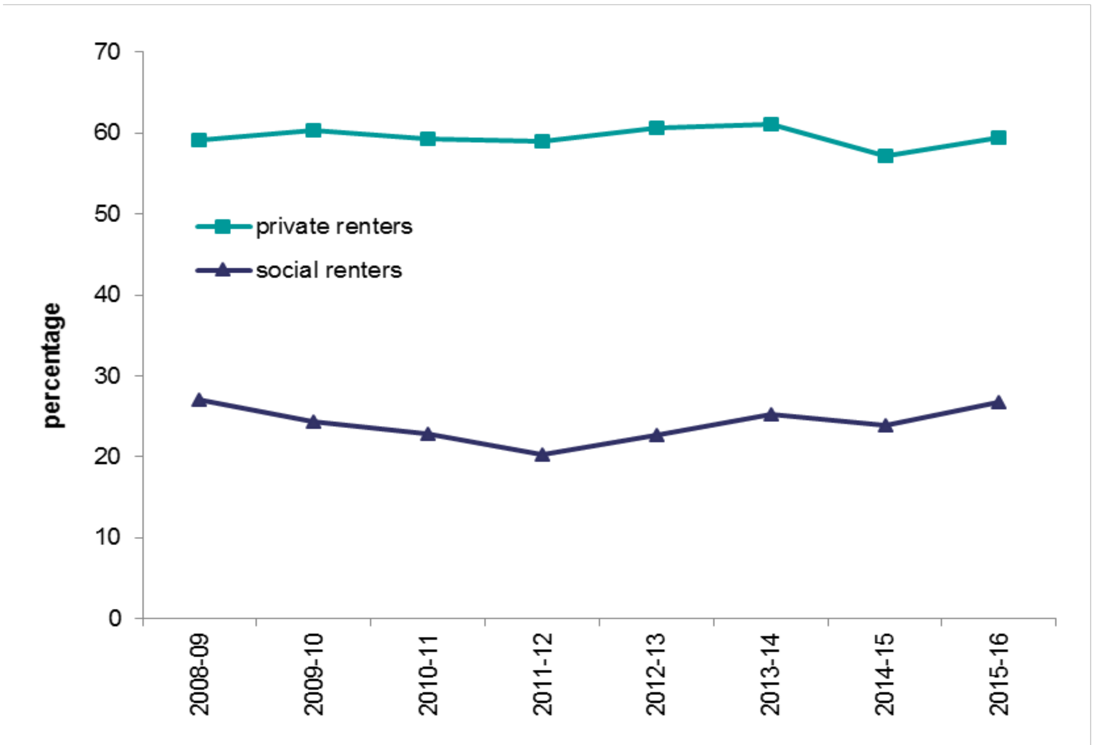
Year	16-24 yrs	25-34 yrs	35-44 yrs
1981	32.0%	62.1%	69.1%
1991	36.1%	66.5%	78.0%
2001/02	23.4%	59.6%	73.9%
2013/14	8.9%	35.8%	58.8%

From the above table we can see that from 1981 onwards the percentage of homeowners for each of the three age groups has fallen every ten years or so.

For example, in 1991 66.5% of young adults in the 25-34 age group in the UK were homeowners but this percentage had fallen sharply by 2013-14 to just 35.8%. It must therefore be assumed that far more young adults are either continuing to live with their parents or they have moved into rented accommodation because the cost of buying their own home is too great.

It will come as no surprise to learn that over recent years the average age of FTBs has risen. However, what may be surprising is that reports from various sources (UK Finance and a major high street lender) indicate the average age of a FTB has only risen by about one year since around 2005 and now stands at 30 years of age. In London the figure is 32 years of age.

Figure 4: Percentage of private and social renters who expected to buy, 2008-09 – 2015-16



Source: English Housing Survey, Headline Report 2015-16

The future home ownership aspirations of renters

Despite the difficulty of getting onto the property ladder, many people in rented accommodation still aspire to one day owning their own home. But what is particularly interesting is how the aspirations of renters vary so much depending upon whether they are private renters (renting from a private landlord) or social renters (renting from a council or Housing Association). Figure 4 on the previous page shows that for the ten year period from 2005/06 – 2015/16 a consistent figure of around 60% of private renters expected one day to be able to buy their own home. This was in stark contrast to social renters where the percentage of those who one day expected to buy their own home ranged from as little as 20.3% to a maximum of 27.1% over this same period.

Future predictions for FTBs and their impact on the housing market and associated professions and industries

We cannot predict the future with complete certainty. But based upon the facts disclosed in this report we can speculate on what possible changes we might expect for FTBs and the knock-on effect for the housing market and associated professions and industries.

- **30-year mortgages**
  Evidence suggests that the proportion of FTBs who opt for mortgages exceeding 30 years duration will continue to grow and soon become the norm.

- **The bank of Mum and Dad**
  Evidence suggests that the proportion of FTBs receiving a gift or loan from their parents to help fund their first home will increase.

- **The proportion of FTBs from wealthier families will increase while those from less well-off families will decrease**
  This is a contentious assertion, but as increasing numbers of FTBs become dependent upon their parents for funding their deposit, this will favour wealthier parents over poorer parents.

- **A rise in equity release loans**
  As more and more FTBs become reliant on funding from their parents, increasing numbers of parents who are asset rich but relatively cash poor will turn to Equity Release products to provide funding for their children’s deposit. The surveying profession and mortgage industry should expect this area of the market to provide them with increased business in the years ahead.

- **Funding initiatives**
  We should expect that lenders and successive governments will continue to develop products and schemes specifically designed for FTBs that become increasingly imaginative but also more risky.

- **Risk levels for stakeholders**
  FTBs will be seen by lenders and the surveying profession as an increasing high-risk buyer group due to their propensity for high loan to value mortgages, their reliance upon imaginative but higher risk financial products and their fondness for new build homes which by nature tend to be higher risk than second hand purchasers. These levels of risk will need to be carefully managed by lending institutions and the surveying profession.

- **Couples will become parents later in life**
  As increasing numbers of young people remain living with their parents for longer and the average age of FTBs gradually rises, many young people will delay starting a family until they can afford to buy a home of their own.

- **An increase in modern methods of construction (MMC)**
  In the drive to meet government house building targets it is likely that developers will increasingly turn towards MMC's as a way of increasing the production of new homes built while reducing construction time on site.

Feedback

This paper was produced by the Risk & Governance department of e.surv Chartered Surveyors. We aim to address the issues that matter to our corporate clients and therefore invite your feedback on this paper.

In addition, we are keen to hear about any other subject areas that are of interest to you so that we may consider covering these in future.

Please send your feedback to David Ward at david.ward@esurv.co.uk or ring 01536 535527.