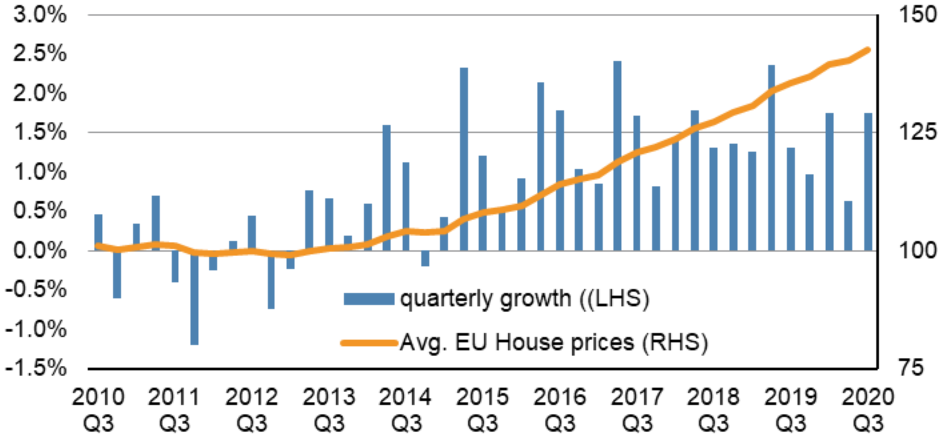
European house prices back to trend though sensitive to length and severity of pandemic

Growth in house prices across Europe is back to its long-term trend. Even countries that exhibited some slowing or even a decline during the early phase of the pandemic (e.g. UK and Sweden) are now back on track. Growth in some countries is stronger than ever before, even though many are locked down and unemployment is increasing.

The pandemic could further accelerate house price growth (or postpone a correction) as affordability for high-income consumers within the 25-65 age bracket remains high. The severity and duration of the pandemic, in particular its impact on bankruptcies and unemployment, will determine how European house prices develop in 2021.

Figure 1: Quarterly growth in European house prices

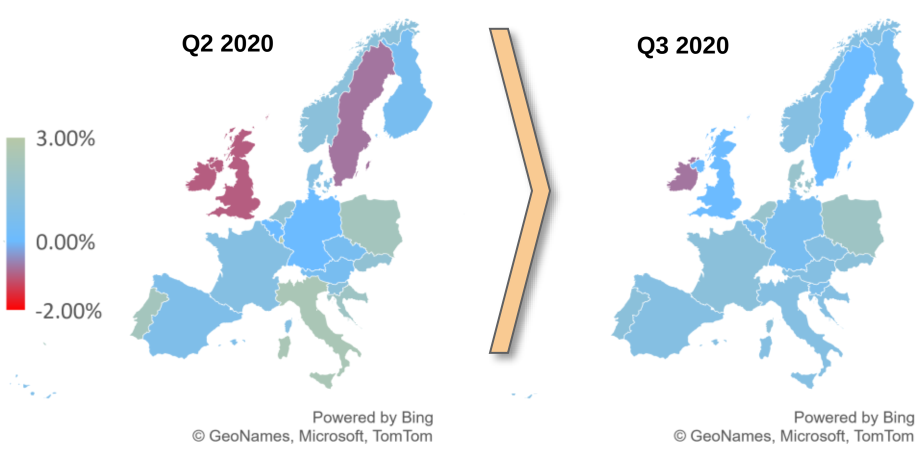


Source: Eurostat, Scope Ratings

In Q3 2020, quarterly growth of European house prices increased, averaging 1.75%. This compares to growth of 0.63% in Q2. Average growth of 1.4% for 9M 2020 is double the average growth of the last decade.

Countries that in the last quarter had decoupled from the long-term trend are now back. Only Ireland appears to remain below trend. And even in Ireland, Q3 growth was positive again for first time in three quarters.

Figure 2: European house price heat map (quarterly growth vs 10y avg)



Analysts

Mathias Pleissner
+49 69 66 77 389-39
m.pleissner@scoperatings.com

Reber Acar
+49 69 66 77 389-50
r.acar@scoperatings.com

Team leader

Karlo Fuchs
+49 69 66 77 389-78
k.fuchs.scoperatings.com

Media

Keith Mullin
k.mullin@scopegroup.com

Related Research

2021 European Covered Bond Outlook. Covid-19 as a stress test? What stress test?
January 2021

Sovereign outlook Q4 update: gradual, uneven recovery faces new virus-containment challenge
October 2020

Growth in German house prices to shift to more sustainable levels
February 2020

Scope Ratings GmbH

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389 0

Headquarters

Lennéstraße 5
10785 Berlin

Phone +49 30 27891 0
Fax +49 30 27891 100

info@scoperatings.com
www.scoperatings.com

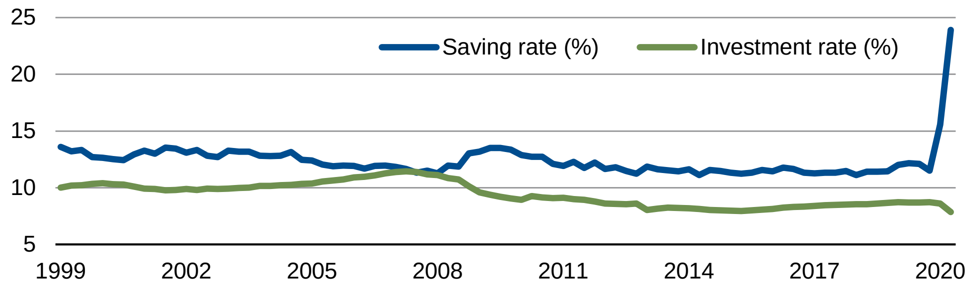
Bloomberg: RESP SCOP

House prices seem to be immune to the pandemic despite the extreme economic stress the European economy is facing.

