Crunch point for UK property market looms

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As the UK’s 13-year property bull market comes to an end, a whole new set of conditions, assumptions and expectations are taking hold.

Will 2023 prices fall by 5%, 10%, 15% or not at all? Will the Bank of England push up base rates to (and beyond) 5%? Will lenders cut back, spooked by uncertainty and volatility?

Down valuations on the up

In 2022, a new factor has plagued property transactions: the rise of the ‘down valuation’, where a surveyor values a property below its asking price, jeopardising the sale and prompting disputes between sellers and lenders.

“As markets change, we can probably expect this difference in opinion to widen,” says John Baguely at Countrywide Surveying Services. As early as August 2022, brokers noted valuations falling as far as 20% below agreed purchase prices, leading to fraught negotiations with lenders.

“There is a gulf between the reality of what buyers are willing to pay and what surveyors are willing to let go through,” adds Jonathan Hopper of Garrington Property Finders. At the Association of Short Term Lenders, CEO Vic Jannels believes down valuations result from surveyors “taking a severe view, with one eye on the future state of the market, including rental values.”

For lenders, including bridging finance providers, the advent of down valuations poses new challenges. It narrows the options for lenders to confirm exit strategies and potentially places them at greater risk.

Risk protection

Yet for the Royal Institution of Chartered Surveyors, the issue is black and white. “Valuers have a duty to report the market value of a property,” it states. This is liable to be different from what people are willing to pay. “This is not a down-valuation, but in fact protects the lender and the buyer from risk, by ensuring the loan is advanced on the basis of a professionally derived value.”

Whatever we call it, below-market valuations may seriously disrupt the property market in the months to come, as homebuying chains break under the strain of withdrawn lending. As Sara Griffiths, lending expert at Ratio Law points out, in a falling market exits become harder to achieve, meaning that both buyers and sellers face delays and get stuck in chains. “People lack the specialist skills to deal with these situations,” she says.

This is where bridging finance could play an increasingly important role. As Stephen Clark at Finbri explains: “In 2022, the most common use of bridging finance was to overcome a property chain break, surpassing its use to buy investment property. We anticipate this will continue into 2023, as down valuations restrict homebuyers options, together with falling house prices, rising interest rates and the cost of living.”

Auctions in action

As property prices dip, demand for property auctions increases. Here again, bridging finance can play a helpful role, enabling buyers to secure purchases in competition with cash buyers. Since the pandemic, auctions are now commonly conducted online, giving greater access to the sector, along with the newfound acceptability of electronic signatures.

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“We have seen rising demand from auction buyers for bridging finance, enabling them to move at speed, with flexible terms,” adds Stephen Clark at Finbri. “Again, we expect this pattern to repeat itself through 2023, as more properties come up for auction.”

While UK interest rates began to rise in the third quarter of 2022, a total of £214.7 million in bridging loans was transacted in Q3, compared with £178.4 million in Q2 – an increase of 30%, according to the latest Bridging Trends report.

At the ASTL, Vic Jannels argues that bridging loans are at historically affordable levels. “Some brokers are offering rates below 6%, whereas the Halifax headline rate is above 6%. Bridging loans are extremely competitive at the moment,” he says.

This helps explain the rise in demand, along with shifts in the risk appetite of conventional lenders. “Borrowers who have had mortgage products withdrawn with little or no notice, or have lost their sale due to their buyers no longer fitting mortgage affordability criteria, have turned to short-term funding solutions to ensure their purchase can go through as planned,” says bridging finance expert Stephen Watts.

Unbreaking the chain

Among the causes of these disruptions are the ‘down-valuations’ noted above, together with buyers becoming more cautious, as the direction of the property market grows less predictable. Whereas 24% of bridging loans were taken out for investment property purchases in Q2, this figure fell to 16% in Q3, overtaken by customers seeking bridging finance to overcome chain breaks.

So far, there have been few reports of widespread home repossessions. Yet as thousands of fixed-rate mortgages expire, followed by sharply higher monthly payments, combined with falling house prices and an economic recession, this may once more become a feature of the UK market. Compared with previous downturns, today’s homeowners have relatively high levels of equity in their properties, making them less liable to fall into negative equity.

“The biggest worry is households on shorter-term fixed rates due to expire in the next 12 months, rolling off sub-1% mortgages that are set to jump up to somewhere around 6%,” says mortgage expert Lewis Shaw. “For an average sized mortgage loan, this could be an increase of £600 per month.”

Given the government’s willingness to subsidise pandemic-affected salaries, followed by hugely expensive energy pay-outs, some believe that money will be found to prevent widespread repossessions, especially with a General Election in prospect in 2024.

It would be brave to depend on this outcome, however, given the government’s newfound focus on budgetary responsibility and cost-cutting.

Whatever 2023 brings, it is likely to be a year of recalibration, as the 13-year property party gives way to sober reflection. Like hangovers throughout history, though, it will leave many with severe headaches, determined never to put themselves through such misery again.

Then that same evening they’ll be down the pub ordering a pint.

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