Immunity in housing demand remains primarily driven by ultra-low interest rates. However, the pandemic may have even amplified demand. Not only because people feel a stronger benefit in owning property during forced home-office working but also because housing may have become more affordable, given savings were hitting the roof.

The average savings rate of EU households has almost doubled (+98%) and had reached 23.9% as of the second quarter 2020, which is the highest since 1999. Savings have always been around 30% higher on average than household investments. Nowadays they are three times, the level of investments.

Figure 3: EU saving and investment rate



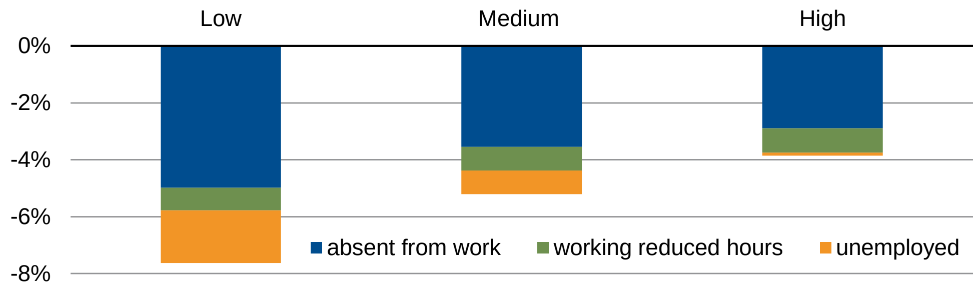
Source: Eurostat, Scope Ratings

Savings rates are sensitive to the severity of the pandemic. The more relaxed Covid-19 situation in the early parts of the third quarter of 2020 prompted a drop in savings in most European countries. Rising infection rates in Q4, further exacerbated by region or countrywide lockdowns, have again curbed the ability to spend and will have increased savings.

This cycle will continue throughout 2021 until increasing vaccination rates and herd immunity allow for a new normal, which will likely be accompanied by a prolonged spending spree in the latter part of the year.

Initially, spending will likely focus on areas postponed by the pandemic in areas such as consumer goods and travel. Once that need has been satisfied, we believe that real estate investments will then increase. In particular, people aged 25-65 with above-average income were able to increase savings and are less exposed to pandemic-related income loss (see Figure 4). For these individuals, it is most likely that additional savings will be used for asset accumulation.

Figure 4: % employment income loss by income group and transition (EU27)



Source: Eurostat

Eurostat has shown in an analysis of the “Impact of COVID-19 on employment income – advanced estimates” that it is mainly the younger generation that has borne an income loss from the pandemic.

Those experiencing the highest decreases in income due to job losses across the EU are temporary workers and those aged 16-24. The estimated income loss is more than twice as high for those in the 16-24 bracket than for aged 25-65.

This discrepancy is explained by the high number of young employees working in sectors strongly affected by Covid-19 lockdowns such as hospitality and retail.

The study also shows that high and medium wage earners are less affected by employment transition. Employees in the high-income segment tend to suffer half the income loss of those in the low-income group. This is explained by the higher likelihood of low wage earners being more affected by employment transition and not benefiting from the safety nets such as salary compensation schemes.

Future house price developments at the crossroads

House prices are driven by underlying economic conditions so are at a crossroads. While the direct effects of the pandemic may only have a short-term effect on house prices, indirect effects may alter prices longer term. If the global economy suffers more and longer than expected, this will filter through to national housing markets.

Different to short-term effects, this will also impact the high-income segment, which may not be able to accumulate assets during a lasting recession.

In our 2021 Sovereign Update published on 9 December, we forecast a recovery of 5.6% in 2021 for the Euro Area economy. However, this growth follows a severe slump of 5.9% in 2020; the sharpest global contraction of the post-World War II era.

The development of house prices will be strongly influenced by the impact of rising unemployment – likely driven by increasing bankruptcies in the corporate and SME segment. In our baseline scenario, we expect unemployment to increase by 0.9% in 2020 to 8.5% and to 9.4% in 2021.

Rising insolvencies can turn current moratoriums into lasting provisions for banks and prompt a credit contraction – which will ultimately also impact house buyers and therefore influence future house-price developments.

Prior to the pandemic, house prices in most European countries were already reaching their sustainable limits. Lasting support and looser macroprudential measures as well as the low interest-rate environment are helpful for the economy.

But they can have unintended consequences for the European housing market as they may fuel growth beyond what is sustainable. The longer the pandemic lasts, the higher the risk of regional corrections – even more so if a rapid recovery is pushed out and insolvencies and unemployment start to impact the relevant housing target groups.

European house prices back to trend though sensitive to length and severity of pandemic

Scope Ratings GmbH

Headquarters Berlin

Lennéstraße 5
D-10785 Berlin

Phone +49 30 27891 0

Frankfurt am Main

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389 0

Paris

23 Boulevard des Capucines
F-75002 Paris

Phone +33 1 8288 5557

Oslo

Karenslyst allé 53
N-0279 Oslo

Phone +47 21 62 31 42

Madrid

Edificio Torre Europa
Paseo de la Castellana 95
E-28046 Madrid

Phone +34 914 186 973

Milan

Regus Porta Venezia
Via Nino Bixio, 31
20129 Milano MI

Phone +39 02 30315 814

Scope Ratings UK Limited

111 Buckingham Palace Road
UK-London SW1W 0SR

info@scoperatings.com
www.scoperatings.com

Disclaimer